investor's eye

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Telecommunications

Sector Update

End of 3G roaming pact among the players- Raises question on 3G revenue model

The event

- The Department of Telecom (DoT) has asked the telecom operators to terminate the 3G intra circle roaming arrangements entered amongst them, with immediate effect. The show cause notices in this respect would be issued to the players today or latest by Friday morning.
- The DoT has taken such a decision acting on the ground that such arrangements entered between the players result in spectrum sharing which is illegal and not permissible.
- Further the telecom ministry is also contemplating imposing penalty on the players for entering into such an arrangement, though the final decision on penalty imposition is yet not taken.

The background

- In the auction for 3G license and spectrum held in 2010, owing to the fierce pricing and strong competition, none of the players could bag a pan India 3G license. Thus in order to provide a seamless and pan-India 3G coverage to the subscribers, operators had entered into a 3G intra circle roaming pact. Following the pact, players used other players' licenses and networks to provide 3G services in circles where they themselves did not have a 3G license.
- In July 2011, Bharti Airtel, Idea Cellular and Vodafone signed a pact amongst themselves to provide 3G services, which allowed customers to avail 3G services in areas where at least one of the three companies had bandwidth.
- Tata Teleservices and Aircel had also entered into similar arrangements but relinquished the same earlier this month.

Impact

- We believe that if the 3G roaming pact/ arrangements are not permissible, as stated by the government, then it would be sentimentally negative and would also have a potential revenue impact. Further the entire 3G model would come under question with players having to work their business economics again in the light of changed policy environment.
- Bharti Airtel has paid Rs12,295 crore for bagging 13 licenses that cover 70% of its 2G services revenue, while Vodafone and Idea Cellular have paid Rs11,618 crore and Rs5,769 crore each for bagging licenses in 9 and 11 circles respectively. For Vodafone and Idea Cellular, the bagged license covers 65% and 80% of the revenue respectively.
- The per share investment incurred by Bharti Airtel and Idea Cellular stands at Rs32 and Rs17, forming 10% and 21% respectively of their market capitalisation.
- Further if a penalty is imposed on the players then it would further create a strain on the cash flow and the earnings.

View

The Indian telecom industry is suffering from a lot of negative regulatory developments and news flow (levy of one-time spectrum charges, higher uniform licence fee of 8% and bringing tower companies under the licence net) which have been in public domain for long and been discounted by the market. The result has been a strong underperformance of the telecom stocks (Bharti Airtel [-10%], Idea Cellular [-14%] and Reliance Communications [-12.8%]) over the last three months. Further now, with 3G roaming arrangements being declared illegal and void, there will be a sentimental as well as potential revenue impact. Thus we continue to keep a watch on the regulatory development and maintain a cautious stance on the sector.

Player wise bid to 3G license Rs (cr)

Circles	Final 3G bid price	Total Revenue	Bharti	Vodafone	Rcom	Aircel	Tata	Idea
Number of slots won			**13**	**9**	**13**	**13**	**9**	**11**
All India Price/ Price paid by operators	**16,751**		**12,295**	**11,618**	**8,585**	**6,499**	**5,864**	**5,769**
Gross Government revenue collection	**67,719**							
Revenue Coverage (%)			**70.0**	**62.0**	**55.0**	**95.0**	**47.0**	**80.0**
Metros		**28433.04**						
Kolkata	544	2,177		544	544	544		
Delhi	3,317	13,268	3,317	3,317	3,317			
Mumbai	3,247	12,988	3,247	3,247	3,247			
Category 'A'		**27007.48**						
AP	1,373	5,493	1,373			1,373		1,373
Gujarat	1,076	4,304		1,076			1,076	1,076
Karnataka	1,580	6,320	1,580			1,580	1,580	
Maharashtra	1,258	5,031		1,258			1,258	1,258
TN (incl. Chn)	1,465	5,860	1,465	1,465		1,465		
Category 'B'		**10200.44**						
Haryana	223	890		223			223	223
Kerala	312	1,250				312	312	312
MP	258	1,033			258		258	258
Punjab	322	1,610			322	322	322	322
Rajasthan	321	1,284	321		321		321	
UP (E)	365	1,458		365		365		365
UP (W)	514	2,056	514				514	514
West Bengal	124	618	124	124	124	124		
Category 'C'		**2077.99**						
Assam	41	166	41		41	41		
Bihar	203	1,017	203		203	203		
HP	37	186	37		37			37
North East	42	169	42		42	42		
Orissa	97	388			97	97		
J&K	30	152	30		30	30		30

Gujarat State Fertiliser Corp

Viewpoint

In expansion mode

CMP: Rs351

Extensive expansion plans: Gujarat State Fertiliser Corporation (GSFC) has plans to expand its product portfolio across segments especially the chemical segment with a total investment of about Rs1,400 crore. The projects that shall contribute significantly to the total revenue include a methanol plant (at a cost of about Rs350 crore), a TIFERT unit (at a cost of about Rs1,200 crore) and a nylon 6 plant (at a cost of about Rs275 crore). These three proposed plants will contribute nearly Rs1,825 crore at full capacity utilisation. The methanol plant will be operational by Q4FY2012 whereas the TIFERT unit would start production by Q1FY2013 and the nylon–6 project will commence production in Q3FY2013.

Cash rich with almost no debts on books: The planned capital expenditure of about Rs1,400 crore for the debottlenecking and brownfield projects will be fully funded through internal accruals. This will help the company to remain debt-free and utilise the huge cash at its disposal for growing in future through investing in projects related to its core competence. The company's management has clarified that it will invest only in projects related to the company's product portfolio and will not diversify in non-core areas. At the end of the Q3FY2012 GSFC has cash balance of Rs850 crore, which is enough to fund its future projects.

Softening of caprolectam spreads to restrict growth in earnings: The spread between the prices of caprolactam and benzene reduced to $1,700 per tonne in November 2011 after touching a peak of $2,700 per tonne. The management believes that the spread could stabilise at around $1,500 level. Thus, the margin pressure in the chemical business is likely to restrict the overall earnings growth in the coming quarters as well as in the next fiscal.

Input cost pressure in the fertiliser business: The sustained input cost pressure in the fertiliser business is also a matter of concern. GSFC may not be able to pass on the increase in the prices of the raw materials as one of the biggest players in the fertiliser industry has refused to increase the prices of non-urea fertilisers whose prices have increased by over 50-100% in the last one year. This can have a negative effect on the fertiliser margin as well as the overall margin of the company.

Outlook and stock view: Though we believe the company should be able to report a 9.0-9.5% compounded annual growth rate (CAGR) in its revenues over FY2011-13, its earnings could at best remain flat, if not decline, due to the margin pressure in both the fertiliser and the chemical business. On the positive side, its valuations are supportive and the company has a strong balance sheet with a huge cash of Rs850 crore (30% of its market capitalisation) at the end of Q3FY2012. Its return on equity was healthy at over 25% in FY2011. At the current market price the stock is trading 3.5x and 4.0x its FY2012E and FY2013E earnings respectively and has a dividend yield of 2%. We do not have a rating on the stock.

Valuations

Particular	2008-09	2009-10	2010-11	2011-12E	2012-13E
Revenue	5881	4019	4755	5414	5674
PBITA	836	422	1120	1225	1058
APAT	557	257	743	793	686
OPM %	13%	8%	21%	21%	16%
PAT margin %	9%	6%	16%	15%	12%
Adj. EPS	70	32	93	99	86
EV/EBITDA	3.66	8.06	2.28	1.96	1.67
P/E	4.98	10.80	3.73	3.50	4.04
RoCE (%)	35%	16%	35%	32%	24%
RoE (%)	30%	13%	27%	23%	17%
Dividend yield	1.5%	1.5%	2.0%	3.2%	3.4%

Key takeaways from the analyst meet

Future expansion plans

Upcoming projects by GSFC to be fully funded by internal accruals

a. A new methanol plant with a rated capacity of 1.73 lakh tonne to be set up at a cost of Rs301 crore. It is expected to get commissioned in Q4FY2012. The total turnover from this plant at 100% capacity utilisation is estimated at Rs347 crore.

b. The TIFERT is a partnership with a foreign entity to manufacture phosphoric acid in order to meet its raw material requirement. The total investment required for the project is $500 million of which GSFC's share is $120 million. The expected date of commissioning is Q1FY2013 and the total turnover expected from this plant is Rs1,244 crore.

c. A fifth windmill project with a total capacity of 50.4MW and a total capital expenditure of Rs281 crore has been planned. It is expected to get commissioned by H2FY2013. The total turnover from this project is estimated at Rs31 crore.

d. The nylon-6 project with a total capacity of 15,000 tonne will require a total capital expenditure of Rs125 crore. It is expected to get commissioned by Q3FY2013. The total turnover expected from this project is Rs285 crore.

e. GSFC is setting up a new ammonia plant at Vadodara in order to replace its old ammonia plant.

Other greenfield and brownfield expansion projects over next 3 to 5 years

a. The fourth line for DAP/NPK is being set up at Sikka with a total installed capacity of 4 lakh tonne and a total capital expenditure of Rs250 crore. The current status of project LSTK tenders is in process

b. The methyl-ethyl ketone project is being set up with a total investment of Rs120 crore. It will have an installed capacity of 24,000 tonne. The tenders for the project have been invited.

c. The phosphoric acid/SSP plant at Sikka is being set up with a total capital expenditure of Rs1,000 crore. The DFR studies for the project are under process.

d. The integrated fertiliser and petrochemical complex at Dahej will require a total capital of Rs7,000 crore. The DPR study, land allocation and tendering for the project is being done currently. The capacity of the chemical plants are given below:

i.	Urea	1.0 million tonne
ii.	Caprolectam	0.1 million tonne
iii.	Melamine	0.04 million tonne

Other takeaways

- GSFC consumes 2mmscmd of gas of which 45% is from APM fields and the remaining is from D6 KG field basin and imported LNG. The average cost of APM gas is Rs9.5SCM; the average price of D6 gas is Rs11SCM while the average cost of imported LNG is Rs21SCM.
- GSFC imports 0.2 million tonne of phosphoric acid from Tunisia and the remaining phosphoric acid is imported from OCP, GCT and Foskor on a long-term contract basis.
- The company sells near about 10,000 tonne of caprolectam in the international markets while the remaining is for captive use and for the domestic market. The biggest clients of caprolectam in India are SRF and Century Enka.
- GSFC sells melamine in both the domestic and international markets at International parity price.
- The company is hedging on the business cycle against the purchase of raw materials. If the prices of the raw materials increase it will pass on the price to the customer in order to maintain its margin. If the rupee depreciates GSFC will try to renegotiate the prices of raw materials to offset the effect of a stronger dollar on raw material cost.

Company profile: GSFC was set up in 1962 with the objective of helping farmers by offering them the best agriculture practices in Gujarat. Initially it was set up with an equity structure in which the state government had a 49% stake, and public and financial institutions had 51% stake. Today the state government's involvement has come down to 38.4%. Over the years, GSFC has gone for product diversification and value addition with a product mix of fertilisers, chemicals, industrial gases, plastics, fibres and other products. GSFC operates in two business segments: fertilisers and industrial products.

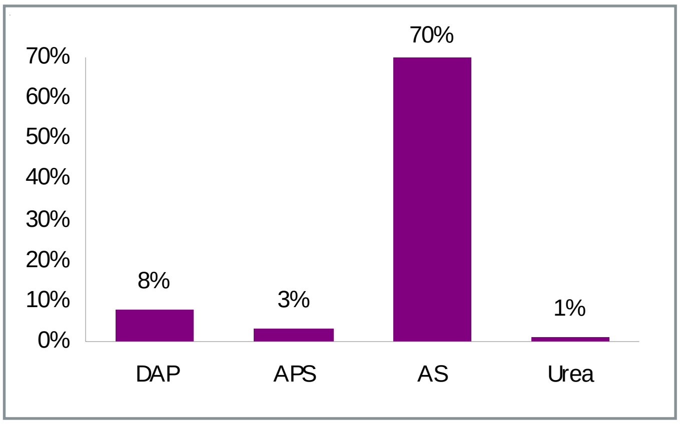
Business overview

GSFC has two business segments: fertilisers and industrial products, which contributed 69% and 31% respectively to its total revenues in FY2011. In the fertiliser segment di-ammonium phosphate contributed 49% of the total revenue in FY2011 while urea, ammonium sulphate and ASP contributed 5%, 5.8% and 9.2% respectively. In the industrial products, caprolactum contributed 15.4% to the total revenue while nylon-6 fibres and melamine contributed 3% and 2.3% respectively.

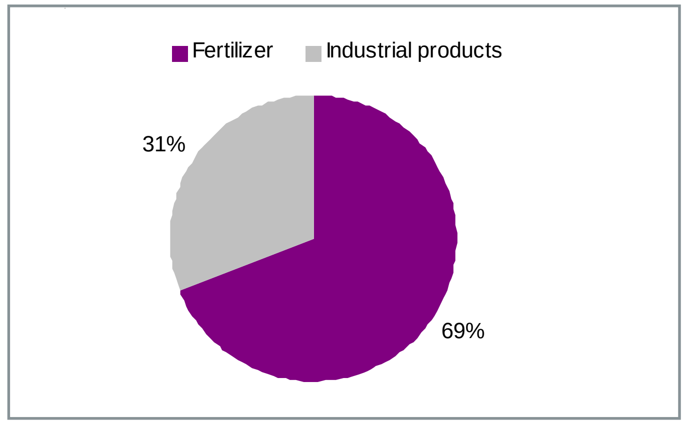
Manufacturing units	Location	Products
Fertilizernagar	Vadodara	Ammonia, urea, sulphuric acid, ammonium sulphate, phosphoric acid, caprolactum and melamine.
Nandesari	Vadodara	This unit was the result of the amalgamation of Polymer Corporation of Gujarat with GSFC. It produces a wide range of acrylic, monomers and polymers.
Sikka	Jamnagar	This plant is located 27km from Jamnagar near Sikka port. It is based on imported phosphoric acid and ammonia. It produces 7.22 lakh tonne of DAP.
Kosamba	Surat	The fibre unit at Kosamba would manufacture nylon yarn, nylon-6 chips and engineering plastic grade chips.

Market share in fertilizer and chemical business

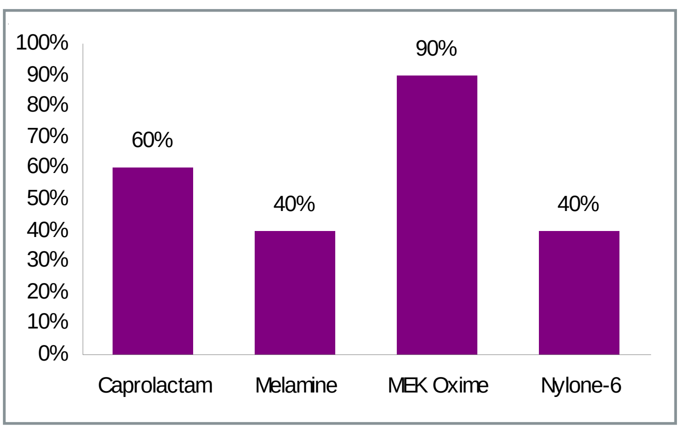
Market share of GSFC in fertilisers



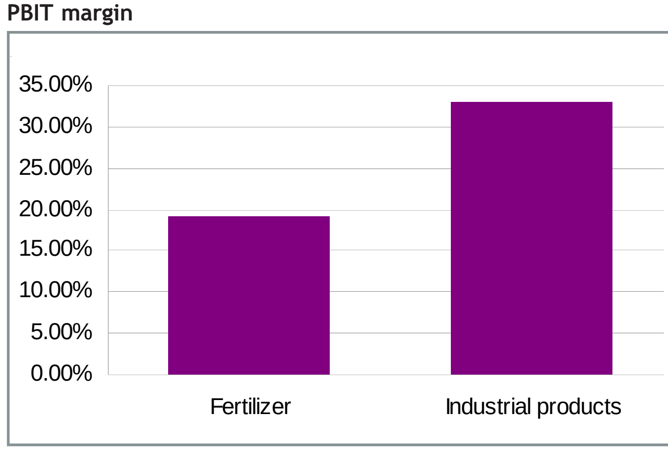
Segmental revenue break-up



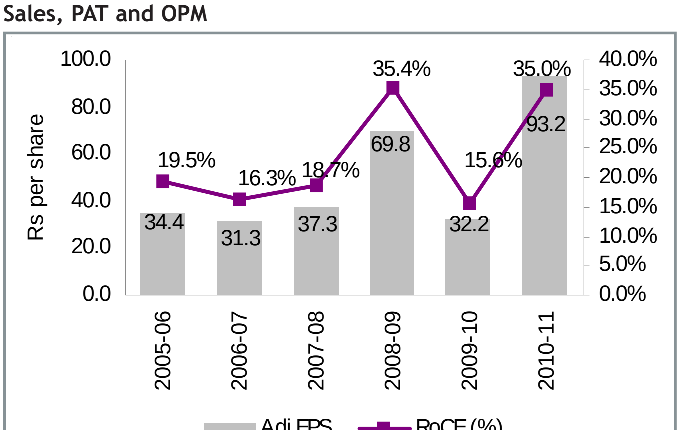
Market share of GSFC in chemicals



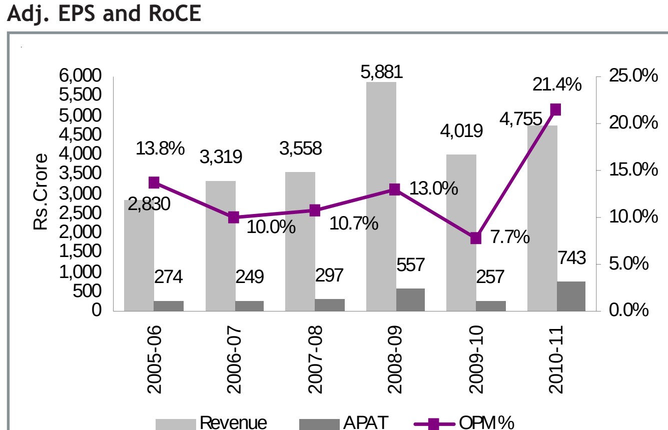
PBIT margin



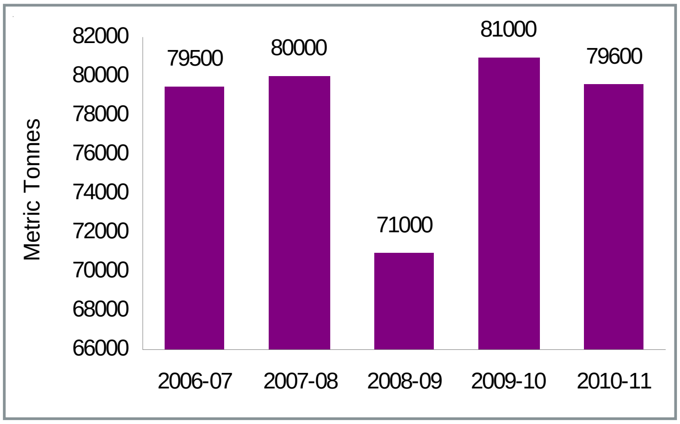
Sales, PAT and OPM



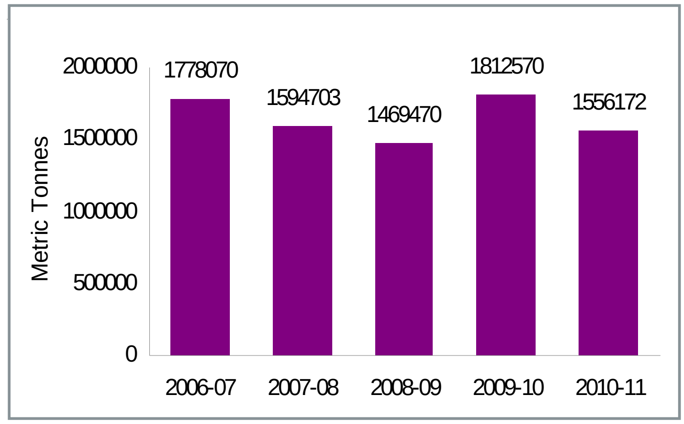
Adj. EPS and RoCE



Annualised production of chemicals



Annualised production of fertilisers



Sharekhan Limited, its analyst or dependant(s) of the analyst might be holding or having a postition in the companies mentioned in the article.

Mutual Gains

Mutual Fund

Sharekhan's top equity mutual fund picks

Top rated equity mutual funds

Data as on November 30, 2011

Scheme Name	Stars rating	NAV (Rs)	Returns (%) 6 mths	1 yr	3 yrs	5yrs	Since inception
Large-cap funds							
ICICI Prudential Focused Bluechip Equity Fund - Ret	★★★★★	15.2	-5.4	-12.0	**36.9**	18.8	19.5
Principal Large Cap Fund	★★★★	24.5	-13.3	-19.2	**30.0**	7.2	15.7
Franklin India Bluechip	★★★★★	197.8	-7.8	-12.2	**27.2**	8.6	25.3
Birla Sun Life Frontline Equity Fund - Plan A	★★★★	77.7	-10.9	-16.9	**25.5**	9.0	24.6
Tata Pure Equity Fund	★★★★	88.2	-7.6	-17.2	**23.4**	7.4	24.3
Indices							
BSE Sensex		16123.5	-11.6	-17.4	22.2	3.3	
Mid-cap funds							
SBI Magnum Sector Funds Umbrella - Emerg Buss Fund	★★★★★	42.1	2.4	0.9	**45.5**	7.2	21.9
IDFC Premier Equity Fund - Plan A	★★★★★	30.3	-5.4	-12.0	**36.9**	18.8	19.5
Religare Mid Cap Fund - Growth	★★★★	13.3	-6.1	-12.8	**36.6**	--	6.2
HDFC Mid-Cap Opportunities Fund	★★★★	14.5	-8.2	-11.8	**35.8**	--	8.5
Sundaram Select Small Cap Fund	★★★★	11.8	-6.0	-16.3	**33.4**	--	3.5
Indices							
BSE MID CAP		5627.7	-17.1	-27.5	25.5	-0.3	
Multi-cap funds							
ICICI Prudential Discovery Fund	★★★★★	42.6	-13.7	-16.4	**40.7**	9.4	21.7
Reliance Equity Opportunities Fund	★★★★★	32.3	-10.0	-14.5	**35.5**	9.0	19.0
Mirae Asset India Opportunities Fund - Reg	★★★★★	14.9	-10.0	-13.5	**34.9**	--	11.0
Tata Dividend Yield Fund	★★★★★	31.0	-7.5	-9.5	**34.1**	12.2	17.3
UTI Opportunities Fund	★★★★★	26.3	-3.6	-7.8	**30.7**	12.9	16.1
Indices							
BSE 500		6117.0	-14.1	-20.8	23.8	3.2	
Tax saving funds							
ICICI Prudential Taxplan	★★★★	124.1	-12.3	-16.2	**33.8**	6.0	22.6
HDFC Taxsaver	★★★★	204.1	-11.3	-17.9	**30.4**	6.7	28.5
Religare Tax Plan	★★★★★	16.0	-8.2	-13.7	**28.1**	--	9.8
Fidelity Tax Advantage Fund	★★★★	19.7	-9.9	-15.5	**28.1**	9.8	12.2
Franklin India Taxshield	★★★★★	197.1	-6.3	-9.5	**27.2**	9.1	26.5
Indices							
CNX500		3811.3	-13.8	-20.3	23.0	3.0	
Thematic funds							
UTI India Lifestyle Fund	★★★★★	11.3	-4.9	-7.5	**23.6**	--	2.6
Birla Sun Life India GenNext Fund	★★★★★	23.4	-3.8	-7.0	**24.7**	8.7	14.3
Fidelity India Special Situations Fund	★★★★	16.4	-11.0	-17.0	**25.6**	4.9	9.1
Canara Robeco Infrastructure Fund	★★★★	19.9	-9.6	-13.0	**26.5**	7.4	12.1
DSP BlackRock Natural Resources & New Energy Fund - Ret	★★★★	13.0	-8.5	-10.2	**29.0**	--	7.7
Indices							
S&P Nifty		4832.1	-11.7	-17.6	21.7	4.1	
Balanced funds							
HDFC Prudence Fund	★★★★	195.6	-8.2	-11.2	**30.7**	11.6	19.8
HDFC Balanced Fund	★★★★★	53.6	-5.6	-5.3	**29.7**	10.5	16.0
Birla Sun Life 95	★★★★	291.7	-6.1	-9.2	**26.1**	10.3	22.1
Canara Robeco Balance	★★★★	58.2	-4.1	-6.0	**24.3**	9.1	10.0
ICICI Prudential Balanced	★★★	45.1	-2.8	-4.3	**22.3**	5.7	13.2
Indices							
Crisil Balanced Fund Index		--	-6.2	-9.5	**16.6**	5.9	

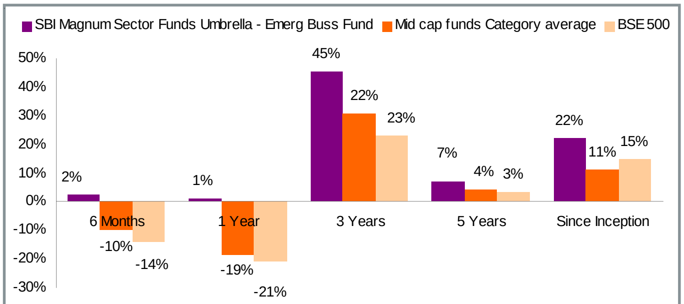
Note: Returns < 1 year - absolute, > 1 year - CAGR (compunded annualised growth rate)

SBI Magnum Sector Funds Umbrella - Emerging Bussiness Fund

Fact sheet

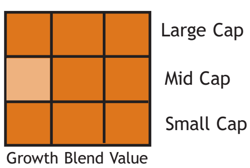
The investment objective of the SBI Magnum Sector Funds Umbrella -Emerging Business Fund would be to participate in the growth of various companies that are considered emergent and have export orientation/outsourcing opportunities or are globally competitive. The fund may also evaluate the emerging businesses with growth potential and domestic focus. Investment in equities would be well diversified across emerging sectors with exposure to any particular business restricted to 25% of the total investment portfolio under normal market conditions.

Scheme performance

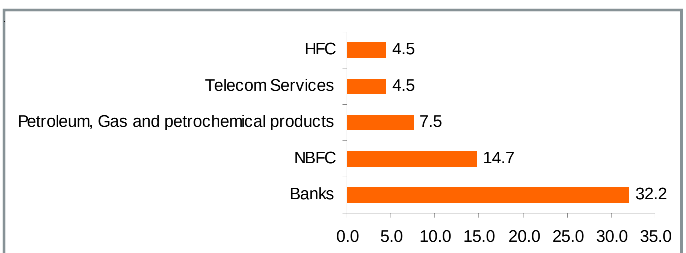


Returns < 1 yr: Absolute, >1yr: CAGR

Style box analysis



Top 5 sectors



Key features

• Fund category	Mid cap funds
• Launch date	Sept 17, 2004
• Minimum investment	Rs2,000
• Load structure	Entry:0%, Exit:1% if redeemed within 1 Year
• Fund manager	Rama Iyer Srinivasan
• Latest NAV (Gr.)	Rs42.26
• Latest NAV (Div.)	Rs16.00
• Expense ratio	2.3100 (Sep 2011)
• AUM (Sept 2011)	428.94 crore
• Benchmark Index	BSE 500

Holding by market cap

Particular	%
BSE Sensex	-
BSE Midcap	30.5
BSE Small cap	35.6
BSE 500	38.2
Top 5 holdings	33.0
Top 10 holdings	53.4

Top 10 stock holdings (Total no of scrips: 25)

Company name	% of net assets
Page Industries	7.3
Manappuram Finance	6.9
Bajaj Holdings & Investment	6.8
Hawkins Cooker	6.8
Spicejet	5.3
Goodyear India	5.3
Agro Tech Foods	4.2
Divis Laboratories	4.2
Cox & Kings (India)	3.4
Texmaco	3.3

Scheme analysis

The fund has been around for more than seven years now and been able to show good returns. Since its inception the fund has generated compounded annualised returns of 22%, outperforming its benchmark BSE 500, which grew by 15% over the same time frame. Over the past three years, the fund has displayed a growth of 45% (compounded annual growth rate) whereas the other multi-cap funds have grown by 31% on an average over the same period. It is noteworthy that despite the volatility in the market in the past six months, the fund emerged as a clear outperformer gaining 2%, while both, its peers as well the benchmark index, recorded losses of 19% and 21% respectively.

As the fund's strategy conveys, the fund manager has been investing in high-growth stocks majorly in the mid-cap and small cap segments. This has paid off the fund very well. On the sector front, the fund has been maintaining a somewhat concentrated allocation to the top five sectors constituting about 63.4% of the total allocation. The fund has nearly 84% of its net assets exposed to equities while the rest is exposed to money market instruments. Banks, non-banking financial institutions and petroleum sector have been the priority sectors for the fund manager with 32.2%, 14.7% and 7.5% of net assets allocated to them.

Fund ranking procedure

We have identified the best equity-oriented schemes available in the market today based on the following five parameters: the past performance as indicated by the one-year, two-year and three-year returns, the Sharpe ratio and the Information ratio.

The Sharpe ratio indicates risk-adjusted returns, ie the returns earned in excess of the risk-free rate for each unit of the risk taken. The Sharpe ratio is also indicative of the consistency of the returns as it takes into account the volatility in the returns as measured by the standard deviation.

The Information ratio is one of the most important tools in active fund management. It is the ratio of active return (the return over the index return) to active risk annualised. A higher Information ratio indicates a better fund manager.

We have selected the schemes based upon their ranking using the above five parameters and then calculated the maximum value of each of the five parameters. Thereafter, we have calculated the percentage under-performance or over-performance of each scheme (relative performance) based on each of the five parameters vis-a-vis the maximum value among them.

For our final selection of schemes, we have generated a total score for each scheme giving 60% weightage each to the relative performance as indicated by the one-year, two-year and three-year returns; 20% weightage to the relative performance as indicated by the Sharpe ratio; and the remaining 20% to the relative performance as indicated by the Information ratio of the scheme.

Sharekhan mutual fund ranking scale

Stars	Description
★★★★★	For top 10 percentile of the eligible schemes
★★★★	Next 22.5 percentile of the eligible schemes
★★★	Next 35 percentile of the eligible schemes
★★	Next 22.5 percentile of the eligible schemes
★	Bottom 10 percentile of the eligible schemes

Every individual has a different investment requirement, which depends on his financial goals and risk-taking capacities. We at Sharekhan first understand the individual's investment objectives and risk-taking capacity, and then recommend a suitable portfolio. So, we suggest that you get in touch with our Mutual Fund Advisor before investing in the best funds.

Disclaimer: Mutual fund investments are subject to market risk. Please read the offer document carefully before investing. Past performance may or may not be sustained in the future.

Evergreen

GlaxoSmithKline Consumer Healthcare
Housing Development Finance Corporation
HDFC Bank
Infosys
Larsen & Toubro
Reliance Industries
Tata Consultancy Services

Apple Green

Aditya Birla Nuvo
Apollo Tyres
Bajaj Auto
Bajaj FinServ
Bajaj Holdings & Investment
Bank of Baroda
Bank of India
Bharat Electronics
Bharat Heavy Electricals
Bharti Airtel
Corporation Bank
Crompton Greaves
Divi's Laboratories
GAIL India
Glenmark Pharmaceuticals
Godrej Consumer Products
Grasim Industries
HCL Technologies
Hindustan Unilever
ICICI Bank
Indian Hotels Company
ITC
Mahindra & Mahindra
Marico
Maruti Suzuki India
Lupin
Piramal Healthcare (Nicholas Piramal India)
PTC India
Punj Lloyd
Sintex Industries
State Bank of India
Tata Global Beverages (Tata Tea)
Wipro

Cannonball

Allahabad Bank
Andhra Bank
IDBI Bank
Madras Cements
Phillips Carbon Black
Shree Cement

Emerging Star

Axis Bank (UTI Bank)
Cadila Healthcare
Eros International Media
Greaves Cotton
IL&FS Transportation Networks
IRB Infrastructure Developers
Max India
Opto Circuits India
Thermax
Yes Bank
Zydus Wellness

Ugly Duckling

Ashok Leyland
Bajaj Corp
CESC
Deepak Fertilisers & Petrochemicals Corporation
Federal Bank
Gayatri Projects
Genus Power Infrastructures
India Cements
Ipca Laboratories
ISMT
Jaiprakash Associates
Kewal Kiran Clothing
NIIT Technologies
Orbit Corporation
Polaris Software Lab
Pratibha Industries
Provogue India
Punjab National Bank
Ratnamani Metals and Tubes
Raymond
Selan Exploration Technology
Shiv-Vani Oil & Gas Exploration Services
Sun Pharmaceutical Industries
Torrent Pharmaceuticals
UltraTech Cement
Union Bank of India
United Phosphorus
V-Guard Industries

Vulture's Pick

Mahindra Lifespace Developers
Orient Paper and Industries
Tata Chemicals
Unity Infraprojects