

**Acquisition Details**

|                      |                                    |
|----------------------|------------------------------------|
| Company acquired     | SLI Sylvania (Germany)             |
| Enterprise value     | Euro 227 mn (Rs 13.3 bn)           |
| Total debt raised    | Euro 200 mn (Rs 11.7 bn)           |
| Convertible debt     | Euro 50 mn (Rs 2.9 bn)             |
| Conversion Period    | 18 months (Q2/Q3FY09)              |
| Equity post dilution | Rs 302 mn (12% dilution at Rs 447) |

**Background:** Havell's India Ltd is India's leading electrical goods manufacturers with presence across product categories like wires & cables, switchgear & CFLs. It is expanding its portfolio to include motors & capacitors. The company's expansion plans over the years has successfully enabled it to capitalise on the growing demand for electrical products arising from upsurge in activity in commercial & residential segments of the construction sector.

**Investment Highlights:**

- Havell's India Ltd (HIL) acquired Germany-based *SLI Sylvania (SLI)* for an enterprise value of Euro 227 mn.
- *SLI Sylvania* was originally a *General Telephone & Electronics (US)* group company. In 1993, *GTE* sold the North American operations to *OSRAM* division of *Siemens*. Upon restructuring of the Siemens group, *SLI's* ownership has been with financial investors.
- Upon the acquisition, HIL will get access to *Sylvania's* brands, which include *Sylvania, Concord:marlin, Lumiance, SLI Lighting, Zenith and Linolite*.
- The acquisition will be routed through a 100% SPV i.e. *Havell's Netherlands BV* at an enterprise value of Euro 227 mn. *SLI* currently has 10 manufacturing units and post acquisition, HIL plans to leverage *SLI's* distribution network in Europe to propel the growth of its switchgears business.
- *SLI* has a strong presence in the Latin American and European regions. While EU is growing at a slow pace, LatAm has been witnessing a sharp growth in demand i.e. in excess of ~10-15%. However, exposure to these markets is only to the extent of 20%. This is expected to grow over the next few years as HIL plans to increasingly tap the LatAm markets.

**FINANCIAL SUMMARY**

| Particulars (Rs mn) | FY06   | FY07E  | FY08E  | FY08E Cons |
|---------------------|--------|--------|--------|------------|
| Net Sales           | 10,037 | 15,467 | 18,680 | 47,629     |
| YoY Gr (%)          | 72.5   | 54.1   | 20.8   | 207.9      |
| Op profit           | 1,039  | 1,506  | 1,836  | 3,863      |
| Op. Marg. (%)       | 10.4   | 9.7    | 9.8    | 8.1        |
| Net profit          | 632    | 1,017  | 1,368  | 1,989      |
| Equity Capital      | 134    | 269    | 269    | 302        |
| Diluted EPS (Rs)    | 10.5   | 16.9   | 25.5   | 32.9       |
| PE (x)              | 37.5   | 23.3   | 17.3   | 13.7       |
| EV/Sales (x)        | 2.2    | 1.5    | 1.2    | 0.7        |

**ACQUISITION DETAILS**

|  | SLI Sylvania<br>Euro mn | SLI Sylvania<br>Rs mn |
|--|-------------------------|-----------------------|
| <b>EV paid</b>   | <b>227</b>              | <b>13,316</b>         |
| <b>Represented by</b>  |                         |                       |
| SLI Equity value paid  | 105                     | 6,159                 |
| SLI's Debt (working cap & other)                               | 87                      | 5,103                 |
| <b>Current cash outflow</b>                                    | <b>192</b>              | <b>11,263</b>         |
| Other liabilities (pension)                                    | 35                      | 2,053                 |
| <b>Total Liability</b>   | <b>227</b>              | <b>13,316</b>         |
| <b>Funding pattern</b>   |                         |                       |
| Non-recourse debt on Sylvania                                  | 40                      | 2,346                 |
| Non-recourse debt on HIL subsidiary                            | 80                      | 4,693                 |
| Recourse, con. bridge loan on HIL sub.                         | 50                      | 2,933                 |
| Recourse debt on HIL subsidiary                                | 30                      | 1,760                 |
| <b>Total debt</b>  | <b>200</b>              | <b>11,732</b>         |
| Estimated conversion in FY08 @ CMP<br>of Rs 447 (no of shares) |                         | 6.6                   |
| Existing HIL equity in no of shares (FV Rs 5)                  |                         | 53.8                  |
| <b>Estimated % dilution</b>                                    |                         | <b>12.2</b>           |
| <b>Diluted Equity (Rs mn)</b>                                  |                         | <b>301.8</b>          |

**Funding pattern**

- HIL is raising Euro 227 mn, to fund the acquisition through its subsidiary *Havell's Netherlands*. Of this, pension liability is ~Euro 35 mn, would be paid when it arises. Thus, against an immediate liability of Euro 192 mn (227-35), HIL proposes to raise Euro 200 mn. The debt raised will be a mix of non-recourse (Euro 120 mn) and recourse type.
- Of the recourse debt of Euro 80 mn, Euro 50 mn will be converted to equity, as otherwise it would weigh on HIL's balance sheet and drag its performance.
- Around Euro 60 mn of the total debt raised would be for replacing high cost debt / working capital. The average interest rate on the debt would be ~Euro Libor+175 bps, leading to an effective interest cost of ~5.8-6%.
- The conversion of Euro 50 mn debt is expected to lead to a dilution of ~10-12% in HIL's current equity from Rs 269 mn to Rs 302 mn.

Mar 26, 2007

Sensex : 13285

Nifty: 3861

CMP: Rs 450

Recomm : BUY

### Leveraging Sylvania's network

The key to make the acquisition a success rests in HIL effectively leveraging SLI's network to improve Sylvania's performance as well as route its current switchgear products for the European markets.

Currently, bulk of SLI's revenues accrue from independent wholesalers, with balance being routed through large wholesalers. However, it will take time for synergy benefits to accrue to the consolidated entity.

### Financial impact

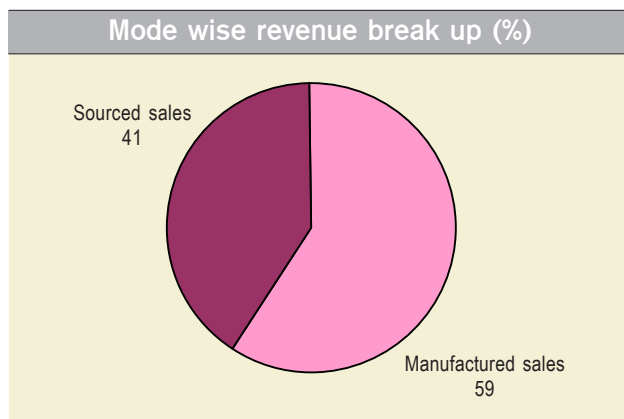
The European and LatAm regions are low margins markets due to the high cost structure in manufacturing. Thus, SLI's operating margins of ~6.9%, would adversely impact consolidated margins by ~204 bps to 8.4%.

Further, SLI's existing debt is high cost working capital debt. Any additional debt being raised for the acquisition, would obviously lead to an increase in interest charges.

Despite the higher leverage, the acquisition will be earnings accretive due to the asset already being restructured and sweated to a higher degree.

Thus, on a consolidated basis, we expect HIL's net sales to be Rs 47.6 bn for FY08, as against net sales of Rs 15.4 bn on a standalone basis. Accordingly, OP should grow by 95% in FY08 on a consolidated basis to Rs 1.9 bn.

The lower margins and higher interest charges would impact profitability in the near term. However, this will improve over the next couple of years as operations are ramped up, synergies get reflected in performance and operational cash flows replace debt raised for the acquisition.



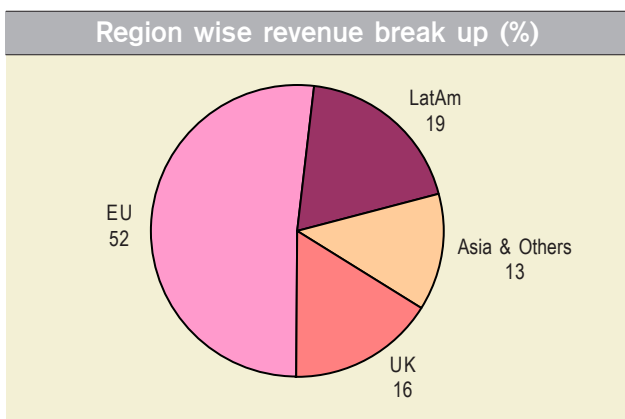
Source: Company

### Valuations

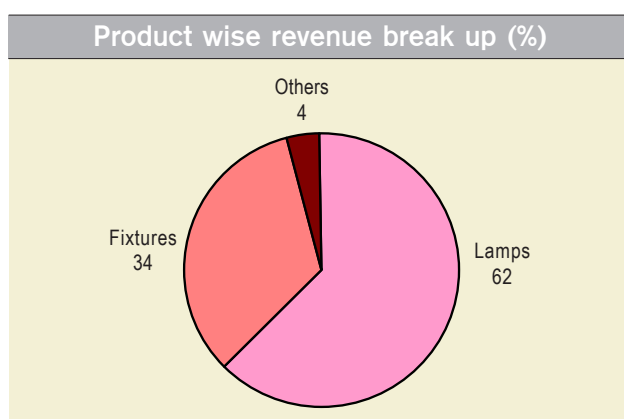
HIL's acquisition at an EV/Sales of 0.5x and EV/EBIDT of 7.3x is at a discount compared to domestic valuations ranging from 1.2-1.5x EV/Sales and 6-9x EV/EBIDT. While richer valuations domestically reflect higher growth rates, valuations for the acquisition appear to be at a discount given the high growth rates in LatAm and its increasing share in revenues.

*HIL trades at a P/E of 13.7x FY08E consolidated EPS of Rs 32.9. The stock trades at an EV/Sales of 0.7x and EV/EBIDT of 9x FY08 estimates. While the appreciation in stock price adequately captures the immediate benefit of consolidation, valuations should improve as benefits of synergies set in over the next 18-24 months.*

*A ramp up in international revenues should help HIL sustain high growth levels without undue strain on its balance sheet. We revise upwards our recommendation to 'BUY' with a price target of Rs 530 over a one year investment perspective as large scale benefits start flowing.*



Source: Company



Source: Company

Year Ended March (Figures in Rs Mn)

| <b>Income Statement</b>              | <b>2005</b>  | <b>2006</b>   | <b>2007E</b>  | <b>2008E Con</b> | <b>Cash Flow Statement</b>            | <b>2005</b>  | <b>2006</b>  | <b>2007E</b> | <b>2008E Con</b> |
|--------------------------------------|--------------|---------------|---------------|------------------|---------------------------------------|--------------|--------------|--------------|------------------|
| <b>Revenues</b>                      | <b>5,820</b> | <b>10,037</b> | <b>15,467</b> | <b>47,629</b>    | <b>PBT &amp; Extra-ord. items</b>     | <b>432</b>   | <b>785</b>   | <b>1,271</b> | <b>2,575</b>     |
| <b>Total Expenditure</b>             | <b>5,215</b> | <b>8,998</b>  | <b>13,960</b> | <b>43,766</b>    | Depreciation                          | 41           | 65           | 95           | 599              |
| <b>Operating Profit</b>              | <b>604</b>   | <b>1,039</b>  | <b>1,506</b>  | <b>3,863</b>     | Interest & dividend inc.              | (34)         | (5)          | (40)         | (60)             |
| Interest & dividend income           | 34           | 35            | 40            | 60               | Interest paid                         | 165          | 179          | 180          | 749              |
| <b>EBIDT</b>                         | <b>638</b>   | <b>1,075</b>  | <b>1,546</b>  | <b>3,923</b>     | Tax paid                              | (96)         | (115)        | (244)        | (575)            |
| (-) Interest                         | 165          | 226           | 180           | 749              | (Inc/Dec in working capital           | (552)        | 512          | (642)        | (4,251)          |
| (-) Depreciation                     | 41           | 64            | 95            | 599              | <b>Cash from operations</b>           | <b>(44)</b>  | <b>1,422</b> | <b>620</b>   | <b>(963)</b>     |
| <b>PBT &amp; extraordinary items</b> | <b>432</b>   | <b>785</b>    | <b>1,271</b>  | <b>2,575</b>     | Net capital expenditure               | (500)        | (638)        | (950)        | (4,194)          |
| (-) Tax provision                    | 127          | 153           | 254           | 587              | Goodwill                              | -            | -            | -            | (3,490)          |
| <b>Net Profits</b>                   | <b>305</b>   | <b>632</b>    | <b>1,017</b>  | <b>1,989</b>     | Interest recd                         | 34           | 12           | 40           | 60               |
| Fully diluted Eq. sh. O/s (mn no)    | 11.6         | 27            | 54            | 60               | <b>Cash from investing activities</b> | <b>(466)</b> | <b>(626)</b> | <b>(910)</b> | <b>(4,134)</b>   |
| Book Value (Rs)                      | 74.7         | 65            | 48            | 122              | Issue of eq. shares                   | -            | -            | -            | 33               |
| <b>Diluted EPS (Rs)</b>              | <b>6.6</b>   | <b>11.8</b>   | <b>18.9</b>   | <b>32.9</b>      | Share premium                         | -            | -            | -            | 2,900            |
|                                      |              |               |               |                  | Change in debt                        | 724          | (591)        | 710          | 9,477            |
|                                      |              |               |               |                  | Dividend paid                         | (37)         | (29)         | (174)        | (195)            |
|                                      |              |               |               |                  | Interest paid                         | 165          | 179          | 180          | 749              |
|                                      |              |               |               |                  | <b>Cash from financing activities</b> | <b>853</b>   | <b>(441)</b> | <b>716</b>   | <b>12,964</b>    |
|                                      |              |               |               |                  | <b>Inc/Dec. in cash</b>               | <b>16</b>    | <b>2</b>     | <b>67</b>    | <b>2,880</b>     |
|                                      |              |               |               |                  |                                       |              |              |              |                  |
| <b>Balance Sheet</b>                 | <b>2005</b>  | <b>2006</b>   | <b>2007E</b>  | <b>2008E Con</b> | <b>Key Ratios</b>                     | <b>2005</b>  | <b>2006</b>  | <b>2007E</b> | <b>2008E Con</b> |
| <i>Equity Share Capital</i>          | 58           | 134           | 269           | 302              | EBIDT %                               | 10.4         | 10.4         | 9.7          | 8.1              |
| Reserves & Surplus                   | 808          | 1,626         | 2,335         | 7,082            | ROACE (%)                             | 28.0         | 36.6         | 41.4         | 29.7             |
| <b>Net worth</b>                     | <b>866</b>   | <b>1,760</b>  | <b>2,604</b>  | <b>7,384</b>     | ROANW (%)                             | 41.8         | 48.1         | 46.6         | 39.8             |
| Total Debt                           | 1,742        | 1,098         | 1,808         | 11,286           | Sales/Total Assets (x)                | 2.5          | 3.8          | 3.7          | 2.6              |
| Deferred Tax liability               | 74           | 95            | 105           | 117              | Debt:Equity (x)                       | 0.5          | 0.5          | 0.6          | 0.9              |
| <b>Capital Employed</b>              | <b>2,682</b> | <b>2,954</b>  | <b>4,517</b>  | <b>18,787</b>    | Current Ratio (x)                     | 2.3          | 1.6          | 1.7          | 1.9              |
| Fixed Assets                         | 923          | 1,532         | 2,387         | 5,982            | Debtors (days)                        | 88.5         | 41.4         | 30.8         | 39.7             |
| Net current assets                   | 1,728        | 1,390         | 2,098         | 9,283            | Inventory (days)                      | 73.2         | 76.3         | 71.4         | 65.0             |
| Investments                          | 32           | 32            | 32            | 32               | Net working capital (days)            | 93.5         | 44.9         | 44.7         | 67.7             |
| <b>Total Assets</b>                  | <b>2,683</b> | <b>2,954</b>  | <b>4,517</b>  | <b>15,297</b>    | EV/Sales (x)                          | 1.0          | 2.3          | 1.5          | 0.7              |
|                                      |              |               |               |                  | EV/EBIDT (x)                          | 10.7         | 23.4         | 16.7         | 9.0              |
|                                      |              |               |               |                  | P/E (x)                               | 68.4         | 38.3         | 23.8         | 13.7             |
|                                      |              |               |               |                  | P/BV (x)                              | 6.0          | 6.9          | 9.3          | 3.7              |

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