ABB India

Accumulate

Result Update

DART
DOLAT ANALYSIS & RESEARCH THEMES
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Rich valuation leaves little upside

- ABB India's Q2CY21 EBITDA miss (14%/21% vs DART/Cons est.) was primarily on the account of, i) Delays in manufacturing clearances which led to lower than expected sales in Process Automation (PA) biz & ii) EBIT margin contraction of ~500bps QoQ in Electrification (EL) biz due to hardening of commodity prices.
- Despite headwinds caused by pandemic, Motion (MO) biz sustained strong momentum with ordering growth of +92%/+15% YoY/QoQ, which led to total order inflow growth of 41% YoY. Order backlog stood at Rs46bn, 0.7x TTM sales. Data centers, F&B, Pharma and Electronics manufacturing are high growth areas for ABB. Power distribution, Water, Railways & Metro and Automotive sectors are likely to grow in double digits in the near term while conversion of enquiries into firm orders from sectors such as Oil & Gas, Cement, Chemicals and Steel is taking longer given the Covid restrictions.
- We build in 15% sales CAGR over CY20-23E as improving demand environment augurs well for ABB. EBITDA margins are expected to reach ~10% by CY24E led by better operative leverage of Robotics biz, cost rationalization, completion of low margin legacy orders under Industrial Automation (IA) biz and exit of loss making businesses.
- ABB trades at 69x/58x PE CY22E/23E even after building in a healthy earnings CAGR of 42% over CY20-23E. We retain 'Accumulate' rating as most of the positives are already priced in, implying limited upside & low margin of safety. We roll forward to Dec'23 and assign a TP of Rs1745, valuing at 60x PE multiple.

Q2CY21 Result (Rs Mn)

Particulars	Q2CY21	Q2CY20	YoY (%)	Q1CY21	QoQ (%)
Revenue	14,250	9,858	44.6	16,292	(12.5)
Total Expense	13,302	9,623	38.2	14,969	(11.1)
EBITDA	948	234	304.2	1,323	(28.4)
Depreciation	284	249	14.1	253	12.4
EBIT	664	(15)	(4644.5)	1,070	(38.0)
Other Income	252	266	(5.3)	253	(0.2)
Interest	16	38	(57.3)	32	(49.7)
EBT	900	234	284.3	1,842	(51.2)
Tax	216	67	224.9	336	(35.6)
RPAT	683	168	307.9	1,506	(54.6)
APAT	683	148	363.2	955	(28.4)
			(bps)		(bps)
Gross Margin (%)	33.6	37.8	(416)	33.3	28
EBITDA Margin (%)	6.6	2.4	427	8.1	(147)
NPM (%)	4.8	1.7	310	9.2	(445)
Tax Rate (%)	24.1	28.4	(439)	18.2	582
EBIT Margin (%)	4.7	(0.1)	480	6.6	(191)

CMP	Rs 1,687
Target / Upside	Rs 1,745 / 3%
NIFTY	15,779

Scrip Details

Equity / FV	Rs 424mn / Rs 2
Market Cap	Rs 357bn
	USD 5bn
52-week High/Low	Rs 1,857/ 847
Avg. Volume (no)	1,98,129
Bloom Code	ABB IN

Price Performance	1M	3M	12M
Absolute (%)	(6)	22	91
Rel to NIFTY (%)	(6)	16	53

Shareholding Pattern

	Dec'20	Mar'21	Jun'21
Promoters	75.0	75.0	75.0
MF/Banks/FIs	7.0	7.3	7.1
FIIs	4.1	3.8	3.7
Public / Others	14.0	13.9	14.2

Valuation (x)

	CY21E	CY22E	CY23E
P/E	98.3	68.7	58.0
EV/EBITDA	67.7	48.6	41.5
ROE (%)	9.8	13.0	14.1
RoACE (%)	10.0	13.1	14.2

Estimates (Rs mn)

	CY21E	CY22E	CY23E
Revenue	66,042	76,879	85,661
EBITDA	4,914	6,773	7,855
PAT	3,637	5,201	6,164
EPS (Rs.)	17.2	24.5	29.1

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Play on Automation, Make in India and Cyclical Improvement

We remain structurally positive on ABB as it is a play on: i) Durable and accelerating automation theme, ii) Beneficiary of increased manufacturing investments in India driven by Make in India, iii) no lasting damage from COVID-19 and iv) Signs of cyclical improvement. Further, it is expected to gain benefits from increasing relevance of energy efficiency and emerging needs in electrification given its strong competitive positioning globally in the motors and drives business. ABB's motors and drives business can grow meaningfully as the industry goes for upgradation of the existing base of inefficient motors. It has a very large product basket, diversified industry and infrastructure (including buildings) presence, a very wide and varied (channel, EPCs, OEMs, direct) distribution platform, large manufacturing and services footprint and technology edge. Exports (motors and switchgear equipment) and services (automation related as well as provision of services for global business such as customisation, etc.) could be additional drivers of growth.

Growth momentum to continue

The order inflows for the quarter stood at Rs16.8bn, up by 41% YoY, with growth in short cycle orders. Revenues for Robotics & Discretion Automation (RA)/ Electrification (EL)/ Motion (MO) / Industrial Automation (IA) increased by 262%/61%/27%/13% YoY respectively. Pertinently, Service business has improved marginally in the range of 18.5 -19% in H1CY21 (compared to 18% in H1CY20), we believe given the large installed base of ABB products this should see uptick. Overall, ABB's future growth will be led by Data centres, electronics manufacturing, renewables, and pharmaceuticals due to the demand for more reliable & energy efficient products. Notably, the demand for robotics solutions is increasing in India, with management stating that, in addition to automotive, repeat orders are being received from sectors such as food and beverage, pharmaceutical, and electronics manufacturing. While in case of Data Centres, ABB is in a sweet spot with its Electrification and Process Automation solutions.

Margin expansion is key stock trigger

The ABB Group's margin target of 13-16% by 2023 would be met through a decentralised strategy in which each unit is accountable for its own performance. ABB India's current margin is in the 6-8% range, but management plans to increase it to around double digit by CY23E. We believe ABB India will play an important role in exports due to its low cost structure; additionally, India remains a strategic importance for the group, as evidenced by the fact that the group's Global R&D centre is located in India, following Europe. Especially, the Motion portfolio (MV offerings), we believe, will be the primary growth driver in export markets, followed by the Drives system.

Exhibit 1: Actual V/s Estimates

Particulars (Rs mn)	Actual	DART Estimates	Variance (%)	Comments
Revenue	14,250	15,324	(7.0)	Lower due to muted offtake in April
EBITDA	948	1,103	(14.1)	
EBITDAM (%)	6.6	7.2	(55.1)	
Adj. PAT	683	816	(16.2)	Impacted due to lower other income

Source: DART, Company

Exhibit 2: Change in estimates

Particulars (Rs mn)	New Estimates			% Change			Old Estimates		
	CY21E	CY22E	CY23E	CY21E	CY22E	CY23E	CY21E	CY22E	CY23E
Sales	66,042	76,879	85,661	0.0	0.0	0.0	66,042	76,879	85,661
EBITDA	4,914	6,773	7,855	0.0	0.0	0.0	4,914	6,773	7,855
PAT	3,637	5,201	6,164	0.0	0.0	0.0	3,637	5,201	6,164
EPS	17.2	24.5	29.1	0.0	0.0	0.0	17.2	24.5	29.1
EBITDAM (%)	7.4	8.8	9.2	0.0	0.0	0.0	7.4	8.8	9.2

Source: DART, Company

Exhibit 3: Segment Revenue

Particulars (Rs mn)	Q2CY21	Q2CY20	YoY (%)	Q1CY21	QoQ (%)
Robotics & Discrete automation	890	246	261.7	479.5	85.6
Motion	5,005	3932.2	27.3	6311.9	(20.7)
Electrification Products	5,766	3578.2	61.1	6329.7	(8.9)
Industrial Automation	2,674	2373.2	12.7	3255.8	(17.9)

Source: DART, Company

Exhibit 4: Segment EBIT

Particulars (Rs mn)	Q2CY21	Q2CY20	YoY (%)/ bps	Q1CY21	QoQ (%)/bps
Robotics & Discrete automation	46	9	390.3	53	(14.0)
EBIT margin (%)	5.1	3.8	134.4	11.1	(592.8)
Motion	550	321	71.2	896	(38.6)
EBIT margin (%)	11.0	8.2	281.7	14.2	(320.7)
Electrification Products	394	173	127.8	745	(47.2)
EBIT margin (%)	6.8	4.8	199.9	11.8	(494.6)
Industrial Automation	161	1	14,563.6	285	(43.4)
EBIT margin (%)	6.0	0.0	598.5	8.8	(272.2)

Source: DART, Company

Conference call highlights

- **Outlook** – The management anticipates that robotics and flexible automation will grow faster in the medium term. Furthermore, the demand for energy efficiency and electrical portfolio, particularly building automation, will witness huge demand due to the need for highly reliable components. In the case of Process Automation, demand from Metals/Oil & Gas is directly correlated with Opex & Capex, which is expected to gain traction in 3-4 years with a significant share coming from this segment. While railways and metros have continued to expand, ABB is looking to play a role in rail electrification. Overall, given how the portfolio and market segments will play out over the next 4-5 years, ABB is well-positioned.

  ABB has a high double-digit exposure to the Steel/Metals/Mining/Oil & Gas markets. The company is also seeing double-digit revenue and order growth in the Building & Infra/Textiles/Water & wastewater sectors. Notably, the growth rates for Data Center/F&B/Pharma are as high as 18%/14%/13%, respectively.

- **Pricing** – ABB's ability to spread costs across the segment is strong. Pricing, on the other hand, varies across industries. For example, in the sensitive segment of Data Center, customers prefer reliability, availability, maintainability, and serviceability, where ABB excels. Power Distribution is the same way. When it comes to railways, there is no pricing power due to tenders and reverse auctions, but given the good volumes, ABB has adjusted to meet Railways' expectations. In the case of waste and water treatment, the intensity of completion was previously higher; however, with increasing demand for energy-efficient solutions and reliability, the competition has evened out, resulting in higher prices.

- **Expansion mandate** - In line with Parent's effort to click higher margins, each division has been mandated to expand in the coming year through organic or inorganic growth. ABB India has enough land bank at its current manufacturing facilities, as well as a strong cash position, to expand its product line. Notably, during the pandemic, the company expanded its Robotics factories. ABB is also expanding its GIS plant in Nashik, which is scheduled to be completed by the end of next year.

- **ESG plan**: The company has solidified its ESG plan with 10 steps under implementation through significant allocation of resource, the main focus would be on - i) Green Infrastructure, ii) Energy Efficiency Improvement, iii) Renewable Energy, iv) GHG Emission Reduction, v) Water Conservation, vi) Material Conservation, vii) Waste Management & Circularity, viii) Green Supply Chain & Customer, ix) Product Stewardship & Life cycle analysis, and x) Innovation & Biodiversity.

- **All-round order inflows** - Electrification business area secured orders from utility, data center segments for a range of power equipment especially in the low voltage category. Motion business area secured order growth across all divisions supported by channel businesses and exports with our world-class energy efficiency portfolio. Robotics & Discrete Automation business continued to record reasonable order inflows, including green shoots of recovery in the automotive market and demand in new market segments. Besides, the portfolio in energy management, grid integration stability with advanced process controls and digitalization were some of the focus areas for Process Automation business area orders.

  The **key order wins** included – i) One of the biggest orders for city gas distribution network with SCADA and remote terminal unit, solutions for a leading public sector , ii) Power equipment for data center in north India from 33kV GIS Substation- E house, GIS, AIS and LV supply, iii) Power equipment like switchgears of 33kV and 11kV for railway tunnel project in J&K, iv) Electrification and instrumentation package for a red mud filtration project for an aluminium major, v) Gas insulated switchgear package for a north India corridor of the Regional Rapid Transit System, and vi) Robotics paint system order from Indian auto major.

- **Unallocated expenses**: Unallocated expense was Rs235mn in Q2CY21 (vs Rs656mn in Q1CY21), a lower figure due to a change in CSR rules and an actuarial valuation loss. Unallocated expenses are expected to align with revenues in the future.

- **E-mart** - The digital e-mart platform has gained good traction and ABB is looking to strengthen its online presence while maintaining a strong physical distribution network. Notably, in last couple of months, there has been steep increase in number of inquiries from Tier-2 & Tier 3 cities.

- **Business restructuring** - The carved out Mechanical Power transmission business is a Trading Business with US centric portfolio. While in case of EV business, it is still at nascent stage in India. EV segment has been performing very well in US and European regions as compared to Asia Pacific. However, this business requires significantly higher investments vs ABBs's traditional business, which necessitated the carve out of the entity. ABB India does not manufacture most of the equipment in EV space, so impact on India business is expected to be limited.

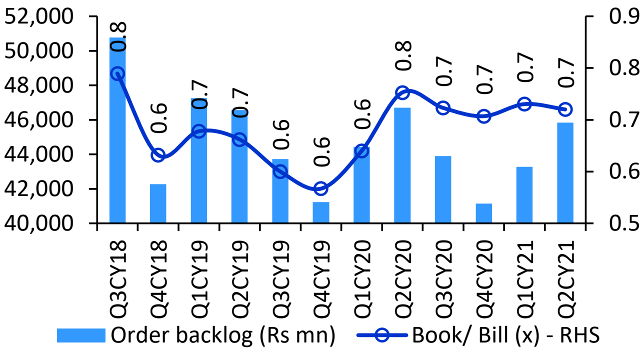
- **Impact of legacy project mitigated for Process automation** - In the last quarter, Process Automation was impacted by legacy projects, and volume was down because the market was not supporting orders, which was a double whammy. Going forward, with the legacy impact reduced, and a large part of it due to the fact that the market for metals and oil and gas has begun to recover, and with services moving in the right direction, Process Automation should fare better. Though management stated that over the next two quarters, a clearer picture would emerge.
- **Exports** - The company witnessed good order inflows during the quarter constituting 16% of exports. While revenues were muted (affected due to the lost 3-3.5 weeks) contributing 12% of the revenues during the quarter.
- **Services** - In Q2CY21, 18% of revenues came from services, while the number stood in the range of 18.5-19% in H1CY21 (vs 18% in H1CY20).
- The Blended **Capacity utilization level** is around 80-85%

Segmental performance

- **Electrification**: The segment registered a revenue of Rs5.8bn, up by 61% YoY. The order inflows stood at Rs5.8bn with Order backlog of Rs13.7bn, with good order booking seen in Utility and Data Center. EBIT stood at Rs394mn, with margin at 6.8%, was due to better mix and increased price realizations though partially offset by increase in commodity prices.
- **Motion**: The segment reported a revenue growth of Rs5bn, up by 27% YoY driven by growth in higher LV motors, drives, and services business. The order inflows were reported at Rs7.3bn primarily driven by Short cycle orders. The EBIT came in at Rs550mn with margin at 11.0% due to better volume growth and mix and higher services business.
- **Process Automation**: The segment revenues stood at Rs2.7bn, relatively lower due to delay in manufacturing clearances. The order inflows came in at Rs3.6bn with system orders staging a comeback. The EBIT margin was reported at 6.0% mainly due to better revenue mix and higher service revenues.
- **Robotics**: The segment's revenue came in at Rs890mn, up by as services revenue were up with steady upgrades. The order inflows stood at Rs650mn with early signs of recovery in automotive segment. The EBIT margin stood at 5.1%supported by service revenues.

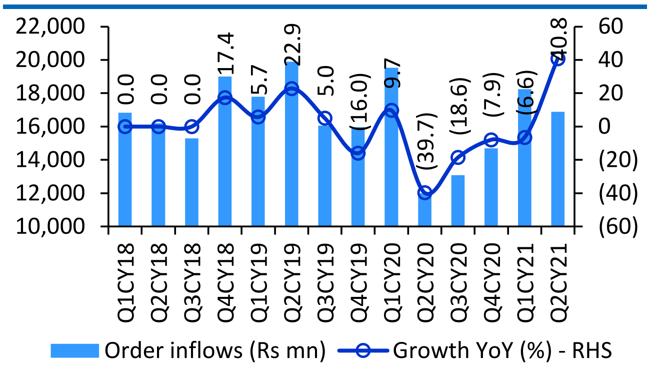
Story in chart

Exhibit 5: Order backlog of RsRs46bn, 0.7x TTM sales



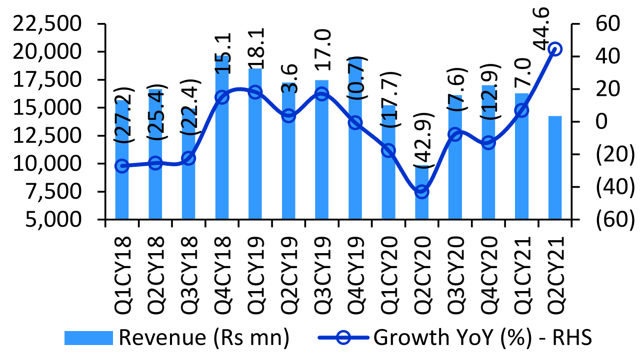
Source: DART, Company

Exhibit 6: Gradual bounce back in orders across businesses



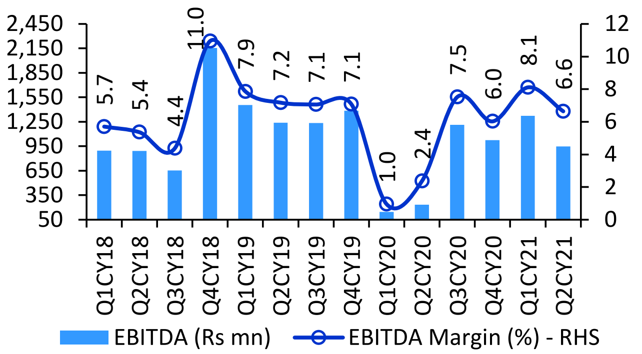
Source: DART, Company

Exhibit 7: Revenues partly impacted due to lower offtake in April



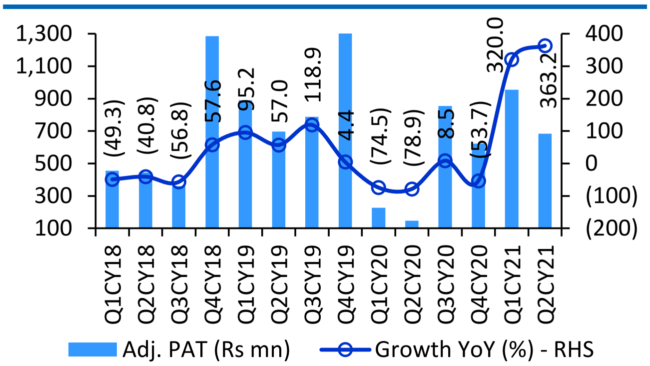
Source: DART, Company

Exhibit 8: Margin miss was primarily due to delay in manufacturing clearances in PA and hardening of commodity prices for EL



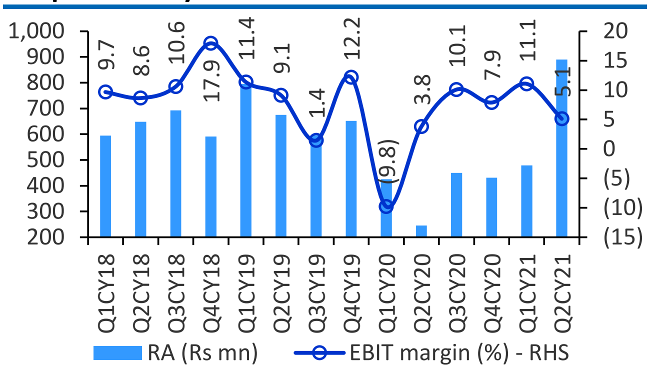
Source: DART, Company

Exhibit 9: Adj. PAT lower than estimates due to lower other income



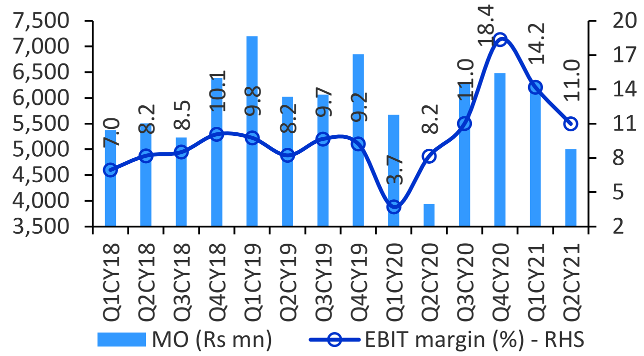
Source: DART, Company

Exhibit 10: Services revenue boosted overall profitability for RA



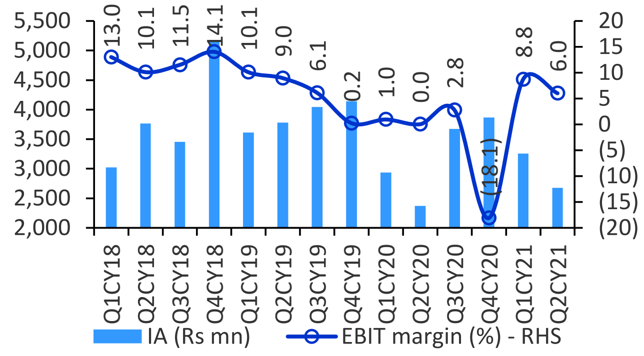
Source: DART, Company

Exhibit 11: Growth driven by Low voltage motors, drives and service business for MO



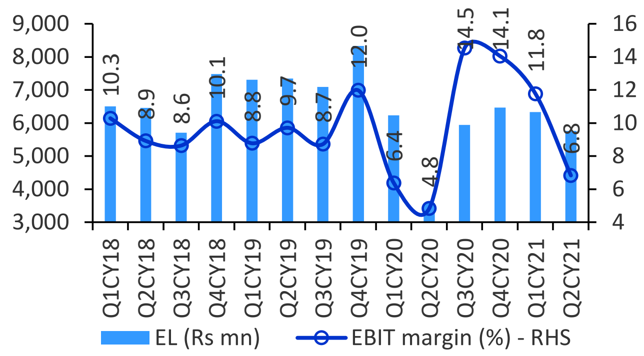
Source: DART, Company

Exhibit 12: IA revenues impacted due to delay in manufacturing clearances



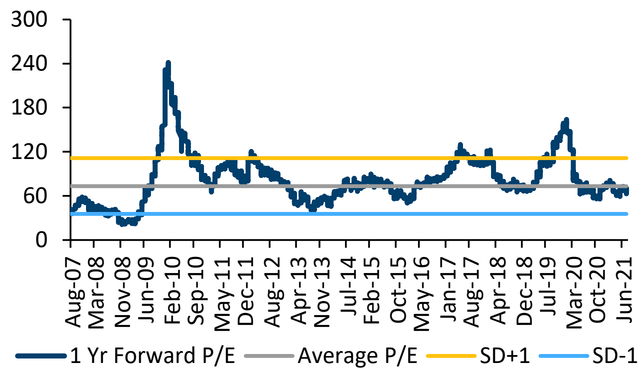
Source: DART, Company

Exhibit 13: Sharp margin contraction for EL due to hardening of commodity prices



Source: DART, Company

Exhibit 14: Stock is trading at a 1-Yr fwd PE of 64x



Source: DART, Company

Profit and Loss Account

(Rs Mn)	CY20A	CY21E	CY22E	CY23E
Revenue	**58,210**	**66,042**	**76,879**	**85,661**
Total Expense	**55,450**	**61,127**	**70,106**	**77,805**
COGS	38,704	43,720	49,971	55,251
Employees Cost	5,680	5,851	6,143	6,450
Other expenses	11,066	11,557	13,992	16,104
EBIDTA	**2,759**	**4,914**	**6,773**	**7,855**
Depreciation	1,204	1,126	1,138	1,148
EBIT	**1,556**	**3,788**	**5,635**	**6,707**
Interest	169	155	120	120
Other Income	1,069	1,229	1,438	1,654
Exc. / E.O. items	588	0	0	0
EBT	**3,044**	**4,862**	**6,953**	**8,241**
Tax	739	1,225	1,752	2,077
RPAT	2,304	3,637	5,201	6,164
Minority Interest	0	0	0	0
Profit/Loss share of associates	**0**	**0**	**0**	**0**
APAT	**1,717**	**3,637**	**5,201**	**6,164**

Balance Sheet

(Rs Mn)	CY20A	CY21E	CY22E	CY23E
Sources of Funds				
Equity Capital	424	424	424	424
Minority Interest	0	0	0	0
Reserves & Surplus	35,640	38,004	41,384	45,391
Net Worth	**36,064**	**38,428**	**41,808**	**45,815**
Total Debt	133	0	0	0
Net Deferred Tax Liability	502	502	502	502
Total Capital Employed	**36,699**	**38,930**	**42,310**	**46,317**
Applications of Funds				
Net Block	**6,938**	**7,012**	**7,074**	**7,326**
CWIP	749	749	749	749
Investments	7,382	7,382	7,382	7,382
Current Assets, Loans & Advances	**60,836**	**66,307**	**74,496**	**82,491**
Inventories	8,408	9,540	10,531	11,734
Receivables	16,950	17,189	20,010	22,295
Cash and Bank Balances	22,066	24,901	27,922	31,770
Loans and Advances	179	203	236	263
Other Current Assets	13,234	14,475	15,797	16,428
Less: Current Liabilities & Provisions	**39,206**	**42,520**	**47,391**	**51,631**
Payables	17,207	18,094	20,010	21,122
Other Current Liabilities	21,999	24,426	27,381	30,509
sub total				
Net Current Assets	21,630	23,787	27,105	30,860
Total Assets	**36,699**	**38,930**	**42,310**	**46,317**

E – Estimates

Important Ratios

Particulars	CY20A	CY21E	CY22E	CY23E
(A) Margins (%)				
Gross Profit Margin	33.5	33.8	35.0	35.5
EBIDTA Margin	4.7	7.4	8.8	9.2
EBIT Margin	2.7	5.7	7.3	7.8
Tax rate	24.3	25.2	25.2	25.2
Net Profit Margin	4.0	5.5	6.8	7.2
(B) As Percentage of Net Sales (%)				
COGS	66.5	66.2	65.0	64.5
Employee	9.8	8.9	8.0	7.5
Other	19.0	17.5	18.2	18.8
(C) Measure of Financial Status				
Gross Debt / Equity	0.0	0.0	0.0	0.0
Interest Coverage	9.2	24.4	47.0	55.9
Inventory days	53	53	50	50
Debtors days	106	95	95	95
Average Cost of Debt	165.6	232.9		
Payable days	108	100	95	90
Working Capital days	136	131	129	131
FA T/O	8.4	9.4	10.9	11.7
(D) Measures of Investment				
AEPS (Rs)	8.1	17.2	24.5	29.1
CEPS (Rs)	13.8	22.5	29.9	34.5
DPS (Rs)	5.3	6.0	8.6	10.2
Dividend Payout (%)	65.5	35.0	35.0	35.0
BVPS (Rs)	170.2	181.3	197.3	216.2
RoANW (%)	6.5	9.8	13.0	14.1
RoACE (%)	5.2	10.0	13.1	14.2
RoAIC (%)	9.0	26.4	39.7	46.4
(E) Valuation Ratios				
CMP (Rs)	1687	1687	1687	1687
P/E	208.2	98.3	68.7	58.0
Mcap (Rs Mn)	3,57,383	3,57,383	3,57,383	3,57,383
MCap/ Sales	6.1	5.4	4.6	4.2
EV	3,35,451	3,32,483	3,29,461	3,25,613
EV/Sales	5.8	5.0	4.3	3.8
EV/EBITDA	121.6	67.7	48.6	41.5
P/BV	9.9	9.3	8.5	7.8
Dividend Yield (%)	0.3	0.4	0.5	0.6
(F) Growth Rate (%)				
Revenue	(20.4)	13.5	16.4	11.4
EBITDA	(48.0)	78.1	37.8	16.0
EBIT	(64.7)	143.5	48.7	19.0
PBT	(31.4)	59.8	43.0	18.5
APAT	(53.8)	111.9	43.0	18.5
EPS	(53.8)	111.9	43.0	18.5

Cash Flow

(Rs Mn)	CY20A	CY21E	CY22E	CY23E
CFO	3,182	5,441	6,042	7,405
CFI	4,424	(1,200)	(1,200)	(1,400)
CFF	(1,523)	(1,406)	(1,820)	(2,157)
FCFF	7,725	4,357	4,932	6,095
Opening Cash	15,976	22,066	24,901	27,922
Closing Cash	22,066	24,901	27,922	31,770

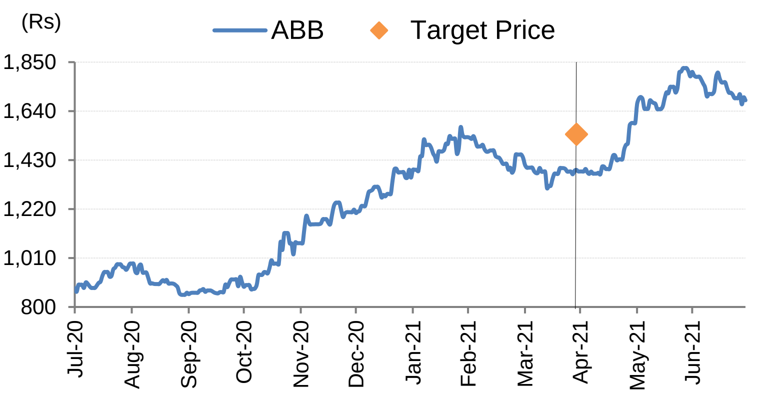
E – Estimates

DART RATING MATRIX

Total Return Expectation (12 Months)

Buy	**> 20%**
Accumulate	**10 to 20%**
Reduce	**0 to 10%**
Sell	**< 0%**

Rating and Target Price History



Month	Rating	TP (Rs.)	Price (Rs.)
Apr-21	Accumulate	1,541	1,388

*Price as on recommendation date

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