

Way2Wealth



Capital Goods Sector Outlook

*making investing simpler,
more understandable and profitable.*



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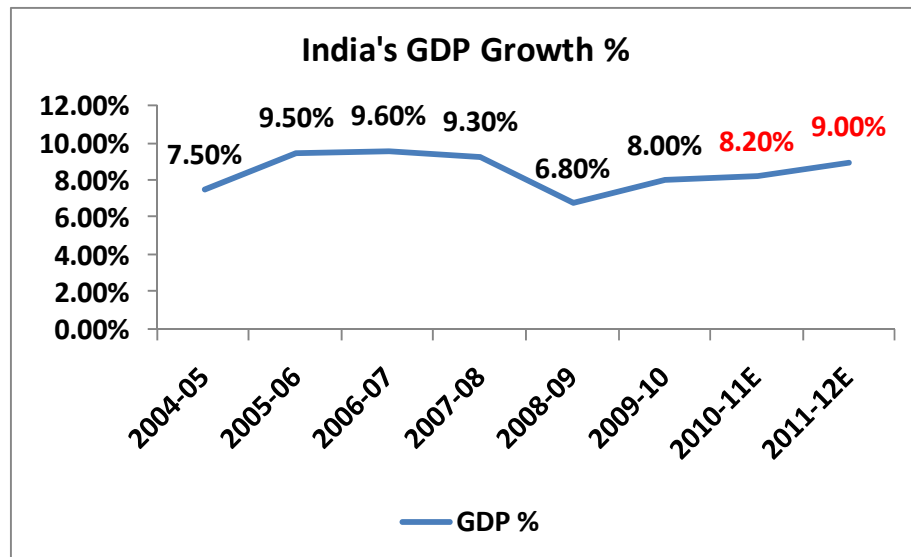
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India's GDP growth: Building Muscle

- Indian economy to grow to \$2 trillion in 2011-12
- The mass of economic activity shifts to Asia
- GDP forecasted to expand between 8.75% and 9.25% in 2011-12
- High domestic consumption and investment boom to trigger this high growth
- India would outpace China in growth
- China lowers its economic growth target to 7% over the next five years
- Prudent fiscal policy stance, openness to foreign trade and investment, increased investment in transport and energy infrastructure, and improved educational standards are India's key growth prospects

..... (Cont.)



The League Standings		
Country	GDP \$ mIn	GDP \$ trn
USA	14256	14.3
Japan	5068	5.1
China	4909	4.9
Germany	3347	3.3
France	2649	2.6
UK	2175	2.2
Italy	2113	2.1
Brazil	1572	1.6
Spain	1460	1.5
Canada	1336	1.3
India	1296	1.3

Key Drivers

- India's economy to become less dependent on outsourced services for exports
- To become more focused on manufacturing exports by growing its engineering muscle
- The growing Middle class to attract international companies to focus on consumer markets

The IIP Trend

- Industrial production to see healthy growth during 2011-13 backed by
 - Increase in consumption demand
 - Buoyancy in investment demand
- Key demand drivers:**
 - Rise in income of urban consumers
 - Higher income in hands of farmers, laborers & industrial workers
 - Lower inflation expected at 6-7% as compared to 9% inflation in FY11
 - 7-8 lac cr worth capacity additions expected in FY12 & FY13 each from power, steel & petroleum industry

% YOY chg	Jan FY11	Jan FY10	Dec FY10	YTD	YTD
				FY 2010	FY 2011
IIP	3.7	16.8	2.5	8.3	9.5
Basic	7.6	11.5	6.0	6.5	6.6
Intermediate	7.9	22.2	6.6	9.1	13.4
General					
Manufacturing	3.3	17.9	2.0	8.6	9.9
Mining	1.6	15.3	5.7	7.1	9.5
Electricity	10.5	5.6	6.0	5.3	5.6
Use based					
Capital Goods	-18.6	57.9	-9.3	12.3	16.1
Consumer Goods	11.3	0.4	3.7	7.1	5.9
Durables	23.3	28.2	18.8	21.6	23.2
Non Durables	6.9	-7.0	-1.5	1.4	0.4

11th & 12th Five year Plan

Projected Investment: 11th & 12th Plan (2006-07 prices)				
Sectors	XI Plan		XII Plan	
	Rs. Cr. (US \$ bn)	Share %	Rs. Cr. (US \$ bn)	Share %
Electricity (incl NCE)	658630 (165)	32.1	1289946 (322)	30.8
Roads & Bridges	278658 (70)	13.6	500977 (125)	12.0
Telecommunication	345134 (86)	16.8	1095550 (274)	26.2
Railways (incl MRTS)	200802 (50)	9.8	320361 (80)	7.7
Irrigation	246234 (62)	12	387808 (97)	9.3
Water Supply & Sanitation	111689 (5.4)	5.4	173730 (43)	4.2
Ports	40647 (10)	2.0	63452 (16)	1.5
Airports	36138 (9)	1.8	65656 (16)	1.6
Storage	8966 (2)	0.4	29376 (7)	0.7
Oil & Gas Pipelines	127306 (32)	6.2	258482 (65)	6.2
Total	2054205 (514)	100	4185338 (1046)	100

Projected Investment in Infrastructure		
% of GDP	XIth plan	XIIth Plan
Year 1	6.44%	9.00%
Year 2	7.18%	9.50%
Year 3	7.51%	9.90%
Year 4	7.94%	10.30%
Year 5	8.37%	10.70%
Total	7.55%	9.95%

(GDP growth assumed at 9% for 12th plan)

Key Investment opportunities

Sectors	Opportunities		
Power	<ul style="list-style-type: none"> • 62000 MW capacity to be added in the 11th plan period • 9 UMPPs to be implemented during the 11th and 12th plans • Transmission capacity augmentation through JVs for new generation 	Airports	<ul style="list-style-type: none"> • Metro Airport development through PPP route • Greenfield Airports • Concept of Merchant Airports being examined by Govt • City side development in 24 Non-metro Airports • Provision of Services within airports
Roads	<ul style="list-style-type: none"> • Investment in NHDP • State Roads program in addition 	Ports	<ul style="list-style-type: none"> • National Maritime Development Program • Development of ports • New berths on PPP basis • Gradual transition of old berths to PPP
Railways	<ul style="list-style-type: none"> • Dedicated Freight Corridors with PPP sub-projects • Container operations • Rail side warehousing • Logistics Parks • Development of Rail links to Ports • Dedicated rail links for evacuation of specific industrial items • Modernization of Railway Stations • Development of new routes 		

Demand Drivers

Industry	Growth expected
Machineries	<ul style="list-style-type: none">• Projects worth 15 lakh cr to get over by 2011-13 (mainly from the power sector)• Boilers to grow at a CAGR of 20.7% from 2011-13• Transformers to grow by 44.3% in 2011-12 & 16.2% in 2012-13• Healthy growth expected from other machineries like bearings, compressors, cranes, lifts & switchgears
Auto & auto ancillary	<ul style="list-style-type: none">• Buoyancy in production of automobiles expected to continue• Passenger car production to grow by 12.5% in 2011-12 & 13.5% in 2012-13• Commercial vehicles production to grow by 12% in 2011-12 & 8.6% in 2012-13 backed by increase in industrial production & domestic trade & faster growth in road construction
Construction equipment	<ul style="list-style-type: none">• Construction equipment industry expected to grow by 18% in 2010-11 & 21% in 2011-13• Material handling equipment expected to grow at a CAGR of 22% in 2010- 13 due to healthy demand from the infra projects

Demand Drivers

Industry	Growth expected
Metals	<ul style="list-style-type: none">• Appr. 11.4 mln tons of steel mfg capacity to come on stream in 2010-11 & 38.9 mln tons to get commissioned during 2011-13• Industry to clock a growth of 11% & 15% in 2011-12 & 12-13 resp.
Cement	<ul style="list-style-type: none">• With the construction sector to grow by 10% pa in 2011-13, cement production is expected to grow by 10.8% in 2011-12 & 11.3% in 2012-13
Construction equipment	<ul style="list-style-type: none">• Construction equipment industry expected to grow by 18% in 2010-11 & 21% in 2011-13• Material handling equipment expected to grow at a CAGR of 22% in 2010-13 due to healthy demand from the infra projects

Q3 Result Update

QUARTERLY	SALES			EBITDA			EBITDA (%)			PAT			PAT (%)	
Company	Q3FY11	Q3FY10	YoY%	Q3FY11	Q3FY10	YoY%	Q3FY11	Q3FY10	Q3FY11	Q3FY10	YoY%	Q3FY11	Q3FY10	
L&T	114,131	81,222	40.5	12,379	10,069	22.9	10.8	12.4	8,052	6,963	15.6	7.1	8.6	
BHEL	88,493	71,003	24.6	18,977	14,328	32.4	21.4	20.2	14,032	10,726	30.8	15.9	15.1	
Siemens	25,381	19,023	33.4	3,627	3,679	-1.4	14.3	19.3	2,438	2,385	2.2	9.6	12.5	
Crompton Greaves	23,970	22,464	6.7	3,402	3,200	6.3	14.2	14.2	2,328	1,996	16.6	9.7	8.9	
Bharat Electronics	13,213	11,796	12	1,710	2,477	-31	12.9	21	1,706	2,239	-23.8	12.9	19	
Voltas	10,393	9,875	5.2	763	875	-12.8	7.34	8.86	551	663	-16.9	5.3	6.71	
Blue Star	6,068	5,862	3.5	407	552	-26.3	6.7	9.4	224	336	-33.5	3.7	5.7	
Thermax	12,161	7,263	67.4	1,214	674	80.1	10	9.3	1,002	565	77.3	8.2	7.8	
Cummins	9,584	8,148	17.6	1,455	1,767	-17.7	15.2	21.7	1,389	1,482	-6.3	14.5	18.2	
Aggregate	303,393	236,656	28	43,933	37,621	17	14.50%	15.90%	31,722	27,354	16	10.5	11.6	

ORDER INTAKE	Q3FY11	Q3FY10	YoY%	9MFY11	9MFY10	YoY%
L&T	134	178	-25	495	457	8
BHEL	122	156	-22	365	371	-2
Siemens	40	52	-23	90	101	-11
Crompton Greaves	24	20	20	79	67	19
Bharat Electronics	57	NA	NA	83	55	49
Voltas	8	14	-46	35	37	-6
Blue Star	7	6	9	23	22	6
Thermax	10	14	-28	40	44	-9

9MONTHS	SALES			EBITDA			EBITDA (%)			PAT			PAT (%)	
Company	9MFY11	9MFY10	YoY%	9MFY11	9MFY10	YoY%	9MFY11	9MFY10	9MFY11	9MFY10	YoY%	9MFY11	9MFY10	
L&T	286,175	234,493	22	32,662	26,740	22.1	11.4	11.4	21,655	18,276	18.5	7.6	7.8	
BHEL	236,574	193,212	22.4	42,115	30,785	36.8	17.8	15.9	32,132	24,011	33.8	13.6	12.4	
Siemens	78,455	63,023	24.5	10,066	8,673	16.1	12.8	13.8	6,535	5,192	25.9	8.3	8.2	
Crompton Greaves	70,971	66,330	7	9,707	8,743	11	13.7	13.2	6,372	5,534	15.2	9	8.3	
Bharat Electronics	31,951	33,796	-5.5	3,420	6,498	-47.4	10.7	19.2	3,561	5,339	-33.3	11.1	15.8	
Voltas	35,059	33,016	6.2	3,047	3,092	-1.5	8.69	9.37	2,238	2,328	-3.9	6.38	7.05	
Blue Star	19,484	16,704	16.6	1,511	1,829	-17.4	7.8	10.9	977	1,190	-17.9	5	7.1	
Thermax	30,427	19,169	58.7	3,017	1,851	63	9.9	9.7	2,559	1,571	62.9	8.4	8.2	
Cummins	29,359	20,673	42	5,184	3,825	35.5	17.7	18.5	4,470	3,256	37.3	15.2	15.7	
Aggregate	818,454	680,415	20	110,729	92,036	20%	13.5	13.5	80,500	66,697	21	9.8	9.8	

ORDER BOOK	9MFY11	9MFY10	YoY%
L&T	1,149	911	26
BHEL	1,580	1,340	18
Siemens	151	136	11
Crompton Greaves	70	61	15
Bharat Electronics	164	114	44
Voltas	47	50	-6
Blue Star	21	19	10
Thermax	72	56	27
Aggregate	3,254	2,686	21

Concerns

- **Rising commodity prices**

Rise in commodity prices to dent operating margins

- **Competition**

Increasing domestic & foreign entrants in the power equipment manufacturing space to bring in low pricing power for players

- **Higher interest rates**

Rising interest rates to impact industrial & infra capex negatively thereby hampering growth for capital goods players

- **Slowdown in order inflows**

Order inflows have been weak in Q3FY11 & are expected to remain the same in Q4 with improvement happening from FY12 onwards

Factors affecting order inflows:

- Delays in financial closure
- Lack of coal linkages
- Delay in environmental clearances & deterioration in macro environment

Q4FY11 Preview

Companies	Net Sales			Operating Profit			PAT			EPS		
	W2W Estimates (Rs. Mlns)	Q4FY11W2WE	Q4FY10	% Y-o-Y	Q4FY11W2WE	Q4FY10	% Y-o-Y	Q4FY11W2WE	Q4FY10	% Y-o-Y	Q4FY11W2WE	Q4FY10
BHEL (Provisional Result)	434510	341985	27%	90160	70822	27%	60210	43106	40%	123	87.60	40%
BGR Energy	17117	16571	3%	1909	1752	9%	1138	1083	5%	15.80	15.04	5%
Thermax	13829	11715	18%	1971	1466	34%	1315	992	33%	11.03	8.32	33%
Voltas	18650	14806	26%	2072	1511	37%	1456	1369	6%	4.45	4.11	8%
McNally Bharat	6451	5624	15%	430	408	5%	237	215	10%	7.64	6.92	10%

- **BHEL** has declared its provisional result with an order inflow meeting its own guidance of Rs. 60 bn, an incremental sales growth of 27% & PAT growth of 40%.
- **BGR Energy** will be having an order inflow of close to 30-35 bn as its RRVUNL order intake has been delayed, we expect with a higher execution its Q4 will be up by 3% as in FY10 major revenues have been booked in Q4FY10 whereas for 9Ms FY11 BGR has a revenue growth of more than 133%.
- For **Thermax** we expect the momentum to continue in Q4 with its low base effect to deliver a sales growth of 18% & PAT growth of 33%.
- We expect **Voltas** to deliver better than its first 9Mths on account of higher crude prices led growth in Middle East, the AC business to deliver good volumes & the upcoming material handling segment which is expected to pick up. We are expecting a growth of 26% sales wise & a PAT growth of 6% on account of higher commodity prices.
- As the material handling sector seems to be picking up we expect **McNally** to deliver a growth of 15% sales wise & a growth of 10% in its PAT.

Top Picks

- **BHEL**
 - Robust order backlog at 1580 blns with an as on Q3FY11
 - Focused approach geared around strong execution, lean manufacturing, cost control measures along with increasing diversification
 - With measures being taken to beat competition, it remains attractively valued at its CMP of Rs. 2050 per share.
- **Voltas**
 - Strong execution in Domestic and International markets in Q4FY11,
 - Engineering Business to deliver good performance with low profit margin jobs being completed
 - Volume growth in Unitary Cooling products business to be exceptionally strong which should post strong results
 - We stay positive on Voltas
- **BGR**
 - A healthy order book of Rs. 93.17 bln gives a revenue visibility of 1.91x
 - Emerged from a small BOP player to full fledged EPC player
 - JV with Hitachi group to set up a 4,000 MW of manufacturing facility each for Boiler & Turbine sets makes it the 3rd player (after BHEL & L&T) to set up domestic facility for the entire BTG package
 - With the entry into the BTG space, we expect strong prospects for BGR and it remains a value buying opportunity at its CMP of Rs. 469 per share

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