Sharekhan top picks

In the February 2008 issue, we had recommended the best 12 of our Stock Ideas as Sharekhan Top Picks. As on February 29, 2008 the basket of stocks has given a negative return of 0.9%. The basket's performance has been in line with the market's, as the Sensex has declined by 0.4% and the S&P CNX Nifty has risen by only 1.7% during the same month.

We have made three changes in the portfolio this month. We have replaced Jaiprakash Associates, Punj Lloyd and State Bank of India with ITC, Maruti Suzuki and Larsen & Toubro.

Name	CMP* (Rs)	PER			RoE (%)			Target price	Upside (%)
		FY07	FY08E	FY09E	FY07	FY08E	FY09E		
Aban Offshore	3,618.0	-	37.6	9.1	-7.1	55.5	94.6	5,420.0	49.8
Axis (UTI) Bank	845.0	36.1	28.7	20.6	20.9	16.0	15.7	1,302.0	54.1
BHEL	2,030.0	41.2	31.5	24.2	27.5	27.7	28.0	2,845.0	40.1
Grasim	2,785.0	13.0	9.6	11.2	27.5	27.2	27.0	3,950.0	41.8
Indo Tech Transformer	585.0	24.4	15.3	10.5	31.4	37.1	38.2	830.0	41.9
ITC	191.0	26.6	23.0	19.5	27.7	27.7	27.6	247.0	29.2
Larsen & Toubro	2,999.0	48.5	32.5	23.9	26.1	29.9	31.0	4,428.0	47.6
M&M	664.0	16.5	15.8	14.2	27.0	22.0	19.6	900.0	35.5
Marico	61.0	33.0	22.6	18.5	58.7	51.6	39.2	70.0	14.6
Maruti Suzuki	936.0	17.7	14.4	12.2	24.9	26.3	24.1	1,237.0	32.2
Ranbaxy	437.0	31.6	20.6	20.4	26.3	24.4	23.8	558.0	27.8
Shiv-vani Oil	528.0	62.8	23.5	14.6	10.4	16.9	19.4	670.0	26.9

* CMP as on March 07, 2008

Name	CMP	PER			RoE (%)			Target	Upside
	(Rs)	FY07	FY08E	FY09E	FY07	FY08E	FY09E	price	(%)
Aban Offshore	**3,618.0**	-	37.6	9.1	-7.1	55.5	94.6	**5,420.0**	49.8

Remarks:
- Aban Offshore, one of Asia's largest oil drilling companies, is benefiting from the increase in oil exploration and production activities globally. The robust demand environment is resulting in firm day rates for its assets.
- In addition to re-pricing of its assets at higher day rates, the company is also benefiting from the efforts taken to substantially ramp up the asset base through organic and inorganic initiatives. This would significantly improve its financial performance over the next few years.
- At the current market price the stock trades at 9.1x FY2009 and 7x FY2010 estimated earnings. We maintain the Buy call on the stock with a price target of Rs5,420.

Name	CMP (Rs)	PER FY07	PER FY08E	PER FY09E	RoE FY07	RoE FY08E	RoE FY09E	Target price	Upside (%)
Axis (UTI) Bank	**845.0**	36.1	28.7	20.6	20.9	16.0	15.7	**1,302.0**	54.1

Remarks:
- Axis Bank is one of the fastest growing private sector banks. It has considerably improved its earnings quality and overall performance under the able chairmanship of Mr Nayak.
- The bank's assets are expected to grow at a compounded annual growth rate (CAGR) of 36.9% over FY2007-09. The growing assets along with stable to improving margins will lead to a strong growth in net interest income of the company during the period. The bank has a very robust fee income model in place.
- It has raised around Rs4,200 crore which would help it to maintain its growth momentum in the next three years.
- At the current market price, the stock is quoting at 20.6x FY2009E earnings per share (EPS), 9.8x FY2009E pre-provision profits and 3x FY2009E book value. We maintain our Buy recommendation on the stock with a twelve-month price target of Rs1,302.

Name	CMP (Rs)	PER FY07	PER FY08E	PER FY09E	RoE FY07	RoE FY08E	RoE FY09E	Target price	Upside (%)
BHEL	**2,030.0**	41.2	31.5	24.2	27.5	27.7	28.0	**2,845.0**	40.1

Remarks:
- Bharat Heavy Electricals Ltd (BHEL), a leading supplier of power equipment, will be the prime beneficiary of a four-fold increase in the investments (Rs500,000 crore in the 11th Five-Year Plan as against Rs112,000 crore in the 9th Five-Year Plan) being made in the power sector.
- BHEL's current order book of Rs78,000 crore, ie 3.6x its FY2008E revenue, provides high earnings visibility.
- The power ministry has proposed around five ultra mega power projects entailing a capacity addition of 20,000MW (4,000MW 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 24.2x its FY2009E earnings. BHEL's valuation looks attractive as compared with that of its peers, such as Siemens, ABB and Larsen and Toubro.

Name	CMP (Rs)	PER FY07	PER FY08E	PER FY09E	RoE FY07	RoE FY08E	RoE FY09E	Target price	Upside (%)
Grasim Industries	**2,785.0**	13.0	9.6	11.2	27.5	27.2	27.0	**3,950.0**	41.8

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

Name	CMP (Rs)	PER			RoE (%)			Target price	Upside (%)
		FY07	FY08E	FY09E	FY07	FY08E	FY09E		
Indo Tech Transformers	**585.0**	24.4	15.3	10.5	31.4	37.1	38.2	**830.0**	41.9

Remarks:

- Transmission and distribution of power is all set to attract huge investments (Rs427,000 crore over the XIth Five-year Plan) owing to the need to develop a robust network for power distribution. Transformer making companies like Indo Tech Transformers are all set to benefit from the huge investments in the sector.
- Indo Tech Transformers, a niche player in the transformer manufacturing space, arguably has the best margins in the industry. The high margins due to operational efficiencies are fuelling the growth of the company.
- The company is expanding its manufacturing capacity to 7,450 MVA per annum to meet the rise in demand for transformers. It has an outstanding order book of Rs180 crore.
- The stock trades at a price/earnings ratio of 10.5x its FY2009E. We maintain Buy recommendation on the stock.

Name	CMP (Rs)	PER FY07	PER FY08E	PER FY09E	RoE FY07	RoE FY08E	RoE FY09E	Target price	Upside (%)
ITC	**191.0**	26.6	23.0	19.5	27.7	27.7	27.6	**247.0**	29.2

Remarks:

- ITC's cigarette's business that has dominance in the category continues to be a cash cow for the company. ITC has chalked out aggressive roadmap for making a mark in the Indian FMCG market. With successful brands such as Bingo, Sunfeast and Aashirwaad already in the reckoning among the best in the industry, ITC's non-cigarette FMCG business is on a strong footing. The company has further ventured into the personal care category with the launch of Superia and Fiama Di Wills soaps and shampoos that would compete with the likes of the products of HUL and P&G.
- Aggressive expansion plans in hotels and paper segments would ensure, inclusive growth across segments for the company.
- We believe ITC has a well-diversified business model with multiple revenue drivers that would ensure sustained growth for the company. It thus remains our top pick in the sector. At the current market price, ITC trades at 19.5x its FY09E EPS of Rs9.8. We maintain our Buy recommendation on the stock with a price target of Rs247.

Name	CMP (Rs)	PER FY07	PER FY08E	PER FY09E	RoE FY07	RoE FY08E	RoE FY09E	Target price	Upside (%)
Larsen & Toubro	**2,999.0**	48.5	32.5	23.9	26.1	29.9	31.0	**4,428.0**	47.6

Remarks:

- Larsen & Toubro, the largest engineering and construction (E&C) company in India, is a direct beneficiary of the strong domestic infrastructure development and industrial capital expenditure (capex) booms. Consequently, we estimate the order inflows to grow at a CAGR of 20.7% between FY2007 and FY2010.
- The international business is expected to emerge as one of the key drivers going forward with immense opportunities from the Gulf Corporation Council markets.
- There lies innumerable opportunities in the new verticals in which the company is entering, namely ship building, defence, railways, thermal and nuclear power.
- We believe that there is a scope for further improvement in the margins on the back of rising operational efficiencies, larger ticket-size and more complex nature of orders, better raw material sourcing and integration, and higher contribution of its new businesses which carry higher margins.
- We value the core business of L&T at 28x FY2010E earnings, or Rs3,403 per share, while we value the subsidiaries at Rs1,025 per share of L&T. At the current levels, the stock is trading at 18.5x its FY2010E consolidated earnings. We maintain our Buy recommendation with a price target of Rs4,428.

Name	CMP	PER			RoE (%)			Target	Upside
	(Rs)	FY07	FY08E	FY09E	FY07	FY08E	FY09E	price	(%)
M&M	**664.0**	16.5	15.8	14.2	27.0	22.0	19.6	**900.0**	35.5

Remarks:

- Government's increasing thrust on agriculture and easy availability of credit would benefit M&M's tractor sales.
- Launch of Logan in collaboration with Renault and other planned launches such as new UV platform and other products in collaboration with International Trucks is set to further enrich its product mix. Another multi-purpose vehicle (code named Ingenio) is slated to be launched in FY2008.
- A better product mix and higher operating efficiencies have helped improve the margins of the company.
- Subsidiaries like Tech Mahindra, Mahindra Gesco, and MMFSL are rendering strong performances and are adding significant value to its sum-of-the-parts valuation.
- Currently M&M is quoting at 8.9x FY2009E its consolidated earnings.

Name	CMP	FY07	FY08E	FY09E	FY07	FY08E	FY09E	Target price	Upside (%)
Marico	**61.0**	33.0	22.6	18.5	58.7	51.6	39.2	**70.0**	14.6

Remarks:

- Marico is a major player in the Indian hair care and edible oil markets. Its flagship brand *Parachute* combined with *Nihar* commands a 57% share of the branded coconut oil market in India. Its 'good for heart' edible oil brand '*Saffola*' is also witnessing good volume growth.
- Marico has been growing both the organic and inorganic way and thereby follows the strategy of adding new products and territories to its portfolio. Apart from domestic operations, its international business covers countries like Bangladesh and Egypt. The company is also expanding its business to some extent to the US and the UAE.
- We believe apart from the growth in the existing business through product innovations, the expanding new age businesses of Kaya Clinics and weight loss centers and spas in the USA promise a great deal.
- Marico is among the fastest growing FMCG companies in India with very good return ratios. At the current market price, the stock trades at 22.6x its FY2008E earnings and 18.5x its FY2009E earnings.

Name	CMP	FY07	FY08E	FY09E	FY07	FY08E	FY09E	Target price	Upside (%)
Maruti Suzuki	**936.0**	17.7	14.4	12.2	24.9	26.3	24.1	**1,237.0**	32.2

Remarks:

- Maruti Suzuki, the market leader in the passenger car market in India, is set to benefit from the number of new launches made by it in the recent times.
- Most of its new launches, namely *WagonR Duo*, *Zen Estilo*, *Diesel Swift* and *SX4*, have been well received by the market and are clocking strong volumes.
- Also, with the addition of the diesel vehicle and a sedan, the company has expanded its product basket, making it a full-fledged play on the country's booming passenger car market. The company also plans to launch its *Swift* sedan at the start of the next fiscal.
- With the expansion of its Manesar plant, its exports are also set to go on a top gear. Suzuki has identified India as a hub for manufacture of small cars for its worldwide markets and the company would be exporting about 100,000 units of the new vehicle to its parent, while another 50,000 units would be supplied to Nissan.
- At the current levels, the stock is trading at 12.2x its FY2009E and is available at an EV/EBIDTA of 7.8x.

Name	CMP (Rs)	PER			RoE (%)			Target price	Upside (%)
		FY07	FY08E	FY09E	FY07	FY08E	FY09E		
Ranbaxy Lab	**437.0**	31.6	20.6	20.4	26.3	24.4	23.8	**558.0**	27.8

Remarks:

- With a geographically diversified presence and a large product portfolio, Ranbaxy is one of the best plays on the global generic opportunity.
- The company has guided towards an impressive 18-20% growth in CY2008, an expansion of margins to 17.5-18%, resulting in a net profit growth of 20-25%. This guidance is excluding any one-time exclusivity opportunities in the USA.
- Ranbaxy believes the next wave of its growth to come from the branded markets in Asia, Africa and Latin America. With a product pipeline of over 100 products for these markets, revenues from emerging markets will drive the company's growth.
- Ranbaxy believes that it has FTF status on approximately 18 Para IV ANDA filings, representing a market size of about USD27 billion. It expects to monetise at least one FTF opportunity every year for the next few years and has already announced the opportunities until CY2010. The FTF opportunities announced so far are collectively valued at Rs2,716 crore, translating into a per share value of Rs68.
- Ranbaxy has decided to de-merge its new drug discovery research (NDDR) operations into a separate entity effective from January 1, 2008 and list it subsequently. This will boost the overall profitability of the core business and also unlock value in the discovery research and development (R&D) assets. The announcement of further details on the demerger scheme in February 2008 will act as a near-term trigger for the stock.
- At the current market price, Ranbaxy is trading at 20.4x its estimated CY2008E and 17.8x its estimated CY2009E earnings. We maintain our Buy recommendation on the stock with a price target of Rs558 (Rs490 for base business plus Rs68 for FTFs).

Name	CMP (Rs)	PER FY07	PER FY08E	PER FY09E	RoE FY07	RoE FY08E	RoE FY09E	Target price	Upside (%)
Shiv- vani Oil & Gas	**528.0**	62.8	23.5	14.6	10.4	16.9	19.4	**670.0**	26.9

Remarks:

- With a fleet of 25 onshore drilling rigs and six seismic survey crew, Shiv-Vani Oil & Gas Exploration (SOGEL) has emerged as the largest onshore service provider catering to oil and gas exploration companies.
- Augmentation of assets by the company is well timed in the industry up-cycle as heightened exploration activity has led to a severe shortage of resources with service providers, leading to firming up of day rates (or billing rates per km in case of seismic survey) for various services. Moreover, the order backlog of over Rs3,000 crore (over 8x CY2006 revenues) provides strong revenue-growth visibility.
- The consolidated revenues and earnings are expected to grow at CAGR of 60.3% and 72.7% respectively over the three-year period CY2006-09.
- Despite the robust growth prospects, the scrip is available at attractive valuations of 14.6x CY2008 and 11.1x CY2009 earning estimates. We recommend Buy call on the stock.

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