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Investor Update
June ,2010

India Notes

India Economy Grows at Fastest Pace in 6 Months....

India's economy grew at its fastest pace in six months in the quarter through March 2010, fuelled mainly by government and consumer spending. The 8.6 percent expansion in the fourth quarter of the fiscal year FY10 lifted the annual average growth rate for the full fiscal year to a slightly better-than-expected 7.4 percent.

India's economy had grown 6.7 percent in FY09, and the Q4 FY10 growth rate matches the revised data for the second quarter of FY10.

Govt kitty swells by $15 bn as telcos pay 3G fee in full

The recently concluded auction of 3G spectrum which earned the revenues of € 11.90 billion (Rs 677.19 billion) has put the government in a better position to handle its finances. Besides, the government expects more revenue from the forthcoming auction of broadband wireless access. The government had projected a fiscal deficit of 5.5 per cent for 2010-11 against an estimated 6.7 per cent in the previous year. The additional revenue from 3G spectrum auction alone would enable the Centre to cut its fiscal deficit from estimated 5.5 per cent of GDP to little over 5 per cent during 2010-11.

Real Estate revival gains strength

Following the record € 702 million (Rs 40 billion) land transaction in MMRDA's Wadala auction, various government agencies (RLDA, MMRDA, NTC) are now reviving their land auction plans in the Mumbai city. More than 25 acres of land is likely to come up for auction in Central Mumbai and BKC over the next few months thereby augmenting the supply in the suburbs by 20msf. While the upcoming supply is more than Mumbai's total last year absorption (16msf), it will take atleast 4-5 years for the build out to happen and hence may not exert immediate pressure on prices.

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Economy & Markets

8.6% surge in Q4 boosts FY10 GDP growth to 7.4%

The Indian economy roared past estimates to post a growth rate of 8.6% in the January-March quarter of FY10. The quarter's strong showing also helped India end the fiscal year with 7.4% growth, against the earlier estimate of 7.2%. Manufacturing led the way, with a 16.3% growth in the quarter and 10.8% overall. Even agriculture, which was expected to decline, ended with a marginal growth of 0.2% year-on-year after growing 0.7% in Q4. The GDP growth rate had slowed to 6.7% during FY09 following the global economic crisis, after topping 9% in the previous three years. The Finance Minister reiterated his confidence that the economy would grow at 8.5%-plus in 2010-11.

The fourth-quarter performance is particularly commendable in light of the dip in the third quarter to 6.5% from 8.6% in the second quarter due to the impact of a drought-like situation in the country. China is the only large economy with a higher growth rate at 11.9% in the January-March quarter. The rest of the world is witnessing a fragile recovery, which is now under threat due to the brewing Euro-zone crisis. The sixteen developed countries in the Euro-zone expanded by just 0.2% in the quarter. The United States and Japan grew at 0.8% and 1.2% respectively.

In the backdrop of slow recovery in the global economy, the strong growth is a testimony to India’s vibrant domestic markets. The growth during FY10 also showed that stimulus provided by government has yielded desired results. The manufacturing sector, which bore the brunt of slowdown and grew 3.8% in FY09, bounced back and posted 10.8% growth in FY10.

Inflation higher than comfort level: RBI

India's inflation is still higher than the central bank's comfort level and the country's 7.4 per cent expansion seen in the fiscal year 2009/10 is encouraging but not surprising, according to Reserve Bank of India (RBI) Governor Duvvuri Subbarao. India's annual wholesale inflation was at 9.59 per cent in April, coming off from a 16-month high of 10 per cent in February, providing more room for the central bank to hold off raising interest rates at least till its next review on July 27. Official data showed Asia's third-largest economy grew 8.6 per cent in the March quarter, its fastest in six months, broadly in line with market expectations and growth in the 2009/10 year was 7.4 per cent, from 6.7 per cent in 2008/09. The Governor added that RBI will also take into account other global developments while formulating monetary policy and that India's external sector did not face any problems because of the Greek crisis. The RBI governor said there was no need to be overly concerned about the flight to the dollar as it was part of the financial markets' natural reaction to shift to safety.

Inflation to remain high:

Goldman Sachs has observed that inflation will remain high at 7.5% during the fiscal on the back of strong demand, which may lead the Reserve Bank to further tighten policy rates to reign it in. However, the hike is not expected before the next policy meeting on July 27, 2010.

IIP: Healthy numbers

India's industrial output rose by an impressive 13.5 per cent in March, despite the withdrawal of fiscal stimuli packages and the tightening of monetary policy, taking the overall expansion for the previous fiscal to 10.4 per cent. The Index of Industrial Production (IIP) had expanded by 0.3 per cent in March last year and 2.8 per cent during the whole of 2008-09.

Data released by the Ministry of Statistics and Programme Implementation shows that the manufacturing output rose 14.3 per cent in March, mining by 11 per cent and electricity by 7.7 per cent. The cumulative growth for 2009-10 for these three sectors were 10.9 per cent, 9.7 per cent and 6 per cent respectively.

In terms of industries, as many as 14 out of the 17 industry groups have shown positive growth during the month of March 2010, as compared to the corresponding month of the previous year.

Early signs of pick-up in capex

During FY10, the private consumption slowed down, while capex picked up, particularly in the last quarter. Peaking capacity utilization has prompted corporates to make fresh investments. The government expenditure continues to remain strong (but lower than previous fiscal). During FY10 exports contributed positively to the GDP growth as against negatively in FY09. However, going forward contributions from government expenditure and net exports are likely to reduce. Therefore, pick-up in private consumption is important to sustain uptrend in investments.

RBI to continue with its cautious monetary tightening

We believe that given the lingering global uncertainties and still nascent global economic recovery, RBI's cautious approach to monetary tightening is appropriate. In the coming months, IIP would moderate from its current double-digit growth rates and the headline inflation will also see some softening. Besides, excess liquidity conditions would fade as reflected in the reverse repo balances.

In light of this, it is expected that pressure on the central bank to tighten monetary policy has reduced and, therefore, RBI will continue with its cautious approach towards monetary tightening using repo/reverse repo instruments.

Auto Sales at all time high

India's top auto makers posted robust sales growth in May 2010 as demand for vehicles in Asia's third-biggest market continues to rise despite price increases and a partial withdrawal of government stimulus measures. Automobile sales in India have been growing since early 2009, helped by the government's stimulus steps, easier availability of loans and the launch of several new models. Sales growth isn't showing any signs of cooling off, even after the government rolled back some tax incentives, while most auto makers raised prices thrice in 2010 to offset a rise in taxes and input costs.

A case in the point is Tata Motors Ltd., India's biggest truck maker and the third-biggest car maker by sales. The company sold 56,779 vehicles locally and overseas in May, a 41% jump from the previous year. The exports for the month more than doubled year on year to 3,978 vehicles as against 1,804 vehicles. It also sold 31,475 trucks and buses locally during May, a growth of 37% year on year.

Fiscal deficit is key focus for Foreign Institutional Investors (FIIs)

Historically FIIs focus on India has been dominated by its fiscal position. Developments over the past few weeks are incrementally positive for India's fiscal position- One, the proceeds from 3G and WiMax license sales are much higher than budgeted (€ 11.90 billion (Rs 677.19 billion) vs € 6.15 billion (Rs 350 billion)). Two, natural gas price rise can add € 1 billion (Rs 60.5 billion)in FY11E revenue to Oil PSUs & the government. Three, potential reforms on fuel prices are likely to reduce the government's fiscal burden. All these events are potentially accretive and expected to bode well for India's fiscal position. This is especially important as a lot of the institutional focus has been focused on the strength of the sovereign fiscal positions post the PIIGS crisis.

Real Estate

Land supply and transactions picking up pace

Mumbai witnessed its largest land deal last month wherein MMRDA sold a 6 acre plot for Rs 40 bn to Lodha Group, a private developer. The plot was sold at a 105% premium to its reserve price. The second bidder was 15% below the winning bid. The auction attracted number of developers because of a deferred land payment schedule with majority of the payment being back ended.

Following the success of MMRDA's Wadala auction last month, various government agencies (RLDA, MMRDA, NTC) are now reviving their land auction plans for the city. More than 25 acres of land is likely to come up in Central Mumbai and Bandra Kurla Complex over the next few months. Upcoming land auctions coupled with recently concluded land transactions will augment the supply in the suburbs by 20msf. While the new planned supply is more than Mumbai's last year total absorption of 16msf, it will take atleast 4-5 years for the build out to happen and hence is unlikley to put an immediate pressure on prices

Seller	Location	Plot area	Estimated saleable area
Upcoming auctions			
MMRDA	BKC, Mumbai	3125 sq m	0.2
NTC - Bharat Mill	Central Mumbai	8 acres	2.1
NTC - Poddar Mill	Central Mumbai	2.5 acres	0.7
RLDA	Bandra, Mumbai	45731 sq m	2.9
Total			**5.9**
Recently concluded transaction			
MMRDA	Wadala, Mumbai	25000 sq m	8.0
GTC	Vile Parle, Mumbai	14 acre	2.3
Wadhwa	LBS Marg, Mumbai	18 acre	3.0
Total			**19.2**

**Saleable area in mn sq ft*

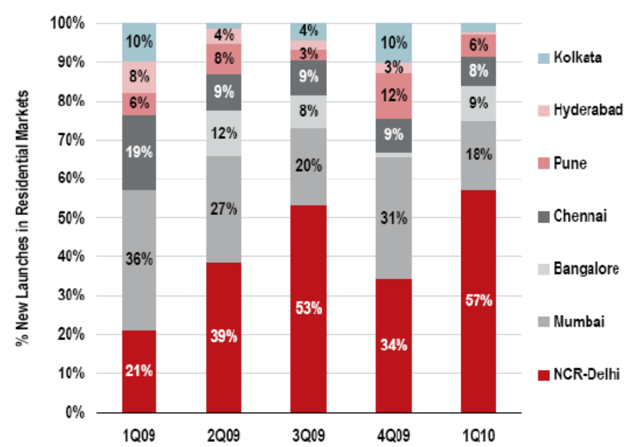
Residential volumes have declined in QI but are stabilizing at current levels

Residential volumes after witnessing a strong revival over the last year seems to have tapered off in QI as prices reach their peak levels in key cities (NCR/Mumbai). The year 2009 was one with record volumes for a number of developers, however incrementally volumes in the key markets have come off by 10-15% in 1Q10.

Decline in volumes can be attributed to tapering off of pent up demand and sharp price increases in few markets. Mumbai market seems to be the most stretched in terms of affordability while Bangalore looks the most attractive. Mumbai prices have risen sharply by 30-40% since Mar-09 and are now above their 2008 peak levels. Price inflation in other cities however has been between 5-15%. Given the decline in absorption, we expect the pace of prices to soften going ahead.

In terms of micro-markets, Bangalore is likely to outperform on the back of positive off-shoring outlook. Double-digit wage growth and strong hiring trends augur well for the Bangalore property market where prices and volumes are still ~20% off highs. Prominent Bangalore based developers Brigade, Sobha and Purvankara reported strong pick up in absorption over the last quarter. Encouraged by strong revival in buyer interest, these players have announced aggressive launch plans for FY11.

Residential lanches



Source: JLL REIS

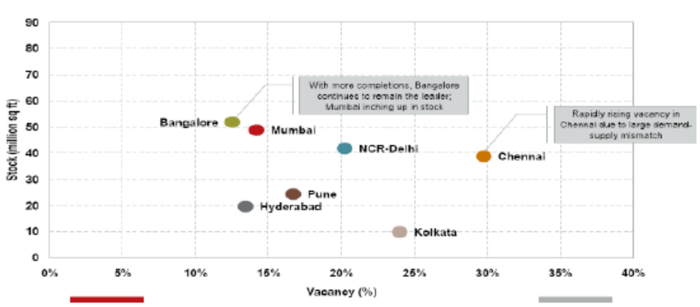
Office recovery is gaining traction; volumes should increase but new supply would likely keep rentals under check

Demand for office space continues to improve as rentals across markets seem to have bottomed out. Rentals for office space have stabilized after falling 30-40% from their peak levels. A number of companies that had earlier adopted a "wait and watch" approach are now looking to lease space. The market has witnessed a noticeable pick up in large ticket transactions over the last quarter in Mumbai/NCR. Though transaction prices are still off peak levels, a pickup in volumes is surely an encouraging sign.

While the demand revival to date has primarily been led by domestic sectors (pharma/telecom) and consolidation demand in city centric locations (of NCR/Mumbai), demand from IT sector has also started to return on the back of positive off-shoring trends. Even while absorption has picked up, rentals are likely to remain under pressure and vacancies will continue to increase across all markets due to huge supply pipeline (FY11E completions of 58.5 msf vs. absorption of 29.3 msf).

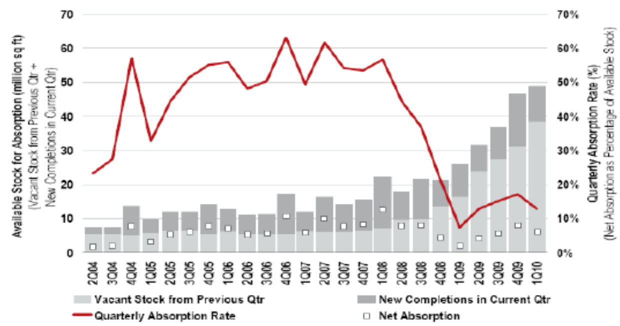
Capital values are expected to start increasing given the decline in yields. Investment yields across markets have declined by 50-100bps over the last year and the trend is expected to continue on the back improving demand environment and of reduced risk aversion. In terms of markets, Bangalore is likely to emerge as an outperformer on the back of healthy level of pre-leasing and affordable rents.

Stock vs Vacancy



Source: JLL, REIS

Key Absorption Trends



Retail showing signs of improvement as rentals bottom out

Retail market has witnessed an improvement in transaction activity over the last few months as developers become more flexible in terms of their asking rents and lease terms in order to ensure higher occupancy. Minimum guarantee coupled with revenue sharing has emerged as a favored model amongst the retailers over the past one year.

Even though absorption levels have picked up, rental values remain under pressure as supply continues to outstrip demand levels. The year 2010 is expected to witness completion of 16.4msf of retail space vs. an estimated absorption of ~9msf. Of the total expected supply, over 50% is expected to become operational by 2010 end. This would keep the vacancy levels elevated and rentals under check. Rentals across markets have corrected by 30-40% from their peak levels.

Most retailers (Pantaloons, Shoppers Stop) are witnessing positive sales trends as economic recovery gains pace. While improving retailer and consumer sentiment is an encouraging sign, we believe it may still be too early to call for a full recovery in this segment.

	Percentage of revenue as rent (%)
Hypermarket	3%-4%
Departmental Stores	7%-8%
Apparel	12%-18%
Footwear	15%-18%
Jewellery	2%-2.5%
Health and Beauty	10%-12%
Food	15%-20%
Entertainment	8%-10%