investor's eye

Index

Take Five

Scrip	Reco Date	Reco Price	CMP	Target
Deepak Fertiliser	17-Mar-05	51	**86**	126
HCL Tech	30-Dec-03	103	**337**	395
JP Associates	30-Dec-03	125	**614**	850
Madras Cement	17-Nov-05	1,498	**2,807**	4,000
Tata Elxsi	14-Dec-06	232	**320**	385

Cipla

Cannonball

Stock Update

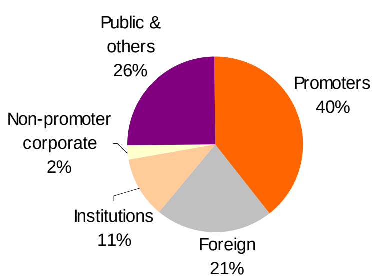
Price target revised to Rs256

Buy; CMP: Rs215

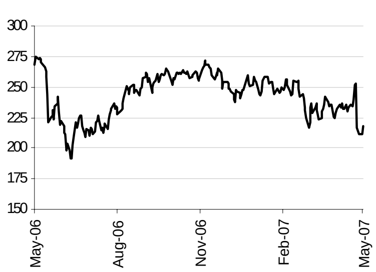
Company details

Price target:	Rs256
Market cap:	Rs16,673 cr
52 week high/low:	Rs280/180
NSE volume: (No of shares)	2.8 lakh
BSE code:	500087
NSE code:	CIPLA
Sharekhan code:	CIPLA
Free float: (No of shares)	47.1 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-5.1	-12.9	-15.0	-18.4
Relative to Sensex	-13.0	-10.2	-20.3	-28.9

Result highlights

- Cipla reported lower than expected results for Q4FY2007 with a net profit of Rs125.7 crore against the expectation of Rs199.6 crore. The earnings have been lower due to the disappointing exports of active pharmaceutical ingredients (APIs) and significant contraction in the operating profit margin (OPM).
- The revenues were marginally higher by 6.3% to Rs938.5 crore. The sales growth was lower due to a 27% decline in the API exports to Rs141.46 crore.
- The OPM witnessed a 590-basis-point decline to 15.7% in the quarter due to the higher contribution of low-margin anti-retrovirals and lower API sales to the regulated markets. Consequently, the operating profit stood at Rs147.0 crore, down by 22.8%. With the 40% fall in other income and the higher tax incidence (up from 4.0% to 11.3%), the net profit declined by 40.3% in the net profit to Rs125.7 crore.
- The FY2007 numbers saw a 19% growth in the top line at Rs3,438.1 crore, the margins remained almost flat at 20% and resulted in a mere 9% rise in the net profit to Rs660.8 crore.
- Cipla reported disappointing numbers for both Q4FY2007 and FY2007, largely due to the lower than expected performance of the export business and the decline in the OPM. Hence, we are revising down our FY2008 earning estimate by 17.4%; we are also introducing our FY2009 estimate. As per our revised estimate, the earnings per share (EPS) estimates for FY2008 and FY2009 stand at Rs10.9 and Rs12.8 respectively.

Result table Rs (cr)

Particulars	Q4FY06	Q4FY07	% yoy chng	FY2006	FY2007	% yoy chng
Net sales	882.6	938.5	6.3	2891.4	3438.1	18.9
Total expenditure	692.2	791.5	14.3	2306.1	2749.4	19.2
Material cost	431.3	497.5	15.4	1411.6	1728.0	22.4
Staff cost	42.6	43.3	1.8	150.8	184.3	22.2
Other expenditure	218.4	250.7	14.8	743.7	837.1	12.6
Operating profit	190.4	147.0	-22.8	585.3	688.7	17.7
% OPM	21.6	15.7	-27.4	20.2	20.0	-1.0
Other income	36.7	22.1	-39.9	216.2	223.2	3.2
EBIDTA	227.1	169.1	-25.5	801.4	911.9	13.8
% EBITDA margin	25.7	18.0	-30.0	27.7	26.5	-4.3
Interest	3.3	1.3	-60.8	11.4	7.0	-39.1
Depreciation	25.0	26.1	4.3	80.2	104.1	29.8
PBT	198.8	141.7	-28.7	709.8	800.8	12.8
Taxes	8.0	16.0	99.4	102.2	140.0	37.0
PAT (after extraordinary)	210.5	125.7	-40.3	607.6	660.8	8.8
% PAT margin	23.8	13.4	-43.8	21.0	19.2	-8.5

- At the current price of Rs215, the stock trades at 19.7x and 16.7x of its FY2008 and FY2009 earnings respectively. Though, we have toned down our estimate, positive earnings surprises for the company at frequent intervals from exports are not ruled out. We maintain our Buy recommendation on the stock with a revised price target of Rs256 (ie 20x of FY2009E EPS of Rs12.8).

Disappointing API exports affect performance

Cipla reported a marginal revenue growth of 6.3% to Rs938.5 crore in Q4CY2007, which was lower than our expectations of Rs961.7 crore. The sales growth was lower basically due to a 27% decline in the API exports to Rs141.46 crore. The API exports were higher in the corresponding previous quarter on account of higher sales of Sertraline to Teva.

Seeing the disappointing API exports and considering the lumpy business cycle in the API business, we have reduced our API export estimate for FY2008, modeling a marginal 5% compounded annual growth rate (CAGR) for FY2007-09.

Formulation export growth moderated

Cipla maintained its steady growth momentum for formulation exports by reporting a 16.8% growth to Rs387.87 crore in Q4FY20007. However, the growth in the formulation business was moderated during the quarter.

Going forward, we believe the supply pact with US and European generic players for about 160 products, the increasing momentum in the anti-retroviral business and the anticipated approval as well as ramp-up in the export of CFC-free inhalers to Europe would catalyse Cipla's formulation growth. We estimate a 27% CAGR for formulation exports during FY2007-09.

In fact, Cipla has one of the strongest pipelines of 160 generic products (comprising plain generics, patent challenges and first-to-file products) for regulated markets, to be marketed through its allied partners. These products are at various stages of development. On the anti-retroviral business front, the up-coming tenders worth $600 million in the South African market may provide a big opportunity to Cipla, given its lowest cost manufacturing capability for anti-retrovirals.

Domestic formulation business maintains steady growth

The domestic formulation business reported a 14.4% growth to Rs399.70 crore, which was slightly better than the industry growth of about 10%. We believe the company would continue to deliver better than industry growth on the back of regular introduction of products and increased penetration into the rural markets. We expect a 15% and 13% growth for FY2008 and FY2009 respectively.

Revenue break-up

Sales break-up (Rs cr)	Q4 FY06	Q4 FY07	% growth	FY06	FY07	% growth
Domestic	349.5	399.7	14.4	1506.0	1752.3	16.4
% of total sales	*39.9*	*43.0*		*49.9*	*49.6*	
Exports	526.6	529.3	0.5	1513.6	1780.7	17.6
% of total sales	*60.1*	*57.0*		*50.1*	*50.4*	
Formulation exports	332.0	387.9	16.8	1029.8	1297.8	26.0
% of total sales	*37.9*	*41.7*		*34.1*	*36.7*	
API exports	194.6	141.5	-27.3	483.8	482.9	-0.2
% of total sales	*22.2*	*15.2*		*16.0*	*13.7*	
Total sales	876.2	929.1	6.0	3019.7	3533.0	17.0

OPM falls by 590bps to 15.7%

Cipla's OPM witnessed a 590-basis-point decline to 15.7% in the quarter. The contraction in the margin was due to a change in the product mix (higher volume of anti-retrovirals where the margins are low) and lower API sales to the regulated markets. Also, a higher other expenditure due to higher factory overhead, selling expenses, professional fees etc affected the margins. Consequently, the operating profit stood at Rs147.0 crore, down by 22.8%.

The increasing proportion of the low-margin anti-retrovirals in Cipla's revenue mix is a cause for concern, but the likely ramp-up in the formulation exports to regulated market and CFC-free inhalers would drive some expansion in the OPM going forward. However, the margin expansion will not be as high as our earlier estimate of 24.5% in FY2008. We are now revising down our OPM estimates to 21.5% and 22% for FY2008 and FY2009 respectively.

Net profit slips by 40%

With the other income declining by 40%, depreciation higher by 4.3% and the tax incidence up from 4.0% to 11.3%, Cipla's net profit declined by 40.3% to Rs125.7 crore.

FY2007 performance remained lacklustre

In FY2007, the company reported an 18.9% growth in sales to Rs3,438.1 crore, as API exports remained flat. Otherwise, formulation exports and domestic formulation sales grew by 26% and 16.4% respectively. Due to a change in the product mix, the OPM slipped by 20 basis points to 20%, resulting in an 8.5% decline in the bottom line.

Revise down FY2008 estimate and introduce FY2009 numbers

Cipla reported disappointing numbers for both Q4FY2007 and FY2007, largely due to the lower than expected performance of the export business and the decline in the OPM. Hence, we are revising down our FY2008 earning estimate by 17.4%. We are also introducing our FY2009 estimate. As per our revised estimates, the EPS for FY2008 and FY2009 stands at Rs10.9 and Rs12.8 per share respectively.

Valuation & view

At the current price of Rs215, the stock trades at 19.7x and 16.7x of its FY2008E and FY2009E earnings respectively. Though, we have toned down our estimates, positive earnings surprises for the company at frequent intervals from the export front are not ruled out. We maintain our Buy recommendation on the stock with a revised price target of Rs256 (ie 20x of FY2009 EPS estimate of Rs12.8).

Valuation table Rs (cr)

Particulars	FY05	FY06	FY07	FY08E	FY09E
Net sales	2181.3	2891.4	3438.1	4100.5	4795.5
Net profit	411.9	692.4	660.8	847.2	998.0
Shares in issue (cr)	77.7	77.7	77.7	77.7	77.7
EPS (Rs)	5.3	8.9	8.5	10.9	12.8
PER (x)	40.5	24.1	25.2	19.7	16.7

WS Industries India

Vulture's Pick

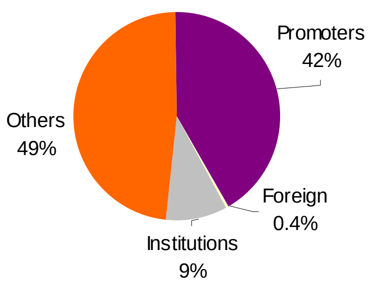
Stock Update

No surprises

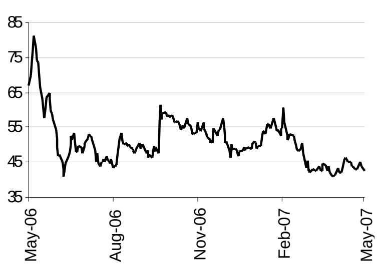
Buy; CMP: Rs43

Company details	
Price target:	Rs87
Market cap:	Rs91 cr
52 week high/low:	Rs85/39
BSE volume: (No of shares)	64,293
BSE code:	504220
Sharekhan code:	WSIND
Free float: (No of shares)	1.2 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	5.5	-19.5	-18.0	-27.8
Relative to Sensex	-3.2	-17.0	-23.0	-37.1

Result highlights

- WS Industries' (WSI) Q4FY2007 results are in line with our expectations.
- The revenues for the quarter grew by 16% to Rs44.8 crore while the net profit grew by 113% to Rs2.2 crore on the back of its high operating leverage and lower depreciation expense.
- The operating profit for the quarter grew by 37% yoy to Rs5.3 crore as the operating profit margin (OPM) expanded by 180 basis points to 11.9%. The OPM expanded because of lower power & fuel cost and other operational efficiencies. The power & fuel cost as a percentage of sales declined to 15.5% from 18.4% in Q4FY2006 and the other expenses, as a percentage of sales, dropped to 17.4% from 19.4% in Q4FY2006.
- The interest cost increased by 25.7% while the depreciation cost decreased by 10.6%.
- The order book at the end of March 2007 stood at a healthy Rs200 crore.
- The Q4FY2007 results of WSI are in line with our estimates; the company is having a good order book of Rs200 crore, which is around 1.2x its FY2007 sales and provides good earnings visibility. We have valued WSI using the sum-of-the part (SOTP) valuation method, wherein we have valued WSI's core insulators business at 10x its FY2008E earnings per share (EPS). This gives the fair value Rs58 per share. Further, we have valued WSI's realty subsidiary at the current realisable value of Rs3,500 per square feet. Taking WSI's current 59% stake in the realty venture, we arrive at a value of Rs29 per share. This gives us a fair value of Rs87 per share of WSI.

Result table Rs (cr)

Particulars	Q4FY07	Q4FY06	% yoy chg	FY07	FY06	% yoy chg
Net sales	44.8	38.6	16.1	165.4	147.1	12.5
Total expenditure	39.5	34.7	13.7	145.6	132.2	10.2
Operating profit	**5.3**	**3.9**	**36.9**	**19.8**	**14.9**	**32.9**
Other income	0.1	0.0	1193.3	0.4	0.2	84.2
EBIDTA	**5.4**	**3.9**	**39.1**	**20.1**	**15.1**	**33.5**
Interest	1.8	1.4	25.7	7.1	6.4	11.5
Depreciation	0.8	0.9	-10.6	3.7	3.3	11.1
PBT	**2.8**	**1.6**	**81.0**	**9.3**	**5.4**	**73.3**
Tax	0.6	0.5	16.0	1.5	1.1	36.1
PAT	**2.2**	**1.0**	**113.3**	**7.9**	**4.3**	**82.6**
Extraordinary items	0.0	0.0	-	0.0	0.0	-
Reported PAT	**2.2**	**1.0**	**113.3**	**7.9**	**4.3**	**82.6**
EPS	1.1	0.5	113.3	3.7	2.0	82.6
Margins						
OPM (%)	11.9	10.1		12.0	10.1	
PATM (%)	5.0	2.7		4.8	2.9	

Net sales up by 16%, operating profit up by 37%

WSI's revenue for the quarter grew by 16% to Rs44.8 crore while its operating profit for the quarter grew by 37% year on year (yoy) to Rs5.4 crore as the OPM expanded by 180 basis points to 11.9%. The OPM expanded because of lower power & fuel cost and other operational efficiencies. The power & fuel cost as a percentage of sales declined to 15.5% from 18.4% in Q4FY2006 and the other expenses as a percentage of sales declined to 17.4% from 19.4% in Q4FY2006.

Net earnings up by 113%

Helped by a lower depreciation cost and the improvement in the OPM, the net profit at Rs2.2 crore grew by 113% yoy.

Strong order book position

The company has a strong order book position of Rs200 crore, which includes an order book of around Rs170 crore for its insulator business and that of Rs30 crore for the project business. Going forward, the strong investment pipeline in the transmission and distribution sector will drive the order book of WSI. The company has expanded the capacity at its existing Chennai location. It is also setting up a new greenfield hollow core insulator plant and focusing on the development of its 15-lakh-square-feet information technology park, the first phase of which project is expected to commence in October FY2007.

Setting up greenfield plant for hollow core insulators

The company has been working at around its full capacity and the management believes further expansion at the current location at Porur in Chennai would not yield great results because it is within the city limits and the company has to bear high overheads on account of a high power & fuel cost as well as labour and transportation. Thus in order to overcome the problem of capacity constraint and also to sort out its power and fuel cost problem, WSI has decided to set up a greenfield porcelain insulator plant. This plant will have a capacity of 8,000 tonne, which will double its current capacity. This plant will largely manufacture high-margin hollow core insulators. The plant is expected to get operational by March 2008. On a fully operation basis, this plant is expected to generate around Rs120-130 crore of revenues.

The company has finalised the land for this facility, which will be based in Andhra Pradesh Special Economic Zone (SEZ). The provision of natural gas will reduce the new plant's power and fuel cost substantially. Also, given the location of the proposed plant in an SEZ, WSI will have access to port facility whereby it will be able to exploit the tremendous growth opportunity presented by the lucrative export markets. By virtue of the new plant's location in an SEZ, the company would also enjoy some fiscal benefits.

Valuation and view

We have valued WSI using the SOTP method, wherein we have valued its core insulator business at 10x its FY2008E EPS. This gives the fair value of Rs58 per share. Further, we have valued WSI's realty subsidiary at the current realisable value of Rs3,500 per square feet. Taking WSI's current 59% stake in the realty venture, we arrive at a value of Rs29 per share. This gives us a fair value of Rs87 per share of WSI. We maintain our Buy recommendation on the stock with a price target of Rs87.

WSI: SOTP price target is Rs87

Value of realty venture	
Total area	300000
Rate / sq ft	3500
Realisable value Rs crore	105
WSI stake in the realty venture	59%
Value attributable to WSI	62
Equity	2.12
Fair value	**29.1**
Value of core business	
PER	10
EPS	5.8
Value	57.7
Total value	**87**

Key financials

Particulars	FY04	FY05	FY06	FY07	FY08E
Net sales (Rs cr)	103.7	120.0	147.1	165.4	200.5
Net profit (Rs cr)	5.5	2.1	4.3	7.9	12.2
Shares in issue (cr)	2.1	2.1	1.8	1.8	1.8
EPS (Rs)	3.1	1.2	2.4	3.7	5.8
% yoy growth	*2.6*	*-61.6*	*104.3*	*82.6*	*55.5*
PER (x)	17.7	46.0	22.5	14.5	9.4
Book value (Rs)	19.3	20.3	22.6	33.1	38.9
P/BV (Rs)	2.8	2.7	2.4	1.6	1.4
EV/EBIDTA (x)	9.9	10.9	9.4	7.9	8.5
RoCE (%)	14.4	10.1	13.0	15.4	13.5
RoNW (%)	15.9	5.8	10.6	11.2	14.9

Corporation Bank

Apple Green

Stock Update

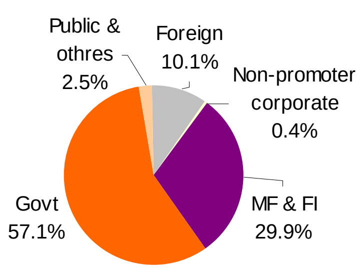
Numbers in line with expectations

Buy; CMP: Rs317

Company details

Price target:	Rs374
Market cap:	Rs4,547 cr
52 week high/low:	Rs445/206
NSE volume: (No of shares)	72,775
BSE code:	532179
NSE code:	CORPBANK
Sharekhan code:	CORPBANK
Free float: (No of shares)	2.4 cr

Shareholding pattern



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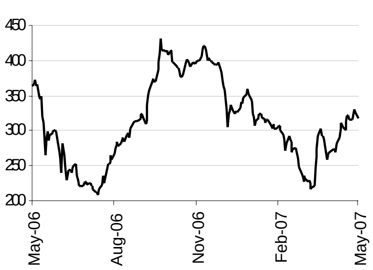


Price performance

(%)	1m	3m	6m	12m
Absolute	23.8	9.0	-16.8	-11.9
Relative to Sensex	13.5	12.4	-21.9	-23.2

Result highlights

- Corporation Bank's results are in line with our expectations; the profit after tax (PAT) grew by 18.2% year on year (yoy) but declined 19.1% quarter on quarter (qoq) to Rs118.5 crore compared with our estimate of Rs116.1crore.
- Adjusted net interest income (NII) was up by 31.2% yoy and 16.1% qoq to Rs387 crore. A moderate loan growth and significant increase in float balances helped the bank to improve its margins by 25 basis points to 3.06% on a sequential basis.
- The non-interest income increased by 14.4% yoy and 13% qoq to Rs180 crore. The core fee income was up 15.9% yoy and 5% qoq.
- With the net income up 25.4% yoy and the operating expenses up only 11.3% yoy, the operating profit was up by 36.4% yoy to Rs345.3 crore. The core operating profit (operating profit less treasury and recovery income) showed a good growth of 36.2% yoy and 29.2% qoq.
- Provisions and contingencies grew by 55.5% yoy and 103.7% qoq due to higher non-performing assets (NPA) and standard asset provisioning during the quarter. The significant increase in the provisions on a sequential basis resulted in a 19.1% sequential decline in the PAT although the operating profit grew by 17.8% qoq.
- The asset quality of the bank continues to be healthy with stable gross NPA at Rs624 crore and the net NPA at 0.47% in percentage terms. The capital adequacy ratio (CAR) remains at a comfortable 12.7% with Tier-I CAR at 11.3%.
- At the current market price of Rs317, the stock is quoting at 7.4x its FY2008E earnings per share (EPS), 3.4x pre-provision profit (PPP) and 1.1x book value. We maintain our Buy call on the stock with a price target of Rs374.

Result table Rs (cr)

Particulars	Q4FY07	Q4FY06	% yoy chng	% qoq chng	FY07	FY06	% yoy chng
Net interest income*	387.0	294.9	31.2	16.1	1377.8	1226.8	12.3
Non-interest income	180.0	157.4	14.4	13.0	639.87	571.46	12.0
Treasury	12.2	12.3	-0.5	-69.5	126.42	135.75	-6.9
Fee income	43.8	37.8	15.9	5.0	163.7	138.5	18.2
Net income	567.1	452.3	25.4	15.1	2017.7	1798.3	12.2
Operating expenses	221.7	199.2	11.3	11.1	803.59	746.75	7.6
Operating profit	345.3	253.2	36.4	17.8	1214.1	1051.5	15.5
Core operating profit (excluding treasury & recovery)	293.4	215.5	36.2	29.2	1087.7	915.77	18.8
Provisions & Contingencies	169.4	108.9	55.5	103.7	397.49	377.02	5.4
PBT	191.9	160.2	19.8	-8.6	816.58	674.5	21.1
Provision for taxes	73.5	60.0	22.5	15.8	280.44	230.04	21.9
Net profit	118.5	100.3	18.2	-19.1	536.14	444.46	20.6

*Adjusted for Rs16 crore of CRR interest income in Q4FY2007 and Rs16 crore of interest on income tax refund in Q4FY2006

NII driven by asset growth and sequential NIM expansion

During the quarter the bank's NII grew by 31.2% yoy and 16.1% qoq to Rs387 crore. The 31.2% year-on-year (y-o-y) growth in the NII was driven mainly by a 30.2% growth in the balance sheet size. However the 16.1% sequential growth in the NII was driven by an 8.5% sequential asset growth and a 25-basis-point improvement in the NIM to 3.06%. The bank's cost of funds declined by 11 basis points to 4.56% on a sequential basis, which is a deviation from the trend we have seen so far.

Yield analysis (%) table

Particulars	Q4FY2007	Q4FY2006	Q3FY07
Yield on funds	7.62	7.06	7.48
Cost of funds	4.56	4.04	4.67
NIM	3.06	3.02	2.81

Source: Company, Sharekhan Research, all figures are calculated based on average closing quarterly balances

Significant increase in float funds helped to decrease costs and improve margins

The current account deposits of the bank increased by 37.9% qoq compared to total deposit growth rate of 6.8% qoq. This helped in improving the low cost deposit base by 310 basis points on a sequential basis. This appears to be the primary reason for such a decline in the cost of funds, contrary to the industry trend. The savings account balances grew by only 3.7% qoq, hence in all likelihood this improvement is a one-quarter phenomenon and margin pressure could resurface in the coming quarters in the absence of such high float balances.

Particulars	Q4 FY07	Q4 FY06	yoy chng	qoq chng
Current account deposits	6777.33	4746.5	42.8	37.9
Savings account deposits	7651.79	6539.6	17.0	3.7
Total demand deposit	14429.12	11286.1	27.8	17.4
As a % of total deposits	34.1	34.0	-30 bps	310 bps
Term deposits	27927.8	21590.4	29.4	2.1
Total deposits	42356.89	32876.5	28.8	6.8

Moderation in loan growth has also helped the margins

Unlike in Q3FY2007 when we witnessed a 30.7% y-o-y credit growth funded largely by term deposits, the bank has concentrated more on yield management during the quarter and has grown its advance book cautiously by 25% yoy and 3.8% qoq, in line with the industry. This has also helped the bank in protecting its margins, as incremental term deposits have not added to the cost of funds significantly as witnessed in the previous quarter.

Core non-interest income shows improvement

The non-interest income increased by 14.4% yoy and 13% qoq to Rs180 crore, the fee income was up by 15.9% yoy and 5% qoq. The other income excluding treasury and recovery grew by 37.3% qoq, driven by fee, foreign exchange and other incomes.

Non-interest income (Rs crore)	Q4 FY07	Q4 FY06	% yoy chng	% qoq chng
Treasury	12.2	12.3	-0.5	-69.5
Fee income	43.8	37.8	15.9	5.0
Recovery of bad debts	39.7	25.4	56.5	53.2
Forex	26.2	6.4	309.4	536.9
Other income, dividend	58.0	75.5	-23.1	22.3
Other Income (excluding treasury & recovery)	128.1	119.8	7.0	37.3
Total	180.0	157.4	14.4	13.0

Source: Company, Sharekhan Research

Provisions and contingencies show significant increase

Provisions have increased by 55.5% yoy and 103.7% qoq driven by higher NPA and standard assets provisions coupled with higher investment depreciation.

Particulars (Rs crore)	Q4FY2007	Q4FY2006
Amortisation	18.1	24.4
Investment depreciation	52.9	30.5
NPA & stand. assets	97.1	54.0
Others	1.3	0.1
Total	169.4	108.9

Source: Company, Sharekhan Research

Asset quality continues to remain healthy

The asset quality of the bank continues to be healthy with the net NPA in percentage terms remaining stable at 0.47% on a sequential basis and the gross NPA staying stable at Rs625 crore.

CAR to decline after Basel II implementation

The bank's CAR remains at a comfortable 12.7% with the Tier-I CAR at 11.3%. However with the Basel II implementation, its CAR is expected to reduce by 100 basis points.

Valuation and view

At the current market price of Rs317, the stock is quoting at 7.4x its FY2008E EPS, 3.4x PPP and 1.1x book value. We maintain our Buy call on the stock with a price target of Rs374.

Valuation table

Year to 31 March	FY04	FY05	FY06	FY07E	FY08E
Net profit (Rs cr)	504.1	402.2	444.5	536.1	631.1
Shares in issue (cr)	14.3	14.3	14.3	14.3	14.3
EPS (Rs)	35.1	28.0	31.0	37.4	44.0
EPS growth (%)	18.6	-20.2	10.5	20.6	17.7
PE (x)	9.2	11.6	10.5	8.7	7.4
P/PPP (x)	5.1	4.4	4.4	3.8	3.4
Book value (Rs/share)	193.0	213.0	235.3	262.0	292.2
P/BV (x)	1.7	1.5	1.4	1.2	1.1
Adjusted book value (Rs/share)	175.6	198.6	224.6	251.4	281.4
P/ABV (x)	1.9	1.6	1.4	1.3	1.2
RONW (%)	19.7	13.8	13.8	15.0	15.9

Ashok Leyland

Ugly Duckling

Stock Update

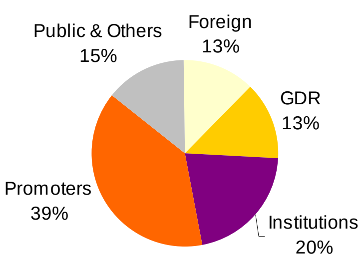
Good show

Buy; CMP: Rs39.5

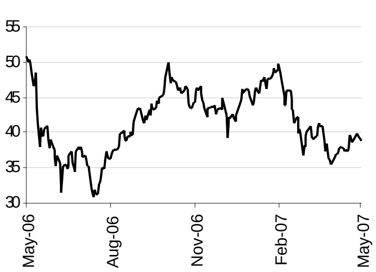
Company details

Price target:	Rs44
Market cap:	Rs5,143 cr
52 week high/low:	Rs52.5/30
NSE volume: (No of shares)	44.75 lakh
BSE code:	500477
NSE code:	ASHOKLEY
Sharekhan code:	ASHOKLEY
Free float: (No of shares)	63.2 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	11.3	-15.2	-5.5	-16.4
Relative to Sensex	2.1	-12.6	-11.3	-27.1

Result highlights

- Ashok Leyland Ltd (ALL) has delivered strong results for Q4FY2007 and the same are ahead of our expectations on the margin front. The top line has grown by 32.1% for the quarter, driven by a volume growth of 28.4% and a realisation growth of 2.9%.
- We are positively surprised by the operating profit margin (OPM), which stood at 11.6% for the current quarter against our expectations of 10.7%. In comparison with last year, the OPM has declined by 100 basis points, mainly due to a higher raw material cost. Consequently, the operating profits for the quarter have grown by 21.1% to Rs264.9 crore.
- Lower interest cost and taxes helped the company to post a net profit growth of 28.8% to Rs174.6 crore.
- For FY2007 the net sales for the company have grown by 36.5% led by a volume growth of 35%. The OPM has come down slightly by 30 basis points to 9.9% while the profit for the year has grown by 46% to Rs436.3 crore.
- For FY2008 the company has earmarked a capital expenditure of Rs1,000 crore for capacity expansions and new product developments; another Rs400 crore may be spent on acquisitions.

Result table Rs (cr)

Particulars	Q4FY07	Q4FY06	% yoy	FY2007	FY2006	% yoy
Net sales	**2,291.0**	**1,734.8**	**32.1**	**7,168.2**	**5,250.6**	**36.5**
Expenditure	2,026.1	1,516.1		6,459.8	4,717.4	
Raw material consumed	1,537.9	1,087.7		5,403.8	3,973.9	
Change in stock	168.0	196.1		-64.7	-204.9	
Staff cost	116.3	81.6		480.7	403.9	
Other exp	203.8	150.8		640.0	544.6	
Operating profit	**264.9**	**218.7**	**21.1**	**708.4**	**533.1**	**32.9**
Op profits excl forex gain/loss	259.6	214.1	21.2	705.4	536.7	31.4
Other income	16.9	11.0		47.0	33.0	
EBIDTA	**281.8**	**229.7**	**22.7**	**755.4**	**566.1**	**33.4**
Interest	1.9	9.8		5.3	16.5	
PBDT	280.0	219.9	27.3	750.0	549.6	36.5
Depreciation	48.1	33.0		150.6	126.0	
PBT	231.8	186.9		599.5	423.6	
Tax	57.3	51.3		163.2	125.0	
PAT	**174.6**	**135.5**	**28.8**	**436.3**	**298.7**	**46.1**
Extraordinary items	-3.0	-2.1		5.1	21.6	
Net profit	**171.5**	**133.5**	**28.5**	**441.3**	**320.3**	**37.8**
EPS (Rs)	1.3	1.1		3.3	2.3	
OPM (%)	11.6	12.6		9.9	10.2	
OPM-excl forex (%)	11.3	12.3		9.8	10.2	
PATM (%)	7.6	7.8		6.1	5.7	

- We would take a cautious outlook on the industry considering the rising interest rates and tightening liquidity in the country, which would affect the sales volumes. Consequently, after a dream run in FY2007, we expect the growth rates to moderate and expect a volume growth of 11.9% for FY2008. The company expects the industry to grow at 10-12% in FY2008 and has set a target of reaching the 100,000-vehicle mark during the current fiscal.
- At the current market price of Rs39.5, the stock discounts its revised FY2008E earnings by 11x and quotes at an enterprise value (EV)/earnings before interest, depreciation, tax and amortisation (EBIDTA) of 6.4x. We maintain our Buy recommendation on the stock with a price target of Rs44.

Strong volume growth drives top line

ALL gave a stellar performance in Q4FY2007, marking a revenue growth of 32.1% to Rs2,291 crore led by a strong volume growth of 28.4%. The goods carrier segment, contributing the bulk of the sales, led the growth with a strong 29.9% increase year on year (yoy). The sales of the passenger carrier segment too improved during the quarter as the segment recorded a growth of 26.3% yoy.

Sales performance

	Q4 FY07	Q4 FY06	% yoy	FY07	FY06	% yoy
MDV passenger	5,094	4,032	26.3	15,497	15,665	-1.1
MDV goods	21,006	16,169	29.9	67,301	45,193	48.9
LCV	47	201	-76.6	303	797	-62.0
Total sales	26,147	20,402	28.2	83,101	61,655	34.8

Margins better than our estimation

The OPM for the quarter declined by 100 basis points to 11.6% but was higher than our estimates of 10.7%. The year-on-year drop in the OPM is attributed to a steep rise in the raw material cost. During the year, the company effected two price hikes which were just about enough to offset the impact of the high raw material prices. However, the other cost increases could not be passed upon. Going forward, we expect the margin to remain in a narrow range. However there is scope for improvement, considering that Mission Gemba, the company's initiative to reduce costs, is entering the final stage and also because it was able to raise its prices by about 1.5% in April 2007.

Aggressive capex plans

As mentioned by the company on previous occasions, it has earmarked a capex of Rs4,000 crore for the next four years. For FY2008, the company would spend Rs1,000 crore. Out of this Rs400 crore would be spent on Uttaranchal, Rs350 crore shall be spent on the Ennore plant and another Rs80-100 crore would be spent on new launches and product developments. Further, the company shall spend about $17 million to acquire a testing facility in Detroit. The company may also spend another Rs300 crore for further acquisitions. For part funding the capex, the company is planning to raise about Rs1,000 crore through loans in Q2 or Q3 of the current year.

The company has a current capacity to manufacture 84,000 vehicles. With the completion of the Ennore plant, the capacity would be raised by 134,000 units, which shall be further raised to 200,000 vehicles in two years' time.

Outlook and valuations

The company re-affirms the strong growth prospects of the commercial vehicle industry and expects the industry to register a 10-12% growth in FY2008. It has set a target of 100,000 vehicles for itself. We would take a cautious outlook on the industry considering the rising interest rates and tightening liquidity in the country which would affect the sales volumes. Consequently, after a dream run in FY2007, we expect the growth rates to moderate and expect a volume growth of 11.9% for FY2008.

The company's capacity expansions plans, better operating efficiencies and increasing presence in the overseas markets (after the acquisition of Avia and the construction of a facility in the Middle East) are some of the big positives for the stock which make us bullish on the stock. At the current market price of Rs39.5, the stock quotes at FY2008E price/earnings ratio of 10.8x and at an EV/EBIDTA of 6.7x. We maintain our Buy recommendation on the stock with a price target of Rs44.

Earnings table Rs (cr)

Year ended March 31	FY05	FY06	FY07	FY08E
Net sales (Rs cr)	4247.7	5329.8	7168.2	8302.2
Net profit (Rs cr)	233.8	285.0	436.3	480.0
% yoy growth		*22%*	*53%*	*10%*
EPS (Rs)	1.8	2.2	3.3	3.6
% yoy growth		22%	53%	10%
PER (x)	22.0	18.0	11.8	10.8
P/BV (Rs)	4.4	3.6	2.7	2.4
EV/EBIDTA (x)	12.1	9.1	7.0	6.7
RoCE (%)	19.3	21.6	26.6	26.0
RoNW (%)	20.0	20.2	23.3	22.6

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

Sundaram Clayton

Apple Green

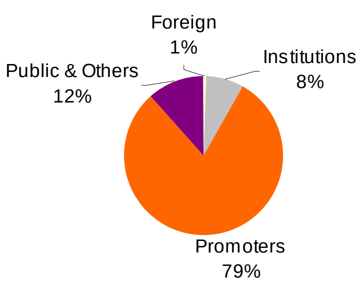
Stock Update

Beating expectations with strong margins

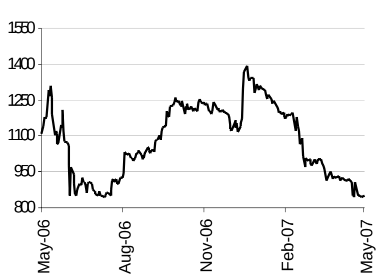
Buy; CMP: Rs847

Company details	
Price target:	Rs1,350
Market cap:	Rs1,607 cr
52 week high/low:	Rs1,410/779
NSE volume: (No of shares)	1,560
BSE code:	520056
NSE code:	SUNDRMCLAY
Sharekhan code:	SUNCLA
Free float: (No of shares)	0.38 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-10.6	-30.0	-29.7	-21.0
Relative to Sensex	-18.0	-27.8	-34.0	-31.1

Result highlights

- Sundaram Clayton Ltd's (SCL) Q4 results are ahead of our estimates because of a positive surprise on the operating profit margin (OPM) front.
- The net sales for the quarter grew by 25.3% to Rs218.4 crore, with both the die-casting and the air-brake division rendering a strong performance.
- The OPM improved by 160 basis points year on year (yoy) to 18.2% because of strong improvement in the operating performance of the company. The company was able to achieve better operating efficiencies due to higher volumes that led to considerable savings in the employee cost and other expenses.
- Both interest cost and depreciation charge rose due to high capital expenditure (capex) incurred by the company last year. Consequently, the adjusted net profit grew at 21% to Rs27.8 crore.
- The company has increased its capex for the next year to Rs175 crore, which shall be spent on both the divisions for capacity expansions and new product development.
- SCL has a huge investment portfolio, as it holds 56.8% in TVS Motors and also has holdings in other companies like TVS Electronics and TVS Finance & Services. In valuing the company we have assumed a 75% discount to the total investment value per share. After adjusting for the investments, the stock is currently trading at around 11.3x its stand-alone FY2008E earnings. We maintain our Buy recommendation on the stock with a revised price target of Rs1,350.

Result table Rs (cr)

Particulars	Q4FY07	Q4FY06	% yoy	FY07	FY06	% yoy
Net sales	**218.4**	**174.3**	**25.3**	**816.3**	**629.7**	**29.7**
Expenditure	178.7	145.4	22.9	687.3	532.6	29.1
Consumption of RM	121.5	91.7	-	445.5	321.4	
Incr/decr in stock	-4.4	-6.9	-	-13.0	-11.2	
Employee expenses	19.4	17.5	-	87.8	75.2	
Other expenses	42.2	43.1	-	167.0	147.2	
Operating profit	**39.7**	**28.9**	**37.0**	**129.0**	**95.4**	**35.3**
Other income	11.8	6.4	83.4	48.6	37.9	28.4
EBIDTA	51.5	35.4	45.5	177.7	133.2	33.3
Interest	4.2	3.0	38.9	16.1	8.3	94.5
PBDT	47.3	32.4	46.1	161.6	125.0	29.3
Depreciation	8.8	7.5	16.4	32.7	27.0	21.2
Profit before tax	38.5	24.8	55.1	128.9	98.0	31.5
Tax	10.8	1.9	458.5	36.1	23.0	57.2
Profit after tax	**27.8**	**22.9**	**21.1**	**92.8**	**75.0**	**23.6**
Extraordinary		5.8	-	0	5.8	
PAT after extraordinary	**27.8**	**28.7**	**-3.4**	**92.8**	**68.6**	
EPS (Rs)	14.6	12.1	21.1	48.9	36.2	
OPM (%)	18.2	16.6	-	15.8	15.2	
PATM (%)	12.7	13.1	-	11.4	11.9	

Strong top line growth

The net sales grew by 25.3% Rs218.4 crore in Q4FY2007, in line with our expectations. The growth in both the air-brake and the die-casting division remained strong for the quarter. The revenues from the air-brake division stood at Rs133.6 crore as against Rs109.4 crore in Q4FY2006, marking a growth of 22.1% yoy. The die-casting division too grew well as its revenues increased by 30.5% to Rs84.8 crore this quarter. The exports increased by 10.2%, mainly led by the growth in the die-casting division.

	Q407	Q406	% growth	FY07	FY06	% growth
Air-brakes						
Domestic	131.1	106.5	23.1	477.8	406.2	17.6
Exports	2.5	2.9	-12.5	10.0	11.1	-10.4
Total	**133.6**	**109.4**	**22.1**	**487.8**	**417.3**	**16.9**
Die-casting						
Domestic	57.8	41.1	40.7	196.8	136.2	44.5
Exports	26.9	23.9	13.0	131.8	75.7	74.0
Total	**84.8**	**64.9**	**30.5**	**328.5**	**211.9**	**55.0**

A positive surprise on the margin front

The OPM for SCL rose by 160 basis points yoy and by 260 basis points sequentially to 18.2%, mainly led by better operating efficiencies. Higher volumes and a tight control over the fixed costs led to this strong growth in the OPM despite a high raw material cost. The raw material cost, as a percentage of sales, rose from 48.3% in Q4FY2006 to 52.8%. For the full year, the fixed cost as a percentage of sales came down from 24% to 20.5%.

With the implementation of the value added tax in the state of Tamil Nadu, the company has started enjoying the benefits of setting off of the input tax against the goods sold in the state. Since, the same was implemented w.e.f January 1, 2007, the benefits have started flowing in from the present quarter.

The other income stood at Rs11.8 crore and was higher than our estimates. The interest cost and depreciation charge have risen due to an increase in the capex of the company. Consequently, the net profits have risen by 21.1% to Rs27.8 crore.

Capex for FY2008 increased

For FY2007 SCL had lined up a capex plan of Rs175 crore to be spent on both the die-casting and air-brake division. The capex shall be for both capacity expansion and new product development.

Outlook and valuations

SCL has performed well in the last one year, riding on the boom in the commercial vehicle sector. Going forward, we expect the higher usage of anti-lock braking systems in commercial vehicles to trigger a huge replacement demand for brakes. SCL is expected to be the biggest beneficiary of the same. We also believe that there is a strong potential for outsourcing to WABCO. Considering the higher volumes and the company's constant drive to control costs, we believe that the margins would stabilise at these levels going forward. However, the company is on a capex spree and would have to incur higher interest and depreciation costs going forward. Consequently, we are downgrading our FY2008E earnings by 9.1% to Rs67.6.

SCL has a huge investment portfolio with an investment value of Rs607 per share. It holds 56.8% in TVS Motors (8.8% directly and 48% indirectly, through its 100% subsidiary Anusha Investments). In valuing the company we have assumed a 75% discount to the total investment value per share. After adjusting for the investments, the stock is currently trading at around 11.3x its stand-alone FY2008E earnings. We maintain our Buy recommendation on the stock with a revised price target of Rs1,350.

Earnings table

Particulars	FY04	FY05	FY06	FY07	FY08E
Net sales	417.4	536.3	629.3	816.3	1,001.7
Net profit	46.3	52.5	68.6	92.8	116.5
EPS	24.4	27.7	36.2	48.9	61.4
% yoy growth		*13.4*	*30.7*	*35.1*	*25.6*
PER	28.5	25.1	19.2	14.2	11.3
P/B	7.8	6.7	5.6	4.6	3.8
EV/EBIDTA	29.6	19.8	14.4	10.7	8.6
ROCE (%)	30.6	26.7	27.8	31.2	32.5
RONW (%)	22.5	21.9	23.7	26.5	27.2

Pharmaceuticals

Sector Update

Omnicef loses patent protection

Event

The patent for Omnicef, the antibiotic used to treat various infections, expired on May 6, 2007, paving the way for generic companies to enter the cefdinir market in the USA. In this regard, Lupin and Sandoz (the generic arm of Swiss drug maker Novartis) have received the final approval from the US Food and Drug Administration (USFDA) for manufacturing and marketing cefdinir in both capsule and solution forms. On the other hand, Orchid Chemicals (Orchid), Ranbaxy Laboratories (Ranbaxy) and Teva—the world's largest generic companies—are awaiting approval from the USFDA.

About Omnicef

Abbot Laboratories' Omnicef is the branded version of the antibiotic Cefdinir. The total annualised market sales of cefdinir stood at $643 million (IMS-MAT: December 2005) of which $137 million came from the solution form of the drug and the remaining $506 million was derived from the sale of capsules. The combined sales of the solution and capsule form of the drug are estimated to have reached approximately $900 million in December 2006. Cefdinir is an extended-spectrum semisynthetic cephalosporin used to treat or prevent a variety of infections related to the ear, sinus, throat and skin.

Background of the case

The basic compound patent of the drug expired on May 6, 2007. However, the crystalline salt of the drug is additionally protected by a patent, which will expire in 2011. The innovator company, Abbot Laboratories, has sued all the generic companies to prevent them from launching the generic version of Omnicef upon the expiry of the basic compound patent in May 2007, alleging that their generic versions of Omnicef use the crystalline salt of the drug, which is protected by a patent until 2011. The next trial date for the litigation between Abbot Laboratories and the generic companies is set for May 2007, during which the court is expected to give a final verdict.

Since the patent for the drug has already expired on May 6, 2007, generic companies like Lupin and Sandoz, which already have approval from the USFDA, are free to attempt at-risk launches of their generic versions of Omnicef. We believe Sandoz will attempt an at-risk launch of the drug, whereas Lupin might wait for the court verdict. Even though the entry of generic companies into the Cefdinir market remains uncertain until the receipt of the final verdict from the US courts, Indian generic players like Lupin and Orchid seem confident of the ruling coming in their favour, as they will be able to prove that they are not using the crystalline salt to manufacture their generic copies of cefdinir.

Competitive scenario

The competitive landscape for generic Omnicef is likely to comprise six players: the innovator (Abbot Laboratories), the authorised generic company and four other generic companies (Orchid, Lupin, Sandoz and Teva) in the first wave of launch. Ranbaxy, which also has a pending abbreviated new drug application filing for the product is likely to receive its approval at a later date, as its filing was made later than those of the other four generic companies.

Implication & valuation

The management of Orchid has indicated that it is expecting the USFDA to approve its ANDA for cefdinir by the end of May 2007, enabling it to launch the drug in June 2007. By that time, the final verdict of the ongoing litigation between the generic companies and Abbot Laboratories is also expected. Hence we assume Indian companies—Lupin and Orchid—to launch the product in the USA by June 2007.

For our calculations, we have assumed the market size of cefdinir at approximately $900 million as of December 2006 (as indicated by the companies). While the entry of the generic players is expected to lower the prices of the drug in the USA, we expect the market to get eroded by 80-85% as against the high level of 95-98% that is typically seen in the case of blockbuster products going off patent. This is because of the limited competition seen in this space, with only four generic players as compared with 10-15 players entering the market typically.

Based on the above assumptions, we estimate cefdinir to contribute approximately $13.5 million and $16.9 million in revenues for Orchid and Lupin respectively. On a fully diluted expanded equity base of Orchid, the impact on the earnings is likely to be minimal at Rs0.4 per share in FY2008. For Lupin, the product is expected to contribute Rs2.4 per share in earnings during FY2008.

Estimation of revenues and earnings from Cefdinir

	Orchid	Lupin
Market size ($m)	900	900
Price erosion	85%	85%
Market share	12%	15%
Months in FY2008	10	10
Estimated revenues ($m)	13.5	16.9
Estimated profits ($m)	4.1	5.1
Incremental EPS (Rs)	0.4	2.4

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New Delhi Television
Nucleus Software Exports
Orchid Chemicals & Pharmaceuticals
ORG Informatics
Tata Elxsi
Television Eighteen India
Thermax
UTI Bank

Ugly Duckling

Ahmednagar Forgings
Ashok Leyland
BASF India
Ceat
Deepak Fertilisers & Petrochemicals Corporation
Fem Care Pharma
Genus Power Infrastructures
Hexaware Technologies
ICI India
India Cements
Indo Tech Transformers
Jaiprakash Associates
JM Financial
KEI Industries
NIIT Technologies
Punjab National Bank
Ratnamani Metals and Tubes
Sanghvi Movers
Saregama India
Selan Exploration Technology
South East Asia Marine Engineering & Construction
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Sun Pharmaceutical Industries
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Universal Cables
Wockhardt

Vulture's Pick

Esab India
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WS Industries India

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