Index

Take Five

Scrip	Reco Date	Reco Price	CMP	Target
Aban Loyd	03-Mar-05	330	**989**	1,760
Bajaj Auto	15-Nov-05	1,873	**2,688**	3,500
BHEL	11-Nov-05	1,203	**1,881**	2,650
Infosys	30-Dec-03	1,378	**2,994**	3,324
TV18	23-May-05	280	**511**	704

Sharekhan Ltd
A-206, Phoenix House, 2nd Floor, Senapati Bapat Marg, Lower Parel, Mumbai - 400013, India.

Pulse Track

Monsoon back to work

- The monsoon is back to work after taking a long break of twelve days.
- The monsoon will reach eastern Madhya Pradesh, Chattisgarh, Bihar and eastern Uttar Pradesh, and intensify over the regions already covered over the next five days.
- Further, an expected formation of a "low" over the Bay of Bengal will intensify the monsoon activity over the mainland.
- The sowing of the *kharif* crops is not yet affected (barring cases like oil seeds and cereals), thanks to higher water reservoir levels and an early visit by the monsoon to some places.
- The actual rainfall from June 1 to June 21, 2006 stands at 71.9mm, 24% below the normal rainfall. However, it is still early days and a revival of the monsoon (which is on the cards) could change the picture.

Monsoon in revival mood

The monsoon is back to work after taking a long break of twelve days. Its revival began on June 21 when it revisited Kerala. Since then it has advanced to cover most of the peninsula, Andhra Pradesh and Maharashtra. According to the National Centre for Medium Range Weather Forecasting, although the monsoon pulse is weak, yet the higher moisture content will help to sustain the revival, which is expected to continue for the next five days. The monsoon will reach eastern Madhya Pradesh, Chattisgarh, Bihar and eastern Uttar Pradesh over the next five days.

Further, the weather models are predicting a formation of a "low" over the Bay of Bengal by early next week, which should intensify the monsoon over the mainland, covering central and north-western parts of the country. The "low" will be formed owing to the shifting of the north-westerly wind flows to the south.

Sowing not yet affected, crops not to be affected if the revival is sustained

The monsoon, after its early arrival last month, is running behind its schedule. However, the sowing was not affected in the areas where the monsoon was active before it took a break because of higher water content in the soil owing to the early rains. Also, the higher water reservoir levels helped continue the sowing activity. According to the Central Water Commission, the total water storage in 76 major dams was around 30.43 billion cubic metre, which was twice that of the corresponding level in the last year. These levels are also higher by a good 81% above the last ten years' average level in mid June.

Although the late arrival of the monsoon may delay the planting of oil seeds and coarse cereals that depend heavily on the monsoon, yet with the revival of the monsoon in the mainland, the crops may not get affected. Barring these crops, the sowing activity for all the other main crops like rice, sugar-cane and cotton has been satisfactory.

Actual rainfall up to June 21 is 71.9mm, 24% below normal

The cumulative rainfall from June 1 to June 21, 2006 has been 71.9mm, which is 24% below the normal rainfall of 94.9mm. The same was lower on account of a fortnight-long dry spell. Out of a total of 36 meteorological sub-divisions, 17 witnessed normal to excess rainfall and there was a deficient rainfall at another 17 sub-divisions. The cumulative rainfall up to June 14 was 54.2mm, just 3% below the normal rainfall of 55.9mm. On a corresponding basis, for 2005 the rainfall from June 1 to June 15 was 59% lower than the normal rainfall. However, the year 2005 has been hailed as a year of a good monsoon. Thus though the rainfall for the current season is below the average, these are still early days to take a call on the monsoon and a revival of the monsoon (as expected) could change the picture.

Actual rainfall in mm and its comparison

From June 1	Actual	Normal	% Departure
Upto June 21 2006	71.9	94.9	-24.0
Upto June 14, 2006	54.2	55.9	*-3.0*
Upto June 15, 2005	25.0	61.6	*-59.0*

Source: IMD

Summary of rainfall activity of 36 sub divisions

	From June 1		
	Up to June 21 2006	Up to June 14 2006	Up to June 15 2005
Excess	6	10	3
Normal	11	8	2
Deficient	17	13	10
Scanty	2	5	31
No rain	0	0	0

Source: IMD

Tata Tea

Apple Green

Stock Update

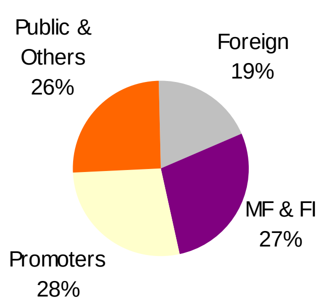
Focusing on core business

Buy; CMP: Rs755

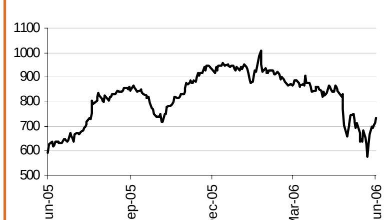
Company details

Price target:	Rs1,040
Market cap:	Rs4,122 cr
52 week high/low:	Rs1,047/560
NSE volume: (No of shares)	2.7 lakh
BSE code:	500800
NSE code:	TATATEA
Sharekhan code:	TATATEA
Free float: (No of shares)	4.0 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	9.2	-17.6	-23.0	24.0
Relative to Sensex	10.9	-13.5	-30.2	-15.2

Tata Tea to sell NIPO

Tata Tea (TTL) is reportedly in talks with the potential buyers for the sale of its North India Plantation Operation (NIPO). NIPO has 24 tea estates of which four are located in northern West Bengal and 20 are located in Assam.

We believe that this move is in line with Tata Tea's overall strategy to focus on packaged and specialty tea and is likely to result in substantial cost savings for the company.

Sale likely to result in substantial savings in cost

We expect the proposed move to result in substantial savings in cost for TTL, similar to what had happened when TTL had sold its 17 tea estates in the South Indian Plantation Operation (SIPO) to Kanan Devan Hills Plantations Company Private Ltd, a company jointly owned by the SIPO workers and Tata Coffee Ltd (a subsidiary of TTL).

While TTL is estimated to have lost revenues of Rs50 crore on the sale of SIPO, it has helped TTL to cut down its wage cost by nearly Rs70-80 crore, resulting in net savings of Rs20-30 crore.

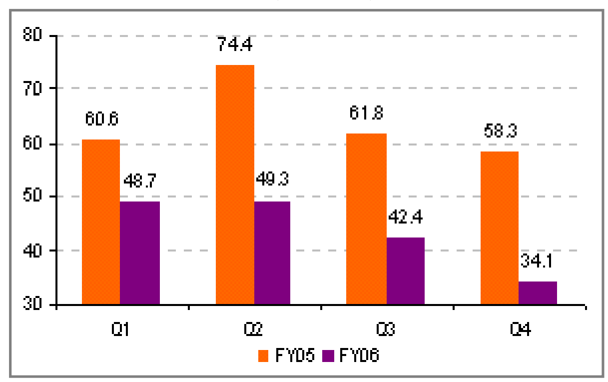
Sale to differ slightly from SIPO sale

TTL has indicated that the mode of the sale for NIPO will be slightly different from that of SIPO. While TTL holds 19% of the divested SIPO, TTL's stake in NIPO after its sale may remain at a higher level and the employee participation may not be as high as it was in the case of the SIPO sale. The reason for the same is that the valuations of NIPO are likely to be much higher as it holds 24 estates compared with 17 estates held by SIPO and also the productivity of NIPO is much higher than the productivity of SIPO.

Valuation and view

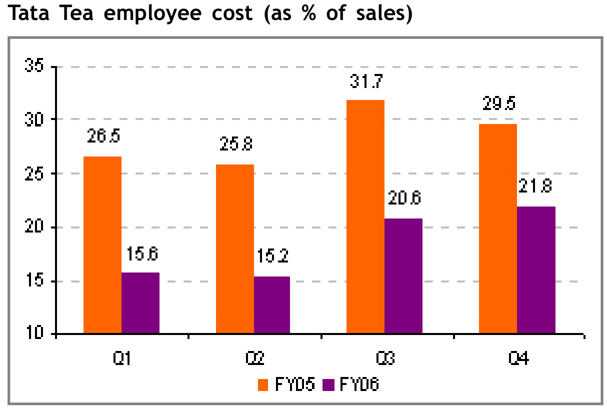
After the divestment of NIPO, TTL will be an absolute packaged tea player. With the company's aspirations and efforts towards

Tata Tea employee cost (Rs crore)



Source: Company, Sharekhan research

Tata Tea employee cost (as % of sales)



Source: Company, Sharekhan research

becoming a leading player in branded tea and expanding its footprints in specialty tea (like herbal and fruit flavoured), its valuations at 11.1x its FY2008E earnings per share and 6.7x its FY2008E enterprise value (EV)/earnings before interest, depreciation, tax and amortisation (EBIDTA) are very attractive compared to its peers in the fast moving consumer goods sector. We maintain our Buy on the stock with a price target of Rs1,040.

Valuation table

Particulars	FY2005	FY2006P	FY2007E	FY2008E
Net profit (Rs cr)	245.7	296.7	330.8	372.7
Shares in issue (cr)	5.6	5.6	5.6	5.6
EPS (Rs)	43.7	52.8	58.8	66.3
% y-o-y growth	*29.6*	*20.7*	*11.5*	*12.7*
PER (x)	16.8	13.9	12.5	11.1
Per adjusted for investments (x)	15.2	13.1	11.5	10.3
Book value (Rs)	270.2	312.5	359.9	414.8
P/BV (x)	2.7	2.4	2.0	1.8
EV/EBIDTA (x)	10.0	8.9	7.9	6.7
EV/Sales (x)	1.8	1.6	1.4	1.2
RoCE (%)	14.0	15.4	17.0	18.6
RoNW (%)	17.2	18.1	17.5	17.1

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

Ador Welding

Viewpoint

Welding gains

CMP: Rs364

We attended the annual general meeting of Ador Welding Ltd (Ador) and here are the key takeaways from the meeting.

- Helped by the pick-up in the country's infrastructure spending and industrial growth, Ador's net revenues grew by a healthy 22.2% to Rs266 crore in FY2006. The revenue growth came on the back of an 18% growth in the welding electrode business and a 45% growth in the welding equipment business.
- With a 440-basis-point improvement in the operating profit margin (OPM), the performance at the operating level was even better: the operating profit grew by an impressive 67.3% to Rs43 crore.
- The pre-exceptional net earnings grew by 51.5% to Rs35 crore as Ador maintained its debt-free status for the fourth consecutive year. At Rs40 crore the reported net profit grew by 45.4%.
- Encouraged by the continuing growth momentum in India's infrastructure spend and the growth in the industrial sector, Ador has lined up a capex programme of Rs20 crore to increase the manufacturing capacity of its Silvassa plant (which is located in a tax-free zone) and re-engineer the processes to improve efficiency.
- The company's balance sheet is in an excellent shape, with cash and cash equivalents of almost Rs38 crore on the books. Its return ratios have also improved substantially with the return on capital employed (RoCE) at 52.5% and return on equity (RoE) at 34.2%. Further the company has declared a dividend of 150% (Rs15 per share). Consequently, the stock's dividend yield works out to 4.1%.
- The management, which has experience of more than five decades in the welding industry, is confident that business conditions are improving and has a positive outlook on the welding business. It expects the company's top line to grow by 30% during FY2007.
- Our back-of-the-envelope calculations (using the guidance given by the management) show that the company would report earnings of Rs35 per share in FY2007. At the current market price of Rs364, the stock is trading at 10.1x its FY2007 earnings, which is slightly lower than that of its peer ESAB India, which is trading at 12x its CY2006 earnings. However ESAB India has an edge over Ador, as it is the market leader with better pricing power and access to the technologies of its parent, ESAB Worldwide.

Background

Promoted by JB Advani & Co, Ador offers a welding package, which includes a wide variety of welding electrodes, fluxes, flux-cored wires and welding and cutting equipment. Ador operates in two segments: consumables (75% of revenue and 78% of earnings before interest and tax or EBIT) and equipment & project engineering (25% of revenue and 22% of EBIT). The consumable division manufactures welding electrodes, wires and fluxes; the equipment division manufactures welding and cutting equipment. Ador also has a project engineering division (PED), which is a sub-division of the equipment division and manufactures flares, cremators and incinerators that are basically environmental control equipment.

Key positives

Impressive financial performance continues—revenue grows at 20% CAGR

Aided by the pick-up in India's infrastructure spending and industrial growth, Ador's net revenues grew by a healthy 22.2% to Rs266 crore in FY2006 driven by an 18% growth in the welding electrode business and a 45% growth in the welding equipment business. The company's exports grew by 25%, posting sales of around Rs40 crore. Over the last four years, the company's revenues have grown at an impressive compounded annual growth rate (CAGR) of 20%.

32% CAGR in operating profit

Along with the remarkable top line growth, the company was able to improve its OPM from 14.5% to 18.8% year on year (yoy). This too was very impressive, given the volatility in the prices of the key inputs seen last year. Consequently, Ador's operating profit grew by a good 67.3% to Rs43 crore. In the last four years, the operating profit has grown at a CAGR of 32%.

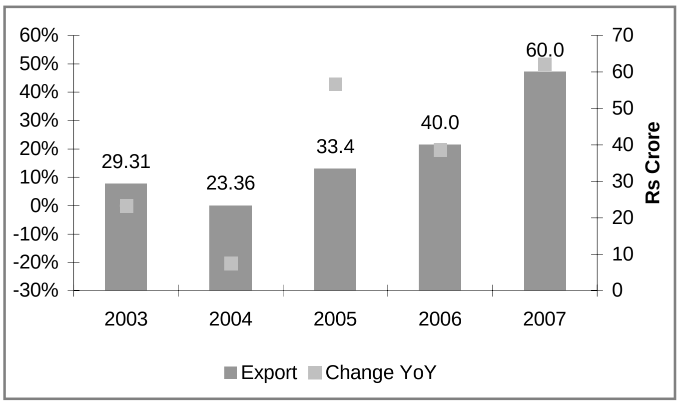
...and 50% CAGR in net earnings

With the company maintaining its debt-free status for the fourth successive year, the benefit at the operating level trickled down to the net level, improving the net margin from 11.9% to 17.6% yoy. The pre-exceptional net earnings grew by 51.5% to Rs35 crore. In the last four years, the pre-exceptional net earnings have grown at a CAGR of 50%. At Rs40 crore the reported net profit grew by 45.4%.

Improving focus on diversifying business geography

Ador has been focused on diversifying its business geography and has established an office at the Sharjah Airport International Free Zone in Sharjah, the UAE. The office will service the customers from all over the Middle East. During FY2006 the export business of the company grew by a decent 25% to Rs40 crore. The company remains bullish on its export business and expects the same to grow by 50% to Rs60 crore in FY2007.

Strong exports growth



New product launches to buoy revenues

In an industry where technological development is the key to gaining and maintaining market share, Ador has managed to expand its range of customer specific welding solutions (like specialised welding solution for the Navy) and introduce new product lines. All this has been possible because of its two technology development centres located at Bhandup and Pune. Last year the company came out with new products in all its segments. Of these the products launched by the PED, such as waste management systems and effluent treatment plants, appears to be promising. Further the company has launched power generator sets (gensets) in the 15-125KVA range. The gensets have received an encouraging response from the market and the company expects to clock sales of Rs5-8 crore from the gensets this year.

Buoyant demand from the user industry to continue

With the user industries witnessing an exceptional growth, the welding industry is firing on all cylinders. The management expects the growth momentum to continue on two counts as mentioned below.

Engineering & construction activity on the rise

Electrodes and welding/cutting equipment are essential for fabrication works in the engineering and construction (E&C) sector, which is having a dream run with the order book of the E&C players growing by the day. The huge order backlogs of the E&C companies are expected to maintain the growth momentum for the welding industry.

Investment in steel and oil and gas

As in April 2005, projects entailing investments of Rs46,339 crore were under implementation in the steel and oil and gas sectors. Investments to the tune of another Rs297,119 crore have been proposed in these sectors. This huge investment drive in a core sector of the Indian economy will maintain the growth momentum in the businesses of welding equipment and consumables.

User industries to shift towards organised sector

Around 60-65% of the total welding market comprises manual welding with automatic and semi-automatic welding making for the balance. Increasing competitiveness among the user industries, such as engineering, steel and construction, automobile and consumer durables, is bringing into focus the need for highly efficient processes. This need of the industry to improve its efficiency and quality is resulting in a gradual shift from the manual processes to semi-automatic processes. This shift, in turn, will trigger a shift towards the organised sector and being the leading player in the organised sector Ador will be the prime beneficiary of this change.

Management to expand capacities to cash in on rising demand

Ador incurred a cost of Rs19 crore in FY2006 to install a submerged arc wire plant in Chennai and expand its wire product plant at Raipur. Encouraged by the sustained growth momentum in the user industries, Ador has lined up a capex programme of Rs20 crore for FY2007 as well. As part of the capex plan, it would expand the manufacturing capacity of its Silvassa plant (located in a tax-free zone) and re-engineer the manufacturing processes to improve efficiency. Also a higher proportion of sales from the Silvassa unit will bring down Ador's tax burden. The entire capex will be funded through internal accruals of the company.

The company also intends to shift the operations of its Ahmednagar facility to its Chennai plant, in order to achieve economies of scale at the Chennai plant. This shall help Ador in two ways. First, the overheads incurred on the Ahmednagar facility will be saved and second, the idle land at the Ahmednagar plant site could be disposed of to realise additional funds.

Move to VAT to remove the price differential between organised and unorganised sectors

The organised players will enjoy a greater market share in the value-added tax (VAT) regime because they will have to pay lesser tax now as they will get credit for the tax they pay on their raw material. Hence the price differential between the products offered by them and those offered by the unorganised players will disappear. This will make the unorganised players uncompetitive and cause them to lose their share to the organised counterparts. Being the market leader in the organised sector, Ador will be the prime beneficiary of the VAT system in the welding business.

Management expects top line to grow by 30% in FY2007

Welding products find application in diverse sectors like ports, airports, shipbuilding, oil and gas pipelines, automobiles and consumer durables. Considering the mammoth size of the capex lined up in these sectors, we believe that the growth prospects for Ador remain very good. Again, since the projects in these sectors are spread over a period of five to six years, there is a good amount of visibility for the company's future earnings. With rich experience of more than five decades in the welding industry, Ador is expecting to make the most of the benefits coming its way. The management expects the company's top line to grow by 30% this year to Rs345 crore. The growth shall come on the back of a 24% growth in its mainstay, ie the welding consumable business, and a higher growth of 40% in the revenues of the equipment division and the PED.

Strong balance sheet and handsome dividend yield of 4.1%

The company's balance sheet is in an excellent shape, with zero debt and cash and cash equivalents of almost Rs38 crore on its books. Its return ratios have also improved substantially with the RoCE at 52.5% as against 38.8% in the last year. The RoE too has improved from 26.8% in the last year to 34.2%. Further the company has an excellent track-record of giving handsome dividends. For example, during FY2005 it gave a dividend of 100% (Rs10 per share) and in FY2006 it declared a dividend of 150% (Rs15per share). Consequently, the dividend yield of the stock works out to a handsome 4.1%.

Key concerns

Considering the proposed capex in the construction and infrastructure space as well as the continued growth in the industrial sector, the company is optimistic about its own growth prospects. However the rising interest rates and the resultant slowdown in the manufacturing and/or infrastructure sector could affect the demand for welding products, thereby hampering the growth of the company. The other concern pertains to the increasing input prices, which could dent the company's OPM.

Valuations

Our back-of-the-envelope calculations (using the guidance given by the management) show that the company could report earnings of Rs35 per share in FY2007. At the current market price of Rs364, the stock is trading at 10.1x its FY2007 earnings, which is slightly lower than that of its peer ESAB India, which is trading at 12x its CY2006 earnings. However ESAB India has an edge over Ador, as it is the market leader with better pricing power and access to the technologies of its parent, ESAB Worldwide.

	Ador Welding		ESAB India	
	FY2006	FY2007	CY2005	CY2006
Sales (Rs crore)	265.9	345.9	237.6	267.1
EBIDTA (Rs crore)	43.2	65.8	53.2	73.7
EBIDTA (%)	16.2	19.0	22.4	27.6
EPS (Rs)	25.9	36.0	25.8	29.7
PER	12.2	10.0	15.9	13.8
EV/EBIDTA	10.5	6.3	12.0	8.0

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
Bharat Bijlee
Bharat Heavy Electricals
Corporation Bank
Crompton Greaves
Godrej Consumer Products
Elder Pharmaceuticals
Grasim Industries
Hindustan Lever
Hyderabad Industries
ICICI Bank
Indian Hotel Company
ITC
Mahindra & Mahindra
Marico Industries
Maruti Udyog
MRO-TEK
Lupin
Nicholas Piramal India
Omax Auto
Ranbaxy Laboratories
Satyam Computer Services
Sintex Industries
SKF India
State Bank of India
Sundaram Clayton
Tata Motors
Tata Tea
Unichem Laboratories
Wipro

Cannonball

Cipla
Gateway Distriparks
International Combustion (India)
JK Cements
Madras Cement
Shree Cement
Transport Corporation of India

Emerging Star

3i Infotech
Aarvee Denim and Exports
Aban Loyd Chiles Offshore
Alok Industries
Alphageo India
Cadila Healthcare
KSB Pumps
Marksans Pharma
Navneet Publications (India)
New Delhi Television
Orchid Chemicals & Pharmaceuticals
ORG Informatics
Solectron Centum Electronics
Television Eighteen India
Thermax
Tube Investments of India
TVS Motor Company
UTI Bank
Welspun Gujarat Stahl Rohren
Welspun India

Ugly Duckling

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

Vulture's Pick

Esab India
Orient Paper and Industries
WS Industries India

Home

Disclaimer

"This document has been prepared by Sharekhan Ltd.(SHAREKHAN) This Document is subject to changes without prior notice and is intended only for the person or entity to which it is addressed to and may contain confidential and/or privileged material and is not for any type of circulation. Any review, retransmission, or any other use is prohibited. Kindly note that this document does not constitute an offer or solicitation for the purchase or sale of any financial instrument or as an official confirmation of any transaction.

Though disseminated to all the customers simultaneously, not all customers may receive this report at the same time. SHAREKHAN will not treat recipients as customers by virtue of their receiving this report.

The information contained herein is from publicly available data or other sources believed to be reliable. While we would endeavour to update the information herein on reasonable basis, SHAREKHAN, its subsidiaries and associated companies, their directors and employees ("SHAREKHAN and affiliates") are under no obligation to update or keep the information current. Also, there may be regulatory, compliance, or other reasons that may prevent SHAREKHAN and affiliates from doing so. We do not represent that information contained herein is accurate or complete and it should not be relied upon as such. This document is prepared for assistance only and is not intended to be and must not alone betaken as the basis for an investment decision. The user assumes the entire risk of any use made of this information. Each recipient of this document should make such investigations as it deems necessary to arrive at an independent evaluation of an investment in the securities of companies referred to in this document (including the merits and risks involved), and should consult its own advisors to determine the merits and risks of such an investment. The investment discussed or views expressed may not be suitable for all investors. We do not undertake to advise you as to any change of our views. Affiliates of Sharekhan may have issued other reports that are inconsistent with and reach different conclusion from the information presented in this report.

This report is not directed or intended for distribution to, or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject SHAREKHAN and affiliates to any registration or licensing requirement within such jurisdiction. The securities described herein may or may not be eligible for sale in all jurisdictions or to certain category of investors. Persons in whose possession this document may come are required to inform themselves of and to observe such restriction.

SHAREKHAN & affiliates may have used the information set forth herein before publication and may have positions in, may from time to time purchase or sell or may be materially interested in any of the securities mentioned or related securities. SHAREKHAN may from time to time solicit from, or perform investment banking, or other services for, any company mentioned herein. Without limiting any of the foregoing, in no event shall SHAREKHAN, any of its affiliates or any third party involved in, or related to, computing or compiling the information have any liability for any damages of any kind. Any comments or statements made herein are those of the analyst and do not necessarily reflect those of SHAREKHAN."