



Sharekhan top picks

In the September 2007 issue, we had recommended the best 12 of our Stock Ideas as Sharekhan Top Picks. As on October 1, 2007, the basket of stocks has given an absolute return of 13% as compared with a 12.4% appreciation in the Sensex and a 13.2% rise in the S&P CNX Nifty.

This month, we have made four changes in the portfolio. Due to continued strengthening of the rupee, we have replaced the tech stocks (both Infosys and HCL Tech) with

ITC and Wockhardt. In terms of churn within the sector, Bharat Bijlee has been replaced with Indo Tech Transformer and Axis Bank comes in place of HDFC Bank.

The price targets of Grasim Industries and Maruti Suzuki are under review and would be upgraded along with their Q2 result updates. We expect a strong Q2 performance from both these companies.

Name	CMP* (Rs)	PER			RoE (%)			Target price	Upside (%)
		FY07	FY08E	FY09E	FY07	FY08E	FY09E		
Axis Bank (UTI Bank)	750.5	32.1	30.5	23.2	20.9	13.7	12.8	960.0	27.9
Balaji Telefilms	270.2	22.1	18.0	14.8	28.6	28.6	28.0	303.0	12.2
Bharat Heavy Electricals	1,990.1	40.4	31.7	25.4	27.5	26.8	26.4	2,450.0	23.1
Bharti Airtel	942.3	41.9	28.1	22.3	29.1	33.0	32.0	1,100.0	16.7
Grasim	3,599.5	16.8	13.6	15.6	27.5	27.2	27.0	**	-
Hindustan Unilever#	222.4	31.8	26.2	23.2	56.5	57.4	52.0	280.0	25.9
Indo Tech Transformers	517.5	21.8	17.1	11.0	32.3	30.6	35.2	650.0	25.6
ITC	186.0	25.8	23.2	19.4	27.7	26.6	27.5	200.0	7.6
Jaiprakash Associates	1,146.3	56.5	37.5	32.8	16.1	15.5	15.3	1,350.0	17.8
Madras Cements	4,308.4	16.9	11.7	9.7	46.3	41.7	34.1	4,600.0	6.8
Maruti Suzuki	991.8	18.7	15.7	13.8	24.9	26.1	23.8	**	-
Wockhardt#	419.8	15.2	13.5	11.7	22.6	19.6	19.0	552.0	31.5

* CMP as on October 01, 2007

#December ending company

** Price under review

Name	CMP (Rs)	PER			RoE (%)			Target price	Upside (%)
		FY07	FY08E	FY09E	FY07	FY08E	FY09E		
Axis Bank (UTI Bank)	750.5	32.1	30.5	23.2	20.9	13.7	12.8	960.0	27.9

Remarks:

- Axis Bank is one of the fastest growing private sector banks, which has considerably improved its earnings quality and overall performance under the able Chairmanship of Mr Nayak.
- The bank's assets are expected to grow at a compounded annual growth rate (CAGR) of 36% over FY2007-09E. The growing assets along with stable to improving margins will lead to a strong growth in net interest income of the company during the period. The bank has a very robust fee income model in place.
- The bank has raised around Rs4,200 crore which would help it to maintain its growth momentum in the next three years.
- At the current market price, the stock is quoting at 23.2x FY2009E earnings per share (EPS), 10.3x FY2009E pre-provision profits and 2.8x FY2009E book value. We maintain our Buy recommendation on the stock with a twelve-month price target of Rs960.

Balaji Telefilms	270.2	22.1	18.0	14.8	28.6	28.6	28.0	303.0	12.2
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Remarks:

- The flurry of entertainment channels to be launched over the next couple of years would result in a huge opportunity for quality and leading content providers such as Balaji Telefilms.
- Balaji has an established presence in the general entertainment channel category and is among the top content provider for channels like Star, Zee and Sony for past few years. Its shows consistently figure in the top slots on the rating charts.
- Going forward, the joint venture with Star for launch of at least six regional entertainment channels would create substantial value for the shareholders. Balaji would produce ~530 hours of annual prime time content for each of these channels, thus scaling up its core content business.
- At current market price the stock quotes at 14.8x its FY2009 estimated earnings. Our sum-of-parts valuation gives us a target price of Rs303.

BHEL	1,990.1	40.4	31.7	25.4	27.5	26.8	26.4	2,450.0	23.1
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Remarks:

- Bharat Heavy Electricals Ltd (BHEL), a leading supplier of power equipment, will be the prime beneficiary of a four-fold increase in the investments (Rs500,000 crore in the 11th Five-Year Plan as against Rs112,000 crore in the 9th Five-Year Plan) being made in the power sector.
- BHEL's current order book of Rs62,400 crore, ie 3.6x its FY2007 revenue, provides high earnings visibility.
- The power ministry has proposed around five ultra mega power projects entailing a capacity addition of 20,000MW (4,000MWx5) with the combined turnkey value of at least Rs80,000 crore.
- BHEL's recent technology transfer agreement with Alstom for design and manufacture of large-sized (500MW+) super-critical boilers will enable it to bid for the ultra mega power projects. We expect BHEL to bag a fair share out of this huge Rs80,000-crore potential investment, which in turn will maintain the growth momentum in the company's order book.
- The stock trades at a PER of 25.4x its FY2009E earnings. BHEL's valuation looks attractive as compared with that of its peers, such as Siemens, ABB and Larsen and Toubro.

Bharti Airtel	942.3	41.9	28.1	22.3	29.1	33.0	32.0	1,100.0	16.7
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Remarks:

- Bharti Airtel, the largest wireless telephony service operator, is one of the key beneficiaries of the consumption boom in the country. It has reportedly added subscribers at a healthy CAGR of over 75% in the past three years and is expected to increase its subscriber base at a CAGR of over 35% over the next two years.
- The company's focus on introducing innovative services, cost control measures and growing economies of scale is resulting in an improvement in its margins, despite the continued pressure on the average revenue per unit (ARPU). Consequently, the earnings are estimated to grow at CAGR of over 46% over the three-year period FY2006-09.
- At the current market price the stock trades attractively at 28.1x FY2008 and 22.3x FY2009 earning estimates. The target price of Rs1,100 is based on multiple of 22x FY2009E earnings estimates plus Rs170 per share as the value of the tower company.

Name	CMP (Rs)	PER			RoE (%)			Target price	Upside (%)
		FY07	FY08E	FY09E	FY07	FY08E	FY09E		
Grasim	3,599.5	16.8	13.6	15.6	27.5	27.2	27.0	**	-

Remarks:

- ♦ Grasim Industries will be augmenting its capacity by 9.5MMT comprising two greenfield units of 4MMT each at Kotputli and Shambhupura, and a brownfield expansion of 1.5MMT. With the tight demand-supply situation expected to persist in FY2009, the incremental volumes will augur well for the company.
- ♦ With the outlook for the VSF business remaining positive, the incremental volumes coupled with a firm pricing scenario will provide stability for the company's business.
- ♦ These two factors coupled with the incremental profits from the UltraTech's business will boost the consolidated earnings of the company.

Hindustan Unilever#	222.4	31.8	26.2	23.2	56.5	57.4	52.0	280.0	25.9
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Remarks:

- ♦ HUL is India's largest fast moving consumer good (FMCG) company. The volume growth is picking up in FMCG sector and HUL is likely to be a key beneficiary.
- ♦ The company has regained the pricing power in all the product segments. We believe better pricing power and improved product mix will be the revenue drivers. The turn-around of loss-making businesses, cost-cutting initiatives and increased focus on its food business should help it to improve its profitability.
- ♦ At the current market price the stock is quoting at 23.2x its CY2008E EPS of Rs9.6. We maintain our Buy recommendation on the stock with a price target of Rs280.

Indo Tech Transformers	517.5	21.8	17.1	11.0	32.3	30.6	35.2	650.0	25.6
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Remarks:

- ♦ Transmission and distribution of power is all set to attract huge investments (Rs427,000 crore over the XIth Five-year Plan) owing to the need to develop a robust network for power distribution. Transformer making companies like Indo Tech Transformers are all set to benefit from the huge investments in the sector.
- ♦ Indo Tech Transformers, a niche player in the transformer manufacturing space, arguably has the best margins in the industry. The high margins due to operational efficiencies are fuelling the growth of the company.
- ♦ The company is expanding its manufacturing capacity to 7,450 MVA per annum to meet the rise in demand for transformers. It has an outstanding order book of Rs134 crore.
- ♦ The stock trades at a price/earnings ratio of 11x its FY2009E. We maintain Buy recommendation on the stock with price target of Rs650.

Name	CMP (Rs)	PER			RoE (%)			Target price	Upside (%)
		FY07	FY08E	FY09E	FY07	FY08E	FY09E		
ITC	186.0	25.8	23.2	19.4	27.7	26.6	27.5	200.0	7.6

- Remarks:**
- ♦ ITC has successfully channelised the strong cash flows generated from its cigarette business into the businesses of fast moving consumer goods (FMCG), hotels, paperboards and now e-Choupals .
 - ♦ Despite huge spending on brand building, product development and infrastructure creation, the loss in the non-cigarette FMCG businesses has remained stable. This indicates that the performance of the existing portfolio is improving.
 - ♦ The company has incurred huge capital expenditure (capex) in its various businesses without affecting its return on capital employed (ROCE), which is quite commendable. With a strong cash flow of Rs2,000 crore and a debt of only Rs200 crore, we believe the company has enough cash surplus to pump into new avenues of growth.
 - ♦ At the current market price, the stock is quoting at 19.4x its CY2008E EPS of Rs9.6. We maintain our Buy recommendation on the stock with a price target of Rs200.

Jaiprakash Associates	1,146.3	56.5	37.5	32.8	16.1	15.5	15.3	1,350.0	17.8
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- Remarks:**
- ♦ Jaiprakash is expanding its capacity by 15MMT over the next three years at the end of which it will emerge as one of the largest cement players in north India with a capacity of 22MMT.
 - ♦ The company is the largest private sector hydropower player and is currently sitting on a huge construction order book of Rs7,200 crore. Taking cognisance of the government's target of achieving 50,000MW in hydropower electricity by 2012, we expect the order book to maintain its current momentum.
 - ♦ The Taj Expressway project coupled with the company's real estate business (Taj Greens) will add value to the company's shareholders.
 - ♦ Thus the company's diversified businesses will provide the much-needed stability to the overall business in the wake of a downturn in the cement cycle.

Madras Cement	4,308.4	16.9	11.7	9.7	46.3	41.7	34.1	4,600.0	6.8
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- Remarks:**
- ♦ The company is incurring a capital expenditure of Rs1,474 crore to expand its capacity by 4MMT in the next one year. The 2MMT expansion at Jayantipuram (including a 1MMT grinding unit at Kolkata) will be commissioned by the third quarter of FY2008, whereas the remaining 2MMT capacity at Ariyalur including an additional 56MW wind power plant will be commissioned by the second quarter of FY2009.
 - ♦ The higher capacities will drive the volume growth of the company going forward whereas the improved pricing scenario will improve its profits. The captive power plants will help lower the power & fuel cost. The company will be able to save income tax in FY2009 to the extent of the accelerated depreciation available on wind power plants, which will positively increase the cash flows of the company. At the current market price of the stock is trading at a valuation of 9.7x its FY2009 earnings.

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Name	CMP (Rs)	PER			RoE (%)			Target price	Upside (%)
		FY07	FY08E	FY09E	FY07	FY08E	FY09E		
Maruti Suzuki	991.8	18.7	15.7	13.8	24.9	26.1	23.8	**	-

Remarks:

- ♦ Maruti Suzuki, the market leader in the passenger car market in India, is set to benefit from the number of new launches made by it in the recent times.
- ♦ Most of its new launches, namely WagonR Duo, Zen Estilo, Diesel Swift and SX4, have been well received by the market and are clocking strong volumes. Also, with the addition of the diesel vehicle and a sedan, the company has expanded its product basket, making it a full-fledged play on the country's booming passenger car market.
- ♦ With the expansion of its Manesar plant, its exports are also set to go on a top gear. Suzuki has identified India as a hub for manufacture of small cars for its worldwide markets and the company would be exporting about 100,000 units of the new vehicle to its parent, while another 50,000 units would be supplied to Nissan.
- ♦ At current levels, the stock is trading at 13.8x its FY2009E and is available at an EV/EBIDTA of 8x. We maintain our Buy recommendation with a price target under review.

Wockhardt#	419.8	15.2	13.5	11.7	22.6	19.6	19.0	552.0	31.5
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Remarks:

- ♦ Wockhardt is an integrated, diversified pharmaceutical company having presence in formulations, generics and bio-pharmaceuticals. The company's operations are spread across the globe.
- ♦ The company has a successful history of turning around and creating value for its acquisitions. Hence, it is all set to reap the benefits from its recently acquired Pinewood Laboratories, an Ireland based generic company, and France-based Negma Laboratories.
- ♦ We expect its US business to grow at a fast pace going forward, led by the new launches made in the latter part of 2006 and 26 new abbreviated new drug application filings.
- ♦ The approval of Wosulin in various export markets would give a huge boost to its bio-pharmaceutical business.
- ♦ At current levels, the stock is available at 13.5x its CY2007E and 11.7x its CY2008E earnings. The valuations seem very attractive at these levels and should be viewed as a strong buying opportunity.

The author doesn't hold any investment in any of the companies mentioned in the article.

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