

Asia Pacific Equity Research 15 May 2007

Suzion Energy Ltd

Margin pressures in Wind business lead to disappointment - ALERT

- Earnings disappoint: Suzlon reported FY07 net earnings of Rs8.6B, up 17% Y/Y and 25% below our estimate of Rs11.3B. Lower-than-expected sales (Rs80B vs our estimate of Rs86B) and margin pressures in the wind business were the key reason for the variance from our estimate.
- Margin drop in wind business: Suzlon reported 16.7% EBITDA margin for its wind business vs our estimate of c20% and the company's earlier guidance of 20%-21%. Key items impacting the reported EBITDA margins were: 1) in-transit inventory of 222MW -100bp negative impact; 2) FX- 40bp; 3) increase in tower costs in the international business- 50bp; 4) component (bearings) supply issue in the domestic market- 50bp; and 5) set-up expenses for international business (organization set up for 2,500MW, and slower-than-expected pick-up in US production) 100bp.
- Outlook on volume growth remains healthy on the back of a strong macro environment: Suzlon's current orderbook of Rs94.8B is 1.2x FY07E sales. The company in the conference call indicated that it will look to operate near its full capacity of 2,700MW going ahead (vs FY07 sales volumes of 1,456MW). The macro environment for wind power projects remains positive. Global wind industry recorded a 31% Y/Y growth in installations driven by US, Europe, China, and India.
- Capacity expansion remains on track: Suzlon's capacity expansion program of achieving 4,200MW by 4Q FY08 remains on track. The company is also backward integrating into foundry, forging and machining business in order to secure component supplies for its domestic and international business. The facility is expected to come up by 4Q FY08. Hansen's capacity too is being expanded to 9,300MW with a 3,500MW proposed expansion in India (expected by 4Q FY09).
- **REpower bid resolution by May 24, 2007:** The final resolution of REpower's bid is only expected by May 24, 2007 when the extended grace period expires. There is already newsflow in *Financial Times* that Areva might be looking to increase its bid beyond Suzlon's offer of €150/share.

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Underweight

Rs1,138.30

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Table 1: P&L Consolidated

Rs in millions, year-end March

	4Q FY06	4Q FY07	% Y/Y	FY06	FY07	% Y/Y
Net Sales	15,263	29,159	91%	38,410	79,857	108%
Inc/dec in stock	265	3,890		2,200	11,028	
Consumption of RM	(9,071)	(21,749)	140%	(25,479)	(59,142)	132%
Total Raw Materials	(8,806)	(17,858)	103%	(23,279)	(48,114)	107%
Staff Cost	(418)	(1,838)	340%	(1,216)	(6,496)	434%
Other Cost	(2,073)	(4,510)	118%	(5,263)	(12,290)	133%
Total Expenditure	(11,297)	(24,206)	114%	(29,758)	(66,899)	125%
EBITDA	3,966	4,954	25%	8,652	12,958	50%
EBITDA Margin	26.0%	17.0%		22.5%	16.2%	
Other Income	338	463	37%	556	965	73%
Interest	(133)	(972)	631%	(508)	(2,523)	397%
Depreciation	(277)	(600)	116%	(716)	(1,718)	140%
PBT	3,894	3,846	-1%	7,985	9,683	21%
Тах	(141)	(256)	81%	(568)	(1,035)	82%
Tax Rate	4%	7%		7%	11%	
PAT	3,753	3,590	-4%	7417	8,648	17%
Less Minority share	(37)	0		(10)	(8)	
Net Profit	3,715	3,590	-3%	7407	8,640	17%
Net Margin	24.3%	12.3%		19.3%	10.8%	
As % of sales						
RM	57.7%	61.2%		60.6%	60.2%	
Staff Cost	2.7%	6.3%		3.2%	8.1%	
Other Costs	13.6%	15.5%		13.7%	15.4%	

Source: Company Reports

Table 2: Segment Results

Rs in millions, year-end March

Revenues	4Q FY06	4Q FY07	% Y/Y	FY06	FY07	% Y/Y
WTG	15,076	21,950	46%	37,917	59,986	58%
Gearbox		6,508		-	18,561	NA
Others	188	706	277%	499	1,321	165%
Total	15,264	29,164	91%	38,417	79,868	108%
EBIT						
WTG	3,887	3,806	-2%	8,631	10,192	18%
Gearbox		1,434		-	2,918	NA
Others	387	285	-26%	433	391	-10%
EBIT Margin						
WTG	25.8%	17.3%		23%	17.0%	
Gearbox	NA	22.0%		NA	15.7%	
Others	206.5%	40.3%		87%	29.6%	

Source: Company Reports

Table 3: Wind Business

Rs in millions, year-end March

Wind business	FY06	FY07	% Y/Y
Sales	38,410	61,300	60%
EBITDA	8,650	10,210	18%
EBITDA Margin	22.5%	16.7%	
PBT	7,980	8,780	10%
Тах	(570)	(530)	-7%
Tax Rate	7%	6%	
PAT	7,600	8,250	9%

Source: Company reports

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Price Target

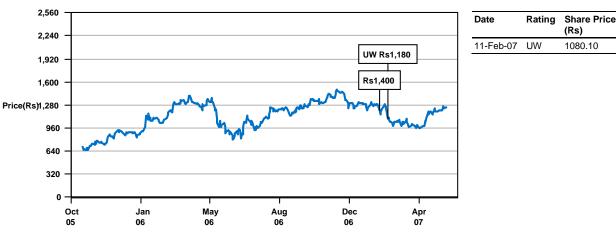
(Rs)

1180.00

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Suzlon Energy Ltd (SUZL.BO) Price Chart

Source: Reuters and JPMorgan; price data adjusted for stock splits and dividends. Initiated coverage Feb 11, 2007. This chart shows JPMorgan's continuing coverage of this stock; the current analyst may or may not have covered it over the entire period. JPMorgan ratings: OW = Overweight, N = Neutral, UW = Underweight.

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