Sharekhan top picks

In the March 2008 issue, we had recommended the best 12 of our Stock Ideas as Sharekhan Top Picks. As on March 31, 2008 the basket of stocks declined by 2.6% during the month as volatility in the markets continued. The Sensex declined by 2.1% and the S&P CNX Nifty by 0.8% during the same period.

We have made three changes in the portfolio this month. We have replaced Axis Bank, Bharat Heavy Electricals, Indo Tech Transformers and Mahindra and Mahindra with Bharti Airtel, Hindustan Unilever, Sun Pharmaceuticals and Zee News. We have reduced our exposure to capital goods companies and interest rate sensitive stocks in Top Picks. This is due to the possibility of the tightening of the monetary policy by the Reserve Bank of India in the light of inflationary concerns.

Name	CMP* (Rs)	PER			RoE (%)			Target price	Upside (%)
		FY07	FY08E	FY09E	FY07	FY08E	FY09E		
Aban Offshore	3,049	-	31.7	7.6	-7.1	55.5	94.6	5,420	77.8
Bharti Airtel	784	34.8	22.3	18.4	29.1	34.2	31.6	1,100	40.3
Grasim	2,541	11.8	8.8	10.2	27.5	27.2	27.0	3,950	55.4
Hindustan Unilever	242	34.5	29.8	26.0	61.2	85.0	112.8	280	15.9
ITC	201	28.0	24.2	20.5	27.7	27.7	27.7	247	23.0
Larsen & Toubro	2,686	43.5	31.5	21.4	26.1	28.2	31.5	4,428	64.8
Marico	69	37.0	25.4	20.8	58.7	51.6	39.2	70	2.2
Maruti Suzuki	764	14.4	11.7	10.0	24.9	26.3	24.1	1,237	61.8
Ranbaxy Lab	458	33.2	21.6	21.4	19.9	26.3	24.4	558	21.8
Shiv-vani oil	520	61.9	23.1	14.4	10.4	16.9	19.4	670	28.9
Sun Pharmaceuticals	1,239	30.6	24.8	19.2	28.3	22.0	22.8	1,475	19.0
Zee News	49	245.5	32.7	22.3	3.2	17.8	22.1	79	60.9

* CMP as on April 04, 2008

Name	CMP	PER			RoE (%)			Target	Upside
	(Rs)	FY07	FY08E	FY09E	FY07	FY08E	FY09E	price	(%)
Aban Offshore	3,049	-	31.7	7.6	-7.1	55.5	94.6	5,420	77.8

Remarks:

- Aban Offshore, one of Asia's largest oil drilling companies, is benefiting from the increase in oil exploration and production activities globally. The robust demand environment is resulting in firm day rates for its assets.
- In addition to re-pricing of its assets at higher day rates, the company is also benefiting from the efforts taken to substantially ramp up the asset base through organic and inorganic initiatives. This would significantly improve its financial performance over the next few years.
- At the current market price the stock trades at 7.6x FY2009 and 5.8x FY2010 estimated earnings. We maintain the Buy call on the stock with a price target of Rs5,420.

Name	CMP	PER FY07	PER FY08E	PER FY09E	RoE FY07	RoE FY08E	RoE FY09E	Target price	Upside (%)
Bharti Airtel	784	34.8	22.3	18.4	29.1	34.2	31.6	1,100	40.3

Remarks:

- Bharti Airtel with over 24% market share is a leader in the Indian telecom space. On average, the company is adding ~2 million subscribers every month and currently has a subscriber base of approximately 60 million.
- The embedded value in the company's tower business offers considerable downside support to the stock price. Bharti Infratel (with 22,000 towers in circles other than the 16 covered by Indus Towers) has raised $1 billion through placement to the leading foreign institutions. It has been valued in the range of $10-12.5 billion depending on the actual performance in FY2009. This apart, Bharti Infratel would hold 40% stake in Indus Towers (formed along with Vodafone and Idea Cellular).
- Bharti Airtel is likely to be a key beneficiary of the removal of the access deficit charge (ADC). Bharti Airtel is estimated to benefit to the extent of Rs180-200 crore from the removal of ADC. The company is likely to pass on the benefits accruing from the ADC removal to the end consumers by way of reduced tariffs or similar benefits.
- At the current market price the stock trades at 22.3x FY2008 and 18.4x FY2009 estimated earnings.

Name	CMP	PER FY07	PER FY08E	PER FY09E	RoE FY07	RoE FY08E	RoE FY09E	Target price	Upside (%)
Grasim Industries	2,541	11.8	8.8	10.2	27.5	27.2	27.0	3,950	55.4

Remarks:

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

Name	CMP	PER FY07	PER FY08E	PER FY09E	RoE FY07	RoE FY08E	RoE FY09E	Target price	Upside (%)
Hindustan Unilever	242	34.5	29.8	26.0	61.2	85.0	112.8	280	15.9

Remarks:

- HUL is the largest FMCG company in India, occupying ~20% of the Indian consumer space. With dominance across categories such as soaps, detergents, personal care products, food and beverages, it stamps its presence as an FMCG giant.
- With increasing per capita income fueling consumerism and upgradation of lifestyle of the Indian consumer, HUL's revenues and profitability are expected to gain momentum.
- Further, hefty free cash flow generation has lead to huge cash reserves for HUL and rich dividends (dividend yield of ~4%) for its shareholders over the years.
- At the current market price, the stock trades at 26x its CY2008E EPS of Rs9.3. We maintain our Buy recommendation on the stock.

Name	CMP	PER			RoE (%)			Target	Upside
	(Rs)	FY07	FY08E	FY09E	FY07	FY08E	FY09E	price	(%)
ITC	**201**	28.0	24.2	20.5	27.7	27.7	27.7	**247**	23.0

Remarks:

- ITC.s cigarette.s business that has dominance in the category continues to be a cash cow for the company. ITC has chalked out aggressive roadmap for making a mark in the Indian FMCG market. With successful brands such as Bingo, Sunfeast and Aashirwaad already in the reckoning among the best in the industry, ITC.s non-cigarette FMCG business is on a strong footing. The company has further ventured into the personal care category with the launch of Superia and Fiama Di Wills soaps and shampoos that would compete with the likes of the products of HUL and P&G.
- Aggressive expansion plans in hotels and paper segments would ensure, inclusive growth across segments for the company.
- We believe ITC has a well-diversified business model with multiple revenue drivers that would ensure sustained growth for the company. It thus remains our top pick in the sector. At the current market price, ITC trades at 20.5x its FY09E earnings. We maintain our Buy recommendation on the stock with a price target of Rs247.

Name	CMP	FY07	FY08E	FY09E	FY07	FY08E	FY09E	Target price	Upside (%)
Larsen & Toubro	**2,686**	43.5	31.5	21.4	26.1	28.2	31.5	**4,428**	64.8

Remarks:

- Larsen & Toubro, the largest engineering and construction (E&C) company in India, is a direct beneficiary of the strong domestic infrastructure development and industrial capital expenditure (capex) booms. Consequently, we estimate the order inflows to grow at a CAGR of 20.7% between FY2007 and FY2010.
- The international business is expected to emerge as one of the key drivers going forward with immense opportunities from the Gulf Corporation Council markets.
- There lies innumerable opportunities in the new verticals in which the company is entering, namely ship building, defence, railways, thermal and nuclear power.
- We believe that there is a scope for further improvement in the margins on the back of rising operational efficiencies, larger ticket-size and more complex nature of orders, better raw material sourcing and integration, and higher contribution of its new businesses which carry higher margins.
- We value the core business of L&T at 28x FY2010E earnings, or Rs3,403 per share, while we value the subsidiaries at Rs1,025 per share of L&T. At the current levels, the stock is trading at 16.6x its FY2010E consolidated earnings. We maintain our Buy recommendation with a price target of Rs4,428.

Name	CMP	FY07	FY08E	FY09E	FY07	FY08E	FY09E	Target price	Upside (%)
Marico	**69**	37.0	25.4	20.8	58.7	51.6	39.2	**70**	2.2

Remarks:

- Marico is a major player in the Indian hair care and edible oil markets. Its flagship brand Parachute combined with Nihar commands a 57% share of the branded coconut oil market in India. Its 'good for heart' edible oil brand 'Saffola' is also witnessing good volume growth.
- Marico has been growing both the organic and inorganic way and thereby follows the strategy of adding new products and territories to its portfolio. Apart from domestic operations, its international business covers countries like Bangladesh and Egypt. The company is also expanding its business to some extent to the US and the UAE.
- We believe apart from the growth in the existing business through product innovations, the expanding new age businesses of Kaya Clinics and weight loss centers and spas in the USA promise a great deal.
- Marico is among the fastest growing FMCG companies in India with very good return ratios. At the current market price, the stock trades at 25.4x its FY2008E earnings and 20.8x its FY2009E earnings.

Name	CMP	PER			RoE (%)			Target	Upside
	(Rs)	FY07	FY08E	FY09E	FY07	FY08E	FY09E	price	(%)
Maruti Suzuki	**764**	14.4	11.7	10.0	24.9	26.3	24.1	**1,237**	61.8

Remarks:

- Maruti Suzuki, the market leader in the passenger car market in India, is set to benefit from the number of new launches made by it in the recent times.
- Most of its new launches, namely *WagonR Duo*, *Zen Estilo*, *Diesel Swift* and *SX4*, have been well received by the market and are clocking strong volumes.
- Also, with the addition of the diesel vehicle and a sedan, the company has expanded its product basket, making it a full-fledged play on the country's booming passenger car market. The company also plans to launch its Swift sedan at the start of the next fiscal.
- With the expansion of its Manesar plant, its exports are also set to go on a top gear. Suzuki has identified India as a hub for manufacture of small cars for its worldwide markets and the company would be exporting about 100,000 units of the new vehicle to its parent, while another 50,000 units would be supplied to Nissan.
- At current levels, the stock is trading at 10x its FY2009E and is available at an EV/EBIDTA of 6.4x.

Name	CMP	PER			RoE (%)			Target	Upside
	(Rs)	FY07	FY08E	FY09E	FY07	FY08E	FY09E	price	(%)
Ranbaxy lab	**458**	33.2	21.6	21.4	19.9	26.3	24.4	**558**	21.8

Remarks:

- With a geographically diversified presence and a large product portfolio, Ranbaxy is one of the best plays on the global generic opportunity.
- The company has guided towards an impressive 18-20% growth in CY2008, an expansion of margins to 17.5-18%, resulting in a net profit growth of 20-25%. This guidance is excluding any one-time exclusivity opportunities in the USA.
- Ranbaxy believes the next wave of its growth to come from the branded markets in Asia, Africa and Latin America. With a product pipeline of over 100 products for these markets, revenues from emerging markets will drive the company's growth.
- Ranbaxy believes that it has FTF status on approximately 18 Para IV ANDA filings, representing a market size of about USD27 billion. It expects to monetise at least one FTF opportunity every year for the next few years and has already announced the opportunities until CY2010. The FTF opportunities announced so far are collectively valued at Rs2,716 crore, translating into a per share value of Rs68.
- Ranbaxy has decided to de-merge its new drug discovery research (NDDR) operations into a separate entity effective from January 1, 2008 and list it subsequently. This will boost the overall profitability of the core business and also unlock value in the discovery research and development (R&D) assets. The announcement of further details on the demerger scheme in February 2008 will act as a near-term trigger for the stock.
- At the current market price, Ranbaxy is trading at 21.4x its estimated CY2008E and 18.7x its estimated CY2009E earnings. We maintain our Buy recommendation on the stock with a price target of Rs558 (Rs490 for base business plus Rs68 for FTFs).

Name	CMP	PER			RoE (%)			Target	Upside
	(Rs)	FY07	FY08E	FY09E	FY07	FY08E	FY09E	price	(%)
Shiv- vani Oil & Gas	**520**	61.9	23.1	14.4	10.4	16.9	19.4	**670**	28.9

Remarks:

- With a fleet of 25 onshore drilling rigs and six seismic survey crew, Shiv-Vani Oil & Gas Exploration (SOGEL) has emerged as the largest onshore service provider catering to oil and gas exploration companies.
- Augmentation of assets by the company is well timed in the industry up-cycle as heightened exploration activity has led to a severe shortage of resources with service providers, leading to firming up of day rates (or billing rates per km in case of seismic survey) for various services. Moreover, the order backlog of over Rs3,000 crore (over 8x CY2006 revenues) provides strong revenue-growth visibility.
- The consolidated revenues and earnings are expected to grow at CAGR of 60.3% and 72.7% respectively over the three-year period CY2006-09.
- Despite the robust growth prospects, the scrip is available at attractive valuations of 14.4x CY2008 and 10.9x CY2009 earning estimates. We recommend Buy call on the stock.

Name	CMP (Rs)	PER			RoE (%)			Target price	Upside (%)
		FY07	FY08E	FY09E	FY07	FY08E	FY09E		
Sun Pharmaceuticals	**1,239**	30.6	24.8	19.2	28.3	22.0	22.8	**1,475**	19.0

Remarks:

- Sun Pharma's track record of delivering consistent and robust growth while maintaining strong profitability and return ratios makes it the best Indian play in the generic space.
- With 98 abbreviated new drug applications (ANDAs) pending USFDA approval and a filing rate of 30+ ANDAs per year, Sun Pharma has one of the strongest product pipelines for the US market. The company is amongst the top three players in around 15 of the 25 products that it sells in the US market.
- With a strong focus on the chronic lifestyle diseases, Sun Pharma's domestic formulations business has been outperforming the industry growth by a wide margin. Sun Pharma maintains the numero uno ranking with neurologists, cardiologists, diabetologists and orthopedics.
- It is an aggressive participant in the Para IV patent challenge space. Having already monetised three of its Para IV wins (oxcarbazepine, pantoprazole and amifostine), approvals and launch of generic Gemzar and generic Effexor XR would act as triggers for the stock.
- The stock is quoting at 24.8x FY2008E earnings and at 19.2x FY2009E earnings.

Name	CMP (Rs)	PER FY07	PER FY08E	PER FY09E	RoE FY07	RoE FY08E	RoE FY09E	Target price	Upside (%)
Zee News	**49**	245.5	32.7	22.3	3.2	17.8	22.1	**79**	60.9

Remarks:

- Zee News Ltd (ZNL) operates a unique bouquet comprising six regional entertainment channels and four news channels. The key revenue contributors are Zee News, Zee Marathi and Zee Bangla, with the latter two channels being dominant leaders in their respective genres.
- ZNL is making steady progress in garnering better market share in the Telugu and Kannada markets, which would drive its growth going forward. Also, the flow of hefty subscription revenues in future augurs well for the company's growth.
- We expect ZNL's earnings to grow at a compounded annual growth rate of 43.1% from FY2008-10.
- At the current market price of Rs49 the stock trades at 16.2x its FY2010 EPS of Rs3.0. We recommend a Buy on the stock.

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