16 May 2019

Update | Sector: Capital Goods

Siemens

BSE SENSEX	S&P CNX
37,393	11,257

SIEMENS

Stock Info

Bloomberg	SIEM IN
Equity Shares (m)	356
M.Cap.(INRb)/(USDb)	402.2 / 5.7
52-Week Range (INR)	1199 / 841
1, 6, 12 Rel. Per (%)	0/10/1
12M Avg Val (INR M)	494
Free float (%)	25.0

Financials Snapshot (INR b)

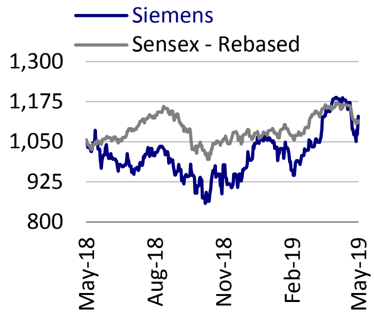
Y/E Sep	2019E	2020E	2021E
Net Sales	139.5	150.9	169.6
EBITDA	16.3	16.9	19.6
PAT	11.6	12.1	14.1
EPS (INR)	32.5	34.0	39.7
Gr. (%)	29.5	4.6	16.6
BV/Sh (INR)	255.9	281.7	311.9
RoE (%)	13.3	12.7	13.4
RoCE (%)	18.7	17.7	18.7
P/E (x)	34.5	32.9	28.2
P/BV (x)	4.4	4.0	3.6

Shareholding pattern (%)

As On	Mar-19	Dec-18	Mar-18
Promoter	75.0	75.0	75.0
DII	11.4	11.2	9.5
FII	2.3	2.7	4.8
Others	11.4	11.1	10.7

FII Includes depository receipts

Stock Performance (1-year)



CMP: INR1,120 TP: INR1,290 (+15%) Upgrade to Buy

Ready to reap the rewards

A play on digitalization and industry automation

- **Multiple growth levers across industry segments:** The strong focus on products/services has helped Siemens (SIEM) to mitigate the slowdown in industrial capex, as it has been able to capitalize on opex-related spending. We expect the trend to continue, driving strong growth for its products business. Any revival in capex spending can further strengthen its revenue trajectory (not a base-case scenario for us and consensus).
- **Revenue CAGR (excl. Energy Management) estimated at 17% over FY18-21 (year ending September):** We expect overall revenue growth to be driven by Building Technologies, Mobility, Digital Factory and Process Industries. However, as the HVDC order approaches completion, the Energy Management division (~40% of revenue) growth will likely come under pressure. Thus, we expect overall revenue CAGR of ~10% over FY18-21, but growth to pick up thereafter.
- **Margin expansion – a key driver of earnings:** We expect the EBIT margin to expand from 8.8% in FY18 to 10.1% in FY21, as the share of products/services business increases further. We note that over the past five years, SIEM has steadily expanded its EBIT margin from 4.7% in FY14 to 8.8% in FY18. This is attributable to (a) the rising share of products/services business, (b) the completion of early loss-making/low-margin projects and (c) export incentives in services business in Power & Gas and Energy Management segments. A comparison of the segmental margins with the parent company suggests a further scope of margin expansion in the products/services business.
- **Second-quarter earnings exceed expectations driven by better margins:** Revenue grew 8% YoY to INR35.5b, while EBITDA increased 32% YoY with margin expansion to 12% (2QFY18: 9.8%). Adj. PAT came in at INR3.0b (+35% YoY), 16% ahead of our estimate. The beat was largely driven by the margins surprise in the Power & Gas, Mobility and Energy Management segments.
- **Valuations provide comfort:** SIEM trades at FY19E/20E P/E of 34.5x/32.9x versus its long-term average trading multiple of 49x. The underperformance over the past one year can be ascribed to (a) MSCI exclusion, (b) the decision to sell-off the Mobility division to parent and (c) de-rating of the overall capital goods sector amidst election uncertainty. The current valuation provides comfort, given the scope of an improvement in the operating performance and the likely gradual recovery in capex spending. **We upgrade SIEM to Buy with a target price of INR1,290 (35x Mar'21E EPS).**
- **Key risks – (a) Divestment of Gas & Power segment** – Siemens AG has announced the demerger of its Gas & Power segment from the existing listed Siemens AG entity. The same may be implemented for Siemens India entity as well. The process followed for the demerger (slump sale, demerger, re-listing, etc.) and the fair and transparent valuation are critical for the stock performance. **(b) Plans for Mobility remain unclear** – Management shared that the global board is yet to decide on the way forward for the Mobility business, as the earlier JV transaction with Alstom did not conclude.

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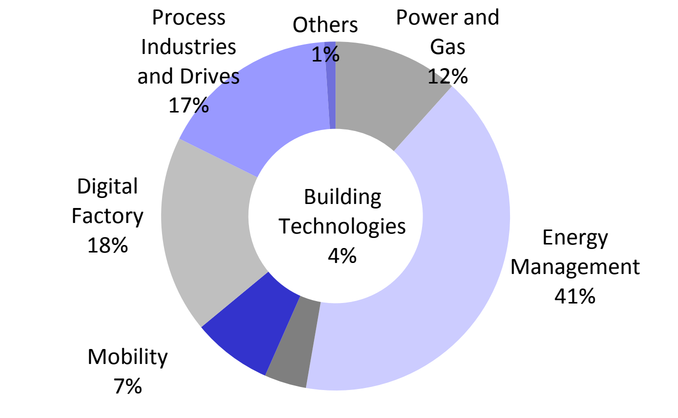
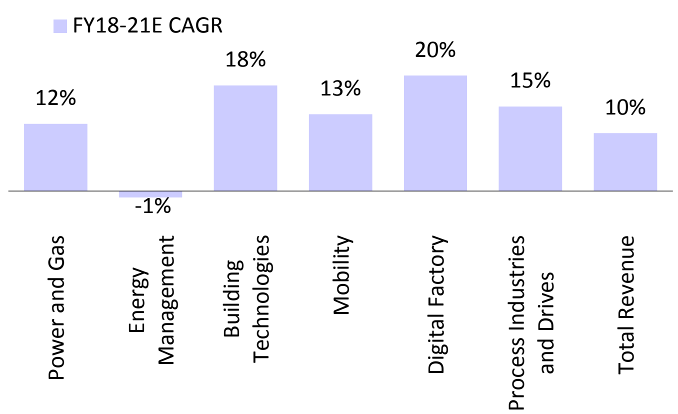
Story in charts

Exhibit 1: Revenue breakdown (FY18)



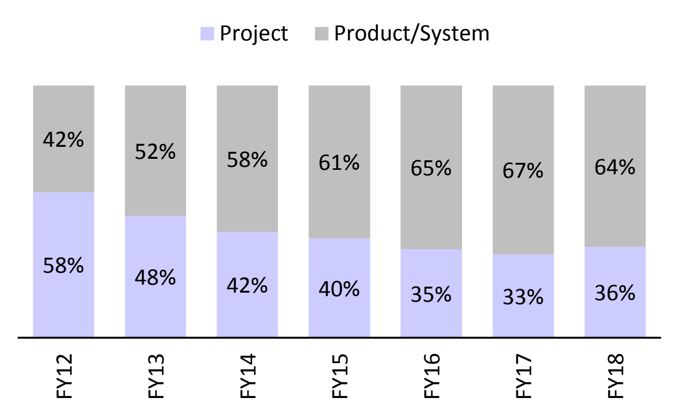
Source: Company, MOFSL

Exhibit 2: Segment-wise growth assumption (FY18-21E)



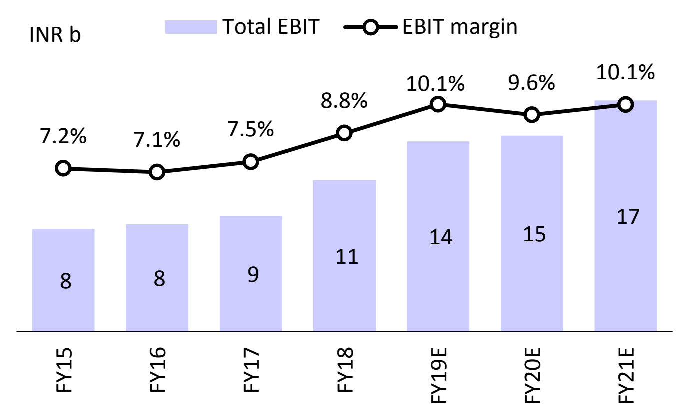
Source: Company, MOFSL

Exhibit 3: Share of product business has been on an uptrend



Source: Company, MOFSL

Exhibit 4: Margin improvement has led to earnings growth, despite muted revenue growth over past five years



Source: Company, MOFSL

Exhibit 5: Siemens trades at a discount to its long-term trading average

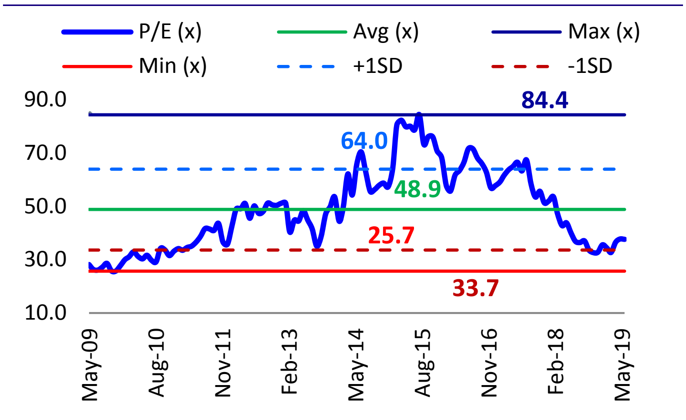
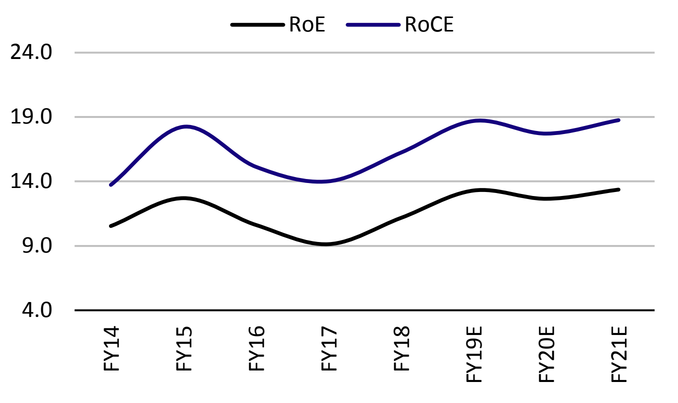


Exhibit 6: RoEs and RoCEs to improve going forward



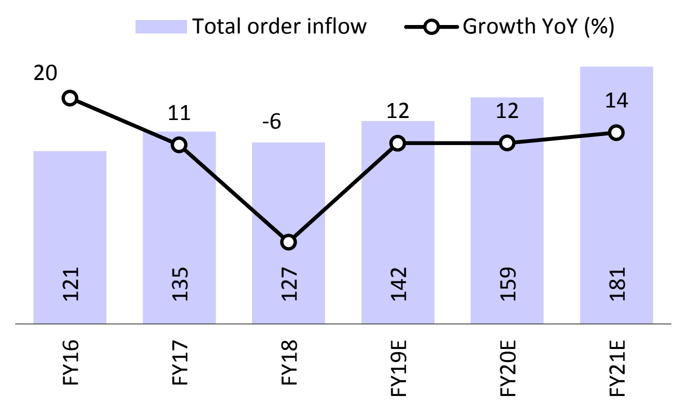
Strong offerings towards automation and digitalization

Siemens' products cater to wide industry segments, making it a beneficiary of capex revival and digitalization trend

Margin expansion to drive earnings growth

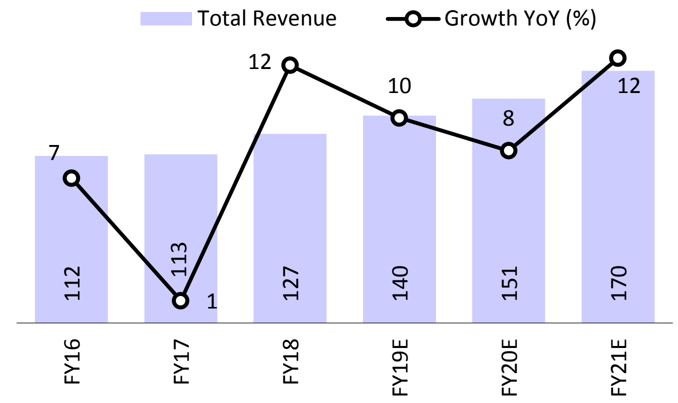
- **Revenue CAGR (excl. Energy Management) estimated at 17% over FY18-21…:** We expect overall revenue growth to be driven by Building Technologies, Mobility, Digital Factory and Process Industries. However, as the HVDC order approaches completion, the Energy Management division (~40% of revenue) growth will likely come under pressure. Thus, we expect overall revenue CAGR of ~10% over FY18-21.

Exhibit 7: Order inflow to grow in double digits (INR b)



Source: MOFSL, Company

Exhibit 8: Revenue growth driven by HVDC order (INR b)



Source: MOFSL, Company

- **…however, margin expansion is key driver of earnings:** We expect the EBIT margin to expand from 8.8% in FY18 to 10.1% in FY21, as the share of products/services business increases further. We note that over the past five years, SIEM has steadily expanded its EBIT margin from 4.7% in FY14 to 8.8% in FY18. This is attributable to (a) the rising share of products/services business, (b) the completion of early loss-making/low-margin projects and (c) export incentives in services business in Power & Gas and Energy Management segments. A comparison of the segmental margins with the parent company suggests a further scope of margin expansion in the products/services business.

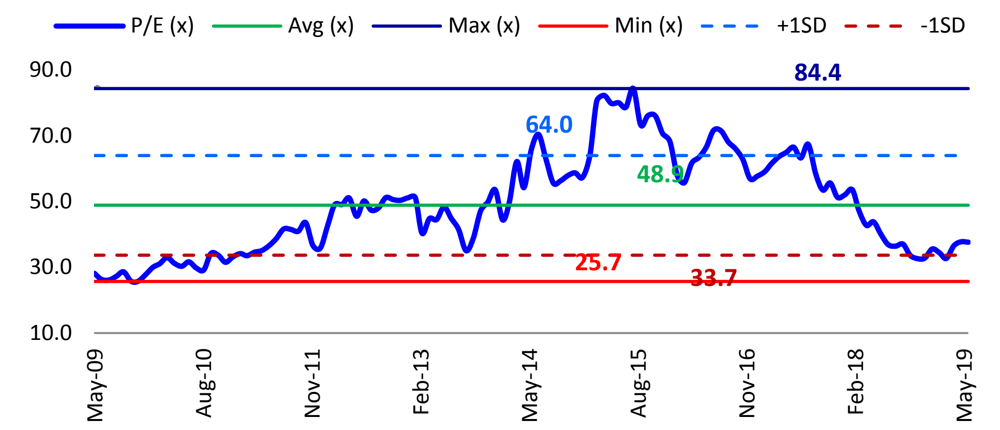
Exhibit 9: Ample scope of margin improvement (%)

Segment	FY18	FY21E	Global margin	Comment
Power and Gas	15.9%	17.0%	11-15%	❖ In-line
Energy Management	7.7%	9.0%	7-10%	❖ In-line
Building Technologies	8.6%	10.0%	8-11%	❖ Scope for margin improvement
Mobility	10.0%	10.0%	6-9%	❖ In-line
Digital Factory	8.1%	12.0%	14-20%	❖ Scope for margin improvement
Process Industries and Drives	3.5%	4.0%	8-12%	❖ Scope for margin improvement

Source: MOFSL, Company

- **Valuations provide comfort as SIEM trades at a discount to its historical trading average and to its peers:** SIEM trades at FY19E/20E P/E of 34.5x/32.9x versus its long-term average trading multiple of 49x. The underperformance over the past one year can be ascribed to (a) MSCI exclusion, (b) the decision to sell-off the Mobility division to parent and (c) de-rating of the overall capital goods sector amidst election uncertainty. The current valuation provides comfort, given the scope of an improvement in the operating performance and the likely gradual recovery in capex spending. **We upgrade SIEM to Buy with a target price of INR1,290 (35x Mar'21E EPS).**

Exhibit 10: P/E multiple at a discount to historical average



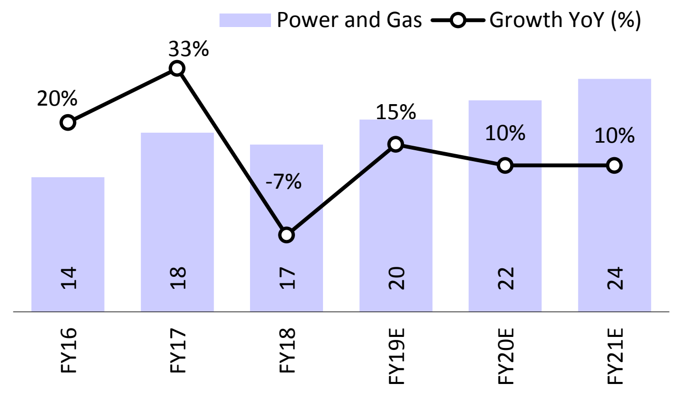
Source: MOFSL, Company

Segment growth outlook – automation and digitalization theme

Power & Gas – higher service content aiding margins

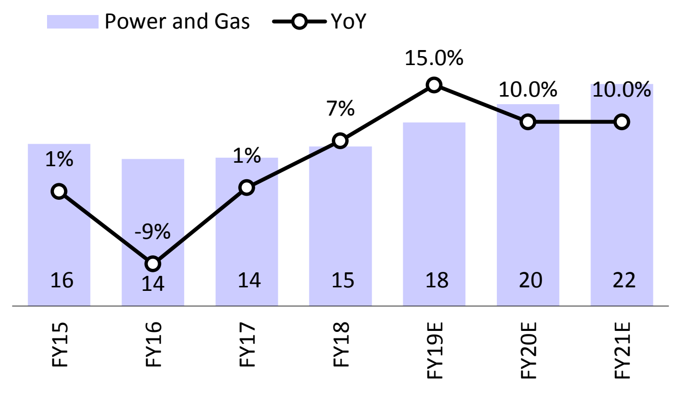
- **Offerings:** Power & Gas division offers a broad spectrum of products and solutions for reliable, efficient and clean power for (a) generation of electricity from fossil fuels and (b) reliable generation of power for oil & gas and industrial applications.
- **Key customers:** Utilities, independent power producers, engineering, procurement and construction (EPC) companies, and businesses in industries such as oil and gas, sugar and cement.
- **Growth drivers:** (a) Growing demand for turbines in CPPs (chemicals, sugar, paper) and waste heat recovery (cement). (b) Higher demand for services business on account of higher maintenance required for ageing power plants. (c) Grid stabilization as the share of renewables rises.
- **We expect Power & Gas revenue CAGR of 12% over FY18-21:** We expect the Power & Gas segment to deliver a 12% CAGR in revenue over FY18-21. We do not factor in large scale orders in this segment, given the low plant load factors (PLFs) for the thermal plants.

Exhibit 11: Order inflow to be supported by demand of CPP and waste heat recovery system order finalization (INR b)



Source: MOFSL, Company

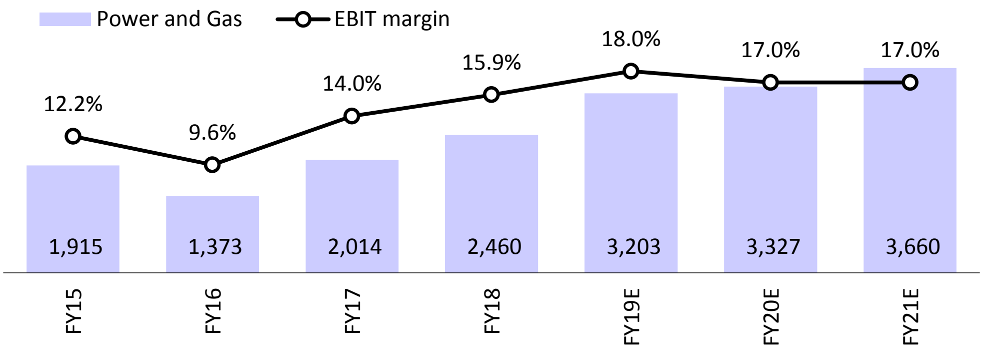
Exhibit 12: Expect revenue CAGR of 12% over FY18-21 (INRb)



Source: MOFSL, Company

- **Margins to expand as share of products/services rises:** The Power & Gas margin expanded to 15.9% in FY18 from 7% in FY14 due to (a) the completion of low-margin/loss-making legacy projects, (b) the rising share of services content and (c) export incentives on services. For the current year, the segment margins have been boosted by higher forex gains. However, on a steady basis, we project an EBIT margin of 17% for the business in FY20/21.

Exhibit 13: EBIT margins of the business to remain stable (INR m)

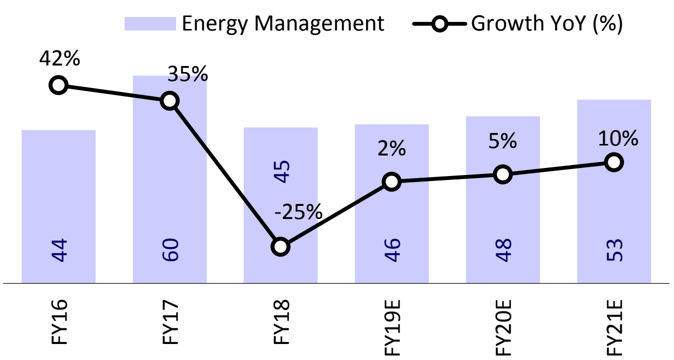


Source: MOFSL, Company

Energy Management – muted growth outlook as HVDC orders approach completion

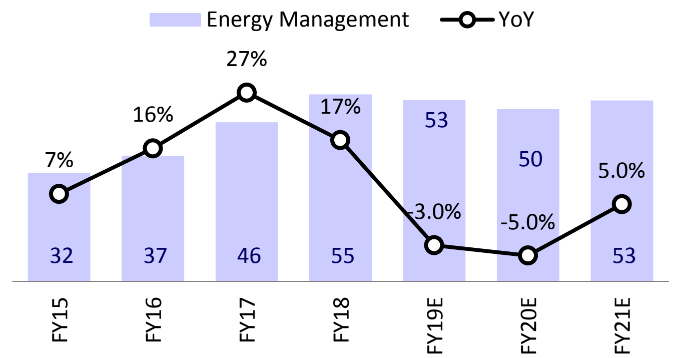
- **Offerings:** This division caters to the power transmission and distribution segment, as well as management and control of electrical energy. Its electrification products range from low-voltage products for domestic electrification to electrification of medium voltage distribution and ultra-high voltage transmission grids.
- **Key customers:** Central and state utilities, private transmission and distribution system operators.
- **Growth drivers:** State capex toward power T&D to offset slowdown in Power Grid capex.
- **Energy Management revenue to be muted over FY18-21:** We expect the segmental revenue to be flattish over the next three years as the under-execution HVDC order approaches completion by mid-FY20. The HVDC order is ~65% completed, and may support revenue for the current year. However, the order inflow outlook continues to be tepid amidst a slowdown in Power Grid capex and working capital risk from state capex, requiring selective order intakes.

Exhibit 14: We expect tepid growth in Energy Management segment until FY20 (INR b)



Source: MOFSL, Company

Exhibit 15: Energy management to witness muted revenue growth given completion of HVDC order (INR b)

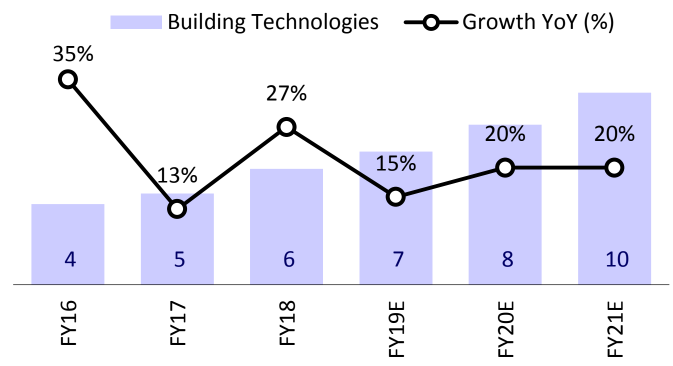


Source: MOFSL, Company

Building Technologies – airports, data centers provide strong growth opportunities

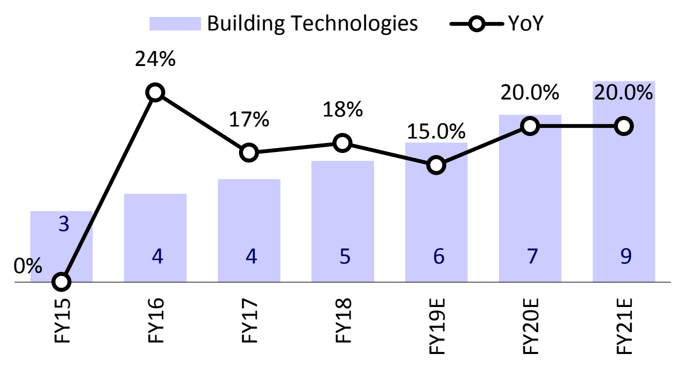
- **Offerings:** Building Technologies provides solutions for safe, secure, energy efficient and eco-friendly buildings and infrastructures. It also has solutions for applications such as fire safety, security, building automation, heating, ventilation, air conditioning and energy management.
- **Key customers:** Commercial spaces, life sciences, data centers, IT/ITES and hospitality sectors.
- **Growth drivers:** Increase in private investment and government-led infrastructure projects, continued growth in commercial spaces, data centers and IT/ITES. Opportunities exist across hotels, airports and industries as well.
- **We expect robust revenue CAGR of 18% over FY18-21:** Over the past three years, the segment has delivered strong revenue CAGR of 20%. We expect the growth momentum to continue, with opportunities emerging across hospitality, airports and commercial spaces. Data centers can potentially be a huge market and not factored in our base-case growth.

Exhibit 16: Order inflow growth to remain healthy (INR b)



Source: MOFSL, Company

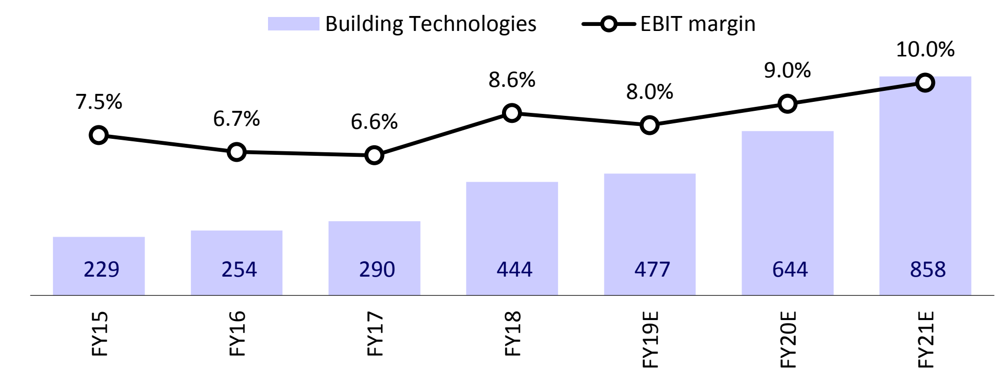
Exhibit 17: Robust growth supported by strong demand in data center, hospitality and commercial spaces (INR b)



Source: MOFSL, Company

- **Scope for margin expansion as scale increases:** Building segment has scope for margin expansion, led by product & services content. We expect the margins to expand from 8.6% in FY18 to 10% in FY21.

Exhibit 18: Margins to improve supported by product % services content (INR m)

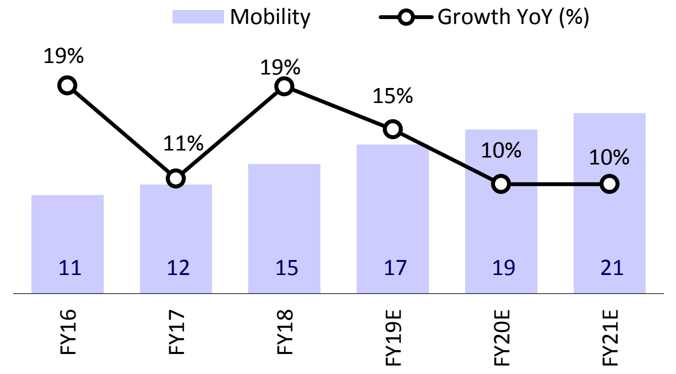


Source: MOFSL, Company

Mobility – riding on railway and metro projects capex

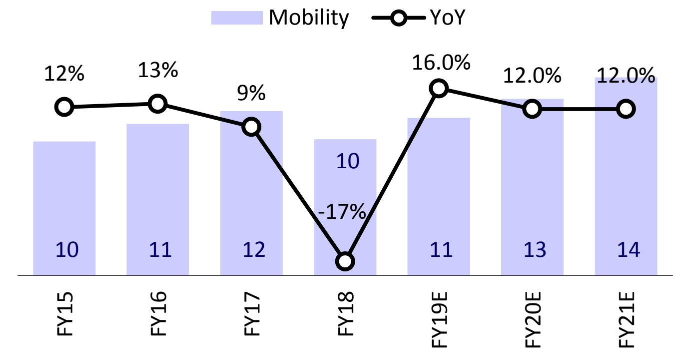
- **Offerings:** Mobility division provides solutions for mainline and metro Railways covering the entire gamut of rail infrastructure comprising signaling and electrification and rolling stock components and systems.
- **Key customers** – Indian railways, metro projects.
- **Growth drivers** – (a) Increasing railway capex. (b) Rising metro projects as new cities upgrade their urban transportation system.
- We expect Mobility revenue CAGR of 13% over FY18-21. The segment witnessed order inflow growth of 19% in FY18. We expect railway capex to drive overall capex spending in the country. Thus, we forecast 13% CAGR in order inflows/revenue in this segment.

Exhibit 19: Order inflow to be driven by metros and railways capex (INR b)



Source: MOFSL, Company

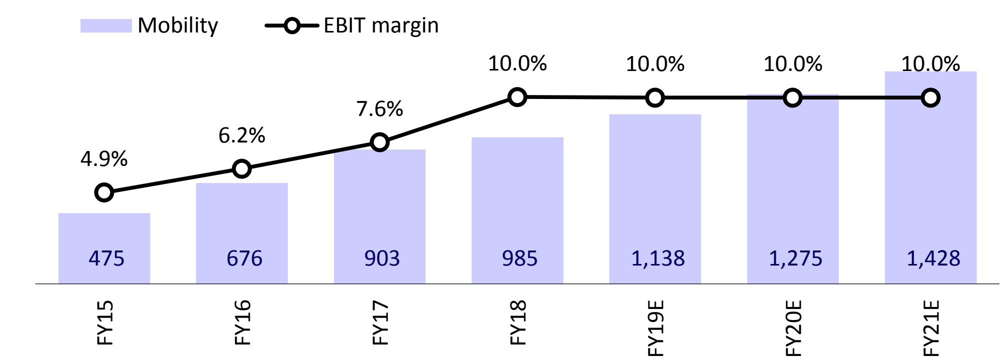
Exhibit 20: Mobility revenue growth to be supported by railways spend and metros (INR b)



Source: MOFSL, Company

- **Margins to remain stable:** We expect margins to remain stable at 10%, same as FY18.

Exhibit 21: Margins to remain stable (INR m)

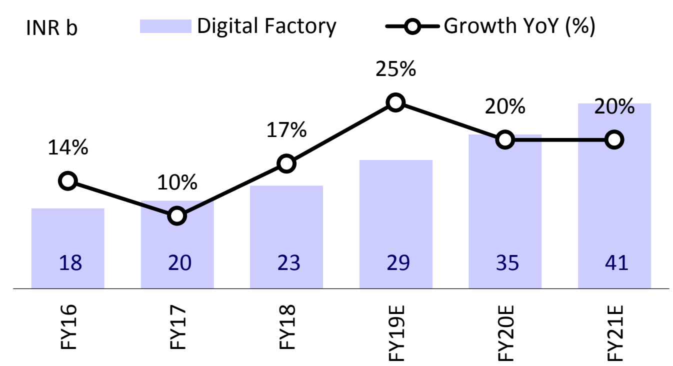


Source: MOFSL, Company

Digital factory – adoption of digitalization picking up

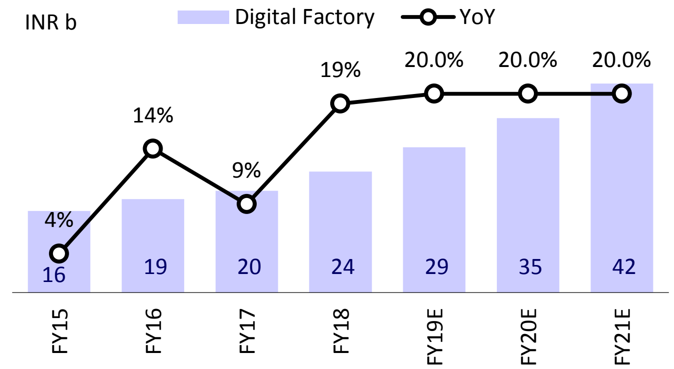
- **Offerings:** Digital Factory offers a portfolio of industrial software and automation technologies for optimizing the manufacturing value chain, covering product design, production planning, engineering and execution, and aftersales services. The division's 'Digital Enterprise Suite' offers flexibility and efficiency to various discrete industries, general engineering segments and OEMs engaged in machine tools, printing, packaging and electrical panel manufacturing.
- **Key customers:** Automotive, tyre industry, food and beverages, etc.
- **Growth drivers:** Manufacturing-led growth and greater adoption of digitalization and Industry 4.0 are expected to boost demand for factory automation, software and data analytics.
- **We expect Digital Factory revenue CAGR of 20% over FY18-21:** Adoption of digitalization and the increasing customer focus on cost productivity should drive growth for the segment. We expect revenue CAGR of 20% for the segment over the next three years.

Exhibit 22: Digital factory order inflow to be supported by productivity improvement drive in industries segment



Source: MOFSL, Company

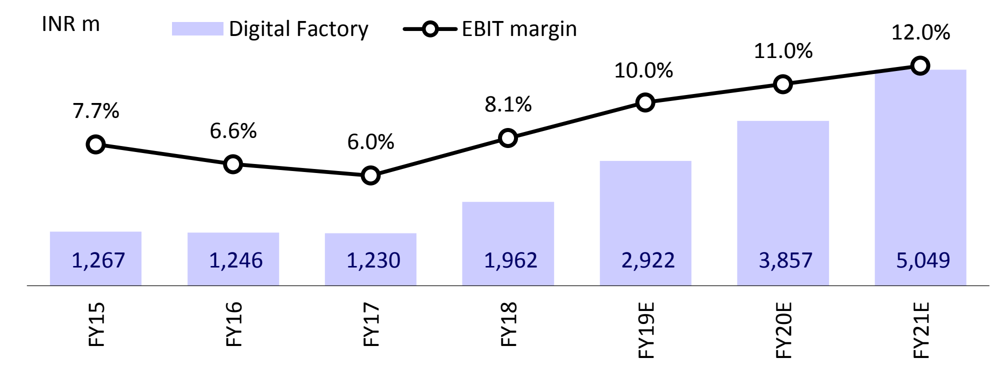
Exhibit 23: Revenue growth to be healthy at 20% CAGR



Source: MOFSL, Company

- **Huge scope of margin improvement**- Digital factory EBIT margin expanded to 8.1% in FY18 from 5.4% in FY14. In 1HFY19, it has further expanded to 9.8%. We expect margins to expand to 12% by FY21, still below strong margins of 14-20% enjoyed by parent company in global markets.

Exhibit 24: Digital factory margins to improve by 200bp over FY19-21

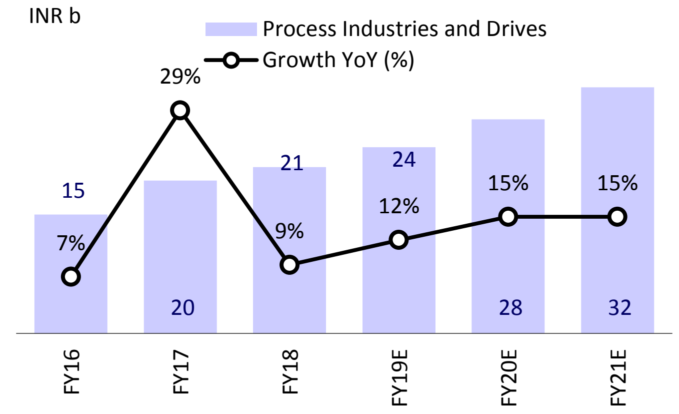


Source: MOFSL, Company

Process Industries – strong growth but subdued margins due to competitive environment

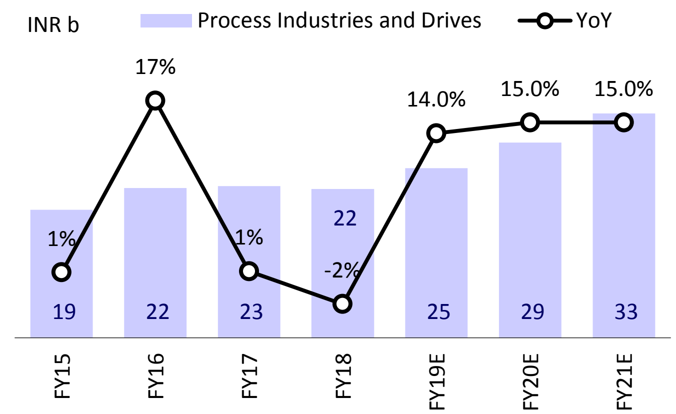
- **Offerings:** Process Industries and Drives division offers a comprehensive portfolio for industrial application and solutions in the field of automation and drives for process industries.
- **Key customers:** Chemical, pharmaceuticals, food and beverages, water and waste water, cement, mining, oil & gas, paper and marine companies.
- **Growth drivers:** Adoption of digitalization.
- **We expect revenue CAGR of 15% over FY18-21:** We forecast revenue CAGR of 15% in this segment over the next three years.

Exhibit 25: Process Industries and Drives growth at 13%



Source: MOFSL, Company

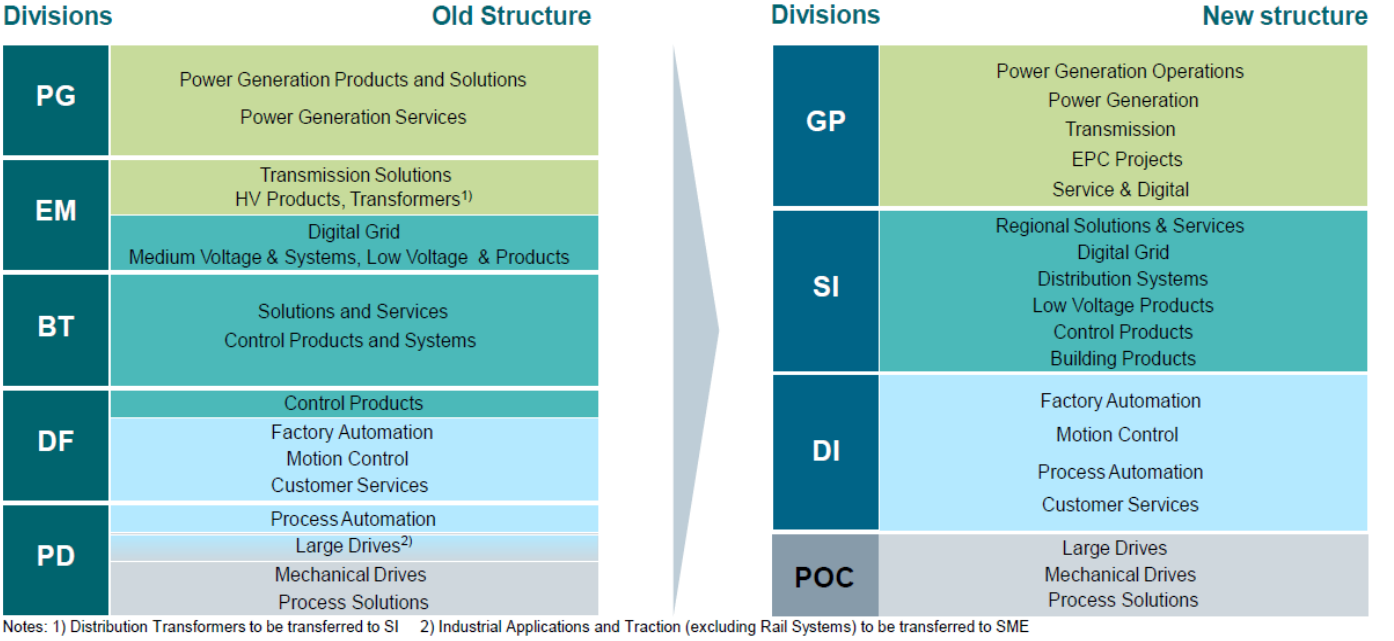
Exhibit 26: Expect revenue CAGR of 15% over FY18-21



Source: MOFSL, Company

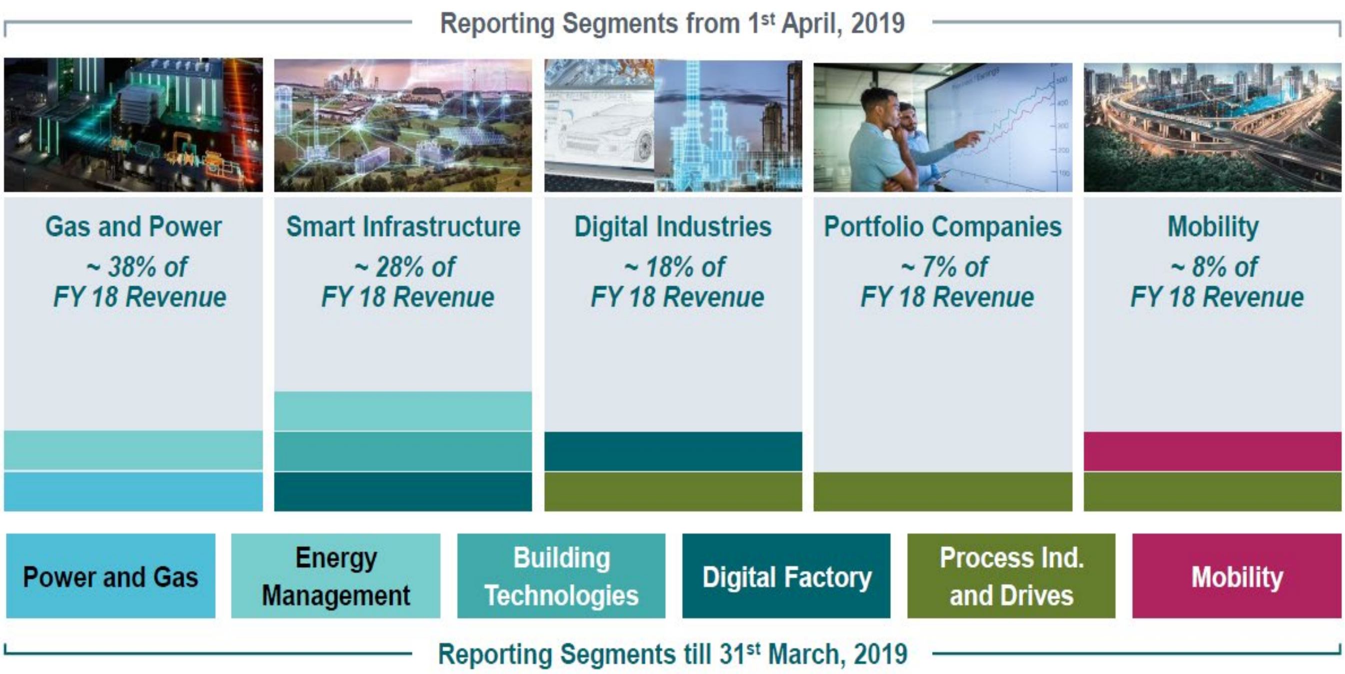
Overview of new segmentation from 3QFY19

Exhibit 27: Segmental regrouping of the existing business



Source: MOFSL, Company

Exhibit 28: Revenue breakup of Siemens India in new segments (FY18)



Source: MOFSL, Company

Exhibit 29: Margin guidance by Siemens AG for new segments

New segments	Siemens AG margin guidance
Digital industries	17-23%
Smart infrastructure	10-15%
Gas and Power	8-12%
Mobility	9-12%

Source: MOFSL, Company

2QFY19 earnings above expectation

- Sales of INR35.5b (+8% YoY) were in line with our estimate of INR36b, led by strong growth in Digital Factory (+14% YoY), Power & Gas (+22% YoY), and Mobility segment (+63% YoY, supported by weak base of a 43% decline in 2QFY18). Power & Gas growth was driven by captive demand and small turbines.
- EBITDA was at INR4.3b (+32% YoY), with the margin coming in at 12.0% (+220bp YoY) v/s our estimate of 10.3%. Margins were positively impacted by forex gain of INR189m.
- EBIT margin expanded in Power & Gas (16.3%, +430bp – helped by a forex gain of INR109m), Energy Management (10.7%, +230bp) and Mobility (18%, +1050bp). Mobility segment margin expansion was on account of achievement of milestones in certain projects and operating leverage.
- Other income was at INR830m v/s our estimate of INR700m.
- Tax rate was at 35.3% v/s our estimate of 34.6%.
- PAT came in at INR2.8b (+28% YoY), ahead of our estimate of INR2.6b.
- Orders were at INR36.5b (+24% YoY) and order book at INR130b, with an OB/rev ratio of 1.1x.

Exhibit 30: Quarterly Performance (Standalone) **(INR Million)**

Y/E September	FY18				FY19				FY18	FY19	MOFSLe	Var
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q			2Q	%
Total Revenues	**24,295**	**32,834**	**30,730**	**39,392**	**28,071**	**35,496**	**32,429**	**43,540**	**1,27,251**	**1,39,536**	**36,045**	**-1.5**
Change (%)	5.9	12.1	15.9	25.4	15.5	8.1	5.5	10.5	17.7	9.7	9.8	
EBITDA	**2,724**	**3,228**	**3,023**	**4,186**	**3,661**	**4,257**	**3,569**	**4,834**	**13,161**	**16,321**	**3,764**	**13.1**
Change (%)	16.6	15.9	33.4	32.0	34.4	31.9	18.1	15.5	25.2	24.0	16.6	
As % of Revenues	11.2	9.8	9.8	10.6	13.0	12.0	11.0	11.1	10.3	11.7	10.3	
Depreciation	470	490	500	507	532	571	570	575	1,967	2,248	550	
Interest	17	11	4	51	2	24	20	34	82	80	11	
Other Income	705	639	692	764	877	830	750	824	2,800	3,281	700	
Extra-ordinary Items	0	0	0	0	-596	-157	0	0	0	-753	0	
PBT	**2,942**	**3,366**	**3,211**	**4,392**	**3,408**	**4,335**	**3,729**	**5,049**	**13,912**	**16,521**	**3,903**	**11.1**
Tax	1,037	1,169	1,167	1,600	1,128	1,532	1,268	1,773	4,973	5,701	1,350	
Effective Tax Rate (%)	35.2	34.7	36.3	36.4	33.1	35.3	34.0	35.1	35.7	34.5	34.6	
Reported PAT	**1,905**	**2,197**	**2,044**	**2,792**	**2,280**	**2,803**	**2,461**	**3,276**	**8,939**	**10,821**	**2,553**	**9.8**
Adjusted PAT	**1,905**	**2,197**	**2,044**	**2,792**	**2,876**	**2,960**	**2,461**	**3,276**	**8,939**	**11,574**	**2,553**	**15.9**
Change (%)	18.6	22.6	25.5	39.1	51.0	34.7	20.4	17.4	27.1	29.5	16.2	

Exhibit 31: Quarterly Performance (INR m)

	FY18				FY19			
Revenues (INR m)	**1Q**	**2Q**	**3Q**	**4Q**	**1Q**	**2Q**	**3Q**	**4Q**
Power & Gas	2,982	3,699	3,439	5,354	3,509	4,513	3,783	5,989
Energy Management	10,365	14,842	13,136	16,284	10,518	13,711	12,216	16,544
Building Technologies	890	1,245	1,251	1,796	1,081	1,330	1,439	2,110
Mobility	2,051	2,079	2,132	3,552	1,745	3,380	2,345	3,914
Digital Factory	5,046	6,204	6,290	6,807	6,842	7,060	7,234	8,082
Process Industries & Drives	4,013	5,670	5,484	6,959	5,257	5,884	6,142	7,941
Others	270	445	359	312	226	340	359	322
Gross Sales	**25,617**	**34,184**	**32,091**	**41,064**	**29,178**	**36,218**	**33,518**	**44,901**
Less: Inter Segment Revenues	1,322	1,350	1,361	1,672	1,107	722	1,089	1,362
Net Sales	**24,295**	**32,834**	**30,730**	**39,392**	**28,071**	**35,496**	**32,429**	**43,540**
Revenue Growth (%)								
Power & Gas	-14%	-8%	13%	38%	18%	22%	10%	12%
Energy Management	21%	20%	8%	21%	1%	-8%	-7%	2%
Building Technologies	-4%	8%	12%	50%	21%	7%	15%	17%
Mobility	-30%	-43%	-21%	39%	-15%	63%	10%	10%
Digital Factory	14%	19%	33%	12%	36%	14%	15%	19%
Process Industries & Drives	-27%	-2%	0%	20%	31%	4%	12%	14%
Others	-11%	36%	-1%	-6%	-16%	-24%	0%	3%
Net Sales	**1.4%**	**7.6%**	**11.4%**	**25.4%**	**16%**	**8%**	**6%**	**11%**
EBIT Margin %								
Power & Gas	18.1	11.9	19.5	15.1	26.5	16.3	15.0	16.2
Energy Management	10.6	8.4	5.7	6.8	13.6	10.7	10.0	10.3
Building Technologies	7.3	8.9	8.5	9.0	8.0	5.1	9.0	9.1
Mobility	5.6	7.5	7.6	15.6	(8.5)	18.0	10.0	11.3
Digital Factory	8.1	7.0	9.8	7.4	9.7	9.9	10.0	10.3
Process Industries & Drives	(1.0)	4.4	2.2	6.3	3.1	1.7	2.0	1.5
Others	25.9	23.4	27.0	32.4	(0.9)	2.4	0.0	(1.9)
Total EBIT	**8.8**	**8.0**	**7.9**	**9.0**	**10.7**	**10.2**	**8.9**	**9.5**

Key takeaways from analyst meeting

Outlook on capex activity

- Muted capex in general industry – focus is on improving efficiencies.
- Renewables continue to lead bulk of power generation capacity addition; however, conventional power is still not picking up.
- Indian Railways achieved highest-ever capex (maximum spent on electrification; signaling and safety yet to pick up) and metro rail execution is on track.
- April and May have seen slowdown across verticals, mainly on account of elections.
- Private capex still 3-4 months away.
- Enquiry levels high and conversion low.

Emphasis on energy efficiency, automation and digitalization across sectors

Power

- Growing demand for turbines in CPPs (chemicals, sugar, paper) and waste heat recovery (cement).
- Higher maintenance required for ageing power plants – increased requirement for services.

Infra

- SEBs drive ordering in T&D; investments on grid quality and stability likely over the medium term.

- Metro rail execution on track – 140 km commissioned in 2018-19.
- Strong demand for smart infrastructure in data centers, hospitals, commercial offices and airports.

Industry

- Capital expenditure growing in certain segments (F&B, chemicals, water).
- Interest in digitalization for operational flexibility and enhanced efficiency continues to grow.

Order inflow stands healthy and order book at six-year high

- Base order inflow grew by 16.2% YoY in 2QFY19; overall order inflow increased 24% YoY to INR36.3b.
- Order backlog stood at INR130.2b providing visibility of 1.1x its TTM sales.

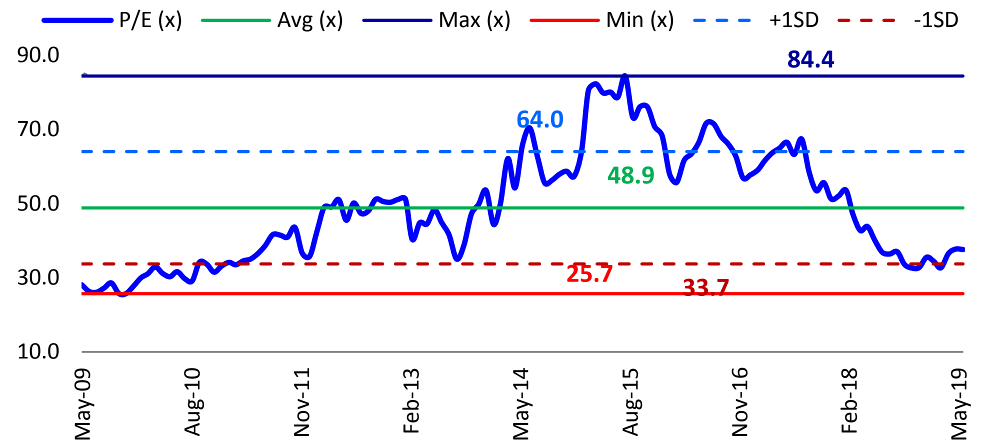
Execution remains strong across segments

- **Power & Gas:** Sales (+18% YoY) supported by the small steam turbine business across the cement, chemicals and sugar segments; margin at 21.6% supported by forex gains during the quarter.
- **Energy Management:** Revenue decline 4% YoY impacted by lower PGCIL spend; margin was at 12.7% (+290bp YoY) supported by forex gains during the quarter.
- **Building Technologies:** Revenue growth of 12.4% supported by growth across end users for energy efficiency and advanced surveillance solutions in data centers, hospitals, commercial offices and airports and margin of 6.8% (-190bp YoY).
- **Mobility**: Sales growth of 23.4% YoY supported by execution of order backlog in the metro segment and margin of 9.1%. Present in electrification and signaling and is not in rolling stock. Spending is done on electrification and signaling is yet to pick up.
- **Digital factory:** Sales growth of 24% YoY supported by digitalization initiatives across automotive, F&B and machine building, driving growth and margin of 10.4% YoY. Provides factory automation, motion control and process automation services in the segment
- **Process industries and drive:** Sales growth of 33% YoY, supported by wind, water and pharma segment.
- **Restructuring of the segmental reporting:** Segmental reporting has been reclassified in four segments compared to five segments earlier. New segments are (a) Gas and Power (38% of sales), (b) Smart infrastructure (28% of sales), (c) Digital infrastructure (18% of sales), (c) Mobility (8% of sales) and (d) Portfolio of companies (7% of sales)
- **Exports:** Not actively driving exports but has access to more than 100 markets as it is part of the global supply chain. Exports will fluctuate given global slowdown. Siemens exports only products and is not present in services.

Upgrade to Buy, TP raised to INR1,290

- **Upgrade to Buy:** SIEM trades at FY19E/20E P/E of 34.5x/32.9x versus its long-term average trading multiple of 49x. The underperformance over the past one year can be ascribed to (a) MSCI exclusion, (b) the decision to sell-off the Mobility division to parent and (c) de-rating of the overall capital goods sector amidst election uncertainty. The current valuation provides comfort, given the scope of an improvement in the operating performance and the likely gradual recovery in capex spending. **We upgrade SIEM to Buy with a target price of INR1,290 (35x Mar'21E EPS).**

Exhibit 32: P/E multiple at a discount to historical average



Source: MOFSL, Company

- **Raise earnings by 7-12%:** We increase our earnings estimates by 10%/7%/12% for FY19/20/21, led by higher margin assumption and other income.

Exhibit 33: We earnings by 7-12% over FY19-21E

Earnings Change	Old			New			Change (%)		
INR m	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E
Revenue	141,687	150,567	168,382	139,536	150,851	169,649	-2	0	1
EBITDA	15,229	16,697	18,538	16,321	16,864	19,559	7	1	6
EBITDA margin	10.70%	11.10%	11.00%	11.70%	11.20%	11.50%	0.90	0.10	0.50
Reported PAT	9,965	11,306	12,634	10,821	12,106	14,119	9	7	12
Adj. PAT	10,561	11,306	12,634	11,574	12,106	14,119	10	7	12

MOFSL, Company

- **Key risks – (a) Divestment of Gas & Power segment** – Siemens AG has announced the demerger of its Gas & Power segment from the existing listed Siemens AG entity. The same may be implemented for Siemens India entity as well. The process followed for the demerger (slump sale, demerger, re-listing, etc.) and the fair and transparent valuation are critical for the stock performance. **(b) Plans for Mobility remain unclear** – Management shared that the global board is yet to decide on the way forward for the Mobility business, as the earlier JV transaction with Alstom did not conclude.

Financials and Valuations

Income Statement (Standalone) (INR M)

Y/E September	2014	2015	2016	2017	2018	2019E	2020E	2021E
Total Revenues	**1,06,626**	**1,05,124**	**1,08,094**	**1,10,148**	**1,27,251**	**1,39,536**	**1,50,851**	**1,69,649**
Change (%)	-6.1	-1.4	2.8	1.9	15.5	9.7	8.1	12.5
Raw Materials	75,543	70,814	71,812	73,504	85,864	94,720	1,03,678	1,16,416
Staff Cost	14,118	13,942	14,139	13,926	14,487	15,936	16,732	18,406
SGA Expenses	9,676	10,607	11,940	12,205	13,739	12,558	13,577	15,268
EBITDA	**7,289**	**9,761**	**10,203**	**10,512**	**13,161**	**16,321**	**16,864**	**19,559**
Change (%)	5.6	34	5	3	25	24	3	16
% of Total Rev.	6.8	9.3	9.4	9.5	10.3	11.7	11.2	11.5
Depreciation	2,291	2,156	2,264	1,967	1,967	2,248	2,360	2,472
Interest	82	73	91	77	82	80	80	80
Other Income	1,039	1,604	1,645	2,547	2,800	3,281	3,645	4,067
EO Items (net)	4,296	5,798	22,825	4,301	0	-753	0	0
PBT	**10,250**	**14,934**	**32,318**	**15,317**	**13,912**	**16,521**	**18,068**	**21,074**
Tax	1,526	3,102	3,148	3,982	4,973	5,701	5,963	6,954
Rate (%)	14.9	20.8	9.7	26.0	35.7	34.5	33.0	33.0
PAT	**6,032**	**11,832**	**29,170**	**11,335**	**8,939**	**10,821**	**12,106**	**14,119**
Adjusted PAT	**4,428**	**6,034**	**6,345**	**7,034**	**8,939**	**11,574**	**12,106**	**14,119**
Change (%)	2.7	36.3	5.2	10.9	27.1	29.5	4.6	16.6

Balance Sheet (Standalone) (INR M)

Y/E September	2014	2015	2016	2017	2018	2019E	2020E	2021E
Share Capital	712	712	712	712	712	712	712	712
Reserves	43,044	50,554	67,494	76,335	82,342	90,385	99,585	1,10,316
Net Worth	**43,756**	**51,266**	**68,207**	**77,047**	**83,054**	**91,097**	**1,00,297**	**1,11,028**
Net Deferred Tax Liab	**-3,738**	**-3,175**	**-3,350**	**-2,442**	**-2,665**	**-2,665**	**-2,665**	**-2,665**
Capital Employed	**40,018**	**48,092**	**64,856**	**74,605**	**80,389**	**88,432**	**97,632**	**1,08,363**
Gross Fixed Assets	28,114	28,802	29,803	17,502	19,574	20,574	21,574	22,574
Less: Depreciation	14,558	15,269	15,959	4,158	6,060	8,308	10,669	13,141
Net Fixed Assets	**13,556**	**13,533**	**13,844**	**13,344**	**13,514**	**12,266**	**10,905**	**9,433**
Capital WIP	409	321	0	1,430	624	624	624	624
Investments	82	1,764	550	550	550	550	550	550
Curr. Assets	**84,803**	**86,485**	**99,042**	**1,13,465**	**1,25,139**	**1,40,364**	**1,56,226**	**1,77,235**
Inventory	10,472	9,509	9,993	10,165	11,389	12,616	13,639	15,338
Debtors	36,437	30,183	30,533	34,725	37,250	40,905	44,222	49,733
Cash & Bank Balance	11,210	20,959	35,094	40,713	36,457	42,880	50,837	58,714
Loans & Advances	14,134	14,958	3,425	6,216	8,733	9,557	10,332	11,620
Other Current assets	12,550	10,875	19,997	21,646	31,310	34,406	37,196	41,831
Current Liab. & Prov.	**58,832**	**54,011**	**48,579**	**54,184**	**59,438**	**65,372**	**70,673**	**79,479**
Creditors	32,323	24,863	19,386	26,556	30,303	33,259	35,956	40,437
Other Liabilities	14,607	12,687	18,030	17,377	18,123	19,879	21,491	24,169
Provisions	11,903	16,460	11,163	10,251	11,012	12,233	13,225	14,873
Net Current Assets	**25,970**	**32,474**	**50,462**	**59,281**	**65,701**	**74,992**	**85,553**	**97,756**
Application of Funds	**40,017**	**48,092**	**64,856**	**74,605**	**80,389**	**88,432**	**97,632**	**1,08,363**

Financials and Valuations

Ratios

Y/E September	2014	2015	2016	2017	2018	2019E	2020E	2021E
Basic (INR)								
EPS	**12.4**	**17.0**	**17.8**	**19.8**	**25.1**	**32.5**	**34.0**	**39.7**
Growth (%)	2.7	36.3	5.2	10.9	27.1	29.5	4.6	16.6
Cash EPS	18.9	23.0	24.2	25.3	30.6	38.8	40.6	46.6
Book Value	122.9	144.0	191.6	216.4	233.3	255.9	281.7	311.9
DPS	6.0	10.0	33.5	7.0	7.0	9.1	9.5	11.1
Payout (incl. Div. Tax.)	35.4	30.1	40.9	22.0	27.9	27.9	27.9	27.9
Valuation (x)								
P/E (Standalone)	90.0	66.1	62.8	56.7	44.6	34.5	32.9	28.2
Cash P/E	59.3	48.7	46.3	44.3	36.6	28.8	27.6	24.0
EV/EBITDA	53.2	38.7	35.6	34.1	27.5	21.8	20.6	17.4
EV/Sales	3.6	3.6	3.4	3.3	2.8	2.6	2.3	2.0
Price/Book Value	9.1	7.8	5.8	5.2	4.8	4.4	4.0	3.6
Dividend Yield (%)	0.5	0.9	3.0	0.6	0.6	0.8	0.8	1.0
Profitability Ratios (%)								
RoE	10.5	12.7	10.6	9.1	11.2	13.3	12.7	13.4
RoCE	13.7	18.2	15.1	14.0	16.2	18.7	17.7	18.7
RoIC	11.4	16.7	17.5	16.3	18.0	20.4	20.4	23.0
Turnover Ratios								
Debtors (Days)	125	105	103	115	107	107	107	107
Inventory (Days)	36	33	34	34	33	33	33	33
Creditors. (Days)	111	86	65	88	87	87	87	87
Asset Turnover (x)	2.7	2.2	1.7	1.5	1.6	1.6	1.5	1.6
Leverage Ratio								
Debt/Equity (x)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0

Cash Flow Statement (INR M)

Y/E September	2014	2015	2016	2017	2018	2019E	2020E	2021E
PBT before EO Items	**5,955**	**9,136**	**9,493**	**11,016**	**13,912**	**17,274**	**18,068**	**21,074**
Add : Depreciation	2,291	2,156	2,264	1,967	1,967	2,248	2,360	2,472
Interest	0	1	2	3	4	5	6	7
Less: Directtaxespaid	1,526	3,102	3,148	3,982	4,973	5,701	5,963	6,954
(Inc)/Dec in WC	97	3,246	-3,853	-3,200	-10,676	-2,868	-2,604	-4,326
CF from Operations	**6,817**	**11,436**	**4,755**	**5,801**	**230**	**10,954**	**11,862**	**12,265**
EO Income	4,296	5,798	22,825	5,205	0	-753	0	0
CF from oper. Incl. EOitems	**11,112**	**17,235**	**27,581**	**11,006**	**230**	**10,201**	**11,862**	**12,265**
(Inc)/dec in FA	-1,020	-1,481	-2,214	-2,863	-1,554	-1,000	-1,000	-1,000
Free Cash Flow	**10,093**	**15,753**	**25,366**	**8,143**	**-1,324**	**9,201**	**10,862**	**11,265**
(Pur)/Sale of Investments	350	-1,682	0	-0	0	0	0	0
CF from Investments	**-669**	**-3,163**	**-2,214**	**-2,863**	**-1,554**	**-1,000**	**-1,000**	**-1,000**
(Inc)/Dec in Networth	-16	-38	2,082	496	58	1,094	1,144	1,335
Inc/(Dec) in Debt	0	0	0	0	0	0	0	0
Less : Interest Paid	0	1	2					
Dividend Paid	2,563	4,285	14,312	2,990	2,990	3,872	4,050	4,723
CF from Fin. Activity	**-2,579**	**-4,324**	**-12,232**	**-2,495**	**-2,932**	**-2,778**	**-2,905**	**-3,389**
Inc/Dec of Cash	7,865	9,748	13,134	5,648	-4,256	6,423	7,957	7,877
Add: Beginning Bal.	6,038	11,210	20,959	35,094	40,713	36,457	42,880	50,837
Closing Balance	**11,210**	**20,958**	**34,094**	**40,742**	**36,457**	**42,880**	**50,837**	**58,714**

Explanation of Investment Rating	
Investment Rating	**Expected return (over 12-month)**
BUY	>=15%
SELL	< - 10%
NEUTRAL	> - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

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