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Rating	BUY
Price	Rs357
Target Price	Rs393
Implied Upside	10.1%
Sensex	17,193

(Prices as on November 11, 2011)
Trading data

Market Cap. (Rs bn)	70.6
Shares o/s (m)	198.0
3M Avg. Daily value (Rs m)	120.1

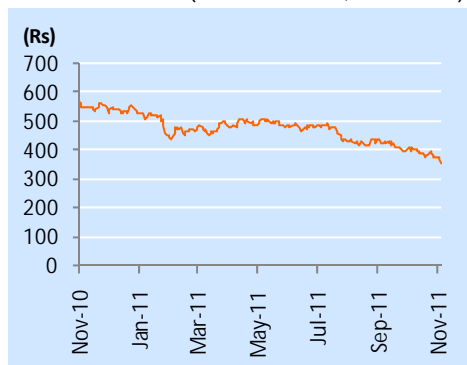
Major shareholders

Promoters	51.00%
Foreign	11.19%
Domestic Inst.	21.87%
Public & Other	15.94%

Stock Performance

(%)	1M	6M	12M
Absolute	(10.8)	(28.7)	(36.8)
Relative	(14.6)	(21.6)	(19.1)

Price Performance (RIC: CUMM.BO, BB: KKC IN)



Source: Bloomberg

■ **Results disappoints:** Sales for the quarter was flat YoY at Rs10.9bn. Domestic sales were down 5% YoY and flat QoQ. Strong growth in export (up 14% YoY) cushioned sales. The Power gen business was down 20% YoY, Industrial business was down 6% YoY and Auto business was up 50% YoY. The company highlighted that consistent rise in interest rates has dampened demand, especially in power generation segment. EBITDA margin was down 380bps YoY and 170bps QoQ to 16.1% (lowest margin in the last ten quarters). Increased commodity prices (mainly pig iron), unfavourable currency and adverse sales mix (in favour of smaller engines) led to pressure on margins. Adj. PAT was down 23% YoY to Rs1.2bn.

■ **Guidance revised downwards:** The company had guided for sales growth of 10-15% which has been downgraded to 5-10%. It has guided further 100bps reduction in PBT margin (from Q2FY12 levels of 16.7%) as it expects adverse sales mix in favour of low HP engines to continue for the rest of the year. It highlighted that if volumes come back and inflation continues at current levels, then it could see margins improve next year.

■ **Outlook and valuation:** The stock is currently trading at 15.4x FY13E earnings. We have downgraded our estimate for FY12 and FY13 by 18% and 15%, respectively. Though there might be some near-term pain, we believe the company is on track to double its turn over the next five years. With investment in capacity and technology leadership, the company will be able to capitalize once the market bounces back. Strong balance sheet and cash flow will continue to support valuations. We maintain our '**BUY**' rating on the stock.

Key financials (Y/e March)	2010	2011	2012E	2013E
Revenues (Rs m)	28,990	40,568	43,118	48,122
Growth (%)	(19.4)	39.9	6.3	11.6
EBITDA (Rs m)	5,817	7,748	7,028	8,373
PAT (Rs m)	4,559	5,992	5,146	6,402
EPS (Rs)	16.5	21.6	18.6	23.1
Growth (%)	(1.5)	31.4	(14.2)	24.4
Net DPS (Rs)	8.6	10.7	7.4	8.1

Source: Company Data; PL Research

Profitability & Valuation	2010	2011	2012E	2013E
EBITDA margin (%)	20.1	19.1	16.3	17.4
RoE (%)	29.9	35.6	26.5	28.1
RoCE (%)	29.8	35.5	26.1	27.7
EV / sales (x)	3.4	2.4	2.3	2.0
EV / EBITDA (x)	16.9	12.6	14.1	11.7
PE (x)	21.7	16.5	19.2	15.4
P / BV (x)	6.3	5.5	4.7	4.0
Net dividend yield (%)	2.4	3.0	2.1	2.3

Source: Company Data; PL Research

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Exhibit 1: Q2FY12 Result Overview (Rs m)

Y/e March	Q2FY12	Q2FY11	YoY gr. (%)	Q1FY12	H1FY12	H1FY11	YoY gr. (%)
Net Sales	10,903	10,914	(0.1)	10,453	21,356	20,194	5.8
Expenditure							
Raw Material	6,332	6,928	(8.6)	6,061	12,393	12,655	(2.1)
<i>% of Net Sales</i>	<i>58.1</i>	<i>63.5</i>		<i>58.0</i>	<i>58.0</i>	<i>62.7</i>	<i>(7.4)</i>
Personnel Cost	750	672	11.6	698	1,448	1,202	20.5
<i>% of Net Sales</i>	<i>6.9</i>	<i>6.2</i>		<i>6.7</i>	<i>6.8</i>	<i>6.0</i>	<i>13.9</i>
Others	2,062	1,141	80.7	1,838	3,900	2,189	78.1
<i>% of Net Sales</i>	<i>18.9</i>	<i>10.5</i>		<i>17.6</i>	<i>18.3</i>	<i>10.8</i>	<i>68.4</i>
Total Expenditure	9,144	8,742	4.6	8,597	17,741	16,046	10.6
EBITDA	1,759	2,172	(19.0)	1,856	3,616	4,148	(12.8)
<i>Margin (%)</i>	<i>16.1</i>	<i>19.9</i>	<i>(3.8)</i>	<i>17.8</i>	<i>16.9</i>	<i>20.5</i>	<i>(17.6)</i>
Other income	163	205	(20.3)	159	322	302	6.7
Depreciation	98	93	5.9	94	192	186	3.2
EBIT	1,824	2,285	(20.2)	1,921	3,746	4,263	(12.1)
Interest	5	4	17.1	4	8	8	1.2
PBT	1,819	2,281	(20.2)	1,918	3,737	4,255	(12.2)
Total Taxes	534	602	(11.3)	661	1,194	1,173	1.8
<i>ETR (%)</i>	<i>29.3</i>	<i>26.4</i>		<i>34.4</i>	<i>32.0</i>	<i>27.6</i>	<i>15.9</i>
PAT	1,286	1,679	(23.4)	1,257	2,543	3,082	(17.5)
Exceptional Item		-		514.7	515	-	
Reported PAT	1,286	1,679	(23.4)	1,772	3,058	3,082	(0.8)

Source: Company Data, PL Research

Exhibit 2: Operating Metrics (Rs m)

Y/e March	Q2FY12	Q2FY11	YoY gr. (%)	Q1FY12	H1FY12	H1FY11	YoY gr. (%)
Revenues							
Engine Business	9,996	9,914	0.8	9,478	19,475	18,339	6.2
Others	702	764	(8.1)	741	1,443	1,440	0.2
Total	10,698	10,678	0.2	10,219	20,917	19,778	5.8
EBIT							
Engine Business	1,562	1,914	(18.4)	1,503	3,065	3,483	(12.0)
Others	99	166	(40.5)	260	359	479	(25.1)
Total	1,661	2,080	(20.1)	1,763	3,424	3,961	(13.6)
EBIT Margins (%)							
Engine Business	15.6	19.3		15.9	15.7	19.0	
Others	14.1	21.7		35.1	24.9	33.2	

Source: Company Data, PL Research

**Exhibit 3: Balance Sheet (Rs m)**

Y/e March	H1FY12	H1FY11	FY11	FY12E
Shareholder's Funds				
Capital	396	554	396	554
Reserves & Surplus	18,295	20,566	17,667	20,525
Loan Funds				
Secured loans	50	134	183	183
Unsecured Loans	0	-	0	500
Total	18,741	21,254	18,245	21,762
Fixed Assets	3,502	4,984	4,411	7,022
Investments	7,901	5,644	7,255	7,255
Deferred tax assets	248	209	187	236
Current assets, Loans and advances				
Inventories	5,006	5,841	5,190	5,933
Sundry Debtors	6,866	7,423	7,182	7,679
Cash and bank balances	834	1,931	1,037	805
Other current assets	108	157	3,297	3,449
Loans & Advances	2,722	3,613	99	123
Less: Current Liabilities				
Liabilities	7,033	6,881	7,109	7,910
Provisions	1,413	1,666	3,303	3,018
Net Current Assets	7,091	10,418	6,393	7,060
Total	18,741	21,255	18,245	21,572

Source: Company Data, PL Research



Key takeaways of Conference Call

- According to the company, the main cause of slowdown is end-market related and not channel related.
- The intensity of competition is increasing, but company feels that it will be able to maintain prices.
- Slowdown in Power gen business is due to slowdown in key market drives. The growth in commercial reality has come down to 3.4% against 10-12%. In Infrastructure, the growth has come down to 6% from 15%. In Auto, the growth has come down to 8% from 15%. The most robust segments are Retail and the IT enabled or data centres, banking and hospitality growing at about 5-10%. Telecom is also quite slow, moving with a de-growth of ~15%.
- It highlighted that in Power gen, the market is more skewed towards standby. ~60% to 65% of the market today is on a standby.
- In terms of size, sales mix is less than 160 kVA, ~35% of sales in the quarter (generally lower at ~20% to 25%). 160 to 380 kVA is approximately 20%, 400 to 625 kVA is ~15% and 750kVA and above has actually declined to about 30% (generally 45%).



Income Statement (Rs m)

Y/e March	2010	2011	2012E	2013E
Net Revenue	28,990	40,568	43,118	48,122
Raw Material Expenses	18,358	25,808	27,811	31,038
Gross Profit	10,633	14,760	15,307	17,083
Employee Cost	1,953	2,546	2,975	3,320
Other Expenses	2,864	4,466	5,304	5,390
EBITDA	5,817	7,748	7,028	8,373
Depr. & Amortization	361	366	389	478
Net Interest	21	19	68	18
Other Income	674	661	645	863
Profit before Tax	6,109	8,023	7,216	8,740
Total Tax	1,670	2,114	2,165	2,447
Profit after Tax	4,439	5,910	5,051	6,293
Ex-Od items / Min. Int.	121	82	94	109
Adj. PAT	4,559	5,992	5,146	6,402
Avg. Shares O/S (m)	276.9	276.9	277.2	277.2
EPS (Rs.)	16.5	21.6	18.6	23.1

Cash Flow Abstract (Rs m)

Y/e March	2010	2011	2012E	2013E
C/F from Operations	5,759	4,179	4,608	6,018
C/F from Investing	(3,219)	(788)	(2,906)	(2,391)
C/F from Financing	(2,157)	(2,913)	(1,935)	(3,095)
Inc. / Dec. in Cash	383	478	(232)	531
Opening Cash	500	559	1,037	805
Closing Cash	559	1,037	805	1,336
FCFF	7,243	3,936	1,635	4,608
FCFE	6,982	4,118	2,135	4,108

Key Financial Metrics

Y/e March	2010	2011	2012E	2013E
Growth				
Revenue (%)	(19.4)	39.9	6.3	11.6
EBITDA (%)	(3.0)	33.2	(9.3)	19.1
PAT (%)	(1.5)	31.4	(14.1)	24.4
EPS (%)	(1.5)	31.4	(14.2)	24.4
Profitability				
EBITDA Margin (%)	20.1	19.1	16.3	17.4
PAT Margin (%)	15.7	14.8	11.9	13.3
RoCE (%)	29.8	35.5	26.1	27.7
RoE (%)	29.9	35.6	26.5	28.1
Balance Sheet				
Net Debt : Equity	—	—	—	—
Net Wrkng Cap. (days)	44	37	39	39
Valuation				
PER (x)	21.7	16.5	19.2	15.4
P / B (x)	6.3	5.5	4.7	4.0
EV / EBITDA (x)	16.9	12.6	14.1	11.7
EV / Sales (x)	3.4	2.4	2.3	2.0
Earnings Quality				
Eff. Tax Rate	27.3	26.3	30.0	28.0
Other Inc / PBT	11.0	8.2	8.9	9.9
Eff. Depr. Rate (%)	4.6	4.0	3.2	3.5
FCFE / PAT	153.1	68.7	41.5	64.2

Source: Company Data, PL Research.

Balance Sheet Abstract (Rs m)

Y/e March	2010	2011	2012E	2013E
Shareholder's Funds	15,610	18,063	20,842	24,667
Total Debt	—	183	683	183
Other Liabilities	—	—	—	—
Total Liabilities	15,610	18,245	21,525	24,850
Net Fixed Assets	3,337	4,411	7,022	8,044
Goodwill	—	—	—	—
Investments	7,329	7,255	7,255	8,255
Net Current Assets	4,860	6,393	7,060	8,363
<i>Cash & Equivalents</i>	<i>559</i>	<i>1,037</i>	<i>805</i>	<i>1,336</i>
<i>Other Current Assets</i>	<i>12,113</i>	<i>15,767</i>	<i>17,184</i>	<i>19,107</i>
<i>Current Liabilities</i>	<i>7,812</i>	<i>10,411</i>	<i>10,928</i>	<i>12,081</i>
Other Assets	84	187	189	189
Total Assets	15,610	18,245	21,525	24,850

Quarterly Financials (Rs m)

Y/e March	Q3FY11	Q4FY11	Q1FY12	Q2FY12
Net Revenue	9,925	10,493	10,453	10,903
EBITDA	1,794	1,849	1,856	1,759
<i>% of revenue</i>	<i>18.1</i>	<i>17.6</i>	<i>17.8</i>	<i>16.1</i>
Depr. & Amortization	91	89	94	98
Net Interest	3	8	4	5
Other Income	103	213	159	163
Profit before Tax	1,802	1,964	1,918	1,819
Total Tax	416	525	661	534
Profit after Tax	1,386	1,440	1,257	1,286
Adj. PAT	1,386	1,440	1,257	1,286

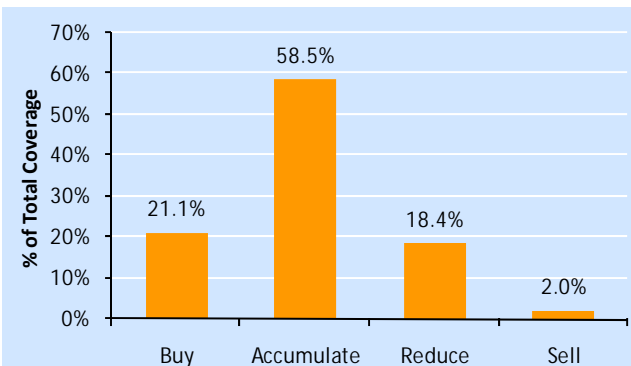
Source: Company Data, PL Research.

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Rating Distribution of Research Coverage



PL's Recommendation Nomenclature

BUY	: Over 15% Outperformance to Sensex over 12-months	Accumulate	: Outperformance to Sensex over 12-months
Reduce	: Underperformance to Sensex over 12-months	Sell	: Over 15% underperformance to Sensex over 12-months
Trading Buy	: Over 10% absolute upside in 1-month	Trading Sell	: Over 10% absolute decline in 1-month
Not Rated (NR)	: No specific call on the stock	Under Review (UR)	: Rating likely to change shortly

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