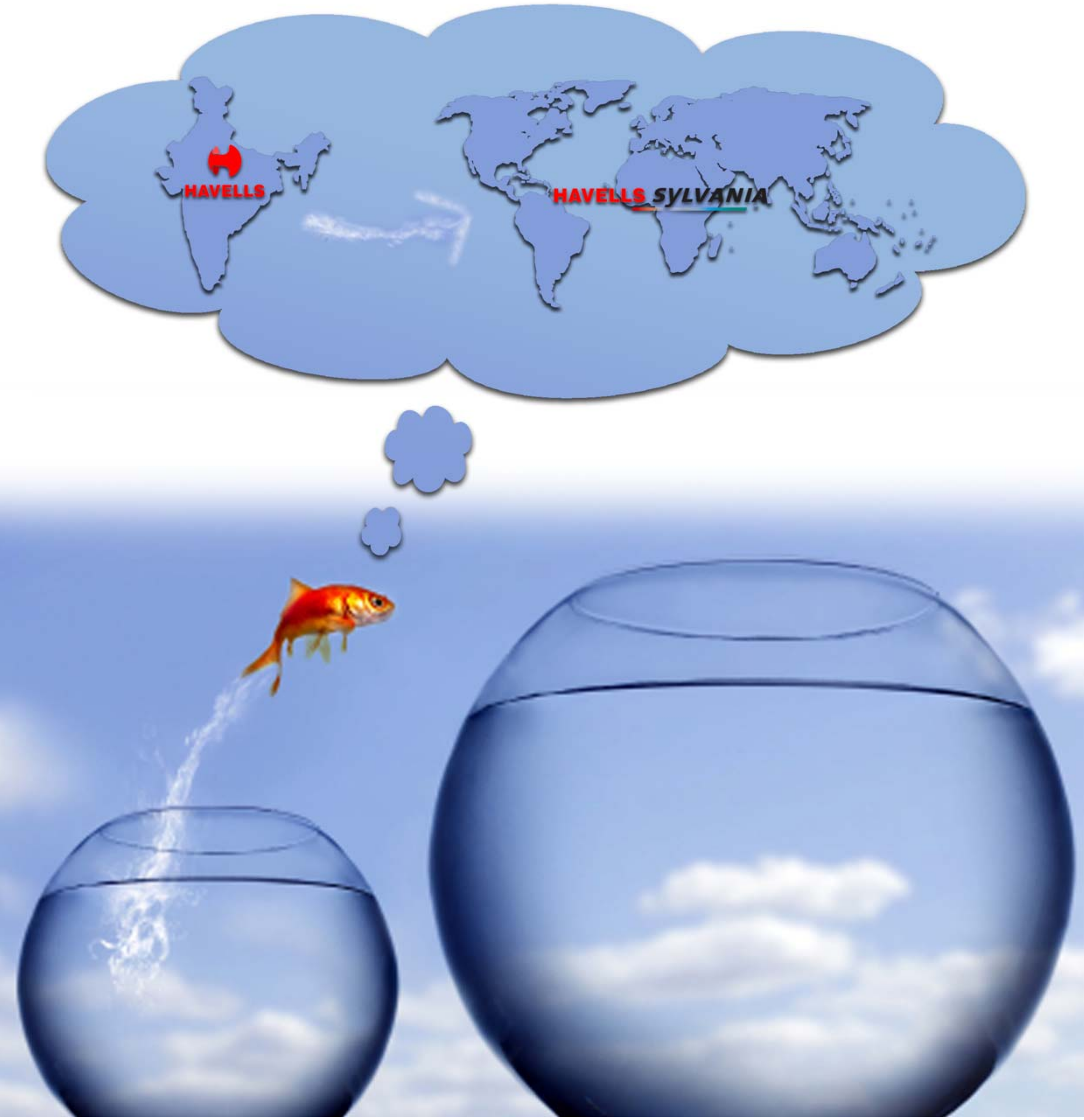
21 March 2011

Base Report | Sector: Engineering

Havells India



Thinking big

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Havells India: Thinking big

Page No.

HAVELLS

Havells India

Rs347 | Buy

BSE SENSEX	S&P CNX	BLOOMBERG	REUTERS
17,839	5,365	HAVL IN	HVEL.BO

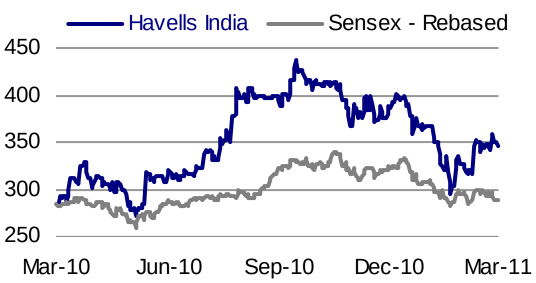
Y/E MARCH	2010	2011E	2012E	2013E
Net Sales (Rs b)	54.3	57.8	64.2	70.4
EBITDA (Rs b)	3.2	4.9	6.1	7.0
PAT * (Rs b)	0.7	2.5	3.4	4.2
EPS (Rs)*	5.6	20.1	27.3	33.7
EPS Growth (%)*	80.9	259.9	36.3	23.3
BV/Share (Rs)	32.1	49.2	71.3	99.2
P/E (x)*	62.1	17.2	12.7	10.3
P/BV (x)	10.8	7.0	4.9	3.5
EV/EBITDA (x)	16.2	11.0	8.5	6.9
EV/ Sales (x)	1.0	1.0	0.8	0.7
RoE (%)	17.4	40.7	38.3	34.0
RoCE (%)	7.5	18.2	21.7	22.9

* Consolidated

KEY FINANCIALS	
Shares Outstanding (m)	124.8
Market Cap. (Rs b)	44.7
Market Cap. (US$b)	1.0
Past 3 yrs. Sales Growth (%)	5.0
Past 3 yrs. PAT Growth (%)	15.9
Dividend Payout (%)	23.3
Dividend Yield (%)	1.1

STOCK DATA	
52-W High/Low Range (Rs)	447/264
Major Shareholders (as of December 2010)	**(%)**
Promoter	61.6
Domestic Institution	2.4
Foreign	16.3
Others	19.7
Average Daily Turnover	
Volume ('000 shares)	468.1
Value (Rs million)	286.2
1/6/12 Month Rel. Performance (%)	8/-4/21
1/6/12 Month Abs. Performance (%)	6/-13/22

STOCK PERFORMANCE (1 YEAR)



Thinking big

Turnaround of Sylvania and steady growth in domestic sales to drive 30% EPS CAGR over FY11-13

Havells India has emerged as a leading player in the Indian consumer electrical goods industry. After acquiring Sylvania, the company has strongly set its footprint in the lucrative European and Latin American markets. Expected turnaround of Sylvania and possible entry into newer segments in India will drive Havells' growth in the next few years. We expect Havells to deliver a consolidated EPS CAGR of 30% over FY11-13. The stock trades at attractive valuations of 17.2x FY11E and 12.7x FY12E earnings. We initiate coverage, with a Buy rating and a price target of Rs437.

Domestic business to maintain steady growth: Havells offers an impressive mix of consumer and industrial electrical products in India. While it is the market leader in the highly profitable low voltage switchgear segment, it also has cables and wires in its product portfolio, which provide significant volume growth. It is looking at aggressively expanding its consumer durables portfolio beyond its highly successful fans range. We expect standalone revenue to grow at a CAGR of 15% over FY11-13 after a healthy 19% growth in FY11. We expect standalone EBITDA margin to be maintained at ~11.8%, leading to an earnings CAGR of 18% over the next two years.

Sylvania to meaningfully contribute to earnings growth in FY12: After incurring substantial losses in FY09 due to a weak business environment in Europe, Havells' European subsidiary, Sylvania is likely to break even in FY11 and report a sharp jump in earnings in FY12. Restructuring of its European facilities coupled with strong growth in Latin American markets will significantly improve its profitability over the next few years. We expect Sylvania's EBITDA margin to increase to 5.4% in FY11 and to 7% in FY12 from 0.4% in FY10. Latin America and Asia will help drive revenue CAGR of 5% in FY11-13, even as Europe remains sluggish. We expect Sylvania to contribute ~21% to the group's consolidated PAT of Rs4.2b in FY13.

Expect acceleration in consolidated earnings; initiating coverage with Buy: We expect Havells to report consolidated earnings CAGR of 30% over FY11-13, on the back of sharp jump in profitability of Sylvania. Consolidated EBITDA margin should expand by 410bp over FY10-13. The stock trades at 17.2x FY11E and 12.7x FY12E EPS and at an EV of 8.8x FY12E EBITDA. We initiate coverage with a **Buy** rating and a price target of Rs437 on the basis of 16x FY12E consolidated earnings.

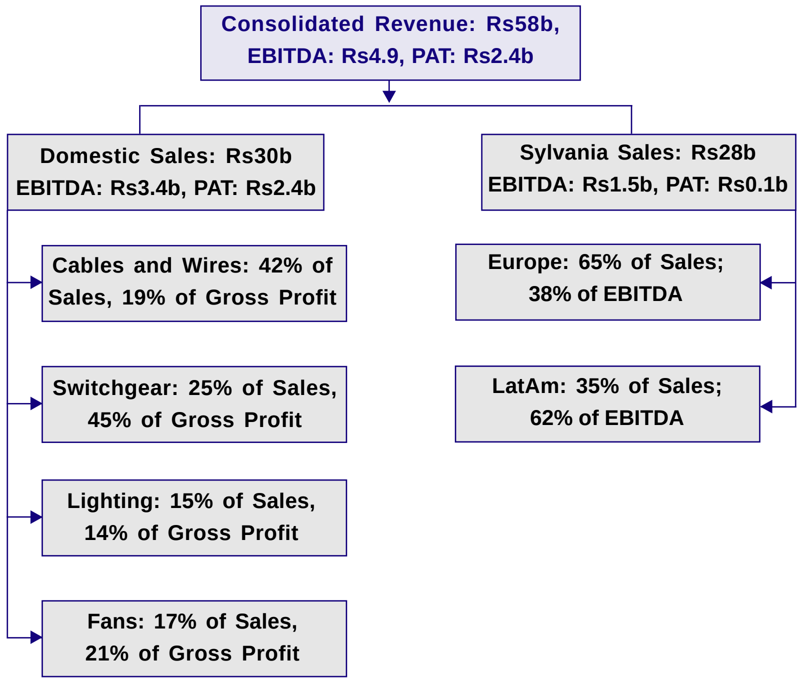
Indian MNC with global footprint in consumer electricals market

Havells India has emerged as a leading player in the power and consumer electrical goods industry. It has effectively used the inorganic route to expand its product and geographical coverage. After acquiring Sylvania, a strong European brand but thinly profitable, the company has set its footprint in the lucrative European and Latin American markets. Expected turnaround of Sylvania and possible entry into newer segments in India will drive Havells' growth in the next few years.

Lighting accounts for 2/3rd of consolidated sales, while switchgear accounts for 45% of gross profit

With turnaround of Sylvania in FY11, lighting will contribute meaningfully to consolidated profit

Well balanced business mix (FY11)



Source: Company/MOSL

Multiple drivers to sustain long-term growth

- **Domestic business:** Consumer spending, booming housing market and growing rural per capita income will keep demand for consumer electricals robust. Likely surge in the power distribution sector will also boost demand for cables and wires.
- **European and LatAm markets:** Sylvania will be the key vehicle to ride the expected demand boom in the Latin American markets. Cost competitiveness will drive the company's presence in the European region.
- **New products:** Havells intends to aggressively introduce new products in India. With growing spread across regions, Havells is well placed to outpace the competition.

Domestic business to maintain steady growth

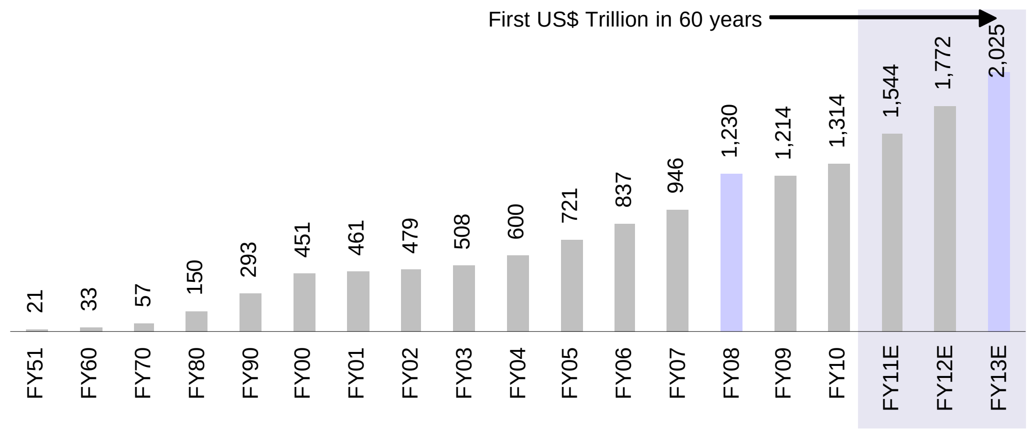
Havells offers an impressive mix of consumer and industrial electrical products in India. While it is the market leader in the highly profitable low and medium switchgear industry, it also has cables and wires in its product portfolio, which provide significant volume growth. It is looking at aggressively expanding its consumer durables portfolio beyond its highly successful fans range. Havells will be a direct beneficiary of the consumption boom in India due to its strong brand equity and nationwide distribution network. We expect standalone revenue to grow at a CAGR of 15% over FY11-13 after a healthy 19% growth in FY11.

Direct beneficiary of NTD opportunity

Havells a key beneficiary of growing per capita consumption in India; growing urbanization to further accelerate growth

It took India almost 60 years after independence to create its first trillion dollars of GDP. Growing at 13-15% per annum, it will add the next trillion dollars (NTD) in the next 6-7 years. This linear growth in GDP will drive up consumption across sectors. Havells will be a direct beneficiary of the construction boom and industrial capex in the country. Rising awareness and income levels of consumers across tier-II and tier-III cities will propel growth for all of Havells' products: (a) cables and wires, (b) electrical consumer durables, (c) lighting and fixtures, and (d) switchgear. Its strong brand equity and nationwide distribution network give it a competitive advantage.

India to add the next trillion dollars in GDP by FY13

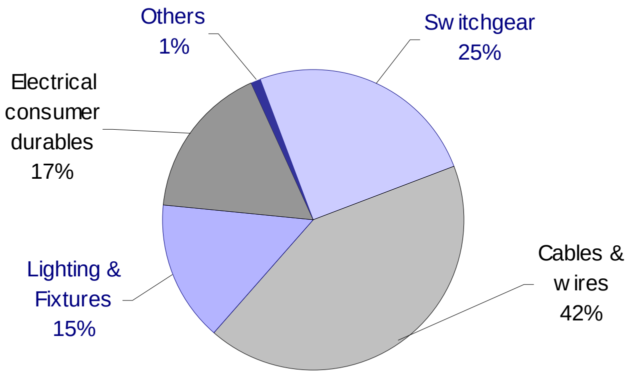


Source: Company/MOSL

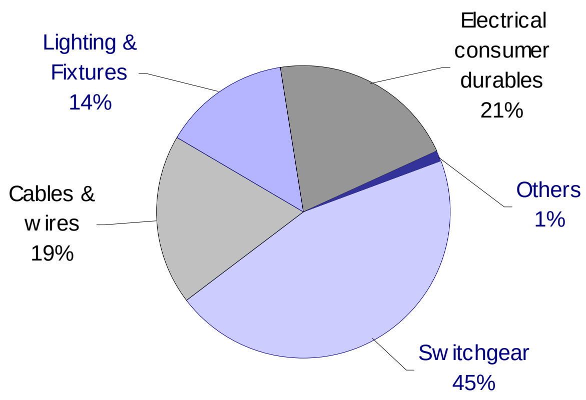
Diversified, growth-oriented product portfolio

Havells has a diversified product portfolio, with leadership across product ranges. Switchgear, which accounts for 45% of its EBIT, is its most profitable segment. Havells is a dominant player in the low voltage switchgear business. The cables and wires segment contributes the largest share of its revenue.

Cables and Wires contributes the largest share of revenue



Switchgear contributes 45% of gross profit



Source: Company/MOSL

Business segment analysis

Switchgear	Market Size	Domestic Switchgear - Rs12b
		Modular Switches - Rs10b
		Industrial Switchgear - Rs20b
	Market Share	~20% (15% in 2006)
	Competition	Legrand, Schneider
	Revenue	Rs7.2b
	EBIT	Rs2.61b
	EBIT Margin (%)	36.0
Electrical Consumer Durables	Market Size	Fans - Rs30b
		Electrical Water Heater - Rs8b
	Market Share	18%
	Competition	Crompton, Orient, Bajaj, Usha
	Revenue	Rs3.7b
	EBIT	Rs705m
	EBIT Margin (%)	18.8
Lighting & Fixtures	Market Size	CFL's - Rs12b
		Luminaries - Rs12b
	Market Share	CFL's- 10%
		Luminaires - 10%
	Competition	Philips, Osram, Bajaj, Wipro, Crompton
	Revenue	Rs3.7b
	EBIT	Rs705m
	EBIT Margin (%)	18.8
Cables & Wires	Market Size	Rs120b
	Market Share	~9% (6% in 2006)
	Competition	Polycab, KEI, Finolex
	Revenue	Rs11b
	EBIT	Rs90m
	EBIT Margin (%)	8.1

Source: Company/MOSL

Switchgear: Havells' most profitable segment

The Rs100b Indian switchgear market can be classified into low voltage (<1.1kV), medium voltage (1.1-36kV) and high voltage (>36 kV) sub-segments. Havells is a strong player in low voltage switchgear. It is India's largest manufacturer of MCBs (miniature circuit boards), mini MCBs, RCCBs (residual current circuit breakers), switches, sockets, regulators, rewirable switches, SDF (switch disconnector fuse), etc.

Havells is a strong player in domestic low-voltage switchgear industry, with nearly 20% market share

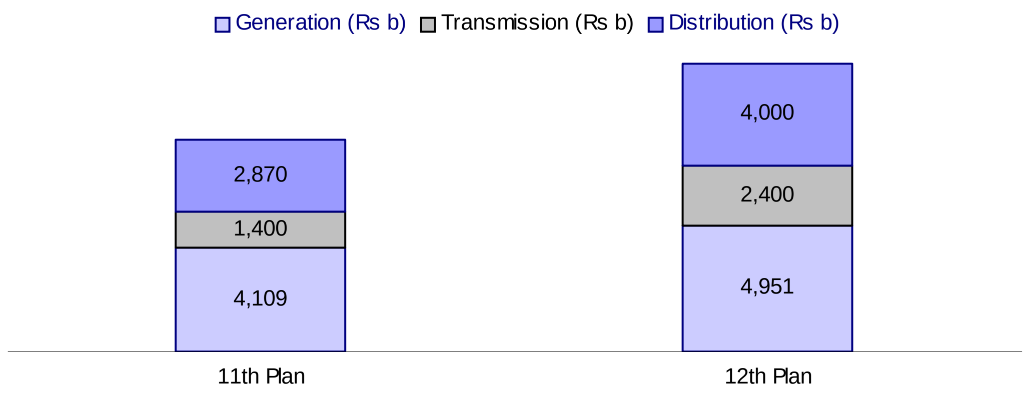
In this segment, Havell's mainly competes with multinationals like Legrand and Schneider. It currently commands a 20% market share, up from 15% in 2006. Since this market is dominated by organized players and the nature of the product is such that customers are willing to pay a premium for superior quality, there is pricing discipline. Limited competition and high-end positioning enable Havells to enjoy healthy margins in this segment.

Havells has the right to market the Crabtree brand (which mainly has high-end modular plate switches in its portfolio) in India. The modular switches market in India is worth Rs10b per year, and Havells' Crabtree brand generates annual revenue of Rs1.5b.

It is well placed to ride on consumption spend by both households and the government

The industrial switchgear market remains a direct beneficiary of government spend on power transmission and distribution under the XIth and XIIth plans, and capex in key industries like cement, metals, autos, etc. Havells has capabilities to handle voltage levels of 33kV and 66kV, and competes with large players like L&T, Siemens and Crompton. The company's presence in this segment is limited but it has the potential to grow meaningfully in the next few years.

Targeted spend of US$90b on distribution under XIIth plan augurs well for Havells

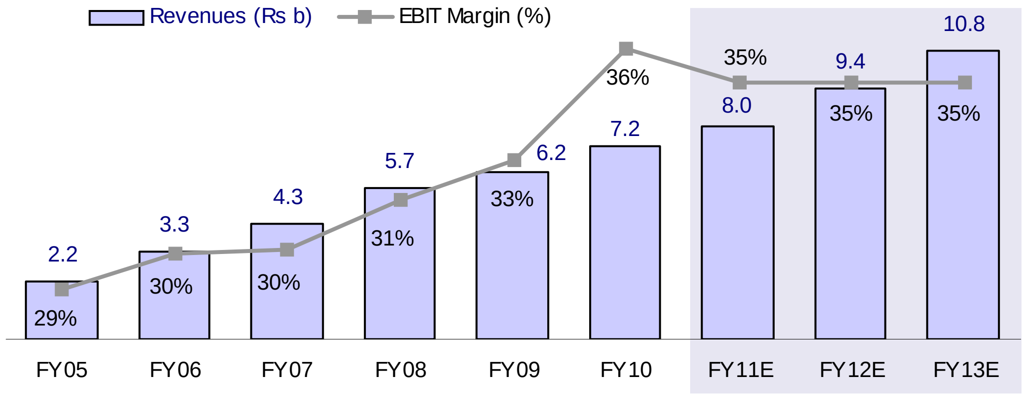


Source: Company/MOSL

Havells is launching its own switchgear products in UK, which is a significant step towards creating a market for its own switchgear brand in Europe

Havell's switchgear business revenue grew by a marginal 9% YoY in 9MFY11, due to cancellation of contract with a UK-based OEM to sell MCB (miniature circuit breaker) models in that country. The company's domestic switchgear sales grew strongly by 20% YoY, while exports declined by 50% during 9MFY11. We expect the share of exports to decline from 30% in FY10 to 14% in FY11. The company will launch its own products in UK under the Havells brand, using Sylvania's distribution channels. Given its brand and Sylvania's distribution strength, we expect exports to revive in FY12. We expect Havell's switchgear business revenue to grow at a CAGR of 16% over FY11-13, after a moderate 10% growth in FY11.

Switchgear: Expect revenue to grow at 16% CAGR; EBIT margin to be stable over FY11-13



Source: Company/MOSL

Cables and Wires: Least profitable, but integrates product offerings, aids brand recall

Cables and wires volumes are expected to grow at a CAGR of 8-10%

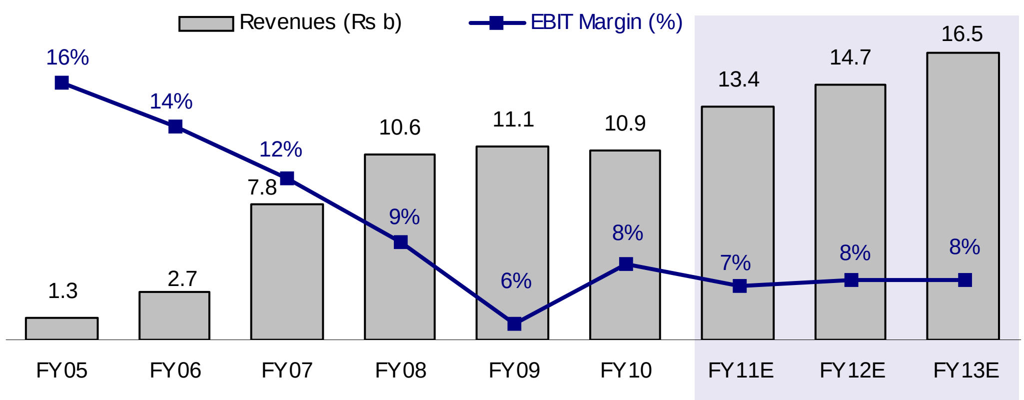
Havells is the second largest player in cables and wires, and enjoys a share of 9%. It manufactures a range of low and high voltage PVC and XLPE cables, coaxial TV and telephone cables and FR/FRLS wires. Its industrial cables can handle voltages of up to 66kV. In the cables and wires segment, Havells faces competition from players like Finolex, KEI and Polycab.

The business contributes only 20% of standalone profit, but provides access to distribution channels

Unlike switchgear, the cables and wires business is largely commoditized, with the presence of a large number of unorganized players. Being a low technology business, barriers to entry are low. The competitive environment can quickly turn negative in case of inventory pile-up in the industry, leading to price erosion and margin pressure. Also, there is always the inherent risk of copper price volatility - revenue growth and EBIT margin fluctuate significantly, driven by movement in input prices.

Havells' cables and wires business has grown at a CAGR of 53% over FY05-10. In 9MFY11, revenue grew 21% YoY, largely due to higher copper prices. Volume growth was just 7% YoY while realizations improved by 13-14%. We expect 8-10% volume growth over the next few years. In FY11, we expect this business to contribute 42% Havell's revenue and 19% to its gross profit.

Cables and Wires: Expect revenue to grow at 10% CAGR over FY11-13



Source: Company/MOSL

Lighting: Shift to CFL to light up growth

Havells' lighting segment sales of Rs3.7b included luminaires at Rs 2.2b and CFL at Rs1.4b

Havells' domestic lighting business (ex-Sylvania) generated revenue of Rs3.7b (Luminaires: Rs2.2b, CFL: Rs1.4b), with EBIT margin of 19% in FY10. The domestic lighting business contributes 15% of Havell's standalone revenue. Havells has a relatively premium positioning in the lighting products market. The bottom end of the pricing segment is dominated by products offered by unorganized players and Chinese imports.

Shift towards energy-saving lighting will help companies like Havells to grow at an accelerated pace over the next few years

The lighting industry in India has grown at a CAGR of 12.3% from Rs45b in CY05 to Rs72b in CY09. The compact fluorescent lamp (CFL) sub-segment has grown at more than double the rate of the industry at 28% CAGR over CY05-09. Favorable economics, low penetration (below 10%) of CFLs and increasing shift towards energy efficient lighting will enable this segment to sustain its growth momentum over the next five years.

India's lighting industry (Rs b): 12% CAGR over CY05-09

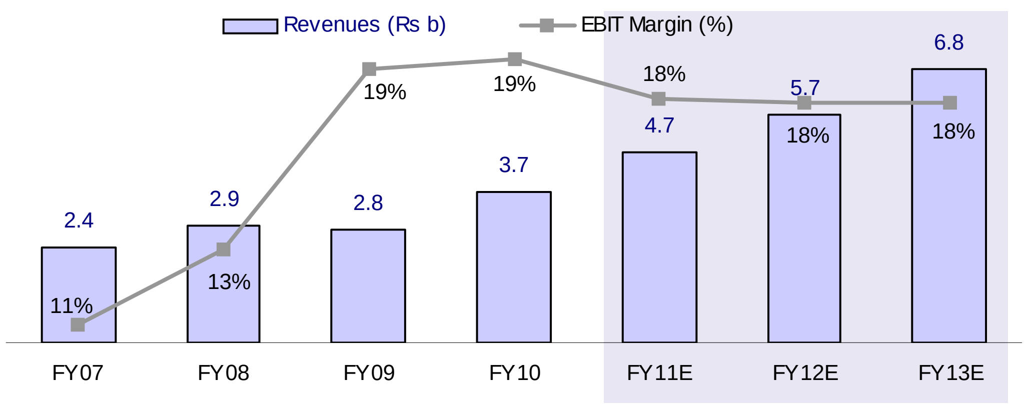
Industry Size	CY05	CY06	CY07	CY08	CY09	CAGR (%)
GLS Lamps	6	7	7	7	7	4.6
FTL	11	12	13	12	12	1.8
CFL	7	8	12	15	19	28.4
Special Lamps	4	4	6	6	5	7.3
Other Lamps	2	2	2	3	3	6.8
Luminaires	9	10	11	14	16	14.9
Control Gears & High Masts	2	2	2	4	4	17.8
Accessories	2	2	2	3	3	8.8
Components	2	2	3	3	3	14.4
Total	**45**	**50**	**58**	**66**	**72**	**12.3**

Source: ELCOMA

Havells is an aggressive player in the Indian lighting industry, commanding nearly 12% of CFL market and 10% in luminaires market

Havells has always been aggressive in the CFL market. It commands 10-12% share of the Rs12b organized market, making it the second largest player after Philips. In the Rs20b luminaires market, Havells has a market share of 10%, and competes with Philips and Bajaj Electricals. The company has a capacity to manufacture 55m pieces per annum (as at March 2010). Its manufacturing facilities are located at Neemrana (Rajasthan), which also cater to demand for lighting pieces from Sylvania.

Lighting: Expect revenue to grow at 20% CAGR over FY11-13



Source: Company/MOSL

Consumer durables: Expanding by entering new product categories

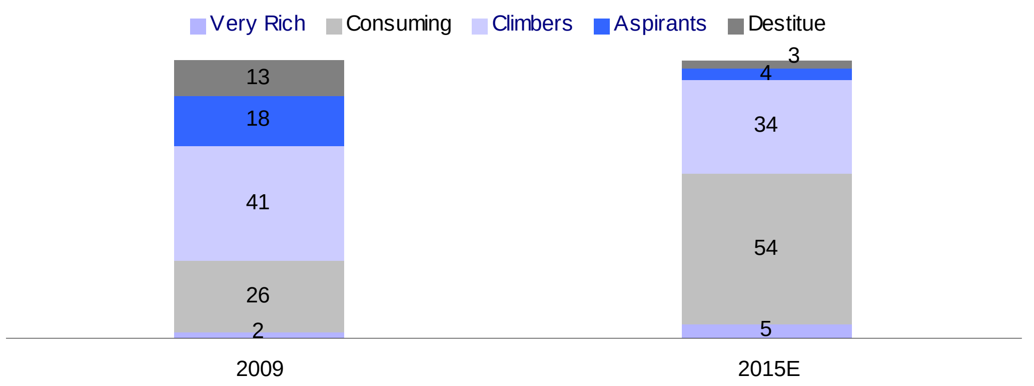
Havells has strong presence in the Indian fans market with 13% market share; focus on premium category provides superior returns

Until 2QFY11, Havells only had fans in its consumer durables portfolio. It enjoys 13% market share in fans, with competition mainly coming from Crompton Greaves, Orient Fans, Bajaj Electricals, Usha, etc. Havells has positioned its fans in the premium category. Its fan business EBIT margin was 28% in FY10. The lower end of the market remains intensely competitive, especially for table top and portable fans, and is dominated by unorganized players or Chinese imports. Low penetration of ceiling fans in rural areas and the construction boom in the urban areas will drive demand for the product.

Foray into new segments such as geysers (sales of Rs300m in FY11) and irons will aid growth

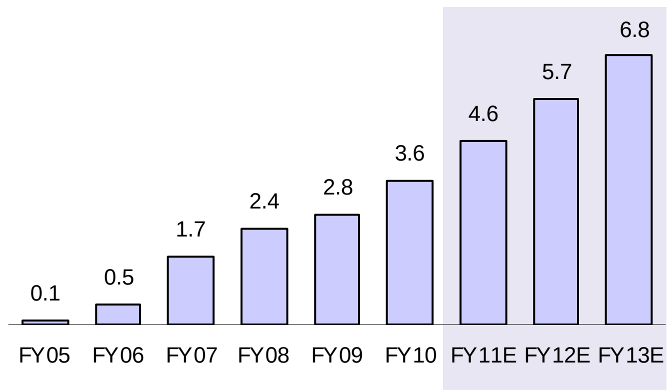
Havells intends to expand its consumer durables portfolio by including geysers and irons. It has already launched geysers in 2QFY11 and has been generating decent revenue. We expect geysers to contribute revenue of Rs400m in FY11, and grow at 35-40% over the next few years.

Consuming class to constitute 54% of the population by 2015, making the appliances market highly lucrative for incumbents

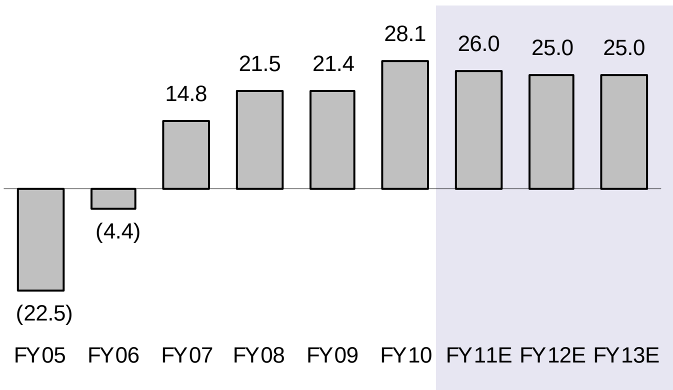


Source: Marketing WhiteBook

Consumer durables: Expect revenue to grow at 21% CAGR over FY11-13



Estimate long-term EBIT margin of 25%; entry into new segments may put pressure on margins



Source: Marketing White Book

Havells' consumer durables revenues have grown at a CAGR of 97% over FY05-10, making it the company's fastest growing business

Successful business strategy helping to maintain profitable growth

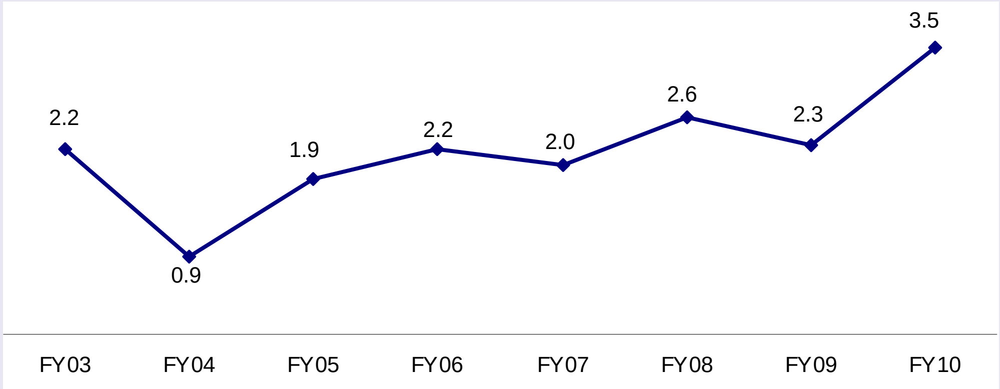
- **Strong market positioning through effective advertising and brand building:** Havells has been spending 2.5-3.5% of its annual revenue on advertising. It has launched successful brand building campaigns in the past five years, which have helped create strong brand equity. It is the market leader in switchgear and is amongst the top 3-4 in all the other product categories (cables, lighting and electrical durables).

Havells is amongst the top 3-4 players across segments

Segment	Mkt. Size (Rs b)	Mkt. Sh. (%)	Mkt.Position (Rank)	Competition
Cable & Wires	120	9	2	Polycab, KEI, Finolex
Domestic Switchgears	12	20	1	Legrand, Siemens, Schneider
Modular Switches	10	15	2	Anchor-Roma
Industrial Switchgears	20	8	4	L&T, Siemens, Schneider
CFL's	12	10	2	Philips, Osram
Fans	20	18	3	Crompton, Orient, Bajaj, Usha
Luminaries	20	10	4	Philips, Bajaj, Wipro, Crompton

Source: Company/MOSL

Spend on advertising (% of revenue)



Source: Company/MOSL

- **Strength of distribution:** Havells has a well entrenched distribution network, which is constantly expanding. It currently has 4,000 dealers in India, which will go up by 500 each year. It has also adopted a strategy of brand building by setting up its own stores used for exhibiting its portfolio of products across categories. These stores are called "Havells Galaxy". These stores are owned by dealers and Havells' investment is restricted to display of products. Currently, it has 80 such stores, which it intends to take up to over 200 by FY12.
- **Focus on manufacturing:** Unlike many competitors, Havells has kept manufacturing at the core of its business strategy. It manufactures ~90% of its sales in-house, which is starkly different from other leading players like Crompton Greaves, Bajaj Electricals, Orient, Phillips, etc. This helps the company to maintain product quality, and hence, good margins.
- **Innovative working capital management:** Havells has pioneered many ways to bring in cash by effectively managing working capital. It brought its receivables down to 12 days of sales in FY10 from 103 days in FY05. Net working capital reduced to 20 days of sales in FY10 from 147 days in FY05. This was achieved by bill discounting of receivables and channel financing. The company used channel financing effectively. It facilitated bank funding to its dealers and removed debt from its own books.

Sylvania to meaningfully contribute to earnings growth in FY12

Havells' European subsidiary, Sylvania is likely to break even in FY11 and report a sharp jump in earnings in FY12. Restructuring of its European facilities coupled with strong growth in Latin American markets will significantly improve its profitability over the next few years. Latin America and Asia will help drive revenue CAGR of 5% in FY11-13, even as Europe remains sluggish. We expect Sylvania to contribute ~21% to the group's consolidated PAT of Rs4.2b in FY13.

Successful turnaround led by effective business restructuring

Acquisition of Sylvania helped Havells set up distribution franchise and brand strength in Europe and other emerging markets in Asia and Latin America

In April 2007, Havells acquired majority stake in Sylvania from a private equity player at EUR227m, valuing Sylvania at an EV of 7.5x EBITDA. In CY06, Sylvania had reported revenue of EUR473m, with EBITDA margin of 6.4%. It is a 100-year old company and is ranked fourth globally in lighting and fixtures. The rationale behind the acquisition was to leverage Sylvania's established distribution franchise and brand strength in Europe to enter other emerging markets in Asia and Latin America. It also gave substantial product design capabilities and technology to Havells. The acquisition was entirely financed through debt of EUR200m, of which EUR80m was with recourse to Havells. There were also pension liabilities of EUR27m on Sylvania's books.

Sylvania's high cost structure and poor fixed cost absorption resulted in a loss of EUR47m in FY09

Post the acquisition in 2007, the global economy went into recession due to the financial crisis of 2008. The resultant contraction in housing demand across the EU and US impacted Sylvania's volumes. Its high cost structure restricted efficient fixed cost absorption, leading to losses at the EBITDA and the PAT level. In FY09, Sylvania's losses mounted to EUR47m. Havells had to revise the terms of the debt covenants wherein debt repayment was deferred till 2011 under a new agreement finalized in 2009. It issued 4.1m equity shares to Warbug Pincus at Rs625/share, aggregating to Rs2.6b, which it used to repay a bridge loan of EUR50m that it had taken for the acquisition. To regain profitability at Sylvania, Havells put together a two-phased restructuring plan, which helped to achieve cumulative savings of EUR40m per annum.

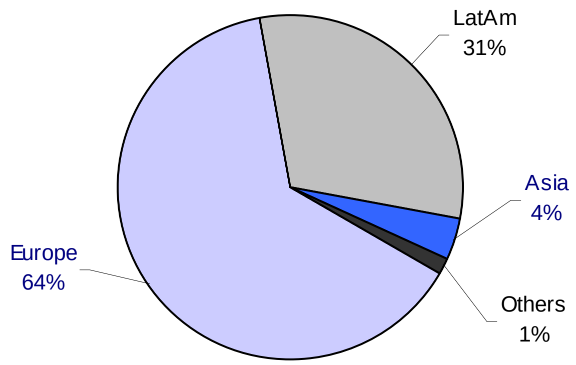
To regain profitability at Sylvania, Havells put together a two-phased restructuring plan, which helped to achieve cumulative savings of EUR40m per annum and brought about a turnaround in FY11

- **Phase-I (Phoenix):** This entailed cutting down on fixed costs within the company, mainly relating to manpower and factory expenses (8 warehouses, 3 plants and 1,300 staff). This resulted in manpower reduction and closure of plants in Europe and Latin America at a total one-time cost of EUR12m, with annual savings of EUR17m. This was implemented between January 2009 and September 2009.
- **Phase-II (Prakram):** This phase was implemented over September 2009 - December 2010, during which 400 people were laid-off. The process of catering to Sylvania's production requirements from China. The estimated cost of this exercise was EUR20m and it helped to achieve annual savings of EUR22m.

Latin America growing; Europe stabilizing

Havells has been aggressively focusing on growing its Latin America business. It has also begun focusing on expanding Sylvania's presence in the high growth markets of South East Asia. During 9MFY11, while Europe sales remained flat, Latin America/US/Asia grew 27% YoY. As a result the revenue share of Europe declined to 62% from 70% in 9MFY10.

Sylvania: Revenue break-up by geography (9MFY11)

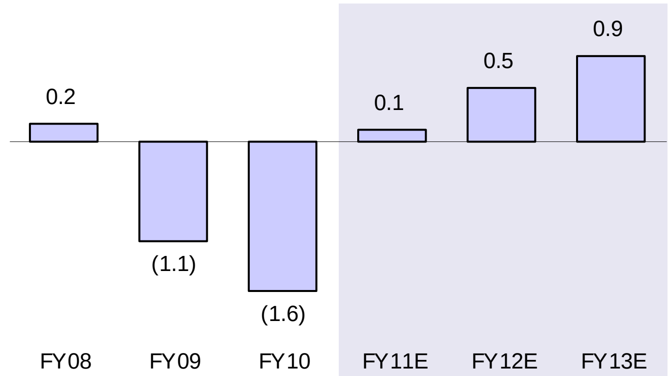


Source: Company/MOSL

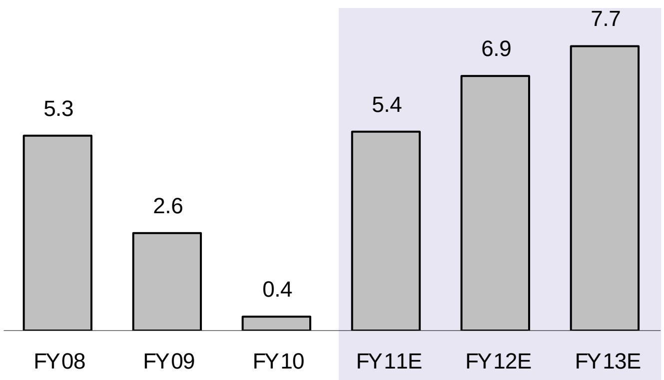
Expect margin-led earnings growth

We expect Sylvania's EBITDA margin to expand to 5.4% in FY11 and to 7% in FY13, led by revenue CAGR of 5% over FY11-13. Sylvania should contribute ~21% to the groups' consolidated PAT of Rs4.2b by FY13. It has broken even in 9MFYFY11 and is expected to report PAT of EUR2m in FY11, EUR9m in FY12 and EUR15m in FY13.

Sylvania to break even in FY11 (PAT, Rs b)



EBITDA margin to return to normative levels of 7-8%, as fixed costs go down and volumes go up

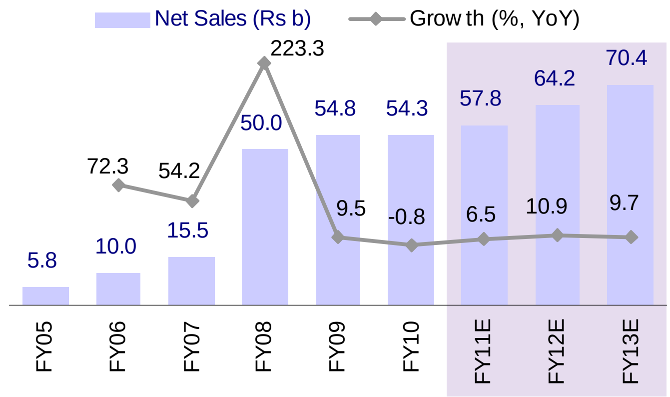


Source: Company/MOSL

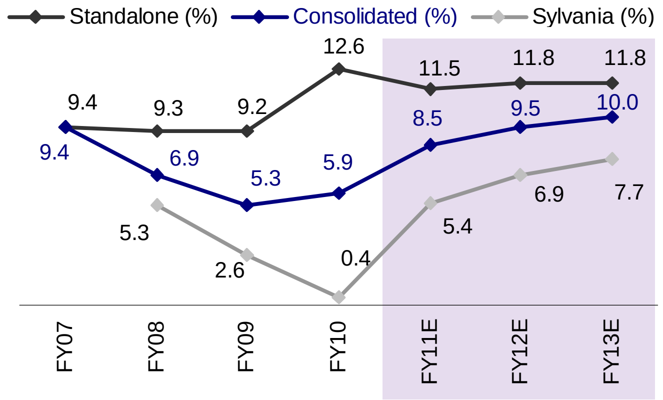
Expect acceleration in consolidated earnings

We expect Havells to report consolidated earnings CAGR of 30% over FY11-13, mainly driven by revenue CAGR of 10% and EBITDA margin expansion of 410bp over FY10-13. We estimate 730bp expansion in Sylvania's EBITDA margin from 0.4% in FY10 to 7.7% in FY13, led by revenue CAGR of 5% and cost cutting initiatives. Havells is likely to repay Rs2b in debt by FY13, mainly on the back of cumulative cash flows from operations adding up to Rs12b over FY11-13, leading to reduced interest outgo for the consolidated entity.

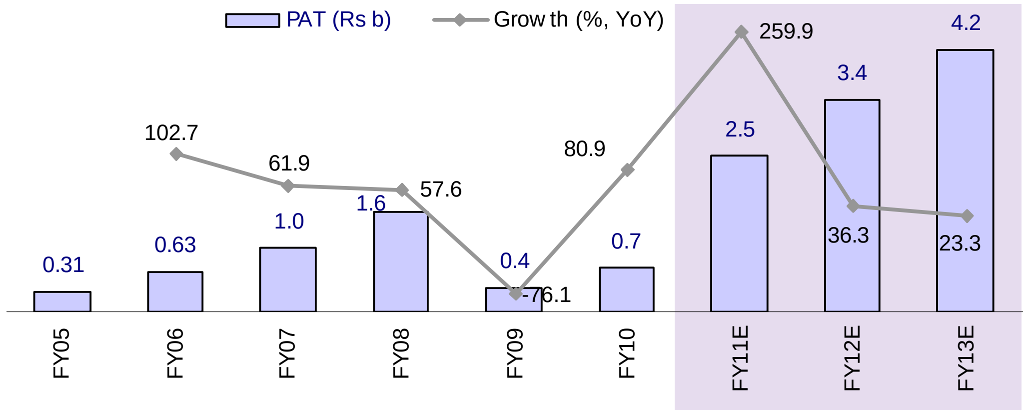
Expect consolidated revenue to grow at a CAGR of 10% over FY11-13



Expect the gap between standalone and consolidated operating margin to narrow



Expect consolidated PAT to grow at a CAGR of 30% over FY11-13



Source: Company/MOSL

Expect consolidated revenue CAGR of 10% over FY11-13

Revenue CAGR	(FY11-13)
Standalone	15%
Sylvania	5%

We expect consolidated revenue to grow at a CAGR of 10% over FY11-13. While Sylvania's revenue is likely to grow at 5% CAGR, standalone revenue should grow at 15% CAGR over FY11-13. Domestic sales will be driven by growth in electrical durables (21% CAGR, due to entry into new product segments like geysers, irons, electric motors, etc), lighting (20% CAGR) and switchgear (16% CAGR). We estimate standalone EBITDA margin to remain stable at 11.8%, despite volatile copper and aluminum prices.

Standalone revenue assumptions

(Rs m)	FY09	FY10	FY11E	FY12E	FY13E
Revenues					
Switchgear	6,234	7,244	7,969	9,403	10,814
Cables & wires	11,066	10,949	13,358	14,693	16,456
Lighting & Fixtures	2,805	3,743	4,717	5,660	6,792
Electrical consumer durables	2,769	3,625	4,640	5,660	6,793
Others	541	367	385	424	466
Total	**23,414**	**25,928**	**31,068**	**35,841**	**41,321**
Revenue Growth (%)					
Switchgear	9.7	16.2	10.0	18.0	15.0
Cables & wires	3.97	(1.1)	22.0	10.0	12.0
Lighting & Fixtures	(3.1)	33.5	26.0	20.0	20.0
Electrical consumer durables	**15.4**	**30.9**	**28.0**	**22.0**	**20.0**
Others	29.1	(32.1)	5.0	10.0	10.0
Total	**4.3**	**10.7**	**19.8**	**15.4**	**15.3**
EBIT Margin (%)					
Switchgear	32.6	36.0	35.0	35.0	35.0
Cables & wires	5.7	8.1	7.2	7.5	7.5
Lighting & Fixtures	18.5	18.8	17.6	17.5	17.5
Electrical consumer durables	21.4	28.1	26.0	25.0	25.0
Others	**15.8**	**18.4**	**17.0**	**15.0**	**15.0**

Source: Company/MOSL

Sylvania to break even in FY11

For Sylvania, we expect revenue to grow at 5% CAGR over FY11-13, mainly led by new geographies of Asia/Middle-East/Latin America. In 9MFY11, Sylvania recorded a revenue decline of 8% (in EUR terms), with EBITDA margin of 4.4% (+440bp YoY). For FY11, we estimate revenue growth of 8% in EUR terms (4% decline in INR terms), with EBITDA margin at 5% and PAT at Rs120m (EUR2m). For FY12, we estimate revenue growth of 6%, with margin of 7% (+240bp) and PAT of Rs550m (EUR9m). FY12 will see savings of EUR40m due to restructuring will start reflecting in Sylvania's EBITDA.

Sylvania returns to profitability in FY11

(Euro m)	FY09	FY10	FY11E	FY12E	FY13E
Net Sales	**508.6**	**438.4**	**472.0**	**501.9**	**518.7**
Growth (%)	8.9	-13.8	7.7	6.3	3.3
Raw Materials	247.9	213.1	222.5	237.0	240.9
% of Net Sales	48.7	48.6	47.1	47.2	46.4
Staff Cost	117.8	101.5	108.1	108.5	112.0
% of Net Sales	23.2	23.2	22.9	21.6	21.6
Other Expenses	129.5	122.1	116.1	121.8	125.8
% of Net Sales	25.5	27.9	24.6	24.3	24.2
Operating Expenses	495.3	436.7	446.6	467.3	478.6
EBITDA	**13.3**	**1.7**	**25.4**	**34.6**	**40.1**
EBITDA Margin (%)	2.6	0.4	5.4	6.9	7.7
Depriciation	11.3	9.0	9.2	9.5	9.6
EBIT	**2.1**	**-7.3**	**16.2**	**25.1**	**30.5**
Interest	15.5	12.8	13.7	11.9	9.5
Other Income	0.2	1.1	3.7	2.0	2.6
PBT	**-13.3**	**-18.9**	**6.2**	**15.2**	**23.7**
Tax	3.2	4.6	4.2	6.0	8.9
Tax (% of PBT)	-24.3	-24.3	67.9	39.7	37.7
Adj.PAT	**-16.5**	**-23.5**	**2.0**	**9.2**	**14.7**
EO Expenses	-31.0	-44.0	-2.0	-	-
Reported PAT	**-47.0**	**-67.0**	**0.5**	**9.1**	**14.7**

Source: Company/MOSL

Sylvania's debt position (Euro m)

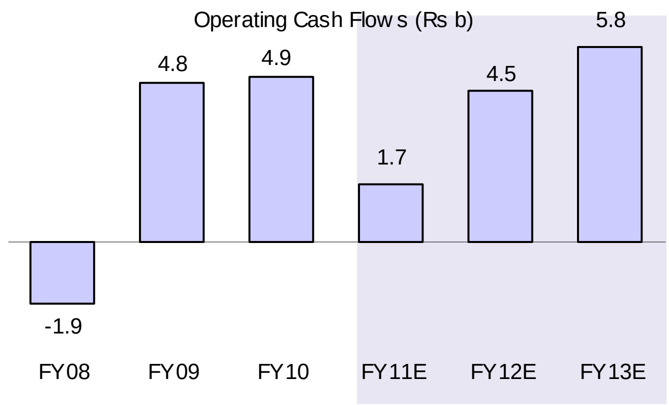
	FY09	1QFY10	2QFY10	3QFY10	4QFY10	1QFY11	2QFY11	3QFY11
With recourse to Havells	23	20	20	17	17	13	13	10
Without recourse to Havells	148	146	138	135	139	150	162	150
Total Debt	**172**	**166**	**158**	**151**	**156**	**164**	**175**	**160**
Less: Cash	13	17	11	13	13	8	13	13
Net Debt	**158**	**149**	**147**	**138**	**143**	**155**	**162**	**147**

Source: Company/MOSL

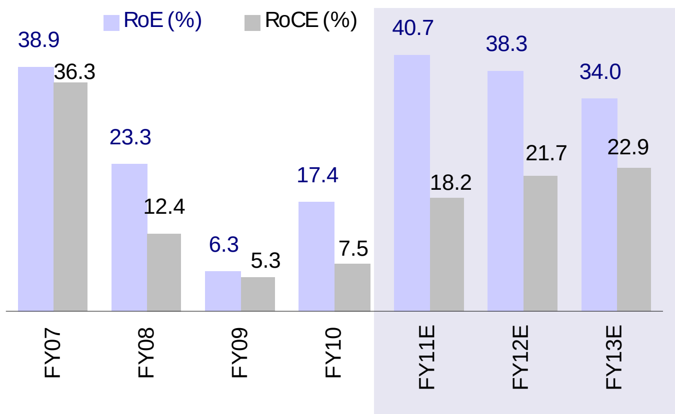
Expect operating cash flows of Rs12b over FY11-13

We expect operating cash flows of Rs12b over FY11-13, mainly led by strong revenue and margin performance in the India business, while Sylvania begins generating profits from FY11. We expect Havells to utilize the cash flows to repay debt of Rs2.6b. This should result in the gearing ratio declining from 2.7x in FY10 to 0.7x in FY13. As a result, we see RoCE going up from 7.5% in FY10 to 23% in FY13.

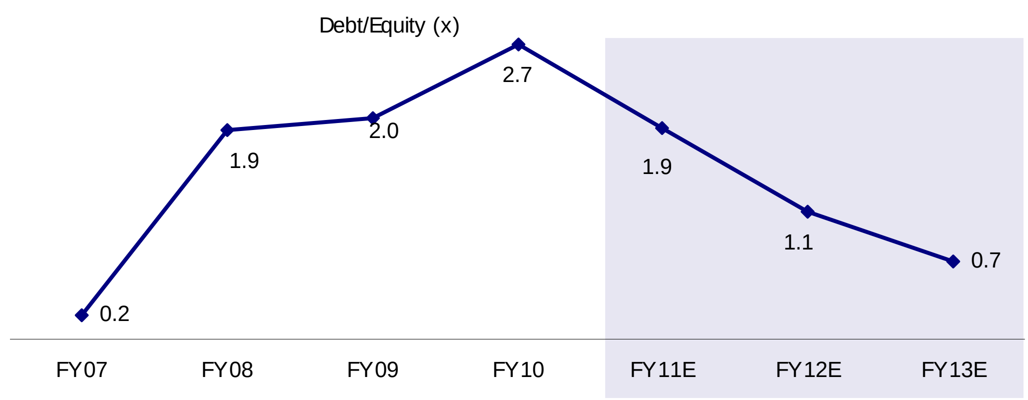
Expect cumulative cash flows of Rs12b over FY11-13



Return ratios to improve, following successful turnaround of Sylvania



Leverage to decline considerably, with increasing cash flows from operations



Source: Company/MOSL

Initiating coverage with Buy

The stock trades at 17.2x FY11E and 12.7x FY12E EPS and at an EV of 11.0x FY11E and 8.5x FY12E EBITDA. We initiate coverage with a Buy rating and a price target of Rs437 - 26% upside. To arrive at our target price, we have valued the consolidated business at 16x FY12E earnings (12% discount to our target P/E for Crompton Greaves).

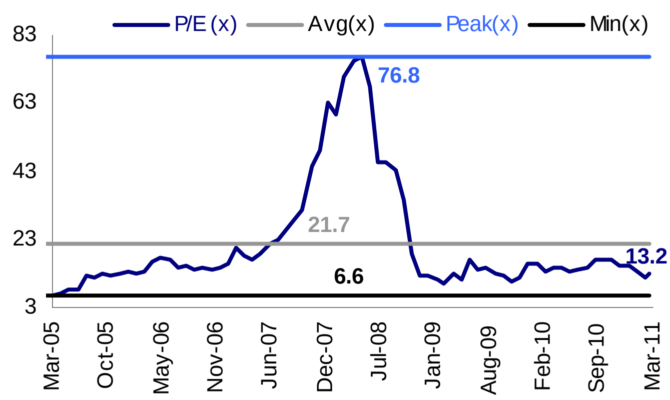
Comparative valuation

	Rating	CMP	EPS (Rs)			P/E (x)			EV/EBITDA (x)			RoE (%)		
		Rs/sh	FY11E	FY12E	FY13E	FY11E	FY12E	FY13E	FY11E	FY12E	FY13E	FY11E	FY12E	FY13E
ABB#	Neutral	742	3.0	18.5	24.7	248.8	40.0	30.0	101.5	25.4	18.6	2.6	14.8	17.1
BHEL	Buy	1,922	119.2	146.4	173.0	16.1	13.1	11.1	9.3	7.5	6.2	32.6	32.2	30.8
BGR Energy	Buy	437	43.0	49.0	61.4	10.2	8.9	7.1	5.5	4.4	3.8	36.9	31.3	29.9
Crompton	Neutral	265	14.4	17.3	20.4	18.5	15.3	13.0	12.3	10.0	6.2	45.5	43.2	24.8
Cummins	Buy	637	31.3	40.0	48.6	20.4	15.9	13.1	9.2	7.6	8.9	36.1	37.6	36.5
L&T	Buy	1,506	74.5	89.9	123.2	20.2	16.8	12.2	17.1	14.9	12.2	19.0	19.4	20.4
Siemens##	Buy	869	31.3	39.7	49.8	27.8	21.9	17.5	16.8	12.9	10.9	27.3	28.3	28.9
Thermax	Neutral	568	31.5	41.1	41.1	18.0	13.8	13.8	10.6	8.3	8.3	0.0	0.0	31.5
Havells	**Buy**	**346**	**20.1**	**27.3**	**33.7**	**17.2**	**12.7**	**10.3**	**11.0**	**8.5**	**6.9**	**40.7**	**38.3**	**34.0**

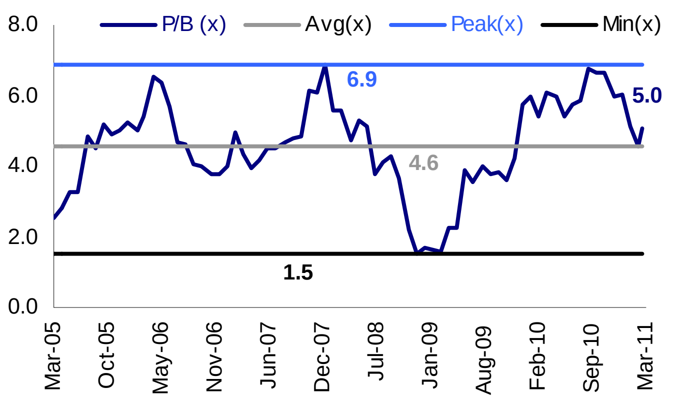
PER is based on FY12E; # Year end December; ## Year end September

Source: MOSL

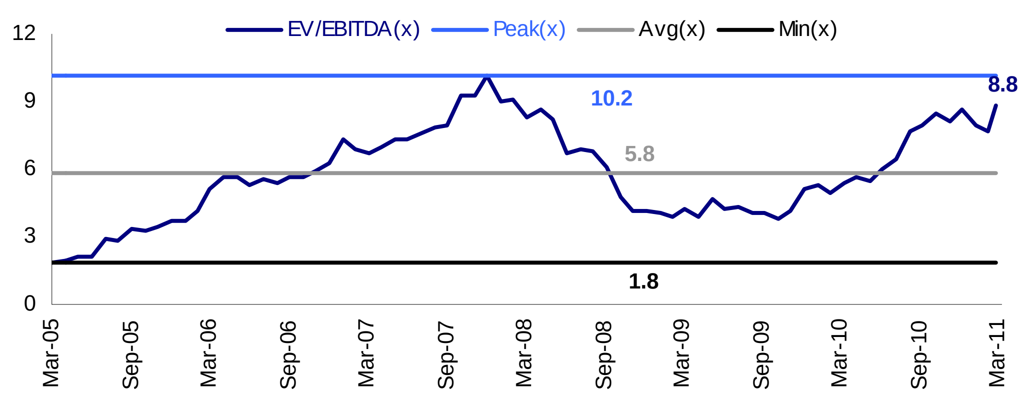
P/E band: Historical average of 21x



P/B band: Historical average of 4.6x



EV/EBITDA band: Historical average of 5.8x



Source: Company/MOSL

Key risks

Delays in turnaround of Sylvania: We expect Sylvania to turn around in FY11. We have assumed 6% revenue growth in FY12, mainly coming in from entry into newer markets in Asia and Latin America. Continued weakness in Europe, delay in turnaround of Sylvania and lack of initial success in Latin America could impact our estimates for the consolidated entity.

Rising domestic competition: Most of the segments where Havells is present are prone to price wars, especially cables and CFL, where there is considerable competition from the unorganized market. Besides, launch of new products like geysers, irons and motors might necessitate competitive pricing, which might impact near-term margins for the India business.

Increasing raw material prices: The wires business is sensitive to fluctuations in copper prices. Inventory piles up during a downturn, resulting in predatory pricing by the competition. In such a scenario, Havell's margins are adversely impacted.

Forex risk: Appreciation of other currencies against the EUR will impact earnings estimates for Sylvania due to its increased outsourcing to India and China. Also, appreciation of currencies in Latin America will pose a risk to Sylvania's earnings; the share of earnings from the Americas has risen from 26% in FY10 to 34% in 2QFY11.

Management background

Havells was founded by Mr Qimat Rai Gupta, who is its Chairman now, in 1971. Day-to-day management is handled by Mr Anil Gupta, Joint MD, who takes care of Sylvania and Marketing & Brand-building, Mr Surjit Gupta, Director - Operations, and Mr Rajesh Gupta, Director - Finance. The Board comprises of 10 members - five are independent and one is a nominee of Warbug Pincus. The promoter group is known as QRG Enterprises, and is owned by Mr Qimat Rai Gupta and family. As at September 2010, promoter holding in the company was 61.6%, while FII shareholding was 16.8% including 14% stake of Warbug Pincus.

Financials and valuation

Income Statement (Standalone) (Rs Million)

Y/E March	2008	2009	2010	2011E	2012E	2013E
Net Sales	**20,549**	**21,984**	**24,735**	**29,515**	**34,049**	**39,255**
Change (%)	32.8	7.0	12.5	19.3	15.4	15.3
Raw Materials	13,115	14,087	14,803	17,709	20,429	23,553
Staff Cost	744	881	797	1,033	1,192	1,374
Mfg. Expenses	1,343	1,291	1,704	2,066	2,281	2,630
Other Expenses	3,446	3,699	4,323	5,313	6,129	7,066
EBITDA	**1,902**	**2,025**	**3,108**	**3,394**	**4,018**	**4,632**
% of Net Sales	9.3	9.2	12.6	11.5	11.8	11.8
Depreciation	131	179	233	293	356	390
Interest	254	250	117	199	246	260
Other Income	145	76	145	153	160	168
PBT	**1,663**	**1,672**	**2,903**	**3,055**	**3,576**	**4,150**
Tax	227	220	622	672	715	830
Rate (%)	13.7	13.2	21.4	22.0	20.0	20.0
Adjusted PAT	**1,435**	**1,451**	**2,281**	**2,383**	**2,861**	**3,320**
Change (%)	40.5	1.1	57.2	4.4	20.1	16.1
Reported PAT	**1,435**	**1,451**	**2,281**	**2,383**	**2,861**	**3,320**
Change (%)	40.5	1.1	57.2	4.4	20.1	16.1

Balance Sheet (Standalone) (Rs Million)

Y/E March	2008	2009	2010	2011E	2012E	2013E
Share Capital	469	325	312	624	624	624
Reserves	6,201	9,018	11,040	12,527	14,731	17,321
Net Worth	**6,670**	**9,343**	**11,352**	**13,151**	**15,355**	**17,945**
Loans	358	703	1,158	1,758	1,858	1,958
Deffered Tax Liability	136	147	270	270	270	270
Capital Employed	**7,164**	**10,193**	**12,780**	**15,179**	**17,483**	**20,173**
Gross Fixed Assets	3,445	5,076	6,440	7,440	8,140	8,940
Less: Depreciation	426	579	724	1,017	1,373	1,763
Net Fixed Assets	**3,019**	**4,497**	**5,715**	**6,422**	**6,766**	**7,176**
Capital WIP	834	158	297	354	409	471
Investments	1,648	3,879	5,317	5,317	5,317	5,317
Curr. Assets	**6,403**	**5,332**	**5,613**	**8,978**	**11,192**	**14,281**
Inventory	4,303	2,075	3,307	4,043	4,664	5,377
Debtors	661	867	795	1,456	1,679	1,936
Cash & Bank Balance	649	1,574	683	2,599	3,929	6,008
Loans & Advances	761	736	731	760	780	800
Other Current Assets	29	79	98	120	140	160
Current Liab. & Prov.	**4,741**	**3,673**	**4,162**	**5,892**	**6,202**	**7,072**
Creditors	1,895	2,338	2,713	2,830	2,799	3,226
Other Liabilities	2,468	1,136	1,247	2,005	2,256	2,536
Provisions	378	200	201	1,056	1,147	1,310
Net Current Assets	**1,663**	**1,659**	**1,451**	**3,086**	**4,991**	**7,209**
Misc. Expenses	1	1	0	0	0	0
Application of Funds	**7,164**	**10,193**	**12,780**	**15,179**	**17,483**	**20,173**

E: MOSL Estimates; Standalone financials unless otherwise stated

Financials and valuation

Income Statement (Consolidated) (Rs Million)

Y/E March	2008	2009	2010	2011E	2012E	2013E
Net Sales	**50,022**	**54,775**	**54,315**	**57,834**	**64,163**	**70,378**
Change (%)	223.3	9.5	-0.8	6.5	10.9	9.7
Raw Materials	27,127	30,070	29,180	31,057	34,648	38,004
Staff Cost	7,631	8,477	7,645	7,518	7,700	8,093
Mfg. Expenses	2,799	2,666	3,250	3,181	3,529	3,871
Other Expenses	9,000	10,676	11,019	11,162	12,191	13,372
EBITDA	**3,466**	**2,886**	**3,222**	**4,916**	**6,095**	**7,038**
% of Net Sales	6.9	5.3	5.9	8.5	9.5	10.0
Depreciation	694	905	837	843	928	966
Interest	1,036	1,253	979	1,022	962	827
Other Income	250	86	222	377	283	325
PBT	**1,986**	**814**	**1,628**	**3,428**	**4,488**	**5,570**
Tax	377	429	932	926	1,077	1,365
Rate (%)	19.0	52.7	57.2	27.0	24.0	24.5
Adjusted PAT	**1,610**	**385**	**696**	**2,503**	**3,411**	**4,205**
Change (%)	57.6	-76.1	80.8	259.7	36.3	23.3
Extra-ordinary Inc.(net)	0	(1,986)	(2,935)	(90)	0	0
Reported PAT	**1,610**	**-1,601**	**-2,240**	**2,413**	**3,411**	**4,205**
Change (%)	57.6	-199.5	39.9	-207.7	41.4	23.3

Balance Sheet (Consolidated) (Rs Million)

Y/E March	2008	2009	2010	2011E	2012E	2013E
Share Capital	290	301	312	624	624	624
Reserves	6,613	5,845	3,690	5,519	8,273	11,748
Net Worth	**6,902**	**6,146**	**4,002**	**6,143**	**8,897**	**12,372**
Loans	12,962	12,278	10,664	11,694	10,194	8,694
Deffered Tax Liability	(76)	(97)	266	0	0	0
Minority Interest	0	2	2	2	2	2
Capital Employed	**19,789**	**18,328**	**14,934**	**17,838**	**19,092**	**21,067**
Gross Fixed Assets	27,262	28,961	26,963	28,663	29,863	31,063
Less: Depreciation	19,944	20,427	18,089	18,932	19,860	20,826
Net Fixed Assets	**7,318**	**8,534**	**8,874**	**9,731**	**10,003**	**10,237**
Capital WIP	1,005	308	336	578	642	704
Investments	32	0	0	0	0	0
Goodwill	3,346	3,579	3,212	2,891	2,602	2,342
Curr. Assets	**23,229**	**20,215**	**18,389**	**20,762**	**23,089**	**26,719**
Inventory	10,419	7,947	8,246	11,091	12,305	13,497
Debtors	8,227	7,573	6,982	7,130	7,911	8,677
Cash & Bank Balance	2,429	2,473	1,481	941	1,355	3,106
Loans & Advances	2,124	2,141	1,578	1,478	1,378	1,278
Other Current Assets	29	79	102	122	142	162
Current Liab. & Prov.	**15,142**	**14,308**	**15,876**	**16,123**	**17,243**	**18,934**
Creditors	5,821	5,795	6,147	6,338	7,032	7,713
Other Liabilities	8,831	8,139	9,408	9,262	9,618	10,536
Provisions	490	373	321	523	594	685
Net Current Assets	**8,087**	**5,907**	**2,512**	**4,639**	**5,846**	**7,785**
Misc. Expenses	1	1	0	0	0	0
Application of Funds	**19,789**	**18,328**	**14,934**	**17,838**	**19,092**	**21,067**

E: MOSL Estimates

Financials and valuation

Ratios (Consolidated)

Y/E March	2008	2009	2010	2011E	2012E	2013E
Basic (Rs)	**12.9**	**-12.8**	**-18.0**	**19.3**	**27.3**	**33.7**
Adjusted EPS	**12.9**	**3.1**	**5.6**	**20.1**	**27.3**	**33.7**
Growth (%)	57.6	-76.1	80.9	259.9	36.3	23.3
Cash EPS	18.5	10.3	12.3	26.8	34.8	41.4
Book Value	55.3	49.3	32.1	49.2	71.3	99.2
DPS	1.2	1.4	1.9	4.0	4.5	5.0
Payout (incl. Div. Tax.)	10.5	45.8	38.9	23.3	19.3	17.4
Valuation (x)						
P/E (consolidated)	26.8	112.3	62.1	17.2	12.7	10.3
Cash P/E	18.7	33.5	28.2	12.9	9.9	8.3
EV/EBITDA	15.5	18.4	16.2	11.0	8.5	6.9
EV/Sales	1.1	1.0	1.0	0.9	0.8	0.7
Price/Book Value	6.3	7.0	10.8	7.0	4.9	3.5
Dividend Yield (%)	0.3	0.4	0.5	1.2	1.3	1.4
Profitability Ratios (%)						
RoE	23.3	6.3	17.4	40.7	38.3	34.0
RoCE	12.4	5.3	7.5	18.2	21.7	22.9
Turnover Ratios						
Debtors (Days)	60	50	47	45	45	45
Inventory (Days)	76	53	55	70	70	70
Creditors. (Days)	42	39	41	40	40	40
Asset Turnover (x)	2.5	3.0	3.6	3.2	3.4	3.3
Leverage Ratio						
Debt/Equity (x)	1.9	2.0	2.7	1.9	1.1	0.7

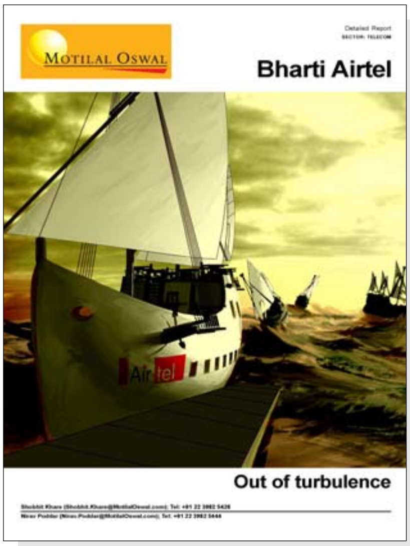
Cash Flow Statement (Consolidated) (Rs Million)

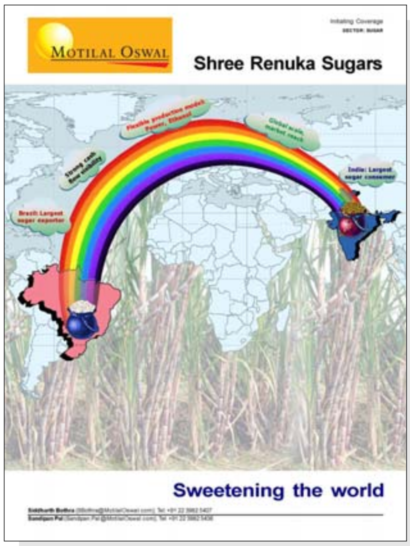
Y/E March	2008	2009	2010	2011E	2012E	2013E
PBT before EO Items	1,986	814	1,628	3,428	4,488	5,570
Add: Depreciation	694	905	837	843	928	966
Interest	1,036	1,253	979	1,022	962	827
Less: Direct Taxes Paid	377	429	932	926	1,077	1,365
(Inc)/Dec in WC	-5,195	2,224	2,403	-2,667	-794	-188
CF from Operations	**-1,855**	**4,767**	**4,915**	**1,700**	**4,507**	**5,811**
EO Income	0	-1,986	-2,935	-90	0	0
CF from Oper. incl. EO Items	**-1,855**	**2,781**	**1,979**	**1,610**	**4,507**	**5,811**
(Inc)/Dec in FA	-6,595	-1,424	-1,205	-1,942	-1,263	-1,262
(Pur)/Sale of Investments	0	32	0	0	0	0
CF from Investments	**-9,941**	**-1,625**	**-838**	**-1,621**	**-974**	**-1,002**
(Inc)/Dec in Net Worth	2,860	1,001	731	46	0	0
(Inc)/Dec in Debt	12,402	-684	-1,615	1,030	-1,500	-1,500
Less: Interest Paid	1,036	1,253	979	1,022	962	827
Dividend Paid	365	176	271	584	657	730
CF from Fin. Activity	**13,860**	**-1,112**	**-2,134**	**-530**	**-3,119**	**-3,057**
Inc/Dec of Cash	**2,064**	**44**	**-992**	**-541**	**414**	**1,752**
Add: Beginning Balance	365	2,429	2,473	1,481	941	1,355
Closing Balance	**2,429**	**2,473**	**1,481**	**941**	**1,355**	**3,106**

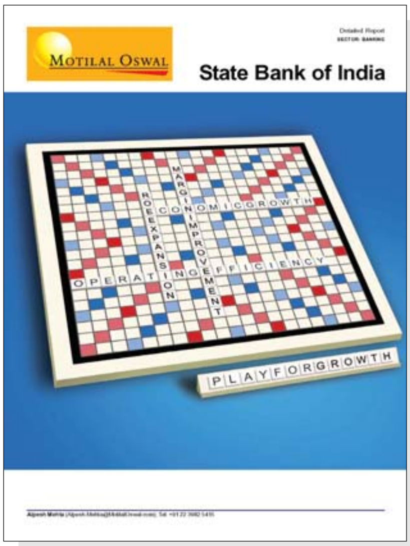
E: MOSL Estimates

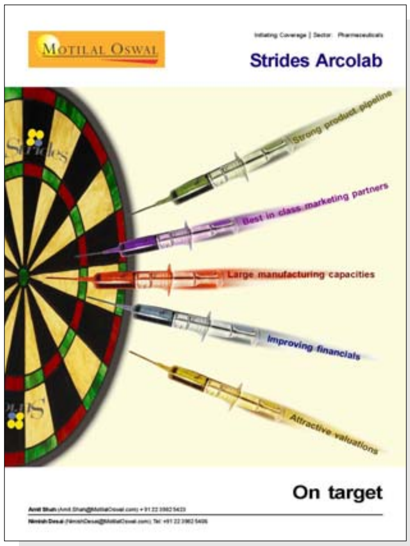
NOTES

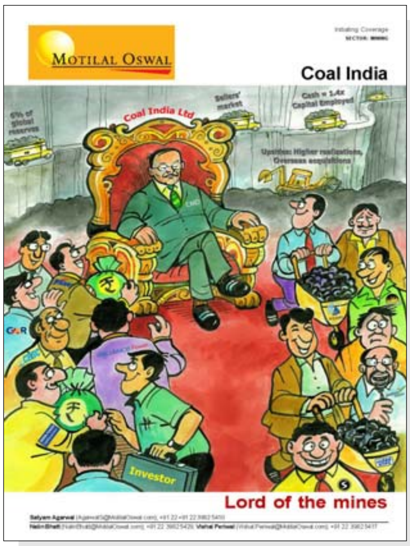
Motilal Oswal Company Gallery











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Disclosure of Interest Statement	Havells India
1. Analyst ownership of the stock	No
2. Group/Directors ownership of the stock	No
3. Broking relationship with company covered	No
4. Investment Banking relationship with company covered	No