

August 31, 2010

ACCUMULATE

MEDIUM RISK

PRICE Rs.87

TARGET Rs.102

ENGINEERING

SHARE HOLDING (%)

Promoters	45.7
FII	2.3
FI / MF	13.0
Body Corporate	7.4
Public & Others	31.6

STOCK DATA

Reuters Code	ELCN.BO	
Bloomberg Code	ELCN@IN	
BSE Code	505700	
NSE Symbol	ELECON	
Market Capitalization*	Rs. 8278 mn US\$ 171.9 mn	
Shares Outstanding*	92.85 mn	
52 Weeks (H/L)	Rs.111 / 70	
Avg. Daily Volume (6m)	197,320 Shares	
Price Performance (%)		
1M	3M	6M
(4)	13	15
200 Days EMA: Rs.84		

*On fully diluted equity shares

Part of  Classic



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Elecon Engineering Company Ltd (Elecon) is engaged in manufacturing of bulk material handling equipment (MHE) and industrial gears. Its product range in MHE segment includes design, engineering, manufacture, supply, erection and commission of wagon tipplers, wagon loader, stacker-reclaimer, barrel type reclaimer, roller screen, feeder, conveyors, idlers, pulley, scrapers, ship loaders etc. In Gear segment, Elecon manufactures worm, helical, spiral bevel, vertical roller mill drive, modular, planetary gear boxes, couplings and geared motors etc. With increasing investment in core sectors such as power, steel, port etc. and increasing visibility from its order book, we are re-instating our coverage on the stock.

DECENT ORDER BOOK WITH HEALTHY PIPELINE

Elecon has an order book position of about Rs. 15.8 bn, which includes about Rs. 6 bn worth of orders added during Q1FY11. Out of the current order book, the MHE orders stand at Rs.12.5 bn and the gears division orders stand at about Rs.3.3 bn. The current execution period for MHE orders is about 18-24 months, while the gears division orders are executed in 10-12 months. Moreover, the Company has submitted bids worth Rs. 25 bn, which are likely to be finalized in next 3-4 months. Elecon expects to get at least Rs. 6.5 to 7 bn worth of orders from the current bids, while the MHE order inflows for FY11 is expected to be at Rs.10 bn. Given its current order book position and healthy pipeline, we expect a decent Revenues growth for the next two years.

HUGE INVESTMENT IN CORE SECTORS TO DRIVE MHE BUSINESS

The MHE business would grow at a decent pace, driven by strong growth expected from core sectors such as power, steel and mining etc. The MHE contributes about 10-12% of overall investment in power plant, which is going to be significant opportunities for MHE players. The demand from the steel sector was sluggish in the recent past as no major green field expansion happened. However, with improved economic scenario which is moving towards growth phase, the steel sector would also create huge demand for the MHE players. Elecon is very well placed to grab the opportunities coming out from power as well as steel segments for its MHE business.

MUTED FY10 PERFORMANCE BUT WORST IS OVER

During FY10, the Company has reported 9.6% growth in its revenues to Rs. 10463.7 mn. Its MHE Revenues grew by 10.7% to Rs.6204.5 mn, while Revenues from gears division grew by 8% to Rs.4259.2 mn. During the period, its EBITDA grew by just 0.3% to Rs.1495.5 mn, while its EBITDA margins declined by 130 bps to 14.3%. Its PBT (including other income) fell by 15.6% to Rs.743.6 mn while its APAT for FY10 fell by 12.6% to Rs.502 mn. However, its RPAT including the Rs. 159.6 mn profits from sale of investment increased by 15.2% to Rs. 661.7 mn. The major reason for a disappointing performance in FY10, apart from muted growth in orders & delay in execution, was the higher proportion of buy-outs in its Revenues (with low margins). However, we believe the worst is over and going forward, Elecon's performance is expected to improve substantially given its strong order book position & relatively very low level of buy-out component in its order book.

EXCELLENT Q1FY11 PERFORMANCE

During Q1FY11, its Revenues increased by 15.9% YoY to Rs. 2,460.5 mn. The revenues from MHE business increased by 19.2% YoY to Rs. 1450.4 mn, while the revenues from gear division grew by 11.4% to 1010 mn. Its EBITDA increased by 12.9% to Rs. 367.9 mn, while EBITDA margins stood at 15%. However, its APAT increased by strong 56.7% to Rs.133.2 mn, mainly due to lower interest cost (at Rs. 98.5 mn against 144.2 mn in Q1FY10).

OUTLOOK & VALUATION

Elecon is one of the leading players and supplies MHE equipment to industries such as power, steel, mining, port etc. The current order book and pipeline provide strong Revenues growth visibility for next two years. We expect its Revenues to grow at 16.7% in FY11E to Rs. 12,215.7 mn and 18% in FY12E to Rs. 14,420.3 mn, while its APAT to grow at 48.4% in FY11E to 745.1 mn & 26.8% in FY12E to Rs. 945.1 mn. At the CMP of Rs. 87, the stock is trading at a valuation of 10.8x & 8.5x its FY11E & FY12E Earnings of Rs. 8.0 & Rs. 10.2 respectively. We re-instate our coverage on the stock with an 'ACCUMULATE' rating and a price target of Rs. 102 (10x FY12E EPS).

KEY FINANCIALS

Y/E Mar	Revenue (Rs mn)	APAT (Rs mn)	AEPS (Rs)	AEPS (% Ch.)	P/E (x)	ROCE (%)	ROE (%)	P/BV (x)
FY10	10463.7	502.2	5.4	(12.6)	16.1	14.8	15.4	2.5
FY11E	12215.7	745.1	8.0	48.4	10.8	17.9	19.7	2.1
FY12E	14420.3	945.1	10.2	26.8	8.5	20.1	20.9	1.8

QUARTERLY STATEMENT

(Rs.mn)

Y/E March	Q1FY10	Q4FY10	Q1FY11
Net Sales	2,122.9	3,290.9	2,460.5
(%) YoY	25.9	14.1	15.9
Total Expenditure	1,797.0	2,853.9	2,092.6
PBIDT	325.9	437.0	367.9
(%) Margin	15.3	13.3	15.0
Interest	144.2	117.3	98.5
PBDT	181.7	319.7	269.4
Depreciation	74.9	95.3	89.2
Other Income	21.9	34.5	11.3
PBT incl OI	128.7	258.9	191.5
Tax	43.7	70.5	58.4
(%) of PBT	33.9	27.2	30.5
APAT	85.0	188.4	133.2
Non-Recurring Items	0.0	(82.3)	0.0
RPAT	85.0	270.7	133.2

PROFIT & LOSS STATEMENT

(Rs.mn)

Y/E March	FY09	FY10	FY11E	FY12E
Revenues	9,550.6	10,463.7	12,215.7	14,420.3
Total Operating Cost	6,319.8	7,284.3	8,453.3	10,022.1
Employee Cost	438.3	435.2	487.4	565.4
Other Expenditure	1,302.1	1,248.6	1,373.5	1,565.8
PBIDT	1,490.4	1,495.5	1,901.5	2,267.0
EBIDTA (%)	15.6	14.3	15.6	15.7
Interest	483.7	508.9	470.0	479.4
Depreciation	221.5	331.2	397.4	457.1
PBT excl OI	785.2	655.5	1,034.1	1,330.6
Other Income	95.8	88.1	86.4	90.7
PBT incl OI	881.0	743.6	1,120.4	1,421.2
Tax	306.5	241.4	375.4	476.1
APAT	574.5	502.2	745.1	945.1
APAT %	6.0	4.8	6.1	6.6
Extraordinary Items	0.0	(159.6)	0.0	0.0
RPAT	574.5	661.8	745.1	945.1

BALANCE SHEET STATEMENT

(Rs.mn)

As on 31st March	FY09	FY10	FY11E	FY12E
Equity Share Capital	185.7	185.7	185.7	185.7
Reserves & Surplus	2568.3	3075.3	3603.1	4331.0
Networth	2754.0	3261.1	3788.9	4516.7
Secured Loans	5236.1	3328.8	3228.8	3028.8
Unsecured Loans	684.7	1887.0	1887.0	1887.0
Capital Employed	8674.8	8476.8	8904.6	9432.5
Net Block	2829.1	3443.4	3746.0	3688.9
Cap. WIP	281.1	178.8	150.0	150.0
Investments	108.7	56.8	56.8	56.8
Inventories	4007.5	3151.8	3088.8	3243.2
Sundry Debtors	4717.4	5175.9	5693.4	6262.8
Cash and Bank	610.6	388.2	475.7	781.1
Loans & Advances	749.2	546.8	623.4	685.7
Current Liab. & Prov	4317.7	4088.2	4497.0	4946.7
Net Current Assets	5766.9	5174.5	5384.3	6026.0
Deferred Tax Assets (Net)	(327.8)	(402.6)	(447.4)	(504.3)
Miscellaneous Exp	16.9	26.0	15.0	15.0
Total Assets	8674.8	8476.8	8904.6	9432.5

FINANCIAL RATIO STATEMENT

Y/E March	FY09	FY10	FY11E	FY12E
Growth (%)				
Net Sales	15.6	9.6	16.7	18.0
EBITDA	(14.5)	(12.6)	48.4	26.8
Adjusted Net Profit	14.2	0.3	27.1	19.2
Profitability				
EBIDTA Margin (%)	15.6	14.3	15.6	15.7
Net Profit Margin (%)	6.0	4.8	6.1	6.6
ROCE (%)	15.7	14.8	17.9	20.1
ROE (%)	20.9	15.4	19.7	20.9
Per Share Data				
EPS (Rs.)	6.2	5.4	8.0	10.2
CEPS (Rs.)	9.9	11.5	12.8	15.7
BVPS (Rs)	29.7	35.1	40.8	48.6
Valuation				
PER (x)	14.1	16.1	10.8	8.5
PEG (x)	(1.0)	(1.3)	0.2	0.3
P/BV (x)	2.9	2.5	2.1	1.8
EV/EBITDA (x)	8.9	8.6	6.7	5.4
EV/Net Sales (x)	1.4	1.2	1.0	0.8
Turnover				
Debtor Days	178	178	168	156
Creditor Days	154	133	125	117
Gearing Ratio				
D/E	2.1	1.6	1.4	1.1

Source: Company, Sushil Finance Research Estimates

Rating Scale

This is a guide to the rating system used by our Equity Research Team. Our rating system comprises of six rating categories, with a corresponding risk rating.

Risk Rating

Risk Description	Predictability of Earnings / Dividends; Price Volatility
Low Risk	High predictability / Low volatility
Medium Risk	Moderate predictability / volatility
High Risk	Low predictability / High volatility

Total Expected Return Matrix

Rating	Low Risk	Medium Risk	High Risk
Buy	Over 15 %	Over 20%	Over 25%
Accumulate	10 % to 15 %	15% to 20%	20% to 25%
Hold	0% to 10 %	0% to 15%	0% to 20%
Sell	Negative Returns	Negative	Negative
Neutral	Not Applicable	Not Applicable	Not Applicable
Not Rated	Not Applicable	Not Applicable	Not Applicable

Please Note

Recommendations with "Neutral" Rating imply reversal of our earlier opinion (i.e. Book Profits / Losses).

** Indicates that the stock is illiquid With a view to combat the higher acquisition cost for illiquid stocks, we have enhanced our return criteria for such stocks by five percentage points.

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