

**BUY**

TP: Rs 1,500 | ▲ 24%

**HAVELLS INDIA**

| Consumer Durables

| 20 October 2022

## Margins hit trough; expect recovery in H2

- Muted margins in Q2 owing to poor profitability in both ECD and cables along with wider losses at Lloyd
- Expect margin recovery in H2 given full absorption of high-cost inventory and easing of commodity prices
- FY23/FY24 EPS cut 9%/6%; on rollover, our TP remains unchanged at Rs 1,500 – retain BUY

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**Margins drag down Q2:** HAVL's Q2FY23 revenue grew 14% YoY to Rs 36.8bn (3Y CAGR: 18%), with volumes contributing ~80% of the growth. However, EBITDA margin deteriorated 600bps YoY to 7.8% (3Y avg: 12.2%) due to larger losses at Lloyd and poor margins in the electronic consumer durables (ECD) and cables & wires (C&W) segments.

**Lloyd's losses widen but market share rises:** Management reiterated its strategy of chasing market share and has seen visible results, in that Lloyd now commands 12-13% share in the air conditioner segment. However, this strategy caused the subsidiary's EBITDA losses to rise to Rs 840mn in Q2 vs. Rs 563mn in Q1FY23. The company expects to hike prices from Q4FY23 in response to scheduled changes in energy efficiency norms. Management is guiding for lower losses at Lloyd in coming quarters and expects double-digit contribution margins by Q4.

**ECD to improve in H2:** The ECD business, which witnessed strong traction over the past year, remained muted in Q2 (+6% YoY vs. 3Y CAGR of 12%) on account of lower volumes in fans. Sluggish B2C demand and channel destocking curtailed sales. We expect the slowdown to continue in Q3, but a relatively favourable season for water heaters should compensate for the pullback.

**Margins bottoming out:** The full absorption of high-cost inventory in Q2 amidst softer raw material prices and lower realisations weighed on margins, with C&W reporting a muted EBIT margin of 6.3%. Extended EBITDA losses at Lloyd was a further dampener. We expect easing commodity costs along with a winding down of high inventory to enable EBITDA margins to return to normal.

**Growth and margin pullback transient; maintain BUY:** We believe the margin deterioration and subdued growth in key verticals is transient in nature and will normalise in H2FY23. Additionally, HAVL's balance sheet (Rs 2.1bn in cash equivalents) is robust. We remain positive on the company's branding, wide presence, superior execution and inherent growth story. Factoring in the Q2 print, we trim our FY23/FY24 EPS estimates by 9%/ 6%. On rolling valuations forward to Sep'24E, our TP stays at Rs 1,500 based on an unchanged 53x P/E (10% premium to 5Y avg). BUY.

### Key changes

Target	Rating
◀ ▶	◀ ▶

Ticker/Price	HAVL IN/Rs 1,210
Market cap	US\$ 9.2bn
Free float	41%
3M ADV	US\$ 12.3mn
52wk high/low	Rs 1,429/Rs 1,037
Promoter/FPI/DII	60%/23%/9%

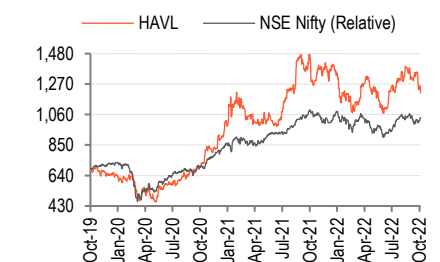
Source: NSE | Price as of 20 Oct 2022

### Key financials

Y/E 31 Mar	FY22A	FY23E	FY24E
Total revenue (Rs mn)	1,39,385	1,58,658	1,78,918
EBITDA (Rs mn)	17,604	19,292	23,817
Adj. net profit (Rs mn)	11,965	13,277	16,403
Adj. EPS (Rs)	19.1	21.2	26.2
Consensus EPS (Rs)	19.1	23.1	27.7
Adj. ROAE (%)	21.4	20.7	22.2
Adj. P/E (x)	63.3	57.1	46.2
EV/EBITDA (x)	43.1	39.3	31.8
Adj. EPS growth (%)	14.6	11.0	23.5

Source: Company, Bloomberg, BOBCAPS Research

### Stock performance

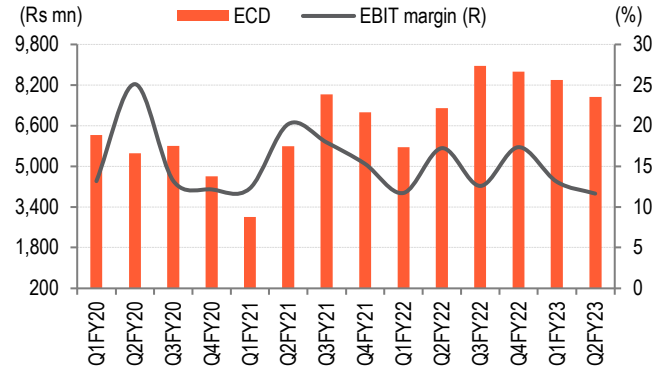


Source: NSE



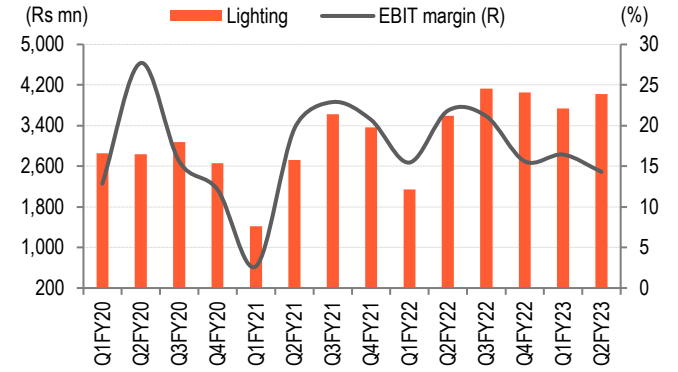
Quarterly trends

**Fig 1 – ECD margin under pressure due to channel destocking in fans segment**



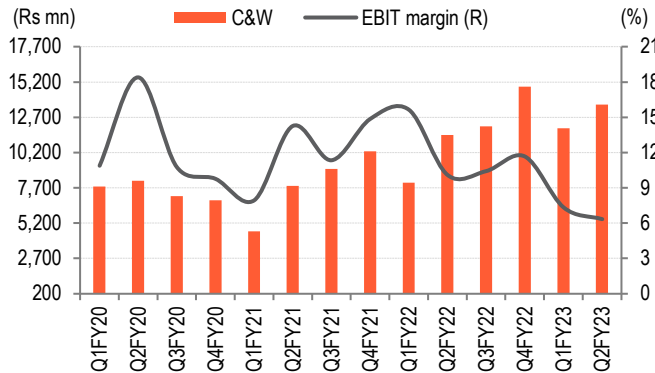
Source: Company, BOBCAPS Research

**Fig 2 – Lighting business impacted due to factory accident**



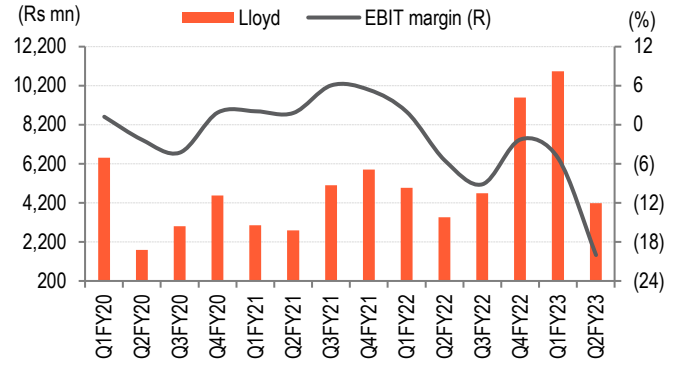
Source: Company, BOBCAPS Research

**Fig 3 – C&W margin impacted by absorption of high-cost inventory**



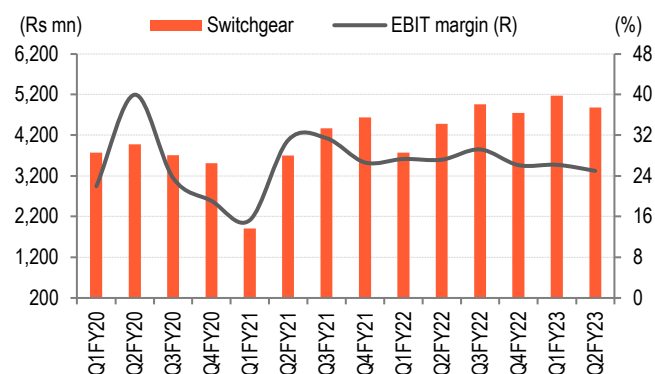
Source: Company, BOBCAPS Research

**Fig 4 – Lloyd continued to face losses in pursuit of market share**



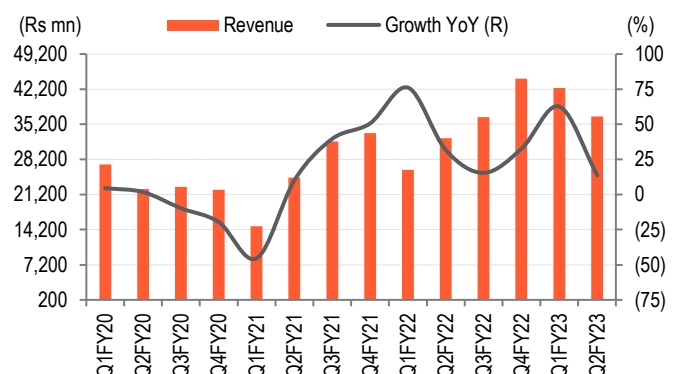
Source: Company, BOBCAPS Research

**Fig 5 – Switchgear business fared relatively better**



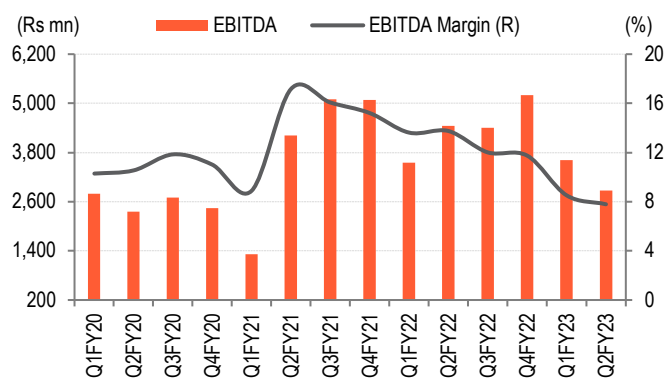
Source: Company, BOBCAPS Research

**Fig 6 – Overall revenue in line with estimates**



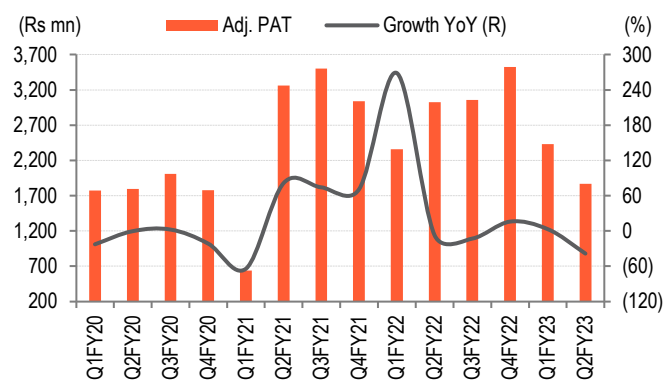
Source: Company, BOBCAPS Research

**Fig 7 – Absorption of high-cost inventory hurt margin...**



Source: Company, BOBCAPS Research

**Fig 8 – ...in turn depleting net profit**



Source: Company, BOBCAPS Research

**Fig 9 – Quarterly performance**

(Rs mn)	Q2FY23	Q2FY22	YoY (%)	Q1FY23	QoQ (%)
Revenue	36,794	32,380	13.6	42,445	(13.3)
EBITDA	2,868	4,450	(35.5)	3,615	(20.7)
EBITDA margin (%)	7.8	13.7	595bps	8.5	72bps
Depreciation	721	624		721	
Interest	68	111		98	
Other Income	438	333		476	
PBT	2,516	4,048	(37.8)	3,273	(23.1)
Tax	647	1,024		841	-
Adjusted PAT	1,870	3,024	(38.2)	2,432	(23.1)
Exceptional item					
Reported PAT	1,870	3,024	(38.2)	2,432	(23.1)
Adj. PAT margin (%)	5.1	9.3	(426bps)	5.7	(65bps)
EPS (Rs)	3.0	4.8	(38.2)	3.9	(23.1)

Source: Company, BOBCAPS Research

**Fig 10 – Actual vs. Estimates**

(Rs mn)	Actual	Estimates	Variance (%)
Revenue	36,794	36,479	0.9
EBITDA	2,868	4,160	(31.1)
EBITDA margin (%)	7.8	11.4	(360bps)
Adj. PAT	1,870	2,893	(35.4)

Source: Company, BOBCAPS Research

**Fig 11 – Segment-wise performance**

(Rs mn)	Q1FY20	Q2FY20	Q3FY20	Q4FY20	Q1FY21	Q2FY21	Q3FY21	Q4FY21	Q1FY22	Q2FY22	Q3FY22	Q4FY22	Q1FY23	Q2FY23
<b>Revenue</b>														
ECD	6,235	5,506	5,814	4,603	3,017	5,799	7,831	7,124	5,763	7,294	8,955	8,727	8,396	7,735
Lighting	2,853	2,831	3,080	2,659	1,423	2,723	3,626	3,367	2,144	3,591	4,129	4,052	3,737	4,018
Switch Gears	3,775	3,977	3,713	3,511	1,902	3,703	4,371	4,633	3,773	4,482	4,960	4,745	5,169	4,879
Cables & Wires	7,785	8,213	7,121	6,823	4,611	7,847	9,052	10,292	8,072	11,440	12,058	14,881	11,929	13,594
Llyod Consumer	6,520	1,800	3,004	4,579	3,062	2,804	5,116	5,906	4,975	3,463	4,698	9,596	10,938	4,198
<b>EBIT</b>														
ECD	823	1,383	770	560	370	1,172	1,405	1,090	676	1,257	1,128	1,515	1,100	900
EBIT margin (%)	13.2	25.1	13.2	12.2	12.3	20.2	17.9	15.3	11.7	17.2	12.6	17.4	13.1	11.6
Lighting	367	785	481	322	38	534	831	698	331	784	874	633	614	576
EBIT margin (%)	12.9	27.7	15.6	12.1	2.7	19.6	22.9	20.7	15.5	21.8	21.2	15.6	16.4	14.3
Switch gear	830	1,589	875	670	291	1,150	1,372	1,234	1,031	1,218	1,448	1,239	1,354	1,220
EBIT margin (%)	22.0	39.9	23.6	19.1	15.3	31.0	31.4	26.6	27.3	27.2	29.2	26.1	26.2	25.0
Cables & wires	845	1,510	767	666	366	1,118	1,026	1,528	1,262	1,153	1,256	1,734	875	859
EBIT margin (%)	10.9	18.4	10.8	9.8	7.9	14.3	11.3	14.8	15.6	10.1	10.4	11.7	7.3	6.3
Lloyd consumer	82	(42)	(128)	85	64	51	309	318	97	(188)	(429)	(215)	(563)	(840)
EBIT margin (%)	1.3	(2.3)	(4.3)	1.9	2.1	1.8	6.0	5.4	2.0	(5.4)	(9.1)	(2.2)	(5.1)	(20.0)

Source: Company, BOBCAPS Research

## Earnings call highlights

- **Growth backed by volumes:** Volume-led growth (80%) has been a key positive for HAVL in Q2FY23, as opposed to price-led growth in the previous three years. Per management, the company has seen a demand uptick over the past fortnight despite continued inflationary pressures. That said, the impact of inflation on rural demand is particularly noticeable (rural market formed 5-6% of consumer revenue in Q2FY23; tier-2/3 cities contributed >50% of overall business). Nonetheless, management expects healthy growth in the next 2-3 years, supported by strong real estate demand and expanded electrification in India.
- **Margins bottoming out:** HAVL's EBITDA margin has deteriorated for the second consecutive quarter mainly due to underperformance at Lloyd and in the W&C and ECD segments. Nonetheless, management expects margins to normalise by Q4FY24 as a majority of high-cost inventory, particularly in W&C and ACs, has been absorbed.
- **Market share gains:** The company has 15% share in W&C while Lloyd commands 12-13% in the AC segment.
- **Aggressive growth at Lloyd to continue:** Lloyd's is focused on growth, gaining market share in room ACs (among the top three players) and adding product categories. Investments in brand building are expected to continue over the next 2-3 years. Lloyd is currently in a transition period due to new energy efficiency regulations (effective Jan'23) and expects to raise prices in Q4FY23. Management anticipates a double-digit contribution margin and a normalised EBIT margin by Q4FY23.
- **Fans facing the heat:** Fans sales continued to slow due to channel destocking, largely caused by the new energy efficiency norms, with management guiding for a slowdown in Q3 as well followed by stronger traction from Q4FY23. Water heaters and appliances, on the other hand, are guided to perform well in Q3 due to festive demand, with margins likely to be supported by moderating raw material prices for the ECD segment
- **Capex:** HAVL plans to spend Rs 10bn-12bn over FY23-FY24, with Rs 1.7bn spent in H1FY23. The company is setting up a new facility in Tumkur (Karnataka), with water heater capacity to come online soon and AC production to start from Q4FY23.
- **A&P:** Normalised advertising spends are guided at 2.5% of sales for FY23.

## Valuation methodology

HAVL is a comprehensive play on consumer durables with a presence across all relevant categories. We believe the company is well positioned for a recovery in growth and profitability from H2FY23, driven by execution in the cables business and margin normalisation at Lloyd. Further, we remain positive on HAVL's wide presence, superior execution and inherent growth structure.

Factoring in the Q2FY23 performance, we trim our FY23/FY24 EPS estimates by 9%/6%. On rolling valuations forward to Sep'24E, our TP stays at Rs 1,500 based on an unchanged 53x P/E – 10% premium to the five-year average. Retain BUY.

**Fig 12 – Revised estimates**

Particulars (Rs mn)	New		Old		Change (%)	
	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E
Sales	1,58,658	1,78,918	1,58,387	1,78,593	0.2	0.2
EBITDA	19,292	23,817	21,073	25,352	(8.4)	(6.1)
PAT	13,277	16,403	14,609	17,405	(9.1)	(5.8)
EPS	21.2	26.2	23.3	27.8	(9.1)	(5.8)
EBITDAM (%)	12.2	13.3	13.3	14.2	(114.5)	(88.4)

Source: Company, BOBCAPS Research

## Key risks

Key downside risks to our estimates are:

- failure to normalise Lloyd's EBIT margin, and
- demand slowdown in the cables & wires segment.

## Sector recommendation snapshot

Company	Ticker	Market Cap (US\$ bn)	Price (Rs)	Target (Rs)	Rating
Amber Enterprises	AMBER IN	0.9	2,199	2,300	HOLD
Blue Star	BLSTR IN	1.4	1,204	1,100	HOLD
Crompton Greaves	CROMPTON IN	2.9	381	500	BUY
Dixon Technologies	DIXON IN	3.1	4,296	4,500	BUY
Havells India	HAVL IN	9.2	1,210	1,500	BUY
Orient Electric	ORIENTEL IN	0.7	269	310	HOLD
Polycab India	POLYCAB IN	4.8	2,649	3,300	BUY
V-Guard Industries	VGRD IN	1.3	253	250	HOLD
Voltas	VOLT IN	3.5	869	1,100	HOLD

Source: BOBCAPS Research, NSE | Price as of 20 Oct 2022

## Financials

### Income Statement

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23E	FY24E	FY25E
<b>Total revenue</b>	<b>1,04,573</b>	<b>1,39,385</b>	<b>1,58,658</b>	<b>1,78,918</b>	<b>2,06,336</b>
EBITDA	15,718	17,604	19,292	23,817	28,227
Depreciation	2,489	2,609	2,722	3,129	3,894
EBIT	13,229	14,995	16,570	20,688	24,334
Net interest inc./(exp.)	(727)	(534)	(585)	(612)	(648)
Other inc./(exp.)	1,874	1,604	1,765	1,853	1,946
Exceptional items	0	0	0	0	0
EBT	14,376	16,066	17,750	21,929	25,631
Income taxes	3,932	4,101	4,473	5,526	6,459
Extraordinary items	0	0	0	0	0
Min. int./Inc. from assoc.	0	0	0	0	0
<b>Reported net profit</b>	<b>10,443</b>	<b>11,965</b>	<b>13,277</b>	<b>16,403</b>	<b>19,172</b>
Adjustments	0	0	0	0	0
<b>Adjusted net profit</b>	<b>10,443</b>	<b>11,965</b>	<b>13,277</b>	<b>16,403</b>	<b>19,172</b>

### Balance Sheet

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23E	FY24E	FY25E
Accounts payables	15,971	23,800	26,081	29,411	33,918
Other current liabilities	10,525	10,881	12,385	13,967	16,107
Provisions	0	0	0	0	0
Debt funds	4,922	3,955	3,900	4,078	4,320
Other liabilities	5,341	6,567	7,475	8,429	9,721
Equity capital	626	626	626	626	626
Reserves & surplus	51,137	59,403	67,667	78,745	92,592
Shareholders' fund	51,763	60,029	68,294	79,372	93,219
<b>Total liab. and equities</b>	<b>88,523</b>	<b>1,05,232</b>	<b>1,18,134</b>	<b>1,35,257</b>	<b>1,57,285</b>
Cash and cash eq.	19,591	27,014	29,035	37,925	50,200
Accounts receivables	5,637	7,663	8,638	9,788	11,261
Inventories	26,199	29,681	33,905	38,167	44,055
Other current assets	1,778	1,708	1,944	2,193	2,529
Investments	0	0	0	0	0
Net fixed assets	32,904	34,336	39,114	40,985	42,091
CWIP	899	572	651	734	847
Intangible assets	0	0	0	0	0
Deferred tax assets, net	0	0	0	0	0
Other assets	1,515	4,258	4,847	5,466	6,304
<b>Total assets</b>	<b>88,523</b>	<b>1,05,232</b>	<b>1,18,134</b>	<b>1,35,257</b>	<b>1,57,285</b>

### Cash Flows

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23E	FY24E	FY25E
<b>Cash flow from operations</b>	<b>6,603</b>	<b>17,278</b>	<b>14,349</b>	<b>18,784</b>	<b>22,017</b>
Capital expenditures	(1,536)	(2,528)	(7,500)	(5,000)	(5,000)
Change in investments	0	0	0	0	0
Other investing cash flows	(6,096)	(5,067)	240	252	342
<b>Cash flow from investing</b>	<b>(7,632)</b>	<b>(7,595)</b>	<b>(7,260)</b>	<b>(4,748)</b>	<b>(4,658)</b>
Equities issued/Others	98	312	0	0	0
Debt raised/repaid	14,883	0	(56)	179	242
Interest expenses	0	0	0	0	0
Dividends paid	(13,083)	(5,783)	(5,012)	(5,325)	(5,325)
Other financing cash flows	0	0	0	0	0
<b>Cash flow from financing</b>	<b>1,898</b>	<b>(5,472)</b>	<b>(5,068)</b>	<b>(5,147)</b>	<b>(5,083)</b>
<b>Chg in cash &amp; cash eq.</b>	<b>869</b>	<b>4,212</b>	<b>2,021</b>	<b>8,889</b>	<b>12,275</b>
<b>Closing cash &amp; cash eq.</b>	<b>19,591</b>	<b>27,014</b>	<b>29,035</b>	<b>37,925</b>	<b>50,200</b>

### Per Share

Y/E 31 Mar (Rs)	FY21A	FY22A	FY23E	FY24E	FY25E
Reported EPS	16.7	19.1	21.2	26.2	30.6
Adjusted EPS	16.7	19.1	21.2	26.2	30.6
Dividend per share	6.5	7.5	8.0	8.5	8.5
Book value per share	82.6	95.8	109.0	126.7	148.8

### Valuations Ratios

Y/E 31 Mar (x)	FY21A	FY22A	FY23E	FY24E	FY25E
EV/Sales	7.2	5.4	4.8	4.2	3.7
EV/EBITDA	48.2	43.1	39.3	31.8	26.9
Adjusted P/E	72.6	63.3	57.1	46.2	39.5
P/BV	14.6	12.6	11.1	9.5	8.1

### DuPont Analysis

Y/E 31 Mar (%)	FY21A	FY22A	FY23E	FY24E	FY25E
Tax burden (Net profit/PBT)	72.6	74.5	74.8	74.8	74.8
Interest burden (PBT/EBIT)	108.7	107.1	107.1	106.0	105.3
EBIT margin (EBIT/Revenue)	12.7	10.8	10.4	11.6	11.8
Asset turnover (Rev./Avg TA)	3.2	4.1	4.1	4.4	4.9
Leverage (Avg TA/Avg Equity)	0.7	0.6	0.6	0.6	0.5
<b>Adjusted ROAE</b>	<b>22.0</b>	<b>21.4</b>	<b>20.7</b>	<b>22.2</b>	<b>22.2</b>

### Ratio Analysis

Y/E 31 Mar	FY21A	FY22A	FY23E	FY24E	FY25E
<b>YoY growth (%)</b>					
Revenue	10.8	33.3	13.8	12.8	15.3
EBITDA	52.8	12.0	9.6	23.5	18.5
Adjusted EPS	42.0	14.6	11.0	23.5	16.9
<b>Profitability &amp; Return ratios (%)</b>					
EBITDA margin	15.0	12.6	12.2	13.3	13.7
EBIT margin	12.7	10.8	10.4	11.6	11.8
Adjusted profit margin	10.0	8.6	8.4	9.2	9.3
Adjusted ROAE	22.0	21.4	20.7	22.2	22.2
ROCE	22.0	20.5	20.1	21.7	21.7
<b>Working capital days (days)</b>					
Receivables	20	20	20	20	20
Inventory	91	78	78	78	78
Payables	56	62	60	60	60
<b>Ratios (x)</b>					
Gross asset turnover	2.5	3.2	3.2	3.2	3.4
Current ratio	1.9	1.8	1.8	2.0	2.1
Net interest coverage ratio	18.2	28.1	28.3	33.8	37.6
<b>Adjusted debt/equity</b>	<b>0.1</b>	<b>0.1</b>	<b>0.1</b>	<b>0.1</b>	<b>0.0</b>

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

## Disclaimer

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

**BUY** – Expected return >+15%

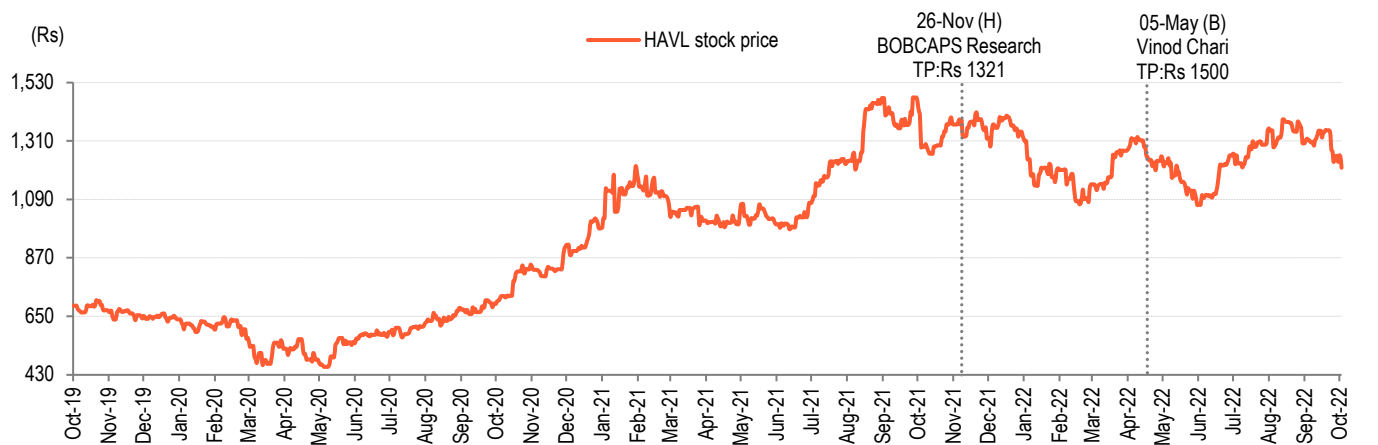
**HOLD** – Expected return from -6% to +15%

**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.

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

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