

**HOLD**

TP: Rs 1,200 | ▲ 20%

**BLUE STAR**

| Consumer Durables

| 30 May 2022

## AC industry growth to double amid ‘golden era’

- Management expects AC market to clock 20% CAGR over five years (vs. 7-10% historically) buoyed by increased affordability and reach
- Focus on AC cost optimisation and distribution reach to boost BLSTR’s market share; targeting 15% share from the current 13%
- Projects business and exports guided to perform well. Maintain HOLD with TP of Rs 1,200 in light of margin pressures

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**AC industry to clock 20% CAGR:** BLSTR expects the next five years to be a “golden era for the AC industry”, marked by a robust 20% CAGR – well ahead of the 7-10% CAGR seen over the past two decades. Management’s forecast is predicated on two factors – continued growth from first-time AC buyers and greater inroads by players into tier-2-and-below cities. Moreover, the capacities created under the government’s PLI scheme will make ACs more affordable and, in turn, deepen the market.

**Current summer growth at 25% of previous peak:** BLSTR estimates that the AC industry is currently growing at just 20-25% of the previous summer peak season in 2019. Management indicated that BLSTR has outperformed the industry at 25-30%. For Q1FY23, it expects margins across segments to be similar to Q4.

**Cost optimisation yielding market share gains:** BLSTR has focused on design optimisation and sourcing over the last two years. This has helped the company compete at lower price ranges, which was not the case two years ago. Apart from cost, it has also focused on distribution, especially in North Indian markets. The company believes the combination of product and distribution will propel it towards its targeted market share of 15% vs. the current 13%.

**Exports a sunrise opportunity:** Western countries, especially the US and EU, are gradually embracing the idea of India being a credible alternative to their China-Plus-One strategy. Heating using reverse cycle and VRF systems is gaining acceptance as an alternate to gas-based systems. BLSTR, which has current exports of US\$ 100mn, expects sales to hit US\$ 300mn in the medium term.

**Projects unaffected by interest cycle:** Per management, the projects business is unaffected by the rate cycle/inflation and hence unlikely to face major issues in FY23.

**Maintain HOLD:** Despite BLSTR’s various growth initiatives, we believe the current inflationary climate could take a toll on margins. Our TP remains at Rs 1,200, set at 40x FY24E EPS, a 16% premium to the stock’s 5Y average. Factoring in recent stock price volatility, we retain HOLD.

### Key changes

Target	Rating
◀▶	◀▶

Ticker/Price	BLSTR IN/Rs 1,004
Market cap	US\$ 1.2bn
Free float	61%
3M ADV	US\$ 1.8mn
52wk high/low	Rs 1,225/Rs 758
Promoter/FPI/DII	39%/12%/22%

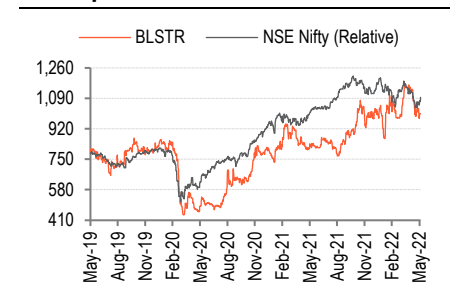
Source: NSE | Price as of 30 May 2022

### Key financials

Y/E 31 Mar	FY22P	FY23E	FY24E
Total revenue (Rs mn)	60,456	70,203	80,924
EBITDA (Rs mn)	3,465	4,362	5,027
Adj. net profit (Rs mn)	1,677	2,531	2,790
Adj. EPS (Rs)	17.4	26.3	29.0
Consensus EPS (Rs)	27.7	35.2	34.7
Adj. ROAE (%)	17.6	23.7	23.9
Adj. P/E (x)	57.6	38.2	34.6
EV/EBITDA (x)	27.9	22.2	19.6
Adj. EPS growth (%)	148.8	50.9	10.2

Source: Company, Bloomberg, BOBCAPS Research | P – Provisional

### Stock performance



Source: NSE



## Valuation methodology

BLSTR has undertaken several initiatives to increase market share, such as launching a fully revamped product portfolio consisting of mass-premium ACs at lower price points, and improving the supply chain. However, we believe the current inflationary environment would result in margin pressure which can play spoilsport for the company. We maintain HOLD and continue to value the stock at 40x FY24E EPS, a 16% premium to its five-year average, for an unchanged TP of Rs 1,200.

**Fig 1 – Key assumptions**

Parameter (Rs bn)	FY21	FY22E	FY23E	FY24E
Revenue	42.6	60.5	70.2	80.9
EBITDA	2.4	3.5	4.4	5.0
EBITDA Margin (%)	5.6	5.7	6.2	6.2
EPS (Rs)	7.0	17.4	26.3	29.0

Source: Company, BOBCAPS Research

## Key risks

Upside risks to our estimates are:

- above-expected market share gains due to recently launched mass-premium ACs, and
- above-expected growth due to a faster recovery in construction or a demand surge should prices fall.

Downside risks to our estimates are:

- demand being impacted by pricing increases due to raw material inflation and/or potential new Covid wave,
- intense competition leading to challenges in growing market share in the RAC and water cooler business, and
- delays in infrastructure rollout leading to slower growth in new orders for the EMP and HVAC businesses.

## Sector recommendation snapshot

Company	Ticker	Market Cap (US\$ bn)	Price (Rs)	Target (Rs)	Rating
Amber Enterprises	AMBER IN	1.1	2,630	3,500	HOLD
Blue Star	BLSTR IN	1.2	1,004	1,200	HOLD
Crompton Greaves	CROMPTON IN	2.8	352	621	BUY
Dixon Technologies	DIXON IN	2.9	3,804	5,431	HOLD
Havells India	HAVL IN	9.8	1,218	1,500	BUY
Orient Electric	ORIENTEL IN	0.8	275	350	HOLD
Polycab India	POLYCAB IN	4.7	2,434	3,000	BUY
V-Guard Industries	VGRD IN	1.3	235	250	HOLD
Voltas	VOLT IN	4.4	1,039	1,250	BUY
Whirlpool India	WHIRL IN	2.7	1,647	2,901	BUY

Source: BOBCAPS Research, NSE | Price as of 30 May 2022

## Financials

### Income Statement

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22P	FY23E	FY24E
<b>Total revenue</b>	<b>53,602</b>	<b>42,636</b>	<b>60,456</b>	<b>70,203</b>	<b>80,924</b>
EBITDA	2,828	2,398	3,465	4,362	5,027
Depreciation	(880)	(923)	(860)	(991)	(1,072)
EBIT	1,948	1,475	2,605	3,372	3,955
Net interest inc./(exp.)	(215)	(545)	(362)	(472)	(499)
Other inc./(exp.)	367	192	255	255	255
Exceptional items	(40)	330	0	0	0
EBT	2,090	1,478	2,509	3,166	3,722
Income taxes	(653)	(471)	(829)	(631)	(928)
Extraordinary items	0	0	0	0	0
Min. int./Inc. from assoc.	26	23	8	7	6
<b>Reported net profit</b>	<b>1,433</b>	<b>1,004</b>	<b>1,677</b>	<b>2,531</b>	<b>2,790</b>
Adjustments	40	(330)	0	0	0
<b>Adjusted net profit</b>	<b>1,473</b>	<b>674</b>	<b>1,677</b>	<b>2,531</b>	<b>2,790</b>

### Balance Sheet

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22P	FY23E	FY24E
Accounts payables	15,824	16,049	20,417	24,042	26,605
Other current liabilities	16,473	16,533	21,025	24,650	27,213
Provisions	0	0	0	0	0
Debt funds	4,489	4,516	4,778	4,778	4,778
Other liabilities	635	536	843	847	852
Equity capital	193	193	193	193	193
Reserves & surplus	7,631	8,659	9,983	10,973	12,029
Shareholders' fund	7,824	8,852	10,176	11,165	12,221
<b>Total liab. and equities</b>	<b>34,393</b>	<b>35,495</b>	<b>43,126</b>	<b>47,746</b>	<b>51,370</b>
Cash and cash eq.	2,939	6,112	2,697	3,641	3,044
Accounts receivables	8,377	8,110	11,897	12,502	14,411
Inventories	8,698	8,824	11,442	12,502	13,303
Other current assets	6,498	5,549	8,798	8,798	8,798
Investments	0	0	0	0	0
Net fixed assets	2,742	2,692	3,801	9,843	11,343
CWIP	0	0	0	0	0
Intangible assets	621	557	489	0	0
Deferred tax assets, net	818	475	276	276	276
Other assets	3,699	3,175	3,727	184	195
<b>Total assets</b>	<b>34,393</b>	<b>35,495</b>	<b>43,126</b>	<b>47,746</b>	<b>51,370</b>

### Cash Flows

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22P	FY23E	FY24E
<b>Cash flow from operations</b>	<b>5,428</b>	<b>3,600</b>	<b>1,308</b>	<b>5,483</b>	<b>3,715</b>
Capital expenditures	(860)	(635)	(2,179)	(2,000)	(1,500)
Change in investments	0	0	0	0	0
Other investing cash flows	(128)	(1,832)	1,377	(986)	(1,067)
<b>Cash flow from investing</b>	<b>(988)</b>	<b>(2,467)</b>	<b>(802)</b>	<b>(2,986)</b>	<b>(2,567)</b>
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	1,128	(21)	217	0	0
Interest expenses	(311)	(395)	(411)	0	0
Dividends paid	(2,301)	(12)	(388)	(1,541)	(1,734)
Other financing cash flows	1,299	162	294	1,541	1,734
<b>Cash flow from financing</b>	<b>(185)</b>	<b>(267)</b>	<b>(287)</b>	<b>0</b>	<b>0</b>
<b>Chg in cash &amp; cash eq.</b>	<b>2,877</b>	<b>509</b>	<b>(250)</b>	<b>944</b>	<b>(597)</b>
<b>Closing cash &amp; cash eq.</b>	<b>2,939</b>	<b>6,112</b>	<b>5,862</b>	<b>6,807</b>	<b>6,210</b>

### Per Share

Y/E 31 Mar (Rs)	FY20A	FY21A	FY22P	FY23E	FY24E
Reported EPS	14.9	10.4	17.4	26.3	29.0
Adjusted EPS	15.3	7.0	17.4	26.3	29.0
Dividend per share	10.0	4.0	10.0	16.0	18.0
Book value per share	81.2	91.9	105.7	115.9	126.9

### Valuations Ratios

Y/E 31 Mar (x)	FY20A	FY21A	FY22P	FY23E	FY24E
EV/Sales	1.9	2.3	1.6	1.4	1.2
EV/EBITDA	35.1	41.1	27.9	22.2	19.6
Adjusted P/E	65.6	143.4	57.6	38.2	34.6
P/BV	12.4	10.9	9.5	8.7	7.9

### DuPont Analysis

Y/E 31 Mar (%)	FY20A	FY21A	FY22P	FY23E	FY24E
Tax burden (Net profit/PBT)	69.1	58.7	66.8	79.9	74.9
Interest burden (PBT/EBIT)	109.4	77.8	96.3	93.9	94.1
EBIT margin (EBIT/Revenue)	3.6	3.5	4.3	4.8	4.9
Asset turnover (Rev./Avg TA)	157.9	122.0	153.8	154.5	163.3
Leverage (Avg TA/Avg Equity)	4.1	4.2	4.1	4.3	4.2
Adjusted ROAE	17.8	8.1	17.6	23.7	23.9

### Ratio Analysis

Y/E 31 Mar	FY20A	FY21A	FY22P	FY23E	FY24E
<b>YoY growth (%)</b>					
Revenue	2.4	(20.5)	41.8	16.1	15.3
EBITDA	(18.4)	(15.2)	44.5	25.9	15.2
Adjusted EPS	(21.5)	(54.2)	148.8	50.9	10.2
<b>Profitability &amp; Return ratios (%)</b>					
EBITDA margin	5.3	5.6	5.7	6.2	6.2
EBIT margin	3.6	3.5	4.3	4.8	4.9
Adjusted profit margin	2.7	1.6	2.8	3.6	3.4
Adjusted ROAE	17.8	8.1	17.6	23.7	23.9
ROCE	21.7	13.5	19.8	24.2	26.4
<b>Working capital days (days)</b>					
Receivables	57	69	72	65	65
Inventory	59	76	69	65	60
Payables	108	137	123	125	120
<b>Ratios (x)</b>					
Gross asset turnover	12.6	9.2	10.2	8.8	8.3
Current ratio	1.0	1.3	1.2	1.1	1.1
Net interest coverage ratio	9.1	2.7	7.2	7.2	7.9
Adjusted debt/equity	0.6	0.5	0.5	0.4	0.4

Source: Company, BOBCAPS Research | Note: TA = Total Assets

## Disclaimer

### Recommendation scale: Recommendations and Absolute returns (%) over 12 months

**BUY** – Expected return >+15%

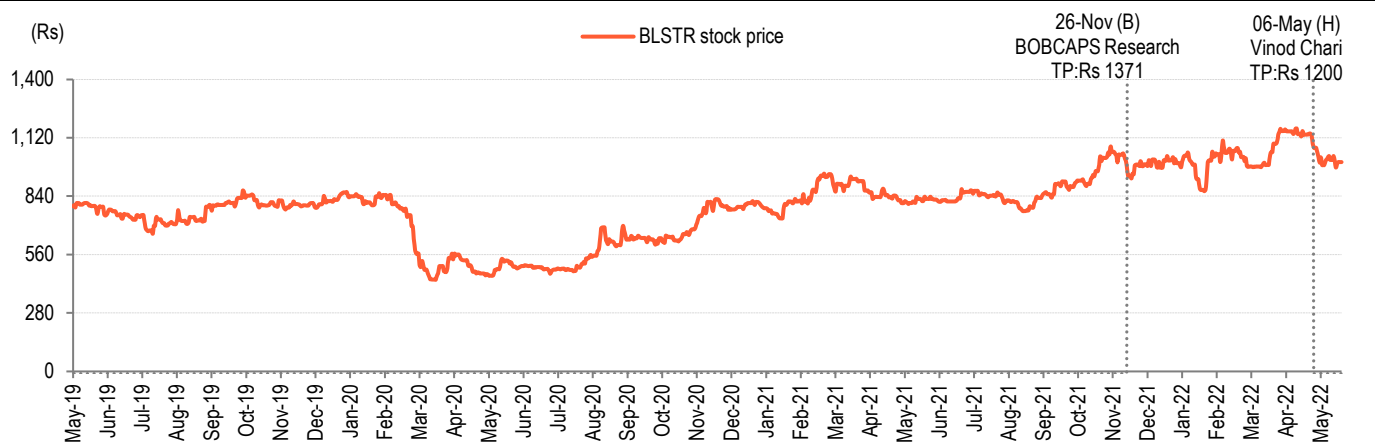
**HOLD** – Expected return from -6% to +15%

**SELL** – Expected return <-6%

**Note:** Recommendation structure changed with effect from 21 June 2021

Our recommendation scale does not factor in short-term stock price volatility related to market fluctuations. Thus, our recommendations may not always be strictly in line with the recommendation scale as shown above.

### Ratings and Target Price (3-year history): BLUE STAR (BLSTR IN)



B – Buy, H – Hold, S – Sell, A – Add, R – Reduce

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