PPFAS

Looking Forward

Investment Ideas for 2007

Looking forward...

There was considerable debate at our end before publishing the book which you are currently holding. The past year has been a remarkable one for the Indian stock markets with many stocks displaying superlative returns. Many of the ideas contained in our February 2006 publication titled “Investment Ideas 2006” also did well. However, we believed that 2007 would find it difficult to follow in the footsteps of 2006 primarily because global and local factors were loaded against it. Consequently fresh investment ideas were becoming increasingly difficult to unearth, especially considering that we as a firm bend more towards the “Value” side of investing.

Finally, we thought that this year we would combine a few new ideas with updates on many existing ones which still merit consideration. Hence, it is through deliberate design, rather than coincidence, that this book appears more as “Performance Review 2006” rather than “Investment Ideas 2007”.

Like the previous book, this one too contains large-cap as well as mid-cap ideas, and hence will appeal to a cross-section of investors. Defensive scrips such as BEL and Britannia rub shoulders with consumer discretionary/cyclicals such as TELCO, Ashok Leyland & Maruti and power sector related companies such as KEC International and Jyoti Structures. Our positive view on the banking sector is reflected in our coverage of stocks such as State Bank of India, Punjab National Bank and Indian Overseas Bank. As always, we have a take on some upcoming companies such as Kitex Garments (a micro-cap, if there ever was one), Centurion Bank of Punjab and SEAMAC, coupled with continuing coverage on VST Industries, Matrix Labs, Bombay Rayon, Infosys Technologies, Sonata Software, NIIT Technologies, Mphasis BFL.

You may have noticed that many of the companies mentioned above have had a lukewarm 2006. That has actually increased our comfort level regarding them. Companies and sectors which are fundamentally sound but temporarily ignored for varied reasons are the ones which we like. We hope that you will like them too....

Index...

Investment Research

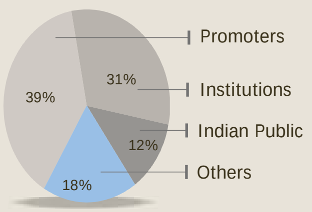
Ashok Leyland Limited

BUY | CMP Rs. 45.0

Stock Codes

Bloomberg	: AL.IN
Reuters	: ASOK.BO
BSE Code	: 500477
NSE Code	: ASHOKLEY
BSE Group	: A

Share Holdings
(as on 31st Dec. 06)



Stock Data

Benchmark	: BSE 100
52 W High Rs.	: 53.95
52 W Low Rs.	: 30.30
Mkt Cap in Mn.	: 59548.0
Face Value	: Rs. 1.0

Absolute Return

%	1m	3m	6m
Ashok	-10.50	-6.67	-6.33
BSE 100	-13.18	-12.16	-9.99

Price Comparison

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- Ashok Leyland Limited reported impressive top line growth of 48% on Y-o-Y basis on the back of strong volume growth especially in domestic M&H CV Goods segment. Over all volume grew by 54% on Y-o-Y basis and 38% on YTD basis. The company for the first time recorded the highest sales for the quarter of 20,051 units. The company has target to sale around 25,000 units for its fourth quarter. The ban of supreme court on overloading, ongoing infrastructure development and firm freight rates were the main reasons behind such strong volume growth.

- The company successfully increased its market share in M&H CV Domestic Goods segment to 26% from 23% on YTD basis. However, this was at the expense of its position in M&H CV Passenger segment where its market share declined to 39% from 53% on YTD basis. The reason for such decline was shift in focus from Passenger segment to Goods segment as later witnessed tremendous demand.

- The company's net sales recorded growth of 48% on Y-o-Y basis and growth of 39% on YTD basis on account of strong volume growth. Though realization saw decline during quarter on account of defense sales.

- The company witnessed increase in EBDITA margins from 9.87% to 10.71% on Y-o-Y basis. This is commendable, especially considering that other companies across sector are striving hard to maintain their operating margins. Total expenditure increased by 47% on Y-o-Y basis and 39% on YTD basis. The raw material expenses as a percentage of sales increased to 74% compared to 71% last year for the same period. This is in line with what its peers faced. The company was successful in reducing their staff cost and other expenditure. The Staff cost reduced from 8.34% last year to 6% as a percentage of sales. The company had implemented VRS plan last year and same is being reflected in lower staff costs this quarter. The other expenditure as a percentage of sales reduced to 8.7% from 11.34% last year. The other income saw increase of 158% on Y-o-Y basis.

Particulars (Rs Mn)	2004	2005	2006	2007A	2008E	2009E
Net Sales	33920.19	41823.78	52476.57	65029.12	76076.56	88975.35
EBDITA	4132.24	4766.05	5730.44	6375.68	7846.97	9136.85
EBDITA margins (%)	12.18	11.40	10.92	9.80	10.31	10.27
PAT	1935.80	2714.10	3273.20	3450.68	4542.58	5380.32
EPS (Rs)	1.63	2.28	2.68	2.59	3.41	4.04
P/E (x)	27.65	19.72	16.79	17.36	13.19	11.14
EV/EBDITA (x)	13.37	11.40	9.75	8.91	6.74	5.27
MCAP/SALES (x)	1.58	1.28	1.05	0.92	0.79	0.67
ROCE (%)	24.33	21.67	25.17	25.11	25.65	24.94
RONW (%)	18.99	23.63	23.29	15.74	17.17	16.90

- The PAT increased 93.11% on Y-o-Y basis and 39.15% on YTD basis. The PAT margin improved from 4.54% last year to 5.92 % on Y-o-Y basis. Apart from successful increase in operating margins, reduction in interest costs and benign increase in depreciation helped the company to witness growth in PAT margins. The interest expenses declined by 68% on Y-o-Y basis on account of stringent control over working capital. The depreciation increased by merely 14 % on Y-o-Y basis.

Strong volume growth lead by domestic M&H CV Goods segment

The company reported impressive top line growth of 48% on Y-o-Y basis on the back of strong volume growth especially in domestic M&H CV Goods segment. Over all volume grew by 54% on Y-o-Y basis and 38% on YTD basis. The M&H CV segment grew by 63% on Y-o-Y basis and 42% on YTD basis. The domestic M&H CV Goods segment reported growth of 92% on Y-o-Y basis and 66% on YTD basis. The growth in Goods segment is spurred by the ban of supreme court on overloading, ongoing infrastructure development and firm freight rates.

The company has expertise in heavy multi-axle vehicles. Due to the heavy demand from the Goods segment, the company concentrated its production more towards this segment, leading to mere 5% Y-o-Y growth in domestic Passenger vehicle sales. The demand for Passenger segment mainly arises from STU orders, where there is some flexibility in delivery schedules. However, the exports of M&H CV Passenger segment grew by 46% on Y-o-Y basis where as it declined for Goods segment by 46% on Y-o-Y basis. Overall Exports recorded growth of mere 1% on Y-o-Y basis. The reason for the same appears to be supply constraint than demand. Total export is 4280 units YTD with target to reach 6,000 units by the year end.

The company is currently executing an order from the Indian Army for 872 water bowsers and spares worth over Rs 230 crs. It has supplied 350 units till date and has an order book of around 600 units to be deliver before March 2007 for defense segments.

ALL Sales Break Up

Particulars	Q3FY07	Q3FY06	% Change	9MFY07	9MFY06	% Change
M&H CV Passenger						
Domestic	3,385	3,477	(2.6)	7,682	10,027	(23.4)
Exports	1,067	726	47.0	2,721	1,606	69.4
Total	4,452	4,203	5.9	10,403	11,633	(10.6)
M&H CV Goods						
Domestic	15,160	7,900	91.9	44,739	26,955	66.0
Exports	369	691	(46.6)	1,556	2,069	(24.8)
Total	15,529	8,591	80.8	46,295	29,024	59.5
Total M&H CV						
Domestic	18,545	11,377	63.0	52,421	36,982	41.7
Exports	1,436	1,417	1.3	4,277	3,675	16.4
LCVs						
Domestic	69	244	(71.7)	253	572	(55.8)
Exports	1	-	-	3	24	(87.5)
Domestic	18,614	11,621	60.2	52,674	37,554	40.3
Exports	1,437	1,417	1.4	4,280	3,699	15.7
Total Sales	20,051	13,038	53.8	56,954	41,253	38.1

New facilities and launches

ALL has announced its plan to setup a vehicle manufacturing unit in Uttaranchal with an investment of Rs 1,200cr. The company will set up a vehicle assembly and cab facility to produce 25,000 vehicles annually initially which will be stepped to 40,000 vehicles eventually. This unit will strengthen ALL's presence in Northern India which already contributes nearly a quarter of their sales. The investments will enjoy excise duty and income tax exemption for five/ten years. It plans to complete Uttranchal expansion by 2010.

Also, ALL's Ennore unit will manufacture 50,000 more engines by May 2007 and equal number of gear boxes by the end of May 2008 in addition to the 85,000 existing ones. The company targets to expand its vehicle capacities to 2,00,000 units and engine capacities to 1,20,000 units within next 3 years.

The company plans 'Intercentury Luxura' bus with a globally acclaimed, powerful 260 PS, 8-litre J engine that meets BS2 emission by the end of March 2007.

New Subsidiary

Ashok Leyland has established a subsidiary company in Ras Al Khaimah, UAE for setting up a bus body assembly plant to cater to the Gulf Cooperation Council (GCC) and neighboring markets. The unit, with an initial annual capacity for 1,000 buses of international styling, manufacture and quality, will start operations as a bus body assembly using ALL chassis and bus body CKD kits sent from India (including Irizar TVS). The facility, to be built with an initial investment of US$ 5 million, will include a state-of-the-art paint plant for bus bodies. The unit will be managed and operated by ALL. The unit will be provided an Industrial License that will enable duty free import of vehicle kits and duty free export of finished vehicles to GCC and the Middle East. ALL enjoys a market share in excess of 60% in Dubai's standard bus market, with exports to the region set to cross 1,500 vehicles per annum.

AVIA started operation

In October 2006, the Company's wholly owned foreign subsidiary completed the acquisition of truck business unit of AVIA in Czech Republic in pursuance of the framework agreement signed earlier in July 2006. AVIA is part of ALL's inorganic growth plan and is a significant step in securing a beachhead in the European Union and the Eastern European markets. The acquisition will also give the company a modern, international vehicle for their light and medium commercial vehicle range of trucks for India and other export markets. The strategic location of AVIA also opens up possibilities of using its facilities as an assembly and marketing base for some of ALL's future products on the anvil. The subsidiary has begun its business operations post acquisition in Q3FY07 with production of around 200 units out of this facility.

Valuation

At present the stock is trading at 11 x EPS FY09E, 0.67 x M Cap / Sales FY09E and 1.88 x P/B FY09E.

Despite the below mentioned risk factors these, taking into account several positives such as expected rise in demand of CV with rising GDP, overall boost to highway projects, continuing effect of ban on overloading, rising export opportunities, expected growth in bus segment and expansion of 'E-comet' and 'Newgen' range apart from new launches like 'Intercentury Luxura', we estimate that ALL will witness topline growth of CAGR 17% over 2007-09. The story becomes stronger with Management plans to enter into the LCV business by acquiring businesses abroad. The company is also looking for acquisition in the areas of component, foundry and engineering services business abroad.

We maintain 'BUY'.

Risk Factors

We envisage the following risk factors:

- ALL's product profile is loaded with mainly M&H CVs which makes it vulnerable to cyclical trends in CV industry
- Fuel accounts for more than 50% of operating cost of truck operators. Any rise in oil prices poses a key threat to operator's profitability and thus CV demand.
- Rising interest rate is a cause of concern as sales through financing accounts for 90% of trucks sold.
- Any increase in commodity prices will reduce operating margins.
- Increasing competition from new players like MAN, International Truck and M&M pose a risk to the company's market share

Quarterly Financials

Particulars (Rs Mn)	Q3FY07	Q3FY06	% Chng	9MFY07	9MFY06	% Chng
Gross Sales	20,699.8	13,774.8	50.3	56,399.8	40,497.3	39.3
Less: Excise Duty	2,923.9	1,763.0	65.8	7,627.9	5,368.8	42.1
Net Sales	17,775.9	12,011.8	48.0	48,771.8	35,128.5	38.8
Expenditure						
Raw Material Cost	13,225.6	8,486.3	55.8	36,332.1	24,852.1	46.2
Staff Cost	1,149.0	1,002.0	14.7	3,643.8	3,223.3	13.0
Other Expense	1,560.8	1,362.5	14.5	4,418.4	3,839.2	15.1
Total Expenditure	15,935.4	10,850.8	46.9	44,394.3	31,914.6	39.1
Operating Profit	1,840.5	1,161.0	58.5	4,377.5	3,213.9	36.2
OPM%	10.4	9.7		9.0	9.1	
Other Income	63.5	24.6	157.8	539.0	244.4	120.5
PBDIT	1,904.1	1,185.6	60.6	4,916.5	3,458.3	42.2
PBDIT Margin (%)	10.7	9.9		10.1	9.8	
Interest	25.7	79.3	(67.7)	34.5	91.4	(62.2)
PBDT	1,878.4	1,106.3	69.8	4,882.0	3,366.9	45.0
Depreciation	332.3	290.2	14.5	1,024.5	929.8	10.2
PBT	1,546.1	816.2	89.4	3,857.5	2,437.1	58.3
PBT Margin (%)	8.7	6.8		7.9	6.9	
Exceptional Items	31.1	20.8		100.3	(238.0)	
Tax	462.5	250.3	84.8	1,059.5	736.5	43.9
PAT	1,052.6	545.0	93.1	2,697.7	1,938.6	39.2
PAT Margin (%)	5.9	4.5		5.5	5.5	
Equity Capital	1,323.3	1,189.3		1,323.3	1,189.3	
EPS Diluted (Rs.)	0.8	0.5		2.1	1.5	

Financials

P & L Ac (Rs Mn)	2006	2007E	2008E	2009E
Net Sales	52,476.6	65,029.1	76,076.6	88,975.3
Material Cost	37,690.0	48,442.8	55,535.9	64,952.0
Empl Cost	4,038.9	4,858.3	6,086.1	7,118.0
Others	5,347.0	5,891.2	6,846.9	8,007.8
Total Mfg Cost	47,075.9	59,192.4	68,468.9	80,077.8
Operating Profit	5,400.7	5,836.7	7,607.7	8,897.5
Other Income	329.7	539.0	239.3	239.3
PBDIT	5,730.4	6,375.7	7,847.0	9,136.9
Interest	164.5	46.0	89.5	136.0
PBDT	5,565.9	6,329.6	7,757.5	9,000.8
Depreciation	1,260.1	1,366.0	1,448.3	1,528.1
PBT	4,305.9	4,963.7	6,309.1	7,472.7
Exceptional Items	217.2	100.3	-	-
Tax	1,249.8	1,412.7	1,766.6	2,092.3
PAT	3,273.2	3,450.7	4,542.6	5,380.3

RATIOS	2006	2007E	2008E	2009E
PBDIT %	10.92	9.80	10.31	10.27
PBT %	8.21	7.63	8.29	8.40
NPM %	6.24	5.31	5.97	6.05
Interest Cover	27.17	108.81	71.50	55.93
RONW %	23.29	15.74	17.17	16.90
ROCE %	25.17	25.11	25.65	24.94
Inv Days	62.78	54.75	54.75	54.75
Debtor Days	25.59	31.56	31.57	31.57
Debt/Equity	0.49	0.16	0.16	0.15
Creditor Days	105.34	102.89	105.00	105.00
EPS	2.68	2.59	3.41	4.04
P/E	16.79	17.36	13.19	11.14
Price/BV	3.91	2.73	2.26	1.88
BV	11.50	16.46	19.87	23.91
M CAP (Rs Mn)	54971.55	59919.75	59919.75	59919.75
MCAP/Sales	1.05	0.92	0.79	0.67
EV (Rs Mn)	55862.07	56790.45	52857.55	48129.11
EV/EBDITA (x)	9.75	8.91	6.74	5.27
EV/Sales (x)	1.06	0.87	0.69	0.54

Balance Sheet (Rs Mn)	2006	2007E	2008E	2009E
Equity	1,221.6	1,331.6	1,331.6	1,331.6
Reserves	12,902.9	20,585.9	25,128.4	30,508.8
Misc Exp Etc	73.1	-	-	-
Actual Reserves	12,829.9	20,585.9	25,128.4	30,508.8
Net Worth	14,051.5	21,917.4	26,460.0	31,840.3
Total Debt	6,919.3	3,470.5	4,135.5	4,800.5
Def. Tax Liability (net)	1,796.9	-	-	-
Total Liabilities	22,767.6	25,387.9	30,595.5	36,640.8
Gross Block	21,385.0	22,799.2	24,139.2	25,469.2
Acc Depreciation	11,952.3	13,318.3	14,766.6	16,294.8
Net Block	9,432.7	9,480.9	9,372.6	9,174.4
CWIP	1,414.2	1,340.0	1,330.0	1,330.0
Fixed Assets	10,846.9	10,820.9	10,702.6	10,504.4
Investments	3,681.8	3,681.8	3,681.8	3,681.8
Working Capital				
Inventories	9,025.6	9,754.4	11,411.5	13,346.3
Debtors	4,243.4	6,502.9	7,607.7	8,897.5
Cash/bank	6,028.8	6,599.8	11,197.7	16,591.2
Loans & Advances	3,026.4	4,552.0	5,325.4	6,228.3
Current Assets	22,324.1	27,409.2	35,542.2	45,063.3
Liabilities	11,469.0	13,656.1	15,976.1	18,684.8
Provisions	2,616.2	2,867.8	3,355.0	3,923.8
Current Liabilities	14,085.2	16,523.9	19,331.1	22,608.6
Net Working Capital	8,239.0	10,885.3	16,211.2	22,454.7
Total Assets	22,767.6	25,387.9	30,595.5	36,640.8

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PPFAS

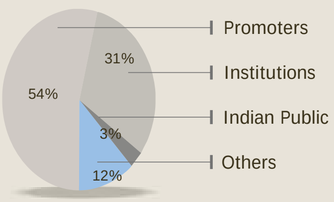
Maruti Udyog Limited

ACCUMULATE | CMP Rs. 795.0

Stock Codes

Bloomberg	: MUL.IN
Reuters	: MRTI.BO
BSE Code	: 532500
NSE Code	: MARUTI
BSE Group	: A

Share Holdings
(as on 31st Dec. 06)



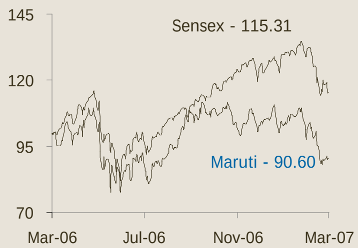
Stock Data

Benchmark	: Sensex
52 W High Rs.	: 991.0
52 W Low Rs.	: 670.0
Mkt Cap in Mn.	: 229,755.0
Face Value	: Rs. 10.0

Absolute Return

%	1m	3m	6m
Maruti	-7.01	-11.94	-16.01
Sensex	-10.46	-7.80	4.45

Price Comparison



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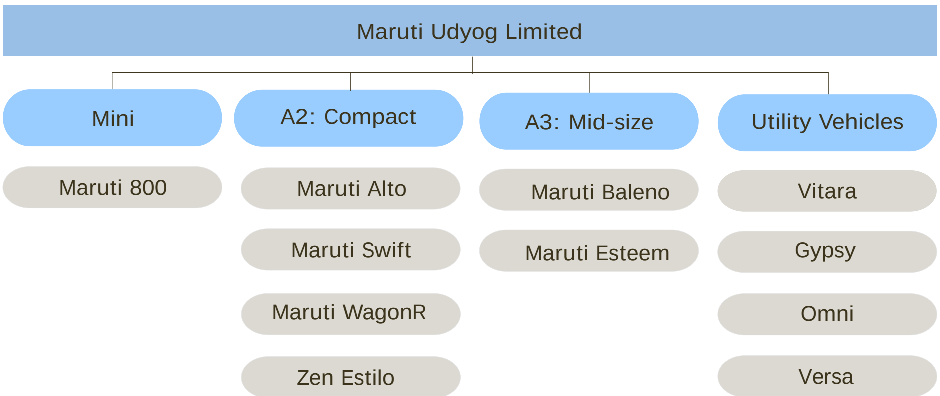
Maruti Udyog Limited (MUL) was established in Feb 1981 through an Act of Parliament, to meet the growing demand of a personal mode of transport caused by the lack of an efficient public transport system. Joint venture with Suzuki Motor company was entered in October 1982 in order to bring to MUL contemporary technology and Japanese management practices. At present, MUL is market leader in the compact car segment with 58% market share. MUL has sales network of 307 state-of-the-art showrooms across 189 cities with over 6000 trained personnel. MUL is known for its lowest cost of operation/ km for its petrol cars. MUL's top five models are Maruti 800, Alto, Zen, Omni and WagonR.



Quarterly Performance :

- Maruti Udyog Limited (MUL) maintained its leadership position in the passenger car segment by posting impressive results for the quarter ended 31st December 2006. This performance was on the back of growth in sales, better operational efficiency and positive macro-economic environment. The company has maintained its market leadership in the compact car segment with 58% market share.

(Rs.Mn) Mar -End	2004	2005	2006	2007E	2008E	2009E
Net Sales	90,812.00	109,108.00	120,034.20	135,717.33	168,486.43	225,513.53
EBDITA	13,805.00	18,140.00	20,558.00	24,437.47	26,335.93	34,322.70
EBDITA margins(%)	15.20	16.63	17.13	18.01	15.63	15.22
PAT	5,421.00	8,536.00	11,890.50	14,845.60	15,246.13	19,371.53
EPS	18.76	29.54	41.14	51.37	52.75	67.03
P/E	42.38	26.92	19.32	15.48	15.07	11.86
EV/EBDITA	16.69	12.27	10.53	8.87	8.54	6.71
MCAP/SALES	2.53	2.11	1.91	1.69	1.36	1.02
ROCE(%)	33.92	37.82	36.70	35.02	30.05	31.20
RONW(%)	15.16	19.49	21.81	21.40	18.02	18.63

- The company reported spectacular growth of 18% in its net sales on Y-o-Y basis on the back of strong volume growth of 18.7% on Y-o-Y basis. The growth in volumes were primarily driven by impressive performance of 30.2% growth in A2 segment which also constitutes around two third of overall volumes. The other income grew by around 26% on Y-o-Y basis.

- Total expenditure increased by around 20% on Y-o-Y basis. The company witnessed reduction in raw material as a percentage of sales from 76.31% last year same period to 75.49%. This is commendable especially when prices of key raw materials like steel and rubber reported steep increase in recent period and other automobile OEMs are facing significant pressure on these front. Employee cost as a percentage of sales has increased from 1.88% last year same period to 2%. Other expenses too witnessed increase as a percentage of sales from 7.1% last year same period to 9.1%. This was mainly due to higher royalty and promotional expenses for the launch of New Zen Estilo.

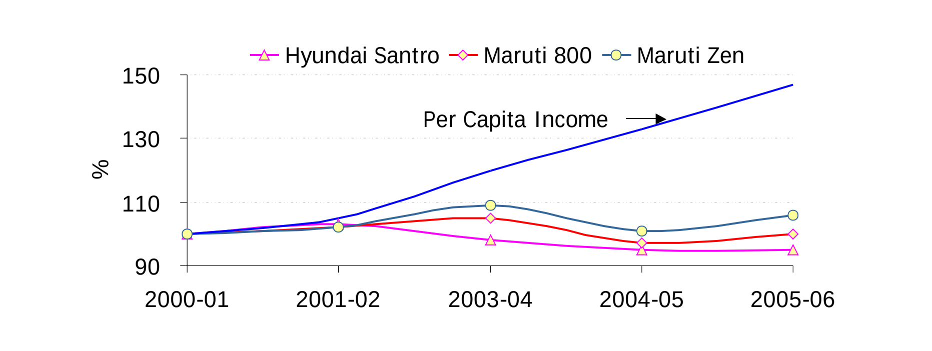
- The company reported decline in EBDIT margin from 18.44% to 17.35% on Y-o-Y basis. Prima Facie it seems that the company faced margin pressure. But this is not true as the company has arrived at PBT number after deducting the loss of Rs. 546.10 million of erstwhile subsidiary Maruti Suzuki Automobiles India Ltd(MSAIL) which is now merged with itself. If one adds back Rs.546 million, operating margins shows marginal improvement.

- Depreciation has increased by 11.5% on Y-o-Y basis. The company has huge capex plan for coming years. This will increase its depreciation expenses in coming years. Interest expenses has increased by more than 9 times although on a lower base. If we remove the merger effect, PAT margin has actually increased from 10.92% to 11.59% on Y-o-Y basis.

Rising consumerism, favorable demographics and abolition of excise duty on small cars to fuel growth

Demand for cars is mainly a function of economic growth, per- capita income, new model launches, price tags, availability and cost of finance, duties and taxes, road conditions and urban infrastructure. Volume growth will mainly come from younger generation. Income of younger generation is rising in the wake of growing opportunities in IT , BPO and KPO sectors. Also, rising middle class income, liberal salary hikes of government employees and massive car-finance availability will drive demand for passenger small cars more by aspiration than need in years to come. Abolition of special excise duty cut on small and compact passenger cars has resulted in reduction in final prices. All the above factors has contributed to change in consumers preference from motor bikes to small and compact passenger cars.

Price Movement of Cars vis-a-vis per capita income



We believe that with its strong focus on small and compact cars and market leadership, Maruti will benefit most from expansion of car markets due to low penetration, rising per capita income and aspirations, excise duty and custom duty cuts and construction of highways and flyovers across cities. This will help to boost passenger car demand by 15% CAGR till FY2006-2010.

Strong volume growth fuels the top line growth

The company reported spectacular growth of 18% in its net sales on Y-o-Y basis on the back of strong volume growth of 18.7% on Y-o-Y basis. The growth in volumes were primarily driven by impressive performance of 30.2% growth in A2 segment which also constitutes around two third of overall volumes. The A2 segment comprises of Alto, Wagon R, Zen and Swift. This growth got further boost by successful launch of Wagon R (LPG), New Zen Estilo and recently launched Swift (Diesel). The newly launched Zen Estilo and Swift (Diesel) is gaining popularity in urban markets. Also, The C segment which comprises of Omni and Versa reported good sales number witnessing a growth of 31.7% on Y-o-Y basis.

The segments that witnessed decline were A1, A3 and MUVs. The decline of 17.1% on Y-o-Y basis in A1 segment offering Maruti 800 has been cannibalized by the company's own offering in A2 segment Alto. The company witnessed decline of 13.13% on Y-o-Y basis in A3 segment and 50% on Y-o-Y basis in MUV segment is a matter of concern going forward. The exports grew by 15.1% on Y-o-Y basis. With expected new launches and well accepted recently launched models, we expect good performance by the company in A2 segment.

Domestic	Q3FY07	Q3FY06	% Chng	9MFY07	9MFY06	% Chng
A1	19,683.0	23,736.0	(17.1)	60,128.0	63,950.0	(6.0)
C	21,426.0	16,264.0	31.7	58,758.0	48,496.0	21.2
A2	114,461.0	87,917.0	30.2	305,658.0	242,421.0	26.1
A3	6,910.0	7,954.0	(13.1)	22,870.0	22,889.0	(0.1)
Total Passenger Cars	162,480.0	135,871.0	19.6	447,414.0	377,756.0	18.4
MUVs	628.0	1,256.0	(50.0)	2,316.0	3,007.0	(23.0)
Total Domestic	163,108.0	137,127.0	18.9	449,730.0	380,763.0	18.1
Exports	9,073.0	7,886.0	15.1	25,082.0	26,659.0	(5.9)
Grand Total	172,181.0	145,013.0	18.7	474,812.0	407,422.0	16.5

High Capex to meet strong demand

Suzuki Motor Corporation (SMC) and MUL have drawn up an investment plan of Rs 9000 crore in India up to 2010. This includes investment in the fourth car assembly plant, the diesel engine and transmission plant, launch of new models and upgradation of MUL's existing facilities in Gurgaon.

Out of Rs. 9000 crores, Rs. 4,000 crore would be spent on the Gurgaon plant to introduce, expand and automate new models and develop new engines. The remaining capex would be utilised to set up a new four wheeler manufacturing facility at Manesar for Nissan. The new plant will start with initial capacity of 1,00,000 units which will be scaled up to 3,00,000 units. Here MUL will manufacture 1,00,000 units of Swift and 2,00,000 units of new model of small car primarily for exports market which is expected to be launched by 2008-09. Out of this 2,00,000 units, MUL will export

1,00,000 units to Europe and sell another 50,000 units in domestic market. Another 50,000 units will be supplied to Nissan for exports. Thus the company is aggressively targeting export market which could be positive move with increase in competition in domestic market. The new assembly plant is also a key step forward in MUL's goal of achieving annual sales of 1 million cars in India by 2010.

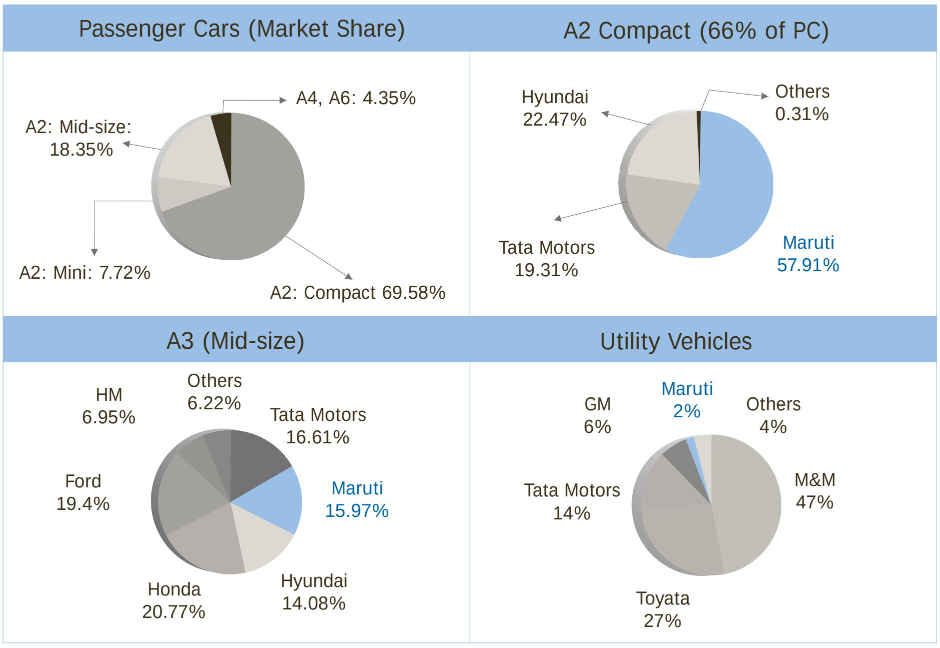
Entry into diesel market will boost top line

MUL has entered the diesel segment by launching the diesel version of Swift in January 2007. Swift Diesel is powered by a state-of-the-art, 1.3 litre, DDiS engine. Unlike conventional diesel engines, this engine is silent, clean, compact and powerful, while clearly offering superior fuel efficiency. This is the smallest 4-cylinder diesel engine for passenger cars in the world. Compactness of engine leads to superior performance and better fuel economy. It has been launched in two variants: Ldi and Vdi. The new model is priced aggressively.

The diesel Swift is expected to be a big boost for the company as it would be MUL's first serious attempt to cater to the fast growing diesel segment. The diesel segment constitutes about 25% of the total car market in India at present and it is likely to expand to 40% in next three years. With more complete range of products, Maruti would be able to attract customers and also hold on to existing customers in the entry and compact car segments. After Swift, Zen Estilo and Esteem are regarded as best models to enter in diesel markets followed by other models in compact segment.

Big threat from new entrants

Several players have announced plans to enter the small car segment, including Honda and Toyota. The entry of strong players like these, who have a strong brand equity and financial muscle might hurt existing players. The comfortable three player structure of the small car market might get shaken up with a re-alignment of market shares. Though many global giants are planning to have a share in the pie of the growing small car segment in India, we believe MUL will be able to retain if not increase its overall market share because of its highly loyal customer base, low maintenance costs, aggressive model launches and wide-spread national sales and service network.



Massive car financing infrastructure targeting B and C cities to boost volumes

Traditionally Maruti with outlets spread over more than 160 cities suffered in financial sales vis-a-vis others because the others operated in cities and towns, which had organized finance. Post tie-up with SBI and its associates, the penetration of SBI for Maruti Car Finance has increased from about 5-6% to about 10%-11% last year. With this Maruti's overall share of financed cars is now over 70% compared to industry's over 80% thus helping it to raise volumes from untapped small towns and rural areas targeting two-wheeler owners, teachers, government employees etc..Also, the company has tied up with Mahindra Finance and Magma Leasing recently which will help it to penetrate deep to untapped areas with their strong rural reach.

As a good marketer, Maruti in a way is helping in expanding small car markets complemented by its penetrative and innovative financing network coupled with loads of advertising and promotional sales. In today's market, the increasing role of car financing has reduced the correlation of consumer-buying behavior with sentimental and other macro factors. With several initiatives like Maruti Finance, Maruti Insurance, 'True Value'(for exchange of used cars), extended warranty, 'Dil se' etc., Maruti is well-positioned to strengthen customer loyalty thus leading to repeat purchases. Maruti has topped JD Power Survey in customer satisfaction for 7th consecutive year in row which will help it to have repeat customer purchases.

Valuation

MUL has a sales network of 307 state-of-the-art showrooms across 189 cities with over 6000 trained personnel. The company enjoys a market share of 58% in small and compact car segment and overall 51% market share in passenger cars. The company has aggressive plans to launch five new models over next five years which includes an export car by the year 2009. This would be a car specifically designed for exports market especially European market. Moreover, It has successfully entered into growing diesel segment with the launch of Swift(Diesel). Also, Despite its rising raw material cost, MUL has been able to maintain its margins at commendable levels due to increasing efficiencies and a better product mix. Though many global giants are planning to have a share in the pie of the growing small car segment in India, we believe MUL will be able to retain if not increase its overall market share because of its highly loyal customer base, low maintenance costs, aggressive model launches and wide-spread national sales and service network.

We believe the company will be able to retain its leadership in passenger cars market if not increase with its strong leadership position in compact car segment which accounts for 69.5% of overall car market size. Indian market is expected to remain centered around compact cars due to poor roads, heavy traffic, high petrol prices and affordability issues for at least next three years. Factors like rising consumerism, favorable demographics, affordable financing, excise duty cuts (in the previous Budget) coupled with wide-spread dealer network, superior customer rating and aggressive marketing with continuous new product launches will strengthen Maruti's position further in domestic car market. At present stock looks attractive at 15.0x FY08E & 11.8x FY09E earnings, 8.5x FY08E EV/EBDITA & 6.7x FY09E EV/EBDITA and 1.3x FY08E MCAP/Sales & 1.02x FY09E MCAP/Sales. We maintain 'Accumulate' with one year perspective.

Risk Factors

- Any further rise in interest rates could dampen the demand
- Increasing competition in small car segment in coming years could lead to loss of market share and realisations.

Quarterly Financials

Particulars (Rs Mn)	Q3FY07	Q3FY06	% Change	9MFY07	9MFY06	% Change
Net Sales	36641.90	31043.10	18.04	101788.00	87430.90	16.42
Expenditure						
Raw Material Cost	27662.10	23690.30	16.77	76827.30	67811.10	13.30
Manufacturing Exps	3322.70	2187.20	51.92	8942.60	6816.10	31.20
Employee Cost	738.30	583.90	26.44	2077.60	1720.60	20.75
Total Expenditure	31723.10	26461.40	19.88	87847.50	76347.80	15.06
Operating Profit	4918.80	4581.70	7.36	13940.50	11083.10	25.78
OPM %	13.42	14.76		13.70	12.68	
Other Income	1437.10	1143.10	25.72	4387.60	3460.70	26.78
PBDIT	6355.90	5724.80	11.02	18328.10	14543.80	26.02
PBDIT Margin (%)	17.35	18.44		18.01	16.63	
Interest	157.40	17.30	809.83	220.70	169.80	29.98
PBDT	6198.50	5707.50	8.60	18107.40	14374.00	25.97
Depreciation	758.60	680.60	11.46	1995.40	2128.60	-6.26
PBT	5439.90	5026.90	8.22	16112.00	12245.40	31.58
PBT Margin (%)	14.85	16.19		15.83	14.01	
Tax	1675.80	1636.80	2.38	4977.80	3964.10	25.57
PAT	3764.10	3390.10	11.03	11134.20	8281.30	34.45
PAT Margin (%)	10.27	10.92		10.94	9.47	
EPS (Rs.)	13.03	11.73		38.54	28.66	

Particulars (Rs Mn)	Q3FY07	Q3FY06		9MFY07	9MFY06	
Raw Material/Sales	75.49	76.31		75.48	77.56	
Employee Cost/Sales	2.01	1.88		2.04	1.97	
Other Exps/Sales	9.07	7.05		8.79	7.80	

Financials

Profit & Loss (Rs Mn)	2006	2007E	2008E	2009E
Net Sales	120,034.2	135,717.3	168,486.4	225,513.5
Material Cost	92,169.9	102,436.4	128,049.7	171,390.3
Manufacturing Exps	6,239.0	11,923.5	13,815.9	18,492.1
Empl Cost	2,287.4	2,770.1	3,201.2	4,284.8
Selling & Distribution	3,560.0	-	-	-
Total Mfg Cost	104,256.3	117,130.0	145,066.8	194,167.2
Operating Profit	15,777.9	18,587.3	23,419.6	31,346.4
Other Income	4,780.1	5,850.1	2,916.3	2,976.3
PBDIT	20,558.0	24,437.5	26,335.9	34,322.7
Interest	203.9	294.3	314.5	584.5
PBDT	20,354.1	24,143.2	26,021.4	33,738.2
Depreciation	2,854.2	2,660.5	3,600.6	5,250.6
PBT	17,499.9	21,482.7	22,420.8	28,487.5
Tax	5,609.4	6,637.1	7,174.6	9,116.0
PAT	11,890.5	14,845.6	15,246.1	19,371.5

Ratios	2006	2007E	2008E	2009E
PBDIT%	17.13	18.01	15.63	15.22
PBT%	14.58	15.83	13.31	12.63
NPM%	9.91	10.94	9.05	8.59
Interest Cover	86.83	74.00	72.28	49.74
RONW%	21.81	21.40	18.02	18.63
ROCE%	36.70	35.02	30.05	31.20
Inv Days	26.80	25.55	21.90	21.90
Debtor Days	16.25	18.61	17.06	17.06
Debt/Equity	0.01	0.01	0.04	0.06
Creditors Days	58.22	60.45	60.03	60.03
EPS	41.14	51.37	52.75	67.03
P/E	19.32	15.48	15.07	11.86
Price/BV	4.21	3.31	2.72	2.21
BVPS	188.67	240.04	292.79	359.82
Market Cap (Rs Mn)	229,755.0	229,755.0	229,755.0	229,755.0
EV (Rs Mn)	216,456.0	216,671.3	224,787.4	230,231.4
EV/EBDITA (x)	10.53	8.87	8.54	6.71
MCap/Sales (x)	1.91	1.69	1.36	1.02
EV/Sales (x)	1.80	1.60	1.33	1.02

Balance Sheet (Rs Mn)	2006	2007E	2008E	2009E
Equity	1,445.0	1,445.0	1,445.0	1,445.0
Reserves	53,081.0	67,926.6	83,172.7	102,544.3
Secured Loans	717.0	417.0	3,017.0	6,017.0
Total Debt	717.0	417.0	3,017.0	6,017.0
Def. Tax Liability (Net)	779.0	-	-	-
TOTAL LIABILITIES	56,022.0	69,788.6	87,634.7	110,006.3
Gross Block	49,546.0	50,466.0	65,466.0	95,466.0
ACC Depreciation	32,594.0	35,254.5	38,855.2	44,105.8
Net Block	16,952.0	15,211.5	26,610.8	51,360.2
CWIP	920.0	15,000.0	30,000.0	30,000.0
Fixed Assets	17,872.0	30,211.5	56,610.8	81,360.2
Investments	20,512.0	20,512.0	20,512.0	20,512.0
Working Capital				
Inventories	8,812.0	9,500.2	10,109.2	13,530.8
Debtors	6,548.0	8,143.0	9,266.8	12,403.2
Cash/Bank	14,016.0	13,500.7	7,984.6	5,540.6
Loans & Advances	7,662.0	8,821.6	9,266.8	12,403.2
Others	458.0	814.3	842.4	902.1
Current Assets	37,496.0	40,779.9	37,469.7	44,780.0
Liabilities	15,058.0	16,964.7	21,060.8	28,189.2
Provisions	4,800.0	4,750.1	5,897.0	8,456.8
Current Liabilities	19,858.0	21,714.8	26,957.8	36,645.9
Net Working Capital	17,638.0	19,065.1	10,511.9	8,134.0
Total Assets	56,022.0	69,788.6	87,634.7	110,006.3

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Investment Research

PPFAS

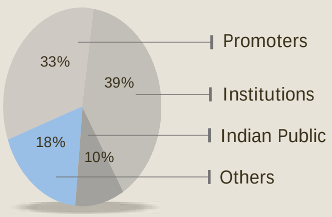
Tata Motors Limited

BUY | CMP Rs. 776.0

Stock Codes

Bloomberg	: TTMT.IN
Reuters	: TELC.BO
BSE Code	: 500570
NSE Code	: TATAMOTORS
BSE Group	: A

Share Holdings
(as on 31st Dec. 06)



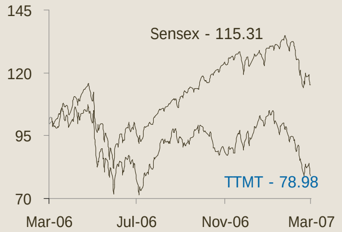
Stock Data

Benchmark	: Sensex
52 W High Rs.	: 997.0
52 W Low Rs.	: 650.0
Mkt Cap in Crs.	:29,900.0
Face Value	: Rs. 10.0

Absolute Return

%	1m	3m	6m
Tata Motors	-17.61	-9.81	-7.73
Sensex	-10.88	-5.44	9.49

Price Comparison



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- Tata Motors Limited once again reported strong numbers during Q3FY07 in line with market expectations. The net sales grew by 37.08 % from Rs.5074.8 crs to Rs. 6956.8 crs on Y-o-Y basis including foreign exchange gains of Rs. 131.6 crs. The net sales grew by 34.5% excluding gain on account of foreign exchange. The net sales grew by 40% on YTD basis from Rs.13756 crs to Rs. 19250 crs. This has been made possible on the back of robust growth in volumes of 27% on Y-o-Y basis and 33% on YTD basis. Also, average realizations for the company increased on back of selective price hikes during the year. On consolidated basis, The net sales grew by 37% on Y-o-Y basis and 43% on YTD basis.

- The operating profit improved by 53% on Y-o-Y basis and 40% on YTD basis. The operating margin showed improvement from 12.26% to 13.69% on Y-o-Y basis. However, If one excludes effect of foreign exchange gain, operating margins witnessed decline of around 80 basis points. The margins has shown improvement on sequential basis on account of more or less stable raw material prices and cost savings in other expenditures.

- Product development expenses increased by 272% on Q-o-Q basis and 170% on YTD basis. Other income was down by 83% on Q-o-Q basis from Rs.185 crs to Rs. 31 crs. and 32% down on YTD basis. The company had sold some stake in one of its subsidiary Telco Construction Equipment Company Ltd. for Rs.164.30 crs. This was included in last year's other income. The absence of such income in this year's quarter was main reason in decline of other income. Also, with most of the dividend income from its subsidiaries accruing in first two quarters, the other income was depressed on a Q-o-Q basis.

- The interest cost increased by 32% on Y-o-Y basis from Rs. 77 crs to Rs. 102 crs. and 38% on YTD basis from Rs. 216 crs to Rs.299 crs. This was mainly on account of the company's large capex plans in order to double the capacities in next four

Particulars (Rs Crs)	2004	2005	2,006	2007E	2008E	2009E
Net Sales	13,223.22	17,419.13	20,654.35	25,667.60	29,695.79	34,513.26
EBDITA	1,889.06	2,270.06	2,790.98	3,300.97	4,043.72	4,680.11
EBDITA margins(%)	14.29	13.03	13.51	12.86	13.62	13.56
PAT	810.34	1,236.95	1,528.88	1,782.66	2,191.60	2,485.14
EPS	22.71	34.19	39.93	46.26	56.88	64.50
P/E	34.17	22.70	19.43	16.77	13.64	12.03
EV/EBDITA	14.92	12.58	11.30	9.67	7.99	6.92
MCAP/SALES	2.09	1.61	1.44	1.16	1.01	0.87
ROCE(%)	35.34	31.73	30.73	29.09	29.87	29.21
RONW(%)	22.69	30.22	27.68	24.35	23.04	20.71

years. The depreciation expenses increased by 9% on Y-o-Y basis and 11% on YTD basis. The tax expenses increased by 48% on Y-o-Y basis and 36% on YTD basis.

- The PAT witnessed increased of 11.50% from Rs. 460 crs to Rs. 513 crs on Y-o-Y basis and an increase of 25% on YTD basis from Rs. 1070 crs. To Rs. 1336 crs. The PAT margin witness decline from 9.07% to 7.38% on Y-o-Y basis on account of higher interest and tax expenses and reduced other income. But if we remove the other income effect, the PAT margin witnessed improvement from 5.41% to 6.92% in Y-o-Y basis. On consolidated basis, PAT witnessed an increase of 9% on Y-o-Y basis and 26% on YTD basis.

Strong Volumes across segments

The company reported strong 38% Y-o-Y basis growth in Domestic Commercial Vehicles (CVs) segment and 22% growth in Domestic Passenger Vehicles (PVs) segment. The growth in CV segment was mainly on account of strong growth in M/HCV and LCV segment. During April-Dec'06 period, M/HCv industry grew by 37.2% where as the company recorded growth of 42%. Similarly, LCV industry grew by 34% on YTD basis and the company recorded growth of 55% on YTD basis in similar segment. On an average 6,200 units of Tata Ace were sold during Q3FY07. Overall, the company successfully increased its market share to 64.7% from 60.2% on YTD basis in CV segment.

Overall PVs industry grew by 20.8% on YTD basis where as the company achieved growth of 23%. While the entry level mid size car segment declined by nearly 32% in Q3FY07, decline in the company's sale was limited to 24% during that period. The company retained its market leadership with 37.2% in that segment. The company recorded growth of 26% in Utility Vehicle(UV) segment on YTD basis compared to industry growth of 12%. The UV segment has recovered due to the successful re-launch of Safari at a lower price point. Overall market share was improved to 16.1% from 15.8% on YTD basis.

On export front with sale of 11,610 vehicle during third quarter, the company reported marginal 1% decline on Y-o-Y basis. Where as on YTD basis, the company reported

Volume Growth in Q307

Particulars	Q3FY07	Q3FY06	Y-o-Y %	9MFY07	9MFY06	YTD %
M/HCVs	44,824.0	33,558.0	33.6	121,776.0	85,602.0	42.3
LCVs	32,402.0	22,519.0	43.9	89,343.0	57,818.0	54.5
Total Cvs	77,226.0	56,077.0	37.7	211,119.0	143,420.0	47.2
Compact Car	34,633.0	25,309.0	36.8	102,361.0	75,399.0	35.8
Mid-size Car	6,656.0	8,724.0	(23.7)	23,299.0	27,192.0	(14.3)
Uvs	11,425.0	9,336.0	22.4	31,347.0	24,926.0	25.8
Total Pvs	52,714.0	43,369.0	21.5	157,007.0	127,517.0	23.1
Total Domestic Sales	129,940.0	99,446.0	30.7	368,126.0	270,937.0	35.9
CV s	9,230.0	7,273.0	26.9	26,125.0	20,843.0	25.3
PV s	2,380.0	4,509.0	(47.2)	12,709.0	14,006.0	(9.3)
Total Exports	11,610.0	11,782.0	(1.5)	38,834.0	34,849.0	11.4
Total Volumes	141,550.0	111,228.0	27.3	406,960.0	305,786.0	33.1

growth of 11%. During Q3FY07, depreciation of Rand continued to adversely impact exports to South Africa which is one of the major market for the company. The company also introduced its passenger vehicles in Ghana during the quarter. It is to be noted that revenues from International Business formed around 16% of the consolidated revenue of the company during April-December'06.

JV with Thonburi Automotive Assembly Plant Company

During the quarter, Tata Motors announced that it would set up a joint venture with a Thailand-based company, Thonburi, to manufacture, assemble and market pick-up trucks. Tata Motors will own 70% in these joint venture. This facility will get commissioned within one year with capex of around Rs. 120 crs. Such a joint venture would be a win-win situation for both Tata Motors and Thonburi. The venture provides Tata Motors an entry into the Thai market, which is the world's second largest pick-up vehicle market. The market size for pick-ups in Thailand currently stands at 450,000 units and is expected to grow at a good pace going forward. Tata Motors targets to sell 30,000 vehicles annually within three years of its starting operations. Tata Motors is specially developing a pick-up vehicle for the Thai market with a 3.0-litre Dicor engine and is looking to price the model competitively. The vehicle would have an initial local content of 50%, which shall be later scaled up to 80%. Initially, the venture would focus on the Thai market, and may later expand operations to other ASIAN countries. This is positive development as it will help the company to de-risk its CV business by reducing its dependence on domestic market.

JV with Fiat : win-win deal

Recent tie-up between Tata Motors and Fiat is a win -win deal for both players. As per MOU, Tata Motors and Fiat Auto would invest Rs4,000 crore to make cars and engines at Fiat's Ranjangaon unit. The plant would have capacity to manufacture 100,000 cars and 200,000 engines and transmissions on yearly basis. The commercial operations will begin in the current year 2008. Fiat would introduce its premium cars for the B and C segments, like Fiat Grande Punto and the Fiat Linea. The venture would manufacture the Fiat-1.3-litre multi-jet diesel engine, the 1.4-litre engine and a new 1.2-litre gasoline engine, which are part of the "Fire" family. Tata Motors would also benefit from the joint venture, as the same would provide it access to Fiat Auto's world class power train technology. Tata Motors could also use the engines produced through this joint venture for its forthcoming models.

In future, this deal has scope to explore potential to work together on product development, procurement and sourcing, joint manufacturing and overseas marketing. TM will be able to access Fiat's distribution network to sell its cars and utility vehicles in Europe. TM may also get access to underutilized manufacturing facilities of Fiat India which will reduce its capital outlay. In turn, Fiat will benefit from TM's cost competitiveness in manufacturing and distribution network. Tie up with TM is in line with Fiat’s turnaround strategy.

Capacity expansion

Tata Motors has announced a capital expenditure plan of Rs. 10,000cr over next three years to be invested in its existing and new capacities. It includes capital expenditure for the small car plant in West Bengal and a new plant for the Ace likely to come in Uttranchal. It is also setting up a bus manufacturing plant with Marco Polo of Brazil.

New Launches

The company has a series of plans for new model launches and new platforms across segments besides face lift of its existing models including the Indica platform. Tata Motors will launch NOVAS, the heavy duty truck range from the Tata Daewoo Motors stable. The new products are scheduled to be launched only from the beginning of FY2008.

Strong Subsidiaries performance

Most of key subsidiaries reported robust turnover growth and PAT growth. In long-term, Investments in subsidiaries of the companies would unlock the real value of Tata Motors. Tata Motor Financial Services (TMFSL) started its operations this quarter. Total vehicle financing disbursal during the fiscal stood at Rs. 6370, out of which Rs. 1540 crs were disbursed by TMFSL.

Subsidiaries	Turnover			PAT		
	Q3FY07	Q3FY06	% Chng	Q3FY07	Q3FY06	% Chng
Tata Daewoo CV Ltd.(TDCV)	589.8	424.9	38.8	22.5	24.7	(9.2)
Telco Construction Equipment Co.Ltd.	486.3	329.0	47.8	49.3	24.3	103.1
Tata Technologies Ltd.	246.9	221.1	11.6	3.4	10.1	(66.3)
HV Transmission Ltd.	47.2	33.1	42.4	13.3	8.2	62.1
HV Axles Ltd.	53.0	38.7	37.1	18.0	12.0	49.8
T Financial Services Ltd.(TMFSL)	52.1	-		3.9	-	

Valuations

Tata Motors is the largest automobile company in India with ambitious global plans. It is the world's fifth largest medium and heavy truck manufacturer and the second largest heavy bus manufacturer. Tata Motors is expected to witness growth of 16% CAGR in its top line for FY07-09E because of its product-mix, leadership position in CV segments, positive growth in passenger car segment, surprises in bus segment, aggressive cost cutting strategies, robust growth in exports and proposed launches of new products in both CVs and passengers car segments in next three years. At present, the stock is trading at 12.03 x FY09E EPS of Rs. 64.50, 0.87 Mcap/Sales FY09E and 2.49 x P/BV FY09E on a stand alone basis.

TM has strategic investments in several subsidiaries which has attained maturity in their respective businesses and have shown robust performance. The management also has shown their interest to unlock the value in these subsidiaries via either induction of a strategic partner or through public listing of the same in near future. We envisage around at least 13% increase in EPS on account of these subsidiaries. There is significant upside over our present valuation.
We maintain “Buy”.

Consolidated Valuation (presuming 13% increase in EPS)

	2007A	2008E	2009E
EPS (Rs.)	52.27	64.27	72.88
P/E (x)	14.85	12.07	10.65

Risk Factors

- Fuel accounts for more than 50% of operating cost of truck operators. Any rise in oil prices poses a key threat to operator's profitability and thus CV demand.
- Rising interest rate is a cause of concern as sales through financing accounts for 90% of trucks sold.
- Any increase in commodity prices will reduce operating margins
- The competition from Hyundai, Maruti, General Motors and Honda will become more cut throat in coming days as rival companies are getting into diesel products. Though TM's focus on diesel cars (80% of cars sold) and already stabilised player in terms of technology (with Fiat's Alliance) will insulate it against rivalry. Also, the company might face pressure on margins as it has to offer attractive discounts in order to sustain its sales.
- In CV business, the company is the leader with 65% market share. However, it may face competition from international majors like Volvo which are also eyeing the Indian market.

Quarterly Financials

Particulars (Rs Crs)	Q3FY07	Q3FY06	% Chng	9MFY07	9MFY06	% Chng
Gross Sales	8,047.4	5,908.2	36.2	22,284.0	16,029.0	39.0
Less: Excise Duty	1,090.6	833.4	30.9	3,033.3	2,273.5	33.4
Net Sales	6,956.8	5,074.9	37.1	19,250.7	13,755.6	39.9
Expenditure						
Raw Material Cost	4,762.1	3,427.5	38.9	13,169.8	9,200.9	43.1
Staff Cost	358.1	279.9	27.9	1,003.2	832.1	20.6
Other Expense	884.5	745.4	18.7	2,730.5	2,038.8	33.9
Total Expenditure	6,004.6	4,452.8	34.9	16,903.5	12,071.8	40.0
Operating Profit	952.2	622.1	53.1	2,347.2	1,683.8	39.4
OPM %	13.7	12.3		12.2	12.2	
Product Devlpt Expenses	28.7	7.7	272.2	56.5	20.9	170.7
Other Income	31.5	185.5	(83.0)	231.3	343.7	(32.7)
PBDIT	955.0	799.9	19.4	2,521.9	2,006.6	25.7
PBDIT Margin (%)	13.7	15.8		13.1	14.6	
Interest	102.3	77.3	32.4	299.5	216.2	38.6
PBDT	852.7	722.6	18.0	2,222.4	1,790.5	24.1
Depreciation	143.5	130.8	9.7	428.0	384.7	11.3
PBT	709.2	591.8	19.8	1,794.4	1,405.8	27.6
PBT Margin (%)	10.2	11.7		9.3	10.2	
Exceptional Items	0.5	-		1.0	-	
Tax	195.6	131.5	48.7	456.6	335.0	36.3
PAT	513.2	460.2	11.5	1,336.7	1,070.8	24.8
PAT Margin (%)	7.4	9.1		6.9	7.8	
Equity Capital	385.3	376.3		385.3	376.3	
EPS Diluted (Rs.)	12.7	11.5		33.0	26.8	

Financials

Profit And Loss (Rs Crs)	2006	2007A	2008E	2009E
Net Sales	20,654.4	25,667.6	29,695.8	34,513.3
Material Cost	14,007.0	17,559.8	20,193.1	23,469.0
Manufacturing Exps	2,924.6	3,640.7	3,860.5	4,486.7
Empl Cost	1,147.2	1,337.6	1,633.3	1,898.2
Product Development	73.8	75.3	86.1	100.1
Total Expenditure	18,152.5	22,613.4	25,773.0	29,954.1
Operating Profit	2,501.9	3,054.2	3,922.8	4,559.2
Other Income	289.1	246.7	120.9	120.9
Pbdit	2,791.0	3,301.0	4,043.7	4,680.1
Interest	226.4	337.7	322.0	322.0
Pbdt	2,564.6	2,963.2	3,721.7	4,358.1
Depreciation	520.9	570.7	799.6	1,044.6
Pbt	2,043.7	2,392.5	2,922.1	3,313.5
Exceptional Items	(9.7)	1.0	-	-
TAX	524.5	608.9	730.5	828.4
PAT	1,528.9	1,782.7	2,191.6	2,485.1

RATIOS:	2006	2007A	2008E	2009E
PBDIT %	13.51	12.86	13.62	13.56
PBT %	9.89	9.32	9.84	9.60
PAT %	7.40	6.95	7.38	7.20
Interest Coverage	10.03	8.08	10.07	11.29
RONW (%)	27.68	24.35	23.04	20.71
ROCE (%)	30.73	29.09	29.87	29.21
Inventory T/O Days	35.56	39.99	36.50	36.50
Debtors T/O Days	10.88	11.04	10.99	10.99
Debt/ Equity (x)	0.53	0.55	0.42	0.34
Creditors T/O Days	150.98	160.06	161.03	161.03
EPS (Rs.)	39.93	46.26	56.88	64.50
P/E (x)	19.43	16.77	13.64	12.03
P/ BV (x)	5.38	4.08	3.14	2.49
BVPS (Rs.)	144.25	190.03	246.91	311.40
Market Cap (Rs.crs)	29,710.7	29,900.8	29,900.8	29,900.8
EV (Rs.crs)	31,528.1	31,931.2	32,295.5	32,386.2
EV/EBITDA (x)	11.30	9.67	7.99	6.92
M Cap/Sales (x)	1.44	1.16	1.01	0.87
EV/Sales(x)	1.53	1.24	1.09	0.94

Balance Sheet (Rs Crs)	2006	2007A	2008E	2009E
Equity Capital	382.9	385.3	385.3	385.3
Reserves	5,154.2	6,936.9	9,128.5	11,613.6
Misc Exp Etc	14.1	-	-	-
Actual Reserves	5,140.1	6,936.9	9,128.5	11,613.6
Shareholders Funds	5,523.0	7,322.2	9,513.8	11,998.9
Secured Loans	822.8	1,910.9	1,910.9	1,910.9
Unsecured Loans	2,114.1	2,114.1	2,114.1	2,114.1
Total Borrowed Funds	2,936.8	4,025.0	4,025.0	4,025.0
Deferred Tax Liability	622.5	-	-	-
Total Liabilities	9,082.3	11,347.2	13,538.8	16,023.9
Gross Block	7,971.6	8,922.7	11,422.7	14,922.7
Acc Depreciation	4,401.5	4,972.2	5,771.8	6,816.4
Net Block	3,570.0	3,950.5	5,650.9	8,106.3
Cwip	951.2	2,500.0	3,500.0	3,500.0
Fixed Assets	4,521.2	6,450.5	9,150.9	11,606.3
Investments	2,015.2	2,015.2	2,015.2	2,015.2
Working Capital				
Inventory	2,012.2	2,812.0	2,969.6	3,451.3
Sundry Debtors	715.8	898.4	1,039.4	1,208.0
Cash & Bank Balance	1,119.4	1,994.6	1,630.3	1,539.6
Loans & Advances	5,813.9	6,416.9	7,423.9	8,628.3
Current Assets	9,661.3	12,121.9	13,063.2	14,827.2
Liabilities	5,900.3	7,700.3	8,908.7	10,354.0
Provisions	1,215.0	1,540.1	1,781.7	2,070.8
Current Liabilities	7,115.4	9,240.3	10,690.5	12,424.8
Net Working Capital	2,546.0	2,881.5	2,372.7	2,402.4
Total Assets	9,082.3	11,347.2	13,538.8	16,023.9

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Investment Research

Centurion Bank of Punjab Limited

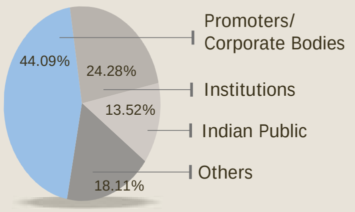
ACCUMULATE | CMP Rs. 35.75

Stock Codes

Bloomberg	: CBOP.IN
Reuters	: CENB.BO
BSE Code	: 532273
NSE Code	: CENTBOP
BSE Group	: B1

Share Holdings

(as on 31st Dec. 06)



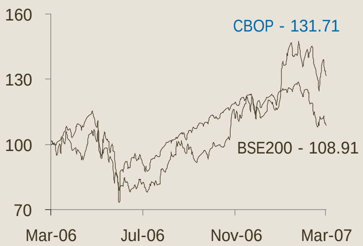
Stock Data

Benchmark	: BSE 200
52 W High Rs.	: 39.70
52 W Low Rs.	: 18.60
Mkt Cap in Crs.	: 5232.0
Face Value	: Rs. 1.0

Absolute Return

%	1m	3m	6m
Centurion	-10.29	8.45	34.65
BSE 200	-13.10	-12.11	-9.97

Price Comparison



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Centurion Bank of Punjab (CBoP), a new generation private sector bank was formed by the merger of Centurion Bank and Bank of Punjab. The bank, operating through 256 branches and 402 ATMs, has a strong retail franchisee. The day-to-day operations of the bank are looked after by Mr. Shailendra Bhandari, Managing Director & CEO and Mr. Rana Talwar is the Chairman of the Board. Some of the bank's major shareholders, Sabre Capital, Bank Muscat and Keppel Corporation, Singapore are represented on the Board.

Merger with LKB

CBoP is awaiting RBI approvals for merger with Lord Krishna Bank (LKB), a Cochin based bank. Post merger LKB will add 112 branches and 44 ATMs to CBoP's network with major presence in Kerala. Further 38% of LKB's branches are spread in the rest of the country, primarily in metro and urban areas. LKB will also add Rs 3700 crs of business to CBoP. The merger will be effective from April 1, 2006. The share swap ratio has been fixed at 5:7, i.e. For every 5 shares in LKB, its shareholders will receive 7 shares of CBoP. This will add up to Rs 13.21 crs equity share capital in CBoP's balance sheet.

Sustainable Margins?

CBoP is largely concentrated toward retail, which constitutes around 69% of its total advances resulting in high yields. In retail, 2 wheelers, mortgages and commercial vehicles form a major portion. The bank will continue to maintain its focus on retail. LKB will add Rs 1400 crs to CBoP's advance book, of which around Rs 1200 crs comes from SME segment. CBoP intends to continue to focusing on retail and expand their SME segment so that the retail portion comes down to 65% over a few years.

As on Dec 06, the yield on advances (YoA) stood at 12.5%. With the rising rates, CBoP has increased its PLR to 14.5% which should reflect in the numbers of first quarter of FY2008. Most of the mortgage loans of CBoP are on a floating basis. Further when the hike in rates is passed on to other retail borrowers, the increase in EMI is marginal for the borrower to feel the pinch. This enables CBoP to easily pass on the rate hikes.

However to fund the expansion in loan book, CBoP has been aggressively raising deposits. The cost of deposits (CoD) has gone up from 4.7% as on Dec 05 to 5.6% as on Dec 06. The CASA ratio has also fallen from 38% as on Dec 05 to 33.5% as on Dec 06. LKB operates at low NIMs of about 2.2%, but taking into account the size of the bank, the impact on CBoP's margins should not be much. Despite the rising cost of funds, the management is confident that their NIMs will be maintained above 4.2%.

Asset Quality

CBoP has been aggressive on the provisioning front. As on Dec 2006, the net NPA ratio stood at 1.2%. The bank plans to bring down LKB's Net NPA ratio to CBoP's levels of 1.2% before the merger.

High Contribution of Non-Interest Income

Non-interest income contributes a significant portion of the total income for CBoP. CBoP also sells a number of wealth management products such as mutual funds and general and life insurance products. The bank also offers various NRI banking products to overseas Indians. Merger with LKB, which has a high NRI customer base, will allow CBoP to leverage on LKB's branches and sell its wealth management and NRI banking products.

High Cost of Operations Likely to Come Down

Currently CBoP is making huge investments in technology, risk management and expanding its network. The bank plans to increase its penetration in the urban areas. CBoP's cost to income ratio as on March 06 stood at 77%, and is expected to come down slightly from these levels. However on completion of these initial investments, the cost to income ratio should moderate and the benefits should get reflected in the net profit.

Branch Expansion

As on Dec 06, CBoP operated from 256 branches and 402 ATMs. During the last quarter of FY07, 23 additional branches have been opened. LKB will add 112 branches to CBoP's network, which is around 40% of CBoP's current branch network. Post merger, CBoP will be the largest new generation banking network in the state of Kerala. 38% of LKB's branches are located in metro and urban areas. This will enable CBoP to tap the retail and SME potential as well as its NRI links by leveraging on LKB's branch network. CBoP will try to increase its penetration in certain urban areas. The bank is open to inorganic growth, but is now looking out for a similar sized bank which will considerably add to its business.

Investment Book

CBoP has a well hedged investment book, with 78% of its investments in the HTM category and 83% of its SLR securities in HTM category. The duration of its AFS book as on Dec 06 stood at 0.55 years.

Comfortable Capital Adequacy Ratio

CBoP has recently made a preferential issue to India Advantage Value Fund, of 7.5 crs equity shares at a price of Rs 24.54 per equity share. The bank is also in the process of placing 9.5 crs equity shares at Rs 24.54 per share with Bank of Muscat in the current financial year. Post these placements the capital adequacy for the year will improve to 13.5% of which Tier I capital will be 12.5%. The bank does not propose any further dilutions in equity till March 2008. With enough Tier II room, CBoP is well capitalised for growth.

Outlook and Valuations

We expect the bank to grow above the sector average due to its lower base. CBoP's management has successfully completed the merger of Centurion Bank with Bank of Punjab and the merger with LKB is also moving well. The bank is open for inorganic growth with a bank of similar size. CBoP also makes a good acquisition target when the banking sector will be opened up in 2009. The bank is trading at 4.6x FY08 book value per share. We recommend “Accumulate”.

Financials

Income Statement (Rs Crs)				
Year Ended March 31	FY05*	FY06**	FY07E#	FY08E
Interest Income	346.1	803.2	1,352.3	1,896.6
Growth (%)		132.1	68.4	40.2
Interest Expense	168.2	404.4	690.9	1,028.4
Growth (%)		140.4	70.8	48.9
Net Interest Income	177.9	398.8	661.5	868.2
Growth (%)		124.2	65.9	31.3
Other Income	72.2	248.9	377.5	536.0
Growth (%)		244.7	51.7	42.0
Net Revenues	250.1	647.6	1,038.9	1,404.2
Operating Expense	219.2	499.7	694.0	880.3
-Employee Expense	42.7	139.3	222.2	300.0
-Other opex	176.5	360.4	471.8	580.4
Pre Provision Profit	30.9	148.0	344.9	523.8
Provisions	5.8	122.7	216.1	325.6
Amount Realised under FSA	-	62.5	-	-
Net Profit	25.1	87.8	128.8	198.2
Growth (%)		249.7	46.7	53.8

Ratios				
Year Ended March 31	FY05*	FY06**	FY07E#	FY08E
Net Interest Margin	5.10%	4.60%	4.79%	5.00%
Int Income / Total Income	82.74%	76.35%	78.18%	77.97%
Non-Int Income / Total Income	17.26%	23.65%	21.82%	22.03%
LCD to Total Deposits	29.02%	38.73%	33.08%	31.50%
RoNW	4.26%	9.43%	11.27%	15.11%
RoAA	0.54%	1.10%	0.90%	1.01%
Int Expended / Int Earned	48.60%	50.35%	51.09%	54.22%
Cost to Income Ratio	87.64%	77.15%	66.80%	62.70%
Op Expense/Total Expense	55.75%	48.66%	43.35%	39.40%
Employee Cost/Op Expense	19.48%	27.87%	32.02%	34.07%
Credit Deposit Ratio	62.14%	69.51%	72.58%	73.15%
Investment Deposit Ratio	41.91%	31.10%	31.00%	31.00%
Net NPAs to Advances	2.51%	1.13%	1.16%	0.90%
CAR	21.42%	12.52%	13.50%	12.00%
-Tier 1	17.80%	10.84%	12.50%	10.00%
-Tier 2	3.62%	1.68%	1.00%	2.00%

Balance Sheet (Rs Crs)				
Year Ended March 31	FY05*	FY06**	FY07E#	FY08E
LIABILITIES				
Equity Capital	101.3	140.8	161.5	171.0
Reserves	488.6	776.9	968.4	1,127.0
Networth	590.0	931.2	1,143.4	1,311.5
Total Deposits	3,530.4	9,399.6	14,247.8	17,952.2
-Savings Deposits	513.6	1,429.9	1,902.0	2,282.4
-Current Deposits	511.1	2,210.4	2,810.7	3,372.8
-Term Deposits	2,505.7	5,759.4	9,535.1	12,297.0
Borrowings	43.8	51.6	57.2	64.1
Other Liabilities	447.5	947.8	1,931.2	2,534.1
Total	4,611.7	11,330.2	17,379.7	21,861.9
ASSETS				
Loans	2,194.0	6,533.4	10,340.6	13,132.5
Bal with Bk at call & short notice	131.0	489.5	569.9	718.1
Investments	1,479.6	2,922.8	4,416.8	5,565.2
Cash / Equiv	331.9	556.5	926.1	1,166.9
Fixed Assets	136.4	311.3	403.1	483.8
Other Assets	338.7	516.6	723.1	795.4
Total	4,611.7	11,330.2	17,379.7	21,861.9

Valuation Ratios				
Year Ended March 31	FY05*	FY06**	FY07E#	FY08E
EPS (Rs)	0.25	0.62	0.80	1.16
P/E	142.84	56.78	44.39	30.55
BVPS (Rs)	5.82	6.61	7.08	7.67
P/B	6.08	5.35	5.00	4.62

* FY 2005 Financials represent Centurion Bank only

** FY 2006 Financials represent Centurion Bank of Punjab

\# FY 2007E Financials represent Lord Krishna Bank also

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Investment Research

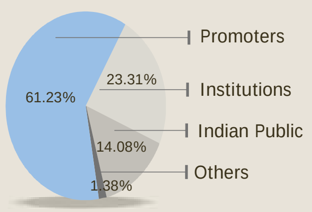
Indian Overseas Bank

BUY | CMP Rs. 98.0 | Target Price Rs. 124.0

Stock Codes

Bloomberg	: IOB.IN
Reuters	: IOBK.BO
BSE Code	: 532388
NSE Code	: IOB
BSE Group	: A

Share Holdings
(as on 31st Dec. 06)



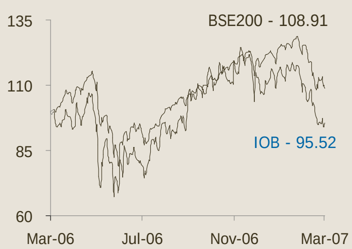
Stock Data

Benchmark	: BSE 200
52 W High Rs.	: 129.0
52 W Low Rs.	: 65.55
Mkt Cap in Crs.	: 5325.4
Face Value	: Rs. 10.0

Absolute Return

%	1m	3m	6m
IOB	-12.33	-12.33	-10.38
BSE 200	-13.10	-12.11	-9.97

Price Comparison



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Indian Overseas Bank (IOB), a mid-sized PSU bank with a market cap of Rs 5300 crs. The bank has a network of 1513 branches and 165 ATMs with a major focus in the south. The bank stands out in the public sector banking space due to its consistent delivery of 20%+ RoEs since FY02.

Investment Argument

Expanding Business at the cost of margins?

IOB has been lending aggressively where the Y-o-Y growth in advances as on Dec 2006 stood grew by 39% supported by a 20% Y-o-Y growth in deposits, resulting in a high credit deposit ratio of 74.5%. Though the Net Interest Margins (NIM) of the bank has not deteriorated, supported by increasing Yield on Advances (YoA), future growth in business may come at the cost of margins.

It has affected a PLR hike to 12.5% with effect from mid February which should reflect in the yields from Q1FY08. The YoA as on Dec 06 stood at 9.49% which should move up to 9.6% and 9.82% in FY07E and FY08E respectively.

Pressed for funds, banks are increasing the interest rates offered on term deposits to fund the loan book growth, which has resulted in a decline in the demand deposits in the system. IOB's cost of deposits (CoD) has gone up from 4.8% in Dec 05 to 5.34% in Dec 06. The CoD for Sept 06 was 4.99%, showing a jump in deposit costs over the preceding quarter too. Proportion of demand deposits in total deposits has also declined 38% in Dec 05 to 36% in Dec 06. We expect the CoDs to rise to 5.68% for FY07E and further to 6.44% in FY08E. As the business growth will be supported by deposit growth, going forward we expect the NIMs to come down to 3.86% and 3.37% for FY07E and FY08E respectively.

Improving Asset Quality to Lower Provisioning Requirements

Gross NPA to Advances has declined from 4.43% in Dec 05 to 2.54% as on Dec 06. Due to improving asset quality, the bank has written back NPA provisions during 9MFY07. We expect the Gross NPA ratio of 2.5% and 1.8% FY07E and FY08E respectively. We have considered a net NPA ratio of 0.46% for FY07E and 0.4% in FY08E. Drop in the provisioning should boost profitability. The NPA coverage as on Dec 06 stood at 81.6%.

Investments

IOB has 85% of its SLR securities in HTM category. The AFS book has a duration of 2 years. The high Yield on Investments (YoI) of the bank, when compared to other PSBs, has also aided in maintaining superior margins.

Improving Operating Efficiency

The Cost to Income ratio stood at 45.13% as on March 06 and we expect it to come down to 43.03% as on March 07. If AS 15 is implemented immediately, the one time hit on reserves would be Rs 200 crs. As per the revised AS-15 guidelines, which accounts for employee benefits, pension liabilities has to be estimated as per the last drawn salary as against current salaries. There is a provision where any arrears of pension and gratuity of the past can be adjusted through reserves. IBA has also taken up the matter with RBI to defer the provisions over 5 years.

Superior Return ratios

High margins, moderate cost to income ratio improving asset quality has enabled IOB to maintain its return ratios. IOB has consistently delivered superior return ratios as compared to its peer Public Sector banks. We expect the bank to maintain a RoNW of around 24-25% in FY07E and FY08E. The Return on Average Assets (ROAA) should be maintained at around 1.4%.

Acquisition of 100% stake in Bharat Overseas Bank

IOB has acquired 100% equity stake in Bharat Overseas Bank (BhoB). BhoB is a small bank with 104 branches with a high concentration in south India. BhoB will add Rs 5298 crs of business and Rs 3730 crs of assets to IOB's balance sheet. With a Net NPA of 1.87% and a capital adequacy ratio of 11.2%, of which 8.4% comprises of Tier I capital, BhoB is quite a healthy bank. Thus IOB has successfully added 100 branches in one financial year, allowing it to consolidate its position in the south. BhoB will be subsequently merged with IOB.

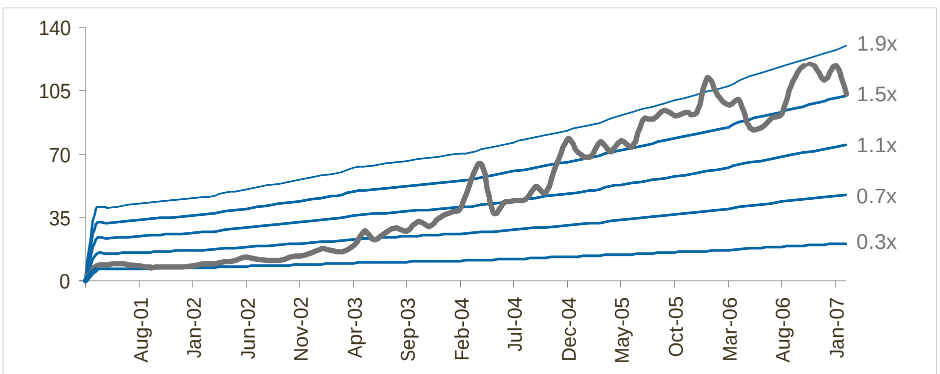
Financial Performance

We expect the business growth to moderate in the last quarter of FY07, with advance and deposit growth settling at 29% and 24% respectively. The credit deposit ratio should be maintained around 72-73% in the next 2 years. Improving yields and costs should pull the NIMs down, resulting in a 13% and 5% growth in net interest income for FY07E and FY08E. However the improving non-interest income, marginal increase in operating expenses and lower provisioning should boost profitability. We expect the net profit to grow by 20% and 19% in FY07E and FY08E respectively.

Outlook and Valuations

Due to superior return ratios compared to its peer public sector banks, IOB has always commanded premium valuations. We expect the sector to witness some compression in the margins and returns. IOB will also experience a decline in margin. However with its high yields in the sector, improving operating efficiency and lower provisioning requirements, we expect the bank to continue to deliver 20%+ returns. The recent fall in the stock prices, has placed IOB at 4.8x FY08E earnings and 1.13x FY08E price to book. We recommend a "Buy" with a target price of Rs 124.

P/B Band



Financials

Income Statement (Rs Crs)			
Year Ended March 31	FY 2006	FY 2007E	FY 2008E
Interest Income	4,406.3	5,478.7	6,779.2
Growth (%)		24.3	23.7
Interest Expense	2,339.1	3,134.3	4,317.9
Growth (%)		34.0	37.8
Net Interest Income	2,067.2	2,344.4	2,461.3
Growth (%)		13.4	5.0
Other Income	728.2	804.7	877.1
Growth (%)		10.5	9.0
Net Revenues	2,795.4	3,149.1	3,338.4
Operating Expense	1,261.6	1,355.1	1,452.7
-Employee Expense	893.6	947.2	1,004.0
-Other opex	368.0	407.9	448.7
Pre Provision Profit	1,533.8	1,794.0	1,885.6
Provisions	750.5	850.8	767.1
Net Profit	783.4	943.2	1,118.6
Growth (%)		20.4	18.6

Ratios			
Year Ended March 31	FY 2006	FY 2007E	FY 2008E
Net Interest Margin	4.05%	3.86%	3.37%
Int Income / Total Income	85.82%	87.19%	88.54%
Non-Int Income / Total Income	14.18%	12.81%	11.46%
LCD to Total Deposits	39.91%	35.87%	34.47%
RoNW	24.65%	24.34%	23.78%
RoAA	1.42%	1.42%	1.41%
Int Expended / Int Earned	53.09%	57.21%	63.69%
Cost to Income Ratio	45.13%	43.03%	43.52%
Op Expense / Total Expense	28.99%	25.38%	22.22%
Employee Cost / Op Expense	70.83%	69.90%	69.11%
Credit Deposit Ratio	68.78%	71.56%	72.78%
Investment Deposit Ratio	37.51%	34.50%	33.50%
Net NPAs to Advances	0.65%	0.46%	0.40%
CAR	13.04%	13.40%	12.00%
-Tier 1	8.54%	8.50%	7.00%
-Tier 2	4.50%	4.90%	5.00%

Balance Sheet (Rs Crs)			
Year Ended March 31	FY 2006	FY 2007E	FY 2008E
LIABILITIES			
Equity Capital	544.8	544.8	544.8
Reserves	2,632.6	3,330.6	4,158.4
Networth	3,177.4	3,875.4	4,703.2
Total Deposits	50,529.3	62,656.4	73,307.9
-Savings Deposits	5,700.3	6,270.3	6,960.1
-Current Deposits	14,468.1	16,204.3	18,310.9
-Term Deposits	30,360.9	40,181.7	48,037.0
Borrowings	736.6	810.3	891.3
Other Liabilities	4,914.4	5,968.5	6,864.3
Total	39,189.4	50,835.9	60,495.8
ASSETS			
Loans	34,756.2	44,835.5	53,354.2
Bal with Bank at call and short notice	629.3	783.2	1,026.3
Investments	18,952.3	21,616.4	24,558.2
Cash / Equiv	3,078.0	4,072.7	4,765.0
Fixed Assets	457.7	503.5	548.8
Other Assets	1,484.3	1,499.2	1,514.2
Total	59,357.8	73,310.5	85,766.7

Valuation Ratios			
Year Ended March 31	FY 2006	FY 2007E	FY 2008E
EPS (Rs)	14.38	17.31	20.53
P/E	6.80	5.65	4.76
BVPS (Rs)	58.32	71.13	86.33
P/B	1.68	1.37	1.13

DISCLAIMER

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Investment Research

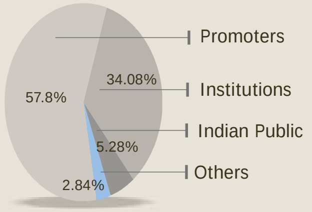
Punjab National Bank

BUY | CMP Rs. 439.0 | Target Price Rs. 520.0

Stock Codes

Bloomberg	: PNB.IN
Reuters	: PNBK.BO
BSE Code	: 532461
NSE Code	: PNB
BSE Group	: A

Share Holdings
(as on 31st Dec. 06)



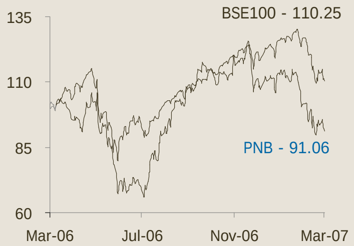
Stock Data

Benchmark	: BSE 100
52 W High Rs.	: 584.90
52 W Low Rs.	: 300.0
Mkt Cap in Crs.	: 13840.0
Face Value	: Rs. 10.0

Absolute Return

%	1m	3m	6m
PNB	-8.49	-16.80	-15.10
BSE 100	-13.18	-12.16	-9.99

Price Comparison



Analyst: Swati Korvi
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Punjab National Bank (PNB), the second largest public sector bank in the country, has a very large network of 4525 branches and 898 ATMs as on Dec 2006, with a major focus on northern and central India. Nearly 60% of the bank's branches are located in semi-urban and rural areas, because of which PNB is one of the best positioned banks in terms of composition of low cost deposits in its total deposit portfolio.

Investment Argument

Business Growth

PNB has posted a robust 26% Y-o-Y growth in business as on December 2006 led by a 23% growth in deposits and 30% growth in advances. The credit deposit ratio as on Dec 06 stood at 67.3%. the bank has been expanding its business cautiously which can be seen in its stable NIMs. High yielding retail, SME and Agriculture loans constituted 53% of the total loan book. Further a 12.9% capital adequacy as on Dec 06 provides enough room to grow.

Superior Margins in the Sector

PNB enjoys one of the best spreads in the sector. The high CASA ratio and rising yield on advances (YoA) has helped maintain high margins for the bank. PNB has raised its PLR twice during the last 2 months from 11.5% to 12.25%. We expect the hike to start reflecting in the yields only in Q1FY08.

However with increasing competition for garnering deposits in the system, resulting in higher interest rates, we believe that the growth in term deposits will be much higher than demand deposits. PNB's CASA ratio has come down from 49% in March 06 to 47% in Dec 06. We expect the cost of deposits (CoD) to move up substantially from the current levels of 4.4% as on Dec 06 due to lower CASA and higher rates.

We estimate the Net Interest Margins (NIM) for the bank to settle at 4.08% for FY07E, which will move down further to 3.96% in FY08E.

Aggressive Provisioning

PNB has always been aggressive on the provisioning front. Gross NPA ratio as on Dec 06 has come down from 4.79% as on Dec 05 to 3.65% as on Dec 06. The net NPA ratio has shown an increase from 0.25% as on Dec 05 and 0.18% as on Sept 06 to 0.42% as on Dec 06. However we expect the net NPA ratio for the year to settle at 0.35% due to increased provisioning.

Contribution from Other Income Stabilising

The subdued performance of other income in the last year has resulted in a 9.7% growth in other income for the 9MFY07 over the corresponding period last year. In the last quarter of FY07, PNB has sold 1% of its holding in National Stock Exchange, i.e. 4.5 lac shares at Rs 2260 per share carrying a face value of Rs 10 per share. This has resulted in a one time income of Rs 101 crs for PNB during the year. We expect the non interest income to register a growth of 11% for FY07. However due to improved yields, the contribution of non interest income to total income will remain low.

Improving Operating Efficiency

The Cost to Income ratio for the 9MFY07 stood at 45.4%, mainly due to a decline in the employee expenses by 10.8% and an increase in the net income by 16% for 9MFY07. During the 9MFY07, provision of Rs 311 crs was made for retirement benefits on an estimated basis.

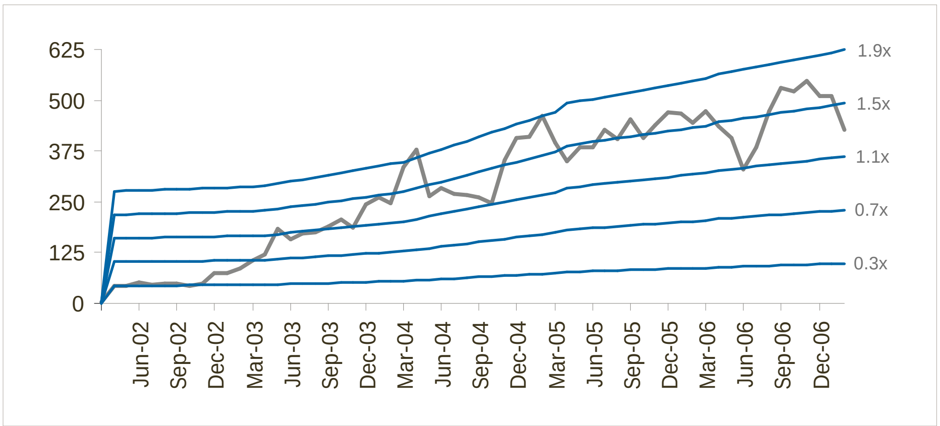
Strong Profitability Growth

After the subdued performance in FY06, we expect an improvement in the profitability and return ratios for the year. We expect the Net Interest Income to rise by a marginal 12% in FY07E due to a surge in the interest expenses. However due to improved contribution of non-interest income and marginal increase in operating expenses, we expect the bank to report a 25% jump in its net profit in FY07E. We expect the net profit to grow by 22% in FY08E. We expect the RoNW and RoAA to improve from 15.35% and 1.06% in FY06 to 16.97% and 1.1% in FY07E respectively.

Outlook and Valuation

With pressure on margins mounting, we believe that PNB is better placed to absorb the narrowing spreads. The bank still operates at comfortable credit deposit ratio, which leaves enough room for growth at selected margins. We expect the bank to grow its balance sheet by 12-13% in FY07E and FY08E translating into a 20%+ growth in net profits in both these years. The recent fall in the market has made PNB an attractive pick at 6.3x FY08E earnings and 1.14x FY08E Price to Book. We upgrade to “Buy” with a target price of Rs 520.

P/B Band



Financials

Income Statement (Rs Crs)			
Year Ended March 31	FY 2006	FY 2007E	FY 2008E
Interest Income	9,584.2	11,092.0	13,437.0
Growth (%)		15.7	21.1
Interest Expense	4,917.4	5,881.7	7,530.4
Growth (%)		19.6	28.0
Net Interest Income	4,666.8	5,210.3	5,906.7
Growth (%)		11.6	13.4
Other Income	1,231.2	1,366.6	1,489.6
Growth (%)		11.0	9.0
Net Revenues	5,897.9	6,576.9	7,396.2
Operating Expense			
-Employee Expense	2,115.0	2,136.1	2,200.2
-Other opex	908.2	978.7	1,057.0
Pre Provision Profit	2,874.8	3,462.0	4,139.0
Provisions	1,435.5	1,656.9	1,932.1
Net Profit	1,439.3	1,805.1	2,206.9
Growth (%)		25.4	22.3

Ratios			
Year Ended March 31	FY 2006	FY 2007E	FY 2008E
Net Interest Margin	4.00%	4.08%	3.96%
Int Income / Total Income	88.62%	89.03%	90.02%
Non-Int Income / Total Income	11.38%	10.97%	9.98%
LCD to Total Deposits	48.99%	47.66%	46.16%
RoNW	15.35%	16.97%	18.11%
RoAA	1.06%	1.10%	1.21%
Int Expended / Int Earned	51.31%	53.03%	56.04%
Cost to Income Ratio	51.26%	47.36%	44.04%
Op Expense / Total Expense	32.24%	29.24%	25.61%
Employee Cost / Op Expense	69.96%	68.58%	67.55%
Credit Deposit Ratio	62.35%	68.53%	71.56%
Investment Deposit Ratio	34.30%	34.00%	33.00%
Net NPAs to Advances	0.28%	0.35%	0.30%
CAR	11.95%	12.50%	11.50%
-Tier 1	10.06%	9.00%	7.00%
-Tier 2	1.89%	3.50%	4.50%

Balance Sheet (Rs Crs)			
Year Ended March 31	FY 2006	FY 2007E	FY 2008E
LIABILITIES			
Equity Capital	315.3	315.3	315.3
Reserves	9,061.1	10,324.7	11,869.5
Networth	9,376.4	10,640.0	12,184.8
Total Deposits	119,684.9	132,850.3	150,120.8
-Savings Deposits	16,723.8	18,061.7	19,506.6
-Current Deposits	41,908.2	45,260.9	49,787.0
-Term Deposits	61,052.9	69,527.7	80,827.2
Borrowings	6,687.2	7,355.9	9,562.7
Other Liabilities	9,601.3	12,991.1	11,196.8
Total	145,349.8	163,837.2	183,065.0
ASSETS			
Loans	74,627.4	91,045.4	107,433.6
Bal with Bank at call and short notice	1,397.1	2,391.3	2,401.9
Investments	41,055.3	45,169.1	49,539.9
Cash / Equiv	23,394.6	19,927.5	18,014.5
Fixed Assets	1,030.2	1,112.6	1,190.5
Other Assets	3,845.2	4,191.3	4,484.6
Total	145,349.8	163,837.2	183,065.0

Valuation Ratios			
Year Ended March 31	FY 2006	FY 2007E	FY 2008E
EPS (Rs)	45.65	57.25	69.99
P/E	9.62	7.67	6.27
BVPS (Rs)	297.38	337.46	386.45
P/B	1.48	1.30	1.14

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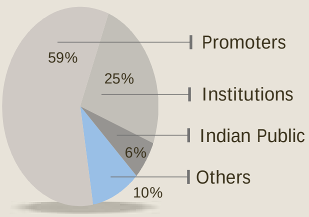
State Bank of India

HOLD | CMP Rs. 980.0

Stock Codes

Bloomberg	: SBIN.IN
Reuters	: SBI.BO
BSE Code	: 500112
NSE Code	: SBIN
BSE Group	: A

Share Holdings
(as on 31st Dec. 06)



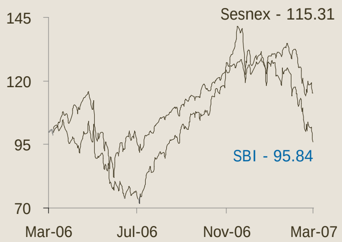
Stock Data

Benchmark	: Sensex
52 W High Rs.	: 1378.0
52 W Low Rs.	: 684.15
Mkt Cap in Crs.	: 51614.0
Face Value	: Rs. 10.0

Absolute Return

%	1m	3m	6m
SBI	-16.29	-27.09	-5.90
Sensex	-10.46	-7.80	5.45

Price Comparison



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ppfas@bloomberg.net

State Bank of India is the largest commercial bank in India, with a balance sheet over Rs 4930 bn. The bank along with its associate banks has a network of 14061 branches with a share of 25% in India's deposits and advances. SBI group with its 71 subsidiaries, joint ventures, associates and RRBs has positioned itself as the largest 'Universal Bank' in the country catering to every segment of financial services ranging from traditional banking products to factoring services, credit cards, mutual funds, life insurance, investment banking, asset reconstruction, etc.

Key Highlights of the 9MFY07 Results

- Net interest income (NII) for 9MFY07 registered a decline of 2.9% over 9MFY06. However excluding the one-time items, the NII has grown by 19%.
- Non-Interest Income rose by 6.3%
- Net Profit of the bank declined by 14% due to flat operating profit and a 14.5% increase in provisioning.
- Business grew by 18% led by a 28% increase in advances and a 11% growth in deposits.

Cautious Growth in Business

The bank has reported a 27% increase in gross advances and a 11% growth in deposits. The bank has been funding its growth by not relying on bulk deposits, which can be seen from a marginal increase in CoDs. The proportion of bulk deposits to total deposits stood at 17% as on Dec 06.

Net Interest Income to Grow Supported by Improving Yields and Containing Costs

Net interest income (NII) for 9MFY07 registered a decline of 2.9% over 9MFY06. However excluding the one-time items, the NII has grown by 19%. The improvement in NII was supported by a 37% increase in interest income on advances led by a 28% increase in advances and a 74 bps hike in YoA. The interest expenses for 9MFY07 grew by a marginal 6.6% over 9MFY06 due to decline in CoD from 4.79% for 9MFY06 to 4.52% for 9MFY07. However 9MFY06 included the cost of India Millennium Deposits (IMD). Excluding IMDs, the CoD for 9MFY06 stood at 4.52% showing a marginal increase in deposit cost for the bank in 9MFY07 over 9MFY06. The improving CASA ratio also helped in containing the CoDs. The deposits have clocked a 11% Y-o-Y growth. The margins have come off from 3.32% in Sept 06 to 3.29% in Dec 06. Going forward we expect the NIMs to stablise with improving yields once the PLR hike of 50 bps gets factored in the lending rates.

Non-Interest Income Growth to Pick up

Fee income for 9MFY07 over 9MFY06 grew by 20%. However due to a flat treasury income and one-time income in 9MFY06, the non-interest income rose by only 6.3%. We expect treasury income to start contributing by FY08E.

Decline in Operating Expenses

We expect the cost to income ratio to increase for FY07E due to a flat Net Income due to lower contribution of other income and increasing interest expenses. However when the rate hikes get factored into the interest income from advances and with stable growth in other income, we expect the cost to income ratio to stabilise to 51.6% in FY08E.

Net Profitability Lower due to Higher Provisioning

The bank's net profit for 9MFY07 declined by 14% due to a marginal decline in operating profit by 2% and a 14.5% increase in provisioning. The bank increased its NPA provisioning from Rs 144.18 crs for 9MFY06 to Rs 698.26 crs for 9MFY07. Provision for depreciation on investment and taxation also remained high. We expect the bank to increase provisioning towards their NPAs, with provisioning requirement for investment depreciation declining.

Improving Asset Quality

Asset quality has shown an improvement from Q3FY06, with Gross NPA and Net NPA ratio declining from 4.41% and 1.67% to 3.30% and 1.45%. In Q3FY07, the bank has significantly increased its provisioning for NPAs. The incremental slippage ratio as on Dec 06 stood at 1.12%. We expect the Gross NPA and Net NPA ratios to come down to 2.9% and 1.2% respectively by FY08E.

Comfortable Capital Adequacy Ratio

As on December 06, the capital adequacy ratio of the bank stood at 11.86%, a decline from the preceding quarter. The Tier I capital adequacy stood at 8%. The bank had raised Rs 6943 crs of upper Tier II subordinated debt during the 9MFY07. Government has also agreed to purchase 59% stake in SBI from RBI. Government is allowed to bring down its stake in a bank to 51% as against 55% by RBI. This should provide enough room to raise Tier I capital. Capital adequacy ratio is expected to remain comfortable.

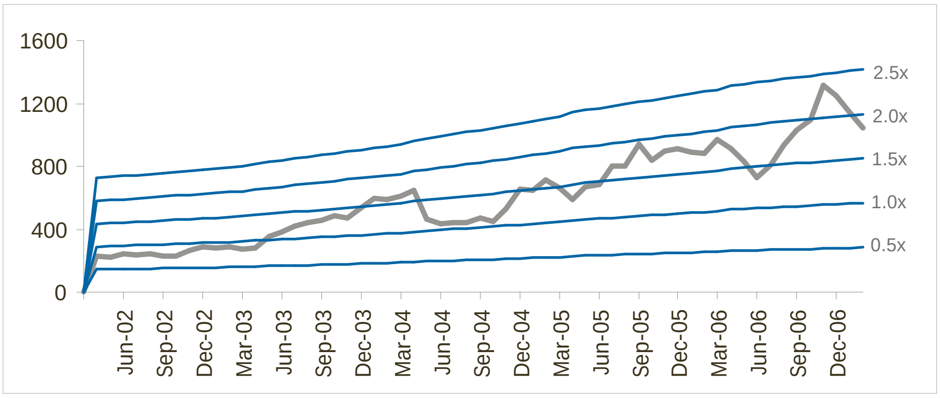
Results on a Consolidated basis for 9MFY07

On a consolidated basis, the interest income and non-interest income registered a growth of 8% and 32% respectively for the 9MFY07 over 9MFY06. However the operating profit grew by a marginal 4.5% due to a 14% increase in interest expenses and operating expenses. A 9% increase in provisioning resulted in a 1.8% dip in the consolidated net profit.

Valuations

The performance of the bank was subdued due to margin pressures and low contribution from non-interest income. However we expect the bank to perform better in FY08E and report an EPS of Rs 94.5. SBI is trading at a P/Ex of 10.4 FY08E and a

P/B Band



Financials

Income Statement (Rs Crs)			
Year Ended March 31	FY 2006	FY 2007E	FY 2008E
Interest Income	35,794.9	39,258.4	48,153.3
Growth (%)		9.7	22.7
Interest Expense	20,159.3	22,908.3	29,294.7
Growth (%)		13.6	27.9
Net Interest Income	15,635.6	16,350.1	18,858.7
Growth (%)		4.6	15.3
Other Income	7,388.7	6,649.8	7,181.8
Growth (%)		(10.0)	8.0
Net Revenues	23,024.3	22,999.9	26,040.5
Operating Expense	11,725.1	12,568.2	13,427.3
-Employee Expense	8,123.0	8,405.3	8,573.9
-Other opex	3,602.1	4,162.9	4,853.4
Pre Provision Profit	11,299.2	10,431.7	12,613.1
Provisions	6,892.6	6,384.8	7,637.6
Net Profit	4,406.7	4,046.9	4,975.5
Growth (%)		(8.2)	22.9

Ratios			
Year Ended March 31	FY 2006	FY 2007E	FY 2008E
Net Interest Margin	3.40%	3.17%	3.10%
Int Income / Total Income	82.89%	85.51%	87.02%
Non-Int Income / Total Income	17.11%	14.49%	12.98%
LCD to Total Deposits	47.55%	45.25%	43.96%
RoNW	15.94%	13.28%	14.65%
RoAA	0.92%	0.76%	0.81%
Int Expended / Int Earned	56.32%	58.35%	60.84%
Cost to Income Ratio	50.92%	54.64%	51.56%
Operating Expense / Total Expense	30.24%	30.02%	26.66%
Employee Cost / Op Expense	69.28%	66.88%	63.85%
Credit Deposit Ratio	68.84%	73.59%	76.13%
Investment Deposit Ratio	42.77%	37.00%	36.00%
Net NPAs to Advances	1.88%	1.42%	1.20%
CAR	11.88%	11.60%	11.50%
-Tier 1	9.36%	7.90%	7.00%
-Tier 2	2.52%	3.70%	4.50%

Balance Sheet (Rs Crs)			
Year Ended March 31	FY 2006	FY 2007E	FY 2008E
LIABILITIES			
Equity Capital	526.3	526.3	526.3
Reserves	27,117.8	29,950.6	33,433.5
Networth	27,644.1	30,476.9	33,959.8
Total Deposits	380,046.1	440,853.4	511,390.0
-Savings Deposits	67,995.7	75,475.2	85,286.9
-Current Deposits	112,723.9	123,996.3	139,495.9
-Term Deposits	199,326.5	241,381.9	286,607.2
Borrowings	30,641.2	36,769.5	42,284.9
Other Liabilities	55,538.2	60,222.1	78,474.6
Total	493,869.6	568,321.9	666,109.3
ASSETS			
Loans	261,641.5	324,435.5	389,322.6
Bal with Bank at call and short notice	22,907.3	28,655.5	35,797.3
Investments	162,534.2	163,115.8	184,100.4
Cash / Equiv	21,652.7	26,451.2	30,683.4
Fixed Assets	2,752.9	2,835.5	2,920.6
Other Assets	22,380.8	22,828.5	23,285.0
Total	493,869.6	568,321.9	666,109.3

Valuation Ratios			
Year Ended March 31	FY 2006	FY 2007E	FY 2008E
EPS (Rs)	83.73	76.89	94.54
P/E	11.71	12.75	10.37
BVPS (Rs)	525.25	579.08	645.26
P/B	1.87	1.69	1.52

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Investment Research

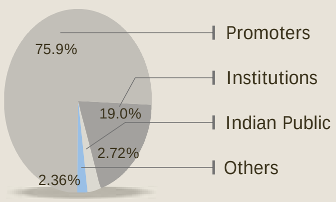
Bharat Electronics Limited

BUY | CMP Rs. 1511.20

Stock Codes

Bloomberg	: BHE.IN
Reuters	: BAJE.BO
BSE Code	: 500049
NSE Code	: BEL
BSE Group	: A

Share Holdings
(as on 31st Dec. 06)



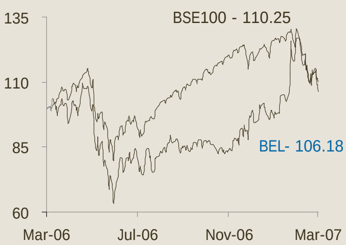
Stock Data

Benchmark	: BSE 100
52 W High Rs.	: 1794.0
52 W Low Rs.	: 815.0
Mkt Cap in Crs.	: 12089.0
Face Value	: Rs. 10.0

Absolute Return

%	1m	3m	6m
BEL	-10.90	12.90	28.33
BSE 100	-13.18	-12.16	-9.99

Price Comparison



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Bharat Electronics Limited (BEL) is a leading Indian defence electronics company with around 95 per cent of the market share for strategic electronics in India. Established in 1954, BEL manufactures a wide range of cutting-edge Military Communication Systems, Radars and Sonars, Naval Systems, Telecom & Broadcast Systems, Electronic Warfare Systems, Tank Electronics, Opto Electronics, Professional Electronic Components and Solar Powered Systems. The Company has been using the technologies and skills acquired over the years to design a number of civilian products such as Electronic Voting Machines, Set Top Boxes, etc. BEL is one of the select PSUs signing the MoU with the Department of Defence Production ever since the Government of India introduced this performance measurement system in 1989-90. The Company has achieved MoU rating of 'Excellent' for the past 8 consecutive years.

Key Investment attributes

- Excellent relationship based strategic position and a Quasi Monopoly business
- A Non cyclical and Low Capital intensiveness business
- Excellent RONWs of 25%+ and ROICs of 100% +
- Good revenue visibility due to high indigenisation level targets for defence expenditure
- Target of being a Rs. 5000 Cr company in 2008 and Rs. 10,000 Cr company by 2012 implying a compounded growth rate of 19% over the next five years
- Steady Order Book to Sales ratio of ~2x for the past five years

Post Budget Outlook Intact

The budget outlay for the next financial year at Rs. 96,000 Crs represent a decent 11.63% increase over the revised estimate of Rs. 86,000 for 2006-07. Last year there was a shortfall to the tune of Rs. 3,000 Crs on the initial annual estimate of Rs. 89,000 Crs. More importantly, the increasing trend of capital outlay has been continued and would benefit key players like BEL. The capital outlay has been pegged at 43.7% as compared to 42.1% last year. The capital spending has steadily increased from 26.6% in FY03 to over 43% in FY08E.

Summary Financials

Particulars (Rs Crs)	2004	2005	2006	2007 E	2008 E
Net Revenues	2,736.2	3,182.2	3,560.8	3,965.8	4,759.0
Net Profit	316.0	446.3	581.0	676.2	794.2
EPS (Rs.)	39.5	55.8	72.6	84.5	99.3
ROCE %	37.2	43.4	42.7	38.4	36.0
RONW %	28.0	29.2	28.5	25.8	24.1
P/E (x)	38.3	27.1	20.8	17.9	15.2
P/BV (x)	9.68	7.59	5.92	4.61	3.67

Introduction

Bharat Electronics Limited (BEL) is a leading Indian defence electronics company with around 95 per cent of the market share for strategic electronics in India. Established in 1954, BEL manufactures a wide range of cutting-edge Military Communication Systems, Radars and Sonars, Naval Systems, Telecom & Broadcast Systems, Electronic Warfare Systems, Tank Electronics, Opto Electronics, Professional Electronic Components and Solar Powered Systems. The Company has been using the technologies and skills acquired over the years to design a number of civilian products such as Electronic Voting Machines, Set Top Boxes, etc. BEL is one of the select PSUs signing the MoU with the Department of Defence Production ever since the Government of India introduced this performance measurement system in 1989-90. The Company has achieved MoU rating of 'Excellent' for the past 8 consecutive years.

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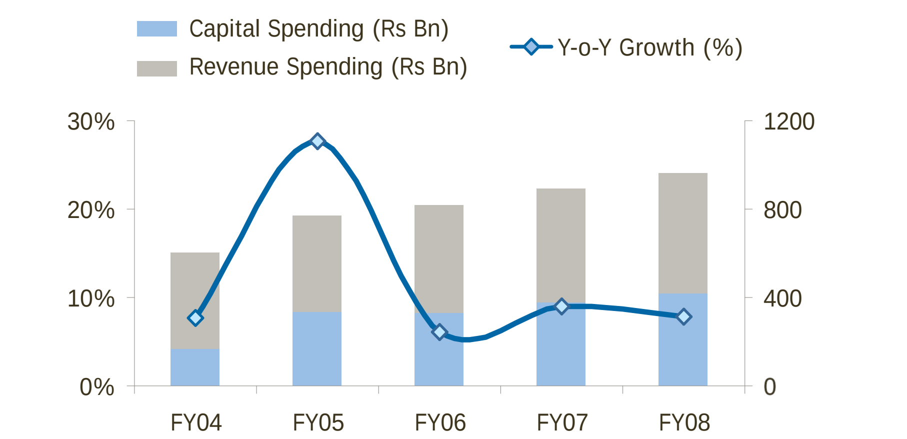
	2003	2004	2005	2006	2007E
Sales (Rs Crs)	2,465.0	2,736.0	3,182.0	3,561.0	3,965.8
Order Book (Rs Crs)	6,944.0	6,740.0	6,108.0	6,633.0	7330.0*
Order Book/Sales Ratio (x)	2.8	2.5	1.9	1.9	1.8

* Order Book as on December 06

Post Budget Outlook Intact

The budget outlay for the next financial year at Rs. 96,000 Crs represent a decent 11.63% increase over the revised estimate of Rs. 86,000 for 2006-07. Last year there was a shortfall to the tune of Rs. 3,000 Crs on the initial annual estimate of Rs. 89,000 Crs. More importantly, the increasing trend of capital outlay has been continued and would benefit key players like BEL. The capital outlay has been pegged at 43.7% as compared to 42.1% last year. The capital spending has steadily increased from 26.6% in FY03 to over 43% in FY08E.

India's Defence Spend



Aero India 2007 – Participation Outcome

BEL participated in the Aero India 2007 show held between February 07-11 at the Yelahanka Air Force Station in Bangalore. Highlighted below are the three important deals signed by this Indian defence major.

Bharat Electronics signed 2 MoUs on Day 1 of Aero India 2007. BEL signed an MoU with Elbit Systems Electro Optics ELOP Ltd, Israel, for selling up a Joint Venture Company (JVC) for co-operation in the development, production and marketing of Thermal Imaging Cameras and Forward Looking Infra Red (FLIRs) for the Indian and global markets. The JVC will develop and market products. The products will be manufactured by the Company and ELOP. BEL also gave a Letter of Intent to Elbit for manufacture of Tactical Computers and Elbit gave Supply Order worth approximately US $ 0.45 million to the Company for Gun Display Unit and other accessories required for Ireland. BEL also signed an MoU with Northrop Grumman Corporation on the same day.

During the show, BEL and Lockheed Martin signed an MoU to explore business opportunities on potential co-production opportunities in support of the Indian government's current and future aerospace and defence electronics requirements as well as Lockheed Martin's international market requirements. Headquartered in Bethesda, Maryland, USA, Lockheed Martin employs about 140,000 people worldwide and is principally engaged in the research, design, development, manufacture, integration and sustainment of advanced technology systems, products and services. The Corporation reported 2006 sales of $39.6 billion.

Outlook

For the fourth quarter, we have estimated a net profit of Rs. 3,195 Mn. to be achieved on a topline of Rs. 17,846 Mn. including exports to the tune of Rs. 1,100 Mn. We perceive that our targets for the coming years should be met comfortably.

Increasing share of civilian contracts :

In the last quarter, BEL has bagged a prestigious order for supply of 2,00,000 nos. of Set Top Boxes (STB) from M/s. Wire & Wireless Ltd. of Zee Group. The supplies would be matched with the Conditional Access (CAS) roll out scheduled for January 2007. BEL also manufactures DTH & DTT varieties. Products like STBs & Voting Machines are expected to increase the civilian product sales in the coming quarters.

Indigenisation policy :

As per the new Offset policy of the defence sector, for every capital order of Rs.3,000 Mn. and above, to any foreign companies/ contractors, they will have to import goods from India to the tune of 30% of the worth of the order received by them. A guidance released by the defence ministry indicates that in the 11th plan period (2007-2012), the offset clause can lead to a demand to the tune of USD 10 Bn. The positive impact of this on BEL is reflected in the fact that its revenues from indigenously developed products has increased from 63% to 73% in a year's timeframe.

Targeting Exports business :

Export business, though an extremely small fraction of the total revenues is set to grow at an exponential rate. BEL is setting up a new manufacturing unit for super components and an assembly unit for electronic circuit boards (ECBs) for contract manufacturing for exports market. Earlier in this report, we referred to the various MOUs signed with the international defence companies.

Q307 Performance Review

Bharat Electronics Limited has a track record of reporting erratic earnings on a quarterly basis. This is largely due to the high share of defence business (over 80 % of the revenues), where the earnings are highly skewed in the last quarter (need to exhaust the budgetary allocation targets). Despite the quarterly lumpiness, BEL has grown its revenues at 16% CAGR for the past five years. In the current fiscal, the 28% increase in Q3 revenues has compensated for the absolutely flat performance in the first two quarters.

Result Highlights

- Net Revenues up 27.5% at Rs. 8,638 Mn.
- RM costs increase but Staff & Other expenditure lower; OPM up 150 bps
- EBITDA at 28.5% higher by 300 bps
- PAT up 53% at Rs. 1,482 Mn.
- NPM at 17.2% v/s. 14.3% in Q3FY06

Quarterly Financials

(Rs. Crs)	Dec 06	Sept 06	Q-Q (%)	Dec 05	Y-Y (%)	9M FY07
Net Sales	863.8	834.3	3.5%	677.2	27.5%	2,181.2
Total Expenditure	666.2	647.7	2.8%	532.6	25.1%	1,724.9
Operating Profit	197.6	186.5	6.0%	144.7	36.6%	456.3
Other Income	40.7	50.8	-19.9%	21.7	87.5%	129.9
EBITDA	238.4	237.4	0.4%	166.4	43.3%	586.2
Depreciation	20.5	19.8	3.3%	18.1	13.0%	61.1
PBIT	217.9	217.6	0.2%	148.3	47.0%	525.1
Interest	0.2	0.1	114.3%	1.3	-88.5%	0.5
PBT	217.7	217.5	0.1%	147.0	48.2%	524.6
Tax	69.6	69.2	0.5%	49.9	39.3%	167.9
PAT	148.2	148.3	-0.1%	97.0	52.7%	356.7
Reported PAT	148.2	148.3	-0.1%	97.0	52.7%	356.7
Equity Capital	80.0	80.0		80.0		80.0
EPS (in Rs.)	18.5	18.5		12.1		44.6
Earnings Analysis	**Dec 06**	**Sept 06**	**Q-Q (bps)**	**Dec 05**	**Y-Y (bps)**	**9M FY07**
Profitability						
OPM %	22.9%	22.4%	52.1	21.4%	152.1	20.9%
EBITDA %	27.6%	28.5%	(85.9)	24.6%	302.8	26.9%
PBIT %	25.2%	26.1%	(85.3)	21.9%	333.4	24.1%
PAT %	17.2%	17.8%	(62.0)	14.3%	283.0	16.4%
Operational Parameters						
RM Consumed	53.0%	54.9%	(185.2)	46.8%	622.8	53.6%
Staff Cost	12.8%	13.9%	(110.4)	15.5%	(263.9)	15.5%
Other Expenditure	11.3%	8.8%	243.4	16.4%	(511.0)	9.9%

Yearly Financials

(Rs. Mn)	FY 05	FY 06	FY 07E	FY 08E
Net Sales	3,182.2	3,560.8	3,965.8	4,759.0
Total Expenditure	2,558.4	2,718.4	3,043.4	3,613.8
Operating Profit	623.8	842.4	922.5	1,145.2
Other Income	122.3	110.8	173.2	140.0
EBITDA	746.1	953.2	1,095.7	1,285.2
Depreciation	71.5	77.8	85.6	96.0
PBIT	674.6	875.4	1,010.1	1,189.2
Interest	11.6	27.3	15.0	15.0
PBT	663.1	848.1	995.2	1,174.2
Tax	216.8	266.9	318.9	380.0
PAT	446.3	581.2	676.2	794.2
Equity Capital	80.0	80.0	80.0	80.0
EPS (in Rs.)	55.8	72.6	84.5	99.3
(Rs. Mn)	FY 05	FY 06	FY 07E	FY 08E
Profitability				
OPM %	19.6%	23.7%	23.3%	24.1%
EBITDA %	23.4%	26.8%	27.6%	27.0%
PBIT %	21.2%	24.6%	25.5%	25.0%
PAT %	14.0%	16.3%	17.1%	16.7%
Operational Parameters				
RM Consumed	49.1%	55.4%	61.5%	73.8%
Staff Cost	12.4%	11.9%	12.9%	15.1%
Other Expenditure	10.3%	9.0%	11.1%	12.6%

Summary Financials

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Investment Research

PPFAS

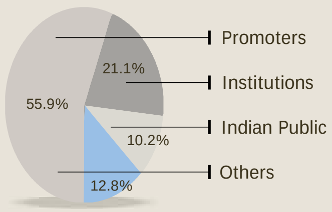
Britannia Industries Limited

ACCUMULATE | CMP Rs. 1281.50

Stock Codes

Bloomberg	: BRIT.IN
Reuters	: BRIT.BO
BSE Code	: 500825
NSE Code	: BRITANNIA
BSE Group	: A

Share Holdings
(as on 31st Dec. 06)



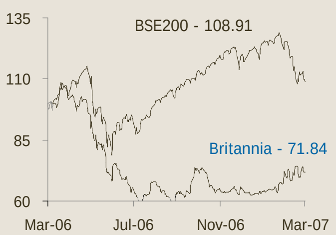
Stock Data

Benchmark	: BSE 200
52 W High Rs.	: 1955.0
52 W Low Rs.	: 1025.0
Mkt Cap in Mn.	: 30603.0
Face Value	: Rs. 10.0

Absolute Return

%	1m	3m	6m
Britannia	13.09	-35.55	-12.44
BSE 200	-13.10	-12.11	-9.97

Price Comparison



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Britannia Industries Limited (BIL) is a market leader in the biscuit and bakery products segment with over 38 per cent market share. It is promoted by Nusli Wadia group and Groupe Danone, French food and beverages giant. The company's main biscuit brands include Good Day, Tiger, 50:50, Treat, Milk Bikis and Marie Gold. Britannia mainly caters to the premium segment. However, with the launch of Tiger brand, it has dived into the low-end category, taking competition head on with Parle which is the leader in this segment. The company has also diversified within the bakery products and entered the bread, cakes and rusks markets.

Summary Financials

P & L (Rs Mn)	Mar 04	Mar 05	Mar 06	Mar 07A	Mar 08E	Mar 09E
Net Sales	14,396.13	15,095.48	17,133.38	21,196.33	24,780.56	28,839.81
EBIDTA	2,150.88	2,631.31	2,195.66	1,612.33	2,531.56	3,599.81
PAT	1,091.09	1,487.70	1,464.26	1,031.93	1,520.56	2,282.81
RoE	25.31	33.54	26.67	17.95	24.41	34.38
RoCE	40.98	54.30	35.43	23.12	35.30	47.55
EV/EBIDTA	7.09	7.98	19.29	18.78	11.96	8.33
EV/Sales	1.06	1.39	2.47	1.43	1.22	1.04

Investment Arguments

Excellent Growth Rates

"We have grown at a rate of 25 per cent in the last three quarters. BIL grew at 85 per cent in rural areas last year, while in modern format stores its growth rate has been 100%" says CEO Vinita Bali. BIL has identified six "pillar brands" to power its growth. Each of these brands viz. Good Day, Tiger, 50:50, Treat, Milk Bikis and Marie Gold have witnessed double-digit growth. Demand for biscuits is expected to be driven by rising disposable incomes in the robustly growing Indian economy. We expect BIL to grow at 23 per cent in FY07 and at 17 and 16 per cent in FY08 and FY09 respectively.

Capacity Additions

BIL has decided to invest Rs175-200 Crs over the next two to three years to expand production capacity by nearly 40 per cent. The expansion project will be funded through a mix of internal accruals and borrowings. The company's average after tax profit is around Rs 120 Crs in the last three years and has reserves of over Rs 500 Crs. Therefore borrowings will not significantly hamper the current debt equity ratio.

Favorable budget

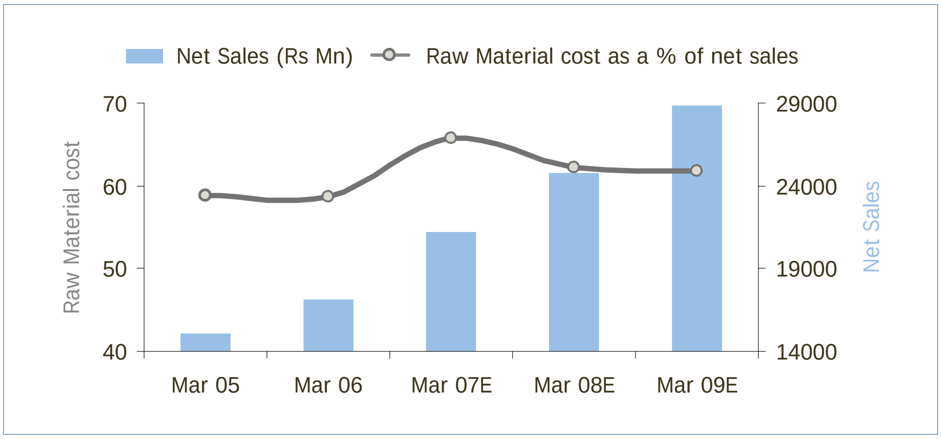
Low cost biscuits are now exempted from excise duty. This will have a direct impact on Britannia as "Tiger" brand accounts for 30 per cent of its revenue. The reduction of import duty of edible oil will also help Britannia.

Indirect price hike

BIL have reduced the size of 100 gram biscuit packet to 90 grams by taking out one biscuit from the pack whilst maintaining the same price.

Stabilization of raw material prices

FY07 was an exceptional year as far as the raw material prices were concerned. Cost of raw-materials as a percentage of sales shot up from 58 per cent in 2006 to over 65 per cent. This is expected to come down on the back of good wheat production and lower sugar prices. We expect this figure to fall and hover around 62 per cent during FY08 and FY09. Crude oil prices now stabilizing will also act as a sweetener.



Acquisition spree

BIL acquired Daily Breads to strengthen its presence in the freshly baked gourmet food market. DB has eight outlets in Bangalore and BIL plans to set up new outlets in Mumbai and Delhi and also opening counters at leading convenience stores. It has also acquired a company in the middle east.

Risk Factors

Dispute between the management

Dispute between Wadia Group and Group Danone began with the ownership of the "Tiger" brand. The matter worsen when Nusli Wadia filed a complaint with the government on the French group's investment in the bio-actives manufacturer Avesthagen, alleging violation of the joint venture. The settlement is nowhere in sight

ITC's foray into biscuits

Sunfeast has about 8 per cent market share in the biscuit market. Its aggressive marketing and attractive pricing pose a threat to Britannia in the long run. It also has more number of variants than BIL.

Threat from regional players

Regional players have a strong presence in the local market. Their manufacturing facilities are closer to their markets and have a superior distribution system. This makes it difficult for any national player to penetrate into these markets.

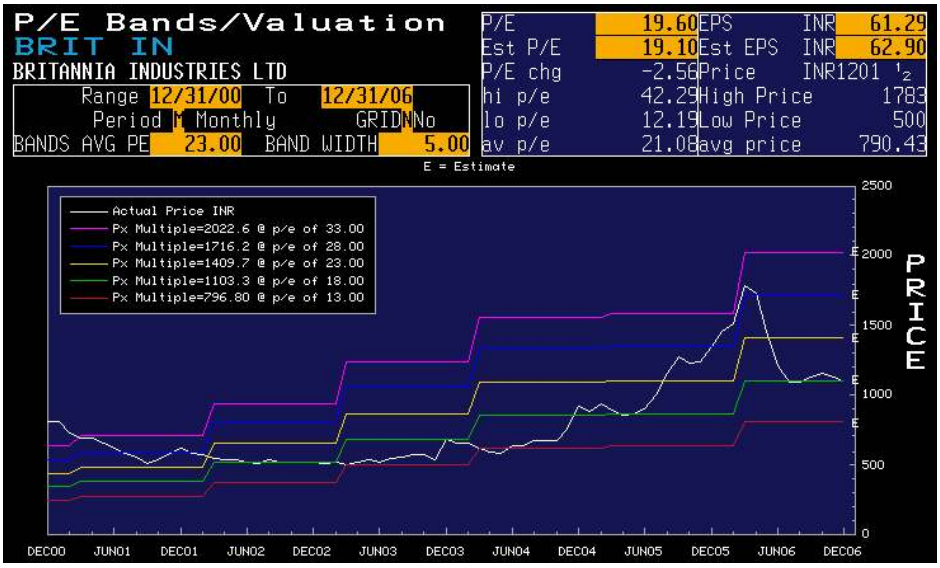
Valuation

The stock is trading currently at P/E of 20.13x FY08 and 13.41x FY09 and M Cap / Sales of 1.24 and 1.06 for the same period. This is after considering the additional growth prospects as a result of capacity additions. Moreover, it has been trading at an average PE of 23x since 2000.

Despite the risk factors BIL have achieved a growth of 25 per cent for the 9 months ended December06. We expect the revenue to grow at 23 per cent for FY07. However, reduced margins will shrink PAT by over 20 per cent and EPS by over 30 per cent in the current year. This dip might see a correction in the stock price but will not be substantial. We expect the revenue to grow at 17 per cent and 16 per cent in FY08 and FY09 as a result of increased capacity additions. This coupled with stable raw material prices will lead to a jump in EPS by 45 per cent and 33 per cent respectively for the same period.

Particulars	Mar 04	Mar 05	Mar 06	Mar 07E	Mar 08E	Mar 09E
EPS	45.67	62.27	61.29	43.20	63.65	95.55
P/E	13.68	14.19	29.10	29.67	20.13	13.41
P/B	3.46	4.76	7.76	5.33	4.91	4.61

PE Band



Quarterly Financials

Profit and Loss Account (Rs Mn)	9 mths ended Dec2005	9 mths ended Dec2006	% Change
Gross Sales	13,389.00	16,876.00	26.04
Excise Duty (Net)	207.00	878.00	324.15
Net Sales	13,182.00	15,998.00	21.36
Other Income	95.00	196.00	106.32
Total Income	13,277.00	16,194.00	21.97
EXPENDITURE			
Consumption of Materials	7,299.00	10,313.00	41.29
% of net sales	55.37	64.46	
Salaries, Wages, Bonus, Commission etc	534.00	539.00	0.94
% of net sales	4.05	3.37	
Other Expenses	3,582.00	4,271.00	19.24
% of net sales	27.17	26.70	
Total Expenses	11,415.00	15,123.00	32.48
% of net sales	259.71	283.41	
EBIDTA	1,862.00	1,071.00	(42.48)
% of net sales	14.13	6.69	
Depreciation & Amortization	160.00	186.00	16.25
EBIT	1,702.00	885.00	(48.00)
% of net sales	12.91	5.53	
Interest	28.00	46.00	
PBT	1,674.00	839.00	(49.88)
% of net sales	38.13	16.10	
Taxes	488.00	74.00	(84.84)
PAT	1,186.00	765.00	(35.50)
% of net sales	26.96	14.63	
Exceptional items		86.00	
PAT after exceptional items	1,186.00	679.00	(42.75)
% of net sales	27.04	13.02	
Equity Capital	23.90	23.90	
Diluted EPS – before exceptional items	49.62	28.41	
Diluted EPS – after exceptional items	49.62	32.01	

Financials

P&L (Rs Mn)	Mar 06	Mar 07A	Mar 08E	Mar 09E
Gross Sales	18,179.2	22,501.3	26,326.6	30,538.8
Excise Duty (Net)	1,045.8	1,305.0	1,546.0	1,699.0
Net Sales	17,133.4	21,196.3	24,780.6	28,839.8
Other Income	216.8	241.0	120.0	189.0
Total Income	17,350.2	21,437.3	24,900.6	29,028.8
EXPENDITURE				
Raw Materials Consumed	10,049.6	13,938.0	15,434.0	17,810.0
Employee Expenditure	730.7	724.0	1,010.0	1,109.0
Other Expenses	4,374.3	5,163.0	5,925.0	6,510.0
Total Expenses	15,154.6	19,825.0	22,369.0	25,429.0
EBIDTA	2,195.7	1,612.3	2,531.6	3,599.8
Depre. & Amortization	217.2	249.0	280.0	376.0
EBIT	1,978.4	1,363.3	2,251.6	3,223.8
Interest	20.1	29.4	31.0	76.0
PBT	1,958.4	1,333.9	2,220.6	3,147.8
Taxes	542.9	250.0	480.0	667.0
PAT	1,415.5	1,083.9	1,740.6	2,480.8
Exceptional items	(48.8)	52.0	220.0	198.0
PAT after EI	1,464.3	1,031.9	1,520.6	2,282.8

Ratios	Mar 06	Mar 07A	Mar 08E	Mar 09E
Diluted EPS – before EI	59.25	45.37	72.86	103.84
Diluted EPS – after EI	61.29	43.20	63.65	95.55
Cash EPS	70.38	53.62	75.37	111.29
EBIDTA	12.82	7.61	10.22	12.48
EBIT	11.55	6.43	9.09	11.18
PAT – before EI	8.26	5.11	7.02	8.60
PAT – after EI	8.55	4.87	6.14	7.92
RoE – after EI	26.67	17.95	24.41	34.38
Before EI	25.78	18.85	27.94	37.36
RoCE	35.43	23.12	35.30	47.55
Debt / Equity	0.02	0.03	0.02	0.02
Current Ratio	1.11	1.10	1.05	1.10
Asset Turnover	5.43	5.90	6.36	6.86
Debtors Ratio	4.44	3.41	4.43	5.05
EV/EBIDTA	19.29	18.78	11.96	8.33
EV/Sales	2.47	1.43	1.22	1.04
Market Cap/Sales	2.49	1.44	1.24	1.06

Balance Sheet (Rs Mn	Mar 06	Mar 07A	Mar 08E	Mar 09E
SOURCE OF FUNDS				
Shareholders' Funds				
Capital	238.9	239.0	239.0	239.0
Reserves and Surplus	5,252.0	5,510.0	5,990.0	6,401.0
Total Shareholders' Funds	5,490.9	5,749.0	6,229.0	6,640.0
Loan Funds				
Secured	16.2	28.0	25.0	19.0
Unsecured	77.4	120.0	125.0	121.0
	93.6	148.0	150.0	140.0
Capital Employed	5,584.5	5,897.0	6,379.0	6,780.0
Deferred Tax Liability	16.9	28.0	26.0	20.0
	5,601.4	5,925.0	6,405.0	6,800.0
APPLICATION OF FUNDS				
Fixed Assets				
Gross Block	3,153.7	3,590.0	3,899.0	4,201.0
Less: Depre. & Amortization	1,748.1	2,045.0	2,222.0	2,393.0
Net Block	1,405.6	1,545.0	1,677.0	1,808.0
Capital Work-in-Progress	110.8	124.0	205.0	190.0
	1,516.4	1,669.0	1,882.0	1,998.0
Investments	3,598.6	3,701.0	4,010.0	4,000.0
Deferred Tax Assets				
Current Assets, Loans and Advances				
Inventories	1,848.0	2,011.0	2,205.0	2,359.0
Sundry Debtors	208.5	198.0	301.0	399.0
Cash and Bank Balances	353.4	491.0	494.0	753.0
Other Current Assets	5.6	5.0	4.0	10.0
Loans and Advances	940.7	890.0	969.0	911.0
	3,356.1	3,595.0	3,973.0	4,432.0
Less:				
CURRENT LIABIALITIES AND PROVISIONS				
Liabilities	2,247.0	2,591.0	3,010.0	3,211.0
Provisions	783.3	690.0	761.0	810.0
	3,030.3	3,281.0	3,771.0	4,021.0
Net Current Assets	325.8	314.0	202.0	411.0
Misc. Expenditure (written off)	160.6	241.0	311.0	391.0
	5,601.4	5,925.0	6,405.0	6,800.0

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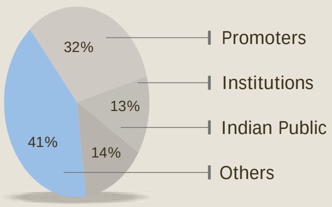
VST Industries Limited

BUY | CMP Rs. 331.0

Stock Codes

Bloomberg	: VST.IN
Reuters	: VSTI.BO
BSE Code	: 509966
NSE Code	: VSTIND
BSE Group	: B1

Share Holdings
(as on 31st Dec. 06)



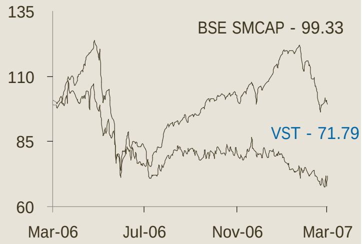
Stock Data

Benchmark	: BSE Small Cap
52 W High Rs.	: 554.4
52 W Low Rs.	: 345.0
Mkt Cap in Mn.	: 5640.
Face Value	: Rs. 10.0

Absolute Return

%	1m	3m	6m
VST	-9.97	24.47	29.21
BSE SMCAP	-14.24	-12.65	-10.52

Price Comparison



Analyst: Sandeep Elamon
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ppfas@bloomberg.net

VST Industries witnessed sluggish growth in the last quarter with its net sales crawling to Rs 808 million. Its OPM was down by 125 basis points and PAT margin down by 205 basis points. This was primarily because of increase in staff cost by over 80 per cent. The company paid Rs 92.50 million to its employees under Voluntary Retirement Scheme for the quarter as well as for the nine months ended 31 December 2006. The dip in margins is not a cause of much concern as the VRS will help reduce the operating costs going forward.

Price Hike

Price of Charminar brand of cigarette was increased by 10% in November 2006. Full impact of this hike will be seen in the current quarter.

Price Hike in Bidis to benefit

VST mainly caters to low end segment or micro cigarettes which competes directly with bidis. Increase in cess in Bidis in this budget will will witness customers switching to cigarettes. VST will be a direct beneficiary of this hike.

Dividend Payout

VST has been consistently paying dividends of over 40 per cent in the last 5 years and 125 per cent in the last 2 years. With the improvement in operational efficiencies, cash flows are expected to be strong and we expect this trend to continue going forward.

Pictorial Warning

Pictorial warning on the cigarette carton is to be implemented from 1st February 2007. Statuary warning along with the picture of a skull and a bone will now occupy half the area of the cigarette box. This will increase the packaging cost by 2 per cent.

Valuation & Our Recommendation

We rate VST Industries as a defensive pick. Cigarette industry is growing at 5 – 6 per cent per annum (volume) and we expect VST to move at this pace. In the absence of any formal promotional efforts, selling and administrative expenses will continue to be on the lower side. With improved efficiencies on the back of maintenance and up gradation of capital expenditure, company earnings are expected to jump significantly from the current level.

PAT for the TTM ended December '06 increases by Rs 100 million when adjusted for one-off expenses such as VRS and "prior-period" excise duty paid to certain north-eastern states. Thus, at the CMP of Rs 331/-, it is selling at a P/E of 10.72 of TTM with an EPS of Rs 30.89. We recommend a long term buy as the company's per share intrinsic net-worth will keep on increasing and a high RoE will improve the valuations.

Financials

Profit and Loss Account (Rs Mn)	QE Dec 05	QE Dec 06	% change	9mths ending Dec 05	9 mths ending Dec 06	% change
Net Sales	728.10	808.00	10.97	2,295.90	2,413.30	5.11
Other Income	68.60	33.10		110.00	100.30	
Total Income	796.70	841.10	5.57	2,405.90	2,513.60	4.48
EXPENDITURE						
Consumption of Materials	241.70	216.60	(10.38)	815.60	721.80	(11.50)
Salaries, Wages, Bonus, Commission etc	86.10	194.60	126.02	273.70	415.20	51.70
Other Expenses	122.30	233.90	91.25	453.60	709.50	56.42
Total Expenses	450.10	645.10	43.32	1,542.90	1,846.50	19.68
EBIDTA	346.60	196.00	(43.45)	863.00	667.10	(22.70)
Depreciation & Amortization	26.20	29.20		77.30	86.20	
EBIT	320.40	166.80	(47.94)	785.70	580.90	(26.07)
Interest	(4.80)	(1.80)		(14.40)	(8.00)	
PBT	325.20	168.60	(48.15)	800.10	588.90	(26.40)
Taxes	96.30	57.70		260.90	188.50	
PAT	228.90	110.90	(51.55)	539.20	400.40	(25.74)
Exceptional items	147.80			287.10		
PAT after exceptional items	81.10	110.90	36.74	252.10	400.40	58.83
Equity	15.44	15.44		15.44	15.44	
Diluted EPS – before exceptional items	14.83	7.18		34.92	25.93	
Diluted EPS – after exceptional items	5.25	7.18		16.33	25.93	
Margins						
OPM	47.60	24.26		37.59	27.64	
NPM – before exceptional items	31.44	13.73		23.49	16.59	
NPM – after exceptional items	11.14	13.73		10.98	16.59	

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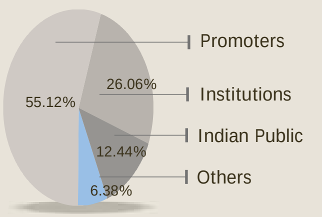
Matrix Laboratories Limited

BUY | CMP Rs. 160.0

Stock Codes

Bloomberg	: HDPH.IN
Reuters	: HERE.BO
BSE Code	: 524794
NSE Code	: MATRIXLABS
BSE Group	: B1

Share Holdings
(as on 31st Dec. 06)



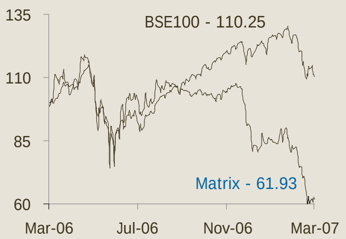
Stock Data

Benchmark	: BSE 100
52 W High Rs.	: 312.80
52 W Low Rs.	: 184.0
Mkt Cap in Mn.	: 34106.0
Face Value	: Rs. 2.0

Absolute Return

%	1m	3m	6m
Matrix	-24.60	-31.63	-40.49
BSE 100	-13.18	-12.16	-9.99

Price Comparison



Analyst: Urmil Negandhi
Ph: 2284 6555 | urmil@ppfas.com
ppfas@bloomberg.net

Matrix reported net loss of Rs.8.74 mn in its Q3FY07 results compared to profit of Rs.1004.83 mn last year. The company reported net profit of Rs.488 mn for the 9 months ending on 31st December 2006 compared to Rs.1700 mn last year same period. The result for the quarter and nine months ended 31st December 2006 are not comparable with the current periods due to acquisitions made by the Matrix at different points of time during last year.

- The company reported quarterly net sales of Rs.3953 mn compared to Rs.3731.78 mn last quarter. The net sales increased by 6% on Q-o-Q basis. Total net sales were Rs.12106 mn for nine months ended 31st December 2006 compared to Rs. 7797 mn last year for the same period i.e. increase of 55% on YTD basis.

- Total expenditure increased by 10% on Q-o-Q basis to Rs.3468 mn from Rs.3162 mn. Total expenditure increased by 55% on YTD basis compared to last year. As a result, operating margin witnessed decline of around 300 basis points on Q-o-Q basis. But on YTD basis we saw marginal improvement in the same. The main constituent of increase in total expenditure were Other Expenses, R&D expenses and Employee costs.

  - Raw material cost increased by around 9% on Q-o-Q basis from Rs.2017 mn to Rs.2200 mn and 47% on YTD basis from Rs.4612 mn to Rs.6796 mn.

  - Employee cost increased by 106% on YTD basis from Rs.667 mn to Rs.1376 mn. This rise is mainly on account of acquisition of Docpharma(Belgium), Concord Biotech India and Mchem Group (China) last year. Though there is decline of 5% on Q-o-Q basis.

  - Other expenses saw increase of 22% on Q-o-Q basis from Rs.672 mn to Rs.821 mn and 57% on YTD basis from Rs.1382 mn to Rs.2168 mn. This increase of around Rs.140 mn compared to last quarter was mainly on account of Docpharma's foray into lucrative markets like France and Italy. This is mainly one time expenditure relating to marketing and legislation expenses while foraying in other countries. Management is of the view that it is unlikely to have such expenses in coming quarters. Management expects stream of revenue flowing in coming quarters because of this expansion and foray into lucrative European markets.

  - Research & Development expenses have increased by almost 16% on Q-o-Q basis from Rs.226 mn to Rs.262 mn and 170% on YTD basis from Rs. 246 mn to Rs. 666 mn .This can be regarded as positive development from the long term point of view. Management has already filed 10 ANDAs and DMFs till date. They have plan to take ANDAs filing number to 25 by this year end.

- Other Income saw decline of about 70% on YTD basis from Rs.1512 mn to Rs.463 mn. This is on account of one time income the company had last year because of transfer of one of its Active Pharmaceutical Ingredients (APIs) manufacturing facilities, technology and Intellectual Property (IP) related to the manufacture of certain APIs to Astrix Laboratories Limited. (Astrix - an Indian joint venture company with Aspen Pharmacare Holdings Limited, South Africa) for a total consideration of US $ 36 million. Though there was an increase in other income by 52% on Q-o-Q basis.

- Interest expenses has seen increase of 5% on Q-o-Q basis from Rs.195 mn to Rs. 204 mn and around 300% increase on YTD basis from Rs.138 mn to Rs.555 mn. This is mainly on account of Euro 165 mn debt taken to acquire Docpharma (Belgium).This expenditure is likely to reduce by H1FY08 as half of that debt will be repaid.

- Depreciation has increased by 15% on Q-o-Q basis and around 78% on YTD basis. Tax saw huge rise in current quarter as the company had to meet some tax obligation related to Docpharma (Belgium) which was one time in nature.

- Rajiv Malik, CEO of Matrix Laboratories, has been named as Head of Global Technical Operations for Mylan Laboratories, where he will oversee global R&D,manufacturing, supply chain management and regulatory affairs. Mr. Malik has over 24 years of global generic pharmaceutical industry experience in leadership positions. Prior to joining Matrix, Mr. Malik was Head of Global Development and Registration for Sandoz and also formerly served as Head of Pharma Research and Global Regulatory Affairs at Ranbaxy.

  This is apart from the fact that Mr. Prasad has joined Mylan Board and Executive Management Team as Head of Global Strategies. This is a positive development for Matrix Laboratories per se. Mr. N Prasad (Promoter & Chairman) has retained a 5% stake in the Matrix Laboratories. He will remain on Matrix board as Non-Executive Vice Chairman.

- The stock is currently trading at around 7.5x FY 08E EPS of 21 and 5.6x FY 09E EPS of Rs. 29 respectively. The risk to our recommendation includes risk pertaining to the generics business and APIs where margins are witnessing erosion due to fierce competition. It also includes lack of clarity on transfer pricing between Matrix and Mylan. Also, there is still no clarity on the issue of management of various subsidiaries and their current profitability including Docpharma (Belgium).

Quarterly Financials

Particulars (Rs Mn)	Q3FY07	Q3FY06	% Chng	Q2FY07	% Chng	9MFY07	9MFY06	% Chng
Net Sales	3,952.52	3,338.01	18.41	3,731.78	5.92	12,105.90	7,797.23	55.26
Expenditure								
Raw Material Cost	2,199.76	2,083.95	5.56	2,017.47	9.04	6,795.97	4,611.98	47.35
Other Expenses	820.89	594.66	38.04	672.24	22.11	2,168.28	1,382.06	56.89
Employee Cost	447.77	290.13	54.33	473.00	(5.33)	1,375.94	667.20	106.23
Total Expenditure	3,468.42	2,968.74	16.83	3,162.71	9.67	10,340.19	6,661.24	55.23
Operating Profit	484.10	369.27	31.10	569.07	(14.93)	1,765.71	1,135.99	55.43
OPM %	12.25	11.06		15.25		14.59	14.57	
Other Income	195.15	1,158.68	(83.16)	128.63	51.71	463.31	1,512.00	(69.36)
PBDIT before R&D Exps	679.25	1,527.95	(55.55)	697.70	(2.64)	2,229.02	2,647.99	(15.82)
PBDIT before R&D Margin (%)	17.19	45.77		18.70		18.41	33.96	
R&D Expenses	262.86	104.54	151.44	226.26	16.18	666.14	246.26	170.50
PBDIT	416.39	1,423.41	(70.75)	471.44	(11.68)	1,562.88	2,401.73	(34.93)
PBDIT Margin (%)	10.53	42.64		12.63		12.91	30.80	
Interest	203.97	99.98	104.01	194.54	4.85	555.42	138.47	301.11
PBDT	212.42	1,323.43	(83.95)	276.90	(23.29)	1,007.46	2,263.26	(55.49)
Depreciation	148.24	94.26	57.27	128.30	15.54	413.84	232.62	77.90
PBT	64.18	1,229.17	(94.78)	148.60	(56.81)	593.62	2,030.64	(70.77)
PBT Margin (%)	1.62	36.82		3.98		4.90	26.04	
Exceptional Items	5.55	3.28		-		19.38	3.72	
Tax	67.37	221.06	(69.52)	(6.16)	(1,193.67)	86.37	325.75	(73.49)
PAT	(8.74)	1,004.83	(100.87)	154.76	(105.65)	487.87	1,701.17	(71.32)
PAT Margin (%)	(0.22)	30.10		4.15		4.03	21.82	
Equity Capital	307.96	306.47		307.96		307.96	306.47	
EPS Diluted (Rs.)	(0.06)	6.53		1.01		3.10	11.09	

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Power Transmission Companies

Visit Note

The Indian Transmission Tower EPC players are expected to ride the continued industry up cycle at a pace of about 20-25% growth rate for the foreseeable future. Importantly, the business scenario continues to be vibrant, with no red flags still in sight. We remain sanguine about the revenue & earnings visibilities for the key industry players. However, it would be perilous to take no account of the sharp run up in the share prices of most of the companies in this space. We initiate our coverage on this industry segment with an accumulate call on Jyoti Structures & KEC International.

Industry Outlook

Domestic

From a trivial 1,350 MW in 1947, the power generation capacity of India had steadily increased to 1,00,000 MW by 2002. Well, with a series of some landmark reforms during that period, India embarked upon a vaulting target to reach 2,00,000 MW by 2012. India is expected to end the current fiscal with an installed capacity of ~1,32,000 MW as against the targeted 1,40,000 by 2007.

The existing inter-regional power transfer capacity is 9,750MW, which will now be enhanced to 37,000MW by 2012 through creation of Transmission Super Highways. Power Grid Corporation of India Limited has envisaged a capex of Rs. 70,000 Crs for this grid of which Rs. 50,000 Crs will be invested by itself, while the balance Rs. 20,000 Crs will come through private sector participation.

The government has lined up a sizable Rs. 23,000 Crs worth of BOOT projects of which Rs. 11,000 Crs comprising of 4 major projects has already been advertised. We see most of the EPC tower players to venture with the larger players for these projects. However, we understand that their interest is mainly towards executing these projects rather than owning & operating them. Such joint venture participation includes consortium like Jyoti Structures – Reliance Energy and KEC International – GMR Group.

To summarize the Domestic growth story, there is tremendous business prospects from activities like evacuation from new generation plants, transfer of inter-regional grid capacity and distribution to mass consumers, with key emphasis on rural electrification. The seeds for the above task is laid in the various initiatives like 'Power for All by 2012' mission, APDRP Program, Electricity Act, RGGVY scheme, etc.

Exports

Things could not had been better for these EPC tower companies at the moment. Apart from the domestic developments discussed above, there is a marked improvement in the exports scenario. Jyoti Structures which a few years ago had reduced their exposure to the international market following some turbulent times, is now actively pursuing growth opportunities and is likely to double the proportion of exports in its revenues from 10% currently to 20% by next year. KEC International, one of the largest players with a huge exposure (70% of sales) to exports, will be the biggest beneficiary. The three key bubbling markets from exports perspective includes the Middle East region, The North African market and also some of the neighboring CIS nations.

Exports v/s. Domestic

The export contracts are fixed price contracts with no price variation clause, unlike the domestic market, which has a practice of an embedded price variation clause in the contract. Here, it is pertinent to note that this clause can work negatively as well in case of a falling raw material price scenario.

Also the exports operating margins are a tad lower than prevalent in the domestic market. Here, one should note that key markets like Middle East have zero taxation regimes & ergo, the slightly lower operating margins. The final net profitability is by & large unaffected.

Margin Expansion

The financial revival of the SEBs has helped the EPC tower players improve on both revenues & earnings. We highlight some of the key reasons, which has caused the margins improve for the industry players.

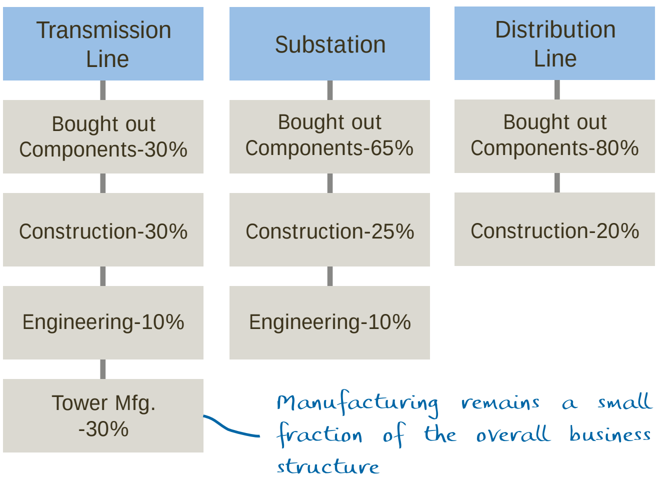
- Faster execution – Averaging 18 months vis-a-vis 30 months earlier
- Improved Capacity Utilization – presently at ~90%
- Cost cutting measures implemented – Excess staff reduced
- Better absorption of fixed costs through increased sales
- Enough options & availability of high margin complex work – Players are not compromising on the margins when bidding for projects, negating the likelihood of any price war in the near term atleast.

Business Model

Minimal Capex :

Tower manufacturing is not a capital intensive business. However, having one's own manufacturing capabilities does help in timely execution of the projects and also brings in some other efficiencies in the system. Also having inhouse manufacturing is important & a pre-requisite, when it comes to select projects. For example in USA , EPC tower companies are preferred over general contractors, who are also otherwise capable of executing the projects. The trivial importance of this can be gauged by the fact, that the towers are just a small fraction of the entire project contract. We take the example of various divisions of Jyoti Structures which is a relatively integrated player in terms of having its own tower manufacturing & testing facilities.

Jyoti Structure's Business Model



- More of construction & bought out components
- Working Capital Intensive – 10% retention money
- Efficient working capital management is of utmost critical for this business. Not just that a substantial proportion of the business involves construction & use of bought-out components, 10% of the proceeds are retained for a period of 1-2 years.

Competitive Scenario

The competitive structure is neither very fragmented nor highly consolidated. The key established players, namely KEC, Jyoti Structures, RPG Transmission, Kalpataru and L&T enjoy ~75%-80% market share. The balance is distributed amongst companies like Tata Projects, Transrail, Spic and new entrants like IVRCL. Spanish companies like Cobro, Isolux, Inabensa have also got active. We learn from the companies we have met recently that the pre-qualification norms & the fulfillment criteria (requirement for experience to have had executed certain level of smaller work before being awarded a bigger contract) should provide some immunity to the established lot, at least for a few years.

Recent Budgetary proposals

The Union Budget for 2007-08 has proposed an increase in the budgetary support for APDRP from Rs.650 crore to Rs.800 crore. Also the allocation for the Rajiv Gandhi Grameen Vidyutikaran Yojana has been increased from Rs.3,000 crore to Rs.3,983 crore. This is regarded as a positive development for power & power ancillaries (transmission & transformer companies) like KEC International, Jyoti Structures, RPG Transmission, Indo Tech Transformer, etc.

No red flags in sight at the moment

With the business booming both at the domestic as well as the international arena, these EPC players are witnessing modest pricing power. What we mean exactly is that with high capacity utilization levels and with no dearth in getting new business, the players are not compromising on the margins. Margins over the past few years have steadily increased from 5-7% to 12-14%. However, in the longer run, these are expected to get retraced and settle at ~10% level. A slightly declining margin scenario is what we have assumed for our forward earning estimates.

Valuations have steadily increased over the past many quarters

Most of the power ancillary companies has had a good run up on the bourses over the past few quarters. Certainly, the companies has delivered excellent growth in both revenues & earnings. The ever surging order book provides some reference point for the encouraging future growth as well. However, the increase in the scrip prices seem to have been much faster in the recent quarters. The key transmission companies, which a few quarters earlier were trading at ~10x its two-year forward earnings are now trading at ~13x on a comparable basis. While there has been a marked improvement in the execution time reflected by the order book/sales ratio and also the operating margins, there is a diminishing scope for much further improvements from hereon. But, there is a reasonable case for maintaining the current trend and continuance of a decent performance going ahead. We initiate with an Accumulate view on both the scrips.

Summary Valuations

KEC	Sales (Rs. Mn.)	EBITDA (Rs. Mn.)	PAT (Rs. Mn.)	EPS (Rs.)	P/E (x)	ROCE (%)	RONW (%)
FY06	17,272.5	1,626.9	493.0	13.1	38.5	25.1%	26.3%
FY07E	20,798.3	2,511.2	1,010.1	26.8	18.8	31.7%	35.7%
FY08E	24,438.0	2,888.7	1,251.0	33.2	15.2	31.0%	31.1%
FY09E	28,103.7	3,180.7	1,438.2	38.2	13.2	28.9%	26.6%

Jyoti	Sales (Rs. Mn.)	EBITDA (Rs. Mn.)	PAT (Rs. Mn.)	EPS (Rs.)	P/E (x)	ROCE (%)	RONW (%)
FY06	7,399.1	755.0	258.6	3.7	46.5	24.8%	22.4%
FY07E	10,787.7	1,288.5	683.5	8.2	21.1	28.9%	23.9%
FY08E	13,759.1	1,603.2	862.7	10.4	16.7	28.3%	23.4%
FY09E	16,493.9	1,919.9	1,046.7	12.6	13.8	27.1%	22.3%

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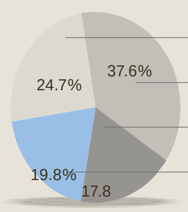
Jyoti Structures Limited

ACCUMULATE | CMP Rs. 174.00 | Target : Rs. 190.0

Stock Codes

Bloomberg	: JYS.IN
Reuters	: JYTS.BO
BSE Code	: 513250
NSE Code	: JYOTISTRUC
BSE Group	: B1

Share Holdings
(as on 31st Dec. 06)



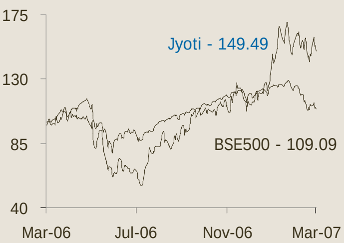
Stock Data

Benchmark	: BSE 500
52 W High Rs.	: 630.0
52 W Low Rs.	: 74.0
Mkt Cap in Mn.	: 12024.0
Face Value	: Rs. 2.0

Absolute Return

%	1m	3m	6m
Jyoti	-13.68	21.21	62.71
BSE 500	-12.94	-11.93	-9.85

Price Comparison



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Jyoti Structures Limited has been providing turnkey solutions in the field of High Voltage Power Transmission Lines and Substations for the past 27 years and enjoys nearly 15-16% market share in the Indian market. It undertakes turnkey projects on a global scale, offering a complete range of services from Design, Engineering Consulting, Tower Testing, Manufacturing, Construction and Project Management. Till date it has supplied over 550,000 MT of transmission line towers, structures to various utilities in India and abroad.

Business & Capacities

JSL's manufacturing plants are located at Nashik and Raipur. Last year it added 24,000 MT capacity at its Nashik facility. Post this expansion, its current capacity stands at 76,000 MT, equally distributed between its two manufacturing facilities. JSL was earlier into the business of refractories, through its ~100% subsidiary Jyoti Refractories Limited. This company has closed operations for the past some time & its spare facilities are now being converted to manufacture transmission towers. 18,000 MT of capacity will get added for JSL at this facility near Nashik by early FY08. JSL also has an in-house Tower Testing station at Igatpuri.

JSL has formed a Joint Venture company in Dubai, viz. Gulf Jyoti International LLC, with Gulf Investment Corporation (GIC). This unit in Dubai Investment Park shall have a manufacturing capacity of 33,000 MT (on a 2 shift basis) operational by July 07.

JSL is one of the few players who apart from TL is also in building sub-stations. With sizable tower manufacturing capacity, tower testing facilities and presence in the sub-station segment, JSL is certainly at a slight advantage against its counterparts.

Valuation & Recommendation

Valuations at 13.8x FY09E earnings & 0.9 times Market Cap/Sales seems to have captured much of the encouraging developments within the company. Nevertheless, there is a reasonable scope for JSL to grow at a faster than our estimated pace of ~20% over the coming two years. The robust business environment & earnings outlook does provide us enough optimism & comfort to recommend Accumulate with a price objective of Rs. 190 per share.

Summary Financials

	Sales (Rs. Mn.)	EBITDA (Rs. Mn.)	PAT (Rs. Mn.)	EPS (Rs.)	P/E (x)	ROCE (%)	RONW (%)
FY06	7,399.1	755.0	258.6	3.7	46.5	24.8%	22.4%
FY07E	10,787.7	1,288.5	683.5	8.2	21.1	28.9%	23.9%
FY08E	13,759.1	1,603.2	862.7	10.4	16.7	28.3%	23.4%
FY09E	16,493.9	1,919.9	1,046.7	12.6	13.8	27.1%	22.3%

Introduction

Jyoti Structures Limited has been providing turnkey solutions in the field of High Voltage Power Transmission Lines and Substations for the past 27 years and enjoys nearly 15-16% market share in the Indian market. It undertakes turnkey projects on a global scale, offering a complete range of services from Design, Engineering Consulting, Tower Testing, Manufacturing, Construction and Project Management. Till date it has supplied over 550,000 MT of transmission line towers, structures to various utilities in India and abroad.

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JV Modalities

Gulf Investment Corporation, the 70% partner in the Middle East JV, is an investment company setup by the GIC countries to promote investments & projects in the region. Jyoti Structures, the 30% partner, will look after the operational aspects and will get a 15% of profits as management fees. Also it would earn an one time income of 5% of the project cost of ~Rs. 650 Mn. JSL would book ~Rs. 30 Mn+ in FY08 on account of this non-recurring income. JSL's investment in the JV will be reflected under investments and it would account for dividend income and management fee income from JV on a recurring basis. There would be no proportionate consolidation of financials in this case.

While the operating margins may be a tad lower than the domestic margins, the 5% target NPM should be achieved comfortably on account of various considerations like zero tax, lower interest rates and logistics savings.

This JV has already bagged an order worth Rs. 1,800 Mn. in October 06 for a 400 kv DC overhead transmission line on a turnkey basis, executable over a period of 18 months. Of the above, Rs. 1,800 Mn. orders business worth Rs. 800 Mn. is expected to flow back to Jyoti Structures in India for tower supply & engineering functions. This, we believe is only because the Dubai facility would get functional only by July 2007.

Capex Details

JSL has undergone minimal capex to reach its current standing. Last year it expanded its capacity at a capex of ~Rs. 120 Mn. The ongoing addition at its old refractory premises would entail a spending of Rs. 150-200 Mn. JSL has invested close to Rs. 90 Mn. for its 30% share in the JV. These expansions are likely to take care of the increasing business flow in the coming few years. This apart, no major capex is envisaged over the next couple of years.

Changing business mix – increasing share of exports

JSL has had a strong exposure to the exports markets a few years ago. However, exports as a percentage of business was brought down from 70% in FY02 to just 10% in FY06, due to intense competition & cut-throat pricing. But now, with the improved scenario for the international business, JSL has started re-focusing on the export market. The share of exports in the business is likely to increase to 20-25% levels.

Leverage to come down & NPM to move up

We have discussed the various factors enhancing the operating margins for the industry in our industry overview section. There apart, there are enough margin levers for JSL in particular, which will enhance the margins at the net profit level.

JSL has so far repaid debt of Rs. 300 Mn. with the money raised through preferential allotment of shares. Debt repayment for this highly working capital intensive company will save a good amount om interest costs.

More importantly, the accounting treatment of income from the Gulf JV, would increase the profitability on one hand, but would not reflect the corresponding increase in revenues. The ultimate impact of the management fee income, dividend income and the one time project commissioning income will be reflected in the higher profit margins.

Order Book Info & Analysis

JSL's order book position as on Feb 01, 2007 is reflected below :

Sector	Domestic	Exports/Demand Exports	Total
Tranmission Line	1,112.0	298.0	1,410.0
Substation	309.0	139.0	448.0
Rural Electrification	122.0	-	122.0
Total	1,543.0	437.0	1,980.0

Sales/ Income from Operations (Rs. Mn.)	FY05	FY06	FY07E	FY08E	FY09E
Closing Order Book Positions	10,000.0	13,400.0	19,800.0	24,750.0	29,700.0
Order Book/ Sales	2.2	1.8	1.8	1.8	1.8

While the order book growth has been robust, we expect the revenue growth to moderate at around 20% on account of the increasing base and also on account of ill-execution risks.

Expanding Share Capital

In April 2006, JSL issued 1.55 Mn. shares on a preferential basis at Rs. 572 per share to FIIs. The total proceeds from this issue were Rs. 887 Mn.. In January 2007, the warrants held by promoters were converted into equity shares of Rs. 2.2 Mn. for a consideration of Rs. 80 Mn. The money raised through the issue will be utilized for repayment of unsecured debt and working capital requirement. No major dilution is further expected for the foreseeable future. However, JSL has recently started with an ESOP policy and some very nominal dilutions on this front cannot be ruled out.

Quarterly Financials

(Rs. Mn)	Q3FY07	Q2FY07	Q-Q (%)	Q3FY06	Y-Y (%)
Net Sales	2,571.5	2,426.1	6.0%	1,986.0	29.5%
Total Expenditure	2,213.4	2,156.9	2.6%	1,777.3	24.5%
Operating Profit	358.2	269.2	33.1%	208.7	71.6%
Other Income	2.6	2.4	10.5%	2.2	21.1%
EBITDA	360.8	271.6	32.9%	210.9	71.1%
Misc Write off	0.0	0.0		0.0	
Depreciation	15.2	14.2	7.0%	12.2	24.6%
PBIT	345.6	257.4	34.3%	198.7	73.9%
Interest	76.6	79.0	-3.0%	79.1	-3.2%
PBT	269.0	178.4	50.8%	119.6	125.0%
Tax	95.0	63.6	49.4%	44.5	113.5%
Reported PAT	174.0	114.8	51.6%	75.1	131.8%
Equity Capital	154.3	153.7		138.2	
EPS (in Rs.)	2.3	1.5		1.1	
Profitability					
OPM %	13.9%	11.1%	283.4	10.5%	341.9
EBITDA %	14.0%	11.2%	283.8	10.6%	341.2
PBIT %	13.4%	10.6%	283.2	10.0%	343.5
PAT %	6.8%	4.7%	203.6	3.8%	298.6
Operational Parameters					
RM Consumed	61.4%	60.9%	49.6	57.9%	347.5
Staff Cost	2.5%	2.5%	(1.6)	2.9%	(38.8)
Jobwork Chgs	9.3%	11.5%	(227.6)	0.0%	926.5
Other Expenditure	13.0%	14.0%	(103.8)	28.7%	(1,577.1)

Valuations & Recommendation

We observe that JSL has been trading at a modest premium to its counterpart KEC International. While KEC is a larger & geographically a much diversified player, JSL has demonstrated a higher growth rate in business. With no major difference between the two players qualitatively, we believe that both of them should command similar valuations. Valuations at 13.8x FY09E earnings & 0.9 times Market Cap/Sales seems to have captured much of the encouraging developments within the company. Nevertheless, there is a reasonable scope for JSL to grow at a faster than our estimated pace of 20% over the coming two years. The topline growth for FY06 & FY07E stands out much higher at 66% & 46% respectively. The declining leverage and the healthy return ratios are encouraging. The robust business environment & earnings outlook does provide us enough optimism & comfort to recommend Accumulate with a price objective of Rs. 190 per share.

Financials

Earnings Statement				
YE March (Rs. Mn.)	FY06	FY07E	FY08E	FY09E
Sales	7,399.1	10,787.7	13,759.1	16,493.9
Other Operating Income	-	38.0	10.9	13.1
Total Expenditure	6,665.0	9,547.1	12,176.8	14,597.1
Operating Profit	734.1	1,278.5	1,593.2	1,909.9
Other Income	20.9	10.0	10.0	10.0
EBITDA	755.0	1,288.5	1,603.2	1,919.9
Depreciation	55.6	64.7	70.7	76.7
EBIT	699.4	1,223.8	1,532.5	1,843.2
Interest	259.3	193.5	225.5	257.5
PBT	440.1	1,030.3	1,307.0	1,585.7
Tax	181.5	346.8	444.2	539.0
PAT	258.6	683.5	862.7	1,046.7

Ratio Analysis				
YE March (Rs. Mn.)	FY06	FY07E	FY08E	FY09E
OPM (%)	9.9%	11.8%	11.6%	11.6%
EBITDA (%)	10.2%	11.9%	11.6%	11.6%
PBIT (%)	9.5%	11.3%	11.1%	11.2%
PAT (%)	3.5%	6.3%	6.3%	6.3%
Interest Cover	2.7	6.3	6.8	7.2
EPS (Rs.)	3.7	8.2	10.4	12.6
P/E (x)	46.5	21.1	16.7	13.8
P/BV (x)	10.4	5.0	3.9	3.1
BVPS (Rs.)	16.7	34.5	44.4	56.6
M Cap (Rs. Mn.)	12,024.2	14,416.7	14,416.7	14,416.7
M Cap/Sales (x)	1.6	1.3	1.0	0.9
EV (Rs. Mn.)	13,633.5	15,626.0	15,826.0	16,026.0
EV/EBITDA (x)	18.6	12.2	9.9	8.4
EV/Sales (x)	1.8	1.4	1.2	1.0
ROCE (%)	24.8%	28.9%	28.3%	27.1%
RONW (%)	22.4%	23.9%	23.4%	22.3%
Debt/Equity (x)	1.4	0.4	0.4	0.3
Inventory T/o Days	60.1	60.0	60.0	60.0
Debtors T/o Days	122.8	120.0	120.0	120.0
Advances T/o Days	23.4	30.0	30.0	30.0
Creditors T/o Days	126.8	120.0	115.0	105.0
Working Cap T/o Days	105.8	116.0	121.5	131.5
Fixed Assets T/o (Gross)	8.2	10.0	11.7	12.9
DPS (Rs.)	2.2	0.4	0.4	0.4
Dividend Payout (%)	59.4%	4.8%	3.8%	3.2%
Dividend Yield (%)	1.3%	0.2%	0.2%	0.2%

Balance Sheet				
YE March (Rs. Mn.)	FY06	FY07E	FY08E	FY09E
Equity Capital	138.2	165.7	165.7	165.7
Share Warrants	14.7	-	-	-
Reserves	1,005.8	2,694.9	3,518.9	4,526.8
Shareholders Funds	1,158.7	2,860.6	3,684.6	4,692.5
Borrowed Funds	1,609.3	1,209.3	1,409.3	1,609.3
Deferred Tax Liability	53.8	169.4	317.5	497.2
Total Liabilities	2,821.9	4,239.4	5,411.4	6,799.0
Fixed Assets	571.6	679.6	708.8	732.1
Investments	101.6	113.1	113.1	113.1
Current Assets				
Inventory	1,218.7	1,779.6	2,263.6	2,713.5
Sundry Debtors	2,490.1	3,559.1	4,527.1	5,426.9
Loans & Advances	473.7	889.8	1,131.8	1,356.7
Cash & Bank Balance	39.3	78.9	108.1	105.5
Current Liabilities				
Sundry Creditors	2,569.7	3,559.1	4,338.5	4,748.6
Provisions	141.7	196.3	239.2	261.8
Net Current Assets	2,143.8	3,441.8	4,584.6	5,948.9
Misc Expenditure	4.9	4.9	4.9	4.9
Total Assets	2,821.9	4,239.4	5,411.4	6,799.0

Cash Flow				
Particulars	FY06	FY07E	FY08E	FY09E
Opening Cash & Bank	174.7	39.3	78.9	108.1
Profit After Tax	258.6	683.5	862.7	1046.7
Less : Invt Income	(20.9)	(10.0)	(10.0)	(10.0)
Depreciation	55.6	64.7	70.7	76.7
Deferred Taxation	4.6	115.6	148.1	179.7
Others	4.6	0.0	0.0	0.0
Change in Working Cap	(673.8)	(1258.4)	(1113.6)	(1367.0)
CF - Operating Activities	(371.3)	(404.5)	(42.1)	(73.9)
Change in Fixed Assets	(143.9)	(172.7)	(100.0)	(100.0)
Change in Investments	(78.6)	(11.5)	0.0	0.0
Investment Income	20.9	10.0	10.0	10.0
CF - Investing Activities	(201.6)	(174.2)	(90.0)	(90.0)
Increase in Equity	0.0	1056.2	0.0	0.0
Changes in Borrowings	457.8	(400.0)	200.0	200.0
Dividend Paid	(35.1)	(37.8)	(38.8)	(38.8)
CF - Financing Activities	437.5	618.4	161.2	161.2
Net Change in Cash	(135.4)	39.7	29.1	(2.6)
Closing Cash & Bank Bal	39.3	78.9	108.1	105.5

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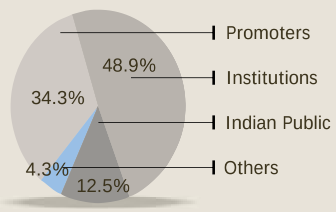
KEC International Limited

ACCUMULATE | CMP Rs. 504.0 | Target : Rs. 570.0

Stock Codes

Bloomberg	: KECI.IN
Reuters	: KECL.BO
BSE Code	: 532714
NSE Code	: KEC
BSE Group	: B1

Share Holdings
(as on 31st Dec. 06)



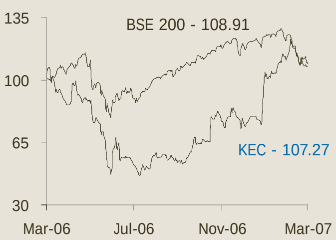
Stock Data

Benchmark	: BSE 200
52 W High Rs.	: 599.0
52 W Low Rs.	: 210.0
Mkt Cap in Mn.	: 18993.7
Face Value	: Rs. 10.0

Absolute Return

%	1m	3m	6m
KEC	-3.30	39.64	99.26
BSE 200	-13.10	-12.11	-9.97

Price Comparison



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KEC International is one of the largest Power Transmission Engineering, Procurement & Construction (EPC) companies in the world, second only to ABB. KEC designs, manufactures, supplies & constructs turnkey projects for power transmission lines. It is also involved in the execution of railway electrification projects, setting up sub-stations & power distribution networks, optical fibre cable installations, turnkey telecom infrastructure services and maintenance of power transmission lines. KEC exports almost 70% of its production to clients spread over 40 countries and also enjoys nearly 15% market share in the domestic market.

Business and Capacities

Capacity:

With 1,40,000 MT of tower capacity, KEC is the largest Indian player in EPC power transmission space. Its state of art manufacturing plants at Jaipur & Nagpur manufacture upto 48,000 MT of towers, while the balance 92,000 MT of tower capacities are spread over its value added partners. Its two tower testing facilities are located at Jaipur & Vashi. This apart KEC has also heavily invested in a construction equipments like tension stringing machines (45+ nos.) & hydraulic mobile cranes (40+ nos.).

Business Spectrum :

- Turnkey Transmission Projects : Design & engineering, manufacturing, procurement & supply, construction.
- Turnkey Distribution Projects : Distribution network, rural electrification, sub-transmission, sub-station.
- Railways/ Telecom Infrastructure : Optical fibre cable installation, Telecom towers EPC, railway electrification.
- Engineering Services : Tower Testing, Satellite/ GPRS survey, cabling.

Valuation & Recommendation

Valuations for most EPC transmission players & so also KEC has got re-rated over the past few quarters. Valuations at 13.2x FY09E earnings & 0.7 times Market Cap/Sales is not exactly cheap. However there is some scope of corrective re-rating here. We recommend accumulate, with a price objective of Rs. 570 per share.

Summary Financials

	Sales (Rs. Mn.)	EBITDA (Rs. Mn.)	PAT (Rs. Mn.)	EPS (Rs.)	P/E (x)	ROCE (%)	RONW (%)
FY06	17,272.5	1,626.9	493.0	13.1	38.5	25.1%	26.3%
FY07E	20,798.3	2,511.2	1,010.1	26.8	18.8	31.7%	35.7%
FY08E	24,438.0	2,888.7	1,251.0	33.2	15.2	31.0%	31.1%
FY09E	28,103.7	3,180.7	1,438.2	38.2	13.2	28.9%	26.6%

Introduction

KEC International is one of the largest Power Transmission EPC companies in the world, second only to ABB. KEC designs, manufactures, supplies & constructs turnkey projects for power transmission lines. It is also involved in the execution of railway electrification projects, setting up sub-stations & power distribution networks, optical fibre cable installations, turnkey telecom infrastructure services and maintenance of power transmission lines. It exports 70% of its production to over 40 countries.

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Capex Details

KEC has been incurring a capex of ~ Rs. 350 Mn. for the past two years. Much of these was towards the large orders received from Ethiopia. We have assumed annual capex in the range of Rs. 250 – 300 Mn. to continue over the coming few years.

Joint Venture with PEI, USA

KEC has entered into a joint venture with Power Engineers Inc. (PEI) USA. This North American company has an annual turnover of US $ 100 million, with an employee base of 750. We perceive that KEC would initially supply towers & execute some EPC work on behalf of PEI, before some real work flows to the JV. The new company formed, KEC Power Inc. (KPI) would be based out of Idaho and focus on establishing itself as an EPC tower player in the North American region.

A String of Restructuring Initiatives

KEC has exercised a string of restructuring initiatives in order to focus & strengthen its position, both operationally & financially in the EPC power transmission space. To briefly touch base on these, KEC sold off its non-core petrochemical business in FY05 soon followed by a debt restructuring (no haircut though) which helped streamline the financing costs. Interest costs as a percentage on net sales has come down from 15.74% in FY02 to 3.43% in FY06. In a major reshuffle last year, KEC International transferred its core business assets & liabilities on a slump sale basis to KEC Infrastructure (later rechristened as KEC International through a name swap exercise) for Rs. 1.43 billion. Its non-core investments, loans & advances to group companies and its land at Kurla, were transferred to another company, namely, KEC Holdings Limited. This move was driven with an intention of cashing on some tax benefits and also improving the return ratios of the core operating company.

Growth Areas Identified

Geographical Expansion :

KEC International is way ahead of its counterparts as far as its international presence is concerned. While other players like Jyoti had slowed down in their focus on exports during difficult times a few years ago, KEC has strengthened its foundation in the international space. In addition to the Middle East region, the North African region and certain CIS countries currently offers tremendous business opportunity for EPC tower players like KEC. Having successfully tapped the aforesaid three markets, KEC now has its eyes set on the US market. Its JV with PEI, will be its entry route to the large US market. Apart from growth, this geographical spread is bringing with itself tremendous diversification risks, which will help KEC over its counterparts during difficult times.

Distribution & Rural Electrification :

KEC has increased its focus from just being a TL player and is now also focusing on distribution lines & rural electrification businesses. KEC is eying a share out of the tremendous government spending on these two sub-segments over the coming years.

Build, Own, Operate (BOO) Projects :

KEC is on the forefront amongst the TL players in the race to capture a pie from the upcoming 14 BOO based projects. KEC has bid for a Rs 15 billion BOOT project along with joint venture partner, GMR Infrastructure, to undertake the construction and operation of a power transmission project.

Order Book Info & Analysis

The details of the current order book is given below :

Total Order Book	2900 Crs + (84% Transmission & 16% Distribution)
International	1930 Crs
Domestic	970 Crs

This apart, there could be some sizable business coming in from the BOO projects, wherein it has jointly bid with GMR group. This we believe would be large volumes & competitive margin business. Also some gradual growth over the coming few quarters is expected out of the American JV.

A probable slowdown in order-book growth at an industry wide level and more particularly for KEC (on account of its large base) is an ensuing concern. However, we feel that most companies would comfortably grow at atleast 20%. While KEC has a larger base, it offers the best bet on geographical growth & risk diversification. With its philosophy of focusing on execution rather than manufacturing, it could well surpass the growth expectations. For our calculations, we have estimated a steady order book/sales ratio with growth stabilizing from 20% to 15% over FY07E – FY09E.

Quarterly Performance

(Rs. Mn)	Q3FY07	Q2FY07	Q-Q (%)	Q3FY06	Y-Y (%)
Net Sales	5,722.7	4,676.6	22.4%	4,575.2	25.1%
Total Expenditure	4,918.2	4,105.4	19.8%	4,153.6	18.4%
Operating Profit	804.5	571.2	40.8%	421.6	90.8%
Other Income	1.6	1.8	-11.1%	3.4	-52.9%
EBITDA	806.1	573.0	40.7%	425.0	89.7%
Depreciation	82.5	83.6	-1.3%	63.8	29.3%
PBIT	723.6	489.4	47.9%	361.2	100.3%
Interest	149.2	156.9	-4.9%	136.1	9.6%
PBT	574.4	332.5	72.8%	225.1	155.2%
Tax	192.3	115.7	66.2%	48.5	296.5%
PAT	382.1	216.8	76.2%	176.6	116.4%
Equity Capital	376.9	376.9		376.9	
EPS (in Rs.)	10.1	5.8		4.7	
Profitability					
OPM %	14.1%	12.2%	184.4	9.2%	484.3
EBITDA %	14.1%	12.3%	183.4	9.3%	479.7
PBIT %	12.6%	10.5%	218.0	7.9%	475.0
PAT %	6.7%	4.6%	204.1	3.9%	281.7
Operational Parameters					
RM Consumed	51.0%	41.7%	930.2	53.2%	(214.9)
Staff Cost	4.3%	4.7%	(39.0)	5.3%	(98.5)
Jobwork Chgs	20.4%	21.8%	(139.4)	20.4%	3.5
Other Expenditure	10.2%	19.6%	(936.3)	12.0%	(174.5)

Valuations & Recommendation

Valuations for most EPC transmission players & so also KEC has got re-rated over the past few quarters. Valuations at 13.2x FY09E earnings & 0.7 times Market Cap/Sales is not exactly cheap. The value of holdings of 10% of RPG Transmission per share of KEC International is very nominal and unlikely to make any notable difference in the valuations for KEC. However, the outlook is robust and the excellent return ratios of over 25% are expected to continue going ahead. Secondly, one should take into account that KEC has historically been denied leadership valuations, despite being the largest player and offering the best bet on geographical growth & risk diversification. There is some scope of corrective re-rating here. We recommend accumulate, with a price objective of Rs. 570 per share.

Summary Valuation

	Sales (Rs. Mn.)	EBITDA (Rs. Mn.)	PAT (Rs. Mn.)	EPS (Rs.)	P/E (x)	ROCE (%)	RONW (%)
FY06	17,272.5	1,626.9	493.0	13.1	38.5	25.1%	26.3%
FY07E	20,798.3	2,511.2	1,010.1	26.8	18.8	31.7%	35.7%
FY08E	24,438.0	2,888.7	1,251.0	33.2	15.2	31.0%	31.1%
FY09E	28,103.7	3,180.7	1,438.2	38.2	13.2	28.9%	26.6%

Financials

Earnings Statement				
YE March (Rs. Mn.)	FY06	FY07E	FY08E	FY09E
Net Sales	17,272.5	20,798.3	24,438.0	28,103.7
Total Expenditure	15,649.7	18,292.1	21,554.3	24,928.0
Operating Profit	1,622.8	2,506.2	2,883.7	3,175.7
Other Income	4.2	5.0	5.0	5.0
EBITDA	1,626.9	2,511.2	2,888.7	3,180.7
Depreciation	269.4	291.0	309.0	325.5
EBIT	1,357.5	2,220.2	2,579.7	2,855.2
Interest	592.8	642.0	625.0	608.0
PBT	764.7	1,578.2	1,954.7	2,247.2
Tax	271.7	568.2	703.7	809.0
PAT	493.0	1,010.1	1,251.0	1,438.2

Ratio Analysis				
YE March (Rs. Mn.)	FY06	FY07E	FY08E	FY09E
OPM (%)	9.4%	12.1%	11.8%	11.3%
EBITDA (%)	9.4%	12.1%	11.8%	11.3%
PBIT (%)	7.9%	10.7%	10.6%	10.2%
PAT (%)	2.9%	4.9%	5.1%	5.1%
Interest Cover	2.3	3.5	4.1	4.7
EPS (Rs.)	13.1	26.8	33.2	38.2
P/E (x)	38.5	18.8	15.2	13.2
P/BV (x)	10.1	6.7	4.7	3.5
BVPS (Rs.)	49.7	75.1	106.9	143.7
M Cap (Rs. Mn.)	18,993.7	18,993.7	18,993.7	18,993.7
M Cap/Sales (x)	1.1	0.9	0.8	0.7
EV (Rs. Mn.)	22,320.0	22,770.0	22,670.0	22,570.0
EV/EBITDA (x)	13.8	9.1	7.9	7.1
EV/Sales (x)	1.3	1.1	0.9	0.8
ROCE (%)	25.1%	31.7%	31.0%	28.9%
RONW (%)	26.3%	35.7%	31.1%	26.6%
Debt/Equity (x)	1.8	1.3	0.9	0.7
Inventory T/o Days	26.4	30.0	30.0	30.0
Debtors T/o Days	153.4	165.0	165.0	165.0
Advances T/o Days	34.2	33.0	33.0	33.0
Creditors T/o Days	205.5	190.0	175.0	160.0
Working Cap T/o Days	19.1	42.9	56.5	70.0
Fixed Assets T/o (Gross)	3.8	4.3	4.7	5.2
DPS (Rs.)	1.2	1.2	1.2	1.2
Dividend Payout (%)	9.2%	4.5%	3.6%	3.1%
Dividend Yield (%)	0.2%	0.2%	0.2%	0.2%

Balance Sheet				
YE March (Rs. Mn.)	FY06	FY07E	FY08E	FY09E
Equity Capital	376.9	376.9	376.9	376.9
Zero % Preference Cap	130.0	130.0	130.0	130.0
Reserves	1,365.1	2,323.6	3,521.7	4,907.0
Shareholders Funds	1,871.9	2,830.4	4,028.5	5,413.9
Borrowed Funds	3,326.3	3,776.3	3,676.3	3,576.3
Deferred Tax Liability	201.1	390.5	625.1	894.8
Total Liabilities	5,407.2	6,997.3	8,330.0	9,885.0
Fixed Assets	4,289.9	4,350.2	4,341.2	4,290.7
Investments	204.8	204.8	204.8	204.8
Current Assets				
Inventory	1,249.0	1,709.4	2,008.6	2,309.9
Sundry Debtors	7,260.4	9,402.0	11,047.3	12,704.4
Loans & Advances	1,618.7	1,880.4	2,209.5	2,540.9
Cash & Bank Balance	636.1	428.8	399.7	326.5
Current Liabilities				
Sundry Creditors	9,723.2	10,826.5	11,716.8	12,319.4
Provisions	136.3	151.8	164.3	172.8
Net Current Assets	904.7	2,442.3	3,784.0	5,389.5
Total Assets	5,407.2	6,997.3	8,330.0	9,885.0

Cash Flow				
Particulars	FY06	FY07E	FY08E	FY09E
Opening Cash & Bank	1653.9	636.1	428.8	399.7
Profit After Tax	493.0	1010.1	1251.0	1438.2
Less : Invt Income	(4.2)	(5.0)	(5.0)	(5.0)
Depreciation	269.4	291.0	309.0	325.5
Deferred Taxation	201.1	189.4	234.6	269.7
Others	(128.9)	0.0	0.0	0.0
Change in Working Cap	(404.3)	(1744.9)	(1370.7)	(1678.8)
CF - Operating Activities	426.2	(259.4)	418.8	349.6
Change in Fixed Assets	(375.8)	(351.3)	(300.0)	(275.0)
Change in Investments	204.8	0.0	0.0	0.0
Investment Income	4.2	5.0	5.0	5.0
CF - Investing Activities	(166.8)	(346.3)	(295.0)	(270.0)
Increase in Equity	0.5	0.0	0.0	0.0
Changes in Borrowings	(1226.1)	450.0	(100.0)	(100.0)
Dividend Paid	(51.6)	(51.6)	(52.9)	(52.9)
CF - Financing Activities	(1277.1)	398.4	(152.9)	(152.9)
Net Change in Cash	(1017.8)	(207.3)	(29.1)	(73.3)
Closing Cash & Bank Bal	636.1	428.8	399.7	326.5

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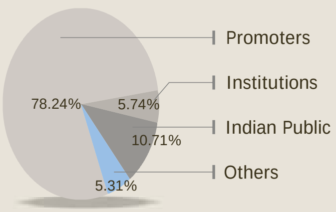
South East Asia Marine Engineering & Construction Limited

BUY | CMP Rs. 180.0

Stock Codes

Bloomberg	: PSOS.IN
Reuters	: PSOS.BO
BSE Code	: 526807
NSE Code	: SEAMECLTD
BSE Group	: B1

Share Holdings
(as on 31st Dec. 06)



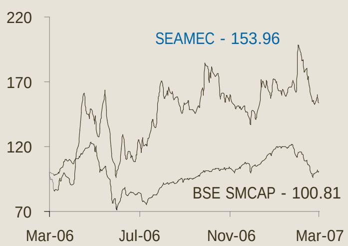
Stock Data

Benchmark	: BSE Small Cap
52 W High Rs.	: 239.0
52 W Low Rs.	: 96.50
Mkt Cap in Mn.	: 6102.0
Face Value	: Rs. 10.0

Absolute Return

%	1m	3m	6m
SEAMEC	-14.53	4.11	0.89
BSE SMCAP	-14.24	-12.65	-10.52

Price Comparison



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South East Asia Marine Engineering & Construction Ltd. (SEAMEC) is engaged in operating multi-support vessels (MSV) for underwater-sea engineering services, deep-sea diving, inspection of underwater-structures, rescue-operations and fire-fighting. SEAMEC currently is a 78.24% subsidiary of Technip S.A of France. SEAMEC owns 4 of the only 7 MSVs owned by Indian companies. Two are owned by ONGC & one by Great Offshore.

Investment Arguments

- Industry Growth Visibility for oil exploration & offshore activity
- Market Leadership with a Strong Pedigree of the company
- Strong Financials
  - Deleveraged status when it can be very high as per industry standards
  - Good cash generation : Cash/share of Rs. 36 for CY07E & Rs. 71 for CY08E
- Immediate Positives
  - Redeployment of SEAMEC 1 at > twice its earlier contracted rate to bring in immediate impact on profits
  - Contribution from new asset MSV 4 (Seamec Princess)
  - Low cost acquisition (just Rs. 832 Mn.) of its 4th MSV also augers well for near term earnings & return ratios
- Undervalued Stock
  - DCF Valuation (DCF of FCF for CY06 – CY21) = Rs. 288 per share
  - Replacement Valuations - @ $50 Mn. /vessel equals Rs. 260/share
  - Relative Valuations – Undervalued at just 5.6 times CY07E

P/E	CY05	CY06	CY07	CY08
SEAMEC (Rs. 180)	33.7	10.4	5.6	4.8
Garware (Rs. 170)	20.5	17.0	12.8	7.8
P/E	FY06	FY07	FY08	FY09
Great Offshore (Rs. 570)	23.3	15.9	9.7	9.0
Global Vectra (Rs. 245)	35.0	16.1	9.4	8.1
Aban Lloyd (Rs. 1750)	84.1	96.2	14.3	5.8

- Potential de-listing candidate with 78.24% held by French conglomerate parent

Summary Valuations

	Sales (Rs. Mn.)	EBITDA (Rs. Mn.)	PAT (Rs. Mn.)	EPS (Rs.)	P/E (x)	ROCE (%)	RONW (%)
CY05	822.8	322.5	181.2	5.3	33.7	11.8%	10.1%
CY06E	1,591.3	752.8	585.7	17.3	10.4	25.1%	24.6%
CY07E	2,420.1	1,335.9	1,090.1	32.2	5.6	33.1%	31.4%
CY08E	2,853.8	1,534.3	1,265.7	37.3	4.8	28.3%	26.7%

Introduction

South East Asia Marine Engineering & Construction Ltd.(SEAMEC) was formed in 1996 as Peerless Shipping & Oilfield Services Ltd. The Peerless group has exited the business, selling their stake to M/s. Coflexip Stena Offshore Mauritius Ltd, a part of the renowned Technip Group of France. SEAMEC currently is a 78.24% subsidiary of Technip S.A of France. SEAMEC is engaged in sub-sea engineering and inspection of under water structures and operates multi-support vessels. Currently SEAMEC holds 4 multi support vessels.

Business

SEAMEC is a pure play on charter hiring of MSVs. Multi Support Vessels are more specialized vessels in the Offshore Supply Vessels(OSV) segment. These vessels are equipped with Dynamic Positioning(DP) system and are used for repair & maintenances of underwater pipelines. 3 MSVs owned by SEAMEC are required by oil companies for construction and maintenance of underwater pipelines and for fire fighting. The 4th vessel it acquired sometime ago caters towards underwater cable laying activity.

Earlier, SEAMEC was also engaged previously in providing drilling services to onshore oil fields, from which it has withdrawn, as it did not form part of its core business. In the quarter April-June 04, the company sold off its Onshore drilling rig for a consideration of US $ 3.10 million (Rs.14 Crores).

Until a few years ago, the company also undertook operations and management of MSVs owned by ONGC. However, a few years ago, ONGC decided to allot the operations & management for all its MSVs & and half of its OSVs to Shipping Corporation of India (SCI).

The company is purely into business of chartering of its vessels. It does not undertake any turnkey projects.

Competition

SEAMEC currently enjoys unique market positioning as there are only 7 Multi Support Vessels; 4 are with SEAMEC and of the remaining 2 are with ONGC & one with Great Offshore. The tide had turned in favour of SEAMEC with ONGC's Samudra Suraksha experiencing a major accident on July 27, 2005. The accident at Bombay High disrupted a huge 15% of the 665,000 barrels of daily oil output. Overall, in lines with the surging oil prices and the increased E&P activities, the operating rates of MSV's have also improved.

Reduced dependence on ONGC

We may generalize that virtually all the offshore players are significantly dependent on ONGC. In case of SEAMEC, its dependency on ONGC has somewhat reduced over the past years. This can primarily attributed to the international parentage in case of SEAMEC. Currently SEAMEC 2 has been chartered to M/s. Global Industries for operations in American Waters. Also SEAMEC 3 has been contracted with Offshore Technology Solutions Ltd, Trinidad, West Indies.

Asset Deployment

SEAMEC 1 : This 1700 DWT MSV was deployed on a long term charter with M/s. Dolphin Offshore Enterprises Limited for a firm period of two years (w.e.f. September 23, 2005) @ $20,000 per day with a provision for extension for a further period of two years. However, Dolphin has abruptly terminated the contract and returned the vessel back to SEAMEC, which it has now deployed with ONGC from July 30, 2006 onwards at an expected rate of $40,000-45,000 per day.

SEAMEC 2 : This is a 2100 DWT MSV and had been chartered to M/s. Global Industries for the period January – May 2006 at $40,000 per day. These rates were higher than rates contracted last year ($30,000 per day). Thereafter, SEAMEC 2 is operating in Mexico Region for a firm period of 180 days with an option of 2 Six Months Extension. For this, she has been contracted at $47,000 per day.

SEAMEC 3 : She was deployed in Bombay High fields on long term charter for HAL Offshore Limited till February 28, 2006. Later, this 2100 DWT MSV was chartered to IOEC until May 15, 2006 @ $36,000 per day. Thereafter, SEAMEC 3 has been contracted with Offshore Technology Solutions Ltd, Trinidad, West Indies for engagement for a period of one year, with a provision of extension for further one year for working in Port of Spain, Trinidad. The mobilization commenced in early June 2006. We have assumed revenues @ $47,000/day for this vessel.

SEAMEC PRINCESS : South East Asia Marine Engineering & Construction Ltd took the delivery of its 4th MSV rechristened "Seamec Princess" at Pasir Gudang, Malaysia on June 12, 2006. The company bought this 6700 DWT Cable Laying Vessel at an attractive price of Rs. 832 Mn. During Q306, SEAMEC expensed ~Rs. 80 Mn. towards mobilization & repairs cost on Seamec Princess. This newly acquired vessel was also engaged for a short term charter as a cable layer during Q4CY06. The vessel is presently abroad for conversion to MSV and is expected to be completed during the later part of the first half of the year. We have assumed revenues for 180 days in CY07 @ $47,000/day for this vessel and a capital cost of Rs. 300 Mn towards the said conversion.

Dry Docking

Operational Rates could be seriously impacted on account of Dry Docking, which is like a scheduled repair & maintenance for the vessel. Vessels need to undergo dry docking twice every five years, the schedule for which is decided by the classification society. Based on the new accounting policies, dry docking charges are expensed completely in the same period, in contrast to the earlier practice of deferring the same. This exposes the company to a double impact caused by the expensing of significant amount of dry docking charges coupled with loss of sizable revenues, as the vessel would be non- operational during that period.

For SEAMEC, the financial impact on account of dry docking could be severe as it owns only 4 vessels. Its MSV 1 & MSV 3 have underwent dry docking during the second quarter of CY2005. Even in case of MSV 2, the dry docking exercise was carried out only during December 2004. Considering these, we had not expected any dry docking expenses for CY 2006. However, as mentioned earlier, ~Rs. 80 Mn. were expensed towards mobilization of & repairs on Seamec Princess. We have assumed dry docking expenses at Rs. 120 Mn. with effect from CY07, increasing @ 10% p.a.

Q4CY06 Performance Review

The company has posted encouraging results for the last quarter of the year. The growth is primarily on account of deployment of vessels at renewed higher rates. Also, the new vessel was operational for a brief period on spot basis and made its contribution. Seamec princess however, will not be available for the coming two quarters and ergo the revenues & earnings will be lower to that extent sequentially. Any expensing towards repairs & mobilization could surprise negatively. The new deployment of the existing fleet will reflect the growth over a comparable period in the previous year.

Quarterly Financials

(Rs. Mn)	Q4CY06	Q3CY06	Q-Q (%)	Q4CY05	Y-Y (%)
Net Sales	616.0	336.0	83.3%	274.1	124.7%
Total Expenditure	312.3	290.5	7.5%	95.7	226.2%
Operating Profit	303.7	45.5	567.4%	178.4	70.3%
Other Income	5.0	5.3	-6.0%	14.2	-64.7%
EBITDA	308.7	50.8	507.2%	192.6	60.3%
Depreciation	46.3	42.6	8.8%	28.8	60.6%
PBIT	262.4	8.3	3070.9%	163.8	60.2%
Interest	0.8	0.8	-3.6%	1.9	-57.2%
PBT	261.6	7.4	3413.7%	161.9	61.6%
Tax	3.0	2.4	23.2%	4.9	-38.5%
PAT	258.6	5.0	5055.2%	157.1	64.7%
Equity Capital	339.0	339.0		339.0	
EPS (in Rs.)	7.6	0.1		4.6	
Profitability	Q4CY06	Q3CY06		Q4CY05	
OPM %	49.3%	13.5%		65.1%	
EBITDA %	50.1%	15.1%		70.3%	
PBIT %	42.6%	2.5%		59.8%	
PAT %	42.0%	1.5%		57.3%	
Operational Parameters	Q4CY06	Q3CY06		Q4CY05	
RM Consumed	3.5%	27.8%		5.5%	
Staff Cost	36.2%	36.8%		18.0%	
Other Expenditure	10.9%	21.8%		11.3%	

Investment Arguments

Industry Growth Visibility for oil exploration & offshore activity

The broader industry outlook is extremely robust and is likely to continue for atleast 5-10 years to come. As many as 55 exploration blocks are currently on offer under NELP VI, as against a total of 108 blocks offered cumulatively under NELP I to NELP V. Of these 24 deep water blocks and 10 shallow water blocks have recently been awarded under the NELP VI round. The new gas finds in the KG Basin and the sharp pickup in exploratory activities by players like Reliance, ONGC & GSPL can potentially trigger exponential growth opportunities for sub-sea contractors & so for SEAMEC.

Market Leadership with a Strong Pedigree of the company

This is evident from the fact that SEAMEC has 4 of the only 7 vessels owned by Indian companies. Its major owners with over 78% equity share is the Technip group, which is one of the topmost players in marine construction globally.

Strong Financials

- Deleveraged status when it can be very high as per industry standards:
  Due to the long term nature of contracts, the financing scenario for offshore companies is in sharp contrast to that of a normal shipping company. With a high predictability in earnings in the medium term on account of the long duration contracts, offshore companies find favour of the banks & lending institutions. SEAMEC stands out in this regard with almost zero debt on its books. Infact the cash position is good enough not to warrant any leverage even in case of executing some further expansion plans.

- Good cash generation business-Cash/share of Rs. 36 for CY07E & Rs. 71 for CY08E :
  With the current upswing in the offshore business, its pouring cash for SEAMEC. We expect SEAMEC to generate almost Rs. 1,200 Mn. of free cashflows from operating the 4 MSVs, which should leave them enough to internally finance any further growth plans for the company. Since we have not accounted for any further addition to the current fleet & also its poor dividend track record, we see the Cash per share steadily increasing year after year.

Immediate Positives

- Redeployment of SEAMEC 1 at > twice its earlier contracted rate to bring in immediate impact on profits :
  Seamec 1 was deployed on a long term charter with M/s. Dolphin Offshore Enterprises Limited for a firm period of two years @ ~ $20,000/day (w.e.f. September 23, 2005) with a provision for extension for a further period of two years. However, the abrupt termination of the contract by Dolphin & its redeployment with ONGC at ~$40,000-45,000/day brings in windfall gains for the company.

- Contribution from new asset MSV 4 (Seamec Princess) :
  This new vessel is expected to be functional by the second half of CY07. With this SEAMEC should earn an increased cashflow of ~Rs. 1,100 - 1,200 Mn. as compared to Rs. 800-900 Mn. it would have earned from its earlier fleet of 3 vessels.

- Low cost acquisition (just Rs. 832 Mn.) of its 4th MSV also augers well for near term earnings & return ratios :
  It seems that SEAMEC has been able to get its 4th vessel at an extremely attractive price. Considering that a new vessel would cost about ~$50 Mn., at Rs. 832 Mn. the deal looks clearly in favour of SEAMEC. However, it has already expensed Rs. 80 Mn towards its mobilization & repairs of this vessels. Also this cable layer is now undergoing major modifications. Its conversion into a MSV would entail a cost of Rs. 250-300 Mn., which we anticipate the management to capitalize. Nevertheless, even after all these, the deal is still very much in favour of SEAMEC. With the earnings atleast at par or higher in comparison with the current fleet, the overall impact would be reflected in both, improved earnings and also the return ratios.

Undervalued Stock

- DCF Valuation (DCF of FCF for CY06 – CY21) = Rs. 288 per share : We have discounted the free cashflows for the explicit period CY06-CY21 at a desired 13% rate. Our estimates are based on the current fleet & we have not accounted for any increase in fleetsize going ahead. We also assume that the current charter rates at $47,000/day would sustain on an average for the entire explicit period. In line with our choice to restrict to the current fleet size, we decide to entirely ignore the terminal value, if any. This is on account of the limited working life of the vessels. We have factored in an increasing spend towards dry docking and also in the tax rates due to increasing contribution from non-chartering income, which will get taxed at normal rates & not at lower tonnage tax.

Rs Mn			
DCF (CY06-CY21E)	9,136.01	WACC	13.00%
Terminal Value	-	Terminal Growth	N.A
Enterprise value	9,136.01	Nos of Eq Shares	33.90
Cash	665.49	Fair Value Per share	288.24
Debt	(30.00)	CMP	180.00
Shareholder Value	9,771.50	Upside	60.14%

- Replacement Valuations :
  @ $50 Mn. /vessel equals Rs. 260/share

- Relative Valuations# :
  Not just SEAMEC is the cheapest of the lot, there is a big gap in its valuations , relatively speaking. This is despite that SEAMEC is not leveraged and also stands out on all other financial parameters.

SEAMEC (Rs. 180)	CY05	CY06	CY07	CY08
EPS	5.3	17.3	32.2	37.3
P/E	33.7	10.4	5.6	4.8
Great Offshore (Rs. 570)	FY06	FY07	FY08	FY09
EPS	24.5	35.8	58.7	63.6
P/E	23.3	15.9	9.7	9.0
Global Vectra (Rs. 245)	FY06	FY07	FY08	FY09
EPS	7.0	15.2	26.1	30.3
P/E	35.0	16.1	9.4	8.1
Aban Lyod (Rs. 1750)	FY06	FY07	FY08	FY09
EPS	20.8	18.2	122.3	303.6
P/E	84.1	96.2	14.3	5.8
Gareware (Rs. 170)	CY05	CY06	CY07	CY08
EPS	8.3	10.0	13.3	21.9
P/E	20.5	17.0	12.8	7.8

Potential de-listing candidate

Its 78.24% ownership held by French conglomerate parent (Technip Group) and the opaque management behaviour towards any company/industry information are suggestive of the de-listing candidature of the company.

Financials

Earnings Statement				
Particulars (Rs Mn)	CY05	CY06	CY07E	CY08E
Net Revenues	822.8	1591.3	2420.1	2853.8
Total Expenditure	822.8	1591.3	2420.1	2853.8
Operating Profit	272.3	707.8	1302.6	1461.8
Other Income	50.2	45.0	33.3	72.5
EBITDA	322.5	752.8	1335.9	1534.3
Depreciation	112.0	149.1	189.9	193.2
EBIT	210.4	603.7	1145.9	1341.1
Interest	10.4	2.7	0.0	0.0
PBT	200.0	600.9	1145.9	1341.1
Tax	18.9	15.3	55.8	75.4
PAT	181.2	585.7	1090.1	1265.7
Extraordinary Items	12.1	0.0	0.0	0.0
Reported PAT	193.2	585.7	1090.1	1265.7

Ratio Analysis				
Particulars	CY05	CY06E	CY07E	CY08E
OPM (%)	33.1%	44.5%	53.8%	51.2%
EBITDA (%)	39.2%	47.3%	55.2%	53.8%
PBIT (%)	25.6%	37.9%	47.4%	47.0%
PAT (%)	22.0%	36.8%	45.0%	44.4%
Interest Cover	20.2	220.3	0.0	0.0
EPS (Rs.)	5.3	17.3	32.2	37.3
P/E (x)	33.7	10.4	5.6	4.8
P/BV (x)	3.4	2.6	1.8	1.3
BVPS (Rs.)	52.8	70.1	102.3	139.6
Market Cap (Rs. Mn.)	6102.0	6102.0	6102.0	6102.0
M Cap/Sales (x)	7.4	3.8	2.5	2.1
EV (Rs. Mn.)	6102.0	6132.0	6102.0	6102.0
EV/EBITDA (x)	22.4	8.7	4.7	4.2
EV/Sales (x)	7.4	3.9	2.5	2.1
ROCE (%)	0.1	0.3	0.3	0.3
RONW (%)	0.1	0.2	0.3	0.3
Debt/Equity (x)	0.0	0.0	0.0	0.0
Inventory T/o Days	69.7	75.0	75.0	75.0
Debtors T/o Days	100.6	65.0	65.0	65.0
Advances T/o Days	17.6	20.0	20.0	20.0
Creditors T/o Days	53.2	60.0	60.0	60.0
Working Cap T/o Days	466.1	234.0	297.2	432.2
Fixed Assets T/o (Gross)	0.5	0.6	0.8	1.0
DPS (Rs.)	0.0	0.0	0.0	0.0

Balance Sheet				
Particulars (Rs Mn)	CY05	CY06E	CY07E	CY08E
Equity Capital	339.0	339.0	339.0	339.0
Reserves	1451.5	2037.2	3127.3	4393.0
Shareholders Funds	1790.5	2376.2	3466.3	4732.0
Borrowed Funds	0.0	30.0	0.0	0.0
Total Liabilities	1790.5	2406.2	3466.3	4732.0
Fixed Assets	738.5	1384.7	1494.8	1351.6
Investments	1.3	1.3	1.3	1.3
Current Assets				
Inventory	105.1	181.5	229.6	286.0
Sundry Debtors	226.8	283.4	431.0	508.2
Loans & Advances	26.5	48.4	61.2	76.3
Cash & Bank Balance	780.0	665.5	1449.1	2758.5
Current Liabilities				
Sundry Creditors	80.3	145.2	183.7	228.8
Provisions	7.4	13.4	16.9	21.1
Net Current Assets	1050.7	1020.2	1970.2	3379.1
Misc Expenditure	0.0	0.0	0.0	0.0
Total Assets	1790.5	2406.2	3466.3	4732.0

Cash Flow				
Particulars	CY05	CY06E	CY07E	CY08E
Opening Cash & Bank	777.2	780.0	665.5	1449.1
Profit After Tax	193.2	585.7	1090.1	1265.7
Investment Income	-50.2	-45.0	-33.3	-72.5
Interest Paid	10.4	2.7	0.0	0.0
Depreciation	112.0	149.1	189.9	193.2
Others	855.6	0.0	0.0	0.0
Change in Working Cap	-211.6	-84.0	-166.5	-99.4
CF - Operating Activities	909.5	608.6	1080.3	1287.0
Change in Fixed Assets	-82.9	-795.4	-300.0	-50.0
Change in Investments	0.0	0.0	0.0	0.0
Investment Income	50.2	45.0	33.3	72.5
CF - Investing Activities	-32.8	-750.4	-266.7	22.5
Increase in Equity	0.0	0.0	0.0	0.0
Changes in Borrowings	-86.3	30.0	-30.0	0.0
Interest Paid	-10.4	-2.7	0.0	0.0
Dividend Paid	0.0	0.0	0.0	0.0
CF - Financing Activities	-96.7	27.3	-30.0	0.0
Net Change in Cash	780.0	-114.5	783.6	1309.5
Closing Cash & Bank Bal	780.0	665.5	1449.1	2758.5

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PPFAS

Software Sector

We recently saw a number of IT scrips tank on the Indian bourses; a fallout of the Union Budget proposals. Measures like FBT on ESOPs, MAT on Section10-A & 10-B companies and Service Tax on rental payments were certainly neither anticipated nor ever desired for the IT Services companies. There were some marginal positives for companies like Vakrangee Software & Tera Soft on account of increased allocation for e-governance and some others like Educomp Solutions & NIIT are expected to benefit on account of the overall increased spending towards education. Nevertheless, the new budget alterations are unlikely to cause any notable change in the growth prospects of the industry. We perceive that the momentum in the sector shall continue and the current dip in scrip prices provide for opportunities for fresh investments in these counters.

MAT is now extended to income in respect of which deductions are claimed under sections 10A & 10B. Firstly, the continuance of tax sops under sections 10A & 10B is limited till FY09 only & as such, the applicability of MAT would have its impact on for FY08 & FY09 only. Even here, there would be only a small impact on the cashflows for just two years, the impact of which will get reversed post FY09. The earnings would by & large remain unaffected on account of the provisioning of deferred tax assets. While there is almost no impact on earnings on account of MAT, even FBT on ESOPs & Service tax on rental payments would have little impact on the overall profitability of most companies. While the new norms appear a negative for the industry, the impact would be marginal and does not warranty the sharp fall in the scrip prices as witnessed over the past few weeks.

We maintain our positive view on the sector and so the companies under coverage, namely Infosys, Mphasis, NIIT Tech & Sonata Software. Infosys Tech is likely to continue with its impeccable growth record, notwithstanding any temporary aberrations. Mphasis is a long term growth play on the post acquisition synergies with EDS. NIIT Tech & Sonata are strong plays on the niche European markets. NIIT Tech seems to have had a strong image revamp and some valuation re-rating as well upon shift from a defensive bet to an aggressive player with a key focus & foothold on the European markets. Sonata Software is a bet on the various growth opportunities consequent its German acquisition. Any re-rating to this otherwise undervalued company would be an added bonus.

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Investment Research

PPFAS

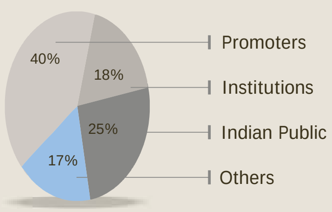
Infosys Technologies Limited

BUY | CMP Rs. 2105.0 | Target Rs. 2735.0

Stock Codes

Bloomberg	: INFO.IN
Reuters	: INFY.BO
BSE Code	: 500209
NSE Code	: INFOSYSTCH
BSE Group	: A

Share Holdings
(as on 31st Dec. 06)



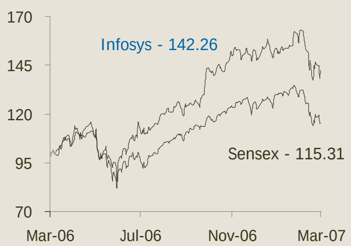
Stock Data

Benchmark	: Sensex
52 W High Rs.	: 3400.0
52 W Low Rs.	: 1572.0
Mkt Cap in Mn.	: 1295880.0
Face Value	: Rs. 10.0

Absolute Return

%	1m	3m	6m
Infosys	-9.01	-6.90	14.88
Sensex	-10.46	-7.80	4.45

Price Comparison



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Demanding Expectations..

Infosys Technologies has posted a fair performance for the third quarter of FY07. The key positives includes the fact that the business grew at 10% Q-Q in dollar terms and also the margins improved marginally despite a unfavourable currency scenario. Infosys continues to clock 50% Y-Y profit growth.

However, it seems that Infosys failed to meet expectations on a few fronts. Firstly, the final numbers did not beat the market expectations as it did over the past few quarters in a row, thanks to the contrast currency scenario over the two periods compared. Secondly, its muted Q4 guidance revision, again after factoring a stronger INR appeals little. Thirdly, if we may add, would be the absence of announcement of any mega billion dollar deals.

We suggest that not much should be read in the Q4 guidance revision by the management. The guidance factors in a much weaker $ at Rs. 44.11 as compared to the average rate of Rs. 44.53 for the December quarter. Also Q4 is generally a mild quarter as clients are finalizing & reallocating budgets, employee additions are slow and also certain costs like visa, etc. go up. The outlook for offshoring continue to remain buoyant and industry growth in the range of 25-30% is likely to continue. Infact, the shift towards larger deal sizes and global delivery model suggest a larger benefit to the larger companies like Infosys.

We maintain our positive call on the company with a near term target price of Rs. 2,400 and a FY08E target price of Rs. 2,735 based on a modest 25% growth and a forward multiple of 25x.

Summary Financials

Particulars	FY05	FY06	FY07E	FY08E
Net Revenues (Rs Crs)	7,130.0	9,521.0	14,137.3	19,469.3
Net Profit (Rs Crs)	1,891.0	2,458.0	3,772.8	4,868.6
EPS (Rs.)	34.2	44.5	67.5	87.2
ROCE (%)	40.8%	39.7%	40.0%	35.7%
RONW (%)	35.3%	35.3%	35.1%	31.2%
P/E (x)	61.6	47.3	31.2	24.1
P/BV (x)	10.9	8.3	10.9	7.5
M Cap/Sales (x)	8.0	6.1	8.3	6.0
EV/EBITDA (x)	24.4	18.8	26.0	19.1
EV/Sales (x)	8.0	6.1	8.3	6.0

Q307 Performance Review

Result Highlights

- > 10% revenue growth in $ terms for the third quarter in a row
- 5.91% Q-Q revenue growth in INR terms
- Marginal margin improvement despite negative forex impact
- Translation losses limit PAT growth to 5.8% Q-Q; 51.5% Y-Y
- Average Rupee rate at Rs. 45.53 for Q3FY07 as compared to Rs. 46.29 for Q2FY07
- Utilization rates excluding trainees down by 170 bps Q-Q from 77.5% to 75.8%

Quarterly Financials

Earnings Statement					
YE March (Rs. Mn.)	Q3FY07	Q2FY07	Q-Q(%)	Q3FY06	Y-Y(%)
Net Revenues	3,655.0	3,451.0	5.91%	2,532.0	44.35%
Direct Expenses	1,938.0	1,833.0	5.73%	1,327.0	46.04%
Gross Profit	1,717.0	1,618.0	6.12%	1,205.0	42.49%
Selling & Marketing expenses	236.0	221.0	6.79%	158.0	49.37%
General & Admin Expenses	285.0	288.0	-1.04%	186.0	53.23%
Total Expenditure	2,459.0	2,342.0	5.00%	1,671.0	47.16%
Operating Profit	1,196.0	1,109.0	7.84%	861.0	38.91%
OPM (%)	0.3	0.3	1.83%	0.3	-3.77%
Other Income	59.0	66.0	-10.61%	(5.0)	-1280.00%
EBITDA	1,255.0	1,175.0	6.81%	856.0	46.61%
Depreciation	141.0	122.0	15.57%	117.0	20.51%
EBIT	1,114.0	1,053.0	5.79%	739.0	50.74%
Interest	-	-		-	
PBT	1,114.0	1,053.0	5.79%	739.0	50.74%
Tax	130.0	123.0	5.69%	83.0	56.63%
PAT Before MI	984.0	930.0	5.81%	656.0	50.00%
Minority Interest	1.0	1.0	0.00%	7.0	-85.71%
PAT	983.0	929.0	5.81%	649.0	51.46%
Ratio Analysis					
YE March (Rs. Mn.)	Q3FY07	Q2FY07	Q-Q(bps)	Q3FY06	Y-Y(bps)
OPM (%)	32.72%	32.14%	58.7	34.00%	-128.2
EBITDA (%)	34.34%	34.05%	28.8	33.81%	52.9
PBIT (%)	30.48%	30.51%	-3.4	29.19%	129.2
PAT (%)	26.92%	26.95%	-2.7	25.91%	101.4

Sustained Employee Growth

Particulars	Dec-05	Mar-06	Jun-06	Sep-06	Dec-06
Total Employee	49,422	52,715	58,409	66,150	69,432
Net Addition	3,226	3,293	5,694	7,741	3,282
Q-Q growth	6.98%	6.66%	10.80%	13.25%	4.96%
Y-Y growth	40.30%	43.44%	46.73%	43.19%	40.49%

Growth from lower bracket clients

Particulars	Dec-05	Mar-06	Jun-06	Sep-06	Dec-06
Active Clients	454	460	469	476	488
Added during the quarter	36	38	38	45	43
Number of million dollar client*	206	221	221	232	256
Number of 5 million + dollar clients*	78	81	94	97	108
Number of 10 million + dollar clients*	51	54	56	61	67
Number of 20 million + dollar clients*	25	26	28	29	35
Number of 30 million + dollar clients*	18	19	19	20	22
Number of 40 million + dollar clients*	14	14	15	16	17
Number of 50 million + dollar clients*	7	9	11	12	11
Clients accounting for > 5% revenues	-	-		1	1
Revenue - Top client %	5	5	6	7	7
Revenue - Top 5 clients %	18	19	20	21	19
Revenue - top 10 clients %	30	31	32	33	31
Repeat business %	93	92	97	95	95
Account receivables - LTM(in days)	57	62	65	65	63

"LTM" - Last Twelve Months
* LTM Revenues

Key developments in Q3

- Revenue growth driven primarily by good volume growth coupled with improved realization from new clients and some old clients as well. New clients have signed at 3-4% higher pricing. The company has been able to re-negotiate for a 2-3% higher billing rates from existing clients.

- Margin expansion was driven by increase in product license revenues, marginal improvements on blended billing rates, slight improvement in the offshore-onsite mix and lower SGA costs.

- BPO business grew at 20% Q-Q (its 3rd quarter of double digit growth) with margins higher at 24%+. The consulting arm, still in the investment phase, posted higher losses. However, there were significant client additions.

- Utilization levels including trainees remained flat at 67.5%. Excluding trainees, the figures were lower at 75.8% down by 170 bps Q-Q. Going ahead, the management expects the rate to be maintained in the range of 76-80%.

- Attrition levels continued its uptrend and reached 13.5% for the quarter, the highest in the past many quarters. However, it is pertinent to note that 13.5% is inclusive of 1.3% involuntary attrition. Also, the increased attrition is after a significant increase in the recruitments itself.

- Good increase in client additions, mostly in the lower revenue brackets. Overall 43 clients have been added during the quarter, including a leading US grocery chain, a large distributor of paper products in the US and a leading North American insurance company.

Outlook for the coming quarters

The management has indicated that the outlook going ahead is robust. Overall IT spending by the US companies will be maintained with an upward bias. The budgets are expected to be moving up higher by 3-5% or even 6% for the coming year. A recent Nasscom study reiterates that offshore outsourcing to India will grow at 25-30%. Another pertinent point is that the deal sizes are becoming bigger. This calls for a strong mining opportunity from clients in the lower revenue brackets with increasing deal size. Also the top client continues to grow at a good pace. The top client constituted 6.9% in Q307 v/s. just 4.5% in the same period last year.

On the wage inflation, the management feels that the increase will be reasonable with higher increases for select categories. For example, the middle management & the employees in the 3-5 year experience bracket are witnessing increased poaching from the MNC competition.

Net net, volume growth should be good. The upside from increase in billing rates will have to make up for the wage inflation and the rupee appreciation, in order to maintain the overall profitability. Apart from the normal organic growth, Infosys has now clearly indicated that it is looking at acquisitions of European players with US$200-300 Mn. top-line and with operations focused on a single European country.

FY07E Guidance analysis

Particulars	FY07E	Implied Gowth	Q4FY07	Implied Gowth	Implied Gowth
		(Y-Y)		(Y-Y)	(Q-Q)
Revenue (Rs. Crs)	13919	46.2%	3798	44.7%	3.91%
EPS (Rs.)	66.63	48.1%	17.88	46.3%	3.71%

Opinion

The outlook for offshoring continue to remain buoyant and industry growth in the range of 25-30% is likely to continue. Infact, the shift towards larger deal sizes and global delivery model suggest a larger benefit to the larger companies like Infosys. We suggest that not much should be read in the Q4 guidance revision by the management. We rather await much more details by next quarter and also the guidance for the next year. Until then, we maintain our positive call on the company with a near term target price of Rs. 2,400 and a FY08E target price of Rs. 2,735 based on a modest 25% growth and a forward multiple of 25x.

Risk to our Call

Key risk to our call apart from the operational risks emanate from the P/E multiple. Infosys has been earning premium valuations for its superiority. There is a possibility of the market lowering valuation multiple for this IT major, in case of unfulfilled expectations.

Yearly Financials

Particulars (Rs. Crs)	FY05	FY06	FY07E	FY08E
Net Revenues	7,130.0	9,521.0	14,137.3	19,469.3
- Growth %		33.5%	48.5%	37.7%
Total Expenditure	4,795.0	6,431.0	9,622.6	13,313.0
Software Development Expenses	3,765.0	5,066.0	7,615.1	10,645.7
Gross Profit	3,365.0	4,455.0	6,522.2	8,823.6
Selling & Marketing Expenses	461.0	600.0	876.5	1,148.7
General & Administration Expenses	569.0	765.0	1,131.0	1,518.6
Operating Profit	2,335.0	3,090.0	4,514.7	6,156.3
- OPM %	32.7%	32.5%	31.9%	31.6%
Other Income	124.0	139.0	303.6	130.0
EBITDA	2,459.0	3,229.0	4,818.3	6,286.3
- EBITDA Margins %	34.5%	33.9%	34.1%	32.3%
Depreciation	287.0	437.0	523.1	720.4
EBIT	2,172.0	2,792.0	4,295.2	5,565.9
- EBIT Margin %	30.5%	29.3%	30.4%	28.6%
Interest	-	-	-	-
EBT	2,172.0	2,792.0	4,295.2	5,565.9
Tax	326.0	313.0	520.4	697.3
Net Profit before MI	1,846.0	2,479.0	3,774.8	4,868.6
Minority Interest	-	21.0	8.0	-
Net Profit after MI	1,846.0	2,458.0	3,766.8	4,868.6
- NP Margin %	25.9%	25.8%	26.6%	25.0%
- Growth %		33.2%	53.2%	29.2%
Extra-ordinary Items	45.0	-	6.0	
Reported Net Profit	1,891.0	2,458.0	3,772.8	4,868.6

Summary Financials

Particulars	FY05	FY06	FY07E	FY08E
Net Revenues (Rs Crs)	7,130.0	9,521.0	14,137.3	19,469.3
Net Profit (Rs Crs)	1,891.0	2,458.0	3,772.8	4,868.6
EPS (Rs.)	34.2	44.5	67.5	87.2
ROCE (%)	40.8%	39.7%	40.0%	35.7%
RONW (%)	35.3%	35.3%	35.1%	31.2%
P/E (x)	61.6	47.3	31.2	24.1
P/BV (x)	10.9	8.3	10.9	7.5
M Cap/Sales (x)	8.0	6.1	8.3	6.0
EV/EBITDA (x)	24.4	18.8	26.0	19.1
EV/Sales (x)	8.0	6.1	8.3	6.0

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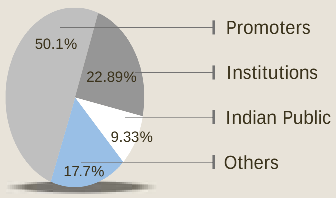
Mphasis Limited

ACCUMULATE | CMP Rs. 276.0

Stock Codes

Bloomberg	: BFL.IN
Reuters	: BLFS.BO
BSE Code	: 526299
NSE Code	: MPHASISBL
BSE Group	: A

Share Holdings
(as on 31st Dec. 06)



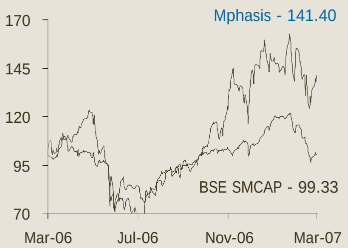
Stock Data

Benchmark	: BSE 500
52 W High Rs.	: 266.7
52 W Low Rs.	: 121.0
Mkt Cap in Mn.	: 50800.0
Face Value	: Rs. 10.0

Absolute Return

%	1m	3m	6m
Mphasis	-5.10	2.23	46.83
BSE 500	-12.94	-11.93	-9.85

Price Comparison



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Nearing Inflexion point..

Mphasis is a leading tier 2 vendor in BFSI segment and one of the Top 20 integrated software services vendors employing more than 17,500 people in both IT services as well as BPO services. EDS acquired 52% of Mphasis in June 2006 and has subsequently hiked their stake by merging its subsidiary EDS(India) with Mphasis, the increased stake now standing at 61.8%. We maintain a positive view on the company's growth prospects both in terms of growth as well as margin expansion.

- Phase 1 of the integration got completed in December 2006. There is an expressed intent to maintain the two separate brands with minimal client overlapping as EDS is more active on the manufacturing vertical, while Mphasis focuses on the BFSI.
- EDS had won a multi-year, multi-million dollar deal from a telecom company. Mphasis will be working as its offshore arm for this $5 Mn. mega project and the ramp-up in this mega deal will be visible from July 07. The are six other mega deals actively pursued by Mphasis & EDS jointly. Mphasis has charted a game plan to get enrolled with top 70 clients of EDS in the current year.
- Mphasis is targeting to become a $ 1 billion revenue company by FY10 from currently at ~ $ 350 Mn, reflecting a desired growth CAGR of ~40%.
- Mphasis has planned to add a net 10,000 employees to its current total strength of 17,500 employees in Cy07 including 7,000-8,000 towards Application business & the balance 2,000-3,000 would be towards BPO & Infra-services.
- Application business will be the highest growth driver in CY2007. This apart, it is foreseeing big traction in the remote infrastructure management space and expects this segment to constitute 20% of its revenues by 2009.
- Margin expansion will be achieved through a combination of billing rate increases, higher utilization, offshore shift, lower SGA expenses etc. While the bill rate increases are mainly in case of new clients, the major thrust for margin expansion would come from increased offshoring and reduction in SGA costs.

The scrip is trading at 31x Q3FY07 annualized earnings. On forward basis, it is trading at 21.6x FY08E & 19x FY09E consensus earnings estimates of Rs. 12.8 & Rs. 14.6 per share respectively. While we do believe in the future growth story, our investment call is constrained by the prevailing rich valuations. We maintain Accumulate.

Q307 Performance Review

The third quarter performance by Mphasis Limited puts to rest some of the post-acquisition concerns and brings in improved visibility for the tremendous growth potential waiting to be unleashed over the next two quarters.

Result Highlights

- Revenues up 4.8% Q-Q and 26.2% Y-Y
- PAT up 52.6% Q-Q but down 12.4% Y-Y
- Q3FY07 performance benefited from increase in billing rates, improvement in utilization rates, steady offshore mix, reduction in SGA costs and lower taxation
- Currency movement had a slight negative impact
- Added 11 new clients in the quarter (non EDS)

Quarterly Financials

(Rs. Mn)	Q3FY07	Q2FY07	Q-Q (%)	Q3FY06	Y-Y (%)
Revenues	3,059.6	2,919.2	4.81%	2,424.5	26.20%
Cost of Revenues	2,123.5	2,070.3	2.57%	1,643.3	29.22%
Gross Profit	936.1	848.9	10.27%	781.2	19.83%
Selling Expenses	216.9	237.4	-8.62%	136.2	59.27%
General Admin Exp	288.2	277.6	3.80%	210.2	37.10%
Provision for Doubtful Debts	3.9	5.6	-30.61%	4.7	-17.12%
Operating Profit	427.1	328.3	30.10%	430.1	-0.70%
Forex gain/ (loss)	(59.9)	(69.2)	-13.41%	(25.9)	131.74%
Other Income/ (expense)	(2.1)	0.7	-403.77%	6.8	-130.75%
EBIT	365.1	259.8	40.54%	411.1	-11.19%
Interest	(12.5)	(12.8)	-2.68%	(3.0)	319.75%
PBT	377.6	272.6	38.51%	414.0	-8.81%
Tax	19.9	38.7	-48.62%	5.6	253.80%
PAT	357.7	233.9	52.93%	408.4	-12.43%
Equity Capital	1,624.1	1,620.4		1,605.0	
EPS (in Rs.)	2.2	1.4	52.58%	2.5	-13.46%
Profitability Ratios	Q3FY07	Q2FY07	Q-Q (bps)	Q3FY06	Y-Y (bps)
GPM %	30.59%	29.08%	151.5	32.22%	(162.6)
OPM %	13.96%	11.25%	271.4	17.74%	(378.1)
EBIT %	11.93%	8.90%	303.4	16.96%	(502.3)
PAT %	11.69%	8.01%	367.9	16.85%	(515.6)

Outlook

- Phase 1 of the integration got completed in December 2006. There is an expressed intent to maintain the two separate brands with minimal client overlapping as EDS is more active on the manufacturing vertical, while Mphasis focuses on the BFSI.

- EDS had won a multi-year, multi-million dollar deal from a telecom company. Mphasis will be working as its offshore arm for this $5 Mn. mega project and the ramp-up in this mega deal will be visible from July 07. The are six other mega deals actively pursued by Mphasis & EDS jointly. These deals although very large, however, have longer sales cycle. Mphasis has charted a game plan to get enrolled with top 70 clients of EDS in the current year.

- EDS will continue to work with its other three vendors in India, namely, Wipro, Cognizant & WNS. The current focus would be to increase the scale and capabilities at Mphasis, before any change is contemplated on this front.

- Mphasis is targeting to become a $ 1 billion revenue company by FY10 from currently at ~ $ 350 Mn, reflecting a desired growth CAGR of ~40%. This ambitious target does not seem to be unachievable, when one looks at the fact that there is a tremendous scope for outsourcing from the $19 billion EDS. India & Mphasis are clearly the biggest beneficiaries of the Best-Source strategy. Also similar feat has already been achieved by IBM when its revenues soared from just $350 Mn. in 2002 to over 1 billion in 2005.

- To materialize this growth opportunity, Mphasis has planned to add a net 10,000 employees to its current total strength of 17,500 employees in CY07. Of these additional 10,000 almost 7,000-8,000 are towards Application business, while the balance 2,000-3,000 would be towards BPO & Infra-services.
  Management has suggested that Application business will be the highest growth driver in CY2007. This apart, it is foreseeing big traction in the remote infrastructure management space and expects this segment to constitute 20% of its revenues by 2009. In the BPO business, a strong transformation is being witnessed from voice to non-voice mix, largely coming from new focus on F&A, HR & credit card businesses. CRM & Technical help are the two growth prospects in the voice based BPO business.

- Margin expansion in an otherwise wage inflationary scenario, would have to be achieved through a combination of billing rate increases, higher utilization, offshore shift, lower SGA expenses etc. While the bill rate increases are mainly in case of new clients, we perceive that the major thrust for margin expansion would come from increased offshoring and reduction in SGA costs. It is interesting to note that there is unlikely to be any notable margin change for Mphasis, when it directly bills the client or obtains work through sub-contracting from EDS. The reason lies in the increased pricing power of EDS as compared to Mphasis, which neutralizes the impact for the Indian arm in both cases.

- The near term risks largely emanate from the supply side constraints and the other generic risks like currency appreciation and a slowdown in US economy.

Valuation & Recommendation

The scrip is trading at 31x Q3FY07 annualized earnings. On forward basis, it is trading at 21.6x FY08E & 19x FY09E consensus earnings estimates of Rs. 12.8 & Rs. 14.6 per share respectively. While we do believe in the future growth story, our investment call is constrained by the prevailing rich valuations. We maintain Accumulate.

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Investment Research

PPFAS

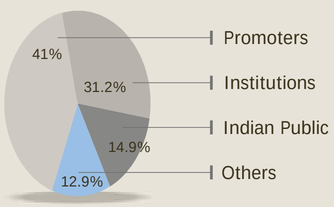
NIIT Technologies Limited

ACCUMULATE | CMP Rs. 445.0 | Target Rs. 494.0

Stock Codes

Bloomberg	: NITEC.IN
Reuters	: NIIT.BO
BSE Code	: 532541
NSE Code	: NIITTECH
BSE Group	: B1

Share Holdings
(as on 31st Dec. 06)



Stock Data

Index	: Sensex
52 W High Rs.	: 443.35
52 W Low Rs.	: 131.35
Mkt Cap in Mn.	: 15592.0
Face Value	: Rs. 10.0

Absolute Return

%	1m	3m	6m
NIIT Tech	0.29	64.63	119.44
Sensex	-10.46	-7.86	4.45

Price Comparison

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ppfas@bloomberg.net

Still Value in this Growth story..

NIIT Technologies appears to be at the threshold of a re-rating exercise post announcement of its third quarter results. This IT midcap has historically traded at inexpensive valuations as a defensive bet. However, over the past few quarters, the company has taken up many enterprising initiatives, some flavour of which is reflected in the recently announced quarterly results.

NIIT Tech has a number of margin & growth drivers, which can catapult it into a higher orbit, closer to the other mid-tier companies.

- Sustained focus on select verticals over the years and the strong growth traction seen in business from the top clients, puts to rest any downside concerns whatsoever.
- Significant growth will be witnessed on account of its inorganic initiatives. NIIT Tech acquired UK based insurance service provider 'Room Solutions' and has entered into a 50:50 JV with Switzerland based HR services firm 'Adecco SA'.
- NIIT Tech has been a key beneficiary of the increase IT spend by the European companies. It is seriously eyeing a pie out of the lucrative German market.
- NIIT Tech which is very strong in the life insurance segment will see a big traction from Room Solutions which is a leading insurance service provider in the non-life 'Property & Casualty' segment. Also there are potential prospects for the BPO business as well.
- Improving share of annuity based revenues in BPO business and improving onsite-offshore mix would help leverage SGA costs & further improve margins.
- NIIT Tech will benefit from Room Solutions IPR based ADM business. Increased offshoring from Room Solutions will be a key to the overall margin improvement from 6-6.5% margins to initially 13-14% & then to 19-20% over the years.
- It is currently building a 3,000 seater capacity, which will be further expanded to 10,000 in three phases to cater to the growing opportunities. For the supply side, it is dependent on NIIT Limited (its quasi bench in work-in-progress)

The scrip currently trades at 13.5 times its FY08E earning estimate of Rs. 32.9 per share. We perceive that there is room for further upside, considering the robust business prospects, which should push the company higher in the mid-tier space. We recommend ACCUMULATE.

Q307 Performance Review

NIIT Technologies appears to be at the threshold of a re-rating exercise post announcement of its third quarter results. This IT midcap has historically traded at inexpensive valuations as a defensive bet. However, over the past few quarters, the company has taken up many enterprising initiatives, some flavour of which is reflected in the recently announced quarterly results.

NIIT Tech figures amongst the top 20 Indian IT Solutions providers having presence in both IT services & BPO services. It has delivered very encouraging Q3 results, which imparts positive visibility for both growth & margins.

Result Highlights

- Revenues up 5% Q-Q & 47% Y-Y to Rs. 2,315 Mn.
- OPM expand by 234 bps Q-Q & 183 bps Y-Y to 21.2%
- Net Profit up 29% sequentially & 92% annually
- NPM at 14.9% as compared to 12.2% in Q207 & 11.4% in Q306

Analysis of Q3 performance

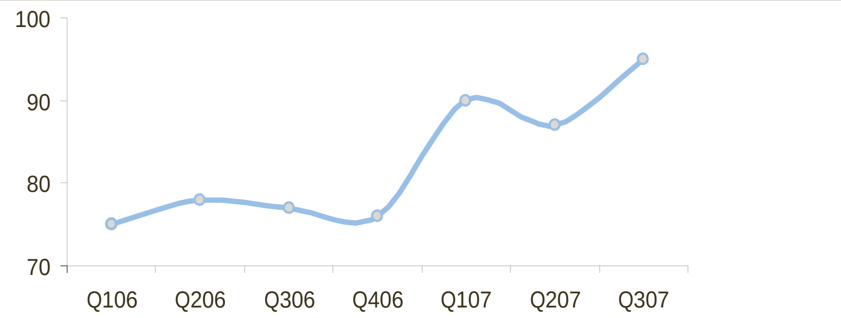
Key highlight of Q307 is the margin expansion which has made a major impact on the bottomline. Margins in the Software Solutions segment increased substantially, thanks to the contribution from M/s. Room Solutions. NIIT Tech acquired Room Solutions in May 2006 and has recently completed the integration process. Also the BPO business contributed positively; its margins improving from mere 1.1% to 3.2% Q-Q.

The share of BPO in overall business is maintained at 6%. Other factors which helped the profit surge includes better utilization and the improving onsite – offshore mix. Capacity utilization improved by a percentage from 81% to 82.1%. The onsite : offshore mix improvement continued with the offshore share increasing from 35% to 36%.

In the Software business, Financial Services & Transportation saw the maximum growth at 87% & 50% respectively. The share of revenues from the 'Focused Verticals' namely, BFSI, Transportation, Retail & manufacturing has now increased to 81% of the consolidated revenues.

Sustained increase in the new order receipts provides confidence on the future growth prospects of the company. In the last quarter, NIIT Tech received a recorded fresh orders intake of $ 56 Mn. This leads the total executable order book over the next 12 months to $95 Mn.

12 Month Executable Order Book ($ Mn.)



Quarterly Financials

(Rs. Mn)	Dec 06	Sept 06	Q-Q Chng	Dec 05	Y-Y Chng
Software Solutions	2,173.0	2,060.0	5.5%	1,469.0	47.9%
BPO Solutions	142.0	139.0	2.2%	105.0	35.2%
Net Revenues	2,315.0	2,199.0	5.3%	1,574.0	47.1%
Operating Expenditure	1,824.0	1,784.0	2.2%	1,269.0	43.7%
Software Solutions	1,686.5	1,646.5	2.4%	1,151.0	46.5%
BPO Solutions	137.5	137.5	0.0%	118.0	16.5%
Operating Profit	491.0	415.0	18.3%	305.0	61.0%
Software Solutions	486.5	413.5	17.7%	318.0	53.0%
BPO Solutions	4.5	1.5	200.0% -	13.0	-134.6%
Other Income	33.0	24.0	37.5%	1.0	3200.0%
EBITDA	524.0	439.0	19.4%	306.0	71.2%
Depreciation	105.0	112.0	-6.3%	93.0	12.9%
PBIT	419.0	327.0	28.1%	213.0	96.7%
Interest	-	-		-	
PBT	419.0	327.0	28.1%	213.0	96.7%
Tax	68.0	53.0	28.3%	30.0	126.7%
PAT before MI	351.0	274.0	28.1%	183.0	91.8%
Minority interest	5.0	5.0		3.0	
Reported PAT	346.0	269.0	28.6%	180.0	92.2%
Equity Capital	386.0	386.0		386.0	
EPS (in Rs.)	9.0	7.0		4.7	
Profitability					
OPM %	21.2%	18.9%	233.7	19.4%	183.2
Software Solutions (%)	22.4%	20.1%	231.6	21.6%	74.1
BPO Solutions (%)	3.2%	1.1%	209.0	-12.4%	
EBITDA %	22.6%	20.0%	267.1	19.4%	319.4
PBIT %	18.1%	14.9%	322.9	13.5%	456.7
PAT %	14.9%	12.2%	271.3	11.4%	351.0

Outlook

NIIT Tech has a number of margin & growth drivers, which can catapult it into a higher orbit, closer to the other mid-tier companies.

- Sustained focus on select verticals over the years and the strong growth traction seen in business from the top clients, puts to rest any downside concerns whatsoever. The four focused verticals have increased their share steadily, the non core (& also slow-growth) businesses constituting below 20% of the total revenues as compared to 29% during Q2FY06. Also the top 10 clients, which constitute over 50% of the business are growing at a very healthy rate of 38-39%.

- NIIT Technologies Ltd has announced a Suite of Insurance Framework Solutions (IFS). These frameworks provide components to rapidly build customizable solutions to support key processes of businesses engaged in Life and Non-Life insurance.

- Significant growth will be witnessed on account of its inorganic initiatives. NIIT Tech acquired 51% of UK based insurance service provider 'Room Solutions' in May 2006 for ~$25 Mn and has entered into a 50:50 JV with Switzerland based HR services firm 'Adecco SA'. NIIT Tech will be further increasing its stake in Room Solutions to 75% before November 2006 &to 100% by June 2007. As far as the JV is concerned, it will start contributing by Q1FY08 and is expected to pour in $150-200 Mn. revenues over a five year period.

- NIIT Tech has been a key beneficiary of the increase IT spend by the European companies. It enjoys established relationship with some marquee clients for over a decade and has an early mover advantage. It is seriously eyeing a pie out of the difficult but lucrative German market.

- NIIT Tech has historically resorted to the inorganic route to strengthen its business model. It acquired Osprey, DEI & AD Solutions in the domain of SAP, Insurance & Logistics respectively. NIIT Tech which is very strong in the life insurance segment will see a big traction from Room Solutions which is a leading insurance service provider in the non-life 'Property & Casualty' segment. Also there are potential prospects for the BPO business as well.

- The BPO business has started contributing positively and would help further improve profitability on account of improved utilization. Improving share of annuity based revenues would help leverage SGA costs & further improve margins. On the onsite-offshore mix, the management has guided that the offshore share will increase steadily by a percentage every quarter.

- NIIT Tech will benefit from Room Solutions IPR based ADM business. Increased offshoring from Room Solutions will be a key to the overall margin improvement from 6-6.5% margins to initially 13-14% & then to 19-20% over the years.

- Group company NIIT continues to hold 25% stake in the company, which is intended to be sold to a strategic partner, who could pave the way for further growth of the company.

- It is currently building a 3,000 seater capacity, which will be further expanded to 10,000 in three phases to cater to the growing opportunities. For the supply side, it is dependent on NIIT Limited (its quasi bench in work-in-progress)

Overall, we feel that NIIT Tech has evolved from an attractive yet defensive bet to a growth story. We perceive that the developments over the past few quarters will have its lasting effects over the times to come. The scrip has had a sharp run-up over the past months and is currently trading at 13.5 times its FY08E consensus earnings estimate of Rs. 32.9 per share. We recommend ACCUMULATE on this growth story from a re-rating perspective with a target price of Rs. 494 based on 15x FY08E EPS.

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Investment Research

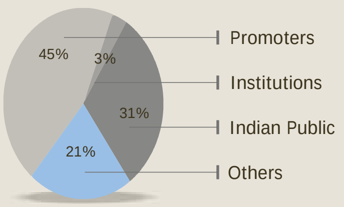
Sonata Software Limited

BUY | CMP Rs. 60.0

Stock Codes

Bloomberg	: SSOF.IN
Reuters	: SOFT.BO
BSE Code	: 532221
NSE Code	: SONATSOFTW
BSE Group	: T

Share Holdings
(as on 31st Dec. 06)



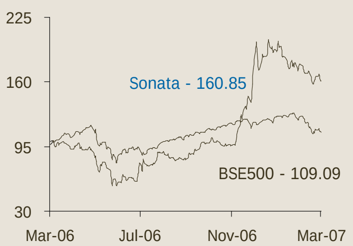
Stock Data

Benchmark	: BSE 500
52 W High Rs.	: 75.05
52 W Low Rs.	: 17.85
Mkt Cap in Mn.	: 7361.0
Face Value	: Rs. 10.0

Absolute Return

%	1m	3m	6m
Sonata	-6.83	-7.06	97.75
BSE 500	-12.94	-11.93	-9.85

Price Comparison



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ppfas@bloomberg.net

Introducing JV 'Sonata TUI Infotech' earnings..

Sonata Software Ltd. is a SEI CMM 5 IT services company has differentiated itself in the space of Product re-engineering services to Independent Software Vendors (ISVs) and is in the nascent but high growth European Offshoring market. Top Clients include, Microsoft, Dell, TUI, Amdocs etc. Sonata has had a 51% CAGR growth over the past 3 years. Sonata Software Ltd on March 13, 2007 has announced the launch of SonnetITeS, a solution built on Microsoft Dynamics CRM 3.0, Microsoft's Customer Relationship Management (CRM) solution, targeted at Information Technology Enabled Services (ITeS) and Business Process Outsourcing (BPO) companies.

Robust outlook for Sonata going ahead.

Sonata Software has recently bought 50.1% in TUI Infotec for Euro 18 Mn. or Rs.106 Crs. TUI Infotech earned revenues of Euro 130 Mn. & a net profit of Euro 6 Mn. in CY 2005. TUI Infotec provides ITservices, Infrastructure Management Service to the Euro 20 Bn. TUI AG Group of Germany. TUI group has committed a Euro 670 Mn. of revenue to TUI Infotec over the next 5 years during 2006-2011 which includes a 40% cash penalty compensation clause for non fulfillment.

Key Positives for Sonata

- Acquisition at an attractive price with guaranteed future revenues
- Additional offshoring potential of Euro 21 Mn. (Rs.400 Mn.) over next 18-24 months
- Opens tremendous growth opportunity in the tough to penetrate but lucrative German market
- Evolution from a $100 Mn. to $250 Mn. run rate company & would benefit in RFP bidding criteria
- Learnings in the IMS segment (key strength of TUI Infotech; new focus of Sonata)

The Growth Ladder - Timeline

- Consolidation of JV's earnings – Immediate Impact
- Offshoring to Sonata Standalone entity (~Rs. 400 Mn. over 18-24 Months)– Near Term Impact
- Increased business from Euro 300 Mn. annual IT spend from TUI Group – Near to Medium Term Impact
- Further increase in outsourcing to Sonata Standalone entity – Medium Term Impact
- Business to JV from new clients in Germany & EU - Medium to Long Term Impact
- Growth opportunities for Sonata Standalone entity in IT Software Services space in European territories not demarked to the JV - Medium to Long Term Impact

Valuation

At CMP Rs. 60, Sonata is trading at 12x FY07E & 8.2x FY08E of Rs. 5.0 & Rs. 7.3 respectively. We maintain BUY.

Quarter Ended Dec '06
Result Update

Standalone Results

- 4.2 % drop in revenues sequentially to Rs. 451 M
- Modest 9.6% Y-Y increase in revenues
- OPM fall by 356 bps sequentially & by 163bps Y-Y to 22%
- PAT growth due to impact of negative taxation

Consolidated Results

- 89% Q-Q revenue growth incl. 2 Months impact of consolidation of TUI Infotech
- EBITDA up 125% Q-Q led by topline growth & margin expansion by 160 bps
- NP growth lower at 59% due to higher impact of depreciation & interest and contribution to minority shareholders
- Excluding the new acquisition Q-Q Revenues & Net Profit grew by 3% & 6% respectively

Revenues

Sequentially, the standalone revenue dropped by 4.2%, mainly on account of loss of 1 client. This said client has acquired another company, which operates an ODC at Hyderabad and would ergo, no longer require the services of Sonata.

At the consolidated level, the topline growth is spiked (89% Q-Q) on account of consolidation of 2 months revenues of TUI Infotech, which contributed Rs. 1289.80 Mn. to the revenues. Excluding the impact of this acquisition, the revenues have grown by 3% sequentially and 22% Y-Y.

Profits

Reported profits for Q3FY07 are up by 59% sequentially largely driven by inorganic growth. Excluding the profits from TUI Infotech, the comparable net net profit is up by 6%. Overall margins improved on account of consolidation of TUI Infotech, which earns ~15% EBITDA margins, which more than offsets the slight drop in normal business margins. Tax provisioning is lower on account of write-back of old provisioning.

Q4 Expectation

TUI Infotech has contributed Rs. 1,289.8 Mn. in revenues for Nov-Dec. For the fourth quarter, the incremental revenues could be in the region of Rs. 2,000 Mn.

Datapoints

Mix	FY04	FY05	FY06	9M 07
Onsite	38	26	26	32
Offshore	62	74	74	68
Geography	FY04	FY05	FY06	9M 07
US	41	50	45	46
Europe	59	50	55	54
Client Concentration	FY04	FY05	FY06	9M 07
Top 5	53	54	60	61
Next 5	13	15	16	15
Top 10	66	69	76	76
Balance	34	31	24	24
Manpower Strength	FY04	FY05	FY06	9M 07
Number of Employees	932	1,251	1,606	2,181

Quarterly Financials

(Rs. Mn)	Q3FY07	Q2FY07	Q-Q (%)	Q3FY06	Y-Y (%)	9MFY07	9MFY06	Y-Y (%)
Sales & Service	2,841.6	1,506.2	88.66%	1,274.5	122.96%	5,429.3	3,266.9	66.19%
Other Income	96.4	15.3	531.73%	10.4	826.85%	122.8	28.5	330.20%
Total Revenues	2,938.0	1,521.4	93.11%	1,284.9	128.66%	5,552.1	3,295.4	68.48%
Total Expenditure	2,604.5	1,373.1	89.69%	1,154.5	125.59%	4,926.4	2,984.1	65.09%
EBITDA	333.4	148.4	124.73%	130.4	155.80%	625.7	311.3	100.98%
Depreciation	107.9	32.1	236.52%	30.8	250.57%	170.1	76.8	121.36%
PBIT	225.5	116.3	93.90%	99.6	126.49%	455.6	234.5	94.30%
Interest	7.6	3.7	102.11%	2.0	270.54%	12.3	4.0	205.19%
PBT	217.9	112.6	93.63%	97.5	123.48%	443.3	230.5	92.36%
Tax	5.7	13.8	-58.99%	12.5	-54.51%	36.1	32.8	10.04%
PAT before MI	212.3	98.8	114.97%	85.1	149.53%	407.2	197.6	106.03%
Minority Interest	55.2	-		-		55.2	-	
PAT	157.1	98.8	59.09%	85.1	84.66%	352.0	197.6	78.11%
Reported PAT	157.1	98.8	59.09%	85.1	84.66%	352.0	197.6	78.11%
Equity Capital	105.2	105.2		105.2		105.2	105.2	
EPS (in Rs.)	1.5	0.9		0.8		3.3	1.9	
Particulars	Q3FY07	Q2FY07	Q-Q (bps)	Q3FY06	Y-Y (bps)	9MFY07	9MFY06	Y-Y (bps)
EBITDA %	11.35%	9.75%	159.7	10.14%	120.4	11.27%	9.45%	182.2
PBIT %	7.68%	7.64%	3.1	7.75%	(7.3)	8.21%	7.12%	109.1
PAT %	5.35%	6.49%	(114.3)	6.62%	(127.4)	6.34%	6.00%	34.3

Outlook

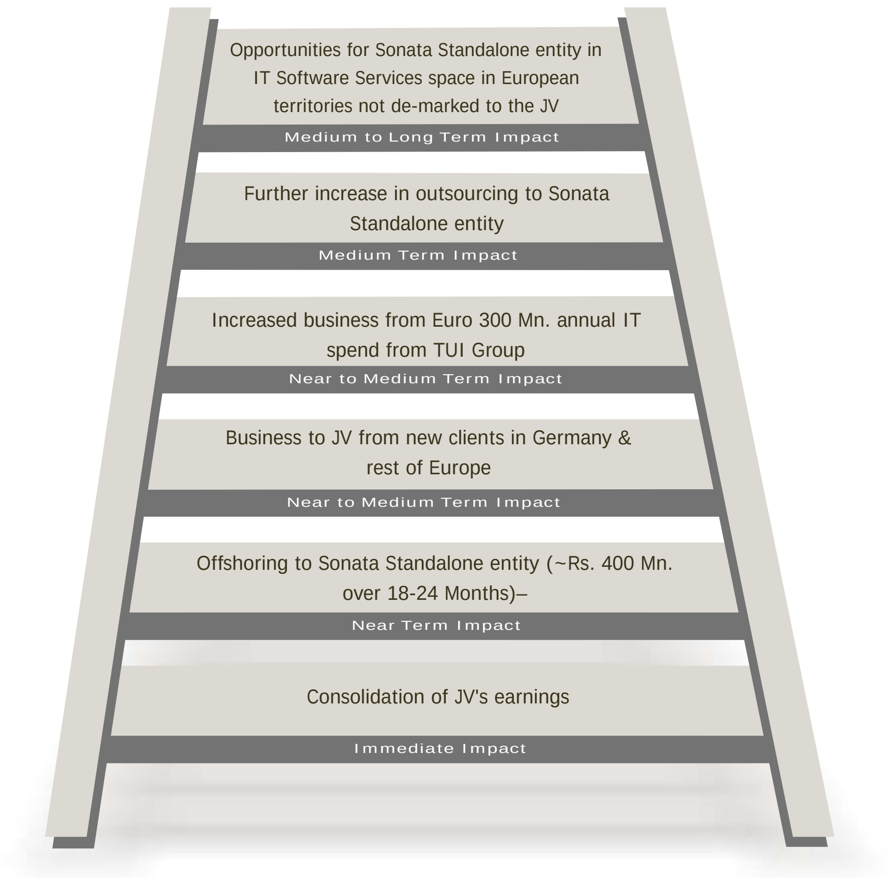
Robust outlook for Sonata going ahead

Sonata Software has recently bought 50.1% in TUI Infotec for Euro 18 Mn. or Rs.106 Crs. TUI Infotech earned revenues of Euro 130 Mn. & a net profit of Euro 6 Mn. in CY 2005. TUI Infotec provides IT services, Infrastructure Management Service to the Euro 20 Bn. TUI AG Group of Germany. TUI group has committed a Euro 670 Mn. of revenue to TUI Infotec over the next 5 years during 2006-2011 which includes a 40% cash penalty compensation clause for non fulfillment.

Key Positives for Sonata

- Acquisition at an attractive price with guaranteed future revenues
- Additional offshoring potential of Euro 21 Mn. plus (Rs.400 Mn.) over the next 18-24 months
- Opens tremendous growth opportunity in the tough to penetrate but lucrative German market
- Evolution from a $100 Mn. to $250 Mn. run rate company & would benefit in RFP bidding criteria
- Learnings in the IMS segment (key strength of TUI Infotech; new focus of Sonata)

The growth ladder - Timeline



Upward revision of near term earnings estimates

We have upwardly revised our FY07E EPS estimate from Rs. 4.4 to Rs. 5.0 (up by 15%) post reflection of the better than anticipated TUI performance. Sonata Software Limited has earned Rs. 352 Mn. of net profits for the nine month period ended December 2006. For the fourth quarter, we anticipate a bottomline of Rs. 180 Mn. We have kept our FY08E earnings guidance unchanged and would re-visit this, post some more visibility coming over the next few months. The management has guided that the JV would be targeting outside customer acquisition, as early as in CY07 itself. We have not captured any upside from these in our earnings estimates so far.

Recommendation

At CMP Rs. 60, Sonata is trading at 12x FY07E & 8.2x FY08E of Rs. 5.0 & Rs. 7.3 respectively. We maintain BUY.

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Sugar Industry: Tough times ahead

If the recent newspaper reports (Economic Times dated 7 March, 2007) are to be believed, the government is considering significant decontrol measures for the Indian Sugar Industry. The key changes that have been proposed are as follows:

- Removal of the cane support prices (Statutory Minimum Price).
- Abolishing the cane reservation area for the sugar factories.
- Removal of the levy quota for sugar.
- Doing away with the sugar release control mechanism.

The above-proposed measures if implemented would change the complete dynamics of the highly regulated sugar industry. This would drive consolidation in the sugar industry and improve the overall profitability of the sugar industry. The first two measures are too ambitious and their implementation seems to be a remote possibility. The implementation of the last two measures may not be such a big concern. In the current scenario and also in the long run the removal of the cane support prices would be in the best interest of the sugar companies which are facing the serious problem of the falling sugar prices. The sugar prices are declining to almost zero EBIDTA levels. The removal of the cane support prices would link the cane price to the sugar price cycle/industry-demand supply dynamics. Historically the sugar cane prices have always been on the rising trend but the sugar prices fluctuate according to the sugar production, demand and the closing inventory situation. The removal of the cane reservation area for the sugar factories would also be extremely difficult, as the sugar factories specially the smaller ones and the cooperative sugar factories, which contribute about 43% to the total sugar production, would oppose the move. Over the years, levy sugar percentage has been brought down from 70% to 10% and there is reasonable possibility of abolishing levy sugar. This would slightly improve the overall profitability of the sugar companies but in the current scenario when the sugar prices are declining and reaching close to the levy sugar prices this may not be of bigger help to the sugar companies. The lifting of the export ban completely will not be of any help to the sugar factories as the current global sugar prices rule out the viability of exports at present and the chances of the prices improving in the near future also seem to me almost nil. However in the future this measure would help the sugar factories to export sugar if the prices in the global market seem attractive.

Global Sugar Scenario

The global sugar prices have declined by more than 30% from their peak as global supply has expanded in response to spikes in sugar prices. The current sugar prices in the international market are in the range of $335-350 per ton. The global sugar prices lack triggers unless some radical changes occur like extreme change in the weather patterns of the major sugar producing nations like Brazil and India. The International Sugar Organisation (ISO) has estimated a higher global sugar surplus of 7.2 million tonnes for the year 2006-07. The ISO had in November, 2006 pegged the surplus at around 5.8 million tonnes. In its quarterly report released in February 2007, the ISO said global sugar output is estimated at 160.2 million tonnes against a consumption demand of 153 million tonnes. World consumption is projected to grow by 2.15%, only a fraction down from the 10-year average of 2.29%. For 2006/07, world export availability is projected to exceed import demand by more than 4 million tonnes, the organisation said.

Domestic sugar scenario

Domestic sugar prices have dropped by more than 20% since the beginning of the ongoing crushing season. With a bumper sugar production forecast in the current as well as for the sugar season 2007-08, the inventories have already started building up which is evident by the falling sugar prices. Currently, the sugar realizations for sugar factories in the north range from Rs 13500 to Rs 14000 per ton while for the south base mills the realizations range from Rs

Demand Supply scenario

	Unit	SS 2003-04	SS 2004-05	SS 2005-06	SS 2006-07 E	SS 2007-08 E
Cane acreage	'000 Hectares	3,938.0	3,662.0	4,198.0	4,545.0	4,659.0
Yield per hectare	MT/hectare	59.4	64.8	66.2	70.9	70.9
Cane production	Mn MT	233.9	237.3	277.9	322.2	330.3
Drawal rate	%	56.6	52.6	67.5	68.9	69.2
Cane crushed	Mn MT	132.5	124.8	187.6	221.9	228.5
Recovery	%	10.2	10.2	10.2	10.3	10.3
Sugar Production	Mn MT	13.5	12.7	19.1	22.9	23.5
Opening stock	Mn MT	12.5	8.5	4.5	3.8	4.8
Imports	Mn MT	0.6	2.0	0.5		-
Domestic consumption	Mn MT	17.9	18.6	19.2	19.9	20.5
Exports	Mn MT	0.2	-	0.9	1.5	1.8
Closing stock	Mn MT	8.5	4.6	4.0	5.3	6.0

Source: ISMA, CRISINFAC

13300 to Rs 13800 per ton. We don't see any improvement in the realizations in the near future (except for some abberations here and there to the efect of festive seasons) but a possibility of a further decrease in realizations cannot be ruled out. At sugar realizations of Rs 14000/ton and the sugar cane cost of Rs 1350 (Factory gate prices in Uttar Pradesh) per ton the EBIDTA of the sugar companies would be close to zero. The standalone players would be sverely hit and the situation would be no better for the integrated players as sugar contributes the most to the revenues.

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Investment Research

PPFAS

Bombay Rayon Fashions Limited

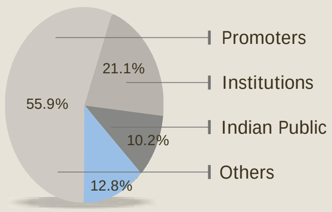
BUY | CMP Rs. 172.00 | Target : Rs. 230.

Stock Codes

Bloomberg	: BRFL.IN
Reuters	: BRFL.BO
BSE Code	: 532678
NSE Code	: BRFL
BSE Group	: B1

Share Holdings

(as on 31st Dec. 06)



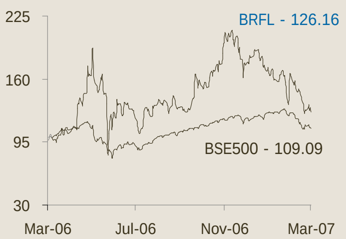
Stock Data

Benchmark	: BSE 500
52 W High Rs.	: 275.50
52 W Low Rs.	: 104.0
Mkt Cap in Mn.	: 11885.0
Face Value	: Rs. 10.0

Absolute Return

%	1m	3m	6m
BRFL	-7.33	-25.04	-0.12
BSE 500	-12.94	-11.93	-9.85

Price Comparison



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ppfas@bloomberg.net

From 6,000 garments per day to 64,000 garments per day in less than two years; Bombay Rayon Fashions Limited (BRFL) has catapulted to become the largest shirt manufacturer in India. Also, unlike most garment manufacturers, BRFL is vertically integrated with its own fabric processing capacity. This has been possible, mainly on account of BRFL's focus in the woven segment.

- Company has announced new capex plan up to Rs. 350 Crs for its core business
- Rs. 50 Crs equity contribution towards new Retail venture
- Rs. 50 Crs – BRFL's equity contribution towards 50:50 JV with Scott Fashions for SEZ venture

Growth Story

BRFL's achievement over the past few quarters is commendable. Firstly, it set-up the largest shirt capacities in the country at an extremely quick pace. Also it has established a decent size of clientèle (mostly top brands & labels & not just the large discount stores) in a very short time, in a new (export) market for a new product offering. On account of its vertical integration, the company boasts that it will have the shortest lead time in the industry.

The underlying chart in brief summarizes the expansion story for BRFL.

Particulars	Units	March 05	March 07	March 08
Yarn Dyeing	kgs/day	-	4,000	4,000
Weaving	looms	142	266	266
Processing	mtrs/day	-	93,999	281,997
Garments	pieces/day	6,000	64,000	150,000

Valuation & Recommendation

The scrip is trading at 12.5x FY08E and 7.9x FY09E earnings. The return ratios comfortably stabilize at over 15% and the leverage is just about 0.7x. Any concrete developments on the retailing & SEZ plans could be the future drivers for the share price. Based on our earnings estimates, we feel that the scrip could command Rs. 230 on the bourses.

Summary Financials

	Sales (Rs. Mn.)	EBITDA (%)	PAT (Rs. Mn.)	NPM (%)	EPS (Rs.)	P/E (x)	EV/EBITDA (x)	RONW (%)
FY06	1,989.8	17.4%	178.8	9.0%	3.7	47.1	28.2	11.7%
FY07E	4,141.7	24.2%	505.8	12.2%	7.3	23.5	19.0	8.3%
FY08E	8,227.6	21.3%	838.8	10.2%	12.1	14.2	10.5	12.3%
FY09E	13,080.1	21.7%	1,431.8	10.9%	20.7	8.3	6.5	17.8%

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Expansion Project

BRFL has now charted another leg of an ambitious expansion plan. The Rs. 350 Cr expansion plan would entail increase in the garmenting capacity from 64,000 units per day to 1,50,000 units per day, a whopping increase by 86,000 units per day. The fabric capacity would see a similar increase in the form of a greenfield 70 Mn. Meters per annum processing plant. With this capacity, BRFL will figure as one of the largest garment player in India, not only in volume terms but also in terms of absolute value.

This Rs. 350 Crs project will be funded through TUF loans & a QIP issue. BRFL has recently concluded a QIP issue, wherein it raised almost Rs. 300 Crs. The balance portion will get funded through TUF Loans.

BRFL allotted 14 Mn. equity shares @ Rs. 210 per share raising a total of Rs. 2,944.27 Mn.; these proceeds to be utilized to part fund the core business expansion project. The balance will go towards the company's new retailing & SEZ initiatives in equal proportion.

Capex	Rs. Mn.
Fabric Processing (70 Mn. Mtrs. p.a.)	1,600
Garments (86,000 pcs per day)	1,470
Power Plant (6.5 MW)	230
Working Capital Margin	200
Retail Subsidiary (Equity)	500
SEZ JV (Equity)	500
Total	4,500

Domestic Retail Foray

BRFL has decided to make an entry into the domestic branded retail market. BRFL will set-up a new company with an initial seed capital of Rs. 50 Crs and similar funding from bank borrowings. The company will open 25 stores in the first phase in the Tier 1 cities by March 08. These will be large 5,000-10,000 square feet fashion stores, modeled somewhat in lines with Zara, with say 6 season collections within affordable range. The company will have to spend towards brand building and would take about two years for each store to break even. More concrete details on this front will be available only by June 07.

SEZ Plans

BRFL is tying up with Bangalore based Scott Fashions (Knits) to setup a 1000 acre SEZ at a plot identified at Whitefield Road in Bangalore. BRFL will invest Rs. 50 Crs as its equity contribution for this 50:50 JV. The JV would sell almost 900 acres of land to outsiders and the balance would be available to the two JV partners for their independent expansion plans. BRFL management expects the government approval to come in the current fiscal. The land acquisition process however, may take time.

Rs. 50 Crs each needed for the retailing & SEZ initiatives is funded from the QIP issue. In our estimates, we have accounted for the QIP receipt and investments in these two new initiatives. No other income or expenses have been accounted for these at this stage.

Equity Dilution

The equity capital stands increased on account of the recently concluded QIP issue. In order to maintain their share at over 51%, promoters have been issued 6.1 Mn. Warrants convertible into equivalent number of equity shares at a price of Rs. 207.

Risks

Lower than estimated capacity utilization or lower comparable realization would have a direct impact on the profitability.

The new plan envisages huge capacity addition. Fabric capacity increased by another 70 Mn. Meters annually over presently less than 50 Mn. Meters per annum. Additional garmenting capacity of 86,000 pieces per day on top of the current 64,000 pieces per day to total a whopping 1,50,000 pieces per day. Ergo, modest delays, even by a quarter would cause significant change in our earnings estimates and consequently valuations.

Retailing venture would require substantial initial investment towards property acquisition for store set-up and also for brand building. Generally, a store achieves break-even in two years time frame. Thus there would be initial strain on the cash flows.

SEZ – This again is a high gestation venture. Acquiring land including some farm lands will not be easy. Even otherwise the entire project would take over a couple of years to come into existence and flourish to generate good revenues for the company.

Being largely an export oriented company, BRFL is exposed to significant forex risks.

Assumptions

Garment Production

Garment (Pieces per day)	Commercial Production	Installed Capacity FY09	Production		
			FY07E	FY08E	FY09E
Unit 1	– March 05	3,000	2,550	2,550	2,550
Unit 2	– March 05	3,000	2,550	2,550	2,550
Unit 3	– October 05	8,000	6,400	6,800	6,800
Unit 4	– March 06	26,000	16,900	22,100	22,100
Unit 5	– March 06	2,000	1,125	1,700	1,700
Unit 6	– January 07	22,000	-	13,200	16,500
Unit 7	– September 07	86,000	-	17,200	64,500
Total		150,000	29,525	66,100	116,700

Fabric Production

Fabric – (Mtrs. Per annum)	FY07E	FY08E	FY09E
Fabric - Purchased	18.90	51.46	81.21
Fabric - Mnfg at Mumbai	12.24	12.24	12.24
Fabric - Mnfg at Bangalore	4.72	6.29	6.29
Sub - Total	35.87	69.99	99.74
Less : Internal Consumed	18.68	41.70	67.50
Fabric - Sold	17.19	28.29	32.24

Realisation

Average Realization	FY07E	FY08E	FY09E
Fabric (Rs. / Mtr.)	99.00	93.00	92.00
Garments (Rs. / Piece)	285.00	290.70	296.51

Margins

We have assumed 13% margins for fabrics and 23% for garments on net revenues.

Valuation & Recommendation

Based on our assumptions stated earlier, we envisage that the scrip is trading at 12.5x FY08E and 7.9x FY09E earnings. The growth in EPS is excellent, notwithstanding the increase in equity. The return ratios comfortably stabilize at over 15% and the leverage is just about 0.7.

Factoring that the expansion goes smoothly, the earnings growth would be excellent. Also any concrete developments on the retailing & SEZ plans could be the future drivers for the share price. However, the risks as mentioned above are critical. Based on our earnings estimates, we feel that the scrip could command Rs. 230 on the bourses.

Quarterly Financials

(Rs. Mn)	Q3FY07	Q2FY07	Q-Q (%)	Q3FY06	Y-Y (%)	9MFY07	9MFY06	Y-Y (%)
Net Sales	1,316.2	1,032.6	27.5%	549.3	139.6%	3,161.0	1,409.5	124.3%
Total Expenditure	1,041.7	833.1	25.0%	461.8	125.6%	2,533.9	1,190.1	112.9%
Operating Profit	274.5	199.5	37.6%	87.5	213.6%	627.1	219.4	185.8%
Other Income	11.4	12.8	-11.2%	2.3	399.6%	27.3	4.8	466.9%
EBITDA	285.8	212.3	34.6%	89.8	218.3%	654.4	224.3	191.8%
Depreciation	35.1	14.6	141.1%	9.6	267.2%	62.3	24.0	159.2%
PBIT	250.7	197.7	26.8%	80.2	212.5%	592.1	200.2	195.8%
Interest	42.6	31.1	37.1%	18.5	130.2%	94.0	39.9	135.8%
PBT	208.2	166.7	24.9%	61.8	237.1%	498.2	160.3	210.7%
Tax	70.6	55.9	26.3%	5.6	1156.3%	169.5	14.6	1060.4%
PAT	137.6	110.8	24.2%	56.1	145.1%	328.7	145.7	125.5%
Equity Capital	489.8	489.8		489.8		489.80	489.8	
EPS (in Rs.)	2.8	2.3		1.1		6.7	3.0	
Profitability								
OPM %	20.9%	19.3%	153.5	15.9%	492.0	19.8%	15.6%	427.1
EBITDA %	21.7%	20.6%	115.8	16.3%	537.0	20.7%	15.9%	479.3
PBIT %	19.1%	19.1%	- 9.9	14.6%	444.3	18.7%	14.2%	453.1
PAT %	10.5%	10.7%	- 27.5	10.2%	23.4	10.4%	10.3%	5.9
Operational Parameters								
RM Consumed	60.5%	60.4%	9.6	62.6%	- 209.0	60.4%	60.8%	- 41.6
Staff Cost	6.8%	8.8%	- 193.4	4.2%	263.2	7.8%	4.1%	367.1
Jobwork Chgs	5.8%	4.6%	122.7	9.3%	- 345.2	5.7%	10.7%	- 500.8
Other Expenditure	6.0%	6.9%	- 92.5	8.0%	- 201.0	6.3%	8.8%	- 251.8

Summary Financials

	Sales (Rs. Mn.)	EBITDA (%)	PAT (Rs. Mn.)	NPM (%)	EPS (Rs.)	P/E (x)	EV/EBITDA (x)	RONW (%)
FY06	1,989.8	17.4%	178.8	9.0%	3.7	47.1	28.2	11.7%
FY07E	4,141.7	24.2%	505.8	12.2%	7.3	23.5	19.0	8.3%
FY08E	8,227.6	21.3%	838.8	10.2%	12.1	14.2	10.5	12.3%
FY09E	13,080.1	21.7%	1,431.8	10.9%	20.7	8.3	6.5	17.8%

Financials

Earnings Statement				
YE March (Rs. Mn.)	FY06	FY07E	FY08E	FY09E
Net Sales	1,989.8	4,141.7	8,227.6	13,080.1
Total Expenditure	1,657.5	3,355.9	6,593.1	10,362.3
Operating Profit	332.3	785.8	1,634.5	2,717.7
Other Income	13.7	217.1	117.1	117.1
EBITDA	346.0	1,002.9	1,751.7	2,834.9
Depreciation	29.9	76.6	233.6	321.1
EBIT	316.2	926.4	1,518.1	2,513.8
Interest	64.5	160.0	247.2	344.5
PBT	251.7	766.4	1,270.9	2,169.3
Tax	72.8	260.6	432.1	737.6
PAT	178.8	505.8	838.8	1,431.8

Ratio Analysis				
YE March (Rs. Mn.)	FY06	FY07E	FY08E	FY09E
OPM (%)	16.7%	19.0%	19.9%	20.8%
EBITDA (%)	17.4%	24.2%	21.3%	21.7%
PBIT (%)	15.9%	22.4%	18.5%	19.2%
PAT (%)	9.0%	12.2%	10.2%	10.9%
Interest Cover	4.9	5.8	6.1	7.3
EPS (Rs.)	3.7	7.3	12.1	20.7
P/E (x)	47.1	23.5	14.2	8.3
P/BV (x)	5.5	1.9	1.7	1.5
BVPS (Rs.)	31.3	88.6	98.4	116.2
Market Cap (Rs. Mn.)	8,424.5	11,885.2	11,885.2	11,885.2
M Cap/Sales (x)	4.2	2.9	1.4	0.9
EV (Rs. Mn.)	9,374.4	14,935.2	17,087.7	17,635.2
EV/EBITDA (x)	28.2	19.0	10.5	6.5
EV/Sales (x)	4.7	3.6	2.1	1.3
ROCE (%)	12.7%	10.0%	12.4%	17.6%
RONW (%)	11.7%	8.3%	12.3%	17.8%
Debt/Equity (x)	0.6	0.5	0.8	0.7
Inventory T/o Days	152.9	150.0	150.0	150.0
Debtors T/o Days	63.5	63.0	63.0	63.0
Advances T/o Days	52.7	33.0	33.0	33.0
Creditors T/o Days	56.2	70.0	60.0	60.0
Working Cap T/o Days	218.6	161.4	172.3	170.8
Fixed Assets T/o (Gross)	2.5	1.4	1.3	2.0
DPS (Rs.)	1.0	1.5	2.0	2.5
Dividend Payout (%)	27.4%	20.5%	16.5%	12.1%
Dividend Yield (%)	0.6%	0.9%	1.2%	1.5%

Balance Sheet				
YE March (Rs. Mn.)	FY06	FY07E	FY08E	FY09E
Equity Capital	489.8	691.0	691.0	691.0
Reserves	1,040.9	5,431.2	6,108.4	7,338.0
Shareholders Funds	1,530.7	6,122.2	6,799.4	8,029.0
Borrowed Funds	949.9	3,050.0	5,202.5	5,750.0
Deferred Tax Liability	14.9	99.2	239.0	477.6
Total Liabilities	2,495.5	9,271.4	12,240.9	14,256.6
Fixed Assets	1,204.4	3,097.2	6,013.7	5,792.6
Investments	99.2	4,342.8	2,342.8	2,342.8
Current Assets				
Inventory	833.5	1,702.1	3,381.2	5,375.4
Sundry Debtors	346.2	714.9	1,420.1	2,257.7
Loans & Advances	287.1	374.5	743.9	1,182.6
Cash & Bank Balance	117.5	57.5	71.6	59.8
Current Liabilities				
Sundry Creditors	306.3	794.3	1,352.5	2,150.2
Provisions	86.0	223.1	379.9	604.0
Net Current Assets	1,191.9	1,831.4	3,884.4	6,121.2
Misc Expenditure	-	-	-	-
Total Assets	2,495.5	9,271.4	12,240.9	14,256.6

Cash Flow				
Particulars	FY06	FY07E	FY08E	FY09E
Opening Cash & Bank	8.7	117.5	57.5	71.6
Profit After Tax	178.8	505.8	838.8	1431.8
Less : Invt Income	(13.7)	(217.1)	(117.1)	(117.1)
Depreciation	29.9	76.6	233.6	321.1
Deferred Taxation	11.6	84.3	139.8	238.6
Others	(72.9)	0.0	0.0	0.0
Change in Working Cap	(647.5)	(699.5)	(2038.8)	(2248.7)
CF - Operating Activities	(513.8)	(250.0)	(943.8)	(374.4)
Change in Fixed Assets	(938.6)	(1969.4)	(3150.0)	(100.0)
Change in Investments	(98.0)	(4243.6)	2000.0	0.0
Investment Income	13.7	217.1	117.1	117.1
CF - Investing Activities	(1022.8)	(5995.9)	(1032.9)	17.1
Increase in Equity	1024.0	4207.0	0.0	0.0
Changes in Borrowings	677.3	2100.1	2152.5	547.5
Dividend Paid	(55.8)	(121.3)	(161.7)	(202.1)
CF - Financing Activities	1645.5	6185.8	1990.8	345.4
Net Change in Cash	108.8	(60.0)	14.2	(11.9)
Closing Cash & Bank Bal	117.5	57.5	71.6	59.8

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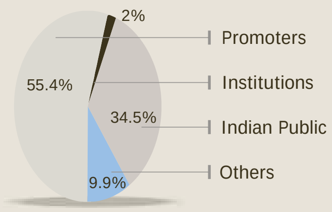
Kitex Garments Limited

BUY | CMP Rs. 9.17

Stock Codes

Bloomberg	: KTG.IN
Reuters	: KITE.BO
BSE Code	: 521248
NSE Code	: -
BSE Group	: B2

Share Holdings
(as on 31st Dec. 06)



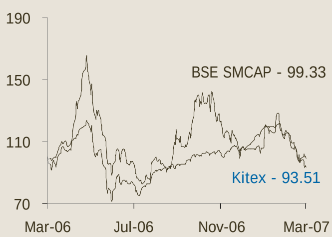
Stock Data

Benchmark	: BSE Small Cap
52 W High Rs.	: 16.6
52 W Low Rs.	: 7.8
Mkt Cap in Mn.	: 580.0
Face Value	: Rs. 1.0

Absolute Return

%	1m	3m	6m
Kitex	-17.28	-10.75	-15.81
BSE SMCAP	-14.24	-12.65	-10.52

Price Comparison



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Kitex Garments Limited (KGL) is a Kochi based fast growing garmenting company with a key focus on kids wear. Kitex has recently ramped up its garmenting capacity to 2,00,000 pieces per day and is currently expanding backward to manufacture processed knit fabrics. On the back of its world-class facilities and efficient production management, the company has already evolved as a preferred supplier to the international buyers.

KGL is currently in the midst of its backward integration project. The company is setting up India's largest knitting cum processing plant with an initial installed capacity of 27 TPD, with provision to further expand upto 45 TPD at the same place.

Business Ideology

In its attempt to be a leading supplier of garments to international retailers, KGL has been following a focused strategy.

- Investment in Infrastructure & Social Compliance for eligibility & business growth
- Thrust on Scale & Efficiency for economies & profitability
- Concentration on a niche area instead of undertaking unwarranted diversifications
- Increase competitiveness rather than being another 'me too' player.
- The aforementioned strategy coupled with the locational advantage (nearest international airport & sea port both within 25 kilometers distance), should enable
- Kitex to thrive on the current textile boom.

Recommendation

At the CMP of Rs. 9.17, the scrip trades at 5.32 times its FY07E earnings of Rs. 1.7 per share. On forward estimates, it is extremely attractive at just 2.3 times its FY09 EPS of Rs. 4. All other valuation parameters also reflect an extremely attractive proposition. With sustained ROE at 30%, Market Cap/ Sales of ~ 0.2x , 2.5 times EV/EBITDA and large growth potential, it is extremely cheap and more than discounts any concerns whatsoever. BUY.

Summary Financials

	Revenues (Rs. Mn.)	EBITDA (%)	PAT (Rs. Mn.)	NPM (%)	EPS (Rs.)	P/E (x)	EV/ EBITDA (x)	Mkt Cap/ Sales (x)	RONW (%)
FY05	795.9	9.4%	26.2	3.3%	0.6	19.9	10.7	0.7	27.9%
FY06	1,116.0	10.0%	44.3	4.0%	0.9	11.8	8.0	0.5	33.3%
FY07E	1,621.1	12.9%	81.9	5.1%	1.7	6.4	4.7	0.3	39.0%
FY08E	1,827.2	16.6%	134.2	7.3%	2.8	3.9	4.0	0.3	39.6%
FY09E	2,236.4	17.5%	191.9	8.6%	4.0	2.7	2.7	0.2	36.6%

Introduction

Kitex Garments Limited (KGL) is a Kochi based fast growing garmenting company with a key focus on kids wear. On the back of its world-class facilities and efficient production management, the company has already evolved as a preferred supplier to the international buyers.

Scale & Infrastructure

Having set up its huge infrastructure early on, KGL has been ramping up its production capacities at a brisk pace. The company has recently added more capacity, which will increase the number of production lines to 42. With each line able to produce 4,200 pieces per day at optimum utilization, the total production capacity will increase to ~2,00,000 pieces per day per shift. KGL is currently in the midst of its backward integration project. The company is setting up India's largest knitting cum processing plant with an initial installed capacity of 27 TPD, with provision to further expand upto 45 TPD at the same place.

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Operational Management

A critical factor favouring KGL is its ability to manage efficiency with scalability in its labour intensive business. Efficiency in case of KGL is a function of its product focus and its system driven processes. KGL maintains high standards of social compliance. Its fully air-conditioned manufacturing facility also provides for quality food & accommodation facilities to all its employees. In turn, KGL enjoys almost nil absenteeism, least possible employee turnover & high productivity. KGL's sustained capacity utilization at over 90% is amongst the highest in the industry. Clever manpower management is also reflected in the fact that Kitex Garments (since its incorporation in 1992) the entire Kitex Group (established in 1968) has not experienced a single strike, notwithstanding its entire setup in the predominantly communist state of Kerala.

Revision in our Estimates

We have revised our earnings estimates on account of the delay in commissioning of the processing facility. As per our discussion with the management, we understand that, while a few machines would start functioning by end of February 2007, the plant would be functional in entirety only by May – June. We have incorporated earnings from this new facility from H2FY08 in our calculations.

We have incorporated our initial FY09E earnings estimates. The garment capacity has been taken as constant. The growth ahead is primarily reflected on account of gradual improvement in the capacity utilization from the new fabric facility. Also we have accounted for the cost of borrowings at a higher rate in lines with the market trend.

Conflict of Interest

Kitex group operates its garment business through two companies, Kitex Garment Ltd (KGL) and Kitex Childrenware Ltd (KCL). The size of both the companies is similar. The management has indicated that they may integrate the two companies in the coming times.

Q307 Performance Review

Kitex Garments Ltd has reported excellent results for the third quarter of FY 2007.

Result Highlights :

- Sales higher by 74% at Rs. 368 Mn.
- EBITDA grew by 171% from Rs. 22 Mn. to Rs. 58 Mn.
- PAT up 143% to Rs. 30 Mn.
- PAT growth lower on account of higher Interest cost
- Interest costs increases ~4 fold from Rs. 4 Mn to Rs. 16 Mn.

Quarterly Financials

(Rs. Mn.)	QE Dec 06	QE Dec 05	Y-Y (%)	9M FY07	9M FY06	Y-Y (%)
Net Sales	367.6	211.5	73.8%	1,160.0	805.9	43.9%
Total Expenditure	332.1	205.3	61.7%	1,067.2	757.2	40.9%
Operating Profit	35.6	6.2	475.3%	92.8	48.6	90.9%
Other Income	22.7	15.3	48.6%	69.3	48.3	43.6%
EBITDA	58.3	21.5	171.4%	162.1	96.9	67.3%
Depreciation	5.7	2.3	144.6%	14.0	8.1	73.1%
PBIT	52.6	19.2	174.7%	148.1	88.8	66.8%
Interest	16.1	4.2	283.4%	38.5	17.8	116.3%
PBT	36.5	14.9	144.0%	109.6	71.0	54.4%
Tax	6.3	2.5	149.2%	26.2	20.2	29.9%
PAT	30.1	12.4	143.0%	83.4	50.8	64.1%
Equity Capital	47.5	47.5	0.0%	47.5	47.5	0.0%
EPS (in Rs.)	0.63	0.26	143.0%	1.76	1.07	64.1%

Particulars (%)	QE Dec 06	QE Dec 05	Y-Y (bps)	9M FY07	9M FY06	Y-Y (bps)
Profitability						
OPM %	9.7%	2.9%	675.0	8.0%	6.0%	196.9
EBITDA %	15.9%	10.2%	570.2	14.0%	12.0%	195.3
PBIT %	14.3%	9.1%	525.3	12.8%	11.0%	175.0
PAT %	8.2%	5.9%	233.2	7.2%	6.3%	88.3
Operational Parameters						
RM Consumed	68.8%	71.0%	(220.8)	71.0%	73.1%	(206.2)
Staff Cost	17.3%	18.1%	(75.8)	17.1%	15.6%	145.7
Other Expenditure	4.2%	8.0%	(378.4)	3.9%	5.3%	(136.3)
Effective Tax Rate	17.4%	17.0%	36.2	23.9%	28.4%	(450.8)

Recommendation

At the CMP of Rs. 9.17, it is extremely attractive at just 2.3 times its FY09 EPS of Rs. 4. All other valuation parameters also reflect an extremely attractive proposition. We continue to be optimistic on this extremely competent company and maintain BUY.

Financials

Particulars (Rs. Mn.)	FY06	FY07E	FY08E	FY09E
Net Sales	1,058.3	1,540.0	1,740.1	2,150.4
Other Operating Income	57.7	81.2	87.0	86.0
Total Revenues	1,116.0	1,621.1	1,827.2	2,236.4
Total Expenditure	1,004.3	1,412.2	1,523.2	1,844.2
Operating Profit	111.7	209.0	304.0	392.2
EBITDA	111.7	209.0	304.0	392.2
Depreciation	14.3	22.6	43.8	48.5
EBIT	97.4	186.3	260.2	343.7
Interest	23.5	55.3	45.5	36.6
EBT	73.9	131.0	214.7	307.1
Tax	29.6	49.1	80.5	115.2
Net Profit	44.3	81.9	134.2	191.9
Dividend Paid	5.4	5.4	5.4	5.4

Ratios	FY06	FY07E	FY08E	FY09E
OPM (%)	10.0%	12.9%	16.6%	17.5%
EBITDA (%)	10.0%	12.9%	16.6%	17.5%
PBIT (%)	8.7%	11.5%	14.2%	15.4%
PAT (%)	4.0%	5.1%	7.3%	8.6%
Interest Cover Ratio	4.1	3.4	5.7	9.4
EPS	0.9	1.7	2.8	4.0
Book Value per share	2.8	4.4	7.1	11.1
Market Cap	435.6	435.6	435.6	435.6
Enterprise Value	803.5	893.5	1,143.5	988.7
P/E	9.8	5.3	3.2	2.3
P/BV	3.3	2.1	1.3	0.8
M Cap/Sales	0.4	0.3	0.3	0.2
EV/EBITDA	7.2	4.3	3.8	2.5
EV/Sales	0.8	0.6	0.7	0.5
ROCE (%)	18.6%	25.7%	22.5%	27.2%
RONW (%)	33.3%	39.0%	39.6%	36.6%
Debt/Equity Ratio	2.8	2.2	2.1	1.1
Inventory T/o Days	39.5	40.0	40.0	40.0
Debtors T/o Days	60.7	60.0	60.0	60.0
Advances T/o Days	21.3	25.0	25.0	25.0
Creditors T/o Days	42.3	57.0	57.0	57.0
Net Wrkg Cap T/o Days	75.3	59.3	58.0	60.8
Fixed Assets T/o (Gross)	3.8	3.2	1.9	2.1
DPS (Rs.)	0.1	0.1	0.1	0.1
Dividend Payout (%)	10.7%	5.8%	3.5%	2.5%
Dividend Yield (%)	1.1%	1.1%	1.1%	1.1%

Balance Sheet (Rs. Mn.)	FY06	FY07E	FY08E	FY09E
Equity Capital	47.5	47.5	47.5	47.5
Reserves	85.8	162.3	291.0	477.5
Borrowed Funds	367.9	457.9	707.9	553.1
Deferred Tax Liability	24.1	56.8	110.5	187.3
Total Liabilities	525.3	724.5	1,156.9	1,265.5
Fixed Assets	306.8	474.3	880.5	907.0
Current Assets				
Inventory	108.8	154.8	166.9	202.1
Sundry Debtors	176.1	253.1	286.1	353.5
Loans & Advances	58.6	96.7	104.3	126.3
Cash & Bank Balance	20.1	20.6	15.8	35.7
	363.6	525.3	573.1	717.6
Current Liabilities				
Sundry Creditors	116.4	220.5	237.9	288.0
Provisions	28.8	54.5	58.8	71.2
	145.2	275.1	296.7	359.2
Net Current Assets	218.4	250.2	276.4	358.4
Miscellaneous Expenditure	-	-	-	-
Total Assets	525.3	724.5	1,156.9	1,265.5

Particulars	FY06E	FY07E	FY08E	FY09E
Opening Cash & Bank Bal	89.2	20.1	20.6	15.8
Profit After Tax	44.3	81.9	134.2	191.9
Investment Income Adj	0.0	0.0	0.0	0.0
Interest Paid Adj	23.5	55.3	45.5	36.6
Depreciation	12.4	22.6	43.8	48.5
Deferred Taxation	5.3	32.8	53.7	76.8
Others	-	-	-	-
Net Change in Wrkg Cap	(121.9)	(31.2)	(31.1)	(62.1)
CF - Operating Activities	(36.4)	161.3	246.1	291.7
Change in Fixed Assets	(173.0)	(190.1)	(450.0)	(75.0)
Change in Investments	0.0	-	0.0	0.0
Investment Income	0.0	0.0	0.0	0.0
CF - Investing Activities	(173.0)	(190.1)	(450.0)	(75.0)
Increase in Equity	0.0	-	-	-
Changes in Borrowings	169.2	90.0	250.0	(154.8)
Interest Paid	(23.5)	(55.3)	(45.5)	(36.6)
Dividend Paid	(5.4)	(5.4)	(5.4)	(5.4)
CF - Financing Activities	140.3	29.3	199.0	(196.8)
Net Change in Cash	(69.1)	0.5	(4.9)	19.9
Closing Cash & Bank Bal	20.1	20.6	15.8	35.7

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PERFORMANCE REVIEW

S.NO.	COMPANY	RECOMM. PRICE	DATE	CURR. PRICE	RETURN % (ABS.)	RETURN % (ANN.)	POST REC. HIGH (RS.)	CURRENT RECOMM.
1	Agrotech Foods	129.0	Feb 10, 06	78.65	(39.03)	(35.98)	171.00	SELL
2	Ashok Leyland	35.0	Jun 8, 06	41.00	17.14	22.51	51.00	BUY
3	Banswara Syntex *	64.0	Feb 10, 06	63.70	(0.47)	(0.43)	129.00	BUY
4	Bombay Rayon	125.0	Mar 27, 06	171.55	37.24	38.73	275.00	BUY
5	Bharat Electronics	900.0	Dec 7, 05	1,511.20	67.91	53.77	1,794.00	BUY
6	Britannia Ind.	1,191.0	Feb 23, 07	1,281.50	7.60	154.08	1,350.00	ACCUMULATE
7	Castrol India	170.0	Jun 12, 06	215.20	26.59	35.42	285.00	HOLD
8	Cosmo Films	72.0	Feb 9, 06	73.65	2.29	2.11	123.00	HOLD
9	Gokaldas Exports *	347.0	Feb 10, 06	246.50	(28.96)	(26.70)	395.00	BUY
10	Heritage Foods	168.0	Feb 10, 06	247.40	47.26	43.56	466.00	SELL
11	Infosys Tech. *	1,432.0	Feb 10, 06	2,105.65	47.04	43.36	2,439.00	BUY
12	Infotech Enter. *	74.0	Feb 21, 05	352.90	376.89	183.42	447.00	HOLD
13	Kitex Garments	16.0	May 10, 06	9.17	(42.69)	(50.75)	16.59	BUY
14	Mphasis BFL	141.0	Jul 13, 06	276.05	95.78	143.87	329.00	ACCUMULATE
15	Maruti Udyog	918.0	Apr 27, 06	803.80	(12.44)	(14.19)	991.00	BUY
16	Matrix Labs	222.0	Jan 12, 07	159.65	(28.09)	(170.85)	238.00	BUY
17	NIIT Techno.	122.0	Apr 25, 05	445.45	265.12	140.86	535.00	ACCUMULATE
18	Orient Paper	137.0	Jul 7, 05	404.15	195.00	115.92	667.00	HOLD
19	Pantaloon *	356.0	Feb 10, 06	361.00	1.40	1.29	527.00	SELL
20	Punjab National Bank	445.0	Feb 10, 06	438.95	(1.36)	(1.25)	585.00	BUY
21	Rain Calcining	42.0	Oct 19, 05	37.85	(9.88)	(7.07)	57.00	BUY
22	Rain Commodities	23.0	Feb 7, 05	118.30	414.35	197.95	210.00	HOLD
23	SSI Ltd.	119.0	Feb 10, 06	180.35	51.55	47.52	248.00	HOLD #
24	S Kumars	20.0	Mar 24, 05	67.95	239.75	121.71	84.00	HOLD
25	Satnam Overseas	89.0	Feb 10, 06	69.65	(21.74)	(20.04)	112.00	HOLD
26	Satyam Comp. *	366.0	Feb 8, 06	452.15	23.54	21.59	525.00	BUY
27	State Bank of india	880.0	Feb 10, 06	980.70	11.44	10.55	1,379.00	HOLD
28	Sonata Software	34.0	Nov 16, 06	59.60	75.29	234.89	74.00	BUY
29	Syngenta	435.0	Apr 4, 06	460.40	5.84	6.21	516.00	HOLD ##
30	Tata Motors	700.0	Jul 18, 06	773.20	10.46	16.04	975.00	BUY
31	VST Industries	484.0	Feb 10, 06	331.00	(31.61)	(29.14)	534.00	BUY
32	Wyeth Labs	763.0	Feb 8, 06	467.10	(38.78)	(35.57)	780.00	HOLD

* Adjusted Prices

Open offer for delisting expected in April 2007

Open offer from acquirer (@ Rs. 208) expected in Q1 FY08

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