

HAVELLS INDIA

On a transformational growth path

India Equity Research | Engineering and Capital Goods

A strong top line helped Havells India (HAVL) post double digit growth across most businesses, except lighting, in Q4FY17. However, EBITDA growth was lower due to promotional schemes to counter the demonetisation impact. We believe HAVL, armed with Lloyds' brand/network, is embarking on an exciting journey: a) ready to leverage Lloyds' strong 10,000 touch points to market its products; and b) huge scope to improve profitability of Lloyds' business. Additionally, multiple growth levers—GST, Housing For All etc.,—brighten prospects over the next 3-5 years, which, in our view, has been a key valuation driver over the past 12 months. We assign a higher PE of 38x (28x earlier) FY19E earnings on account of: (1) structural drivers—low penetration, rising disposable incomes; (2) renewed business positioning post Lloyd acquisition. Maintain 'BUY' with revised target price of INR575 (INR413 earlier).

Reasonable growth despite multiple headwinds

Top line and PAT growth of 14% and 17% YoY in FY 17 along with double digit spurt in most businesses (except lighting), despite demonetisation, Lloyds' acquisition and weak switch gears market headwinds, is commendable. The EBITDA margin dip was contained at 60bps despite the company extending support to channel partners/dealers during demonetisation. We estimate reasonable operating margin ramp up over FY18-19 led by waning of demonetisation impact and potential improvement in margin of Lloyds' business.

Multiple value drivers in place post business consolidation

HAVL is best positioned amongst peers to ride India's structural growth story. Our conviction stems from reconfiguration of business structure post Lloyds acquisition to serve a much larger market with significant potential to drive profitability.

Outlook and valuations: Ready for big Leap; maintain 'BUY'

With a solid track record of industry-leading growth in most of its businesses—cables & wires, switchgears etc.,—HAVL is now preparing to penetrate the huge USD5-7bn new market with an available reach akin to most large players post the Lloyds acquisition. This, we believe, could be a key value driver given that Lloyds has one of the lowest margins, which under HAVL could see a material turnaround, driving significant share holder value. We maintain 'BUY/SO'.

Financials (Standalone)

(INR mn)

Year to March	Q4FY17	Q4FY16	% change	Q3FY17	% change	FY17	FY18E	FY19E
Net revenues	17,102	14,597	17.2	15,060	13.6	61,353	98,236	115,217
EBITDA	2,296	2,218	3.5	1,907	20.4	8,241	12,063	14,563
Adj. profit	1,715	1,634	5.0	1,339	28.0	5,969	7,634	9,452
Diluted EPS (INR)	2.7	2.6	5.0	2.1	28.0	9.6	12.2	15.2
Diluted P/E (x)						53.6	41.9	33.9
ROAE (%)						19.2	21.8	23.9

EDELWEISS 4D RATINGS

Absolute Rating	BUY
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 513
Target Price	: INR 575
52-week range (INR)	: 526 / 303
Share in issue (mn)	: 624.9
M cap (INR bn/USD mn)	: 321 / 4,980
Avg. Daily Vol.BSE/NSE('000)	: 1,674.6

SHARE HOLDING PATTERN (%)

	Current	Q2FY17	Q1FY17
Promoters *	61.6	61.6	61.6
MF's, FI's & BK's	2.7	2.7	2.9
FII's	26.5	26.2	26.7
Others	9.2	9.5	8.8
* Promoters pledged shares (% of share in issue)	:		NIL

PRICE PERFORMANCE (%)

	Stock	Nifty	EW Capital Goods Index
1 month	6.6	2.0	2.7
3 months	16.8	7.2	16.2
12 months	50.8	20.0	32.5

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Q4FY17 conference call: Key takeaways

- **Overall comments:** In FY18, management will try to get back to FY16 EBITDA margin of 14.1%. FY17 margins were impacted by schemes introduced during demonetisation. These schemes have been subsequently phased out. Management has been investing in secondary sales force to get in touch with retailers to keep them engaged and for demand creation. Touch points are also increasing.
- **Performance highlights:**
 - **Cables:** Grew 11% YoY in volume terms. Price rise has been taken due to an increase in commodity prices. Last quarter Havells had deferred price increases and have now taken the increases in a calibrated way
 - **Switchgear:** This segment grew 16% YoY primarily led by EWA . Green shoots in the building segment and Havells is confident of double digit growth in FY18. Both industrial and domestic switchgear recorded high single digit growth.
 - **Electrical consumer durables (ECD):** All segments have recorded double digit growth
 - **Air Coolers:** This segment has just started and in FY18 this segment can provide good growth to the ECD segment.
 - **Water Heaters:** Amongst the top 3 players in India.
 - **Fans:** Economic segment has declined, but premium segment has recorded double digit growth.
 - **Lighting:** Revenue (excluding exports) was up 9% and domestic (excluding CFL and convention) was up 29%. LED revenue now accounts for 70-75% of lighting segment and the market is headed towards fixtures due to large life of LEDs.
 - **Standard brand:** Recorded an INR 4000 mn top line in FY17 and is growing well. It has received good response from the channel and consumers.
 - **Rio brand:** Good response and may benefit from the government's affordable housing scheme.
 - **EESL:** Prices have bottomed out for FY18 and are now moving up further; healthy order book for FY18; margins are lower in this segment and Havells will only participate in niche areas. It is not planning to supply fans to EESL.
 - **Lloyds:** It will start reflecting as a separate segment from Q1FY18. Management will continue to procure from Lloyd Electric for the next 2 years.
- **Other comments:**
 - **Employee cost:** It has grown 35% YoY due to significant senior level recruitment. Has developed a matrix structure within the organisation with separate SBUs
 - **Unorganised segment:** These players have started becoming active again in the market
 - **FY18 capex guidance:** INR1500-2000mn.

Table 1: Segmental snapshot (standalone)

Year to March	Q4FY17	Q4FY16	% change	FY17	FY16	% change
Segment revenue (INR mn)						
Switchgear	3,913	3,401	15.1	14,677	13,197	11.2
Cable & Wire	7,601	6,785	12.0	26,756	23,954	11.7
Lighting & Fixtures	2,399	2,406	(0.3)	8,945	8,280	8.0
Electrical Consumer Durables	3,970	3,092	28.4	14,199	11,429	24.2
Others	432	-	-	1,283	-	-
Total	18,315	15,684	16.8	65,860	56,859	15.8
Segment revenue mix (%)						
Switchgear	21.4	21.7		22.3	23.2	
Cable & Wire	41.5	43.3		40.6	42.1	
Lighting & Fixtures	13.1	15.3		13.6	14.6	
Electrical Consumer Durables	21.7	19.7		21.6	20.1	
Others	2.4	-		-	-	
EBIT (INR mn)						
Switchgear	1,441	1,269	13.5	5,610	5,006	12.1
Cable & Wire	875	884	(1.1)	3,256	3,089	5.4
Lighting & Fixtures	635	559	13.6	2,357	1,909	23.5
Electrical Consumer Durables	951	852	11.6	3,494	2,864	22.0
Others	96	-	-	294	-	-
Total	3,998	3,565	12.1	15,011	12,868	16.7
EBIT margin (%)						
Switchgear	36.8	37.3		38.2	37.9	
Cable & Wire	11.5	13.0		12.2	12.9	
Lighting & Fixtures	26.5	23.3		26.4	23.1	
Electrical Consumer Durables	24.0	27.6		24.6	25.1	
Others	-	-		-	-	
Total	21.8	22.7		22.8	22.6	
EBIT mix (%)						
Switchgear	36.0	35.6		37.4	38.9	
Cable & Wire	21.9	24.8		21.7	24.0	
Lighting & Fixtures	15.9	15.7		15.7	14.8	
Electrical Consumer Durables	23.8	23.9		23.3	22.3	
Others	2.4	-		-	-	

Source: Company, Edelweiss research

Financial snapshot

(INR mn)

Year to March	Q4FY17	Q4FY16	% change	Q3FY17	% change	FY16	FY17	FY18E
Net revenues	17,102	14,597	17.2	15,060	13.6	53,783	61,353	98,236
Direct costs	10,415	8,588	21.3	9,141	13.9	31,735	36,485	60,785
Employee expenses	1,312	1,004	30.6	1,238	5.9	3,708	5,004	7,402
Other expenses	3,080	2,788	10.5	2,773	11.0	10,791	11,623	17,985
EBITDA	2,296	2,218	3.5	1,907	20.4	7,549	8,241	12,063
Depreciation	308	274	12.3	301	2.2	1,049	1,196	1,473
EBIT	1,988	1,943	2.3	1,606	23.8	6,500	7,045	10,590
Other income	419	298	40.8	286	46.6	694	1,343	417
Interest	71	46	53.7	15	364.1	127	122	254
Add: Prior period items	(768)	2,024	NA	-		2,024	(578)	-
Profit before tax	1,569	4,219	(62.8)	1,877	(16.4)	9,090	7,688	10,753
Provision for taxes	622	562	10.8	538	15.7	1,970	2,298	3,118
Reported net profit	947	3,657	(74.1)	1,339	(29.3)	7,120	5,390	7,634
Adjusted Profit	1,715	1,634	5.0	1,339	28.0	5,096	5,969	7,634
Equity capital(FV INR 5)	624	624		624		624	624	624
No. of shares (mn)	624	624		624		624	624	624
Diluted EPS (INR)	2.7	2.6	5.0	2.1	28.0	8.2	9.6	12.2
As % of net revenues								
Raw material	60.9	58.8		60.7		59.0	59.5	61.9
Employee cost	7.7	6.9		8.2		6.9	8.2	7.5
Other expenses	18.0	19.1		18.4		20.1	18.9	18.3
EBITDA	13.4	15.2		12.7		14.0	13.4	12.3
Depreciation	1.8	1.9		2.0		2.0	1.9	1.5
EBIT	11.6	13.3		10.7		12.1	11.5	10.8
Interest expenditure	0.4	0.3		0.1		0.2	0.2	0.3
Other income	2.5	2.0		1.9		1.3	2.2	0.4
Adjusted profit margin	10.0	11.2		8.9		9.5	9.7	7.8
Tax rate	39.6	13.3		28.7		21.7	29.9	29.0

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.

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%. In the switchgear market, HAVL is the market leader in the low voltage segment with ~28% share. In India, the company has a network of ~7,000 distributors spread across the four regions servicing ~100,000 retailers/ touch points. HAVL has been highly successful in bolstering market share of existing products along with launching new products, which have received good response, driven by high brand visibility.

Key Risks

Slowdown in domestic business; increased competition could put pressure on margin

Slowdown in key consumer segments of construction and industrial capex could impact the domestic business.

Slowdown in power T&D could impact the demand for its cables and wires business.

Slower than expected revenue growth and profitability turnaround in Lloyd's consumer business poses risk to estimates and valuations.

Financial Statements

Key Assumptions

Year to March	FY16	FY17	FY18E	FY19E
Macro				
GDP(Y-o-Y %)	7.2	6.5	7.1	7.7
Inflation (Avg)	4.9	4.8	5.0	5.2
Repo rate (exit rate)	6.8	6.3	6.3	6.3
USD/INR (Avg)	65.0	67.5	69.0	69.0
Company				
Cables & Wires	0.8	20.4	19.9	18.3
Switchgears	0.6	10.5	23.6	10.5
Lighting & Fixtures	8.2	32.5	20.9	11.1
Consumer durables	11.0	30.9	29.5	27.3
Depreciation	7.1	6.5	7.5	7.5
Tax rate (%)	21.7	27.5	29.0	29.0
Capex (INR mn)	1,766	1,340	2,000	2,000

Income statement

(INR mn)

Year to March	FY16	FY17	FY18E	FY19E
Income from operations	53,783	61,353	98,236	115,217
Materials costs	31,735	36,485	60,785	71,355
Employee costs	3,708	5,004	7,402	8,534
Other mfg expenses	10,791	11,623	17,985	20,764
Total operating expenses	46,234	53,111	86,172	100,653
EBITDA	7,549	8,241	12,063	14,563
Depreciation	1,049	1,196	1,473	1,613
EBIT	6,500	7,045	10,590	12,951
Add: Other income	693.5	1,342.8	416.88	612.63
Less: Interest Expense	127	122	254	252
Add: Exceptional items	2,024	(578)	-	-
Profit Before Tax	9,090	7,688	10,753	13,312
Less: Provision for Tax	1,970	2,298	3,118	3,860
Reported Profit	7,120	5,390	7,634	9,452
Exceptional Items	2,024	(578)	-	-
Adjusted Profit	5,096	5,969	7,634	9,452
Shares o /s (mn)	624	624	624	624
Diluted shares o/s (mn)	624	624	624	624
Adjusted Diluted EPS	8.2	9.6	12.2	15.2
Adjusted Cash EPS	9.9	11.5	14.6	17.7
Dividend per share (DPS)	6.0	3.5	4.3	6.1
Dividend Payout Ratio(%)	88.1	43.3	42.0	48.0

Common size metrics

Year to March	FY16	FY17	FY18E	FY19E
Operating expenses	86.0	86.6	87.7	87.4
EBITDA margins	14.0	13.4	12.3	12.6
Net Profit margins	13.2	8.8	7.8	8.2

Growth ratios (%)

Year to March	FY16	FY17	FY18E	FY19E
Revenues	2.7	14.1	60.1	17.3
EBITDA	8.0	9.2	46.4	20.7
Adjusted Profit	9.6	17.1	27.9	23.8

Balance sheet		(INR mn)			
As on 31st March	FY16	FY17	FY18E	FY19E	
Share capital	625	625	625	625	
Shareholders' funds	29,537	32,736	37,166	42,085	
Long term borrowings	-	1,981	1,981	1,981	
Total Borrowings	-	1,981	1,981	1,981	
Long Term Liabilities	87	137	137	137	
Sources of funds	30,487	35,990	40,421	45,340	
Gross Block	16,268	17,608	19,608	21,608	
Net Block	11,773	11,917	12,446	12,836	
Capital work in progress	205	119	119	119	
Intangible Assets	108	182	179	176	
Total Fixed Assets	12,086	12,217	12,744	13,131	
Non current investments	5,032	5,471	5,471	5,471	
Cash and Equivalents	13,652	19,375	20,844	24,505	
Inventories	7,844	9,284	13,262	15,825	
Sundry Debtors	1,576	2,285	2,691	3,157	
Loans & Advances	60	60	70	83	
Other Current Assets	639	906	639	639	
Current Assets (ex cash)	10,119	12,536	16,662	19,704	
Sundry creditors	9,489	12,508	14,198	16,370	
Provisions	914	1,102	1,102	1,102	
Total Current Liab	10,403	13,610	15,300	17,472	
Net Curr Assets-ex cash	(284)	(1,074)	1,363	2,232	
Net Deferred tax	863	1,138	1,138	1,138	
Uses of funds	30,487	35,990	40,421	45,340	
BVPS (INR)	47.3	52.5	59.6	67.5	

Free cash flow		(INR mn)			
Year to March	FY16	FY17	FY18E	FY19E	
Reported Profit	7,120	5,390	7,634	9,452	
Add: Depreciation	1,049	1,196	1,473	1,613	
Interest (Net of Tax)	(443)	(885)	(116)	(256)	
Others	(1,626)	(336)	(47)	(105)	
Less: Changes in WC	911	(790)	2,435	870	
Operating cash flow	5,189	6,155	6,509	9,833	
Less: Capex	1,766	1,340	2,000	2,000	
Free Cash Flow	3,423	4,815	4,509	7,833	

Cash flow metrics		FY16	FY17	FY18E	FY19E
Year to March					
Operating cash flow	5,189	6,155	6,509	9,833	
Investing cash flow	7,675	(437)	(1,583)	(1,387)	
Financing cash flow	(4,965)	(726)	(3,458)	(4,785)	
Net cash Flow	7,899	4,992	1,468	3,662	
Capex	(1,766)	(1,340)	(2,000)	(2,000)	
Dividend paid	(4,488)	(2,585)	(3,204)	(4,533)	

Profitability and efficiency ratios		FY16	FY17	FY18E	FY19E
Year to March					
ROAE (%)	19.1	19.2	21.8	23.9	
ROACE (%)	26.8	26.1	29.8	32.6	
Inventory Days	85	86	68	74	
Debtors Days	10	11	9	9	
Payable Days	104	110	80	78	
Cash Conversion Cycle	(9)	(13)	(3)	5	
Current Ratio	2.3	2.3	2.5	2.5	
Gross Debt/EBITDA	-	0.2	0.2	0.1	
Gross Debt/Equity	-	0.1	0.1	-	
Adjusted Debt/Equity	-	0.1	0.1	-	

Operating ratios		FY16	FY17	FY18E	FY19E
Year to March					
Total Asset Turnover	1.9	1.8	2.6	2.7	
Fixed Asset Turnover	5.0	5.2	8.1	9.1	
Equity Turnover	2.0	2.0	2.8	2.9	

Valuation parameters		FY16	FY17	FY18E	FY19E
Year to March					
Adj. Diluted EPS (INR)	8.2	9.6	12.2	15.2	
Y-o-Y growth (%)	9.6	17.1	27.9	23.8	
Adjusted Cash EPS (INR)	9.9	11.5	14.6	17.7	
Diluted P/E (x)	62.8	53.6	41.9	33.9	
P/B (x)	10.8	9.8	8.6	7.6	
EV / Sales (x)	5.7	4.9	3.1	2.6	
EV / EBITDA (x)	40.6	36.7	25.0	20.4	

Additional Data

Directors Data

Rajesh Gupta	Whole-Time Director Finance and Group CFO	Puneet Bhatia	Non-Independent & Non-Executive Director
Surjit Gupta	Non-Independent & Non-Executive Director	S B Mathur	Independent Non-Executive Director
S K Tuteja	Independent Non-Executive Director	V K Chopra	Independent Non-Executive Director
AP Gandhi	Independent Non-Executive Director	Adarsh Kishore	Independent Non-Executive Director
Anil Gupta	Chairman & Managing Director	Pratima Ram	Independent Non-Executive Director
Ameet Kumar Gupta	Whole Time Director	T.V.Mohandas Pai	Non-Independent & Non-Executive Director

Auditors - S.R.Batliboi & Co. LLP

**as per last annual report*

Holding – Top10

	Perc. Holding		Perc. Holding
Qrg enterprises ltd	30.38	Qrg investments	11
Gupta vinod	8.45	Nalanda india equity	5.29
Gupta surjit	5.23	Max new york life in	3.21
Capital group compan	3.15	Norges bank	2.89
Government pension f	2.89	Gupta anil rai	2.78

**in last one year*

Bulk Deals

Data	Acquired / Seller	B/S	Qty Traded	Price
29 Mar 2017	Guptajee & Company	Sell	18862400	450.00
29 Mar 2017	Arg Family Trust	Buy	18862400	450.00

**in last one year*

Insider Trades

Reporting Data	Acquired / Seller	B/S	Qty Traded
29 Mar 2017	Anil Rai Gupta as Managing Trustee of ARG Family Trust	Buy	18862400.00
29 Mar 2017	Vinod Gupta on behalf of Guptajee & Co.	Sell	13320000.00
29 Mar 2017	Anil Rai Gupta on behalf of Guptajee & Co.	Sell	5542400.00

**in last one year*

Company	Absolute reco	Relative reco	Relative risk	Company	Absolute reco	Relative reco	Relative Risk
ABB India	REDUCE	SP	L	Bajaj Electricals	HOLD	SP	M
Bharat Forge	BUY	SO	M	Bharat Heavy Electricals	BUY	SO	M
Crompton Greaves	HOLD	SP	M	Cummins India	BUY	SO	L
Engineers India Ltd	BUY	SO	L	Greaves Cotton	HOLD	SP	M
Havells India	BUY	SP	M	Kalpataru Power	BUY	SO	M
KEC International	BUY	SP	M	Larsen & Toubro	BUY	SO	M
Praj Industries	BUY	None	None	Ramkrishna Forgings	BUY	SP	M
Siemens	REDUCE	SP	L	TD Power Systems	BUY	None	None
Techno Electric & Engineering	BUY	SO	M	Thermax	REDUCE	SP	L
Triveni Turbine	BUY	None	None	VA Tech Wabag	BUY	None	None
Voltas	BUY	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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Coverage group(s) of stocks by primary analyst(s): Engineering and Capital Goods

ABB India, Bharat Heavy Electricals, Bharat Forge, Bajaj Electricals, Crompton Greaves, Engineers India Ltd, Greaves Cotton, Havells India, KEC International, Cummins India, Kalpataru Power, Larsen & Toubro, Praj Industries, Ramkrishna Forgings, Siemens, TD Power Systems, Techno Electric & Engineering, Thermax, Triveni Turbine, VA Tech Wabag, Voltas

Recent Research

Date	Company	Title	Price (INR)	Recos
05-May-17	Greaves Cotton	Growth challenges mount amidst stretched valuations ; <i>Result Update</i>	166	Hold
24-Apr-17	Bharat Forge	Building visibility ahead of time...; <i>Visit Note</i>	1133	Buy
27-Mar-17	KEC International	Palpable growth momentum; <i>Company Update</i>	192	Buy

Distribution of Ratings / Market Cap

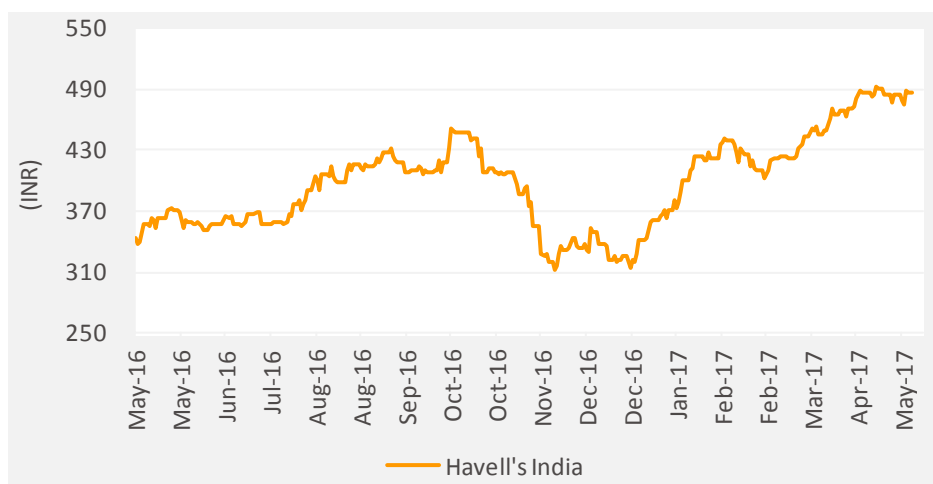
Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution*	161	67	11	240
* 1stocks under review				
	> 50bn	Between 10bn and 50 bn	< 10bn	
Market Cap (INR)	156	62	11	

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

One year price chart



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