investor's eye

Index

Take Five

Scrip	Reco Date	Reco Price	CMP	Target
Ashok Leyland	23-May-06	38	**41**	53
Elder Pharma	26-Apr-06	298	**329**	410
Subros	26-Apr-06	206	**215**	370
TVS Motor	03-Apr-06	140	**125**	210
WS Industries	02-Dec-05	51	**65**	112

Sharekhan Ltd
A-206, Phoenix House, 2nd Floor, Senapati Bapat Marg, Lower Parel, Mumbai - 400013, India.

Mahindra & Mahindra

Apple Green

Stock Update

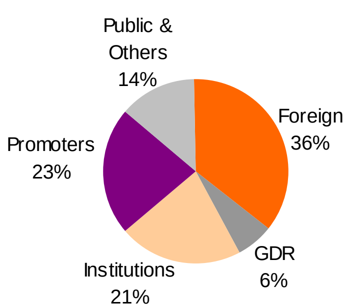
Strong consolidated numbers

Buy; CMP: Rs592

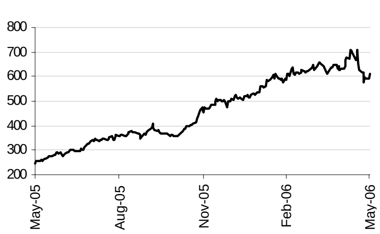
Company details

Price target:	Rs700
Market cap:	Rs14,719 cr
52 week high/low:	Rs724/245
NSE volume: (No of shares)	8.8 lakh
BSE code:	500520
NSE code:	M&M
Sharekhan code:	M&M
Free float: (No of shares)	17.13 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-5.3	0.6	27.3	140.8
Relative to Sensex	3.2	-4.2	4.3	46.2

Result highlights

- The stand-alone net sales of Mahindra and Mahindra (M&M) grew by 20% year on year (yoy) to Rs2,289 crore in Q4FY2006. The operating profit margin (OPM) improved by 86 basis points yoy to 11.9% in the quarter but declined by 100 basis points on a sequential basis due to a rise in the raw material costs. A lower other income of Rs13.8 crore due to a low dividend from Tech Mahindra and a higher tax outgo of Rs85.9 crore kept the pre-exceptional profit after tax (PAT) flat at Rs155 crore, below our estimate. There was an extraordinary income of Rs166 crore relating to profits from the sale of the shares of MMFSL. This resulted in a 110% growth in the reported PAT at Rs321 crore as compared with Rs152.6 crore in the corresponding quarter in the previous year.
- The stand-alone FY2006 net sales grew by 23% to Rs8,222.7 crore. The operating profit was up 26% to Rs967.2 crore. In the automotive business, the domestic sales were almost flat while the exports surged by 82%. The tractor segment however recorded a strong growth of 30%.
- Looking at the consolidated numbers, the full year's net sales grew by 31.3% to Rs12,335.4 crore. The OPM surged to 14.01% from 12.59% last year. Consequently, the operating profit for the full year grew by 46% to Rs1,728.7 crore. The pre-exceptional PAT for the year stood at Rs1,136.2 crore, marking a growth of 68% yoy.
- The company has planned to double its capital expenditure (capex) for the year to Rs650 crore. The funds will be utilised to develop new products, expand the existing business and carry out research and development (R&D) activities.

Result table Rs (cr)

Particulars	Q4FY06	Q4FY05	% yoy chg	FY2006	FY2005	% yoy chg
Net sales	**2,288.8**	**1,910.7**	**19.8**	**8,222.7**	**6,660.6**	**23.5**
Total expenditure	2,016.8	1,699.8	18.6	7,255.4	5,890.0	23.2
Change in stocks	170.4	42.7		-103.2	-174.1	
Consumption of raw materials	1,466.9	1,286.7		5,817.0	4,776.7	
Staff cost	140.3	116.9		551.8	464.3	
Other expenses	242.7	254.0		989.1	822.7	
Provision for contingencies	-3.6	-0.6		0.8	0.3	
Operating profits	**272.1**	**210.8**	**29.0**	**967.2**	**770.6**	**26.0**
Other income	13.8	40.6		103.9	108.5	
EBIDTA	285.8	251.5	14.0	1071.1	879.1	22.0
Interest	-6.1	-0.1		-18.4	-5.6	
PBDT	291.9	251.6	16.0	1089.5	884.7	23.0
Depreciation	50.9	51.8		200.0	184.1	
PBT	241.0	199.8		889.5	700.6	
Tax	85.9	43.2		242.4	201.5	
PAT	**155.1**	**156.6**	**-1.0**	**647.1**	**499.1**	**29.6**
Exceptional items (Net)	166.1	-3.9		210.0	13.6	
PAT after exceptional items	321.2	152.7	110.4	857.1	512.7	67.2
Margins						
OPM (%)	11.9	11.0		11.8	11.6	
EBIDTAM (%)	12.5	13.2		13.0	13.2	
PBDTM (%)	12.8	13.2		13.2	13.3	
PATM (%)	6.8	8.2		7.9	7.5	

- The contribution of the non-automotive business has increased significantly in the recent years. For FY2006, the non-automotive business contributed 33% to the top line and 48% to the bottom line. The company expects the ratio to reach 50:50 in the next two to three years.
- The stock is currently trading on a consolidated basis at 11x on FY2007E and 9.5x on FY2008E. We maintain our Buy recommendation on M&M with the price target of Rs700.

Q4 results-margins decline sequentially

M&M's stand-alone net sales for Q4FY2006 grew by 20% yoy to Rs2,289 crore. The OPM for the quarter improved by 86 basis points yoy to 11.9% but declined by 100 basis points sequentially on account of a rise in the raw material cost and the closing inventory.

A lower other income of Rs13.8 crore due to a low dividend from Tech Mahindra and a higher tax outgo of Rs85.9 crore kept the growth in the pre-exceptional PAT flat at Rs155 crore. There was an extraordinary income of Rs166 crore on account of the sale of its stake in MMFSL during the quarter. This led to a 110% growth in the PAT at Rs321 crore as compared with Rs152.6 crore in Q4FY2005. The stand-alone FY2006 net sales grew by 23% to Rs8,222.7 crore. The operating profit increased by 26% to Rs967.2 crore during the quarter.

A look at the segment-wise results now. The automotive segment has reported a revenue growth of 13.1% yoy in Q4FY2006. The profit before interest and tax (PBIT) margins have improved slightly to 9.76% from 9.61% this year, primarily due to a higher contribution of *Scorpio*. In the farm equipment segment, the revenues have grown 33% while the margins have increased significantly to 10.39%, led by a huge surge in exports.

Automotive sector

In the automotive business, the domestic growth was almost flat while the exports surged by 82%. The tractor segment however recorded a strong growth of 30%. M&M's domestic utility vehicle sales grew by 3% during the year to 114,694 vehicles. It continued to dominate the utility vehicle (UV) industry with a market share of 47.7%. *Scorpio* continued to drive the volume growth, recording a growth of 18% yoy in FY2006. In Q4 the company also launched the new *Scorpio* model with 43 additional customer-centric features. The product has been received well in the market and is expected to drive the demand in the premium UV segment.

Hit by the high success of Tata Motors' *Ace*, the company recorded a decline of 16.4% yoy in its light commercial vehicle (LCV) segment. The three-wheeler segment reported a decline of 21% yoy, but it managed to maintain its market share at 41.6%. Exports witnessed a strong growth of 82% during the year with the company increasing its presence across the globe in Europe, the Middle-East, South America, South-East Asia and Africa.

Volume growth

	FY2006	FY2005	% change
UV	114,694	111,138	3.2
LCV	6,777	7,887	-14.1
Three-wheelers	18,112	22,943	-21.1
TOTAL	139,583	141,968	-1.7
Exports	5,534	3,046	81.7

Farm equipment sector

M&M's tractors sales grew by 30% to 85,029 units. The company further strengthened its leadership position in the industry by increasing its market share from 26.5% last year to 29.7%. In Q4, the company recorded a growth

Segmental results

Particulars	Q4FY2006	Q4FY2005	% change	FY2006	FY2005	% change
Revenues						
Automotive segment	1484.81	1313.32	13.1	5240.29	4568.17	14.7
Farm equipment segment	764.06	574.38	33.0	2853.84	2029.88	40.6
Other segments	89.12	62.30	43.1	307.15	199.26	54.1
Total	2338.00	1950.00		8401.27	6797.31	
Segment results (after exceptional item)						
Automotive segment	144.90	126.15	14.9	581.17	466.33	24.6
Farm equipment segment	79.35	47.23	68.0	315.82	188.23	67.8
Other segments	3.46	4.66	-25.8	12.47	8.22	51.7
Total segment results	227.71	178.04		909.46	662.79	
PBIT Margins						
Automotive segment	9.76	9.61		11.09	10.21	
Farm equipment segment	10.39	8.22		11.07	9.27	
Other segments	3.88	7.48		4.06	4.13	

of 23.1% yoy. The company expects the tractor segment to post a growth rate of 8-10% for FY2007.

Other highlights

Capex plans for FY2007 doubled

The company has doubled its capex to Rs650 crore for this year. The funds will be utilised to develop new products, expand business and carry out R&D activities.

New products in the pipeline

Among the products in the pipeline is the *Logan* model, which is going to be launched in the first half of FY2007. The company also plans to launch its new multi-purpose vehicle (MPV) *Ingenio* in 2008. Further, the company is developing a new 49-tonne vehicle in joint venture with US-based International Trucks and Engine Corporation. The new vehicle would be launched in another 18 months.

Consolidated PAT increased by 68%.

M&M's consolidated net sales stood at Rs12,335.4 crore for FY2006, up 31% yoy. The consolidated PAT before exceptional items grew by 68% yoy to Rs1,136.2 crore. The consolidated OPM has improved substantially by 142 basis points to 14.01%. The consolidated results have been better than our expectations due to a sharp rise in the consolidated revenues in Q4. The revenue growth was driven by the strong performance of group companies like Tech Mahindra, Mahindra Finance, Mahindra Holidays, Mahindra Gesco, Mahindra South Africa and MUSCO. Also, some of the group companies like Stokes Forgings, Jensad, Plexion Technologies and Tech Mahindra became subsidiaries of M&M with effect from Q4FY2006.

The company expects some of the subsidiaries such as Tech Mahindra to grow at a fast pace. This implies that the growth in the consolidated revenues and profit could be higher even in FY2007.

Contribution of non-automotive business increasing

The contribution of the non-automotive business has increased significantly in the recent years. For FY2006, the non-automotive business contributed 33% to the top line and 48% to the bottom line. The company expects the ratio to reach 50:50 in the next two to three years.

Valuations and view

Looking at the strong volume growth in the tractor segment, the margin improvement and the company's global reach as a result of overseas acquisitions done in previous quarters, we maintain our bullish outlook on the company. The stock is currently trading on a consolidated basis at 11x on FY2007E and 9.5x on FY2008E. We maintain our Buy recommendation on M&M with the price target of Rs700.

Earnings table

Particulars	FY04	FY05	FY06	FY07E	FY08E
Stand-alone					
Net sales (Rs cr)	4873.8	6511	8222.7	9524.5	10899.3
% y-o-y change		*33.6*	*26.3*	*15.8*	*14.4*
Net profit (Rs cr)	322.5	499.5	647.2	711.5	804.7
EPS (Rs)	13.8	21.4	27.7	30.5	34.5
% y-o-y change		*54.9*	*29.6*	*9.9*	*13.1*
PER (x)	44.2	28.5	22.0	20.0	17.7
Consolidated					
Net profit (Rs cr)	398.3	711.0	1136.2	1300.9	1496.1
% y-o-y change		*78.5*	*59.8*	*14.5*	*15.0*
EPS (Rs)	17.1	30.5	48.7	55.7	64.1
% y-o-y change		*78.5*	*59.8*	*14.5*	*15.0*
PER (x)	35.8	20.1	12.6	11.0	9.5

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

ITC

Apple Green

Stock Update

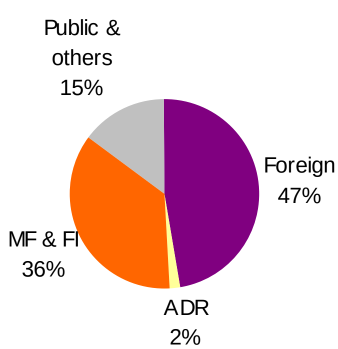
Growth in all businesses

Buy; CMP: Rs177

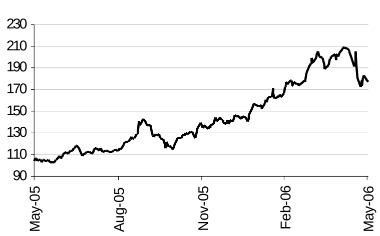
Company details

Price target:	Rs220
Market cap:	Rs65,844 cr
52 week high/low:	Rs213/101
NSE volume: (No of shares)	71.3 lakh
BSE code:	500875
NSE code:	ITC
Sharekhan code:	ITC
Free float: (No of shares)	365 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-11.2	3.5	30.5	73.6
Relative to Sensex	-3.3	-1.4	6.9	5.4

Result highlights

- ITC's net revenues grew by a robust 27.9% year on year (yoy) and by 8.9% quarter on quarter (qoq) in Q4FY2006 to Rs2,784.5 crore, powered by a strong growth in all the business segments.
- All the businesses reported a high double-digit growth for Q4FY2006 with the main business of cigarettes growing at a healthy rate of 15%.
- The operating profit grew at a slower pace of 21% yoy to Rs802.4 crore for Q4FY2006 as the operating profit margin (OPM) fell by 165 basis points yoy to 28.8%. The margin dropped primarily due to a higher contribution of the revenues from the low-margin agri business and a marginal slip in the margins of the cigarette business.
- ITC's profit after tax (PAT) increased by 35.9% to Rs567.5 crore due to higher other income.
- At the current market price of Rs177, the stock is attractively quoting at 20.1x its FY2008E earnings. We maintain our Buy recommendation on ITC with a price target of Rs220.

Revenues, all-round performance

ITC reported a revenue growth of 27.9% to Rs2,784.5 crore. The cigarette business showed a growth of 15.1% in its revenues. The revenues of the other businesses also saw a strong growth momentum: non-cigarette fast moving consumer goods (FMCGs; up 75.7%), hotels (up 45.5%), agri products (up 55.8%) and paper and packaging (P&P; up 15.5%).

Result table Rs (cr)

Particulars	Q4FY06	Q4FY05	% yoy chg	FY2006	FY2005	% yoy chg
Net sales	2,784.5	2,177.1	27.9	9,790.5	7,485.1	30.8
Other income	74.6	413.7	-82.0	286.1	592.5	-51.7
Total income	2,859.1	2,590.8	10.4	10,076.6	8,077.6	24.7
Total expenditure	1,982.0	1,513.9	30.9	6,509.2	4,750.8	37.0
Operating profit	802.4	663.2	21.0	3,281.3	2,734.3	20.0
Interest	9.7	1.3		11.9	42.4	
Depreciation	86.2	89.7	-4.0	332.3	297.8	11.6
Profit before tax	781.2	985.9	-20.8	3,223.2	2,986.6	7.9
Tax	213.8	214.1		988.8	818.3	
Reported profit after tax	567.5	771.8	-26.5	2,234.3	2,168.4	3.0
Extraordinary items	0.0	354.3		-30.9	354.3	
Profit after extraordinary	567.5	417.4	35.9	2,265.2	1,814.0	24.9
OPM (%)	28.8	30.5	-164.5	33.5	36.5	-301.5

Segmental results

	Cigarettes	Other FMCG	Hotels	Agri	Paper	Total
Sales (Rs crore)	2882.7	305.7	263.3	804	475.5	4731.2
% y-o-y growth	15.1	75.7	45.5	55.8	15.5	25
PBIT (Rs crore)	638.3	-42.3	97.8	8.8	78.7	781.2
% y-o-y growth	13.9	-38.2	72.2	247.2	46.4	29.2
PBIT margins (%)	22.1	-13.9	37.1	1.1	16.5	16.5

Cigarettes remain the core business

The cigarette division grew by 15% yoy to Rs2,882.7 crore, driven by a double-digit growth in the volumes.

The profit before interest and tax (PBIT) margin in this business however declined by 28 basis points yoy and 200 basis points qoq.

Agri business clocks strong growth

With a strong growth of 56%, the agri business continued its strong growth, which was mainly led by wheat, non-basmati rice and leaf tobacco exports. ITC has increased its exposure in this business by scaling up its *e-Choupal* network to 6,000 kiosks, reaching over 35 lakh farmers in the seven states of Madhya Pradesh, Uttar Pradesh, Maharashtra, Rajasthan, Karnataka, Kerela and Andhra Pradesh. After creating a strong network in the rural areas, ITC has now set up seven *Choupal Sagars* in Madhya Pradesh, Maharashtra and Uttar Pradesh, and the total transaction value at these *Choupal Sagars* has reached Rs100 crore. ITC's agri venture will provide it with a strong competitive edge in the procurement and distribution of its food products. ITC plans to add 700 *Choupal Sagar* malls over the next seven to ten years.

However the PBIT margins in this business remained low at 1.1% due to the high costs associated with the ramping-up of the *e-choupal* network. Even though this business contributes marginally to ITC's profitability at present, yet with its strong potential it is expected to contribute substantially to the company's bottom line in the future.

FMCG business on strong growth trajectory

ITC's FMCG business (non-cigarettes) saw a strong growth of 75.7% to Rs305.7 crore, driven by the strong performance of the businesses of biscuits and packaged *atta* (flour). ITC has launched a host of new products in its *Sunfeast*, *Ashirwaad* and the *Kitchen of India* brands during the year which should help in keeping up the robust growth in the FMCG business. The company is now planning to enter the other FMCG product segments, such as shampoos, soaps and personal care products, which together make for a Rs50,000-crore opportunity.

The FMCG business continues to make losses. However, with the increase in its size the magnitude of the losses is going down.

Hotel business—a huge opportunity

ITC's hotel division reported an increase of 45.5% in its revenues to Rs263.3 crore in Q4FY2006. With the increasing tourist inflows into India and domestic travel reaching an all-time high level, the hotel industry is achieving record increases in the average room rates and occupancy levels. The acquisition of Ansal Hotels and the addition of ITC Grand Central, Mumbai have powered the strong growth in this division. By setting up new properties in Bangalore and Delhi, ITC is all set to capitalise on the upcoming boom in the hotel industry.

The PBIT margin of this division expanded by a robust 576 basis points to 37.1% in Q4FY2006.

P&P business—expanding capacity to fuel margins

The P&P business of the company grew by 15.5% to Rs475.5 crore in the quarter, with the margin expanding by 340 basis points. The margin improvement was driven by the addition of 75,000 tonne of capacity at ITC's paperboard plant towards the end of 2005. The company plans to further expand the capacity in this space in the future.

Operating profit grew by 21%

Despite achieving a strong sales growth, ITC's reported operating profit margin (OPM) slipped by 165 basis points in the quarter. The margin dropped primarily due to a higher contribution of the revenues from the low-margin agri business and a marginal slip in the margins of the cigarette business.

Net profit grows by 35.9%

ITC's reported net profit stood at Rs567.5 crore, up 35.9% due to higher other income. The other income adjusted for one-time income (in Q4FY2005) grew by 25% to Rs75 crore.

Valuation

At the current market price of Rs177, the stock is attractively quoting at 20.1x its FY2008E earnings. We maintain our Buy recommendation on ITC with a price target of Rs220.

Earnings table

Particulars	FY2005	FY2006	FY2007E	FY2008E
Net sales (Rs crore)	7,639.5	9,790.5	10,817.2	12,674.6
y-o-y chg (%)	*18.0*	*28.2*	*10.5*	*17.2*
Net profit (Rs crore)	1,837.1	2,265.2	2,649.0	3,274.9
Shares in issue (crore)	372.0	372.0	372.0	372.0
EPS (Rs)	4.9	6.1	7.1	8.8
y-o-y chg (%)	*15.3*	*23.3*	*16.9*	*23.6*
PER (x)	35.8	29.1	24.9	20.1

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

Sharekhan Stock Ideas

Evergreen
HDFC Bank
Infosys Technologies
Reliance Industries
Tata Consultancy Services

Apple Green
Aditya Birla Nuvo
Associated Cement Companies
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Crompton Greaves
Godrej Consumer Products
Elder Pharmaceuticals
Grasim Industries
Hindustan Lever
Hyderabad Industries
ICICI Bank
Indian Hotel Company
ITC
Mahindra & Mahindra
Marico Industries
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Sintex Industries
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