investor's eye

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Index

Take Five

Scrip	Reco Date	Reco Price	CMP	Target
BEL	26-Sep-06	1,108	**1,163**	1,525
ICICI Bank	23-Dec-03	284	**720**	770
India Cements	28-Sep-06	220	**225**	315
ITC	12-Aug-04	69	**194**	220
TV18	23-May-05	214	**636**	704

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KEI Industries

Ugly Duckling

Stock Update

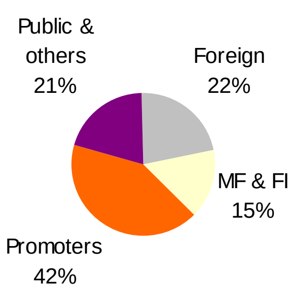
Power packed performance

Buy; CMP: Rs361

Company details

Price target:	Rs500
Market cap:	Rs369 cr
52 week high/low:	Rs529/159
NSE volume: (No of shares)	58,066
BSE code:	517569
NSE code:	KEI
Sharekhan code:	KEIINDUS
Free float: (No of shares)	58.4 lakh

Shareholding pattern



Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	6.4	27.0	-23.9	98.6
Relative to Sensex	-0.6	8.0	-33.6	28.8

Result highlights

- In Q2FY2007 KEI Industries (KEI) recorded a robust growth of 96% year on year (yoy) in its net profit to Rs10.1 crore. The growth was in line with our expectations.
- KEI's net sales for the quarter rose to Rs136.8 crore, up 108.6% yoy and by 37.7% quarter on quarter (qoq). The revenues from the cable segment grew by 105.3% yoy and by 35.6% qoq on the back of expanded capacities.
- The operating profit grew by 142.5% yoy and by 45.2% qoq as the operating profit margin (OPM) expanded by 225 basis points yoy and by 83 basis points qoq.
- However, the pressure on the raw material cost continued as the raw material consumed (RMC)/sales ratio increased by 100 basis points to 70.1% during the quarter.
- The profit before tax (PBT) increased by 137% yoy and by 39.5% qoq. However, the net profit grew by a lower 95.8% yoy and by 33.2% qoq because of a higher effective tax rate.
- KEI is planning a foreign currency convertible bond (FCCB) issue of $35 million (Rs150 crore) to fund its expansion at Uttaranchal. The funds would be raised over the next three to four weeks. The promoters are ready to dilute their stake up to 10% which means the issue may be priced at Rs440-450 per share.
- At the current market price of Rs361, the stock quotes at 7.4x its FY2008E earnings per share (EPS) and 4.5x its enterprise value (EV)/earnings before interest, depreciation, tax and amortisation (EBIDTA). We maintain our Buy recommendation on KEI with a price target of Rs500.

Net sales grow by robust 108.6% yoy

KEI's net sales for the quarter grew by 108.6% yoy to Rs136.8 crore backed by improved capacity utilisation at the high-tension (HT) cable plant and marginally improved price realisations.

Result table Rs (cr)

Particulars	H1FY07	H1FY06	% yoy chg	Q2FY07	Q2FY06	% yoy chg	% qoq chg
Net sales	236.1	130.6	80.8	136.8	65.6	108.6	37.7
Other income	0.2	0.3	-42.6	0.0	0.0	394.6	-63.5
Total income	236.2	130.9	80.5	136.8	65.6	108.6	37.6
Total expenditure	198.9	113.1	75.9	114.8	56.5	103.1	36.4
Operating profit	37.2	17.5	112.2	22.0	9.1	142.5	45.2
Interest	9.2	4.4	111.4	5.9	2.2	160.7	74.8
Depreciation	2.9	1.2	149.8	1.5	0.6	135.3	7.1
Profit before tax	25.2	12.3	105.1	14.7	6.2	137.0	39.5
Tax	7.5	2.1	262.3	4.6	1.0	342.3	55.8
Profit after tax	17.7	10.2	73.2	10.1	5.2	95.8	33.2
OPM (%)	15.7	13.4		16.1	13.8	224.9	82.7

Gross sales

Rs crore	H1 FY07	H1 FY06	% yoy chg	Q2 FY07	Q2 FY06	% yoy chg	% qoq chg
Revenues							
Cable	231.4	128.6	80.0	133.2	64.9	105.3	35.6
SS	35.4	19.8	79.0	20.7	9.6	116.6	40.5
Total	266.9	148.4	79.9	153.9	74.4	106.7	36.2

Gross sales (plant-wise)

Particulars	Rs crore
Existing facilities	Rs119 crore
HT cable plant	Rs35 crore
Of which	
HT cable	*Rs15 crore*
LT cable	*Rs20 crore*

Operating profit grows by a stronger 142.5% yoy...

Backed by better economies of scale the operating profit grew by 142.5% (by 45.2% qoq) as the OPM expanded by 225 basis points yoy and by 89 basis points qoq.

Segmental PBIT

Rs crore	H1 FY07	H1 FY06	% yoy chg	Q2 FY07	Q2 FY06	% yoy chg	% qoq chg
Cable	36.3	19.8	82.8	21.3	10.0	113.2	41.6
Margins (%)	*15.7*	*15.4*		*16.0*	*15.4*		
SS	3.3	0.5	566.2	2.2	0.3	690.2	91.3
Margins (%)	*9.3*	*2.5*		*10.4*	*2.9*		
Total	39.6	20.3	94.5	23.4	10.2	128.5	45.1
Margins (%)	*14.8*	*13.7*		*15.2*	*13.8*		

...but pressure on raw material cost continues

The raw material cost as a percentage of sales increased by 110 basis points yoy during Q2FY2007 due to an increase in the price of the raw materials.

The RMC/sales ratio (adjusted for stocks) increased by 370 basis points yoy and by 196 basis points qoq. However, the management has attributed the same to the need to carry higher inventories to meet the strong demand for the products.

Finance charges rise steeply

During the quarter under review KEI's finance charges rose steeply by nearly 75% over Q1FY2007. The rise could be attributed to the increased finance charges on letters of credit and bank guarantees as well as increased borrowings to meet its working capital requirements.

Net profit grew at a marginally lower rate due to higher taxes

In Q2FY2007 the net profit grew at a marginally lower rate of 96% yoy and of 33.2% qoq due to higher interest cost and effective tax rate. The effective tax rate for the quarter stood at 31.2% compared with 16.7% for Q2FY2006 and 27.9% for Q1FY2007.

Strong order book of Rs180 crore

KEI had an order book of Rs180 crore on hand (compared with Rs100-120 crore as on June 30, 2006) as on September 30, 2006, executable over a period of two to three months. Of the total order book nearly Rs45 crore is for HT cables.

Pick-up in HT cable business

KEI's HT cable business has slowly started picking up: its customer approvals increased to ten in Q2FY2007 from just two in Q1FY2007. KEI is expecting to add another 15 customers during Q3FY2007 and take the total tally to 25 by the end of Q3FY2007.

Expansion plans to become clear over next two months

KEI is planning another Rs170-crore expansion in the state of Uttaranchal. The company is planning to raise $30 million (Rs132 crore) with a greenshoe option of $5 million (Rs18 crore) through an FCCB issue. The draft letter of offer will be filed with the Luxemburg Stock Exchange by next month. The promoters are ready to dilute equity up to 10-11%; this means the issue could be done at a conversion price of Rs440-450 per share.

KEI plans to commence the operation of the Uttaranchal plant by December 2007. The land for the expansion is expected to be acquired by November 2006.

Valuation and view

We expect KEI's revenues to grow at a compounded annual growth rate (CAGR) of 52% over FY2006-08E as

- the HT cable plant will be operational for full FY2008;
- the additional capacity for LT cable at the existing plant at Silvassa may commence operations by September 2006;
- KEI is putting up a control cable plant at the existing facility for HT cables at a cost of Rs5-6 crore and the same will be operational throughout FY2008.

The new plant at Uttaranchal will be contributing to the growth from FY2009 onwards.

At the current market price of Rs361, the stock quotes at 7.4x its FY2008E EPS and 4.5x its EV/EBIDTA. We maintain our Buy recommendation on KEI with a price target of Rs500.

Key financials

Particulars	FY2005	FY2006E	FY2007E	FY2008E
Net profit (Rs cr)	8.6	26.0	45.2	58.0
Shares in issue (cr)	0.8	1.0	1.2	1.2
EPS (Rs)	10.9	25.8	38.4	49.2
% y-o-y change	*911.8*	*137.3*	*48.9*	*28.2*
PER (x)	33.3	14.0	9.4	7.4
Book value (Rs)	35.5	94.4	117.2	181.9
P/BV (x)	10.2	3.8	3.1	2.0
EV/EBIDTA (x)	19.2	9.8	5.5	4.5
RoCE (%)	29.1	32.6	36.5	33.1
RoNW (%)	34.9	42.3	38.8	32.9

Crompton Greaves

Apple Green

Stock Update

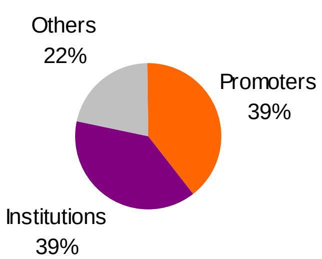
Margins under pressure

Buy; CMP: Rs240

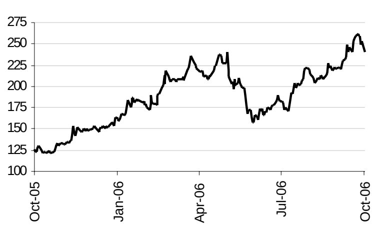
Company details

Price target:	Under review
Market cap:	Rs6,292 cr
52 week high/low:	Rs270/120
NSE volume: (No of shares)	67,995
BSE code:	500093
NSE code:	CROMPGREAVE
Sharekhan code:	CROMPTON
Free float: (No of shares)	15.9 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	13.8	36.4	14.0	99.6
Relative to Sensex	6.3	15.9	-0.6	29.4

Result highlights

- Crompton Greaves' revenues grew by 48.6% year on year (yoy) in Q2FY2007 to Rs824.0 crore, beating our expectations. Although all its three divisions reported a strong performance, the power system division led the pack with a revenue growth of 68.7% yoy to Rs449.7 crore. The revenue of the consumer product division grew by 33.3% yoy to Rs225.3 crore and that of the industrial system division grew by 36.8% yoy to Rs226.1 crore.
- The raw material cost/sales ratio spiked to 75.6% in Q2FY2007 from 69.5% in Q2FY2006 largely due to an increase in the prices of the base metals like copper and steel, and the inability of the company to pass on the same to its customers. However, lower employee and other expenses muted the impact of the same. Consequently, the operating profit margin (OPM) reduced by 60 basis points yoy to 8.9% and the operating profit for the quarter grew by 39.1% to Rs73.6 crore.
- The profit before interest and tax margin of the power system division declined by 50 basis points to 8.0% during the period. The high-margin businesses maintained their margins (the consumer product division's margin was up 10 basis points to 9.7% and the industrial system division's margin was up 20 basis points to 13.6%).
- Crompton Greaves moved out of the ambit of the minimum alternate tax (MAT) in Q3FY2006 and hence paid tax at the full tax rate in Q2FY2007 as against at the MAT rate in Q2FY2006. Also, it provided for deferred tax to the tune of Rs7.5 crore. The increased tax provisioning led to a slower growth of 25.0% yoy to Rs40.7 crore in the profit after tax. But the growth was still in line with our expectations.
- The top line and PBT of its Belgium subsidiary, Pauwels, stood at Rs595.38 crore and Rs21.3. crore respectively during the quarter.

Result table Rs (cr)

Particulars	Q2FY2007	Q2FY2006	% yoy chg
Net sales	824.0	554.6	48.6
Expenditure	750.4	501.7	49.6
Operating profit	73.6	52.9	39.1
Other income	9.4	6.5	44.8
PBIDT	83.0	59.4	39.7
Interest	7.2	5.9	22.7
Depreciation	8.1	10.4	-22.6
PBT	67.7	43.1	57.0
Tax	27.04	10.59	155.3
PAT	40.7	32.5	25.0
EPS (Rs/Share)	1.6	1.2	25.0
OPM (%)	8.9	9.5	-60 bps
PBTM (%)	8.2	7.8	40 bps
PATM (%)	4.9	5.9	-100 bps

- The stand-alone order book grew by 0.6% sequentially and by 20.0% yoy to Rs1,800.0 crore in Q2FY2007. The consolidated order book stood at Rs3,739.0 crore.
- The board has announced a bonus of two shares for every five shares held.
- The stock is currently hovering around our price target of Rs239. Although the top line performance of Crompton Greaves in H12007 has beaten our estimates, yet there is a severe threat to the OPM going forward and the same poses a risk to our call. We are in the process of revising our estimates and may revise our price target as well.
- At the current market price of Rs240, Crompton Greaves is trading at 28.4x its FY2008E stand-alone earnings and 19.1x it's FY2008E consolidated earnings.

UltraTech Cement

Ugly Duckling

Stock Update

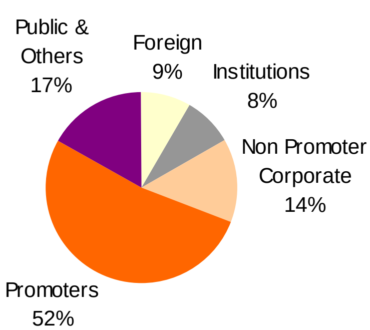
Results below expectations

Buy; CMP: Rs886

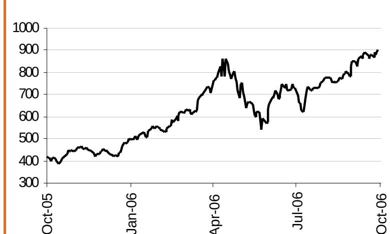
Company details

Price target:	Rs1,000
Market cap:	Rs11,022 cr
52 week high/low:	Rs921/381
NSE volume: (No of shares)	84,365
BSE code:	532538
NSE code:	ULTRACEMCO
Sharekhan code:	ULTRACEM
Free float: (No of shares)	5.9 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	15.3	24.2	27.6	107.0
Relative to Sensex	7.6	5.6	11.3	34.2

Result highlights

- UltraTech Cement Ltd (UCL) has announced a net profit of Rs127.4 crore for Q2FY2007 and the same is below our expectations, primarily because of higher-than-expected power & fuel cost and other expenditure.
- The company's revenue for the quarter grew by a healthy 58.3% to Rs1,004 crore driven by a 17% rise in its cement volume and a 35.2% increase in its cement realisation.
- The operating profit for the quarter grew by 291.8% to Rs254.5 crore as the operating profit margin (OPM) expanded by 15.1 percentage points to 25.3%. The same was however below our expectations primarily because of higher-than-expected power & fuel cost and other expenditure.
- During the quarter UCL's jetty situated at its Gujarat plant was non-operational for about 15 days. Hence the company not only lost some export volumes but also had to incur an additional expense of Rs15-20 crore on its repairs. Also the packing cost has gone up by Rs10 crore. This in turn increased the other expenditure per tonne by 30% yoy. Had these costs not been there, the company would have easily met our estimates.
- During the quarter UCL's cost per tonne of cement increased by 12.5% against a 35% rise in realisation per tonne. Hence its earnings before interest, tax, depreciation and amortisation (EBITDA) per tonne in the quarter stood at Rs691 against Rs206 per tonne in Q2FY2006.
- On the back of flat interest cost and depreciation charge, the net profit for the quarter registered a quantum jump to Rs127.4 crore during the quarter.

Result table Rs (cr)

Particulars	Q2FY07	Q2FY06	% yoy chg	H1FY07	H1FY06	% yoy chg
Net sales	**1004.5**	**634.51**	**58.3**	**2184.8**	**1449.5**	**50.7**
Total expenditure	750.1	569.6	31.7	1555.8	1235.4	25.9
Raw material consumed	84.2	55.5	51.6	175.1	125.6	39.4
Stock adjustment	-1.1	-23.5		-11.0	-37.1	-70.3
Purchase of finished goods	24.2	88.8	-72.8	49.9	152.4	-67.3
Employee expenses	29.4	18.9	55.6	56.9	34.4	65.3
Power, oil & fuel	248.5	181.2	37.1	534.0	391.5	36.4
Freight & handling	206.2	144.1	43.1	451.8	322.9	39.9
Other expenses	158.7	104.6	51.8	299.1	245.5	21.8
Operating profit	**254.5**	**64.9**	**291.8**	**629.0**	**214.2**	**193.7**
Other income	11.9	8.1	46.6	25.3	19.2	31.7
Interest	23.7	22.4	6.0	46.3	44.5	4.2
Depreciation	54.7	52.1	5.0	109.1	103.1	5.9
PBT	**187.9**	**-1.5**		**498.9**	**85.9**	**480.9**
Tax	60.5	-1.5		160.7	25.8	523.0
PAT	**127.4**	**0.1**	**159150.0**	**338.2**	**60.1**	**462.8**
Margins						
OPM's	25.3	10.2	15.1	28.8	14.8	0.3
PBT	18.5	-0.2	18.7	22.6	5.8	12.9
PAT	12.5	0.0	12.5	15.3	4.1	8.4

As mentioned earlier, UCL's Q2FY2007 results are below our expectations, primarily because of higher other expenditure on account of higher repairs and packing cost. However we are not changing our full-year earnings estimates for the company. Going forward, UCL should benefit from firm cement prices across the country as well as higher volumes owing to rising capacity utilisation and improving cost efficiency, as it commissions its captive power plants. At the current market price of Rs886, the stock is discounting its FY2008E earnings by 14.5x and its FY2008E EBITDA by 7.9x. On an enterprise value (EV)/tonne basis, the stock is trading at USD158 which is a huge 30% discount to its peers. We maintain our positive view on the cement sector with UCL as one of our top picks. We maintain Buy on UCL with a price target of Rs1,000.

Higher volumes and realisations bolster revenues by 58%

UCL's cement volumes registered a healthy growth of 17% year on year (yoy). Its capacity utilisation level stood at 84% as against 74% in the same quarter last year. A tight demand-supply scenario in the country, as reflected in the ruling cement prices (currently hovering around Rs200 per bag against Rs160 per bag last year), led to a 35% jump in the realisations. A cumulative effect of both these factors led to a healthy jump of 58% in the revenues to Rs1,005 crore.

Higher repair and packing cost restricts operating profit growth

Though the operating profit has grown by a staggering 292% yoy to Rs254.7 crore, the same is below our expectations. The total operating cost per tonne rose by 12.5% to Rs2,038 owing to a 17% rise in the power & fuel cost (mainly on account of an increase in the shipping freight for imported coal) and a 29.71% rise in the other expenditure. During the quarter UCL's jetty situated at its Gujarat plant was non-operational for about 15 days. Hence the company not only lost some export volumes but also had to incur an additional expense of Rs15-20 crore on the repairs of its jetty. Also the packing cost has gone up by Rs10 crore. This in turn increased the other expenditure per tonne by 30% yoy. Had these costs not been there, the company would have easily met our estimates.

Per tonne analysis

Rs per tonne	Q2FY07	Q2FY06	% yoy chg
Raw material consumed	229	177	29.5
Stock adjustment	-3	-75	-96.0
Purchase of finished goods	66	282	-76.7
Employee expenses	80	60	32.9
Power, oil & fuel	675	576	17.2
Freight	560	458	22.3
Other expenses	431	332	29.7
Total cost per tonne	2038	1811	12.5
Realisation per tonne	2729	2018	35.3
EBIDTA Per tonne	691	206	234.8

Net profit registers a quantum jump

Last year floods in Gujarat during the monsoon season had affected the company's operations at the Kovaya plant. This had affected the volumes, leading to a muted revenue growth. As a result of this and a lower EBITDA margin of 10.4%, a higher interest cost and a higher depreciation cost, the bottom line saw a negligible growth of Rs10 lakh. But this year, backed by a healthy growth in the cement volumes and realisations, and flat interest cost and depreciation charge, the bottom line jumped to Rs127 crore. However the net profit is still below our expectations of Rs144 crore.

Capex plans on track, Rs2,700 crore to be spent over next two years

Even though UCL has reported an EBIDTA per tonne of cement of Rs691, its power & fuel cost at Rs675 per tonne is among the highest in the industry. This is primarily because UCL still has to rely on grid power and diesel generator sets for energy. In order to address the issue of rising energy cost, UCL has earmarked a capital expenditure (capex) of around Rs1,424 crore to be spent over the next two to three years on modernisation of its cement plants. This includes Rs844 crore towards the installation of captive power plants at the Gujarat and Chhatisgarh units. Further to meet the growing demand for cement and to maintain its share in the southern market, UCL has approved a capex of Rs1,274 crore to expand the cement capacity of its Andhra Pradesh plant by 4 million tonne per annum and set up a captive power plant of 46 megawatt capacity. The total capex of almost Rs2,700 crore will be spent over the next two years.

Maintain earnings estimates and recommendation

As mentioned earlier, UCL's Q2FY2007 results are below our expectations, primarily because of higher other expenditure on account of higher repairs and packing cost. However we are not changing our full-year earnings estimates for the company. Going forward, UCL should benefit from firm cement prices across the country as well as higher volumes owing to rising capacity utilisation and improving cost efficiency, as it commissions its captive power plants. At the current market price of Rs886, the stock is discounting its FY2008E earnings by 14.5x and its FY2008E EBITDA by 7.9x. On an enterprise value (EV)/tonne basis, the stock is trading at USD158 which is a huge 30% discount to its peers. We maintain our positive view on the cement sector with UCL as one of our top picks. We maintain Buy on UCL with a price target of Rs1,000.

Key financials

Year ended 31 Mar	2004	2005	2006	2007E	2008E
Net profit (Rs cr)	38.8	79.7	229.8	668.3	759.4
% y-o-y growth	-	*105.0*	*188.0*	*191.0*	*14.0*
Shares in issue (cr)	12.5	12.4	12.4	12.4	12.4
EPS (Rs)	3.1	6.4	18.5	53.7	61.0
PER (x)	285.0	138.3	48.0	16.5	14.5
P/BV (Rs)	10.3	10.3	10.6	6.7	4.8
EV/EBIDTA (x)	39.8	35.6	22.4	8.5	7.9
RoCE (%)	6.0	5.7	14.7	39.0	33.5
RoNW (%)	3.6	7.5	22.1	40.8	32.7

Tata Consultancy Services

Evergreen

Stock Update

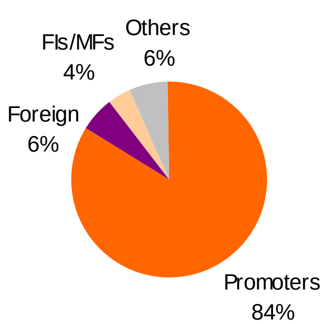
Margins firm up

Buy; CMP: Rs1,130

Company details

Price target:	Rs1,325
Market cap:	Rs110,582 cr
52 week high/low:	Rs1,148/675
NSE volume: (No of shares)	5.5 lakh
BSE code:	532540
NSE code:	TCS
Sharekhan code:	TCSCONS
Free float: (No of shares)	16.0 cr

Shareholding pattern



Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	10.8	18.5	23.5	55.0
Relative to Sensex	3.4	0.7	7.7	0.5

Result highlights

- For Q2FY2007 Tata Consultancy Services (TCS) has reported a growth of 8.2% quarter on quarter (qoq) and of 42% year on year (yoy) in its consolidated revenues to Rs4,482.2 crore. The sequential revenue growth was largely driven by a 10.8% quarter-on-quarter (q-o-q) growth in the international business with the domestic revenues declining by 14.3% on a sequential basis. The international business witnessed a strong volume growth of 11.33% sequentially.
- The earnings before interest and tax (EBIT) margins improved sharply by 294 basis points to 25.3% on a sequential basis. Apart from the impact of lower visa cost, the margins were boosted by an offshore shift (67 basis points), gains from foreign exchange (forex) movement (50 basis points) and an overall improvement in the employee productivity (driven by better realisations and operational efficiencies). The EBIT margins were also positively impacted by the write back of Rs46.8 crore worth of provisions (made for the provident fund earlier) and lower provisioning for bad debts during the last quarter. The operating profit grew by 21.4% qoq to Rs1,229.4 crore.
- Consequently, despite the sharp decline in the other income to Rs7.7 crore (down from Rs66.8 crore reported in Q1), the consolidated earnings grew by 15% qoq and by 43.7% yoy to Rs991.5 crore (higher than the consensus estimate of around Rs835 crore).
- In terms of outlook, the company does not provide any specific growth guidance. However, the management reiterated that the demand environment is quite

Result table (consolidated US GAAP) Rs (cr)

Particulars	Q2FY07	Q1FY07	Q2FY06	% qoq chg	% yoy chg
Revenue	4,482.2	4,144.3	3,156.7	8.2	42.0
Development cost	2,388.0	2,298.0	1,684.0	3.9	41.8
Gross profit	2,094.2	1,846.3	1,472.7	13.4	42.2
SG&A expenses	864.8	833.6	593.7	3.7	45.7
Operating profit	1,229.4	1,012.8	879.0	21.4	39.9
Depreciation	95.8	86.3	62.5	11.0	53.2
EBIT	1,133.6	926.5	816.5	22.4	38.8
Other income	7.7	66.8	25.2	(88.4)	(69.3)
Profit before tax	1,141.4	993.2	841.7	14.9	35.6
Tax	144.7	123.8	146.9	16.9	(1.5)
PAT	996.7	869.5	694.9	14.6	43.4
Affiliates earnings	0.8	1.6	(0.5)	(50.4)	(242.6)
Minority interest	5.9	8.5	4.3	(29.9)	37.1
RPAT	**991.5**	**862.6**	**690.0**	**15.0**	**43.7**
Equity capital	48.9	48.9	48.9		
EPS (Rs)	20.3	17.6	14.1		
Margins (%)					
GPM	46.7	44.6	46.7		
OPM	27.4	24.4	27.8		
EBIT	25.3	22.4	25.9		
NPM	22.1	20.5	21.7		

favourable. It is also confident of maintaining the EBIT margins at around the 25.8% level (on the full year basis) in line with FY2006. This implies a significant improvement in the EBIT margins in the second half as the margins stood at 23.9% during the first half ended September 2006.

- The company has announced an interim dividend of Rs3 per share.
- At the current market price the stock trades at 27.8x FY2007 and 22.1x FY2008 revised earning estimates. We maintain our Buy call on the stock with a price target of Rs1,325.

Robust growth in international business

The sequential growth of 10.8% in the international business was contributed by the volume growth of 11.33%, gains of 1.89% from the forex movement and the positive impact of 1.17% from the improvement in the billing rates. On the other hand, the shift towards offshore negatively impacted the international revenues by 3.59% on a sequential basis.

In terms of specific growth drivers, the company reported an impressive growth in the revenues from the Americas, which grew by 15.9% sequentially. The key industry verticals of banking, financial services and insurance (BSFI) and energy & utilities are also showing significant traction with a double-digit sequential growth in the revenues. In terms of service offerings, business intelligence (up 19.3% qoq), infrastructure services (up 22.6% qoq) and enterprise solutions (up 17.2% qoq) boosted the overall growth in the revenues.

Margins recover smartly

The 294-basis-point improvement in the EBIT margins was much higher than expectations. The margins were boosted by an offshore shift (67 basis points), gains from the forex movement (50 basis points) and overall productivity (driven by better realisations and operational efficiencies). The EBIT margins were also positively impacted by the write back of Rs46.8 crore worth of provisions (made for the provident fund) and lower provisioning for bad debts during the last quarter.

Other income declines

The other income declined sharply to Rs7.7 crore as against the healthy other income of Rs66.7 crore in Q1FY2007. That is because of the 0.2% appreciation in the rupee against the dollar. Thus, the company did not accrue any positive impact of the foreign exchange fluctuations in its other income component during the last quarter.

Robust demand environment but margins under pressure

In terms of outlook, the company does not provide any specific growth guidance. However, the management reiterated that the demand environment is quite favourable. The management indicated that there has been a considerable increase in the number of deals available and the average size of an order.

In term of profitability, the management is confident of maintaining the full year FY2007 margins at around the 25.8% level reported in FY2006. It indicated that the pricing environment has improved considerably and the new contracts have been signed at 5-10% higher realisations. Moreover, the company has also been able to extract 3-5% increase in the billing rates from the existing clients. Moreover, the management expects to further improve offshore contribution and achieve better-cost leverage in the coming quarters.

Given the robust growth in the volumes and the expectation of further improvement in the margins, we are upgrading our earning estimates for FY2007 and FY2008 by 3.5% and 3.4% respectively.

Other highlights

The sequential revenue growth of 8.8% in its top five clients was largely driven by the 32.5% q-o-q growth in the revenues from its largest client. This implies that the other four clients in the top five bracket cumulatively grew at a tepid rate of 1.3% on a sequential basis. On the brighter side, the clients with over $50 million revenue run rate increased to 15 from 10 in Q1.

It added 6,663 employees during the quarter, taking the total staff strength to 78,028. The attrition rate remained flat at 10.6%, which is better than that of most of its peers.

Valuation

At the current market price the stock trades at 27.8.4x FY2007 and 22.1x FY2008 revised earning estimates. We maintain our Buy call on the stock with a price target of Rs1,325 (26x FY2008 estimated earning).

Key financials

Particulars	FY2005	FY2006	FY2007E	FY2008E
Net revenue (Rs cr)	9727.0	13245.0	18344.0	23803.0
Net profit (Rs cr)	2356.0	2911.0	3977.0	4993.0
Number of shares (cr)	96.0	97.9	97.9	97.9
EPS(Rs)	24.5	29.7	40.6	51.0
% y-o-y chg		*21.3*	*36.6*	*25.5*
PER	46.1	38.0	27.8	22.1
OPM (%)	27.7	25.7	24.9	24.2
RoNW	58.2	49.4	44.3	38.5
RoCE	51.4	40.1	38.7	35.6

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
- Associated Cement Companies
- 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 Auto
- 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
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