

Negative surprise from Lloyd...

Havells' muted topline growth at 4% YoY in Q1FY20 was below our estimate mainly due to Lloyd division, which surprised us with revenue de-growth of 8% YoY in the strong season for air conditioners. In addition, the poor demand for switchgear and cable business is largely due to prevailing weakness in the real estate industry and delay in government projects post elections. On the margin front, decline in EBITDA margin by ~200 bps YoY was largely on account of higher employee cost and advertisement expenditure incurred in the Lloyd business. Though the management guided for a recovery in EBITDA margin from H2FY20E onwards, we believe it would be below its five year average margin of ~13%. We cut our revenue, earning estimate by 2%, 9% and 4%, 9% for FY20E and FY21E, respectively.

Demand slowdown hurts topline growth

Though Havells' ECD segment recorded strong growth (led by fan, water purifier and small domestic appliances), the Lloyd business remained a drag in Q1FY20. The rationalisation of AC dealers (shift towards more organised network to build Lloyd into a mass premium product) coupled with structural shift in LED panel industry (despite rising competitive intensity from Chinese players) took a toll on volume growth of Lloyd. Industrial product categories like industrial cable, professional lighting and switchgear demand were impacted by a delay in fresh government projects since elections and continuous weakness in the real estate business. Though the management was confident of a recovery in demand from H2FY20, we build in revenue CAGR of 15% FY19-21E (earlier 17%) led by ECD revenue CAGR 17% (of which 18% CAGR in the Lloyd business).

EBITDA margin remains intact

Though Havells maintained its gross margin in Q1FY20, the EBITDA margin was largely hit by higher employee cost (~23% YoY) and advertisement expenses (~19% YoY). Segment wise, while Havells' core EBITDA margin declined 60 bps YoY at 12.9%, Lloyd's EBITDA margin fell from 9.3% to 1.4% in Q1FY20. Lloyd's margin has remained lower compared to Havells business (at 5.3% vs. Havells' EBITDA margin of 13.4% in FY19). We believe pressure to take a price hike due to rising competition in the Lloyd business would keep Havells' overall EBITDA margin under check.

Valuation & Outlook

We believe Havells' Lloyd business is in a transition phase with high investment in people, technology and branding. This, coupled with pricing pressure in the air conditioner business (due to significant competition from MNCs) would likely weigh on overall EBITDA margin of the company in the near term. We maintain our **HOLD** rating on the stock and revise our target price lower to ₹ 725.



Particulars

Particular	Amount
Market Capitalization (₹ Crore)	41,551.7
Total Debt (FY19) (₹ Crore)	40.5
Cash and Inv (FY19) (₹ Crore)	707.7
EV (₹ Crore)	40,884.6
52 week H/L	807 / 550
Equity capital (₹ Crore)	62.5
Face value (₹)	1.0

Key Highlights

- Lloyd business dragged overall Havells' performance in Q1FY20
- Industrial product demand remained muted owing to delay in fresh government projects
- Margin expected to recover in FY20 albeit at a slower pace than FY19 level
- We maintain HOLD rating on the stock with revised target price of ₹ 720/share

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Key Financial Summary

₹ Crore	FY17	FY18	FY19	FY20E	FY21E	CAGR FY19-21E
Net Sales	6135.3	8138.5	10057.6	11480.3	13234.0	14.7
EBITDA	824.2	1049.2	1192.2	1376.0	1739.6	20.8
EBITDA Margin (%)	13.4	12.9	11.9	12.0	13.1	
PAT	539.2	712.5	791.5	887.0	1110.0	18.4
EPS (₹)	8.6	11.4	12.7	14.2	17.8	
P/E (x)	77.1	58.3	52.5	46.8	37.4	
Price/Book Value (x)	12.7	11.1	9.8	9.4	8.1	
Mcap/Sales	6.8	5.1	4.1	3.6	3.1	
RoE (%)	17.7	18.8	18.7	20.1	21.5	
RoCE (%)	23.4	25.2	25.3	27.9	30.1	

Exhibit 1: Variance Analysis

	Q1FY20	Q1FY20E	Q1FY19	YoY (%)	Q4FY19	QoQ (%)	Comments
Revenue	2712.0	2907.5	2596.3	4.5	2751.9	-1.4	Decline in Lloyd revenue (by ~8% YoY) dragged overall revenue growth
Other Income	39.7	34.1	29.2	35.9	31.0	28.3	
Raw Material Exp	1276.7	1686.3	1081.2	18.1	1260.4	1.3	
Employee Exp	241.3	226.8	197.0	22.5	221.3	9.0	
Purchase of Traded goods	422.2	145.4	539.7	-21.8	470.4	-10.2	
Other expenses	496.2	494.3	466.3	6.4	476.9	4.0	
EBITDA	275.7	354.7	312.2	-11.7	322.9	-14.6	
EBITDA Margin (%)	10.2	12.2	12.0	-186 bps	11.7	-157 bps	Sharp decline in profitability of Lloyd business (EBITDA margin down from 9.3% to 1.4%) dragged overall EBITDA margin of the company
Depreciation	46.9	42.5	35.0	33.9	39.1	20.1	
Interest	4.7	1.2	2.6	85.1	6.1	-23.1	
PBT	263.8	345.1	303.8	-13.2	308.6	-14.5	
Total Tax	89.8	105.6	93.5	-3.9	101.8	-11.7	
PAT	173.9	239.5	210.4	-17.3	206.8	-15.9	Lower EBITDA margin translated into PAT decline
Key Metrics							
Cable	778.5	816.2	749.9	3.8	897.9	-13.3	Delay in fresh government projects since elections had impacted demand of cable business
Switchgear	377.5	440.4	375.8	0.5	436.8	-13.6	Real estate slowdown impacted switchgear segment
ECD	1,275.5	1,356.2	1,212.3	5.2	1,037.3	23.0	ECD (excluding Lloyd) grew ~24% YoY at ~₹ 624 crore led by new product categories such as (water purifier and air cooler). while Lloyd sales declined 8% YoY at ₹ 652 crore mainly due to steep decline in LED panels
Lighting & Fixtures	280.5	380.0	258.3	8.6	380.0	-26.2	Lower demand of professional lighting coupled with absence of price hike had impacted lighting segment

Source: Company, ICICI Direct Research

Exhibit 2: Change in estimates

(₹ Crore)	FY20E			FY21E			Comments
	Old	New	% Change	Old	New	% Change	
Revenue	11694.7	11480.3	(1.8)	13707.2	13234.0	(3.5)	We model revenue CAGR of 15% in FY19-21E largely driven by ECD segment
EBITDA	1492.8	1376.0	(7.8)	1883.2	1739.6	(7.6)	
EBITDA Margin %	12.8	12.0	-81bps	13.7	13.1	-56bps	High competition in AC business kept price hike under check. We believe there will be a gradual recovery in margin in FY20E-21E from FY19 level
PAT	978.2	887.0	(9.3)	1244.4	1110.0	(10.8)	
EPS (₹)	15.7	14.2	(9.4)	20.0	17.8	(10.8)	

Source: Company, ICICI Direct Research

Exhibit 3: Assumptions

	Current			Earlier			Comments
	FY18	FY19E	FY20E	FY21E	FY20E	FY21E	
Cable Growth (%)	9.3	24.4	12.7	13.8	13.7	13.6	Higher government expenditure in infrastructure growth would be key growth driver for cable segment, going forward
Switchgear Growth (%)	0.1	19.4	10.7	13.0	14.0	15.1	Expectation of better demand from real estate and export segment would be key drivers for segment performance, going forward
ECD Growth (%)	115.8	29.4	16.9	17.0	18.3	21.3	Lower penetration coupled with rising aspiration level of middle class would help drive performance of ECD segment
Lighting & Fixtures (%)	19.1	11.9	14.2	16.7	19.9	16.4	Lighting segment growth to largely be driven by LED fixtures

Source: Company, ICICI Direct Research

Conference call highlights

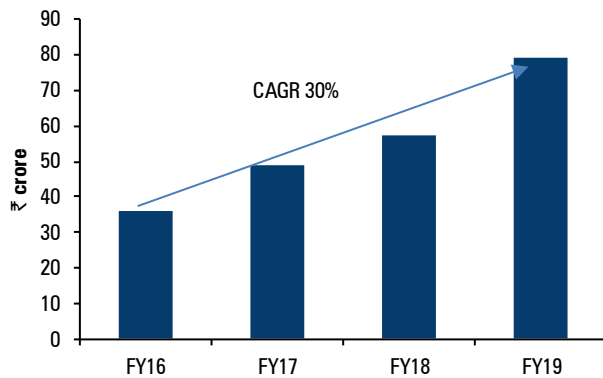
- Havells continues to shift from the mass category to the mass premium category while undergoing a structural change
- Electrical segment grew 24% YoY led by water heater, water purifier & air cooler sales. Havells continued to dominate the water heater segment retaining the No. 1 position
- The ECD segment gained market share but suffered a lower contribution margin due to product mix
- The company with 19% market share in fans category continued to grow and consolidate while water heaters and other small appliances, which have relatively lower market share witnessed good growth
- Switchgear segment, which contributes to around 17% of the revenue was mainly impacted by construction slowdown, liquidity crunch and competition from Chinese players
- Switchgear segment is focusing more towards wholesale, dealers & contractors while the ECD & lighting segment is more inclined towards retail stores
- Under the Lloyd brand, air conditioner segment witnessed a slight decline in margins while LED panels suffered a greater decline in margin due to competition from new Chinese products
- Professional Luminare segment was sluggish due to overall economic downturn while the consumer luminare segment witnessed decent growth led by high volume growth of 10-12%
- The company has commissioned a plant for in house manufacturing of Lloyd products, which is estimated to produce 75% of production in-house
- The company has incurred a capex of ₹ 140 crore in Q1FY20 and has further outlined a capex of ₹ 500 crore for FY19-20
- Havells currently has 1,17,000 retail outlets in semi urban & urban areas and 25,000 in rural areas & small towns. The company plans to increase their retail outlets in rural areas to 60,000 outlets
- Havells is preparing for the future with constant product expansion, deepening market reach and brand enforcement

Annual report highlights

Continue focus on 'Deeper into Home' strategy

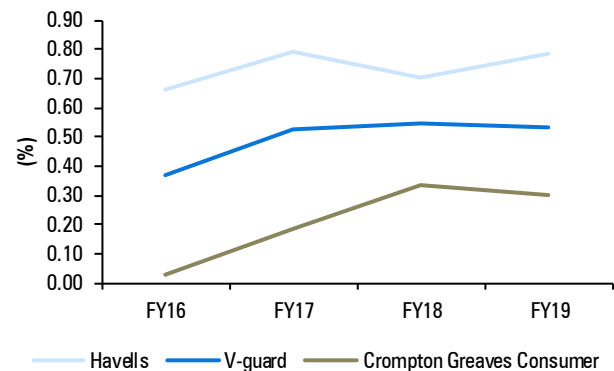
- Over the years, Havells has continuously been increasing its product mix towards electrical consumer durable (ECD) categories. The revenue contribution of ECD segment into total topline has increased from 20% in FY15 to 38% in FY19
- Today Havells has total four product portfolios (cable & wire, switchgear, lightings and ECD) with over ~10700 SKUs
- Started with only three consumer products (fans, lightings & switches) in 2004, today Havells has wide range of consumer facing products includes fans, water heaters, personal grooming products, home appliances, air conditioners, washing machines, TV, luminaires for domestic, etc
- In FY19, the company introduced/upgraded ~200 products, which includes water purifiers, connected products in the appliance, switches and lighting areas, low noise ceiling fans and mixer grinders, power saving BLDC fans
- With the aim of being a global peer in electrical products, Havells is investing significantly in R&D. In the last five years, R&D expenditure increased at a CAGR of 30%. According to the management, Havells would continuously increase its R&D expenditure, going ahead. The higher expenditure in R&D would keep Havells ahead of its competition in terms of new product launches

Exhibit 4: R&D expenditure trend



Source: Company, ICICI Direct Research

Exhibit 5: R&D expenditure(% of sales) vis a vis competition



Source: Company, ICICI Direct Research

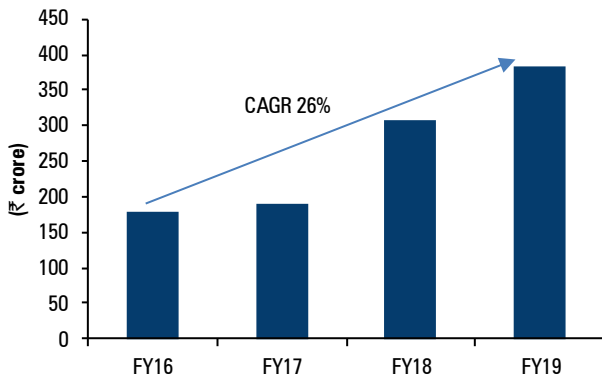
- Under the new product category, the company will enter the refrigerator segment by end of FY20

Leveraging channel by expanding product portfolio

- The company has a dealer network that has increased from 6259 dealers in FY15 to 10500+ in FY19
- The company is leveraging its existing dealer networks to push new products
- In order to focus on mass premium category products, Havells is continuously expanding its reach in semi-urban and urban areas. The company is focusing on increasing its presence in small towns with population ranging from 10,000 to 50,000. In the last year, Havells has reached more than 1,000 semi-urban and rural towns. It is further planning is to expand its presence in more than 3,000 towns in FY20

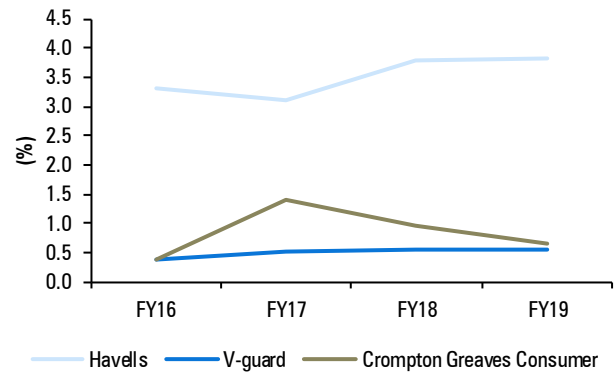
- While competition has reduced its advertisement and promotional (A&P) expense, Havells A&P expenses increased 25% YoY. Havells has remained ahead of competition in case of branding exercise

Exhibit 6: Aggressive advertisement expenses



Source: Company, ICICI Direct Research

Exhibit 7: Higher ad expenses compared to peers



Source: Company, ICICI Direct Research

Seasonality factor hits margin

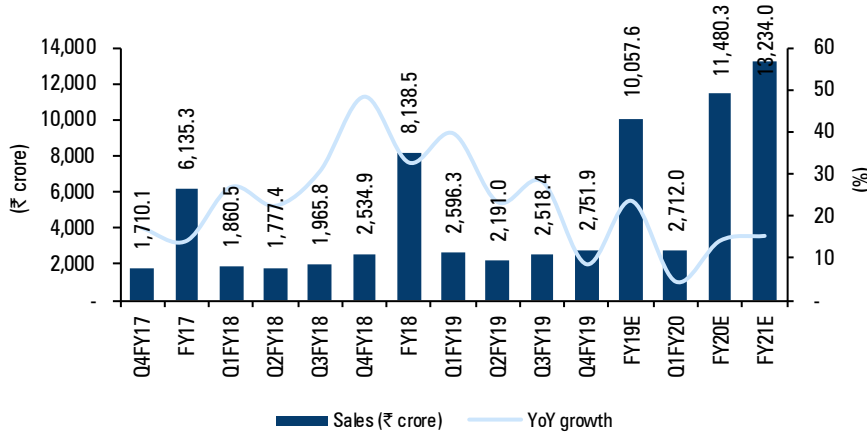
- Havells experienced a demand slowdown intensified by liquidity crunch, extended winters and impending general elections in Q4
- Despite this, the company recorded a revenue growth of 24% YoY led by market share gains in some products and launch of new products. However, Havells faced pressure in gross margin fluctuation in commodity prices & forex rates, hike in custom duty and liquidity shortage due to NBFC crisis
- This coupled with higher A&P expenses and employee cost resulting in EBITDA margin declining ~100 bps YoY at 11.9% in FY19. As a result, PAT grew albeit a lower pace of 11% YoY
- Higher working capital days was largely on account of a reduction in payable days during FY19

Capex to increase in house manufacturing

- During the period, the company incurred a capex of ₹ 350 crore to set up its first AC manufacturing plant at Ghiloth, Rajasthan
- The company has outlined a capex of ₹ 600 crore for FY20E mainly to expand the existing product capacity

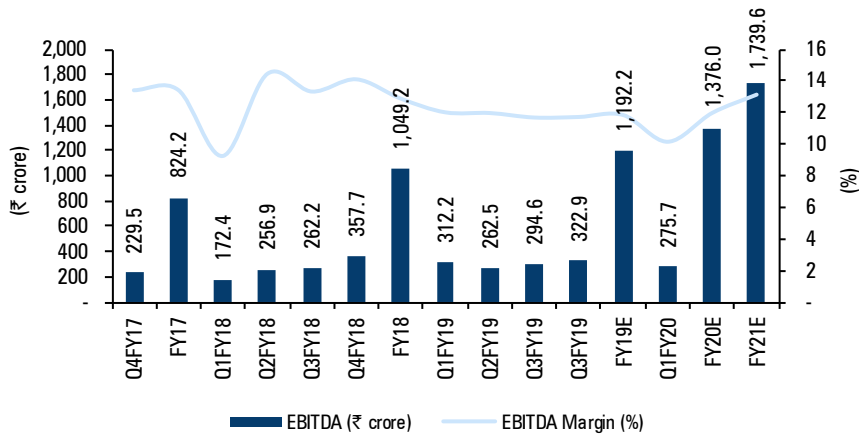
Financial story in charts

Exhibit 8: ECD segment leads revenue growth



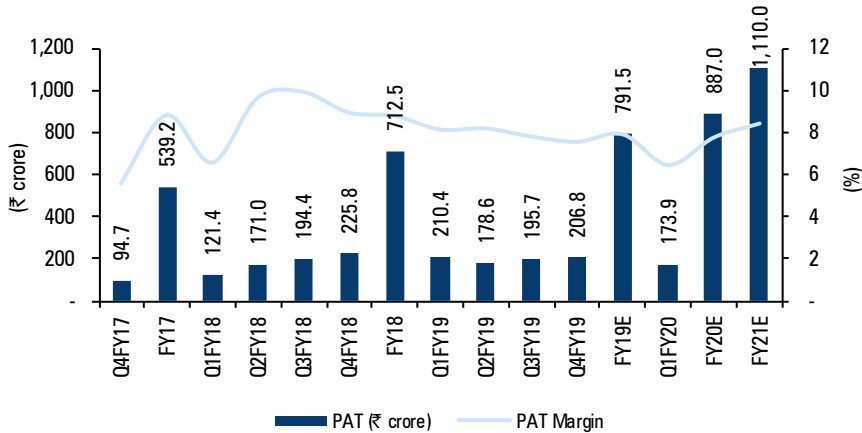
Source: Company, ICICI Direct Research

Exhibit 9: EBITDA margin movement



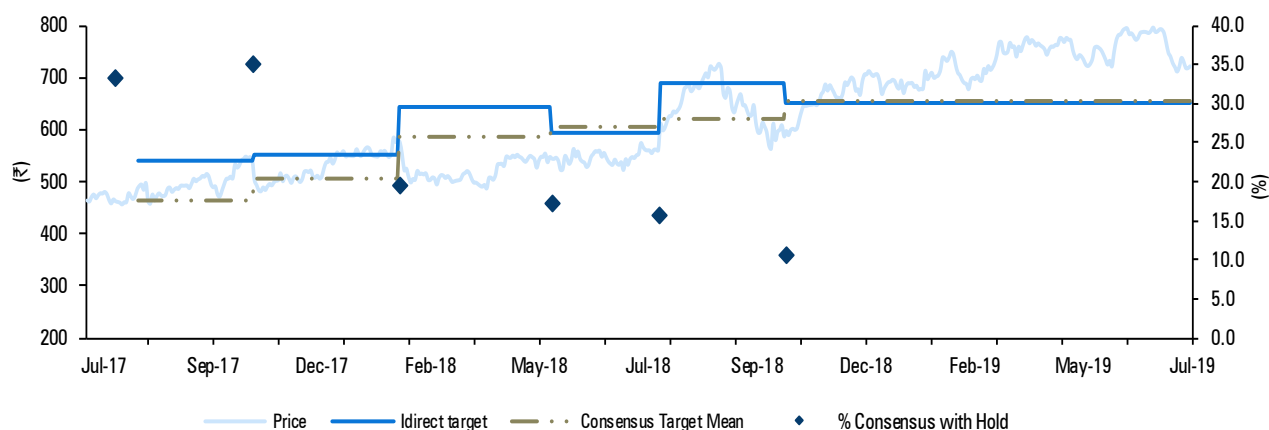
Source: Company, ICICI Direct Research

Exhibit 10: Sales growth leads PAT growth



Source: Company, ICICI Direct Research

Exhibit 11: Recommendation History vs. Consensus



Source: Bloomberg, Company, ICICI Direct Research

Exhibit 12: Top 10 Shareholders

Rank	Name	Last filing date	% O/S	Position (m)	Change (m)
1	QRG Enterprises, Ltd.	30-06-2019	41.3%	258.60M	0
2	Gupta (Anil Rai)	30-06-2019	12.4%	77.43M	+13.58M
3	Gupta (Surjeet Kumar)	30-06-2019	5.8%	36.43M	0
4	Nalanda India Equity Fund Ltd.	30-06-2019	5.3%	33.04M	0
5	Capital Research Global Investors	30-06-2019	2.5%	15.80M	-3.24M
6	Norges Bank Investment Management (NBIM)	30-06-2019	2.4%	14.81M	+0.56M
7	Life Insurance Corporation of India	30-06-2019	1.8%	11.43M	+11.43M
8	Steadview Capital Management HK Limited	30-06-2019	1.7%	10.67M	0
9	The Vanguard Group, Inc.	30-06-2019	1.4%	8.72M	+0.01M
10	BlackRock Institutional Trust Company, N.A.	30-06-2019	1.2%	7.26M	-0.00M

Source: Reuters, ICICI Direct Research

Exhibit 13: Recent Activity

Buys				Sells			
Investor name	Value(m)	Shares(m)		Investor name	Value(m)	Shares(m)	
Gupta (Anil Rai)	+154.9M	+13.58M		Gupta (Smt Vinod)	-154.9M	-13.58M	
Life Insurance Corporation of India	+130.4M	+11.43M		Gupta (Qimat Rai)	-136.6M	-13.58M	
Norges Bank Investment Management (NBIM)	+6.4M	+0.56M		Capital Research Global Investors	-37.0M	-3.24M	
Florida State Board of Administration	+3.1M	+0.28M		Ivy Investment Management Company	-6.9M	-0.62M	
FIL Investment Management (Hong Kong) Limited	+2.4M	+0.23M		Amundi Hong Kong Limited	-5.9M	-0.53M	

Source: Reuters, ICICI Direct Research

Exhibit 14: Shareholding Pattern

(in %)	Jun-18	Sep-18	Dec-18	Mar-19	Jun-19
Promoter	59.6	59.6	59.6	59.6	59.5
FII	24.8	25.8	26.5	27.3	27.0
DII	5.2	4.9	4.4	3.9	4.6
Others	10.5	9.8	9.5	9.3	8.9

Source: Company, ICICI Direct Research

Financial summary

Exhibit 15: Profit and loss statement				
	₹ crore			
Year End March	FY18	FY19	FY20E	FY21E
Total Operating Income	8138.5	10057.6	11480.3	13234.0
Growth (%)		23.6	14.1	15.3
Raw Material Expenses	3586.7	4513.0	5969.8	7146.3
Employee Expenses	649.7	832.4	884.5	838.0
Marketing Expenses	307.6	384.2	463.2	510.5
Other expenses	1151.2	1370.2	1489.4	1786.7
Operating Expenditure	7089.3	8865.4	10104.3	11494.4
EBITDA	1049.2	1192.2	1376.0	1739.6
Growth (%)		13.6	15.4	26.4
Other Income	117.0	127.6	152.4	183.7
Interest	24.0	15.9	15.4	12.4
Depreciation	139.5	148.6	189.4	251.4
Less: Exceptional Items	-11.9	0.0	0.0	0.0
PBT	1014.6	1155.3	1323.6	1659.3
Total Tax	302.2	363.7	436.6	549.3
PAT	712.5	791.5	887.0	1110.0

Source: Company, ICICI Direct Research

Exhibit 16: Cash flow statement				
	₹ crore			
(Year-end March)	FY18	FY19	FY20E	FY21E
Profit after Tax	712.5	791.5	887.0	1110.0
Depreciation	139.5	148.6	189.4	251.4
CF before working cap changes	875.9	956.0	1091.8	1373.9
Net Increase in Current Assets	-670.8	125.3	-767.3	-675.7
Net Increase in Current Liabilities	1094.1	89.0	285.2	299.5
CF from operating activities	1299.3	1170.3	609.7	997.6
(Purchase)/Sale of Liquid Investrn	-8.0	-21.7	-50.0	-50.0
Others	-1352.6	-451.2	-350.0	-350.0
(Purchase)/Sale of Fixed Assets	-1360.6	-472.8	-400.0	-400.0
CF from Investing Activities	-1187.6	-421.9	-500.0	-500.0
Proceeds frm Equity Shares	0.0	0.0	0.0	0.0
Inc / (Dec) in Loan Funds	-94.6	-67.5	0.0	20.0
Others	-271.0	-304.0	-732.3	-383.7
CF from Financing Activities	-365.6	-371.5	-732.3	-363.7
Net Cash flow	-253.9	376.8	-622.6	133.9
Opening Cash	555.1	301.2	678.0	55.4
Closing Cash	301.2	678.0	55.4	189.4

Source: Company, ICICI Direct Research

Exhibit 17: Balance sheet				
	₹ crore			
(Year-end March)	FY18	FY19	FY20E	FY21E
Equity Capital	62.5	62.6	62.6	62.6
Reserve and Surplus	3676.7	4180.0	4350.0	5088.8
Total Shareholders funds	3739.1	4242.5	4412.6	5151.4
Total Debt	108.0	40.5	40.5	60.5
Deferred Tax Liability	207.0	321.7	321.7	321.7
Total Liabilities	4077.3	4625.9	4796.0	5554.8
Assets				
Total Gross Block	3180.9	3445.6	3845.6	4245.6
Less Acc. Depreciation	706.2	854.7	1044.2	1295.6
Net Block	2474.7	2590.9	2801.4	2950.0
Capital WIP	24.1	232.2	232.2	232.2
Total Fixed Assets	2498.7	2823.0	3033.6	3182.1
Investment	491.21	67.29	109.29	209.29
Inventory	1621.7	1917.0	2201.7	2538.0
Debtors	325.4	422.4	943.6	1160.2
Other Current Assets	1359.9	833.3	803.6	926.4
Cash	301.2	678.0	55.4	189.4
Total Current Assets	3608.1	3859.6	4004.4	4814.0
Total Current Liabilities	2464.1	2553.1	2838.3	3137.7
Net Current Assets	1144.0	1306.6	1166.1	1676.3
Total Assets	4077.3	4625.9	4796.0	5554.8

Source: Company, ICICI Direct Research

Exhibit 18: Key ratios				
	₹ crore			
(Year-end March)	FY18	FY19	FY20E	FY21E
Per Share Data				
Reported EPS	11.4	12.7	14.2	17.8
Cash EPS	13.7	15.1	17.3	21.8
BV per share	59.9	68.0	70.7	82.6
DPS	4.8	5.4	4.2	6.0
Operating Ratios (%)				
EBITDA Margin (%)	12.9	11.9	12.0	13.1
PAT Margin (%)	8.7	7.9	7.7	8.4
Asset Turnover	2.0	2.2	2.4	2.4
Debtors Turnover	14.6	15.3	30.0	32.0
Creditor Turnover	73.3	56.6	55.0	55.0
Return Ratios (%)				
RoE	18.8	18.7	20.1	21.5
RoCE	25.2	25.3	27.9	30.1
RoIC	22.6	25.7	23.9	26.8
Valuation Ratios				
EV / EBITDA	39.4	34.3	30.1	23.7
P/E	58.3	52.5	46.8	37.4
EV / Net Sales	5.1	4.1	3.6	3.1
EV / Net Sales	5.1	4.1	3.6	3.1
Market Cap / Sales	5.1	4.1	3.6	3.1
Price to Book Value	11.1	9.8	9.4	8.1
Solvency Ratios				
Debt / Equity	0.0	0.0	0.0	0.0
Current Ratio	1.8	1.8	2.1	2.1
Quick Ratio	0.9	0.7	0.9	0.9

Source: Company, ICICI Direct Research

Exhibit 19: ICICI Direct Coverage Universe (Consumer Discretionary)

Sector / Company	CMP			M Cap (₹ Cr)	EPS (₹)			P/E (x)			EV/EBITDA (x)			RoCE (%)			RoE (%)		
	(₹)	TP(₹)	Rating		FY19E	FY20E	FY21E	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E	FY18E	FY19E	FY20E
Asian Paints (ASIPAI)	1,513	1,550	Hold	145,097	23.0	27.1	33.1	65.7	55.9	45.8	37.7	31.9	26.8	30.4	32.7	34.6	23.2	24.7	26.2
Astral Polytechnik (ASTPOL)	1,245	1,250	Hold	14,909	16.5	20.9	27.9	75.5	59.5	44.6	36.4	29.1	22.8	20.7	22.7	26.0	15.4	16.6	18.3
Bajaj Electricals (BAJELE)	369	470	Hold	3,766	18.9	21.4	26.3	19.6	17.2	14.0	14.8	13.0	11.5	17.2	17.8	19.5	18.5	17.9	18.5
Havells India (HAVIND)	666	720	Hold	41,552	12.7	14.2	17.8	52.5	46.8	37.4	34.3	30.1	23.7	25.3	27.9	30.1	18.7	20.1	21.5
Kansai Nerolac (KANNER)	431	455	Hold	23,227	8.7	9.7	11.3	49.7	44.6	38.1	29.5	25.7	22.0	20.2	21.8	22.9	13.6	14.6	15.4
Pidilite Industries (PIDIND)	1,241	1,335	Buy	63,619	18.8	18.1	22.8	65.9	68.5	54.5	42.6	34.3	28.4	29.6	32.3	34.0	22.7	24.5	25.6
Essel Propack (ESSPRO)	133	136	Hold	4,179	6.2	6.7	7.9	21.5	19.8	16.7	9.3	8.3	7.2	16.9	17.4	19.3	13.9	13.7	15.0
Supreme Indus (SUPIND)	1,055	1,165	Buy	13,401	35.3	39.3	44.8	29.9	26.8	23.6	16.6	14.0	12.4	25.0	28.6	28.6	18.7	21.5	21.5
Symphony (SYMLIM)	1,226	1,110	Hold	8,577	13.0	23.2	31.6	94.2	52.8	38.8	35.9	60.5	33.7	41.3	18.7	30.4	31.5	16.2	27.0
V-Guard Ind (VGUARD)	229	230	Hold	9,748	3.9	5.0	5.7	58.8	45.8	40.2	53.2	45.0	33.9	23.7	23.7	29.1	17.7	18.4	22.1
Voltas Ltd (VOLTAS)	572	645	Hold	18,918	15.5	27.2	23.8	36.8	21.0	24.1	28.1	29.4	14.9	19.8	17.3	27.4	14.8	12.7	21.0
Time Techno (TIMTEC)	77	101	Hold	1,741	9.0	10.6	12.5	8.6	7.3	6.1	6.2	5.7	5.2	14.9	15.0	15.8	12.2	12.1	12.9

Source: Company, ICICI Direct Research

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Buy: >15%

Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



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