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Honeywell Automation India Limited

Optimistic of better times ahead

Capital Goods	Sharekhan code: HONAUT	Company Update

Summary

- We retain a Buy on Honeywell Automation India with a revised price target of Rs. 56,265 considering its strong earnings growth potential, led by a domestic economic recovery.
- The management expects FY2021 performance to be better than FY2020, backed by execution capabilities and growing demand for industrial automation and software solutions.
- Growth in the domestic business is expected to benefit Honeywell driven by increasing technological capabilities with large opportunities in sectors such as oil & gas, pharma & life sciences, smart cities, airports and building solutions. This provides strong growth visibility for FY2022. Exports to remain steady.
- New brand to cater to SMEs, providing tailor-made products and solutions. Company foresees huge opportunity ahead and expects business to contribute 10% of revenues in 2-3 years.

3R MATRIX

	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)		✓	

\+ Positive = Neutral - Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↔	

Reco/View	Change
Reco: **Buy**	↔
CMP: **Rs. 48,901**	
Price Target: **Rs. 56,265**	↑

↑ Upgrade ↔ Maintain ↓ Downgrade

Company details

Market cap:	Rs. 43,236 cr
52-week high/low:	Rs. 49799/20142
NSE volume: (No of shares)	4,562
BSE code:	517174
NSE code:	HONAUT
Free float: (No of shares)	0.2 cr

Shareholding (%)

Promoters	75.0
FII	1.0
DII	13.8
Others	10.2

Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	17	53	44	57
Relative to Sensex	18	44	13	2

Sharekhan Research, Bloomberg

Honeywell Automation India Limited (Honeywell), is a leader in integrated automation and software solutions, including process solutions and building solutions. In a recent media interaction, the management indicated that overall capex in the industrial automation segment is rising (India's total industrial automation products market stands at ~over Rs. 42,500 crore-plus) and looks optimistic ahead too with renewed interest on more productivity and digitalisation from clients and Honeywell India with its diversified portfolio is well-placed to reap benefits from the same. With growing trends towards remote working as more firm shifting to that along with more clients adopting digital transformation with an impetus towards digital security. The company is also at the forefront in providing solutions in the given segments. Further investments in these segments provide optimism as well, given the healthy order pipeline ahead. Further, Honeywell is witnessing opportunities across pharmaceuticals & life-sciences, where the company has been investing and it has very strong solutions here (products like BluTag 360TM being a digital tracking and shipment condition monitoring solution for vaccines and drugs). Other areas of opportunity include the oil & gas sector, especially gas (infrastructure for gas pipelines, equipment for storage and distribution being required) and industrial digital transformation where product offerings in cyber security provides huge opportunity. Domestically, the company typically targets 1.5-2x of GDP growth as far as order booking is concerned and if the real GDP is expected at 10% the company expects to grow its current order book by ~15%, providing a strong outlook for FY2022.

Honeywell has been also exploring newer areas for growth and has recently launched a new brand — "Impact" to take affordable and easy-to-use automation and digital technologies to the SME in India. The company had till now focused only on the large enterprise segment with a portfolio for premium companies in India and the company will now develop products and solutions that are developed locally and tailor-made to meet the SME sector's needs, which include products and solutions for productivity, cost control, revenue leakage, quality and compliance in India and expect this to contribute 10% of the revenues in next 2-3 years. The company expects other newer products in the offing includes warehouse automation, digital safety, productivity solutions and asset health monitoring. With strong parentage, the company would be leveraging the global sourcing teams available with Honeywell to access semiconductors and electronic components for automation and digitisation products. On the exports front (~45% of sales), the business remains buoyant and all the large orders from clients remains intact. Overall, the company expects strong growth in FY22, backed by its execution capabilities and ample opportunities. Honeywell is expected to benefit from domestic growth driven by increasing technological capabilities and steady export opportunities from global group entities. Going ahead, the company's focus on developing new products and services, foray into new industries and addressing a growing mass mid-market is expected to maintain healthy net earnings growth trend (23% CAGR over FY2021E-FY2023E). Currently, the stock is trading at a P/E of 69.7x and 57.4x its FY22E and FY23 earnings. Led by AatmaNirbhar Bharat, localised procurement and a faster pick-up in manufacturing and automation activity, the entire sector is getting rerated and Honeywell remains at the forefront of leveraging opportunities, which trades at a discount to its peak 5-year average multiple. Hence, we maintain a Buy rating on the Honeywell with modestly increasing our target PE to factor overall rerating in the space along with strong growth potential in automation across industries, robust balance sheet and steady cash flow generation to arrive at a revised price target of Rs 56,265.

Our Call

Valuation –Retain Buy with revised price target of Rs. 56,265: The company has multiple domestic growth levers like government's infrastructure investments such as smart cities, airports, real estate development, industrial internet of Things (IIOT), AatmaNirbhar Bharat initiatives which we believe would help the company maintain a healthy growth trend. An asset-light model (zero debt), strong cash position healthy operating cash flow generation, strong return ratios consistent dividend paying record justify the stock's premium valuation. Currently, the stock is trading at a P/E of 69.7x and 57.4x its FY22E and FY23 earnings. Led by AatmaNirbhar Bharat, localized procurement and a faster pick-up in manufacturing and automation activity, the entire sector is getting rerated and Honeywell remains at the forefront the leverage the opportunities, which trades at a discount to its peak 5-year average multiple. Hence, we maintain a Buy rating on the Honeywell with modestly increasing our target PE to factor overall re-rating in the space and a strong growth potential in automation across industries, robust balance sheet, and steady cash flow generation to arrive at a revised price target of Rs. 56,265.

Key Risks

- A significant proportion of revenue and profits come from Honeywell International and its affiliates; and
- Softening of investments domestically as well as globally, increase in crude oil prices and volatility in foreign exchange rate would affect business operations.

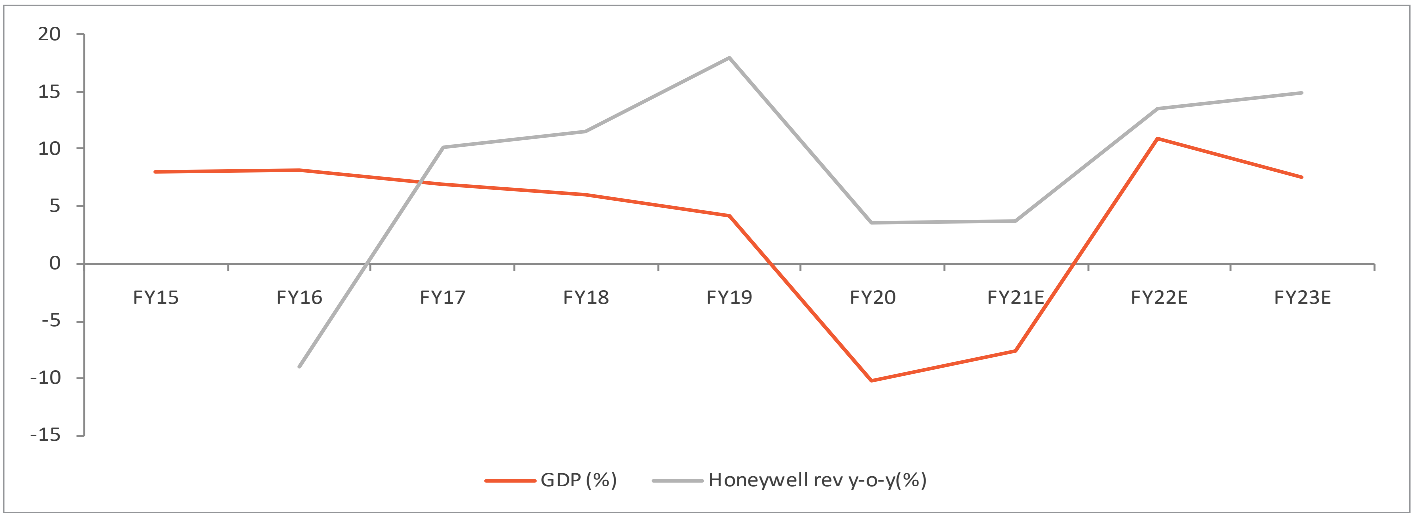
Valuation (Standalone) Rs cr

Particulars	FY20	FY21E	FY22E	FY23E
Revenue	3,290	3,258	3,735	4,313
OPM (%)	19.3	20.0	21.6	21.8
Adjusted PAT	491	499	621	754
% Y-o-Y growth	37.0	1.6	24.3	21.4
Adjusted EPS (Rs.)	556.0	564.8	702.0	852.5
P/E (x)	88.0	86.6	69.7	57.4
P/B (x)	19.8	19.7	15.6	12.4
EV/EBIDTA (x)	65.6	64.1	51.1	43.0
RoNW (%)	25.0	22.8	25.0	24.1
RoCE (%)	31.4	28.3	31.1	28.8

Source: Company; Sharekhan estimates

Strong beneficiary of the automation drive: Honeywell Automation India Limited (Honeywell), is a leader in integrated automation and software solutions, including process solutions and building solutions. In a recent media interaction, the management indicated that overall capex in the industrial automation segment is rising (India's total industrial automation products market stands at ~over Rs. 42,500 crore-plus) and looks optimistic ahead too with renewed interest on more productivity and digitalisation and Honeywell India with its diversified portfolio is well-placed to reap benefits from the same. With growing trends towards remote working as more firm shifting to that along with more clients adopting digital transformation with an impetus towards digital security. The company is also at the forefront in providing solutions in the given segments. Further investments in these segments provide optimism as well, given the healthy order pipeline ahead. Further, Honeywell is witnessing opportunities across pharmaceuticals & life-sciences, where the company has been investing and it has very strong solutions here (products like BluTag 360TM being a digital tracking and shipment condition monitoring solution for vaccines and drugs). Other areas of opportunity include the oil & gas sector, especially gas (infrastructure for gas pipelines, equipment for storage and distribution being required) and industrial digital transformation where product offerings in cyber security provides huge opportunity. Domestically, the company typically targets 1.5-2x of GDP growth as far as order booking is concerned and if the real GDP is expected at 10% the company expects to grow its current order book by ~15%, providing a strong outlook for FY2022.

GDP growth vs Honeywell revenue growth



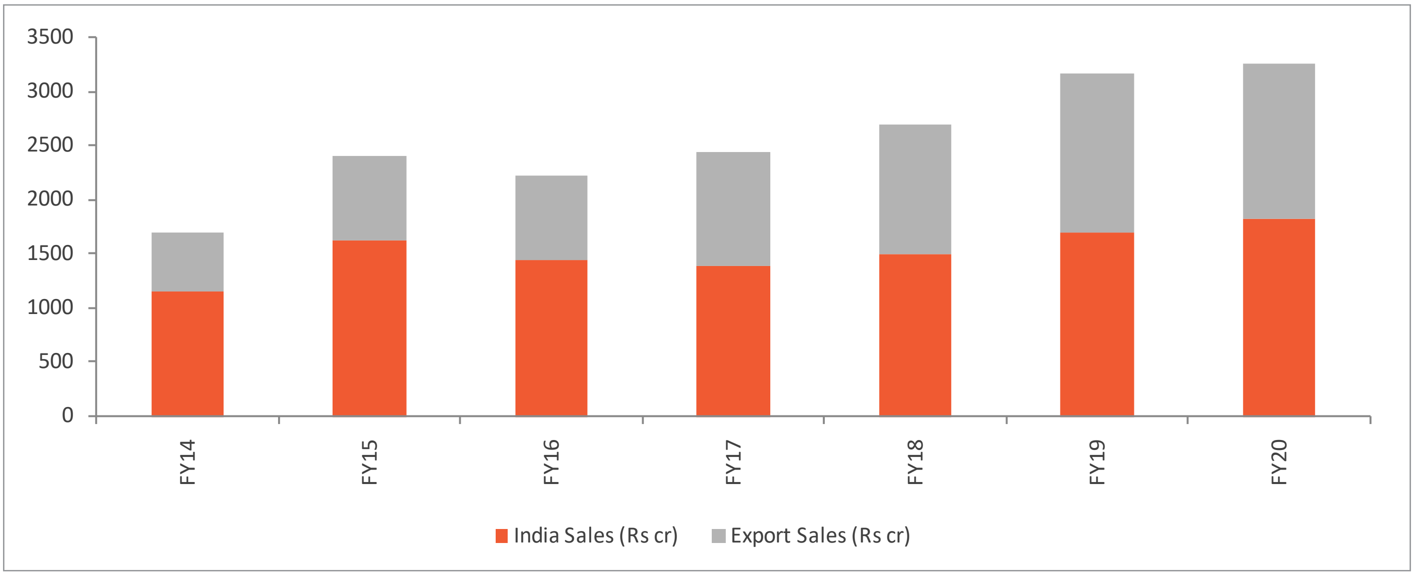
Source: MoSPI, Company

Segment-wise growth levers

Business vertical	Potential Customers	Key growth levers / focus areas
Process solutions	Oil and gas, refining, pulp and paper, industrial power generation, chemical and petchem, pharma, metals/mining	• Focus on expanding local engineering, product development and manufacturing capabilities. • Enhancing reach to serve large and growing mass mid-market in India.
Building solutions	IT, Pharma, Industrial/commercial, airports, metro and railways, smart cities.	• Honeywell exploring opportunities to create India-specific integrated products for different sectors.
Building management system	Airports, stadiums, metro, IT, residential, industrial, hospitality and healthcare	• Focus on new launches: recently introduced mechanical PICV, Variable Frequency drives, Piston type PRVs. • Focus on sales deployment, on boarding, channel excellence and pipeline management.
Sensing and IOT	Diverse customer base including transportation, aerospace, medical, industrial.	• Focus on consolidation of small business a/c to master's distributors, which is helping company direct sales team focus on key a/c management with a wider portfolio. • Localisation of child parts for transportation segmentlike stalk controls, pressure switches is planned to roll out from Pune. This will improve supply chain, quality control and customer satisfaction. • Putting extra efforts in rail/stationary power to generate long term business for packaged sensors.

Newer products and initiatives to drive growth: Honeywell has been also exploring newer areas for growth and has recently launched a new brand — "Impact by Honeywell" — to take affordable and easy-to-use automation and digital technologies to the SME in India. The company had till now focused only on the large enterprise segment with a portfolio for premium companies in India and the company will now develop products and solutions that are developed locally and tailor-made to meet the SME sector's needs, which include products and solutions for productivity, cost control, revenue leakage, quality and compliance in India and expect this to contribute 10% of the revenues in next 2-3 years. The company expects other newer products in the offing includes warehouse automation, digital safety, productivity solutions and asset health monitoring. With strong parentage, the company would be leveraging the global sourcing teams available with Honeywell to access semiconductors and electronic components for automation and digitisation products. On the exports front (~45% of sales), the business remains buoyant and all the large orders from clients remains intact. Overall, the company expects witness strong growth in FY22, backed by its execution capabilities and ample opportunities. Honeywell is expected to benefit from domestic growth driven by increasing technological capabilities and steady export opportunities from global group entities.

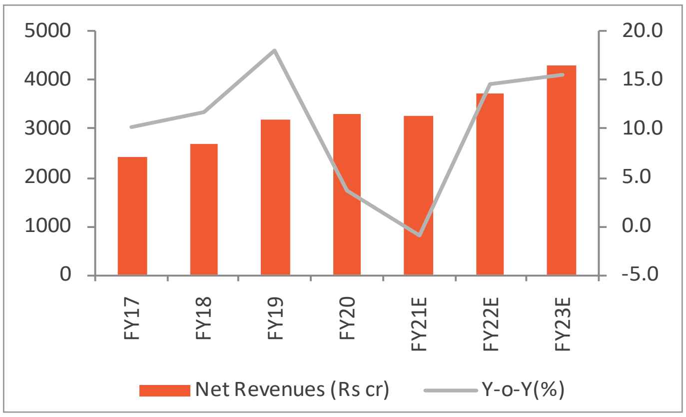
Domestic sales and Export trend



Source: MoSPI, Company

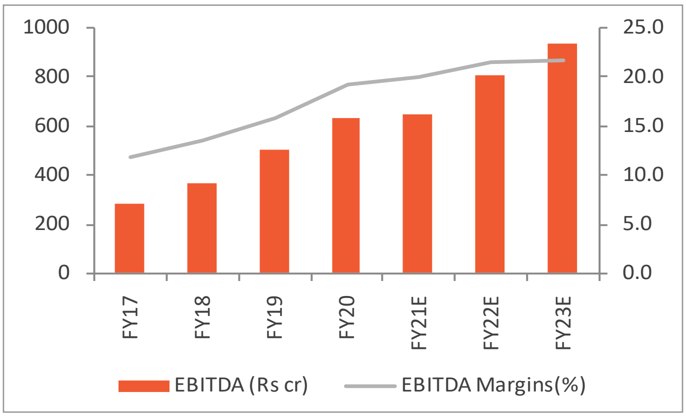
Financials in charts

Revenue trend



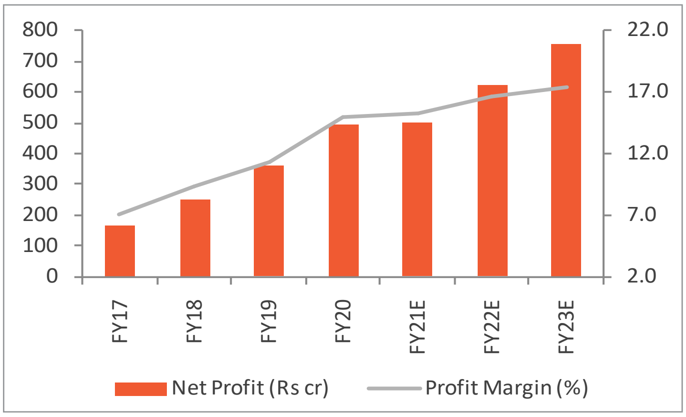
Source: Company, Sharekhan Research

EBITDA trend



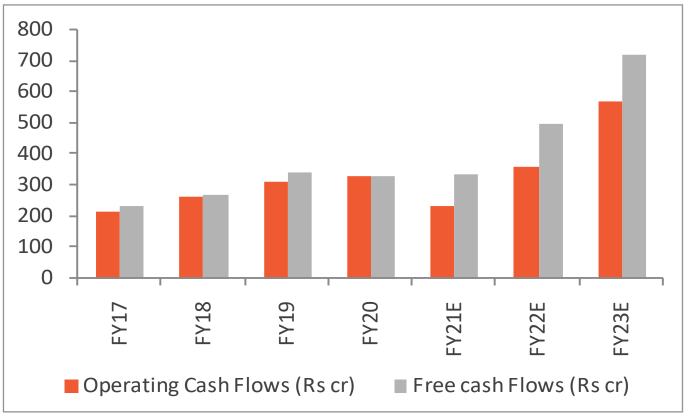
Source: Company, Sharekhan Research

Net Profit trend



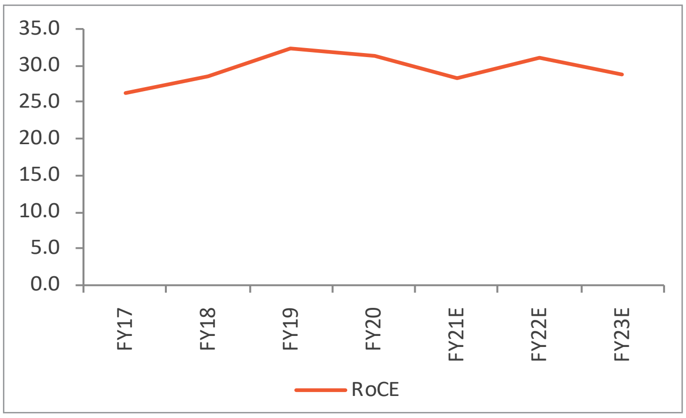
Source: Company, Sharekhan Research

OCF/FCF trend



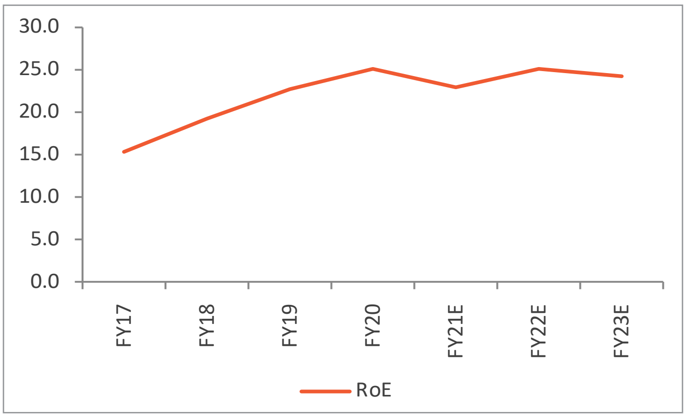
Source: Company, Sharekhan Research

ROCE trend



Source: Company, Sharekhan Research

ROE trend



Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector view - Multiple structural growth enablers to drive growth

India's focus on turning itself into a manufacturing hub through 'Make in India', huge investments in infrastructure across sub-sectors through the National Infrastructure Pipeline (NIP) over FY2020-FY2025 and ensuring energy security through increased share of renewable energy are key growth levers for Honeywell, which has positioned itself across various industries viz. oil & gas, chemical/petrochemicals, metals & mining, infrastructure and residential and commercial construction. The Indian's ambition is tied with its increasing requirement of adopting automation technologies such as artificial intelligence (AI), IoT (connected devices), cloud services and industrial internet of things (IIoT) that can support and transform its existing and upcoming infrastructure and industrial projects. The COVID-19 pandemic has opened further opportunities in healthcare and pharmaceuticals sectors through expected rise in capacity additions.

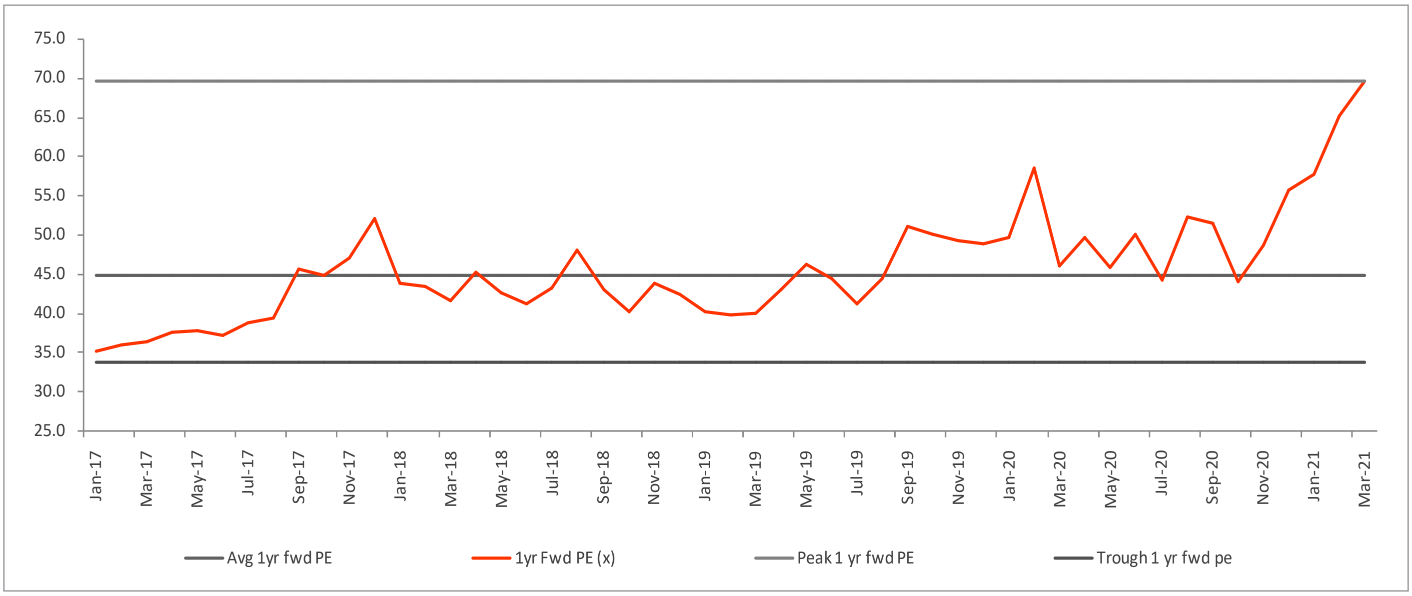
■ Company outlook - Long-term growth levers intact

The company's focus on development of products and services, foraying into new industries and addressing the growing mass mid-market is expected to maintain a healthy earnings growth trend. Further, the company is expected to benefit from domestic long term growth levers viz. smart city development, modernisation of railway stations, metro projects, airport expansions, RERA, GST, Industrial Internet of Things (IIoT) and 'Make in India" initiatives.

■ Valuation - Retain Buy with revised price target of Rs. 56,265:

The company has multiple domestic growth levers like government's infrastructure investments such as smart cities, airports, RERA, industrial internet of Things (IIoT), AatmaNirbhar Bharat initiatives which we believe would help the company maintain a healthy growth trend. An asset-light model (zero debt), strong cash position healthy operating cash flow generation, strong return ratios consistent dividend paying record justify the stock's premium valuation. Currently, the stock is trading at a P/E of 69.7x and 57.4x its FY22E and FY23 earnings. Led by AatmaNirbhar Bharat, localized procurement and a faster pick-up in manufacturing and automation activity, the entire sector is getting rerated and Honeywell remains at the forefront the leverage the opportunities, which trades at a discount to its peak 5-year average multiple. Hence, we maintain a Buy rating on the Honeywell with modestly increasing our target PE to factor overall re-rating in the space and a strong growth potential in automation across industries, robust balance sheet, and steady cash flow generation to arrive at a revised price target of Rs. 56,265.

One year forward P/E (x) band



Source: Sharekhan Research

About company

Honeywell Automation India Limited (HAIL) is a leader in providing integrated automation and software solutions, including process solutions and building solutions. It has a wide product portfolio in environmental and combustion controls, and sensing and control, and also provides engineering services in the field of automation and control to global clients. A Fortune India 500 company, HAIL has more than 3,000 employees based in nine offices across India – Pune, Baroda, Bangalore, Hyderabad, Mumbai, Chennai, Gurgaon, Kolkata, and Jamshedpur.

Investment theme

Honeywell Automation India Limited (Honeywell), a step down subsidiary of Honeywell International (a diversified technology and manufacturing company) is a leader in providing integrated automation and software solutions, including process solutions and building solutions. The company has positioned itself across various industries diversifying sector specific risk and to a greater extent shielding itself from economic downturn. The company's focus on development of new products and services, venturing into new industries apart from core industries and addressing the growing mass mid-market is expected to maintain its healthy earnings growth trend. The company's asset light model, strong cash position, strong cash flow generation, healthy return ratios, consistent dividend paying record are some of its salient features.

Key Risks

- Good percentage of revenue and profits come from Honeywell International and its affiliates
- Softening of investments domestically as well as globally, increase in crude oil prices and volatility in foreign exchange rate affects its business operations.

Additional Data

Key management personnel

Mr. Ashish Gaikwad	Executive Director-MD
Amit Kumar Tantia	Chief Financial Officer
Mr. Davies Walker	Director
Mr. Suresh Senapaty	Non-Executive - Independent Director-Chairperson

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Hail Mauritius	75.00
2	AdityaBrila Sun Life AMC	5.56
3	AdityaBrila Sun Life Trustee Co. Pvt Ltd	5.52
4	Reliance Capital Trustee Co. Pvt Ltd	4.03
5	Sundaram AMC	0.81
6	CanaraRobeco AMC /India	0.67
7	UTI Asset Management Company	0.58
8	Dimensional Fund Advisors	0.28
9	L&T Mutual Fund Trustee Ltd/India	0.26
10	Axis Asset Management Ltd	0.19

Source: Bloomberg

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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