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Top picks and view on Indian equities during continuous rupee depreciation era.. Sep. 01, 2018

The Indian economy grew 8.2 percent in April-June this year, the highest in two years, amid signs that households are buying more and companies are adding capacities, shrugging off the disorderly effects of the twin shocks of demonetisation and the goods and services tax (GST). Domestic air passenger traffic, robust rail freight movement, rising sales growth of passenger vehicles and strong consumer durables sales also point to a turnaround in the greater household spending. Gross Fixed Capital Formation (GFCF), a useful metric to measure corporate investment activity, grew 10.0 percent in April-June. The agriculture sector grew 5.3 percent, from 3 percent in the same period last year, largely reflecting a strong Rabi or winter sown harvest. The monsoon rains, critical for the summer-sown kharif crop, has been slightly below normal this year so far, particularly in the grain bowl states in north India, but the shortfall isn't alarming enough to pull down growth in the broader economy.

India also cemented its status as the world's fastest growing major economy, ahead of China, which grew 6.7 percent in April-June 2018. At the current pace, India looks set to become the world's fifth largest economy, ahead of the United Kingdom.

According to latest World Bank data, India edged past France to become the world's sixth largest economy. India's GDP stood at USD 2.597 trillion (Rs 178 lakh crore) in 2017 in current prices in market exchange rates, ahead of France whose GDP stood at USD 2.582 trillion (Rs 177 lakh crore) in 2017.

Despite GDP showing good strength, the perils like Rupee trading at record low against the dollar and high crude prices can have a huge bearing on the Fiscal Deficit which can eventually dent market sentiments. We believe markets may come under pressure due to sliding rupee and burgeoning fiscal deficit. We recommend a cautious approach. Going ahead, we believe, progress of ongoing monsoons, rupee movement against the dollar, volatility in oil prices, trade war tensions, US Fed meeting on rate hike will keep domestic bourses volatile. We believe that the investors can have a stock specific approach. We still believe that there is significant value in midcaps after the recent correction post implementation of ASM and announcement of LTCG in Union Budget 2018-19. Midcap stocks did show some signs of bottoming out in August but it will be difficult to say that the pain is over and stock selection will be the key. With regards to rupee hitting record low against the dollar we believe IT, Pharma, textile and speciality chemicals will be beneficial. The rupee fall will be favourable for ONGC and Oil India as they sell crude to oil marketing companies in dollar terms. Hence, HPCL, BPCL and IOC will be impacted in margin terms as they buy oil in dollars. Even some of metals, power and cement companies which are dependent on coal import will also be impacted. Importers will be badly hit due to this currency war. Companies which have high external commercial borrowings will, too, get impacted, which include telecom sector as well.

Cholamandalam Investment and Finance Company Ltd.

CMP: Rs. 1466, FV: Rs. 10, Target Price: Rs. 1,905, Upside: 30%

The company is part of the Murugappa Group – founded in 1900, one of India's leading business conglomerates with 28 businesses including 8 listed companies and workforce of 40,000 employees. The Company operates from 883 branches across 27 states. Cholamandalam Investments is a strong play on the uptick on commercial vehicles cycle as its loan book is dominated by CV financing. The company boasts of a robust operating profile with total AUM of Rs. 451 bn as on June 2018 with Net NPA of 1.71 percent and ROA of 4 percent, operating income witnessed a CAGR of 14% over FY14-18.

In Q1FY19, the revival in Commercial Vehicle business cycle was witnessed in the robust disbursement in vehicle Finance business which registered growth of 48 percent on yoy basis to ~Rs. 5,665 crores. HCV and LCV continued to show strong growth, complemented by used vehicles. On recent change in Axle norms, the management remains confident of minimal impact on demand however considering company's higher exposure towards new MHCV, we may see some demand contraction.

Home Equity business saw a yoy growth of 27 percent in disbursement at ~Rs939cr. Aggregate disbursements for the quarter witnessed a growth of 45 percent at ~Rs7,014cr.

Assets under management clocked a growth of 30% in Q1FY19 to Rs. 46,663cr. The management sounds optimistic for strong AUM growth going ahead. NIM in Q1FY19 declined by 50 bps on yoy basis to 7.2% owing to IND AS implementation as loan origination fees spread over to life of assets instead of upfront recognition. Similarly, Opex witnessed a sequential decline as costs involved with loan origination has also been amortized over life of asset. Additionally as overall cost of funds heading northwards (especially for shorter duration liabilities), we expect some pressure on margins to stay in near term. Capital Adequacy Ratio (CAR) of the company as of June 30, 2018, stood at 18.15% as against the regulatory requirement of 15%. Its PCR for the quarter stood at 42.72%. Cost/Income ratio declined by 240 bps on yoy basis to touch 32.5 percent in Q1FY19. ROE stood at 21.8 percent in Q1FY19.

During FY18, India Ratings and CARE have upgraded long-term debt rating from AA to AA+. Return on equity stood at 20.78 percent in FY18. The company is consistently profit making and dividend paying company since 1979 with a strong track record of dividends to shareholders. It operates from around 873 branches across India with assets under management above Rs 42,000 crore. At CMP of Rs. 1,466, the stock trades at a P/BV of 4.45x at FY18 Book Value of Rs. 329. Considering Q1FY19 results and the above factors, we recommend a "BUY" with a target price of Rs. 1905, an upside of 30 percent. (P/BV of 4.45x on estimated FY19 Book Value).

Oil India Ltd.

CMP: Rs. 213, FV: Rs. 10, Target Price: Rs. 250, Upside: 17%

The Company is present in oil & gas sector since last 6 decades. It owns and operates a fully -automated cross country crude oil pipeline. The Company became a Public Sector Undertaking in 1981. GoI ownership stands at 66.13% as on June 2018 and was awarded 'Navratna' status in 2010.The Company has strong reserve base which is as follows: Reserve Replacement Ratio (Dom) consistently > 100%. 2P reserves (Dom): Oil - 78.67 MMT, Gas – 127.59 BCM. 2P reserves (Overseas): Oil-38.06 MMT, Gas-6.90 BCM

In Q1FY19, Oil India reported decent set of numbers. The Company reported a 56 per cent jump in its April-June quarter net profit on back of higher oil prices. Net profit in the first quarter of current fiscal rose to Rs 703.22 crore, from Rs 450.24 crore, or, in the same period of previous financial year. Revenue from operations rose by about 45 per cent to Rs 3,390.46 crore.

Crude Oil production for Q1FY19 stood at 0.844 MMT which is same to the crude oil production during Q1FY18 although realization improved. Crude Oil price realisation improved by US$23.59/BBl to US$ 72.00/BBl in Q1FY19 as compared to US$48.41/BBl during Q1FY18. Natural gas production during Q1FY19 declined by 3.87% to 696 MMSCM as compared to 724 MMSCM during Q1FY18 owing to short upliftment by certain consumers.

Oil India in consortium with Assam Gas Company & GAIL Gas Ltd., has been allotted two geographical areas, namely Cachar, Hailakandi & Karimganj Districts and Kamrup & Kamrup Metropolitan Districts in the state of Assam in the recently concluded 9th round of City Gas Distribution (CGD) bidding by PNGRB.

The Company reported whopping increase in PAT by 72% to Rs.2,668 crore in FY 18 from Rs.1,549 crore in FY 17. The Company offers high dividend yield of 7.04 percent return to its equity shareholders.

The Company has an aspiration to be an international E&P player with operations at scale in at least two geographical clusters outside India, significantly higher production, reserves and cash flows while being known globally for its capabilities to extract value from mature assets. The stock price has seen decent correction after making peak in January 2018 despite a rise of 5% increase in crude oil prices owing to subsidy burden concern. We believe current share price has discounted the worst case scenario. At CMP, the stock trades at a P/E of 9x at FY18 EPS of Rs. 23.5. We recommend a “BUY” with a target price of R. 250 (9x at estimated FY19 EPS of Rs. 28).

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