

**March 04, 2013**

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Operating 94 branches in 52 nations, Havells India Ltd is one of the fastest developing electrical and power distribution equipment manufacturers of India. Over the past few years, the company has become a reliable household name with many reputed brands, such as Crabtree, Sylvania, Concord etc. In the Indian business scenario, we believe with investment in brand building through high media spend, ever improving product portfolio and extensive distribution network, Havells is expected to grow at a CAGR of 24% during FY12- FY14E, respectively in the domestic domain.

**Investor's Rationale**

Havells has successfully transformed itself from an industrial switchgear manufacturer towards a company that has an extensive product mix of electric consumer durables. With increased preference for branded products and robust consumption trends in India due to cumulative electrification, rising housing demand and a shift toward energy-saving lighting products, we expect Havells net earnings to garner continuous support and surpass the level of ₹5 billion mark by FY14E. Further, the electronic consumer durables and lighting segment would drive the growth ahead. Firsthand product launch in switchgear segment would also augur well for the company.

Havells got hold of Sylvania worldwide in April 2007 for the enterprise value of €227 million plus transaction costs of € 7.5 million. The underlying acquisition gives Havells access to over 10,000 distributors spread in Latin America, Europe, Africa and Asia. During Q3FY13, Sylvania has reported marginal decline in revenue by 3.7% to €109.7 million as the European revenue decline by 8%, reported PAT stood at €3 million as against profit of €1.7 million in Q3FY12, aided by decline in net debt, driven by €23.4 million proceeds received from Osram arrangement.

Over the past year, Havells has become a reliable household entity with investment in brand building and has been maintaining sync between its distribution network and the tactical goal of becoming a customer oriented company. The company operates with extensive distribution network of over 5,600 dealers and nearly 100,000 retail outlet. The distribution network has grown over fourfold over the past eight years. Further, Havells has a blueprint to mount it by adding another 700-800 dealers every year.

Havells' India's cash flow generation improved over the past periods, the company's net debt has shown continuous decline. Further, Havells is now using cash created for taking lower buyer credit. In Sylvania too, net debt has been reduced from €125.9 million in FY12 to €103.9 million during the quarter.

**Market Data**

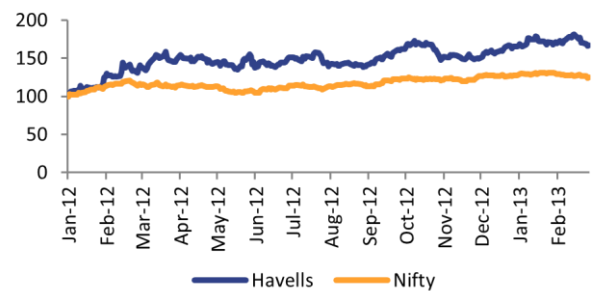
<b>Rating</b>	<b>BUY</b>
<b>CMP (₹)</b>	623.7
<b>Target (₹)</b>	<b>744.0</b>
<b>Potential Upside</b>	~19.3%
<b>Duration</b>	Long Term

52 week H/L (₹)	708.3/503.0
All time High (₹)	891.9
Decline from 52WH (%)	11.9
Rise from 52WL (%)	24.0
Beta	0.2
Mkt. Cap (₹ bn)	77.8
Enterprise Value (₹ bn)	80.0

**Fiscal Year Ended**

Y/E	FY11A	FY12A	FY13E	FY14E
Revenue (₹bn)	56.4	65.6	70.2	77.2
Net Profit(₹bn)	3.0	3.7	4.9	5.4
Share Capital	0.6	0.6	0.6	0.6
EPS (₹)	24.3	29.6	39.5	43.6
P/E (x)	25.6	21.0	15.8	14.3
P/BV (x)	11.9	8.1	5.7	4.3
EV/EBITDA (x)	14.1	11.5	9.3	8.7
ROCE (%)	31.7	34.2	33.8	29.2
ROE (%)	46.4	38.7	36.0	29.8

**One year Price Chart**



**Shareholding Pattern**

	Dec'12	Sep'12	Diff.
<b>Promoters</b>	61.6	61.6	-
<b>FII</b>	20.0	20.0	-
<b>DII</b>	1.2	1.1	0.1
<b>Others</b>	17.3	17.4	(0.1)

### Heading towards a pure consumption play

*Havells, has strategically transformed into B2C players, from largely an industrial switchgear manufacturer.*

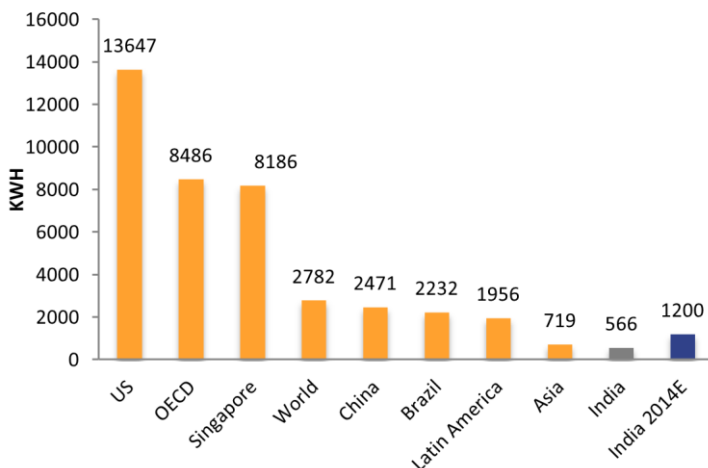
*The company is betting on the consumption story of India. Havells is well-positioned to reap rich dividend from high demand for electrical equipment's backed by accumulative electrification, rising housing demand in the country.*

Over the past decade, Havells has strategically transformed itself from an industrial switchgear manufacturer towards a company that has an extensive product portfolio of electric consumer durables. The company is playing on domestic consumption story. Havells has been successfully able to capitalize the discernible shift in the consumer's preference for higher end, technologically superior products, spurred by increasing consumer awareness towards brand. Havells, one of the prominent makers of branded electrical products, is well-positioned to reap rich dividend from high demand for electrical equipment's backed by accumulative electrification, rising housing demand in India, and a shift toward energy-saving lighting products, thereby enabling the company to maintain sustainable growth rate over stretched period of time. The company is the dominant player across various segments like switchgears, cables & wires, crabtree, fluorescent lamps, electric water heaters, lighting products & fixtures and in consumer durables like fans, mass market switchgear. Demand for these products is increasing rapidly (20%-25% growth over the past 5 years) and we expect this trend to continue going forward.

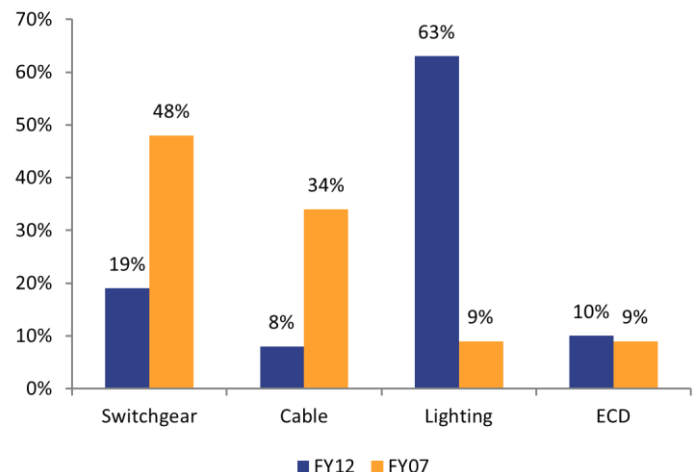
In addition, it is anticipated that domestic consumption in the country would support the company's products application. The residential sector in India is expected to grow strongly as the Indian economy is also expected to grow. The increasing urban population in the country along with improved job opportunities in the country is also expected to help the housing growth. As a result of its strong band, expanded distribution network and continuous product innovation, the company may receive direct benefits from the consumption boom in the country.

The revolution in the company took place in sync with its supply channel, which has become a vital part of the company's business. For the past few years while the company has grown its portfolio of products and has converted from an industrial goods company to a consumer durable player in India, its distribution channel has continued to be the same, as the dealers have been associated with its growth goals. The company has effectively transformed the business, as is reflected in its strong stand-alone revenue CAGR of 33% during FY04-FY12 and changing profitability mix in favour of B2C segment.

#### Per Capita Consumption of Electricity



#### Shift in EBIT contribution from each segment



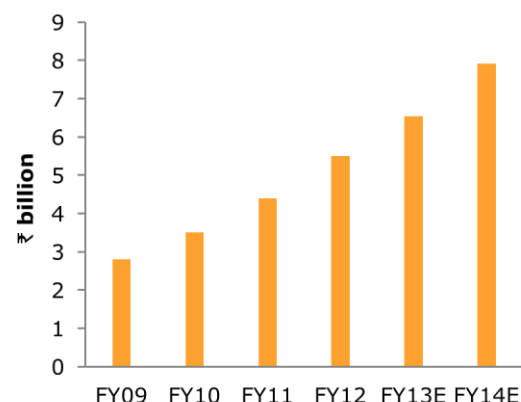
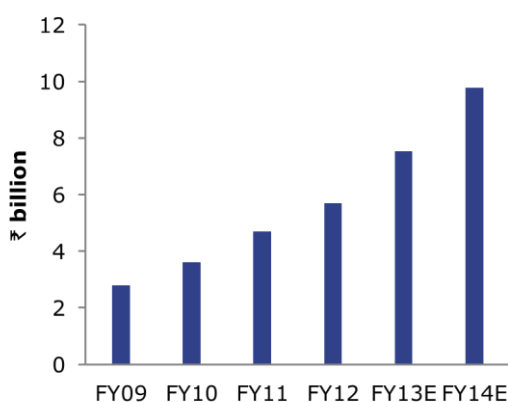
## Electric consumer durables and lighting fixture to enterprise escalation

Havells has posted a robust 51% growth in electrical consumer durable (ECD) division for quarter ended Dec 2012. The segment has picked up momentum aided by strong growth in fans by 30% and higher contribution from newly launched domestic appliances, contributed over ₹760 million to the revenue. Havells is steadily penetrating into this segment through its existing fans network, exclusive stores and the response of its products has been buoyant despite being rated at a premium to competition. The company continues to launch new products in its ECD segment, towards its extensive goal of becoming a customer oriented company. It is expected that ECD division would grow at a CAGR of 30% during FY12- FY14E.

Havells ranks 2nd in the CFL category with 11% market share behind Philips and Surya. During Q3FY13, the segment posted over 22% surge in its revenue at ₹1,770 million. The company expanded its CFL capacity to become the largest CFL manufacturer in the country. We expect Havells to aggressively pitch this segment by introducing a new array of its products range, as it brings products from the stable of Sylvania into the Indian markets. Havells has set up luminaries' plant in Neemrana, Rajasthan at an outlay of ₹1 billion, which is targeted towards reducing subcontracted products from China and superior product quality. We assume Havells to have a persistent progress in this segment with revenues accumulating at 20% CAGR over FY12-14E as industrial growth is likely to pick up.

**ECD division to grow 30% in FY12-FY14E**

**Lighting segment to grow at a CAGR of 20%**



## Reo to ensure escalation in switchgear

Havells is the largest manufacturers of MCBs, RCCBs, and distribution boards in India with the market share of around 25% in the market for MCBs. It contributed around 25% to the standalone revenues during Q3FY13. Demand for switchgears segment is expected to remain robust due to increasing demand from the construction sector and need for electricity. Further, Havells has recently launched its firsthand Reo switch for mass market, which is expected to add eventually 12-15% growth in switchgear segment. Currently, Reo has received favorable response from the interior markets and is clocking a run rate of ₹50 million per month. It expects to close FY13E with ₹250 million of revenues from Reo, while this would cross ₹1 billion by FY14E.

## Cable Division

Havells is recognized as quality manufacturers of cable & wires and offers a complete range of low and high voltage PVC and XLPE cables, besides, domestic FR/FRLS wires, Co-Axial TV and telephone cables. The Company is the second largest player in the cables & wires segment and enjoys 9% share. During the quarter, revenue growth remains muted at 5%, as the slowdown witnessed in demand for industrial cables.

*The company has increased its penetration in Electronic consumer durables; further ECD is expected to grow at a CAGR of 30% during FY12-14E, largely driven by new product launch.*

*We expect Havells lighting division to post 20% CAGR during FY12-14E.*

*Reo and Murano switch would ensure growth in switchgear segment.*

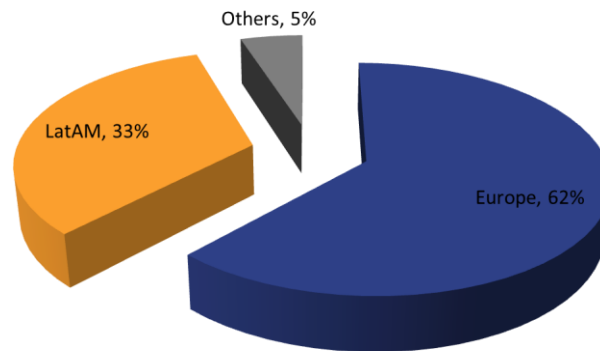
### Sylvania recovering slowly and steadily

Havells got hold of Sylvania worldwide excluding North America, Australia and New Zealand, in April 2007 for the enterprise value of €227 million plus transaction costs of € 7.5 million. The underlying acquisition gives Havells access to over 10,000 distributors spread in Latin America, Europe, Africa and Asia, which can be used to launch Havells products like switchgear, etc in these markets.

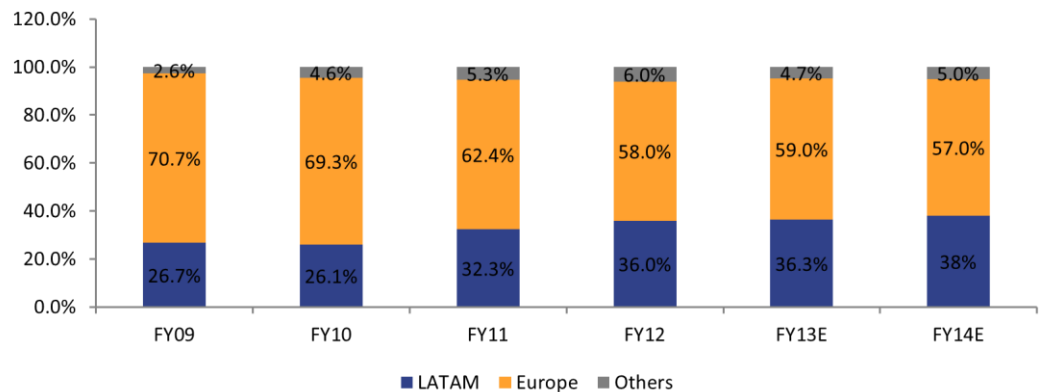
Sylvania has reported marginal decline in Q3FY13 revenue by 3.7% to €109.7 million as compared with €113.9 million a year ago, largely driven by 8% drop in net revenue from European region on overall sluggishness. However, profitability in the European region rebounded strongly, with stated EBITDA margin at 5% higher by 420bps on sequential basis, largely due to operating leverage and price increases across segments in H2FY12. Management has guided to achieve 0-2% growth in European region. However, the larger hit came from LatAM region, which posted muted growth of 3% at €36.1 million, as compared with growth of over 9% during the first half of the fiscal, largely due to poor show in Brazilian markets.

*Sylvania Q3FY13 revenue decline by 3.7% to €109.7 million, led by 8% drop reported from European region.*

**Revenue Mix**



**LatAM revenue share to grow steadily**



*We believe the high growth LatAM region would outperform and is expected post 10% CAGR during FY12-14E, while the revenue from Euro zone is expected to remain moderate.*

We believe the present euro zone crisis has resulted in a passive growth. Further, we anticipate revenues from Euro zone to stay relatively low. However, we believe a strong growth in the LatAM markets will support offsetting this subdued growth in euro zone. The European revenues are expected to grow at 1.5% CAGR, whereas LatAM region is expected to outperform the Europe with 10% CAGR expected during FY12-14E respectively.

Sylvania reported PAT of €3 million in Q3FY13 as against profit of €1.7 million in Q3FY12 and loss of €1.5 million in Q2FY13, aided by decline in net debt, driven by €23.4 million proceeds received from Osram arrangement. The profit margin was 7.5% in Q3FY13 as against 5.9% in Q3FY12. The management has guided to maintain 6-7% EBITDA margins during FY13-14E.

*Havells banks on its strong distribution network, it is expected that the company would carry on widening its distribution network by adding 700-800 dealers every year, in sync with streamlining the product portfolio.*

### Expanding its products portfolio & extensive distribution network

Havells is leveraging on its sturdy presence in the pan India network with over 5,600 dealers and nearly 100,000 retail outlet. The distribution network has grown over fourfold over the past eight years, which it carries on to enhance by mounting 700-800 dealers every year. The company has rolled out elite brand outlets under the name 'Havells Galaxy', currently the company operates with over 170 Galaxy outlets, with a blueprint to cross 200 Galaxy outlets by FY13E. Havells has direct presence in metros and major towns and rural area. The company also launched various products like coffee maker, mixer Grinder, Induction cooker, rice cooker, fans, energy saving water heaters and host of other appliances to offer customers a wide array of products to choose from. We expect a strong brand equity and extensive distribution network to help roll out its new consumer durables products going forward. The company is spending considerable amount on building the visibility for a number of its brands. Product innovation is the key mantra for the company to maintain its position and to expand its portfolio.

Segments	Market Size (₹ Million)	Market Share %	Rank
Domestic Switchgears	16,000	28	1
Modular Switches - Crabtree	14,000	15	2
Industrial Switchgears	30,000	7	5
Cable & wire	170,000	9	2
CFL	20,000	11	2
Luminaries	25,000	12	4
Fans	38,000	15	3
Domestic Appliances (New)	50,000	-	-

QRG Enterprises Ltd owning brand name/trade mark 'Havells' has entered into a revised Trademark License Agreement with Havells India, pursuant to which, the brand would be transferred to Havells India for ZERO consideration wef April 01, 2016. This existing Trademark License Agreement expires in FY16. Presently, Havells pays ₹400 million annual royalty to QRG Enterprises.

### Successfully entered into mass market by launching Reo and other products

The company has been continuously focusing on en-cashing on its high quality products, thereby cementing its leadership position in electrical consumer durables. Havells enjoy leadership position in domestic switchgears while also command sizeable market share in other segment. The company has made gradual shift in its product mix towards retail customers.

Havells has recently made its mark in mass market switches by launching its firsthand products like Reo (low priced switches), Murano (premium end switch), XPRO (premium switchgear), Endura (LED lighting) and AURA (remote control lighting). Reo will open up market of virtually ₹20,000 million for Havells, which is yet to be tapped by the prevailing range of Havells switches. The company has rated its Reo switch at a marginal premium to its competitors owing to superior quality of the product. Further, the company is aiming its new range of products towards value conscious consumers in Tier III cities and rural India, thereby mounting its penetration in hinterland India. Reo along with Murano and XPRO are expected to carry on the growth in switches. In addition, Havells has set up Luminaries manufacturing capability by spending ₹1 billion, which would help moderate subcontracting from China and also maintain the superiority of the product.

*The company has entered into mass market switches by launching its Reo low priced switches and Murano (premium switches). Further, Havells continue to launch new products to penetrate deeper into interior India.*

Havells reported 9% YoY growth in its Q3FY13 consolidated revenue at ₹18,140 million on the back of 18.0% YoY increase in domestic performance at ₹10,521 million, largely driven robust performance from consumer durables segment and Lighting segment.

## Robust Q3FY13 domestic performance supported consolidated revenue to grow by 9%

During Q3FY13, the consolidated revenue of the company surged over 9% to ₹18,140 million, primarily backed by 18% jump in domestic performance. While, the Sylvania revenue remains muted by 3.5% at ₹110 million as compared with ₹114 million a year ago. The consolidated EBITDA reported muted growth of 1% at ₹1,791 million, however, the net profit surged over 33% to ₹1,183 million, on the back of lower finance cost. Under its standalone performance, Havells Q3FY13 revenue increased to ₹10,521 million, reflecting a hike of 18% on a year-on-year basis, backed by significant contribution from all its four verticals, however, the main portion came from the lighting (30% y-o-y) and Switch gears (19% y-o-y) segments. Consumer durable segment launched recently in 2011 contributed over ₹750 million to the total revenue, higher by 51% against a year ago figures, while cables and wires segment reported muted growth of 5%. Despite of higher ad expenses the company protected its operating margins by increasing the product prices and generating a higher volume growth. This margin expansion helped Havells to show a 10% growth in its domestic EBITDA. However, the net profit growth jumped to 20%. Havells offers an impressive mix of consumer and industrial electrical products in India. With increased preference for branded products and strong consumption trends in India, we expect Havells net earnings to reach a level of ₹4.5-5 billion in the next two years.

	Q3FY13	Q3FY12	% Chg	Q2FY13	% Chg	9MFY13	9MFY12	% Change
<b>Segment Revenue</b>								
Switchgear	2697	2261	19.3%	2551	5.7%	7663	6586	16.4%
Cable & Wire	4085	3907	4.6%	3907	4.6%	12305	11163	10.2%
Lighting & Fixtures	1770	1448	22.2%	1561	13.4%	4829	4033	19.7%
Electrical Consumer Durables	2032	1346	51.0%	1623	25.2%	5757	3908	47.3%
<b>Total</b>	<b>10584</b>	<b>8962</b>	<b>18.1%</b>	<b>9642</b>	<b>9.8%</b>	<b>30554</b>	<b>25690</b>	<b>18.9%</b>
<b>Segment Revenue Mix %</b>								
Switchgear	25.5	25.2	30bps	26.5	(100bps)	25.1	25.6	(50bps)
Cable & Wire	38.6	43.6	(500bps)	40.5	(190bps)	40.3	43.5	(320bps)
Lighting & Fixtures	16.7	16.2	50bps	16.2	50bps	15.8	15.7	10bps
Electrical Consumer Durables	19.2	15	420bps	16.8	240bps	18.8	15.2	360bps
<b>EBIT</b>								
Switchgear	950	855	11.1%	847	15.9	2676	2432	10.0%
Cable & Wire	414	354	16.9%	423	10.2	1261	953	32.3%
Lighting & Fixtures	423	358	18.2%	351	11.5	1119	960	16.6%
Electrical Consumer Durables	508	378	34.4%	367	-19.2	1408	1114	26.4%
<b>Total</b>	<b>2295</b>	<b>1945</b>	<b>18.0%</b>	<b>1988</b>	<b>-19.2</b>	<b>6464</b>	<b>5459</b>	<b>18.4%</b>
<b>EBIT Margin %</b>								
Switchgear	35.2	37.8	(260bps)	33.2%	200bps	34.9	36.9	(200bps)
Cable & Wire	10.1	9.1	100bps	10.8%	(70bps)	10.3	8.5	180bps
Lighting & Fixtures	23.9	24.7	(80bps)	22.5%	140bps	23.2	23.8	(60bps)
Electrical Consumer Durables	25.0	28.1	(310bps)	22.6%	240bps	24.5	28.5	(400bps)
<b>Total</b>	<b>21.7</b>	<b>21.7</b>	<b>-</b>	<b>20.6%</b>	<b>110bps</b>	<b>21.2</b>	<b>21.2</b>	<b>-</b>

**Balance Sheet**

Y/E (₹million)	FY11A	FY12A	FY13E	FY14E
Share Capital	624	624	624	624
Reserve and surplus	5,914	8,932	13,044	17,678
<b>Net Worth</b>	<b>6,537</b>	<b>9,556</b>	<b>13,668</b>	<b>18,302</b>
Minority Interest	6	1	1	1
Loan funds	5,952	4,541	4,632	4,794
Long Term Provisions	2,709	3,020	3,050	3,111
Current liabilities	19,873	24,080	25,044	26,044
Deferred tax liabilities	559	556	556	556
<b>Capital Employed</b>	<b>35,635</b>	<b>41,754</b>	<b>46,950</b>	<b>52,807</b>
Goodwill	3,354	3,625	3,543	3,543
Fixed assets	10,204	10,946	12,041	13,365
Loans and advances	390	462	467	476
Other asset	123	120	120	121
Current assets	21,565	26,601	30,777	35,302
<b>Capital Deployed</b>	<b>35,635</b>	<b>41,754</b>	<b>46,950</b>	<b>52,807</b>

**Key Ratios**

Y/E	FY11A	FY12A	FY13E	FY14E
EBITDA Margin (%)	10.3	10.7	12.0	11.6
EBIT Margin (%)	8.9	9.2	10.5	10.1
NPM (%)	5.4	5.6	7.0	7.0
ROCE (%)	31.7	34.2	33.8	29.2
ROE (%)	46.4	38.7	36.0	29.8
EPS (₹)	24.3	29.6	39.5	43.6
P/E (x)	25.6	21.0	15.8	14.3
BVPS(₹)	52.4	76.6	109.5	146.7
P/BVPS (x)	11.9	8.1	5.7	4.3
EV/Operating Income (x)	1.5	1.2	1.1	1.0
EV/EBITDA (x)	14.1	11.5	9.3	8.7
EV/EBIT (x)	16.4	13.3	10.6	9.9

**Profit & Loss Account**

Y/E (₹million)	FY11A	FY12A	FY13E	FY14E
<b>Total Income</b>	<b>56,364</b>	<b>65,596</b>	<b>70,187</b>	<b>77,268</b>
Expenses	50,556	58,609	61,765	68,327
<b>EBITDA</b>	<b>5,807</b>	<b>6,987</b>	<b>8,422</b>	<b>8,940</b>
EBITDA margin (%)	10.3	10.7	12.0	11.6
Depreciation	804	949	1,024	1,127
<b>EBIT</b>	<b>5,003</b>	<b>6,038</b>	<b>7,398</b>	<b>7,814</b>
Interest	902	1,281	1,087	833
Exceptional Item.	(31)	0	0	0
<b>Profit Before Tax</b>	<b>4,070</b>	<b>4,757</b>	<b>6,311</b>	<b>6,981</b>
Tax	1,031	1,058	1,388	1,536
Minority Interest	4	0	0	0
<b>Net Profit</b>	<b>3,036</b>	<b>3,699</b>	<b>4,923</b>	<b>5,445</b>
NPM (%)	5.4	5.6	7.0	7.0

**Valuation and view**

Havells reported robust headline domestic performance with over 18% revenue growth during Q3FY13, led by consumer durables, lighting and switch gear business. We believe, Havells to continue to grow its domestic business by 15-20% in line with management guidance backed by new product launches; strong demand in lighting division and price hike across product verticals. Further, the company is well poised to maintain margins in the domestic market going ahead on account of steady cost management across the board and higher contribution from new product launches. On Sylvania, having turnaround the business, the company seems on track to achieve the guided EBITDA margin. Further, we still believe that the Havells ability to outpace its competitors and manage high growth has not been completely appreciated. Valuations look attractive at the current market price ₹623.70 and therefore we rate the stock as 'BUY' with a target price of ₹744. At the current market price, the stock is trading at a PE of 15.8x on FY'13E EPS of ₹39.5 and 14.3x on FY'14E EPS of ₹43.6.



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