

Walking a tight rope with margins

- Price hikes deferred beyond Q2 to maintain market share/topline; commodity deflation partly negated by adverse currency
- Sales impacted ahead of new energy norms, particularly in fans and partly in ACs; soft margin outlook for H2
- Our top picks remain HAVL, CROMPTON, DIXON and POLYCAB

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Price hikes delayed: The consumer durables industry deferred price hikes to Q3FY23 amid the ongoing transition phase to new energy norms (for room ACs, fridge and fans) and rupee depreciation. Raw material deflation helped cut costs but was partially offset by unfavourable currency movement. While the industry largely managed to meet consensus topline estimates for Q2FY23, it underperformed on margins owing to inflationary pressures in the economy.

BEE transition hurting sales of ECD: The impact of Bureau of Energy Efficiency (BEE) energy norms was visible across electronic durable categories, particularly fans, sparking channel destocking in Q2FY23. Commentaries across players point to a slump in fans and a dull outlook for Q3, followed by improvement in Q4 as the BEE transition draws near an end. Premium players see an opportunity to grab market share from low-to-mid segment players aided by better, diversified portfolios.

AC margins falter as competition intensifies: During the seasonally weak second quarter, demand was tepid and margins contracted YoY across the board (except for BLSTR). Management commentaries reflect a gloomy margin outlook for H2FY23. A&P expenses increased and returned to normal after a Covid-led hiatus, while inventories swelled more than usual. Competition intensified as players put market share gains ahead of profitability. For AMBER, the key challenge is insourcing plans by manufacturers (OEMs) looking to avail of production-linked benefits.

EMS a mixed bag: Electronic manufacturing services (EMS) players are working to strengthen original design manufacturing (ODM) to gain end-to-end capabilities, drive client engagement and thus boost margins. Leading EMS companies under our coverage had a mixed performance in Q2. DIXON is confident of a guidance beat in FY23 led by a better September-ending quarter and deal wins, even as AMBER's sustained capex drive eases the uncertainty stoked by OEM insourcing.

Retain top picks: We have maintained our ratings for coverage stocks in Q2 while adjusting target prices to bake in the results. Our top picks remain HAVL (TP Rs 1,500), CROMPTON (TP Rs 500, BUY), DIXON (TP Rs 5,200), and POLYCAB (TP Rs 3,300).

Recommendation snapshot

Ticker	Price	Target	Rating
AMBER IN	2,019	2,100	HOLD
BLSTR IN	1,202	1,350	HOLD
CROMPTON IN	357	500	BUY
DIXON IN	4,540	5,200	BUY
HAVL IN	1,203	1,500	BUY
ORIENTEL IN	261	280	HOLD
POLYCAB IN	2,687	3,300	BUY
VGRD IN	262	250	HOLD
VOLT IN	837	1,000	HOLD

Price & Target in Rupees | Price as of 9 Nov 2022

Consumer durables: Q2 result reviews

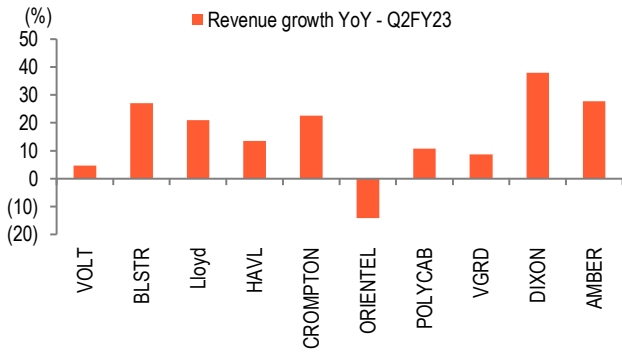
Company	Result review link
AMBER IN	Structural growth overhang persists
BLSTR IN	Best Q2 performer among AC pack
CROMPTON IN	Q2 a minor blip; expect swift recovery
DIXON IN	Buoyant numbers, bright prospects
HAVL IN	Margins hit trough; expect recovery in H2
ORIENTEL IN	One-offs mar performance
POLYCAB IN	Beat on all fronts
VGRD IN	Margin pressure dampens performance
VOLT IN	Dismal Q2; UCP margins at decadal low

Source: BOBCAPS Research



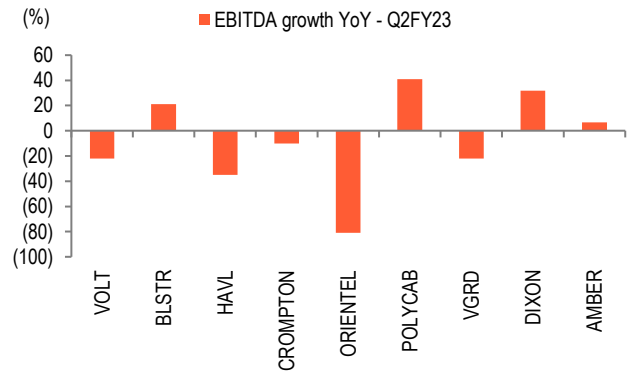
Quarterly trends

Fig 1 – Revenue growth intact for RAC and EMS players



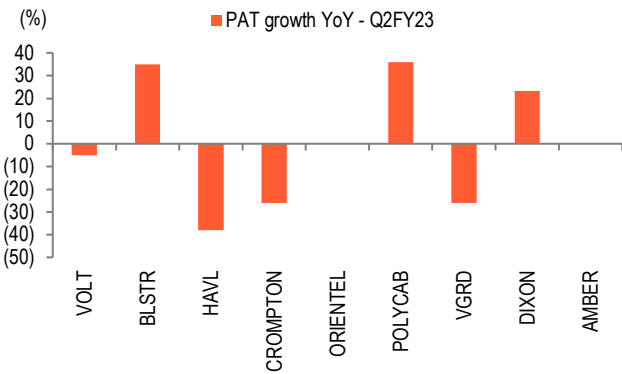
Source: Company, BOBCAPS Research | RAC: Room Air Conditioners, EMS: Electronic Manufacturing Services

Fig 2 – EBITDA growth has largely declined in Q2FY23



Source: Company, BOBCAPS Research

Fig 3 – PAT growth has slowed as well



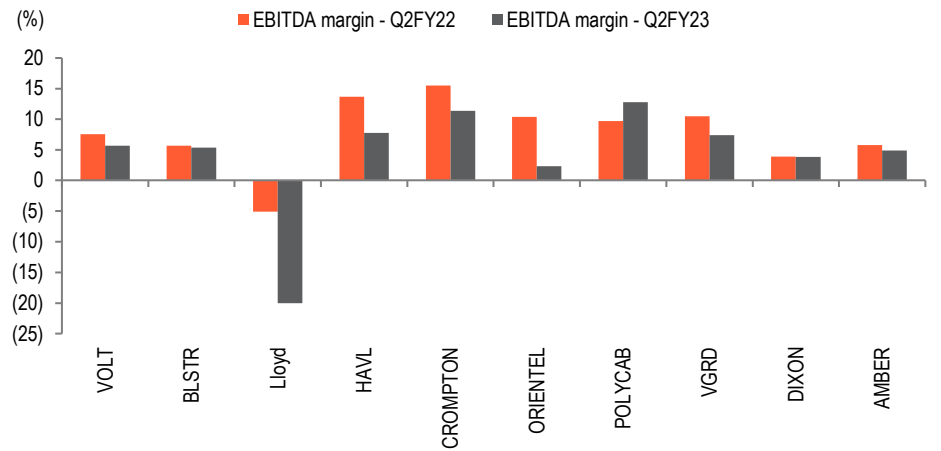
Source: Company, BOBCAPS Research | Note: AMBR, ORIENTEL posted losses and are thus not comparable

Fig 4 – Gross margins moderated despite raw material deflation



Source: Company, BOBCAPS Research

Fig 5 – EBITDA margins contracted across the board



Source: Company, BOBCAPS Research

Q2FY23: Company-wise snapshot

- **VOLT:** VOLT posted a weak September quarter performance as its electromechanical product (EMP) business was tepid and unitary cooling product (UCP) margins came in at a 10-year low of 7.3%, with a weak UCP margin outlook for another 4-5 quarters. The company's exit market share also dropped to 23% from 24% in Jun'22.
- **BLSTR:** BLSTR posted the best performance amongst room AC (RAC) players as its UCP margin expanded YoY (unlike peers). Traction also continued in the EMP business. Management commentary remains buoyant, contrasting with the gloomy outlook for peers.
- **HAVL:** Operating margin deteriorated owing to increased losses at Lloyd and a weak showing in both the electronic consumer durables (ECD) and cables businesses. The absorption of high-cost inventory weighed on margins, with recovery likely in H2FY23.
- **CROMPTON:** Revenue was in line with estimates, but margins fell short. The revenue run-rate for subsidiary Butterfly Gandhimathi Appliances (BGAL) appears to be back on track, accompanied by double-digit margins. The fans segment slowed, though management estimates a relatively better H2 for the business.
- **ORIENTEL:** Q2 saw a net loss amidst one-offs (streamlining of distribution in new states and transition to new energy norms in fans). Weakness in the fans business is expected to persist in H2, offering a meagre outlook.
- **POLYCAB:** Q2 was a beat on all fronts led by a strong performance in wires & cables and better exports. The fast-moving electrical goods (FMEG) segment lagged on transition to new BEE norms in fans and a distribution rejig. The outlook remains positive, in line with the company's long-term guidance of Rs 200bn by FY26.
- **VGRD:** Utilisation of high-cost inventory weighed on Q2 margins, but management expects a recovery by Q4FY23. The company's strategy of expanding beyond the traditional southern market is paying off.
- **DIXON:** Q2 was strong with revenue and margins ahead of expectations. The topline was boosted by broad-based growth across verticals, while a better performance by ODM verticals aided margins. Management remains upbeat on meeting its FY23 revenue guidance of Rs 150bn, reflecting a better H2.
- **AMBER:** A seasonally lean period and higher interest expenses drove a net loss in Q2. AMBER's capex is well on track which partly assuages the uncertainty arising from insourcing by OEMs. Management continues to expect record growth in the RAC industry, but the advent of capex by OEMs compels a cautious outlook on the company.

Fig 6 – UCP segment: Peer comparison

Company	EBIT margin Q2FY23 (%)	Revenue Q2FY23		
		3Y CAGR (%)	Growth YoY (%)	Growth QoQ (%)
BLSTR	6.2	12	15	(53)
VOLT	7.3	26	4	(52)
Lloyd	(20.0)	33	21	(62)

Source: Company, BOBCAPS Research

Fig 7 – ECD segment: Peer comparison

Company	EBIT margin Q2FY23 (%)	Revenue Q2FY23		
		3Y CAGR (%)	Growth YoY (%)	Growth QoQ (%)
HAVL	11.6	12	6	(8)
CROMPTON	17.1	10	(3)	(21)
ORIENTEL	4.4	3	(26)	(30)
VGRD	2.9	24	21	13

Source: Company, BOBCAPS Research

Fig 8 – Lighting segment: Peer comparison

Company	EBIT margin Q2FY23 (%)	Revenue Q2FY23		
		3Y CAGR (%)	Growth YoY (%)	Growth QoQ (%)
HAVL	14.3	12	12	8
CROMPTON	8.0	(2)	(7)	3
ORIENTEL	11.3	10	15	14
VGRD	5.4	15	1	1

Source: Company, BOBCAPS Research

Fig 9 – Wires & Cables segment: Peer comparison

Company	EBIT margin Q2FY23 (%)	Revenue Q2FY23		
		3Y CAGR (%)	Growth YoY (%)	Growth QoQ (%)
HAVL	6.3	18	19	14
POLYCAB	11.7	15	12	23
VGRD	5.4	15	1	1

Source: Company, BOBCAPS Research

Fig 10 – Valuation snapshot

Tickers	Revenue (Rs bn)				EBITDA (Rs bn)				EBITDA Margin (%)		
	FY23E	FY24E	FY25E	CAGR (%)	FY23E	FY24E	FY25E	CAGR (%)	FY23E	FY24E	FY25E
VOLT	89	108	127	17	6.6	9.1	11.6	19	7.4	8.5	9.1
BLSTR	70	80	93	16	4.1	5.0	6.7	25	5.8	6.2	7.2
POLYCAB	148	167	184	15	17.1	20.0	22.4	21	11.6	12.0	12.2
CROMPTON	76	87	101	23	9.9	12.3	14.6	24	13.0	14.1	14.5
HAVL	159	179	206	14	19.3	23.8	28.2	17	12.2	13.3	13.7
ORIENTEL	27	32	36	14	2.1	2.8	3.4	14	7.7	8.8	9.5
VGRD	40	44	50	13	4.0	4.6	5.2	15	10.0	10.4	10.3
DIXON	171	221	263	35	6.6	8.8	10.6	41	3.9	4.0	4.0
AMBER	58	74	87	28	4.0	5.2	6.2	31	7.0	7.1	7.1

Tickers	PAT (Rs bn)				EPS (Rs)				ROE (%)			P/E (x)		
	FY23E	FY24E	FY25E	CAGR (%)	FY23E	FY24E	FY25E	CAGR (%)	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E
VOLT	4.6	6.4	8.1	17	14.1	19.4	24.4	17	8.3	10.9	12.7	60	43	34
BLSTR	2.4	2.8	4.1	35	24.6	28.8	42.4	35	21.9	22.6	28.0	49	42	28
POLYCAB	11.5	13.5	15.1	22	76.9	90.2	101.0	22	19.1	19.0	18.2	35	30	27
CROMPTON	6.5	8.6	10.4	21	10.3	13.6	16.3	21	24.1	26.1	25.4	35	26	22
HAVL	13.3	16.4	19.2	17	21.2	26.2	30.6	17	21.4	21.4	21.4	57	46	39
ORIENTEL	1.1	1.5	1.9	15	5.0	7.1	9.0	15	18.6	23.3	25.6	52	37	29
VGRD	2.6	3.0	3.3	13	6.0	6.9	7.6	13	17.2	17.3	16.7	44	38	34
DIXON	3.6	5.0	6.2	48	60.0	85.1	103.9	48	22.0	30.4	31.8	76	53	44
AMBER	1.7	2.2	2.9	38	51.6	65.4	87.5	38	9.6	11.1	13.4	39	31	23

Source: Company, BOBCAPS Research

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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

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