

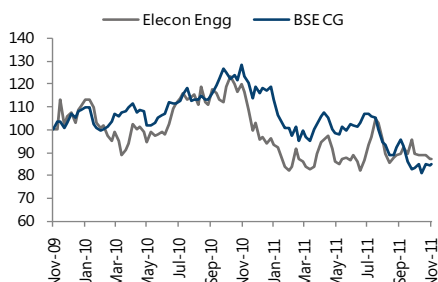
Result Update - Q2FY12

Buy

Reco	Maintained
CMP	₹ 69.4
Target Price	₹ 91.0
Upside Potential	30.8%

Price Performance

52 wk Hi/Lo	98/59
All time Hi/Lo	343/0.54
6 mnth Average Vol	94310
Stock Beta	0.62



Valuation

	FY11	FY12P	FY13P
P/E (x)	9.6	8.4	6.6
P/BV (x)	1.6	1.4	1.2
RONW (%)	24.4	18.1	19.9
ROCE (%)	11.4	11.2	12.3

Peer Valuation (FY13P)

	McNally	TRF
P/E	3.5	7.9
P/BV	0.7	1.5

Equity Data

Market Cap. (₹ bln)	6.4
Face value (₹)	2
No of shares o/s (mln)	93

	Sep'10	Sep'11	%Δ
Promoters	45.71	45.82	0.24
DFI's	13.76	13.36	-2.91
FII's	3.40	2.05	-39.70
Public	37.13	38.77	4.42

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Elecon Engineering

Strong quarter; though order inflow sluggish

Elecon's Q2FY12 were above expectations with sales exceeding our estimates by 7%. Sales for the company grew by 20% y-o-y to ₹ 3.4bln. EBITDA grew by 24% y-o-y to ₹ 496mln driven by decline in raw material cost and improvement in margins of material handling equipment (MHE) segment. PAT grew by 10% y-o-y to ₹ 156mln.

- MHE segment's sales grew by 19.4% y-o-y to ₹ 1.9bln driven by strong execution as well as deferred sales of previous quarter being booked in Q2FY12. Gear segment's sales jumped 21.6% y-o-y to ₹ 1.5bln in Q2FY12. MHE division contributed 56% to the total sales and the rest was contributed by Gear segment.
- EBITDA margin for Elecon improved by 40bps y-o-y to 14.7% due to decline in raw material cost as a percentage to sales from 67% to 64.9%. Margin expansion is also a result of 60bps increase in MHE's EBIT margin which contributed 55% to the total EBIT. Gear division's margin declined 70bps from 14.47% to 13.76% PAT grew moderately by 9.6% y-o-y to ₹ 156mln due to increase in interest cost by 34% to ₹ 143mln.
- Elecon's order book is ₹ 15.15bln (up 28.6% y-o-y and down 5.5% q-o-q) of which MHE division's order book is ₹ 11.7bln; while order backlog for transmission gear stands at ₹ 3.5bln. Order inflow was just ₹ 2.4bln (up 3% y-o-y and down 50% q-o-q) mainly due to seasonality in award of orders.
- Currently Elecon has a strong bidding pipeline which includes coal handling packages for NTPC bulk tenders of 11x660MW. Elecon is also optimistic on prospective orders from Adani and Bajaj Hindustan.

Outlook and Valuation

The management still sticks to their guidance of 20-25% y-o-y growth; which makes the asking rate for H2FY12 26% y-o-y. In the backdrop of decline in commodity prices, we believe the sustainable margins should be between 15.4-15.6%. We have revised our sales estimates to factor in our concern on meeting its sales target and hence sales estimates for FY12 and FY13 stands reduced by 6.7% and 9.2% respectively. We expect the company's top line to grow at a CAGR of 16.8% over FY11-13P and bottom line by 20.7% over the same period. At CMP; Elecon trades at a PE of 8.4x FY12P and 6.6x FY13P earnings. We maintain Buy with a revised target price of ₹ 90.7 per share ((based on standalone value of ₹ 84.3 (FY13Px8) and Benzlers Radicon's value of ₹ 6.4 (FY13EPS of ₹ 1.28x5)).

Summary Financials

₹ in Mn	FY10	FY11	FY12P	FY13P
Total Income	10543	11845	13463	16171
OPBDIT	1575	1838	2093	2498
Net Profit	661	879	767	979
EPS	7.1	9.5	8.3	10.5
Networth	3261	3946	4539	5278
Debt	5216	5303	5616	5916
Fixed Assets	3622	3506	4250	4743
Net Current Assets	5174	5578	6271	7267

Key Result Highlights

Exhibit 1: Q2FY12 Highlights

(in ₹ Mln)	Q2FY12	Q2FY11	Y-o-Y	Q1FY12	Q-o-Q
Total Income	3368	2798	20%	2573	31%
Raw material cost	2186	1874	17%	1594	37%
Staff cost	185	156	19%	149	25%
Other expenditure	501	368	36%	380	32%
OPBDIT	496	400	24%	450	10%
OPBDIT margin (%)	14.7	14.3		17.5	
Depreciation	108	98	11%	98	10%
Interest cost	143	107	34%	133	8%
Other Income	4	4	1%	-	-
PBT	248	200	24%	218	14%
Tax	93	57	61%	69	33%
PAT	156	142	10%	149	4%
EPS	1.68	1.53		1.61	

Source: Company

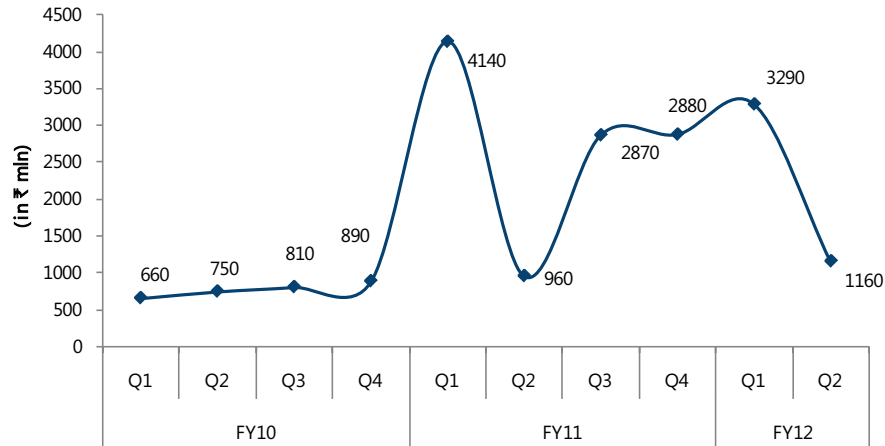
- Elecon's total income for Q2FY12 grew by 20% y-o-y to ₹ 33.7bln compared to ₹ 27.98bln in Q2FY11. The growth in top line was led by 19.4% y-o-y increase in MHE division and 21.6% y-o-y jump in Transmission Gear segment.
- EBITDA increased by 24% y-o-y to ₹ 496mln. EBITDA margin for the company improved by around 40bps y-o-y from 14.3% to 14.7% in Q2FY12. The raw material cost as a percentage of sales declined sharply from 67% to 64.9%; which led to improvement in margins. EBIT margin for MHE has increased from 12.7% to 13.3%, although EBIT margin in transmission gear segment declined due to high depreciation expenses as a result of capex incurred off late in gear division.
- Interest cost for the quarter has grown by 34% y-o-y and has resulted in PAT growth of just 10% y-o-y to ₹ 156mln. Currently, the company has debt of ₹ 5.27bln on standalone basis and on consolidated basis the debt stands around ₹ 6.2bln.

Exhibit 2: Segmental Analysis

(in ₹ Mln)	Q2FY12	Q2FY11	Y-o-Y	Q1FY12	Q-o-Q
MHE					
Revenue	1922	1610	19%	1424	35%
PBIT	256	204	25%	193	32%
PBIT Margin (%)	13.3	12.7		13.6	
Transmission Gear					
Revenue	1521	1251	22%	1209	26%
PBIT	209	181	16%	184	14%
PBIT Margin (%)	13.8	14.5		15.2	
Revenue Mix (%)					
MHE	55.8%	59.7%		54.1%	
Transmission Gear	44.2%	40.3%		45.9%	

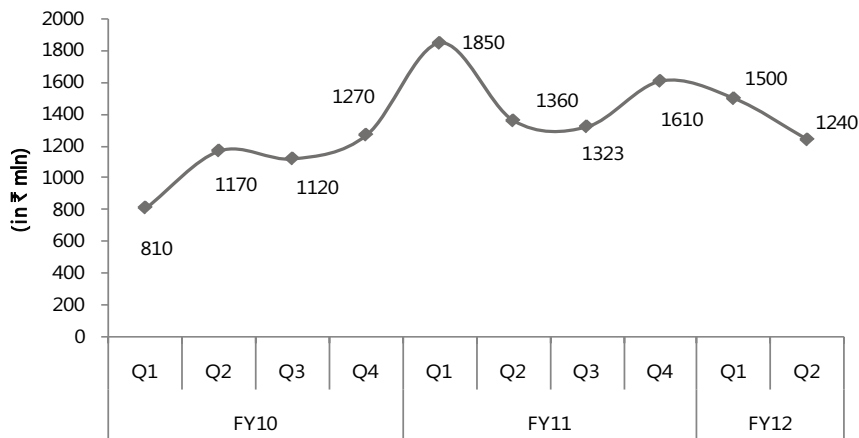
Source: Company

Exhibit 3: Quarterly Order Inflow in MHE division



Source: Company, MSFL Research

Exhibit 4: Quarterly Order Inflow in Gear division



Source: Company, MSFL Research

Unexecuted order book at ₹ 15.2bln (up 28.6% y-o-y, down 5.5% q-o-q)

The order book of MHE segment stands at ₹ 11.6bln as against ₹ 8.4bln in Q2FY11. In gear division the order book stands at ₹ 3.4bln as compared to ₹ 3.35bln in Q2FY11. Order inflow for the company for Q2FY12 was ₹ 4.79bln; up 3% y-o-y of which orders from MHE division were of ₹ 3.3bln; while transmission gear had an order inflow of ₹ 1.5bln. Elecon has a strong order pipeline as it is awaiting an LOI for coal handling packages for NTPC bulk tenders of 11x660MW. Elecon is also optimistic of prospective orders from Adani and Bajaj Hindustan.

Change in estimates

Although management is confident of managing 20-25% y-o-y growth in sales for FY12; we are skeptical as the asking rate for H2FY12 comes to around 26% y-o-y. We believe this can be challenging based on the existing capacity. Therefore, we revise our sales estimates by 6.7% and 8.9% respectively. Also, factoring in the decline in commodity prices we revise our EBITDA margin estimates upwards. Although, bottom line estimates are revised downwards keeping in line with the increased interest cost.

Exhibit 5: Change in estimates

In ₹ Mln	FY12P			FY13P		
	Revised	Old	% chg	Revised	Old	% chg
Sales	13463	14425	-6.7%	16171	17804	-9.2%
EBITDA	2093	2214	-5.4%	2498	2707	-7.7%
EBITDA Margin %	15.6	15.3	30 bps	15.5	15.2	30 bps
PAT	767	876	-12.4%	979	1157	-15.4%

Source: MSFL Research

Other key conference call takeaways

- The company plans to incur capex of ₹ 1-1.1bln for FY12; out of which 60-65% will be towards gear division for enhancing capacity and replacement of few equipments.
- Management has maintained its guidance of 25% y-o-y growth in FY12 for sales and expects to maintain its margins. The management is of the view that Elecon as well as its competitors have decent revenue visibility and it is unlikely that these players will resort to aggressive bidding to win orders.
- Elecon's SPV- Benzlers Radicon has recorded sales of ₹ 1.21bln for H1FY12 and PAT margin is around 2-3%. The company maintained its sales guidance of ₹ 2.4bln for FY12.

Outlook and Valuation

At CMP; Elecon trades at a PE of 8.4x FY12P and 6.6x FY13P on standalone earnings. The stock looks attractive at this level given the decent revenue visibility and strong bidding pipeline and attractive margins. However, good order inflow is imperative for a strong visibility beyond first quarter of FY13. We expect top line to grow at a CAGR of 16.8 % over FY11-FY13P. We expect recurring PAT to grow at a CAGR of 20.7% during the same period. We arrive at a target price of ₹ 91 per share, which is based on standalone value of ₹ 84.3 (FY13P EPS of ₹ 10.5x8) and Benzlers-Radicon's value of ₹ 6.4 (FY13P EPS of ₹ 1.28x5).

Financial Summary

Profit & Loss

Particulars (₹ in mln)	2009	2010	2011	2012P	2013P
Total Income	9551	10543	11845	13463	16171
Total Expenditure	8060	8968	10007	11369	13673
EBITDA	1490	1575	1838	2093	2498
EBITDA Margin (%)	15.6	14.9	15.5	15.6	15.5
Depreciation	221	331	384	435	507
EBIT	1269	1243	1454	1658	1991
Interest cost	484	509	458	555	580
Operating Profit	785	735	996	1103	1412
Other Income	96	168	211	17	17
Extraordinary Item	25	-	-	-	-
PBT	906	903	1207	1120	1429
Tax	306	241	328	353	450
PAT	550	661	879	767	979
Rec. PAT	549	500	672	767	979
PAT Margin (%)	7.0	6.3	7.4	5.7	6.1
EPS	5.9	7.1	9.5	8.3	10.5
Adj. EPS	5.9	5.4	7.2	8.3	10.5
Sales Growth (%)	15.6	10.4	12.4	13.7	20.1
EBITDA Growth (%)	14.2	5.7	16.8	13.9	19.3
PAT Growth (%)	-18.2	20.3	32.9	-12.7	27.6
Recurring PAT Growth (%)	-12.6	-8.9	34.5	14.2	27.6

Balance Sheet

Particulars (₹ in mln)	2009	2010	2011	2012P	2013P
Sources of Funds					
Share Capital	186	186	186	186	186
Reserves & Surplus	2568	3075	3760	4353	5092
Networth	2754	3261	3946	4539	5278
Secured Loans	5236	3329	3135	3729	4029
Unsecured Loans	685	1887	2169	1887	1887
Total Loans	5921	5216	5303	5616	5916
Deferred Tax Liability (Net)	328	403	411	411	411
TOTAL	9003	8879	9660	10565	11605

Application of Funds

Net Fixed Assets	3111	3622	3506	4250	4743
Investment	109	57	363	429	429
Current Assets	10085	9263	10610	11998	14462
Current Liabilities	4318	4088	5032	5728	7195
Net Current Assets	5767	5174	5578	6271	7267
Deferred Tax Asset (Net)	17	26	34	34	34
TOTAL	9003	8879	9660	10565	11605

Cash Flow

Particulars (₹ in mln)	2009	2010	2011P	2012P	2013P
Internal accruals	771	993	1263	1202	1486
(Inc)/Dec in Net Current Assets	(2171)	887	(756)	237	(395)
Other adjustments	2113	(178)	-	-	-
Cash flow from Operations	713	1701	819	1792	1541
Inc/(Dec) in Debt	1828	(705)	88	312	300
Inc/(Dec) in Equity	-	-	-	-	-
Interest, Dividend & Tax	(652)	(616)	(652)	(174)	(240)
Cash flow from Financing	1176	(1322)	(564)	138	60
Fixed Asset formation	(1400)	(841)	(444)	(1000)	(1000)
Inc/(Dec) in Investment	(14)	212	-	-	-
Other adjustments	61	28	-	-	-
Cash flow from Investment	(1353)	(602)	(473)	(1000)	(1000)
Net Change in Cash	535	(222)	(218)	930	601

Ratio

Valuation Ratio	2009	2010	2011P	2012P	2013P
P/E	11.7	12.9	9.6	8.4	6.6
P/BV	2.3	2.0	1.6	1.4	1.2
EV/EBIDTA	7.9	7.2	6.3	5.3	4.3
EV/Sales	1.1	1.1	1.0	0.8	0.7
Dividend Yield (%)	2.2	2.2	2.6	2.3	3.2
EPS	5.9	7.1	9.5	8.3	10.5
DPS	1.5	1.5	1.8	1.6	2.2
Book Value	29.7	35.1	42.5	48.9	56.8
ROE	21.5%	22.0%	24.4%	18.1%	19.9%
ROCE	10.7%	10.2%	11.4%	11.2%	12.3%

Solvency Ratio (x)

Debt/Equity	2.1	1.6	1.3	1.2	1.1
Debt/EBIDTA	4.0	3.3	2.9	2.7	2.4

Turnover Ratio (x)

Asset Turnover	1.2	1.2	1.3	1.3	1.5
Fixed Asset Turnover	3.8	3.1	3.2	3.4	3.6
Current Ratio	2.3	2.3	2.1	2.1	2.0
Inventory (days)	189	179	146	133	127
Debtors (days)	184	171	183	184	180
Creditors (days)	177	170	167	169	163

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Key ratings:

Rating	Expected Return
Buy	> 15%
Accumulate	5 to 15%
Hold	-5 to 5%
Sell	< -5%
Not Rated	-

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