

Q2FY2012 Review
 Sector: Engineering
 BSE Sensex : 17,805

BLUE STAR

 Downgrade SELL
 CMP Rs211
 TP Rs135

28 October 2011

Macro headwinds mar the outlook

Blue Star reported disappointing results. Net sales declined by 12% to Rs6bn (PINCe Rs7bn). OPM contracted sharply by 840bps to 2.3% led by cost overrun in the MEP division and cost pressure in the cooling prod. division. Management expects margin pressure to continue for few more quarters. Higher interest cost coupled with unrealized foreign exchange losses resulted into loss of Rs208mn. Adj. loss was Rs14mn (PINCe PAT of Rs161mn).

MEP division continues to incur losses

Cost overrun in some of the projects and execution delays resulted into margin erosion which the management believes would continue for few more quarters. Sales declined by 19% to Rs3.8bn and incurred loss of Rs34mn. We believe margins on the existing order book to remain under pressure for the next 4-5 quarters. Any improvement in the macro environment would lead to better execution and arrest the fall in profitability. New orders are expected to have better margins. Management aims to achieve high single digit margin only in FY14.

Other segments also disappointed

Cooling product division and Professional Electronics & Industrial systems division also disappointed. Sales growth in the cooling product division slowed down to 11% to Rs1.6bn. High cost of raw material and huge inventory into the industry leading to intense competition adversely impacted the segmental margins which declined by 556bps to 5.4%. Overall slowdown in the economy and weak consumer sentiments might continue to impact the performance of the cooling product division segment.

Professional Electronics & Industrial Systems performance was also impacted by the economic slowdown. Sales declined by 12% to Rs594mn. However, segmental profits were up by ~2% to Rs173mn led by 388bps improvement in margins. We believe improved margins were on account of favourable product mix.

VALUATIONS AND RECOMMENDATION

Standalone order book at the end of Q2FY12 stands at Rs21.6bn up by 8% YoY. Order inflow in Q2FY12 was Rs6.8bn down 5% on a YoY basis. On going sluggish investment environment plagued with high interest rates have resulted into slowdown in order inflows. Management believes business slowdown to continue for some time. Revenues and profitability are expected to remain under pressure for few more quarters. Sustained decline in commodity prices might arrest the fall in the profitability. On account of expected slowdown in order inflows, margin pressure and deterioration in return ratios we downgrade our target multiple to 10x FY13E (earlier 13x FY13E). We have reduced our sales and profit estimates for FY12 by 8% and 68% respectively. Similarly, FY13 estimates are reduced by 13% and 32% respectively. We downgrade our recommendation on the stock from 'HOLD' to 'SELL' with a reduced target price of Rs135 (10x FY13E).

KEY FINANCIALS (CONSOLIDATED)

| | (Rs mn) | | | | |
|------------------|---------|--------|--------|--------|--------|
| | FY09 | FY10 | FY11 | FY12E | FY13E |
| Net Sales | 25,194 | 25,494 | 29,761 | 29,864 | 32,093 |
| YoY Gr. (%) | 13.4 | 1.2 | 16.7 | 0.3 | 7.5 |
| Op. Profits | 2,764 | 2,992 | 2,544 | 1,150 | 2,359 |
| OPM (%) | 11.0 | 11.7 | 8.5 | 3.9 | 7.4 |
| Adj. Net Profits | 1,803 | 2,008 | 1,607 | 428 | 1,215 |
| YoY Gr. (%) | 3.6 | 17.3 | (23.9) | (82.3) | 326.9 |

KEY RATIOS

| | | | | | |
|-------------------|------|------|------|------|------|
| Dil. EPS (Rs) | 20.0 | 22.3 | 17.9 | 3.2 | 13.5 |
| ROCE (%) | 77.9 | 62.5 | 36.0 | 8.9 | 17.4 |
| ROE (%) | 57.2 | 46.8 | 32.0 | 8.2 | 21.5 |
| PER (x) | 10.5 | 9.4 | 11.8 | 44.1 | 15.6 |
| EV/ Net Sales (x) | 0.8 | 0.7 | 0.8 | 0.8 | 0.8 |
| EV/ EBITDA (x) | 6.9 | 6.3 | 9.0 | 22.0 | 10.6 |

 Ankit Babel +91-22-6618 6551
 ankit.b@pinc.co.in

 Vinod Nair +91-22-6618 6379
 vinod.nair@pinc.co.in

QUARTERLY SNAPSHOT (Rs mn)

| | Quarter Ended | | |
|------------------|---------------|--------|---------|
| | Mar-11 | Jun-11 | Sep-11 |
| Net Sales | 9,085 | 7,032 | 5,988 |
| YoY Gr. (%) | 6.3 | 0.1 | (12.2) |
| Op. Profits | 1,026 | 276 | 136 |
| OPM (%) | 11.3 | 3.9 | 2.3 |
| Adj. Net Profits | 568 | 98 | (14) |
| YoY Gr. (%) | (27.6) | (73.0) | (103.6) |

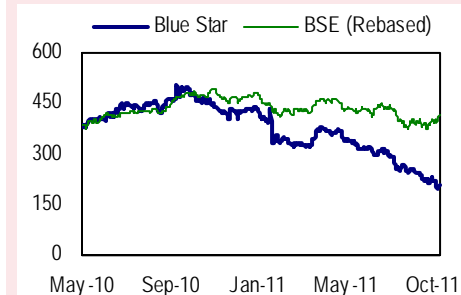
STOCK DATA

| | |
|----------------------------|-----------|
| Market Cap | Rs18.9bn. |
| Book Value per share | Rs54.7 |
| Eq Shares O/S (F.V. Rs2) | 89.9mn. |
| Free Float | 59.9% |
| Avg Traded Value (6 mnths) | Rs180mn |
| 52 week High/Low | Rs479/194 |
| Bloomberg Code | BLSTR IN |
| Reuters Code | BLUS.BO |

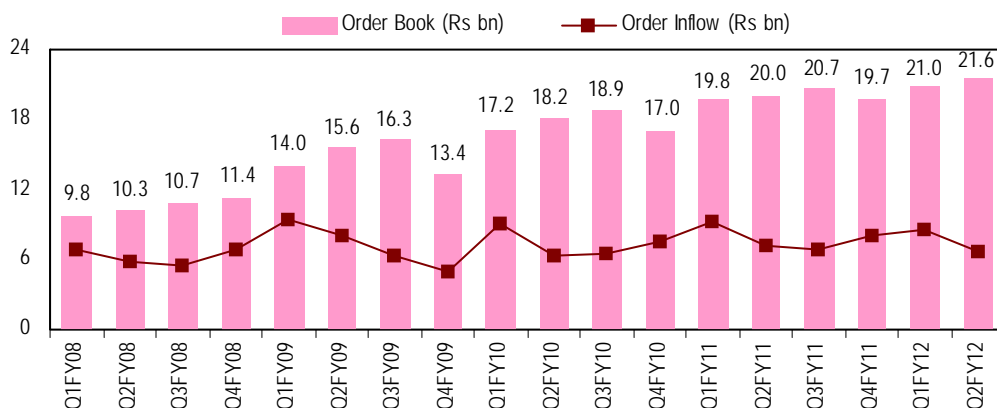
PERFORMANCE (%)

| | 1M | 3M | 12M |
|----------|--------|--------|--------|
| Absolute | (6.2) | (28.6) | (53.4) |
| Relative | (13.3) | (25.8) | (47.8) |

RELATIVE PERFORMANCE



Order Book (Rs bn)



Source: Company & PINC Research

Segmental Result

| Particulars (Rs mn) | Quarter Ended | | | Year Ended | | |
|---------------------------------------|---------------|--------------|----------------|---------------|---------------|----------------|
| | Q2FY12 | Q2FY11 | Gr(%) | H1FY12 | H1FY11 | Gr(%) |
| Segment Revenue | | | | | | |
| Electro Mech Projects | 3,825 | 4,729 | (19.1) | 7,242 | 8,446 | (14.3) |
| Cooling Products | 1,569 | 1,414 | 10.9 | 4,850 | 3,972 | 22.1 |
| Professional Electronics and Ind Sys. | 594 | 674 | (11.9) | 928 | 997 | (7.0) |
| Total | 5,988 | 6,818 | (12.2) | 13,019 | 13,416 | (3.0) |
| Segment Result (PBIT) | | | | | | |
| Electro Mech Projects | (34) | 434 | (107.9) | (123) | 785 | (115.6) |
| Cooling Products | 85 | 155 | (45.3) | 526 | 517 | 1.7 |
| Professional Electronics and Ind Sys. | 173 | 170 | 1.6 | 253 | 217 | 16.5 |
| Total PBIT | 224 | 759 | (70.5) | 656 | 1,519 | (56.8) |
| Less: Interest | 306 | 33 | 831.7 | 381 | 69 | 455.2 |
| Net other un-allocable Exp | 158 | 166 | (4.6) | 385 | 373 | 3.4 |
| Total PBT | (240) | 561 | (142.7) | (110) | 1,078 | (110.2) |
| Capital Employed | | | | | | |
| Electro Mech Projects | 6,377 | 5,416 | 17.7 | 6,377 | 5,416 | 17.7 |
| Cooling Products | 2,700 | 1,738 | 55.4 | 2,700 | 1,738 | 55.4 |
| Professional Electronics and Ind Sys. | 755 | 484 | 56.1 | 755 | 484 | 56.1 |
| Add: Un-allocable Capital Employed | (4,207) | (1,963) | | (4,207) | (1,963) | 114.3 |
| Total | 5,625 | 5,675 | (0.9) | 5,625 | 5,675 | (0.9) |
| PBIT Margin (%) | | | | | | |
| Electro Mech Projects | (0.9) | 9.2 | (1,006) | (1.7) | 9.3 | (1,099) |
| Cooling Products | 5.4 | 11.0 | (556) | 10.8 | 13.0 | (217) |
| Professional Electronics and Ind Sys. | 29.2 | 25.3 | 388 | 27.3 | 21.8 | 551 |
| Total | 3.7 | 11.1 | (740) | 5.0 | 11.3 | (628) |
| ROCE (%) | | | | | | |
| Electro Mech Projects | (2.1) | 32.0 | | (1.9) | 14.5 | |
| Cooling Products | 12.6 | 35.7 | | 19.5 | 29.8 | |
| Professional Electronics and Ind Sys. | 91.8 | 141.0 | | 33.5 | 44.9 | |
| Total | 15.9 | 53.5 | | 11.7 | 26.8 | |
| Net Sales Mix (%) | | | | | | |
| Electro Mech Projects | 63.9 | 69.4 | | 55.6 | 63.0 | |
| Cooling Products | 26.2 | 20.7 | | 37.3 | 29.6 | |
| Professional Electronics and Ind Sys. | 9.9 | 9.9 | | 7.1 | 7.4 | |
| Total | 100.0 | 100.0 | | 100.0 | 100.0 | |
| PBIT Mix (%) | | | | | | |
| Electro Mech Projects | (15.2) | 57.1 | | (18.7) | 51.7 | |
| Cooling Products | 37.9 | 20.4 | | 80.2 | 34.0 | |
| Professional Electronics and Ind Sys. | 77.4 | 22.4 | | 38.5 | 14.3 | |
| Total | 100.0 | 100.0 | | 100.0 | 100.0 | |

Consolidated Financials

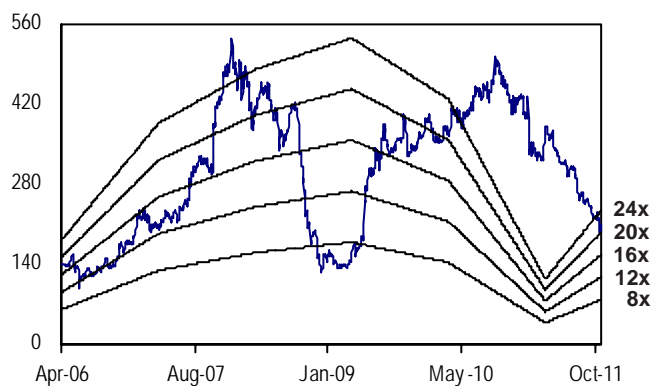
| Income Statement | FY09 | FY10 | FY11 | FY12E | FY13E |
|------------------------|--------|--------|--------|--------|--------|
| Net Sales | 25,194 | 25,494 | 29,761 | 29,864 | 32,093 |
| Growth (%) | 13.4 | 1.2 | 16.7 | 0.3 | 7.5 |
| Operating Profit | 2,764 | 2,992 | 2,544 | 1,150 | 2,359 |
| Growth (%) | 23.9 | 8.2 | (15.0) | (54.8) | 105.2 |
| Other income | 49 | 67 | 338 | 150 | 165 |
| EBITDA | 2,814 | 3,058 | 2,882 | 1,300 | 2,524 |
| Growth (%) | 21.8 | 8.7 | (5.8) | (54.9) | 94.2 |
| Depreciation | 259 | 347 | 319 | 361 | 415 |
| EBIT | 2,555 | 2,711 | 2,563 | 938 | 2,108 |
| Interest paid | 173 | 85 | 256 | 396 | 467 |
| PBT (before E/o items) | 2,382 | 2,627 | 2,307 | 543 | 1,641 |
| E/o Income / (loss) | - | 140 | 4 | (194) | - |
| Tax provision | 579 | 651 | 728 | 91 | 427 |
| Net Profit | 1,803 | 2,115 | 1,610 | 284 | 1,215 |
| Growth (%) | 3.6 | 17.3 | (23.9) | (82.3) | 326.9 |
| Adjusted net profit | 1,803 | 2,008 | 1,607 | 428 | 1,215 |
| Adj Dil EPS (Rs) | 20.0 | 22.3 | 17.9 | 3.2 | 13.5 |
| Diluted EPS Growth (%) | 24.4 | 11.4 | (19.8) | (82.3) | 326.9 |

| Cash Flow Statement | FY09 | FY10 | FY11 | FY12E | FY13E |
|-------------------------|-------|---------|---------|---------|---------|
| Pre-tax profit | 2,382 | 2,766 | 2,311 | 349 | 1,641 |
| Depreciation | 259 | 347 | 319 | 361 | 415 |
| Total tax paid | (631) | (732) | (845) | (91) | (427) |
| Chg in working capital | (379) | (1,278) | (2,969) | (2,603) | (211) |
| Other items | 265 | 51 | 52 | 380 | 451 |
| Cash from oper. (a) | 1,896 | 1,155 | (1,132) | (1,605) | 1,870 |
| Capital expenditure | (851) | (239) | (505) | (465) | (600) |
| Chg in investments | 2 | 92 | 4 | - | - |
| Other items | 8 | 35 | (767) | 43 | 16 |
| Cash flow from inv. (b) | (841) | (112) | (1,267) | (423) | (584) |
| Free cash flow (a+b) | 1,055 | 1,043 | (2,400) | (2,027) | 1,286 |
| Equity raised/ (repaid) | - | - | - | - | - |
| Debt raised/ (repaid) | (84) | (181) | 3,769 | 2,415 | (372) |
| Interest Paid | (172) | (85) | (252) | (396) | (467) |
| Dividend (incl. tax) | (737) | (737) | (839) | (116) | (497) |
| Other items | 3 | - | - | - | - |
| Cash flow from fin. (c) | (989) | (1,002) | 2,677 | 1,903 | (1,336) |
| Net chg in cash (a+b+c) | 65 | 40 | 278 | (124) | (50) |

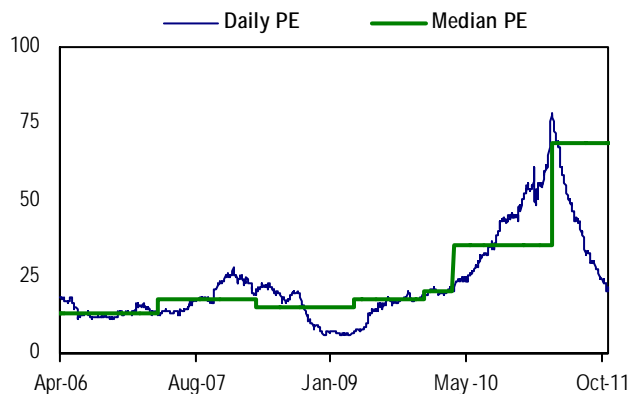
| Balance Sheet | FY09 | FY10 | FY11 | FY12E | FY13E |
|--------------------------|-------|-------|-------|--------|--------|
| Equity Share Capital | 180 | 180 | 180 | 180 | 180 |
| Reserves & surplus | 3,491 | 4,737 | 4,933 | 5,101 | 5,818 |
| Shareholders' funds | 3,671 | 4,917 | 5,112 | 5,280 | 5,998 |
| Total Debt | 273 | 89 | 4,445 | 6,860 | 6,488 |
| Deferred Tax liability | 6 | (15) | (7) | (7) | (7) |
| Capital Employed | 3,950 | 4,991 | 9,550 | 12,133 | 12,479 |
| Net fixed Assets | 2,124 | 1,992 | 2,225 | 2,329 | 2,513 |
| Cash & Cash Eq. | 92 | 132 | 524 | 400 | 350 |
| Net other current assets | 1,685 | 2,825 | 6,529 | 9,132 | 9,343 |
| Investments | 44 | 42 | 272 | 272 | 272 |
| Misc Exp. | 6 | - | - | - | - |
| Total assets | 3,950 | 4,991 | 9,550 | 12,133 | 12,479 |

| Key Ratios | FY09 | FY10 | FY11 | FY12E | FY13E |
|----------------------------|------|-------|-------|-------|-------|
| OPM (%) | 11.0 | 11.7 | 8.5 | 3.9 | 7.4 |
| Net margin (%) | 7.2 | 7.9 | 5.4 | 1.4 | 3.8 |
| Dividend yield (%) | 3.3 | 3.8 | 3.3 | 0.5 | 2.3 |
| Net debt/ Equity (x) | 0.0 | (0.0) | 0.8 | 1.2 | 1.0 |
| Net working capital (days) | 57.8 | 81.5 | 145.1 | 149.0 | 134.0 |
| Asset turnover (x) | 6.4 | 5.1 | 3.1 | 2.5 | 2.6 |
| ROCE (%) | 77.9 | 62.5 | 36.0 | 8.9 | 17.4 |
| RoE (%) | 57.2 | 46.8 | 32.0 | 8.2 | 21.5 |
| EV/Net sales (x) | 0.8 | 0.7 | 0.8 | 0.8 | 0.8 |
| EV/EBITDA (x) | 6.9 | 6.3 | 9.0 | 22.0 | 10.6 |
| PER (x) | 10.5 | 9.4 | 11.8 | 44.1 | 15.6 |
| Price/Book (x) | 5.1 | 3.8 | 3.7 | 3.6 | 3.1 |

1-Year forward P/E Band



Median PE v/s Daily PE



T E A M

EQUITY DESK

| | | | |
|---------------|---|--|-----------------|
| Sadanand Raje | Head - Institutional Sales Technical Analyst | sadanand.raje@pinc.co.in | 91-22-6618 6366 |
|---------------|---|--|-----------------|

RESEARCH

| | | | |
|-------------------------|---------------------------------------|--|-----------------|
| Vineet Hetamasaria, CFA | Head of Research, Auto, Cement | vineet.hetamasaria@pinc.co.in | 91-22-6618 6388 |
| Nikhil Deshpande | Auto, Auto Ancillary, Cement | nikhil.deshpande@pinc.co.in | 91-22-6618 6339 |
| Tasmai Merchant | Auto, Auto Ancillary, Cement | tasmai.merchant@pinc.co.in | 91-22-6618 6377 |
| Vinod Nair | Construction, Power, Capital Goods | vinod.nair@pinc.co.in | 91-22-6618 6379 |
| Ankit Babel | Capital Goods, Engineering | ankit.b@pinc.co.in | 91-22-6618 6551 |
| Hitul Gutka | Power | hitul.gutka@pinc.co.in | 91-22-6618 6410 |
| Subramaniam Yadav | Construction | subramaniam.yadav@pinc.co.in | 91-22-6618 6371 |
| Madhura Joshi | Power | madhura.joshi@pinc.co.in | 91-22-6618 6395 |
| Satish Mishra | Fertiliser, Natural Gas | satish.mishra@pinc.co.in | 91-22-6618 6488 |
| Urvashi Biyani | Fertiliser, Natural Gas | urvashi.biyani@pinc.co.in | 91-22-6618 6334 |
| Naveen Trivedi | FMCG | naveent@pinc.co.in | 91-22-6618 6384 |
| Rohit Kumar Anand | IT Services | rohit.anand@pinc.co.in | 91-22-6618 6372 |
| Namrata Sharma | Media | namrata.sharma@pinc.co.in | 91-22-6618 6412 |
| Sakshee Chhabra | Media | sakshee.chhabra@pinc.co.in | 91-22-6618 6516 |
| Bikash Bhalotia | Metals, Mining | bikash.bhalotia@pinc.co.in | 91-22-6618 6387 |
| Harleen Babber | Metals, Mining | harleen.babber@pinc.co.in | 91-22-6618 6389 |
| Dipti Vijaywargi | Metals, Mining | dipti.vijaywargi@pinc.co.in | 91-22-6618 6393 |
| Sushant Dalmia, CFA | Pharma | sushant.dalmia@pinc.co.in | 91-22-6618 6462 |
| Poonam Sanghavi | Pharma | poonam.sanghavi@pinc.co.in | 91-22-6618 6709 |
| Suman Memani | Real Estate, Mid caps | suman.memani@pinc.co.in | 91-22-6618 6479 |
| Abhishek Kumar | Real Estate, Mid caps | abhishek.kumar@pinc.co.in | 91-22-6618 6398 |
| C Krishnamurthy | Technical Analyst | krishnamurthy.c@pinc.co.in | 91-22-6618 6747 |

SALES

| | | | |
|----------------|-------------|--|-----------------|
| Rajeev Gupta | Equities | rajeev.gupta@pinc.co.in | 91-22-6618 6486 |
| Ankur Varman | Equities | ankur.varman@pinc.co.in | 91-22-6618 6380 |
| Himanshu Varia | Equities | himanshu.varia@pinc.co.in | 91-22-6618 6342 |
| Shailesh Kadam | Derivatives | shaileshk@pinc.co.in | 91-22-6618 6349 |
| Ganesh Gokhale | Derivatives | ganeshg@pinc.co.in | 91-22-6618 6347 |

DEALING

| | | | |
|----------------------|-------------------------|--|-----------------|
| Mehul Desai | Head - Sales Trading | mehul.desai@pinc.co.in | 91-22-6618 6303 |
| Naresh Panjnani | Co-Head - Sales Trading | naresh.panjnani@pinc.co.in | 91-22-6618 6333 |
| Amar Margaje | | amar.margaje@pinc.co.in | 91-22-6618 6327 |
| Ashok Savla | | ashok.savla@pinc.co.in | 91-22-6618 6321 |
| Sajjid Lala | | sajjid.lala@pinc.co.in | 91-22-6618 6337 |
| Raju Bhavsar | | rajub@pinc.co.in | 91-22-6618 6322 |
| Kinjal Mehta | | kinjal.mehta@pinc.co.in | 91-22-6618 6333 |
| Chandani Bhatia | | chandani.bhatia@pinc.co.in | 91-22-6618 6324 |
| Hasmukh D. Prajapati | | hasmukhp@pinc.co.in | 91-22-6618 6325 |
| Kamlesh Purohit | | kamlesh.purohit@pinc.co.in | 91-22-6618 6357 |

SINGAPORE DESK

| | | | |
|-----------|--|--|--------------|
| Amul Shah | | amul.shah@sg.pinc.co.in | 65-6327 0626 |
|-----------|--|--|--------------|

DIRECTORS

| | | | |
|----------------|--|--|-----------------|
| Gaurang Gandhi | | gaurangg@pinc.co.in | 91-22-6618 6400 |
| Hemang Gandhi | | hemangg@pinc.co.in | 91-22-6618 6400 |
| Ketan Gandhi | | ketang@pinc.co.in | 91-22-6618 6400 |

COMPLIANCE

| | | | |
|---------------|-----------------|--|-----------------|
| Rakesh Bhatia | Head Compliance | rakeshb@pinc.co.in | 91-22-6618 6400 |
|---------------|-----------------|--|-----------------|

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