kotak® Institutional Equities

INDIA DAILY

July 22, 2013

Contents

EQUITY MARKETS

		Change %		
India	**19-Jul**	**1-day**	**1-mo**	**3-mo**
Sensex	20,150	0.1	7.3	5.1
Nifty	6,029	(0.1)	6.4	3.3
Global/Regional indices				
Dow Jones	15,544	(0.0)	5.0	6.7
Nasdaq Composite	3,588	(0.7)	6.9	10.9
FTSE	6,631	(0.1)	8.4	5.6
Nikkei	14,693	0.7	11.1	8.3
Hang Seng	21,387	0.1	5.5	(3.0)
KOSPI	1,888	0.9	3.6	(2.0)
Value traded – India				
Cash (NSE+BSE)	142		124	125
Derivatives (NSE)	1,594		1,336	2,060
Deri. open interest	1,554		1,525	1,562

Forex/money market				
	Change, basis points			
	19-Jul	**1-day**	**1-mo**	**3-mo**
Rs/US$	59.4	(8)	(42)	515
10yr govt bond, %	8.3	-	62	41
Net investment (US$mn)				
	18-Jul		**MTD**	**CYTD**
FIIs	(19)		(1,001)	12,341
MFs	(51)		(174)	(2,411)

Top movers				
	Change, %			
Best performers	**19-Jul**	**1-day**	**1-mo**	**3-mo**
RCOM IN Equity	145.4	(0.9)	21.6	48.7
HUVR IN Equity	686.1	(0.3)	16.2	42.1
IDEA IN Equity	150.5	(0.3)	7.6	34.0
LPC IN Equity	899.2	1.0	14.2	31.6
UNSP IN Equity	2740.3	(2.1)	13.7	30.6
Worst performers				
MMTC IN Equity	52.5	5.0	(60.2)	(76.1)
EDSL IN Equity	33.1	(1.8)	(12.2)	(49.5)
SUEL IN Equity	8.1	(2.4)	(13.4)	(44.7)
JSP IN Equity	210.5	(2.7)	2.9	(38.4)
BOI IN Equity	211.5	(3.1)	(13.2)	(38.2)

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kotak Institutional Equities

Strategy

Portfolio

INDIA

JULY 22, 2013

UPDATE

BSE-30: 20,150

Naughty thoughts. We raise two uncomfortable issues. First, the strong economic growth of the mid-2000s was perhaps an aberration, driven largely by a wonderful confluence of global liquidity, good and bad policy actions leading to large private investment, and the Government's ability to provide fiscal stimulus. This questions the theory that the current economic woes are cyclical in nature. Second, investors continue to act differently versus their views, perhaps driven by lack of alternatives (among EMs and stocks in India).

Can India fulfill its potential under the current system and way of doing things?

We are not sure. The current conditions do not suggest India can implement fundamental changes that can take it to a higher growth trajectory. Parochial interests across society, a paralyzed political system and mandatory obeisance to socialism appear to hobble entrepreneurship and true capitalism. The Government has implemented some reforms but they may not be enough to address India's deep-seated challenges, especially with looming general elections.

The strong growth of the mid-2000s was an aberration if basic issues remain unaddressed

India's economic growth in the mid-2000s was well above its historical trend growth (see Exhibit 1). As discussed in detail in our June 12, 2013 report, *Blasphemy*, the strong growth in the mid-2000s was driven by a confluence of (1) good and bad policy framework for investment; deregulation of several sectors led to greater private-sector participation (see Exhibit 2) and drove overall economic growth as did robber-baron capitalism in the area of natural resources, (2) large global liquidity and liking for emerging markets; the EMs did not use the capital flows to fix their basic problems but blew up CAD significantly and India was no exception (see Exhibit 3) and (3) large Government-related stimulus in the form of increase in agricultural product prices, subsidies and social welfare spending (see Exhibits 4-6).

Foreigners' preference for India among EMs and expensive stocks among Indian stocks

The oft-repeated argument about a positive inclination to India, and within Indian equities, to expensive defensives is (1) India's better positioning among EMs and (2) lack of alternatives among Indian stocks. Investors may have their own compulsions for staying invested (as they had in December 2007, perhaps) but the thought of India depending on continued foreign interest for portfolio capital flows (see Exhibit 7) in light of (1) a weakening macro-economic environment and (2) faltering interest in a narrow set of frightfully expensive stocks is quite worrisome. India's macro-economic weaknesses (like Mumbai's potholed roads during the monsoons) will be exposed if and when the 'tide' of global liquidity goes out (see our report dated July 16, 2013 titled, *The coming low tide)*. As things stand, India has very little defense against foreign portfolio outflows given its weak external position (see Exhibit 8).

It doesn't have to be this way but...

India would require real reforms to get back to the path of high and sustainable GDP growth seen in the mid-2000s. This would entail (1) stronger democratic institutions, (2) rule-based systems for investment, (3) reforms in all input and output markets, (4) reduction of the Government's role in the economy and privatization of public assets and (5) a greater appreciation of the basic virtues of hard work, frugality, integrity and rule of law. More important, the type of reforms (so-called next generation) required hereon would likely face strong opposition from vested interests; the political system is ill-prepared to meet those challenges.

QUICK NUMBERS

- FY2014E CAD/GDP 4.1% or ~US$80 bn
- FYTD net FII equity inflow US$2.2 bn and debt outflow US$5.3 bn
- Private sector GFCF trended down at 9.7% in FY2012 versus a peak of 14.3% in FY2008

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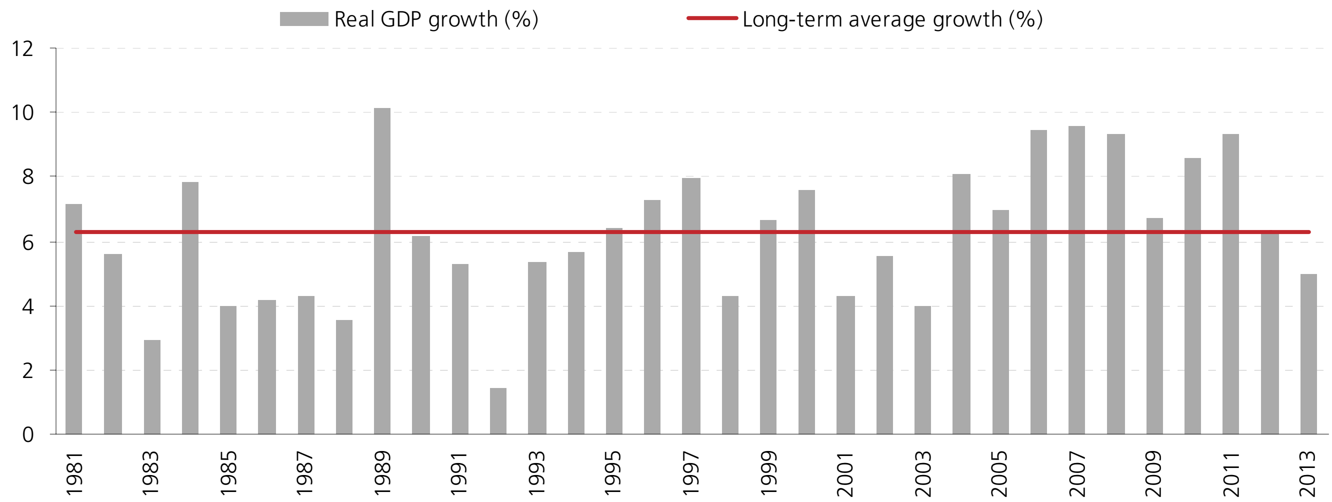
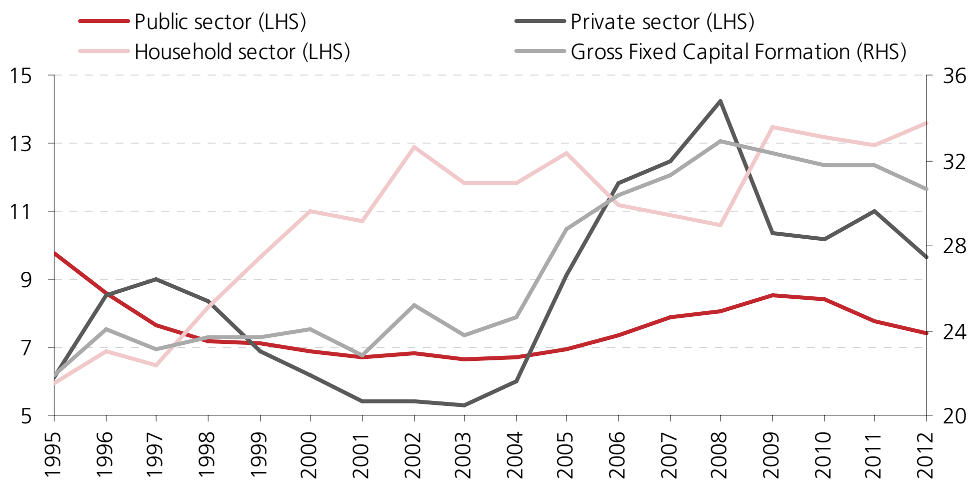
Exhibit 1: India's economic growth in the mid-2000s was well above its historical trend growth
India's GDP growth and long-term average growth, March fiscal year-ends, 1981-2013 (%)



Source: CSO, Kotak Institutional Equities

Exhibit 2: Private-sector investment as a proportion of GDP peaked in FY2008
Sector-wise gross fixed capital formation as a percentage of GDP, March fiscal year-ends, 1995-2012



Source: RBI, Kotak Institutional Equities

Exhibit 3: India's CAD/GDP ratio is overshadowed only by South Africa and Turkey
CAD/GDP ratio of key countries, calendar year-ends, 2005-12 (%)

Country	2005	2006	2007	2008	2009	2010	2011	2012
Brazil	1.6	1.3	0.1	(1.7)	(1.5)	(2.2)	(2.1)	(2.4)
China	5.9	8.5	10.1	9.3	4.9	4.0	1.9	2.3
Greece	(7.6)	(11.3)	(14.6)	(15.0)	(11.2)	(10.4)	(9.9)	(3.5)
India	**(1.2)**	**(1.0)**	**(0.7)**	**(2.5)**	**(1.9)**	**(3.1)**	**(3.2)**	**(5.1)**
Indonesia	0.6	2.7	1.6	0.1	2.0	0.7	0.2	(2.8)
Italy	(1.7)	(2.6)	(2.4)	(2.8)	(1.9)	(3.6)	(3.1)	(0.8)
Korea, Rep.	2.2	1.5	2.1	0.3	3.9	2.9	2.3	3.8
Malaysia	13.9	16.1	15.4	16.8	15.7	11.1	11.0	6.4
Mexico	(0.7)	(0.6)	(1.3)	(1.7)	(0.7)	(0.2)	(0.8)	(0.8)
Philippines	1.9	4.4	4.8	2.1	5.6	4.5	3.2	2.9
Portugal	(10.3)	(10.7)	(10.1)	(12.7)	(11.0)	(10.6)	(7.1)	(1.6)
South Africa	**(3.4)**	**(5.3)**	**(7.0)**	**(7.4)**	**(4.0)**	**(2.8)**	**(3.4)**	**(6.2)**
Spain	(7.4)	(9.0)	(10.0)	(9.7)	(4.8)	(4.5)	(3.7)	(1.1)
Thailand	(4.3)	1.1	6.3	0.8	8.3	3.1	1.7	0.7
Turkey	**(4.4)**	**(6.0)**	**(5.8)**	**(5.5)**	**(2.0)**	**(6.2)**	**(9.7)**	**(6.0)**

Source: IMF, Kotak Institutional Equities

Exhibit 4: There has been a significant boost to rural incomes over the past few years from higher agricultural product prices
Computation showing the changing profile of rural incomes

	Prices			Production (mn tons)			Value (Rs bn)		Change	
	2004	2012	Chg (%)	2004	2012	Chg (%)	2004	2012	(Rs bn)	(%)
Agriculture - important commodities										
Wheat (Rs/qtl)	630	1,285	104	72	94	19	455	1,207	752	165
Paddy-Grade A (Rs/qtl)	590	1,110	88	89	104	8	522	1,158	636	122
Dairy (Rs/lit)	12	25	108	88	122	38	1,057	3,038	1,980	187
Total							**2,034**	**5,402**	**3,368**	**166**

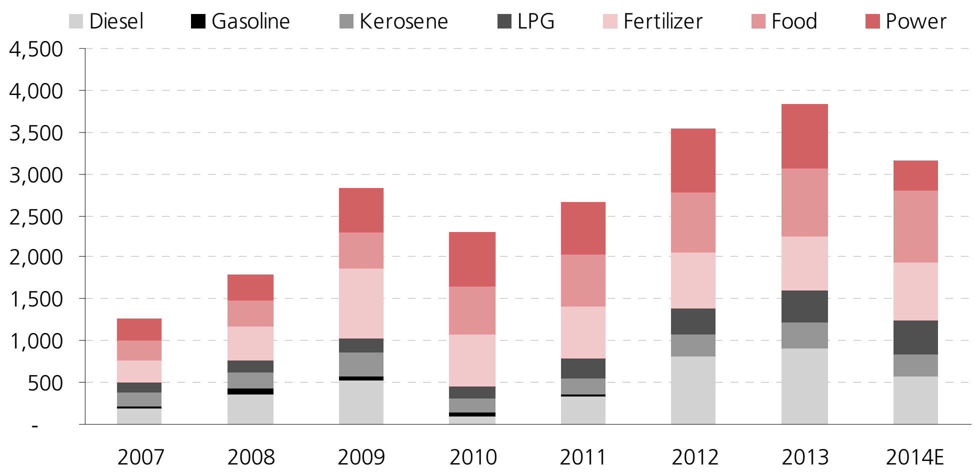
Source: Kotak Institutional Equities estimates

Exhibit 5: Expenditure on social welfare schemes has increased sharply
Budget estimates of flagship programs, March fiscal year-ends, 2006-14 (Rs bn)

	2006	2007	2008	2009	2010	2011	2012	2013	2014	Purpose/Focus
Backward Region Grant Fund	50	50	58	58	58	87	111	105	115	Bridges infrastructure gap in backward districts
Indira Awaas Yojana (IAY)	26	29	40	54	88	100	100	90	152	Offers assistance for construction and upgradation of dwelling units for rural families living below the poverty line
Jawaharlal Nehru National Urban Renewal Mission (JNNURM)	NA	46	55	69	129	53	73	68	140	Urban development
Mahatma Gandhi National Rural Employment Guarantee Scheme (MGNREGS)	NA	113	120	160	391	401	400	330	330	Guarantees a minimum of 100 days of wages for unskilled manual employment to every rural household's adults
Mid-Day Meal Scheme	30	53	73	80	80	94	104	115	132	Provides nutrition and primary education through programmes for children at the primary and upper primary stages
National Rural Health Mission (NRHM)	19	82	99	121	141	157	178	171	212	Develops the health delivery system to provide accessible, affordable and quality health care to the rural population
Pradhan Mantri Gram Sadak Yojana (PMGSY)	NA	NA	61	75	120	195	136	36	112	Provides connectivity to unconnected habitations in rural areas with a population of more than 500 persons
Rajiv Gandhi Grameen Vidyutikaran Yojana (RGGVY)	NA	30	40	55	70	55	60	49	45	Develops rural electricity
Rashtriya Krishi Vikas Yojana (RKVY)	NA	NA	NA	32	41	67	78	84	100	Offers assistance for crop husbandry, water harvesting, watershed management to enhance productivity in farming areas
Sarva Shiksha Abhiyan (SSA)	NA	110	107	131	131	150	210	256	273	Provides access, equity, retention and quality in elementary education
Swarnajayanti Gram Swarozgar Yojana (SGSY)/NRLM/Ajeevika	9	12	18	22	24	30	29	39	40	Promotes self employment of rural poor through capacity building, training and financial assistance through banks
Total planned expenditure	**1,406**	**1,699**	**2,051**	**2,752**	**3,034**	**3,790**	**4,266**	**5,210**	**5,553**	

Source: Budget estimates, Kotak Institutional Equities

Exhibit 6: Subsidies have mounted to more than Rs3 tn
Breakdown of major subsidies by type, March fiscal year-ends, 2007-14E (Rs bn)



Source: GOI, Kotak Institutional Equities estimates

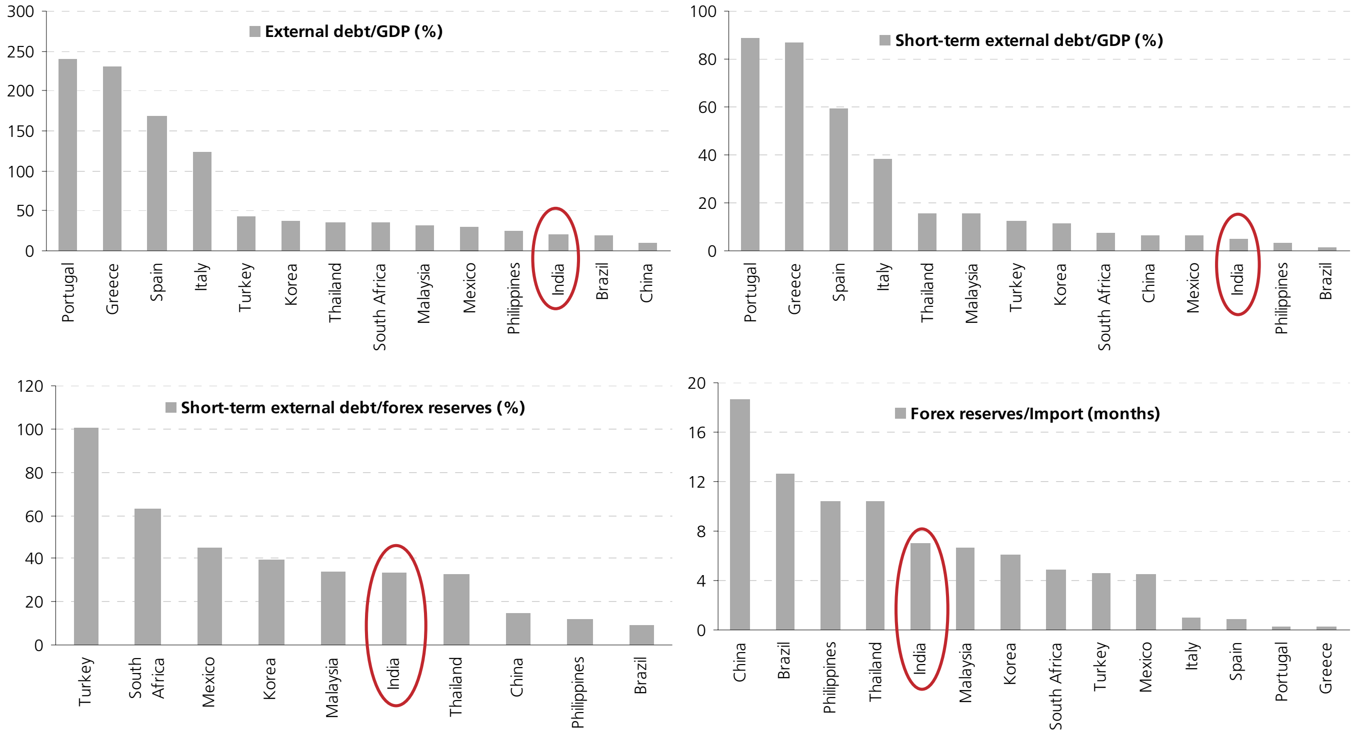
Exhibit 7: Stress on the BOP is expected to continue with wide CAD and volatile capital flows
India's balance of payments, March fiscal year-ends, 2011-14E (US$ bn)

				2014E		
	2011	2012	2013	Oil@100	Oil@105	Oil@110
Current account	**(45.9)**	**(78.2)**	**(88.2)**	**(72.8)**	**(78.5)**	**(84.2)**
GDP	1,708	1,871	1,842	1,927	1,927	1,927
CAD/GDP (%)	**(2.7)**	**(4.2)**	**(4.8)**	**(3.8)**	**(4.1)**	**(4.4)**
Trade balance	(130.6)	(189.8)	(195.7)	(184.4)	(190.1)	(195.8)
Trade balance/GDP (%)	**(7.7)**	**(10.3)**	**(10.6)**	**(9.6)**	**(9.9)**	**(10.2)**
- Exports	250	310	307	308	310	312
- Imports	381	500	502	492	500	507
- oil imports	105	155	170	154	162	169
- non-oil imports	276	345	332	338	338	338
Invisibles (net)	85	112	107	112	112	112
- Services	49	64	65	71	71	71
- software	53	61	64	69	69	69
- non-software	(4.4)	3.1	1.4	2.0	2.0	2.0
- Transfers	53	63	64	65	65	65
- Income (net)	(17.3)	(16.0)	(21.5)	(24.0)	(24.0)	(24.0)
Capital account	**62.1**	**67.8**	**89.4**	**77.0**	**77.0**	**77.0**
Percentage of GDP	3.7	3.7	4.9	4.0	4.0	4.0
Foreign investment	39.7	39.2	46.7	35.0	35.0	35.0
- FDI	**9.4**	**22.1**	**19.8**	**20.0**	**20.0**	**20.0**
- FII	**30.3**	**17.2**	**26.9**	**15.0**	**15.0**	**15.0**
- Equities	**18.9**	**7.1**	**23.3**	—	—	—
- Debt	**10.5**	**9.8**	**4.3**	—	—	—
Banking capital	5.0	16.2	16.6	17.0	17.0	17.0
- NRI deposits	3.2	11.9	14.8	12.0	12.0	12.0
Short-term credit	11.0	6.7	21.7	20.0	20.0	20.0
ECBs	12.5	10.3	8.5	8.0	8.0	8.0
External assistance	4.9	2.3	1.0	2.0	2.0	2.0
Other capital account items	(11.0)	(6.9)	(5.0)	(5.0)	(5.0)	(5.0)
E&O	(3.0)	(2.4)	2.7	0.0	0.0	0.0
Overall balance	**13.1**	**(12.8)**	**3.9**	**4.2**	**(1.5)**	**(7.2)**
Memo items						
Average USD/INR	45.63	47.96	54.41	57.56	57.56	57.56
Average crude (US$/bbl)	85.1	111.7	108.2	100.0	105.0	110.0

Source: RBI, Kotak Institutional Equities estimates

Exhibit 8: India's external debt position is superior to other EM countries

External debt/GDP, short-term debt/GDP, short-term debt/forex reserves and forex reserves/imports of various courtiers, calendar year-end, 2012 (%)



Notes:

(a) Short-term debt is on the basis of original maturity. In most cases, actual short-term debt repayment (within one year) based on residual maturity of debt will be higher.

(b) We have used CY2011 data for China and FY2013 for India.

Source: RBI, World Bank, Kotak Institutional Equities

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Reliance Industries (RIL)

Energy

ADD

JULY 22, 2013

RESULT

Coverage view: Attractive

Price (Rs): 924

Target price (Rs): 980

BSE-30: 20,150

High other income covers up for middling operating performance. RIL reported 1QFY14 net income at ₹53.5 bn (+19.7% yoy, -4.2% qoq), higher versus our estimate of ₹51.3 bn led by higher other income at ₹25.4 bn. However, EBITDA was 4.5% lower versus our estimate. We retain our ADD rating on RIL stock with a revised 12-month forward TP of ₹980 (₹920 previously). We expect RIL to hold up relatively better in case of any correction in the Indian market on macroeconomic concerns.

Company data and valuation summary

Reliance Industries

Stock data			
52-week range (Rs) (high,low)			955-682
Market Cap. (Rs bn)			2,983.1
Shareholding pattern (%)			
Promoters			41.6
FIIs			21.3
MFs			2.0
Price performance (%)	1M	3M	12M
Absolute	11.1	18.2	26.9
Rel. to BSE-30	6.1	11.5	8.8

Forecasts/Valuations	2013	2014E	2015E
EPS (Rs)	65.0	68.1	71.8
EPS growth (%)	6.2	4.7	5.4
P/E (X)	14.2	13.6	12.9
Sales (Rs bn)	3,603.0	4,211.9	4,135.8
Net profits (Rs bn)	210.0	220.0	231.7
EBITDA (Rs bn)	307.9	308.2	344.4
EV/EBITDA (X)	10.1	10.0	8.8
ROE (%)	11.3	10.9	10.5
Div. Yield (%)	0.9	0.9	1.0

9.6% qoq decline in EBITDA led by lower refining margins and decline in oil & gas production

RIL reported net income at ₹53.5 bn (-4.2% qoq and +20% yoy), 4% higher than our estimated ₹51.3 bn led by sharp increase in other income to ₹25.4 bn (+13% qoq and +33% yoy). We note that RIL's other income has contributed 38% of reported PBT in 1QFY14. Reported EBITDA was lower at ₹70.8 bn (-9.6% qoq and +4.9% yoy) versus our estimate of ₹74.1 bn. The qoq decline in EBITDA reflects (1) lower refining margins (-US$1.7/bbl) and (2) lower oil and gas production.

Stable qoq EBIT of petchem segment; lower qoq EBIT from refining and E&P segments

RIL's petchem segment EBIT remained steady qoq at ₹18.9 bn (+7.5% yoy) despite sequential improvement in petchem margins reflecting presumably lower sales volumes. RIL's refining segment EBIT declined 16.2% qoq to ₹29.5 bn led by lower refining margins (-US$1.7/bbl qoq), which was partially offset by higher crude throughput (+6.2%). E&P segment EBIT declined sharply by 24% qoq and 64% yoy to ₹3.5 bn led by lower oil and gas production volumes.

Retain ADD rating on RIL; RIL is relatively better-positioned to withstand an economic downturn

We retain our ADD rating on RIL stock with a revised fair value of ₹980 (₹920 previously). We compute FY2017E EPS (standalone adjusted for treasury shares) at ₹110 assuming (1) full utilization of new projects, (2) reasonable margins for core businesses, (3) revival in gas production and (4) US$9.5/mn BTU gas price. We compute FY2016E fair value of ₹1,100 assuming a mid-cycle ex-growth P/E of 10X without ascribing any value to non-core businesses. (1) Better visibility on new E&P development, (2) timely completion of new projects and (3) value creation in non-core businesses will drive stock performance in the medium term.

Fine-tune earnings

We revise our FY2014-16E EPS to ₹68.1 (-0.1%), ₹71.8 (-0.5%) and ₹71.6 (-0.7%) to reflect (1) 1QFY14 results, (2) lower refining margins and (3) other minor changes. Steady refining margins and moderation of decline in KG D-6 gas production are critical for the company to meet our estimates. However, our exchange rate assumptions provide some buffer.

QUICK NUMBERS

- 9.6% qoq decline in EBITDA; 4.2% qoq decline in net income
- Fair value of ₹1,050 based on FY2015E estimates
- 3% increase in EPS from ₹1/US$ depreciation in exchange rate

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Key highlights of 1QFY14 results

Exhibit 1 compares RIL's 1QFY14 results with 4QFY13 and 1QFY13 results. We discuss key highlights of RIL's 1QFY14 results below; all figures pertain to standalone RIL.

Exhibit 1: Interim results of Reliance Industries, March fiscal year-ends (₹ mn)

	1QFY14	1QFY14E	1QFY13	4QFY13	(% chg.) 1QFY14E	1QFY13	4QFY13	FY2013	FY2012	(% chg.)	FY2014E
Net sales	**876,450**	**992,898**	**918,750**	**841,980**	***(11.7)***	***(4.6)***	***4.1***	**3,602,970**	**3,299,040**	***9.2***	**4,211,946**
Total expenditure	(805,700)	(918,832)	(851,280)	(763,730)	*(12.3)*	*(5.4)*	*5.5*	(3,295,100)	(2,962,850)	*11.2*	(3,903,741)
Inc/(Dec) in stock	7,460	—	9,870	12,890				33,170	8,720		—
Raw materials	(741,210)	(858,018)	(794,980)	(712,040)	*(13.6)*	*(6.8)*	*4.1*	(3,066,290)	(2,762,550)	*11.0*	(3,715,947)
Staff cost	(8,990)	(8,516)	(8,470)	(7,920)	*5.6*	*6.1*	*13.5*	(33,540)	(28,620)	*17.2*	(36,894)
Other expenditure	(62,960)	(52,298)	(57,700)	(56,660)	*20.4*	*9.1*	*11.1*	(228,440)	(180,400)	*26.6*	(150,900)
EBITDA	**70,750**	**74,065**	**67,470**	**78,250**	***(4.5)***	***4.9***	***(9.6)***	**307,870**	**336,190**	***(8.4)***	**308,205**
Other income	25,350	19,695	19,040	22,430	*28.7*	*33.1*	*13.0*	79,980	61,920	*29.2*	87,598
Interest	(8,100)	(7,958)	(7,840)	(7,090)	*1.8*	*3.3*	*14.2*	(30,360)	(26,670)	*13.8*	(29,053)
Depreciation	(21,380)	(21,678)	(24,340)	(22,390)	*(1.4)*	*(12.2)*	*(4.5)*	(94,650)	(113,940)	*(16.9)*	(84,954)
Pretax profits	**66,620**	**64,125**	**54,330**	**71,200**	***3.9***	***22.6***	***(6.4)***	**262,840**	**257,500**	***2.1***	**281,796**
Extraordinaries/sales tax benefit	—	—	—	—				—	—		—
Tax	(13,910)	(12,825)	(10,820)	(14,150)	*8.5*	*28.6*	*(1.7)*	(52,440)	(51,500)	*1.8*	(60,841)
Deferred taxation	810	—	1,220	(1,160)		*(33.6)*	*(169.8)*	(370)	(5,600)	*(93.4)*	(995)
Net income	**53,520**	**51,300**	**44,730**	**55,890**	***4.3***	***19.7***	***(4.2)***	**210,030**	**200,400**	***4.8***	**219,960**
Adjusted profits	**53,520**	**51,300**	**44,730**	**55,890**	***4.3***	***19.7***	***(4.2)***	**210,030**	**200,400**	***4.8***	**219,960**
EPS (Rs)	**16.6**	**15.9**	**13.9**	**17.3**				**65.0**	**61.3**		**68.1**
Income tax rate (%)	19.7	20.0	17.7	21.5				20.1	22.2		21.9
Chemicals production											
Polymer volumes ('000 tons)	1,122		1,101	1,084		*1.9*	*3.5*	4,400	4,462	*(1.4)*	
Polyester volumes ('000 tons)	411		415	390		*(1.0)*	*5.4*	1,628	1,662	*(2.0)*	
Fiber intermediates ('000 tons)	1,086		1,203	1,151		*(9.7)*	*(5.6)*	4,764	4,756	*0.2*	
Refining											
Crude throughput (mn tons)	17.1	17.2	17.3	16.1		*(1.2)*	*6.2*	68.5	67.6	*1.3*	68.5
Refining margin (US$/bbl)	8.4	8.5	7.6	10.1		*10.5*	*(16.8)*	9.2	8.6	*7.0*	8.7
Average exchange rate	56.0	56.0	54.2	54.2		*3.2*	*3.2*	54.4	47.9	*13.5*	57.6
Upstream production											
Crude oil production (000 tons)	123	135	181	138		*(32.0)*	*(11.0)*	631	1,022	*(38.2)*	488
Gas production (bcf)	37	37	72	44		*(48.8)*	*(15.9)*	236	450	*(47.5)*	135
Segment results											
Revenues											
Petrochemicals	219,500		218,390	221,580		*0.5*	*(0.9)*	881,080	806,250	*9.3*	
Refining & marketing	814,580		853,830	778,720		*(4.6)*	*4.6*	3,337,740	2,947,340	*13.2*	
Oil & gas	14,540		25,080	15,970		*(42.0)*	*(9.0)*	82,800	128,980	*(35.8)*	
Others (retail, SEZ, textiles)	6,160		2,480	3,590		*148.4*	*71.6*	9,530	12,130	*(21.4)*	
Gross turnover	1,054,780		1,099,780	1,019,860		*(4.1)*	*3.4*	4,311,150	3,894,700	*10.7*	
Inter segment	148,890		150,520	153,680		*(1.1)*	*(3.1)*	599,960	496,780	*20.8*	
Excise duty	29,440		30,510	24,200		*(3.5)*	*21.7*	108,220	98,880	*9.4*	
Net sales	**876,450**		**918,750**	**841,980**		***(4.6)***	***4.1***	**3,602,970**	**3,299,040**	***9.2***	
Operating costs											
Petrochemicals	200,620		200,830	202,630		*(0.1)*	*(1.0)*	807,800	716,580	*12.7*	
Refining & marketing	785,070		832,320	743,520		*(5.7)*	*5.6*	3,209,860	2,850,800	*12.6*	
Oil & gas	11,020		15,360	11,370		*(28.3)*	*(3.1)*	53,930	76,480	*(29.5)*	
Others (retail, SEZ, textiles)	5,320		2,470	3,110		*115.4*	*71.1*	6,980	11,780	*(40.7)*	
Total	**1,002,030**		**1,050,980**	**960,630**		***(4.7)***	***4.3***	**4,078,570**	**3,655,640**	***11.6***	
EBIT											
Petrochemicals	18,880		17,560	18,950		*7.5*	*(0.4)*	73,280	89,670	*(18.3)*	
Refining & marketing	29,510		21,510	35,200		*37.2*	*(16.2)*	127,880	96,540	*32.5*	
Oil & gas	3,520		9,720	4,600		*(63.8)*	*(23.5)*	28,870	52,500	*(45.0)*	
Others (retail, SEZ, textiles)	840		10	480		*8,300*	*75.0*	2,550	350	*628.6*	
Total	**52,750**		**48,800**	**59,230**		***8.1***	***(10.9)***	**232,580**	**239,060**	***(2.7)***	
Interest expense	(8,100)		(7,840)	(7,090)		*3.3*	*14.2*	(30,360)	(26,670)	*13.8*	
Interest income	16,280		12,910	19,790		*26.1*	*(17.7)*	62,450	44,140	*41.5*	
Other unallocable (net)	5,690		460	(730)				(1,830)	970		
PBT	**66,620**		**54,330**	**71,200**		***22.6***	***(6.4)***	**262,840**	**257,500**	***2.1***	
Current tax	(13,910)		(10,820)	(14,150)		*28.6*	*(1.7)*	(52,440)	(51,500)	*1.8*	
Deferred tax	810		1,220	(1,160)		*(33.6)*	*(169.8)*	(370)	(5,600)	*(93.4)*	
PAT	**53,520**		**44,730**	**55,890**		***19.7***	***(4.2)***	**210,030**	**200,400**	***4.8***	

Source: Company, Kotak Institutional Equities estimates

Exhibit 2: RIL has historically included a portion of other income in segment EBIT numbers
Difference between RIL's segment EBIT and reported EBIT, March fiscal year-ends, 2012-14YTD (₹ mn)

	1QFY12	2QFY12	3QFY12	4QFY12	1QFY13	2QFY13	3QFY13	4QFY13	1QFY14
Segment EBIT									
Petrochemicals	22,150	24,220	21,570	21,740	17,560	17,400	19,370	18,950	18,880
Refining	31,990	30,750	16,850	16,960	21,510	35,230	36,150	35,200	29,510
Oil & gas	14,730	15,310	12,940	9,510	9,720	8,660	5,900	4,600	3,520
Others	80	100	90	70	10	710	770	480	840
Total EBIT (A)	68,950	70,380	51,450	48,280	48,800	62,000	62,190	59,230	52,750
Reported EBIT									
EBITDA (excluding other income)	99,260	98,440	72,850	65,630	67,470	77,770	83,730	78,250	70,750
DD&A	(31,950)	(29,690)	(25,700)	(26,590)	(24,340)	(23,060)	(24,570)	(22,390)	(21,380)
Reported EBIT (B)	67,310	68,750	47,150	39,040	43,130	54,710	59,160	55,860	49,370
Difference (A)-(B)	**1,640**	**1,630**	**4,300**	**9,240**	**5,670**	**7,290**	**3,030**	**3,370**	**3,380**

Source: Company, Kotak Institutional Equities

- Financial highlights

  - **EBITDA and net income.** RIL's 1QFY14 EBITDA declined 9.6% qoq and increased 4.9% yoy to ₹70.8 bn. 1QFY14 net income declined 4.2% qoq and increased 19.7% yoy to ₹53.5 bn. The yoy improvement in EBITDA and net income reflects higher refining margins (+US$0.8/bbl) and weaker Rupee-Dollar exchange rate.

  - **Higher other income.** Other income increased sharply by 13% qoq and 33% yoy to ₹25.4 bn led by (1) profits on sale of investments in fixed income instruments and (2) higher average liquid investments. We note that RIL's cash and cash equivalents increased sharply to ₹931 bn at end-June 2013 versus ₹830 bn at end-March 2013.

  - **Increase in interest expense.** 1QFY14 interest expense increased to ₹8.1 bn compared to ₹7.1 bn in 4QFY13 and ₹7.8 bn in 1QFY13 led by depreciation of the Indian Rupee; gross interest expense including interest capitalized of ₹1.5 bn was ₹9.6 bn. RIL's implied interest rate was 5% in 1QFY14 versus 4.9% in FY2013 and 4.6% in FY2012. Exhibit 3 shows our computation of RIL's implied borrowing cost over the past few quarters.

Exhibit 3: Average borrowing cost of RIL has remained low in the recent years
Implied average borrowing cost, March fiscal year-ends, 2009-14YTD (₹ bn)

	1QFY14	FY2013	4QFY13	3QFY13	2QFY13	1QFY13	FY2012	FY2011	FY2010	FY2009
Interest expense charged to P&L	8.1	30.4	7.1	8.1	7.4	7.8	26.7	23.3	20.0	17.5
Interest capitalized	1.5	3.9	2.2	0.7	0.6	0.4	4.3	4.7	9.8	34.0
Total interest incurred	9.6	34.2	9.3	8.8	7.9	8.2	31.0	28.0	29.8	51.4
Beginning debt	724	683	723	701	732	683	674	625	739	493
Closing debt	803	724	724	723	701	732	683	674	625	739
Average debt	764	703	723	712	716	707	678	649	682	616
Implied average borrowing cost (%)	**5.0**	**4.9**	**5.1**	**4.9**	**4.4**	**4.6**	**4.6**	**4.3**	**4.4**	**8.3**

Source: Company, Kotak Institutional Equities estimates

  - **Lower DD&A charges.** RIL's reported DD&A expense declined to ₹21.4 bn (-4.5% qoq and -12.2% yoy) reflecting lower oil and gas production. RIL has not provided breakdown of depreciation and depletion separately.

- **Lower effective tax rate.** RIL's 1QFY14 effective tax rate was 19.7% compared to 21.5% in 4QFY13 and 17.7% in 1QFY13. We continue to be surprised by lower cash tax rate of 20.9% in 1QFY14 given (1) full taxation of income from petchem segment and the first Jamnagar refinery; other income will also be largely taxed at the corporate tax rate of 33.99% and (2) applicability of MAT rate of 20% on the income from SEZ refinery and E&P segment.

- **Increase in net cash balance.** RIL has reported net cash balance of ₹128 bn at end-June 2013 against net cash balance of ₹105 bn at end-March 2013. The modest increase in net cash balance despite ₹74 bn of gross cash flow generation (net profit + DDA + deferred taxation) presumably reflects capex in core business projects. We note that net addition to fixed assets was higher at ₹105 bn in 1QFY14 led by forex-related capitalization of ₹53 bn.

- **Chemical segment highlights.** 1QFY14 chemical segment EBIT remained steady qoq at ₹18.9 bn (+7.5% yoy) despite sequential improvement in petchem margins reflecting lower sales volumes presumably. RIL's 1QFY14 polymer production volumes increased 1.9% yoy and 3.5% qoq to 1.1 mn tons. Polyester production volumes declined 1% yoy and increased 5.4% qoq to 411,000 tons. As per the company, domestic polymer demand increased 15% yoy and polyester demand increased 10% yoy in 1QFY14.

Exhibit 4: Domestic petchem margins were higher qoq
Asia and domestic petchem margins and prices, March fiscal year-ends, 2012-14YTD

	1QFY12	2QFY12	3QFY12	4QFY12	1QFY13	2QFY13	3QFY13	4QFY13	1QFY14	yoy (% chg)	qoq (% chg)
Global margins (US$/ton)											
HDPE – naphtha	370	422	386	320	437	375	397	464	528	20.9	13.7
LLDPE – naphtha	345	365	298	241	392	370	409	485	525	33.9	8.2
PP – naphtha	610	572	485	344	486	465	464	481	543	11.7	12.9
PVC – naphtha	213	138	17	(24)	93	32	7	58	127	36.6	118.1
PSF – naphtha	1,134	832	804	660	754	642	726	762	753	(0.1)	(1.3)
PFY – naphtha	1,215	1,127	1,113	975	980	855	919	989	1,004	2.4	1.5
PX – naphtha	534	617	568	569	525	509	619	655	560	6.7	(14.4)
Domestic margins (Rs/ton)											
HDPE – naphtha	26,172	27,813	30,112	27,385	35,300	37,482	32,875	34,600	39,242	11.2	13.4
LLDPE – naphtha	26,172	27,813	30,112	27,385	35,300	37,482	32,875	34,600	39,242	11.2	13.4
PP – naphtha	37,445	33,487	33,818	28,092	35,507	38,188	35,682	39,440	42,582	19.9	8.0
PVC – naphtha	10,245	8,887	3,285	192	5,273	9,788	5,515	5,073	10,048	90.5	98.1
PSF – naphtha	53,995	44,970	46,868	40,442	39,190	42,455	41,765	42,990	42,965	9.6	(0.1)
PFY – naphtha	44,702	40,860	40,935	35,732	35,833	40,062	37,465	38,867	41,715	16.4	7.3
Global prices (US$/ton)											
HDPE	1,356	1,372	1,273	1,340	1,332	1,296	1,341	1,427	1,386	4.1	(2.9)
LLDPE	1,331	1,315	1,186	1,261	1,286	1,291	1,353	1,448	1,382	7.4	(4.5)
PP	1,596	1,522	1,372	1,363	1,381	1,387	1,408	1,443	1,400	1.4	(3.0)
PVC	1,199	1,088	904	996	988	954	951	1,021	985	(0.3)	(3.6)
PSF	2,120	1,782	1,692	1,680	1,648	1,563	1,670	1,725	1,610	(2.3)	(6.7)
PFY	2,202	2,077	2,000	1,995	1,875	1,777	1,863	1,952	1,862	(0.7)	(4.6)
PX	1,520	1,567	1,456	1,589	1,419	1,430	1,563	1,617	1,418	(0.1)	(12.4)
Domestic prices (Rs/ton)											
HDPE	76,593	76,260	80,327	83,360	91,860	91,193	89,360	93,027	92,527	0.7	(0.5)
LLDPE	76,593	76,260	80,327	83,360	91,860	91,193	89,360	93,027	92,527	0.7	(0.5)
PP	87,867	81,933	84,033	84,067	92,067	91,900	92,167	97,867	95,867	4.1	(2.0)
PVC	60,667	57,333	53,500	56,167	61,833	63,500	62,000	63,500	63,333	2.4	(0.3)
PSF	104,417	93,417	97,083	96,417	95,750	96,167	98,250	101,417	96,250	0.5	(5.1)
PFY	95,123	89,307	91,150	91,707	92,393	93,773	93,950	97,293	95,000	2.8	(2.4)

Source: Platt's, Bloomberg, Kotak Institutional Equities

- **Refining segment highlights.** 1QFY14 refining segment EBIT declined 16.2% qoq to ₹29.5 bn reflecting lower refining margins, which was partially offset by sequentially higher crude throughput. The company reported lower refining margins qoq at US$8.4/bbl (+US$0.8/bbl yoy and -US$1.7/bbl qoq), marginally lower than our estimate of US$8.5/bbl. Crude throughput increased sequentially to 17.1 mn tons in 1QFY14 versus 16.1 mn tons in 4QFY13 and 17.3 mn tons in 1QFY13.

- **E&P segment highlights.** 1QFY14 E&P segment EBIT declined 24% qoq and 64% yoy to ₹3.5 bn led by lower oil and gas production. KG D-6 gas volume (gross basis) was 15.3 mcm/d in 1QFY14 versus 19.2 mcm/d in 4QFY13 and 32.2 mcm/d in 1QFY13. Oil and condensate production from MA-1 field declined to 6.5 kb/d in 1QFY14 versus 7.3 kb/d in 4QFY13 and 11.4 kb/d in 1QFY13. Oil production (gross basis) from Panna-Mukta fields declined 19% yoy to 1.8 mn bbls in 1QFY14; gas production declined 5% yoy to 16.9 bcf. 1QFY14 condensate production (gross basis) from Tapti field declined by 53% yoy to 0.07 mn bbls and gas production declined 43% yoy to 7.8 bcf. The sharp decline in production from PMT fields reflects (1) natural decline in reserves and (2) shutdown of Panna-Mukta field for three days.

Other updates

- **Domestic E&P business.** RIL is planning to augment production from the existing D1-D3 fields by installing a booster compressor, which is expected to complete by 4QFY15. RIL is also planning to initiate appraisal program in the recently discovered MJ-1 field by 2HFY14, subject to necessary approvals.

  We note that RIL has relinquished three exploration blocks, which were awarded during NELP-VI regime. The company's domestic portfolio consists of KG D-6 block, PMT fields and seven exploration blocks (see Exhibit 5).

Exhibit 5: Details of RIL's blocks in India

Block	Consortium	RIL stake (%)	Comments
Producing blocks			
KG-DWN-98/3	Reliance, Niko, BP	60	
PMT fields	Reliance, BG, ONGC	30	
Exploratory blocks			
NEC-OSN-97/2	Reliance, Niko, BP	60	Recoverable gas reserves of 1.185 tcf
GS-OSN-2000/1	Reliance, Hardy	90	Gas discovery (D-33)
CY-DWN-2001/2	Reliance, BP	70	Gross reserves of 719 bcf; recoverable reserves of 447 bcf
CY-PR-DWN-2001/3	Reliance, BP	70	Gas discovery (D-53)
KG-DWN-2003/1	Reliance, Hardy, BP	60	Gas initial in place of 195 bcf; estimated ultimate recovery of 94 bcf
CB-ONN-2003/1	Reliance, BP	70	Oil initial in place of 15.04 mn bbls; recoverable reserves of 2.05 mn bbls
KG-DWN-2005/2	Reliance, BP	50	

Source: Indian Petro, Company, Kotak Institutional Equities

- **Retail business.** RIL's retail business has reported revenues of ₹34.7 bn and EBITDA of ₹700 mn in 1QFY14. The company has added 45 stores in 1QFY14, increasing the overall store count to 1,511 as of June 30, 2013. Exhibit 6 shows key operating and financial metrics of retail business as disclosed by RIL over the past few years.

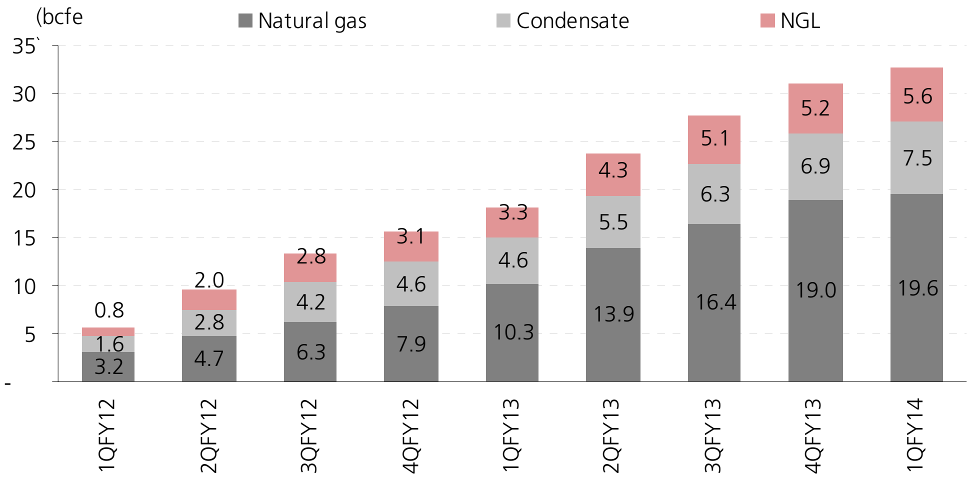
Exhibit 6: RIL has reported robust growth in revenues from retail operations
Key operating metrics and financials for RIL's retail operations, March fiscal year-ends, 2011-14YTD (₹ bn)

	2011	2012	2013	1QFY14
Operating metrics				
Store category				
Brands		49	68	82
Jewellery		37	51	54
Fashion & lifestyle		353	448	455
Digital		93	139	151
Value and others		750	760	769
Total stores	**1,090**	**1,282**	**1,466**	**1,511**
Area (mn sq. ft)	**NA**	**6.5**	**9.0**	**9.4**
Revenue break-up				
Brands	1	1	2	1
Jewellery	3	5	8	4
Fashion & lifestyle	8	11	16	4
Digital	7	12	21	7
Value and others	42	46	61	19
Financials				
Revenue	**61**	**76**	**108**	**35**
EBITDA	NA	(3.4)	0.8	0.7
Net profit	**(5.0)**	**(4.5)**	**(2.7)**	**NA**

Source: Company, Kotak Institutional Equities

- **Shale gas.** RIL reported higher revenues at US$214 mn (+84% yoy and 11% qoq) and EBITDA at US$165 mn (+74% yoy and 6% qoq) from the shale gas business in 1QFY14. RIL's share of gross production volumes increased modestly by 4% qoq to 37.7 bcf (+71% yoy). The slower qoq production growth reflects (1) higher maintenance-related shutdowns and (2) flooding-related delays in Pioneer JV. The company invested US$331 mn in 1QFY14; cumulative investments across shale gas JVs stand at US$6 bn as of end-1QFY14. Exhibit 7 shows RIL's net sales volumes of shale gas and related hydrocarbon since 1QFY12.

Exhibit 7: RIL has reported a rather robust growth in sales volumes from its shale gas operations
Quarterly net sales volumes, March fiscal year-ends, 2012-14YTD (bcfe)



Source: Company, Kotak Institutional Equities

Key assumptions behind earnings model

We discuss the key assumptions behind our earnings model below.

- **Refining margins.** We model FY2014E, FY2015E and FY2016E refining margins at US$8.7/bbl, US$8.6/bbl and US$8.7/bbl versus US$9.2/bbl in FY2013 (see Exhibit 8). We assume flat margins in the medium term given a significant increase in refining capacity, which will offset the incremental oil demand in CY2013-15E. Current and FYTD14 benchmark margins are lower than FY2013 margins.

Exhibit 8: Major assumptions for RIL's refining segment, March fiscal year-ends, 2008-16E (US$/bbl)

	2008	2009	2010	2011	2012	2013	2014E	2015E	2016E
RIL refinery									
Rupee-dollar exchange rate	40.3	45.8	47.4	45.6	47.9	54.4	57.6	57.8	56.5
Import tariff on crude (%)	2.4	1.3	1.1	5.4	1.7	0.5	0.5	0.5	0.5
Refinery yield (per bbl of crude throughput)	98.1	104.8	82.1	96.0	128.3	128.4	122.1	116.3	110.7
Cost of inputs (per bbl of crude throughput)	83.1	92.6	75.7	88.4	121.5	120.4	114.4	108.5	102.7
Net refining margin	**15.0**	**12.2**	**6.4**	**7.6**	**6.8**	**8.0**	**7.7**	**7.8**	**8.0**
Crude throughput (mn tons)	31.8	32.0	34.5	34.5	35.2	35.3	35.3	35.3	35.3
Fuel and loss-own fuel used (%)	8.0	8.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0
Fuel & loss equivalent-gas used (%)			2.0	2.0	2.0	2.0	2.0	2.0	2.0
SEZ refinery									
Import tariff on crude (%)			—	0.6	0.7	0.6	0.6	0.6	0.6
Refinery yield (per bbl of crude throughput)			71.1	91.9	129.8	129.5	122.8	116.6	110.7
Cost of inputs (per bbl of crude throughput)			64.2	82.7	119.3	119.1	113.1	107.2	101.3
Net refining margin			**7.0**	**9.2**	**10.5**	**10.4**	**9.7**	**9.5**	**9.4**
Crude throughput (mn tons)			26.4	32.1	32.4	33.2	33.2	33.2	33.2
Fuel and loss-own fuel used (%)			6.5	6.5	6.5	6.5	6.5	6.5	6.5
Fuel & loss equivalent-gas used (%)			2.0	2.0	2.0	2.0	2.0	2.0	2.0
Blended refining margin (US$/bbl)			**6.6**	**8.4**	**8.6**	**9.2**	**8.7**	**8.6**	**8.7**
Total crude throughput (mn tons)			**60.9**	**66.6**	**67.6**	**68.5**	**68.5**	**68.5**	**68.5**

Notes:
(a) Refining margins do not include sales tax incentives.

Source: Kotak Institutional Equities estimates

Exhibit 9: We expect 4.1 mn b/d of net addition to global refining capacity in CY2013-15E
World refinery capacity additions (net), calendar year-ends, 2007-15E ('000 b/d)

	2007	2008	2009	2010	2011	2012	2013E	2014E	2015E
OECD North America	240	—	(124)	(211)	164	63	280	—	50
OECD Europe	—	30	(270)	(121)	(89)	(418)	(234)	—	—
OECD Pacific	—	—	(57)	(17)	—	(85)	(110)	(448)	—
FSU	—	84	—	140	—	43	39	44	48
Non-OECD Europe	—	—	—	(70)	—	—	—	30	—
China	—	206	446	560	266	380	680	170	1,100
Other Asia	315	65	790	229	140	480	0	420	—
Latin America	—	—	(235)	50	85	(585)	135	158	280
Middle East	77	226	179	70	95	70	120	1,217	—
Africa	—	6	6	—	60	—	60	28	—
Total World	**632**	**616**	**735**	**630**	**721**	**(52)**	**970**	**1,619**	**1,478**

Source: OGJ, Downstream, Kotak Institutional Equities estimates

Exhibit 10: We see risks to IEA's estimated growth of 3.4 mn b/d in oil demand for CY2013-15E
Estimated global crude demand, supply and prices, calendar year-ends, 2008-15E

	2008	2009	2010	2011	2012	2013E	2014E	2015E
Demand (mn b/d)								
Total demand	**86.5**	**85.5**	**88.3**	**88.9**	**89.9**	**90.8**	**92.0**	**93.3**
Yoy growth	(0.5)	(1.0)	2.8	0.6	1.0	**0.9**	**1.2**	1.3
Supply (mn b/d)								
Non-OPEC	50.6	51.5	52.7	52.8	53.4	**54.6**	**55.9**	57.0
Yoy growth	(0.1)	0.9	1.2	0.1	0.6	1.2	1.3	1.1
OPEC								
Crude	31.6	29.2	29.3	29.9	31.3	29.6	29.3	29.4
NGLs	4.5	4.9	5.6	5.9	6.3	6.6	6.7	6.9
Total OPEC	36.2	34.1	34.9	35.8	37.7	36.2	36.1	36.3
Total supply	**86.8**	**85.6**	**87.6**	**88.6**	**91.1**	**90.8**	**92.0**	**93.3**
Total stock change	0.0	0.0	(0.8)	(0.5)	1.2			
OPEC crude capacity	34.2	34.9	35.7	34.2	35.0	35.4	36.3	36.4
Implied OPEC spare capacity	**2.5**	**5.7**	**5.6**	**3.8**	**4.9**	**5.8**	**7.0**	**7.0**
Demand growth (yoy, %)	(0.6)	(1.1)	3.3	0.7	1.1	1.0	1.3	1.4
Supply growth (yoy, %)								
Non-OPEC	(0.3)	1.8	2.3	0.2	1.1	2.2	2.4	2.0
OPEC	3.3	(5.8)	2.4	2.6	5.2	(4.0)	(0.2)	0.6
Total	1.2	(1.3)	2.4	1.1	2.8	(0.3)	1.3	1.4
Dated Brent (US$/bbl)	**102**	**62**	**80**	**111**	**112**	**107**	**101**	**96**
World GDP growth (%)	**2.8**	**(0.6)**	**5.3**	**3.7**	**3.1**	**3.1**	**3.8**	**4.1**

Source: IEA, Kotak Institutional Equities estimates

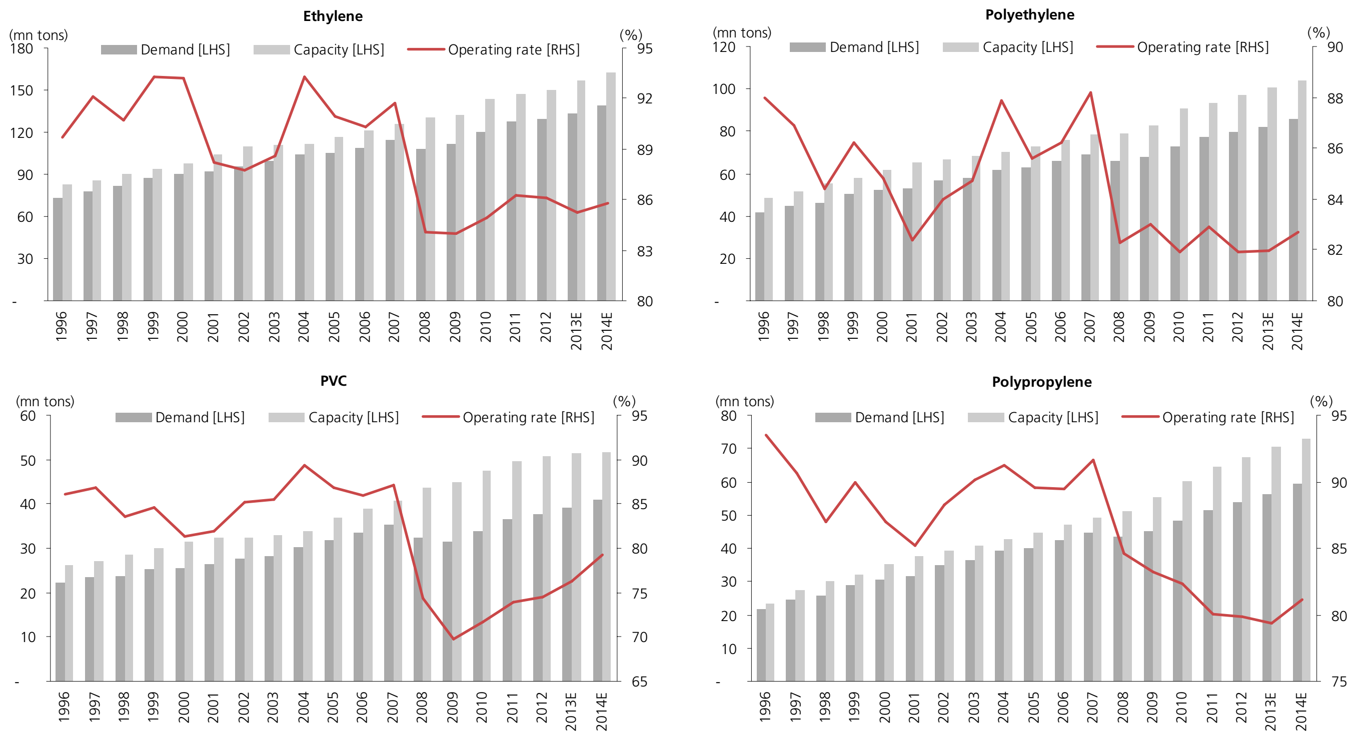
- **Chemical margins.** Exhibit 11 shows our major assumptions for RIL's chemical prices and margins. We model higher chemical margins, to increase moderately in FY2014-16E reflecting gradual improvement in global operating rates and likely recovery in downstream demand.

Exhibit 11: Key chemical prices and margins assumptions, March fiscal year-ends, 2008-16E (US$/ton)

	2008	2009	2010	2011	2012	2013	2014E	2015E	2016E
Chemical prices									
LDPE	1,600	1,400	1,500	1,555	1,650	1,485	1,460	1,445	1,430
LLDPE	1,575	1,330	1,400	1,455	1,525	1,570	1,545	1,530	1,515
HDPE	1,500	1,275	1,375	1,415	1,550	1,560	1,540	1,525	1,510
Polypropylene	1,470	1,300	1,360	1,525	1,635	1,585	1,575	1,560	1,545
PVC	1,100	925	1,000	1,075	1,100	1,050	1,025	1,010	995
PFY	1,550	1,485	1,380	1,640	1,790	1,615	1,605	1,620	1,605
PSF	1,475	1,320	1,310	1,660	1,910	1,675	1,655	1,670	1,655
Paraxylene	1,200	1,085	1,050	1,125	1,550	1,520	1,510	1,460	1,410
Chemical margins									
LLDPE—naphtha	**850**	**655**	**770**	**725**	**590**	**645**	**655**	**675**	**695**
HDPE—naphtha	775	600	745	685	615	635	650	670	690
PP—naphtha	**745**	**625**	**730**	**795**	**700**	**660**	**685**	**705**	**725**
PVC—1.025 x (0.235 x ethylene + 0.864 x EDC)	396	401	389	367	383	414	395	402	405
POY—naphtha	**825**	**810**	**750**	**910**	**855**	**690**	**715**	**765**	**785**
PSF—naphtha	750	645	680	930	975	750	765	815	835
PX—naphtha	**475**	**410**	**420**	**395**	**615**	**595**	**620**	**605**	**590**
POY—0.85 x PTA—0.34 x MEG	364	496	341	437	349	333	349	382	384
PSF—0.85 x PTA—0.34 x MEG	**289**	**331**	**271**	**457**	**469**	**393**	**399**	**432**	**434**
PTA—0.67 x PX	121	133	217	281	187	72	58	77	95

Source: Kotak Institutional Equities estimates

Exhibit 12: Global operating rates for key chemical products are expected to improve in CY2013-14E
World demand and capacity (mn tons), operating rate (%), 1996-2014E



Source: CMAI, Kotak Institutional Equities estimates

- **E&P segment.** We model FY2014-16E KG D-6 gas production at 13.5 mcm/d, 12 mcm/d and 12 mcm/d. We have assumed gas price of US$8.5/mn BTU for FY2015, US$9/mn BTU for FY2016, US$9.5/mn BTU for FY2017 and US$10/mn BTU from FY2018 onwards.

- **Other income.** We expect RIL's other income to remain strong over the next few years driven by significant cash pile. We expect RIL to generate ₹259 bn of free cash flow in FY2014-16E. The quantum of other income will depend on (1) RIL's dividend policy; RIL has followed a conservative dividend pay-out policy historically, (2) acquisitions and (3) capex, which would depend on schedule of ongoing petrochemical projects and new E&P discoveries.

- **Taxation.** We model effective tax rate at 21.9%, 26.7% and 26.7% for FY2014E, FY2015E and FY2016E versus 20.1% in FY2013 and 22.2% in FY2012. We assume that RIL will continue to avail of income tax exemption on gas production from KG D-6 block and prepare our forecasts accordingly. However, in case the income tax exemption is not available, we compute RIL's FY2015E EPS to drop by 2.3% to ₹70.

- **Exchange rate.** We assume Rupee-Dollar exchange rate for FY2014E, FY2015E and FY2016E at ₹57.56/US$, ₹57.75/US$ and ₹56.5/US$.

Exhibit 13 gives sensitivity of RIL's earnings to various key variables. Exhibits 14 & 15 give our SOTP-based valuation of RIL for FY2014E and FY2015E while Exhibit 16 is our summary financial statement for RIL. We have increased our target EV/EBITDA multiple for the chemical and refining segments to 6.5X from 6X previously to factor in potentially higher earnings from a weaker-than-expected exchange rate. The Rupee is currently trading at significantly lower levels versus our assumptions for FY2014-16E. More important, (1) India's weak CAD/BOP position and (2) elevated concerns about tighter global liquidity may result in the INR being significantly weaker versus our current estimates.

Exhibit 13: Reliance's earnings have high leverage to refining margins
Sensitivity of RIL's earnings to key variables

	Fiscal 2014E			Fiscal 2015E			Fiscal 2016E		
	Downside	Base case	Upside	Downside	Base case	Upside	Downside	Base case	Upside
Rupee-dollar exchange rate									
Rupee-dollar exchange rate	56.6	57.6	58.6	56.8	57.8	58.8	55.5	56.5	57.5
Net profits (Rs mn)	213,659	219,960	226,260	225,368	231,730	238,092	224,513	231,133	237,754
EPS (Rs)	66.2	68.1	70.1	69.8	71.8	73.7	69.5	71.6	73.6
% upside/(downside)	**(2.9)**		**2.9**	**(2.7)**		**2.7**	**(2.9)**		**2.9**
Chemical prices									
Change in prices (%)	(5.0)		5.0	(5.0)		5.0	(5.0)		5.0
Net profits (Rs mn)	212,519	219,960	227,400	222,929	231,730	240,531	221,943	231,133	240,324
EPS (Rs)	65.8	68.1	70.4	69.0	71.8	74.5	68.7	71.6	74.4
% upside/(downside)	**(3.4)**		**3.4**	**(3.8)**		**3.8**	**(4.0)**		**4.0**
Blended refining margins									
Margins (US$/bbl)	7.7	8.7	9.7	7.6	8.6	9.6	7.7	8.7	9.7
Net profits (Rs mn)	196,146	219,960	243,786	210,196	231,730	253,252	210,076	231,133	252,177
EPS (Rs)	60.7	68.1	75.5	65.1	71.8	78.4	65.1	71.6	78.1
% upside/(downside)	**(10.8)**		**10.8**	**(9.3)**		**9.3**	**(9.1)**		**9.1**
Natural gas price									
Natural gas price (US$/bbl)		4.2	5.2	7.5	8.5	9.5	8.0	9.0	10.0
Net profits (Rs mn)		219,960	224,434	227,584	231,730	235,912	227,032	231,133	235,269
EPS (Rs)		68.1	69.5	70.5	71.8	73.1	70.3	71.6	72.9
% upside/(downside)			**2.0**	**(1.8)**		**1.8**	**(1.8)**		**1.8**

Source: Kotak Institutional Equities estimates

Exhibit 14: SOTP valuation of Reliance is ₹910 per share on FY2014E estimates
Sum-of-the-parts valuation of Reliance Industries, FY2014E basis (₹)

	Valuation base (Rs bn)		Multiple (X)		EV	Valuation
	Other	EBITDA	Multiple	EV/EBITDA	(Rs bn)	(Rs/share)
Chemicals		107		6.5	698	238
Refining & Marketing		171		6.5	1,109	378
Oil and gas—PMT		23		2.5	57	19
Gas—producing and developing (DCF-based) (a)	327				327	111
KG D-6	279				279	95
NEC-25	48				48	16
Oil—KG-DWN-98/3 (b)	10				10	4
Investments excluding subsidiaries	355				355	121
Retailing	63		0.8		50	17
Shale gas	54		0.8		41	14
Telecom	74		0.8		56	19
Capital WIP (book value)	176		1.0		176	60
Total enterprise value					**2,878**	**980**
Net debt					206	70
Implied equity value					**2,672**	**910**

Notes:
(a) We value KG D-6 and NEC-25 blocks on DCF.
(b) 20 mn bbls of recoverable reserves.
(c) Capital WIP includes capex on petrochemical expansion and petcoke gasification projects.
(d) We use 2.936 bn shares (excluding treasury shares) for per share computations.

Source: Kotak Institutional Equities estimates

Exhibit 15: SOTP valuation of Reliance is ₹1,050 per share on FY2015E estimates
Sum-of-the-parts valuation of Reliance Industries, FY2015E basis (₹)

	Valuation base (Rs bn)		Multiple (X)		EV	Valuation
	Other	EBITDA	Multiple	EV/EBITDA	(Rs bn)	(Rs/share)
Chemicals		132		6.5	857	292
Refining & Marketing		168		6.5	1,093	372
Oil and gas—PMT		21		2.5	53	18
Gas—producing and developing (DCF-based) (a)	366				366	125
KG D-6	309				309	105
NEC-25	56				56	19
Oil—KG-DWN-98/3 (b)	10				10	4
Investments excluding subsidiaries	355				355	121
Retailing	63		0.8		50	17
Shale gas	54		0.8		41	14
Telecom	74		0.8		56	19
Capital WIP (book value)	339		1.0		339	116
Total enterprise value					**3,220**	**1,097**
Net debt					129	44
Implied equity value					**3,091**	**1,053**

Notes:
(a) We value KG D-6 and NEC-25 blocks on DCF.
(b) 20 mn bbls of recoverable reserves.
(c) Capital WIP includes capex on petrochemical expansion and petcoke gasification projects.
(d) We use 2.936 bn shares (excluding treasury shares) for per share computations.

Source: Kotak Institutional Equities estimates

Exhibit 16: RIL: Profit model, balance sheet, cash model, March fiscal year-ends, 2010-17E (₹ mn)

	2010	2011	2012	2013	2014E	2015E	2016E	2017E
Profit model (Rs mn)								
Net sales	1,924,610	2,481,700	3,299,040	3,602,970	4,211,946	4,135,829	3,934,907	3,852,288
EBITDA	**305,807**	**381,257**	**336,190**	**307,870**	**308,205**	**344,359**	**337,672**	**519,676**
Other income	24,605	30,517	61,920	79,980	87,598	81,555	79,441	87,058
Interest	(19,972)	(23,276)	(26,670)	(30,360)	(29,053)	(20,753)	(11,465)	(17,855)
Depreciation & depletion	(104,965)	(136,076)	(113,940)	(94,650)	(84,954)	(89,162)	(90,241)	(128,313)
Pretax profits	205,474	252,422	257,500	262,840	281,796	315,999	315,408	460,566
Extraordinary items	—	—	—	—	—	—	—	—
Tax	(31,118)	(43,204)	(51,500)	(52,440)	(60,841)	(80,005)	(82,600)	(115,679)
Deferred taxation	(12,000)	(6,355)	(5,600)	(370)	(995)	(4,264)	(1,675)	(27,751)
Net profits	162,357	202,863	200,400	210,030	219,960	231,730	231,133	317,136
Adjusted net profits	**162,357**	**202,863**	**200,400**	**210,030**	**219,960**	**231,730**	**231,133**	**317,136**
Earnings per share (Rs)	**49.6**	**62.0**	**61.3**	**65.0**	**68.1**	**71.8**	**71.6**	**98.2**
Balance sheet (Rs mn)								
Total equity	1,371,706	1,515,403	1,660,960	1,800,200	1,988,985	2,186,353	2,381,407	2,647,001
Deferred taxation liability	109,263	115,618	121,220	121,930	122,925	127,189	128,863	156,614
Total borrowings	624,947	673,967	684,470	724,270	561,322	500,861	400,035	268,055
Currrent liabilities	404,148	542,206	484,750	538,710	620,673	604,715	575,439	546,916
Total liabilities and equity	**2,510,064**	**2,847,194**	**2,951,400**	**3,185,110**	**3,293,904**	**3,419,119**	**3,485,745**	**3,618,586**
Cash	134,627	271,349	395,980	495,470	355,334	371,519	311,975	527,767
Current assets	489,165	644,070	800,570	875,910	984,386	979,693	948,499	918,383
Total fixed assets	1,653,987	1,555,260	1,214,770	1,288,640	1,429,095	1,542,817	1,700,182	1,647,346
Investments	232,286	376,515	540,080	525,090	525,090	525,090	525,090	525,090
Total assets	**2,510,064**	**2,847,194**	**2,951,400**	**3,185,110**	**3,293,904**	**3,419,119**	**3,485,745**	**3,618,586**
Free cash flow (Rs mn)								
Operating cash flow, excl. working capital	222,605	304,310	265,810	237,080	212,532	234,987	229,693	384,427
Working capital	(53,015)	695	(27,700)	57,820	(26,513)	(11,265)	1,918	1,592
Capital expenditure	(219,427)	(123,661)	(80,080)	(159,440)	(198,298)	(194,270)	(238,308)	(73,763)
Investments	14,206	(195,439)	(201,760)	(54,140)	—	—	—	—
Other income	22,043	23,316	18,930	65,280	87,598	81,555	79,441	87,058
Free cash flow	**(13,587)**	**9,220**	**(24,800)**	**146,600**	**75,319**	**111,007**	**72,745**	**399,315**
Ratios (%)								
Debt/equity	42.2	41.3	38.4	37.7	26.6	21.6	15.9	9.6
Net debt/equity	33.1	24.7	16.2	11.9	9.8	5.6	3.5	(9.3)
RoAE	11.8	13.1	11.6	11.1	10.6	10.2	9.4	11.7
RoACE	**8.6**	**10.1**	**9.2**	**9.0**	**8.9**	**8.8**	**8.2**	**10.8**
Adjusted ROACE	**12.3**	**12.5**	**11.6**	**11.8**	**11.6**	**12.1**	**12.2**	**16.1**

Source: Company, Kotak Institutional Equities estimates

kotak Institutional Equities

HDFC (HDFC)

Banks/Financial Institutions

REDUCE

JULY 22, 2013

RESULT

Coverage view: Cautious

Price (Rs): 803

Target price (Rs): 790

BSE-30: 20,150

1QFY14 performance on track. HDFC's strong core performance during 1QFY14 was characterized by healthy retail loan growth and lower bond yields (during the quarter). We continue to expect HDFC to deliver 20% loan growth over the medium term. However, current challenges in the bulk borrowing markets pose risks on the liability-side of NBFCs. Hence, despite the recent correction in stock price, we retain REDUCE rating on HDFC with price target of Rs790. We await better entry points and more clarity on liquidity in the system.

Company data and valuation summary

HDFC

Stock data			
52-week range (Rs) (high,low)			931-631
Market Cap. (Rs bn)			1,248.3
Shareholding pattern (%)			
Promoters			0.0
FIIs			73.7
MFs			2.6
Price performance (%)	**1M**	**3M**	**12M**
Absolute	(4.7)	(1.8)	15.8
Rel. to BSE-30	(9.0)	(7.4)	(0.7)

Forecasts/Valuations	2013	2014E	2015E
EPS (Rs)	31.4	37.4	43.9
EPS growth (%)	12.3	19.3	17.4
P/E (X)	25.6	21.5	18.3
NII (Rs bn)	61.8	75.3	88.5
Net profits (Rs bn)	48.5	57.8	67.9
BVPS	161.7	181.6	205.1
P/B (X)	5.0	4.4	3.9
ROE (%)	22.0	21.8	22.7
Div. Yield (%)	1.6	1.9	2.2

Earnings up 17%

HDFC reported PAT of Rs11.7 bn, up 17% yoy and 3% below estimates. Core PBT (PBT before capital gains and adjustment of interest of zero coupon bonds) was up 23% yoy and 2% below estimates. Net operational income was up 16% at Rs17.9 bn, 2% below estimates. Marginally lower NIM and loan growth were the key reasons for lower-than-expected earnings.

We expect HDFC to deliver 19-20% growth over the next three years (no change in estimates). We value the core mortgage business at 3.6X PBR for 27-30% ROE in the medium term. The core business drives 60% value in our SOTP, the balance (30%) being from HDFC Bank (valued at our target price, i.e. 3.5X PBR) and 10% from insurance and asset management businesses.

Retail business holds up, non-retail loans flat qoq

HDFC's loan growth (including loans sold to banks) was stable at 20% yoy. The retail business was in a sweet spot with 24% yoy (6% qoq) loan growth; its non-retail loan book was flat qoq. Overall disbursements and approvals were up 16% yoy. Decline in marginal borrowing cost by about 1% qoq (in the bond markets) made the retail lending segment more profitable for HDFC. Higher competitive intensity in lending to developers likely kept HDFC away from the non-retail segment during the quarter. HDFC will likely resume focus on this segment as constraints on liquidity in the system will result in higher interest rates for developers. We continue to model 19-21% loan growth for HDFC over the next three years.

Reported spreads stable, liability-side management crucial in the current environment

HDFC's NIM (calculated) declined to 3.4% in 1QFY14 from 4.3% in 4QFY13—this is in line with its seasonal trends. We note that HDFC's bond borrowings have increased by 9% qoq during 1QFY14; marginal bond borrowings during the quarter were about 7% of its total outstanding borrowings. Notably, the marginal borrowing cost on bonds raised during the quarter was down by about 100 bps as compared to FY2013 levels (though bond yields have moved back again). Reported overall spreads are stable at 2.3%. Spread in the retail business increased marginally to 2% from 1.95%.

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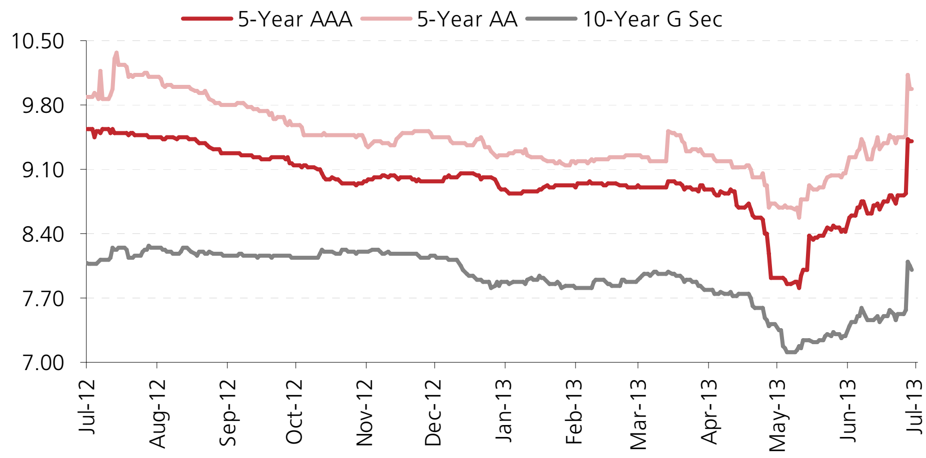
We believe that effective liability-side management is crucial in the current environment of deficit liquidity, especially in light of large balance sheet of HDFC. Improvement in liquidity conditions will clearly provide more comfort to investors of NBFCs.

In the past, HDFC has effectively managed such periods (when liquidity is a challenge). We believe that HDFC can focus on retail deposits or bank loans if bond yields are elevated. The share of bank loans has declined to 8% of HDFC's total borrowings in 1QFY14 from 26% in 1QFY13, providing some headroom for the company. Incremental bank loans will, however, be constrained by base rate (about 10%, i.e. 50 bps over current 5-year AAA bond yields).

Higher dividend income, no capital gains

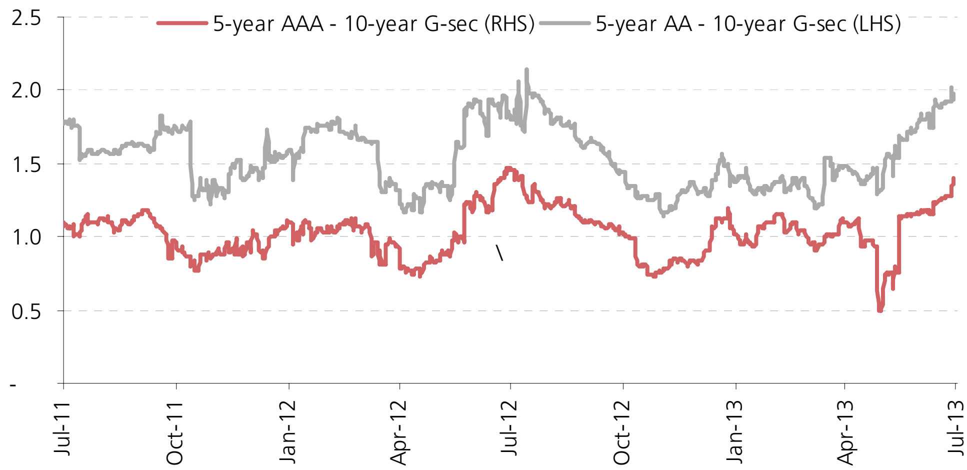
HDFC reported dividend income of Rs2.2 bn (largely from HDFC Bank). The company did not book any capital gains during the quarter. We expect HDFC to recognize capital gains of Rs6 bn in the next three quarters—stable qoq.

Exhibit 1: Yields for AAA-rated and AA-rated corporate bonds have increased in past few days
Yields on 5-year corporate bonds and 10-year G-Secs in India, July 2012- July 2013 (%)



Source: Kotak Institutional Equities, Company

Exhibit 2: Spreads between G-Sec and bonds have increased
Spread between 5-year corporate bonds and 10-year G-Secs in India, July 2011- July 2013 (%)



Source: Kotak Institutional Equities, Company

Exhibit 3: HDFC Ltd – P&L
March fiscal year-ends, 1QFY13-1QFY14

	1Q13	2Q13	3Q13	4Q13	1Q14	YoY (%)	1Q14E	Actual vs KS (%)
Operating income	49,346	52,697	52,421	56,661	55,558	13	58,101	(4)
Interest on loans	46,462	48,357	49,972	53,392	52,197	12	54,825	(5)
Fees and other charges	617	525	392	879	544	(12)	600	(9)
Dividend	1,595	1,946	452	814	2,171	36	2,026	7
Sale of investment	202	941	963	1,049	—	(100)	200	(100)
Other op income	470	928	642	526	646	38	450	44
Interest expense	33,882	35,414	35,214	34,398	37,633	11	39,811	(5)
Net operating income	**15,464**	**17,283**	**17,207**	**22,263**	**17,925**	**16**	**18,289**	**(2)**
Op. inc. excl. gains, capital gains and lease income	**13,667**	**14,396**	**15,792**	**20,399**	**15,754**	**15**	**16,064**	**(2)**
Net Fund based income	14,847	16,758	16,815	21,383	17,381	17	17,689	(2)
Net Fund based income (int income less int exp)	12,580	12,943	14,758	18,994	14,564	16	15,014	(3)
Other exp.	1,691	1,821	1,780	1,309	1,879	11	1,945	(3)
Other exp.	1,083	1,200	1,138	718	1,135	5	1,245	(9)
Staff expenses	608	621	642	590	744	22	699	6
PBDT	13,773	15,462	15,427	20,954	16,046	17	16,345	(2)
Depreciation	47	56	59	73	55	17	60	(8)
Other income	74	78	84	116	80	9	80	0
PBT	13,799	15,484	15,452	20,997	16,071	16	16,365	(2)
Tax	3,780	3,970	4,050	5,445	4,350	15	4,255	2
PAT	**10,019**	**11,514**	**11,402**	**15,552**	**11,721**	**17**	**12,110**	**(3)**
Tax rate	27	26	26	26	27		26	

Source: Company, Kotak Institutional Equities

Exhibit 4: HDFC Ltd – quarterly data
March fiscal year-ends, 1QFY13-1QFY14

Other details - Rs bn	1Q13	2Q13	3Q13	4Q13	1Q14	YoY (%)
Disbursement for the quarter	156	250	141	277	183	17
Outstanding (Rs bn)	1,483	1,551	1,605	1,700	1,769	19
Annualised NII (Rs mn)	50,320	51,772	59,032	75,976	58,256	16
NIMs (%)	3.5	3.4	3.7	4.6	3.4	
Gross NPL ratio (%)	0.8	0.8	0.8	0.7	0.8	
CAR (%)	14.6	16.7	17.5	16.2	16.3	
Tier I (%)	11.8	14.1	14.9	13.8	14.0	
Avg spread - reported (%)	2.3	2.3	2.3	2.3	2.3	
ROA	2.5	2.7	2.6	3.5	2.5	
ROE	20.3	20.5	18.3	24.6	18.2	
Balance sheet (Rs mn)						
Sharecapital	2,977	3,078	3,082	3,093	3,108	4
Reserves	201,678	241,191	252,398	246,907	260,987	29
Total liabilities and shareholders funds	**1,642,760**	**1,718,635**	**1,740,846**	**1,838,280**	**1,896,785**	**15**
Loans	1,482,622	1,551,270	1,604,340	1,700,460	1,769,930	19
Individuals	954,129	994,010	1,047,300	1,113,210	1,184,290	24
Corporate bodies	509,977	537,630	539,350	569,550	566,200	11
Others	18,516	19,630	17,690	17,700	19,440	5
Investments	151,825	150,241	145,780	136,841	171,985	13
Deferred tax	6,282	6,552	6,692	6,314	6,353	1
Current liabilities	61,115	87,736	77,016	114,688	125,892	106
Fixed assets	2,350	2,367	2,380	2,379	2,405	2
Total assets	**1,642,760**	**1,718,635**	**1,740,846**	**1,838,280**	**1,896,785**	**15**
Loan book calculations						
Loan on balance sheet	1,482,622	1,551,270	1,604,340	1,700,460	1,769,930	19
Loans outside balance sheet	138,720	157,480	160,490	169,640	172,920	25
Individual loans pre sell down	1,092,849	1,151,490	1,207,790	1,282,850	1,357,210	24
Loans under management	1,621,342	1,708,750	1,764,830	1,870,100	1,942,850	20
Compostition of loan book under management						
Total loan under management	1,621,342	1,708,750	1,764,830	1,870,100	1,942,850	20
Individual loans under management	1,092,849	1,151,490	1,207,790	1,282,850	1,357,210	24
Other loans	528,493	557,260	557,040	587,250	585,640	11

Source: Company, Kotak Institutional Equities

Exhibit 5: HDFC Ltd consolidated – quarterly data
March fiscal year-ends, 1QFY13-1QFY14 (Rs mn)

	1Q13	2Q13	3Q13	4Q13	1Q14	YoY (%)
Total operating income	73,808	103,376	101,286	81,013	84,748	15
Operating income	51,230	54,235	55,384	59,476	58,399	14
Premium Income from Insurance business	20,073	29,713	30,065	46,652	22,905	14
Other Income from Insurance Business	2,282	18,413	14,819	(26,643)	3,378	48
Profit on sale of Investments	222	1,015	1,019	1,528	65	(71)
Interest expense	34,486	36,709	36,272	35,489	38,837	13
Net operating income	**39,322**	**66,667**	**65,014**	**45,523**	**45,911**	**17**
Other exp.	25,114	48,885	46,753	20,948	26,622	6
Other exp.	23,362	47,146	44,935	19,489	24,705	6
Staff expenses	1,284	1,309	1,356	1,332	1,518	18
Provisioning expenses	468	429	461	127	399	(15)
PBDT	14,208	17,782	18,262	24,575	19,289	36
Depreciation	128	132	135	147	90	(30)
Other income	77	125	108	77	80	4
PBT	14,157	17,776	18,235	24,506	19,279	36
Tax	4,283	4,613	4,693	6,432	5,144	20
PAT	**9,874**	**13,163**	**13,542**	**18,074**	**14,136**	**43**
Minority interest	(436)	(1,059)	(803)	(1,121)	(1,333)	206
Profit from associates	3,320	3,635	4,329	3,878	4,268	29
Consolidated PAT	**12,759**	**15,749**	**17,058**	**20,831**	**17,071**	**34**

Source: Company, Kotak Institutional Equities

Exhibit 6: HDFC, sum-of-the-parts-based valuation based on March fiscal year-end, 2014

Business/ subsidiaries	HDFC's holding (%)	Value of companies (Rs mn)	Value per share (Rs)	Valuation methodology
HDFC			442	Based on residual growth model; multiple of 3.6X PBR FY2014E
Value of subsidiaries and associates			**307**	
HDFC Bank	23	1,546,350	220	Based on target price
HDFC Standard Life MF	60	48,480	19	4% of March 2014E AUMs
Life Insurance	72	111,520	47	11% margins and 16X NBV multiple
General insurance	74	9,890	4	Based on deal with ERGO
Gruh Finance	62.0	33,960	12	Based on market price
IDFC	1.9	190,856	2	Based on market price
Equity investments			**14**	
BVPS of non-strategic investments			5	
Unrealised gains on above			9	
Total value per share			**763**	

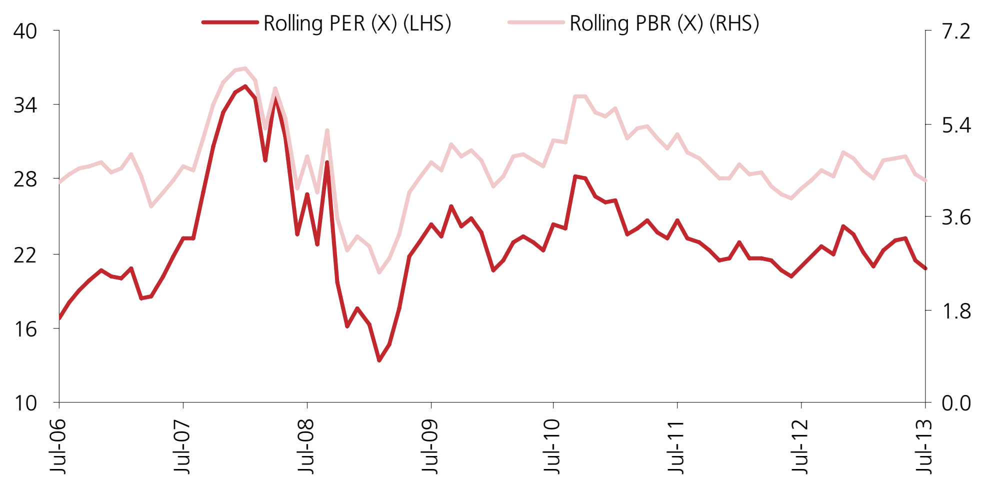
Source: Kotak Institutional Equities estimates

Exhibit 7: HDFC, sum-of-the-parts-based valuation based on March fiscal year-end, 2015

Business/ subsidiaries	HDFC's holding (%)	Value of companies (Rsmn)	Value per share (Rs)	Valuation methodology
HDFC			522	Based on residual growth model; multiple of 3.6X PBR FY2015E
Value of subsidiaries and associates			**345**	
HDFC Bank	23.2	1,731,912	247	Based on HDFC Bank's price target
HDFC Standard Life MF				
MF business	60.0	58,176	23	4% of March 2015E AUMs
PMS business	60.0	1,440	1	10% of AUMs
Life insurance	72.0	128,248	54	11% margins and 16X NBV multiple
General insurance	74.0	11,374	5	Based on deal with ERGO
Gruh Finance	62.0	33,960	12	Based on market price
IDFC	1.9	190,856	2	Based on market price
Equity investments			**14**	
BVPS of non-strategic investments			5	
Unrealised gains			9	
Total value per share			**881**	

Source: Kotak Institutional Equities estimates

Exhibit 8: HDFC – one-year forward rolling PER and PBR
Monthly data, July 2006 - July 2013 (X)



Source: Company, Bloomberg, Kotak Institutional Equities estimates

Exhibit 9: HDFC valuation
March fiscal year-ends, 2011-16E

March y/e	Profit after tax (Rs mn)	EPS (Rs)	EPS core (Rs)	P/E (X)	PE on core operations (X)	BVPS (Rs)	BVPS Core (Rs)	P/B (X)	P/B on core operations (X)	RoA (%)	RoE (%)	Core RoE (%)
2011	35,351	24	20	33	25.3	118	58	7	8.8	2.8	21.7	38.9
2012	41,226	28	24	29	21.2	129	67	6	7.5	2.7	22.7	38.4
2013	48,481	31	26	26	19.4	162	104	5	4.9	2.7	22.0	31.2
2014E	57,849	37	32	21	15.9	182	122	4	4.2	2.7	21.8	28.4
2015E	67,918	44	38	18	13.4	205	145	4	3.5	2.7	22.7	28.3
2016E	80,007	52	45	16	11.4	233	173	3	2.9	2.7	23.6	28.0

Share price (Rs)	**803**
Market Capitalisation (Rs mn)	1242028
Less :value of subsidiaries and investments (Rs mn)	496596
Price adjusted for subsidiaries and investments (Rs)	745,432
Price per share adjt for subsidiaries and investments (Rs)	**508**

Source: Kotak Institutional Equities

Exhibit 10: HDFC: Key ratios
March fiscal year-ends, 2011-16E (%)

	2011	2012	2013	2014E	2015E	2016E
Spread calc						
Average yield on assets (incl fees)	10.1	11.3	11.7	11.6	11.7	11.8
Average cost of funds	7.3	9.0	9.4	9.2	9.2	9.2
Overall spread	2.8	2.4	2.3	2.5	2.5	2.6
Spread on housing loans	**3.0**	**2.7**	**2.7**	**2.7**	**2.6**	**2.6**
NIM (pre provisions)	**4.0**	**3.9**	**3.9**	**3.9**	**3.9**	**3.9**
DU PONT Analysis						
Net total income	4.0	3.8	3.8	3.9	3.9	3.9
Net interest income	3.5	3.5	3.4	3.5	3.5	3.5
Capital gains	0.3	0.2	0.2	0.2	0.2	0.2
Dividend income	0.2	0.2	0.3	0.2	0.2	0.2
Net other income	0.2	0.2	0.2	0.2	0.2	0.1
Operating expenses	0.3	0.3	0.3	0.3	0.3	0.3
ROA	**2.8**	**2.7**	**2.7**	**2.7**	**2.7**	**2.7**
Average assets/average equity	7.9	8.4	8.2	8.0	8.4	8.7
ROE	**21.7**	**22.7**	**22.0**	**21.8**	**22.7**	**23.6**
Growth (%)						
Net loans	20	20	21	21	20	19
Total assets	20	20	17	18	18	17
PBT	24	16	16	19	17	18
PAT	25	17	18	19	17	18

Source: Company, Kotak Institutional Equities estimates

Exhibit 11: HDFC standalone P&L and balance sheet
March fiscal year-ends, 2011-16E (Rs mn)

	2011	2012	2013	2014E	2015E	2016E
Income statement						
Total income excluding fee income	126,325	170,646	208,710	244,053	289,867	342,308
Interest on Housing Loans	110,683	150,214	187,345	222,500	266,234	316,182
Dividends	2,252	3,096	4,806	4,279	4,961	5,661
Lease rentals	231	175	43	38	35	31
Other operating income	13,159	17,161	16,516	17,235	18,638	20,434
Income from investments	7,799	12,189	11,265	10,719	11,073	11,258
Capital gains	3,597	2,702	3,155	4,000	4,500	5,500
Interest payable	75,597	111,568	138,909	160,423	191,910	227,203
Net Income before provision	**50,728**	**59,078**	**69,801**	**83,630**	**97,957**	**115,105**
Provision	700	800	1,450	2,175	2,436	2,728
Fee income	**2,204**	**2,683**	**2,413**	**2,969**	**3,468**	**4,054**
Total income	128,528	173,329	211,123	247,021	293,335	346,362
Total expenses	**3,619**	**4,313**	**5,153**	**6,101**	**7,003**	**8,043**
Depreciation	192	205	236	248	260	273
Other income	251	213	351	351	351	351
Profit before tax	**48,671**	**56,656**	**65,726**	**78,426**	**92,077**	**108,466**
Tax	13,320	15,430	17,245	20,577	24,159	28,459
Profit after tax	**35,351**	**41,226**	**48,481**	**57,849**	**67,918**	**80,007**
- .EPS	24	28	31	37	44	52
EPS (core)	**20**	**24**	**26**	**32**	**38**	**45**
Book value	118	129	162	182	205	233
Book value (core)	58	67	104	122	145	173
Balance sheet						
Net loans	1,171,268	1,408,750	1,700,460	2,054,507	2,457,561	2,923,810
Total Investments	118,324	122,070	136,841	143,551	148,181	148,181
In equity	88,446	90,588	89,898	92,398	92,398	92,398
Fixed assets owned	2,340	2,340	2,379	2,570	2,775	2,997
Total assets	**1,395,023**	**1,675,205**	**1,952,968**	**2,313,915**	**2,721,805**	**3,188,277**
Total Borrowings	1,154,105	1,391,275	1,588,280	1,912,605	2,278,211	2,670,353
Total borowings and CL	**1,221,856**	**1,485,024**	**1,702,968**	**2,033,027**	**2,404,654**	**2,828,407**
Share capital	2,934	2,954	3,093	3,093	3,093	3,093
Reserves	170,231	187,222	246,907	277,795	314,058	356,777
Shareholders fund	**173,165**	**190,176**	**250,000**	**280,887**	**317,151**	**359,870**

Source: Company, Kotak Institutional Equities estimates

Kotak Institutional Equities

Bajaj Auto (BJAUT)

Automobiles

ADD

JULY 22, 2013

RESULT

Coverage view: Neutral

Price (Rs): 1,966

Target price (Rs): 2,000

BSE-30: 20,150

Pricing power in export markets boosts margin. Bajaj Auto 1QFY14 results were better than estimates due to higher-than-expected average selling prices (ASPs). Reported EBITDA was impacted by MTM loss of Rs960 mn; adjusted EBITDA margin was 20.4% versus 17.9% in 1QFY13. Launch of new Discover models and normalization of Pulsar production will likely help Bajaj Auto to improve domestic sales, in our view. We expect three-wheeler volumes to pick up on the issue of new permits by state governments. We will review our estimates after the result concall on Monday.

Company data and valuation summary

Bajaj Auto

Stock data			
52-week range (Rs) (high,low)			2,229-1,505
Market Cap. (Rs bn)			568.9
Shareholding pattern (%)			
Promoters			50.0
FIIs			18.2
MFs			1.4
Price performance (%)	1M	3M	12M
Absolute	7.1	9.7	27.0
Rel. to BSE-30	2.3	3.5	8.9

Forecasts/Valuations	2013	2014E	2015E
EPS (Rs)	105.2	119.1	139.2
EPS growth (%)	1.3	13.2	17.0
P/E (X)	18.7	16.5	14.1
Sales (Rs bn)	194.9	212.9	240.3
Net profits (Rs bn)	30.4	34.5	40.3
EBITDA (Rs bn)	41.1	45.1	51.7
EV/EBITDA (X)	13.8	12.7	11.0
ROE (%)	43.2	38.6	36.9
Div. Yield (%)	2.3	2.4	2.8

Increase in net realizations due to higher export ASPs; notional MTM loss impacts reported EBITDA

Bajaj Auto reported net profit of Rs7,377 mn (+3% yoy), which was 2% below estimates; ex forex loss, profit would have been 7% higher than our estimate. Net sales of Rs49.1 bn (+1% yoy) were 3% above our estimates, driven by 12% yoy increase in average selling prices (ASPs) due to a better product mix (higher three-wheeler sales) and 26% yoy increase in export ASPs.

We note that the company reported a notional MTM loss on range forward contracts of Rs960 mn, which would reverse during the tenure of the contracts. Reported EBITDA margin was 18.5%, and ex forex loss, EBITDA margin would have been 20.4%, higher than our estimate of 19.3%.

Domestic sales volumes were subdued due to a weak market; three-wheeler exports up 44% yoy

The company's domestic motorcycle sales declined by 13% yoy driven by subdued market conditions and loss in market share. We highlight that a strike at the Chakan plant caused Bajaj Auto to lose 20,000 units of Pulsar in 1QFY14. Motorcycle export volumes declined sharply (-21% yoy) driven by a ban on motorcycle sales in Nigeria and weak Latin American markets.

Domestic three-wheeler volumes were flattish yoy but are expected to improve, driven by new permits being issued in Hyderabad (20,000 units) and Maharashtra (30,000 units). Three-wheeler exports increased by 44% yoy due to normalization of sales in Sri Lanka and strong growth in Bangladesh.

Revival in domestic and export motorcycle volumes, weaker Rupee to boost EBITDA margin

We expect a revival in domestic motorcycle volumes, driven by good monsoons and normalization of Pulsar volumes. Domestic three-wheeler volumes should also inch upwards due to the issue of new permits by state governments. We expect EBITDA margin to improve due to the depreciation of the Rupee (current quarter average USD/INR rate was 55.96) and the company will realize 58 in the coming quarters. Export volumes to Africa are expected to increase with penetration in other African markets, besides Nigeria. We maintain our ADD rating on the stock (target price: Rs2,000) and will review our earnings estimates after the conference call on Monday.

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Results better than estimates on higher-than-expected net realizations

Exhibit 1 highlights Bajaj Auto's 1QFY14 results and compares them with the performance in 4QFY13 and 1QFY13. We discuss highlights below.

Exhibit 1: 1QFY14 results were better than our estimates driven by higher-than-expected export net realizations
Bajaj Auto interim results, March fiscal year-ends (Rs mn)

					% change		
	1QFY14	1QFY14E	1QFY13	4QFY13	KIE est	yoy	qoq
Volumes (units)	979,275	979,275	1,078,971	981,242	—	(9.2)	(0.2)
Net realisations	49,105	47,408	43,686	47,400	3.6	12.4	3.6
Net sales	**48,087**	**46,426**	**47,136**	**46,511**	**3.6**	**2.0**	**3.4**
Operating income	1,024	1,500	1,520	954	(31.8)	(32.7)	7.3
Net sales (including op income)	**49,111**	**47,926**	**48,657**	**47,465**	**2.5**	**0.9**	**3.5**
Inc/dec in stock	622	—	1,156	(1,342)			
Raw materials	33,445	33,500	33,925	35,430	1.7	(2.9)	(0.1)
Staff costs	1,837	1,800	1,604	1,666	2.1	14.5	10.2
Other expenses	4,141	3,388	3,255	3,344	22.2	27.2	23.8
Total expenses	40,044	38,687	39,940	39,099	3.5	0.3	2.4
EBITDA	**9,067**	**9,238**	**8,717**	**8,366**	**(1.9)**	**4.0**	**8.4**
Other income	1,756	1,840	1,820	2,436	(4.6)	(3.5)	(27.9)
Interest expense	1	0	0	2			
Depreciation expense	444	470	352	466	(5.6)	26.0	(4.8)
Profit before tax before exceptional	10,378	10,608	10,184	10,334	(2.2)	1.9	0.4
Extraordinary income	—	—	—	—			
Profit before tax	**10,378**	**10,608**	**10,184**	**10,334**	**(2.2)**	**1.9**	**0.4**
Tax expense	3,002	3,076	3,000	2,676	(2.4)	0.0	12.1
Profit after tax	7,377	7,532	7,184	7,658	(2.1)	2.7	(3.7)
Adj PAT	**7,377**	**7,532**	**7,184**	**7,658**	**(2.1)**	**2.7**	**(3.7)**
Raw material cost as % of net sales	69.4	69.9	72.1	71.8			
Staff cost as % of net sales	3.7	3.8	3.3	3.5			
Other expenses as % of net sales	8.4	7.1	6.7	7.0			
EBITDA margin (%)	18.5	19.3	17.9	17.6			
No of shares	289	289	289	289			
EPS	25.5	26.0	24.8	26.5			
Tax rate (%)	28.9	29.0	29.5	25.9			
Volume breakdown (units)							
Economy	133,019	133,019	149,492	93,454		(11.0)	42.3
Executive	289,954	289,954	299,318	299,891		(3.1)	(3.3)
Premium	148,682	148,682	169,679	162,814		(12.4)	(8.7)
Domestic motorcycle	**571,655**	**571,655**	**618,489**	**556,158**		**(7.6)**	**2.8**
Export motorcycle	288,496	288,496	364,134	303,537		(20.8)	(5.0)
Total motorcycle	**860,151**	**860,151**	**982,623**	**859,695**		**(12.5)**	**0.1**
Domestic 3 wheelers	45,057	45,057	44,837	60,079		0.5	(25.0)
Export 3 wh	74,067	74,067	51,511	61,468		43.8	20.5
3 wheelers	**119,124**	**119,124**	**96,348**	**121,547**		**23.6**	**(2.0)**
Total volumes	**979,275**	**979,275**	**1,078,971**	**981,242**		**(9.2)**	**(0.2)**
Volume mix (%)							
Economy	13.6	13.6	13.9	9.5			
Executive	29.6	29.6	27.7	30.6			
Premium	15.2	15.2	15.7	16.6			
Domestic motorcycle	58.4	58.4	57.3	56.7			
Export motorcycle	29.5	29.5	33.7	30.9			
Total motorcycle	**87.8**	**87.8**	**91.1**	**87.6**			
Domestic 3 wheelers	4.6	4.6	4.2	6.1			
Export 3 wh	7.6	7.6	4.8	6.3			
3 wheelers	**12.2**	**12.2**	**8.9**	**12.4**			
Total volumes	**100.0**	**100.0**	**100.0**	**100.0**			

Source: Company, Kotak Institutional Equities estimates

- **Increase in net realizations.** Bajaj Auto's net realizations increased 3.6% qoq and 12.4% yoy, reflecting (1) a weaker Rupee, which boosted export realizations, (2) a superior export product mix and (3) a price hike taken in the domestic market in April 2013 (~1.5%). We believe export realizations increased by ~26% yoy due to a weaker Rupee (10% depreciation of the Rupee versus the US Dollar) and a superior product mix (higher share of three-wheelers in the mix). Domestic net realizations improved by 5% yoy, driven by a higher share of Discover bikes in the mix and a slightly higher share of three-wheeler volumes.

- **Higher gross margin.** Gross margin improved by 270 bps yoy and 250 bps qoq, driven by improvement in the domestic and export businesses.

- **Increase in EBITDA margin.** Reported EBITDA margin increased by ~80 bps qoq, reflecting sharp improvement in gross margin by ~250 bps, which was partially offset by ~140 bps increase other expenses due to Rs960 mn MTM loss on range forward option contracts. Adjusting for the MTM loss, which is notional and would be reversed over the tenure of the contract, EBITDA margin was 20.4% (versus 17.6% in 4QFY13 and 17.9% in 1QFY13).

- **Higher staff costs. Staff costs increased by 10.2% qoq and 14.5% yoy to Rs1,837 mn in 4QFY13, in line with our estimates.**

- **Higher other expenses due to notional MTM loss.** Bajaj Auto reported higher other expenses of Rs4,141 mn in 1QFY14 versus Rs3,344 mn in 4QFY13 and Rs3,255 mn in 1QFY13. We note that the company booked an MTM loss of Rs960 mn on range forward option contracts during the quarter versus an MTM gain of Rs330 mn in 1QFY13. The loss is notional in nature and would be reversed over the tenure of the contract. **The company reported lower other income of Rs1,756 mn versus Rs2,436 mn in 4QFY13 and 1,820 mn in 1QFY13. Company received dividend income of Rs270 mn from KTM. Bajaj holds 48% stake in KTM.**

- **Lower depreciation expense, higher tax rate qoq.** The company reported sequentially lower depreciation expenses of Rs444 mn versus Rs466 mn in 4QFY13 (-4.8%). Tax rate was higher at 28.9% versus 25.9% in 4QFY13, in line with our estimates.

Domestic motorcycle segment affected by weak market and strike at Chakan

The company's domestic motorcycle sales increased marginally by 2.8% qoq and declined by 7.6% yoy, driven by weak market conditions and loss of market share (see Exhibit 2). We highlight that Bajaj Auto lost 20,000 units of Pulsar due to a strike at its Chakan plant in 1QFY14. Production has normalized to the extent of 90% of current demand for Pulsar. We expect the launch of the new Discover models and normalization of Pulsar production will help Bajaj Auto to regain market share.

Exhibit 2: Competition is eating into Bajaj Auto's market share

Quarterly market share trend in the domestic motorcycle segment, 2QFY11-1QFY14 (%)

	Sep-10	Dec-10	Mar-11	Jun-11	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12	Mar-13	Jun-13
Economy												
Bajaj Auto	**23.1**	**23.1**	**24.1**	**26.2**	**27.2**	**29.7**	**31.3**	**28.9**	**25.4**	**23.6**	**21.2**	**26.4**
Hero motocorp	47.3	47.2	46.6	44.7	43.0	45.6	45.4	48.7	53.1	53.0	59.0	54.7
Executive												
Bajaj Auto	**23.6**	**19.8**	**21.5**	**21.5**	**22.5**	**19.0**	**17.6**	**17.6**	**21.8**	**22.9**	**18.7**	**17.8**
Hero motocorp	64.2	68.1	67.5	67.7	68.0	69.6	69.8	68.8	59.3	60.5	61.7	63.7
HMSI	9.0	8.7	8.5	8.7	7.8	9.7	11.2	12.1	16.4	14.7	15.9	15.5
Premium												
Bajaj Auto	**51.3**	**47.4**	**44.3**	**40.7**	**42.3**	**43.6**	**41.6**	**41.5**	**41.5**	**41.5**	**38.3**	**37.6**
Hero motocorp	18.6	19.9	23.9	21.5	20.6	16.8	19.0	15.9	8.9	18.8	19.5	13.8
HMSI	7.6	7.7	6.5	9.0	8.8	10.3	9.6	13.9	16.6	13.0	14.1	16.1
Yamaha	10.1	12.7	12.2	15.3	14.8	16.6	14.7	13.2	16.9	12.8	13.1	14.3
Total												
Bajaj Auto	**28.5**	**25.6**	**26.1**	**25.3**	**26.8**	**25.1**	**24.5**	**23.5**	**25.7**	**26.0**	**22.5**	**22.6**
Hero motocorp	52.9	55.5	55.9	56.5	55.0	56.2	56.2	56.5	50.0	51.9	54.0	54.1
HMSI	7.3	7.1	6.8	7.3	6.5	8.1	8.7	10.0	13.1	11.5	12.7	12.5

Source: CRISIL, Kotak Institutional Equities

Motorcycle export volumes declined by a sharp 21% yoy and 5% qoq, driven by a ban on motorcycle taxis in big Nigerian cities and weak Latin American markets. The company said it grew sales volumes in Kenya and Uganda and sales in Sri Lanka were stable. The company expects to improve market share in Africa as it penetrates North Nigeria and other countries.

Domestic three-wheeler volumes flat, export volumes rise sharply

Domestic three-wheeler volumes were flat yoy at ~45,000 units. The company improved market share in the diesel passenger-carrier segment to 32% (from 31% in 4QFY13) in 1QFY14. In the LPG, CNG and gasoline three-wheeler segment, Bajaj Auto maintained its market share at 87% in 1QFY14 versus the preceding quarter. We expect domestic three-wheeler volumes to benefit from the issue of new permits by state governments.

Exports volumes in 1QFY14 increased sharply by ~44% yoy, driven by normalization of sales in Sri Lanka and growth in Bangladesh. The company's guidance indicates 12-15% yoy growth in export and domestic three-wheeler volumes in FY2014.

Exhibit 3: We expect Bajaj Auto's volumes to rise by ~6% yoy in FY2014
Volume assumptions, March fiscal year-ends, 2010-16E (mn units)

	2010	2011	2012	2013	2014E	2015E	2016E
Sales volume (units)							
Motorcycles	**2,506,845**	**3,387,043**	**3,834,405**	**3,757,105**	**3,982,234**	**4,390,215**	**4,891,384**
Domestic	1,781,748	2,414,606	2,566,757	2,463,874	2,559,680	2,754,278	2,928,260
Platina	426,726	383,735	535,648	484,600	508,830	539,360	539,360
Discover	795,337	1,234,788	1,315,400	1,311,843	1,416,790	1,530,134	1,621,942
Pulsar	559,685	796,083	715,709	667,431	634,059	684,784	766,958
Exports	725,097	972,437	1,267,648	1,293,231	1,422,554	1,635,937	1,963,125
Total two-wheelers	**2,511,696**	**3,387,043**	**3,834,405**	**3,757,105**	**3,982,234**	**4,390,215**	**4,891,384**
Domestic three-wheelers	176,027	205,627	202,979	226,131	253,153	273,405	295,211
Passenger three-wheelers	164,493	201,270	195,141	223,287	250,081	270,088	291,695
Goods three-wheelers	11,534	4,357	7,838	2,844	3,072	3,317	3,516
Exports	164,909	231,281	312,176	253,926	266,622	298,617	343,410
Total three-wheelers	**340,936**	**436,908**	**515,155**	**480,057**	**519,775**	**572,022**	**638,621**
Total vehicles	**2,852,632**	**3,823,951**	**4,349,560**	**4,237,162**	**4,502,009**	**4,962,237**	**5,530,005**
Growth (yoy %)							
Motorcycles	**31.4**	**35.1**	**13.2**	**(2.0)**	**6.0**	**10.2**	**11.4**
Domestic	39.6	35.5	6.3	(4.0)	3.9	7.6	6.3
Platina		(10.1)	39.6	(9.5)	5.0	6.0	—
Discover		55.3	6.5	(0.3)	8.0	8.0	6.0
Pulsar		42.2	(10.1)	(6.7)	(5.0)	8.0	12.0
Exports	14.8	34.1	30.4	2.0	10.0	15.0	20.0
Total two-wheelers	**30.8**	**34.9**	**13.2**	**(2.0)**	**6.0**	**10.2**	**11.4**
Domestic three-wheelers	29.9	16.8	(1.3)	11.4	11.9	8.0	8.0
Passenger three-wheelers	31.3	22.4	(3.0)	14.4	12.0	8.0	8.0
Goods three-wheelers	13.1	(62.2)	79.9	(63.7)	8.0	8.0	6.0
Exports	18.6	40.2	35.0	(18.7)	5.0	12.0	15.0
Total three-wheelers	**24.2**	**28.1**	**17.9**	**(6.8)**	**8.3**	**10.1**	**11.6**
Total vehicles	**30.0**	**34.0**	**13.7**	**(2.6)**	**6.3**	**10.2**	**11.4**

Source: Company, Kotak Institutional Equities estimates

Exhibit 4: We expect earnings to post 16% CAGR over FY2014-16

Bajaj Auto profit and loss, balance sheet and cash-flow statement, March fiscal year-ends, 2010-16E (Rs mn)

	2010	2011	2012	2013	2014E	2015E	2016E
Profit model (Rs mn)							
Net sales	115,085	158,968	188,803	194,890	212,927	240,338	274,744
EBITDA	**26,175**	**34,138**	**40,284**	**41,064**	**45,059**	**51,661**	**60,171**
Other income	976	3,339	2,997	3,244	5,218	6,944	9,039
Interest	(60)	(17)	(222)	(5)	—	—	—
Depreciation	(1,365)	(1,228)	(1,456)	(1,640)	(1,750)	(1,851)	(1,899)
Profit before tax	**25,726**	**36,232**	**41,602**	**42,662**	**48,527**	**56,755**	**67,311**
Extra-ordinary items	(1,624)	7,246	(1,340)	—	—	—	—
Taxes	(7,075)	(10,080)	(10,221)	(12,227)	(14,073)	(16,459)	(19,520)
Net profit	**17,027**	**33,397**	**30,041**	**30,436**	**34,454**	**40,296**	**47,791**
Adjusted net profit	**18,171**	**26,152**	**30,041**	**30,436**	**34,454**	**40,296**	**47,791**
Adjusted earnings per share (Rs)	**62.8**	**90.4**	**103.8**	**105.2**	**119.1**	**139.2**	**165.1**
Balance sheet (Rs mn)							
Equity	29,283	49,102	60,411	79,020	97,350	118,788	144,214
Deferred tax liability	17	297	484	1,151	1,151	1,151	1,151
Total borrowings	13,386	4,855	2,546	1,934	1,934	1,933	1,933
Current liabilities	28,579	38,222	47,370	42,682	42,377	47,308	53,487
Total liabilities	**71,265**	**92,476**	**110,811**	**124,786**	**142,811**	**169,180**	**200,785**
Net fixed assets	15,211	15,483	14,914	20,277	21,027	21,426	21,777
Investments	40,215	47,219	48,828	64,305	81,425	104,425	132,925
Cash	1,014	2,288	16,538	5,589	704	1,013	452
Other current assets	14,824	27,443	30,211	33,913	38,951	41,612	44,928
Miscellaneous expenditure	—	43	320	703	703	703	703
Total assets	**71,265**	**92,476**	**110,811**	**124,786**	**142,811**	**169,180**	**200,785**
Free cash flow (Rs mn)							
Operating cash flow excl. working capital	18,874	24,352	28,802	26,557	27,592	32,399	38,543
Working capital changes	8,498	(8,215)	797	(5,213)	(5,344)	2,270	2,863
Capital expenditure	(1,078)	(2,006)	(1,090)	(5,082)	(2,500)	(2,250)	(2,250)
Free cash flow	**26,293**	**14,131**	**28,509**	**16,262**	**19,748**	**32,419**	**39,156**
Ratios							
EBITDA margin (%)	21.9	20.5	20.3	20.1	20.3	20.7	21.0
PAT margin (%)	15.8	16.5	15.9	15.6	16.2	16.8	17.4
Book Value (Rs/share)	101.2	169.7	208.7	273.0	336.4	410.5	498.3
RoAE (%)	70.9	84.9	54.5	43.2	38.6	36.9	36.0
RoACE (%)	**42.5**	**63.6**	**47.5**	**38.6**	**33.7**	**31.8**	**30.7**

Source: Company, Kotak Institutional Equities estimates

kotak Institutional Equities

Hindustan Zinc (HZ)

Metals & Mining

ADD

JULY 22, 2013

RESULT

Coverage view: Neutral

Price (Rs): 104

Target price (Rs): 150

BSE-30: 20,150

In line, shutdowns cap benefit of higher mined metal. Hindustan Zinc reported EBITDA of Rs15.03 bn (+5% yoy, -29% qoq), in line with our estimate. Upstream mined metal increased 27% yoy to 238 kt though full benefit of higher volumes was not realized due to inventory build-up—plant shutdowns impacted downstream metal volumes. Decline in prices hurt silver profitability the most, though higher premiums on zinc and lead cushioned the impact. The company maintained guidance on mined metal production with 15% growth to 1 mn tons in FY2014. Maintain ADD.

Company data and valuation summary

Hindustan Zinc

Stock data			
52-week range (Rs) (high,low)			147-96
Market Cap. (Rs bn)			440.9
Shareholding pattern (%)			
Promoters			64.9
FIIs			1.5
MFs			1.2
Price performance (%)	**1M**	**3M**	**12M**
Absolute	(6.6)	(5.1)	(12.3)
Rel. to BSE-30	(10.8)	(10.4)	(24.8)

Forecasts/Valuations	2013	2014E	2015E
EPS (Rs)	16.4	14.7	15.3
EPS growth (%)	24.2	(10.4)	4.1
P/E (X)	6.4	7.1	6.8
Sales (Rs bn)	127.0	127.0	135.4
Net profits (Rs bn)	69.2	62.0	64.5
EBITDA (Rs bn)	64.8	63.3	64.8
EV/EBITDA (X)	3.5	3.0	2.2
ROE (%)	23.5	17.9	16.4
Div. Yield (%)	3.0	3.0	3.0

QUICK NUMBERS

- Mined metal at 238 kt (+27% yoy)
- MTM gain of Rs800 mn on bond portfolio

In-line operational performance, shutdowns put a production cap despite higher mined metal

Hindustan Zinc reported in-line operational performance for 1QFY14 with EBITDA of Rs15.03 bn (+5% yoy, -29% qoq). Highlight of the quarter was higher mined metal of 238 kt (+27% yoy, -9% qoq)—increase mainly led by Rampura Agucha mine (expected) after mining stabilized at lower stripping ratios. However, full benefit of higher mined metal was not realized as concentrate ended up in inventory due to plant shutdowns at downstream units, i.e. zinc roaster and lead smelter. HZ's concentrate inventory increased by 22 kt during the quarter to 54 kt. Due to smelter shutdowns, refined metal production declined by (1) 4% qoq to 174 kt (+11% yoy) of zinc, (2) 6% qoq to 33 kt (+6% yoy) of lead and (3) 11% qoq to 96 tons (net of captive consumption) of silver. Metal sales during 1QFY14 were 171 kt of zinc, 30 kt of lead and 92 tons of silver.

HZ reported net income of Rs16.6 bn (+5% yoy, -23% qoq), 16% ahead of our estimate. Net income beat was due to MTM gains of Rs800 mn (Rs740 mn loss in 4QFY13) on bond portfolio due to decline in interest rates.

Lower prices hurt silver profitability most, premiums strengthen—likely on increased domestic sales

Decline in commodity prices hurt profitability of silver the most with 40% qoq decline in EBIT to Rs2.7 bn (-23% yoy) on the back of 22% sequential decline in realizations. However, effective sequential decline in zinc-lead prices by 6-8% (in Rupee terms) was cushioned by higher premiums. We estimate blended zinc premiums (exports and domestic) at US$233/ton and blended lead premiums at US$344/ton—higher than FY2013 premiums of US$194/ton for zinc and US$294/ton for lead. Increase in domestic volumes will increase effective premiums due to 5% duty protection on zinc-lead imports. In FY2013, HZ's export sales of zinc declined to 34% from 42% in FY2012.

Delivers strong mined metal production and maintains 15% guidance for FY2014. Maintain ADD

HZ maintained full-year mined metal guidance of 1 mn tons after strong 1QFY14 performance. Our estimates are based on conservative LME of US$1,875/ton for zinc, US$23/troy ounce for silver and 927 kt of mined metal. The stock is inexpensive at 3X FY2014E EBITDA. Maintain ADD.

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Cash reserve increases by Rs9 bn, cash profit at Rs18 bn

HZ's cash reserve increased by Rs9 bn to Rs224 bn at end-1QFY14. The company earned cash profit of Rs18.4 bn during the quarter. The lower accretion was on account of capex spend of Rs3 bn and dividend payout of Rs7 bn.

Other points

- Company did not sell any zinc concentrate against 61 kt sold in 4QFY13.
- Zinc cost of production (COP) was reported at Rs46,800/ton (US$836/ton) on ex-royalty basis. COP increased by 2% yoy due to lower acid realizations and higher mining costs. Coal costs were lower during the quarter.
- Other than MTM gains, company earned 9.5% yield on its investments.
- Effective tax rate for 1QFY14 was 13.9% compared to 11.8% for FY2013.

Our estimates are based on conservative volume and price assumptions

Our estimates are based on conservative volume assumptions. We model mined metal at 927 kt for FY2014 and 947 kt for FY2015—lower than management guidance of 1 mn tons (FY2014). Note that our estimate for FY2014 is based on total ore production of 9.6 mn tons (+12% yoy) and mined metal recovery rates of 89% for zinc (88.9% in FY2013) and 68.5% for lead (66.2% for FY2013). We have assumed marginal improvement in mine grades of zinc/lead over FY2013. Our ore production estimate includes (1) 6 mn tons (-3% yoy) from Rampura Agucha, (2) 810 kt (+44% yoy) at Rajpura Dariba, (3) 1.8 mn tons (+14% yoy) from SK mine, (4) ~1 mn ton (against 277 kt in FY2013) from Zawar mines after mining resumes at three non-operational mines and (5) small quantity of 40 kt from Kayar mines. We believe improvement in mined ore grades or recovery rates (above historical performance) can drive the volume beat above our estimates.

Our estimates are based on conservative base metal price assumptions of US$1,875/ton for zinc, US$2,050/ton for lead and US$23/troy ounce for silver.

Exhibit 1: Interim results of Hindustan Zinc, March fiscal year-ends (Rs mn)

	1QFY14	1QFY14E	1QFY13	4QFY13	(% chg.) 1QFY14E	1QFY13	4QFY13
Net sales	**29,842**	**29,519**	**27,477**	**39,087**	**1.1**	**8.6**	**(23.7)**
Total expenditure	(14,811)	(14,796)	(13,192)	(17,927)	0.1	12.3	(17.4)
Inc/(Dec) in stock	2,085	1,023	(81)	(1,220)			
Raw materials	(11,068)	(10,666)	(8,546)	(10,457)	3.8	29.5	5.8
Staff cost	(1,781)	(1,674)	(1,492)	(1,768)	6.4	19.4	0.7
Other expenditure	(4,047)	(3,480)	(3,073)	(4,481)	16.3	31.7	(9.7)
EBITDA	**15,031**	**14,723**	**14,286**	**21,160**	**2.1**	**5.2**	**(29.0)**
OPM (%)	**50.4**	**49.9**	**52.0**	**54.1**			
Other income	6,203	4,511	5,743	4,118	37.5	8.0	50.6
Interest	(109)	(109)	(129)	(108)		(15.1)	1.0
Depreciation	(1,843)	(1,666)	(1,734)	(1,219)	10.6	6.3	51.2
Pretax profits	**19,281**	**17,458**	**18,166**	**23,951**	**10.4**	**6.1**	**(19.5)**
Extraordinaries	(5)	—	-	(175)			
Tax	(2,671)	(3,142)	(2,353)	(2,117)	(15.0)	13.5	26.1
Deferred taxation	—	—	—	—			
Net income	**16,605**	**14,315**	**15,813**	**21,658**	**16.0**	**5.0**	**(23.3)**
Adjusted profits	**16,605**	**14,315**	**15,813**	**21,658**	**16.0**	**5.0**	**(23.3)**
Ratios							
EBITDA margin (%)	50.4	49.9	52.0	54.1			
ETR (%)	13.9	18.0	13.0	8.9			
EPS (Rs)	3.9	3.4	3.7	5.1			
Other details							
Sales volumes							
Zinc (tons)	171,000	177,912	160,000	182,000	(3.9)	6.9	(6.0)
Lead (tons)	30,000	30,653	29,000	33,000	(2.1)	3.4	(9.1)
Silver -saleable (kgs)	92,000	85,500	73,357	107,774	7.6	25.4	(14.6)
Zinc concentrate (tons)	-	-	-	61,000			
Average realizations (Rs/ton)							
Zinc	116,140	114,270	113,500	109,259	1.6	2.3	6.3
Lead	134,000	127,085	117,931	134,242	5.4	13.6	(0.2)
Silver	44,348	45,249	52,892	56,693	(2.0)	(16.2)	(21.8)
Segment revenues (Rs mn)							
Zinc and lead	24,660		22,532	32,088		9.4	(23.1)
Silver	4,080		3,882	6,110		5.1	(33.2)
Others	654		712	305		(8.3)	114.6
Total	**29,394**		**27,127**	**38,503**		**8.4**	**(23.7)**
Segmental EBIT (Rs mn)							
Zinc and lead	10,213		8,627	15,592		18.4	(34.5)
Silver	2,718		3,510	4,549		(22.6)	(40.2)
Others	285		390	(84)		(26.8)	(440.0)
Total	**13,217**		**12,527**	**20,057**		**5.5**	**(34.1)**

Notes:
(1) Other income was higher due to MTM gains of Rs800 mn on bond portfolio due to decline in interest rates.

Source: Company, Kotak Institutional Equities

Exhibit 2: Hindustan Zinc, key assumptions, March fiscal-year ends, 2011-16E (Rs mn)

	2011	2012	2013	2014E	2015E	2016E
Volumes (tons)						
Zinc	712,603	758,499	674,958	757,160	769,505	781,850
Lead	57,229	91,701	117,445	123,950	125,800	157,250
Silver	147	207	374	338	366	414
Average realizations (Rs/ton)						
Zinc	106,469	108,481	114,664	116,629	121,504	125,867
Lead	114,877	120,722	130,976	129,280	134,173	134,610
Silver (Rs mn/ton)	37	55	56	42	45	47
LME-assumptions (US$/ton)						
Zinc	2,186	2,098	1,948	1,875	1,925	2,050
Lead	2,244	2,269	2,113	2,050	2,100	2,150
Silver (US$/ozt)	23.9	35.4	30.5	23.5	25.1	26.5
Cost per ton (US$/ton)	1,250	1,308	1,425	1,255	1,366	1,482

Source: Company, Kotak Institutional Equities estimates

Exhibit 3: Hindustan Zinc, valuation details, FY2014E basis

	EBITDA	Multiple	Enterprise Value		
	(Rs bn)	(X)	(Rs bn)	(US$ mn)	(Rs/ share)
FY2014E EBITDA	63	6	380	6,601	90
Less: Net debt			(253)	(4,398)	(60)
Arrived market capitalization			**633**	**10,999**	**150**
Target price (Rs/share)					**150**

Source: Kotak Institutional Equities estimates

Exhibit 4: Hindustan Zinc, profit model, balance sheet and cash flow model, March fiscal year-ends, 2010-16E (Rs mn)

	2010	2011	2012	2013	2014E	2015E	2016E
Profit model (Rs mn)							
Net sales	80,170	99,121	114,053	126,998	126,992	135,376	144,864
EBITDA	**46,701**	**54,956**	**60,695**	**64,816**	**63,324**	**64,749**	**65,523**
Other income	7,222	9,792	15,428	20,321	19,598	22,258	23,957
Interest	(439)	(194)	(140)	(291)	(100)	(50)	(25)
Depreciaiton	(3,343)	(4,747)	(6,107)	(6,470)	(7,214)	(8,247)	(9,140)
Profit before tax	**50,141**	**59,596**	**69,445**	**78,200**	**75,608**	**78,711**	**80,316**
Current tax	(8,309)	(8,255)	(12,547)	(7,551)	(11,623)	(11,784)	(11,596)
Deferred tax	(1,418)	(2,336)	(1,638)	(1,656)	(1,987)	(2,384)	(2,861)
Net profit	**40,414**	**49,005**	**55,260**	**68,994**	**61,998**	**64,543**	**65,859**
Earnings per share (Rs)	**9.6**	**11.6**	**13.1**	**16.3**	**14.7**	**15.3**	**15.6**
Balance sheet (Rs mn)							
Equity	181,240	225,332	268,813	322,757	369,431	418,648	469,182
Deferred tax liability	7,112	9,447	11,088	12,799	14,785	17,169	20,030
Total Borrowings	605	4	4	4	4	4	4
Current liabilities	13,258	15,747	14,326	19,094	19,123	19,074	19,412
Total liabilities	**202,215**	**250,530**	**294,230**	**354,654**	**403,343**	**454,895**	**508,628**
Net fixed assets	72,771	81,294	89,578	95,656	105,832	115,022	123,133
Investments	109,492	93,346	126,949	145,399	175,399	205,399	235,399
Cash	9,275	56,329	52,553	69,421	77,765	90,229	104,786
Other current assets	10,677	19,560	25,151	44,178	44,347	44,245	45,311
Miscellaneous expenditure	—	—	—	—	—	—	—
Total assets	**202,215**	**250,530**	**294,230**	**354,654**	**403,343**	**454,895**	**508,628**
Free cash flow (Rs mn)							
Operating cash flow (excl. work cap.)	45,555	44,835	45,529	49,345	71,199	75,174	77,860
Working capital changes	767	(2,116)	(609)	(1,829)	(140)	53	(728)
Capital expenditure	(22,492)	(14,457)	(16,677)	(17,526)	(17,390)	(17,438)	(17,250)
Free cash flow	**23,831**	**28,262**	**28,243**	**29,990**	**53,669**	**57,789**	**59,882**
Ratios							
Debt/equity (X)	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net debt/equity (X)	(0.6)	(0.6)	(0.6)	(0.6)	(0.7)	(0.7)	(0.7)
RoAE (%)	24.9	24.1	22.4	23.3	17.9	16.4	14.8
RoACE (%)	**25.1**	**24.3**	**22.6**	**23.5**	**17.9**	**16.4**	**14.8**

Source: Company, Kotak Institutional Equities estimates

Federal Bank (FB)

Banks/Financial Institutions

BUY

JULY 22, 2013

RESULT

Coverage view: Cautious

Price (Rs): 382

Target price (Rs): 530

BSE-30: 20,150

Keep the faith; business stabilizing. Despite disappointing earnings, led by one large specific asset provision, Federal Bank is witnessing a broad stability in performance. NIM appears to have bottomed while growth and NPLs are steadily improving across non-corporate segments. Key concerns like high cost structure and slow liability share improvement will persist. Post the recent correction, the stock is trading at inexpensive multiples at ~1X book. Maintain BUY.

Company data and valuation summary

Federal Bank

Stock data			
52-week range (Rs) (high,low)			571-362
Market Cap. (Rs bn)			65.3
Shareholding pattern (%)			
Promoters			0.0
FIIs			47.9
MFs			16.0
Price performance (%)	1M	3M	12M
Absolute	(8.1)	(17.6)	(8.2)
Rel. to BSE-30	(14.4)	(21.6)	(21.8)

Forecasts/Valuations	2013	2014E	2015E
EPS (Rs)	49.0	44.0	56.6
EPS growth (%)	7.9	(10.3)	28.7
P/E (X)	7.8	8.7	6.8
NII (Rs bn)	19.7	22.0	26.1
Net profits (Rs bn)	8.4	7.5	9.7
BVPS	355.7	395.5	437.3
P/B (X)	1.1	1.0	0.9
ROE (%)	13.9	11.3	13.2
Div. Yield (%)	2.4	2.1	2.7

QUICK NUMBERS

- Earnings declined 46% yoy due to a specific provision
- Gross NPLs at 3.4%; loan-loss provisions at 2.2%
- Maintain BUY, TP of ₹530 (unchanged)

Performance on key metrics stable; share of low-cost deposits driven by non-resident deposits

Earnings declined 46% yoy led by weak NII growth and high loan-loss provisions. NII increased 4% yoy on the back of subdued loan growth (9% yoy, 6% qoq decline) but NIM has improved marginally (6 bps qoq) driven by high share of low-cost deposits. CASA ratio improved 200 bps qoq to 29% on the back of impressive growth in NRE deposits (51% yoy). High treasury gains (2.4X yoy) cushioned the weak revenue growth to some extent. Asset quality performance was patchy (fresh slippages were at 2.8%) as a large corporate account slipped into NPL, even as SME and retail loans held well. Credit costs were high at 2.2% on the back of high write-offs and full provisioning made on the Government account that had slipped earlier. Cost-income ratio remained high at 45% as revenue drivers reported a weak performance.

High costs (operating and credit) while revenue drivers slow down is our key concern

We note that the bank has a few key challenges ahead: (1) Cost ratios (45%) have expanded in recent years (~20% CAGR in operating expenses since FY2011) led by investments in branch network (20% CAGR). The pay-offs appear to be slower than expected: customer acquisition details appear strong but growth in balances appears to be a lot lower, (2) pushing the slow revenue growth through better NIM and fee income. Loan growth can be a challenge as all banks are revisiting their gold-loan portfolio post the recent decline and (3) credit costs continue to be high led by volatile performance of slippages from the corporate portfolio.

Retain BUY on inexpensive valuations, though challenges persist

We cut earnings by 11% for FY2014E to factor high credit costs and subdued net interest income growth. However, we maintain our BUY rating and target price of ₹530 (unchanged) on inexpensive valuations post the recent correction, healthy tier-1 ratio at 14% and likely improvement of key business metrics from here. Among all regional banks, we like Federal Bank for its strong regional franchise, which enables the bank to directly benefit from the strong NRI deposits flowing into the country. We are valuing the bank at 1.3X book and 11X EPS.

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Slippages and credit costs remain at elevated levels

Slippages remained high at 2.8% led by higher slippages from the corporate loan portfolio (1.1%) while retail and SME continue to hold up well. One large corporate account in the pharmaceutical sector, >0.9% of total loans, slipped in the current quarter. Slippages in SME portfolio declined to 0.5% of loans, which is impressive. However, gross NPLs declined 5% qoq on an absolute basis as another large corporate account was written off in the current quarter (2.7% annualized write-offs). Gross NPLs increased to 3.5% of loans from 3.4% in March 2013 on the back of a sequential decline in advances.

Credit costs were higher at 2.2% of loans, primarily driven by 100% provisioning made for the Government account that had slipped in an earlier quarter and high write-offs. Provision coverage ratio, including technical write-offs, increased to 83% from 81% in the previous quarter. Fresh restructuring of loans was low at 0.7% of loans (annualized).

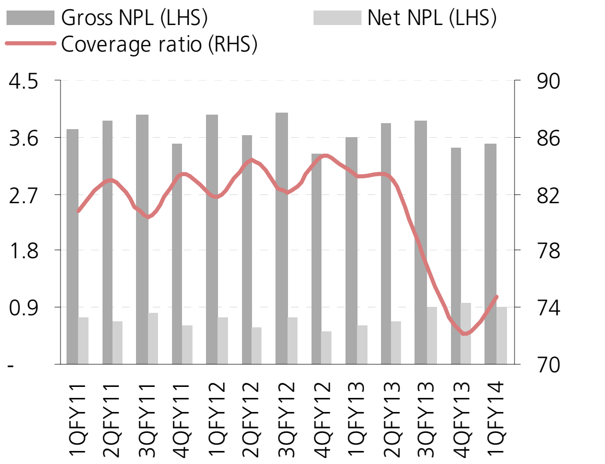
We maintain our cautious outlook on slippages and credit costs as the corporate loan portfolio has yet to stabilize despite the current management focusing on this portfolio for >2 years. We are factoring overall slippages at 2.7-2.9% for FY2014-15E and credit costs higher at 1.1%.

Exhibit 1: Slippages remain high in the corporate portfolio
Sectoral break-up of slippages, 1QFY12-1QFY14 (₹ mn)

	1QFY12	2QFY12	3QFY12	4QFY12	1QFY13	2QFY13	3QFY13	4QFY13	1QFY14
Retail	1,420	640	460	430	568	420	640	360	520
SME	1,420	1,220	900	950	972	1,050	720	1,190	710
Corporate	410	1,110	190	1,320	1,351	-	2,860	2,020	1,810
Total	**3,230**	**2,650**	**3,300**	**2,690**	**2,890**	**1,470**	**4,220**	**3,570**	**3,040**

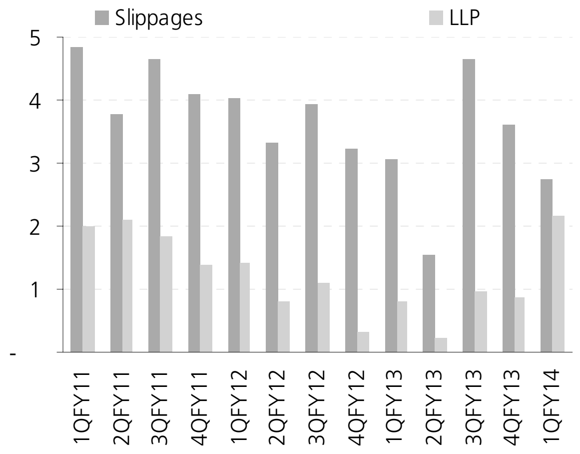
Source: Company, Kotak Institutional Equities

Exhibit 2: Coverage ratio improved in the current quarter
March fiscal year-ends, 1QFY11-1QFY14 (%)



Source: Company, Kotak Institutional Equities

Exhibit 3: Loan-loss provisioning at peak levels
March fiscal year-ends, 1QFY11-1QFY14 (%)



Source: Company, Kotak Institutional Equities

SME and retail-led loan growth

Loans grew 9% yoy (6% qoq) led by strong growth in SME (20% yoy) and retail portfolios (21% yoy) while corporate advances declined 13% yoy. All segments of loans reported a sequential decline barring SME loans, which grew a tad 2% qoq. Retail loans remained almost flat qoq, as even the gold-loan segment reported a 6% sequential decline, which we believe is due to cautious stance of the management post the sharp decline in gold prices (reduction in LTVs).

Share of corporate loans declined to 36% from 41% as of March 2013, as there was a sharp rise in the balance sheet in the end of FY2013 resulting from disbursal of short-term loans. We are building overall loan growth at 15-16% CAGR for FY2014-15E with expectation that the bank should see higher focus in retail and SME portfolios.

Growth in the gold-loan portfolio was the slowest in recent quarters as the bank appears to have focused on the NPL/pricing volatility issues. Discussions with the management indicate that there are no serious impact that is likely to emerge in the short term, but the bank is actively working with its borrowers where the value of collateral has fallen sharply as compared to the loan.

Exhibit 4: Contribution of retail and SME loans has increased in the recent quarters
Break-up of loans, March fiscal year-ends, 2008-1QFY14 (%)

	2008	2009	2010	2011	2012	2013	1QFY14
Retail	29.7	32.0	32.0	29.5	28.1	30.2	32.0
Housing	16.0	18.9	17.9	17.4	14.9	11.6	12.6
Gold loans			3.2	3.2	6.9	9.7	9.7
Others	13.6	13.1	10.9	8.9	6.3	9.0	9.7
SME	36.8	32.9	31.5	29.9	27.0	29.1	31.7
Others	33.6	35.2	36.5	40.5	44.9	40.7	36.3

Source: Company, Kotak Institutional Equities

NIM improves marginally; high share of low-cost deposits

NIM improved marginally by 6 bps qoq on the back of run-down of the low-yielding corporate loans and lower costs of funds, resulting from higher share of low-cost deposits. We note that the yields had declined significantly, almost ~100 bps in 4QFY13 as the bank expanded the balance sheet on low-yielding, short-term corporate loans.

Deposits grew 13% yoy led by 14% yoy growth in CASA deposits. CASA ratio improved 200 bps qoq to 29% on the back of increase in NRE saving deposits in the quarter. Overall saving deposits grew 8% qoq, ~95% of which was led by growth in NRE saving deposits in the quarter. We expect a further improvement in share of low-cost deposits as the strong expansion in branches has significantly increased new account mobilization, but is yet to translate into faster-than-balance-sheet growth in deposits.

We believe that NIM has scope for improvement as the improvement in funding costs should start reflecting from the current quarter while the full impact of the NRI deposit re-pricing appears to have been completed.

Exhibit 5: NRI deposits led growth in total deposits
March fiscal year-ends, 2012-1QFY14

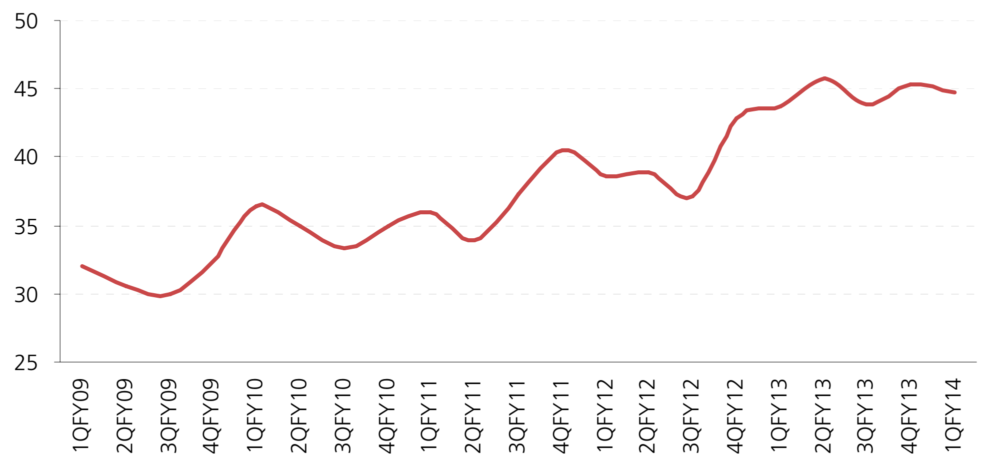
	2012	2013	1QFY14
Total deposits	489	576	570
NRI deposits	112	153	170
(% of total deposits)	22.9	26.5	29.9
NRE deposits	80	132	151
(% of total deposits)	16.3	22.8	26.5
Savings deposits		127	138
NRI		55	58
(% of saving deposits)		43.3	42.3
NRE savings		48	58
(% of saving deposits)		38.0	42.3

Source: Company, Kotak Institutional Equities

Other operational highlights for the quarter

- Non-interest income, 74% yoy, was led by high treasury gains in the current quarter (240% yoy). Core fee income reported a weak performance, increased only 1% yoy. Income from forex increased 11% yoy and 41% from recovery of written-off accounts.
- Cost-income ratio remained high at 45% though cost growth has slowed, led by weak revenue profile. The low cost-income ratio (~40%) that Federal Bank had witnessed between FY2007 and FY2012 has been replaced by an expensive model, but with weak returns. We are a bit unsure on the expected time-frame on these investments and would be wary on further investments from here.
- Tier-1 stands comfortable at 13.6% as per Basel-3 norms, with overall capital adequacy at 14.3%.

Exhibit 6: Cost-to-income ratio has increased in recent quarters
Cost-to-income ratio, March fiscal year-ends, 1QFY08-1QFY4 (%)



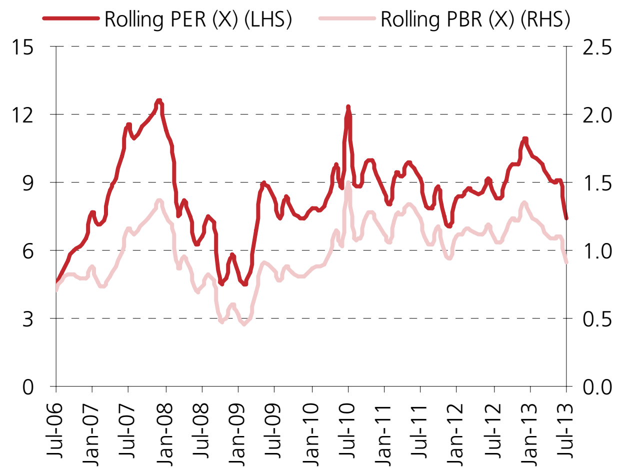
Source: Company, Kotak Institutional Equities

Exhibit 7: We marginally change our near-term earnings estimates
Old and new estimates, March fiscal year-ends, 2014-16E (₹ mn)

	New estimates			Old estimates			% change		
	2014E	2015E	2016E	2014E	2015E	2016E	2014E	2015E	2016E
Net interest income	22,017	26,122	31,412	23,111	27,041	32,057	(4.7)	(3.4)	(2.0)
NIM (%)	2.98	3.02	3.08	3.13	3.13	3.16			
Loan growth (%)	15.9	15.5	15.1	15.9	15.5	15.1			
Loan loss provisions	5,237	5,508	5,716	4,999	6,059	6,986	4.8	(9.1)	(18.2)
Other income	8,007	9,612	10,523	8,008	9,616	10,530	(0.0)	(0.0)	(0.1)
Treasury income	2,400	2,700	2,700	2,400	2,700	2,700	-	-	-
Operating expenses	13,650	15,993	18,667	13,655	16,007	18,704	(0.0)	(0.1)	(0.2)
Employee expenses	7,284	8,502	9,878	7,300	8,503	9,900	(0.2)	(0.0)	(0.2)
Net profit	**7,520**	**9,679**	**11,992**	**8,444**	**9,925**	**11,533**	**(10.9)**	**(2.5)**	**4.0**
PBT-treasury+provisions	13,974	17,042	20,568	15,065	17,949	21,183	(7.2)	(5.1)	(2.9)

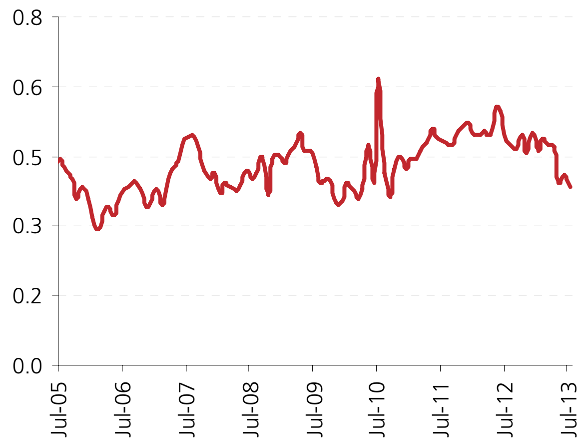
Source: Company, Kotak Institutional Equities

Exhibit 8: Federal Bank: Rolling PER and PBR (X)
July 2006-July 2013 (X)



Source: Company, Bloomberg, Kotak Institutional Equities

Exhibit 9: Federal Bank trading premium to peers
July 2006-July 2013 (X)



Source: Company, Bloomberg, Kotak Institutional Equities

Exhibit 10: Federal Bank quarterly results
March fiscal year-ends, 1QFY13-1QFY14 (` mn)

	1QFY13	2QFY13	3QFY13	4QFY13	1QFY14	% chg	1QFY14E	Actual Vs KS
Interest earned	15,367	15,256	15,218	15,835	16,533	7.6	16,975	(2.6)
Interest/discount on advances/bills	11,633	11,530	11,509	11,684	12,421	6.8	12,666	(1.9)
Income on Investments	3,552	3,542	3,582	3,970	3,971	11.8	4,147	(4.3)
Interest on balances / inter bank	167	128	115	154	132	(20.8)	132	0.3
Others								
Interest expended	10,451	10,197	10,244	11,037	11,437	9.4	11,673	(2.0)
Net interest income	**4,916**	**5,059**	**4,974**	**4,798**	**5,096**	**3.7**	**5,303**	**(3.9)**
Other Income	1,243	1,394	2,039	1,969	2,158	73.6	1,996	8.1
Fee income	303	334	328	374	307	1.3	378	(18.8)
Sale of investments	262	358	861	576	893	240.2	800	11.6
Recovery of written off assets	71	104	132	174	100	41.0	150	(33.2)
Others	364	476	512	620	588	61.7	400	47.0
Total income	6,160	6,453	7,012	6,766	7,254	17.8	7,298	(0.6)
Operating Expenses	2,695	2,957	3,073	3,071	3,249	20.6	3,157	2.9
Staff costs	1,524	1,594	1,635	1,512	1,735	13.9	1,752	(1.0)
Other operating expenses	1,171	1,362	1,438	1,560	1,514	29.3	1,405	7.7
Operating profit	**3,465**	**3,496**	**3,939**	**3,695**	**4,005**	**15.6**	**4,141**	**(3.3)**
Other Provisions and Contingencies	628	305	744	982	2,451	290.4	1,061	131.1
NPL	759	201	890	874	2,394	215.3	1,048	128.4
PBT	**2,837**	**3,192**	**3,196**	**2,713**	**1,554**	**(45.2)**	**3,080**	**(49.5)**
Provision for Taxes	934	1,041	1,088	494	498	(46.7)	933	(46.6)
Net Profit	**1,904**	**2,151**	**2,108**	**2,219**	**1,020**	**(46.4)**	**2,147**	**(52.5)**
Tax rate (%)	33	33	34	18	32			
PBT before provisions	**3,465**	**3,496**	**3,939**	**3,695**	**4,005**	**15.6**	**4,141**	**(3.3)**
Key balance sheet items (Rs bn)								
Deposits	506	495	516	576	570	12.7	593	
CASA ratio (%)	28.4	28.7	29.2	27.2	29.0			
Advances	380	363	395	441	413	8.5	445	
Retail	109	114	122	133	132	21.0		
SME and agri	109	115	121	128	131	19.8		
Others	162	134	152	179	150	(3.4)		
Investments	193	186	194	212	240	7.0		
Asset management details								
Gross Non-performing assets (Rs mn)	14,089	14,353	15,640	15,540	14,833	5.3		
Gross NPL ratio (%)	3.6	3.8	3.9	3.4	3.5			
Net Non-performing assets (Rs mn)	2,362	2,450	3,620	4,319	3,736	58.2		
Net NPL ratio (%)	0.6	0.7	0.9	1.0	0.9			
Slippages	2,890	1,470	4,220	3,570	3,040			
Slippage ratio (%)	3.1	1.5	4.7	3.6	2.8			
Yield management measures (%)								
Yield on advances	12.5	12.8	12.4	11.8	11.9			
Cost of deposits	7.6	7.6	7.6	7.6	7.4			
NIM	3.4	3.6	3.5	3.1	3.1			
Capital Adequacy details (%)								
Capital Adequacy ratio	15.5	15.8	14.9	14.7	14.3			
Tier I	14.7	15.1	14.3	14.1	13.6			

Source: Kotak Institutional Equities, Company

Exhibit 11: Federal Bank growth rates and key ratios
March fiscal year-ends, 2011-16E (%)

	2011	2012	2013	2014E	2015E	2016E
Growth rates (%)						
Net loan	18.6	18.2	16.8	15.9	15.5	15.1
Customer assets	18.0	18.9	16.0	15.5	15.1	14.9
Investments excluding CPs and debentures	8.0	17.1	25.7	23.4	30.8	28.9
Net fixed and leased assets	0.0	12.5	21.9	9.4	9.1	7.8
Cash and bank balance	37.6	(5.8)	5.3	14.9	12.7	13.0
Total assets	17.8	17.8	17.2	15.6	17.3	17.3
Deposits	19.3	13.8	17.7	17.0	18.7	18.3
Current	31.4	5.8	14.3	17.0	18.7	18.3
Savings	20.2	19.5	16.6	18.6	19.7	19.4
Fixed	18.2	12.7	18.3	16.5	18.4	18.0
Net interest income	23.8	11.8	1.1	11.5	18.6	20.2
Loan loss provisions	24.5	(41.3)	0.2	73.0	5.2	3.8
Total other income	(2.7)	3.0	24.8	20.5	20.0	9.5
Net fee income	137.7	0.5	21.1	18.0	24.0	30.0
Net capital gains	(57.5)	79.4	150.7	16.6	12.5	-
Net exchange gains	28.3	47.1	(5.7)	30.0	25.0	25.0
Operating expenses	23.5	17.1	20.5	15.7	17.2	16.7
Employee expenses	31.2	13.2	15.2	16.3	16.7	16.2
Key ratios (%)						
Yield on average earning assets	8.8	10.3	9.8	9.2	9.0	8.8
Yield on average loans	10.8	12.0	11.3	10.6	10.3	10.1
Yield on average investments	6.5	8.5	7.8	7.6	7.4	7.1
Average cost of funds	5.6	7.3	7.2	6.7	6.4	6.2
Interest on deposits	5.5	7.2	7.2	6.9	6.6	6.3
Difference	**3.2**	**2.9**	**2.5**	**2.5**	**2.5**	**2.6**
Net interest income/earning assets	3.8	3.6	3.1	3.0	3.0	3.1
New provisions/average net loans	1.7	0.9	0.7	1.1	1.0	0.9
Interest income/total income	77.2	78.6	74.8	73.3	73.1	74.9
Fee income to total income	11.1	10.1	11.5	12.0	12.5	13.8
Fees income to PBT	27.7	21.5	25.5	33.3	32.1	33.7
Net trading income to PBT	3.8	4.0	20.7	21.8	19.1	15.4
Exchange income to PBT	6.3	7.2	6.7	9.6	9.3	9.4
Operating expenses/total income	36.9	39.4	44.7	45.5	44.8	44.5
Operating expenses/assets	1.8	1.7	1.8	1.8	1.8	1.8
Operating profit /AWF	1.9	2.0	1.6	1.1	1.3	1.4
Tax rate	34.9	33.6	29.8	30.3	30.3	30.3
Dividend payout ratio	24.8	19.8	18.4	18.4	18.4	18.4
Share of deposits						
Current	5.6	5.2	5.0	5.0	5.0	5.0
Fixed	73.1	72.5	72.8	72.5	72.3	72.1
Savings	21.3	22.3	22.1	22.4	22.6	22.8
Loans-to-deposit ratio	74.3	77.2	76.5	75.8	73.8	71.8
Equity/assets (EoY)	9.9	9.4	9.0	8.5	8.0	7.7
Asset quality trends (%)						
Gross NPL	3.5	3.3	3.4	3.2	3.0	2.6
Net NPL	0.6	0.5	1.0	0.6	0.6	0.7
Slippages	3.2	2.1	2.1	2.2	2.1	2.0
Provision coverage	83.4	84.7	72.2	82.4	79.0	72.8
Dupont analysis (%)						
Net interest income	3.7	3.5	3.0	2.9	2.9	3.0
Loan loss provisions	1.1	0.5	0.5	0.7	0.6	0.5
Net other income	1.1	0.9	1.0	1.0	1.1	1.0
Operating expenses	1.8	1.7	1.8	1.8	1.8	1.8
Invt. depreciation	0.0	0.1	(0.1)	0.0	0.0	0.0
(1- tax rate)	65.1	66.4	70.2	69.7	69.7	69.7
RoA	1.2	1.4	1.3	1.0	1.1	1.1
Average assets/average equity	9.7	10.4	10.9	11.5	12.2	12.8
RoE	12.0	14.4	13.9	11.3	13.2	14.6

Source: Kotak Institutional Equities, Company

Exhibit 12: Federal Bank income statement and balance sheet
March fiscal year-ends, 2011-16E (` mn)

	2011	2012	2013	2014E	2015E	2016E
Income statement						
Total interest income	40,520	55,584	61,676	67,947	77,630	89,685
Loans	31,688	41,898	46,357	50,318	56,596	64,238
Investments	8,680	13,157	14,646	16,945	19,801	23,542
Cash and deposits	152	529	673	684	1,233	1,905
Total interest expense	23,054	36,050	41,929	45,930	51,508	58,273
Deposits from customers	21,620	33,313	38,375	42,864	48,325	54,981
Net interest income	17,466	19,534	19,747	22,017	26,122	31,412
Loan loss provisions	5,143	3,021	3,026	5,237	5,508	5,716
Net interest income (after prov.)	12,323	16,513	16,720	16,781	20,614	25,696
Other income	5,168	5,323	6,644	8,007	9,612	10,523
Net fee income	2,502	2,516	3,047	3,595	4,458	5,796
Net capital gains	458	821	2,058	2,400	2,700	2,700
Net exchange gains	572	842	794	1,032	1,290	1,613
Operating expenses	8,361	9,793	11,795	13,650	15,993	18,667
Employee expenses	4,804	5,439	6,265	7,284	8,502	9,878
Depreciation on investments	111	349	(415)	50	50	50
Other Provisions	-	-	47	300	300	300
Pretax income	9,018	11,695	11,938	10,788	13,884	17,202
Tax provisions	3,147	3,927	3,556	3,267	4,205	5,210
Net Profit	**5,871**	**7,768**	**8,382**	**7,520**	**9,679**	**11,992**
% growth	26.3	32.3	7.9	(10.3)	28.7	23.9
PBT - Treasury + Provisions	13,815	14,244	12,538	13,974	17,042	20,568
% growth	19.4	3.1	(12.0)	11.5	21.9	20.7
Balance sheet						
Cash and bank balance	37,483	35,326	37,200	42,750	48,180	54,464
Cash	3,327	3,958	5,289	5,341	5,608	5,889
Balance with RBI	26,024	20,283	22,136	27,633	32,796	38,800
Balance with banks	3,138	4,633	6,890	6,890	6,890	6,890
Net value of investments	145,377	174,025	211,546	246,431	303,590	373,875
Govt. and other securities	99,645	115,312	145,751	181,438	239,318	310,252
Shares	1,681	1,907	2,564	2,564	2,564	2,564
Debentures and bonds	6,053	9,604	8,017	7,216	6,494	5,845
Net loans and advances	319,532	377,560	440,967	511,158	590,411	679,790
Fixed assets	2,898	3,261	3,975	4,347	4,745	5,116
Other assets	9,273	16,096	16,808	16,808	16,808	16,808
Total assets	**514,564**	**606,268**	**710,496**	**821,494**	**963,734**	**1,130,053**
Deposits	430,148	489,371	576,149	673,984	799,910	946,352
Borrowings and bills payable	19,127	42,616	52,172	59,369	68,005	78,368
Other liabilities	14,203	17,218	18,528	18,528	18,528	18,528
Total liabilities	**463,477**	**549,204**	**646,849**	**751,881**	**886,443**	**1,043,248**
Paid-up capital	1,710	1,710	1,711	1,711	1,711	1,711
Reserves & surplus	49,376	55,353	61,936	67,902	75,581	85,095
Total shareholders' equity	**51,087**	**57,063**	**63,647**	**69,613**	**77,292**	**86,806**

Source: Kotak Institutional Equities, Company

kotak Institutional Equities

Hexaware Technologies (HEXW)

Technology

REDUCE

JULY 22, 2013

RESULT

Coverage view: Cautious

Price (Rs): 107

Target price (Rs): 110

BSE-30: 20,150

Revenues in line, one-offs aid margins. Hexaware reported qoq revenue growth of 0.9%, in line with expectations. Strong margin beat was aided by one-off provision reversals. Revenue growth guidance for 3QCY13 of 3.5-5.5% indicates improving growth momentum, but requires sustainability. Currency may aid margin in the near term but it is unlikely to prevail in the long term at current levels, as Hexaware will need to accelerate investments to drive sustainable revenue growth. We maintain our REDUCE rating with an increased target price of Rs110 (from Rs90).

Company data and valuation summary

Hexaware Technologies

Stock data			
52-week range (Rs) (high,low)			142-72
Market Cap. (Rs bn)			31.9
Shareholding pattern (%)			
Promoters			28.0
FIIs			46.2
MFs			6.0
Price performance (%)	1M	3M	12M
Absolute	28.9	22.1	(7.0)
Rel. to BSE-30	23.1	15.2	(20.3)

Forecasts/Valuations	2013	2014E	2015E
EPS (Rs)	11.2	12.7	12.7
EPS growth (%)	22.8	14.0	(0.6)
P/E (X)	9.6	8.4	8.4
Sales (Rs bn)	19.5	22.2	25.0
Net profits (Rs bn)	3.3	3.7	3.7
EBITDA (Rs bn)	4.1	4.8	4.8
EV/EBITDA (X)	7.3	5.6	5.5
ROE (%)	29.5	29.1	25.9
Div. Yield (%)	5.6	6.0	5.9

2QCY13 results – revenue growth as expected, one-offs help strong margin performance

Hexaware's reported revenues of US$94.8 mn (+0.9% qoq, +3.9% yoy) were in line with our estimates and the company's guidance of 0-2% growth. Revenue growth guidance of 3.5-5.5% for 3QCY13 indicates improving momentum as recently signed deals ramp up. Strong EBITDA margin expansion of 440 bps was aided by several non-operational factors – (1) about 150 bps from bonus provision reversal, a one-off, (2) 130 bps from currency depreciation and (3) about 150 bps from non-recurrence of certain one-time costs incurred in 1QCY13. Utilization was up a marginal 30 bps while onsite pricing declined 0.8%. Net income of Rs979 mn (+23.5% qoq, +10% yoy) was 14% ahead of estimates due to flow-through of beat at the EBITDA level.

Revenue growth still a struggle; further margin pressure ahead

Hexaware's yoy revenue growth has dipped to just 3.9% from almost 22% just four quarters ago. This has partly been due to project restructuring issues at the top client. However, dependence on large deal wins for growth and poor account mining of clients below the top-10 clients have also been responsible for declining revenue growth momentum. Strong 3QCY13 guidance indicates improvement on this front, but Hexaware still has a long way to go to catch up with peers on revenue growth. We estimate revenue growth of 7% in CY2013E and 10.9% in CY2014E. Despite near-term support from a weak Rupee, margins could come under pressure as the company invests in its sales force and domain capabilities to boost its revenue growth.

Balance between growth, profitability and investments critical. Retain REDUCE

Underinvestment during a phase of high growth and margin expansion have hurt Hexaware's recent performance. Building up pipeline will require fresh investments in service offerings, account management and sales capabilities. In our view, Hexaware will struggle to retain currency windfall benefits due to these investments. We have revised our OPM estimates upwards but forecast just 90 bps OPM expansion in CY2013E despite 6.5% Rupee depreciation and 250 bps decline in CY2014E. Revised currency and margin assumptions drive a 21% increase in EPS estimates. Revised target price stands at Rs110 (Rs90 earlier), valuing the stock at 9X 12-month forward earnings. Retain REDUCE.

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Key 2QCY13 result and earnings call highlights

- Volume growth for the quarter was 1.5% while impact of decline in onsite realization was 35 bps. Cross-currency movements impacted revenue growth by 35 bps.
- Banking and capital markets vertical had a strong quarter with 4.1% revenue growth while other key segments of healthcare & insurance and travel & transportation had a weak quarter with flat revenues.
- Among geographies, Americas grew 1.3% while Europe grew 0.9%.
- Hexaware indicated that it is currently chasing 4 deals over US$25 mn, with two of those in advanced stages of negotiation. Management expects these deals to close in 2HCY13.
- Regarding its investment plan, Hexaware outlined that it intends to add 8-10 heads to its front-end sales team and 7-8 BFS domain experts in consulting and BI. These will be funded by gains from currency. It will also look to improve its account management structure with greater focus on mining top 21-50 accounts.
- End-period headcount increased to 8,700, a net addition of 30 from 1QCY13. Attrition increased marginally to 11% from 9.9% in the previous quarter.
- Utilization was up 30 bps to 70.9% from 70.6% in the previous quarter. Onsite billing rates were down 0.8% due to ramp-up of recently signed deals. Offshore billing rate was flat qoq.
- The DSO days including unbilled revenues were 63 days, down from 71 days in the previous quarter. DSO excluding unbilled revenues also declined to 47 days from 53 days in 1QCY13.
- The total outstanding hedges stood at US$226 mn at an average USD-INR rate of 56.26 and EUR13 mn at an average EUR-INR rate of 74.14. The hedges mature over the next eight quarters.

Exhibit 1: Key changes in CY2013-14E estimates

	New		Old		Change (%)	
	2013	2014	2013	2014	2013	2014
Revenues (US$ mn)	**390**	**432**	**389**	**426**	**0.2**	**1.5**
Revenue growth (%)	7.0	10.9	6.8	9.3		
EBITDA Margin (%)	21.8	19.3	19.3	18.0		
Recurring EPS (Rs/ share)	**12.7**	**12.7**	**10.5**	**10.4**	**21.5**	**21.4**
Re/ US$ rate	57.0	57.8	55.3	55.9	3.0	3.4

Source: Kotak Institutional Equities estimates

Exhibit 2: Hexaware - consolidated quarterly results, December year-ends, 2QCY13 (Rs mn)

	2QCY12	1QCY13	2QCY13	% chg. qoq	% chg. yoy	Kotak estimates	% deviation
Revenue (US$ mn)	**91.2**	**94.0**	**94.8**	**0.9**	**3.9**	**94.5**	**0.3**
Revenues	**5,001**	**5,077**	**5,366**	**5.7**	**7.3**	**5,386**	**(0.4)**
Software Development Costs	(2,995)	(3,162)	(3,252)	2.8	8.6	(3,292)	(1.2)
Gross profit	**2,006**	**1,915**	**2,114**	**10.4**	**5.4**	**2,094**	**0.9**
Total SG&A Expenses	(859)	(936)	(841)	(10.1)	(2.1)	(957)	(12.1)
EBITDA	**1,147**	**979**	**1,273**	**30.0**	**11.0**	**1,138**	**11.9**
Depreciation	(76)	(93)	(94)	1.1	23.7	(108)	(13.1)
EBIT	**1,071**	**886**	**1,179**	**33.1**	**10**	**1,030**	**14.5**
Other Income	49	118	62	(47)	27	83	(25)
Profit Before Tax	**1,120**	**1,004**	**1,241**	**23.6**	**10.8**	**1,112**	**11.6**
Provision for Tax	(230)	(211)	(262)	24.2	13.9	(255)	2.9
Net Profit	**890**	**793**	**979**	**23.5**	**10.0**	**858**	**14.1**
Extraordinary items	—	—	—			—	
Net Profit- Reported	**890**	**793**	**979**	**23.5**	**10.0**	**858**	**14.1**
Recurring EPS (Rs/share)	3.0	2.7	3.3	23.5	10.0	2.9	14.1
No of shares outstanding (mn)	293.4	293.4	293.4			293.4	
As % of revenues							
Gross Margin (%)	40.1	37.7	39.4			38.9	
EBITDA Margin	**22.9**	**19.3**	**23.7**			**21.1**	
SG&A Expenses (%)	17.2	18.4	15.7			17.8	
Billing Rates (US$/manhour)							
Onsite	73.5	73.6	73.1	(0.8)	(0.6)		
Offshore	22.9	23.4	23.4	0.1	2.4		
Revenue Mix (%)							
Onsite	53.4	52.4	52.5				
Offshore	46.6	47.7	47.5				

Hexaware has guided revenues for 3QCY13 to be US$98.1-100 mn, an increase of 3.5-5.5% qoq

Source: Company, Kotak Institutional Equities estimates

Exhibit 3: Hexaware: Key operational metrics

	Jun-11	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12	Mar-13	Jun-13
Revenues (US$ mn)	74.8	78.8	84.1	88.0	91.2	92.8	92.4	94.0	94.8
qoq growth (%)	6.2	5.3	6.7	4.6	3.6	1.8	(0.4)	1.7	0.9
Revenues (Rs mn)	3,341	3,660	4,319	4,383	5,001	5,075	5,023	5,077	5,366
Exchange rate	44.67	46.45	51.36	49.81	54.84	54.69	54.36	54.01	56.60
Revenue by verticals (%)									
Banking & capital markets	27.4	28.6	28.5	27.3	28.7	32.3	33.7	34.4	35.5
Healthcare & Insurance	13.0	13.6	16.4	17.3	16.3	15.2	16.3	16.0	15.9
Travel & transportation	24.6	23.2	20.7	22.0	19.8	20.1	20.2	19.6	19.5
Emerging segments	35.0	34.6	34.4	33.4	35.2	32.4	29.8	30.0	29.1
Revenue by service lines (%)									
ADM	39.2	40.5	39.7	38.9	38.3	38.4	35.8	37.9	38.1
EAS	31.3	30.5	29.8	28.9	32.3	30.6	30.1	29.1	29.0
Testing / BTO	9.4	9.2	10.8	10.5	8.9	9.8	11.6	12.0	13.0
Business intelligence & analytics	9.9	9.6	10.5	12.5	10.6	11.6	12.8	11.0	10.2
BPO	5.7	5.7	5.1	4.7	4.8	4.3	4.0	4.3	4.3
Others	4.5	4.5	4.1	4.5	5.1	5.3	5.7	5.7	5.4
Revenue by geographies (%)									
Americas	66.4	64.7	64.4	63.8	63.3	65.1	69.2	66.8	67.1
Europe	27.2	28.4	28.7	29.6	29.2	27.4	23.2	26.3	26.3
Rest of the world	6.4	6.9	6.9	6.6	7.5	7.5	7.6	6.9	6.6
Onsite-Offshore mix (%)									
Onsite	56.7	53.7	55.1	53.4	53.4	53.4	54.6	52.4	52.5
Offshore	43.3	46.3	44.9	46.6	46.6	46.6	45.4	47.7	47.5
Client metrics									
Repeat business (%)	92.5	93.5	94.1	94.3	93.2	93.2	93.4	94.6	95.6
Clients billed	190	194	192	201	210	217	218	216	219
Clients added	14	12	15	12	12	12	11	11	14
Revenue concentration (%)									
Top 1 client	12.5	13.6	13.9	14.8	14.8	14.8	11.7	13.0	13.8
Top 5 clients	38.3	38.3	38.9	38.9	37.8	36.3	36.0	36.8	37.9
Top 10 clients	51.8	52.5	52.6	52.7	51.7	50.9	51.1	51.2	53.1
Client size (ttm)									
> US$1 mn	50	51	52	55	57	57	55	55	53
Between US$1 mn - US$5 mn	40	39	40	42	44	43	40	40	37
Between US$5 mn - US$10 mn	6	8	7	7	7	7	7	7	8
> US$10 mn	4	4	5	6	6	7	8	8	8
Billing rates (US$/hr)									
Onsite	72.0	72.5	73.0	73.9	73.5	73.5	74.3	73.6	73.1
Offshore	22.5	23.0	23.0	22.9	22.9	23.0	23.2	23.4	23.4
Employee metrics									
Total employees (consolidated)	7,419	8,164	8,317	8,624	8,733	9,143	9,069	8,670	8,700
Billable personnel (%)									
Onsite (%)	19.6	18.7	18.8	18.5	18.6	18.8	19.3	18.1	18.8
Offshore (%)	71.9	73.0	72.9	73.4	73.5	73.4	73.0	73.6	72.9
Marketing (incl sales support - %)	2.0	1.8	1.8	1.8	1.9	2.0	1.9	2.0	2.0
Others (incl tech support - %)	6.5	6.5	6.5	6.3	6.0	5.8	5.8	6.3	6.3
Utilization (%)	71.4	70.6	69.7	68.6	70.0	67.6	63.9	70.6	70.9
Attrition rate (%) LTM	18.0	14.7	13.9	11.0	9.6	8.4	8.7	9.9	11.0
DSO - Billed	55	57	62	52	45	56	66	53	47
DSO - including unbilled accruals	71	74	72	72	66	77	77	71	63

Source: Kotak Institutional Equities

Exhibit 4: Consolidated financials for Hexaware, December year-ends, 2010-14E (Rs mn)

	2010	2011	2012	2013E	2014E
Profit model					
Total income	10,546	14,505	19,482	22,210	24,967
EBITDA	**938**	**2,646**	**4,074**	**4,834**	**4,828**
Depreciation and ammortisation	(242)	(248)	(324)	(316)	(387)
Other income	249	677	290	283	342
Pretax profits	**945**	**3,076**	**4,041**	**4,801**	**4,784**
Tax	(92)	(407)	(764)	(1,066)	(1,071)
Profit after tax	**853**	**2,669**	**3,277**	**3,735**	**3,713**
Diluted recurring EPS (Rs/share)	**3.0**	**9.1**	**11.2**	**12.7**	**12.7**
Balance sheet					
Total equity	9,655	10,162	12,039	13,588	15,129
Deferred taxation liability	(169)	(162)	(73)	(73)	(73)
Current liabilities	2,785	4,331	3,616	3,901	4,179
Total liabilities and equity	**12,382**	**14,331**	**15,581**	**17,416**	**19,235**
Cash	4,356	4,377	1,969	4,625	5,225
Other current assets	3,551	4,939	6,058	7,090	7,779
Tangible fixed assets	4,078	4,785	5,199	5,701	6,231
Total assets	**12,382**	**14,331**	**15,581**	**17,416**	**19,235**
Free cash flow					
Operating cash flow, excl. WC	1,089	2,558	3,409	3,542	3,873
Working capital changes	(836)	(1,187)	(1,186)	(746)	(411)
Capital expenditure	(340)	(633)	(744)	(818)	(917)
Free cash flow	**(88)**	**738**	**1,480**	**1,977**	**2,545**
Ratios (%)					
EBITDA margin	8.9	18.2	20.9	21.8	19.3
ROE	9.4	26.9	29.5	29.1	25.9
ROCE	6.8	20.9	27.4	27.4	24.0

Source: Company, Kotak Institutional Equities estimates

Rallis India (RALI)

Others

BUY

JULY 22, 2013

RESULT

Coverage view:

Price (Rs): 152

Target price (Rs): 165

BSE-30: 20,150

Metahelix offsets a weak quarter for agri-chem. Rallis reported an in-line 1QFY14. While standalone agri-chem business disappointed on sales front (flat yoy), Metahelix threw a big positive surprise with sales up 2X yoy. As per the management, product placements (agri-chem) could have been higher at the cost of sacrificing working capital discipline, which it did not do and instead chose to place closer to the actual usage (Jul-Aug). In our view, Metahelix will reach a critical size in FY2014E after which scale-up in profits could be substantial. We have increased estimates for Metahelix and revised them downwards for SA business. Retain BUY (target price Rs165; Rs155 earlier).

Company data and valuation summary

Rallis India

Stock data			
52-week range (Rs) (high,low)			170-110
Market Cap. (Rs bn)			29.6
Shareholding pattern (%)			
Promoters			50.1
FIIs			10.6
MFs			4.4
Price performance (%)	1M	3M	12M
Absolute	8.6	20.2	17.5
Rel. to BSE-30	3.8	13.4	0.8

Forecasts/Valuations	2013	2014E	2015E
EPS (Rs)	6.1	8.5	10.2
EPS growth (%)	20.0	38.2	20.6
P/E (X)	24.8	18.0	14.9
Sales (Rs bn)	14.6	17.2	19.4
Net profits (Rs bn)	1.2	1.6	2.0
EBITDA (Rs bn)	2.1	2.8	3.2
EV/EBITDA (X)	14.4	10.6	9.1
ROE (%)	18.9	24.0	24.6
Div. Yield (%)	1.5	1.4	1.4

Metahelix compensates for a weak standalone quarter

Rallis reported a weak quarter for the SA agri-chem business as sales were flat yoy. Performance is particularly disappointing as (1) trends in monsoons have been good so far and (2) 1Q is anyway a placement quarter for the company as insecticides comprise the dominant part of the portfolio (usage of insecticides/fungicides starts post June). Given lackluster sales, 1QFY14 EBITDA (SA) margins at 9.4% were also under pressure (down ~90 bps yoy). As per the management, it could have placed more stock at the cost of working capital discipline, which it did not do and instead chose to sell products near their usage period (Jul-Aug). Hence, over the kharif season (Apr-Sep) growth in sales should be good. Consolidated results were in line as Metahelix reported a superlative 1QFY14. The company reported consolidated sales, EBITDA and PAT at Rs4.1 bn (+19% yoy; +45% qoq), Rs553 mn (+33% yoy; +96% qoq) and Rs275 mn (+14% yoy; +144% qoq) respectively.

Metahelix delivers a blockbuster quarter—profits could scale up significantly from here

Metahelix delivered a superlative quarter. Sales (represented by consol-standalone) at Rs1.4 bn almost doubled yoy. 1QFY14 EBITDA at Rs297 mn grew more than 2X from Rs134 mn in 1QFY13. In our view, Metahelix will achieve a critical level of sales (Rs2-2.5 bn) in FY2014E versus our earlier expectation of FY2016E. As per our understanding, profits could scale up significantly once the critical level of sales is achieved; the current quarter marks a watershed in this regard.

Adjusting our estimates; retain BUY with a revised target price of Rs165 (Rs155 earlier)

We have lowered our estimates for the standalone agri-chemical business. We are now estimating SA margins at 16.8% for FY2014/15/16E versus 18% earlier. We have increased our earning estimates for Metahelix. We are now estimating Metahelix sales at Rs2.2 bn, Rs2.8 bn and Rs3.4 bn versus Rs1.7 bn, Rs1.85 bn and Rs2 bn earlier in FY2014/15/16E respectively. Also, we have scaled up our estimates of EBITDA to Rs255 mn, Rs390 mn and Rs470 mn from Rs140 mn, Rs266 mn and Rs294 mn earlier in FY2014/15/16E respectively. We retain our BUY rating with a revised target price of Rs165 (at 16X FY2015E EPS).

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Exhibit 1: In-line quarter—Metahelix offset a weak quarter for the standalone business
Interim results of Rallis, consolidated, March fiscal year-ends (Rs mn)

					% change		
	1QFY14	1QFY14E	4QFY13	1QFY13	Est	qoq	yoy
Sales	**4,119**	**4,032**	**2,849**	**3,453**	**2**	**45**	**19**
Raw material cost	(2,117)	—	(1,760)	(1,894)		20	12
Employee cost	(295)	—	(219)	(268)		35	10
Other expenses	(1,155)	—	(588)	(876)		96	32
EBITDA	**553**	**553**	**282**	**415**	**(0)**	**96**	**33**
Other income/forex gain/(loss)	(69)	10	18	44			
Depreciation and amortization	(90)	(85)	(84)	(74)			
Interest cost	(34)	(33)	(33)	(52)			
Extraordinaries	-	-	—	-			
Profit before tax	**360**	**445**	**183**	**333**	**(19)**	**97**	**8**
Tax (net)	(27)	(101)	(79)	(62)			
Net income	**333**	**344**	**104**	**271**	**(3)**	**220**	**23**
Minority interest	58	(8)	(8)	29			
Adjusted net income	**275**	**352**	**113**	**242**	**(22)**	**144**	**14**
Margins (%)							
Gross margins	48.6		38.2	45.1			
EBITDA	13.4	13.7	9.9	12.0			
Other exp/sales	28.0		20.6	25.4			
Emp. Cost/sales	7.2		7.7	7.8			

Note:
Other income includes forex loss of Rs79.8 mn on trade payables.

Source: Company, Kotak Institutional Equities

Exhibit 2: Metahelix delivered a blockbuster quarter
Consol-standalone numbers for Rallis, March fiscal year-ends (Rs mn)

	1QFY13	2QFY13	3QFY13	4QFY13	1QFY14
Income	755	198	195	196	1,418
EBITDA	134	(32)	(16)	(13)	297
PBT	117	(52)	(40)	(36)	273
PAT (before minority int.)	117	(52)	(40)	(31)	273

Source: Company, Kotak Institutional Equities

Metahelix delivers a blockbuster quarter—profits could scale up significantly from here

Metahelix delivered a superlative quarter. Sales (represented by consol-standalone) at Rs1.4 bn almost doubled yoy. 1QFY14 EBITDA at Rs297 mn grew more than 2X from Rs134 mn in 1QFY13. In our view, Metahelix will achieve a critical level of sales (Rs2-2.5 bn) in FY2014E versus our earlier expectation of FY2016E. As per our understanding, profits could scale up significantly once the critical level of sales is achieved; the current quarter marks a watershed in this regard.

As per our understanding, Metahelix is placed well versus competition in hybrid paddy, pearl millets and corn. In hybrid paddy, the company is among the top 3 in India. Hybrid paddy represents a large opportunity for the company as currently hybridization is only 4-5% in India, and is expected to increase to 25% in the next five years. The company is also focusing on hybrid seeds for vegetables. As of now, it has seeds for okra, chillies and melons in its portfolio.

Exhibit 3: Standalone business disappoints—sales growth much lower versus estimates
Quarterly results for Rallis, standalone, March fiscal year-ends (Rs mn)

	3QFY12	4QFY12	1QFY13	2QFY13	3QFY13	4QFY13	1QFY14	% change qoq	% change yoy
Net sales from operations	3,028	1,895	2,628	4,612	3,204	2,593	2,676	3	2
Other operating income	70	100	70	46	26	60	26	(57)	(63)
Total income	**3,098**	**1,994**	**2,698**	**4,658**	**3,230**	**2,653**	**2,702**	**2**	**0**
Raw material cost	(1,835)	(1,214)	(1,627)	(2,988)	(2,032)	(1,715)	(1,660)	(3)	2
Employee cost	(208)	(177)	(213)	(175)	(201)	(180)	(226)	26	6
Other expenditure	(484)	(472)	(578)	(496)	(514)	(462)	(560)	21	(3)
EBITDA	**570**	**132**	**281**	**999**	**482**	**295**	**256**	**(13)**	**(9)**
Depreciation	(69)	(82)	(68)	(71)	(73)	(76)	(79)		
Other income/forex gain/(loss)	(62)	71	43	41	(12)	18	(70)		
Interest (net)	(29)	(16)	(39)	(39)	(28)	(18)	(20)		
Exceptional items	(242)	71	—	—	—	—	—		
PBT	**168**	**175**	**216**	**930**	**369**	**219**	**87**	**(60)**	**(60)**
Tax	(57)	(57)	(62)	(273)	(121)	(83)	(27)		(57)
PAT	**111**	**118**	**154**	**657**	**248**	**135**	**60**	**(56)**	**(61)**
Ratio analysis (%)									
Gross margin	40.8	39.1	39.7	35.8	37.1	35.3	38.6		
EBITDA margin	18.4	6.6	10.4	21.4	14.9	11.1	9.5		
Employee cost/sales	6.7	8.9	7.9	3.7	6.2	6.8	8.4		
Other expenditure/sales	16.0	24.9	22.0	10.7	16.1	17.8	20.9		

Source: Company, Kotak Institutional Equities

Standalone business—gross margins improve (qoq) while EBITDA margins lower than estimates

Gross margins for the standalone business improved from 35.3% in 4QFY13 to 38.6% in 1QFY14, reflecting the price increase that the company has taken in the quarter. EBITDA margins were below estimates at 9.5%, down ~90 bps yoy. As per the management, it will take further price increase in 2QFY14, which should partially offset the impact of Rupee depreciation on margins.

Other highlights

- One of the export orders of the company has been deferred to 2QFY14, which has resulted in export revenues declining yoy. Adjusting for that, domestic agri-chem revenues are up yoy.
- The company has taken a price increase in 1QFY14. It will take further price increase in 2QFY14 as well.
- Metahelix could have sold more of some hybrids, especially corn. The company underestimated demand and hence production was lower versus demand.
- The company has already provided for possible sales returns in the case of seeds in 1QFY14 as per historical trends. Only in case sales returns are higher versus historical trends, the company would have to take a hit in the coming quarters.

Adjusting our estimates; retain BUY with a revised target price of Rs165 (Rs155 earlier)

We have lowered our estimates for the standalone agri-chemical business. We are now estimating SA margins at 16.8% for FY2014/15/16E versus 18% earlier. We have increased our earning estimates for Metahelix. We are now estimating Metahelix sales at Rs2.2 bn, Rs2.8 bn and Rs3.4 bn versus Rs1.7 bn, Rs1.85 bn and Rs2 bn earlier in FY2014/15/16E respectively. Also, we have scaled up our estimates of EBITDA to Rs255 mn, Rs390 mn and Rs470 mn from Rs140 mn, Rs266 mn and Rs294 mn earlier in FY2014/15/16E respectively. We retain our BUY rating with a revised target price of Rs165 (at 16X FY2015E EPS).

Exhibit 4: Assumptions for Rallis, consolidated, March fiscal year-ends (Rs mn)

	2012	2013	2014E	2015E	2016E
Sales	**12,749**	**14,582**	**17,165**	**19,376**	**21,678**
Standalone	11,813	13,238	15,010	16,575	18,317
Metahelix (a)	936	1,344	2,155	2,801	3,362
EBITDA	**2,030**	**2,106**	**2,802**	**3,205**	**3,581**
Standalone	1,973	2,032	2,522	2,785	3,077
Metahelix	57	73	280	420	504
EBITDA (%)					
Standalone	16.7	15.4	16.8	16.8	16.8
Metahelix	6.09	5.47	13.00	15.00	15.00

Note:
(a) Metahelix numbers have been computed by substracting standalone numbers from consol.

Source: Company, Kotak Institutional Equities

Exhibit 5: Summary financials: Rallis
Profit model, cash flow statement and balance sheet for Rallis, consolidated, March fiscal year-ends (Rs mn)

	2009	2010	2011	2012	2013	2014E	2015E	2016E
Profit model (Rs mn)								
Sales	8,562	9,005	10,934	12,749	14,582	17,165	19,376	21,678
EBITDA	**1,303**	**1,667**	**1,991**	**2,030**	**2,106**	**2,802**	**3,205**	**3,581**
Other income	33	70	69	69	117	90	103	161
Interest	(34)	(27)	(40)	(146)	(185)	(102)	(28)	(28)
Depreciation	(229)	(183)	(175)	(287)	(315)	(366)	(390)	(426)
Extraordinardy items	—	—	—	(172)	—	—	—	—
Profit before tax	**1,072**	**1,527**	**1,845**	**1,494**	**1,723**	**2,424**	**2,891**	**3,289**
Tax expense	(352)	(512)	(580)	(487)	(535)	(731)	(824)	(913)
Minority interest	—	—	—	15	(2)	48	83	102
Extraordinardy items	—	—	—	—	—	—	—	—
PAT	**720**	**1,015**	**1,264**	**992**	**1,190**	**1,644**	**1,983**	**2,275**
EPS	3.7	5.2	6.5	5.1	6.1	8.5	10.2	11.7
Balance sheet (Rs mn)								
Equity	2,617	4,245	5,049	5,530	6,207	7,353	8,837	10,613
Preference capital	880	—	—	—	—	—	—	—
Total borrowings	825	81	1,172	1,523	1,314	220	220	220
Deferred tax liability/minority interest	(102)	(53)	54	145	328	377	460	562
Current liabilities and provisions	2,608	3,041	3,891	4,028	4,047	4,204	4,732	5,286
Total liabilites	**6,828**	**7,314**	**10,167**	**11,226**	**11,897**	**12,153**	**14,249**	**16,681**
Net fixed assets	1,877	2,648	4,009	4,236	4,223	4,323	4,334	4,708
Goodwill	—	—	1,236	1,533	1,676	1,676	1,676	1,676
Investments	1,362	1,402	256	227	197	197	197	197
Cash	82	119	146	112	258	(110)	319	1,369
Other current assets and miscellaneous	3,509	3,145	4,520	5,118	5,542	6,066	7,722	8,731
Total assets	**6,828**	**7,314**	**10,167**	**11,226**	**11,897**	**12,152**	**14,249**	**16,681**
Free cash flow (Rs mn)								
Operating cash flow	987	1,073	1,271	1,453	1,764	2,204	2,486	2,778
Working capital changes	403	1,079	(284)	(507)	(321)	(502)	(1,232)	(563)
Capital expenditure	(644)	(949)	(1,378)	(570)	(349)	(466)	(400)	(800)
Free cash flow	**747**	**1,203**	**(391)**	**376**	**1,094**	**1,236**	**854**	**1,415**
Ratios								
EBITDA margin (%)	15.2	18.5	18.2	15.9	14.4	16.3	16.5	16.5
Net debt/equity (X)	0.28	(0.01)	0.20	0.26	0.17	0.04	(0.01)	(0.11)
Book value (Rs/share)	13.5	21.8	26.0	28.4	31.9	37.8	45.4	54.6
ROAE (%)	29.0	28.2	26.2	20.4	18.9	24.0	24.6	23.2
ROACE (%)	18.9	23.2	23.6	17.4	16.4	21.5	23.0	21.8

Source: Company, Kotak Institutional Equities

kotak Institutional Equities

Magma Fincorp (MGMA)

Banks/Financial Institutions

BUY

JULY 22, 2013

RESULT

Coverage view: Cautious

Price (Rs): 88

Target price (Rs): 125

BSE-30: 20,150

Slowing down. Slowdown in autos (primarily CVs/CEs) affected Magma's business—loan book was flat qoq in 1QFY14 and collection efficiency dropped to 95% from 98% last quarter even as reported earnings were in line with estimates. Higher NIM (due to re-pricing of loan assets), increase in share of income-earning loans and better operating efficiency will likely drive earnings even as loan growth moderates and credit cost moves up. We revise down our earning estimates and price target to Rs125 (from Rs135 earlier). Retain BUY on the back of inexpensive valuations.

Company data and valuation summary

Magma Fincorp

Stock data			
52-week range (Rs) (high,low)			111-59
Market Cap. (Rs bn)			16.7
Shareholding pattern (%)			
Promoters			33.7
FIIs			43.6
MFs			0.3
Price performance (%)	**1M**	**3M**	**12M**
Absolute	3.2	2.3	27.7
Rel. to BSE-30	(1.5)	(3.4)	9.5

Forecasts/Valuations	2013	2014E	2015E
EPS (Rs)	6.5	10.2	12.3
EPS growth (%)	100.6	55.6	21.0
P/E (X)	13.5	8.7	7.2
NII (Rs bn)	7.8	9.8	11.8
Net profits (Rs bn)	1.2	1.9	2.3
BVPS	73.5	81.8	91.9
P/B (X)	1.2	1.1	1.0
ROE (%)	10.1	12.7	14.0
Div. Yield (%)	1.3	1.8	2.2

Earnings in line, growth and asset quality performance weak

Magma reported PAT of Rs454 mn, up 37% yoy, 5% ahead of estimates. NIM (calculated) increased 20 bps yoy to 5% though declined qoq. With its focus on maintaining expenses, cost-to-income ratio was flat at 56% qoq, lower than 62% in 1QFY13. Other operating trends were, however, weak:

- The ongoing slowdown in autos, specifically CVs and CEs (construction equipments), has affected Magma's business. Loan book was flat qoq at Rs162 bn, up 28% yoy. 8% qoq decline in CVs, flat CE and used CV loan book offset loan growth in cars and tractors (cars were up 4% qoq and tractors were up 9% qoq).

- Magma's gross NPLs increased to 2.2% from 1.6% in 4QFY13 largely due to lower (90%) collections in CV portfolio. The overall collections declined to 95% from 98% in FY2013.

Revise estimates, retain BUY rating

Post 1QFY14 results, we are revising down our earnings estimates by 8-10% to factor lower loan growth and higher credit cost, somewhat offset by lower operating expenses. We revise our price target to Rs125 (from Rs135). At our price target, Magma will trade at 1.5X and 1.4X PBR FY2014E and FY2015E respectively. We model medium-term RoE of 14-16% even as near-term ratio will be lower at about 13%. At the current market price, the stock trades at 1X PBR FY2015E. In light of the inexpensive valuations, we retain BUY rating on the stock.

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Loan book flat, guidance cautious

Magma's loan book remained flat qoq as most segments, barring tractors and cars, declined in the current quarter. Overall disbursements were weak at Rs19 bn, compared to an average of over Rs20 bn in the past few quarters. Commercial vehicle loans declined 8% qoq, due to decline in underlying CV sales in the quarter. Tractor loans grew 9% qoq (51% yoy), following surprisingly strong traction in tractor sales in the industry, primarily from Andhra Pradesh, Madhya Pradesh and Maharashtra. In light of the slowdown in vehicle sales, we expect mortgages (housing and LAP) and SME loans to drive business. On the back of weak operating environment, we are reducing our loan growth estimate to 17% for FY2014E from 24% earlier.

Asset quality deteriorates in CVs and CEs; we model higher credit costs

Magma's gross NPLs increased to 2.17% of gross loans compared to 1.63% in March 2013, resulting from decline in collection efficiency to 95.5% from 98.2% in FY2013, particularly in the CV and CE segments. Collection in the CVs declined to 91% from 95.7% in the previous quarter. The asset quality has been on track for most other segments.

In light of the stress in the underlying business environment, we will monitor the trends in collections cautiously—we expect credit costs to remain high at 0.6-0.75% of loans over FY2014-16E compared to 0.6% in FY2012 and 0.2-0.3% over FY2011-12.

Margins improve qoq

Magma Finance's NIM increased 14 bps qoq to 5.54% from 5.4% in 4QFY13 (4.91% for FY2013). Reported yield on advances increased 26 bps due to rundown in low-yielding book and higher yield on recent disbursements. Reported cost of funds declined by 37 bps due to lower interest rates in the system and a change in the borrowing mix—higher share of borrowings funded through the debt capital markets (21%) as compared to 13% in FY2012. High yield on recent disbursements and rising share of income-earnings loan assets (97% from 90% last year) will likely buoy spreads in FY2014E as well—we assume 40 bps rise in NIM in FY2014E versus 100 bps rise in FY2013.

Operating costs decline

Costs to average AUMs declined to 3.1% from 3.6% in 4QFY13 (3.3% for FY2013). On an absolute basis, operating expenses were down 6% qoq, resulting from strong management focus on reducing costs to increase productivity. We note that the integration of the housing finance business is fully complete and may not result in incremental costs though the general insurance business poses a risk. We model cost-to-average AUMs of 3.0-3.1% over FY2014-15E.

Exhibit 1: Auto finance business is slowing down across banks and NBFCs
Qoq loan growth in auto finance, March fiscal year-ends, 2QFY12-1QFY14 (%)

	2QFY12	3QFY12	4QFY12	1QFY13	2QFY13	3QFY13	4QFY13	1QFY14
Axis Bank								
Auto finance	9	13	13	8	9	0	31	(10)
HDFC Bank								
Car loans	6	5	2	4	5	4	3	4
2W	5	11	5	5	4	7	2	0
CVs	25	11	4	11	14	(1)	(2)	5
IndusInd Bank								
CVs	10	10	11	7	8	2	2	2
Uvs	11	11	10	15	12	10	2	8
Cars	14	13	14	15	12	10	3	8
2W	8	10	6	5	6	9	6	5
3W	13	9	4	5	6	3	(3)	0
Equipments	7	15	9	10	6	8	1	5
Magma Fincorp								
Car	(0)	(6)	4	(2)	4	(2)	(12)	3
CV	(6)	(12)	(6)	(11)	(6)	(12)	(24)	(8)
CE	(5)	(18)	0	(10)	0	(11)	(22)	0
Used CV	3	13	0	14	0	10	(24)	0
Tractor	14	1	0	4	9	2	(19)	8

Source: Company

Exhibit 2: Magma Finance—consolidated quarterly results
March fiscal year-ends, 1QFY13-1QFY14 (Rs mn)

	1Q13	2Q13	3Q13	4Q13	1Q14	YoY (%)	1Q14E	Act vs KS (%)
Income statement								
Interest income	3,213	3,769	4,240	4,758	4,852			
Interest expenses	1,853	2,226	2,522	2,661	2,820			
Net interest income	1,360	1,543	1,718	2,097	2,032	49	2,132	(5)
Provisions	117	170	173	365	361	208	410	(12)
NII post provisions	1,206	1,338	1,498	1,712	1,659	38	1,698	(2)
Other income	39	50	-	-	-	(100)	-	-
Other operational income	267	164	216	301	245	(8)	300	(18)
Operating expnenses	1,027	1,127	1,149	1,359	1,276	24	1,360	(6)
Employees	476	466	491	607	548	15	550	(0)
Other operating expenses	428	586	569	663	642	50	720	(11)
Depreciation	123	76	89	89	86	(30)	90	(4)
PBT	485	425	565	654	629	30	638	(1)
Tax	154	141	183	197	175	13	204	(15)
PAT	331	284	382	457	454	37	434	5
Pref. dividends	70	70	50	-	-	-	-	-
PAT post pref divd	261	214	332	457	454	74	434	5
Minority interest	20	16	16	-	17	-	-	-
PAT post minority interest	241	198	316	457	437	82	434	1
Tax rate (%)	31.8	33.1	32.4	30.1				
Total AUM	**127,270**	**135,330**	**143,380**	**162,400**	**162,740**	**28**	**171,332**	**(5)**
On books	83,560	98,050	98,740	108,808	114,480	37	118,601	(3)
Off books	43,710	37,280	44,640	53,592	48,260	-	52,731	(8)
Loan book	**127,270**	**135,330**	**143,380**	**162,400**	**162,740**	**28**		
Car	35,636	39,246	43,014	48,720	50,449	42		
CV	40,726	40,599	40,146	38,976	35,803	(12)		
CE	22,909	24,359	24,375	24,360	24,411	7		
Used CV	7,636	8,120	10,037	9,744	9,764	28		
SME loans	6,364	6,767	7,169	8,120	8,137	28		
Tractor	14,000	16,240	18,639	19,488	21,156	51		
Mortgages	-	-	-	12,992	13,019	-		
Balance sheet consolidated								
Liabilities	**93,793**	**109,268**	**115,471**	**131,138**	**131,858**	**41**		
Shareholders funds	11,326	12,239	12,595	13,974	14,413	27		
Preference capital (+share application money	1,297	1,472	1,657	1,970	1,845	42		
Minority interest	208	225	240	255	272	31		
Non current liabilities	24,733	26,793	32,214	40,067	41,162	66		
Current Liabilities & Provisions	56,229	68,539	68,765	74,872	74,166	32		
Assets	**93,792**	**109,266**	**115,476**	**131,137**	**131,859**	**41**		
Fixed assets	1,693	1,701	1,735	1,902	1,832	8		
Investment	260	165	1,768	2,669	3,138	1,107		
Long term loans and advances	51,889	61,055	61,141	74,319	73,657	42		
Cash & Bank Balances	5,325	6,133	9,594	12,178	7,733	45		
other current assets & loans & advances	34,625	40,212	41,238	40,069	45,499	31		
Other details (%)								
NIM reported	4.2	4.7	5.1	5.4	5.5			
NIM (KS calc)	4.9	5.0	5.4	6.2	5.8			
Cost to income	61.6	64.2	59.4	56.7	56.0			
Cost to average AUM	3.3	3.4	3.3	3.6	3.1			
RoA (reported)	1.2	1.1	1.4	1.5	1.5			
RoE (reported)	8.3	8.1	10.6	13.2	13.3			
Asset Qaulity								
Gross NPL	-	-	1.3	1.6	2.2			
Net NPL	-	-	1.1	1.3	1.7			

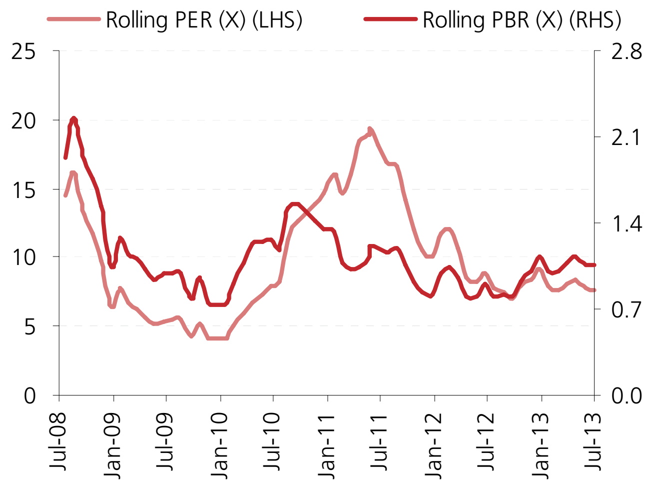
Source: Company, Kotak Institutional Equities

Exhibit 3: Changes in estimates
March fiscal year-ends, 2014-16E (Rs mn)

	New estimates			Old estimates			Change in estimates		
	2014E	2015E	2016E	2014E	2015E	2016E	2014E	2015E	2016E
NIM (%)	5.5	5.6	5.3	5.5	5.5	5.3			
Loan book (Rs bn)	**191**	**233**	**278**	**201**	**245**	**295**	**(5)**	**(5)**	**(6)**
Loan growth (%)	17.2	21.8	19.6	23.6	21.4	20.6			
Net interest income	**9,774**	**11,782**	**13,579**	**10,102**	**12,304**	**14,227**	**(3)**	**(4)**	**(5)**
Other income	-	-	-	-	-	-	-	-	-
Provisions	1,387	1,591	1,651	1,180	1,450	1,615	18	10	2
Operating expenses	5,388	6,508	7,301	5,586	6,748	7,581	(4)	(4)	(4)
Employee expenses	2,311	2,805	3,471	2,311	2,805	3,471	-	-	-
PBT	2,999	3,683	4,628	3,335	4,106	5,032	(10)	(10)	(8)
Tax	900	1,178	1,481	1,067	1,314	1,610	(16)	(10)	(8)
PAT	**2,099**	**2,504**	**3,147**	**2,268**	**2,792**	**3,422**	**(7)**	**(10)**	**(8)**
EPS (Rs)	10	12	16	11	14	17	(8)	(11)	(8)
BVPS (Rs)	82	92	105	83	94	108	(1)	(2)	(3)

Source: Company, Kotak Institutional Equities

Exhibit 4: Magma Finance—one-year forward PER and PBR
July 2008 – July 2013



Source: Company, Bloomberg, , Kotak Institutional Equities

Exhibit 5: Magma Finance—key ratios and growth rates
March fiscal year-ends, 2011-16E (%)

	2011	2012	2013E	2014E	2015E	2016E
Growth in key parameters (%)						
Profit and loss statement - yoy (%)						
Net interest income	20	(17)	96	26	21	15
Provisioning expenses	(13)	(13)	213	44	15	4
Net income (post provisions)	36	(16)	67	24	22	17
Operating expneses	23	(0)	54	16	21	12
Staff expenses	28	11	37	13	21	24
Other operating expenses	30	(12)	80	19	22	3
Depreciation expenses	(15)	6	27	10	10	10
PBT post extraordinaries	65	(43)	105	41	23	26
Tax	53	(57)	160	33	31	26
PAT post pref div and minority interest	70	(43)	101	56	21	27
Balance sheet - yoy (%)						
Loans and advances	38	52	58	14	22	20
Total loans (incl sell down)	17	26	35	17	22	20
Fixed assets	(10)	(4)	6	10	10	10
Other current assets	1	(6)	63	30	30	30
Total assets	28	39	60	16	23	21
Borrowings	26	33	73	18	25	23
Current liabilities	15	45	11	10	10	10
Total liabilities	24	33	65	16	24	22
Share capital	19	46	0	0	0	0
Reserves and surplus	72	87	28	12	13	14
Shareholders funds	69	85	27	11	12	14
Key ratios (%)						
Interest yield	15.5	16.6	17.0	17.2	17.5	17.5
Interest cost	8.5	11.7	11.1	11.0	11.0	11.0
Spreads	7.0	4.9	5.9	6.3	6.5	6.5
NII/ loans under management	5.4	3.7	5.5	5.5	5.6	5.3
Operating costs/ net income (post provisions)	62.5	74.5	68.7	64.2	63.9	61.2
Cash/ total assets + loan sold down	9.2	6.1	6.6	6.2	5.6	5.1
Tax rate	33.0	25.0	33.0	33.0	33.0	33.0
Debt/ equity (X)	7.7	5.6	7.6	8.0	9.0	9.7
Du Pont analysis						
(% of average assets including loans sold down)						
Net interest income	5.4	3.7	5.5	5.5	5.6	5.3
Credit costs	0.4	0.3	0.7	0.8	0.8	0.6
Operating expenses	3.4	2.8	3.3	3.0	3.1	2.9
RoAUM	**1.4**	**0.7**	**1.0**	**1.2**	**1.2**	**1.2**
Average AUM / average equity (X)	14.5	10.7	9.8	10.7	11.8	13.1
RoE (incl pref shares)	**19.9**	**7.7**	**10.1**	**12.7**	**14.0**	**16.1**
ROE (excluding preference shares and minority int	**23.0**	**7.3**	**9.9**	**13.1**	**14.1**	**15.9**

Source: Company, Kotak Institutional Equities estimates

Exhibit 6: Magma Finance—consolidated financial statements
March fiscal year-ends, 2011-16E (Rs mn)

	2011	2012	2013E	2014E	2015E	2016E
Income statement (Rs mn)						
Interest income	6,096	9,514	15,191	20,076	24,032	28,990
Interest costs	(3,523)	(6,254)	(9,262)	(12,655)	(15,430)	(19,229)
Net interest income	**4,790**	**3,953**	**7,753**	**9,774**	**11,782**	**13,579**
Net total income	**5,217**	**4,377**	**7,753**	**9,774**	**11,782**	**13,579**
Provisioning expenses	(356)	(308)	(966)	(1,387)	(1,591)	(1,651)
Net income (post provisions)	**4,861**	**4,069**	**6,787**	**8,386**	**10,191**	**11,929**
Operating expneses	(3,039)	(3,031)	(4,661)	(5,388)	(6,508)	(7,301)
Staff expenses	(1,347)	(1,490)	(2,040)	(2,311)	(2,805)	(3,471)
Other operating expenses	(1,414)	(1,245)	(2,245)	(2,664)	(3,248)	(3,329)
Depreciation expenses	(279)	(296)	(376)	(414)	(455)	(500)
PBT post extraordinaries	**1,822**	**1,038**	**2,126**	**2,999**	**3,683**	**4,628**
Tax	(601)	(259)	(675)	(900)	(1,178)	(1,481)
PAT	**1,221**	**779**	**1,451**	**2,099**	**2,504**	**3,147**
PAT post pref div and minority interest	**1,090**	**618**	**1,240**	**1,929**	**2,334**	**2,962**
No of shares (mn)	130	190	190	190	190	190
EPS (Rs)	**8**	**3**	**7**	**10**	**12**	**16**
DPS (Rs)	**1**	**1**	**1**	**2**	**2**	**2**
BVPS (Rs)	**46**	**58**	**74**	**82**	**92**	**105**
Balance sheet (Rs mn)						
Assets						
Loans and advances	**45,520**	**69,310**	**109,210**	**124,157**	**151,222**	**180,805**
Investments	114	115	2,669	2,869	3,069	3,269
Fixed assets	1,871	1,788	1,902	2,092	2,301	2,532
Current assets	11,409	10,668	17,356	22,563	29,332	38,131
Cash and bank balances	10,075	8,101	12,178	13,484	14,942	16,535
Total assets	**58,914**	**81,881**	**131,137**	**151,681**	**185,924**	**224,737**
Liabilities						
Borrowings	**45,921**	**61,163**	**105,990**	**125,148**	**156,671**	**192,943**
Current liabilities	5,578	8,087	8,949	9,844	10,828	11,911
Preference shares	1,468	1,426	1,971	1,142	970	-
Total liabilities	**52,967**	**70,676**	**116,910**	**136,134**	**168,469**	**204,854**
Share capital	260	380	380	380	380	380
Reserves and surplus	5,686	10,636	13,594	15,167	17,075	19,502
Shareholders funds	**5,946**	**11,016**	**13,974**	**15,547**	**17,455**	**19,882**
Minority interest	**98**	**188**	**255**	**293**	**347**	**416**
Aggregate loan book (incl sell down)						
Loan on books	45,520	69,310	109,210	124,157	151,222	180,805
Loans under management	**95,670**	**120,360**	**163,000**	**191,010**	**232,649**	**278,162**

Source: Company, Kotak Institutional Equities estimates

IDEA (IDEA)

Telecom

BUY

JULY 22, 2013

CHANGE IN RECO.

Coverage view: Neutral

Price (Rs): 151

Target price (Rs): 180

BSE-30: 20,150

Of tailwinds, headwinds, and possibilities; BUY. We believe the tailwinds (market share gain potential, improving sector dynamics) and possibilities (upside inflection extent) overweigh the headwinds (Reliance-Jio entry, data capex spike) for Idea, and upgrade the stock a notch to BUY (from ADD). We also raise our target price to Rs180/share (Rs142 earlier). We continue to rate Idea as our top pick in the sector even as we expect Bharti to benefit from improving sector fundamentals as well.

Company data and valuation summary

IDEA

Stock data			
52-week range (Rs) (high,low)			164-72
Market Cap. (Rs bn)			499.0
Shareholding pattern (%)			
Promoters			25.1
FIIs			45.2
MFs			9.6
Price performance (%)	**1M**	**3M**	**12M**
Absolute	7.6	34.0	84.2
Rel. to BSE-30	0.3	27.4	56.9

Forecasts/Valuations	2013	2014E	2015E
EPS (Rs)	3.1	6.1	9.5
EPS growth (%)	39.8	100.6	55.5
P/E (X)	49.2	24.5	15.8
Sales (Rs bn)	224.6	264.3	305.8
Net profits (Rs bn)	10.1	20.3	31.5
EBITDA (Rs bn)	60.0	77.7	95.0
EV/EBITDA (X)	10.5	7.9	6.1
ROE (%)	7.4	13.3	17.9
Div. Yield (%)	0.2	0.3	0.5

Tailwinds galore – scope for further market share gains, improving sector fundamentals

We expect sustained improvement in the Indian wireless industry's fundamentals as basic scale economics of the business catch up and both the scope and intensity of competitive pressure reduce. We expect quasi consolidation (challengers curbing their footprint) theme to continue, aiding sustained market share gains for the GSM incumbents. We see Idea very well-positioned to benefit from this theme and expect sustained market share gains for the company over the next few years. We also believe that incremental regulatory developments should be in favor of the industry as spectrum pricing and allocation start falling in sync with the economic realities of the business – increasing (even if forced) industry discipline should drive this change.

Possibilities immense – Street (including us) could be underestimating inflection strength

Alignment of interest (profitability improvement) across players in the industry after years of competitive-intensity-led pressure on industry EBITDA bodes well, in our view. More importantly, Street's (including ours) linear ways of thinking and forecasting make underestimation of positive inflection strength a real possibility (similar to the underestimation of negative inflection impact in FY2010 and FY2011). Idea's massive 4QFY13 earnings beat (without any RPM increase) and Vodafone's 1QFY14 4%+ RPM uptick give a glimpse of the possibilities ahead should industry discipline sustain – we expect it to.

Two key headwinds – potential disruption by RIL-Jio and spike in capex led by data

We see two key headwinds/risks – (1) RIL-Jio launch turns out to be more disruptive than the Street is factoring in, at this point; this would of course need RIL-Jio to overcome the current techno-commercial challenges around TD-LTE on 2.3 GHz spectrum band, find a way to be cost-competitive versus scale operators, and be ready for years of cash burn, and (2) negative surprise on the data capex front; data capex is not as easily understood as voice capex given lack of separate disclosures on this front; even as we are positive on strong volume-led growth in data revenues over the coming years, we are not sure if we fully comprehend the associated capex intensity at this point. This is not to say that we are not building in any backhaul capex surge in our model.

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Upgrade to BUY; remains our preferred pick in the Indian telecom space

We upgrade Idea a notch to BUY from ADD earlier, recent solid absolute performance and relative outperformance notwithstanding. We also raise our price target on the stock to Rs180/share (from Rs142 earlier).

Bulk (Rs25/share out of the increase of Rs38/share) of our price target increase comes from us now building in a regulatory impact of Rs55/share versus Rs80/share earlier. Reduction in regulatory drag comes from our increased confidence on the industry remaining disciplined in forthcoming spectrum auctions and driving base 1800 pricing as well as 900 multiplier to more reasonable (reflective of industry economics) levels.

The balance Rs13/share of target price increase derives from (1) moderate increase in estimates, and (2) rollover to Sep-2014-based valuation from Mar 2014 earlier.

Exhibits 1, 2 and 3 below give the key changes to our estimates, operational DCF and target price derivation, respectively.

Exhibit 1: Key changes to Idea earnings model, March fiscal year-ends, 2014-15E

	Revised		Earlier		Change (%)	
	FY2014E	**FY2015E**	**FY2014E**	**FY2015E**	**FY2014E**	**FY2015E**
Consolidated						
Revenues (Rs mn)	264,317	305,808	262,214	302,501	0.8	1.1
EBITDA (Rs mn)	77,714	94,990	75,674	91,856	2.7	3.4
EBIT (Rs mn)	40,280	54,748	37,161	51,510	8.4	6.3
EPS (Rs/share)	6.12	9.51	5.54	8.89	10.4	7.0
EBITDA margin (%)	29.4	31.1	28.9	30.4	54 bps	69 bps
Capex (Rs bn)	39	46	37	38	4.8	20.8
Wireless metrics						
Subs (mn)	131	143	131	143	—	—
Volumes (bn min)	607	679	604	663	0.4	2.4
RPM (paise/min)	0.430	0.446	0.424	0.447	1.4	(0.2)
ARPU (Rs/sub/month)	172	184	174	185	(1.2)	(0.5)

Source: Kotak Institutional Equities estimates

Exhibit 2: Our 12-month forward DCF-based fair value for Idea's core business is Rs234/share

	2012	**2013**	**2014E**	**2015E**	**2016E**	**2017E**	**2018E**	**2019E**	**2020E**	**2021E**
EBITDA	50,923	60,044	77,714	94,990	112,699	129,498	144,250	156,019	168,492	181,660
Tax	(3,947)	(7,991)	(13,494)	(18,341)	(23,272)	(27,908)	(31,891)	(34,927)	(38,240)	(41,819)
Change in working capital	(24,642)	7,897	3,769	5,136	5,362	5,345	4,775	4,243	3,495	3,606
Post-tax operating cash flow	**22,334**	**59,950**	**67,990**	**81,785**	**94,790**	**106,935**	**117,133**	**125,334**	**133,747**	**143,447**
Capex	(42,020)	(49,131)	(39,104)	(45,514)	(46,233)	(47,160)	(46,127)	(45,417)	(45,282)	(45,135)
Free cash flow	**(19,686)**	**10,819**	**28,885**	**36,272**	**48,557**	**59,775**	**71,007**	**79,917**	**88,464**	**98,312**
						WACC and terminal growth assumptions				
PV of cash flows	336,055					**Terminal growth - g (%)**				**4.0**
PV of terminal value	559,136					**WACC (%)**				**12.5**
EV	895,191									
Net debt	120,923									
Equity value (Rs mn)	**774,268**									
Equity value (US$ mn)	**16,651**									
Shares outstanding (mn)	3,314									
Equity value (Rs/Idea share)	**234**									
Exit FCF multiple (X)	12.2									
Exit EBITDA multiple (X)	**6.6**									
Key assumptions (%)										
Revenue growth	26.0	14.9	17.7	15.7	13.5	10.6	8.5	6.5	6.3	6.1
EBITDA growth	34.3	17.9	29.4	22.2	18.6	14.9	11.4	8.2	8.0	7.8
EBITDA margin	**26.1**	**26.7**	**29.4**	**31.1**	**32.5**	**33.7**	**34.6**	**35.1**	**35.7**	**36.3**
Capex/sales	21.5	21.9	14.8	14.9	13.3	12.3	11.1	10.2	9.6	9.0
Effective tax rate	31.5	35.9	33.5	33.5	33.5	33.5	33.5	33.5	33.5	33.5

Source: Company, Kotak Institutional Equities estimates

Exhibit 3: Target price derivation for Idea

Operational DCF (Rs/share)	234
Gross spectrum liability NPV (Rs/share)	(79)
One-time excess	(6)
Spectrum renewal	(56)
Spectrum refarming	(16)
% of regulatory impact taken	70
Spectrum related liability	(55)
Target price (Rs/share)	**179**

Source: Kotak Institutional Equities estimates

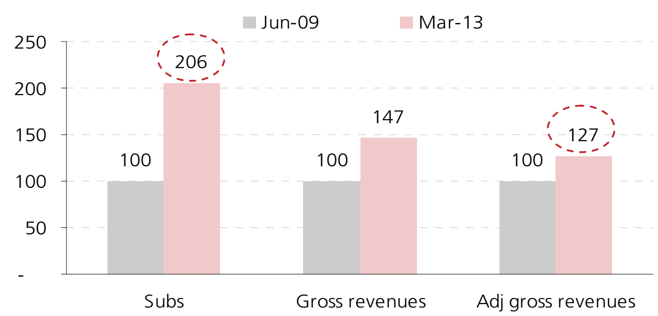
Tailwind # 1 – improving sector dynamics

Unsustainable disconnect between weak P&Ls and bloated debt-heavy balance sheets has forced the challengers in the industry to start seeking price-improvement and cost-reduction (through footprint rationalization) led P&L improvement. Both of these (challengers seeking pricing improvement and rationalizing their footprint) play to the advantage of the incumbents who gain on both the volume as well as pricing side of the revenue equation. In essence, there is (forced or otherwise) alignment of interest in the industry to expand overall profit pool of the industry – a reversal from the past 4+ years when market-share and 3G/BWA spectrum dogfights led to a shrinkage in the industry profit pool.

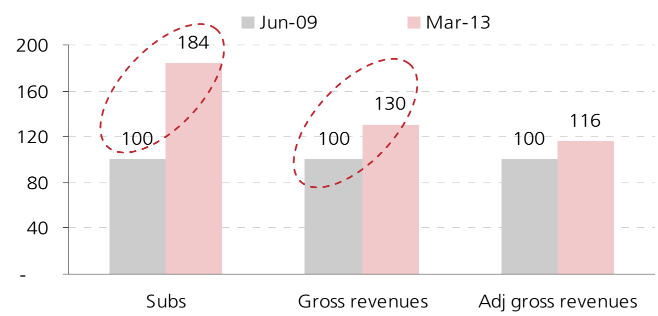
Exhibit 4 depicts the industry scenario over the past five years using Bharti as an example – robust subscriber and volume growth failed to translate into EBITDA/PAT growth as competitive dynamics took a toll on pricing as well as costs. Exhibit 5 depicts the recent phase of quasi consolidation in the industry while Exhibit 6 depicts the financial challenge facing the challengers.

Exhibit 4: Strong subscriber growth has not translated into revenue growth for the industry

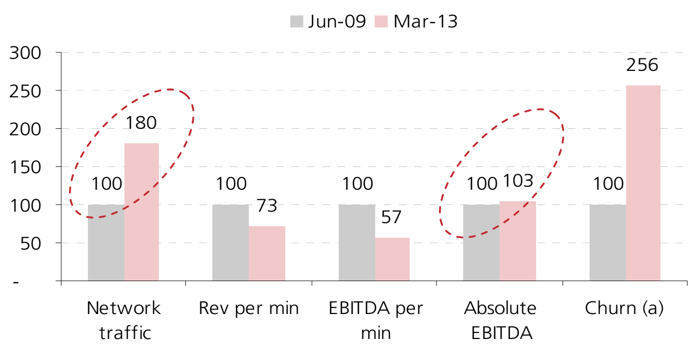
Industry - subs growth versus revenue growth



Bharti - subs growth versus revenue growth



Bharti - quarterly EBITDA levels still the same as nearly four years back



Note: (a) June 2009 churn (%, montly) compared to the peak hit in June 2012

Source: TRAI, Company, Kotak Institutional Equities

Exhibit 5: Challengers have started rationalizing their networks

	# of circles		
Player/network	**Mar-08**	**Mar-11**	**Mar-13**
Bharti - GSM	22	22	22
Vodafone - GSM	15	22	22
Idea - GSM	13	22	22
RCOM - GSM	8	22	22
RCOM - CDMA	22	22	22
TTSL - GSM	—	21	21
TTSL - CDMA	19	**22**	**19**
Aircel - GSM	9	**22**	**17**
BSNL/MTNL - GSM	22	22	22
Telenor - GSM	—	**13**	**6**
Loop - GSM	1	**8**	**1**
MTS - CDMA	1	**18**	**9**
S Tel	—	**5**	**—**
Etisalat	—	**15**	**—**
Videocon	—	**16**	**6**
Total	**132**	**272**	**211**

Source: TRAI

Exhibit 6: Challengers under severe balance sheet stress

Player	Net debt (Rs bn)	EBITDA (Rs bn)	Net debt/ EBITDA (X)
Bharti	638	249	2.6
Vodafone	335	90	3.7
Idea	129	60	2.1
RCOM	388	50	7.8
TTSL	280	2	140.0
BSNL	35	11	3.2
Uninor	—	(15)	(-) ve EBITDA
MTS	46	(13)	(-) ve EBITDA
MTNL	115	(1)	(-) ve EBITDA
Aircel	250	(12)	(-) ve EBITDA
Loop	—	2	NM
HFCL	—	(1)	(-) ve EBITDA
Total	**2,216**	**421**	

Source: Companies, Kotak Institutional Equities estimates

As an aside, we must mention here that it would take a lot of RPM improvement for the industry to reach a stage where even 5/6 players have a viable business model. This may not happen, in our view, and hence we expect more quasi-consolidation in the industry – this would happen in the form of each of the challengers (barring BSNL/MTNL) reducing their footprint (and focus) to fewer circles – circles where they have a real shot at being among the top 4 or 5 players. Exhibit 7 gives the breakeven RPM levels along various cuts for the industry – note that RPM needs to be above 50 paise/min if the 5^{th} largest player in the industry (with a 10% market share) has to achieve FCF breakeven. Industry RPM today is around the 41-42 paise/min mark, leaving ample headroom for expansion, should the industry discipline sustain – we think it would.

A good example of industry discipline can be seen in the recent announcements of 'free incoming roaming' plans across operators. Challengers followed the incumbents on pricing of these plans and we note that none of them has attempted to undercut the incumbents to gain some 'quality' market share; heavy-roaming customers typically tend to be higher-quality ones, as well. See Exhibit 8 for 'free incoming roaming' plans announced by various operators.

Exhibit 7: Challengers barely break even at EBITDA level at current RPM levels

EBITDA break-even RPM		**ROCE break-even RPM**		**8% ROCE RPM**	
Top-3	0.310	Top-3	0.342	**Top-3**	**0.437**
Top-5	0.408	Top-5	0.503	Top-5	0.639
Top-6	0.415	Top-6	0.525	Top-6	0.680
All	0.524	All	0.772	All	0.996
Cash break-even RPM		**6% ROCE RPM**		**12% ROCE RPM**	
Top-3	0.393	Top-3	0.413	**Top-3**	**0.485**
Top-5	0.515	Top-5	0.605	Top-5	0.707
Top-6	0.533	Top-6	0.642	Top-6	0.758
All	0.672	All	0.940	All	1.108

Source: Kotak Institutional Equities estimates

Exhibit 8: Recently launched 'free' roaming plans across operators

Operator	MRP	Local Calls (Home & Roam)	STD Calls (Home & Roam)	Incoming Calls (while in Roaming)	SMS (Home & Roam)	Validity	Remarks
Tata Docomo	Rs. 152	78p/min	90p/min	75p/min	Local:Re1, STD:Rs.1.5	60 days	
Tata Docomo	**Rs. 252**	**78p/min**	**90p/min**	**Free**	**Local:Re1, STD:Rs.1.5**	**60 days**	
Uninor	Rs. 61	1.6p/sec	2.2p/sec	1.25p/sec	Local:Re1, STD:Rs.1.5	180 days	
Uninor	**Rs. 1,199**	**Re.1/min**	**Rs.1.5/min**	**Free**	**Local:Re1, STD:Rs.1.5**	**180 days**	
Loop	Rs. 47	Re.1/min	Rs.1.5/min	75p/min		180 days	
Loop	Rs.64 + Rs.2/day after 30 days	60p/min	80p/min	Free		180 days	
Reliance Com	Rs. 5	1.5p/sec	1.5p/sec	Free		1 day	
Reliance Com	**Rs. 77**	**1.5p/sec**	**1.5p/sec**	**Free**		**28 days**	
Reliance Com	Rs. 194	1.5p/sec	1.5p/sec	Free		180 days	
BSNL	Rs. 5	1.5p/sec	1.5p/sec	Free		1 day	
BSNL	**Rs. 69**	**1.5p/sec**	**1.5p/sec**	**Free**		**30 days**	
BSNL	Rs. 199	Local & STD (Home) : 1.2p/sec to BSNL N/W, 1.5p/sec to others	Local & STD (Roaming) : Re.1/min, Rs.1.5/min	Free in BSNL N/W (75p/min in MTNL Mumbai & Delhi N/W)		180 days	
MTNL	Rs. 9	3p/2sec	3p/2sec	Free	Local:Re1, STD:Rs.1.5	2 days	
MTNL	**Rs. 75**	**3p/2sec**	**3p/2sec**	**Free**	**Local:Re1, STD:Rs.1.5**	**30 days**	
MTNL	Rs. 89	90p/min	Rs.1.40/min	75p/min	Local:Re1, STD:Rs.1.5	180 days	
MTNL	Rs. 310	90p/min	Rs.1.40/min	Free	Local:Re1, STD:Rs.1.5	180 days	Post paid plans also available
Vodafone	Rs. 5	1.5p/sec	1.5p/sec	Free		1 day	
Vodafone	**Rs. 71**	**1.5p/sec**	**1.5p/sec**	**Free**		**30 days**	
Vodafone	Rs. 149	Re.1/min	Rs.1.5/min	Free		30 days	Free 100 minutes voice (Local+STD+Roam), Free 100 SMS (Local, STD, Roam)
Vodafone	Rs. 149	1.2p/sec	1.2p/sec	Free		30 days	Free 100 minutes voice (Local+STD+Roam), Free 100 SMS (Local, STD, Roam)
Airtel	Rs. 5	1.5p/sec	1.5p/sec	Free		1 day	
Airtel	**Rs. 79**	**1.5p/sec**	**1.5p/sec**	**Free**		**30 days**	
Airtel	Rs.75 (postpaid Add-on)	As per selected postpaid plan	As per selected postpaid plan	Free		Postpaid	Add-on pack with auto renewal
Airtel	Rs.99 (Postpaid)	75p/min	75p/min	75p/min	Local:Re1, STD:Rs.1.5	Postpaid	
Airtel	Rs.99 (Postpaid)	1.5p/sec	1.5p/sec	Free	Local:Re1, STD:Rs.1.5	Postpaid	
Airtel	Rs.499 (Postpaid)	1.2p/sec	1.2p/sec	Free	Local:Re1, STD:Rs.1.5	Postpaid	

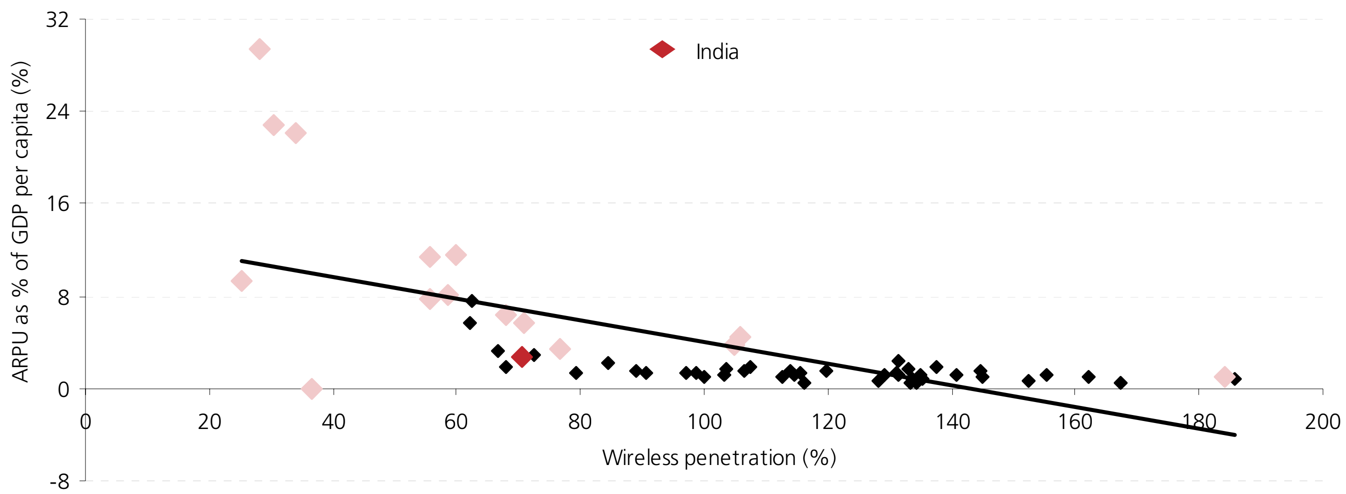
Source: Companies, media reports

Risks to tailwind # 1 (devil's advocate view) – negative elasticity and/or regulatory curbs on price hikes

Logical skepticism on both counts; however, we see the former (negative elasticity) as a low-probability/low-impact and the latter as a low-probability event. On the former, our comfort derives from –

- Low wallet share of telecom spending in India as compared to most global markets (see Exhibit 9) – this has been a direct result of hyper-competition-led sustained high price deflation in the Indian market.

Exhibit 9: India's per capita spend on telecom low relative to other markets



Source: Telegeography, Kotak Institutional Equities

- The way we have seen the Indian consumer absorb inflation in several other consumption categories, especially staples – telecom is largely a staple, non-discretionary consumption item, in our view, and
- Still-untapped voice volume potential – against a headline SIM penetration of 71%, active SIM penetration in India is 57% and unique user penetration just ~50%. Rural wireless tele-density at 39% still offers a good few years of penetration-led voice volume growth. In addition, vintage effect (usage for a new sub increasing for the first few years before plateauing) for new subs added in the past three years should aid volume growth too. From the perspective of incumbents, some market share gains on voice volumes should aid, as well.

The latter (the risk of Government intervention in pricing) is a trickier one. However, we believe the interest of the Government should be aligned with the industry on this aspect, given – (1) the huge potential off balance sheet liabilities that BSNL and MTNL are at risk of becoming, (2) the industry fundamentals need to improve for the Government to be able to sell spectrum, especially 700 MHz, and (3) being pro-consumer is not just about driving price deflation – it is about ensuring sufficient investments in network quality while curbing monopolistic/oligopolistic behavior on pricing. As discussed earlier, telecom spend wallet share in India is at reasonably depressed levels and the consumer can absorb some inflation, as long as it is a calibrated increase and not a sharp spike.

Tailwind # 2 – further market share gain potential for Idea

We had addressed part of this aspect (why we believe Idea and Vodafone should continue to gain relative market share over Bharti) in a couple of notes we published in March 2012. We continue to believe the same. In addition, footprint rationalization by challengers opens up fresh market share gain opportunities for the GSM incumbents (Bharti, Vodafone, and Idea) – Idea should be able to garner its fair share of this incremental opportunity, in our view.

Despite material market share gains and ground covered versus Bharti over the past 3-4 years (see Exhibit 10 for circle-wise market share movement for Bharti, Vodafone and Idea since June 2009), Idea's asset leverage (we define the same as revenue market share divided by network market share) as well as asset base remains substantially below Bharti. The company, in essence, has both the market share gain legs available to it – close in further on network market share versus Bharti (Idea has 90,000 2G cell sites versus nearly 134,000 for Bharti) and improve on asset leverage as well. Exhibit 11 substantiates our argument.

Exhibit 10: Circle-wise change in revenue market share of incumbents from Jun-09 to Mar-13

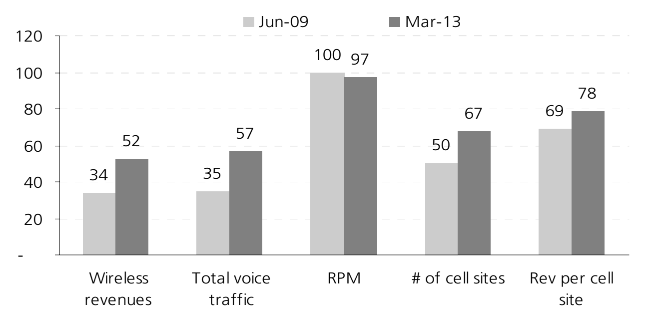
Circle	Bharti				Vodafone				Idea			
	% of Rev	Market share (%)		Change	% of Rev	Market share (%)		Change	% of Rev	Market share (%)		Change
	Mar 13	Jun-09	Mar-13	(bps)	Mar 13	Jun-09	Mar-13	(bps)	Mar 13	Jun-09	Mar-13	(bps)
Metro + Circle A	**54.0**	**33.6**	**29.6**	**(402)**	**59.2**	**23.2**	**24.9**	**171**	**48.4**	**11.0**	**13.9**	**288**
Andhra Pradesh	9.6	40.1	37.5	(266)	3.6	13.7	10.8	(287)	9.7	17.7	19.8	209
Delhi	9.4	38.6	34.4	(418)	10.4	22.9	29.3	636	6.1	9.7	11.6	189
Gujarat	3.4	21.1	18.0	(311)	9.7	40.7	39.1	(157)	7.0	17.6	19.4	178
Karnataka	10.7	54.0	45.3	(872)	4.8	16.0	15.6	(41)	4.6	6.2	10.2	406
Kolkata	2.2	32.2	26.6	(562)	3.4	32.1	31.3	(75)	0.9	—	5.6	555
Maharashtra	5.5	23.4	19.7	(365)	9.2	18.8	25.4	661	14.8	28.7	27.8	(89)
Mumbai	4.4	20.7	20.2	(48)	9.4	31.5	33.4	182	3.7	3.9	9.0	511
TN (incl Chennai)	8.7	34.3	30.4	(397)	8.5	21.3	22.7	146	1.6	0.0	3.0	295
Circle B	**30.1**	**30.0**	**26.8**	**(317)**	**34.2**	**22.1**	**23.3**	**128**	**46.4**	**17.1**	**21.6**	**450**
Haryana	1.2	19.9	17.7	(225)	2.7	25.4	30.0	468	3.3	20.1	24.6	449
Kerala	2.4	21.2	16.8	(442)	4.5	19.6	24.1	449	9.6	28.0	34.9	691
Madhya Pradesh	3.8	32.1	23.9	(818)	1.8	2.6	9.0	639	10.5	28.6	34.8	625
Punjab	4.4	38.8	34.2	(456)	3.1	16.1	18.5	241	5.2	18.0	21.3	333
Rajasthan	6.5	45.7	39.5	(613)	5.0	23.1	23.6	52	3.7	5.7	11.8	617
U.P. (E)	6.0	29.1	28.5	(63)	7.7	32.1	28.4	(375)	5.1	8.5	12.8	430
U.P. (W)	2.8	17.8	19.7	190	4.5	25.0	23.8	(120)	7.8	27.1	28.3	125
West Bengal	3.1	29.0	28.4	(56)	4.8	36.3	33.9	(231)	1.3	—	6.1	614
Circle C	**15.9**	**47.5**	**40.4**	**(715)**	**6.6**	**3.5**	**12.9**	**943**	**5.1**	**2.5**	**6.8**	**432**
Assam	1.9	35.7	32.1	(357)	1.3	2.7	16.8	1,412	0.3	—	2.5	247
Bihar	7.4	49.8	44.3	(551)	2.7	4.0	12.6	859	3.4	4.7	10.6	591
Himachal Pradesh	0.9	46.9	39.3	(764)	0.3	2.6	9.0	640	0.4	6.1	9.8	364
J&K	1.4	68.2	37.0	(3,117)	0.4	1.5	8.8	722	0.2	—	3.3	333
North East	1.6	39.0	42.0	300	0.6	4.1	12.3	823	0.2	—	3.4	337
Orissa	2.7	45.6	39.5	(609)	1.3	4.1	14.2	1,012	0.6	0.8	4.3	349
Pan India	**100.0**	**33.9**	**29.9**	**(392)**	**100.0**	**20.8**	**23.0**	**217**	**100.0**	**12.2**	**15.7**	**351**

Note:
(a) Circles shaded in pink represent the top-5 circles for each operator.

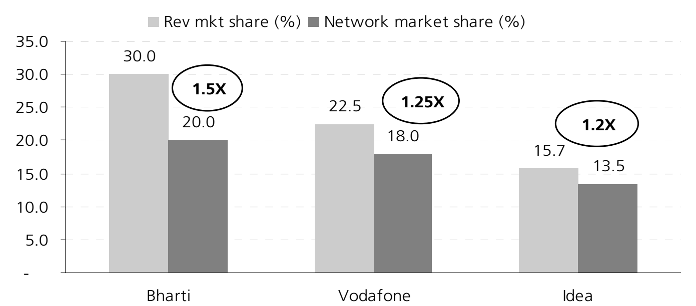
Source: TRAI, Kotak Institutional Equities

Exhibit 11: Idea still has potential to catch up with Bharti

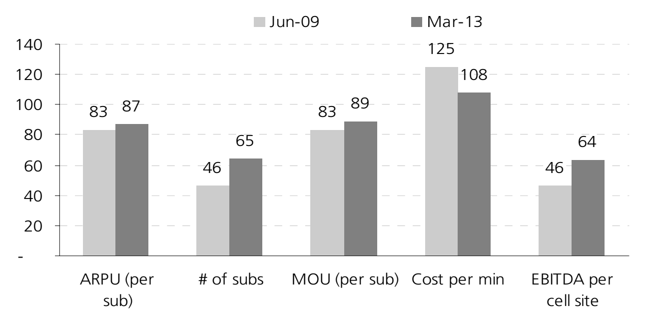
Revenue drivers - Idea as % of Bharti



Idea still has potential to leverage its assets better



Other drivers - Idea as % of Bharti



Source: Companies

We also note that Idea's current low market share in several circles presents good market share gain potential should the company keep executing well. Vodafone's performance in its seven new circles (Madhya Pradesh and the six C category circles) shows that execution, investments and brand strength can drive profitable market share gains even at this stage of market evolution (see Exhibit 12 for Vodafone's performance in its new circles).

Exhibit 12: Vodafone has built meaningful market share in its seven new circles without price disruption

Circle	Commercial launch	Mar-2013 quarter GR RMS (%)	RMS rank (#)
M.P.	Dec-08	9.0	4
Bihar	Dec-08	12.6	2
Orissa	Sep-08	14.2	2
North East	Sep-08	12.3	3
Assam	Sep-08	16.8	3
Himachal Pradesh	Mar-09	9.0	5
J&K	Jun-09	8.8	4
Total - seven new circles		**11.8**	
Mar 2013 quarter RPM analysis versus Bharti			
Bharti blended RPM (paise/min)	42.4		
Vodafone blended RPM (paise/min)	43.1		
Bharti total traffic (mn min)	253,144		
Vodafone total traffic (mn min)	201,170		
Assuming Vodafone's RPM in seven new circles is 10% lower than Bharti			
Vodafone revenues - 7 new circles (Rs mn)	7,546		
Vodafone revenues - 15 legacy circles (Rs mn)	81,411		
Vodafone RPM (paise/min) - 7 new circles	38.2		
Vodafone minutes in 7 new circles (mn)	19,776		
Vodafone minutes in 15 legacy circles (mn)	181,394		
Vodafone implied RPM - 15 legacy circles	44.9		
Implied RPM premium to Bharti in legacy circles (%)	**5.9**		
Assuming Vodafone's RPM in seven new circles is 20% lower than Bharti			
Vodafone revenues - 7 new circles (Rs mn)	7,546		
Vodafone revenues - 15 legacy circles (Rs mn)	81,411		
Vodafone RPM (paise/min) - 7 new circles	33.9	Too high a premium to be true	
Vodafone minutes in 7 new circles (mn)	22,248		
Vodafone minutes in 15 legacy circles (mn)	178,922		
Vodafone implied RPM - 15 legacy circles	45.5		
Implied RPM premium to Bharti in legacy circles (%)	**7.3**		

Source: TRAI, Kotak Institutional Equities estimates

Risks to tailwind # 2 (devil's advocate view) – (a) Bharti hits back hard, (b) Idea slips on execution, and (c) one of the challengers becomes competitive

Valid points, all, again. Bharti indeed lost substantial market share from Jun 2009 through Jun 2012 and has had to make meaningful margin sacrifice to stem the fall since. We do have a lot of respect for Bharti's execution engine; however, (1) given the industry tailwinds, Bharti does not need to hit back at Idea (or Vodafone); in fact, getting into a fierce market share battle with the other two incumbents would be a counter-productive move by Bharti, in our view, and (2) Bharti can do little about the natural network coverage upside that Idea and Vodafone enjoy over itself.

As far as Idea slipping on execution is concerned, it is indeed a risk; in fact, execution slippage is a risk with any company one invests in and one builds the same into the WACC applied while valuing the company. We do not see a reason to start building in any higher or lower risk on this front for Idea than we historically have.

The last one, i.e. one of the challengers becoming more competitive, would need massive equity infusion into one of them. We see the same as a low-probability event and hence would not be unduly worried. We also do not see a merger-led creation of a more competitive challenger.

‘All goes well’ scenario analysis – 20% market share for Idea in FY2018E can mean the stock goes up 2X from current levels

Even as we believe Idea can achieve 20% market share of the Indian wireless market in the next few years, we do not build the same into our model, to be on the conservative side and build some margin of safety. Nonetheless, in a hypothetical ‘all goes well’ scenario, where Idea does reach 20% market share in FY2018E and industry remains rational, we believe Idea stock can double in the next four years. See Exhibit 13 below: we also note that this is not a ‘blue sky’ scenario, by any means – most assumptions on industry revenue growth only assume sustained rationality; our voice RPM and regulatory impact assumptions can be termed conservative, in fact.

Exhibit 13: Idea ‘blue sky’ scenario

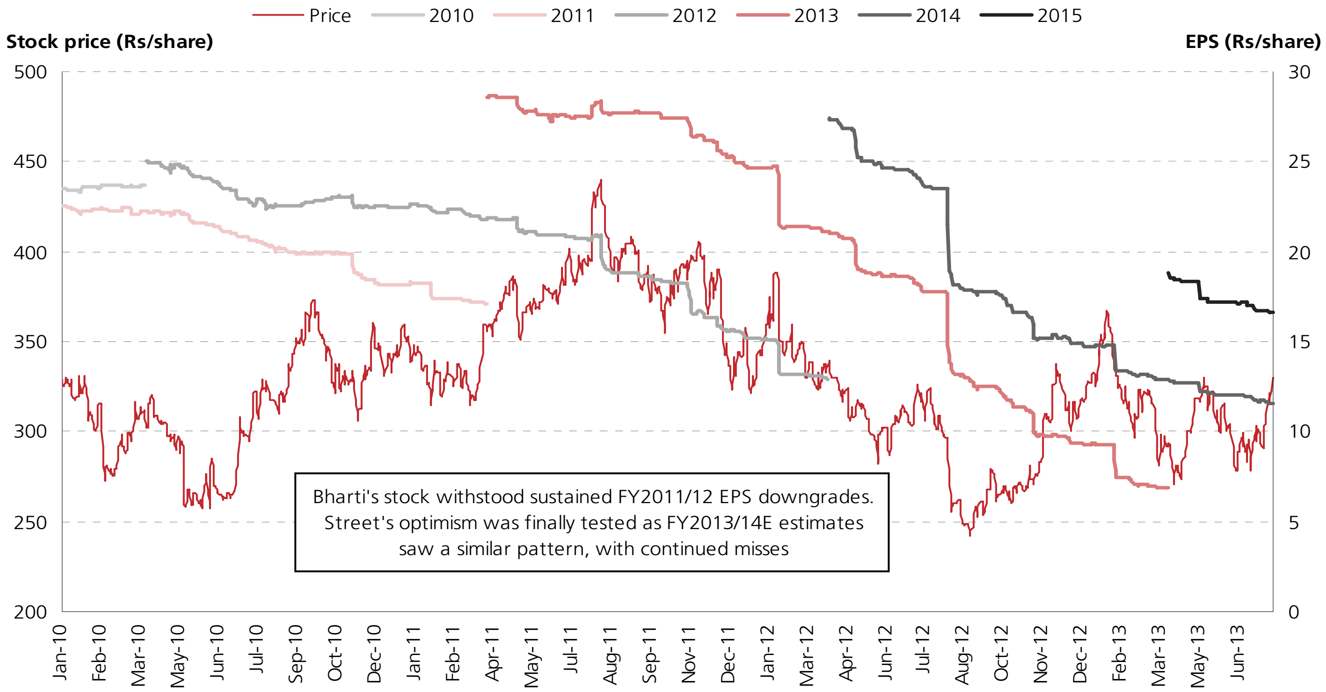
	FY2013	FY2018E	CAGR (%)
Industry size - India wireless			
Voice volumes (bn min)	3,709	4,734	5.0
Voice RPM (Rs/min)	0.319	0.370	3.0
Voice revenues (Rs bn)	1,184	1,752	
SMS revenues (Rs bn)	103	94	(2.0)
VAS revenues (Rs bn)	43	50	3.0
Data revenues (Rs bn)	115	740	45.0
Total industry revenues (Rs bn)	**1,446**	**2,636**	**12.8**
Idea 'all goes well' financials			
Wireless business			
Revenues (Rs bn)	219	527	19.2
Revenue market share (%)	15.2	20.0	
EBITDA (Rs bn)	51.8	184.5	28.9
EBITDA margins (%)	23.6	35.0	
EV/EBITDA (X) - on wireless		5.5	
EV (Rs bn) - wireless only		1,015	
Tower business EV computation			
Owned towers (#)		10,000	
Proportionate share of Indus towers (#)		16,000	
Total towers (#)		26,000	
EV/tower (Rs mn)		4.0	
Tower EV (Rs bn)		104	
Total EV (Rs bn)		**1,119**	
Net debt/ (cash) without regulatory payments (Rs bn)		(157)	
Regulatory payments FY2014-18E (Rs bn)		177	
PV of regulatory payments beyond FY2018E (Rs bn)		100	
Equity value (Rs bn)		999	
Per share (Rs)		**303**	
Upside (%)		**100**	

Source: FactSet

Risk of underestimating the strength of positive inflection – on voice pricing, data volumes, and resultant absolute EBITDA and EBITDA growth

We present a single chart to drive home the point here – Exhibit 14 shows the consistent downgrades in Street’s EPS estimates for Bharti over the past four years. Even as a part of the downgrade cycle for Bharti was driven by weaker-than-expected performance in Africa and market share losses in India, underestimation of competition’s impact on RPM and cost structure in the India wireless business had a role to play as well. Similar underestimation, this time on the positive side, is very much a possibility. Idea’s 4QFY13 earnings surprise and Vodafone’s 1QFY14 RPM beat are two very relevant pointers as well. We also reproduce a quote Idea’s CEO made in the 4QFY13 earnings call – *“…the future can no longer be extrapolated from the past. Change is a discontinuous function rather than a linear projection, to the discomfort of many analyst colleagues.”*

Exhibit 14: Consensus EPS estimates for Bharti have seen consistent downgrades



Source: FactSet

Valuation – are we stretching it a bit?

At current market price, Idea is trading at 6X FY2015E EV/EBITDA and 2.6X P/B (for an expected FY2015E ROE of 17.9%) and our target price implies 7X FY2015E EV/EBITDA and 3.1X P/B. Even as the same may appear high in light of the multiples in recent past and in general versus the trading multiples of global comps, we note that (1) we base our fair value target on DCF, and (2) the same bakes in several years of strong EBITDA and FCF growth; strong FCF generation should drive some EV to equity shift as well over the coming years, regulatory payouts notwithstanding.

Part of our aggressive stance on valuations also stems from (1) potential upside versus our already high estimates versus the Street, and (2) our view that solid 'defensives with earnings visibility/comfort' should continue to command a premium relative to the market; Indian telcos with reasonable leverage, especially Idea, fit the bill.

Exhibits 15 and 16 give various valuation parameters for Idea at the CMP and our target price, respectively.

Exhibit 15: Idea - valuation summary at current market price, March fiscal year-ends, 2011-17E

Rs bn	2011	2012	2013	2014E	2015E	2016E	2017E
@ Rs150							
Market cap	497	497	497	497	497	497	497
Net debt	106	131	121	100	72	30	(25)
Enterprise value	603	628	618	598	569	527	472
P/E (X)	55.3	68.8	49.2	24.5	15.8	11.6	9.2
EV/EBITDA (X)	15.9	12.3	10.3	7.7	6.0	4.7	3.6
EV/FCF (X)	NM	NM	57.1	20.7	15.7	10.9	7.9
FCF yield (%)	NM	NM	1.8	**4.8**	**6.4**	**9.2**	**12.7**
P/B (X)	**4.0**	**3.8**	**3.5**	**3.1**	**2.6**	**2.2**	**1.8**
ROE (%)	**7.4**	**5.7**	**7.4**	**13.3**	**17.9**	**20.4**	**21.3**
EV/GCI (X)	**2.1**	**1.9**	**1.8**	**1.7**	**1.5**	**1.3**	**1.2**
ROCE (%)	**4.9**	**4.7**	**4.8**	**7.5**	**9.9**	**12.0**	**13.9**
EPS (Rs/share)	**2.7**	**2.2**	**3.0**	**6.1**	**9.5**	**12.9**	**16.3**
EBITDA (Rs bn)	**37.9**	**50.9**	**60.0**	**77.7**	**95.0**	**112.7**	**129.5**

Source: Kotak Institutional Equities estimates

Exhibit 16: Idea - valuation summary at target price, March fiscal year-ends, 2011-17E

Rs bn	2011	2012	2013	2014E	2015E	2016E	2017E
@ Rs180							
Market cap	597	597	597	597	597	597	597
Net debt	106	131	121	100	72	30	(25)
Enterprise value	703	728	718	697	669	627	572
P/E (X)	66.4	82.6	59.0	29.4	18.9	13.9	11.0
EV/EBITDA (X)	18.5	14.3	12.0	9.0	7.0	5.6	4.4
EV/FCF (X)	NM	NM	66.3	24.1	18.4	12.9	9.6
FCF yield (%)	NM	NM	1.5	**4.1**	**5.4**	**7.8**	**10.5**
P/B (X)	**4.9**	**4.6**	**4.2**	**3.7**	**3.1**	**2.6**	**2.1**
ROE (%)	**7.4**	**5.7**	**7.4**	**13.3**	**17.9**	**20.4**	**21.3**
EV/GCI (X)	**2.4**	**2.2**	**2.0**	**1.9**	**1.8**	**1.6**	**1.4**
ROCE (%)	**4.9**	**4.7**	**4.8**	**7.5**	**9.9**	**12.0**	**13.9**
EPS (Rs/share)	**2.7**	**2.2**	**3.0**	**6.1**	**9.5**	**12.9**	**16.3**
EBITDA (Rs bn)	**37.9**	**50.9**	**60.0**	**77.7**	**95.0**	**112.7**	**129.5**

Source: Kotak Institutional Equities estimates

Quick thoughts on the oft-discussed 'Idea versus Bharti' question

As noted earlier, we continue to prefer Idea over Bharti. Even as we believe Bharti's India business should benefit as well from the improving sector fundamentals, our relative preference for Idea is driven by (1) Idea's higher leverage to India wireless fundamentals, given pure-India-wireless-play nature, and (2) our discomfort with Bharti Africa – we believe there could be more negative surprises on the EBITDA/capex (simple FCF, in essence) equation for Bharti Africa in the coming years. Bharti faces license/spectrum renewals in several of its African operations starting FY2016 – the Street (including us) is not in a position to appreciate the potential payouts in the absence of any guidance from Bharti.

As far as relative valuations are concerned, we prefer to look at like-on-line India wireless versus India wireless valuation comparison instead of headline comparison. We present the same in Exhibit 17 below; on a like-on-like comparison, Idea is in fact trading at a 3% discount to Bharti on an FY2015E EV/EBITDA basis – cheap, in light of relative growth differential. Exhibit 18 gives the same comparison on our target prices – Rs350/share for Bharti and Rs180/share for Idea – our price targets value Idea's India wireless business at about 10% premium to Bharti, fair in our view.

Exhibit 17: Idea versus Bharti - what is the Indian wireless business being valued at?

Bharti (proportionate consolidation of Africa)		Idea	
@ Rs330		@ Rs150	
Market cap (Rs bn)	1,320	Market cap (Rs bn)	497
Net debt - FY15E (Rs bn)	489	Net debt - FY15E (Rs bn)	77
Consol EV (Rs bn)	**1,809**	**Consol EV (Rs bn)**	**575**
Consol EBITDA (Rs bn)	**313**	**Consol EBITDA (Rs bn)**	**95.0**
Consol EV/EBITDA (X)	**5.8**	**Consol EV/EBITDA (X)**	**6.0**
Less		**Less**	
Africa EV (Rs bn)	**320**	**Tower EV - Indus (Rs bn)**	**54**
Africa EBITDA (Rs bn) - proportionate	64	**# of towers (13.4%)**	**14,950**
EV/EBITDA (X)	**5.0**	**EV/tower (Rs mn)**	**3.6**
Tower EV	**235**	**Tower EV - non-Indus (Rs bn)**	**34**
# of towers (proportionate, minority-adjusted)	**65,156**	**# of towers**	**10,000**
EV/tower (Rs mn)	**3.6**	**EV/tower (Rs mn)**	**3.4**
DTH EV	**66.0**		
FY2014E Sales (Rs bn)	**22.0**		
EV/sales (X)	**3.0**		
India non-wireless, non-DTH EV (Rs bn)	**64**		
EBITDA (Rs bn)	**13**		
EV/EBITDA (X)	**5.0**		
Residual EV - India wireless (Rs bn)	**1,124**	**Residual EV - India wireless (Rs bn)**	**487**
India wireless EBITDA (Rs bn)	**188**	**India wireless EBITDA (Rs bn) (a)**	**84.0**
India wireless EV/EBITDA (X)	**6.0**	**India wireless EV/EBITDA (X)**	**5.8**

Idea premium/ (discount)	**(2.9)**

Note:
(a) Adjusted for EBITDA from owned towers, which we have valued separately.

Source: Kotak Institutional Equities estimates

Exhibit 18: Idea versus Bharti - residual India wireless valuations at our target prices

Bharti (proportionate consolidation of Africa)		Idea	
@ Rs350		@ Rs180	
Market cap (Rs bn)	1,400	Market cap (Rs bn)	597
Net debt - FY15E (Rs bn)	489	Net debt - FY15E (Rs bn)	77
Consol EV (Rs bn)	**1,889**	**Consol EV (Rs bn)**	**674**
Consol EBITDA (Rs bn)	**313**	**Consol EBITDA (Rs bn)**	**95.0**
Consol EV/EBITDA (X)	**6.0**	**Consol EV/EBITDA (X)**	**7.1**
Less		**Less**	
Africa EV (Rs bn)	**320**	**Tower EV - Indus (Rs bn)**	**54**
Africa EBITDA (Rs bn) - proportionate	64	**# of towers (13.4%)**	**14,950**
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# of towers (proportionate, minority-adjusted)	**65,156**	**# of towers**	**10,000**
EV/tower (Rs mn)	**3.6**	**EV/tower (Rs mn)**	**3.4**
DTH EV	**66.0**		
FY2014E Sales (Rs bn)	**22.0**		
EV/sales (X)	**3.0**		
India non-wireless, non-DTH EV (Rs bn)	**64**		
EBITDA (Rs bn)	**13**		
EV/EBITDA (X)	**5.0**		
Residual EV - India wireless (Rs bn)	**1,204**	**Residual EV - India wireless (Rs bn)**	**586**
India wireless EBITDA (Rs bn)	**188**	**India wireless EBITDA (Rs bn) (a)**	**84.0**
India wireless EV/EBITDA (X)	**6.4**	**India wireless EV/EBITDA (X)**	**7.0**

Idea premium/ (discount)	**9.2**

Note:
(a) Adjusted for EBITDA from owned towers, which we have valued separately.

Source: Kotak Institutional Equities estimates

Exhibit 19: Key assumptions driving Idea model, March fiscal year-ends, 2012-17E

	2012	2013	2014E	2015E	2016E	2017E
Subscriber base ('000s)	**112,723**	**121,607**	**131,286**	**143,267**	**151,250**	**159,229**
Net adds per month ('000s)	1,935	740	807	998	665	665
Voice traffic (bn mins)	**453**	**532**	**607**	**679**	**747**	**800**
Change(%)	25.0	17.4	14.0	12.0	10.0	7.0
Voice RPM (Rs/min)	**0.366**	**0.350**	**0.361**	**0.370**	**0.375**	**0.379**
Change(%)	(0.5)	(4.2)	3.0	2.5	1.5	1.0
Overall RPM (Rs/min)	**0.422**	**0.412**	**0.430**	**0.446**	**0.461**	**0.478**
Change(%)		(2.4)	4.4	3.7	3.5	3.6
Data revenues (Rs mn)	**6,649**	**12,059**	**21,185**	**31,008**	**43,609**	**58,476**
Change(%)		81.4	75.7	46.4	40.6	34.1
SMS & VAS revenues (Rs mn)	**18,932**	**20,754**	**20,754**	**20,754**	**20,754**	**20,754**
Change(%)		9.6	—	—	—	—
ARPU (Rs/sub/month)	**158**	**156**	**172**	**184**	**195**	**205**
Change(%)		(1.1)	10.2	7.0	6.1	5.2
MOU (min/sub/month)	**373**	**378**	**400**	**412**	**423**	**429**
Change(%)		1.3	5.6	3.2	2.5	1.5
EBITDA per minute (Rs/min)	**0.100**	**0.101**	**0.117**	**0.129**	**0.140**	**0.151**
Change(%)		1.3	15.7	10.2	8.6	7.9
Capex (Rs mn)						
Standalone	**39,012**	**45,303**	**34,557**	**41,168**	**42,090**	**43,236**
As % of revenues	19.8	20.0	13.0	13.4	12.0	11.1
Consolidated	**42,020**	**49,131**	**39,104**	**45,514**	**46,233**	**47,160**
As % of revenues	21.5	21.9	14.8	14.9	13.3	12.3

Source: Company, Kotak Institutional Equities estimates

Exhibit 20: Idea Cellular's condensed financial statements, March fiscal year-ends, 2011-15E

	2011	2012	2013	2014E	2015E
Profit model (Rs mn)					
Revenue	155,034	195,412	224,575	264,317	305,808
EBITDA	37,907	50,923	60,044	77,714	94,990
EBIT	13,934	21,110	25,266	40,280	54,748
Net interest income / (expense)	(3,965)	(10,559)	(9,495)	(9,791)	(7,336)
Tax	(982)	(3,323)	(5,664)	(10,214)	(15,883)
Recurring Net profit	8,987	7,228	10,107	20,275	31,529
Fully diluted EPS	**2.7**	**2.2**	**3.1**	**6.1**	**9.5**
Balance sheet (Rs mn)					
Cash	14,777	2,497	11,709	12,145	20,824
Other current assets	25,980	47,119	51,660	59,370	69,877
Fixed assets	215,396	214,409	224,617	232,286	243,558
Other long term assets	45,981	62,327	75,794	69,794	63,794
Short tem debt	28,944	38,150	14,585	—	—
Other current liabilities	55,331	56,205	76,915	88,394	104,037
Long term debt	91,761	95,222	118,047	112,633	92,633
Other long term liabilities	3,099	6,273	11,180	11,180	11,180
Shareholders funds (incl. minorities)	122,999	130,502	143,053	161,389	190,204
Free cash flow (Rs mn)					
EBITDA	**37,907**	**50,923**	**60,044**	**77,714**	**94,990**
Change in working capital	(24,642)	7,897	3,769	5,136	5,362
Cash tax (paid)	(416)	(1,973)	(3,864)	(10,214)	(15,883)
Capex on PP&E and intangibles	(92,080)	(42,020)	(49,131)	(39,104)	(45,514)
Miscallenous	41,658	(29,216)	9,792	(1,367)	(226)
Free cash flow	**(37,573)**	**(14,389)**	**20,610**	**32,165**	**38,729**
Ratios (%)					
Sales growth	24.6	26.0	14.9	17.7	15.7
EBITDA growth	11.3	34.3	17.9	29.4	22.2
EPS growth	(0.5)	(19.6)	39.8	100.6	55.5
FCF growth	NM	NM	NM	56.1	20.4
EBITDA margin	**24.5**	**26.1**	**26.7**	**29.4**	**31.1**
Net margin	5.8	3.7	4.5	7.7	10.3
FCF margin	(24.2)	(7.4)	9.2	12.2	12.7
RoAE	7.4	5.7	7.4	13.3	17.9
ROAE (excl. cash and int. income)	**7.5**	**5.6**	**7.1**	**13.1**	**18.2**
RoACE	6.4	6.8	7.0	14.3	19.2
ROACE (excl. cash and int. income)	**6.4**	**6.9**	**7.0**	**14.8**	**20.2**
Net debt/EBITDA (X)	2.8	2.6	2.0	1.3	0.8
Net debt/equity (X)	0.9	1.0	0.8	0.6	0.4
Total debt/capital (X)	1.0	1.0	0.9	0.7	0.5

Source: Company, Kotak Institutional Equities estimates

June 2013: Results calendar

Mon	Tue	Wed	Thu	Fri	Sat
15-Jul	**16-Jul**	**17-Jul**	**18-Jul**	**19-Jul**	**20-Jul**
					HT Media
22-Jul	**23-Jul**	**24-Jul**	**25-Jul**	**26-Jul**	**27-Jul**
Asian Paints	Coromandel International	Ambuja Cements	ACC	Bharat Elect	Corporation Bank
Blue Star	Dewan Housing	Cairn India	Bata India	CESC	
IL&FS Investment Managers	L&T Finance Holdings	Central Bank	Biocon	Dish TV	
ING Vysya Bank	SBBJ	Dabur India	Container Corp	JSW ENERGY	
L&T	Shriram Trans	Hero MotoCorp	Gail India	Mcleod Russel	
Mangalore Ref		Indiabulls Real Estate	Indian Overseas Bank	Nestle India	
		Mahindra Lifespace Developers	ITC	Punjab National Bank	
		United Phos	Kalpataru Power	State Bank Trav	
		Yes Bank	Maruti Suzuki	Tata Communications	
			MMFSL	Torrent Pharma	
			Muthoot Finance	Wipro	
			Shriram City Union Finance		
			SKS Microfinance		
			Sterlite Industries		
			Thermax		
			Torrent Power		
			Zee Entertainment		
29-Jul	**30-Jul**	**31-Jul**	**1-Aug**	**2-Aug**	**3-Aug**
Bharti Infratel	Dr Reddys Lab	Bharti Airtel	Adani Ports	Berger Paints	Coal India
Colgate Palmolive	Financial Technologies	Chambal Fertilisers	Adani Power	ICRA	Godrej Consumers
IDFC	GMDC	Dishman Pharma	Castrol		
Madras Cements	Gujarat Pipavav	ICICI Bank	Idea Cellular		
Monsanto India	Havells India	JSW Steel			
Ultratech Cement	IPCA Lab	Karnataka Bank			
	NTPC	NHPC			
	Petronet LNG	Religare Enter			
	Shree Cement				
	Shree Cement				
	Syndicate Bank				
5-Aug	**6-Aug**	**7-Aug**	**8-Aug**	**9-Aug**	**10-Aug**
Tata Chemicals	Tata Power	Apollo tyres	Adani Enter	ABB	Godrej Industries
		Ranbaxy Laboratories	Jet Airways		
12-Aug	**13-Aug**	**14-Aug**	**15-Aug**	**16-Aug**	**17-Aug**
Brittania Industries	BPCL	Amara Raja Batteries			
	Hindalco Industries				
	Mahindra & Mahindra				

Source: BSE, NSE, Kotak Institutional Equities

Kotak Institutional Equities: Valuation summary of KIE Universe stocks

Company	19-Jul-13 Price (Rs)	Rating	Mkt cap. (Rs mn)	Mkt cap. (US$ mn)	O/S shares (mn)	EPS (Rs) 2013	EPS (Rs) 2014E	EPS (Rs) 2015E	EPS growth (%) 2013	EPS growth (%) 2014E	EPS growth (%) 2015E	PER (X) 2013	PER (X) 2014E	PER (X) 2015E	EV/EBITDA (X) 2013	EV/EBITDA (X) 2014E	EV/EBITDA (X) 2015E	Price/BV (X) 2013	Price/BV (X) 2014E	Price/BV (X) 2015E	Dividend yield (%) 2013	Dividend yield (%) 2014E	Dividend yield (%) 2015E	RoE (%) 2013	RoE (%) 2014E	RoE (%) 2015E	Target price (Rs)	Upside (%)	ADVT-3mo (US$ mn)
Automobiles																													
Amara Raja Batteries	248	REDUCE	42,336	713	171	16.8	16.9	17.6	33.3	0.5	4.0	14.8	14.7	14.1	8.3	8.7	7.9	4.0	3.3	2.8	1.0	1.4	1.4	30.4	24.6	21.5	240	(3.2)	1.5
Apollo Tyres	70	REDUCE	35,463	598	504	12.3	14.2	14.6	51.6	15.4	2.4	5.7	4.9	4.8	4.0	3.5	3.6	0.9	0.8	0.7	1.0	1.2	1.2	19.9	19.1	16.6	64	(9.0)	8.7
Ashok Leyland	15	ADD	40,442	681	2,661	0.5	(0.9)	1.1	(74.5)	(265.0)	224.5	28.1	(17.0)	13.7	9.5	15.6	7.3	0.8	0.8	0.8	3.9	(2.9)	3.3	12.6	(6.7)	8.2	18	18.4	1.8
Bajaj Auto	1,966	ADD	568,960	9,587	289	105.2	119.1	139.2	1.3	13.2	17.0	18.7	16.5	14.1	13.8	12.7	11.0	7.1	5.8	4.7	2.3	2.4	2.8	43.2	38.6	36.9	2,000	1.7	13.9
Bharat Forge	222	SELL	52,716	888	237	9.6	11.7	18.1	(44.7)	21.6	54.7	23.1	19.0	12.3	9.7	8.9	7.1	2.1	1.9	1.7	1.1	1.1	1.7	12.7	9.6	12.3	200	(10.0)	1.1
Exide Industries	134	ADD	114,240	1,925	850	6.2	7.6	8.6	13.4	23.0	14.1	21.9	17.8	15.6	14.5	12.1	10.9	3.3	2.9	2.6	1.2	1.4	1.6	16.1	17.6	17.8	135	0.4	3.0
Hero Motocorp	1,773	ADD	354,048	5,965	200	106.1	117.1	146.9	(10.9)	10.4	25.5	16.7	15.1	12.1	12.7	10.3	7.8	6.9	5.3	4.2	1.8	2.0	2.9	44.0	39.6	39.0	1,900	7.2	8.7
Mahindra & Mahindra	879	ADD	494,226	8,327	562	58.0	57.6	67.1	17.7	(0.7)	16.4	15.2	15.3	13.1	10.9	11.0	9.4	3.2	2.8	2.5	1.6	2.0	2.3	24.4	20.6	20.9	1,050	19.4	20.6
Maruti Suzuki	1,452	SELL	438,469	7,388	302	79.2	92.0	102.3	39.9	16.2	11.1	18.3	15.8	14.2	11.8	9.1	7.6	2.3	2.0	1.8	0.6	0.7	0.8	13.3	13.2	13.1	1,360	(6.3)	17.5
Motherson Sumi Systems	222	BUY	130,536	2,199	588	7.6	13.6	18.3	71.2	80.4	33.9	29.4	16.3	12.2	9.7	7.3	5.7	5.7	4.3	3.3	0.9	1.8	2.5	26.8	29.3	30.7	235	5.9	1.5
Tata Motors	295	BUY	948,139	15,975	3,218	30.7	35.0	41.9	(31.1)	14.0	19.4	9.6	8.4	7.0	5.0	4.4	3.9	2.6	2.0	1.6	0.7	-	-	28.8	27.3	25.1	330	12.0	42.0
Automobiles		**Neutral**	**3,219,576**	**54,247**					**(11.1)**	**8.5**	**20.7**	**13.7**	**12.6**	**10.4**	**7.8**	**6.9**	**5.9**	**3.2**	**2.6**	**2.2**	**1.3**	**1.2**	**1.5**	**23.2**	**20.8**	**20.8**			
Banks/Financial Institutions																													
Andhra Bank	78	ADD	43,451	732	560	23.0	22.0	23.6	(4.1)	(4.3)	7.0	3.4	3.5	3.3	—	—	—	0.6	0.6	0.5	6.4	6.2	6.6	16.2	13.9	13.4	110	41.7	2.0
Axis Bank	1,192	ADD	557,755	9,398	468	110.7	117.4	130.4	7.8	6.1	11.0	10.8	10.1	9.1	—	—	—	1.7	1.5	1.4	1.5	1.6	1.8	18.5	15.6	15.2	1,380	15.8	47.0
Bajaj Finserv	630	BUY	100,301	1,690	159	103.4	76.4	90.6	9.1	(26.1)	18.5	6.1	8.2	7.0	—	—	—	1.3	1.1	1.0	2.2	2.2	2.2	25.7	14.6	15.2	825	30.9	1.1
Bank of Baroda	571	REDUCE	235,593	3,970	412	109.3	115.5	119.2	(10.0)	5.7	3.2	5.2	4.9	4.8	—	—	—	0.8	0.7	0.7	3.8	4.0	4.1	15.7	14.5	13.5	740	29.5	13.1
Bank of India	212	ADD	126,189	2,126	597	46.1	55.4	58.3	(1.1)	20.2	5.1	4.6	3.8	3.6	—	—	—	0.7	0.6	0.6	4.7	5.7	6.0	12.9	13.7	13.1	365	72.6	5.2
Canara Bank	318	REDUCE	141,073	2,377	443	64.8	69.8	79.4	(12.5)	7.7	13.8	4.9	4.6	4.0	—	—	—	0.7	0.7	0.6	4.1	3.8	3.8	12.1	11.9	12.2	415	30.3	7.5
City Union Bank	53	BUY	28,591	482	539	6.0	6.7	7.8	(13.0)	11.6	17.1	8.9	8.0	6.8	—	—	—	1.8	1.4	1.2	1.7	1.9	2.2	22.3	19.4	18.8	70	32.0	0.2
Corporation Bank	326	BUY	49,826	840	153	93.8	102.3	108.7	(7.7)	9.0	6.3	3.5	3.2	3.0	—	—	—	0.6	0.5	0.5	6.1	6.7	7.1	16.1	15.4	14.6	480	47.3	1.0
Development Credit Bank	50	BUY	12,406	209	250	4.1	5.5	6.2	78.3	33.7	13.6	12.2	9.1	8.0	—	—	—	1.4	1.2	1.0	-	-	-	11.6	13.4	13.3	60	21.0	1.2
Federal Bank	382	BUY	65,379	1,102	171	49.0	44.0	56.6	7.9	(10.3)	28.7	7.8	8.7	6.8	—	—	—	1.1	1.0	0.9	2.4	2.1	2.7	13.9	11.3	13.2	530	38.7	3.9
HDFC	803	REDUCE	1,242,028	20,927	1,546	31.4	37.4	43.9	12.3	19.3	17.4	25.6	21.5	18.3	—	—	—	5.0	4.4	3.9	1.6	1.9	2.2	22.0	21.8	22.7	790	(1.6)	45.5
HDFC Bank	680	REDUCE	1,618,005	27,262	2,379	28.3	36.0	44.8	28.4	27.5	24.2	24.1	18.9	15.2	—	—	—	4.5	3.8	3.2	0.8	1.0	1.3	20.3	21.7	22.7	655	(3.7)	34.2
ICICI Bank	959	BUY	1,110,946	18,719	1,158	71.9	74.0	78.4	28.2	2.9	6.0	13.3	13.0	12.2	—	—	—	1.7	1.6	1.5	2.1	2.3	2.5	13.1	12.3	12.1	1,290	34.5	67.2
IDFC	126	BUY	190,482	3,209	1,512	12.1	14.0	16.3	18.1	15.1	16.4	10.4	9.0	7.7	—	—	—	1.4	1.2	1.1	1.9	2.2	2.5	14.2	14.6	15.2	185	46.9	17.6
India Infoline	55	ADD	16,594	280	304	9.2	10.9	13.1	102.9	17.7	20.3	5.9	5.0	4.2	—	—	—	0.8	0.7	0.6	5.6	3.4	4.1	15.1	16.4	16.2	77	41.2	0.4
Indian Bank	107	BUY	46,050	776	430	35.8	35.4	37.3	(9.5)	(1.1)	5.4	3.0	3.0	2.9	—	—	—	0.5	0.5	0.4	6.2	5.9	6.2	15.4	13.6	13.0	230	114.7	0.5
Indian Overseas Bank	48	REDUCE	43,895	740	924	6.1	16.5	19.4	(53.3)	169.0	17.2	7.7	2.9	2.4	—	—	—	0.4	0.4	0.3	4.2	8.1	9.6	4.5	10.9	11.7	65	36.8	1.2
IndusInd Bank	445	ADD	232,677	3,920	523	20.3	24.9	28.1	18.3	22.8	12.5	21.9	17.8	15.9	—	—	—	3.2	2.8	2.5	0.7	0.8	0.9	18.3	16.6	16.1	530	19.1	14.7
ING Vysya Bank	576	ADD	107,842	1,817	187	39.6	37.0	44.8	30.2	(6.4)	21.1	14.5	15.5	12.8	—	—	—	2.4	1.5	1.4	0.8	0.9	1.1	14.6	11.9	11.2	650	12.9	2.4
J&K Bank	1,247	REDUCE	60,479	1,019	48	217.6	199.6	188.1	31.4	(8.3)	(5.8)	5.7	6.2	6.6	—	—	—	1.3	1.1	1.0	4.0	3.7	3.5	23.6	18.5	15.4	1,320	5.8	1.5
Karur Vysya Bank	411	ADD	44,019	742	107	51.3	52.9	62.2	9.7	3.1	17.5	8.0	7.8	6.6	—	—	—	1.5	1.3	1.1	3.4	3.2	3.8	19.0	17.3	17.9	510	24.2	0.7
LIC Housing Finance	208	ADD	105,206	1,773	505	20.3	25.4	30.8	11.9	25.3	21.3	10.3	8.2	6.8	—	—	—	1.7	1.4	1.2	1.9	2.4	2.9	16.8	18.4	19.3	300	44.0	12.9
L&T Finance Holdings	74	SELL	126,892	2,138	1,715	4.3	4.7	5.3	60.3	10.1	12.8	17.4	15.8	14.0	—	—	—	2.3	2.0	1.7	—	—	—	14.1	13.4	13.2	60	(18.9)	3.1
Magma Fincorp	88	BUY	16,720	282	190	6.5	10.2	12.3	100.6	55.6	21.0	13.5	8.7	7.2	—	—	—	1.2	1.1	1.0	1.3	1.8	2.2	10.1	12.7	14.0	125	42.0	0.3
Mahindra & Mahindra Financial	250	REDUCE	142,088	2,394	568	15.5	18.9	21.8	28.6	21.6	15.2	16.1	13.2	11.5	—	—	—	3.3	2.8	2.4	1.5	1.8	2.0	23.8	22.2	21.8	230	(8.0)	7.1
Muthoot Finance	97	NR	38,555	650	397	28.2	29.9	34.9	17.3	6.1	16.7	3.4	3.3	2.8	—	—	—	1.0	0.7	0.6	4.1	4.6	5.4	31.2	26.2	23.7	—	—	—
Oriental Bank of Commerce	173	REDUCE	50,606	853	292	45.5	53.7	56.7	16.3	17.9	5.6	3.8	3.2	3.1	—	—	—	0.5	0.4	0.4	5.3	6.3	6.6	10.7	11.7	11.4	280	61.4	4.0
PFC	133	ADD	175,669	2,960	1,319	33.5	36.7	43.6	45.6	9.6	18.7	4.0	3.6	3.1	—	—	—	0.7	0.7	0.6	5.3	5.8	6.8	19.8	18.7	19.2	245	84.0	9.3
Punjab National Bank	631	REDUCE	223,042	3,758	353	134.3	130.2	144.3	(6.7)	(3.0)	10.8	4.7	4.8	4.4	—	—	—	0.8	0.8	0.7	4.3	4.1	4.6	16.5	13.9	13.9	810	28.4	11.9
Reliance Capital	370	ADD	91,055	1,534	246	26.9	23.4	28.5	27.5	(13.0)	21.7	13.7	15.8	13.0	—	—	—	0.8	0.8	0.7	2.2	1.9	2.3	5.9	4.9	5.8	505	36.5	34.5
Rural Electrification Corp.	192	ADD	189,727	3,197	987	38.7	44.3	47.6	35.3	14.6	7.5	5.0	4.3	4.0	—	—	—	1.1	1.0	0.9	4.3	4.1	4.9	23.7	22.8	20.7	270	40.5	5.3
Shriram City Union Finance	937	NR	54,625	920	58	80.2	98.3	118.7	22.6	22.6	20.7	11.7	9.5	7.9	—	—	—	2.4	1.9	1.6	1.0	1.4	1.6	22.3	22.5	22.0	—	—	0.6
Shriram Transport	660	ADD	147,239	2,481	223	61.0	71.8	84.8	8.2	17.7	18.2	10.8	9.2	7.8	—	—	—	2.1	1.8	1.5	1.1	1.5	1.8	20.6	20.4	20.3	800	21.2	11.8
State Bank of India	1,811	ADD	1,238,984	20,876	684	206.2	210.4	227.0	18.2	2.0	7.9	8.8	8.6	8.0	—	—	—	1.6	1.4	1.3	2.3	2.4	2.5	15.4	13.8	13.4	2,430	34.2	88.0
Union Bank	157	ADD	93,427	1,574	597	36.0	36.4	37.4	11.5	1.3	2.6	4.4	4.3	4.2	—	—	—	0.7	0.6	0.5	5.1	5.1	5.3	15.0	13.1	12.3	285	82.1	6.4
Yes Bank	425	REDUCE	152,271	2,566	359	36.3	36.9	39.3	31.0	1.8	6.4	11.7	11.5	10.8	—	—	—	2.6	2.2	1.9	1.4	1.4	1.5	24.8	20.9	18.9	450	6.0	19.1
Banks/Financial Institutions		**Cautious**	**8,919,686**	**150,290**					**15.7**	**8.9**	**11.8**	**10.2**	**9.4**	**8.4**	**—**	**—**	**—**	**1.7**	**1.5**	**1.3**	**2.1**	**2.3**	**2.5**	**16.6**	**16.1**	**16.0**			
Cement																													
ACC	1,276	REDUCE	239,641	4,038	188	73.7	68.1	79.6	29.1	(7.7)	16.9	17.3	18.7	16.0	10.8	10.7	8.6	3.0	2.8	2.5	2.8	1.8	1.8	19.5	16.4	17.1	1,170	(8.3)	5.5
Ambuja Cements	207	REDUCE	315,588	5,317	1,522	10.3	10.1	12.3	32.8	(2.3)	21.3	20.0	20.5	16.9	11.5	11.4	10.0	3.4	3.2	2.9	1.3	1.3	2.1	17.8	16.1	17.7	175	(15.6)	7.7
Grasim Industries	2,817	ADD	258,343	4,353	92	272.6	312.6	354.8	(5.6)	14.7	13.5	10.3	9.0	7.9	5.7	5.0	3.6	1.3	1.2	1.0	0.8	1.2	1.2	13.7	13.9	14.0	3,500	24.3	3.0
India Cements	58	ADD	17,678	298	307	6.8	8.9	9.5	(24.4)	31.2	7.2	8.5	6.5	6.0	4.2	3.6	3.0	0.4	0.4	0.4	3.7	5.5	5.5	5.2	6.6	6.6	95	65.1	1.3
Shree Cement	4,451	SELL	155,059	2,613	35	281.2	303.0	336.2	76.1	7.7	11.0	15.8	14.7	13.2	9.4	7.5	6.4	4.5	3.6	2.9	0.4	0.4	0.4	32.2	27.3	24.4	3,700	(16.9)	0.9
UltraTech Cement	1,930	SELL	529,236	8,917	274	101.3	108.7	131.5	13.4	7.3	21.0	19.1	17.8	14.7	11.7	9.8	8.0	3.1	2.6	2.2	0.5	0.5	0.5	18.9	18.0	18.4	1,700	(11.9)	6.8
Cement		**Cautious**	**1,515,545**	**25,536**					**15.1**	**6.0**	**16.9**	**16.1**	**15.2**	**13.0**	**9.0**	**7.9**	**6.5**	**2.5**	**2.2**	**1.9**	**1.1**	**1.1**	**1.2**	**15.3**	**14.4**	**14.7**			

Source: Company, Bloomberg, Kotak Institutional Equities estimates

Kotak Institutional Equities: Valuation summary of KIE Universe stocks

	19-Jul-13		Mkt cap.		O/S shares	EPS (Rs)			EPS growth (%)			PER (X)			EV/EBITDA (X)			Price/BV (X)			Dividend yield (%)			RoE (%)			Target price	Upside	ADVT-3mo
Company	**Price (Rs)**	**Rating**	**(Rs mn)**	**(US$ mn)**	**(mn)**	**2013**	**2014E**	**2015E**	**2013**	**2014E**	**2015E**	**2013**	**2014E**	**2015E**	**2013**	**2014E**	**2015E**	**2013**	**2014E**	**2015E**	**2013**	**2014E**	**2015E**	**2013**	**2014E**	**2015E**	**(Rs)**	**(%)**	**(US$ mn)**
Consumer products																													
Asian Paints	5,165	SELL	495,465	8,348	96	116.1	135.3	159.2	12.7	16.5	17.7	44.5	38.2	32.5	28.2	23.5	19.9	14.0	11.6	9.8	0.9	1.1	1.4	36.3	34.9	34.6	3,850	(25.5)	7.5
Bajaj Corp.	245	BUY	36,101	608	148	11.3	13.8	16.4	39.4	21.7	18.9	21.6	17.7	14.9	19.9	15.7	12.7	7.5	6.6	5.9	2.7	3.4	4.1	26.4	32.6	35.2	320	30.7	0.5
Colgate-Palmolive (India)	1,497	SELL	203,588	3,430	136	36.5	41.3	46.6	11.3	12.9	13.1	41.0	36.3	32.1	30.3	26.5	23.0	43.6	35.1	31.9	1.9	2.1	2.4	107.4	102.7	100.4	1,300	(13.2)	3.0
Dabur India	168	ADD	292,197	4,923	1,743	4.4	5.4	6.4	19.1	23.3	17.8	38.3	31.0	26.3	29.9	24.0	20.1	13.8	11.1	9.0	0.9	1.3	1.5	40.0	39.8	37.9	160	(4.6)	3.8
GlaxoSmithkline Consumer	5,300	SELL	222,902	3,756	42	103.8	124.9	149.0	20.7	20.2	19.3	51.0	42.4	35.6	44.8	37.8	31.6	16.4	13.9	11.9	0.8	1.1	1.4	34.9	35.4	36.1	3,500	(34.0)	4.5
Godrej Consumer Products	951	REDUCE	323,557	5,452	340	20.3	26.2	32.8	20.4	29.4	24.9	46.9	36.3	29.0	35.1	25.9	20.2	9.2	7.6	6.2	0.5	0.6	0.7	22.6	24.5	25.4	825	(13.2)	4.2
Hindustan Unilever	686	REDUCE	1,483,691	24,999	2,163	15.4	15.8	17.3	28.1	2.6	9.2	44.5	43.4	39.7	36.6	33.1	28.5	60.1	45.8	37.1	2.7	1.5	1.7	103.1	111.7	97.6	530	(22.8)	39.0
ITC	369	ADD	2,938,302	49,508	7,962	9.3	11.1	13.0	19.0	19.3	17.1	39.6	33.2	28.3	28.1	23.4	19.8	12.5	11.2	10.0	1.4	1.7	2.1	36.1	37.4	38.9	350	(5.2)	39.2
Jubilant Foodworks	1,175	SELL	77,861	1,312	66	19.9	25.0	34.0	21.7	25.4	35.8	58.9	47.0	34.6	32.1	24.9	18.1	18.1	13.7	10.5	—	—	0.6	30.5	29.2	30.6	900	(23.4)	7.6
Jyothy Laboratories	178	ADD	29,317	494	165	1.1	4.3	8.3	(53.3)	290.2	91.2	160.2	41.1	21.5	26.9	17.5	13.1	4.5	4.2	3.7	1.4	0.6	1.3	—	—	—	200	12.2	0.5
Marico	219	REDUCE	141,247	2,380	645	5.6	6.7	7.9	8.1	19.5	17.3	39.0	32.6	27.8	23.4	20.3	17.5	7.0	6.0	5.2	0.5	0.6	0.9	23.2	20.2	20.4	210	(4.2)	1.2
Nestle India	5,703	SELL	549,850	9,265	96	110.8	126.6	142.7	5.9	14.3	12.8	51.5	45.1	39.9	30.4	25.5	22.6	30.6	23.2	18.5	0.9	1.0	1.2	71.6	60.3	52.9	4,050	(29.0)	2.7
Speciality Restaurants	150	ADD	7,028	118	47	5.0	6.5	7.6	1.8	30.2	17.6	30.0	23.1	19.6	18.9	14.4	11.3	2.4	2.2	2.0	—	—	—	11.5	10.0	10.6	195	30.3	0.1
Tata Global Beverages	156	BUY	96,285	1,622	618	6.3	7.4	8.5	14.8	17.3	13.8	24.6	21.0	18.4	14.5	12.0	10.5	1.7	1.6	1.5	1.6	2.0	2.4	8.4	9.3	10.1	165	6.0	6.7
Titan Industries	261	ADD	232,112	3,911	888	8.2	9.3	11.1	20.9	13.4	20.1	32.0	28.2	23.5	21.8	18.7	15.2	11.8	9.3	7.4	0.9	1.1	1.2	42.3	36.8	34.9	295	12.8	15.0
United Breweries	830	SELL	219,324	3,695	264	6.5	10.2	15.1	36.2	56.7	47.5	127.0	81.0	54.9	48.3	32.9	25.0	15.4	13.4	11.3	0.2	0.2	0.4	12.0	17.1	21.6	700	(15.6)	5.6
United Spirits	2,740	ADD	398,242	6,710	145	9.4	64.1	79.2	(30.8)	579.9	23.5	290.6	42.7	34.6	34.9	23.6	20.0	6.6	4.4	4.0	0.3	0.2	0.3	8.3	12.4	12.1	2,900	5.8	67.6
Consumer products		**Cautious**	**7,747,068**	**130,532**					**17.3**	**24.3**	**17.1**	**45.3**	**36.5**	**31.1**	**30.3**	**25.0**	**21.1**	**13.4**	**11.2**	**9.8**	**1.4**	**1.4**	**1.6**	**29.6**	**30.8**	**31.5**			
Constructions																													
NCC	26	ADD	6,735	113	257	2.4	2.3	2.6	74.2	(5.9)	15.0	10.7	11.4	9.9	6.0	6.4	6.2	0.3	0.3	0.3	2.3	3.8	3.8	2.6	2.4	2.7	55	109.5	0.7
Punj Lloyd	32	REDUCE	10,714	181	340	(0.9)	1.2	4.2	(125.9)	236.3	257.6	(36.8)	27.0	7.6	6.0	5.6	5.1	0.4	0.4	0.4	(0.1)	0.3	1.2	(1.0)	1.4	4.9	45	42.6	3.4
Sadbhav Engineering	89	BUY	13,359	225	151	4.9	5.6	9.7	(47.3)	13.8	74.6	18.0	15.8	9.1	12.8	7.9	5.8	1.5	1.4	1.2	0.7	0.7	0.7	8.6	9.0	13.7	180	103.4	0.3
Construction		**Cautious**	**30,808**	**519**					**(62.7)**	**69.9**	**95.0**	**28.6**	**16.8**	**8.6**	**6.6**	**6.1**	**5.4**	**0.5**	**0.5**	**0.5**	**0.8**	**1.2**	**1.5**	**1.8**	**2.9**	**5.4**			
Energy																													
Aban Offshore	243	RS	10,560	178	44	38.6	80.1	81.1	(43.5)	107.5	1.2	6.3	3.0	3.0	7.4	6.1	5.9	0.3	0.3	0.3	1.5	2.1	2.1	6.4	10.4	9.4	—	—	1.8
Bharat Petroleum	347	BUY	250,656	4,223	723	36.6	35.8	41.0	99.2	(2.1)	14.7	9.5	9.7	8.4	6.9	6.1	5.2	1.4	1.2	1.1	2.8	3.1	3.6	14.6	12.7	13.3	485	39.9	6.3
Cairn india	308	BUY	588,449	9,915	1,910	63.1	61.9	55.0	51.7	(2.0)	(11.2)	4.9	5.0	5.6	3.9	3.6	3.8	1.2	1.0	0.9	3.7	3.9	3.9	24.8	22.4	17.1	350	13.6	10.1
Castrol India	332	SELL	164,021	2,764	495	9.0	10.0	10.8	(4.4)	10.8	7.8	36.7	33.1	30.7	25.4	22.2	20.4	28.1	26.6	24.9	2.1	2.4	2.6	79.0	82.6	83.8	220	(33.7)	0.9
GAIL (India)	333	ADD	422,023	7,111	1,268	35.5	31.6	33.4	16.5	(10.9)	5.6	9.4	10.5	10.0	6.3	6.6	6.0	1.6	1.4	1.3	2.9	2.7	3.0	17.2	13.6	12.9	380	14.2	6.5
GSPL	56	ADD	31,652	533	563	9.6	8.4	9.2	2.6	(12.6)	9.8	5.9	6.7	6.1	3.7	3.6	3.2	1.0	0.8	0.7	1.8	1.8	3.3	17.6	13.2	12.9	78	38.7	0.6
Hindustan Petroleum	227	ADD	76,786	1,294	339	26.7	24.6	30.2	(0.5)	(8.0)	23.1	8.5	9.2	7.5	8.4	8.2	6.7	0.4	0.4	0.4	3.8	3.5	4.2	5.1	4.5	5.3	290	28.0	3.4
Indian Oil Corporation	225	ADD	547,139	9,219	2,428	16.8	26.3	31.8	(48.7)	56.4	20.9	13.4	8.6	7.1	10.1	6.4	5.1	0.9	0.8	0.8	2.8	3.3	4.0	6.2	9.4	10.6	300	33.1	2.4
Oil India	552	BUY	331,550	5,586	601	59.7	61.9	67.4	4.1	3.6	8.9	9.2	8.9	8.2	4.4	3.7	3.1	1.6	1.5	1.4	5.4	5.6	5.5	16.0	15.3	15.5	700	26.9	6.2
Oil & Natural Gas Corporation	317	BUY	2,711,672	45,690	8,556	29.9	33.6	39.3	(8.9)	12.5	16.8	10.6	9.4	8.1	4.4	3.6	2.9	1.4	1.3	1.2	3.0	3.5	4.1	13.5	13.7	14.4	400	26.2	21.6
Petronet LNG	125	BUY	93,675	1,578	750	15.3	12.8	14.6	8.7	(16.5)	14.0	8.2	9.8	8.6	5.6	6.7	5.3	1.9	1.6	1.4	2.0	2.0	2.4	25.6	17.5	16.8	175	40.1	2.3
Reliance Industries	924	ADD	2,711,983	45,695	2,936	65.0	68.1	71.8	6.2	4.7	5.4	14.2	13.6	12.9	9.2	9.2	8.0	1.4	1.3	1.2	1.0	1.0	1.1	11.3	10.9	10.5	980	6.1	55.9
Energy		**Attractive**	**7,940,167**	**133,785**					**0.7**	**7.7**	**8.9**	**10.4**	**9.6**	**8.8**	**6.4**	**5.6**	**4.7**	**1.4**	**1.2**	**1.1**	**2.4**	**2.6**	**3.0**	**13.1**	**12.7**	**12.6**			
Industrials																													
ABB	581	SELL	123,193	2,076	212	6.7	17.0	24.5	(23.6)	155.6	44.3	87.4	34.2	23.7	51.2	21.1	15.6	4.7	4.3	3.7	0.6	0.6	0.6	5.5	13.1	16.8	425	(26.9)	1.9
BGR Energy Systems	119	REDUCE	8,580	145	72	22.3	16.9	18.2	(28.1)	(24.6)	8.1	5.3	7.1	6.5	4.9	4.3	3.6	0.7	0.7	0.6	3.8	3.0	3.2	13.8	9.6	9.7	150	26.2	0.7
Bharat Electronics	1,201	REDUCE	96,104	1,619	80	113.6	122.9	135.3	6.8	8.2	10.1	10.6	9.8	8.9	8.0	4.3	3.4	1.4	1.3	1.2	2.5	2.5	2.5	14.5	14.0	14.0	1,370	14.0	0.5
Bharat Heavy Electricals	174	SELL	425,148	7,163	2,448	27.1	21.1	16.2	(6.0)	(22.0)	(23.2)	6.4	8.2	10.7	4.1	4.9	5.7	1.4	1.2	1.1	3.3	2.6	2.0	23.7	16.0	11.1	175	0.7	10.5
Crompton Greaves	88	ADD	56,292	948	642	1.3	5.4	8.1	(77.2)	314.1	50.0	67.1	16.2	10.8	15.9	8.2	6.3	1.6	1.5	1.3	1.4	1.4	1.6	2.3	9.4	12.9	105	19.7	4.7
Cummins India	451	REDUCE	125,045	2,107	277	28.3	26.1	28.8	28.3	(7.7)	10.4	15.9	17.3	15.6	15.6	14.8	13.3	5.2	4.6	4.1	2.9	2.6	2.8	34.5	27.5	26.3	450	(0.2)	1.7
Kalpataru Power Transmission	65	BUY	10,013	169	153	8.8	13.1	15.3	(34.1)	49.0	17.6	7.4	5.0	4.3	5.5	3.9	3.4	0.5	0.5	0.4	2.3	2.3	2.3	6.6	9.2	9.9	120	83.9	0.1
KEC International	34	BUY	8,767	148	257	2.5	6.5	9.3	(63.1)	154.7	44.4	13.5	5.3	3.7	6.3	4.8	3.9	0.7	0.7	0.6	1.1	2.8	4.1	5.5	13.0	16.6	70	105.3	0.2
Larsen & Toubro	974	ADD	899,099	15,149	923	52.4	51.9	64.0	4.4	(1.0)	23.3	18.6	18.8	15.2	15.1	13.9	12.6	2.6	2.2	1.9	1.3	0.8	0.8	15.2	12.6	13.2	1,075	10.4	41.2
Siemens	559	SELL	196,856	3,317	352	10.0	18.6	23.2	(27.4)	86.6	24.8	56.2	30.1	24.1	23.5	14.1	11.6	5.0	4.6	4.2	0.9	1.0	1.0	8.8	15.9	18.3	425	(24.0)	3.3
Thermax	605	REDUCE	72,102	1,215	119	26.4	31.6	37.0	(19.7)	19.4	17.3	22.9	19.2	16.3	14.7	12.3	10.2	3.9	3.4	3.0	1.5	1.5	1.7	18.0	18.9	19.5	575	(5.0)	0.7
Voltas	81	BUY	26,704	450	331	5.9	7.8	8.8	(37.6)	31.7	12.9	13.7	10.4	9.2	9.1	6.0	5.0	1.6	1.5	1.3	2.2	2.9	3.3	12.5	14.9	15.3	105	30.0	2.0
Industrials		**Cautious**	**2,047,902**	**34,506**					**(5.6)**	**(3.2)**	**5.5**	**14.1**	**14.5**	**13.8**	**10.9**	**10.3**	**10.0**	**2.2**	**1.9**	**1.7**	**1.8**	**1.5**	**1.4**	**15.9**	**13.3**	**12.6**			

Source: Company, Bloomberg, Kotak Institutional Equities estimates

Kotak Institutional Equities: Valuation summary of KIE Universe stocks

Company	19-Jul-13 Price (Rs)	Rating	Mkt cap. (Rs mn)	Mkt cap. (US$ mn)	O/S shares (mn)	EPS (Rs) 2013	EPS (Rs) 2014E	EPS (Rs) 2015E	EPS growth (%) 2013	EPS growth (%) 2014E	EPS growth (%) 2015E	PER (X) 2013	PER (X) 2014E	PER (X) 2015E	EV/EBITDA (X) 2013	EV/EBITDA (X) 2014E	EV/EBITDA (X) 2015E	Price/BV (X) 2013	Price/BV (X) 2014E	Price/BV (X) 2015E	Dividend yield (%) 2013	Dividend yield (%) 2014E	Dividend yield (%) 2015E	RoE (%) 2013	RoE (%) 2014E	RoE (%) 2015E	Target price (Rs)	Upside (%)	ADVT-3mo (US$ mn)
Infrastructure																													
Adani Port and SEZ	147	BUY	295,960	4,987	2,017	8.1	9.8	12.6	48.7	20.4	28.6	18.1	15.0	11.7	17.0	11.8	9.4	4.5	3.4	2.7	0.8	1.2	1.4	28.5	25.8	25.8	180	22.7	7.2
Container Corporation	1,117	ADD	145,129	2,445	130	72.5	80.9	93.0	7.4	11.6	14.9	15.4	13.8	12.0	11.1	10.0	8.2	2.3	2.1	1.8	1.5	1.7	1.9	15.9	15.8	16.1	1,150	3.0	1.1
GMR Infrastructure	16	RS	62,278	1,049	3,892	(1.8)	(0.6)	(0.7)	(56.2)	67.2	(19.6)	(9.0)	(27.6)	(23.0)	17.3	9.0	5.9	0.7	0.7	0.8	—	—	—	(9.3)	(3.2)	(3.9)	—	—	2.6
Gujarat Pipavav Port	48	BUY	23,205	391	483	1.5	3.1	3.4	29.7	104.0	7.6	31.4	15.4	14.3	13.1	10.7	9.0	1.9	1.7	1.5	—	—	—	7.6	14.0	11.9	60	25.0	0.3
IRB Infrastructure	94	BUY	31,126	524	332	16.7	16.6	13.7	11.1	(0.8)	(17.5)	5.6	5.6	6.8	6.1	5.2	5.3	0.7	0.6	0.6	—	—	—	15.1	11.8	8.8	170	81.5	4.2
Infrastructure		**Cautious**	**557,699**	**9,397**					**20.3**	**38.8**	**16.9**	**22.1**	**15.9**	**13.6**	**13.9**	**9.3**	**7.2**	**2.0**	**1.8**	**1.6**	**0.8**	**1.0**	**1.2**	**9.2**	**11.4**	**12.0**			
Media																													
DB Corp	267	BUY	48,960	825	183	11.9	14.8	17.7	7.9	24.6	19.3	22.4	18.0	15.1	12.7	10.3	8.5	4.8	4.2	3.8	2.1	2.6	3.4	22.3	24.9	26.6	300	12.4	0.3
DishTV	57	ADD	60,678	1,022	1,064	(1.4)	0.2	1.3	(33.9)	115.4	543.2	(42.0)	272.9	42.4	12.2	10.0	8.1	(37.5)	(43.5)	(50)	—	—	1.8	113.0	(14.8)	(110)	75	31.5	2.7
Eros International	135	ADD	12,367	208	92	16.7	20.4	23.8	1.5	22.0	16.5	8.1	6.6	5.7	5.6	4.7	3.9	1.2	1.0	0.9	—	—	—	16.7	17.2	16.7	200	48.4	0.5
Jagran Prakashan	90	BUY	28,431	479	316	5.4	6.5	8.4	(4.5)	20.4	29.0	16.7	13.9	10.7	9.2	7.9	6.3	3.3	3.1	2.8	3.9	4.4	5.0	21.0	22.9	27.1	130	44.6	0.2
Sun TV Network	401	ADD	157,829	2,659	394	18.0	18.9	22.5	2.6	4.7	19.3	22.2	21.2	17.8	13.9	13.0	10.9	5.4	5.1	4.8	2.5	3.0	4.0	26.5	25.6	28.8	400	(0.1)	7.9
Zee Entertainment Enterprises	240	REDUCE	227,905	3,840	950	7.6	8.8	10.7	25.6	16.1	21.8	31.7	27.3	22.4	22.2	18.4	14.9	4.6	4.3	4.1	0.7	0.9	1.0	15.3	16.6	19.2	220	(8.3)	10.0
Media		**Neutral**	**567,914**	**9,569**					**8.1**	**23.4**	**25.9**	**27.4**	**22.2**	**17.6**	**13.9**	**11.8**	**9.6**	**4.5**	**4.1**	**3.8**	**1.5**	**1.9**	**2.6**	**16.3**	**18.5**	**21.7**			
Metals & Mining																													
Coal India	297	BUY	1,875,960	31,608	6,316	27.5	29.3	33.3	18.1	6.8	13.5	10.8	10.1	8.9	6.9	5.5	4.5	3.9	3.4	2.9	4.9	5.2	5.9	38.2	35.6	35.1	410	38.0	14.8
Hindalco Industries	104	REDUCE	198,500	3,345	1,915	15.8	10.8	9.8	(10.9)	(31.9)	(8.7)	6.6	9.6	10.6	8.5	8.9	7.9	0.6	0.5	0.5	1.4	1.4	1.4	9.0	5.7	5.0	100	(3.5)	13.2
Hindustan Zinc	104	ADD	440,879	7,428	4,225	16.4	14.7	15.3	24.2	(10.4)	4.1	6.4	7.1	6.8	3.5	3.0	2.2	1.4	1.2	1.1	3.0	3.0	3.0	23.5	17.9	16.4	150	43.7	1.2
Jindal Steel and Power	210	ADD	196,729	3,315	935	31.1	34.4	38.3	(26.6)	10.4	11.5	6.8	6.1	5.5	6.6	7.2	6.1	0.9	0.8	0.7	0.9	0.9	0.9	14.9	14.2	13.9	385	82.9	19.0
JSW Steel	571	SELL	127,491	2,148	223	43.2	55.7	85.7	79.1	28.9	54.0	13.2	10.3	6.7	5.0	5.6	5.2	0.7	0.7	0.6	1.8	1.8	1.8	7.8	7.0	10.0	585	2.4	13.1
National Aluminium Co.	30	REDUCE	76,544	1,290	2,577	2.3	2.7	3.1	(31.2)	15.4	15.7	12.9	11.2	9.7	3.1	3.4	3.8	0.6	0.6	0.6	4.2	4.2	4.2	5.0	5.7	6.4	38	27.9	0.2
NMDC	108	BUY	426,800	7,191	3,965	16.0	14.2	14.9	(13.3)	(10.9)	4.9	6.7	7.6	7.2	2.9	3.3	3.0	1.6	1.4	1.3	6.5	6.5	6.5	24.4	19.7	18.9	150	39.3	4.5
Sesa Goa	146	ADD	126,932	2,139	869	26.2	25.8	24.9	(15.4)	(1.8)	(3.5)	5.6	5.7	5.9	36.9	25.4	17.0	0.7	0.6	0.6	0.1	0.1	0.1	3.3	(0.3)	1.5	180	23.2	4.2
Sterlite Industries	83	ADD	278,139	4,686	3,361	18.4	14.9	15.5	16.6	(19.1)	4.5	4.5	5.6	5.3	3.5	3.6	3.3	0.5	0.5	0.5	2.8	2.8	2.8	12.7	9.4	9.1	110	32.9	6.7
Tata Steel	241	ADD	234,110	3,945	971	3.4	40.0	49.7	(86.9)	1,070.7	24.2	70.5	6.0	4.8	6.5	5.4	5.5	0.7	0.6	0.6	3.3	5.0	5.0	0.9	11.0	12.6	370	53.5	26.3
Metals & Mining		**Neutral**	**3,982,084**	**67,095**					**0.2**	**1.8**	**10.4**	**8.3**	**8.2**	**7.4**	**5.8**	**5.5**	**4.9**	**1.3**	**1.2**	**1.1**	**4.0**	**4.2**	**4.5**	**16.1**	**14.9**	**15.0**			
Pharmaceutical																													
Apollo Hospitals	988	SELL	137,464	2,316	139	21.4	27.6	33.4	35.7	28.7	21.2	46.1	35.9	29.6	23.6	19.1	15.6	5.0	4.5	4.1	0.6	0.7	0.8	11.3	13.3	14.6	850	(14.0)	8.0
Biocon	306	ADD	61,130	1,030	200	25.4	19.3	22.6	48.7	(24.2)	17.3	12.0	15.8	13.5	10.7	8.8	7.9	2.3	2.1	1.9	2.5	2.0	2.3	20.5	13.7	14.7	295	(3.5)	1.6
Cipla	416	ADD	333,654	5,622	803	18.7	18.3	21.5	34.0	(2.4)	17.7	22.2	22.7	19.3	16.0	14.6	12.1	3.7	3.2	2.8	0.5	0.5	0.5	16.0	15.2	15.6	420	1.1	10.0
Cadila Healthcare	775	ADD	158,702	2,674	205	32.0	39.7	53.2	0.4	24.1	34.0	24.2	19.5	14.6	19.2	15.3	11.8	5.2	4.4	3.6	1.0	1.2	1.6	23.3	24.4	27.1	840	8.4	2.0
Divi's Laboratories	976	REDUCE	129,489	2,182	133	45.4	51.4	61.0	12.9	13.3	18.7	21.5	19.0	16.0	15.6	13.3	10.9	5.2	4.4	3.8	1.5	1.7	2.0	26.0	25.1	25.4	1,060	8.6	3.2
Dr Reddy's Laboratories	2,346	BUY	398,368	6,712	170	96.3	112.2	132.0	14.6	16.5	17.7	24.4	20.9	17.8	16.4	13.9	11.8	5.5	4.5	3.8	0.6	0.7	0.8	24.1	23.4	23.2	2,400	2.3	14.2
GlaxoSmithkline Pharmaceuticals	2,527	SELL	214,188	3,609	85	81.4	84.5	97.5	9.7	3.8	15.5	31.0	29.9	25.9	23.9	22.9	19.1	10.7	9.8	8.9	2.0	2.2	2.4	28.5	34.2	36.0	1,920	(24.0)	1.6
Glenmark Pharmaceuticals	605	REDUCE	163,855	2,761	271	22.7	28.1	33.1	3.7	23.7	17.9	26.7	21.6	18.3	18.9	14.8	12.7	5.9	4.7	3.8	0.3	0.3	0.3	23.8	24.4	23.1	535	(11.6)	5.6
Lupin	899	ADD	401,942	6,772	447	29.4	32.8	38.9	51.0	11.5	18.6	30.6	27.4	23.1	18.3	16.3	13.8	7.6	6.2	5.1	0.4	0.6	0.7	28.5	25.3	24.6	800	(11.0)	15.5
Ranbaxy Laboratories	324	REDUCE	137,087	2,310	423	21.8	16.5	28.6	217.7	(24.4)	73.0	14.9	19.6	11.3	8.1	13.9	6.9	3.4	2.5	1.5	—	—	—	26.5	12.8	14.8	430	32.7	10.2
Sun Pharmaceuticals	1,080	SELL	1,118,574	18,847	1,036	29.0	36.8	41.9	16.3	26.8	13.8	37.2	29.3	25.8	20.7	19.1	16.6	7.1	5.8	4.8	0.5	0.6	0.7	20.7	21.7	20.2	825	(23.6)	21.0
Pharmaceuticals		**Attractive**	**3,254,454**	**54,835**					**43.7**	**11.2**	**20.8**	**27.6**	**24.8**	**20.6**	**17.6**	**16.2**	**13.3**	**5.7**	**4.7**	**3.9**	**0.7**	**0.8**	**0.9**	**20.6**	**19.1**	**18.9**			
Real Estate																													
DLF	168	ADD	299,474	5,046	1,779	4.0	4.2	11.1	(41.9)	5.9	163.5	42.5	40.1	15.2	20.1	17.0	11.0	1.1	1.0	1.0	1.1	1.2	1.2	2.5	2.6	6.5	270	60.4	30.6
HDIL	39	NR	16,530	279	419	1.7	11.0	14.3	(91.0)	528.0	30.4	22.6	3.6	2.8	8.1	7.1	6.1	0.2	0.2	0.1	—	—	—	0.7	4.3	5.4	—	—	18.5
Oberoi Realty	194	BUY	63,726	1,074	328	14.5	23.2	25.1	9.2	59.6	8.3	13.4	8.4	7.7	9.1	5.4	4.2	1.5	1.3	1.1	1.0	1.0	1.0	12.1	16.8	15.6	290	49.4	0.5
Prestige Estates Projects	128	ADD	44,958	757	350	8.2	13.1	17.1	224.5	60.9	30.1	15.7	9.8	7.5	11.0	7.0	5.8	1.6	1.4	1.2	—	—	—	11.7	15.6	17.4	200	55.7	0.7
Sobha Developers	321	BUY	31,513	531	98	22.1	23.2	36.5	5.4	4.7	57.5	14.5	13.9	8.8	8.1	8.1	6.0	1.5	1.4	1.2	2.2	1.6	1.6	10.5	10.2	14.6	500	55.6	0.8
Sunteck Realty	384	BUY	23,054	388	60	0.7	76.5	25.4	29.1	11,307	(66.8)	573.0	5.0	15.1	511.2	3.7	7.1	4.7	2.5	2.1	—	0.5	0.5	0.7	64.3	15.2	560	45.7	0.2
Real Estate		**Cautious**	**521,679**	**8,790**					**(34.8)**	**91.0**	**45.7**	**28.5**	**14.9**	**10.3**	**15.6**	**10.4**	**7.8**	**1.1**	**1.0**	**0.9**	**1.0**	**1.0**	**1.0**	**3.7**	**6.5**	**8.8**			

Source: Company, Bloomberg, Kotak Institutional Equities estimates

Kotak Institutional Equities: Valuation summary of KIE Universe stocks

	19-Jul-13		Mkt cap.		O/S shares	EPS (Rs)			EPS growth (%)			PER (X)			EV/EBITDA (X)			Price/BV (X)			Dividend yield (%)			RoE (%)			Target price	Upside	ADVT-3mo
Company	Price (Rs)	Rating	(Rs mn)	(US$ mn)	(mn)	2013	2014E	2015E	2013	2014E	2015E	2013	2014E	2015E	2013	2014E	2015E	2013	2014E	2015E	2013	2014E	2015E	2013	2014E	2015E	(Rs)	(%)	(US$ mn)
Technology																													
HCL Technologies	892	REDUCE	634,390	10,689	711	54.3	57.8	61.9	57.0	6.5	7.2	16.4	15.4	14.4	10.7	9.8	8.8	4.6	3.7	3.1	0.9	1.1	1.3	31.7	26.1	23.4	675	(24.3)	17.3
Hexaware Technologies	107	REDUCE	31,331	528	293	11.2	12.7	12.7	22.8	14.0	(0.6)	9.6	8.4	8.4	7.2	5.5	5.4	2.6	2.3	2.1	5.6	6.0	5.9	29.5	29.1	25.9	110	3.0	3.4
Infosys	2,847	ADD	1,627,033	27,414	571	164.9	172.2	195.7	13.3	4.5	13.7	17.3	16.5	14.5	12.2	11.0	9.2	4.3	3.7	3.2	1.7	2.2	2.4	27.2	24.1	23.8	3,050	7.1	48.4
Mahindra Satyam	115	ADD	135,416	2,282	1,176	11.3	11.3	12.2	10.7	0.5	7.4	10.2	10.2	9.5	6.5	6.0	5.0	3.3	2.6	2.2	0.5	2.0	2.1	37.5	28.9	25.3	130	12.9	8.6
Mindtree	945	ADD	39,696	669	42	81.7	99.5	108.1	53.2	21.8	8.7	11.6	9.5	8.7	8.0	6.9	5.8	3.0	2.4	2.0	1.3	1.6	1.7	29.8	28.1	24.6	1,050	11.1	0.6
Mphasis	407	SELL	85,817	1,446	211	37.6	35.7	35.9	(3.7)	(5.0)	0.6	10.8	11.4	11.3	8.1	8.6	8.2	1.9	1.8	1.7	4.2	4.4	4.4	19.1	16.5	15.5	360	(11.6)	1.3
Polaris Financial Technology	118	REDUCE	11,735	198	100	20.0	17.2	17.2	(3.8)	(13.9)	(0.0)	5.9	6.8	6.8	3.0	3.0	2.7	0.9	0.8	0.7	3.5	3.7	3.8	15.3	12.2	11.2	110	(6.5)	2.2
TCS	1,743	ADD	3,411,008	57,473	1,957	71.2	87.3	97.5	31.1	22.6	11.6	24.5	20.0	17.9	18.3	14.2	12.5	8.3	6.8	5.7	1.3	2.0	2.2	37.9	37.5	34.5	1,800	3.3	37.0
Tech Mahindra	1,132	ADD	145,048	2,444	128	98.3	111.3	110.0	17.6	13.3	(1.2)	11.5	10.2	10.3	10.7	9.5	9.7	2.7	2.3	2.1	0.4	0.7	0.9	27.2	25.0	21.9	1,100	(2.9)	12.6
Wipro	391	REDUCE	964,018	16,243	2,463	24.9	27.3	29.7	9.9	9.6	8.8	15.7	14.3	13.2	10.8	9.4	8.3	3.4	2.9	2.5	1.8	2.0	2.3	21.6	21.9	20.6	365	(6.7)	10.5
Technology		**Cautious**	**7,085,492**	**119,385**					**22.2**	**12.4**	**10.3**	**18.8**	**16.8**	**15.2**	**13.6**	**11.6**	**10.2**	**5.1**	**4.3**	**3.7**	**1.4**	**2.0**	**2.2**	**27.1**	**25.6**	**24.2**			
Telecom																													
Bharti Airtel	330	ADD	1,252,638	21,106	3,798	6.0	11.9	17.5	(46.6)	99.1	46.4	55.0	27.7	18.9	7.9	6.8	5.6	2.5	2.3	2.1	0.3	0.4	1.1	4.5	8.7	11.7	350	6.1	22.5
Bharti Infratel	155	ADD	292,577	4,930	1,889	5.3	7.0	7.9	23.3	31.5	12.8	29.2	22.2	19.7	8.4	7.6	6.8	1.7	1.6	1.6	2.5	1.8	2.2	6.3	7.5	8.1	170	9.8	—
IDEA	151	BUY	497,147	8,377	3,303	3.1	6.1	9.5	39.8	100.6	55.5	49.2	24.5	15.8	10.5	7.8	6.1	3.5	3.1	2.6	—	—	0.5	7.4	13.3	17.9	180	19.6	12.5
Reliance Communications	145	SELL	300,002	5,055	2,064	3.3	9.3	8.6	(27.5)	186.7	(8.3)	44.6	15.6	17.0	10.4	7.6	7.5	1.0	1.0	0.9	—	—	—	0.4	6.5	5.6	65	(55.3)	61.5
Tata Communications	165	REDUCE	47,011	792	285	(29.4)	(9.8)	(1.6)	(5.5)	66.6	83.7	(5.6)	(16.8)	(103.0)	7.8	7.0	6.3	2.9	3.5	3.6	—	—	—	(42.6)	(18.8)	(3.5)	220	33.4	1.4
Telecom		**Neutral**	**2,389,375**	**40,259**					**(39.1)**	**166.5**	**36.4**	**66.9**	**25.1**	**18.4**	**8.7**	**7.2**	**6.1**	**2.1**	**2.0**	**1.8**	**0.5**	**0.5**	**0.9**	**3.2**	**7.9**	**9.9**			
Utilities																													
Adani Power	40	SELL	94,654	1,595	2,393	(9.0)	(1.9)	5.3	(2,023.1)	79.2	380.9	(4.4)	(21.1)	7.5	44.9	10.1	6.8	2.2	2.5	1.9	—	—	—	(41.7)	(11.0)	28.2	35	(11.5)	3.8
CESC	336	REDUCE	41,985	707	125	34.3	38.4	38.1	57.6	11.9	(0.5)	9.8	8.8	8.8	10.7	8.9	7.9	0.6	0.6	0.6	2.1	2.2	2.2	6.7	6.9	6.5	324	(3.6)	1.8
JSW Energy	43	ADD	70,192	1,183	1,640	6.7	6.9	6.3	232.1	3.2	(8.8)	6.4	6.2	6.8	6.1	4.9	4.7	1.1	1.0	0.8	—	—	—	18.5	16.8	13.2	50	16.8	2.2
Lanco Infratech	7	RS	15,005	253	2,223	(4.7)	(6.0)	4.5	(790.4)	(28.6)	174.6	(1.4)	(1.1)	1.5	14.8	13.5	5.9	0.4	0.6	0.4	—	—	—	(24.2)	(41.9)	33.3	—	—	1.1
NHPC	18	ADD	220,183	3,710	12,301	1.9	2.0	2.3	(22.4)	6.1	11.7	9.3	8.7	7.8	9.6	8.4	6.3	0.7	0.7	0.6	2.9	3.1	3.5	7.9	7.8	8.2	26	45.3	1.5
NTPC	144	ADD	1,184,873	19,964	8,245	13.0	13.3	14.2	20.8	2.3	6.3	11.0	10.8	10.1	10.0	8.6	8.0	1.5	1.4	1.2	4.7	2.8	3.0	14.0	13.1	12.8	175	21.8	12.0
Power Grid	111	BUY	515,520	8,686	4,630	9.1	10.7	12.8	28.7	17.3	19.9	12.2	10.4	8.7	10.9	8.6	7.3	2.0	1.8	1.6	2.5	2.9	3.5	16.9	17.7	18.9	140	25.7	5.5
Reliance Infrastructure	388	BUY	102,082	1,720	263	70.9	68.1	74.7	17.5	(4.0)	9.8	5.5	5.7	5.2	9.3	6.7	7.2	0.4	0.4	0.3	1.9	2.9	2.9	11.0	11.2	9.3	810	108.7	25.1
Reliance Power	80	SELL	224,270	3,779	2,805	3.6	3.7	3.9	16.7	2.4	5.1	22.2	21.7	20.6	25.9	20.0	13.4	1.2	1.1	1.1	—	—	—	5.6	5.4	5.4	75	(6.2)	15.1
Tata Power	93	BUY	228,322	3,847	2,468	4.0	5.7	6.3	(12.9)	43.0	10.2	23.1	16.1	14.6	9.3	7.7	7.0	1.7	1.6	1.5	1.2	1.3	1.3	7.4	10.2	10.4	104	12.4	4.3
Utilities		**Attractive**	**2,697,086**	**45,444**					**1.7**	**15.3**	**27.9**	**13.8**	**12.0**	**9.4**	**11.4**	**9.1**	**7.5**	**1.2**	**1.2**	**1.1**	**3.0**	**2.3**	**2.5**	**9.0**	**9.7**	**11.4**			
Others																													
Carborundum Universal	112	BUY	21,007	354	187	5.7	9.6	13.7	(50.7)	67.5	43.4	19.6	11.7	8.2	9.8	6.4	4.7	1.8	1.6	1.4	0.9	1.5	2.1	10.3	15.7	19.1	180	60.6	0.1
Coromandel International	179	SELL	50,594	852	283	18.1	18.1	20.4	(19.7)	0.0	12.4	9.9	9.9	8.8	8.7	6.7	6.2	1.9	1.7	1.5	4.1	4.3	4.3	18.8	16.9	17.3	150	(16.2)	0.3
Havells India	781	REDUCE	97,424	1,642	125	33.4	38.6	42.9	6.0	15.8	11.0	23.4	20.2	18.2	15.2	12.3	11.1	6.5	5.2	4.3	1.0	1.0	1.1	33.3	28.8	25.9	625	(20.0)	5.8
Jaiprakash Associates	50	BUY	108,656	1,831	2,191	2.0	9.6	17.1	(32.1)	383.4	78.3	25.0	5.2	2.9	8.7	6.4	4.7	0.9	0.8	0.6	—	—	—	3.7	16.0	23.7	100	101.6	28.0
Jet Airways	371	SELL	42,115	710	114	1.2	91.5	45.4	100.6	7,639	(50.4)	313.5	4.1	8.2	9.9	6.8	6.2	29.8	1.3	1.1	—	—	—	7.5	61.5	14.7	550	48.3	24.1
MCX India	739	ADD	37,534	632	51	58.1	44.3	49.9	(2.4)	(24)	12.7	12.7	16.7	14.8	7.3	11.0	8.5	3.3	3.0	2.8	3.3	3.3	3.3	27.4	18.9	19.7	990	33.9	1.8
Rallis India	152	BUY	29,560	498	194	6.1	8.5	10.2	20.0	38	20.6	24.8	18.0	14.9	14.4	10.6	9.1	4.8	4.0	3.3	1.5	1.4	1.4	18.9	24.0	24.6	165	8.6	0.6
SpiceJet	28	BUY	13,442	226	484	0.4	3.5	5.1	103.2	679.1	47.5	62.6	8.0	5.4	18.3	5.8	3.8	(41.8)	10.0	3.5	—	—	—	(23)	325.1	95.5	60	116.2	1.9
Tata Chemicals	285	BUY	72,547	1,222	255	33.6	37.7	40.7	2.2	12.2	8.0	8.5	7.6	7.0	5.3	4.6	4.1	0.9	0.8	0.8	3.5	3.5	3.5	11.1	11.2	10.9	370	30.0	1.9
United Phosphorus	147	REDUCE	65,151	1,098	443	17.5	18.3	19.1	39.4	4.4	4.8	8.4	8.1	7.7	4.9	4.9	4.4	1.4	1.2	1.1	1.7	1.7	1.7	18.0	16.6	15.2	135	(8.3)	5.7
Others			**538,030**	**9,065**					**142.0**	**87.2**	**23.7**	**15.2**	**8.1**	**6.5**	**8.3**	**6.4**	**5.2**	**1.7**	**1.4**	**1.2**	**1.6**	**1.6**	**1.7**	**11.1**	**16.8**	**17.6**			
KIE universe			**53,014,565**	**893,253**					**6.7**	**11.7**	**14.1**	**14.8**	**13.2**	**11.6**	**10.0**	**8.6**	**7.4**	**2.2**	**2.0**	**1.8**	**1.8**	**2.0**	**2.2**	**15.1**	**15.1**	**15.3**			
KIE universe ex-energy			**45,074,398**	**759,468**					**8.4**	**12.8**	**15.4**	**16.0**	**14.2**	**12.3**	**11.3**	**9.7**	**8.3**	**2.5**	**2.2**	**2.0**	**1.7**	**1.8**	**2.1**	**15.8**	**15.8**	**16.2**			
KIE universe ex-energy & ex-commodities			**39,576,769**	**666,837**					**10.0**	**15.4**	**16.3**	**17.6**	**15.2**	**13.1**	**12.9**	**10.8**	**9.2**	**2.8**	**2.4**	**2.2**	**1.5**	**1.6**	**1.9**	**15.7**	**16.1**	**16.5**			

Notes:

(a) For banks we have used adjusted book values.

(b) 2012 means calendar year 2011, similarly for 2013 and 2014 for these particular companies.

(c) EV/Sales & EV/EBITDA for KS universe excludes Banking Sector.

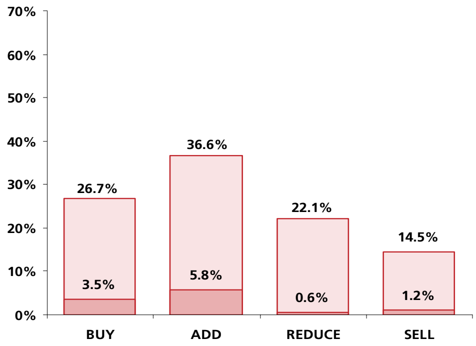
(d) Rupee-US Dollar exchange rate (Rs/US$)= 59.35

Source: Company, Bloomberg, 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: Sanjeev Prasad, Kawaljeet Saluja, Rohit Chordia, Hitesh Goel, M.B. Mahesh, Nischint Chawathe, Jasdeep Walia."

Kotak Institutional Equities Research coverage universe

Distribution of ratings/investment banking relationships



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 deliver more than 15% returns over the next 12 months; Add = We expect this stock to deliver 5-15% returns over the next 12 months; Reduce = We expect this stock to deliver -5-+5% returns over the next 12 months; Sell = We expect this stock to deliver less than -5% returns over the next 12 months. Our target prices are also on a 12-month horizon basis. These ratings are used illustratively to comply with applicable regulations. As of 30/06/2013 Kotak Institutional Equities Investment Research had investment ratings on 172 equity securities.

Source: Kotak Institutional Equities — As of June 30, 2013

Ratings and other definitions/identifiers

Definitions of ratings

BUY. We expect this stock to deliver more than 15% returns over the next 12 months.

ADD. We expect this stock to deliver 5-15% returns over the next 12 months.

REDUCE. We expect this stock to deliver -5-+5% returns over the next 12 months.

SELL. We expect this stock to deliver <-5% returns over the next 12 months.

Our target prices are also on a 12-month horizon basis.

Other definitions

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