



INDIA

CRG IN Underperform

Price 20 Oct 11 Rs142.50

12-month target Rs 117.00

Upside/Downside % -17.9

Valuation Rs 117.00

- PER

GICS sector Capital Goods

Market cap Rsm 91,425

30-day avg turnover US\$m 1.5

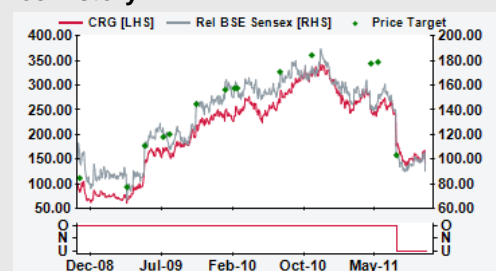
Market cap US\$m 1,860

Number shares on issue m 641.6

Investment fundamentals

Year end 31 Mar		2011A	2012E	2013E	2014E
Revenue	bn	100.1	107.7	114.8	129.2
EBIT	bn	11.5	7.5	9.3	11.3
EBIT growth	%	2.5	-35.1	25.0	21.6
Recurring profit	bn	12.7	7.6	9.7	11.8
Reported profit	bn	9.3	5.8	7.4	8.9
Adjusted profit	bn	9.7	5.8	7.4	8.9
EPS adj	Rs	15.10	9.00	11.47	13.91
EPS adj growth	%	17.5	-40.4	27.4	21.3
PER adj	x	9.4	15.8	12.4	10.2
Total DPS	Rs	2.42	1.57	2.01	2.43
Total div yield	%	1.7	1.1	1.4	1.7
ROA	%	17.2	9.8	11.3	12.4
ROE	%	33.5	16.4	18.9	20.4
EV/EBITDA	x	6.9	9.4	7.9	6.6
Net debt/equity	%	5.2	5.6	3.4	-7.3
P/BV	x	2.8	2.4	2.3	1.9

CRG IN rel BSE Sensex performance, & rec history



Note: Recommendation timeline - if not a continuous line, then there was no Macquarie coverage at the time or there was an embargo period.

Source: FactSet, Macquarie Research, October 2011
(all figures in INR unless noted)

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20 October 2011

Macquarie Capital Securities India (Pvt)

Ltd

Crompton Greaves India

Disappointment galore

Event

- Expectations of revival were belied in CRG's 2QFY12 results. India business has started facing problems and issues in overseas businesses remain unresolved. We reduce our earnings estimates by ~15% and our target price from Rs158 to Rs117. Retain Underperform.

Impact

- **Problem creeping into India business:** CRG's India power business had a 7% revenue decline (v/s 11% growth in 1QFY12). The consumer business continues to struggle with low growth of 4% and the industrial segment slowed down significantly to 9% in 2QFY12.
- **No revival yet in overseas power systems:** Contrary to expectations, the liquidation of inventories in overseas power systems has not taken place, resulting in an increase of Rs5.5bn (~50%) from FY11 levels. We note that the standalone company has been extending loans and advances to its overseas subsidiaries to help them meet their rising working capital needs.
- **Margin revival unlikely to happen in a hurry:** Competition continues to hurt India's power business (30% decline in transformer realisations since Jan'09). Interestingly, the recently won 765kV substation order from Powergrid has ~8% margins. Slow growth in the consumer business (~3% in 1HFY12) will continue to pressure margins.
- **Management maintains FY12 guidance:** Management maintains FY12 guidance of 10-12% revenue growth, with 8-10% EBITDA margin in the consolidated entity. It also plans to reduce its effective tax rate from 25% in FY11 to 15% in FY12E on an increase in R&D expenses from ~Rs1bn in FY11 to ~Rs2.5bn.
 - CRG paid Rs1bn of tax at overseas subsidiaries in 1HFY12 despite Rs3bn of losses, indicating that there is no tax offset across geographies. Even with 15% tax rate on higher R&D, FY12 tax outgoings will be at least Rs1.9bn (which has been paid in 1HFY12).

- **Downside risks to consensus estimates:** We believe there is downside risk to consensus EPS estimate of Rs11 in FY12, given that CRG clocked just Rs3.8 EPS in 1HFY12. We reduce our FY12-13E EPS by 15-16%.

Earnings and target price revision

- We cut our FY12-13E EPS estimates by 15-16%, mainly due to cuts in margins. We reduce our target price from Rs158 to Rs117 due to cut in EPS and target multiple from 15x to 13x, as uncertainty persists on the company meeting its guidance and the lower tax rate boosting its earnings.

Price catalyst

- 12-month price target: Rs117.00 based on a PER methodology.
- Catalyst: rising competition in India power and late revival in overseas power

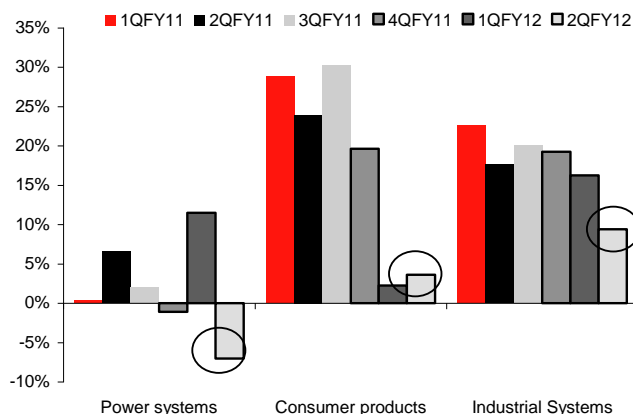
Action and recommendation

- **Investor confidence unlikely to return in a hurry:** Operating performance for CRG needs to improve significantly for investor confidence to return to the stock. We retain our Underperform and revise our TP to Rs117.

2QFY12 results – problems entering into India now

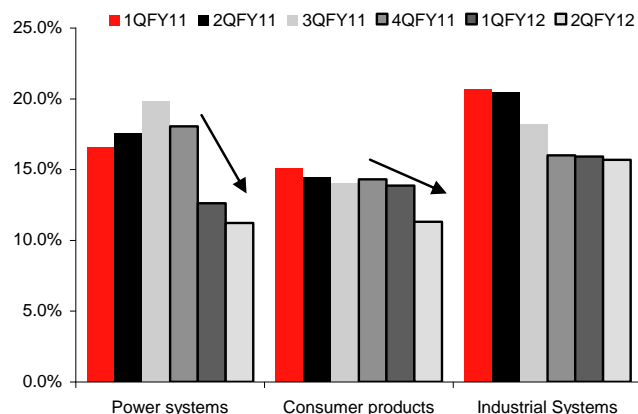
- **Sharp revenue deceleration in India business:** CRG standalone had 0% revenue growth in 2QFY12 due to a revenue decline of 7% in power systems. The consumer business continues to struggle, with low growth of 4%, while the industrial business slowed to 9% growth in 2QFY12.

Fig 1 Significant slowdown in India business...



Source: Company data, Macquarie Research, October 2011

Fig 2 ...with sharp fall in margins across segments



Source: Company data, Macquarie Research, October 2011

- **Overseas revenue growth partly aided by new subsidiaries:** Overseas revenues at Rs12.5bn were up 32% YoY. However, these numbers included Rs940mn revenue contribution (€12mn from Emotron and US\$4mn from QEI Systems). Excluding these, the revenues increased by 22% in 2QFY12.

Fig 3 CRG – 2QFY12 consolidated result snapshot

Figs in Rs mn	2QFY11	2QFY12	YoY	1QFY11	QoQ	Comments
Net Revenues	23,979	27,055	13%	24,377	11%	Revenue growth partly driven by incorporation of QEI and Emotron
EBITDA	3,332	2,260	-32%	1,819	24%	
Net Financial Cost	49	102	111%	110	-7%	
Depreciation	458	726	59%	608	20%	
Other Income	228	215	-6%	151	42%	
PBT	3,054	1,646	-46%	1,253	31%	
Tax	920	463	-50%	475	-3%	
Reported PAT	2,136	1,167	-45%	795	47%	
EBITDA margin	13.9%	8.4%	-5.5%	7.5%	0.9%	Sequential improvement in margins due to lower losses in overseas subs
Order position						
Order book	71,160	71,200	0%	70,880	0%	Order book remains largely flat
Order inflow	27,119	22,600	-17%	17,040	33%	Reclassification of 1QFY12 orders led to growth sequentially

Source: Company data, Macquarie Research, October 2011

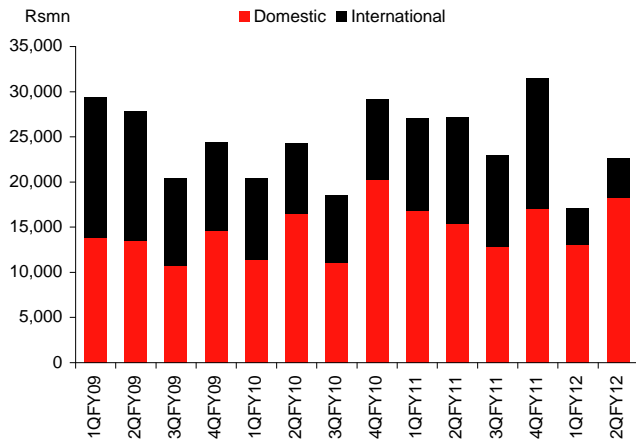
Fig 4 CRG – 2QFY12 standalone result snapshot

Figs in Rs mn	2QFY11	2QFY12	YoY	1QFY11	QoQ	Comments
Net Revenues	14,448	14,515	0%	14,688	-1%	Decline of 7% in power systems, meagre 4% growth in consumers
EBITDA	2,309	1,614	-30%	1,867	-14%	
Net Financial Cost	-7	1	-107%	14	-97%	
Depreciation	195	267	37%	286	-7%	
Other Income	193	168	-13%	157	7%	
PBT	2,314	1,515	-35%	1,723	-12%	
Tax	729	391	-46%	433	-10%	
Reported PAT	1,585	1,123	-29%	1,290	-13%	
EBITDA margin	16.0%	11.1%	-4.9%	12.7%	-1.6%	Margin dip primarily due to power systems

Source: Company data, Macquarie Research, October 2011

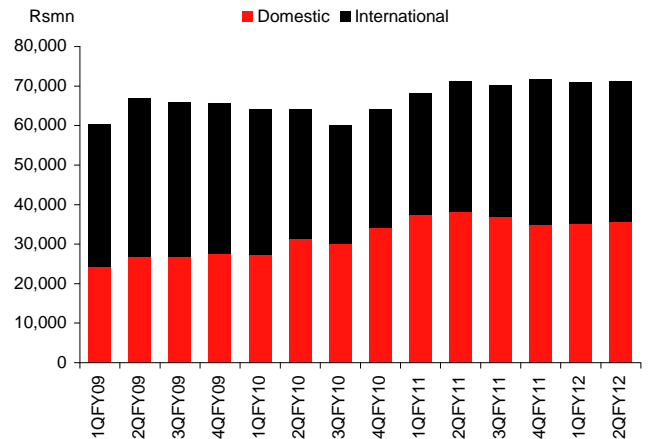
- **Inventory liquidation yet to take place:** Liquidation of power inventory in overseas subsidiaries has not yet taken place in 2QFY12. Inventories for CRG have increased by Rs5.5bn (50%) from FY11 end to 1HFY12.
- **Order inflow increases by 33% QoQ due to reclassification:** The company reported order inflows of Rs22.6bn (Rs18.3bn in power and Rs4.3bn in industrial segments) in 2QFY12. CRG indicated that 1QFY12 was Rs17bn, and not Rs22bn as reported earlier, due to an error in classification.

Fig 5 Order inflow for CRG consolidated entity



Source: Company data, Macquarie Research, October 2011

Fig 6 Order book for CRG consolidated entity

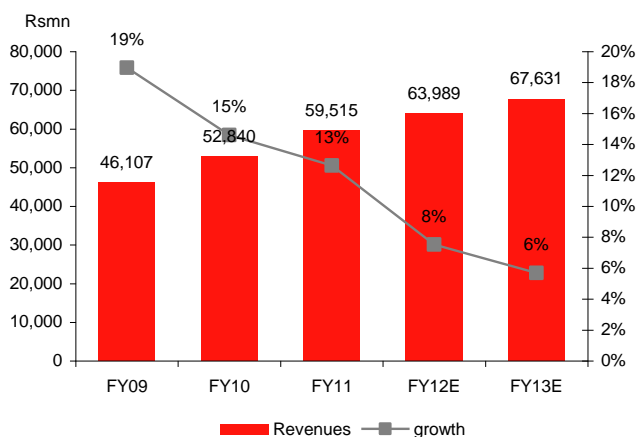


Source: Company data, Macquarie Research, October 2011

Revising our estimates downwards by 15-16%

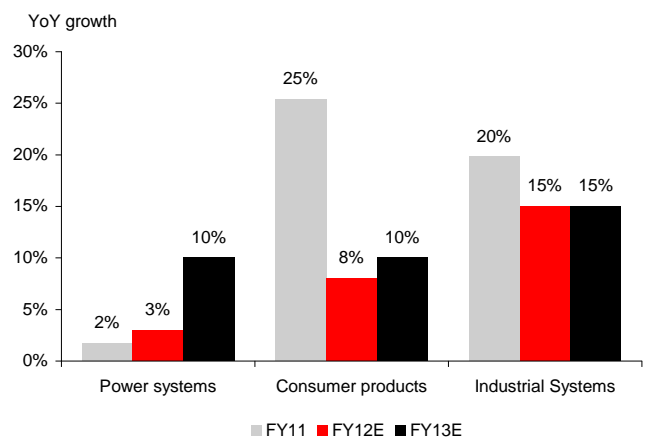
- **Reducing our revenue estimates due to slowdown in India industrial and consumers segments:** We reduce our revenue forecasts by 1.6-2% for FY12-13E to factor in slowdown in industrials segment and no pick-up in consumer segments in India. The industrial segment grew by 12% and consumer by 3% in 1HFY12.

Fig 7 We expect modest growth in India business...



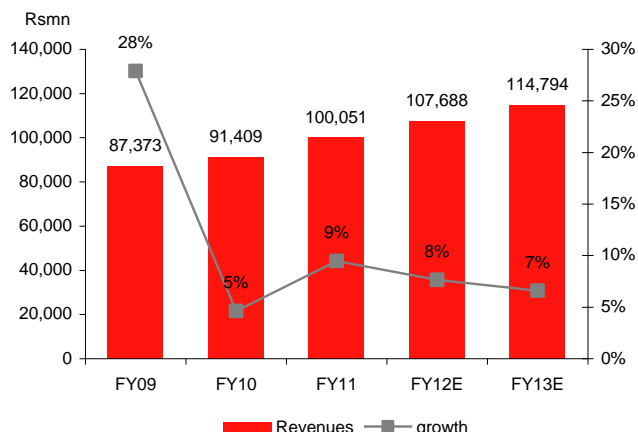
Source: Company data, Macquarie Research, October 2011

Fig 8 ... as growth remains subdued across segments



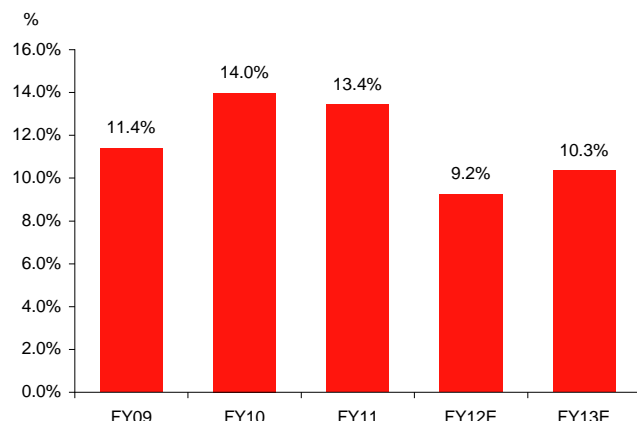
Source: Company data, Macquarie Research, October 2011

Fig 9 We are building 8% revenue growth...



Source: Company data, Macquarie Research, October 2011

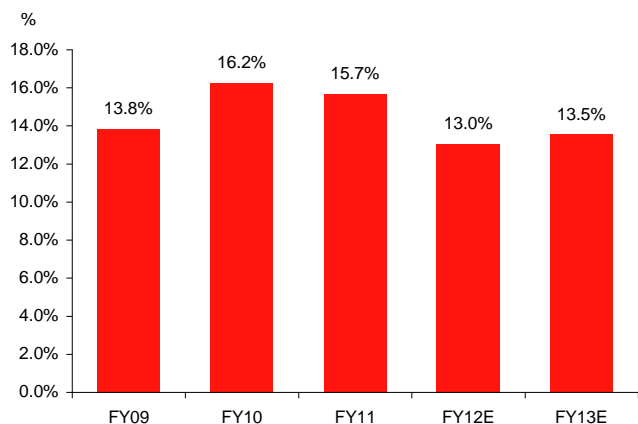
Fig 10 ... with 9.2% margin in consolidated entity



Source: Company data, Macquarie Research, October 2011

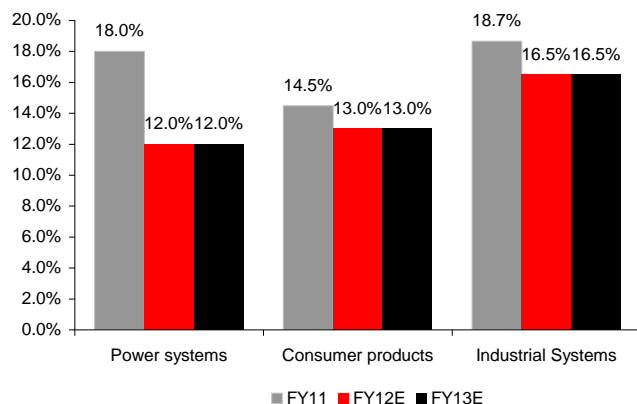
- **Reducing our margin forecasts to factor in continued competition in power systems:** The management continues to indicate high competition in domestic power systems, which led to a margin decline from 12.1% in 1QFY12 to 11.1% in 2QFY12. New orders, like 765kV substation order from Powergrid, have come at 8% margins.

Fig 11 We are building significant margin compression in India entity...



Source: Company data, Macquarie Research, October 2011

Fig 12 ... as we do not expect margin revival



Source: Company data, Macquarie Research, October 2011

- **Reducing our EPS forecasts by 15-16%:** Our EPS forecasts have been reduced by 15-16% for FY12-13 to factor in lower margins.

Fig 13 Reducing our FY12-13 consolidated EPS estimates by 15-16%

	FY12E		FY13E		% Change	
	old	new	old	new	12E	13E
Net Revenues	109,389	107,688	117,160	114,794	-1.6%	-2.0%
EBITDA	11,248	9,945	13,701	11,863	-11.6%	-13.4%
Net Income	6,766	5,772	8,712	7,356	-14.7%	-15.6%
EPS	10.5	9.0	13.6	11.5	-14.7%	-15.6%
EBITDA margin	10.3%	9.2%	11.7%	10.3%	-1.0%	-1.4%

Source: Company data, Macquarie Research, October 2011

Valuation – reducing our target price to Rs117

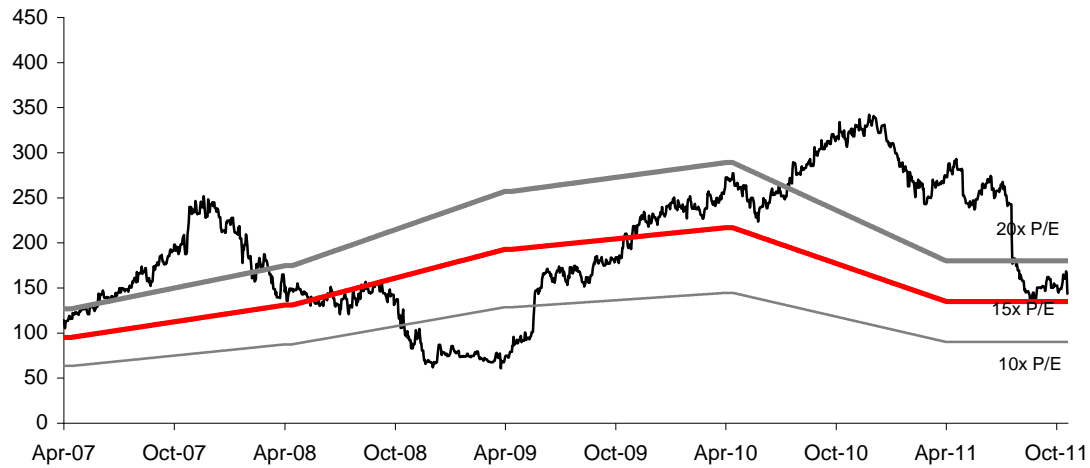
- **Reducing our target price to Rs117:** We reduce our target price from Rs158 to Rs117 to factor in a 15% earnings cut in FY12 and lower target multiple from 15x to 13x to factor in uncertainties in earnings and tax outgoings for the company.

Fig 14 Reducing our target price to Rs117

Segment	EV (Rs mn)	Value per share (Rs)	Comment
Core business	75,039	117	13x FY12 earnings
Total	75,039	117	

Source: Company data, Macquarie Research, October 2011

Fig 15 CRG – 1yr fwd PE chart



Source: Company data, Macquarie Research, October 2011

Crompton Greaves India (CRG IN, Underperform, Target Price: Rs117.00)

Quarterly Results					Profit & Loss						
	2Q/12A	3Q/12E	4Q/12E	1Q/13E		2011A	2012E	2013E	2014E		
Revenue	m	25,845	26,922	31,229	25,255	Revenue	m	100,051	107,688	114,794	129,198
Gross Profit	m	9,433	9,826	11,399	9,218	Gross Profit	m	37,363	39,306	41,900	47,157
Cost of Goods Sold	m	16,412	17,095	19,831	16,037	Cost of Goods Sold	m	62,689	68,382	72,894	82,040
EBITDA	m	2,387	2,486	2,884	2,610	EBITDA	m	13,438	9,945	11,863	14,059
Depreciation	m	596	621	720	557	Depreciation	m	1,936	2,482	2,534	2,715
Amortisation of Goodwill	m	0	0	0	0	Amortisation of Goodwill	m	0	0	0	0
Other Amortisation	m	0	0	0	0	Other Amortisation	m	0	0	0	0
EBIT	m	1,791	1,866	2,164	2,052	EBIT	m	11,502	7,463	9,330	11,344
Net Interest Income	m	-128	-134	-155	-75	Net Interest Income	m	209	-534	-339	-317
Associates	m	0	0	0	0	Associates	m	0	0	0	0
Exceptionals	m	0	0	0	0	Exceptionals	m	-381	0	0	0
Forex Gains / Losses	m	0	0	0	0	Forex Gains / Losses	m	0	0	0	0
Other Pre-Tax Income	m	168	175	203	165	Other Pre-Tax Income	m	999	699	748	803
Pre-Tax Profit	m	1,831	1,907	2,212	2,143	Pre-Tax Profit	m	12,329	7,628	9,739	11,830
Tax Expense	m	-458	-477	-553	-536	Tax Expense	m	-3,100	-1,907	-2,435	-2,957
Net Profit	m	1,373	1,430	1,659	1,607	Net Profit	m	9,229	5,721	7,304	8,872
Minority Interests	m	12	13	15	11	Minority Interests	m	77	52	52	53
Reported Earnings	m	1,385	1,443	1,674	1,618	Reported Earnings	m	9,305	5,772	7,356	8,925
Adjusted Earnings	m	1,385	1,443	1,674	1,618	Adjusted Earnings	m	9,687	5,772	7,356	8,925
EPS (rep)		2.16	2.25	2.61	2.52	EPS (rep)		14.50	9.00	11.47	13.91
EPS (adj)		2.16	2.25	2.61	2.52	EPS (adj)		15.10	9.00	11.47	13.91
EPS Growth yoy (adj)	%	-40.4	-40.4	-40.4	27.4	EPS Growth (adj)	%	17.5	-40.4	27.4	21.3
						PE (rep)	x	9.8	15.8	12.4	10.2
						PE (adj)	x	9.4	15.8	12.4	10.2
EBITDA Margin	%	9.2	9.2	9.2	10.3	Total DPS		2.42	1.57	2.01	2.43
EBIT Margin	%	6.9	6.9	6.9	8.1	Total Div Yield	%	1.7	1.1	1.4	1.7
Earnings Split	%	24.0	25.0	29.0	22.0	Weighted Average Shares	m	642	642	642	642
Revenue Growth	%	7.6	7.6	7.6	6.6	Period End Shares	m	642	642	642	642
EBIT Growth	%	-35.1	-35.1	-35.1	25.0						
Profit and Loss Ratios					Cashflow Analysis						
		2011A	2012E	2013E	2014E		2011A	2012E	2013E	2014E	
Revenue Growth	%	9.5	7.6	6.6	12.5	EBITDA	m	13,438	9,945	11,863	14,059
EBITDA Growth	%	5.2	-26.0	19.3	18.5	Tax Paid	m	-3,100	-1,907	-2,435	-2,957
EBIT Growth	%	2.5	-35.1	25.0	21.6	Chgs in Working Cap	m	-5,859	-3,994	-571	-1,158
Gross Profit Margin	%	37.3	36.5	36.5	36.5	Net Interest Paid	m	0	-534	-339	-317
EBITDA Margin	%	13.4	9.2	10.3	10.9	Other	m	0	0	0	0
EBIT Margin	%	11.5	6.9	8.1	8.8	Operating Cashflow	m	4,479	3,510	8,518	9,627
Net Profit Margin	%	9.2	5.3	6.4	6.9	Acquisitions	m	0	0	0	0
Payout Ratio	%	16.1	17.5	17.5	17.5	Capex	m	-7,627	-3,769	-4,018	-4,264
EV/EBITDA	x	6.9	9.4	7.9	6.6	Asset Sales	m	0	0	0	0
EV/EBIT	x	8.1	12.5	10.0	8.2	Other	m	1,333	803	881	964
						Investing Cashflow	m	-6,295	-2,966	-3,137	-3,300
Balance Sheet Ratios						Dividend (Ordinary)	m	-1,555	-1,555	-1,555	-1,555
ROE	%	33.5	16.4	18.9	20.4	Equity Raised	m	0	0	0	0
ROA	%	17.2	9.8	11.3	12.4	Debt Movements	m	-306	0	0	0
ROIC	%	36.8	16.2	17.6	20.4	Other	m	0	0	0	0
Net Debt/Equity	%	5.2	5.6	3.4	-7.3	Financing Cashflow	m	-1,862	-1,555	-1,555	-1,555
Interest Cover	x	nmf	14.0	27.5	35.7						
Price/Book	x	2.8	2.4	2.3	1.9	Net Chg in Cash/Debt	m	-3,654	-989	3,849	4,795
Book Value per Share		51.0	58.5	62.6	74.0	Free Cashflow	m	-3,148	-259	4,501	5,364
						Balance Sheet	2011A	2012E	2013E	2014E	
						Cash	m	2,984	2,598	3,336	8,199
						Receivables	m	25,427	27,368	29,174	32,835
						Inventories	m	11,893	12,732	13,572	15,275
						Investments	m	6,747	10,191	10,191	10,191
						Fixed Assets	m	18,314	19,601	21,085	22,633
						Intangibles	m	0	0	0	0
						Other Assets	m	7,379	7,736	8,068	8,741
						Total Assets	m	72,744	80,225	85,426	97,873
						Payables	m	29,595	31,853	33,956	38,216
						Short Term Debt	m	0	0	0	0
						Long Term Debt	m	4,703	4,703	4,703	4,703
						Provisions	m	4,298	4,626	4,931	5,550
						Other Liabilities	m	1,244	1,348	1,481	1,642
						Total Liabilities	m	39,840	42,531	45,070	50,111
						Shareholders' Funds	m	32,747	37,509	40,133	47,496
						Minority Interests	m	157	186	222	267
						Other	m	0	0	0	0
						Total S/H Equity	m	32,904	37,695	40,356	47,763
						Total Liab & S/H Funds	m	72,744	80,225	85,426	97,873

All figures in INR unless noted.

Source: Company data, Macquarie Research, October 2011

Important disclosures:

Recommendation definitions	Volatility index definition*	Financial definitions																																
<p>Macquarie - Australia/New Zealand Outperform – return >3% in excess of benchmark return Neutral – return within 3% of benchmark return Underperform – return >3% below benchmark return</p> <p>Benchmark return is determined by long term nominal GDP growth plus 12 month forward market dividend yield</p> <p>Macquarie – Asia/Europe Outperform – expected return >+10% Neutral – expected return from -10% to +10% Underperform – expected return <-10%</p> <p>Macquarie First South - South Africa Outperform – expected return >+10% Neutral – expected return from -10% to +10% Underperform – expected return <-10%</p> <p>Macquarie - Canada Outperform – return >5% in excess of benchmark return Neutral – return within 5% of benchmark return Underperform – return >5% below benchmark return</p> <p>Macquarie - USA Outperform (Buy) – return >5% in excess of Russell 3000 index return Neutral (Hold) – return within 5% of Russell 3000 index return Underperform (Sell) – return >5% below Russell 3000 index return</p>	<p>This is calculated from the volatility of historical price movements.</p> <p>Very high–highest risk – Stock should be expected to move up or down 60–100% in a year – investors should be aware this stock is highly speculative.</p> <p>High – stock should be expected to move up or down at least 40–60% in a year – investors should be aware this stock could be speculative.</p> <p>Medium – stock should be expected to move up or down at least 30–40% in a year.</p> <p>Low–medium – stock should be expected to move up or down at least 25–30% in a year.</p> <p>Low – stock should be expected to move up or down at least 15–25% in a year. * Applicable to Australian/NZ/Canada stocks only</p> <p>Recommendations – 12 months Note: Quant recommendations may differ from Fundamental Analyst recommendations</p>	<p>All "Adjusted" data items have had the following adjustments made: Added back: goodwill amortisation, provision for catastrophe reserves, IFRS derivatives & hedging, IFRS impairments & IFRS interest expense Excluded: non recurring items, asset revals, property revals, appraisal value uplift, preference dividends & minority interests</p> <p>EPS = adjusted net profit / epowa* ROA = adjusted ebit / average total assets ROA Banks/Insurance = adjusted net profit / average total assets ROE = adjusted net profit / average shareholders funds Gross cashflow = adjusted net profit + depreciation *equivalent fully paid ordinary weighted average number of shares</p> <p>All Reported numbers for Australian/NZ listed stocks are modelled under IFRS (International Financial Reporting Standards).</p>																																
<p>Recommendation proportions – For quarter ending 30 September 2011</p> <table border="1"> <thead> <tr> <th></th> <th>AU/NZ</th> <th>Asia</th> <th>RSA</th> <th>USA</th> <th>CA</th> <th>EUR</th> <th></th> </tr> </thead> <tbody> <tr> <td>Outperform</td> <td>57.35%</td> <td>65.88%</td> <td>56.94%</td> <td>46.54%</td> <td>74.68%</td> <td>47.85%</td> <td>(for US coverage by MCUSA, 11.63% of stocks covered are investment banking clients)</td> </tr> <tr> <td>Neutral</td> <td>31.99%</td> <td>20.68%</td> <td>31.94%</td> <td>50.00%</td> <td>23.42%</td> <td>34.66%</td> <td>(for US coverage by MCUSA, 9.30% of stocks covered are investment banking clients)</td> </tr> <tr> <td>Underperform</td> <td>10.66%</td> <td>13.45%</td> <td>11.11%</td> <td>3.46%</td> <td>1.90%</td> <td>17.49%</td> <td>(for US coverage by MCUSA, 0.47% of stocks covered are investment banking clients)</td> </tr> </tbody> </table>				AU/NZ	Asia	RSA	USA	CA	EUR		Outperform	57.35%	65.88%	56.94%	46.54%	74.68%	47.85%	(for US coverage by MCUSA, 11.63% of stocks covered are investment banking clients)	Neutral	31.99%	20.68%	31.94%	50.00%	23.42%	34.66%	(for US coverage by MCUSA, 9.30% of stocks covered are investment banking clients)	Underperform	10.66%	13.45%	11.11%	3.46%	1.90%	17.49%	(for US coverage by MCUSA, 0.47% of stocks covered are investment banking clients)
	AU/NZ	Asia	RSA	USA	CA	EUR																												
Outperform	57.35%	65.88%	56.94%	46.54%	74.68%	47.85%	(for US coverage by MCUSA, 11.63% of stocks covered are investment banking clients)																											
Neutral	31.99%	20.68%	31.94%	50.00%	23.42%	34.66%	(for US coverage by MCUSA, 9.30% of stocks covered are investment banking clients)																											
Underperform	10.66%	13.45%	11.11%	3.46%	1.90%	17.49%	(for US coverage by MCUSA, 0.47% of stocks covered are investment banking clients)																											

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