

HAVELLS INDIA

Garnering growth arsenal

India Equity Research | Consumer Durables

We recently attended Havells India's (HAVL) analyst meet. Key takeaways are: a) entrepreneurship culture has empowered management to take bolder organic/inorganic initiatives versus 10 years ago; b) aims to nurture 100 Business Leaders over 2-3 years to sustain growth; c) independent SBUs with separate P/L, marketing & business heads will not only enhance focus/rigour on each business, but will also help manage expanding operations; d) product innovation (SKU ramp up) & direct reach (2x jump in retailers) key focus areas to garner 2x growth across businesses in 4-5 years; and e) multi-pronged strategy to ensure Lloyds' profitability ramp up over the medium term. HAVL's organisational/growth framework, in our view, places it favourably to capture upcoming market opportunities and successfully tackle competition. Maintain 'BUY' with revised TP of INR640 (INR564 earlier) as we roll over to FY20 with a target multiple of 35x FY20 EPS.

Reinforcing growth framework; sharpening focus on retail channel

Management stated that the entrepreneurship culture at HAVL has led to bolder & swifter decisions in the organization, which has spurred growth. Also, it is planning to nurture 100 Business Leaders in 2-3 years to sustain the momentum. With growing importance of retailers (60% of revenue), HAVL is targeting 2x jump in their retail distribution network to 2.0 lakh over FY18-20.

Lloyd: Medium-term ramp up in profitability

HAVL aims to align Lloyd's OPMs with industry average of 9-10% over medium term, (implying 20% PAT CAGR) which it envisages to achieve via: 1) upcoming integrated consumer durables manufacturing hub at Gehlot (Neemrama); 2) reduction in seasonality of AC revenues (50% of Lloyd revenue); and 3) improved brand perception.

Outlook & valuations: Growth framework in place; maintain 'BUY'

Management's capability to handle growth as each SBU expands riding tailwinds like low penetration, rising income levels/premiumisation etc., remain key monitorables. Short/ Medium term triggers are profitability ramp up in Lloyd and pick up in currently struggling switchgear/cables business. We maintain 'BUY/SO' with a TP of INR640.

Financials

(INR mn)

Year to March	FY17	FY18E	FY19E	FY20E
Revenues	61,353	86,640	108,606	126,989
Rev. growth (%)	14.1	41.2	25.4	16.9
EBITDA	8,241	10,834	13,950	16,686
Adjusted Profit	5,969	6,966	9,233	11,274
Adjusted diluted EPS (INR)	9.6	11.2	14.8	18.1
Diluted P/E (x)	57.1	48.9	36.9	30.2
ROAE (%)	19.2	20.0	23.6	25.3

EDELWEISS 4D RATINGS

Absolute Rating	BUY
Rating Relative to Sector	Outperform
Risk Rating Relative to Sector	Low
Sector Relative to Market	Overweight

MARKET DATA (R: HVEL.BO, B: HAVL IN)

CMP	: INR 546
Target Price	: INR 640
52-week range (INR)	: 565 / 311
Share in issue (mn)	: 625.1
M cap (INR bn/USD mn)	: 342 / 5,292
Avg. Daily Vol.BSE/NSE('000)	: 1,447.1

SHARE HOLDING PATTERN (%)

	Current	Q1FY18	Q4FY17
Promoters *	61.6	61.6	61.6
MF's, FI's & BK's	3.5	3.2	2.7
FII's	25.7	26.3	26.5
Others	9.3	8.9	9.2
* Promoters pledged shares (% of share in issue)	:	NIL	

PRICE PERFORMANCE (%)

	Stock	Nifty	EW Capital Goods Index
1 month	7.4	0.0	(1.3)
3 months	8.5	3.2	2.1
12 months	54.4	24.9	32.8

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Analyst meet: Key highlights

Organizational build up:

- **HR focus** — Build organisational capabilities: HAVL was a functional organisation prior to 2016. Post which, it has set up 6 SBUs with dedicated sales teams for each business at branches with branch and business reporting, dedicated CFOs and Business Heads for each business.
- **Reinforcing capability:** Has hired 43 GM and above leaders from Schneider, Philips, Airtel, Voltas, Dover, HCL, Samsung, LG, Cargill, Dalmia Bharat, Reliance, etc.
- **Develop 100 potential business leaders over FY18-19:** 360 degree feedback on business acumen, execution excellence, strategic thinking, etc.
- **Sales:** 80% of 2,500 employees have thorough knowledge of HAVL's products.

Go-to-market-strategy:

- Exclusive sales teams for all 18 verticals, but common channel (man to market approach).
- **Omni-channel strategy:** Direct and indirect channels (retailers). 60% of sales comes from retailers who have no direct connect with the company. Under loyalty programme *SAMPARK*, 1,500 key account managers visit 60K retailers every month. Data base of 1.0 lakh retailers. Direct benefit transfer for 45k retailers, conduit for communication via mobile apps.
- **Direct channels -**
 - **Dealers and distributors:**
 - **Growth** – Focus on demand generation from indirect channel, addition of new product divisions, providing channel finance.
 - **Profit** – Providing healthy trade policies, innovative schemes (Shahensha, Gruhalakshmi and Maharaja (surprise incentive) are key schemes currently) to enhance profitability of dealers.
 - **Connect-** Dealer business visibility over mobile app & dealer portal-order booking scheme (80% order via portal) which helps generate real-time business information, updated price list, mediclaim insurance for channel partners and families. This takes care of dealers' growth and profitability with no scope for undercutting.
 - **Havells Galaxies** - Strategic brand advantage with brand shops—414 Galaxies.
 - **Channel expansion:** With the transition to rural and semi-urban cities HAVL plans to take channel number from 1,100 to 2,000 in 25k plus population towns and the retail count from 1.0 to 2.0 lakh in next 2 years.

Other highlights:

- HAVL already has 75% share in electrical sockets in a typical household with ~80% market coverage across electricals/consumer durables.
- More than 93% of sales come from in-house manufacturing, which will broadly sustain with upcoming Gehlot complex for consumer durable products.
- Lloyds is envisaged to grow faster than most businesses of HAVL over 3-5 years given significant scope for market share ramp up in key verticals.
- Management plans to sharpen focus on Tier II/III cities for most segments, except Lloyds, where the focus is more on top 25 cities where it has scope for improvement.

Table 2: Strategic plan for various SBU of Havells -

SBU	Products	Market Size (INR bn)	HAVL Mkt. Share	Growth Driver	Peers	Distribution Target	What's Changing
Switchgears							
MCB	MCB, RCCB, DB	~28	52%	<ul style="list-style-type: none"> • GST implementation to boost organised segment's growth • Real estate accelerating post demonetisation & RERA 	Legrand, Schneider	<ul style="list-style-type: none"> • Currently present mainly in trade & residential space. Plans to expand into non-residential and take the share from <10% to over 30% in next 3 years 	<ul style="list-style-type: none"> • Focus on new product categories applications – to be 10% of portfolio in next 2-3 years • Leverage the tie up with Hyundai Electric
Electrical Wiring Accessories	Switches				Anchor, Philips	<ul style="list-style-type: none"> • Geographical reach – Strengthen West and South regions with specific policies. 	<ul style="list-style-type: none"> • Multi-brand strategy • Upgrading through technology
Cables & Wires	LV, MV, HV and Solar Cables and Flexible Wires	265 (excluding industrial cables)	10%	Govt. initiatives like Affordable Housing, GST, National Telecom Policy expected to spur growth and revive sentiments	Finolex, Polycab, Havells, Anchor, RR Kabel	<ul style="list-style-type: none"> • Enhance market share in western region from 12% to 20% of total sales • Increase share of export revenue from 2% to 10% of total sales • Target South market with specific regional policies 	<ul style="list-style-type: none"> • Entry in EHV cable market • Enhance share of B2B sales • Continued thrust on network expansion • Increase capacity of Multi Core/Higher Sizes & Flat Cables
Lighting	LED and CFL Lighting and fixtures	176	5%	<ul style="list-style-type: none"> • Growing Investment in Infrastructure development like roads, Metro and commercial spaces • Govt is supporting adoption of LED lighting through policies & regulations 	Philips, Bajaj, Crompton Consumer, Syska LED	Opportunity to have direct reach in tier 2 and semi urban towns	<ul style="list-style-type: none"> • Ability to create consumer delight through innovation • Effectively communicating with consumers / TV , Radio , outdoor & activations at POP
Electric Consumer Durables							
Fans	Basic and premium fans	100	10%	<ul style="list-style-type: none"> • Rural electrification to increase one time buyers of basic fans. • Higher replacement demand in urban and tier-1 areas to increase sales of premium fans 	Crompton Consumer, Orient, Usha	<ul style="list-style-type: none"> • Currently existing in tier 1-2 areas and plans to expand to tier 3-4 cities • Also sell through alternate channels of MFR, e-comm • Institutions and projects 	<ul style="list-style-type: none"> • Targeting 20% share in 3 years, dominance in premium segment • Expand presence through regional focus, and focus on BTL marketing to create brand loyalty
Water Heaters	Electrical and Smart Water Heater	14	2-3%		V-Guard, Crompton Consumer, Racold		<ul style="list-style-type: none"> • Targeting 20% share in 3 years and to be among the top 2 players • Focus on free installation and free accessories
Small Domestic Appliances	Mixer, Grinder, Juicer, Mixer, Air Fryer, Induction Cooktop,	47	3-4%	Higher demand for premium products	Bajaj Electricals, Philips, TTK Prestige, Butterfly		<ul style="list-style-type: none"> • 10% share in 3 years, to be among the top 3 players and dominance in superior design. • Regional focus and focus on non trade channel
Lloyd Consumer Durables	AC's, Washing Machines and TV's	500	AC's - 10%, WM - 2-3% TV's - 1-2%	<ul style="list-style-type: none"> • Lower penetration across product segments • Shift towards energy-efficient ACs, rising disposable incomes 	Whirlpool, LG, Samsung, Voltas	Expand its distribution network from 10k currently to 15k with increase in reach in urban and tier 1 & 2 cities	<ul style="list-style-type: none"> • Aspiration to be USD1bn in medium term • Top quartile margins in next 4-5 years • To invest significantly in setting up manufacturing facilities • To be among top 5 players in all categories

Source: Company Presentation, Edelweiss research

Table 2: Neemrana plant contributed ~30% of HAVL's FY17 revenues

Location	State	Products Manufactured
Alwar	Rajasthan	Cables and wires along with a private Cable & Wire testing facility
Neemrana	Rajasthan	Air Coolers Motors (in collaboration with Lafert of Spain) CFL CMH Lamp Lighting Fixtures Electric Water Heater
Baddi	Himachal Pradesh	Domestic Switchgear Piano Switches
Faridabad	Haryana	Control Gear Products
Haridwar	Uttarakhand	Fans Switchgears TPW range of fans
Sahibabad, Noida	Uttar Pradesh	Changeover Switches Switchboards Capacitor Industrial Switchgear
Guwahati	Assam	Switchgear
Badli	Delhi	HBC Fuses MCBs
Tilak Nagar	Delhi	High quality Energy Meters
Noida HO	Uttar Pradesh	R&D Centre

Source: Company Annual Report, Edelweiss research

Company Description

Incorporated in 1983, HAVL is one of the largest and fastest growing manufacturers of electrical components and systems in India. It is the market leader in light-duty power distribution products. Its offerings include electrical products like circuit protection equipment (domestic and industrial switchgears), cables and wires, and consumer durables like fans, CFLs, and lighting fixtures. Havells recently acquired (Feb 2017) the Consumer segment of Lloyd electricals (which the company plans to continue) which would give HAVL access to Lloyds' strong distribution network with 10k touch points along with leadership in room AC segment (12-14% market share)

Investment Theme

We expect Havells to continue to grow its domestic business on the back of strong product portfolio. The company is currently one of the fastest growing fan brands in the Indian market with market share at ~15%. In the switchgear market, HAVL is the market leader in the low voltage segment with ~28% share. In India, the company has a network of ~7,000 distributors spread across the four regions servicing ~100,000 retailers/ touch points. HAVL has been highly successful in bolstering market share of existing products along with launching new products, which have received good response, driven by high brand visibility. Recent buyout of Lloyd brand imparts access to a high growth larger white good market adding USD2-5bn new market.

Key Risks

Slowdown in domestic business; increased competition could put pressure on margin

Slowdown in key consumer segments of construction and industrial capex could impact the domestic business.

Slowdown in power T&D could impact the demand for its cables and wires business.

Slower than expected revenue growth and profitability turnaround in Lloyd's consumer business poses risk to estimates and valuations.

Financial Statements

Key Assumptions

Year to March	FY17	FY18E	FY19E	FY20E
Macro				
GDP(Y-o-Y %)	6.6	6.5	7.1	7.1
Inflation (Avg)	4.5	4.0	4.5	4.5
Repo rate (exit rate)	6.3	5.8	5.8	5.8
USD/INR (Avg)	67.1	65.0	66.0	66.0
Company				
Cables & Wires	8.8	8.2	30.3	20.1
Switchgears	10.0	2.7	28.3	18.0
Lighting & Fixtures	10.0	42.0	10.0	10.4
Consumer durables	24.2	23.4	38.0	18.8
Depreciation	6.5	7.6	7.5	7.5
Tax rate (%)	27.5	29.0	29.0	29.0
Capex (INR mn)	2,386	2,000	2,000	1,502

Income statement

(INR mn)

Year to March	FY17	FY18E	FY19E	FY20E
Income from operations	61,353	86,640	108,606	126,989
Materials costs	36,485	53,584	67,161	79,082
Employee costs	5,004	6,580	7,910	8,461
Other mfg expenses	11,623	15,641	19,586	22,760
Total operating expenses	53,111	75,806	94,657	110,303
EBITDA	8,241	10,834	13,950	16,686
Depreciation	1,196	1,493	1,613	1,724
EBIT	7,045	9,342	12,337	14,962
Add: Other income	1,342.8	723.79	918.48	1,157.91
Less: Interest Expense	122	254	252	242
Add: Exceptional items	(578)	-	-	-
Profit Before Tax	7,688	9,811	13,004	15,878
Less: Provision for Tax	2,298	2,845	3,771	4,605
Reported Profit	5,390	6,966	9,233	11,274
Exceptional Items	(578)	-	-	-
Adjusted Profit	5,969	6,966	9,233	11,274
Shares o /s (mn)	624	624	624	624
Diluted shares o/s (mn)	624	624	624	624
Adjusted Diluted EPS	9.6	11.2	14.8	18.1
Adjusted Cash EPS	11.5	13.6	17.4	20.8
Dividend per share (DPS)	3.5	3.9	5.9	7.2
Dividend Payout Ratio(%)	43.3	42.0	48.0	48.0

Common size metrics

Year to March	FY17	FY18E	FY19E	FY20E
Operating expenses	86.6	87.5	87.2	86.9
EBITDA margins	13.4	12.5	12.8	13.1
Net Profit margins	8.8	8.0	8.5	8.9

Growth ratios (%)

Year to March	FY17	FY18E	FY19E	FY20E
Revenues	14.1	41.2	25.4	16.9
EBITDA	9.2	31.5	28.8	19.6
Adjusted Profit	17.1	16.7	32.5	22.1

Balance sheet		(INR mn)			
As on 31st March	FY17	FY18E	FY19E	FY20E	
Share capital	625	625	625	625	
Shareholders' funds	32,736	36,779	41,583	47,450	
Long term borrowings	1,981	1,981	1,981	2,034	
Total Borrowings	1,981	1,981	1,981	2,034	
Long Term Liabilities	137	137	137	137	
Sources of funds	35,990	40,033	44,838	50,758	
Gross Block	17,608	19,608	21,608	23,110	
Net Block	11,917	12,426	12,817	12,597	
Capital work in progress	119	119	119	119	
Intangible Assets	182	179	176	173	
Total Fixed Assets	12,217	12,724	13,112	12,889	
Non current investments	5,471	5,471	5,471	5,471	
Cash and Equivalents	19,375	20,680	24,170	30,471	
Inventories	9,284	11,662	14,851	17,334	
Sundry Debtors	2,285	2,374	2,976	3,479	
Loans & Advances	60	70	83	104	
Other Current Assets	906	639	639	639	
Current Assets (ex cash)	12,536	14,744	18,549	21,557	
Sundry creditors	12,508	12,485	15,363	18,530	
Provisions	1,102	1,102	1,102	1,102	
Total Current Liab	13,610	13,587	16,465	19,632	
Net Curr Assets-ex cash	(1,074)	1,158	2,085	1,926	
Net Deferred tax	1,138	1,138	1,138	1,138	
Uses of funds	35,990	40,033	44,838	50,758	
BVPS (INR)	52.5	59.0	66.7	76.1	

Free cash flow		(INR mn)			
Year to March	FY17	FY18E	FY19E	FY20E	
Reported Profit	5,390	6,966	9,233	11,274	
Add: Depreciation	1,196	1,493	1,613	1,724	
Interest (Net of Tax)	(885)	(334)	(474)	(651)	
Others	754	(136)	(193)	(266)	
Less: Changes in WC	(1,323)	2,231	927	(159)	
Operating cash flow	7,778	5,758	9,252	12,241	
Less: Capex	2,386	2,000	2,000	1,502	
Free Cash Flow	5,392	3,758	7,252	10,739	

Peer comparison valuation

Name	Market cap (USD mn)	Diluted P/E (X)		P/B (X)		ROAE (%)	
		FY18E	FY19E	FY18E	FY19E	FY18E	FY19E
Havells India	5,292	48.9	36.9	9.3	8.2	20.0	23.6
Bajaj Electricals	756	36.4	25.8	5.0	4.3	14.5	18.0
Voltas	3,227	33.9	29.3	5.5	4.8	17.3	17.5
Median	-	36.4	29.3	5.5	4.8	17.3	18.0
AVERAGE	-	39.7	30.7	6.6	5.8	17.3	19.7

Source: Edelweiss research

Cash flow metrics		FY17	FY18E	FY19E	FY20E
Year to March					
Operating cash flow		7,778	5,758	9,252	12,241
Investing cash flow		(2,275)	(1,276)	(1,082)	(344)
Financing cash flow		(724)	(3,177)	(4,680)	(5,595)
Net cash Flow		4,780	1,305	3,491	6,301
Capex		(2,386)	(2,000)	(2,000)	(1,502)
Dividend paid		(2,585)	(2,923)	(4,428)	(5,407)

Profitability and efficiency ratios

Year to March	FY17	FY18E	FY19E	FY20E
ROAE (%)	19.2	20.0	23.6	25.3
ROACE (%)	26.1	27.4	32.2	34.6
Inventory Days	86	71	72	74
Debtors Days	11	10	9	9
Payable Days	110	85	76	78
Cash Conversion Cycle	(13)	(4)	5	5
Current Ratio	2.3	2.6	2.6	2.7
Gross Debt/EBITDA	0.2	0.2	0.1	0.1
Gross Debt/Equity	0.1	0.1	-	-
Adjusted Debt/Equity	0.1	0.1	-	-

Operating ratios

Year to March	FY17	FY18E	FY19E	FY20E
Total Asset Turnover	1.8	2.3	2.6	2.7
Fixed Asset Turnover	5.2	7.1	8.6	10.0
Equity Turnover	2.0	2.5	2.8	2.9

Valuation parameters

Year to March	FY17	FY18E	FY19E	FY20E
Adj. Diluted EPS (INR)	9.6	11.2	14.8	18.1
Y-o-Y growth (%)	17.1	16.7	32.5	22.1
Adjusted Cash EPS (INR)	11.5	13.6	17.4	20.8
Diluted P/E (x)	57.1	48.9	36.9	30.2
P/B (x)	10.4	9.3	8.2	7.2
EV / Sales (x)	5.3	3.7	2.9	2.5
EV / EBITDA (x)	39.2	29.7	22.8	18.7

Additional Data

Directors Data

Rajesh Gupta	Whole-Time Director Finance and Group CFO	Puneet Bhatia	Non-Independent & Non-Executive Director
Surjit Gupta	Non-Independent & Non-Executive Director	S B Mathur	Independent Non-Executive Director
S K Tuteja	Independent Non-Executive Director	V K Chopra	Independent Non-Executive Director
AP Gandhi	Independent Non-Executive Director	Adarsh Kishore	Independent Non-Executive Director
Anil Gupta	Chairman & Managing Director	Pratima Ram	Independent Non-Executive Director
Ameet Kumar Gupta	Whole Time Director	T.V.Mohandas Pai	Non-Independent & Non-Executive Director

Auditors - S.R.Batliboi & Co. LLP

**as per last annual report*

Holding – Top10

	Perc. Holding		Perc. Holding
Qrg enterprises ltd	30.37	Qrg investments	11
Gupta vinod	6.31	Nalanda india equity	5.29
Gupta surjit	5.22	Gupta anil rai	4.9
Norges bank	2.91	Capital group compan	2.81
Government pension f	2.79	Gupta qimat rai	2.17

**in last one year*

Bulk Deals

Data	Acquired / Seller	B/S	Qty Traded	Price
29 Mar 2017	Guptajee & Company	Sell	18862400	450.00
29 Mar 2017	Arg Family Trust	Buy	18862400	450.00

**in last one year*

Insider Trades

Reporting Data	Acquired / Seller	B/S	Qty Traded
29 Mar 2017	Anil Rai Gupta as Managing Trustee of ARG Family Trust	Buy	18862400.00
29 Mar 2017	Vinod Gupta on behalf of Guptajee & Co.	Sell	13320000.00
29 Mar 2017	Anil Rai Gupta on behalf of Guptajee & Co.	Sell	5542400.00

**in last one year*

Company	Absolute reco	Relative reco	Relative risk	Company	Absolute reco	Relative reco	Relative Risk
Bajaj Electricals	HOLD	SP	M	Crompton Greaves Consumer Electrical	BUY	SO	L
Finolex Cables	BUY	SO	L	Havells India	BUY	SO	L
KEI Industries	BUY	SO	L	Symphony	BUY	SO	L
V Guard Industries	HOLD	SP	L	Voltas	BUY	SO	L
Whirlpool of India	BUY	SO	M				

ABSOLUTE RATING

Ratings	Expected absolute returns over 12 months
Buy	More than 15%
Hold	Between 15% and - 5%
Reduce	Less than -5%

RELATIVE RETURNS RATING

Ratings	Criteria
Sector Outperformer (SO)	Stock return > 1.25 x Sector return
Sector Performer (SP)	Stock return > 0.75 x Sector return
	Stock return < 1.25 x Sector return
Sector Underperformer (SU)	Stock return < 0.75 x Sector return

Sector return is market cap weighted average return for the coverage universe within the sector

RELATIVE RISK RATING

Ratings	Criteria
Low (L)	Bottom 1/3rd percentile in the sector
Medium (M)	Middle 1/3rd percentile in the sector
High (H)	Top 1/3rd percentile in the sector

Risk ratings are based on Edelweiss risk model

SECTOR RATING

Ratings	Criteria
Overweight (OW)	Sector return > 1.25 x Nifty return
Equalweight (EW)	Sector return > 0.75 x Nifty return
	Sector return < 1.25 x Nifty return
Underweight (UW)	Sector return < 0.75 x Nifty return



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Coverage group(s) of stocks by primary analyst(s): Consumer Durables

Bajaj Electricals, Crompton Greaves Consumer Electrical, Finolex Cables, Havells India, KEI Industries, Symphony, V Guard Industries, Voltas, Whirlpool of India

Recent Research

Date	Company	Title	Price (INR)	Recos
27-Nov-17	Whirlpool India	Management sets a bullish tone; <i>Company Update</i>	1,521	Buy
14-Nov-17	KEI Industries	Robust growth despite GST headwind; bright prospects; <i>Result Update</i>	329	Buy
09-Nov-17	Bajaj Electricals	RREP focus dents revenue; BS improvement positive; <i>Result Update</i>	384	Hold

Distribution of Ratings / Market Cap

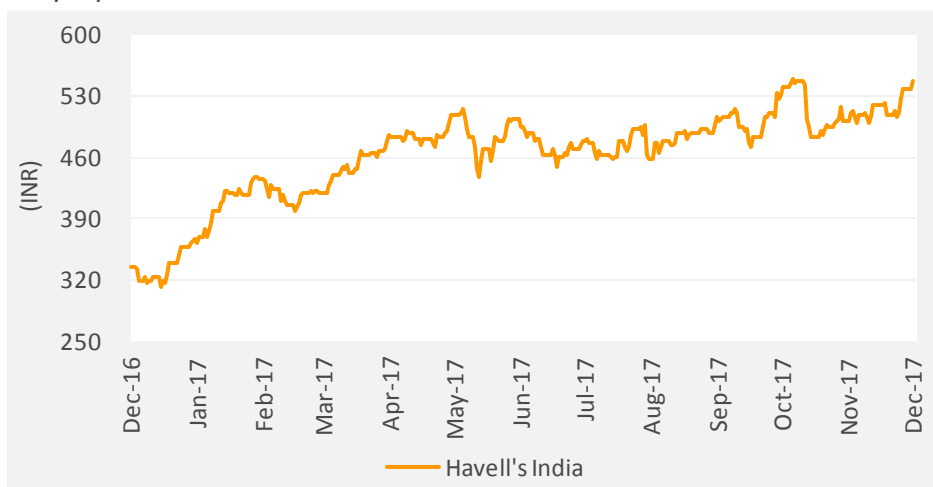
Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution*	161	67	11	240
* 1stocks under review				
	> 50bn	Between 10bn and 50 bn	< 10bn	
Market Cap (INR)	156	62	11	

Rating Interpretation

Rating	Expected to
Buy	appreciate more than 15% over a 12-month period
Hold	appreciate up to 15% over a 12-month period
Reduce	depreciate more than 5% over a 12-month period

One year price chart



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