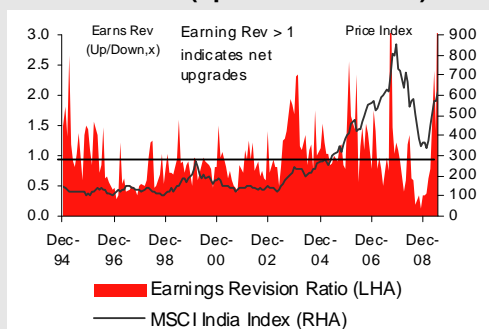


INDIA

# Microstrategy

3 August 2009

## MSCI India – index and earnings revisions ratio (up / down revision)



Source: Bloomberg, Macquarie Research, August 2009

### Microstrategy top picks

Code	Name	Industry	M cap (US\$m)
BOI IN	Bank of India	Banks	3,874
HZ IN	Hindustan Zinc Ltd.	Div Metals	5,975
RCOM IN	Reliance Comm	Wireless	11,703
ACEM IN	Ambuja Cements L	Cement	3,047
POWF IN	Power Finance Corp.	Div Fin	5,209
JSP IN	Jindal Steel & Power	Steel	9,341
RIL IN	Reliance Industries L	DnStm O&G	66,208
WPRO IN	Wipro Ltd.	Software	13,802
UT IN	Unitech Ltd.	Real Estate	4,162
CRG IN	Crompton Greaves	Indust'l Equip	2,220

Source: Macquarie Research, August 2009

### Microstrategy bottom picks

Code	Name	Industry	M cap (US\$m)
GMRI IN	GMR Infrastructure	Const & Engg	5,316
IBREL IN	Indiabulls Real Est	Real Estate	1,900
ABB IN	ABB Ltd. (India)	Industrial Equip	3,141
SIEM IN	Siemens India Ltd.	Conglomo	3,282
HDFC IN	HDFC Ltd	Banks	14,401
TTAN IN	Titan Industries Ltd.	Textile/Apparels	1,201
DABUR IN	Dabur India Ltd.	HPC	2,379
CAIR IN	Cairn India Ltd.	Upstream O&G	9,350
IDEA IN	Idea Cellular Ltd.	Wireless	4,978
HDFCB IN	HDFC Bank Ltd.	Banks	12,806

Source: Macquarie Research, August 2009

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## Fundamental support for valuations

### Event

- Emerging market equities, including India, have been a big beneficiary of the improving global macro environment and continued easy money policy of central banks around the world. The recent India June 1Q10 quarterly reporting season highlights some recovery in company fundamentals.

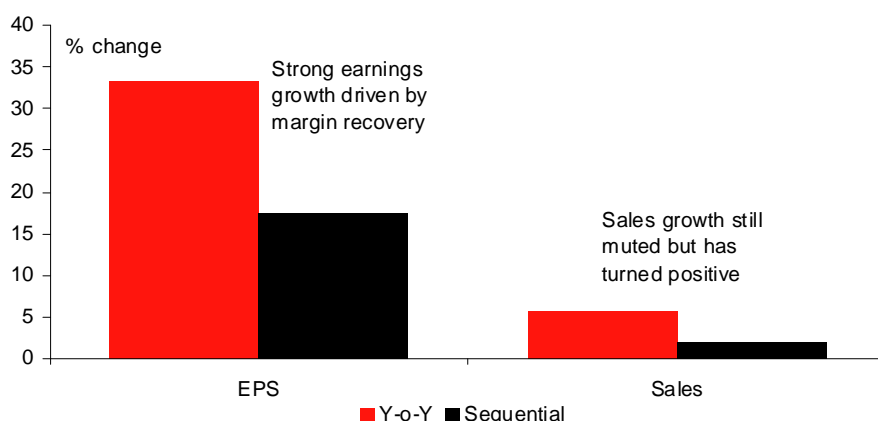
### Impact

- The June 1Q10 quarterly reporting season has provided some relief to stretched valuations for the Indian market.** Our analysis shows quarterly earnings of large-cap companies in India grew YoY and sequentially by 33% and 17%, respectively. More important, over 50% of the companies had better earnings on a sequential QoQ basis.
- EBITDA margin recovery remains the key driver of this earnings growth,** as sales revenue only barely registered positive sequential quarterly growth, although more than 50% of companies still had better sales than in the March 2009 quarter.
- Higher operating leverage due to higher margins could lead to even better earnings growth** once the top-line growth also picks up, particularly for capital goods, telecoms, software and banks.
- At the stock level we find the improved macro environment is driving earnings upgrades across all sectors, except property.** Companies with the worst EPSg forecast for FY10/11 performed the best last month, while those stocks with the highest FY10/11 PER performed the worst.

### Outlook

- In the short term, we favour stocks with the lowest forecast EPS growth,** in the hope of subsequent positive earnings revisions driving performance. We would avoid stocks with extremely high forward PERs, as positive earnings revisions seem to have already been factored in for such stocks.

### India large-cap universe – June 1Q10 quarter EPS and sales growth



Source: Bloomberg, Macquarie Research, August 2009

Please refer to the important disclosures and analyst certification on inside back cover of this document, or on our website [www.macquarie.com.au/research/disclosures](http://www.macquarie.com.au/research/disclosures).

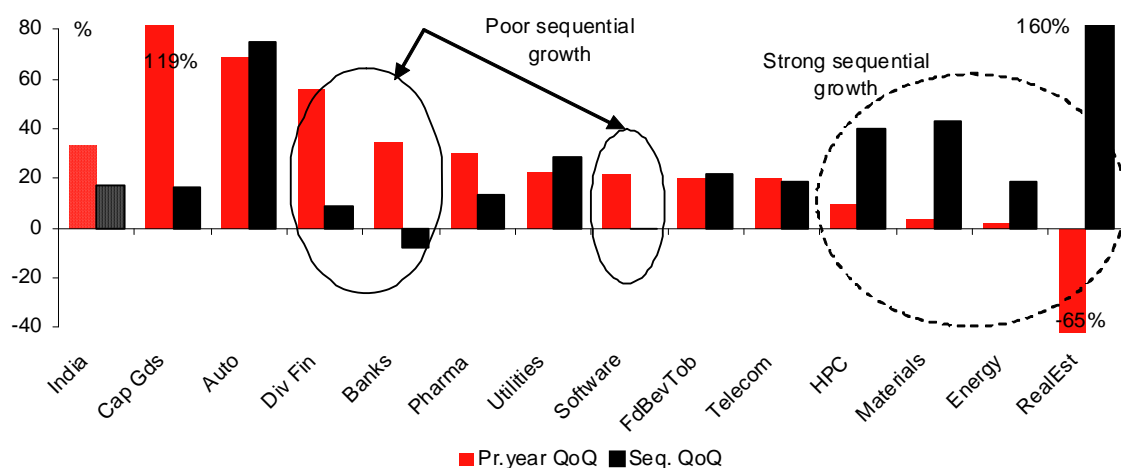
### Quarterly results reinforce a quick reversal of fortunes

We believe the positive, if not stellar, results provide definite support to current valuations, as investors would not be unhappy paying 16x forward earnings if the EPS growth is more than 20% for FY10/FY11. We have been highlighting the current reporting season as critical for the Indian market, because positive results would provide support to the market that has been trading close to the upper range of the forward PER band of 16x.

We tracked the results of over 600 Indian companies (parent level) for this reporting season. More than 80% of the 140 large-cap companies (market cap > US\$1bn) have reported so far, and the weighted quarterly EPS growth was +33% and +17% on a YoY and sequential basis, respectively.

Almost all the sectors, except property, saw YoY quarterly growth, with the strongest growth registered for capital goods, autos, diversified financials and banks. The other positive aspect of this reporting season has been the strong sequential EPS growth posted by cyclical sectors such as materials, energy and property. This is perhaps the most crucial evidence that the cycle is turning around, and the earnings scenario gets better from here. On the negative side, some of the sectors, especially software and financials, still registered poor sequential growth.

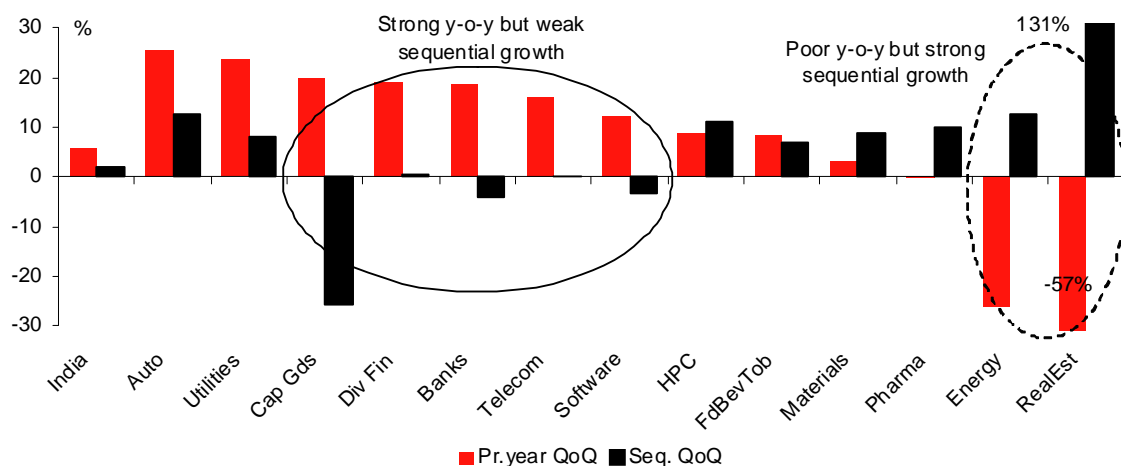
**Fig 1 Positive YoY and sequential quarterly EPS growth for June 1Q10 quarter**



Note: Data shows only large-cap companies that have reported on a market cap-weighted and free float-adjusted basis. Source: Bloomberg, Macquarie Research, August 2009

Further analysis highlights significant improvement in EBITDA margin has underpinned this strong result. Sales growth is still muted for most of the sectors on a sequential as well as YoY basis, but the cyclical sectors witnessed strong sequential growth in sales.

**Fig 2 Sales growth for June 1Q10 quarter remains muted**



Note: Data shows only large-cap companies that have reported on a market cap-weighted and free float-adjusted basis. Source: Bloomberg, Macquarie Research, August 2009

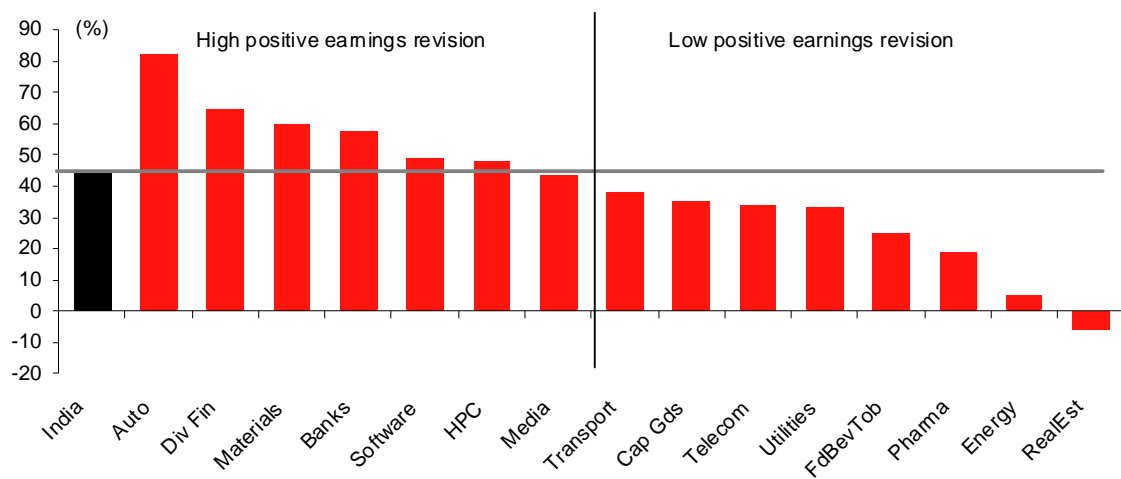
### Earnings revisions remain positive

**Strong earnings revisions last month underpinned by strong quarterly results:** We analyse the earnings revisions for the broader large-cap universe in India. Net earnings revisions, defined as net positive revisions divided by total revisions, was close to 45%, implying 2.6 positive revisions for every 1 negative revision. This trend of strong positive earning revisions during the last four months continues to be a big support factor for the overall market.

The current reporting season also provides much clearer insight into the future performance of companies. The higher margins are clearly sustainable for some time until the WPI (wholesale price index) catches up with the CPI (consumer price index). If sales growth continues to recover on a sequential basis, it will be very positive for sequential EPS growth, on account of higher operating leverage.

**From an earnings-revisions perspective, we prefer cyclical sectors such as real estate, energy and capital goods, which did not see very strong earnings revisions last month.** The reason behind these choices is the assumption that with the improved macro environment, almost all the sectors (especially the cyclicals) will see positive earnings revisions sooner or later.

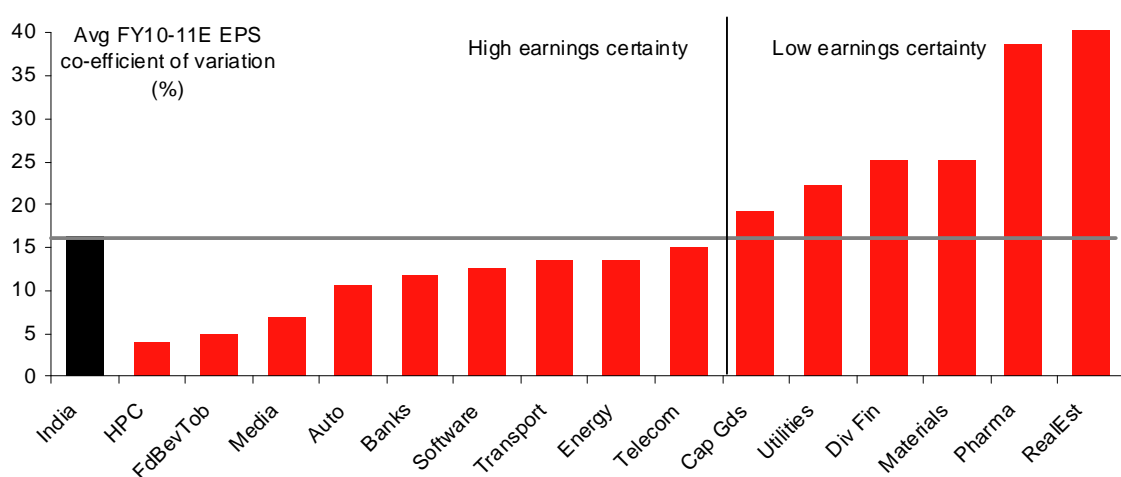
**Fig 3 Further upside for sectors that have not yet seen strong earnings revisions**



Note: Data shows only large-cap companies.  
 Source: FactSet, Macquarie Research, August 2009

**Earnings certainty also remains good for the broader large-cap universe,** at just over 15% average FY10/11 coefficient of variation for EPS estimates. Even here we prefer sectors with lower certainty, especially cyclical sectors such as capital goods, materials and property, because it indicates that at least some analysts expect much better results than the consensus.

**Fig 4 Further earnings upside for sectors with low earnings certainty**



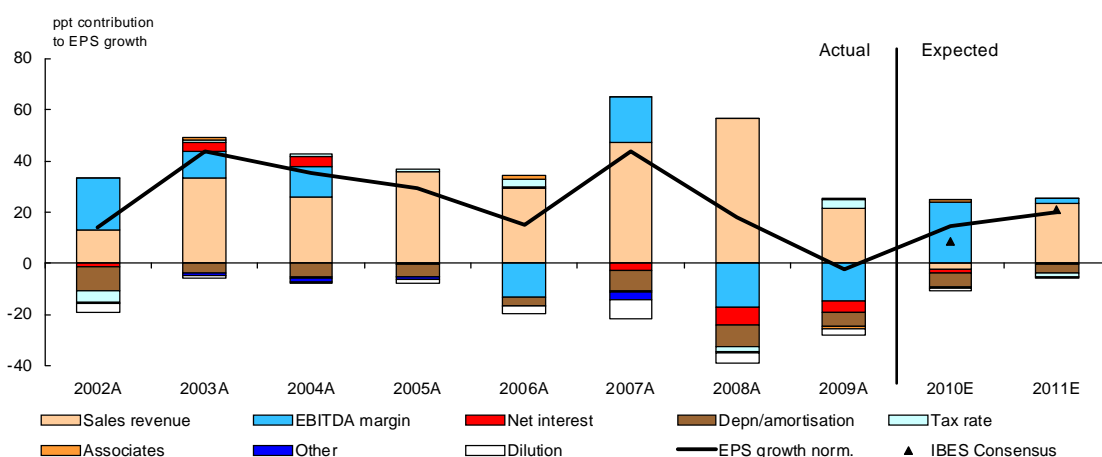
Note: Data shows only large-cap companies that have reported on a market cap-weighted and free float-adjusted basis.  
 Source: FactSet, Macquarie Research, August 2009

### Strong EPS growth forecast for FY10 as margins recover

Consensus FY10 and FY11 EPS growth estimates for our coverage of more than 100 stocks continues to get upgraded and now stands at 8.6% and 21%, respectively. Our analysts' estimates for FY10 EPS growth are comfortably above the consensus numbers, and we believe the strong earnings declared for the last quarter would lead to upgrades by consensus.

EBITDA margins still continue to be the most important driver of EPS growth for FY10. We do not think EBITDA margin expansion will abate anytime during this fiscal year, as the cost savings and lower raw material costs are still benefiting companies across the board. We also believe that sales revenue expectations will get upgraded slowly, and in our view that would be the biggest positive for earnings, as coupled with higher margins, they would lead to significant upgrades in EPS.

**Fig 5 Earnings analyser – India\* (ex financials) after FFF adjustment**



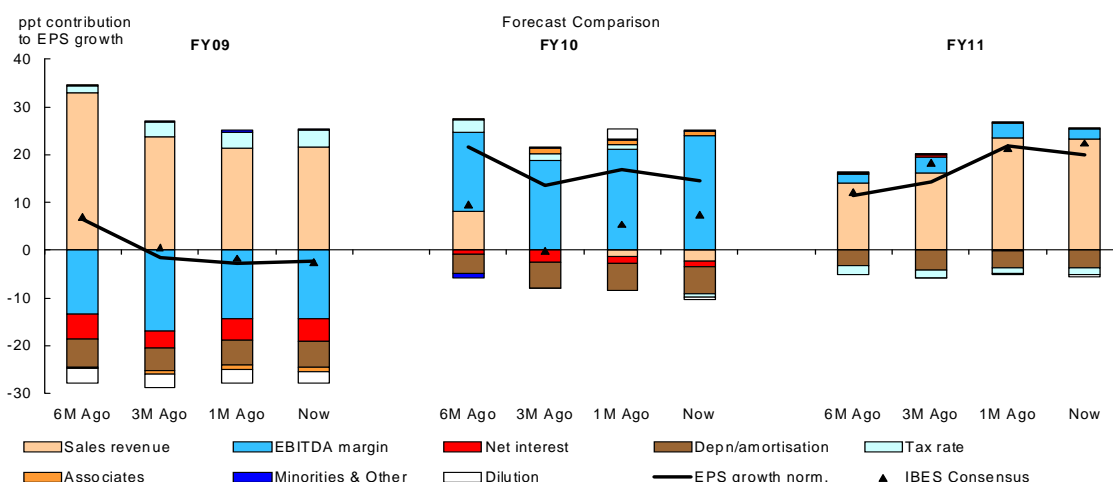
### Contribution to EPS growth (YoY %)

Year end: 31 Mar	2002A	2003A	2004A	2005A	2006A	2007A	2008A	2009A	2010E	2011E
Sales revenue	12.9	33.5	26.0	35.8	29.4	47.0	56.5	21.6	-2.2	23.4
EBITDA margin	20.3	10.3	11.6	-0.1	-12.9	17.8	-17.2	-14.4	24.0	2.1
Net interest	-1.1	3.6	4.3	-0.4	0.7	-2.6	-6.8	-4.8	-1.4	0.0
Deprn/amortisation	-9.5	-3.8	-5.2	-4.9	-3.5	-7.9	-8.6	-5.4	-5.6	-3.8
Tax rate	-4.5	0.9	0.9	1.1	2.9	0.4	-2.1	3.5	-0.7	-1.3
Associates	0.1	0.8	-0.3	-0.1	1.4	-0.8	0.2	-0.9	1.0	0.1
Minorities & other	-0.3	-0.9	-1.5	-0.8	-0.1	-2.8	-0.1	0.5	0.0	0.0
Dilution	-3.6	-0.9	-0.4	-1.5	-2.8	-7.2	-4.1	-2.4	-0.6	-0.5
<b>EPS growth norm</b>	<b>14.2</b>	<b>43.5</b>	<b>35.4</b>	<b>29.2</b>	<b>15.0</b>	<b>43.9</b>	<b>17.9</b>	<b>-2.4</b>	<b>14.6</b>	<b>20.1</b>
<b>IBES consensus</b>									<b>8.6</b>	<b>21.0</b>

\*All data is pro-rated to March.

Source: Datastream, Macquarie Research, August 2009

**Fig 6 Trend analyser – India\* (ex financials) after FFF adjustment**



\*All data is pro-rated to March.

Source: Datastream, Macquarie Research, August 2009

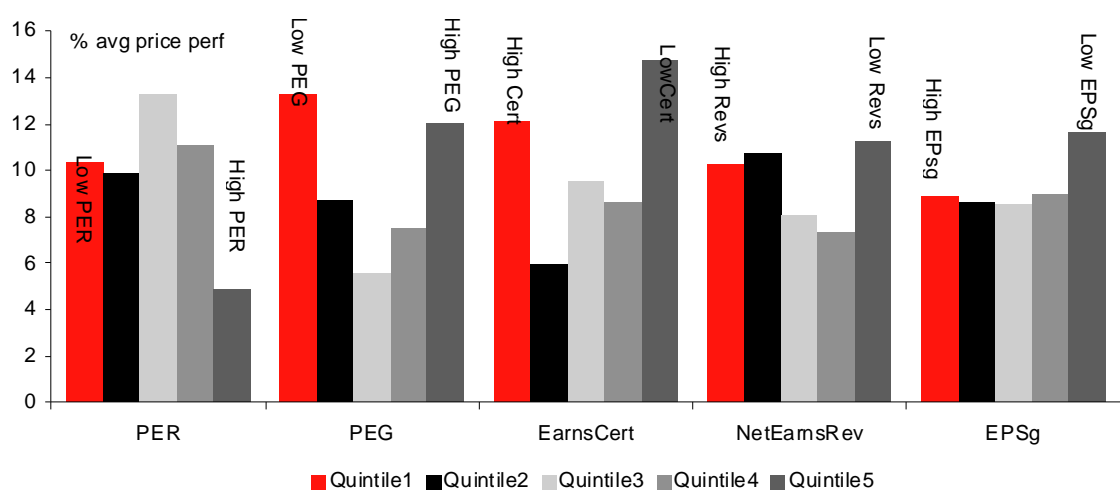
### Stock picking during this recovery period

With earnings upgrades now a given for all sectors, we find upside in stocks whose EPS growth expectations are low. We also prefer stocks that have the least earnings certainty. We do not put much weight in earnings revisions right now at the stock level, because we think all stocks are expected to get decent earnings revisions. We will definitely avoid stocks with extremely high forward PERs, as higher earnings expectations have already been factored in.

Our backtest for the Indian large-cap universe for July (equally weighted) highlights the following.

- Stocks with low EPS growth (average FY1 and FY2) expectation performed the best.
- Stocks with the highest PERs (average FY1 and FY2) performed the worst.
- Stocks with either the highest PEG (FY1 PER / average FY1 and FY2 EPSg) or the lowest PEG did better than the stocks in the middle range on a PEG basis.
- Stocks with either the worst earnings certainty (average coefficient of variation for FY1 and FY2 EPS estimate) did better than the rest of the stocks.
- Net positive earnings revision (net up revisions for FY1 and FY2 / total revisions for FY1 and FY2) was not effective at all in picking stocks.

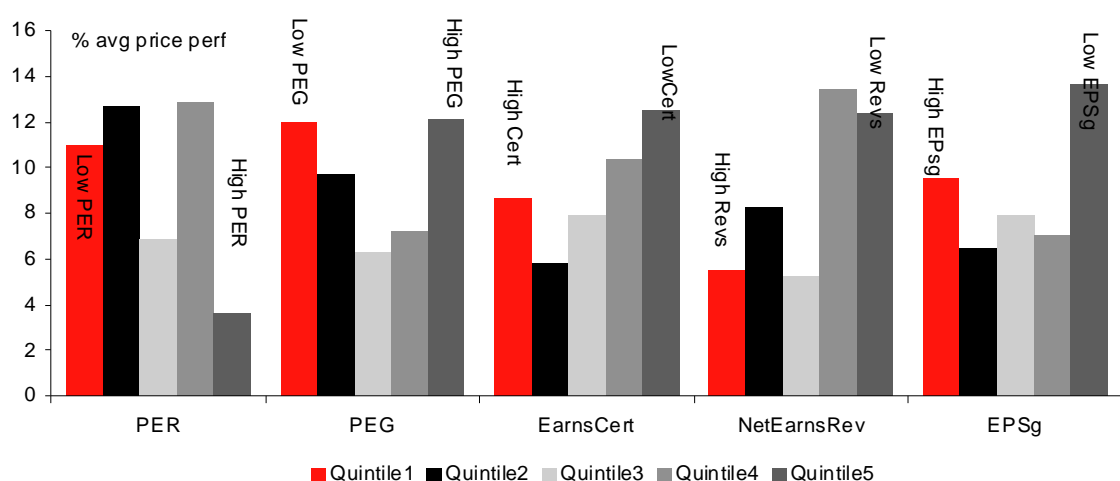
**Fig 7 Quintile performance of various strategies for the large-cap universe in July**



Source: Macquarie Research, August 2009

The results were similar for the larger universe of stocks on market cap and free float-adjusted basis.

**Fig 8 Quintile performance of various strategies for the broader universe in July**



Source: Macquarie Research, August 2009

### Stock picking strategy for the month

We expect the strategy in the previous month to continue working in the short term, because earnings upgrades are being seen across sectors due to the improving macro picture, as during the month of June. This means it will be hard to differentiate between stocks based on the magnitude and quality of growth, therefore **leaving value as the key discriminating factor**.

**Top picks:** The key criteria for selecting top picks from the large-cap universe are: stocks that do not have an extremely high average FY1 and FY2 PER and those with a low average EPS growth forecast. In addition, it is preferable that these stocks are at the extreme ends of earnings certainty. We ignore net earnings revision as a factor, because sectors across the board are getting revisions due to a better macro environment.

**Fig 9 Top picks – large-cap universe**

Bloomberg code	Company name	Sector	Mcap (US\$m)	EPS Growth (%)			PER (x)			Earning certainty*	Net earns rev ratio (x)**
				FY1	FY2	Avg	FY1	FY2	Avg		
BOI IN	Bank of India	Banks	3,874	0.1	12.6	6.4	6.0	5.3	5.7	11.7%	20.0
SESA IN	Sesa Goa Ltd.	Steel	3,809	-12.4	15.7	1.6	8.3	7.1	7.7	24.5%	35.7
TTCH IN	Tata Chemicals Ltd.	Other Chem	1,060	-5.9	7.0	0.6	8.8	8.3	8.5	13.5%	0.0
SRCM IN	Shree Cement Ltd.	Const. Mat	1,015	-20.6	-0.5	-10.6	9.0	9.0	9.0	28.5%	60.0
HZ IN	Hindustan Zinc Ltd.	Div Metals	5,975	-6.7	19.4	6.4	10.0	8.4	9.2	16.5%	55.6
TT IN	Tata Tea Ltd.	Agri/Pkgd Food	1,002	-32.0	-8.5	-20.2	9.4	10.2	9.8	34.1%	-100.0
RCOM IN	Reliance Communications L	Wireless	11,703	-16.2	10.5	-2.9	12.6	11.4	12.0	15.0%	37.9
ACEM IN	Ambuja Cements Ltd.	Const. Mat	3,047	-16.0	-12.8	-14.4	11.4	13.1	12.3	25.4%	75.0
POWF IN	Power Finance Corp. Ltd.	Other Div Fin	5,209	-13.3	11.0	-1.1	13.0	11.7	12.4	12.2%	80.0
JSP IN	Jindal Steel & Power Ltd.	Steel	9,341	-2.6	13.3	5.4	13.3	11.7	12.5	19.7%	85.7
RIL IN	Reliance Industries Ltd.	DnStream O&G	66,208	31.2	30.7	30.9	15.5	11.9	13.7	7.3%	17.9
WPRO IN	Wipro Ltd.	Software	13,802	-4.5	6.7	1.1	14.8	13.9	14.3	6.3%	3.6
BHARTI IN	Bharti Airtel Ltd.	Wireless	31,891	17.2	15.0	16.1	15.4	13.4	14.4	5.0%	14.3
PUNJ IN	Punj Lloyd Ltd.	Const & Engg	1,530	nmf	15.1	15.1	15.9	13.8	14.9	15.4%	36.0
MM IN	Mahindra & Mahindra Ltd.	4WAUTO	4,615	-17.7	13.1	-2.3	17.4	15.4	16.4	10.9%	73.9
UT IN	Unitech Ltd.	Real Estate	4,162	-38.8	15.9	-11.5	17.7	15.2	16.4	32.3%	23.5
CRG IN	Crompton Greaves Ltd.	Industrial Equip	2,220	6.3	17.5	11.9	18.0	15.3	16.6	9.2%	100.0
GCPL IN	Godrej Consumer Products	HPC	1,047	31.1	16.2	23.7	18.5	15.9	17.2	4.3%	100.0
NATP IN	NTPC Ltd.	IPPs	35,373	9.0	9.9	9.5	18.2	16.6	17.4	6.0%	31.0
INFO IN	Infosys Technologies Ltd.	Software	23,181	-5.3	6.5	0.6	18.0	16.9	17.4	6.5%	-25.7
MRCO IN	Marico Ltd.	HPC	1,084	21.8	19.5	20.6	19.3	16.2	17.8	5.1%	71.4
TPWR IN	Tata Power Co. Ltd.	Elec Util	5,246	1.6	11.0	6.3	19.8	17.9	18.8	36.3%	15.4
GLXO IN	GlaxoSmithKline Pharmaceu	Pharma	2,335	9.0	12.4	10.7	20.0	17.8	18.9	3.9%	-100.0
TTMT IN	Tata Motors Ltd.	Auto	3,160	nmf	-3.7	-3.7	19.9	20.7	20.3	39.8%	-7.7

\*Earnings certainty is defined as the average Coefficient of Variation of the earnings estimates for FY1 and FY2.

\*\* Net earns rev ratio = (Total upgrades - Total downgrades)/(Total upgrades + Total downgrades) for FY1 and FY2

Source: FactSet, Macquarie Research, August 2009

**Bottom picks:** The key criteria for selecting bottom picks is stocks with extremely high average FY1 and FY2 PERs, and those do not have low average EPS growth forecasts. In addition to this, it is preferable that these stocks do not have either too-high or too-low earnings certainty.

**Fig 10 Bottom picks – large-cap universe**

Bloomberg code	Company name	Sector	Mcap (US\$m)	EPS Growth (%)			PER (x)			Earning certainty*	Net earns rev ratio (x)**
				FY1	FY2	Avg	FY1	FY2	Avg		
GMRI IN	GMR Infrastructure Ltd.	Const & Engg	5,316	23.7	-13.5	5.1	74.6	86.2	80.4	54.0%	14.3
RPWR IN	Reliance Power Ltd.	IPPs	12,590	118.3	15.9	67.1	75.3	64.9	70.1	48.3%	-11.1
MSEZ IN	Mundra Port & Special Eco	Ports	4,619	36.0	48.9	42.5	41.3	27.7	34.5	23.7%	27.3
IBREL IN	Indiabulls Real Estate Lt	Real Estate	1,900	2601.0	95.6	1348.3	45.3	23.1	34.2	50.8%	-62.5
ABB IN	ABB Ltd. (India)	Industrial Equip	3,141	40.3	17.7	29.0	31.6	26.8	29.2	7.8%	-35.1
KMB IN	Kotak Mahindra Bank Ltd.	Other Div Fin	4,584	7.7	28.3	18.0	31.1	24.2	27.7	27.6%	50.0
NEST IN	Nestle India Ltd.	Agri/Pkgd Food	3,987	21.9	18.9	20.4	29.6	24.9	27.3	5.5%	52.9
EDSL IN	Educomp Solutions Ltd.	Educ Svcs	1,553	55.5	48.7	52.1	32.4	21.8	27.1	15.4%	-66.7
GVKP IN	GVK Power & Infrastructur	IPPs	1,395	88.2	33.3	60.7	28.2	21.2	24.7	24.3%	20.0
SIEM IN	Siemens India Ltd.	Conglomo	3,282	7.6	1.7	4.6	24.7	24.3	24.5	17.8%	38.5
HDFC IN	Housing Development Finan	Banks	14,401	15.4	18.0	16.7	25.5	21.6	23.6	8.5%	51.5
TTAN IN	Titan Industries Ltd.	Textile/Apparels	1,201	27.6	18.1	22.9	24.9	21.1	23.0	13.4%	-16.7
CLGT IN	Colgate-Palmolive (India)	HPC	1,832	21.0	9.8	15.4	23.8	21.7	22.8	6.0%	88.2
DABUR IN	Dabur India Ltd.	HPC	2,379	18.5	16.7	17.6	23.6	20.3	21.9	3.7%	88.2
APNT IN	Asian Paints (India) Ltd.	Other Chem	2,540	21.0	18.6	19.8	23.5	19.8	21.6	5.0%	76.5
CAIR IN	Cairn India Ltd.	Upstream O&G	9,350	57.6	303.2	180.4	34.5	8.6	21.6	29.9%	25.0
IDEA IN	Idea Cellular Ltd.	Wireless	4,978	-1.2	22.8	10.8	23.5	19.1	21.3	16.6%	43.8
HDFCB IN	HDFC Bank Ltd.	Banks	12,806	23.5	24.7	24.1	22.9	18.4	20.7	11.5%	51.0
SUNTV IN	Sun TV Network Ltd.	Media	1,985	24.5	18.5	21.5	20.1	17.0	18.6	9.2%	-60.0
HNDL IN	Hindalco Industries Ltd.	Div Metals	3,183	8.6	114.6	61.6	24.7	11.5	18.1	87.4%	11.1
CIPLA IN	Cipla Ltd.	Pharma	4,560	36.8	14.1	25.4	18.7	16.4	17.5	9.6%	28.0
DRRD IN	Dr. Reddy's Laboratories	Pharma	2,736	nmf	20.2	20.2	18.0	15.0	16.5	16.6%	67.6
BJAUT IN	Bajaj Auto Ltd.	Motorcycle	3,503	85.5	14.6	50.0	14.5	12.6	13.6	13.4%	83.3
IOCL IN	Indian Oil Corp. Ltd.	DnStream O&G	13,267	129.9	14.8	72.3	10.8	9.4	10.1	20.7%	14.3

\*Earnings certainty is defined as the average coefficient of variation of the earnings estimates for FY1 and FY2

\*\*Net earns rev ratio = (Total upgrades - Total downgrades)/(Total upgrades + Total downgrades) for FY1 and FY2

Source: FactSet, Macquarie Research, August 2009

## Important disclosures:

<p><b>Recommendation definitions</b></p> <p><b>Macquarie - Australia/New Zealand</b>  Outperform – return &gt;5% in excess of benchmark return  Neutral – return within 5% of benchmark return  Underperform – return &gt;5% below benchmark return</p> <p><b>Macquarie – Asia/Europe</b>  Outperform – expected return &gt;+10%  Neutral – expected return from -10% to +10%  Underperform – expected return &lt;-10%</p> <p><b>Macquarie First South - South Africa</b>  Outperform – expected return &gt;+10%  Neutral – expected return from -10% to +10%  Underperform – expected return &lt;-10%</p> <p><b>Macquarie - Canada</b>  Outperform – return &gt;5% in excess of benchmark return  Neutral – return within 5% of benchmark return  Underperform – return &gt;5% below benchmark return</p> <p><b>Macquarie - USA</b>  Outperform (Buy) – return &gt;5% in excess of benchmark return (Russell 3000)  Neutral (Hold) – return within 5% of benchmark return (Russell 3000)  Underperform (Sell) – return &gt;5% below benchmark return (Russell 3000)</p> <p><b>Recommendations – 12 months</b>  <b>Note:</b> Quant recommendations may differ from Fundamental Analyst recommendations</p>	<p><b>Volatility index definition*</b></p> <p>This is calculated from the volatility of historical price movements.</p> <p><b>Very high–highest risk</b> – Stock should be expected to move up or down 60–100% in a year – investors should be aware this stock is highly speculative.</p> <p><b>High</b> – stock should be expected to move up or down at least 40–60% in a year – investors should be aware this stock could be speculative.</p> <p><b>Medium</b> – stock should be expected to move up or down at least 30–40% in a year.</p> <p><b>Low–medium</b> – stock should be expected to move up or down at least 25–30% in a year.</p> <p><b>Low</b> – stock should be expected to move up or down at least 15–25% in a year.  * Applicable to Australian/NZ/Canada stocks only</p>	<p><b>Financial definitions</b></p> <p>All "Adjusted" data items have had the following adjustments made:  Added back: goodwill amortisation, provision for catastrophe reserves, IFRS derivatives &amp; hedging, IFRS impairments &amp; IFRS interest expense  Excluded: non recurring items, asset revals, property revals, appraisal value uplift, preference dividends &amp; minority interests</p> <p><b>EPS</b> = adjusted net profit / efpowa*  <b>ROA</b> = adjusted ebit / average total assets  <b>ROA Banks/Insurance</b> = adjusted net profit / average total assets  <b>ROE</b> = adjusted net profit / average shareholders funds  <b>Gross cashflow</b> = adjusted net profit + depreciation  *equivalent fully paid ordinary weighted average number of shares</p> <p>All Reported numbers for Australian/NZ listed stocks are modelled under IFRS (International Financial Reporting Standards).</p>
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## Recommendation proportions – For quarter ending 30 June 2009

	AU/NZ	Asia	RSA	USA	CA	EUR
Outperform	40.38%	48.53%	40.00%	44.02%	57.42%	40.20%
Neutral	39.25%	17.08%	45.00%	37.45%	32.90%	39.21%
Underperform	20.38%	34.40%	15.00%	18.53%	9.68%	20.59%

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