

ABB

ENGINEERING

HOLD

Target Price: Rs 1,400

Strong order inflow, outlook; in line Q1

ABB's Q1CY17 order inflow at Rs 23 bn increased 28% YoY, which was significantly better than estimate. Growth was broad-based: 5-fold rise in large orders (on a low base), short cycle base orders (up 17%), services (up 40%) and exports (up 120%). Order backlog at Rs 120 bn was up 54% YoY and 2% QoQ.

Revenue at Rs 22 bn (up 8% YoY) was in line with our/consensus expectations. **EBITDA margin** declined 80 bps YoY and missed estimate **impacted by expected credit loss (ECL) on transition to Ind AS** (our est. impact of ~200bps). ECL provisioning is expected to normalize over next few quarters. PAT at Rs 880 mn was slightly above our estimate on higher other income.

CMP : Rs 1,538
Potential Upside : -9%

MARKET DATA

No. of Shares : 212 mn
Free Float : 25%
Market Cap : Rs 326 bn
52-week High / Low : Rs 1,595 / Rs 950
Avg. Daily vol. (6mth) : 87,786 shares
Bloomberg Code : ABB IB Equity
Promoters Holding : 75%
FII / DII : 4% / 13%

Outlook positive: Management expects future growth to be driven by increased investments in domestic sectors such as T&D, renewables, railways, and Industrial automation, as well as rebound in exports.

Management optimism stems from increased investments in government sectors such as T&D, Railways and PSU Refiners. It also highlighted first signs of pick-up in private capex driven by Cement sector and continued traction in Renewables. However, it cautioned on pricing pressures in Renewables on falling tariffs which it plans to offset through higher volumes and cost rationalization.

Cut estimates, maintain TP; downgrade to HOLD on stock price appreciation: We cut our CY17 EPS to Rs 25 (Rs 26 earlier) and CY18 EPS to Rs 35 (Rs 40 earlier) to adjust for expected credit loss impact and increasing competitive pressure in renewables equipment market. However, we raise our target multiple to 40x (vs 35x earlier) to account for strong order inflow and improved outlook for T&D markets and private capex. Our TP stands at Rs 1,400 (40x CY18E).

Financial summary (Standalone)

Y/E December	CY15	CY16	CY17E	CY18E
Sales (Rs mn)	80,152	85,156	95,828	115,472
EBITDA (Rs mn)	7,192	7,466	9,108	11,728
Adj PAT (Rs mn)	3,066	3,567	5,239	7,414
Consensus EPS* (Rs)	-	-	23.6	29.3
EPS (Rs)	14.5	16.8	24.7	35.0
Change YoY (%)	33.9	16.4	46.8	41.5
P/E (x)	106.3	91.3	62.2	44.0
RoE (%)	10.5	11.3	15.2	19.1
EV/E (x)	45.3	42.8	34.8	26.8
DPS (Rs)	4.5	4.8	8.2	11.7

Source: *Consensus broker estimates, Company, Axis Capital

Key drivers

(Rs bn)	CY16	CY17E	CY18E
Order Inflow	125	101	117
Order Backlog	118	122	122
Margin (%)	8.6	9.4	10.0

Price performance



Exhibit 1: Results update(Rs mn)

	Quarter ended					12 months ended		
	Mar-17	Mar-16	% Chg	Dec-16	% Chg	CY17E	CY16	% Chg
Total Income	21,688	20,035	8.3	24,939	(13.0)	97,316	86,484	12.5
EBITDA	1,714	1,737	(1.3)	3,017	(43.2)	9,108	7,467	22.0
Other income	186	149	24.3	97	91.8	700	353	98.5
PBIDT	1,900	1,887	0.7	3,113	(39.0)	9,808	7,819	25.4
Depreciation	376	359	4.9	389	(3.2)	1,574	1,510	4.2
Interest	212	223	(5.0)	303	(30.1)	750	849	(11.7)
PBT	1,312	1,305	0.5	2,422	(45.8)	7,484	5,461	37.1
Tax	430	442	(2.7)	835	(48.5)	2,245	1,893	18.6
Adjusted PAT	882	863	2.2	1,587	(44.4)	5,239	3,568	46.8
No. of shares (mn)	212	212	-	212	-	212	212	-
EBITDA margins (%)	7.9	8.7	-	12.1	-	9.4	8.6	-
PBIDT margins (%)	8.8	9.4	-	12.5	-	10.1	9.0	-
EPS - annualized (Rs.)	16.6	16.3	2.2	29.9	(44.4)	24.7	16.8	46.8

Source: Company, Axis Capital

ABB's earnings have turned around, well ahead of peers – driven by renewables

- ◆ Earnings have posted CAGR of 25% over CY13-16, driven by closure of loss-making rural electrification jobs and exponential growth in renewables
- ◆ Renewables now constitute ~ 16% of sales and have grown 4-fold in the last 4 years. Within renewables, ABB addresses the most profitable value chain in both solar and wind. In Solar, ABB is market leader in Invertors (50% market share) and in wind it is leader in generators (>35% mkt share)
- ◆ Additionally, concentration on renewables helps in pushing its bread and butter products in T&D segment

New sectors like renewables, railways, industrial automation/ digitization, smart cities, etc. to take a lead over the conventional sectors in driving growth

- ◆ **Railways:** Now expanded the product portfolio, almost similar to Siemens. Product portfolio for locomotives include: turbochargers, transformers, convertors, etc. Besides this, ABB is present in signaling and has tied-up with GE and ALSTOM for component supplies to its diesel and electric locomotive space. Management commented that share of railways in the order inflow has increased to 5% (vs. 2% earlier)
- ◆ **Industrial automation** is usually first to turn around in the private capex cycle, as companies initially spend to cut energy and employeecosts. ABB is also one of the leading manufacturers of industrial robots
- ◆ Management highlighted **transformation in energy** (smart grids, micro grids, remote monitoring, renewable energy storage), **robotics and digitization** (Industry 4.0), **transportation and infrastructure** (railways, metro, EV charging, electrical propulsion) as the key areas of future growth for the company

Geared for growth acceleration by right-sizing itself

- ◆ As the company waits for volumes in conventional sector to revive, it has lowered raw material cost to 65% of revenue from 77% historically
- ◆ Strong focus on exports (~16% of revenue vs. 8% in CY10). Company expects **significant growth in exports as ABB India is acting as the feeder factory** and has started export of new product lines in CY16

Financial summary (Standalone)

Profit & loss (Rs mn)

Y/E December	CY15	CY16	CY17E	CY18E
Net sales	80,152	85,156	95,828	115,472
Other operating income	1,251	1,328	1,487	1,666
Total operating income	81,403	86,484	97,316	117,138
Cost of goods sold	(53,646)	(56,897)	(64,086)	(77,869)
Gross profit	27,757	29,587	33,230	39,270
<i>Gross margin (%)</i>	<i>34.6</i>	<i>34.7</i>	<i>34.7</i>	<i>34.0</i>
Total operating expenses	(20,565)	(22,121)	(24,122)	(27,541)
EBITDA	7,192	7,466	9,108	11,728
<i>EBITDA margin (%)</i>	<i>9.0</i>	<i>8.8</i>	<i>9.5</i>	<i>10.2</i>
Depreciation	(1,598)	(1,510)	(1,574)	(1,737)
EBIT	5,594	5,957	7,534	9,991
Net interest	(912)	(849)	(750)	(200)
Other income	130	353	700	800
Profit before tax	4,813	5,460	7,484	10,591
Total taxation	(1,747)	(1,893)	(2,245)	(3,177)
<i>Tax rate (%)</i>	<i>36.3</i>	<i>34.7</i>	<i>30.0</i>	<i>30.0</i>
Profit after tax	3,066	3,567	5,239	7,414
Minorities	-	-	-	-
Profit/ Loss associate co(s)	-	-	-	-
Adjusted net profit	3,066	3,567	5,239	7,414
<i>Adj. PAT margin (%)</i>	<i>3.8</i>	<i>4.2</i>	<i>5.5</i>	<i>6.4</i>
Net non-recurring items	(67)	195	-	-
Reported net profit	2,999	3,762	5,239	7,414

Balance sheet (Rs mn)

Y/E December	CY15	CY16	CY17E	CY18E
Paid-up capital	424	424	424	424
Reserves & surplus	29,662	32,404	35,903	40,831
Net worth	30,086	32,828	36,327	41,255
Borrowing	6,000	6,000	6,000	-
Other non-current liabilities	-	-	-	-
Total liabilities	36,086	38,828	42,327	41,255
Gross fixed assets	20,267	21,142	23,819	25,819
Less: Depreciation	(7,283)	(8,592)	(10,166)	(11,903)
Net fixed assets	12,984	12,549	13,653	13,916
Add: Capital WIP	443	678	-	-
Total fixed assets	13,427	13,227	13,653	13,916
Total Investment	164	163	163	163
Inventory	9,396	9,403	10,502	12,655
Debtors	33,909	30,633	32,537	37,650
Cash & bank	5,736	11,892	14,394	11,225
Loans & advances	7,003	7,114	7,876	9,491
Current liabilities	38,003	38,461	41,783	49,690
Net current assets	22,005	24,655	27,727	26,392
Other non-current assets	490	784	784	784
Total assets	36,086	38,828	42,327	41,255

Source: Company, Axis Capital

Cash flow (Rs mn)

Y/E December	CY15	CY16	CY17E	CY18E
Profit before tax	4,813	5,460	7,484	10,591
Depreciation & Amortisation	1,598	1,510	1,574	1,737
<i>Chg in working capital</i>	<i>(1,330)</i>	<i>3,506</i>	<i>(570)</i>	<i>(1,834)</i>
Cash flow from operations	4,178	9,627	6,993	7,517
<i>Capital expenditure</i>	<i>(672)</i>	<i>(1,109)</i>	<i>(2,000)</i>	<i>(2,000)</i>
Cash flow from investing	(1,583)	(1,958)	(2,750)	(2,200)
<i>Equity raised/ (repaid)</i>	-	-	-	-
<i>Debt raised/ (repaid)</i>	<i>2,289</i>	-	-	<i>(6,000)</i>
<i>Dividend paid</i>	<i>(944)</i>	<i>(1,020)</i>	<i>(1,740)</i>	<i>(2,486)</i>
Cash flow from financing	895	(1,020)	(1,740)	(8,486)
Net chg in cash	3,490	6,649	2,503	(3,169)

Key ratios

Y/E December	CY15	CY16	CY17E	CY18E
OPERATIONAL				
FDEPS (Rs)	14.5	16.8	24.7	35.0
CEPS (Rs)	21.7	24.9	32.1	43.2
DPS (Rs)	4.5	4.8	8.2	11.7
Dividend payout ratio (%)	31.5	27.1	33.2	33.5
GROWTH				
Net sales (%)	5.0	6.2	12.5	20.5
EBITDA (%)	28.6	3.8	22.0	28.8
Adj net profit (%)	33.9	16.4	46.8	41.5
FDEPS (%)	33.9	16.4	46.8	41.5
PERFORMANCE				
RoE (%)	10.5	11.3	15.2	19.1
RoCE (%)	16.9	16.8	20.3	25.8
EFFICIENCY				
Asset turnover (x)	2.7	3.0	3.5	4.0
Sales/ total assets (x)	1.1	1.1	1.2	1.3
Working capital/ sales (x)	0.2	0.2	0.1	0.1
Receivable days	154.4	131.3	123.9	119.0
Inventory days	46.2	43.4	43.5	43.8
Payable days	165.9	157.0	163.5	164.1
FINANCIAL STABILITY				
Total debt/ equity (x)	0.2	0.2	0.2	-
Net debt/ equity (x)	-	(0.2)	(0.2)	(0.3)
VALUATION				
PE (x)	106.3	91.3	62.2	44.0
EV/ EBITDA (x)	45.3	42.8	34.8	26.8
EV/ Net sales (x)	4.1	3.8	3.3	2.7
PB (x)	10.8	9.9	9.0	7.9
Dividend yield (%)	0.3	0.3	0.5	0.8
Free cash flow yield (%)	-	-	-	-

Source: Company, Axis Capital

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