



Economy News

- ▶ India and the US may sign a memorandum of understanding (MoU) on sharing technology for shale gas exploration when US President Barack Obama visits the country next month. India will also launch its first shale gas auction round by December 2011. "We are evolving a policy framework for shale gas and the first shale gas round is planned for end-2011," Petroleum Secretary S Sundareshan said. (BS)
- ▶ The government on Monday said it would not free diesel prices from its control in hurry as the move would lead to sharp rise in price of fuel most used in the transport sector. "There is no thinking at this juncture to move any further," Oil Secretary S Sundareshan told reporters. (ET)
- ▶ The decision on opening sugar exports is likely only by February 2011, as an inflation-scarred government would prefer to wait for the more reliable second advance crop estimates. Both the industry and the government have put out gung-ho estimates of sugar production for 2010-11 but there is still some unease over freeing controls. (ET)

Corporate News

- ▶ **Biocon Ltd** signed a mega marketing deal with the world's largest drug-maker Pfizer on Monday to globally commercialise four of its insulin biosimilar products initially. Pfizer will upfront pay \$200 million (around Rs 9bn) for the exclusive world rights. In India, Malaysia and Germany, the two partners will sell these products separately as their respective brands. Biocon can also get an additional \$150 million as development and regulatory milestone payments; besides payments linked to Pfizer's sales of these products. (BL)
- ▶ In a major relief for the Vedanta Resources Group's **Sterlite Industries**, the Supreme Court on Monday extended till the second week of December its earlier stay on closure of the company's copper smelter at Tuticorin (BL)
- ▶ **Indian Oil Corp (IOC)** will start shortlisting merchant bankers next week for its public issue that is likely to raise about Rs 190bn, making it the largest-ever equity offer in the country, three government officials and a company executive said. Half the proceeds would go to the government, which will offload 10% of IOC shares to help it meet its disinvestment target of Rs 400bn this fiscal. In addition, the company will issue new shares amounting to another 10% of its equity capital to help the country's largest state refiner build new units. (ET)
- ▶ **Larsen & Toubro** has appointed Ravi Uppal, the head of its power arm, as a director on the board of the parent engineering company, a move that some see as a precursor to his ascension to the top job. Mr Uppal, 57, is widely seen as one of the strongest contenders for the post of chairman of the company. The incumbent, the high-profile AM Naik, retires in September 2012, and a successor has not been publicly identified. An L&T spokesman did not comment on the succession issue. (ET)
- ▶ **Adani Enterprises** will invest \$6.9 billion in developing its recently acquired Australian coal mines, the company said on Monday. The acquisition is one of the largest coal mine deals by an Indian group. The company in August bought the coal mine for about Rs 126bn in a cash and royalty deal. (ET)

Equity

	18 Oct 10	% Chg		
		1 Day	1 Mth	3 Mths
Indian Indices				
SENSEX Index	20,169	0.2	2.9	12.5
NIFTY Index	6,076	0.2	3.2	12.8
BANKEX Index	14,026	(0.2)	2.0	22.8
BSET Index	6,153	1.3	5.3	13.0
BSETCG INDEX	15,964	0.4	2.9	6.1
BSEOIL INDEX	10,782	0.8	0.4	2.8
CNXMcap Index	9,317	(0.3)	1.7	10.6
BSESMCAP INDEX	10,614	(0.1)	3.7	12.2
World Indices				
Dow Jones	11,144	0.7	5.1	9.7
Nasdaq	2,481	0.5	7.1	12.8
FTSE	5,743	0.7	4.2	11.5
Nikkei	9,498	(0.0)	(0.8)	1.5
Hangseng	23,469	(1.2)	7.2	17.2

Value traded (Rs cr)

	18 Oct 10	% Chg - Day
Cash BSE	4,210	(11.0)
Cash NSE	16,254	1.4
Derivatives	140,929	2.2

Net inflows (Rs cr)

	15 Oct 10	% Chg	MTD	YTD
FII	654	(77.4)	18,107	106,391
Mutual Fund	(1,085)	171.7	(4,746)	(27,502)

FII open interest (Rs cr)

	15 Oct 10	% Chg
FII Index Futures	16,246	3.1
FII Index Options	63,289	(0.1)
FII Stock Futures	44,869	1.3
FII Stock Options	1,292	(1.8)

Advances / Declines (BSE)

	18 Oct 10	A	B	S	Total	% total
Advances	83	735	181	999	39	
Declines	118	1095	216	1,429	56	
Unchanged	2	87	16	105	4	

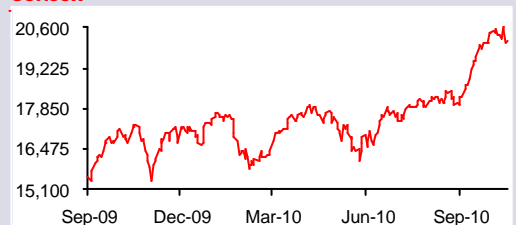
Commodity

	18 Oct 10	% Chg		
		1 Day	1 Mth	3 Mths
Crude (NYMEX) (US\$/BBL)	82.8	(0.3)	12.4	8.2
Gold (US\$/OZ)	1,371.3	0.0	7.2	15.8
Silver (US\$/OZ)	24.4	0.5	16.6	37.9

Debt / forex market

	18 Oct 10	1 Day	1 Mth	3 Mths
10 yr G-Sec yield %	N/A	8.07	7.98	7.64
Re/US\$	44.37	44.11	45.71	47.13

Sensex



RESULT UPDATE**Dipen Shah**dipen.shah@kotak.com
+91 22 6621 6301**NIIT TECHNOLOGIES LTD (NIITT)****PRICE: Rs.228****TARGET PRICE: Rs.291****RECOMMENDATION: BUY****FY12E P/E: 7.5x**

NIITT's 2QFY11 results were better than our estimates. Revenues grew by 9.5% (excluding BSF order), on the back of a 7% rise in volumes, which was a positive surprise. Average realizations remained stable. The company was able to maintain the EBITDA margins (ex-BSF) despite some increase in on-site salaries. The order bookings have increased QoQ, which is in line with the increased management optimism on the demand scenario. In fact, 2Q has seen growth across geographies and verticals. Non-linear revenues also grew at company average and did provide some support to margins. We have marginally increased our FY11E EPS estimate to Rs.27. We introduce FY12E earnings and estimate FY12 EPS to be Rs.30. Our DCF - based price target now stands at Rs.291 (Rs.240 earlier), based on FY12 earnings. At our TP, our FY12 earnings will be discounted by about 9.6x which, we believe, is undemanding. We maintain BUY. We note that, 3Q revenues may see a de-sequential growth in line with the reduction in BSF bought-out component.

Summary table

(Rs mn)	FY10	FY11E	FY12E
Sales	9138	11818	12480
Growth (%)	-6.7	29.3	5.6
EBITDA	1889	2219	2602
EBITDA margin (%)	20.7	18.8	20.8
Net profit	1263	1622	1776
Net cash (debt)	1678	2828	4149
EPS (Rs)	21.5	27.6	30.2
Growth (%)	9.9	28.4	9.5
CEPS	27.6	33.0	36.9
DPS (Rs)	7.0	8.0	9.0
ROE (%)	26.1	25.5	23.5
ROCE (%)	29.1	30.1	29.2
EV/Sales (x)	1.5	1.1	1.1
EV/EBITDA (x)	6.2	4.8	3.6
P/E (x)	10.6	8.3	7.5
P/Cash Earnings	8.3	6.9	6.2
P/BV (x)	2.3	1.9	1.6

Source: Company, Kotak Securities - Private Client Research

2QFY11 results

(Rs mn)	1QFY11	2QFY11	% Chg	2QFY10	% Chg
Income	2914	3246	11.4	2263	43.4
Expenditure	2373	2653		1804	
Operating Profit	541	593	9.6	459	29.2
Depreciation	80	72		90	
Gross Profit	461	521	13.0	369	41.2
Other Income	24	17		15	
PBT	485	538	10.9	384	40.1
Tax	70	97		62	
PAT	415	441	6.3	322	37.0
Minority interest	6	6		1	
Adjusted PAT	409	435	6.4	321	35.5
Shares (mns)	59	59		59	
EPS (Rs)	7.0	7.4		5.5	
Margins					
OPM (%)	18.6	18.3		20.3	
GPM (%)	15.8	16.1		16.3	
NPM (%)	14.2	13.6		14.2	

Source : Company

Revenues grow by 10% QoQ (excluding bought-outs for BSF deal)....

- Revenues grew by 10% on a sequential basis, excluding the bought-outs for the BFS deal.
- During 1QFY11, NIITT had started executing the BSF project. The initial phase involves building the infrastructure and the same was partially carried out in 1QFY11 and 2QFY11.
- The revenues of 2QFY11 include about Rs.537mn (Rs.450mn) of bought out components towards this.

...led by 7% volume growth

- Revenues also include forex loss on hedging of Rs.96mn as against a loss of Rs.79mn in the previous quarter.
- Excluding these, revenues were higher by about 10% QoQ, which was a pleasant surprise.
- According to the management, volumes grew by about 7% QoQ and currency fluctuations added about 3% to the revenues.
- The 7% growth is encouraging and would in all probability be in line with the growth rates of larger peers. Infosys reported a 7% QoQ rise in volumes.

Broad-based growth

- What is more encouraging is that the revenue growth was experienced across clients, geographies, verticals.
- The Top 20 clients gave 10% higher revenues QoQ.
- All the geographies grew by 10% QoQ in INR terms.
- The management indicated greater traction in APAC region because of the faster economic recovery in this region.
- Among verticals, BFSI grew by 10% QoQ. The company experienced strong recovery with US clients and also added a significant new customer in Insurance.
- ROOM Solutions, which has now been named NIIT Insurance Technologies Ltd, saw revenue grow by 12% QoQ with stand-alone margins at 26% (22%).
- ROOM's margins have expanded significantly over the past two quarters in line with higher revenues and the non-linear nature of these revenues.
- The Travel & Transportation revenues grew at a faster pace of 14% during the quarter as NIIT managed to get a higher share of the clients' IT budgets.
- Key accounts in US and Europe contributed to growth whereas the APAC region also witnessed expansion. 2 new customers were added during the quarter.

Macro scene improving

- The company has witnessed an overall improvement in the macro scene, especially in USA and in India.
- The overall spending on IT is on the rise, buoyed by the release of pent-up demand of the past few quarters.
- The off-shore component in budgets has increased and this move towards off-shoring is helping Indian vendors who are receiving larger order-flows.
- BFSI and Travel & Transportation (T&T) verticals have seen further improvement in demand. The retail vertical has also seen traction.
- Within T&T, the airlines vertical has seen a re-emergence of spending. According to the management, as compared to a combined loss of about \$10bn in CY2009, airlines are expected to rake in profits of about \$2.5bn in CY2010.

Non-linear initiatives

- Non-linear initiatives has continued to scale in the current quarter.
- Non-linear initiatives formed 27% of overall revenues in 2QFY11 v/s 26% QoQ and we expect them to continue to form about 27% of overall revenues in the near term.
- However, the contribution is expected to increase as the business gains greater scale.

- The various initiatives on the non-linear side include Infrastructure management services, Platform based services and Managed services. The company has platforms like Subscribe (ROOM) & Monalisa (SofTec).
- The platform based services should gather steam in the future quarters (with ROOM's platform gaining traction) while the IMS business is expected to contribute for the whole fiscal.
- ROOM's revenues have scaled up during the quarter. ROOM is more into the non-life market, which had not been impacted significantly.
- The company has plans of introducing ROOM's platform to the US markets. This is expected to be done by implementing the PF at the Bermuda location of an existing European client.
- We expect the entry into US to be slow because of the need to incorporate changes required by different regulations.
- The company has also launched the SaaS initiative and the Cloud initiative recently. Initially, it had planned to offer only infrastructure outsourcing services.
- It has announced a partnership with Hitachi Information Systems, Ltd., Japan FY10 to offer Cloud services. Revenues from this partnership are expected to start from 2HFY11.
- Initially, non-critical applications like HR, Payroll, etc will be offered by NIIT on Cloud.
- The company has also executed two projects wherein it has offered Testing as a service.
- These non-linear initiatives are expected to help the company restrict impact on margins due to salary hikes and potential rupee appreciation, if any.

BSF order - implementation revenues have started to accrue, bought-outs to reduce WEF 3Q

- The company announced an order from BSF (Border Security Force) worth Rs.2.28bn in 4QFY10, to be implemented over a five year period. The order involves the entire gamut of operations including troop movement, payrolls, accounting, etc.
- This SI order also includes a hardware component which, we believe, is about Rs.1.2bn.
- The order started in 1QFY11 and the company has already supplied hardware of about rs.1bn till 2Q.
- The implementation revenues have started accruing and further revenues are expected to accrue going forward.
- According to the management, the bought-out component is expected to reduce in 3QFY10 to Rs.200mn (Rs.537mn in 2Q)

Record addition to employees; attrition remains high

- Attrition remained high at about 18.6% during the quarter (18% QoQ).
- With a view to compensate for this, NIIT added 409 employees on a net basis during the quarter. This is the highest net addition done by the company during any quarter.
- We believe that, attrition will remain high because of the general buoyancy in the sector and aggressive hiring / salary increments by larger peers.
- At 83%, the company also does not have the liberty to expand the utilization levels further.

- The company has given staggered salary hikes to off-shore employees.
- The 9% average hike has been divided equally between 1QFY11 and 3QFY11E, we believe.
- On-site employees were given an average hike of 2% - 3% WEF 2QFY11.

Margins maintained

- EBIDTA margins excluding the bought-outs, were maintained at about 21.3%, despite the salary increment given to on-site employees and the increased employee additions.
- We understand that, better leverage on costs and higher revenues helped company sustain margins.
- Non-linear revenues formed 27% of the quarter revenues v/s 26% in 1Q and also helped in restricting impact on margins.

Exchange rate movement - company has started hedging against Euro and GBP

- NIIT had forex loss of about Rs.23mn (gain of about Rs.6mn) during the quarter, largely due to translation losses.
- The company has \$46mn (\$73mn) of hedges at an average of about Rs.43.4 / USD maturing over the next 4 quarters.
- NIIT has also started hedging its Euro and GBP revenues, though to a smaller extent (\$4.2mn).

Future prospects

- We tweak our earnings estimates. We have assumed the rupee to be at Rs.45 per USD in 2HFY11.
- For FY11, we expect USD revenues (ex bought-outs) to grow by 21% on the back of a 25% rise in volumes. The expected rupee appreciation may impact overall revenue growth.
- EBIDTA margins are expected to be marginally lower as against FY10 levels because of the exchange rate and the expected salary increments in FY11.
- Net profits are expected to be Rs.1.62bn in FY11, translating into earnings of Rs.27 in FY11.
- We introduce Fy12 earnings estimates.
- We expect volumes to grow by 21%. We need to watch out for the evolving macro scenario in the developed economies.
- We have assumed the rupee to average 45 / USD in FY12.
- EBIDTA margins are expected to be lower due to the potential rupee appreciation and salary increments.
- We have increased the tax rate to 21% of PBT as STPI unit benefits are expected to expire WEF FY12.
- Consequently, PAT is expected to rise by 12% to Rs.1.78bn, translating into EPS of Rs.30.

We recommend BUY on NIIT Technologies with a price target of Rs.291

Valuations and recommendation

- In our DCF model, we have incorporated a benign operating environment in our near term assumptions for the company.
- A WACC of 14% and terminal growth of 2% leads us to a fair value of Rs.291 for the stock, based on FY12 estimates.
- At those levels the stock will quote at about 9.6x FY12 earnings, which is reasonable, in our view.
- We maintain a **BUY**.
- The company may have net cash of about Rs.73 per share by FY12 end, as per our estimates.

Concerns

- Rupee appreciation beyond our assumed levels could provide a downward bias to our earnings estimates.
- A delayed recovery in major global economies could impact growth prospects of NIIT.

RESULT UPDATE**Sanjeev Zarbade**

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LARSEN & TOUBRO LTD (L&T)**PRICE: Rs.2013****TARGET PRICE: Rs.2100****RECOMMENDATION: ACCUMULATE****FY11E P/E: 26.8x**

- ❑ L&T came out with numbers that were ahead of our expectations on the revenue front as the company exhibited robust project execution. EBITDA margins expanded marginally on a yoy basis but were down on a qoq basis. Profits were boosted by significantly higher other income that included non-recurring gain on sale of Mahindra Satyam shares and sale of property. Adjusted for these one-offs, profit growth has been moderate.
- ❑ Order intake has been sluggish in Q2 FY11. The management highlighted that public sector orders have been slow to take-off. Nevertheless, the company is in a good position to meet its order intake target for current fiscal.
- ❑ Strong revenue growth in Q2 FY11 has addressed concerns on execution capability and the company should be able to meet its revenue growth guidance in FY11.
- ❑ Valuations are at a significant premium to domestic engineering and construction companies. Expect the stock to remain move in line with broad markets. Maintain Accumulate with a target price of Rs 2100 (Rs 2022 earlier). Recommend investors to utilize declines to buy into the stock.

Summary table

(Rs mn)	FY10	FY11E	FY12E
Sales	439,698	528,425	649,905
Growth (%)	8.6	20.2	23.0
EBITDA	63,697	76,375	93,714
EBITDA margin (%)	14.5	14.5	14.4
PBT	74811	68514	83490
Growth (%)	45.8	-8.4	21.9
Net profit	54,507	45,187	55,106
EPS (Rs)	60.8	75.0	91.5
Growth (%)	11.8	23.5	22.0
DPS (Rs)	10.5	10.5	10.5
ROE (%)	31.7	20.1	20.6
ROCE (%)	13.8	13.6	14.7
EV/Sales (x)	3.0	2.6	2.1
EV/EBITDA (x)	20.5	17.7	14.6
P/E (x)	33.1	26.8	22.0
P/BV (x)	5.9	5.0	4.2

Source: Company, Kotak Securities - Private Client Research

Execution coming back on track

- At the beginning of the quarter, the company had signaled subdued revenue booking in the H1 FY11 as several large orders were in the nascent stage and revenue booking was sluggish.
- In this backdrop, the revenue growth of 17.7% yoy has come as a surprise and the company is now in a better position to meet its full year revenue growth target of 20%.
- E&C segment reported robust revenue growth as the company continued executing the large order backlog without any major delays. There are signs of revenue growth now catching up with the rise in order backlog. The management indicated that there has been execution pick-up in construction and hydrocarbon jobs.
- The Electrical and Electronics segment posted a degrowth of 5%, which came as a negative surprise. The management indicated that segment sales were impacted by project deferments in "Engineer to Order" projects.
- The machinery and industrial products (MIP) posted a growth of 18% yoy in Q2 FY11. This segment was severely impacted by the economic slowdown in FY09 and has been on a recovery mode since Q3 FY10. This is a product business and prospects have improved in light of massive spending potential in the road and infrastructure sector. There has been a decent uptick in the construction and mining business.
- "Others" segment include Technology Services division, e-Engineering solutions and embedded systems. This segment posted robust growth of 73% yoy on robust demand from the US.

Quarterly performance

(Rs mn)	Q2FY11	Q2FY10	YoY (%)	H1FY11	H2FY11	YoY (%)
SalesTurnover	93,422	79,363	17.7	172,552	158,725	8.7
excise duty	815	701	16.2	1,593	1,402	13.7
Excise rate %	1%	1%		1%	1%	
Net sales	92,608	78,662	17.7	170,959	157,324	8.7
Other op income	700	527	32.9	1,202	1,053	14.1
Total op expenses	83,251	70,816	17.6	152,033	141,632	7.3
Raw material	19,871	19,488	2.0	33,727	38,976	-13.5
Sun-contracting charges	18,632	19,350	-3.7	35,313	38,699	-8.7
Construction materials	19,203	13,114	46.4	37,138	26,228	41.6
purchase of trading goods	5,084	3,577	42.1	9,527	7,154	33.2
Other operating expenses	7,067	4,769	48.2	13,592	9,537	42.5
sales and admin exp	5,105	3,433	48.7	8,815	6,865	28.4
Personnel	8,288	7,087	17.0	13,921	14,173	-1.8
Operating Profit	10,057	8,372	20.1	20,127	16,745	20.2
Other income	3,822	2,176	75.7	6,091	4,351	40.0
Interest	1,932	1,310	47.5	3,355	2,619	28.1
Gross Profit	11,947	9,238	29.3	22,863	18,477	23.7
Depreciation	1,212	1,001	21.1	2,354	2,003	17.5
PBT	10,735	8,237	30.3	20,509	16,474	24.5
Current Tax	3,705	2,726	35.9	6,815	5,452	25.0
Deferred tax	89	(19)	-558.8	90	(39)	-332.0
Adjusted PAT	6941	5530	25.5	13604	11060	23.0
Extraordinary gains	708.4	273.8	158.7	708	548	29.4
Reported PAT	7650	5804	31.8	14,313	11,608	23.3
EBITDA (%)	10.9	10.6		11.8	10.6	
Raw Matl costs to sales (%)	21.5	24.8		19.7	24.8	
Sub-contracting costs to sales (%)	20.1	24.6		20.7	24.6	
Construction materials costs to sales (%)	20.7	16.7		21.7	16.7	
Purchase of trading goods costs to sales (%)	5.5	4.5		5.6	4.5	
Other op expenses costs to sales (%)	7.6	6.1		8.0	6.1	
sales and admin costs to sales (%)	5.5	4.4		5.2	4.4	
Personnel costs to sales (%)	9.0	9.0		8.1	9.0	
Current tax rate (%)	35	33		34	33	

Source: Company

Segment Performance

Segment revenues (Rs mn)	Q2 FY11	Q2 FY10	YoY (%)
Engg and Construction	80,150	68,541	17
Electrical and Electronics	6,724	7,088	-5
Machinery and Industrial products	6,981	5,906	18
Others	1,597	923	73
Total	95,453	82,458	17

Source: company

Capital employed

(Rs mn)	Q2 FY11	Q2 FY10
Engg and Construction	73,342	66,690
Electrical and Electronics	11,571	11,021
Machinery and Industrial products	2,723	1,761
Others	2,228	1,832
Total capital employed in segments	89,864	81,304

Source: company

Margin expansion despite increase in material prices

- EBITDA margins for the quarter stood at 10.9% up 30 bps on a yoy basis. We believe margin expansion could be due to favourable project mix changes and execution efficiencies. On a qoq basis however, margins shrunk 200 bps.
- The management highlighted that during the quarter, the material prices were up on a yoy basis of basic commodities including Steel, Aluminium and Copper. In the manufacturing business, it is normal to have a time lag between rise in material price and transfer of higher costs to customers.
- During the quarter, the company incurred the impact of wage hikes in its employee costs. As a result, employee costs rose 17% yoy. Other expenses also included Rs 600 mn of forex losses.
- Segment wise, the E&C division reported margin expansion on efficient project management. The Electrical business group reported margin decline on account of material cost pressures (higher prices of copper and silver) and deferments in higher margin customized orders.
- Although EBITDA margins in H1 FY11 are a good 120 bps higher, the management maintained that it expects to maintain margins at previous year's levels.

Segment margins

(%)	Q2 FY11	Q2 FY10	Q1 FY11
Engg and Construction	11.2	10.1	12.3
Electrical and Electronics	12.9	14.9	9.9
Machinery and Industrial products	16.6	15.7	20.6
Others	10.8	19.1	27.4

Source: company

Other income boosted by one-timers like sale of Mahindra Satyam shares and gain on property sale

Other income rose 74% yoy led mainly higher interest income and dividends from subsidiary and associate companies. Profit on sale of investments includes gain of Rs 700 mn on sale 0.284 mn of Satyam shares. In addition to this, other income also includes Rs 700 mn on sale of property.

Details of other income

(Rs mn)	Q2 FY11	Q2 FY10	% yoy
Interest income	890	298	198.7
Dividend from S&A companies	530	81	554.3
Dividend/income from investments	420	484	-13.2
Profit on sale of investments	680	56	1114.3
Misc income	1190	1213	-1.9
Total other income	3710	2132	74.0

Source: company

Higher interest cost led by some one-time costs

Interest costs rose 47.5% yoy to Rs 1.9 bn led by some one-time charges of around Rs 300 mn due to increase in provident fund liabilities and interest on advance tax payments.

Profit growth lower than reported after adjustment for one-timers in other income

L&T reported PAT before extraordinary items of Rs 6.9 bn, an increase of 26% over Q1 FY10. However, adjusted for non-recurring items included in other income of Rs 1400 mn, the PBT declines substantially.

Adjustments for non-recurring items

	(Rs mn)
Sale of satyam shares (included in other income)	700
Income from sale of property (included in other income)	700
Higher provision for provident fund liabilities (included in interest costs)	300
Total	1100

Source: Company

Capex of Rs 20-25 bn

The company plans to incur Rs 20-25 bn in capex on shipbuilding and forging ventures. It has already spent Rs 7.0 bn in the capital expenditure in H1 FY11. The company plans to invest Rs 20 bn in its infrastructure subsidiaries.

Extraordinary item pertaining to reversal of provision on Satyam investment

Following the sale of 28.4 mn shares of Mahindra Satyam, the company has proportionately reversed provision for loss on investment made in earlier years. This amount stood at Rs 700 mn included in extraordinary items.

Order intake momentum slackened in Q1 but appears to be ontrack to meet guidance for the year

- Order backlog for L&T is up 41.4% yoy to Rs 1154 bn, equivalent to revenue visibility of 36 months based on trailing four quarters revenues.
- Order inflows for Q2FY11 came in at Rs 205 bn, up 11% yoy. Order intake was driven by the power and infrastructure sectors. The two sectors accounting for 75% of the order intake. The management highlighted that order intake in Q2 had slowed down mainly due postponement of Rs 400 bn of orders into Q3 and Q4 FY11. These orders are mainly in the infrastructure sector. The company has observed that order finalization cycle has become longer partially due to organizational inertia. As a result, the infrastructure projects from public sector have seen lackluster activity.
- The power sector including the generation as well as T&D continues to see heightened activity. The company expects to book large orders in this segment. However, the roads and railways segment continue to remain sluggish.

Order inflows mix

(%)	Q2 FY11	Q2 FY10	Q1 FY11
Process	9	8	7
O&G	8	26	8
Power	47	32	52
Infrastructure	28	26	25
Others	8	8	8

Source: Company

Major Order Wins in Q2FY11

	(Rs mn)
BOP for 2x600 MW TPP for Visa Power	16100
Processing facilities at Hazira for ONGC	11950
Metallurgical sector orders from SAIL and Balco	17490
700 MW EPC for Nabha Power, Rajpura	30006
3x660 MW STG for JP Associated	27990
Construction of road NH 46 (148 km)	19390

Source: Company

Moderate increase in borrowings and working capital

Total borrowings have increased at the end of H1 FY11 has increased to Rs 77.2 bn up from Rs 69.4 in H1 FY10. Gross debt equity ratio stood at a benign 0.39x. Net current assets remained unchanged on a yoy basis at Rs 49.5 bn.

The company has invested substantially in the associate and subsidiary companies in the current fiscal. The company plans to invest Rs 20 bn per annum in its developmental projects executed through its subsidiaries.

Future Outlook

- Management has indicated that it does not anticipate major execution related issues in the foreseeable future and is well positioned to deliver its guidance of 20% growth in revenues in FY11.
- Order intake is expected to grow by 25% in FY11 while order backlog at the end of FY11 is targeted at Rs 1350-1400 bn.
- The company needs to increase by 22% in the H2 FY11 for the company to meet its order intake guidance of 25% or Rs 870 bn.
- We continue to positive on L&T on account of revival in industrial capex, scale-up of power equipment business, enviably positioned to play verticals like Defence, Nuclear Power and Shipbuilding and revenue growth driven by multiple drivers.
- We see earnings growth gaining further traction FY12 onwards as the revenue growth which has been lagging the growth in order backlog starts catching up.

Stock outlook

- At the current price, the stock is trading at a significant premium to its peers in the engineering sector ie BHEL and Thermax.
- We believe current valuations restrict upsides in the near-term. As a result, we believe that the stock may move in line with the markets.

Valuation and Rating: Maintain Accumulate with a target price of Rs 2100

We recommend ACCUMULATE on L&T with a revised price target of Rs.2100

- L&T is trading at 26.8x and 22.0x FY11 and FY12 earnings respectively.
- The stock has traded in a PEx band of 10x to 30x one year forward earnings. The average PEx for L&T has been 24x one year forward earnings.
- We have valued the stock on a SOTP basis. At our target price of Rs 2100, the stock is valued at 23x FY12 earnings, which is also in line with its average trading multiple.

Valuation

(Rs mn)	Parameter	Fair Value	Per share	% share
L&T Infotech	15x FY11 earnings	45,974	79	3.7
L&T Finance	15x FY11	33,263	57	2.7
L&T Infrastructure subsidiaries	2x BV	23,000	39	1.9
L&T Standalone	DCF		1925	91.7
Total			2,100	

Source: Kotak Securities - Private Client Research

RESULT UPDATE

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HDFC LTD

PRICE: Rs.725
TARGET PRICE: Rs.720

RECOMMENDATION: ACCUMULATE
FY12E P/E:25.6; P/ABV:5.4x

- Healthy mortgage loan growth and steady spreads lead to better than expected growth in net profit to Rs.8.1bn as compared to our expectation of Rs.7.9
- Firm spreads aided strong growth in earnings; NII grew by 38.5% yoy to Rs.10.2bn, Net profit grew by 21.7% yoy to Rs 8.1bn
- Revising our earnings estimates to factor in higher earnings growth; revising our price target to Rs.720, maintain ACCUMULATE recommendation.

Quarterly performance

(Rs bn)	Q2FY11	Q1FY10	Q2FY10	YoY (%)	QoQ (%)	H1FY11	H1FY10	YoY (%)
Interest income	27.4	26.2	25.7	6.4	4.6	53.5	52.0	2.9
Interest expenses	17.2	17.2	18.4	(6.5)	(0.1)	34.4	38.0	(9.5)
Net Income	10.2	9.0	7.4	38.5	13.6	19.2	14.0	36.4
Other Income	1.7	1.9	2.8			3.6	5.0	(28.8)
Total Income	11.9	10.8	10.1	17.8	10.3	22.8	19.1	19.2
Operating Expense	1.0	1.0	0.9			2.0	1.8	
Operating profit	10.9	9.8	9.3			20.7	17.3	
Loan loss provision	0.2	0.2	0.1			0.3	0.3	
Profit before tax	10.7	9.7	9.1	17.7	11.2	20.4	17.0	19.9
Provisions for taxes	3.1	2.7	2.5			5.8	4.4	
Profit after tax	7.6	6.9	6.6	14.8	9.7	14.6	12.6	
PAT incl. extr-ordi gains	8.1	6.9	6.6	21.7	16.3	15.0	13.5	11.1
EPS (Rs)	27.7	24.4	23.3			52.0	43.2	
Cost/Income ratio (%)	8.7	9.3	8.5			9.0	9.5	
Effective Tax rate (%)	29.1	28.1	27.3			28.3	25.7	
Sanctions (Rs bn)	296.7	69.9	161.6	83.6	324.6	366.6	284.2	29.0
Disbursements (Rs bn)	140.4	143.4	136.5	2.8	(2.1)	283.7	223.4	27.0
Mortgaged Loan (Rs bn)	1,062.9	1,016.3	895.2	18.7	4.6	1,062.9	895.2	18.7

Source: Company

Healthy mortgage loan growth and steady spreads lead to better than expected growth in net profit to Rs.8.1bn as compared to our expectation of Rs.7.9 bn

HDFC's has reported a strong growth in its earnings during Q2FY11 in the backdrop of a 27% yoy growth in disbursements to Rs. 208bn. The impressive growth in the advances is supported by steady retail demand for housing, which is reflective in a 42% yoy growth in retail disbursements during H1FY11. HDFC's mortgage loan book grew by 18.7% yoy to Rs. 1062bn (excluding loan sell down of Rs. 48.6bn) from Rs. 895.2bn. Disbursements for the H1FY11 have remained healthy with a 29% yoy growth to Rs. 283.4bn from Rs. 223.4bn. Given the robust growth in its sanctions book we remain positive on HDFC's future loan growth outlook.

Firm spreads aided strong growth in earnings; NII grew by 38.5% yoy to Rs.10.2bn, Net profit grew by 21.7% yoy to Rs 8.1bn

HDFC has reported a strong growth in earnings during Q2FY11, aided by firm interest spreads coupled with steady growth in mortgage loans. NII grew by 38.5% yoy to Rs. 10.2bn from Rs. 7.4bn, which is largely attributed to its firm interest spread of 2.34% (2.03% in Q2FY10). HDFC has benefited from its flexible borrowing strategy and also being a bulk borrower in the wholesale debt markets which helps contain cost of funds. With HDFC's dual interest rate product's reset clause, the new asset will be re-priced in the second year and is less likely to have material impact on its spreads. We maintain our positive outlook on HDFC's interest spreads and opine that it is likely to remain firm going forward. HDFC's other operating income of Rs.2.28bn also includes a treasury gain amounting to Rs.590mn

Asset quality remains healthy - HDFC's asset quality continues to remain impeccable during Q2FY11. It reported a gross NPA of Rs.9.4bn (0.9% of assets) and net NPA of 2.1bn. Provision coverage for Q2FY11 stood firm at 77%.

Revising our earnings estimates to factor in higher earnings growth; revising our price target to Rs. 720, maintain accumulate recommendation.

- We are revising our earnings estimates for HDFC following strong earnings growth and steady mortgage loan growth. We expect a net profit growth of 20% yoy to Rs.34bn for FY11 and 19.8% yoy growth and net profit of Rs.40.7 bn for FY12.
- We value HDFC using sum-of-the-parts (SOTP) methodology. The core business (mortgage financing) is valued on dividend discount model (DDM), based on which we arrive at a fair value of Rs.486 (rolling over to FY12), which is 3.6x its FY12 adjusted book value of Rs.134. We have valued HDFC subsidiaries-at Rs.235, leading to a price target of Rs.721. The stock is trading at 3.6x P/ABVx-post stripping the value of subsidiaries and investments. We maintain our **ACCUMULATE** recommendation with a revising price target of Rs. 720.

We recommend ACCUMULATE on HDFC with a price target of Rs.720

Summary Table

(Rs bn)	2010	2011E	2012E
Int. Income	109.0	129.0	156.2
Int. expenses	70.6	81.5	99.3
NII	38.3	47.6	56.9
Non-Int Income	4.6	6.0	7.2
Total Income	42.98	53.54	64.13
Optg Profit	39.7	49.1	59.2
PAT	28.3	34.0	40.7
GNPA - 6 mths(%)	0.7	0.6	0.5
NNPA (%)	0.2	0.1	0.0
Spreads (%)	2.2	2.2	2.2
RoA (%)	2.7	2.8	2.8
RoE (%)	20.0	20.9	22.2
Divi. Payout (%)	29.5	126.8	109.4
EPS (Rs)	98.4	23.7	28.3
BV (Rs)	529.3	120.8	134.6
Adj. BV (Rs)	524.1	120.1	134.6
P/E (x)	36.8	30.6	25.6
P/ABV (x)	6.9	6.0	5.4

Source: Company, Kotak Securities - Private Client Research

Bulk deals

Trade details of bulk deals

Date	Scrip name	Name of client	Buy/ Sell	Quantity of shares	Avg. price (Rs)
18-Oct	Amulya Leas	Securocrop Securities India Pvt Ltd	B	28,600	46.7
18-Oct	Arrow Sec	Tushar Rameshbhai Patel	B	34,000	75.2
18-Oct	Arrow Sec	Benko Trading Pvt Ltd	B	54,000	77.1
18-Oct	Arsi Cosmetics	Susmit Bhupendrabhai Sutaria	S	50,000	19.5
18-Oct	Arvind Intl	Kaizen Stoktrade Pvt Ltd	B	50,000	23.4
18-Oct	Arvind Intl	Alintekizhakethil Mathai Joseph	S	43,295	23.4
18-Oct	Aryaman Fin	Finstock Limited Mhs	B	95,000	17.6
18-Oct	Aryaman Fin	Palaparthi Venkataramana Murthy	S	70,000	17.5
18-Oct	Axtel Inds	Ajay Nalin Parikh	B	120,600	12.0
18-Oct	Axtel Inds	The Catholic Syrian Bank Ltd	S	120,600	12.0
18-Oct	Broadcast Init	Naman Securities & Finance Pvt. Ltd.	B	108,064	27.0
18-Oct	Choice Intl	Tejsingh Dhansingh Ramola	B	34,752	126.7
18-Oct	Exelon Infra	Bala Rama Venkata Siva Naga S	B	28,546	30.6
18-Oct	Explicit Fin	Ranjanben Anilbhai Shah	S	24,400	21.6
18-Oct	Fiem Inds	Rajyog Share and Stock Brokers	B	61,986	181.2
18-Oct	Golden Tob	Rajasthan Global Securities Ltd	S	127,000	97.3
18-Oct	Haryana Ship	Sar Auto Products Limited	B	35,802	53.5
18-Oct	Hittco Tools	Jitendra Narottamdas Mehta	B	49,000	43.0
18-Oct	Ishita Drugs	Prince Joseph	B	20,000	63.2
18-Oct	Ishita Drugs	Dilipkumar Kantilal Shah	S	22,500	63.2
18-Oct	JMD Telefilms	Narayani Shares & Securities Pvt Ltd	B	350,000	56.6
18-Oct	Kadvani Sec	Ashwinbhai Prabhudas Ruparel	S	37,842	18.4
18-Oct	LKP Fin	Fortune Capital Holding Pvt Ltd	B	66,000	149.1
18-Oct	Mahalaxmi Rub	Pravesh Rani Pahwa	B	500,000	26.2
18-Oct	Master	Bala Rama Venkata Siva Naga S	B	57,006	54.1
18-Oct	Midfield Ind	Winners Sales Pvt Ltd	B	78,649	435.3
18-Oct	Msk Projects	International Synthfabs Pvt Ltd	B	175,000	160.5
18-Oct	Msk Projects	Shilpa Stock Broker Pvt Ltd	S	157,399	160.3
18-Oct	Neogem India	Jignesh Rameshbhai Mehta	B	35,000	12.1
18-Oct	Oregon Comm	Mahesh Somabhai Desai	S	12,526	147.8
18-Oct	Pipavavship	Citadel Mt Trading Ltd	S	3,885,005	75.5
18-Oct	Polypro Fibrils	Ajay Ravindra Shah	B	44,106	26.4
18-Oct	Polypro Fibrils	Anila Ravindra Shah	S	40,000	26.4
18-Oct	Prism Info	Idhasoft Limited	S	4,986	460.0
18-Oct	Raj Packaging	Jatin Sampatkumar Dokwal	S	22,988	146.4
18-Oct	Rama Phosphat	Hitesh Shashikant Jhaveri	B	57,211	101.3
18-Oct	Ranklin Sol	Bala Rama Venkata Siva Naga S	B	42,264	129.0
18-Oct	Reliance Chem	Venture Broking Pvt. Ltd	B	54,949	107.0
18-Oct	Sacheta Metals	Pravesh Rani Pahwa	B	50,000	74.6
18-Oct	Seasons Tex	Ravindra Choudhary	S	55,503	15.5
18-Oct	Seasons Tex	Kiran Ravindra Kumar Choudhary	S	54,420	15.5
18-Oct	Seshachal Tech	Rajesh Vijayvargiya	B	35,000	10.2
18-Oct	Singer India	Arora Farm Pvt.Ltd.	S	100,000	36.5
18-Oct	Unisys Soft	Mahesh Kumar Agrawal	B	100,146	77.4
18-Oct	Vax Housing	Agrawa Bhikhalal Prahalad Rai	B	25,000	71.6
18-Oct	Venmax	Sandeep Kewalchand Mehta	B	200,000	9.9
18-Oct	Vikram Thermo	Kusum Gupta	B	20,000	24.9
18-Oct	White Diamond	Rameshchandra Popatlal Kothari	S	40,000	15.6

Source: BSE

Gainers & Losers

Nifty Gainers & Losers

	Price (Rs)	chg (%)	Index points	Volume (mn)
Gainers				
TCS	981	3.3	5.3	2.2
Infosys Tech	3,107	1.0	5.0	1.6
Larsen & Toubro	2,015	1.4	4.8	2.9
Losers				
ICICI Bank	1,116	(0.8)	(3.3)	5.8
Bharti Airtel	327	(1.9)	(2.6)	7.1
Tata Power	1,395	(2.4)	(1.9)	0.3

Source: Bloomberg

Forthcoming events

Company/Market

Date	Event
19-Oct	Bajaj Auto, Bajaj Holdings, Cadila Health, Container Corporation, Greaves Cotton, HCL Tech, HDFC Bank, Ingersoll Rand, Mindtree, Polaris Software earnings expected
20-Oct	Ashok Leyland, BASF, Bombay Dyeing, Canara Bank, Ceat, Hindustan Zinc, Indiabulls Power, Indiabulls Real Estate, Jubilant Org, Kotak Mahindra Bank, Mahindra Lifesp, Merck, Pidilite Inds, Power Grid Corp, Tanta Solutions, Yes Bank earnings expected
21-Oct	ACC, Allahabad Bank, Alstom Projects, Ambuja Cements, Corporation Bank, Indiabulls Fin, Novartis India, SKF Ind, Sterlite Tech, TCS, TVS Motors, Wipro, earnings expected

Source: Bloomberg

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