



Another chance to buy

They say that God always offers another chance. And they are so right. The fall of over 650 points in the benchmark index, the Sensex, seems to be God's way of offering one more chance to all those who missed the bus the last time. If you too have been feeling left out while your brother-in-law has been making a killing in the market, don't worry. Collect all your investible cash and get ready to go shopping.

Surprised that we are talking of entering the market when the same is under attack from bears? Don't be. Agreed that the market has lost over 650 points in just four trading sessions but we view this fall as a correction and remain bullish on the market in the long term. In fact we view this correction as a good opportunity to buy those stocks that are both good investment ideas and attractively valued as compared with their peers.

A similar opportunity had presented itself last October when the market had witnessed a correction of over 1,000 points. In response to that huge correction, on October 24, 2005 we had come out with a list of ten stocks that had also corrected and were quoting at attractive valuations. These stocks were recommended as a good buy at that time. If by following our advice you had entered the market when the others were exiting, you could have not only made some good money but also outsmarted the market.

Top ten value pick

Company name	CMP (Rs)	PER			RoE (%)			Price target	% upside
		FY05	FY06	FY07E	FY05	FY06	FY07E		
Bharat Heavy Electricals	2,183.8	56.1	34.7	23.2	15.5	21.4	26.2	2,650.0	21.0
Hindustan Lever	263.5	48.8	43.9	34.2	56.5	56.9	58.6	300.0	14.0
ICICI Bank	615.0	22.6	21.6	15.6	19.0	17.0	14.0	750.0	22.0
ITC	191.8	38.9	30.4	27.0	26.3	25.4	24.6	220.0	15.0
M&M	656.1	30.5	21.9	20.4	28.0	21.0	29.2	700.0	7.0
Maruti Udyog	887.1	33.6	21.6	17.7	20.4	23.4	21.7	1050.0	18.0
Orchid Chemicals	269.0	84.1	22.6	13.2	6.6	8.1	12.9	460.0	71.0
TVS Motors	144.0	25.3	29.4	17.6	20.0	15.3	21.1	210.0	46.0
Esab India	411.0	31.1	15.9	13.8	51.0	49.0	56.0	575.0	40.0
Selan Exploration Technology	87.0	96.6	18.9	15.2	5.1	26.2	16.6	94.0	8.0

Note: The list should not be confused with the "Sharekhan Top Picks" dated May 05, 2006. The stocks listed in "Sharekhan Top Picks" still remain a Buy.

Performance of October's list (Diwali shopping list)

	Price as on 24-Oct-05	Returns (%)		
		30-day	180-day	Till date*
Concor	1,307.8	0.1	16.5	31.8
Crompton Greaves	624.9	7.0	70.4	81.9
ITC	117.1	10.3	73.4	63.5
M&M	359.4	19.6	79.6	85.9
Orient Paper	166.8	16.4	141.7	146.2
Sanghvi Movers	326.8	22.5	158.8	160.9
Satyam	598.6	8.0	29.2	25.3
SKF India	228.0	3.2	38.4	48.9
TIL	143.9	0.3	76.1	60.4
TV18	344.7	16.9	87.1	96.2
UltraTech Cement	413.0	11.4	101.1	65.5
UTI Bank	229.3	8.4	49.2	51.0
Average return		10.3	76.8	76.5
Return on Sensex	7,920.8	9.1	50.4	49.3

*Closing price on May 15, 2006

But no use crying over spilt milk. Instead let us focus on the opportunity that is knocking at our door. Several of our Stocks Ideas have corrected significantly in the past few sessions and are sporting attractive valuations as a result. These are fundamentally sound companies and we remain bullish on them. We believe these are a good buy at the current levels and have listed them below for your benefit. Go ahead and take your pick. Remember here is your chance to match your brother-in-law's wealth.

Bharat Heavy Electricals

- ♦ Bharat Heavy Electricals Ltd (BHEL), a leading supplier of power equipment, will be the prime beneficiary of a four-fold increase in the investments (Rs500,000 crore in the 11th Five-Year Plan as against Rs112,000 crore in the 9th Five-Year Plan) being made in the power sector.
- ♦ BHEL's current order book of Rs37,500 crore, ie 3.0x its FY2005 revenue, provides a high earnings visibility.
- ♦ The power ministry has proposed around five ultra mega power projects entailing a capacity addition of 20,000MW (4,000MW x 5) with the combined turnkey value of at least Rs80,000 crore.
- ♦ BHEL's recent technology transfer agreement with Alstom for design and manufacture of large-sized (500MW+) super-critical boilers will enable it to bid for the ultra mega power projects. We expect BHEL to bag a fair share of this huge Rs80,000-crore potential investment which in turn will maintain the growth momentum in the company's order book.
- ♦ The stock trades at a PER of 23.2x its FY2007E earnings. BHEL's valuation looks attractive as compared with that of its peers, such as Siemens, ABB and Larsen and Toubro.

Hindustan Lever

- ♦ Growth in various fast moving consumer good (FMCG) segments is recovering due to changing demographic trends, eg growing urbanisation and higher incomes, and a strong growth in rural economy.
- ♦ HLL has regained its double-digit top line growth on the back of this surge in FMCG demand and its investment in advertising and promotional activities.
- ♦ We expect its operating profit margin to expand significantly as the product mix changes in favour of high-margin personal care products and it starts making profit in processed foods and ice-cream businesses on the back of volume growth. The reduction in the customs duty on raw material and packaging material would also reduce its costs.
- ♦ We expect HLL to regain its premium to the market that had narrowed down over the last couple of years due to its lacklustre performance.

ICICI Bank

- ♦ ICICI Bank is India's second-largest bank. Its strong positioning in the retail advance segment gives it the dual advantages of a healthy growth in both loans and fee income.
- ♦ A key concern regarding the non-performing assets (NPAs) is now receding with the bank's NPAs now below 1%.

- ♦ Various subsidiaries (life insurance, general insurance, ICICI Securities) add Rs150 to the overall valuation.
- ♦ The stock trades at a price/earnings ratio (PER) of 15.6x its FY2008E earnings and 2.0x its FY2008E book value. ICICI Bank's valuation looks attractive as compared with that of its peers, such as HDFC Bank.

ITC

- ♦ ITC is the undisputed market leader in the cigarette business in India. Over the years ITC has gained substantial pricing power in the market and has been recording a good volume growth in the business.
- ♦ ITC has diversified its revenue stream by successfully channelising the huge cash flows generated from the cigarette business into new and upcoming businesses like hotels, FMCG, paperboards and agri-marketing.
- ♦ ITC's huge investments in these businesses have now started showing up in the form of a robust growth in the revenues and profits.
- ♦ ITC's venture into agri-marketing through the e-Choupal programme is now set to replicate the urban mall mania in rural areas through the Choupal Sagar project. The Choupal Sagar project is expected to be a major driver of the company's revenue and profit over the long term.
- ♦ Given that the company's earnings are growing at a compounded annual growth rate (CAGR) of 23.4% over FY2005-07E, the stock is attractively quoting at a PER of 27.0x its FY2007E earnings.

M&M

- ♦ Mahindra and Mahindra (M&M) is the leader in the Indian tractor market. It has also carved a niche for itself in the Indian utility vehicle market with a wide product range.
- ♦ M&M's growth prospects in the tractor segment remain positive on the back of the government's focus on the rural economy and initiatives to boost agri-loans. Add to that the fact that the south-west monsoon for the last season was good. As a cumulative effect of these factors we expect M&M's tractor volumes to grow at a healthy rate of 20% in FY2006 as against the industry growth rate of 11% during the same period.
- ♦ M&M's key subsidiaries, Mahindra-British Telecom (in which it holds a 57% stake) and M&M Financial Services (a holding of 97%), are doing extremely well. Apart from that M&M holds a majority stake in the real estate company, Mahindra Gesco Developers, which is the leader in the housing and commercial construction sectors.
- ♦ M&M has undertaken an auto component business initiative under Mahindra Systems and Automotive Technology (MSAT). MSAT will provide end-to-end solutions for designing, engineering and manufacturing auto components. We expect MSAT to be a big positive for the company.

- ♦ The stock is discounting its FY2007E earnings per share (EPS) by 20.4x. We believe that the stock's current valuations are very attractive considering the fact that the significant growth coming from the subsidiaries will also trigger a re-rating in the stock going forward.

Maruti Udyog

- ♦ Maruti Udyog Ltd (MUL), India's largest small car manufacturer, would be the biggest beneficiary of the reduction in the excise duty on small cars in Union Budget 2006-07. The lower duty is expected to boost the company's volume significantly.
- ♦ Increased cost-cutting measures, improved productivity and increased indigenisation would help to improve the margins.
- ♦ The merger of Maruti Suzuki Automobiles India with MUL will add value for the shareholders and eliminate all the potential issues relating to inter-company transactions.
- ♦ At the current market price of Rs887, the stock is quoting at 17.7x its FY2007E.

Orchid Chemicals

- ♦ Orchid Chemicals and Pharmaceuticals (Orchid), historically a manufacturer of bulk drugs, has now entered the high-revenue, high-margin business of finished dosages in the USA. This transition from a bulk drug manufacturer to an integrated manufacturer of formulations will drive the earnings and also result in higher valuations.
- ♦ Orchid has set up marketing alliances with US companies for the sale of 20 lifestyle drugs representing a market size of US\$20 billion. Thus the lifestyle segment in the regulated markets provides a huge opportunity for the company from FY2008 onwards.
- ♦ Orchid has repaid Rs265 crore of its high-cost debt. Going ahead, we expect the interest savings to add to the bottom line directly from FY2007 onwards. We expect the profit after tax to increase 4.5x over FY2005-07, at a CAGR of over 110%.
- ♦ Orchid is trading at 13.7x its FY2007E EPS and is at a deep discount to its peers. Considering the robust generic opportunity available to Orchid and its strong growth prospects, we are positive on the stock.

TVS Motors

- ♦ TVS Motor Company is a perfect play on the booming two-wheeler industry. The company now has a strong presence in all the product categories: motorcycles, scooters and mopeds. The proposed foray into the three-wheeler market should further fuel the company's growth.
- ♦ Its recently launched motorcycle, Apache, has won huge accolades and is expected to capture a 13% share of the premium segment in FY2007.
- ♦ With rising volumes, the implementation of various cost-cutting measures and its entry into high-end products, the company's margins are set to improve.
- ♦ The exports of the company are expected to rise with the setting up of a new plant in Indonesia.
- ♦ At the current market price of Rs144 the stock discounts its FY2007E earnings by 17.6x.

Esab India

- ♦ ESAB India, the country largest manufacturer of welding electrodes and machines, will be the primary beneficiary of the mammoth investments lined up in sectors like ports, automobile and construction.
- ♦ The company has consciously adopted the strategy of sacrificing low-margin, high-volume products for capturing the market for quality and high-margin products.
- ♦ With the company's earnings growing at a CAGR of 22%, the stock is trading at attractive valuations of 13.8x its CY2006 earnings.

Selan Exploration Technology

- ♦ Selan Exploration Technology has production sharing agreement for five oil & gas fields situated in the oil rich Cambay Basin.
- ♦ It produces around 70,000 barrel of crude oil annually and is one of the key beneficiaries of the firm crude oil prices globally.
- ♦ In addition to higher realisations, the growth will be driven by the initiatives taken to ramp up the production volumes through the development of its oil assets.
- ♦ The efforts undertaken to develop new oil wells in its Bakrol oil field are likely to result in over 250% increase in its production volumes over the next 24 months.
- ♦ At the current price the stock trades at 15.2x FY2007 estimated earnings and \$1.1 per barrel of oil & oil equivalent.

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

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