MORNING INSIGHT
kotak
Kotak Securities
PRIVATE CLIENT RESEARCH
FEBRUARY 6, 2011

Economy News

- The Asian Development Bank (ADB) sees Indian economy growing at 7-7.5 per cent this fiscal, lower than the 7.9 per cent growth forecast by it around September last year. (BL)
- Government may include 20 more categories such as construction, health, entertainment, restaurants, non-AC rail fares, travel by the metro or public buses, etc. under the service tax ambit in this Budget. (BS)
- Power ministry would introduce a rating methodology of utilities to enable them get loans, provide a reform-linked interest subsidy to utilities and promote distribution franchises to reduce aggregate transmission and commercial (AT&C) losses. (BS)
- The Reserve Bank of India has asked banks to exclude stamp duty, registration and like charges while calculating the value of a property which could lead to a further decline in home sales in the lower and medium segments. (BS)
- To safeguard interests of ailing aviation sector, a Group of Ministers will meet later this week on Thursday to give final touches on allowing FDI in aviation, direct import of jet fuel by Indian carriers and Air India's financial restructuring plan. (BS)
- The Reserve Bank of India has partially lifted the curbs on banks foreign exchange transactions imposed after the rupee came under attack from currency speculators. (ET)

Corporate News

- **NMDC Ltd** is set to use the huge cash pile of Rs 180 bn it is currently sitting on for overseas buys of iron ore and coking coal assets. (BL)
- **Reliance Industries,** which will have to start the process of discovering a new price for D6 gas in 2013, is in a fix over how it will go about the task. (BL)
- **NTPC** has received seven bids including from Adani Enterprise for procurement of 4 mn tonnes imported coal for its power plants across India. (BL)
- **Himadri Chemicals and Industries,** one of the largest Indian coal tar pitch (CTP) manufacturers has lined up investment plans worth Rs 12 bn in the state of West Bengal in the next four years. (BS)
- Public sector lender **Central Bank of India** may go in for restructuring of some of its loans given to power companies in the current quarter. (BS)
- Amid costly Indonesian coal putting a question mark over the viability of many power projects, **Tata Power** has said that the 4,000-MW Mundra UMPP could become a "non-performing asset" if no decision is taken on increasing tariffs for electricity from the plant. (BS)
- **Cairn India Ltd** has been unsuccessful in starting work on its 80km pipeline from Salaya to Bhogat in Gujarat because of opposition from some groups. (Mint)

Source: ET = Economic Times, BS = Business Standard, FE = Financial Express, BL = Business Line, ToI: Times of India, BSE = Bombay Stock Exchange

Equity

	3 Feb 12	% Chg 1 Day	1 Mth	3 Mths
Indian Indices				
SENSEX Index	17,605	1.0	10.9	0.2
NIFTY Index	5,326	1.1	12.0	0.8
BANKEX Index	11,644	1.4	19.6	3.0
BSET Index	5,912	0.9	0.6	2.6
BSETCG INDEX	10,260	0.3	20.0	(6.8)
BSEOIL INDEX	8,689	1.1	13.0	(3.7)
CNXMcap Index	7,324	0.5	17.3	0.1
BSESMCAP INDEX	6,687	0.5	17.2	(3.9)
World Indices				
Dow Jones	12,862	1.2	4.1	7.3
Nasdaq	2,906	1.6	8.7	8.2
FTSE	5,901	1.8	4.4	6.8
NIKKEI	8,832	(0.5)	6.4	1.4
HANGSENG	20,757	0.1	12.3	5.2

Value traded (Rs cr)

	3 Feb 12	% Chg - Day
Cash BSE	2,881	(20.6)
Cash NSE	13,650	(26.5)
Derivatives	95,491	(20.9)

Net inflows (Rs cr)

	2 Feb 12	% Chg	MTD	YTD
FII	2,135	2.0	4,228	15,317
Mutual Fund	(113)	(161.1)	72	(1,776)

FII open interest (Rs cr)

	2 Feb 12	% Chg
FII Index Futures	12,408	4.9
FII Index Options	34,844	2.8
FII Stock Futures	27,550	2.1
FII Stock Options	1,197	5.2

Advances / Declines (BSE)

3 Feb 12	A	B	T	Total	% total
Advances	141	1,216	359	1,716	57
Declines	62	822	281	1,165	39
Unchanged	1	81	30	112	4

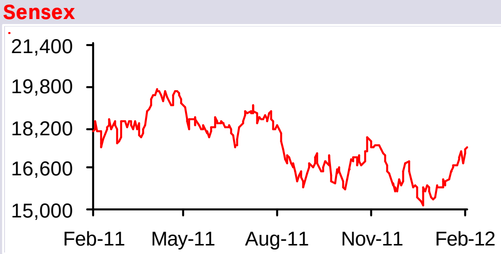
Commodity

	3 Feb 12	% Chg 1 Day	1 Mth	3 Mths
Crude (NYMEX) (US$/BBL)	97.3	(0.6)	(4.2)	3.2
Gold (US$/OZ)	1,738.7	(0.9)	7.4	(1.2)
Silver (US$/OZ)	33.8	(0.5)	16.9	(1.5)

Debt / forex market

	3 Feb 12	1 Day	1 Mth	3 Mths
10 yr G-Sec yield %	8.16	8.13	8.33	8.97
Re/US$	49.2	49.3	53.3	49.2

Sensex



RESULT UPDATE

Saday Sinha
saday.sinha@kotak.com
+91 22 6621 6312

ANDHRA BANK

PRICE: RS.110 **RECOMMENDATION: BUY**
TARGET PRICE: RS.148 **FY13 P/E: 4.0X; P/ABV: 0.9X**

Q3FY12 results: Stable Quarter; higher exposure to power sector (~17%) continues to be the potential risk.

- **NII grew 17.1% mainly aided by healthy growth in advances (20.7% YoY) despite 10 bps decline (YoY) in NIM. However, net profit was subdued (decline of 8.43% YoY) on back of spike in provisions on restructured book (Rs.2.33 bn in Q3FY12).**
- **Loan growth came at 20.7% during Q3FY12 mainly supported by strong growth in 'Corporate & Mid Corporate' and MSME segments. Deposit growth was also healthy at 20.2% YoY with marginal improvement in LDR to ~80% (135 bps QoQ) at the end of Q3FY12.**
- **Asset quality remained stable - in absolute terms, gross NPA and net NPA declined by 5.2% and 13.2%, respectively. Although slippage declined to 2.1% in Q3FY12 (annualized) from the high of 6.1% seen in the previous quarter, it is higher than the average run-rate of 1.5% witnessed during previous 4 quarters. Its Provision Coverage Ratio (PCR) excluding technical W/Os improved by 460 bps (QoQ) to ~50%, positive in terms of B/S quality.**
- **We are modeling earnings to grow 10.1% CAGR during FY11-13E, while returns profile is also expected to remain healthy (RoA: ~1.1%, RoE: ~20%) during next two years. We are maintaining BUY rating on the stock with unchanged TP of Rs.148 based on 1.2x of its FY13E adjusted book value.**

Result Performance

(Rs mn)	Q3FY12	Q3FY11	YoY (%)
Interest on advances	23,906.1	17,121.7	39.6
Interest on Investment	4,986.3	4,006.6	24.5
Interest on RBI/ banks' balances	337.6	87.5	285.8
Other interest	-	-	NM
Total Interest earned	**29,230.0**	**21,215.8**	**37.8**
Interest expenses	19,391.5	12,816.5	51.3
Net interest income (NII)	**9838.5**	**8399.3**	**17.1**
Other income	2,352.6	1,986.2	18.4
Net Revenue (NII + Other income)	**12,191.1**	**10,385.5**	**17.4**
Operating Expenses	4515.1	4119.4	9.6
Payments to / Provisions for employees	2,847.0	2,595.0	9.7
Other operating expenses	1,668.1	1,524.4	9.4
Operating profit	**7,676.0**	**6,266.1**	**22.5**
Provisions & contingencies	3,094.3	1,717.0	80.2
Provision for taxes	1,550.0	1,240.0	25.0
Total Provisions	4,644.3	2,957.0	57.1
Net profit	**3,031.7**	**3,309.1**	**-8.4**
EPS (Rs.)	**5.42**	**6.82**	**-20.5**

Source: Company

NII came at Rs.9.84 bn (17.1% YoY) mainly aided by strong growth in advances; however, net profit was subdued on back of spike in provisions on restructured book.

NII came at Rs.9.84 bn, a growth of 17.1% (YoY) mainly aided by healthy growth in advances (20.7% YoY) despite 10 bps decline (YoY) in NIM. However, net profit was subdued (decline of 8.43% YoY) on back of spike in provisions on restructured book (Rs.2.33 bn in Q3FY12).

Non-interest income grew at healthy pace (18.4% YoY) to Rs.2.35 bn in Q3FY12 mainly aided by strong growth in non-core component of other income (90.5% YoY, 57.2% QoQ).

Healthy business growth; LDR improved 135 bps QoQ to ~80% implying future deposits mobilization to be the key to fund its future loan growth.

Loan growth came at 20.7% during Q3FY12 mainly supported by strong growth in 'Corporate & Mid Corporate' and MSME segments; while growth in agriculture and retail segments remained muted at 13.0% and 9.1%, respectively.

Break up of Advances

(% of advaces)	Q12011	Q22011	Q32011	Q42011	Q12012	Q22012	Q32012
Corporate & Mid Corporate	51.9	52.4	52.5	54.0	NA	NA	53.8
Agriculture	15.5	15.8	15.3	14.4	13.8	14.4	14.4
MSME	15.3	15.1	15.0	15.4	15.3	15.5	15.0
Retail	15.4	15.1	15.3	14.5	14.4	14.8	13.8
Others	0.0	6.5	6.4	1.7	NA	NA	3.0

Source: Company

Deposit growth was also healthy at 20.2% YoY during the same period. In absolute terms, loan book grew faster than deposits leading to marginal improvement in LDR to ~80% (135 bps QoQ) at the end of Q3FY12.

Within deposits, CASA mix grew only by 12.1% YoY, while term deposits grew 23.4% YoY leading to 192 bps contraction in CASA share (26.6% at the end of Q3FY12). Going forward, we believe deposit mobilization would be the key to fund its future loan growth as not much scope is left to enhance the LDR (loan deposit ratio).

NIM remained healthy at 3.81% during Q3FY12 (3.8% during 9MFY12); we have modeled NIM at 3.71%/3.53% during FY12/ FY13 as against 3.8% witnessed during FY11.

NIM remained healthy at 3.81% (stable QoQ) during Q3FY12, marginally higher than our expectations. The change in loan mix (share of MSME and retail portfolio is declining) is impacting the yield of funds, which increased by 124 bps (YoY) while cost of funds rose by 136 bps.

Yield Movement

	Q12011	Q22011	Q32011	Q42011	FY11	Q12012	Q22012	Q32012
Advances	10.89	10.98	11.07	11.60	11.16	12.23	12.45	12.76
Investments	NA	6.91	NA	7.43	7.38	7.68	7.75	7.82
Yield from Assets	8.58	8.80	9.07	9.20	8.93	9.74	10.11	10.31
Cost of Deposits	5.49	5.67	5.84	6.48	5.90	7.02	7.46	7.59
Cost of Funds	5.19	5.25	5.48	5.85	5.46	6.37	6.65	6.84
NIM (%)	**3.72**	**3.91**	**3.91**	**3.69**	**3.80**	**3.77**	**3.82**	**3.81**

Source: Company

We believe NIM is less likely to stay at the current level as declining CASA share (~190 bps YoY) would impact the cost of funds for the bank, while there is little scope to further increase the C/D ratio (currently at ~80%) which remains at the elevated levels. We are modeling NIM at 3.71%/3.53% during FY12/FY13 as against 3.8% witnessed during FY11.

Asset quality remained stable; although slippage declined to 2.1% in Q3FY12 (annualized) from the high of 6.1% seen in Q2FY12, it is higher than the average run-rate of 1.5% witnessed during previous 4 quarters.

Asset quality remained stable - in absolute terms, gross NPA and net NPA declined by 5.2% and 13.2%, respectively. In percentage terms, gross NPA and net NPA now stands at 2.38% and 1.21% (as against 2.67% and 1.48%, respectively during Q2FY12), respectively at the end of Q3FY12.

Although slippage declined to 2.1% in Q3FY12 (annualized) from the high of 6.1% seen in Q2FY12, it is higher than the average run-rate of 1.5% witnessed during previous 4 quarters. Its Provision Coverage Ratio (PCR) excluding technical W/Os improved by 460 bps (QoQ) to ~50%, positive in terms of B/S quality.

Trend in asset quality

	Q1FY11	Q2FY11	Q3FY11	Q4FY11	Q1FY12	Q2FY12	Q3FY12
Gross NPA (Rs. bn)	5.79	7.70	8.72	9.96	11.76	19.87	18.84
% of Net NPA	1.01	1.26	1.33	1.38	1.55	2.67	2.38
Net NPA (Rs. bn)	1.70	2.39	3.08	2.74	3.37	10.87	9.43
% of Net NPA	0.30	0.49	0.47	0.38	0.45	1.48	1.21

Source: Company

During Q3FY12, provisions spiked 80.2% YoY on back of Rs.2.3 bn provided on account of restructured book. During the same period NPA provisions declined 74% YoY on back of robust upgradation/recovery (Rs.4.83 bn as against slippage of Rs.3.81 bn). We are modeling higher credit costs at 139 bps in FY12 and 121 bps in FY13 as against 115 bps witnessed in FY11.

Provisions & Contingencies

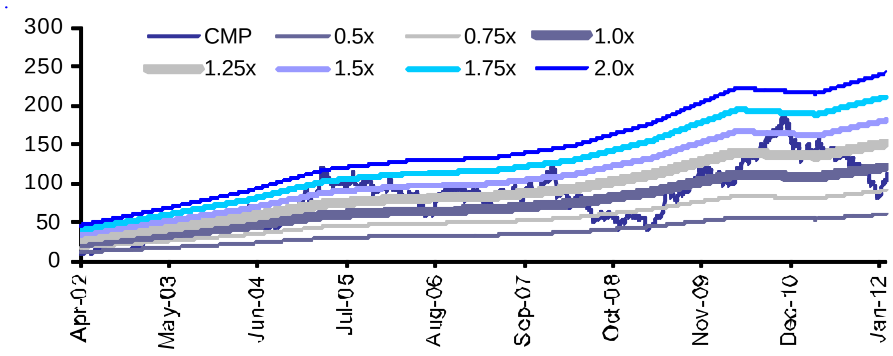
(Rs bn)	Q32011	Q42011	Q1 2012	Q22012	Q32012
NPA	1.52	2.03	1.17	2.21	0.39
Std assets (includes prov on restructured book)	0.32	0.40	0.33	0.30	2.48
Investment Depreciation	0.00	0.00	0.02	0.03	0.19
Transfer of Investment to HTM category	0.00	0.00	0.24	0.00	0.00
Other provisions	-0.12	0.60	0.01	0.06	0.03
Total	**1.72**	**3.03**	**1.77**	**1.77**	**3.09**

Source: Company

Valuation & recommendation

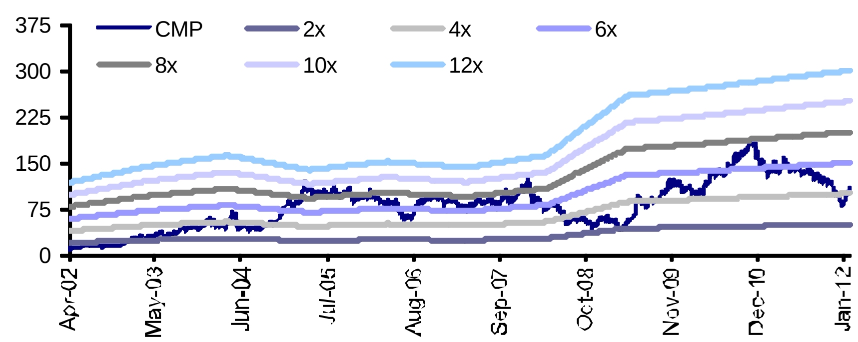
At the current market price of Rs.110, the stock is trading at 4.0x its FY13E earnings and 0.9x its FY13E ABV. We believe higher exposure to Infrastructure (especially Power exposure at Rs.132 bn, ~17% of loan book) continues to be the potential risk for its asset quality.

Rolling 1-year forward P/ABV band



Source: Company, Kotak Securities - Private Client Research

Rolling 1-year forward P/E band



Source: Company, Kotak Securities - Private Client Research

We recommend BUY on Andhra Bank with a price target of Rs.148

We are modeling earnings to grow 10.1% CAGR during FY11-13E, while returns profile is also expected to remain healthy (RoA: ~1.1%, RoE: ~20%) during next two years. We are maintaining **BUY** rating on the stock with unchanged TP of Rs.148 based on 1.2x of its FY13E adjusted book value.

Key Financials:

(Rs. bn)	2010	2011	2012E	2013E
Interest income	63.73	82.91	113.27	129.21
Interest expense	41.78	50.70	74.84	86.71
Net interest income	**21.95**	**32.21**	**38.43**	**42.50**
Growth (%)	34.9	46.8	19.3	10.6
Other income	9.65	8.97	8.50	9.29
Gross profit	18.10	24.13	28.90	31.86
Net profit	**10.46**	**12.67**	**13.39**	**15.37**
Growth (%)	60.1	21.2	5.7	14.7
Gross NPA (%)	0.9	1.4	2.6	2.5
Net NPA (%)	0.2	0.4	1.3	1.1
Net int. margin (%)	3.2	3.8	3.7	3.5
CAR (%)	13.9	14.4	12.8	12.4
RoE (%)	26.0	23.2	19.6	20.4
RoA (%)	1.3	1.3	1.1	1.1
Dividend per share (Rs)	5.0	5.5	6.0	7.0
EPS (Rs)	**21.6**	**22.6**	**23.9**	**27.5**
Adjusted BVPS (Rs)	**88.9**	**111.1**	**107.6**	**123.2**
P/E (x)	**5.1**	**4.9**	**4.6**	**4.0**
P/ABV (x)	**1.2**	**1.0**	**1.0**	**0.9**

Source: Company, Kotak Securities - Private Client Research

RESULT UPDATE

Sanjeev Zarbade
sanjeev.zarbade@kotak.com
+91 22 6621 6305

THERMAX LTD

PRICE: RS.522 **RECOMMENDATION: REDUCE**
TARGET PRICE: RS.505 **FY13E P/E: 17.1X**

- **The deceleration in the revenue growth of Thermax was largely expected as the order backlog has been on a declining trend.**
- **Order backlog (Standalone) is down 20% yoy to Rs 51 bn, thus imparting a revenue visibility of 12 months based on trailing four quarters revenues. Revenue visibility has been trending downwards in FY11 as order intake has decelerated.**
- **Order intake (Standalone) of Rs 5.9 bn in the quarter, down 40% and 49% yoy as well as sequentially.**
- **We downgrade rating from Accumulate to REDUCE in view of reducing revenue visibility as a result of weak order intake and weak macroeconomic scenario (elevated interest rates). Target price revised to Rs 505 (Rs 484 earlier)**

Summary table

(Rs mn)	FY11	FY12E	FY13E
Sales	53371	58042	57177
Growth (%)	58	9	-1
EBITDA	5746	6021	5759
EBITDA margin (%)	10.8	10.4	10.1
PBT	5743.6	5917.0	5489.6
Net profit	3777	3911	3629
EPS (Rs)	31.7	32.9	30.5
Growth (%)	46.0	3.6	-7.2
CEPS (Rs)	36.7	37.7	35.6
BV (Rs/share)	110.5	132.8	152.8
Dividend / share (Rs)	9.0	9.0	9.0
ROE (%)	24.5	20.4	16.7
ROCE (%)	39.2	32.4	26.7
Net cash (debt)	8433	5354	4659
NW Capital (Days)	-18.3	7.2	21.2
EV/Sales (x)	1.0	1.0	1.0
EV/EBITDA (x)	9.4	9.5	10.0
P/E (x)	16.4	15.9	17.1
P/Cash Earnings	14.2	13.8	14.6
P/BV (x)	4.7	3.9	3.4

Source: Company, Kotak Securities - Private Client Research

Quarterly financial performance

(Rs mn)	Q3FY12	Q3FY11	YoY (%)	9MFY12	9MFY11	YoY (%)
Net Sales	**12,630**	**12,161**	**3.9**	**35,826**	**30,427**	**17.7**
other income from operations	64	250	-74.6	347	797	-56.5
Total Expenditure +	**11,339**	**10,947**	**3.6**	**32,276**	**27,516**	**17.3**
Raw Matl costs	8,029	8,178	-1.8	23,716	20,278	17.0
Purchase of trading goods	660	468	41.1	1,385	1,072	29.2
Staff costs	1,042	975	6.9	2,932	2,697	8.7
Other costs	1,608	1,327	21.2	4,243	3,469	22.3
PBIDT	**1,354**	**1,464**	**-7.5**	**3,896**	**3,707**	**5.1**
Other Income	157	117	34.0	512	390	31.3
Depreciation	120	106	13.5	348	316	9.9
EBIT	**1,391**	**1,476**	**-5.7**	**4,060**	**3,781**	**7.4**
Interest	7	2	245.0	22	12	78.7
PBT	**1,384**	**1,474**	**-6.1**	**4,039**	**3,769**	**7.2**
Tax	429.3	471	-8.9	1,268	1,212	4.6
Adj Profit After Tax	**955**	**1,002**	**-4.7**	**2,771**	**2,557**	**8.4**
Extra-ordinary Items +	-	-		-	-	
Rep Profit After Extra-ord item	**955**	**1,002**		**2,771**	**2,557**	**8.4**
EPS (Rs)	**8.0**	**8.4**		**23.3**	**21.5**	**8.4**
Ratios (%)						
PBDIT % exc other op income	10.2%	10.0%		9.9%	9.6%	
RM costs to sales (%)	64%	71%		66%	70%	
Other costs to sales (%)	12.7%	10.9%		11.8%	11.4%	
PBIDTM (%)	10.7%	12.0%		10.9%	12.2%	
Tax rate (%)	34%	34%		34%	35%	

Source: Company

Result Highlights

- The deceleration in the revenue growth of Thermax was largely expected as the order backlog has been on a declining trend. For the quarter, Thermax reported modest revenue growth of 3.9% yoy to Rs 12.6 bn. With large orders hard to come by, the company has been banking on short-cycle orders.
- Revenue visibility has declined to 12 months of trailing four quarter revenues from a high of 23 months, we believe revenue growth can decelerate significantly.

- Segment-wise, the revenues of energy segment have remained flat while the environment segment has registered a modest revenue growth of 3% yoy.

Segment revenues

(Rs mn)	Q3FY12	Q3FY11	% change
Segment- Energy	9931	9904	0
Segment - Enviro	3024	2943	3

Source: Company

- EBITDA margin for the quarter was down 120 bps yoy to 10.7% mainly due to lower other operating income and under-absorption of fixed expenditure.
- Bulk of the order backlog is fixed priced. The company freezes prices of bulk of the material and components including specialised steel for boilers and bought-outs like valves. The balance material consists of structural steel which is procured on a spot basis. This restricts volatility in margins due to material price fluctuation.
- The company has been working at making its cost structure flexible through higher contract labour and leveraging its long-term relationship with vendors.

Segment Margins

(%)	Q3FY12	Q3FY11
Segment- Energy	9.5	10.8
Segment - Enviro	13.0	13.6

Source: Company

Consolidated PAT lower due to losses at Chinese subsidiary

Consolidated PAT for the quarter was lower (than the standalone PAT) by 11% yoy due to loss at its Chinese Subsidiary which makes Chillers. The Chinese operations are expected to turnaround in FY13.

Consolidated Numbers

	Q3FY12	Q3FY11	YoY (%)	9MFY12	9MFY11	YoY (%)
Revenues	14671.8	13716.2	7.0	42,004	33,723	24.6
PBT	1328.8	1540.8	-13.8	4,132	3,895	6.1
PAT	942.9	1061.6	-11.2	2,886	2,644	9.2

Source: Company

Order intake sharply lower as projects finalisations dwindles significantly in Q3FY12

- Order backlog (Standalone) is down 20% yoy to Rs 51 bn, thus imparting a revenue visibility of 12 months based on trailing four quarters revenues. Revenue visibility has been trending downwards in FY11 as order intake has decelerated.
- Order intake (Standalone) of Rs 5.9 bn in the quarter, down 40% and 49% yoy as well as sequentially.
- Traditionally the main user industries are Power, Ferrous, Textiles and Cement. The company receives low value boiler orders from Food processing and Breweries. During the quarter, there was no major EPC order won by the company.
- The company indicated that due to elevated interest rates (~13-14%), Eurozone crisis, and policy bottlenecks, finalization of big-ticket projects had dropped to a trickle. This situation was more pronounced in the power sector. As a result, order inquiries were sharply lower in the Q3FY12.

- The management indicated that there are early signs of improvement in investor sentiment since January 2012.
- Despite being in a favourable position, the company lost out on one large utility order from a steel major. This order was ultimately won by a PSU competitor.

Capacity expansion

The capacity expansion initiatives are progressing on schedule. Construction work at the manufacturing facility for supercritical boilers set up by its joint venture (with Babcock Wilcox) is going on and the plant is expected to be commissioned in September 2012. TBW has been prequalified for the recent NTPC tenders. Thermax has indicated that there is informal understanding with Babcock and Wilcox for joint servicing of the Asian power generation market.

Other concall highlights

- The management expected to maintain revenues in FY13 at FY12's level despite the sharp drop in order backlog.
- The company expects to maintain EBITDA margins at double-digit level. We have built in a 30 bps reduction in EBITDA margins in FY13.
- The management indicated that it has no IPP orders under negotiation at this stage.
- Power projects based in non-coastal areas would find it challenging to import coal due to logistical constraints.
- BHEL has become increasingly price-competitive in recent times due to shortage of orders in the market.
- There have early signs of uptick in industrial investment. For instance, the Tata Steel project at Kalinganagar has been revived and POSCO steel project may also see light of the day. The management indicated that order intake in the next year should rebound if industrial investment sentiment improves.

Assumption

WACC (%)	13.4
NPV of cash flows 2011-24	35524
TV	22906
Profit growth between FY11-19 (%)	12.0
One year forward target price	505

Source: Kotak Securities - Private Client Research

Earnings Outlook - Maintain estimates for FY12. Introduce FY13 estimates

In view of the weak order intake in 9M FY12, we project 27% decline in order intake in FY12 followed by a recovery in FY13. We forecast the company to exit FY12 with an order backlog of Rs 49.4 bn down 25% yoy. A utility order win in the power space could pose upside risk to our order backlog estimate. We forecast revenue and earnings to decline in FY13.

Change in Earnings Estimates

(Rs mn)	FY12		FY13E	
	Earlier	Revised	Earlier	Revised
Revenue (Rs mn)	60194	58042	55989	57177
EBITDA (%)	10.5	10.4	10.1	10.1
EPS (Rs)	35.8	32.9	32.3	30.5
% change		-8.2		-5.6

Source: Kotak Securities - Private Client Research

Valuation - Downgrade to Reduce on fair valuations and limited

We recommend REDUCE on Thermax with a price target of Rs.505

We downgrade rating from Accumulate to **REDUCE** in view of reducing revenue visibility as a result of weak order intake and deteriorating macroeconomic scenario (rising interest rates). Target price revised to Rs 505 (Rs 484 earlier)

RESULT UPDATE

Teena Virmani
teena.virmani@kotak.com
+91 22 6621 6302

PRATIBHA INDUSTRIES LTD

PRICE: RS.46 **RECOMMENDATION: BUY**
TARGET PRICE: RS.62 **FY13E P/E: 5.0X**

Result highlights: Pratibha industries revenue growth was better than our estimates led by improved execution. Order inflow also remained strong during the quarter. Operating margins stayed strong, though lower than last year. Net profit growth was impacted by higher borrowings but growth was better than our estimates. We continue to remain positive on the company and maintain BUY.

- **Revenues of the company reported a growth of 53.2%% for Q3FY12, better than our estimates.**
- **Operating margins were in line with our estimates and stood at 13%. Company expects to maintain margins between 13-14% going forward.**
- **Net profit growth was impacted by increase in borrowings for large sized projects and stood at 35%YoY. This was however boosted by better than expected revenue growth.**
- **At current price of Rs46, stock is trading at 5.3x and 5.0x P/E and 4.4x and 4.3x EV/EBITDA on FY12 and FY13 estimates respectively. We tweak our estimates to factor in higher revenue growth and higher borrowings and continue to maintain BUY on the stock with an unchanged price target of Rs 62.**

Summary table

(Rs mn)	FY11	FY12E	FY13E
Sales	12,681	16,195	19,434
Growth (%)	26.0	28.0	20.0
EBITDA	1,720	2,267	2,526
EBITDA margin (%)	13.6	14.0	13.0
PBT	968	1,186	1,264
Net profit	714	866	923
EPS (Rs)	7.2	8.7	9.3
Growth (%)	6.0	21.0	6.6
CEPS(Rs)	8.9	10.7	12.1
Book value(Rs/share)	47.1	55.4	64.2
DPS (Rs)	0.4	0.4	0.4
ROE (%)	19.2	17.0	15.5
ROCE (%)	19.9	20.8	19.0
Net debt	3,107	5,338	6,361
NW capital (days)	123.2	135.0	135.0
P/E (x)	6.5	5.3	5.0
P/BV (x)	1.0	0.8	0.7
EV/Sales (x)	0.6	0.6	0.6
EV/EBITDA (x)	4.5	4.4	4.3

Source: Company, Kotak Securities - Private Client Research

Financial highlights -Consolidated results

(Rs mn)	Q3FY12	Q3FY11	YoY (%)
Net Sales	**4,507.5**	**2,942**	**53.2**
Expenditure	3,943	2,499	57.8
Raw material	3,189	2,191	
As a % of net sales	71%	74%	
Employee cost	312	140	
As a % of net sales	7%	5%	
Other expenditure	442	168	
As a % of net sales	10%	6%	
EBITDA	**564**	**443**	**27.5**
EBITDA margin	13%	15%	
Depreciation	55	44	
EBIT	**509**	**399**	**27.6**
Interest	300	210	
PBT (exc other income)	209	189	10.4
Other Income	57	13	
PBT	**266**	**202**	**31.7**
Tax	75	60	
Tax (%)	28%	30%	
PAT	**191**	**142**	**34.7**
NPM (%)	4.2%	4.8%	
No. of shares	99.43	99.43	
EPS (Rs)	**1.92**	**1.42**	

Source: Company

Revenue growth led by healthy order book and execution

- Revenues of the company reported a growth of 53.2% for Q3FY12, better than our estimates. We believe this was led by improvement in execution in large sized projects like Delhi Metro and Delhi Jal Board project. Order inflow also remained strong for the company during Q3FY12 and stood at Rs 13.43 bn spread across building, water supply and irrigation segment.
- Order inflow during 9MFY12 stood at nearly Rs 25 bn corresponding to company's share in the projects and current order book stands at nearly Rs 65 bn diversified across buildings, tunnelling, water and roads. Company continues to witness improved traction in the building segment mainly from real estate developers and water supply segment led by excellent order inflows from Gujarat and Delhi region. Orders awarded during FY12 in the building segment include -
  - Order worth Rs 3.6 bn from Runwal Homes for civil and structural works of a residential building 'Runwal Greens' located at Mulund-Goregaon Link Road, Mulund (West). The project is scheduled to be completed within a period of 27 months and will have a total built up area of 40 lakh sq. ft.
  - Order worth Rs1.79 bn from Lodha Group for its prestigious project 'Casa Rio'. This involves the construction of 58 buildings for the integrated township to be set up at Dombivali. The project is scheduled for completion within a period of 16 months in two phases.
  - Order worth Rs 1.53 bn from Rustomjee Realty Pvt Ltd for civil and structural works of a residential buildings at Upper Juhu, Andheri (W). The project is scheduled to be completed within a period of 26 months and will have a total built up area of 14 lakh sq. ft.
  - Another project is from Tata Housing and Development company worth Rs 1.36 bn for its prestigious project Tata Amantra with a total built up area of 30 lakh sqft and completion time frame of 27 months.
  - During the year, company also bagged contract worth Rs 606 mn from Magnum Developers for construction of residential building.
- Irrigation and water supply segment witnessed increased traction from Gujarat with company bagging projects worth Rs 5.04 bn from Gujarat Water Infrastructure Ltd during the current fiscal.
- Pratibha industries continues to remain confident about the building and water supply related projects and expects to tap upcoming opportunities from urban infra especially metro projects like Delhi Metro phase III, water supply especially from NCR- Yamuna River Action Plan, Gujarat and Rajasthan.
- We revise our revenue estimates upwards and expect revenues to grow at a CAGR of 24% between FY11-FY13.

Margins continue to stay strong

- Operating margins were in line with our estimates and stood at 13%. Company has been able to maintain margins due to its diversified project mix and higher margin water supply related projects.
- Company expects to maintain margins between 13-14% going forward. We thus continue to maintain our operating margin estimates and expect margins to be 14% and 13% for FY12 and FY13 respectively.

Working capital and borrowing requirements continue to stay high; impacting net profit growth

- Net profit growth was impacted by increase in borrowings for large sized projects and stood at 35%YoY. This was however boosted by better than expected revenue growth.
- We expect borrowings to remain high in near future to meet increased working capital requirements as well as higher capex. We tweak our estimates slightly to factor in higher borrowings and thus expect net profits to grow at a CAGR of 13.7% between FY11-FY13.

Valuation and recommendation

We rmaintain BUY on Pratibha Industries with a price target of Rs.62

- At current price of Rs46, stock is trading at 5.3x and 5.0x P/E and 4.4x and 4.3x EV/EBITDA on FY12 and FY13 estimates respectively.
- We value core business at 6x FY13 estimated earnings and add valuation of its BOT investments at book value.
- We continue to maintain BUY on the stock with an unchanged price target of Rs 62.

RESULT UPDATE

Arun Agarwal
arun.agarwal@kotak.com
+91 22 6621 6143

ESCORTS LTD

PRICE: RS.78 **RECOMMENDATION: ACCUMULATE**
TARGET PRICE: RS.89 **FY12E P/E: 9.6X**

1QFY12 Result update - Disappointment becoming a habit

- **Escorts 1QFY12 results once again disappointed with revenues, EBITDA margin and net profit coming below expectations.**
- **Revenues during the quarter remained flat YoY, whereas EBITDA dropped by 21% YoY. Loss in railway equipment division led to drop in EBITDA margin from 4.1% to 3.2%. Accordingly, PAT was lower by 57% over 1QFY11.**
- **Company's performance for the past few quarters had been disappointing but we were expecting improvement given strong growth in tractor demand.**
- **However, tractor demand has started to slowdown and we expect that to impact the company's earnings in FY12. Further, lower order off-take from the railway equipment division has led to loss in 1QFY12 from this division. Company's construction equipment business too has posted net loss due to lower margins and rise in interest cost.**
- **On the back of reasons mentioned above, we are lowering our revenue estimates by 8.7% primarily due to lowering of tractor volume estimates. We are pruning down our EBITDA margin estimates from 5% to 3.5% to factor in weak tractor demand scenario and losses from the railway equipment division and construction equipment business. Based on above measures, our revised FY12 net profit estimates stands lower by 41%.**
- **Due to downward revision in our earnings estimate we are cutting down our DCF based price target to Rs89 (from Rs157). At our revised target price of Rs89, the stock will trade at a PE of 10.9x, price/sales of 0.2x and price/book of 0.5x. We downgrade the stock from BUY to ACCUMULATE.**

Summary table - Consolidated

(Rs mn)	FY10	FY11E	FY12E
Sales	33,242	40,503	41,960
Growth (%)	28.0	21.8	3.6
EBITDA	1,909	1,304	1,518
EBITDA margin (%)	5.7	3.2	3.6
PBT	1,813	1,097	1,123
Reported PAT	1,320	1,264	778
Reported EPS (Rs)	13.8	13.2	8.2
Growth (%)	289.0	(4.3)	(38.4)
CEPS (Rs)	19.4	18.3	15.1
BV (Rs/share)	176.5	186.7	193.9
Dividend / share (Rs)	1.7	1.7	1.1
ROE (%)	8.3	7.7	4.3
ROCE (%)	9.7	6.5	5.5
Net cash / (debt)	(1,936)	(1,702)	(2,314)
NW Capital (Days)	45	46	50
P/E (x)	5.6	5.9	9.6
P/BV (x)	0.4	0.4	0.4
EV/Sales (x)	0.3	0.2	0.3
EV/EBITDA (x)	5.3	7.6	7.0

Source: Company, Kotak Securities - Private Client Research

Quarterly Data - Standalone entity

(Rs mn)	1QFY12	1QFY11	YoY(%)	4QFY11	QoQ (%)
Revenues	**8,231**	**8,278**	**(0.6)**	**7,636**	**7.8**
Total expenditure	7,964	7,939	0.3	7,337	8.6
RM consumed	6,064	6,042	0.4	5,460	11.1
Employee cost	927	801	15.8	771	20.2
Other expenses	974	1,097	(11.2)	1,105	(11.9)
EBITDA	**267**	**339**	**(21.2)**	**299**	**(10.8)**
EBITDA margin	3.2	4.1		3.9	
Depreciation	97	100	(2.3)	97	(0.1)
Interest cost	114	37	209.4	80	43.1
Other operating income	67	100	(32.8)	88	(23.9)
Other Income			-	-	-
EO income/(loss)	(18)	6	-	(99)	(81.4)
PBT	**104**	**308**	**(66.2)**	**111**	**(6.4)**
PBT margins	1.3	3.7		1.5	
Tax	(5)	53	-	30	(115.9)
Tax rate	(4.5)	17.2		26.6	
Reported PAT	**109**	**255**	**(57.4)**	**82**	**33.2**
PAT margins	1.3	3.1		1.1	
No. of equity shares	102	102	0.0	102	-
EPS (Rs)	**1.1**	**2.5**	**(57.4)**	**0.8**	**33.2**

Source: Compqny

1QFY12 result update (Standalone)

- Escorts 1QFY12 results came in below expectations. Revenues for the quarter stood at Rs8,231mn as against our expectation of Rs.8569 mn. Lower than expected tractor sales during the quarter led to shortfall in revenues. Revenues remained flat YoY.
- Agri machinery group (AMG) revenues stood at Rs7,728mn as against Rs7,730mn reported during 1QFY11. Tractor volumes during the period stood at 16,606 units against 16,333 units sold in 1QFY11. Realization during the same period saw a marginal dip due to product mix.
- EBIT margins from the AMG segment dropped from 6.2% in 1QFY11 to 5.8% in 1QFY12 but an improvement over 4QFY11 margin of 5.5%. However the margin remains well below the 10% average reported in FY10.
- Railway equipment division (RED) revenues were a major disappointment during the quarter and prime reason for poor 1QFY12 performance. Revenues during the quarter from this division fell from Rs423mn in 1QFY11 and Rs552mn in 4QFY11 to Rs303mn in 1QFY12.
- Lower order off-take from the railways led to drop in revenues. Lower revenues led to in efficient utilization of fixed overheads and accordingly the company reported losses from this segment. This has been one of the high margin segment for the company and loss in this segment has impacted the overall performance of this quarter. EBIT margin fell from 19.5% in 4QFY11 to negative 2.1% in the quarter under consideration.
- Revenues in the auto ancillary business grew by 25% YoY to Rs311mn. However the company continues to report losses from this segment. During the quarter, Escorts reported a negative EBIT of 16% from this segment.

Segmental Revenues - Standalone entity

(Rs mn)	1QFY12	1QFY11	YoY(%)	4QFY11	QoQ (%)
Agri Machinery	7,728	7,730	(0.0)	6,919	11.7
Auto Ancillary	311	250	24.6	297	4.5
Railway Equipments	303	423	(28.4)	552	(45.1)

Source: Company

Segmental margins - Standalone entity

(Rs mn)	1QFY12	1QFY11	4QFY11
Agri Machinery	5.8	6.2	5.5
Auto Ancillary	(16.0)	(21.9)	(18.8)
Railway Equipments	(2.1)	7.0	19.5

Source: Company

- On the back of poor show from railway equipment segment, the company reported 21% drop in EBITDA that came down from Rs339mn to Rs267mn. Sequentially EBITDA was lower by 11%.
- EBITDA margin for the quarter came in at 3.2% as against margins of 4.1% in 1QFY11 and 3.9% in 4QFY11.
- Increase in raw material cost (steel and rubber) during the quarter too negatively impacted the margins for the company.
- Employee cost increased by 20% QoQ on account of annual increments in wages and salaries.
- Other expenses though saw a reduction in 1QFY12.

- Increased usage of working capital limits and higher interest cost led to sharp rise interest cost from Rs37mn in 1QFY11 to Rs114mn in 1QFY12.
- Exceptional item of Rs18mn mainly pertained to write-off of provision for doubtful debts. Debt write-off led to tax write-back of Rs5mn during the quarter.
- PAT for the quarter stood at Rs109mn that was much lower than our expectation of Rs265mn. PAT came in 57% lower YoY.

Escorts construction equipment - 1QFY12 performance review

- Sales in this 100% subsidiary of Escorts grew by 26% YoY to Rs2,090mn.
- However EBITDA margin over the same period dropped from 3.6% to 1.9%. Decline in margins happened due to increase in commodity prices and mandatory switching over from BS II to BS III engines.
- Further 49% rise in interest cost led to net loss of Rs14.2mn for the quarter as against profit of Rs10.8mn in 1QFY11. 4QFY11 profit from this segment stood at Rs44.2mn.

Initiatives planned by the company to improve performance

- In the tractor segment, company has already taken a 1.5%+ price increase in January 2012 in line with competitors to deal with rise in material cost.
- INR appreciation could be positive for raw material. Further rubber prices too have softened and the same should work positively for the margins.
- Company is in advanced field testing stage for the new 50HP tractor designed specifically for black cotton soil areas of Karnataka and Andhra Pradesh.
- Further initiatives for the tractor business includes 1.New dealer appointment in unrepresented territories that accounts for 8% of total industry 2.Rationalization and strengthening of dealer network 3.Tie-up with leading manufacturers of farm implements in order to push for rotary tillers.
- In the auto suspension segment, the company is banking on price increases from the customers and cost control for margin improvement. Further the company is also working on new better margin products for the domestic and export markets. Company has added new customers like Suzuki Motorcycle and Piaggio for their new motorcycle and scooter models respectively.
- For the railway equipment division, the company claims that the order book for 2QFY12 is better than 1QFY12 and thus expect their performance to improve going ahead. Further, in line with railways expansion requirements the company has inked collaborations with DAKO (Czechoslovakia) for manufacture of disc brakes, Ingeteam (Spain) for traction systems and Honeywell (USA) for brake blocks over the last few months. Company is also ready with some new product for the Indian railway which is expected to translate into orders going forward.
- Escorts construction equipment future sales growth initiatives include 1.Looking at African markets and 2.Expanding its distribution base from 110 to 145 locations.

Change in estimates

- We are significantly lowering our FY12 estimates on account of three prime reasons.
- Firstly, tractor industry demand has started to weaken and the same will impact the company's FY12 earnings as 75% of the consolidated revenues come from this segment. Slowing tractor volumes will also have negative impact on the operating margins.

- Secondly, detoriating performance of the railway equipment division. Lower order off-take led to net loss from this segment during the quarter. Poor performance from this segment will have negative bearing on the overall operating performance of Escorts for this being a high margin business for the company.
- Thirdly, Escorts construction equipment business too faced margin pressure during the quarter leading to net loss for the quarter which otherwise had been a profitable venture for the company.
- Out of the four segments, the company operates into; it posted net loss in three of them. Further the only profitable tractor segment is showing signs of weakness.
- Based on the above mentioned reasons, we have cut our FY12 revenue estimates by 8.7%, lowered our EBITDA margin estimates from 5% to 3.6% leading to 41% lowering of our consolidated net profits.

Change in estimates (FY12)

(Rs mn)	Old	New	% change
Revenues	45,969	41,960	(8.7)
EBITDA margin (%)	5.0	3.6	-
PAT	1,325	778	(41.2)

Source: Kotak Securities - Private Client Research

Valuations

We recommend ACCUMULATE on Escorts with a price target of Rs.89

- Due to downward revision in our earnings estimate we are cutting down our DCF based price target to Rs89 (from Rs157).
- At our revised target price of Rs89, the stock will trade at a PE of 10.9x, price/sales of 0.2x and price/book of 0.5x.
- We downgrade the stock from BUY to **ACCUMULATE.**

Bulk deals

Trade details of bulk deals

Date	Scrip name	Name of client	Buy/ Sell	Quantity of shares	Avg. price (Rs)
3-Feb	Aryaman Fin	Sadhana Sachin Deshmukh	B	100,765	20.8
3-Feb	Aryaman Fin	D Mehta Mitesh	S	100,000	20.8
3-Feb	Banas Finance	Pondurai	S	821,000	55.9
3-Feb	Banas Finance	Pondurai Balaselvi	S	793,000	55.9
3-Feb	BDH Inds	Raj Kumar Lohia	B	51,651	17.0
3-Feb	BDH Inds	Pushpa Balkrishna Kabare	S	51,000	17.1
3-Feb	Devine Impex	New Horizon Equity Advisors Pvt Ltd	B	50,000	20.0
3-Feb	Devine Impex	Pine Tree Consultants Pvt Ltd	S	50,000	20.0
3-Feb	Dhvanil Chem	Arsenal Finstock Services Pvt Ltd	B	40,000	38.7
3-Feb	Dr Agarwals-$	Amit Goel	B	200,500	146.3
3-Feb	Dr Agarwals-$	Discovery Wealth Mgmt Services	S	200,000	146.3
3-Feb	Essen Supp	R S Vinimay Pvt.Ltd.	B	50,000	59.2
3-Feb	Essen Supp	Rekha Gupta	S	55,000	58.5
3-Feb	Essen Supp	Sangeeta Bajoria	S	37,500	59.4
3-Feb	Gflfin	Swastik Vintrade Pvt Ltd	B	51,000	31.2
3-Feb	Gflfin	Ramtech Industries Pvt. Ltd.	B	160,335	32.4
3-Feb	Gflfin	Rajesh HUF	S	30,000	31.2
3-Feb	Gflfin	Aishwarya Dubey	S	34,000	31.2
3-Feb	Gflfin	Rupesh Kumar Singh	S	34,500	34.3
3-Feb	Gflfin	Asha Agarwal	S	50,000	31.2
3-Feb	Gujarat Medi	Gold Dust Trading Co	B	48,054	19.1
3-Feb	Gujarat Medi	Usha Devi Agarwal	S	28,000	19.5
3-Feb	Hittco Tools	Umeshbhai Mahashankar Purohit	B	29,000	9.8
3-Feb	Hittco Tools	Pushpaben Bansilal Talati	B	30,000	9.8
3-Feb	Hittco Tools	Ami Dipesh Talati	B	70,000	9.8
3-Feb	Hittco Tools	Citadel Software Pvt Ltd	S	99,096	9.8
3-Feb	Hittco Tools	Amit Capital And Securites Pvt Ltd	S	100,000	9.8
3-Feb	Kanchan Intl	Slp Traders (Satish Vasant Ghone)	B	24,820	86.0
3-Feb	Kanchan Intl	Suresh Laxman Patil	S	35,000	86.0
3-Feb	Khaitan Chem	Vardhaman Textile Company Pvt Ltd	S	1,000,000	15.1
3-Feb	Kwality Cred	Smita Srivastava	B	25,000	33.9
3-Feb	Kwality Cred	Rekha Digvijay Shah	B	75,000	33.9
3-Feb	Kwality Cred	Pawantar Agro Agencies Pvt Ltd	S	28,512	33.9
3-Feb	Kwality Cred	Kalpa Mercantile Pvt Ltd	S	24,000	33.9
3-Feb	Kwality Cred	Chirayush Agro Marketing Pvt Ltd	S	24,000	33.9
3-Feb	Kwality Cred	Sangam Agro Agencies Pvt Ltd	S	24,000	33.9
3-Feb	Pankaj Poly	Ramakant Mangalchand Gaggar	B	64,021	9.4
3-Feb	Pankaj Poly	STC Securities Pvt Ltd	S	35,413	9.4
3-Feb	Parichay Invest	Arif Gulammustufa Shaikh	B	11,604	39.0
3-Feb	Pasupati Fin	Amit Krishnakant Thakker	S	40,000	31.6
3-Feb	Ravinay Trad	Hotel Polo Towers Pvt Ltd	B	50,000	302.6
3-Feb	Ravinay Trad	Harshvardhan Singhania	S	25,000	302.7
3-Feb	Ravinay Trad	Nile Enterprises Pvt Ltd	S	25,500	301.0
3-Feb	Sampada Chem	Vrajlal H Karani HUF	B	27,500	9.6
3-Feb	Sampada Chem	Pavak Securities Pvt Ltd	S	25,345	9.6
3-Feb	Vikas Wsp	Mukesh Kumar Shah	B	779,812	33.5
3-Feb	VST Tillers-$	Novastar Fund Advisors Pvt Ltd	B	52,200	439.0
3-Feb	VST Tillers-$	Novastar International Fund	S	57,800	439.0

Source: BSE

Gainers & Losers

Nifty Gainers & Losers

	Price (Rs)	chg (%)	Index points	Volume (mn)
Gainers				
ICICI Bank	916	1.6	5.3	4.9
Reliance Ind	838	1.1	5.0	4.6
HDFC Bank	506	1.7	4.9	3.7
Losers				
Hindalco	153	(3.4)	(2.3)	10.4
Jindal Steel	556	(2.9)	(2.1)	1.8
Tata Steel	468	(1.8)	(1.8)	5.9

Source: Bloomberg

Fundamental Research Team

Dipen Shah
IT, Media
dipen.shah@kotak.com
+91 22 6621 6301

Saurabh Agrawal
Metals, Mining
agrawal.saurabh@kotak.com
+91 22 6621 6309

Ruchir Khare
Capital Goods, Engineering
ruchir.khare@kotak.com
+91 22 6621 6448

Amit Agarwal
Logistics, Transportation
agarwal.amit@kotak.com
+91 22 6621 6222

Sanjeev Zarbade
Capital Goods, Engineering
sanjeev.zarbade@kotak.com
+91 22 6621 6305

Saday Sinha
Banking, NBFC, Economy
saday.sinha@kotak.com
+91 22 6621 6312

Ritwik Rai
FMCG, Media
ritwik.rai@kotak.com
+91 22 6621 6310

Jayesh Kumar
Economy
kumar.jayesh@kotak.com
+91 22 6652 9172

Teena Virmani
Construction, Cement, Mid Cap
teena.virmani@kotak.com
+91 22 6621 6302

Arun Agarwal
Automobiles
arun.agarwal@kotak.com
+91 22 6621 6143

Sumit Pokharna
Oil and Gas
sumit.pokharna@kotak.com
+91 22 6621 6313

K. Kathirvelu
Production
k.kathirvelu@kotak.com
+91 22 6621 6311

Technical Research Team

Shrikant Chouhan
shrikant.chouhan@kotak.com
+91 22 6621 6360

Amol Athawale
amol.athawale@kotak.com
+91 20 6620 3350

Premshankar Ladha
premshankar.ladha@kotak.com
+91 22 6621 6261

Derivatives Research Team

Sahaj Agrawal
sahaj.agrawal@kotak.com
+91 22 6621 6343

Rahul Sharma
sharma.rahul@kotak.com
+91 22 6621 6198

Malay Gandhi
malay.gandhi@kotak.com
+91 22 6621 6350

Prashanth Lalu
prashanth.lalu@kotak.com
+91 22 6621 6110

Registered Office: Kotak Securities Limited, Bakhtawar, 1st floor, 229 Nariman Point, Mumbai 400021 India.