AAG

Market Impact

February 10, 2016

Company	Rating	Impact on Company
Crompton Greaves (Rs.128)	Buy	Negative

Brief:

- Crompton Greaves Ltd reported weak set of numbers for Q3FY16.
- Consolidated revenue for the quarter fell by 14.2% YoY to Rs.20.68 bn.
- EBITDA for the quarter fell by 86.3% YoY to Rs.86 mn.
- EBITDA margin came in at 0.4% against 2.6% in Q3FY15.
- Company reported net loss of Rs.1.07 bn.
- **We continue to recommend a BUY on the stock with a revised target price of Rs.179 based on SOTP method, valuing Power and Industrial business at Rs.43 (14xFY18E EPS of Rs.3.1) and Consumer business at Rs.135 (25xFY18E EPS of Rs.5.4).**

Our Comments

Crompton Greaves Ltd (CGL) reported weak set of numbers for Q3FY16. Total Revenue (Ex. Demerged Consumer Business) for the quarter fell by 14.2% YoY to Rs.20.68 bn, due to weak performance in the Power System segment of the company. EBITDA for the quarter fell by 86.3% YoY to Rs.86 mn. The EBITDA margin came in at 0.41% against 2.6% in Q3FY15, due to weak performance in the Power segment. Hence, due to weak operating performance, Company reported loss of Rs.1.07 bn. On Consolidated basis (incl. Consumer business), revenue was down by 8.4% YoY to Rs.28.80 bn and loss came in at Rs.658.5 mn.

As announced earlier, the Consumer Business (23% contribution to the total revenue in FY15) of the company has been demerged from 1st October 2015 onwards and a new company “Crompton Greaves Consumer Electrical Ltd” (CGCEL) has been formed. Revenue for CGCEL for the quarter grew by 12.0% YoY to Rs.8.1 bn. EBIT margin improved by 50bps YoY to 12.3%. Company reported PAT of Rs.411.8 mn for Q3FY16. As per the demerged scheme, CGCEL will have equity capital of Rs.1.25 bn and debt of Rs.7 bn. The fixed assets are worth Rs.800 mn, having been transferred at their book value. Further, the business operates with a negative working capital cycle. With demerger, goodwill worth Rs7.5bn has been created while the cash stands at Rs.500 mn at the end of Q3FY16. Management stated that CGCEL is likely to list in April 2016 and will issue equity shares in the ratio of 1:1 to existing equity share holders of CGL as on the record date, which will be determined at a later date.

Power System segment revenue fell by 18.9% YoY to Rs.15.91 bn and Company reported an EBIT loss of Rs.384 mn during the quarter. This was largely on the back of weak execution in the domestic and international markets. The Company has been in the process of selling its International Power System business (contributes ~60% to the total Power System business) due to consistent losses. This has also impacted the order inflow and execution of the existing orders. The management stated that the planned sale of the International power business has hit a roadblock as the binding offer made by the buyer is not acceptable to the CGL management. The timelines of the closure of the deal are now uncertain. However management would continue to focus on turning around the loss making subsidiaries.

The Industrial Segment of the Company reported revenue growth of 4.5% YoY to Rs.4.75 bn due to improved execution. EBIT margin improved by 130bps YoY to 7.5%. Management highlighted that they are seeing a revival in demand for large/small motors.

CGL has announced that Mr. Laurent Demortier will be stepping down as the CEO and MD of the company with effect from 3rd February 2016 and will be replaced by Mr. K.N Neelkanth, who will take in charge of the domestic power systems business and industrial systems business including the rotating machines, drives and automation business in India and Europe.

While Q3FY16 numbers were a major disappointment, CGL continues to focus on restructuring the key businesses of the company. The current environment for Power business remains weak; however management is hopeful of uptick in the orders from DISCOMs due to the government’s recent initiative UDAY. On the Consumer business, the company is planning to focus on (1) Brand investments, (2) Product innovation, (3) Strengthening distribution, especially via modern trade and ecommerce and (4) Systems and process overhaul, which is likely to result in higher growth in the revenue and earnings. Also, the management is likely to maintain the asset-light business model (currently 50% is manufactured in-house and 50% is outsourced) and foresees plenty of scope for organic growth. Product-wise, small appliances and consumer LED offers large growth potential, while it aims to sustain market leadership position in fans. Based on the current performance, we have revised earnings and also rolled over to FY18. We continue to recommend a BUY on the stock with a revised target price of Rs.179 based on SOTP method, valuing Power and Industrial business at Rs.43 (14xFY18E EPS of Rs.3.1) and Consumer business at Rs.135 (25xFY18E EPS of Rs.5.4). Any change in the earnings/target price would depend upon the order inflow & execution, change in the management’s strategy on the international business and general business momentum.

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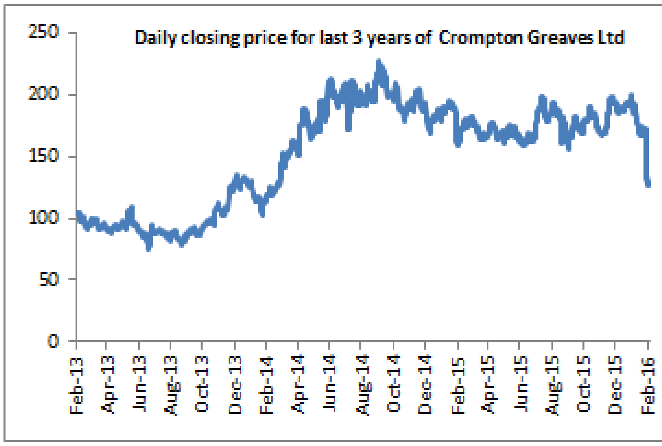

Rating Interpretation	
Rating	**Expected to**
Buy	Appreciate more than 10% over a 12 to 15 month period
Hold	Appreciate below 10% over a 12 to 15 month period
Under Review	Rating under review
Exit	Exited out of the Model Portfolio

Source: Bloomberg

Disclosures:

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