

**HOLD**

TP: Rs 280 | ▲ 7%

**ORIENT ELECTRIC**

Consumer Durables

04 November 2022

### One-offs mar performance

- Q2 in the red as fans business remained a drag, marked by transition to new energy norms and one-time distribution exercise
- Streamlining of distribution in new states likely to stabilise by Q4, with plans to increase coverage area in fans by the year-end
- We slash FY23/FY24 EPS 30%/19% post the Q2 upset and roll over to a new TP of Rs 280 (vs. Rs 310); retain HOLD

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**Gloomy quarter:** ORIENTEL's Q2FY23 revenue declined 14% YoY (23% below our est.) as a one-time revenue loss reduced growth by 11ppt. EBITDA margin plunged 800bps YoY to 2.3% due to (i) low operating leverage, (ii) higher A&P spends, and (iii) investment in strategic initiatives. Excluding strategic investments, the normalised EBITDA margin would have been ~6%. All these factors led to a net loss of Rs 2.8mn vs. our estimate of Rs 325mn in profits.

**Fans a drag for second consecutive quarter:** The electrical consumer durables (ECD) segment saw a steep revenue drop of 26% YoY due to transition to new energy norms (resulting in channel destocking), sales disruption in the key African market, and exceptional loss due to a one-time distribution exercise. Adjusted for the latter exceptional loss, ECD fell 10%. Lower fan volumes weighed on ECD EBIT margin, which stood at 4.4% (vs. 12.3% in Q2FY22). Management remains uncertain of how channel partners will react as energy efficiency ratings turn stricter (effective Jan'23).

**Streamlining of distribution dents Q2:** ORIENTEL undertook phase-2 of its fan distribution streamlining exercise in Uttar Pradesh (UP), Karnataka, Andhra Pradesh (AP) and Telangana – per management, this caused a one-time revenue loss. The company expects UP and Karnataka to grow in Q3FY23, followed by AP and Telangana in Q4. Bihar and Orissa (part of Phase 1) have stabilised and are growing at +50% YoY.

**Lighting segment a silver lining:** Lighting segment growth was at 15% YoY, led by a 40% upswing in the B2B category. The company is gaining traction in the facade lighting space after winning major projects. It has introduced house wires in order to enhance product portfolio in ECD.

**Maintain HOLD:** With new energy rating norms kicking in and the phase-2 distribution model yet to find its feet, we expect ORIENTEL's fans business to remain weak in the near term. Following the Q2 upset, we slash FY23/FY24 EPS estimates by 30%/19%. On rollover to Sep'24E valuations, our TP moves to Rs 280 (vs. Rs 310). We continue to value the stock at 35x P/E – a 20% discount to the 3Y mean – and retain HOLD.

### Key changes

Target	Rating
▼	◀ ▶

Ticker/Price	ORIENTEL IN/Rs 263
Market cap	US\$ 677.8mn
Free float	62%
3M ADV	US\$ 0.9mn
52wk high/low	Rs 408/Rs 244
Promoter/FPI/DII	39%/6%/29%

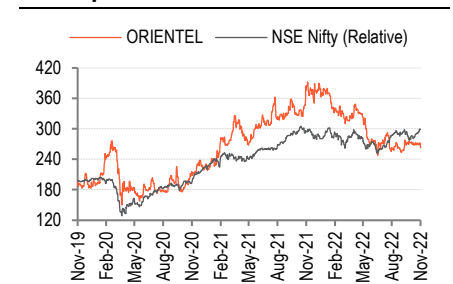
Source: NSE | Price as of 4 Nov 2022

### Key financials

Y/E 31 Mar	FY22A	FY23E	FY24E
Total revenue (Rs mn)	24,484	27,336	31,591
EBITDA (Rs mn)	2,313	2,117	2,790
Adj. net profit (Rs mn)	1,266	1,064	1,503
Adj. EPS (Rs)	6.0	5.0	7.1
Consensus EPS (Rs)	6.0	8.2	10.0
Adj. ROAE (%)	25.4	18.6	23.3
Adj. P/E (x)	44.0	52.4	37.1
EV/EBITDA (x)	24.1	26.3	20.0
Adj. EPS growth (%)	46.1	(16.0)	41.3

Source: Company, Bloomberg, BOBCAPS Research

### Stock performance



Source: NSE



**Fig 1 – Quarterly performance**

Particulars (Rs mn)	Q2FY23	Q2FY22	YoY (%)	Q1FY23	QoQ (%)	H1FY22	H1FY23	YoY (%)
Revenue	5,106	5,944	(14.1)	6,216	(17.9)	10,167	11,322	(10.2)
EBITDA	116	619	(81.2)	382	(69.6)	842	498	69.2
EBITDA Margin (%)	2.3	10.4	(810bps)	6.1	(390bps)	8.3	4.4	(210bps)
Depreciation	131	117	-	128	-	233	259	-
Interest	48	50	-	52	-	98	100	-
Other Income	65	13	-	52	-	22	117	-
PBT	1	466	(99.7)	254	(99.5)	534	255	109.1
Tax	4	118	-	64	-	136	69	-
Adjusted PAT	(3)	348	NA	190	NA	398	187	113.1
Exceptional item	-	-	-	-	-	-	-	-
Reported PAT	(3)	348	NA	190	NA	398	187	113.1
Adj. PAT Margin (%)	(0.1)	5.8	(590bps)	3.0	(310bps)	3.9	1.6	(170bps)
EPS (Rs)	0.0	1.6	(100.8)	0.9	(101.5)	2	1	113.1

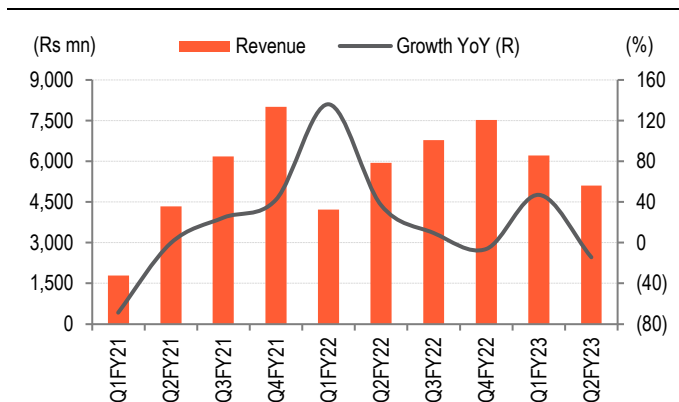
Source: Company, BOBCAPS Research

**Fig 2 – Actual vs. Estimates**

Particulars (Rs mn)	Actual	BOBCAPS	Variance (%)
Revenue	5,106	6,659	(23.3)
EBITDA	116	587	(80.2)
EBITDA Margin (%)	2	8.8	(654bps)
Adj. PAT	-3	325	(100.9)

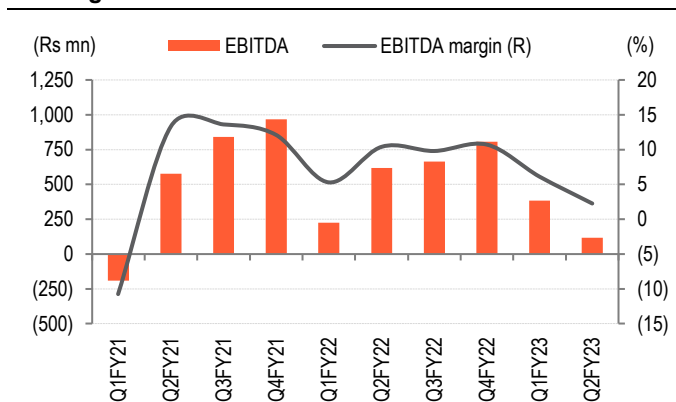
Source: Company, BOBCAPS Research

**Fig 3 – Revenue growth muted due to one-off events**



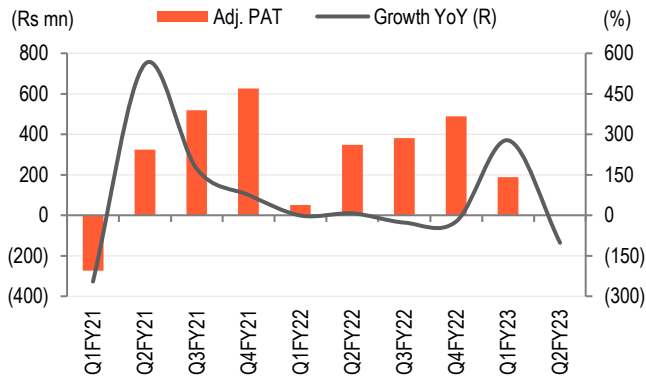
Source: Company, BOBCAPS Research

**Fig 4 – EBITDA margin impacted due to A&P spend and strategic investments**



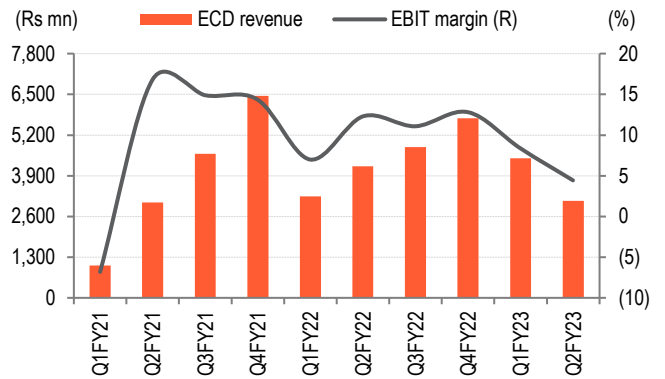
Source: Company, BOBCAPS Research

**Fig 5 – Net loss reported in Q2**



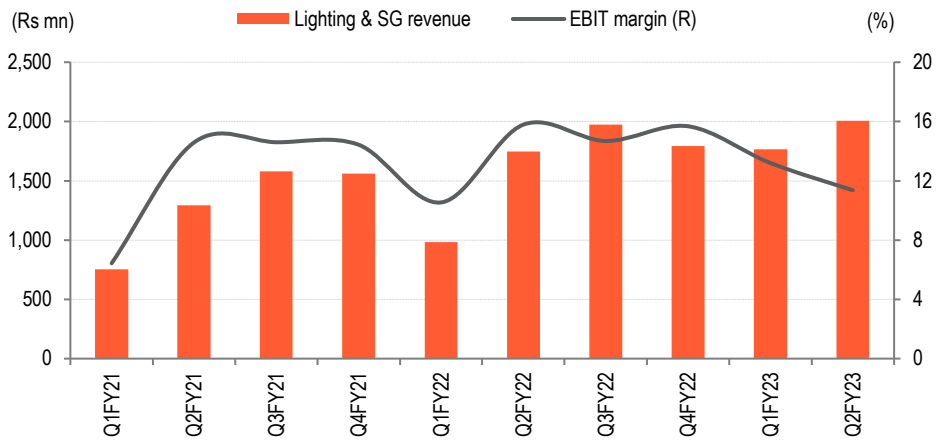
Source: Company, BOBCAPS Research

**Fig 6 – ECD: Fans remain a drag**



Source: Company, BOBCAPS Research

**Fig 7 – Lighting: Growth momentum continues**



Source: Company, BOBCAPS Research

## Earnings call highlights

- **Outlook:** Management continues to focus on expanding market share and depth. In the case of fans, the vacuum created by channel destocking is likely to result in an increase in trade in the coming quarters. Further, the company believes that the government's awareness campaign about power-guzzling fans is likely to increase consumer spends on energy-efficient products, which should benefit the segment.
- **Fan distribution strategy:** ORIENTEL's Master Distributor programme is currently only for fans and is restricted to geographies where the company has a small market share. States covered by the new strategy account for 25% of the market potential in fans. The company plans to stabilise distribution in current states by end-FY23 before venturing into new markets.
- **ECD:** The ECD segment declined 26% YoY in Q2FY23 and grew 2% in H1. Fans performed the worst during the quarter. In the case of appliances, a strong push for channel filling of water heaters in Q1 followed by weak consumer demand in Q2, liquidity challenges and stock corrections by trade resulted in a quarterly decline.
- **Lighting:** The lighting segment continued to grow in double digits, with a 15% increase in Q2FY23 and a 38% rise in H1. In Q2, revenue from the B2B segment climbed 40% YoY. Luminaires rose 17% compared to last year. ORIENTEL is also emerging as a significant player in the fast-growing facade lighting space. This quarter's key projects include: (i) the Varanasi Cantonment Railway Station, (ii) the Kanpur Ganga Barrage Project, and (iii) the Srinagar Smart City Project. This apart, the company is aggressively investing in brand building with the launch of an expanded range of festival lighting ('Joylight').
- **Wires:** ORIENTEL has no intention of making a large investment in wires; the focus is solely on providing a comprehensive portfolio that will spur the promotion of other products.
- **Other income:** Other income rose five-fold to Rs 65mn in Q2 due to the liquidation of previous provisions.
- **Employee cost:** Employee benefit expenses decreased 12% YoY owing to lower manpower deployment (as production was curtailed) and as past vacancies were left unfilled.
- **Cost saving programme:** In the first half of FY23, Project 'Spark Sanchay' identified annualised cost reduction opportunities worth Rs 680mn.
- **BEE (Bureau of Energy Efficiency) ratings:** Only BLDC (brushless direct current motor) fans are eligible for 5-star energy ratings which denote the highest efficiency. According to the company, most fans today do not qualify for even a single star, so technological advancement is required. The production cost difference between a star-rated and a non-star-rated product could be 3-10%.
- **Inventory:** Per management, inventory has corrected at present with only a small proportion of non-star-rated products that are expected to be cleared this month.

- **Exports:** Sales in Africa are suffering due to political and economic turmoil. Management expects recovery there to take a while whereas other markets are recovering.
- **Go-to-Market strategy**
  - **Fans:** ORIENTEL has reached ~9,000 retailers in six direct-to-market states, and the company plans to increase distribution reach and visibility by ~85% of the market potential by end-FY23. Management indicated that Bihar, Orissa, and UP are already experiencing significant growth, while AP, Telangana, and Karnataka are expected to start delivering results in Q3FY23. Per the company, digital marketing solutions are being implemented in all states and sales force automation has been stabilised across geographies.
  - **Lighting:** Aggressive efforts are being made to capture market share in lighting. ORIENTEL has ~28,000 retail points following the addition of 5,200 touchpoints in Q2. In H1, 100 new distributors were appointed, accounting for 116mn units in sales. Digital marketing solutions and sales force automation are being fully implemented in the division, and the latter is fully operational.

## Valuation methodology

With new energy rating norms kicking in from Jan'23 and the company's phase-2 distribution model yet to find its feet, we expect ORIENTEL's performance in its core fans business to remain lacklustre in the near term. Following the Q2FY23 upset, we slash our FY23/ FY24 EPS estimates by 30%/19%. On rollover to Sep'24E valuations, our TP reduces to Rs 280 (earlier Rs 310). We continue to value the stock at 35x P/E – a 20% discount to the three-year average – and retain HOLD.

**Fig 8 – Revised estimates**

Particulars (Rs mn)	New		Old		Change (%)	
	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E
Sales	27,336	31,591	28,826	33,150	(5.2)	(4.7)
EBITDA	2,117	2,790	2,718	3,269	(22.1)	(14.6)
PAT	1,064	1,503	1,509	1,857	(29.5)	(19.0)
EPS (Rs)	5.0	7.1	7.1	8.7	(29.5)	(19.0)
EBITDA Margin (%)	7.7	8.8	9.4	9.9	(170bps)	(100bps)

Source: Company, BOBCAPS Research

## Key risks

Key risks to our estimates are:

- **Upside risks:** Above-expected performance in fans; significant margin expansion
- **Downside risks:** Renewed distribution strategy failing to pan out

## Sector recommendation snapshot

Company	Ticker	Market Cap (US\$ bn)	Price (Rs)	Target (Rs)	Rating
Amber Enterprises	AMBER IN	0.8	2,020	2,100	HOLD
Blue Star	BLSTR IN	1.4	1,223	1,100	HOLD
Crompton Greaves	CROMPTON IN	2.8	362	500	BUY
Dixon Technologies	DIXON IN	3.3	4,514	5,200	BUY
Havells India	HAVL IN	9.2	1,209	1,500	BUY
Orient Electric	ORIENTEL IN	0.7	263	280	HOLD
Polycab India	POLYCAB IN	5.0	2,729	3,300	BUY
V-Guard Industries	VGRD IN	1.3	255	250	HOLD
Voltas	VOLT IN	3.4	845	1,000	HOLD

Source: BOBCAPS Research, NSE | Price as of 4 Nov 2022

## Financials

### Income Statement

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23E	FY24E	FY25E
<b>Total revenue</b>	<b>19,993</b>	<b>24,484</b>	<b>27,336</b>	<b>31,591</b>	<b>36,330</b>
EBITDA	1,864	2,313	2,117	2,790	3,436
Depreciation	432	471	532	616	700
EBIT	1,433	1,842	1,585	2,174	2,736
Net interest inc./(exp.)	(207)	(203)	(227)	(235)	(253)
Other inc./(exp.)	63	58	64	70	77
Exceptional items	0	0	0	0	0
EBT	1,288	1,698	1,422	2,009	2,560
Income taxes	422	431	358	506	645
Extraordinary items	(331)	0	0	0	0
Min. int./Inc. from assoc.	0	0	0	0	0
<b>Reported net profit</b>	<b>1,197</b>	<b>1,266</b>	<b>1,064</b>	<b>1,503</b>	<b>1,915</b>
Adjustments	(331)	0	0	0	0
<b>Adjusted net profit</b>	<b>867</b>	<b>1,266</b>	<b>1,064</b>	<b>1,503</b>	<b>1,915</b>

### Balance Sheet

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23E	FY24E	FY25E
Accounts payables	5,191	4,495	5,617	6,491	7,465
Other current liabilities	1,036	930	1,038	1,199	1,379
Provisions	0	0	0	0	0
Debt funds	614	675	732	784	842
Other liabilities	226	361	403	466	536
Equity capital	212	212	212	212	212
Reserves & surplus	4,344	5,201	5,786	6,688	7,837
Shareholders' fund	4,557	5,413	5,998	6,900	8,049
<b>Total liab. and equities</b>	<b>11,624</b>	<b>11,874</b>	<b>13,788</b>	<b>15,841</b>	<b>18,271</b>
Cash and cash eq.	2,576	1,505	2,029	2,329	2,843
Accounts receivables	3,552	3,904	4,607	5,325	6,123
Inventories	2,492	3,261	3,524	4,072	4,683
Other current assets	345	280	313	362	416
Investments	0	0	0	0	0
Net fixed assets	1,716	1,900	2,200	2,500	2,800
CWIP	0	0	0	0	0
Intangible assets	230	234	234	234	234
Deferred tax assets, net	0	0	0	0	0
Other assets	714	789	881	1,018	1,171
<b>Total assets</b>	<b>11,624</b>	<b>11,874</b>	<b>13,788</b>	<b>15,841</b>	<b>18,271</b>

### Cash Flows

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23E	FY24E	FY25E
<b>Cash flow from operations</b>	<b>4,273</b>	<b>114</b>	<b>1,827</b>	<b>1,841</b>	<b>2,305</b>
Capital expenditures	(359)	(423)	(300)	(300)	(300)
Change in investments	22	1,172	0	0	0
Other investing cash flows	(1,169)	33	(582)	(691)	(783)
<b>Cash flow from investing</b>	<b>(1,506)</b>	<b>782</b>	<b>(882)</b>	<b>(991)</b>	<b>(1,083)</b>
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	(900)	(208)	57	52	58
Interest expenses	0	0	0	0	0
Dividends paid	(537)	(588)	(479)	(601)	(766)
Other financing cash flows	0	0	0	0	0
<b>Cash flow from financing</b>	<b>(1,437)</b>	<b>(797)</b>	<b>(422)</b>	<b>(549)</b>	<b>(708)</b>
<b>Chg in cash &amp; cash eq.</b>	<b>1,330</b>	<b>99</b>	<b>523</b>	<b>301</b>	<b>514</b>
<b>Closing cash &amp; cash eq.</b>	<b>2,576</b>	<b>1,505</b>	<b>2,029</b>	<b>2,329</b>	<b>2,843</b>

### Per Share

Y/E 31 Mar (Rs)	FY21A	FY22A	FY23E	FY24E	FY25E
Reported EPS	5.6	6.0	5.0	7.1	9.0
Adjusted EPS	4.1	6.0	5.0	7.1	9.0
Dividend per share	2.0	2.0	2.3	2.8	3.6
Book value per share	21.5	25.5	28.3	32.5	37.9

### Valuations Ratios

Y/E 31 Mar (x)	FY21A	FY22A	FY23E	FY24E	FY25E
EV/Sales	2.8	2.3	2.0	1.8	1.5
EV/EBITDA	29.9	24.1	26.3	20.0	16.2
Adjusted P/E	64.4	44.0	52.4	37.1	29.1
P/BV	12.2	10.3	9.3	8.1	6.9

### DuPont Analysis

Y/E 31 Mar (%)	FY21A	FY22A	FY23E	FY24E	FY25E
Tax burden (Net profit/PBT)	67.3	74.6	74.8	74.8	74.8
Interest burden (PBT/EBIT)	89.9	92.1	89.7	92.4	93.6
EBIT margin (EBIT/Revenue)	7.2	7.5	5.8	6.9	7.5
Asset turnover (Rev./Avg TA)	11.7	12.9	12.4	12.6	13.0
Leverage (Avg TA/Avg Equity)	0.4	0.4	0.4	0.4	0.4
Adjusted ROAE	21.3	25.4	18.6	23.3	25.6

### Ratio Analysis

Y/E 31 Mar	FY21A	FY22A	FY23E	FY24E	FY25E
<b>YoY growth (%)</b>					
Revenue	(1.7)	22.5	11.7	15.6	15.0
EBITDA	26.2	24.1	(8.5)	31.8	23.1
Adjusted EPS	73.7	46.1	(16.0)	41.3	27.4
<b>Profitability &amp; Return ratios (%)</b>					
EBITDA margin	9.3	9.4	7.7	8.8	9.5
EBIT margin	7.2	7.5	5.8	6.9	7.5
Adjusted profit margin	4.3	5.2	3.9	4.8	5.3
Adjusted ROAE	21.3	25.4	18.6	23.3	25.6
ROCE	19.6	25.2	19.2	23.3	25.4
<b>Working capital days (days)</b>					
Receivables	65	58	62	62	62
Inventory	45	49	47	47	47
Payables	95	67	75	75	75
<b>Ratios (x)</b>					
Gross asset turnover	11.3	13.5	13.3	13.4	13.7
Current ratio	1.4	1.6	1.5	1.5	1.5
Net interest coverage ratio	6.9	9.1	7.0	9.2	10.8
Adjusted debt/equity	0.1	0.1	0.1	0.1	0.1

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

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**BUY** – Expected return >+15%

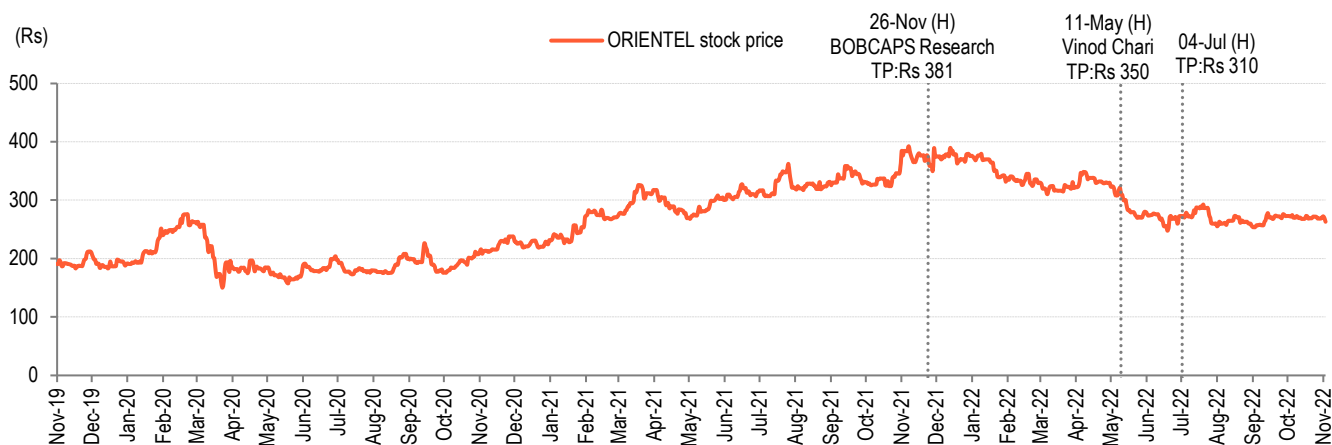
**HOLD** – Expected return from -6% to +15%

**SELL** – Expected return <-6%

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

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): ORIENT ELECTRIC (ORIENTEL IN)



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

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