

October 21, 2011

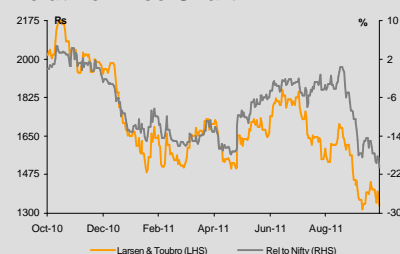
Reco	Previous Reco
Accumulate	Accumulate
CMP	Target Price
Rs 1,336	Rs 1,603
EPS change FY12E/13E (%)	NA
Target Price change (%)	NA
Nifty	5,050
Sensex	16,786

Price Performance

(%)	1M	3M	6M	12M
Absolute	(14)	(25)	(22)	(34)
Rel. to Nifty	(13)	(18)	(9)	(21)

Source: Bloomberg

Relative Price Chart



Source: Bloomberg

Stock Details

Sector	Engineering & Capital Goods
Bloomberg	LT@IN
Equity Capital (Rs mn)	1222
Face Value(Rs)	2
No of shares o/s (mn)	611
52 Week H/L	2,212/1,303
Market Cap (Rs bn/USD mn)	817/16,318
Daily Avg Vol (No of shares)	2066606
Daily Avg Turnover (US\$ mn)	64.0

Shareholding Pattern (%)

	Sep-11	Jun-11	Mar-11
Promoters	0.0	0.0	0.0
FII/NRI	21.1	21.3	19.6
Institutions	36.2	36.6	37.5
Private Corp	6.7	6.3	6.9
Public	36.0	35.7	36.1

Source: Capitaline

Pritesh Chheda, CFA

pritesh.chheda@emkayglobal.com
+91 22 6612 1273

Prerna Jhavar

prerna.jhavar@emkayglobal.com
+91 22 6612 1337

- **Mixed Bag performance in Q2FY12 – Ebidta margins decline 30 bps yoy but APAT grew 28% to Rs8.0 bn – led by higher other income**
- **Q2FY12 order inflows of Rs161 bn (down 21% yoy) & H1FY12 down 11% to Rs330 bn – Asking rate for H2FY12 increases Order book of Rs1,422 bn – 3.2X sales**
- **Lowered guidance – order inflows growth of 5% and Ebidta margins decline 75-125 bps – Same remains factored in our estimates**
- **L&T at attractive valuations of 14.9X FY13E earnings, but lacks re-rating catalysts- Maintain ACCUMULATE with target price of Rs1603/Shares**

Mixed Bag – EBITDA margins decline 30 bps yoy but APAT up 28% yoy

L&T reported mixed results in Q2FY12 (1) Sustained growth momentum on back of robust order backlog – revenues up 21% yoy to Rs112.5 bn – marginally above estimates (2) Operating margins fell by 30 bps yoy to 10.4% (Vs estimate of 10.6%) - owing to change in revenue mix and rise in staff costs (3) Operating profit growth at 17% yoy to Rs11.5 bn – in line with estimates (4) However, net profit growth at 28% yoy to Rs8.0 bn was above estimates – attributed to higher other income (Rs3.6 bn Vs estimate of Rs2.9 bn).

Segment level – E&C and E&E deliver while M&IP disappoints

- **Engineering & Construction (E&C)** – Led by strong opening order backlog, E&C segment posted yet another quarter of strong performance. Revenues grew by 21% yoy to Rs97.2 bn while EBIT margins declined 60 bps yoy to 10.6% - decline in margins attributed to cost inflation and change in revenue mix.
- **Electrical & Electronics (E&E)** – After 4 quarters of muted performance, E&E segment posted strong revenue growth at 26% yoy to Rs8.5 bn – ahead of estimates. However, with sharp rise in raw material prices (largely copper and silver) EBIT margins continued to contract – down 450 bps yoy to 8.4%.
- **Machinery & Industrial Products (M&IP)** – M&IP division performance was impacted by slowdown in industrial demand in general and in mining in particular. After posting strong growth for the past 5 quarters, revenues declined by 3% yoy to Rs6.8 bn. EBIT margins also dropped by 90 bps yoy to 15.7%.

Secures orders worth Rs161 bn – Down 21% yoy

Order inflows remained subdued on back of continued delays and deferrals in order finalizations. Order inflows declined by 21% yoy during Q2FY12E to Rs161 bn. Order inflows were led by Hydrocarbons (up 134% yoy on low base), while all the other sectors witnessed decline on yoy basis – namely Infrastructure (-20% yoy), Power (-53%) and Process (-3%). Order book growth at 23% yoy to Rs1422 bn – though forward order book cover remains healthy at 3.2X FY11E revenues.

Consolidated Financial Snapshot

Rs Mn

YE-	Net Sales	EBITDA (Core)	EBITDA (%)	APAT	EPS (Rs)	EPS %Chg	ROE (%)	P/E	EV/ EBITDA	P/BV
FY10	436,989	65,390	15.0	33,745	56.2	9.7	19.3	23.8	14.0	3.8
FY11P	520,991	81,855	15.7	41,790	68.9	22.7	18.2	19.4	12.1	3.3
FY12E	610,615	86,699	14.2	45,662	76.2	10.6	17.3	17.5	11.7	2.8
FY13E	675,814	98,537	14.6	52,692	89.6	17.6	17.6	14.9	10.4	2.4

Standalone Quarterly Results

Rs mn	Q2FY11	Q3FY11	Q4FY11	Q1FY12	Q2FY12	YoY (%)	QoQ (%)	YTD'12	YTD'11	Gr (%)
Revenue	93,308	114,131	153,842	94,826	112,452	20.5	18.6	207,279	171,620	20.8
Expenditure	83,251	101,752	130,434	83,561	100,712	21.0	20.5	184,273	151,513	21.6
Consumption of RM	69,857	89,613	114,734	73,082	83,807	20.0	14.7	156,889	130,251	20.5
as % of sales	75.4	79.2	76.1	77.1	74.5			75.7	76.4	
Employee Cost	8,288	6,772	8,153	7,660	11,041	33.2	44.1	18,701	13,928	34.3
as % of sales	9.0	6.0	5.4	8.1	9.8			9.0	8.2	
Other expenditure	5,105	5,367	7,547	2,819	5,865	14.9	108.0	8,684	7,334	18.4
as % of sales	5.5	4.7	5.0	3.0	5.2			4.2	4.3	
EBITDA	10,057	12,379	23,409	11,265	11,741	16.7	4.2	23,005	20,107	14.4
Depreciation	1,212	1,281	2,358	1,679	1,709	41.0	1.8	3,388	2,354	43.9
EBIT	8,845	11,098	21,051	9,586	10,032	13.4	4.6	19,618	17,753	10.5
Other Income	3,122	2,472	3,698	2,962	3,632	16.3	22.6	6,594	5,278	24.9
Interest	1,932	1,757	1,362	1,613	1,970	2.0	22.2	3,583	3,223	11.2
PBT	10,035	11,813	23,387	10,935	11,693	16.5	6.9	22,629	19,808	14.2
Total Tax	3,794	3,760	8,793	3,474	3,709	-2.2	6.8	7,183	6,905	4.0
Adjusted PAT	6,241	8,052	14,594	7,461	7,984	27.9	7.0	15,445	12,903	19.7
Extra ordinary items	1408	353	2268	0	0	-100.0	NA	0	1418	-100.0
Reported PAT	7,650	8,405	16,862	7,461	7,984	4.4	7.0	15,445	14,322	7.8
Adjusted EPS (Rs)	10.3	13.2	24.0	12.2	13.1	26.6	6.8	25.4	21.4	18.4

Margins (%)						(bps)	(bps)			(bps)
EBIDTA	10.8	10.8	15.2	11.9	10.4	-30	-140	11.1	11.7	-60
EBIT	9.5	9.7	13.7	10.1	8.9	-60	-120	9.5	10.3	-90
EBT	10.8	10.4	15.2	11.5	10.4	-40	-110	10.9	11.5	-60
PAT	6.7	7.1	9.5	7.9	7.1	40	-80	7.5	7.5	-10
Effective Tax rate	37.8	31.8	37.6	31.8	31.7	-610	0	31.7	34.9	-310

Lowered guidance – Order inflow growth at 5% and EBITDA margin decline 75-125 bps

L&T retained its revenue growth guidance at 25% for FY12E on the back of a robust order backlog and stable execution thereof – optimistic assumption with higher probability of downward revision in ensuing quarters. However it sharply revised down guidance for EBITDA margins and order inflows – (1) Expects EBITDA margins to decline by 75-125 bps (Vs 50-75 bps earlier) –change in revenue mix and sharp increase in raw material prices (2) Expects muted growth in order inflows at 5% (Vs erstwhile 15%) – in view of 11% yoy decline in H1FY12, no signs of revival in investment spends and continued postponements in order finalizations

...The same already stands factored in our estimates

We have already factored slowdown in order inflows & order execution and pressure on operating margins (the 2 principle concerns and risk to earnings) highlighted in our report “Delusional optimism to reality” dated 19 Oct'11. Consequently, EMKAY estimates are 7% and 6.7% lower then consensus estimates for FY12E and FY13E respectively.

Retain Accumulate rating

At CMP, stock is trading at attractive valuations of 17.5X FY11E and 14.9X FY13E consolidated earnings of Rs76.2 and Rs89.6 per share. However, absence of re-rating catalysts and earnings downgrades cycle in the near- term remains a concern. We have an Accumulate rating with a target price to Rs1603 (@ 18.3X FY13E earnings).

Segmental Performance

Rs mn	Q2FY11	Q3FY11	Q4FY11	Q1FY12	Q2FY12	YoY (%)	QoQ (%)	YTD'12	YTD'11	Gr (%)
Segment Revenues										
E&C	80,150	100,041	136,643	80,994	97,213	21.3	20.0	178,207	146,111	22.0
E&E	6,724	7,950	10,014	7,462	8,474	26.0	13.6	15,936	14,145	12.7
M&IP	6,981	6,807	8,661	6,904	6,780	-2.9	-1.8	13,684	12,449	9.9
Others	1,597	1,681	2,105	1,990	2,221	39.1	11.6	4,211	2,807	50.0
Less: Inter-seg. Rev.	1,331	1,382	2,237	1,566	938	-	-	0	0	
Total	94,122	115,097	155,186	95,784	113,750	20.9	18.8	209,534	173,222	21.0
Segment Results										
E&C	9,002	10,647	19,906	8,104	10,350	15.0	27.7	18,454	17,169	7.5
E&E	868	868	1,521	623	710	-18.2	14.0	1,332	1,606	-17.0
M&IP	1,156	1,286	1,733	1,220	1,063	-8.1	-12.9	2,282	2,286	-0.2
Others	172	214	459	422	477	177.0	12.9	899	507	77.3
Total	11,198	13,015	23,619	10,368	12,599	12.5	21.5	12,599	11,198	12.5
Add- Unall Income / (Exp)	1,438	1,006	3,403	2,091	1,212	-15.7	-42.0	1,212	1,438	-15.7
Less- Seg. Mgn on Cap.	-31	98	5	-89	148	-579.0	-266.1	148	-31	-
Less- Interest Exp	1,932	1,757	1,362	1,613	1,970	2.0	22.2	1,970	1,932	2.0
PBT	10,735	12,166	25,655	10,935	11,693	8.9	6.9	11,693	10,735	8.9
Capital Employed										
E&C	73,342	70,293	75,465	88,305	98,284	34.0	11.3	98,284	73,342	34.0
E&E	11,571	12,040	11,862	12,777	13,858	19.8	8.5	13,858	11,571	19.8
M&IP	2,723	3,278	4,702	5,597	6,904	153.5	23.4	6,904	2,723	153.5
Others	2,228	2,100	5,425	5,677	6,295	182.5	10.9	6,295	2,228	182.5
Unallocated	187,628	201,888	195,255	195,021	196,007	4.5	0.5	196,007	187,628	4.5
Total	277,492	289,599	292,708	307,375	321,349	15.8	4.5	321,349	277,492	15.8
Segment Margins (%)										
						(bps)	(bps)			(bps)
E&C	11.2	10.6	14.6	10.0	10.6	-60	60	10.4	11.8	-140
E&E	12.9	10.9	15.2	8.3	8.4	-450	0	8.4	11.4	-300
M&IP	16.6	18.9	20.0	17.7	15.7	-90	-200	16.7	18.4	-170
Average	11.7	11.2	15.0	10.7	11.0	-70	30	10.8	12.3	-150

Note:

E&C - Engineering & Construction

E&E - Electrical & Electronics

M&IP - Machinery & Industrial Products

Order Backlog Details

Rs bn	Q2FY11	Q3FY11	Q4FY11	Q1FY12	Q2FY12	YoY (%)	QoQ (%)
Order Backlog							
Order Inflows	204.6	133.7	304.1	161.9	161.0	(21.3)	(0.6)
Closing Order Book	1,153.9	1,148.8	1,302.2	1,361.7	1,421.9	23.2	4.4
Order Book Break-up (%)							
						(bps)	(bps)
Process	12.0	11.0	16.0	16.0	15.0	300	-100
Hydrocarbons	15.0	14.0	12.0	11.0	13.0	-200	200
Power	37.0	37.0	32.0	31.0	31.0	-600	0
Infrastructure	31.0	32.0	36.0	38.0	37.0	600	-100
Others	5.0	6.0	4.0	4.0	4.0	-100	0
Order Inflow Break-up (%)							
Process	9.7	5.3	29.0	8.2	11.6	190	340
Hydrocarbons	8.7	0.6	8.6	10.3	25.2	1,650	1,490
Power	42.9	32.1	14.0	22.7	25.2	-1,770	250
Infrastructure	30.1	50.0	44.4	50.5	30.0	-10	-2,050
Others	7.9	11.7	3.7	8.2	7.7	-20	-50

Subsidiaries Performance

Rs mn	Q2FY11	Q3FY11	Q4FY11	Q1FY12	Q2FY12	YoY (%)	QoQ (%)
L&T Infotech							
Revenues	5,860	6,040	7,020	7,370	7,920	35.2	7.5
Net Profit	780	710	910	950	1,080	38.5	13.7

Key Consolidated Financials

Income Statement

Y/E, Mar (Rs. mn)	FY10	FY11P	FY12E	FY13E
Net Sales	436,989	520,991	610,615	675,814
<i>Growth (%)</i>	8.3	18.3	18.4	10.7
Expenditure	371,599	439,137	523,916	577,277
Materials Consumed	273,933	326,668	386,851	428,157
Employee Cost	30,661	38,020	45,024	49,831
Manufacturing Exp	22,140	22,660	26,834	29,700
Other Exp	44,865	51,790	65,207	69,589
EBITDA	65,390	81,855	86,699	98,537
<i>Growth (%)</i>	16.4	25.2	5.9	13.7
EBITDA margin (%)	15.0	15.7	14.2	14.6
Depreciation	9,793	13,197	19,289	27,007
EBIT	55,597	68,658	67,410	71,529
EBIT margin (%)	12.7	13.2	11.0	10.6
Other Income	5,442	4,920	13,126	21,096
Interest expenses	6,919	8,309	9,221	10,329
PBT	54,119	65,269	71,316	82,297
Tax	20,374	23,479	25,654	29,604
<i>Effective tax rate (%)</i>	37.6	36.0	36.0	36.0
Adjusted PAT	33,745	41,790	45,662	52,692
<i>Growth (%)</i>	15.7	23.8	9.3	15.4
Net Margin (%)	7.7	8.0	7.5	7.8
(Profit)/loss from JVs/Ass/MI	71	10	559	1,663
Adj. PAT After JVs/Ass/MI	33,816	41,800	46,221	54,356
E/O items	20,691	2,761	-	-
Reported PAT	54,507	44,562	46,221	54,356
<i>Growth (%)</i>	12.8	23.6	10.6	17.6

Cash Flow

Y/E, Mar (Rs. mn)	FY10	FY11P	FY12E	FY13E
PBT	73,454	65,269	71,316	82,297
Depreciation	9,793	13,197	19,289	27,007
Interest Provided	6,919	8,309	9,221	10,329
Other Non-Cash items	-18,655	2,771	559	1,663
Chg in working cap	-28,318	-63,163	-49,973	-53,479
Tax paid	-17,547	-23,479	-25,654	-29,604
Operating Cashflow	25,647	2,904	24,757	38,214
Capital expenditure	-44,800	-62,057	-27,738	-28,280
Free Cash Flow	-19,154	-59,153	-2,980	9,934
Other income	0	0	0	0
Investments	-10,802	8,500	-1,368	-1,505
Investing Cashflow	-10,802	8,500	-1,368	-1,505
Equity Capital Raised	21,327	2,570	2,561	2,561
Loans Taken / (Repaid)	43,098	110,303	36,978	44,935
Interest Paid	-6,919	-8,309	-9,221	-10,329
Dividend paid (incl tax)	-7,219	-8,794	-10,553	-12,663
Income from investments	0	0	0	0
Others	114	786	532	-456
Financing Cashflow	50,402	96,556	20,298	24,048
Net change in cash	20,446	45,903	15,949	32,477
Opening cash position	14,590	33,216	79,119	95,068
Closing cash position	33,499	79,119	95,068	127,545

Balance Sheet

Y/E, Mar (Rs. mn)	FY10	FY11P	FY12E	FY13E
Equity share capital	4,699	4,707	4,707	4,707
Reserves & surplus	205,214	243,543	281,772	326,026
Net worth	209,913	248,250	286,479	330,733
Minority Interest	10,873	11,658	12,190	11,734
Secured Loans	141,859	0	0	0
Unsecured Loans	84,701	0	0	0
Loan Funds	226,561	336,864	373,842	418,777
Net deferred tax liability	1,530	1,530	1,530	1,530
Total Liabilities	448,876	598,302	674,042	762,774
Gross Block	161,081	223,138	250,876	279,155
Less: Depreciation	37,476	50,673	69,961	96,969
Net block	123,605	172,465	180,914	182,187
Capital work in progress	66,184	66,184	66,184	66,184
Investment	99,279	90,779	92,147	93,652
Current Assets	417,009	535,845	638,955	740,074
Inventories	23,782	42,996	67,646	93,385
Sundry debtors	125,280	142,097	168,276	186,244
Cash & bank balance	33,216	79,119	95,068	127,545
Loans & advances	160,299	197,200	233,531	258,467
Other current assets	0	0	0	0
Current lia & Prov	257,201	266,971	304,158	319,322
Current liabilities	232,459	240,593	272,688	284,646
Provisions	24,743	26,378	31,470	34,676
Net current assets	159,808	268,874	334,797	420,752
Misc. exp	-	-	-	-
Total Assets	448,876	598,302	674,042	762,774

Key Ratios

Y/E, Mar	FY10	FY11P	FY12E	FY13E
Profitability (%)				
EBITDA Margin	15.0	15.7	14.2	14.6
Net Margin	7.7	8.0	7.5	7.8
ROCE	15.6	14.3	12.9	13.1
ROE	19.3	18.2	17.3	17.6
RoIC	22.2	19.0	16.0	15.0
Per Share Data (Rs)				
EPS	56.2	68.9	76.2	89.6
CEPS	70.7	87.4	101.1	122.6
BVPS	348.6	409.3	472.4	545.3
DPS	12.5	14.5	17.4	20.9
Valuations (x)				
PER	23.8	19.4	17.5	14.9
P/CEPS	18.9	15.3	13.2	10.9
P/BV	3.8	3.3	2.8	2.4
EV / Sales	2.1	1.9	1.7	1.5
EV / EBITDA	14.0	12.1	11.7	10.4
Dividend Yield (%)	0.9	1.1	1.3	1.6
Gearing Ratio (x)				
Net Debt/ Equity	0.5	0.7	0.7	0.6
Net Debt/EBIDTA	1.6	2.2	2.3	2.2
Working Cap Cycle (days)	113.6	151.7	180.4	204.0

Recommendation History: Larsen & Toubro – LT IN

Date	Reports	Reco	CMP	Target
19/10/2011	Engineering and Capital Goods Sector Update			
08/08/2011	Larsen & Toubro Q1FY12 Result Update	Buy	1,630	1,936
20/05/2011	Larsen & Toubro Q4FY11 Result Update	Buy	1,595	2,015
17/01/2011	Larsen & Toubro Q3FY11 Result Update	Buy	1,681	2,015

Recent Research Reports

Date	Reports	Reco	CMP	Target
16/08/2011	McNally Bharat Q1FY12 Result Update	Buy	135	201
16/08/2011	Punj Lloyd Q1FY12 Result Update	Hold	56	76
05/08/2011	Cummins India Q1FY12 Result Update	Buy	614	687
04/08/2011	Elecon Engineering Q1FY12 Result Update	Buy	77	101

Emkay Global Financial Services Ltd.

Corporate Add: B – Ruby Mills Tower, 7th Floor, South East Wing, Senapati Bapat Marg, Dadar (W), Mumbai - 400028 India.

Tel.: +912266121212 Web: www.emkayglobal.com

DISCLAIMER: This document is not for public distribution and has been furnished to you solely for your information and may not be reproduced or redistributed to any other person. The manner of circulation and distribution of this document may be restricted by law or regulation in certain countries, including the United States. Persons into whose possession this document may come are required to inform themselves of, and to observe, such restrictions. This material is for the personal information of the authorized recipient, and we are not soliciting any action based upon it. This report is not to be construed as an offer to sell or the solicitation of an offer to buy any security in any jurisdiction where such an offer or solicitation would be illegal. No person associated with Emkay Global Financial Services Ltd. is obligated to call or initiate contact with you for the purposes of elaborating or following up on the information contained in this document. The material is based upon information that we consider reliable, but we do not represent that it is accurate or complete, and it should not be relied upon. Neither Emkay Global Financial Services Ltd., nor any person connected with it, accepts any liability arising from the use of this document. The recipient of this material should rely on their own investigations and take their own professional advice. Opinions expressed are our current opinions as of the date appearing on this material only. While we endeavor to update on a reasonable basis the information discussed in this material, there may be regulatory, compliance, or other reasons that prevent us from doing so. Prospective investors and others are cautioned that any forward-looking statements are not predictions and may be subject to change without notice. We and our affiliates, officers, directors, and employees world wide, including persons involved in the preparation or issuance of this material may; (a) from time to time, have long or short positions in, and buy or sell the securities thereof, of company (ies) mentioned herein or (b) be engaged in any other transaction involving such securities and earn brokerage or other compensation or act as a market maker in the financial instruments of the company (ies) discussed herein or may perform or seek to perform investment banking services for such company(ies) or act as advisor or lender / borrower to such company(ies) or have other potential conflict of interest with respect to any recommendation and related information and opinions. The same persons may have acted upon the information contained here. No part of this material may be duplicated in any form and/or redistributed without Emkay Global Financial Services Ltd.'s prior written consent. No part of this document may be distributed in Canada or used by private customers in the United Kingdom. In so far as this report includes current or historical information, it is believed to be reliable, although its accuracy and completeness cannot be guaranteed.