



$1+1+1=111?$

Sum of the Parts explained

Edelweiss Research

+9122 22864256

research@edelcap.com

August 06, 2007

- * A **Sum of the Parts** approach to valuing Indian companies is credible, as significant value exists in balance sheets which is not near-term earnings accretive
- * India's long term fundamental growth drivers, increasing financial sector sophistication and recent corporate actions make it a sweet spot to apply this concept on a wider scale
- * We have developed a **framework** to identify value in the balance sheet, identifying various value buckets in conjunction with time frame and stages of value unlocking
- * Applying the framework to a cross-section of companies, we see significant upsides to current earnings based valuations
- * We also conclude that this approach is sustainable, and not just a one-time phenomena

Top Picks (SOTP upside)

- * State Bank of India
- * Tata Motors
- * ONGC
- * ICICI Bank
- * Bharti Airtel
- * Mahindra & Mahindra
- * Aditya Birla Nuvo
- * Tata Steel
- * Bajaj Auto
- * Reliance Industries

A Sum of the Parts valuation approach is extremely credible

- * There is significant embedded value in the balance sheets of Indian companies
 - * These range beyond the obvious cash/cash equivalents to many 'assets' that are reflected at historical costs
 - * Development of other asset classes, particularly real estate, are bringing hard assets into focus
 - * Conglomerates with related and unrelated subsidiaries exist as products of the erstwhile license raj and capital scarce economy, e.g. M&M, Reliance
 - * Recent robust performance and positive outlook provides companies with plenty of options on new business initiatives, e.g. Insurance ventures
- * Most of these 'assets' have developed to a stage where they should be valued separately; existing monolithic valuations understate the true value, e.g. Zee, Reliance, Indiabulls, L&T
- * Development of financial markets, access to capital and increased interest in India as an asset class is enabling unwinding of this value - through IPO, demerger, private equity, etc.

And the time to apply this on a wider scale is now

- * Indian corporates are taking concrete steps to unlock this value
 - * Growth opportunities and competition encourage corporates to focus, e.g. Zee
 - * Historical advantages of conglomerate structure have been eroding post liberalization
 - * In some cases the trigger has been ownership linked, e.g. Reliance
- * Actions of Indian corporates provide comfort and improved visibility on long term growth
 - * Huge upsurge in capacity addition and infrastructure creation
 - * Investing for the next leg of growth which is not immediately earnings accretive
- * Equity markets are willing to look farther into the future (FY09 and beyond) as structural strength of growth story plays out
- * All these initiatives will scale up earnings with a lag; in the interim SOTP based valuations could provide support to tide over near term aberrations

Evidence: stock performance is running ahead of earnings growth

Stock performance and earnings growth for select Nifty companies

	1yr. Perf	EPS FY08E	EPS FY09E	EPS CAGR FY07-09E
Nifty	38%			19.2%^a
Larsen & Toubro	125%	90.8	118.0	33%
ABB India	125%	26.4	34.9	51%
Bharti Airtel	121%	31.8	39.2	32%
Steel Authority of India*	114%	15.0	13.4	-5%
Reliance Communications**	105%	21.7	30.2	18%
State Bank of India*	93%	109.7	126.0	20%
Zee Entertainment Enterprises	89%	7.5	10.1	41%
Reliance Industries*	85%	78.6	86.6	5.2%
Sterlite Industries India	74%	77.4	70.2	-5%
Reliance Energy**	66%	37.5	42.1	6%
Housing Development Finance Corp*	65%	71.4	82.4	15%
ICICI Bank*	64%	36.7	45.0	14%
Bharat Heavy Electricals	59%	58.5	70.5	21%
HDFC Bank*	50%	46.6	51.8	20%
Grasim Industries**	40%	227.1	242.1	6%

Source: Bloomberg, Edelweiss research. Updated as of August 01, 2007. ^a Nifty profit growth CAGR (CY06-CY08E), * Standalone numbers, ** Consensus estimates.

Key stock drivers are not near-term earnings accretive

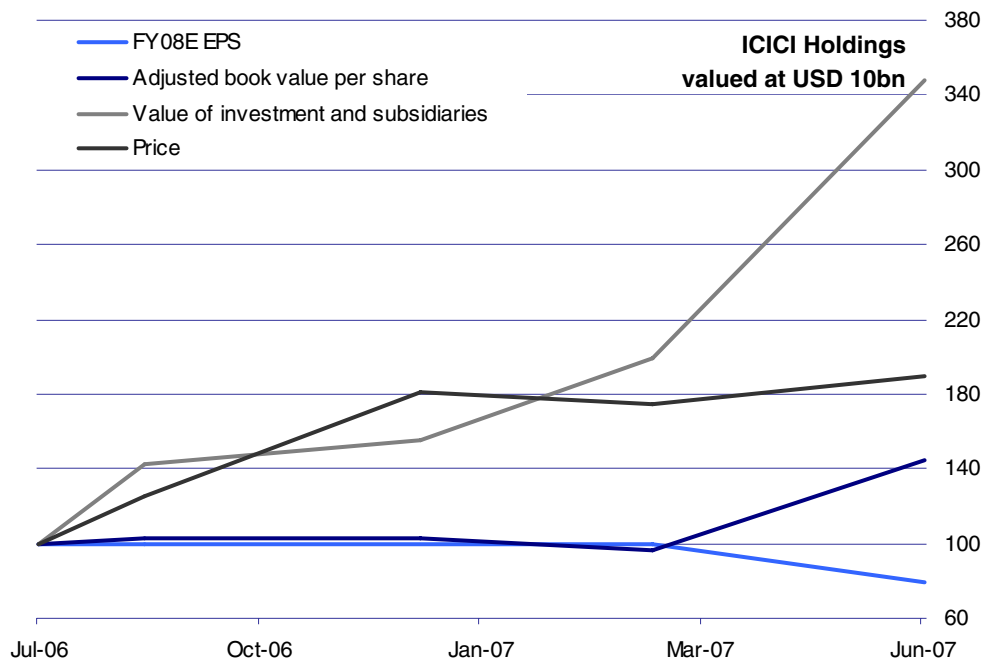
- * Lets look at the 'reasons' driving stock performance of some of the Nifty companies, where valuations appear to have gone beyond earnings support

Company	EPS CAGR FY07-09E	Factor driving the stock
Bharti Airtel	34%	Telecom towers
HDFC	15%	Insurance and other subsidiaries
ICICI Bank	14%	Insurance and other subsidiaries
Larsen & Toubro	33%	Subsidiary value unlocking
Reliance Communications	18%	Telecom towers, FLAG listing
Reliance Industries	5.2%	E&P assets, retail, SEZ
State Bank of India	20%	Insurance and other subsidiaries

- * Common story: the market is looking beyond the next two years earnings and seeking value - and finding it - in everything from unrelated subsidiaries and real estate to real options
- * Enter Sum of the Parts: an approach to valuation that considers this

Example: ICICI Bank - value in investments and subsidiaries

Key parameters for ICICI Bank



- * Both earnings and book value fail to explain price performance
- * Value unlocking came from insurance and asset management business

Source: Bloomberg, Edelweiss research. Date points rebased to 100 on 24 July 2006.

	24-Jul-06	1-Sep-06	11-Dec-06	6-Mar-07	14-Jun-07
FY08E EPS	46	46	46	45.7	36.7
Adjusted book value per share	273	279.5	279.5	262.2	393.3
Value of investment and subsidiaries	115	164	179	229	400
Price	479.5	602.5	867.2	836.7	908

Source: Bloomberg, Edelweiss estimates.

Example: Reliance Industries – value in E&P

Key parameters for RIL

INR per share	16-Nov-06	26-Feb-07	5-Mar-07	27-Apr-07	13-Jun-07
FY08E EPS	72	72	72	73	73
Exploration & Production	302	354	563	717	719
Refining & Marketing	392	392	392	432	428
Chemicals	330	362	362	312	299
Retailing	80	80	80	80	80
Investments	99	146	146	146	144
SOTP	1,275	1,406	1,615	1,760	1,743
Market Price	1,249	1,401	1,306	1,538	1,680

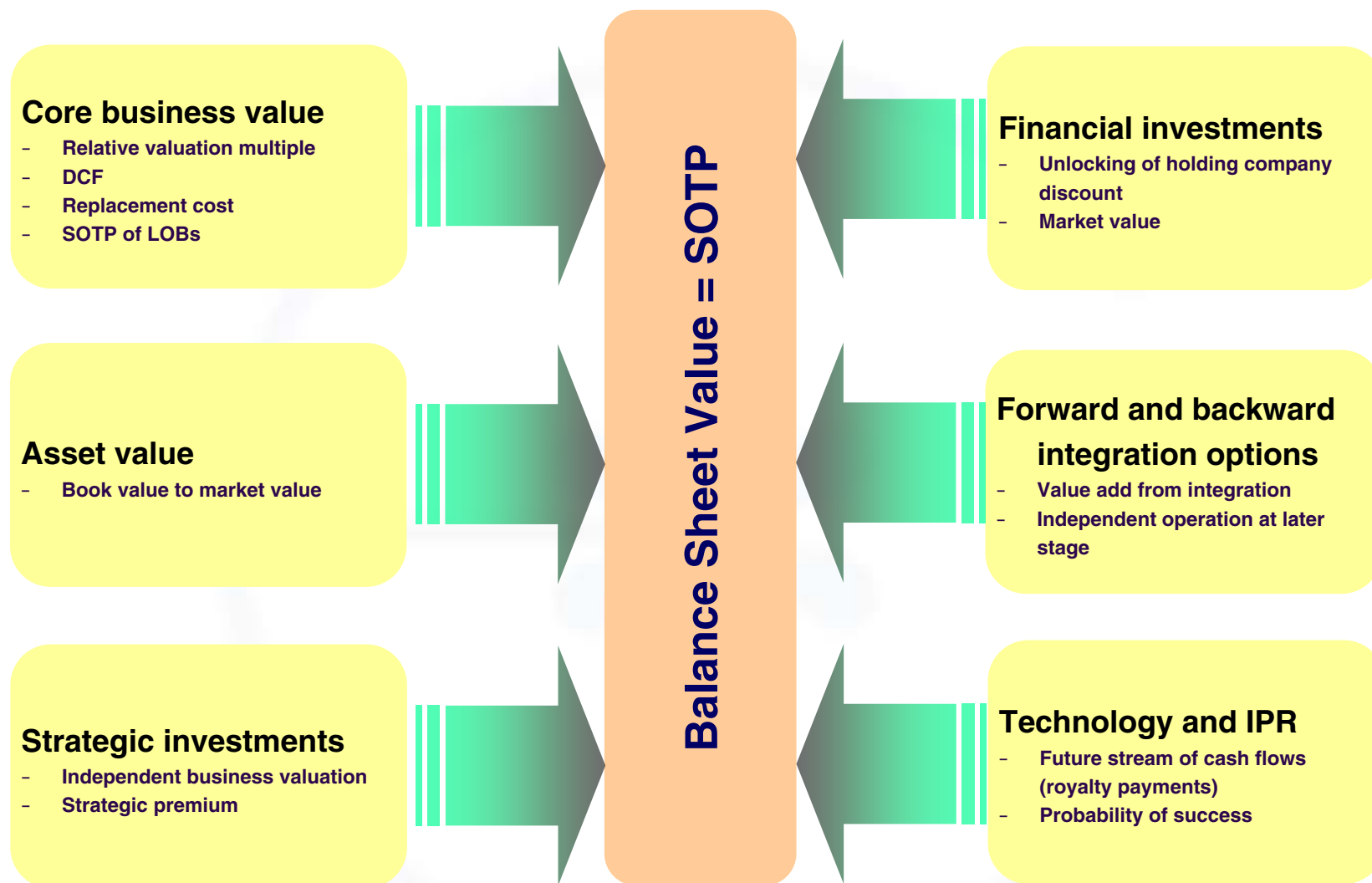
Source: Bloomberg, Edelweiss estimates.

- * Value of exploration and production business increased by more than 135% in less than seven months
- * There is no immediate incremental benefit to earnings
- * In the absence of any significant value contribution from other business lines, we can infer that the market is ready to look beyond the near future

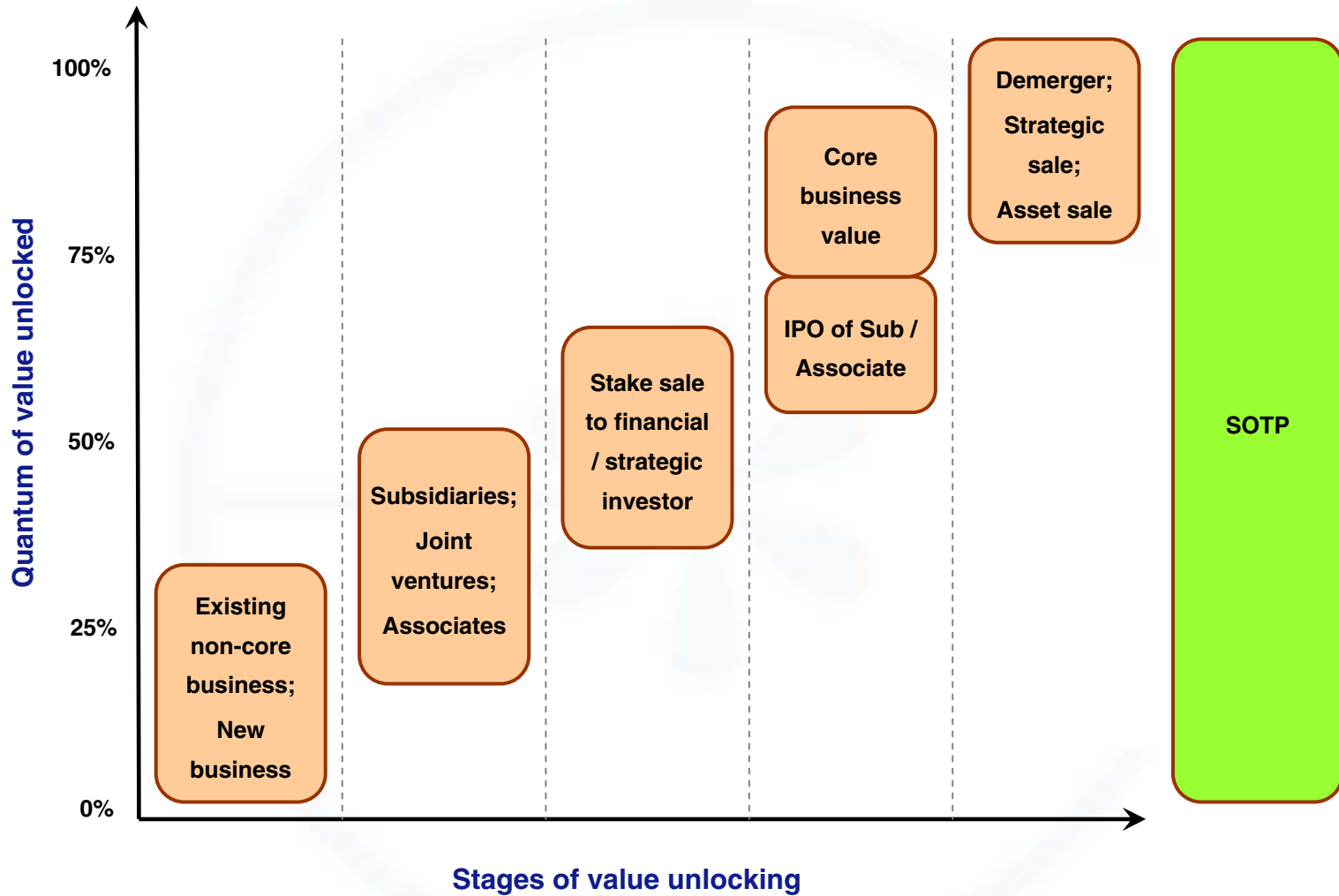
Our SOTP framework – a holistic view

- * While the idea of SOTP valuations appear intuitive and timely, the key challenge is in being able to apply them in practice. Our framework addresses this
- * Looking beyond the horizon
 - * As a first step, we identify mutually exclusive and collectively exhaustive value buckets
 - * These value buckets are used to identify individual business parts/assets which should be valued separately
 - * An appropriate valuation methodology is applied to each part and the parts summed to arrive at the current SOTP valuation
 - * We then superimpose a time frame and stage of value unlocking to evaluate the potential for further value unlocking
- * The framework provides a means to identify business parts/assets (hard and soft assets and real options), quantify their current value, and show the timeframe and extent for further value creation

Identifying balance sheet value buckets



Value is unlocked at every stage



Significant SOTP upside exists across sectors

Top companies with SOTP upside

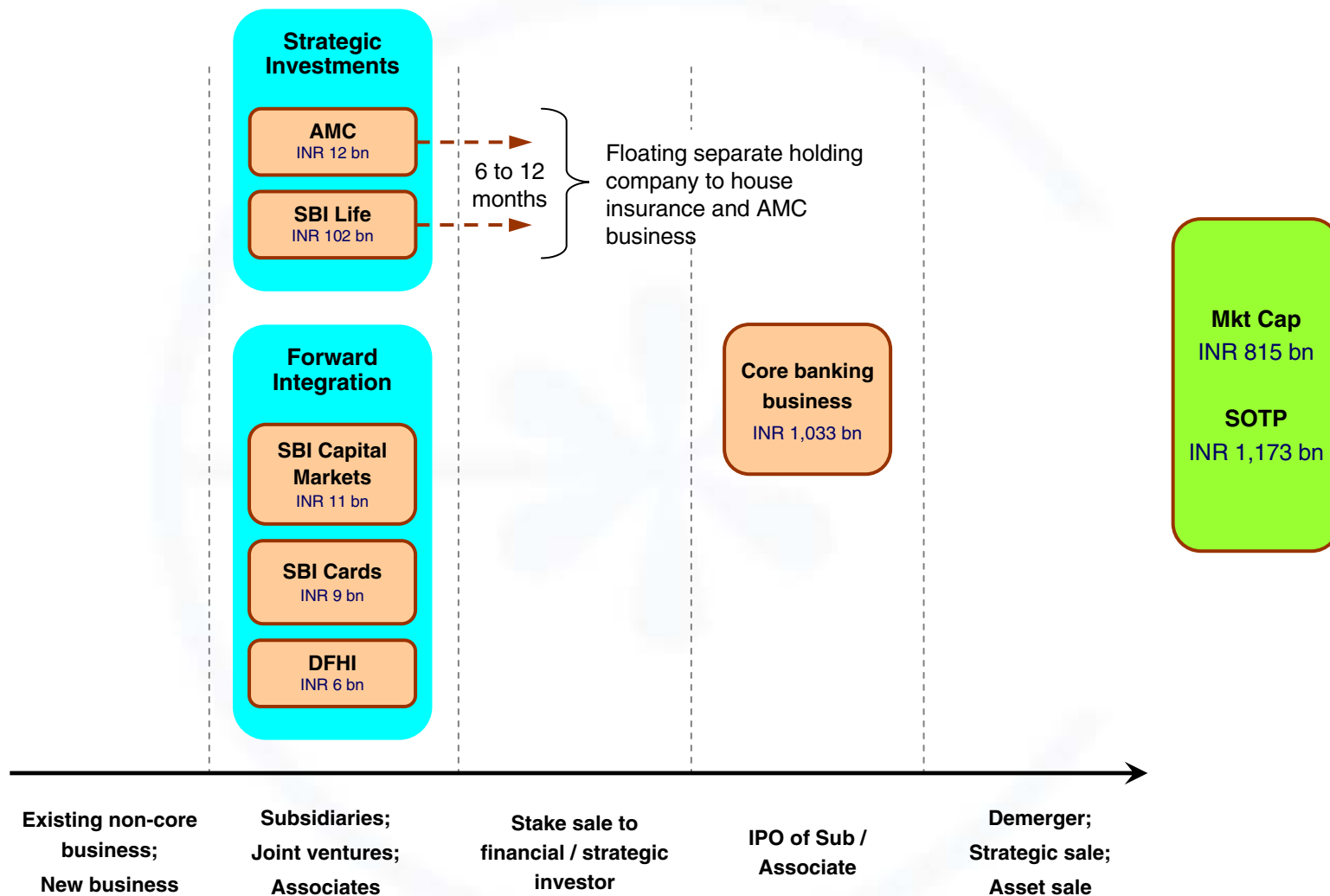
Company	SOTP upside %	EPS CAGR FY07-09E %
SBI	44	20
Tata Motors	40	13
ONGC	38	7
ICICI Bank	32	14
Bharti Airtel	30	34
Mahindra & Mahindra	29	11
Aditya Birla Nuvo	27	19
Tata Steel	26	12
Reliance Industries	25	5
Bajaj Auto	25	17
Reliance Communications	21	18
HDFC	21	15
Hindalco Industries	21	-20
Jaiprakash Associates	16	36
ITC	16	15
Larsen & Toubro	10	33
Pantaloon Retail	9	44
Television Eighteen	2	38

Source: Capital line, Bloomberg, Consensus estimates, Edelweiss research. Updated as of August 01, 2007 closing price.

State Bank of India - value from non-banking businesses

SOTP upside 44%

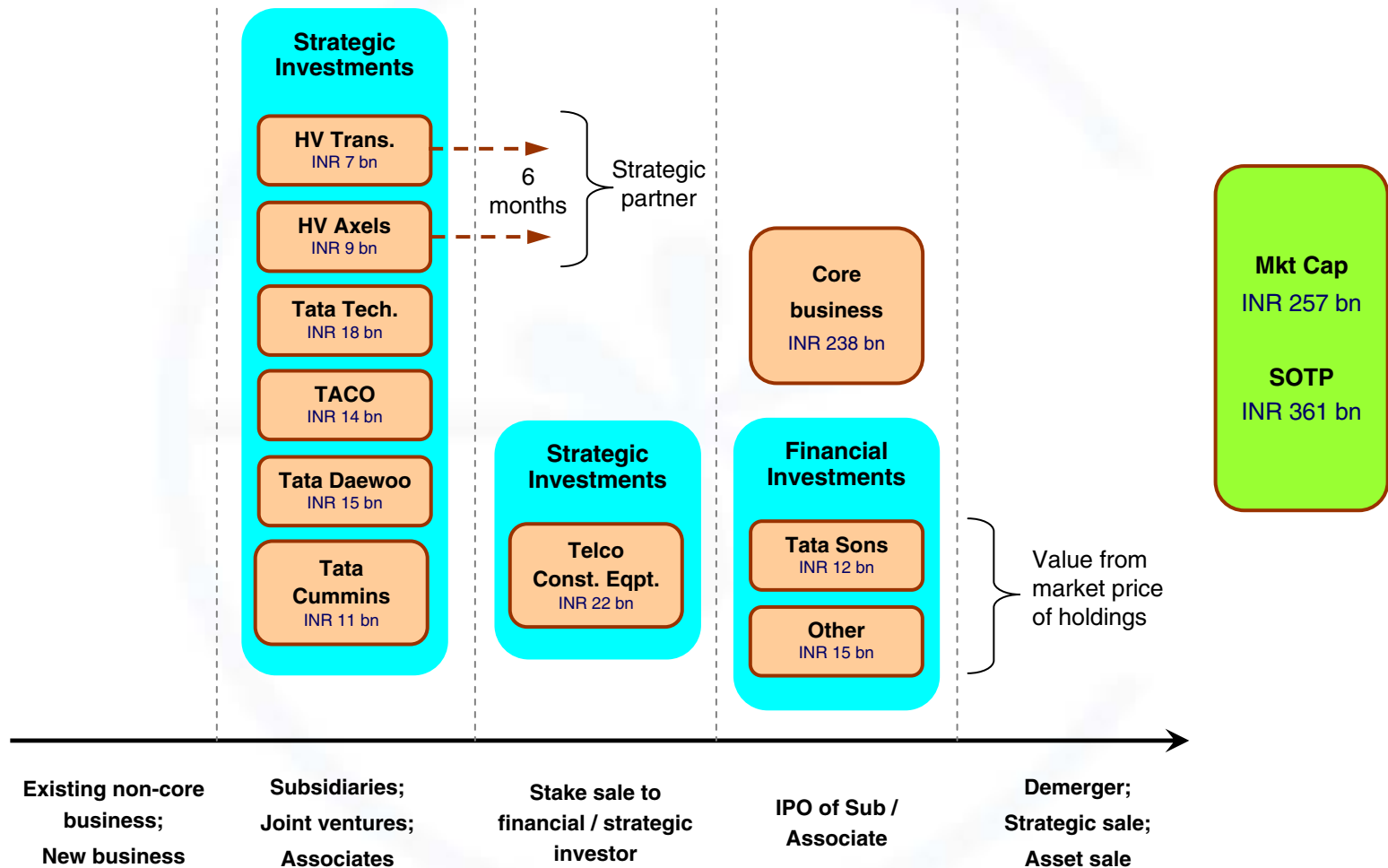
Price: INR 1,548 Mkt Cap: INR 815 bn / USD 20.2bn



Tata Motors - value from backward integrated subsidiaries

SOTP upside 40%

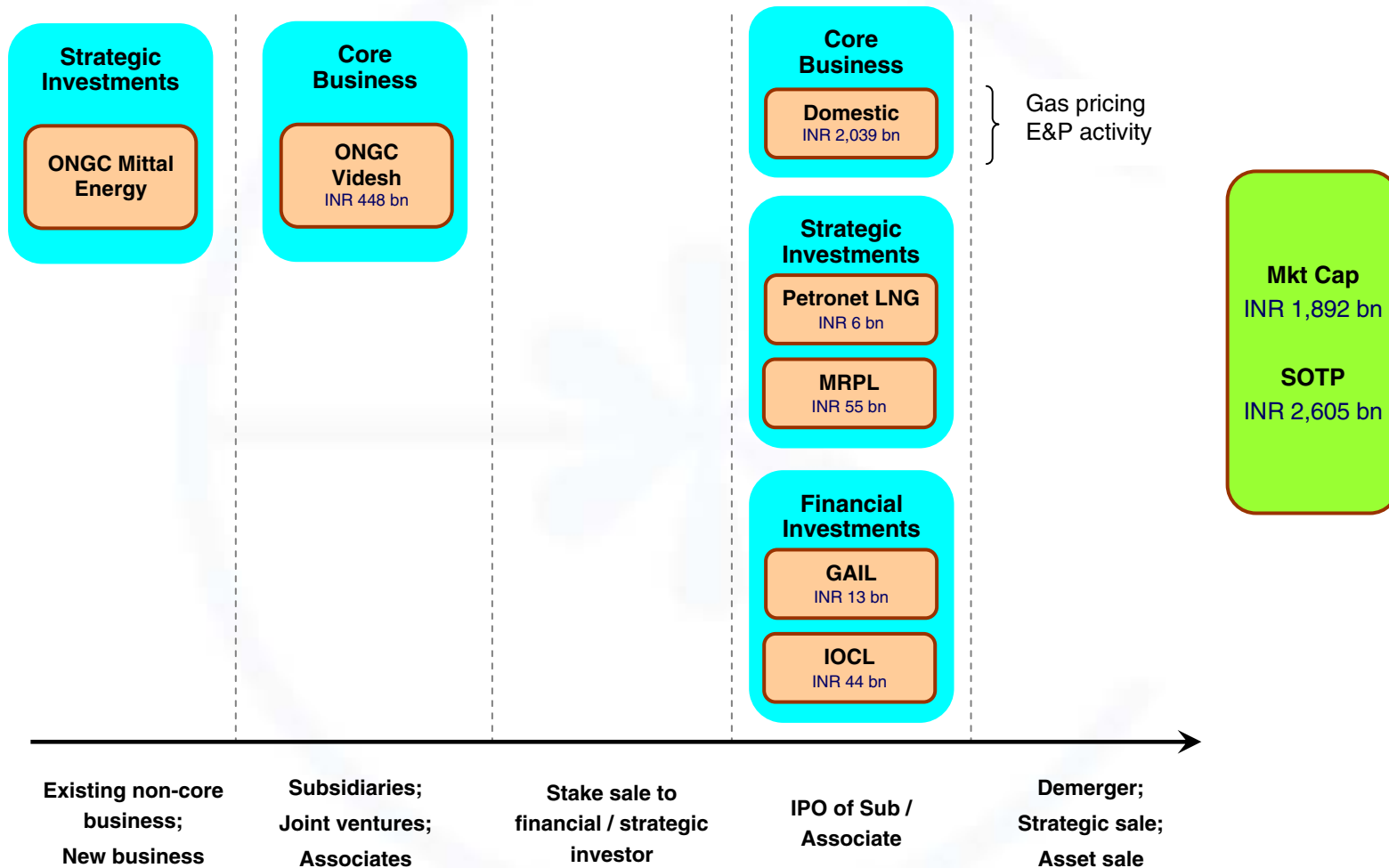
Price: INR 667 Mkt Cap: INR 257 bn / USD 6.4bn



Oil and Natural Gas Corp. - value from E&P activity

Price: INR 884 Mkt Cap: INR 1,892 bn / USD 46.8bn

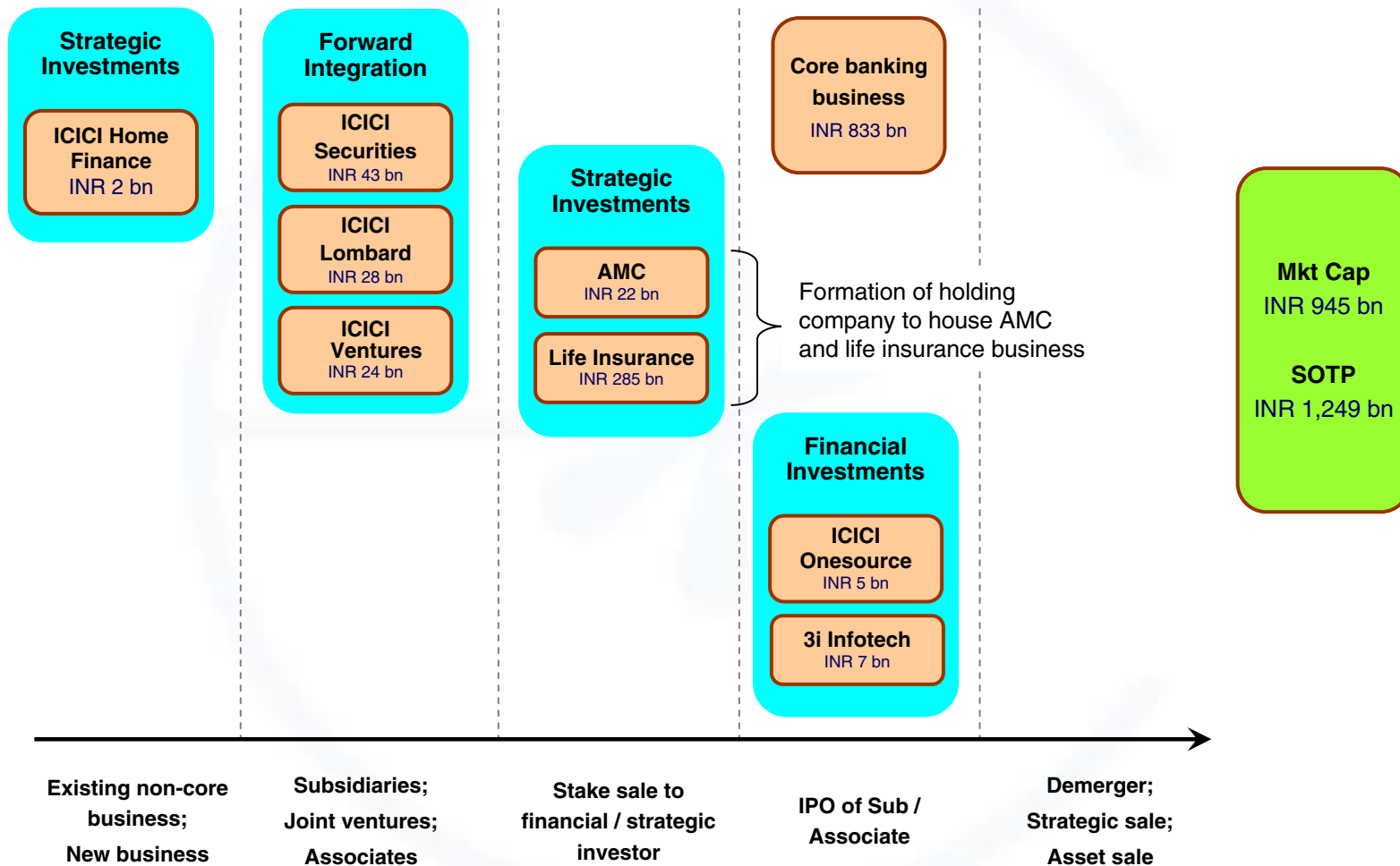
SOTP upside 38%



ICICI Bank - value from non-banking businesses

Price: INR 891 Mkt Cap: INR 945bn / USD 23.4bn

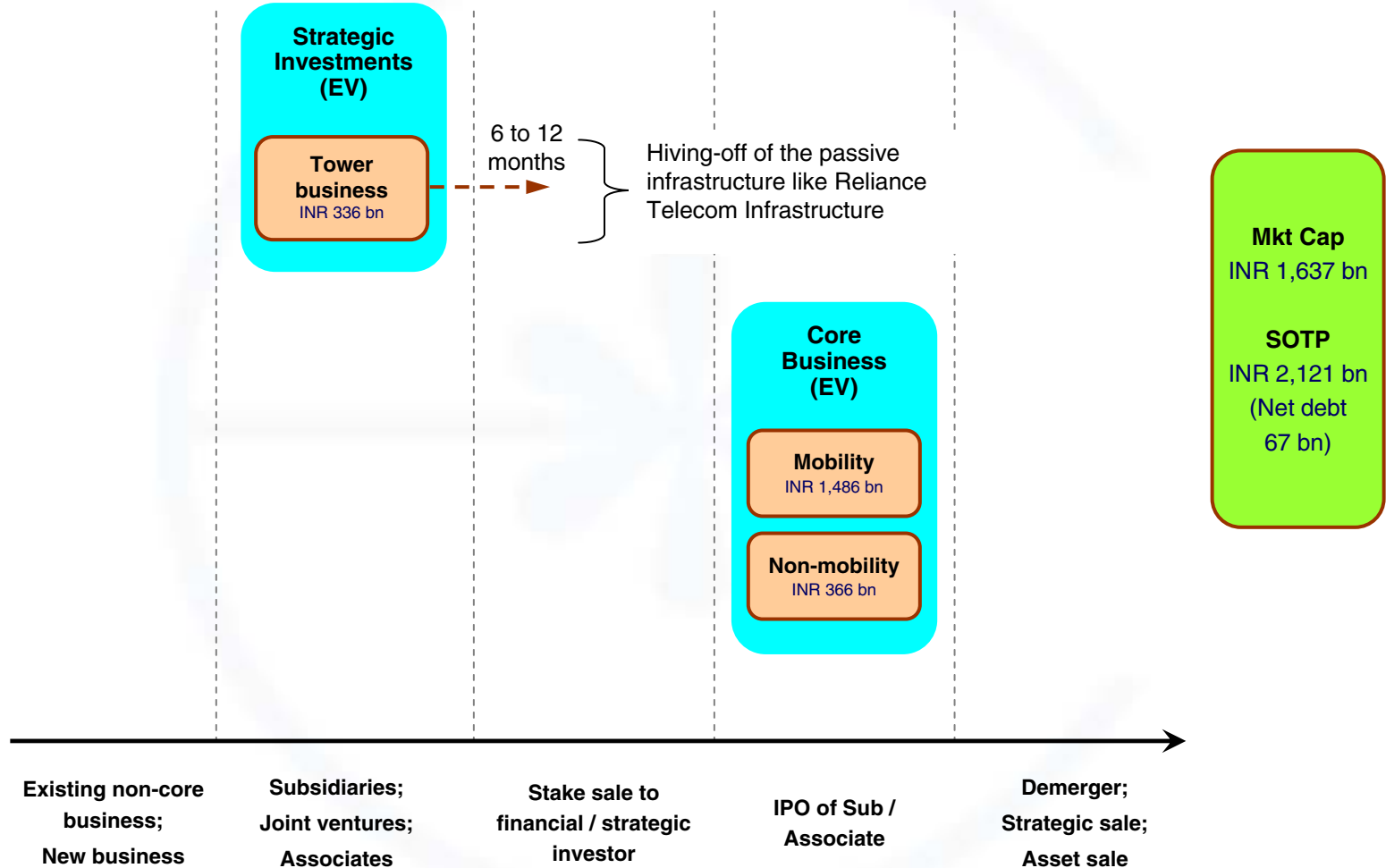
SOTP upside 32%



Bharti Airtel - value from passive infrastructure

SOTP upside 30%

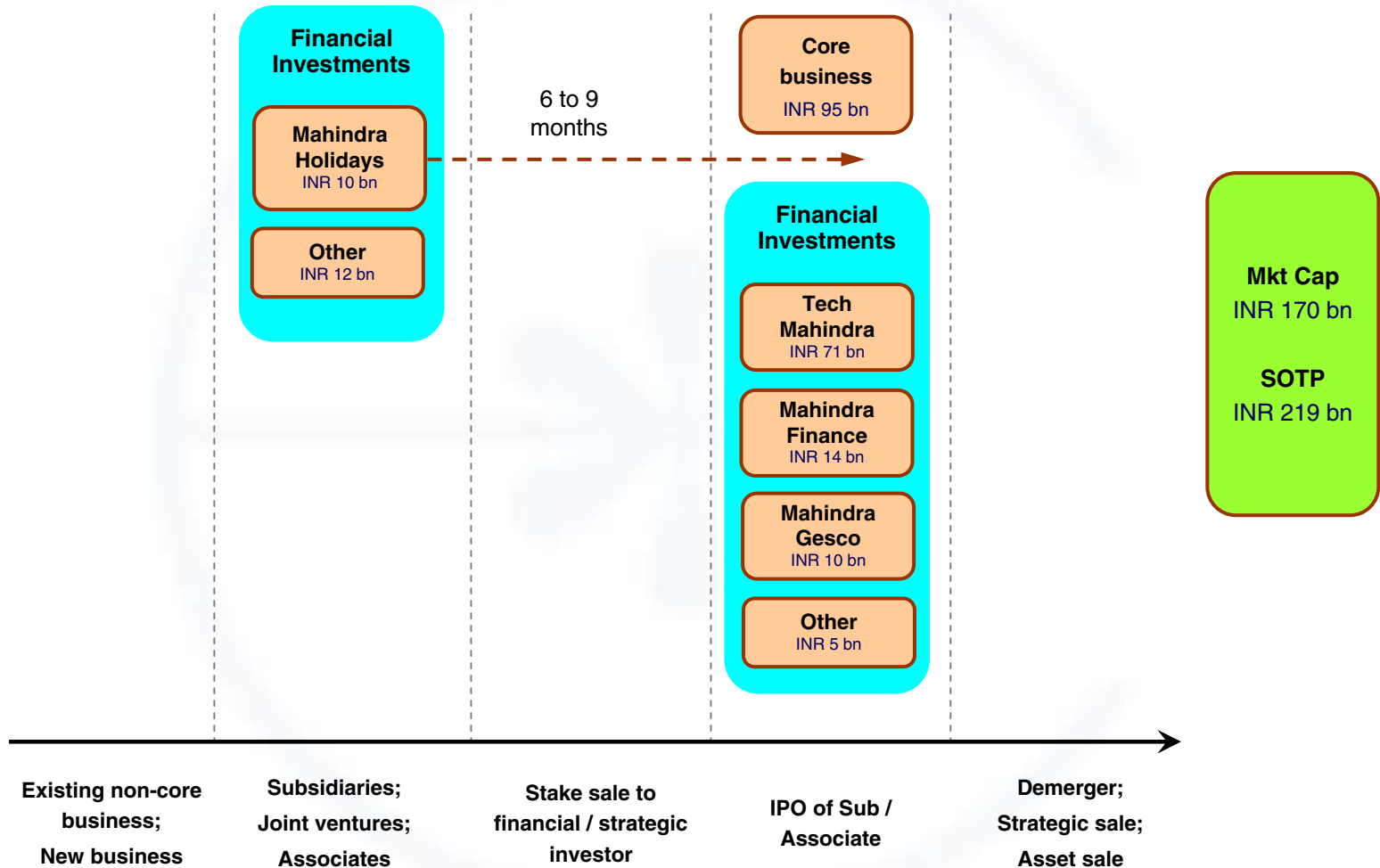
Price: INR 863 Mkt Cap: INR 1,637 bn / USD 40.5bn



Mahindra and Mahindra - value from unrelated subsidiaries

SOTP upside 29%

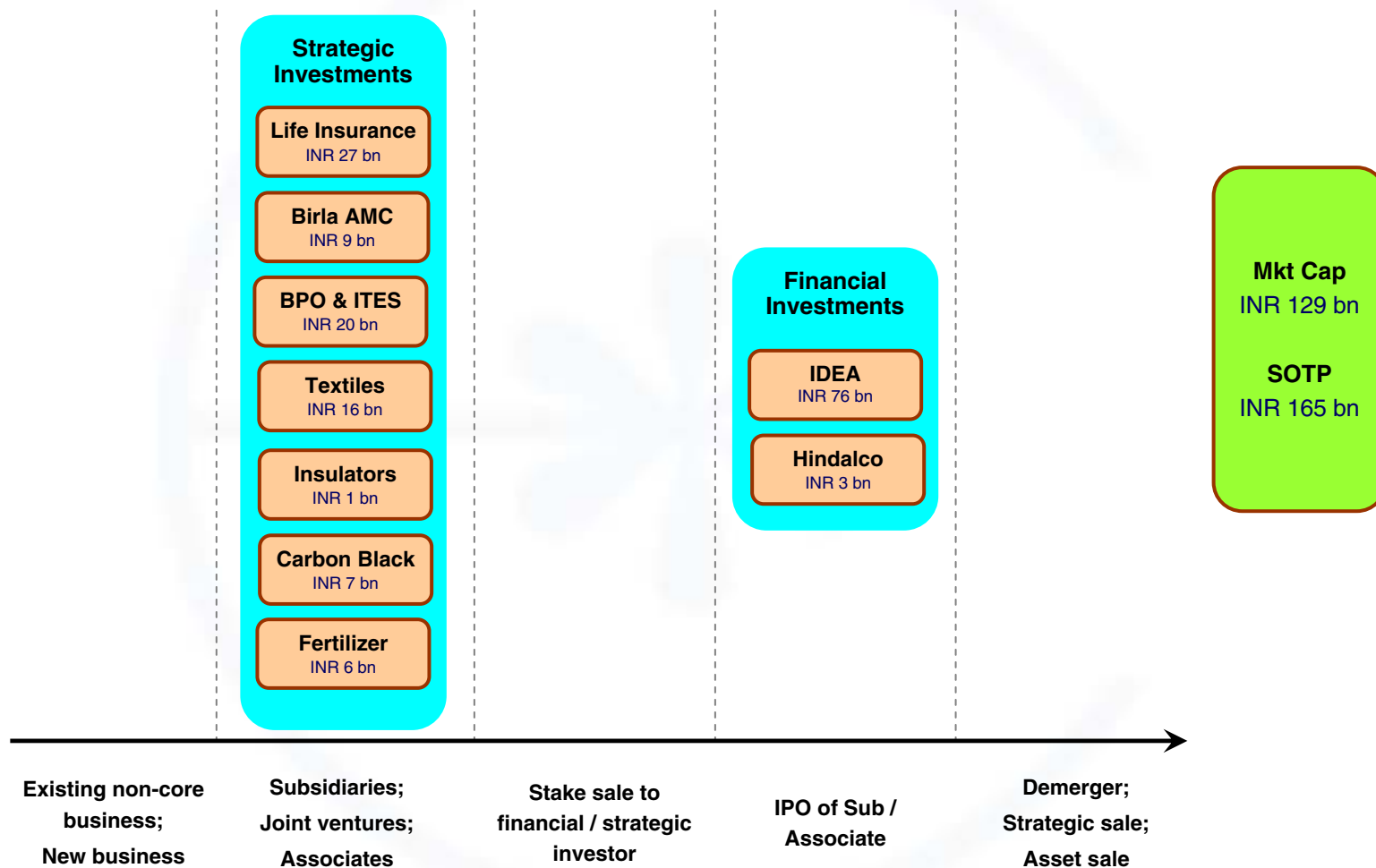
Price: INR 694 Mkt Cap: INR 170 bn / USD 4.2bn



Aditya Birla Nuvo – value from diversified business structure

SOTP upside 27%

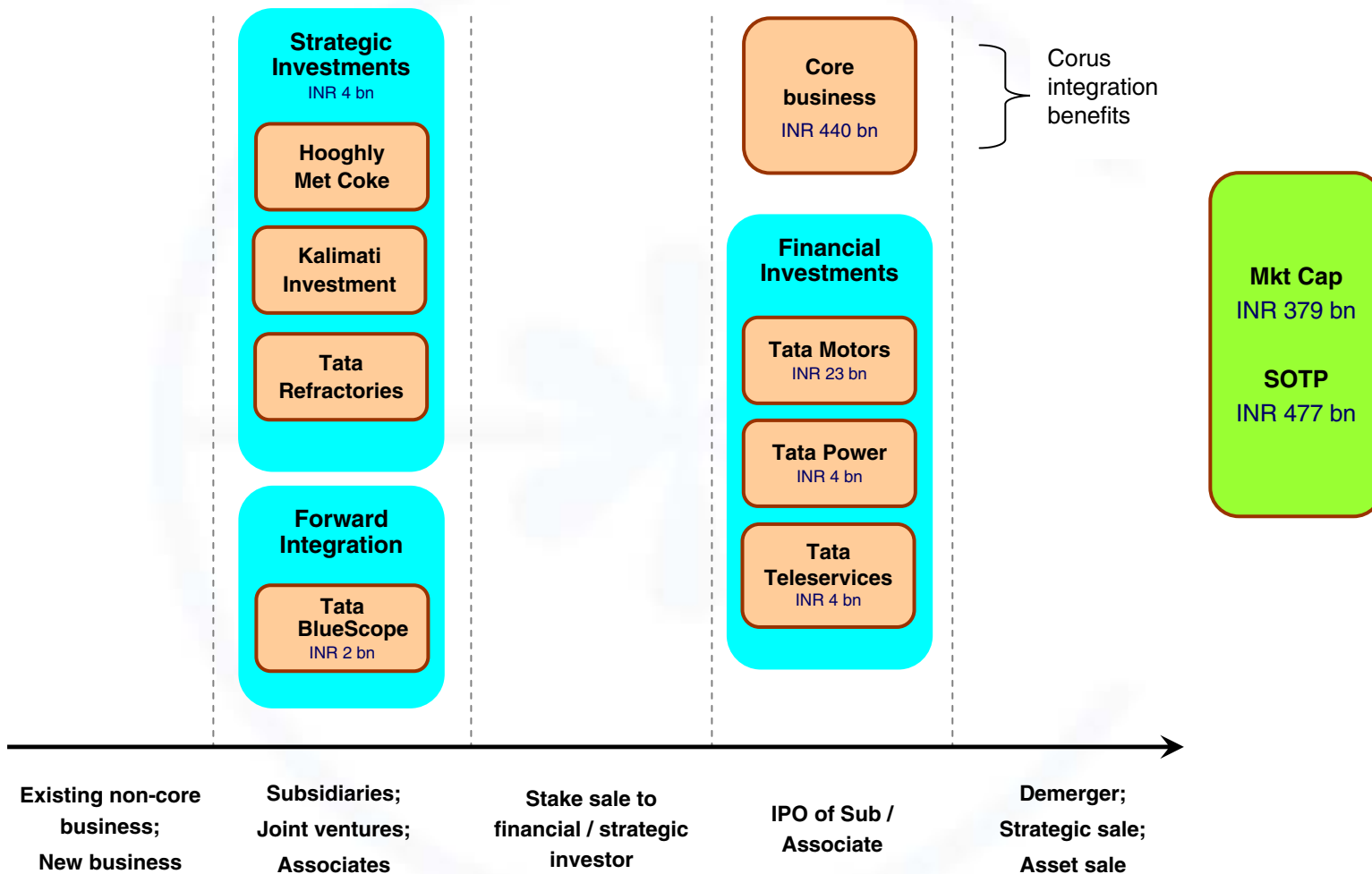
Price: INR 1385 Mkt Cap: INR 129 bn / USD 3.2bn



Tata Steel - value from integration benefits

SOTP upside 26%

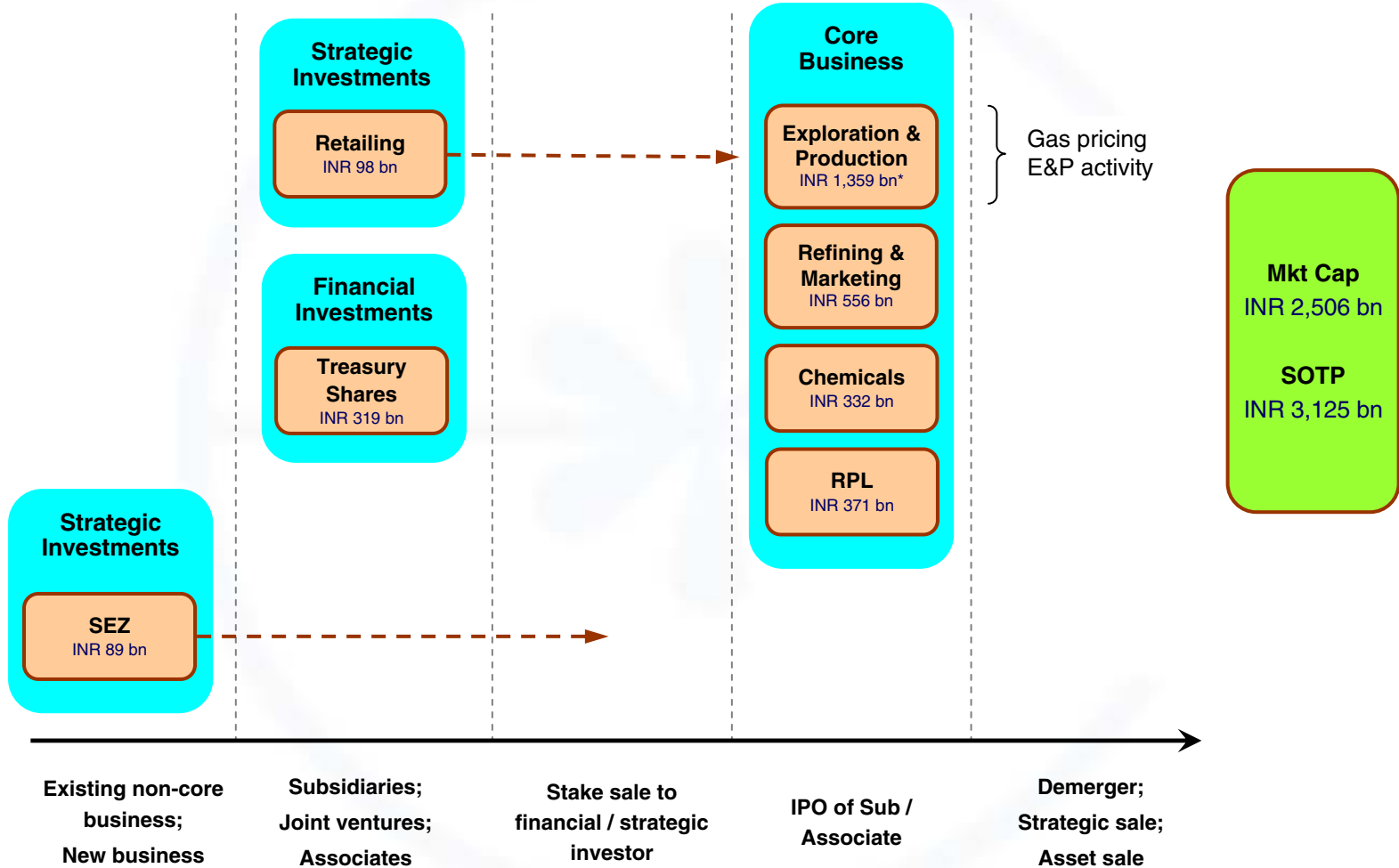
Price: INR 622 Mkt Cap: INR 379 bn / USD 9.4bn



Reliance Industries - value from new business activities

Price: INR 1,798 Mkt Cap: INR 2,506 bn / USD 62.0bn

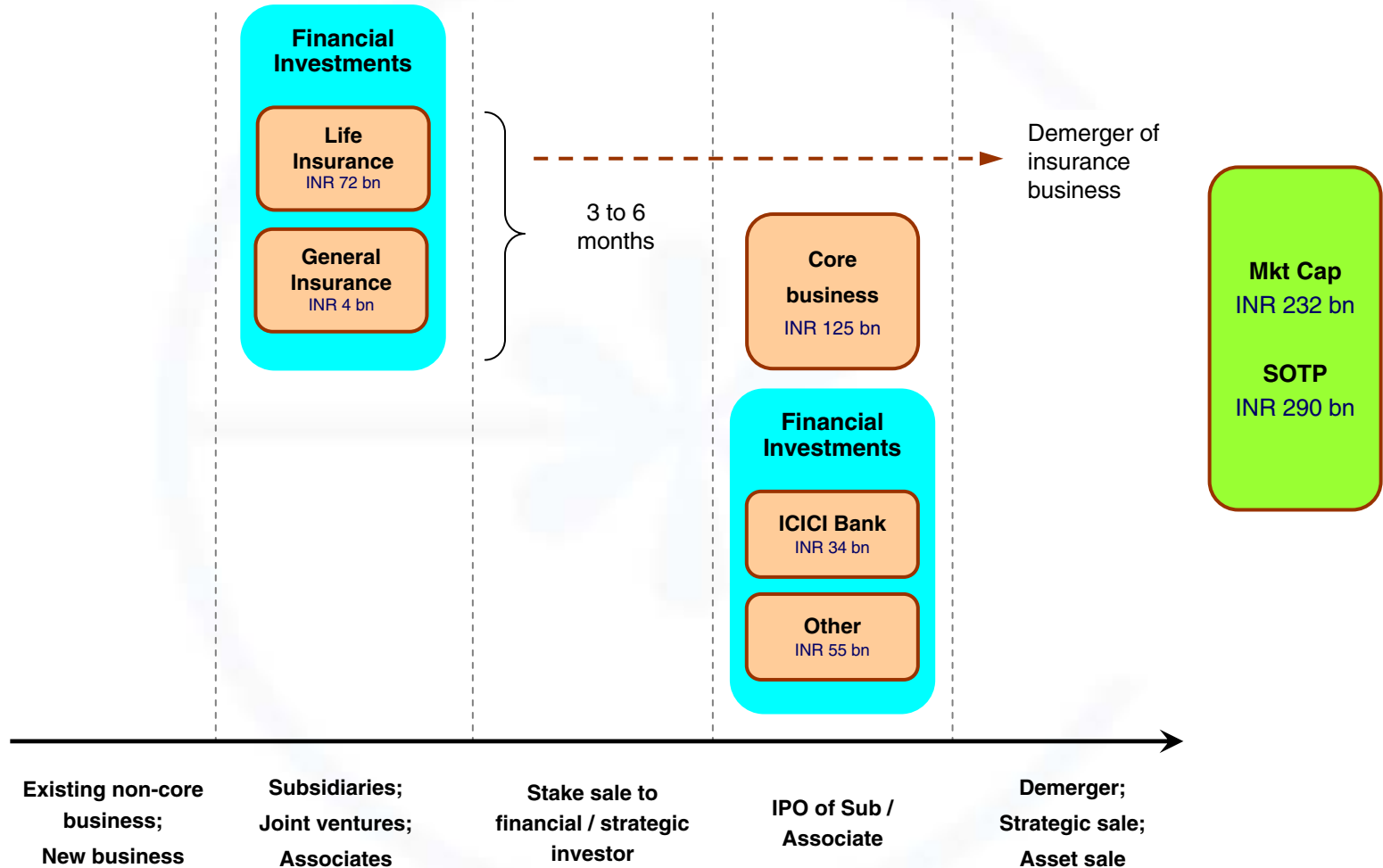
SOTP upside 25%



Bajaj Auto - value from insurance business

SOTP upside 25%

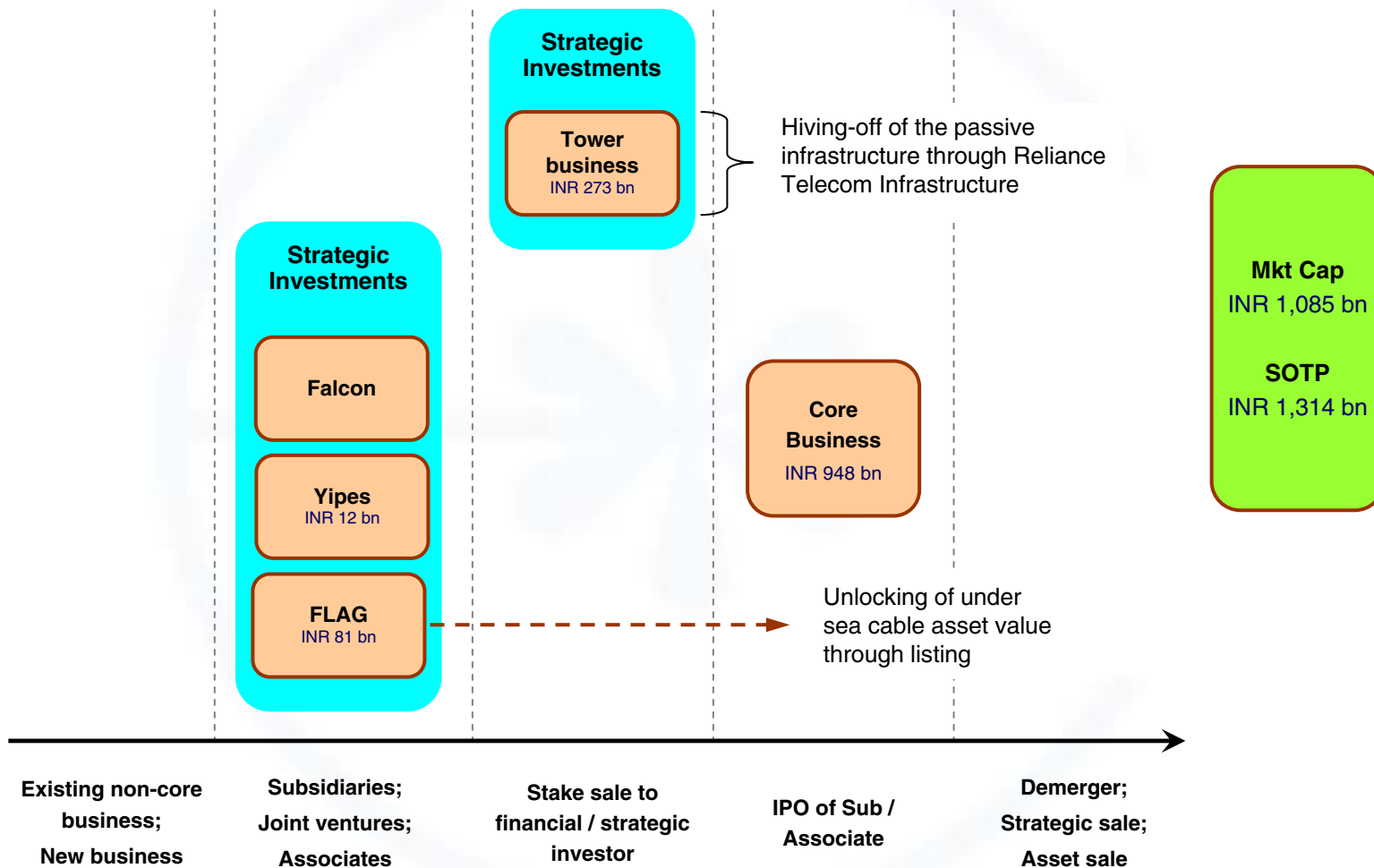
Price: INR 2,288 Mkt Cap: INR 232 bn / USD 5.7bn



Reliance Communications - value from passive infrastructure

SOTP upside 21%

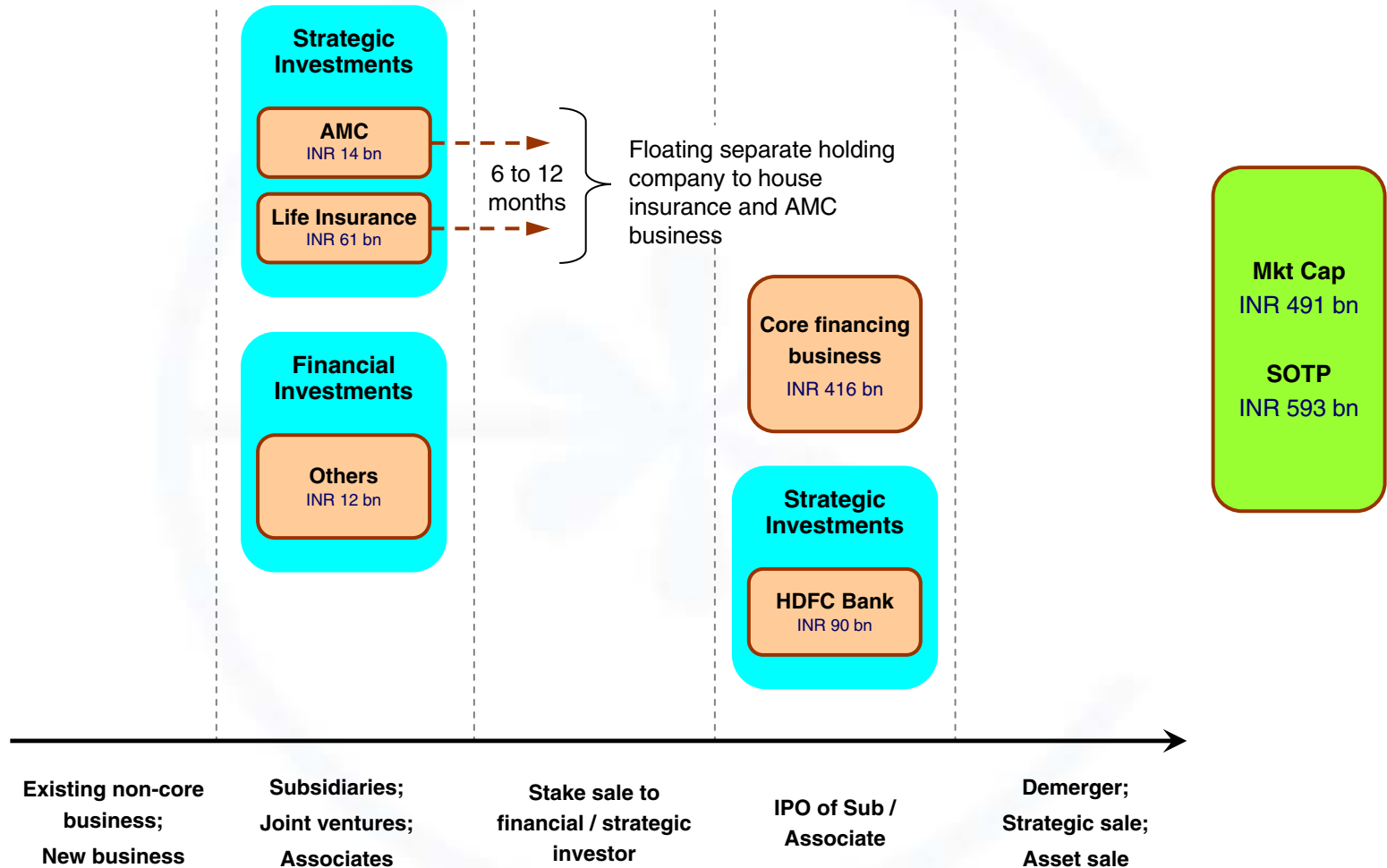
Price: INR 531 Mkt Cap: INR 1,085 bn / USD 26.9bn



HDFC - value from non-banking businesses

SOTP upside 21%

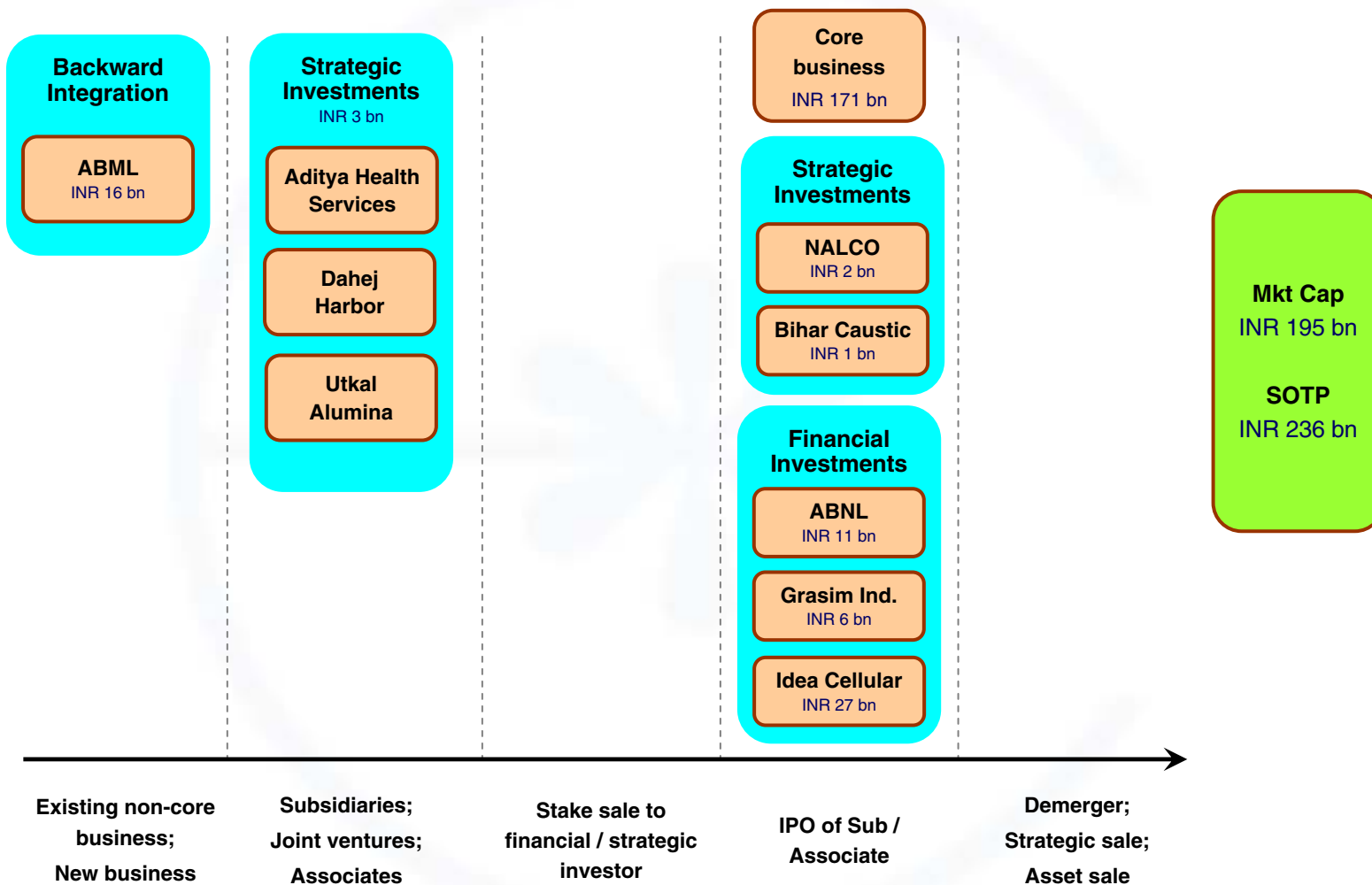
Price: INR 1,941 Mkt Cap: INR 491 bn / USD 12.1bn



Hindalco Industries - value from unrelated subsidiaries

Price: INR 159 Mkt Cap: INR 195 bn / USD 4.8bn

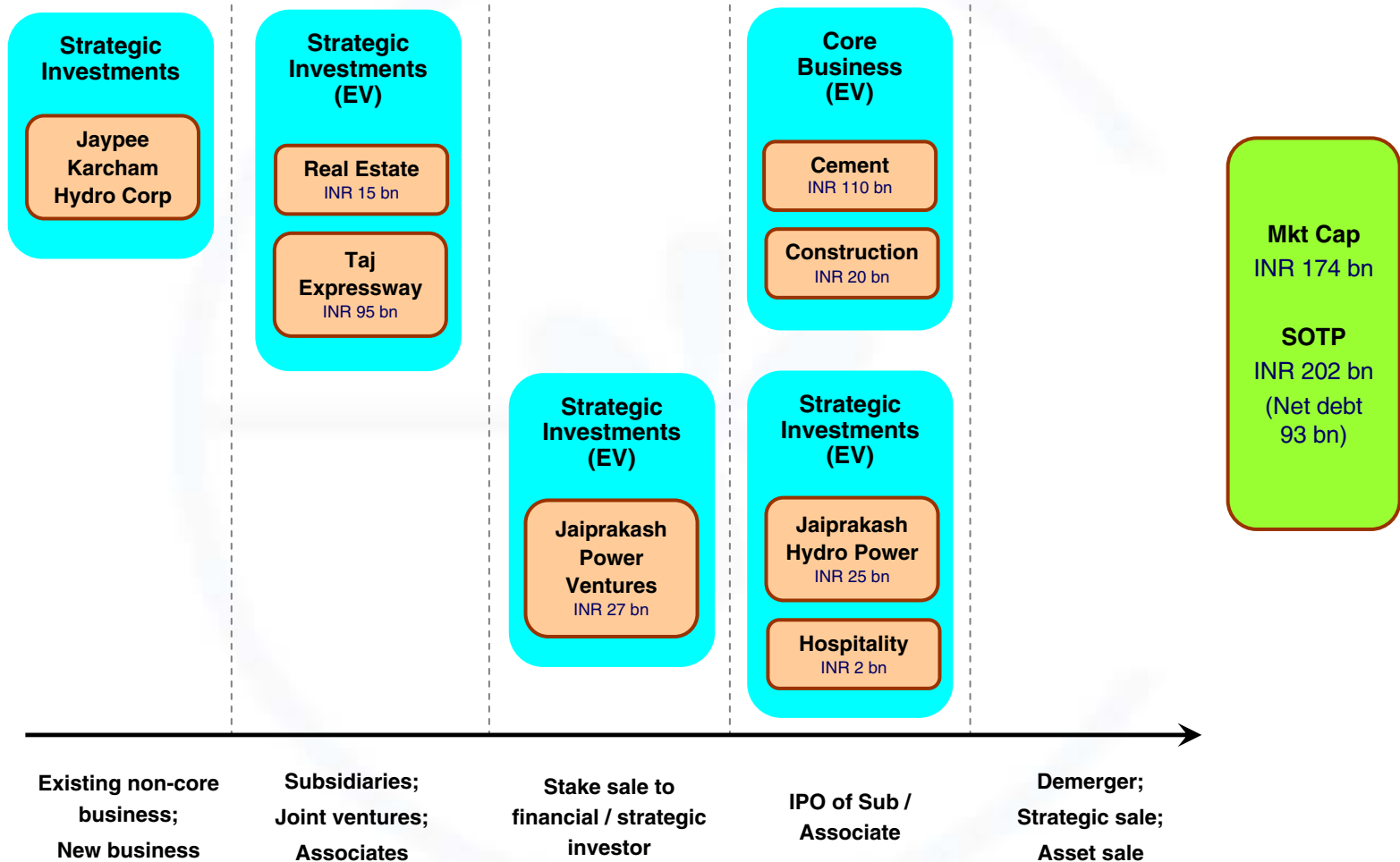
SOTP upside 21%



Jaiprakash Associates - value from subsidiaries

Price: INR 796 Mkt Cap: INR 174 bn / USD 4.3bn

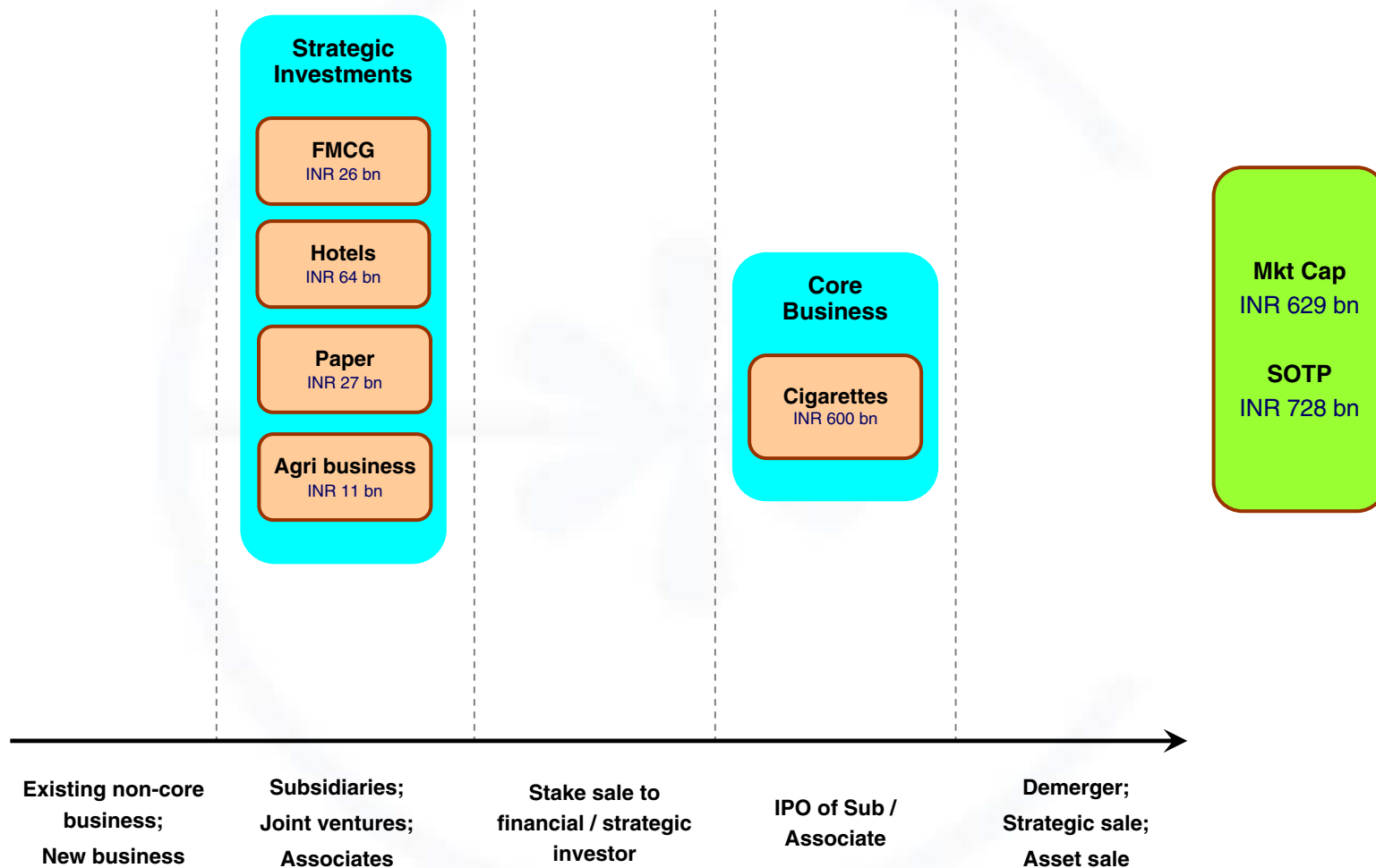
SOTP upside 16%



ITC - value from diversified business structure

SOTP upside 16%

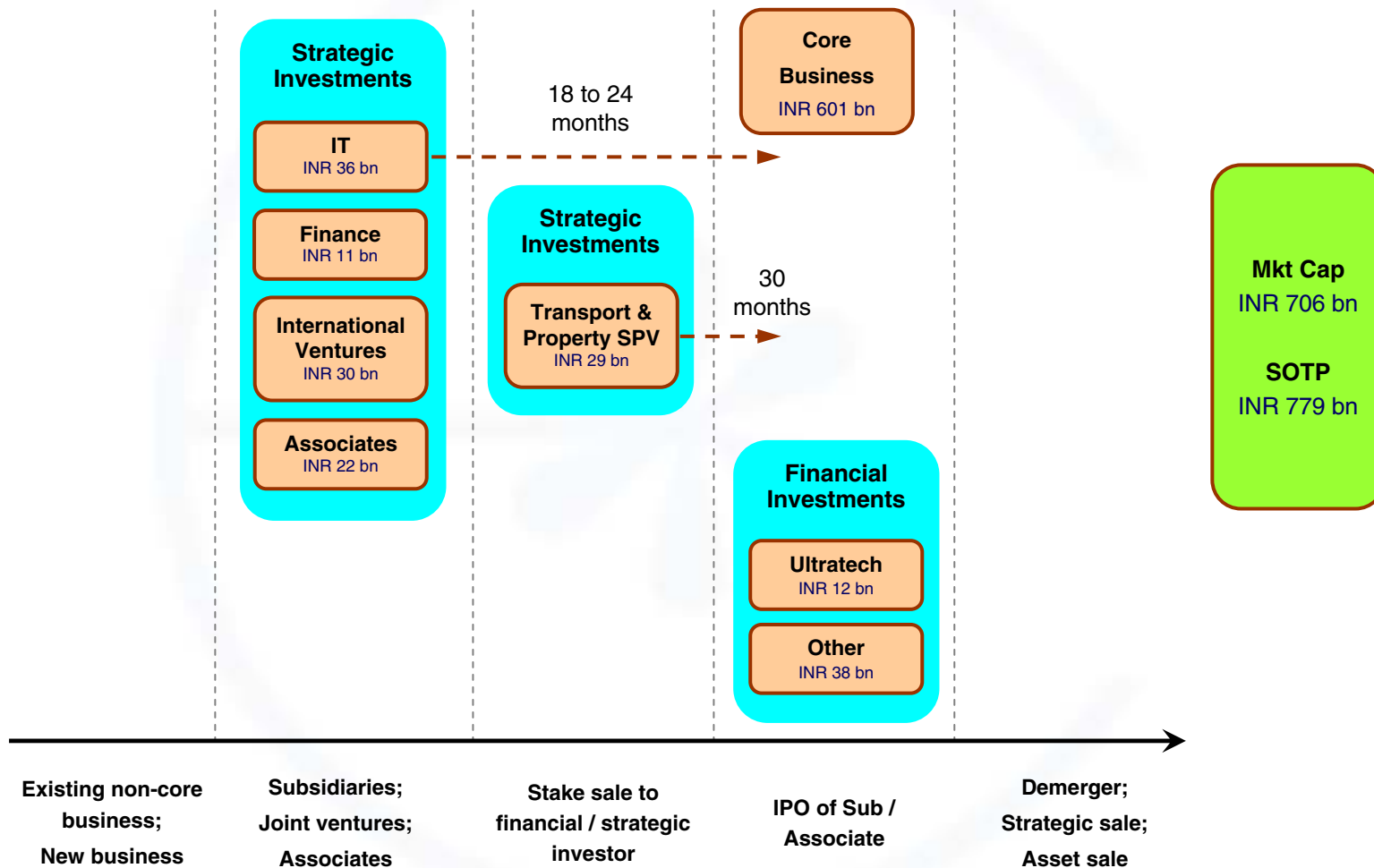
Price: INR 167 Mkt Cap: INR 629 bn / USD 15.6bn



Larsen and Toubro - value from unwinding conglomerate structure

SOTP upside 10%

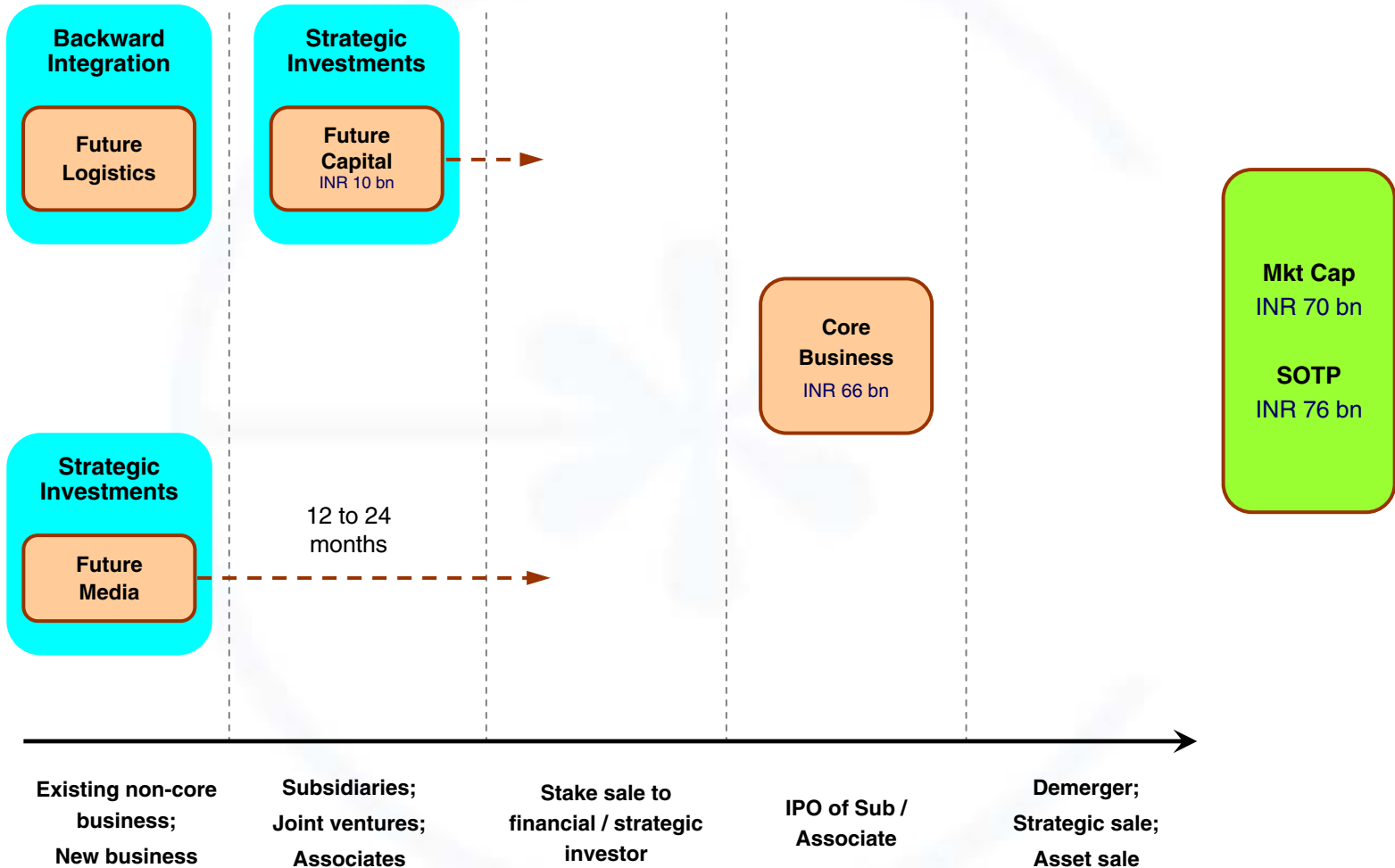
Price: INR 2,485 Mkt Cap: INR 706 bn / USD 17.5bn



Pantaloon Retail - value from new business initiatives

SOTP upside 9%

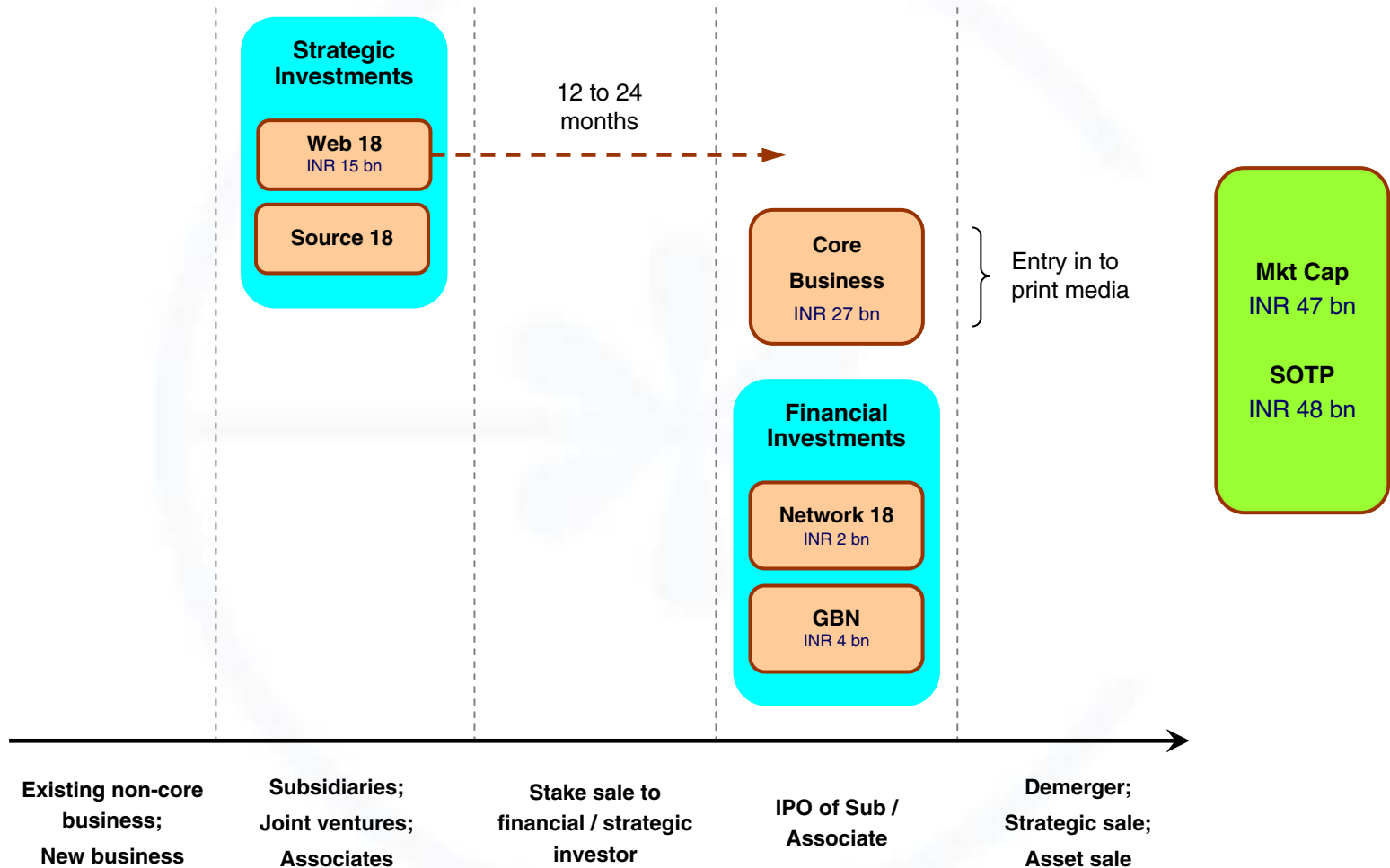
Price: INR 496 Mkt Cap: INR 70 bn / USD 1.7bn



Television Eighteen - value from related subsidiaries

SOTP upside 2%

Price: INR 824 Mkt Cap: INR 47 bn / USD 1.2bn



A few other candidates

Company	SOTP upside potential
Adani Enterprises	Unlocking diversified business structure
Adhunik Metaliks	Captive mines
Construction (IVRCL, Nagarjuna, HCC, Gammon, BLK)	Real estate, infrastructure BOT
DLF	REIT
Emco	Merchant power
Financial Technologies	Listing of MCX, other exchanges
Godrej Industries	Real estate
Hindustan Unilever	Real estate
IDFC	NSE stake, investments in PE fund, unlisted investments
IFCI	Value of investments, real estate, strategic stake sale
Indiabulls	Separation of broking and credit businesses
Jindal Steel & Power	Merchant power, captive mines
Max India	Unlocking diversified business structure
Moser Baer	PE/IPO of PV cell business
Navabharat Ventures	Merchant power
Ranbaxy, Dr. Reddy's, Glenmark, Nicholas Piramal, Biocon	R&D, Out-licensing of molecules, M&A
Reliance Energy	EPC/BOT, merchant power
Sintex	Unlocking diversified business structure
Tata Power	EPC, captive mines, merchant power
UB Holdings	PE/IPO/strategic sale in Kingfisher Air
Videocon	Separation of E&P business, real estate, retail
VSNL, MTNL	Real estate

- * Besides these, there are quite a few companies that are primarily valued only on an SOTP basis such as Reliance Capital, GMR, etc.

Balance sheet value unlocking – is this sustainable?

- * A large proportion of existing balance sheet value is explained by historical reasons
- * However, we believe that going forward, such value will as much be on account of historical costs as of ongoing opportunities
- * Such opportunities will continue to come up for a number of reasons
 - * Privatization and deregulation opens up new areas, e.g. infrastructure asset ownership
 - * Growth opportunities in adjacent markets, e.g. NDTV and TV18 entry into entertainment, banks into insurance
 - * Forward and backward integration, e.g. acquiring mines, technology, products
 - * Continuing investment in technology/IPR/R&D
 - * Sunrise sectors where there is little competition, e.g. retail, alternate energy
- * The underlying assumption is that of continued robust performance generating strong cash flows and keeping corporate confidence high

Limitations to our approach

- * SOTP valuations are dependant on stage of value unlocking - in many cases these may be understated given limited visibility of movement to higher stages
- * While the framework provides value buckets to identify 'assets', hidden assets are not considered; similarly it is not possible to value assets where adequate details are not available, e.g. real estate
- * Conversely, given heightened awareness of the SOTP approach, it is possible that individual parts may be valued ahead of what the value unlocking stage dictates, leading to over-valuation
- * We assume that:
 - * Indian corporates will actively seek value unlocking opportunities
 - * Fundamental parameters of the economy and corporate performance do not change drastically
 - * Adverse global events do not significant affect investor sentiment

This Information Package is distributed by Edelweiss on a strictly confidential basis. This Information Package and the information and projections contained herein may not be disclosed, reproduced or used in whole or in part for any purpose or furnished to any other persons without the express prior written permission of Edelweiss.

This Information Package is distributed by Edelweiss upon the express understanding that no information herein contained has been independently verified. Further, no representation or warranty expressed or implied is made nor is any responsibility of any kind accepted with respect to the completeness or accuracy of any information. Also no representation or warranty expressed or implied is made that such information remains unchanged in any respect as of any date or dates after those stated herein with respect to any matter concerning any statement made in this Information Package. Edelweiss and its directors, employees, agents and consultants shall have no liability (including liability to any person by reason of negligence or negligent misstatement) for any statements, opinions, information or matters (express or implied) arising out of, contained in or derived from, or for any omissions from the Information Package. All recipients of the Information Package should make their own independent evaluations and should conduct their own investigation and analysis and should check the accuracy, reliability and completeness of the Information and obtain independent and specific advice from appropriate professional advisers, as they deem necessary.

Where this Information Package summarizes the provisions of any other document, that summary should not be relied upon and the relevant documentation must be referred to for its full effect.