investor's eye

Index
Sharekhan Special >> Monetary policy preview
Stock Update >> Alphageo India
Stock Update >> Maruti Udyog
Stock Update >> KEI Industries
Stock Update >> Apollo Tyres
Stock Update >> Union Bank of India

Take Five

Scrip	Reco Date	Reco Price	CMP	Target
Bharat Bijlee	29-Nov-04	192	**1,408**	1,730
BEL	25-Sep-06	1,108	**1,395**	1,525
Ceat	28-Nov-06	122	**146**	190
F-M Goetze	18-Jan-07	385	**390**	559
Lupin	06-Jan-06	403	**570**	670

Sharekhan Special

Monetary policy preview

Another rate hike looks imminent

We feel a 25-basis-point hike in the repo and reverse repo rates may be on the cards. All the current indicators, which the Reserve Bank of India (RBI) normally considers, are above their target zone or rate. This increases the likelihood of another rate hike. In a recent poll conducted by Reuters among the top Indian banks and investment companies, almost all voted for a hike in both the repo and the reverse repo rate in the forthcoming policy review meet on January 31, 2007. The market looks to be ready for a 25-basis-point hike in the key rates. However any higher measure of hike could come as a surprise and affect market sentiments.

Bank rate may not be raised

We feel the bank rate may not be raised currently as it is the RBI's medium-term policy rate and nothing seems to have drastically changed on that front. The inflation rate has breached the 6% level all right but we feel the same may come down in the medium term due to the recent measures taken by the government, such as the customs duty cut and the import of food grains. Only two respondents out of the fifteen voted for a 25-basis-point hike in the bank rate in the Reuters poll.

Particulars	RBI's target range (%)	Current yoy growth rates (%)	Measures taken so far in FY2007
Inflation	5 - 5.5	5.95	Reverse repo rate hiked twice in June and July 2006 by 25 basis points each; currently at 6%.
M3 growth	15.5	20.00	Repo rate hiked thrice in June, July and October 2006 by 25 basis points each; currently at 7.25%. CRR hiked by 50 basis points in two phases during December 2006.
Credit growth	20.0	30.00	

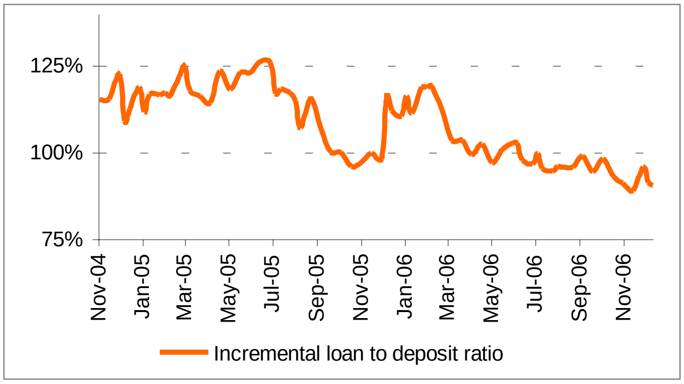
Factors to influence domestic interest rates in the near term

Particulars	Outlook for next three months
Global interest rates and inflation	Look benign with US Fed not raising rates and Japan adopting a wait-and-watch policy.
India's current account and BOP policy	Current account deficit may widen on higher imports, but capital account flows should be able to finance the deficit.
Money supply and nominal GDP growth	Money supply continues to be above RBI's target rate which remains a cause for concern.
Incremental loan/deposit ratio	Expected to continue its decline, as banks run out of excess SLR.
Government finances	Robust tax collections have helped to improve the fiscal performance; going forward lower government borrowings would help in freeing more funds for private investments.
Existing system liquidity	Currently liquidity in the system has improved but the same still remains low from the July levels. It is expected to improve with government spending and foreign inflows.
Inflation	Continues to be above RBI's target zone. With state elections round the corner, inflation management may become a key issue for the government. We have seen some measures like customs and import duty cuts. Expect some more duty cuts in the budget.

Credit growth continues unabated

Despite RBI's move to hike the key policy rates and raise the cash reserve ratio (CRR) by 50 basis points year on year, the credit growth continues to be ~30%. The credit/deposit ratio is around 74% while the investment/deposit ratio has come down to 30% levels from the highs of 35% in the last couple of years. Most of the banks' statutory liquidity ratio (SLR) is at 26-27%, which is very close to their threshold level of 25% SLR requirement. Banks have been reducing their investment holdings to fund credit growth. The incremental loan/deposit ratio has been steadily coming down with banks running out of excess SLR securities.

Incremental loan/deposit ratio

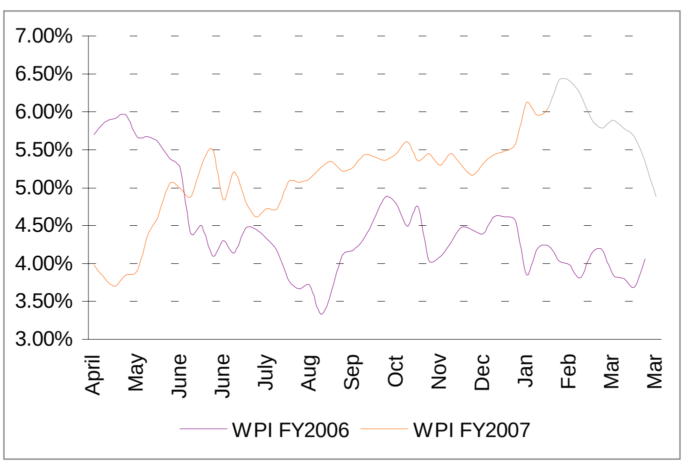


Source: RBI

Inflation above the comfort zone

The current inflation rate at 6.12% is much above the comfort zone (5-5.5%) of the RBI. The inflation rate has touched the 6% level mainly due to the rise in the price of primary articles owing to higher food article prices. A lower base in the corresponding period of the previous year has also played its part. We expect the inflation rates to moderate in the medium term, however the rates may persist above the 6% level in the near term.

Wholesale Price Index y-o-y change



Source: Office of the economic advisor

Customs duty cut would help moderate inflationary pressures

With the state elections round the corner, the government has its hands full to curb inflation. The recent reduction announced in customs duties would help curb inflationary pressures going forward. Primary articles and manufactured products have been the key drivers of the recent spurt in inflation. The reduction in customs duty in select raw materials would provide a broad-based approach to tame the rising inflationary pressures. This fiscal measure will help cap the ability of the domestic producers to hike the prices of these goods and ultimately lead to moderation in the manufactured products group, which has recently seen a rise in its pricing power.

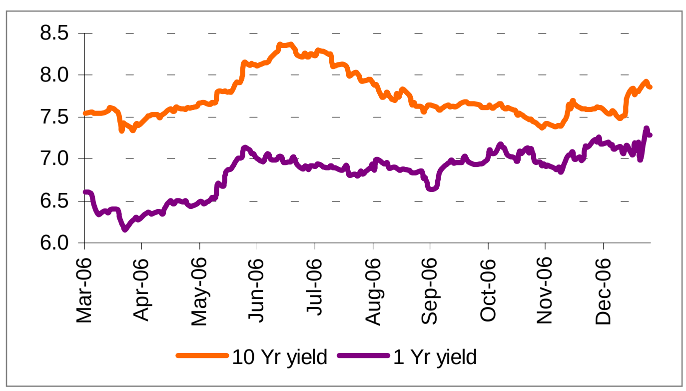
RBI to have SLR flexibility

Although the year-on-year credit growth remains robust at 30%, the deposit growth at 20% is lagging behind. Currently banks need to hold 25% of their deposits in government and other approved securities. Currently the RBI does not have the power to lower the SLR requirement from 25%. But the government has been working on a proposal to empower the central bank to set the SLR requirement floor below 25% and it is in the final stages of getting the President's assent. We feel even if the RBI is granted the power to lower the SLR during the policy review meet, the apex bank may not choose to exercise it. Nevertheless, the move would provide the RBI greater flexibility in the future to manage system liquidity.

Bond market appears to have factored in the rate hike

After the latest inflation data of 6.12% was released on January 19, 2007, the one-year benchmark yield closed almost 36 basis points above its previous close. The sharp rise in the bond yield indicates that the market feels the RBI would further hike the rates. The yields had earlier firmed up after the 50-basis-point hike in the CRR announced in December 2006. Overall, the bond market seems to have factored in another rate hike.

10-year and 1-year benchmark yields

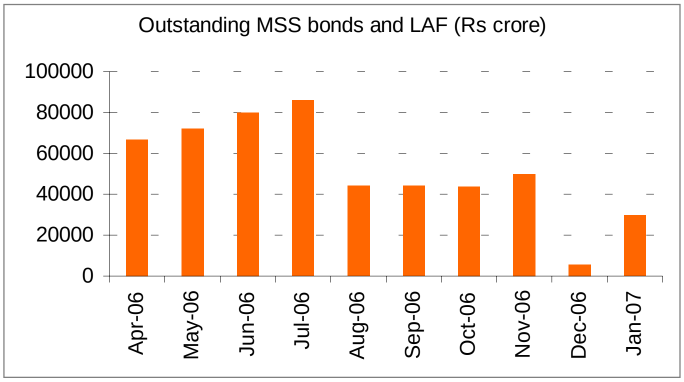


Source: Bloomberg

Liquidity in the system has shrunk

The system liquidity has shrunk to some extent; the advance tax outflows and the CRR hike had drastically lowered the liquidity in December 2006. Although the situation has improved since then, yet liquidity remains lower than the earlier levels.

Trend in banking system liquidity



Source: RBI

Deposit rates on the rise

State Bank of India and ICICI Bank have hiked their deposit rates once again by 50-100 basis points each after the rate hikes announced in December 2006 in the wake of the CRR hike. The demand for credit is not slowing down significantly and banks are required to offer much higher rates to attract deposits. Mid-sized banks like Union Bank of India have also announced a rate hike and we expect the other banks to follow suit. HDFC has said that if the RBI raises rates, then it would need to hike its lending rates again. Banks may also consider revising their lending rates to protect their margins.

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

Alphageo India

Emerging Star

Stock Update

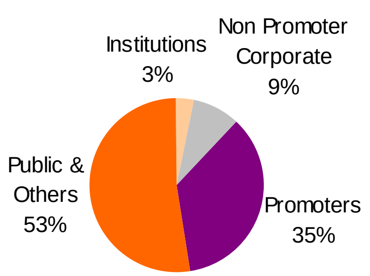
Price target revised to Rs270

Buy; CMP: Rs203

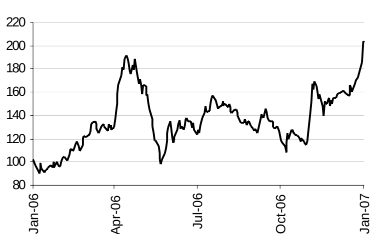
Company details

Price target:	Rs270
Market cap:	Rs100 cr
52 week high/low:	Rs219/89
BSE volume: (No of shares)	28,542
BSE code:	526397
Sharekhan code:	ALPHAGEO
Free float: (No of shares)	0.32 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	31.4	61.4	65.1	93.7
Relative to Sensex	25.4	44.2	19.0	29.2

Result highlights

- After the lacklustre performance in the first half of FY2007, Alphageo India (Alphageo) has reported a robust growth of 718% in its revenues to Rs13.2 crore for Q3FY2007. The revenues were largely contributed by the execution of the 3D survey order located in Rajasthan that the company had received from Essar Oil.
- The operating profit margin (OPM) stood at 50.9%, up from 33.8% reported in Q3FY2006. The margin improvement was driven by the better revenue bookings on the back of the large order located in Rajasthan as compared with the concentration of work in the tough terrain of north-east area in Q3FY2006.
- Consequently, the earnings stood at Rs2.2 crore as compared with a marginal loss of Rs0.3 crore in Q3FY2006. The earnings grew in spite of the over five-fold jump in the depreciation cost and the higher effective tax rate.
- On a nine-month basis, the revenues grew by 392% to Rs24.8 crore and the earnings stood at Rs1.6 crore as against a loss of Rs0.1 crore in the same period of the last fiscal.
- The performance is on track in terms of achieving the full-year revenue and earnings estimates. The earnings estimate for FY2007 remains unchanged. But we are revising upward the earnings estimate for FY2008 by 9.4% to factor in the healthy growth in the pending order book to Rs110 crore by the end of December 2006.
- At the current market price the stock trades 15x FY2007 and 8.1x FY2008 estimated earnings. We maintain our Buy call on the stock with a revised price target of Rs270 (11x FY2008 estimated earnings).

Result table Rs (cr)

Particulars	Q3FY07	Q3FY06	% yoy	9MFY07	9MFY06	% yoy
Net sales	**13.2**	**1.6**	**718.1**	**24.8**	**5.0**	**392.1**
Total expenditure	6.5	1.1	506.3	12.6	3.2	288.6
Operating profit	6.7	0.5	1133.5	12.2	1.8	577.0
Other income	0.1	0.1	-32.8	0.3	0.5	-44.9
Interest	0.7	0.7	5.6	2.5	0.9	179.0
Depreciation	2.5	0.4	471.6	7.4	1.3	461.9
PBT	3.6	-0.5	-	2.6	0.1	3696.3
Tax	1.3	-0.2		1.0	0.1	707.4
Deferred tax						
PAT	**2.2**	**-0.3**	**-**	**1.6**	**-0.1**	**-**
Equity capital	5.5	4.95		5.5	5.0	
EPS (Rs)	4.0	-0.6		2.8	-0.1	
Margin (%)						
OPM	50.9	33.8		49.4	35.9	
NPM	16.8	-19.3		6.3	-1.2	

Robust revenue growth visibility

The company has shown a better than expected performance in Q3 on the back of the partial execution of the 3D survey order from Essar Oil, which contributed around 80% of the company's quarterly turnover. The rest of the revenues were contributed by the on-going 2D survey work for Geo Petro.

In addition to the completion of the Essar Oil order, the revenue growth would be driven by the commencement of work on the orders from Oil India in the fourth quarter. Thus, we expect the company to achieve the full-year revenue estimate of Rs55 crore.

The healthy pending order book position of around Rs110 crore provides a strong revenue growth visibility for FY2008. The recent order wins include an order worth Rs20 crore for 2D survey from Oil India and some new orders from Oil & Natural Gas Corporation (ONGC) that have boosted the order book position. Apart from this, the company has a healthy order pipeline in terms of the bids made for around Rs120 crore worth of tenders from ONGC.

Third crew to become functional soon

The setting up of the third crew for 3D surveys has been delayed by about a month and the crew is now likely to become functional from mid-February. The delay in the supply of some critical survey equipment has caused the delay.

During the quarter, the company issued to the promoters 5.5 lakh warrants that are convertible into equity shares at a price of Rs136 per share (that's a premium of Rs126 per share). The issue was done to part finance the capital expenditure for setting up the third 3D survey crew. In addition to the equity dilution, the company has taken a debt of around Rs10-12 crore for the same.

Revision in earnings estimates

Considering the improvement in its pending order backlog over the past couple of months, we are revising upward the revenue and earnings estimates for FY2008 by 2.6% and 9.4% respectively.

Valuation

At the current market price the stock trades at 15x FY2007 and 8.1x FY2008 estimated earnings. We maintain our Buy call on the stock with a revised price target of Rs270 (11x FY2008 estimated earnings).

Earnings table

Particulars	FY05	FY06	FY07E	FY08E
Net profit (Rs cr)	3.3	4.2	7.5	13.5
Share in issue (cr)	0.5	0.5	0.6	0.6
EPS (Rs)	6.6	8.5	13.6	24.5
% y-o-y growth	*3.5*	*29.5*	*59.5*	*80.5*
PER (x)	30.9	23.9	15.0	8.3
Book value (Rs)	37.3	45.9	56.0	91.9
P/BV (x)	5.4	4.4	3.6	2.2
EV/EBIDTA (x)	15.4	11.3	5.8	4.0
Dividend yield (%)	0.0	0.0	0.0	0.0
ROCE (%)	37.5	27.0	30.7	37.1
RONW (%)	19.3	20.4	27.9	33.1

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

Maruti Udyog

Apple Green

Stock Update

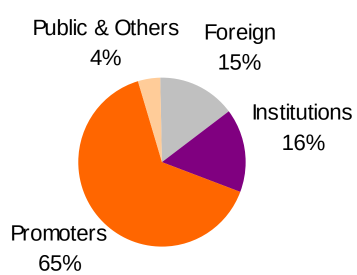
Diesel *Swift* hits the road

Buy; CMP: Rs944

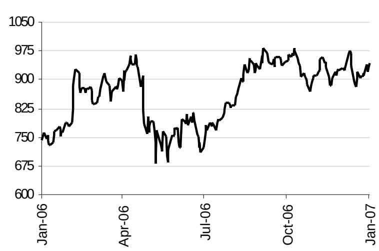
Company details

Price target:	Rs1,050
Market cap:	Rs27,273 cr
52 week high/low:	Rs991/649
NSE volume: (No of shares)	8.2 lakh
BSE code:	532500
NSE code:	MARUTI
Sharekhan code:	MARUTIUD
Free float: (No of shares)	10.3 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	0.8	-1.5	29.4	26.0
Relative to Sensex	-3.9	-12.0	-6.7	-15.9

Key points

- Maruti Udyog Ltd (MUL) has made its first serious attempt to capture share in the diesel segment with the launch of the new diesel *Swift*. Powered with a superior CRDi engine, we believe that the car would present itself as a very strong option in the small car diesel segment.
- The two variants—LDi and Vdi—are priced at Rs4.68 lakh and Rs4.96 lakh respectively, ex-showroom Delhi.
- We expect MUL to gain market share in the compact car segment despite some amount of cannibalisation after the launch of the new *Zen Estilo* and now the diesel version of *Swift*.
- At the current market price of Rs944, the stock discounts its FY2008E earnings by 14.3x and quotes at an enterprise value/earnings before interest, depreciation, tax and amortisation of 9.9x. We maintain our Buy recommendation on the stock with a price target of Rs1,050.

MUL has finally made its much-awaited entry into the diesel segment with the launch of the diesel version of *Swift*. This is MUL's first serious attempt to enter the diesel segment after the unsuccessful attempts to launch the diesel variants of *Zen* and *Esteem* a few years ago. However, we believe *Swift*'s design and engineering are well equipped to handle a diesel power train. *Swift Diesel* would present itself as one of the best options for consumers looking for a car in the small car diesel segment, as it is powered with the latest common rail direct injection (CRDi) technology, a 1.3-litre DOHC engine, 75HP power and a torque of 190NM. The technology for the diesel engine was obtained by Suzuki Motor Corp (SMC) through a technical licence agreement with Fiat and Adam Opel. The *Swift's DDiS* engine will be the country's first super compact CRDi engine. It has won the international engine of the year award for 2005.

Aggressive pricing

The two variants—LDi and Vdi—are priced at Rs4.68 lakh and Rs4.96 lakh respectively, ex-showroom Delhi. This, however, is an introductory offer and the company will review the prices soon. Currently, its only competition in the small car diesel segment is Tata Motors' *Indica*. We expect the diesel *Swift* to do well, given its superior engine, lower nose and the good track record of its petrol version. However, we do not see a major impact of this on Tata *Indica* since the same is available at a lower price point of about Rs3.5-4.0 lakh.

Going forward, we expect the competition to intensify in the diesel segment, with various new launches lined up, including the diesel variant of Hyundai's *Getz*, Mahindra and Mahindra's *Logan*, another *Indica* variant, and the planned launch of a diesel vehicle by General Motors. Currently, the penetration of the diesel car stands at about 25% in the passenger vehicle category, having grown four-fold in the last five years. With new launches lined up, we expect this share to rise further to about 35% in the coming two years.

Strong export potential

Diesel engines manufactured by MUL in India also have a strong outsourcing potential. In India diesel engines are manufactured by Suzuki Powertrain India Ltd (SPIL), a joint venture between SMC and MUL. MUL plans to spend a total of Rs2,500 crore on its Manesar plant to increase the production capacity of diesel engines from 1 lakh units to 3 lakh units in two years. SMC plans to source diesel engines from this joint venture for its plant in Hungary.

Valuations and view

We expect a lot of action in the diesel car space in the next few months, with MUL's competitors like General Motors, Hyundai, and Mahindra and Mahindra also joining the fray. However, the new diesel *Swift* appears well set to take on the competition and we expect the car to be a hit. Moreover, since it qualifies to be in the small car category, the car would also enjoy a lower excise duty of 16%. Overall, we expect MUL to gain market share in the compact car segment despite some amount of cannibalisation after the launch of the new *Zen Estilo* and now the diesel version of *Swift*. We had already factored in the strong growth to accrue from such new launches by MUL and hence maintain our volume growth estimate of 21% for FY2008.

At the current market price of Rs944, the stock discounts its FY2008E earnings by 14.3x and quotes at an enterprise value/earnings before interest, depreciation, tax and amortisation of 9.9x. We maintain our Buy recommendation on the stock with a price target of Rs1,050.

Earnings table

Particulars	FY05	FY06	FY07E	FY08E
Net sales (Rs crore)	10,962.4	12,052.2	14,368.9	18,001.3
Net profit (Rs crore)	762.7	1,189.2	1,514.4	1,884.4
% growth	41.7	55.9	27.3	24.4
EPS (Rs)	26.4	41.1	52.4	65.2
PER (x)	35.8	22.9	18.0	14.5
EV/EBIDTA (x)	18.5	15.5	11.4	9.9
RONW (%)	20.4	24.7	20.0	15.3
ROCE (%)	27.0	34.5	31.7	22.0

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

KEI Industries

Ugly Ducking

Stock Update

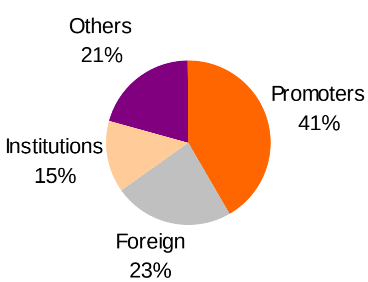
Price target revised to Rs140

Buy; CMP: Rs118

Company details

Price target:	Rs140
Market cap:	Rs696 cr
52 week high/low:	Rs130/40
NSE volume: (No of shares)	1.3 lakh
BSE code:	517569
NSE code:	KEI
Sharekhan code:	KEIINDUS
Free float: (No of shares)	3.4 cr

Shareholding pattern



Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	42.6	71.4	204.0	142.2
Relative to Sensex	36.0	53.2	119.1	61.6

Result highlights

- KEI Industries (KEI) has reported a growth of 107% in its net sales for Q3FY2007. The same is in line with our expectations. The net profit growth of 46.9% is however slightly below our expectations on account of a higher interest cost and a lower other income during the quarter.
- The power cable segment grew by 102% to Rs157 crore while the stainless steel wire segment showed a growth of 122% during the quarter.
- The operating profit margin (OPM) for the quarter improved by 140 basis points to 15.6%, led by the better performance of the stainless steel wire segment. The earnings before interest and tax (EBIT) margin of the stainless steel wire segment increased to 8.6% from just 1% in Q3FY2006 while the EBIT margin of the power cable segment declined by 110 basis points to 14.9% from 16% in Q3FY2006.
- The operating profit for the quarter grew by 126% to Rs24.5 crore.
- The interest expense for the quarter increased by 238% to Rs7 crore as the company availed of higher working capital loans. The working capital loans during this quarter were to the tune of Rs100 crore as against Rs50 crore in the same quarter last year. The depreciation cost for the quarter increased by 148% to Rs1.6 crore.
- Consequently the net profit for the quarter grew by 46.9% to Rs11 crore.
- The order book at the end of December 2006 stood at Rs200 crore (including the high-tension [HT] order book of around Rs30 crore) as against Rs180 crore at the end of September 2006.

Result table Rs (cr)

Particulars	Q3FY07	Q3FY06	% yoy	9MYFY07	9MYFY06	% yoy
Gross	181.4	88.2	105.7	448.1	236.3	89.7
Excise duty	20.9	10.8	93.2	54.6	29.7	83.9
Net sales	160.5	77.4	107.5	393.5	206.5	90.5
Total expenditure	136.0	66.5	104.5	331.8	178.2	86.2
Operating profit	24.5	10.9	125.5	61.7	28.3	117.7
Other income	0.0	1.6	-99.8	0.2	1.9	-90.9
EBIDTA	24.5	12.5	96.2	61.9	30.3	104.4
Interest	7.0	2.1	238.2	16.2	6.4	152.3
Depreciation	1.6	0.6	148.4	4.5	1.8	150.6
PBT	15.9	9.8	62.6	41.2	22.0	86.7
Tax	4.9	2.2	119.4	12.4	4.3	188.3
PAT	11.0	7.5	45.8	28.7	17.7	62.0
Extraordinary items	0.0	0.0	-	0.0	0.0	-
Reported PAT	11.0	7.5	45.8	28.7	17.7	62.0
EPS	2.2	1.5	45.8	5.7	3.5	62.0
Margins						
OPM (%)	15.2	14.0		15.7	13.7	
PATM (%)	6.8	9.7		7.3	8.6	

Segment results

	Q3FY07	Q3FY06	% yoy chg	9MFY07	9MFY06	% yoy chg
Revenue						
Power cables	157.14	77.60	102.5	388.59	206.18	88.5
Stainless steel wires	24.30	10.96	121.7	59.73	30.76	94.2
PBIT						
Power cables	23.40	12.06	394.6	59.67	31.91	87.0
Stainless steel wires	2.08	0.06	3549.1	5.36	0.55	875.4
PBIT margin						
Power cables	14.89	15.55		15.36	15.48	
Stainless steel wires	8.56	0.52		8.98	1.79	

Exports for M9FY2007 up 246% to Rs52 crore

Exports in the first nine months of FY2007 increased by a whopping 246% to Rs52 crore from Rs15 crore in M9FY2006. The company expects to do Rs30 crore worth of exports in Q4FY2007E. Although the domestic demand for cables is quite high, yet we see this as a de-risking strategy as the margins are similar in the export business.

HT cables sales rose by 86.7% (qoq)

The sales from the HT cable segment increased to Rs28 crore in this quarter from Rs18 crore in the previous quarter, showing a good growth of 86.7% on a sequential basis.

Chopanki plant to start contributing to revenues from Q2FY2008

The company is currently expanding its low-tension (LT) cable capacity at Chopanki by 9,000 kilometre at a cost of Rs35 crore. The plant, which is expected to get commissioned by June 2007, is expected to contribute around Rs150 crore to the turnover in FY2008.

Housing wire unit at Silvassa commissioned in January 2007

The company commissioned the housing wire unit at its Silvassa plant in the current month. It expects this unit to contribute around Rs15 crore in Q4FY2007.

Successful completion of FCCB of USD 36 million

KEI raised USD36 million (Rs164 crore) through a foreign currency convertible bond (FCCB) issue in November 2006. The bonds have been issued at 1% coupon rate and are convertible within five years at a price of Rs86. The funds raised will be used to set up a greenfield capacity at either Uttaranchal or Himachal Pradesh. The total cost of the project is estimated at Rs160 crore. This plant is expected to take 12 months for completion from the date of commencement of construction, which is likely to happen in the next two to three months. The plant is expected to start contributing revenues from Q1FY2009 and would thus provide greater revenue visibility in two to three years.

Revision of estimates

Considering the good order book position and the contribution from the Chopanki plant, we have revised our estimates for FY2008. Our earnings per share (EPS) estimate for FY2008 now stands at Rs11.8 against Rs9.8 earlier.

Particulars	FY2007	FY2008
Earlier	7.7	9.8
Current	7.7	11.8
% change	-	19.8

Valuation and view

At the current market price of Rs118, the stock is quoting at 10x its FY2008E EPS and 6.5x its FY2008E enterprise value/earnings before interest, depreciation, tax and amortisation. We maintain our Buy recommendation on the stock with a revised price target of Rs140.

Earnings table

Particulars	FY2005	FY2006	FY2007E	FY2008E
Net sales (Rs crore)	205.0	299.4	576.0	837.2
Net profit (Rs crore)	8.6	26.1	45.2	69.5
Shares in issue (crore)	4.0	5.0	5.9	5.9
EPS (Rs)	2.2	5.2	7.7	11.8
% y-o-y change	*911.8*	*137.9*	*48.4*	*53.8*
PER (x)	54.3	22.8	15.4	10.0
Book value (Rs)	7.1	18.9	23.7	38.3
P/BV (x)	16.6	6.3	5.0	3.1
EV/EBIDTA (x)	21.0	10.6	9.2	6.5
EV/Sales (x)	1.9	1.4	1.3	0.9
Dividend yield (%)	0.2	0.3	1.0	0.7
RoCE (%)	29.1	32.6	36.9	37.1
RoNW (%)	34.9	42.3	38.5	38.1

Apollo Tyres

Apple Green

Stock Update

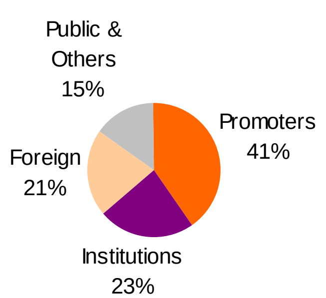
Lower raw material costs aid margin growth

Buy; CMP: Rs356

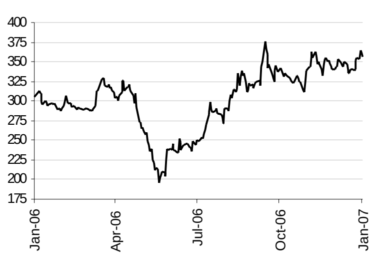
Company details

Price target:	Rs425
Market cap:	Rs1,794 cr
52 week high/low:	Rs386/194
NSE volume: (No of shares)	62,580
BSE code:	500877
NSE code:	APOLLOTYRE
Sharekhan code:	APOLLOTYR
Free float: (No of shares)	3.5 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-2.2	5.3	29.9	55.7
Relative to Sensex	-6.7	-5.9	-6.3	25.9

Result highlights

- Apollo Tyres' Q3FY2007 results are ahead of our expectations, both on the top line as well as on the margins front.
- The net sales for the quarter grew by 26.3% to Rs857.5 crore, ahead of our expectations. This was led by a 10% rise in the volumes and a 17% growth in the realisations.
- The operating margins improved by 280 basis points in comparison to last year and by 300 basis points sequentially at 10.8%. The margin improvement was mainly triggered by lower raw material costs, particularly rubber, during the quarter.
- Consequently, the operating profit for the quarter grew by 71.6% to Rs92.4 crore. Stable interest and depreciation costs led to a profit after tax (PAT) growth of 113%, which stood at Rs35.1 crore.
- A further rise in the rubber prices would necessitate another price hike. A decision regarding the same is likely to be taken in the next one month.
- At the current market price (CMP) of Rs356, the stock quotes at FY2008E price/ earnings ratio (PER) of 11.3x and enterprise value (EV)/earnings before interest, depreciation, tax and amortisation (EBIDTA) of 5.2x. We maintain our Buy recommendation on the stock with a price target of Rs425.

Result table Rs (cr)

Particulars	Q3FY07	Q3FY06	% yoy	9MYFY07	9MYFY06	% yoy
Net sales	**857.5**	**678.8**	**26.3**	**2382.1**	**1879.7**	**26.7**
Expenditure	765.1	624.9		2173.2	1713.3	
RM consumed	551.7	480.3		1681.2	1332.2	
Change in stock	20.3	-10.3		-65.4	-81.7	
Staff cost	51.7	41.3		148.9	122.5	
Other expenses	141.4	113.7		408.5	340.3	
Operating profit	**92.4**	**53.9**	**71.6**	**208.9**	**166.4**	**25.6**
Other income	0.1	0.3		0.4	1.4	
EBIDTA	92.6	54.2	70.8	209.3	167.7	24.8
Interest	13.0	12.8		39.3	37.2	
PBDT	79.6	41.4	92.1	170.0	130.6	30.2
Depreciation	18.3	18.0		55.3	52.3	
PBT	61.3	23.4	161.8	114.7	78.3	46.6
Tax	26.2	7.0		44.0	23.1	
Profit after tax	35.1	16.4	113.3	70.7	55.2	28.0
Extraordinary items	0.0	0.0		0.0	0.0	
Net profit	**35.1**	**16.4**	**113.3**	**70.7**	**55.2**	**28.0**
EPS	7.6	4.3	76.3	15.2	11.9	28.0
OPM (%)	10.8	7.9		8.8	8.8	
PATM (%)	4.1	2.4		3.0	2.9	

Strong top line growth led by tonnage and realisation growth

The net sales for the quarter exceeded our expectations, growing at 26.3% to Rs857.5 crore. The sales growth was backed by a strong volume growth of about 10% and a realisation growth of 17%. In the first nine months, Apollo's volumes in the trucks segment grew by 7% against an industry growth of 3%, and by 15% in the passenger car radial segment against a 7% industry growth.

Fall in raw material cost triggers margin expansion

The operating profit margin (OPM) improved by 280 basis points year on year and by 300 basis sequentially to 10.8%. This was largely due to a fall in the raw material costs. The raw material costs as a percentage of sales declined to 65.9% from 69.7% last year. This was mainly on account of a 10% sequential decline in the average cost of acquiring rubber, which accounts for almost 45% of the total raw material cost. The company also managed to control its other overheads, which were also down as a percentage of sales.

The interest costs and the depreciation charges remained fairly stable. Consequently, the net profit for the quarter rose by a brilliant 113% to Rs35.1 crore.

Further rise in rubber prices may necessitate price hike

The prices of rubber have sprinted up to Rs96 per kilogram currently, after having cooled off between June 2006 and November 2006 to the Rs76 per kilogram level. This rise is largely attributed to international factors like the floods in Malaysia, adverse climatic conditions in Vietnam and certain law and order related problems in Thailand. The industry majors have maintained that a further rise in the rubber prices would necessitate a price hike and the management is expected to take a decision regarding the same in the next one month.

At the same time, the cost of some of the other raw materials like carbon black and SBR are on a downturn due to the recent fall in the prices of crude oil, which should provide some respite. However, we believe maintaining the margins at the current levels would be a challenge in the short term considering the high level of rubber prices. Hence, we believe that the margins would be slightly under pressure for Q4FY2007, but would report an increase in comparison to last year.

Subsidiary's performance expected to improve

The performance of Apollo's subsidiary, Dunlop South Africa, is set to improve going forwards post its debt restructuring. Its performance has improved in the past few months, after a price hike of around 10% taken by the entire tyre industry in South Africa. The company has also made efforts to reduce the high-cost debt of Dunlop through some debt restructuring. This has been done through a qualified institution buyer (QIB) placement of Rs250 crore, which was completed during the quarter under review. Hence, the effect of the same should start being seen from Q4FY2007 onwards.

Tamil Nadu plant expected to start next year

The capital expenditure for FY2008 is slated to be Rs330 crore. Out of this amount, Rs250 crore would be spent on the new greenfield plant at Tamil Nadu. The Tamil Nadu plant would be predominantly for the manufacture of tyres for trucks and bus radials, and would commence operations with a capacity of 90 tonne per day. The operations are expected to commence by mid-2008. Apart from this, the company would also expand its passenger car radial (PCR) tyre capacity and also its cross-ply capacity from 10,000 to 12,000 tyres per day at its Baroda plant.

Valuations and view

Considering the strong growth seen in the medium and heavy commercial vehicle segment over the past two years, we expect the replacement demand for tyres to be triggered going forward. Being the segment leader, Apollo is expected to be one of the prime beneficiaries of the same. The consolidated performance is also set to improve post the debt restructuring of Dunlop. At the current market price of Rs356, the stock is trading at 11.3x its FY2008E earnings and at an EV/EBIDTA of 5.2x. We maintain our Buy recommendation on the stock with a price target of Rs425.

Earnings table

Particulars	FY04	FY05	FY06	FY07E	FY08E
Net sales (Rs cr)	1910.8	2235.8	2613.6	3230.8	3741.0
Net profit (Rs cr)	70.4	67.6	78.2	101.3	158.0
Shares in issue (cr)	3.8	3.8	3.8	5.0	5.0
EPS (Rs)	18.4	17.6	20.4	20.1	31.3
% y-o-y growth		*-4.0*	*15.6*	*-1.4*	*56.0*
PER (x)	19.0	18.8	18.6	17.7	11.3
Book value (Rs)	149.2	150.4	165.4	190.6	237.2
P/BV	2.4	2.4	2.1	1.9	1.5
EV/EBITDA	9.7	14.5	8.3	7.6	5.2
Mcap/Sales	0.7	0.6	0.5	0.6	0.5
ROCE (%)	16.3	13.1	12.7	13.5	17.8
RONW (%)	12.5	12.6	11.6	10.5	13.2

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

Union Bank of India

Ugly Duckling

Stock Update

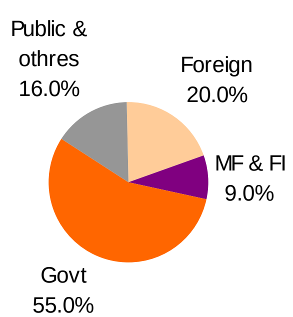
First-cut analysis of Q3 results

Buy; CMP: Rs112

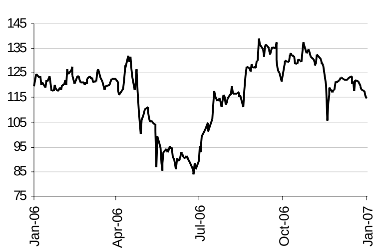
Company details

Price target:	Rs150
Market cap:	Rs5,657 cr
52 week high/low:	Rs142/81
NSE volume: (No of shares)	7.7 lakh
BSE code:	532477
NSE code:	UNIONBANK
Sharekhan code:	UBI
Free float: (No of shares)	22.5 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-3.9	-4.3	30.4	-2.8
Relative to Sensex	-8.3	-14.5	-6.0	-35.1

Result highlights

- The Q3FY2007 results of Union Bank of India are in line with expectations with the profit after tax reporting a growth of 11.4% to Rs255.2 crore compared to our estimate of Rs251.3 crore.
- The net interest income was up 7.3% to Rs685.9 crore compared to our estimate of Rs695 crore and the other income increased by 47.6% to Rs205.2 crore.
- The net interest margin of the bank has improved on a sequential basis by 23 basis points from 2.76% for Q2FY2007 to 2.99% for Q3FY2007. The bank's CASA share has improved to 34.90% from 33.49% sequentially and from 32.74% on a year-on-year (y-o-y) basis.
- The operating profit was up 17.8% and the provisions showed an increase of 9.5%.
- The capital adequacy ratio (CAR) of the bank improved to 13.22% as on December 31, 2006 from 10.91% as on December 31, 2005 and from 10.79% as on September 30, 2006. The higher CAR is on account of an increase in the capital due to the raising of funds by way of perpetual bonds of Rs300 crore for Tier I and bonds worth Rs750 crore for upper Tier II.
- The net non-performing assets of the bank improved to 1.12% as on December 31, 2006 from 1.24% on a y-o-y basis and from 1.15% on a sequential basis.
- The gross advances on a y-o-y basis grew by 14.96% to Rs58,303 crore while the deposits increased by 9.68% year on year to Rs77,292 crore.
- At the current market price of Rs112, the stock is quoting at 5x its FY2008E earnings and 0.9x expected FY2008E book value. We maintain our Buy recommendation on the stock with a price target of Rs150.

Result table Rs (cr)

Particulars	Q3FY07	Q3FY06	% yoy	% qoq	9MFY07	9MFY06	% yoy
Net interest income	685.9	639.4	7.3	9.3	1,947.9	1,776.4	9.7
Other income	205.2	139.0	47.6	7.0	562.0	413.0	36.1
Net income	891.1	778.4	14.5	8.8	2,509.9	2,189.4	14.6
Operating expenses	386.7	350.1	10.4	-1.1	1,150.7	1,050.9	9.5
Operating profit	504.5	428.3	17.8	17.8	1,359.2	1,138.5	19.4
Provisions & contingencies	142.6	130.2	9.5	16.9	422.4	463.9	-8.9
PBT	361.9	298.1	21.4	18.1	936.8	674.6	38.9
Provision for taxes	106.7	69.0	54.6	-4.9	320.6	144.0	122.7
Net profit	255.2	229.1	11.4	31.4	616.2	530.6	16.1

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
ACC
Apollo Tyres
Bajaj Auto
Balrampur Chini Mills
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
Hindustan Lever
Hyderabad Industries
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

3i Infotech
Aban Offshore
Alphageo India
Cadila Healthcare
Federal-Mogul Goetze (India)
KSB Pumps
Marksans Pharma
Navneet Publications (India)
New Delhi Television
Nucleus Software Exports
Orchid Chemicals & Pharmaceuticals
ORG Informatics
Solectron Centum Electronics
Tata Elxsi
Television Eighteen India
Thermax
TVS Motor Company
UTI Bank

Ugly Duckling

Ahmednagar Forgings
Ashok Leyland
BASF India
Ceat
Deepak Fertilisers & Petrochemicals Corporation
Fem Care Pharma
Genus Overseas Electronics
HCL Technologies
ICI India
India Cements
Indo Tech Transformers
Jaiprakash Associates
JM Financial
KEI Industries
NIIT Technologies
Punjab National Bank
Ratnamani Metals and Tubes
Sanghvi Movers
Saregama India
Selan Exploration Technology
South East Asia Marine Engineering & Construction
Subros
Sun Pharmaceutical Industries
Surya Pharmaceuticals
UltraTech Cement
Union Bank of India
Universal Cables
Wockhardt

Vulture's Pick

Esab India
Orient Paper and Industries
WS Industries India

Home