

### Indices

	Last close	% Chg	% YTD
Sensex	12,389	1.5	31.8
Nifty	3,565	1.4	25.7
CNX Midcap	4,758	1.9	18.1
Nasdaq	2,306	0.7	4.6
DJIA	11,867	0.1	10.7

### Volumes

	US\$m	% Chg
BSE	751	1.2
NSE	1,611	1.1
Derivatives (NSE)	4,729	8.1

### ADR/GDR (US\$)

	Latest	% Chg	% Prem
Dr Reddy's Lab	15.7	0.6	0.5
HDFC Bank	63.5	3.0	4.0
ICICI Bank	31.2	0.5	1.0
ITC	4.0	1.8	(1.7)
Infosys	48.0	1.1	17.7
Satyam	39.9	0.4	11.4
Ranbaxy	9.2	0.5	(0.8)
Reliance	50.6	0.5	0.0
Wipro	13.6	2.3	19.6
SBI	55.5	0.9	22.1
Tata Motors	19.6	2.2	(0.1)

### Net Inflows/Outflows (US\$m)

	05-Oct	MTD	YTD
FII's	(90.1)	(153)	5,094
Dom MF's	(28.8)	(25)	3,044

### Currencies

	Closing	Chg
Rs/US\$	45.71	(0.53)
US\$/EUR	1.27	(0.0)

### Bond Markets

	Closing	Chg
10 yr bond	7.58	(0.01)
Interbank call	6.35	0.05

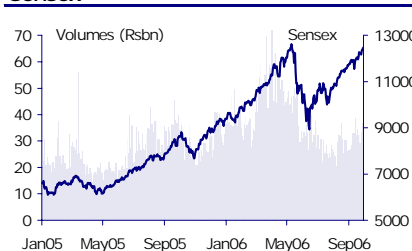
### Commodities

	Latest	% Chg	% Chg 1 m
Brent (US\$/bbl)	58.8	(0.5)	(11.3)
Gold (US\$/oz)	571	(3.3)	(9.9)
Cu (US\$/MT)	7,251	(2.7)	(7.6)
Steel (US\$/MT)	600	-	(3.2)

### FII activity in derivatives 05-Oct

	Index	Stocks
Net buying	223.1	(52.5)
Open interest	2,297.8	2,621.1
Chg in open int. (DoD)	0.0	0.0

### Sensex



## What's inside

### Reliance Industries

### News headlines: Corporate

- **UB Group** to acquire Whyte & Mackay (Scotland) for £400m(TOI).
- **DaimlerChrysler** is likely to increase its stake in **Eicher Motors** from 4% to 24%. (ET).
- **Volvo** close to acquiring 30% stake in LRIH, the holding company of **Ashok Leyland**. (ET)
- **Ashok Leyland** and **Rico Auto** have bid for acquiring Doktas, a Turkish casting company. (ET).
- **M&M** and **ICICI Ventures** are making a bid to acquire Lombardini, a diesel engine manufacturer in Italy. (ET)
- **Tata Tea** has acquired a 33% stake in Joekels Tea (S. Africa). (ET).
- **Reliance Ind.** Has doubled the commercial production target from KG basin to 80mmscmd. (ET)
- **Tata Steel** planning a US\$2bn bond issue to part-finance acquisition of Corus Steel. (BS)
- Communications Ministry to approach Cabinet for approval to form an SPV to administer **VSNL's** surplus land of 773acres. (BS)
- Indian Govt. has offered the Qatar Govt. a stake in **Petronet LNG** as part of ongoing negotiations over LNG supply from Qatar. (BL).

### News headlines: Economic and Political

- Govt. has approved six-laning of 6,500km of national highways, incl. 5,700km of the Golden Quadrilateral, at a cost of Rs410bn. (ET)
- NHAI has yet to award a single project under NHDP, as against a target of awarding contracts for 3,000km in FY07. (FE)

### Turnover highlights

	Price (Rs)	Chg (%)	Vol (\$m)	YTD chg (%)
SAIL	80	5.7	37.5	48.5
HDFC Bank	931	4.3	10.7	315
Infosys	1866	3.5	58.1	24.5
Tata Steel	537	2.7	34.6	413
SBI	1039	2.4	39.1	14.5
Wipro	521	2.3	10.9	12.4
L&T	1262	2.3	16.2	36.9
Grasim	2,547	2.2	22.1	83.1
Satyam	818	1.9	47.7	10.9
Tata Motors	895	1.6	49.2	37.0
ICICI Bank	705	1.4	19.2	20.7
ITC	187	1.4	12.7	32.0
HLL	250	1.2	10.7	26.7
TCS	999	1.1	40.6	17.4
ONGC	1,144	0.9	25.5	(2.7)
HDFC	1,453	0.9	17.3	20.5
IOC	539	0.7	4.5	(3.3)
Ranbaxy	424	0.7	10.3	17.0
Bajaj Auto	3,107	0.6	18.8	55.3
NTPC	131	0.6	2.6	16.9
Gail	258	0.6	3.1	(2.9)
Hindalco	173	0.5	15.5	20.3
Reliance	1,155	0.5	132.7	68.8
BHEL	2,312	0.4	33.9	66.7
Hero Honda	753	0.3	10.7	(12.4)
Sun Pharma	936	0.2	0.9	37.2
Maruti	948	0.0	28.3	48.9
Zee	293	0.0	34.6	86.5
Dr.Reddy's	712	(0.1)	7.8	45.5
Bharti	459.1	(0.5)	6.7	32.8

### BSE 200 Movers and Shakers

	Price (Rs)	Chg (%)	YTD chg (%)
<b>Top Gainers</b>			
Petronet LNG	58	20.0	(2.2)
Moser Baer	249	18.6	27.1
Apollo Tyres	344	7.4	23.6
Bank Of India	167	6.7	30.7
Polaris Software	131	6.6	(0.3)
Asahi India	126	5.8	39.1
SAIL	80	5.7	48.5
Britannia	1,181	5.2	(2.7)
MRF	4,066	5.0	47.8
Alstom	363	4.5	67.4
Dredging Corp.	613	4.5	3.2
Allahabad Bank	90	4.4	7.9
Cummins India	243	4.4	53.2
Bank Of Maharashtra	33	4.3	11
<b>Top Losers</b>			
Novartis	439	(2.6)	(25.5)
HCL Info	140	(1.4)	(49.4)
Apollo Hospitals	486	(1.0)	(2.6)
Balrampur Chini	100	(0.8)	(14.0)
Hindustan Zinc	591	(0.7)	14.2
Engineers India	504	(0.5)	(24.2)
HCL Tech	550	(0.5)	2.1
Gillette	866	(0.5)	18.0
Monsanto	1,711	(0.5)	(10.9)
Marico	514	(0.5)	39.7
Bajaj Hindusthan	324	(0.5)	3.7
Bharti	459	(0.5)	32.8
Matrix Labs	266	(0.5)	9.1
Gujarat NRE Coke	34	(0.4)	(34.9)

**Key to CLSA investment rankings:** **BUY** = Expected total return greater than 10%; **O-PF** = Expected to outperform the local market by 0-10%; **U-PF** = Expected to underperform the local market by 0-10%; **SELL** = Expected to underperform the local market by >10%. Performance is defined as 12-month total return (including dividends).

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**Note: In the interests of timeliness, this document has not been edited.**

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19/07/2006

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06 October 2006

### India Energy

Reuters RELI.BO  
Bloomberg RIL IN

Priced on 5 October 2006  
India Sensex @ 12,389

12M price target Rs1,237.00  
±% up/downside +7%  
Target set on 5 Oct 06

Market cap US\$35,210m  
Shares in issue 1,393.5m  
Free float (est.) 54.0%

3M average daily volume  
Rs5,950.7m (US\$128.4m)

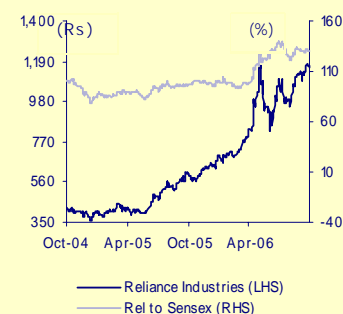
12M high/low  
Rs1,195.00/558.10

Foreign shareholding}} 24.7%

Major shareholders  
Ambani family 34.0%  
FIIs 19.8%

#### Stock performance (%)

	1M	3M	12M
Absolute	1.6	7.1	88.3
Relative	(0.8)	(6.4)	35.8
Abs (US\$)	3.0	8.1	82.6



Source: Bloomberg

www.clsa.com

## Stepping on the gas

Upstream E&P has transformed Reliance's profile with and promises to make it a global top-20 player in the space. Strong newsflow in this business is also the key reason why Reliance has added US\$14bn in market cap since the demerger and has outperformed the Sensex by 33pnt. With core profits having run into a growth challenge, however, investor focus will increasingly shift towards execution. At 16x PE and with half of the current price already accounted for by new businesses (that start coming onstream in two years), the margin for error is minimal.

**A steady stream of upstream newsflow.** Expectations on Reliance's upstream business have scaled up materially over the last few months. A slew of newsflow points towards the possibility of (a) a 3.5x reserve upgrade in KG-D6 to 50tcf, (b) a deeper Cretaceous hydrocarbon play in KG-D6 indicating further reserve accretion potential, (c) possibility of billion barrel crude finds in KG-III-6 and KG-D6, and (d) huge exploration upside from the KG-D4 block won in NELP-V. Based on the potential reserves in KG-D6, NEC-25 and its CBM blocks, Reliance may now hold over 5bnboe of 2P in recoverable reserves (95% gas) – 75% of size of ONGC today.

**Huge potential value in upstream.** On the back of favourable upstream newsflow, Reliance has added US\$14bn in market value (+66%) since the demerger outperforming the Sensex by 33pnt over this period. Our base case upstream valuation of Rs442/share (US\$12bn) still leaves some value on the table if the best case reserve assessments in KG-D6 are proved correct and KG-D4 holds material reserves. Further newsflow confirming these best case assessments have now started forming the baseline of expectations, though, indicating that upside scenarios are getting priced in.

**Focus to shift on execution.** With a large chunk of new business optimism already factored in the stock price and with core earnings running into a growth challenge, investor focus will increasingly shift towards project execution in Reliance Petroleum, upstream development and organised retail. Reliance's stellar record is a source of confidence and the impending organised retail rollout (expected to commence in the next couple of weeks) will be an important gauge to reassess this in a B2C landscape; it is likely, though, that the rollout will be gradual and phased. At the same time, recent developments around SEZs point towards medium term challenges that need to be overcome in Reliance's chosen new business segments.

**Margin of error is minimal.** If all current speculation of upstream reserve size get confirmed, the retail rollout sees flawless execution and core business profits remain robust, Reliance could deliver a c.10% three year stock price cagr from here on. At 16x PE (zero discount to market multiples) and with half of the current price already accounted for by new businesses (which start coming onstream only two years from now), the margin for error is minimal, however. Our target price of Rs1,237 (which factors in most of the optimism on upstream) indicates an 7% upside.

#### Financials

Year to 31 Mar	05A	06A	07CL	08CL	09CL
Revenue (Rsm)	654,641	782,416	1,052,528	982,370	926,255
Ebitda (Rsm)	126,753	144,216	164,556	164,680	198,976
Net profit (Rsm)	75,717	90,693	96,735	96,773	114,757
EPS (Rs)	54.3	65.1	69.4	69.5	82.4
CLSA/consensus(13) (%)	-	-	97	100	113
EPS (% YoY)	46.8	19.8	6.6	-	18.5
ROAE (%)	20.30	26.30	29.80	24.00	23.50
Net gearing (%)	29.0	62.0	53.1	47.3	34.7
PEX (@Rs1,155)	21.2	17.7	16.6	16.5	14.0
Price/book (x)	4.0	5.6	4.4	3.6	3.0
EV/Op Ebitda (x)	13.6	12.3	10.9	11.0	9.0

Source: CLSA Asia-Pacific Markets

Reliance likely has over 5bn boe of recoverable (predominantly gas) reserves

There could be further reserve upsides but the market may already be pricing part of it in

With US\$17bn in value ascribed to businesses that are still getting executed, the margin of execution error is receding

Figure 1

Reliance's upstream portfolio has gained in size. Although its formal announcements indicate recoverable reserves of 2.6bn boe, recent media speculation and assessments by partner Niko Resources indicate that reserves could be upgraded to 5bn boe. Exploration upsides may take this even higher

	In Base Case Valuation			Upside Potential		
	Gas (tcf)	Crude (mboe)	Total (mboe)	Gas (tcf)	Crude (mboe)	Total (mboe)
KG-D6	20.9	0	3,487	20.9	-	3,487
KG-D6 Gas Upside	13.5	0	2,250	27.0	-	4,500
KG-D6 Crude Upside	0.0	0	-	0.0	900	900
NEC 25	3.3	0	555	7.4	-	1,230
CBM	3.7	0	608	3.7	-	608
KG-III-6 Crude	0.0	900	900	0.0	900	900
KG-D4	0.0	0	-	9.9	-	1,647
<b>Total in place</b>	<b>41.4</b>	<b>900</b>	<b>7,800</b>	<b>68.8</b>	<b>1,800</b>	<b>13,272</b>
<b>Recoverable</b>	<b>29.2</b>	<b>270</b>	<b>5,132</b>	<b>48.8</b>	<b>540</b>	<b>8,668</b>
<b>% recovery</b>	<b>70</b>	<b>30</b>	<b>66</b>	<b>71</b>	<b>30</b>	<b>65</b>

Source: Media reports, Niko Resources, CLSA Asia-Pacific Markets

Figure 2

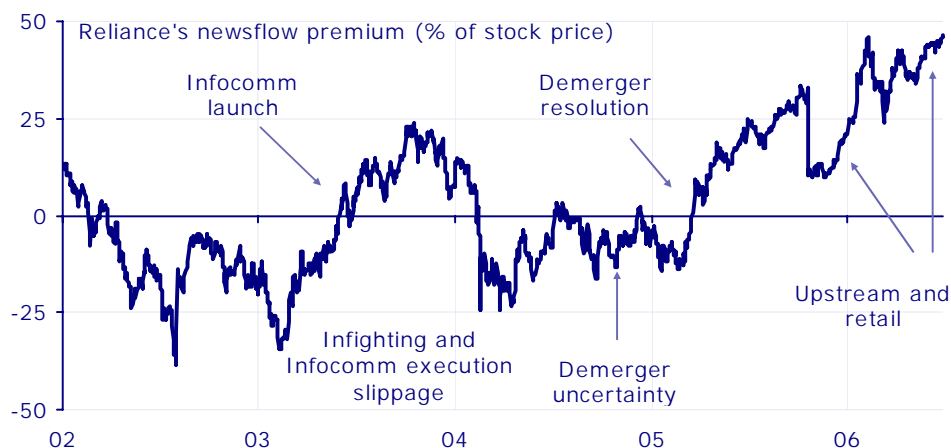
Our base case valuation includes US\$12bn of upstream reserve value. These will start getting monetised only two years from now, however. Market expectations on further reserve accretion is rising, though – especially in D4 and D6-Cretaceous

(Rs/share)	Target Price	Potential	Comments
KG-D6	229	229	Base case KG-D6 gas reserve value (23.2tcf 2P best est.)
KG-D6 Gas Upside	91	182	Reserve upside to 50 tcf OGIP. Field development phased to optimize profit sharing. Target price factors in 50% risk weight. Clarity expected over the next 6-12 months
KG-D6 Crude Upside	-	50	1bn boe of crude reserves estimate from Cretaceous plays factored in. First well encountered crude.
NEC 25	41	67	Reserve upgrade to 8.2tcf (high estimate of GCA reserves and resources)
CBM	31	31	
KG-III-6 Crude	50	50	1bn boe of crude reserves factored in
KG-D4	-	142	Half the size of KG-D6 adjusted for better fiscal terms and 85% ownership. This is still in an exploration stage and further clarity is expected only in next 12-18 months
<b>Total</b>	<b>442</b>	<b>751</b>	Factoring in media speculation and initial assessments of Niko, upstream value can increase by 70% from base case
<b>EV (US\$m)</b>	<b>12,013</b>	<b>20,406</b>	
<b>Rec. reserves (mboe)</b>	<b>5,132</b>	<b>8,668</b>	Based on Reliance's formal announcements, recoverable reserves are 2.6bn boe
<b>EV/boe (US\$)</b>	<b>2.3</b>	<b>2.4</b>	

Source: CLSA Asia-Pacific Markets

Figure 3

The recent stock price appreciation means that half the stock price now is accounted for by expectations on new businesses – a five year high.



Source: CLSA Asia-Pacific Markets. Note: Calculated as Stock Price – 8\*adjusted EPS

On earnings alone, current stock prices will be justified only by end FY08

Reliance's traditional 20% PE multiple discount has also vanished

We expect a moderate 10-11% annual return for Reliance is a flawless execution scenario.

Flawless execution and continuing strong newsflow will mean a 20-22% cagr in stock price. This is our best case

Figure 4

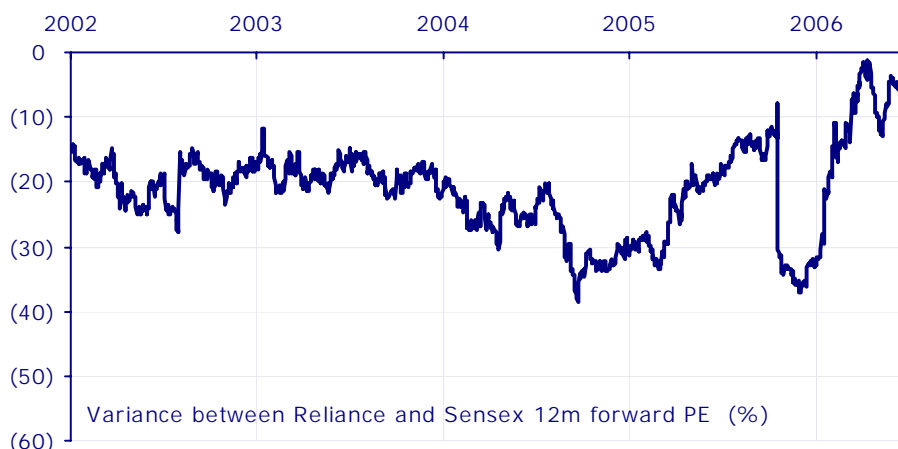
**Reliance's PE has re-rated to 16x and now seems to be trading on FY10 estimates**

(Rsm)	FY06	07CL	08CL	09CL	10CL	Comments
Core profits	90,693	96,735	96,773	84,831	78,863	Core margins will moderate
KG Basin	-	-	-	29,926	68,752	Start in June-08 ramping up from 40 to 80mmscmd in phases
NEC-25	-	-	-	-	13,117	Start in FY10 at 10mmscmd
Rel Petro (75%)	0	0	0	10,084	37,935	US\$10/bbl GRM for RPL in FY09-10
Reliance Retail (100%)		645	1,983	7,544	13,648	Phased rollout to US\$20bn revenues and 4.5% net margin in 7years
Others	3,289	3,250	3,250	3,250	3,250	IPCL and other affiliates
<b>Consolidated</b>	<b>93,982</b>	<b>100,630</b>	<b>102,006</b>	<b>135,635</b>	<b>215,565</b>	<b>FY10 will be a landmark year</b>
<b>EPS</b>	<b>67.4</b>	<b>72.2</b>	<b>73.2</b>	<b>97.3</b>	<b>154.7</b>	<b>13% FY06-09CL EPS cagr</b>
<b>PE @ Rs1155</b>	<b>17.1</b>	<b>16.0</b>	<b>15.8</b>	<b>11.9</b>	<b>7.5</b>	

Source: CLSA Asia-Pacific Markets

Figure 5

**Reliance's PE discount to the market has vanished**



Source: CLSA Asia-Pacific Markets

Figure 6

**We expect an 10-11% cagr in stock prices indicating that Reliance is finely priced for growth. Our blue-sky scenario (which assumes that newsflow will accelerate) indicates only a 22% cagr in stock price. The margin for error is receding**

	Profits (Rsm)	PEx	FY10 Equity Value	
			US\$bn	Rs/share
<b>Current business and growth projects</b>				
Core profits	78,863	10.6	18.6	600
KG Basin	68,752	8.0	12.2	395
NEC-25	13,117	6.5	1.9	61
Reliance Petroleum (75%)	37,935	7.5	6.3	204
Reliance Retail (100%)	13,648	40.0	12.1	392
Others	3,250	8.0	0.6	19
<b>Consolidated</b>	<b>215,565</b>		<b>51.7</b>	<b>1,670</b>
<b>Base case stock price cagr (%)</b>				<b>11</b>
<b>Blue-sky upstream upsides</b>				
KG-D6 Gas Upside			5.0	182
KG-D6 Crude Upside			1.3	50
NEC 25			0.7	26
CBM			0.9	31
KG-III-6 Crude			1.3	50
KG-D4			7.7	285
<b>Total</b>			<b>16.9</b>	<b>623</b>
<b>Best Case Stock Price (base + upside)</b>			<b>68.7</b>	<b>2,294</b>
<b>Base case stock price cagr (%)</b>				<b>22</b>

Source: CLSA Asia-Pacific Markets.

Our target price indicates 7% upside from current levels

Upstream, RPL and Reliance Retail make up half of our target price. These will start contributing to earnings from FY09 onwards

Our target price upgrade is led by upgrades to upstream reserve value.

Reliance has still not made any formal announcements backing up higher upstream reserve numbers

Figure 7

<b>Reliance sum of parts and target price</b>		
	Rs/share	Comments
<b>Core Business</b>	<b>600</b>	<b>Implies a 7.5x PE and 5.5x EV/Ebitda on FY07-08 earnings</b>
Petrochemicals	322	At mean of mid-cycle, peak cycle, bottom cycle EV/Ebitda, DCF and Replacement Cost. Implies 5.8x EV/Ebitda.
Refining	354	DCF backed up by peer comps, historic multiples. Implies 5.4x EV/Ebitda.
Fuel Retailing	24	At estimated cost at end of FY07. Reliance is losing money in this busbies
Panna-Mukta	57	At separate asset valuation benchmarks for oil and gas reserves
Net Debt	(158)	FY07CL end estimated end net debt
<b>New upstream</b>	<b>442</b>	<b>US\$16bn in value. Monetization starts in two years</b>
KG-D6	229	DCF based on 23 tcf 2P best estimate reserves; 80mmscmd peak production; US\$3/mmbtu for the first 40mmscmd and US\$4/mmbtu for incremental production. Implies US\$2.5/boe on recoverable reserves.
KG-D6 Upside	91	Media reports suggest further upside from Cretaceous and deeper hydrocarbon plays. We have risked these by a 50% probability
NEC 25	41	DCF based on 3.7 tcf 2P best estimate reserves and US\$4/mmbtu gas price. Implies US\$2.8/boe on recoverable reserves.
CBM	31	3.65tcf of reserves; 70% recovery at US\$2.0/boe
KG-III-6 Crude	50	1bn boe of reserves, 30% recovery, EV/boe = US\$5. Reliance holds 90%
KG-D4	0	Niko Resources has indicated significant prospectivity
<b>Investments</b>	<b>196</b>	<b>RPL is discounting strong GRMs in FY09-10</b>
IPCL	22	20% strategic holding discount on market value
Rel Petroleum	132	20% strategic holding discount on recent IPO price of Rs60/share
Rel Retail	41	Retail investments at 1.5x P/B on committed US\$750m investment. Reliance will invest US\$5.5bn eventually
SEZs	0	Potential value is significant but there is insufficient business and financial clarity currently.
<b>Sum of Parts</b>	<b>1,237</b>	<b>12m target price indicates 7% upside from current levels.</b>

Source: CLSA Asia-Pacific Markets

Figure 8

<b>What has changed in our sum-of-parts</b>			
(Rs/share)	Current	Old	Comments
<b>Core Business</b>	<b>600</b>	<b>600</b>	
<b>New upstream</b>	<b>442</b>	<b>153</b>	<b>Rs289/share upgrade (+US\$9bn)</b>
KG-D6	229	141	Reserve upgrade from 14tcf to 35.4tcf by Niko Resources; we factor in 23.2tcf of 2P reserves and resources. Production upgrade from 40mmscmd to 80mmscmd. Gas pricing increased from US\$2.34/mmbtu to blended US\$3.5/mmbtu
KG-D6 Upside	91	0	Media reports speculate on 50tcf of potential in place reserves and resource in KG-D6. More hydrocarbon plays also possible
NEC 25	41	12	Pricing upgraded to US\$4/mmbtu and reserve upgraded to 3.7tcf (best estimate of 2P reserves and resources as per GCA)
CBM	31	0	Monetization likely in FY09
KG-III-6 Crude	50	0	1bn boe of in place reserves factored in as per media speculation
KG-D4	0	0	Exploration upsides not factored in. Further clarity is 12-18 months away. Pre-drill assessments are currently underway.
<b>Investments</b>	<b>196</b>	<b>192</b>	
IPCL	22	19	Increase in market price
Rel Petroleum	132	132	No change, still pegged at 20% discount to IPO price
Rel Retail	41	41	No change. Rollout with be gradual and phased.
SEZ	0	0	No change
<b>Sum of Parts</b>	<b>1,237</b>	<b>945</b>	<b>Rs292/share upgrade (+US\$9bn)</b>

Source: CLSA Asia-Pacific Markets

Recommendation history - Reliance Industries RIL IN

Date	Rec level	Closing price	Target
05 October 2006	O-PF	1,149.35	1,237.00
28 April 2006	O-PF	1,007.80	945.00
18 January 2006	BUY	693.85	750.00
04 January 2006	BUY	704.00	763.37
29 November 2005	BUY	642.28	704.30
26 November 2005	BUY	639.63	708.09
20 September 2005	BUY	589.57	641.44
11 July 2005	BUY	479.34	562.68
04 July 2005	BUY	487.60	565.71
03 July 2005	BUY	484.41	564.95
21 June 2005	BUY	489.15	530.88
28 March 2005	BUY	429.43	511.94
28 October 2004	BUY	408.68	474.83
27 October 2004	BUY	409.86	418.79
26 October 2004	BUY	417.85	474.83
22 July 2004	BUY	344.43	418.79
24 May 2004	BUY	343.52	486.95
30 April 2004	BUY	398.65	498.31
30 January 2004	BUY	423.79	499.83
09 January 2004	BUY	436.14	487.71
01 January 2004	BUY	431.52	502.10
27 November 2003	BUY	359.95	443.78
26 November 2003	BUY	353.89	445.30
17 October 2003	BUY	370.40	436.97

Source: CLSA Asia-Pacific Markets

**Key to CLSA investment rankings:** BUY = Expected total return greater than 10%; O-PF = Expected to outperform the local market by 0-10%; U-PF = Expected to underperform the local market by 0-10%; SELL = Expected to underperform the local market by >10%. Performance is defined as 12-month total return (including dividends).

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Note: In the interests of timeliness, this document has not been edited.

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