Company Flash

26 April 2007 | 7 pages

ABB (India) (ABB.BO)

Buy: Strong Quarter – PAT Up 69% YoY

- **1Q07 recurring PAT up 69% yoy** — ABB reported 1Q07 recurring PAT of Rs866m, up 69% yoy and 8% ahead of our estimate. Revenue acceleration, costs savings and a lower tax rate boosted PAT growth.
- **Revenues up 64%, margins expanded 112bps** — ABB 1Q07 revenues of Rs13bn (up 64% yoy) were 11% ahead of our estimate on account of faster execution of the order backlog. The company continued its focus on cost savings — reduction in staff costs and other expenses helped expand margins by 112bps during the quarter.
- **Strong growth across all divisions** — ABB's Power systems revenues grew 49% yoy, Power products revenues grew 84% yoy, Process Automation revenues grew 65% and Automation Products revenues grew 51% yoy, indicating that all businesses were seeing good momentum.
- **Record order intake in 1Q07** — ABB posted a record order intake of Rs20bn (up 43% yoy) in 1Q07 taking its order backlog to Rs42.5bn (up 59% yoy). The company received orders from power utilities, cement, steel and pulp & paper sectors during the quarter.
- **Maintain Buy/Low Risk rating** — Our target price of Rs4,400 is based on a P/E of 34.7x FY08E, derived from a ~50% premium to BHEL, in line with the premium over the last 3 years.

Buy/Low Risk	**1L**
Price (26 Apr 07)	Rs4,094.40
Target price	Rs4,400.00
Expected share price return	7.5%
Expected dividend yield	0.2%
Expected total return	**7.7%**
Market Cap	Rs173,528M
	US$4,270M

Statistical Abstract

Year to 31 Dec	Net Profit (RsM)	Diluted EPS (Rs)	EPS growth (%)	P/E (x)	P/B (x)	ROE (%)	Yield (%)
2004A	1,505	35.52	49.2	115.3	24.5	23.2	0.2
2005A	2,187	51.60	45.3	79.4	19.5	27.4	0.2
2006E	3,316	78.24	51.6	52.3	14.7	32.1	0.2
2007E	4,845	114.32	46.1	35.8	10.7	34.6	0.2
2008E	6,943	163.82	43.3	25.0	7.6	35.6	0.3

Source: Powered by dataCentral

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See Appendix A-1 for Analyst Certification and important disclosures.

[1]Citigroup Global Market India Private Limited

Figure 1. ABB India — 1Q07 Income Statement (Rs Mn)

	1QCY06	1QCY07	% Chg	1QCY07E	Remarks
Order Backlog	**26,743**	**42,596**	**59.3%**		
Order Inflow	**14,019**	**20,003**	**42.7%**		
Net Sales	**8,029**	**13,124**	**63.5%**	**11,803**	**Sales 11% ahead of CIR estimates**
(Increase)/Decrease in Stock in Trade	466	97			
Consumption of Raw materials	(6,333)	(9,848)	55.5%	(8,687)	
as a % of net sales	73.1%	74.3%		73.6%	
Staff Cost	(555)	(698)	25.7%	(707)	
as a % of net sales	6.9%	5.3%		6.0%	Reduction in staff costs helped margins
Other Expenditure	(912)	(1,394)	52.9%	(1,239)	
as a % of net sales	11.4%	10.6%		10.5%	
Total Expenditure	(7,335)	(11,843)	61.5%	(10,634)	
EBITDA	**695**	**1,282**	**84.6%**	**1,169**	
EBITDA margin%	**8.7%**	**9.8%**	**112**	**9.9%**	
Depreciation	(62)	(86)	38.8%	(74)	
EBIT	**632**	**1,196**	**89.0%**	**1,095**	
EBIT margin%	**7.9%**	**9.1%**		**9.3%**	
Interest	(2)	(10)	416.5%	(2)	
Other Income	180	152	-15.5%	185	
PBT	**810**	**1,337**	**65.1%**	**1,278**	
PBT margin%	**10.1%**	**10.2%**		**10.8%**	
Tax	(297)	(471)	58.6%	(473)	
Effective Tax Rate%	36.7%	35.2%		37.0%	Lower tax rates than expected
PAT	**513**	**866**	**68.9%**	**805**	**PAT 8% ahead of CIR estimates**
Recurring PAT margin%	6.4%	6.6%		6.8%	

Source: Company , Citigroup Investment Research

ABB (India)

Company description

ABB is a global provider of power transmission and distribution (T&D) products and automation technologies to utility and industry customers. The ABB group operates in over 100 countries and employs about 104,000 people. ABB India employs over 4000 people, has 10 manufacturing units, is a global engineering and operations centre and is a group corporate R&D facility. The company has a countrywide marketing and service presence spanning 27 marketing offices, a network of over 650 channel partners and 8 service centres. Traditionally, ABB had 2 divisions — power technologies and automation technologies. But on January 1, 2006 the ABB group was restructured into 5 divisions for better management and control, and ABB India adopted the same five-division structure.

Investment thesis

We rate ABB India Buy/Low Risk. Our rating is supported by our positive views on: i) *Power capex* in India, given GDP growth of 8%-plus, government support for adding generation capacity and a massive rural electrification programme; ii) *Industrial capex* in India, which CRISINFAC sees as increasing to Rs4,326bn in FY06-10, up 181% from Rs1,541bn in FY99-FY05; iii) *ABB India's increasing importance in the ABB Group*, with India not only a promising domestic market but also a key regional and global resource base; iv) *ABB India's access to* *parent technology;* v) *EPS growth*, being one of the highest in our Indian industrials universe at 40% over CY06-09E; vi) *RoEs* (in the 32 -36% band over the next 4 years) and *positive free cash flows.*

Valuation

Our target price for ABB of Rs4,400 is based on 34.7x FY08E EPS, and is set at ~ 50% premium to our target FY08E P/E multiple of 23x for BHEL. ABB has traded at average premium of ~ 50%+ to BHEL for the last three years, a premium that actually narrowed in CY03 – CY06, compared to CY99 – CY03, as BHEL re-rated significantly. ABB has also traded at an average premium of 85%+ to the BSE Sensex over the last three years. At our target price, ABB would trade at 26.9x CY08E EPS and 20.4x CY09E EPS.

Risks

Our quantitative risk-rating system, which tracks 260-day historical share price volatility, assigns a Medium Risk rating to ABB India. However, we believe a Low Risk rating is more appropriate given that strong power and industrial capex in India provides ABB with significantly visibility on order inflows and that ABB is India’s market leader in the power and automation space. Our Low Risk rating is also in line with that of BHEL. The key downside risks to our positive view on ABB India include the following: (a) Increased competition; (b) Slowdown in investments in generation, transmission and distribution (c) Slowdown in the industrial capex cycle; (d) Substantial increase in input prices; (e) Employee retention.

Bharat Heavy (BHEL.BO - Rs2,510.85; 1L)

Valuation

Our target price of Rs2,764 is based on a target P/E multiple of 23x FY08E EPS, assuming continued strong order inflows and strong 1QFY07-ending order backlog of Rs393bn. This should provide visibility for the next two years. Our target P/E multiple of 23x FY08E is well below the historical high of 27.1x. A 27% CAGR in earnings over FY06-09E should support these valuations. We believe that BHEL can trade at a premium to the market given its strong earnings growth vis-à-vis the relative pedestrian earning growth of the BSE Sensex companies. Alternatively, at our target price, BHEL would trade at an EV/EBITDA multiple of 14.1x FY08E.

Risks

We rate BHEL shares as Low Risk. The rating differs from the Medium Risk rating assigned by our quantitative risk rating system, which tracks 260-day historical share price volatility. We believe BHEL's current order book of Rs393bn represents nearly two years sales and provides good earnings visibility over the medium term. Risks to our target price include: 1. Delay in power sector reforms could affect order flows and earnings; 2. The sector could also be subject to regulatory uncertainties, which could affect sentiment and valuations on the stock; 3. Competitive pressures from global majors are also a concern; particularly as technology upgrades are affected. We believe it is imperative that BHEL demonstrate the ability to upgrade technology at reasonable costs for valuation ratings to sustain at current levels over the medium term; and 4. Over the short-term, investor progress on order flows does influence sentiment and delays herein could dampen sentiment. If any of these risk factors have a greater impact than we anticipate, BHEL's share price will likely have difficulty attaining our target price.

Appendix A-1

Analyst Certification

We, Venkatesh Balasubramaniam and Deepal Delivala, research analysts and the authors of this report, hereby certify that all of the views expressed in this research report accurately reflect our personal views about any and all of the subject issuer(s) or securities. We also certify that no part of our compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report.

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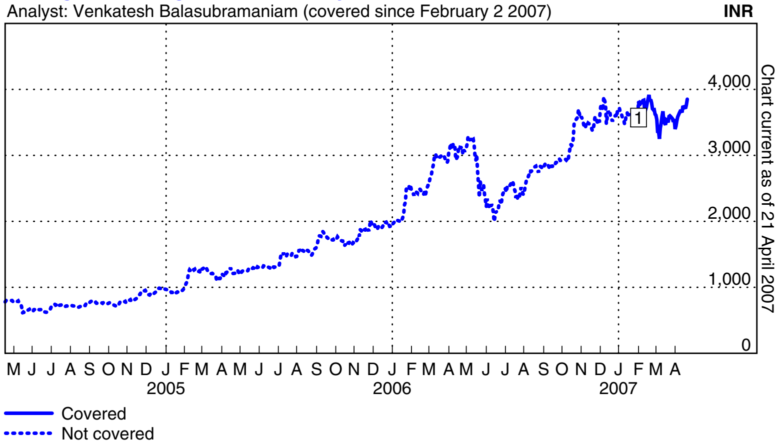
Ratings and Target Price History - Fundamental Research

Analyst: Venkatesh Balasubramaniam (covered since February 2 2007)



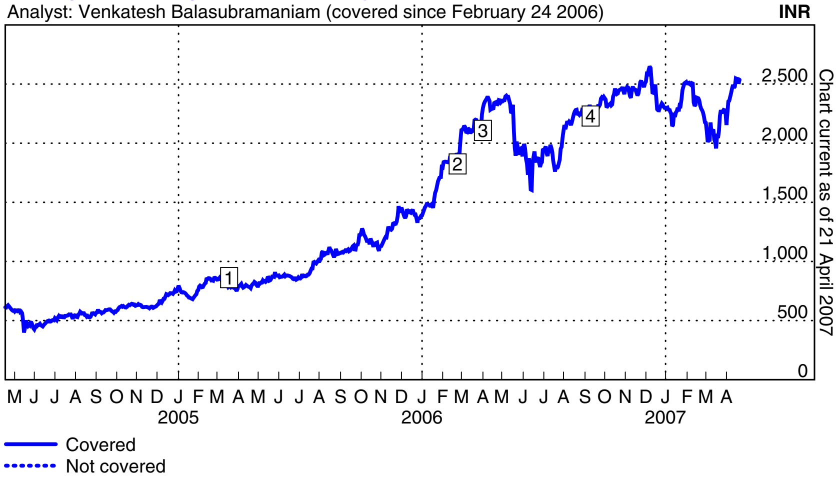
#	Date	Rating	Target Price	Closing Price
1:	1 Feb 07	1L	4,400.00	3,802.75

*Indicates change.

Bharat Heavy (BHEL.BO)

Ratings and Target Price History - Fundamental Research

Analyst: Venkatesh Balasubramaniam (covered since February 24 2006)



#	Date	Rating	Target Price	Closing Price
1:	18 Mar 05	1L	*945.00	789.90
2:	23 Feb 06	1L	*2,256.00	1,893.85
3:	3 Apr 06	1L	*2,643.00	2,298.05
4:	10 Sep 06	1L	*2,764.00	2,254.60

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