India Equity Research | Engineering & Capital Goods | Initiating Coverage

Siemens India

INR 1,250

Edelweiss
Ideas create, values protect

Building cities

ACCUMULATE

November 6, 2006

Priyanko Panja
+91-22-2286 4300
priyanko.panja@edelcap.com

Siddharth Sanghvi
+91-22- 2286 4397
siddharth.sanghvi@edelcap.com

Hiral Desai
+91-22- 2286 4537
hiral.desai@edelcap.com

Opportunities unlimited; prominent play across infrastructure and corporate capex

India is in the middle of a transitional boom in the infrastructure space with expected investment of ~ INR 14 tn (Edelweiss estimates) in the next six years. While the infra opportunity for Siemens India (SIL) is estimated at INR 9 tn, its addressable market for Automation stand at ~ INR 45 bn. We believe strong tailwinds in the core businesses (power, automation & drives, and engineering) is likely to drive SIL's growth in the future.

Stellar performance from IT portfolio

The company's information technology (IT) portfolio has grown at a CAGR of 46% over past three years and contributed one-fourth to consolidated revenues in FY05 . The IT part of SIL's business has caught tremendous traction and the secular nature of the business reinstates our belief of a robust performance going ahead. We remain positive on SIL's IT business and have estimated a CAGR of ~ 38% over FY04-08E. Given that the IT space has operating margin of ~ 20% plus, it is likely to contribute ~ 40% *plus* of SIL's consolidated EBIT mix.

Consolidation strategy: A value-accretive move

SIL, in the recent past, has made strategic investments to enhance its portfolio and consolidate its position in India. We are likely to see significant improvement in the return ratios, post consolidation of businesses, given that its IT arm (SISL) has excellent return ratios and significant growth opportunities. Further, quite a few of Siemens AG's group companies, having presence in India, can be consolidated with SIL, going forward. We believe the consolidation of group companies with SIL is likely to improve group synergies, thus enhancing shareholders' value.

Attractive plays available; initiate with 'ACCUMULATE'

The current order backlog, expected robust order intake, and continuing stellar performance from its subsidiary portfolio comforts us on estimating consolidated revenue CAGR of 28% and profit CAGR of 32% over the next two years. Given SIL's diversified business portfolio, we have valued it on the basis of sum-of-the-parts (SOTP) valuation. On our SOTP valuation of INR 222 bn, we expect limited upside from current valuations, given that there are attractive plays of similar scalability and size in the Indian engineering space, which are available at a discount to SIL. We initiate coverage on Siemens with an **'ACCUMULATE'** recommendation.

Reuters	:	SIEM.BO
Bloomberg	:	SIEM IN

Market Data

52-week range (INR)	:	1,262 / 741
Share in issue (mn)	:	168.6
M cap (INR bn/USD mn)	:	210.7/4,764.3
Avg. Daily Vol. BSE/NSE ('000)	:	406.0

Share Holding Pattern (%)

Promoters	:	55.2
MFs, FIs & Banks	:	15.2
FIIs	:	12.3
Others	:	17.3

Financials

Year to September	FY05	FY06E	FY07E	FY08E
Revenue (INR mn)	36,781	55,470	71,630	91,494
Rev. growth (%)	*61.4*	*50.8*	*29.1*	*27.7*
EBITDA (INR mn)	4,718	7,356	9,671	12,673
Net profit (INR)	3,092	5,501	7,368	9,539
Shares outstanding (mn)	166	169	169	169
EPS (INR mn)	18.7	32.6	43.7	56.6
EPS growth (%)	*82.5*	*74.9*	*33.9*	*29.5*
P/E (x)	67.8	38.7	28.9	22.3
EV/ EBITDA (X)	43.8	28.1	21.4	16.3
ROAE (%)	38.0	49.9	48.4	45.8
ROACE (%)	46.8	52.5	50.5	49.8

Investment Rationale

Opportunities unlimited; prominent play across infrastructure and corporate capex

Addressable market INR 9 tn

India is in the middle of a transitional boom in the infrastructure space with expected investment of ~ INR 14 tn (Edelweiss estimates) in the next six years. Out of the total INR 14 tn, Siemens India (SIL) has presence in power, railways, urban infrastructure, and telecom space, the investment on which is estimated to be ~ INR 9 tn. In FY05, the above verticals *(Infrastructure includes telecom, power, transport, building technologies and real estate segments)* accounted for 48% and 43% of SIL's standalone and consolidated revenues, respectively. Apart from huge opportunities across the infrastructure space, we believe SIL's automation division is likely be a beneficiary of the upcoming corporate capex programmes including modernization/upgradation of automation processes, especially in the metal sector. The addressable automation market currently pegged at INR 45 bn is expected to grow at CAGR of over 20% in the medium term. We believe strong tailwinds in core businesses (power, automation & drives, and engineering) is likely to drive SIL's growth in the future.

Table 1: Expected investment on infrastructure in India

Sectors	*FY06E-FY12E (INR bn)*	USD bn
Roads	1,520	34
Power*	4,812	107
Railways*	1,100	24
Telecom*	1,227	27
Aviation	370	8
Ports	800	18
O&G	2,201	49
Urban Infra*	1,974	44
Total spend	**13,973**	**311**

Source: RBI, Edelweiss research

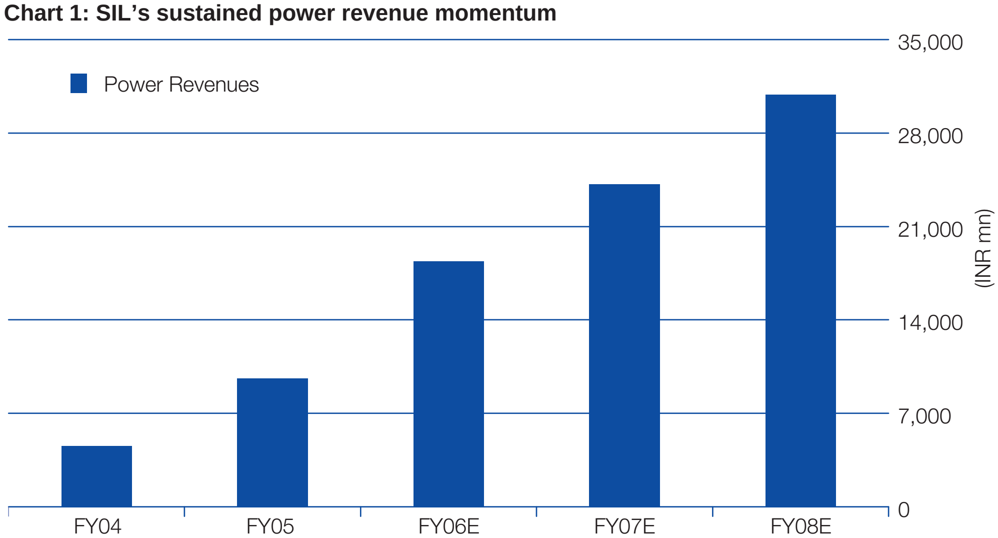
*Note: (1) * Siemens has presence in these verticals. (2) # USD/INR rate of 45*

Powerful growth ahead

Powering 45% CAGR over FY05-08E

Given that power sector reforms continue to remain high on the government's agenda, we believe the envisaged thrust augurs well for SIL's power business. In the power space, SIL provides automation solutions in the form of equipment like switchgears, switchboards, meters, and industrial turbines for a wide range of applications in power plants.

Chart 1: SIL's sustained power revenue momentum



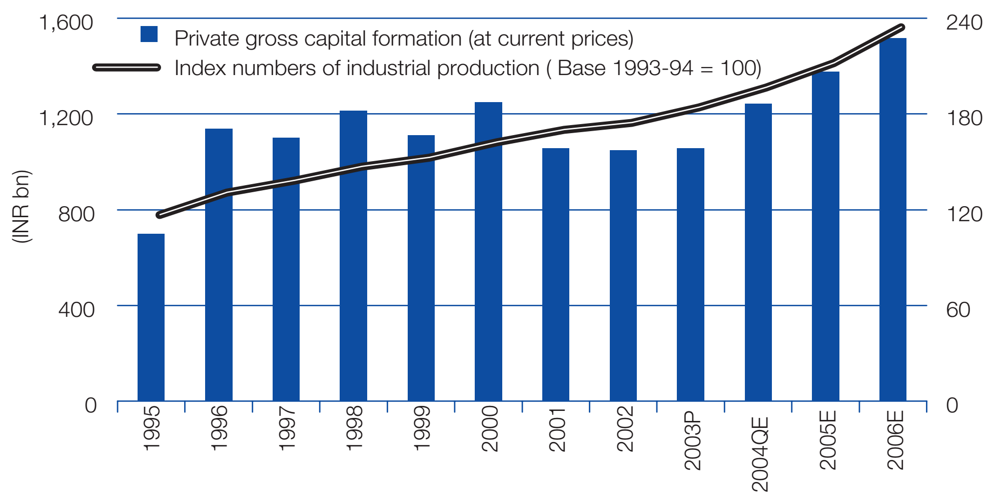
Source: Edelweiss research

Power operations contributed one-fourth of SIL's consolidated revenues in FY05. Growing at a CAGR of 35% over the past three years, this segment continues to remain SIL's core business growth driver. We expect it to register revenue of INR 24 bn and INR 31 bn in FY07E and FY08E, respectively, a CAGR of 48% over FY05-08E.

Automation momentum to continue

We expect the upward momentum in corporate capex to continue, based on rapid infrastructure-led growth, providing huge potential to the automation and drives segment. Along with the new capex, efficiency-driven capex of existing manufacturing and process facilities in the corporate sector is gathering pace. The INR 45 bn Indian automation industry is currently going through a boom and is expected to grow at CAGR of over 20% in the medium term. Currently, SIL has a market share of ~25% (ABB is the leader with ~40% share) and we expect this to improve further on back of an improving product profile.

Chart 2: Private gross capital formation and industrial production



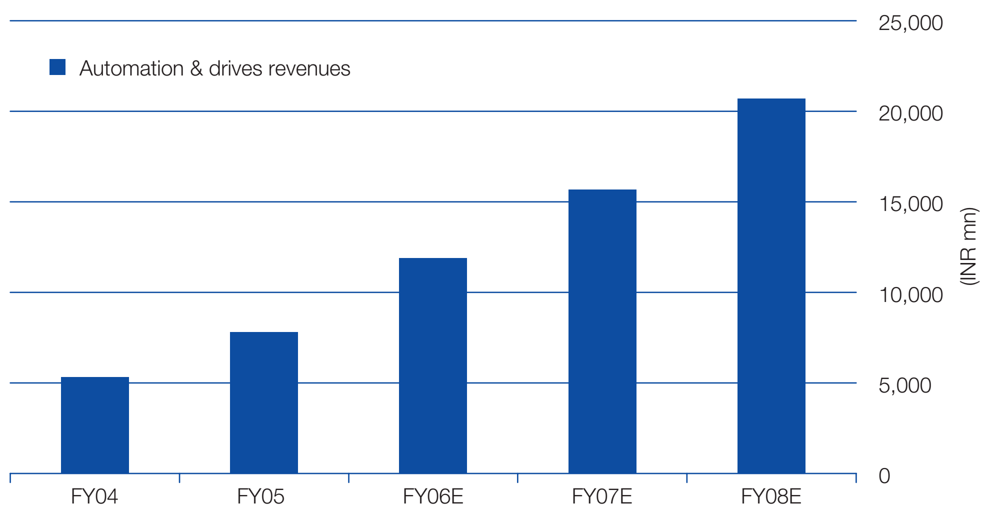
Source: Central Satistical Organisation of Industrial Production (Base 1993-94 - 100)

Note: P: provisional estimates, RBI; QE: quick estimates, RBI.

Corporate capex and metal sector capex to boost opportunities

We have estimated automation revenue to grow at a CAGR of 39% over FY05-08E. We are likely to see strong growth in corporate expansion plans, especially in process industries and metal-related sectors. Margins and growth momentum for SIL's diverse application portfolio is likely to be stronger than ever.

Chart 3: SIL's growing automation and drives revenues



Source: Edelweiss research

Newer growth opportunities

Additionally, the company has recently entered the lucrative building technologies and security space. With India continuing to emerge as the globally preferred destination for back office activities, information hubs and R&D, leading domestic and international companies are making large infrastructure investments in this space. Although the electronic security systems market in India is at a nascent stage, it is currently pegged at INR 5.8 bn and expected to grow at a CAGR of 25-30% in the medium term. This is a new growth trajectory for SIL and it currently holds about 9% market share in this space. However, given the low base, we believe the company's market share in this space is likely to grow gradually and expect it to outperform the market in terms of growth. With SIL entering into higher end-to-end security service contracts, we expect margins to improve, going forward. Although the initial investment is high, higher sales volumes will lead to economies of scale, plus the higher margin service contracts will improve profitability and return ratios for the segment.

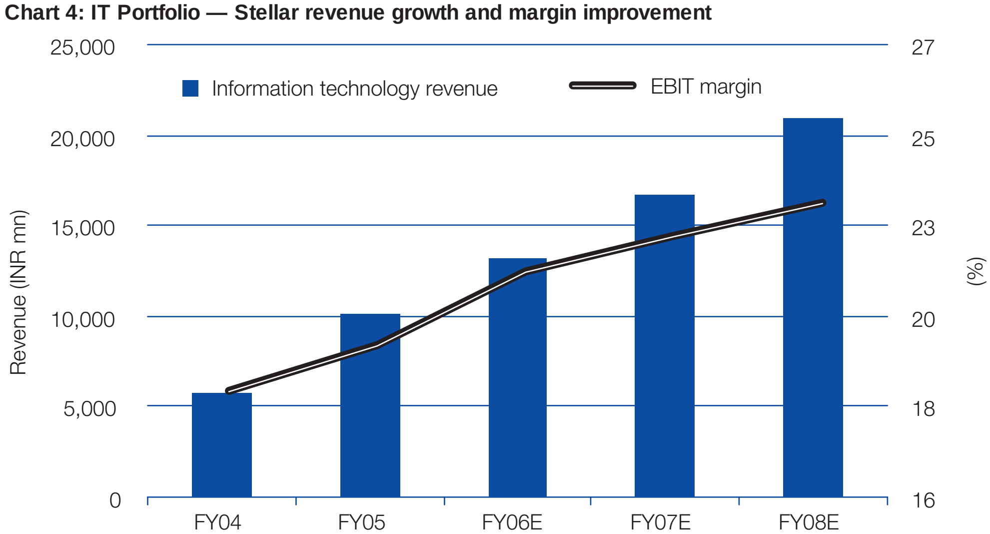
Stellar performance from IT portfolio

From hardware to software

The consolidated story for SIL has been the IT revolution (SISL, SBPO, SPCNL and IT related standalone service portfolio). Over the past three years, the company's IT portfolio has grown at a CAGR of 77% (information and communication) and 36% (information technology services) and contributed one-fourth to consolidated revenues. The IT part of SIL's business has caught tremendous traction and the secular nature of the business reinstates our belief of a robust performance going ahead. With SIL's business services division SBS (the information technology arm of Siemens AG) undergoing a restructuring plan, all its business is likely to be executed by Siemens Information Systems Limited (SISL). The parent (Siemens AG) has been focusing on sustained movement of headcount to low-cost countries, especially for its information technology business. Around 80% of SISL's revenue comes from the international market. Given the distinct cost advantage and huge international growth opportunities available through SBS, we believe SISL is likely to become the IT outsourcing hub for Siemens AG.

Siemens Public Communication Networks Pvt. Ltd. (SPCNL), acquired by SIL in April 2005, represents the information and communication arm of SIL's business along with its standalone information and communication division. We expect the domestic telecom market to grow at ~15% for the next five years. Further growth could be expected from high-end networking and convergence solutions (SIL is the market leader in the space), where the company is looking to tap fast-growing market segments like call centres, hospitality & convergent voice, and data & video communications.

Chart 4: IT Portfolio — Stellar revenue growth and margin improvement



Source: Edelweiss research

We remain positive on the IT business of SIL and have estimated a CAGR of ~ 38% over FY04-08E. Given that the IT space has an operating margin of ~ 22-23%, it is likely to contribute almost 40% plus to SIL's consolidated EBIT mix.

Consolidation strategy: A value-accretive move

SIL has been on a consolidation drive over the past couple of years, which we believe is likely to enhance shareholders' value. Some of the highlights of consolidation over the past two years are:-

Table 2: Current consolidated portfolio

Company	Stake (%)	Brief description
Siemens Information Systems (SISL)	100	Systems integrator and total solutions provider, having extensive domain expertise and technology specialisation. Provides solutions for clients primarily in the fields of telecommunications, healthcare, manufacturing, utilities, public sector and government
Siemens Public Communication Networks (SPCNL)	100	Provider of network equipment including supply, design and installation; portfolio comprises wireline, transmission, access, mobile and IP products etc
Siemens BPO Services (SBPO)	51	Provides back office and customer contact services to Siemens operating companies mainly in the US, with the necessary technology and process competence
Siemens Industrial Turbomachinery Services (SITS)#	51	Specializes in the service, repair and overhaul of small gas turbines and rotating equipment
Siemens VDO Automotive (SVDO)	Merged	Provides precision and control automotive information systems; competence to combine advanced electronics with precision mechanics
Flender*	50	Manufacture of industrial gear boxes, couplings and has a CAD centre at Chennai

Source: Company, Edelweiss research

*Note: (1) * additional 50% assumed to be acquired after 1/10/2006. (2) # additional 23% assumed to be acquired in FY07E*

SIL, in the recent past, has made strategic investments to enhance its portfolio and consolidate its position in India. Post acquiring 100% stake in Siemens Information Systems Limited (SISL) in FY03, SIL has gone ahead and merged Demag Delaval Industrial Turbomachinery (DDIT) with itself, thus entering into the business of industrial turbines. It also acquired 100% stake in Siemens Public Communication Networks (SPCNL) and 51% stake in Siemens BPO Services (SBPO) from Siemens AG.

We are likely to see significant improvement in the return ratio, post consolidation of businesses, given that its IT arm—SISL—has an excellent return ratio and significant growth opportunities.

Table 3: Siemens' subsidiary portfolio

Subsidiary	SISL		SBPO		SPCNL		SITS		Flender	
	FY06E	FY07E	FY06E	FY07E	FY06E	FY07E	FY06E	FY07E	FY06E	FY07E
Revenues (INR mn)	8,471	10,677	416	707	2,896	3,418	183	238	1,114	1,448
PAT (INR mn)	1,777	2,352	56	95	336	406	24	33	118	158
ROCE (%)	82.4	85.1	31.1	35.8	20.4	21.0	22.5	25.5	12.1	14.6

Source: Edelweiss research

Further, quite a few of Siemens AG's group companies, having presence in India, can be consolidated with SIL, going forward. We believe the consolidation of group companies with SIL is likely to improve group synergies, thus enhancing shareholders' value.

Table 4: Consolidating opportunities from Siemens AG

Company	Shareholding	Business description
Osram India	Osram AG 100% (Osram AG is a 100% Siemens AG company)	Product portfolio includes incandescent, fluorescent and compact fluorescent lamps, 734 employees and manufacturing plant at Sonepat, Haryana
Siemens Hearing Instruments	Siemens Audiologische Technik GmbH 100%	Offers hearing aids from the In the canal (ITC) to In the ear (ITE) and Behind the Ear (BTE) hearing devices
Siemens Power Engineering	Siemens AG 100%	Undertakes total power plant engineering activities from concept to commissioning. Supports AG's power generation (PG) business process worldwide
Powerplant Performance Improvement	Siemens AG 50% + 1 share BHEL 50% - 1 share	Offers engineering solutions for upgrading, renovating and refurbishment of power plants
Siemens Corporate Finance	Siemens AG 100%	Partners with Siemens AG Corporate Finance in providing value-added services to various sub functional areas within treasury, reporting and taxes and strategy consulting

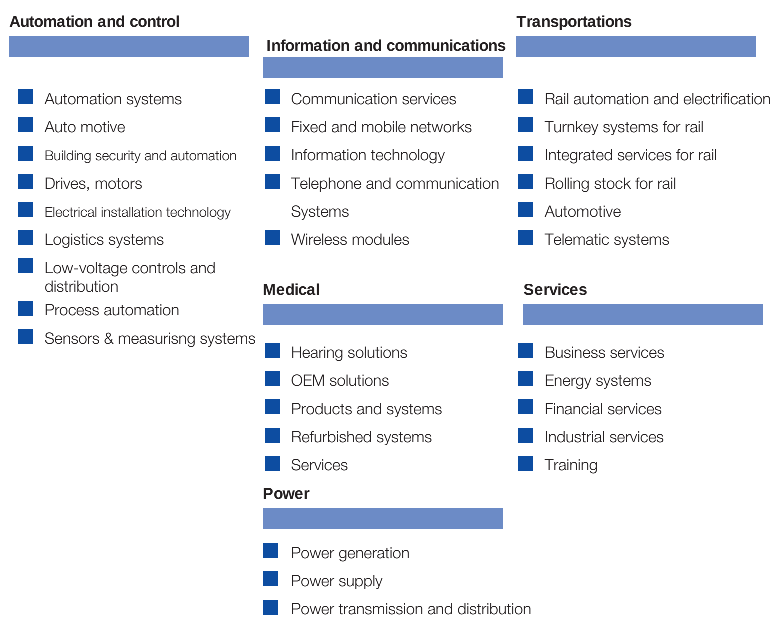
Source: Company, Edelweiss research

Strong global parentage…outsourcing hub in the making

Leveraging the global parentage

SIL is a part of the global powerhouse in electrical engineering and electronics, Siemens AG, headquartered at Berlin and Munich. The parent (Siemens AG) founded more than 155 years ago, currently operates in over 190 countries across the globe. In fiscal 2005 (ended September 30) Siemens AG had sales of Euro 75.4 bn and net income of Euro 2.2 bn. The company has a taskforce of 461,000 employees working to develop and manufacture products, design and install complex systems and projects, and tailor a wide range of services for individual requirements. The group boasts of a product portfolio unmatched across the globe, making it one of the largest global conglomerates.

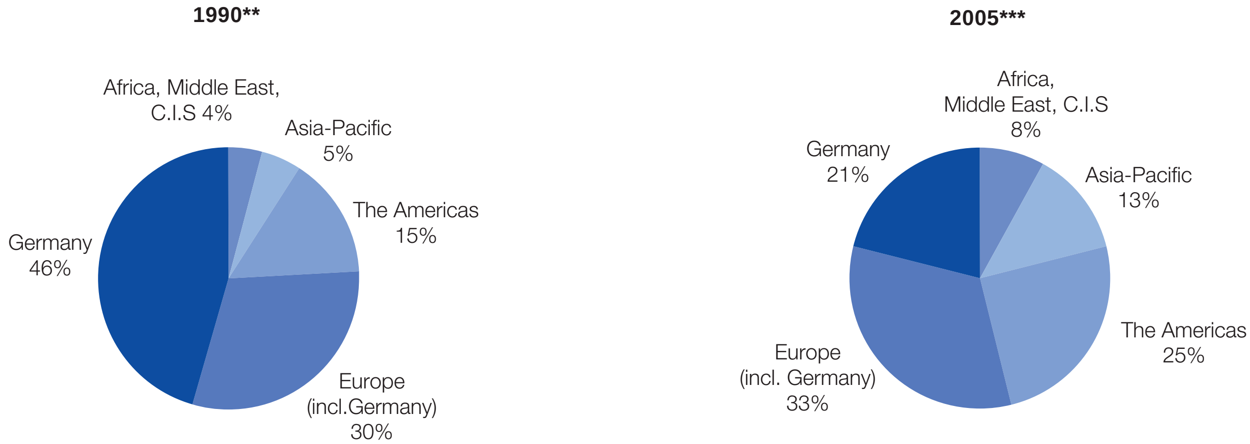
Fig. 1: Product and service offerings by Siemens AG



Source: Company, Edelweiss research

Asia, and in particular India and China, has emerged as a key market for Siemens AG. In 2005, the Asia-Pacific region comprised 13% of Siemens' global revenues of Euro 75 bn. Of this, around Euro 830 mn came from SIL.

Chart 5: Sales by region



Source: Company, Edelweiss research

*Note: (1) ** Sales as determined under German Commercial Code* *(2) *** Sales as determined under U.S. GAAP*

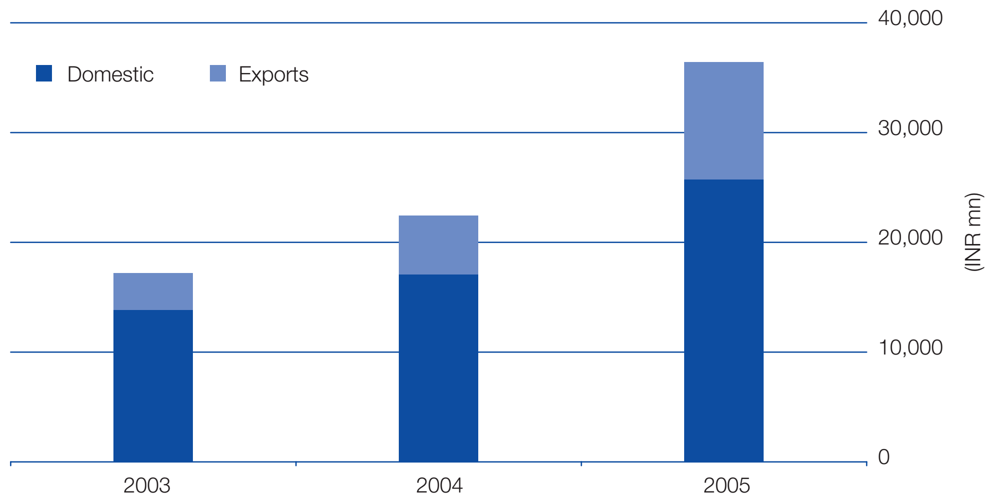
Advantage India

India is emerging as a prominent base for various outsourcing needs of Siemens AG.

- SIL's Gurgaon centre has been recognized as a 'competence centre' for high voltage turnkey solutions.
- The Goa centre has been identified as a 'global competency centre' for mobile X-ray generators.
- The Aurangabad works have been recognized as a major supply source for switchgears for exports to Siemens AG.
- The plant being set up in Vadodra will supply turbine components to Siemens' facilities in Europe.

Importance of exports in SIL's revenues has been growing over the years. In FY05, exports nearly doubled to INR 10 bn and comprised 29% of total revenues.

Chart 6: Consolidated revenue break-up — Domestic versus export (SIL)



Source: Company, Edelweiss research

Going forward, we believe that SIL will continue to gain further importance in its parent's scheme of things, especially with huge infrastructure projects in India on the anvil. SIL is likely to benefit as Siemens AG's key partner in the joint bidding of international projects in certain geographies. We are likely to see the share of exports going up for SIL, with SISL (~ 80% plus revenue from exports) playing an important role in the consolidated revenue mix, higher regional outsourcing through other subsidiaries, and some of its standalone business divisions.

Financials

Order intake accretion improves revenue/earnings visibility

SIL witnessed a strong order inflow in FY05, which continued in FY06. We expect order intake of INR 79.6 bn in FY06E, a 93% increase over FY05. As a result, we are likely to see order backlog of INR 72.6 bn in FY06E. With strong tailwind in core businesses of power, automation and industrial solutions unfolding, we expect order intake of INR 270 bn over FY07-08E.

Table 5: Order book break-up

(INR bn)

Year to September	FY02	FY03	FY04	FY05	FY06E	FY07E	FY08E
Opening order backlog	7.9	6.6	9.1	21.3	35.1	72.6	137.8
Order intake	11.5	16.8	30.1	41.2	79.6	119.9	150.1
Execution	12.9	14.2	17.9	27.5	42.0	54.8	70.6
Closing order backlog	6.6	9.1	21.3	35.1	72.6	137.8	217.3

Source: Edelweiss research

Surging order book to push up execution pace, improving visibility

The current order backlog, expected robust order intake, and continuing stellar performance from its subsidiary portfolio comforts us on estimating consolidated revenue CAGR of 28.4% over the next two years, translating into revenue estimates of INR 91.5 bn in FY08. Of the total consolidated revenues, we expect the subsidiaries portfolio to contribute ~20% plus in the next two years, to be driven by strong performance from SISL and SPCNL.

On the margins front, we expect the standalone EBITDA margin to be soft by 95bps in FY06E at 9.2% on account of increase in input prices and improve moderately to 9.3% and 9.7% in FY07E and FY08E, respectively. However, on account of strong revenue growth ahead, we expect standalone net profit to grow by a CAGR of 30% to INR 5.5 bn in FY08E.

Despite lower EBITDA margin in standalone, we expect the consolidated EBITDA margin to improve and post in excess of 13% in FY07E and FY08E on account of better performance from its subsidiaries.

Led by the continuing stellar performance from SISL, we expect the share of subsidiaries in consolidated net profit before minority interest to be ~ 40% in FY07E and FY08E each. We expect SIL to post consolidated net profit of INR 7.4 bn and INR 9.5 bn in FY07E and FY08E, respectively.

Overall improvement in balance sheet size and return ratios

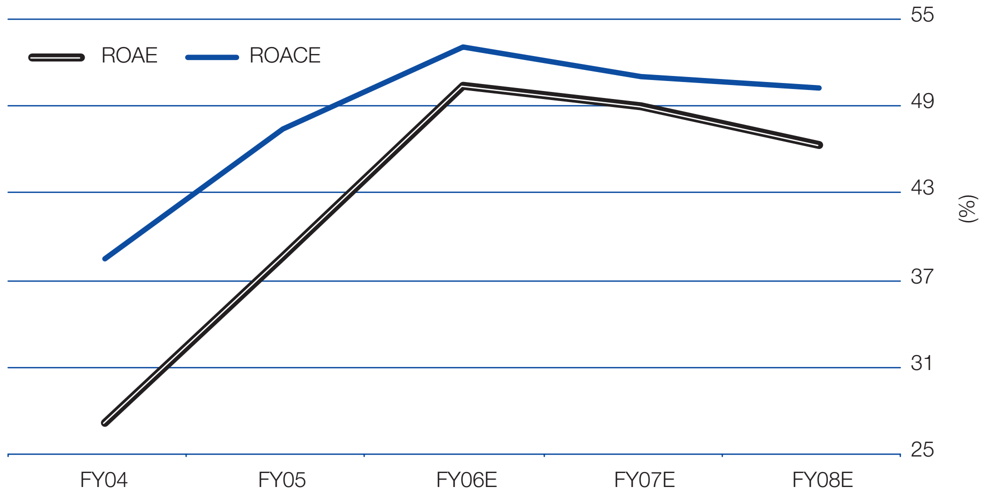
Unlocking a strong balance sheet to grow

SIL's consolidated reserves and surplus are estimated to increase by 2.6x over FY05-08E to INR 23 bn, which reflects the strength of the balance sheet. With SIL consistently generating positive free cash flows, we expect capex of INR 6 bn over the next two years to be funded through internal accruals. As a result, we do not expect the debt/equity ratio to increase further from 0.1.

SIL's return ratios improved significantly over FY03-05. Given that we expect the robust operation performance to continue in ensuing periods with capex plan to be funded through internal accruals, we expect the return ratio to improve further.

Chart 7: Improving return ratios

Greater operational efficiency seen boosting return ratios



Source: Company, Edelweiss research

Valuation

Sum-of-the-parts valuation

Given SIL's diversified business portfolio, we have valued it on the basis of sum-of-the-parts (SOTP) valuation to capture value of each of its verticals and subsidiaries.

Table 6: Sum-of-the-parts valuation

Business segment	Assumption for valuation	Multiple (x)	Value (INR mn)
Infrastructure Portfolio			
Power	Valued at 25% premium to BHEL's EV/EBIT (x)	23.9	45,329
Building Technologies	Valued at 3x sales	3.0	2,569
Real Estate	Net profits valued at bond yields	-	3,148
Transport	Valued at par with Sensex P/E one year forward	19.0	5,610
SITS	Valued at 2x equity investments	2.0	322
Flender	Valued at 2x equity investments	2.0	2,806
Sub total			**59,784**
IT Portfolio			
Information & Comm	Valued at mid cap sector market cap/ sales	2.0	3,865
SISL and SBPO	Valued at average IT sector P/E one year forward	17.0	41,607
SPCNL	Valued at 3x sales	3.0	10,253
Sub total			**55,725**
Automation Segment			
Automation & Drives	Valued at 25% premium to ABB's EV/EBIT (x)	30.5	26,564
Industrial Soln & Servcs	Valued at 25% premium to ABB's EV/EBIT (x)	30.5	19,185
Sub total			**45,749**
Others			
Healthcare	Valued at 3x sales	3.0	13,937
Other Investments	At book value	-	847
Total Enterprise Value			176,043
Recurring Investment of Net Cash	Assumed 50% ROIC and valued at bond yields	-	44,745
Fair Equity Valuation			**220,788**

Source: Edelweiss research

Key drivers of operating performance and, consequently stock performance are likely to be power in the infrastructure space, industrial solutions (including automation and drives) in the corporate capex space and IT services in technology services. Importantly, the business segments of power, industrial solutions and IT services are likely to grow faster than the overall revenue and earnings growth driving improvement in financial metrics.

We expect accelerated order accretion in the power space, wider and deeper product portfolio driving revenues from corporate capex, and ramp-up in IT services.

Dissecting SOTP valuation

- For valuing SIL's power, automation & drives, and industrial solution and services business, we have assumed 25% premium to BHEL's and ABB's EV/EBIT (x) given SIL's far superior return ratios.
- Healthcare and building technologies are valued at 3x sales given high ROCE in excess of 50% plus for these two segments.
- We have assumed that SIL will take the balance 50% stake in Flender and additional 23% stake in SITS in FY07E. The total investment has been valued at 2x equity investments.

- Since SIL's consolidated ROCE is likely to be at ~ 50%, we have assumed that net cash available with SIL will be deployed on recurring basis and generate 50% ROIC. The reinvested amount is valued at bond yields.

Based on the above assumptions for SOTP valuation, we have arrived at fair equity valuation of INR 221 bn. With SIL currently quoting at market cap of INR 207 bn, we expect limited upside from current valuations when current market cap is compared to our SOTP valuation.

Robust return ratios justify premium valuations

On a consolidated basis, SIL trades at P/E of 29x and 22x on FY07E and FY08E EPS of INR 44 and INR 57, respectively. Amongst the large cap engineering basket, SIL scores over its peers in terms of return ratios and working capital turnover ratio. As a result, SIL continues to command premium valuations over its Indian engineering peers, but trades at a discount to ABB.

Table 7: Peer valuation comparison (FY07E)

Companies*	Crompton	L&T	BHEL	Average of indian companies	ABB	Siemens	Relative advantage to Indian companies
P/E (x)	19.3	25.2	26.3	23.6	33.7	28.6	Yes
Price/BV(x)	5.9	6.3	6.1	6.1	9.5	11.9	Yes
EV/Sales (x)	0.9	1.6	2.9	1.8	2.5	2.8	Yes
EV/EBITDA (x)	11.3	16.2	16.1	14.5	22.6	21.1	Yes
ROAE (%)	34.9	26.7	25.6	29.1	32.1	48.4	No
ROACE (%)	30.6	20.7	34.1	28.5	42.4	50.5	No
Fixed assets t/o (x)	9.7	7.4	11.4	9.5	4.1	8.2	Yes
Working capital t/o (x)	9.0	3.9	2.6	5.2	7.0	10.5	No

Source: Edelweiss research

*Note: (1) *Crompton,L&T and BHEL are Mar ending, Siemens is Sep ending & ABB is Dec ending.*

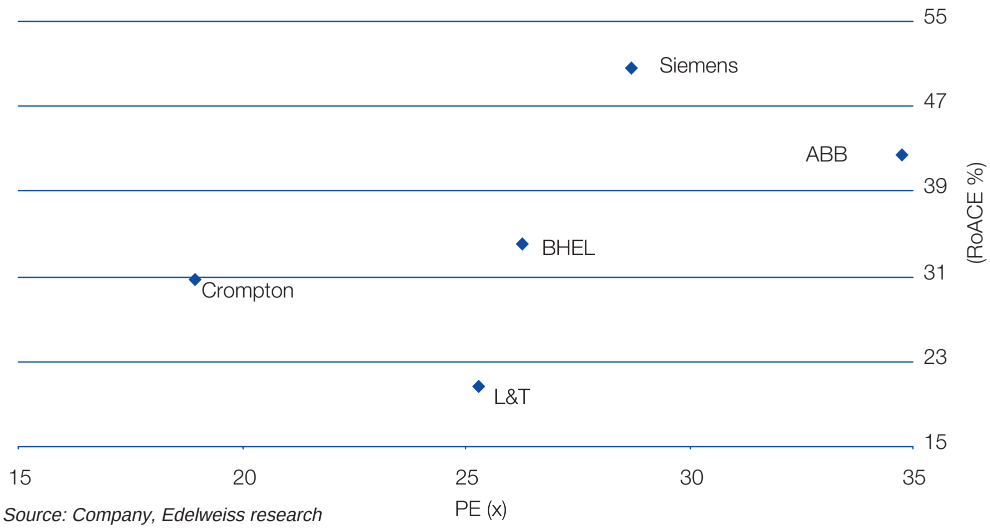
*(2) * All valuation parameters taken as average of FY07E and FY08E for Crompton, BHEL and L&T.*

Quality comes at a cost

While ABB trades at a P/E of 34x, the Indian engineering basket is trading at discount of 26% at an average P/E of 23x FY07E. Premium valuations of global engineering plays are justified as the return ratios (ROACE) are far more superior at ~ 60% plus as compared to that of Indian engineering companies (L&T, BHEL and Crompton Greaves). However, with Indian players diversifying geographically and expanding their horizon through organic/inorganic route, there is a strong case for return ratio disparities contracting over a period of time. We, therefore, initiate coverage on SIL with an **'ACCUMULATE'** recommendation, given that the Indian engineering plays of similar scale and size are available at a discount to SIL's and ABB's valuations.

SIL, up there with the best

Chart 8: P/E and RoACE — Peer comparison



Source: Company, Edelweiss research

Risks and Concerns

Temporary slowdown in the India story

Economic slowdown could hinder growth

Any slowdown in the economy is bound to impact the capital goods industry. By nature, the capital goods industry is the first to be impacted by economic slowdown and the last to benefit from an economic upturn. Since SIL is a direct play on India's growth story, any short-term slowdown or temporary recession could affect SIL's performance in the coming two years. Besides, since we have estimated the share of exports going up in the revenue mix, slowdown in regional markets could negatively impact our estimates.

Slowdown in the capex cycle, delayed project execution

Any downturn in the fast-paced capex growth in India is likely to impact the profitability and return ratios given that large investments have already been made by SIL to establish its India presence. Any delay in the rollout and execution plan is likely to lead to slower-than-expected growth.

Increased raw material prices could impact margins

High raw material prices could impact margins

All the companies in the capital goods space have faced margin pressure in the products division due to spike in metal prices, especially copper, aluminum and CRGO steel. Since ~ 30% of SIL's consolidated portfolio is likely to be contributed by product offerings (largely in the power space) in FY07 and FY08, SIL's operating margins in the products division could come under pressure.

Company background

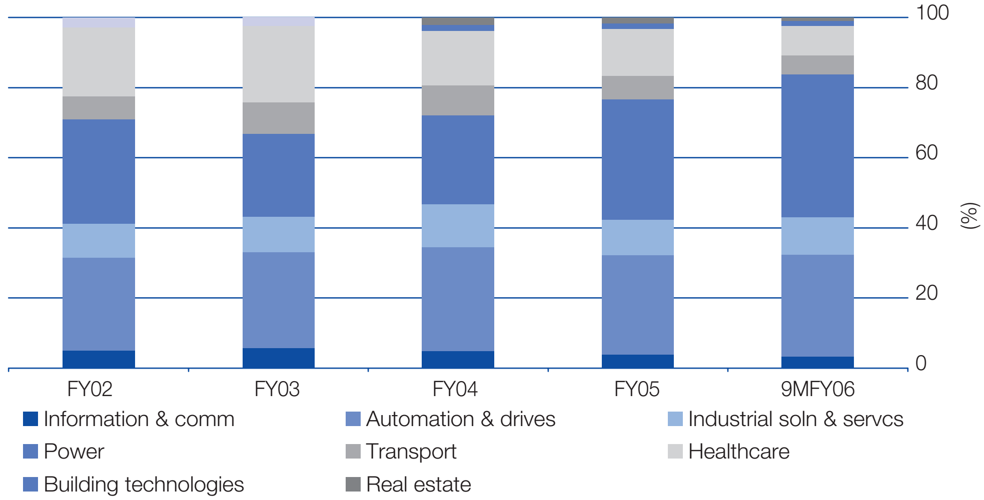
Siemens India Limited (SIL) is a 55% subsidiary of Siemens AG, Germany, which has presence in more than 190 countries, making it one of the most global business organizations. SIL, mirroring its parent company's portfolio in India, offers diverse products and services solutions in power generation, transmission and distribution, automation and drives, industrial solution and healthcare. It has nation-wide sales and service network, 17 manufacturing plants, and 500 strong network of channel partners. The Siemens Group employs over 14,500 people through its 12 companies.

Business description

SIL has transformed from an engineering major to a company with a diversified portfolio encompassing seven different business segments — energy, industrial solutions, healthcare, information technology, real estate, transportation, and communication.

Play across

Chart 9: Segment mix



Source: Company, Edelweiss research

For 9MFY06, ~ 80% of the revenue is contributed by power, automation & drives and industrial solution. These three segments also play an important role in the profitability, contributing ~ 80% for 9MFY06.

Table 8: SIL product portfolio

Power & Energy space	Transport
Switchgears	Railway signalling equipments
Electric motors & generators	Traction converter for diesel locomotive
Switchboards/Control boards	Audio frequency track circuits
AC/DC drive sys. - Variable speed	Interlocking relays
Electrical control cabinet	
Circuit breakers > 1,000 volts	
Single/stage/multistage turbine	
Rectifier cubicles	
Information Technology	**Healthcare**
Data acq.logging sys./Control	Electro medical equipments, X-ray equipments

Source: Company, Edelweiss research

Additionally, SIL also has five subsidiaries in India, viz., Siemens Information Systems Limited (SISL), Siemens Public Communication Networks Pvt. Ltd. (SPCNL), Siemens Industrial Turbo Machinery Services Pvt. Ltd. (SITMS), Siemens BPO Services Pvt. Ltd. (SBPO), and Flender Ltd.

Financial Statements (standalone)

Income statement (INR mn)

Year to September	FY04	FY05	FY06E	FY07E	FY08E
Income from operations	18,249	27,966	42,863	55,662	71,549
Direct costs	13,375	20,858	32,815	42,439	54,232
Employee costs	1,652	2,043	2,818	3,732	4,894
Other expenses	1,352	2,239	3,304	4,290	5,515
Total operating expenses	16,379	25,140	38,936	50,462	64,640
EBITDA	1,870	2,826	3,926	5,200	6,909
Depreciation and amortisation	228	291	401	501	552
EBIT	1,641	2,535	3,525	4,699	6,357
Interest expenses	1	0	1	1	1
Other income	658	1,096	1,127	1,482	1,675
Extraordinary items	(18)	4	-	-	-
Profit before tax	2,317	3,627	4,652	6,180	8,031
Provision for tax	785	1,084	1,392	1,849	2,402
Reported profit	1,532	2,544	3,261	4,332	5,629
Adjusted net profit	1,514	2,547	3,261	4,332	5,629
Shares outstanding (mn)	166	166	169	169	169
Dividend per share (INR)	1.8	2.9	3.1	3.5	4.0
Dividend payout (%)	19.5	18.9	16.0	13.6	12.0

Common size metrics as % of net revenues

Year to September	FY04	FY05	FY06E	FY07E	FY08E
Operating expenses	89.8	89.9	90.8	90.7	90.3
Depreciation	1.3	1.0	0.9	0.9	0.8
Interest expenditure	0.0	0.0	0.0	0.0	0.0
EBITDA margins	10.2	10.1	9.2	9.3	9.7
Net profit margins	8.3	9.1	7.6	7.8	7.9

Growth metrics (%)

Year to September	FY04	FY05	FY06E	FY07E	FY08E
Revenues	22.1	53.2	53.3	29.9	28.5
EBITDA	12.0	51.2	38.9	32.4	32.9
PBT	17.7	56.6	28.3	32.8	29.9
Net profit	8.6	68.3	28.0	32.8	29.9
EPS	8.6	68.3	25.8	32.8	29.9

Cash flow statement (INR mn)

Year to September	FY04	FY05	FY06E	FY07E	FY08E
Net profit	1,514	2,547	3,261	4,332	5,629
Add: Depreciation	228	291	401	501	552
Add: Deferred tax	10	18	23	31	41
Gross cashflow	1,752	2,857	3,685	4,864	6,221
Less: Dividends	337	548	588	664	759
Less: Changes in W. C.	(995)	(1,301)	326	1,074	1,710
Operating cash flow	2,411	3,610	2,771	3,126	3,752
Less: Change in investments	316	2,087	-	781	-
Less: Capex	(2)	71	3,132	1,000	1,500
Free cash flow	**2,096**	**1,452**	**(361)**	**1,345**	**2,252**

Balance sheet (INR mn)

As on 30th September	FY04	FY05	FY06E	FY07E	FY08E
Equity capital	331	331	337	337	337
Reserves & surplus	5,730	7,476	10,149	13,817	18,687
Shareholders funds	6,062	7,808	10,486	14,154	19,024
Unsecured loans	29	26	26	26	26
Borrowings	29	26	26	26	26
Sources of funds	**6,090**	**7,833**	**10,512**	**14,180**	**19,050**
Gross block	5,461	5,226	8,726	9,726	11,226
Depreciation	3,595	3,256	3,657	4,158	4,710
Net block	1,867	1,970	5,069	5,568	6,516
Capital work in progress	62	368	0	0	0
Total fixed assets	1,929	2,338	5,069	5,568	6,516
Investments	1,215	3,303	3,303	4,084	4,084
Inventories	1,698	3,284	5,537	7,190	9,242
Sundry debtors	4,173	7,320	10,569	13,725	17,642
Cash and equivalents	4,310	4,855	4,500	5,845	8,097
Loans and advances	1,658	1,811	0	0	0
Total current assets	11,839	17,270	20,605	26,760	34,982
Sundry creditors and others	7,363	12,759	16,124	19,859	24,119
Provisions	1,677	2,469	2,469	2,469	2,469
Total CL & provisions	9,040	15,228	18,592	22,328	26,587
Net current assets	2,799	2,042	2,013	4,432	8,394
Net deferred tax	148	150	127	96	55
Uses of funds	**6,090**	**7,833**	**10,512**	**14,180**	**19,050**
Book value per share (BV)	37	47	62	84	113

Ratios

Year to September	FY04	FY05	FY06E	FY07E	FY08E
ROAE (%)	27.6	36.7	35.6	35.2	33.9
ROACE (%)	29.8	36.4	38.4	38.1	38.3
Current ratio	1.3	1.1	1.1	1.2	1.3
Debtors (days)	83	96	90	90	90
Fixed assets t/o (x)	9.7	13.1	11.6	10.5	11.8
Average working capital t/o (x)	7.5	11.6	21.1	17.3	11.2

Valuation parameters

Year to September	FY04	FY05	FY06E	FY07E	FY08E
EPS (INR)	9.1	15.4	19.3	25.7	33.4
Y-o-Y growth (%)	*8.6*	*68.3*	*28.0*	*32.8*	*29.9*
CEPS (INR)	10.5	17.1	21.7	28.7	36.7
PE (x)	136.8	81.3	64.6	48.6	37.4
Price/BV(x)	34.2	26.5	20.1	14.9	11.1
EV/Sales (x)	11.1	7.3	4.7	3.6	2.8
EV/EBITDA (x)	108.5	71.8	51.7	39.0	29.4

Financial Statements (consolidated)

Income statement (INR mn)

Year to September	FY04	FY05	FY06E	FY07E	FY08E
Income from operations	22,794	36,781	55,470	71,630	91,494
Direct costs	14,968	24,105	37,480	48,347	61,811
Employee costs	3,150	4,834	6,348	8,203	10,279
Other expenses	1,778	3,124	4,287	5,408	6,731
Total operating expenses	19,897	32,063	48,115	61,959	78,821
EBITDA	2,897	4,718	7,356	9,671	12,673
Depreciation and amortisation	477	684	930	1,172	1,390
EBIT	2,421	4,034	6,425	8,499	11,283
Interest expenses	1	19	33	33	46
Share of profit in asso. companies	16	22	-	-	-
Other income	195	488	1,127	1,482	1,675
Profit before tax	2,630	4,524	7,520	9,948	12,912
Provision for tax	937	1,428	1,948	2,572	3,362
Profit before minority interest	1,694	3,097	5,572	7,377	9,550
Minority interest	-	9	71	9	11
Reported profit after minority int.	1,694	3,088	5,501	7,368	9,539
Adjusted net profit	1,694	3,088	5,501	7,368	9,539
Shares outstanding (mn)	166	166	169	169	169
Dividend per share (INR)	1.8	2.9	3.1	3.5	4.0
Dividend payout (%)	17.6	15.6	9.5	8.0	7.1

Common size metrics as % of net revenues

Year to September	FY04	FY05	FY06E	FY07E	FY08E
Operating expenses	87.3	87.2	86.7	86.5	86.1
Depreciation	2.1	1.9	1.7	1.6	1.5
Interest expenditure	0.0	0.1	0.1	0.0	0.1
EBITDA margins	12.7	12.8	13.3	13.5	13.9
Net profit margins	7.4	8.4	9.9	10.3	10.4

Growth metrics (%)

Year to September	FY04	FY05	FY06E	FY07E	FY08E
Revenues	27.2	61.4	50.8	29.1	27.7
EBITDA	22.5	62.9	55.9	31.5	31.0
PBT	17.6	72.0	66.2	32.3	29.8
Net profit	2.2	82.3	78.1	33.9	29.5
EPS	2.2	82.3	75.1	33.9	29.5

Balance sheet (INR mn)

As on 30th September	FY04	FY05	FY06E	FY07E	FY08E
Equity capital	331	331	337	337	337
Reserves & surplus	6,671	8,847	12,339	17,161	23,515
Minority interest	0	72	143	152	163
Shareholders funds	7,003	9,251	12,819	17,650	24,015
Secured loans	0	35	0	0	0
Unsecured loans	29	926	1,461	1,711	1,961
Borrowings	29	961	1,461	1,711	1,961
Sources of funds	**7,031**	**10,211**	**14,280**	**19,361**	**25,976**
Gross block	6,976	9,379	14,269	16,744	20,035
Depreciation	4,398	5,248	6,179	7,350	8,740
Net block	2,579	4,131	8,090	9,394	11,295
Capital work in progress	82	613	0	0	0
Total fixed assets	2,660	4,743	8,090	9,394	11,295
Investments	408	847	847	847	847
Inventories	1,698	3,700	5,952	7,606	9,658
Sundry debtors	4,259	10,700	13,678	17,662	22,560
Cash and equivalents	6,411	6,745	7,283	9,317	12,417
Loans and advances	2,094	2,896	1,085	1,866	1,866
Total current assets	14,462	24,041	27,997	36,451	46,500
Sundry creditors and others	8,809	16,429	20,034	24,513	29,572
Provisions	1,959	3,419	3,025	3,192	3,428
Total CL & provisions	10,768	19,848	23,059	27,704	32,999
Net current assets	3,695	4,193	4,938	8,746	13,501
Net deferred tax	269	428	405	373	333
Uses of funds	**7,031**	**10,211**	**14,280**	**19,361**	**25,976**
Book value per share (BV)	42	56	76	105	142

Cash flow statement (INR mn)

Year to September	FY04	FY05	FY06E	FY07E	FY08E
Net profit	1,694	3,100	5,572	7,377	9,550
Add: Depreciation	477	684	930	1,172	1,390
Add: Deferred tax	56	33	23	31	41
Gross cash flow	2,226	3,818	6,526	8,579	10,981
Less: Dividends	298	481	523	590	674
Less: Changes in W. C.	(2,182)	164	208	1,773	1,655
Operating cash flow	4,110	3,173	5,795	6,216	8,651
Less: Change in investments	378	439	-	-	-
Less: Capex	578	2,768	4,277	2,476	3,291
Free Cash Flow	**3,155**	**(34)**	**1,518**	**3,740**	**5,361**

Ratios

Year to September	FY04	FY05	FY06E	FY07E	FY08E
ROAE (%)	26.6	38.0	49.9	48.4	45.8
ROACE (%)	37.9	46.8	52.5	50.5	49.8
Current ratio	1.3	1.2	1.2	1.3	1.4
Debtors (days)	68	106	90	90	90
Fixed assets t/o (x)	8.7	9.9	8.6	8.2	8.8
Average working capital t/o (x)	7.0	9.3	12.1	10.5	8.2
Debt/Equity	0.0	0.1	0.1	0.1	0.1

Valuation parameters

Year to September	FY04	FY05	FY06E	FY07E	FY08E
EPS (INR)	10.2	18.6	32.6	43.7	56.6
Y-o-Y growth (%)	*2.2*	*82.3*	*78.1*	*33.9*	*29.5*
CEPS (INR)	13.1	22.8	38.2	50.7	64.8
PE (x)	122.3	67.1	38.3	28.6	22.1
Price/BV(x)	29.6	22.4	16.4	11.9	8.8
EV/Sales (x)	9.0	5.5	3.7	2.8	2.2
EV/EBITDA (x)	70.4	43.3	27.7	21.1	16.1

Edelweiss Securities
14th Floor, Express Towers,
Nariman Point, Mumbai – 400 021
Board: +91 22 2286 4400
Email*: research@edelcap.com*

Edelweiss
Ideas create, values protect

Naresh Kothari - 22864246	Head, Institutional Equities
Vikas Khemani - 22864206	Co-Head, Institutional Equities

INDIA RESEARCH			SECTOR
Shriram Iyer	-	2286 4256	Head – Research
Gautam Roy	-	2286 4305	Airlines, Textile
Ashutosh Goel	-	2286 4287	Automobiles, Auto Components
Vishal Goyal, CFA	-	2286 4370	Banking & Finance
Revathi Myneni	-	2286 4413	Cement
Sumeet Budhraja	-	2286 4430	FMCG
Harish Sharma	-	2286 4307	Infrastructure, Auto Components, Mid Caps
Priyanko Panja	-	2286 4300	Infrastructure, Engineering, Telecom
Hitesh Zaveri	-	2286 4424	Information Technology
Pritesh Vinay	-	2286 4429	Metals, Mining
Priyank Singhal	-	2286 4302	Media, Retail
Prakash Kapadia	-	2286 4432	Mid Caps
Niraj Mansingka	-	2286 4304	Oil & Gas, Petrochemicals
Nimish Mehta	-	2286 4295	Pharmaceuticals, Agrochemicals
Swati Khemani	-	2286 4266	Textile
Manika Premsingh	-	4019 4847	Economist
Sachin Arora	-	2286 4512	Alternative & Quantitative
Sunil Jain	-	2286 4308	Alternative & Quantitative
Yogesh Radke	-	2286 4328	Alternative & Quantitative

INSTITUTIONAL SALES		
Nischal Maheshwari	-	2286 4205
Rajesh Makharia	-	2286 4202
Shabnam Kapur	-	2286 4394
Amish Choksi	-	2286 4201
Deepak Rao	-	2286 4204
Balakumar V	-	(044) 4263 8283
Monil Bhala	-	2286 4363
Ashish Agrawal	-	2286 4301
Nikhil Garg	-	2286 4282
Neha Shahra	-	2286 4276
Priya Ramchandran	-	2286 4389
Anubhav Kanodia	-	2286 4361
Tushar Mahajan	-	2286 4439
Harsh Biyani	-	2286 4419
Nirmal Ajmera	-	2286 4258
Ankit Doshi	-	2286 4671
Ravi Pilani	-	4009 4533
Dipesh Shah	-	2286 4434

Email addresses: firstname.lastname@edelcap.com **e.g.** naresh.kothari@edelcap.com *unless otherwise specified*

RATING INTERPRETATION

Buy	Expected to appreciate more than 20% over a 12-month period	**Reduce**	Expected to depreciate up to 10% over a 12-month period
Accumulate	Expected to appreciate up to 20% over a 12-month period	**Sell**	Expected to depreciate more than 10% over a 12-month period
Trading Buy	Expected to appreciate more than 10% over a 45-day period	**Trading Sell**	Expected to depreciate more than 10% over a 45-day period