

March 22, 2011

Price Performance

BHEL	Buy			
CMP Rs 1,922	TP Rs 3,030			
(%)	1M	3M	6M	12M
Absolute	(8)	(17)	(21)	(19)
Rel. to Nifty	(7)	(8)	(12)	(21)

L&T	Buy			
CMP Rs 1,525	TP Rs 2,015			
(%)	1M	3M	6M	12M
Absolute	(8)	(24)	(25)	(7)
Rel. to Nifty	(7)	(16)	(16)	(9)

Cummins India	Buy			
CMP Rs 663	TP Rs 800			
(%)	1M	3M	6M	12M
Absolute	(5)	(16)	(15)	28
Rel. to Nifty	(3)	(7)	(5)	25

Thermax	Buy			
CMP Rs 594	TP Rs 943			
(%)	1M	3M	6M	12M
Absolute	(12)	(33)	(29)	(16)
Rel. to Nifty	(10)	(26)	(21)	(18)

Voltas	Buy			
CMP Rs 152	TP Rs 250			
(%)	1M	3M	6M	12M
Absolute	(9)	(29)	(35)	(10)
Rel. to Nifty	(7)	(22)	(27)	(12)

Blue Star	Buy			
CMP Rs 322	TP Rs 455			
(%)	1M	3M	6M	12M
Absolute	(6)	(25)	(36)	(16)
Rel. to Nifty	(4)	(16)	(28)	(17)

Greaves Cotton	Buy			
CMP Rs 85	TP Rs 111			
(%)	1M	3M	6M	12M
Absolute	(3)	(10)	(1)	41
Rel. to Nifty	(2)	(0)	10	38

Source: Bloomberg

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- **ECI sector witnessed marginal earnings changes for FY11E (up 4.9% since Jun'09) and FY12E (down 0.5% since Mar'10)**
- **ECI sector's current valuations imply resumption of capex spends - Non-resumption could trigger upto 20% de-rating in valuations**
- **At 14.1X PER, BHEL has best risk-to-reward (15% lower than Lehman crisis). L&T, Voltas and Greaves Cotton also attractive - being 11-37% lower than FY04-08 cycle**
- **Cummins and Crompton Greaves have large downside risks, highly susceptible to negative surprises**

Earnings forecast for FY11E & FY12E have seen marginal changes so far

The ECI (Engineering, Capital Goods & Infrastructure) sector has witnessed marginal earnings changes for FY11E and FY12E. Consensus earnings forecasts for FY11E have been upgraded by 4.9% since Jun'09 – net profit forecasts upgraded from Rs127 bn in Jun'09 to Rs133 bn in Mar'11. Whereas, earnings forecasts for FY12E have been downgraded by 0.5% – net profit forecasts declined from Rs162 bn in Mar'10 to Rs161 bn in Mar'11. Further, the ECI sector's implied earnings forecasts for Q4FY11E is 42% of FY11E earnings - at the higher end of its historic band of 35-44% of annual earnings. Assuming a worst case scenario of 35% of FY11E earnings earned in Q4FY11E, the ECI sector could witness an earnings downgrade upto 10%.

Resumption of capex spends, becomes imperative to sustain current valuations

The ECI sector has underperformed the Nifty index in the last 6 months by approximately 15%. ECI sector's current valuations at 16.9X or 18% premium to Sensex PER, imply resumption of capex spends in India. Hence, non-resumption of capex spends in immediate future could trigger de-rating. Though not quantifiable, based on simple reference to the Lehman crisis (Oct'08-Mar'09 period), ECI sector has risk of upto 20% de-rating in valuations.

BHEL has best risk-to-reward, followed by L&T, Voltas and Greaves Cotton

Amongst ECI companies, BHEL has best risk-to-reward with PER at 14.1X being 15% lower than valuations during the Lehman crisis. Inherently, BHEL's current valuations do not factor resumption of positive events in the near future. Even L&T, Voltas and Greaves Cotton have attractive risk to reward profile with current valuations being 11-37% lower than FY04-08 cycle. Companies like Cummins and Crompton Greaves, trading at premium to FY04-08 cycle have large downside risks and are highly susceptible to negative surprises.

Note

- *ECI sector referred in analysis and assessment comprises of 10 companies → L&T, BHEL, ABB, Cummins India, Siemens, Crompton Greaves, Thermax, Voltas, Blue Star and Greaves Cotton.*
- *Valuations are based on prices as on 15 March 2011*
- *Below analysis is based ONLY on consensus earnings estimates as on 15 March 2011 (including for stocks under active coverage)*

Comparing PER against different time periods

1-Yr Fwd PER (X)	Current	15-year Average		FY04-08 Average		Cap Good Cycle-Start	
	PER	PER	Premium/Discount	PER	Premium/Discount	PER	Premium/Discount
BHEL	14.1	13.9	1%	20.0	-30%	19.1	-26%
L&T	18.0	18.0	0%	21.8	-17%	20.1	-10%
Cummins	17.8	16.1	10%	16.5	8%	14.8	20%
Thermax	15.5	15.6	-1%	17.4	-11%	14.2	9%
Voltas	11.7	12.9	-10%	18.4	-37%	21.6	-46%
Blue Star	13.7	9.5	44%	13.7	0%	14.6	-6%
Greaves Cotton	11.0	7.1	54%	12.3	-11%	13.2	-17%
Crompton Greaves	15.9	11.8	35%	15.8	0%	17.9	-11%
Siemens	25.2	18.3	38%	27.0	-6%	25.7	-2%
ABB	36.8	33.2	11%	31.7	16%	33.6	9%
Industry	16.9	17.0	-1%	21.0	-20%	20.3	-17%

Source: Bloomberg, Company, Emkay Research

Computing downsides to current valuations - Worst Case

1-Yr Fwd PER (X)	Current PER	Versus Lehman Crisis			
		Average Oct08-Mar09		Minimum	
		PER	Downside	PER	Downside
BHEL	14.1	16.5	17%	15.7	12%
L&T	18.0	13.2	-27%	11.1	-38%
Cummins	17.8	8.6	-52%	6.9	-61%
Thermax	15.5	8.8	-43%	7.2	-53%
Voltas	11.7	5.5	-53%	3.7	-69%
Blue Star	13.7	7.1	-48%	6.4	-54%
Greaves Cotton	11.0	3.4	-69%	2.3	-79%
Crompton Greaves	15.9	6.2	-61%	5.4	-66%
Siemens	25.2	11.6	-54%	9.7	-61%
ABB	36.8	24.0	-35%	20.8	-43%
Industry	16.9	13.5	-20%	12.3	-27%

Source: Bloomberg, Company, Emkay Research

Analyzing earnings forecasts for FY11E and FY12E - Marginal changes

The ECI sector has undergone marginal earnings changes for FY11E and FY12E. Consensus earnings forecasts for FY11E have been upgraded by 4.9% since Jun'09 – net profit forecasts upgraded from Rs127 bn in Jun'09 to Rs133 bn in Mar'11. Whereas, earnings forecasts for FY12E have been downgraded by 0.5% – net profit forecasts declined from Rs162 bn in Mar'10 to Rs161 bn in Mar'11. Further, the ECI sector's implied earnings forecasts for Q4FY11E is 42% of FY11E earnings - at the higher end of its historic band of 35-44% of annual earnings.

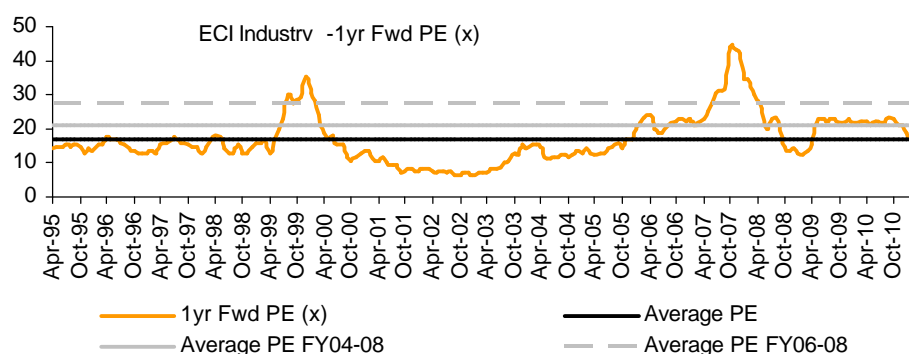
1-year forward PER valuation has declined by 28%, despite marginal change in earnings forecasts

The ECI sector's 1-year forward PER valuation has declined by 28% from 23.3X in Sep'10 to 16.9X in Mar'11. However, there has been NO commensurate downgrade in earnings estimates in the last 6 months. The earnings downgrades have been miniscule at -0.4% for FY11E and -1.0% for FY12E since Sep'10. Further, 9MFY11 performance is extremely robust with earnings growth of 23% yoy.

Valuations at 16.9X 1-year forward earnings → at par to long-term (15-year) 1-year forward PER of 17.0X

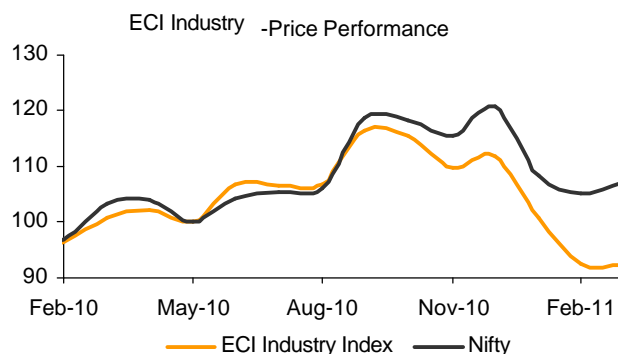
The ECI sector has underperformed the Nifty index in the last 6 months by approximately 15%. The ECI sector has fallen 21% from its peak in Sep'10 and approximately 18% since Dec'10. Post the fall-off, ECI sector is trading at 1-year forward PER valuations of 16.9X or at par to long term 1-year forward PER of 17.0X. Even relative to Sensex valuation, ECI sector is trading at 18% premium to Sensex valuation – significantly lower than average long term (15-year) premium of 28% and FY04-08 cycle average premium of 37%.

ECI sector trading at par with long term PER



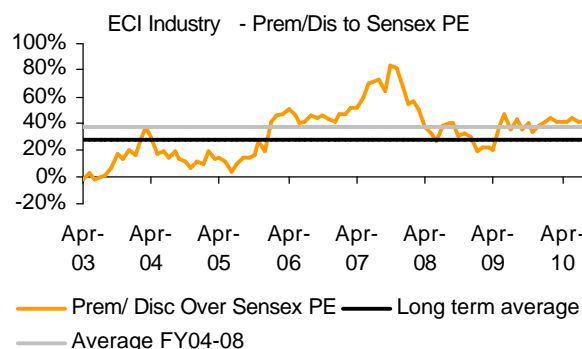
Source: Bloomberg, Company, Emkay Research

ECI sector underperformed Nifty by 15% over the past 6 months



Source: Bloomberg, Emkay Research

ECI sector trading at 18% premium to Sensex valuations – Vs long-term premium of 28%



Source: Bloomberg, Emkay Research

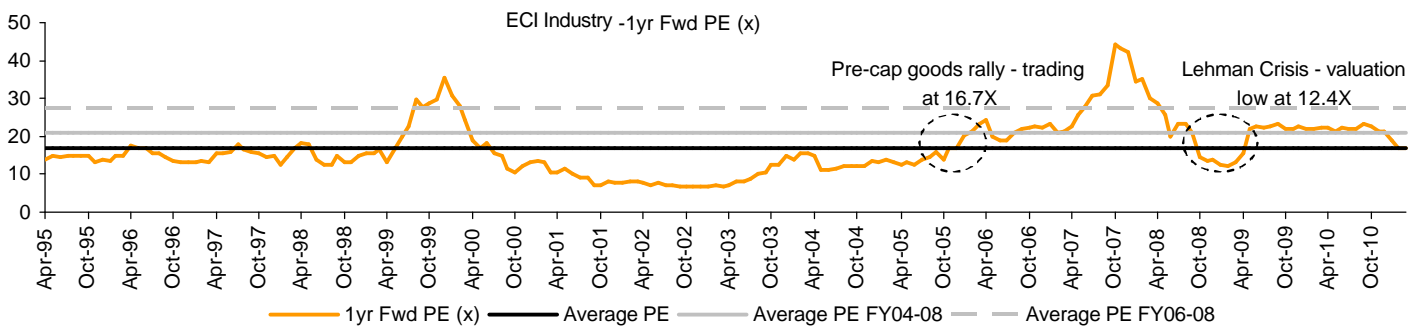
Current valuations at par with inflection of FY06-08 ECI cycle

At 16.9X, the ECI sector is trading at par with the valuations attained at inflection point (i.e. FY06) of investment up-cycle in ECI sector (16.0-17.0X). We believe current valuations are attractive and certainly offer a favorable risk reward with the structure of the Indian economy necessitating resumption of capex spends, albeit with a time lag.

...But remains significantly higher than Lehman crisis (FY09)

Current valuation, however, is significantly higher than valuations during Lehman crisis i.e. during Oct'08 – Mar'09 period. The average PER valuation during Oct'08-Mar'09 was 13.5X, whereas the lowest PER valuation attained was 12.3X. Thus, current valuations are 20% higher than valuations during Lehman crisis- indicating an equivalent downside risk.

ECI sector valuations are equal to long-term average valuations



Source: Bloomberg, Emkay Research

Current valuations factor resumption of capex spends in India, non-recurrence could trigger de-rating

The 1-year forward PER for ECI sector at 16.9X or 18% premium to Sensex PER, factors resumption of capex spends in India i.e. both government and private. It factors 16-18% growth in capex spends, which is normalized and sustainable, considering the structure of the Indian economy. Thus, resumption of capital spends is extremely imperative for sustaining current valuations. Also, lead time for resumption of capital spends could have a bearing on current valuations. It also indicates that non-recurrence of capex spends in the immediate future could trigger de-rating. Though true extent is not quantifiable, but based on reference to Lehman crisis – PER for ECI sector could fall by 20% from 16.9X to 13.5X. These valuations could emerge on further delay in resumption of capex spends – triggered by probable events like re-elections in India, oil shock spooking growth, etc.

With fair valuation at 21.0X 1-year forward PER (i.e. FY04-08 average) – CMP support earnings downgrade of 20%

In EMKAY sector note “ECI-Roll the Dice” – fair valuations were pegged at FY04-08 average for the sector i.e. 21.0X. Based on fair valuations, current PER valuations of 16.9X indirectly support 20% downgrade in FY12E earnings in ensuing quarters. This would in turn reduce FY12E sector earnings growth from +21% to -3%.

But, 20% downgrade in FY12E earnings combined with 10% downgrade in FY11E earnings (on achieving 35% of FY11E earnings in Q4FY11E instead of 42% of FY11E earnings) would result in reduction of FY12E earnings growth from the erstwhile 21% to 8%. Just to highlight, highest earnings downgrade for ECI sector has been 22% in FY09 followed by 17% in FY10.

Sector influenced by factors from external environment; whereas earnings cues acts as a lag indicator

ECI sector is dependent on capital spends in the economy, which in turn, is closely linked to macro trends of the economy. Thus, ECI sector performance is strongly influenced by macro factors like interest rates, inflation, supply-demand economics, capital availability and overall sentiment. This in turn, influences order finalization and execution. These factors, which have acted as lead indicators for sector valuations and performance, remain identifiable but not quantifiable. Earnings performance remains a lag indicator- showcasing real impact of external environment.

Most importantly, institutional investors remain 'Underweight'

We continue to highlight that institutional investors (IIs) have remained underweight on the ECI sector for the last 8 quarters, with the exception of infrastructure companies. IIs have reduced exposure (in absolute terms) by 360 bps over the past 3 quarters. Thus, 28% de-rating of PER valuations (since Sep'10), 'Underweight' stance of IIs and reduction in absolute holding on quarterly basis are strong reason to cap downsides for the ECI sector.

BHEL is best on risk to reward – L&T, Voltas and Greaves Cotton have limited downside risk

Amongst ECI companies, BHEL is best placed, offering attractive risk to reward profile with current PER valuations at 14.1X, being 15% lower than valuations during Lehman crisis. Inherently, BHEL's current valuations do not factor resumption of positive events in the near future. Even, L&T, Voltas and Greaves Cotton have attractive risk to reward profile with current valuations being 11-37% lower than FY04-08 cycle (captures earnings up-cycle for the ECI sector). But, inherently current valuations factor resumption of capex spends in ensuing quarters. Thus, any non-recurrence of capex spends could trigger significant de-rating in valuations – quantified upto 27-69% (stock Specific) (assuming occurrence of Lehman like event).

Cummins and Crompton Greaves to be most vulnerable to negative surprises

Cummins and Crompton Greaves emerged as top performers in the ECI sector post the Lehman crisis in Sep'08. This is attributed to consistent earnings upgrades for 6 quarters and equally strong earnings performance. Despite the de-rating for the sector at large, these companies trade at premium to FY04-08 average valuations. Thus, these companies have large downside risk and would be highly susceptible to negative surprises.

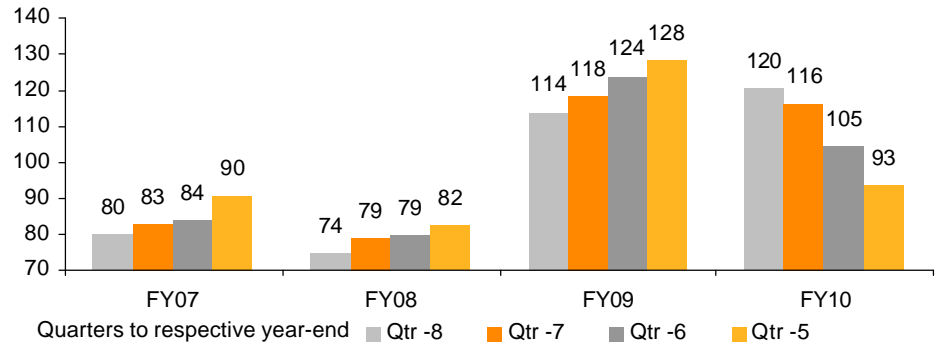
Annexure I – Earnings forecasts & its relevance

General observations on forecasting trends in earnings for the ECI sector

- Observations for 2-year forward earnings forecasts

- Estimating 2-year forward earnings is akin to a dart-board game – estimates fluctuate within a broad range of > (+/-)15%

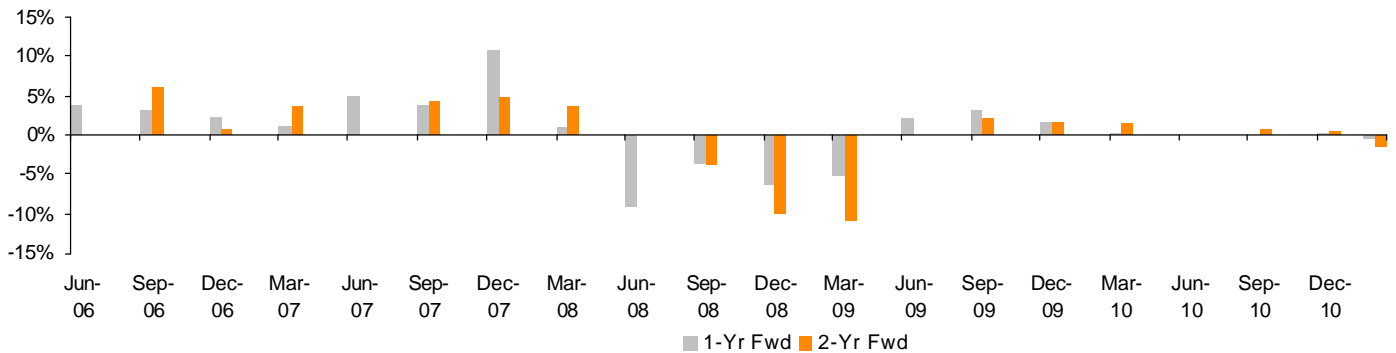
Low conviction on 2-year forward earnings



Source: Bloomberg, Emkay Research

- Directionally, change in 2-year forward earnings mirrors change in 1-year forward earnings. That is, 2-year forward earnings change directionally driven by change in near term (1-year) earnings – not a derivative of independent forecasting

Change in 2-year forward earnings mirrors change in 1-year forward earnings

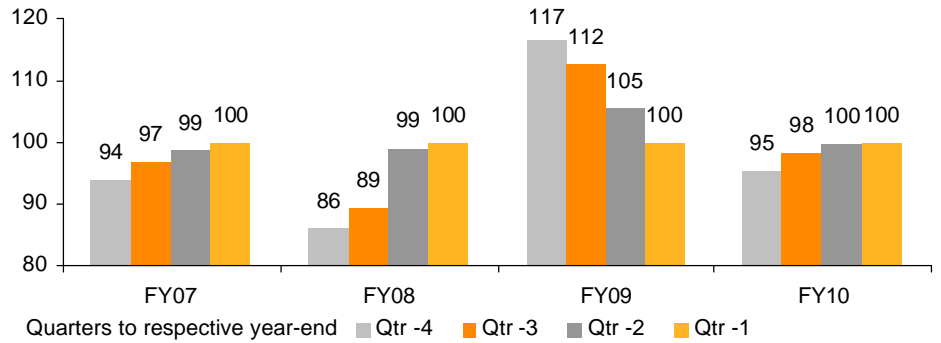


Source: Bloomberg, Emkay Research

■ **Observations for 1-year forward earnings forecasts**

- 1-year forward earnings estimates are more reliable – estimates change within a narrow range of $(+/-7\%)$

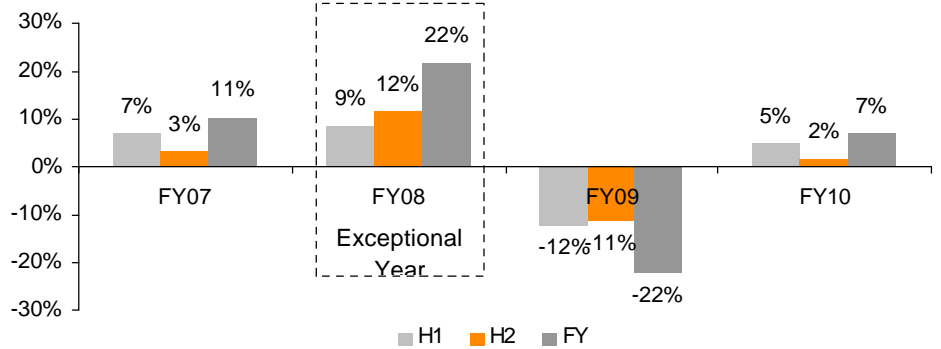
Analysts have better clarity on 1-year forward earnings



Source: Bloomberg, Emkay Research

- Highest revision in earnings is implemented in H1 of current year

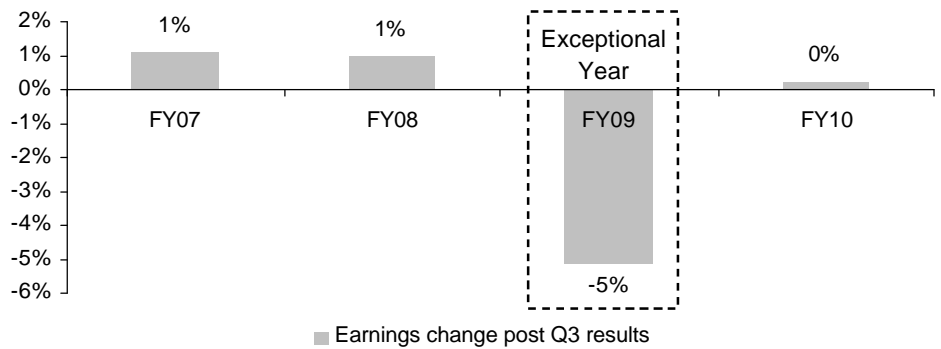
H1 of the current year undergoes highest revision in earnings



Source: Bloomberg, Emkay Research

- Extent of earnings revision is lowest (approximately +/- 1%) post Q3 results of current year

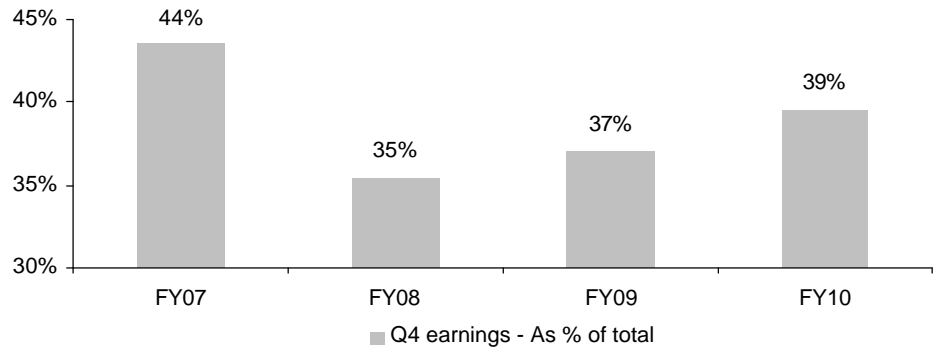
Revision in annual earnings post Q3 performance is a meager 1%



Source: Bloomberg, Emkay Research

- Sector at large, reports 35-44% of earnings in Q4 of fiscal year

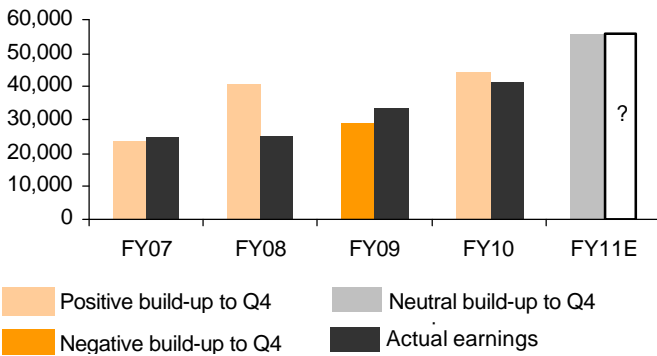
ECI sector reports 35-44% of annual earnings in Q4



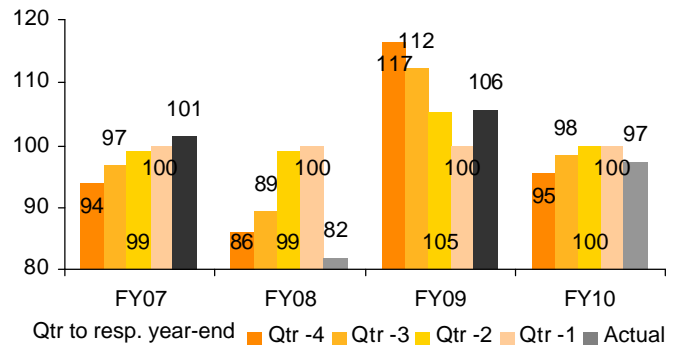
Source: Bloomberg, Emkay Research

- Sector has proven history of earning surprises versus Q4 estimates – range of earnings surprises varies from -39% to +17%. Actual earnings performance contradicts underlying forecasts i.e. healthy earnings forecasts are followed by negative surprises and vice versa.

Contrarian earnings surprises posted by ECI sector in Q4...



Source: Bloomberg, Emkay Research

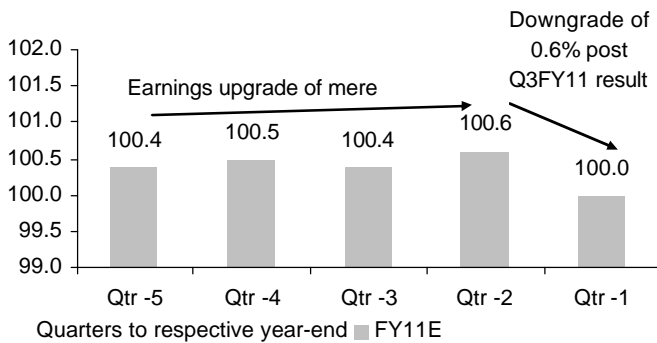


Source: Bloomberg, Emkay Research

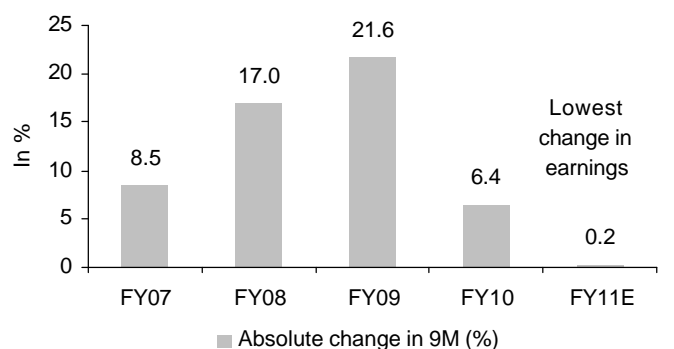
How are sector earnings forecasts for FY11E and FY12E stacked-up?

- For FY11E (1-year forward earnings) – No clear trend visible
 - Earnings forecasts remain unchanged until 9MFY11 – earnings upgrade of a mere 0.2%

Unlike in the past, FY11E earnings underwent miniscule change at 0.2% during Apr'10 to Dec'10



Source: Bloomberg, Emkay Research



Source: Bloomberg, Emkay Research

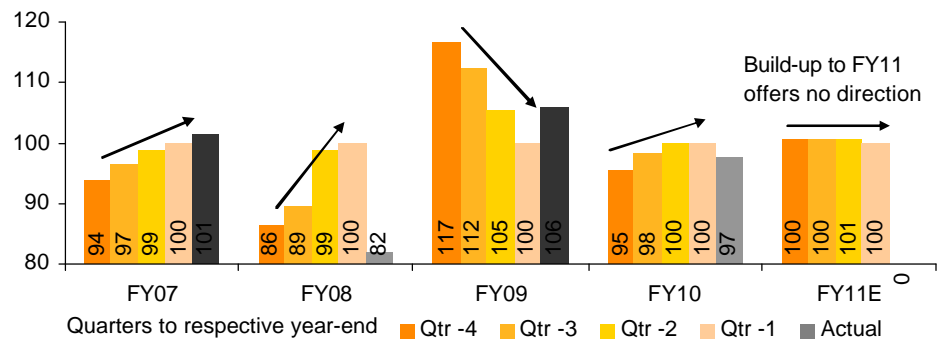
- Earnings change is polarized for FY11E – handful of companies have seen earnings upgrades i.e. Cummins, Thermax, Voltas and Crompton Greaves

(In Rs Mn)						
FY11E earnings as on	Mar-10	Jun-10	Sep-10	Dec-10	Mar-11	% Change since Mar'10
BHEL	55,283	54,816	54,787	55,116	55,630	0.6%
L&T	37,907	38,350	38,144	37,974	38,298	1.0%
Cummins	5,412	5,226	5,968	6,397	6,065	12.1%
Thermax	3,341	3,345	3,533	3,618	3,701	10.8%
Voltas	3,333	3,591	3,851	3,858	3,565	7.0%
Blue Star	2,123	2,207	2,207	2,030	1,619	-23.7%
Greaves Cotton	1,375	1,375	1,375	1,375	1,375	0.0%
Crompton Greaves	8,626	8,728	8,934	9,014	9,102	5.5%
Siemens	9,652	9,877	9,300	9,564	9,637	-0.2%
ABB	6,697	6,346	5,649	5,061	4,238	-36.7%
Total	133,748	133,861	133,747	134,006	133,229	-0.4%

Source: Bloomberg, Emkay Research

- ...With no earnings change on YTD basis, FY11E earnings forecast fails to give any direction

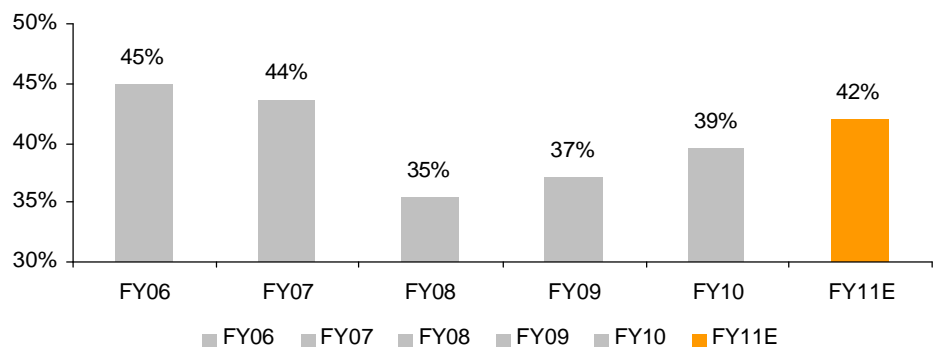
Build-up to FY11E offers no definitive earnings direction



Source: Bloomberg, Emkay Research

- Implied rate for Q4FY11E pegged at 42% of FY11E earnings – achievable, albeit at the higher end of historic performance

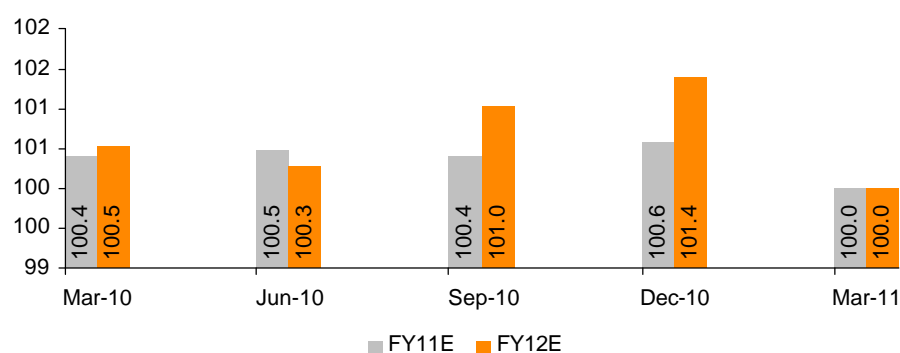
Implied Q4FY11E earnings within historic band – albeit at higher end



Source: Bloomberg, Emkay Research

- Hypothetically, if actual earnings for Q4FY11E remains at lower-end (35% of annual earnings), it would imply a 10% downgrade in FY11E earnings. This translates into a mere 2% yoy growth in earnings for Q4FY11E (Vs 23% growth in witnessed in 9MFY11).
- **FY12E (2-year forward earnings) – mirroring FY11E trend**
 - FY12E has mirrored FY11E. FY12E earnings have witnessed a miniscule downgrade of 0.5% in 9MFY11. Whereas, upgrades are polarized towards handful of companies i.e. Cummins, Thermax, Voltas, Crompton Greaves and Siemens.
 - No trend or direction derived from changes in earnings forecasts on YTD basis

No significant change in FY12E earnings forecasts



Source: Bloomberg, Emkay Research

FY12E earnings as on						(In Rs Mn)
	Mar-10	Jun-10	Sep-10	Dec-10	Mar-11	% Change since Mar'10
BHEL	66,104	65,657	65,568	66,182	66,908	1.2%
L&T	47,117	47,509	47,238	47,020	46,568	-1.2%
Cummins	6,711	6,711	7,644	8,122	7,396	10.2%
Thermax	4,229	4,281	4,569	4,740	4,567	8.0%
Voltas	3,730	4,202	4,655	4,668	4,297	15.2%
Blue Star	2,508	2,637	2,629	2,519	2,118	-15.6%
Greaves Cotton	1,876	1,876	1,876	1,876	1,876	0.0%
Crompton Greaves	10,027	10,042	10,344	10,495	10,537	5.1%
Siemens	10,817	11,046	11,055	11,392	11,383	5.2%
ABB	8,877	7,629	7,221	6,420	5,511	-37.9%
Total	161,995	161,591	162,799	163,434	161,161	-0.5%

Source: Bloomberg, Emkay Research

Annexure II - Company-level change in earnings forecasts

We have analysed FY11E and FY12E earnings forecasts for the ECI sector and come up with the following observations

FY11E – (1-year forward earnings)

Though the ECI sector saw a mere 4.9% upgrade in FY11E earnings, this remains largely influenced by two large heavy-weights i.e. BHEL and L&T. Both of them experienced approximately 35% upgrade in FY11E earnings. Earnings upgrades were witnessed in Cummins (51%), followed by Crompton Greaves (29%), Thermax (20%) and Voltas (13%). Whereas, ABB (-40%) and Blue Star (-26%) witnessed earnings downgrades.

FY11E Earnings	Apr'09 to Mar'11	Apr'09 to -Mar'10	Apr'10 to Mar'11
BHEL	3.5%	2.8%	0.6%
L&T	3.6%	2.6%	1.0%
Cummins	50.9%	34.7%	12.1%
Thermax	19.9%	8.3%	10.8%
Voltas	13.4%	6.0%	7.0%
Blue Star	-26.5%	-3.6%	-23.7%
Greaves Cotton	0.0%	0.0%	0.0%
Crompton Greaves	29.5%	22.7%	5.5%
Siemens	14.9%	15.1%	-0.2%
ABB	-40.0%	-5.2%	-36.7%
Industry	4.9%	5.3%	-0.4%

Source: Bloomberg, Emkay Research

FY12E (2-year forward earnings)

FY12E earnings forecasts for ECI sector has remain unchanged with just 0.5% downgrade in last 4 quarters. Though, there were company level changes, sector aggregates remain unchanged. Earnings upgrades were witnessed in Voltas (15%) followed by Cummins (10%) and Thermax (8%). Whereas, earnings downgrades were witnessed in ABB (-38%) and Blue Star (-16%).

FY12E Earnings	Apr'10 to Mar'11	Dec'10 to Mar'11
BHEL	1.2%	1.1%
L&T	-1.2%	-1.0%
Cummins	10.2%	-8.9%
Thermax	8.0%	-3.6%
Voltas	15.2%	-7.9%
Blue Star	-15.6%	-15.9%
Greaves Cotton	0.0%	0.0%
Crompton Greaves	5.1%	0.4%
Siemens	5.2%	-0.1%
ABB	-37.9%	-14.2%
Industry	-0.5%	-1.4%

Source: Bloomberg, Emkay Research

Q4FY11E implied earnings

Further, ECI sector Q4FY11E implied earnings forecasts is 42% of FY11E earnings, which is at the higher-end of the historic band of 35-44% of annual earnings. Few companies like L&T, Blue Star, and Siemens are at the higher end of their respective historic bands – hence, risk to earnings is higher. Whereas, companies at lower end of respective historic bands are BHEL, Cummins, Thermax, Voltas, Crompton Greaves and Greaves Cotton.

Q4FY11E Implied	YoY Gr (Q4FY11E On Q4FY10)	As % of FY11E Earnings	Q4 Earnings (As % of Annual)
BHEL	26%	43%	42 - 48
L&T	30%	45%	42 - 50
Cummins	35%	26%	27 - 29
Thermax	15%	31%	28 - 39
Voltas	8%	37%	27 - 64
Blue Star	-18%	40%	25 - 48
Greaves Cotton	-14%	21%	23 - 33
Crompton Greaves	1%	30%	33 - 36
Siemens	72%	32%	0 - 27
ABB	-	87%	2 - 23
Industry	35%	42%	35 - 44

Source: Bloomberg, Emkay Research

Annexure III - Comparing valuations under different time periods

We are extending our valuation analysis on the ECI sector to individual companies constituting the sector. Further, we have compared current valuations under different time periods – with the inherent assumption that capex spends would resume. Current valuations have been compared with (1) recent peak in Sep'10 (2) De-rating witnessed from Dec'10 (3) 15-year average (4) FY04-08 average and (5) on-set of capital goods earnings cycle in January 2006

■ Versus market peak of Sep'10

The ECI sector has undergone a 28% de-rating since Sep'10 with unanimous behavior by the constituents. Sharpest de-rating is seen in Voltas and Blue Star at 41%, followed by Thermax at 32%, L&T at 32% and BHEL at 29%. Siemens, owing to ongoing open offer, saw a mere 2% de-rating in PER valuations.

On 1-Yr Fwd PER	Current PER	Sep'10 PER	Premium / (Discount)	
BHEL	14.1	19.8	-29%	Discount
L&T	18.0	26.3	-32%	Discount
Cummins	17.8	21.7	-18%	Discount
Thermax	15.5	23.0	-32%	Discount
Voltas	11.7	20.3	-42%	Discount
Blue Star	13.7	23.4	-41%	Discount
Greaves Cotton	11.0	12.7	-14%	Discount
Crompton Greaves	15.9	20.4	-22%	Discount
Siemens	25.2	25.7	-2%	Discount
ABB	36.8	59.0	-38%	Discount
Industry	16.9	23.3	-28%	Discount

Source: Bloomberg, Emkay Research

■ De-rating from Dec'10 (participation in market slide)

Since Dec'10, the ECI sector has witnessed PER de-rating of 21% from 21.4X to 16.9X – higher than BSE Sensex PER correction of 15% from 16.8X to 14.4X. L&T (-26%), Thermax (-35%), Voltas (-33%) and Blue Star (-31%) witnessed the sharpest correction. Siemens remained the exception with stable PER at 25.2X, owing to the open offer.

On 1-Yr Fwd PER	Current PER	Dec'10 PER	Premium / (Discount)	
BHEL	14.1	17.8	-21%	Discount
L&T	18.0	24.3	-26%	Discount
Cummins	17.8	21.9	-19%	Discount
Thermax	15.5	23.7	-35%	Discount
Voltas	11.7	17.5	-33%	Discount
Blue Star	13.7	19.7	-31%	Discount
Greaves Cotton	11.0	13.9	-21%	Discount
Crompton Greaves	15.9	19.6	-19%	Discount
Siemens	25.2	24.8	2%	Premium
ABB	36.8	44.5	-17%	Discount
Industry	16.9	21.4	-21%	Discount

Source: Bloomberg, Emkay Research

■ Comparison with 15-year average

At 16.9X, the ECI sector is trading at par to the long-term (15-year) average (LTA) PER of 17.0X – also signifying favorable risk-to-reward. Voltas is best placed with 10% discount to LTA PER, followed by L&T, Thermax and BHEL trading at LTA PER. Companies like Greaves Cotton, Blue Star and Crompton Greaves are trading at significant premium to LTA PER, owing to change in scale and size of operations and business dynamics.

On 1-Yr Fwd PER	Current PER	Long Term Average (15-year)	Premium / (Discount)	
BHEL	14.1	13.9	1%	Premium
L&T	18.0	18.0	0%	Premium
Cummins	17.8	16.1	10%	Premium
Thermax	15.5	15.6	-1%	Discount
Voltas	11.7	12.9	-10%	Discount
Blue Star	13.7	9.5	44%	Premium
Greaves Cotton	11.0	7.1	54%	Premium
Crompton Greaves	15.9	11.8	35%	Premium
Siemens	25.2	18.3	38%	Premium
ABB	36.8	33.2	11%	Premium
Industry	16.9	17.0	-1%	Discount

Source: Bloomberg, Emkay Research

■ Comparison with FY04-08 average

ECI sector is trading at 20% discount to FY04-08 valuations of 21.0X. Infact, these were fair valuations ascribed to the ECI sector in our earlier report “Roll the Dice...” (Dated Sep’09). BHEL and Voltas are trading at highest discount of -30% and -37% respectively, whereas L&T is at -17% discount. On the contrary, companies like ABB and Cummins are trading at 16% and 8% premium to FY04-08 valuations.

On 1-Yr Fwd PER	Current PER	FY04-08 Average	Premium / (Discount)	
BHEL	14.1	20.0	-30%	Discount
L&T	18.0	21.8	-17%	Discount
Cummins	17.8	16.5	8%	Premium
Thermax	15.5	17.4	-11%	Discount
Voltas	11.7	18.4	-37%	Discount
Blue Star	13.7	13.7	0%	Premium
Greaves Cotton	11.0	12.3	-11%	Discount
Crompton Greaves	15.9	15.8	0%	Premium
Siemens	25.2	27.0	-6%	Discount
ABB	36.8	31.7	16%	Premium
Industry	16.9	21.0	-20%	Discount

Source: Bloomberg, Emkay Research

■ **On comparison with on-set of Capital Goods earnings cycle in Jan'06**

ECI sector is trading at 17% discount. Cummins, ABB and Thermax remain an exception, trading at 8-18% premium to Jan'06 valuations. BHEL and Voltas have highest discount of 26% and 46% respectively, followed by Greaves Cotton at 17% and Crompton Greaves at 11%.

On 1-Yr Fwd PER	Current PER	January 2006	Premium / (Discount)	
BHEL	14.1	19.1	-26%	Discount
L&T	18.0	20.1	-10%	Discount
Cummins	17.8	14.8	20%	Premium
Thermax	15.5	14.2	9%	Premium
Voltas	11.7	21.6	-46%	Discount
Blue Star	13.7	14.6	-6%	Discount
Greaves Cotton	11.0	13.2	-17%	Discount
Crompton Greaves	15.9	17.9	-11%	Discount
Siemens	25.2	25.7	-2%	Discount
ABB	36.8	33.6	9%	Premium
Industry	16.9	20.3	-17%	Discount

Source: Bloomberg, Emkay Research

■ **Non-resumption of capex spends could trigger further de-rating for ECI sector**

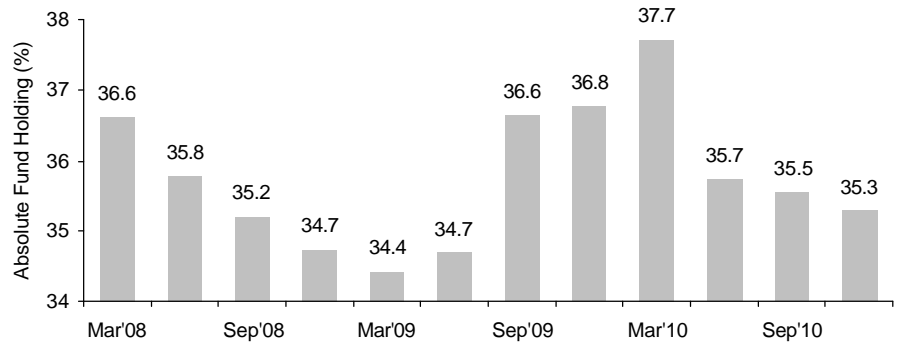
Non-resumption of capex spends could trigger further de-rating of ECI sector. We have drawn analogy to Oct'08-Mar'09 period, which was characterized by Lehman crisis, followed by uncertainty surrounding the central elections in India. Said valuations in Oct'08-Mar'09 period reflected non-resumption of capex spends in Indian economy. Thus, drawing analogy to said event, there is 20% downside risk or de-rating scope to current valuations of ECI sector, with BHEL being the only exception. Large downside risk exists in Cummins, Thermax and Crompton Greaves.

On 1-Yr Fwd PER	Current PER	Oct '08-Mar '09 Average	Downside
BHEL	14.1	16.5	17%
L&T	18.0	13.2	-27%
Cummins	17.8	8.6	-52%
Thermax	15.5	8.8	-43%
Voltas	11.7	5.5	-53%
Blue Star	13.7	7.1	-48%
Greaves Cotton	11.0	3.4	-69%
Crompton Greaves	15.9	6.2	-61%
Siemens	25.2	11.6	-54%
ABB	36.8	24.0	-35%
Industry	16.9	13.5	-20%

Source: Bloomberg, Emkay Research

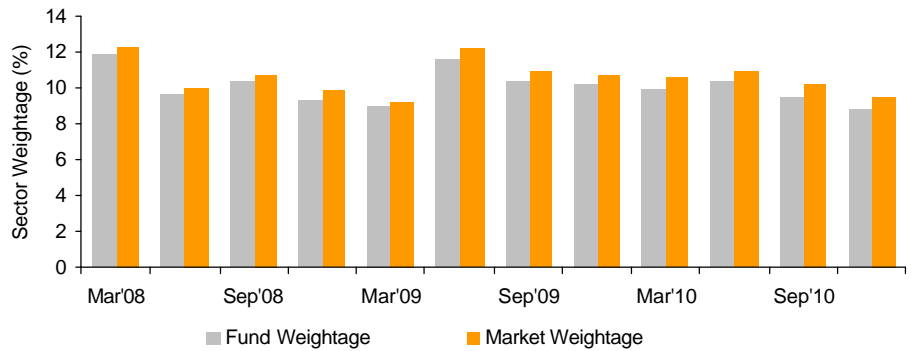
Annexure IV – Fund holding in ECI sector

Fund holding in ECI sector decreased by 240 bps in last 4 quarters



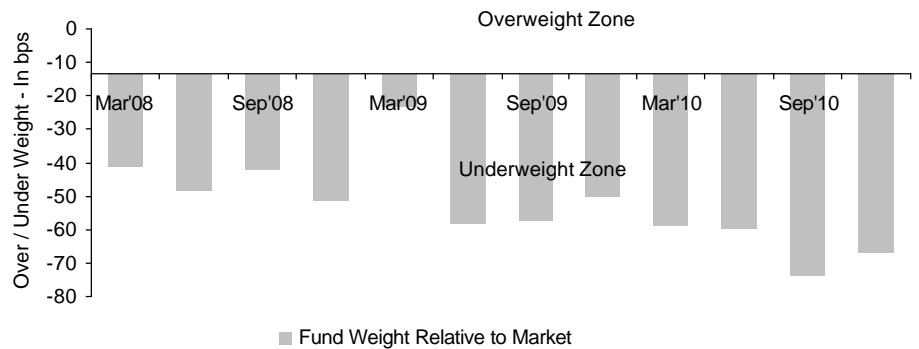
Source: Capitaline, Emkay Research

Fund versus Benchmark weightage in ECI sector



Source: Capitaline, Emkay Research

Factoring simple average, Funds are largely Underweight ECI sector for past 12 quarters



Source: Capitaline, Emkay Research

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