

Earnings surprise & growth justify premium valuation

1Q'07 beat expectations; PAT +69%; Order Backlog +59%YoY

ABB continues to surprise both in terms of growth & quality of growth, with 1QCY07 Sales at Rs13.1bn, +63%YoY, & PAT at Rs866mn, +69%YoY (MLE Rs763mn). More importantly, its 112bps EBITDA margin expansion was commendable given volatility in copper. Order intake (Rs20bn +43%) & backlog (Rs42.6bn +59%YoY) were at a historic high. Reiterate Buy with PO of Rs4550.

Order book & Order Inflow at historic highs

ABB reported its highest ever quarterly order intake of Rs20bn +43%YoY. Order Intake was led by power as well as automation business orders such as:

- Rs3.1bn order for power & automation from Grasim/Ultratech Cement.
- Turnkey solutions order: JSW Steel (Rs2.5bn) and KPTCL (Rs1.86bn).

Consequently, the order book reached Rs42.6bn (+59%YoY), also a historic high.

Power segment drives margin

The highlight of the quarter was 112bps YoY expansion in EBITDA margins led by 83bps YoY expansion in margin for power business (59% of operating profits) even as the automation segment witnessed a margin contraction (50bps). ABB changed its A/c policy for revenue recognition, from dispatch to milestone achievement basis from 1QCY07 for certain complex products, which has resulted in higher sales & PBT of Rs114mn & Rs22mn respectively.

Maintain Buy with PO of Rs4,550

Our PO of Rs4550 is based on 1-yr forward PER of 28x at PEG of 0.8x (Sensex PEG - 1.2x) & 15% discount to its current PER, to factor in slower growth vs past.

Estimates (Dec)

(Rs)	2005A	2006A	2007E	2008E	2009E
Net Income (Adjusted - mn)	2,188	3,403	4,898	6,422	8,288
EPS	51.60	80.26	115.51	151.45	195.47
EPS Change (YoY)	45.3%	55.6%	43.9%	31.1%	29.1%
Dividend / Share	8.00	10.00	14.99	19.99	19.99
Free Cash Flow / Share	46.01	115.97	131.63	189.14	262.09

Valuation (Dec)

	2005A	2006A	2007E	2008E	2009E
P/E	79.35x	51.01x	35.45x	27.03x	20.95x
Dividend Yield	0.195%	0.244%	0.366%	0.488%	0.488%
EV / EBITDA*	50.40x	33.64x	22.78x	17.59x	13.89x
Free Cash Flow Yield*	1.12%	2.83%	3.21%	4.62%	6.40%

* For full definitions of *iQmethod*SM measures, see page 8.

Equity | India | Engineering & Construction
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Merrill Lynch

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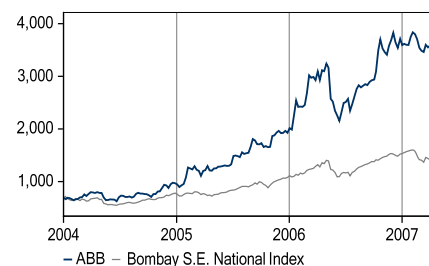
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Stock Data

Price	Rs4,094
Price Objective	Rs4,550
Date Established	19-Feb-2007
Investment Opinion	C-1-7
Volatility Risk	HIGH
52-Week Range	Rs1,920-Rs4,122
Mrkt Val / Shares Out (mn)	US\$4,244 / 42.4
Average Daily Volume	26,311
ML Symbol / Exchange	ABVFF / BSE
Bloomberg / Reuters	ABB IN / ABB.BO
ROE (2007E)	35.2%
Net Dbt to Eqty (Dec-2006A)	-81.6%
Est. 5-Yr EPS / DPS Growth	25.0% / 25.0%
Free Float	47.9%



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Refer to important disclosures on page 9 to 10. Analyst Certification on page 7. Price Objective Basis/Risk on page 7.

27 April 2007

*iQprofile*SM ABB India

Key Income Statement Data (Dec)	2005A	2006A	2007E	2008E	2009E
(Rs Millions)					
Sales	29,631	42,740	57,684	72,102	88,490
Gross Profit	5,724	7,821	10,781	13,567	16,831
Sell General & Admin Expense	(380)	(570)	(785)	(1,020)	(1,302)
Operating Profit	2,951	4,502	6,699	8,722	11,091
Net Interest & Other Income	445	730	1,020	1,399	1,970
Associates	NA	NA	NA	NA	NA
Pretax Income	3,396	5,232	7,719	10,121	13,062
Tax (expense) / Benefit	(1,208)	(1,829)	(2,821)	(3,699)	(4,774)
Net Income (Adjusted)	2,188	3,403	4,898	6,422	8,288
Average Fully Diluted Shares Outstanding	42	42	42	42	42

Key Cash Flow Statement Data

Net Income (Reported)	2,188	3,403	4,898	6,422	8,288
Depreciation & Amortization	231	265	340	395	457
Change in Working Capital	136	1,939	454	899	1,696
Deferred Taxation Charge	NA	NA	NA	NA	NA
Other Adjustments, Net	397	811	1,139	1,555	2,173
Cash Flow from Operations	2,952	6,417	6,831	9,271	12,614
Capital Expenditure	(1,001)	(1,500)	(1,250)	(1,251)	(1,501)
(Acquisition) / Disposal of Investments	NA	NA	NA	NA	NA
Other Cash Inflow / (Outflow)	(445)	(730)	(1,020)	(1,399)	(1,970)
Cash Flow from Investing	(1,446)	(2,230)	(2,270)	(2,650)	(3,471)
Shares Issue / (Repurchase)	0	0	0	0	0
Cost of Dividends Paid	(386)	(484)	(723)	(965)	(965)
Cash Flow from Financing	(386)	(484)	(723)	(965)	(965)
Free Cash Flow	1,951	4,917	5,581	8,020	11,113
Net Debt	(6,100)	(9,641)	(13,240)	(18,583)	(26,356)
Change in Net Debt	(1,120)	(3,703)	(3,838)	(5,656)	(8,178)

Key Balance Sheet Data

Property, Plant & Equipment	2,911	4,146	5,056	5,912	6,956
Other Non-Current Assets	579	579	579	728	930
Trade Receivables	9,774	11,984	14,698	18,371	22,547
Cash & Equivalents	6,201	9,742	13,341	18,684	26,457
Other Current Assets	4,452	5,894	7,486	8,931	10,575
Total Assets	23,917	32,345	41,159	52,626	67,465
Long-Term Debt	0	0	0	0	0
Other Non-Current Liabilities	208	127	8	NA	NA
Short-Term Debt	101	101	101	101	101
Other Current Liabilities	14,711	20,301	25,061	31,078	38,594
Total Liabilities	15,020	20,529	25,170	31,179	38,695
Total Equity	8,897	11,815	15,990	21,447	28,770
Total Equity & Liabilities	23,917	32,345	41,159	52,626	67,465

*iQmethod*SM - Bus Performance*

Return On Capital Employed	26.9%	32.1%	35.0%	34.4%	33.2%
Return On Equity	27.4%	32.9%	35.2%	34.3%	33.0%
Operating Margin	10.0%	10.5%	11.6%	12.1%	12.5%
EBITDA Margin	10.7%	11.2%	12.2%	12.6%	13.0%

*iQmethod*SM - Quality of Earnings*

Cash Realization Ratio	1.3x	1.9x	1.4x	1.4x	1.5x
Asset Replacement Ratio	4.3x	5.7x	3.7x	3.2x	3.3x
Tax Rate (Reported)	35.6%	35.0%	36.5%	36.5%	36.5%
Net Debt-to-Equity Ratio	-68.6%	-81.6%	-82.8%	-86.6%	-91.6%
Interest Cover	44.7x	NM	NM	NM	NM

Key Metrics

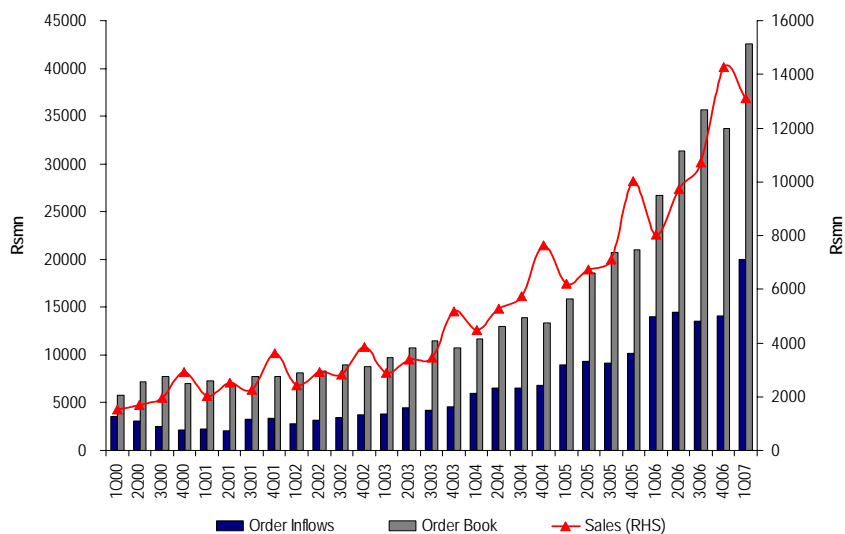
* For full definitions of *iQmethod*SM measures, see page 8.

Company Description

ABB India is the 52% subsidiary of ABB, the Swiss-Swedish electrical engineering company. In India, its operations mainly consist of T&D and industrial automation and control. The company had also commissioned a turbine facility, which it demerged in 1999 after ABB decided to divest it to Alstom.

Stock Data

Price to Book Value 10.9x

Chart 1: ABB – Quarterly Order Inflows, Order Book & Sales


Source: Company

Table 1: ABB - Key Ratios & Valuation

Year to Dec (Rs mn)	CY05A	CY06A	CY07E	CY08E	CY09E
Sales growth % y-o-y	31.1%	44.2%	35.0%	25.0%	22.7%
EBITDA growth % y-o-y	49.5%	49.8%	47.6%	29.5%	26.7%
PAT growth % y-o-y	45.3%	55.6%	43.9%	31.1%	29.1%
EPS (Rs)	51.6	80.3	115.5	151.5	195.5
P/E (x)	214.7	281.7	377.3	502.3	670.3
RoE (%)	26.7%	32.3%	35.1%	34.4%	33.3%
RoCE (%)	35.6%	42.4%	47.6%	46.5%	44.4%
CEPS (Rs)	57.05	74.02	107.50	142.14	184.70
Price/CEPS (x)	71.8	55.3	38.1	28.8	22.2
EV/EBITDA (x)	52.6	34.4	22.8	17.0	12.8
EV/Sales (x)	5.65	3.84	2.78	2.15	1.66
Gross Dividend (Rs)	8.0	10.0	15.0	20.0	20.0
Gross Yield (%)	0.2%	0.2%	0.4%	0.5%	0.5%
P/BV (x)	19.1	14.5	10.9	8.2	6.1
Book Value (Rs)	215	282	377	502	670

Source: Company, Merrill Lynch Research

Table 2: ABB - 1QCY07 Results Review

Rs mn	1QCY06	1QCY07	% YoY
Order Inflows (Qtr)	14019	20003	42.7%
Order Backlog (Qtr)	26743	42596	59.3%
Net sales	8,029	13,124	63.5%
Total Materials	5,868	9,751	66.2%
% to sales	73.1%	74.3%	
Staff Costs	555	698	25.7%
% to sales	6.9%	5.3%	
Others	912	1394	52.9%
% to sales	11.4%	10.6%	
Total Expenditure	7,335	11,843	61.5%
EBITDA	695	1282	84.6%
EBITDA Margin	8.7%	9.8%	
Interest	2	10	415.5%
Depreciation	62	86	38.9%
Other Income	180	152	-15.5%
P B T	810	1337	65.1%
Taxation	260	434	
Provision for Deferred Tax	17	14	
Fringe Benefit Tax	20	23	
P A T	513	866	68.9%
Segmental Revenue			
(Rs mn)	1QCY06	1QCY07	% YoY
Power Product	2,072	3,803	83.6%
Power systems	3,008	4,480	48.9%
Automation Products	1,912	2,880	50.6%
Process Automation	1,620	2,671	64.9%
Others	19	54	191.0%
Total	8,631	13,889	60.9%
Unallocated	133	98	
Total	8,764	13,987	59.6%
Less : Inter segment revenue	(555)	(711)	
Net sales	8,209	13,276	61.7%
Segment EBIT (Rs mn)	1QCY06	1QCY07	% YoY
Power Product	183	344	88.2%
Power systems	246	424	72.2%
Automation Products	217	326	50.1%
Process Automation	136	200	47.0%
Others	2	(1)	-162.0%
Total	784	1,292	64.8%
(Add)/less interest	2	10	
other unallocated expenses	(28)	(55)	
PBIT	810	1,337	65.1%
PBIT Margin	1QCY06	1QCY07	
Power Product	8.8%	9.0%	
Power systems	8.2%	9.5%	
Automation Products	11.3%	11.3%	
Process Automation	8.4%	7.5%	

Source: Company

Table 3: ABB - Profit & Loss Statement Summary

Year to Dec (Rs mn)	CY05A	CY06A	CY07E	CY08E	CY09E
Sales	29,631	42,740	57,684	72,102	88,490
% growth YoY	31.1%	44.2%	35.0%	25.0%	22.7%
EBITDA	3,182	4,767	7,038	9,117	11,548
EBITDA Margin (%)	10.7%	11.2%	12.2%	12.6%	13.0%
% growth YoY	49.5%	49.8%	47.6%	29.5%	26.7%
Interest	66	7	47	82	117
Depreciation	231	265	340	395	457
Other Income	511	737	1,067	1,481	2,088
P B T	3396	5232	7719	10121	13062
% growth YoY	41%	54%	48%	31%	29%
PAT	2188	3403	4898	6422	8288
% growth YoY	41.8%	55.6%	43.9%	31.1%	29.1%

Source: Company, Merrill Lynch Research

Table 4: ABB - Balance Sheet Summary

Year to Dec (Rs mn)	CY05A	CY06A	CY07E	CY08E	CY09E
Net fixed assets	2,911	4,146	5,056	5,912	6,956
Investments	579	579	579	579	579
Inventories	2,402	3,604	4,730	5,765	6,905
Receivables	9,774	11,984	14,698	18,371	22,547
Cash & bank balances	6,194	9,735	13,334	18,677	26,450
Other Current Assets	2,057	2,297	2,763	3,173	3,676
Total Current Assets	20,427	27,620	35,524	45,986	59,579
TOTAL ASSETS	23,917	32,345	41,159	52,477	67,114
Equity Capital	424	424	424	424	424
Reserves & surplus	8,681	11,519	15,574	20,874	27,995
Net Worth	9,105	11,943	15,997	21,298	28,419
Total Debt	101	101	101	101	101
Current Liabilities	14,711	20,301	25,061	31,078	38,594
TOTAL LIABILITIES	23,917	32,345	41,159	52,477	67,114

Source: Company, Merrill Lynch Research

Table 5: ABB - Cash Flow Statement

Year to Dec (Rs mn)	CY05A	CY06A	CY07E	CY08E	CY09E
Pre tax profit	3,396	5,232	7,719	10,121	13,062
Net other income	445	730	1,020	1,399	1,970
Depreciation	231	265	340	395	457
Less: Taxation	(1,256)	(1,748)	(2,702)	(3,542)	(4,572)
Profit from operations before WC changes	2,816	4,478	6,377	8,372	10,917
Working capital changes					
Change in inventory	(549)	(1,202)	(1,126)	(1,035)	(1,141)
Change in debtors	(2,243)	(2,210)	(2,714)	(3,674)	(4,176)
Change in other current assets	(187)	(240)	(466)	(411)	(503)
Change in payables	2,213	4,128	2,573	3,977	5,397
Change in other current liabilities	901	1,462	2,186	2,040	2,119
Net change in working capital	136	1,939	454	899	1,696
Net funds from operations	2,952	6,417	6,831	9,271	12,614
Issue of equity	0	0	0	0	0
Inc/(Dec) in debt	0	0	0	0	0
Dividend paid	(386)	(484)	(723)	(965)	(965)
Others	96	(162)	(239)	(315)	(406)
Net cash from financing	(290)	(646)	(963)	(1,279)	(1,371)
(Addition to fixed assets)	(1,001)	(1,500)	(1,250)	(1,251)	(1,501)
Net other income	(445)	(730)	(1,020)	(1,399)	(1,970)
(Inc)/Dec in investments	0	0	0	0	0
Net cash from investing	(1,446)	(2,230)	(2,270)	(2,650)	(3,471)
Total inc/Dec in cash/cash equivalents	1,216	3,541	3,598	5,342	7,771
Increase in cash	1,216	3,541	3,598	5,342	7,771
Cash balance in beginning	4,978	6,194	9,735	13,334	18,677
Cash balance at year end	6,194	9,735	13,333	18,675	26,448

Source: Company, Merrill Lynch Research

Price Objective Basis & Risk

Our PO of Rs4,550 is based on 1-yr forward PER of 28x at PEG of 0.8x (vs Sensex PEG of 1.2x) & 15% discount to its current multiples, to factor in slower growth vs past. Trading at 35x CY07E PER, ABB stock is not cheap, but we believe our target valuation is justified given its MNC parentage, technology and outsourcing opportunity leading to sustained earnings CAGR of 34% over CY06-09E and expanding RoE (35% by CY07E v/s 32% in CY06).

Risks: Competition & delay in power sector reforms/capex

Analyst Certification

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27 April 2007

iQmethodSM Measures Definitions

Business Performance	Numerator	Denominator
Return On Capital Employed	$\text{NOPAT} = (\text{EBIT} + \text{Interest Income}) * (1 - \text{Tax Rate}) + \text{Goodwill Amortization}$	$\text{Total Assets} - \text{Current Liabilities} + \text{ST Debt} + \text{Accumulated Goodwill Amortization}$
Return On Equity	Net Income	Shareholders' Equity
Operating Margin	Operating Profit	Sales
Earnings Growth	Expected 5-Year CAGR From Latest Actual	N/A
Free Cash Flow	Cash Flow From Operations – Total Capex	N/A
Quality of Earnings		
Cash Realization Ratio	Cash Flow From Operations	Net Income
Asset Replacement Ratio	Capex	Depreciation
Tax Rate	Tax Charge	Pre-Tax Income
Net Debt-To-Equity Ratio	Net Debt = Total Debt, Less Cash & Equivalents	Total Equity
Interest Cover	EBIT	Interest Expense
Valuation Toolkit		
Price / Earnings Ratio	Current Share Price	Diluted Earnings Per Share (Basis As Specified)
Price / Book Value	Current Share Price	Shareholders' Equity / Current Basic Shares
Dividend Yield	Annualised Declared Cash Dividend	Current Share Price
Free Cash Flow Yield	Cash Flow From Operations – Total Capex	Market Cap. = Current Share Price * Current Basic Shares
Enterprise Value / Sales	$\text{EV} = \text{Current Share Price} * \text{Current Shares} + \text{Minority Equity} + \text{Net Debt} + \text{Sales Other LT Liabilities}$	
EV / EBITDA	Enterprise Value	Basic EBIT + Depreciation + Amortization

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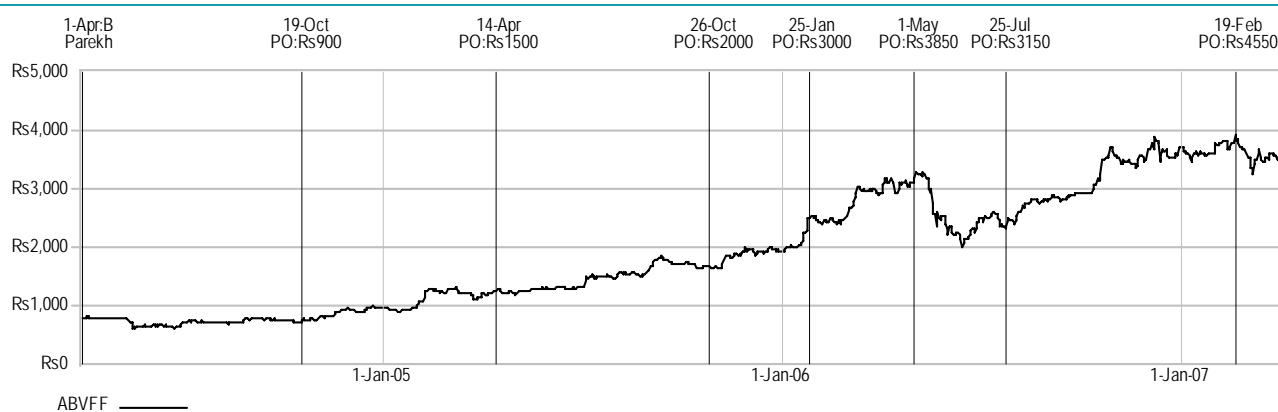
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27 April 2007

Important Disclosures

ABVFF Price Chart



B : Buy, N : Neutral, S : Sell, PO : Price objective, NA : No longer valid

The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark Grey shading indicates the security is restricted with the opinion suspended. Light Grey shading indicates the security is under review with the opinion withdrawn. Chart current as of March 31, 2007 or such later date as indicated.

Investment Rating Distribution: Engineering & Construction Group (as of 31 Mar 2007)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	14	63.64%	Buy	1	8.33%
Neutral	8	36.36%	Neutral	4	57.14%
Sell	0	0.00%	Sell	0	0.00%

Investment Rating Distribution: Global Group (as of 31 Mar 2007)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1562	45.16%	Buy	415	30.09%
Neutral	1615	46.69%	Neutral	446	30.65%
Sell	282	8.15%	Sell	49	19.76%

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