

Bajaj Electricals | BJE IN

BUY

Target: ₹220 (Mar'12)

Consumer Durables steady; E&P holds the key

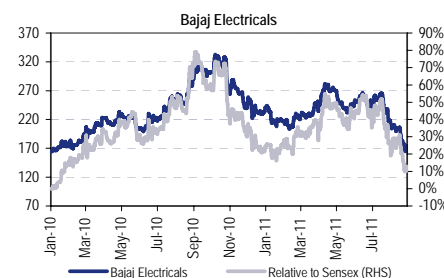
- **E&P profitability to remain under pressure in FY12:** Despite robust consumer durables performance in 1Q12 (revenue/EBIT up 15.3%/16.1% YoY) Bajaj Electricals (BEL) reported 51% YoY decline in net profit to ₹111mn due to ₹76mn loss in E&P business (1st in past 18 quarters). This was mainly due to **a)** adverse revenue mix (high proportion of execution than material supplies), **b)** stable fixed cost, and **c)** additional one-time costs incurred to reduce outstanding number of projects. While management appears confident of recovery in E&P revenues, profitability is expected to remain under pressure due to competition and higher working capital. We cut our E&P EBIT estimate by 24.4%/26.3% in FY12/13 respectively as we reduce revenue growth (14% from 17%) and EBIT margin assumption (7% from 9%). Our EBIT estimates are c.10% below management guidance.
- **Consumer Durables remains steady despite weak fans revenue:** Consumer Durables segment witnessed steady growth despite very weak fans (+10% YoY in 1Q12) and room cooler (-50% YoY) revenues due to an unfavourable summer. However, mixers, OTG, irons grew 35% YoY in 1Q12, depicting strong underlying demand momentum. Management maintains its revenue CAGR of 22-25% for the medium-term (3xGDP growth) based on **a)** further scope for rural penetration, **b)** recent product launches (pressure cookers, water heaters, gas appliances), and **c)** BEL's brand building strategy.
- **Reduce FY12/13E earnings by 18%/19% on poor E&P performance; cut TP to ₹220, maintain BUY:** We cut FY12/13E earnings by 18%/19% to reflect weak E&P segment outlook (based on poor 1Q/2Q12 guidance) and BEL's focus on margin protection in a fiercely competitive scenario. Given the headwinds to E&P earnings growth, we cut our target multiple for BEL from 13x to 12x FY13 EPS of ₹18.3 to arrive at TP of ₹220 (earlier ₹305). We maintain our BUY rating on the stock (potential upside of 25.7%). We see meaningful recovery in BEL's rating after E&P shows improved performance over 3Q/4Q12.

Achal Lohade, CFA
 achal.lohade@jmfinancial.in
 Tel: (91 22) 66303081

Key Data

| | |
|--------------------------|-------------------|
| Market cap (bn) | ₹ 17.4 / US\$ 0.4 |
| Shares in issue (mn) | 98.8 |
| Diluted share (mn) | 98.8 |
| 3-mon avg daily val (mn) | ₹ 35.6/US\$ 0.8 |
| 52-week range | ₹ 347.0/160.1 |
| Sensex/Nifty | 16,416/4,920 |
| ₹/US\$ | 46.0 |

Daily Performance



| % | 1M | 3M | 12M |
|----------|-------|-------|-------|
| Absolute | -20.0 | -29.1 | -37.3 |
| Relative | -10.2 | -19.0 | -28.5 |

* To the BSE Sensex

Shareholding Pattern (%)

| | Jun-11 | Jun-10 |
|-----------------|--------|--------|
| Promoters | 64.8 | 65.5 |
| FII | 9.0 | 3.5 |
| DII | 11.2 | 16.1 |
| Public / others | 15.0 | 14.9 |

Exhibit 1. Financial Summary

(₹ mn)

| Y/E March | FY09A | FY10A | FY11A | FY12E | FY13E |
|----------------------|--------|--------|--------|--------|--------|
| Net sales | 17,657 | 22,286 | 27,408 | 31,658 | 37,098 |
| Sales growth (%) | 27.8 | 26.2 | 23.0 | 15.5 | 17.2 |
| EBITDA | 1,856 | 2,433 | 2,580 | 2,828 | 3,347 |
| EBITDA (%) | 10.5 | 10.9 | 9.4 | 8.9 | 9.0 |
| Adjusted net profit | 951 | 1,302 | 1,499 | 1,518 | 1,869 |
| EPS (₹) | 11.0 | 13.3 | 15.2 | 14.9 | 18.3 |
| EPS growth (%) | 32.4 | 21.4 | 13.6 | -1.8 | 23.2 |
| ROCE (%) | 29.4 | 30.3 | 26.8 | 22.3 | 21.7 |
| ROE (%) | 38.8 | 35.2 | 27.1 | 22.8 | 23.6 |
| PE (x) | 15.9 | 13.1 | 11.5 | 11.7 | 9.5 |
| Price/Book value (x) | 6.2 | 3.4 | 2.8 | 2.5 | 2.1 |
| EV/EBITDA (x) | 8.8 | 7.2 | 6.8 | 7.0 | 5.8 |

Source: Company data, JM Financial. Note: Valuations as of 30/08/2011

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 Bloomberg - JMFR <GO>, Thomson Publisher & Reuters.

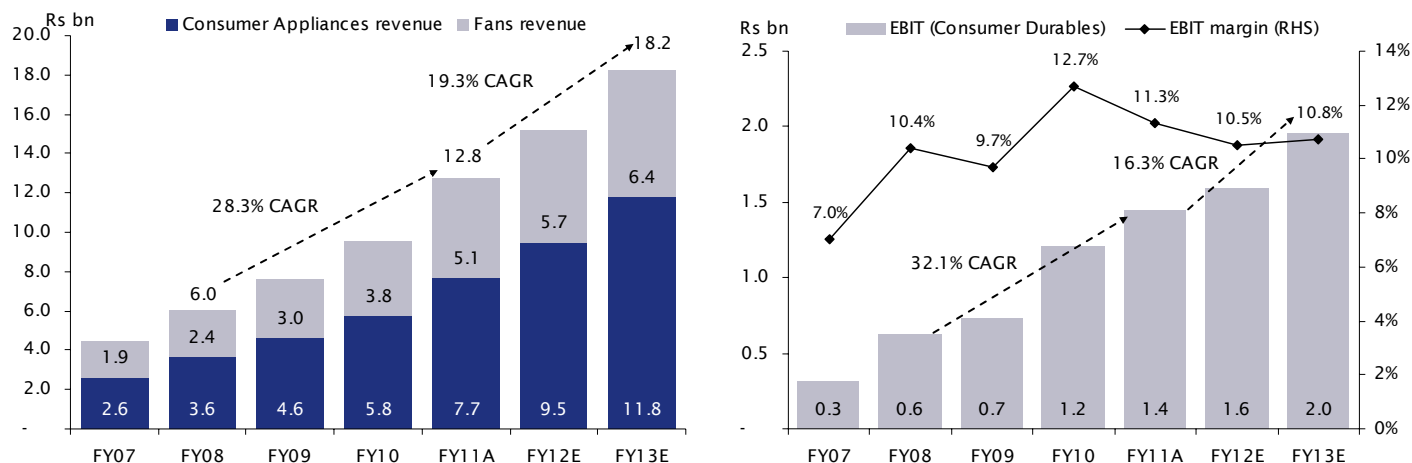
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Segment overview

Consumer Durables:

- **Fans and room cooler** sales remained extremely weak during 1Q12 (fans grew 10% YoY vs 25-30% historical growth and room cooler sales declined 50% YoY) due to a relatively less hot summer and unseasonal rainfall in certain parts of the country. However, management has guided for growth in fans revenue to the tune of 15-20% for FY12 as it remains a 12-month business (instead of the one quarter phenomenon perception).
- **Consumer appliances (excluding room coolers)** however, witnessed extremely strong growth in 1Q12. Mixers/juicers revenue grew 23% YoY, OTG 15% YoY, dry irons 10-12% YoY, indicating strong underlying demand momentum. The company remains extremely bullish on consumer appliances space and maintained its revenue guidance of 3x GDP growth (22-24% growth) based on **a)** significant scope for rural expansion (currently rural/semi urban account for only 15-20% of total revenue), **b)** recent product launches (pressure cookers, gas appliances, water purifiers, small scale gas-based diesel gensets), **c)** BEL's robust dealership network and plans to expand aggressively, **d)** aggressive advertising and brand building exercise.
- 1Q12 operating margins (EBIT) were stable YoY, despite **a)** weaker fans and room coolers revenue growth, and **b)** rise in raw material cost by 5-10%. This was due to **a)** price hikes undertaken in 1Q12 (4-8% in select product categories), **b)** operating leverage, and **c)** constant endeavour to protect margins.
- We believe softness in domestic general economy and higher inflation will likely impact demand for consumer durables, in general. Therefore, we cut FY12/13E revenue for consumer durables by 2.3%/4.3% and now assume revenue CAGR of 19.3% (earlier 22%) during FY11-13E, slightly below management guidance of 22-24% (Exhibit 4). We cut FY12/13E EBIT by 7.6%/2.8% as we assume EBIT margins of 10.5% (earlier 11%)/11% for FY12/13E respectively.

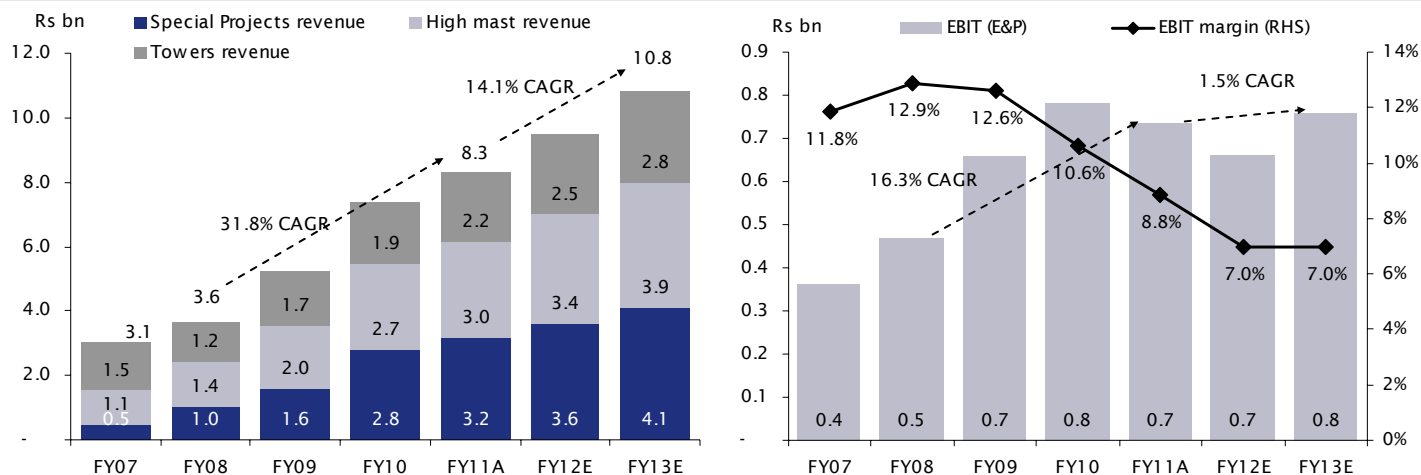
Exhibit 2. Consumer Durables sales and EBIT to see 19.3%/16.3% CAGR in FY11-13E



Source: Company data, JM Financial

E&P:

- E&P segment EBIT margins witnessed significant compression in 1Q12 (-7.6% vs 10.2% in 1Q11/10.5% in 4Q11) on **a)** adverse product mix (more execution component), **b)** rise in raw material cost coupled with lower realisation in certain orders, and **c)** additional cost towards resources deployed to speed up execution and reduce number of ongoing projects (BEL targets to cut current 82 sites to 50-55 sites by Mar'12 and 30-35 on sustainable basis).
- Order book at the end of June'11 stood at ₹7.3bn (post revenue booking in 1Q12); co has bid for additional ₹22bn worth orders. Orderbook de-grew sequentially (₹8.0bn in 4Q11) as key customers such as Power Grid Corp delayed issuing orders and BEL has been selective in new order booking in order to protect its margins.
- Management guided for partial recovery in operating margins to 4.11% in 2Q12 (from -7.6% in 1Q12) and further improvement to 10.5%/12.7% in 3Q/4Q12 respectively based on its existing order book and near-term visibility on orders in the pipeline. It expects to register revenue growth of 24% YoY in FY12. For FY12, it cut EBIT margin guidance to 8% from 9-10% and expressed confidence in achieving the same.
- Over the medium-term, it expects E&P segment to continue to contribute 30-35% to total revenue, implying 18-20% CAGR in E&P revenue. This, in light of the competitive scenario and company's focus on margins, is slightly optimistic in our view.
- Based on the FY11 performance and 1Q12 disappointment, we remain slightly skeptical on BEL's ability to grow its E&P profitability at a significant pace as guided. We reduce our FY12/13E E&P margin to 7% from 9%, leading to reduction in FY12/13E EBIT by 24.4%/26.3%. We trim FY12/13E revenue by 2.7%/5.2%.

Exhibit 3. Sales and EBIT to see 14.1%/1.5% CAGR in FY11-13E

Source: Company data, JM Financial

Exhibit 4. Cut FY12/13 estimates on E&P growth and margin compression

(₹ mn except EPS)

| Y/E March | FY12E | | | FY13E | | |
|--------------------------|---------------|---------------|---------------|---------------|---------------|---------------|
| | Old | New | Chg | Old | New | Chg |
| Sales | 32,278 | 31,658 | -1.9% | 38,501 | 37,098 | -3.6% |
| Lighting | 7,259 | 7,259 | 0.0% | 8,433 | 8,433 | 0.0% |
| Consumer Durables | 15,578 | 15,219 | -2.3% | 19,005 | 18,185 | -4.3% |
| Engineering and Projects | 9,743 | 9,475 | -2.7% | 11,422 | 10,826 | -5.2% |
| EBITDA | 3,140 | 2,828 | -9.9% | 3,740 | 3,347 | -10.5% |
| EBITDA margin | 9.7% | 8.9% | | 9.7% | 9.0% | |
| EBIT | 3,027 | 2,682 | -11.4% | 3,627 | 3,202 | -11.7% |
| Margin | 9.4% | 8.5% | | 9.4% | 8.6% | |
| Lighting | 421 | 421 | 0.0% | 489 | 489 | 0.0% |
| EBIT margin | 5.8% | 5.8% | | 5.8% | 5.8% | |
| Consumer Durables | 1,729 | 1,598 | -7.6% | 2,110 | 1,955 | -7.3% |
| EBIT margin | 11.1% | 10.5% | | 11.1% | 10.8% | |
| Engineering and Projects | 877 | 663 | -24.4% | 1,028 | 758 | -26.3% |
| EBIT margin | 9.0% | 7.0% | | 9.0% | 7.0% | |
| Interest | 305 | 450 | 47.4% | 321 | 455 | 41.8% |
| Adjusted Profit | 1,857 | 1,518 | -18.3% | 2,319 | 1,869 | -19.4% |
| EPS (diluted) | 18.8 | 14.9 | -20.8% | 23.5 | 18.3 | -21.8% |

Source: Company data, JM Financial

Exhibit 5. Quarterly performance summary

(₹ mn except EPS)

| Y/E March | 1Q11A | 1Q12A | YoY | 4Q11A | QoQ | 1Q12E | Var |
|----------------------------|--------------|--------------|---------------|--------------|---------------|--------------|---------------|
| Net Sales | 4,839 | 5,443 | 12.5% | 9,796 | -44.4% | 5,584 | -2.5% |
| RM cost | 3,699 | 4,111 | 11.1% | 7,645 | -46.2% | 4,299 | -4.4% |
| % of sales | 76.5% | 75.5% | | 78.0% | | 77.0% | |
| Employee costs | 239 | 315 | 32.0% | 324 | -2.7% | 279 | 12.8% |
| % of sales | 4.9% | 5.8% | | 3.3% | | 5.0% | |
| Admin and other exp. | 493 | 715 | 45.0% | 810 | -11.7% | 526 | 36.0% |
| % of sales | 10.2% | 13.1% | | 8.3% | | 9.4% | |
| Total Expenditure | 4,431 | 5,141 | 16.0% | 8,779 | -41.4% | 5,104 | 0.7% |
| EBITDA | 408 | 302 | -26.1% | 1,017 | -70.3% | 479 | -37.1% |
| EBITDA Margin | 8.4% | 5.5% | | 10.4% | | 8.6% | |
| Depreciation | 24 | 31 | 30.6% | 34 | -10.0% | 34 | -9.7% |
| EBIT | 384 | 271 | -29.5% | 983 | -72.4% | 445 | -39.2% |
| Other Income | 12 | 7 | -46.0% | 23 | -70.6% | 12 | -46.0% |
| Interest | 57 | 107 | 87.5% | 65 | 63.7% | 60 | 77.8% |
| PBT | 340 | 171 | -49.7% | 941 | -81.8% | 398 | -57.0% |
| Tax Expense | 114 | 60 | -47.5% | 306 | -80.4% | 131 | -54.3% |
| Tax rate | 33.6% | 35.1% | | 32.5% | | 33.0% | |
| Reported Net Profit | 226 | 111 | -51.0% | 635 | -82.6% | 267 | -58.5% |
| Reported EPS | 2.3 | 1.1 | -51.1% | 5.7 | -80.7% | 2.7 | |
| Adjusted net profit | 226 | 111 | -50.8% | 635 | -82.5% | 267 | -58.4% |
| Adjusted EPS (Diluted) | 2.3 | 1.1 | -51.1% | 5.7 | -80.7% | 2.7 | -58.9% |

Source: Company data, JM Financial

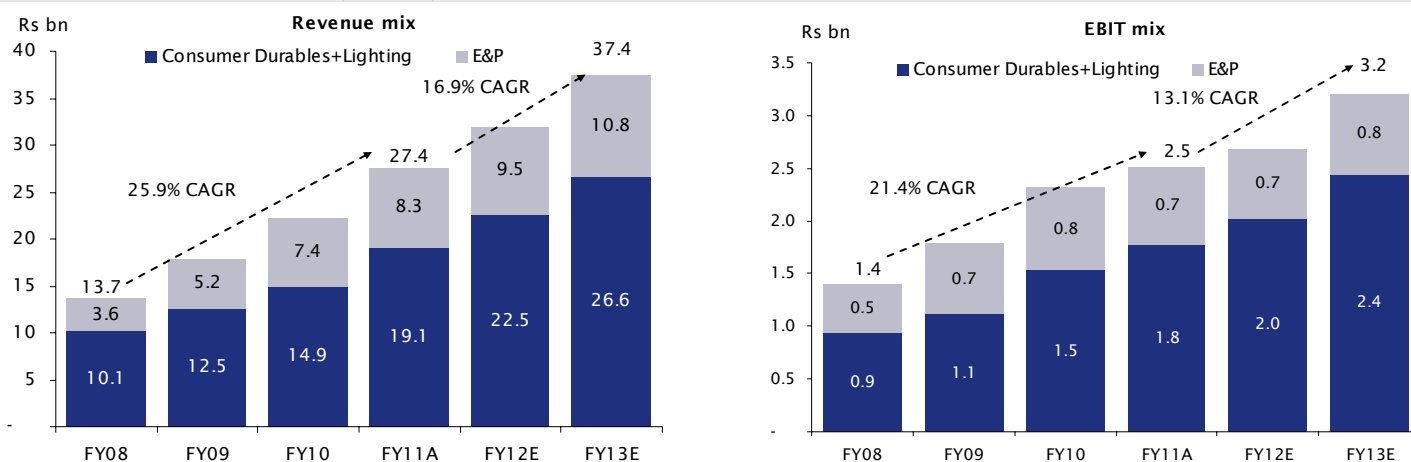
Exhibit 6. Segmental performance summary

(₹ mn)

| Y/E March | 1Q11A | 1Q12A | YoY | 4Q11A | QoQ | 1Q12E | Var |
|----------------------------------|--------------|--------------|---------------|--------------|---------------|--------------|---------------|
| Revenue (gross of excise) | | | | | | | |
| Lighting | 1,100 | 1,274 | 15.8% | 2,013 | -36.7% | 1,210 | 5.3% |
| Consumer Durables | 2,630 | 3,031 | 15.3% | 4,022 | -24.6% | 3,156 | -4.0% |
| Engineering Projects | 1,107 | 1,136 | 2.6% | 3,759 | -69.8% | 1,218 | -6.8% |
| Total | 4,839 | 5,442 | 12.5% | 9,796 | -44.5% | 5,584 | -2.5% |
| EBIT | | | | | | | |
| Lighting | 22 | 62 | 183.1% | 161 | -61.4% | 48 | 28.1% |
| Consumer Durables | 251 | 291 | 16.1% | 446 | -34.7% | 300 | -2.9% |
| Engineering Projects | 114 | -76 | -167.2% | 396 | NM | 110 | NM |
| Total | 385 | 276 | -28.4% | 998 | | 458 | -39.7% |
| EBIT margins | | | | | | | |
| Lighting | 2.0% | 4.9% | | 8.0% | | 4.0% | |
| Consumer Durables | 9.5% | 9.6% | | 11.1% | | 9.5% | |
| Engineering Projects | 10.2% | -6.7% | | 10.5% | | 9.0% | |
| Total | 8.0% | 5.1% | | 10.2% | | 8.2% | |

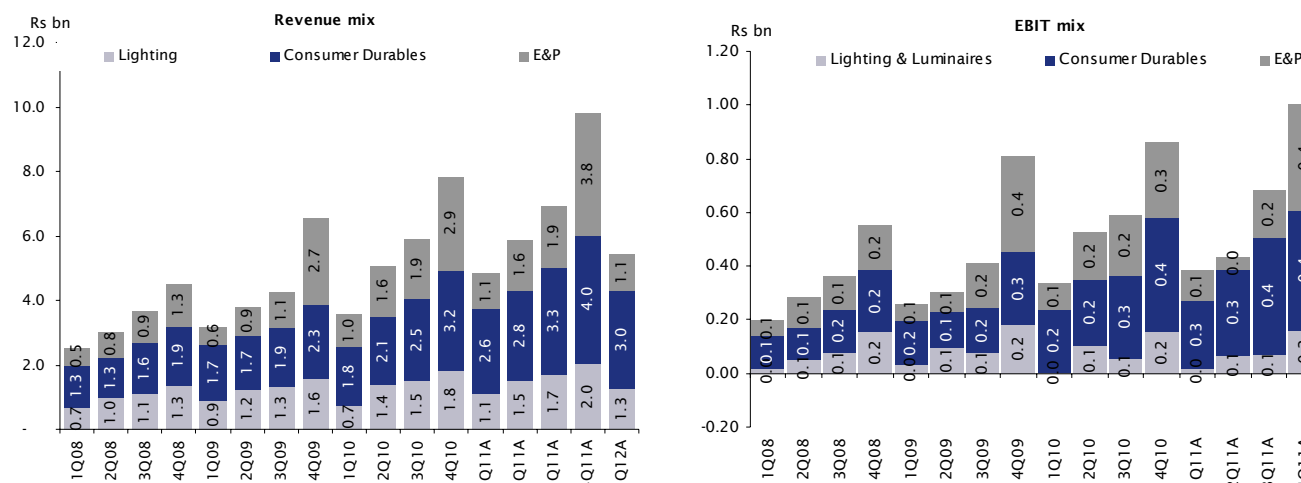
Source: Company data, JM Financial

Exhibit 7. Sales and EBIT mix (Annual)

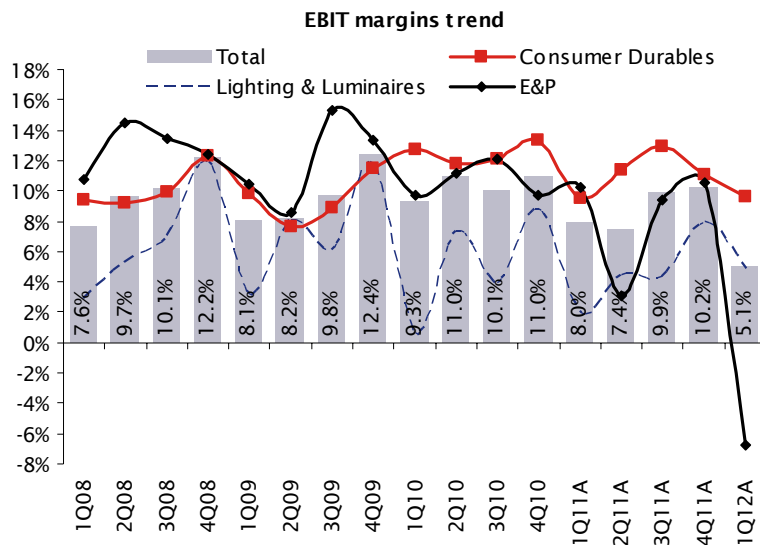


Source: Company data, JM Financial

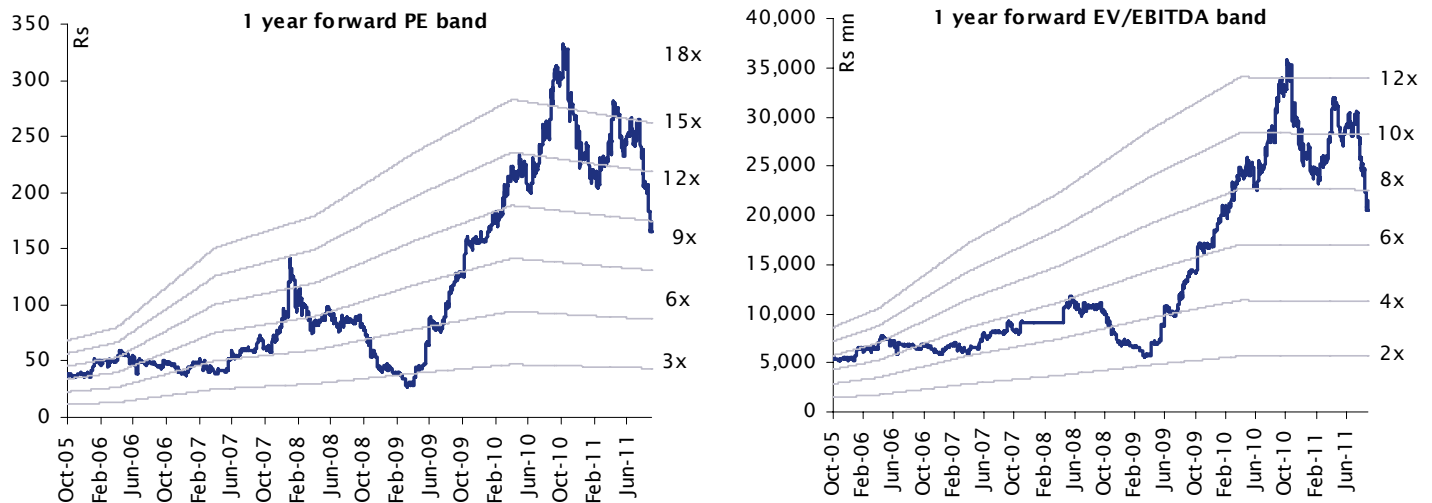
Exhibit 8. Sales and EBIT mix (Quarterly)



Source: Company data, JM Financial

Exhibit 9. Quarterly operating margins (EBIT) trend

Source: Company data, JM Financial

Exhibit 10. BEL's historical PE, EV/EBITDA band

Source: Bloomberg, JM Financial

Financial Tables

| Profit & Loss Statement (₹ mn) | | | | | |
|--------------------------------|--------------|--------------|--------------|--------------|--------------|
| Y/E March | FY09A | FY10A | FY11A | FY12E | FY13E |
| Net sales (Net of excise) | 17,657 | 22,286 | 27,408 | 31,658 | 37,098 |
| Growth (%) | 27.8 | 26.2 | 23.0 | 15.5 | 17.2 |
| Other operational income | 0 | 0 | 0 | 0 | 0 |
| Raw material (or COGS) | 13,149 | 16,524 | 20,947 | 24,377 | 28,566 |
| Personnel cost | 771 | 972 | 1,224 | 1,520 | 1,781 |
| Other expenses (or SG&A) | 1,881 | 2,358 | 2,657 | 2,934 | 3,404 |
| EBITDA | 1,856 | 2,433 | 2,580 | 2,828 | 3,347 |
| EBITDA (%) | 10.5 | 10.9 | 9.4 | 8.9 | 9.0 |
| Growth (%) | 28.9 | 31.1 | 6.0 | 9.6 | 18.4 |
| Other non-op. income | 57 | 29 | 57 | 50 | 55 |
| Depreciation and amort. | 85 | 92 | 108 | 146 | 146 |
| EBIT | 1,827 | 2,370 | 2,529 | 2,732 | 3,257 |
| Add: Net interest income | -370 | -314 | -291 | -450 | -455 |
| Pre tax profit | 1,458 | 2,056 | 2,239 | 2,282 | 2,802 |
| Taxes | 507 | 754 | 740 | 765 | 933 |
| Add: Extraordinary items | -57 | -49 | -61 | 0 | 0 |
| Less: Minority interest | 0 | 0 | 0 | 0 | 0 |
| Reported net profit | 893 | 1,253 | 1,438 | 1,518 | 1,869 |
| Adjusted net profit | 951 | 1,302 | 1,499 | 1,518 | 1,869 |
| Margin (%) | 5.4 | 5.8 | 5.5 | 4.8 | 5.0 |
| Diluted share cap. (mn) | 86 | 98 | 99 | 102 | 102 |
| Diluted EPS (₹) | 11.0 | 13.3 | 15.2 | 14.9 | 18.3 |
| Growth (%) | 32.4 | 21.4 | 13.6 | -1.8 | 23.2 |
| Total Dividend + Tax | 173 | 234 | 277 | 351 | 390 |

Source: Company, JM Financial

| Balance Sheet (₹ mn) | | | | | |
|-----------------------------|--------------|--------------|--------------|--------------|---------------|
| Y/E March | FY09A | FY10A | FY11A | FY12E | FY13E |
| Share capital | 173 | 195 | 196 | 195 | 195 |
| Other capital | 28 | 2 | 2 | 0 | 0 |
| Reserves and surplus | 2,249 | 4,747 | 5,913 | 7,013 | 8,434 |
| Networth | 2,450 | 4,944 | 6,111 | 7,208 | 8,629 |
| Total loans | 2,139 | 1,518 | 1,165 | 2,600 | 2,600 |
| Minority interest | 0 | 0 | 0 | 0 | 0 |
| Sources of funds | 4,589 | 6,462 | 7,276 | 9,808 | 11,229 |
| Intangible assets | 0 | 0 | 0 | 0 | 0 |
| Fixed assets | 1,545 | 1,700 | 2,324 | 2,824 | 3,124 |
| Less: Depn. and amort. | 599 | 683 | 791 | 937 | 1,082 |
| Net block | 946 | 1,016 | 1,533 | 1,887 | 2,042 |
| Capital WIP | 25 | 1 | 0 | 100 | 100 |
| Investments | 316 | 366 | 366 | 366 | 366 |
| Def tax assets/- liability | -32 | 5 | 20 | 5 | 5 |
| Current assets | 9,038 | 11,990 | 15,749 | 18,487 | 21,637 |
| Inventories | 1,777 | 2,094 | 2,947 | 4,337 | 5,082 |
| Sundry debtors | 5,592 | 7,507 | 10,654 | 12,576 | 14,738 |
| Cash & bank balances | 538 | 612 | 481 | 306 | 750 |
| Other current assets | 0 | 0 | 0 | 0 | 0 |
| Loans & advances | 1,131 | 1,777 | 1,668 | 1,268 | 1,068 |
| Current liabilities & prov. | 5,704 | 6,916 | 10,392 | 11,037 | 12,921 |
| Current liabilities | 5,192 | 6,273 | 9,661 | 10,268 | 12,021 |
| Provisions and others | 513 | 643 | 731 | 769 | 900 |
| Net current assets | 3,334 | 5,074 | 5,357 | 7,450 | 8,716 |
| Others (net) | 0 | 0 | 0 | 0 | 0 |
| Application of funds | 4,589 | 6,462 | 7,276 | 9,808 | 11,229 |

Source: Company, JM Financial

| Cash flow statement (₹ mn) | | | | | |
|---------------------------------|--------------|-------------|-------------|---------------|-------------|
| Y/E March | FY09A | FY10A | FY11A | FY12E | FY13E |
| Reported net profit | 893 | 1,253 | 1,438 | 1,518 | 1,869 |
| Depreciation and amort. | 75 | 85 | 108 | 146 | 146 |
| -Inc/dec in working cap. | 40 | -1,151 | -611 | -2,706 | -1,154 |
| Others | 0 | 0 | 0 | 0 | 0 |
| Cash from operations (a) | 1,008 | 186 | 935 | -1,043 | 861 |
| -Inc/dec in investments | -92 | -50 | 0 | 0 | 0 |
| Capex | -127 | -131 | -623 | -600 | -300 |
| Others | -155 | -515 | 196 | 438 | 331 |
| Cash flow from inv. (b) | -373 | -696 | -427 | -162 | 31 |
| Inc/-dec in capital | -5 | 1,475 | 6 | -69 | -59 |
| Dividend+Tax thereon | -173 | -234 | -277 | -351 | -390 |
| Inc/-dec in loans | -229 | -620 | -354 | 1,435 | 0 |
| Others | -10 | -37 | -15 | 15 | 0 |
| Financial cash flow (c) | -416 | 584 | -639 | 1,030 | -449 |
| Inc/-dec in cash (a+b+c) | 218 | 74 | -132 | -175 | 443 |
| Opening cash balance | 320 | 538 | 612 | 481 | 306 |
| Closing cash balance | 538 | 612 | 481 | 307 | 750 |

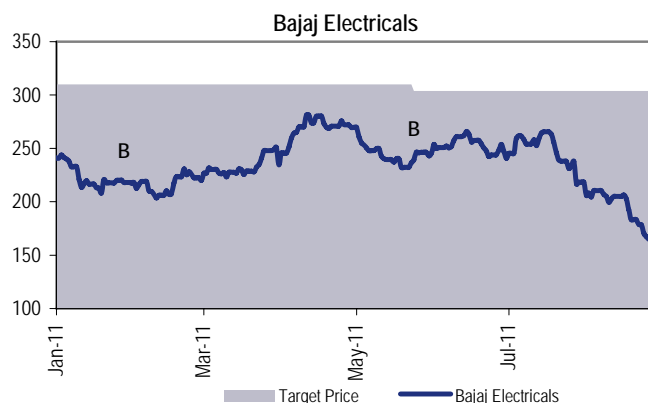
Source: Company, JM Financial

| Key Ratios | | | | | |
|------------------------------|-------|-------|-------|-------|-------|
| Y/E March | FY09A | FY10A | FY11A | FY12E | FY13E |
| BV/Share (₹) | 28.3 | 50.7 | 61.8 | 70.7 | 84.6 |
| ROCE (%) | 29.4 | 30.3 | 26.8 | 22.3 | 21.7 |
| ROE (%) | 38.8 | 35.2 | 27.1 | 22.8 | 23.6 |
| Net Debt/equity ratio (x) | 0.5 | 0.1 | 0.1 | 0.3 | 0.2 |
| Valuation ratios (x) | | | | | |
| PER | 15.9 | 13.1 | 11.5 | 11.7 | 9.5 |
| PBV | 6.2 | 3.4 | 2.8 | 2.5 | 2.1 |
| EV/EBITDA | 8.8 | 7.2 | 6.8 | 7.0 | 5.8 |
| EV/Sales | 0.9 | 0.8 | 0.6 | 0.6 | 0.5 |
| Turnover ratios (no.) | | | | | |
| Debtor days | 116 | 123 | 142 | 145 | 145 |
| Inventory days | 37 | 34 | 39 | 50 | 50 |
| Creditor days | 144 | 139 | 168 | 154 | 154 |

Source: Company, JM Financial

History of earnings estimates and target price

| Date | FY12E EPS (₹) | % Chg. | FY13E EPS (₹) | % Chg. | Target Price | Target Date | % Chg. |
|-----------|------------------|--------|------------------|--------|-----------------|----------------|--------|
| 22-Dec-10 | 18.9 | | 23.9 | | 310 | Mar-12 | |
| 28-Jan-11 | 19.1 | 1.1 | 23.9 | 0.0 | 310 | Mar-12 | 0.0 |
| 24-May-11 | 18.8 | -1.6 | 23.5 | -1.7 | 304 | Mar-12 | -1.9 |

Recommendation history**JM Financial Institutional Securities Private Limited**

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BOARD: +9122 6630 3030 | FAX: +91 22 6747 1825 | EMAIL: JMFINANCIAL.RESEARCH@JMFINANCIAL.IN | WWW.JMFINANCIAL.IN

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