

SELL
 TP: Rs 4,200 | ▼ 26%

HITACHI ENERGY

Capital Goods

24 January 2024

In-line quarter but valuations overdone; cut to SELL

- Q3 EBITDA margin rose 150bps YoY to 5.3% as chip constraints eased, leading to 5x jump in PAT off a low base
- Management retains guidance of double-digit margins by end-FY25 led by HVDC, rail and export orders
- Stock has rallied sharply by 70% in FY24 YTD and current P/E of 65x on Dec'25E looks overstated – cut from HOLD to SELL

Vinod Chari | Arshia Khosla
 Swati Jhunjhunwala
 research@bobcaps.in

Improved YoY numbers: Hitachi's Q3FY24 revenue grew 23% YoY to Rs 12.7bn, and the easing chip shortage aided 150bps YoY improvement in EBITDA margin to 5.3% (flat QoQ). PAT came in at Rs 230mn compared to Rs 46mn on a YoY basis.

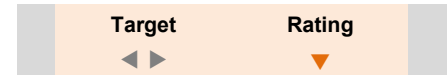
Chip constraints reduce: The company has been plagued by chip shortages over the past few quarters, but management indicated that supply chain constraints have receded in Q3 and it is now equipped to better manage the same.

Good order inflow mix: Q3 order intake was flat at 1% YoY to Rs 12.3bn with 25% export share, taking the backlog to Rs 75.5bn which signifies 22 months of revenue visibility. This compares well with the Rs 75.9bn backlog in Q2FY24 and Rs 70.7bn in FY23. Transmission projects from multiple state utilities, renewable orders, Chennai metro rail, data centre and hydropower orders, along with exports to Africa, the Middle East and Europe drove the inflows. This mix of export and service orders augurs well for margins in coming quarters.

Guidance retained: Management maintained its guidance of reaching a double-digit EBITDA margin run-rate by the close of FY25.

Valuations overstated; cut to SELL: We remain positive on Hitachi's order prospects but lower our FY24/FY25/FY26 EPS estimates by 35%/11%/9% to reflect the below-expected 9MFY24 performance. Our TP remains at Rs 4,200 as we roll valuations forward to Dec'25E and reset to a 48x target P/E from 45x earlier to maintain our 50% valuation premium to the stock's three-year average. The stock has run up 27% since our **last quarterly update** of 6 Nov 2023, propelling valuations to 65x Dec'25E EPS, which we believe look overdone given the tepid margin performance so far. We downgrade the stock from HOLD to SELL and await a better entry point.

Key changes



Ticker/Price	POWERIND IN/Rs 5,673
Market cap	US\$ 2.9bn
Free float	25%
3M ADV	US\$ 2.7mn
52wk high/low	Rs 6,280/Rs 2,906
Promoter/FPI/DII	75%/5%/2%

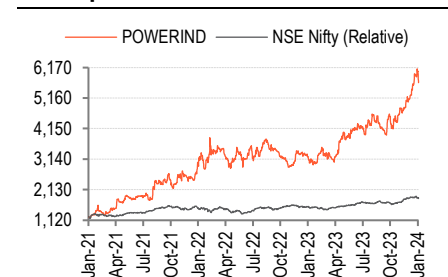
Source: NSE | Price as of 24 Jan 2024 | POWERIND = Hitachi

Key financials

Y/E 31 Mar	FY23A	FY24E	FY25E
Total revenue (Rs mn)	44,685	51,160	61,520
EBITDA (Rs mn)	2,359	3,029	5,487
Adj. net profit (Rs mn)	939	1,370	3,138
Adj. EPS (Rs)	22.2	32.3	74.0
Consensus EPS (Rs)	22.2	58.0	95.0
Adj. ROAE (%)	8.0	10.7	21.1
Adj. P/E (x)	256.1	175.6	76.6
EV/EBITDA (x)	101.7	79.0	43.9
Adj. EPS growth (%)	(44.0)	45.9	129.1

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE

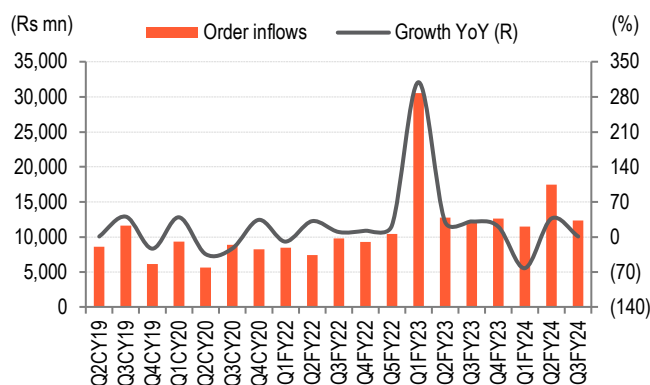


Fig 1 – Quarterly performance

Particulars (Rs mn)	Q3FY24	Q3FY23	YoY (%)	Q2FY24	QoQ (%)	9MFY24	9MFY23	YoY (%)
Revenue	12,742	10,339	23.2	12,280	3.8	35,422	31,345	13.0
EBITDA	680	395	72.4	653	4.1	1,670	1,409	18.6
EBITDAM (%)	5.3	3.8	150bps	5.3	0bps	4.7	4.5	20bps
Depreciation	227	202		225		675	591	
Interest	137	130		107		354	289	
Other Income	22	71		2		54	129	
PBT	338	134	152.5	324	4.4	695	657	5.8
Tax	108	88		76		194	226	
Adjusted PAT	230	46	401.5	247	(7.2)	501	431	16.3
Exceptional item	0	0		0		0	0	
Reported PAT	230	46	401.5	247	(7.2)	501	431	16.3
Adj. PATM (%)	1.8	0.4	140bps	2.0	(20bps)	1.4	1.4	0bps
EPS (Rs)	5.4	1.1	401.5	5.8	(7.2)	11.8	10.2	16.3

Source: Company, BOBCAPS Research

Fig 2 – Order backlog



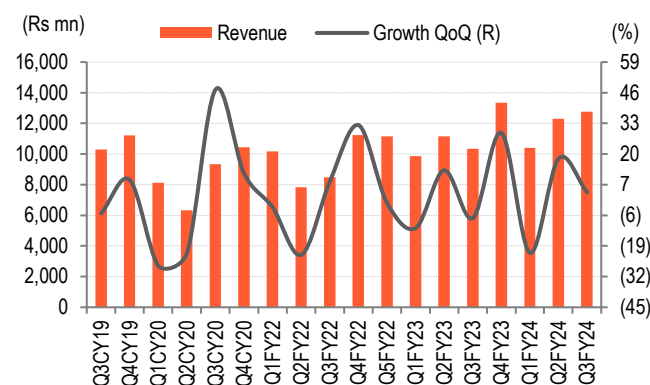
Source: Company, BOBCAPS Research

Fig 3 – Order inflow



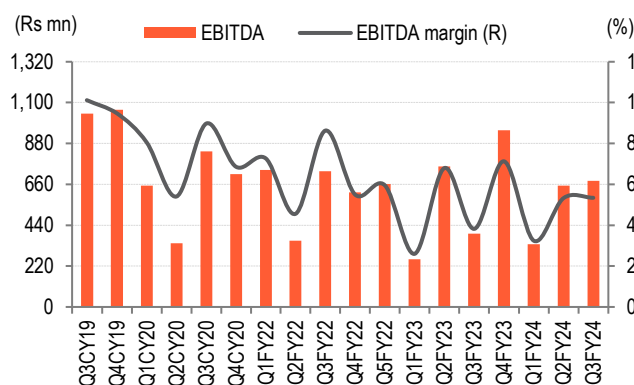
Source: Company, BOBCAPS Research

Fig 4 – Revenue growth



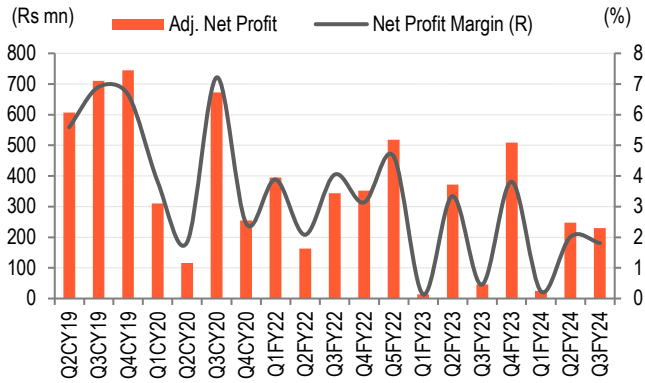
Source: Company, BOBCAPS Research

Fig 5 – EBITDA growth



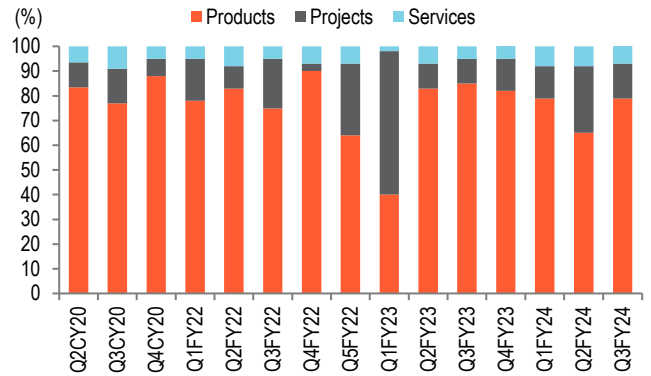
Source: Company, BOBCAPS Research

Fig 6 – Net profit growth



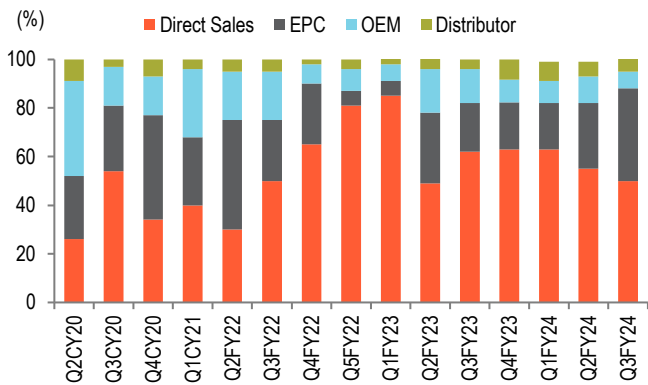
Source: Company, BOBCAPS Research

Fig 7 – Order inflows by segment



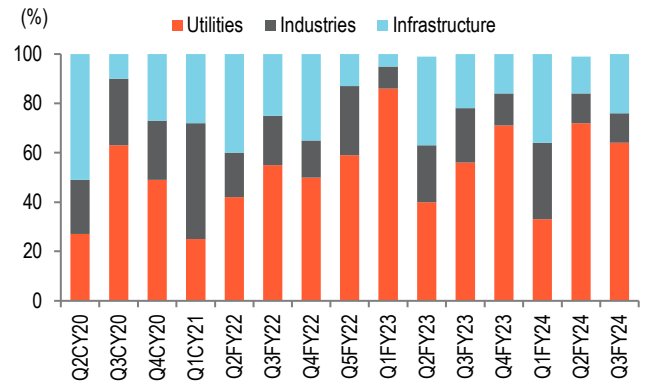
Source: Company, BOBCAPS Research

Fig 8 – Order inflows by channel



Source: Company, BOBCAPS Research

Fig 9 – Order inflows by sector



Source: Company, BOBCAPS Research

Earnings call highlights

- Opportunities:** Management sees high-voltage direct current (HVDC) lines as a large domestic opportunity and expects at least two projects to be awarded in the next 12 months. A typical HVDC project is worth Rs 80bn-100bn, half of which would constitute Hitachi’s addressable market. The company sees further transmission opportunities from the 35 tariff-based competitive bidding (TBCB) projects awarded so far in FY24. In railways, demand from high-speed rail, locomotives and trainsets continues, while data centres are a nascent but fast-growing market.
- Order book:** Hitachi’s order book grew 4% YoY to Rs 75.5bn in Q3FY24 and provides revenue visibility of 22 months. Per management, inflows from renewable projects continue to accelerate. The company also saw 92% growth in data centre orders, where the government is pushing for 5G data localisation. Transmission orders were stable while inflows from the railways slowed during the quarter. On the channel side, engineering, procurement & construction or EPC-related orders led the pack (as compared to the direct end user, OEM and distributor segments).

Service orders, accounting for 9-10% of the book, grew 70% YoY driven by the utilities industry. Export orders, which account for 25% of the book, grew 61% YoY led by demand for transformers in European & African markets and for quality

power products (high-voltage) in South and Central America, Africa, the US and Europe.

- **Profitability:** Hitachi reported a 6.3% operational EBITDA margin (100bps currency impact led to 5.3% accounting EBITDA margin) in Q3FY24 and expects margins to improve as exports and service orders are increasing in the mix. Further, its greenfield factories are ramping up utilisation. Geopolitical risks such as transport hurdles through the Red Sea amid the war between Israel and Hamas do pose risks to its export operations.
- **Capacity utilisation:** Utilisation for the quarter swung between 75% and 90% for different factories, with newly commissioned units operating at lower rates.
- **Progress in ongoing projects/bids:** (a) The Leh-Ladakh feasibility study for Power Grid is on track and scheduled to be completed by FY24-end. (b) The bullet train bid is expected to be finalised in the next 1-2 quarters. (c) The Mumbai HVDC project is on track and expected to be completed by Q1FY26.

Valuation methodology

We remain positive on Hitachi's order prospects but cut our FY24/FY25/FY26 EPS estimates by 35%/11%/9% to reflect the below-expected 9MFY24 performance. Our TP remains at Rs 4,200 as we roll valuations forward to Dec'25E and reset to a 48x target P/E from 45x earlier to maintain our 50% valuation premium to the stock's three-year average.

The stock has rallied 27% since our [last quarterly update](#) of 6 Nov 2023, propelling valuations to 65x Dec'25E EPS, which we believe look overdone given the tepid margin performance thus far. Hitachi has also run up ~35% since our [last downgrade](#) (from BUY to HOLD) on 25 Jul 2023. We now lower our rating from HOLD to SELL and await a better entry point.

Fig 10 – Revised estimates

Particulars (Rs mn)	New			Old			Change (%)		
	FY24E	FY25E	FY26E	FY24E	FY25E	FY26E	FY24E	FY25E	FY26E
Sales	51,160	61,520	69,949	56,851	66,149	73,716	(10.0)	(7.0)	(5.1)
EBITDA	3,029	5,487	6,504	4,013	5,967	6,946	(24.5)	(8.0)	(6.4)
PAT	1,370	3,138	3,903	2,094	3,541	4,279	(34.6)	(11.4)	(8.8)
EPS	32.3	74.0	92.1	49.4	83.5	101.0	(34.6)	(11.4)	(8.8)
EBITDAM (%)	5.9	8.9	9.3	7.1	9.0	9.4	(110bps)	(10bps)	(10bps)

Source: Company, BOBCAPS Research

Key risks

Key upside risks to our estimates are:

- faster recovery in T&D capex than estimated,
- speedy resolution of the chip shortage, and
- hitting double-digit margins earlier than the guided timeline of end-FY25.

Financials

Income Statement

Y/E 31 Mar (Rs mn)	FY22A	FY23A	FY24E	FY25E	FY26E
Total revenue	48,840	44,685	51,160	61,520	69,949
EBITDA	3,107	2,359	3,029	5,487	6,504
Depreciation	955	802	931	943	954
EBIT	2,152	1,558	2,097	4,544	5,551
Net interest inc./(exp.)	414	401	500	500	500
Other inc./(exp.)	669	151	136	150	165
Exceptional items	0	0	0	0	0
EBT	2,407	1,308	1,734	4,194	5,215
Income taxes	732	369	364	1,056	1,313
Extraordinary items	(359)	0	0	0	0
Min. int./Inc. from assoc.	0	0	0	0	0
Reported net profit	2,034	939	1,370	3,138	3,903
Adjustments	(359)	0	0	0	0
Adjusted net profit	1,676	939	1,370	3,138	3,903

Balance Sheet

Y/E 31 Mar (Rs mn)	FY22A	FY23A	FY24E	FY25E	FY26E
Accounts payables	16,190	15,146	16,820	19,383	22,039
Other current liabilities	5,915	8,648	11,213	13,484	15,331
Provisions	0	0	0	0	0
Debt funds	1,250	2,750	3,148	3,786	4,305
Other liabilities	560	488	559	672	764
Equity capital	85	85	85	85	85
Reserves & surplus	11,239	12,068	13,290	16,258	19,991
Shareholders' fund	11,324	12,153	13,374	16,343	20,076
Total liab. and equities	35,239	39,185	45,115	53,668	62,515
Cash and cash eq.	859	1,633	3,601	6,230	9,680
Accounts receivables	13,438	15,278	20,324	24,439	27,788
Inventories	7,073	8,179	6,307	6,742	7,666
Other current assets	5,443	5,629	6,307	7,585	8,624
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	45,115	53,668	62,515

Cash Flows

Y/E 31 Mar (Rs mn)	FY22A	FY23A	FY24E	FY25E	FY26E
Cash flow from operations	(1,267)	54	2,687	3,088	4,048
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	31	73	52
Cash flow from investing	(1,670)	(118)	(969)	(927)	(948)
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	1,250	1,500	398	638	519
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	250	468	349
Chg in cash & cash eq.	(2,331)	773	1,968	2,629	3,450
Closing cash & cash eq.	859	1,633	3,601	6,230	9,680

Per Share

Y/E 31 Mar (Rs)	FY22A	FY23A	FY24E	FY25E	FY26E
Reported EPS	48.0	22.2	32.3	74.0	92.1
Adjusted EPS	39.5	22.2	32.3	74.0	92.1
Dividend per share	3.0	3.4	3.5	4.0	4.0
Book value per share	267.2	286.8	315.6	385.6	473.7

Valuations Ratios

Y/E 31 Mar (x)	FY22A	FY23A	FY24E	FY25E	FY26E
EV/Sales	5.0	5.4	4.7	3.9	3.5
EV/EBITDA	78.4	101.7	79.0	43.9	37.3
Adjusted P/E	143.5	256.1	175.6	76.6	61.6
P/BV	21.2	19.8	18.0	14.7	12.0

DuPont Analysis

Y/E 31 Mar (%)	FY22A	FY23A	FY24E	FY25E	FY26E
Tax burden (Net profit/PBT)	69.6	71.8	79.0	74.8	74.8
Interest burden (PBT/EBIT)	111.9	84.0	82.7	92.3	94.0
EBIT margin (EBIT/Revenue)	4.4	3.5	4.1	7.4	7.9
Asset turnover (Rev./Avg TA)	139.0	120.1	121.4	124.6	120.4
Leverage (Avg TA/Avg Equity)	3.4	3.2	3.3	3.3	3.2
Adjusted ROAE	16.2	8.0	10.7	21.1	21.4

Ratio Analysis

Y/E 31 Mar	FY22A	FY23A	FY24E	FY25E	FY26E
YoY growth (%)					
Revenue	42.8	(8.5)	14.5	20.2	13.7
EBITDA	23.8	(24.1)	28.4	81.2	18.5
Adjusted EPS	33.2	(44.0)	45.9	129.1	24.4
Profitability & Return ratios (%)					
EBITDA margin	6.4	5.3	5.9	8.9	9.3
EBIT margin	4.4	3.5	4.1	7.4	7.9
Adjusted profit margin	3.4	2.1	2.7	5.1	5.6
Adjusted ROAE	16.2	8.0	10.7	21.1	21.4
ROCE	18.1	12.3	15.1	26.7	26.6
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	4.0	4.4	4.7
Current ratio	1.1	1.2	1.2	1.2	1.3
Net interest coverage ratio	5.2	3.9	4.2	9.1	11.1
Adjusted debt/equity	0.0	0.1	0.0	(0.1)	(0.3)

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

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 Registered office Address: **1704, B Wing, Parinee Crescenzo, G Block, BKC, Bandra East, Mumbai 400051**
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BUY – Expected return >+15%

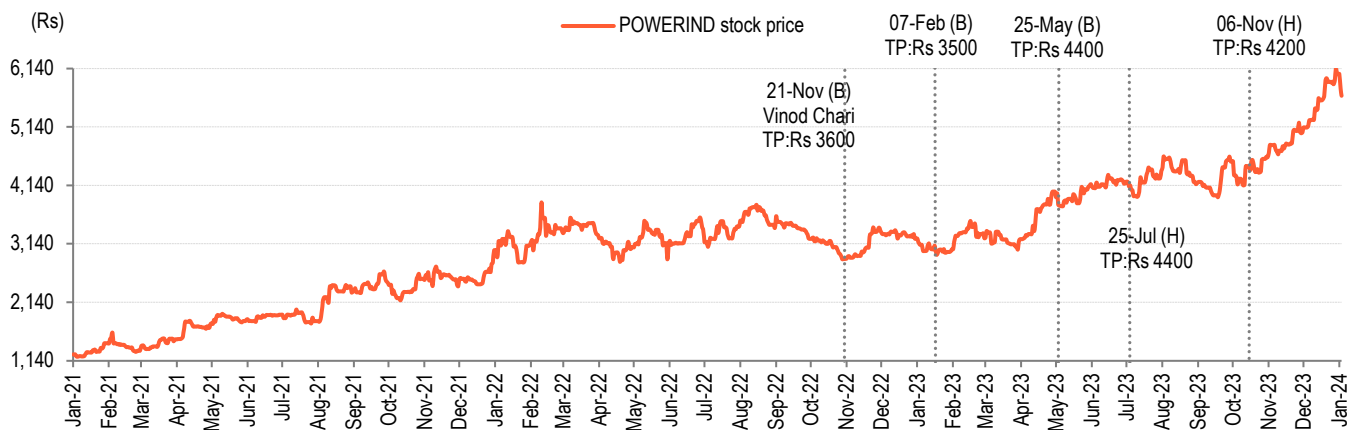
HOLD – Expected return from -6% to +15%

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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