

Company Flash

19 February 2007 | 6 pages

ABB(India) (ABB.BO)

Buy: Another Strong Quarter, PAT Up 43% YoY

- PAT up 43% YoY** — ABB (India) 4QCY06 PAT at Rs1.35bn (up 43% YoY) was 7% ahead of CIR estimate of Rs1.26bn on faster execution of orders leading to net sales of Rs14.3bn, which was 5% ahead of CIR estimates. CY06 PAT of Rs3.4bn (up 56% YoY) was 3% ahead of CIR estimate of Rs3.3bn.
- Strong order inflow momentum** — ABB (India) booked Rs14.1bn (up 40% YoY) of fresh orders in 4QCY06, ending the year with an order backlog of Rs33.7bn (up 60% YoY). In CY06, the company booked orders worth Rs56.2bn (up 50% YoY). Strong industrial growth and power capex imply future order inflows.
- Power capex: stronger for longer** — The power capex cycle will be stronger for longer as the first concrete numbers of the Ministry of Power's (MoP) generation targets for the XIIth Plan (FY12-17E) at 86.5GW has started trickling in, implying that capacity addition targets in the 10 years from FY07E-FY17E is likely to be 153.5GW, up 89% vis-à-vis that in FY97A-FY07E.
- Peak utilizations drive corporate capex** — India's industrial capex is set to take off driven by (1) a strong macroeconomic tail-wind, (2) peak industry utilizations and (3) strong corporate balance sheets. According to CRISINFAC, industrial capex is set grow 181% in FY06-10, up 181% over that in FY99-FY05.
- Maintain Buy/Low Risk rating** — Our target price of Rs4,400 is based on a P/E of 34.7x FY08E which is a ~50% premium to BHEL, in line with the premium over the last 3 years.

Buy/Low Risk	1L
Price (15 Feb 07)	Rs3,800.95
Target price	Rs4,400.00
Expected share price return	15.8%
Expected dividend yield	0.2%
Expected total return	16.0%
Market Cap	Rs161,091M US\$3,671M

Figure 1. ABB Statistical Abstract

Year to	Net Profit	EPS	EPS Growth	P/E	EV / EBITDA	P / Book	ROE	DPS	Div. Yield
31-Dec	(Rsmn)	(Rs)	(%)	(x)	(x)	(x)	(%)	(Rs)	(%)
CY05	2,187	51.60	45.28%	73.7	49.4	18.1	27.4%	8.00	0.2%
CY06E	3,316	78.24	51.64%	48.6	33.4	13.7	32.1%	9.00	0.2%
CY07E	4,845	114.32	46.11%	33.2	22.0	9.9	34.6%	10.00	0.3%
CY08E	6,943	163.82	43.30%	23.2	14.9	7.1	35.6%	11.00	0.3%
CY09E	9,159	216.10	31.91%	17.6	11.1	5.1	33.7%	12.00	0.3%

Source: Citigroup Investment Research

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

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Figure 2. ABB 4QCY06 Results

Year End Dec31 (Rsmn)	4QCY05	4QCY06	% Chg	4QCY06E	% Chg	Remarks
Order Backlog	21,032	33,723	60.3%			
Order Inflow	10,166	14,126	39.0%			
Net Sales	9,857	14,263	44.7%	13,545	37.4%	Sale 5% ahead of CIR estimates
(Inc)/Dec in Stock in Trade	(165)	(71)				
Raw materials	(6,850)	(10,431)	52.3%	(9,888)	44.4%	
<i>as a % of net sales</i>	71.2%	73.6%		73.0%		
Staff Cost	(493)	(657)	33.4%	(625)	26.7%	
<i>as a % of net sales</i>	5.0%	4.6%		4.6%		
Other Expenditure	(957)	(1,157)	20.9%	(1,219)	27.3%	
<i>as a % of net sales</i>	9.7%	8.1%		9.0%		
Total Expenditure	(8,466)	(12,316)	45.5%	(11,732)	38.6%	
EBITDA	1,392	1,947	39.9%	1,814	30.3%	
EBITDA margin%	14.1%	13.6%		13.4%		Marginally better than expectations
Depreciation	(62)	(71)	14.8%	(69)	11.3%	
EBIT	1,330	1,876	41.1%	1,745	31.2%	
EBIT margin%	13.5%	13.1%		12.9%		
Interest	(26)	(1)	-95.9%	(2)	-90.7%	
Other Income	159	174	9.4%	200	25.8%	
PBT	1,462	2,049	40.1%	1,942	32.8%	
PBT margin%	14.8%	14.4%		14.3%		
Tax	(516)	(699)	35.5%	(680)	31.7%	
Effective Tax Rate%	35.3%	34.1%		35.0%		
PAT	946	1,350	42.6%	1,262	33.4%	PAT 7% ahead of CIR estimates
Recurring PAT margin%	9.6%	9.5%		9.3%		

Source: 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 from 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.

Risk

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.

Other Companies: Valuation and Risks

Bharat Heavy (BHEL.BO, Rs2,386, Buy/Low Risk)

Valuation: Our target price for BHEL is Rs2,764. Our target P/E multiple of 23x FY08E EPS is based on continued strong order inflow and strong 1QFY07 ending order backlog of Rs393bn providing visibility for the next 2 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 of Rs2,767, BHEL would trade at an EV/EBITDA multiple of 14.1x FY08E in line with that of Larsen & Toubro and Suzlon.

Risk: We rate BHEL 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 Rs 393bn represents nearly 2 years sales and provides very good earnings visibility over the medium term.

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.
4. Over the short-term investor progress on order flows does influence sentiment and delays herein could dampen sentiment.

Appendix A-1

Analyst Certification

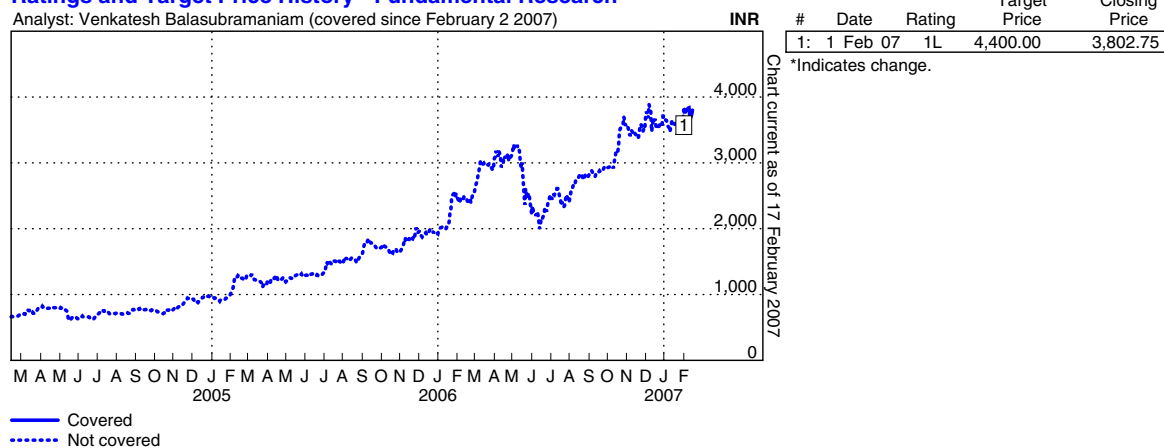
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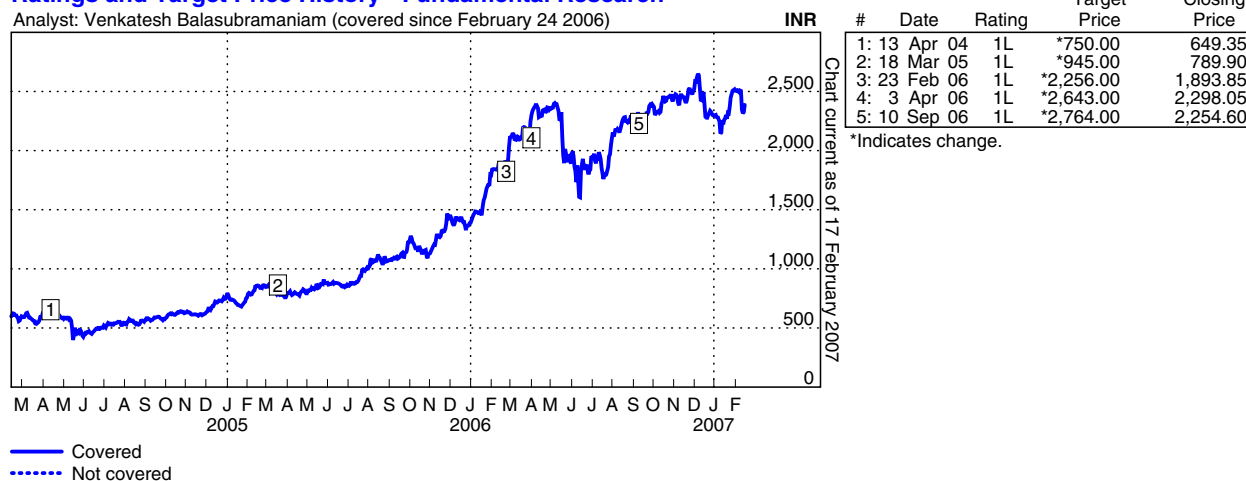
Analyst: Venkatesh Balasubramaniam (covered since February 2 2007)



Bharat Heavy Electricals (BHEL.BO)

Ratings and Target Price History - Fundamental Research

Analyst: Venkatesh Balasubramaniam (covered since February 24 2006)



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Data current as of 31 December 2006

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