

HAVELLS INDIA

Local gain, global pain

India Equity Research | Engineering and Capital Goods



We recently interacted with Havells India's (HAVL) senior management at an analyst meet and also visited its manufacturing facilities at Baddi (Himachal Pradesh) and Neemrana (Rajasthan). During our interaction, management exuded confidence regarding the domestic business. The company expects existing products to fuel 15-20% growth in FY13-14 and new launches to further augment it. However, tough macros are clouding its international business horizon. Hence, the company is eyeing a modest 7-9% revenue growth along with double digit margin over the medium term in Sylvania, even as near-term challenges stay put. We maintain 'HOLD' with revised target price of INR 585 (INR537 earlier).

Resilient domestic business; new launches to fuel growth

Management is confident of resilience of the domestic business. It expects existing products to generate revenue growth of 15-20% in FY13-14, which will be further augmented by new launches. Also, on the anvil are ~200 Havells Galaxy stores over the next two years. Another positive is the capping of royalty payment at INR400mn/year. In the dealer interactions, HAVL was rated the most dealer-friendly company, another feather in its already overcrowded cap.

Tough macros taking a toll on international business

Tough macros in Europe are clouding HAVL's international business horizon. Ergo, management commentary on Sylvania was muted. While near-term concerns persist, HAVL is targeting a modest 7-9% revenue growth along with double digit margin over the medium term. The company did not share a detailed roadmap to achieve the same. We expect price hike taken in September to aid margin expansion.

Outlook and valuations: Challenging; maintain 'HOLD'

While the domestic business seems to be on the right track with HAVL increasing its market penetrations/ share, profitability of its international operations remains the primary concern. We continue to believe that the pain in Europe is unlikely to subside soon. On a consolidated EPS, the stock is trading at 21.7x and 16.0x FY13E and FY14E, respectively. We maintain 'HOLD/ Sector Performer' with revised TP of INR 585.

Financials (Consol)

Year to March	FY11	FY12	FY13E	FY14E
Revenues (INR mn)	56,126	65,182	72,517	82,019
Growth (%)	3.8	10.8	11.8	12.8
EBITDA (INR mn)	5,571	6,573	6,842	8,163
Net profit (INR mn)	3,099	3,699	3,543	4,783
Shares outstanding (mn)	125	125	125	125
Diluted EPS (INR)	24.6	29.7	28.4	38.3
Diluted P/E (X)	25.0	20.7	21.7	16.0
EV / EBITDA (X)	15.5	12.6	12.4	10.4
ROAE (%)	58.3	46.0	32.6	34.2

EDELWEISS 4D RATINGS

Absolute Rating	HOLD
Rating Relative to Sector	Performer
Risk Rating Relative to Sector	Medium
Sector Relative to Market	Overweight

MARKET DATA (R: HVEL.BO, B: HAVL IN)

CMP	: INR 616
Target Price	: INR 585
52-week range (INR)	: 708 / 365
Share in issue (mn)	: 124.8
M cap (INR bn/USD mn)	: 77/ 1,401
Avg. Daily Vol.BSE/NSE('000)	: 323.5

SHARE HOLDING PATTERN (%)

	Current	Q1FY13	Q4FY12
Promoters*	61.6	61.6	61.6
MF's, FI's & BK's	1.1	0.9	1.1
FII's	20.0	20.0	19.8
Others	17.4	17.5	17.5

* Promoters pledged shares : NIL
(% of share in issue)

PRICE PERFORMANCE (%)

	Stock	Nifty	EW Capital Goods Index
1 month	2.8	3.4	12.5
3 months	3.7	5.4	2.5
12 months	41.3	23.4	(14.2)

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Domestic standalone business

Overall guidance maintained

HAVL sounded confident as far as its domestic business is concerned and also maintained its FY13-14 revenue guidance of 15-20% from existing products. New launches are likely to supplement this growth.

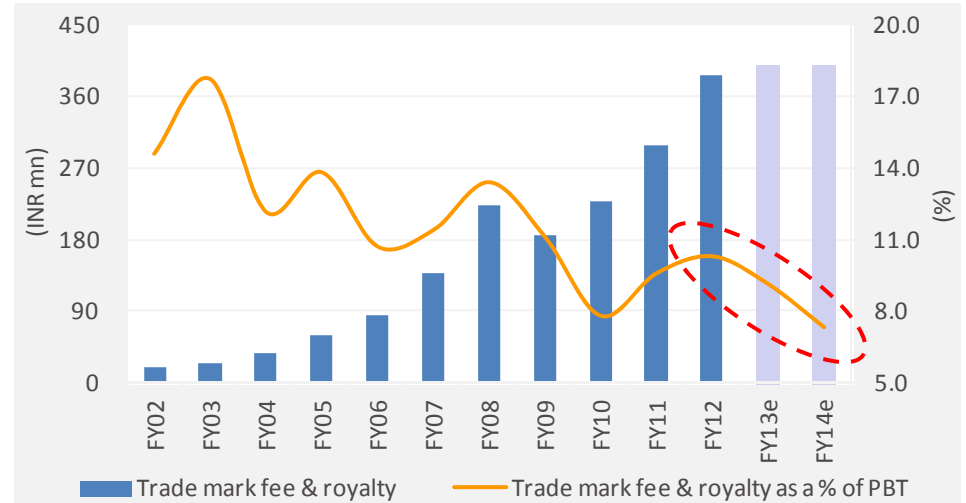
New economy range of switches to fuel growth

HAVL recently launched (two months ago) *REO*, an economy range of switches, which could help it tap ~95% of the switchgear market (geography wise, beyond tier 3-4 towns/cities). The product has already garnered a turnover of INR50mn/ month, which the management targets to raise to INR100mn/ month over the following six months. Ergo, HAVL is eyeing a turnover of INR~1bn in FY14E itself.

Royalty payment to promoter group capped

The *Havells* brand was bought by the promoter group company in early seventies. HAVL has been paying royalty/ trade mark payment to the promoter group entity, which had been capped at 1% of sales and 10% of PBT. During FY12, the company paid INR385mn to the promoter entity. The former stated that royalty/ trade mark payment has now been capped at INR 400mn/year.

Chart 1: Trade mark fees and royalty payment trend



Source: Company, Edelweiss research

Sylvania: Facing turbulence

Management was less vocal on Sylvania’s performance given the tough macros, especially in Europe. While near-term concerns persist, the company is targeting 7-9% revenue growth along with double digit margin over the medium term. However, the company did not share a detailed roadmap of how it plans to achieve the same. Price hike taken in September is likely to aid margin expansion. HAVL plans to sharpen its focus on newer markets like China and Africa. It also continues to scout for acquisitions to aid footprint expansion.

Company Description

Incorporated in 1983, HAVL is one of the largest and fastest growing manufacturers of electrical components and systems in India. It is the market leader in light-duty power distribution products. Its offerings include electrical products like circuit protection equipment (domestic and industrial switchgears), cables and wires, and consumer durables like fans, CFLs, and lighting fixtures.

With the acquisition of Sylvania in April 2007, the company now has international presence and operations in over 50 countries. Sylvania is one of the world's largest manufacturers of artificial light sources. It has a broad product offering, from incandescent light bulbs, halogen and low-energy lamps for the consumer market, to fluorescent lamps, HID lamps and various special products for the professional specifier. It owns powerful brands like *Crabtree, Sylvania, Concord, Luminance, Linolite, and SLI Lighting*.

Investment Theme

We expect Havells to continue to grow its domestic business on the back of strong product portfolio. The company is currently one of the fastest growing fan brands in the Indian market with market share at ~15%. The company has launched innovative products with its energy efficient fans (consuming only 50W) making it the largest energy efficient fan in the country. In the switchgear market, HAVL is the market leader in the low voltage segment with ~ 28% share (market size INR 16 bn) with the largest manufacturing facility (48 mn pieces per annum) in the country. It has the second largest CFL manufacturing capacity in India at 50 mn annually. In India, the company has a network of ~7,000 distributors spread across the four regions servicing ~100,000 retailers/ touch points.

In the international business, we believe Sylvania having turnaround the business is on track to improve overall margins with growth primarily coming from emerging markets in Latin America and Asia including new markets. Any meaningful growth in The European region could provide significant operating leverage. At the same time, the current tough macros are likely to keep pressure on margin improvement.

Key Risks

Pickup in domestic business

Pickup in key consumer segments of construction and industrial capex could impact the domestic business. Lower-than-anticipated volume growth and higher price cuts in the domestic business are risks to our estimates. Also, slowdown in power T&D could impact the demand for its cables and wires business.

Pickup in international business mainly the European operations

Slowdown in the international business mainly Europe has put pressure on margins which had improved through the restructuring program adopted by the company. Any meaningful pickup in the operations and margin profile of the international business is an upside .

Financial Statements(Consolidated)

Key assumptions

Year to March	FY10	FY11	FY12	FY13E	FY14E
Macro -					
GDP(Y-o-Y %)	8.4	8.4	6.5	5.5	6.5
Inflation (Avg)	3.6	9.9	8.8	7.8	6.0
Repo rate (exit rate)	5.0	6.8	8.5	7.5	6.8
USD/INR (Avg)	47.4	45.6	47.9	53.5	52.0
Company - Revenue growth(%)					
Cables & Wires	(1.3)	27.6	15.2	21.0	21.0
Swithgears	15.8	11.6	12.7	29.0	20.0
Lighting and fixtures	33.4	28.4	16.3	25.0	20.0
Electrical consumer durables	29.9	39.5	14.7	41.0	24.0
EBIT DA Margins - %					
Standalone	12.6	11.8	12.6	12.1	12.2
Sylvania	2.6	5.8	8.3	5.5	6.0

Income statement

Year to March	FY10	FY11	FY12	FY13E	FY14E
Income from operations	54,315	56,126	65,182	72,517	82,019
Materials costs	32,430	35,753	36,272	43,799	49,583
Employee costs	7,645	6,405	7,904	6,971	7,308
Other manufacturing expenses	11,019	8,398	14,432	14,905	16,965
Total operating expenses	51,093	50,556	58,609	65,676	73,856
EBITDA	3,222	5,571	6,573	6,842	8,163
Depreciation & Amortization	837	804	949	1,201	1,258
EBIT	2,385	4,766	5,625	5,640	6,905
Other income	222	237	414	106	119
Interest expenses	979	902	1,281	1,310	968
Profit before tax	1,628	4,102	4,757	4,436	6,056
Provision for tax	932	1,031	1,058	893	1,273
Deferred taxes	266	559	556	556	556
Net profit	696	3,071	3,699	3,543	4,783
Extraordinary income/ (loss)	-	31	-	-	-
Profit After Tax	696	3,102	3,699	3,543	4,783
Profit after minority interest	696	3,099	3,699	3,543	4,783
Shares outstanding (mn)	125	125	125	125	125
Diluted EPS (INR)	5.6	24.6	29.7	28.4	38.3
Dividend payout (%)	38.9	11.8	25.6	21.1	20.9

Common size metrics - as % of net revenues

Year to March	FY10	FY11	FY12	FY13E	FY14E
Other manufacturing expenses (Growth)	20.3	15.0	22.1	20.6	20.7
EBITDA margins	5.9	9.9	10.1	9.4	10.0
Net profit margins	1.3	5.5	5.7	4.9	5.8

Growth ratios (%)

Year to March	FY10	FY11	FY12	FY13E	FY14E
Rev. growth (%)	(0.8)	3.3	16.1	11.3	13.1
EBITDA	11.7	72.9	18.0	4.1	19.3
Net profit	80.8	341.3	20.5	(4.2)	35.0

Balance sheet						(INR mn)
As on 31st March	FY10	FY11	FY12	FY13E	FY14E	
Equity capital	312	624	624	624	624	
Reserves & surplus	3,690	5,914	8,932	11,539	15,199	
Shareholders funds	4,002	6,537	9,556	12,163	15,823	
Minority interest (BS)	2	6	1	1	1	
Secured loans	9,963	10,473	7,343	7,843	8,343	
Unsecured loans	700	700	1,342	1,342	1,342	
Borrowings	10,664	11,173	8,685	9,185	9,685	
Sources of funds	14,934	18,275	18,798	21,905	26,065	
Gross block	26,963	28,454	27,577	28,577	29,577	
Depreciation	18,089	18,499	17,293	18,494	19,752	
Net block	8,874	9,955	10,284	10,082	9,824	
Capital work in progress	336	249	663	763	863	
Goodwill	3,212	3,354	3,625	3,625	3,625	
Inventories	8,250	10,860	13,678	14,214	17,298	
Sundry debtors	6,982	7,724	8,905	9,934	12,359	
Cash and equivalents	1,481	1,779	2,336	1,211	1,580	
Loans and advances	1,574	1,615	2,144	2,358	2,948	
Other current assets	102	100	120	132	165	
Total current assets	18,389	22,077	27,183	27,849	34,351	
Sundry creditors and others	15,555	16,722	17,860	19,478	21,474	
Provisions	321	639	5,096	936	1,123	
Total current liabilities & provisions	15,876	17,361	22,956	20,414	22,597	
Net current assets	2,513	4,717	4,227	7,436	11,754	
Uses of funds	14,934	18,275	18,798	21,905	26,065	
Book value per share (INR)	32.1	52.4	76.6	97.5	126.8	

Free cash flow						(INR mn)
Year to March	FY10	FY11	FY12	FY13E	FY14E	
Net profit	696	3,102	3,699	3,543	4,783	
Depreciation	837	804	949	1,201	1,258	
Deferred tax	331	99	2	-	-	
Others	(1,493)	522	1,171	1,310	968	
Gross cash flow	371	4,527	5,821	6,054	7,009	
Less: Changes in WC	(2,543)	1,998	1,204	4,333	3,949	
Operating cash flow	2,914	2,529	4,617	1,721	3,059	
Less: Capex	1,077	1,647	1,511	1,100	1,100	
Free cash flow	1,837	882	3,106	621	1,959	

Cash flow metrics					
Year to March	FY10	FY11	FY12	FY13E	FY14E
Operating cash flow	2,914	2,529	4,617	1,721	3,059
Investing cash flow	(1,061)	(1,762)	(1,053)	(1,100)	(1,100)
Financing cash flow	(2,858)	(654)	(2,568)	(1,746)	(1,591)
Net cash flow	(1,005)	113	996	(1,125)	369
Capex	(1,077)	(1,647)	(1,511)	(1,100)	(1,100)
Dividends paid	(226)	(207)	(363)	(936)	(1,123)

Engineering and Capital Goods

Profitability & efficiency ratios

Year to March	FY10	FY11	FY12	FY13E	FY14E
ROAE (%)	13.7	58.3	46.0	32.6	34.2
ROACE (%)	14.3	28.7	30.3	27.7	28.8
Inventory day	91	98	123	116	116
Debtors days	49	48	47	47	50
Payable days	166	165	174	156	151
Cash conversion cycle (days)	(26)	(19)	(4)	8	15
Current ratio	1.2	1.3	1.2	1.4	1.5
Debt/EBITDA	3.3	2.0	1.3	1.3	1.2
Debt/Equity	2.7	1.7	0.9	0.8	0.6
Adjusted debt/equity	2.7	1.7	0.9	0.8	0.6
Interest coverage	2.4	5.3	4.4	4.3	7.1

Operating ratios

Year to March	FY10	FY11	FY12	FY13E	FY14E
Total asset turnover	3.3	3.4	3.5	3.6	3.4
Fixed asset turnover	6.2	6.0	6.4	7.1	8.2
Equity turnover	10.7	10.7	8.1	6.7	5.9

Valuation parameters

Year to March	FY10	FY11	FY12	FY13E	FY14E
Diluted EPS (INR)	5.6	24.6	29.7	28.4	38.3
Y-o-Y growth (%)	74.4	341.3	20.5	(4.2)	35.0
CEPS (INR)	14.9	31.9	37.3	38.0	48.4
Diluted PE (x)	110.4	25.0	20.8	21.7	16.1
Price/BV (x)	19.2	11.8	8.0	6.3	4.9
EV/Sales (x)	1.6	1.5	1.3	1.2	1.0
EV/EBITDA (x)	26.7	15.5	12.7	12.4	10.4

Peer comparison valuations

Name of the companies	CMP (INR)	Market cap (USD mn)	PE (x)		P/BV (x)		ROE (%)	
			2013E	2014E	2013E	2014E	2013E	2014E
Havells (SA)	615	1,429	21.9	17.6	4.1	3.5	20.2	21.5
V Guard Industries	529	287	21.6	16.9	5.8	4.6	29.7	29.6
TTK Prestige	3,543	729	29.9	23.8	10.2	7.5	38.0	36.1
Bajaj Electricals	210	381	17.9	12.6	5.3	4.6	15.8	19.6

Source: Bloomberg, Edelweiss research

Company	Absolute reco	Relative reco	Relative risk	Company	Absolute reco	Relative reco	Relative Risk
ABB India	REDUCE	SU	L	Bajaj Electricals	HOLD	SP	M
BGR Energy	REDUCE	SU	M	Bharat Electronics	BUY	SO	H
Bharat Heavy Electricals	HOLD	SP	L	Crompton Greaves	HOLD	SP	M
Cummins India	BUY	SO	L	Havells India	HOLD	SP	M
Jyoti Structures	HOLD	SP	M	Kalpataru Power	HOLD	SP	M
KEC International	BUY	SO	M	Larsen & Toubro	BUY	SO	M
Siemens	HOLD	SO	L	Sterlite Technologies	HOLD	SP	H
Techno Electric & Engineering	BUY	SO	M	Thermax	REDUCE	SP	L
Voltamp Transformers	REDUCE	SU	M	Voltas	HOLD	SP	L

ABSOLUTE RATING

Ratings	Expected absolute returns over 12 months
Buy	More than 15%
Hold	Between 15% and - 5%
Reduce	Less than -5%

RELATIVE RETURNS RATING

Ratings	Criteria
Sector Outperformer (SO)	Stock return > 1.25 x Sector return
Sector Performer (SP)	Stock return > 0.75 x Sector return
	Stock return < 1.25 x Sector return
Sector Underperformer (SU)	Stock return < 0.75 x Sector return

Sector return is market cap weighted average return for the coverage universe within the sector

RELATIVE RISK RATING

Ratings	Criteria
Low (L)	Bottom 1/3rd percentile in the sector
Medium (M)	Middle 1/3rd percentile in the sector
High (H)	Top 1/3rd percentile in the sector

Risk ratings are based on Edelweiss risk model

SECTOR RATING

Ratings	Criteria
Overweight (OW)	Sector return > 1.25 x Nifty return
Equalweight (EW)	Sector return > 0.75 x Nifty return
	Sector return < 1.25 x Nifty return
Underweight (UW)	Sector return < 0.75 x Nifty return



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Recent Research

Date	Company	Title	Price (INR)	Recos
18-Dec-12	Cummins	In a sweet spot; <i>Company Update</i>	507	Buy
14-Dec-12	Thermax	In search of broad-based revival; <i>Visit Note</i>	604	Reduce
14-Dec-12	Larsen and Toubro	Urea investment policy to spur business opportunity; <i>EdelFlash</i>	1626	Buy

Distribution of Ratings / Market Cap

Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution*	118	46	17	181
* - stocks under review				
	> 50bn	Between 10bn and 50 bn	< 10bn	
Market Cap (INR)	117	57	7	

Rating Interpretation

Rating	Expected to
Buy	appreciate more than 15% over a 12-month period
Hold	appreciate up to 15% over a 12-month period
Reduce	depreciate more than 5% over a 12-month period

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