Crompton Greaves

28 May 2012

Reuters: CROM.BO; Bloomberg: CRG IN

4QFY12 Result Update

Risk-Reward Ratio Turns Favourable; We Upgrade To Buy

Crompton Greaves (CGL) reported 4QFY12 consolidated revenue of Rs30.7bn, in line with our estimate, posting a 5.8% YoY revenue growth. However, as seen in the 9MFY12 period, profitability was under severe pressure as consolidated EBITDA/PAT fell 42.9%/60.1% YoY to Rs2.1bn/Rs1.0bn, respectively. EBITDA/PAT was 16.6%/31.2% below our and 19.3%/38.7% below Bloomberg consensus estimates, respectively. Consequently, we revise downwards our FY13 earnings estimates by 15.3%. On the positive side, operating margin grew 90bps sequentially, while order inflow was better than expected at Rs29bn. After a 630bps YoY decline in operating margin in FY12, from 13.4% to 7.1%, we expect recovery in margins in FY13/14E across business segments driven by cost rationalisation and improving product realisation. We believe the erosion of margins in FY12 is priced in and the stock trades at an attractive valuation considering likely 34.8% earnings CAGR over FY12-14E, albeit on a low base. We introduce FY14 financials and upgrade the stock from Sell to Buy with a target price of Rs127 (from Rs108 earlier) based on 12xFY14E EPS.

Healthy order book to drive revenue: Order inflows rose 12% YoY to Rs29bn for the quarter led by a 13% YoY rise in Power systems orders (Rs24.5bn) and a 9% YoY rise in Industrial systems orders (Rs4.5bn). As a result, the order backlog rose 17% YoY to Rs83.6bn, the highest ever, offering healthy revenue visibility. Order book to TTM sales ratio stands at 0.74x, maintained even during the tough times in FY12.

FY13 guidance encouraging: The management believes the worst is over in FY12 and have given guidance of 12-14% revenue growth, 8-9% operating margin and robust order inflow in FY13. Our expectations are lower than the management's guidance as we expect revenue to show 10.5% CAGR over FY12-14E while we factor in 90bps/80bps YoY rise in operating margin to 8.0%/8.8% in FY13/14E, respectively.

Valuation attractive, we upgrade stock to Buy: Owing to severe erosion in margins in FY12, the stock declined 57.8% YTD and 25% since we initiated coverage in January 2012, trading near our earlier TP of Rs108. We find it attractive at CMP considering healthy revenue visibility owing to a life-time high order backlog, recovery in operating margin over FY13-14E and likely strong earnings CAGR of 34.8% over FY12-14E. At the CMP of Rs106, it trades at 12.8x/10x FY13/14E EPS versus the past five years' average PE of 17.9x. We value CGL at 12xFY14E EPS of Rs10.6 with a TP of Rs127, offering 20% upside, and upgrade our rating on it from Sell to Buy.

BUY

Sector: Capital Goods

CMP: Rs106

Target Price: Rs127

Upside: 20%

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Key Data

Current Shares O/S (mn)	641.7
Mkt Cap (Rsbn/US$bn)	68.8/1.2
52 Wk H / L (Rs)	278/103
Daily Vol. (3M NSE Avg.)	1,934,840

Price Performance (%)

	1 M	6 M	1 Yr
Crompton Greaves	(19.2)	(11.0)	(57.8)
Nifty Index	(5.4)	4.5	(8.0)

Source: Bloomberg

Y/E March (Rsmn) (consolidated)	4QFY11	3QFY12	4QFY12	YoY (%)	QoQ (%)	FY11	FY12	YoY (%)
Revenues (net)	29,080	30,280	30,774	*5.8*	*1.6*	100,051	112,486	*12.4*
Raw material costs	18,972	21,297	21,073	*11.1*	*(1.1)*	62,689	76,850	*22.6*
Staff costs	2,719	3,929	3,938	*44.8*	*0.2*	11,811	14,662	*24.1*
Other expenses	3,658	3,227	3,631	*(0.7)*	*12.5*	12,113	12,937	*6.8*
Total expenditure	25,350	28,453	28,642	*13.0*	*0.7*	86,613	104,449	*20.6*
EBITDA	3,731	1,826	2,132	*(42.9)*	*16.7*	13,438	8,037	*(40.2)*
EBITDAM (%)	*12.8*	*6.0*	*6.9*	-	-	*13.4*	*7.1*	-
Depreciation	597	627	639	*7.1*	*1.9*	1,936	2,600	*34.3*
Interest costs	72	112	139	*93.1*	*24.1*	201	463	*131.0*
Other income	468	155	3	*(99.3)*	*(98.0)*	990	524	*(47.1)*
PBT	3,148	1,242	1,357	*(56.9)*	*9.2*	11,910	5,497	*(53.8)*
Tax	683	487	396	*(42.0)*	*(18.6)*	3,100	1,821	*(41.2)*
PAT before M.I and profits from associates	2,465	755	960	*(61.0)*	*27.2*	8,810	3,676	*(58.3)*
Less: Minority interest	2	(3)	(3)	-	-	4	(7)	-
Add: Share of profits from associates	51	13	40	-	-	80	53	-
Net profit	2,514	771	1,003	*(60.1)*	*30.0*	8,886	3,737	*(58.0)*
NPM (%)	*8.6*	*2.5*	*3.3*	-	-	*8.9*	*3.3*	-
EPS (Rs)	3.9	1.2	1.6	*(60.1)*	*30.0*	13.9	5.8	*(58.0)*

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 1: Financial summary (consolidated)

Y/E March (Rsmn)	FY10	FY11	FY12	FY13E	FY14E
Net sales	91,409	100,051	112,486	124,832	137,398
EBITDA	12,770	13,438	8,037	9,989	12,103
Net profit	8,599	8,886	3,737	5,309	6,791
EPS (Rs)	13.4	13.9	5.8	8.3	10.6
EPS growth (%)	*53.6*	*3.3*	*(58.0)*	*42.1*	*27.9*
EBITDA margin (%)	*14.0*	*13.4*	*7.1*	*8.0*	*8.8*
PER (x)	7.9	7.7	18.2	12.8	10.0
P/BV (x)	2.7	2.1	1.9	1.7	1.5
EV/EBITDA (x)	5.2	5.2	8.8	7.4	6.2
Dividend yield (%)	*1.4*	*2.4*	*2.1*	*2.1*	*2.1*
RoCE (%)	*40.3*	*34.0*	*14.2*	*16.5*	18.1
RoE (%)	*38.0*	*32.1*	*11.0*	*14.3*	*16.3*

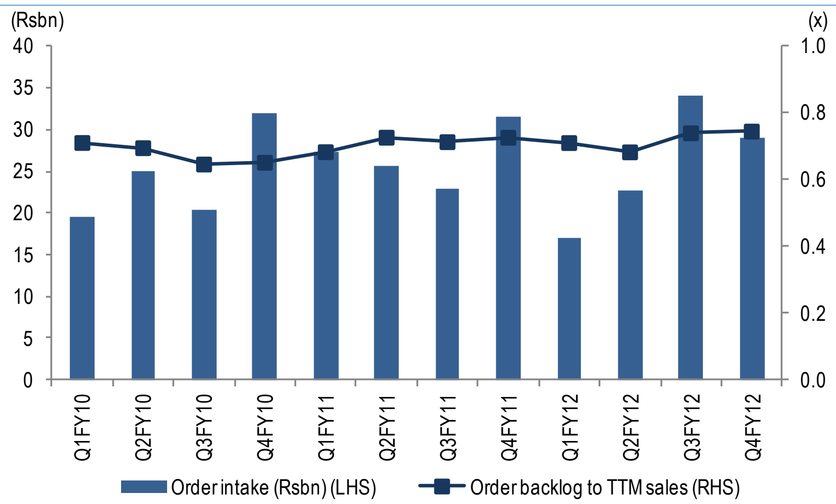
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 2: Segmental snapshot (consolidated)

Y/E March	4QFY11	3QFY12	4QFY12	*YoY (%)*	*QoQ (%)*	FY11	FY12	*YoY (%)*
Revenue (Rsmn)								
Power systems	19,235	20,689	19,683	*2.3*	*(4.9)*	65,029	73,149	*12.5*
Consumer products	5,508	5,033	6,065	*10.1*	*20.5*	20,212	21,336	*5.6*
Industrial systems	4,346	4,749	5,001	*15.1*	*5.3*	14,971	18,202	*21.6*
Revenue mix (%)								
Power systems	*66.1*	*67.9*	*64.0*			*64.9*	*64.9*	
Consumer products	*18.9*	*16.5*	*19.7*			*20.2*	*18.9*	
Industrial systems	*14.9*	*15.6*	*16.3*			*14.9*	*16.2*	
EBIT (Rsmn)								
Power systems	2,570	518	541	*(78.9)*	*4.6*	8,068	2,394	*(70.3)*
Consumer products	789	593	740	*(6.2)*	*24.8*	2,928	2,629	*(10.2)*
Industrial systems	649	494	542	*(16.5)*	*9.6*	2,642	2,103	*(20.4)*
EBIT margin (%)								
Power systems	*13.4*	*2.5*	*2.7*			*12.4*	*3.3*	
Consumer products	*14.3*	*11.8*	*12.2*			*14.5*	*12.3*	
Industrial systems	*14.9*	*10.4*	*10.8*			*17.6*	*11.6*	

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 3: Consolidated order inflow, earnings visibility – Maintained even during tough times



Source: Company, Nirmal Bang Institutional Equities Research

Segmental snapshot: The revenue of consolidated power systems segment grew by a healthy 12.5% YoY to Rs73.2bn, driven by domestic business (Rs28.7bn revenue, 12.3% YoY growth) and overseas subsidiaries (Rs44.5bn revenue, 12.6% YoY growth). For FY13E/14E, we expect the consolidated power systems segment to register revenue growth of 11.4%/10.8% YoY, respectively, on the back of a 17% YoY rise in order inflow to Rs84.7bn in FY12. However, margins fell sharply due to severe pricing pressure in the domestic T&D (transmission and distribution) segment, 25% of order backlog in low-margin systems business and cost overrun in some projects in Europe worth euro 50mn delivered at 0% margin. Operating margin of the consolidated power systems segment fell 910bps YoY, from 12.4% in FY11 to 3.3% in FY12. For FY13E/14E, we expect consolidated operating margins of the power systems segment to recover to 5.6%/6.7%, respectively, driven by improved product realisation (765KV transformer prices have recovered to Rs125mn in 4QFY12 from Rs100mn in 4QFY11) and cost rationalisation measures. The consumer products segment grew 5.6% YoY, registering revenue of Rs21.3bn. We expect modest revenue growth of 5% YoY each in FY13E and FY14E on the high base of FY12. Operating margins are also likely to remain stable at 12.5%/12.8% in FY13/14E, respectively, compared to FY12 margin of 12.3%. The industrial systems segment registered highest revenue growth among the three segments, at 21.6% YoY, resulting in revenue of Rs18.2bn, partly driven by incremental revenue from Emotron and QEI acquisition. However, operating margin fell 600bps YoY, from 17.6% in FY11 to 11.6% in FY12, partly due to pressure on margins in the HT/LT motors business and partly due to goodwill write-off in the case of Emotron and QEI. We expect the segment's revenue growth to moderate to 15.0%/12.5% YoY in FY13E/14E, respectively, as the high base effect of incremental revenue of the two acquisitions kicks in while we factor in a marginal recovery in operating margins to 12.5%/13.0% in FY13E/14E, respectively.

Exhibit 4: Segmental projections (consolidated)

Y/E March (Rsmn)	FY11	FY12	FY13E	FY14E
Power systems - domestic revenue	25,542	28,675	31,686	34,538
% growth	*1.7*	*12.3*	*10.5*	*9.0*
EBITDA	4,602	3,106	3,327	3,799
Operating margin (%)	*18.0*	*10.8*	*10.5*	*11.0*
Power systems - overseas subsidiaries' revenue	39,486	44,474	49,811	55,788
% growth	*6.9*	*12.6*	*12.0*	*12.0*
EBITDA	3,467	(712)	1,245	2,232
Operating margin (%)	*8.8*	*(1.6)*	*2.5*	*4.0*
(A) Total power systems revenue	65,028	73,149	81,497	90,326
% growth	*4.8*	*12.5*	*11.4*	*10.8*
EBITDA	8,069	2,394	4,572	6,031
Operating margin (%)	*12.4*	*3.3*	*5.6*	*6.7*
(B) Consumer products revenue	20,212	21,336	22,403	23,523
% growth	*25.4*	*5.6*	*5.0*	*5.0*
EBITDA	2,928	2,629	2,800	3,011
Operating margin (%)	*14.5*	*12.3*	*12.5*	*12.8*
(C) Industrial systems revenue	14,971	18,202	20,932	23,549
% growth	*18.9*	*21.6*	*15.0*	*12.5*
EBITDA	2,642	2,103	2,617	3,061
Operating margin (%)	*17.6*	*11.6*	*12.5*	*13.0*
Total revenue (A+B+C)	**100,211**	**112,687**	**124,832**	**137,398**
% growth	*10.4*	*12.4*	*10.8*	*10.1*
Total EBITDA	13,639	7,126	9,989	12,103
Operating margin (%)	*13.6*	*6.3*	*8.0*	*8.8*

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 5: Actuals versus our estimates, Bloomberg consensus estimates

4QFY12 (Rsmn)	Actuals	Our estimates	*Deviation (%)*	Bloomberg cons. est.	*Deviation (%)*
Revenue	30,774	30,726	*0.2*	32,471	*(5.2)*
EBITDA	2,132	2,556	*(16.6)*	2,641	*(19.3)*
PAT	1,003	1,457	*(31.2)*	1,635	*(38.7)*

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 6: Change in earnings estimates for FY13E

Y/E Mar (Rsmn)	Old	New	*Variation (%)*
Revenue	123,547	124,832	*1.0*
EBITDA	10,648	9,989	*(6.2)*
PAT	6,271	5,309	*(15.3)*

Source: Company, Nirmal Bang Institutional Equities Research

Rating track

Date	Rating	Market price (Rs)	Target price (Rs)
27 January 2012	Sell	142	118
31 January 2012	Sell	134	118
2 February 2012	Sell	144	108
13 April 2012	Sell	135	108

Disclaimer

Stock Ratings Absolute Returns

BUY > 15%

HOLD 0-15%

SELL < 0%

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