

Q3 an aberration; outlook positive

ABB's Q3CY17 (Y/E Dec) revenue at Rs 19 bn (down 7% YoY) was ~15% lower than our/consensus expectations. Order inflow at Rs 19 bn (down 35% YoY; large railway order of Rs 10 bn year ago) was slightly lower than expectations. Management commented that **Q3 order inflow as well as execution was impacted by GST-related issues**; these issues have been resolved and, orders/sales should flow in Q4 and CY18. Management's **outlook commentary was positive** for most segments.

EBITDA margin increased 120 bps YoY and was broadly in line with our estimate. PAT at Rs 834 mn (up 18% YoY) was 6% below our estimate, as lower EBITDA was partially offset by higher other income. Order inflow was driven by strong growth in base orders, exports and services. Order backlog at Rs 121 bn was up 40% YoY.

CMP : Rs 1,400
Potential Upside : 21%

MARKET DATA

No. of Shares : 212 mn
Free Float : 25%
Market Cap : Rs 297 bn
52-week High / Low : Rs 1,619 / Rs 950
Avg. Daily vol. (6mth) : 121,606 shares
Bloomberg Code : ABB IB Equity
Promoters Holding : 75%
FII / DII : 3% / 14%

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's optimism stems from increased investments in government sectors such as T&D and Railways. There has been continued traction in renewables. However, management cautioned on pricing pressure in renewables on falling tariffs, which it plans to offset through higher volumes and cost rationalization.

First signs of corporate capex revival: Management highlighted that industry customers are looking to improve operational efficiencies and strengthen existing infrastructure leading to brownfield investments. This has led to some traction in oil and gas, chemicals, cement as well as metals and mining segments.

Trim CY17/CY18 estimates, TP; maintain BUY: We trim our CY17 EPS to Rs 21 (Rs 23 earlier) and CY18 EPS to Rs 34 (Rs 35 earlier) to adjust for Q3 results partially compensated by higher revenue/order inflow expected over the next few quarters. Our revised TP stands at Rs 1,690 (50x CY18E) vs. Rs 1,750 earlier.

Financial summary (Standalone)

Y/E December	CY15	CY16	CY17E	CY18E
Sales (Rs mn)	80,152	85,099	93,398	116,742
EBITDA (Rs mn)	7,192	6,945	7,509	11,719
Adj PAT (Rs mn)	3,066	3,566	4,365	7,162
Consensus EPS* (Rs)	-	-	22.6	28.8
EPS (Rs)	14.5	16.8	20.6	33.8
Change YoY (%)	33.9	16.3	22.4	64.1
P/E (x)	96.7	83.2	67.9	41.4
RoE (%)	10.5	11.3	12.8	19.0
EV/E (x)	41.2	41.8	38.3	24.4
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	102	115
Order Backlog	118	125	122
Margin (%)	8.0	7.9	9.9

Price performance



Exhibit 1: Results update (Rs mn)

	Quarter ended					12 months ended		
	Sep-17	Sep-16	% Chg	Jun-17	% Chg	CY17E	CY16	% Chg
Total Income	19,154	20,550	(6.8)	22,237	(13.9)	94,885	86,427	9.8
EBITDA	1,342	1,183	13.4	1,773	(24.3)	7,509	6,945	8.1
Other income	378	214	76.7	326	15.9	1,100	941	16.9
PBITD	1,719	1,396	23.1	2,099	(18.1)	8,609	7,886	9.2
Depreciation	389	405	(4.2)	383	1.4	1,574	1,510	4.2
Interest	152	196	(22.2)	231	(33.9)	800	919	(12.9)
PBT	1,178	795	48.2	1,485	(20.7)	6,235	5,458	14.2
Tax	344	284	21.2	435	(20.8)	1,871	1,892	(1.1)
Adjusted PAT	834	511	63.3	1,051	(20.6)	4,365	3,566	22.4
Extra ordinary income/ (exp.)	0	195	-	0	-	0	179	-
Reported PAT	834	706	18.2	1,051	(20.6)	4,365	3,745	16.6
No. of shares (mn)	212	212	-	212	-	212	212	-
EBITDA margins (%)	7.0	5.8	-	8.0	-	7.9	8.0	-
PBITD margins (%)	9.0	6.8	-	9.4	-	9.1	9.1	-
EPS - annualized (Rs.)	15.7	9.6	63.3	19.8	(20.6)	20.6	16.8	22.4

Source: Company, Axis Capital

Growth drivers in medium to long term

- ♦ **Exports (15% of CY16 revenue) and Railways (5% of CY16 revenue) – the next growth drivers**
 - **Direct exports to MEA and SAARC nations along with global growth (as outsourced manufacturer) to boost growth:** Earlier, ABB India's exports were to parent only, wherein ABB India was used as a 'global feeder factory' for select products. The parent changed its strategy in CY16 and ABB India now also exports directly to the Middle East, Africa (MEA) and SAARC region. Exports likely to grow in higher teens with robust margin
 - **Broadening of railways product portfolio and tie-up with GE and Alstom to drive exponential growth:** ABB India's mainstay product in Indian Railways (IR) has been only turbochargers so far. It is now looking to increase its share from IR through other products such as traction motors, traction electronics, traction transformers, electrical products, etc. Also, ABB India has tied up with Alstom Transportation and GE to supply parts for their new locomotive factories
- ♦ **New technologies – the long-term growth engines**
 - New technologies like smart and micro grids, remote monitoring, EV charging, renewable energy storage, robotics and digitization are key areas of future growth for the company. Globally, ABB has introduced fast chargers for electric buses and cars. These technologies are available with ABB India but size of market is negligible currently
- ♦ **Rise in T&D and automation capex – augurs well for ABB India**
 - Transmission capex is expected to grow 49% in the 13th plan (FY18-22E) to ~ Rs 2.6 trn (vs ~Rs 1.8 trn in 12th plan), with inter-state capex at ~Rs 1.5 trn (+30% YoY) and the balance as intra-state capex (+75% YoY)
 - Industrial automation is usually first to turnaround in private capex cycle, as companies initially spend to cut energy and employee costs. Significant potential exists considering size of automation market in India is just <USD 2 bn p.a. vis-à-vis total manufacturing capex of USD 350 bn p.a. Normally, automation is 5-10% of industrial capex

Profit & loss (Rs mn)

Y/E December	CY15	CY16	CY17E	CY18E
Net sales	80,152	85,099	93,398	116,742
Other operating income	1,251	1,328	1,487	1,666
Total operating income	81,403	86,427	94,885	118,408
Cost of goods sold	(53,646)	(56,897)	(62,969)	(78,439)
Gross profit	27,757	29,531	31,916	39,969
<i>Gross margin (%)</i>	<i>34.6</i>	<i>34.7</i>	<i>34.2</i>	<i>34.2</i>
Total operating expenses	(20,565)	(22,585)	(24,408)	(28,250)
EBITDA	7,192	6,945	7,509	11,719
<i>EBITDA margin (%)</i>	<i>9.0</i>	<i>8.2</i>	<i>8.0</i>	<i>10.0</i>
Depreciation	(1,598)	(1,510)	(1,574)	(1,737)
EBIT	5,594	5,436	5,935	9,982
Net interest	(912)	(919)	(800)	(350)
Other income	130	941	1,100	600
Profit before tax	4,813	5,458	6,235	10,232
Total taxation	(1,747)	(1,892)	(1,871)	(3,069)
<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	3,566	4,365	7,162
Minorities	-	-	-	-
Profit/ Loss associate co(s)	-	-	-	-
Adjusted net profit	3,066	3,566	4,365	7,162
<i>Adj. PAT margin (%)</i>	<i>3.8</i>	<i>4.2</i>	<i>4.7</i>	<i>6.1</i>
Net non-recurring items	(67)	179	-	-
Reported net profit	2,999	3,745	4,365	7,162

Balance sheet (Rs mn)

Y/E December	CY15	CY16	CY17E	CY18E
Paid-up capital	424	424	424	424
Reserves & surplus	29,662	32,404	35,029	39,705
Net worth	30,086	32,828	35,452	40,129
Borrowing	6,000	6,000	6,000	-
Other non-current liabilities	-	-	-	-
Total liabilities	36,086	38,828	41,452	40,129
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	10,235	12,794
Debtors	33,909	30,633	31,649	38,098
Cash & bank	5,736	11,892	14,587	9,956
Loans & advances	7,003	7,114	7,677	9,595
Current liabilities	38,003	38,461	41,389	50,293
Net current assets	22,005	24,655	26,853	25,267
Other non-current assets	490	784	784	784
Total assets	36,086	38,828	41,453	40,129

Source: Company, Axis Capital

Cash flow (Rs mn)

Y/E December	CY15	CY16	CY17E	CY18E
Profit before tax	4,813	5,458	6,235	10,232
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>497</i>	<i>(3,045)</i>
Cash flow from operations	4,178	9,679	7,235	6,205
<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)	(2,027)	(2,800)	(2,350)
<i>Equity raised/ (repaid)</i>	<i>-</i>	<i>-</i>	<i>-</i>	<i>-</i>
<i>Debt raised/ (repaid)</i>	<i>2,289</i>	<i>-</i>	<i>-</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	6,631	2,695	(4,631)

Key ratios

Y/E December	CY15	CY16	CY17E	CY18E
OPERATIONAL				
FDEPS (Rs)	14.5	16.8	20.6	33.8
CEPS (Rs)	21.7	24.8	28.0	42.0
DPS (Rs)	4.5	4.8	8.2	11.7
Dividend payout ratio (%)	31.5	27.2	39.9	34.7
GROWTH				
Net sales (%)	5.0	6.2	9.8	25.0
EBITDA (%)	28.6	(3.4)	8.1	56.1
Adj net profit (%)	33.9	16.3	22.4	64.1
FDEPS (%)	33.9	16.3	22.4	64.1
PERFORMANCE				
RoE (%)	10.5	11.3	12.8	19.0
RoCE (%)	16.9	17.0	17.5	25.9
EFFICIENCY				
Asset turnover (x)	2.7	3.0	3.5	4.1
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	131.4	123.7	119.1
Inventory days	46.2	43.2	42.8	43.8
Payable days	165.9	156.1	162.4	164.1
FINANCIAL STABILITY				
Total debt/ equity (x)	0.2	0.2	0.2	-
Net debt/ equity (x)	-	(0.2)	(0.3)	(0.3)
VALUATION				
PE (x)	96.7	83.2	67.9	41.4
EV/ EBITDA (x)	41.2	41.8	38.3	24.4
EV/ Net sales (x)	3.7	3.4	3.1	2.5
PB (x)	9.9	9.0	8.4	7.4
Dividend yield (%)	0.3	0.3	0.6	0.8
Free cash flow yield (%)	-	-	-	-

Source: Company, Axis Capital

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