



ENAM Securities
India Research

CMP: Rs 333
Target Price: Rs 375
Potential Upside: 13%
Absolute Rating: **HOLD**

Blue Star Ltd

Relative to sector: **Underperformer**

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Relative Performance



Source: Bloomberg, ENAM Research

Stock data

No. of shares : 90 mn
Market cap : Rs 30.0 bn
52 week high/low : Rs 554/ Rs 321
Avg. daily vol. (6mth) : 57,900 shares
Bloomberg code : BLSTR IB
Reuters code : BLUS.BO

Shareholding (%)

	Dec-10	QoQ chg
Promoters	40.1	(0.0)
FIs	6.7	0.2
MFs / UTI	8.9	0.4
Banks / FIs	2.1	(0.0)
Others	42.2	(0.6)

Financial summary (Standalone)

Y/E Mar	Sales (Rs mn)	PAT (Rs mn)	Consensus EPS* (Rs)	EPS (Rs)	Change YoY (%)	P/E (x)	RoE (%)	RoCE (%)	EV/EBITDA (x)	DPS (Rs)	P/ BV (x)
2010	25,250	1,844	-	20.5	8.1		43.0	55.8		9.0	
2011E	28,379	1,568	19.7	17.4	(15.0)	19.1	30.0	43.7	11.5	10.7	5.4
2012E	33,977	1,872	24.8	20.8	19.4	16.0	31.9	45.7	9.9	12.9	4.8
2013E	39,934	2,213	-	24.6	18.2	13.5	32.8	46.8	8.4	12.9	4.1

Source: *Consensus broker estimates, Company, ENAM estimates

PAIN IN MEP SEGMENT TO CONTINUE FOR 1-2 QTRS

We recently had an interaction with the management of Blue Star for a feel on its business prospects. Mgmt has indicated that the muted outlook for domestic MEP (Electro-mechanical Projects i.e., Centralized AC for Commercial Establishments) industry is likely to continue for a further 1-2 qtrs (in-line with our estimates). However, the mgmt is optimistic about strong growth prospects in cooling products, especially in Room AC which is expected to grow at 25%+ p.a. in medium term (in-line with our estimates). Given Blue Star will take time to benefit from the AC segment growth, as it looks to re-establish stronger mkt share, we maintain muted outlook on financials and a **HOLD** rating with a TP of Rs 375 – PE of 18x FY12E (upside of 13% from CMP).

MEP Segment (60-65% of EBIT)

- **Slow order inflow from the Commercial sector** – Order inflow and enquiries for bids have slowed down in the past few qtrs. Mgmt mentioned that visibility of fresh ordering in near term is muted (in-line with our estimates of slow ordering expected for next 1-2 qtrs) with only some top IT cos looking to set up new facilities. There has been no significant development from mid-sized IT players, Industrial sector (Rs 1 bn order inflow in 9MFY11 v/s expectation of Rs 2 bn), Retail or Real estate players (setting up IT parks/ SEZs).

Order Inflow

Rs bn	Order Inflow	YoY Growth (%)
1QFY11	6.2	(32.8)
2QFY11	4.9	(24.6)
3QFY11	5.1	(24.1)
4QFY11E	8.5	18.9

Source: Company, ENAM Research

- **Ordering of Metro rail projects could provide some relief** – Management expects fresh ordering from Chennai and Bangalore Metro projects (bids have been submitted). Also, bids are expected to be submitted for Kolkata and Hyderabad metro in the next 1-2 qtrs.

Slowing Avg. Execution

(%)	FY11	FY10
1Q	20.2	35.3
2Q	23.7	31.4
3Q	21.3	32.2

Source: Company, ENAM Research

Cooling Prod. Sales

(Rs bn)	FY11	FY10	Grth (%)
1Q	2.5	1.9	32.7
2Q	1.4	1.1	29.4
3Q	1.3	1.0	34.0

Source: Company, ENAM Research

- **Concerns over delay in execution** – Management has mentioned that out of the MEP projects being executed by Blue Star, ~50% are facing execution delays due to payment issues and client side delays (reflected in dip in avg. execution during 9MFY11). Our estimates are factoring in these delays, as we have assumed that only 82% of the avg. order book will see execution in FY12E v/s past run-rates of over 90%.
- **No current plans to foray into Middle East (ME) mkts** – Blue Star at present has no plans to enter the MEP market in ME, as they feel that ME is fairly competitive and would rather strengthen their presence in India. This is also reflective of Blue Star not entering this market and establishing a presence during the boom period.

Cooling Products segment (25-30% of EBIT)

- **Efforts to gain mkt share in Residential AC segment** - While over the last 4-5 yrs, Blue Star has gradually marginalized its presence in AC segment (current mkt share of less than 5%), management now expects growth in this segment to be robust (in-line with our estimates of 25%+ growth p.a. in medium term). Management is hopeful of 30%+ growth in volumes for Blue Star in FY12E.
- **Expects Room AC Pricing to be firm** – Management anticipates firm prices in Room AC market in the medium term and believes that strong growth in the sector will ensure players do not compromise on profitability for market share gain. Further, management mentioned that risk from cheaper Chinese imports is unlikely in medium term as Chinese companies are unlikely to be interested in significantly smaller Indian market v/s larger opportunity in China (Annual Industry volumes of ~2.5mn units p.a. (FY10) in India v/s opportunity in China of more than 15-20x size).

Outlook & Valuation

- We maintain that domestic MEP segment outlook will remain muted and take longer to recover. Given Blue Star will take time to benefit from AC segment growth, as it looks to re-establish stronger market share, we maintain muted outlook on financials in coming qtrs. **We have a HOLD rating on the stock with a TP of Rs 375 (upside of 13% from CMP).**
- **In the MEP and Room AC space, we prefer Voltas (Buy, TP of Rs 240 – valued at 18x FY12E PE - v/s CMP of Rs 158) to Blue Star as: (A)** Voltas' presence in MEP in other geographies, esp. in ME (~70% of OB) insulates it to a large extent from MEP slowdown in India v/s Blue Star (focused presence in India). **Also, it must be noted that Voltas has presence in UAE and Qatar in ME with no significant exposure to regions of current unrest (Libya and Egypt) (B)** Voltas is better placed to capitalize on the robust growth opportunity in Room AC mkt considering strong mkt share of 15%+ (v/s Blue Star's mkt sh of under 5%).

Financials of Voltas and Blue Star

(Rs bn)	Voltas			Blue Star		
	FY10	FY11E	FY12E	FY10	FY11E	FY12E
Sales	48.1	51.9	61.7	25.2	28.4	34.0
EBITDA	4.6	4.8	5.5	2.7	2.6	3.0
PAT	3.5	3.8	4.4	1.8	1.6	1.9
P/E (x)	15.1	13.9	11.9	16.3	19.1	16.0
PBV (x)	4.8	3.8	3.1	6.1	5.4	4.8

Source: Company, ENAM Research

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