RESULT UPDATE

HAVELLS INDIA

Tepid Q1 temporary hiccup; exciting story ahead

Edelweiss
Ideas create, values protect

India Equity Research| Consumer Durables

Havells India (HAVL) missed Q1FY18 sales / EBITDA by a huge margin—22% / 35%—due to multiple factors which, in our view, are non-recurring. Key highlights: a) INR2bn plus sales attributable to Lloyds wherein HAVL reported only 50 days of sales, missing the crucial AC season, apart from impact of GST affecting primary off take; and b) weak switchgears / consumer durables sales, sharp rise in low margin cables & wires' sales and one-time expenses impacted EBITDA margin—down 440bps YoY. While we revise down FY18/19E EPS ~2.5% each building in Q1 impact, we expect HAVL to do much better in coming quarters given strong underlying demand outlook (refer *Consumer Durables - Home Run*) and gradual transition of Lloyds' business. Maintain 'BUY' with revised TP of INR564 (INR575 earlier).

How HAVL fared in Q1FY18? What to expect going ahead?

HAVL's (excluding Lloyds) Q1FY18 top line grew 9% YoY, way below >20% estimate as dealers resorted to inventory de-stocking, especially in switchgears / consumer durables. Cables grew a healthy 19% YoY as channel partners advanced purchases fearing price rise. Weak top line, INR130mn one-time expense related to Lloyds and poor sales mix impacted EBITDA margin—tumbled 400bps plus YoY. We expect most of the company's segments to pick up going ahead given healthy underlying demand drivers. Hence, we estimate 11% and 20% YoY top line and EBITDA growth, respectively, in 9MFY18 led by operating leverage and favourable revenue mix.

What's the big story? Key monitorables

We are bullish on HAVL from the medium- to long-term perspective given potent demand drivers and its strong competitive positioning in existing businesses. However, we believe, incremental value driver will be repositioning of the Lloyds business with focus on product positioning and cost structure. This will improve latter's inherent OPM to atleast industry average of ~8-10% (up 300-400bps) from current level.

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

HAVL now has a huge target market in place with more than 95% reach in the consumer durable / light electrical industry. We believe, management has significant potential to drive business growth / profitability as the company expands its distribution and product portfolio catering to tier III/IV/V cities. Also, we expect earnings surprise, especially from FY19E in the Lloyds business. We maintain **'BUY/SO'**.

Financials (Standalone) (INR mn)

Year to March	Q1FY18	Q1FY17	*% change*	Q4FY17	*% change*	FY17	FY18E	FY19E
Net revenues	18,605	14,668	*26.8*	17,102	*8.8*	61,353	94,788	113,438
EBITDA	1,724	2,004	*(14.0)*	2,296	*(24.9)*	8,241	11,446	14,007
Adj. profit	1,214	1,456	*(16.6)*	1,715	*(29.2)*	5,969	7,416	9,278
Diluted EPS (INR)	1.9	2.3	*(16.6)*	2.7	*(29.2)*	9.6	11.9	14.9
Diluted P/E (x)						48.8	39.3	31.4
ROAE (%)						19.2	21.3	23.5

EDELWEISS 4D RATINGS

Absolute Rating	BUY
Rating Relative to Sector	Outperform
Risk Rating Relative to Sector	Low
Sector Relative to Market	Overweight

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

CMP	: INR 467
Target Price	: INR 564
52-week range (INR)	: 526 / 303
Share in issue (mn)	: 625.1
M cap (INR bn/USD mn)	: 292 / 4,537
Avg. Daily Vol.BSE/NSE('000)	: 1,504.3

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	(3.0)	2.5	0.8
3 months	(3.9)	8.7	2.6
12 months	29.8	16.1	14.7

Amit Mahawar
+91 22 4040 7451
amit.mahawar@edelweissfin.com

Swarnim Maheshwari
+91 22 4040 7418
swarnim.maheshwari@edelweissfin.com

Darshika Khemka
+91 22 4063 5544
darshika.khemka@edelweissfin.com

Krish Kohli
+91 22 6620 3130
krish.kohli@edelweissfin.com

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Q1FY18 conference call: Key takeaways

Havells:

- Sales plunged in May and June, which impacted the contribution margin as there was a fixed overhead cost of running all factories. Though HAVL continued to invest in branding and manpower, according to management, SG&A has peaked at 11% of total revenue.
- HAVL is confident of reverting to 13.0-13.5% margin level.
- Q1FY18 margin was impacted due to product mix—low margin segments like cables & wires, EESL and exports clocked good growth.
- Trade payables increased from INR6.3bn in Q4FY17 to INR11.86bn in Q1FY18 due to trade payables inherited from Lloyds. This was primarily due to credit terms provided by Chinese suppliers to Lloyds. HAVL will be renegotiating these contracts over the next few months.
- Management is planning capex of INR2bn in FY18.
- While cables volumes jumped 13%, wires volumes grew 9%.

Lloyds:

- Revenue from Lloyds was only for 50 days as HAVL completed the acquisition on May 8. The transition has been smooth.
- Non-recurring expenses of INR120-140mn have been captured under HAVL's expenses.
- Lloyds' Q1FY18 revenue jumped 20% YoY.
- Management believes, margin will improve with the right mix of sourcing and manufacturing. Currently, 70% components are sourced from China and 30% from LEEL.
- Promotional expenses for Lloyds were higher at 6.8% due to consumer finance schemes. HAVL's promotional expenses were much lower as it does not do much consumer financing. Management expects blended promotional expenses going forward to be in the 5.5-6.0% range.

GST impact:

- There was significant channel destocking in May and June, which led to channel stock levels plunging 35-50%.
- All cost hikes due to GST have been passed on to consumers from July 1.
- HAVL waited till July 1 to increase prices. Billing with the new system started from July 1 itself with the new increased prices.
- Management does not see any restocking as dealers and retailers are still coming to terms with the new system. Large organised retailers have put systems in place only by July 10, but small retailers still have not adjusted to the new system.
- Primary sales were primarily impacted, but secondary & tertiary sales remained healthy.

Rio:

- Rio is catering to markets where HAVL is not present, such as Piano switches.

Financial snapshot (INR mn)

Year to March	Q1FY18	Q1FY17	% change	Q4FY17	% change	FY17	FY18E	FY19E
Net revenues	18,605	14,668	*26.8*	17,102	*8.8*	61,353	94,788	113,438
Direct costs	11,965	8,467	*41.3*	10,415	*14.9*	36,485	58,802	70,534
Employee expenses	1,619	1,239	*30.6*	1,312	*23.4*	5,004	7,251	8,355
Other expenses	3,297	2,958	*11.5*	3,080	*7.1*	11,623	17,289	20,542
EBITDA	1,724	2,004	*(14.0)*	2,296	*(24.9)*	8,241	11,446	14,007
Depreciation	336	280	*20.0*	308	*9.1*	1,196	1,473	1,613
EBIT	1,389	1,724	*(19.5)*	1,988	*(30.2)*	7,045	9,972	12,394
Other income	348	314	*10.7*	419	*(17.0)*	1,343	727	925
Interest	34	16	*109.9*	71	*(52.1)*	122	254	252
Add: Prior period items						(578)		
Profit before tax	1,703	2,022	*(15.8)*	2,337	*(27.1)*	7,688	10,446	13,067
Provision for taxes	489	567	*(13.7)*	622	*(21.4)*	2,298	3,029	3,790
Reported net profit	1,214	1,456	*(16.6)*	1,715	*(29.2)*	5,390	7,416	9,278
Adjusted Profit	1,214	1,456	*(16.6)*	1,715	*(29.2)*	5,969	7,416	9,278
Equity capital(FV INR 5)	624	624		624		624	624	624
No. of shares (mn)	624	624		624		624	624	624
Diluted EPS (INR)	1.9	2.3	*(16.6)*	2.7	*(29.2)*	9.6	11.9	14.9
As % of net revenues								
Raw material	64.3	57.7		60.9		59.5	62.0	62.2
Employee cost	8.7	8.4		7.7		8.2	7.6	7.4
Other expenses	17.7	20.2		18.0		18.9	18.2	18.1
EBITDA	9.3	13.7		13.4		13.4	12.1	12.3
Depreciation	1.8	1.9		1.8		1.9	1.6	1.4
EBIT	7.5	11.8		11.6		11.5	10.5	10.9
Interest expenditure	0.2	0.1		0.4		0.2	0.3	0.2
Other income	1.9	2.1		2.5		2.2	0.8	0.8
Reported net profit	6.5	9.9		10.0		9.7	7.8	8.2
Tax rate	28.7	28.0		26.6		29.9	29.0	29.0

Change in Estimates

	FY18E			FY19E			
	New	Old	% change	New	Old	% change	Comments
Net Revenue	94,788	98,236	*(3.5)*	113,438	115,217	*(1.5)*	Building in impact of weaker Q1 and GST & destocking impact
EBITDA	11,446	12,063	*(5.1)*	14,007	14,564	*(3.8)*	
EBITDA Margin	*12.1*	*12.3*		*12.3*	*12.6*		
Adjusted Profit After Tax	7,416	7,634	*(2.9)*	9,278	9,452	*(1.8)*	
Net Profit Margin	*7.8*	*7.8*		*8.2*	*8.2*		
Capex	2,000	2,000	*0.0*	2,000	2,000	*0.0*	

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. Recent buyout of Lloyd brand imparts access to a high growth larger white good market adding USD2-5bn new market.

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	4.5	4.0	4.5
Repo rate (exit rate)	6.8	6.3	5.8	5.8
USD/INR (Avg)	65.0	67.5	66.0	66.0
Company				
Cables & Wires	0.8	20.4	19.9	18.3
Switchgears	0.6	10.5	14.4	21.3
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	2,386	2,000	2,000

Income statement (INR mn)

Year to March	FY16	FY17	FY18E	FY19E
Income from operations	53,783	61,353	94,788	113,438
Materials costs	31,735	36,485	58,802	70,534
Employee costs	3,708	5,004	7,251	8,355
Other mfg expenses	10,791	11,623	17,289	20,542
Total operating expenses	46,234	53,111	83,342	99,431
EBITDA	7,549	8,241	11,446	14,007
Depreciation	1,049	1,196	1,473	1,613
EBIT	6,500	7,045	9,972	12,394
Add: Other income	693.5	1,342.8	727.29	924.56
Less: Interest Expense	127	122	254	252
Add: Exceptional items	2,024	(578)	-	-
Profit Before Tax	9,090	7,688	10,446	13,067
Less: Provision for Tax	1,970	2,298	3,029	3,790
Reported Profit	7,120	5,390	7,416	9,278
Exceptional Items	2,024	(578)	-	-
Adjusted Profit	5,096	5,969	7,416	9,278
Shares o /s (mn)	624	624	624	624
Diluted shares o/s (mn)	624	624	624	624
Adjusted Diluted EPS	8.2	9.6	11.9	14.9
Adjusted Cash EPS	9.9	11.5	14.3	17.5
Dividend per share (DPS)	6.0	3.5	4.2	5.9
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	87.9	87.7
EBITDA margins	14.0	13.4	12.1	12.3
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	54.5	19.7
EBITDA	8.0	9.2	38.9	22.4
Adjusted Profit	9.6	17.1	24.3	25.1

Balance sheet (INR mn)

As on 31st March	FY16	FY17	FY18E	FY19E
Share capital	625	625	625	625
Shareholders' funds	29,537	32,736	37,040	41,868
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**	**40,295**	**45,123**
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	20,780	24,331
Inventories	7,844	9,284	12,815	15,647
Sundry Debtors	1,576	2,285	2,597	3,108
Loans & Advances	60	60	70	83
Other Current Assets	639	906	639	639
Current Assets (ex cash)	10,119	12,536	16,120	19,477
Sundry creditors	9,489	12,508	13,719	16,186
Provisions	914	1,102	1,102	1,102
Total Current Liab	10,403	13,610	14,821	17,288
Net Curr Assets-ex cash	(284)	(1,074)	1,300	2,190
Net Deferred tax	863	1,138	1,138	1,138
Uses of funds	**30,487**	**35,990**	**40,295**	**45,123**
BVPS (INR)	47.3	52.5	59.4	67.1

Free cash flow (INR mn)

Year to March	FY16	FY17	FY18E	FY19E
Reported Profit	7,120	5,390	7,416	9,278
Add: Depreciation	1,049	1,196	1,473	1,613
Interest (Net of Tax)	(443)	(885)	(336)	(478)
Others	(1,511)	754	(137)	(195)
Less: Changes in WC	960	(1,323)	2,373	890
Operating cash flow	5,254	7,778	6,044	9,327
Less: Capex	1,766	2,386	2,000	2,000
Free Cash Flow	**3,488**	**5,392**	**4,044**	**7,327**

Cash flow metrics

Year to March	FY16	FY17	FY18E	FY19E
Operating cash flow	5,254	7,778	6,044	9,327
Investing cash flow	(781)	(2,275)	(1,273)	(1,075)
Financing cash flow	(4,976)	(724)	(3,366)	(4,701)
Net cash Flow	(503)	4,780	1,405	3,551
Capex	(1,766)	(2,386)	(2,000)	(2,000)
Dividend paid	(4,488)	(2,585)	(3,112)	(4,450)

Profitability and efficiency ratios

Year to March	FY16	FY17	FY18E	FY19E
ROAE (%)	19.1	19.2	21.3	23.5
ROACE (%)	26.8	26.1	29.0	32.1
Inventory Days	85	86	69	74
Debtors Days	10	11	9	9
Payable Days	104	110	81	77
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

Year to March	FY16	FY17	FY18E	FY19E
Total Asset Turnover	1.9	1.8	2.5	2.7
Fixed Asset Turnover	5.0	5.2	7.8	9.0
Equity Turnover	2.0	2.0	2.7	2.9

Valuation parameters

Year to March	FY16	FY17	FY18E	FY19E
Adj. Diluted EPS (INR)	8.2	9.6	11.9	14.9
Y-o-Y growth (%)	*9.6*	*17.1*	*24.3*	*25.1*
Adjusted Cash EPS (INR)	9.9	11.5	14.3	17.5
Diluted P/E (x)	57.1	48.8	39.3	31.4
P/B (x)	9.9	8.9	7.9	7.0
EV / Sales (x)	5.3	4.6	2.9	2.4
EV / EBITDA (x)	36.8	33.2	23.8	19.2

Peer comparison valuation

	Market cap	Diluted P/E (X)		P/B (X)		ROAE (%)	
Name	(USD mn)	FY18E	FY19E	FY18E	FY19E	FY18E	FY19E
Havells India	4,537	39.3	31.4	7.9	7.0	21.3	23.5
Bajaj Electricals	525	23.6	17.7	3.4	3.0	15.4	18.0
Voltas	2,541	27.3	24.2	4.3	3.8	16.9	16.7
Median	-	27.3	24.2	4.3	3.8	16.9	18.0
AVERAGE	-	30.1	24.4	5.2	4.6	17.8	19.4

Source: Edelweiss research

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	30.37	Qrg investments	11
Gupta vinod	6.31	Nalanda india equity	5.29
Gupta surjit	5.22	Gupta anil rai	4.9
Norges bank	2.88	Capital group compan	2.8
Government pension f	2.67	Gupta qimat rai	2.17

**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
Bajaj Electricals	HOLD	SP	M	Crompton Consumer Electricals	BUY	SO	L
Finolex Cables	BUY	SO	L	Havells India	BUY	SO	L
KEI Industries	BUY	SO	L	Symphony	BUY	SO	L
V-Guard	HOLD	SP	L	Voltas	BUY	SO	L
Whirlpool of India	BUY	SO	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

Edelweiss Securities Limited, Edelweiss House, off C.S.T. Road, Kalina, Mumbai – 400 098.
Board: (91-22) 4009 4400, Email: *research@edelweissfin.com*

Aditya Narain
Head of Research
aditya.narain@edelweissfin.com

ADITYA NARAIN

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***Coverage group(s) of stocks by primary analyst(s):** Consumer Durables*

Bajaj Electricals, Crompton Consumer, Finolex Cables, Havells India, KEI Industries, Symphony, V-Guard, Voltas, Whirpool India

Recent Research

Date	Company	Title	Price (INR)	Recos
18-Jul-17	**Consumer Durables**	Home Run; *Sector Update*		

Distribution of Ratings / Market Cap

Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution*	161	67	11	240

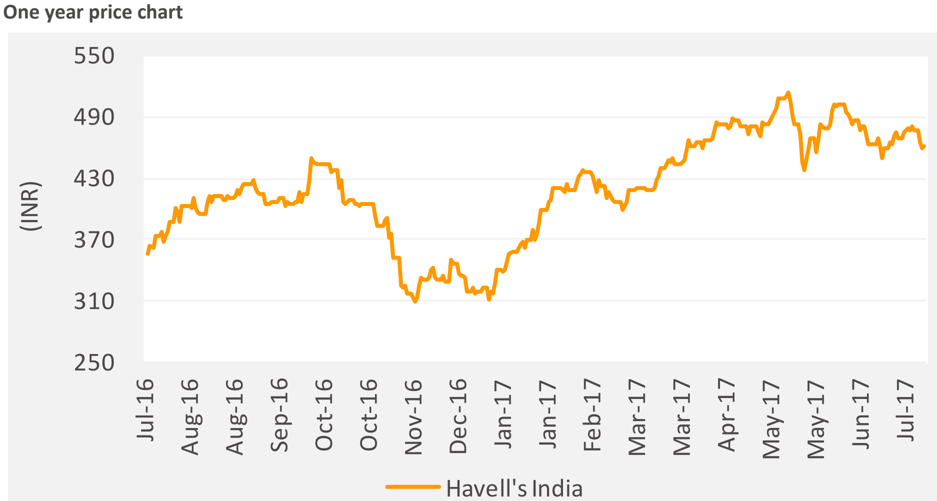
* 1stocks under review

	> 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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