

30 October 2018

HIL*Growth momentum continues; Buy*

Its sharper focus on cost optimisation, solution-centric approach and ramped-up pipe capacities led HIL to report a good performance. Its strong brand, optimised working capital, Parador acquisition and leading position in asbestos-based roofing and AAC blocks are other positives. We retain our Buy recommendation.

Cost optimisation to aid margins. Amid rising cost pressures, through its premium-pricing position and continuous cost-optimisation, HIL reported a margin improvement of 467bps y/y to 13.4%, backed by the good performance in roofing and building solutions. Greater utilisation in its pipe capacities, its strong brand and distribution channel are other positives. We expect revenue and EBITDA CAGRs of respectively 14% and 32% over FY18-20.

Parador acquisition. In the quarter, the Parador Holdings acquisition was completed, infusing ₹2.73bn equity and a ₹1.59bn shareholder loan in HIL International, Germany, which led the standalone D/E ratio to rise to 0.5x. The company's strong global operations and wide range of flooring solutions would help HIL expand its product range and global footprint, besides doubling its revenue and expanding its EPS.

Business outlook. With the ramping up of its pipe capacities and the proposed wall putty expansion, besides its rising BS revenue share, the non-asbestos share is set to rise. Buttressed by the better operating performance and the constant focus on optimising working capital, HIL is expected to do rather well. We expect a 31% CAGR in PAT over FY18-20 and good FCF generation.

Valuation. We believe that HIL, with its leading position, expansion in a high-growth market and its better operating performance, will post a sturdy performance. We, therefore, retain our Buy rating, with a target of ₹2,763 at a 15x PE on FY20e. **Risk:** Higher input costs.

Key financials (YE Mar)	FY16	FY17	FY18	FY19e	FY20e
Sales (₹ m)	10,963	11,191	12,786	14,974	16,752
Net profit (₹ m)	424	615	808	1,094	1,380
EPS (₹)	56.6	82.1	107.8	157.7	184.2
PE (x)	8.9	9.5	15.0	13.7	11.7
EV / EBITDA (x)	5.3	6.1	7.8	8.9	7.0
PBV (x)	0.8	1.2	2.1	2.4	2.1
RoE (%)	9.4	12.7	15.1	19.2	19.2
RoCE (%)	6.2	7.2	10.4	13.5	13.5
Dividend yield (%)	3.5	1.3	1.4	1.1	1.2
Net debt/equity (x)	0.3	0.1	0.1	0.5	0.2

Source: Company, Anand Rathi Research

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Rating: **Buy**

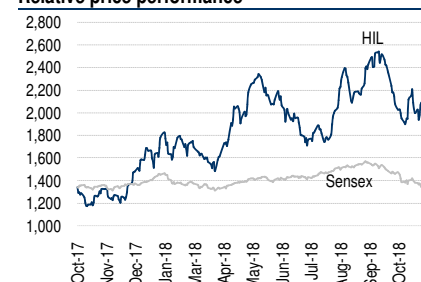
Target price: ₹2,763

Share price: ₹2,153

Key data	HIL IN / HLLT.BO
52-week high / low	₹2,600 / 1180
Sensex / Nifty	33891 / 10198
3-m average volume	\$0.5m
Market cap	₹16bn / \$219m
Shares outstanding	7m

Shareholding pattern (%)	Sep'18	Jun'18	Mar'18
Promoters	41.0	41.0	41.0
- of which, Pledged	-	-	-
Free float	59.1	59.0	59.0
- Foreign institutions	5.2	4.7	3.0
- Domestic institutions	8.4	8.5	6.5
- Public	45.5	45.8	49.5

Estimates revision (%)	FY19e	FY20e
Sales	(0.0)	0.4
EBITDA	14.6	13.2
PAT	1.7	3.3

Relative price performance

Source: Bloomberg

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Quick Glance – Financials and Valuations

Fig 1 – Income statement (₹m)

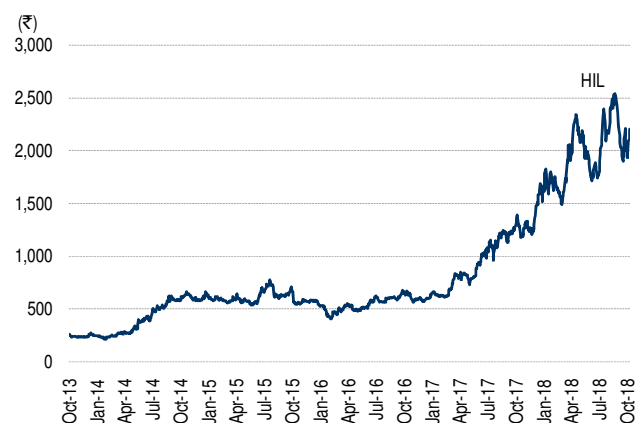
Year-end: Mar	FY16	FY17	FY18	FY19e	FY20e
Net revenues	10,963	11,191	12,786	14,974	16,752
Growth (%)	-1.0	2.1	14.3	17.1	11.9
Direct costs	6,239	5,435	6,315	7,496	8,332
SG&A	3,729	4,717	5,001	5,329	5,860
EBITDA	995	1,040	1,470	2,149	2,560
EBITDA margins (%)	9.1	9.3	11.5	14.4	15.3
- Depreciation	397	410	469	500	527
Other income	122	226	236	100	110
Interest expenses	92	52	39	125	172
PBT	628	804	1,199	1,625	1,971
Effective tax rate (%)	34.0	25.7	32.7	30.0	30.0
+ Associates / (minorities)					
Net income	397	546	808	1,239	1,380
Adjusted income	424	615	808	1,094	1,380
WANS	7	7	7	7	7
FDEPS (₹/ sh)	56.6	82.1	107.8	146.1	184.2
Adj. FDEPS growth (%)	-39.6	45.0	31.3	35.5	26.1
Gross margins (%)	43.1	51.4	50.6	49.9	50.3

Fig 3 – Cash-flow statement (₹m)

Year-end: Mar	FY16	FY17	FY18	FY19e	FY20e
PBT	628	804	1,199	1,625	1,971
+ Non-cash items	397	410	469	500	527
Oper. prof. before WC	1,025	1,213	1,668	2,125	2,498
- Incr./ (decr.) in WC	445	-669	-798	1,921	277
Others incl. taxes	194	208	447	531	591
Operating cash-flow	386	1,674	2,019	-327	1,630
- Capex (tang. + intang.)	756	322	734	450	300
Free cash-flow	-370	1,352	1,285	-777	1,330
Acquisitions					
- Div. (incl. buyback & taxes)	157	90	203	197	232
+ Equity raised	-	-	-	-	-
+ Debt raised	373	-858	-52	2,696	-800
- Fin investments	-76	181	1,011	1,570	-0
- Misc. (CFI + CFF)	-61	164	-18	0	-0
Net cash-flow	-17	59	38	152	297

Source: Company, AnandRathi Research

Fig 5 – Price movement



Source: Bloomberg

Fig 2 – Balance sheet (₹ m)

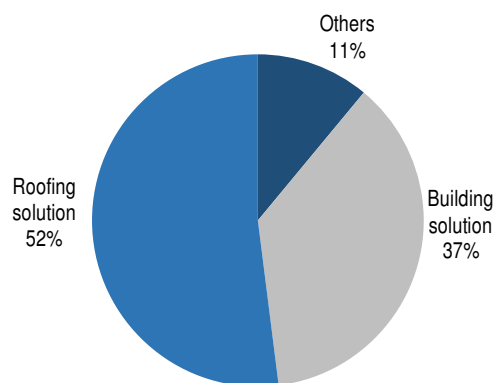
Year-end: Mar	FY16	FY17	FY18	FY19e	FY20e
Share capital	75	75	75	75	75
Net worth	4,672	5,035	5,661	6,558	7,705
Total debt	1,577	719	668	3,364	2,564
Minority interest					
DTL/(assets)	475	454	395	395	395
Capital employed	6,724	6,208	6,724	10,317	10,664
Net tangible assets	4,877	4,847	4,707	5,098	4,871
Net intangible assets	246	230	213	213	213
Goodwill	-	-	-	-	-
CWIP (tang. & intang.)	110	69	490	50	50
Investments (strategic)	17.4	17.7	3.7	2,738.3	2,738.3
Investments (financial)	-	180.6	1,205.9	41.2	41.2
Current assets (ex cash)	3,777	3,361	3,429	5,661	6,426
Cash	40	100	138	290	587
Current liabilities	2,343	2,596	3,463	3,774	4,261
Working capital	1,433	765	-34	1,887	2,164
Capital deployed	6,724	6,208	6,724	10,317	10,664
Contingent liabilities	670	712	866	-	-

Fig 4 – Ratio analysis

Year-end: Mar	FY16	FY17	FY18	FY19e	FY20e
P/E (x)	8.9	9.5	15.0	14.7	11.7
EV/EBITDA (x)	5.3	6.1	7.8	8.9	7.1
EV / sales (x)	0.5	0.6	0.9	1.3	1.1
P/B (x)	0.8	1.2	2.1	2.5	2.1
RoE (%)	9.4	12.7	15.1	17.9	19.3
RoCE (%) - after tax	6.2	7.2	10.4	13.6	13.6
Fixed asset T/O (x)	1.8	2.1	2.3	2.4	2.5
DPS (₹ / sh)	17.4	10.0	22.5	21.9	25.8
Dividend yield (%)	3.5	1.3	1.4	1.0	1.2
Dividend payout (%) - incl. DDT	39.6	16.4	25.1	15.9	16.9
Net debt / equity (x)	0.3	0.1	0.1	0.5	0.3
Receivables (days)	34	28	28	30	30
Inventory (days)	74	67	53	50	50
Payables (days)	76	82	94	88	88
CFO:PAT%	91.1	272.3	250.1	-29.9	118.1

Source: Company, AnandRathi Research

Fig 6 – Segment-wise revenue break-up (Q2FY19)



Source: Company

Company update

A respected name in building materials in India, founded in 1946 and a pioneer of “green” building materials, HIL (formerly Hyderabad Industries Ltd.) offers roofing solutions, panels, wall blocks, plywood substitutes, high-quality pipes & fittings and industrial insulation. It manufactures a comprehensive range of products and is the flagship company of the C K Birla Group, a growing \$1.8bn conglomerate with diversified interests.

HIL is the market leader in fibre cement sheets, solid wall panels, and fly-ash bricks (AAC). Its Charminar brand is an established market leader in roofing solutions. HYSIL, an industrial thermal insulation, is widely used in energy-intensive industries. Birla Aerocon provides “green” building solutions, including dry-wall, wet-wall and plumbing solutions. Headquartered in Hyderabad, its plants are located across India. It has 20 manufacturing plants, 43 sales depots, eight sales offices, 2,500 stockists/distributors and 6,500 sub-dealers.

The Roofing Solutions division

HIL is the market leader in asbestos roofing with a 21% market share and the highest capacity (1.15m tonnes) of fibre cement sheets. It has a strong marketing network across the country and its brand, Charminar, is well established. Its roofing solutions comprise fibre cement sheets (capacity ~1.15m tonnes), non-asbestos cement sheets (~33,600 tonnes) and coloured steel sheets (~27,600 tonnes).

Asbestos Cement sheets

With seven manufacturing plants, HIL possess the highest capacity of 1.15m tonnes of AC sheets. Boosted by revived demand due to various government measures, lower tax rates under the GST resulting in a closing of the price gap between steel sheets and AC sheets, the good monsoon and the demonetization-impacted base year, FY18 volumes grew 6% (vs. a 10% decline in FY17) at ~70% capacity utilisation.

Coloured Steel sheets

To cater to demand (aesthetic look and feel) of urban customers, the company installed ~27,600 tonnes of coloured steel sheets at two manufacturing plants, at Maharashtra and Odisha.

‘Charminar Fortune’

This asbestos-free roofing product, launched in Q3FY18 to cater to the institutional segment (such as the Railways, as asbestos sheets are banned there), enabled the company to address 100% of the market. With installed capacity of ~33,600 tonnes at Konadapalli (AP), Charminar Fortune is expected to contribute substantially from Q2FY19.

Roofing sheets is the company’s cash cow, bringing ~65% to overall revenue in FY18. Over FY14-17, the roofing solutions division was flat. Driven by 6% y/y volume growth in asbestos cement sheets, the division’s revenue grew 4% y/y (net of taxes) to `1.6bn in Q2FY19. Its PBIT margin rose 751bps to 14%.

Being a key beneficiary of the upgrading of rural housing/infrastructure, revenue of the roofing-solutions division is expected to clock a 6% CAGR over FY18-20.

The Building Solutions division

HIL has positioned itself as a complete solutions provider in building materials. It caters to 18% of the regulated market in AAC blocks. Its building solutions consists of wet-walling and dry-walling solutions with products such as fly-ash bricks (AAC) - light-weight-large bricks, “smart fix”, “smart putty”, “smart plaster”, “Aerocon panels & boards” and “Smart Bond”. The share of its business from building solutions has grown from 15% to 30% in the last four years, reducing dependence on asbestos roofing products.

Wet-walling solutions

AAC blocks. With installed capacity of 825,000cu. metres, HIL is the leader in the regulated market. AAC blocks have several advantages in terms of speed of construction and cost savings, resulting in greater demand and preference for AAC blocks over red-clay bricks, despite the cost of AAC blocks being higher than the latter. With its better quality and the latest technology-driven manufacturing processes, volumes grew 5% to 702,586 cu. metres in FY18.

Other products in this category include “**Smart Fix**”, “**Smart Putty**” and “**Smart Plaster**”. Together, they offer a complete range of solutions to stakeholders in the building material industry.

Dry-walling solutions

Dry walling consists of “Aerocon Panels”, “Aerocon Boards” and “Smart Bond”. Aerocon panels, used to construct prefab structures and partition walls are easy to install and help in speedy construction, thereby expanding markets in the commercial and industrial sectors, infrastructure and low-cost housing.

HIL has capacity of 78,000 tonnes of solid wall panels. Due to its various advantages such as light weight, time-saving, termite- and water-resistance etc., panel volumes grew 22% y/y in Q2FY19, boosted by strong demand.

Building solutions revenue grew 30% y/y(net of taxes) in Q2FY19 and reported a ~8% PBIT margin, up 346bps. Driven by its solution-oriented focus of providing fresh uses for its product range, well-planned marketing, focus on quality, strong brand recall, multiple potential applications and lower tax rates under the GST, we expect the division to clock a 15% CAGR over FY18-20.

Others

The “others” division consists of plumbing solutions and wind power. For FY18, it brought 5% to overall revenue. We expect that with the ramped-up pipe capacities, the division would clock a 57% CAGR over FY18-20.

Plumbing solutions

HIL has 7,555 tonne capacity of C-PVC and U-PVC pipes, at Faridabad and Timmapur. To cater to growing demand with the expected growth in infrastructure and construction and the government-initiated ‘Swatch Bharat Abhiyan’ together with its sharper focus on irrigation and advertising the entire range of pipes & fittings, management implemented a `1.3bn capacity expansion for its pipes & fittings division, to 20,000 tonnes.

Commercial production of SWR (soil, waste and rain) pipes & pressure

pipes at Faridabad (capacity: 2,160 tonnes), started in Feb'18 and the greenfield expansion at Golan of SWR pipes, pressure pipes and SWR fittings with capacity of 2,160 tonnes and 900 tonnes respectively started in Apr'18. Further on 21st Aug'18, the company commenced commercial production of 5,218 tonnes of C-PVC and U-PVS capacity at Golan, taking overall capacity to 18,000 tpa.

Wind power

With existing capacity of 9.35MW, the company has wind turbines installed at Gujarat, Tamil Nadu and Rajasthan. The power generated at its Gujarat and Tamil Nadu units help it cut down power costs at its block manufacturing plants in those states.

Acquisition: Parador Holdings, GmbH

Parador Holdings, GmbH, founded in 1977, is a German, vertically integrated, full-range supplier, designing, manufacturing and distributing a wide range of flooring solutions, including resilient flooring, laminate and engineered wood floors, wall & ceiling panels, skirtings and related accessories. It has two manufacturing plants: Coesfeld (Germany) and Gussing (Austria) running at ~67% capacities. The company has long-standing relationships with all major customers and exports more than 50% of sales to over 80 countries, with ~60% of its revenue coming from outside Germany. Its net worth on 31stDec'17 was €10.3m.

The enterprise value of Parador is €82.8m and cash payable is €72.3m, which management said would be funded by a mix of debt (in euros and rupees) and internal accruals

Parador is the category leader in design and innovation with all products developed internally and produced with “Made in Germany” and “Made in Austria” quality. It has been a partner of the "Plant for-the-Planet" Foundation, which is active worldwide for afforestation and climate protection. Its products greatly complement HIL's product range.

The HIL Board acquired 100% stake (100,000 shares of face value €1 each) in Parador Holdings, GmbH, Germany, from shareholders on 27th Aug'18 through the company's wholly-owned subsidiary, HIL International, GmbH, Germany.

To finance the acquisition, the company infused equity of ₹2.73bn and a shareholder loan of ₹1.59bn in HIL International, GmbH, Germany, resulting in its standalone D/E ratio rising to 0.5x (and 1x for consolidated financials) on 30thSep'18, which management said would decline in a year.

Management said Parador results would be consolidated with HIL from the annual year ending 31stMar'19. The consolidation will take into account Parador financials for the period from 1stSep'18 to 31stMar'19.

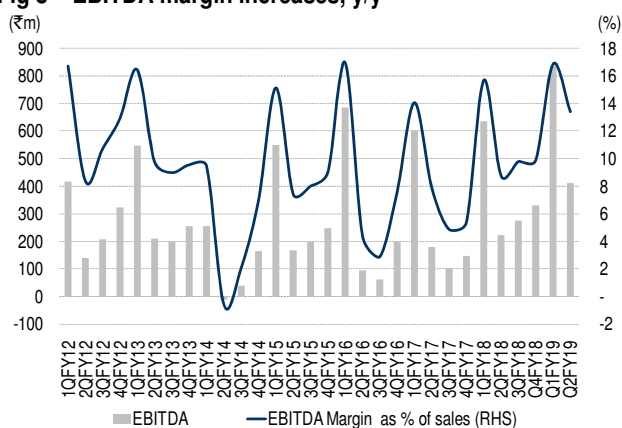
The acquisition would enable HIL to expand its product range by entering flooring solutions and gaining entry to European and other markets incl. India, South-East Asia and the USA, giving HIL a global footprint.

Fig 7 – Segment-wise trend

	Q2FY19	Q2FY19	Q1FY18	Q2FY18	Q3FY18	FY18	FY19	FY20
Net Revenue(₹m)								
Roofing solutions	1,594	3,520	1,987	1,596	1,533	8,567	9,081	9,717
Building solutions	1,142	1,165	1,133	1,050	881	3,999	4,598	5,288
Others	347	288	237	180	159	712	1,294	1,747
Segment PBIT(₹m)								
Roofing solutions	224	967	381	221	100	1,313	1,816	2,041
Building solutions	89	128	66	65	38	192	345	412
Others	(7)	(9)	17	8	44	71	39	140
PBIT Margin(%)								
Roofing solutions	14.0	27.5	19.2	13.8	6.5	15.3	20.0	21.0
Building solutions	7.8	10.9	5.8	6.2	4.3	4.8	7.5	7.8
Others	-1.9	-3.1	7.2	4.4	28.0	9.9	3.0	8.0

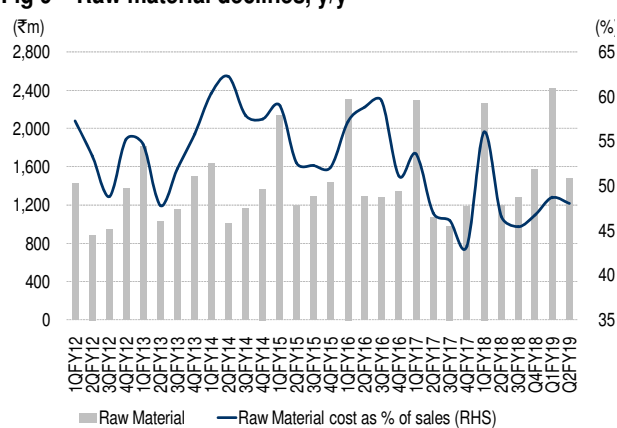
Source: Company, Anand Rathi Research

Fig 8 – EBITDA margin increases, y/y



Source: Company, Anand Rathi Research

Fig 9 – Raw material declines, y/y



Source: Company, Anand Rathi Research

Change in estimates

Bolstered by the roofing and building-solutions divisions' enhanced performances, the company's widening footprint in high-growth markets, product diversification and various cost-control measures, we raise our FY20 revenue estimates 0.4% and FY19e and FY20e EBITDA 14.6% and 13.2% respectively, and PAT 1.7% and 3.3%.

Fig 10 – Change in estimates

(₹ m)	Old estimates		New estimates		Change (%)	
	FY19e	FY20e	FY19e	FY20e	FY19e	FY20e
Revenue	14,974	16,688	14,974	16,752	(0.0)	0.4
EBITDA	1,876	2,262	2,149	2,560	14.6	13.2
PAT	1,076	1,335	1,094	1,380	1.7	3.3

Source: Anand Rathi Research

Key takeaways and Concall highlights

Operational highlights

- Other income includes ₹63m gain on sale of assets and ₹82m gain on re-statement of advances given to HIL International, GmBH.
- Volumes of AC sheets for the quarter grew 6% y/y to 145788 tonnes.
- The company has had no working capital borrowings for 10 consecutive years.

The Roofing Solutions division

- Management spoke about a 5% increase in prices in lieu of increasing input costs (higher diesel prices, forex fluctuations).
- It has applied for a patent for Charminar Fortune in three countries including India
- The Charminar brand enjoys a premium in prices to other brand named products.

The Building Solutions division

- Revenue from AAC blocks was ₹631m, panels ₹217m, boards ₹64m, dry-mix products ₹135m and thermal insulation ₹95m in Q2FY19 (vs. ₹501m, ₹174m, ₹55m, ₹78m and ₹77m respectively a year ago).
- The company continues to have a solutions-based approach in BS and is establishing a strong brand and direct connections with builders in order to groom and train them.

Plumbing Solutions

- The pipes division contributed ₹303m to revenue in Q2FY19 vs ₹132m a year ago.
- The SWR pipe capacity at Golan is running at 100% capacity while other capacities are running at 67%.

Parador

- Of Parador's sales, 72% is through retail and DIY (Do-it-Yourself); the rest through an e-channel.
- HIL had taken a ₹2.76bn Indian rupee loan at 8.5% interest, and a €22m loan at 3.5% interest.
- Parador contributed revenue of €142.2m and €10.7m in EBITDA in CY17.
- Management said 70% of premium wood flooring is imported.
- Parador manufactures resilient flooring, laminate and engineered wood floors, wall & ceiling panels, skirting and related accessories and exports to ~80 countries. 50% of its sales are outside Germany.

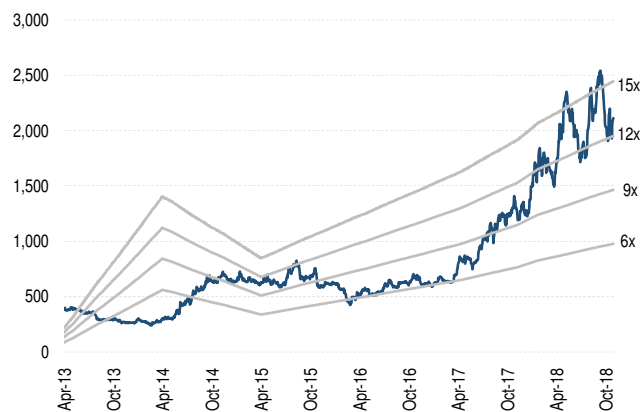
Outlook

- Management is planning to set up an additional plant for wall putty as the Jhajjar plant is running at 100% capacity.

Valuation

At the ruling price, the stock trades at an EV/EBITDA of 7x and aP/BV of 2.1x on FY20e. We believe that HIL, with its leading position, expansion in a high-growth market and better operating performance, will post a strong performance. We, therefore, retain our Buy rating, with a target price of ₹2,763 at a 15x PE on FY20e.

Fig 11 – PE band



Source: Bloomberg, Anand Rathi Research

Risks

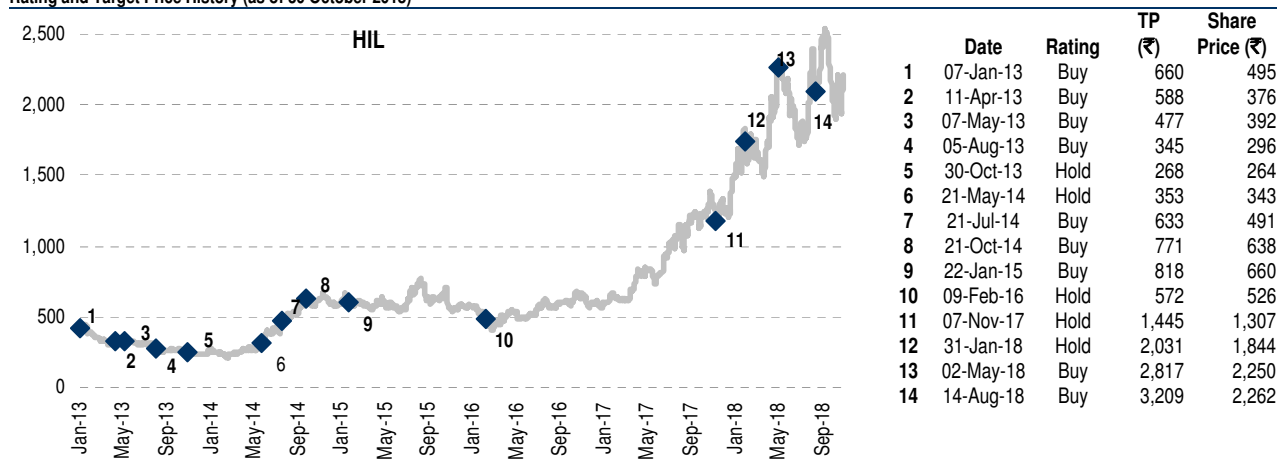
- **Competition may pinch prices.** The unregulated market poses stiff competition to HIL, restricting its pricing power.
- **Fluctuating raw-material prices.** The persistent rise in prices of the raw material, fly ash, is a continuing cause of concern.

Appendix

Analyst Certification

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Ratings Guide (12 months)

	Buy	Hold	Sell
Large Caps (>US\$1bn)	>15%	5-15%	<5%
Mid/Small Caps (<US\$1bn)	>25%	5-25%	<5%

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