sharekhan
top picks

Sharekhan top picks

On March 3, 2006 we had recommended the best 12 of our Stock Ideas as Sharekhan Top Picks. As on April 5, 2006, this basket of stocks has given a return of 12% as against the 11% returns given by the Sensex' constituents over the same period. We have outperformed the Sensex yet again. We believe there is a lot of steam left in the market and you still have an opportunity to add good stocks to your portfolio. However, selectivity remains the key.

In continuation with our tradition, we are giving our best 12 Stock Ideas in today's market as Sharekhan Top Picks. The portfolio has been reshuffled to replace Infosys Technologies, Lupin and Mahindra & Mahindra with Satyam Computers, Cadila Heathcare and Tata Motors.

So go shopping!!!!

Name	CMP* (Rs)	PER			RoE (%)			Target price	Upside (%)
		FY05	FY06E	FY07E	FY05	FY06E	FY07E		
Bajaj Auto	2825.0	35.7	25.8	21.6	14.9	18.8	19.8	3500.0	24%
Bharat Heavy Electricals	2382.0	61.2	37.9	25.3	15.5	21.4	26.2	2650.0	11%
Godrej Consumer Products	769.9	52.4	37.7	31.7	166.8	125.9	85.4	912.0	18%
Satyam Computers	815.9	36.6	26.8	20.7	23.3	25.7	25.9	900.0	10%
ITC	200.7	40.7	31.9	28.3	26.3	25.4	24.6	220.0	10%
Cadila Healthcare	691.0	36.8	26.6	19.1	19.9	21.6	23.1	850.0	23%
Tata Motors	924.0	27.1	25.5	21.3	26.9	25.4	23.8	1004.0	9%
Orchid Chemicals	376.0	117.5	30.1	18.1	6.6	8.1	12.9	460.0	22%
Sanghavi Movers	774.5	41.2	16.4	12.4	23.8	31.9	33.6	800.0	3%
Shree Cement	985.0	31.5	26.9	18.3	46.1	35.6	34.8	1100.0	12%
SKF India*	312.5	25.0	20.2	14.1	22.1	22.3	25.7	406.0	30%
UltraTech Cement	715.1	3575.5	55.4	27.2	9.3	16.9	23.5	850.0	19%

*CMP as on April 07, 2006
**Calendar year ending

Name	CMP	PER			RoE (%)			Target	Upside
	(Rs)	FY05	FY06E	FY07E	FY05	FY06E	FY07E	price	(%)
Bajaj Auto	**2825.0**	35.7	25.8	21.6	14.9	18.8	19.8	**3500.0**	24%

Remarks:

- With the help of new product launches over the last few years, Bajaj Auto Ltd (BAL) is well poised to take advantage of the secular growth in the two-wheeler market. BAL is likely to consolidate its position in the market further as the new product launches continue.
- The three-wheeler segment, which is a high-margin business, is turning around after a brief lull. The changes in the regulatory regime in favour of vehicles using cleaner fuel is likely to boost the demand for three-wheelers where BAL is the undisputed leader.
- With the increased contribution of high-margin vehicles and the softening of the prices of steel, BAL is expected to see a 20% compounded annual growth in its earnings over FY2005-07E.
- The stock is currently quoting at a PER of 19.8x its FY2007E earnings. The investment on the company's books (Rs648 per share) and the insurance subsidiaries (Rs920 per share) add substantial value to BAL's fair value.

Name	CMP	FY05	FY06E	FY07E	FY05	FY06E	FY07E	Target price	Upside (%)
BHEL	**2382.0**	61.2	37.9	25.3	15.5	21.4	26.2	**2650.0**	11%

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 Rs37,500 crore, ie 3.0x its FY2005 revenue, provides high earnings visibility. .
- The power ministry has proposed around five ultra mega power projects entailing a capacity addition of 20,000MW (4,000MW x 5) with the combined turnkey value of at least Rs80,000 crore.
- BHEL's recent technology transfer agreement with Alstom for design and manufacture of large-sized (500MW+) super-critical boilers will enable it to bid for the ultra mega power projects. We expect BHEL to bag a fair share 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 21.4x its FY2007E earnings. BHEL's valuation looks attractive as compared with that of its peers, such as Siemens, ABB and Larsen and Toubro.

Name	CMP	FY05	FY06E	FY07E	FY05	FY06E	FY07E	Target price	Upside (%)
Godrej Consumer	**769.9**	52.4	37.7	31.7	166.8	125.9	85.4	**912.0**	18%

Remarks:

- Godrej Consumer Products Ltd (GCPL) is a big beneficiary of the expected consumption boom in India. A rising proportion of the middle-income families will translate into a strong demand for its products like soaps, hair colours and toiletries.
- The market share gains in the soap business through the consolidation of brands (Godrej No 1) and the launch of new products will lead to a robust growth, outpacing the growth in the soap market.
- The hair colour segment offers huge opportunity owing to its under-penetration and a strong 16-20% compounded annual growth rate (CAGR). GCPL with its dominant market share and a quality product basket should reap handsome gains.
- Cash flows are expected to grow at a CAGR of 22% in the FY2005-08 period; the same will be deployed in purchasing growth by augmenting capacities and through inorganic growth aspirations.
- GCPL trades at a PER of 31.7x its FY2007E earnings in view of the inorganic growth triggers and the shareholders' value maximising strategy.

Name	CMP	PER			RoE (%)			Target	Upside
	(Rs)	FY05	FY06E	FY07E	FY05	FY06E	FY07E	price	(%)
Satyam Computers	**815.9**	36.6	26.8	20.7	23.3	25.7	25.9	**900.0**	10%

Remarks:

- Unlike some of its front-line peers, Satyam has shown a healthy and consistent sequential growth over the past six to eight quarters.
- Despite the continued losses of its subsidiaries and the other cost pressures, the company's top line growth has been accompanied by stability in profitability.
- It has levers to support its profitability like the turn-around in its subsidiaries, the broadening employee base, an increasing offshore contribution etc which would limit any downside to its profitability.
- It is ahead of some of its peers in terms of bagging business in the recently announced large outsourcing deals.
- It trades at attractive valuations of 20.7x its FY2007E earnings, which is still at a considerable discount to some of its peers.

Name	CMP	PER FY05	PER FY06E	PER FY07E	RoE FY05	RoE FY06E	RoE FY07E	Target price	Upside
ITC	**200.7**	40.7	31.9	28.3	26.3	25.4	24.6	**220.0**	10%

Remarks:

- ITC is the undisputed market leader in the cigarette business in India. Over the years ITC has gained substantial pricing power in the market and has been posting a good volume growth in the business.
- ITC has diversified its revenue stream by successfully channelising the huge cash flows generated from the cigarette business into new and upcoming businesses like hotels, fast moving consumer goods (FMCG), paperboards and agri-marketing.
- ITC's huge investment in these businesses has now started reflecting in a robust growth in the revenues as the profits.
- ITC's venture into agri-marketing through e-Choupal is now set to replicate the urban mall mania in rural areas through Choupal Sagar. Choupal Sagar is expected to be a major revenue and profit driver for ITC over the long term.
- With an earnings CAGR of 23.4% over FY2005-07E the stock is attractively quoting at a PER of 28.3x its FY2007E earnings.

Name	CMP	PER FY05	PER FY06E	PER FY07E	RoE FY05	RoE FY06E	RoE FY07E	Target price	Upside
Cadila Healthcare	**691.0**	36.8	26.6	19.1	19.9	21.6	23.1	**850.0**	23%

Remarks:

- A strong research-based, integrated pharma player, Cadila is now spreading its wings to the high-margin regulated markets. It has a strong research and product pipeline with 30 products expected to receive generic approval by FY2007.
- Cadila is ranked number five in the domestic formulation business. It plans to introduce over 40 products in the Indian market in the next two years.
- Cadila has subsidiaries in France, the USA and Brazil, and these were making losses until FY2005. We expect these subsidiaries to collectively make a profit of over Rs32 crore in FY2008 as compared with a loss of over Rs30 crore in FY2005.
- We expect Cadila's earnings to grow at a CAGR of 38.6 % over FY2005-07E. The stock is trading at a PER of 19.1x FY2007E earnings.

Name	CMP	PER			RoE (%)			Target	Upside
	(Rs)	FY05	FY06E	FY07E	FY05	FY06E	FY07E	price	(%)
Tata Motors	**924.0**	27.1	25.5	21.3	26.9	25.4	23.8	**1004.0**	9%

Remarks:

- The commercial vehicle segment has seen a revival in its fortunes with the Supreme Court ban on overloading and improvement in economic activity. Tata Motors (TAMO) with its strong product range is poised to drive this growth. TAMO is expected to introduce products from the Daewoo stable and further consolidate its positioning in the market.
- The passenger vehicle segment is also expected to grow in double-digits after the reduction in the excise duty on small cars in the budget. The distribution tie-up with FIAT should also help TAMO in showcasing a wider product portfolio.
- Strong earnings growth in subsidiaries like Tata Daewoo, Tata Technologies, Telcon etc and a strong possibility of value unlocking in HV Axles and HV Transmissions through the IPO ahead would drive up the valuation.
- We expect the company to report a consolidated EPS of Rs 43.3 in FY2007E. The stock trades at an attractive valuation of a PER of 21.3x on its FY2007 earnings.

Name	CMP (Rs)	PER FY05	PER FY06E	PER FY07E	RoE FY05	RoE FY06E	RoE FY07E	Target price	Upside (%)
Orchid Chemicals	**376.0**	117.5	30.1	18.1	6.6	8.1	12.9	**460.0**	22%

Remarks:

- Orchid Chemicals and Pharmaceuticals (Orchid), historically a manufacturer of bulk drugs, has now entered the high-revenue, high-margin business of finished dosages in the USA. This transition from a bulk drug manufacturer to an integrated manufacturer of formulations will drive the earnings and also result in higher valuations.
- Orchid has made marketing alliances with US companies for the sale of 20 lifestyle drugs representing a market size of US$20 billion. Thus the lifestyle segment in the regulated markets provides a huge opportunity for the company from FY2008 onwards.
- Orchid has repaid Rs265 crore of its high-cost debt. Going ahead, we expect the interest savings to add to the bottom line directly from FY2007 onwards. We expect the profit after tax (PAT) to increase 4.5x from FY2005 to FY2007, at a CAGR of over 110%.
- Orchid is trading at cash earnings per share (CEPS) 11.3x its FY2007E CEPS and that is at a deep discount to its peers. Considering the robust generic opportunity available to Orchid and the strong growth prospects, we are positive on the stock.

Name	CMP (Rs)	PER FY05	PER FY06E	PER FY07E	RoE FY05	RoE FY06E	RoE FY07E	Target price	Upside (%)
Sanghvi Movers	**774.5**	41.2	16.4	12.4	23.8	31.9	33.6	**800.0**	3%

Remarks:

- Sanghvi Movers Ltd (SML) is the fourth largest crane-hiring company in Asia and is ranked 24th in the world by Cranes International, an international crane magazine. It has a fleet of 190 cranes of capacity ranging from 20 tonne to 800 tonne. The capacity expansion exercise undertaken by India Inc in recent times has led to a strong demand for cranes.
- SML plans to add cranes worth Rs160 crore in FY2006. Of this the company has already purchased cranes worth Rs70 crore in H1FY2006 which will lead to a strong growth during H2FY2006. Moreover SML is also planning to add cranes worth Rs135 crore in FY2007 which will lead to the growth in FY2008 as well.
- Currently SML is running at 95-100% utilisation levels. The company has adopted a strategy to have a back-to-back tie-up for most of its cranes which shall ensure strong cash flows going forward.
- We expect the company to report EPS of Rs47.2 in FY2006E and of Rs62.3 in FY2007E, but the CEPS will be significantly higher.

Name	CMP (Rs)	PER FY05	PER FY06E	PER FY07E	RoE FY05	RoE FY06E	RoE FY07E	Target price	Upside (%)
Shree Cement	**985.0**	31.5	26.9	18.3	46.1	35.6	34.8	**1100.0**	12%

Remarks:

- Shree Cement, a leading and lowest cost cement manufacturer in the country, is strategically located in the vicinity of lucrative markets like Delhi and Haryana in the northern region.
- The tight demand-supply scenario in the northern region has ensured a healthy improvement in the prices of cement over the last one year and the prices are expected to maintain the uptrend going forward.
- To make the most of the tight demand-supply scenario, Shree Cement is proactively expanding its cement capacity. The recently commissioned 1.2-million-tonne cement plant and the proposed new 1.2 million cement unit will ensure a healthy volume growth for Shree Cement for the next two to three years.
- We expect the company's earnings to grow at a CAGR of 20% for the next two years. The stock is trading at attractive valuations of 18.3x its FY2007E earnings and EV/tonne of US$107.

Name	CMP (Rs)	PER			RoE (%)			Target price	Upside (%)
		FY05	FY06E	FY07E	FY05	FY06E	FY07E		
SKF India	**312.5**	25.0	20.2	14.1	22.1	22.3	25.7	**406.0**	30%

Remarks:

- SKF India Ltd (SKFIL), a 54% subsidiary of world leader SKF, Sweden, is a leading technology & solution provider of bearings and related systems. It also provides services to the aerospace, automotive, electrical and industrial sectors.
- SKFIL enjoys good visibility in the high-margin replacement market which is a huge positive for the company. Factors such as the company's market dominance (a 29% share of the organised market), limited capex plans for the next two years, a debt-free status by CY2006 and higher returns on the capital employed (over 22%) are some other investment positives.
- We believe that the substantial de-risking of the company's business portfolio (like reduced dependence on the automobile industry, which is cyclical in nature) and a significant increase in its free cash flow will trigger a re-rating in its stock's price.
- The stock quotes at PER of 14.1x its CY2006E earnings. We believe the stock's valuation is attractive as compared with that of the other auto component companies.

Name	CMP (Rs)	PER FY05	PER FY06E	PER FY07E	RoE FY05	RoE FY06E	RoE FY07E	Target price	Upside (%)
Ultra Tech Cement	**715.1**	3575.5	55.4	27.2	9.3	16.9	23.5	**850.0**	19%

Remarks:

- The prices of cement in the country have risen in the past one year and are expected to remain buoyant owing to a rising demand, a depleting surplus supply and a slow-down in capacity addition. We expect UltraTech Cement Ltd (UCL) to be the biggest beneficiary of the upswing in the cement prices due to its high leverage to them.
- The freight cost, which is one of the major costs for cement producers, is very high for UCL. However it shall reduce as the company explores the synergies with Grasim Industries.
- UCL has lined up a capex plan of Rs1,003 crore to be implemented over the next two years. As part of the plan it shall set up a 92-megawatt thermal power plant at a cost of Rs540 crore for captive use; this shall reduce its power cost substantially.
- The stock is quoting at an enterprise value of US$120 per tonne of cement; we believe the valuation is attractive considering the stock's steep discount to the valuation commanded by its peers.

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