Earnings growth to be key factor driving market momentum…

Earnings growth would be the key factor driving markets from hereon. We note that with enabling fundamental factors such as a stabilised commodity base, upbeat consumption and most importantly, a favourable low base, the earnings from hereon, could witness a growth recovery in FY18E and, thus, drive the market momentum. Furthermore, factors like liquidity along with relative attractiveness of equity vs. other asset classes would continue to be other determinants driving markets from here on.

We expect domestic led sectors to do well over the next couple of years. Our top picks are reflective of the same. Furthermore, we also see pockets of opportunity for players like Wabco Industries (government's focus on emission & safety norms) and State Bank of India (gain in efficiency and market share given the merger).

Company	I-direct code	Action	Recommended Price	CMP	Market Cap	P/E (x) FY19E	RoE (%)	
EIH Ltd	EIHLIM	Buy	132	132	7559	39.0	5.1	Read More
Federal Bank	FEDBAN	Buy	93	93	15981	9.7	5.9	Read More
Gail Ltd	GAIL	Buy	395	395	33149	13.1	7.5	Read More
NCC Ltd	NAGCON	Buy	96	96	5404	16.2	7.9	Read More
State Bank of India	STABAN	Buy	286	286	239190	13.1	7.3	Read More
Wabco Industries	WABIND	Buy	6175	6175	11712	32.3	19.4	Read More

East India Hotel (EIHLIM)

- EIH has majority of its hotels in business destinations. Out of the company's total room inventory of 4752, EIH owns around 44% of rooms, of which, ~95% are at business locations. We expect revenue from these business destinations to drive the growth of the company, going ahead, led by a revival in the economic environment
- For FY16, hotel room demand growth (10.5% YoY) has outpaced supply growth (3.9% YoY). Going forward, we expect occupancy levels to improve further due to slowing down of capacity additions coupled with a rise in spending by domestic travellers. In addition, with improved tourism measures by the government, we expect the sector to see a better growth trajectory & healthy pricing in the next three to four years
- In FY19E, we expect EIH to report 22.0% YoY revenue growth led by re-opening of the Delhi property and healthy demand
- In the next three years, EIH plans to open at least six new hotels consisting of ~641 rooms. We believe EIH is in a better position on the balance sheet front (D/E of 0.2x) to fund these expansions
- Re-opening of the Delhi property and opening of six new hotels is expected to drive topline (CAGR of 14.4% over FY17E-19E) and bottomline growth (32.7% CAGR in FY17E-19E). The stock is trading at attractive valuation of 15.4x FY19E EV/EBITDA (i.e. at ₹ 3.5 crore/room)

Key Financials		FY16	FY17E	FY18E	FY19E
Net sales	₹ crore	1786.9	1679.6	1800.6	2196.7
Growth	%	7.1	(6.0)	7.2	22.0
EBITDA margins	%	21.6	19.5	20.0	21.8
PAT	₹ crore	123.3	105.7	126.4	186.2
PAT growth	%	95.3	(14.3)	19.6	47.3
P/E	x	58.9	68.7	57.4	39.0
P/BV	x	2.7	3.0	2.7	2.6
RoE	%	5.1	4.4	4.7	6.6
RoCE	%	7.8	6.7	7.0	9.7

Federal Bank (FEDBAN)

- Federal Bank is a Kerala based old private sector bank. The bank has a diversified credit book with SME (23%) & retail (40%) proportion of ~63% as on Q3FY17. Its CASA ratio of 34.7% is among the best in regional banks. The Tier I capital at ~12% is also on the higher side vs. peers
- Despite being well capitalised, the bank saw slower credit growth of ~9% in FY12-Q3FY17 to ₹ 69939 crore. This was due to asset quality issues and a conservative stance on asset growth. This impacted its RoE
- However, in the last three quarters, the bank has been on a strong growth path with advances increasing >20% YoY in first three quarters of FY17. We estimate advances will increase 25% to ₹ 91187 crore by FY18E
- The presence in Kerala enables the bank to mobilise strong NRI deposits. CASA ratio has been above 30% for last five years. This strong liability franchise allowed bank to earn relatively high NIM of ~3.2-3.3% vs. peers
- GNPA deteriorated from ₹ 821 crore in FY10 to ₹ 1952 crore or 2.77% of credit in Q3FY17. The RA was at ₹ 1453 crore (2.8% of credit). Higher slippages have been hurting earnings. However, the pace has pared down to ₹ 273 crore in Q3FY17. We factor in GNPA ratio at 2.3% by FY19E
- Factoring in higher asset growth, we estimate PAT growth of ~40% in FY17-19E. RoA is expected to cross 1% by FY19E. Thus, we expect the forward multiple to improve. Further, value unlocking of stakes in life insurance JV & NBFC subsidiary would add to valuations, going ahead

Key Financials		FY16	FY17E	FY18E	FY19E
NII	₹ crore	2,503.5	3,027.7	3,775.0	4,832.0
PPP	₹ crore	1,424.6	1,856.6	2,432.0	3,303.0
PAT	₹ crore	476.1	786.1	1164.0	1647.0
EPS	₹	2.8	4.6	6.8	9.6
P/E	x	33.4	20.2	13.7	9.7
P/ABV	x	2.2	2.1	1.9	1.6
ROA	%	0.5	0.8	1.0	1.2
ROE	%	5.9	9.1	12.4	15.7

Gail India Ltd (Gail)

- Gail (India) Ltd is India's largest gas transmission company, operating a gas pipeline network of ~11500 km with a capacity of ~240 mmscmd. The core strength of Gail lies in its pan-India presence and further pipeline expansion plan, which will enable the company to tap the growing demand for natural gas in the country. Gail's transmission volumes are expected to increase at 6.6% CAGR in FY16-19E to 112 mmscmd in FY19E, due to incremental LNG capacity coming on stream and higher demand for contracted LNG
- The positive judgment by APTEL, restoration of gas volumes and expected tariff revision for its major pipelines including HVJ pipeline are important triggers for the stock. We expect Gail's gas transmission EBIT to increase at 18.8% CAGR over FY16-19E to ₹ 3095.3 crore in FY19E
- The petchem business, which is operating at an optimal level at Pata phase 2 unit, is expected to contribute mainly on the profitability front due to lower feedstock prices. The petchem EBIT is expected at ₹ 803.4 crore in FY19 against a loss of ₹ 806.6 crore in FY16
- We expect Gail's profit to increase at 28.9% CAGR over FY16-19E to ₹ 4920.5 crore in FY19E. Stable gas transmission and trading business, turnaround in petchem operations, increasing CGD business and stable LPG/LHC make Gail a preferred choice

Key Financials		FY16	FY17E	FY18E	FY19E
Net sales	₹ crore	51914.2	47809.8	50887.0	53237.7
Growth	%	-8.5	-7.9	6.4	4.6
EBITDA margins	%	8.2%	14.0%	15.3%	15.2%
PAT	₹ crore	2298.9	4301.7	4650.9	4920.5
PAT growth	%	-24.4	87.1	8.1	5.8
P/E	x	28.0	14.9	13.8	13.1
P/BV	x	2.1	1.9	1.7	1.6
RoE	%	7.5	12.8	12.5	12.1
RoCE	%	7.6	13.0	15.2	14.8

NCC Ltd (NAGCON)

- NCC is a leading EPC player with a strong orderbook of ₹ 20,466 crore, providing strong revenue visibility over the next couple of years. Further, the company is also L1 (lowest bidder) in orders worth ~₹ 3000 crore, including a patch of Lucknow-Ballia expressway worth ~₹ 2000 crore. In terms of opportunities, the management is eyeing orders in the irrigation space from the Telangana government and building contracts from Andhra Pradesh. Further, it is also sensing strong traction in the road space and is also keen on bidding for EPC & HAM projects. Consequently, the management seems quite confident of meeting its initial order inflow guidance of ₹ 12400 crore for FY17E
- We also derive our comfort in the company due to its balance sheet strength. With asset monetisation, rights issue and improvement in working capital cycle, NCC has managed to keep its balance sheet under check (it managed to reduce its D/E to 0.5x in FY16 vs. 1x in FY14)
- We have a positive stance on the stock as it is well poised to capture huge opportunities ahead given its balance sheet position. Going ahead, we expect topline, bottomline to grow robustly at 12.6%, 15.8% CAGR to ₹ 10303.4 crore, ₹ 323.2 crore, respectively, in FY17E-19E. Currently, the stock is trading at 13.1x FY19E EPS (after adjusting for investment in subsidiaries)

Key Financials		FY16	FY17E	FY18E	FY19E
Net sales	₹ crore	8325.2	8128.3	9074.5	10303.4
Growth	%	0.3%	-2.4%	11.6%	13.5%
EBITDA margins	%	8.9%	9.0%	9.2%	9.3%
PAT	₹ crore	222.8	241.1	273.9	323.2
PAT growth	%	99%	8%	14%	18%
P/E	x	23.5	21.7	19.1	16.2
P/BV	x	1.5	1.5	1.4	1.3
RoE	%	6.5	6.7	7.2	7.9
RoCE	%	15.5	12.9	13.7	14.5

State Bank of India (STABAN)

- SBI is the largest bank in India by asset size (₹ 23 lakh crore) and has played a lead role in banking space in setting interest rate, products, etc. It has managed CASA ratio of >41% and retail deposit >80% of deposit, which is stable in nature. Its credit grew strongly in the past at 17.4% CAGR in FY09-FY14 to ₹ 1209829 crore. It has been moderating since FY15. Going ahead, with retail & better rated corporate segment in focus, credit growth may stay in line with industry at 11.5% CAGR in FY17-19E
- With the merger of five associate bank, SBI has joined the league of top 50 banks globally in terms of assets. The merged entity will have a deposit base of more than ₹ 26 lakh crore and advances of ~ ₹ 18.5 lakh crore. The total customer base of the bank will reach ~37 crore with a branch network of ~ 24,000 and nearly 59,000 ATMs. With associate banks having higher level of stressed assets, the near term performance is expected to remain muted. However, the merged entity is expected to gain market share & enjoy efficiencies of scale ahead
- Sale of non core assets (NSE stake) & stake in life & general insurance subsidiaries will remain book accretive aiding capital required for growth
- SBI has depicted strength in the current environment managing the asset quality and profitability well. Rolling our estimates to FY19E & anticipating ~30% CAGR standalone banking PAT growth in FY17-19E, we remain positive on the stock

Key Financials		FY16	FY17E	FY18E	FY19E
NII	₹ crore	56,874	57,990	59,728	67,512
PPP	₹ crore	43,250	46,128	46,766	52,854
PAT	₹ crore	9,950	10,285	14,826	17,417
EPS (₹)	₹	12.8	13.0	18.8	22.1
PE (x)	x	22.6	22.2	15.4	13.1
P/ABV (x)	x	2.5	1.8	1.6	1.6
ROA (%)	%	0.5	0.4	0.5	0.6
ROE (%)	%	7.3	6.1	7.5	8.6

Wabco India (WABIND)

- Wabco India (WIL) is one of the major beneficiaries of an improvement in M&HCV volumes, as it holds leadership position (share of ~85%) in the air braking systems. The long term growth in M&HCV volumes will be driven by 1) improving viability of fleet operators, 2) government's thrust on infrastructure development & 3) government's focus on scrappage policy. In the past, WIL has benefited from the mandatory implementation of anti-lock brake systems (ABS) on new vehicles. We believe that if ABS gets mandated for all on-road M&HCV vehicles (~25 lakh plying vehicles), WIL will have an incremental revenue potential of ₹ 3,000 crore. Also, the content per vehicle in India is at ~$500/vehicle and is lowest compared to Europe ($3200) & US ($1500). It is focusing on increasing its content per vehicle, by introducing newer systems like AMT, wiring harness, pole wheels & lift axle control system which will further drive its growth
- WIL's parent's strategy is to source from the low cost country (includes India, China, Brazil & Poland). Contribution from these low cost countries has improved from ~10% in 2000 to 44% in 2015. WIL is the preferred sourcing company (~50% of probability of getting new orders) & expects exports revenue to touch ₹ 1,000 crore in the next three to four years
- With the government focusing more on safety norms, WIL is well placed to capture this growth opportunity. Thus, we remain positive on the long term growth prospects of WIL.

Key Financials		FY16	FY17E	FY18E	FY19E
Sales	₹ crore	1838.2	2092.5	2484.4	2925.1
Growth	%	36.4	13.8	18.7	17.7
EBITDA margins	%	15.9	16.2	17.6	18.0
PAT	₹ crore	204.4	225	300.4	357.3
PAT growth	%	69.4	10.1	158.4	188.4
P/E	x	56.4	51.2	38.4	32.3
P/BV	x	10.9	9.1	7.4	6.1
RoE	%	19.4	17.8	19.4	18.9
RoCE	%	25.5	24.5	26.8	26.1

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