



JV CAPITAL SERVICES PVT. LTD

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IL&FS Investment Managers
INDUSTRY: Financial Services

CMP: 44.25
RISK PROFILE: High

BUY
TARGET: 75.0

Data Table

CMP	44.25
Target price(Rs)	75.00
Upside (%)	70%
52 Week H/L (Rs)	58.30 / 20.40
P/E Ratio	12.16
P/BV Ratio	6.76
Dividend Yield %	3.10%
Market cap (Rs. Cr)	898.50
6m Avg vol ('000Nos)	79,333
No. of o/s shares (cr)	20,30,27,595
FV (Rs)	2.00
NSE code	IVC

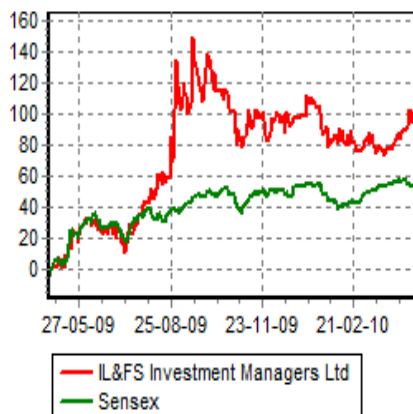
IL&FS Investment Managers Limited (IIML) is India's first and only listed Private Equity firm. IIML has been a pioneer in managing and advising private equity investments, ranging from Consumer Goods, Logistics, Real Estate and Infrastructure to sector agnostic Private Equity Funds. IIML has, to date, invested in over 100 investments and managed over 50 exits/liquidity events. IIML manages assets of around US\$2.8 bn across sectors and has delivered a gross internal rate of return of over 25% (in US\$ terms).

Key Investment Themes

Penetration of Private Equity is low – likely to rise in coming years

Indian Private Equity space is approximately 1% of GDP; Mature markets like the US and the UK have Private Equity to GDP ratio of 1.5%-2%. PE investment in US, for instance, was \$ 191 billion last year. This indicates the tremendous scope for growth, not just on account of the underlying GDP growth but also on account of catch-up to global levels.

Relative Performance Analysis



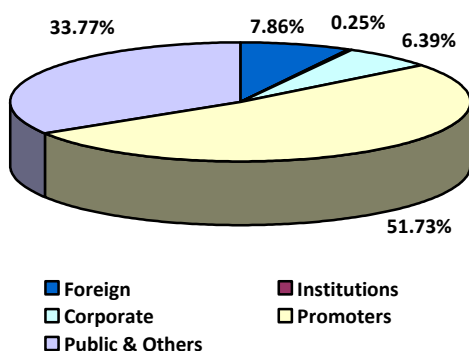
India - one of the most attractive Private Equity destinations

Strong economic growth leading to a majority of Indian companies looking for growth capital. Private Equity has fast emerged as an alternate source of funds for companies to support expansion plans. Large Global Private Equity investors are either setting up dedicated Indian funds or increasing allocations for Indian investments in their global portfolios. In 2007, India was the largest recipient of Private Equity capital in Asia, ahead of Australia (US\$ 14.6 bn), Japan (US\$ 14.4 bn) and China (US\$ 11.5 bn). About US\$ 3.3bn was invested in Jan-Mar 2008 and US\$ 17 bn invested in 2007. Fund sizes have increased from US\$ 25 - 100mn, to about US\$ 400 - 1,000mn. Increasing deal sizes: average investment size up from US\$ 4mn in 2000 to US\$ 50mn.

Unique business model - only listed player in its domain

The uniquely placed business model offers retail participation in an otherwise exclusive institutional domain. Thus allowing indirect exposure to growth potential of large unlisted companies. It also provides stable and predictable revenue stream (through annual management fees) with defined performance upsides. The company is better positioned to create upsides v/s managers of other asset classes as higher degree of value additions and relatively early stage of investment provides significant upside at exit. This is well supported by empirically documented advantages of Private Equity participation in the value unlocking from the unlisted companies at the maturity point of investment cycle.

Shareholding Pattern



Rebound in Private Equity – Better times ahead

After euphoric 2006 and 2007, 2008 and 2009 have mirrored global trends and turned difficult for Private Equity investments in India. However, we believe the worst of the cycle is behind us and we should see a recovery in second half of 2010. The logic of investing in scale and in locations of growth means that India will likely be at the forefront of a global PE recovery. The reduction in capital from overseas may be offset to an extent by the emergence of domestic investments from family and corporate accounts. Overall, a healthier trend will emerge where experienced managers like IIML will emerge stronger.

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Private Equity – An Introduction

Private equity funds are investment companies do not hold publicly traded securities

What are Private Equity Funds?

Private equity funds are investment companies that, as a rule, do not hold publicly traded securities. Instead, they normally seek equity stakes (that is, partial ownership) in private companies. They also may invest in so-called private placements of securities from public companies. That is, securities that are not offered to the general public or traded in the public securities markets.

Private Equity funds draw capital from wealthy individuals, pension funds and other investment managers

Many private equity funds are standalone operations that draw their investment pools from wealthy individuals, pension funds and other investment managers. Most are private companies themselves, but some have been publicly traded entities. Other private equity funds are subsidiaries or divisions of larger financial services firms.

Private Equity funds have much longer investment horizons and are highly illiquid.

Private equity funds tend to have much longer investment horizons than funds that hold publicly traded securities. There are several reasons for this. First, securities issued by private companies (as well as private placements from public companies) are highly illiquid, since they are not traded in public securities markets. Also, the opportunities for resale to another party are highly limited, with possible contractual and regulatory constraints adding to the difficulties. Second, some private equity funds tend to act as partners in managing the companies that they back, rather than being merely passive investors.

Private Equity provides capital in situations where traditional lenders lack the necessary expertise.

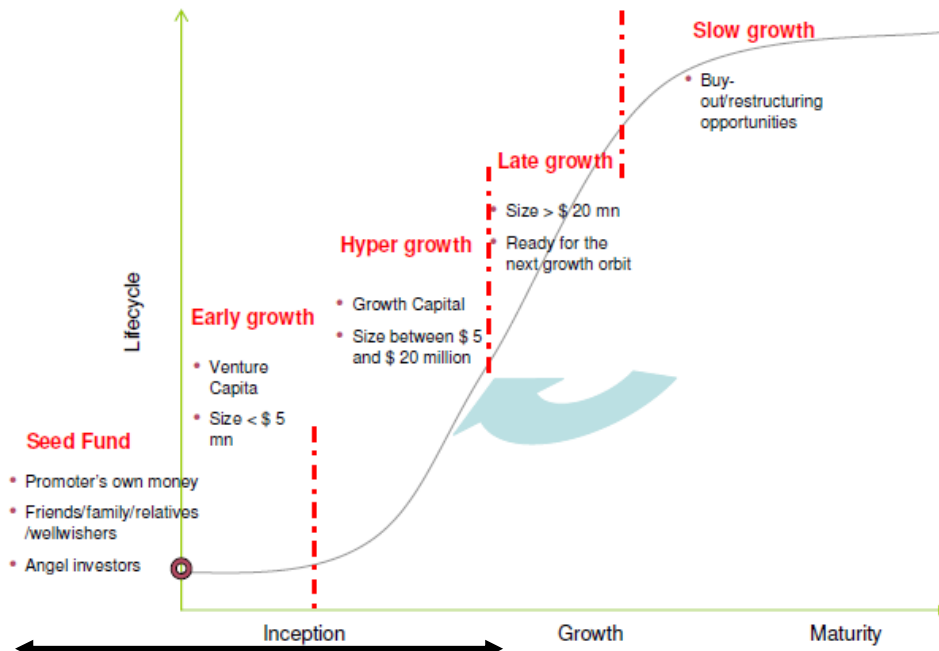
Private Equity investors, such as professional venture and buyout firms, institutional investors and high net worth individuals, can provide capital in situations where traditional lenders lack the necessary expertise. In these cases, private equity investors can be a valuable resource to these private companies, whether the companies are seeking to develop an initial business idea, expand a business or reconfigure it to become more profitable.

- Private equity investment avoids the cost associated with pursuing a public stock offering
- Private Equity securities are not regulated as stringently as are public securities

Stages of Private Equity funding

- Seed Financing: Providing small sums of capital necessary to develop a business idea.
- Start-up financing: Providing capital required for product development and initial marketing activities.
- First-stage: Financing the commercialization and production of products.
- Second-stage: Providing working capital funding and required financing for young firms during growth period.
- Third-stage: Financing the expansion of growth companies.
- Bridge financing: Last financing round prior to an initial public offering of a company.
- PIPE deals: A private investment in public equity, often called a PIPE deal, involves the selling of publicly traded common shares or some form of preferred stock or convertible security to private investors.
- Leveraged Buyout (LBO): It entails the purchase of a company by a small group of investors, especially buyout specialists, largely financed by debt.
- Management Buyout (MBO): It is a subset of LBO whereby incumbent management is included in the buying group and key executives perform an important role in the LBO transactions.

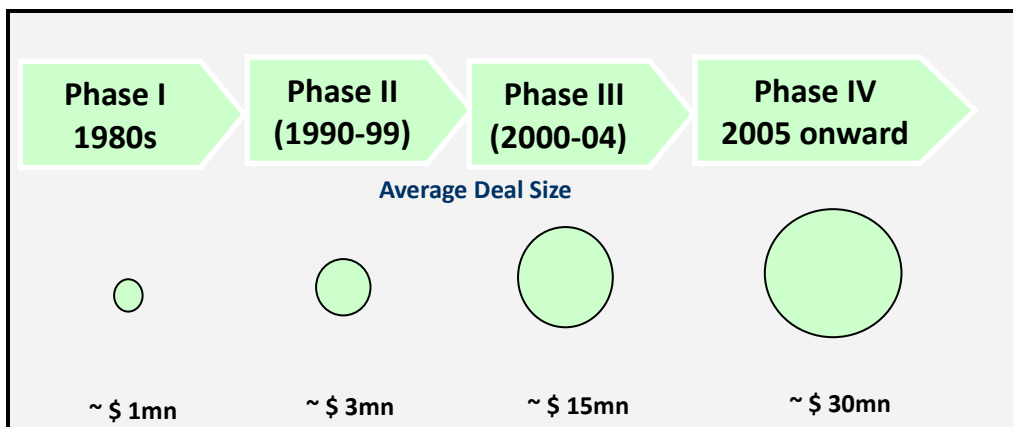
Typical life-cycle of a company and the role of Private Equity capital



Stages in a company's life-cycle where Private Equity investments are made

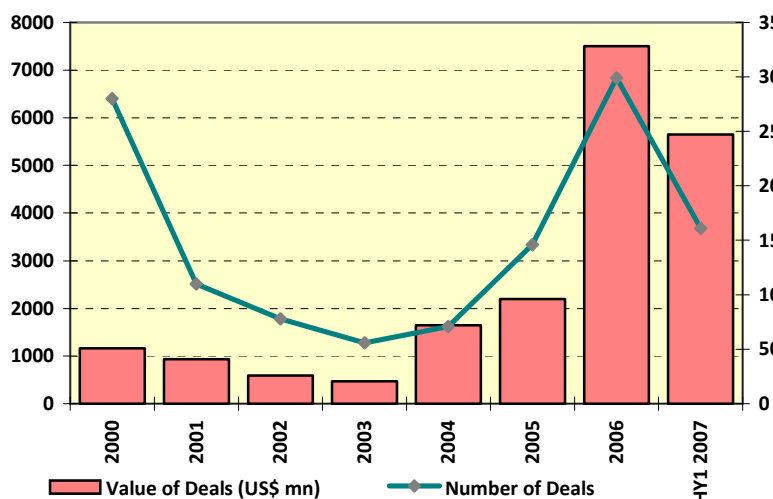
Indian Private Equity Scenario

Strong economic growth has led to a majority of Indian companies looking for capital to fund their business expansion. Initially the avenues for capital were limited to debt from banks and financial institutions and equity raised from capital markets. However, considering different needs of various owners, alternate sources of capital funding started in 1980s. One of the prominent of such sources was Private Equity. As a Private Equity fund can provide capital in situations where traditional lenders lack the necessary expertise, it quickly emerged as an alternate source of funds for companies to support expansion plans. The biggest recipient of Private Equity capital were young companies which had a brilliant business idea and a credible promoter or promoter group but lacked the deep pockets to get financial backing from a lending institution. As economy boomed in 21st century, many private equity funds started shop in India. Even today large global Private Equity investors are either setting up dedicated Indian funds or increasing allocations for Indian investments in their global portfolios.



Indian Private Equity progression in capital invested and average deal size amount

India - increasing attractiveness as a PE destination



Over years Private Equity capital invested in Indian companies has increased exponentially. In 2007, India was the largest recipient of Private Equity in Asia, ahead of Australia (US\$ 14.6 bn), Japan (US\$ 14.4 bn) and China (US\$ 11.5 bn). Capital from Private Equity funds to the tune of US\$ 3.3 bn invested in Jan-Mar 2008 and US\$ 17 bn was invested in Indian companies in 2007. Fund sizes have increased from US\$ 25 – 100 mn, to about US\$ 400 – 1,000 mn. Increasing deal sizes: average investment size up from US\$ 4 mn in 2000 to US\$ 50 mn

Private Equity investments are just 1% of the GDP, half that of the mature markets in US or UK

Huge scope for catch-up to global levels

Indian Private Equity investment is approximately 1% of GDP. Mature markets like the US and the UK have Private Equity to GDP ratio of nearly 2%. Private Equity investment in the US, for instance, was US\$191 billion last year. This indicates the tremendous scope for growth, not just on account of the underlying GDP growth but also on account of catch-up to global levels of Private Equity investments.

Projected to grow to US\$ 20 bn by 2012, from US\$ 1 bn in 2004. Achieved a peak of US\$ 11 bn in 2007

What lies ahead?

Indian Private Equity space has come a long way. Indian Private Equity industry is still relatively young. It was a minuscule segment of investment landscape up to and including 2004. What we've seen since then is an explosion, both in investment and in the number of funds operating in India. In 2007 a peak of US\$ 11bn was achieved in just about three years. From around a billion dollars in 2007; it is projected to grow to more than US\$ 20 bn by 2012.

Investments in infrastructure, logistics, pharmaceuticals to drive growth. Real Estate to also get a large pie

Cross sectoral investments opportunities are set to increase in the coming years. A third of investments in 2007 went into Real Estate. The slump in the Real Estate markets hit the Private Equity players hard. However, the long term drivers of the industry are intact and will continue to see good investments. Infrastructure is all set to capture a larger share of the investment pie. Robust levels in Banking, Financial services, Telecom, IT and manufacturing are already present.

Increasing opportunity for non-minority investments. Exit routes options also likely to be better in coming years

While minority investments dominate Private Equity activity today, there may be more opportunities for buyouts in the future. Traditionally, business owners have looked on selling a company as an admission of failure, but attitudes are changing. Rather than simply handing a business on to the next generation, one can expect to see more owners selling controlling stakes. Equally, in the case of those who own multiple businesses, there is more interest in selling selected units in order to focus on others. Therefore, we can expect the Private Equity model in India to evolve significantly over the next few years, as business owners become more aware of what funds can offer both in terms of growth capital and exit opportunities.

IL&FS Investment Managers

Started in 1989 as Credit Capital Venture Fund (India) Limited (CCVF), an affiliate of Lazard Brothers.

The origins of IL&FS Investment Managers Limited date back to 1989 when it was founded as Credit Capital Venture Fund (India) Limited (CCVF), an affiliate of Lazard Brothers. CCVF was the first private sector venture capital company in India, and managed a number of small sector focused funds apart from investing its own proprietary capital.

Acquired by Infrastructure Leasing & Financial Services Limited (IL&FS) in 1996 and renamed.

Infrastructure Leasing & Financial Services Limited (IL&FS) acquired CCVF in 1996, completed an intensive management and financial restructuring, merged its own private equity business into CCVF and renamed it IL&FS Investment Managers Limited (IIML).

In late 1990s, IIML became the first Fund Manager to establish an Infrastructure focused Private Equity Fund, with participation from large international investors (The AIG India Sectoral Equity Fund).

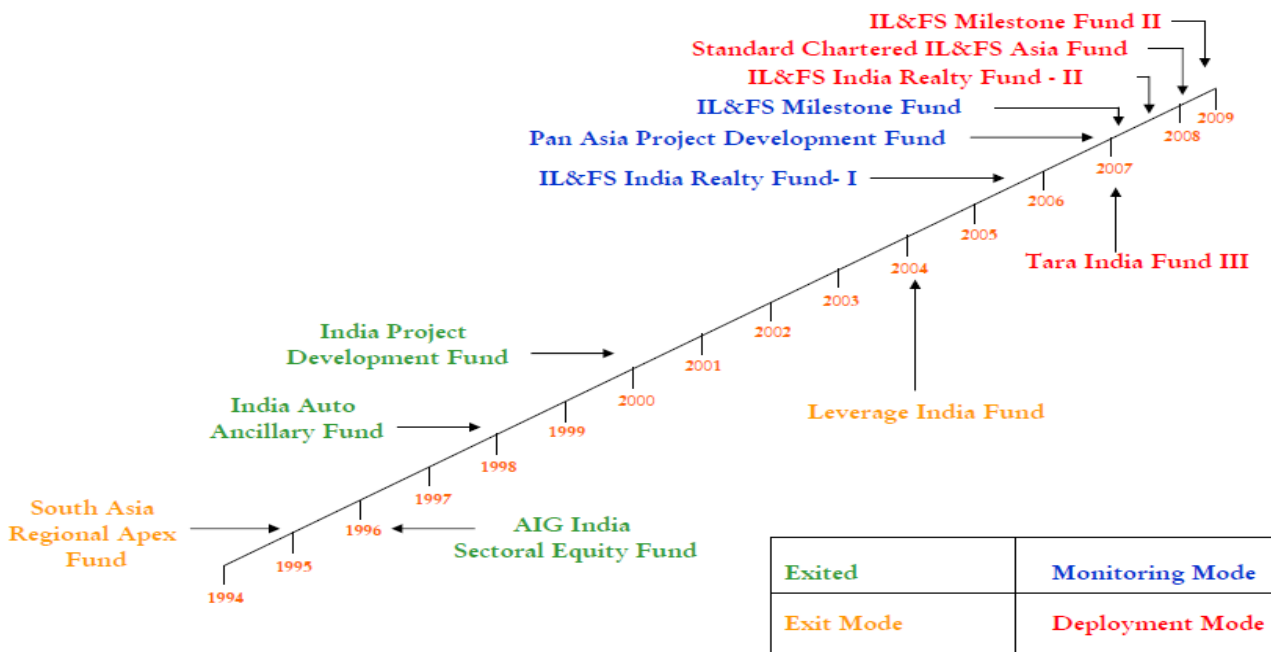
Set-up a dedicated infrastructure seed capital fund

In early 2000s, IIML recognized the need for specialized seed capital funding for project development activities relating to large format infrastructure project and was a pioneer in establishing a dedicated infrastructure seed capital fund (The India Project Development Fund).

By mid-2000s, as the country opened its doors to real estate investing, IIML moved quickly to establish one of the first and the largest real estate funds.

Three of its Funds were fully divested in 2007 - 08, providing attractive returns for their investors.

Three of the Funds - AIG India Sectoral Equity Fund (Vintage: 1996), India Project Development Fund (Vintage: 2000) and India Auto Ancillary Fund (Vintage: 1998) - were fully divested in 2007 - 2008, providing attractive returns for their investors. This experience across fund cycles is unique for any Indian Private Equity fund manager.



Timeline and stage in life cycle of various funds of IL&FS Investment Managers

Business Model

Unique business model offers an opportunity for retail participation in an otherwise exclusive institutional domain

IL&FS Investment Managers operates on a business model that is common to Private Equity Managers. However being the only listed company in its domain it offers a unique value proposition to investors. The uniquely placed business model offers an opportunity for retail participation in an otherwise exclusive institutional domain. It also offers to an investor an indirect exposure to growth potential of large unlisted companies.

The company has stable and predictable revenue stream. Better positioned to create upsides vs. managers of other asset classes

The company has stable and predictable revenue stream (through management fees) with defined performance upsides. The company is better positioned to create upsides vs. managers of other asset classes due to inherent benefits in the structure of investment made by the investors (this is discussed in detail in the section below on "Benefits of Private Equity Fund Management").

Private Equity participation in the value of unlisted companies leads to higher degree of value addition

It is also historically observed and documented that Private Equity participation in the value of unlisted companies leads to higher degree of value addition. The relatively early stage of investment in company's cycle provides significant upside at exit. This upside is captured through the "Carry" Structure (explained in the box below).

"Carry" is also referred to as the incentive fees. This is the percentage charged as an incentive fee on profits earned above the hurdle rate of the fund. What it amounts to is the percentage of the profit above a specified hurdle rate that goes to the fund managers. Given the potential for outsized gains in the Private Equity space the Carry is a necessary incentive for the fund manager to go for higher return on capital by going for deals which have a higher probability for gains.

Management fee for AUM is typically between 1.5% and 2% of AUM for the fund life

IL&FS Investment Managers charges management fee for Assets Under Management (AUM) which is typically between 1.5% and 2% of AUM for the fund life. This highly visible, annuity revenue stream over 6 - 10 years leads to higher predictability of revenue streams.

An embedded "Carry" structure leaves room for significant increase in revenue in form of performance upside through profit share (without risk of any downside). Hurdle rate for "Carry" generally ranges between 8% - 11% per annum. "Carry" is generally 20% of profits from investments above the hurdle rate. This leads to an upside component as Fund Size / Asset Under Management increases.

In a nutshell, the business model has the following features:

- Long-term fund investment horizon of 3-6 years
- Majority investments in unlisted companies
- Active investors with clear focus on value creation
- Mitigates risk of stock market volatility
- Provides predictable earnings in form of management fee
- Captures superior performance through "Carry" structure

Long term committed investors; predictable AUM and management fees. High investor fidelity with repeat investments in follow-up funds

Benefits of Private Equity Fund Management

A Private Equity fund has some intrinsic advantages which make it better placed than traditional mutual funds. A Private Equity fund has long term committed investors with a defined lock-in period which leads to a predictable asset under management (AUM). This allows more flexibility and surety to manage funds as there is no pressure of redemption before a specified date. The fund manager does not require managing NAV on day-to-day basis and can concentrate on growth of capital. This structure also leads to need to predictable fees earned on managing the fund. Another big advantage of this structure is high level of investor fidelity with the Private Equity fund manager, with investors generally making repeat investments in follow-on funds.

Proprietary deals result in entry at lower than market comparables

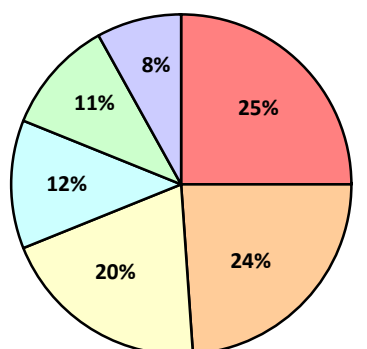
The entry price for investors in a company through proprietary deals result in entry at lower than market comparables (via Initial Public Offers (IPO) or in transactions through stock exchanges). This is because they forego the transaction costs involved in an Initial Public Offering or the costs associated with large market transactions. A Private Equity fund manager also exercises significant ability to guide investor companies and control outcomes as they bring with them expertise and skills in various domains.

Infrastructure growth is necessary if India is to achieve 10% GDP growth in coming years. This translates into US\$495 bn worth of investments in 2008-2013.

Emerging areas of opportunity in Private Equity Space

PE opportunity in Infrastructure

Infrastructure investments are set to rise from 4.5% to 8% of GDP by 2012. What make infrastructure a key area is that it is imperative for a sustained 8% GDP growth. It is also necessary if we are to achieve 10% GDP growth in coming years. Such growth rate can only be achieved if infrastructural bottle necks are removed. All this translates into \$495 bn worth of investments in 2008-2013. Already the sector has well entrenched private players in Roads, Telecom, Power, Ports and Airports. There are opportunities for Private Equity investments in Urban Infrastructure, Railways and pipelines.



■ Transportation ■ Ancillary
■ Infra Services ■ Telecom
■ Logistics ■ Power & Gas

Break-up of Infrastructure investments

Already key drivers for this humongous opportunity are in place. Investments were not permitted in areas like power distribution, airports, and railways etc. This is now history. Independent regulators add to investor comfort. Government driven integrated mega projects like NHDP and UMPP need funds. Some of it comes from Government contribution in form of viability gap funding, project specific cess etc. Rest is through debt, internal accruals of the company and equity funding. Private players are expected to invest over US\$ 200 bn in infrastructure projects in the coming years. The key features of this would be

- Cost efficient borrowing with sufficient depth possible
- Growing size of project executors of comfort to international lenders
- Change in attitude - Willingness to pay commercial user charges
- India growth story - Sheer demand turning hitherto unviable opportunities into doable business plans

IL&FS Investment Mangers was one of the early investors in Infra, Telecom, Roads, City Gas and Rail. The company has a Pan-Asia focus in its infrastructure dedicated funds. Its infrastructure dedicated funds have a total corpus of over US\$ 703 mn. Out of which US\$ 330 mn have already been invested in thirty-one transactions.

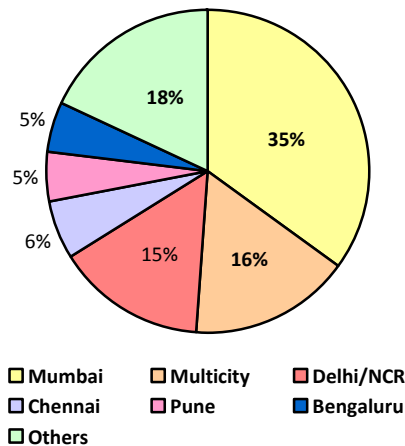
Opportunity in Real Estate

This was one of the most popular sectors for Private Equity investments before the economic turmoil. The fall in real estate prices and lack of demand in some areas led to steep price correction in the ensuing years. However, we remain optimistic on the long term structural story in this space. This growth is expected due to the following factors:

- Strong economic fundamentals
- Growing middle class; changing socio-economic trends
- Increasing demand for quality office space driven by IT and KPO companies
- Emergence of new investment vehicles: REIT, REMF

Opportunities in Real Estate exist in:

- Integrated Townships with a focus on mass and middle class housing
- Organized Retail with
- Adaptive re-use of industrial land and slum-rehabilitation in metro cities
- Special Economic Zones
- IT / ITeS / KPO/ LPO Sector



City-wise investments in Real Estate

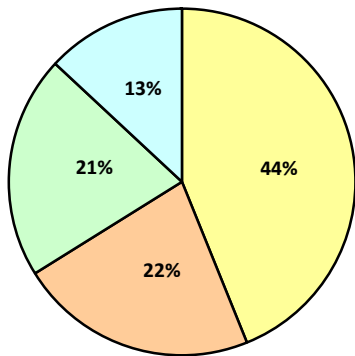
IL&FS Investment Mangers was the pioneer in India in the Real Estate vertical. The first Real Estate fund in India was launched in 2005-06 by IIML. Similarly the first yield fund in India was launched by IIML in 2007-08. The company has two active international funds under management with total fund size of nearly US\$ 1.4 bn. It also has two domestic funds for stabilized yield earning assets with total fund size of approximately US\$ 350 mn. The company has already invested US\$ 880 mn in 32 transactions.

Opportunities also exist in freight handling and forwarding, education, healthcare and pharmaceuticals, sustainable development and high-end technology. However these opportunities are still in a nascent stage and will come to a fruition in a coming few years.

As on the end of March 2010, IL&FS Investment Managers manages assets worth US\$ 2.8 bn. This Asset Under Management base yields recurring fee stream in form of a management fee. Management Fees are based on capital committed and have little sensitivity to market conditions, during the life of the fund. About 90% of Capital invested into the fund has an average contractual life of about seven years.

It is the only private equity player operating in India which has:

- Experience across sectors from IT, manufacturing, retail to real estate and infrastructure
- Has experience of exiting three funds and returning capital plus returns to investors
- The management team has experience straddling various funds and three economic cycles



■ Manufacturing ■ IT & ITeS
■ Consumer Services ■ Life Sciences
Sectoral distribution of Investments

It is also the oldest and the largest Private Equity player with experience across various sectors. In the Private Equity vertical IL&FS Investment Managers was the first investors in Retail, Shipyard and Media. It has three Private Equity funds, of which first fund is now fully divested, other two funds under active management / investment mode. The two funds under active management / investment mode aggregate to US\$ 378 mn, with US\$ 263 mn invested in thirty-five transactions.

IIML has a successful business model built assiduously over the last decade

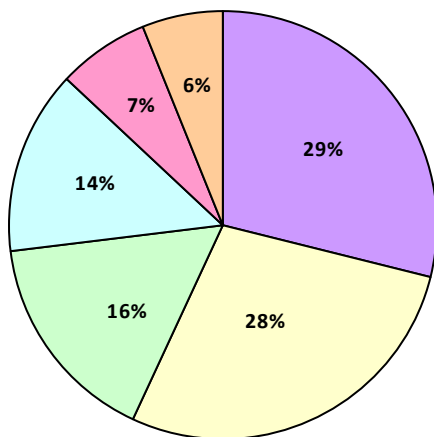
- It is a fund manager of repute in Indian and overseas markets
- A port of first call for investors in Private Equity space

IIML's business model can easily be replicated resulting in enhanced AUM / revenues through

- Larger follow on funds
- New emerging opportunities
- Extending Geographies

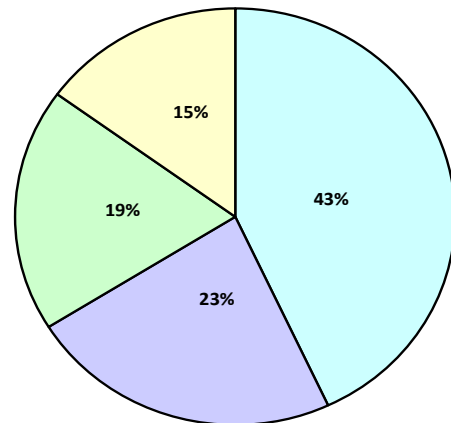
Substantial increase in activity levels on all counts in the next 2-4 years

- Enhanced Fund raising
- High level of investment deal flow
- More investments to reach liquidity / exit stage



■ Real Estate ■ Infrastructure ■ IT / ITeS
■ Manufacturing ■ Retail / Media ■ Life Sciences

Investments across sectors till date



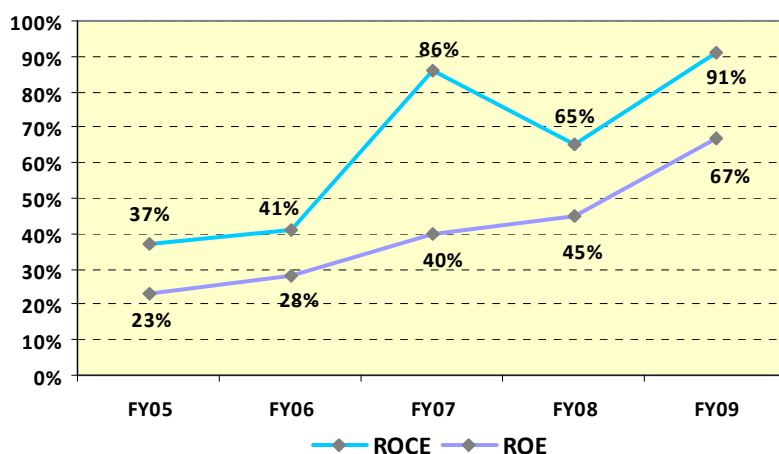
■ Listing / IPO ■ Strategic Sale
■ Buyback ■ Trade Sales

Mode of exit till date

Returns	IRR	Multiple	Investments
Realised / Liquid Investments	>25%	2.4x	52

Valuations

IL&FS Investment Mangers is the only player of its type to be listed in stock exchanges in India. The company has had a stellar record in terms of returns. As is well evidenced from the graph below the company has consistently had high ratios of Return on Capital Employed (RoCE). This indicates sound operational metrics of the business.



The company has also consistently delivered higher Return on Equity (RoE). As per our estimates the company is expected to post a 35% rise in income and a 45% rise in net profit (after exceptional items) in FY2011. The business outlook is optimistic as investors start looking afresh at emerging market economies after the financial crisis abates. The buoyancy in capital markets and pick-up in Mergers and Acquisitions also augurs well for the company in as it is likely to have more exit opportunities on its existing investments. We have

valued the stock using relative valuation methodology. The stock has historically traded in a price-earning ratio band of 10-20 except during the times of market panic when due to panic the price-earning ratio fell below 10. We have valued the stock at the average of its price-earning ratio trading band of 15. Our projection of an annual EPS for FY2011 of Rs.5.26 per share gives a price target of Rs.78.9, implying an upside of 78.30%.

Income Statement

Rs. Crores	FY11E	FY10	FY09	FY08	FY07
Net Sales	229.28	169.84	153.93	98.98	59.92
Other Operating Income	6.00	6.11	4.22	6.11	0.00
Other Income	5.70	5.39	6.00	0.89	0.63
Total Income	240.98	181.34	164.15	105.98	60.55
Total Expenditure	81.61	68.01	57.76	48.95	22.12
PBIDT	159.37	113.33	106.39	57.03	38.43
Interest	0.00	0.00	0.00	0.00	0.00
PBDT	159.37	113.33	106.39	57.03	38.43
Depreciation	21.16	17.63	21.80	10.20	10.75
Tax	30.41	21.36	20.58	14.30	9.69
Fringe Benefit Tax	0.00	0.00	0.47	0.45	0.28
Deferred Tax	0.50	0.18	1.21	(-0.11)	(-0.51)
Reported PAT	107.30	74.16	62.33	32.19	18.22
Minority Interest	0.60	0.31	0.14	0.23	0.01
Net Profit after Minority Interest	106.70	73.85	62.19	31.96	18.21
Extra-ordinary Items	0.00	0.00	0.00	0.00	0.00
Adjusted Profit after Extraordinary Items	106.70	73.85	62.19	31.96	18.21
EPS (Rs. Unit)	5.26	3.69	15.63	8.22	7.48
Face Value (Rs. Unit)	2	2	10	10	10
Equity	41.00	40.61	39.79	26.53	25.71

Source: Company, JVCS

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Risk Profile

Low Risk: Fundamentally sound companies, with low beta. Expected market out-performance is 0-10%

Medium Risk: Expected market out-performance is 10 - 20%. Preferably for the Investors with a maximum time frame of 12 months.

High Risk: High Beta Stocks, expected market out-performance is more than 20%, Preferably for the investors willing to take advantage of market momentum and are aggressive in nature.

Disclosure Appendix

Analyst ownership of the stock: No

I, Shaurya Priya, the writer of this research report hereby certify that no compensation/incentive was received from any agency/agencies for giving an investment recommendation on the company/companies mentioned herein. All views expressed in this research report correctly, factually and fully express my opinion and outlook on the company/companies mentioned herein.

Company ownership of the stock: No

Disclaimer Appendix

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