

**BUY**

TP: Rs 1,450 | ▲ 18%

**BLUE STAR**

| Consumer Durables

| 01 February 2023

## Buoyant performance; UCP margin expansion continues

- UCP EBIT margin expands further to 7.4% (+100bps YoY) in Q3; outlook remains positive for Q4
- EMP business gathers pace as order book continues to swell (+47% YoY)
- We tweak estimates and roll forward to a revised TP of Rs 1,450 (vs. Rs 1,350), offering 18% upside – upgrade to BUY

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**Strong momentum:** BLSTR reported a good Q3FY23 with in-line revenue growth of 19% YoY to Rs 17.9bn in the wake of a solid performance across key verticals. EBIT margin in the unitary cooling product (UCP) business improved 100bps to 7.4% while electromechanical projects (EMP) saw its highest ever margin of 7.2%. Management remains optimistic on the near-term outlook and expects the upcoming summer season to be a key growth trigger. Market share guidance has been maintained at 15% by FY25.

**EMP sees robust order booking:** Traction continued in the EMP business with its best margin performance in five years and a 47% YoY rise in the carried-forward order book to Rs 4.9bn (vs. Rs 4.2bn in Q2FY23). Revenue touched the Rs 10bn mark, growing 21% YoY, primarily led by healthy order inflow. Growth momentum is expected to continue in the coming quarters led by steady order inflows from regular as well as newer verticals such as railway electrification.

**UCP margin continues to rise:** BLSTR was an outlier in Q2FY23 with UCP margin expansion amidst a tepid business environment – a trend that has continued into Q3 as margins expanded to 7.4% despite the gloomy festive demand. Management reiterated its optimistic 8-8.5% target for FY23. UCP revenue at Rs 7bn rose 15% YoY on channel restocking late in quarter and sustained traction in the commercial refrigeration business.

**Raise to BUY with TP of Rs 1,450:** BLSTR's UCP performance has been a positive departure from peers, with strong margins and an upbeat outlook for Q4FY23. In addition, the healthy EMP order book has strong tailwinds from higher infrastructure led capex and is thus expected to maintain traction near term. We increase our FY23/FY24 EPS estimates by 2%/1% given a change in depreciation methodology. On rolling valuations forward to Dec'24E, our TP moves to Rs 1,450 (from Rs 1,350), based on an unchanged 38x P/E – a 14% premium to the 3Y average on 2Y forward basis. With this, the stock offers 18% upside potential, leading us to upgrade our rating from HOLD to BUY.

## Key changes

Target	Rating
▲	▲

Ticker/Price	BLSTR IN/Rs 1,229
Market cap	US\$ 1.4bn
Free float	61%
3M ADV	US\$ 1.1mn
52wk high/low	Rs 1,288/Rs 856
Promoter/FPI/DII	39%/11%/25%

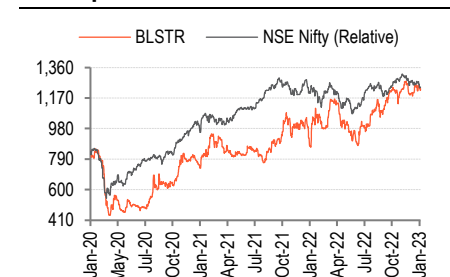
Source: NSE | Price as of 31 Jan 2023

## Key financials

Y/E 31 Mar	FY22A	FY23E	FY24E
Total revenue (Rs mn)	60,456	71,086	81,640
EBITDA (Rs mn)	3,465	4,165	4,950
Adj. net profit (Rs mn)	1,677	2,420	2,789
Adj. EPS (Rs)	17.4	25.1	29.0
Consensus EPS (Rs)	17.4	27.8	36.1
Adj. ROAE (%)	17.6	22.3	22.6
Adj. P/E (x)	70.6	48.9	42.4
EV/EBITDA (x)	34.2	28.4	23.9
Adj. EPS growth (%)	67.1	44.3	15.2

Source: Company, Bloomberg, BOBCAPS Research

## Stock performance



Source: NSE



**Fig 1 – Quarterly performance**

Particulars (Rs mn)	Q3FY23	Q3FY22	YoY (%)	Q2FY23	QoQ (%)	9MFY23	9MFY22	YoY (%)
Revenue	17,882	15,062	18.7	15,762	13.4	53,348	37,980	40.5
EBITDA	1,047	906	15.6	856	22.3	3,136	2,035	54.1
EBITDA Margin (%)	5.9	6.0	(20bps)	5.4	40bps	5.9	5.4	50bps
Depreciation	156	225	-	245	-	621	629	-
Interest	139	116	-	121	-	366	335	-
Other Income	52	137	-	86	-	242	295	-
PBT	804	703	14.3	576	39.6	2,392	1,366	75.1
Tax	216	228	-	149	-	629	453	-
Adjusted PAT	584	476	22.6	426	37.3	1,752	915	91.4
Exceptional item	-	-	-	-	-	-	-	-
Reported PAT	584	476	22.6	426	37.3	1,752	915	91.4
Adj. PAT Margin (%)	3.3	3.2	10bps	2.7	60bps	3.3	2.4	90bps
EPS (Rs)	6.1	4.9	23.5	4.4	37.6	18.3	9.5	93.1

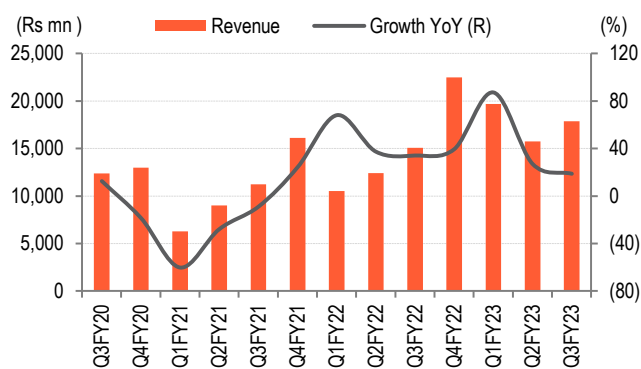
Source: Company, BOBCAPS Research

**Fig 2 – Actual vs. Estimates**

Particulars (Rs mn)	Actual	Estimate	Variance (%)
Revenue	17,882	16,850	6.1
EBITDA	1,047	1,011	3.6
EBITDA Margin (%)	5.9	6.0	(10bps)
Adj. PAT	584	567	2.9

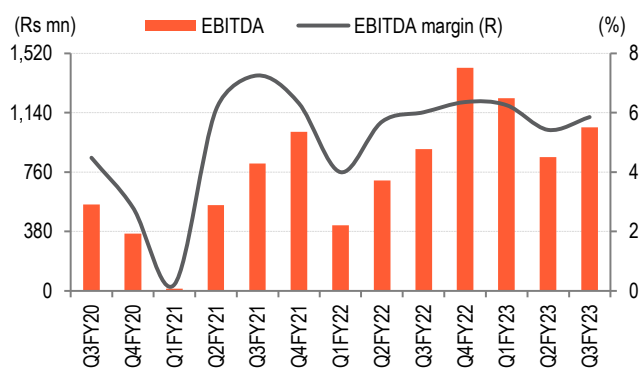
Source: Company, BOBCAPS Research

**Fig 3 – Revenue growth trend**



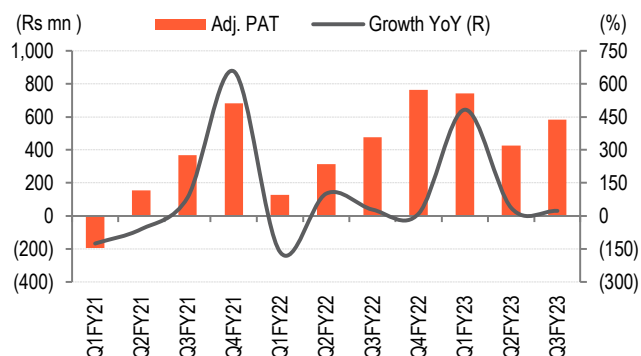
Source: Company, BOBCAPS Research

**Fig 4 – EBITDA growth trend**



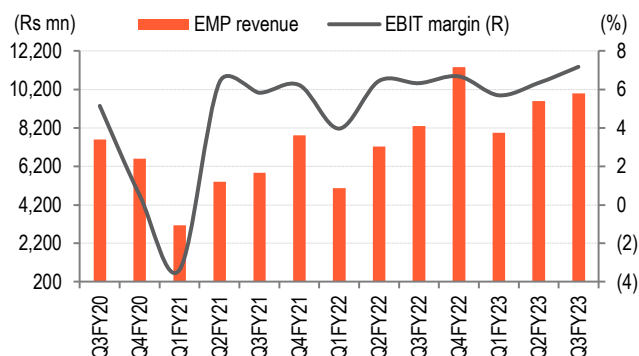
Source: Company, BOBCAPS Research

**Fig 5 – PAT growth trend**



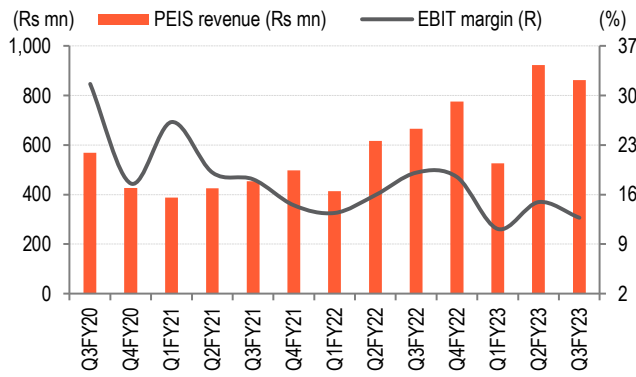
Source: Company, BOBCAPS Research

**Fig 6 – EMP vertical growth trend**



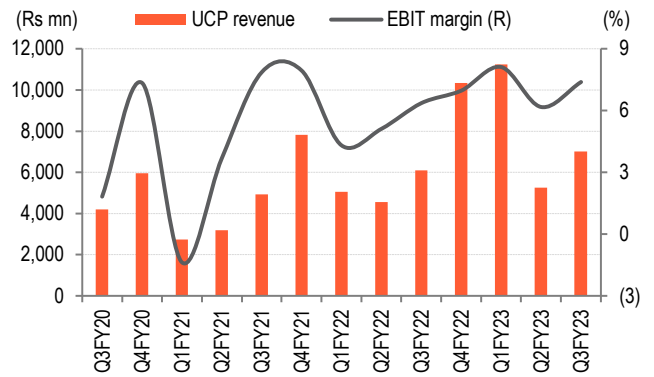
Source: Company, BOBCAPS Research

**Fig 7 – PEIS vertical growth trend**



Source: Company, BOBCAPS Research | Professional Electronics & Industrial Systems

**Fig 8 – UCP vertical growth trend**



Source: Company, BOBCAPS Research

### Earnings call highlights

- Outlook:** Management maintains its optimistic outlook for Q4FY23 and aims to sustain the growth momentum aided by channel restocking, traction in commercial refrigeration, an improving mix of affordable products, and strong order inflows. The benefits of Sri City commissioning are expected to kick in as well, which will improve operational efficiency. Management expects March to be a strong month for the room air conditioner (RAC) business given the onset of summer.
- Guidance:** BLSTR controls ~13.25% market share and expects to close FY23 at ~13.75%. The company maintains its target of 15% share by FY25 led by growing penetration in the RAC business and above-industry growth. Management has also guided for an 8-8.5% operating margin in the UCP division in FY23. The thrust on improving sales in the northern region of the country continues. Management expects the industry to grow 15% YoY in value terms in FY24.
- Depreciation:** BLSTR has switched to the ‘written down method’ from the ‘straight line method’, leading to lower depreciation in Q3 (benefit of ~Rs 0.1bn). Typically, this methodology shift is done when there is strong capacity addition – for BLSTR, additions at Sri City and Wada were the trigger.
- Sri City update:** The company has commissioned commercial production at its Sri City plant from Jan’23, in time for the upcoming summer season. It aims to garner operating cost benefits from the plant and expects working capital days to reduce. Geographical advantages will also help to lower logistics costs. The plant will offer products across three categories – affordable, affordable premium and premium. Product launches will be largely in the affordable segment (for market share protection), with some in the premium segment (to meet institutional client requirements).
- International business:** Barring Qatar and Malaysia where growth was subdued owing to country-specific headwinds, the international business has grown across verticals in Q3.

## Valuation methodology

BLSTR's UCP performance has been a positive departure from peers, with strong margins and an upbeat outlook for Q4FY23. In addition, the healthy EMP order book has strong tailwinds from infrastructure led capex and is thus expected to maintain traction near term. We increase our FY23/FY24 EPS estimates by 2%/1% given the change in depreciation methodology. On rolling valuations forward to Dec'24E, our TP moves to Rs 1,450 (from Rs 1,350), based on an unchanged 38x P/E – a 14% premium to the 3Y average on 2Y forward basis. With this, the stock offers 18% upside potential, leading us to upgrade our rating from HOLD to BUY.

**Fig 9 – Revised estimates**

(Rs mn)	New			Old			Change (%)		
	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E
Sales	71,086	81,640	94,794	69,965	80,341	93,276	1.6	1.6	1.6
EBITDA	4,165	4,950	6,659	4,074	4,995	6,687	2.2	(0.9)	(0.4)
PAT	2,420	2,789	4,018	2,369	2,772	4,081	2.2	0.6	(1.5)
EPS (Rs)	25.1	29.0	41.7	24.6	28.8	42.4	2.2	0.6	(1.5)
EBITDA Margin (%)	5.9	6.1	7.0	5.8	6.2	7.2	0bps	(20bps)	(10bps)

Source: Company, BOBCAPS Research

## Key risks

Key downside risks to our estimates are:

- Unable to achieve incremental market share while maintaining apt margins
- Slowness in EMP order book amidst recessionary environment
- Increase in competition in RAC business

## Sector recommendation snapshot

Company	Ticker	Market Cap (US\$ bn)	Price (Rs)	Target (Rs)	Rating
Amber Enterprises	AMBER IN	0.8	1,912	2,100	HOLD
Blue Star	BLSTR IN	1.4	1,229	1,450	BUY
Crompton Greaves	CROMPTON IN	2.6	331	500	BUY
Dixon Technologies	DIXON IN	1.9	2,682	4,100	BUY
Havells India	HAVL IN	9.0	1,182	1,500	BUY
KEI Industries	KEII IN	1.8	1,616	1,900	BUY
Orient Electric	ORIENTEL IN	0.7	263	290	HOLD
Polycab India	POLYCAB IN	5.3	2,921	3,300	BUY
Syrma SGS	SYRMA IN	0.5	256	390	BUY
V-Guard Industries	VGRD IN	1.3	247	250	HOLD
Voltas	VOLT IN	3.2	803	950	HOLD

Source: BOBCAPS Research, NSE | Price as of 31 Jan 2023

## Financials

### Income Statement

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23E	FY24E	FY25E
<b>Total revenue</b>	<b>42,636</b>	<b>60,456</b>	<b>71,086</b>	<b>81,640</b>	<b>94,794</b>
EBITDA	2,398	3,465	4,165	4,950	6,659
Depreciation	923	860	801	1,145	1,308
EBIT	1,475	2,605	3,364	3,805	5,352
Net interest inc./(exp.)	(647)	(464)	(479)	(494)	(479)
Other inc./(exp.)	624	357	339	407	489
Exceptional items	0	0	0	0	0
EBT	1,452	2,498	3,225	3,718	5,361
Income taxes	471	829	813	937	1,351
Extraordinary items	0	0	0	0	0
Min. int./Inc. from assoc.	26	11	11	11	11
<b>Reported net profit</b>	<b>1,004</b>	<b>1,677</b>	<b>2,420</b>	<b>2,789</b>	<b>4,018</b>
Adjustments	0	0	0	0	0
<b>Adjusted net profit</b>	<b>1,004</b>	<b>1,677</b>	<b>2,420</b>	<b>2,789</b>	<b>4,018</b>

### Balance Sheet

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23E	FY24E	FY25E
Accounts payables	16,049	20,417	11,685	13,420	15,583
Other current liabilities	5,301	8,448	9,934	11,408	13,246
Provisions	0	0	0	0	0
Debt funds	4,516	3,003	3,191	3,294	3,422
Other liabilities	223	324	376	427	491
Equity capital	193	193	193	193	193
Reserves & surplus	8,659	9,983	11,344	12,977	15,840
Shareholders' fund	8,852	10,176	11,537	13,170	16,033
<b>Total liab. and equities</b>	<b>34,941</b>	<b>42,368</b>	<b>36,722</b>	<b>41,719</b>	<b>48,774</b>
Cash and cash eq.	6,112	4,147	(10,668)	(11,811)	(13,471)
Accounts receivables	8,110	11,897	13,755	15,932	18,421
Inventories	8,824	11,442	15,191	16,449	19,678
Other current assets	5,549	7,348	8,640	9,922	11,521
Investments	0	0	0	0	0
Net fixed assets	3,836	4,328	6,027	6,882	7,575
CWIP	681	1,451	1,706	1,959	2,275
Intangible assets	0	0	0	0	0
Deferred tax assets, net	0	0	0	0	0
Other assets	1,829	1,755	2,063	2,369	2,751
<b>Total assets</b>	<b>34,941</b>	<b>42,368</b>	<b>36,714</b>	<b>41,703</b>	<b>48,750</b>

### Cash Flows

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23E	FY24E	FY25E
<b>Cash flow from operations</b>	<b>3,498</b>	<b>918</b>	<b>(10,931)</b>	<b>2,419</b>	<b>2,001</b>
Capital expenditures	174	(2,179)	(2,500)	(2,000)	(2,000)
Change in investments	(2,791)	1,340	0	0	0
Other investing cash flows	232	166	(512)	(508)	(633)
<b>Cash flow from investing</b>	<b>(2,385)</b>	<b>(673)</b>	<b>(3,012)</b>	<b>(2,508)</b>	<b>(2,633)</b>
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	2,968	654	188	103	128
Interest expenses	0	0	0	0	0
Dividends paid	(3,663)	(1,521)	(1,059)	(1,156)	(1,156)
Other financing cash flows	0	0	0	0	0
<b>Cash flow from financing</b>	<b>(696)</b>	<b>(868)</b>	<b>(872)</b>	<b>(1,053)</b>	<b>(1,028)</b>
<b>Chg in cash &amp; cash eq.</b>	<b>418</b>	<b>(623)</b>	<b>(14,815)</b>	<b>(1,143)</b>	<b>(1,660)</b>
<b>Closing cash &amp; cash eq.</b>	<b>6,112</b>	<b>4,147</b>	<b>(10,668)</b>	<b>(11,811)</b>	<b>(13,471)</b>

### Per Share

Y/E 31 Mar (Rs)	FY21A	FY22A	FY23E	FY24E	FY25E
Reported EPS	10.4	17.4	25.1	29.0	41.7
Adjusted EPS	10.4	17.4	25.1	29.0	41.7
Dividend per share	4.0	10.0	11.0	12.0	12.0
Book value per share	91.9	105.7	119.8	136.7	166.5

### Valuations Ratios

Y/E 31 Mar (x)	FY21A	FY22A	FY23E	FY24E	FY25E
EV/Sales	2.8	2.0	1.7	1.4	1.2
EV/EBITDA	49.4	34.2	28.4	23.9	17.8
Adjusted P/E	118.0	70.6	48.9	42.4	29.5
P/BV	13.4	11.6	10.3	9.0	7.4

### DuPont Analysis

Y/E 31 Mar (%)	FY21A	FY22A	FY23E	FY24E	FY25E
Tax burden (Net profit/PBT)	69.1	67.1	75.0	75.0	74.9
Interest burden (PBT/EBIT)	98.4	95.9	95.9	97.7	100.2
EBIT margin (EBIT/Revenue)	3.5	4.3	4.7	4.7	5.6
Asset turnover (Rev./Avg TA)	11.1	14.0	11.8	11.9	12.5
Leverage (Avg TA/Avg Equity)	0.5	0.5	0.6	0.6	0.5
Adjusted ROAE	12.0	17.6	22.3	22.6	27.5

### Ratio Analysis

Y/E 31 Mar	FY21A	FY22A	FY23E	FY24E	FY25E
<b>YoY growth (%)</b>					
Revenue	(20.5)	41.8	17.6	14.8	16.1
EBITDA	(15.2)	44.5	20.2	18.8	34.5
Adjusted EPS	(31.9)	67.1	44.3	15.2	44.1
<b>Profitability &amp; Return ratios (%)</b>					
EBITDA margin	5.6	5.7	5.9	6.1	7.0
EBIT margin	3.5	4.3	4.7	4.7	5.6
Adjusted profit margin	2.4	2.8	3.4	3.4	4.2
Adjusted ROAE	12.0	17.6	22.3	22.6	27.5
ROCE	11.2	14.9	19.9	20.2	24.3
<b>Working capital days (days)</b>					
Receivables	69	72	71	71	71
Inventory	76	69	78	74	76
Payables	137	123	60	60	60
<b>Ratios (x)</b>					
Gross asset turnover	5.8	7.6	7.2	6.8	6.7
Current ratio	1.3	1.2	1.2	1.2	1.2
Net interest coverage ratio	2.3	5.6	7.0	7.7	11.2
Adjusted debt/equity	0.5	0.3	0.3	0.3	0.2

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

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

**BUY** – Expected return >+15%

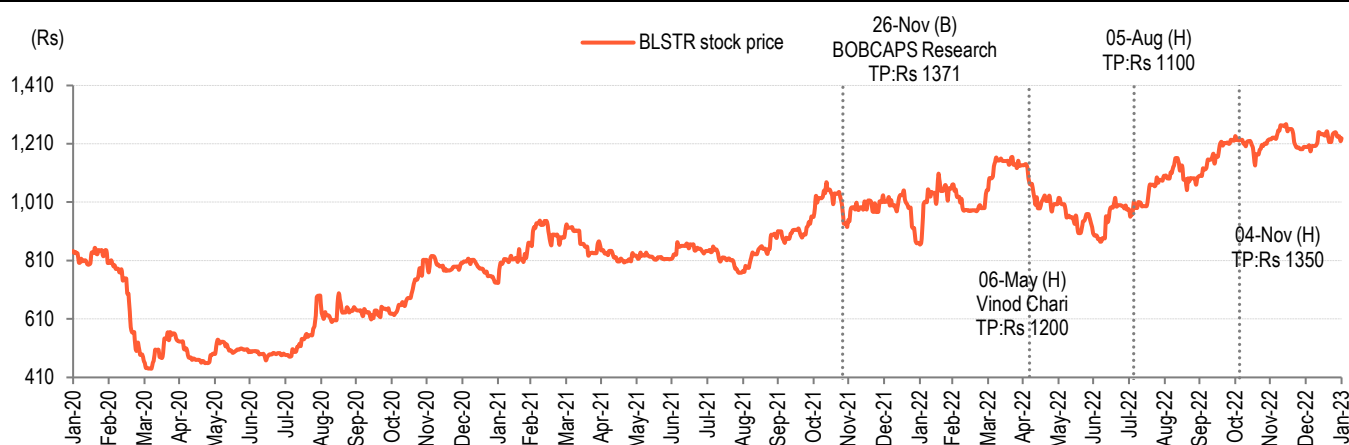
**HOLD** – Expected return from -6% to +15%

**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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