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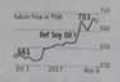
The Smart Investor

QUICK TAKE: REFINED SOY OIL TO REMAIN FIRM



Refined soy oil prices increased nine per cent in the past month on the NCDEX. Analysts say prices will remain firm in the medium term, as crude palm oil prices are rising in Malaysia. Palm crop is expected to be lower in Malaysia due to La Niña and a dry spell in Brazil

TSI P2

TATA MOTORS NET SOARS THREEFOLD TO ₹2,502 CR

Rating downgrades still outpace upgrades

Credit ratio hits 5-year low of 0.97 in the first half of 2017-18

PAVAN BURUGULA
Mumbai, 9 November

India Inc's credit health has further deteriorated in the current financial year (FY18), if rating action is to go by. The credit ratio — number of upgrades to downgrades of debt paper — is at a five-year low of 0.97. In the first six months of the current financial year, rating agencies have upgraded 189 debt papers and downgraded 195.

Debt worth nearly ₹2.57 lakh has been downgraded in FY18, which is 1.5 times that of FY17's, show data provided by the Securities and Exchange Board of India (Sebi). In value terms, FY18 is already the second worst year, after FY16.Experts say subdued earnings and disruptions such as demonetisation and the goods and services tax (GST) have hit the cash flows of India Inc. Earnings growth has largely been flat in the past three years. Companies have reported an average eight per cent growth in profits for the just-concluded September quarter. Analysts say revival in the earnings cycle is at least two quarters away.

Another reason behind the surge in downgrades is low capacity utilisation. Between 2010 and 2013, manufacturing companies spent heavily on capacity building, anticipating a surge in demand as the economy was expected to embark upon a high growth trajectory. However, a fall in global commodity prices with less than anticipated macroeconomic growth spoilt the plan.

"Capacity utilisation has not picked up and important sectors such as infrastructure and cement are not doing well. Even the scenario in telecom and allied sectors don't look great after the disruption created by Reliance Jio. Introduction of GST has also hit the earnings of small and mid-level companies. To summarise, demand and cash flows are looking good only in a handful of sectors," said G Chokkalingam, founder and managing director, Equinomics Research & Advisory.

Although the current downgrade cycle started in FY16, the sector-wise composition has changed significantly in two years. Initially, the cycle was led by metal and commodity-related companies, as the collapse in global commodity prices induced stress. Now, banks are in the forefront on downgrades. The sector has, in the past few years, been hit by a sharp increase in non-performing assets. Lenders have become cautious, leading to a fall in credit growth among public sector banks.

The current downgrade cycle is nearing a trough, analysts say. The impact of one-time disruptions such as GST and demonetisation is fading, and improving macroeconomic indicators could improve the credit health, they say. Rating agencies say low interest rates, stable operating cycles and improving domestic demand are expected to ease the stress on credit health.

"We expect growth to be consumption-led because of a near-normal monsoon, softer interest rates and inflation. Implementation of the Pay Commission recommendation by states, and remnants of pent-up demand that were postponed due to demonetisation could also be tailwinds," said Pawan Agrawal, chief analytical officer, CRISIL.

Also, economic growth could improve in the next few quarters, as the government steps up spending. The current export numbers suggest a recovery in global demand, especially in developed markets.

Analysts remain bullish on the consumption and automobile sectors, as these are expected to register double-digit annual growth for the next two-three years. The key concern has been real estate, where analysts are expecting declining sales and large unsold inventory.

DOWNGRADE CYCLE CONTINUES

Debt worth ₹2.5 lakh crore downgraded during FY18

Year	Downgrades		Upgrades		Credit ratio
	Number	Amount	Number	Amount	
2008-09	251	1,60,021	36	17,033	0.14
2009-10	324	1,31,668	197	61,052	0.61
2010-11	310	28,203	743	1,57,395	2.40
2011-12	650	1,35,515	696	1,01,523	1.07
2012-13	904	2,19,321	463	28,624	0.51
2013-14	231	1,02,385	220	46,606	0.95
2014-15	206	1,03,203	464	1,87,443	2.25
2015-16	352	4,11,977	357	97,275	1.01
2016-17	189	1,77,620	368	79,325	1.95
2017-18*	195	2,56,946	189	71,492	0.97

*As of September; amount in ₹ crore
Source: Sebi

Sebi mulls 'out-of-the-box' approach for effective corporate governance

SHRIMI CHOUDHARY
Mumbai, 9 November

Sebi Chairman Ajay Tyagi

Capital market regulator Securities and Exchange Board of India (Sebi) is exploring "out of the box" measures to improve corporate governance standards at India Inc. Speaking at a corporate governance summit, 'Gatekeepers of Governance', Sebi Chairman Ajay Tyagi said, "The need of the hour is to have a back-to-basics reconceptualisation of what sound corporate governance means."

To have an effective enforcement mechanism, the Sebi will have to do some out-of-the-box thinking, he said, adding that not just shareholders, but even the other stakeholders can act as change agents. The move towards a "stewardship code" could be a good step in this direction, Tyagi said.

At present, there is no specific provision for such a code under the securities norms. For mutual funds, some stewardship principles have been adopted, such as on voting and conflict of interest. In March, the Insurance Regulatory and Development Authority of India (Irdai) issued a stewardship code for companies in its ambit.

Citing the World Bank's Ease of Doing Business report, where India's rank in protection of minority shareholders improved to the fourth to the 13th, he said "effective implementation of stewardship principles" by all institutional investors may lead to further improvement in India's current ranking in the "protection of minority shareholders".

Sebi's whole-time member G Mahalingam said, "The important dilemma we (Sebi) face is ease of doing business versus protection of investors... We need to resolve this dilemma in favour of ease of doing business (and) less in favour of protecting interests of investors hoping that overall shareholders' democracy in a company would ensure protection of minority shareholders."

Experts believe the stewardship code will make it a formal mandate for institutional investors to play a stewardship role, rather than remain silent spectators with respect to the affairs of their investee companies.

His remarks come at a time when an expert panel constituted by the Sebi has proposed changes to the corporate governance structure for listed companies, including having a common stewardship code for all institutional investors.

He also cited various examples, where renowned companies worldwide commanded a premium of anywhere between 10 per cent and 40 per cent over their not-so-well-governed counterparts.

"Numerous studies have also indicated that the payoff from good corporate governance manifests both in the operating results of publicly listed companies as well as the market capitalisation of such companies," he said.

Tyagi also called for "equitable balance of power" between shareholder directors and independent directors.

"This could involve treading a very fine line but nevertheless, one may have to see that the balance of power or accountability is not tilted in the favour of one at the cost of the other, which may compromise the effective functioning of the board," he said.

HDFC Life IPO subscribed 4.8 times

SAMIE MODAK
Mumbai, 9 November

HDFC Standard Life Insurance Company's ₹8,700-crore initial public offering (IPO) — the largest by a private sector firm in nearly a decade — was subscribed five times on Thursday, the last day of the offering. The IPO saw bids worth ₹30,827 crore, of which more than 80 per cent came from qualified institutional buyers (QIBs). The institutional investor category saw 16 times more demand than shares on offer.

Barring for the QIB portion, most other categories saw a lukewarm response. The retail portion was subscribed 80 per cent, with some bids yet to be uploaded. The high net worth individual (HNI) portion was subscribed 2.3 times.

Market players say poor post-listing performance of insurance companies that came out with offers in recent months impacted small investors' sentiment towards the IPO. Shares of life insurer SBI Life and reinsurance company GIC Re, both of whom made their stock market debut last month, are currently trading below their IPO price.

Analysts say companies in this space are a play on higher penetration of insurance products amid rising share of financial assets in household savings. Insurance in India is deeply under-penetrated currently. But, these benefits will only accrue in the long term, they warn.

STATUS CHECK

Barring QIBs, all other segments saw tepid response

	No. of times	Bids (₹ cr)
QIB	16.6	25,692
HNI	2.3	2,652
Retail	0.8	2,148
Employee	1.2	102
Shareholder	0.3	232
Total	4.84	30,827

Source: NSE, BSE; Data as on 5 pm; *Calculated at top-end of the price band

THE COMPASS

Sun Pharma: Taro provides some respite

Improvement in ex-Taro performance, resolution of US FDA issues key triggers

UJJVAL JAUHARI

The performance of Taro, Sun Pharma's US subsidiary, for the quarter ending September 2017 (Q2), while indicating that pricing pressure continues in the US market, has some positives. The numbers show compared to the sharp fall in sales, gross margins fell at a slower pace. Taro also saw volumes grow by one per cent for Q2 and four per cent during the first half of FY18. The company clocked some market share gains as well. While these are positives, from an investors' perspective, it may not be enough to significantly move the needle for Sun Pharma's stock.

The pricing pressure on Taro's key products continues and the company indicated price erosion in such products was at about 20-25 per cent. Net sales, thus, declined 26 per cent year-on-year (y-o-y). The positive is that gross profit margins (gross profit as percentage of sales) declined at a slower rate from 77.5 per cent in the year-ago quarter to 73.6 per cent in Q2. In fact, on a sequential basis, gross profit margins expanded 140 basis points. Analysts such as Surajit Pal of Prabhudas Lilladher, however, said this may imply one-off sales in Q2FY18. While subsequent quarterly results will provide further indication, given Taro's operating performance and if it could sustain the trend, it could rub off well the Street's sentiment.

Notably, Taro continues to invest heavily in research and development (R&D), important to drive future growth. R&D spends were up sixfold to $18 million in Q2FY18, but meant 37 per cent y-o-y decline in operating profits, as margins declined from 61.9 per cent in Q2FY17 to 52.3 per cent now.

Sarabjit Kour Nangra of Angel Broking said despite challenges, Taro's operating performance was a positive sign. The pricing and regulatory environment has led to a continuous decline in Sun's stock price (down from peak levels of ₹1,168 in April 2015 to ₹535 now). But, for long-term investors, this is an opportunity to buy such stocks, she said, adding the stock will rebound over time. Also, from here on, the pricing pressure in the US may not be that intense, analysts said. Last month, Credit Suisse had said they prefer Sun, as it has low price-erosion risk from here on, and monetisation of the specialty pipeline implies a compounded annual growth in profit of 20 per cent over FY19-22.

In the near term, the Street will be watching Sun's ex-Taro performance and progress on resolution of US FDA issues, which would help analyse if there is a reversal in the present trend of declining profits. Sun Pharma's results are scheduled for next week and the management's commentary on turnaround of Ranbaxy's business and an update on resolution of the US FDA warning letter and 483 observations on Halol plant will be keenly watched.

Stronger growth prospects to drive Bharat Forge

Growth recovery in key businesses will boost revenues and margins

RAM PRASAD SAHU

The Bharat Forge stock has been hitting its 52-week highs on expectations of stronger growth in FY18 and FY19, led by both the auto and industrial segments. Recent quarterly results, including that of the September quarter (Q2), have increased investor confidence. Most brokerages have increased their earnings estimates as well as target prices given the recovery in key segments.

While there are multiple triggers, the company's Q2 results have been the most recent. Led by a better product mix, especially industrial exports, the company reported better-than-expected performance especially at the operating profit level. Better product mix and improving leverage saw its margins come in at 30 per cent, beating estimates. Overall revenues were up 48 per cent, led by a 27 per cent improvement in volumes and higher exports. The share of the higher-margin industrial exports segment to revenues more than doubled from 12 per cent in Q2 of FY17 to 27 per cent in Q2 of FY18. The company's important non-auto customers such as Halliburton, Cummins and Caterpillar are witnessing strong growth, and given rising investments, this should rub off on suppliers such as Bharat Forge. The recovery in the shale gas segment has been sharp and rising crude oil prices should help improve revenues and margins of its customers in this segment.

The other growth engine would be auto (commercial vehicles or CV) exports, especially to the US market. After falling growth over the past couple of years, Class-8 truck order inflows improved 69 per cent year-on-year in the first seven months of FY18. Given the traction in order inflows and higher production since the start of the current fiscal year, analysts at Nomura expect Bharat Forge's CV exports to the US to grow 15 per cent in FY18 and 25 per cent in FY19. Exports form half of the company's revenues.

In the domestic segment, the company is expected to benefit from the recovery in medium and heavy commercial vehicles, given overloading restrictions. The company is increasing its supplies to existing and new customers, both in India and international markets, thus gaining share in the passenger vehicles market. Higher orders from the defence, railways and aerospace segments, which are currently small, should help increase revenues from the domestic industrial space.

The company is building a new plant in Andhra Pradesh to manufacture products based on aluminium and other metals, which are expected to help bring down the weight of vehicles, reduce emissions and improve fuel efficiency. The products would cater to the auto, engineering and aerospace segments, among other. While the prospects are bright, the stock which has gained 64 per cent over the past year, is trading at 29 times its FY19 earnings estimates. Buy on dips.

LAURUS Labs
Knowledge . Innovation . Excellence

Laurus Labs Limited

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Extract of Unaudited Consolidated Financial Results of Laurus Labs Limited for the quarter and half year ended September 30, 2017 prepared in compliance with Indian Accounting Standards

(₹ in millions)

SL. No.	Particulars	Quarter ended			Half year ended		Year ended
		30-Sep-17	30-Jun-17	30-Sep-16	30-Sep-17	30-Sep-16	31-Mar-17
		(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
1	Total Income from Operations	5,386.10	4,912.22	5,254.11	10,298.32	9,419.02	19,315.49
2	Net Profit for the period (Before tax, Exceptional and/or Extraordinary items)	696.00	551.74	658.72	1,247.74	1,005.19	2,351.95
3	Net Profit for the period before tax (After Exceptional and/or Extraordinary items)	696.00	551.74	658.72	1,247.74	1,005.19	2,351.95
4	Net Profit for the period after tax (After Exceptional and/or Extraordinary items)	487.55	389.05	482.81	876.60	739.24	1,902.76
5	Total Comprehensive Income for the period	488.46	386.08	483.24	874.54	736.38	1,897.57
6	Equity Share Capital	1,060.30	1,057.56	987.47	1,060.30	987.47	1,057.56
7	Reserves (Excluding Revaluation Reserve) as shown in the Audited Balance Sheet of the previous year						12,246.92
8	Earnings Per Share (of ₹ 10/- each)						
	1. Basic : ₹ *	4.61	3.68	5.18	8.29	9.18	20.78
	2. Diluted : ₹ *	4.58	3.66	4.88	8.24	7.47	18.79

* Not annualised for quarter and half year ended

Notes :

1. Additional information on standalone financial results for the quarter and half year ended September 30, 2017

(₹ in millions)

SL. No.	Particulars	Quarter ended			Half year ended		Year ended
		30-Sep-17	30-Jun-16	30-Sep-16	30-Sep-17	30-Sep-16	31-Mar-17
		(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
1	Total Income from Operations	5,334.81	4,854.92	5,250.70	10,189.73	9,398.13	19[illegible].17
2	Profit before tax	734.90	589.47	679.73	1,324.37	1,059.38	2,[illegible].26
3	Profit after tax	527.62	426.43	508.29	954.05	808.35	2,[illegible].65
4	Total Comprehensive Income for the period	529.36	423.48	508.60	952.84	805.07	2,[illegible]

2. The above is an extract of the detailed format of Quarterly/Half-Yearly Financial Results filed with the Stock Exchanges under Regulation 33 of the SEBI (Listing and Other Disclosure Requirements) Regulations, 2015. The full format of the Quarterly/Half-Yearly Financial Results are available on the websites of the Stock Exchanges and the Company namely www.bseindia.com, www.nseindia.com and www.lauruslabs.com
3. The Government of India introduced the Goods and Services Tax (GST) with effect from July 01, 2017. Accordingly, in compliance with Indian Accounting Standard (Ind AS) 18 - 'Revenue', Revenue from operations for the quarter ended September 30, 2017 is presented net of GST. Revenue from operations of earlier periods included Excise duty which is now subsumed in GST. Revenue from operations for the half year ended September 30, 2017 includes Excise duty up to June 30, 2017.
4. The unaudited financial results have been reviewed by the Audit Committee of the Board and approved by the Board of Directors of the Company at their respective meetings held on November 09, 2017.

By order of the Board
For Laurus Labs Limited

Place : Hyderabad
Date : November 09, 2017

Dr. Satyanarayana Chava
Whole Time Director & Chief Executive Officer