

Equities

8 November 2011 | 9 pages

ABB (India) (ABB.BO)

Sell: 14th Consecutive Disappointing Quarter; TP Cut to Rs461

- Another quarter of disappointment** — ABB's 3Q11 sales of Rs17.3bn were up 29% YoY which was 6% ahead of CIRA. Despite the sales beat, EBITDA margins at 2.9% v/s CIRA at 4.6% implied that PAT at Rs222m was 48% below CIRA at Rs427m.
- Inflows up 23% YoY - But is this reason to cheer?** — ABB's 3Q11 inflows at Rs24.9bn was up 23% YoY. We believe this is not a reason to cheer given: (1) dismal EBITDA margins reported over the last seven quarters (0.2% to 5%), (2) not all these quarters were impacted by rural electrification provisions, (3) severe competition on account of drying up of order pipeline and (4) a very high possibility that ABB has been cutting prices to gain market share.
- Focus on RE in CY07-08 impacted traditional business** — ABB's bought-out components as % of sales shot up in CY07-10 as the lack of indigenization implied other companies could make components more cost-competitively. When Chinese/ Koreans entered India in CY09, ABB was not well prepared to compete.
- Significant pile-up of receivables** — Since CY04 ABB has seen a pile-up of receivables. It is worried that the quantum of receivables >6 months has increased. We wonder if this is a reflection of poor SEB finances. However, by delaying supplier payments, ABB has delivered healthy operating cash flows over the years.
- Maintain Sell - Target price cut to Rs461** — Revise CY11E-13E EPS down by 18-26% to factor in: (1) 4-10% higher sales on higher-than-expected inflows and (2) 134-162 bps structurally lower margins. Our EPS estimates are 21-31% lower than consensus. Revise target price downwards to Rs461 (from Rs501 earlier) to factor in (1) EPS cuts and (2) roll forward of target P/E of 25x to Mar13E from Sep12E earlier. ABB continues to be most the over valued stock in our electrical equipment and engineering & construction universe. Barring a possible delisting we believe there is no fundamental support for the stock to trade at current valuations.

- Company Update
- Target Price Change
- Estimate Change

Sell		3
Price (08 Nov 11)		Rs682.30
Target price		Rs461.00
	from Rs501.00	
Expected share price return		-32.4%
Expected dividend yield		0.3%
Expected total return		-32.1%
Market Cap		Rs144,585M
		US\$2,954M

Price Performance (RIC: ABB.BO, BB: ABB IN)



Statistical Abstract

Year to	Net Profit	Diluted EPS	EPS growth	P/E	P/B	ROE	Yield
31 Dec	(RsM)	(Rs)	(%)	(x)	(x)	(%)	(%)
2009A	3,546	16.74	-33.1	40.8	6.0	15.7	0.3
2010A	632	2.98	-82.2	nm	6.0	2.6	0.3
2011E	2,243	10.59	254.8	64.4	5.5	8.9	0.3
2012E	3,795	17.91	69.1	38.1	4.9	13.7	0.4
2013E	4,243	20.02	11.8	34.1	4.3	13.5	0.4

Source: Powered by dataCentral

Venkatesh Balasubramaniam

 +91-22-6631-9864
 venkatesh.balasubramaniam@citi.com

 Deepal Delivala
 deepal.delivala@citi.com

 Atul Tiwari, CFA
 atul.tiwari@citi.com

 Rishi V Iyer
 rishi.iyer@citi.com

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Fiscal year end 31-Dec	2009	2010	2011E	2012E	2013E
Valuation Ratios					
P/E adjusted (x)	40.8	nm	64.4	38.1	34.1
EV/EBITDA adjusted (x)	26.4	165.8	38.3	23.6	21.1
P/BV (x)	6.0	6.0	5.5	4.9	4.3
Dividend yield (%)	0.3	0.3	0.3	0.4	0.4
Per Share Data (Rs)					
EPS adjusted	16.74	2.98	10.59	17.91	20.02
EPS reported	16.74	2.98	10.59	17.91	20.02
BVPS	113.72	114.38	123.19	139.11	156.98
DPS	2.00	2.20	2.20	2.40	2.60
Profit & Loss (RsM)					
Net sales	62,372	62,871	73,969	85,095	92,455
Operating expenses	-57,567	-62,550	-71,268	-80,204	-87,048
EBIT	4,805	321	2,701	4,891	5,407
Net interest expense	-256	-174	-249	-249	-249
Non-operating/exceptionals	726	855	913	1,050	1,207
Pre-tax profit	5,274	1,002	3,365	5,692	6,366
Tax	-1,728	-370	-1,122	-1,898	-2,122
Extraord./Min.Int./Pref.div.	0	0	0	0	0
Reported net income	3,546	632	2,243	3,795	4,243
Adjusted earnings	3,546	632	2,243	3,795	4,243
Adjusted EBITDA	5,290	838	3,635	5,911	6,546
Growth Rates (%)					
Sales	-8.8	0.8	17.7	15.0	8.6
EBIT adjusted	-35.7	-93.3	741.5	81.1	10.5
EBITDA adjusted	-32.5	-84.2	333.9	62.6	10.7
EPS adjusted	-33.1	-82.2	254.8	69.1	11.8
Cash Flow (RsM)					
Operating cash flow	3,363	2,120	1,168	2,374	3,980
Depreciation/amortization	485	517	933	1,020	1,139
Net working capital	-631	1,017	-2,009	-2,441	-1,403
Investing cash flow	-1,107	-999	-2,185	-1,076	-1,258
Capital expenditure	-1,549	-1,000	-2,185	-1,076	-1,258
Acquisitions/disposals	442	1	0	0	0
Financing cash flow	-496	-493	156	-422	-457
Borrowings	0	0	530	0	0
Dividends paid	-494	-494	-545	-595	-645
Change in cash	1,760	629	-861	875	2,265
Balance Sheet (RsM)					
Total assets	55,417	57,714	63,121	70,450	77,509
Cash & cash equivalent	5,242	5,871	5,010	5,885	8,150
Accounts receivable	28,577	29,260	32,425	36,836	40,021
Net fixed assets	7,755	8,238	9,489	9,545	9,664
Total liabilities	31,320	33,477	37,015	40,972	44,245
Accounts payable	14,784	16,402	17,885	20,283	22,037
Total Debt	0	0	530	530	530
Shareholders' funds	24,097	24,237	26,106	29,478	33,264
Profitability/Solvency Ratios (%)					
EBITDA margin adjusted	8.5	1.3	4.9	6.9	7.1
ROE adjusted	15.7	2.6	8.9	13.7	13.5
ROIC adjusted	17.2	-0.3	8.0	13.2	13.3
Net debt to equity	-21.8	-24.2	-17.2	-18.2	-22.9
Total debt to capital	0.0	0.0	2.0	1.8	1.6

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Figure 1. ABB 3QCY11 Results Review

Year End Dec31 (Rsmn)	Q110	Q111	YoY	Q210	Q211	YoY	Q310	Q311	YoY	Q311E
Net Sales	14,559	17,813	22%	14,466	16,930	17%	13,340	17,263	29%	16,214
EBITDA	29	899	3015%	500	660	32%	195	494	153%	739
EBITDA margin%	0.2%	5.0%		3.5%	3.9%		1.5%	2.9%		4.6%
Depreciation	(120)	(144)		(122)	(264)		(126)	(263)		(268)
EBIT	(92)	755	nm	378	396	5%	69	231	234%	471
EBIT margin%	-0.6%	4.2%		2.6%	2.3%		0.5%	1.3%		2.9%
Interest	(38)	(40)		(43)	(67)		(45)	(71)		(67)
Other Income	212	163		220	260		184	210		224
PBT	83	877	952%	555	589	6%	208	371	78%	628
Tax	(17)	(282)		(172)	(202)		(93)	(149)		(201)
Tax Rate%	20.4%	32.1%		31.0%	34.3%		44.7%	40.2%		32.0%
PAT	66	595	797%	383	387	1%	115	222	93%	427
PAT margin%	0%	3%		3%	2%		1%	1%		3%

Source: Company and Citi Investment Research and Analysis estimates

Figure 2. ABB EPS Revision Table

End Dec31 (Rsmn)	CY11E	CY12E	CY13E
Inflows			
Old	73,902	84,987	97,735
New	84,793	93,272	102,600
% Chg	14.7%	9.7%	5.0%
Net Sales			
Old	71,260	78,303	84,319
New	73,969	85,095	92,455
% Chg	3.8%	8.7%	9.6%
EBITDA Margin %			
Old	6.3%	8.5%	8.7%
New	4.9%	6.9%	7.1%
% Chg	-134	-150	-162
PAT			
Old	3050	4646	5154
New	2243	3795	4243
% Chg	-26.4%	-18.3%	-17.7%
EPS			
Old	14.4	21.9	24.3
New	10.6	17.9	20.0
% Chg	-26.4%	-18.3%	-17.7%

Source: Citi Investment Research and Analysis estimates

Figure 3. ABB EPS CIRA v/s Consensus

End Dec31 (Rsmn)	CY11E	CY12E	CY13E
CIRA	10.6	17.9	20.0
Consensus	14.9	22.7	28.9
Difference	-29.1%	-21.0%	-30.8%

Source: Bloomberg and Citi Investment Research and Analysis estimates

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 more than 100 countries and employs about 104,000 people. ABB India employs more than 4,000 people, has 10 manufacturing units, is a global engineering and operations centre and group corporate R&D facility. It has a countrywide marketing and service presence spanning 27 marketing offices, a network of more than 800 channel partners and eight service centres. ABB had two divisions: power technologies and automation technologies. But from January 1, 2006, it was restructured into five divisions for better management and control, and ABB India adopted the same five-division structure.

Investment strategy

We rate ABB Sell, with a target price of Rs461. The oft-repeated argument in favor of ABB is that India's power transmission and distribution (T&D) capex is a multi-year theme and ABB is the best play in this context given its technological superiority and quality management. We agree that India's power T&D capex is a multi-year theme, but competition and oversupply have derailed the story. Quality management and technological superiority can only help so much in the face of overcapacity/competition. Industry dynamics and the business cycle generally tend to be more powerful than management ability. This has been obvious in the telecoms and FMCG sectors. So why should it be any different in power T&D?

Valuation

Our Rs461 target price for ABB is based on 25x P/E for Mar13E, a ~30% discount to historical average trading bands given structurally lower margins and RoE. Investors tend to focus on P/E while valuing Indian electric equipment stocks. Our valuation methodology is similar to those used for peers like BHEL and Crompton.

Risks

Key upside risks to our target price are: 1) better-than-expected order wins; 2) better-than-expected order execution; and 3) better-than-expected margins.

Appendix A-1

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Analyst: Venkatesh Balasubramaniam

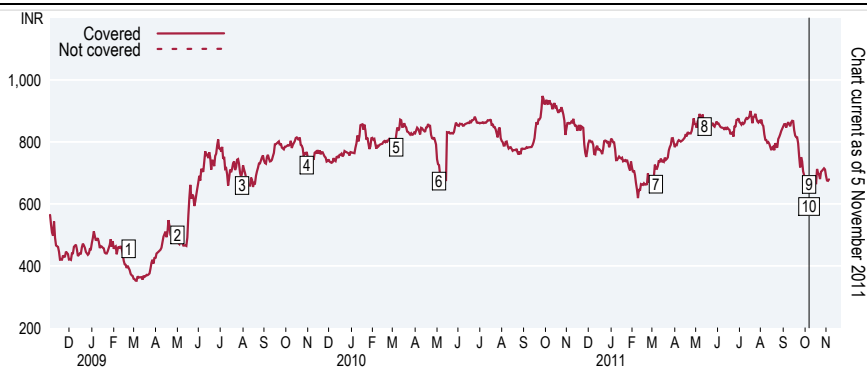


Chart current as of 5 November 2011

	Date	Rating	Target Price	Closing Price
1	22-Feb-09	3L	*332.00	400.35
2	1-May-09	3L	*380.00	487.35
3	31-Jul-09	3L	*503.00	699.00
4	30-Oct-09	3L	*539.00	767.85

	Date	Rating	Target Price	Closing Price
5	5-Mar-10	3L	*694.00	823.10
6	5-May-10	3L	*597.00	725.20
7	7-Mar-11	3L	*517.00	713.95
8	13-May-11	3L	*501.00	863.20

	Date	Rating	Target Price	Closing Price
9	7-Oct-11	Stock rating system changed		
10	7-Oct-11	*3	501.00	665.25

* Indicates change

Rating/target price changes above reflect Eastern Standard Time

ABB (India) (ABB.BO) Ratings and Target Price History Best Ideas Research Relative Call (3 Month)

Analyst: Venkatesh Balasubramaniam

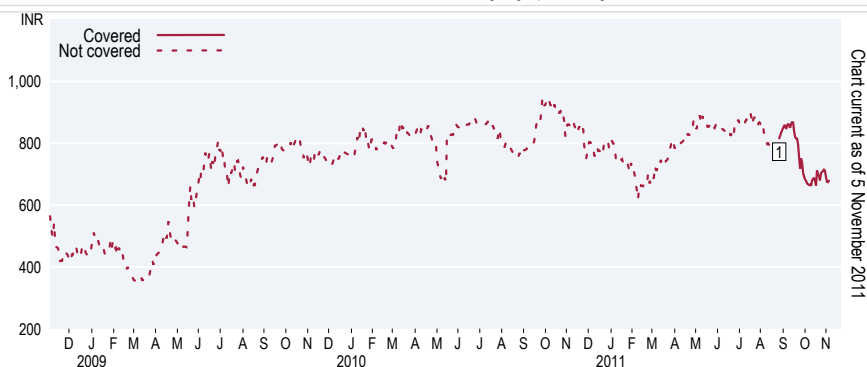


Chart current as of 5 November 2011

	Date	Rating	Target Price	Closing Price
1	26-Aug-11	*ADD LP	-	816.10

* Indicates change

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12 Month Rating			Relative Rating		
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59%	34%	7%	10%	79%	10%
45%	42%	37%	50%	43%	46%

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