ICICI direct Research

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Decent execution, muted order inflows amid unlock

Q2FY22E is likely to be a decent quarter for the capital goods universe in terms of execution as most companies likely to recover to pre-Covid levels while order inflows are yet to see any major momentum owing to a delay in finalisation and order deferrals. Product companies are likely to post a decent quarter YoY on a low base, aided by normalisation of supply chain and dispatches. Larsen & Toubro (L&T) announced EPC orders in the range of ~₹ 5000-12500 crore (as on date, ex-services segment) across water treatment, heavy engineering, hydrocarbon, buildings & factories segments indicating muted order inflows for the quarter amid a challenging environment. In the T&D space, KEC has announced decent order inflows of ₹ 2660 crore aided by orders from T&D (domestic, international markets), railways, civil, etc, while Kalpataru Power (KPTL) has not yet announced any order as on date for the quarter. Thermax has announced order inflows worth ~₹ 293 crore as on date for the quarter while a further pick-up in industrial capex is expected to improve its revenue visibility. Bharat Electronics (BEL) has received ~₹ 2700 crore worth orders for the quarter.
Overall, order inflows are expected to remain muted, with delays in project finalisations and project deferrals across key segments. However, the order pipeline remains robust across T&D, green energy corridor, railways, transportation, water and infrastructure, etc, and are expected to be lumpy in H2FY22E. Key risks remain project delays/deferrals, lesser conversion of the tendering pipeline.

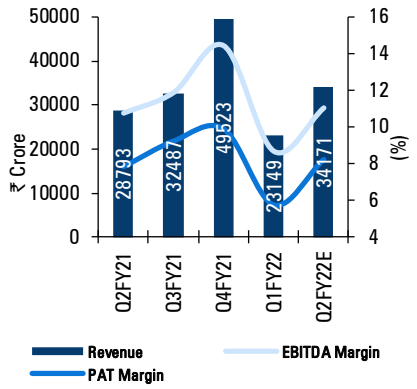
Revenue, EBITDA to grow 18.7%, 21.8%, respectively

Overall, the coverage universe revenue is expected to grow 18.7% YoY owing to decent execution amid low base at engineering and T&D companies like L&T, KEC, KPTL, BEL and Cochin Shipyard. The international business and exports likely to aid performance of companies like L&T, KEC, AIA, Elgi, etc. We expect EBITDA to grow 21.8% YoY owing to operating leverage in product companies and execution pick-up by EPC companies amid low base factoring in pandemic impact and higher commodity prices. Consequently, overall PAT is expected to grow 24.8% YoY accounting for other income, operating leverage and tax effect in the base quarter.

Decent execution expected among EPC companies…

Overall, EPC companies are expected to post a decent performance on the execution front factoring in the second wave impact while margins are expected to see some impact owing to high commodity prices. Power T&D companies like KEC, KPTL are expected to report combined revenue, EBITDA, PAT growth of 8.6%, -4.2%, -15.4% YoY, respectively, factoring in higher commodity prices and execution pick-up in key international markets. L&T (standalone, ex-E&A) is likely to report a decent performance with revenue growth of 19.6% YoY to ₹ 18893.2 crore, EBITDA is expected to grow 27.4% to ₹ 1568.1 crore amid low base and execution pick-up and adjusted PAT (ex-E&A) expected to grow 28.3% at ₹ 1349 crore partly aided by higher other income, lower interest expense. Thermax' revenue is expected to grow 34.3% while EBITDA is expected at ₹ 111.8 crore with margin of 7.3%. On the defence front, BEL is expected to report a better performance with revenue growth of 22.7% to ₹ 3911.1 crore while EBITDA is expected to grow 37.4% to ₹ 856.4 crore YoY. Cochin Shipyard is expected to report revenue, EBITDA growth of 20% while EBITDA is expected at ₹ 153.8 crore, up 22.3% YoY on a low base.

Topline & Profitability (Cap. Goods Universe)



Top Picks

L&T
Bharat Electronics
Elgi Equipments
SKF India

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Focus on working capital, cash flows likely to continue…

Overall, EPC companies like L&T, KEC, KPTL, BEL and Cochin Shipyard are expected to remain focused on working capital and cash flow management amid reasonable execution factoring in second wave impact and focus on receivables collections. Companies with stronger balance sheets and cash flows like are well placed to gain the most from a gradual economic recovery. Product companies like SKF India, Elgi Equipment, AIA Engineering, which have a strong balance sheet, zero debt and healthy cash balances are likely to benefit as demand gradually coming back to normal.

Exports likely to aid performance of product companies

In the bearing space, we see a sequential increase in revenue in the range of 14-17%. This is largely due to increase in economic activities due to reducing Covid impact and increasing demand in the automobile sector. We expect price hikes across manufacturers to curtail the impact of rising commodity prices, to an extent. However, we believe margins should remain under pressure due to negative operating leverage and higher inventory costs. Greaves Cotton is expected to report revenue growth of 40% while EBITDA is expected at ₹ 28.3 crore on a low base and muted engine volumes in conventional 3-W, 4-W space. Elgi Equipment is expected report revenue, EBITDA growth of 16%, -24.6%, respectively, owing to strong growth in international business. Companies like AIA Engineering are expected to report revenue, EBITDA growth of 11.4%, -2.6%, respectively, factoring in commodity price impact.

Exhibit 1: Estimates for Q2FY22E: (Capital Goods) (₹ crore)

Company	Revenue	Change (%)		EBITDA	Change (%)		PAT	Change (%)	
	Q2FY22E	YoY	QoQ	Q2FY22E	YoY	QoQ	Q2FY22E	YoY	QoQ
AIA Engineering	827.0	11.4	11.8	185.2	-2.6	7.8	157.0	9.1	4.9
Bharat Electronics	3,911.6	22.7	139.3	856.4	37.4	NA	574.9	44.8	NA
Greaves Cotton	403.6	40.0	88.3	28.3	61.8	NA	14.1	316.3	NA
Elgi Equipments	557.0	16.0	13.8	50.0	-24.6	55.6	22.3	-32.9	79.4
Kalpataru Power	2,182.7	16.0	37.6	222.6	10.2	37.4	133.2	-10.0	75.2
KEC International	3,401.2	4.4	33.9	251.7	-14.1	57.4	112.6	-21.0	144.0
L&T	18,893.2	19.6	44.1	1,568.1	27.4	52.8	1,349.0	28.3	79.8
NRB Bearings	239.6	21.2	19.0	30.6	0.7	14.2	16.8	47.4	0.0
SKF India	787.2	11.9	13.5	120.3	31.0	5.7	84.0	29.2	6.2
Thermax Ltd	1,532.2	34.3	45.6	111.8	41.0	77.4	81.1	66.5	91.3
Timken India	540.4	37.8	15.5	96.4	16.6	3.9	59.7	19.6	5.3
Cochin Shipyard	788.9	20.0	139.5	153.8	22.3	571.6	127.9	18.0	296.0
IEX	106.4	50.1	16.9	88.5	59.5	18.2	71.7	61.9	15.5
Total	**34,171.0**	**18.7**	**47.6**	**3,763.8**	**21.8**	**87.9**	**2,804.2**	**24.8**	**111.6**

Source: Company, ICICI Direct Research

Exhibit 3: Company Specific Views (Capital Goods)

Company	Remarks
AIA Engineering	For Q2FY22E, we expect AIA Engineering to report volume numbers at 66806 MT, down 2.6% YoY, owing to marginal impact on the base business from repeat customers amid challenges in new customer engagements due to pandemic. We expect realisation at ₹ 119 per kg, up 13.4%, on account of a change in the product mix and price pass-through. Consequently, revenue is expected to grow 12.4% to ₹ 827 crore, up 11.4% YoY. EBITDA is expected to declined marginally by ~2.6% to ₹ 185.2 crore with EBITDA margin of 22.4% while PAT is expected to grow 9.1% to ₹ 157 crore YoY factoring in lower margins and higher other income
Bharat Electronics	We expect BEL to report revenues at ₹ 3911.6 crore, up 22.7% YoY, on a low base and with improved execution and supply chain. EBITDA margin is expected at 21.9% owing to product mix & execution pace, leading to absolute EBITDA growing 37.4% YoY to ₹ 856.4 crore. Accordingly, we expect PAT to grow 44.8% YoY to ₹ 574.9 crore on a low base. Overall, strong order backlog of ~₹ 55800 crore is likely to augur well in the long term
Greaves Cotton	For Q2FY22E, we expect Greaves Cotton to report 3-W & 4-W engine volumes at 37505 units owing to slowdown in conventional 3-W, 4-W space and low base effect. Non-auto volumes are likely to aid growth. New business initiatives and Ampere sales are likely to support overall sales. Consequently, revenues are expected to grow 40% YoY on a low base to ₹ 403.6 crore, EBITDA is expected at ₹ 28.3 crore with margins of 7.0% factoring in high commodity prices and cost rationalisation initiatives while adjusted PAT is expected at ₹ 14.1 crore on a low base amid pandemic
Elgi Equipments	For Q2FY22E, Elgi is likely to see a rebound in domestic performance while international air compressor market is likely to report strong revenue growth as it is gradually ramping up in key markets. Consolidated revenues are expected to grow 16% YoY to ₹ 557 crore while EBITDA margin is expected at 9% leading absolute EBITDA decline of 24.6% to ₹ 50 crore factoring in impact of commodity prices and pandemic impact while PAT is expected at ₹ 22.3 crore, down 32.9% factoring in operating leverage and tax adjustments
Kalpataru Power (KPTL)	KPTL has not yet announced any new orders, as on date for the quarter. For Q2FY22E, KPTL is expected to report decent performance on the back of execution pick-up in key segments like international T&D despite challenges. We expect revenues to grow 16% YoY to ₹ 2182.7 crore, as base quarter saw marginal impact of pandemic. EBITDA is expected to grow 10.2% to ₹ 222.6 crore with EBITDA margin expected at around 10.2% YoY factoring in impact of higher commodity prices. Adjusted PAT is expected decline 10% to ₹ 133.2 crore factoring in lower interest cost, taxes and other income in base quarter
KEC International	KEC announced new orders worth ~ ₹ 2660 crore, as on date for the quarter. For Q2FY22E, KEC is expected to report a decent performance on the revenue front in key segments like T&D, railways, civil while SAE Tower business to see muted execution amid cost overrun and commodity price impact. We expect revenues to grow 4.4% to ₹ 3401.2 crore, as base quarter was only marginally impacted by pandemic. EBITDA is expected to marginally decline 14.1% to ₹ 251.7 crore with EBITDA margin expected to see an impact of 90 bps to 7.4% YoY primarily due to change in business mix and higher commodity prices having substantial impact on SAE Tower business. Adjusted PAT is expected to de-grow 21% to ₹ 112.6 crore YoY

Source: ICICI Direct Research, Company

Exhibit 4: Company Specific Views (Capital Goods) Continued...

Company	Remarks
Larsen & Toubro (L&T)	During Q2FY22E, EPC order inflows announced by L&T are in the range of ~₹ 5000-12500 crore (as on date, ex-services segment) across water treatment, heavy engineering, hydrocarbon, buildings & factories segments indicating muted on YoY order inflows while improving QoQ amid challenging environment. We expect decent execution pick-up YoY amid a low base factoring in marginal impact on work force mobilisation and supply chain disruptions on Q2 performance due to second wave of pandemic. In our view, working capital and cash flow management will be key monitorables. Consequently, we expect adjusted standalone revenue to grow 19.6% to ₹ 18893.2 crore on a low base. EBITDA is expected to grow 27.4% to ₹ 1568.1 crore with margins expected to improve 50 bps to 8.3% owing to better execution and adjusted PAT (ex-E&A) expected to grow 28.3% to ₹ 1349 crore partly aided by lower interest expense and tax adjustments in the base quarter
NRB Bearings	NRB Bearings is expected to report a good set of numbers in Q2FY22E both YoY and QoQ, on account of a recovery in the auto segment on Covid induced lockdown in preceding quarter. We estimate revenue at ₹ 239.6 crore, up 19% QoQ and 21.2% YoY. We build in gross margins to the tune of 60.4% for the quarter vs 68.8% in Q1FY22 and 61.6% in Q2FY21. Higher steel prices will have an impact on the gross margins. Consequently, we arrive at EBIDTA margin estimate of 12.8% for the quarter vs. 13.3% in Q1FY22. Absolute EBIDTA is estimated at ₹ 30.6crore, up 12.8% QoQ. Hence, we expect NRB to register adjusted PAT of ₹ 16.8 crore
SKF India	For SKF, we see domestic and exports business doing well mainly due to easing of nationwide lockdown norms. We built in revenue to the tune of ₹ 787.2 crore, up 13.5% QoQ, 11.9& YoY. Sales for Q1FY22 were ₹ 693.5 crore. We expect industrial segment to grow 11% and automobile segment to grow about 15%. We estimate gross margins at 41.3% for the quarter, down ~410 bps QoQ, mainly due to rising steel prices and higher inventory cost. Consequently, we expect EBIDTA margin of 15.3% during the quarter vs 16.4% sequentially. Following suit, we expect EBIDTA to increase 7.6% QoQ to ₹ 120.3 crore. We estimate PAT of ₹ 84 crore vs ₹ 65 crore in Q2FY21
Thermax	For Q1FY22E, Thermax announced order inflows worth ~ ₹ 250 crore, as on date for the quarter. In terms of financial performance, we expect revenues to grow 43% to ₹ 951 crore on a low base factoring in impact of second wave of pandemic. We expect EBITDA at ₹ 66.6 crore with EBITDA margins at 7.0% factoring in pandemic and commodity price impact. Adjusted PAT is expected at ₹ 44.2 crore partly aided by tax adjustment in base quarter
Timken India	An overall good quarter for automobiles and better performing CV segment should boost Timken's Q2FY22E performance. For Q2FY22E, we expect revenue increase of 15.5% QoQ to ₹ 540 crore as ₹ 467.9 crore in Q1FY22. Revenue for the same period last year was at ₹ 392.2 crore. We build in gross margins to the tune of 42.2% vs. 44.5% in Q1FY22. Consequently, we expect EBIDTA margin at 17.8% vs. 19.8% sequentially. Absolute EBITDA is expected to be around ₹ 96.4 crore compared to ₹ 82.7 crores in the same quarter last year. We expect PAT at ₹ 59.7 crore, post a tax rate assumption of 26%
Cochin Shipyard	For Q2FY22E, we expect Cochin Shipyard to post a better set of results as operations of the company are coming back on track due to easing of lockdown norms. We build in revenue to the tune of ₹ 788.9 crore, up 16.7% YoY. Our EBIDTA margin estimate is at 20.2% vs. 19.1% YoY. Consequently, we expect absolute EBIDTA to be around ₹ 153.8 crore. Post a tax rate of 26%, we estimate PAT at ₹ 127.9 crore, up ~18% compared to the same quarter last year
IEX	High electricity demand during the quarter helped IEX to report total volume of 25856 million units vs. 21340 million units, growth of 21.1%. We expect IEX to report revenue of ₹ 106.4 crore, up 51%, 16.9% YoY, QoQ, respectively, subsequently. For the quarter, we expect IEX to report an EBIDTA of ₹ 88.5 crore with a margin of 83.2% vs. 78.2% YoY and 82.2% QoQ. We estimate PAT at ₹ 71.7 crore, up 61.7% YoY and 15.5% QoQ

Source: Company, ICICI Direct Research

Exhibit 6: ICICI Direct coverage universe (Capital Goods)

Company	CMP			M Cap	EPS (₹)			P/E (x)			RoCE (%)			RoE (%)		
	(₹)	TP(₹)	Rating	(₹ Cr)	FY21	FY22E	FY23E	FY21	FY22E	FY23E	FY21	FY22E	FY23E	FY21	FY22E	FY23E
L&T (LARTOU)	1729	1,870	Buy	242613	81.9	46.7	52.9	21.1	37.1	32.7	7.4	8.0	8.8	18.8	10.2	11.0
Siemens Ltd	2228	2,550	Buy	79344	28.3	37.9	45.1	78.8	58.8	49.4	13.5	16.3	17.4	9.9	12.1	13.0
AIA Engineering (AIAENG)	1869	2,230	Buy	17629	59.7	60.4	69.7	31.3	30.9	26.8	16.4	15.3	16.1	13.3	12.4	12.9
Thermax (THERMA)	1400	1,680	Buy	16682	17.3	26.8	40.0	80.8	52.2	35.0	9.8	11.9	16.3	7.6	9.3	12.7
Kalpataru Power(KALPOW)	408	550	Buy	6312	41.3	33.9	42.0	9.9	12.0	9.7	15.9	16.6	17.6	12.7	11.5	12.7
KEC International (KECIN)	463	485	Buy	11904	21.5	23.3	32.2	21.5	19.8	14.4	19.4	18.3	20.9	16.5	15.9	18.3
Greaves Cotton (GREAVE)	139	190	Buy	3214	0.4	3.6	6.1	310.2	38.9	22.7	6.5	12.0	20.1	3.3	8.7	14.7
Elgi Equipment (ELGEQU)	202	260	Buy	6402	3.2	3.9	6.2	62.5	51.5	32.8	11.7	12.8	18.1	11.8	13.9	18.7
Bharat Electronics (BHAELE)	200	250	Buy	48732	8.5	9.6	11.3	23.6	20.8	17.7	27.2	27.0	28.7	19.1	19.9	21.4
Cochin Shipyard (COCSHI)	361	500	Buy	4720	46.4	44.0	55.6	7.8	8.2	6.5	14.4	15.2	16.0	15.3	13.0	14.7
SKF (SKFIND)	3300	3,300	Buy	16310	60.2	72.0	94.0	54.8	45.8	35.1	24.8	25.0	28.0	19.0	19.0	21.0
Timken India (TIMIND)	1702	1,740	Hold	12800	19.0	28.2	36.3	89.4	60.4	46.9	13.7	18.3	23.5	10.7	14.0	18.0
NRB Bearing (NRBBEA)	143	175	Buy	1280	5.6	8.0	9.8	25.5	17.9	14.6	11.8	15.8	17.2	10.4	13.1	14.1
Action Construction (ACTCON)	267	300	Buy	3170	7.1	9.4	13.7	37.6	28.4	19.5	26.9	25.8	30.7	15.3	17.1	20.3

Source: Company, ICICI Direct Research

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Sell: <-15%

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