Initiating Coverage

BUY

VOLTAS LTD

Structural story intact…

Sunidhi
"In your prosperity lies our success"
Institutional Research

July 12, 2011

Rating	Buy
CMP (₹)	157
Price Target (₹)	200
Upside (%)	27.4
Key Data	
BSE Code	500575
NSE Code	VOLTAS
Reuters Code	VOLT.BO
Bloomberg Code	VOLT IN
Sensex	18412
No. of Shares, mn	330.7
Face Value ₹	1
Mcap, ₹ mn	51920
Mcap,USD mn @ ₹45	1153.8
52 week H/L	262/147
2Wk Avg. Daily Vol. BSE	5.1 Lac
Share holding, June'11	**% Holding**
Promoters	30.6
FIIS	18.4
DIIs	29.8
Others & Public	21.2
Share Holding >1%	**%**
LIC	10.8
ICICI Pru Life Insurance	4.1
Govt. Pension Fund Global	1.8

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Electromechanical project business to witness recovery in FY12-13E

Electromechanical project (EMP) business of Voltas faced headwinds in FY11 as its main focus markets in middle east remained challenging with high competitive intensity. Management however hopes to book sufficient orders in FY13E due to its expanded geographical presence through two new JVs in Saudi Arabia and Oman and few tie ups in Hong Kong. The company expects to generate substantial amount of revenue from few large orders it is executing in Qatar which accounts for 50% of its total international order book of ₹ 29.3 bn. After a sluggish beginning, work on these projects has picked up now. Thus we expect Voltas' EMP business to return to a stronger growth trajectory in H2FY12E and FY13E. Also Rohini's expected break-even in FY12E will lend stability to the revenue stream of its EMP segment.

Engineering products business on a sustainable growth path

The engineering segment contributed about 10.9% of total consolidated revenues and about 20.6% of total EBIT generated in FY11. The segment has shown lacklustre growth of only 4% CAGR (FY07-10) as this business suffered due to slowdown in industrial, mining and construction capex. However going forward we expect the engineering business to show 8.2% sales CAGR (FY10-13E) with EBIT margin of 18% and 17.8% in FY12E and FY13E due to 1) higher proportion of agency business; 2) operating leverage from sales growth; and 3) increasing higher margin service revenue (contributes a third to total segmental sales).

Maintains market share in unitary cooling business despite stiff competition

Over the last several years, Voltas has maintained its market share in the UCP segment owing to its strong brand equity, efficient distribution channels and competitive pricing despite facing stiff competition from new entrants.

High return ratios and net cash on books to facilitate future inorganic growth

Voltas' low cost operations and asset light model with significant outsourcing have resulted in high return ratios (RoCE >33%). Its net cash rich balance sheet provides ample funds to facilitate future inorganic growth through acquisitions.

Outlook &Valuation

Voltas witnessed muted revenue growth and contraction in margins (especially in EMP segment) in FY11. Going forward we see its margins stabilizing around 9-10% level on the back of improved execution and resumption of order inflows from middle east region. Voltas remains the preferred player in the MEP and HVAC space and would continue to be a key beneficiary of industrial capex. At CMP of ₹157, the stock is trading at 11.8x FY13E estimates. We initiate coverage with a 'Buy' rating and a price target of ₹200 based on FY13E target PE of 15x

Brief Financials ₹ mn	Revenues	growth %	EBITDA	PAT	growth %	EPS ₹	P/E x	EV/EBITDA x	ROE %
FY09	43617.2	35.1	3189.1	2514.0	22.6	7.6	20.7	14.9	28.5
FY10	48236.0	10.6	4768.7	3809.9	51.6	11.5	13.6	9.5	32.8
FY11	51913.7	7.6	4553.8	3572.4	(6.2)	10.8	14.5	10.2	23.9
FY12E	56561.1	9.0	5235.5	3762.1	5.3	11.4	13.8	8.8	23.4
FY13E	64388.9	13.8	6262.8	4392.3	16.8	13.3	11.8	7.2	22.8

Source: Company & Sunidhi Research

Investment Rationale

Voltas provides end-to-end solutions in the domains of mechanical, electrical and plumbing (MEP) and low-temperature refrigeration for process cooling & cold storage

Electromechanical project business (EMP) to witness recovery in FY12-13E

Voltas is India's largest provider and exporter of electromechanical projects (EMP) and services, and covers infrastructure (airports, metros), real-estate (buildings, hospitals, hotels, IT parks) and industrial (power, cement, steel, paper and others) sectors. Voltas provides end-to-end solutions in the domains of mechanical, electrical and plumbing (MEP) and low-temperature refrigeration for process cooling and cold storage in both domestic and international markets. Some of the recent projects executed in this segment are Formula 1 race track in Abu Dhabi, Burj Dubai, Rajiv Gandhi International Airport, Hyderabad and Chennai International Airport. Key technology partners for this segment include, MIDEA (China) for variable refrigerant flow (VRF) systems and Ruks Engineering (Canada) for ozone-engineered systems.

We believe Voltas can target 3 metro projects that will be constructed over FY11-15E namely, Chennai Metro Phase-I, Bengaluru Metro Phase-I and Kolkata Metro Phase-II will be built with a total cost of ₹100 bn

Urban infrastructure spending to boost domestic business dynamics

With increased spending on urban infrastructure, pick up in construction activities for hospitals, airports and metros continue to be bright. We believe Voltas can target 3 metro projects that will be constructed over FY11-15E namely, Chennai Metro Phase-I, Bengaluru Metro Phase-I and Kolkata Metro Phase-II will be built with a total cost of ₹100 bn. In addition, over next five years, the country will see new construction/modernisation of 33 airports. We believe Voltas will see good demand for MEP services from Tier-2 cities which are also witnessing rapid growth (in the form of malls, hospitals etc). Its timely execution of Hyderabad airport project led to repeat business worth ₹3 bn from Chennai extension project and Kolkata's Netaji Subhas Chandra Bose international airport. Voltas received 45% of new orders in domestic MEP segment in FY10 from repeat clients which indicates high customer acceptance of Voltas' offerings. Also in recently concluded Commonwealth Games in New Delhi, it completed 9 out of 15 sporting venues in a timely manner.

Exhibit-1: Revenue and profitability of EMP business

Particulars (₹ mn)	FY06	FY07	FY08	FY09	FY10	FY11	FY12E	FY13E
Net Sales	11751	14383	17449	27668	31134	30411	32844	35800
EBIT	683	686	1170	2135	3182	2394	2456	2856
EBIT Margins (%)	5.8	4.8	6.7	7.7	10.2	7.9	7.5	8.0

Source: Company, Sunidhi Research

Voltas has started moving away from pure heating ventilation and air conditioning (HVAC) projects to more integrated projects (MEP)

Domestic EMP business

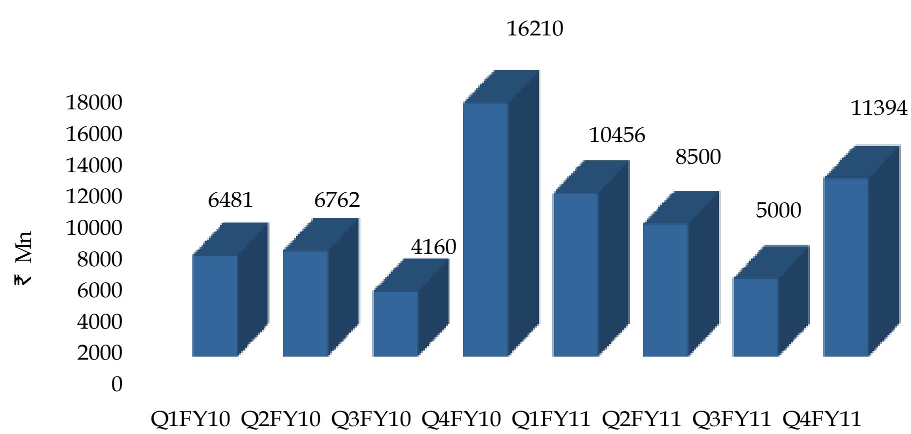
With projects becoming more complex, the trend of awarding entire MEP package to a single vendor instead of awarding separate contracts for each component of the MEP has gained significance. As the preference of clients shifts towards agencies offering comprehensive capabilities and single point responsibility in MEP domain, Voltas has started moving away from pure heating ventilation and air conditioning (HVAC) projects to more integrated projects (MEP) (integration of electrical, plumbing, HVAC and other components such as fire and safety) in the domestic market. This is evident as revenue from pure HVAC has come down from 90% to 50% in the past three years and we believe it is likely to drop further. Margins are also likely to improve for MEP contractor compared to pure HVAC player as moving up the value chain reduces the competitive intensity. In India only 20% of contracting market is currently integrated in MEP format as compared to over 75% in developed countries. As the market penetration increases the quantum of opportunities will expand substantially for Voltas as it is best placed among the domestic full service MEP contractors due to its vast experience in executing projects in different countries in the middle east region.

Voltas is a market leader in India's HVAC and MEP segments, followed by Blue Star

Rohini Electricals

The company acquired Rohini Industrial Electricals Ltd in August 2008, an electrical contracting company, to compete effectively as an MEP solution provider. Of its EMP revenue, 40% comes from the industrial (steel, cement and textiles) sector, while the remaining comes from real estate and infrastructure. Voltas is a market leader in India's HVAC and MEP segments, followed by Blue Star. This segment has seen a revenue CAGR of 15% in the past two years and its order book has grown to ₹2.1bn (as of 31 March 2011). The main drivers of the domestic EMP order book are: 1) commercial real estate including IT parks and campuses; 2) hospitals; 3) airports; 4) metros and 5) industrial and power plants.

Exhibit-2: EMP segment – order inflow over the quarters (consolidated)



Source: Company, Sunidhi Research

Voltas has good order visibility for the next 12 months' revenue

International EMP business

In the international arena, Voltas operates mainly in ASEAN and Middle East markets and has undertaken complex and sophisticated projects in these markets. In Singapore, the company recently undertook some prestigious projects, where it has a Contractor A status. In the Middle East, the company started with Dubai and has now expanded to other areas such as Abu Dhabi, Qatar, Saudi Arabia and Oman. According to management, investments in major GCC countries have picked up from the second half of last year, especially in Abu Dhabi, Qatar and Saudi Arabia and the company has good order visibility for the next 12 months' revenue.

In last quarter Q4FY11, the EMP segment (59% of FY11 sales) reported muted revenue growth of 2% yoy as against 7% growth in Q4FY10

Middle east region facing headwinds for last few quarters

Historically major revenue for EMP segment has been contributed by middle east region comprising Dubai, Abu Dhabi, Qatar and Bahrain alongwith other regions in Singapore and Hong Kong. However for the last few quarters EMP segment is facing some headwinds in the form of slower execution and drying up of fresh orders due to prevailing negative sentiment across the middle east especially MEENA region. In last quarter Q4FY11, the EMP segment (59% of FY11 sales) reported muted revenue growth of 2% yoy as against 7% growth in Q4FY10, mainly on account of weaker execution in international projects segment coupled with declining revenues in Rohini Electricals (its 83.6% subsidiary). As a result segmental EBIT margin also declined 180 bps yoy to 8.3% in Q4FY11, as losses in Rohini continued to dent margins. Rohini booked a loss of ₹120 mn in Q4FY11, (₹95 mn in Q3FY11 and ₹310 mn for FY11).

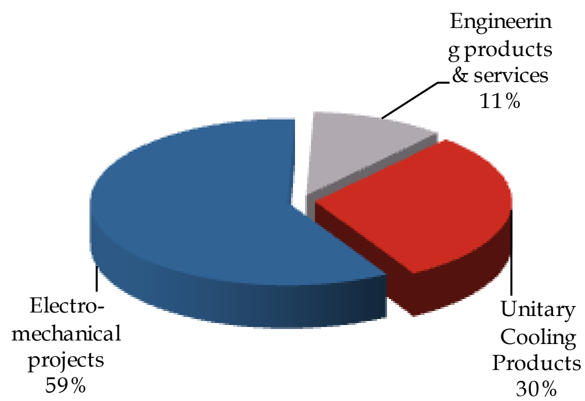
Saudi market offers huge opportunity with US$678 bn worth of projects underway (largest in MEA region)

Huge market in Saudi – limited competition to augur well for Voltas

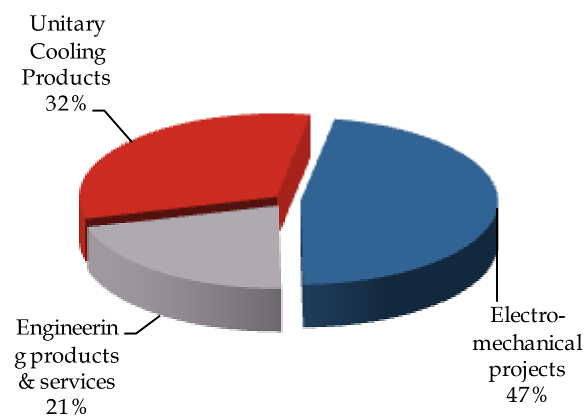
In terms of geographic mix, UAE commands over 50% of project awards and given the slowdown in Dubai, contractors have shifted focus to other geographies such as Abu Dhabi, Saudi Arabia, Oman and Qatar. In order to capture a larger share of the market, Voltas has now formed a 65:35 JV with the Mustafa Sultan group in Oman. Saudi market offers huge opportunity with US$678 bn worth of projects underway (largest in MEA region). Also limited competition in Saudi compared to UAE augurs well for Voltas. The company expects to generate substantial amount of revenue from a set of large projects worth ₹25 bn in UAE and Qatar which would enter mid execution phase. After a sluggish start, work has picked up now on these projects.

Exhibit-3: Revenue and EBIT mix of Voltas (FY11 consolidated)

Segment-wise revenue break-up (FY11 consolidated)



Segment-wise EBIT break-up (FY11 consolidated)



Source: Company, Sunidhi Research

IMF has projected a growth of 4.1% in 2010 and 5.1% in 2011 for the MENA region

Contract awards likely to pick up in middle east region in FY12E-13E

In its World Economic Outlook report, dated October 2010, the IMF stated, with a gradual increase in crude oil prices from its trough level in 2009, they expect the middle east region to show strong growth. IMF has projected a growth of 4.1% in 2010 and 5.1% in 2011 for the MENA region. Based on IMF's projections, we believe target countries in which Voltas operates are expected to see better-than-regional growth rates as they are primarily oil exporters rather than oil importers such as Egypt, Morocco, and Jordan.

Singapore market offers a staggering ₹150 bn annual MEP opportunity driven by pent up government spending on infrastructure projects

Singapore and Hong Kong market to witness increased MEP activities

We believe contract awards will pick up over the next two to three quarters given rising oil prices. Sensing the collapse of the property market in Dubai, Voltas management shifted its focus from Dubai market and has been diversifying to other markets such as Singapore and Hong Kong. Voltas' renewed focus on Singapore alleviates concerns over order inflows. The Singapore market offers a staggering ₹150 bn annual MEP opportunity driven by pent up government spending on infrastructure projects. Leveraging its Contractor A status in Singapore, Voltas is aggressively bidding in this region. Thus we expect Voltas' EMP business to return to a stronger growth trajectory in H2FY12E and FY13E. Also Rohini's expected break-even in FY12E will lend stability to the revenue stream of its EMP segment. **We expect EMP segment to witness a growth of 8% and 9% respectively for FY12E and FY13E, with EBIT margin of 7.5% and 8% respectively for FY12E and FY13E**.

Engineering products business (EPS) on a sustainable growth path

Voltas is present in three businesses textile machinery, mining and construction and forklifts

The engineering segment contributed about 10.9% of total consolidated sales and about 20.6% of consolidated EBIT in FY11. Engineering products are either self manufactured by Voltas, traded (imported and then sold) or sold by acting as an agent of Indian/foreign vendor. While working on agency basis, Voltas earns commission on sales where its scope of work includes installation, commissioning and maintenance of machineries and equipments. It also undertakes repairs and after sales servicing of these machines. Higher agency business results in overall improvement in margins for the engineering product segment as it does not have to undergo manufacturing costs or working capital expenses. The segment has shown lacklustre growth of only 4% CAGR (FY07-10) as this business suffered due to a slowdown in industrial, mining and construction capex. In EPS segment, Voltas is present in three businesses — a) textile machinery, b) mining & construction and c) forklifts. **Going forward we expect the EPS business to show 8.2% sales CAGR (FY10-13E) with EBIT margin of 18% and 17.8% in FY12E and FY13E respectively** helped by: 1) higher proportion of agency business; 2) operating leverage from sales growth; and 3) increasing higher margin service revenue (contributes a third to total segmental sales).

Exhibit-4: Revenue and profitability of EPS business

Particulars (₹ mn)	FY06	FY07	FY08	FY09	FY10	FY11	FY12E	FY13E
Net Sales	2434	4162	5535	5422	4680	5638	5300	5936
EBIT	697	984	1136	628	769	1031	955	1055
EBIT Margins (%)	28.6	23.6	20.5	11.6	16.4	18.3	18.0	17.8

Source: Company, Sunidhi Research

Textile machinery

Voltas is an agent for Laxmi Machine Works, one of the largest equipment suppliers to the textile industry in India and several other equipment manufacturers for spinning, weaving, knitting and processing applications. In addition to representing Laxmi Machine Works, Voltas represents Shandong Rifa Textile Machinery in weaving, Terrot GmbH and Steiger SA in knitting machinery, Lakshmi Card Clothing, Reggiani, Brueckner Textile Technologies GmBH, Dunline Rubber Products, Thies GmBH & Co KG in processing and finishing, and Brueckner Plant Technologies, Oskar Dilo Maschnen Fabrik KG, Hansa Industrir Mixer GmBH & Co KG in non-wovens. Textile machinery products have seen significant traction in the past few quarters and going forward also we expect the positive trend to continue.

Exhibit-5: Voltas has 60% market share in textile machinery (spinning machines)

Source: Company, Sunidhi Research

Exhibit-6: Textile value chain of Voltas

Spinning	Weaving	Knitting	Processing & Finishing	Non-woven & Technical Textiles
Lakshmi Machine Works Ltd & Associates (India)	Lakshmi Automatic Loom Works (India)	Terrot GmbH (Germany)	Lakshmi Card Clothing Mfg. Co. Pvt. Ltd (India)	Brueckner Plant Technologies GmbH & Co Kg (Germany)
Kalpatharu Software Ltd (India)	Lakshmi Precision Tools Ltd (India)	Steiger SA (Switzerland)	Erbatech Textile Plant & Equipment GmbH (Germany)	Oskar Dilo Maschinen Fabrik Kg (Germany)
Kluber Lubrication (Germany)	Shandong Rifa Textile Machinery Co Ltd (China)	Klueber Lubrication (Germany)	Brueckner Textile Technologies GmbH & Co. Kg (Germany)	Hansa Industrie Mixer GmbH & Co Kg (Germany)
Adwaith Lakshmi Industries Ltd (India)		Memminger – IRO GmbH (Germany)	Reggiani (Italy)	
			Dunline Rubber Products Co (Canada)	
			Pleva GmbH (Germany)	
			Wumag GmbH (Germany)	
			Thies GmbH & Co Kg (Germany)	

Source: Company, Sunidhi Research

Construction and mining equipment

Construction and mining equipment is a US$2 bn market annually, and is expected to see a 16% CAGR over next few years

Construction and mining equipment is a US$2 bn market annually, and is expected to see a 16% CAGR over next few years. Voltas operates an agency business for products manufactured by Terex. As technology transforms the style and scale of the core sector surface mining industry, Voltas plays a vital role in making the latest and most efficient surface mining equipment available to Indian end users, especially for mining of coal, iron, copper, zinc and lignite. With growing investment in infrastructure development, Voltas is increasingly focusing on construction equipment, especially catering to the needs of road building. Hydro-electric projects and quarrying are also prime end-user industries. The scope, scale and impact of several recent milestones testify to Voltas' vital role in mechanizing and modernizing mining and construction in India. Management is of the view that the sector is heading into an up-cycle.

Exhibit-7: Voltas plays a vital role in making the latest and most efficient surface mining equipment

Source: Company, Sunidhi Research

Material handling (forklifts)

Revenue & profit of this segment will come down in FY12E due to transfer of Materials Handling Business effective 1st May 2011 to a Joint Venture with KION Group

Voltas supplies forklifts, cranes and warehousing equipment. In the forklift segment, Voltas and Godrej command a 70% market share while Ace commands the rest. The ‘cranes’ segment is very small for Voltas and it sells only 20-30 large cranes annually. Voltas now plans to sell cranes to power companies. The revenues and profits of the business will come down during FY12E arising from transfer of Materials Handling Business effective 1st May 2011 to a Joint Venture with KION Group. The transfer of Materials Handling business has resulted in a one-time inflow of ₹1100 mn in the year FY12E, and is subject to working capital and other related adjustments.

Unitary cooling products (UCP)

In its third business segment namely unitary cooling products (UCP) Voltas sells air conditioners and commercial refrigeration products. It is a key segment in terms of revenue growth driver as well as brand identity creation. The segment consists of two business divisions, a) room air conditioners which accounts for 75% of UCP segment revenues and b) commercial refrigeration accounting for the balance 25% revenues.

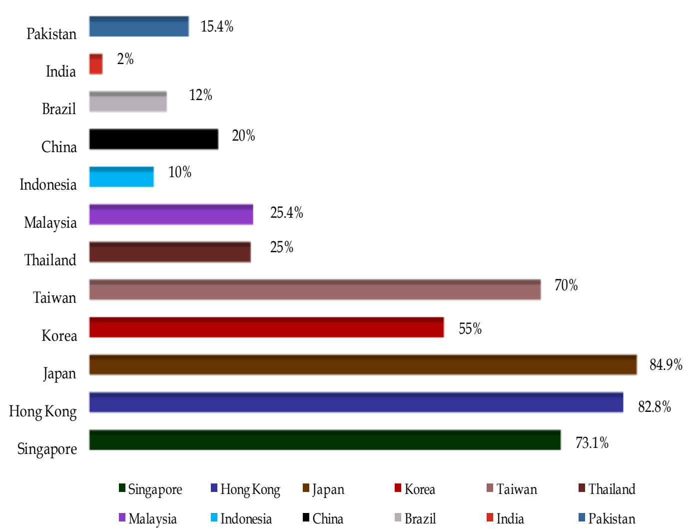
The ₹300 bn AC industry is expected to grow by 25% annually for next 6-7 years, Voltas having second highest market share (19% in FY11 after 28% of LG) will be a direct beneficiary

Air conditioning division

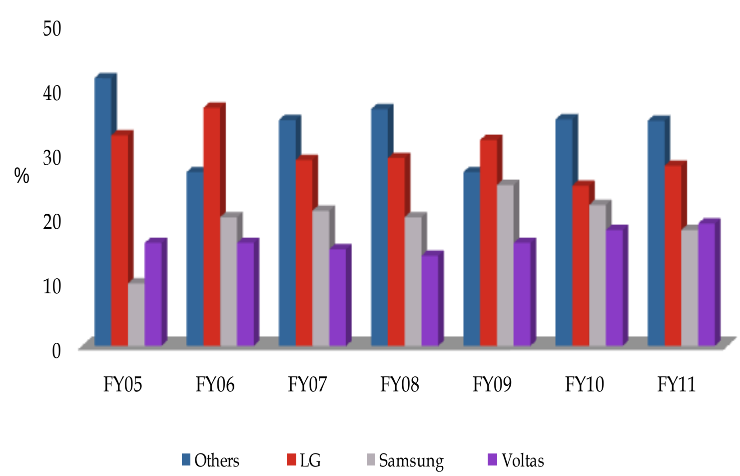
Indian air conditioning industry is witnessing phenomenal growth over the past few years mainly on account of very low AC penetration in India (only 2% compared to 20% in developed countries). With rising disposable income of people and growth in residential property units, the ₹300 bn AC industry is expected to grow by 25% annually for next 6-7 years. Voltas being a major player in the segment will be a direct beneficiary of this boom. Over the past few years, Voltas has maintained its market share in the UCP segment owing to its brand equity, distribution, and competitive pricing despite stiff competition from new entrants. Also, the company's early switch to star-rated products which are energy efficient, along with aggressive advertising, helped maintain market share. In the AC segment Voltas has the second highest market share of 19% (FY11) after LG (28%); Samsung is ranked number three with a 18% market share.

Exhibit-8: AC market in India witnessing phenomenal growth over past few years

Low penetration of AC in India vis-à-vis developed nations



Maintaining market share in AC despite stiff competition



Source: Company, Sunidhi Research

Commercial refrigeration division

This division accounts for 25% of UCP segment revenues and is witnessing significant growth for the last few years

Under commercial refrigeration division Voltas provides products like Deep Freezers, Chest Coolers, Visi Coolers, Water Coolers and Water Dispensers which are primarily used in commercial and retail establishments as well as office premises. This division accounts for 25% of UCP segment revenues and is witnessing significant growth for the last few years emanating from the retail boom in the country. The division grew by 46% and 37% yoy in FY10 and FY11 respectively and going forward we expect the commercial refrigeration division to grow at more than 35% CAGR driven by growing demand-supply gap and need for quality refrigeration infrastructure in user industries like retail, dairy, ice cream and brewery.

Voltas' manufacturing operations are in low cost regions of India enabling it to maintain a low cost and lean operating structure

Asset-light model with low operating cost

Voltas has a flexible asset-light business model with judicious mix of outsourcing and in house manufacturing thus helping it to maintain a low cost and lean operating structure. In FY05 Voltas relocated its manufacturing operation from Hyderabad (AP) to Pantnagar (Uttaranchal) and exited the domestic refrigerator segment as it could not keep pace with low-priced, frost-free offerings from foreign competitors. The company also undertook several cost-cutting measures such as introducing a VRS scheme for its workers in Hyderabad and implementing a judicious mix of outsourcing and in-house manufacturing to keep operating costs low. Voltas' manufacturing operations are in low cost regions of India, such as Dadra, Uttarakhand and Thane (Mumbai). Consequently its low cost operations with significant outsourcing have resulted in Voltas' improving RoCE profile.

Exhibit-9: Revenue and profitability of UCP business

Particulars (₹ mn)	FY06	FY07	FY08	FY09	FY10	FY11	FY12E	FY13E
Net Sales	4596	5957	8259	9223	11387	15608	18417	22653
EBIT	(337)	26	553	611	1226	1604	1599	2099
EBIT Margins (%)	(7.3)	0.4	6.7	6.6	10.8	10.3	8.7	9.3

Source: Company, Sunidhi Research

Exhibit-10: Voltas has the second highest market share (19%) in domestic AC market in FY11

Source: Company, Sunidhi Research

Indian commercial refrigeration industry is expected to grow at 35% annually over the next few years

Future growth of UCP business

The UCP segment contributed 30% of company's revenues in FY11 compared to 24% in FY10. The room air conditioner business accounts for 70% of this segment's revenue, while the remaining comes from commercial refrigeration. According to management, the Indian room conditioner industry is likely to grow at 25-30% annually over the next few years and the company is likely to grow more than the market rate in this segment. Similarly, as per management, the Indian commercial refrigeration industry is expected to grow at 35% annually over the next few years driven by,--

- growing need for cold chain solutions in Indian market
- demand-gap in user industries – retail, dairy, ice-cream, brewery
- need for quality infrastructure

We expect the UCP segment to show 25.8% sales CAGR (FY10-13E) with EBIT margin of 8.7% and 9.3% in FY12E and FY13E respectively

We expect strength in sales of unitary cooling products to continue, due to strong market growth led by low penetration of ACs in India and improving affordability of cooling products like ACs. Voltas's market share has also improved over the years due to successful branding efforts and introduction of star-rated products. The company is also improving its distribution reach by expanding its sales and service network from 3,700 dealers to over 4,600 dealers and setting up an organised retail vertical. **We expect the UCP segment to show 25.8% sales CAGR (FY10-13E) with EBIT margin of 8.7% and 9.3% in FY12E and FY13E respectively.**

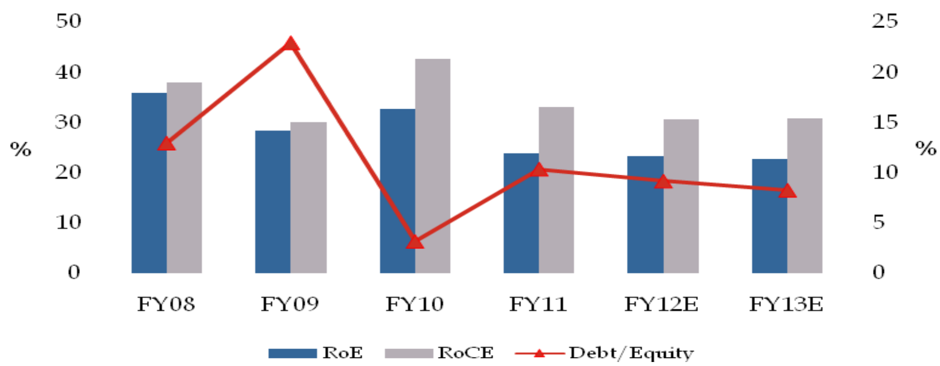
Financial Analysis

Voltas' strong emphasis on capital efficiency and cash generation resulted in high RoCEs over the years

High return ratios and capital efficiency

Voltas' low cost operations and asset light model with significant outsourcing have resulted in high return ratios (RoCE in excess of 33% in FY11). In the past management's careful selection of projects helped it avoid adverse impacts of the Dubai crisis. Taking lessons from the past Dubai crisis and recent turmoil in Libya and MENA region, management is now focusing more on government projects in the Middle East which have lower credit risk and lesser risk of cancellation. Moreover Voltas' strong emphasis on capital efficiency and cash generation resulted in high RoCEs over the years. As a result Voltas has been able to keep its leverage very low despite being a project company and has not diluted its equity in last five years.

Exhibit-11: High return ratios and low leverage



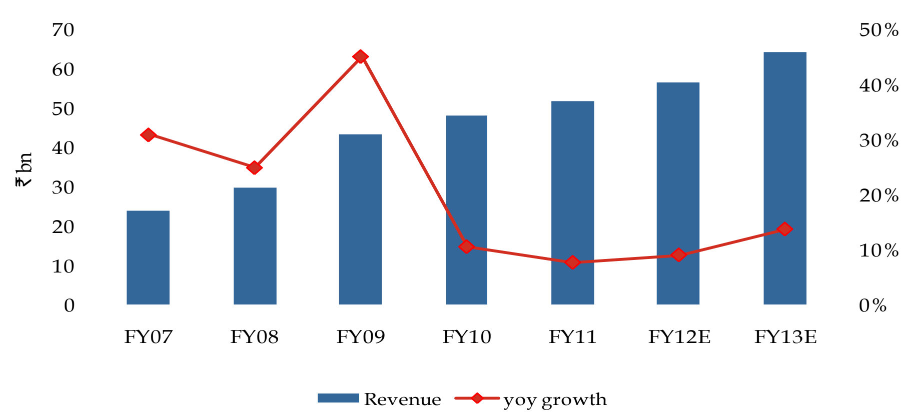
Source: Company, Sunidhi Research

Voltas has a consolidated order backlog of ₹48.9 bn at FY11 end, which is 0.9x FY11 sales

Revenues to grow at a CAGR of 10.6%

Voltas' revenue has grown at a CAGR of 23.9% over FY07-10, driven primarily by its EMP and UCP segments. The company has a consolidated order backlog of ₹48.9 bn at the end of FY11, which is 0.9x FY11 sales, thus providing revenue visibility for next 1 year. Going forward we expect middle east situation to improve and overall order intake to grow at a CAGR of 20.6% over FY10-13E. We expect Voltas to report 10.6% CAGR growth in revenues over FY10-FY13E. UCP segment is expected to lead the overall growth in revenues with 18% and 23% yoy growth in FY12E and FY13E respectively. While EMP segment will register yoy growth of 8% and 9% respectively for FY12E and FY13E. However we foresee a 6% de-growth in EPS segment for FY12E due to high base of FY11 (20.5% growth in FY11). The growth will again pick up by 12% yoy in FY13E.

Exhibit-12: Consolidated revenue growth over the years



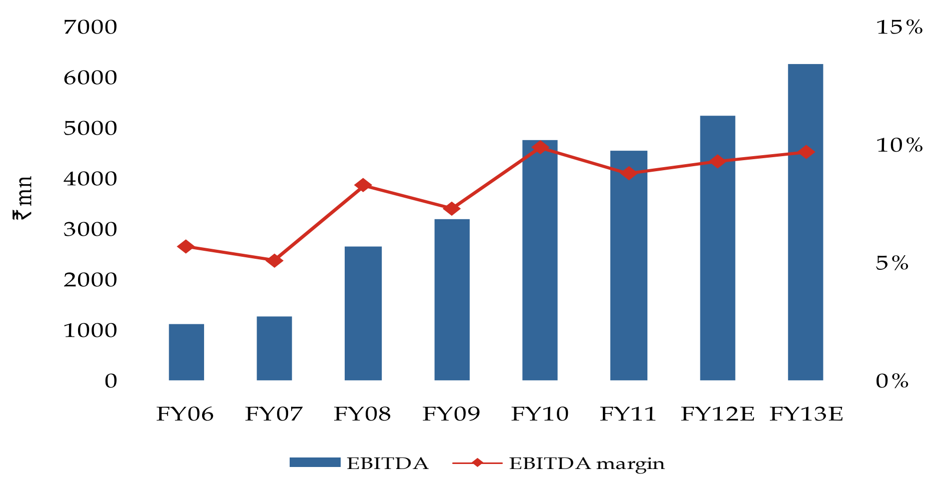
Source: Company, Sunidhi Research

Operating margins to improve by 50 bps

Our forecasted EBITDA for FY12E and FY13E stand at ₹5.2 bn and ₹6.3 bn thereby translating in to a margin of 9.3% and 9.7% respectively

Despite a moderate 10.6% sales growth in FY10, Voltas expanded its EBITDA margins by 260 bps mainly due to falling commodity prices and improved project execution. However with rise in commodity prices in the second half of FY11 and poor execution due to middle east problems, margins again saw a dip of 110 bps to 8.8% for FY11. We expect project execution to improve going forward, however given rising competitive intensity and high commodity prices we do not expect the margins to improve substantially and factored in a nominal 50 bps increase each over FY12E and FY13E to 9.3% and 9.7% respectively. Consequently, our forecasted EBITDA for FY12E and FY13E stand at ₹5.2 bn and ₹6.3 bn respectively.

Exhibit-13: EBITDA margin to witness moderate growth of 50bps yoy over FY12-13E



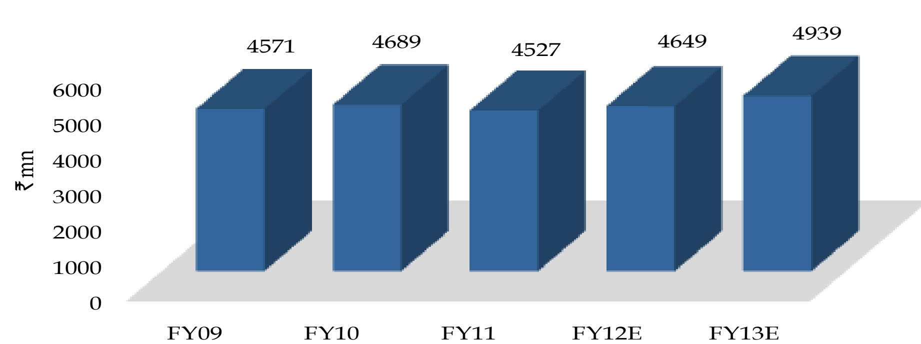
Source: Company, Sunidhi Research

High cash balance to help in inorganic growth through acquisition

Voltas has always been a net cash company with total cash & bank balances far exceeding total long term and short term borrowings

Voltas has always given highest priority to healthy cash flow generation over any other parameters while bidding for an order. It has always been a net cash company with total cash & bank balances far exceeding total long term and short term borrowings. Voltas has seen consistent rise in its cash balances (excluding investments) over the years. Its net cash position provides ample funds to facilitate future inorganic growth through acquisitions. We expect its cash balance to reach ₹4.9 bn in FY13E translating to ₹14.9 per share thus representing ~11% of its current market capitalization.

Exhibit-13: Cash and bank balance seen steady increase over the years



Source: Company, Sunidhi Research

Outlook and Valuation

We expect Voltas to report 10.6% CAGR growth in revenues over FY10-FY13E, and see its margins stabilizing around 9-10% level on the back of improved execution and order inflows

Future business outlook

Voltas is one of the few globally competitive services companies present in India, which have the capability and expertise to execute world-class projects. Over the years, Voltas has successfully changed its focus and direction based on macro conditions and continued to increase revenues and profits. We believe going forward Voltas will be a significant beneficiary of pick-up in domestic capex cycle. We expect Voltas to report 10.6% CAGR growth in revenues over FY10-FY13E, and see its margins stabilizing around 9-10% level on the back of improved execution and resumption of order flows from middle east region. Voltas remains the preferred player in the MEP and HVAC space and would continue to be a key beneficiary of industrial capex. The company is a net cash company having zero long-term debt, generates significant FCF every year and enjoys relatively high RoCE and RoE. We believe its operating parameters are likely to remain strong as the company has developed capabilities to execute large and complex projects across the world.

Exhibit-14: One year forward P/E Band

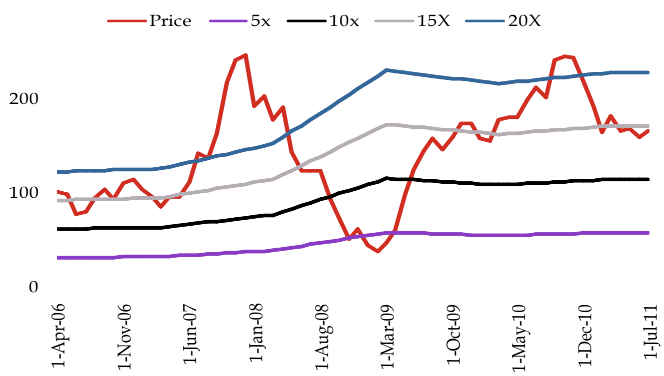
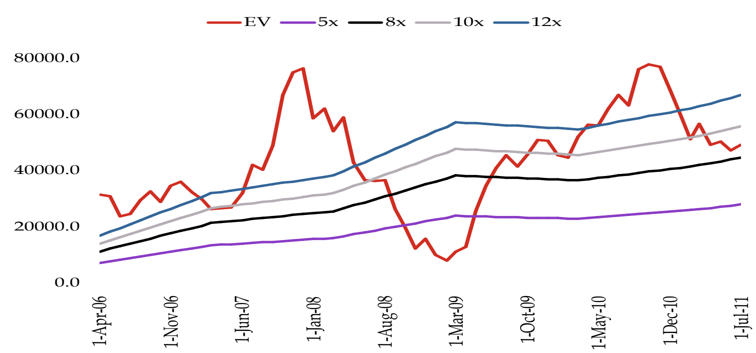


Exhibit-15: One year forward EV/EBITDA Band



Source: Capitaline, Sunidhi Research

We initiate coverage on Voltas with a 'Buy' rating and a price target of ₹200 based on FY13E target PE of 15x

Valuation and target price

Voltas has traded at its highest one year forward PE multiple of 41x during the market peak of Dec'07. The stock witnessed a severe correction to a PE of 3x one year forward EPS during the global recession in Mar'09. The average PE of last five years works out to 16.5x one year forward earnings. At CMP of ₹162, the stock is trading at 12.2x FY13E estimates. In our view, the stock is likely to be re-rated once the order inflows pick up in the next few quarters and the overall sentiment for infrastructure investment and industrial capex improves in the country. We initiate coverage on the stock with a 'Buy' rating and a price target of ₹200 based on conservative FY13E target PE of 15x, which is at a discount to its five year average one year forward multiple.

Exhibit-16: Peer Valuation

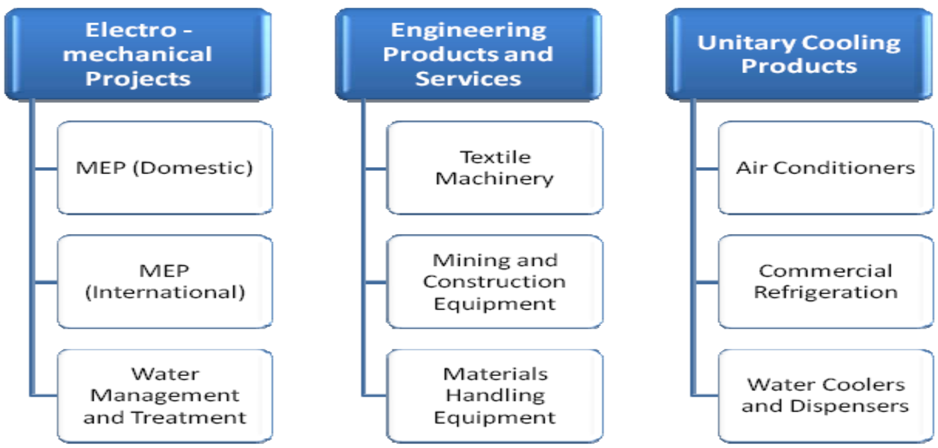
Company	Bloomberg Code	Share Price	P/E		EV/EBITDA	
		(₹)	FY12E	FY13E	FY12E	FY13E
ABB	ABB IN	867	49.0	35.8	31.6	22.8
Siemens	SIEM IN	914	30.8	25.8	19.2	16.0
Crompton	CRG IN	243	15.4	13.4	10.1	8.7
Areva T&D	ATD IN	246	24.4	18.0	12.6	10.2
Voltas	VOLT IN	157	13.8	11.8	8.8	7.2
Blue Star	BLSTR IN	314	13.9	11.7	10.2	8.7
Thermax	TMX IN	615	17.0	14.5	10.4	9.0
BHEL	BHEL IN	1948	13.9	12.3	8.9	8.0
L&T	LT IN	1796	21.1	17.9	13.3	11.4

Source: Bloomberg, Sunidhi Research

Company Background

Voltas, a Tata Group company incorporated in 1954, is one of the world's premier engineering solutions providers and project specialists. Voltas executes turnkey projects relating to mechanical, electrical, and public health (MEP) for both government as well as private customers in India and Middle East. Over the years Voltas has evolved from being a refrigeration and air-conditioning company into a full-fledged integrated MEP solutions provider. Voltas operates into three independent business specific clusters, electromechanical projects & services (EMP), engineering products & services (EPS) and unitary cooling products (UCP).

Exhibit-17: Business divisions of Voltas



Source: Company, Sunidhi Research

Electromechanical projects and services (EMP)

Voltas is India's largest provider and exporter of electromechanical projects & services, and covers infrastructure (airports, metros), real-estate (buildings, hospitals, hotels, IT parks) and industrial (power, cement, steel, paper and others) sectors. Voltas provides heating, ventilation, air conditioning as well as power systems, fire detection & protection, indoor air quality etc. Some of the recent projects executed in this segment are Formula 1 race track in Abu Dhabi, Burj Dubai, Rajiv Gandhi International Airport, Hyderabad and Chennai International Airport.

Over the years Voltas has evolved from being a refrigeration and air-conditioning company into a full-fledged integrated MEP solutions provider operating in three segments of EMP, EPS and UCP

Engineering products and services (EPS)

Voltas also has presence in engineering products and services segment catering to three specific industry verticals: (1) textile machinery, (2) mining & construction equipment and (3) material handling equipment. The engineering products are either self manufactured by Voltas, traded (imported and then sold) or sold by acting as an agent of Indian/foreign vendor. While working on agency basis, Voltas earns commission on sales where its scope of work includes installation, commissioning and maintenance of machineries and equipments.

Unitary cooling products (UCP)

The unitary cooling products segment is into designing, manufacturing and marketing of a range of air conditioners and commercial refrigeration products for household and institutional use. The various products manufactured by the company are air conditioners, deep freezers, water coolers, chest coolers, visi coolers and water dispensers. Voltas has grown the domestic market share of Air Conditioners steadily from 12% in the FY04 to 19% in year FY11 making it the second largest AC brand in terms of volumes.

Management Team

Managing Director

Mr Sanjay Johri
Mr. Johri has been the managing director of Voltas Ltd since 23 April 2010 and its president since 30 November 2009. He has also worked on various other leadership roles at Voltas. Prior to Voltas, Mr Johri has worked as general manager, accounts, of Havells India Ltd. He holds an M.A. and B.A (Hons) degrees.

President

Mr A. K. Joshi
Mr. Joshi serves as an executive vice-president and chief operating officer of EM&RBG of Voltas Ltd. He has also served as chief operating officer of AC & RBG, Mumbai of Voltas Ltd. Prior to that, he served as project engineer of Kirloskar
Pneumatic Co Ltd for four years. He holds B.E. (Mech.) degree.

CFO

Mr Anil George
He is responsible for the overall management and supervision of the finance functions. He serves as chief financial officer (CFO) of Voltas Ltd, and has recently replaced Mr. M. M. Miyajiwala who used to be Executive Vice President of finance and CFO.

CFO – Central F&C Services

Mr Utsav Shah
He is responsible for financial statements reporting and related financial activities of Voltas Ltd. He also represents the company in its quarterly investor conference calls.

General Manager – Corporate Communication & Investor Relations

Mr B. N. Garudachar
He is responsible for the overall corporate communication matters of Voltas Ltd, and is one point contact for investor relations.

Investment Concerns

Volatile commodity prices

Voltas is highly susceptible to volatility in commodity prices both in domestic as well as international markets, which could also arise from currency fluctuations. Any sharp increase in commodity prices could threaten its profitability as some of its international projects are of long-gestation periods and bound by fixed-price contracts. Voltas mitigates the risk of commodity prices by entering into contracts with its vendors soon after the contract win.

Volatile commodity prices, slowing order inflows in the middle east region and increase in competitive activity are some of the concerns

Slowing order inflows from middle east markets

Voltas generates ~37% of its revenues from Middle East markets and any slowdown in order intake from the Middle East region could threaten its revenue stream and consequently impact margins.

Increasing competition

Of late due to strong growth opportunity in the Indian and Middle East markets competitive intensity has increased as new players are entering the markets both in domestic and global arena. This could lead to increased pricing competition and market share erosion for Voltas.

Financials (consolidated)

Valuations Summary

Particulars	FY09	FY10	FY11	FY12E	FY13E
Revenues, ₹ mn	43617.2	48236.0	51913.7	56561.1	64388.9
EBITDA, ₹ mn	3189.1	4768.7	4553.8	5235.5	6262.8
PAT, ₹ mn	2514.0	3809.9	3572.4	3762.1	4392.3
Capital Employed, ₹ mn	9870.9	11343.5	14797.6	17684.6	21031.4
Gross Block, ₹ mn	3986.2	3889.8	4409.5	4794.2	5271.2
EPS, ₹	7.6	11.5	10.8	11.4	13.3
CEPS,₹	8.3	12.3	11.3	12.1	14.2
BVPS, ₹	23.9	32.8	40.1	48.6	58.4
P/E, x	20.7	13.6	14.5	13.8	11.8
P/BV, x	6.6	4.8	3.9	3.2	2.7
EV/EBITDA, x	14.9	9.5	10.2	8.8	7.2

Key Ratios

Particulars	FY09	FY10	FY11	FY12E	FY13E
EBIDTA %	7.3	9.9	8.8	9.3	9.7
PAT %	5.8	7.9	6.9	6.7	6.8
ROE %	28.5	32.8	23.9	23.4	22.8
ROCE %	30.2	42.9	33.2	30.8	31.0
D/E %	23.0	3.2	10.4	9.2	8.3

Growth Ratios

Particulars	FY09	FY10	FY11	FY12E	FY13E
Revenue growth %	35.1	10.6	7.6	9.0	13.8
EBITDA growth %	11.9	49.5	(4.5)	15.0	19.6
PAT growth %	22.6	51.6	(6.2)	5.3	16.8

Turnover Ratios

Particulars	FY09	FY10	FY11	FY12E	FY13E
Asset Turnover, x	4.4	4.3	3.5	3.2	3.1
Inventory Days	53	86	80	75	75
Debtors Days	67	74	77	85	82
Creditors days	104	150	135	120	115

Source: Company & Sunidhi Research

Consolidated Income Statement

March 31 Ending (₹ Mn)	FY09	FY10	FY11	FY12E	FY13E
Net Sales	**43617.2**	**48236.0**	**51913.7**	**56561.1**	**64388.9**
Growth (%)	*35.1*	*10.6*	*7.6*	*9.0*	*13.8*
Operating Expense	**40428.1**	**43467.3**	**47359.9**	**51325.5**	**58126.1**
Cost of Raw Materials	21925.0	21882.8	27973.6	30045.8	34083.2
Cost of Traded Goods	9760.3	11109.3	8834.1	9293.8	10272.7
Employee Expenses	4655.7	5356.9	5562.6	6216.7	7018.4
Other Expenditure	4087.1	5118.3	4989.6	5769.2	6751.8
EBITDA	**3189.1**	**4768.7**	**4553.8**	**5235.5**	**6262.8**
EBITDA Margin (%)	*7.3*	*9.9*	*8.8*	*9.3*	*9.7*
Interest	127.5	98.4	165.4	172.4	202.5
Depreciation & Amortization	209.6	214.1	210.2	225.5	252.8
EBT	**2852.0**	**4456.2**	**4178.2**	**4837.7**	**5807.5**
Other Income	603.9	611.5	664.4	702.5	680.6
Exceptional Items	261.3	250.2	401.9	-	-
PBT after Exceptional Items	**3717.2**	**5317.9**	**5244.5**	**5540.2**	**6488.1**
Tax	1171.8	1472.3	1728.7	1772.9	2050.2
PAT	**2545.4**	**3845.6**	**3515.8**	**3767.3**	**4437.9**
Minority Interest	28.9	35.7	(56.6)	5.2	45.6
Share of Profit/(Loss) in Associates	(2.5)	-	-	-	-
Net Profit after MI & Associates	**2514.0**	**3809.9**	**3572.4**	**3762.1**	**4392.3**
Net Profit Margin (%)	5.8	7.9	6.9	6.7	6.8

Source: Company & Sunidhi Research

Consolidated Balance Sheet

March 31 Ending (₹ Mn)	FY09	FY10	FY11E	FY12E	FY13E
Capital Employed	**9870.9**	**11343.5**	**14797.6**	**17684.6**	**21031.4**
Net Worth	**7897.5**	**10851.6**	**13277.4**	**16068.9**	**19296.5**
Equity Capital	330.7	330.7	330.7	330.7	330.7
Reserves & Surplus	7566.8	10520.9	12946.7	15738.2	18965.8
Total Debt	**1814.4**	**351.7**	**1380.0**	**1475.5**	**1594.7**
Deferred Tax Liability	**-**	**1.5**	**1.5**	**1.5**	**1.5**
Minority Interest	159.0	138.6	138.6	138.6	138.6
Total Assets	**9870.9**	**11343.5**	**14797.6**	**17684.6**	**21031.4**
Gross Block	3986.2	3889.8	4409.5	4794.2	5271.2
Depreciation & Amortization	1838.5	1821.1	1987.3	2212.8	2465.6
Net Block	**2147.7**	**2068.6**	**2422.2**	**2581.4**	**2805.7**
Capital WIP	132.4	193.4	35.0	67.0	85.0
Total Fixed Assets	**2280.1**	**2262.0**	**2457.2**	**2648.4**	**2890.7**
Goodwill on Consolidation	675.4	763.9	763.9	763.9	763.9
Investments	**1562.5**	**2339.4**	**2295.3**	**2457.0**	**3412.1**
Deferred Tax Assets	224.0	203.9	203.9	203.9	203.9
Current Assets	**27488.7**	**28267.4**	**30205.7**	**32851.9**	**36692.9**
Inventories	11193.9	11440.9	11224.1	11622.1	13230.6
Debtors	9520.9	10059.7	11704.8	13171.8	14465.5
Cash & Bank Balances	4570.5	4689.1	4526.8	4648.9	4939.4
Loans & Advances	2203.4	2077.7	2750.0	3409.2	4057.4
Current Liabilities & Provisions	**22359.6**	**22493.1**	**21128.4**	**21240.5**	**22932.0**
Liabilities	19742.8	19848.0	18483.3	18595.4	20286.9
Provisions	2616.9	2645.1	2645.1	2645.1	2645.1
Net Current Assets	**5129.0**	**5774.3**	**9077.3**	**11611.4**	**13760.8**

Source: Company & Sunidhi Research

Consolidated Cash flow Statement

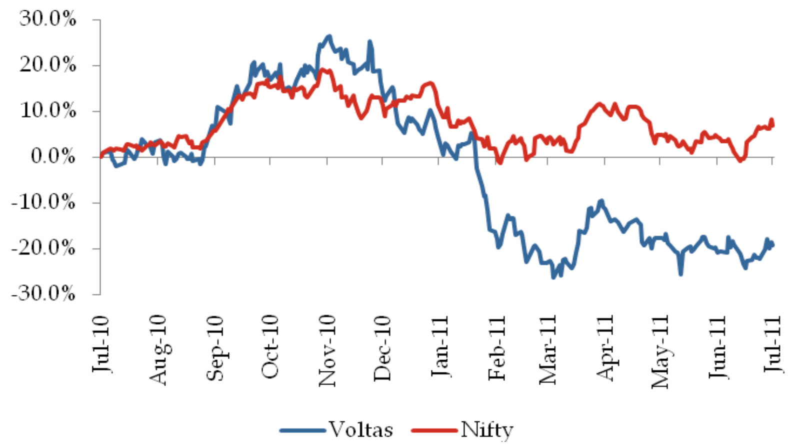
March 31 Ending (₹ Mn)	FY09	FY10	FY11E	FY12E	FY13E
Net profit before tax (PBT)	3717.2	5317.9	5244.5	5540.2	6488.1
Depreciation	209.6	214.1	210.2	225.5	252.8
Provision for doubtful debt & advances	412.1	(239.0)	-	-	-
(Profit)/loss on sale of assets	(355.2)	(141.2)	-	-	-
Interest (net)	(114.7)	(134.0)	165.4	172.4	202.5
Operating profit before WC changes	**3869.0**	**5017.9**	**5620.1**	**5938.0**	**6943.4**
(Increase)/decrease in sundry debtors	(3101.5)	(411.1)	(1645.1)	(1467.0)	(1293.7)
(Increase)/decrease in inventories	(4618.2)	(247.0)	216.8	(398.0)	(1608.5)
(Increase)/decrease in trade payables	4530.2	(442.2)	(1364.7)	112.1	1691.5
(Increase)/decrease in other CA	1358.3	752.6	(672.3)	(659.2)	(648.2)
Change in WC	**(1831.3)**	**(347.8)**	**(3465.3)**	**(2412.0)**	**(1858.9)**
Tax paid (net of refund)	1047.5	1610.7	1728.7	1772.9	2050.2
CF from operating activities	**990.2**	**3059.4**	**426.1**	**1753.1**	**3034.3**
Capital expenditure	(366.6)	33.1	(603.7)	(451.7)	(562.0)
Investments	1015.6	(797.6)	(75.9)	(131.8)	(933.7)
CF from investing activities	**649.0**	**(764.4)**	**(679.6)**	**(583.5)**	**(1495.7)**
Proceeds from share capital	0.2	-	-	-	-
Proceeds from debt	577.4	(1462.7)	1028.3	95.5	119.2
Interest paid	(128.7)	(98.9)	(165.4)	(172.4)	(202.5)
Dividend paid (including div. tax)	(519.5)	(614.9)	(771.7)	(970.6)	(1164.7)
CF from financing activities	**(70.5)**	**(2176.5)**	**91.2**	**(1047.5)**	**(1248.0)**
Net cash flow	**1568.7**	**118.5**	**(162.3)**	**122.1**	**290.6**
Opening cash balance	3001.8	4570.5	4689.1	4526.8	4648.9
Closing cash balance	4570.5	4689.1	4526.8	4648.9	4939.4

Source: Company & Sunidhi Research

Sunidhi Recommendation Scale

BUY	**Absolute Return >20%**
ACCUMULATE	**Absolute Return Between 10-20%**
HOLD	**Absolute Return Between 0-10%**
REDUCE	**Absolute Return 0 To Negative 10%**
SELL	**Absolute Return > Negative 10%**

Relative Price Performance



	1 Month	3 Months	6 Months	1 Year
Stock Return %	2.0	-9.1	-22.9	-19.3
Relative Return %	-0.4	-6.0	-18.7	-26.1

SUNIDHI SECURITIES & FINANCE LTD

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