

HOLD

TP: Rs 4,200 | ▼ 5%

HITACHI ENERGY

| Capital Goods

| 06 November 2023

Chip constraints receding

- Q2 EBITDA margin rose sequentially to 5.3% as chip constraints eased but PAT still down 33% YoY
- Management now expects double-digit margins only by end-FY25 led by domestic projects (HVDC, rail) and improving exports
- We cut FY24/FY25 EPS by 15%/12% following a subpar H1, yielding a new TP of Rs 4,200 (vs. Rs 4,400); retain HOLD

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Sequentially better numbers: Hitachi Energy's (Hitachi) Q2FY24 revenue grew 18% QoQ (+10% YoY) to Rs 12.3bn and the easing chip shortage aided a 210bps sequential improvement in EBITDA margin to 5.3% (albeit with a contraction of 150bps YoY). PAT came in at Rs 247mn compared to Rs 24mn last quarter, though this is still 33% lower on a YoY basis.

Chip constraints reduce: Hitachi has been plagued by chip shortages during the past few quarters and estimates that this caused a revenue loss of Rs 680mn in Q1FY24 and Rs 500mn in Q4FY23. Management indicated that supply chain constraints have receded in Q2 and will continue to normalise going forward.

Order inflow strong: Q2 order intake soared 52% YoY to Rs 17.5bn with a 25% export share, taking the backlog to Rs 75.9bn which signifies 22 months of revenue visibility. This compares well with the Rs 70.2bn backlog in Q1FY24 and Rs 70.7bn in FY23. Transmission projects from multiple utilities, especially related to the new green energy corridors, along with renewable orders propelled the strong growth.

Outlook remains positive: Management sees high-voltage direct current (HVDC) lines as a big domestic opportunity, with potential for at least one Rs 80bn-100bn tender to be floated every year, half of which would constitute Hitachi's addressable market. In railways, opportunities continue in high-speed rail, locomotives and trainsets. From an open-ended timeframe of FY25 earlier, management now expects to reach a double-digit EBITDA margin run-rate only by the close of that fiscal.

Retain HOLD: We remain positive on Hitachi's order flow prospects but cut our FY24/FY25 EPS estimates by 15%/12% to reflect the below-expected H1FY24 performance. Upon rolling valuations forward to Sep'25E, our TP reduces to Rs 4,200 (vs. Rs 4,400) based on an unchanged 45x P/E multiple. The stock price has remained flat since our last quarterly update of 25 Jul 2023 when we had downgraded our rating from BUY to HOLD – we maintain our stance and await a better entry point.

Key changes

Target	Rating
▼	◀ ▶

Ticker/Price	POWERIND IN/Rs 4,405
Market cap	US\$ 2.3bn
Free float	25%
3M ADV	US\$ 1.6mn
52wk high/low	Rs 4,800/Rs 2,840
Promoter/FPI/DII	75%/5%/2%

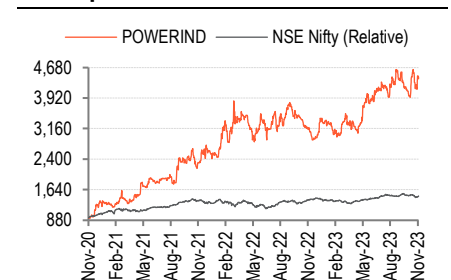
Source: NSE | Price as of 6 Nov 2023

Key financials

Y/E 31 Mar	FY23A	FY24E	FY25E
Total revenue (Rs mn)	44,685	56,851	66,149
EBITDA (Rs mn)	2,359	4,013	5,967
Adj. net profit (Rs mn)	939	2,094	3,541
Adj. EPS (Rs)	22.2	49.4	83.5
Consensus EPS (Rs)	22.2	58.0	95.0
Adj. ROAE (%)	8.0	16.0	22.4
Adj. P/E (x)	198.8	89.2	52.7
EV/EBITDA (x)	79.0	46.2	31.4
Adj. EPS growth (%)	(44.0)	123.0	69.1

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE



Fig 1 – Quarterly performance

Particulars (Rs mn)	Q2FY24	Q2FY23	YoY (%)	Q1FY24	QoQ (%)	H1FY24	H1FY23	YoY (%)
Revenue	12,280	11,146	10.2	10,401	18.1	22,680	21,006	8.0
EBITDA	653	758	(13.8)	337	94.0	990	1,014	(2.4)
EBITDA Margin (%)	5.3	6.8	(150bps)	3.2	210bps	4.4	4.8	(50bps)
Depreciation	225	184		223		448	389	
Interest	107	75		110		216	158	
Other Income	2	4		29		32	57	
PBT	324	502	(35.6)	34	857.7	358	523	(31.7)
Tax	76	131		10		86	138	
Adjusted PAT	247	372	(33.4)	24	926.6	272	385	(29.5)
Exceptional item	0	0		0		0	0	
Reported PAT	247	372	(33.4)	24	926.6	272	385	(29.5)
Adj. PAT Margin (%)	2.0	3.3	(130bps)	0.2	180bps	1.2	1.8	(60bps)
EPS (Rs)	5.8	8.8	(33.4)	0.6	926.6	6.4	9.1	(29.5)

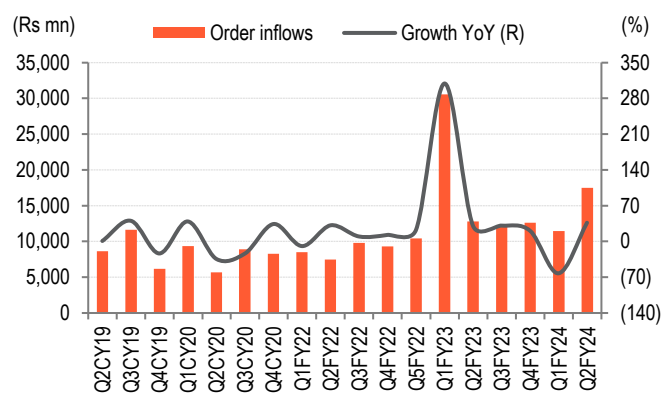
Source: Company, BOBCAPS Research

Fig 2 – Order backlog



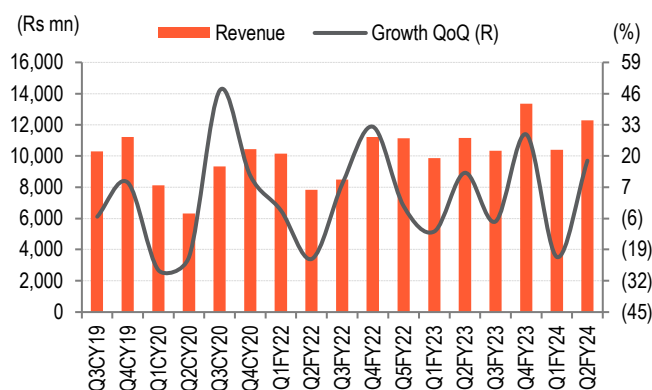
Source: Company, BOBCAPS Research

Fig 3 – Order inflow



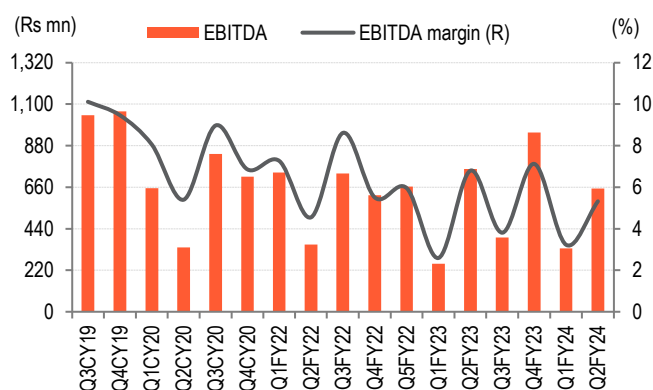
Source: Company, BOBCAPS Research

Fig 4 – Revenue growth



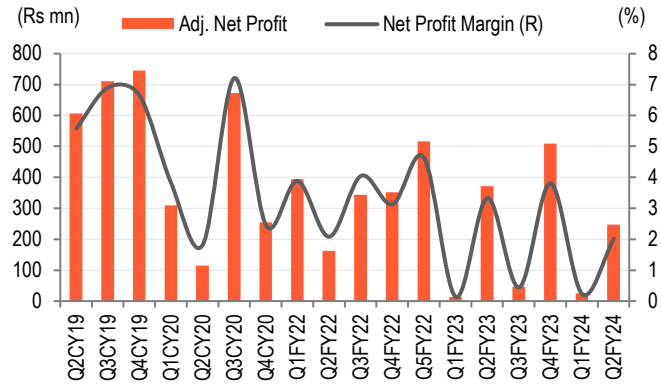
Source: Company, BOBCAPS Research

Fig 5 – EBITDA growth



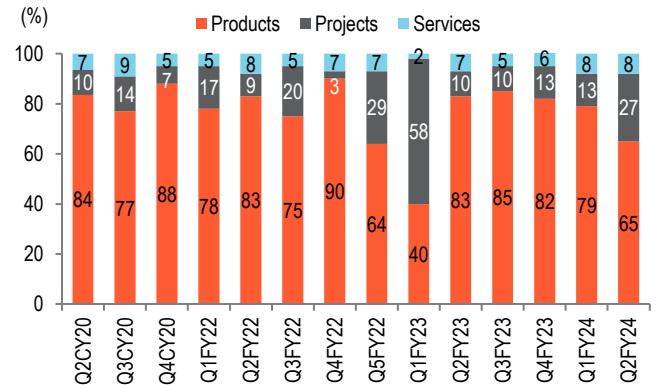
Source: Company, BOBCAPS Research

Fig 6 – Net profit growth



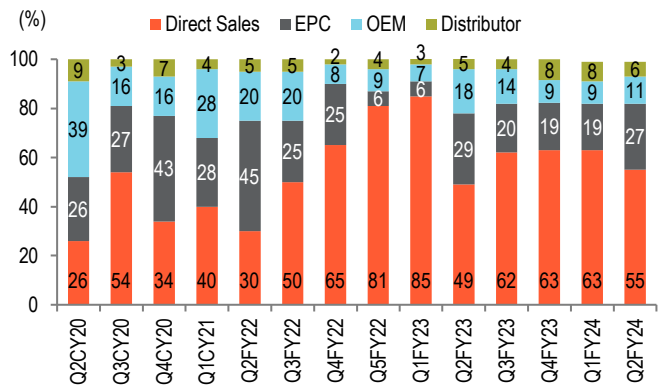
Source: Company, BOBCAPS Research

Fig 7 – Order inflows by segment



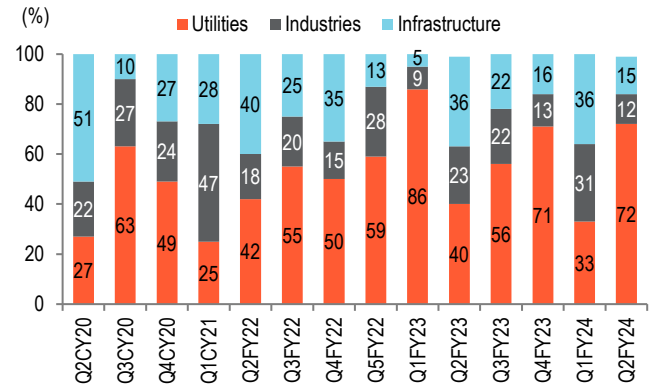
Source: Company, BOBCAPS Research

Fig 8 – Order inflows by channel



Source: Company, BOBCAPS Research

Fig 9 – Order inflows by sector



Source: Company, BOBCAPS Research

Earnings call highlights

- **Project milestones:** During Q2FY24, Hitachi commissioned a 220/33kV substation for one of the world's largest web service providers, completed a test trial run of the Indore metro with a 750V DC third rail, and is on track to commission a 220/33kV gas insulated switchgear substation (GIS S/S) at Gedu, Bhutan.
- **Potential orders:** After racking up Rs 17.5bn in order flows during Q2, Hitachi is eyeing a large order stemming from India's energy transition – this includes two 300MVAr STATCOM systems for renewable evacuation and integration in Fatehgarh, Rajasthan, along with two 400kV air-insulated switchgear (AIS) extension bays.
- **Export orders:** Export orders grew 45% YoY in Q2 and include a 66/33/11kV GIS S/S for Bhutan Power, AIS switchgears for PLN Indonesia, a 132kV harmonic filter for UAE Transco, and the company's largest single order for the supply of a disconnecter from Kalpataru Power for a Guyana project.
- **Key segments:** Hitachi's transmission segment grew 139% YoY in H1FY24 mainly driven by the breakthrough STATCOM order. Power quality grew 59% and data centres grew 28%, while the railways and metros segment declined 3% in H1.
- **Profitability:** Management indicated that the semiconductor crunch is easing but inventory backlog issues persist, prompting it to move its double-digit EBITDA margin guidance from FY25 earlier to the end of that fiscal. The company expects better margins as raw material prices and chip constraints recede, alongside higher exports and a larger share of fast-growing segments, such as HVDC.
- **Strategy:** Management reiterated its strategy of maintaining leadership in its core segments and boosting orders in services, exports and the digital space. Localisation is another important strategy.
- **Capex:** Management maintained capex guidance at Rs 1bn each for FY24 and FY25. The company has commissioned its HVDC and power quality factory in Chennai that will manufacture advanced power electronics for products such as HVDC Light, HVDC Classic, and STATCOM, together with MACH Control and protection systems. These technologies are key for growth in the transmission business, especially for the integration of renewables and electrical grid stability.

Valuation methodology

We remain positive on Hitachi's order flow prospects but cut our FY24/FY25 EPS estimates by 15%/12% to reflect the below-expected H1FY24 performance. We also introduce FY26 forecasts in this note. Upon rolling valuations forward to Sep'25E, our TP reduces to Rs 4,200 (vs. Rs 4,400) based on an unchanged 45x P/E multiple.

The stock price has remained flat since our last quarterly update of 25 Jul 2023 when we had downgraded our rating from BUY to HOLD – we maintain our stance and await a better entry point.

Fig 10 – Revised estimates

Particulars (Rs mn)	New		Old		Change (%)	
	FY24E	FY25E	FY24E	FY25E	FY24E	FY25E
Sales	56,851	66,149	56,851	66,149	0.0	0.0
EBITDA	4,013	5,967	4,525	6,628	(11.3)	(10.0)
PAT	2,094	3,541	2,477	4,036	(15.5)	(12.3)
EPS (Rs)	49.4	83.5	58.4	95.2	(15.5)	(12.3)
EBITDA Margin (%)	7.1	9.0	8.0	10.0	(90bps)	(100bps)

Source: Company, BOBCAPS Research

Key risks

Key upside risks to our estimates are:

- faster recovery in T&D capex than estimated, and
- speedy resolution of the chip shortage.

Key downside risks are:

- slowdown in T&D capex,
- increase in commodity prices, and
- higher royalty to parent.

Sector recommendation snapshot

Company	Ticker	Market Cap (US\$ bn)	Price (Rs)	Target (Rs)	Rating
ABB India	ABB IN	10.8	4,204	4,400	HOLD
AIA Engineering	AIAE IN	4.2	3,637	4,200	BUY
Cummins India	KKC IN	5.8	1,725	2,110	BUY
Hitachi Energy	POWERIND IN	2.3	4,405	4,200	HOLD
KEC International	KECI IN	1.8	582	670	HOLD
Larsen & Toubro	LT IN	50.9	2,975	3,500	BUY
Siemens India	SIEM IN	14.6	3,367	3,900	HOLD
Thermax	TMX IN	4.2	2,895	3,000	HOLD

Source: BOBCAPS Research, NSE | Price as of 6 Nov 2023

Financials

Income Statement

Y/E 31 Mar (Rs mn)	FY22A	FY23A	FY24E	FY25E	FY26E
Total revenue	48,840	44,685	56,851	66,149	73,716
EBITDA	3,107	2,359	4,013	5,967	6,946
Depreciation	955	802	931	943	954
EBIT	2,152	1,558	3,082	5,023	5,992
Net interest inc./(exp.)	414	401	450	475	475
Other inc./(exp.)	669	151	167	183	202
Exceptional items	0	0	0	0	0
EBT	2,407	1,308	2,798	4,732	5,719
Income taxes	732	369	704	1,191	1,439
Extraordinary items	(359)	0	0	0	0
Min. int./Inc. from assoc.	0	0	0	0	0
Reported net profit	2,034	939	2,094	3,541	4,279
Adjustments	(359)	0	0	0	0
Adjusted net profit	1,676	939	2,094	3,541	4,279

Balance Sheet

Y/E 31 Mar (Rs mn)	FY22A	FY23A	FY24E	FY25E	FY26E
Accounts payables	16,190	15,146	18,691	20,842	23,226
Other current liabilities	5,915	8,648	12,460	14,498	16,157
Provisions	0	0	0	0	0
Debt funds	1,250	2,750	3,499	4,071	4,537
Other liabilities	560	488	621	723	805
Equity capital	85	85	85	85	85
Reserves & surplus	11,239	12,068	14,014	17,385	21,495
Shareholders' fund	11,324	12,153	14,099	17,470	21,580
Total liab. and equities	35,239	39,185	49,370	57,603	66,304
Cash and cash eq.	859	1,633	4,192	7,248	11,095
Accounts receivables	13,438	15,278	22,585	26,278	29,284
Inventories	7,073	8,179	7,009	7,249	8,078
Other current assets	5,443	5,629	7,009	8,155	9,088
Investments	0	0	0	0	0
Net fixed assets	6,525	7,133	7,202	7,259	7,305
CWIP	1,183	487	487	487	487
Intangible assets	0	0	0	0	0
Deferred tax assets, net	0	0	0	0	0
Other assets	717	847	887	927	967
Total assets	35,239	39,185	49,370	57,603	66,304

Cash Flows

Y/E 31 Mar (Rs mn)	FY22A	FY23A	FY24E	FY25E	FY26E
Cash flow from operations	(1,267)	54	2,866	3,592	4,508
Capital expenditures	(1,675)	(120)	(1,000)	(1,000)	(1,000)
Change in investments	0	0	0	0	0
Other investing cash flows	5	2	93	62	43
Cash flow from investing	(1,670)	(118)	(907)	(938)	(957)
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	1,250	1,500	749	572	466
Interest expenses	0	0	0	0	0
Dividends paid	0	0	0	0	0
Other financing cash flows	(644)	(663)	(148)	(170)	(170)
Cash flow from financing	606	837	600	403	296
Chg in cash & cash eq.	(2,331)	773	2,559	3,057	3,847
Closing cash & cash eq.	859	1,633	4,192	7,248	11,095

Per Share

Y/E 31 Mar (Rs)	FY22A	FY23A	FY24E	FY25E	FY26E
Reported EPS	48.0	22.2	49.4	83.5	101.0
Adjusted EPS	39.5	22.2	49.4	83.5	101.0
Dividend per share	3.0	3.4	3.5	4.0	4.0
Book value per share	267.2	286.8	332.7	412.2	509.2

Valuations Ratios

Y/E 31 Mar (x)	FY22A	FY23A	FY24E	FY25E	FY26E
EV/Sales	3.9	4.2	3.3	2.8	2.6
EV/EBITDA	61.1	79.0	46.2	31.4	27.3
Adjusted P/E	111.4	198.8	89.2	52.7	43.6
P/BV	16.5	15.4	13.2	10.7	8.7

DuPont Analysis

Y/E 31 Mar (%)	FY22A	FY23A	FY24E	FY25E	FY26E
Tax burden (Net profit/PBT)	69.6	71.8	74.8	74.8	74.8
Interest burden (PBT/EBIT)	111.9	84.0	90.8	94.2	95.4
EBIT margin (EBIT/Revenue)	4.4	3.5	5.4	7.6	8.1
Asset turnover (Rev./Avg TA)	139.0	120.1	128.4	123.7	119.0
Leverage (Avg TA/Avg Equity)	3.4	3.2	3.4	3.4	3.2
Adjusted ROAE	16.2	8.0	16.0	22.4	21.9

Ratio Analysis

Y/E 31 Mar	FY22A	FY23A	FY24E	FY25E	FY26E
YoY growth (%)					
Revenue	42.8	(8.5)	27.2	16.4	11.4
EBITDA	23.8	(24.1)	70.1	48.7	16.4
Adjusted EPS	33.2	(44.0)	123.0	69.1	20.9
Profitability & Return ratios (%)					
EBITDA margin	6.4	5.3	7.1	9.0	9.4
EBIT margin	4.4	3.5	5.4	7.6	8.1
Adjusted profit margin	3.4	2.1	3.7	5.4	5.8
Adjusted ROAE	16.2	8.0	16.0	22.4	21.9
ROCE	18.1	12.3	20.9	27.6	26.8
Working capital days (days)					
Receivables	100	125	145	145	145
Inventory	53	67	45	40	40
Payables	121	124	120	115	115
Ratios (x)					
Gross asset turnover	4.7	3.8	4.4	4.8	5.0
Current ratio	1.1	1.2	1.2	1.2	1.3
Net interest coverage ratio	5.2	3.9	6.8	10.6	12.6
Adjusted debt/equity	0.0	0.1	0.0	(0.2)	(0.3)

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

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BUY – Expected return >+15%

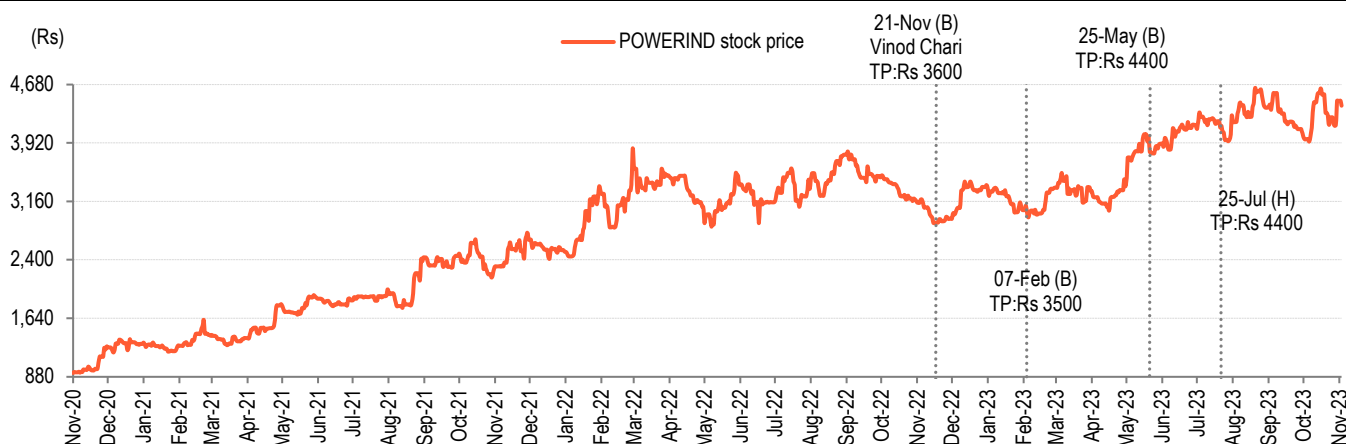
HOLD – Expected return from -6% to +15%

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): HITACHI ENERGY (POWERIND IN)



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

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