Market outlook

Domestic markets, following the trend of global markets, fell sharply amid weak Chinese manufacturing data and a surprise devaluation of its currency, which rattled the global economy and risk assets, in general. Indian markets were no exception. However, at the same time, this has created opportunities, which in our view, provide an attractive entry point for investors from a two to three year horizon. Hence, we recommend investing into quality large cap and midcap names that have reasonable growth visibility coupled with strong balance sheets. Currently the global markets are volatile. Therefore, we advise investors to buy in a staggered manner.

Given a sectoral perspective, we are positive on auto, cement and capital goods (cyclical recovery in earnings aided by lower input costs and declining interest rates will provide strong operating and financial leverage). We have a positive to neutral rating on IT, pharma and consumers (rich valuations amid moderation in earnings but supporting depreciating currency) while we are negative on metals, oil & gas and real estate.

Company	Recommended Price Range	Market Cap	P/E (x)		P/BV (x)		ROE (%)	
	(₹)	(₹ crore)	FY16E	FY17E	FY16E	FY17E	FY16E	FY17E
Ajanta Pharmaceuticals	1370-1400	12586.0	31.2	25.1	10.8	8.1	34.8	32.1
United Spirits Limited	3150-3200	46762.0	151.9	84.6	49.9	33.6	32.9	39.8
Idea Cellular	148-154	54429.9	15.0	19.7	2.3	2.1	15.6	10.7
Kansai Nerolac	220-230	12327.8	17.2	28.1	5.6	4.8	49.1	17.1
Larsen and Toubro	1570-1630	151269.0	32.1	27.1	4.3	3.9	13.4	14.4
NBCC	880-920	10983.6	40.1	24.8	5.4	4.7	13.4	18.7
Maruti Suzuki	4100-4200	126857.0	23.3	19.0	4.5	3.8	19.4	20.1
Mahindra CIE	245-255	8281.0	29.1	19.5	3.5	3.3	12.3	16.9
Infosys	1060-1080	249563.0	19.5	17.1	4.2	3.7	21.3	21.7
MindTree	1240-1280	10720.0	17.8	14.6	4.4	3.7	24.9	25.3

Market Pandemonium – Stick to Quality

Ajanta Pharmaceuticals (AJAPHA)

- With focus on niche therapies in domestic formulations and a calculated approach in exports market, APL remains an interesting candidate from the midcap pharma space with high growth rates, strong margins, commendable return ratios and lighter balance sheet. Defying the normal trend of targeting developed markets for generic generics initially, the company focused on branded generics in the semi-regulated markets. At this juncture, the company is well poised to foray in the US market Ajanta has filed 25 ANDAs with USFDA and received five product approvals
- In the domestic market (32.7% of total revenue), Ajanta's main distinguishing factor compared to its peers is the uncanny knack of launching maximum number of first time launches with focus on new drug delivery system (NDDS). Of the 188 actively marketed brands, 129 brands were first in India
- It is currently deriving almost its entire export revenues (65% of total revenue) from emerging regions like Africa (Franco Africa), Asia and LatAm having a presence in more than 35 countries. As opposed to the common practice of forging alliances with regional pharmaceutical players, APL's front-end marketing team interacts directly with doctors. The company has consistently introduced new products in these markets
- We expect revenues to grow at a CAGR of 20.4% to ₹ 2584.4 crore in FY15-18E, on the back of strong growth in both exports and domestic formulation segments

Key Financials		FY15	FY16E	FY17E
Net sales	₹ crore	1,480.6	1,725.0	2,119.8
Growth	%	22.5	16.5	22.9
EBITDA margins	%	34.1	35.1	35.0
PAT	₹ crore	309.9	405.7	504.4
PAT growth	%	32.5	30.9	24.3
P/E	x	40.1	30.6	24.6
P/BV	x	14.8	10.7	7.9
RoE	%	37.8	34.8	32.1
RoCE	%	50.3	46.9	42.8

United Spirits Limited (MCDOWE)

- United Spirits (USL) is a pioneer in the Indian alcohol industry with ~40% market share in the IMFL segment. USL is perfectly poised to benefit from a change in management control and the resultant shift in focus from volume to value growth. With the world's major spirit company Diageo at the helm, we expect an orbital shift in USL's profitability due to infusion of funds, thereby enabling it to reduce its debt and undergo premiumisation of its brand and product portfolio
- India's per capita consumption continues to remain low at ~2 litre per annum. With a population of ~ 485 million in the drinking age and another 150 million likely to be added to the target population in the next four or five years, the demography greatly favours the dynamics of the industry. Any increase in per capita consumption is expected to alter the industry growth significantly on account of the large population base
- In a bid to clean up and strengthen the balance sheet of USL, Diageo has resorted to write-off & impairment of certain loans & advances and to exit non-core investments. Further, with a slew of management changes in the top brass, Diageo intends to have a tighter grip on the company
- In Q1FY16, Diageo sold its international brands directly, which added ₹ 42 crore in net sales of USL. This bodes well for USL as keeping sales and distribution cost under check, the company was able to push some of the iconic premium brands of Diageo that would be more earnings accretive

Key Financials		FY15	FY16E	FY17E
Net sales	₹ crore	9,335.0	10,253.7	12,311.1
Growth	%	-12.1	9.8	20.1
EBITDA margins	%	8.4	10.6	11.3
PAT	₹ crore	-1,687.3	305.4	548.6
PAT growth	%	NA	LP	79.6
P/E	x	NA	164.4	91.5
P/BV	x	76.7	54.0	36.4
RoE	%	NA	32.9	39.8
RoCE	%	9.7	12.5	15.6

Market Pandemonium – Stick to Quality

Idea Cellular (IDECEL)

- Idea has been witnessing robust voice volume in the past two quarters and has continued the trend with 5.8%QoQ voice volume growth to 195.6 billion minutes in Q1FY16. Robustness in voice minutes provides some respite to the cannibalisation fears towards VoIP. Going ahead, we have factored in voice volume growth of 12.6% CAGR in FY15-17E to 867 billion minutes. Voice revenues are expected to grow at 8.3% CAGR in FY15-17E to ₹ 28626.1 crore
- Data revenues have grown 3.7x from FY13 to ₹ 4553.0 crore in FY15 growing from 5.6% to 14.6% of total revenues over the same period. Though the data realisation per MB is seeing a declining trend, we expect data volumes to be stellar at 51.5% CAGR in FY15-17E to 396.0 billion MB. As a result, data revenues are expected to grow at 38.6% CAGR in FY15-17E to ₹ 8743.8 crore, forming 21.6% of mobility revenues
- Idea has also initiated multiple steps towards introduction of 4G LTE services on 1800 MHz band in 10 service areas in a phased manner from 2016 onwards. It will also evaluate a range of digital services and apps in areas including entertainment, communications, etc. to complement its 4G entry. It has, thus, revised its capex guidance to ₹ 6000-6500 crore from ₹ 5000-5500 crore in light of the 4G roll-out. . We expect revenue and EBITDA to post 13.9% and 20.8% CAGR (FY15-17E)

Key Financials		FY15	FY16E	FY17E
Net sales	₹ crore	31,570.9	36,557.2	40,933.4
Growth	%	19.1	15.8	12.0
EBITDA margins	%	34.2	37.3	38.6
PAT	₹ crore	3,192.9	3,625.4	2,757.8
PAT growth	%	62.3	13.5	-23.9
P/E	x	20.2	17.8	23.3
P/BV	x	2.8	2.8	2.5
RoE	%	13.9	15.6	10.7
RoIC	%	13.9	10.9	10.5

Kansai Nerolac (GOONER)

- Kansai Nerolac (KNL) is India's largest industrial paint company with ~35% market share in industrial paints and third largest player with overall 14% market share. With sustainable growth in decorative paints and subdued industrial demand, KNL has increased its revenue contribution in decorative paints from 50% in FY09 to 55% in FY15. The company continues to invest in brands with 4-5% of sales going into advertisement and promotion
- We believe decorative paints would continue to grow strongly with the presence of limited players and strong repainting demand. We expect a revival in industrial paints demand (75% automotive paints), led by a recovery in the automotive segment
- With a leadership position in industrial paints given ~35% market share, KNL has a strong client base of auto OEMs. They account for 30-35% of its sales with Maruti Suzuki being its largest client. Automobile demand was subdued as Maruti has seen mere 1% volume CAGR in FY12-14. However, with a revival in automotive demand (Maruti's domestic passenger car volumes rose 11% in FY15), industrial paints also saw a sharp recovery in FY15. Further, with an improvement in automotive paint demand, we expect industrial and decorative volume growth of 13% and 11% YoY, respectively, in FY17E

Key Financials		FY15	FY16E	FY17E
Net Sales	₹ crore	3,532.4	3,854.2	4,432.6
Growth	%	12.6	9.1	15.0
EBITDA Margin (%)	%	12.6	15.1	16.0
PAT	₹ crore	271.7	754.0	459.9
Growth	%	31.5	177.5	-39.0
P/E	x	47.6	17.2	28.1
P/BV	x	8.1	5.6	4.8
RoE	%	17.0	49.1	17.1
RoCE	%	23.3	23.1	24.1

Market Pandemonium – Stick to Quality

Larsen and Toubro (LARTOU)

•L&T is the most diversified engineering & infrastructure developer in India with a presence across all segments of infrastructure i.e. power, roads, hydrocarbons & process industries. It is also planning to scale up in niche areas like defence, nuclear power & shipbuilding that have the potential to add significantly to overall revenues in the next three to five years (for instance, opening of defence FDI and ordering can help L&T achieve scale of 5x in terms of defence segment revenues from current ₹ 1000 crore)

•Over the last couple of years, L&T has added capacity to meet increasing volumes. For instance, the company had added 5000 MW of power equipment facility, the heavy engineering facility in Oman (FY10) and recently added complex shipbuilding facility. Hence, we expect L&T to register a revenue CAGR of 17.7% in FY15-17E as it commands a strong order backlog of ₹ 239000 crore providing visibility of two to three years

•Though Q1FY16 was a miss on all counts for L&T, the strong order backlog, macroeconomic environment and pick-up in domestic ordering will provide enough room to L&T to cover the lost ground, going ahead. Even with 10% order inflow growth and muted execution rate, L&T is well poised to exhibit strong 17.8% and 12.6% CAGR in revenue and PAT over FY15-17E. Also, listing of the technology subsidiary in early FY17E can lead to medium-term re-rating for the stock. We believe L&T is the best way to play the capex cycle in India.

Key Financials		FY15	FY16E	FY17E
Net Sales	₹ crore	57,017.4	65,195.3	78,989.0
Growth	%	0.7	14.3	21.2
EBITDA margin	%	11.4	11.3	11.2
PAT	₹ crore	4,746.8	5,076.6	6,014.1
PAT growth	%	-1.4	6.9	18.5
P/E	x	34.3	32.1	27.1
P/BV	x	4.7	4.3	3.9
RoNW	%	13.6	13.4	14.4
RoCE	%	16.7	16.4	17.5

National Buildings Construction Corporation (NBCC)

- National Building Construction Corporation (NBCC) is one of the largest public sector enterprises (PSEs) in the construction industry. We believe its PMC division (~85% of FY15 revenues) is an economic moat for NBCC in which it gets orders largely on a nomination basis, enjoys negative WC & cash rich balance sheet along with a strong order book
- Furthermore, NBCC's order book stands at ₹ 27000.0 crore as on June 30, 2015, 5.5x TTM revenues providing strong revenue visibility over the next couple of years
- Going forward, the management has guided that order inflows will increase substantially primarily due to opportunities arising from redevelopment of old colonies in New Delhi and government's Smart City mission. Therefore, we expect order acquisition and execution to remain healthy. Hence, we have built in 86% CAGR growth in the order book during FY15-17E
- With respect to smart city mission of Government of India, the company has entered into MoU with IBM and a Malaysian JV firm to provide for complete solution including both construction and Technical (IT/Electronic) solutions for smart cities
- We expect NBCC's revenues to grow at CAGR of over 44.0% in FY15-17E thereby leading PAT to grow at a CAGR of 41.5% during same period

Key Financials		FY15	FY16E	FY17E
Net sales	₹ crore	4,621.0	5,748.2	9,661.6
Growth	%	15.3	24.4	68.1
EBITDA margins	%	6.2	6.8	7.7
PAT	₹ crore	277.3	343.3	555.0
PAT growth	%	12.2	23.8	61.7
P/E	x	49.7	40.1	24.8
P/BV	x	10.4	5.4	4.7
RoE	%	21.0	13.4	18.7
RoCE	%	21.6	15.2	25.1

Market Pandemonium – Stick to Quality

Maruti Suzuki (MARUTI)

- Maruti Suzuki India (MSIL) is the market leader with ~47% share in the Indian passenger vehicle industry. A recovery in the overall economy would have a multiplier effect on the passenger vehicle up cycle, which would benefit MSIL. It has vast distribution network of ~1200 dealership and ~3000 workshops across India. In the next five years, we expect penetration levels to increase from levels of ~15 cars per 1000 and march towards peer penetration levels (China: ~60/1000, Brazil: ~200/1000).
- With demand expected to revive in addition with higher discretionary spending coupled new launches is likely to drive MSIL's volumes going forward. The Launch of "S-Cross" recently and compact SUV, going forward, would help MSIL create presence in the SUV segment. Diesel variant of Celerio & AMT based Swift model would help improve market share. Hence, a strong product pipeline of new launches and facelifts of some of its existing models coupled with further enhancement of distribution network & production capacity will help MSIL to maintain its leadership position in passenger vehicle even as competition intensifies.
- New launches, higher contribution from the premium segment, reduction in discount levels and localisation efforts and JPY depreciation is likely to aid margins for MSIL. We continue to remain bullish on longer-term growth prospects of the car segment, especially MSIL and expect volume to grow ~13% CAGR over FY15-17E, outpacing the industry

Key Financials		FY15	FY16E	FY17E
Net sales	₹ crore	49,874.0	57,350.0	67,649.0
Growth	%	14.0	15.0	18.0
EBITDA margins	%	13.2	16.0	16.0
PAT	₹ crore	3,711.0	5,433.0	6,670.0
PAT growth	%	33.0	46.0	23.0
P/E	x	34.1	23.3	19.0
P/BV	x	5.3	4.5	3.8
RoE	%	15.6	19.4	20.1
RoCE	%	17.2	23.3	23.6

Mahindra CIE Automotive (MAHAUT)

- Mahindra CIE Ltd (MCI) is a strong Tier 1.5 (critical component) supplier to global OEM. We believe MCI provides a rare, unique Indian auto component play, which has a global footprint with global promoters along with massive turnaround possibilities in the company. MCI has a presence across both commercial vehicles (MFE) and passenger vehicles (CIE Forging Europe) with complementary strengths of dual parents
- Post the Mahindra-CIE merger, MCI had first targeted Mahindra Forging Europe (MFE) for its potential turnaround candidate. MFE's margins have gradually improved from ~3% in Q1FY14 to >9% in Q1FY16, reflecting management focus on a turnaround. According to the management, MFE's turnaround is progressing steadily and the 'Phase 1' action (internal efficiency) has been completed while 'Phase 2' actions on optimising products and product lines have begun. A turnaround in the Metalcastello business has improved after MCI had taken restructuring actions last year
- The consolidated debt stands at ~₹ 1400 crore; and with no major capex and free cash flow generation (mainly after various business turning profitable), the debt level is likely to come down. We expect utilisation levels to improve, leading to EBIT margins of ~8% and RoCE expansion to ~15% in FY17E. The management's turnaround strategy continues to be in place with focus on improving its profitability despite sluggish sales growth. Hence. we maintain our positive stance on the stock

Key Financials		FY15	FY16E	FY17E
Net sales	₹ crore	5,569.9	5,875.5	6,441.2
Growth	%	-1.9	5.5	9.6
EBITDA margins	%	7.9	12.3	13.8
PAT	₹ crore	-78.1	285.6	424.2
PAT growth	%	NA	NA	48.5
P/E	x	NA	29.1	19.5
P/BV	x	4.3	3.5	3.3
RoE	%	-4.1	12.3	16.9
RoCE	%	5.9	11.5	15.9

Market Pandemonium – Stick to Quality

Infosys (INFTEC)

- Infosys expects to achieve revenue of $20 billion by FY20. This includes $1.5 billion contribution from acquisition and ~10% or $2 billion from new technologies such as design thinking, artificial intelligence and platform based offerings. This translates to 13.6% CAGR for existing business (FY15-20E). Infosys aims to achieve 30% margins by 2020 aided by employee productivity improvement ($80k vs. $52.3 in FY15). Employee productivity improvement could be driven by initiatives in 1) new technology and 2) automation in commoditised business. Infosys also expects to return to industry leading growth and margins by FY17E.
- After a disappointing Q4, Infosys' reported an excellent quarter as dollar revenues grew 4.5% QoQ. Growth was led by volumes, 5.4% QoQ growth (highest in 19 quarters) and 14.2% YoY (highest in 17 quarters) while realisations declined 70 bps. Volume growth was led by large deal wins and top clients focus. Infosys raised its FY16E $ revenue growth guidance even as it maintained its 10-12% constant currency growth guidance led by healthy deal wins, improved win rates, better execution and top accounts mining
- We estimate Infosys will report revenue, PAT CAGR of 13%, 10%, respectively, over FY15-17E (with average 25.3% EBIT margins in FY16-17E). Recovery to industry average growth and margins could lead to re-rating. Rupee depreciation could aid profitability in FY16E.

Key Financials		FY15E	FY16E	FY17E
Net sales	₹ crore	53,319	60,008	67,501
Growth	%	6.4	12.5	12.5
EBIT margins	%	25.9	25.0	25.5
PAT	₹ crore	12,329	13,022	14,858
PAT growth	%	15.8	5.6	14.1
P/E	x	20.6	19.5	17.1
P/BV	x	4.6	4.2	3.7
RoE	%	22.5	21.3	21.7
RoCE	%	31.4	29.7	30.1

MindTree (MINCON)

- MTL has aligned its strategy to capture the changing industry dynamics under its six pillars, 1) digital transformation, which industry studies suggest $225 billion spending by 2020 and 50-80% of the incremental spends, 2) expertise led selling and to emerge as multi-segment specialists, 3) focused acquisitions to fill white spaces (Discoverture aided MTL's thrust to become top 3 service providers for P&C insurers), 4) value driven delivery model led by lean, agile development and automation that could advance client's time-to-market, 5) differentiated culture, and 6) increased global footprint led by higher investments in local geographies. Management reiterated its sharp focus on delivering industry leading growth that could fulfil its $1 billion revenue target by 2020 (assuming a modest 11% CAGR over FY15-20) and market cap in excess of $5 billion.
- MindTree reported healthy growth in Q1FY16 as dollar revenues grew 4.8% QoQ (6.4% volumes, 1.5% realisation dip) while organic dollar revenues (excluding Discoverture contribution of $3.75 million in Q1 and $2.7 million in Q4) grew 4.2% QoQ. This represents significant acceleration compared to 0.1%, 0.5% reported in Q4 and Q3FY15, respectively.
- We estimate MTL will report revenue, earnings CAGR of 20%, 17% in FY15-17E (average 18.8% EBITDA margins in FY16-17E). Rupee depreciation could aid profitability in FY16E.

Key Financials		FY15E	FY16E	FY17E
Net sales	₹ crore	3,561.9	4,445.3	5,143.8
Growth	%	17.5	24.8	15.7
EBITDA margins	%	19.9	18.5	19.0
PAT	₹ crore	536.3	600.0	730.6
PAT growth	%	18.9	11.9	21.8
P/E	x	19.9	17.8	14.6
P/BV	x	5.3	4.4	3.7
RoE	%	26.6	24.9	25.3
RoCE	%	33.7	31.7	32.2

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