investor's eye

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Index

Take Five

Scrip	Reco Date	Reco Price	CMP	Target
BEL	26-Sep-06	1,108	**1,110**	1,525
ICICI Bank	23-Dec-03	284	**777**	*
India Cements	28-Sep-06	220	**215**	315
ITC	12-Aug-04	69	**190**	220
TV18	23-May-05	214	**700**	704

*Target under review

JK Cement

Cannonball

Stock Update

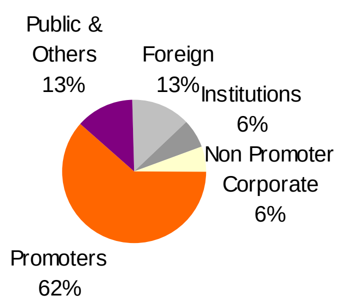
Whopper results

Buy; CMP: Rs190

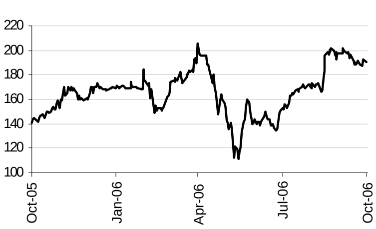
Company details

Price target:	Rs295
Market cap:	Rs1,329 cr
52 week high/low:	Rs231/109
NSE volume: (No of shares)	74,700
BSE code:	532644
NSE code:	JKCEMENT
Sharekhan code:	JKCEMENT
Free float: (No of shares)	2.7 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-3.6	26.4	1.9	39.8
Relative to Sensex	-7.9	3.3	-8.4	-18.7

Result highlights

- JK Cement reported a pre-exceptional net profit of Rs30 crore for Q2FY2007, much higher than expected. The same was better than expected because of higher-than-expected cement volume and realisation. Also its white cement business delivered a good performance during the quarter.
- Impressed by JK Cement's Q2FY2007 results we are upgrading our earnings estimates for FY2007 and FY2008 by 59% and 49% respectively. Our earnings per share (EPS) estimates now stand at Rs21.3 for FY2007 and Rs31 for FY2008.
- The revenues for Q2FY2007 grew by a healthy 30% year on year (yoy) to Rs268 crore driven by a growth of 36.6% in the cement realisation. Overall cement volume declined by 4.6% because of excessive rains and floods in Rajasthan and Gujarat.
- The grey cement volume declined by 6.4% whereas its realisation grew by a massive 37%. On the other hand, the white cement volume and realisation grew by 29.6% and 9% respectively yoy.
- The company's leverage to cement prices led to a massive 125% jump in its operating profit to Rs63.5 crore whereas the operating profit margin (OPM) expanded by 10% points to 23.7%. The earnings before interest, tax, depreciation and amortisation (EBITDA)/tonne more than doubled to Rs726 from Rs308 in the same quarter last year.
- The net interest cost stood at Rs9.2 crore whereas the depreciation charge stood at Rs8.1 crore, in line with our expectations.

Result table Rs (cr)

Particulars	Q2FY07	Q2FY06	% yoy	H1FY07	H1FY06
Net sales	**268.2**	**205.8**	**30.3**	**547.7**	**406.1**
Total expenditure	204.7	177.6	15.3	418.5	352.9
Operating profits	63.5	28.2	125.2	129.2	53.2
Other income	1.1	2.7	-59.3	1.8	4.2
EBIDTA	64.6	30.9	109.1	131.0	57.4
Interest	9.2	15.4	-40.3	17.4	28.5
PBDT	55.4	15.5	257.4	113.6	28.9
Depreciation	8.1	7.8	3.8	16.3	15.4
PBT	47.3	7.7	514.3	97.3	13.5
Tax	17.3	0.8	2062.5	34.3	1.5
Deferred tax		2.0		0.0	2.0
PAT	**30.0**	**4.9**	**512.2**	**63.0**	**10.0**
Extraordinary items	4.0	0.0			0.0
Reported profit after tax	34.0	4.9	593.9		10.0
EPS	4.3	0.70		9.01	1.43
Margins					
Operating Margins (%)	23.7	13.7		23.6	13.1
EBIDTA (%)	24.1	15.0		23.9	14.1
PATM (%)	11.2	2.4		11.5	2.5

- The pre-exceptional net profit for the quarter stood at Rs30 crore, up a whopping 512% yoy. The quarter included a one-time extraordinary other income of Rs4 crore in the form of a refund given by the Rajasthan State Electricity Board (RSEB) towards a waiver on electricity duty pertaining to an earlier period. We have treated this as an extraordinary item and accounted for it below the line. The reported net profit grew by 594%.

In the wake of the narrowing cement demand-supply gap and rising capacity utilisation levels of cement producers, cement prices have stayed firm across the country. This signifies the extent of cement consumption the country is witnessing. Going forward, the firm cement prices and volume growth from the recent capacity expansion would drive JK Cement's top line. This coupled with the company's drive to bring down its power cost by installing a captive power plant (CPP) and a waste heat recovery unit would result in substantial margin improvement and drive the earnings at a compounded annual growth rate (CAGR) of 158% over FY2006-08.

At the current market price of Rs190 the stock is discounting its FY2007E earnings by 8.9x and FY2008E earnings by 6.1x. On enterprise value (EV)/tonne basis, the stock is trading at an attractive valuation of USD79 (FY2008E) per tonne of cement. We believe the valuation is attractive as in the next 18 months the company will completely transform itself with 100% captive power arrangement, access to blending material for higher blended cement ratio, a lot cleaner balance sheet owing to constant repayment of debt and a strong improvement in the return ratios. We maintain our Buy recommendation on the stock with a price target of Rs295.

Buoyant realisation boosts revenues by 30% yoy

JK Cement witnessed a healthy 30% year-on-year (y-o-y) jump in its revenues to Rs268.2 crore driven mainly by a 36.6% y-o-y growth in its cement realisation per tonne. The overall cement volume declined by 4.6% because of excessive rains and floods in Rajasthan and Gujarat during the monsoons.

The volume of grey cement declined by 6.4% whereas its realisation grew by a massive 37% to Rs2,752 per tonne. On the other hand, the white cement volume grew by a healthy 29.6% to 60,900 tonne on the back of capacity expansion; the white cement realisation too grew by a healthy 9% yoy. JK Cement is one of the two major players present in the white cement market.

Particulars	Q2FY2007	Q2FY2006	% yoy chg
Volume break-up			
Grey	814000	870000	-6.4
White	60900	47000	29.6
Realisation per tonne			
Grey	2752	2011	36.8
White	7274	6638	9.6

Operating profit jumps by 125%

Buoyed by the huge improvement in cement (grey and white) realisation, JK Cement's operating profit grew by a staggering 125% to Rs63.2 crore as the OPM improved by 10% points to 23.7%. On the cost front, the cost per tonne went up by 20.8%, against a growth of 36.6% in the cement realisation. Majority of the cost increase can be attributed to a more than 50% increase in the raw material cost per tonne and a 32% rise in the freight cost per tonne. Hence the EBIDTA per tonne grew by a very impressive 137% to Rs726 per tonne yoy.

Per tonne analysis

Particulars	Q2FY07	Q2FY06	% yoy chg
Raw material consumed	337.2	214.8	57.0
Stock adjustment	-27.4	28.4	-196.7
Stores	225.2	200.7	12.2
Employee expenses	134.9	112.3	20.1
Power, oil & fuel	839.0	716.5	17.1
Freight	602.4	456.9	31.8
Other expenses	228.6	207.2	10.3
Total exp	2339.7	1936.8	20.8
Realisation	3065.0	2244.0	36.6
EBIDTA/Tonne	725.8	307.5	136.0

Net profit up 512%

JK Cement's net interest cost during the quarter reduced by 37% yoy to Rs9.2 crore. The interest expense stood at Rs14 crore whereas the interest earned on unutilised money mobilised from the public stood at Rs5 crore. The other income, which stood at Rs5.1 crore, included a one-time income of Rs4 crore arising out of refund given by the RSEB towards a waiver on electricity duty pertaining to an earlier period. We have treated this as an extraordinary item and accounted for it below the line. Adjusting for the same, the net profit for the quarter grew by a staggering 512% yoy to Rs30 crore. The reported net profit grew by 594%.

Upgrading earnings by 59% for FY2007 and 49% for FY2008

Impressed by JK Cement's Q2FY2007 results we are upgrading our earnings estimates for FY2007 and FY2008 by 59% and 49% respectively. Our EPS estimates now stand at Rs21.3 for FY2007 and Rs31 for FY2008.

Particulars	FY2007	FY2008
Earlier EPS	13.4	20.9
Revised EPS	21.3	31.0
Upgrade (%)	59.0	49.0

First phase of capex complete

In FY2007 JK Cement mobilised Rs290 crore through a follow-on public issue for its capital expenditure (capex) plan that shall be implemented in two phases. The first phase of the plan involves enhancing the capacity of the grey and white cement plants by 0.5 million tonne and 50,000 tonne respectively. The second phase includes setting up a 20MW pet coke-based CPP, replacement of the existing 7.5MW thermal power turbine with a 10MW turbine, and installation of a waste heat recovery power plant. The first phase of the capex is already complete and the company would enjoy the benefit of higher capacity going forward. The second phase will be completed in three parts, first the 10MW turbine will be commissioned by December 2006; the pet coke-based CPP will be commissioned by April 2007 and the waste heat recovery plant will be commissioned by June 2007. JK Cement would save significantly on the power cost. Our estimate is that after the completion of the second phase of the capex, JK Cement will be able to save at least Rs50 crore on the production of 4 million tonne of gray cement.

Work on Karnataka plant to start by December 2006

The company has proposed a 3-million-metric-tonne greenfield plant at Karnataka. It has completed 80% of the land acquisition and expects the civil construction work to start by December 2006. An advance of Rs15 crore has already been given to FL Smidth for equipment supply and JK Cement expects the plant to be commissioned by December 2008. With the cement cycle boom expected to continue for the next three to four years and the southern region remaining one of the biggest gainers of this upturn, we expect the proposed capacity to drive the revenues of the company further.

Valuation and view

In the wake of the narrowing cement demand-supply gap and rising capacity utilisation levels of cement producers, cement prices have stayed firm across the country. This signifies the extent of cement consumption the country is witnessing. Going forward, the firm cement prices and volume growth from the recent capacity expansion would drive JK Cement's top line. This coupled with the company's drive to bring down its power cost by installing a CPP and a waste heat recovery unit would result in substantial margin improvement and drive the earnings at a CAGR of 158% over FY2006-08.

At the current market price of Rs190 the stock is discounting its FY2007E earnings by 8.9x and FY2008E earnings by 6.1x. On EV/tonne basis, the stock is trading at an attractive valuation of USD79 (FY2008E) per tonne of cement. We believe the valuation is attractive as in the next 18 months the company will completely transform itself with 100% captive power arrangement, access to blending material for higher blended cement ratio, a lot cleaner balance sheet owing to constant repayment of debt and a strong improvement in the return ratios. We maintain our Buy recommendation on the stock with a price target of Rs295.

Earnings table

Year ended Mar 31	FY2005	FY2006	FY2007E	FY2008E
Net profit (Rs cr)	6.5	32.5	148.7	216.7
% y-o-y growth	-	*400.0*	*357.0*	*45.7*
Shares in issue (cr)	5.0	5.0	7.0	7.0
EPS (Rs)	1.3	6.5	21.3	31.0
PER (x)	145.9	40.8	8.9	6.1
EV/EBIDTA (x)	49.5	12.3	5.8	4.4
RoCE (%)	6.8	9.6	20.3	23.9
RoNW (%)	1.7	4.8	18.6	21.8

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

Sanghvi Movers

Ugly Duckling

Stock Update

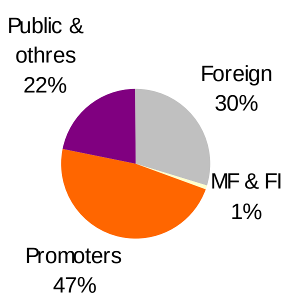
Strong operational performance

Buy; CMP: Rs762

Company details

Price target:	Rs1,150
Market cap:	Rs533 cr
52 week high/low:	Rs913/320
BSE volume: (No of shares)	19,887
BSE code:	530073
Sharekhan code:	SANGMOVE
Free float: (No of shares)	38 lakh

Shareholding pattern



Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	-5.6	13.6	-17.3	119.6
Relative to Sensex	-9.8	-7.1	-25.6	27.8

Result highlights

- The Q2FY2007 net profit of Sanghvi Movers Ltd (SML) grew by 90.1% year on year (yoy) to Rs13.1 crore, ahead of our expectations of Rs11.4 crore.
- The net revenues grew by 37.1% yoy to Rs47.3 crore driven by the addition of cranes worth Rs80 crore during H1FY2007 and a utilisation rate of 43%, which was higher than that of 40% achieved in Q1FY2007.
- The operating profit grew by 52.3% yoy driven by an 820-basis-point expansion in the operating profit margin (OPM). The OPM expanded by 170 basis points sequentially.
- Despite the addition of the new cranes, the depreciation charge was down 9.7% yoy to Rs8.5 crore, reflecting the effect of the change in the company's accounting policy for depreciation of new assets (bought after April 1, 2005), effected in Q3FY2006. The company has shifted from the written-down value (WDV) method to the straight-line method (SLM). Also it has changed the depreciation method for all assets (bought between April 1, 2002 and March 31, 2005) in the current quarter.
- Driven by the strong operational performance and aided by the lower depreciation the net profit grew by a robust 90.1% yoy to Rs13.1 crore.
- We have upgraded our estimates of earnings per share (EPS) for FY2007 and FY2008 by 4.1% and 5.2% to Rs63.7 and Rs82.9 respectively to take into account the better-than-expected OPM and the revenue growth that is in line with our estimates.
- At the current market price of Rs762, the stock is trading at 9.2x its FY2008E EPS, 6.2x FY2008E cash EPS (CEPS) and 5.0x FY2008E enterprise value (EV)/ earnings before interest, depreciation, tax and amortisation (EBIDTA). We reiterate our Buy recommendation on the stock with a price target of Rs1,150.

Result table Rs (cr)

Particulars	H1FY07	H1FY06	% yoy	Q2FY07	Q2FY06	% yoy
Net sales	87.6	62.3	40.7	47.3	34.5	37.1
Expenditure	24.8	22.5	10.3	13.0	12.0	8.7
Operating profit	62.8	39.8	57.8	34.3	22.5	52.3
Other income	0.8	0.4	107.5	0.2	0.3	-55.2
Interest	11.6	5.5	111.7	6.2	3.0	106.5
Depreciation	16.1	17.6	-8.4	8.5	9.4	-9.7
Profit before tax	35.9	17.1	109.6	19.8	10.5	88.6
Tax	9.7	8.1		5.5	4.6	
Deferred tax	2.5	-2.2		1.3	-1.0	
Profit after tax	23.7	11.1	112.4	13.1	6.9	90.1
Extra-ordinary items	17.1	0.0		0.0	0.0	
PAT (after extraordinary)	40.8	11.1	266.0	13.1	6.9	90.1
OPM (%)	71.7	63.9		72.5	65.2	

Revenue growth of 37.1% yoy, ahead of estimates

SML reported a 37.1% year-on-year (y-o-y) growth in its revenues to Rs47.3 crore in Q2FY2007, ahead of our estimates. The strong revenue growth was driven by the utilisation of the assets added during FY2006 and H1FY2007. The asset utilisation rate improved to 43% in the quarter from 40% in Q1FY2007.

OPM continues to zoom

Driven by the utilisation of the cranes added during FY2006 and H1FY2007, and the continued operational leverage that SML enjoys, the operating profit grew by 52.3% yoy to Rs34.3 crore. The OPM improved by a robust 820 basis points yoy and 170 basis points sequentially to 72.5%, ahead of our estimates.

Depreciation lower due to policy changes

Despite the addition of the new cranes the depreciation charge was down 9.7% yoy to Rs8.5 crore, reflecting the effect of the change in the company's accounting policy for depreciation of new assets (bought after April 1, 2005) effected in Q3FY2006, ie a shift from the WDV to the SLM.

Also the company has changed the depreciation method for all assets (bought between April 1, 2002 to March 31, 2005) in the current quarter.

Net profit grows by 90.1%

The strong performance at the operational level was further aided by the lower depreciation and as a result the net profit grew by a robust 90.1% yoy to Rs13.1 crore, ahead of our expectations of Rs11.5 crore.

Windmill division continues to be profitable

SML has two windmill power generation plants, one each at Rajasthan and Karnataka, with a combined capacity of 5.5 megawatt. A better plant load factor during the quarter helped the company in posting a profit in this division. The division reported a profit of Rs0.5 crore at the profit before interest and tax level in Q2FY2007 as compared with a profit of Rs0.2 crore in Q2FY2006.

Expansion of fleet continues

SML has incurred a capital expenditure (capex) of Rs16.0 crore during the quarter. After adding cranes worth Rs170 crore in FY2006, the company plans to add more cranes worth Rs150 crore in FY2007. For H1FY2007, the company has added cranes worth Rs80 crore. We believe the capacity expansion will boost growth in FY2008 as well. Such an aggressive expansion plan is clearly indicative of the visibility of SML's growth and the buoyant demand for its cranes.

Expansion is partly funded through debt

The capex has been funded partly through debt and partly through internal accruals. Though the interest cost went up substantially in Q2FY2007, we are not worried, as the interest coverage ratio remains comfortable at 3.6x.

Valuation and view

We have upgraded our EPS estimates for FY2007 and FY2008 by 4.1% and 5.2% to Rs63.7 and Rs82.9 respectively to take into account the better-than-expected OPM and the revenue growth that is in line with our estimates.

At the current market price of Rs762, the stock is trading at 9.2x its FY2008E EPS, 6.2x FY2008E CEPS and 5.0x FY2008E EV/EBIDTA). We reiterate our Buy recommendation on the stock with a price target of Rs1,150.

Earnings table

Year ended Mar 31	FY2005	FY2006	FY2007E	FY2008E
Net profit (Rs cr)	13.7	31.9	50.3	65.5
Share in issue (cr)	0.7	0.7	0.8	0.8
EPS (Rs)	18.7	43.8	63.7	82.9
% y-o-y growth	*111.1*	*133.6*	*45.6*	*30.1*
PER (x)	40.7	17.4	12.0	9.2
CEPS (Rs)	38.6	75.2	94.7	122.8
P/CEPS (x)	19.7	10.1	8.0	6.2
Book value (Rs)	77.8	110.7	209.2	282.1
P/BV (x)	9.8	6.9	3.6	2.7
EV/EBIDTA (x)	14.4	8.0	6.1	5.0
Dividend yield (%)	0.7	1.3	1.3	1.3
ROCE (%)	19.7	26.4	26.4	25.1
RONW (%)	24.1	39.6	30.5	29.4

Hindustan Lever

Apple Green

Stock Update

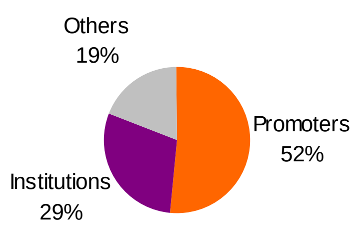
Price target revised to Rs280

Buy; CMP: Rs234

Company details

Price target:	Rs280
Market cap:	Rs51,542 cr
52 week high/low:	Rs296/158
NSE volume: (No of shares)	8.9 lakh
BSE code:	500696
NSE code:	HINDLEVER
Sharekhan code:	HLL
Free float: (No of shares)	107.2 cr

Shareholding pattern



Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	-10.7	-4.3	-20.2	48.6
Relative to Sensex	-14.7	-21.8	-28.3	-13.6

Result highlights

- The Q3CY2006 net profit of Hindustan Lever Ltd (HLL) grew by 17.5% year on year (yoy) to Rs383.0 crore, in line with our expectations.
- The net revenues grew by 12.2% yoy on the back of a 14% year-on-year (y-o-y) growth in the home and personal care (HPC) segment, which comprises the soap and detergent, and personal care businesses. Adjusted for *Nihar* (a brand sold by HLL to Marico Industries) the growth in the revenues stood at 12.8%.
- The profit before interest and tax (PBIT) grew by 15.3% yoy as the PBIT margin expanded by 44 basis points yoy to 16.2%.
- The expansion in the PBIT margin was partly a result of an improvement in the margins of the ice cream business and exports. Another reason was the turnaround in the process foods business, which had made losses in Q3CY2005.
- The PBIT margin in the soap and detergent, and personal product businesses contracted by 76 basis points and 136 basis points respectively despite price increases, as the sales and promotion expenses of these businesses went up substantially.
- We have lowered our earnings per share (EPS) estimates for CY2006 and CY2007 by 5% and 6.6% to Rs7.1 and Rs8.5 respectively to take into account the slower-than-expected expansion in the margin of the HPC segment.
- At the current market price of Rs234, the stock is quoting at 26.8x its CY2007E EPS and 24.6x CY2007E enterprise value (EV)/earnings before interest, depreciation, tax and amortisation (EBIDTA). We reiterate our Buy recommendation on the stock with a revised price target of Rs280.

Net sales grow by 12.2%

HLL's net sales grew by 12.2% yoy in Q3CY2006 driven by a strong growth in all its businesses, especially the HPC business. Adjusted for the revenues from the *Nihar* brand (which was sold off in Q1CY2006), the total sales grew by 12.8% yoy. All the fast moving consumer goods businesses of the company grew at high double-digit rates except beverages.

Result table Rs (cr)

Particulars	Q3CY06	Q3CY05	% yoy chng	M9CY06	M9CY05	% yoy chng
Net sales	3066.0	2731.5	12.2	8947.3	8074.2	10.8
Total expenditure	2663.1	2387.2	11.6	7799.3	7140.7	9.2
Operating profits	402.9	344.4	17.0	1148.1	933.5	23.0
Other income	96.8	85.5	13.2	247.6	239.5	3.4
Interest	3.4	4.8	-28.1	8.9	14.9	-40.1
Depreciation	32.0	32.5	-1.4	95.9	95.3	0.6
Profit before tax	464.2	392.6	18.2	1290.8	1062.8	21.4
Tax	81.2	66.6	22.0	234.5	214.4	9.4
Profit after tax	383.0	326.0	17.5	1056.3	848.4	24.5
Extraordinary items	-137.7	0.5	-27648.0	-285.3	-17.4	1536.8
Profit after extraordinary	520.7	325.5	60.0	1341.6	865.8	54.9

Segment revenue (Rs crore)

Particulars	Q3CY06	Q3CY05	% yoy chng	M9CY06	M9CY05	% yoy chng
HPC	2,247.1	1,971.9	14.0	6,634.2	5,746.4	15.5
Beverages	345.5	324.0	6.6	963.7	938.6	2.7
Processed foods total	97.3	81.5	19.3	282.7	227.2	24.4
Ice creams	33.8	23.0	47.1	110.7	81.0	36.8
Exports	327.4	273.1	19.9	931.6	937.7	-0.7
Others (includes chemicals, plantations etc)	48.0	89.4	-46.3	119.9	238.4	-49.7
Total	3,099.1	2,762.9	12.2	9042.9	8169.2	10.7
HPC (adjusted for *Nihar*)	2,247.1	1,955.8	14.9	6,634.2	5,710.3	16.2
Total (adjusted for *Nihar*)	3,099.1	2,746.8	12.8	9042.9	8133.1	11.2

HPC records strong growth—10.8% in volume terms

The HPC segment achieved a strong revenue growth of 14.0% yoy on the back of a volume growth of 10.8% and selective price increases. Adjusted for the sale of the *Nihar* brand (which happened in Q1CY2006), the revenue growth in the HPC segment was at 14.9%.

Segmental results—HPC business

Particulars	Q3CY2006	Q3CY2005	% yoy chg
Revenue			
Soaps and detergents	1,393.3	1,242.9	12.1
Personal products	853.8	729.1	17.1
Total	2,247.1	1,971.9	14.0
PBIT			
Soaps and detergents	183.6	173.3	6.0
Personal products	240.9	215.6	11.7
Total	424.5	388.9	9.2
PBIT margins (%)			
Soaps and detergents	13.2	13.9	-76.3
Personal products	28.2	29.6	-136.0
Total	18.9	19.7	-83.0

The PBIT in the HPC business grew by slower 9.2% yoy as the PBIT margin contracted by 83 basis points to 18.9%. The contraction in the PBIT margin was on account of higher advertising and promotional expenses for these products.

Food business—revenues and profitability going strong

The food business reported a strong growth of 25.4% yoy for the quarter backed by a strong growth in both the businesses, viz processed foods and ice creams.

The processed food business recorded a strong growth of 19.3% with all the key brands, viz *Kissan*, *Annapurna* and *Knorr*, growing strongly during the quarter. The processed food business improved its profitability substantially with a PBIT of Rs4.1 crore compared with a loss of Rs6.2 crore in Q3CY2005.

The ice cream business reported a strong growth of 47.1% yoy. The improving scale helped the company to expand the margin in this business by nearly 250 basis points.

Segmental results—food business

Particulars	Q3CY2006	Q3CY2005	% yoy chg
Revenues (Rs cr)			
Processed foods	97.3	81.5	19.3
Ice creams	33.8	23.0	47.1
Total	131.1	104.5	25.4
PBIT (Rs cr)			
Processed foods	4.1	-6.2	-166.3
Ice creams	4.7	2.6	79.3
Total	8.8	-3.6	NA
PBIT margins (%)			
Processed foods	4.2	-7.6	1,177.4
Ice creams	13.8	11.4	248.8
Total	6.7	-3.4	1,009.8

Beverages—growth catching up

The sales in the beverage segment grew by 6.6% as the revenues from the branded tea business returned to growth. The coffee business grew as the company expanded its market share by 8% to 49.4% in the instant coffee business.

Segmental results—beverages business

Particulars	Q3CY2006	Q3CY2005	% yoy chg
Revenues (Rs crore)	345.5	324.0	6.6
PBIT (Rs crore)	52.9	56.7	-6.6
PBIT margins (%)	15.3	17.5	-217.8

Price increase helps mitigate rising crude oil prices without affecting growth

The recent price increases effected by HLL have helped the company to meet the rising crude oil prices, which increased its raw material, packaging and freight costs. The impact was visible in the higher contribution of the margins, which went up by 264 basis points during the quarter. A part of the savings on the raw material cost was invested in the brand building exercise, as the company's advertising and promotional expenses went up by nearly 41% during the quarter.

Cost as % of sales

Particulars	Q3 CY06	Q3 CY05	Chg in bps	M9 CY06	M9 CY05	Chg in bps
Raw material cost	53.6	56.2	-264.0	52.9	55.3	-241.4
Employee expenses	5.7	6.3	-63.9	5.8	6.3	-52.8
Advertising and promotion	11.1	9.1	193.9	11.1	8.8	229.2
Other expenses	16.9	16.8	7.1	17.1	16.9	11.7
Total cost	87.2	88.4	-126.9	86.9	87.4	-53.3

Net profit grows by 17.5%

The net profit for the quarter under review grew at 17.5% yoy in line with the operating profit growth, as the other income, depreciation and tax rate remained stable.

Valuations

We have lowered our EPS estimates for CY2006 and CY2007 by 5% and 6.6% to Rs7.1 and Rs8.5 respectively to take into account the slower-than-expected margin expansion in the HPC segment.

At the current market price of Rs234, the stock is quoting at 26.8x its CY2007E EPS and 24.6x CY2007E EV/EBIDTA. We reiterate our Buy recommendation on the stock with a revised price target of Rs280.

Valuation table (Rs crore)

Particulars	CY2004	CY2005	CY2006E	CY2007E
Net profit (Rs crore)	1,182.7	1,310.7	1,568.7	1,870.4
% y-o-y growth	*-31.4*	*10.8*	*19.7*	*19.2*
Shares in issue (crore)	220.1	220.1	220.1	220.1
EPS (Rs)	5.4	6.0	7.1	8.5
% y-o-y growth	*-31.4*	*10.8*	*19.7*	*19.2*
PER (x)	42.4	38.3	32.0	26.8
Book value (Rs)	9.5	10.5	12.6	16.1
P/BV (Rs)	24.0	21.8	18.1	14.2
EV/EBIDTA (x)	33.9	33.2	29.8	24.6
Dividend yield (%)	2.2	2.2	2.2	2.2
RoCE (%)	45.8	68.7	66.1	61.9
RoNW (%)	56.5	56.8	56.6	52.8

Subros

Ugly Duckling

Stock Update

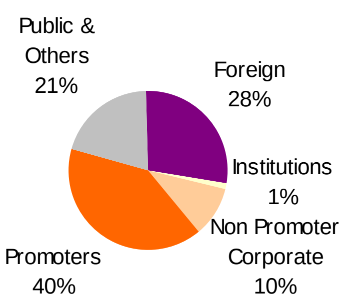
Cool gains

Buy; CMP: Rs250

Company details

Price target:	Rs370
Market cap:	Rs300 cr
52 week high/low:	Rs270/134
NSE volume: (No of shares)	10,205
BSE code:	517168
NSE code:	SUBROS
Sharekhan code:	SUBROS
Free float: (No of shares)	72 lakh

Shareholding pattern



Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	6.6	28.3	-3.5	84.2
Relative to Sensex	1.9	4.9	-13.2	7.2

Result highlights

- Subros' Q2FY2007 net profit at Rs7.8 crore is sharply ahead of our expectation, primarily because of a higher-than-expected revenue growth and a better operating profit margin (OPM).
- We are upgrading our earnings estimates for Subros by 17% for FY2007 and 13% for FY2008. Our earnings per share (EPS) estimates now stand at Rs28.1 for FY2007 and Rs40.5 for FY2008.
- The revenues for the quarter at Rs166 crore grew by 27% year on year (yoy), driven by an impressive growth in the volumes of its key clients, Maruti Udyog Ltd (MUL) and Tata Motors (TAMO), which are currently reaping the benefits of an 8% reduction in the excise duty on small cars. The total automotive air-conditioning system (AAS) volumes grew by a handsome 41% to 125,756 units and, as expected, the realisation came down by 10%.
- The volume growth (41%) reported by Subros is higher than that reported by its key clients MUL (13%) and TAMO (21%). This means it has been able to increase its combined supply share for these two auto majors from 47% a year ago to 58% in Q2FY2007.
- Driven by a slight improvement in the raw material cost and a strict control on the other operating costs, the OPM for the quarter improved by 240 basis points yoy to 11.1%. Hence the operating profit for the quarter grew by 61.5% yoy to Rs18.3 crore.
- With the commissioning of some of the capacities set up as part of the first phase of the capacity expansion programme, depreciation for the quarter inched up by 10.3% and the interest charge doubled to Rs1.71 crore.
- The net profit for the quarter grew by a handsome 93% to Rs7.8 crore.

Result table Rs (cr)

Particulars	Q2FY07	Q2FY06	% yoy chg	H1FY07	H1FY06	% yoy chg
Gross sales	**193.4**	**152.0**	**27.3**	**358.8**	**152.0**	**136.1**
Excise duty	27.8		-	51.7	0.0	-
Net sales	165.6	130.8	26.6	307.1	263.2	16.7
Total expenditure	147.2	119.5		273.6	239.3	
Operating profit	18.3	11.4	61.5	33.5	23.8	40.8
Other income	0.3	0.6	-52.5	0.6	0.9	-33.0
EBIDTA	18.6	11.9	55.9	34.1	24.7	38.2
Interest	1.71	0.8	103.6	3.0	1.6	86.4
Depreciation	6.1	5.5	10.3	11.7	11.0	6.9
PBT	10.8	5.6	93.9	19.4	12.1	60.0
Tax	3.0	1.5	96.1	5.6	3.5	60.6
PAT	**7.8**	**4.0**	**93.1**	**13.8**	**8.6**	**59.7**
EPS	5.7	6.5	3.4		11.5	7.2
Margins						
OPM (%)	11.1	8.7		10.9	9.1	
EBIDTAM (%)	11.2	9.1		11.1	9.4	
PATM (%)	4.7	3.1		4.5	3.3	

Going forward, a strong volume growth for two of its major clients, MUL and TAMO, and its own efforts to expand its portfolio through supply to Mahindra and Mahindra (M&M) will maintain the growth momentum in its earnings. Further, a sharp revival in the sales of small cars, particularly those manufactured by MUL and TAMO (Subros is virtually the only supplier to these original equipment manufacturers [OEMs]), would beef up the volume growth. Further the company is all set to add new vehicles to its supply portfolio, like *Swift* for MUL and *Logan* for M&M. To cater to these growth opportunities, Subros is all set to commence its new 2.5-lakh Gurgaon unit from December 2006 and that will take its manufacturing capacity to 7.5 lakh units from the current 5 lakh units. Further, its research and development (R&D) centre will help in indigenisation of the AAS components which will in turn help the company to capture substantial value and expand its margin. We remain positive on the company's prospects and expect its earnings to grow at a healthy compounded annual growth rate (CAGR) of 48% over FY2006-08. At the current market price of Rs250 the stock is trading at compelling valuations of 8.9x FY2007E EPS and 6.2x FY2008E EPS. The valuations are at a huge discount to that commanded by its peers. We maintain our Buy recommendation on the stock with a price target of Rs370.

Excise duty sops to automobile majors buoys Subros' revenue by 26.6%

Buoyed by the excise duty reduction on small cars Subros' revenues grew by 26.6% in Q2FY2007 driven by a handsome growth of 41% in the volumes to 125,756 units. As expected the realisation came down by 10% yoy. Usually the OEMs bargain for lower price in lieu of an increase in the volume, hence this drop in the realisation was expected. Going forward, the supply for MUL's *Swift* and M&M's *Logan*, which are high-end units, shall arrest the drop in the realisation.

Unit-wise details

Particulars	Q2FY07	Q2FY06	% yoy chg
Volume	125756	89180	41.0
Realisation	13187	14669	-10.1
Costs			
RM cost	9443	10710	-11.8
Staff cost	761	844	-9.9
Other exp	1527	1842	-17.1
Total	11731	13397	-12.4
EBIDTA	1456	1273	14.4

Operating profit grows 61%, net profit doubles

Subros' continued thrust on R&D and its strict vigil on cost are yielding handsome fruits. The operating profit registered a healthy growth of 61% yoy to Rs18.3 crore, as the OPM expanded by 240 basis points to 11.1%. The expansion has come on the back of savings in the raw material cost, which as a percentage of sales declined by 140 basis points to 71.6%. Similarly, the other expenditure as a percentage of sales also came down. Going forward, the company's continued efforts to increase indigenisation of components through the efforts of its in-house R&D centre are likely to yield good results and help the company to further reduce its raw material cost. Hence the net profit for the quarter almost doubled to Rs7.8 crore.

Upgrading earnings

Subros' Q2FY2007 net profit at Rs7.8 crore is sharply ahead of our expectation, primarily because of a higher-than-expected revenue growth and a better OPM. As the company has already achieved a net profit of Rs13.8 crore for H1FY2007, to meet our full-year net profit estimate of Rs28.6 crore it will have to register a decline of 5% yoy in the net profit for H2FY2007. Hence we are upgrading our earnings estimates for Subros by 17% for FY2007 and 13% for FY2008. Our earnings per share (EPS) estimates now stand at Rs28.1 for FY2007 and Rs40.5 for FY2008.

New plant to commence production in Q3FY2007

The volumes of automobile majors like MUL and TAMO have seen a steady growth. These companies have also undertaken huge capital expenditure (capex) plans, eg MUL plans to set up a new manufacturing plant. With its top clients embarking on capex, Subros has also drawn up a capex plan of its own. It is on the verge of commissioning the first phase of the capex wherein it would expand its capacity from 5 lakh units to 7.5 lakh units. The new facility at Gurgaon is expected to commence production by December end. The second phase of the capex will be completed by the end of FY2008 wherein the capacity will be expanded to 10 lakh units. The new plant will help Subros to save a lot on the logistic cost, as the new plant is located at Gurgaon, in the vicinity of MUL's plant. Further the supply of AAS for MUL's *Swift* by December 2006 and M&M's *Logan* by July 2007 is on schedule.

Valuation—extremely attractive

Going forward, a strong volume growth for two of its major clients, MUL and TAMO, and its own efforts to expand its portfolio through supply to M&M will maintain the growth momentum in its earnings. Further, a sharp revival in the sales of small cars, particularly those manufactured by MUL and TAMO (Subros is virtually the only supplier to these OEMs), would beef up the volume growth. Further the company is all set to add new vehicles to its supply portfolio, like *Swift* for MUL and *Logan* for M&M. To cater to these growth opportunities, Subros is all set to commence its new 2.5-lakh Gurgaon unit from December 2006 and that will take its manufacturing capacity to 7.5 lakh units from the current 5 lakh units.

Further, its R&D centre will help in indigenising the AAS components which will in turn help the company to capture substantial value and expand its margin. We remain positive on the company's prospects and expect its earnings to grow at a healthy compounded annual growth rate (CAGR) of 48% over FY2006-08. At the current market price of Rs250 the stock is trading at compelling valuations of 8.9x FY2007E EPS and 6.2x FY2008E EPS. The valuations are at a huge discount to that commanded by its peers. We maintain our Buy recommendation on the stock with a price target of Rs370.

Earnings table

Particulars	FY2005	FY2006	FY2007E	FY2008E
Net profit (Rs cr)	21.2	24.3	33.8	48.6
% y-o-y growth	*44.0*	*19.0*	*38.9*	*43.8*
Shares in issue (cr)	1.2	1.2	1.2	1.2
EPS (Rs)	17.7	20.3	28.1	40.5
% y-o-y growth	*44.0*	*19.0*	*38.9*	*43.8*
PER (x)	14.7	12.3	8.9	6.2
Book value (Rs)	91.1	107.4	138.4	183.1
P/BV (Rs)	2.7	2.3	1.8	1.4
EV/EBIDTA (x)	6.6	6.1	4.4	3.0
Dividend yield (%)	1.2	1.0	1.4	1.9
RoCE (%)	21.2	20.6	23.1	26.1
RoNW (%)	18.7	18.9	20.3	22.1

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

Ashok Leyland

Ugly Duckling

Stock Update

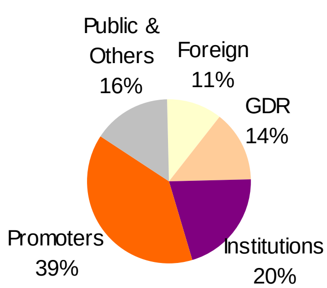
Higher truck sales impact margins

Buy; CMP: Rs44

Company details

Price target:	Rs53
Market cap:	Rs5,764 cr
52 week high/low:	Rs54/25
NSE volume: (No of shares)	13.4 lakh
BSE code:	500477
NSE code:	ASHOKLEY
Sharekhan code:	ASHOKLEY
Free float: (No of shares)	61.7 cr

Shareholding pattern



Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	2.7	31.8	-4.8	80.6
Relative to Sensex	-1.9	7.8	-14.4	5.1

Result highlights

- Ashok Leyland's (ALL) Q2FY2007 results are in line with our expectations, though the margins have been slightly lower than our expectations.
- The net sales for the quarter grew by 34% to Rs1,675.7 crore led by a volume growth of 33%.
- The operating margins have declined by 80 basis points to 8.2% as a result of higher raw material costs, particularly rubber and non-ferrous metals. Consequently, the operating profits (after adjusting for the foreign exchange [forex] gain/loss) for the quarter rose by 22% to Rs138 crore.
- With a price hike of 2.5% with effect from November and a higher contribution from the defence and bus segments in the second half, the margins should improve.
- Higher other income, lower interest costs and stable depreciation aided the company in posting a 27.1% growth in the reported net profits to Rs95.4 crore.
- At the current market price (CMP) of Rs44, the stock quotes at 11.6x its FY2008E earnings. We maintain our Buy recommendation on the stock with a price target of Rs53.

Strong volume growth drives top line

On the back of a strong volume growth of 33%, the top line witnessed a growth of 34% to Rs1,675.7 crore. The goods carrier segment, contributing about 81% of the total sales by volume, led the growth with a 62% increase year on year (yoy). However,

Result table Rs (cr)

Particulars	Q2FY07	Q2FY06	% yoy chg	H1FY07	H1FY06	% yoy chg
Net sales	**1675.7**	**1250.1**	**34.0**	**3099.6**	**2313.3**	**34.0**
Expenditure	1537.6	1137.3	35.2	2840.2	2115.0	34.3
Raw material consumed	1321.6	1096.4	20.5	2448.2	1943.7	26.0
Change in stock	-55.4	-212.6		-137.6	-307.2	
Staff cost	120.3	117.5	2.4	249.5	222.1	12.3
Other exp	151.2	136.0	11.1	280.1	256.3	9.3
Operating profit	**138.1**	**112.8**	**22.4**	**259.4**	**198.3**	**30.8**
Other income	9.9	17.0		23.7	20.3	
EBIDTA	148.0	129.8	14.0	283.1	218.7	29.5
Interest	0.4	0.7		0.9	-0.4	
PBDT	147.6	129.1	14.3	282.2	219.1	28.8
Depreciation	36.5	34.2		69.2	64.0	
PBT	111.1	94.9	17.1	213.0	155.1	37.3
Tax	33.4	21.5		59.7	48.6	
PAT	**77.7**	**73.4**	**5.9**	**153.3**	**106.5**	**43.9**
Extraordinary items*	17.7	1.6		11.2	25.8	
Net profit	**95.4**	**75.0**	**27.1**	**164.5**	**132.3**	**24.4**
EPS (Rs)	0.6	0.6		1.2	0.8	
OPM (%)	8.2	9.0		8.4	8.6	
PATM (%)	4.6	5.9		4.9	4.6	

* Includes forex gain/loss, profit on sale of stake in IndusInd

the sales of the passenger carrier segment declined by 21.8% yoy to 3,771 units. The company has revised its sales target from 77,000 to 80,000 vehicles for the current year.

The company has raised its product prices by 2.5% with effect from November 2006, the benefits of which should accrue in the next quarterly results. The company has pending orders from the defence sector, which would be executed in the second half of the fiscal. The passenger vehicle sales are also expected to be higher in the second half of the fiscal because of the orders from the state transport corporations.

Sales performance

	Q2FY07	Q2FY06	% yoy chg
MDV passenger	3,771	4,822	-21.8
MDV goods	16,010	9,838	62.7
LCV	88	235	-62.6
Total sales	19,869	14,895	33.4

Higher raw material costs hurt margins

The other expenditure for the quarter includes a forex gain of Rs3.05 crore as against a loss of Rs3.4 crore in the same quarter last year. The operating profits have grown by 22% year on year (yoy) to Rs138 crore, while the operating margins declined by 80 basis points to 8.2%. The raw material to sales ratio rose to 76.3% of sales from 75% of sales in the corresponding period last year, primarily due to the increase in the prices of rubber and non-ferrous metals. The operating margins were also impacted due to the change in the product mix in favour of goods vehicles, and the lower contribution of the sales of the defence vehicles in the current quarter. However, the same were partially offset due to the success of the cost saving drive, Mission Gemba, initiated by the company.

A lower other income (excluding the stake sale in IndusInd Bank), lower interest charges and stable depreciation led to the adjusted PAT growth of only 6% at Rs 77.7 crore. The reported PAT grew by 37.1% to Rs95.36 crore aided by the exceptional income and forex gains.

Avia acquisition

In July 2006 ALL acquired the truck business of the Czech truck maker, Avia at a price of $35 million. Out of the total acquisition cost, $25 million has already been paid while the rest would be paid in the next twelve months. ALL has acquired full control of Avia and has started production at its plant. At present the production stands at 2,000 vehicles, which would be scaled up to 5,000 units and subsequently to 10,000-15,000 vehicles in the next three years.

The acquisition would focus on the European markets. Avia has a strong presence in the European markets with 55% of its sales coming from outside the Czech Republic. As of now, ALL is not planning to introduce Avia's product in the Indian markets. For newer markets like South Africa, Turkey and Iran, ALL would be using its own power train hino 'H' series engine, while sourcing cabs from Avia.

Raising funds to finance its capex plans

ALL plans to spend Rs350 crore in the current year, as it plans to raise the capacity from the current 77,000 units to 90,000 units. The capacity would be further scaled up to 100,000 units by the end of FY2008. The capital expenditure (capex) for FY2008 would also be in the range of Rs350 crore. Apart from this, an additional capex of Rs1,000 crore will be incurred for setting up of the new plant at Uttaranchal.

To invest Rs1,000 crore for a plant in Uttaranchal

Ashok Leyland would set up a plant in Uttaranchal at a planned capex of Rs1,000. The plant would be set up on a 175-acre plot at Pantnagar, which offers excise and income tax benefits. The initial capacity of the plant would be 25,000 vehicles, which would be later ramped up to 40,000 vehicles in 2-3 years. The funding for the same would be through internal accruals and some debt.

Setting up a bus assembly unit in the UAE

To further boost its export revenues ALL is setting up a bus assembly unit at Ras Al Khaimah, the northern most emirate of the UAE. The company has signed a memorandum of understanding with Ras AL Khaimah Investment Authority for the same. The unit, with an initial annual capacity of 1,000 buses, will start operations as a bus body assembling plant using ALL's chassis and bus body CKD kits sent from India. In the second phase of the project the bus-assembling unit will be upgraded to a vehicle-assembling unit (trucks and buses). The operations are expected to start in a year's time. The unit would entail an initial investment of USD5 million and would include a state-of-the-art paint plant for the buses. The unit will be managed and operated by ALL. The unit will also be provided an industrial licence that will enable duty-free import of vehicle kits and duty-free export of finished vehicles to GCC and the Middle East. ALL enjoys a market share in excess of 60% in Dubai's standard bus market and exports to the region are set to cross 1,500 vehicles per annum.

New product launches in the pipeline

The company plans to introduce a number of products in the next two years. During the current year, the company plans to launch its Inter Century-Luxura buses, a 6x4 multi-axle mining tipper, and a higher tonnage vehicle with J-series engine. The other launches planned are the NEWGEN range of trucks and a new HMV defence truck for the Indian army.

Outlook

The strong growth in the commercial vehicle (CV) segment, capacity expansion plans, benefits accruing from the recent acquisition of Avia and strengthening of its auto components operations would act as triggers for the stock. A beefed up product portfolio would de-risk its business model across products and geographies.

Though the margins have been lower this year, primarily due to the lower contribution of the bus segment (where the margins are considerably higher), going forward, the margins are expected to be restored to earlier levels, mainly due to two reasons. a) The price hike of about 2.5% effected by the company, which would come into effect from November 1, 2006; and b) the higher contribution of the defence and bus segments in the second half of the current fiscal.

At the current market price of Rs44, the stock quotes at 11.6x its FY2008E earnings and 6.5x its FY2008E earnings before interest, depreciation, tax and amortisation. We maintain our positive outlook on Ashok Leyland with a Buy recommendation on the stock with a price target of Rs53.

Earnings table

Particulars	FY2005	FY2006	FY2007E	FY2008E
Net profit (Rs cr)	281.0	305.6	406.7	503.5
% y-o-y growth	-	*9.0*	*33.0*	*24.0*
Shares in issue (Cr)	118.90	122.16	133.20	133.20
EPS (Rs)	2.4	2.5	3.1	3.8
% y-o-y growth	-	*9.0*	*33.0*	*24.0*
PER (x)	18.6	17.6	14.4	11.6
Book value (Rs)	9.6	11.4	15.0	15.6
P/BV (Rs)	4.6	3.9	2.9	2.8
EV/EBIDTA (x)	12.6	10.1	8.1	6.5
Dividend yield (%)	2.3	3.0	2.7	2.7
RoCE (%)	20.7	21.8	25.9	28.8
RoNW (%)	23.7	23.6	20.4	24.2

Punjab National Bank

Ugly Duckling

Stock Update

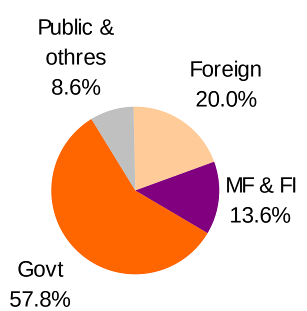
Core operating numbers look promising

Buy; CMP: Rs520

Company details

Price target:	Rs600
Market cap:	Rs16,396 cr
52 week high/low:	Rs544/300
NSE volume: (No of shares)	6.2 lakh
BSE code:	532461
NSE code:	PNB
Sharekhan code:	PUNBANK
Free float: (No of shares)	13.3 cr

Shareholding pattern



Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	-1.4	40.6	26.5	42.9
Relative to Sensex	-5.8	15.0	13.7	-16.9

Result highlights

- Punjab National Bank's results are slightly below our expectations with the profit after tax (PAT) reporting a growth of 19.7% to Rs505 crore compared to our estimates of a PAT of Rs532 crore.
- The net interest income (NII) was up by 14.4% compared to our estimates of 20.5%. The reported net interest margins (NIMs) for H1FY2007 at 4.16% have improved by 16 basis points year on year (yoy). The bank's CASA ratio at 49% is among the best in the industry.
- The other income decreased by 9.1% to Rs284 crore mainly due to the lower trading income as the fee income growth remained robust at 17.6%.
- The core operating profit was up 33.5% while the operating profit was up 30% with the provisions up from Rs9.4 crore to Rs101 crore mainly due to the higher non-performing assets (NPAs) and standard assets provisioning. We expect that the bank must have utilised the write-back in the excess depreciation due to a fall in the bond yields, booked during Q1FY2007 to make higher NPA related provisions during Q2FY2007.
- The advances growth has been at 28.9% yoy as on September 2006 compared to 37.4% yoy as on June 2006. The moderation in the advances growth is welcome with the high yielding advances like retail growing by 47.7% yoy as on September 2006.
- We have revised our earnings per share (EPS) estimates for FY2007 and FY2008 from Rs51.8 and Rs 65.2 to Rs56.1 and Rs 70.7 respectively mainly on account of the improving core banking performance on the back of improving margins and selective credit growth along with a high 49% CASA which protects the cost of deposits during a rising interest scenario. However, the scrip remains exposed to some amount of interest rate risk if the bond yields move up significantly beyond 8% from the current levels.
- At the current market price of Rs520, the stock is quoting at 7.4x its FY2008E EPS, 4.2x pre-provision profits (PPP) and 1.3x book value. The bank is available at attractive valuations given its improving operating performance and asset quality that is one of the best in the industry. We maintain our Buy call on the stock with a price target of Rs600.

Result table Rs (cr)

Particulars	H1FY07	H1FY06	% yoy	Q2FY07	Q2FY06	% yoy	% qoq
Net interest income	2,655.6	2,279.1	16.5	1,362.8	1,190.7	14.4	5.4
Other income	565.3	565.6	-0.1	284.0	312.3	-9.1	1.1
Other income (excl treasury)	516.0	452.2	14.1	213.0	241.3	-11.7	-
Fee income	461.0	345.0	33.6	217.9	185.3	17.6	-10.4
Net income	3,221.0	2,844.7	13.2	1,646.8	1,503.1	9.6	4.6
Operating expenses	1,454.8	1,516.2	-4.0	758.0	819.5	-7.5	8.8
Operating profit	1,766.2	1,328.6	32.9	888.8	683.6	30.0	1.3
Core operating profit	1,716.9	1,215.1	41.3	817.8	612.6	33.5	-9.0
Provisions	465.6	125.6	270.8	101.8	9.4	-	-72.0
Tax	428.0	422.4	1.3	282.0	252.2	11.8	93.1
Reported net profit	872.5	780.2	11.8	505.0	422.0	19.7	37.4

NII growth at 14.4% yoy

The NII was up by 14.4% compared to our estimates of 20.5%. The reported NIMs for H1FY2007 at 4.16% have improved by 16 basis points yoy. The bank's CASA ratio at 49% is among the best in the industry, which helps it to keep the cost of deposits down.

Yield assessment (%)

Particulars	H1 FY07	H1 FY06	yoy chg (in bps)	Q2 FY07	Q1 FY07	qoq chg (in bps)
NIM	4.2	4.0	16	4.2	4.1	12
Cost of deposits	4.3	4.3	5	4.3	4.4	-6
Yield on advances	9.0	8.3	62	9.1	8.8	32

Source: Sharekhan Research, Q2FY07 calculated, rest reported by the bank

Advances growth moderates

The advances growth has been at 28.9% yoy as on September 2006 compared to 37.4% yoy as on June 2006. The moderation in the advances growth is welcome with the high yielding advances like retail growing by 47.7% yoy as on September 2006.

Business Mix (Rs crore)

Particulars	H1FY07	H1FY06	% yoy chng
Business	210755.0	173282.0	21.6
Deposits	128415.0	109414.0	17.4
Advances	82340.0	63868.2	28.9
- Retail	19794.0	13403.0	47.7
- Housing	6689.0	5308.7	26.0
Agriculture	16570.0	12553.0	32.0

Source: Sharekhan research

Other income down 9.1%

The other income decreased by 9.1% to Rs284 crore mainly due to the lower trading income as the fee income growth remained robust at 17.6%.

Other income (Rs crore)

Particulars	Q2Y07	Q2FY06	% yoy chng	% qoq chng
Fee income	217.9	185.3	17.6	-10.4
Total	284.0	312.3	-9.1	1.0

Source: Company, Sharekhan Research

Operating expenses down 7.5% yoy

The operating expenses reported a 7.5% decrease yoy to Rs758 crore with the staff cost reporting a decline of 12.1% to Rs510 crore. The decrease is due to a higher base as the bank had provided Rs70 crore for the wage arrears settlement during the corresponding quarter in the previous year. The same is not present in Q2FY2007 staff expenses, which also explains the 12.1% fall in the staff expenses. Adjusting for the same the operating expenses growth remained flat.

Operating expenses (Rs crore)

Particulars	Q2Y07	Q2FY06	% yoy chng	% qoq chng
Employee cost	510.8	581.2	-12.1	6.6
Other operating expenses	247.2	238.3	3.7	13.6
Total operating expenses	758.0	819.5	-7.5	8.8

Operating profit grew by 30% yoy

The operating profit grew by 30% yoy due to the improved core banking numbers on the NII front coupled with a fall in the operating expenses.

Provisions up due to higher NPA provisioning

The provisions were up from Rs9.4 crore to Rs101 crore mainly due to higher NPAs and standard assets provisioning. We expect that the bank must have utilised the write-back in excess depreciation due to a fall in the bond yields booked during Q1FY2007 to make higher NPA related provisions during Q2FY2007.

Asset quality among the best in the industry

The bank's net NPAs reduced to 0.18% of its net advances at the end of September 2006 from 0.32% at the end of September 2005. However, on a sequential basis the same decreased by only three basis points from 0.35% at the end of June 2006.

Valuation and view

We have revised our EPS estimates for FY2007 and FY2008 from Rs51.8 and Rs 65.2 to Rs56.1 and Rs 70.7 respectively mainly on account of the improving core banking performance on the back of the improving margins and selective credit growth along with a high 49% CASA, which protects the cost of deposits during a rising interest scenario. However, the scrip remains exposed to some amount of interest rate risk if the bond yields move up significantly beyond 8% from the current levels.

At the current market price of Rs520, the stock is quoting at 7.4x its FY2008E EPS, 4.2x pre-provision profits (PPP) and 1.3x book value. The bank is available at attractive valuations given its improving operating performance, improving RoE and asset quality that is one of the best in the industry. We maintain our Buy call on the stock with a price target of Rs600.

Earnings table

Particulars	FY2005	FY2006	FY2007E	FY2008E
Net profit (Rs cr)	1,410.1	1,439.5	1,766.4	2,226.9
Shares in issue (cr)	31.5	31.5	31.5	31.5
EPS (Rs)	44.8	45.7	56.1	70.7
EPS growth (%)	9.5	2.1	22.7	26.1
PE (x)	11.6	11.4	9.3	7.4
P/PPP (x)	5.6	5.2	4.8	4.2
Book value (Rs)	258.8	297.4	342.0	401.2
P/BV (x)	2.0	1.7	1.5	1.3
Adj. book value (Rs)	255.3	291.0	331.3	398.4
P/ABV (x)	2.0	1.8	1.6	1.3
RONW (%)	20.0	16.4	17.5	19.0

Tata Motors

Apple Green

Stock Update

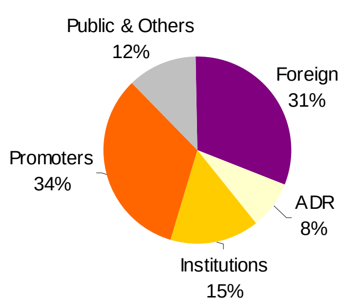
Margins dip, just a blip

Buy; CMP: Rs828

Company details

Price target:	Rs1,004
Market cap:	Rs31,719 cr
52 week high/low:	Rs997/465
NSE volume: (No of shares)	17.0 lakh
BSE code:	500570
NSE code:	TATAMOTORS
Sharekhan code:	TELCO
Free float: (No of shares)	22.3 cr

Shareholding pattern



Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	-1.2	17.1	-6.7	88.0
Relative to Sensex	-5.5	-4.3	-16.1	9.4

Result highlights

- Tata Motors' Q2 results are below our expectations due to a marginal drop in the operating margins and higher interest and product development costs.
- The net sales for the quarter are in line with our expectations, marking a growth of 37.4% to Rs6,571.8 crore.
- The operating margins (excluding forex gain/loss and some non-incurring employee expenses) for the quarter have declined by 60 basis points to 11.8%. The margins have been affected due to the higher consumption of steel and rubber in commerical vehicles. Consequently, the operating profits for the quarter have grown by 30.8% to Rs777.9 crore.
- Higher interest and product development costs led to a net profit growth of 30.4% to Rs441.9 crore.
- The company is in talks with Fiat to expand the terms of its joint venture agreement across product categories and markets.
- In view of the favourable domestic market, increasing international dimension (soaring exports, acquisitions & tie-ups) and an aggressive growth strategy, we believe Tata Motors is set to assert itself as a globally competitive auto major.
- Considering the decline in the operating profit margins we are marginally downgrading our estimates by 7% from Rs58.0 to Rs53.9 for FY2007 and by 5% for FY2008 from Rs70.6 to Rs67.4. At the current market price of Rs828, the stock quotes at 12.4x its consolidated FY2008E earnings and 7.9x its FY2008E earnings before interest, depreciation, tax and amortisation. We maintain our Buy recommendation on the stock with a price target of Rs1,004.

Result table Rs (cr)

Particulars	Q2FY2007	Q2FY2006	% yoy change
Net sales	**6571.8**	**4788.2**	**37.3**
Total expenditures	5768.5	4213.2	36.9
RM cost	4650.5	3377.6	37.7
Change in stock	-122.4	-116.5	
Staff cost	342.7	275.2	24.5
Other expenditure	897.8	676.8	32.6
Operating profits	803.3	575.0	39.7
Operating profits excl forex gain/loss	**777.9**	**594.6**	**30.8**
Other income	84.8	58.0	46.2
EBIDTA	888.2	633.1	40.3
Interest	95.6	46.1	
PBDT	792.6	587.0	35.0
Depreciation	161.0	133.0	
PBT	631.6	454.0	39.1
Tax	144.7	116.1	
PAT	**486.9**	**337.9**	**44.1**
Extra-ordinary item	-45.2	-1.0	
Reported PAT	**441.7**	**336.9**	**31.1**
EPS (Rs)	12.6	9.0	
OPM (%)	12.2	12.0	
OPM excl forex gain/loss (%)	11.8	12.4	
PATM (%)	7.4	7.1	

Strong volumes drive the top line growth

Tata Motors' Q2FY2007 net sales are in line with our expectations. The sales grew by 37.4% to Rs6,571.8 crore, led by a strong volume growth of 30.7% to 139,894 units during the quarter and witnessed an average realisation growth of 5.2%. During the quarter, the company launched a new range of *Tata Safari*, and face lifted versions of *Indigo Sedan* and *Indigo Marina* range of vehicles, which have received an enthusiastic response from the market. Tata *Ace*, the new mini-truck continues to post strong growth with its gradual extension across the country and after its launch in Sri Lanka.

Q2 Volume growth table

Volumes	Q2FY07	Q2FY06	% yoy change
M&HCV	40,787	29,052	40.4
LCV	30,443	21,063	44.5
Total CV	71,230	50,115	42.1
Utility vehicles	11,506	8,242	39.6
Cars	42,882	34,711	23.5
Total domestic	125,618	93,068	34.9
Exports	14,276	13,994	2.0
TOTAL	139,894	107,062	30.7

Tata Motors delivered a good performance in Q2FY2007 with an overall growth of 31%. The light commercial vehicle (LCV) segment continued on its high growth path recording a growth of 44.5% as *Ace* continued to do well. The utility vehicle (UV) segment has recovered due to the successful re-launch of *Safari* and the reduction in its price. The car segment too performed well with the good performance of *Indica Xeta* and the launch of the face lifted versions of the *Indigo* family. The commercial vehicle (CV) segment has also witnessed a growth, albeit at a lower rate.

The exports for Q2FY2007 grew marginally to 14,063 vehicles with the key export destinations for the company being South Africa, South Asia, the Middle East and Europe. The exports were slow due to significant depreciation of the South African 'Rand' v/s US$.

The company improved its market share position across its entire product range. The market share in the commercial vehicle segment has grown to 65.2% as compared to 58.0% in the corresponding period of the previous year, and in the passenger vehicle segment, the company's market share has grown to 16.3% as compared to 15.8% a year ago.

Margins down by 60 basis points

The reported operating margins have declined by 50 basis points to 11.5%. The decline in the profit margins is due to the higher raw material cost mainly due to the higher quantity of steel and rubber consumed by the CV segment.

Excluding the forex gain of Rs25.39 crore during the quarter as against a loss of Rs19.6 crore in the same quarter last year and adjusting for the one-time expenditure to the tune of Rs45 crore relating to the higher provisioning for gratuity and superannuation, the amount spent on maintenance and productivity improvement of Pune and the Jamshedpur plants, the operating profit margin for the quarter is down by 60 basis points to 11.8%. The operating profits after forex gain/loss have marked a growth of 30.8% to Rs777.9 crore.

The other income was higher due to higher dividend income from associate companies. This coupled with stable depreciation led the profits after taxes to mark a growth of 30.7% yoy to Rs441.7 crore.

Capex plans

Tata Motors' capital expenditure (capex) for the next three -four years stands at Rs10,000 crore. The amount would be used for the development of new platforms, capacity expansions, and modernisation of the present facilities. Out of the above, approximately 45% would be spent for commercial vehicles while 55% would be spent for passenger vehicles. The above capex includes about Rs1,000 crore that will be spent on the development of the new small car. Other than that the company is looking to develop a new platform for *Indica*, one for UV and another for a pick-up vehicle. Starting from the next fiscal, the company plans to launch at least three new products in the next two years.

Vehicle financing business performing well

The vehicle financing division is rendering a good performance with the disbursement rising by 78% yoy to Rs2,094 crore in Q2FY2007 and by 97% to Rs4,184 crore in H1FY2007.

Consolidated performance

The company's consolidated revenues (net of excise) at Rs7,702.7 crore recorded an increase of 41.9% as against Rs5,428.9 crore in the corresponding period of the previous year. The consolidated profit after tax (PAT) at Rs542.2 crore, as against Rs392.6 crore in the corresponding period of the previous year recorded a growth of 38.1%.

Subsidiaries performances

	Turnover			Net profits		
	Q2FY07	Q2FY06	% yoy chg	Q2FY07	Q2FY06	% yoy chg
Tata Daewoo CV Ltd, Korea (TDCV)	565.5	351.4	60.9	24.0	15.8	52.0
Telco Construction Equipment Co Ltd (Telcon)	352.2	283.3	24.3	37.1	18.1	104.8
Tata Technologies Ltd (TTL)	60.3	56.3	7.2	1.7	2.1	-17.6
HV Transmissions Ltd (HVTL)	40.5	31.2	29.8	9.6	7.3	32.7
HV Axles Ltd (HVAL)	44.3	34.7	27.6	12.5	10.6	17.8

Tata Daewoo (TDCV)

The turnover for the quarter increased by 61% yoy to Rs565.5 crore, while the PAT grew by 52% to Rs23.95 crore. The sales volumes rose brilliantly by 70% yoy to 2,141 units.

Telcon

The turnover in Q2FY2007 rose to Rs352.2 crore, marking a growth of 24.3%, while the PAT rose by 104.8% to Rs37.1 crore. Telcon registered a 41% volume growth to 1,189 units during the quarter while its market share in excavators increased to 53% as against 52% a year ago. The company also increased its market share in backhoe to 10% while the share in wheel loaders stood at 18% during H1FY2007.

Tata Technologies

The turnover of Tata Technologies (TTL) in Q2FY2007 rose by 7.2% yoy to Rs60.3 crore, while the PAT declined by 17.6% to Rs1.7 crore during the quarter. Post the acquisition of INCAT, TTL has increased its global share of the revenues with 50% of the business coming from the USA, 24% from Europe and 27% from Asia Pacific.

HV Transmissions Ltd (HVTL) and HV Axles Ltd (HVAL)

In Q2FY2007, HVAL reported a 27.6% increase in its revenues and a 17.8% increase in its net profits; while HVTL reported a 29.8% increase in its revenues and a 32.7% increase in its net profits.

Pune plant to be restored by November

Towards the end of the quarter, a fire broke out at the passenger vehicle paint shop of Tata Motors' Pune facility. The company would face no financial loss as a result of the fire. However, the car sales in Q3FY2007 are likely to be impacted to the extent of about 3,000-4,000 units due to the production losses caused by the same.

The facility is expected to be fully restored by November with the volumes of 750 cars per day.

Talks going on with Fiat to expand the MoU

Tata Motors and the Fiat group have signed a new memorandum of understanding (MoU) to establish a 50:50 joint venture to manufacture passenger vehicles, engines and transmissions for both the domestic and export markets. Both the companies will use the Ranjangaon facility of Fiat in Maharashtra. Fiat will introduce the *Fiat Grande Punto* and the new *Fiat Sedan*—its premium cars for the B and C segments—and its small diesel engines. The company is also in talks with Fiat to expand the joint venture across product categories and geographies.

Valuations and view

The demand in the CV segment is expected to continue in the second half of the year, albeit at a slower growth rate due to the high base of H2FY2006. Further the brilliant demand for its LCV *Ace* would help Tata Motors register good growth numbers going forward. For FY2007, we expect Tata Motors to clock a 29% growth in the M&HCV segment and a 30% growth in the LCV segment. Tata Motors has also managed to improve its market share in the car segment, with the success of its *Indica Xeta* and the success of the face lifted version of the *Indigo* family. The company is in the process of renegotiating its contracts with some of the ancillary companies, particularly the tyre companies, in order to reduce its costs. The company maintains that it would be able to maintain its operating margins at around 12% for the current fiscal.

In view of the decline in the operating profit margins we are marginally downgrading our estimates by 7% from Rs58.0 to Rs53.9 for FY2007 and by 5% for FY2008 from Rs70.6 to Rs67.4. At the current market price of Rs828, the stock quotes at 12.4x its consolidated FY2008E earnings and 7.9x its FY2008E earnings before interest, depreciation, tax and amortisation. We maintain our Buy recommendation on the stock with a price target of Rs1,004.

Earnings table

Year to March 31	FY2005	FY2006	FY2007E	FY2008E
Stand-alone				
Net profit (Rs cr)	1237.0	1528.9	1703.4	2111.9
% y-o-y change	*52.3*	*23.6*	*11.4*	*24.0*
Shares in issue (cr)	361.8	382.9	385.2	385.2
EPS (Rs)	34.2	39.9	44.2	54.8
PER (x)	24.2	20.7	18.7	15.1
EV/EBIDTA (x)	12.7	12.2	10.5	8.8
Consolidated				
Net profit (Rs cr)	1385.3	1730.0	2076.0	2595.0
% y-o-y change	*51.4*	*24.9*	*20.0*	*25.0*
Shares in issue (cr)	361.8	382.9	385.2	385.2
EPS (Rs)	38.3	45.2	53.9	67.4
PER (x)	21.6	18.3	15.4	12.3
EV/EBIDTA (x)	12.4	11.2	9.3	7.9

Sharekhan Stock Ideas

Evergreen

HDFC Bank
Infosys Technologies
Reliance Industries
Tata Consultancy Services

Apple Green

Aditya Birla Nuvo
ACC
Bajaj Auto
Balrampur Chini Mills
Bank of Baroda
Bank of India
Bharat Bijlee
Bharat Electronics
Bharat Heavy Electricals
Canara Bank
Corporation Bank
Crompton Greaves
Elder Pharmaceuticals
Godrej Consumer Products
Grasim Industries
Hindustan Lever
Hyderabad Industries
ICICI Bank
Indian Hotels Company
ITC
Mahindra & Mahindra
Marico Industries
Maruti Udyog
Lupin
Nicholas Piramal India
Omax Autos
Ranbaxy Laboratories
Satyam Computer Services
SKF India
State Bank of India
Sundaram Clayton
Tata Motors
Tata Tea
Unichem Laboratories
Wipro

Cannonball

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

Emerging Star

3i Infotech
Aban Offshore
Cadila Healthcare
KSB Pumps
Marksans Pharma
Navneet Publications (India)
New Delhi Television
Orchid Chemicals & Pharmaceuticals
ORG Informatics
Solectron Centum Electronics
Television Eighteen India
Thermax
TVS Motor Company
UTI Bank
Welspun Gujarat Stahl Rohren

Ugly Duckling

Ahmednagar Forgings
Ashok Leyland
BASF India
Deepak Fertilisers & Petrochemicals Corporation
Genus Overseas Electronics
HCL Technologies
ICI India
India Cements
Jaiprakash Associates
JM Financial
KEI Industries
NIIT Technologies
Punjab National Bank
Ratnamani Metals and Tubes
Sanghvi Movers
Saregama India
Selan Exploration Technology
South East Asia Marine Engineering & Construction
Subros
Sun Pharmaceutical Industries
Surya Pharmaceuticals
UltraTech Cement
Union Bank of India
Universal Cables
Wockhardt

Vulture's Pick

Esab India
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WS Industries India

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