Sharekhan top picks

In the January 2008 issue, we had recommended the best 12 of our Stock Ideas as Sharekhan Top Picks. As on January 31, 2008 the basket of stocks has declined by 9.7% in the steep fall during the month, which is relatively better than the decline of 13% in Sensex and 16.3% in S&P CNX Nifty.

We have made one change in the portfolio. We have replaced Maruti Suzuki with Ranbaxy Labs. The volume growth in Maruti is expected to be subdued in the intermediate term due to high base effect. On the other hand, Ranbaxy has triggers in terms of hiving of R&D into a separate entity and its valuations are also attractive.

Name	CMP* (Rs)	PER			RoE (%)			Target price	Upside (%)
		FY07	FY08E	FY09E	FY07	FY08E	FY09E		
Aban Offshore	3,649	-	33.4	9.3	-7.1	60.4	90.9	5,420.0	48.5
Axis (UTI) Bank	1,111	47.5	37.8	27.0	20.9	16.0	15.7	1,302.0	17.2
Bharat Heavy Electricals	2,064	41.9	32.0	24.6	27.5	27.7	28.0	2,845.0	37.8
Grasim Industries	2,949	18.0	13.0	15.1	27.5	27.2	27.0	3,950.0	34.0
Indo Tech Transformer	666	27.8	17.5	12.0	31.4	37.1	38.2	830.0	24.6
Jaiprakash Associates	363	88.5	64.8	63.6	16.1	15.5	15.3	484.0	33.4
M&M	669	16.7	16.0	14.4	27.0	22.0	19.6	900.0	34.4
Marico	64	34.4	23.6	19.3	58.7	51.6	39.2	70.0	9.9
Punj Lloyd	442	59.0	38.5	25.4	16.4	19.8	20.5	620.0	40.2
Ranbaxy Lab	351	16.6	16.5	14.3	26.3	24.4	23.8	558.0	58.9
Shiv- vani Oil & Gas	566	67.3	15.6	12.1	10.4	16.9	19.4	670.0	18.5
SBI	2,162	25.1	24.3	20.2	15.4	12.2	11.9	2,680.0	23.9

* CMP as on January 31, 2008

Name	CMP (Rs)	PER FY07	PER FY08E	PER FY09E	RoE (%) FY07	RoE (%) FY08E	RoE (%) FY09E	Target price	Upside (%)
Aban Offshore	**3,649**	-	33.4	9.3	-7.1	60.4	90.9	**5,420.0**	48.5

Remarks:

- Aban Offshore, one of Asia's largest oil drilling companies, is benefiting from the increase in oil exploration and production activities globally. The robust demand environment is resulting in firm day rates for its assets.
- In addition to re-pricing of its assets at higher day rates, the company is also benefiting from the efforts taken to substantially ramp up the asset base through organic and inorganic initiatives. This would significantly improve its financial performance over the next few years.
- At the current market price the stock trades at 9.3x FY2009 and 7.2x FY2010 estimated earnings. We maintain the Buy call on the stock with a price target of Rs5,420.

Name	CMP (Rs)	PER FY07	PER FY08E	PER FY09E	RoE (%) FY07	RoE (%) FY08E	RoE (%) FY09E	Target price	Upside (%)
Axis (UTI) Bank	**1,111**	47.5	37.8	27.0	20.9	16.0	15.7	**1,302.0**	17.2

Remarks:

- Axis Bank is one of the fastest growing private sector banks, which has considerably improved its earnings quality and overall performance under the able Chairmanship of Mr Nayak.
- The bank's assets are expected to grow at a compounded annual growth rate (CAGR) of 36.9% over FY2007-09E. The growing assets along with stable to improving margins will lead to a strong growth in net interest income of the company during the period. The bank has a very robust fee income model in place.
- The bank has raised around Rs4,200 crore which would help it to maintain its growth momentum in the next three years.
- At the current market price, the stock is quoting at 27x FY2009E earnings per share (EPS), 12.9x FY2009E pre-provision profits and 4x FY2009E book value. We maintain our Buy recommendation on the stock with a twelve-month price target of Rs1,302.

Name	CMP (Rs)	PER FY07	PER FY08E	PER FY09E	RoE (%) FY07	RoE (%) FY08E	RoE (%) FY09E	Target price	Upside (%)
BHEL	**2,064**	41.9	32.0	24.6	27.5	27.7	28.0	**2,845.0**	37.8

Remarks:

- 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 Rs78,000 crore, ie 3.6x its FY2008E revenue, provides high earnings visibility.
- The power ministry has proposed around five ultra mega power projects entailing a capacity addition of 20,000MW (4,000MWx5) 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 out 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 24.6x its FY2009E earnings. BHEL's valuation looks attractive as compared with that of its peers, such as Siemens, ABB and Larsen and Toubro.

Name	CMP (Rs)	PER FY07	PER FY08E	PER FY09E	RoE (%) FY07	RoE (%) FY08E	RoE (%) FY09E	Target price	Upside (%)
Grasim Industries	**2,949**	18.0	13.0	15.1	27.5	27.2	27.0	**3,950.0**	34.0

Remarks:

- Grasim industries will be augmenting its capacity by 9.5MMT. This will include two greenfield units of 4MMT each (one at Kotputli and the second at Shambhupura) and a brownfield expansion of 1.5MMT. With the tight demand-supply situation expected to persist in FY2009 the incremental volumes will augur well for the company.
- With the outlook for the VSF business remaining positive, the incremental volumes coupled with a firm-pricing scenario will provide stability to the company's business.
- These two factors coupled with incremental profits from UltraTech's business will boost the consolidated earnings of the company.

Name	CMP	PER			RoE (%)			Target	Upside
	(Rs)	FY07	FY08E	FY09E	FY07	FY08E	FY09E	price	(%)
Indo Tech Transformers	**666**	27.8	17.5	12.0	31.4	37.1	38.2	**830.0**	24.6

Remarks:

- Transmission and distribution of power is all set to attract huge investments (Rs427,000 crore over the XIth Five-year Plan) owing to the need to develop a robust network for power distribution. Transformer making companies like Indo Tech Transformers are all set to benefit from the huge investments in the sector.
- Indo Tech Transformers, a niche player in the transformer manufacturing space, arguably has the best margins in the industry. The high margins due to operational efficiencies are fuelling the growth of the company.
- The company is expanding its manufacturing capacity to 7,450 MVA per annum to meet the rise in demand for transformers. It has an outstanding order book of Rs180 crore.
- The stock trades at a price/earnings ratio of 12x its FY2009E. We maintain Buy recommendation on the stock.

Jaiprakash Associates	**363.0**	88.5	64.8	63.6	16.1	15.5	15.3	**484.0**	33.4

Remarks:

- Jaiprakash is expanding its capacity by 15MMT over the next three years at the end of which it will emerge as one of the largest cement players in north India with a capacity of 22MMT.
- The company is the largest private sector hydropower player and is currently sitting on a huge construction order book of Rs7,200 crore. Taking cognisance of the government's target of achieving 50,000MW in hydropower electricity by 2012, we expect the order book to maintain its current momentum.
- The Taj Expressway project coupled with the company's real estate business (Taj Greens) will add value to the company's shareholders.
- Thus the company's diversified businesses will provide the much-needed stability to the overall business in the wake of a downturn in the cement cycle.

Mahindra & Mahindra	**669**	16.7	16.0	14.4	27.0	22.0	19.6	**900.0**	34.4

Remarks:

- Government's increasing thrust on agriculture and easy availability of credit would benefit M&M's tractor sales.
- Launch of Logan in collaboration with Renault and other planned launches such as new UV platform and other products in collaboration with International Trucks is set to further enrich its product mix. Another multi-purpose vehicle (code named Ingenio) is slated to be launched in FY2008.
- A better product mix and higher operating efficiencies have helped improve the margins of the company.
- Subsidiaries like Tech Mahindra, Mahindra Gesco, and MMFSL are rendering strong performances and are adding significant value to its sum-of-the-parts valuation.
- Currently M&M is quoting at 9x FY2009E its consolidated earnings.

Name	CMP	PER			RoE (%)			Target	Upside
	(Rs)	FY07	FY08E	FY09E	FY07	FY08E	FY09E	price	(%)
Marico	**64**	34.4	23.6	19.3	58.7	51.6	39.2	**70.0**	9.9

Remarks:

- Marico is a major player in the Indian hair care and edible oil markets. Its flagship brand Parachute combined with Nihar commands a 57% share of the branded coconut oil market in India. Its 'good for heart' edible oil brand 'Saffola' is also witnessing good volume growth.
- Marico has been growing both the organic and inorganic way and thereby follows the strategy of adding new products and territories to its portfolio. Apart from domestic operations, its international business covers countries like Bangladesh and Egypt. The company is also expanding its business to some extent to the US and the UAE.
- We believe apart from the growth in the existing business through product innovations, the expanding new age businesses of Kaya Clinics and weight loss centers and spas in the USA promise a great deal.
- Marico is among the fastest growing FMCG companies in India with very good return ratios. At the current market price, the stock trades at 23.6x its FY2008E earnings and 19.3x its FY2009E earnings.

Name	CMP	PER FY07	PER FY08E	PER FY09E	RoE FY07	RoE FY08E	RoE FY09E	Target price	Upside (%)
Punj Lloyd	**442**	59.0	38.5	25.4	16.4	19.8	20.5	**620.0**	40.2

Remarks:

- Punj Lloyd Ltd (PLL) is the second largest EPC player in the country with a global presence. We believe PLL with SEC and Simon Carves is well-integrated and poised to tap the global opportunity available in hydrocarbons and infrastructure sectors.
- PLL has witnessed a five-fold increase in its average order size from $30 million to about $130-140 million. This move-up on the value chain has made PLL more competitive in executing larger and complex orders.
- We expect the spectacular order flow to continue for PLL. The current order book of Rs16,012 crore is 3.1x its FY2007 sales and imparts strong visibility. We expect PLL's consolidated revenues and profits to grow at a compounded annual growth rate (CAGR) of 37.1% and 55.8% respectively over FY2007-10E.
- At the current market price the stock trades at 38.5x and 25.4x its FY2008E and FY2009E fully diluted earnings per share (EPS) respectively. We maintain our Buy on the stock with a price target of Rs620.

Name	CMP	PER FY07	PER FY08E	PER FY09E	RoE FY07	RoE FY08E	RoE FY09E	Target price	Upside (%)
Ranbaxy	**351**	16.6	16.5	14.3	26.3	24.4	23.8	**558.0**	58.9

Remarks:

- With a geographically diversified presence and a large product portfolio, Ranbaxy is one of the best plays on the global generic opportunity.
- The company has guided towards an impressive 18-20% growth in CY2008, an expansion of margins to 17.5-18%, resulting in a net profit growth of 20-25%. This guidance is excluding any one-time exclusivity opportunities in the USA.
- Ranbaxy believes the next wave of its growth to come from the branded markets in Asia, Africa and Latin America. With a product pipeline of over 100 products for these markets, revenues from emerging markets will drive the company's growth.
- Ranbaxy believes that it has FTF status on approximately 18 Para IV ANDA filings, representing a market size of about USD27 billion. It expects to monetise at least one FTF opportunity every year for the next few years and has already announced the opportunities until CY2010. The FTF opportunities announced so far are collectively valued at Rs2,716 crore, translating into a per share value of Rs68.
- Ranbaxy has decided to de-merge its new drug discovery research (NDDR) operations into a separate entity effective from January 1, 2008 and list it subsequently. This will boost the overall profitability of the core business and also unlock value in the discovery research and development (R&D) assets. The announcement of further details on the demerger scheme in February 2008 will act as a near-term trigger for the stock.
- At the current market price of Rs351, Ranbaxy is trading at 16.5x its estimated CY2008E and 14.3x its estimated CY2009E earnings. We maintain our Buy recommendation on the stock with a price target of Rs558 (Rs490 for base business plus Rs68 for FTFs).

Name	CMP (Rs)	PER			RoE (%)			Target price	Upside (%)
		FY07	FY08E	FY09E	FY07	FY08E	FY09E		
Shiv- vani Oil & Gas	**566**	67.3	15.6	12.1	10.4	16.9	19.4	**670.0**	18.5

Remarks:

- With a fleet of 25 onshore drilling rigs and six seismic survey crew, Shiv-Vani Oil & Gas Exploration (SOGEL) has emerged as the largest onshore service provider catering to oil and gas exploration companies.
- Augmentation of assets by the company is well timed in the industry up-cycle as heightened exploration activity has led to a severe shortage of resources with service providers, leading to firming up of day rates (or billing rates per km in case of seismic survey) for various services. Moreover, the order backlog of over Rs3,000 crore (over 8x CY2006 revenues) provides strong revenue-growth visibility.
- The consolidated revenues and earnings are expected to grow at CAGR of 60.3% and 72.7% respectively over the three-year period CY2006-09.
- Despite the robust growth prospects, the scrip is available at attractive valuations of 12.1x FY2009 earning estimates. We recommend Buy call on the stock.

Name	CMP (Rs)	PER FY07	PER FY08E	PER FY09E	RoE FY07	RoE FY08E	RoE FY09E	Target price	Upside (%)
State Bank of India	**2,162**	25.1	24.3	20.2	15.4	12.2	11.9	**2,680.0**	23.9

Remarks:

- SBI has received the approval from the government and is likely to complete its rights issue of Rs16,740 crore by end of FY2008. The rights issue proceeds should help the bank fund its growth plans for years to come.
- The launch of new businesses such as general insurance by April 2008 and private equity business along with the expected improvement in the operating performance in H2FY2008 should sustain the positive sentiment for the stock over the medium term.
- At the current market price, the stock is quoting at 20.2x its FY2009E earnings, 8.6X pre-provision profit and, and 2.3x standalone and 1.9x its consolidated FY2009E book value. We maintain our Buy recommendation on the stock with a revised twelve-month forward price target of Rs2,680.

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