# Capital Goods

Institutional Equity Research

Results Preview | 07 April 2022

## Inflationary Pressure to Impact Margin

### Strong Tender Pipeline, Higher Commodity Prices to Impact Order Finalization

Capital goods sector witnessed healthy tender pipeline in sectors like Infrastructure, Data centers, Railways, Metro, Civil, Water Treatment and iInternational Power T&D, however higher commodity prices may result in some spillover in order finalization. Rising crude price to boost capex in oil exporting economies like the Middle East, while oil importing economies like India may have a negative impact of the higher oil price. The ongoing Russia-Ukraine crisis has further escalated the inflated commodity prices, which likely to impact margin and execution in the near term. Companies with higher fixed price contract exposure will likely to be most impacted. Companies with lower fixed price contracts and cost-plus model will have better ability to withstand the commodity inflation during 4QFY22.

### Price Hikes to Continue

Revenue growth for product companies is largely led by price with rounds of price hikes in the last couple of quarters. We expect the price hike may continue in the near term to restore gross margin. The demand for consumer durables and electricals was impacted in Jan'22/Feb'22 due to the Omicron scare and continued price hikes. However, demand picked up in Mar'22, particularly in summer categories like room AC/cooler/fans. Companies continued to face challenges due to the steep rise in commodity prices, elevated logistic costs and shortage of semiconductors.

### Healthy Order Inflow

In terms of key highlights during the quarter, L&T announced orders worth ~Rs350bn in 4QFY22, and the labor availability was stable during the quarter. A minor execution impact is expected due to supply chain bottleneck and delayed exports during 4QFY22. For KEC, we expect healthy execution in the domestic T&D, railway and civil segments, while SAE Tower's execution and profitability will be impacted due to the higher steel prices and legacy projects. The workforce crunch and an additional cost of time overruns would impact profitability. We expect SAE Tower to report an EBIT loss in 4QFY22 and break even in 1QFY23 onwards with the completion of legacy projects. KEC reported the highest order inflow of Rs172bn in FY22, up 45% YoY, mainly led by the civil segment.

We expect our capital goods coverage universe to report 6.3% YoY growth in revenue, while EBITDA and PAT to decline by 13.4% YoY and 11.8% YoY respectively in 4QFY22E. EBITDA margin is expected to decline by 60bps YoY to 11.4%.

### Our View:

The Indian economy witnessed a sharp recovery in the past few quarters, while the strong capex revival in capital goods sector is likely to continue ahead. Key economic indicators like GDP, GST collections, manufacturing PMI, core sector output growth, import-export data among others continue to show that the ongoing economic recovery should propel a sustained improvement in corporate earnings. GST collections for Mar'22 hit a record high of Rs1,420bn, up 6.8% MoM. The 8 core sector industries notched up a positive growth rate. India is one of the resilient and fastest-growing economy during the pandemic in the world. The sustained increase in government capex could be supportive to the economy until private capex revives. To reduce India's dependence on foreign military equipments, the ministry of defence has identified various items for indigenization and 'Make-II' list, which will benefit the defence companies ahead. The ministry of defence announced a second negative import list of 108 items, which are likely to provide a boost to Atmanirbhar Bharat and indigenization plans in the defence sector, with the active participation of both public and private sectors.

**Our Top Picks: L&T, Kalpataru Power and KEC International**

**Research Analyst:**
**Arafat Saiyed**
Contact : (022) 41681371 / 9819503007
Email : arafat.saiyed@relianceada.com

**Exhibit 1: Capital Goods & Defence - Quarterly Estimates**

| Company | Revenue (Rs mn) | | | | | EBITDA (Rs mn) | | | | | PAT (Rs mn) | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Mar-22E | Mar-21 | YoY (%) | Dec-21 | QoQ (%) | Mar-22E | Mar-21 | YoY (%) | Dec-21 | QoQ (%) | Mar-22E | Mar-21 | YoY (%) | Dec-21 | QoQ (%) |
| ABB India | 18,305 | 16,292 | 12.4 | 21,015 | (12.9) | 1,409 | 1,323 | 6.6 | 1,852 | (23.9) | 1,038 | 947 | 9.6 | 1,468 | (29.3) |
| BEL | 62,716 | 69,175 | (9.3) | 37,017 | 69.4 | 14,613 | 19,809 | (26.2) | 8,293 | 76.2 | 10,518 | 13,682 | (23.1) | 5,961 | 76.4 |
| BEML | 16,496 | 17,738 | (7.0) | 11,331 | 45.6 | 2,128 | 1,771 | 20.2 | 743 | 186.4 | 1,866 | 1,599 | 16.6 | 785 | 137.6 |
| Blue Star | 18,562 | 16,116 | 15.2 | 15,062 | 23.2 | 1,102 | 1,018 | 8.2 | 906 | 21.6 | 560 | 680 | (17.6) | 475 | 17.9 |
| Crompton Consumer | 16,817 | 15,221 | 10.5 | 14,106 | 19.2 | 2,275 | 2,280 | (0.2) | 2,015 | 12.9 | 1,805 | 2,491 | (27.5) | 1,483 | 21.8 |
| Engineers India | 10,827 | 11,167 | (3.0) | 6,816 | 58.9 | 1,254 | 1,640 | (23.5) | 625 | 100.7 | 1,189 | 1,855 | (35.9) | 680 | 74.7 |
| Havells India | 38,622 | 33,392 | 15.7 | 36,642 | 5.4 | 4,956 | 5,082 | (2.5) | 4,402 | 12.6 | 3,300 | 3,038 | 8.6 | 3,058 | 7.9 |
| Kalpataru Power | 24,305 | 23,370 | 4.0 | 18,480 | 31.5 | 2,236 | 2,430 | (8.0) | 1,680 | 33.1 | 1,238 | 1,300 | (4.8) | 530 | 133.5 |
| KEC International | 48,573 | 43,605 | 11.4 | 33,400 | 45.4 | 3,157 | 3,545 | (10.9) | 2,390 | 32.1 | 1,455 | 1,943 | (25.1) | 936 | 55.4 |
| Larsen & Toubro | 5,14,541 | 4,80,879 | 7.0 | 3,95,629 | 30.1 | 56,361 | 63,889 | (11.8) | 45,304 | 24.4 | 31,662 | 34,173 | (7.3) | 20,547 | 54.1 |
| Rites | 6,702 | 6,359 | 5.4 | 7,666 | (12.6) | 1,627 | 1,854 | (12.2) | 1,873 | (13.1) | 1,261 | 1,416 | (10.9) | 1,443 | (12.6) |
| Voltas | 31,334 | 26,517 | 18.2 | 17,936 | 74.7 | 2,806 | 3,307 | (15.1) | 1,556 | 80.3 | 2,193 | 2,377 | (7.8) | 960 | 128.5 |
| **Aggregate** | **8,07,799** | **7,59,829** | **6.3** | **6,15,100** | **31.3** | **93,925** | **1,07,947** | **(13.0)** | **71,639** | **31.1** | **58,084** | **65,500** | **(11.3)** | **38,326** | **51.6** |

*Source: Company, RSec Research*

**Exhibit 2: Capital Goods & Defence - 4QFY22 Results Preview**

| Company (Rs mn) | Mar-22E | Mar-21 | YoY (%) | Dec-21 | QoQ (%) | Comments |
|---|---|---|---|---|---|---|
| **ABB India** | | | | | | |
| Revenue | 18,305 | 16,292 | 12.4 | 21,015 | (12.9) | ▶ We expect the company's revenue to increase by 12% YoY to Rs18.3bn in 1QCY22, led by the demand uptick in electrification and process automation segments. Adjusted PAT is expected to increase by 10% YoY to Rs1bn, while operating margin is likely to decline by 40bps YoY to 7.7%, due to higher RM cost. |
| EBITDA | 1,409 | 1,323 | 6.6 | 1,852 | (23.9) | |
| EBITDA Margin (%) | 7.7 | 8.1 | (42)bps | 8.8 | (111)bps | |
| PAT | 1,038 | 947 | 9.6 | 1,468 | (29.3) | |
| **Bharat Electronics (BEL)** | | | | | | |
| Revenue | 62,716 | 69,175 | (9.3) | 37,017 | 69.4 | ▶ We expect BEL to report a revenue of Rs62.7bn (down 9% YoY), mainly due to the shortage of semiconductors in 4QFY22. EBITDA is expected to decline by 26% YoY to Rs14.6bn, while EBITDA margin is likely to decline by 530bps YoY to 23.3%, due to lower sales and higher RM cost. We expect its PAT to decline by 23% YoY to Rs10.5bn, due to lower execution and margin compression. |
| EBITDA | 14,613 | 19,809 | (26.2) | 8,293 | 76.2 | |
| EBITDA Margin (%) | 23.3 | 28.6 | (534)bps | 22.4 | 90bps | |
| PAT | 10,518 | 13,682 | (23.1) | 5,961 | 76.4 | |
| **BEML** | | | | | | |
| Revenue | 16,496 | 17,738 | (7.0) | 11,331 | 45.6 | ▶ We expect BEML to report Rs16.5bn revenue (down 7% YoY), led by a muted performance of key segments. EBITDA to increase by 20% YoY to Rs2.2bn, while PAT is seen at Rs1.9bn, up 17% YoY. |
| EBITDA | 2,128 | 1,771 | 20.2 | 743 | 186.4 | |
| EBITDA Margin (%) | 12.9 | 10.0 | 292bps | 6.6 | 634bps | |
| PAT | 1,866 | 1,599 | 16.6 | 785 | 137.6 | |
| **Blue Star** | | | | | | |
| Revenue | 18,562 | 16,116 | 15.2 | 15,062 | 23.2 | ▶ The company's revenue is expected to decline by 15% YoY to Rs18.6bn, led by 11% YoY and 20% YoY growth in projects and unitary product segments, respectively. Its EBITDA margin is seen at 5.9%, down 40bps YoY, due to a lower margin in key segments impacted by the higher commodity prices, while PAT is seen at Rs560mn, down 18% YoY. |
| EBITDA | 1,102 | 1,018 | 8.2 | 906 | 21.6 | |
| EBITDA Margin (%) | 5.9 | 6.3 | (38)bps | 6.0 | (8)bps | |
| PAT | 560 | 680 | (17.6) | 475 | 17.9 | |
| **Crompton Greaves Consumer Electricals** | | | | | | |
| Revenue | 16,817 | 15,221 | 10.5 | 14,106 | 19.2 | ▶ The company's revenue is expected to increase by 11% YoY to Rs16.8bn, led by 12% YoY growth in ECD segment and 5% YoY growth in lighting segment. It is expected to see a healthy growth in appliances with the continued price hike. EBITDA to remain flat YoY at Rs2.3bn, while EBITDA margin is likely to decline by 150bps YoY to 14.2% due to the higher commodity prices. PAT is seen at Rs1.8bn (down 28% YoY), impacted by a lower margin. |
| EBITDA | 2,275 | 2,280 | (0.2) | 2,015 | 12.9 | |
| EBITDA Margin (%) | 13.5 | 15.0 | (145)bps | 14.3 | (76)bps | |
| PAT | 1,805 | 2,491 | (27.5) | 1,483 | 21.8 | |

## Capital Goods & Defence - 4QFY22 Results Preview

| Company (Rs mn) | Mar-22E | Mar-21 | YoY (%) | Dec-21 | QoQ (%) | Comments |
|---|---|---|---|---|---|---|
| **Engineers India** | | | | | | |
| Revenue | 10,827 | 11,167 | (3.0) | 6,816 | 58.9 | ▶ The company's revenue is expected to decline by 3% YoY to Rs10.8bn, impacted by 15% YoY decline in turnkey revenue at Rs6bn, due to a lower execution. Revenue of consultancy segment to increase by 18% YoY to Rs4.8bn. EBITDA is expected to decline by 24% YoY, while EBITDA margin is likely to decline by 310bps YoY to 11.6%. PAT is likely to decline by 36% YoY to Rs1.18bn, due to a lower execution. |
| EBITDA | 1,254 | 1,640 | (23.5) | 625 | 100.7 | |
| EBITDA Margin (%) | 11.6 | 14.7 | (311)bps | 9.2 | 241bps | |
| PAT | 1,189 | 1,855 | (35.9) | 680 | 74.7 | |
| **Havells India** | | | | | | |
| Revenue | 38,622 | 33,392 | 15.7 | 36,642 | 5.4 | ▶ We expect the company's revenue to increase by 16% YoY to Rs38.6bn, owing to a higher revenue from the key segments, especially ECD and cable and wire segments. Havells' expanding distribution footprint, robust supply chain and market share gain from the unorganized sector are likely to support a higher growth during the quarter. EBITDA margin is expected to decline by 240bps YoY to 12.8% due to the higher commodity prices. PAT growth to moderate at 9% YoY to Rs3.3bn due to a lower margin. |
| EBITDA | 4,956 | 5,082 | (2.5) | 4,402 | 12.6 | |
| EBITDA Margin (%) | 12.8 | 15.2 | (239)bps | 12.0 | 82bps | |
| PAT | 3,300 | 3,038 | 8.6 | 3,058 | 7.9 | |
| **Kalpataru Power** | | | | | | |
| Revenue | 24,305 | 23,370 | 4.0 | 18,480 | 31.5 | ▶ Revenue is expected to increase by 4% YoY to Rs24.3bn, led by a muted execution in the key segments -- T&D, railway and pipeline. EBITDA is expected to decline by 8% YoY to Rs2.2bn, while EBITDA margin is expected to decline by 120bps YoY to 9.2%, due to the higher raw material cost. PAT is expected to decline by 5% YoY to Rs1.2bn. The performance of JMC Projects and Shree Shubham Logistics is likely to remain strong on a YoY basis. |
| EBITDA | 2,236 | 2,430 | (8.0) | 1,680 | 33.1 | |
| EBITDA Margin (%) | 9.2 | 10.4 | (120)bps | 9.1 | 11bps | |
| PAT | 1,238 | 1,300 | (4.8) | 530 | 133.5 | |
| **KEC International** | | | | | | |
| Revenue | 48,573 | 43,605 | 11.4 | 33,400 | 45.4 | ▶ Execution is on track for projects barring localized issues in some international projects. Two legacy projects in Brazil (SAE) are likely to report a loss, thus impacting the overall margins. Revenue is expected to increase by 11% YoY to Rs48.5bn led by a strong growth in T&D, railway and civil businesses, while PAT is likely to decline by 25% YoY to Rs1.45bn. We expect its EBITDA margin to decline by 160bps YoY to 6.5% due to losses in the legacy projects in Brazil. |
| EBITDA | 3,157 | 3,545 | (10.9) | 2,390 | 32.1 | |
| EBITDA Margin (%) | 6.5 | 8.1 | (163)bps | 7.2 | (66)bps | |
| PAT | 1,455 | 1,943 | (25.1) | 936 | 55.4 | |
| **Larsen & Toubro** | | | | | | |
| Revenue | 5,14,541 | 4,80,879 | 7.0 | 3,95,629 | 30.1 | ▶ L&T secured orders worth ~Rs350bn in 4QFY22. The company is focusing on liquidity management and witnessed a significant headway in the current challenging scenario. We expect L&T to report a revenue of Rs514bn (up 7% YoY), owing to an uptick in core infra segment. We expect its EBITDA to decline by 12% YoY to Rs56.3bn, while EBITDA margin is likely to decline by 230bps YoY to 11%. We expect PAT to decline by 7% YoY to Rs31.7bn, supported by the lower interest cost. |
| EBITDA | 56,361 | 63,889 | (11.8) | 45,304 | 24.4 | |
| EBITDA Margin (%) | 11.0 | 13.3 | (233)bps | 11.5 | (50)bps | |
| PAT | 31,662 | 34,173 | (7.3) | 20,547 | 54.1 | |

**Capital Goods & Defence - 4QFY22 Results Preview**

| Company (Rs mn) | Mar-22E | Mar-21 | YoY (%) | Dec-21 | QoQ (%) | Comments |
|---|---|---|---|---|---|---|
| **RITES** | | | | | | |
| Revenue | 6,702 | 6,359 | 5.4 | 7,666 | (12.6) | ▶ Revenue is expected to increase by 5.4% YoY to Rs6.7bn, led by a strong uptick in the export business and on a low base, after a complete washout in 4QFY21. We expect its EBITDA margin to decline by 490bps YoY to 24.3%, due to the higher raw material cost. PAT is likely to decline by 11% YoY to Rs1.26bn. |
| EBITDA | 1,627 | 1,854 | (12.2) | 1,873 | (13.1) | |
| EBITDA Margin (%) | 24.3 | 29.2 | (488)bps | 24.4 | (15)bps | |
| PAT | 1,261 | 1,416 | (10.9) | 1,443 | (12.6) | |
| **Voltas** | | | | | | |
| Revenue | 31,334 | 26,517 | 18.2 | 17,936 | 74.7 | ▶ We expect Voltas to report Rs31.3bn revenue (up 18% YoY), led by a strong growth in key segments. Revenue from unitary cooling is expected to increase by 25% YoY to Rs20.6bn, led by price hikes and the first full peak season after 2 years of lockdown. Revenue of EMPS segment to grow by 10% YoY to Rs9.6bn. The company's EBITDA margin is likely to decline by 350bps YoY to 9%, due to a lower margin in the key segments impacted by the higher RM prices, while PAT is seen at Rs2.2bn (down 8% YoY). |
| EBITDA | 2,806 | 3,307 | (15.1) | 1,556 | 80.3 | |
| EBITDA Margin (%) | 9.0 | 12.5 | (352)bps | 8.7 | 28bps | |
| PAT | 2,193 | 2,377 | (7.8) | 960 | 128.5 | |

*Source: RSec Research*

## Change in Ratings

We have changed our rating system and included **HOLD** recommendation. We have **BUY, HOLD and SELL** recommendation now.

We have also shifted to **1-Year Target Price** from **2-Year Target Price**.

Mitul Dilipkumar Shah

Digitally signed by Mitul Dilipkumar Shah
DN: c=IN, o=Personal, title=1748, pseudonym=ae7ad4bd9ee9795ea86bc594a157b5c534580118, 2.5.4.20=e0fb9e3e232847cf9f073d3b1df63fa001f377a7004fd86cbea87122ce044303, postalCode=400067, st=Maharashtra, serialNumber=0fa3b306aafde36b539707b48cce4e7ac307839092b8cd8323de535e18683c65, cn=Mitul Dilipkumar Shah
Date: 2022.04.07 22:35:30 +05'30'

Reliance Securities Limited (RSL), the broking arm of Reliance Capital is one of the India's leading retail broking houses. Reliance Capital is amongst India's leading and most valuable financial services companies in the private sector. Reliance Capital has interests in asset management and mutual funds, life and general insurance, commercial finance, equities and commodities broking, wealth management services, distribution of financial products, private equity, asset reconstruction, proprietary investments and other activities in financial services. The list of associates of RSL is available on the website www.reliancecapital.co.in. RSL is registered as a Research Analyst under SEBI (Research Analyst) Regulations, 2014

General Disclaimers: This Research Report (hereinafter called 'Report') is prepared and distributed by RSL for information purposes only. The recommendations, if any, made herein are expression of views and/or opinions and should not be deemed or construed to be neither advice for the purpose of purchase or sale of any security, derivatives or any other security through RSL nor any solicitation or offering of any investment /trading opportunity on behalf of the issuer(s) of the respective security(ies) referred to herein. These information / opinions / views are not meant to serve as a professional investment guide for the readers. No action is solicited based upon the information provided herein. Recipients of this Report should rely on information/data arising out of their own investigations. Readers are advised to seek independent professional advice and arrive at an informed trading/investment decision before executing any trades or making any investments. This Report has been prepared on the basis of publicly available information, internally developed data and other sources believed by RSL to be reliable. RSL or its directors, employees, affiliates or representatives do not assume any responsibility for, or warrant the accuracy, completeness, adequacy and reliability of such information / opinions / views. While due care has been taken to ensure that the disclosures and opinions given are fair and reasonable, none of the directors, employees, affiliates or representatives of RSL shall be liable for any direct, indirect, special, incidental, consequential, punitive or exemplary damages, including lost profits arising in any way whatsoever from the information / opinions / views contained in this Report.

Risks: Trading and investment in securities are subject to market risks. There are no assurances or guarantees that the objectives of any of trading / investment in securities will be achieved. The trades/ investments referred to herein may not be suitable to all categories of traders/investors. The names of securities mentioned herein do not in any manner indicate their prospects or returns. The value of securities referred to herein may be adversely affected by the performance or otherwise of the respective issuer companies, changes in the market conditions, micro and macro factors and forces affecting capital markets like interest rate risk, credit risk, liquidity risk and reinvestment risk. Derivative products may also be affected by various risks including but not limited to counter party risk, market risk, valuation risk, liquidity risk and other risks. Besides the price of the underlying asset, volatility, tenor and interest rates may affect the pricing of derivatives.

Disclaimers in respect of jurisdiction: The possession, circulation and/or distribution of this Report may be restricted or regulated in certain jurisdictions by appropriate laws. No action has been or will be taken by RSL in any jurisdiction (other than India), where any action for such purpose(s) is required. Accordingly, this Report shall not be possessed, circulated and/or distributed in any such country or jurisdiction unless such action is in compliance with all applicable laws and regulations of such country or jurisdiction. RSL requires such recipient to inform himself about and to observe any restrictions at his own expense, without any liability to RSL. Any dispute arising out of this Report shall be subject to the exclusive jurisdiction of the Courts in India.

Disclosure of Interest: The research analysts who have prepared this Report hereby certify that the views /opinions expressed in this Report are their personal independent views/opinions in respect of the securities and their respective issuers. None of RSL, research analysts, or their relatives had any known direct /indirect material conflict of interest including any long/short position(s) in any specific security on which views/opinions have been made in this Report, during its preparation. RSL's Associates may have other potential/ material conflict of interest with respect to any recommendation and related information and opinions at the time of publication of research report. RSL, its Associates, the research analysts, or their relatives might have financial interest in the issuer company(ies) of the said securities. RSL or its Associates may have received a compensation from the said issuer company(ies) in last 12 months for the brokerage or non brokerage services.RSL, its Associates, the research analysts or their relatives have not received any compensation or other benefits directly or indirectly from the said issuer company(ies) or any third party in last 12 months in any respect whatsoever for preparation of this report.

The research analysts has served as an officer, director or employee of the said issuer company(ies)?: No

RSL, its Associates, the research analysts or their relatives holds ownership of 1% or more, in respect of the said issuer company(ies).?: No



RSL's activities were neither suspended nor have defaulted with any stock exchange with whom RSL is registered. Further, there does not exist any material adverse order/judgments/strictures assessed by any regulatory, government or public authority or agency or any law enforcing agency in last three years. Further, there does not exist any material enquiry of whatsoever nature instituted or pending against RSL as on the date of this Report.

Important These disclaimers, risks and other disclosures must be read in conjunction with the information / opinions / views of which they form part of.

RSL CIN: U65990MH2005PLC154052. SEBI registration no. (Stock Broker: INZ000172433, Depository Participants: CDSL IN-DP-257-2016 IN-DP-NSDL-363-2013, Research Analyst: INH000002384); AMFI ARN No.29889.