Market Strategy

September 21, 2010

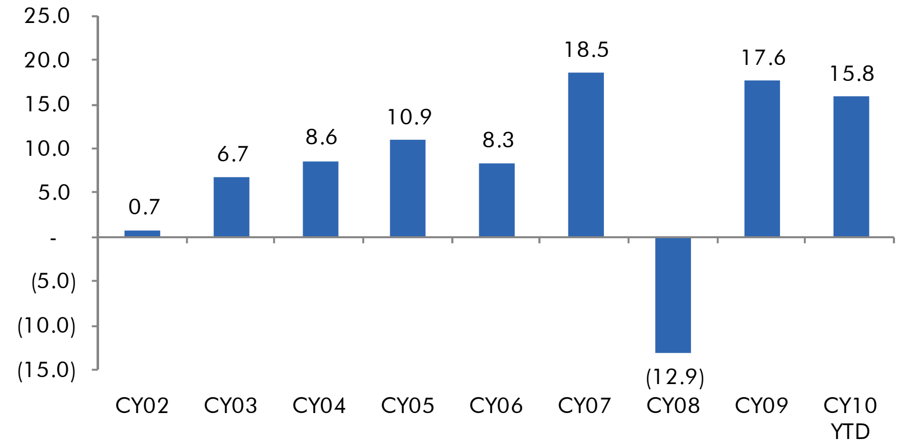
Finding Alpha returns at 20,000 Sensex

Alpha Picks		
Company (Rs)	CMP	TP
High RoE Businesses		
Blue Star	502	589
Maruti Suzuki	1,413	1,550
Mphasis	657	872
Reliance Industries	1,033	1,260
Tech Mahindra	728	950
United Phosphorous	187	228
Deep Value Stocks		
Anant Raj	139	178
Denso India	110	136
Electrosteel Castings	48	72
Finolex Cables	58	85
GE Shipping	311	396

Note: Investment period – 12 Months BSE Sensex (20,001) and Price as on September 21, 2010

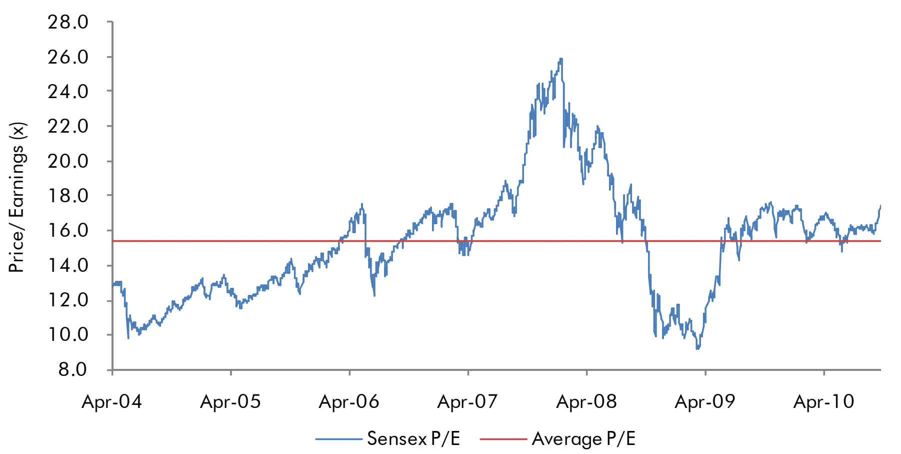
The Sensex is once again at 20,000, buoyed by US$16bn of FII liquidity since January this year. The Sensex is now trading at a one-year forward P/E of 17.5x and we believe these premium valuations should sustain on the back of the relatively strong growth outlook of the Indian economy and the huge amount of foreign investments that India is therefore expected to attract. However, at these kind of valuation levels, finding Alpha stocks i.e. stocks that could give positive returns, even if the Sensex remains where it is, becomes all the more important. In this note we have discussed two key categories of stocks that have the potential to generate Alpha returns, viz., High RoE Businesses and Deep Value Sectors.

Exhibit 1: FII Inflow remain strong (US$ Bn)



Source: Company, Angel Research

Exhibit 2: Sensex: One year forward P/E



Source: Company, Angel Research

Learning from the last cycle

Many stocks have gone up 4, 5 even 10 times from the lows of March last year. But is this the best benchmark to judge how much money investors have made? We tried to analyse how many stocks have given high returns even if one had invested the last time the Sensex was at 20,000+ levels – towards the end of December 2007.

We used a cut-off of 50% returns, implying a reasonable 15% annual return over this ~three year period. In fact, a large number of stocks met this cut-off:

- 30 stocks with a market cap of Rs10,000cr+
- 79 stocks with 1,000-10,000cr market cap
- 99 midcaps with 250cr+ market cap

Interestingly, almost all these stocks fell into one of two categories that we believe are the hallmarks of ***Alpha*** stocks:

1. **High RoE** businesses, rather than expensive growth stocks
2. **Deep Value** sectors facing challenges, rather than high margin commodities

High RoE Businesses

Generally, stocks of those companies did well, that improved or maintained strong RoEs, either due to strong ad spend or distribution (FMCG) or because of a high element of value addition or intangible advantage (Software). Also important was the existence of reasonable valuations in these stocks – either relative to the Sensex or to their peers or in EV/Sales terms due to temporarily depressed margins. Below, we have given an indicative list of 5 such stocks that have given 61-306% returns since December 2007. Selecting stocks on similar criteria viz., inherently high-RoE businesses at relatively reasonable valuations, we have included 5 stocks that we expect to give alpha returns going forward.

Winners since December 2007

- **Asian Paints (up 155%)** was trading at reasonable P/E levels, with the strong RoIC profile and growth of the company not fully discounted.

Asian Paints	FY2005	FY2006	FY2007	FY2008	FY2009	FY2010	Current
Sales	2,574	3,021	3,670	4,407	5,464	6,681	
ROIC	24.3	26.6	33.8	44.6	35.0	58.0	
P/E	21.5	29.0	25.6	27.6	18.8	25.4	35.0
Stock Price	391	644	765	1,200	786	2,043	2,815
Sales	2,574	3,021	3,670	4,407	5,464	6,681	

Note: Valuations are on trailing nos.

- **Infosys, TCS (up 63% and 61% respectively)** were trading at too low a valuation premium vs. Sensex due to temporary negative cues from global economies.

TCS	FY2005	FY2006	FY2007	FY2008	FY2009	FY2010	Current
ROE	118.8	62.6	57.0	48.1	36.9	40.2	
P/E	35.8	31.6	28.5	15.6	10.2	22.2	27.1
Sensex P/E	14.5	21.7	18.7	18.3	12.3	19.6	22.3
Stock price	358	479	616	405	270	781	953

Note: Valuations are on trailing nos.

- **Rallis (up 306%)** – a high RoE agri-chemical distribution business, **Bayer Cropscience (up 144%)** – high RoE, R&D driven business, with land unlocking.

Rallis	FY2005	FY2006	FY2007	FY2008	FY2009	FY2010	Current
Sales	489	592	617	675	856	901	
ROE	24.9	24.0	(3.2)	11.8	19.6	25.5	
P/E	8.2	10.2	(50.5)	13.2	7.3	16.5	29.1
Stock price	155	220	174	224	261	837	1,474
Sales	489	592	617	675	856	901	

Note: Valuations are on trailing nos.

Outperformers going ahead

Blue Star (CMP: Rs.502/ TP: Rs.589/ Upside: 17%)

- Blue Star operates in a high value add space, as indicated by its high RoE profile of over 40%. The company is poised for strong growth in the years to come, based on positive business outlook across all its segments and a healthy order book of Rs1,976cr, which is 1.1x FY2010 sales of the Electro Mechanical Projects and Packaged Air Conditioning Systems (EMPPACS) segment. The acquisition of DS Gupta Construction will complement the company's service bouquet, which would now have a strong presence in the plumbing and fire fighting space.
- Over the past few months, there has been higher demand in the ducted systems space, which is generally a precursor to the improvement in the general business. Going ahead, we expect the demand from the traditional IT and office segments to improve, driving the growth of the company. We expect the sales to grow at a CAGR of 22.3% over FY2010-12E.
- At the CMP, the stock is trading at reasonable valuations of 16.2x FY2012E EPS. We believe that this is a good entry point into the stock, keeping in view its strong growth prospects. We have valued the stock at P/E of 19x FY2012E EPS and arrived at a target price of Rs589.

Y/E March	Sales (Rs cr)	OPM (%)	PAT (Rs cr)	EPS (Rs)	ROE (%)	P/E (x)	P/BV (x)	EV/EBITDA (x)	EV/Sales (x)
FY2011E	3,061	10.5	222	24.6	40.1	20.4	7.3	14.1	1.5
FY2012E	3,778	10.7	279	31	40.4	16.2	5.9	11.2	1.2

Maruti Suzuki (CMP: Rs.1,413/ TP: Rs.1,550/ Upside: 10%)

- Given India's low car penetration (12 per 1,000 v/s 21 per 1,000 in China) and with PPP-based per capita estimated to approach the empirically-observed inflection point for car demand of US $5,000 over the next 4-5 years, we expect 15.2% CAGR in domestic volumes over FY2010-12E.
- Maruti has a sizeable competitive advantage over foreign entrants due to its widespread distribution network (2,767 service and 681 sales outlets).
- Moreover, with Suzuki Japan making Maruti a manufacturing hub for small cars, to cater to increasing global demand caused by rising fuel prices and stricter emission standards, we estimate 7.2% CAGR in export volumes over FY2010-12E.

- The company, through de-bottlenecking, would be able to manufacture around 1.1lakh units per month from 2HFY2011E thereby reducing the uncertainty of capacity constraints to a certain extent. Further, we believe that, the recent hike in royalty payment would be passed by the company to certain extent with a price hike.
- Maruti is trading at an EV/Sales of 0.7x FY2012E vs. Tata Motors valuation of 0.6x, even though in case of Tata Motors, 2/3rds of the topline is from its global acquisition, Jaguar, where profitability is significantly lower than India.
- At the CMP, the stock is trading at attractive valuation (13.9x FY2012E earnings). At our Target Price of Rs1,550, Maruti would trade at 15.3x FY2012E (10% discount to our Sensex target multiple).

EV/Sales	FY2005	FY2006	FY2007	FY2008	FY2009	FY2010	FY2011E	FY2012E
Maruti	0.9	1.8	1.3	1.1	0.9	1.2	0.9	0.7
Tata Motors	0.7	1.5	1.0	0.8	0.6	0.7	0.7	0.6

Y/E March	Sales (Rs cr)	OPM (%)	PAT (Rs cr)	EPS (Rs)	ROE (%)	P/E (x)	P/BV (x)	EV/EBITDA (x)	EV/Sales (x)
FY2011E	34,053	10.5	2,481	85.9	18.3	16.5	2.7	9.1	0.9
FY2012E	39,514	10.8	2,927	101.3	16.6	13.9	2.3	7.2	0.7

Mphasis (CMP: Rs.657/ TP: Rs.872/ Upside: 33%)

- The company steered the pricing headwind from HP's renegotiation exercise very prudently by making up the cuts in application services with higher price points in Infrastructure services. The major pricing review overhang is done and, going forward, management expects a stable pricing arrangement with HP given that the 50% of rate card pricing will remain fixed and 50% will be market driven
- Management is focused on enhancing the company's growth trajectory in the Non-HP business going forward. This initiative coupled with the effective rate card implementation, which has witnessed cost optimisation, would see improved operational performance for Mphasis going ahead.
- Mphasis has strong cash position of Rs1,487cr as on July 2010, which would help it to go for acquisitions of strategic fit in the size of US $50mn–$100mn annual revenue run rate.
- Considering the company's parentage of one of the largest IT companies globally (HP-EDS), driving rapid growth and bringing it closer to Top Tier status, we expect Mphasis to be rerated from the FY2012E P/E of 10.8x that it is currently trading at. We value the stock at 14.3x FY2012E EPS of Rs60.9 (at 32% discount to Infosys' target PE of 21x) and maintain our Buy rating on the stock with a Target Price of Rs872.

Y/E March	Sales (Rs cr)	OPM (%)	PAT (Rs cr)	EPS (Rs)	ROE (%)	P/E (x)	P/BV (x)	EV/EBITDA (x)	EV/Sales (x)
FY2011E	6,083	25.4	1,237	58.9	30.5	11.2	3.1	7.2	1.8
FY2012E	7,101	24.2	1,279	60.9	24.1	10.8	2.4	6.1	1.5

Reliance Industries (CMP: Rs.1,033/ TP: Rs.1,260/ Upside: 22%)

- RIL's stock price has borne the brunt of negative news flows on account of slower ramp-up of KG Basin gas, subdued refining and petrochemical margins and concerns over the redeployment of the cash flows. However, we believe that the current price has discounted the worst case scenario and there is potential upside for the stock from the current levels.
- We expect RIL's profitability to register 34% CAGR over FY2010-12E driven by improvement in refining margins coupled with ramp up of oil and gas production at the KG Basin. Moreover, increase in the share of E&P in the profit matrix will in turn reduce exposure to cyclical segments.
- We expect the company's foray in the newer ventures (such as shale gas, Broadband and power) along with discovery and monetisation of its upstream portfolio to keep it on high-growth orbit going ahead. Moreover, the same is also likely to resolve the concerns over the redeployment of the cash flows. On the valuation front, the stock is relatively under-valued trading at 1.8x FY2012E P/BV.
- Moreover, RIL is trading at ~35% discount to Sensex in terms of FY2012E P/BV, even though estimated ROIC continues to be as high as 18.0%. Hence, we maintain a Buy on RIL, with a Target Price of Rs1,260, translating into an upside of 22% from current levels.

Y/E March	Sales (Rs cr)	OPM (%)	PAT (Rs cr)	EPS (Rs)	ROE (%)	P/E (x)	P/BV (x)	EV/EBITDA (x)	EV/Sales (x)
FY2011E	234,754	17.4	22,718	69.5	15.0	14.9	2.1	9.0	1.6
FY2012E	243,596	20.0	28,530	87.2	16.4	11.8	1.8	7.1	1.4

Tech Mahindra (CMP: Rs.728/ TP: Rs.950/ Upside: 31%)

- The company is currently seeing strong traction and pursuing some large transformational deals in North America (average size of these deals range from US $25mn–75mn for a period of five years). Thus, we believe the company's growth will be led by strong volume ramp ups in non –BT counter and BT business will maintain its steady state.
- Mahindra Satyam has signed many new clients over the past six months and has been invited for various RFP's. BFSI & Manufacturing verticals are driving growth for the company. Also the companies ERP business is back on growth path. Broad expectations for the financials are USD $1 billion revenue run rate for FY10. Positive news flow from Satyam in the form of key client retention, stable operational matrix and new key deal wins will provide comfort on this company's future business prospects.
- We have valued Tech Mahindra on an SOTP basis, valuing Tech Mahindra (excluding Satyam) at 12x FY12E EPS, i.e. at a 43% discount to Infosys target multiple of 21x and valued Satyam's stake at Rs312 per share based on a market cap basis by applying a 20% holding company discount to arrive at a Target Price of Rs950.
- Even on EV/Sales basis, the company is trading at attractive valuations of 1.2x FY2012E, once conservative topline estimate of Rs4,800cr for Satyam are taken into account – a steep discount to peers. Thus we continue to maintain our Buy recommendation on the stock.

Y/E March	Sales (Rs cr)	OPM (%)	PAT (Rs cr)	EPS (Rs)	ROE (%)	P/E (x)	P/BV (x)	EV/EBITDA (x)	EV/Sales (x)
FY2011E	4,858	19.5	656	50.3	21.9	14.5	2.7	6.2	1.2
FY2012E	5,554	18.6	693	53.2	18.5	13.7	2.3	5.2	1.0

United Phosphorous (CMP: Rs.187/ TP: Rs.228/ Upside: 23%)

- United Phosphorus (UPL) figures among the Top-5 generic Agrichemical players in the world, with a presence across major markets like the US, EU, Latina America and India.
- Total off-patent market is worth US $29bn, of which a mere US $16bn is currently being catered by the generic players. Furthermore, 61% of the same is controlled by the five largest generic players including UPL. Further, given the high entry barriers by way of high investments, entry of new players is also restricted. Thus, amidst this scenario and on account of having a low cost base, we believe that UPL enjoys an edge over competition and is placed in sweet spot to leverage the upcoming opportunities in the global Generic space
- Over FY2010-12E, we expect UPL to post 9% and 22% CAGR in Sales and PAT, respectively. We expect RoCE and RoE to improve from 14% and 19% in FY2010 to 20% each in FY2012E.
- At current valuations of 10.6x FY2012E EPS, the stock is attractively valued vis-a-vis its global (10x) and domestic peers (16x), and historic average (15x).

Y/E March	Sales (Rs cr)	OPM (%)	PAT (Rs cr)	EPS (Rs)	ROE (%)	P/E (x)	P/BV (x)	EV/EBITDA (x)	EV/Sales (x)
FY2011E	5,830	20.3	652	14.1	19.3	13.2	2.3	7.8	1.5
FY2012E	6,406	21.3	814	17.6	19.9	10.6	2.0	6.5	1.4

Deep Value Sectors

The other set of stocks that have given stellar returns are the Deep Value stocks i.e. should be trading ideally below book value. Usually, such stocks belonged to sectors going through a cyclical downturn, leading to depressed margins, debt-ridden balance sheets and RoEs insufficient to add capacity to meet demand. Eventually, this self-correcting mechanism led demand to catch up with supply, leading to cyclical turnaround and *Alpha* returns.

Winners since Dec 2007

- Textile companies like Vardhaman Textiles (up 91%) were trading at far below book even at Dec 2007 peak, because their RoEs were depressed. Low RoEs and high debt prevented capacity addition in the industry, eventually leading to pricing power, margin improvement and stock rerating.

Vardhman Textiles	FY2005	FY2006	FY2007	FY2008	FY2009	FY2010	Current
ROE	19.1	19.6	17.1	11.2	12.5	17.4	
P/BV	0.6	2.0	1.0	0.5	0.2	0.9	1.1
BVPS	322.3	177.7	203.1	223.0	244.2	283.2	
PAT	129.5	179.8	184.6	135.0	166.0	259.2	
Stock Price	182	350	207	104	48	266	311

Note: Valuations are on trailing nos.

- Similarly, **Packaging companies like Polyplex (up 110%)** were trading at far below book even at Dec 2007 peak, because their RoEs were depressed. Low RoEs and high debt prevented capacity addition in the industry, eventually leading to pricing power, margin improvement and stock re-rating

Polyplex	FY2005	FY2006	FY2007	FY2008	FY2009	FY2010	Current
ROE	23.0	12.1	8.5	22.4	19.4	13.9	
P/BV	0.9	0.7	0.4	0.5	0.3	0.4	1.6
Stock Price	185	171	103	157	113	194	726

Note: Valuations are on trailing nos.

Outperformers going ahead

Anant Raj Industries (CMP: Rs.139/ TP: Rs.178/ Upside: 28%)

- Almost all of ARIL's land bank (872 acres) is exclusively located in the NCR within 50km of Delhi, with approximately 525 acres in Delhi. This land bank has been acquired at an historical average cost of Rs300/sq ft.
- We expect ARIL's residential projects to drive its near-term operational visibility and help register Rs600cr Profit over the next three years. ARIL recently launched two residential projects in NCR; Kapashera (0.28mn sq. ft.) and Manesar (1mn sq. ft.) for Rs5,000/sq. ft. and Rs2,500/sq. ft., respectively. Management has indicated that it has entirely sold Kapashera project and ~50% of Manesar project. Further, we expect ARIL’s Manesar and Kirti Nagar properties to reach their peak occupancy levels in 6–9 months as leasing activity improves coupled with five hotels getting operational by FY2011E. Consequently, we expect ARIL to report rental income of Rs201cr in FY2012E as compared to Rs49cr reported in FY2010.
- ARIL is trading at a 33% discount to its NAV. The stock is trading at 10.1x FY2012E EPS and 1.0x FY2012E P/BV and hence we maintain a Buy on stock with a Target Price of Rs178 (15% discount to our one-year forward NAV).

Y/E March	Sales (Rs cr)	OPM (%)	PAT (Rs cr)	EPS (Rs)	ROE (%)	P/E (x)	P/BV (x)	EV/EBITDA (x)	EV/Sales (x)
FY2011E	491	52.7	209	6.6	5.6	20.8	1.1	15.1	8.0
FY2012E	995	58.2	434	13.8	10.6	10.1	1.0	7.6	4.4

Denso India (CMP: Rs. 110/ TP: Rs. 136/ Upside: 24%)

- Denso is a subsidiary of Denso Corp., a US $30bn enterprise, which has strong relations with global auto majors, viz. Suzuki, Honda and Toyota. Besides strong relations with global majors, Denso Corp. provides strong financial backing and technological knowledge to Denso, which will help the company to expand capacity as well as add new products to its portfolio in the future to cater to the growing domestic demand.
- With the huge spurt in demand for automobiles, OEMs have witnessed a supply-side constraint from auto ancillary companies. This has resulted in a considerable increase in the bargaining power of these companies. Denso on the back of its strong balance sheet is likely to be a preferred supplier going forward.
- On the back of strong growth in the auto sector, we expect Denso to witness a 17% CAGR in sales, with a gradual increase in EBITDA margins over FY2010–12E. Consequently, the company's net profit is expected to increase at a 49% CAGR over FY2010–12E. Denso has traded at a five-year average of 9x one-year forward earnings. Currently, the stock is trading at 6.5x FY2012E earnings and we value the company at 9x FY2012E earnings of Rs15.1/share. We recommend a Buy rating on Denso with a Target Price of Rs136, implying an upside of 24%.

Y/E March	Sales (Rs cr)	OPM (%)	PAT (Rs cr)	EPS (Rs)	ROAE (%)	P/E (x)	P/BV (x)	EV/EBITDA (x)	EV/Sales (x)
FY2011E	884	4.8	21.2	7.6	9.9	12.9	1.2	6.1	0.3
FY2012E	1,016	7.3	42.1	15.1	17.5	6.5	1.1	3.1	0.2

Electrosteel Castings (CMP: Rs.48/ TP: Rs.72/ Upside: 50%)

- Electrosteel's (ECL) backward integration initiatives through coking coal mines, which are already operational, are expected to result in expansion of EBITDA margin by 329bp over FY2010-12E.
- The company is also awaiting final environmental clearance for its iron ore mine, which will further lower costs, but has not been factored in our estimates.
- ECL is venturing into steel-making through its subsidiary Electrosteel Steels (ESL), which is setting up a 2.2mn tonne steel plant expected to begin progressive commissioning from October 2010E. The plant is expected to be fully commissioned by June 2011E.
- We maintain a Buy on the stock, valuing the Core business at 8x FY2012E FDEPS and its investments in the Steel business at 1x Book Value.

Y/E March	Sales (Rs cr)	OPM (%)	PAT (Rs cr)	EPS (Rs)	ROE (%)	P/E (x)	P/BV (x)	EV/EBITDA (x)	EV/Sales (x)
FY2011E	1,706	26.2	246	6.5	14.2	7.3	0.8	5.6	1.5
FY2012E	1,818	28.0	254	6.7	13.1	7.1	0.8	4.9	1.4

Finolex Cables (CMP: Rs.58/ TP: Rs.85/ Upside: 46%)

- Finolex Cables is poised for a strong growth over the next few years, owing to entry in the verticals of High Tension (HT) and Extra High Voltage (EHV) Cables and market share expansion in the existing Low Tension (LT) Cables segment.
- The rapid ramp up of production at the Roorkee plant has already started delivering results. The company has further increased the capacity at this plant by 50%. The proximity to the growing North Indian markets and tax benefits from this plant are expected to boost the turnaround of the company.
- Company's derivatives losses are expected to decline going ahead. By FY2012, these losses are estimated to decline to Rs 24cr from Rs76cr in FY2010.
- We believe attractive valuations of 6.3x FY2012E EPS and 1.1x FY2012E BV provides a good entry point for investors. We have valued the stock at 9x FY2012E EPS which result into target price of Rs85.

Y/E March	Sales (Rs cr)	OPM (%)	PAT (Rs cr)	EPS (Rs)	ROE (%)	P/E (x)	P/BV (x)	EV/EBITDA (x)	EV/Sales (x)
FY2011E	2,048	10.0	90	5.9	13.3	9.8	1.3	4.4	0.4
FY2012E	2,458	10.2	143	9.3	18.6	6.3	1.1	3.7	0.4

GE Shipping (CMP: Rs. 311/ TP: Rs. 396/ Upside: 27%)

- As per Clarksons, 13% and 14% of the existing fleet of crude and product tankers will be added in CY2010. However, accelerated phase out of single hull tankers, which account for 12% of the existing global tanker fleet, will relieve supply-side pressures and keep the freight rates at current sustainable levels over the medium term. GE Shipping (Gesco) will be a key beneficiary of higher tanker freight rates as it derives around 46% of its consolidated revenues from the Tanker Segment.
- The company intends to list its 97.62% subsidiary, Greatship Ltd (GIL) by 2HFY2011E through fresh equity issuance. We believe this will unlock potential value of the Offshore business, which globally trades at higher multiples than the Shipping business due to high earnings visibility. We have valued Gesco's Offshore business at 5.0x FY2012E EV/EBIDTA which is at a discount to Great Offshore (5.6x FY2012E EV/EBITDA) and fetches Rs107/share or Rs1,678cr
- We value Gesco on SOTP basis, with its Shipping business contributing Rs289/share (15% discount to NAV) and its Offshore business contributing Rs107/share (5.0x FY2012E EV/EBIDTA). Based on our Target Price of Rs396 the implied EV/ EBITDA, P/BV, P/E multiple works out to 6.2x, 0.9x, and 5.9x respectively, on FY2012E basis. Thus, on account of trading at a significant discount to its global peers, we recommend a Buy on stock.

Y/E March	Sales (Rs cr)	OPM (%)	PAT (Rs cr)	EPS (Rs)	ROE (%)	P/E (x)	P/BV (x)	EV/EBITDA (x)	EV/Sales (x)
FY2011E	2,985	37.7	686	45.0	11.5	6.9	0.8	7.2	2.7
FY2012E	3,833	40.2	1,028	67.5	15.5	4.6	0.7	5.4	2.2

Biggest underperformers since December 2007

Not surprisingly, some of the biggest underperformers since December 2007 have been those stocks that had almost opposite characteristics. For instance, commodity sectors such as cement were enjoying 3.0x+ P/BV extrapolating cyclical upturn and unsustainably high operating margins. Similarly, low-Roe businesses such as retail were commanding 4.0-5.0x P/BV, paying extremely high premiums for future growth, without factoring execution risks. Stocks from such sectors are still down 35-80% from peak levels, even though the Sensex has largely recovered lost ground.

- Real estate companies like Unitech (down 83%) were trading at far above book at Dec 2007 peak, factoring in opaque land bank values. These stocks have significantly underperformed since then.

Unitech	FY2005	FY2006	FY2007	FY2008	FY2009	FY2010	Current
P/BV	2.2	13.4	15.8	12.5	1.1	1.7	2.1
Stock Price	3	21	194	276	35	73	86

Note: Valuations are on trailing nos.

- Infrastructure companies like Gammon (down 62%) were trading at far above book at Dec 2007 peak, factoring in extremely high growth, ignoring the essentially low RoE nature of the business.

Gammon India	FY2005	FY2006	FY2007	FY2008	FY2009	FY2010	Current
ROE	13.8	15.6	8.6	7.4	8.6	6.2	
P/BV	4.2	5.1	3.6	4.3	0.5	1.4	1.4
Stock Price	220	542	301	389	58	219	212

Note: Valuations are on trailing nos.

- Retail companies like Pantaloon (down 36%) were trading at far above book at Dec 2007 peak, factoring in extremely high growth, again, ignoring the essentially low RoE nature of the business.

Pantaloon*	FY2005	FY2006	FY2007	FY2008	FY2009	FY2010	Current
ROE	18.3	17.0	7.4	8.6	7.0	8.6	
P/BV	6.2	9.1	4.8	3.4	1.4	2.8	3.6
Stock Price	123	357	361	392	162	390	488

** Pantaloon reporting year is June ending;* Note: Valuations are on trailing nos.

- Cement companies like India cement (down 64%) were trading at far above replacement cost at Dec 2007 peak, extrapolating prevailing high RoEs, ignoring the essentially commodity nature of the business.

India Cements	FY2005	FY2006	FY2007	FY2008	FY2009	FY2010	FY2011E	FY2012E
ROE	(12.6)	4.1	24.2	24.4	14.7	9.1	2.1	3.0
P/BV	2.7	3.7	3.0	2.0	1.0	1.2	1.0	1.0
Stock Price	67	165	162	187	106	132	118	

Note: Valuations are on trailing nos.

Invest in Alpha stocks

We remain bullish on India's growth prospects and attractiveness for receiving continued foreign investments. Several sectors, such as steel (1/7th penetration vs. the US), Aviation (1/12th penetration), Power (1/23rd penetration), Automobiles (1/32nd penetration) and so on remain highly underpenetrated in per capita consumption terms and there is a long way to go before we catch up to productivity levels prevailing in developed countries.

Looking at Sensex valuations of 17.5x one-year forward P/E also, valuations while not cheap, are not stretched either. Hence we maintain our positive view on several sectors such as banking, infrastructure, steel and pharma, where we have an overweight stance in our model portfolio. At the same time, based on the above mentioned themes, we recommend the top picks discussed in this note, for generating ***Alpha*** returns.

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Ratings (Returns):	Buy (> 15%)	Accumulate (5% to 15%)	Neutral (-5 to 5%)	Reduce (-5% to -15%)	Sell (< -15%)

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