

Institutional Equity Research

CG Power

Capital Goods | India

1QFY18 Result Update | August 23, 2017

CMP* (Rs)	80
Upside/ (Downside) (%)	(2.5)
Bloomberg Ticker	CRG IN
Market Cap. (Rs bn)	51.3
Free Float (%)	65.6
Shares O/S (mn)	630

HOLD

Target Price: Rs78

Exit from Loss-making Overseas Assets in Sight

CG Power & Industrial Solutions (CG Power) has reported a dismal performance in 1QFY18 with its consolidated net loss widening to Rs481mn in 1QFY18. However, net loss stood at Rs860mn including loss from discontinued operations of Rs379mn due to higher commodity prices, which could not be passed on owing to weak demand scenario in the run-up to GST roll-out. Its consolidated revenues declined by 5.7% YoY to Rs14.3bn in 1QFY18, as lower sales in Indonesia on account of local Ramzan festivity during the quarter. Notably, following successful sale of the US arm for US\$37mn (as guided in 4QFY17), the Management expects to sell loss-making unit in Hungary by Nov'17, which will lead to earnings upgrade. **Expecting CG Power's consolidated earnings to recover, going forward on low base and exit from loss-making assets in Hungary and Belgium, we change our recommendation on the stock to HOLD from REDUCE with an upwardly revised Target Price of Rs78 (from Rs70 earlier).**

Indonesian Biz Drags Consolidated Revenues

CG Power's consolidated net revenues declined by 5.7% YoY to Rs14.3bn in 1QFY18 compared to Rs15.2bn in 1QFY17 largely due to lower sales in Indonesia on account of local Ramzan festivity during the quarter, which led to deferred revenue of US\$30mn. However, the Management expects to realise the deferred revenue in the current quarter. CG Power's Industrial segment – which contributes 55.7% to its total revenue – grew by 13.1% YoY to Rs6.3bn due to faster execution of orders. However, Power System segment – which contributes 44.0% to its total revenue – de-grew by 16.5% YoY to Rs8.0bn.

Higher Commodity Prices Impair Operating Margin

CG Power's overall consolidated EBITDA margin declined by 580bps YoY to 3.1% in 1QFY18 primarily due to 510bps YoY decline in Industrial segment margin to 1.9% on the back of higher commodity prices. Further, GST-led channel de-stocking also accentuated pressure on margins as the Company couldn't undertake any price hike owing to sharp drop in Industrial segment's margins and loss provisions for overseas arms. Similarly, Power System segment's margins declined by 622bps YoY to 5.1% due to write-downs, which led to 67% YoY decline in EBITDA. Apart from the afore-mentioned factors, 76% YoY rise in interest cost to Rs536mn led to wider loss. However, the Management expects the margin to improve by 150-200bps in 2QFY18.

Outlook & Valuation

Looking ahead, we expect recovery in CG Power's consolidated earnings owing to low base and exit from loss-making overseas power business in Hungary and Belgium, which have been dragging the Company's profitability. **Expecting a successful exit from loss-making overseas assets, we change our recommendation on the stock to HOLD from REDUCE with an upwardly revised Target Price of Rs78 based on 22x P/E of FY19E EPS of Rs3.5.**

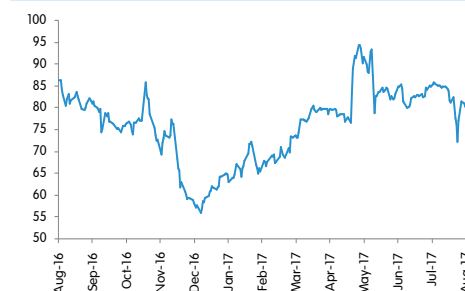
Key Financials (Rs mn)	FY16	FY17	FY18E	FY19E
Sales	55,950	61,198	63,257	72,490
EBITDA	4,302	4,702	4,934	5,944
Net Profit	1,133	1,100	1,637	2,213
EPS (Rs)	1.8	1.8	2.6	3.5
P/E (x)	44.3	45.6	30.6	22.7
P/B (x)	1.1	1.2	1.2	1.1
EV/EBITDA (x)	13.5	11.6	11.4	10.1
ROE (%)	2.5	2.7	3.8	4.9
ROCE (%)	6.6	8.4	8.2	9.3
EV/Sales	1.0	0.9	0.9	0.8

Source: Company, RSec Research

Share price (%)	1 mth	3 mth	12 mth
Absolute performance	(5.6)	(9.0)	(7.4)
Relative to Nifty	(4.5)	(14.2)	(21.2)

Shareholding Pattern (%)	Mar'17	Jun'17
Promoter	34.4	34.4
Others	65.6	65.6

1 Year Stock Price Performance



Note: * CMP as on Aug 23, 2017

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Risks to the View

- **Downside Risks:** Lower-than-expected recovery in Power System business; inordinate delay in selling loss-making overseas assets; sustained weakness in Indonesian operation and sustained weakness in Indonesian operation.
- **Upside Risks:** Early exit from overseas assets; and faster-than-expected recovery in domestic Power System Segment.

Exhibit 1: Quarterly Performance

(Rs mn)	1QFY18	1QFY17	YoY (%)	4QFY17	QoQ (%)
Net Sales	14,364	15,234	(5.7)	17,101	(16.0)
Operating Costs	13,913	13,869	0.3	15,919	(12.6)
EBIDTA	451	1,365	(66.9)	1,181	(61.8)
EBIDTA Margin (%)	3.1	9.0		6.9	
Other Income	118	155	(23.7)	232	(49.2)
Interest	537	304	76.5	625	(14.1)
Depreciation	361	381	(5.3)	438	(17.6)
Profit Before Tax	(328)	834		351	-
Tax	146	150		(31)	
Tax Rate (%)	(44.4)	18.0		(8.8)	
Share of profit/loss in associates	(7.00)	(2.40)		(6.30)	
PAT	(481)	682	-	(318)	51.5
Extraordinary Income	-	-	-	(693)	-
PAT	(481)	682	-	(316)	52.1
Loss from discontinued operation	(379)	(813)		(4,173)	
Tax expenses on discontinued operations	0	(27)	-	(51)	
Net profit discontinued operations	(379)	(786)		(4,123)	-
Net profit after discontinued operations	(860)	(104)	-	(4,440)	-

Source: Company, RSec Research

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Profit & Loss

Y/E March (Rs mn)	FY16	FY17	FY18E	FY19E
Net Sales	55,950	61,198	63,257	72,490
Raw Materials	36,116	40,141	41,370	47,263
Employee Costs	5,590	5,371	5,630	6,379
Other Expenditure	9,941	10,983	11,323	12,903
Total Expenditure	51,648	56,495	58,323	66,545
EBIDTA	4,302	4,702	4,934	5,944
% of Sales	7.7	7.7	7.8	8.2
Other Income	1,115	687	925	1,175
Depreciation	1,717	1,500	1,782	1,982
EBIT	3,700	3,889	4,077	5,138
Interest	800	1,880	1,611	1,809
Extraordinary	(1,113)	(727)	-	-
PBT	1,788	1,282	2,466	3,329
Total Tax	667	166	814	1,098
Tax Rate	37.3	13.0	33.0	33.0
PAT	1,121	1,116	1,652	2,230
Minority/profit from associate	12	(16)	(15)	(17)
Reported PAT	1,133	1,100	1,637	2,213
EPS	1.8	1.8	2.6	3.5

Balance Sheet

Y/E March (Rs mn)	FY16	FY17E	FY18E	FY19E
Share Capital				
Equity	1,254	1,254	1,254	1,254
Reserves	44,718	39,857	41,494	43,708
Net Worth	45,972	41,111	42,748	44,961
Secured Loans	6,003	5,038	5,038	5,038
Unsecured Loans	10,093	7,107	9,607	11,407
Total Debt	16,095	12,145	14,645	16,445
Deferred Tax Liability	3,427	2,623	2,623	2,623
Total	65,494	55,879	60,016	64,029
Net Block	15,007	15,944	17,687	19,505
Capital work In progress	142	282	725	895
Total Fixed assets	15,150	16,226	18,412	20,400
Goodwill	4,684	1,436	1,436	1,436
Investments	11,567	4,653	4,903	5,193
Current Assets	78,851	79,568	83,578	85,848
Inventory	5,850	8,821	9,268	10,939
Sundry Debtors	20,882	18,772	19,335	20,108
Cash	7,969	7,607	8,388	6,351
Loans & Advances, Prepaid Exp	44,150	44,368	46,587	48,450
Current Liabilities & Provisions	14,911	15,384	17,083	16,994
Creditors	13,579	13,831	15,468	15,315
Provisions	1,338	1,551	1,615	1,680
Others	29,852	30,618	31,230	31,855
Total	65,494	55,879	60,016	64,029

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Cash Flow Statement

Y/E March (Rs mn)	FY16	FY17E	FY18E	FY19E
Net Income/(loss) before Tax & EO items	1,788	1,282	2,466	3,329
Depreciation and Amortization	1,717	1,500	1,782	1,982
Interest Expense	800	1,880	1,611	1,809
Other Items	4,658	(8,360)	(1,628)	(1,826)
OP before Working Capital Changes	8,962	(3,698)	4,231	5,293
Inventories	7,151	(2,971)	(447)	(1,671)
Accounts Receivable	(11,714)	1,892	(2,782)	(2,637)
Accounts Payable	(9,625)	474	1,698	(88)
Net Change in Working Capital	(14,188)	(605)	(1,530)	(4,396)
Cash from Operating Activities	(5,226)	(4,304)	2,701	897
Taxes paid	(667)	(166)	(814)	(1,098)
Cash Flow From Operating Activities	(5,893)	(4,470)	1,887	(202)
Purchase of Fixed Assets	14,076	(2,064)	(3,968)	(3,970)
Purchase of Investment	1,442	6,913	(250)	(290)
Adjustment on acquisition of sub/asso.	23	3,248	-	-
Cash Flow From Investing Activities	15,541	8,097	(4,218)	(4,260)
Increase/(Decrease) of borrowing	(8,212)	(3,951)	2,500	1,800
Increase/(Decrease) of Unsecured loan	(2,944)	(804)	-	-
Others	2,650	766	612	625
Cash Flow From Financing Activities	(8,506)	(3,989)	3,112	2,425
Increase/(Decrease) in cash	1,141	(362)	782	(2,037)
Cash at the beginning of the year	6,827	7,969	7,607	8,388
Cash at the end of the year	7,969	7,607	8,388	6,351

Key Ratios

Y/E March (Rs mn)	FY16	FY17E	FY18E	FY19E
EBITDA margin (%)	7.7	7.7	7.8	8.2
RoE (%)	2.5	2.7	3.8	4.9
RoCE (%)	6.6	8.4	8.2	9.3
EV / sales (x)	1.0	0.9	0.9	0.8
EV / EBITDA (x)	13.5	11.6	11.4	10.1
P/E (x)	44.3	45.6	30.6	22.7
P / BV (x)	1.1	1.2	1.2	1.1

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Rating Guides

Rating	Expected absolute returns (%) over 12 months
BUY	>10%
HOLD	-5% to 10%
REDUCE	>-5%

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