investor's eye

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Take Five

Scrip	Reco Date	Reco Price	CMP	Target
Aurobindo	28-May-07	684	**781**	914
BASF	18-Sep-06	220	**261**	300
JP Associates	30-Dec-03	125	**714**	850
UltraTech	10-Aug-05	384	**816**	935
Zensar Tech	18-Jun-07	342	**334**	484

Ratnamani Metals and Tubes

Ugly Duckling

Stock Update

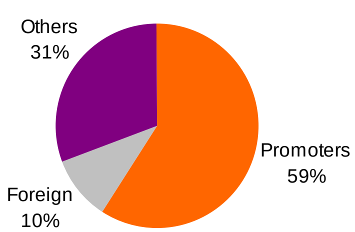
Price target revised to Rs1,215

Buy; CMP: Rs917

Company details

Price target:	Rs1,215
Market cap:	Rs825 cr
52 week high/low:	Rs948/266
NSE volume: (No of shares)	4,630
BSE code:	520111
NSE code:	RATNAMANI
Sharekhan code:	RATNMET
Free float: (No of shares)	0.4 cr

Shareholding pattern



Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	15.8	33.6	115.3	167.9
Relative to Sensex	14.2	21.9	98.7	89.7

Result highlights

- The Q4FY2007 results of Ratnamani Metals & Tubes Ltd (RMTL) are above our expectations.
- The company reported strong quarterly results. Its revenues for the quarter grew by 95.3% to Rs172.6 crore.
- The operating profit for the quarter grew by 78.3% to Rs34 crore. The operating profit margin (OPM) for the quarter declined by 240 basis points to 22.3% from 24.7% in Q4FY2006. The OPM declined due to a higher raw material cost as a percentage of sales. The raw material cost went up by 310 basis points to 62.9% from 59.8% in Q4FY2006. Other expenses as a percentage of sales also went up by 110 basis points to 12.4%.
- The interest expense for the quarter increased by 111.4% to Rs4.9 crore, while the depreciation cost for the quarter increased by 309.6% to Rs6.2 crore.
- The profit before tax grew by 80% to Rs27.7 crore. The net profit for the quarter grew by 39.4% to Rs17.6 crore due to a higher tax rate of 36.7% in this quarter compared with 17.8% in Q4FY2006.
- For the full year, the net sales grew by 79% to Rs571 crore and the net profit grew by 91% to Rs64.2 crore.
- The order book at the end of the quarter stood at Rs500 crore.

Result table Rs (cr)

Particulars	Q4FY07	Q4FY06	% yoy	FY2007	FY2006	% yoy
Gross	172.6	88.3	95.6	614.7	349.9	75.7
Excise duty	20.0	11.0	82.3	43.5	30.8	41.2
Net sales	**152.6**	**77.3**	**97.4**	**571.2**	**319.1**	**79.0**
Total expenditure	118.5	58.2	103.7	443.5	255.8	73.4
Operating profit	34.1	19.1	78.3	127.7	63.3	101.7
Other income	4.7	0.0	14996.8	5.0	0.1	8266.7
EBIDTA	38.8	19.2	102.4	132.7	63.4	109.4
Interest	4.9	2.3	111.1	16.4	8.9	84.6
Depreciation	6.2	1.5	309.6	15.6	7.4	110.5
PBT	**27.7**	**15.3**	**80.6**	**100.7**	**47.1**	**113.9**
Tax	10.1	2.7	270.5	36.5	13.6	169.6
PAT	17.6	12.6	39.4	64.2	33.5	91.4
Extraordinary items	0.0	0.0	-	0.0	0.0	-
Reported PAT	**17.6**	**12.6**	**39.4**	**64.2**	**33.5**	**91.4**
EPS	19.5	14.0	39.4	71.3	37.3	91.4
Margins						
OPM (%)	22.3	24.7		22.4	19.8	
PATM (%)	11.5	16.3		11.2	10.5	

The strong order book and increasing demand for its products from its key user industries, which are in capital expansion phase, impart a strong visibility to its earnings. At the current market price, the stock is quoting at 9.9x its FY2008E earnings and 7.1x its FY2009E earnings. In terms of enterprise value (EV)/earnings before interest, depreciation, tax and amortisation (EBIDTA), the stock is trading at 5.5x its FY2008E EV/EBIDTA and 4.0x its FY2009E EV/EBIDTA. We maintain our Buy recommendation on the stock with a revised price target of Rs1,215.

Strong order book of Rs500 crore

The order book of RMTL stood at Rs500 crore at the end of the fourth quarter as the company added orders worth Rs220 crore during the quarter. Of the total orders, Rs330 crore worth of orders are for the stainless steel tubes & pipes (SSTP) division and Rs170 crore worth of orders are for the carbon steel tubes & pipes (CSTP) division. The majority of the order book is to be executed over the next six months.

Segmental performance

SSTP

The SSTP division's revenues grew by 100% to Rs295 crore in FY2007. The sales volumes of this segment were at 7,358 tonne in FY2007, up 55.3% over FY2006. The realisations were up by about 29%. The realisations are expected to remain buoyant in line with the robust demand for SSTP pipes.

CSTP

The CSTP division's revenues grew by 69% to Rs300 crore in FY2007. The sales volumes of this segment were at 61,525 tonne, up by 57.2% over FY2006. The strong growth in the volumes is expected to continue in FY2008 and FY2009, as the company has expanded its capacity at Kutch from 150,000 tonne to 300,000 tonne. The realisations of this division were higher by 7.6% in FY2007.

SS mother pipe capacity installed

The company has installed a 7,000-metric-tonne capacity for mother pipes, which are used as raw material for making SS pipes. Currently the company imports 100% of its mother pipe requirement from countries like Japan, Korea and China. The new mother pipe capacity will help the company save close to Rs5-10 crore per annum and will also reduce its dependency on the overseas suppliers. This capacity will meet 60-70% of RMTL's mother pipe requirement with imports catering to the balance need.

Capex plans

To cater to the increasing demand for its products the company is expanding its capacities by way of balancing and setting up newer capacities. For instance, RMTL plans to expand its SS pipe capacity from the current 14,000 metric tonne (MT) to 18,000MT by September 2007. It has also set up of a mother pipe plant. The company plans to spend about Rs40-50 crore each in FY2007 and FY2008 towards capital expenditure.

Introducing our FY2009 earnings estimate at Rs134.6 per share, raising price target to Rs1,215

We are introducing our FY2009 earnings estimate for RMTL at Rs134.6 per share and revising our FY2008 earnings per share estimate (EPS) by 28.8% to Rs95.9. We are also raising our price target to Rs1,215, which is based on 9x its expected FY2009 EPS.

We expect RMTL's order book to remain strong with the surge in the demand for both its products, ie stainless steel (SS) pipes and carbon steel (CS) pipes. The capital expenditure lined up by the refining and petrochemical majors in India augurs well for RMTL. SS pipes primarily find application in steam boilers in power plants as well as in heat exchangers in the oil & gas and petrochemical sectors. India is expected to add approximately 68,000 megawatt of power generation capacity in the 11th Five-Year Plan. This would drive the demand for SS pipes.

At the current market price, the stock is quoting at 9.9x its FY2008E earnings and 7.1x its FY2009E earnings. In terms of EV/EBIDTA, the stock is trading at 5.5x its FY2008E EV/EBIDTA and 4.0x its FY2009E EV/EBIDTA. We maintain our Buy recommendation on the stock with a revised price target of Rs1,215.

Key financials

Particulars	FY05	FY06	FY07	FY08E	FY09E
Net sales (Rs crore)	181.0	319.1	571.2	818.4	1087.8
Net profit (Rs crore)	13.3	33.5	64.1	88.5	125.7
Shares in issue (crore)	0.9	0.9	0.9	0.9	0.9
EPS (Rs)	14.7	37.3	71.2	95.9	134.6
% y-o-y change	*226.4*	*153.1*	*91.1*	*34.7*	*40.3*
PER (x)	64.5	25.5	13.3	9.9	7.1
Book value (Rs)	56.3	90.7	156.2	249.8	379.2
P/BV (x)	16.9	10.5	6.1	3.8	2.5
EV/EBIDTA (x)	29.8	14.5	7.7	5.5	4.0
EV/Sales (x)	4.8	2.9	1.7	1.2	0.9
Dividend yield (%)	2.3	0.8	0.5	0.5	0.5
RoCE (%)	45.3	38.7	45.3	45.0	50.0
RoNW (%)	57.7	50.7	57.7	47.7	43.0

Cadila Healthcare

Emerging Star

Stock Update

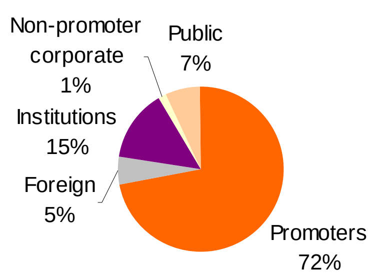
Cadila acquires Brazilian firm Nikkho

Buy; CMP: Rs395

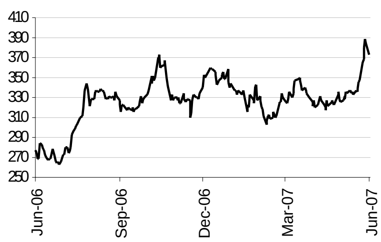
Company details

Price target:	Rs425
Market cap:	Rs4,977 cr
52 week high/low:	Rs385/241
NSE volume: (No of shares)	31,038
BSE code:	532321
NSE code:	CADILAHC
Sharekhan code:	CADILAHEAL
Free float: (No of shares)	3.5 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	14.4	13.3	11.4	32.7
Relative to Sensex	12.9	3.4	2.8	-6.0

Key points

- Cadila Healthcare (Cadila) has signed an agreement to acquire 100% stake in Quimica e Farmaceutica Nikkho do Brasil Ltda. (Nikkho) for a consideration of around $26 million (ie about 1x of Cadila's annual sales).
- Nikkho had posted sales of US$ 26 million for CY2006. It currently markets 22 products under 13 different brands. It also has nearly 50 registered brands that are yet to be launched.
- The acquisition is a strategic one for Cadila, as it would help the company to foray into the high-margin branded generic market of Brazil.
- Anticipating 18% and 15% growth for Nikkho in FY2008 and FY2009 respectively, we estimate the latest acquisition would contribute about 5-6% of our estimated revenue in FY2009. Our back-of-the-envelop calculation shows that the acquisition would have a marginal positive impact on the earnings of Cadila during FY2008.
- At the current market price of Rs395, Cadila is trading at 17.9x its estimated FY2008 earnings and 14.8x its estimated FY2009 earnings. Considering the strong growth momentum of the company, we maintain our Buy recommendation on the stock with a price target of Rs425.

Cadila has signed an agreement to acquire 100% stake in Quimica e Farmaceutica Nikkho for a consideration of around $26 million (ie about 1x of Cadila's annual sales). The proposed acquisition is in line with Cadila's strategy to expand its global business and foray into the high-growth branded generic market of Brazil. However, the agreement would come into effect after the satisfaction of the closing conditions.

About Nikkho

Nikkho is a profit-making mid-sized, privately held company in Brazil with a revenue base of US$26 million. In fact, it had posted sales of US$ 26 million for CY2006. The company caters exclusively to the Brazilian prescription (branded generics) drug market and has been in the market for over four decades.

With a strong marketing network, Nikkho's sales force of 125 people cover all the major markets in Brazil and enjoy a good rapport with 60,000 medical practitioners.

Valuation table Rs (cr)

Particulars	FY2005	FY2006	FY2007	FY2008E	FY2009E
Net sales	1277.9	1484.5	1828.8	2129.7	2474.0
Net profit	132.4	164.9	233.8	277.4	335.6
Shares in issue (cr)	12.6	12.6	12.6	12.6	12.6
EPS (Rs)	10.5	13.1	18.6	22.1	26.7
% y-o-y change	*0.4*	*24.5*	*41.8*	*23.9*	*21.0*
PER (x)	37.5	30.1	21.2	17.9	14.8
Cash EPS (Rs)	16.3	19.3	25.2	29.7	34.9
Cash PER (x)	24.3	20.4	15.7	13.3	11.3

The company currently markets 22 products under 13 different brands. It also has nearly 50 registered brands that are yet to be launched. Its product basket comprises a wide range of therapeutic products covering segments such as general medicine, paediatrics, gynaecology, neurology, gastroenterology, otolaryngology, respiratory and dermatology.

It has also got a manufacturing facility in Brazil with a total annual production capacity of 4.99 million ampoules of both injectable and oral liquids and 96 million units of solids (tablets).

Implication and synergies of acquisition

The acquisition seems to be a beneficial one for Cadila as the latter has valued Nikkho at about 1x its CY2006 sales. As Nikkho is exclusively into high-growth and high-margin branded generic segment of Brazil (which is again one of the fastest growing pharma markets in the world), the deal seems cheaper.

On the other hand, the acquisition is a strategic one for Cadila, as it would help the company to foray into the high-margin branded generic market of Brazil. In fact, Cadila has already gained presence in the highly commoditised pure generic segment and that is under losses. It currently markets 13 generic products in Brazil. In FY2007, Cadila's generic business reported sales of Rs17.6 crore with a loss of Rs10.3 crore. Now, with the entry into the branded generic segment, Cadila expects the latest acquisition to be instrumental in turning around its Brazilian business.

With the acquisition, Cadila would also have access to Nikkho's branded generic portfolio of 22 products, which are growing at over 15% annually. Apart from this Nikkho has 50 registrations in niche therapy segments like gynecology, neurology and respiratory; the same have not been launched yet. Incidentally, the Brazilian branded generic market is expanding at over 20% annually.

Hence, taking into consideration the new launches from the acquired pipeline and its own registrations (Cadila has five branded generic applications pending for Brazil), the company expects over 25% growth for the Brazilian branded generic business in future. But anticipating 18% and 15% growth for Nikkho in FY2008 and FY2009 respectively, we estimate the latest acquisition would contribute about 5-6% of our estimated revenue in FY2009.

Further, the decades of marketing experience of Nikkho in Brazil would strengthen Cadila's position in Brazil (the Brazilian pharma market size is estimated at $8 billion), which is the largest Latin American market and one of the fastest growing pharma markets in the world.

Valuation

The company has not indicated the financial details of the acquisition except for the CY2006 revenues of the Brazilian company. Currently Nikkho is growing at around 15% annually. We have assumed an 18% revenue growth with an EBITDA margin of 14% (as per the Brazilian industry average of 14-18%) for Nikkho for FY2008. We have estimated the asset base of Nikkho by assuming an asset turnover ratio of 0.75 (as per the Brazilian industry average). Our back-of-the-envelop calculation shows that the acquisition would have a marginal positive impact on the earnings of Cadila during FY2008.

The acquisition of Nikkho is in line with Cadila's strategy to expand its global business and achieve its vision of becoming a $1-billion company by December 2010 (ie FY2011). Further, Cadila is in the process of acquiring a couple of mid-sized companies with a marketing platform in Spain and Italy where the generic penetration is limited. These acquisitions would be financed from the planned foreign currency convertible bond/American depository receipt/global depository receipt issue of US$100 million.

At the current market price of Rs395, Cadila is trading at 17.9x its estimated FY2008 earnings and 14.8x its estimated FY2009 earnings. Considering the strong growth momentum of the company, we maintain our Buy recommendation on the stock with a price target of Rs425.

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

Sharekhan Stock Ideas

Evergreen

HDFC Bank
Infosys Technologies
Reliance Industries
Tata Consultancy Services

Apple Green

Aditya Birla Nuvo
ACC
Apollo Tyres
Bajaj Auto
Bank of Baroda
Bank of India
Bharat Bijlee
Bharat Electronics
Bharat Heavy Electricals
Bharti Airtel
Canara Bank
Corporation Bank
Crompton Greaves
Elder Pharmaceuticals
Grasim Industries
HCL Technologies
Hindustan Unilever
ICICI Bank
Indian Hotels Company
ITC
Mahindra & Mahindra
Marico
Maruti Udyog
Lupin
Nicholas Piramal India
Omax Autos
Ranbaxy Laboratories
Satyam Computer Services
SKF India
State Bank of India
Sundaram Clayton
Tata Motors
Tata Tea
Unichem Laboratories
Wipro

Cannonball

Allahabad Bank
Andhra Bank
Cipla
Gateway Distriparks
International Combustion (India)
JK Cement
Madras Cement
Shree Cement
Tourism Finance Corporation of India
Transport Corporation of India

Emerging Star

3i Infotech
Aban Offshore
Alphageo India
Cadila Healthcare
Federal-Mogul Goetze (India)
KSB Pumps
Marksans Pharma
Navneet Publications (India)
Network 18 Fincap
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
Aurobindo Pharma
BASF India
Ceat
Deepak Fertilisers & Petrochemicals Corporation
Fem Care Pharma
Genus Power Infrastructures
Hexaware Technologies
ICI India
India Cements
Indo Tech Transformers
Jaiprakash Associates
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KEI Industries
NIIT Technologies
Punjab National Bank
Ratnamani Metals and Tubes
Sanghvi Movers
Saregama India
Selan Exploration Technology
South East Asia Marine Engineering & Construction
Subros
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Vulture's Pick

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