Investor's Eye

July 27, 2017

Index

Stock Update

Strong earnings visibility; Maintain Buy with a revised PT of Rs.8,500

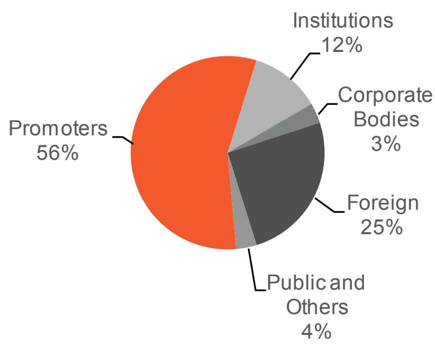
Maruti Suzuki

Reco: Buy | CMP: Rs7,592

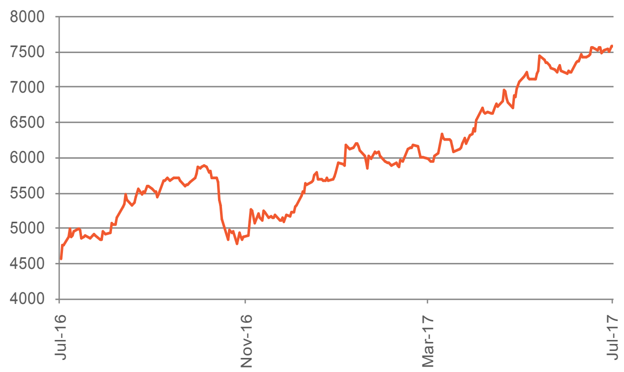
Company details

Price target:	Rs8,500
Market cap:	Rs229,348 cr
52-week high/low:	Rs7,679/4,513
NSE volume: (No of shares)	4.64 lakh
BSE code:	532500
NSE code:	MARUTI
Sharekhan code:	MARUTI
Free float: (No of shares)	13.2 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	4.8	18.1	30.4	70.4
Relative to Sensex	0.4	9.1	10.5	45.2

Key points

- **Higher raw-material cost and one-off GST compensation impact margins:** For Q1FY2018, Maruti Suzuki's (Maruti) performance was in line with our estimates, as increased costs restricted profit growth. The company's topline grew by 17% YoY, driven by sharp 13% YoY volume growth on account of sustained demand for its recent launches. Realisations/vehicle increased by 3% YoY, attributable to price hikes taken by the company and a better product mix. Operating profit margin for the quarter at 13.3% declined by 150BPS YoY (marginally lower than our expectation of 13.8%) due to higher raw-material prices and one-off discounts offered prior to GST rollout. Management stated that the margin impact of one-offs due to GST was to the tune of 80 bps. Other income at Rs.683 crore grew by 40% YoY. However, Tax/PBT ratio at 32.3% inched up in Q1FY2018 (Tax/PBT of 27.2% in Q1FY2017), thus dragging PAT growth to only 4%. Net profit came in line with our expectations.

- **Encouraging demand outlook coupled with commissioning of Gujarat plant to bolster sales; Maruti to continue outpacing the industry:** Demand outlook for passenger vehicles is encouraging, given the upcoming festive season and new product launches lined up. Market leader, Maruti is likely to continue to outpace industry growth, as four of its models (Baleno, Brezza, Ignis and Dzire), which form ~35% of the vehicle portfolio, command a waiting period of 2-5 months. Further, to curtail the waiting period for its cars, Maruti is speeding up production at the new Gujarat plant. Maruti targets to manufacture 150,000-160,000 units at Gujarat plant in FY2018, up from the earlier estimate of ~130,000 units. With supply constraints expected to ease out significantly, we expect Maruti to post strong double-digit volume growth at a ~12% CAGR over the next two years, which is substantially higher than the 8-10% growth expected for the passenger vehicle industry.

- **Outlook:** Maruti has successfully established itself in the big car category (Ciaz, Vitara Brezza, Dzire and Baleno), led by strong product features and success of its premium distribution network Nexa, which offers a unique buying experience. Maruti has established itself as a leader in all passenger vehicles categories, namely passenger cars, utility vehicles and vans. We expect Maruti to sustain its trend of outpacing the industry, given the robust order book for its existing models and strong new product launch pipeline. Maruti remains amongst our top picks in the automotive space.

- **Valuations:** Maruti has reported in-line results for Q1FY2018. Given the speeding up of production at the Gujarat plant, we have raised our FY2019 earnings assumptions by 3%. We maintain our Buy recommendation on the stock with a revised PT of Rs.8,500.

Results Rs cr

Particulars	Q1FY18E	Q1FY17	%YoY	Q4FY17	%QoQ
Revenue	17,546	14,944.7	17.4	18,333.4	-4.3
EBIDTA	2,331.2	2,214.8	5.3	2,559.5	-8.9
EBIDTA Margins (%)	13.3	14.8	(150) BPS	14.0	(70) BPS
Depreciation	683.9	638.0	7.2	701.0	-2.4
Interest (Income)	31.3	18.1	72.9	22.6	38.5
Other Income	682.7	488.1	39.9	449.1	52.0
PBT	2,298.7	2,046.8	12.3	2,285.0	0.6
Tax	742.3	555.9	33.5	574.5	29.2
Adjusted PAT	1,556.4	1,490.9	4.4	1,710.5	-9.0
EPS (Rs.)	51.5	49.4		56.6	

Valuation Rs cr

Particulars	FY15	FY16	FY17	FY18E	FY19E
Net sales	49,971	57,746	68,035	79,196	90,637
Growth (%)	14.3	15.6	17.8	16.4	14.4
EBITDA	6,703	8,979	10,353	11,132	13,455
EBIDTA %	13.4	15.5	15.2	14.1	14.8
PAT	3,711	4,571	7,338	8,032	10,216
Growth (%)	33.4	23.2	60.5	9.5	27.2
FD EPS (INR)	122.9	151.3	242.9	265.9	338.2
P/E (x)	61.8	50.2	31.3	28.6	22.4
P/B (x)	9.7	8.5	6.9	5.8	4.9
RoE (%)	15.7	20.0	23.0	20.9	21.8
RoCE (%)	20.5	26.9	29.3	27.6	28.9
EV/Sales(x)	4.5	4.0	3.0	2.6	2.2
EV/EBITDA (x)	33.8	25.7	19.9	18.3	14.6

Stock Update

Impressive margin execution, retain Buy

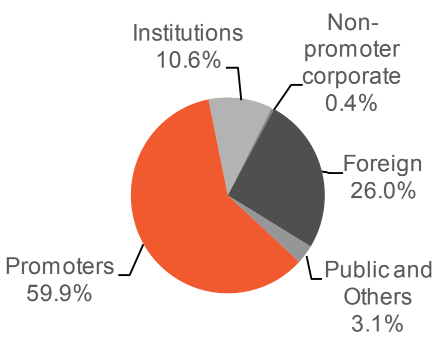
HCL Technologies

Reco: Buy | CMP: Rs890

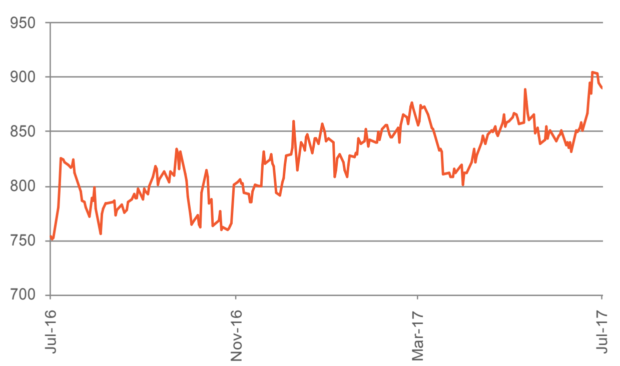
Company details

Price target:	Rs965
Market cap:	Rs123,831 cr
52-week high/low:	Rs926/731
NSE volume: (No of shares)	14.8 lakh
BSE code:	532281
NSE code:	HCLTECH
Sharekhan code:	HCLTECH
Free float: (No of shares)	55.9 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	4.8	12.3	7.6	23.4
Relative to Sensex	0.4	3.7	-8.8	5.2

Key points

- **Strong operating performance:** HCL Technologies (HCL Tech) reported yet another good quarter, with constant currency (CC) revenue growth of 2.6% QoQ. This was driven by a CC growth of 7.9% QoQ in Engineering and R&D Services (ERD) services (includes inorganic revenue from Geometric consolidation). On a reported basis, Q1FY2018 revenue grew by 3.7% QoQ to $1,884.2 million, broadly in-line with our estimates. EBIT margin improved by ~10BPS QoQ to 20.1%, above our expectation, led by operational efficiencies (improved utilisation), partially offset by rupee appreciation (40BPS impact, up 3.2% QoQ against USD and Geometric full quarter consolidation). The improvement in margin is also driven by the automation initiatives through its DRYiCE platform in the application and IMS services. Higher-than-expected forex gains (123% QoQ) offset by absence reversal of tax reversal benefit in Q4FY2017 ($45.5 million, up ~850BPS QoQ) resulted in 6.6% QoQ decline in net profit to Rs2,171 crore in Q1FY18. During the quarter, the company signed 13 transformational deals (vs eight deals in Q4FY2017) primarily in the USA and Europe.

- **Short-term hiccups in IMS, but Mode 2 & 3 to drive growth trajectory:** HCL Tech's management remains hopeful for delivering revenue for FY2018 in the targeted guidance range. The confidence stems from the overall demand environment for Mode 2 (Digital, Next Gen & Cloud) and Mode 3 (Product & Platform) services, despite reducing deal sizes in Mode 1 services (traditional services) and intense pricing pressure in renewals of contracts due to change in the business model. The management indicated that it foresees the slowdown in IMS services (38.6% of total revenues) to continue for the near-term owing to ongoing delays in decision-making process. However, it expects higher acceleration of revenues due to a healthy order book and strong pipeline in the Mode 2 and Mode 3 services and . Further, the company has extended the Intellectual Property (IP) agreement with IBM by investing ~$140 million during the quarter to cover the products in the area of marketing and mainframe area, which complements the company's digital and analytics practice. Till date, the company has made total investment of $780 million in IBM IP partnership till date.

- **Scaling-up capabilities ; maintain Buy with a price target of Rs965:** We have tweaked our revenue estimates for FY2018/FY2019 on account of currency reset to Rs 64.5 and management's commentary on slowdown on demand of IMS services (38.6% of total revenues). We believe, HCL Tech is investing in the right areas of digital technologies and products & Platforms for a more future sustainable growth. However, street is bit concerned on big investments in IBM deal ($780 mn) and its successful execution in terms of earnings. Given the reasonable valuation and best in class earning performance among the top tier IT companies, we have maintained our 'Buy' rating on the stock with a price target of Rs965.

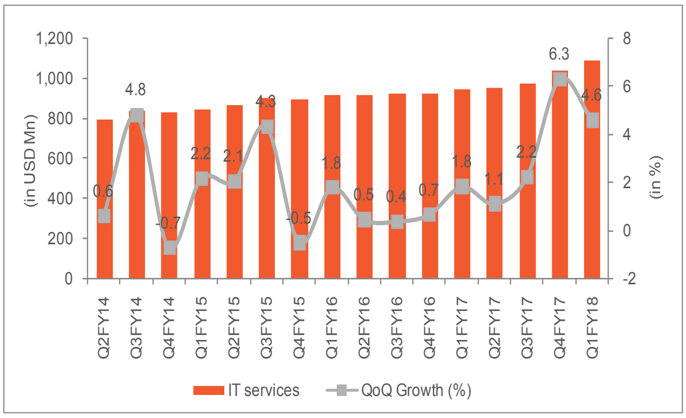
Valuation Rs cr

Particulars	FY16	FY17	FY18E	FY19E
Net sales	40,913.0	46,722.0	50,402.8	56,537.0
EBITDA margin (%)	21.5	22.1	22.0	22.4
Net profit	7,352.0	8,456.0	8,866.7	10,025.3
EPS (Rs)	52.8	60.7	63.7	72.0
P/E (x)	15.9	13.8	13.2	11.6
EV/EBITDA (x)	12.1	10.0	9.0	7.6
RoE (%)	28.1	27.7	24.7	24.0
RoCE (%)	34.3	33.0	30.0	29.4
Dividend yield (%)	1.9	2.1	2.3	3.0

Results Rs cr

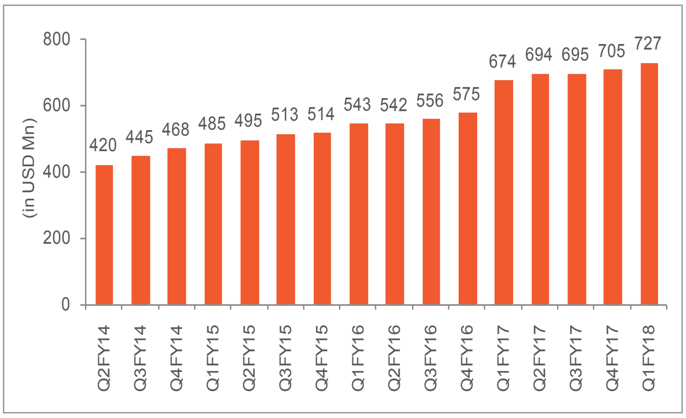
Particulars	Q1FY18	Q1FY17	Q4FY17	YoY (%)	QoQ (%)
Revenues ($ mn)	**1,884.2**	**1,690.7**	**1,816.8**	**11.4**	**3.7**
Net sales	**12,149.0**	**11,336.0**	**12,053.0**	**7.2**	**0.8**
Direct costs	8,057.0	7,440.0	7,987.0	8.3	0.9
Gross profit	**4,092.0**	**3,896.0**	**4,066.0**	**5.0**	**0.6**
SG&A	1,411.0	1,375.0	1,417.0	2.6	-0.4
EBITDA	**2,681.0**	**2,521.0**	**2,649.0**	**6.3**	**1.2**
Depreciation & amortisation	236.0	188.0	233.0	25.5	1.3
EBIT	2,445.0	2,333.0	2,416.0	4.8	1.2
Forex gain/(loss)	107.0	66.0	48.0	62.1	122.9
Other income	162.0	187.0	167.0	-13.4	-3.0
PBT	2,714.0	2,586.0	2,631.0	4.9	3.2
Tax provision	543.0	543.0	303.0	0.0	79.2
Net profit	**2,171.0**	**2,047.0**	**2,325.0**	**6.1**	**-6.6**
EPS (Rs)	**15.6**	**14.7**	**16.7**	**6.1**	**-6.6**
Margin (%)				**BPS**	**BPS**
EBITDA	22.1	22.2	22.0	-17	9
EBIT	20.1	20.6	20.0	-46	8
NPM	17.9	18.1	19.3	-19	-142

IT Services growth led by ERD Services (up 7.9% QoQ)



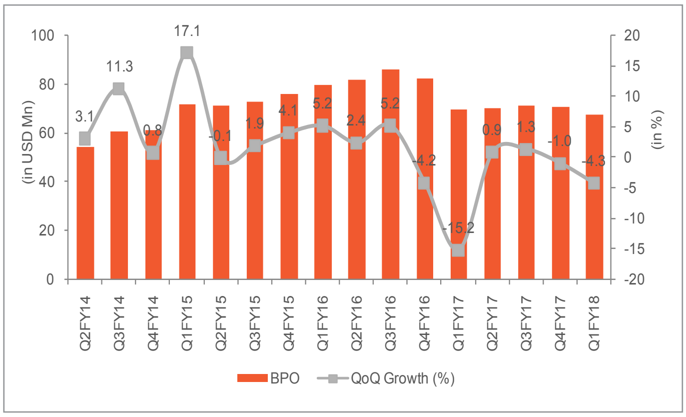
Source: Company, Sharekhan research

IMS up 1.7% QoQ on CC basis; contribution to revenue at 38.6%



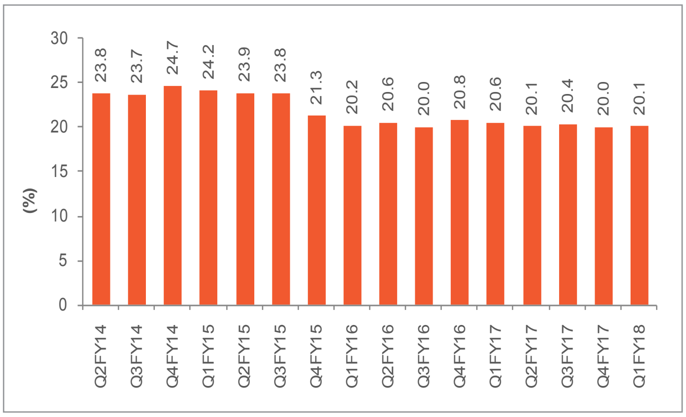
Source: Company, Sharekhan research

BPO continued to report muted growth



Source: Company, Sharekhan research

EBIT margin at 20.1%, ahead of our estimates



Source: Company, Sharekhan research

Other result highlights

- Cash & cash equivalents stood at $1,983.4 million as against $1,954.7 million in Q4FY2017. Borrowings stood at $88.2 million as against $83.5 million in the previous quarter.
- The day's sales outstanding (DSO) (ex-unbilled receivables) remained flat at 63 days on a sequential basis.
- The company's total headcount stood at 117,781 (net addition of 1,808). Gross addition for Q1FY2018 stood at 9,462 employees. Attrition further improved by 70BPS QoQ to 16.2%. Blended utilisation rate for Q1FY2018 increased by 30BPS to 86.0%.
- The company had total hedges worth $1.1 billion in Q1FY2018 against $1.4 billion at the end of Q4FY2017.
- HCL signed 13 transformational deals in Q1FY18, ranging across Financial Services, Manufacturing, Consumer Services, Lifesciences and Healthcare.
- Revenue per employee increased by 6% YoY to $63,500.

Key business metrics:

- Region-wise, the US business grew by 3.8% QoQ on CC basis in Q1FY2018, while European business reported muted revenue (down 0.4% QoQ on CC basis). The muted revenue performance in Europe was due to decline in the BPO vertical (regulatory issues) and structural reduction in the Infra deal last year. The RoW business grew by 3.1% QoQ (vs 15.8% in Q4FY17) on CC basis during Q1FY2018. During the quarter, Financial Services, Retail & CPG verticals and Healthcare verticals performed well, reported impressive CC growth of 5.3% QoQ, 4.9% QoQ and 4.8% QoQ respectively. However, Telecommunications (down 2.5% QoQ) and Public Services (down 2.7% QoQ) verticals performance remained soft during the quarter. ERD services continued its growth momentum on the back of contribution of inorganic revenue from Geometric consolidation, up 7.9% QoQ. IMS and application services CC revenue grew by 1.7% QoQ and 1.6% QoQ during the quarter.

Operating metrics

Particulars	Q1FY18	Q1FY17	Q4FY17	YoY (%)	QoQ (%)	Comments
Geographic mix (%)						
Americas	62.8	59.9	62.6	16.8	4.0	US grew by 3.8% QoQ on CC basis against 5.3% QoQ growth in Q4FY2017; Revenue from Europe continued to decline due to structural reduction in an Infra deal last year - reported marginal decline of 0.4% QoQ in CC terms vs a decline of 3.0% QoQ in Q4FY2017;
in $ mn	1,183.3	1,012.7	1,137.3			
Europe	27.4	31.4	27.7	-2.8	2.6	
in $ mn	516.3	530.9	503.3			
Rest of World	9.8	8.7	9.7	25.5	4.8	
in $ mn	184.7	147.1	176.2			
Service offering (%)						
Engineering and R&D services	21.5	17.7	20.5	35.2	8.8	ERD Services grew by 7.9% QoQ on CC basis against 14.6% QoQ growth in Q4FY2017, led by Geometric consolidation
in $ mn	405.1	299.6	372.4			
Industry application services	36.3	38.3	36.8	5.6	2.3	
in $ mn	684.0	647.5	668.6			
Infrastructure services	38.6	39.8	38.8	8.0	3.2	
in $ mn	727.3	673.6	704.9			
BPO services	3.6	4.1	3.9	-3.1	-4.3	
in $ mn	67.8	70.0	70.9			
Industry verticals (%)						
Financial services	24.9	23.6	24.2	17.6	6.7	Financial services and Lifesciences & Healthcare grew by 5.3% QoQ & 4.8% QoQ on CC basis, respectively. However, Public services and Telcom verticals declined by 2.7% QoQ and 2.5% QoQ on CC terms during the quarter.
in $ mn	469.2	399.0	439.7			
Manufacturing	34.9	33.2	34.6	17.2	4.6	
in $ mn	657.6	561.3	628.6			
Telecom, media & entertainment	7.9	9.1	8.4	-3.3	-2.5	
in $ mn	148.9	153.9	152.6			
Retail & consumer product group	9.5	10.0	9.2	5.9	7.1	
in $ mn	179.0	169.1	167.1			
Healthcare	11.8	11.9	11.5	10.5	6.4	
in $ mn	222.3	201.2	208.9			
Public services	11.1	11.7	11.7	5.7	-1.6	
in $ mn	209.1	197.8	212.6			
Others	0.0	0.5	0.3	NM	NM	
in $ mn	0.0	8.5	5.5			
Client contribution (%)						
Top 5 clients	14.4	13.9	14.7	15.5	1.6	Revenue from top 5 clients bucket was up by 1.6% QoQ; continuing its growth momentum (up 7.8% QoQ in Q4FY2017)
in $ mn	271.3	235.0	267.1			
Top 10 clients	22.4	21.8	22.1	14.5	5.1	
in $ mn	422.1	368.6	401.5			
Top 20 clients	33.0	31.7	32.9	16.0	4.0	
in $ mn	621.8	536.0	597.7			
Revenues by contract type (%)						
Managed Services & FPP	59.8	60.9	61.6	9.4	0.7	Managed Services and Fixed Price Projects (FPP) at 59.8%, down by 180BPS QoQ
in $ mn	1,126.8	1,029.6	1,119.1			
Time and materials	40.2	39.1	38.4	14.6	8.6	
in $ mn	757.4	661.1	697.7			
Number of clients						
1 million dollar +	508	482	506	26	2	Client addition remained strong; added one client in the $40 million and three clients under $30 million bucket on QoQ
5 million dollar +	249	237	246	12	3	
10 million dollar +	154	146	153	8	1	
20 million dollar +	86	80	85	6	1	
30 million dollar +	52	48	49	4	3	
40 million dollar +	35	32	34	3	1	
50 million dollar +	25	20	25	5	0	
100 million dollar +	8	7	8	1	0	

Stock Update

Despite steady asset quality performance, medium term challenges persist

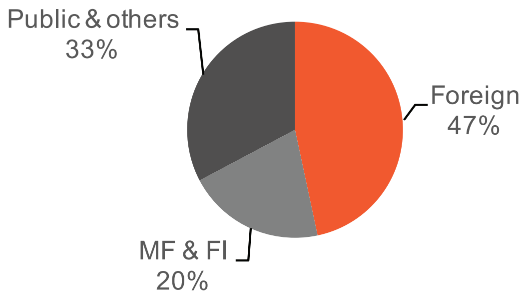
ICICI Bank

Reco: Hold | CMP: Rs307

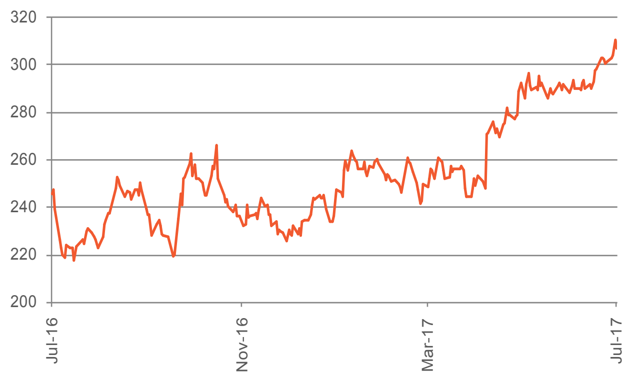
Company details

Price target:	Rs330
Market cap:	Rs196,916 cr
52-week high/low:	Rs314/215
NSE volume: (No of shares)	160.5 lakh
BSE code:	532174
NSE code:	ICICIBANK
Sharekhan code:	ICICIBANK
Free float: (No of shares)	641.28 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	6.3	24.2	32.3	31.5
Relative to Sensex	1.9	14.7	12.1	12.1

Key points

- **Satisfactory operating performance:** The operating performance of ICICI Bank was very much in line with our expectations as the net interest income (NII) growth stood at 8.4% YoY to Rs5589.8 crore. The non-interest income declined by 1.2% YoY. The fee income reported a decent growth of 10.3% YoY. During the quarter, the margins declined by 30BPS on a sequential basis to 3.27% on account of stable cost of funds while the yield on funds declined by 24BPS QoQ. Provisions during the quarter increased marginally by 3.7% YoY. RBI has advised the banks to initiate insolvency proceedings for certain accounts and make higher provisions for them, due to which, the bank will make additional provisions of Rs647 over the next three quarters.

- **Steady growth in retail advances, CASA ratio healthy:** Total advances increased by 3% YoY to Rs 464,075 crore during the quarter. The relatively slower advances growth was due to a decline in overseas loans and slower growth in the corporate book. Growth in domestic advances was better at 11%. The bank continues to leverage its strong retail franchise, resulting in a YoY growth of 19.6% in the retail portfolio. The SME loan book also reported a respectable growth of 16.2% YoY. Growth in the retail advances was driven by segments such as Home loan (up 18.1% YoY), Credit Cards (up 41.0% YoY) and Personal Loans (up 40.4% YoY). The retail portfolio constituted about 53.3% of the total loan book. During the quarter, deposits growth stood at 14.7% YoY fueled by a 24.4% YoY growth in CASA deposits. CASA ratio during the quarter declined by 142 BPS QoQ to 48.9%,but remains at a very healthy level.

- **Outlook:** ICICI Bank posted stable result for Q1 FY18. While the headline asset quality remained stable, the increase in the drill down list as well as outside drill down slippages are worrying factors. Corporate loan demand remains weak and hence the loan book growth outlook appears muted. The management has guided for lesser slippages in FY18 (as compared to FY17), which we believe may be difficult to meet. With several corporate loan exposures yet to undergo resolution and intermittent provision / NPA issues make for a murky asset quality outlook which is likely to be an overhang on stock performance.

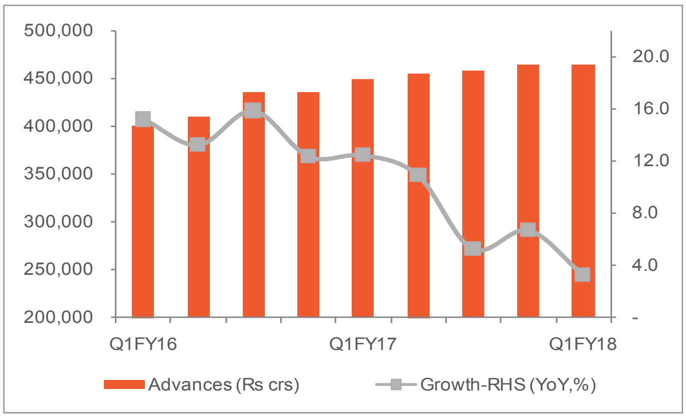
- **Valuation:** Since our last update (dated 3rd May, 2017), ICICI Bank stock has already given returns of ~24%. Considering the stock price run up and the uncertainty on the asset quality front for the stock, we believe there are limited upsides in the near term. Hence, we are downgrading the stock to "Hold" with a revised PT of Rs330.

- **Asset quality remains largely stable:** During the quarter, the asset quality remained largely stable as GNPA ratio increased a tad by 10BPS to 8.84% sequentially. However, considering an overall slower loan book growth, the asset quality performance seems satisfactory. Stress addition during the quarter declined as slippages for the quarter stood at Rs4976 crore versus Rs11,289 crore in the previous quarter. Recoveries and upgrades during the quarter were higher at Rs2775 crore. This was mainly due to one large account that got upgraded to AAA rated company. One engineering account on the other hand, outside the watch list slipped into the NPA category. Slippages from restructured book stood at Rs 1476 crore. The Bank currently has SDR outstanding to the tune of Rs3847 crore while it has implemented 5:25 refinancing in accounts worth Rs2675 crore. The watchlist during the quarter increased to Rs20358 crore form Rs19039 crore in Q4 FY17, up by 6.9%.

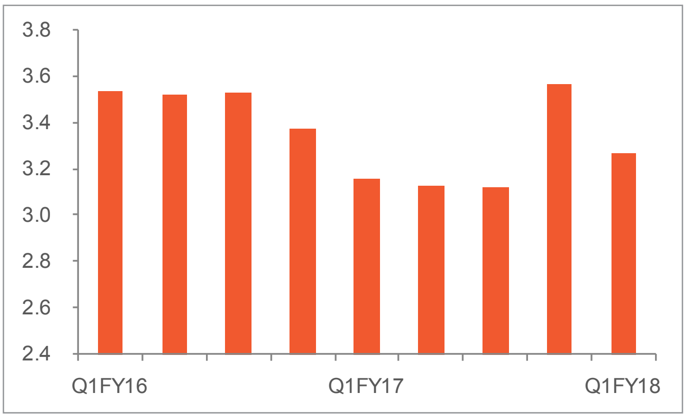
Results Rs cr

Particulars	Q1FY18	Q1FY17	YoY %	Q4FY17	QoQ %
Interest income	13,459.1	13,330.3	1.0	13,568.5	-0.8
Interest expense	7,869.3	8,171.7	-3.7	7,606.4	3.5
Net interest income	5,589.8	5,158.5	8.4	5,962.2	-6.2
Non-interest income	3,387.9	3,429.3	-1.2	3,017.2	12.3
Net total income	8,977.8	8,587.8	4.5	8,979.4	0.0
Operating expenses	3,794.4	3,373.1	12.5	3,867.4	-1.9
-Employee expenses	1,511.2	1,290.7	17.1	1,480.5	2.1
-Other operating expenses	2,283.3	2,082.4	9.6	2,386.9	-4.3
Pre-provisioning profit	5,183.3	5,214.7	-0.6	5,112.0	1.4
Provisions	2,608.7	2,514.5	3.7	2,898.2	-10.0
Profit before tax	2,574.6	2,700.2	-4.7	2,213.8	16.3
Tax	525.6	467.9	12.3	189.2	177.8
Profit after tax	2,049.0	2,232.4	-8.2	2,024.6	1.2
Asset quality					
Gross NPLs	43,147.6	27,193.6	58.7	42,551.5	1.4
Gross NPLs (%)	8.84	5.87	297 bps	8.74	10 bps
Net NPLs	25,306.2	15,040.7	68.3	25,451.0	-0.6
Net NPLs (%)	5.41	3.35	206 bps	5.43	-2 bps
Capital adequacy (%)					
CAR	17.89	16.45	144 bps	17.39	50 bps
Tier I	14.80	13.02	178 bps	14.36	44 bps
Key reported ratios (%)					
NIM	3.27	3.16	11 bps	3.57	-30 bps
CASA	48.95	45.12	383 bps	50.37	-142 bps

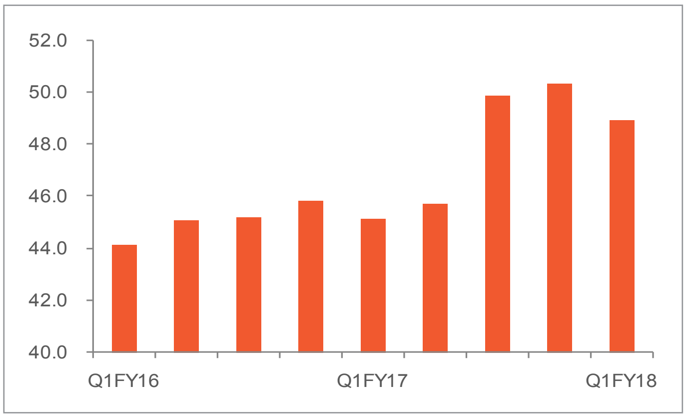
Advances growth (Rs cr)



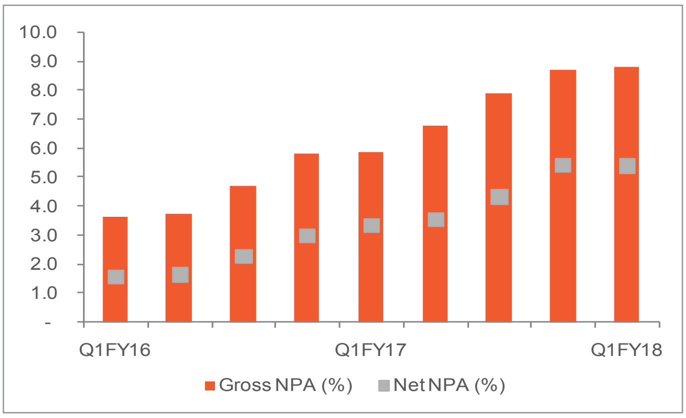
NIM (%)



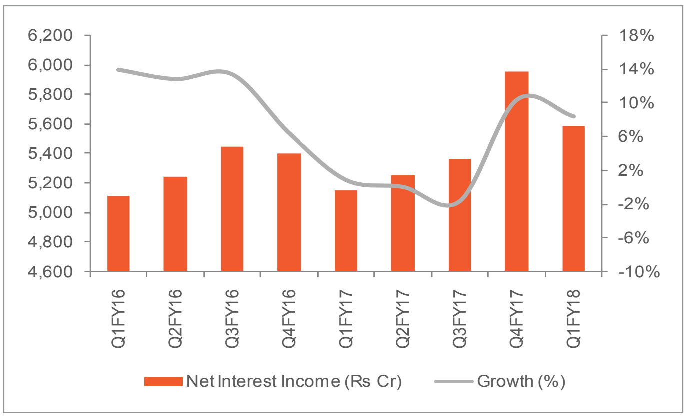
CASA ratio (%)



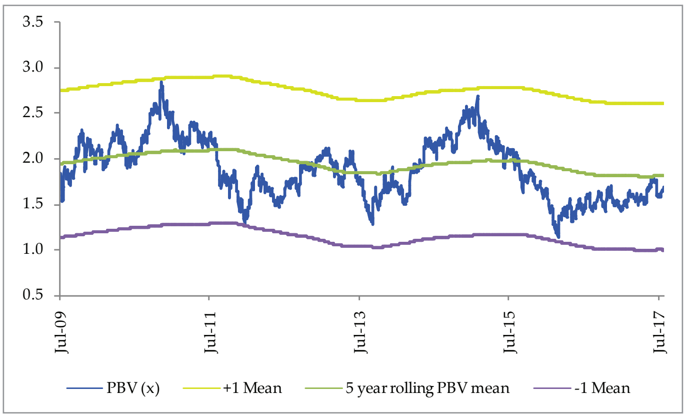
Asset quailty (%)



Net interest income



One-year forward P/BV SD band



Profit and loss statement Rs cr

Particulars	FY15	FY16	FY17	FY18E	FY19E
Net interest income	19,040	21,224	21,737	24,366	28,925
Non-interest income	12,176	15,323	19,504	15,363	16,922
Net total income	31,216	36,547	41,242	39,730	45,846
Operating expenses	11,496	12,684	14,755	16,767	18,601
Pre-provisioning profit	19,720	23,864	26,487	22,962	27,246
Provisions	3,900	11,668	15,208	9,292	8,949
Profit before tax	15,820	12,196	11,279	13,670	18,296
Tax	4,645	2,469	1,478	4,101	6,038
Profit after tax	11,175	9,726	9,801	9,569	12,259

Balance sheet Rs cr

Particulars	FY15	FY16	FY17	FY18E	FY19E
Liabilities					
Networth	80,429	89,736	99,951	102,780	110,688
Deposits	361,563	421,426	490,039	568,445	665,081
Borrowings	172,417	174,807	147,556	201,249	235,894
Other liabilities & provisions	31,720	34,726	34,245	39,262	45,408
Total liabilities	646,129	720,695	771,791	911,736	1,057,070
Assets					
Cash & balances with RBI	25,653	27,106	31,702	28,706	33,587
Balances with banks & money at call	16,652	32,763	44,011	25,580	29,929
Investments	186,580	160,412	161,507	243,516	282,472
Advances	387,522	435,264	464,232	533,867	629,963
Fixed assets	4,726	7,577	7,805	8,195	8,605
Other assets	24,997	57,574	62,535	71,871	72,514
Total assets	646,129	720,695	771,791	911,736	1,057,070

Key ratios

Particulars	FY15	FY16	FY17	FY18E	FY19E
Per share Data (Rs)					
Earnings	19.3	16.7	16.8	14.9	21.0
Dividend	5.0	5.0	0.0	4.2	5.9
Book value	130.1	146.4	164.6	153.9	183.0
Adj. book value	108.0	113.0	110.6	105.8	126.7
Spreads (%)					
Yield on Advances	9.8	9.5	8.8	8.3	8.3
Cost of Deposits	5.9	5.5	5.0	4.7	4.6
Net interest margins	3.3	3.4	3.1	3.2	3.2
Operating ratios (%)					
Credit to Deposit	107.2	103.3	94.7	93.9	94.7
Cost to income	36.8	34.7	35.8	42.2	40.6
CASA	45.5	45.8	50.4	50.4	49.9
Non interest income / Total income	39.0	41.9	47.3	38.7	36.9
Assets/Equity (x)	8.1	8.0	7.9	8.3	9.2
Return ratios (%)					
RoE	14.5	11.4	10.3	9.4	11.5
RoA	1.8	1.4	1.3	1.1	1.2
Asset Quality ratios (%)					
Gross NPA	3.8	5.8	8.8	7.4	6.4
Net NPA	1.6	3.0	5.4	4.6	4.2
Growth Ratios (%)					
Net interest income	15.6	11.5	2.4	12.1	18.7
Pre-provisioning profit	18.8	21.0	11.0	-13.3	18.7
Profit after tax	13.9	-13.0	0.8	-2.4	28.1
Advances	14.4	12.3	6.7	15.0	18.0
Deposits	8.9	16.6	16.3	16.0	17.0
Valuation ratios (x)					
P/E	15.9	18.4	18.3	20.6	14.6
P/BV	2.4	2.1	1.9	2.0	1.7
P/ABV	2.8	2.7	2.8	2.9	2.4

Stock Update

Upgrading to Buy - Weak quarter, improved outlook

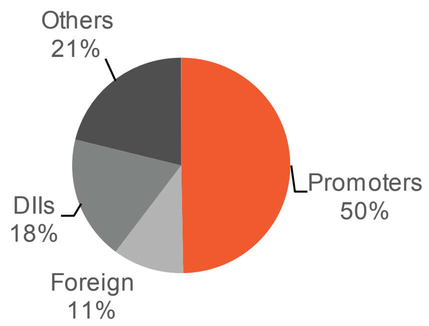
Supreme Industries

Reco: Buy | CMP: Rs 1,126

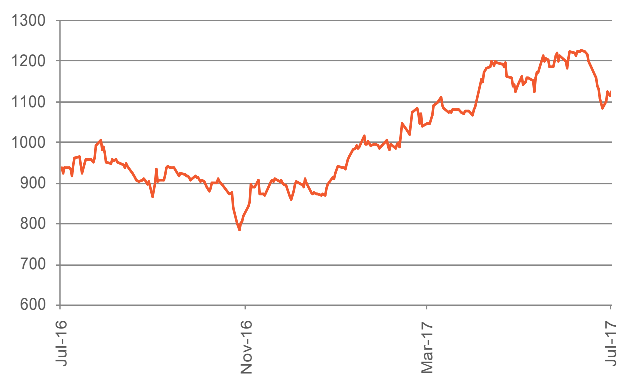
Company details

Price target:	Rs1,250
Market cap:	Rs14,301 cr
52-week high/low:	Rs1,250/780
NSE volume: (No of shares)	0.61 lakh
BSE code:	509930
NSE code:	SUPREMEIND
Sharekhan code:	SUPREMEIND
Free float: (No of shares)	6.4 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-9.1	5.3	22.6	20.7
Relative to Sensex	-12.9	-2.8	3.9	2.9

Key points

- **Weak quarter owing to GST roll out:** On the anticipated line, Supreme Industries Limited (SIL) delivered a weak set of numbers for Q1FY2018, led by major destocking from distributers owing to GST roll out. Revenue declined by 2.3% YoY to Rs.1,161.7 crore, led by volume decline across the product segments except for industrial products (up by 5.8% YoY). For the quarter, plastic piping division's volume declined by 6.7%, packaging declined by 2.3% and consumer products was down by 7.9%. Overall volumes for the quarter declined by 5% YoY. Further, realisation in the packaging segment declined by 4.2%, while realisation for the other three segments was on the positive side. Overall, realisation increased by 3% YoY. Value-added products' (VAR) contribution stood at 32% in Q1FY2018 as compared to 35% in Q1FY2017.

- **Margins much below expectations, attributed to inventory loss:** SIL's operating profit margin (OPM) for the quarter declined by 333BPS YoY to 13.7% (missed estimates), attributed to inventory loss owing to fall in PVC price coupled with a decline in the contribution of value-added products. OPM of the plastic piping division came in at 13% in Q1FY2018 versus 16% in Q1FY2017, while the packaging division's OPM stood at 19% versus 23% in Q1FY2017. Industrial products' OPM stood at 11% versus 12% YoY and consumer products' OPM came in at 16% versus 19% YoY. Net profit for the quarter declined by 23.6% YoY to Rs.75.3 crore.

- **Expect growth revival from Q2FY2018:** Management remains confident of growth revival starting from Q2FY2018 itself. After witnessing soft growth in July, management expects growth to start picking up from August 2017 as most distributers (around 2,699) are already GST registered and re-stocking will aid in better performance in Q2. Overall, for FY2018, management expects 12%+ volume growth, which was revised from earlier guidance of 12-15% owing to GST-related destocking. On the margin side, management expects OPM to be around 15-15.5% for FY2018E. The average monthly borrowing in Q1FY2018 stood at Rs.196 crore in Q1FY2018, down from Rs.382 crore in Q4FY2017. Management expects the company to be virtually debt free by the end of FY2018. The total planned capex for FY2018 is estimated at Rs.300 crore-350 crore, which will be funded entirely from internal accruals.

- **Valuation: Upgrade to Buy with unchanged TP of Rs.1,250:** We have revised down our earnings estimates for FY2018/FY2019E, owing to higher-than-expected impact on volume growth for FY2018 and weak margin performance in Q1FY2018. We continue to remain positive on SIL on a long-term perspective, given the strong tailwinds post the GST regime stabilises and opportunities from spends from housing and irrigation space among others. SIL will be one the prime beneficiaries of the unorganised to organised shift post the GST regime, and we believe potential case for earnings surprise in FY2019 and FY2020 (full impact of GST regime) is quite possible. Additionally, positive news flows from increased market share for organised players in the GST regime will drive further re-rating in the long term and support the valuation multiple in the near term despite earnings cut post weak earnings reported in Q1FY2018. Post our downgrade last month, the stock has corrected close to 9.5% and touched a low of Rs.1,084. Looking at strong long-term triggers and potential re-rating over the next 8-12 months, we upgrade the stock to Buy from Hold with unchanged TP of Rs.1,250.

Results Rs cr

Particulars	Q1FY18	Q1FY17	YoY (%)	Q4FY17	QoQ (%)
Total revenue	1,161.7	1,189.3	-2.3%	1,282.6	-9.4%
Total expenditure	1,003.0	987.3	1.6%	1,040.0	-3.6%
EBITDA	158.7	202.0	-21.5%	242.6	-34.6%
Depreciation	40.6	37.0	9.6%	41.2	-1.4%
EBIT	118.1	165.0	-28.4%	201.5	-41.4%
Other income	0.4	0.6	-28.3%	2.6	-83.2%
Interest expenses	3.3	9.7	-65.8%	3.4	-2.9%
PBT	115.2	155.9	-26.1%	200.6	-42.6%
Tax expenses	39.9	53.7	-25.7%	73.3	-45.6%
Reported net profit	75.3	98.5	-23.6%	90.2	-16.5%
Adjusted EPS (Rs)	5.9	8.0	-26.3%	10.0	-40.9%
Margins (%)			BPS		BPS
EBITDA margin	13.7	17.0	-333	18.9	-526
PAT margin	6.5	8.6	-211	9.9	-344
Effective tax rate	34.6	34.5	17	36.5	-191

Valuation Rs cr

Particulars	M9FY16	FY17	FY18E	FY19E
Revenues (Rs cr)	2,960.1	4,462.3	4,955.7	5,997.7
EBITDA margin (%)	15.6	17.1	15.9	16.9
Adjusted PAT (Rs cr)	212.0	376.7	406.6	547.2
Adjusted EPS (Rs)	16.7	29.7	32.0	43.1
RoCE (%)	21.4	27.8	28.1	32.7
RoE (%)	16.1	22.2	20.7	23.6
P/E (x)	67.8	38.2	35.4	26.3
P/BV (x)	10.9	8.5	7.3	6.2

Viewpoint

Strategy implementation on right track

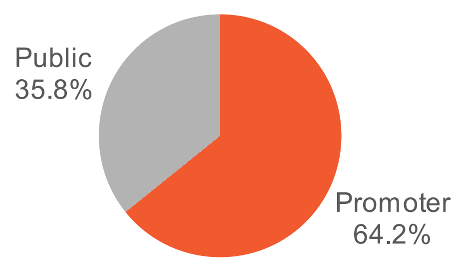
L&T Finance Holdings

View: Positive | CMP: Rs161

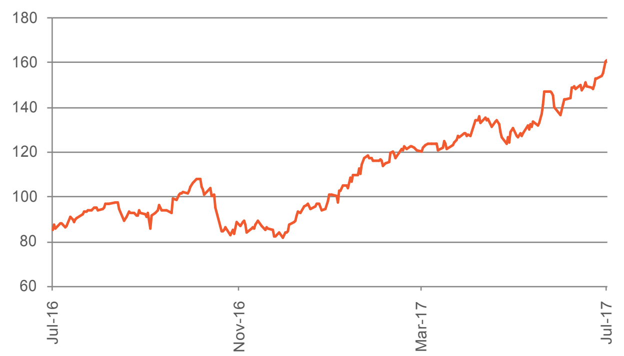
Company details

Market cap:	Rs29,367 cr
52-week high/low:	Rs167/79
NSE volume: (No of shares)	43.6 lakh
BSE code:	533519
NSE code:	L&TFH
Sharekhan code:	L&TFH
Free float: (No of shares)	65.15 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	14.8	26.4	59.6	107.4
Relative to Sensex	10.0	16.8	35.2	76.8

Key points

- **Operating performance outperforms expectations:** L&T Finance Holdings (LTFH) posted impressive results for Q1FY18 and is well on track to achieve top quartile Return on Equity (RoE). The Net interest income was up by 22.0% YoY to Rs1026.1 crore driven by better loan growth. Fee income during the quarter increased substantially by 177% YoY to Rs305 crore while sell down volumes also increased to Rs2583 crore from Rs595 crore YoY and Rs2007 crore in the previous quarter. Tight control on the operations and efficient utilization of resources helped the company contain operating expenses growth at 1.7% YoY. Provisions during the quarter increased by 81.3% YoY as the company made additional voluntary provisions of Rs95 crore and Rs49 crore in its rural and wholesale segment respectively. Driven by better loan growth, control on operating expenses and other income, the net profit during the quarter surged by 49.1% YoY to Rs309.2 crore.
- **Business growth gains traction as effects of Demonetization fade:** LTFH has seen steady increase in its loan book growth post the demonetization quarter as loan book growth for Q1FY18 stood at 18.1% YOY as against 14.4% and 10.4% in the previous two quarters. The focused book growth was even higher at 22.4% YoY while the de-focused book contracted by 45.9% YoY (now <4% of loans). The focused book growth was driven by rural (up 22.3% YoY), housing (up 30.2% YoY) and wholesale (up 20.1% YoY) segments. Growth in disbursements during the quarter was also higher at 201% YoY boosted by a 256% YoY increase in wholesale disbursement (partially driven by IPO funding of Rs8000 crore).
- **Outlook:** LTFH's earlier plans to achieve higher return ratios appears to be working well. The company has seen business traction and is looking to consolidate gains backed by strong processes and focus. LTFH's focus on growing in its area of strength, upgrading technological capabilities to recognize risk early, opex control etc make it an attractive franchise in the making.
- **Valuation:** LTFH currently trades at 2.4xFY19E BVPS which we feel is reasonable for a company in a high business growth phase, improving RoE and RoA trajectory along with better asset quality outlook and rising balance sheet strength. We maintain our "positive" view on the stock and foresee 15-18% potential upside from current levels.

- **Impressive show on the asset quality front:** During the quarter, LTHF moved to 90 Days Past Due (DPD) from 120 DPD. As a result, the Gross Non Performing assets (GNPA) ratio increased by 76BPS to 5.71% from 4.95% in Q4 FY17. However, on comparable 90 DPD basis the GNPA ratio improved from 7.11% to 5.71% QoQ. Even in absolute terms, GNPA reduced to Rs3698 crore versus Rs4519 crore on comparable basis. During the quarter, the provisioning coverage increased from 31.0% to 43.4% on a sequential basis. Surprisingly, the farm loan waivers that has impacted its peers, had no noticeable impact on the rural asset quality. Rural GNPA even improved to 11.35% from 12.21% QoQ. The collection efficiency is also back to normalized levels of 99+%. LTFH is increasingly and effectively using tools such as business analytics and strong risk management framework to shore up asset quality. These efforts will improve overall risk management.

Results Rs cr

Particulars	Q1FY18	Q1FY17	YoY %	Q4FY17	QoQ %
Net Interest Income	1,026.1	840.8	22.0	1,004.6	2.1
Non- Interest Income	107.1	34.2	212.7	75.5	41.7
Net total Income	1,133.2	875.1	29.5	1,080.1	4.9
Operating expenses	327.7	322.2	1.7	306.3	7.0
employee cost	110.4	109.5	0.9	133.8	(17.4)
other costs	217.3	212.7	2.1	172.5	25.9
Pre-provisioning profit	805.5	552.9	45.7	773.8	4.1
Provisions	458.7	253.0	81.3	688.5	(33.4)
Profit before tax	346.8	299.9	15.7	85.3	306.4
Tax	37.8	95.1	(60.2)	(228.6)	NA
Profit after tax	309.2	207.4	49.1	315.8	(2.1)
GNPA %	5.71	10.26	-455 bps	4.95	76 bps
NNPA %	3.31	8.85	-554 bps	2.89	42 bps
Loan Book	68,180	57,736	18.1	66,648	2.3

Profit and loss statement Rs cr

Particulars	FY15	FY16	FY17	FY18E	FY19E
Net interest income	2,335	2,693	3,174	3,959	4,975
Non-interest income	435	653	771	865	986
Net total income	2,770	3,347	3,945	4,825	5,961
Operating expenses	1,077	1,313	1,276	1,468	1,732
Pre-provisioning Profits	1,693	2,034	2,669	3,357	4,229
Provisions	662	781	1,590	1,425	1,753
Profit before tax	1,031	1,253	1,079	1,931	2,476
Tax	324	399	36	637	842
Profit after tax	707	854	1,042	1,294	1,634

Balance sheet Rs cr

Particulars	FY15	FY16	FY17	FY18E	FY19E
Share Capital	3,084	2,967	2,969	2,969	2,969
Reserves & Surplus	4,656	5,442	6,138	7,389	8,971
Networth	7,740	8,409	9,107	10,358	11,940
Minority Interest	100	100	119	119	119
Borrowings	42,695	52,199	60,543	72,046	85,735
Provisions	472	592	367	436	519
Total Liabilities	51,007	61,300	70,136	82,959	98,313
Fixed Assets	1,357	1,335	1,258	1,384	1,522
Investments	2,649	3,563	6,012	5,666	7,071
Loans & Advances	46,042	56,468	62,314	74,777	89,733
Deff. Tax Assets (Net)	290	399	743	884	1,052
Cash & Equivalent	862	402	594	1,183	47
Net Current Assets	(194)	(867)	(785)	(934)	(1,112)
Total Assets	51,007	61,300	70,136	82,959	98,313

Key ratios

Particulars	FY15	FY16	FY17	FY18E	FY19E
Per share data (Rs)					
Earnings	4.3	3.8	5.2	7.4	9.3
Book value	45.0	48.0	51.9	59.0	68.0
Adj. book value	39.6	43.3	38.6	48.5	58.5
Operating ratios (%)					
Cost to income	43.5	45.7	37.5	34.1	32.4
Non interest income / Total	5.7	6.3	6.8	8.1	6.8
Return ratios (%)					
RoE	9.8	10.6	11.9	13.3	14.7
RoA	1.5	1.5	1.5	1.6	1.7
Asset quality ratios (%)					
Gross NPA	2.3	3.1	4.5	3.7	3.1
Net NPA	2.0	1.5	3.8	2.5	1.9
Growth ratios (%)					
Net interest income	29.9	15.4	17.9	24.7	25.7
Pre-provisioning profit	37.3	20.2	31.2	25.8	26.0
Profit after tax	22.8	20.5	21.7	24.2	26.3
Advances	18.4	22.6	10.4	20.0	20.0
Borrowings	17.5	22.3	16.0	19.0	19.0
Valuation ratios (x)					
P/E	37.5	42.5	31.0	21.9	17.3
P/BV	3.6	3.4	3.1	2.7	2.4
P/ABV	4.1	3.7	4.2	3.3	2.8

Viewpoint

Double-digit revenue growth though early EOSS dents margins in Q1FY2018

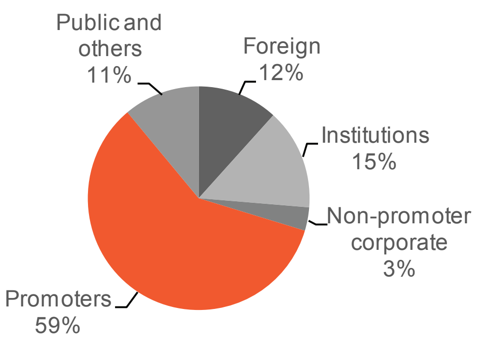
Aditya Birla Fashion & Retail

View: Positive | CMP: Rs170

Company details

Market cap:	Rs13,093 cr
52-week high/low:	Rs188/127
NSE volume: (No of shares)	5.8 lakh
BSE code:	535755
NSE code:	ABFRL
Sharekhan code:	ABFRL
Free float: (No of shares)	31.4 cr

Shareholding pattern



Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	1.9	4.4	18.9	19.2
Relative to Sensex	-2.4	-3.6	0.7	1.6

Key points

- **Strong double digit growth in revenue, margins under pressure due to early EOSS:** Aditya Birla Fashion & Retail's (ABFRL) revenue for Q1FY2018 grew strongly by 24.6% YoY to Rs1,760 crore, ahead of our expectation of Rs1,600.6 crore. The revenue growth was led by a strong ~25% YoY expansion in Madura Fashion & Lifestyle (MFL) and 27% YoY growth in Pantaloons. Wedding season during April-May and an early End of Season Sale (EOSS) spurred the growth momentum. The company reported decline of ~340BPS YoY in gross margins at 52.7%, due to the increase in input prices (cotton prices up by ~15% YoY in Q1FY2018) and sustained losses in the new businesses. Lower realization from sales because of the discounts offered during EOSS had a negative impact on margins. However, the operational efficiencies of the company arrested the significant fall in Operating Profit Margin (OPM) by ~75BPS YoY at 4.2% while the operating profit grew by ~6% YoY to Rs74 crore. The other income was higher by 33% YoY but higher depreciation resulted loss at bottom line to Rs. 20 crore as against loss of Rs. 21 crore in Q1FY2017.

- **Double digit revenue growth to sustain; margins likely to remain muted in near term:** Q1FY2018 performance was positively impacted by EOSS/wedding season resulting in strong double-digit revenue growth in MFL and Pantaloons. Going ahead we expect the double-digit revenue growth momentum to sustain over the forthcoming quarters. Higher sales (led by festive/wedding season) and enhanced brand presence in the domestic market will augment growth. However, revenue growth in Q2FY2018 will be lower than that the first quarter as the benefits of EOSS won't spill on to Q2FY2018. Further, the sustenance of losses in the Forever 21(though expected to break even by end of FY2018) and Van Heusen inner wear/ athleisure segment along with transition effect of GST implementation will keep margins under pressure in the near term. Hence, we expect margins expansion to be better in FY2019. In view of near term pressure on the margins, we downgrade our FY2018 and FY2019 earnings estimates by 6.5% and 5% respectively.

- **Valuation – retain positive view with 12-13% upside:** ABFRL has a strong portfolio of brands in the space of branded apparels. With the scaling up of Forever 21 and inner wear business, we expect strong revenue growth momentum to sustain and a gradual improvement in the margins over the medium term. We maintain our positive view on the stock with an upside of 12-13%. The upside is lower than our earlier expectation of 15-18% mainly due to the lowering of margin expectation.

Results Rs cr

Particulars	Q1FY18	Q1FY17	YoY %	Q4FY17	QoQ %
Total revenues	1,760.0	1,412.0	24.6	1,614.9	9.0
Total expenditure	1,686.0	1,342.0	25.6	1,501.0	12.3
Operating profit	74.0	70.0	5.7	114.0	(35.1)
Interest	43.0	45.0	(4.4)	43.7	(1.6)
Depreciation	59.0	52.0	13.5	65.8	(10.3)
Non operating income	8.0	6.0	33.3	17.4	(53.9)
PBT	(20.0)	(21.0)		21.8	
Tax	-	-		-	
PAT	(20.0)	(21.0)	-	21.8	-
EPS (Rs)	(0.3)	(0.3)	-	0.3	-
GPM (%)	52.7	56.1	(342.0)	54.7	(201.0)
OPM (%)	4.2	5.0	(75.4)	7.1	(285.3)

Valuations Rs cr

Particulars	FY15	FY16	FY17	FY18E	FY19E
Net sales	1,851	6,060	6,603	7,888	9,595
EBITDA	72.7	396.8	437.5	540.2	743.4
EBITDA margin (%)	3.9	6.5	6.6	6.8	7.7
PAT	(228.1)	(104.1)	53.5	123.9	217.1
EPS	(24.5)	(1.4)	0.7	1.6	2.8
RoCE	(6.7)	3.2	7.7	9.0	11.2
RoE	(49.3)	(16.6)	5.7	12.2	18.3
EV/EBITDA (x)	38.7	37.9	34.9	28.4	20.7

Other highlights

MFL revenue growth robust; margins remained under pressure: MFL's Q1FY2018 revenue grew by 24.7% YoY to Rs1,050 crore driven by a 14% revenue growth in the Lifestyle brands segment. The revenues in the Fast Fashion segment tripled in Q1FY2018 due to addition of Forever 21 while other businesses grew by 63% YoY. The Same Stores Sales Growth (SSSG) stood strong at 21% YoY in Q1FY2018 due to focused store level interventions to drive organic growth. Also, the four season cycle led to greater freshness and lower inventory across channels. EBITDA de-grew by ~21% YoY to Rs37 crore due to EOSS and also due to losses in the new businesses of Rs. 28 crores. Post its acquisition in July 2016, operations in Forever 21 have now stabilised and the integration is now complete with 18 stores in India. Also, ABFRL has 90 stores under the People brand, which is positioned to target the college going youth and the new salaried class. The management aims to turn Forever 21 profitable in FY2018 by rationalizing existing stores in terms of store size and also introducing new stores with better pricing in terms of rent and location. The company plans to add 8-10 Forever 21 stores during FY2018. As far as the Van Heusen Innerwear and Athleisure wear segment is concerned, the company has been able to distribute it across 2000 stores and has covered all the main cities of South India. It has also commenced the process of launching the product in New Delhi and NCR and aims to cover 8000-9000 outlets by the end of FY2018.

Madura Fashion & Lifestyle (MFL)

Particulars	Q1 FY18	Q1 FY17	YoY %	Q4 FY17	QoQ %
Revenues	1050.0	842.06	24.7	1045.04	0.5
EBITDA	37	47	(21.3)	117	(68.4)
EBITDA Margin (%)	3.5	5.6	-	11.2	-

Pantaloons posts strong quarter with 27% revenue growth and 77% growth in EBITDA: Pantaloons' saw a good growth of 27% YoY in its Q1FY2018 revenue to Rs731 crore, led by pre GST sales momentum and robust SSSG of 14% YoY. During the months of April-May, revenue growth was in single digits, but shot up significantly in June due to EOSS. The contribution of its own brands to Pantaloons revenue remained stable on a YoY basis at 63% in Q1FY2018. The four-season cycle significantly improved the inventory levels. The company added 5 new stores in Q1FY2018, 1 being a franchisee store. Going ahead, ABFRL will open 40-50 new stores every year with 20% of them being through the franchisee route. At the end of Q1FY2018, there were 213 Pantaloons stores, including 29 franchisee stores, 16 only-women stores and nine only-kids stores. Pantaloons' loyalty customer base increased to eight million at the end of Q1FY2018 from 7 million at the end of Q4FY2017. Pantaloons registered ~77% YoY growth in EBITDA driven by strong SSSG and tighter cost control in spite of an early EOSS. Going ahead, we expect Pantaloons to grow in double digits, driven by the expansion of stores done and improved consumer sentiment.

Pantaloons

Particulars	Q1 FY18	Q1 FY17	YoY %	Q4 FY17	QoQ %
Revenues	731.00	574.35	27.3	585.72	24.8
EBITDA	46	26	76.9	14	-
EBITDA Margin (%)	6.3	4.5	-	2.4	-

IPO Flash

Cochin Shipyard Limited

IPO details:	
Issue opens	August 1, 2017
Issue closes	August 3, 2017
Issue size	Rs.1,415 crore-1,442 crore
Offer size	3.40 crore shares
Of which OFS	1.13 crore shares
Of which employee reservation	0.08 crore shares
Face value	Rs.10
Net Issue to public	3.32 crore shares of which
QIB portion	50% of issue
Non-institution portion	15% of issue
Retail portion	35% of issue
Discount	Rs21 per Equity Share to Retail & Employee
Bid Lot	30 Equity Shares & in multiple thereafter
Price band	Rs.424-432 per share

About the IPO

Cochin Shipyard Limited (CSL) is coming out with an initial public offering (IPO) of 3.40 crore equity shares (of which offer for sale comprises 1.13 crore shares and employee reservation comprises 0.08 crore shares) with a face value of Rs.10 each. The issue is priced at Rs.424-432 per share (Rs.21 discount for retail investors and employees). The company intends to raise Rs.1,415 crore-1,442 crore (post discount to retail investors and employees). The company plans to use the net proceeds for setting up of dry dock within the existing premise of the company (Rs.443 crore), setting up of an international ship repair facility at Cochin Port Trust area (Rs.229.5 crore) and general corporate purposes.

Company Background

CSL is a wholly owned Government of India (GoI) company. The company was incorporated on March 29, 1972, and was conferred the Miniratna status in 2008 by the Department of Public Enterprises, GoI. The company commenced operations in 1975 and has over four decades of experience in shipbuilding. CSL's key shipbuilding clients include the Indian Navy, Indian Coast Guard and the Shipping Corporation of India (SCI). The company has also exported 45 ships to various commercial clients outside India, such as NPCC, the Clipper Group (Bahamas), Vroon Offshore (Netherlands) and SIGBA AS (Norway). CSL began its ship repair operations in 1978 and has undertaken repairs of various types of vessels, including upgradation of ships of the oil exploration industry as well as periodical maintenance, repairs and life extension of ships. The company's key ship repair clients include the Indian Navy, Indian Coast Guard, SCI, the Oil & Natural Gas Corporation (ONGC) and DCI. CSL has also partnered with Techcross Inc. for technical support, engineering, service support and sharing of information in relation to the Ballast Water Treatment System (BWTS) products.

Key investment positives

One of India's leading public sector shipyards catering to both commercial and defence clients with a multitude of offerings

CSL was the largest public sector shipyard in India in terms of dock capacity, as of March 31,2015, according to CRISIL Report. The company's ship repair dock is one of the largest in India and enables it to accommodate vessels with a maximum capacity of 125,000 DWT. In the past two decades, the company has built and delivered vessels across broad classifications including bulk carriers, tankers, platform supply vessels and anchor handling tug supply vessels. CSL is currently building India's first Indigenous Aircraft Carrier (IAC) for the Indian Navy. CSL has also grown its ship repair operations and is the only commercial shipyard to have undertaken repair work of Indian Navy's aircraft carriers, the INS Viraat and INS Vikramaditya. CSL's diversified offerings to the Indian clients engaged in the defence sector and to clients engaged in the commercial sector worldwide has allowed it to adapt to cyclical fluctuations of its industry. CSL's diverse experience and multiple offerings put it in a good position to benefit from the recent Make in India initiative of GoI, from which a steady pipeline of future orders and opportunities is expected.

Shareholding pattern

Particulars	Pre-issue		Post-issue	
	No. of shares	%	No of shares	%
Promoters	11,32,80,000	100.0	10,19,52,000	75.0
Institutions			1,65,80,000	12.2
Non-Institutions			49,74,000	3.7
Public			1,24,30,000	9.1
Total	**11,32,80,000**	**100.0**	**13,59,36,000**	**100.0**

Breakdown of average operating revenue of the past five fiscals

Activity	Defence sector clients (%)	Commercial clients (%)
Shipbuilding	69.44	12.68
Ship repair	10.42	6.94
Other operating revenue	0.48	0.04

Source: RHP

Expansion of capabilities through proposed dry dock and international ship repair facility

CSL is building a dry dock at an estimated cost of Rs.1,799 crore. The length of the dry dock will be greater than the length of the company's existing docks. The large size of its proposed dry dock will enable it to build and repair ships of higher capacity and large naval vessels such as aircraft carriers. CSL has entered into an agreement for development and operation of an international ship repair facility (ISRF) with Cochin Port Trust. The ISRF is to be built at an estimated investment of Rs.969 crore. For the ISRF, it has leased ~8.12 hectares of land and 15 hectares of water body from CoPT for a period of 30 years. Once development of dry dock and ISRF is complete, CSL believes the new facilities will expand its existing capacities significantly and help it to build and repair a broader variety of vessels.

GoI's policy initiatives to help build a strong order book

GoI's policy initiatives such as granting infrastructure status to shipbuilding, granting right of first refusal to Indian shipyards for shipbuilding and ship repair work of the Indian PSUs and support through the new financial assistance scheme are expected to provide a steady pipeline of orders and become key growth drivers. The GoI also plans to promote inland water transportation and coastal shipping. This will present several opportunities, including building high-speed ferry crafts, dredgers, ropax vessels and large capacity passenger ships. This will create demand for shipbuilding and ship repair services, which CSL believes is well equipped to deliver. CSL is also well positioned to take advantage of future orders placed by the Indian Navy and other Indian PSUs, being one of the few commercial shipyards to have won defence orders and deliver successfully on those mandates.

Continuous profits leading to robust financial performance

CSL is a profitable and dividend paying shipyard. CSL's total income and PAT have increased at CAGRs of 15.3% and 112.3%, respectively, during FY2015-FY2017. Additionally, it has continuously delivered positive RoE margins over the past five fiscals. The company has paid dividends to its shareholders at rates of 15%, 15%, 15% and 76.5% in FY2013, FY2014, FY2015 and FY2016, respectively, and has declared dividend of 89.7% for FY2017. As of June 30, 2017, its total cash and bank balance stood at Rs.2,003 crore, while it had fund-based indebtedness in the form of tax-free infrastructure bonds amounting to Rs.123 crore. The strength in terms of liquidity and indebtedness provides it to stay invested in its business and to consistently pay its suppliers on time and benefit from supplier goodwill.

Led by dedicated board and long serving and experienced senior management

CSL's key management staff has, on an average, more than 25 years experience in the industry and has been with the company for an average of two decades. The organisational culture, experienced board and senior management have been instrumental in helping CSL to achieve a low-cost structure, continuous profit margins, efficient operations, short delivery schedules, relatively lower attrition and fewer employee disputes. The company has a large pool of experienced naval architects, engineers and draftsmen.

Valuation

The listed private sector shipyard companies such as Reliance Defence and Engineering, ABG Shipyard and Bharati Defence and Infrastructure have been under financial stress, showing consolidated net loss during FY2016-FY2017. Further, ABG Shipyard and Bharati Defence reported negative net worth in FY2016, while financials for FY2017 have not been publicly available. Consequently, CSL is not comparable with listed private sector shipyard companies. CSL is expected to be available at 18.8x P/E multiple (EPS calculated on post issue number of shares) and 2.9x P/B on FY2017 financials at the upper price band of Rs.432. We believe the valuation factors in CSL's consistent profitability, relatively high return ratios, stronger balance sheet, capacity expansion plans and competitive advantage in catering India's defence sector.

Comparison with listed industry peers for FY2017

Companies	EPS (Rs.)	NAV (Rs. per share)	P/E (x)	RoNW (%)
CSL*	23.0	149.4	18.8	15.4
Reliance Defence and Engineering#	-7.8	19.6	NA	-39.9
ABG Shipyard#	-686.6	-587.3	NA	NA
Bharati Defence and Infrastructure#	-438.9	-673.3	NA	NA

*Standalone financials, Ratios calculated on post issue number of shares #P/E and RoNW not applicable due to negative net profit and negative net worth, Financial information of both ABG Shipyard and Bharati Defence and Infrastructure pertain to FY2016

Key risk

Dependency on global economic conditions

The commercial shipbuilding industry is highly cyclical in nature and is sensitive to industries such as oil, natural gas, shipping, transportation and other trade-related industries. Any deterioration in global economic conditions as well as downward trends in trade-related industries could have material, adverse effect on its business, financial condition, results of operations and prospects.

Dependency on few of its major customers

CSL's top two customers accounted for 82.4%, 89.9% and 84.6% of its revenue in FY2015, FY2016 and FY2017, respectively. If any of CSL's major customers ceases to have business dealings with it and it is unable to secure new orders from other sources, the company's business and prospects will be adversely affected.

Delay or cost overrun in expansion

Any delay or cost overruns in its proposed dry dock or international ship repair facility may have a detrimental impact on CSL's growth prospects.

Financials

Profit & loss account Rs cr

Particulars	FY2013	FY2014	FY2015	FY2016	FY2017
Revenue	**1,680**	**1,798**	**1,583**	**1,990**	**2,059**
Y-o-Y growth (%)	-	7.0	(11.9)	25.7	3.5
EBITDA	**352**	**417**	**89**	**392**	**380**
EBITDA margin (%)	20.9	23.2	5.6	19.7	18.5
Other income	87	61	77	107	149
Depreciation	19	25	38	37	39
Interest	23	19	18	12	11
PBT	**397**	**433**	**110**	**450**	**480**
Tax	131	151	41	158	168
PAT	**266**	**282**	**69**	**292**	**312**

Balance sheet Rs cr

Particulars	FY2013	FY2014	FY2015	FY2016	FY2017
Share capital	113	113	113	113	113
Reserves and surplus	1,112	1,376	1,441	1,711	1,918
Total equity	1,225	1,490	1,554	1,824	2,031
Borrowings	-	334	123	123	123
Provisions	346	380	248	234	232
Trade payables	143	175	171	210	161
Other current liabilities	684	606	793	955	767
Other long term liabilities	3	3	3	3	3
Total liabilities	**2,401**	**2,987**	**2,891**	**3,349**	**3,316**
Fixed assets	378	305	302	321	357
Intangible assets	0	73	81	74	68
Deferred Tax Asset	16	16	24	32	24
loans and advances	70	206	2	167	2
Inventories	355	396	303	232	186
Trade receivables	684	1,203	612	486	307
Cash and bank balances	704	556	1,419	1,820	1,991
Other current assets	130	164	113	180	303
Other Assets	62	68	35	37	78
Total assets	**2,401**	**2,987**	**2,891**	**3,349**	**3,316**

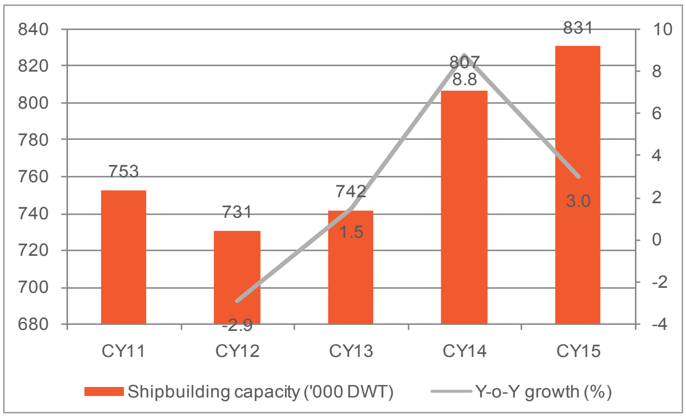
About the industry

Indian shipbuilding industry

The Indian shipbuilding industry can be divided into three segments.

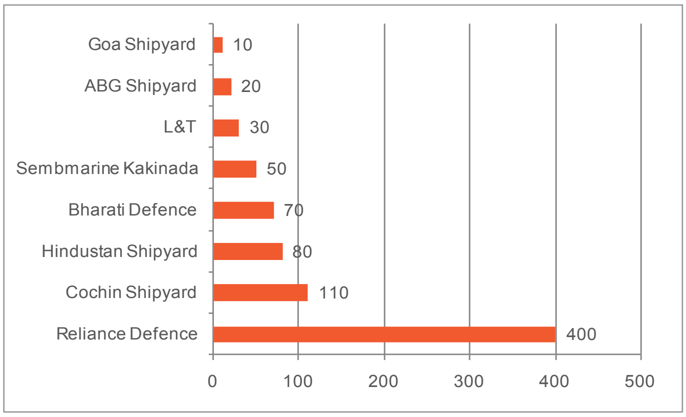
- Public sector shipyards: CSL, Hooghly Dock and Port Engineers, which primarily build merchant class ships and naval vessels.
- Defence shipyards: Hindustan Shipyard, Mazagon Dock, Goa Shipyard and Garden Reach Shipbuilders and Engineers, which come under the purview of the Indian Ministry of Defence.
- Private sector shipyards: Bharati Defence and Infrastructure, ABG Shipyard and Reliance Defence and Engineering are publicly listed. Larsen and Toubro (L&T) is another major private sector shipyard. In addition, there are a number of smaller private shipyards building smaller ships and vessels.

Shipbuilding capacity in India ('000 DWT)



Source: RHP

Shipbuilding capacities of major shipbuilders (as of FY2015) ('000 DWT)

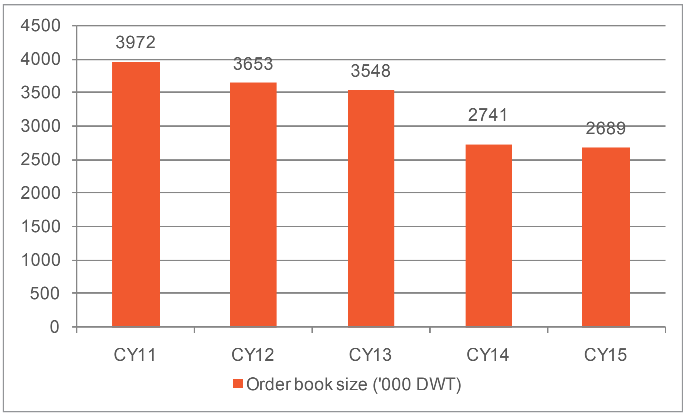


Source: RHP

Commercial order book trends

The shipbuilding order book position declined during FY2014-FY2015 due to a number of factors such as persistent excess supply and weak global trade. Execution of the order book of private shipyards remains uncertain due to the stressed financial position of major shipyards. Public sector shipyards were limited in their ability to take up large export orders due to inadequate capacity and pending orders.

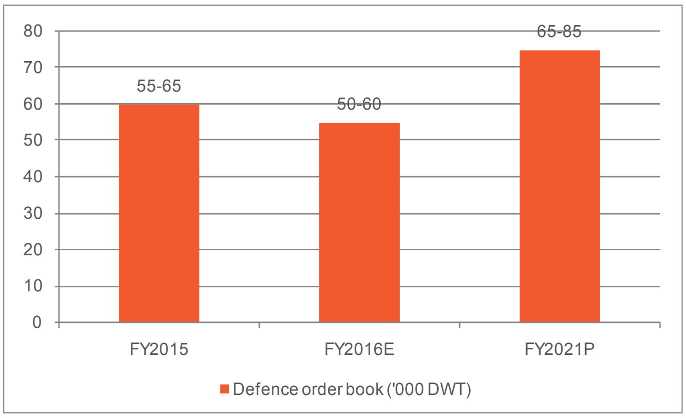
Defence order book trends



Source: RHP

Naval shipbuilding is a sub-segment of the Indian shipbuilding sector. The domestic defence shipbuilding industry primarily caters to two sub-segments, the Indian Navy and the Indian Coast Guard. The order book for the Indian shipbuilding industry is expected to receive a boost on account of the ship acquisition plans of Indian Navy and Coast Guard. Ship orders for clients engaged in the defence sector are expected to increase between FY2016 and FY2021, with the Indian Navy's and Coast Guard's ambitious plans for a 200-ship fleet each. The Indian shipbuilding industry is expected to deliver 14,000-17,000 DWT by FY2021 through the partial or full execution of orders for both the Indian Navy and Indian Coast Guard.

Defence shipbuilding order book to post at a 4-6% over FY2016E-FY2021P

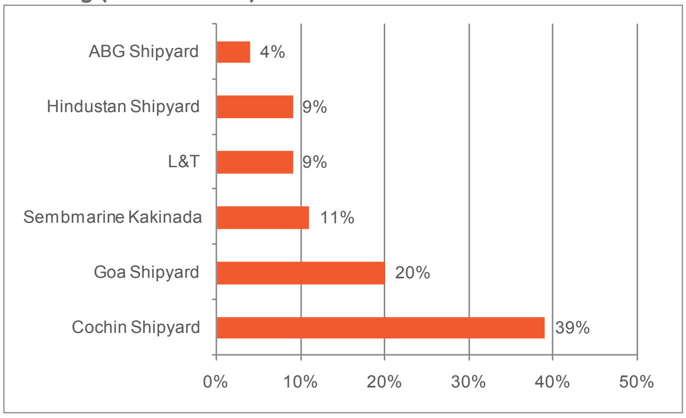


Source: RHP

Indian ship repair industry

According to the statistics of India's ship building and ship repair industry, published by the Ministry of Shipping, the total market size of the Indian ship repair industry in FY2015 was approximately Rs.504 crore. CSL is the leading shipyard company in the ship repair industry, accounting for approximately 39% of the total revenue earned in FY2015 through ship repair. CSL is followed by Goa Shipyard with a share of approximately 20% in revenue earned in FY2015 through ship repair. Private sector shipyards in this segment are Sembmarine Kakinada, L&T and ABG Shipyard. In terms of market size, share of the public sector remained higher than the private sector's share from FY2011 to FY2015. The number of ships repaired by public and private sectors increased at a CAGR of 18% and 52%, respectively, during this period.

Market share of major players in the Indian ship repairing industry (as of FY2015)



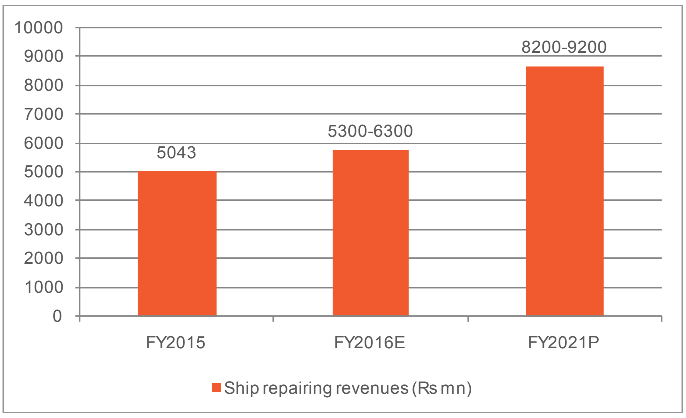
Source: RHP

Future outlook of the ship repair industry

The ship repair industry is expected to report a CAGR of 8%-10% between FY2016 and FY2021. Indian ship repair yards will be driven by greater focus on diversifying their revenue streams to withstand the slowdown in ship building.

Indian yards are expected to benefit from the increasing strength of the Indian Navy and the Coast Guard's operational and support fleet, which will drive the repairs business. Moreover, higher indigenisation in ships for clients engaged in the defence sector is expected to augment the revenue per refit and repair, driving growth and increasing the proportion of defence repairs over the next five years. Revenue generated through repairs of foreign vessels is also expected to improve in the wake of service tax exemptions granted by the Central Government in 2014 and a reduction of central excise duty on capital goods raw materials and spares used for the repair of ocean going vessels. Indian shipyards are facing increasing competition from foreign shipyards as their shipbuilding capacities remain underutilised. Also, major Indian shipyards are sceptical about taking in foreign vessels, as the average ticket sizes are lower despite similar capacity requirements.

Size of the ship repairing market



Source: RHP

Sharekhan Stock Ideas

Automobiles
Apollo Tyres
Ashok Leyland
Bajaj Auto
Gabriel Industries
Hero MotoCorp
M&M
Maruti Suzuki
Rico Auto Industries
TVS Motor

Banks & Finance
Axis (UTI) Bank
Bajaj Finance
Bajaj Finserv
Bank of Baroda
Bank of India
Capital First
Federal Bank
HDFC
HDFC Bank
ICICI Bank
LIC Housing Finance
PTC India Financial Services
Punjab National Bank
SBI
Union Bank of India
Yes Bank

Consumer goods
Britannia
Emami
GSK Consumers
Godrej Consumer Products
Hindustan Unilever
ITC
Jyothy Laboratories
Marico
Zydus Wellness

IT / IT services
Firstsource Soluation
HCL Technologies
Infosys
Persistent Systems
Tata Consultancy Services
Wipro

Capital goods / Power
Bharat Heavy Electricals
CESC
CG Power & Industrial Solutions
Finolex Cable
Greaves Cotton
Kalpataru Power Transmission
KEC International
PTC India
Skipper
Thermax
Triveni Turbine
V-Guard Industries
Va Tech Wabag

Infrastructure / Real estate
Gayatri Projects
ITNL
IRB Infra
Jaiprakash Associates
Larsen & Toubro
NBCC (India)
Sadbhav Engineering

Oil & gas
Oil India
Reliance Ind
Selan Exploration Technology

Pharmaceuticals
Aurobindo Pharma
Cipla
Cadila Healthcare
Divi's Labs
Glenmark Pharmaceuticals
Lupin
Sun Pharmaceutical Industries
Torrent Pharma

Building materials
Grasim
The Ramco Cements
Shree Cement
UltraTech Cement

Discretionary consumption
Arvind Ltd
Century Plyboards (India)
Cox and Kings
Inox Leisure
Info Edge (India)
KKCL
Orbit Exports
Relaxo Footwear
Thomas Cook India
Wonderla Holidays
Zee Entertainment

Diversified / Miscellaneous
Aditya Birla Nuvo
Bajaj Holdings
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