



Sharekhan top picks

In the February 2007 issue, we had recommended the best 12 of our Stock Ideas as Sharekhan Top Picks. As on March 2, 2007, the return on this basket of stocks has been a negative 13.8% as compared to the Sensex, which declined by 10.5%, and the S&P CNX Nifty, which has dropped by 10.9%, during the period.

We have made five changes in the portfolio. We have taken out Ahmednagar Forgings, India Cements, Madras Cement, Ranbaxy Laboratories and UltraTech Cement from the portfolio. We have introduced five new stocks—Alphageo

India, Bharti Airtel, Bharat Electronics, Infosys Technologies and Tata Consultancy Services—in the portfolio.

The adjustments reflect a noticeable shift away from the cement stocks, given the harsh measures indicated by the government to restrict any uptick in cement prices. The cement stocks are replaced by large-cap technology companies that are insulated from the adverse impact of the firm interest rate scenario in the domestic market. Moreover, the recent depreciation of the rupee would also aid the overall sentiments towards the tech counters.

Name	CMP* (Rs)	PER			RoE (%)			Target price	Upside (%)
		FY06	FY07E	FY08E	FY06	FY07E	FY08E		
Aditya Birla Nuvo	1,184.9	54.1	40.6	22.1	12.8	15.5	15.4	1,600.0	35.0
Alphageo India	193.3	22.7	14.2	7.9	20.4	26.5	33.1	270.0	40.0
Bharti Airtel	707.4	59.4	31.9	22.7	20.7	28.8	31.4	820.0	16.0
Bharat Electronics	1,487.8	20.4	17.7	15.7	29.7	25.6	22.5	1,715.0	15.0
Bharat Heavy Electricals	2,099.6	30.6	21.3	16.8	23.0	26.2	26.4	2,650.0	26.0
ICICI Bank	845.9	29.6	22.3	18.6	13.6	14.4	15.5	1,240.0	47.0
Infosys Technologies	2,103.2	47.2	31.0	23.4	35.3	39.6	39.6	2,670.0	27.0
Mahindra & Mahindra	770.8	27.8	20.8	17.8	29.5	27.6	23.2	1,050.0	36.0
NIIT Technologies	442.6	25.7	14.1	12.3	30.3	37.6	31.9	570.0	29.0
Sun Pharmaceutical	967.2	31.3	25.3	20.2	42.2	26.9	20.8	1,341.0	39.0
Tata Consultancy Services	1,208.5	40.7	28.7	22.5	49.4	45.2	39.4	1,508.0	25.0
Thermax	378.0	44.6	22.8	16.5	22.3	31.8	31.8	433.0	15.0

* CMP as on March 02, 2007

Name	CMP (Rs)	PER			RoE (%)			Target price	Upside (%)
		FY06	FY07E	FY08E	FY06	FY07E	FY08E		
Aditya Birla Nuvo	1,184.9	54.1	40.6	22.1	12.8	15.5	15.4	1,600.0	35.0

- Remarks:**
- ♦ ABN participates in India's four most exciting sectors: garments, insurance, telecom and IT/IT enabled services. It has a perfect strategy: to earn cash from its cash cow businesses, such as carbon black, rayon and fertilisers, and invest in high-growth businesses, such as garments, insurance, telecom and IT/IT enabled services.
 - ♦ Idea Cellular in which the company owns 36.26% currently has filed its prospectus for raising Rs2,125 crore from the capital markets in a price band of Rs65-75. Even at the higher band Idea is trading significant to its peers. The listing of the stock and its performance provide good short-term triggers to the stock
 - ♦ At the current market price, the stock trades at a price/earnings ratio of 22.1x FY2008E consolidated earnings and EV/EBIDTA of 11.2x FY2008E.
 - ♦ Given the diverse businesses of ABN, the company is best valued using the sum-of-parts method. Based on the sum-of-parts valuation, we estimate the fair value of ABN to be Rs1,600 per share. Out of the above telecom, insurance and BPO contribute close to Rs1,400.

Alphageo India	193.3	22.7	14.2	7.9	20.4	26.5	33.1	270.0	40.0
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- Remarks:**
- ♦ Alphageo India is engaged in providing all kinds of seismic survey services (ie data acquisition, data processing and data interpretation) to oil exploration companies and has the distinction of being the only domestic company that has capabilities to carry out 3D (three-dimensional) seismic surveys.
 - ♦ It has a pending order book position of Rs110 crore (around 4x its FY2006 revenues) and an order pipeline of around Rs120 crore which provide a strong revenue growth visibility for FY2008.
 - ♦ At the current market price the stock trades attractively at 14.2x FY2007 and 7.9x FY2008 earning estimates.

Bharti Airtel	707.4	59.4	31.9	22.7	20.7	28.8	31.4	820.0	16.0
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- Remarks:**
- ♦ Bharti Airtel, the largest wireless telephony service operator, is one of the key beneficiaries of the consumption boom in the country. It has reportedly added subscribers at a healthy CAGR of over 75% in the past three years and is expected to increase its subscriber base at a CAGR of over 35% over the next two years.
 - ♦ The company's focus on introducing innovative services, cost control measures and growing economies of scale is resulting in an improvement in its margins, despite the continued pressure on the average revenue per unit (ARPU). Consequently, the earnings are estimated to grow at CAGR of over 46% over the three-year period FY2006-09.
 - ♦ At the current market price the stock trades attractively at 31.9x FY2007 and 22.7x FY2008 earning estimates.

Bharat Electronics	1,487.8	20.4	17.7	15.7	29.7	25.6	22.5	1,715.0	15.0
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- Remarks:**
- ♦ Given its wide range of products, research & development capabilities and proven track record, Bharat Electronics is well poised to effectively tap the huge opportunity in the defence sector.
 - ♦ It has a pending order backlog of Rs7,300 crore and would benefit from the over 64% increase in the capital outlay for security and other equipment used by defence forces. Moreover, the recent alliances/tie-ups with leading defence contractors such as Northrop Grumman would further boost the overall growth in the long term.
 - ♦ At the current market price the stock trades attractively at 17.7x FY2007 and 15.7x FY2008 earning estimates.

Name	CMP (Rs)	PER			RoE (%)			Target price	Upside (%)
		FY06	FY07E	FY08E	FY06	FY07E	FY08E		
BHEL	2,099.6	30.6	21.3	16.8	23.0	26.2	26.4	2,650.0	26.0

- 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 Rs46,700 crore, ie 3.4x its FY2006 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 16.8x its FY2008E earnings. BHEL's valuation looks attractive as compared with that of its peers, such as Siemens, ABB and Larsen and Toubro.

ICICI Bank	845.9	29.6	22.3	18.6	13.6	14.4	15.5	1,240.0	47.0
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- Remarks:**
- ♦ ICICI Bank is India's second-largest bank. Its strong positioning in the retail advance segment gives it dual advantages of a healthy growth in both loans and fee income.
 - ♦ The Bank expects to improve margins and moderate business growth. It has no plans to raise fresh equity, which would improve its return on equity going forward. Its international operations are also gaining momentum, the only challenge would be to manage the uptick in non-performing assets.
 - ♦ Various subsidiaries (life insurance, general insurance, ICICI Securities) add Rs400 to the overall valuation.
 - ♦ The stock trades at a PER of 18.6x its FY2008E earnings and 2.7x its FY2008E book value. ICICI Bank's valuation looks attractive as compared with that of its peers, such as HDFC Bank.

Infosys Technologies	2,103.2	47.2	31.0	23.4	35.3	39.6	39.6	2,670.0	27.0
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- Remarks:**
- ♦ Infosys Technologies is a premier offshore IT service company with a proven track-record of consistent and higher than industry average growth rates.
 - ♦ It has been able to maintain its profitability despite the cost pressures. Given its structure, the company is likely to be least affected by the recent amendments in the tax regime.
 - ♦ At the current market price the stock trades attractively at 31.0x FY2007 and 23.4x FY2008 earning estimates.

Name	CMP (Rs)	PER			RoE (%)			Target price	Upside (%)
		FY06	FY07E	FY08E	FY06	FY07E	FY08E		
Mahindra & Mahindra	770.8	27.8	20.8	17.8	29.5	27.6	23.2	1,050.0	36.0

- Remarks:**
- ♦ The government's increasing thrust on agriculture and the easy availability of credit would benefit M&M's tractor sales.
 - ♦ Its product mix would be further enriched with a number of new launches, including a new UV platform, a mid-sized car Logan (in collaboration with Renault) and other products in collaboration with International Trucks. Another multi-purpose vehicle (code named Ingenio) is slated for a launch 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.
 - ♦ Currently M&M is quoting at 13.1x FY2008 its consolidated earnings.

NIIT Technologies	442.6	25.7	14.1	12.3	30.3	37.6	31.9	570.0	29.0
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- Remarks:**
- ♦ NIIT Technologies was formed by hiving off the IT service business of NIIT in 2004. Since then, the company has restructured its operations to emerge as a mid-sized company focused on three key industry domains. Apart from this, the performance has improved considerably due to the efforts taken to rationalise the client base and expand through inorganic route.
 - ♦ It has shown a robust performance in the past two quarters. In Q3FY2007, the consolidated earnings grew at an explosive rate of 28.6% sequentially and 91.9% on an annual basis, which is the second consecutive quarter of over 20% sequential growth in earnings.
 - ♦ In terms of the outlook, the company is expected to maintain the growth momentum on the back of the record order intake of \$56 million during the quarter. The pending order backlog of \$95 million (executable over the next one year) is one of the highest ever reported by the company.
 - ♦ At the current market price the stock trades at 14.1x FY2007 and 12.3x FY2008 estimated earnings, which is quite attractive given the estimated growth of 46% CAGR in its earnings during the two-year period FY2006-08.

Sun Pharmaceutical	967.2	31.3	25.3	20.2	42.2	26.9	20.8	1,341.0	39.0
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- Remarks:**
- ♦ Sun Pharma maintains the numero uno ranking with neurologists, cardiologists, diabetologists and orthopedics.
 - ♦ With 56 abbreviated new drug applications (ANDAs) pending US FDA approval and a filing rate of 30+ ANDAs per year, Sun Pharma has one of the strongest product pipelines for the US market. The company is amongst the top three players in around 15 of the 25 products that it sells in the US market.
 - ♦ Sun Pharma is likely to show a CAGR of about 60% in ROW markets in FY2006-08. It has 750 products registered and another 300+ products pending approval in these markets.
 - ♦ With a strong cash position of over Rs1,500 crore, Sun Pharma is well placed to unlock value from potential acquisitions. The demerger of its innovative research and development research unit into a separate arm is likely to trigger substantial value unlocking going forward. The company's disclosed innovative R&D pipeline consists of one new chemical entity and two novel drug delivery system products.

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Name	CMP (Rs)	PER			RoE (%)			Target price	Upside (%)
		FY06	FY07E	FY08E	FY06	FY07E	FY08E		
TCS	1,208.5	40.7	28.7	22.5	49.4	45.2	39.4	1,508.0	25.0

Remarks:

- ♦ Tata Consultancy Services, the largest Indian IT service company, is effectively using inorganic growth strategy to boost its service and delivery capabilities in some of the key fast-growing areas (like engineering services, software products, consulting services and BPO) and industry domains (like banking, telecom and aerospace).
- ♦ It has shown the ability to maintain margins by utilising various levers of margin improvement like productivity gains, better pricing, improved revenue mix and utilisation levels.
- ♦ At the current market price the stock trades attractively at 28.7x FY2007 and 22.5x FY2008 earning estimates.

Thermax	378.0	44.6	22.8	16.5	22.3	31.8	31.8	433.0	15.0
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Remarks:

- ♦ Thermax, with its diversified product and application range, is riding on a sustainable capital expenditure (capex) boom in the industrial and infrastructure sectors.
- ♦ The capacity expansion and related projects in the core sectors are leading to higher order intake for Thermax. Thermax' current order book of Rs3,024 crore, ie 1.9x its FY2006 revenue, provides high earnings visibility.
- ♦ The robust traction across divisions and a burgeoning order book would drive a 28.9% CAGR in Thermax' consolidated revenues over FY2006-08.
- ♦ The improving operating leverage from cost rationalisation measures and economies of scale will lead to a 260-basis-point margin expansion over FY2006-08.
- ♦ At the current market price of Rs378, the stock trades at a PER of 16.5x its FY2008E earnings and 10.1x EV/EBIDTA. Rs43 per share of cash and cash equivalent on the company's books as on December31, 2006 provides a margin of safety.

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

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