

November 05, 2013

BSE Code: 517354

NSE Code: HAVELLS

Reuters Code: HVEL.NS

Bloomberg Code: HAVL:IN

Havells India Ltd, an electrical consumer production and power distribution equipment manufacturer, was incorporated in 1958. The company operates in four segments, namely, switchgears, cable, lighting and fixtures and electrical consumer durables with products ranging from Industrial and domestic circuit protection switchgear, cables, motors, fans, power capacitors, compact fluorescent lamp (CFL) lamps, and luminaries for domestic, commercial and industrial applications, modular switches, water heaters and domestic appliances covering the entire range of household, commercial and industrial electrical needs.

Investor's Rationale

Havells India witnessed an impressive 22% YoY rise in its standalone net revenue at ₹11.7 bn in Q2FY'14, primarily on account of growth across all of its major segments. EBITDA grew 42% YoY to ₹1.7 bn against ₹1.2 bn. Consequently, EBITDA margin surged 14.4% in Q2FY'14 from 12.4% in Q2FY'13. The growth in EBITDA margins was due to improvement in contribution margins and lower advertisement cost. Further, net profit of the company registered a robust growth of 45% YoY to ₹1.3 bn, during the quarter, backed by continuous improvement in interest cost and other income.

Havells India's cash flow has improved over the past periods, with the company generated operating cash flow at ₹7.5 bn in FY'13 as compared to ₹5.6 bn in FY'12. We expect the company's cash flow generation to remain robust in the future on the back of increasing demand in the consumer business. We expect a strong brand equity and extensive distribution network to help roll out its new consumer durable products in future.

Havells India Ltd has strategically transformed itself from an industrial switchgear manufacturer towards a company that has an extensive product portfolio of electric consumer durables. Havells is well-positioned to reap rich dividends 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 a stretched period of time. We expect the company's revenue to grow at a CAGR of ~11% over the period of FY'13-FY'15E.

With the success in fan segment, the company expanded into the home appliances segment, where it has been gaining strong traction. Following the launch of few new products in this segment including coffee maker, electric kettle, pop up toaster, sandwich maker, induction cooker and mixer grinder, Havells India targets revenue of ₹5 bn in the next two years with a growth rate between 15% to 20% annually.

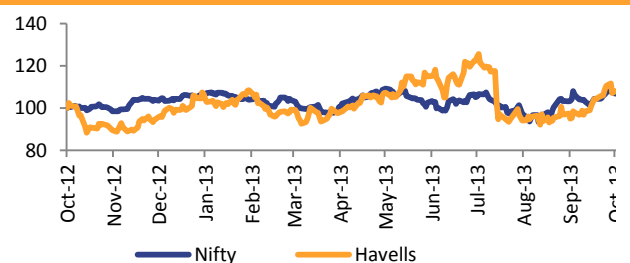
Market Data

Rating	BUY
CMP (₹)	750
Target (₹)	940
Potential Upside	~25.0%
Duration	Long Term
Face Value (₹)	5
52 week H/L (₹)	817/557
Adj. all time High (₹)	765.0
Decline from 52WH (%)	8.0
Rise from 52WL (%)	35.0
Beta	0.8
Mkt. Cap (₹bn)	93.6
Enterprise Value	97.2

Fiscal Year Ended

Y/E	FY12A	FY13A	FY14E	FY15E
Revenue (₹bn)	65.2	72.5	80.5	89.3
Net Profit (₹bn)	3.7	5.8	5.0	6.1
Share Capital (₹bn)	0.6	0.6	0.6	0.6
EPS (₹)	29.6	46.6	39.7	48.5
PE (x)	25.3	15.1	18.9	15.5
P/BV (x)	9.8	6.5	5.1	4.2
EV/EBIDTA(x)	15.2	14.5	11.8	10.0
RoCE (%)	23.4	19.5	23.2	25.2
RoE (%)	38.7	40.3	27.0	26.9

One year Price Chart



Shareholding Pattern

	Sep'13	Jun'13	Diff.
Promoters	61.7	61.6	0.1
FII	30.9	30.7	0.2
DII	0.6	1.0	(0.4)
Others	6.8	6.7	0.1

Havells India is one of the largest and India's fastest growing electrical and power distribution equipment manufacturer serving the industrial, household and commercial sectors.

In a move to expand its geographical footprints, the company plan to double the number of Galaxy stores over the next couple of years.

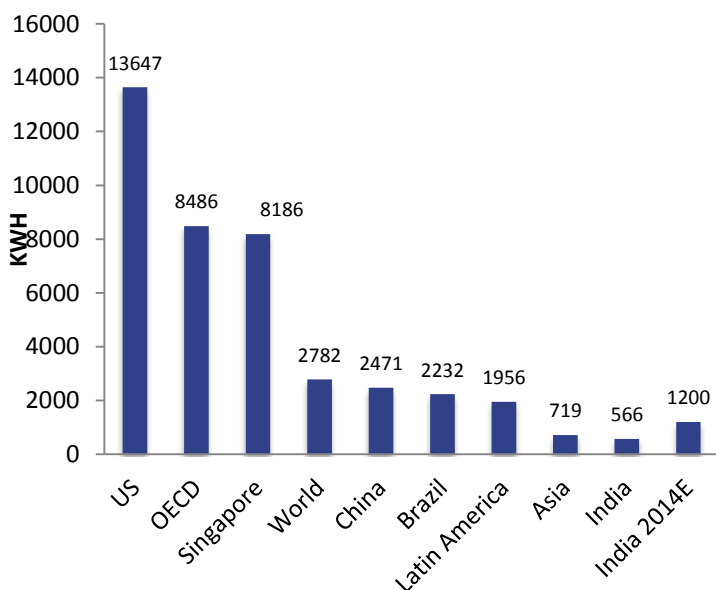
Havells India - a billion-dollar-plus electrical equipment manufacturer

Havells India Ltd, established in 1958, is an electrical and power distribution equipment manufacturer company with products ranging from industrial & domestic circuit protection switchgear, cables & wires, motors, fans, power capacitors, compact fluorescent lamps (CFL), luminaries for domestic, commercial & industrial applications, modular switches covering household, commercial and industrial electrical needs, water heater and domestic appliances. The company operates in four segments, namely, Switchgears, Cable, Lighting and fixtures and Electrical Consumer Durables and it is one of the largest and India's fastest growing electrical and power distribution equipment manufacturer serving the industrial, household and commercial sectors.

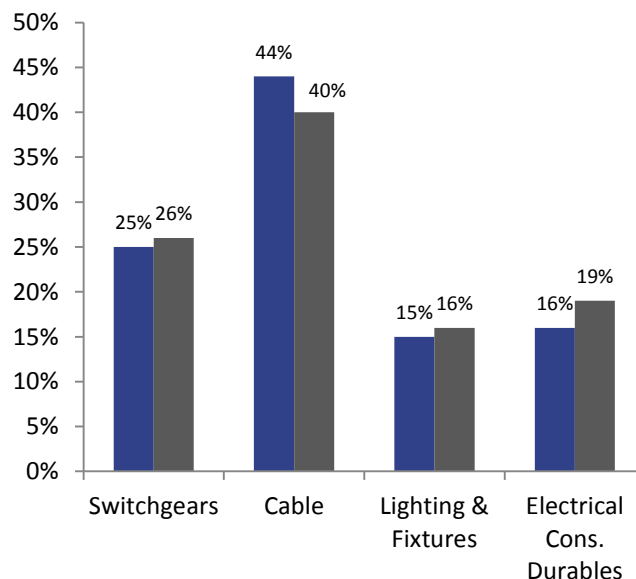
Havells enjoys a dominant market share in the overall organised switchgears market. Havells has some of the best global brands such as Crabtree, Sylvania, Concord, Luminance in its portfolio. During FY'13, Havells has marked its foray into entry level conventional piano switches 'Reo', creating a new segment of Premium Conventional Switches. Over the years, the company has transformed itself from a single product switchgear manufacturer to a full product Fast Moving Electrical Goods Company. The company has a chain of 200 Havells Galaxy stores and contributes 12% of the non-industrial cable business. Further, the company plan to double the number of Galaxy stores over the next couple of years coupled with the strengthening the brand and widening the product portfolio, besides expanding its geographic footprints. The company is having 14 manufacturing units in India spread over eight locations, and six plants abroad.

Havells, one of the prominent makers of branded electrical products, is well-positioned to reap rich dividends 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 a stretched period of time.

Per Capita Consumption of Electricity



Consumer Durables business showed strong traction

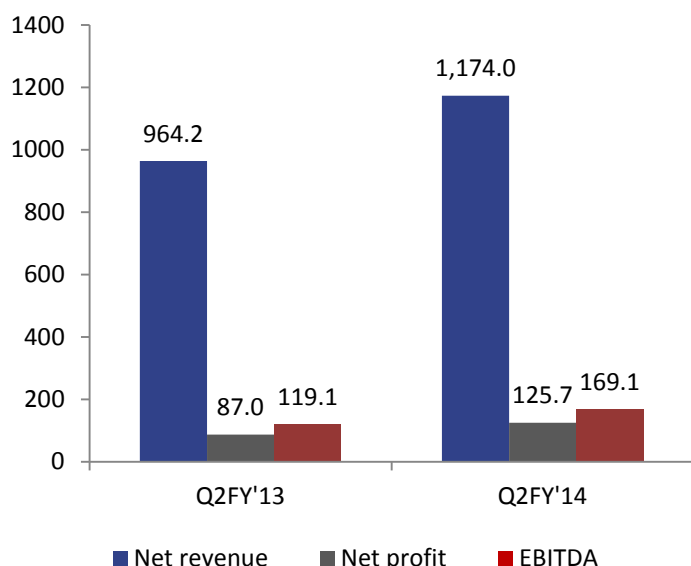


The growth in EBITDA margins was due to improvement in contribution margins and lower advertisement cost.

Witnessed robust performance in Q2FY'14

Despite ongoing economic conditions, all business segments of the electrical equipment manufacturer, Havells India have shown good growth and the company look forward to consistent growth through the year. The management said that the improved performance in the first half is mainly on account of good response from customers to company's new products. This along with lower advertisement costs has resulted in higher contribution at operating level.

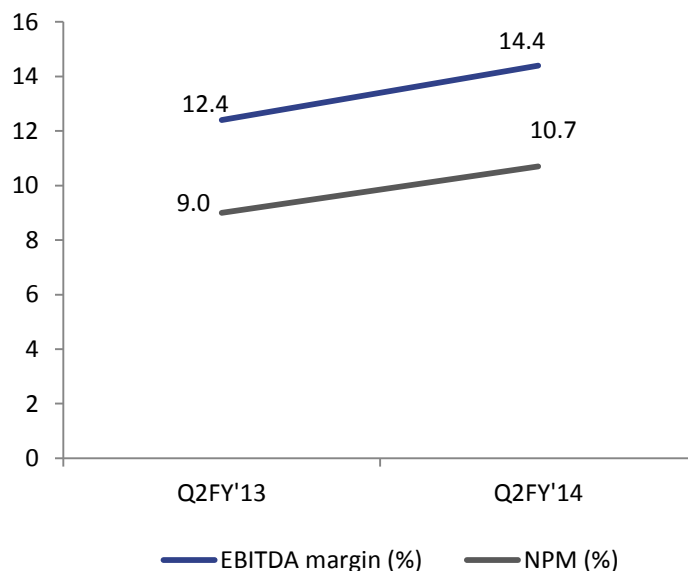
Superior performance in Q2FY'14



Havells India has shown good growth and the company look forward to consistent growth through the year.

During Q2FY'14, the company launched a range of new products in switchgear segment that received good response from the consumer.

Margin Trend (%)



The company witnessed an impressive 22% YoY rise in its standalone net revenue at ₹11.7 bn in Q2FY'14, primarily on account of growth across all of its major segments. EBITDA grow 42% YoY to ₹1.7 bn against ₹1.2 bn. Consequently, EBITDA margin surged 14.4% in Q2FY'14 from 12.4% in Q2FY'13. The growth in EBITDA margins was due to improvement in contribution margins and lower advertisement cost. Further, net profit of the company registered a robust growth of 45% YoY to ₹1.3 bn, during the quarter, backed by continuous improvement in interest cost and other income. Financial cost declined to ₹0.1 bn during the quarter, while other income advanced to ₹0.1 bn compared to ₹0.02 crore in the same period a year ago. On consolidated basis also, the performance remained healthy as the company reported 19% YoY rise in revenue at ₹20.3 bn in Q2FY'14, as against ₹17.0 bn, in the same quarter a year earlier. Pat, however, declined to ₹1.1 bn in Q2FY'14 from ₹2.4 bn, in Q2FY'13.

On segment front, the switchgear business sales showed a growth of 23% to ₹3.1 bn as against ₹2.6 bn achieved in the corresponding quarter of the previous year, of which ₹0.19 bn were contributed by the Reo switches sale. During the quarter, the company launched a range of new products that received good response from the consumer. Cables grew by 25% to ₹4.9 bn as compared to ₹3.9 bn in the same quarter last year. Electrical Consumer Durables segment showed a growth of 19% to ₹1.9 bn as compared to ₹1.6 bn in the corresponding quarter of the last year. Lighting and fixtures segment registered revenue of ₹1.8 bn as against ₹1.6 bn showing a growth of 15%.

The growth in the overall consumption and resurgence of projects in power and realty sector, will push growth in investment demand and fuel rise of industrial cables and switchgears.

Notwithstanding the challenges, the company is cautiously expanding its presence and looking beyond Europe and Latin America to newer geographies.

The company enjoys a leadership position in domestic switchgears.

Rising electrification would benefit Havells

Havells India, one of the prominent makers of branded electrical products, is well-positioned to reap rich dividend from high demand for electrical equipments on the back of increasing 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 has strategically transformed itself from an industrial switchgear manufacturer towards a company that has an extensive product portfolio of electric consumer durables. The growth in the overall consumption, the resurgence of projects, especially the power projects and the realty sector, will also push growth in investment demand and fuel rise of industrial cables and switchgears. The expected pick up in the domestic economy which is likely to push the residential sector growth coupled with growing urbanization will lead to higher demand for branded electrical products. Driven by the company's strong brand presence, expanded distribution network and continuous product innovation, the company may receive direct benefits from the consumption boom in the country. Further, the company's focus towards expanding the range of its products through new launches of products across sectors coupled with the strong brand value, provides the company the benefit of pricing power. We expect the company's revenue to grow at a CAGR of ~11% over the period of FY'13-FY'15E.

While demand headwinds in Europe and currency volatility in Latin America impacted Sylvania; expansion to newer geographies is expected to improve margins

Havells Sylvania is a leading, full-spectrum provider of quality, energy-efficient solutions for professional and architectural lighting. Brand – Sylvania has enabled Havells to have a global presence, exposure and opportunity. Sylvania is amongst the largest lighting companies in the world. The underlying acquisition of Sylvania in 2007 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, a subsidiary of company for international business has witnessed a decline in revenue in the recent past. The management of the company has stated that the operating margins in the last quarter have been impacted by demand headwinds in Europe and currency volatility in Latin America. Notwithstanding the challenges, the company is cautiously expanding its presence and looking beyond Europe and Latin America to newer geographies. The volatile currency movements in some of the emerging markets in the Latin America remain a challenge. However, in order to lessen the dependence on the Europe and Latin America region, the company is pursuing opportunities in other markets, notably ASEAN and Africa. We expect, Sylvania to face headwinds mainly in the European and Latin America regions. Meanwhile, the management of the company has guided a revenue growth of 2-3% in FY'14 (largely driven by LatAm) and EBIDTA margins at 6% in FY'14 as against 5.3% in FY'13.

Eyes significant growth from the 'Reo' range of switchgears

The Reo range of switches, introduced by the company in FY'13, offers the same high standards of quality and safety which is a hallmark of every Havells product. The company while enjoying a leadership position in domestic switchgears also enjoys sizeable market

Demand for switchgears segment is expected to remain robust due to increasing demand from the construction sector and need for electricity.

Havells India's lighting fixtures plant at Neemrana is the first large scale lighting fixtures plant of the country.

We expect Havells to have a persistent progress in the Lighting & Fixtures segment with revenues accumulating at 20% CAGR over FY'13-15E as industrial growth is likely to pick up.

share in other segment. The company has entered into the switchgear segment with the entry level conventional piano switches 'Reo' in FY'13, which marked its entry into the ₹20 bn mass switches market. Demand for switchgears segment is expected to remain robust due to increasing demand from the construction sector and need for electricity. Switchgears segment revenue grew 23% in Q2FY'14 without new product. The new product segment i.e Reo switches contributed ₹0.19 bn in Q2FY'14. With the launch of the Reo brand of conventional switches the company expects the Reo brand to be a growth driver for the company in rural India. The company is betting big on Reo switches and is eyeing to garner ₹1.5 bn revenues from the conventional switches sales in FY'14.

Strengthening Manufacturing Base

Havells India is currently having 14 manufacturing units in India and six plants abroad in six different locations and is considering optimizing the capacity and operations of each of these plants. In line with the company's strategy to enhance its manufacturing base, Havells has set up a lighting fixtures plant at Neemrana, Rajasthan in FY'13, which is the first large scale lighting fixtures plant of the country, at an outlay of ₹1 bn that is targeted towards reducing subcontracted products from China and superior product quality, giving a further edge to its manufacturing base. The company is currently in the process of enhancing the plant's capacity from the present 20 Lacs pcs per month to 40 Lacs pcs per month. The Neemrana plant also caters to the global markets with the 50% of the production is earmarked for exports through the network of Sylvania, with the balance catering to the domestic market. With the growth in the upwardly mobile segment of the population, we expect this division to gain traction in the years to come. Further, the company is also mulling to augment its switchgear capacity to double at its Baddi plant in order to cash-in the burgeoning opportunities of the increment demand of the electrical equipment. We assume Havells to have a persistent progress in the Lighting & Fixtures segment with revenues accumulating at 20% CAGR over FY'13-15E as industrial growth is likely to pick up.

Successfully gained market share in new segments

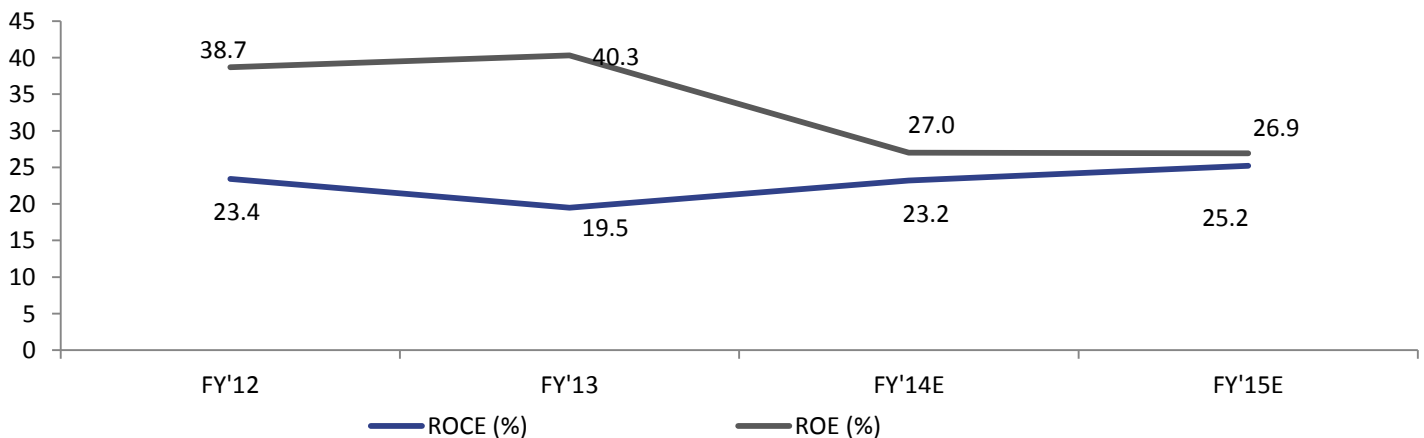
Segments	Market Size (₹ in mn)	Market share (%)	Rank
Switchgears - Domestic MCB	17,000	29%	1
Switchgears - Switches	15,000	16%	2
Cable – Domestic	65,000	14	3
Cable – Industrial	100,000	9	3
Fans	45,000	15	3
Lighting – CFL	23,000	12	2
Lighting – Luminaires	29,000	13	4
Domestic Appliances (New)	50,000	-	-

In India, the company has one of the largest distribution networks of around 7,000 distributors spread across the four regions servicing around 100,000 retailers/touch points.

Distribution network - a critical factor behind its success story

Havells, a dominant market leader in the overall organised switchgears market, is leveraging on its sturdy presence in the pan India network by increasing the number of Galaxy stores to double from 200 to 400 covering 250 towns (against earlier 130 towns) by FY'15. The company has opened 7 Havells Galaxy stores in previous quarter taking the total number to 206 stores across India and Galaxy now contributes 12% of non-cable business apart from a high quality brand visibility and direct consumer engagement. In India, the company has one of the largest distribution networks of around 7,000 distributors spread across the four regions servicing around 100,000 retailers/touch points. Further, the company is also focusing towards brand improvement with the company has spent more than ₹4 bn in advertising over the past 4 years making the company India's biggest making the company India's biggest advertiser in the electrical industry. . The impact of this investment on the consumer can be judged by the fact that Havells has emerged as the number third brand in domestic appliances in the first year of its launch, while maintaining a premium level pricing. During FY'13, the company has spent ₹1.4 bn on advertising. We expect a strong brand equity and extensive distribution network to help roll out its new consumer durables products going forward. With the company's focus towards aggressive expansion of its distribution network and brand recall, we expect Havells to gain further market share across segments.

Key Ratios



Key Concerns

- ✓ The entry of newer players in the lucrative consumer durables electrical goods segment could put pressure on the company to retain its market share.
- ✓ The sharp rise in India's current account deficit, coupled with a continued delay in the global recovery, could see more currency fluctuations. This could dent the company's profits despite the best efforts of the management in mitigating currency volatility risks.

Balance Sheet (Consolidated)

Y/E (₹mn)	FY12A	FY13A	FY14E	FY15E
Share Capital	623.9	623.9	623.9	623.9
Reserve and surplus	8,932.2	13,796.5	17,758.2	21,845.5
Net Worth	9,556.1	14,420.4	18,382.1	22,469.4
Minority Interest	0.9	0.9	0.9	0.9
Loan funds	8,685.1	8,342.0	7,187	6,019
Provisions	5,012.7	4,792.5	2,874.8	2,007.8
Current liabilities	17,689.3	16,054.2	18,462	20,862
Net Deferred Tax Liability	556.1	619.0	619.0	619.0
Other Liabilities	253.70	488.9	488.9	488.9
Capital Employed	41,753.9	44,717.9	48,015.2	52,467.7
Fixed assets	10,946.2	11,555.3	12,133.1	12,739.7
Goodwill	3,624.6	3,694.4	3,694.4	3,694.4
Loans and advances	2,143.9	2,661.6	2,981.0	3,338.7
Current assets	25,035.8	26,667.9	29,068.0	32,556.2
Deferred tax asset	-	138.7	138.7	138.7
Other Assets	3.4	-	-	-
Capital Deployed	41,753.9	44,717.9	48,015.2	52,467.7

Key Ratios (Consolidated)

Y/E	FY12A	FY13A	FY14E	FY15E
EBITDA Margin (%)	10.1	9.2	10.0	10.5
EBIT Margin (%)	8.6	7.7	8.5	8.9
NPM (%)	5.7	8.0	6.2	6.8
ROCE (%)	23.4	19.5	23.2	25.2
ROE (%)	38.7	40.3	27.0	26.9
EPS (₹)	29.6	46.6	39.7	48.5
EPS (₹)	29.6	46.6	39.7	48.5
PE (x)	25.3	15.1	18.9	15.5
P/BV (x)	9.8	6.5	5.1	4.2
EV/EBIDTA(x)	15.2	14.5	11.8	10.0
BVPS	76.6	115.6	147.3	180.1

Profit & Loss Account (Consolidated)

Y/E (₹mn)	FY12A	FY13A	FY14E	FY15E
Operating Income	65,182.0	72,478.9	80,451.6	89,301.3
Expenses	58,608.7	65,790.0	72,369.0	79,967.7
EBITDA	6,573.3	6,688.9	8,082.6	9,333.5
Depreciation	948.5	1,096.6	1,228.2	1,375.6
EBIT	5,624.8	5,592.3	6,854.4	7,957.9
Interest	1,281.0	1,232.2	862.5	603.8
Other Income	413.5	333.7	367.1	403.8
Profit Before Tax	4,757.3	4,693.8	6,358.9	7,757.9
Tax	1,058.1	823.6	1,399.0	1,706.7
Extra ordinary Income	-	1,944	-	-
Net Profit	3,699.2	5,814.3	4,960.0	6,051.2

Valuation and view

We expect Havells to continue to grow its domestic business backed by strong product portfolio and new product launches to help sustain healthy growth rates. 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. In the international business, we believe Sylvania having turnaround the business is on track to improve overall margins mainly driven by high growth from emerging markets in LatAM region coupled with a heightened focus on low market share regions. With the company's focus towards aggressive expansion of its distribution network and brand recall, we expect Havells to gain further market share across segments.

At a current market price (CMP) of ₹751.7, the stock trades at 18.9x FY14E and of 15.5x FY15E, earnings. We recommend 'BUY' with a target price of ₹940, which implies potential upside of ~25.0% to the CMP from 1 year perspective.



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