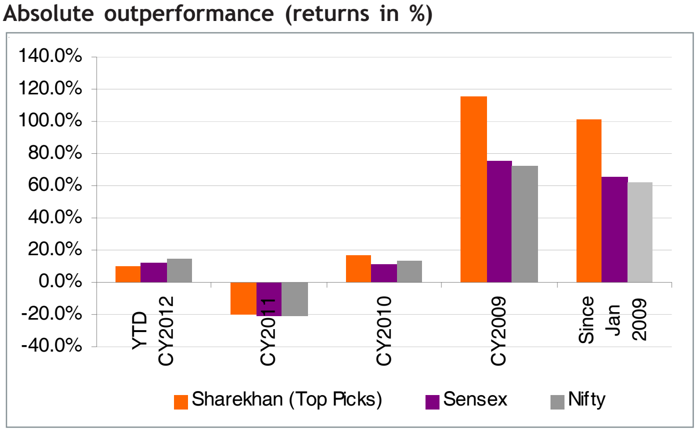
Sharekhan Top Picks

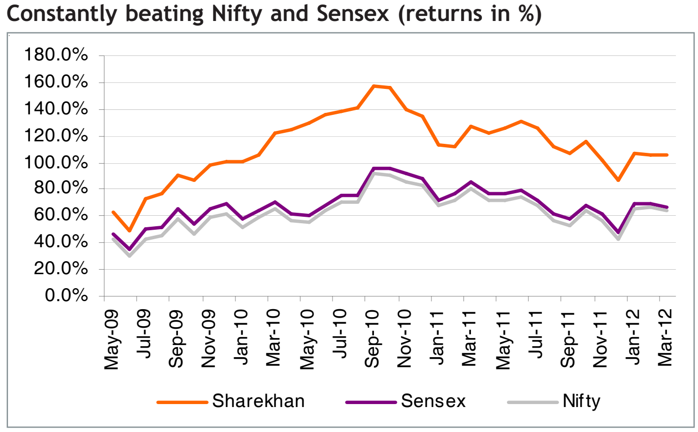
In the third month of 2012, volatility spiked up in the Indian market on account of political and policy concerns. The global environment was also not very conducive for equities during this period with growing concerns related to the hard landing of the Chinese economy. Consequently, the Sensex and the Nifty have declined by around 1.3% each since the release of the previous issue of Sharekhan's Top Picks on March 3, 2012. But the Sharekhan's Top Picks basket outperformed the benchmark indices with a marginal gain in the same period which was aided by gains of 6.1% and 11.1% recorded by Orient Paper and Industries, and Marico respectively in the same period.

We are making three changes to the basket this month. We are replacing Grasim Industries with Madras Cement and Pratibha Industries with IL&FS Transportation Networks as part of the churn within the sectors. In view of the impending Q4 corporate results we are also replacing Tata Consultancy Services (TCS) with Apollo Tyres on account of expectations of weak quarterly results of TCS and an improvement in the performance of Apollo Tyres.

Absolute outperformance (returns in %)



Constantly beating Nifty and Sensex (returns in %)



Name	CMP* (Rs)	PER (x) FY11	FY12E	FY13E	RoE (%) FY11	FY12E	FY13E	Price target	Upside (%)
Apollo Tyres	79	9.1	8.8	6.8	18.3	15.9	17.2	86	8
Bank of Baroda	794	7.4	6.6	5.8	23.5	21.1	20.6	1,065	34
Bharat Electronics	1,515	14.4	13.3	12.0	17.2	14.9	13.8	1,893	25
Divis Laboratories	767	23.7	21.0	16.6	23.9	23.4	25.6	1,015	32
ICICI Bank	887	19.8	16.4	14.4	9.6	10.8	11.4	1,070	21
ITNL	193	8.7	8.1	6.5	22.1	15.3	14.0	330	71
Madras Cement	153	17.2	10.3	9.4	13.0	19.0	18.0	160	4
Marico	175	41.5	32.9	24.6	32.7	30.7	31.7	186	7
Orient Paper	59	8.3	6.7	5.6	17.0	18.4	18.9	70	18
Selan Exploration	280	15.0	10.4	7.5	18.7	21.9	23.6	500	79
Sun Pharma	570	32.5	24.2	24.0	19.2	21.1	17.7	631	11

* CMP as on March 30, 2012

Sharekhan
Your guide to the financial jungle

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Name	CMP	PER (x)			RoE (%)			Price	Upside
	(Rs)	FY11	FY12E	FY13E	FY11	FY12E	FY13E	target	(%)
Apollo Tyres	**79**	9.1	8.8	6.8	18.3	15.9	17.2	**86**	8

Remarks:

- We view Apollo Tyres as the best tyre play amongst the Indian listed tyre companies. The company is also the best diversification story whereby it is now the largest radial manufacturer in the country. It is also a global tyre play after the acquisition of Vredestien in Europe and of Dunlop in South Africa and derives 23% of its sales globally.
- Europe continues to be the shining spot with the company recording double-digit margins at the EBIT level helped by strong sales of Vredestien's branded replacement tyres. Increased sales of Apollo branded tyres in Europe would provide additional fillip to its profitability.
- The company is likely to benefit from an uptick in the domestic commercial vehicle (CV) replacement segment and increased sales of CV radial tyres. The rupee's depreciation will see reduced threat from Chinese imports.
- Stable material prices, recovery in South African operations and increased proportion of Apollo branded tyres in the premium European market are likely to improve the margins. At the current market price the stock trades at a PE multiple of 6.8x discounting its FY2013E earnings. We maintain our Buy with a price target of Rs86.

Name	CMP (Rs)	PER FY11	PER FY12E	PER FY13E	RoE FY11	RoE FY12E	RoE FY13E	Price target	Upside (%)
Bank of Baroda	**794**	7.4	6.6	5.8	23.5	21.1	20.6	**1,065**	34

Remarks:

- Bank of Baroda stands out among the PSU banks as it continues to deliver strong earnings growth with improvement in key operational metrics. The bank's business growth is expected to remain better than industry's (contributed by stronger overseas growth) with relatively stable margins which will lead to a healthy growth in the top line.
- While the asset quality of most PSU banks has deteriorated significantly over the past two to three quarters, BoB's asset quality has remained healthy due to lower slippages. Although, the asset quality risks have risen due to weak macro environment and policy issues, yet BoB is expected to fare better than the other PSU banks in terms of asset quality, resulting in lower credit cost and higher growth in earnings.
- The operating metrics of BoB has improved significantly led by strong focus on CASA, margins, fee income etc. The bank is expected to post RoE and RoA of around 20% and 1.1% respectively over the next two years.
- We believe BoB commands a premium over the other PSU banks due to a steady growth in its core income and a healthy asset quality. Currently, the stock is trading at 1.2x FY2013 book value which is reasonable. We recommend a Buy on the stock with a price target of Rs1,065.

Name	CMP (Rs)	PER (x)			RoE (%)			Price target	Upside (%)
		FY11	FY12E	FY13E	FY11	FY12E	FY13E		
Bharat Electronics	**1,515**	14.4	13.3	12.0	17.2	14.9	13.8	**1,893**	25

Remarks:

- BEL, a public sector unit, is one of the leading defence companies in India. With the increase in the defence budget and the focus on modernisation of the defence technology, BEL is best placed to take a sizeable pie of the defence spend.
- The company's order book currently stands at Rs27,000 crore, which is around 5x its FY2011 revenues. This gives us a strong revenue visibility for at least the next two to three years.
- BEL has entered into joint ventures and technology collaborations to strengthen its position in the defence services space, reap the benefits of the offset clause (which it believes is worth $300 million in the next five to seven years) and enter into newer areas of operations.
- The March quarter is the strongest for BEL and the upcoming budget could also have something positive to offer to the defence sector and in turn to BEL. Also, in the Budget 2012-13, the defence allocation has been increased by 17.6% to Rs1.93 lakh crore and the capex budget has been increased by 15% to Rs79,579 crore.
- The key risk remains its execution: a delay in release of orders could lead to slower execution.
- At the current market price the stock trades at 12x its FY2013E earnings. The company has huge cash reserve of Rs5,875 crore, which translates into cash per share of Rs734 and gives the stock further support. We maintain our Buy recommendation on the stock.

Name	CMP (Rs)	PER FY11	PER FY12E	PER FY13E	RoE FY11	RoE FY12E	RoE FY13E	Price target	Upside (%)
Divis Laboratories	**767**	23.7	21.0	16.6	23.9	23.4	25.6	**1,015**	32

Remarks:

- Strong M9FY2012 performance (PAT growth 27%) has re-affirmed our confidence in the growth potential of Divi's Labs.
- The new DSN SEZ facility at Vishakhapatnam that started production from one of its blocks in June 2011 (the remaining blocks of this facility are likely to get operational over FY2012-13) is likely to bring better economies of scale and tax benefits.
- A near debt-free balance sheet and strong cash flow are likely to help build a war chest for pursuing strategic investments (biosimilars) and exploit growth opportunities in niche segments like high potency drugs for oncology and steroids for contraceptives.
- With the order inflow picking up and its new plant getting operational, Divi's has a strong revenue growth visibility and the operating leverage in the business will boost its margins. At the current market price the stock trades at a PE multiple of 16.6x discounting its FY2013E earnings. We maintain our Buy recommendation.

Name	CMP	PER (x)			RoE (%)			Price	Upside
	(Rs)	FY11	FY12E	FY13E	FY11	FY12E	FY13E	target	(%)
ICICI Bank	887	19.8	16.4	14.4	9.6	10.8	11.4	1,070	21

Remarks:

- ICICI Bank is back on growth path as its advances are growing at a healthy rate (up 19.1% YoY and 5.2% QoQ in Q3FY2012). We expect the advances of the bank to grow by 18% CAGR over FY2011-13. This should lead to a 15% CAGR growth in the net interest income in the same period.
- ICICI Bank's asset quality has shown a turnaround as its NPAs have continued to decline over the last six quarters led by contraction in slippages. This has led to a sharp reduction in the provisions and an increase in the profitability. Going forward, we expect the NPAs to decline further which will lead to lower NPA provisions and hence aid the profit growth.
- With a pick-up in the business growth and an improvement in the margins the RoEs are likely to expand to about 12% over the next two years while the RoA would improve to 1.4%. This would be driven by a 17% CAGR in profits over FY2011-13.
- Despite the run-up in the stock over the past two months it trades at 1.6x FY2013E book value. We expect the stock to re-rate, given the improvement in the profitability led by lower NPA provisions, a healthy growth in the core income and improved operating metrics. We recommend Buy with a price target of Rs1,070.

ITNL	193	8.7	8.1	6.5	22.1	15.3	14.0	330	71

Remarks:

- IL&FS Transportation Networks Ltd (ITNL) is India's largest player in the BOT road segment with 10,269 lane km in various stages of development, construction or operation. It has a pan-India presence and a diverse project portfolio consisting of 23 road and bus transportation projects as well as a metro rail project.
- Recently it bagged four road BOT projects which form 50% of the existing order book, thus providing good revenue visibility over the next two to three years. Further, with 8,800km of NHAI's target for FY2013, ITNL is well equipped to capitalise on the huge and growing opportunity in the road infrastructure sector due to its established track record in operating BOT road projects, its execution capabilities and the strong support from IL&FS.
- It has a fair mix of annuity and toll projects in its portfolio which provides revenue comfort. Further, it is present across the value chain except the civil construction services, which it outsources to the local contractors. This helps the company to handle a large number of projects at a time and diversify geographically, reducing the risk of concentration.
- Thus, we expect the sales and earnings to grow at CAGR of 10% and 16% respectively over FY2012-14E.
- At the current market price, the stock is currently trading at 6.5x its FY2013E earnings and at a P/BV of 0.8x. We maintain our Buy recommendation with a price target of Rs330.

Name	CMP (Rs)	PER (x)			RoE (%)			Price target	Upside (%)
		FY11	FY12E	FY13E	FY11	FY12E	FY13E		
Madras Cement	**153**	17.2	10.3	9.4	13.0	19.0	18.0	**160**	4

Remarks:

- Madras Cement is a predominant player in the south region with an installed capacity of 12.5MMT. The company will be the biggest beneficiary of the recent partial recovery in the cement offtake in the southern region. Further, the supply discipline has resulted in strong realisation. We expect the earnings of the company to grow by around 35% over FY2011-13.
- The company has posted a volume growth of over 22% YoY for February 2012 and we believe the volume growth along with the realisation growth would support the revenue growth in Q4FY2012.
- To overcome the issue of power shortage in Tamil Nadu and to control the power cost the company is setting up captive thermal power plants in Ariyalur and RR Nagar to meet the energy requirements. As per the plan a 60MW thermal power plant would be set up at Ariyalur (of this 40MW has already been commissioned and the balance 20MW is expected in the near term) and a 25MW thermal power plant will be set up at RR Nagar.
- The company is likely to be the biggest beneficiary of the sharp correction in the price of imported coal as it imports 50-60% of its total coal requirement. So going forward, significant savings in the power and fuel costs can be expected.
- Any failure to adhere to supply discipline could be a key risk to the cement price and hence the same could adversely affect the earnings of the company.
- At the current market price of Rs153 the stock trades at PE of 9.4x its FY2013E earnings and an EV/EBIDTA of 5.8x on FY2013E.

Name	CMP (Rs)	PER (x)			RoE (%)			Price target	Upside (%)
		FY11	FY12E	FY13E	FY11	FY12E	FY13E		
Marico	**175**	41.5	32.9	24.6	32.7	30.7	31.7	**186**	7

Remarks:

- Marico is one of the strongest players in the Indian hair care and edible oil markets. Its flagship brand Parachute along with Nihar commands a 54% share in the domestic branded coconut oil market. Its portfolio of value-added hair oil got strong traction in the domestic market helping it to clock around 20% volume growth in the domestic market. The company's good for heart edible oil brand Saffola is also witnessing mid-teen volume growth on account of improving consumer awareness.
- Apart from domestic operations, Marico has strong international presence in Bangladesh, Egypt, South Africa, and the recently entered South East Asia. Though the near-term performance has been affected by political instability and high inflationary environment in some of the international markets, we believe the long-term growth potential is intact in these markets.
- Kaya is showing signs of improvement with a double-digit same-store collection growth in the past few quarters.
- Any significant increase in the prices of the key raw materials (including copra) and a slowdown in the sales volume growth would act as the key risks to our earnings estimates.
- We expect the top line to grow at a CAGR of about 25% over FY2011-13 and the bottom line to grow at a CAGR of 30% over the same period (on the back of an expected improvement in the margins due to the softening of raw material prices). At the current market price the stock trades at 32.9x its FY2012E EPS of Rs5.3 and 24.6x its FY2013E EPS of Rs7.1.

Name	CMP (Rs)	PER (x) FY11	PER (x) FY12E	PER (x) FY13E	RoE (%) FY11	RoE (%) FY12E	RoE (%) FY13E	Price target	Upside (%)
Orient Paper	**59**	8.3	6.7	5.6	17.0	18.4	18.9	**70**	18

Remarks:

- OPIL, a part of CK Birla group, is a diversified conglomerate operating in three segments; cement, paper and fans. The cement division contributes over 53% of the total revenue. The company benefits due to its diversified business model.
- Due to the recent increase in cement prices, the present realisation of the company is higher by over 24% over FY2011. The surge in the realisation will be able to offset the cost inflation and the profitability of the division is likely to improve (marginally).
- In the electrical division, due to the new product launches and gaining market shares, the company would deliver over 11% revenue growth in FY2012. Going forward, the division can witness growth on the back of lighting products (CFL) and household appliances.
- The restructuring plan to demerge the cement division augurs well for the company as the uncertainty in the profitability of the paper division was one of the major overhangs on the stock. Hence, the valuation could get re-rated going ahead.
- However, the key concern remains the poor volume offtake in its key market, ie Andhra Pradesh (which accounts for 37% of the total dispatches).
- At the current market price of Rs59, the stock trades at a PE of 5.6x and EV/EBIDTA of 4.1x, discounting its FY2013 earnings estimate.

Name	CMP (Rs)	PER (x) FY11	PER (x) FY12E	PER (x) FY13E	RoE (%) FY11	RoE (%) FY12E	RoE (%) FY13E	Price target	Upside (%)
Selan Exploration	**280**	15.0	10.4	7.5	18.7	21.9	23.6	**500**	79

Remarks:

- Selan Exploration (Selan) has rights to develop five small discovered (minimal exploration risk) oil fields (Bakrol, Lohar, Indrora, Karjisan and Ognaj) in Cambay Basin (Gujarat) with proven oil & gas reserves.
- Between FY2006 and FY2009, Selan ramped up its production by 4x. In the next phase (FY2009-11), with stagnate oil production it did preparatory work to ramp up drilling in the existing fields and the new field, Indrora (the most prolific one with significant reserves). Currently, the company is waiting for the final approval for drilling which could ramp up its production significantly in the near future.
- Based on this, we expect the company to ramp up its production more than two times by FY2014 over that of FY2011. It would lead to an earnings growth (CAGR) of 41% during FY2011-13.
- At the current market price, the stock trades at a PE of 7.5x and EV/EBITDA of 3.6x based on our FY2013 estimates. We remain bullish on its production ramp-up plan and recommend Buy with a price target of Rs500.

Name	CMP (Rs)	PER (x) FY11	PER (x) FY12E	PER (x) FY13E	RoE (%) FY11	RoE (%) FY12E	RoE (%) FY13E	Price target	Upside (%)
Sun Pharma	**570**	32.5	24.2	24.0	19.2	21.1	17.7	**631**	11

Remarks:

- The combination of Sun Pharma and Taro offers an excellent business model for Sun Pharma, as has been reflected in the M9FY2012 performance (its revenue grew 31% YoY in M9FY2012).
- Though Taro may not show a similar performance in the next quarter, but we expect a better performance from Sun Pharma going forward mainly driven by the resumption of sales from the US based Cranbury facility, which has been cleared by the USFDA recently. Sun Pharma seeks to acquire the remaining equity in Taro and, if successful, that will not only help achieve better synergy but also boost earnings from the first year itself.
- We expect 24% and 16% revenue and PAT CAGR respectively over FY2011-13. With a strong cash balance, Sun Pharma is well positioned to capitalise on the growth opportunities. Its debt-free balance sheet insulates it from the negative impact of volatile currency.
- Due to provisions of Union Budget 2012-13, which provided for Alternate Minimum Tax (ALT) on partnership-based units availing various tax concessions, Sun Pharma's earnings are likely to get reduced to the extent of 9% in FY2013.
- At the current market price, Sun Pharma is trading at 24.2x and 24.0x FY2012 and FY2013 estimated EPS respectively. We maintain our Buy recommendation on the stock with a price target of Rs631, which implies 26x FY2013E EPS.

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