

**HOLD**

TP: Rs 4,400 | ▼ 3%

**ABB INDIA**

| Capital Goods

| 11 August 2023

### Strong quarter, margins shine

- **Robust Q2 with revenue up 22% YoY and 420bps EBITDA margin expansion aided by the robotics and electrification segments**
- **Base order inflows grew 4% YoY despite a high comparable quarter; strong traction expected given customers' large investment lineup**
- **CY23/CY24 EPS raised 17% each and TP increased to Rs 4,400 (vs. Rs 3,700) on rollover; maintain HOLD**

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**Robust quarter:** ABB reported a robust Q2CY23 (Y/E Dec) backed by a favourable product mix, efficient supply chain management and better pricing power. Revenue increased 22% YoY to Rs 25.1bn led by growth of 154% in robotics (to Rs 1.2bn), 10% in the motion division (Rs 9.2bn), 20% in electrification (Rs 10bn), and 38% in industrial automation (Rs 5.1bn). Gross and EBITDA margins expanded 30bps and 420bps YoY to 36.5% and 13.9% respectively on the back of lower metal prices, better operating leverage and higher capacity utilisation. ABB has maintained a strong gross margin trend of over 36% in the last five quarters.

**Strong outlook continues:** Order inflows stood at Rs 30.4bn, advancing 10% YoY in Q2CY23 and taking ABB's order backlog to Rs 77.3bn. Base orders grew 4% YoY despite a high comparable last year. We note that management had earlier guided for 12-15% growth in order inflows for the year (from Rs 86bn in CY22) as many end-user segments are witnessing an upcycle in investments, along with ~Rs 23bn of base orders every quarter. For CY23, management had guided for revenue of Rs 100bn, gross margin of 35-37%, and PAT margin of 10%, which looks achievable given the strong H1CY23 performance.

**Focus on short-cycle orders aiding margins and cash flows:** The short-cycle business has been performing well across segments, posting significant revenue growth of 22% YoY in Q2. This is both lifting margins and shoring up the cash balance. ABB's current cash balance stands at Rs 40.9bn vs. Rs 39.4bn in the previous quarter, some of which is earmarked for potential acquisition targets, both global and local. This includes investments towards digitalisation (for partnerships that enhance the core portfolio and drive value-add for customers) as well as growth in energy and energy-efficiency sectors.

**Maintain HOLD:** We raise our CY23/CY24 EPS estimates by 17% each post H1, given the strong margins and higher confidence of sustainability. We continue to value the stock at 70x P/E – in line with the 5Y mean – and roll valuations forward to Jun'25E. Along with estimate revision, this yields a higher TP of Rs 4,400 (vs. Rs 3,700). Positives appear priced in at current valuations and hence we retain HOLD.

### Key changes

Target	Rating
▲	◀ ▶

Ticker/Price	ABB IN/Rs 4,527
Market cap	US\$ 11.7bn
Free float	25%
3M ADV	US\$ 14.4mn
52wk high/low	Rs 4,614/Rs 2,640
Promoter/FPI/DII	75%/4%/9%

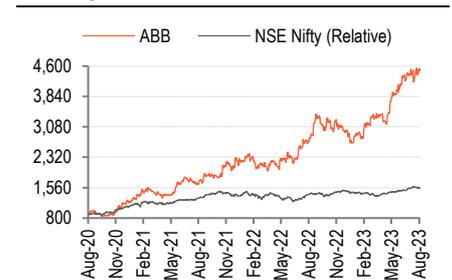
Source: NSE | Price as of 11 Aug 2023

### Key financials

Y/E 31 Dec	CY22A	CY23E	CY24E
Total revenue (Rs mn)	85,675	1,04,522	1,27,355
EBITDA (Rs mn)	9,619	13,457	16,650
Adj. net profit (Rs mn)	6,864	10,671	13,100
Adj. EPS (Rs)	32.4	50.4	61.8
Consensus EPS (Rs)	32.4	47.5	55.7
Adj. ROAE (%)	15.3	20.0	20.6
Adj. P/E (x)	139.8	89.9	73.2
EV/EBITDA (x)	99.7	71.3	57.6
Adj. EPS growth (%)	54.8	55.5	22.8

Source: Company, Bloomberg, BOBCAPS Research

### Stock performance



Source: NSE

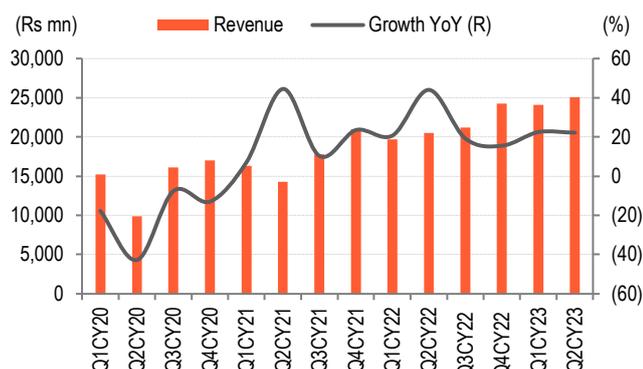


**Fig 1 – Quarterly performance**

Particulars (Rs mn)	Q2CY23	Q2CY22	YoY (%)	Q1CY23	QoQ (%)	H1CY23	H1CY22	YoY (%)
Revenue	25,086	20,525	22.2	24,112	4.0	49,198	40,209	22.4
EBITDA	3,487	1,988	75.4	2,853	22.2	6,340	3,866	64.0
EBITDAM (%)	13.9	9.7	422bps	11.8	207	12.9	9.6	327bps
Depreciation	292	253		275		567	510	
Interest	14	28		22		36	43	
Other Income	750	253		723		1,473	626	
PBT	3,931	1,959	100.7	3,279	19.9	7,210	3,939	83.0
Tax	973	489		827		1,800	1,701	
Adjusted PAT	2,958	1,471	101.1	2,452	20.7	5,410	2,239	141.7
Exceptional item								
Reported PAT	2,958	1,471	101.1	2,452	20.7	5,410	2,238.5	141.7
Adj. PATM (%)	11.8	7.2	463bps	10.2	162	11.0	5.6	543bps
EPS (Rs)	14.0	6.9	101.1	11.6	20.7	25.5	10.6	141.7

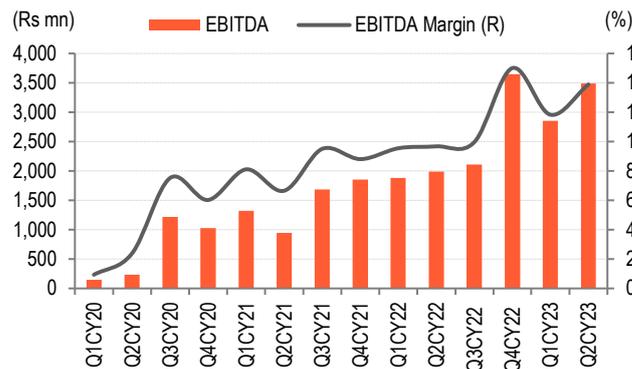
Source: Company, BOBCAPS Research

**Fig 2 – Revenue growth trend**



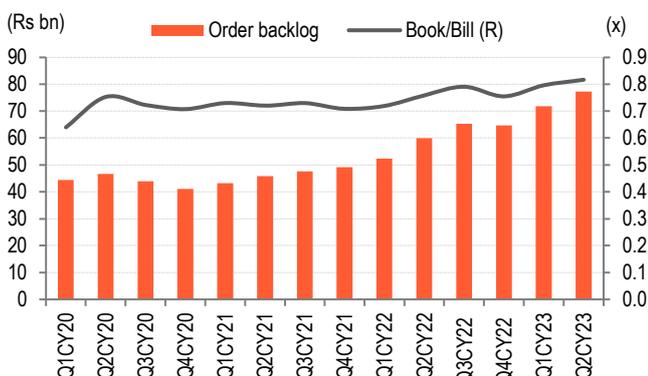
Source: Company, BOBCAPS Research

**Fig 3 – EBITDA growth trend**



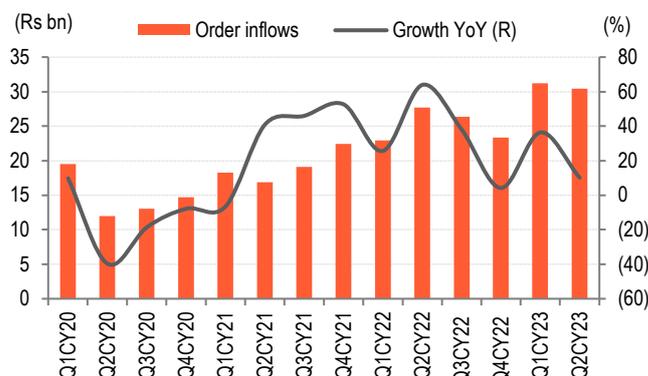
Source: Company, BOBCAPS Research

**Fig 4 – Order backlog trend**



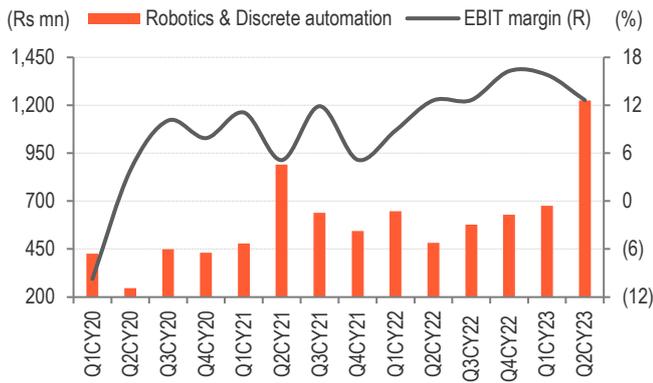
Source: Company, BOBCAPS Research

**Fig 5 – Order inflow trend**



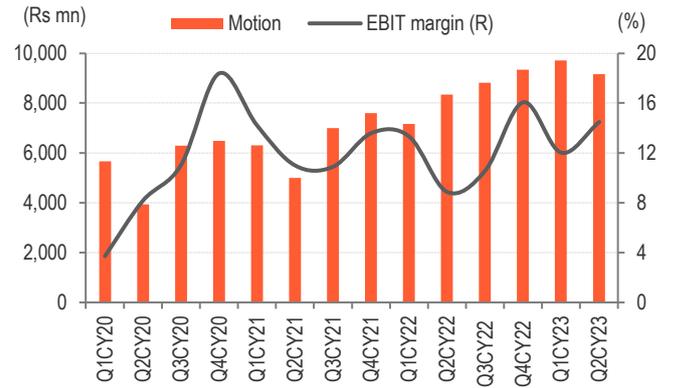
Source: Company, BOBCAPS Research

**Fig 6 – Robotics & discrete automation performance**



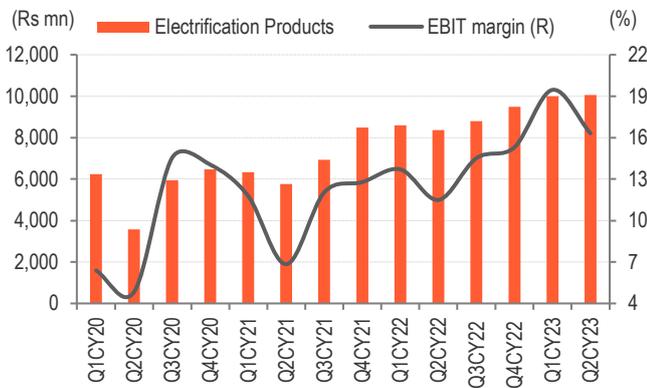
Source: Company, BOBCAPS Research

**Fig 7 – Motion business performance**



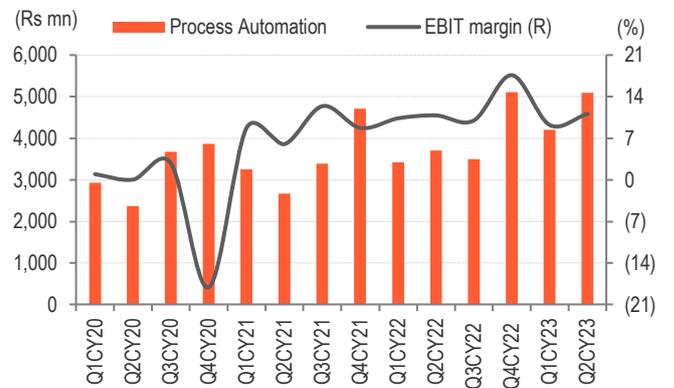
Source: Company, BOBCAPS Research

**Fig 8 – Electrification business performance**



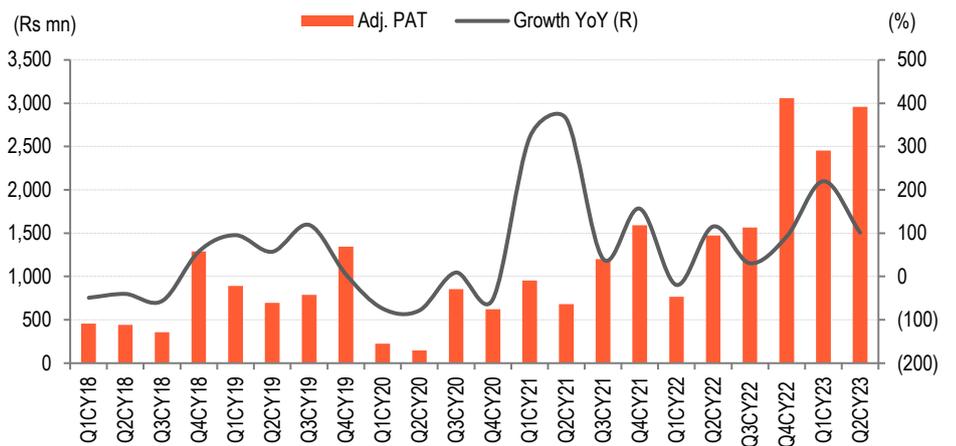
Source: Company, BOBCAPS Research

**Fig 9 – Process Automation performance**



Source: Company, BOBCAPS Research

**Fig 10 – Profit trend**



Source: Company, BOBCAPS Research

## Earnings call highlights

- **Margins:** ABB's gross margin has exceeded the 36% mark over the last five quarters to Q2CY23 when it clocked 30bps YoY expansion to 36.5%. Management is confident of sustaining margins as commodity prices have corrected, but cautioned that any unforeseen movement in commodities or foreign exchange rates could impact profitability. Q2 EBITDA margin expanded 420bps YoY to 13.9% as operating leverage kicked in on the back of higher volumes and better capacity utilisation, coupled with a stronger product mix and improved pricing power.
- **Outlook:** Order inflow was healthy at Rs 30.4bn during the quarter, taking ABB's order backlog to Rs 77.3bn. The company indicated that its customers have large investments lined up that will increase order visibility over the next few years. Management is optimistic on order execution as well as margin sustainability, but indicated that unforeseen volatility in metal prices may impact the profitability of segments such as motion and electrification which also have short-cycle orders.
- **Competition:** Many global players are now looking to set up capacities in India, but ABB does not view this as a concern given the fast-growing Indian market and the company's longstanding relations with its customers.
- **Cash:** Cash balance as of Q2 was at Rs 40.9bn which management expects to gradually deploy into organic and inorganic growth drivers over the next few years. ABB declared a special dividend of Rs 5.5/sh during the quarter.

### Electrification

- The electrification segment grew 20% YoY with a topline of Rs 10bn on the back of better supply chain management, execution visibility and higher demand for low-voltage components.
- Segmental EBIT margin expanded 480bps YoY to 16.3% due to higher capacity utilisation, better price realisation on account of stronger pricing power, and a favourable product mix.
- Order inflows stood at Rs 11bn, growing 15% YoY, motivated by traction in distribution solutions as the company has expanded its granularity in product specifications catering to the lucrative demand sectors of data centres and medium-voltage systems.

### Motion

- EBIT margin in the motion business expanded 560bps YoY to 14.5% on the back of higher volumes. The company has been able to structurally increase margins in this segment over the last three quarters, excluding a one-time warranty provision cost taken in Q1CY23.
- Order inflows increased to Rs 11.2bn, growing 8% YoY led by higher demand in the traction converter segment and higher penetration in tier-2 and 3 cities.

**Process automation**

- Process automation revenue grew 38% YoY to Rs 5.1bn as order execution progressed.
- EBIT margin expanded 30bps YoY to 11.1% due to a higher contribution from services and process efficiencies.
- Orders increased 10% YoY to Rs 7.8bn from various industries such as metals, cement and energy.

**Key orders received during Q1**

- Reliable power and automation solutions for smelter and roll products for an aluminium major
- Energy-efficient drives for a leading manufacturer of industrial and medical gases
- Traction motors for a railway transportation multinational company
- Blending solutions for a Japanese engineering, procurement company for the energy space
- Motion solutions comprising drives and synchronous reluctance motors for a heavy electricals major
- Different solutions for the biggest data centre majors in the country
- Robotics paint and body-in-white orders for automotive majors and copper and aluminum majors
- Distribution solutions package for a branded goods company

## Valuation methodology

ABB's performance has improved significantly in the last few quarters, and management commentary points to strong momentum going forward. We raise our CY23/CY24 EPS estimates by 17% each post H1CY23, given the strong margins and higher confidence of sustainability.

We continue to value the stock at 70x P/E – in line with the five-year mean – and roll valuations forward to Jun'25E. Along with estimate revision, this yields a higher TP of Rs 4,400 (vs. Rs 3,700). However, positives appear priced in at current valuations and hence we retain our HOLD rating.

**Fig 11 – Revised estimates**

Particulars (Rs mn)	New		Old		Change (%)	
	CY23E	CY24E	CY23E	CY24E	CY23E	CY24E
Sales	1,04,522	1,27,355	1,04,522	1,27,355	0.0	0.0
EBITDA	13,457	16,650	11,367	14,102	18.4	18.1
PAT	10,671	13,100	9,108	11,195	17.2	17.0
EPS (Rs)	50.4	61.8	43.0	52.8	17.2	17.0
EBITDA Margin (%)	12.9	13.1	10.9	11.1	200.0	200.0

Source: Company, BOBCAPS Research

## Key risks

Key upside risks to our estimates are:

- sustained momentum in short-cycle orders, translating into higher order wins, and
- above-anticipated margin expansion due to a surge in exports and services.

Key downside risks to our estimates are:

- aggressive pricing strategy by peers,
- inability to scale up the motion segment further, and
- increase in royalty to the parent.

## Sector recommendation snapshot

Company	Ticker	Market Cap (US\$ bn)	Price (Rs)	Target (Rs)	Rating
ABB India	ABB IN	11.7	4,527	4,400	HOLD
AIA Engineering	AIAE IN	4.1	3,601	4,000	BUY
Cummins India	KKC IN	5.9	1,739	2,110	BUY
Hitachi Energy	POWERIND IN	2.3	4,411	4,400	HOLD
KEC International	KECI IN	2.0	623	630	HOLD
Larsen & Toubro	LT IN	45.1	2,639	3,000	BUY
Siemens India	SIEM IN	15.8	3,653	3,900	HOLD
Thermax	TMX IN	3.7	2,545	2,600	HOLD

Source: BOBCAPS Research, NSE | Price as of 11 Aug 2023

## Financials

### Income Statement

Y/E 31 Dec (Rs mn)	CY20A	CY21A	CY22A	CY23E	CY24E
<b>Total revenue</b>	<b>58,210</b>	<b>69,340</b>	<b>85,675</b>	<b>1,04,522</b>	<b>1,27,355</b>
EBITDA	2,712	5,567	9,619	13,457	16,650
Depreciation	1,204	1,027	1,047	1,213	1,266
EBIT	1,508	4,540	8,572	12,244	15,383
Net interest inc./(exp.)	169	107	131	131	131
Other inc./(exp.)	1,116	1,596	1,795	2,154	2,261
Exceptional items	0	0	0	0	0
EBT	2,456	6,029	10,235	14,267	17,514
Income taxes	597	1,597	3,372	3,595	4,413
Extraordinary items	(445)	(892)	(3,393)	0	0
Min. int./Inc. from assoc.	0	0	0	0	0
<b>Reported net profit</b>	<b>2,304</b>	<b>5,325</b>	<b>10,256</b>	<b>10,671</b>	<b>13,100</b>
Adjustments	(445)	(892)	(3,393)	0	0
<b>Adjusted net profit</b>	<b>1,859</b>	<b>4,433</b>	<b>6,864</b>	<b>10,671</b>	<b>13,100</b>

### Balance Sheet

Y/E 31 Dec (Rs mn)	CY20A	CY21A	CY22A	CY23E	CY24E
Accounts payables	17,207	19,613	26,368	28,636	34,892
Other current liabilities	21,999	20,244	17,015	20,758	25,293
Provisions	0	0	0	0	0
Debt funds	133	181	121	0	0
Other liabilities	502	238	285	285	285
Equity capital	424	424	424	424	424
Reserves & surplus	35,640	40,028	48,970	57,162	68,885
Shareholders' fund	36,064	40,452	49,394	57,586	69,309
<b>Total liab. and equities</b>	<b>75,905</b>	<b>80,727</b>	<b>93,182</b>	<b>1,07,266</b>	<b>1,29,778</b>
Cash and cash eq.	22,066	26,877	36,422	31,289	39,670
Accounts receivables	16,950	16,950	20,930	25,534	31,112
Inventories	8,408	10,091	14,207	17,332	21,118
Other current assets	13,413	12,436	7,427	18,674	22,753
Investments	0	0	0	0	0
Net fixed assets	6,938	8,170	8,992	9,379	9,912
CWIP	749	769	693	845	1,029
Intangible assets	0	0	0	0	0
Deferred tax assets, net	0	0	0	0	0
Other assets	7,382	5,435	4,512	4,213	4,184
<b>Total assets</b>	<b>75,905</b>	<b>80,727</b>	<b>93,182</b>	<b>1,07,266</b>	<b>1,29,778</b>

### Cash Flows

Y/E 31 Dec (Rs mn)	CY20A	CY21A	CY22A	CY23E	CY24E
<b>Cash flow from operations</b>	<b>3,182</b>	<b>6,492</b>	<b>7,419</b>	<b>(1,080)</b>	<b>11,713</b>
Capital expenditures	(1,137)	(1,358)	(1,479)	(1,600)	(1,800)
Change in investments	0	(19,670)	18,399	(152)	(185)
Other investing cash flows	5,561	950	1,342	299	29
<b>Cash flow from investing</b>	<b>4,424</b>	<b>(20,079)</b>	<b>18,262</b>	<b>(1,454)</b>	<b>(1,955)</b>
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	(337)	(124)	(300)	(121)	0
Interest expenses	0	0	0	0	0
Dividends paid	0	0	0	0	0
Other financing cash flows	(1,186)	(1,144)	(1,102)	(2,479)	(1,377)
<b>Cash flow from financing</b>	<b>(1,523)</b>	<b>(1,268)</b>	<b>(1,402)</b>	<b>(2,600)</b>	<b>(1,377)</b>
<b>Chg in cash &amp; cash eq.</b>	<b>6,084</b>	<b>(14,855)</b>	<b>24,280</b>	<b>(5,133)</b>	<b>8,381</b>
<b>Closing cash &amp; cash eq.</b>	<b>22,066</b>	<b>26,877</b>	<b>36,422</b>	<b>31,289</b>	<b>39,670</b>

### Per Share

Y/E 31 Dec (Rs)	CY20A	CY21A	CY22A	CY23E	CY24E
Reported EPS	10.9	25.1	48.4	50.4	61.8
Adjusted EPS	8.8	20.9	32.4	50.4	61.8
Dividend per share	4.8	5.2	5.2	11.7	6.5
Book value per share	170.2	190.9	233.1	271.8	327.1

### Valuations Ratios

Y/E 31 Dec (x)	CY20A	CY21A	CY22A	CY23E	CY24E
EV/Sales	16.5	13.8	11.2	9.2	7.5
EV/EBITDA	353.7	172.3	99.7	71.3	57.6
Adjusted P/E	515.9	216.4	139.8	89.9	73.2
P/BV	26.6	23.7	19.4	16.7	13.8

### DuPont Analysis

Y/E 31 Dec (%)	CY20A	CY21A	CY22A	CY23E	CY24E
Tax burden (Net profit/PBT)	75.7	73.5	67.1	74.8	74.8
Interest burden (PBT/EBIT)	162.8	132.8	119.4	116.5	113.8
EBIT margin (EBIT/Revenue)	2.6	6.5	10.0	11.7	12.1
Asset turnover (Rev./Avg TA)	76.1	88.5	98.5	104.3	107.5
Leverage (Avg TA/Avg Equity)	2.1	2.0	1.9	1.9	1.9
Adjusted ROAE	5.2	11.6	15.3	20.0	20.6

### Ratio Analysis

Y/E 31 Dec	CY20A	CY21A	CY22A	CY23E	CY24E
<b>YoY growth (%)</b>					
Revenue	(20.4)	19.1	23.6	22.0	21.8
EBITDA	(48.9)	105.3	72.8	39.9	23.7
Adjusted EPS	(50.0)	138.4	54.8	55.5	22.8
<b>Profitability &amp; Return ratios (%)</b>					
EBITDA margin	4.7	8.0	11.2	12.9	13.1
EBIT margin	2.6	6.5	10.0	11.7	12.1
Adjusted profit margin	3.2	6.4	8.0	10.2	10.3
Adjusted ROAE	5.2	11.6	15.3	20.0	20.6
ROCE	0.0	0.0	0.0	0.0	0.0
<b>Working capital days (days)</b>					
Receivables	106	89	89	89	89
Inventory	53	53	61	61	61
Payables	108	103	112	100	100
<b>Ratios (x)</b>					
Gross asset turnover	5.5	6.1	6.4	6.9	7.6
Current ratio	1.5	1.7	1.8	1.9	1.9
Net interest coverage ratio	8.9	42.4	65.4	93.4	117.3
Adjusted debt/equity	(0.6)	(0.7)	(0.7)	(0.5)	(0.6)

Source: Company, BOBCAPS Research | Note: TA = Total Assets

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**BUY** – Expected return >+15%

**HOLD** – Expected return from -6% to +15%

**SELL** – Expected return <-6%

**Note:** Recommendation structure changed with effect from 21 June 2021

Our recommendation scale does not factor in short-term stock price volatility related to market fluctuations. Thus, our recommendations may not always be strictly in line with the recommendation scale as shown above.

### Ratings and Target Price (3-year history): ABB INDIA (ABB IN)



B – Buy, H – Hold, S – Sell, A – Add, R – Reduce

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