IDFC INSTITUTIONAL SECURITIES
India Research

IDFC Emerging Stars Conference 2011

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IDFC Emerging Stars Conference 2011

We at IDFC Securities recently hosted the 6th edition of our flagship conference – the "Emerging Stars Conference 2011". With the current state of equity markets raising ample questions in the minds of investors (and corporates looking to contain further value erosion!), the conference saw strong participation, with more than 1700 meetings being conducted between managements of 54 companies and over 225 investors from across the globe. The conference format, focused on mid and emerging companies which could be potential game changers, augured well with the bottom-up approach of investing which we believe will play out in the current year.

The spaces that generated the maximum interest were related to Consumerisation, Infrastructure and Pharma as also other stock-based themes. The conference proved to be an important platform for addressing critical apprehensions among investors (clarifications on the most recent corporate changes in Jain Irrigation) and also gave investors a peep into potential value creating businesses (interaction with Tribhovandas Bhimji Zaveri – upcoming IPO).

Amidst the ambitious plans of Corporate India, we thought it would only be pertinent to touch upon the underlying investing styles for the "eventful" Indian markets. We held a panel discussion on "Corporate Governance versus Profiteering" led by the most respected financial industry veterans, including Samir Arora (Helios), Sunil Singhania (Reliance Capital), Vikram Kotak (Birla Sunlife), Satish Ramanathan (Sundaram Mutual), Nitin Bajaj (Fidelity Investments) and Sashi Krishnan (Bajaj Allianz). With the issue being as "controversial" as one would envisage, the steam and depth in the discussion (around relevant anecdotes from Corporate India!) forced us to take the discussion off media coverage! De-stressing at the conference came in the form of some entertaining work by the famous illusionist, Edumonto, and a skit by Bharat Dhabolkar.

The recent issues related to corruption in the bureaucracy and corporate governance for Corporate India has no doubt put investors, particularly FIIs, on the worrying fence. On the positive side, the recent developments have surfaced "latent concerns", which intuitively means that the clean up was due and is for the positive going forward. While the overall investment mood remains cautious on the back of inflation fears, liquidity tightening and capital draw-downs by FIIs, our sense is that the bottom-up strategy will prevail for 2011.

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Panel discussion topic: Corporate governance versus profiteering

Panelists:

- **Samir Arora – Helios Capital**
- **Sunil Singhania – Reliance Mutual**
- **Vikram Kotak –Birla Sun Life Insurance**
- **Satish Ramanathan –Sundaram Mutual**
- **Nitin Bajaj – Fidelity Investments**
- **Sashi Krishnan – Bajaj Allianz Life**

The discussion focused on the following:

- Large-cap investing (assuming more transparency), v/s emerging stars (flexible corporate governance!)
- Starkness of investing styles: How important is corporate governance while investing?
- What has been the return profile of companies with perceived corporate governance issues?
- Experiences as an investor with "failed" corporate stories due to governance issues
- Choice between capital protection and capital growth
- Do markets and investors have short memories? Do untouchables of the past remain so perennially?

The panel discussion hosted some of India's most influential minds, people with more than 15 years experience of markets, having witnessed corruption scams, corporate governance overhang eroding stock values, and the impact of 'perceptions' on markets. Interestingly and ironically, as one of the panelists pointed out, most companies with 'perceived corporate governance issues' find a place among the top performing stocks over the last decade. Does that mean that bad corporate governance is good, or that good corporate governance is bad? With the discussion covering some of the biggest names of corporate India (with relevant anecdotes!) and the impact of past events (and scams!) on markets, our investors and managements were treated to a good perspective of how these influential minds read corporates actions.

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Vikram Kotak
Birla Sun Life Insurance

Nitin Bajaj
Fidelity Investments

Sunil Singhania
Reliance Mutual

Satish Ramanathan
Sundaram Mutual

Sashi Krishnan
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Construction

A2Z Maintenance & Engineering Services — Unrated (Rs214, MCAP: Rs15.8bn / US$347.5m)

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- A2Z Maintenance & Engineering Services is a diversified business group with a presence in EPC (power and roads), municipal solid waste management, renewable energy generation, and facilities management services.
- It clocked revenues of Rs12.2bn, EBIDTA of Rs2bn, PAT of Rs981m, and an ROE of 24% in FY10. Power EPC accounts for ~90% of the company's revenue base.
- The company listed on the bourses in December 2010. The proceeds of Rs6.75bn would be used mainly for investments in power plants that A2Z is developing in the renewable energy sector and for meeting increased working capital requirements.
- A2Z is setting up 185MW worth of projects in the renewable energy segment (cogeneration and biomass) in Punjab, Rajasthan and Uttar Pradesh, with 135MW scheduled to be operational by December 2011.
- It also has a strong presence in facilities management services and derived revenues of Rs910m from this segment in FY10. Its key clients include Aircel, Apollo Munich, DMRC and Indian Railways.
- The company provides IT solutions for AT&C loss reductions. It has also partnered with Sterlite Technologies for undertaking projects under R-APDRP. It has an ongoing automated meter reading project in Jabalpur.
- A2Z recently entered the e-waste management business and is implementing a project in Kanpur.
- The FMS business earns 5-6% PAT margins and has a receivable cycle of 60-65 days.
- The company aims to enhance its focus on solid waste management and renewable energy.
- It is developing a remote metering solution to reduce metering losses and errors.
- A2Z expects its EPC business to grow at ~25% annually in the near term, driven by strong growth opportunities in the power sector.

Key financials

As on 31 March	FY08	FY09	FY10
Net sales (Rs m)	4,790	6,661	11,228
Adj. net profit (Rs m)	503	597	1,003
Shares in issue (m)	53.5	55.2	56.6
Adj. EPS (Rs)	9.4	10.8	17.7
% change	*350.2*	*14.8*	*64.0*
PE (x)	22.7	19.8	12.1
RoE (%)	78.4	38.0	30.9
RoCE (%)	31.0	21.8	20.6

FMCG

ADF FOODS LTD

UNRATED (RS54, MCAP: RS1.1BN / US$24M)

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- ADF Foods Ltd. operates in the rapidly growing 'ready to eat' (RTE) segment and has strong brands like Ashoka. The company manufactures and distributes Indian pickles, chutneys, canned foods, frozen foods, and spices. It derives almost 95% of revenues from exports.
- ADFL's flagship brand is Ashoka, which includes several categories like pickles, frozen vegetables, snacks, frozen breads and ready to eat curries, and is targeted at the Indian diaspora. Besides Ashoka, it has other brands like Camel (premium brand for Middle-East-style pickles and spices) and Aeroplane (economy brand of Indian pickles and chutneys).
- The company recently ventured into the Indian markets with a brand called Soul, targeted at the health conscious. Its current products are olive-oil-based pickles and RTE vegetables. While Soul is currently being test marketed, the management is increasingly focusing on the domestic market, and we expect a spate of new launches. Our sense is that revenues from India will move up to 30-40% over the next 4-5 years from 5% now.
- While the focus of the company has largely been traditional Indian food for the Indian diaspora, the company is also foraying into new foods like hummus, pastas and Indian food customized for non-Indians (via the brand, Truly Indian, which is low on spices).
- ADFL acquired Elena's in September 2010 for an estimated US$15m. Elena's is a US-based manufacturer of organic and natural products of protein-based Mexican foods with revenues of ~US$10m in CY10. The acquisition allows ADF to leverage Elena's manufacturing facility and distribution setup in the US besides widening product range. Elena's, which had been making losses, has broken even at cash level in just a quarter since the acquisition. The management expects to recover its entire investment in the next four years.
- The company currently has no debt and Rs250m cash on the books.

Key financials

As on 31 March	FY07	FY08	FY09	FY10
Net sales (Rs m)	799	898	959	1,033
Adj. net profit (Rs m)	45	58	75	134
Shares in issue (m)	10.0	18.2	17.7	20.0
Adj. EPS (Rs)	4.5	4.2	4.2	7.0
% change	*69.9*	*(5.9)*	*(0.3)*	*67.0*
PE (x)	12.5	13.3	13.3	8.0
Price/ Book (x)	1.6	1.3	1.2	1.1
EV/ EBITDA (x)	5.2	6.2	3.8	5.1
RoE (%)	13.5	10.1	9.3	14.5
RoCE (%)	14.2	11.0	10.3	15.2

Construction

AHLUWALIA CONTRACTS — UNRATED (RS132, MCAP: RS8.3BN / US$181.3M)

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- Ahluwalia Contracts has 44 years of experience in the construction industry and is one of the largest civil contractors in India.
- It has a diverse range of execution capabilities, with experience in construction of malls, hospitals, educational institutes, commercial complexes, super luxury hotels, corporate office complexes, multi-storey residential complexes.
- The company clocked revenues of Rs15bn in FY10, with EBIDTA of Rs1.7bn and PAT of Rs817m.
- It had guided for revenues of Rs20bn in FY11 (33% yoy growth), but has lowered it to Rs18bn (20% yoy growth). The management expects revenues to grow 20-25% in FY12.
- Order inflow to date in FY11 has been Rs16bn. The company currently has a bidding pipeline of Rs15bn and expects strong order flow over the next two months.
- The current gross order backlog stands at Rs55bn and the unexecuted order backlog stands at Rs34bn.
- Nearly 80% of the order backlog has pass-through for materials like steel and cement (20% of the order backlog comprises orders with free issue of materials).
- Construction of the Kota bus terminal is under way (second floor completed). The company expects equity IRR of 24% from the project.
- Borrowing rates have increased by ~200bp over the past six months. The current average borrowing rate is ~11.5%. Total debt on the books is Rs1.3bn, with a cash balance of Rs1.6bn (including cash locked in).

Key financials

As on 31 March	FY08	FY09	FY10
Net sales (Rs m)	8,801	11,641	15,677
Adj. net profit (Rs m)	516	577	818
Shares in issue (m)	62.8	62.8	62.8
Adj. EPS (Rs)	8.2	9.2	13.0
% change	*65.6*	*11.8*	*41.7*
PE (x)	16.0	14.3	10.1
Price/ Book (x)	6.6	4.7	3.3
EV/ EBITDA (x)	7.2	5.6	4.5
RoE (%)	50.5	38.2	37.9
RoCE (%)	34.8	30.1	29.0

Textiles

ALOK INDUSTRIES

UNRATED (RS21, MCAP: RS16.2BN / US$356M)

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- Alok Industries is a fully integrated textile company and one of the largest textile manufacturers in the country.
- The company has been displaying healthy operational performance. It has been able to pass through rising cotton prices, which has protected margins. This, along with increasing end-user demand, has helped the company deliver strong volume growth. Alok's export growth has been outperforming its domestic growth.
- It recently purchased a substantial proportion of its cotton requirement at Rs39,000 per candy (1 candy = 356 kg) as against prevailing prices of Rs48,000-50,000 per candy. This low-cost inventory should provide a cushion for the coming quarters amid rising cotton prices.
- The company added 20 'H&A' stores in Q3FY11, taking the total number of stores to 271. However, it has reduced its store target for March 2011 to 350 from 400 earlier.
- Alok plans to incur capex of ~Rs8bn, mainly in polyester and cotton spinning. It has a capacity of 0.34m spindles in cotton spinning, which it aims to increase to 0.4m. With the commencement of its second polyester plant, total capacity would increase to 0.4m tpa (from 0.2m tpa now). The company is also planning an additional 0.2m tpa in the polyester segment.
- It has captive power capacity of 70MW, of which 15MW is contributed by a gas-based plant in Vapi. The balance 55MW comes from a plant in Silvassa, which operates on furnace oil. The company expects to run the plant on gas to reduce production cost. It also has a parallel connection with the grid in Silvassa, from which it sources power at an average realization of Rs4/ unit.
- **Real estate:** Alok has two commercial properties, Ashford Centre and Peninsula Business Park, which are ready for sale. The properties are valued at ~Rs14bn. The company holds a 50% stake through a JV in a residential project in Nahur, Mumbai, valued at Rs4bn.

Key financials

As on 31 March	FY 2008	FY 2009	FY2010
Net sales (Rs m)	22,676	30,788	44,127
Adj. net profit (Rs m)	1,897	741	1,377
Shares in issue (m)	206.3	197.0	787.8
Adj. EPS (Rs)	9.9	3.8	2.6
% change	*12.1*	*(61.8)*	*(32.4)*
PE (x)	2.1	5.5	8.1
Price/ Book (x)	0.3	0.2	0.6
EV/ EBITDA (x)	9.1	9.0	8.3
RoE (%)	15.5	4.4	5.9
RoCE (%)	6.0	2.9	4.1

Construction

ASHOKA BUILDCON — UNRATED (RS306, MCAP: RS16.1BN / US$353M)

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- Ashoka Buildcon (ABL) is an integrated road BOT player established in 1976. It was listed on the bourses in 2010.
- It has a portfolio of 23 projects, of which 18 are operational and 5 are under construction/ development. ABL has already handed over three projects to the concessioning authorities.
- ABL posted revenues of Rs11bn and PAT of Rs757m in FY10 (standalone). The total order backlog was Rs30bn as of 15 January 2011.
- The company has its own EPC division and has constructed 44 roads and bridges on its own or through JVs/ associates. ABL has also constructed ~5.4m sqft of commercial, industrial and institutional projects. It is currently executing Rs11.7bn worth of power EPC projects (T&D).
- ABL plans to increase its focus on the third-party EPC business in the power sector.
- It has a total debt of Rs1.5bn (including working capital debt of Rs1bn) apart from its BOT project debt of Rs11.5bn.
- The company has so far invested ~Rs3bn as its own share in road BOT projects and will need to invest a further Rs4.5bn as equity in these projects over the next two years. ABL expects to meet the funding requirement through internal accruals (Rs2bn-2.5bn) and the balance from securitization of toll collections in its operational projects.
- ABL expects IRRs of ~17% from its newer road assets, vis-à-vis 18-19% from older ones.

Key financials

As on 31 March	FY08	FY09	FY10
Net sales (Rs m)	3,228	5,184	7,956
Adj. net profit (Rs m)	331	348	804
Shares in issue (m)	45.7	45.7	45.7
Adj. EPS (Rs)	7.3	7.6	17.6
% change	*17.7*	*3.7*	*130.8*
PE (x)	41.7	40.2	17.4
Price/ Book (x)	3.7	3.4	2.5
EV/ EBITDA (x)	9.1	8.4	8.5
RoE (%)	11.1	10.6	19.9
RoCE (%)	10.1	9.1	8.8

Auto

BALKRISHNA INDUSTRIES — OUTPERFORMER (RS125, MCAP: RS12BN / US$267M)

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- **Specialty tire space:** Balkrishna Industries (BIL), which is part of the Poddar Group, operates in specialty off-highway tires in the international market. Revenues are predominantly export-driven, with annual sales of Rs19bn in FY11E (110000MT of volumes). It has a wide portfolio of 1900 SKUs of tires for agricultural, construction and industrial purposes, and presence across 120 countries. Europe accounts for 51% of sales and America accounts for 20%.
- **Penetration-led growth:** BIL, through its brand BKT, predominantly operates in the replacement tire market. The off-highway tire market is 8% of the global USD130bn tire industry and BIL has just 2-3% of this market. As BIL expands its reach in newer countries like Russia, increases its distribution in existing European and American markets, and enhances its portfolio with the launch of all-steel radial mining tires, agri-radial tires, etc., we see immense scope for sustained growth momentum.
- **Capacity expansion mode:** BIL has manufacturing facilities in Waluj (Maharashtra), Bhiwadi and Chopanki (Rajasthan), with an annual achievable capacity of 120,000MT. With YTD sales already at 110,000MT, BIL has lined up aggressive investments for capacity expansion. While Rs2bn of capex on debottlenecking the current facilities would help improve achievable capacity by 10,000MT, BIL has lined up Rs12bn in investments for a greenfield expansion in Bhuj, Gujarat. This plant will have achievable capacity of 90000MT and will be operational in H2FY13. Of the Rs12bn project cost, BIL has tied up USD175m in debt, with the rest to be funded through internal accruals. So, even if BIL maintains a growth pace of 15% in volume terms, it would have sufficient capacity for the next five years. However, capacity constraints would curtail growth until FY13.
- **Rubber prices remain a concern:** The price of natural rubber (which accounts for 32% of BIL's raw material) has moved up Rs235/kg (USD5500+/ tonne) from Rs130/ kg a year ago and an average of Rs80-100/ kg. While BIL is covered up to May 2011 at a blended natural rubber price of USD3800, concerns remain on the sustained high prices of rubber. If the international rubber prices remain at current levels, BIL will have to take a price hike of 15-20% to sustain current spreads. Other raw materials like carbon black, synthetic rubber, chemicals, etc, would remain high in the near term as they are derivatives of crude oil.
- **Better placed to increase prices; but expect margin erosion:** Compared with tire companies operating in the competitive and commoditized CV market, BIL is in the specialty segment and enjoys much better gross margins (35-40%). So, in the wake of increasing commodity costs, BIL is better placed to pass through costs and maintain spreads. BIL's price differential of 20%+ versus competition gives it room to increase prices. However, given the differential of 50% in the spot rubber prices to BIL's current cost, we are building in a margin erosion of 120bp in FY12.
- BIL currently has debt of Rs4.6bn on the books.

Key financials

As on 31 March	FY08	FY09	FY10	FY11E	FY12E
Net sales (Rs m)	9,781	12,524	13,867	19,506	24,001
Adj. net profit (Rs m)	1,061	714	2,087	1,834	2,067
Shares in issue (m)	97	97	97	97	97
Adj. EPS (Rs)	11.0	7.4	21.6	19.0	21.4
% change	*26.8*	*(32.7)*	*192.3*	*(12.1)*	*12.7*
PE (x)	11.4	16.9	5.8	6.6	5.8
Price/ Book (x)	2.9	2.6	1.8	1.4	1.2
EV/ EBITDA (x)	8.6	8.5	4.5	4.6	4.4
RoE (%)	28.0	16.2	37.0	24.5	22.0
RoCE (%)	17.8	14.2	27.9	21.6	19.9

Midcaps

BILCARE — UNRATED (RS479, MCAP: RS11.3BN / US$248MN)

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- Bilcare is one of the largest players in the Indian pharma packaging segment, with a presence in foils and blisters. It operates in three verticals in the pharma value chain – Pharma Packaging Innovation (PPI), Global Clinical Supplies (GCS) and Bilcare Technologies. The company has a ~62% market share in the Indian barrier blister market.
- The main fillip to the PPI business is expected to come from the US market, where an ongoing shift in packaging from high-cost bottle packaging to blister packaging by 2012 is likely to generate huge demand from generic manufacturers.
- Bilcare recently acquired Ineos, a leading global producer of rigid films, with manufacturing facilities in Germany, Italy, India and North America. Of the total deal size of Eur100m, Eur70m was raised through debt at a rate of Libor + 350bp. Ineos had a top line of Eur240m and EBITDA margin of 5.5% in CY09, which is expected to increase to 8% due to savings from procurement and formulation.
- In the GCS segment, Bilcare assists pharmaceutical and bio-pharmaceutical companies in undertaking clinical trials during the new drug discovery process. It offers services like protocol design, regulatory compliance, batch manufacturing, packaging design, clinical packaging and randomization, storage and global distribution.
- The technology division of Bilcare is focused on creating solutions for anti-counterfeiting, security and brand protection across different industries. It has introduced a unique security technology called non-clonable ID, which allows articles to be authenticated along the supply chain.
- Bilcare had an outstanding FCCB of US$128m, which it has fully bought back. The company estimates a capex requirement of US$20m in FY11.

Key financials

	FY06	FY07	FY08	FY09	FY10
Net Sales (Rs. mn)	2,645	4,079	6,507	8,560	10,478
Adj net profit (Rs. mn)	389	599	816	829	1,169
Shares in issue (mn)	14	14	16	20	24
Adj EPS (Rs)	28.4	42.2	49.6	42.1	49.1
% change		*48.6*	*17.5*	*(15.0)*	*16.6*
PE (x)	18.8	12.7	10.8	12.7	10.9
Price/Book (x)	4.9	2.4	2.2	2.1	1.5
EV/EBITDA (x)	32.6	19.3	13.9	11.6	8.7
RoE (%)	24.9	25.6	23.1	18.7	17.1
RoCE (%)	12.1	17.2	15.6	12.3	14.1

Power

CESC

OUTPERFORMER (RS272, MCAP: RS34BN / US$753MN)

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- **Distribution circle profits being driven by capacity expansion:** CESC's current capacity is 1225MW, including the recently commissioned Budge Budge III (250MW) power plant. It is running the plants at 93% PLF, with T&D losses at less than 13.5% and collection of 99.5%. CESC has tied up coal for its power plants through long-term agreements with Coal India and captive coal mines. The current tariff is 4.73/ unit, driven by an increase in costs as also equity base. CESC incurs a capex of Rs5bn annually on maintenance capex.
- **Construction of new power plants on track:** The construction of the Chandrapur (600MW Dhariwal) power project is on track (initial piling work done), with commissioning likely in 2013. The 600MW Haldia project has achieved financial closure and is likely to invite bids for equipment soon. The management expects construction to begin in three months. CESC is awaiting coal linkage for its 1320MW Orissa power plant, work at which has been completed. CESC has a top score of 90% for securing coal linkages and is confident of obtaining the same. Work on the 1320MW Balgarh project started late as the company only recently acquired land and received environment TOR; this accounts for the project's low score of 70% for coal linkage. On the 600MW Jharkhand project, CESC has begun some work on captive power but is facing land acquisition issues.
- **Acquired Resource Generation Ltd (Australia):** CESC has taken a controlling stake in RGL for 600MT to 1bn tonnes of coal in South Africa to hedge itself against any volatility of coal availability for its projects in India. Mining is expected to begin in 2013 and has a formula-based pricing.
- **Retail business losses reducing:** The management is working hard at reducing losses in the retail businesses – shutting unviable stores and focusing on large-format stores (e.g., hyper stores) to ~50% of total area. The company is also boosting back-end systems, trimming marketing spend, and reducing fixed costs by renegotiating lease rentals. It is also strategically focusing on large-format stores and high-margin verticals like private labels. Overall sales increased to Rs983/ sqft in September 2010, compared with Rs758/ sqft in September 2009. Higher revenues and various cost saving measures resulted in store EBITDA/ sqft turning positive in June 2010. CESC expects losses to reduce to Rs2bn in FY11 from Rs3bn in FY10. To reduce losses further, it would need to add more stores and funding the same through internal accruals as well as seek external funding.
- **Attractively valued; maintain Outperformer:** CESC is pursuing growth at its core power business through various power projects, which are steadily progressing. Apart from the acquisition of a 600MW merchant power plant (Chandrapur, Dhariwal), CESC is developing a 1,000MW merchant power project in Jharkhand. It has been jointly awarded a coal mine of 110m tonnes (CESC's share) which would ensure fuel supply and thereby profitability of the plant. Financial closure has been achieved for the 600MW Haldia power plant and ordering is under way. The retail business, which is still a drag on shareholder value, is being strategically modified to help it break even. The company is also looking at strategic partners or fund raising for the retail business. The stock currently trades at 7.5x FY11E earnings and 0.9x FY11E P/BV. We maintain our Outperformer rating on the stock.

Key financials

As on 31 Mar	FY08	FY09	FY10	FY11E	FY12E
Net sales (Rs m)	27,750	30,313	32,910	40,658	43,066
Adj. net profit (Rs m)	3,553	4,022	4,330	4,739	5,180
Shares in issue (m)	126	126	126	126	126
Adj. EPS (Rs)	28.3	32.0	34.5	37.7	41.3
% change	*(20.0)*	*13.2*	*7.7*	*9.5*	*9.3*
PE (x)	9.6	8.5	7.9	7.2	6.6
Price/ Book (x)	1.1	1.0	0.9	0.8	0.8
EV/ EBITDA (x)	7.3	7.4	7.8	6.2	6.0
RoE (%)	14.3	12.6	12.2	12.2	12.1
RoCE (%)	8.8	8.0	8.2	10.2	10.4

Media

DEN NETWORKS — OUTPERFORMER (RS143, MCAP: RS18.7BN / US$415M)

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- Promoted by Sameer Manchanda, DEN Networks forayed into cable distribution in late 2007. An aggressive management and US$65m invested by IL&FS and EMSAF have helped DEN cover significant ground within a short span of time via acquisitions. DEN has emerged as one of the fastest growing MSOs with a reach of ~10m homes and 1.3m paying homes.
- **Star-DEN JV:** In January 2008, DEN entered into the syndication business through a 50:50 JV with Star Network. The JV is an aggregator and distributor of 29 channels (Star Network and NDTV Group channels among others) across India, Nepal and Bhutan on analogue cable, digital cable as also the DTH platform. Being part of one of the largest MSOs, Star-DEN JV is better placed to ensure higher collections from the cable industry. For DEN, the deal also offers stability and higher returns at low capital involvement.
- **Digitization – the way forward:** Having acquired critical mass (reach of 10m+ and a 1.3m paying subscriber base) and raised Rs3.6bn of public equity, DEN's focus is shifting from 'customer acquisition' to 'digitization' and 'monetization'. While digitization would reduce the risk of losing LCOs (or subscribers), monetization would happen through higher declaration rather than ARPU growth. DEN has recently raised Rs3.6bn through public issuance. These funds are planned to be largely utilized for upgrading the existing infrastructure as also for digitization.
- At the end of Q2FY11, DEN had a digital subscriber base of 425,000. It expects the pace of digitization to intensify hereon and is currently estimated to be adding 50,000+ digital subscribers per month. It is targeting to add 1m digital subscribers annually. As digitization gathers momentum, declaration levels would improve (currently at <15%) and, thereby, underpin strong growth in profitability for DEN.
- **Regulatory push towards digitization:** In a major positive for the Indian TV distribution space, the I&B Ministry has given its approval for the TRAI recommendations announced earlier and proposed a revised schedule for digitization in the country. In August 2010, TRAI had announced key recommendations for the Indian TV distribution space, including a sunset date of December 2013 for complete migration from analogue to digital TV distribution services. The I&B Ministry has written to TRAI proposing a revised schedule for the same – indicating a sunset date of March 2015 for the country. The regulatory push towards digitization in the country could potentially underpin faster growth in the overall TV distribution industry. Cabinet approval is the final step for these proposals to get implemented and is likely in the next three months.

Key financials

As on 31 March	FY08	FY09	FY10	FY11E	FY12E
Net sales (Rs m)	826	7,122	9,191	11,194	14,407
Adj. net profit (Rs m)	(240)	(151)	303	459	905
Shares in issue (m)	18	18	130	130	130
Adj. EPS (Rs)	(13.2)	(8.3)	2.3	3.5	6.9
% change	-	*(36.9)*	*(127.8)*	*51.6*	*97.2*
PE (x)	n/a	n/a	61.7	40.7	20.6
Price/ Book (x)	1.3	1.1	2.5	2.3	1.9
EV/ EBITDA (x)	(8.6)	62.9	20.2	12.2	7.5
RoE (%)	(24.6)	(7.1)	6.1	5.8	10.2
RoCE (%)	(22.6)	(4.3)	8.8	10.2	17.8

Note: Prices as on 9th February 2011

Media

DISH TV

OUTPERFORMER (RS57, MCAP: RS60BN / US$1.3BN)

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- Dish TV, promoted by Essel Group, has been a DTH pioneer in India. Having commenced operations in 2005, the company already had a 1.5m subscriber base before competition from Tata Sky (launched in 2006). As of 31 December 2010, Dish TV had a gross subscriber base of 9.4m and a net subscriber base of 7.7m.
- **DTH industry – strong momentum:** The DTH industry in India has shown strong growth and currently forms 30% of the C&S households in the country (at 30m subscribers). The industry essentially is a six-player market in which Dish TV leads with a 31% market share, followed by Tata Sky (20%), Sun Direct (17%), Bharti Airtel (16%), Reliance (9%) and Videocon (7%).
- **Strong performance:** Dish TV, the industry pioneer, has maintained its leadership position in spite of intense competition by heavyweights. It has witnessed strong subscriber growth and added 1m+ subscribers in Q3FY11. It added 310,000 subscribers in January and expects to add 1m subscribers in Q4FY11. The management is also focused on improving ARPUs, which currently stand at Rs142. Accordingly, Dish TV has stopped offering the base package to new subscribers and has increased prices across packages by 10%.
- **Economics to improve:** Dish TV's business model enjoys a superior operating leverage, with its key cost component – content cost – being fixed. Dish TV has entered into fixed fee deals with most broadcasters and is thereby witnessing an improvement in profitability as the subscriber base widens. Over 30% of other operating costs like transmission cost, transponder charges, advertising cost, etc., remain relatively fixed. Subscriber acquisition costs (SAC) currently stand at ~Rs2150 and, with competition remaining firm in the DTH industry, the management expects SAC to remain at current levels in the near term. Given the strong pace of subscriber additions and operating leverage in the business, Dish TV is expected to achieve PAT breakeven in H2FY12.
- **Regulatory push towards digitization:** In a major positive for the Indian TV distribution space, the I&B Ministry has given its approval for the TRAI recommendations announced earlier and proposed a revised schedule for digitization in the country. In August 2010, TRAI had announced key recommendations for the Indian TV distribution space, including a sunset date of December 2013 for complete migration from analogue to digital TV distribution services. The I&B Ministry has written to TRAI proposing a revised schedule for the same – indicating a sunset date of March 2015 for the country. The regulatory push towards digitization in the country could potentially underpin faster growth in the overall TV distribution industry. Cabinet approval is the final step for these proposals to get implemented and is likely in the next three months.

Key financials

As on 31 Mar	FY08	FY09	FY10	FY11E	FY12E
Net sales (Rs m)	4,122	7,375	10,853	14,265	20,573
Adj. net profit (Rs m)	(4,140)	(4,893)	(2,612)	(1,877)	106
Shares in issue (m)	858	948	1,065	1,065	1,065
Adj. EPS (Rs)	(4.8)	(5.2)	(2.5)	(1.8)	0.1
% change	n/a	n/a	n/a	n/a	n/a
PE (x)	(11.7)	(10.9)	(23.0)	(32.1)	568.7
Price/ Book (x)	(10.3)	(8.3)	15.4	29.5	28.0
EV/ EBITDA (x)	(25.1)	(34.1)	65.8	26.1	10.8
RoE (%)	156.9	87.5	204.5	(63.0)	5.1
RoCE (%)	(339.2)	(141.6)	(21.1)	(10.0)	5.8

Note: Prices as on 7th February 2011

IT Services

eClerx

UNRATED (RS610, MCAP: RS8.1BN / US$179MN)

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- Incorporated in 2000, eClerx is a leading player in India's growing Knowledge Process Outsourcing (KPO) space. The company enjoys a strong position in certain high-opportunity segments like data analytics, data management and customized process improvement solutions. It provides business solutions to global enterprise clients by leveraging its cost-effective combination of people, process and technology. eClerx's growth has been aided by its ability to forge multi-year relationships with marquee clients.
- **Business units:** eClerx provides service offerings in two key business units: a) Financial Services, and b) Sales and Marketing Support.
- **Size, employee strength and infrastructure:** eClerx clocked revenues of Rs2.6bn in FY10. It has 3,600 employees working across five delivery centers in Mumbai and Pune, of which 600 are sales and management personnel and the rest execution resources (equally split between the two business units). Attrition rate has been 30-35% over the past several years, helping the company keep average wage costs low. eClerx has 3,200 seats which can accommodate 4,800 employees. About 60% of its revenues are delivered from SEZ and the rest from STPI locations.
- **Clients and related details:** The company has 50 active clients, with 15-20 in financial services and 30-35 in sales and marketing support business unit. It has ~500 engagements across its clientele, which includes more than 20 Fortune 500 companies. The top5 clients accounted for ~86% of revenues in Q3FY11.
- **Client contacts and business model:** Most of eClerx's client relationships are governed by MSA (master service agreements). About 80% of the company's contracts are 2-3 year rolling contracts (usually extended at the end of the contract life) and have a largely fixed billing rate of ~US$30,000pa. The billing rate has historically been revised only for a few key customers, led by inflation and forex changes. About 90% of the engagements are time and material based, with the rest being fixed-price projects.
- **Cost structure and EBIT margins:** Employee cost is a major cost component for eClerx, accounting for ~44% of revenues (including ~14% onsite wage bill). G&A expenses (ex employee costs) form ~13% of revenues, while S&M (ex employee costs) expenses account for ~5%. Depreciation is ~3% of revenues, leading to recurring EBIT margin of 32-35%.
- **M&A:** eClerx acquired Ingentica Group in 2007 for US$3m. Target company had revenue run rate of ~US$2m and the key driver for acquisition was company's seven blue-chip clients. eClerx has not acquired any other company since then, but plans to do so in the coming 12-18 months. It is looking to acquire non-voice BPO companies, with revenues in the range of US$15m-40m. The company recently got Board approval to raise Rs10bn mainly for funding acquisition.
- **Hedge:** 75% of company's revenues are US$ denominated, with a 10-15% natural hedge from USD denominated costs. eClerx employs 18-month rolling hedges.
- **Key differentiators:** eClerx provides highly specialized services based on deep domain expertise in target industries. Its strength lies in technology and knowledge management, with a focus on simplifying the processes thereby reducing people dependency and the average employee cost for moderately complex activities.

Key Financials

(Rs m)	FY07	FY08	FY09	FY10	9MFY11
Revenue	861	1,217	1,973	2,570	2,466
Growth (%)	*82*	*41*	*62*	*30*	-
EBITDA	432	492	724	844	1,062
EBITDA margin (%)	*50*	*40*	*37*	*33*	*43*
EBIT	399	447	650	774	999
EBIT margin (%)	*46*	*37*	*33*	*30*	*41*
Net profit	**397**	**446**	**618**	**735**	**929**
Growth (%)	*62*	*12*	*39*	*19*	-
Fully diluted shares	23	26	29	30	30
EPS - fully diluted (Rs)	**17.29**	**16.91**	**21.67**	**24.76**	**30.91**
Growth (%)	*8*	*(2)*	*28*	*14*	-
Valuations					
PE (Price Rs610)	35.3	36.1	28.2	24.6	-

Source: Company

Auto

ESCORTS

OUTPERFORMER (RS105, MCAP: RS10BN / US$213M)

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- Escorts (ESC), a Nanda Group company, has in the past few years undertaken major business restructuring by exiting businesses like telecom, hospitals, etc.. It is now focused on a business model revolving around agri machinery (Rs25bn of sales in FY10) and construction equipment (Rs5.7bn), besides operating in railway equipment and auto ancillaries. In the process, ESC has also addressed concerns over its extremely leveraged balance sheet.
- **Tractor business on a structural upcycle:** ESC's agri machinery business is witnessing strong growth momentum, with underlying volumes growing by 15-20%. Given the need for mechanization of farm land, increasing need for productivity enhancement, higher minimum support price, and expensive farm labor post NREGA, the tractor industry (with annual sales of over 0.4m units) is poised for 20% growth in the foreseeable future. ESC would derive growth through increased distribution and new launches for paddy cultivation and in the higher horsepower segment. ESC sold nearly 60000 units in FY10 and is expected to sell 69000 in FY11 (21000 units sold in the first four months of FY11). Its current capacity in the tractors business is 90000-100000 units.
- **Strong growth in construction equipment; railway equipment and ancillaries subdued:** The construction equipment business has been clocking high growth of 20%+, driven by growth in the Backhoe Loader segment and new launches. We see growth potential in the construction equipment business given increasing construction activities. However, the railway equipment business remains subdued on account of a slowdown in government spending. In the auto ancillary business, ESC has hired a senior official of Amtek Auto and is also in talks with a few OEMs. The business would continue to be in investment mode over the next couple of years.
- **Margins to remain subdued:** Increasing commodity prices and adverse mix have impacted ESC's operating margins in recent times despite having operating leverage. In the tractor business, margins have been under pressure in the past quarter as the increase in steel, aluminum and rubber prices have been far ahead of the company's price increases in September. ESC affected a price increase of 2-3% in February to offset the impact of commodity prices. However, we expect margins in the tractor business to decrease yoy. Also, continued investment losses in the auto ancillary business, degrowth in the high-margin railway equipment business, and faster growth in the low-margin construction equipment business would keep margins under pressure. We expect a 40bp erosion in FY11.
- **Structurally positive, near-term overhangs:** Two of ESC's largest businesses, tractors and construction equipment, promise to clock high double-digit growth in the next few years. However, the past two quarters of margin disappointment (higher overheads in Q4FY10 and lower operating margins in Q1FY11) would be a major overhang on the stock until margins improve in the coming quarters.

Key financials

As on 30 Sep	FY08	FY09	FY10	FY11E	FY12E
Net sales (Rs m)	27,638	26,639	33,783	41,562	47,791
Adj. net profit (Rs m)	(351)	588	1,260	1,476	1,999
Shares in issue (m)	80	80	92	105	105
Adj. EPS (Rs)	(4.4)	7.3	13.7	14.0	19.0
% change	n/a	n/a	87.3	2.6	35.4
PE (x)	(24.0)	14.3	7.6	7.5	5.5
Price/ Book (x)	0.9	0.6	0.6	0.6	0.6
EV/ EBITDA (x)	-	-	-	-	-
RoE (%)	(3.7)	4.9	8.0	8.4	10.5
RoCE (%)	3.1	7.9	9.1	10.1	12.8

Pharma

ESS DEE ALUMINIUM — UNRATED (RS427, MCAP: RS13.7BN / US$303.6M)

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- Ess Dee Aluminium Ltd. (EDAL) is India's premier manufacturer of aluminium foil and foil products catering to the pharmaceutical and FMCG sectors. It derives 70% of its revenues from the pharma sector and the rest from FMCG.
- Revenues and EBITDA witnessed 64% and 35% CAGR over the past four years on the back of aggressive capacity additions (acquired India Foils Ltd. recently) and buoyant offtake from end-user industries (given limited competition in domestic markets).
- EDAL's product range can be broadly classified into aluminum-foil-based flexible packaging laminates and PVC-based thermo forming products, including aluminium strip foil, blister pack foil, PVC and PVdC coated film, laminates and cold forming Alu-Alu packaging products. The company supplies these products to various reputed domestic and international pharmaceutical and FMCG companies based in India.
- Raw material costs account for 86% of EDAL's revenues. EDAL imports aluminium from the Gulf Aluminium Rolling Mill Co in Bahrain every quarter at market prices. It manages volatility in gross margins by maintaining low inventory days and any gain/ loss in inventory is passed on to customers (packaging accounts for a small amount of the final product price), which helps absorb higher raw material prices by producers.
- EDAL's business model is characterized by the following:
  - Hub & spoke model – the company remains in close proximity to the customer, ensuring lowest lead time/ freight cost
  - Ability to execute a wide range of order sizes
  - Strong designing capability helps provide clients with appropriate solutions
  - Comfortable with long receivable cycles, which eliminates competition from smaller players.

Key financials

As on 31 March	FY07	FY08	FY09	FY10
Net sales (Rs m)	914	1,082	1,237	1,552
Adj. net profit (Rs m)	122	141	91	209
Shares in issue (m)	32	32	32	32
Adj. EPS (Rs)	3.8	4.4	2.9	6.5
% change	*n.a*	*16%*	*-35%*	*129%*
PE (x)	112.0	96.9	149.8	65.4
Price/ Book (x)	3.27	3.99	1.26	2.22
EV/ EBITDA (x)	15.8	17.7	13.0	8.2
RoE (%)	n.a	22.6	25.7	25.3

Education

EVERONN — OUTPERFORMER (RS500, MCAP: RS9.5BN / US$211M)

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- **VITELS – picking up momentum:** VITELS had in its fold 1195 schools, 1812 colleges and 54 retail centres as of end-Q2FY11. In schools, while new additions are being done at an average of four classrooms per school, Everonn (EEDU) is also adding classrooms in existing schools. Thus the average number of classrooms per school is witnessing an uptrend and now stands at 2.5 against 2.2 in Q1FY11.
- **ICT – cherry-picking contracts:** With the ICT segment yielding sub-optimal profits on the back of LI bidding as also high debtor days, the management has been cautious in bidding for contracts. Selective bids by the management have helped maintain EBITDA margins at 40-45% in the segment.
- **Entry into K-12 and HE**: The management is building its capabilities and tie-ups in its more recent initiative – 'Educating India'. The initiative marks EEDU's foray in the K-12 and higher education segments as 'facilitator, aggregator and manager'. While EEDU does not plan to own any institutes, it expects to get 7% of the total project cost in addition to a management fee for managing the institutions. EEDU is looking to start 6-7 B-schools (under the brand GSB – Global School of Business) and 10 K-12 schools in the next academic year (under the brand KenBridge schools). A model B-school in Chennai is currently under operation.
- **SKIL categorized as a co-promoter**: In October 2010, SKIL was categorized as co-promoter in EEDU, which issued 4m optionally convertible debentures to SKIL at Rs520 per share. This triggered an open offer of Rs587 per share, which was completed on 27 November 2010 and led to SKIL acquiring 88,500 shares in EEDU. The deal between EEDU and SKIL was so structured that post the open offer SKIL's equity holding in the company would be lower than that of the exiting promoter, P Kishore. As part of this agreement, EEDU has now issued 3.91m shares to SKIL and redeemed the remaining OCDs (value of Rs46m). Post this transaction, SKIL's stake in the company stands at 21.02% and the existing promoter group's holding has come down to 21.4% (from 26.9% earlier).
- **Creating a strong Board:** EEDU has inducted key industry veterans on its Board, including Tata Group veteran J J Irani and Dr M S Vijay Kumar, senior associate dean at the Massachusetts Institute of Technology.

Key financials

As on 31 March	FY08	FY09	FY10	FY11E	FY12E
Net sales (Rs m)	916	1,447	2,935	4,033	4,878
Adj. net profit (Rs m)	138	221	454	628	832
Shares in issue (m)	13.8	15.1	15.1	19.0	19.0
Adj. EPS (Rs)	10.0	14.6	30.1	33.0	43.7
% change	-	*46.2*	*105.6*	*9.7*	*32.6*
PE (x)	50.0	34.2	16.6	15.2	11.4
Price/ Book (x)	7.2	3.6	3.0	3.1	2.5
EV/ EBITDA (x)	20.9	14.9	7.9	6.3	4.7
RoE (%)	20.8	14.4	19.4	22.4	24.1
RoCE (%)	22.1	16.9	24.2	25.3	25.3

Note: Prices as on 9th February 2011

Exchanges

FINANCIAL TECHNOLOGIES

RATING UNDER REVIEW (RS726, MCAP: RS33BN / US$736M)

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- **Financial Technologies** (FTIL) is Asia's largest exchange conglomerate, with five domestic exchanges (across commodities, power, spot and currencies) and five international exchanges in under-penetrated regions (Dubai, Singapore, Bahrain, Africa and Mauritius). FTIL also operates six ecosystem ventures flanking the exchanges business across the agri warehousing, mobile trading and information dissemination spaces. FTIL stands to be the only listed proxy to the potential US$10trn Indian exchange market.
- **Domestic exchanges – in scale-up mode:** FTIL entered the Indian exchange space with MCX (India's largest commodity exchange) in 2003. MCX today leads the US$2.5trn+ commodities market with an 85% market share. Given the success of MCX, FTIL launched four more niche domestic exchanges in segments like spot (National Spot Exchange), power (Indian Energy Exchange), currencies (MCX-Stock Exchange) and forex trading (IBS Forex). While all these exchanges are a year old, MCX-SX has particularly garnered strong traction and clocks an average daily turnover of US$3bn+. With respect to the other three, FTIL enjoys a market share of 90%+, with NSE-promoted exchanges being the key competitors. However, these exchanges are yet to garner strong liquidity.
- **International exchanges – in potentially under-penetrated geographies:** FTIL currently operates exchanges in four international markets, including Dubai (DGCX), Singapore (Singapore Mercantile Exchange – SMX), Mauritius (Global Board of Trade – GBOT) and Bahrain (Bahrain Financial Exchange – BFX). Excluding DGCX, the other three are multi-asset exchanges, and, being the first in the region, would enjoy first-mover advantage. FTIL is also looking to set up an exchange in Botswana to cater to the African region. While the opportunity landscape on the international front looks promising, execution will be the key monitorable.
- **Entry into Indian equity markets:** MCX-SX, which currently operates in the currency derivatives space, has the license to operate the third equity exchange of the country. SEBI has rejected MCX-SX's application for starting trading in new products like equities, interest rate and debt. The rejection was based on two main grounds: 1) FTIL and MCX are persons acting in concert and, hence, should be considered as a single promoter. This implies that the FT Group (MCX + FTIL) cannot own more than 5% in aggregate. Currently, FTIL and MCX each own 5% equity interest in MCX-SX. 2) SEBI has alleged that concentration of ownership in the form of warrants is not right in 'spirit'. FTIL has challenged SEBI's order in the Bombay High Court.

Key financials

As on 31 March	FY08	FY09	FY10	FY11E	FY12E
Net sales (Rs m)	1,376	3,343	3,070	3,396	3,415
Adj. net profit (Rs m)	9,612	3,686	3,444	2,346	1,713
Shares in issue (m)	46	46	46	46	46
Adj. EPS (Rs)	209.5	80.3	75.1	51.1	37.3
% change	*833.3*	*(61.7)*	*(6.6)*	*(31.9)*	*(27.0)*
PE (x)	3.5	9.0	9.7	14.2	19.5
Price/ Book (x)	2.3	1.9	1.6	1.5	1.4
EV/ EBITDA (x)	56.1	16.0	17.0	17.3	18.4
RoE (%)	115.3	22.9	18.1	11.0	7.5
RoCE (%)	3.3	7.4	5.5	5.0	4.3

Note: Prices as on 9th February 2011

Pharma

FORTIS HEALTHCARE — OUTPERFORMER (RS145, MCAP: RS58.9BN / US$1.31BN)

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- FHL is India's second largest (listed) healthcare player in the secondary/ tertiary segment, with 53 healthcare delivery facilities on track to take total installed capacity to >8,000 beds by FY13. FHL's existing bed count stands at 6033 beds, of which 32% are greenfield, 38% brownfield and 29% managed (under O&M).
- FHL's major expansion plans are progressing on schedule, with Phase 1 of the Gurgaon facility (450 beds) expected to be commissioned by Q1FY12. FHL plans to commission 75, 200 and 234 beds at Ludhiana I and II and Mulund, Mumbai, respectively by Q4FY12.
- The company has doubled its operational bed capacity in two years by aggressive inorganic growth and has a good track record of successfully integrating acquired assets (Escorts Delhi, Fortis Malar, etc). It continues to embrace innovative strategies to reduce resource intensity (land, employees, equipment, etc) and free up capital to fund expansion.
- FHL has significantly improved operational parameters in the past two years. ALOS has reduced from 7 days in FY07 to 5.2 now, while ARPOB has increased from Rs6.7m to Rs10.4m.
- It uses the hub & spoke model to reinforce its presence in existing regions and enter new geographies. As part of the strategy, FHL seeks to establish super specialty "centres of excellence (COE)" in key cities in a region ("hub for the region") and then build a series of feeder hospitals across the region to feed these high-end hospitals.
- The promoters remain keen on expanding the company's global reach by acquiring assets at the right price. FHL (listed entity) would focus on expanding scale at home, while promoters' ambition of gaining a global footprint would be routed through their own holding company.

Key Financials

As on 31 March	FY08	FY09	FY10	FY11E	FY12E
Net sales (Rs m)	5,479	6,589	9,872	14,836	21,316
Adj. net profit (Rs m)	(556)	145	695	1,491	2,223
Shares in issue (m)	406	406	406	406	406
Adj. EPS (Rs)	(1.4)	0.4	1.7	3.7	5.5
% growth	*(42.1)*	*(126.1)*	*379.0*	*114.5*	*49.1*
PER (x)	n/a	405.7	84.7	39.5	26.5
Price/Book (x)	5.1	5.4	3.2	1.8	1.6
EV/EBITDA (x)	101.5	55.4	52.9	25.4	15.0
RoE (%)	(7.2)	1.30	4.72	5.71	6.24
RoCE (%)	1.2	4.12	2.90	1.96	4.73

Telecom VAS

GEODESIC LTD

UNRATED (RS70, MCAP: RS6.3BN / US$138MN)

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- Incorporated in 1999, Geodesic is a software-focused company offering unified communications tools related to CRM applications for enterprises. One of its principal products, Geoamida, a biometric reader, is being used in several eGovernance and financial inclusion projects. It has also developed social networking, voice messaging and entertainment applications for retail subscribers. Geodesic's growth has been aided by its ability to develop innovative products for various consumer segments. The advent of 3G services and eGovernance projects in India are near-term catalysts of growth.
- **Business segments:** Geodesic develops products or applications for two customer segments: I) Enterprise (including government bodies), and ii) retail. With an employee base of 700+, it serves 148 enterprise customers across 12 countries in addition to the retail segment. Retail mix is expected to go up from 14% to 25% by FY13.
- **Enterprise communication tool:** A host of financial services companies in India and abroad like CLSA HK, IDFC, Edelweiss, Daiwa, IIFL, Samsung Investments, etc, use Geodesic's software and services based on Spyder technologies. This unified communication tool embedded with the CRM product helps enterprises to analyze call logs and saves communication costs by up to 40%.
- **Mundu platform and other offerings:** Geodesic launched the 'mundu' series of products to utilize the mobile communication platform: 1) 'mundu' IM, an instant messenger suite; 2) 'mundu' SMS, with which the company delivers ~400m SMS/year; 3) 'mundu' Radio (100+ channels) and mundu.TV (subscription-based mobile TV); and 4) 'Spokn', which is a mobile application for voice messaging and Internet telephony on the go, allows users to retain international numbers (in 8 countries currently). All calls in India pass through Bharti Airtel's network, while the company has tie-ups with six international operators for its global services.
- **Geoamida – the biometric device:** Various versions of Geoamida – the biometric device developed based on the Simputer technology, are being used in eGovernance (UID, PDS), financial inclusion and transportation (traffic police, parking management). The estimated demand for the device is 4m over the next 2-3 years. Each device is priced at ~Rs20,000, with an estimated EBITDA margin of ~35%.
- **Strong growth to continue:** Geodesic reported FY10 revenues of Rs6.4bn with an operating margin of 43% (Rs2.8bn) and net profit margin of 35% (Rs2.2bn). H1FY11 revenue and net profit were Rs4.1bn (up 30% yoy) and Rs1.6bn (41% yoy) respectively. Geodesic is confident about maintaining 30-35% growth over the next 2-3 years with margins of 52-55%. It has Rs9bn in cash reserves, as against outstanding FCCBs of Rs6.7bn.

Key Financials

(Rs m)	FY07	FY08	FY09	FY10	1HFY11
Revenue (Rs m)	1,681	3,164	6,530	6,374	4,118
Growth (%)	*73*	*88*	*106*	*(2)*	*30*
EBITDA (Rs m)	1,042	1,927	3,654	3,538	2,095
EBITDA margin (%)	*62*	*61*	*56*	*56*	*51*
EBIT (Rs m)	834	1,591	3,113	2,736	1,844
EBIT margin (%)	*50*	*50*	*48*	*43*	*45*
Net profit (Rs m)	**898**	**1,486**	**2,643**	**2,237**	**1,644**
Growth (%)	*123*	*65*	*78*	*(15)*	*42*
Fully diluted shares	90.09	92.03	99.30	92.74	92.04
EPS - fully diluted (Rs)	**9.97**	**16.15**	**26.62**	**24.12**	**17.86**
Growth (%)	35	62	65	(9)	43
Valuations					
PE (Price Rs70)	7.0	4.3	2.6	2.9	2.0

Source: Company, IDFC Securities Research

Pharma

GLENMARK — OUTPERFORMER (RS288, MCAP: RS78BN / US$1.7BN)

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- Glenmark saw lower-than-estimated growth in the US in Q2FY11 primarily due to withdrawal of Nitroglycerine and weak pick-up of some of newly launched products. However, its outlook for the market remains positive.
- The company remains confident of 25% yoy revenue growth in FY12 in the US due to these factors: 1) it expects full impact of recent product launches to be realized from Q4FY11; 2) guaranteed niche launches (e.g, Malarone in Q3CY10); and 3) visibility on the pipeline, which largely consists of niche products in segments like dermatology, hormones and Para IVs.
- Glenmark declined to divulge details on Tarka due to an ongoing litigation. It expects the judge's verdict on the double patenting issue over the next few weeks/ months, which should provide clarity.
- Glenmark received seven approvals in Q3FY11, including two tentative ones. It has maintained its earlier guidance for launching 13-15 ANDAs in FY11.
- **Non-US markets:** Glenmark's outlook remains positive, with growth primarily driven by its presence in the respiratory, dermatology and oncology segments.
- **SRM markets:** The company expects largely flat or marginally lower Q4FY11 sales due to a large prior-year base. Overall, the company is positive about clocking 20-25% annual growth in the segment going forward.
- **LatAm operations:** Glenmark expects 30-40% yoy revenue growth going forward on the back of an improvement in the Brazilian operations and incremental contribution from newer markets like Venezuela, Peru and Ecuador, boosted by the impact of a low base.
- Domestic operations saw a slew of product launches – 14 in 9MFY11. Glenmark has a field force of 2300 and expects to expand it in FY12. It has guided for 25% yoy revenue growth, with ~20% contributed by existing products and the rest by new launches. It continues to witness traction in key TAs like respiratory, dermatology, pain management, gynecology, CVS and diabetology.
- The company has guided for a capex of Rs3bn in FY11-12.
- Gross debt and cash position were Rs17.8bn and Rs1.12bn respectively as of December 2010. Net debt increased by Rs980m qoq to Rs16.7bn as of end-Q3FY11.
- The management indicated that the working capital cycle as of end-December 2010 was in line with levels in October 2010. Receivable days were 119 in October 2010, as against 155 in March 2010.
- R&D expenditure for 9MFY11 was Rs950m, or 4.5% of consolidated sales. R&D expenditure is likely to inch up as the company plans to initiate Phase IIb trials for as many as four NCEs, including GBR 500.

Key financials

As on 31 March	FY08	FY09	FY10	FY11E	FY12E
Net sales (Rs m)	19,783	21,160	25,244	30,439	34,877
Adj. net profit (Rs m)	6,303	3,104	3,310	4,939	5,201
Shares in issue (m)	252	271	271	271	271
Adj. EPS (Rs)	25.0	11.5	12.2	18.2	19.2
% change	*103.3*	*(54.1)*	*6.6*	*49.2*	*5.3*
PE (x)	11.5	25.1	23.6	15.8	15.0
Price/ Book (x)	4.8	4.9	3.3	2.8	2.3
EV/ EBITDA (x)	10.1	21.6	14.9	11.9	10.6
RoE (%)	57.1	19.9	16.7	19.0	16.9
RoCE (%)	33.8	11.0	12.9	14.7	14.9

Source: Company, IDFC Securities Research

Construction

HINDUSTAN CONSTRUCTION COMPANY — OUTPERFORMER (RS32, MCAP: RS20BN / US$433M)

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- HCC's execution has bee affected by sluggish order intake in H1FY11 and slow progress of projects in Andhra Pradesh and Jammu & Kashmir.
- Execution of the J&K projects (mainly Kishanganga HEP) has lately improved with significant improvement in working conditions. HCC has also commenced work on the NH-34 road project in West Bengal.
- The company expects order flows of Rs50bn-60bn in FY11, with orders worth Rs27.7bn bagged in 9MFY11. It is an L1 bidder for orders worth Rs15bn.
- HCC's debt has increased due to high working capital levels, which in turn is a result of receivables/ claims worth Rs15bn-16bn.
- As regards the Lavasa project, HCC is in the process of submitting details required by the MoEF. The next hearing is on 10 March 2011.
- HCC recently signed an agreement with VINCI Construction Grands Projects (VINCI) for cooperation in the power, water, transportation and infrastructure sectors. The partners are targeting the proposed 2x 1650MW EPR nuclear reactor of Areva, France, in Jaitapur in Ratnagiri, Maharashtra. VINCI is already engaged in the development of the EPR programme with Areva France.

Key financials (Standalone)*

As on 31 Mar	FY08	FY09	FY10	FY11E	FY12E
Net sales (Rs m)	30,820	33,138	36,292	41,909	51,129
Adj. net profit (Rs m)	724	760	957	880	1,011
Shares in issue (m)	512	512	606	606	606
Adj. EPS (Rs)	1.4	1.5	1.6	1.5	1.7
% change	*17.4*	*4.9*	*6.4*	*(8.0)*	*15.0*
PE (x)*	22.9	21.8	20.5	22.3	19.4
Price/ Book (x)*	1.7	1.6	1.3	1.3	1.2
EV/ EBITDA (x)*	8.0	8.0	8.8	8.2	8.3
RoE (%)	7.6	7.6	7.6	5.7	6.5
RoCE (%)	9.8	9.9	8.6	8.2	9.3

** - valuations not adjusted for Rs38/share value of Lavasa, real estate and BOT assets*

Financials

INDUSIND BANK — OUTPERFORMER (RS210, MCAP: RS86BN / US$1.9BN)

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- **Margins to sustain:** IndusInd Bank's management is confident of maintaining current margin levels (3.6%) over the next couple of quarters. Cost of funds has been on an uptrend, but the bank has been successfully passing it on. Healthy traction in CASA deposits has also cushioned the impact on margins. The management expects asset re-pricing to gain pace in Q4FY11, which should support margins in the near term. Also, the bank is targeting a NIM of ~4% over the next 10 quarters, catalyzed by an expansion in CASA ratio.
- **Branch rollout to aid CASA accretion:** IndusInd intends to maintain a healthy flow of CASA deposits to fortify the bank's liability base. It has added 48 branches this fiscal year (20 in Q3FY11). More branches are likely to be rolled out in Q4FY11, taking the total to ~300 by March 2011. These are expected to significantly contribute to CASA in FY12. The bank expects CASA ratio to steadily scale up to ~35% over the next 10 quarters and remain steady thereafter.
- **Loan growth to remain robust**: The management expects loan growth to remain robust in the near term. Consumer loans are expected to outpace corporate credit over the next couple of quarters. Also, the bank has diversified to fill the missing pieces in its product profile, which should incrementally support growth. New products include high-end credit cards, personal loans and loans against property.
- **Vehicle loans to be financed by CASA and long-term borrowings:** Over the next couple of years, the bank aims to finance vehicle loan book (~45% of total advances) through consumer CASA and long-term funding sources. Meanwhile, corporate loans, which have relatively short tenures, are to be funded by corporate liabilities (deposits and borrowings). This, according to the management, would help manage asset liability better and support NIMs in an adverse interest rate environment.
- **Corporate segment to drive fee income:** The management sees significant potential to scale up fee income led by corporate fees. Trade and remittances are likely to form a significant portion of fee income going forward owing to increased focus on cross-sales. Investment banking fees (primarily debt syndication, debt structuring and advisory) are expected to lead the traction. The bank is tapping clients with which it has established fund-based relationships.
- **Upside in RoA:** Increasing fee income (especially corporate fee income and investment banking fees) and margins are expected to further increase the banks RoA, which grew 10bp qoq to 1.5% in Q3FY11.

Key financials

Year to 31 March	2009	2010	2011E	2012E	2013E
Net profit (Rs m)	682	3,503	5,767	7,854	10,331
yoy growth (%)	*85.3*	*136.1*	*64.6*	*36.2*	*31.5*
Shares in issue (mn)	355.2	410.6	465.0	465.0	465.0
EPS (Rs)	2.1	9.0	12.4	16.9	22.2
EPS growth (%)	68.3	104.8	37.8	36.2	31.5
PE (x)	98.3	23.3	16.9	12.4	9.4
Book value (Rs/share)	33.0	52.7	81.5	94.2	110.8
Adjusted Book value (Rs/share)	28	52	83	98	116
P/ Adj Book (x)	7.6	4.0	2.5	2.1	1.8
RONW (%)	7.1	19.5	19.4	19.2	21.7

Source: IDFC Securities, Price as on 9th Feb 2011

IT Services

INFINITE COMPUTER — OUTPERFORMER (RS158, MCAP: RS6.9BN / US$153MN)

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- Infinite was incorporated in 1999 and is a mid-tier IT services provider focused on acquiring large clients (offering high revenue potential) and mining them deeper. It has successfully positioned itself as a credible Tier2 vendor and co-exists with Tier1 vendors in a few of its key accounts. The company has grown faster than comparable peers due to its strategy of acquiring large clients.
- **Business on track:** The management highlighted that business is growing in line with expectations. It expects the company to clock revenues of US$190m-195m in FY11 (+35-38% yoy) and sees a much higher run rate in FY12 led by recent Motorola, iYogi and R-APDRP deals.
- **Motorola deal:** Infinite acquired SMS and MMS messaging IP from Motorola under a revenue-share deal in March 2010. As part of the agreement, it acquired a non-transferable license of Motorola's messaging solutions for 10 years. In the first year, Infinite's share of revenues from this platform will be 30% and increase to 70% from the second year. The company expects to generate ~US$20m in FY11 and ~US$40m in FY12. The deal is expected to be a key growth driver for the company's top line. It would also boost margins as it operates at margins higher than the company's average levels.
- **iYogi deal:** Infinite entered into a three-year strategic alliance with iYogi in April 2010 to provide IMS services. Infinite uses iYogi's global delivery platform, iMantra, to seamlessly extend L-1, L-2 and L-3 helpdesk support to iYogi's customers across multiple geographies, including the US, Canada, the United Kingdom and Australia. Infinite employs ~1,200 people on this platform and expects the peak strength to be 1,300-1,400. Since most of these employees were under a three-month training period, the company saw minimal revenue contribution from this platform. However, it expects revenues to pick up from April 2011. The deal is expected to contribute ~US$5m in FY11 and US$10m-12m in FY12, with operating margins higher than the company average.
- **R-APDRP deal:** In October 2010, Infinite won a Rs1.3bn contract from the Uttarakhand state government for R-APDRP implementation. This deal has two components – implementation, expected to be the major revenue contributor, and follow-up support. The implementation part is running behind schedule and is expected to complete by March 2012. Revenue from this deal is expected to be lumpy, while operating margins have been below the company's average. While the company has bid for other states' APDRP projects as well, it has not won any because of its stringent margin constraints.
- **Supply side**: The company plans to hire 500-600 employees in FY12. Though the current attrition level (~12%) is at a historical high for Infinite, it is still below current industry levels. Given the strong-demand led environment and industry-wide high attrition, company is likely to give 15-20% wage hikes in FY12.
- **Our view:** We expect Infinite Computer to grow faster than its mid-cap peers over the coming quarters as the Motorola, iYogi and R-APDRP projects are in ramp-up mode. The stock currently trades at inexpensive valuations of ~6x FY12E EPS; we have an Outperformer rating with 12-month price target of Rs260 (based on 10x avg. FY11-12E EPS). Infinite remains a key pick in the small-cap IT services space.

Key financials

As on 31 March	FY09	FY10	FY11E	FY12E	FY13E
Net sales (Rs m)	4,899	6,643	8,672	10,522	12,627
Adj. net profit (Rs m)	457	840	1,045	1,244	1,629
Shares in issue (m)	38	39	44	44	44
Adj. EPS (Rs)	12.0	21.4	23.7	28.2	36.9
% growth	126.5	78.8	10.8	18.8	31.0
PER (x)	13.2	7.4	6.7	5.6	4.3
Price/Book (x)	4.0	1.9	1.7	1.3	1.0
EV/EBITDA (x)	10.3	5.3	5.4	3.4	2.3
RoE (%)	34.6	35.0	28.2	26.1	26.3
RoCE (%)	34.6	38.8	31.6	32.9	32.9

Source: Company, IDFC Securities

IT Services

INFO EDGE — UNRATED (RS502, MCAP: RS22.6BN / US$498MN)

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- Incorporated in 1995, Info Edge is the country's leading online classifieds company in recruitment, matrimony, real estate, education and related services. The company enjoys a strong market position in its online recruitment portal, Naukri.com, and has successfully leveraged its expertise in the same to seek opportunities in other online classifieds areas. Spurred by improving economic conditions, increasing internet penetration, and changing demographics, the company expects to witness growth in all its segments.
- **Business segments:** The company's business broadly encompasses four online classifieds divisions: recruitment – Naukri.com; matrimonial – Jeevansathi.com; real estate – 99acres.com; education – Shiksha.com. It employs ~1,400 sales staff and has a nationwide coverage with ~48 branch offices across ~31 cities.
- **Recruitment business:** Info Edge derives ~85% of its revenues from online recruitment classifieds offerings – Naukri.com, Firstnaukri.com, Naukrigulf.com and related services offerings Quadrangle and Brijj.com. Naukri.com enjoys a dominant position in the Indian online recruitment space with ~60% traffic share. This business segment derives most of its revenues from job listing and resume database access facilities. It also earns revenues from jobseeker services, Google adsense, resume short-listing and screening. The company clocked ~Rs2bn revenue from this division in FY10. On the back of a strengthening recruitment environment led by an improving economic environment and strong hiring in various industries (especially IT services), the management expects this division to grow by ~30% in FY12. In the coming few quarters, the company expects to incur addition product development costs to counter competition from LinkedIn.com. Margins should, however, remain steady (at 40%+) as the increased cost would be offset by a decrease in advertisement-related spend.
- **Non-recruitment segment:** The company derives ~15% of its revenues largely from its offering in matrimony, real estate and education through Jeevansathi.com, 99acres.com, Allcheckdeals.com and Shiksha.com. Most of these non-recruitment businesses are still in the investment phase but have growth potential comparable to the recruitment business. Also, with lesser correlation to the economic environment, these business segments provide a hedge to the inherent cyclicality of the recruitment segment. 99acres.com is the market leader in real estate classifieds, while Jeevansathi.com is the third-largest behind Shaadi.com and Bharatmatrimony.com.
- **Capex plans:** Info Edge plans to incur a capital expenditure of Rs800m-850m over FY12-13. It is also looking to diversify into ecommerce-related platforms either directly or through an investee company as seen in Policybazaar.com, Meritnation.com and Zomato.com.

Key Financials

(Rs m)	FY07	FY08	FY09	FY10
Revenue	1,396	2,189	2,458	2,371
Growth (%)	69	57	12	(4)
EBITDA	372	645	662	625
EBITDA margin (%)	27	29	27	26
EBIT	326	590	591	560
EBIT margin (%)	23	27	24	24
Net profit	271	554	570	521
Growth (%)	104	105	3	(9)
Fully diluted shares	23.9	27.3	27.3	27.3
EPS - fully diluted (Rs)	11.31	20.31	20.89	19.08
Growth (%)	86	80	3	(9)
Valuations				
PE (Price Rs502)	**44.4**	**24.7**	**24.1**	**26.3**

Source: Company

Financials

ING VYSYA BANK — OUTPERFORMER (RS291, MCAP: RS35BN / US$777BN)

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- **Loan growth to sustain:** ING Vysya expects to expand its loan book at slightly higher levels than the industry average in FY11 (~25%). The loan book grew by 6% qoq and 23% yoy in the Q3FY11, driven by traction in the business banking segment (up 10% qoq), which comprises 28% of the total outstanding book. Growth would be supported by expansion in CASA deposits, driven by: i) expanding network coverage; and ii) differentiated product offerings. Mortgages form the bulk of the retail book (~85%), while personal loans remain small at only ~4% of retail book as of December 2010. The CV book also remains small at 6% of outstanding retail credit.
- **Branch rollout to aid CASA accretion:** ING Vysya intends to maintain a healthy flow of CASA deposits to fortify its liability base. The bank holds ~40 more licenses and intends to roll these out by Q1FY12 (~20 in Q4FY11 and the rest in Q1FY12). Currently, ~73% of the bank's network is located in South India. The management is focusing on improving productivity at its existing distribution and scaling up its presence in the North and West India. It added 23 new branches YTD in FY11.
- **Robust fee income growth ahead:** The management expects non-interest income to track balance sheet growth. Wealth management and forex fees are likely to be the primary drivers of growth in the segment.
- **Asset quality remains healthy:** Gross slippages were under control at Rs340m in Q3FY11 (annualized 0.7% of opening loans), significantly lower than Rs1.5bn in H1FY11. Consequently, gross NPAs declined by Rs196m to 2.66% from 2.91% in Q2FY11. Despite lower provisions, net NPAs declined to 0.64% from 0.81% in Q2FY11. Provision coverage ratio increased to 76.4% from 73% in Q2FY11. The bank reached the regulatory coverage ratio in Q2FY11, which should keep provision expenses low in the near term.
- **RoA expansion ahead:** The management expects provisions to significantly reduce in FY12, which, along with buoyant fee income, is expected to be the biggest contributor of profitability. ING expects to scale up RoA to ~1% in FY12. Reduction in the cost-to-income ratio is expected to drive RoA expansion in the medium term.

Key financials

As on 31 Mar	FY08	FY09	FY10	FY11E	FY12E
Net profit (Rs mn)	1,576	1,889	2,115	3,174	4,274
yoy growth (%)	*77*	*20*	*12*	*50*	*35*
Wtd avg shares (m)	102	103	120	120	120
EPS (Rs)	15.4	18.4	17.6	26.5	35.6
EPS growth (%)	57.0	87.9	(4.2)	50.1	34.6
PE (x)	18.9	15.8	16.5	11.0	8.2
Book value (Rs/share)	139.2	155.4	185.0	207.9	238.6
Adj. Book value (Rs/share)	126.2	136.5	174.4	199.2	230.0
P/ Adj. Book (x)	2.3	2.1	1.7	1.5	1.3
RoE (%)	13.0	12.5	11.1	13.5	16.0

Source: IDFC Securities, Price as on 9th Feb 2011

Pharma

IPCA LABORATORIES OUTPERFORMER (RS278, MCAP: RS35BN / US$769M)

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- Ipca remains confident of clocking 20% revenue growth in FY12 and expects operating margins to improve as the impact of recent field force additions kick in. It derives 70% of sales from formulations, with the remaining 30% from API sales. API sales are expected to decline, with APIs being increasingly utilized for internal consumption.
- **Domestic business**: Ipca's top three segments, anti-diabetic, CVS and anti-malarial, grew by 28%, 15% and 31% yoy over 9MFY11. Anti-bacterial, GI and dermatology grew by 9-11% yoy. Ipca currently has 150 brands and plans to launch 10-15 products annually. It remains positive on its ability to grow 18-20% per annum over the next few years.
- It has added 2000 employees to its field force over the past two years, including 1200 in FY11, taking the total to ~5000. Of the 1200 added recently, 1000 were inducted in the existing divisions and 100 each in nephrology and urology, segments created in the recent quarter.
- The management cited that the field force strength had largely stabilized, and expects to add only 400-500 employees over the next two years. New field force additions would be in Dynamics, which would not be therapy–focused, but target existing products with higher revenue potential.
- Ipca's international branded business continues to do well. The management is positive on the prospects in Russia, guiding for 30% growth rates hereon. The company currently markets 14 products in Russia. The LatAm, Middle East and West African operations grew by 76% (to Rs50m), 9% (Rs170m) and 16% yoy (Rs220m) respectively in 9MFY11.
- The company continues to be optimistic about its ability to grow the global tender business of anti-malaria products over the next few years, given low competition in the space.
- Indore SEZ: Ipca has received MHRA (UK) approval for its Indore SEZ facility and expects WHO approval in Q4FY11. However, the management refrained from providing any timelines for US FDA approval. It intends to utilize the facility to service only the UK market and WHO tenders until it receives US FDA approval.
- To hasten the approval process, the management has enrolled certain drugs from the Indore SEZ under the PEPFAR programme. Under this programme, the US FDA is supposed to approve the product facilities within six months of registration, which implies approval latest by June 2011.
- Ipca has incurred Rs1.4bn capex to date and plans to invest another Rs400m for packaging machinery in FY11. The company expects to clock US$100m in sales from the Indore SEZ on full commissioning, i.e, 3-4 years from now.
- It continues to hedge its export receivables at 52% of anticipated exports over the next 12 months at a ~USD/INR rate of 48.
- Ipca has guided for capex of Rs2bn and Rs2.2bn in FY11 and FY12 respectively.

Key financials

As on 31 March	FY08E	FY09E	FY10E	FY11E	FY12E
Net sales (Rs m)	10,510	12,838	15,595	18,526	22,218
Adj. net profit (Rs m)	1,360	1,008	2,083	2,494	3,010
Shares in issue (m)	125	125	125	125	125
Adj. EPS (Rs)	10.9	8.0	16.6	19.9	24.0
% change	*8.9*	*(25.9)*	*106.7*	*19.8*	*20.7*
PE (x)	25.6	34.6	16.7	14.0	11.6
Price/ Book (x)	5.9	5.5	4.0	3.3	2.7
EV/ EBITDA (x)	22.8	15.3	12.0	11.0	8.6
RoE (%)	25.6	16.5	27.8	25.8	25.4
RoCE (%)	15.9	20.9	22.8	20.8	23.1

Construction

ITNL

UNRATED (RS204, MCAP: RS40BN / US$878M)

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- ITNL is a leading road BOT player in the country with a portfolio of 22 road projects totaling ~12,000 lane km. It has also forayed in other transportation sectors like metro rail, city bus services, border check posts and airports.
- It currently has 4000 lane km of commissioned projects and also operates a bus transportation project in Nagpur.
- Construction of the Gurgaon Metro project (4.8km link connecting Delhi Metro Sikanderpur station with DLF Cyber City) commenced recently. The project cost is Rs11bn, with a concession period of 99 years. ITNL has ~54% stake in the project, which is likely to be commissioned in 2012.
- ITNL is also developing two regional airports, Gulbarga and Shimoga, awarded by the Karnataka Government (ITNL stake, 40%). The total cost of the projects is ~Rs4bn, with a concession period of 30 years. The projects have ~300 acres of land available at each location for real estate development.
- The company is also exploring opportunities in automatic multi-level parking systems.
- ITNL bagged BOT projects worth Rs76.3bn to date in FY11 and is a L1/ preferred bidder in Rs113bn worth of projects.
- The company had an unexecuted order backlog of Rs135bn (including L1 orders of Rs15bn) as of 31 October 2010.
- The company has indicated that there are ~1000km road BOT projects from NHAI that are in the price bidding stage. These projects are likely to be awarded by March 2011.

Key financials

As on 31 March	FY 2008	FY 2009	FY2010
Net sales (Rs m)	1,710	1,321	8,455
Adj. net profit (Rs m)	765	404	3,247
Shares in issue (m)	171.4	171.4	194.3
Adj. EPS (Rs)	4.7	2.4	18.9
% change	*(3.4)*	*(49.9)*	*702.7*
PE (x)	43.8	87.3	10.9
Price/ Book (x)	4.5	4.4	2.5
EV/ EBITDA (x)	57.0	88.4	9.3
RoE (%)	10.9	5.1	27.2
RoCE (%)	9.9	5.9	18.3

Metals

JAI BALAJI — UNRATED (RS185, MCAP: RS185BN / US$258.2BN)

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- Jai Balaji (JBIL) has achieved considerable progress at a 5m tpa steel project that it plans to set up in Purulia, West Bengal. It has achieved ginancial closure for phase I through Rs12.3bn debt from a SBI-led consortium and the balance Rs6.4bn via internal accruals/ fresh equity. Phase I comprises a 2.4m tpa beneficiation plant, 1.2m tpa pallet plat, 0.75m tpa DRI plant, 0.45m tpa EAF facility, 0.66m mtpa sponge iron plant and 75MW power plant which will generate power through waster heat recovery. The company has received statutory permissions for the project, including railway traffic, water and environment clearances, besides having acquired the necessary land for the project.
- The ductile iron plant started commercial operation on 3 November 2010 after BIS approvals. The unit has achieved capacity utilization of more than 30% in its first quarter of operations.
- JBIL had been allocated thermal coal from Jagannathpur A and Jagannathpur B (combined reserves of ~800m tonnes) for the project by WBMTDC. Exploration work at Jagannathpur A and B has been completed and the geological reserve report has been prepared. The mines are mainly underground, so they pose fewer land and environmental approval issues than open cast mines.
- Development of the Ragunathpur coal block is on track and the mining plan would be submitted in the next 1-3 months. Production is expected to be synchronized with Purulia.
- Forest clearance for the Dumri coal block is expected in next 2-3 months. JBIL has been allotted the coal block jointly with Bajrang Ispat, which holds a 27.2% stake. All permits, except the stage II forest clearance, have been received. The company expects 0.5m tpa of attributable production and sees it increasing to 1m tpa over the next 1-2 years.
- The management also remains confident of starting production at the Rohne coking coal block given the criticality of coking coal as a mineral resource for India and investments already made into end-user plants.

Key financials

As on 31 March	FY 2008	FY 2009	FY2010
Net sales (Rs m)	13,221	16,894	19,144
Adj. net profit (Rs m)	1,189	13	318
Shares in issue (m)	47.1	47.1	63.8
Adj. EPS (Rs)	25.2	0.3	5.7
% change	*91.2*	*(98.9)*	*1,981.5*
PE (x)	7.3	678.6	32.6
Price/ Book (x)	2.1	2.1	1.3
EV/ EBITDA (x)	8.2	15.4	11.3
RoE (%)	36.0	0.3	4.8
RoCE (%)	15.2	1.2	5.0

Agriculture

JAIN IRRIGATION — OUTPERFORMER (RS175, MCAP: RS63BN / US$1.4BN)

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- The Indian MIS industry offers a huge opportunity with only 5m ha of the potential 62m ha of irrigated land currently under the system. Jain Irrigation (JISL) leads the MIS industry in India with a 55% market share. It is also the second largest MIS player globally. JISL has clocked a commendable 40% CAGR in revenues over FY05-10. Its 40-year legacy of supplying farming equipment has aided in creating a sound foundation with the farmer community. This is the key competitive advantage for JISL, given the business entails managing the sector's three most difficult variables – farmer, weather and government.
- **MIS growth to revive:** While JISL has been consistently tracking 35%+ growth every quarter in MIS, the past two quarters (Q2FY11 and Q3FY11) have been subdued, growing only at ~20% on the back of extended and above-average rainfall in the country. However, the management is confident of growth reviving from the current quarter. Recent moves by the government (National Mission on MIS to achieve 2.85m ha over the next two years; Rs80bn of outlay) reflect the urgency and push towards the space, which should underpin sharper growth for JISL.
- **Agro processing – near-term worry:** Non-availability of onions has impacted JISL's onion dehydration segment. However, with prices now showing signs of correction, the segment is expected to revive. In fruit processing, JISL continues to register strong growth backed by an improved product mix (higher Alphonso sales). The fruit-processing order book for the year is very strong at ~Rs3bn.
- **Corporate actions – bonus DVR:** The Board has recommended issuance of bonus equity shares with differential voting rights (DVR) in the ratio of 1 DVR equity share for every 20 equity shares held. Ten DVR equity shares will carry voting rights equivalent to 1 equity share. JISL is testing the market for such an instrument with the intent of raising capital via DVRs.
- **NBFC on the cards:** The Board has also approved plans to set up an NBFC and JISL intends to apply to the RBI for the same. The company is looking to provide credit to farmers through this arrangement, which in turn could help it bring down receivables and improve its working capital cycle in the MIS business.

Key financials

As on 31 Mar	FY08	FY09	FY10	FY11E	FY12E
Net sales (Rs m)	23,185	29,362	34,369	41,392	50,242
Adj. net profit (Rs m)	1,191	2,005	1,599	2,754	4,224
Shares in issue (m)	72	72	72	362	362
Adj. EPS (Rs)	3.3	5.5	4.4	7.6	11.7
% change	*17.1*	*67.4*	*(20.2)*	*72.2*	*53.4*
PE (x)	53.0	31.6	39.7	23.0	15.0
Price/ Book (x)	7.3	6.3	5.4	5.0	4.4
EV/ EBITDA (x)	7.4	6.0	4.8	10.6	8.1
RoE (%)	18.9	21.5	14.7	22.5	31.1
RoCE (%)	16.8	16.6	16.5	20.4	26.1

Note: Prices as on 8th February 2011

Real Estate

JAYPEE INFRATECH — OUTPERFORMER (RS56, MCAP: RS7.8BN / US$170M)

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- Jaypee Infratech (JIL) is a unique play on the infrastructure and real estate space via a single entity.
- JIL has achieved significant progress on the construction of the Yamuna Expressway in the past two years; more than 93% of the cost has been incurred (Rs93bn) and the project is nearing completion (>85% complete).
    - In 9MFY11, JIL spent more than Rs25bn on the construction
    - It plans to open the expressway to the public by July 2011, with toll revenues expected from October 2011.
    - No further farmer protests over land acquisition have been reported since September 2010.
- In real estate, JIL has been able to achieve record volumes in the past two years despite launches having been restricted to Noida.
    - JIL has sold more than 31msf in Noida with a sales value of Rs96bn (average realization, 3,300psf) and received more than Rs41bn in advances (>43% of sales).
    - While NCR remains a predominant investor-driven market, JIL's collection of more than 40% in advances clearly indicate preference for the Jaypee brand in Noida as also presence of significant end-user interest.
- In 9MFY11, JIL sold 9.83msf with a sales value of ~Rs96bn (average realization of >Rs3,100psf).
- JIL is planning its Greater Noida launch in the next couple of months, while the Agra launch is expected in H1FY12. The company wants to maintain an annual sales run rate of 12-15msf, with Noida contributing 4-6msf and Greater Noida and Agra the rest.
- The stock has corrected ~19% in the past month and ~38% since listing (Rs102). Our Mar-12 NAV stands at Rs132 per share with a price target of Rs105 (20% discount to NAV).

Key Financials

As on 31 March	FY08	FY09	FY10	FY11E	FY12E
Net Sales (Rs. mn)	-	5,545	6,407	26,134	33,716
Adj net profit (Rs. mn)	(163)	2,667	4,875	14,057	10,457
Shares in issue (mn)	965	966	1,226	1,389	1,389
Adj EPS (Rs)	(0.2)	2.8	4.0	10.1	7.5
% change		*(1,731.0)*	*44.0*	*154.5*	*(25.6)*
PE (x)	n/a	20.3	14.1	5.5	7.4
Price/Book (x)	5.7	4.3	3.5	1.6	1.4
EV/EBITDA (x)	(647.9)	22.4	18.3	7.1	6.8
RoE (%)	(3.4)	24.3	30.4	41.5	19.8
RoCE (%)	(3.0)	14.0	10.5	19.7	14.9

Power

KALPATARU POWER — OUTPERFORMER (RS122, MCAP: RS18BN / US$413M)

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- Kalpataru Power is a leading player in power transmission/ distribution and infrastructure.
- It has a diversified business portfolio across transmission EPC, oil & gas pipelines, biomass energy, agri-logistics, real estate and infrastructure (roads, industrial structures, etc), with a focus on transmission and infrastructure.
- The company had an order backlog of ~Rs50bn at the end of Q3FY11 (1.7x FY11 revenues). The order intake in the Oct-Dec 2010 quarter was Rs7bn (+68% yoy). The domestic transmission business accounted for Rs28bn (56% of total order backlog), while international transmission orders were worth Rs17bn (34%). The infrastructure (pipeline) segment had orders worth Rs3.75bn (8%), while the balance orders of Rs1.25bn were contributed by distribution.
- Key management inputs:
  - Orders from PGCIL slowed down in 9MFY11, but are expected to increase in Q4FY11
  - The power transmission business is witnessing increasing competition due to the entry of pure EPC construction companies. However, Kalpataru is bidding cautiously and not trying to compete with the newer entrants by quoting at lower margins. The current order backlog provides revenue visibility for the next 18 months
  - The 'Right of Way' (RoW), a key clearance for transmission projects, is becoming difficult to obtain due to various reasons – increased demand for land for transmission towers, slow decision making by the bureaucracy, interference by local politicians, etc. These issues could cause up to 3-6 months of delay in project execution
  - The cost of borrowing has increased by about ~100bp since April 2010 and is currently ~9.5%
  - From a long-term strategic point of view, the company plans to enter the BOT segment due to higher margins (~15%), v/s 10-11% for EPC projects
  - Kalpataru is currently focusing on BOT projects in India, though the trend of developing transmission projects on BOT basis is catching up in Brazil, Kenya and other African and South American countries.

Key financials

As on 31 Mar	FY08	FY09	FY10	FY11E	FY12E
Net sales (Rs m)	26,749	32,461	39,963	44,565	54,942
Adj. net profit (Rs m)	1,649	1,109	1,777	2,116	2,541
Shares in issue (m)	133	133	133	153	153
Adj. EPS (Rs)	12.4	8.4	13.4	13.8	16.6
% change	*2.2*	*(32.7)*	*60.2*	*2.8*	*20.1*
PE (x)	9.8	14.6	9.1	8.8	7.4
Price/ Book (x)	1.9	1.7	1.4	1.0	0.9
EV/ EBITDA (x)	6.2	7.9	5.9	5.2	4.4
RoE (%)	21.0	12.1	16.8	14.4	13.3
RoCE (%)	23.7	16.7	18.3	16.9	17.1

Power

KEC INTERNATIONAL

OUTPERFORMER (RS79, MCAP: RS20BN / US$445M)

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- KEC International reiterated that order inflow is likely to continue across its key markets.
- PGCIL order inflow has been slow, but the company expects a sharp pick-up over the next six months considering that huge generation capacities are being built.
- Order inflows in the international markets remain robust led by both replacement demand and build-up of fresh infrastructure.
- Unrest in some markets like Algeria, Yemen and Egypt is unlikely to impact KEC as it has a diversified geographical presence.
- KEC expects the US market to provide the next leg of growth on the international front. Accordingly, the acquisition of SAE towers is likely to be extremely value accretive. SAE has a current order backlog of US$160m, as against US$126m at the time of the acquisition.
- Apart from transmission orders, the management is also focusing on diversifying into other EPC areas like railways, telecom, substations, etc., which would provide new avenues of growth. Accordingly, the company is eyeing entry into water-based EPC projects.
- KEC would evaluate and bid for BOT transmission projects in a JV structure if incremental projects are on BOT basis.
- Order backlog as of end-December 2010 was Rs80bn across segments. The order backlog provides visibility on revenues over the next 18 months.
- The management believes that while competition remains intense, irrational bidding to win projects is unlikely to sustain, thereby providing KEC an opportunity to win margins.
- KEC continues to maintain its margin guidance of 10% despite a rise in input costs as it has booked raw material inventories at historical prices for fixed-price contracts. Further, diversification in terms of geographies and segments would drive margins variably over the quarters based on acquisition.
- **Attractively valued; maintain Outperformer:** KEC has maintained traction in order booking over the past few quarters. We expect this to pick up further, led by diversification into business verticals like cables, telecom and railways as also into geographies (particularly America, where activity is picking up strongly). We believe strong activity across verticals will drive growth in KEC's order backlog of Rs80bn (1.9x FY11E revenues) and ensure consolidated earnings of 15% CAGR over FY10-12E. The stock currently trades at 10x FY11E earnings and 8.5x FY12E earnings. Given a strong pipeline of orders, earnings growth visibility over the next two years, and strong return ratios, we believe valuations are attractive. We maintain our Outperformer rating on the stock.

Key financials

As on 31 Mar	FY08	FY09	FY10	FY11E	FY12E
Net sales (Rs m)	28,145	34,288	39,072	43,888	54,932
Adj. net profit (Rs m)	1,598	1,781	1,838	2,091	2,501
Shares in issue (m)	247	247	247	257	257
Adj. EPS (Rs)	6.5	7.2	7.5	8.1	9.7
% change	*21.7*	*11.4*	*3.2*	*9.2*	*19.6*
PE (x)	12.1	10.9	10.5	9.7	8.1
Price/ Book (x)	4.0	3.5	2.5	2.5	2.3
EV/ EBITDA (x)	7.2	6.1	6.7	6.8	5.5
RoE (%)	43.0	34.2	27.3	26.2	29.6
RoCE (%)	35.3	32.2	26.1	20.5	21.2

IT Services

KPIT CUMMINS — OUTPERFORMER (RS142, MCAP: RS11BN / US$246MN)

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- KPIT Cummins is a mid-tier IT services provider focused on the manufacturing vertical with a presence in the automotive, industrial and defense sectors. It is now investing to expand into energy and utilities verticals. Within the above verticals, the company is focused on a few key customers. In terms of service lines, KPIT offers VLSI and embedded software services, package implementation, business intelligence, and BPO services besides regular application development and maintenance services. The company has ~5,600 employees working for 150+ clients.
- **Robust revenue growth momentum:** Driven by the improving macroeconomic environment and an increase in automobile-related discretionary spending, KPIT is witnessing strong revenue growth momentum. The company's organic business is expected to grow by 30-38% and inorganic business by 7-8% in FY12 on the back of overall ~38-40% growth in FY11.
- **Margins to improve gradually**: Operating margins have been declining recently because of acquisition-related costs, high attrition, low utilization, and lower margins at the acquired entities. The management is focused on improving these and is employing various levers like higher fresher hiring, improving utilization, and increasing revenues from offshore and fixed-price projects. These levers would play out in the long term and margins are expected to rise gradually to ~18% in the next 2-3 years.
- **REVOLO update**: In June 2010, KPIT entered into a 50:50 JV with Bharat Forge to manufacture and market an indigenously developed hybrid technology solution for automobiles – REVOLO. This would enable both existing and new vehicles to dramatically increase fuel efficiency (by 50-80% depending upon the driving conditions) and engine performance, while significantly decreasing green house gas emissions (~30%). The solution is currently being successfully tested on a few retrofit fleet operators. REVOLO has received positive feedback from the retrofit market and, post necessary approvals from the government, is expected to be operational by Q1FY12.
- **Attrition continues to be a challenge:** The management conceded that high attrition is a challenge, especially in the 3-5 year experience band. It is trying to address this issue by hiring more freshers and providing existing employees more growth opportunities. The company also did not rule out the possibility of double-digit wage hikes in FY12.
- **M&A**: KPIT acquired three companies (Sparta, In2soft and CPG) in the past six quarters and is seeking more acquisition opportunities in the Oracle and SAP space. It got board approval in January 2011 to raise Rs1.125bn by preferential share allotment, mainly for funding acquisitions.
- We expect KPIT to continue witnessing strong demand-led revenue growth from both the organic and inorganic businesses. We currently do not build in any upside from REVOLO. Trading at ~12x FY11E and ~10x FY12E EPS, KPIT Cummins is a key pick in the small-mid cap IT services space. We have an Outperformer rating with 12-month target price of Rs220 (based on 15x FY12E EPS).

Key Financials

As on 31 Mar	FY09	FY10	FY11E	FY12E	FY13E
Net sales (Rs m)	7,932	7,316	9,944	12,141	14,144
Adj. net profit (Rs m)	659	857	967	1,331	1,573
Shares in issue (m)	78	78	80	87	87
Adj. EPS (Rs)	8.4	10.8	11.7	14.7	17.4
% change	*25.1*	*28.8*	*7.7*	*26.4*	*18.2*
PE (x)	16.9	13.2	12.2	9.7	8.2
Price/ Book (x)	6.8	2.9	0.7	0.7	0.7
EV/ EBITDA (x)	5.8	7.0	0.1	0.4	(0.0)
RoE (%)	30.8	31.1	9.7	8.0	8.7
RoCE (%)	43.5	33.0	11.0	8.3	8.8

Source: Company, IDFC Securities

Financials

MAGMA FINCORP LIMITED

UNRATED (RS63, MCAP: RS8.2BN / US$183M)

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- Magma, headquartered in East India, is an NBFC providing finance across diverse product segments – commercial vehicles, construction equipment, cars, utility vehicles, tractors and SME loans. Magma operates mainly in rural and semi-urban regions, which account for ~80% of its branches. Magma has created a strong position for itself, especially in equipment and vehicle financing space, led by two factors: 1) little or no availability of banks and formal lending institutes in its focus areas; and 2) focus on first-time buyers and small entrepreneurs.
- **Strong growth ahead:** The management expects strong loan growth of ~40% in FY12, driven by: i) strong industry demand in CVs (20-25% growth), cars (30-35% growth) and construction equipment (rebound expected); ii) expansion of branch network (200 branches by FY12, v/s 153 in FY10); and iii) increased availability of all products at the existing branch networks. Magma reported 43% yoy and 12% qoq growth in disbursements in Q3FY11.
- **Proportion of high yielding assets to increase**: The company aims to increase the proportion of high yielding products (tractors, used vehicles and SME loans) to ~25% in FY12, up from 13% in FY10. Increase in high-yield loans would help Magma sustain margins in a rising interest rate environment. High yielding loans constituted 22% of disbursements in Q3FY11, compared with 13% in Q3FY10.
- **Margins to remain stable:** Despite the rise in funding costs, the management expects margins to remain stable at 5.1 - 5.2% over the next few quarters as; i) continued growth in high yielding loans are expected to support margins; ii) ~75% of the book qualifies as priority-sector loans, and a huge demand by the banking systems for PSLs in Q4 would help Magma negotiate superior rates.
- **Superior collection efficiency:** Magma has a collection efficiency of 100%, which has helped it maintain a low write-off ratio (write-off to total assets) of ~0.4%. Magma has segregated its business generation vertical from the credit appraisal vertical, which has helped it contain delinquencies in this risky segment. Magma witnessed no NPAs on its books in the past five years due to its prudent accounting policy – all contracts with more than 180 days past due are treated as loss assets and are written off as bad debt.
- **Funding mix:** A PSL status of ~60% and consistent investment grade ratings of its debt instrument have provided Magma adequate and continued financing lines. Currently, ~50% of Magma's funding needs are financed through working capital loans. Securitization has also been effectively used to enhance the company's funding base. However, with other lines of funding gaining scale, the management expects the share of securitization to decline to ~25% of loan book by FY12 (~40% currently).

Key financials

Year to 31 March	2006	2007	2008	2009	2010
Net profit (Rs m)	202	314	503	398	713
yoy growth (%)	*44.6*	*55.7*	*59.9*	*(20.8)*	*79.3*
Shares in issue (m)	72.0	84.7	108.9	108.9	108.9
EPS (Rs)	2.8	3.7	4.6	3.7	6.6
EPS growth (%)	14.4	32.3	24.3	(20.8)	79.3
PE (x)	28.5	21.5	17.3	21.9	12.2
Book value (Rs/share)	11.6	7.2	14.6	16.6	21.7
P / BV (x)	6.9	11.1	5.5	4.8	3.7
ROAE (%)	18.8	16.4	16.7	11.8	20.1

Note: Price as on 9 February 2011

Financials

MANAPPURAM GENERAL FINANCE AND LEASING LTD — UNRATED (RS104, MCAP: RS40BN / US$889M)

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- MGFL is a South India-based NBFC specializing in loans against gold. Its business has grown at a significant pace in its six decades in the lending space (including more than four decades in gold loans). MGFL's branch network expanded rapidly from 436 in FY08 to ~1800 in Q3FY11.
- **Branch network – dominant presence in South India:** MGFL's network is concentrated in South India, with ~80% of the branches in Andhra Pradesh, Karnataka, Tamil Nadu and Kerala. The management now plans to branch out to other geographies, especially Maharashtra, Gujarat, Orissa and West Bengal (predominantly Kolkata). Besides wider distribution, the company also plans to sustain growth momentum by creating higher awareness about gold loans through advertising, particularly in markets outside South India.
- **Pressure on margins:** As it operates in a highly under-penetrated segment, MGFL has managed to generate attractive yields over the past few years. However, increased competition in the segment led to a ~300bp decline in yields over the past 12 months. Further, after the recent RBI directives on gold loans (loans sanctioned to NBFCs for on-lending to individuals or other entities against gold jewellery and securitized gold loans portfolio would not get classified as agriculture loans), the management expects funding costs to increase by ~100bp in the near term.
- **Strong growth in disbursements and AuM:** Under-penetrated markets, access to multiple sources of funding, and branch expansion have given the lender a 61% CAGR in disbursements with over FY08-10. Correspondingly, AUM too increased (39% CAGR) to Rs26.2bn as of March 2010. With demand drivers in place and a rapid proliferation of branch network, the management expects AuM to grow by 187% yoy (on a low base) to Rs75bn in FY11, and by ~100% to Rs140bn in FY12.
- **Credit costs to remain low:** Given the high sentimental value attached to household jewellery, LTV of 75% and shorter duration of loans, gold loan portfolios typically carry a low rate of default. MGFL's gross NPAs on its gold loan book too have been minuscule (0.2-0.4% over FY06-10). While there does exist a risk to this portfolio if gold prices were to crash significantly in a very short time, the management has indicated that any decline in gold prices does not automatically translate into higher defaults given the higher perceived value of the ornament. Apart from the sentimental value, replacement value of household jewelry remains high as making charges (10-20%) are not accounted for in the total valuation of gold for the purpose of extending loan.

Key Financials

Year to 31 March	FY07	FY08	FY09	FY10
Net profit (Rs mn)	152	280	478	1,197
yoy growth (%)	-	*84.2*	*70.6*	*150.7*
Shares in issue (mn)	18	88	268	340
EPS (Rs)	8.3	3.2	1.8	3.5
EPS growth (%)	-	(61.8)	(43.8)	97.4
PE (x)	0.0	0.0	0.0	29.6
Book value (Rs/share)	21	15	10	18
P / BV (x)	5.0	7.0	10.9	5.8
ROAE (%)	40.3	33.1	24.7	27.6

IT Services

MINDTREE — OUTPERFORMER (RS399, MCAP: RS16.0BN / US$346MN)

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- MindTree is a mid-tier Indian IT services company providing offshore-based services to global organizations in BFSI, manufacturing, transportation and hi-tech industries. It is one of the youngest companies to cross the US$250m mark and has a complete suite of technology services, including IT services, offshore product development and R&D services. The company is one of the preferred Tier2 IT services vendors.
- **IT services business to show traction:** MindTree's core IT services business is highly levered to discretionary IT spending and is expected to show strong revenue traction on the back of improving macroeconomic environment. This segment reported volume-led revenue growth of ~8% qoq in Q3FY11, driven by growth in the BFSI and manufacturing verticals. For 9MFY11, this business segment has grown 30% yoy in USD terms – ahead of other two segments.
- **OPD and R&D services:** The OPD business USD revenue has grown ~9% yoy in 9M FY11 and is expected to show healthy growth in FY12. R&D services USD revenues have grown ~5% yoy in 9M FY11 organically. Including Kyocera acquisition, USD revenues from R&D services have shown 28% yoy growth. Management expects this segment to remain slightly constrained in the coming few quarters. The company, however, has won a deal with a Japanese semiconductor company in the R&D space, which should boost growth in the long term.
- **Chairman's resignation not a business concern:** The management commented that Mr. Soota had resigned for personal reasons; but coming just two months before his expected transition from executive chairman to non-executive chairman role, the decision came as a surprise to the management. At the time of resignation, Ashok Soota had only the strategy function reporting to him. The other four business functions (sales, delivery, finance and HR) were reporting to the CEO, Krishnakumar Natarajan. The transition of responsibilities (reporting lines) had been happening over past few years. Initially, only sales and delivery reported to Krishnakumar and the other three were reporting to Soota. In 2007-08, HR and finance started reporting to the CEO. Because of this gradual transition, the management said the resignation would not affect the business at large.
- **Margins to rebound in FY12**: MindTree's operating margins have declined from 18%+ levels to ~11% in the past three quarters, while services margins were ~15%. With product business closure costs behind, the management expects a rebound in margins in FY12.
- **Hedges**: As of December 2010, the company had outstanding hedges of US$157m at a weighted average rate of Rs45/US$.
- **Our view:** Levered to discretionary spending, MindTree's USD revenues should expand by ~24% CAGR over FY11-13E. We see value in the MindTree's services business, which is currently trading at ~9x FY12E EPS. We have an Outperformer rating on the stock with a 12-month price target of Rs650, based on 14x FY12E EPS.

Key Financials

As on 31 March	FY09	FY10	FY11E	FY12E	FY13E
Net sales (Rs m)	12,375	12,960	15,148	17,768	21,335
Adj. net profit (Rs m)	523	2,148	1,184	1,903	2,248
Shares in issue (m)	38	39	40	40	40
Adj. EPS (Rs)	13.7	52.8	29.0	46.5	55.0
% change	*(48.3)*	*285.2*	*(45.1)*	*60.7*	*18.2*
PE (x)	29.1	7.6	13.8	8.6	7.3
Price/ Book (x)	2.6	2.4	2.1	1.7	1.4
EV/ EBITDA (x)	5.0	6.5	7.6	5.2	4.2
RoE (%)	9.4	34.2	16.3	21.9	21.1
RoCE (%)	40.6	25.8	18.2	24.7	24.0

Source: Company, IDFC Securities

Media

NETWORK18 GROUP

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- The Network18 Group is a leading media conglomerate with businesses panning across news (business and general), entertainment (Hindi GEC, kids channel, youth channel), e-commerce, digital (or internet portals) and print media.
- The Network18 Group has five news channels, which together contribute 31% to overall group revenues. Within the entertainment segment, the group has a JV with Viacom called Viacom18, which operates four channels and houses the Indian Film Company (a film fund). The entertainment segment is the biggest contributor to the group's revenues at nearly 45%. The digital and e-commerce businesses are currently small and contribute 9% and 12% to overall revenues respectively.
- **Group restructuring:** Network18 group has had an extremely complicated group structure with inter-group ownerships. The existing structure of Network18 Group has four separately listed entities – Network18 Media and Investments (the holding company), TV18 (business news and web business), IBN18 (general news and entertainment business) and Infomedia18 (yellow pages and print businesses). The group has announced a restructuring after which IBN18 (New TV18) would own all the broadcast properties and Network18 would be the holding company for New TV18 besides having all the non-broadcast businesses of the group. The restructuring is expected to be complete in Q4FY11. The process would largely put to rest concerns over the complicated ownership structure and bring in transparency.
- **IBN18 (New TV18):** The scale-up of Viacom18 (Colors in particular) has been ahead of expectations with Colors reigning the GEC space and Viacom18 clocking revenues of Rs8.3bn in its second year of operations. As Colors narrows its differential in rack rates with Star Plus, advertising revenues would tread a strong growth trajectory. Colors has terminated its distribution deal with Sony One Alliance (Rs3bn for three years) and has now formed a JV with the Sun TV Group – Sun18 – to distribute all the channels of its network. With ZEEL garnering ~Rs10bn in distribution revenues annually from India and international markets, the #2 GEC channel, Colors, offers strong growth potential. IBN18 is proposing to add new channels in the lifestyle and movies genres.
- **Network18:** Network18 is the holding company for the broadcasting assets (to own 58.3% of New TV18 post restructuring) and houses the digital, publishing and e-commerce businesses of the group. Network18 also runs an investment book (book value of ~Rs3bn), which owns equity stake in companies like DEN Network, Yatra.com, etc. Network18 is looking to monetizing some of these investments over the next six months.

Retail

PANTALOON RETAIL — OUTPERFORMER (RS246, MCAP: RS51BN / US$1.1BN)

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- **Retail space expansion at ~2m in FY11**: Pantaloon Retail (PF) is India's largest retailer, with 13.2m sqft of retail space as of FY10 (June year-end). It added 0.85m sqft in H1FY11 and is expected to add another 1m-1.1m sqft in H2FY11 across select formats – Big Bazaar, Food Bazaar, Central, Pantaloons, Home Town and Brand Factory. Given its electronic retailing format, e-zone, continues to incur losses, it may not increase stores. The overall retail space addition is lower than our earlier estimate of 2.2m for the current year.
- **Double digit same-store-sales growth:** While overall space addition is a tad slower than our expectations and company guidance, SSS growth continues to remain upbeat helped by inflation. In terms of value, SSS growth across formats has been in double digits. Though December 2010 was slow, growth bounced back to double-digit levels in January. We expect it to stabilize at 6-7% in FY12 as the base effect of inflation comes into play. We expect slow offtake in consumer electronics.
- **Margins at 8.5-9%:** Within core retail, the value retail and home solutions segments have been growing the fastest. Both the segments have lower margins than fashion retailing. This, coupled with inflation-led growth, would keep margins under pressure. We expect 8.4% margins in Q2FY11, as against 8.2% in Q1FY11. We see margins at 8.5-9% in the next couple of years.
- **Working capital management key to improving balance sheet health:** With increased festive season inventory, PF's debt in the retail business has gone up to Rs35bn. While PF is focusing on improving working capital through efficient inventory management – SKU rationalization, auto replenishment, procurement planning, etc – it will be some time before results are visible. PF is aiming to bring down its inventory levels from 95-100 days currently to 75 days in the next three years. This would help release over Rs15bn of cash flow and help fund expansion. We expect 80% of the next three years' capex to be funded through internal cash generation.
- **Restructuring and monetization:** PF has completed the first phase of restructuring by bringing the home solutions business under the standalone entity and transferring value retail to a subsidiary to keep room for foreign participation when FDI norms ease. The company is now divesting the Future Capital business and transferring the proportionate shareholding to the investors of PF. It is also mulling options to demerge the cash guzzling Future Generali business, a process that could face regulatory hurdles. PF is also likely to scout for options to deleverage the core retail balance sheet through stake sale in a few of its ventures like logistics, e-commerce, real estate, etc.

Key financials

As on 30 June	FY08	FY09	FY10	FY11E	FY12E
Net sales (Rs m)	50,487	63,416	89,261	114,502	141,853
Adj. net profit (Rs m)	1,258	1,407	2,296	2,594	3,703
Shares in issue (m)	159	174	208	224	224
Adj. EPS (Rs)	7.9	8.1	11.1	11.6	16.5
% change	(3.5)	2.2	37.0	4.8	42.8
PE (x)	31.1	30.4	22.2	21.2	14.9
Price/ Book (x)	2.2	1.9	1.8	1.6	1.4
EV/ EBITDA (x)	13.1	10.5	9.5	8.3	6.9
RoE (%)	8.8	7.0	9.0	8.1	10.1
RoCE (%)	11.5	11.3	10.8	11.3	13.4

Retail

PROVOGUE INDIA — OUTPERFORMER (RS35, MCAP: RS4BN / US$88M)

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- **Retail momentum remains strong:** Provogue's (PROV) retail growth remains on a strong footing on the back of 40-50 store additions in FY11 (including 20 under fit-out) and sustained same store sales growth. Provogue now has nearly 160 stores and is expected to add 25-30 stores annually over the next couple of years. This, coupled with rapid expansion by the likes of Shoppers Stop, would help PROV's retail business grow at 25%+ for the next couple of years.
- **Results of corrective actions in FY10 now visible:** In FY10, PROV started focusing on improving operational efficiency through implementation of ERP, streamlining supply chain by bringing down distribution centres from 22 to 7, and closing down 19 loss-making stores. This is now visible in PROV's performance, wherein other overheads have dropped sharply from earlier levels and inventory days have come down by 25 days. As PROV further streamlines its supply chain from centralized DC, we expect further reduction in inventory levels.
- **Prozone – Aurangabad mall commences operations:** Prozone's 0.8m sqft mall in Aurangabad commenced operations in October 2010. It has already leased out 80% of the space at an average rental of Rs42/ sqft/ month. About 65% of the mall is already operational, with all the anchors barring the mutiplex having commenced operations. The mall has a very strong tenant mix with anchors like Star India Bazaar, Westside, Shoppers Stop, Pantaloons, Croma, etc., and other stores including Orama, Mothercare, Mom & Me, Lilliput, Provogue, Levi's, Pepe, Reebok, Nike, etc. The mall is expected to generate Rs350m-400m of rental income once operations achieve full scale.
- **Construction of other properties to start soon:** Prozone has 15.8m of developable land across Aurangabad, Indore, Nagpur, Coimbatore and Jaipur. All project barring Jaipur, which is on hold, are in approval stage and will commence construction in the next few months. These projects have been delayed while awaiting government approvals and environmental clearances. While the Indore project will be purely residential, Nagpur and Coimbatore are mix-used development plans. Given the cash flow of residential and annuity of retail, we see merit in the mix-used development projects. Prozone will also launch its commercial project in Aurangabad. Next mall in Nagpur and Coimbatore will be operational in 2013.
- **Restructuring of deal with Old Mutual:** According to the revised deal, Triangle Real Estate India Fund, promoted by Old Mutual, will invest Rs3.06bn in Prozone's SPV, Prozone International Limited, for a 35% stake (valuing the SPV at Rs8.65bn post money). The SPV will have three projects – Aurangabad, Nagpur and Coimbatore. Of the total investment of Rs3.06bn, Rs1.41bn would be the value of the stake sale by Prozone in the SPV and the remaining Rs1.65bn would be fresh issuance into the SPV. Indore and Jaipur, which were earlier part of the SPV, will now be directly owned by Prozone, while the Coimbatore project would move into the SPV. With this, Prozone would be fully funded for its expansion.

Key financials

As on 31 March	FY08	FY09	FY10	FY11E	FY12E
Net sales (Rs m)	3,365	3,597	4,807	5,686	6,816
Adj. net profit (Rs m)	258	291	284	367	462
Shares in issue (m)	100	116	114	114	114
Adj. EPS (Rs)	2.6	2.5	2.5	3.2	4.0
% change	*5.7*	*(3.2)*	*(0.7)*	*29.5*	*25.7*
PE (x)	13.6	14.0	14.1	10.9	8.7
Price/ Book (x)	1.1	0.6	0.6	0.5	0.5
EV/ EBITDA (x)	9.8	14.3	11.5	7.7	6.5
RoE (%)	9.0	5.8	4.1	5.1	6.1
RoCE (%)	10.3	4.4	4.4	5.8	7.2

Financials

SHRIRAM CITY UNION FINANCE — OUTPERFORMER (RS486, MCAP: RS24BN / US$528M)

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- Shriram City has displayed remarkable responsiveness to changes in the operating environment in the past two years. Its product mix has shifted away from consumer durables and 2-wheeler financing, while secured loans (auto, gold and business loans) gained prominence during the period. Consequently, the share of secured loans increased from 32% of the portfolio in FY08 to ~70% in Q3FY11.
- Healthy loan growth, a favorable asset-liability gap, and rising loan yields are expected to offset the impact of rising interest expenses on margins in the near term. As the average duration of assets is 16 months, they get re-priced ahead of deposits, which is beneficial in a rising interest rate environment. Also, the management's focus on short-duration gold loans (~3 months) would help Shriram City maintain margins in a rising interest rate scenario.
- SCUF's funding sources continue to be biased towards institutional funds, which comprised ~55% of total debt as of December 2009. The company has access to diverse sources of funding, which has helped it maintain the proportion of retail to institutional funds at 40:60 over the past couple of years.
- The management indicated that, given the diverse sources of funding as well as presence across multiple product segments, the RBI directives on gold loans (loans sanctioned to NBFCs for on-lending to individuals or other entities against gold jewellery and securitized gold loans portfolio would not be classified as agriculture loans) would have only a limited impact on SCUF.
- SCUF expects strong disbursement growth as demand in rural and semi-urban regions continues to be robust. The business banking segment and gold loans are expected to be the key drivers of growth. We expect SCUF's overall disbursements to expand to Rs77bn in FY11 and Rs97.7bn in FY12, a CAGR of 39%.
- The management plans to add ~150 branches and gain access to ~200 branches of associate companies by FY12. In line with Shriram City's business strategy, the new branches will also be located in semi-urban and rural areas (implying limited competition from banks and NBFCs).
- SCUF managed to contain gross NPAs at ~2% and net NPAs at ~1% over FY08-10 by adopting an aggressive write-off strategy and efficient collection mechanism. According to the recent RBI directives, the lender made standard asset provisions of Rs162m (amounting to 0.25% of the loan book) in Q3FY11. Going forward, as the portfolio mix shifts towards the low-default and high-collateral gold and business loan segments, we expect provisioning expenses to decline to ~1.6% of average loans in FY11-12.

Key financials

As on 31 Mar	FY08	FY09	FY10	FY11E	FY12E
Net profit (Rs mn)	877	1,170	1,943	2,443	3,202
yoy growth (%)	*73*	*33*	*66*	*26*	*31*
Wtd avg shares (m)	41	46	49	49	49
EPS (Rs)	21.3	25.5	39.5	49.7	65.1
EPS growth (%)	64.4	96.7	54.9	25.8	31.1
PE (x)	22.8	19.1	12.3	9.8	7.5
Book value (Rs/share)	103.6	154.8	200.6	242.3	297.0
Adj. Book value (Rs/share)	106.3	152.0	200.4	244.5	313.2
P/ Adj. Book (x)	4.6	3.2	2.4	2.0	1.6
RoE (%)	23.3	20.6	22.9	22.4	24.2

IDFC Securities, Price as on 9th Feb 2011

Others

SINTEX — OUTPERFORMER (RS148, MCAP: RS40BN / US$885M)

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- The current order book for the monolithic construction business is Rs26bn (executable over the next two years). The company has maintained its revenue guidance of Rs11bn-12bn in FY11 from the monolithic business. The recent acquisition of Durha construction (DCPL) would help the company grow and strengthen its monolithic and prefab business and expand its building product offerings in the infrastructure and industrial space. The company expects DCPL's revenue CAGR to be in excess of 20% and an EBITDA margin of ~20% over the next 2-3 years. Sintex has reiterated that while government spending and orders have been slow, it has not seen any major slowdown in orders.
- The management has clarified that the company would not invest in any IPP of the promoters or otherwise. Sintex's current requirement at PEAK load at its 19 different locations is ~78MW, of which ~37MW is accounted for by the Kalol plant where it has a captive plant. Sintex may opt for one of the following three options: 1) a group Captive Power Plant (CPP) scheme with an investment of Rs0.8bn-1.4bn. Sintex will not hold more than 24% stake; 2) invest in setting up a dedicated transmission line connected to the grid at a cost of ~Rs0.2bn; and 3) change the captive turbine unit in Kalol at a cost of ~Rs 1.5bn. Since this has to be implemented by 2014, the management would decide on one of the above options within the next year. Sintex Oil & Gas Pvt Ltd (a wholly owned subsidiary) has emerged as a successful bidder for three oil & gas blocks. Sintex has assured that the total investment in the subsidiary would be negligible. It has assured that this investment would not stay on the balance sheet beyond the next 12 to 15 months; NELP guidelines do not permit immediate selling of stake in these blocks before a three-year lock in period.
- **Maintain estimates; reiterate Outperformer:** Sintex's operational performance is on track and the building products segment is gaining traction. We maintain our FY11 and FY12 EPS estimates of Rs15.5 and Rs19 respectively. At 10.8x and 8.8x FY11E and FY12E earnings respectively, the stock trades at a considerable discount to historical multiples. With growth returning and visibility on RoE expansion increasing, we expect earnings multiples to rebound. Maintain Outperformer with a price target of Rs228 per share.

Key financials

As on 31 Mar	FY08	FY09	FY10	FY11E	FY12E
Net sales (Rs m)	22,742	31,355	32,816	39,941	46,169
Adj. net profit (Rs m)	2,322	3,273	3,312	4,209	5,168
Shares in issue (m)	306	271	271	271	271
Adj. EPS (Rs)	7.6	12.1	12.2	15.5	19.1
% change	(30.1)	59.2	1.2	27.1	22.8
PE (x)	19.5	12.2	12.1	9.5	7.8
Price/ Book (x)	2.9	2.3	2.0	1.7	1.4
EV/ EBITDA (x)	13.3	9.9	11.5	7.7	6.1
RoE (%)	21.0	19.9	17.9	19.4	19.7
RoCE (%)	12.2	10.5	7.7	10.3	11.8

Midcaps

SOLAR INDUSTRIES — UNRATED (RS558, MCAP: RS9.68BN / US$215M)

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- **Solar Industries (SIL),** with more than two decades of operations, is the largest manufacturer of industrial explosives in India with a 20% share of the US$535m explosives market. While its fully integrated manufacturing facilities and a superior product mix would help sustain growth momentum in the domestic operations (growing at 25%+), SIL is moving towards new growth frontiers.
- **A unique value proposition:** SIL has developed a footprint in the mineral-rich African subcontinent. With manufacturing units strategically located in demand-centric regions, SIL is in a position to tap a wider market. Incrementally, in a move to forward integrate, SIL has acquired two coal blocks in India with aggregate reserves of 116m tonnes. Thus, while the domestic explosives business would form the mainstay of the business, the African expansion would provide 'growth' and scale, and the coal blocks would bring 'value'.
- **Core domestic business – on a strong footing:** With India's largest installed capacity of 275,000 tonnes of explosives, SIL commands a key competitive advantage while bidding for Coal India tenders. SIL is among the largest supplier to Coal India (a monopoly buyer – consumes over 70% of total industry production). However, contribution of Coal India to SIL's business is down from 60% earlier to ~35% now. Further, incremental contracts being entered with Coal India have a quarterly price revision clause, enabling SIL to pass on any raw material price fluctuations. With private players (TISCO, Hindustan Zinc, etc) now increasingly contributing to SIL's business, we believe its diversified order book will help SIL de-risk the business model and achieve scale.
- **Africa expansion – adding scale:** SIL has set up two manufacturing units in Africa. These are in Zambia (10,000MT bulk explosive plant) and Nigeria (5000MT cartridge and 10,000MT of bulk explosives). These facilities are estimated to contribute ~Rs50m to profits of SIL in the current financial year. However, the full potential of these facilities would be visible only from FY12. SIL is also looking to expand to other regions like Tanzania and Australia.
- **Coal mines – embedded 'value':** Of the aggregate 116m tonnes capacity of the two coal mines in Chhattisgarh, 36m tonnes is held in a consortium (SIL's stake, 20%) of players including Ultratech Cement and Prakash Industries. The mine is located in the Madanpur block. However, this has been identified as a 'no-go' area by the government. The remaining 80m tonnes is held through SMS Infrastructure – a JV with a Nagpur-based mining company – with the coal mine located in Bhatgaon. This block is awaiting final environment and forest clearances. With rapidly rising demand for coal and coal blocks commanding rich valuations, SIL may look at a potential divestment of its stake in the Bhatgaon block (invested Rs500m for a 24% stake).

Key financials

As on 31 March	FY06	FY07	FY08	FY09	FY10
Net sales (Rs m)	1,472	2,058	2,810	4,878	5,576
Adj. net profit (Rs m)	222	189	361	442	587
Shares in issue (m)	17	17	17	17	17
Adj. EPS (Rs)	12.8	10.9	20.8	25.5	33.9
% change	-	*(14.8)*	*91.2*	*22.4*	*32.9*
PE (x)	43.6	51.2	26.8	21.9	16.5
Price/ Book (x)	6.4	5.9	5.2	4.4	3.5
EV/ EBITDA (x)	27.4	33.0	17.0	13.8	11.4
RoE (%)	29.2	12.0	20.8	22.0	23.9
RoCE (%)	28.3	10.3	18.5	20.9	21.6

Note: Prices as on 7th February 2011

Real Estate

SUNTECK REALTY — OUTPERFORMER (RS416, MCAP: RS2.6BN / US$60M)

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- Sunteck Realty Limited (SRL) is a promising premium residential player in the MMR with a strong portfolio comprising 32.2msf saleable area across 26 projects (SRL's effective interest, 13.8msf). Most projects of SRL enjoy favorable locations (city-centric, easy accessibility etc) – a key criteria for acquisition as well as reason for price premium over peers.
- Unlike peers which turned cautious during the downturn, SRL continued to build its portfolio via auctions, JV/ JDAs, SRA (23msf/5.4msf in FY09/FY10).
- SRL's flagship project, Signature Island, is a high-end luxury residential offering (0.71msf of saleable area; effective interest, 0.62msf) in BKC, an MMRDA master-planned commercial region in Mumbai.
  - SRL has pre-sold 30 of 80 apartments in the project at an average price of ~Rs36,000 psf, with the last sale having been concluded at Rs42,000 psf
  - Construction is progressing well and the project is expected to complete by FY12
  - Overall, we expect net cashflows of more than Rs16bn from the project over FY11-14.
- SRL has a busy pipeline of projects scheduled for launch in the next 12-15 months. The company plans to launch 11 projects over the period. Some key launches are Sunteck City, Goregaon (~1.6msf, 100% owned); Signia City, Mulund (~2msf, Phase I 1msf, effective stake 25%); and Sunteck City, Thane (8msf, phase I 1.2msf, effective stake 37.5%).
- To date, SRL has booked sales of more than Rs16bn and received ~Rs5bn in advances. With an aggressive launch pipeline, the company expects to generate significant cashflows over FY12-14 (~US$1bn).
- With low debt on the books (~Rs3bn; SRL's share, ~Rs1.7bn), SRL plans to utilize project cashflows to materially step up land acquisitions and new project launches.
- SRL expects a significant jump in reported financials from FY12 as it follows the project completion method of revenue recognition. Its first project, Signature Island, is expected to be completed in H2FY12.
- Our FY12E NAV for SRL is Rs776 per share. We expect SRL to provide steady upsides to our NAV by adding NAV-accretive projects.

Key financials

As on 31 March	FY09	FY10	FY11E	FY12E
Net Sales (Rs. mn)	206	284	236	17,964
Adj net profit (Rs. mn)	150	40	122	8,086
Shares in issue (mn)	12	63	63	63
Adj EPS (Rs)	12.5	0.6	1.9	128.4
% change		*(94.9)*	*204.8*	*6,512.6*
PE (x)	33.3	652.9	214.2	3.2
Price/Book (x)	2.5	4.1	4.0	1.8
EV/EBITDA (x)	77.6	350.3	348.8	1.5
RoE (%)	15.1	1.0	1.9	76.7
RoCE (%)	4.1	1.1	0.6	91.5

Source: Company, IDFC Securities Research

Midcaps

TALWALKARS — UNRATED (RS224, MCAP: RS5.4BN / US$119MN)

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- Talwalkars, a joint venture between the Talwalkars and Gawande families, is a prominent fitness and wellness player in India. It was listed in May 2010, the first to do so in the space. Talwalkars started with five health clubs in 2003 and now operates around 79 health clubs in India, with a total floor space of ~0.45m sqft as of 31 December 2010. Talwalkars has a market share of approximately 8-10% in the organized health club market in India.
- **Better control ensures quality service**: Talwalkars uses the hub & spoke model unlike the franchised model adopted by Gold Gym, its closest competitor. This enables it to have better control over its health clubs. Currently, Talwalkars has approximately 80% of the health clubs under its ownership. It also has an employee training academy with a floor space of ~25,000 sqft in Thane, Maharashtra, which ensures standardization of service quality across health clubs.
- **Penchant demand**: With the spurt of lifestyle diseases and higher disposable income, health clubs have seen good traction in memberships. Talwalkars' average membership fee is ~10% lower than that of its closest competitors. It has a healthy membership renewal rate of ~ 70%. In line with its strategy of focusing on the middle-income segment, the company is planning to increase its penetration in Tier II and Tier III cities.
- **Drivers of profitability**: Personnel expenses at 25% of revenues form the main cost element. The lease rates at which the space for health clubs are secured is an important driver of profitability. The company pays an average rent of Rs33-35 psf.
- **Service extension strategies**: Apart from offering gym services, Talwalkars has also started offering yoga and aerobics in their health clubs. It has also initiated spa services and currently has 14 spas in operation. This has transformed Talwalkars into a fitness chain that offers the entire gamut of services.
- **Expansion plans in place**: Talwalkars plans to increase the number of health clubs to 140 by FY12 from 76 now. The management is anticipating a capex of Rs750m every year for expansion. The company incurs a capex of approximately Rs18.5m-20m per health club and requires around 750-800 members to break even. The normal payback period for investment is around four years after taking into account interest costs.

Key financials

	FY06	FY07	FY08	FY09	FY10
Net Sales (Rs. mn)	102	221	382	595	661
Adj net profit (Rs. mn)	4	11	45	67	79
Shares in issue (mn)	16	16	16	16	18
Adj EPS (Rs)	0.27	0.69	2.87	4.28	4.42
% change		*NM*	*NM*	*49.1*	*3.3*
PE (x)	748.0	292.7	70.4	47.2	45.7
Price/Book (x)	67.8	54.7	27.3	18.6	4.3
EV/EBITDA (x)	168.4	89.2	40.3	31.4	21.3
RoE (%)	6.9	16.5	48.0	41.8	25.4
RoCE (%)	9.2	13.4	18.9	14.5	16.5

Pharma

TORRENT PHARMA — OUTPERFORMER (RS202, MCAP: RS4.9BN / US$107M)

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- Torrent Pharma (TPL) continues to enjoy a dominant position in CNS and CVS, which contribute 60% of domestic sales. The GI segment accounts for 5-7% of domestic sales. TPL continues to feature among the top 3 players in CNS and CVS (IMS-ORG data). It has increased its field force by 1200 to 3600 in the year to December 2010.
- TPL has commercialized 27 products in the Brazilian market and expects to launch 35-40 over the next 4-5 years, including 4-5 in the next 12 months. The management has said its existing basket of 27 products covers a US$1bn market opportunity and the expected pipeline over the next 4-5 years would target up to US$3bn.
- It derives 80% of its German business from tender sales and the balance from high-margin open-market operations. TPL has been able to successfully register 10% yoy revenue growth despite 40% yoy price declines on the back of strong volume growth (up to 50%) in the past few quarters.
- TPL remains positive on the US markets. It has 25 products approved for launch, of which 10 are under patent, four under cost restructuring and 11 products being currently marketed.
- The company has signed two deals to date, one with Astra Zeneca and the other with a large European pharma company (name not disclosed).
- It has an agreement to supply nine products in 18 countries with AZ, and a contract to supply 50 products in 50 emerging market countries with the European pharma company.
- TPL plans to invest Rs10bn over the next five years. The Dahej facility is expected to see investments of up to Rs8bn.
- Torrent Pharma is a net cash company with Rs200m of cash on the books. It plans to fund its expansion via internal accruals and debt.

Key financials

As on 31 Mar	FY08	FY09	FY10	FY11E	FY12E
Net sales (Rs m)	13,123	15,865	18,330	21,503	25,968
Adj. net profit (Rs m)	1,347	1,844	2,312	2,968	3,826
Shares in issue (m)	85	85	85	85	85
Adj. EPS (Rs)	15.9	21.8	27.3	35.1	45.2
% change	*44.0*	*36.9*	*25.4*	*28.4*	*28.9*
PE (x)	34.3	25.1	20.0	15.6	12.1
Price/ Book (x)	9.1	7.1	5.6	4.3	3.3
EV/ EBITDA (x)	30.4	22.7	14.1	13.2	9.8
RoE (%)	29.3	31.8	31.2	31.1	30.9
RoCE (%)	14.3	16.2	20.9	19.4	21.8

Pharma

UNICHEM LABORATORIES — OUTPERFORMER (RS196, MCAP: RS7.1BN / US$156.8M)

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- Unichem Labs is one of the India's leading integrated pharma companies, with a strong presence in the domestic formulations market. It is ranked 25th in the domestic formulations market (IMS data, December 2010). It derives 76% of its revenues from the domestic market, 20% from regulated markets and the rest from emerging markets.
- Unichem's five brands – Ampoxin, Losar H, Losar, Trika and Unienzyme – feature among the top 300 (ORG IMS data). Unichem's top 10 brands – Ampoxin, Losar, Losar H, Trika, Unienzyme, TG-Tor, Vizylac, Telsar, Telsar H and Serta – contribute 51% of domestic sales. The largest brand/ brand extensions clock revenues in excess of Rs1.48bn, while 13 brands contribute more than Rs100m/ year. Unichem enjoys the No. 1 position in 19 therapeutic sub-groups.
- The company clocked a revenue CAGR of 12% in FY05-10, with its focus portfolio clocking over 20% yoy growth in 9MFY10. Unichem achieved decent growth rates in the domestic market despite the impact of DPCO. About 20% of its domestic portfolio (in value terms) is under price control. Its key products, Metronidazole (API), Ampoxin (anti-infective) and Zator Plus (Spirolactum with Torsilomide), are also under price control.
- The management remains focused on the domestic market, and has taken several measures to enhance its footprint:
  - Potential entry into uncovered market segments like hospitals and gynecology
  - Product portfolio optimization and field resource allocation relating to chronic therapy
  - Focus on field productivity and enhanced field force to support growth
  - Optimal use of manufacturing assets.
- Unichem maintains a balanced mix of chronic and acute therapies in the domestic formulation market, with chronic care accounting for 58% of sales and acute therapy contributing the rest.
- Sales have suffered over the past few quarters due to pricing pressure on Ampoxin, especially the injectable formulation, which has led to value erosion. The company is now focused on reversing this and is hopeful of stemming the decline by FY12. This should provide support to overall domestic business growth.
- Unichem has added nearly 400 people in the domestic business in Q4FY10. The full impact of these additions on productivity would be visible from FY12. Unichem is also looking to hire 200 people, including 150 for the gynecology segment. The company has also set up a team to cater to the hospital segment.
- The management also cautioned that the acute segment, which accounts for ~42% of the business, has not been growing over the past few months and may impact overall growth.
- On the international front, Unichem has more than 565 product registrations across the world and more than 416 regulatory filings (DMFs, EDMFs. e-CTDs, ACTDs, etc). It has filed 15 ANDAs so far, of which nine have been approved. The company is positive about the product pipeline and has guided for R&D spend of up to 4% of sales going forward.
- Unichem is also hopeful of closing 2-3 contract manufacturing deals in antibiotics and non-antibiotics over the next 2-3 quarters. These deals can add Rs1.2bn-1.5bn revenues at peak sales, with potential increases as the deals are expanded.
- RoW currently contributes 4% of overall sales. The company is looking to expand this sharply over the next 4-5 years as it seeks to leverage its 700-800 registrations (secured / under way) in this market segment.

Key financials

As on 31 March	FY06	FY07	FY08E	FY09E	FY10E
Net sales (Rs m)	5,447	6,223	6,660	7,296	7,602
Adj. net profit (Rs m)	680	692	550	1,076	1,074
Shares in issue (m)	36	36	36	36	36
Adj. EPS (Rs)	18.9	19.2	15.3	29.9	29.8
% change	-	*1.8*	*(20.5)*	*95.6*	*(0.2)*
PE (x)	12.8	6.6	6.6	5.3	4.5
Price/ Book (x)	1.7	1.5	1.3	1.0	0.8
EV/ EBITDA (x)	8.1	4.7	4.5	3.2	2.3
RoE (%)	13.9	24.0	20.5	21.3	20.2
RoCE (%)	16.7	27.1	23.8	24.9	23.8

Pharma

UNITED PHOSPHORUS — OUTPERFORMER (RS131, MCAP: RS58BN / US$1.3BN)

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- UPL has maintained its revenue guidance of 5% for FY11, while providing no guidance for FY12. However, the management indicated 18% volume growth (adjusted for adverse FX impact and pricing declines) in 9MFY11. The company expects to maintain these growth levels.
- The company's North America, India, Europe and RoW operations registered -3%, 20%, -25% and 14% yoy growth and contributed 22%, 30%, 19% and 29% respectively to consolidated sales in 9MFY11.
- A sharp 25% yoy decline in the EU business was driven by a combination of price declines and volume correction. The sales decline was a result of: 1) prolonged winters and floods in certain parts of the continent; 2) negligible pest infections in French markets (UPL's biggest market in the EU), which led to low offtake despite a very good harvest; and 3) regulatory restrictions by the French government to limit creditor cycle to 45-60 days, a measure intended to protect small domestic players.
- UPL had staffed its distributor chains in anticipation of higher sales in the US and EU, which led a yoy increase in inventory cycle by 10 days to 109 as of December 2010. It is looking to lower this to 90 in the next few quarters.
- The management said that widening both geographical reach and portfolio was critical in mitigating increasing business risk from adverse climatic conditions. Importantly, it emphasized the increasing importance of the distribution network in quickly responding to changing market conditions. UPL said its ability to adapt was far superior in India, LatAm and EU, where it has its own manufacturing facilities.
- UPL recently launched its second patented product for wheat, and sees a significant opportunity there. The company said it remains optimistic on the macro outlook, with patented products worth up to US$3bn-4bn in sales expected to go off patent over next couple of years.
- The company's gross debt and cash position were Rs28bn and Rs19bn respectively as of December 2010. The management said that the primary motive of retaining significant cash on the books was to fund inorganic growth opportunities and for repayment of debt (~Rs2bn) over the next few months.
- UPL's average cost of debt is 6-7%.
- The company has guided for a capex of Rs2bn in FY12.

Key financials

As on 31 Mar	FY08	FY09	FY10	FY11E	FY12E
Net sales (Rs m)	37,306	49,322	54,602	55,867	64,375
Adj. net profit (Rs m)	3,945	4,957	5,563	5,634	7,985
Shares in issue (m)	439	439	439	439	439
Adj. EPS (Rs)	9.0	11.3	12.7	12.8	18.2
% change	*16.0*	*25.7*	*12.2*	*1.3*	*41.7*
PE (x)	14.6	11.6	10.4	10.2	7.2
Price/ Book (x)	2.6	2.2	1.8	1.6	1.3
EV/ EBITDA (x)	9.7	7.7	6.4	6.0	4.8
RoE (%)	21.1	20.1	19.1	16.5	19.9
RoCE (%)	14.8	17.2	15.0	15.2	16.7

Construction

UNITY INFRAPROJECTS

UNRATED (RS63, MCAP: RS4.7BN / US$103M)

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- Unity Infraprojects is a fast-growing construction company that has benefited from the large infrastructure development opportunity in India across sectors, including roads, airports and irrigation.
- Some showcase projects completed by Unity Infraprojects include structural works for Terminal 1B at Mumbai Airport (as part of modernization of the airport under private developer GVK), and construction of the Major Dhyanchand National hockey stadium for the recently held Commonwealth Games in New Delhi.
- Unity has order backlog of Rs39.6bn (unadjusted for 3QFY11 revenues) as of January 2011. About 48% of the backlog consists of civil works, while water (46%) and transportation (6%) constitute the rest. The company received order inflows of Rs11.44bn in 9MFY11 and is an L1 bidder for Rs3bn worth of orders.
- The company is the highest bidder for a road project in Rajasthan (offered by the state PWD) to be developed on BOT (toll) basis. The project is a 74km long 2-laning project and is valued at Rs1.5bn. The concession period is 25 years, including a construction timeline of 2.5 years. The project entails a Rs190m grant from the state government.
- Unity is looking to focus on state highway projects to develop its asset portfolio. Accordingly, it is looking to tie up with a European company to bid for NHAI projects.
- The management has indicated that the construction business is undergoing a strenuous phase currently due to following reasons:
  - The government apparatus appears to have virtually reached a state of ‘paralysis’. Major project announcements are not being followed up with sufficient activity that would lead to construction on the ground
  - Very few decisions are being taken by the government with regards infrastructure, which has led to a slowdown in order inflows
  - Therefore, lot of construction capacity across the country is lying idle
  - Specific regions are facing their own unique set of challenges; e.g., work in Maharashtra, including Mumbai, has been affected by a ban on sand dredging
  - Average interest rates have increased by 1% over the past four months, leading to higher interest costs.

Key financials

As on 31 March	FY08	FY09	FY10
Net sales (Rs m)	8,624	11,479	14,912
Adj. net profit (Rs m)	600	697	851
Shares in issue (m)	13	13	74.1
Adj. EPS (Rs)	9.0	10.4	11.5
% change	41.9%	16.0%	10.3%
PE (x)	7.0	6.1	5.5
Price/ Book (x)	1.2	1.0	0.8
EV/ EBITDA (x)	5.4	5.2	4.8
RoE (%)	18.3%	18.0%	17.3%
RoCE (%)	21.7%	18.8%	17.6%

Consumer

VADILAL INDUSTRIES — UNRATED (RS92, MCAP: RS697M / US$16M)

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- **One of the most renowned ice-cream brands in India:** Vadilal is one of the most renowned ice cream brands in India with a market share of more than 8% of the Rs25bn organized ice cream industry. It is the second largest player by volume (31m litres sold in FY10) and the third largest by value. Vadilal's ice cream business has been growing by 18% CAGR over the past five years (Rs2bn of sales in FY10). The group has marketing rights across India, barring Maharashtra and four southern states. It also has a presence in the processed foods segment through export of frozen foods. Vadilal Industries is the manufacturing and supply chain arm, while marketing is handled by Vadilal Enterprises.
- **Front end in place…**: The biggest challenge in the ice cream business is building the supply chain and distribution network. Vadilal has over the years created one of the strongest cold chain networks of 32 C&F agents and 550 distributors. It currently distributes its products through 50000 retail outlets (a large number for a frozen food item that needs refrigeration facilities) and 210 ice cream parlors under the brand Happinezz. Vadilal intends to increase its network to 300 outlets. It would also derive growth via more launches in impulse purchase segments like yogurt.
- **…and also end-logistics:** Vadilal has manufacturing facilities in Gujarat and UP and has nearly doubled capacity to 325000 litres per day in the past two years. It Vadilal is also planning to add capacity in eastern India as proximity to the market is critical to improve market share. Vadilal has in the past year spent Rs550m on capacity expansion and IT enhancement.
- **Ice cream – long-term high growth potential:** Despite being sweet and frozen, which gels well for the Indian taste buds, the organized ice cream industry is only worth Rs25bn. The biggest hurdle to growth is the lack of refrigeration facilities at the retail end and load shedding. Given they have to incur high losses even if there is no power for a few hours, retailers in many cities do not store ice cream, which has led to inefficient distribution. As power supply issues get resolved across the country and front-end retail infrastructure improves, we expect multifold growth of the category. Higher volumes would also imply better margins.
- **Negative cash flows in the initial years:** Given the low asset turns (4-5x), high working capital and low margins, ice cream is a negative cash flow business in the initial years. Vadilal has been on an aggressive capex mode and hence has a debt of Rs1bn on its books. However, cash flow tends to improve in the long run as margins improve. Improved cold storage facilities and storage at the retail end would also boost the working capital cycle.

Metals

WELSPUN CORP — OUTPERFORMER (RS167, MCAP: RS38BN / US$830M)

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- Welspun's management has indicated that a significant demand recovery was under way across geographies. A huge replacement demand in the Gulf of Mexico and an uptick in shale gas capex are two key positive triggers that could result in increased demand for pipelines in the years to come. The company is positive about the TransCanada order coming through and is banking on leveraging its superior positioning in the LSAW space. Welspun is also actively bidding for projects in Europe, where entry barriers have eased.
- The management reaffirmed that it is unlikely to compromise on profitability for higher volumes and a larger order book by trying to bid extensively for low-margin domestic orders.
- Welspun had an order book of Rs50bn (0.68x FY10 revenues) at the end of Q3FY11, comprising 776,000 tonnes for pipes and 40,000 tonnes for plates. In terms of volumes, LSAW accounts for 283,000 tonnes, HSAW 458,000 tonnes and ERW 34,000 tonnes. During the quarter, the company received new export orders worth Rs16.7bn from several domestic and North American oil & gas players. It believes the recovery in the US, including replacement demand and breakthrough in shale gas discoveries, is likely to lead to higher order inflows and impart higher visibility on revenue growth.
- The company is planning to double its LSAW capacity at Anjar to 0.7m tpa (from 0.35m tpa) by Q1FY12. The recently commissioned 0.1m tpa HSAW plant in Mandya (Karnataka) is on track, with utilization of ~50% in Q3FY11. Welspun also plans to set up a 0.1m tpa HSAW plant in Madhya Pradesh by FY12. In terms of overseas expansion, the company has a 50% stake in pipe and coating JV companies Welspun Middle East Pipes Company LLC and Welspun Middle East Pipes Coating Company LLC in Saudi Arabia, with an ~investment of US$58m. The company will invest another US$100m to set up the 0.27m tpa HSAW plant. Trial production has already started and the company expects production to ramp up in Q1FY12.
- Welspun Infra (MSK projects) had revenues of Rs640m, with operating margins close to 9.5%. It has an order book of close to Rs2000m (~1x FY10 revenues) which it plans to increase to 2x FY11 revenues over the next few quarters. These plans provide higher revenue growth visibility.
- Parvez Umrigar has joined Welspun Infra as CEO from Gammon Infrastructure.

Key financials

As on 31 Mar	FY08	FY09	FY10	FY11E	FY12E
Net sales (Rs m)	40,104	58,783	73,503	83,204	91,662
Adj. net profit (Rs m)	3,513	2,336	6,108	6,529	6,928
Shares in issue (m)	187	187	225	225	225
Adj. EPS (Rs)	18.8	12.5	27.2	29.1	30.8
% change	*146.6*	*(33.5)*	*117.6*	*6.9*	*6.1*
PE (x)	8.9	13.4	6.2	5.8	5.4
Price/ Book (x)	2.1	2.0	1.8	1.4	1.2
EV/ EBITDA (x)	7.7	7.6	5.0	4.6	3.6
RoE (%)	34.3	15.4	33.3	27.4	23.4
RoCE (%)	19.3	12.1	22.4	20.6	22.4

Financials

YES BANK — OUTPERFORMER (RS236, MCAP: RS80BN / US$1.7BN)

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- **Front-ended growth in FY11; focus on SME segment:** Yes Bank's management has indicated that loan growth in FY11 is expected to be front-loaded due to rising interest rates and tight liquidity. It is targeting loan growth of 60% in FY11 and 30% in FY11. SME loans are expected to be the main driver of growth. The bank aims to increase its proportion from 10% of the loan book currently to ~30% by FY15. The bank is also targeting a loan mix of 40:30:30 for the large, mid and small corporate loans by FY15.
- **Margins to stay stable:** A sharp rise in wholesale interest rates resulted in a 20bp qoq decline in Yes bank's margins in Q3FY11. However, the management expects short-term interest rates to trend downwards in the near term, which, along with the recent rise in lending rates, is expected to keep margins stable at 2.7-2.8% in the near term. The company expects to maintain margins at 3% in FY12.
- **Healthy asset quality; low exposure to sensitive sectors:** Yes Bank has been able to maintain it asset quality to date – gross NPA of 0.23% and net NPA of 0.06% as of Q3FY11. The company is confident of maintaining robust asset quality standards. Regarding exposure to sensitive sectors, the management indicated that the bank has zero exposure to new 2G telecom players and low (2.5% of advances) exposure to the real estate segment. The bank has a small Rs29bn (~1% of total advances) exposure to the MFI segment and expects a part of it to get restructured in FY12. Overall, despite the potential stress in the MFI portfolio, total provisions in FY11 and FY12 are expected to be less than in FY10.
- **Building a strong liability base:** Deposits generated through branch network currently contribute a relatively low proportion (~25%) to Yes Bank's total deposit base. In order to fortify its liability base, the management plans to increase this to ~35% of the total deposit base by FY12 and ~50% by FY15. Expansion of branch network and leveraging of its existing client base are expected to drive this growth. The bank aims to open ~65 branches over the next two quarters (+250 by June 2011) and reach a branch network of 300+ branches by FY12.
- **Fee income to gain traction:** Yes Bank reported strong growth in fee income in Q3FY11 with the impetus being led by transaction banking and financial market fees. Going forward, the management aims to increase the size of its non-fund exposure, which, along with expanding branch network, should provide significant traction to trade, guarantee and transaction banking fees. Financial advisory fees (especially IB revenues) are also expected to remain robust.

Key financials

As on 31 Mar	FY08	FY09	FY10	FY11E	FY12E
Net profit (Rs mn)	2,000	3,038	4,777	7,302	9,893
yoy growth (%)	*112*	*52*	*57*	*53*	*35*
Wtd avg shares (m)	288	297	340	340	340
EPS (Rs)	6.9	10.2	14.1	21.5	29.1
EPS growth (%)	106.2	203.6	37.5	52.8	35.5
PE (x)	34.0	23.1	16.8	11.0	8.1
Book value (Rs/share)	45.8	54.7	91.0	109.2	134.0
Adj. Book value (Rs/share)	44.6	54.2	91.1	109.2	134.5
P/ Adj. Book (x)	5.3	4.4	2.6	2.2	1.8
RoE (%)	19.0	20.6	20.3	21.5	24.0

Source: IDFC Securities, Price as on 9th Feb 2011

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Explanation of Ratings:

1. Outperformer: More than 5% to Index
2. Neutral: Within 0-5% to Index (upside or downside)
3. Underperformer: Less than 5% to Index

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