MOTILAL OSWAL

26 July 2019

1QFY20 Results Update | Sector: Capital Goods

Crompton Gr. Con

BSE SENSEX	S&P CNX
37,831	11,252

Bloomberg	CROMPTON IN
Equity Shares (m)	627
M.Cap.(INRb)/(USDb)	141.7 / 2.1
52-Week Range (INR)	272 / 190
1, 6, 12 Rel. Per (%)	2/0/-7
12M Avg Val (INR M)	173
Free float (%)	65.6

Financials & Valuations (INR b)

Y/E Mar	2019	2020E	2021E
Net Sales	44.8	51.2	59.0
EBITDA	5.9	7.2	8.5
PAT	4.0	4.6	5.7
EPS (INR)	6.0	7.4	9.0
Gr. (%)	15.5	24.0	21.9
BV/Sh (INR)	17.5	21.8	27.0
RoE (%)	39.6	37.6	36.9
RoCE (%)	27.8	28.2	32.2
P/E (x)	37.7	30.4	25.0
P/BV (x)	12.8	10.3	8.3

Estimate change ⟷

TP change ⟷

Rating change ⟷

CMP: INR226 TP: INR270 (+19%) Buy

Weak lighting segment performance impacts results

- **Earnings miss estimates marginally:** 1QFY20 revenue grew 12% YoY to INR13.5b (in line with our est. of INR13.7b), while EBITDA was up 15% YoY to INR1.9b (5% below our est. of INR2b). Reported EBITDA margin improved 30bp YoY to 14.2% (lower than our est. of 14.7%), while other income came in higher than our expectation at INR173m. Thus, adj. PAT at INR1.2b was 6% below our expectation of INR1.3b.
- **Lighting segment performance disappoints:** Lighting segment revenue declined 2% YoY to INR2.7b (our est. INR3b; +12% YoY). Revenue was impacted by (a) price erosion witnessed in the LED segment, (b) decline in the conventional lighting segment (21% YoY decline), and (c) B2B sales affected by elections. EBIT declined 25% YoY to INR141m (our est. INR307m) on account of 170bp margin erosion to 5.1% (our est. 10%). Margin impact was on account of (a) 300bp YoY higher ad spends during the quarter, (b) 200-300bp impact due to incremental provision for ECL, and (c) investment in the B2B business. Management expects Lighting margins to revert to double-digits on sustainable basis gradually.
- **ECD segment makes up for weak lighting segment performance:** ECD segment registered healthy 16% YoY revenue growth to INR10.7b (our est. INR10.6b), supported by strong double-digit revenue growth across fans, pumps and appliances. EBIT margins at 20.3% (+80bp YoY), were ahead of our est. of 19.5%. Margin expansion was supported by better revenue mix.
- **Maintain Buy:** We like CROMPTON for its strong product portfolio, established brand, market leadership, wide distribution network, robust RoE/RoCE profile and healthy free cash flow generating business model. We maintain our **Buy** rating with TP of INR270 (30x Mar'21 EPS).

Crompton: Quarterly Estimates (INR M)

	FY19				FY20				FY19	FY20	Vs Est.	Var.
Y/E March	1Q	2Q	3Q	4Q	1Q	2QE	3QE	4QE			1QE	(%)
Sales	12,039	10,378	10,303	12,069	13,468	11,968	11,880	13,917	44,789	51,233	13,705	-1.7%
Change (%)	14.1	8.1	9.8	7.2	11.9	15.3	15.3	15.3	9.8	14.4	13.8	
EBITDA	1,673	1,239	1,261	1,685	1,919	1,588	1,622	2,054	5,858	7,182	2,018	-4.9%
Change (%)	29.3	2.7	8.3	2.5	14.7	28.1	28.6	21.9	10.3	22.6	20.6	
As of % Sales	13.9	11.9	12.2	14.0	14.2	13.3	13.7	14.8	13.1	14.0	14.7	
Depreciation	31	32	33	33	58	60	60	53	129	231	35	
Interest	152	150	150	143	150	80	80	70	596	380	148	
Other Income	88	98	124	172	173	60	60	57	483	350	98	
PBT	1,578	1,155	1,202	1,681	1,885	1,508	1,542	1,988	5,616	6,921	1,933	-2.5%
Tax	535	386	405	549	660	498	509	618	1,875	2,284	638	
Effective Tax Rate (%)	33.9	33.4	33.7	32.7	35.0	33.0	33.0	31.1	33.4	33.0	33.0	
Adjusted PAT	1,043	769	797	1,132	1,224	1,010	1,033	1,370	3,741	4,637	1,295	-5.5%
Change (%)	30.0	8.6	14.7	9.7	17.4	31.3	29.6	21.0	15.5	24.0	24.2	
Extra-ordinary Income (net)	-	-	-	284.5	-	-	-	-	284.5	-	-	
Reported PAT	1,043	769	797	1,417	1,224	1,010	1,033	1,370	4,025	4,637	1,295	-5.5%
Change (%)	30.0	8.6	14.7	37.3	17.4	31.3	29.6	(3.3)	24.3	15.2	24.2	

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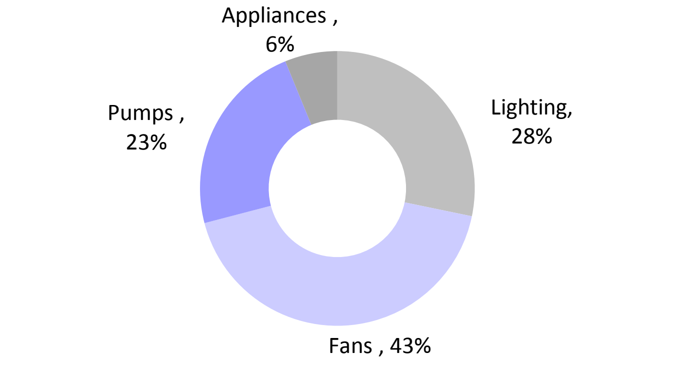
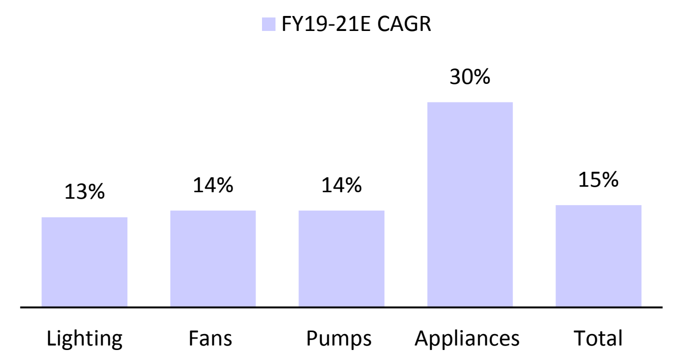
Story in charts

Exhibit 1: FY19 revenue break-up



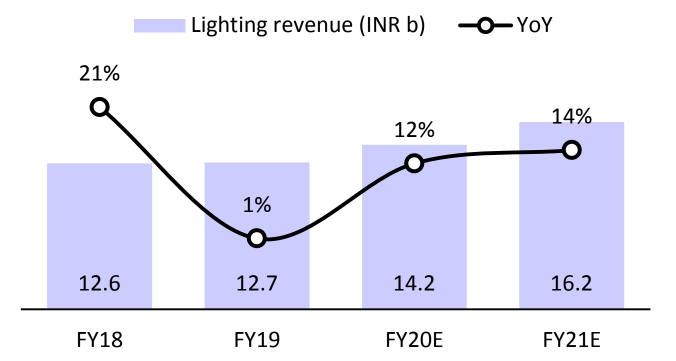
Source: MOFSL, Company

Exhibit 2: FY19-21 CAGR estimates by category



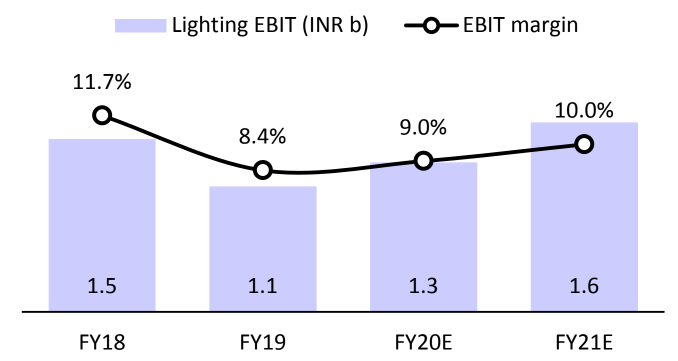
Source: MOFSL, Company

Exhibit 3: Expect lighting revenue CAGR of 13% over FY19-21



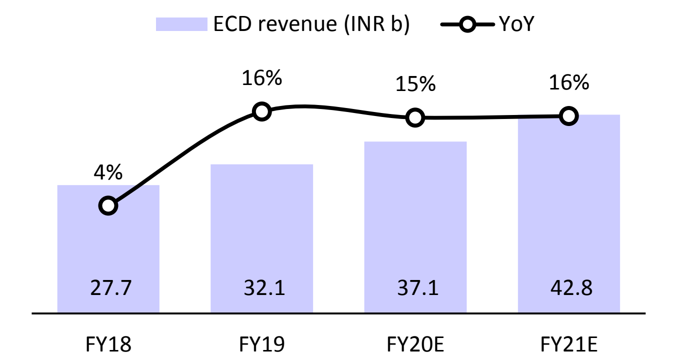
Source: MOFSL, Company

Exhibit 4: Lighting margins to scale back to double-digits



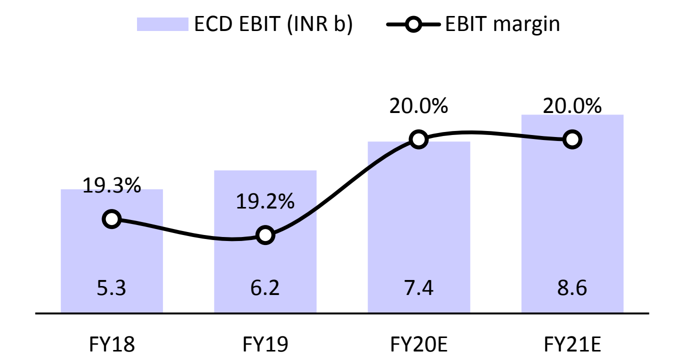
Source: MOFSL, Company

Exhibit 5: Expect ECD revenue CAGR of 15% over FY19-21



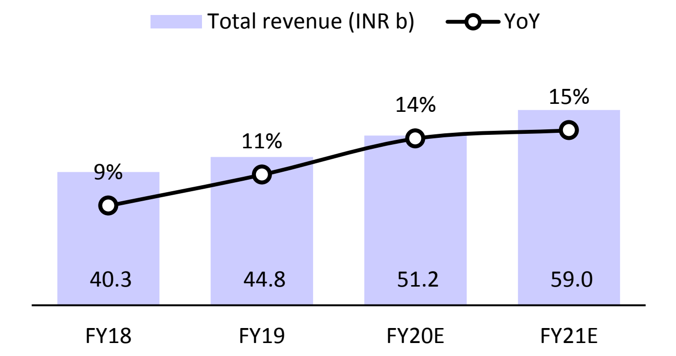
Source: MOFSL, Company

Exhibit 6: ECD margins to improve 80bp to 20% levels



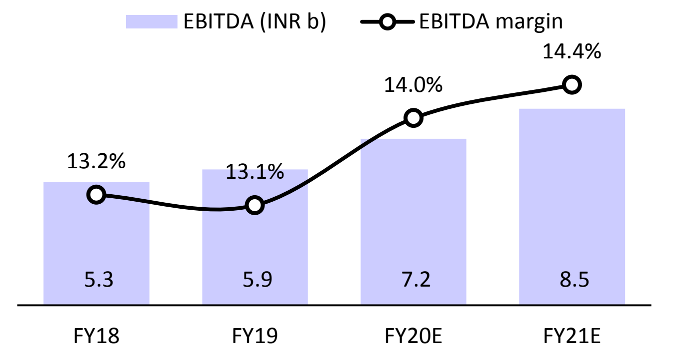
Source: MOFSL, Company

Exhibit 7: Expect revenue CAGR of 15% over FY19-21



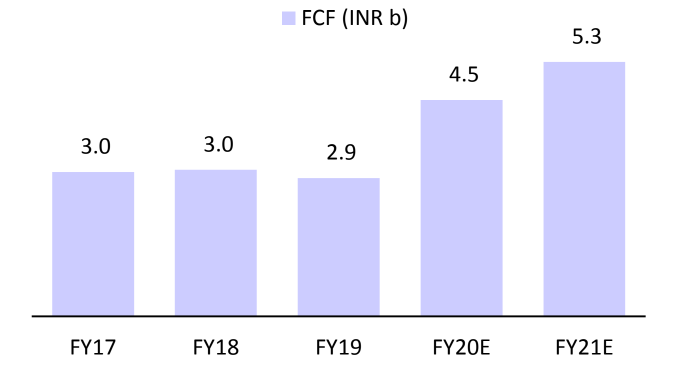
Source: MOFSL, Company

Exhibit 8: EBITDA margin to expand to 14.4% by FY21



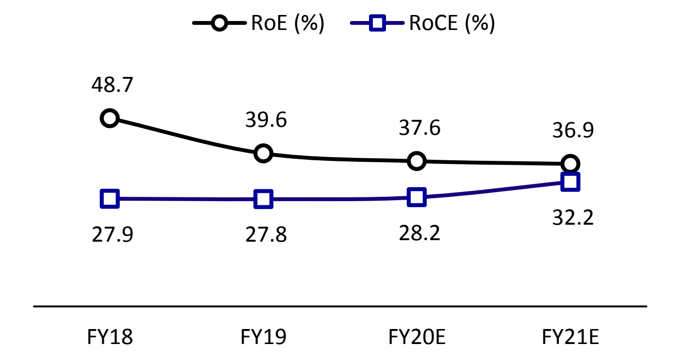
Source: MOFSL, Company

Exhibit 9: Strong FCF generation to drive re-rating



Source: MOFSL, Company

Exhibit 10: Return ratios to remain healthy

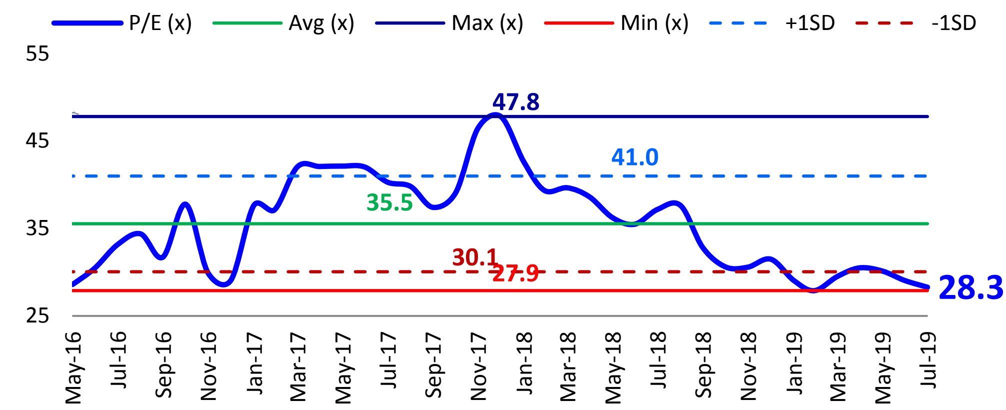


Source: MOFSL, Company

Valuation and view

Valuation extremely comfortable, but needs backing-up with category expansion: Crompton trades at FY20/21E P/E of 30x/25x. Since the demerger of the company from its erstwhile parent, the company has delivered good financial results, led by margin expansion. However, revenue growth has lagged peers like Havells, attributable to its go-to-market (GTM) strategy and slow progress on new launches. We estimate EPS CAGR (FY19-21) of 23% on the back of 15.0% CAGR in revenue. Crompton's strong FCF generation is under-appreciated at current valuations, in our view. Maintain **Buy** at attractive valuations.

Exhibit 11: Valuations tapered off given the pressure witnessed in core business margins



Source: MOFSL, Company

Concall highlights

Overall business environment

- The ECD segment registered healthy revenue growth of 16% YoY to INR10.7b (our est. INR10.6b), supported by strong double-digit revenue growth across fans, pumps and appliances. The segment can grow a further 15% due to an increase in its product range and geographic expansion. EBIT margins stood at 20.3% (+80bp YoY), ahead of our estimate of 19.5%.
- Company wants to scale up the water heater and air cooler business, intending to rank as 2nd/3rd in the segment in the medium term.
- Ad spends for the quarter stood at INR290m v/s INR240m.

Lighting – launched an innovative anti-bacterial bulb

- LED sales increased 4% YoY in value terms and 12% in volume terms. Conventional lighting, which forms 20% of the lighting segment sales, registered 21% YoY sales decline.
- For B2C, which forms 50% of the lighting segment sales, company is focused on introducing new products, increasing ad spends to support new product launches and boosting the distribution network. Launched new products like anti-bacterial bulb and five-star rate bulb, which are sold at 20% premium and now form 15% of the lamp sales.
- The B2B business, which forms balance 50% of the lighting business sales, has seen a slowdown given the delay in awarding from government entities due to the elections. Crompton has focused on improving its sales force and has appointed 12 new account managers to scale up the business meaningfully. B2B order pipeline remains robust.
- Lighting margins witnessed 100bp gross margin improvement. However, EBIT margins declined 160bp YoY to 5.1%. Margin compression was on account of (a) 300bp YoY higher ad spends during the quarter, (b) 200-300bp impact on due to incremental provision for ECL, and (c) investment in B2B business. Management expects Lighting margins to revert to double-digits on sustainable basis gradually.
- Led bulb is seeing price stabilization; however, there is price erosion of 10% in the batons and panels category.
- EESL sales for the quarter stood at INR420m.
- Expect double-digit bottom line growth in the lighting segment, going ahead.

Fans

- Market share further improved by 100bp in the fans segment.
- Premium category fans registered 24% YoY growth.
- Aura Fluidic (5-year warranty) and the anti-dust fan are the growth drivers in the fans category.

Pumps

- *CREST Mini* is doing well. Pumps segment registered double-digit volume as well as value growth Residential pumps form 80% of the category sales and 20% comes in from agriculture pumps forming another 20% of sales.

Water heater/ air coolers

- Water heaters registered 44% YoY growth during the quarter and air coolers registered 138% YoY growth. Air cooler growth was supported by desert coolers.
- Crompton intends to get ranked 2nd/3rd in both the segments in the medium term.

Financials and valuations

Income Statement						(INR Million)
Y/E March	**FY16**	**FY17**	**FY18**	**FY19**	**FY20E**	**FY21E**
Total Revenues	**18,117**	**39,009**	**40,797**	**44,789**	**51,233**	**58,970**
Change (%)	-	115.3	4.6	9.8	14.4	15.1
Raw Materials	12,702	27,335	27,996	30,918	35,095	40,277
Staff Cost	1,005	2,322	2,827	2,919	3,218	3,669
Other Expenses	2,315	4,506	4,664	5,094	5,738	6,546
EBITDA	**2,095**	**4,846**	**5,310**	**5,858**	**7,182**	**8,479**
% of Total Revenues	11.6	12.4	13.0	13.1	14.0	14.4
Depreciation	63	110	126	129	231	244
Other Income	39	195	308	483	350	400
Interest	355	655	637	596	380	198
PBT	**1,716**	**4,276**	**4,854**	**5,616**	**6,921**	**8,437**
Tax	525	1,419	1,617	1,875	2,284	2,784
Rate (%)	30.6	33.2	33.3	33.4	33.0	33.0
Adjusted PAT	**1,191**	**2,857**	**3,238**	**3,741**	**4,637**	**5,653**
Extra-ordinary Income (net)	-139	-25	0	285	0	0
Reported PAT	**1,052**	**2,832**	**3,238**	**4,025**	**4,637**	**5,653**
Change (%)	-96.7	169.2	14.3	24.3	15.2	21.9

Balance Sheet						(INR Million)
Y/E March	**FY16**	**FY17**	**FY18**	**FY19**	**FY20E**	**FY21E**
Share Capital	1,254	1,254	1,254	1,254	1,254	1,254
Reserves	1,034	4,138	6,641	9,731	12,420	15,699
Net Worth	**2,287**	**5,392**	**7,895**	**10,985**	**13,674**	**16,953**
Loans	6,445	6,500	6,486	6,493	3,493	1,793
Deferred Tax Liability	-43	-182	0	0	0	0
Capital Employed	**8,689**	**11,710**	**14,381**	**17,477**	**17,167**	**18,746**
Gross Fixed Assets	2,024	931	1,055	1,197	1,697	2,197
Less: Depreciation	1,238	110	234	359	590	834
Net Fixed Assets	**786**	**821**	**822**	**837**	**1,106**	**1,363**
Capital WIP	1	1	6	10	10	10
Goodwill	7,794	7,794	7,794	7,794	7,794	7,794
Investments		3,185	0	142	142	142
Curr. Assets	**7,907**	**9,167**	**15,628**	**17,915**	**18,662**	**21,577**
Inventory	2,100	2,348	3,032	3,524	4,031	4,640
Debtors	4,165	5,434	5,536	5,660	6,474	7,452
Cash & Bank Balance	900	700	5,450	6,724	5,861	6,843
Loans & Advances	742	685	0	0	0	0
Other Assets	0	0	1,610	2,007	2,296	2,643
Current Liab. & Prov.	**7,798**	**9,258**	**9,869**	**9,221**	**10,547**	**12,140**
Current Liabilities	7,373	8,448	8,719	7,530	8,613	9,914
Provisions	425	811	1,150	1,691	1,934	2,226
Net Current Assets	**109**	**-91**	**5,759**	**8,694**	**8,115**	**9,437**
Application of Funds	**8,689**	**11,710**	**14,381**	**17,477**	**17,167**	**18,746**

Financials and valuations

Ratios

Y/E March	FY16	FY17	FY18	FY19	FY20E	FY21E
Basic (INR)						
Adj EPS	**1.7**	**4.5**	**5.2**	**6.0**	**7.4**	**9.0**
Cash EPS	1.8	4.7	5.4	6.2	7.8	9.4
Book Value	3.6	8.6	12.6	17.5	21.8	27.0
DPS	0.0	1.5	1.8	2.1	2.6	3.2
Payout (incl. Div. Tax.)	0.0	33.5	33.9	32.5	35.0	35.0
Valuation (x)						
P/E	134.1	49.8	43.6	37.7	30.4	25.0
Cash P/E	126.5	47.9	41.9	36.5	29.0	23.9
EV/EBITDA	70.0	30.3	26.8	24.0	19.3	16.0
EV/Sales	8.1	3.8	3.5	3.1	2.7	2.3
Price/Book Value	61.7	26.2	17.9	12.8	10.3	8.3
Dividend Yield (%)	-	0.7	0.8	0.9	1.2	1.4
Profitability Ratios (%)						
RoE	46.0	73.8	48.7	39.6	37.6	36.9
RoCE	22.0	31.7	27.9	27.8	28.2	32.2
RoIC	18.0	39.5	38.7	36.0	41.7	46.9
Turnover Ratios						
Debtors (Days)	42	51	50	46	46	46
Inventory (Days)	21	22	27	29	29	29
Creditors. (Days)	68	67	69	54	54	54
Asset Turnover (x)	2.1	3.3	2.8	2.6	3.0	3.1
Leverage Ratio						
Debt/Equity (x)	2.8	1.2	0.8	0.6	0.3	0.1

Cash Flow Statement **(INR Million)**

Y/E March	FY16	FY17	FY18	FY19	FY20E	FY21E
PBT before EO Items	**1,716**	**4,276**	**4,854**	**5,616**	**6,921**	**8,437**
Depreciation	63	110	126	129	231	244
Interest	355	655	511	399	380	198
Direct Taxes Paid	-525	-1,419	-1,812	-1,994	-2,284	-2,784
(Inc)/Dec in WC	(229)	(497)	(933)	(1,202)	(283)	(340)
CF from Operations	**1,379**	**3,126**	**2,746**	**2,949**	**4,965**	**5,755**
EO Income	0	0	409	66	0	0
CF from Oper. Incl. EO Items	**1,379**	**3,126**	**3,154**	**3,014**	**4,965**	**5,755**
(Inc)/Dec in FA	209	(150)	(130)	(160)	(500)	(500)
Free Cash Flow	**1,588**	**2,976**	**3,025**	**2,855**	**4,465**	**5,255**
Investment & Others	0	(3,324)	(197)	281	0	0
CF from Investments	**209**	**-3,474**	**-327**	**121**	**-500**	**-500**
(Inc)/Dec in Networth	(18)	1,413	7	38	0	0
(Inc)/Dec in Debt	-316	56	0	0	-3,000	-1,700
Interest Paid	-355	-655	-634	-587	-380	-198
Dividend Paid	0	-1,140	-1,129	-1,312	-1,948	-2,374
Others		475	3,721			
CF from Fin. Activity	**(689)**	**148**	**1,967**	**(1,862)**	**(5,327)**	**(4,273)**
Inc/Dec of Cash	**899**	**(200)**	**4,794**	**1,274**	**(863)**	**982**
Add: Beginning Balance	1	900	656	5,450	6,724	5,861
Closing Balance	**900**	**700**	**5,450**	**6,724**	**5,861**	**6,843**

Explanation of Investment Rating	
Investment Rating	**Expected return (over 12-month)**
BUY	>=15%
SELL	< - 10%
NEUTRAL	< - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

*In case the recommendation given by the Research Analyst is inconsistent with the investment rating legend for a continuous period of 30 days, the Research Analyst shall within following 30 days take appropriate measures to make the recommendation consistent with the investment rating legend.

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