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Updates

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News Roundup

- Japanese auto major, **Honda**, through its Indian subsidiary **Honda Siel India** (HSIL), is planning to foray into the Indian boat manufacturing market and is conducting feasibility studies for the purpose. (ET)
- Tata Motors**, set to start selling the world's cheapest car **Nano** in India, unveiled a version of the hatchback for the international markets and an electric vehicle at the Geneva International Motor Show on Tuesday. The "Nano Europa" will be powered by a 3-cylinder all-aluminum gasoline engine with 5-speed automatic transmission. The car is aimed at select international markets. (ET)
- Mahindra & Mahindra** is looking at the defence sector as a strategic business interest. The \$7-billion Indian conglomerate is looking to grow this business through big-ticket global partnerships. M&M, which has already tied up with **BAE** for a land systems-specific joint venture, is reportedly talking to **Lockheed Martin**, as well as, BAE for a naval JV. (ET)
- Aurobindo Pharma** Ltd has entered into licensing and supply agreements with US pharma major, **Pfizer Inc**, for several solid dosage and sterile products. The agreements would give the Hyderabad-based company access to Pfizer's newly-formed established product business unit to exploit the sales potential for the post loss of exclusivity (LOE) products through its global commercial presence. (BL)
- Several companies have announced new projects/orders in the press: **Siemens VAI Metals Technologies** has received an order from Steel **Authority of India Ltd** (SAIL) to build an LD converter steel mill at the **Bhilai Steel Plant**. The project has an order volume of about 200 million (about Rs 1,300 crore). **Suzlon Energy** has won an order from China for supplying 100 MW of wind turbine capacity, the size of the order is estimated to be over \$100 million. **IVRCL Infrastructures and Projects Ltd** (IVRCL) has announced that the irrigation, buildings and industrial structures division (B&IS) of the company has bagged orders worth Rs670.03 crore, including a Rs 178.33-crore civil work project for **HPCL-Mittal Energy Ltd** refinery coming up in Punjab.

Source: ET = Economic Times, BS = Business Standard, FE = Financial Express, BL = Business Line.

EQUITY MARKETS

India	Change, %			
	3-Mar	1-day	1-mo	3-mo
Sensex	8,427	(2.1)	(7.9)	(3.7)
Nifty	2,622	(2.0)	(5.8)	(1.3)

Global/Regional indices

	3-Mar	1-day	1-mo	3-mo
Dow Jones	6,726	(0.6)	(16.7)	(21.7)
FTSE	3,512	(3.1)	(15.7)	(15.8)
Nikkei	7,137	(1.3)	(11.2)	(9.9)
Hang Seng	12,034	(2.3)	(7.9)	(10.9)
KOSPI	1,015	(1.1)	(15.1)	0.8

Value traded - India

	Moving avg, Rs bn		
	3-Mar	1-mo	3-mo
Cash (NSE+BSE)	99.6	107.8	77.7
Derivatives (NSE)	413.0	400.7	336
Deri. open interest	526.5	447	438

Forex/money market

	Change, basis points			
	3-Mar	1-day	1-mo	3-mo
Rs/US\$	52.0	0	324	214
10yr govt bond, %	6.0	2	18	(70)

Commodity market

	Change, %			
	3-Mar	1-day	1-mo	3-mo
Gold (US\$/OZ)	913.3	(0.3)	0.8	19.1
Silver (US\$/OZ)	12.8	(0.3)	2.0	34.6
Crude (US\$/BBL)	43.4	(1.1)	(1.8)	4.9

Net investment (US\$m)

	27-Feb	MTD	CYT
FIs	(67)	-	(1,720)
MFs	53	-	(437)

Top movers -3mo basis

Best performers	Change, %			
	3-Mar	1-day	1-mo	3-mo
Grasim Industries Lt	1,362	2.9	5.9	46.7
Mmtc Limited	13,464	(2.2)	(5.5)	39.3
Maruti Suzuki India	671	(0.5)	11.5	37.6
Gmr Infrastructure	75	(0.4)	6.6	24.2
Power Finance Corp	137	(2.7)	1.0	24.0

Worst performers

Housing Developme	71	(1.3)	(8.9)	(23.2)
Satyam Computer S	39	(2.5)	(21.7)	(83.1)
Aban Offshore Limi	287	(2.2)	(33.2)	(57.0)
Punj Lloyd Limited	70	(2.7)	(19.5)	(54.1)
Glenmark Pharmac	151	(3.7)	24.6	(52.9)

Kotak Institutional Equities Research

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Metals**HALC.BO, Rs37**

Rating	ADD
Sector coverage view	Attractive
Target Price (Rs)	55
52W High -Low (Rs)	191 - 37
Market Cap (Rs bn)	65.5

Financials

March y/e	2008	2009E	2010E
Sales (Rs bn)	600.1	692.5	475.5
Net Profit (Rs bn)	24.2	13.5	4.1
EPS (Rs)	13.8	7.7	2.4
EPS gth	(10.0)	(44.4)	(69.2)
P/E (x)	2.7	4.9	15.8
EV/EBITDA (x)	5.3	4.8	6.7
Div yield (%)	-	-	-

Pricing performance

Perf-1m	Perf-3m	Perf-6m	Perf-1y
(15.6)	(28.4)	(70.5)	(79.4)

Shareholding, December 2008

	% of Pattern Portfolio	Over/(under) weight
Promoters	36.1	-
FIs	21.1	0.4
MFs	3.2	0.3
UTI	-	(0.3)
LIC	8.8	0.3

Hindalco: Aluminium prices remain weak; capex to continue albeit at a slower pace

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- **Our sensitivity analysis suggests that Hindalco's earnings could erode at current price levels**
- **Prices continue to remain slack; inventory levels remain high**
- **Maintain ADD rating with TP of Rs55/share**

We carried out a sensitivity analysis of Hindalco's earnings to LME aluminium prices. Our analysis suggests that if current prices were to prevail throughout FY2010, Hindalco's earnings could erode completely. We met with the management of Hindalco. Key takeaways of the meeting are (1) short-term liquidity could be under pressure and (2) the company will continue with its capex plan albeit at a slower pace. Meanwhile, aluminium prices continue to remain slack. We expect prices to remain under pressure in the near term on account of lack of demand from user industries and high inventory levels.

Our sensitivity analysis suggests that Hindalco's earnings could erode at current price levels

Our sensitivity analysis for Hindalco's earnings to LME aluminium prices suggests that FY2010E earnings could erode substantially if aluminium prices were to remain at current levels throughout the year. We currently estimate FY2010E and FY2011E aluminium prices at US\$1800/ton and US\$2,200/ton, respectively. Our analysis suggests that at US\$1,300/ton, Hindalco could report a loss of Rs5.5/share. We note that currently, aluminium price is around US\$1,350 level while CY2009 average is around US\$1,421/ton.

Prices continue to remain slack; inventory levels remain high

Aluminium prices continue to remain lackluster suffering from sharp demand destruction. Besides, aluminium inventory continues to remain high. We expect that high inventory levels will prevent aluminium price recovery in the near term. Slowing economic conditions across the world and weak performance of the user industries (auto, construction) will likely result in lower demand for primary aluminium.

Pricing pressure to remain on account of poor demand from US and Europe

According to CRU, (1) US demand will likely remain poor in 1H CY09 on account of poor auto demand and slowdown in the construction segment, (2) European demand will likely remain weak on account of slowdown in construction and transport segment. However, can sheet demand continues to remain strong both in US and Europe and this could be a positive for Novelis.

Novelis—Demand weakness to continue, but margins hold up

Novelis is witnessing weak demand from its auto and construction segments due the sharply weak economic scenario, especially in North America and Europe. However, the demand from the packaging and can customers has been fairly resilient.

Key highlights from management meeting

- 1) Short-term liquidity could be under pressure on account of lower sales, of (a) lower sales on account of slowdown in economic conditions, (b) impact of declining LME on future derivative settlements resulting in cash outflows in the near term and (c) higher working capital requirements on account of customer payment delays and higher inventory.

- 2) Hindalco has indicated that it will continue to go ahead with its expansion projects as announced earlier, albeit at a slower pace. The completion of most of the projects would now be pushed forward by 6-12 months.
- 3) Debt covenants not to be triggered as Novelis as no repayment commitments in the near term. We note that Novelis has a long-term debt repayment obligation of only US\$22 mn in the next 12 months.

Valuation

We value Hindalco's domestic aluminium and copper smelting businesses at 5X FY2010E EBITDA (bottom cycle earnings) and Novelis at 0.5X adjusted price/book. We have adjusted the SPV debt of US\$1 bn taken for the acquisition of Novelis. However, we have not factored in the fact that Hindalco has a very aggressive volume expansion plan of adding 3 mtpa of alumina refining and 1 mtpa of aluminium smelting over the next three years. While earnings would continue to weaken over the next few quarter due to depressed aluminium prices at 0.5X price/book the risks appear to be priced. We maintain our ADD rating on the stock with TP of Rs55/share.

Hindalco's earnings are highly sensitive to LME prices

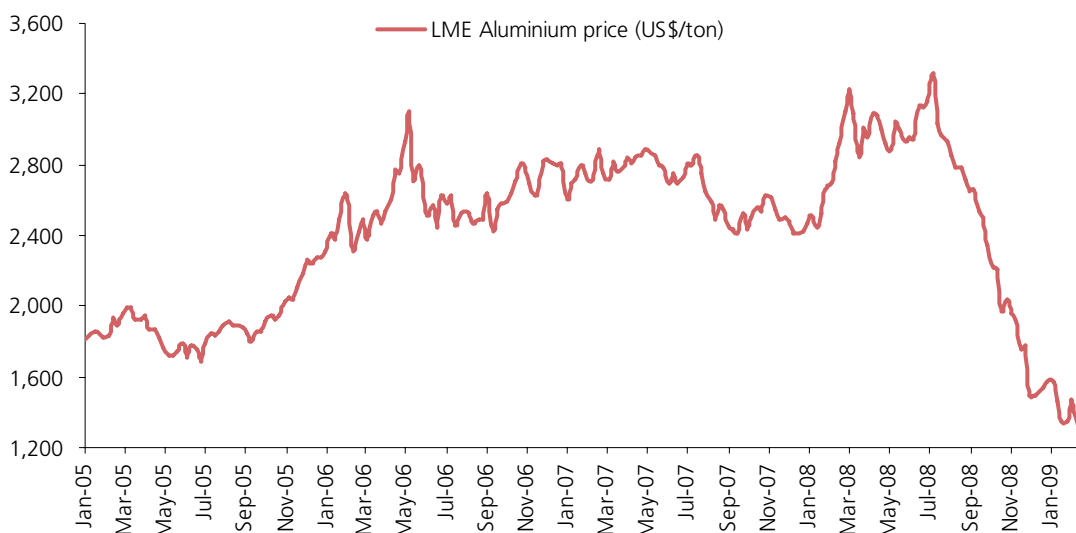
Hindalco, Sensitivity to aluminium prices, March fiscal year-ends, 2009-10E

	2010E				2011E			
	Base case	Case 1	Case 2	Case 3	Base case	Case 1	Case 2	Case 3
LME Aluminium price (US\$/ton)	1,800	1,700	1,500	1,300	2,200	2,100	1,900	1,700
Change in price (US\$/ton)		100	300	500		100	300	500
Hindalco's EPS (Rs)	2.9	0.9	(2.5)	(5.5)	8.7	6.8	3.5	0.5
% change in EPS		(67)	(187)	(293)		(22)	(60)	(94)

Source: Kotak Institutional Equities estimates

Aluminium prices have crashed from their highs on account of reduced demand from user industries

LME cash prices of aluminium, December fiscal year-ends (US\$/ton)



Source: LME, Kotak Institutional Equities.

Hindalco Ind. SOTP-based target-price, 2010E basis

	EBITDA (Rs bn)	EV/EBITDA (X)	EV (Rs bn)	Stake (%)	Attributable EV (Rs bn)	Value (Rs/share)
Hindalco Ind. (India)	25	5.0	123	100.0	123	73
ABML (a)				51.0	1	0.4
Novelis Inc. (b)						22
Total enterprise value					124	95
Less: Debt					71	41
Hindalco Ind. (India)					23	13
AV Minerals (SPV)					48	28
Resultant market capitalization						54
Target price (Rs/share)						55

Notes:

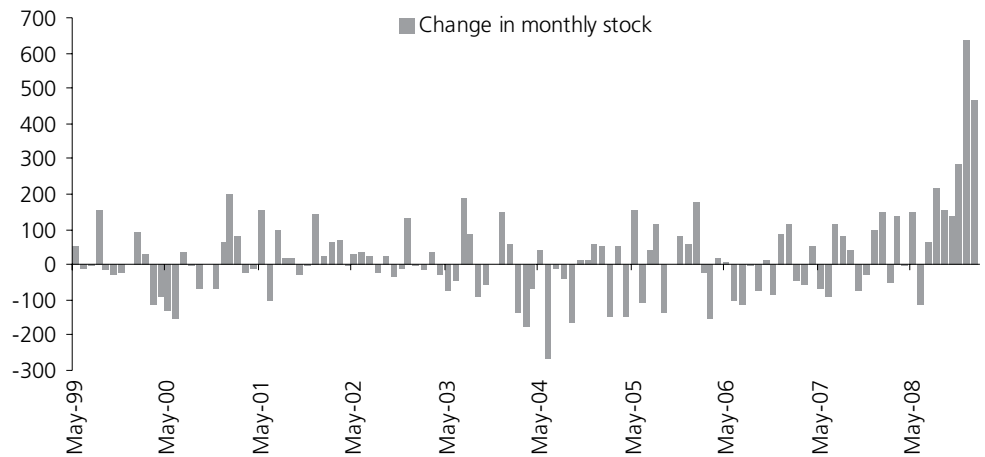
(a) Stake in ABML is valued based on market-capitalization of ABML.

(b) We have valued Novelis at 0.5X P/B given low profitability of the business

Source: Kotak Institutional Equities estimates.

Aluminium inventory has jumped to 15-year highs in the last few months

Reported change in aluminium inventory (monthly, '000 tons)



Source: CRU, Kotak Institutional Equities

Hindalco (consolidated), Profit model, balance sheet and cash flow model, March fiscal year-ends, 2007-2011E (Rs mn)

	2007	2008	2009E	2010E	2011E
Profit model (Rs mn)					
Net sales	193,161	600,128	692,547	475,484	570,537
EBITDA	44,306	66,351	61,223	41,706	53,613
Other income	4,091	6,560	5,402	5,740	5,878
Interest	(3,135)	(18,491)	(17,966)	(14,165)	(14,593)
Depreciation	(8,646)	(24,565)	(24,714)	(23,701)	(23,672)
Profit before tax	36,616	29,855	22,522	8,204	19,849
Taxes	(10,064)	(4,355)	(9,199)	(4,194)	(5,544)
Reported net income	27,030	26,238	13,323	4,011	14,306
Minority interest	(161)	(2,206)	(134)	(129)	(129)
Share in profit/(loss) of associates	(12)	(159)	1,157	1,118	1,118
Adjusted net income	26,858	23,873	14,347	5,000	15,295
Fully diluted EPS (Rs)	15.3	13.6	8.2	2.9	8.7

Balance sheet (Rs mn)					
Equity	133,653	172,819	309,785	294,595	297,931
Deferred tax liability	11,630	39,351	42,083	41,746	42,515
Total Borrowings	84,429	323,524	253,519	254,115	282,765
Current liabilities	38,459	172,180	148,595	117,362	130,617
Minority interest	8,503	16,154	16,287	16,416	16,545
Total liabilities	276,673	724,027	770,269	724,234	770,373
Net fixed assets	111,247	280,880	303,527	318,639	335,569
Goodwill on consolidation	-	88,329	88,329	88,329	88,329
Investments	78,741	140,076	142,111	135,632	135,632
Cash	10,345	17,169	15,020	18,753	23,525
Other current assets	76,340	197,573	220,824	162,422	186,860
Total assets	276,673	724,027	770,269	724,234	770,373

Free cash flow (Rs mn)					
Operating cash flow excl. working capital	39,607	46,417	50,601	36,136	46,693
Working capital changes	(5,347)	7,582	(46,834)	27,168	(11,183)
Capital expenditure	(21,905)	(27,507)	(22,647)	(15,112)	(16,930)
Free cash flow	12,354	26,493	(18,881)	48,192	18,580

Ratios					
Debt/equity (incl. goodwill on consolidation) (X)	0.6	1.6	0.8	0.8	0.9
Debt/equity (excl. goodwill on consolidation) (X)	0.6	2.7	1.0	1.1	1.2
Net debt/equity (X)	0.5	2.5	0.9	0.9	1.0
RoAE (%)	18.5	17.7	7.4	2.0	6.1
RoACE (%)	12.2	11.3	4.7	2.3	4.7

Source: Company, Kotak Institutional Equities estimates

Retail**TITN.BO, Rs720**

Rating	REDUCE
Sector coverage view	Attractive
Target Price (Rs)	830
52W High -Low (Rs)	1347 - 696
Market Cap (Rs bn)	32.0

Financials

March y/e	2008	2009E	2010E
Sales (Rs bn)	30.0	38.7	48.4
Net Profit (Rs bn)	1.6	1.9	2.2
EPS (Rs)	35.1	41.9	48.7
EPS gth	56.8	20.2	16.6
P/E (x)	20.5	17.2	14.8
EV/EBITDA (x)	14.0	10.5	8.9
Div yield (%)	1.1	1.3	1.5

Pricing performance

Perf-1m	Perf-3m	Perf-6m	Perf-1y
(10.4)	(18.1)	(42.0)	(30.8)

Shareholding, December 2008

	% of Pattern	Portfolio weight	Over/(under)
Promoters	53.1	-	-
FIs	12.2	0.1	(0.0)
MFs	5.9	0.3	0.1
UTI	-	-	(0.2)
LIC	-	-	(0.2)

Titan Industries: High gold prices hurting jewelry demand

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- **High gold price, above Rs1,500/gm, keeping customers away from stores**
- **We expect high prices and lower discretionary spend to keep jewelry demand low**
- **Cut target price to Rs830 for lower jewelry volumes, maintain REDUCE**

Our recent channel checks with jewelry stores indicate a sharp decline in jewelry demand due to high gold prices. Consumers are limiting their jewelry purchase to 'unavoidable' wedding requirements while discretionary purchases have been put on hold. Also a large part of the demand is met through the exchange of old jewelry, resulting in very low fresh purchases. We expect jewelry demand to remain low due to (1) high gold prices and (2) reducing consumer spends on discretionary products. We lower our jewelry volume growth assumption for FY2010E and FY2011E to 8% and 10%, respectively, from 10% and 12%. Titan is also extending its Fastrack brand to other products like belts, wallets and a wide range of youth-centric products. We do not include this in our estimate as the project is still at a pilot stage. We revise our EPS estimates for FY2009E, FY2010E and FY2011E to Rs41.9, Rs48.7 and Rs55.7, respectively, from Rs41.4, Rs46.5 and Rs55.8. Our EPS estimate is higher mainly on account of higher gold price and a depreciating Rupee. We cut our 12-month DCF-based target price to Rs830 on account of lower jewelry volume assumption.

High gold prices keeping consumers away from jewelry stores

We highlight that the sharp increase in gold price (13% over the past two months) and reduced consumer willingness to spend on discretionary items is hurting jewelry demand. With gold prices above Rs1,500/gm, jewelry store walk-ins have fallen significantly as consumers put on hold fresh purchases. Our channel checks with various stores across countries confirmed our apprehension of a sharp decline in jewelry demand due to high gold prices. Key observations were:-

- **Jewelry demand very low with volumes down 15-20% yoy.** Demand for gold jewelry is down almost 15-20% yoy on account of high gold prices above Rs1,500/gm. Walk-ins into stores have also reduced considerably as such high prices are forcing consumers to postpone jewelry purchases.
- **Jewelry purchase limited to most necessary requirement.** Consumers are limiting their jewelry purchase to only the most necessary requirements (mainly for wedding purposes) and discretionary purchases have all but stopped. Further, buyers are increasingly exchanging old jewelry to fund their jewelry purchases.
- **Studded jewelry still seeing some traction.** In the case of Titan, studded/diamond jewelry is largely driving volumes as the company is currently offering a discount scheme. However, store owners feel that this may also slowdown too once the offer is withdrawn.
- **Volume growth to be muted over next few months.** General feedback from stores indicates demand will be muted over the next few months if gold prices remain at current levels and macro-economic conditions do not improve.
- **Sharp decline in gold price can boost demand.** We highlight that any sharp decline in gold price can lead to a significant jump in jewelry demand as most consumers waiting on the sidelines will want to benefit from the correction in prices. A similar trend was also witnessed last year in July-Aug 2008 and October 2008, when a sudden correction in gold price led to a sharp jump in volumes.

Recent gold import data also indicate low demand

Import of gold in India has fallen almost 90% yoy over the past three months. As a bulk of gold imports in the country is for the purpose of jewelry, recent data supports reports by store owners of slowing demand. Exhibit 2 shows comparative monthly gold imports in India.

Current gold price rise different from last year—rupee depreciation the key difference

We highlight that even though the domestic gold price has reached near all time high of close to Rs1,600/gm, the international price is much below last year's peak of >US\$1,000/oz. While the international price increase is mainly on account of large demand for ETFs as a safe investment in current scenario, the domestic price has risen mainly on account of a sharp decline in the Rupee exchange rate. Exhibit 3 shows the trend in international and domestic gold price. Last year, the domestic gold price was benefitting from an appreciating Rupee, whereas currently the scenario is the opposite, hence the jump in domestic price is more than that in the international price.

Extending Fastrack brand to other youth products

Titan now plans to extend its Fastrack brand to other products like belts, wallets, fragrances, headwear etc. It has been selling sunglasses and watches under the Fastrack brand targeting the youth and plans to leverage it to diversify into other products. It will launch five pilot stores initially and then expand the network based on the results of the pilot program. These stores will be located in malls or near educational institutes, targeting the young. Break-even for these stores is expected to be much faster than for watches or jewelry stores as they will be relatively smaller (400-600 sq. ft) and will largely be focused on low value items.

Revise estimates for lower jewelry volumes and higher gold prices

We revise our EPS estimates for FY2009E, FY2010E and FY2011E to Rs41.9, Rs48.7 and Rs55.7, respectively, from Rs41.4, Rs46.5 and Rs55.8. Key changes to our assumptions are:

- Lower jewelry volume growth estimates for FY2010E and FY2011E to 8% and 10%, respectively, from 10% and 12%.
- Increase gold price (Rs/gm) assumption for FY2009E, FY2010E and FY2011E to Rs1,275, Rs1,473 and Rs1,488, respectively, from Rs1,263, Rs1,382 and Rs1,368. Our gold price assumption is raised on account of higher international gold prices and a lower exchange rate assumption.

Cut TP to Rs830, maintain REDUCE

We reduce our 12-month DCF-based target price to Rs830 (from Rs930) to factor in lower jewelry volumes across our forecast period. We maintain REDUCE on concerns of lower consumer spending on discretionary products like jewelry and watches. However, a sharp decline in the gold price could result in better-than-expected jewelry volumes. The stock is currently trading at 14.8X FY2010E EPS and appears fairly valued as we see limited upside triggers from current levels.

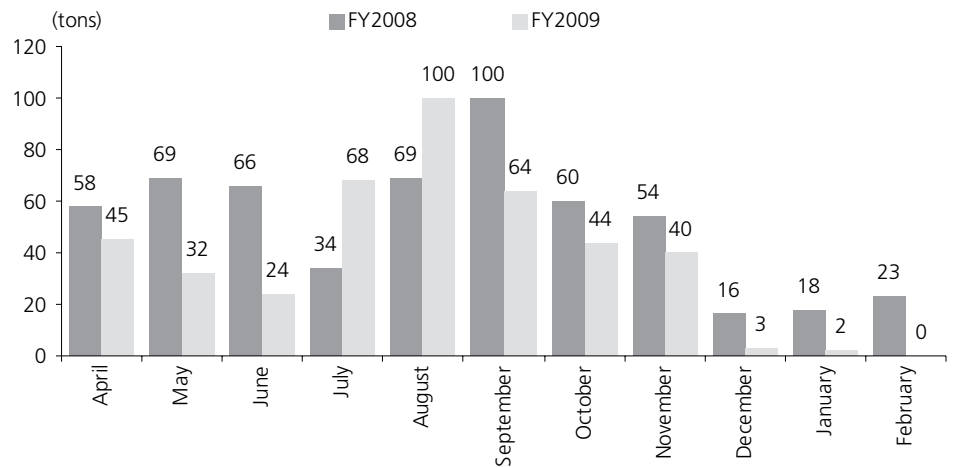
Exhibit 1: Forecasts and valuation (consolidated)

March year-end	Sales (Rs mn)	EBITDA (Rs mn)	Adj. PAT (Rs mn)	EPS (Rs)	RoAE (%)	P/E (X)	EV/EBITDA (X)
2006	14,398	1,529	812	18.6	42.2	38.9	21.7
2007	20,906	2,013	1,001	22.6	34.8	32.0	16.8
2008	29,969	2,388	1,556	35.1	37.7	20.6	14.1
2009E	38,699	3,113	1,861	41.9	34.1	17.2	10.6
2010E	48,390	3,613	2,160	48.7	30.7	14.8	9.0

Source: Company data, Kotak Institutional Equities estimates.

Exhibit 2: Gold imports in India have declined significantly in last three months

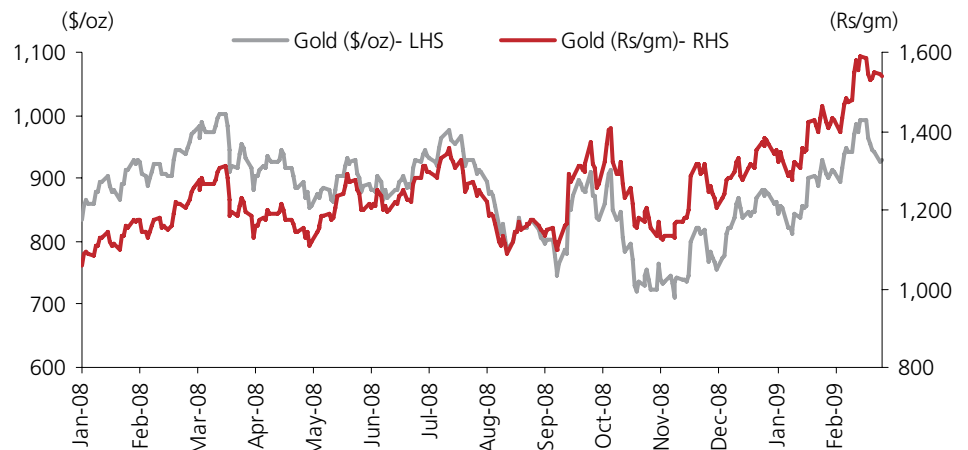
India, gold imports, March fiscal year-ends (tons)



Source: Bombay Bullion Association through news reports

Exhibit 3: Exchange rate fluctuations impact short term domestic gold prices

International and domestic gold price trends



Source: World Gold Council, Bloomberg, Kotak Institutional Equities

Exhibit 4: Titan Industries, change in estimates, March fiscal year-ends, (Rs mn)

	Revised estimates			Old estimates			Change (%)		
	2009E	2010E	2011E	2009E	2010E	2011E	2009E	2010E	2011E
Revenue	38,699	48,390	55,727	38,449	46,856	53,915	0.6	3.3	3.4
EBITDA	3,113	3,613	4,091	3,084	3,479	4,061	0.9	3.9	0.7
EBITDA margin (%)	8.0	7.5	7.3	8.0	7.4	7.5	—	—	—
Adjusted net profit	1,861	2,160	2,475	1,840	2,065	2,454	1.1	4.6	0.8
Diluted EPS (Rs)	41.9	48.7	55.7	41.4	46.5	55.3	1.1	4.6	0.8
Gold price									
(US\$/oz)	870	922	931	862	896	905	1.0	2.9	2.9
(Rs/gm)	1,275	1,473	1,488	1,263	1,382	1,368	1.0	6.6	8.8
INR/USD	45.6	49.7	49.7	45.6	48.0	47.0	—	3.6	5.7

Source: Kotak Institutional Equities estimates

Exhibit 5: Titan, Financial assumptions, March fiscal year-ends, 2006-2011E (Rs mn)

	2006	2007	2008	2009E	2010E	2011E
Jewelry						
Revenues (Rs mn)	7,896	12,903	20,252	27,584	35,294	40,288
EBITDA (Rs mn)	491	913	1,152	1,936	2,353	2,376
EBITDA margin (%)	6.2	7.1	5.7	7.0	6.7	5.9
Volumes ('000 pcs)						
Jewelry	570	720	1,139	1,367	1,476	1,624
Coins	1,427	1,925	1,017	1,169	1,286	1,415
Average realisation (Rs/pc)						
Jewelry	11,530	14,325	15,032	18,633	22,088	22,971
Coins	926	1,343	3,080	1,812	2,093	2,114
Average gold price						
US\$/oz	504	675	835	870	922	931
Rs/gm	723	969	1,081	1,275	1,473	1,488
Diamond share						
Share of diamond jewelry (%)	25	33	33	37	36	36
Watches						
Revenues (Rs mn)	6,198	7,408	8,828	9,494	10,100	11,126
EBITDA (Rs mn)	1,138	1,191	1,418	1,566	1,616	1,836
EBITDA margin (%)	18.4	16.1	16.1	16.5	16.0	16.5
Volumes ('000 pcs)						
Watches	8,336	8,964	10,286	10,836	11,136	11,950
Table clocks	272	149	125	137	151	162
Average realisation (Rs/pc)						
Watches (produced)	716	796	814	834	868	894
Table clocks	413	448	1,053	1,074	1,095	1,106
Eyewear						
Revenues (Rs mn)	129	253	406	1,118	2,377	3,588
EBITDA (Rs mn)	40	99	50	(36)	(47)	169
EBITDA margin (%)	30.7	39.2	12.2	(3.2)	(2.0)	4.7
Sunglasses						
Volume ('000 pcs)	232	380	437	503	603	724
Average realisation (Rs/pc)	558	665	711	782	861	930
Titan Eye+						
No. of stores	—	1	10	65	105	135
Annual revenue per store (Rs mn)	—	—	19	20	22	25

Source: Company, Kotak Institutional Equities estimates

Exhibit 6: Profit model, balance sheet, cash model (consolidated) for Titan Industries, 2006-2011E, March fiscal year-ends (Rs mn)

	2006	2007	2008	2009E	2010E	2011E
Profit model						
Total income	14,398	20,906	29,969	38,699	48,390	55,727
EBITDA	1,529	2,013	2,388	3,113	3,613	4,091
Interest (expense)/income	(248)	(212)	(208)	(232)	(210)	(170)
Depreciation	(200)	(260)	(333)	(316)	(338)	(360)
Other income	42	(47)	45	34	34	34
Pretax profits	1,123	1,494	1,892	2,600	3,099	3,595
Tax	(182)	(404)	(373)	(609)	(877)	(1,085)
Deferred taxation	56	27	(73)	(130)	(62)	(36)
Profit after tax	997	1,117	1,446	1,861	2,160	2,475
Associate income / (loss)	(185)	(116)	110	—	—	—
Adjusted net profit	812	1,001	1,556	1,861	2,160	2,475
Diluted earnings per share (Rs)	18.6	22.6	35.1	41.9	48.7	55.7
Balance sheet						
Total equity	1,966	3,371	4,458	5,825	7,414	9,265
Deferred taxation liability	243	181	252	382	444	480
Total borrowings	3,094	2,478	2,103	1,927	1,727	1,227
Current liabilities	3,632	5,958	9,123	9,554	11,101	12,120
Total liabilities and equity	8,934	11,988	15,936	17,688	20,685	23,092
Cash	386	510	554	1,083	1,365	2,348
Other current assets	6,042	8,402	12,481	13,571	16,174	17,558
Total fixed assets	2,007	2,717	2,877	3,011	3,123	3,163
Miscl. exp. not written off	219	42	—	—	—	—
Investments	280	316	23	23	23	23
Total assets	8,934	11,988	15,936	17,689	20,685	23,092
Free cash flow						
Operating cash flow, excl. working capital	1,186	1,544	1,742	2,272	2,526	2,836
Working capital changes	(195)	(188)	(905)	(736)	(1,135)	(416)
Capital expenditure	(431)	(983)	(509)	(450)	(450)	(400)
Investments	(79)	(265)	(213)	—	—	—
Other income	96	50	50	34	34	34
Free cash flow	577	159	165	1,121	975	2,054
Ratios (%)						
Debt/equity	140.1	69.8	44.6	31.0	22.0	12.6
Net debt/equity	122.6	55.4	32.9	13.6	4.6	(11.5)
RoAE	42.2	34.8	37.7	34.1	30.7	28.1
RoACE	19.7	20.6	26.8	27.2	26.1	25.2

Source: Company data, Kotak Institutional Equities estimates

Exhibit 7: Our DCF-based target price for Titan is Rs830

Titan, DCF-based valuation, March fiscal year-ends (Rs mn)

	2009E	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	Terminal value
EBITDA	3,113	3,613	4,091	4,710	5,425	6,250	7,021	7,646	8,186	8,765	
Tax expense	(521)	(780)	(993)	(1,420)	(1,740)	(2,022)	(2,318)	(2,499)	(2,635)	(2,816)	
Changes in working capital	(736)	(1,135)	(416)	(230)	(920)	(850)	(1,175)	(1,044)	(994)	(1,069)	
Cash flow from operations	1,856	1,698	2,681	3,060	2,766	3,379	3,527	4,104	4,558	4,881	
Capital expenditure	(450)	(450)	(400)	(350)	(350)	(350)	(350)	(350)	(350)	(350)	
Free cash flow to the firm	1,406	1,248	2,281	2,710	2,416	3,029	3,177	3,754	4,208	4,531	64,034
Discounted cash flow-now	1,393	1,089	1,754	1,836	1,442	1,592	1,472	1,532	1,513	1,435	
Discounted cash flow-1 year forward	—	1,236	1,990	2,084	1,636	1,807	1,670	1,739	1,717	1,629	
Discounted cash flow-2 year forward	—	—	2,259	2,365	1,857	2,051	1,896	1,974	1,949	1,849	
Discount rate	13.5%										
Growth from 2018 to perpetuity	6.0%										

Discount factor at WACC	0.99	0.87	0.77	0.68	0.60	0.53	0.46	0.41	0.36	0.32
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	+ 1-year	+ 2-years
Total PV of free cash flow (a)	14,274	13,941
PV of terminal value (b)	23,026	26,135
EV (a) + (b)	37,300	40,076
EV (US\$ mn)	761	818
Net debt	362	(1,121)
Equity value	36,938	41,198
No. of shares	44.4	44.4
Implied share price (Rs)	832	928
Exit EV/EBITDA multiple (X)	7.3	
Exit FCF multiple (X)	14.1	

		Sensitivity of share price to WACC and growth				
		WACC				
		12.5%	13.0%	13.5%	14.0%	14.5%
Growth Rate	4.5%	841	787	740	697	659
	5.0%	878	819	767	720	679
	5.5%	920	855	797	747	702
	6.0%	969	896	832	777	728
	6.5%	1,026	943	872	810	756
	7.0%	1,093	998	918	849	789
	7.5%	1,174	1,063	971	893	826

Source: Kotak Institutional Equities estimates

Utilities**LAIN.BO, Rs117**

Rating	BUY
Sector coverage view	Attractive
Target Price (Rs)	265
52W High -Low (Rs)	589 - 83
Market Cap (Rs bn)	26.0

Financials

March y/e	2008	2009E	2010E
Sales (Rs bn)	32.4	57.4	56.6
Net Profit (Rs bn)	3.3	3.3	3.8
EPS (Rs)	14.8	14.6	17.1
EPS <i>gth</i>	88.0	(1.5)	19.4
P/E (x)	7.9	8.0	6.8
EV/EBITDA (x)	8.0	19.1	14.8
Div yield (%)	-	-	-

Pricing performance

Perf-1m	Perf-3m	Perf-6m	Perf-1y
4.6	(8.6)	(61.8)	(71.5)

Shareholding, December 2008

	% of Pattern	Over/(under) Portfolio weight
Promoters	73.6	-
FIs	11.7	0.1 (0.0)
MFs	1.3	0.0 (0.1)
UTI	-	- (0.1)
LIC	2.4	0.1 (0.1)

Lanco Infratech: Commissioning and stable operation of Amarkantak 1 likely trigger for stock performance

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- **Power—commissioning of Amarkantak phase 1 could be the first milestone**
- **Power project portfolio building up, funding could be a constraint for new projects**
- **Construction business—strong revenue growth hints at steady execution**
- **Retain BUY rating with a revised target price of Rs265/share (Rs320/share previously)**

Lanco Infratech (LITL) has eight projects aggregating 3,956 MW currently under construction and with the addition of Rajpura (1,320 MW) in Punjab and possibly Dhopawe (1,600 MW) in Maharashtra, the project portfolio at the development stage continues to grow. We estimate LITL will be able to fund the balance equity requirement for the projects under construction. However, we are concerned about the funding of the additional projects being taken up by LITL. The Amarkantak-1 project has been delayed by almost six months and we believe the successful commissioning and smooth operations of the project are critical for LITL's stock performance. We have fine-tuned our financial model for slippage in project timelines and assume lower growth in order book buildup for construction business due to lack of visibility on financial closure of more projects. Our EPS estimates stand revised to Rs14.6 (from Rs15.2) for FY2009E and Rs17.1 (from Rs19.9) for FY2010E. We retain our BUY rating with a revised target price of Rs265/share (Rs320/share previously).

Power—commissioning of Amarkantak-phase 1 could be the first milestone

Commissioning of the first unit at Amarkantak (300 MW) has been delayed and we now assume it will start contributing to earnings from June 2009. We believe the successful commissioning of the project and stable operations is the first milestone that holds key to LITL's stock performance. This unit would be the first large power project to be commissioned by LITL using Chinese equipment. The experience with Chinese equipment in India by other developers—at Sagardighi and at Yamunanagar—has been a mixed bag so far.

We highlight other key triggers that can have a significant impact on LITL's power business:

- **Clarity on sale terms for Amarkantak-phase 1.** We assume Amarkantak-1 will sell power under the PPA's entered with PTC. If the High Court upholds the termination of the power sale arrangement with Madhya Pradesh (through PTC) or better terms are negotiated, realization of higher tariffs will be additional income for Lanco Amarkantak.
- **Signing of gas supply agreement with Reliance Industries for Kondapalli extn. project.** In the absence of a firm fuel arrangement, we continue to exclude the Kondapalli expansion project (366 MW) from our valuation. However, the project is part of the list of projects recommended for gas allocation by the empowered group of Ministers (EGoM). The project is being implemented with 100% debt funding and will likely sell power generated on a merchant basis.
- **Financial closure of Lanco Uttaranchal (150 MW) and Amarkantak 3 (660 MW).** While Lanco Uttaranchal will be a merchant power project, Amarkantak 3 will also have part merchant capacity.
- **Land acquisition for Babandh project**

Power project portfolio building up, funding could be a constraint for new projects

We estimate the cash in hand and the free cash flow generation from power projects to be sufficient to fund the balance equity investment required for the 3,956 MW of power projects currently under construction. LITL has incurred a capex of Rs65 bn (funded by debt of Rs43 bn) till December 2008 out of the total capex plan of Rs178 bn towards the development of 3,956 MW of power projects currently under construction. LITL needs to fund additional equity contribution of ~Rs11.6 bn to meet the balance equity commitments for these projects. While most projects have been funded with a debt:equity of 80:20, Lanco Kondapalli extn. (366 MW gas-based power project) is being executed with 100% debt funding and therefore does not require any equity funding. Additional cash flows from the EPC/ construction business will likely address any mismatches in the timing of cash flows.

However, LITL needs to arrange the equity financing of more projects that it plans to develop. These include:

- 1) Lanco Uttaranchal (150 MW) – hydropower project being planned as merchant power project
- 2) Amarkantak 3 and 4 (1,320 MW) – coal linkage available for 660 MW
- 3) Babandh in Orisaa (2,640 MW) – coal linkage available for 600 MW and captive coal block allocated for 1,000 MW
- 4) Rajpura in Punjab (1,320 MW) – coal linkage project won on a competitive bidding with a leveled tariff of Rs3.309/unit
- 5) Dhopawe in Maharashtra (1,600 MW) – media reports suggest Lanco is the lowest bidder for the imported-coal-based power project.

Construction business—strong revenue growth hints at steady execution

LITL's construction revenues have increased by 174% yoy during the nine-months ending December 2008 indicating sustained progress in execution of projects. The order book for the construction business, at Rs113 bn, provides good visibility (3.4X FY2009E revenues) for the next few years. However, the order book largely comprises in-house projects with about Rs91 bn order book from power projects being developed by LITL. Sustainability of the order book is therefore linked to LITL's ability to achieve financial closure of more projects (which are currently at development stage). Considering the reduced visibility in order book growth, we now value the construction business at 5X EV/EBITDA (DCF previously) in line with other engineering and construction stocks.

Real estate—adjusting pace of construction to sales

LITL is developing 3 mn sq.ft of residential space at Lanco Hills out of which about 2 mn sq. ft has been sold. Management also indicated that it has received customer advances of Rs3 bn and has sales (net of cancellations) of around 2 mn sq. ft. We note that this indicates close to 50% cancellations from initial booking levels of 4 mn sq. ft. Our valuation includes the residential projects (8 mn sq. ft) and only 1.5 mn sq. ft of under-construction commercial projects. While the residential construction does not typically require external funding for construction, we are not considering the remaining commercial and retail projects as these are capital intensive and we would value them as and when these projects are launched.

We currently model (1) decline of 10% in selling prices in FY2009E and FY2010E and (2) lower volumes under construction in the current phase as only 12 towers have been launched instead of the 15 planned earlier. After the lowering of selling prices by Lanco, we estimate sales volumes of 0.5 mn sq. ft in FY2010E and 0.4 mn sq. ft in FY2011E. We assign a value of Rs23/share based on NAV of the residential projects and under-construction commercial projects.

Retain BUY with a revised target price of Rs265/share (Rs320/share previously).

Our SOTP-based value of Rs265/share includes—(1) DCF-equity of power project portfolio at Rs150/share, (2) construction business valued at 5X EBITDA on FY2010E at Rs80/share, (3) NAV of the residential/commercial currently under construction at Lanco Hills in Hyderabad ~Rs23/share, (4) DCF-equity of BOT road projects under construction at Rs5/share and (5) value from sale of carbon credits (Rs8/share).

Change in estimates for Lanco Infratech (consolidated), March fiscal year-ends (Rs mn)

	Revenues			EBITDA			Net profit		
	New	Old	% Chg.	New	Old	% Chg.	New	Old	% Chg.
2009E	57,437	57,539	(0.2)	7,813	7,539	3.6	3,254	3,382	(3.8)
2010E	56,566	67,554	(16.3)	11,839	13,737	(13.8)	3,797	4,427	(14.2)

Source: Kotak Institutional Equities estimates.

Segmental breakup of LITL financials (Rs mn)

	2007	2008	2009E	2010E	2011E	2012E
Revenue flows						
Power	10,990	17,501	28,568	28,575	51,156	74,073
Construction	5,417	15,745	32,694	35,266	40,888	41,468
Real estate	—	1,039	1,732	1,542	3,220	5,649
Less inter-segmental	(349)	(1,873)	(5,558)	(8,816)	(6,951)	(7,050)
Total	16,058	32,413	57,437	56,566	88,313	114,140
EBITDA flows						
Power	3,216	3,706	3,300	7,035	17,487	28,015
Construction	1,141	3,141	4,152	4,479	4,579	3,815
Real estate	-	341	514	331	949	1,911
Less inter-segmental	(52)	(281)	(706)	(1,120)	(779)	(649)
Total	4,305	6,907	7,260	10,725	22,237	33,093
Attributable EBITDA	3,056	5,576	6,499	9,428	19,904	30,421
Net profit						
Power	1,454	2,260	1,566	3,151	5,525	7,430
Minority interest	(576)	(939)	(636)	(1,019)	(1,261)	(1,214)
Attributable PAT from Power	877	1,321	929	2,133	4,264	6,215
Construction	732	2,002	1,952	1,914	1,748	1,315
Less inter-segmental	(52)	(281)	(332)	(479)	(297)	(224)
Attributable PAT from Construction	679	1,721	1,620	1,436	1,450	1,091
Real estate	-	218	288	59	452	517
Minority interest	-	(57)	(75)	(15)	(117)	(134)
Attributable PAT from Real Estate	-	161	213	44	334	383
Attributable profit	1,557	3,203	2,763	3,612	6,048	7,689
EPS (Rs)						
Power	3.9	5.9	4.2	9.6	19.2	28.0
Construction	3.1	7.7	7.3	6.5	6.5	4.9
Real estate	-	0.7	1.0	0.2	1.5	1.7
Total	7.0	14.4	12.4	16.2	27.2	34.6
EPS differential due to accounting for depreciation	1.5	0.4	2.2	0.8	(4.9)	(0.6)
Reported EPS	8.5	14.8	14.6	17.1	22.3	34.0
Attributable net debt						
Total	9,440	25,930	53,853	106,124	123,429	114,934

Note: The equity holdings have been consolidated under LITL from FY2007. We have assumed similar holding structure for past financials for the purpose of comparison.

Source: Company data, Kotak Institutional Equities estimates

Lanco: Profit model, balance sheet, cash model 2006-2011E, March fiscal year-ends (Rs mn)

	2006	2007	2008	2009E	2010E	2011E
Profit model (Rs mn)						
Net sales	1,471	16,058	32,413	57,437	56,566	88,313
EBITDA	167	4,198	6,993	7,260	10,725	22,237
Other income	13	416	708	552	1,114	604
Interest	(36)	(829)	(920)	(1,573)	(3,672)	(8,481)
Depreciation	(19)	(656)	(776)	(1,120)	(1,633)	(5,932)
Pretax profits	125	3,130	6,005	5,119	6,533	8,428
Tax	(33)	(471)	(1,404)	(1,154)	(1,378)	(1,974)
Minority Interest	79	(778)	(1,304)	(711)	(1,358)	(1,496)
Net profits	171	1,880	3,542	3,254	3,797	4,958
Extraordinary items	(0)	(1)	245	—	—	—
Earnings per share (Rs)	5.5	8.5	15.9	14.6	17.1	22.3
Balance sheet (Rs mn)						
Total equity	954	15,105	18,333	21,919	26,195	31,450
Deferred taxation liability	31	92	173	186	386	2,912
Total borrowings	1,495	20,821	37,200	84,634	131,059	150,073
Current liabilities	1,581	11,424	27,038	28,536	30,477	36,054
Minority Interest	41	41	41	41	41	42
Total liabilities and equity	4,101	47,482	82,785	135,316	188,157	220,531
Cash	414	5,050	7,411	18,758	12,145	13,868
Current assets (excl cash)	2,264	12,013	30,379	32,162	35,013	48,256
Total fixed assets	409	24,390	38,029	83,590	140,195	157,603
Investments	1,015	6,029	6,966	804	803	803
Deferred Expenditure	—	—	—	1	1	1
Total assets	4,101	47,482	82,785	135,316	188,157	220,531
Free cash flow (Rs mn)						
Operating cash flow, excl. working capital	120	3,739	5,632	5,930	9,482	19,024
Working capital	(230)	95	(2,752)	(285)	(910)	(7,666)
Capital expenditure	(211)	(24,637)	(14,415)	(46,681)	(58,238)	(23,340)
Investments	(419)	(5,014)	(936)	6,161	1	—
Free cash flow	(740)	(25,817)	(12,472)	(34,876)	(49,665)	(11,982)

Source: Kotak Institutional Equities estimates

SOTP value of Rs/share

	Capacity (MW)		Est. CoD	Equity value	Equity Inv.		Attributable value	
	Gross	Attributable		(Rs mn)	(Rs mn)	P/BV (X)	(%)	(Rs mn)
Operating power plants								
Lanco Kondapalli	368	217		7,401	3,400	2.2	59	4,366
Aban Power	120	61		2,155	1,318	1.6	51	1,100
Lanco Electric Utility (Power trading)				327	212	1.5	100	327
Power plants under construction								
Lanco Amarkantak	600	456	Jun-09/Jan-10	10,071	5,598	1.8	76	7,654
Lanco Green	70	63	Mar-10	1,126	840	1.3	90	1,014
Vamshi Hydro	10	9	Mar-09	166	153	1.1	91	152
Vamshi Industrial	10	9	Jul-09	193	153	1.3	91	175
Nagarjuna Power	1,200	1,200	Apr-10/Sep-10	13,917	9,600	1.4	100	13,917
Lanco Energy - Teesta VI	500	370	Sep-12	6,963	5,900	1.2	74	5,153
Anpara 'C'	1,200	1,200	Mar-11/Jun-11	10,067	8,800	1.1	100	10,067
Lanco Kondapalli extn. (366 MW)	366	216	Dec-09				59	
Power projects being sold								
Clarion Power	12	12					98	345
Rithwik Power	6	6					94	152
Sub total	4,444	3,801		52,387	35,974	1.5		44,420
Net equity funding requirement								(13,576)
Power (A)								30,845
Construction (B)								18,407
Property development (C)								5,117
Road projects (D)								1,006
Carbon credits (E)								1,702
Grand total (A+B+C+D+E)								57,077

Source: Kotak Institutional Equities estimates

Lanco largely funded for the set of power projects

Cashflow position of Lanco's power portfolio (Rs mn)

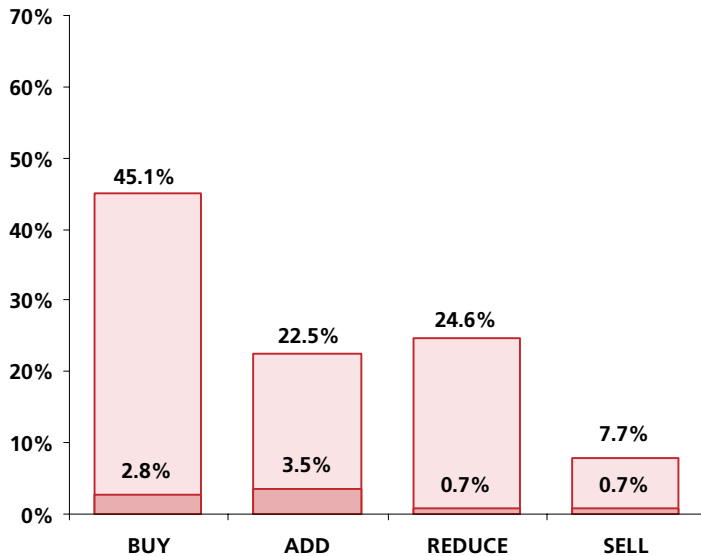
	2009E	2010E	2011E	2012E	2013E
FCFE-outflows					
Lanco Amarkantak I	734				
Lanco Amarkantak II	734	188			
Lanco Green	288	190			
Vamshi Hydro	62				
Vamshi Industrial	14	32			
Nagarjuna Power	79	5600	1800		
Lanco Energy - Teesta VI	699	1564	877	877	871
Lanco Hydro (Uttaranchal)	40	480	526	619	
Anpara C	1350	4288	2184		
Projects under construction	4000	12342	5386	1496	871
FCFE-inflows					
Lanco Kondapalli	242	831	976	1,029	598
Aban Power	192	190	179	174	166
Clarion Power	112	70	85	100	137
Rithwik Power	35	39	48	59	54
Projects under operation	581	1,131	1,288	1,362	955
Lanco Amarkantak I	—	479	41	385	392
Lanco Amarkantak II		220	316	383	388
Lanco Green		17	82	89	96
Vamshi Hydro		29	(26)	(20)	(15)
Vamshi Industrial			24	(32)	(27)
Nagarjuna Power			1,766	1,547	1,970
Anpara C			433	1,947	1,781
Lanco Hydro Energy - Uttaranchal				43	153
Teesta					593
Projects under construction	—	745	2,637	4,342	5,331
Lanco Kondapalli extn.	—	646	1,547	1,110	447
FCFE from power	581	1,876	3,924	5,704	6,286
Net FCFE	(3,419)	(10,466)	(1,462)	4,208	5,415
Existing cash + cumulative FCFE	2,296	(8,170)	(9,631)	(5,424)	(8)

Source: Kotak Institutional Equities estimates

" Each of the analysts named below hereby certifies that, with respect to each subject company and its securities for which the analyst is responsible in this report, (1) all of the views expressed in this report accurately reflect his or her personal views about the subject companies and securities, and (2) no part of his or her compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in this report: Rahul Jain, Augustya Somani, Aman Batra."

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- Percentage of companies covered by Kotak Institutional Equities, within the specified category.
- Percentage of companies within each category for which Kotak Institutional Equities and or its affiliates has provided investment banking services within the previous 12 months.

* The above categories are defined as follows: Buy = We expect this stock to outperform the BSE Sensex by 10% over the next 12 months; Add = We expect this stock to outperform the BSE Sensex by 0-10% over the next 12 months; Reduce = We expect this stock to underperform the BSE Sensex by 0-10% over the next 12 months; Sell = We expect this stock to underperform the BSE Sensex by more than 10% over the next 12 months. These ratings are used illustratively to comply with applicable regulations. As of 31/12/2008 Kotak Institutional Equities Investment Research had investment ratings on 142 equity securities.

Source: Kotak Institutional Equities

As of December 31, 2008

Ratings and other definitions/identifiers

Rating system

Definitions of ratings

- BUY.** We expect this stock to outperform the BSE Sensex by 10% over the next 12 months.
- ADD.** We expect this stock to outperform the BSE Sensex by 0-10% over the next 12 months.
- REDUCE:** We expect this stock to underperform the BSE Sensex by 0-10% over the next 12 months.
- SELL:** We expect this stock to underperform the BSE Sensex by more than 10% over the next 12 months.

Our target price are also on 12-month horizon basis.

Other definitions

Coverage view. The coverage view represents each analyst's overall fundamental outlook on the Sector. The coverage view will consist of one of the following designations: Attractive (A), Neutral (N), Cautious (C).

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