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Havells India Ltd (HIL)

PRICE : RS.372 | **RECOMMENDATION : BUY**

TARGET PRICE : RS.450 | **FY12E: P/E: 12.8X**

Havells India Ltd (HIL) is one of the prominent electrical and power distribution equipment manufacturing companies in India. Its products range from Industrial & Domestic Circuit Protection Switchgear, Cables & Wires to fans, CFL Lamps and luminaries for domestic & industrial applications. The company enjoys healthy market share across all product offerings translating into domestic business operating margins of 12%. With its strong global distribution network in more than 50 countries, competent manufacturing capability and successful restructuring of overseas subsidiary Sylvania, company is well poised for 35% CAGR growth in operating profits between FY10-12E.

In our estimates, we project a 9% CAGR in consolidated revenues over FY10-12E from Rs.55 bn in FY10 to Rs.66 bn in FY12E. Within the revenue streams, we expect domestic sales to grow by 17% in FY11E and by 17% in FY12E mainly driven by robust growth in power and construction space. We expect exports demand to remain muted in FY11E followed by a moderate growth in FY12E due to European crisis where company has substantial exposure.

At current price the stock looks attractively valued on a discounted cash flow basis. We initiate coverage on the HIL stock with a BUY rating and a DCF based target price of Rs.450, over a 12-month horizon.

Key Investment Rationale

- **Strong sustainable demand for consumer electrical products.** *Indian consumer appliances market is estimated at USD 4.3 bn at present. We expect it to grow by 18% CAGR between 2010-15E on the back of 1) growing disposable income with Indian households 2) evolving lifestyle patterns in India leading to shift in preference for premium products*

- **Diversified Product Portfolio.** *Havells has diversified its business into three verticals viz. Consumer appliances, cables & wires and switchgears. Company derives major revenues from wires and cable division but lately it has been successful in expanding product offerings in the consumer appliances segment. It commendably established market share in key product categories especially Fans and Luminaries.*

- **Extensive Distribution Network.** *We believe that efficient distribution is the key to success in the highly competitive consumer appliances market. Industry is highly fragmented and there exist stiff competition from national as well as regional players. HIL has a robust network of over 4000 dealers spread across India in all the four zones: North, South, East and West.*

- **Sylvania restructuring.** *HIL acquired world's fourth largest lighting company 'Sylvania' with revenues of EUR 406 mn through its Dutch subsidiary - Havells Netherlands BV in FY07. The acquisition was made at the valuation of 7xEV/EBITDA implying an Enterprise value of EUR 227 mn for the company.*

  Since acquisition, its revenues have fallen by 25% and company has been making losses at EBITDA level due to global recession and continuing economic crisis in European region. As a counter measure, company has undertaken aggressive restructuring plan aimed at reducing fixed cost through rationalizing personnel headcount. We believe that this would result in substantial savings of nearly EUR 33 mn per annum for the company,

Stock details

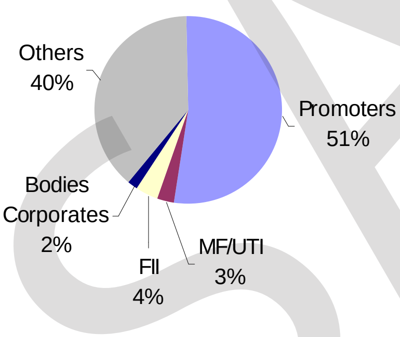
BSE code	:	517354
NSE code	:	HAVELLS
Market cap (Rs bn)	:	44.5
Free float (%)	:	47.9
52-wk Hi/Lo (Rs)	:	454/356
Avg. daily volume	:	1,564,186
Shares o/s (m)	:	120

Summary table

(Rs mn)	FY10	FY11E	FY12E
Sales	55,028	59,056	66,081
Growth (%)	(2.0)	7.3	11.9
EBITDA	3,320	5,056	6,120
EBITDA margin (%)	6.1	8.8	9.6
PBT	1628	3660	4961
Net profit	696	2,562	3,473
EPS (Rs)	5.8	21.3	28.9
Growth (%)		268.1	35.6
CEPS	12.7	29.0	36.8
DPS (Rs)	1.3	1.3	1.4
ROE (%)	10.9	32.8	32.7
ROCE (%)	8.1	17.3	20.0
Net cash (debt)	(8,777)	(6,981)	(4,248)
NW Capital (Days)	18	20	21
EV/Sales (x)	0.8	0.8	0.7
EV/EBITDA (x)	13.5	8.8	7.3
P/E (x)	64.0	17.4	12.8
P/Cash Earnings	29.0	12.7	10.0
P/BV (x)	6.7	4.9	3.6

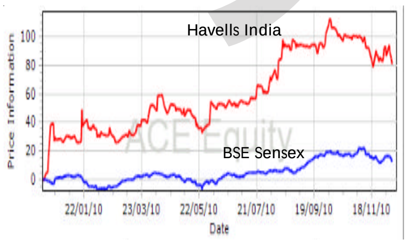
Source: Company, Kotak Securities - Private Client Research

Shareholding pattern



Source: ACE Equity

One-year performance (Rel to Sensex)



Source: ACE Equity

- **Invariable emphasis on R&D efforts**. *HIL constantly ventures into new initiative related to technological advancement. It consistently deploys resources for adding and modifying current product specifications, making it valuable to the end users.*

- **Financials & Valuations.** *We project 10% CAGR in consolidated revenues between FY10-12E from Rs. 55 bn in FY10 to Rs. 66 bn in FY12E. Within the revenue streams, we expect domestic sales to grow by 17% in FY11E and by 19% in FY12E driven by switchgears, wires & cables and consumer appliances segment. We also build 35% CAGR growth in EBITDA in the same period on account of substantial savings from Sylvania post restructuring.*

We initiate coverage on the HIL stock with a BUY rating and a target price of Rs.450, over a 12-month horizon

At current price of Rs.370, stock is trading at 17.4x and 12.7x P/E and 8.8x and 7.3x EV/EBITDA multiples for FY11E and FY12E respectively. We believe that at the current price stock is attractively valued on a discounted cash flow basis. We initiate coverage on the HIL stock with a **BUY** *rating and a DCF based target price of Rs.450, over a 12-month horizon.*

Key Concerns

- **Delays in Sylvania restructuring.** *While we expect meaningful earning contributions from Sylvania post restructuring, repayment of acquisition loan would take a longer time. Therefore any delays in Sylvania restructuring would not only drag company profits but would also worsen the financial health of the company.*

- **Sharp increase in raw material prices.** *Sharp increase in raw material prices would negatively affect the profitability of the company. In our estimates, we build a moderate increase in key raw material costs which is likely to get absorbed by company achieving economies of scale going ahead.*

- **Stiff competition.** *Consumer electrical business is highly fragmented and there exists tremendous competition from the unorganized players having regional presence along with large organized players like HIL, Crompton, Bajaj electric etc incurring pricing pressure.*

- **Slowdown in real estate activity.** *Consumer appliances market growth is highly correlated with the activity in real estate/housing construction sector. Any slowdown in this space would mean lower off take of company's products.*

Company Overview

HIL has a robust network of over 4000 dealers spread across all the four zones of India: North, South, East and West

Havells India Ltd incorporated in 1983, is India's fastest growing player engaged in manufacturing of electrical products like switchgears (domestic and industrial), cables & wires and consumer appliances like fans and luminaries. Leveraging on its strong distribution franchise, efficient R&D base and over twenty five years of experience in the industry, company is all set to benefit from the spurt in perceptible consumer product demand in India. Increasing disposable income and changing lifestyle pattern with a peculiar shift in consumer preference towards premium products augers well for the company's business. Company has its manufacturing facilities in Haridwar, Baddi, Noida, Sahibabad, Faridabad, Alwar and Neemrana along with seven state-of-the-art manufacturing plants located across Europe, Latin America & Africa

HIL along with its subsidiary Sylvania (100% ownership) is present in 52 countries mainly across Asia and Europe. In India, the company has an extensive base of over 4000 dealers and enjoys dominant market share in North India.

Historically, company has been earning major part of its revenue from electric wires and cable division. However, over the past few years, company has been dedicating its resources for establishing itself in India's fast moving consumer electrical market. It has established strong brand image; especially in fans market where it enjoys 17% market share.

Industry Overview

Overview of Indian Consumer Electrical Appliances sector; expected to grow at 18-20% CAGR between FY10-15E.

Indian consumer appliance market is estimated at USD 4.3bn at the end of FY10 and is expected to grow at a CAGR of 18-20% between FY10-15E. The main reasons for this growth are 1) growing disposable income within Indian households (urban & rural) 2) evolving lifestyle patterns in India leading to a peculiar shift in preference for premium products offered by organized players like HIL 3) shortening of product cycle due to higher rate of technological obsolescence 4) increasing electricity supply in urban and rural India.

Indian consumer appliance market is estimated at USD 4.4bn at the end of FY10

In the past, various industry players have strived to gain market share in the urban market. Recently, the penetration level of organized sector has started to increase in semi-urban and rural market. The primary reason for this shift is explained by the unprecedented market growth of over 25% in these regions as against 7%-10% for the former. According to CII, rural consumer market is expected to reach 720-790 million customers by 2010-11

The major products that constitute Indian consumer appliances market are mixers, grinders, irons, water heaters or geysers, electric fans and exhausts. Advanced technology and increasing competition has incurred price pressure and we therefore believe that higher volumes driven by deeper penetration has become a key for any player to establish itself in the industry.

We also believe that consumer behaviour also play a crucial role in building demand for such products. Therefore from business point of view, it becomes important to address issues like product superiority in terms of power savings etc in addition to the overall cost of ownership of these products to the end user.

We opine that with increasing levels of power supply in India by 2012 Industry is bound to grow especially in Tier II/III cities where power cuts are more chronic.

Competitive landscape

The branded brown goods market that consists of products like fans, geysers etc has expanded at a significant pace post liberalization and is expected to retain the growth momentum in the future as well. The market has been transformed by the entry of numerous new brands- domestic and multinationals bringing newer technology and variety to the customer. While focus on price competency remains a key variable to address Indian customer, industry players have also started to focus on enriching product features and efficiency.

Competition is intense in Lighting and fans market due to the large presence of small-mid sized players

Competition is intense in Lighting and fans market due to the large presence of small-mid sized players. Lately there has been meaningful increase in competition from Chinese players who strategize to sweep market by introducing various energy saving products.

Going ahead, we believe that the share of organized players will increase in the consumer appliances space. Key players like Bajaj Electricals, Crompton and Phillips that have pan India presence with effective market reach would benefit from this transition.

HIL USP lies in the quality of its products and it also charges a slight premium in pricing over its competitors. Efficient distribution network and reliable delivery model offers competitive edge to the company.

Like appliances market, domestic wires and cables market is also fragmented. While unorganized sector caters to nearly 50% of annual demand, organized players like Finolex cables, Kei Industries along with Havells have reasonable presence in the organized market. Havells has managed to increase its market share in past few years on account of effective pricing and aggressive distribution franchise.

Havells is present in low capacity market and offers products for domestic as well as Industrial applications

Switchgear market is broadly divided into three categories: low capacity (upto 1.1 KVA), medium capacity (upto 6KVA) and high capacity (6KVA+). Havells is present in low capacity market and offers products for domestic as well as Industrial applications.

Company faces fierce competition from European players like Siemens, ABB and Schneider in addition to the aggressive domestic players like Crompton Greaves and L&T.

HIL market share in key product categories

Product segment	Current Market Size USD mn	HIL Market Share (%)	Key competitors
Industrial Switchgears	450	8	L&T, Siemens, Shneider
Domestic Switchgears	270	20	Legrand-MDS, Scheider
Modular Switches	220	15	Matsushita/Anchor Roma
Industrial Motors	550	-	Crompton, ABB
Cables & Wire	2700	9	Polycab, KEI, Finolex
Compact Fluorescent Lamps	270	10	Philips, Osram
Luminaries	450	10	Philips, Bajaj, Wipro, Crompton
Fans	450	18	Crompton, Orient, Bajaj

Source: Company

Key Investment Arguments

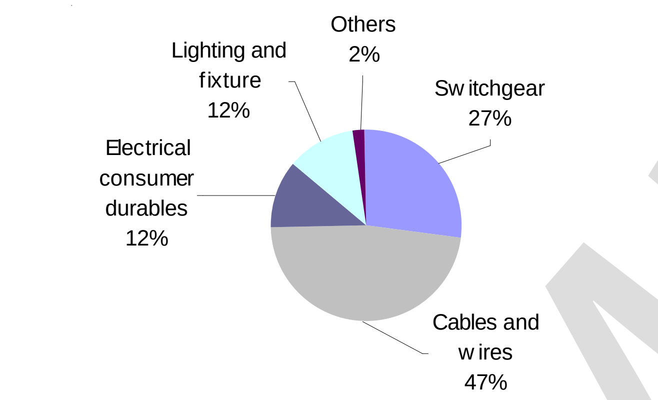
Diversified Product Portfolio

Havells has been observing highest growth in consumer appliances segment

Havells has diversified its business into three verticals viz. Consumer appliances, cables & wires and switchgears. Within the revenue streams it has been observing highest growth in consumer appliances segment and has established market share in key product categories especially Fans and luminaries.

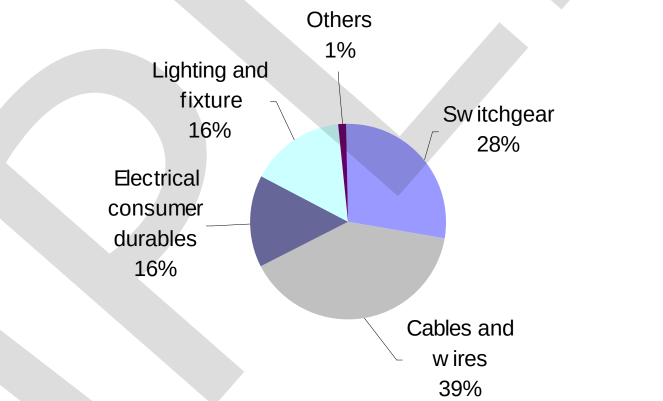
From the historical perspective, company used to earn its major revenues from the cables & wires segment whereas now it has increased contribution from other segments especially consumer appliances division which forms 14% of the revenue pie currently vis-à-vis 10% in FY08. Company is planning to venture into the electric geyser market by the end of FY11.

Revenue mix FY09



Source: Company

Revenue mix FY11E



Source: Company, Kotak Securities - Private Client Research

Strong revenue growth expected on back of sustainable demand for consumer electrical products, switchgears and cables and wire segment

Indian consumer appliances market is estimated at USD 4.3 bn at present. We expect it to grow by 18% CAGR between 2010-15E on back of 1) growing disposable income with Indian households 2) evolving lifestyle patterns in India leading to a shift in preference for premium products catered by the organized players like HIL.

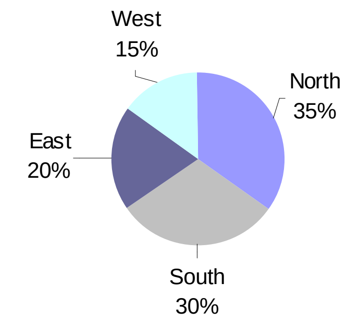
Increasing disposable income with Indian households and evolving lifestyle patterns leading to a shift in preference for premium products are the key growth drivers

The consumer appliances market witnessed tremendous growth in last few years on back of significant investments in the real estate market that grew by over 20% in the last few years. We believe that the growth momentum would remain strong going ahead, leading to a robust 35% CAGR growth between FY10-12E for the segment.

On the back of the sanguine power industry outlook, we expect revenues of HIL's wires and cables business to grow with a CAGR of 13.5% between FY10-12E from Rs11 bn in FY09 to Rs15bn in FY12E.

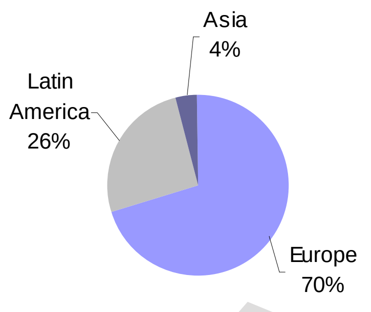
Company is reasonably placed in the low-voltage switchgears segment in both domestic and industrial switchgears. It derives 20% of its revenue from this segment earning 33% contribution margins.

Geographical business mix



Source: Company

Sylvania revenue mix by Geography



Source: Company

Extensive Distribution Network.

We believe that efficient distribution network is the key to success in the highly competitive fast moving consumer appliances space.

HIL has a robust network of over 4000 dealers spread across all the four zones of India: North, South, East and West. While company has strong franchise in North India that contributes to nearly 35% of its revenues, it has been dedicating resource to strengthen the revenue flows from Western India which currently contributes to nearly 15% to the overall revenue pie. Company is seeking to increase its reach in western India which is dominated by its competitors: Compton Greaves and Bajaj Electricals.

Setting up of "Galaxy" showrooms: *Havells is setting up retail showrooms, called "Havells Galaxy", to increase the reach of its products to the end user. Company has been adding 3-4 showrooms on monthly basis and currently operates 47 such showrooms.*

Sylvania restructuring

- *HIL has acquired European company 'Sylvania', world's fourth largest player with over 100 years of existence in manufacturing lighting products. Sylvania's revenues currently stands at EUR 406 mn and was acquired through Havell's Dutch subsidiary - Havells Netherlands BV in FY07. Sylvania is a leading global designer and provider of lighting systems having leading presence in selected markets across Europe and Latin America with a focus on growth in Latin America, Asia and Middle East.*
- *The acquisition was aimed at increasing Havell's global footprint and expanding Sylvania's brand in Asian region in addition to the existing European market. Company acquired the later at the valuation of 7xEV/EBITDA implying an Enterprise value of EUR 227 mn for the company.*
- *Sylvania earns nearly 70% of its revenues from the European region and thus it has been susceptible to the economic health of the region. European crisis has taken toll on the demand for company's products which has eroded 25% of company's revenues in past three years. Company has been accumulating losses at EBITDA levels since acquisition.*
- *As a counter measure, company has undertaken aggressive restructuring plan aimed at reducing fixed cost through rationalizing personnel headcount. Company has split this program into two phases Phoenix and Parakram at the combined cost of EUR 32mn.*
  - **Phoenix** *was initiated in Sept'09 with a cost of EUR 12 mn aiming at rationalizing personnel cost in Latin America and Europe. Company successfully executed this plan and is expected to attain annual savings of EUR 17.5 mn by downsizing its workforce by 1300.*
  - **Parakram** *was commenced in FY10 and is currently under way. This plan is budgeted for EUR 20 mn and should result in the annual savings of EUR 16 mn by employee rationalization.*

Restructuring Plans

	Duration	Estimated Cost in EUR mn	Estimated Annual savings in EUR
Phoenix	Jan'09-Sept'09	12.23	17.50
Prakram	Sept'09-Dec'10	20.00	16.00
Total		32.23	33.50

Source: Company

- *To a large extent company has substituted the overseas higher fixed cost base by outsourcing non critical functions to India. Company has not reduced its sales team or removed any of its key officials under the restructuring plans.*
- *We believe that the company shall successfully execute the Parakram plan by the end of FY11E and thus the profitability at Sylvania would improve on a sustainable basis.*

- We also opine that the revenues from Latin America and Asian regions is likely to grow going ahead and revival in European region would be a key variable to monitor.
- In our projected financials while we build a revenue CAGR of 3% between FY10-12E for Sylvania on constant currency basis. We expect EBITDA to grow to EUR 24 mn by FY12E from current loss levels of EUR 3 mn.

Invariable emphasis on Research & Development

HIL constantly ventures into new initiative related to technological advancement. It consistently deploys resources for adding and modifying current product specifications making it valuable to the end users. Moreover, various R&D efforts become extremely important in the highly competitive consumer appliances segment where profitability is determined by the product's cost effectiveness and power savings.

International footprint offers geographical diversification to take advantage of the upsurge in consumer appliances market in Asian and African markets

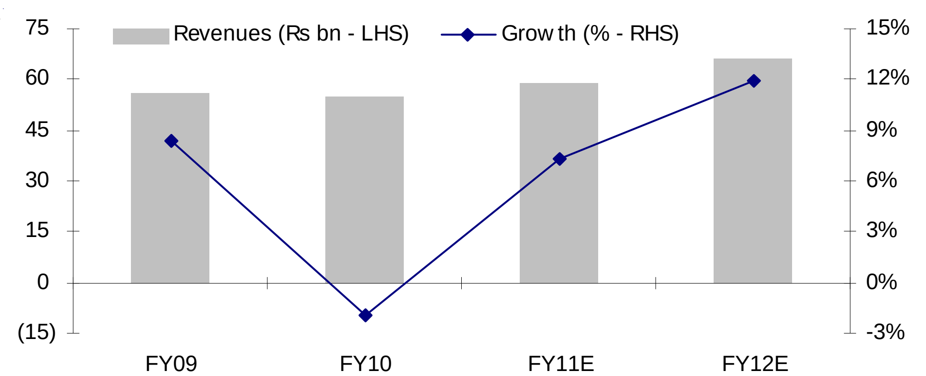
- Company (including Sylvania) is present in nearly 50 countries across Europe and Asia. Moreover it has been witnessing enormous potential in the emerging markets like Africa where housing and real estate market is picking up.
- With an aim to establish itself as a prominent player in these markets, company is planning to strengthen its dealer franchise in these regions. It would be offering its diverse range of products within the parent brand Havells and the acquired brand Sylvania to the overseas customers.
- Going ahead, the company expects substantial amount of revenues through exports on account of revival of the European economy giving a boost to the legacy market of Sylvania coupled with new market development in Asia and Africa regions.

Financials to improve; consistent growth in domestic market, export growth in new geographies and successful restructuring of Sylvania would result in value accretion

We project 10% CAGR growth in consolidated revenues between FY10-12E from Rs. 55 bn in FY10 to Rs. 66 bn in FY12E

- We project 10% CAGR growth in consolidated revenues between FY10-12E from Rs. 55 bn in FY10 to Rs. 66 bn in FY12E. Within the revenue streams, we expect domestic sales to grow by 17% in FY11E and by 19% in FY12E mainly driven by switchgears, wires & cables and consumer appliances segment.
- We also expect exports demand to improve by FY12E on account of expected recovery in European region, growth in Latin America and new geography additions in African and Asian region.

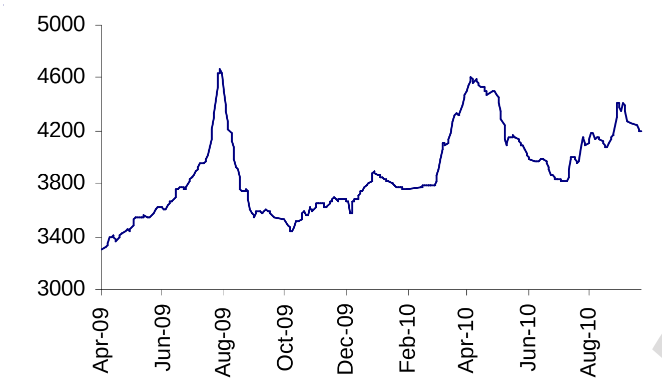
Consolidated revenue trend (Rs bn)



Source: Company, Kotak Securities - Private Client Research

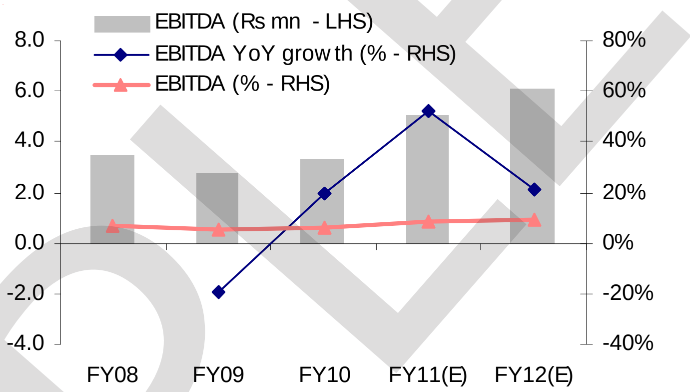
- *We opine that the company would continue to prudently manage its overheads and Sylvania restructuring would boost company's margins. In our projected financials we build 5% EBITDA margins for Sylvania in FY11E.*
- *We believe that the higher operating leverage would obviate any increase in input price. In our projected financials we build 8.8% EBITDA margins at consolidated level for FY11E.*

LME Copper



Source: Bloomberg

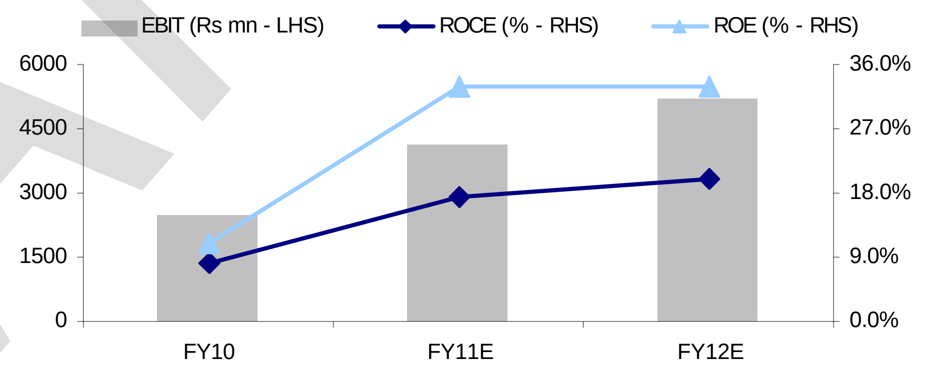
EBITDA (Rs bn)



Source: Company, Kotak Securities - Private Client Research

- *We opine that working capital would slightly increase from current 5% of sales to 5.5% in FY11E and 6% in FY12E to sustain company's expanding dealer franchise in new regions.*
- *Managment has stated that the company is well equipped to support its future growth and would not incur major capex in next two years. We expect the ROCE% of 17.3% and ROE of 32% in FY11E.*

RoE trend



Source: Company, Kotak Securities - Private Client Research

- *We expect that the company would significantly de-leverage its balance sheet and expect D/E to moderate from current 1.9 levels to 0.8 in FY12E mainly on back of 1) higher EBITDA contribution from Sylvania post restructuring 2) higher free cash flow generation in the domestic business.*

Havells Standalone Financials; revenues likely to grow at 19% CAGR between FY10-12E on back of favourable macro environment with deeper brand penetration in TierII/Tier III cities

- *We project revenue growth of 17% and 19% YoY in FY11E and FY12E respectively from current levels of Rs 24.7 bn on back of meaningful growth across all the segments.*

Havells revenue & profitability estimates

(Rs mn)	FY09	FY10	FY11E	FY12E
Revenues	21983	24735	29068	34613
EBITDA	2024	2996	3648	4510
EBITDA (%)	9	12	13	13

Source: Company, Kotak Securities - Private Client Research

Consumer appliances division is likely to drive the company's business for next two years

- *Within the revenue stream we expect 35% CAGR growth between FY10-12E in consumer appliances segment and 18%CAGR growth in switchgear division in the same period.*

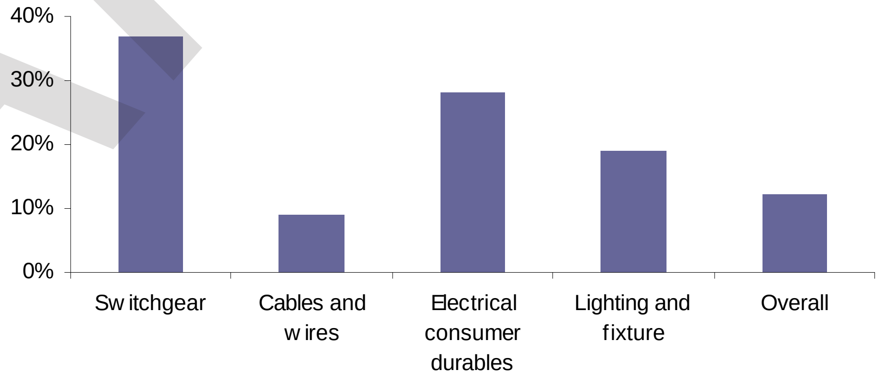
Reported Segments

(Rs mn)	FY09	FY10	FY11E	FY12E
Switchgear	6344.70	7335.74	8680.73	10265.28
Cables and wires	10973.40	11228.11	12014.08	12855.06
Electrical consumer durables	2752.80	3594.50	4852.58	6550.98
Lighting and fixture	2783.80	3667.30	4950.86	6683.65
Others	483.20	369.77	425.24	467.76

Source: Company, Kotak Securities - Private Client Research

- *We expect EBITDA% to increase from current 12% levels going ahead on back of volume pick up across the segments and proportionate increase in contribution by the switchgear division to the overall revenue pie. Company enjoys margins to the tune of 37% in the switchgears business.*

Segmental EBITDA margins FY10



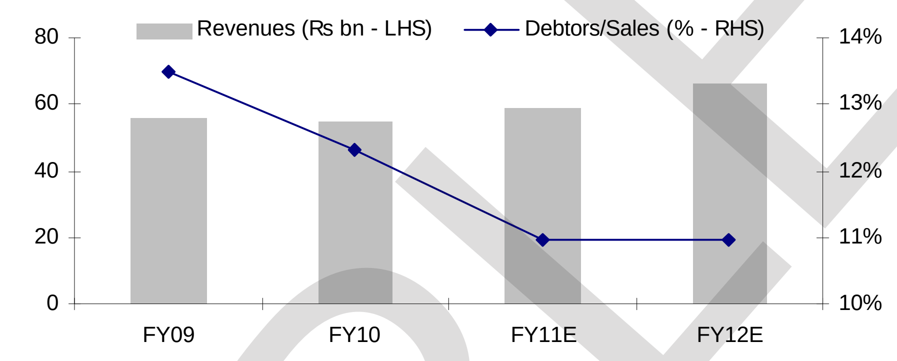
Source: Company

- *While HIL has a strong debt free balance sheet at standalone level, efficient working capital management ensures positive free cash flows for the company going ahead.*

Efficient working capital management; bank limit assistance to dealers strengthens distribution network and reduces working capital requirements of the company

Company provides assistance to its dealers in getting bank limits and receives payments directly from banks. In turn, company extends upfront discounts to the dealers, compensating for accrued interests on the transaction amount.

Debtors/sales



Source: Company, Kotak Securities - Private Client Research

Sylvania Financials; likely sharp improvement in EBITDA on back of aggressive restructuring plans related to operating cost rationalization; muted revenue growth expected in FY11E

- *In our projections we build 3% CAGR revenue growth between FY10-12E for Sylvania (on constant currency basis) on back of continuing economic concerns in its key markets. Early recovery in these geographies poses an upside risk to our earning estimates.*
- *While we believe that the Sylvania would maintain muted revenue growth in FY11E, EBITDA margins would increase on back of substantial cost savings achieved through successful accomplishment of on going restructuring plans.*
- *In our estimates we build EBITDA margins of 5% and 5.5% in FY11E and FY12E respectively.*

Sylvania Revenue & EBITDA estimates

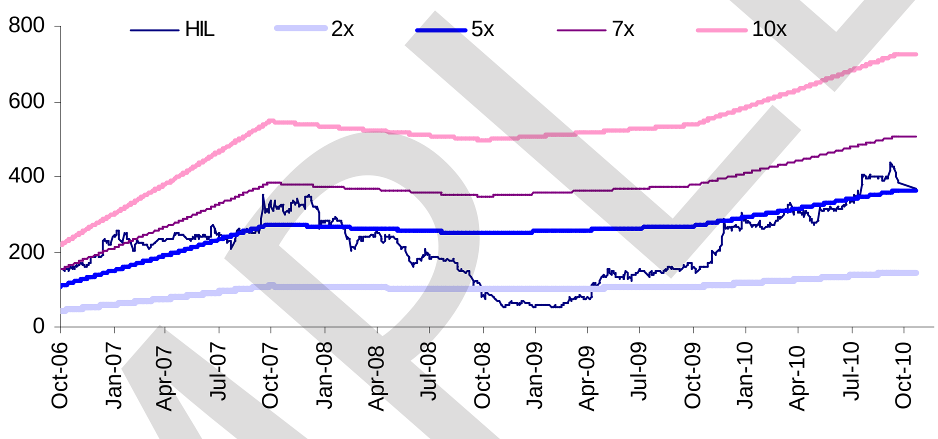
(Rs mn)	FY09	FY10	FY11(E)	FY12(E)
Revenue	32,791	28,833	28,133	29,258
Total Cost	31,931	29,037	26,726	27,649
EBITDA	860	(204)	1,407	1,609

Source: Company, Kotak Securities - Private Client Research

Valuation and Recommendation

- *At current price of Rs.372, stock is trading at 17.4x and 12.8x P/E and 9.6x and 8.8x and 7.3x EV/EBITDA multiples for FY11E and FY12E respectively. We believe that the improved visibility in Sylvania financials implied by 1HYFY11 nos. has led to the recent re-rating in the stock.*
- *At our target price of Rs 450, stock would trade at 6x FY11E and 4.4x FY12E book value respectively. Due to the inconsistent profit growth of the company in the past, we highlight the P/BV trend below that reflects the valuation trend from the historical perspective.*

HIL P/B band



Source: ACE Equity, Kotak Securities - Private Client Research

We initiate coverage on the HIL stock with a BUY rating and a target price of Rs.450, over a 12-month horizon

- *In our earning projections we build meaningful margin expansion in FY11-12E on account of cost restructuring at Sylvania. We also believe that post FY12; the company would expand its operations in other emerging markets leveraging on favourable synergies between Havells and Sylvania. This is likely to result in substantial revenue growth in future.*
- *We value the company using DCF valuation methodology that derives a price target of Rs.450 per share, implying an upside of 22% over a 12- month horizon. Our DCF model employs a WACC of 11.85%, beta of 0.86 and terminal growth of 3%. At our target price of Rs450, the stock will trade at 21.1x and 15.4x FY11E and FY12E EPS respectively.*
- *We initiate coverage on the HIL stock with a BUY rating and a target price of Rs.450, over a 12-month horizon.*

DCF valuation

Free Cash Flow to Firm

	FY12E	FY13E	FY14E	FY15E	FY16E	FY17E	FY18E	FY19E
PAT	3,473	5,517	7,124	8,303	8,358	9,263	9,741	10,243
Add Depriciation	959	943	976	1,010	1,045	1,082	1,120	1,159
Add Int (Net of Tax)	154	157	149	144	140	136	140	144
Less change in WC	(606)	(669)	(667)	(768)	(588)	(647)	(712)	(765)
Less incremental Capex	(900)	(700)	(700)	(700)	(700)	(700)	(700)	(700)
FCFF	**3,080**	**5,247**	**6,881**	**7,990**	**8,255**	**9,133**	**9,588**	**10,081**
Discounting Factor	1.0	0.9	0.8	0.7	0.6	0.6	0.5	0.4
Discounted Value (FCFF)	2,966	4,537	5,318	5,519	5,096	5,040	4,729	4,444

Source: Kotak Securities - Private Client Research

Assumptions

Adjusted beta	0.9
Risk free rate (%)	8.0
Risk premium (%)	6.0
Cost of equity (%)	13.1
Cost of debt (%)	7.5
WACC (%)	11.8
Equity (Rs mn)	44,524
Debt (Rs mn)	12,820
Total (Rs mn)	19,442

Source: Kotak Securities - Private Client Research

DCF Summary (Rs mn)

FCFF	40,162
Terminal growth (%)	3.0
Terminal Value	22,806
Total FCFF	62,968
Less net debt	8,777
Shareholder's value	54,191
Value per share	450
Terminal value as % of FCFF	36.2

Source: Kotak Securities - Private Client Research

Sensitivity Analysis

	Cost of capital				
Terminal growth	**11.0%**	**11.5%**	**11.9%**	**12.5%**	**13.0%**
1.50%	465	438	420	392	372
2.00%	477	448	429	399	379
2.50%	490	459	439	407	385
3.00%	505	471	450	416	393
3.50%	521	485	463	426	401
4.00%	541	501	476	437	411
4.50%	563	519	492	449	421

Source: Kotak Securities - Private Client Research

Business review 1HYFY11; while revenue growth remained muted at 3% YoY given muted revenue growth in overseas markets; operating profits grew by 44% due to successful cost restructuring at Sylvania

- *Company's consolidated revenues for 1HYFY11 remained flat at Rs 27.7 bn a growth of 6% YoY. EBITDA grew at 44% YoY at Rs.2346mn as EBITDA margins expanded to 8% vis-à-vis 6% on account of ongoing restructuring of Sylvania operations.*
- *While domestic revenues grew by 19% in 1HYFY11 at Rs 14 bn, EBITDA stood at Rs 1.4 mn up 6% YoY. Increase in raw material prices impacted the margins of wires and cables division to an extent.*
- *Management expects margin restoration in wires and cables division in 3QFY11 with continued growth momentum across the divisions.*
- *While the lighting division recorded a 30% YoY growth in revenues at Rs 2155 mn, cables and wires division grew by 20% and accounted for 41% of total revenues of the company in 1HYFY11.*
- *Sylvania restructuring has been successful so far and this is getting reflected in last few quarters. Management has been guiding of operational turnaround at Sylvania and expects it to become value accretive by FY12 at PAT levels.*
- *Sylvania reported strong growth of 31% YoY in Latin American region in 1HYFY11 and Europe continued to dominate the revenue pie with 66% contribution.*
- *Management is confident of managing 5% margins for remaining part of FY11 and would launch Sylvania in India over next two quarters.*

Financials

	1HYFY11	1HYFY10	YoY (%)
Net Revenue	**27,727**	**26,268**	**5.6**
Other income	150	63	
EBITDA	**2,346**	**1,626**	**44.3**
Depreciation	393	432	(9.0)
Interest	372	480	(22.5)
Exceptional Items		(823)	-
PBT	**1,731**	**(46)**	**-**
Tax expense	471	302	56.0
PAT	**1,260**	**(348)**	**-**

Source: Company

Key Concerns

Delays in Sylvania restructuring

While we expect meaningful earning contributions from Sylvania post restructuring, repayment of acquisition loan would take a longer time. Therefore any delays in Sylvania restructuring would not only drag company profits but would also worsen the financial health of the company.

Sharp increase in raw material prices

Sharp increase in raw material prices would negatively affect the profitability of the company. In our estimates, we build a moderate increase in key raw material costs which is likely to get absorbed by company achieving economies of scale going ahead.

Stiff competition

Consumer electrical business is highly fragmented and there exists tremendous competition from the unorganized players having regional presence along with large organized players like HIL, Crompton, Bajaj electric etc incurring pricing pressure.

Slowdown in real estate activity

Consumer appliances market growth is highly correlated with the activity in real estate/housing construction sector. Any slowdown in this space would mean lower off take of company's products.

Consolidated Financials: Havells India

Profit and Loss Statement (Rs mn)

(Year-end March)	FY10	FY11E	FY12E
Revenues	**55,028**	**59,056**	**66,081**
% change yoy	(2.0)	7.3	11.9
EBITDA	**3,320**	**5,056**	**6,120**
% change yoy	19.3	52.3	21.1
Depreciation	837	932	959
EBIT	**2,483**	**4,124**	**5,161**
% change yoy	32.2	66.1	25.2
Net Interest	871	484	220
Earnings Before Tax	1,628	3,660	4,961
% change yoy	99.8	124.8	35.6
Tax	932	1,098	1,488
as % of EBT	57.2	30.0	30.0
Recurring PAT	696	2,562	3,473
% change yoy	(143.5)	268.1	35.6
Shares outstanding (m)	120.3	120.3	120.3
EPS (Rs)	**5.8**	**21.3**	**28.9**
DPS (Rs)	1.3	1.3	1.4
CEPS	12.7	29.0	36.8

Source: Company, Kotak Securities - Private Client Research

Balance sheet (Rs mn)

(Year-end March)	FY10	FY11E	FY12E
Cash and cash equivalents	4,043	5,118	6,738
Accounts receivable	6,784	6,472	7,242
Loans & advances	2,568	2,825	3,107
Inventories	7,538	8,090	9,052
Current Assets	16,970	17,466	19,481
WIP	2,764	3,175	3,781
Net fixed assets	8,697	8,865	8,806
Total Assets	**19,391**	**21,045**	**23,212**
Provisions	590	590	590
Current Liabilities	14,206	14,291	15,700
LT debt	12,820	12,100	10,986
Other liabilities(deferred tax)	(97)	(97)	(97)
Equity & reserves	6,622	8,997	12,277
Total Liabilities	**19,369**	**21,023**	**23,190**
BVPS (Rs)	55	75	102

Source: Company, Kotak Securities - Private Client Research

Cash Flow Statement (Rs mn)

	FY10	FY11E	FY12E
Profit Before Tax	1,628	3,660	4,961
Depreciation	837	932	959
Current liabilities incl provisions	(295)	85	1,409
inc in inventory	552	552	962
inc in sundry Debtors	(789)	(312)	770
inc in advances	233	257	282
Tax Paid	932	1,098	1,488
Other Adjustments	-	-	-
Net cash from operations	**2,203**	**3,083**	**3,826**
less:			
Purchase of fixed Assets	(1,000)	(1,100)	(900)
Net investments	-	-	-
Net cash from investing	**(1,000)**	**(1,100)**	**(900)**
Secured loans	100	(524)	(917)
Unsecured loans	443	(197)	(197)
Dividend Paid	(176)	(187)	(193)
Net Cash from financing act	**367**	**(908)**	**(1,307)**
Net Cash Flow	1,569	1,075	1,619
Cash at the end of year	4,043	5,118	6,738

Source: Company, Kotak Securities - Private Client Research

Ratio Analysis

(Year-end March)	FY10	FY11E	FY12E
EBITDA margin (%)	6.1	8.8	9.6
EBIT margin (%)	4.6	7.2	8.1
Net profit margin (%)	1.3	4.5	5.4
Adjusted EPS growth (%)		268.1	35.6
Receivables (days)	45.0	40.0	40.0
Inventory (days)	50.0	50.0	50.0
Sales / Net Fixed Assets (x)	1.9	1.9	2.0
Interest coverage (x)	2.9	8.5	23.5
Debt/ equity ratio	1.9	1.3	0.9
ROE (%)	10.9	32.8	32.7
ROCE (%)	8.1	17.3	20.0
EV/ Sales (x)	0.8	0.8	0.7
EV/EBITDA (x)	13.5	8.8	7.3
Price to earnings (x)	64.0	17.4	12.8
Price to book value (x)	6.7	4.9	3.6
Price to cash earnings (x)	29.0	12.7	10.0

Source: Company, Kotak Securities - Private Client Research

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Disclaimer

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