

November 8, 2011

Reco	Previous Reco
Hold	Hold
CMP	Target Price
Rs 69	Rs 61
EPS change FY12E/13E (%)	NA
Target Price change (%)	NA
Nifty	5,289
Sensex	17,570

Price Performance

(%)	1M	3M	6M	12M
Absolute	(2)	(5)	2	(27)
Rel. to Nifty	(10)	(8)	6	(13)

Source: Bloomberg

Relative Price Chart



Source: Bloomberg

Stock Details

Sector	Material Handling
Bloomberg	ELCN@IN
Equity Capital (Rs mn)	186
Face Value(Rs)	2
No of shares o/s (mn)	93
52 Week H/L	99/59
Market Cap (Rs bn/USD mn)	6/121
Daily Avg Volume (No of sh)	96929
Daily Avg Turnover (US\$m)	0.1

Shareholding Pattern (%)

	Sep-11	Jun-11	Mar-11
Promoters	45.8	45.7	45.7
FII/NRI	2.9	3.5	4.3
Institutions	13.1	12.1	11.9
Private Corp	9.0	7.2	7.5
Public	29.2	31.4	30.6

Source: Capitaline

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- **Meets expectations – (1) Revenue up 20% yoy to Rs3.4 bn led by TE div. (+22%); MHE div. (+19%) (2) EBITDA mgn up 50 bps, TE EBIT mgn fall 70 bps (3) APAT up 10% to Rs156 mn**
- **Order inflows at Rs2.6 bn (down 47% qoq) – YTD secured 52% of FY12E target. Order book healthy at Rs14.4 bn**
- **Debt remains high at 1.3X. EEL in high capex mode despite strained cash flow position – plans to spend Rs1-1.2 bn in FY12E (equal to past 2 years capex spends)**
- **We maintain our earnings estimates with H2FY12E asking rate undemanding at 14% yoy, but risks to earnings remain. Retain HOLD rating with price target of Rs61 per share**

Meets expectations – Net profit growth at 10% yoy to Rs156 mn

Elecon Engineering (EEL) reported healthy revenue growth at 20% yoy to Rs3.4 bn, ahead estimates – led by both divisions (MHE up 19% yoy) and (TE up 22% yoy). EBITDA grew by 24% yoy to Rs0.5 bn – led by 50 bps yoy improvement in EBITDA margins to 14.7%. Expansion in EBITDA margins was lower than estimates of 15.0% mostly due to impairment provisions on JVs in Australia and South Africa (total of Rs50-60 mn provision made in H1FY12 – mostly in Q2FY12 as per the management). High interest charges partially offset strong operational performance. Consequently, 10% yoy growth in net profits to Rs156 mn was in line with estimates (but adjusting for provision – net profit is above estimates)

MHE division – Strong performance

After 4 quarters of subdued performance, Material Handling Equipment (MHE) division saw sharp all round improvement in performance. Led by healthy opening order backlog, revenues grew 19% yoy to Rs1.9 bn – ahead estimates. EBIT margins expanded by 60 bps yoy to 13.3%, ahead estimates – attributed to benefits from operating leverage and favourable revenue mix.

TE division – EBIT margins fall sharply by 70 bps

Transmission Equipment (TE) division continued to witness strong revenue growth - revenues grew 22% yoy to Rs1.5 bn, meeting expectations. However, EBIT growth at 16% yoy to Rs0.2 bn was below estimates – due to 70 bps yoy drop in EBIT margins to 13.8% (lowest in past 20 quarters). Sharp drop in margins was attributed to higher contribution from low margin standard products and commencement of new facility.

Financial Snapshot

										Rs Mn
YE-	Net	EBITDA		EPS	EPS	ROE	EV/			
Mar	Sales	(Core)	(%)	APAT	(Rs)	%Chg	(%)	P/E	EBITDA	P/BV
FY10	10,464	1,540	14.7	500	5.4	-18.5	16.6	12.9	7.3	2.0
FY11	11,772	1,882	16.0	670	7.2	34.0	18.6	9.6	6.2	1.6
FY12E	13,571	2,020	14.9	757	8.2	13.0	17.9	8.5	5.5	1.4
FY13E	14,201	2,084	14.7	772	8.3	2.0	16.0	8.3	5.1	1.3

Standalone Quarterly Results

Rs mn	Q2FY11	Q3FY11	Q4FY11	Q1FY12	Q2FY12	YoY (%)	QoQ (%)	YTD'12	YTD'11	Gr (%)
Revenue	2,809	3,024	3,541	2,573	3,368	19.9	30.9	5,941	5,281	12.5
Expenditure	2,409	2,524	2,966	2,123	2,872	19.2	35.3	4,996	4,509	10.8
Consumption of RM	1,874	2,025	2,298	1,594	2,186	16.6	37.1	3,780	3,566	6.0
as % of sales	66.7	67.0	64.9	62.0	64.9			63.6	67.5	
Employee Cost	156	144	144	149	185	18.5	24.6	334	276	21.0
as % of sales	5.6	4.8	4.1	5.8	5.5			5.6	5.2	
Other expenditure	379	355	523	380	501	32.3	31.8	882	667	32.2
as % of sales	13.5	11.7	14.8	14.8	14.9			14.8	12.6	
EBITDA	400	500	575	450	496	24.0	10.3	945	772	22.5
Depreciation	98	98	99	98	108	10.9	10.1	207	187	10.6
EBIT	302	402	476	351	387	28.3	10.3	739	585	26.2
Other Income	4	-4	-11	0	4	1.3	#DIV/0!	4	11	-63.1
Interest	107	123	130	133	143	34.2	7.8	276	205	34.5
PBT	199	275	336	218	248	24.5	13.7	467	391	19.4
Total Tax	57	112	100	69	93	61.4	33.5	162	116	40.0
Adjusted PAT	142	163	236	149	156	9.7	4.5	305	275	10.7
Extra ordinary items	0	205	0	0	0	NA	NA	0	0	-
Reported PAT	142	368	236	149	156	9.7	4.5	305	275	10.7
Adjusted EPS	1.5	1.8	2.5	1.6	1.7	9.7	4.5	3.3	3.0	10.7

Margins (%)						(bps)	(bps)			(bps)
EBIDTA	14.2	16.5	16.2	17.5	14.7	50	-280	15.9	14.6	360
EBIT	10.8	13.3	13.4	13.6	11.5	80	-210	12.4	11.1	420
PBT	7.1	9.1	9.5	8.5	7.4	30	-110	7.9	7.4	340
PAT	5.1	5.4	6.7	5.8	4.6	-40	-120	5.1	5.2	180
Effective Tax rate	28.8	40.8	29.8	31.8	37.3	850	550	34.7	29.6	610

Order inflows at Rs2.6 bn, Order book at Rs14.4 bn

EEL secured orders worth Rs2.6 bn (up 25% yoy and down 47% qoq) and YTD Rs7.4 bn (52% of FY12E target). Deceleration in order inflow momentum is not a cause of concern, in view of healthy order bid pipeline and low asking rate for H2FY12E. Order backlog declined marginally by 6% qoq to Rs15.2 bn – split as Rs11.7 bn for MHE and Rs3.5 bn for TE. The MHE backlog dominated by Power (49%) followed by Mining (23%), Cement (9%), Port (8%) and Steel (6%). Also MHE backlog contribution has again swung in favour of longer execution Projects - contributing about 65% of backlog.

Debt remains high at 1.3X; EEL in high capex mode – plans to spend Rs1-1.2 bn in FY12E

EEL's standalone debt remained stable at Rs5.3 bn in Sep'11 (Vs Mar'11) – with no improvement in working capital situation. Correspondingly, DER continues to remain high at 1.3X. We believe that EEL's DER will remain stretched in the near future as EEL remains in high capex mode and strained cash flows. It plans to spend Rs1.0–1.2 bn in FY12E – this is equivalent to total capital expenditure incurred in FY10 and FY11 together and 1.5X FY11 operating cash flow. EEL plans to spend on capacity expansion in TE division (on standard helical gears) and regular maintenance of plants (no specific details given).

Retain FY12E and FY13E earnings estimates, Maintain Hold rating

Post revision in earnings (through our report dated 22 Oct'11 – Delusional optimism to reality) and healthy performance in Q2FY12, H2FY12E asking rate is undemanding at 14% yoy. We maintain our earnings estimates of Rs8.2 for FY12E and Rs8.3 per share for FY13E. However, risks to earnings remain from (1) concerns on profitability of incremental order inflows (2) profitable execution of current order backlog (3) high DER at 1.3X (Sep'11) amidst high capital expenditure planned. We retain HOLD rating with price target of Rs61 per share

Standalone segment results

Rs mn	Q2FY11	Q3FY11	Q4FY11	Q1FY12	Q2FY12	YoY (%)	QoQ (%)	YTD'12	YTD'11	Gr (%)
Segment Revenues										
Material Handling Equipment	1,610	1,639	1,998	1,424	1,922	19.4	35.0	3,347	3,108	7.7
Transmission Equipment	1,251	1,423	1,563	1,209	1,521	21.6	25.8	2,729	2,261	20.7
Less: Intersegment Revenues	55	53	54	90	90	-	-	0	0	-
Total	2,805	3,009	3,507	2,543	3,354	19.5	31.9	5,897	5,266	12.0
Segment Results										
Material Handling Equipment	204	220	276	193	256	25.1	32.3	449	396	13.4
Transmission Equipment	181	253	253	184	209	15.7	14.0	393	334	17.7
Total	385	473	529	377	465	20.7	23.4	842	730	15.4
Add- Unall Income / (Exp)	-79	-75	-64	-26	-77	-	-	-103	-134	-
Less- Interest Exp	107	123	130	133	143	34.2	7.8	276	205	34.5
PBT	200	275	336	218	244	22.5	11.8	463	391	18.3
Segment Capital Employed										
Material Handling Equipment	5,041	5,055	4,921	4,819	4,807	-4.6	-0.3	4,807	5,041	-4.6
Transmission Equipment	4,043	3,898	4,704	4,858	5,143	27.2	5.9	5,143	4,043	27.2
Unallocated	0	0	0	0	0			0	0	#DIV/0!
Total	9,084	8,952	9,626	9,677	9,949	9.5	2.8	9,949	9,084	9.5
Segment Margins (%)										
						(bps)	(bps)			(bps)
Material Handling Equipment	12.7	13.4	13.8	13.6	13.3	60	-30	13.4	12.7	70
Transmission Equipment	14.5	17.8	16.2	15.2	13.8	-70	-140	14.4	14.8	-40
Average	13.5	15.5	14.9	14.3	13.5	0	-80	13.9	13.6	30

Order Backlog Details

Rs mn	Q2FY11	Q3FY11	Q4FY11	Q1FY12	Q2FY12	YoY (%)	QoQ (%)
Order Backlog							
Material Handling Equipment	8,430	9,620	10,590	12,280	11,700	38.8	-4.7
Transmission Equipment	3,350	3,250	3,250	3,760	3,450	3.0	-8.2
Total	11,780	12,870	13,840	16,040	15,150	28.6	-5.5
Order Inflows							
Material Handling Equipment	740	2,829	3,780	3,114	1,342	81.4	-56.9
Transmission Equipment	1,311	1,323	1,563	1,719	1,211	-7.6	-29.5
Total	2,050	4,152	5,343	4,833	2,553	24.5	-47.2

Key Financials

Income Statement

Y/E, Mar (Rs. mn)	FY10	FY11	FY12E	FY13E
Net Sales	10,464	11,772	13,571	14,201
Growth (%)	9.6	12.5	15.3	4.6
Expenditure	8,924	9,890	11,552	12,117
Materials Consumed	6,982	7,434	8,747	9,153
Employee Cost	436	565	651	681
Manufacturing Exp	614	819	944	988
Other Exp	892	1,072	1,210	1,295
EBITDA	1,540	1,882	2,020	2,084
Growth (%)	-10.7	22.2	7.3	3.2
EBITDA margin (%)	14.7	16.0	14.9	14.7
Depreciation	331	384	430	463
EBIT	1,209	1,498	1,590	1,621
EBIT margin (%)	11.6	12.7	11.7	11.4
Other Income	41	-42	40	34
Interest expenses	509	458	502	505
PBT	741	998	1,128	1,150
Tax	241	328	370	378
Effective tax rate (%)	32.6	32.8	32.8	32.8
Adjusted PAT	500	670	757	772
Growth (%)	-18.5	34.0	13.0	2.0
Net Margin (%)	4.8	5.7	5.6	5.4
E/O items	161.7	209.1	0.0	0.0
Reported PAT	662	879	757	772
Growth (%)	20.4	32.9	-13.9	2.0

Cash Flow

Y/E, Mar (Rs. mn)	FY10	FY11	FY12E	FY13E
PBT	748	1,207	1,128	1,150
Depreciation	331	384	430	463
Interest Provided	509	458	502	505
Other Non-Cash items	-19	-223	0	0
Chg in working cap	339	-756	294	-53
Tax paid	-180	-220	-370	-378
Operating Cashflow	1,729	851	1,983	1,688
Capital expenditure	-841	-444	-850	-500
Free Cash Flow	888	406	1,133	1,188
Other income	0	0	0	0
Investments	212	-100	24	0
Investing Cashflow	212	-100	24	0
Equity Capital Raised	0	0	0	0
Loans Taken / (Repaid)	-705	88	500	75
Interest Paid	-455	-492	-502	-505
Dividend paid (incl tax)	-161	-160	-167	-167
Income from investments	0	0	0	0
Others	0	0	0	0
Financing Cashflow	-1,322	-564	-169	-597
Net chg in cash	-222	-258	987	591
Opening cash position	611	388	131	1,118
Closing cash position	388	131	1,118	1,709

Balance Sheet

Y/E, Mar (Rs. mn)	FY10	FY11	FY12E	FY13E
Equity share capital	186	186	186	186
Reserves & surplus	3,075	3,760	4,350	4,956
Net worth	3,261	3,946	4,536	5,141
Secured Loans	3,329	3,135	3,635	3,710
Unsecured Loans	1,887	2,169	2,169	2,169
Loan Funds	5,216	5,303	5,803	5,878
Net deferred tax liability	-403	-411	-411	-411
Total Liabilities	8,074	8,839	9,929	10,609
Gross Block	5,094	5,597	6,447	6,947
Less: Depreciation	1,651	2,020	2,450	2,913
Net block	3,443	3,577	3,997	4,034
Capital work in progress	179	108	108	108
Investment	57	363	340	340
Current Assets	9,263	10,610	11,961	12,870
Inventories	3,152	3,144	3,527	3,690
Sundry debtors	5,176	6,720	6,701	6,856
Cash & bank balance	388	131	1,118	1,709
Loans & advances	547	615	615	615
Other current assets	0	1	2	3
Current lia & Prov	4,088	5,032	5,690	5,956
Current liabilities	3,868	4,786	5,444	5,710
Provisions	220	246	246	246
Net current assets	5,174	5,578	6,271	6,915
Misc. exp	26	34	34	34
Total Assets	8,879	9,660	10,750	11,430

Key Ratios

Y/E, Mar	FY10	FY11	FY12E	FY13E
Profitability (%)				
EBITDA Margin	14.7	16.0	14.9	14.7
Net Margin	4.8	5.7	5.6	5.4
ROCE	13.5	16.2	15.6	14.6
ROE	16.6	18.6	17.9	16.0
RoIC	16.2	18.2	19.0	19.2
Per Share Data (Rs)				
EPS	5.4	7.2	8.2	8.3
CEPS	9.0	11.4	12.8	13.3
BVPS	35.1	42.5	48.8	55.4
DPS	1.5	1.8	1.8	1.8
Valuations (x)				
PER	12.9	9.6	8.5	8.3
P/CEPS	7.8	6.1	5.4	5.2
P/BV	2.0	1.6	1.4	1.3
EV / Sales	1.1	1.0	0.8	0.7
EV / EBITDA	7.3	6.2	5.5	5.1
Dividend Yield (%)	2.2	2.6	2.6	2.6
Gearing Ratio (x)				
Net Debt/ Equity	1.5	1.3	1.0	0.8
Net Debt/EBITDA	3.1	2.7	2.3	2.0
Working Cap Cycle (days)	190.8	166.7	159.3	169.5

Recommendation History: Elecon Engineering – ELCN IN

Date	Reports	Reco	CMP	Target
19/10/2011	Engineering & Capital Goods Sector Update			
04/08/2011	Elecon Engineering Q1FY12 Result Update	Buy	77	101
26/05/2011	Elecon Engineering Q4FY11 Result Update	Buy	67	89
25/03/2011	Elecon Engineering Management Meet Update	Buy	65	89

Recent Research Reports

Date	Reports	Reco	CMP	Target
03/11/2011	TRF Q2FY12 Result Update	Hold	353	282
24/10/2011	Greaves Cotton Q2FY12 Result Update	Buy	89	103
24/10/2011	Blue Star Q2FY12 Result Update	Hold	197	185
21/10/2011	Larsen and Toubro Q2FY12 Result Update	Accumulate	1,336	1,603

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