

Engineering & Capital Goods

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Delhi meeting takeaways: Infra capex to continue to drive order visibility

We met several business heads/middle management of listed/unlisted industrial companies in Delhi on February 25-26, 2019.

Key takeaways:

- Infrastructure ordering should continue to drive order inflows, albeit with temporary disruption due to the upcoming general election. Railways looks to be a lucrative opportunity for construction firms as future orders should see an increasing EPC proportion vs. BOQ orders until now.
- The Power T&D equipment space continues to struggle as PGCIL capex is on a downward trajectory. Despite higher state capex, large companies are struggling due to more demand in the low- and medium-voltage space, where the competition is high. Even when the industrial capex picks up, companies felt that the pricing/margin scenario during the golden period of 2004-2010 cycle will not be repeated.
- According to industry experts such as Feedback Infrastructure, solid foundation on infrastructure reforms have been laid. Roads, railways and urban infra ordering should gain pace after the 2019 Lok Sabha election. The government has additionally identified innovative funding mechanisms to alleviate dependency on budgetary resources.
- We are Overweight on L&T, Cummins, BHEL and KEC, while Underweight on ABB and Siemens India in our Emkay Alpha Portfolio – Engineering & Capital Goods.**

Sector feedback

- Railways** looks as a fast-emerging opportunity for construction companies, although the finalization of EPC award framework has been delayed. We expect this to finally take off by mid-FY20E. The funding from LIC and other plans in the work provide a strong visibility on new awards pipeline. Most organized players, however, have struggled to work with the railways on orders due to a restricted approved vendor list who command own payment and pricing norms. Moreover, working capital cycle is excruciatingly long as payment deadlines are often not met on time due to delays at the railways' end. L&T, KEC and Tata Projects (unlisted) are well-positioned to benefit from this opportunity.
- T&D sector feedback:** The state capex is stepping up even as PGCIL capex is falling. However, the competition in this segment remains elevated, resulting in lower margins. Although GIS switchgears and relays are still niche for large players, these hardly add up to the overall numbers. Even if the industrial and power capex accelerates, companies express doubts that the boom will be similar to the 2004-2010 cycle, where there was substantial order inflows in a short span of time, leading to significant pricing power. In this context, we fail to understand why the Power T&D sector MNCs such as ABB/Siemens/GETD command such valuation premiums.
- The hydrocarbon capex** is now gaining pace with numerous refinery orders including expansion, modernization and petchem projects. In the long term, refinery capacity should grow at 4-5% rate per annum, resulting in Rs250-300bn per annum EPC opportunity, besides the capex required for petchem projects. This capex, however, tends to be lumpy and the next upcycle is just starting, according to the feedback.
- Emkay View:** We believe that infrastructure capex will continue to remain the key driver, while industrial capex, except hydrocarbons, remains challenging. L&T and Cummins are our preferred stock picks in the space. We are Underweight (UW) on Power T&D equipment names - ABB and Siemens and Overweight (OW) on Power T&D EPC name - KEC.

Please see our sector EAP (page 5): [Emkay Alpha Portfolio – Engineering & Capital Goods](#)

ABB	ACCUMULATE
CMP	Target Price
1,224	1,596

Cummins India	ACCUMULATE
CMP	Target Price
722	919

GE T&D India	HOLD
CMP	Target Price
287	243

KEC International	BUY
CMP	Target Price
262	330

Kalpataru Power	BUY
CMP	Target Price
385	558

Larsen & Toubro	BUY
CMP	Target Price
1,285	1,606

Siemens	ACCUMULATE
CMP	Target Price
979	1,150

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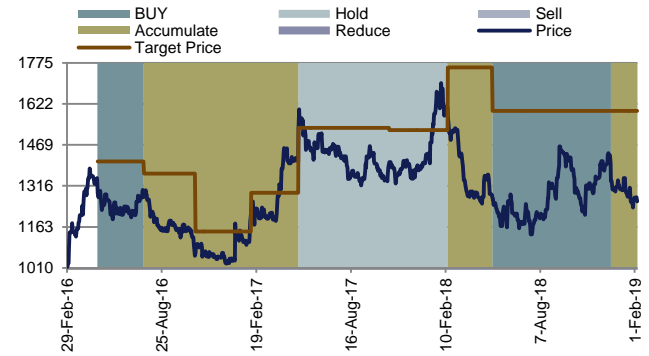
Amar Kedia
amar.kedia@emkayglobal.com
+91 22 6624 2466

Nilesh Soni
nilesh.soni@emkayglobal.com
+91 22 6612 1262

ABB
RECOMMENDATION HISTORY TABLE

Date	Closing Price	TP	Period (months)	Rating	Analyst
18-Dec-18	1,334	1,596	12m	Accumulate	John Perinchery
31-Oct-18	1,279	1,596	12m	Buy	John Perinchery
9-May-18	1,267	1,596	12m	Buy	John Perinchery
14-Feb-18	1,572	1,758	12m	Accumulate	John Perinchery
30-Jan-18	1,606	1,524	12m	Hold	John Perinchery
27-Oct-17	1,404	1,524	12m	Hold	John Perinchery
21-Jul-17	1,463	1,533	12m	Hold	John Perinchery
9-May-17	1,532	1,533	12m	Hold	John Perinchery
9-Feb-17	1,226	1,290	12m	Accumulate	John Perinchery
27-Oct-16	1,066	1,146	12m	Accumulate	John Perinchery
22-Jul-16	1,288	1,362	12m	Accumulate	John Perinchery
26-Apr-16	1,289	1,407	12m	Buy	John Perinchery

Source: Company, Emkay Research

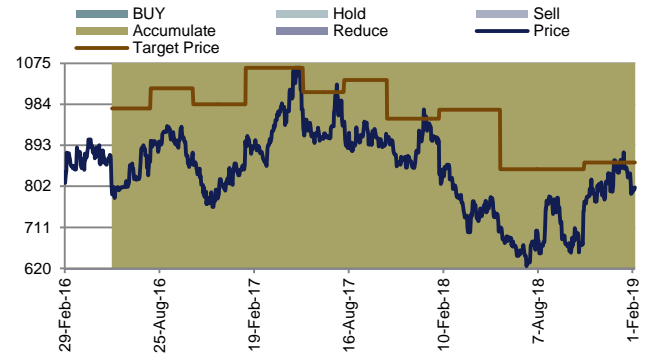
RECOMMENDATION HISTORY CHART

Source: Bloomberg, Company, Emkay Research

Cummins India
RECOMMENDATION HISTORY TABLE

Date	Closing Price	TP	Period (months)	Rating	Analyst
7-Feb-19	770	919	12m	Accumulate	Amar Kedia
2-Nov-18	768	855	12m	Accumulate	John Perinchery
28-May-18	710	840	12m	Accumulate	John Perinchery
2-Feb-18	829	972	12m	Accumulate	John Perinchery
27-Oct-17	912	952	12m	Accumulate	John Perinchery
7-Aug-17	946	1,038	12m	Accumulate	John Perinchery
22-May-17	931	1,011	12m	Accumulate	John Perinchery
3-Feb-17	892	1,065	12m	Accumulate	John Perinchery
27-Oct-16	850	984	12m	Accumulate	John Perinchery
8-Aug-16	903	1,020	12m	Accumulate	John Perinchery
27-May-16	784	975	12m	Accumulate	John Perinchery

Source: Company, Emkay Research

RECOMMENDATION HISTORY CHART

Source: Bloomberg, Company, Emkay Research

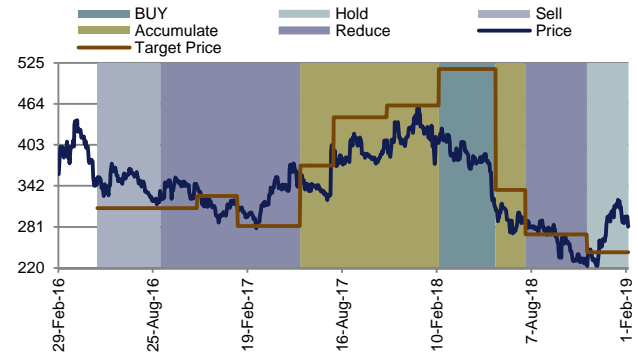
GE T&D India

RECOMMENDATION HISTORY TABLE

Date	Closing Price	TP	Period (months)	Rating	Analyst
20-Nov-18	223	243	12m	Hold	John Perinchery
27-Jul-18	290	270	12m	Reduce	John Perinchery
1-Jun-18	306	336	12m	Accumulate	John Perinchery
14-Feb-18	412	516	12m	Buy	John Perinchery
8-Nov-17	410	462	12m	Accumulate	John Perinchery
31-Jul-17	395	444	12m	Accumulate	John Perinchery
29-May-17	347	372	12m	Accumulate	John Perinchery
31-Jan-17	307	282	12m	Reduce	John Perinchery
16-Nov-16	340	327	12m	Reduce	John Perinchery
8-Sep-16	322	309	12m	Reduce	John Perinchery
12-May-16	353	309	12m	Sell	John Perinchery

Source: Company, Emkay Research

RECOMMENDATION HISTORY CHART



Source: Bloomberg, Company, Emkay Research

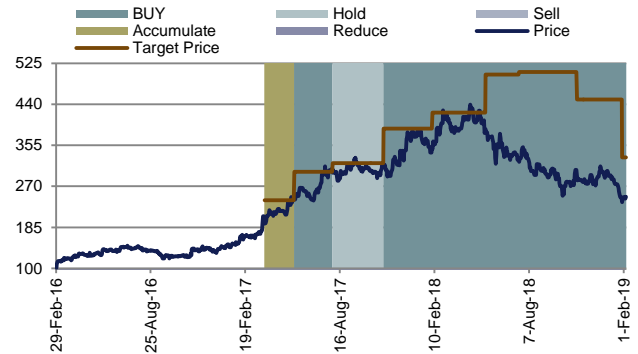
KEC International

RECOMMENDATION HISTORY TABLE

Date	Closing Price	TP	Period (months)	Rating	Analyst
29-Jan-19	237	330	12m	Buy	Amar Kedia
5-Nov-18	291	450	12m	Buy	John Perinchery
19-Jul-18	321	507	12m	Buy	John Perinchery
17-May-18	388	502	12m	Buy	John Perinchery
6-Feb-18	348	423	12m	Buy	John Perinchery
30-Jan-18	351	390	12m	Buy	John Perinchery
6-Nov-17	316	390	12m	Buy	John Perinchery
2-Aug-17	298	318	12m	Hold	John Perinchery
22-May-17	244	300	12m	Buy	John Perinchery
27-Mar-17	192	241	12m	Accumulate	John Perinchery

Source: Company, Emkay Research

RECOMMENDATION HISTORY CHART

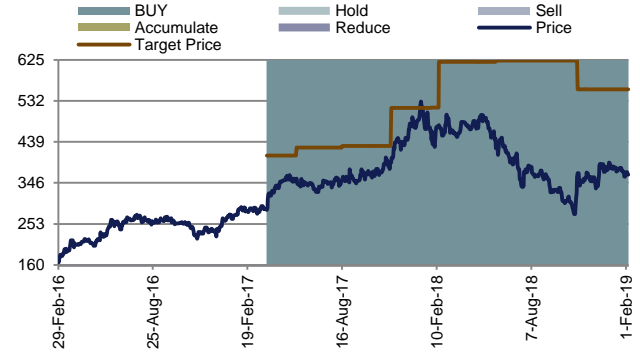


Source: Bloomberg, Company, Emkay Research

Kalpataru Power**RECOMMENDATION HISTORY TABLE**

Date	Closing Price	TP	Period (months)	Rating	Analyst
2-Nov-18	368	558	12m	Buy	John Perinchery
1-Jun-18	425	624	12m	Buy	John Perinchery
14-Feb-18	477	621	12m	Buy	John Perinchery
30-Jan-18	466	517	12m	Buy	John Perinchery
16-Nov-17	393	516	12m	Buy	John Perinchery
16-Aug-17	352	430	12m	Buy	John Perinchery
22-May-17	356	426	12m	Buy	John Perinchery
27-Mar-17	285	408	12m	Buy	John Perinchery

Source: Company, Emkay Research

RECOMMENDATION HISTORY CHART

Source: Bloomberg, Company, Emkay Research

Emkay Alpha Portfolio – Engineering & Capital Goods



Analyst: Amar Kedia

Contact Details

amar.kedia@emkayglobal.com

+91 22 6624 2466

Sector

Engineering & Capital Goods

Analyst bio

Amar Kedia holds a Post Graduate Diploma in Management from IIM Lucknow and comes with a cumulative 15 years of research experience. His team currently covers 14 stocks in the Indian Engineering and Capital Goods sector.

EAP sector portfolio

Company Name	BSE200 Weight	EAP Weight	OW/UW (%)	OW/UW (bps)	EAP Weight (Normalised)
Engineering & Capital Goods	3.58	3.58	0%	0	100
ABB	0.12	0.07	-39%	-5	2
BHEL	0.15	0.20	32%	5	6
Blue Star	0.00	0.00	NA	0	0
Cummins India	0.18	0.27	53%	9	8
Dynumatic Technologies	0.00	0.00	NA	0	0
GE T&D India	0.00	0.00	NA	0	0
Kalpitaru Power	0.00	0.00	NA	0	0
KEC International	0.00	0.07	NA	7	2
Larsen & Toubro	2.76	2.97	8%	21	83
Siemens	0.16	0.00	-100%	-16	0
Skipper	0.00	0.00	NA	0	0
Symphony	0.00	0.00	NA	0	0
Thermax	0.00	0.00	NA	0	0
Triveni Turbine	0.00	0.00	NA	0	0
Voltas	0.22	0.00	-100%	-22	0

Source: Emkay Research

* Not under coverage: Equal Weight

Sector portfolio NAV (for future addition)

Returns by EAP on rolling basis

Performance	NAV	3M	6M	12M
EAP - Engineering & Capital Goods	100			
BSE 200 weighted portfolio	100			

*Formal performance measurement of EAP starts 1st April 2019

Source: Emkay Research

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BUY	Expected total return (%) (Stock price appreciation and dividend yield) of over 25% within the next 12-18 months.
ACCUMULATE	Expected total return (%) (Stock price appreciation and dividend yield) of over 10% within the next 12-18 months.
HOLD	Expected total return (%) (Stock price appreciation and dividend yield) of upto 10% within the next 12-18 months.
REDUCE	Expected total return (%) (Stock price depreciation) of upto (-) 10% within the next 12-18 months.
SELL	The stock is believed to underperform the broad market indices or its related universe within the next 12-18 months.

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Emkay Global Financial Services Ltd.**CIN - L67120MH1995PLC084899**

7th Floor, The Ruby, Senapati Bapat Marg, Dadar - West, Mumbai - 400028. India

Tel: +91 22 66121212 Fax: +91 22 66121299 Web: www.emkayglobal.com

SINGAPORE**DBS Bank Ltd**

Contact: Janice Chua
12 Marina Boulevard, Marina Bay Financial Centre Tower 3
Singapore 018982
Tel. 65-6878 8888
Fax: 65 65353 418
e-mail: equityresearch@dbs.com
Company Regn. No. 196800306E

THAILAND**DBS Vickers Securities (Thailand) Co Ltd**

Contact: Chanpen Sirithanarattanakul
989 Siam Piwat Tower Building,
9th, 14th-15th Floor
Rama 1 Road, Pathumwan,
Nagkok Thailand 10330
Tel. 66 2 857 7831
Fax: 66 2 658 1269
e-mail: research@th.dbs.com
Company Regn. No 0105539127012
Securities and Exchange Commission, Thailand

INDONESIA**PT DBS Vickers Sekuritas (Indonesia)**

Contact: Maynard Priajaya Arif
DBS Bank Tower
Ciputra World 1, 32/F
Jl. Prof. Dr. Satrio Kav. 3-5
Jakarta 12940, Indonesia
Tel. 62 21 3003 4900
Fax: 62 21 3003 4943
e-mail: research@id.dbsvickers.com



Amar Kedia, PGDBM- Finance
amar.kedia@emkayglobal.com
+91 22 6624 2466