investor's eye

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Index

Take Five

Scrip	Reco Date	Reco Price	CMP	Target
Bharat Bijlee	29-Nov-04	192	**1,443**	1,730
BEL	25-Sep-06	1,108	**1,303**	1,525
Ceat	28-Nov-06	122	**146**	190
F-M Goetze	18-Jan-07	385	**383**	559
Lupin	06-Jan-06	403	**584**	670

Omax Autos

Apple Green

Stock Update

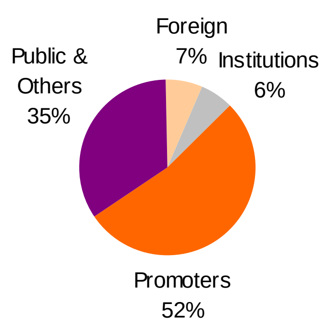
Margins improve

Buy; CMP: Rs93

Company details

Price target:	Rs134
Market cap:	Rs198 cr
52 week high/low:	Rs174/58
NSE volume: (No of shares)	40,187
BSE code:	520021
NSE code:	OMAXAUTO
Sharekhan code:	OMAX
Free float: (No of shares)	1.0 cr

Shareholding pattern



Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	8.2	-7.9	25.8	-39.8
Relative to Sensex	2.5	-17.5	-11.1	-60.2

Result highlights

- The Q3FY2007 results of Omax Autos are ahead of our estimates due to higher margins during the quarter.
- The net sales for the quarter rose by 9% to Rs179.4 crore, led by a 7.9% growth in the domestic revenues and a 32% growth in the export revenues.
- The operating profit for the quarter rose by 52.8% to Rs18.5 crore mainly due to a 300-basis-point improvement in the operating profit margin (OPM) to 10.3%. This is a result of various cost saving initiatives implemented by the company in order to bring down its power, personnel and other manufacturing costs.
- The other income is higher than estimated at Rs2.72 crore. Aggressive capacity expansion plans of the company have also led to higher interest and depreciation costs. The profit after tax (PAT) for the quarter stood at Rs6.66 crore, rising by 34.3%.
- The company has also announced that it would set up a new manufacturing unit in Lucknow to manufacture chassis for Tata Motors. The unit would be set up with an initial capacity of 48,000 chassis and is expected to deliver revenues of Rs120 crore by FY2009 and of about Rs225 crore by FY2011.
- At the current market price of Rs93, the stock discounts its FY2008E earnings by 6.3x and quotes at an enterprise value (EV)/earnings before interest, depreciation, tax and amortisation (EBIDTA) of 3.7x. We maintain our Buy recommendation on the stock with a price target of Rs134.

Result table Rs (cr)

Particulars	Q3FY07	Q3FY07	% yoy	9MYFY07	9MYFY06	% yoy
Net sales	**179.4**	**164.6**	**9.0**	**508.3**	**459.1**	**10.7**
Total expenditure	**160.9**	**152.5**	**5.5**	**457.5**	**420.8**	**8.7**
Raw material consumed	117.1	107.8	8.6	339.1	302.7	12.0
Change in stock	4.3	0.0		1.4	-1.5	
Staff cost	16.9	7.8	115.2	48.5	21.8	122.5
Other expenses	22.8	36.9	-38.4	68.5	97.8	-30.0
Operating profit	**18.5**	**12.1**	**52.8**	**50.9**	**38.3**	**32.9**
Other income	2.7	1.7		6.3	4.2	
EBIDTA	**21.2**	**13.8**	**53.8**	**57.2**	**42.5**	**34.6**
Interest	5.3	2.3	131.3	13.2	6.8	94.8
PBDT	15.9	11.5		44.0	35.7	
Depreciation	5.8	3.8	51.2	16.1	12.6	28.4
PBT	10.1	7.7	32.2	27.9	23.2	20.5
Tax	3.5	2.7		9.8	8.1	
Reported PAT	**6.7**	**5.0**	**34.3**	**18.1**	**15.1**	**19.8**
Prior period expenses				0.2	0.0	
Adjusted PAT	6.7	5.0	34.3	17.9	15.1	18.7
EPS (Rs)	3.1	2.3		8.5	7.1	
OPM (%)	10.3	7.3		10.0	8.3	
NPM (%)	3.7	3.0		3.6	3.3	

Top line rises by 9%, exports still disappoint

The net revenues grew by 9% to Rs179.4 crore, in line with our estimates. The domestic revenues marked a growth of 7.9% to Rs169.4 crore while the export revenues stood at Rs10 crore for the quarter, rising by 32%. The company has further revised its export target for the current fiscal to Rs35 crore from Rs50 crore earlier. The export target for FY2008 has also been reduced to Rs55-60 crore from an earlier target of Rs100 crore. Most of the export orders are catered through the Binola plant, which has been reserved for export orders. The company expects to finalise the Tenneco order by March-end. It is also in the process of negotiating export contracts with international players like Piaggio and Delphi.

Margins improve

The strong improvement in the OPM has been a positive surprise. The margin improved by 300 basis points year on year (yoy) and by about 40 basis points sequentially to 10.3%. The margin improved due to the various cost saving initiatives implemented by the company during the quarter. The company has been able to save substantial power cost due to the use of furnace oil power generation sets. Various other measures, such as slight design and process improvements, are also being implemented in order to further reduce its raw material and other manufacturing costs.

Consequently, the operating profit for the quarter grew by 52.8% to Rs18.5 crore. Further margin improvement can be expected after the coming on stream of the subsidiary Omax Steels, which is being set up at Ludhiana. The subsidiary is expected to start full operations by this fiscal end. Omax Autos would utilise a major part of the subsidiary's output for its internal consumption, resulting in higher economies of scale and efficiency in material consumption.

Setting up a new unit for Tata Motors

The company has just announced that it is setting up of a new manufacturing unit in Lucknow, inside Tata Motors plant, for supply of chassis. The unit is expected to start with an initial capacity of 48,000 chassis by December 2007. The capacity would be gradually increased to 96,000 units. The same is expected to yield revenues of Rs120 crore by FY2009 and of Rs225 crore by FY2011. This is a big positive for the company, as it would help to de-risk its business model, which up till now was skewed towards Hero Honda Motors. Also, it would help to mitigate the impact of lower exports, which have not ramped up as per expectations. For setting up this new unit, the company would be spending Rs50 crore in the first phase of expansion.

Further, Omax Autos has plans to expand capacities across its units including the facilities at Dharuhera, Binola and Bangalore. For the current fiscal, the estimated capital expenditure (capex) is Rs60 crore while Rs120 crore is expected to be spent in FY2008 (including capex on the new unit at Lucknow). All the capex will be funded partly by term loans and partly by internal accruals.

Valuations and view

Margin improvement as a result of cost savings has been a positive surprise this quarter. We expect the margin to improve further owing to the coming on stream of Omax Steel and the various cost saving measures. Also, the new venture to supply chassis to Tata Motors should yield higher margins for the company, with the target EBIDTA margin of 12% by FY2009. On back of slower than expected ramp up in exports, we are marginally reducing our estimates for FY2008. Our revenue estimates have been lowered by 5% to Rs764.6 crore and PAT estimates by 4.4% to Rs30.5 crore.

At the current levels, the stock discounts its FY2008E earnings by 6.5x and quotes at an EV/ EBIDTA of 3.8x. The stock quotes at very attractive valuations and we maintain our Buy recommendation on the stock with a price target of Rs134.

Earnings table

Particulars	FY05	FY06	FY07E	FY08E
Net sales (Rs cr)	505.3	578.6	664.8	764.6
% y-o-y growth		*14.5*	*14.9*	*15.0*
Net profit (Rs cr)	20.3	20.0	24.6	30.5
% y-o-y growth		*-1.2*	*22.6*	*23.9*
EPS (Rs)	8.9	9.4	11.5	14.2
PER (x)	10.4	9.9	8.1	6.5
Book value (x)	43.9	52.8	69.1	90.5
P/BV (x)	2.1	1.8	1.3	1.0
EV/EBITDA (x)	5.7	6.4	4.4	3.8
Dividend yield (%)	2.2	2.2	2.4	2.7
RoCE (%)	16.9	13.3	18.9	15.7
RoNW (%)	23.2	18.8	22.0	17.8

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

Bank of India

Apple Green

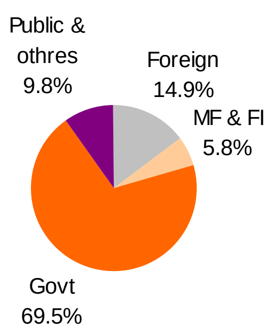
Stock Update

Another excellent quarter

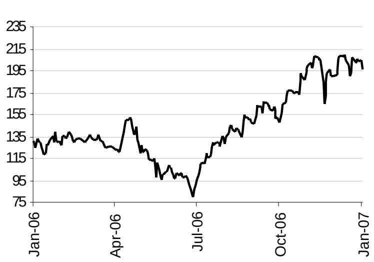
Buy; CMP: Rs196

Company details	
Price target:	Rs220
Market cap:	Rs9,567 cr
52 week high/low:	Rs214/80
NSE volume: (No of shares)	19.5 lakh
BSE code:	532149
NSE code:	BANKINDIA
Sharekhan code:	BOI
Free float: (No of shares)	14.9 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	7.6	35.6	132.2	67.8
Relative to Sensex	1.9	21.4	64.1	10.8

Result highlights

- For Q3FY2007 Bank of India (BOI) reported numbers well above the market's and our expectations. The growth in its net interest income (NII) and other income was in line with the expectations of a good set of numbers. What made the good results look even better was the restrain the bank showed in case of operating expenses.
- The NII grew by 26.9% to Rs920 crore against our estimate of Rs936.3 crore. The 26.9% growth in the NII was brought about by a 22.3% growth in the assets and a 16-basis-point improvement in the global net interest margin (NIM) year on year (yoy) to 3.18%.
- The other income reported a 22.8% growth with the trading income showing a very high growth of 144.5% yoy to Rs55.5 crore. The core fee income was up 22.6% yoy while the recoveries declined by 49% to Rs14.9 crore.
- The operating expenses grew by a sedate 15.3% to Rs627.9 crore as the staff expenses grew by only 7.8% and the other expenses grew by 29.6% yoy.
- The operating profit was up by 38.7% yoy to Rs614.4 crore and the core operating profit excluding the treasury income was up 33% yoy to Rs558.9 crore.
- The provisions increased by 16.6% to Rs289.8 crore with the non-performing asset (NPA) provisions up 55.6% to Rs190.9 crore. Lower taxes during the quarter also helped the profit after tax (PAT) to report a 78% year-on-year (y-o-y) growth while the profit before tax (PBT) grew by 67% yoy.
- At the current market price of Rs196, the stock is quoting at 8.1x its FY2008E earnings per share, 3.3x its FY2008E pre-provisioning profits and 1.5x FY2008E book value. We maintain our Buy recommendation on the stock with a revised price target of Rs220.

Result table Rs (cr)

Particulars	Q3FY07	Q3FY06	% yoy chg	% qoq chg	9MFY07	9MFY06	% yoy chg
Net interest income*	920.0	724.8	26.9	1.3	2,653.4	1,998.3	32.8
Other income	322.3	262.5	22.8	-8.8	986.2	860.0	14.7
Treasury income	*55.5*	*22.7*	*144.5*	*10.4*	*157.1*	*101.0*	*55.5*
Fee	*195.7*	*159.6*	*22.6*	*-14.4*	*613.9*	*542.9*	*13.1*
Net income	1,242.3	987.3	25.8	-1.5	3,639.6	2,858.2	27.3
Operating expenses	627.9	544.4	15.3	-13.2	1,958.9	1,582.8	23.8
Operating profit	614.4	442.9	38.7	14.2	1,680.7	1,275.5	31.8
Core operating profit (excluding treasury)	558.9	420.2	33.0	14.5	1,523.6	1,174.5	29.7
Provisions & contingencies	289.8	248.6	16.6	33.1	736.7	675.7	9.0
PBT	324.6	194.3	67.0	1.3	944.1	599.8	57.4
Provision for taxes	69.7	51.2	36.0	-35.6	268.3	152.8	75.6
Net profit	254.9	143.1	78.1	20.1	675.7	447.0	51.2

*Adjusted for amortisation expenses

Selective growth proving to be the right choice for margins

The bank has maintained its strategy of achieving selective growth with the global business growing by 24% yoy. The advances rose by 27.2% yoy and deposits increased by 21% yoy. The bank has put more focus on the margins and the quality of credit which has helped it improve its global margins by 16 basis points yoy and by 12 basis points quarter on quarter (qoq).

The cost of funds went up by 32 basis points compared with the yields which rose by 47 basis points. This is where selectivity is paying off for the bank, as it has not gone overboard to raise high cost deposits to fund its asset growth and thus prevented margin erosion.

The cost of deposits was contained as the low cost deposits or the current and savings accounts (CASA) increased by 22% and constituted 41.3% of the total deposits compared with 40% of the same on a y-o-y basis.

The yields have improved as the bank was able to grow its retail credit portfolio by 55.5% to 32.3% of the non-food credit from 27.1% of the same in December 2005. It was also able to grow its small and medium enterprises (SME) credit by 18% yoy; the yields are comparatively higher in the retail and SME portfolio.

Yield analysis (%) table

Particulars	Q3FY07	Q3FY06	Q2FY07
Yield on funds	7.96	7.49	7.60
Cost of funds	4.79	4.47	4.54
NIM	3.18	3.02	3.06

Source: Company

Operating expenses remain under control

The operating expenses grew by a sedate 15.3% to Rs627.9 crore as the staff expenses grew by only 7.8% yoy while the other expenses grew by 29.6% yoy. On a sequential basis, both the expense items declined by 7.1% and 21.4% respectively. The sequential decline in the costs is due to the absence of the previous quarter's one-time charges like the centenary promotional expenses and lower charges on account of the implementation of the core banking solution.

Particulars	Q3FY07	Q3FY06	% yoy chg	% qoq chg
Staff	384.2	356.3	7.8	-7.1
Other operating expenses	243.7	188.0	29.6	-21.4
Total operating expenses	627.9	544.4	15.3	-13.2

Asset quality shows considerable improvement

The asset quality showed significant improvement with the gross NPA (GNPA) down to 2.74% from 4.5% and the net NPA (NNPA) falling to below 0.95% from 2% yoy. The NPA provisions were up 55.6% yoy and 27.3% qoq to Rs190.9 crore and the bank has brought down the NNPA in percentage terms below the 1% mark, which it had set as a target to be achieved by March 2007.

Particulars	Q3FY07	Q3FY06	% yoy chg	% qoq chg
Provisions & Contingencies	289.8	248.6	16.6	33.1
NPA	190.9	122.7	55.6	27.3
Amortization	61.2	68.2	-10.3	3.5
Others	37.7	57.7	-34.6	334.8

Source: Company

Capital adequacy remains a concern

The bank's capital adequacy ratio (CAR) stood at 11.76% in December 2006 and the bank expects to maintain the same at 11% in March 2007. The management is not keen on coming out with a follow-on public offer and would rather explore the other options available like the hybrid Tier-I route, which offers a headroom to raise Rs800 crore.

Capital raising options to be decided in due course

Currently the government holds a 69.5% stake in the bank and assuming the holding comes down to 57%, we could see a follow-on offer of 10.6 crore equity shares. That would translate into 22% of the pre-issue capital. We have not factored in an equity dilution but the bank may have to come out with a follow-on offer some time in FY2008 if the hybrid and the other capital routes prove to be insufficient for funding its growth.

Bond portfolio remains insulated from interest rate spikes

The bank has a very low bond duration of 0.55 years in its marked-to-market investment book; this would insulate it from any investment depreciation that has to be booked if the interest rates continue to rise. Currently the interest rate scenario has an upward bias and for most public sector banks the duration is much higher. Hence the bank should be given a better valuation based on the low interest rate risk on its books and improved earnings going forward.

Valuation and view

We feel BOI has proved to be the best performing public sector bank for two quarters in a row with improvement in all parameters. What's more, the bank's management has shown proper intent to maintain the improved performance. Based on the improved performance of the bank for the nine months of FY2007 we have revised our FY2007 and FY2008 PAT estimates upwards by 6.8% and 8.7% to Rs978.3 crore and Rs1,178.4 crore respectively.

At the current market price of Rs196, the stock is quoting at 8.1x its FY2008E earnings per share, 3.3x its FY2008E pre-provisioning profits and 1.5x FY2008E book value. We maintain our Buy recommendation on the stock with a revised price target of Rs220.

Earnings table

Particulars	FY04	FY05	FY06	FY07E	FY08E
Net profit (Rs cr)	1,008.3	340.1	701.4	978.3	1,178.4
Shares in issue (cr)	48.8	48.8	48.8	48.8	48.8
EPS (Rs)	20.7	7.0	14.4	20.0	24.1
% y-o-y change	*71.9*	*-66.3*	*106.3*	*39.5*	*20.5*
PE (x)	9.5	28.1	13.6	9.8	8.1
P/PPP (x)	4.3	6.6	5.6	4.0	3.3
Book value (Rs/share)	82.1	91.5	102.1	116.4	135.1
P/BV (x)	2.4	2.1	1.9	1.7	1.5
RONW (%)	29.9	8.0	14.8	18.3	19.2

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

Cadila Healthcare

Emerging Star

Stock Update

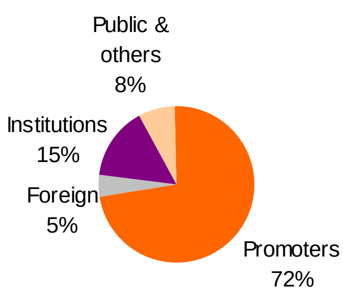
Extraordinary income boosts net profits

Buy; CMP: Rs345

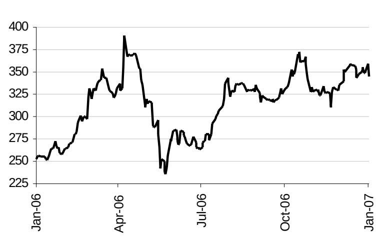
Company details

Price target:	Rs425
Market cap:	Rs4,333 cr
52 week high/low:	Rs400/300
NSE volume: (No of shares)	43,464
BSE code:	532321
NSE code:	CADILAHC
Sharekhan code:	CADILAHEAL
Free float: (No of shares)	3.5 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	7.2	10.5	36.4	44.3
Relative to Sensex	1.5	-1.1	-3.6	-4.7

Result highlights

- The net sales of Cadila Healthcare (Cadila) increased by 24.7% year on year (yoy) to Rs460.9 crore in Q3FY2007. The growth was driven by a 105.1% growth in the formulation exports and a 13.4% rise in the exports of active pharmaceutical ingredients (APIs). The sales growth was ahead of our expectations.
- The 105.1% jump in the formulation exports was driven by the improved performance of the French business (a growth of 188.3% year on year [yoy]) and US business (a growth of 105% yoy). New launches in the USA and regulatory reforms in France led to the strong growth of the US and French businesses respectively.
- An 84.5% rise in the company's generic research and development (R&D) expenses, along with an increased advertising spend in the consumer business, caused Cadila's operating profit margin (OPM) to shrink by 200 basis points to 17.4% in Q3FY2007. However, in view of the fact that the increased advertising spend for the consumer business was a one-time charge, we expect the margin to bounce back in the future quarters.
- Consequently, the operating profit (OP) of the company rose by 12.3% to Rs82.3crore in the quarter.
- Cadila's adjusted net profit grew by a robust 66.4% to Rs65.9 crore, on the back of a one-time extraordinary income of Rs19.6 crore from the sale of the French branded business. The profit growth surpassed our expectations. However, on excluding the extraordinary income, the reported net profit stood at Rs46.3 crore, up by 12.9% yoy. The earnings for the quarter stood at Rs3.7 per share.

Result table Rs (cr)

Particulars	Q3FY07	Q3FY06	% chg	M9FY07	M9FY06	% chg
Net sales	460.9	369.5	24.7	1364.3	1108.8	23.0
Other operating income	11.5	8.3	38.6	28.7	29.6	-3.0
Total operating income	472.4	377.8	25.0	1393.0	1138.4	22.4
Expenditure	390.1	304.5	28.1	1111.9	916.4	21.3
Operating profit	82.3	73.3	12.3	281.1	222.0	26.6
Other income	0.0	4.4	-100.0	5.2	4.5	15.6
EBIDTA	82.3	77.7	5.9	286.3	226.5	26.4
Interest	4.5	4.9	-8.2	17.0	14.3	18.9
Forex loss	0.4	5.4	-92.6	0.2	7.2	-97.2
Depreciation	21.2	21.4	-0.9	62.2	58.5	6.3
PBT	56.2	46.0	22.2	206.9	146.5	41.2
Taxes	9.8	4.9	100.0	27.4	17.4	57.5
PAT	46.4	41.1	12.9	179.5	129.1	39.0
Minority interest	0.1	0.1	0.0	4.3	-1.5	-386.7
Reported net profit	46.3	41.0	12.9	175.2	130.6	34.2
Extraordinary items	19.6	-1.4	1500.0	19.6	-8.8	322.7
Adjusted net profit	65.9	39.6	66.4	194.8	121.8	59.9
OPM (%)	17.4	19.4		20.2	19.5	
EBIDTA margin (%)	17.4	20.6		20.6	19.9	
Net profit margin (%)	9.8	10.9		12.6	11.5	

- The company has signed three new contract manufacturing contracts during the quarter with international companies, taking the cumulative number of contracts to 20, with peak revenue potential of $27.5 million. Cadila has also filed three abbreviated new drug applications (ANDAs) in the quarter, taking the total number of filings to 44 ANDAs.
- At the current market price of Rs345, the company is quoting at 14.7x its FY2008 estimated earnings. We maintain our Buy recommendation on the company with a price target of Rs425.

Cadila's net sales grew by 24.7% yoy to Rs460.9 crore in Q3FY2007 on a consolidated basis. The growth was driven by a 105.1% growth in the formulation exports and a 13.4% rise in the exports of APIs. The improved performance of the French business (a growth of 188.3% yoy) and the US business (a growth of 105% yoy) also aided the robust sales growth. The sales growth was ahead of our expectations. A sharp rise of 84.6% in the R&D cost and an increase in the advertising spend of the consumer business caused the OPM to shrink by 200 basis points to 17.4% in Q3FY2007. Consequently, the OP of the company rose by 12.3% to Rs82.3 crore in the quarter. A one-time extraordinary income of Rs19.6 crore received from the sale of the branded French business boosted the adjusted net profit, which grew by a whopping 66.4% to Rs69.5 crore in Q3FY2007. The profit growth surpassed our expectations. On excluding the extraordinary item, the reported net profit of the company stood at Rs46.3 crore, up by 12.9% yoy.

Domestic formulation business affected by VAT

Cadila's domestic formulation business grew by a meagre 6.2% to Rs258 crore in Q3FY2007, as compared with the industry growth rate of 15-16%. The branded formulation segment grew by 8.6% whereas the generic formulation business declined by 16.1% during the quarter. The overall growth in the domestic formulation business was affected by the introduction of the value added tax (VAT) in Tamil Nadu with effect from January 1, 2007. Due to this, Cadila's sales in Tamil Nadu (which accounts for approximately 10% of the total domestic formulation business) took a severe beating; the company had no sales of its formulations in Tamil Nadu in December 2006.

On the positive side, the company expects to recover the lost sales in Tamil Nadu in the month of January 2007. Further, with the restructuring of its field force now complete, Cadila expects its domestic formulation business to grow at double-digit rates and outperform the industry as a whole.

Acquisition boosts consumer business

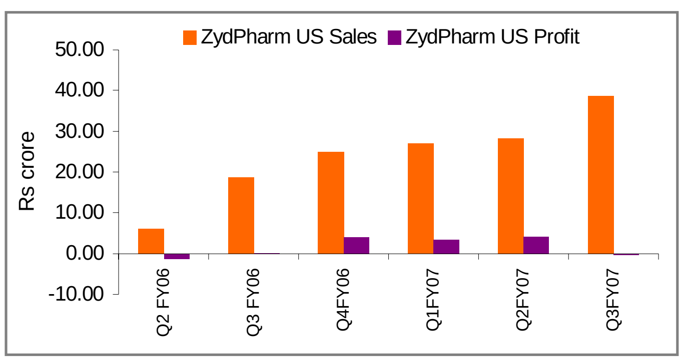
Cadila's consumer division recorded a robust growth of 59.2% yoy to Rs47.6 crore in Q3FY2007. The growth was largely powered by the acquisition of Carnation Nutralogue, which contributed Rs14.7 crore in revenues during the quarter. The company launched a new product, Nutralite, in Q3FY2006, on account of which the sales of this business spiked up in Q3FY2007. Going forward, Cadila expects its consumer business to grow at a more modest rate of 30%.

US generic business expands by 105.3%

Cadila's US subsidiary posted sales of Rs38.6 crore during the quarter, an increase of 105.3% yoy. At the net level, the subsidiary reported a loss of Rs0.3 crore. The loss was due to a Rs7.2-crore R&D cost paid by the subsidiary to its Indian parent. Excluding this, the subsidiary posted a profit of Rs6.8 crore during the quarter. The sales in the US market were driven by two new launches--Zonisamide capsules and Simvastatin tablets--during the quarter. The management has indicated that Cadila's market share for Simvastatin is in the double-digit range despite the entry of over eight players on day one of patent expiry which resulted in a 99%+ erosion of the huge $4.6-billion branded market.

Cadila has filed three ANDAs during the quarter, taking the total number of filings to 44. The company has so far received 18 approvals, including tentative approvals for Pravastatin, Sertraline and Levofloxacin. The company is expecting two more approvals in Q4FY2007. We expect Cadila's US operations to contribute significantly to its total sales going forward, on the back of a strong product pipeline.

US revenues on the rise

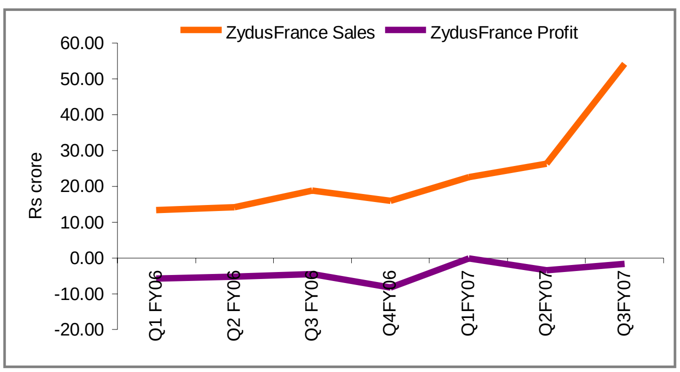


French subsidiary exhibits strong growth

Cadila's French subsidiary's sales were up by 188.3% yoy to Rs54.2 crore in the quarter. The strong growth was largely due to Zydus France's authorised generic deal with Bristol Myers Squibb for Pravastatin. Zydus France launched the authorised generic of Pravastatin in September 2006 in the French market. The product alone has contributed close to euro 2 million (approximately Rs12 crore). Further, the subsidiary also benefitted from the new government reform to reduce the discount to pharmacies by an additional 5% with effect from January 1, 2007. Due to this, the company generated strong sales in France in December 2006, as pharmacists stocked up their inventory prior to the coming into effect of the new regulation.

The management has indicated that Cadila's market share in France has improved from 0.3% in FY2006 to 1.6% currently. Going forward, the company expects its share to increase to 2.6%. It expects to continue growing at the rate of 70-80% yoy on the back of new product launches and a strong field force. Cadila's losses in France have tapered down as well, with the company reporting a loss of Rs1.6 crore during the quarter as compared with a loss of Rs4.5 crore in Q3FY2006. Cadila has filed for two additional site variation applications for its products with the French authorities. With the growing revenues and reducing costs, Cadila's French business is well on its way to breaking even.

Performance of Zydus France--growing revenues and reducing losses



Contributions from Altana JV dips

The revenues from Cadila's joint venture (JV) with Altana for the manufacture of Panteprazole intermediates dipped by 38% yoy and 115% sequentially to Rs9.6 crore in Q3FY2007. Even the profits generated out of the JV dipped to Rs7.3 crore during the quarter, although the JV continued to yield high margins of over 70%. The company has indicated that the dip in the sales was due to an upcoming inspection of the Altana plant in Germany by the US Food and Drug Administration. On account of the inspection the plant remained shut for a considerable period of time during the quarter. However, the company maintains that it is on track to meet its annual revenue target from the Altana JV.

High R&D costs and increased advertising expenses affect margins

Cadila's margins shrank by 200 basis points to 17.4% in Q3FY2007. The contraction in the margins was largely due to an 84.5% rise in the company's generic R&D expenses to Rs29.9 crore during the quarter and a one-time increase in the advertising expenses for its consumer business. On the other hand, the company's raw material cost and employee expenses remained under control during the quarter. The gross margin expanded by 140 basis points yoy to 64.4% during the quarter on account of an improved product and geographical mix. Consequently, Cadila's OP grew by 12.3% to Rs82.3 crore in Q3FY2007.

However, going forward, we expect the margins to bounce back to the 19-20% range as the high advertising expenses for the consumer business are non-recurring in nature.

Cost break-up Rs crore

Particulars	Q3FY07	Q3FY06	% change
Adjusted material cost	168.3	139.9	20.3
% of sales	*35.6*	*37.0*	
Employee expenses	51.9	49.5	4.8
% of sales	*11.0*	*13.1*	
R&D expenses	29.9	16.2	84.6
% of sales	*6.3*	*4.3*	
Other expenses	140.0	98.9	41.6
% of sales	*36.0*	*30.5*	

Revenue break-up Rs crore

Particulars	Q3FY07	Q3FY06	% change	M9FY07	M9FY06	% change
Domestic	313.8	286.8	9.4	991.2	906.2	9.4
Formulations	258.0	243.0	6.2	830.1	781.5	6.2
Branded formulations	237.7	218.8	8.6	237.7	218.8	8.6
Generic formulations	20.3	24.2	-16.1	20.3	24.2	-16.1
APIs	8.2	13.9	-41.0	29.4	37.4	-21.3
Consumer & others	47.6	29.9	59.2	131.7	87.3	50.8
Exports	167.7	100.1	67.5	436.1	251.4	73.5
Formulations	121.2	59.1	105.1	276.1	132.2	108.8
APIs	46.5	41.0	13.4	159.9	119.1	34.3
Total gross sales	**481.5**	**386.9**	**24.5**	**1427.2**	**1157.6**	**23.3**

Extraordinary income boosts profits

The adjusted PAT of the company grew by a whopping 66.4% to Rs69.5crore in Q3FY2007. The adjusted profits were significantly ahead of our estimates. However, this quantum leap in the profits was on account of a Rs16.9 crore one-time extraordinary income from the sale of the French branded business during the quarter. Adjusting for this one-time income, the reported net profit stood at Rs46.3 crore, up by 12.9% yoy. The lower interest and depreciation costs also aided the net profit. The earnings for the quarter stood at Rs3.7 per share.

Innovative R&D efforts progressing well

Through steady investments in R&D, Cadila has managed to create a robust innovative R&D pipeline for itself. The company has a pipeline of four molecules in various stages of development. Its lead molecule--ZYH1, an anti-obesity compound--is currently undergoing Phase-II clinical trials, which are expected to be completed by April 2007. The management has indicated that it intends to take all its innovative molecules up to Phase-II A trials on its own and thereafter outlicence them to global pharma companies for further development. Hence, we expect FY2008 to be a big year for Cadila, in terms of monetising its R&D pipeline.

Valuation & view

Though Cadila's Q3FY2007 performance has been supported largely by the extraordinary income, we believe the strong organic growth would drive the future operating and financial performance of the company. We expect the company to deliver a better than industry growth in the domestic market on the back of regular new product launches, strong brand building and improved field force productivity. Alongside, the US generic business of the company is on a strong footing with 44 product fillings with the USFDA (just eight are in the market and a total of 18 products have been approved). Also, a ramp-up in the contract manufacturing business and the turn-around of the French business would scale up the earnings visibility for Cadila.

At the current market price of Rs345, the company is trading at 14.7x of its FY2008 estimated earnings. With all the growth drivers in place, we maintain our Buy recommendation on Cadila with a price target of Rs425.

Valuation table (consolidated)

Particulars	FY04	FY05	FY06	FY07E	FY08E
Net sales (Rs cr)	1196.2	1243.0	1445.3	1729.4	2029.7
PAT (Rs cr)	133.2	119.9	152.4	226.8	293.8
Shares in issue (cr)	12.6	12.6	12.6	12.6	12.6
EPS (Rs)	10.6	9.5	12.1	18.1	23.4
PER (x)	32.5	36.1	28.4	19.1	14.7
cash EPS (Rs)	16.3	15.3	18.3	24.9	31.0
cash PER (x)	21.2	22.6	18.8	13.8	11.1
EV	4726.6	4666.4	4732.6	4839.6	4978.9
EV/Ebidta (x)	18.9	19.3	16.5	12.9	11.1

Cadila's innovative R&D pipeline

Compound	Therapeutic area	Use	Status	Remark
ZYH1	Metabolic disorders	Dyslipidemia	in Phase-II trials	to be completed by April 2007
ZYI1	Inflammatory disease	Inflammation & pain	Phase-I complete	With DGCI for Phase-II approval
ZYH2	Metabolic disorders	Diabetes	In Phase-I trials	to be completed by February 2007
ZYO1	Metabolic disorders	Obesity	Pre-clinical studies completed	With DGCI for Phase-I approval

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

Bharti Airtel

Apple Green

Stock Update

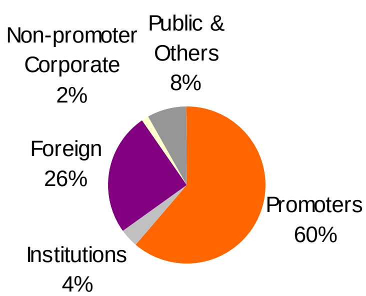
Price target revised to Rs820

Buy; CMP: Rs689

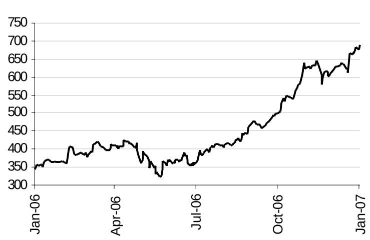
Company details

Price target:	Rs820
Market cap:	Rs130,634 cr
52 week high/low:	Rs700/310
NSE volume: (No of shares)	8.9 lakh
BSE code:	532454
NSE code:	BHARTIARTL
Sharekhan code:	BHARTI
Free float: (No of shares)	74.0 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	10.0	36.2	89.1	97.6
Relative to Sensex	4.8	21.9	33.7	30.6

Result highlights

- Bharti Airtel has announced a robust revenue growth of 12.8% quarter on quarter (qoq) and 62.4% year on year (yoy) to Rs4,912.9 crore for Q3FY2007. The sequential revenue growth was evenly driven by a 13.8% rise in the mobile revenues and a 12.4% growth in the non-mobile businesses.
- The company has positively surprised on the margin front, with a 170-basis-point sequential improvement in the operating profit margin (OPM) to 40.8%--one of the highest ever reported in any quarter. Consequently, the operating profit grew by 17.7% qoq and 81% yoy to Rs2,005 crore.
- In addition to the healthy growth in the operating profit, the earnings growth was also boosted by the foreign exchange fluctuation gains of Rs219.2 crore on the forward hedges (as compared with a marginal gain in Q2). Consequently, the consolidated earnings grew at an exponential rate of 30.1% qoq and 122.9% yoy to Rs1,215 crore, way ahead of the market expectations of around Rs1,070 crore.
- The other key highlights include the proposed acquisition of 100% stake in the submarine cable network from India to Singapore for a consideration of $110 million. The cable link is currently equally owned by SingTel and one of the Bharti group companies.
- The company introduced call card for international calls from the USA to India that would enable it to generate an alternate source of revenues from the 2.5 million strong non-resident Indian (NRI) community based in the USA. It also announced some new initiatives during the quarter, including the approval to launch wireless mobile (2G and 3G) services in Sri Lanka, a new venture to introduce direct-to-home (DTH) broadcasting services and a possible launch of (Internet Protocol) IP-based television channel distribution (IPTV) system after a successful testing in the National Capital Region (NCR).

Result table Rs (cr)

(Rs crore)	Q3FY07	Q3FY06	Q2FY07	% yoy	% qoq
Net sales	**4913.0**	**3026.0**	**4357.0**	**62.4**	**12.8**
Total expenditure	2908.0	1918.0	2654.0	51.6	9.6
Operating profit	2005.0	1108.0	1703.0	81.0	17.7
Other income	11.0	14.0	27.0	-22.4	-58.1
Interest (net)	-132.0	92.0	59.0	-	-
Depreciation	706.0	391.0	593.0	80.7	19.2
PBT	1441.0	639.0	1078.0	125.7	33.7
Tax	214.0	86.0	138.0	149.3	55.2
Minority interest	12.0	8.0	7.0	61.3	83.3
Net profit	**1215.0**	**545.0**	**934.0**	**122.9**	**30.1**
Equity	1894.0	1884.0	1892.0		
EPS	6.4	2.9	4.9		
Margins (%)					
OPM	40.8	36.6	39.1		
NPM	24.7	18.0	21.4		

- To factor in the better than expected performance, we have revised upwards our earnings estimates by 17% and 7.1% for FY2007 an FY2008 respectively.
- At the current market price the stock trades at 31x FY2007 and 22.2x FY2008 estimated earnings. We maintain our Buy call on the stock with a revised one-year price target of Rs820 (24x rolling four quarters forward earnings).

Mobile services

Robust subscriber addition drives growth in revenues

The sequential growth of 13.8% in the mobile revenues was driven primarily by the 18.2% sequential increase in the subscriber base to 32 million users. On the other hand, the average revenue per unit (ARPU) declined by 2.5% qoq to Rs427 per month but the drop was more or less offset by the sequential growth of 2.2% in the minutes of usage (traffic volumes).

Margin improves by 70 basis points

What is encouraging is that the OPM of the mobile business saw a healthy improvement of 70 basis points to 37.6%. This is the highest margin ever reported in any quarter. The company is benefiting from the improvement in the margins in the circles where the services were rolled out in the past four to six quarters. Moreover, the economies of scale are also boosting the overall margin.

Other highlights

The company added a record 4.9 million subscribers (or 24.7% of the all-India net additions) during the quarter. Consequently, its market share improved to 21.8%, up from 21.4% reported in Q2F2007.

The monthly churn continues to be in a manageable range of 3.5% (including the company initiated churn of 2.3%) in the post-paid segment and of 4.8% in the pre-paid segment.

The non-voice revenues as a percentage of the total mobile revenues increased marginally to 10.4%, up from 10.3% reported in Q2FY2007.

Non-mobile services

Revenue growth aided by increase in ARPUs

The sequential growth in the broadband and fixed-line telephony business was contributed by a 6.6% sequential growth in the subscriber base to 1.74 million users and an unexpected sequential improvement of 7.4% in the ARPU to Rs1,198 per month. The enterprise service business grew by 11.6% sequentially due to the healthy contribution from both the long distance (up 11.3% qoq) and corporate service (up 12.8% qoq) businesses.

Revenue break-up

(Rs crore)	Q3FY07	Q3FY06	Q2FY07	% yoy	% qoq
Non mobile services	1771	1174	1575	50.9	12.4
- Broadband & Tele	598	385	524	55.3	14.1
- Enterprise services	1173	818	1051	43.3	11.6

Margins look up in all segments

The sequential improvement of 390 basis points in the OPM of the non-mobile business was driven by the improvement of 660 basis points qoq in the margin of the broadband and fixed-line telephony service business and a 280-basis-point rise in the margin of the enterprise service business.

Margins firm up

(Rs crore)	Q3FY07	Q3FY06	Q2FY07	% yoy	% qoq
Non mobile	670.7	370.6	534.3	81.0	25.5
OPM(%)	37.9	31.6	33.9		
- Broadband & Tele	161.3	94.6	106.9	70.5	50.9
OPM(%)	27.0	24.5	20.4		
- Enterprise services	509.4	276.0	427.4	84.6	19.2
OPM (%)	43.4	33.7	40.7		

Going forward, the OPM of the enterprise service business (that includes the long distance telephony revenues) is expected to get positively affected by the acquisition of Network i2i, which owns the submarine cable link between India and Singapore (that is a key route for the link to the developed countries in the West including the USA and Europe). That's because the company currently has to pay certain charges to Network i2i for the usage of the international bandwidth for the international calls.

Revision of estimates

To factor in the better than expected performance, we have revised upwards our earnings estimates by 17% and 7.1% for FY2007 an FY2008 respectively.

Valuation

At the current market price the stock trades at 31x FY2007 and 22.2x FY2008 estimated earnings. We maintain our Buy call on the stock with a revised one-year price target of Rs820 (24x rolling four quarters' forward earnings).

Earnings table

Particulars	FY05	FY06	FY07E	FY08E
Net Profit (Rs cr)	1497.9	2257.6	4214.0	5894.6
No. of shares (crs)	185.3	189.4	189.6	189.8
EPS (Rs)	8.1	11.9	22.2	31.1
YoY change (%)	195.1	47.5	86.4	39.7
PER (x)	85.3	57.8	31.0	22.2
Price/BV (x)	20.9	14.2	9.7	6.8
EV/EBIDTA(x)	45.4	31.2	18.2	12.8
Market Cap/Sales	16.0	11.2	7.0	5.0
RoCE (%)	24.5	24.6	31.4	30.5
RoNW (%)	17.9	20.7	28.8	31.4

State Bank of India

Apple Green

Stock Update

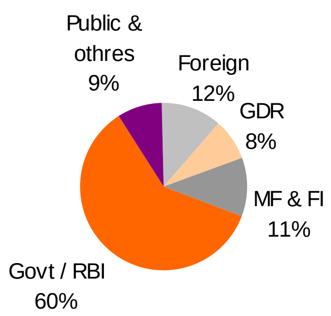
Sequential growth disappoints

Buy; CMP: Rs1,174

Company details

Price target:	Rs1,380
Market cap:	Rs61,788 cr
52 week high/low:	Rs1,379/684
NSE volume: (No of shares)	12.3 lakh
BSE code:	500112
NSE code:	SBIN
Sharekhan code:	SBI
Free float: (No of shares)	17.0 cr

Shareholding pattern



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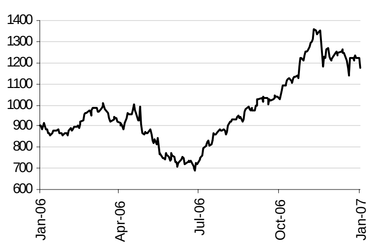


Price performance

(%)	1m	3m	6m	12m
Absolute	0.8	17.6	71.0	37.6
Relative to Sensex	-4.5	5.2	20.8	-9.1

Result highlights

- The Q3FY2007 results of State Bank of India (SBI) are below expectations with the bank's profit after tax (PAT) reporting a decline of 4.5% to Rs1,065 crore as against our estimate of Rs1,195 crore.
- The reported net interest income (NII) at Rs3,951 crore is slightly below our estimate of Rs4,034 crore. However the total other income at Rs1,811 crore is much above our expectation of Rs1,551 crore, mainly due to a higher than expected "Others" component in the "Other income" category. The operating expenses are in line with our expectations; however the provisions have risen more than expected, due to an unexpected investment depreciation. A higher than expected growth in the other income has offset the more than expected rise in the provisions to some extent, as it has actually reduced the gap between the actual PAT and the estimated PAT.
- The reported NII is down by 6.4% year on year (yoy) to Rs3,951.3 crore. However the third quarter saw many one-time items adjusted for which the NII growth stands at 33% yoy. But sequentially the NII has grown by only 1.4%.
- The other income is marginally down by 1.6% to Rs1,811 crore, however adjusted for the India Millennium Deposit (IMD) gains, the growth is strong at 38.3%. The core fee income is up 22.9% yoy and the trading income has risen by 139.3%; the same was expected as the bank planned to make up for the low trading income of Rs7.7 crore reported in Q2FY2007. Though the year-on-year (y-o-y) growth rates are good, the core fee income has seen a sequential growth of only 1.9%.
- The operating expenses are down 16% yoy, however adjusting for the voluntary retirement scheme (VRS), wage arrear and extra gratuity payments made to the tune of Rs641 crore, the growth in the operating expenses remains contained. The operating profit is up 9.8% yoy, however the core operating profit is up 27.3% yoy and 1% quarter on quarter (qoq).

Result table Rs (cr)

Particulars	Q3FY07	Q3FY06	% yoy chg	% qoq chg	9MFY07	9MFY06	% yoy chg
Net interest income	3,951.3	4,219.9	-6.4	1.4	11,734.1	12,081.1	-2.9
Other income	1,811.0	1,840.5	-1.6	26.3	5,008.3	4,711.7	6.3
Treasury income	*310.6*	*129.8*	*139.3*	-	*529.6*	*507.2*	*4.4*
Fee	*860.9*	*700.5*	*22.9*	*1.9*	*2,467.2*	*2,060.8*	*19.7*
Net income	5,762.4	6,060.4	-4.9	8.1	16,742.4	16,792.7	-0.3
Operating expenses	2,907.4	3,460.7	-16.0	1.7	8,577.5	8,770.7	-2.2
Operating profit	2,855.0	2,599.7	9.8	15.5	8,164.9	8,022.1	1.8
Core operating profit (excluding treasury and other income)	2,058.4	1,616.5	27.3	0.9	6,419.3	6,676.8	-3.9
Provisions & contingencies	1,166.2	469.8	148.2	71.2	3,129.5	3,053.9	2.5
PBT	1,688.8	2,129.8	-20.7	-5.7	5,035.4	4,968.1	1.4
Provision for taxes	623.7	1,014.7	-38.5	2.8	1,986.4	1,414.7	40.4
Net profit	1,065.1	1,115.2	-4.5	-10.1	3,049.0	3,553.4	-14.2

- The provisions and contingencies are up 148.2% yoy and 71.2% qoq to Rs1,166.2 crore. The provision base was lower in Q3FY2006 as there was a Rs102.6-crore write-back in the non-performing asset (NPA) provisions during the quarter. This coupled with the unexpected investment depreciation of around Rs158 crore in Q3FY2007 brought about the sharp rise in the total provisions.
- The adjusted numbers reflect a good core income growth on a y-o-y basis, however there has been no sequential improvement which is a cause for concern. With the deposit costs rising steadily and another interest rate hike looking imminent, the pressure on the margin going forward remains the key issue. Hence, the scrip may remain under pressure in the short term until there is more clarity on how the Reserve Bank of India (RBI) wants to tackle inflation as well as on the measures that the central bank may announce in the latest review of the monetary policy scheduled on January 31, 2007.

Adjusted NII growth at 33%, but remains flat sequentially

The adjusted NII growth at 33% looks strong mainly due to the improved net interest margin (NIM) on a y-o-y basis. The NIM was substantially lower for Q3FY2006 as the bank had to park its funds in very short-term low yielding investments to meet the IMD redemption. A better picture of the bank's performance emerges on carrying out a quarter-on-quarter (q-o-q) comparison. On comparing the bank's third quarter performance with its second quarter performance, we witness a 1.4% improvement in the NII and a 2.5% growth in the assets. Hence we can conclude that the NIM witnessed some pressure in the third quarter itself. The reported nine-month NIM at 3.29% and half-yearly NIM at 3.32% imply that the NIM declined slightly in Q3FY2007.

Yield analyis

Particulars	9MFY07	9MFY06	H1FY07
NIM	3.29	2.85*	3.32
Cost of deposits	4.57	4.52	4.51
Yield on advances	8.61	7.87	8.55

* excluding one-off items

Higher CASA ratio aided in containing deposit costs

The current and savings account (CASA) ratio has improved to 43.3% from 40.8% in Q3FY2006 and 42.6% in Q2FY2007, as the bank was able to keep higher floats through its large automated teller machine network and focus on salary accounts. Our calculated cost of deposits shows a seven-basis-point increase in the deposit cost on a sequential basis, which looks to be contained due to the higher CASA deposits. Term deposits have increased by 6.6% yoy compared with an 11.2% increase in the overall deposits to Rs404,352 crore. The growth appears to be low due to the bank's conscious strategy of not relying upon corporate bulk deposits to shore up its deposit growth. However, higher retail term deposit rates offered by the bank would slowly start reflecting in its performance in the coming quarters.

Yield on advances expected to improve sequentially after the PLR hike

The interest on the advances has grown by 37.5% yoy to Rs6,413.6 crore, while the gross advances have gone up by 26.9% yoy; this reflects the improvement in the yield on the advances. The average yield on the advances improved substantially to 8.49% in December 2006 from 7.67% in December 2005, reflecting the hikes in the prime lending rate (PLR). However, on a sequential basis, the same remained flat. The retail advances grew by 22.8% and now constitute 25.6% of the advances. Home loans reported a growth of 20.1% yoy and currently constitute 52.4% of the bank's retail portfolio. With the 50-basis-point hike in the PLR announced in the fag end of December 2006, the yields should further improve.

Adjusted other income was up 38.3%

Adjusted for the IMD gains of Rs531 crore (which is a one-off item), the other income growth is strong at 38.3% mainly due to a higher "Others" component in the non-interest income. The core fee income is up 22.9% yoy but the same is up only 1.9% sequentially. The trading income is up 139.3%, which was expected as the bank planned to make up for the low trading income of Rs7.7 crore reported for Q2FY2007.

Other income	Q3FY07	Q3FY06	% yoy	% qoq
Other income	1,811.0	1,840.5	-1.6	26.3
Treasury	310.6	129.8	139.3	-
Fee income	860.9	700.5	22.9	1.9
IMD	-	531.0	-	-
Forex income	114.1	112.2	1.7	7.0
Dividend	13.5	8.5	59.0	-0.5
Lease income	25.3	35.6	-28.9	-29.7
Others	486.6	322.9	50.7	14.4

Adjusted operating expenses show marginal increase

The operating expenses are down 16% yoy. However adjusting for the VRS, wage arrear and extra gratuity payments made to the tune of Rs641 crore in Q3FY2006, the operating expenses have grown by 3.1%. The staff expenses are up 7.8% yoy adjusted for the one-time charges. The other operating expenses have come down by

6.3% on a y-o-y basis and by 3% on a q-o-q basis. We feel lower core banking solution expenses have actually helped bring down the other expenses on a sequential basis.

Operating expenses	Q3FY07	Q3FY06	% yoy	% qoq
Staff expenses	2,029.7	2,524.1	-19.6	3.8
Other operating expenses	877.7	936.6	-6.3	-3.0
Total	2,907.4	3,460.7	-16.0	1.7

Provisions on the higher side, asset quality shows improvement

The provisions and contingencies are up 148.2% to Rs1,166.2 crore on a lower provision base of Q3FY2006, as there was a Rs102.6-crore write-back in the NPA provisions during Q3FY2006. However, on a sequential basis the provisions are up 71.2% as the NPA provisions have moved up to Rs410.6 crore from Rs116.1 crore in Q2FY2007. The NPAs are down to 1.45% from 1.67% on a sequential basis.

The provision for investment depreciation at Rs158 crore was unexpected as the amortisation expenses for the bank are around Rs500 crore. The increased provision could be on the marked-to-market book as has been seen in case of the other public sector banks like Canara Bank.

Provisions & Contingencies

	Q3FY07	Q3FY06
NPA	410.6	(102.6)
Amortisation	500.0	427.6
Investment deprecn	158.0	-
Std assets	130.0	140.0
Others	(32.9)	4.8
Total	**1,166.2**	**469.8**

SBI's consolidated Q3FY2007 performance

- NII is down 2% yoy to Rs5,684.5 crore
- Other income is up 39% to Rs3,302 crore
- Operating profit is up 13% to Rs4,139 crore
- PAT is up 4% to Rs1,524.4 crore.

Adjusted numbers remain strong on a y-o-y basis

The adjusted numbers reflect a good core income growth but the margin appears to have weakened slightly. With the deposit costs rising steadily and another interest rate hike looking imminent, the pressure on the margin going forward remains the key issue. However, the full effect of the 50-basis-point hike in the PLR announced in the fag end of 2006 will be felt in Q4FY2007 and hence the pressure on the costs would be mitigated to some extent.

Exceptional	Q3FY07	Q3FY06	% yoy chng
Reported NII	3,951.3	4,219.9	-6.4
Adjustments of which	-	1,254.0	9735.9
IT refund	-	954.0	5784.6
Write back of IMD provision	-	300.0	3951.3
Adjusted NII	3,951.3	2,965.9	33.2
Reported PPP	2,855.0	2,599.7	9.8
Adjustments	-	1,145.0	
Adjusted PPP	2,855.0	1,454.7	96.3
Reported PAT	1,065.1	1,115.2	-4.5
Adjusted PAT	1,065.1	397.5	168.0

Revision in FY2007 numbers

We have revised our FY2007 PAT numbers downwards by 3.2% to Rs4,594.7 from Rs4,740.9 crore earlier mainly due to expectations of a lower core fee income in Q4FY2007 and some pressure on NII growth. The other income has shown a robust growth in Q3FY2007 but a large part of it has come from the treasury and others, which continue to be volatile. Hence we have revised the FY2007 PAT numbers downwards by 3.2%. However, we have not changed our FY2008 estimates.

Valuation and view

The adjusted numbers reflect a good core income growth on a y-o-y basis. However there has been no sequential improvement which is a cause for concern. With the deposit costs rising steadily and another interest rate hike looking imminent, the pressure on the margin going forward remains the key issue. Hence, the scrip may remain under pressure in the short term until there is more clarity on how the RBI wants to tackle inflation as well as on the measures that the central bank may announce in the latest review of the monetary policy scheduled on January 31, 2007. At the current market price of Rs1,174, the stock is quoting at 11.4x its FY2008E earnings per share, 5.4x its FY2008E pre-provisioning profits and 1.2x FY2008E consolidated book value. We maintain our Buy recommendation on the stock with a twelve-month price target of Rs1,380.

Earnings table

Particulars	FY04	FY05	FY06	FY07E	FY08E
Net profit (Rs cr)	3681.0	4304.5	4406.7	4594.7	5880.0
Shares in issue (cr)	52.6	52.6	52.6	52.6	57.1
EPS (Rs)	69.9	81.8	83.7	87.3	102.9
% y-o-y change	*18.6*	*16.9*	*2.4*	*4.3*	*17.9*
PE (x)	16.8	14.4	14.0	13.4	11.4
P/PPP (x)	6.5	5.6	5.5	5.6	5.4
Book value	384.4	457.4	525.3	597.6	715.4
P/BV (x)	3.1	2.6	2.2	2.0	1.6
Adj book value	281.0	355.8	432.0	497.5	604.5
P/ABV (x)	4.2	3.3	2.7	2.4	1.9
RONW (%)	19.7	19.4	17.0	15.5	15.7
Consolidated BV	521.6	618.9	707.4	809.9	955.6
P/CBV (x)	2.3	1.9	1.7	1.4	1.2

Ceat

Ugly Duckling

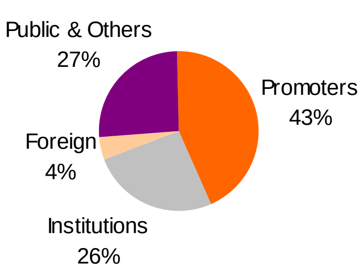
Stock Update

A brilliant performance

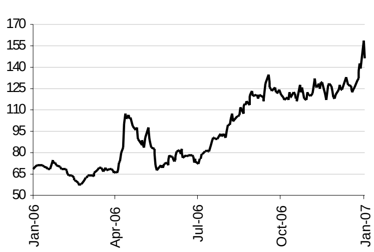
Buy; CMP: Rs146

Company details	
Price target:	Rs190
Market cap:	Rs667 cr
52 week high/low:	Rs162/56
NSE volume: (No of shares)	2.8 lakh
BSE code:	500878
NSE code:	CEAT
Sharekhan code:	CEAT
Free float: (No of shares)	2.6 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	31.6	29.2	114.0	129.9
Relative to Sensex	24.6	15.6	51.3	51.6

Result highlights

- Ceat's Q3FY2007 results are ahead of our expectations. The net sales have risen by a brilliant 30.7% to Rs536.7 crore on the back of a 14% tonnage growth and a very strong realisation growth. The sales to original equipment manufacturers (OEMs) have marked a significant improvement of 130% during the quarter whereas the replacement sales have continued to grow at a handsome pace of 25%.
- The operating profit margin (OPM) has expanded by 250 basis points to 7.3% as a result of a lower raw material cost during the quarter as well as avings in the manpower cost and the other overheads. With several price hikes effected in the last one year, the OEM business has also become a lot more profitable, leading to further margin improvement. As a result, the operating profit has grown by 98.3% to Rs39 crore.
- Stable interest and depreciation costs have helped the company to report a 665% growth in the net profit, which stands at Rs11.8 crore.
- Though the rising rubber prices are a concern, we are pretty confident of the pricing power of the tyre industry and expect another price hike from the tyre majors in the next two to three months.
- At the current market price of Rs146, the stock is trading at 9.4x its FY2008E earnings and at an enterprise value (EV)/earnings before interest, depreciation, tax and amortisation (EBIDTA) of 4.7x. We maintain our Buy recommendation on the sock with a price target of Rs190.

Result table Rs (cr)

Particulars	Q3FY07	Q3FY06	% yoy	9MFY07	9MFY06	% yoy
Net sales	536.7	410.7	30.7	1571.9	1263.1	24.5
Expenditure	497.7	391.0	27.3	1487.4	1219.4	22.0
RM consumed	361.4	302.3		1122.7	920.9	
Stock adjustment	7.7	-26.0		-17.8	-44.9	
Staff cost	32.5	30.3		96.2	89.9	
Other expenditure	96.1	84.4		286.3	253.5	
Operating profit	39.0	19.7	98.3	84.5	43.7	93.5
Other income	2.9	5.6		13.1	16.4	
EBIDTA	41.9	25.3	65.7	97.6	60.0	62.5
Interest	15.6	16.5		47.5	48.0	
PBDT	26.3	8.8		50.0	12.0	
Depreciation	7.8	5.7		23.2	16.7	
Profit before tax	18.5	3.1	492.0	26.9	-4.7	674.1
Tax	6.7	1.6		10.6	-0.3	
Profit after tax	11.8	1.5	664.9	16.3	-4.4	469.6
EPS	2.6	0.4		3.6	-1.0	
OPM (%)	7.3	4.8		5.4	3.5	
EBIDTA (%)	7.8	6.2		6.2	4.8	

Strong top line growth led by tonnage and realisation growth

The net sales for the quarter exceeded our expectations, growing by 30.7% to Rs536.7 crore. The strong growth was achieved on the back of a 14% tonnage growth and a strong realisation growth, as the tyre companies have resorted to significant price hikes in the last one year.

Sales break-up

	Q3FY07	Q3FY06	% change
Domestic	483.0	330.0	46.4
OEM	154.0	67.0	129.9
Replacement	329	263	25.1
Exports	117	125	-6.4
Total	600.0	455.0	31.9

During the quarter the OEM sales rose significantly, up a whopping 130% to Rs154 crore. With a number of price hikes taking place in the last one year (about 22% from the OEM segment), the profitability in the OEM segment improved considerably compared with the last year. Hence, we view the strong growth reported in the OEM segment in a very positive light. The growth in the replacement segment continued with a 25% growth reported during the quarter; the exports stood at Rs117 crore for the quarter.

Brilliant improvement in margins

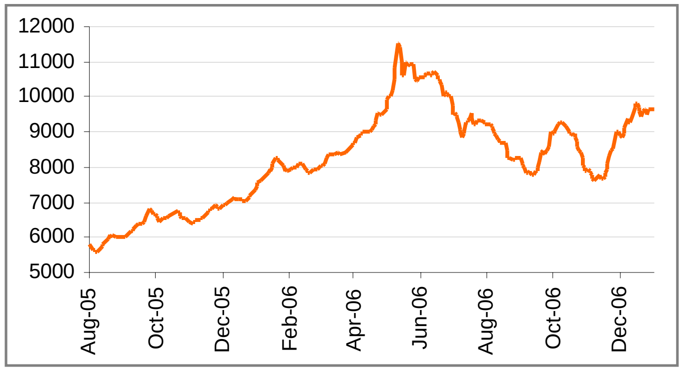
The OPM improved by 250 basis points and by 230 basis sequentially to 7.3%. An improvement in the product mix, a lower raw material cost, and huge savings in the employee cost and the other overheads led to this strong margin growth. Moreover, we believe that there is room for further improvement in the margins, considering the company's effortsto reduce its manpower cost, control its fuel cost by using a lower-cost fuel and improve its product mix in favour of speciality tyres, we believe that there is still some scope for margin improvement.

The other income for the quarter stood at Rs2.9 crore against Rs5.6 crore in Q3FY2006. The EBIDTA has marked a growth of 65.7% with EBIDTA margins improving to 7.8% against 6.2% last year. The repayment of debts further reduced the interest cost. Consequently, the net profit for the quarter rose by a whopping 665% to Rs11.8 crore.

Further rise in rubber prices should be offset with price hikes

After a fall from the peak levels of Rs115 per kilogram during May-June, rubber prices touched Rs76 in November 2006. The rubber prices have again marched up to Rs96 in recent times, mainly due to natural factors such as floods in Malaysia, law and order related problems in Thailand and climatic changes in Vietnam. However, the rise in the price of rubber has been partially offset by a fall in the prices of the other raw materials, particularly crude-linked materials. For instance, with crude coming down to $50 odd levels, the prices of carbon black and SBR are also on a downturn. In fact, carbon black prices have fallen by 8.5% w.e.f. January 1, 2007.

Rubber price movement



Though the rising rubber prices are a concern, we are pretty confident of the pricing power of the tyre industry and expect the tyre companies to raise prices again if the rubber prices harden further. We expect a price hike within the next two or three months, considering the current trend of rising rubber prices.

Land sale expected to be conducted by Q4

The management has also stated its intention to sell off part of the Bhandup property and the board approval to sell off seven acres of land has already been obtained. The sale, which weestimate would fetch about Rs70-80 crore (around Rs16 per share), is expected to be finalised in Q4FY2007.

Valuations and view

Considering the strong growth opportunities for Ceat (particularly in the specialty tyre segment), its strong performance in the last couple of quarters, improving productivity and the scope for improvement in its margins, we maintain our positive outlook on the stock.

Ceat has a huge investment portfolio with investments in many RPG group companies. Assuming a 75% discount to their current market prices, the valuation of these investments works out to Rs21 per share. We believe this provides a cushion to Ceat's valuations and could act as another trigger in case the company resorts to a hive off.

Particulars	Price (Rs)	Remark
Core business	171.2	At 11x FY2008 earnings
Investment value	21.1	At 75% discount to CMP
Fair value	192.3	

At the current market price of Rs147, the stock is trading at 9.4x its FY2008E earnings and an EV/EBIDTA of 4.7x. Considering the strong growth opportunities in the specialty tyre segment, improving productivity and expected growth in the margin of the company, we believe that the stock's valuations are very reasonable. We maintain our Buy recommendation on Ceat with a price target of Rs190.

Earnings table

Particulars	FY04	FY05	FY06	FY07E	FY08E
Net sales (Rs cr)	1407.2	1532.2	1744.1	2122.1	2458.9
Net profit (Rs cr)	14.1	-1.9	0.5	27.9	71.1
Shares in issue (cr)	3.5	3.5	4.6	4.6	4.6
EPS (Rs)	4.0	-0.5	0.1	6.1	15.6
% y-o-y growth				*5259.0*	*155.0*
PER (x)	53.0	-294.9	845.4	24.0	9.4
Book value (Rs)	178.0	179.5	76.4	81.6	96.3
P/BV	0.8	0.8	1.9	1.8	1.5
EV/EBITDA	25.2	15.5	11.8	7.6	4.7
Mcap/Sales	0.4	0.3	0.4	0.3	0.3
ROCE (%)	9.4	6.4	8.4	12.3	21.9
RONW (%)	1.5	-0.3	0.2	7.5	16.2

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

ORG Informatics

Emerging Star

Stock Update

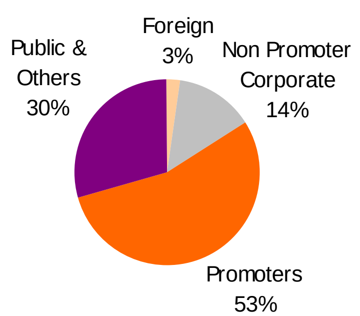
Maintains growth momentum

Buy; CMP: Rs172

Company details

Price target:	Rs190
Market cap:	Rs251 cr
52 week high/low:	Rs209/70
BSE volume: (No of shares)	88,398
BSE code:	517195
Sharekhan code:	SARAELE
Free float: (No of shares)	0.67 cr

Shareholding pattern



Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	6.7	48.1	124	6.3
Relative to Sensex	1.1	32.6	58.3	-29.3

Result highlights

- ORG Infomatics (ORG) reported a 273.5% growth in its net revenues to Rs108.5 crore during the third quarter ended December 2006. The revenue growth was driven by the execution of some its large orders, especially the Mahanagar Telephone Nigam Ltd (MTNL) order.
- The operating profit margin (OPM) declined by 190 basis points to 8.4% as the initial part of the MTNL order involves low-margin hardware supplies.
- However, the jump in the other income (that included a one-time gain of Rs0.8 crore from the sale of assets) aided the overall growth in the earnings. Consequently, the consolidated earnings grew by 70.6% to Rs5.2 crore during the quarter, which is ahead of our expectation of Rs4.6 crore.
- The fresh order intake continues to be robust and the company has been able to maintain the pending order position of around Rs600 crore (marginally lower than Rs625 crore reported in September 2006). The management also indicated that it is pursuing some more large-sized orders and expects to close one to two large orders in the coming months.
- Along with the results the company has also announced the acquisition of 100% sake in the Bangalore-based TechUnified Pvt Ltd (UT) for a total consideration of Rs49 crore (partly paid through issue of 8.93 lakh shares at a price of Rs181 per share). UT is a profitable company at the net level and is expected to report net profit of around Rs7 crore in the current fiscal. It offers wireless, speech and e-Business solutions to financial companies and telecom operators. This is the second acquisition in the month as the company had recently announced the acquisition of a 100% stake in DGIT Solutions.

Result table Rs (cr)

Particulars	Q3FY07	Q3FY06	% yoy chg
Net sales	108.5	29.0	273.5
Total expenditure	99.4	26.0	281.5
Operating profit	9.1	3.0	203.6
Other income	1.5	0.0	4865.8
Interest	0.9	0.2	361.4
Depreciation	0.7	0.3	157.4
PBT	9.0	2.6	248.9
Tax	3.2	0.6	444.2
Deferred tax	0.5	-1.0	-
RPAT	5.3	3.0	73.9
Extraordinary items	-0.1	0.0	-
Net profit	**5.2**	**3.0**	**70.6**
Equity	14.6	11.7	
EPS	3.5	2.6	
Margins (%)			
OPM	8.4	10.3	
NPM	4.8	10.4	

- At the current market price the stock trades at 17x FY2007 and 11.7x FY2008 estimated earnings. The estimates do not include the impact of the acquisitions as details of the same are awaited. However, the equity dilution has already been factored in the calculation of the earnings per share (EPS). We maintain our Buy recommendation on the stock with a price target of Rs190 (10x rolling four quarters forward earnings).

Revenue growth in line with our estimates

The revenue growth of 273.5% was driven purely by the growth in the telecom segment that includes the execution of the MTNL order. On the other hand, the revenues from the system integration (SI) and software service businesses have largely remained flat for the past few quarters.

Revenue break-up

(Rs crore)	Q3FY07	Q3FY06	YoY (%)
SI/software services	4.1	4.1	0.9
Telecom	104.4	25.0	318.0

The growth momentum is expected to continue in the coming quarters on the back of the company's healthy order book position. The pending order backlog stood at around Rs600 crore (marginally down from Rs625 crore in September 2006) despite the huge revenue booking during the quarter. What's more, the management indicated that it is pursuing some large-sized deals and expects to close some of them in the coming months.

Margins hit by higher proportion of low-margin hardware supplies

The OPM declined by 190 basis points yoy and 245 basis points qoq due to the shift in the revenue mix towards low-margin hardware supplies as part of the execution of the MTNL order. The company expects the margin to normalise back to the 10-11% range over the next two quarters. It had shown close to double-digit OPM in the previous four quarters.

Inorganic initiatives

The company has announced two acquisitions in the current month. It strengthened the delivery capabilities and geographical footprint by acquiring 100% stake in the Singapore-based DGIT for an all cash deal of around $1 million. DGIT has a strong consulting and enterprise solutions business. Moreover, it has established client relationship in the Far East and Asean countries.

It is followed by the acquisition of 100% stake in Bangalore-based UT that has reasonably successful software product and solution offerings for the financial companies and telecom operators. UT is a fast-growing and profitable company with a reputed client base including names like Reuters, Siemens, CitiBank and Bank Albhad. ORG proposes to fund the second acquisition through a cash-cum-share swap deal that would result in equity dilution by 8.9 lakh shares.

The two acquisitions would result in a cash outgo of around Rs37 crore and would utilise the bulk of the proceeds from the recent global depository receipt issue.

Revision of estimates

In view of the higher than expected performance, we are revising upwards the earnings estimates by 7.8% and 3.3% for FY2007 and FY2008 respectively. However, the EPS estimates would get revised upwards by 6.3% and 1.3% for FY2007 and FY2008 respectively, due to the dilution of equity as part of the consideration paid for the recent acquisition.

Valuation

At the current market price the stock trades at 17x FY2007 and 11.7x FY2008 estimated earnings. We maintain our Buy recommendation on the stock with a price target of Rs190 (10x rolling four quarters forward earnings).

Earnings table

Particulars	FY05	FY06	FY07E	FY08E
Net sales (Rs cr)	85.5	155.2	331.5	426.2
Net profit (Rs cr)	2.7	8.1	17.7	25.7
No of shares (cr)	1.1	1.4	1.8	1.8
EPS (Rs)	2.4	5.9	10.1	14.7
% y-o-y change	*33.1*	*146.2*	*70.7*	*45.5*
PER (x)	71.6	29.1	17.0	11.7
Price/BV (x)	17.2	7.7	3.0	2.2
EV/EBIDTA (x)	34.5	15.0	8.8	7.2
RoCE (%)	0.0	0.0	0.0	0.0
RoNW (%)	18.7	37.5	39.0	30.9

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

Universal Cables

Ugly Duckling

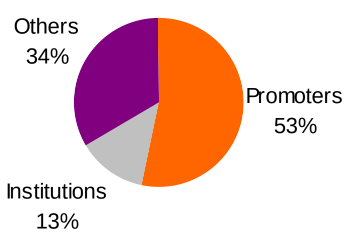
Stock Update

Capacity expansion to drive revenue growth

Buy; CMP: Rs115

Company details	
Price target:	Rs179
Market cap:	Rs266 cr
52 week high/low:	Rs139/61
NSE volume: (No of shares)	12,263
BSE code:	504212
NSE code:	UNIVCABLES
Sharekhan code:	UNCABLES
Free float: (No of shares)	1.1 cr

Shareholding pattern



Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	16.7	2.6	33.5	-1.6
Relative to Sensex	10.5	-8.1	-5.7	-35.0

Result highlights

- The net sales of Universal Cables Ltd (UCL) grew by 25% and the growth is in line with our expectations. However the net profit growth of 10.6% is slightly below our expectations on account of a higher than expected increase in the other expenses.
- The net sales for the quarter grew by 25% to Rs87.64 crore. The power cable business grew by 22% to Rs81.66 crore, the capacitors business grew by 9% to Rs3.41 crore and the telephone cable sales stood at Rs2.60 crore against nil in the corresponding quarter of the previous year.
- The operating profit margin (OPM) for the quarter declined by 211 basis points to 9.32% as the other expenses to sales ratio increased to 17.09% from 14.60% last year. Hence the operating profit for the quarter grew by just 1.62% to Rs8.17 crore.
- Going forward, we expect the OPM to improve, as the company focuses on the high-end products that have better margins and as its 100% subsidiary, Optic Fibre Goa Ltd (OFGL), turns profitable. The segmental losses from the telephone cable division stood at Rs0.33 crore in this quarter as against Rs0.79 crore in the previous quarter.
- The interest expense for the quarter increased by 48% to Rs1.54 crore, while the depreciation cost for the quarter increased by 81% to Rs1.92 crore.
- Consequently the net profit growth was lower at 10.6% to Rs5 crore.
- At the current market price of Rs115, the stock is quoting at 8.7x its FY2008E earnings per share (EPS) and 5.2x its FY2008E enterprise value (EV)/earnings before interest, depreciation, tax and amortisation (EBIDTA). We maintain our Buy recommendation on the stock with a price target of Rs179.

Result table Rs (cr)

Particulars	Q3FY07	Q3FY06	% yoy	9MFY07	9MFY06	% yoy
Net sales	87.6	70.3	24.7	263.2	218.4	20.5
Total expenditure	79.5	62.3	27.7	233.7	191.0	22.3
Operating profit	8.2	8.0	1.6	29.5	27.3	8.0
Other income	3.1	1.1	191.5	5.5	3.1	76.9
EBIDTA	11.3	9.1	23.7	35.0	30.5	15.0
Interest	1.5	1.0	-	4.9	3.8	-
Depreciation	1.9	1.1	81.1	5.1	3.5	44.8
PBT	7.8	7.0	11.4	25.1	23.1	8.6
Tax	2.8	2.5	12.9	8.8	8.1	7.9
PAT	5.0	4.5	10.6	16.3	15.0	9.0
Extraordinary items	0.0	0.0	-	0.0	0.0	-
Reported PAT	5.0	4.5	10.6	16.3	15.0	9.0
EPS	2.2	2.0	10.6	7.0	6.5	9.0
Margins						
OPM (%)	9.3	11.4		11.2	12.5	
PATM (%)	5.7	6.4		6.2	6.8	

Segment results

	Q3FY07	Q3FY06	% yoy chg	9MFY07	9MFY06	% yoy chg
Segment revenue						
Power cables	81.66	67.16	21.6	247.68	207.39	19.4
Capacitors	3.41	3.13	8.9	10.85	9.13	18.8
Telephone cables	2.60	0.00	-	4.83	1.87	158.3
PBIT						
Power cables	9.03	7.42	21.7	28.70	24.78	15.8
Capacitors	0.48	0.59	-18.6	1.70	2.34	-27.4
Telephone cables	-0.33	0.00	-	-1.12	-0.40	180.0
PBIT margin (%)						
Power cables	11.06	11.05		11.59	11.95	
Capacitors	14.08	18.85		15.67	25.63	
Telephone cables	-12.69	-		-23.19	-21.39	

Expansion plans to start contributing to revenues from Q1FY2008

Due to the government's thrust on the power generation sector and the capital expenditure (capex) plans of India Inc, the demand for cables is on the rise. To take advantage of the growth opportunity the company is implementing a capital expansion plan at a cost of Rs64 crore. As part of this plan, it will double the capacity of medium-tension cables and put up a new capacity for extra high-tension (EHT) cables (>220 KV). This capacity expansion is expected to contribute to the revenues from Q1FY2008.

After the capacity expansion, UCL will be the only player in India to produce EHT cables 9>220 KV) other than Cable Corporation of India. This will help the company to improve its OPM, as with its entry into the EHT segment, UCL will slowly reduce its presence in the low-tension cable segment, which is cluttered with too many players.

New product development to drive revenue growth of telecom cable segment

High investment in the telecom segment to provide the last-mile connectivity to users is resulting in a higher demand for optical fibre. UCL through its 100% subsidiary OFGL is making continuous efforts to develop new variants of the conventional single mode optical fibre; this would also lead to better value addition.

The company has successfully developed a newer version of fibre known as low water peak optical fibre (G-652D) with its in-house expertise. It has also taken necessary approvals to supply this fibre to most of the customers in India. We expect the new product development and the addition of G-652D grade fibre to the product range to help the company in turning around the performance of this division. That the turn-around has already begun is reflected in the division's third quarter results, wherein its losses are down to Rs0.33 crore from Rs0.79 crore in the previous quarter.

Valuation and view

We expect UCL's return ratios to improve considerably over FY2006-08E as the return on capital employed improves from 18.1% to 20.2% and the return on net worth improves from 11.9% to 16.4%. Also the company's focus on high-end products and OFGL's turn-around would improve the OPM further. At the current market price of Rs115, the stock is quoting at 8.7x its FY2008E EPS and 5.2x its FY2008E EV/EBIDTA. We maintain our Buy recommendation on the stock with a price target of Rs179, valuing its core business at Rs144 (11x FY2008E EPS) and investments at Rs34 (at 40% discount to the current market price).

Earnings table

Particulars	FY05	FY06	FY07E	FY08E
Net sales (Rs crore)	195.8	297.5	345.0	472.6
Net profit (Rs crore)	3.9	16.6	21.6	30.5
Shares in issue (crore)	2.0	2.0	2.3	2.3
EPS (Rs)	2.2	8.6	9.3	13.1
% y-o-y change	-	*295.8*	*9.0*	*40.9*
PER (x)	53.2	13.4	12.3	8.7
Book value (Rs)	46.6	70.7	68.4	79.2
P/BV (x)	2.5	1.6	1.7	1.5
EV/EBIDTA (x)	16.7	6.5	7.7	5.2
EV/Sales (x)	1.3	0.9	1.0	0.8
Dividend yield (%)	0.9	1.7	1.7	1.7
RoCE (%)	8.3	18.1	15.9	20.2
RoNW (%)	4.5	11.9	13.5	16.4

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

Zee Entertainment Enterprises

Viewpoint

Blow-out performance

CMP: Rs316

Zee Entertainment Enterprises Ltd (ZEEL) declared its first set of quarterly numbers after its incorporation on demerger of the erstwhile Zee Telefilms Ltd (ZTL). As of now ZEEL comprises ZTL's global broadcasting business and direct-to-home (DTH) business. Post-formation of Dish TV India Ltd (Dish TV; likely to be listed in February 2007) the DTH business will be allocated to the new company, leaving ZEEL with the broadcasting operations. Thus the results for Q3FY2007 include the performance of these two revenue streams.

Blow-out performance

ZEEL delivered an excellent set of numbers with the revenues growing by 53% year on year (yoy) to Rs417.7 crore and profit after tax (PAT) rising by a robust 177.6%. This stunning growth in the net profit comes on the back of a huge jump of 1,510 basis points in the operating profit margin (OPM) which led to a 186% growth in the operating profit. An increase in the other income and reduction in the finance cost added another Rs4.2 crore and Rs3.8 crore respectively to the bottom line. However the tax incidence was higher at 30.3% of the profit before tax (PBT) against 19.6% in Q3FY2006, which subdued the outstanding performance a bit.

Results table

Particulars	Q3FY07	Q3FY06	% y-oy change
Total revenue	417.7	272.9	53.0
Total expenditure	282.0	225.5	25.0
Operating profit	135.7	47.4	186.3
Other income	15.5	11.3	37.1
Depreciation	6.9	5.2	33.3
Finance cost	6.8	10.6	-35.9
PBT	137.5	42.9	220.4
Tax	41.7	8.4	396.2
PAT	**95.8**	**34.5**	**177.6**
Revenue break-up			
Advertising	210.54	132.4	59.0
Subscription	195.6	126.2	55.0
Other sales & services	11.6	14.3	-19.2

Ad revenue growth mirrors improved ratings and rate hikes

ZEEL has been continuously investing in content improvement over the last few quarters which led to the bleeding of its financials in the short term. This resulted in improved viewership and ratings. Monetising these the company increased the ad rates at the beginning of the financial year, which together with the better utilisation of the ad inventory led to a 35.6% year-on-year growth in the ad revenues to ~Rs180 crore. During the quarter, ZEEL acquired a 50% stake in Taj TV that owns and operates the sports channel *Ten Sports*. The consolidation of *Ten Sports* added another Rs31 crore to the ad revenues, causing the total ad revenues to grow by 59% yoy.

Subscription revenues zoom

Even before the subscription revenues could get a push on the implementation of the conditional access system (CAS) in the southern parts of the three metros of Mumbai, Delhi and Kolkata, ZEEL kicked in a handsome growth of 55% in its subscription revenues. Digitisation of cable, revenues from DTH (~Rs15 crore) and a contribution of Rs9.8 crore from the consolidation of Taj TV were the factors that brought about a robust growth in the subscription revenues.

Growth drivers

- The implementation of CAS that would lead to the digitisation of cable is expected to be a big boost for the subscription revenues of broadcasters, as this would curb the under declaration of subscriber numbers (estimated at ~85-90%) by local cable operators. The expansion of alternative distribution platforms such as DTH and Internet Protocol TV would also add substantially to the subscription revenues of the broadcasters in general.

- We view its distribution businesses, DTH and Siticable (now separately listed as WWIL), as major growth drivers going forward. Its DTH business, Dish TV, is adding 30,000 subscribers a week and currently has ~2 million subscribers. With the company targeting 8 million subscribers by 2011 and the improvement in the average revenue per user, the future looks impressive for this business. To give impetus to these ventures and meet the growing fund requirements the management has hinted at roping in strategic/financial investors.

- ZEEL's financials have been affected by the losses from its new ventures such as Zee Smile and Zee Sports (Zee Sports had revenues of Rs61 crore and a loss of Rs7 crore for Q3FY2007). As these ventures mature and break even, the combined profitability of ZEEL will improve substantially.

Valuations and view

We value the broadcasting business of ZEEL at Rs266 per share (28x FY2008E EPS) and the DTH business at Rs85 per share ($250 per subscriber). That gives us a sum-of-parts valuation of Rs351 per share.

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Cement

Sector Update

Import duty on cement slashed to zero

With the headline inflation crossing 6%, the government has slashed the customs duty on cement, various raw materials and capital goods to check inflationary pressures. The changes in the duty structure would come into effect immediately. The duty cut comes as no surprise for the cement sector as cement prices have risen unabated in the last one year.

Imported cement price would come down by Rs26 per bag

Before the cut in the customs duty, the landed price of imported cement stood at close to Rs284 per bag (CIF value of USD80). With the duty cut, the landed price of cement is expected to come down by Rs26 per bag.

Landed cost of imported cement

	Pre-duty cut	Post-duty cut
CIF	80	80
USD	45	45
In Rs	3600	3600
Clearing charges	125	125
C&F per tonne	3725	3725
Customs duty @ 12.5%	465.63	0
CVD per tonne	408	408
Landed cost per tonne	4598.63	4133.00
VAT @ 12.5%	574.83	516.63
Secondary freight	500	500
Total	5673.45	5149.63
Price per bag	283.67	257.48

Impact to be muted…

Though on the face of it the duty cut appears to be negative for the industry, the ground realties present a different picture. As seen above, the landed cost of bulk cement would result in a 25% premium to the current national average price of Rs205 per bag. Also it will not be an easy ride for cement importers due to the infrastructure bottlenecks associated with the packing and unloading of imported cement. Except for certain coastal-based projects, the use of imported cement will be unviable due to the high freight costs attached to the transport of cement over a long distance.

City	WP per bag	Landed Cost	Premium
Mumbai	220	254	15%
Chennai	185	254	37%
Hyderabad	170	254	49%
Jaipur	175	254	45%
Delhi	195	254	30%

* WP - Wholesale Price

Also there are few countries from whom we could import cement, like China, Indonesia and Thailand. Also, whether imports from these countries would be possible would depend on the way the demand-supply situation pans out in these countries.

…but pace of price hike expected to slow down

The price of imported cement acts a reference point for the domestic cement producers. Now with the import prices expected to come down, the domestic cement producers would be cautious in raising their prices. This coupled with the fact that the industry will start witnessing capacity additions going ahead will weaken the pricing power of the cement companies.

Duty cuts on raw materials will positively affect the sector

The government is planning to cut the excise duty on diesel by Rs1. It is also contemplating reducing the excise duty on cement from the existing Rs408 per tonne. Any such move would be positive for the cement companies.

We maintain our FY2008 estimates

We believe the duty cut will not have any major impact on the cement industry in the near future. Moreover, our pricing assumptions for the cement companies are conservative. Hence, we maintain our earnings estimates for FY2008.

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