

India

December 11, 2023 - 6:40 PM

Overweight (no change)

Highlighted Companies

ABB India Ltd

ADD, TP Rs4965, Rs4787 close

ABB India witnessed a strong momentum in base orders aided by its focus on the growth segments, rising market penetration, expansion of portfolio and expansion of partner network. The pipeline is strong in the case of large orders, with metals & cement sectors investing in large projects. We feel the trend is likely to remain strong going ahead.

Larsen & Toubro Ltd

ADD, TP Rs3300, Rs3386 close

Larsen & Toubro or L&T is well-placed to achieve its 'Lakshya 2026' revenue of Rs2.7tr and order inflow of Rs3.7tr, translating into a revenue and order inflow CAGR of 14% each. L&T plans to achieve a RoE of over 18% in FY26F vs. a RoE of 13.8% in FY23.

Thermax Ltd

ADD, TP Rs3275, Rs2680 close

Thermax is a key beneficiary of the green shoots witnessed in private sector capex in multiple industries. The company has a healthy order book with a strong pipeline of small ticket-size orders in cement, biomass, food and beverage, and sugar/distillery segments.

Summary Valuation Metrics

P/E (x)	Mar24-F	Mar25-F	Mar26-F
ABB India Ltd	88.11	79.94	72.3
Larsen & Toubro Ltd	36.44	29.75	26.46
Thermax Ltd	48.3	39.76	35.77

P/BV (x)	Mar24-F	Mar25-F	Mar26-F
ABB India Ltd	17.03	14.34	12.2
Larsen & Toubro Ltd	5.32	4.65	4.06
Thermax Ltd	6.88	6	5.24

Dividend Yield	Mar24-F	Mar25-F	Mar26-F
ABB India Ltd	0.13%	0.15%	0.16%
Larsen & Toubro Ltd	0.62%	0.65%	0.65%
Thermax Ltd	0.36%	0.37%	0.37%

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Ind Goods & Services

Double-digit capex stayed intact in 1HFY24

- Capex-led growth was steady in 1HFY24, up 15% YoY. The public sector capex to moderate in the coming quarters, but likely to pick up post general elections.
- The top five sectors accounted for 58% of total capex led by oil & gas (O&G). Dependence on the O&G sector dipped to 27% of total capex vs. 35% in FY21.
- We remain Overweight on the capital goods sector as stock valuations currently factor in a strong capex recovery led by various schemes.

Capex-led growth steady in 1HFY24

- India's capex-led growth remained steady in 1HFY24 while the key monitorables are the outcome of 2024 general elections in India, further consumption recovery, the ongoing geopolitical tensions and the global interest rate cycle, which is on the rise.
- Total capex was up 15% YoY in 1HFY24. Public sector companies' capex is likely to moderate in the coming quarters but may pick up post general elections.
- The government has maintained its strong capex in key infrastructure-related sectors like roads, railway including metro rail, water and power T&D. The capex in 1HFY24 continued to be concentrated in these key sectors.
- This is also reflected in the strong growth in steel consumption, cement production and import of capital goods. Capacity utilization in the manufacturing sector continues to remain above the long-period average.

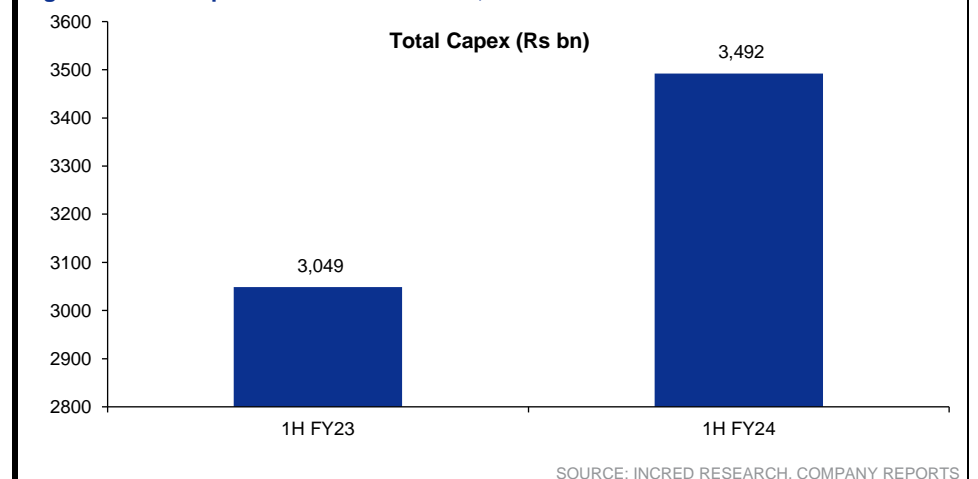
Capex dependence on oil & gas sector reduces

- The top five sectors accounted for 58% of total capex led by oil & gas, up 2%. The dependence on the oil & gas sector reduced to 27% of total capex in 1HFY24 from 35% in FY21.
- The capex growth was led by sectors like steel/metal, up 24% (12% of total), power, up 25% (10% of total), automobile, up 27% (8% of total) & telecom, up 26% (6% of total).
- Over the next few years, renewable energy-led capex is likely to dominate. Festive demand has also spurred discretionary consumption in the past few quarters. Investment activity continues to be aided by buoyancy in public sector capex.

Positive stance on capital goods sector

- We remain Overweight on the capital goods sector as stock valuations currently factor in a strong capex recovery led by various schemes like National Infrastructure Pipeline or NIP, Gati Shakti, and Make in India. The special focus on capex to provide several opportunities for companies going ahead.
- We reiterate our ADD rating on L&T, ABB India, Thermax, Siemens and KEC International, with their order backlog providing revenue visibility, apart from reasonable valuations. We have a HOLD rating on Voltas and a REDUCE rating on Cummins India.

Figure 1: Total capex in India stood at Rs3,492bn in 1HFY24



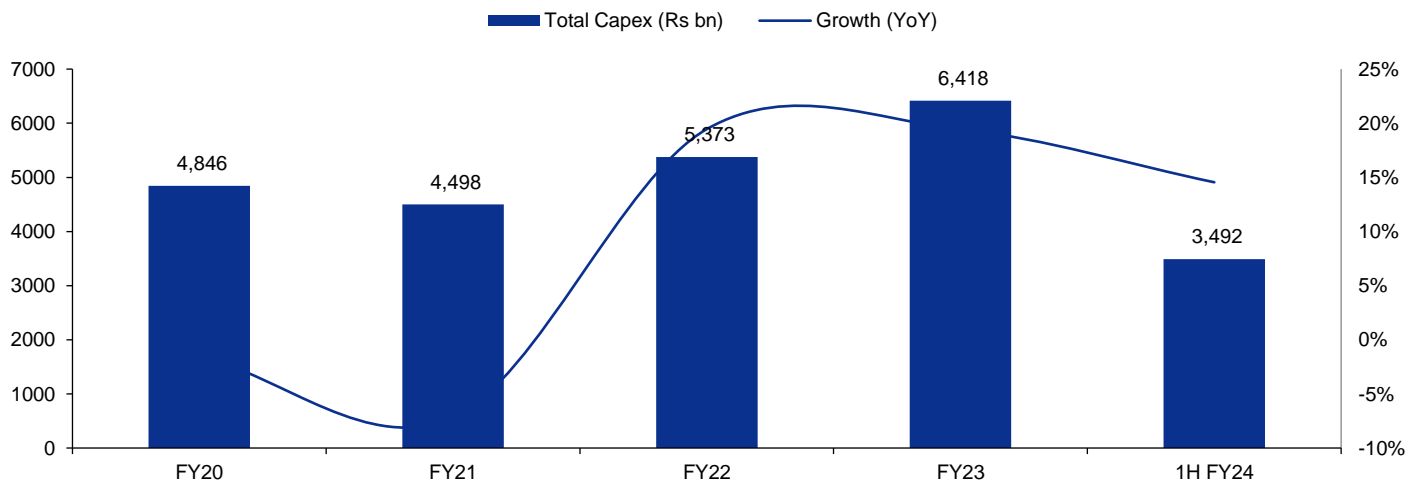
Order inflow momentum continues

- Aggregate order inflow was robust in 1HFY24 (up 52% YoY), mainly led by L&T (up 65% YoY) on the back of its international business while other companies witnessed a lower order inflow. New investments announced in 9MCY23 grew 2% YoY while in 2QFY24 they declined by 71% YoY.
- We expect the new trend of private sector spending led by the energy sector's transition into the segments such as renewables, electrical vehicle or EV, battery technology, and hydrogen.
- We expect new investments, especially from the government, to remain muted in the near term due to the upcoming assembly/general elections in India while manufacturing capex, led by the production-linked incentive or PLI scheme and the China+1 strategy, to see an uptick. We expect the order inflow of our coverage universe to clock a 14% CAGR over FY23-25F.

Margin expansion on the cards

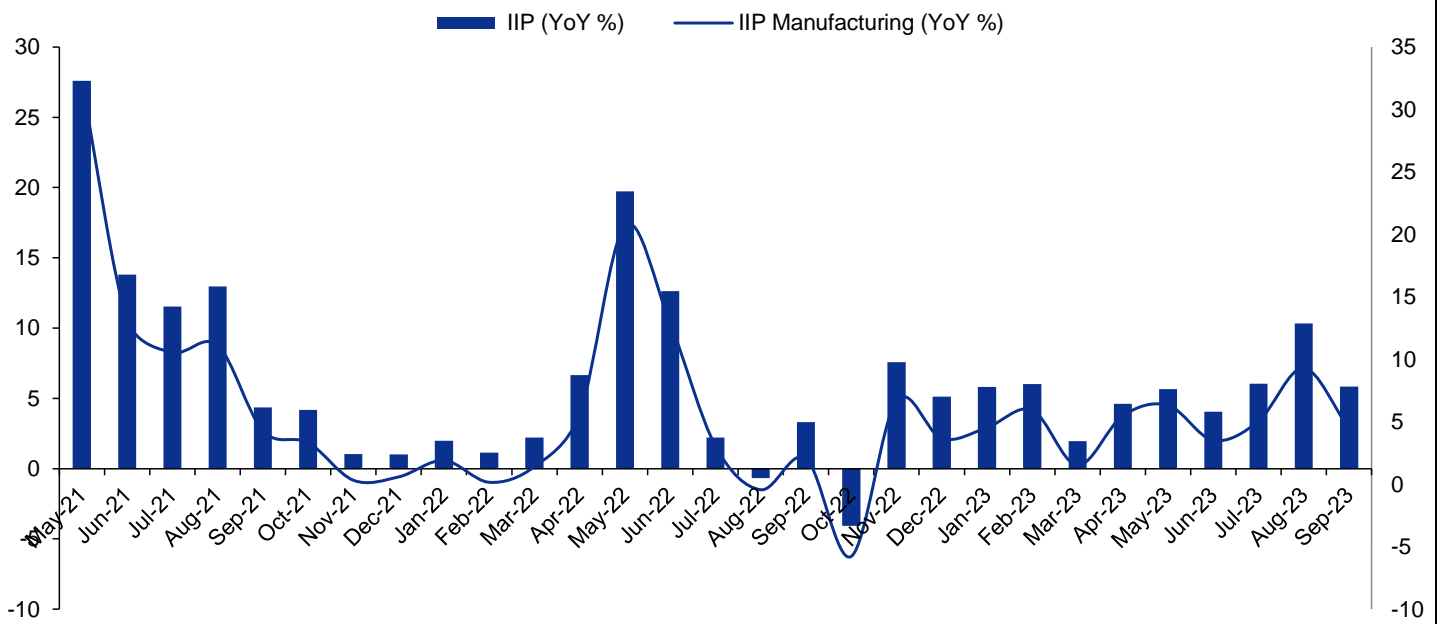
- Management commentaries were positive on the margin expansion front for most companies. L&T's margin was impacted due to legacy orders, which are likely to get completed by 3QFY24F. Margins of the projects and manufacturing businesses are expected at 8.5-9% in FY24F.
- KEC International expects its EBITDA margin to improve from 4.8% in FY23 to 7% in FY24F, as legacy projects of SAE Towers in Brazil have been completed and margin recovery is likely in the standalone T&D segment in 2HFY24F. Voltas expects margin expansion in the coming quarters led by softening commodity prices, manufacturing efficiency and value engineering initiatives.
- Thermax is likely to sustain its higher margin at 8-9% based on the current order book. ABB India expects its PBT margin of 10%+ to sustain, given softening commodity prices, while maintaining the overall pricing level. Cummins India has taken multiple price hikes in the last 15 months.

Figure 2: Total capex in India grew 15% in 1HFY24



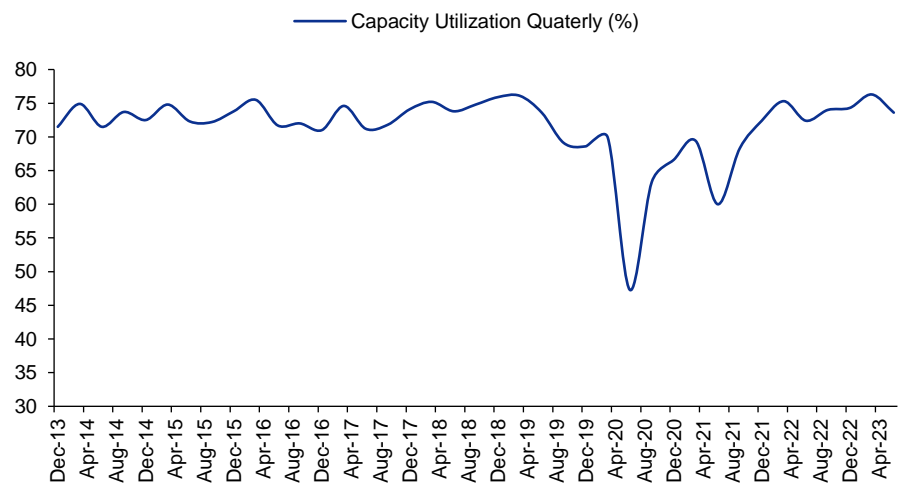
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 3: Index of Industrial Production or IIP growth trend



SOURCE: INCRED RESEARCH, BLOOMBERG

Figure 4: Capacity utilization trend



SOURCE: INCRED RESEARCH, RBI

Top five sectors accounted for 58% of total capex in 1HFY24

Figure 5: Dependence on the oil & gas sector for capex reduces to 27% in 1HFY24 from 35% in FY21

Sector	M-Cap (Rs m)	Capex								Capex Growth				
		1HFY24	1HFY23	FY23	FY22	FY21	FY20	FY19	1HFY24	FY23	FY22	FY21	FY20	
Crude Oil	2,18,49,742	9,48,522	9,25,594	20,27,075	15,88,271	15,72,406	14,76,490	14,05,193	25%	28%	1%	6%	5%	
Power	1,28,23,135	3,57,505	2,85,527	5,87,081	6,62,237	5,00,157	4,33,597	5,57,146	25%	-11%	32%	15%	-22%	
Automobile & Ancillaries	2,13,69,157	2,69,948	2,12,476	4,64,640	4,03,790	3,61,730	4,85,145	5,41,569	27%	15%	12%	-25%	-10%	
Iron & Steel	67,72,847	2,37,507	1,89,328	4,24,194	2,93,927	2,12,464	2,90,087	2,35,796	25%	44%	38%	-27%	23%	
Telecom	76,78,064	2,05,879	1,64,003	3,22,545	3,49,148	3,15,564	2,93,849	3,65,368	26%	-8%	11%	7%	-20%	
Non - Ferrous Metals	38,29,429	1,75,887	1,42,480	2,86,511	2,05,254	1,63,689	1,95,410	1,95,973	23%	40%	25%	-16%	0%	
Construction Materials	73,08,737	1,35,275	1,63,552	2,62,472	1,88,719	1,08,375	1,24,184	1,02,433	-17%	39%	74%	-13%	21%	
Bank	4,31,60,903	1,28,607	90,680	2,49,608	1,92,816	1,80,199	1,70,755	1,47,620	42%	29%	7%	6%	16%	
Chemicals	1,25,77,371	1,14,957	1,11,483	2,25,605	1,80,627	1,20,705	1,59,745	1,58,208	3%	25%	50%	-24%	1%	
Healthcare	1,30,61,686	1,06,147	95,463	2,02,427	1,76,130	1,49,883	1,56,633	1,70,714	11%	15%	18%	-4%	-8%	
Inds. Gases & Fuels	17,64,414	1,00,924	45,716	1,04,606	73,562	59,154	94,103	81,583	121%	42%	24%	-37%	15%	
Diversified	22,04,202	1,00,114	71,689	1,47,348	1,03,992	49,445	69,854	58,882	40%	42%	110%	-29%	19%	
Mining	29,53,574	84,587	64,330	1,60,476	1,33,163	1,26,740	78,769	86,724	31%	21%	5%	61%	-9%	
FMCG	2,20,25,277	66,342	62,375	1,16,959	96,270	69,860	88,817	75,214	6%	21%	38%	-21%	18%	
Infrastructure	71,11,532	54,497	51,418	1,16,816	87,320	56,292	1,44,387	1,43,216	6%	34%	55%	-61%	1%	
IT	3,37,28,646	51,747	67,611	1,28,567	1,28,144	1,09,218	1,30,117	1,29,325	-23%	0%	17%	-16%	1%	
Realty	24,16,929	44,469	37,380	75,747	81,397	73,631	84,144	76,662	19%	-7%	11%	-12%	10%	
Finance	2,67,79,434	43,756	60,348	55,203	38,344	21,226	67,288	59,800	-27%	44%	81%	-68%	13%	
Capital Goods	1,19,84,727	42,173	30,324	74,038	56,616	40,187	56,631	56,337	39%	31%	41%	-29%	1%	
Media & Entertainment	12,27,667	39,949	11,508	37,439	26,436	11,361	15,344	19,973	247%	42%	133%	-26%	-23%	
Textile	21,14,546	25,076	28,128	56,189	50,474	24,515	30,775	39,917	-11%	11%	106%	-20%	-23%	
Agri	18,06,681	24,288	28,412	54,223	39,961	21,205	25,526	29,675	-15%	36%	88%	-17%	-14%	
Retailing	44,94,061	22,735	17,210	40,587	36,509	25,922	27,207	23,713	32%	11%	41%	-5%	15%	
Gas Transmission	8,66,436	22,399	21,409	41,999	46,415	28,349	19,963	15,810	5%	-10%	64%	42%	26%	
Plastic Products	12,51,327	15,405	18,304	35,314	33,012	24,537	25,432	30,182	-16%	7%	35%	-4%	-16%	
Logistics	11,40,414	15,107	8,904	28,381	25,996	23,470	23,336	30,468	70%	9%	11%	1%	-23%	
Hospitality	19,47,501	10,626	6,036	16,101	7,842	6,381	13,060	12,393	76%	105%	23%	-51%	5%	
Consumer Durables	17,64,517	9,793	10,662	20,054	14,488	6,555	12,414	11,931	-8%	38%	121%	-47%	4%	
Paper	1,43,878	8,257	4,698	10,721	10,410	6,982	6,670	6,580	76%	3%	49%	5%	1%	
Electricals	11,28,403	6,480	2,485	6,543	6,357	2,719	4,631	5,304	161%	3%	134%	-41%	-13%	
Diamond & Jewellery	33,36,695	4,564	2,377	5,299	2,787	1,921	3,844	3,546	92%	90%	45%	-50%	8%	
Aviation	11,18,681	3,996	2,832	5,698	3,469	4,369	10,883	17,116	41%	64%	-21%	-60%	-36%	
Miscellaneous	4,91,542	3,843	2,682	6,641	5,969	4,660	7,532	6,714	43%	11%	28%	-38%	12%	
Insurance	47,82,215	3,515	2,100	5,622	4,939	4,279	5,891	5,383	67%	14%	15%	-27%	9%	
Abrasives	5,00,048	2,216	3,547	4,664	6,905	1,567	1,906	1,718	-38%	-32%	341%	-18%	11%	
Alcohol	12,24,562	1,987	2,212	3,858	3,473	3,720	6,330	6,449	-10%	11%	-7%	-41%	-2%	
Trading	4,35,006	1,374	1,845	3,456	3,109	1,138	2,312	1,825	-26%	11%	173%	-51%	27%	
Business Services	2,62,885	925	768	1,465	1,263	937	1,034	993	20%	16%	35%	-9%	4%	
Ship Building	2,61,598	416	337	873	2,294	2,170	1,053	1,103	23%	-62%	6%	106%	-4%	
Ferro Manganese	33,146	202	73	88	1,002	7	46	75	175%	-91%	14008%	-84%	-39%	
Ratings	3,64,487	139	218	502	280	384	331	382	-36%	79%	-27%	16%	-13%	
Photographic Product	449	0	8	10	9	5	116	6	-99%	11%	70%	-95%	1771%	
Education & Training	10,046	-102	50	28	195	3	176	141	-306%	-86%	6850%	-98%	25%	
Total Capex	29,21,06,596	34,92,030	30,48,577	64,17,672	53,73,320	44,98,080	48,45,813	49,19,158	15%	19%	19%	-7%	-1%	

SOURCE: INCRED RESEARCH, COMPANY REPORTS

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