

### INITIATING COVERAGE

#### Share Data

|                       |               |
|-----------------------|---------------|
| Market Cap            | Rs. 425.22 bn |
| Price                 | Rs. 1477.7    |
| BSE Sensex            | 14504.6       |
| Reuters               | SUZL.BO       |
| Bloomberg             | SUEL IN       |
| Avg. Volume (52 Week) | 0.26 mn       |
| 52-Week High/Low      | Rs. 1555/885  |
| Shares Outstanding    | 287.76 mn     |

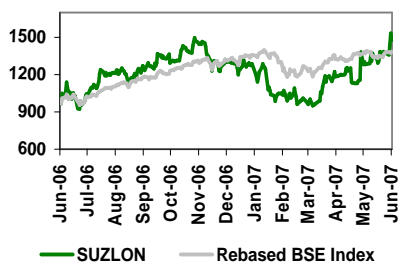
#### Valuation Ratios

| Year to 31 March | 2008E | 2009E |
|------------------|-------|-------|
| EPS (Rs.)        | 43.3  | 70.7  |
| +/- (%)          | 44.1% | 63.3% |
| PER (x)          | 34.1x | 20.9x |
| EV/ Sales (x)    | 3.9x  | 2.8x  |
| EV/ EBITDA (x)   | 35.1x | 30.2x |

#### Shareholding Pattern (%)

|                 |    |
|-----------------|----|
| Promoters       | 70 |
| FII's           | 21 |
| Institutions    | 1  |
| Public & Others | 8  |

#### Relative Performance



### Suzlon Energy Limited

Buy

#### Reaching new heights

Suzlon Energy Limited (Suzlon), the largest manufacturer of Wind Turbine Generators (WTGs) in India and the fifth largest in the world, will likely continue its impressive growth in the coming years. Suzlon's global market share increased from 6.1% in FY06 to 7.7% FY07 in line with its strategy to expand in the high growth and volume markets like China, India and the US. Suzlon's order book of Rs. 94.9 bn reflects its strategy with close to 82% of the orders coming from these countries with the US share being 61%. To ensure its continuous growth and to keep up with the demand Suzlon is investing in new manufacturing facilities and expanding the current facilities. Due to Suzlon's tremendous growth potential, we believe the stock is undervalued and we expect the stock price to rise.

#### Key Figures

| Year to March  | FY05   | FY06   | FY07   | FY08E   | FY09E   | CAGR (%) |
|--|--------|--------|--------|---------|---------|----------|
| (Figures in Rs mn, except per share data) (FY07-09E) |        |        |        |         |         |          |
| Net Sales  | 19,425 | 38,410 | 79,857 | 115,793 | 162,110 | 42.5%    |
| EBITDA   | 1,891  | 4,697  | 8,658  | 12,958  | 15,053  | 31.9%    |
| Net Profit   | 1,243  | 3,653  | 7,593  | 8,639   | 12,451  | 28.1%    |
| <b>Margins(%)</b>                                    |        |        |        |         |         |          |
| EBITDA   | 24.2%  | 22.5%  | 16.2%  | 13.0%   | 15.0%   |          |
| NPM  | 18.8%  | 19.8%  | 10.8%  | 10.8%   | 12.5%   |          |
| <b>Per Share Data (Rs.)</b>                          |        |        |        |         |         |          |
| EPS  | 14.5   | 27.8   | 30.0   | 43.3    | 70.7    | 53.4%    |
| PER (x)  | 102.2x | 53.1x  | 49.2x  | 34.1x   | 20.9x   |          |

- We expect the net sales of Suzlon to grow faster than the industry average with a CAGR of 42.5% for FY07-09E due to Suzlon's strategy of expanding into high growth and volume markets.
- The growth in EBITDA is anticipated to be 31.9% annually for FY07-09E.
- At the current price of Rs. 1,374, the stock is trading at a forward PE of 34.1x FY08E and 20.9x FY09E.
- Using a discounted cash flow method, the stock is valued at Rs. 1,720. We initiate coverage with a Buy with a one year perspective.

*Orders of Rs. 94.9 billion  
already on the order book*

*Through strategic  
acquisitions,  
manufacturing of key  
components kept in-house*

*Production quantity to  
increase from 2,700 mw to  
4,200 mw*

### **Investment Rationale**

#### ***Strong growth to continue***

Suzlon has orders of Rs.94.9 bn in its order book which suggests that the company is likely to continue its robust growth in the coming years. Suzlon is focused on expanding into the new high growth and volume markets like China and US that are growing at a faster rate than the industry average. This is reflected by nearly 70% of the orders placed in the order book by the Chinese and the US customers.

#### ***Vertical integration of key component manufacturers***

The wind energy industry suffers from long lead times due to shortage of a few key components such as gearboxes, rotor blades, tower, etc and strong demand. The strategic acquisition of companies like Hansen Transmissions International NV, a Belgian based gearbox manufacturer, along the value chain allows Suzlon to keep the production of the key components in-house. Suzlon is also investing in building new facilities for forging, foundry and machining of its components in India. This should help Suzlon meet the delivery schedules and lower its lead time for the delivery of WTGs and also to keep up with the rising demand.

#### ***Increasing investment in production facilities***

Suzlon anticipates the strong demand for WTGs to continue and in a response to this the company is investing Rs. 33.1 bn over the next two years to build new facilities and expand the capacities of the existing facilities. Suzlon is expanding its facilities primarily in India and in Belgium. The total production output of Suzlon will increase from 2,700 mw to 4,200 mw by Q4 of FY08.

#### ***Acquisition of REpower***

Suzlon successfully acquired a 33.9% stake and 87.1% of voting rights in REpower, a German based WTG manufacturer. The other two big shareholders in REpower are Areva and Martifer with a stake of 30.1% and 23.1% respectively. Suzlon has an agreement with both of these companies that gives them an option to sell their share in REpower to Suzlon and exit REpower. Due to this agreement, Suzlon does not have to raise all Rs. 73.8 bn

(Euro 1.3 bn) at once, but can pay for this acquisition in installments over the next two years with Areva opting to exit in one year and Martifer in two years. ABN Amro, ICICI Bank and State Bank of India are financing this deal. There are positive synergies between the two companies and their products are complementary to each others products. This strategic move gives Suzlon a strong base in Europe to expand in the European market and also lets Suzlon tap into the technical expertise of REpower in designing large multi-mw offshore turbines.

### Key Risks

#### *Competition*

*High growth and Volume markets would attract more competition due to their higher growth rate than the industry average*

As Suzlon increases its share in the high growth and volume markets, it would also draw more competition from the other WTG manufacturers. Not only are these high growth and volume markets growing at a faster rate than the industry average of 19.1%, but these markets are also high volume markets. The high growth and volume markets would draw more competition especially from other bigger manufacturers like Vestas Wind Systems, GE Wind, Enercon GMBH and Gamesa. By virtue of their bigger size, higher production capacity and more experience in the wind energy industry, these big companies might be able to expand into high growth and volume markets at a much faster rate than Suzlon. It could also prove to be difficult for Suzlon to expand into new high growth and volume markets especially China and US where some of these bigger companies already have a strong foothold and Suzlon is just a new entrant. In China, Gamesa leads with 33.4% market share and in US, GE Wind has a market share of 61.2%.

#### *Continuation of subsidies & Production Tax Credit (PTC)*

The governments of various nations give tax incentives to the companies that use WTGs to produce electricity. The uncertainty about the extension of these tax incentives can lower the demand. In 2004, PTC in US expired and due to this the demand for WTGs fell drastically in US. However, it was extended in 2005 for four more years and the demand picked up with an increase of 36% in 2005 and 27% in 2006. This shows that government tax credits are important to the continuous growth of the wind energy industry.

*Customers wait up to 12 months to receive delivery and if the present situation persists then it could increase to 18-24 months*

### *Supply chain issues*

Due to the shortage of some key components and high demand, the industry has not been able to keep up with the increase in orders. According to Global Wind Energy Council (GWEC), the customers have to wait for 12 months to get the delivery of WTGs for their wind farms and if this trend continues the lead time could increase to 18-24 months. If this issue is not resolved soon then the wind energy industry might lose some potential customers who might look into other alternative energy sources.

### *Rising cost of raw material*

The rising cost of raw material especially steel, copper and carbon in the recent years have put an additional burden on the WTG manufacturers. Due to strong demand in the industry, the manufacturers have been able to pass on most of this cost to the customers, but as the gap between industry supply and demand narrows the manufacturers will not be able to pass this on to their customers. This could translate into lower margins for Suzlon.

### **Forecast**

*Wind energy industry to increase its global share in electricity production from 0.8% in 2006 to 4.0% in 2016*

Due to an increase in demand for energy, fuel prices and environmental awareness, a lot of research is being done on alternative sources of energy. In recent years, the wind energy industry has received a lot of attention as an alternative source of energy and government support in the form of subsidies and tax incentives. The wind energy is expected to continue its strong growth and is expected to increase its share in the overall energy production from 0.8% in 2006 to 4.0% in 2016.

Suzlon has strategically positioned itself for a strong growth in the coming years through vertical integration and expanding into the high growth and volume markets. Due to this, Suzlon is likely to grow at a faster rate than the overall wind energy industry. The planned investment in building new facilities and expanding existing facilities would allow Suzlon to keep up with the rising demand.

*5<sup>th</sup> largest WTG manufacturer in the world with a global market share of 7.7% and more than 50% of the Indian market share*

### Company Background

Founded in 1995, Suzlon Energy Limited is the largest producer of WTGs in India with a market share of more than 50% and the fifth largest in the world with a market share of 7.7%. Based in India, the company has a worldwide presence with operations in 14 countries and manufacturing plants in India, China, US and Belgium (Hansen).

Suzlon provides the complete end-to-end solution to its customers in the wind energy market. Suzlon

- identifies good wind farm sites through wind resource mapping
- acquires and develops the installation sites
- installs WTGs on the site
- provides maintenance services

Suzlon manufactures high performance and cost efficient WTGs. Through acquisition of key component manufacturers in the past, Suzlon has become self-reliant and is able to better streamline its manufacturing and supply chain processes.

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