Index

Take Five

Scrip	Reco Date	Reco Price	CMP	Target
Bharat Bijlee	29-Nov-04	192	**1,401**	1,730
BEL	25-Sep-06	1,108	**1,398**	1,525
Ceat	28-Nov-06	122	**146**	190
F-M Goetze	18-Jan-07	385	**385**	559
NDTV	10-Feb-05	180.9	**324**	348

Navneet Publications (India)

Emerging Star

Stock Update

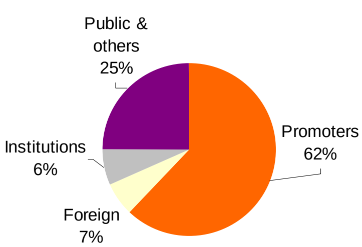
Price target revised to Rs67

Buy; CMP: Rs55.5

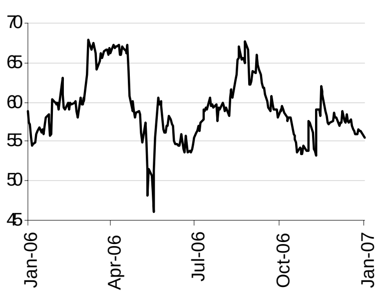
Company details

Price target:	Rs67
Market cap:	Rs530 cr
52 week high/low:	Rs70.8/46
NSE volume: (No of shares)	21,799
BSE code:	508989
NSE code:	NAVNETPUBL
Sharekhan code:	NAVNEET
Free float: (No of shares)	3.6 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-1.3	-5.6	6.7	-0.8
Relative to Sensex	-7.0	-16.7	-22.5	-33.7

Result highlights

- Navneet Publications reported a tepid growth of 2.9% in its revenues to Rs45.7 crore during the third quarter. The publication business showed a decent growth of 11.7% to Rs28.6 crore. However, the stationary business continues to remain sluggish and declined by 11.4% to Rs16.4 crore.
- The operating profit margin (OPM) of 13.7% is 20 basis points lower than 13.9% reported in Q3FY2006. Consequently, the operating profit grew by just 1.1% to Rs6.3 crore.
- However, the healthy other income component of Rs0.9 crore (includes foreign exchange [forex] gains of Rs0.6 crore) against the negative other income of Rs0.2 crore in Q3FY2006, enabled the company to report a healthy earnings growth of 43.2% to Rs3.4 crore.
- On a nine-month basis, the revenues and earnings have grown by 12.1% to Rs279.9 crore and by 18.6% to Rs42.2 crore respectively. The OPM has improved by 190 basis points to 24.2%, largely due to the better profitability in the publication business.
- Grafalco, the wholly-owned subsidiary in Spain, reported revenues of 1.05 million euros and a net loss of 0.02 million euros in its first full year of operations ended December 2006. It reported profit on the operational level and is expected to show a profit on the net level in the calendar year 2007. The results of Grafalco are not yet consolidated in the quarterly performance.
- Along with the results the company announced that it would invest Rs25 crore to set up a windmill-based power generation plant in Gujarat. The same has been approved in the recently held board meeting.

Result table - stand-alone Rs (cr)

Particulars	Q3FY07	Q3FY06	% yoy	9MFY07	9MFY06	% yoy
Net sales	45.7	44.4	2.9	279.9	249.7	12.1
Total expenditure	39.5	38.3	3.1	212.3	194.1	9.4
Operating profit	6.3	6.2	1.3	67.6	55.7	21.5
Other income	0.9	-0.2	-519.0	1.0	0.9	7.6
Interest	0.1	0.3	-70.4	1.2	1.6	-27.4
Depreciation	2.0	2.3	-12.7	5.8	6.7	-13.7
PBT	5.1	3.4	48.2	61.6	48.2	27.8
Tax	1.7	1.1	59.4	19.4	12.6	53.6
PAT	3.4	2.4	43.2	42.2	35.6	18.6
Equity capital	19.1	19.1		19.1	19.1	
EPS (Rs)	0.4	0.2		4.4	3.7	
Margins						
OPM(%)	13.7	13.9		24.2	22.3	
NPM(%)	7.4	5.3		15.1	14.2	

- To factor in the lower-than-expected performance of the stationary business, we have revised downwards the earnings estimates by 1.7% and 4.1% for FY2007 and FY2008 respectively. At the current price the stock trades at 12x FY2007 and 10x FY2008 estimated earnings. We maintain our Buy recommendation on the stock with a one-year target price of Rs67 (12x FY2008 earnings).

Stationary business continues to drag down the overall revenue growth

The revenue growth of 19.8% in the publication revenues during the first nine months was driven by the changes in the syllabus in Maharashtra and Gujarat and was as per the expectations. However, the stationary business continues to drag down the overall growth in the revenues with a decline of 4.8% to Rs80.9 crore in the same period.

The stationary business is witnessing a slow-down in the demand in the exports market, especially from the USA, which has slapped an anti-dumping duty on the import of stationary items from China, Indonesia and India. Thus, the revenues from the stationary business are likely to decline by around 4-5% as against the management guidance of 5-10% growth in FY2007.

Revenue break-up

(Rs crore)	Q3FY07	Q3FY06	% yoy	9MFY07	9MFY06	% yoy
Publication	28.6	25.6	11.7	196.3	163.9	19.8
Stationary	16.4	18.5	-11.4	80.9	84.9	-4.8
Others	0.7	0.3	126.7	2.8	1.0	186.5

Better realisations in publication business boost the margins

During the quarter, the margins in the publication business improved by 140 basis points to 22.8%, largely due to the 3-4% improvement in the average realisation. However, the stationary business reported a segmental loss of Rs0.6 crore due to the slow-down in the exports business and also the additional cost (around Rs0.4 crore) incurred for the introduction of non-paper stationary items (like pencil boxes, pencils, sharpners etc).

On a nine-month basis, the margins in the publication business improved by 120 basis points to 29.7% and the margins in the stationary business were stable at around 10.6%. The margins in the stationary business were aided by the high proportion of the revenues from the high-margin domestic business.

Segmental margins (%)

	Q3FY07	Q3FY06	9MFY07	9MFY06
Publication	22.8	21.4	29.7	28.5
Stationary	-3.9	1.9	10.6	10.7

Grafalco to make meaningful contribution in FY2008

Grafalco (erstwhile Chaplin Disenos and acquired in August 2005) has reported revenues of 1.05 million euros for the calendar year 2006. The company was profitable on the operating level but reported a net loss of 0.024 million euros. The subsidiary is expected to report revenues of around 1.8 million euros and turn profitable in the current calendar year.

Outlook

In terms of the outlook for FY2008, the change in the syllabus of standards 10 and 12 class (that contributed to over 20% of the revenues from Maharashtra) in the Maharashtra Board is expected to drive the growth in the publication business. The stationary business is also likely to show some growth on the back of the lower base effect and the incremental revenues from the non-stationary business.

In terms of the growth outlook beyond FY2008, the major changes in the syllabus of the Maharashtra Board and the Gujarat Board would be over. However, some of the ongoing efforts to expand the size of the addressable market are likely to yield meaningful benefits and make up for the absence of growth triggers in terms of changes in the syllabus. Some of the initiatives taken are given below.

- The company is introducing titles in Urdu language in Maharashtra in the primary school segment. The company believes this is a substantially large and under-penetrated market segment.
- It intends to complete the entire series of title releases for the students in Madhya Pradesh (MP) by FY2008. The company has been working on penetrating the market and expects around Rs2 core of revenues from MP in FY2007.
- It has successfully test marketed the market in Andhra Pradesh by introducing guides for standard 10 class and would further expand the portfolio of titles in the state.
- It is also working on introducing guides as per the syllabus of the central board of secondary education (CBSE) and for the entrance exams.

Diversification into electricity generation business

The company intends to invest Rs25 crore to set up windmill farms in Gujarat for the generation of electricity. The proposal is still in the initial stage but the management expects an internal rate of return (IRR) of 17-18% in the projects (on net investments) and a payback period of around 6 years. We believe that the venture would be dilutive to the return ratios.

On the brighter side, the company does not expect the investment to impact its dividend payout policy. In fact, it has a comfortable cash position and expects to further increase the dividend rate in the coming years.

Revision of earning estimates

To factor in the lower-than-expected performance of the stationary business, we have revised downwards the earnings estimates by 1.7% and 4.1% for FY2007 and FY2008 respectively.

Valuation

At the current price the stock trades at 12x FY2007 and 10x FY2008 estimated earnings. We maintain our Buy recommendation on the stock with a one-year target price of Rs67 (12x FY2008 earnings).

Financial table

	FY2004	FY2005	FY2006	FY2007	FY2008
Net profit	35.2	30.9	35.6	44.0	53.1
Shares in issue	9.5	9.5	9.5	9.5	9.5
EPS Rs	3.7	3.2	3.7	4.6	5.6
% y-o-y growth		*-12.2*	*15.4*	*23.5*	*20.6*
PE x	15.2	17.3	15.0	12.0	10.0
BV Rs	16.6	18.2	19.3	21.7	25.0
P/BV	3.4	3.1	2.9	2.6	2.2
EV/EBIDTA	10.8	10.1	9.9	7.6	6.1
ROCE (%)	15.0	15.0	16.0	19.0	23.0
RONW (%)	22.0	18.0	19.0	21.0	22.0
Dividend yield (%)	2.7	2.7	3.0	3.6	3.6

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

TVS Motor Company

Emerging Star

Stock Update

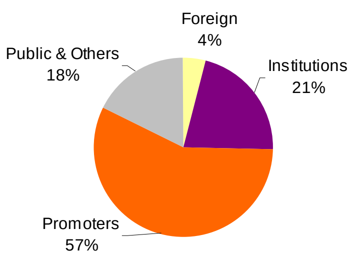
Book Profit

Book Profit; CMP: Rs75

Company details

Market cap:	Rs1,758 cr
52 week high/low:	Rs187/78
NSE volume: (No of shares)	8.45 lakhs
BSE code:	532343
NSE code:	TVSMOTOR
Sharekhan code:	TVSSUZUKI
Free float: (No of shares)	10.2 cr

Shareholding pattern



Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	-7.6	-33.1	-2.4	-27.9
Relative to Sensex	-12.9	-41.0	-29.2	-51.8

Result highlights

- TVS Motors' Q3FY2007 results are below our expectations primarily due to the intensifying competition in the two-wheeler segment and rising raw material prices leading to lower profitability.
- The company has recorded a 7.3% growth in its net sales for the quarter, which stood at Rs935.4 crore due to a marginal volume growth of 1.4% and a realisation growth of 5.8% year on year (yoy).
- The operating profit for the quarter declined by 51% to Rs29.6 crore as the operating margins declined by 380 basis points to disappointing levels of 3.2%. Even on a sequential basis, the margins were down 200 basis points. The lower margins are largely attributed to the lower sales volumes and a rise in the raw material costs.
- The profit before tax (PBT) during the quarter stood at Rs14.1 crore as compared to Rs45 crore a year ago. The profit after tax (PAT) declined by 63% to Rs11.5 crore.
- Considering the competitive pressures in the two-wheeler industry, we expect the pressure on the profit margins to continue in spite of the new product launches. We are downgrading our estimates for FY2007 by 30% and for FY2008 by 80%.
- At the current market price of Rs75, the stock discounts its FY2008E earnings by 17.2x and FY2008E EBIDTA by 9.1x. We advise to book profit in the stock.

Result table Rs (cr)

Particulars	Q3FY07	Q3FY06	VAR [%]	9MFY07	9MFY06	VAR [%]
Net sales	**935.4**	**871.4**	**7.3**	**2935.1**	**2395.7**	**22.5**
Total expenditure	905.8	810.7	11.7	2807.9	2239.4	
Operating profits	**29.6**	**60.7**	**-51.2**	**127.2**	**156.3**	**-18.6**
Other income	17.6	12.0	46.7	46.3	40.0	
EBIDTA	**47.2**	**72.7**	**-35.0**	**173.5**	**196.2**	**-11.6**
Interest	8.6	3.5	148.6	20.8	8.6	142.4
PBDT	**38.6**	**69.2**	**-44.2**	**152.7**	**187.7**	**-18.6**
Depreciation	24.5	24.2	1.2	72.2	70.0	3.2
PBT	**14.1**	**45.0**	**-68.6**	**80.5**	**117.7**	**-31.6**
Tax	7.3	6.5	13.0	21.9	32.4	
Deferred tax	-5.9	7.0	-183.7	-1.6	6.0	
FBT	1.2	0.5	150.0	2.6	1.2	
Adj profit after tax	**11.5**	**31.1**	**-63.0**	**57.6**	**78.2**	**-26.4**
Extraordinary items				0.0	-9.7	
Reported PAT	**11.5**	**31.1**	**-63.0**	**57.6**	**87.9**	**-34.5**
EPS	0.5	1.3		2.4	3.3	
OPM (%)	3.2	7.0		4.3	6.5	
PAT (%)	1.2	3.6		2.0	3.3	

Net sales rise 7.3% with a marginal volume growth of 1%

The net sales of TVS Motors rose by 7.3% to Rs935.4 crore in Q3FY2007, with a volume growth of just 1.4% and a realisation growth of 5.8%. The motorcycle sales during the quarter declined by 3.3% due to the increased competition in the entry-level segment, thereby affecting the sales of *Star City*. *Apache* continued to be the number 2 brand in the premium bike category though the volumes declined towards the end of the quarter. The sales of the mopeds improved by 18.6%.

Sales performance

	Q3FY2007	Q3FY2006	% growth
Motorcycle	214,958	222,309	-3.3
Scooters	61,243	62,481	-2.0
Mopeds	87,469	73,769	18.6
TOTAL	363,670	358,559	1.4

The realisation improved by 5.8% yoy mainly due to a price hike of about 1.5-2% effected in September and also on the improved product mix of the company in comparison to last year. Its newly launched *StaR City ES*, has been well received by the market. The 2-stroke variant of *TVS Scooty*, *Teenz* has also received an encouraging response.

Intensified competition, high raw material costs hurt margins

The operating profit for the quarter declined by 51% yoy to Rs29.6 crore. The operating profit margin (OPM) declined by a massive 380 basis points yoy to 3.2% and 200 basis points on a quarter-on-quarter (q-o-q) basis. The competition in the two-wheeler segment intensified in Q3FY2007. Competitors like Hero Honda and Bajaj Auto offered steep discounts and resorted to other attractive sales promotion activities, which adversely impacted the volume growth for TVS Motors. Hence, the sales offtake for TVS Motors was much lower than expectations. Also, the sales were more skewed towards the entry-level segment, where the profitability is low. The competition between the top two players is expected to continue thereby marginalising the other players. Consequently, we do not expect any substantial improvement in the profitability. Higher raw material costs made the matter worse for TVS. The raw material costs, as a percentage of sales increased from 70.9% last year to 75.3% for Q3FY2007.

The PBT during the quarter was at Rs14.1 crore as compared to Rs45 crores last year. The PAT declined by 63% to Rs11.5 crore.

Exports growing at a solid pace

TVS's exports for the quarter stood at 21,938 units as compared to 18,205 units a year ago, recording a growth of 20%. The total exports of 79,439 units, at a growth rate of 30% yoy, during the 9-month period was the highest ever achieved by the company in a 9-month period. The exports are likely to increase further with the commencement of its Indonesian unit. Further, the company is planning to enter the Columbian market through a joint venture. We believe that these initiatives would boost the company's exports going forward.

Capex programme nearing completion

The Himachal Pradesh plant, with an annual capacity of 300,000 motorcycles, is nearing completion and is expected to start operations by April 2007. This should help the company cater to the north Indian markets. The investment in this plant is approximately Rs120 crore. Further, the three-wheeler plant is expected to commence operations by early FY2008. The Indonesian plant is also expected to commence production by Q1FY2008 with the rollout of the *Bebek* two-wheeler. The *Bebek* type of two-wheelers constitutes 80% of the total two-wheelers sold in Indonesia. In phase I, the plant will have a capacity of 300,000 units and in phase II, the capacity will increase to 500,000 units. The investment planned in phase 1 is US$45 million.

Downgrade estimates

We expect the profitability to improve in Q4FY2007 due to the benefit of VAT expected to accrue. However the pressure on the profit margins will continue considering the aggressively competitive industry scenario. Considering the fall in the profit margins in the current quarter and taking into account the competitive scenario, we are downgrading our earnings estimates for FY2007 and FY2008 by 30% and 84% respectively.

Valuations

TVS is working at putting a strong product portfolio with planned launches of *Victor* and variants of *Star* and *Apache*. This should aid in growth going forward. However, the pressure on the profit margins is expected to continue. Consolidating the product portfolio would lead to higher marketing expenses in a competitive scenario. The volume growth in FY2007 has been lower than our expectations. Its new capacities should start functioning towards the end of this financial year.

At the current market price of Rs75, the stock discounts its FY2008E earnings by 17.2x and FY2008E EBIDTA by 9.1x. We advise to book profit in the stock.

Earnings table

Particulars	FY04	FY05	FY06E	FY07E	FY08E
Net sales	2,820.2	2,875.9	3,235.0	4,139.1	4,642.9
Net profit	137.8	135.8	100.6	79.5	106.3
EPS	5.8	5.7	4.2	3.3	4.5
% y-o-y growth		*-1.40*	*-25.96*	*-20.93*	*33.71*
PER	13.3	13.5	18.2	23.0	17.2
P/B	3.2	2.7	2.4	2.3	2.1
EV/EBIDTA	6.9	8.3	8.9	11.9	9.1
ROCE (%)	34.7	25.6	16.4	11.0	13.0
RONW (%)	24.0	20.0	13.1	9.8	12.1

Bharat Heavy Electricals

Apple Green

Stock Update

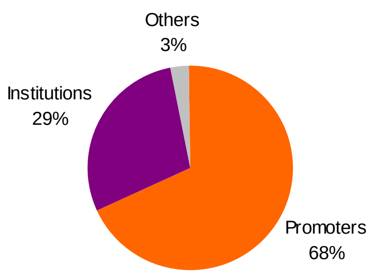
Back on course!

Buy; CMP: Rs2,506

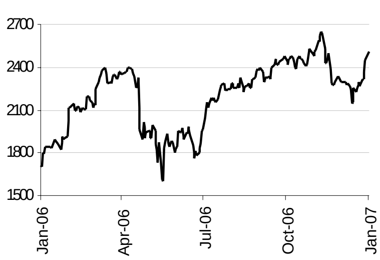
Company details

Price target:	Rs2,650
Market cap:	Rs61,336.9 cr
52 week high/low:	Rs2,668/1,531
NSE volume: (No of shares)	476,989
BSE code:	500103
NSE code:	BHEL
Sharekhan code:	BHEL
Free float: (No of shares)	7.9 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	6.4	0.0	34.0	46.7
Relative to Sensex	0.3	-11.7	-2.7	-2.0

Result highlights

- At Rs667.7 crore, the Q3FY2007 net profit of Bharat Heavy Electricals Limited (BHEL) grew by 57.8%. The same is above our expectations, primarily because of an increase in the margins sequentially and a robust top line growth.
- BHEL's revenues for the quarter grew by a robust 30.5% year on year (yoy) to Rs4,339.7 crore driven by order booking. The power division registered a 28.6% growth in the revenues whereas the industry division recorded a 33.2% growth in the revenues.
- The operating profit margin (OPM) for the quarter increased by 329 basis points yoy and by 775 basis points sequentially to 21.4%, much above our estimates. Consequently the operating profit for the quarter registered a growth of 54.1%, higher than the revenue growth.
- The other income increased by 56.2% to Rs185.5 crore mainly on account of the rising yields on the huge cash reserves of the company.
- The order inflows during the quarter were slower at 9.5% yoy at Rs5,710 crore. There are some orders that have been awarded post the quarter. We are not overtly concerned about this slow-down because the order backlog continues to be robust at Rs46,700 crore, which is 3.2x its FY2006 sales imparting great visibility to the stock.
- The board has announced a bonus of 1:1 and an interim dividend of Rs12.5 per share.

Result table Rs (cr)

Particulars	Q3FY07	Q3FY06	VAR (%)	9MFY07	9MFY06	VAR (%)
Net sales	4339.7	3326.7	30.5	10337.2	7773.6	33.0
Raw material consumed	2584.5	1932.8		6282.8	4757.3	
Stock adjustment	-123.5	-38.7		-419.6	-447.3	
Employee expenses	510.5	452.7	12.8	1547.4	1330.2	16.3
Other expenses	439.0	376.9	16.5	1222.9	990.0	23.5
Total expenditure	3410.5	2723.8		8633.4	6630.2	
Operating profit	929.2	602.9	54.1	1703.8	1143.4	49.0
Other income	185.5	118.7	56.2	475.5	317.5	49.8
Interest	12.0	13.6	-12.0	38.7	39.2	-1.4
Depreciation	66.2	62.0	6.8	196.7	182.0	8.1
PBT	1036.5	646.0	60.4	1943.9	1239.7	56.8
Tax	368.8	222.9	65.5	679.4	428.5	58.6
Reported profit after tax	667.7	423.2	57.8	1264.5	811.2	55.9
OPM (%)	21.4	18.1	329.0	16.5	14.7	177.0
PBT(%)	23.9	19.4	446.0	18.8	15.9	286.0
PATM(%)	15.4	12.7	266.0	12.2	10.4	180.0

- At the current levels, the stock is trading at 20.0x its FY2008E earnings and 12.0x its FY2008E earnings before interest, depreciation, tax and amortisation (EBIDTA). Given the expectations of the continued growth in its order book, a strong compounded annual growth rate (CAGR) of 35.1%, we believe the valuations are attractive. Even on a comparative basis the stock is trading at a significant discount to its peers like Siemens, ABB and Areva. We maintain our Buy recommendation on the stock with a price target of Rs2,650.

Continued momentum in revenue growth

BHEL's revenues for the quarter grew by a robust 30.5% yoy to Rs4,339.7 crore driven by higher order booking. The revenues for both the power and industry divisions grew at a healthy pace. The power division registered a 28.6% growth in the revenues whereas the industry division recorded a 33.2% growth in the revenues. Going forward with the huge order backlog of Rs46,700 crore, which is almost 3.2x the company's FY2006 revenues, the revenue booking is expected to maintain its growth momentum.

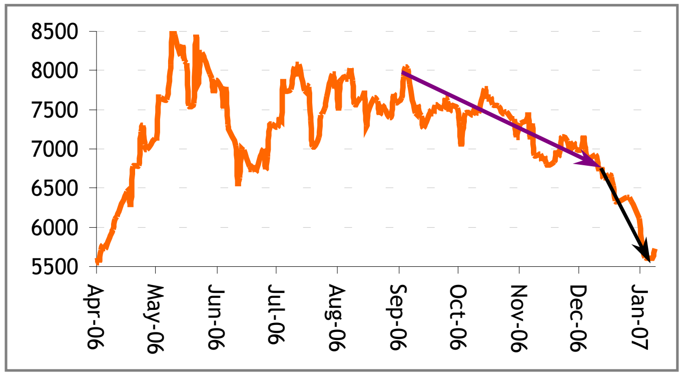
Segment results

Segmental Results	Q3FY07	Q3FY06	VAR (%)
Revenue	4812.8	3708.68	
Power	3538.7	2751.84	28.6
Industry	1274.1	956.84	33.2
EBIT	1002.2	768.53	
Power	845.7	632.54	33.7
Industry	156.5	135.99	15.1
EBIT (%)	20.8	20.7	10 bps
Power	23.9	23.0	91 bps
Industry	12.3	14.2	-193 bps

Margins—back on course

During Q2FY2007 the OPM had come under pressure with the prices of key raw material and employee expenses increasing. In fact the margin contraction of 104 basis points was the first after nine consecutive quarters of margin expansion. During the quarter under review the margins have bounced back with a 329-basis-point yoy and a 775-basis-point sequential expansion to 21.4%. The margin expansion was largely due to the leverage effect coming into play. Though the raw material cost remained under pressure despite the key raw material like copper remaining weak on the LME we had anticipated this in our Q3FY2007 capital goods earnings preview. We expect the material pricing pressure to be lesser in the subsequent quarter.

Copper coming of peaks



Source:- LME

Huge cash reserves yielding fruits--other income up 60% yoy

BHEL has always been a cash rich company as is evident by the huge Rs4,100 cash pile on its balance sheet as of March 31, 2006. BHEL's other income during the quarter increased by 56.2% yoy to Rs185.5 crore mainly on account of the rising yields on the huge cash reserves of the company. Also as BHEL's export revenue was higher during the quarter, the export incentive (which BHEL shows in the other income) buoyed the other income component. This coupled with the stable depreciation and a lower interest rate resulted in the net profit growing by 57.8% during the quarter to Rs667.7 crore, sharply above our expectations.

Order book soars to Rs46,700 crore

BHEL's order backlog during the quarter maintained its momentum and grew by a very impressive 38.2% yoy to Rs.46,700 crore, resulting in an order inflow of Rs5,710 crore. Though the inflow during the quarter was slower at 9.5% we are not overtly concerned as there are some key orders that have been awarded post this quarter and the backlog is at 3.2x FY2006 sales and 2.7x trailing twelve-month sales giving the revenues of BHEL a great visibility. With the power capacity addition of 68,000MW for the Eleventh Five-Year Plan, we expect BHEL's order backlog to maintain the momentum going forward.

Order book Details

	Q3FY07	Q3FY06	VAR (%)
Order book details			
Order at the beginning of the quarter	45700	32200	42
Order inflow	5710	5215	9
Revenue booked	4710	3615	30
Order backlog at the end of the quarter	46700	33800	

BHEL declares interim dividend of Rs12.5/share and a bonus of 1:1

BHEL has declared an interim dividend of 125%, ie Rs12.5 per share of Rs10 each. BHEL has also announced a bonus issue of shares in the ratio of one share for every one held. The record date for the bonus issue is expected to be announced shortly.

Valuation and view

BHEL's Q3FY2007 results are sharply above our and street expectations, primarily because of a sharp jump in the margins. Going forward, the huge orders from the generation companies like NTPC and Reliance Energy would drive the company's order books and earnings. Further the government's increasing thrust on ultra mega power projects, the company's order book could receive a tremendous boost, as each of the 4,000MW project would be worth over Rs10,000 crore. At the current levels, the stock is trading at 20.0x its FY2008E earnings and 12.0x its FY2008E EBIDTA. Given the expectations of the continued growth in its order book, a strong earnings growth of a CAGR of 35.1%, we believe the valuations are attractive. Even on a comparative basis the stock is trading at a significant discount to its peers like Siemens, ABB and Areva. We maintain our Buy recommendation on the stock with a price target of Rs2,650.

Earnings table

Year ended March 31	FY04	FY05	FY06E	FY07E	FY08E
Net profit (Rs Cr)	658.1	955.0	1679.3	2416.8	3066.0
% y-o-y growth	*6.2*	*22.6*	*74.0*	*43.9*	*26.9*
Shares in issue (Cr)	24.5	24.5	24.5	24.5	24.5
EPS (Rs)	26.9	39.0	68.6	98.7	125.3
% y-o-y growth	*6.2*	*22.6*	*74.0*	*43.9*	*26.9*
PER (x)	93.2	64.2	36.5	25.4	20.0
Book Value (Rs)	216.4	246.2	298.3	376.3	475.3
P/BV (Rs)	11.6	10.2	8.4	6.7	5.3
EV/EBIDTA (x)	65.6	41.0	23.2	16.5	12.0
Dividend yield (%)	0.2	0.3	0.6	0.8	1.0
RoCE (%)	19.2	26.8	36.4	42.3	44.3
RoNW (%)	12.4	15.8	23.0	26.2	26.4

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

JK Cement

Cannonball

Stock Update

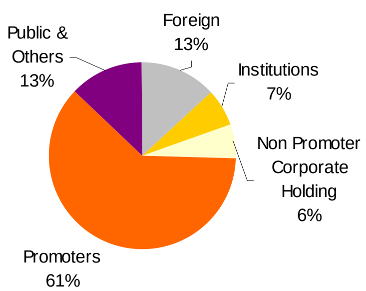
Q3FY2007 results beat expectations

Buy; CMP: Rs193

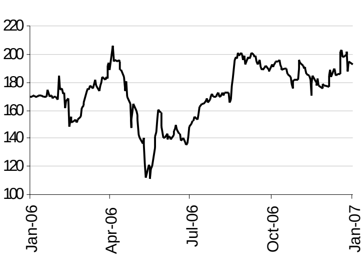
Company details

Price target:	Rs295
Market cap:	Rs1,349 cr
52 week high/low:	Rs231/109
NSE volume: (No of shares)	59,954
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	10.7	3.3	43.2	16.4
Relative to Sensex	4.4	-8.8	4.0	-22.2

Result highlights

- JK Cement has reported a net profit of Rs50 crore, much ahead of our expectations, clocking a mammoth year-on-year (y-o-y) growth of 544%.
- The net sales grew by a healthy 44% year on year (yoy) to Rs319 crore on the back of a buoyant 36% growth in the average cement realisations to Rs3,186 per tonne. The grey cement realisations improved by 45% yoy and by 6% quarter on quarter (qoq) to Rs2,917 per tonne whereas the white cement realisations improved by 14.6% yoy and by 5% qoq to Rs7,609 per tonne.
- The company's operating expenditure grew by 22% yoy to Rs230.7 crore, lower than expected. The power & fuel costs reduced marginally to Rs77.2 crore on a y-o-y basis on account of an increase in the share of blended cement to 56% vis-à-vis 40% last year. The freight expenses increased by 24% yoy to Rs59.2 crore whereas the costs per tonne declined marginally by Rs15 on a sequential basis.
- On account of the company's high leverage to the cement prices as well as a benign increase in the costs, the company's operating expenditure increased by 168% yoy to Rs88.3 crore. The operating margins expanded by a huge 1,430 basis points yoy and by 5% qoq to 28%. The cumulative impact of the rising prices and lower costs resulted in the earnings before interest, tax, depreciation and amortisation (EBITDA) per tonne multiplying 2.75x yoy to Rs882.
- The company's net interest cost has reduced by 47% yoy to Rs8.1 crore on account of a) an interest income component of Rs4 crore from the unutilised proceeds of the foreign currency convertible bonds (FCCBs); and b) the quarterly repayment

Result table Rs (cr)

Particulars	Q3FY07	Q3FY06	% yoy	9MFY07	9MFY06	% yoy
Net sales	319.0	221.7	44.0	866.7	702.0	23.5
Total expenditure	230.7	188.4	22.0	649.2	574.7	13.0
Operating profits	88.3	33.3	165.0	217.5	127.4	70.8
Other income	1.5	1.8	-17.0	3.3	5.2	-36.5
EBIDTA	89.8	35.1	156.0	220.8	132.6	66.6
Interest	8.1	15.4	-47.0	25.5	37.5	-32.0
PBDT	81.7	19.7	315.0	195.3	95.1	105.4
Depreciation	8.2	7.6	8.0	24.5	25.4	-3.5
PBT	73.5	12.1	507.0	170.8	69.7	145.2
Tax	20.3	4.3	372.0	54.6	21.2	158.1
Deferred tax	2.7	0.0		2.7	2.0	35.0
Fringe benefit tax	0.3			0.3	0.0	
Reported profit after tax	50.2	7.8	544.0	113.2	46.5	143.4
Operating margins (%)	28.0	13.7		25.1	18.1	
EBIDTA(%)	28.2	15.0		25.4	18.7	
PBDT (%)	25.6	7.5		22.4	13.4	
PATM (%)	15.7	2.4		13.0	6.6	

of the long-term debt. The depreciation provision stood flat at Rs8.2 crore. Consequently, the net profit zoomed by 544% yoy to Rs50 crore.

- The company has acquired the manufacturing facilities of Nihon Nirmaan Limited from IDBI Limited for Rs42 crore and thus will be able to add close to 3.5 lakh tonne of grey cement to its existing capacity.
- Considering the better-than-expected performance in the 9-month period as well as factoring in the acquisition of the new facility, we are upgrading our FY2007 and FY2008 earnings estimates by 13% to Rs167 crore and by 3% to Rs222.3 crore respectively. The revised earnings per share (EPS) would stand at Rs24.9 for FY2007 and Rs31.8 for FY2008.
- At the current price of Rs193, the stock is discounting its FY2007E earnings by 7.9x and FY2008E earnings by 6.1x. On an enterprise value/tonne basis, the stock is trading at a valuation of USD73.5 per tonne whereas its closest peer Shree Cement commands a valuation of USD179 per tonne. Even after discounting for the efficient cost structure and the consistent performance of Shree Cement, we believe such a steep discount is unjustified and thus the company should command higher valuations. We maintain our Buy recommendation on the stock with a price target of Rs295.

Top line registers a healthy 44% y-o-y growth

With the construction activity picking up in the northern region, the cement volumes have picked up in the third quarter, which was reflected in JK Cement's grey cement volumes, which increased sequentially by 16% to 944,000 tonne. The white cement volumes stood at 57,000 tonne. The average realisations grew by 35% yoy and by Rs100 per tonne sequentially to Rs3,165 per tonne. The grey cement realisations improved by 45% yoy and by 6% qoq to Rs2,917 per tonne whereas the white cement realisations improved by 14.6% yoy and by 5% qoq to Rs7,609 per tonne. The cumulative impact of the buoyant volumes and higher realisations resulted in the net sales growing by a robust 44% to Rs319 crore.

Volumes	Q3FY07	Q3FY06	% yoy	Q2FY07	% qoq
Grey	944000	896000	5.0	814000	16.0
White	57000	56000	2.0	60900	-6.0
Realisations					
Grey	2917	2011	45.0	2752	6.0
White	7609	6638	15.0	7274	4.6

Operating expenditure witnesses a 22% y-o-y growth...

The company's operating expenditure grew by 22% yoy to Rs230.7 crore, lower than expected. The power & fuel costs reduced marginally to Rs77.2 crore on a y-o-y basis on account of an increase in the share of blended cement to 56% vis-à-vis 40% last year. The grid price reduction of 20 paise also aided in the reduction of the power costs, which consequently led to the costs per tonne reducing by 8% sequentially. The freight expenses increased by 24% yoy to Rs59.2 crore whereas the costs per tonne declined marginally by Rs15 on a sequential basis.

Per tonne analysis

Expenditures per tonne	Q3 FY07	Q3 FY06	% yoy chng	Q2 FY07	% qoq chng
Raw material consumed	306.7	225.0	36.3	337.2	-9.0
Stock adjustment	47.0	29.7	58.1	-27.4	-271.0
Stores	212.8	0.0		225.2	-5.0
Employee expenses	124.9	117.6	6.2	134.9	-7.0
Power, oil & fuel	771.2	750.3	2.8	839.0	-8.0
Freight	591.4	478.5	23.6	602.4	-2.0
Other expenses	250.8	427.1	-41.3	228.6	10.0
Total exp	2304.7	2028.1	13.6	2339.7	-1.0
Realisation	3186.8	2350.1	35.6	3065.5	4.0
EBIDTA/Tonne	882.1	322.0	173.9	725.8	22.0

...operating profit grows by 168% year on year

On account of the company's high leverage to the cement prices as well as a benign increase in the costs, the company's operating expenditure increased by 168% yoy to Rs88.3 crore. The operating margins expanded by a huge 1,430 basis points yoy and by 5% qoq to 28%. The cumulative impact of the rising prices and lower costs resulted in EBITDA per tonne multiplying 2.75x yoy to Rs882.

Net profit zooms by 544% yoy to Rs50.2 crore

The company's net interest cost has reduced by 47% yoy to Rs8.1 crore on account of a) an interest income component of Rs4 crore from the unutilised proceeds of FCCBs; and b) the quarterly repayment of the long-term debt. The depreciation provision stood flat at Rs8.2 crore resulting in the net profit zooming by 544% to Rs50 crore.

New acquisition to add 3.5 lakh tonne to the volumes...

The company has acquired the manufacturing facilities of Nihon Nirmaan Limited from IDBI Limited for Rs42 crore. The facility, which can currently manufacture white cement, will be refurbished to manufacture grey cement towards which the company plans to spend Rs33 crore. Upon completing this exercise, the company will be able to add close to 3.5 lakh tonne of grey cement to its existing capacity. The company plans to finish this exercise by September 2007 and thus the capacity will be available effectively for 6 months of FY2008. The company plans to fund the total sum of Rs75 crore through a debt and expects to avail itself an interest subsidy of 5% from the government of Rajasthan.

...will also result in marginal reduction in freight cost

This facility, which is 2kms away from its existing white cement facility at Gotan, will be used to serve the nearby markets. These markets are currently served by the facility at Nimbahera whose lead distance to these markets is 550-600kms. Going ahead, the nearby markets will be fed by this facility, which will result in the lead distance coming down from 600kms to 300kms. Consequently, the company will be able to save close to Rs300 per tonne, which will add to the margins of the company.

Upgrading earnings for FY2007 and FY2008

Considering the better-than-expected performance in the 9-month period as well as factoring in the acquisition of the new facility, we are upgrading our FY2007 and FY2008 earnings estimates by 13% to Rs167 crore and by 3% to Rs222.3 crore respectively. The revised EPS would stand at Rs24.9 for FY2007 and Rs31.8 for FY2008.

Valuation and view

JK Cement has shown an impressive performance in the last three quarters as fallout of the buoyant cement price scenario across the country, more so in the northern region. Its leverage to the cement prices has resulted in its EBITDA per tonne multiplying 2.7x to Rs882 per tonne in the third quarter of the current fiscal year. Realising the importance of managing the power cost, which currently stands very high compared to its peers, the company had undertaken to set up 3 captive power plants (CPPs) of which one CPP of 10MW has already been commissioned in December 2006. One of the other two CPPs will be commissioned by April 2007 whereas the third plant will be commissioned in June 2007. Once these facilities are up and running, the company will be able to drastically cut its power costs leading to savings of Rs200 per tonne.

Going ahead, the Nihon facility will add close to 3.5 lakh tonne to its existing grey cement volumes. The rising prices, savings in the costs as well as increased volumes will lead to the company's net profit registering a 161% compounded annual growth rate (CAGR) over FY2006-08E coupled with the operating margins doubling to 30% in FY2008. At the current price of Rs193, the stock is discounting its FY2007E earnings by 7.9x and FY2008E earnings by 6.1x. On an enterprise value/tonne basis, the stock is trading at a valuation of USD73.5 per tonne whereas its closest peer Shree Cement commands a valuation of USD179 per tonne. Even after discounting for the efficient cost structure and the consistent performance of Shree Cement, we believe such a steep discount is unjustified and thus the company should command higher valuations. We maintain our Buy recommendation on the stock with a price target of Rs295.

Earnings table

Year ended March 31	FY05	FY06	FY07E	FY08E
Net profit (Rs cr)	6.5	32.5	167.6	222.8
% y-o-y growth		*400.0*	*357.0*	*49.8*
Shares in issue (Cr)	5.0	5.0	7.0	7.0
EPS (Rs)	1.3	6.5	24.0	31.9
PER (x)	148.2	41.5	7.9	6.1
EV/EBIDTA (x)	50.0	12.5	5.9	4.3
RoCE (%)	6.8	9.6	20.3	24.4
RoNW (%)	1.7	4.8	18.6	22.3

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

Information Technology

Sector Update

A quarter of strong performance

Key points

- The Indian information technology (IT) services companies reported a robust performance in a difficult quarter. The volume growth continues to be healthy and most of the companies were able to show an improvement in the margins on a sequential basis, despite the adverse impact of the steep appreciation of the rupee.
- The outlook is optimistic in terms of the demand environment as well as the pricing scenario. Despite the expected slow-down in the growth of the IT budgets, the growing awareness and willingness to increase offshore outsourcing is likely to drive the growth in the calendar year 2007. However, the exchange rate fluctuations continue to be the wild card that could potentially spoil the party.
- In the note, we have revised the price targets of the companies under our coverage in line with the expected growth in the coming years. We prefer Infosys Technologies and HCL Tech among the front-line stocks. In the mid-cap space, our top picks are NIIT Tech and 3i Infotech.

Changes in price targets (Rs)

	Earlier target price	Revised target price
Front-line companies		
Infosys	2430	2670
TCS	1500	NC
Wipro	700	NC
Satyam	550	NC
HCL Tech	720	820
Mid-cap companies		
3i Infotech	308	375
Nucleus Software	898	NC
Tata Elxsi	320	NC
NIIT Tech	474	570
ORG Info	190	NC

NC= No change

Review of quarterly performance

The Indian IT services companies have reported an encouraging performance in a quarter that was mired with the double impact of the lower number of working days and a steep appreciation of the rupee. Some of the key takeaways from the quarterly performance are given below.

Revenue growth

The volumes growth in the range of 7-9% was quite decent given the fact that the quarter had three less working days due to the festive season. However, the same was already anticipated and built into the street expectations.

The positive surprise came from the healthy growth in the average realisations (or the billing rates moved up by 0.3% to 2% sequentially) in most of the cases, which was way ahead of the expectations. The only exception was Wipro that showed a sequential decline in the billing rates.

Margins

The ability to manage the adverse impact of the rupee appreciation on the margins as well as the other income component was another key positive that emerged from the quarterly performance. The companies were able to show a healthy improvement in the margins with the exception of Wipro where the margins were also hit by the annual salary hikes.

The rupee appreciation adversely impacted the margins by 80 to 200 basis points on a sequential basis. However, the front-line companies were able to mitigate the same by utilising various levers of margins improvement such as productivity gains (through cost efficiencies in the fixed priced projects) that were not anticipated to make such a notable impact on the margins.

Employee matrix

In terms of the operational matrix, the recruitment in the first nine-month period of the fiscal is quite healthy with an average increase of 29.8% (excluding HCL Tech where the figures are not comparable) over the base as on end of March 2006. This coupled with the fact that the utilisation levels are comfortable (and at the lower end of the range usually maintained) the companies have built a reasonable size of the bench strength to meet any upsurge in the demand going forward. On the flip side, the attrition rate continues to be high (though it has largely stabilised for most of the companies, excluding Infosys).

Outlook

The outlook is optimistic in terms of the demand environment and the pricing scenario. Despite the expected slow-down in the growth of the IT budgets, the growing awareness and willingness to increase offshore outsourcing is likely to drive the growth in the calendar year 2007. The view on the pricing continues to be stable with an upward revision in the rates from some of the existing clients and the new clients coming in at a billing rate 3-5% higher than the average rates. Thus, the exchange rate fluctuations continue to be the wild card that could potentially spoil the party.

On the other hand, the key negative factor was the subdued outlook for the seasonally weak fourth quarter. This coupled with the continued strengthening of the rupee could limit the upside in the valuations over the next couple of months.

Overall, the quarterly performance has reinforced the investor confidence in the ability of the front-line companies to maintain the revenue growth momentum. Moreover, some of the key concerns related to the ability to maintain the margins in a tough environment have also been addressed. However, there are some areas of concerns like the attrition rate, exchange rate and the other company specific issues like the continued losses in the subsidiaries.

Top picks

Our top picks among the front-line stock are Infosys Technologies and HCL Technologies. In the mid-cap space, we prefer NIIT Technologies and 3i Infotech.

Key operational metrics

	Infosys	TCS	Wipro*	Satyam	HCL Tech#
Revenue growth					
- % chg qoq (in $ terms)	10.1%	12.6%	8.8%	6.7%	9.2%
- % chg qoq (in Rs terms)	5.9%	8.4%	6.2%	3.7%	5.2%
Volume growth					
- % chg qoq	7.4%	7.9%	9.3%	8.2%	7.1%
Billing rates					
- Onsite (% chg qoq)	1.9%	NA	-0.5%	0.4%	9.3%
- Offshore (% chg qoq)	1.7%	NA	-0.3%	0.1%	-4.0%
- Blended (% chg qoq)	1.4%	2.0%	-0.4%	0.3%	2.0%
Exchange rate impact on revenue					
- % chg qoq	-3.8%	-3.7%	-2.3%	-2.8%	-3.9%
Recruitment					
- Net employee addition					
June'06	5694	4698	2841	1123	
Sep'06	7741	6663	5326	4025	1611
Dec'06	3282	5562	3489	2746	580
Total YTD FY2007	**16717**	**16923**	**11658**	**7894**	**2191**
- % chg over YTD FY2006**	31.9%	-7.1%	11.6%	85.0%	86.6%
- % increase on base(March'06)	31.7%	26.9%	31.8%	29.8%	10.8%
Employee Utilisation (%)					
- Gross	65.7%	75.0%	62.0%	68.5%	69.4%
% bps chg yoy	-330	10	-100	-580	-310
- Net	75.8%	78.2%	67.0%	77.6%	74.6%
% bps chg yoy	-290	50	-100	-210	NA
Attrition rate					
- IT services (Q3 LTM)	13.5%	10.8%	16.0%	17.6%	17.8%
Salary hikes	Taken in Q1	Taken in Q1	Taken only for offshore	Taken in July	Taken in Q2 & Q3
Operating margin					
- Absolute	32.7%	28.3%	23.7%	24.7%	22.8%
- Bps chg qoq	60	87	-80	205	50
- Forex impact qoq in Q3	-200	-140	-80	-120	-150
- Outlook for Q4	Stable/ improve	Stable/ improve	Stable/ Decline	Decline	Stable/ improve
Implied CQGR					
- Net sales	8.3%	7.9%	6.8%	5.4%	6.2%
- Net profit	9.0%	5.5%		8.7%	2.5%

* In case of Wipro, the figures pertain to the global IT services business.

HCL Tech is a June ending company, and the above figures are only for the software services business (implied growth for the consolidated accounts).

** Figures in case of TCS are not comparable due to consolidation of Tata Infotech employee base in FY2006. In case of Satyam and HCL Tech the percentage growth appears to be skewed due to the bulk of recruitment being concentrated in Q4 in FY2006.

Valuation

We are introducing the earnings estimates for FY2009 and aligning the one-year target price of the front-line stocks with the same. Consequently, the target prices of Infosys Technologies (24x FY2009 earnings to Rs2,670) and HCL Technologies (17x FY2009 earnings to Rs820) have been upgraded whereas the same for Wipro (22.8x FY2009), TCS (22.5x FY2009) and Satyam Computers (18x FY2009) have been maintained.

Infosys continues to be out top pick in the sector with a 20% upside to the target price from the current levels, followed by HCL Technologies that is trading at comparatively attractive valuations (11% discount to Satyam based on FY2009 estimates).

Valuation matrix - frontline stocks

	EPS (Rs)			P/E		
	FY07	FY08	FY09	FY07	FY08	FY09
Infosys	67.8	90.0	112.0	33.1	24.9	20.0
TCS	42.1	53.9	66.8	30.8	24.0	19.4
Wipro	20.1	25.0	30.7	31.4	25.2	20.6
Satyam	21.0	25.2	30.5	22.1	18.4	15.2
HCL Tech	33.5	41.5	48.3	19.7	15.9	13.7

In case of mid-cap IT companies, the price target of 3i Infotech is revised to Rs375 (15x rolling four quarters forward earning estimates in line with Nucleus software) and NIIT Technologies to Rs580 (13x rolling four quarters forward earning estimates, which is at a discount to the valuations of the product-centric mid-cap companies) whereas the target prices of Tata Elxsi, Nucleus Software and ORG Informatics remain unchanged. In the mid-cap space, we prefer NIIT Technologies (39% upside from the current levels) and 3i Infotech (27% upside from the current levels) as our top picks.

Valuation matrix - mid-cap stocks

	EPS (Rs)		P/E	
	FY07	FY08	FY07	FY08
3i Infotech	14.5	20.5	20.4	14.4
Nucleus Software	35.5	49.1	24.6	17.8
Tata Elxsi	15.3	19.9	19.5	15.0
NIIT Tech	31.3	36.5	13.1	11.2
ORG Info	10.1	14.7	16.6	11.4

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

Sharekhan Stock Ideas

Evergreen

HDFC Bank
Infosys Technologies
Reliance Industries
Tata Consultancy Services

Apple Green

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

Cannonball

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

Emerging Star

3i Infotech
Aban Offshore
Alphageo India
Cadila Healthcare
Federal-Mogul Goetze (India)
KSB Pumps
Marksans Pharma
Navneet Publications (India)
New Delhi Television
Nucleus Software Exports
Orchid Chemicals & Pharmaceuticals
ORG Informatics
Solectron Centum Electronics
Tata Elxsi
Television Eighteen India
Thermax
TVS Motor Company
UTI Bank

Ugly Duckling

Ahmednagar Forgings
Ashok Leyland
BASF India
Ceat
Deepak Fertilisers & Petrochemicals Corporation
Fem Care Pharma
Genus Overseas Electronics
HCL Technologies
ICI India
India Cements
Indo Tech Transformers
Jaiprakash Associates
JM Financial
KEI Industries
NIIT Technologies
Punjab National Bank
Ratnamani Metals and Tubes
Sanghvi Movers
Saregama India
Selan Exploration Technology
South East Asia Marine Engineering & Construction
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UltraTech Cement
Union Bank of India
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Wockhardt

Vulture's Pick

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