

DIWALI DHAMAKA

TOP PICKS FOR DIWALI, SAMVAT 2073

Stock Name	CMP	Target	Upside (%)
HDFC Bank	1270	1500	18
LIC Housing Finance	600	748	24
Shriram City Union Finance	2300	3000	30
Bharat Electronics Ltd.	1264	1450	15
Amara Raja Batteries	1025	1257	22

*Prices as on Friday (21st October 2016) closing



NIFTY : 8693

SENSEX : 28077



*Wish you all a
Happy Diwali
and a
Prosperous New
Year!!*

Samvat 2072 had its share of volatility for Indian equities where initial few months were marked by sharp selling while post Budget Bulls took charge driving market all the way to within touching distance of all time high. Indian equities seem to be on a cusp of new growth trajectory enabled by several policy measures being taken and implemented be it coal block allocation, spectrum auction for telecoms, deregulation of petrol and diesel prices, gas price reform, FDI in Insurance & Defense sectors, Reduction in Repo rate, 7th Pay Commission Roll out, Passage of GST Bill among few others. Monsoons have been near normal which is likely to boost agriculture dependent rural income. Better operating efficiencies, higher capacity utilization, slow pick up in pricing power as demand improves aided by higher disposable income will translate to higher ROE's of corporate India. Domestic cyclical have turned from being earnings dragger to earnings driver while global cyclical growth momentum is maintained. Based on aforementioned factors fructifying, we expect earnings growth to pick up momentum from 2QFY17 onwards. Though the market stands at a gain of over 25% from CY16 lows, yet the valuations are around 10 Year average on 12-month forward earnings multiple. The Sensex trades at 16.8x one year forward earnings, at its long-period average of 16.9x. Sensex P/B is at 2.6x, near its 10-year average of 2.7x. Market-cap-to-GDP ratio of 75% (FY17E GDP) is below the long-period average of 78%. Valuations look attractive as we expect Sensex EPS to grow at 17% CAGR over FY16-18 as compared to 6% CAGR witnessed during FY08-16.

Triggers:

- Good Monsoon • Lower inflation • 7th Pay Commission rolls out
- GST bill passage • Lower interest rates

Concerns:

- Continuous slowdown of the global economy
- US rate hikes may make USD stronger and hence FII's may pull out of emerging markets
- Geopolitical concerns particularly between India & Pakistan

Strong pick-up in earnings and return to double digit growth in revenue is crucial for markets to move up on a sustainable basis. We remain bullish on markets and advocate sticking to our QGLP philosophy for deploying money into quality stocks. Following are the list of our preferred picks for Samvat 2073.

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Vice President- Head Retail Research

HDFC Bank

Banking

CMP	1270	<ul style="list-style-type: none"> HDFC Bank is promoted by the biggest mortgage lender in the country, HDFC Limited (21.6% stake). The bank is now the second largest private sector bank in India with asset size of INR6t+ and market share of ~5% in deposit and loans respectively. The bank has a network of 4,500+ branches. Structural drivers in place with (1) CASA ratio of ~40%, (2) growth outlook of at least 1.3x the industry growth, (3) improving operating efficiency led by digitalization initiatives, (4) expected traction in income due to strong expansion in branch network, and (5) best-in-class asset quality. Best in class on all parameters - earnings CAGR of 20%, with core income growth pick-up led by healthy loan growth, superior ROEs, gradual improvement in fee income and operating efficiencies. Over the last 12 years, HDFCB's market share has increased significantly in (1) retail loans, (2) low-cost deposits and (3) profitability, indicating the strength of its franchisee. Strong fundamentals and near-nil stress loans would enable the bank to gain market share. Further, continued strong investment in people and branches indicating management positive outlook on business. RoEs are expected to be the best amongst private banks at ~20%.
Target	1450	
Mkt. Cap.(Cr.)	3,23,295	
52 Weeks High	1318	
52 Weeks Low	928	

LIC Housing Finance

NBFC

CMP	600	<ul style="list-style-type: none"> LIC Housing Finance (LICHF) is the second largest housing finance company with 10% mortgage market share in India. LICHF is promoted by government owned largest insurance company the LIC of India. LICHF provides individual housing loans, loan against property and loans to developers as project finance. LICHF has a granular loan book with retail home loans comprising 88 % of the book and the LAP comprising an additional 10% of the book. Around two-thirds of loan sourcing is from LIC agents. We believe LICHF will be the biggest beneficiary of falling GSec yields as more than 80% of borrowings come from capital markets. Since the RBI started open market operations 10 months back, GSec yields have declined more than 100bp from 7.8% to 6.7%. LICHF has over 20% of outstanding borrowings maturing in FY17 and FY18, and thus will reap significant benefits from refinancing over next few quarters. We believe LICHF should sustain 2%+ incremental spreads in coming years, which would boost its earnings and RoE. We estimate 22% EPS CAGR over FY16-19 with consistent RoEs of ~20% which should drive re-rating.
Target	748	
Mkt. Cap.(Cr.)	30,280	
52 Weeks High	624	
52 Weeks Low	329	

Shriram City Union Finance

NBFC

CMP	2300	<ul style="list-style-type: none"> • SCUF, part of the Shriram Group, has successfully evolved as a multiproduct lender over the past decade. Core focus of the company is towards small enterprise loans where it has market share of over 40% (Source: Frost & Sullivan). It has over 1000+ branches of which around 80% is in underpenetrated semi-urban India. • SCUF is tapping aggressively into the vast potential of those small enterprises (54% loan mix) who find it difficult to deal with scrupulous money lenders on one hand and highly organized banks on the other. It has successfully tried to bridge this gap. • The period FY13-15 was marked by rebalancing of loan book away from gold loans to more of small enterprise and two wheeler loans. We expect SCUF to deliver 21% CAGR in AUM over FY16-18E vs 7% CAGR during FY13-16. Its loan book is now well diversified comprising of small enterprise (54% mix), two wheelers (18% mix), other auto (6% mix), gold (17% mix) and personal loans (5% mix). • We believe that SCUF's deserves to trade at a premium over other asset financiers, owing to high structural loan growth, better earnings visibility, lower cyclicality and superior asset quality.
Target	3000	
Mkt. Cap.(Cr.)	15,164	
52 Weeks High	2,349	
52 Weeks Low	1,332	

Bharat Electronics Ltd.

Capital Goods

CMP	1264	<ul style="list-style-type: none"> • Bharat Electronics Limited (BHE) was established by the Government of India under the Ministry of Defence in 1954 to meet the specialized electronic needs of the Indian defence services. Over the years, it has grown into a multi-product, multi-technology, multi-unit company servicing the needs of customers in diverse fields in India and abroad. • BHE is well positioned to benefit from the rising defense expenditure supported by a) strong manufacturing base (Capacity utilization of ~60%) and execution track record, b) relationship with defense and government agencies, c) strategic collaboration with foreign technology partners for new products development d) in-house R&D capabilities (R&D spend at 8.2% of revenues) and e) Increased focus on exports to friendly countries. • BHE enjoys a robust order book - to - sales position of over 4.6x. Key orders like Akash missile system weapon locating radar, tactical communication system, mobile cellular communication system, electronic warfare systems, advanced composite communication system and commander TI sights are likely to be finalized in coming months which would further strengthen the order book.
Target	1450	
Mkt. Cap.(Cr.)	30,336	
52 Weeks High	1417	
52 Weeks Low	1008	

Amara Raja Batteries

AUTO-ANCILLIARY

CMP	1025	<ul style="list-style-type: none"> • AMRJ is India's second-largest lead-acid battery manufacturer (next to market leader EXID), with market leadership in telecom and UPS segments. It is reckoned as one of the pioneers in VRLA (valve regulated lead acid) batteries. Johnson Control USA (JC) is an equal partner and acquired 26% equity in AMRJ in 1997 • Company aims to increase its share in the OEM and replacement segments to 40% (from current 30%) and 30% (from current 24%) respectively over the medium term. In the telecom segment, AMRJ expects to maintain its market share at current levels (60% currently). • FY16 was an inflection year for AMRJ-with new capacities driving top-line (expectation of ~19% CAGR over FY16-18E) and benign lead prices to drive margins growth (+30bp by FY18), translating into ~20% EPS CAGR (FY16-18E). • Stable competitive environment, significant FCF generation (~INR2.6b over FY16-18) and stable RoE of 25% -coupled with potential shift from unorganized to organized players when GST rolls out is to sustain high growth trajectory.
Target	1257	
Mkt. Cap.(Cr.)	17,508	
52 Weeks High	1080	
52 Weeks Low	778	

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