investor's eye

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Take Five

Scrip	Reco Date	Reco Price	CMP	Target
BASF	18-Sep-06	220	**261**	300
HCL Tech	30-Dec-03	103	**349**	395
Infosys	30-Dec-03	689	**1,961**	2440
Madras Cement	17-Nov-05	1,498	**2,850**	4,000
Ranbaxy	24-Dec-03	533	**399**	558

KEI Industries

Ugly Ducking

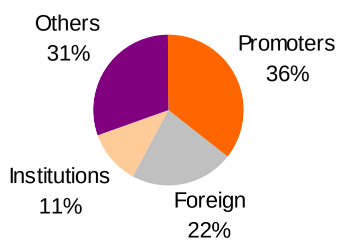
Stock Update

Q4FY2007 results: First-cut analysis

Buy; CMP: Rs75

Company details	
Price target:	Rs140
Market cap:	Rs448 cr
52 week high/low:	Rs130/41
NSE volume: (No of shares)	2.3 lakh
BSE code:	517569
NSE code:	KEI
Sharekhan code:	KEIINDUS
Free float: (No of shares)	3.8 cr

Shareholding pattern



Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	11.0	-18.0	6.1	-3.7
Relative to Sensex	6.1	-17.9	-0.8	-24.6

Result highlights

- KEI Industries' (KEI) net sales grew by 123% to Rs207.4 crore in Q4FY2007, in line with our expectations. However the net profit grew by 37.3% to Rs11.4 crore and the growth was below our expectations on account of rising raw material prices and a higher interest cost.
- The power cable segment's revenues grew by a robust 125% to Rs208 crore while the stainless steel wire segment's revenues grew by 97% to Rs25 crore.
- The operating profit margin (OPM) for the quarter declined by 490 basis points to 12.1% due to a rise in raw material prices. The raw material cost as a percentage of sales increased to 76.6% from 63.9% in Q4FY2006.
- The operating profit for the quarter grew by 59% to Rs25.1 crore.
- The interest expense for the quarter increased by 148% to Rs7.5 crore due to a rise in the interest rates and also because the company availed of higher working capital loans since the business is growing at a rapid pace. The depreciation cost for the quarter increased by 31% to Rs1.2 crore.
- For the full year, the net sales grew by 99% to Rs681.5 crore and the net profit grew by 54.3% to Rs40.1 crore.
- At the current market price of Rs75, the stock is quoting at around 11x its FY2007 earnings per share and 6.6x its FY2007 enterprise value/earnings before interest, depreciation, tax and amortisation. We maintain our Buy recommendation on the stock with a price target of Rs140. We shall be upgrading our FY2008 earnings estimates after analysing the annual report of the company. Watch this space.

Result table Rs (cr)

Particulars	Q4FY07	Q4FY06	% yoy chg	FY07	FY06	% yoy chg
Gross sales	233.4	105.4	121.4	681.5	342.5	99.0
Excise duty	26.0	12.5	108.0	77.6	43.1	80.3
Net sales	**207.4**	**92.9**	**123.2**	**603.9**	**299.4**	**101.7**
Total expenditure	182.3	77.2	136.3	517.1	254.5	103.2
Operating profit	25.1	15.8	59.0	86.8	44.9	93.4
Other income	0.4	-0.2	-270.8	0.6	0.9	-35.1
EBIDTA	25.5	15.5	64.1	87.4	45.8	90.8
Interest	7.5	3.0	148.9	23.7	9.5	151.0
Depreciation	1.2	0.9	30.8	5.7	2.7	110.0
PBT	**16.8**	**11.6**	**44.6**	**58.0**	**33.7**	**72.3**
Tax	5.4	3.3	62.6	17.8	7.6	133.6
PAT	11.4	8.3	37.3	40.1	26.0	54.3
Extraordinary items	0.0	0.0	-	0.0	0.0	-
Reported PAT	**11.4**	**8.3**	**37.3**	**40.1**	**26.0**	**54.3**
EPS	2.3	1.6	37.3	8.0	5.2	54.3
Margins						
OPM (%)	12.1	17.0		14.4	15.0	
PATM (%)	5.5	8.9		6.6	8.7	

Segment results

Particulars	Q4FY07	Q4FY06	% yoy chg	FY2007	FY2006	% yoy chg
Segment revenue						
Power cables	208.16	92.67	124.6	596.75	298.84	99.7
Stainless steel wires	25.45	12.93	96.8	85.17	43.69	94.9
PBIT						
Power cables	26.28	17.72	48.3	85.96	49.63	73.2
Stainless steel wires	2.48	0.63	293.7	7.84	1.18	564.4
PBIT margin (%)						
Power cables	12.62	19.12		14.40	16.61	
Stainless steel wires	9.74	4.87		9.21	2.70	

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

Allahabad Bank

Cannonball

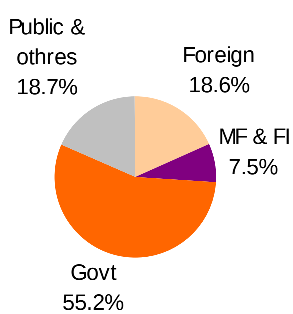
Stock Update

Growth at the cost of margins

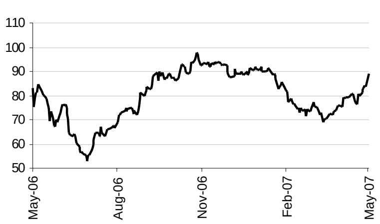
Buy; CMP: Rs89

Company details	
Price target:	Rs101
Market cap:	Rs3,976 cr
52 week high/low:	Rs99/53
NSE volume: (No of shares)	4.6 lakh
BSE code:	532480
NSE code:	ALBK
Sharekhan code:	ALLBANK
Free float: (No of shares)	20.0 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	10.6	-2.2	-11.6	4.5
Relative to Sensex	5.6	-2.1	-17.4	-18.1

Result highlights

- Allahabad Bank's net profit for Q4FY2007 declined by 16.5% year on year (yoy) to Rs125.7 crore. The same was lower than our estimate of Rs143.8 crore mainly due to a higher than expected tax liability of the bank during the quarter.
- During the quarter the bank's adjusted net interest income (NII) marginally declined by 1% yoy. Adjustment has been made for the one-time cash reserve ratio (CRR) interest income of Rs31 crore received during the quarter. The net interest margin (NIM) adjusted for the one-off item has decreased on year-on-year (y-o-y) and sequential bases. A significant increase in the cost of funds unmatched by a commensurate increase in the asset yields has resulted in a 73-basis-point y-o-y decline and a four-basis-point sequential decline in the NIM. The bank's aggressive loan growth policy funded by high-cost bulk deposits is taking a huge toll on its margins.
- The bank had booked Rs49.5 crore (credit balances in sundry accounts) as other income in FY2006. However, on Reserve Bank of India's (RBI) direction it reversed the entry during this quarter. Thus adjusted for the same the non-interest income was up by 19.9% yoy to Rs174.7 crore.
- The operating performance was not exciting despite a sedate 6.3% y-o-y rise in the operating expenses. The operating profit was up only 2.2% yoy with the core operating profit (excluding treasury) up by 9.2% on a y-o-y basis.
- Although provisions and contingencies declined by 23.4% yoy, yet tax provisions increased by 395% during the quarter. This resulted in a 16.5% y-o-y decline in the profit after tax (PAT) as against a 17.6% y-o-y rise at the profit before tax level.
- At the current market price of Rs89, the stock is quoting at 4.7x its FY2008E earnings per share, 2.8x pre-provision profits and 0.9x book value. The bank is available at attractive valuations compared with its peers, given its low price to book multiple and high return on equity. We maintain our Buy call on the stock with a price target of Rs101.

Result table Rs (cr)

Particulars	Q4FY07	Q4FY06	% yoy	FY07	FY06	% yoy
Net interest income*	454.1	458.7	-1.0	1,750.7	1,577.4	11.0
Non-interest income*	174.7	145.7	19.9	376.4	482.5	-22.0
Treasury	19.8	39.5	-49.9	74.4	149.3	-50.2
Fee income	113.5	71.6	58.6	313.0	228.3	37.1
Net income	628.8	604.4	4.0	2,127.1	2,059.9	3.3
Operating expenses	287.2	270.3	6.3	1,027.2	1,035.8	-0.8
Operating profit	341.6	334.1	2.2	1,099.9	1,024.1	7.4
Core operating profit (excluding treasury)	321.8	294.6	9.2	1,025.5	874.8	17.2
Provisions & contingencies	130.2	170.1	-23.4	264.5	269.3	-1.8
PBT	193.0	164.1	17.6	835.4	754.9	10.7
Provision for taxes	67.3	13.6	395.6	85.2	48.7	74.9
Net profit	125.7	150.5	-16.5	750.1	706.1	6.2

*Adjusted for CRR interest income of Rs 31 crore from NII and credit of Rs 49.5 crore of income booked in FY2006 written back in Q4FY2007 as per RBI directives.

Margins remain under pressure due to aggressive growth plans

The bank's adjusted NII declined marginally by 1% yoy to Rs454 crore. The NIM of the bank remained under pressure on both y-o-y and sequential bases. The total assets of the bank grew by 20.8% yoy and 2.9% qoq driven by a 43.8% y-o-y growth in the advances. Deposits rose by 22.8% with the bank's current and savings account (CASA) ratio at 38%, down by 100 basis points on a y-o-y basis. The bank has grown its assets too fast at the cost of its margins, its adjusted interest income grew by 31.3% yoy while interest expended grew by 56.9% yoy. Thus the interest cost has far outpaced the growth in the core operational interest income which has resulted in a 73-basis-point decline in the NIM on a y-o-y basis and a four-basis-point drop on a sequential basis. We feel the NIM would remain under pressure going forward due to an aggressive expansion in the loan book and a stable to declining CASA ratio.

Yield analysis (%)

Particulars	Q4FY07	Q4FY06	Q3FY07	yoy chng in bps	qoq chg in bps
Yield on funds	8.28	7.90	8.23	38	5
Cost of funds	5.52	4.41	5.43	111	9
NIM	2.76	3.49	2.80	-73	-4

Source: Company, Sharekhan estimates based on quarterly closing balances.

Adjusted non-interest income up 20% yoy

The reported non-interest income was down by 14% yoy but the bank had booked Rs49.5 crore (credit balances in sundry accounts) as other income in FY2006. On the RBI's direction it reversed the entry during this quarter. Thus adjusted for the same the non-interest income was up by 19.9% yoy to Rs174.7 crore. The fee income was up by 58.6% yoy driven by the processing fees charged during the quarter (the same had been waived off earlier).

Non-interest income (Rs crore)

Particulars	Q4FY2007	Q4FY2006	% yoy chg	% qoq chg
Trading	19.8	39.5	-49.9	-53.8
CEB	113.5	71.6	58.6	79.0
Forex	19.1	18.1	5.6	672.5
Dividend	11.1	34.0	-67.2	60.5
Others	39.6	9.2	328.7	11.1
Amortisation	-28.4	-26.6	6.5	10.2
Total	174.7	145.7	19.9	39.2
Non-int. income (excl. treasury, others & amortisation)	143.7	123.6	16.3	45.9

Source: Company, Sharekhan Research

Net NPA reports a sequential increase

The gross non-performing asset (NPA) ratio improved to 2.61% from 3.06% in December 2006 and at the absolute level the gross NPA declined by Rs90 crore to Rs1,094 crore. However, the net NPA ratio increased to 1.07% from 0.72% in December 2006. The provision coverage declined from 77% to 60% sequentially.

Particulars	Q4FY2007	Q4FY2006	Q3FY2007
Gross NPA (Rs crore)	1,093.6	1,183.8	1,183.51
Net NPA (Rs crore)	440.2	246.1	273.01
(%) Gross NPA	2.61	3.94	3.06
(%) Net NPA	1.07	0.84	0.72
Provision coverage (%)	60	79	77

Capital adequacy remains comfortable

The capital adequacy ratio (CAR) of the bank stood at 12.5% with the Tier-I CAR at 8.5% as on March 2007. The same is adequate to sustain growth in its assets and comply with the Basel II norms going forward.

Valuation and view

At the current market price of Rs89, the stock is quoting at 4.7x its FY2008E earnings per share, 2.8x pre-provision profits and 0.9x book value. The bank is available at attractive valuations compared with its peers, given its low price to book multiple and high return on equity. We maintain our Buy call on the stock with a price target of Rs101.

Earnings table

Year to 31 March	FY04	FY05	FY06	FY07E	FY08E
Net profit (Rs cr)	463.6	541.9	706.4	750.1	839.6
Shares in issue (cr)	34.7	34.7	44.7	44.7	44.7
EPS (Rs)	13.4	15.6	15.8	16.8	18.8
% y-o-y change	*18.6*	*16.9*	*1.2*	*6.2*	*11.9*
PE (x)	6.7	5.7	5.6	5.3	4.7
P/PPP (x)	3.5	2.9	3.9	3.3	2.8
Book value (Rs/share)	38.1	49.8	68.3	80.0	94.3
P/BV (x)	2.3	1.8	1.3	1.1	0.9
Adj book value	27.6	42.0	62.8	70.1	86.1
P/ABV (x)	3.2	2.1	1.4	1.3	1.0
RONW (%)	19.7	35.6	26.8	22.7	21.6

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

Bajaj Auto

Apple Green

Stock Update

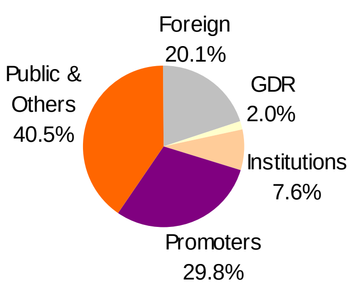
Bruised by demerger, disclosures

Buy; CMP: Rs2,248

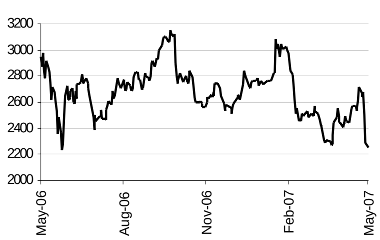
Company details

Price target:	Rs2,500
Market cap:	Rs22,695 cr
52 week high/low:	Rs3,259/2,085
NSE volume: (No of shares)	2.9 lakh
BSE code:	500490
NSE code:	BAJAJAUTO
Sharekhan code:	BAJAJ
Free float: (No of shares)	6.9 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-8.4	-24.0	-10.8	-22.9
Relative to Sensex	-12.5	-24.0	-16.6	-39.6

Result highlights

- The Q4FY2007 results of Bajaj Auto Ltd (BAL) are in line with our expectations. The net sales grew by 6.8% to Rs2,313.6 crore.
- The operating profit of the company declined by 23.2% to Rs326.3 crore as the operating profit margin (OPM) declined by 550 basis points to 14.1%. However, the margins are stable on a sequential basis. The net profit before extraordinary items for the quarter declined by 3.9% to Rs320.75 crore.
- The company announced its long pending demerger, through which two new companies would be created, namely Bajaj Auto Ltd (BAL; new), comprising the manufacturing business, and Bajaj Finserv Ltd (BFL), comprising the insurance, auto finance and wind power businesses. The existing company would be renamed as Bajaj Holdings and Investment Ltd (BHIL). The shareholders would hold 70% in the new companies directly, while 30% of their holding would be routed through the holding company BHIL. We view this process as a negative, as the listed holding company would suffer from a holding company discount.
- For every one share held in the existing BAL (future BHIL), the shareholders would continue to hold one share in BHIL, get one share of the new BAL of Rs10 each and one share of BFL of Rs5 each.
- In another disclosure, BAL has also declared that Allianz has a call option to raise its stake in the life insurance business to 74% from the current 26% at a nominal pre-determined price till 2016. In all likelihood, the foreign direct investment (FDI) norms for insurance are expected to get relaxed till then and hence BAL's stake is likely to get reduced.
- We are downgrading our sum-of-the-parts (SOTP) target on BAL to Rs2,500, valuing the new BAL at Rs1,254 per share and BFL at Rs449 per share. Taking into account the cash and investment portfolio of BAL and also BHIL's stake in the two new companies, we value BHIL at Rs835. We maintain our Buy call on the stock.

Result table Rs (cr)

Particulars	Q4FY07	Q4FY06	% yoy	FY07	FY06	% yoy
Net sales	2313.6	2165.9	6.8	9,520.4	7,667.9	24.2
Total expenditure	1987.3	1740.9		8,103.4	6,311.6	
Operating profits	326.3	425.0	-23.2	1,417.0	1,356.3	4.5
Other income	157.7	103.1		555.6	438.5	
EBIDTA	484.0	528.1	-8.3	1,972.6	1,794.7	9.9
Interest	2.4	0.1		5.3	0.3	
Depreciation	45.8	46.8		190.3	191.0	
PBT	435.8	481.3		1,777.0	1,603.4	
Tax	115.1	147.6		490.1	479.1	
Profit after tax	320.8	333.6	-3.9	1,286.9	1,124.3	14.5
Extraordinary items	-12.4	13.3		23.7	2.5	
Reported PAT	333.2	320.3	4.0	1263.2	1121.7	12.6
EPS	30.5	34.3		122.4	111.4	
OPM(%)	14.1	19.6		14.9	17.7	

Sales performance

	Q4FY07	Q4FY06	% growth	FY07	FY06	% growth
Other two-wheelers	7,895	13,540	-41.7	20,480	116,342	-82.4
Motorcycles	532,864	533,018	0.0	2,376,519	1,912,224	24.3
Total two-wheelers	540,759	546,558	-1.1	2,396,999	2,028,566	18.2
Three-wheelers	84,598	72,638	16.5	321,796	252,006	27.7
Grand total	625,357	619,196	1.0	2,718,795	2,280,572	19.2

Results in line with expectations

BAL's Q4FY2007 results are in line with expectations. The net sales for the quarter grew by 6.8% to Rs2,313.6 crore, driven by a realisation growth of 5.8% and a volume growth of 1%. The company has maintained its market share in the premium segment motorcycles, whereas in the economy segment motorcycles it has lost market share due to aggressive pricing by Hero Honda Motors.

The operating profit of the company declined by 23.2% to Rs326.3 crore as the OPM declined by 550 basis points to 14.1%, due to a change in the product mix and increase in raw material cost. However, the margin was stable on a sequential basis. However, with a higher other income of Rs157.7 crore, stable depreciation and lower taxes, the company was able to record a 3.9% decline in the pre-extraordinary profit to Rs320.75 crore.

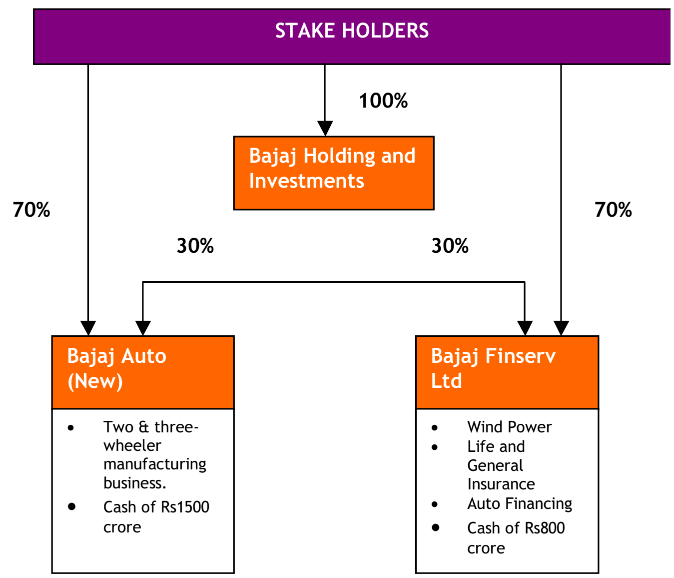
Three-way demerger disappointing

As per the scheme of the demerger, the existing company would be renamed Bajaj Holdings and Investments and two new companies would be created, namely Bajaj Auto (new), which would consist of the two- and three-wheeler manufacturing business, and Bajaj Finserv, which would comprise the wind power, insurance and financing businesses. All shareholders in the existing BAL would become shareholders in each of the new companies. For every share held in the existing company, the shareholders would:

- continue to hold one share of BHIL (the existing BAL) of face value of Rs10 each, fully paid up;
- be allotted one share of the new BAL (the existing BHIL) of face value of Rs10 each, fully paid up; and
- be allotted one share of BFL of face value of Rs5 each, fully paid up.

We view this demerger process as a negative for the stock, as the same would reduce the voting rights of the minority shareholders in the new companies and also route 30% of their holding through a holding company, which would suffer a holding company discount upon listing.

New structure



New disclosures relating to insurance company a negative surprise

BAL has disclosed that its insurance partner Allianz has a call option to increase its stake in the insurance joint ventures at a nominal pre-determined price.

In case of Bajaj Allianz General Insurance Co., Allianz SE can exercise call option to increase its holding to 50% from the present 26%, subject to regulatory approvals. In case the call option is exercised by Allianz up to the expiry of 15 years from the subscription date, ie up to April 22, 2016, the price will be Rs10 per share plus interest at 16% per annum compounded annually from April 23, 2001 to the date of payment.

In case of Bajaj Allianz Life Insurance Co., Allianz SE can exercise call option to increase its holding to 74% from the present 26%, subject to regulatory approvals. In case the call option is exercised by Allianz up to the expiry of 15 years from the subscription date, ie up to April 22, 2016, the price will be Rs5.42 per share plus interest at 16% per annum compounded annually from April 23, 2001 to the date of payment.

As things look now, there is a strong possibility that the FDI ownership rules may be relaxed by 2016 and hence the possibility of the call expiring is virtually nil.

Revision in estimates

We have revised our volume estimates to 11% in FY2008, mainly due to a slowdown in the domestic market. The slowdown is due to rising interest rates and control of liquidity. BAL has underperformed the industry in the last couple of months, due to new product launches by competitors at aggressive prices which caused BAL to lose market share. We expect the volumes to pick up only after Q2FY2008, after the launch of BAL's new motorcycle.

Downgrading price target

In view of the slowdown in its core business, new disclosures in the insurance business and the three-way split, we are downgrading our SOTP price target to Rs2,500.

Earnings table

Particulars	FY05	FY06	FY07E	FY08E	FY09E
Net profit (Rs cr)	627.2	999.3	1,286.9	1,322.1	1,286.9
EPS (Rs)	62.0	98.7	127.2	130.6	146.3
% y-o-y chg	*-0.5*	*59.3*	*28.8*	*2.7*	*12.0*
PER	37.1	23.3	18.1	17.6	15.7
P/B	5.6	4.9	4.2	3.6	3.2
EV/EBIDTA	27.9	16.1	12.9	11.4	9.1
ROCE (%)	18.8	25.5	27.1	24.8	24.6
RONW (%)	15.2	20.9	23.2	20.6	20.1

Sum-of-parts valuation (SOTP)

Bajaj Auto (New)	
EPS (Rs)	95.9
Multiple (x)	12
Cash & Equivalents (Rs)	103.7
Value	**1254.3**
Bajaj Finserv	
Life Insurance	329.6
General Insurance	19.5
Auto Financing	45.0
Cash	55.3
Total	**449.4**
Bajaj Holding & Investments Ltd	
Stake in Bajaj Auto (30%)	350.6
Stake in BFL (30%)	134.8
Total	485.4
Holding co discount	50%
Discounted Value per share	242.7
Cash & Invst	593.0
Value per share	**835.7**
Price target	**2539.4**

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

Sundaram Clayton

Apple Green

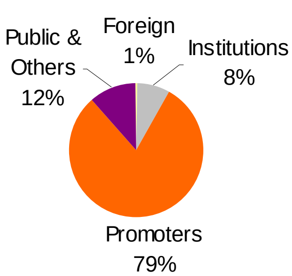
Stock Update

Spinning off its brake division

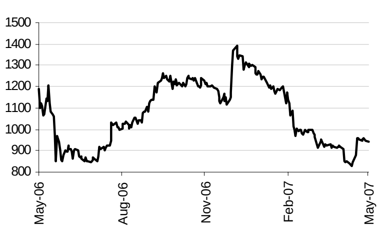
Buy; CMP: Rs941

Company details	
Price target:	Rs1,350
Market cap:	Rs 1,783 cr
52 week high/low:	Rs1,410/779
NSE volume: (No of shares)	2,273
BSE code:	520056
NSE code:	SUNDRMCLAY
Sharekhan code:	SUNCLA
Free float: (No of shares)	0.38 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	2.2	-19.6	-20.7	-24.1
Relative to Sensex	-2.3	-19.5	-25.9	-40.5

Key points

- Sundaram Clayton has finally decided to spin off its brake division into a subsidiary. The new entity will be called WABCO-TVS and will be listed on the stock exchange.
- We believe that the demerger would help both the companies to focus on their core areas. WABCO would control the brake division while the TVS group would run the casting division. The higher control of WABCO in the brake division is in line with WABCO's strategy and may open new outsourcing opportunities for the brakes company as WABCO is scouting for a low-cost producer of brakes.
- For FY2008, Sundaram Clayton has raised its capex plans to Rs200 crore, out of which Rs90 crore would be spent on the brake business and Rs110 crore on the die-casting business.
- We are introducing our FY2009 estimates for Sundaram Clayton. We expect the company to record a revenue growth of 17% and a profit growth of 26% during the year. We expect its earnings to reach Rs74.5 in FY2009.

Event

Sundaram Clayton has finally decided to spin off its brake division into a subsidiary. The new entity will be called WABCO-TVS and will be listed on stock exchange. The co-promoter WABCO would hold a 51% stake in this new air brake company while the TVS group would hold a 29% stake. Eventually, we believe that WABCO would also buy out the entire stake of the TVS group in this business. Sundaram Clayton would be managed by the TVS group (holding a 51% stake) and comprise the casting business and its investments in the group companies. Sundaram Clayton's shareholders will get one share in WABCO-TVS for each held. Due to the spin-off, the face value of the Sundaram Clayton share will be halved to Rs5.

Impact

In our previous report, we had mentioned that the demerger would be one of the triggers for the stock and that the same shall yield strong benefits in the long term for the company. We believe that the demerger would help both the companies to focus on their core areas. WABCO would control the brake division while the TVS

Earnings table

Particulars	FY2005	FY2006	FY2007E	FY2008E	FY2009E
Net sales (Rs cr)	536.3	629.3	816.3	1,001.7	1,172.6
Net profit (Rs cr)	52.5	68.6	92.8	112.2	141.3
EPS	27.7	36.2	48.9	59.1	74.5
% y-o-y chg	*13.4*	*30.7*	*35.1*	*20.9*	*26.0*
PER	25.3	19.4	14.3	11.9	9.4
P/B	7.4	6.2	5.1	4.2	3.4
EV/EBIDTA	19.9	14.5	10.7	9.0	6.9
ROCE (%)	26.7	27.8	31.2	31.5	32.7
RONW (%)	21.9	23.7	26.5	26.5	26.8

group would run the casting division. The higher control of WABCO in the brake division is in line with WABCO's strategy and may open new outsourcing opportunities for the brake company as WABCO is scouting for a low-cost producer of brakes. At present, we understand that the brake business enjoys earnings before interest, depreciation, tax and amortisation (EBIDTA) margin of about 20-21% while the EBIDTA margin of the die-casting division stands at around 15-16%.

Capex for FY2008 raised to Rs200 crore

The capital expenditure (capex) plan for the brake division has also been raised, which is in line with the company's long-term plans for the business. For FY2008, Sundaram Clayton has raised its capex plans to Rs200 crore, out of which Rs90 crore would be spent on the brake business and Rs110 crore on the die-casting business.

Valuation and view

We maintain our positive outlook on the company considering the strong performance that it has delivered in the past, its high productivity levels and strong future outlook. We also believe that a huge replacement demand for brakes would be triggered with the higher use of the anti-lock braking system in commercial vehicles. With the demerger, the focus of both the parents would increase on their respective business, which should yield substantial gains for the company. Also, this further opens the opportunity for WABCO-TVS to become an outsourcing hub for its parent, WABCO. The company is not witnessing any slowdown currently and expects the effect of the same to be more apparent from the second half of the year.

We are introducing our FY2009 estimates for Sundaram Clayton. We expect the company to record a revenue growth of 17% in FY2009 and its margins to improve further to 16.5% on the back of better economies achieved due to high capacity utilisation and ramp-up in the newly added capacities. We expect the profits to grow at 26% during the year and the earnings to reach Rs74.5 in FY2009. While computing the company's value, we have assumed a 75% discount to its total investment. After adjusting for the same, the stock is currently trading at 9.4x its stand-alone FY2009E earnings and 6.9x its EBIDTA. We maintain our Buy recommendation with a price target of Rs1,350.

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

Sun Pharmaceutical Industries

Ugly Duckling

Stock Update

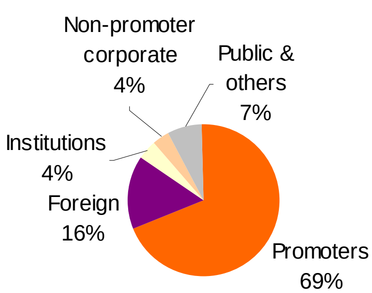
Q4 first-cut analysis and acquisition highlights

Buy; CMP: Rs1,064

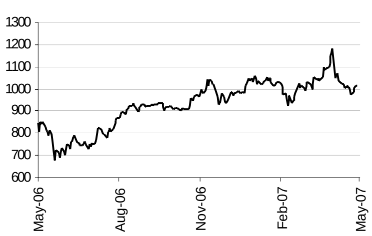
Company details

Price target:	Rs1,297
Market cap:	Rs20,578 cr
52 week high/low:	Rs1,196/640
NSE volume: (No of shares)	2.3 lakh
BSE code:	524715
NSE code:	SUNPHARMA
Sharekhan code:	SUNPHARM
Free float: (No of shares)	6.1 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-12.0	-1.0	4.8	19.3
Relative to Sensex	-15.9	-0.9	-2.0	-6.5

Result highlights

- The consolidated net sales of Sun Pharmaceutical Industries (Sun Pharma) grew by 33.8% year on year (yoy) to Rs544.2 crore in Q4FY2007. The strong growth was driven by an increase of 43.4% in the domestic business and a 22.4% growth in the exports.
- Its US subsidiary, Caraco Pharma (Caraco), continued its growth momentum. Caraco's sales grew by 32% yoy to $32.7 million in Q4FY2007 and by 41% to $117 million in FY2007.
- Sun Pharma's operating profit margin (OPM) expanded by 610 basis points on a lower base to 28.3%, resulting in a 70% spike in its operating profit to Rs154.5 crore.
- Sun Pharma's other income was higher by 24.2% to Rs94.2 crore, which was more than double of our estimate of Rs42.7 crore for the quarter.
- With an impressive revenue growth in both domestic formulation and export businesses, a 610-basis-point expansion in the OPM and a higher than expected other income, Sun Pharma's net profit for Q4FY2007 stood at Rs212.1 crore, up 48.4% yoy. The net profit was ahead of our estimate of Rs184.4 crore.
- For the full year, the company's sales were up 30% at Rs2,132.1 crore and the OPM expanded by 190 basis points to 31.9%, resulting in a net profit of Rs774.1 crore (up 35%). The full-year net profit was above our expectations of Rs737.2 crore.
- Between Sun Pharma and its US subsidiary Caraco 34 abbreviated new drug applications (ANDAs) are now approved compared with 22 at the end of 2006. A

Result table Rs (cr)

Particulars	Q4FY06	Q4FY07	% yoy	FY 2006	FY 2007	% yoy
Net sales	406.7	544.2	33.8	1637.2	2132.1	30.2
Expenditure	315.9	389.7	23.4	1146.2	1452.3	26.7
Adjusted RM cost	120.2	135.5	12.7	487.2	585.0	20.1
Staff cost	43.2	66.4	54.0	141.6	255.8	80.6
Other indirect taxes	8.9	12.9	45.4	42.4	52.8	24.7
Other expenditure	92.8	103.4	11.4	321.7	300.9	-6.4
Recurring R&D expense	51.0	71.6	40.4	153.4	257.7	68.0
Operating profit	90.9	154.5	70.0	492.2	679.8	38.1
OPM (%)	22.3	28.4		30.0	31.9	
Other income	75.4	94.2	24.9	136.3	225.3	65.3
EBITDA	166.3	248.7	49.6	153.4	257.7	68.0
EBIDTA margin (%)	40.9	45.7		38.4	42.5	
Interest expense	0.0	0.0	0.0	15.6	0.0	-100.0
Depreciation / Amortisation	18.4	20.1	9.0	61.0	81.8	34.0
PBT	147.8	228.6	54.7	551.9	823.3	49.2
Taxes	11.3	-1.8		23.9	-6.7	
PAT	136.5	230.4	68.8	528.0	830.0	57.2
Minority interest (Loss) / Profit	-6.5	18.3		-0.3	55.9	
Extraordinary items	0.0	0.0		-45.4	0.0	
PAT	142.9	212.1	48.4	573.6	774.1	-
Pat margin (%)	35.1	39.0		35.0	36.3	

total of 16 ANDAs have been filed during the fourth quarter (eight each by Sun Pharma and Caraco). With this, 77 ANDAs await the approval of the US Food and Drug Administration (USFDA) including seven tentative approvals.

- The company has guided for a conservative 15-18% consolidated revenue growth for FY2008 (which is less than our estimate of a 30% growth) whereas Caraco has guided to a growth of 30% during the year. Sun Pharma expects to maintain the OPM in FY2008.

Sun Pharma agrees to acquire Taro for $454 million

Sun Pharma together with its subsidiaries has signed definitive agreements to acquire Taro. The highlights of the acquisition are as follows.

Sun Pharma, in an all-cash deal, has agreed to acquire Taro for $454 million, out of which it will pay $230 million towards 100% equity and the balance $224 million towards refinancing of Taro's debt. The acquisition is taking place at 1.5 times its CY2005 sales (CY2006 numbers are yet to be disclosed).

In addition, to provide immediate liquidity for Taro, Sun Pharma will provide interim financing to the extent of USD45 million.

Taro is one of the leading generic manufacturers with established subsidiaries, manufacturing bases and products across the USA, Israel and Canada. The point to note is that North America represents more than 90% of Taro's sales.

Taro has a strong franchise in dermatology and topical products, in addition to the products in cardiovascular, neuropsychiatric and anti-inflammatory therapeutic categories.

Taro US has more than 100 ANDA drug approvals in the USA alone. One new drug application as well as 26 ANDAs are awaiting approval of the USFDA.

Taro has large, world class sites with necessary regulatory approvals in Canada and Israel that manufacture topical creams and ointments, liquids, capsules and tablet dosage forms complementing Sun Pharma's existing manufacturing and development capabilities in the USA. Additionally, Taro manufactures active pharmaceutical ingredients, including complex chemistry and steroids that are made at its site in Israel. Over USD225 million has been invested by Taro in capital expenditure (capex) in the last three years which provides Sun Pharma with additional capabilities.

At 12-16% of sales, Taro has invested over USD190 million in R&D so far. Among the active projects in drug discovery is its lead molecule T-2000, which is a non-sedating barbiturate that is being developed for essential tremors. T-2000 is in additional phase II studies in Canada. This is in addition to projects in formulation development for ANDA filing and process chemistry for APIs, organic and steroid chemistry. A novel formulation of Ovide®, a lice treatment, is another interesting product in their portfolio of proprietary products.

By the acquisition Sun Pharma intends to build on Taro's expertise in dermatology and paediatrics, along with specialty and generic pharmaceuticals, and over-the-counter products. Also, it plans to exploit the distribution strength of Taro in the USA, Canada, the UK and Israel. This would provide easy entry for Sun Pharma into Canadian markets.

With the addition of 170 talented scientists, Sun Pharma is looking forward to increasing the number of product filings of higher complexity. The acquisition is a strategic one, as Sun Pharma can exploit Taro's market positioning in the USA for its own expansion.

The Sun Pharma management has indicated to complete the acquisition in three to four months and plans to improve the profitability of the company in 12-18 months.

Valuation & view

Sun Pharma has guided for a conservative 15-18% consolidated revenue growth for FY2008 (which is lesser than our estimate of 30%) whereas Caraco has guided for a 30% growth during the year. Sun Pharma has given a conservative revenue guidance, as it would focus on integrating the acquired business of Taro. Sun Pharma expects to maintain the OPM in FY2008.

Sun Pharma, in an all-cash deal, has agreed to acquire Taro Pharma for $454 million. Taro is one of the leading generic players in North America with reputed R&D capabilities in filing dossiers for complex and less competitive products. Due to pricing issues Taro suffered substantial losses during CY2006. But the company is yet to share the financial numbers for CY2006. So in order to incorporate the financials of Taro and the less than expected revenue guidance of Sun Pharma, we are reviewing our numbers and would come out with a detailed update on the company soon. At the current price of Rs1,064, the stock is trading at 22.2x of our FY2008E earnings. However, considering the track record of Sun Pharma in acquiring impaired assets and converting them into profitable acquisitions without diluting the equity, we maintain our Buy recommendation with price target of Rs1,297. The price target has been reduced from our earlier one of Rs1,341, as we have deducted the value (ie Rs54) of Sun Pharma Advanced Research Company (SPARC) post-demerger. The company has recently demerged its innovative research division into a separate company called SPARC.

Sharekhan Stock Ideas

Evergreen

HDFC Bank
Infosys Technologies
Reliance Industries
Tata Consultancy Services

Apple Green

Aditya Birla Nuvo
ACC
Apollo Tyres
Bajaj Auto
Bank of Baroda
Bank of India
Bharat Bijlee
Bharat Electronics
Bharat Heavy Electricals
Bharti Airtel
Canara Bank
Corporation Bank
Crompton Greaves
Elder Pharmaceuticals
Grasim Industries
HCL Technologies
Hindustan Lever
ICICI Bank
Indian Hotels Company
ITC
Mahindra & Mahindra
Marico
Maruti Udyog
Lupin
Nicholas Piramal India
Omax Autos
Ranbaxy Laboratories
Satyam Computer Services
SKF India
State Bank of India
Sundaram Clayton
Tata Motors
Tata Tea
Unichem Laboratories
Wipro

Cannonball

Allahabad Bank
Andhra Bank
Cipla
Gateway Distriparks
International Combustion (India)
JK Cement
Madras Cement
Shree Cement
Transport Corporation of India

Emerging Star

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Aban Offshore
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Federal-Mogul Goetze (India)
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New Delhi Television
Nucleus Software Exports
Orchid Chemicals & Pharmaceuticals
ORG Informatics
Tata Elxsi
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Thermax
UTI Bank

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BASF India
Ceat
Deepak Fertilisers & Petrochemicals Corporation
Fem Care Pharma
Genus Power Infrastructures
Hexaware Technologies
ICI India
India Cements
Indo Tech Transformers
Jaiprakash Associates
JM Financial
KEI Industries
NIIT Technologies
Punjab National Bank
Ratnamani Metals and Tubes
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