



Providing Financial Solution for All

Hindustan Sanitaryware & Industries Ltd.

-breaking barriers, setting benchmarks

CMP: Rs. 112.70

Initiating Coverage - BUY

Target Price	Rs.152
Sensex	13614.52
S&P Nifty	3888.65
Mid Cap	1628.57
Face Value	Rs. 2
52 Wk high/Low	190/ 80
Equity	Rs 11.0 Crs
Market Cap.	Rs 619.85 crs

Codes

NSE	HINDSANIT
BSE	500187
Bloomberg	HIS@IN
Reuters	HSNT.BO
BSE Group	B1

Group	Indian Private
Industry	Sanitaryware

Shareholding Pattern Sept-06(%)

Promoters	55.63
FII's	4.81
Institutions	10.65
Corporate	17.87
Public & Others	11.04

Financial Snapshot (Rs. in Crs)

	FY06	FY07E	FY08E
Net Sales	391.1	480.5	575.6
Net Profit	25.7	34.7	47.2
OPM %	20.1	19.6	20.7
EPS (Rs.)	5.1	6.3	8.6
PE (x)	22.1	17.9	13.1
BV (Rs.)	27.7	37.9	44.8
ROE %	21.3	20.5	20.7
ROCE %	16.4	17.2	20.6

Analyst: Vimal Mishra, ACA

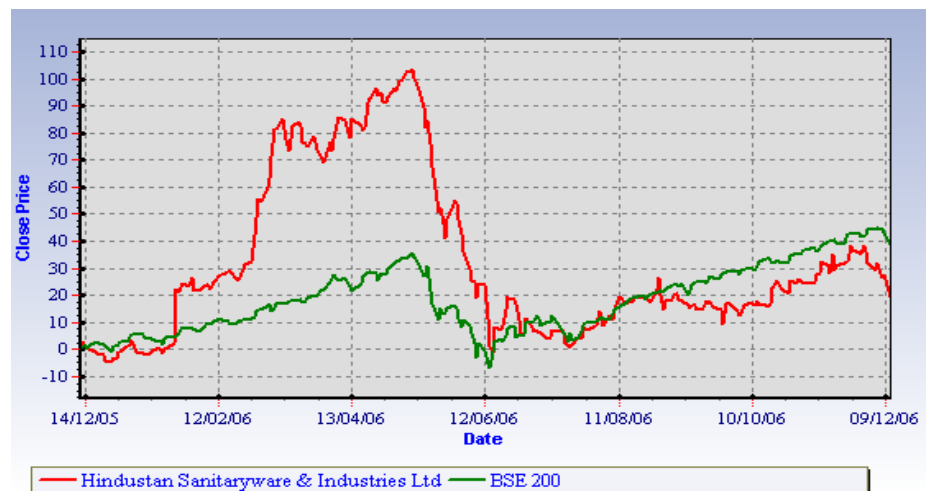
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Investment Rationale

Hindustan Sanitaryware & Industries Ltd. (HSIL), a market leader in sanitarywares in India, has three manufacturing facilities at Bahadurgarh, Haryana; Somanyapuram (Bibinagar) and Sanathnagar both in Andhra Pradesh and sells the Sanitaryware under the famous brand name 'Hindware'. The company is also diversified into the manufacture of glass containers to service the growing needs of institutional buyers in FMCG, liquor, beverage and pharmaceutical industries.

- HSIL posted total revenue growth of 36 % in the FY06 to Rs. 428.20 crs and the net profit grew by 35% to Rs. 25.67 crs. HSIL's revenue is expected to grow at a CAGR of 20% over FY2006-08 in view of real estate and construction boom which will increase the demand in sanitaryware business too.
- Even the container glass business of the company is expected to grow since the entire user industries of glass are on a growth path and demand for container glass is expected to grow by 6 to 7%.
- HSIL has a good market share in both the businesses and is amongst the top two players in both the industries i.e, sanitaryware and container glass.

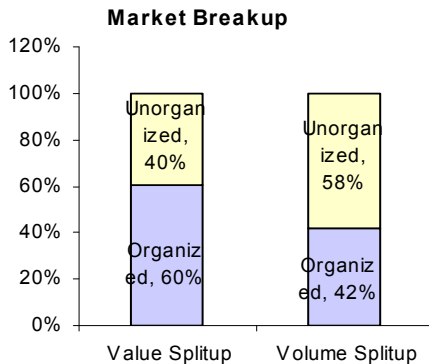


Valuation

At the current market price of Rs 112.70, the stock is trading at PE of 17.9x FY07E and 13.1x FY08E earnings. The stock trades at an EV/ EBITDA of 8.5x FY07E and 6.8x FY08E earnings. We recommend a **BUY** on the stock for **12 months price target of Rs 152 which discounts FY08E earnings by 17.7x.**

Industry Overview

Sanitary ware



The Indian sanitaryware market is estimated at around Rs. 780 crs, characterized by a branded organized sector as well as a large unorganized sector. The industry reported an attractive 12% growth on account of a strong trend in the building and construction industry space riding a favorable environment in India's housing and infrastructure sector. The market for sanitaryware in India comprises the institutional and individual segment. While institutional customers buy directly from the company and use material in construction projects like apartments, commercial complexes and shopping malls, the individual segment buys from retail outlets for residential applications.

This industry is labor intensive and labor cost is a crucial element. In India, labor cost is low unlike in the developed markets. This will thus result in outsourcing manufacturing of mass product items to low cost countries like India in due course of time.

Over the last few years, offtake has been progressively influenced by India's evolving demographics triggered by urbanization, nuclear families, rising incomes, higher aspiration levels and affordable mortgage rates. As a result, the bathroom has evolved from a functional to lifestyle statement. India's Rs. 7300 crs bathroom sector comprises Rs 4800 crs for floor and wall tiles, Rs. 1200 crs for faucets, Rs. 780 crs for sanitaryware and Rs. 700 crs for accessories. While new demand accounts for the majority of purchases, a replacement demand is also gradually accounting for an increase in use.

Container Glass

The container glass industry is centered on India's organized sector with an installed capacity of 1,500,000 tons p.a. and a production level of around 1,236,000 tons, with flint glass bottle accounting for 935,000 tons (around 75%) and amber and green glass bottles for 301,000 tons.

Owing to changing lifestyles and the need for enhanced hygiene, packaging acquired the status of a critical industry with four basic functions: protection, containment, communication and utility of product use. It not only acted as a protective covering but stimulated purchase behaviour.

Container glass industry faces threat from PET bottles industry as well as from the aluminum packaging industry. However with the consumers growing cautious about the environmental hazards of PET bottles, the demand for container glass has been picking up. Even in the developed market of US and Europe, the demand for container glass has been growing.

User segments of container glass in India

India's food processing industry is one of the largest industries in India- ranked fifth in terms of production, consumption and export. The annual demand for glass packaging and containers for the food industry is estimated at around 187,000 tons. Apart from this, the liquor and pharmaceutical industries are also among the major users of container glass.

Features of container glass market

- Presence of large buyers in each user
- Plants located close to user industries
- Extended credit periods
- Top six companies controlling 80% of production
- Increasing use of aesthetics in product application

Investment Argument

Strong demand from housing and hotel sector.

The sanitaryware products would post healthy growth as demand from housing and hotel sector is expected to remain strong. The growing culture of malls is also providing a market for the sanitaryware industry. The company extended from sanitaryware to bathroom solutions to kitchen products and will now move towards comprehensive home solutions. It has entered the Rs. 200 crs kitchen appliance industry through the introduction of a new line of kitchen products.

Growing market share

HSIL's market share for sanitaryware products increased from 36% to 39% of branded sanitaryware market in FY06. Also, in case of container glass products, the market share increased from 13% to 15%. The company introduced 54 new designs in the container glass line accounting for about 8% of the total turnover.

Good brand image

The company products are marketed under the popular 'Hindware' and 'Rassi' brand, the former comprising the 'Art' and 'Italian' collections. The company also markets globally renowned brand 'Keramag' through its distribution channels to capitalize on a growing demand for premium products.

Largest distribution network

The company possesses largest distribution network within industry, comprising 995 dealers and about 11,000 sub-dealers. The company has now started leveraging on this huge network and covers a wider product portfolio like PVC cisterns, fittings and seat covers, kitchen sinks and faucets.

Capturing demand in all price segments

HSIL focuses on middle and high-end premium segment but offers sanitaryware in the price range of Rs. 200 to Rs. 35,000 to tap the demand of all classes of customers. The low end offerings would cater to demand shift from unorganized to organized market as Indian sanitaryware market growing at about 12% is superseded by organized segment which is growing at 16-17%. Rising middle class and growing per capita income would add demand for middle and high end premium segment which ultimately will contribute to the topline. Also, the growth in replacement demand which accounts for just 7% of total demand as compared to 80% in developed countries is another huge growth avenue for the company.

'Hindware' is rated as the most recognized brand by AC Nielsen survey

Outsourcing opportunity

With many European and US sanitaryware manufacturing units closing down due to high operating costs, the demand for sanitaryware would be met by manufacturing units located in low cost countries like India.

New capacities coming in

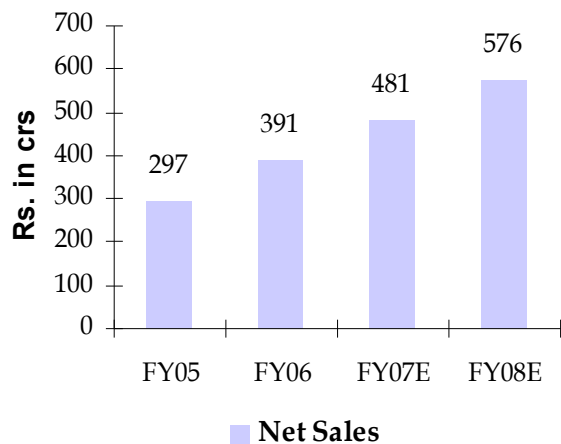
HSIL has increased its manufacturing capacity of its Bibinagar plant from 12000 TPA to 18000 TPA which started operations from February 2006. Further HSIL is planning to expand its capacity at this plant in near future. The company is also planning to acquire some companies in the building products sector to further consolidate its position. This will add additional revenue to the company and will also help in maintaining its market share.

Key Earnings driver for the company

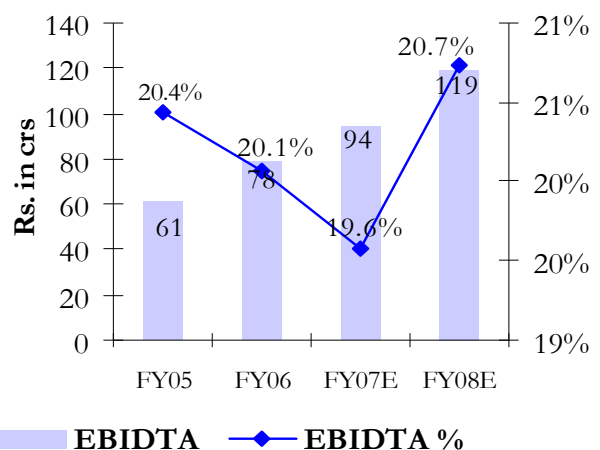
Revenue growth:

The Company has registered a growth of 36% in its revenues in FY06. We expect the revenues to grow by 18% for FY07E and 20% in FY08E. The building products segment is expected to report better performance on the back of rising disposable incomes, greater replacement demand and the on going construction boom. Similarly, in case of container glass segment, the company is concentrating on growing its presence in the high margin FMCG and pharmaceutical segment.

HSIL – Net Sales



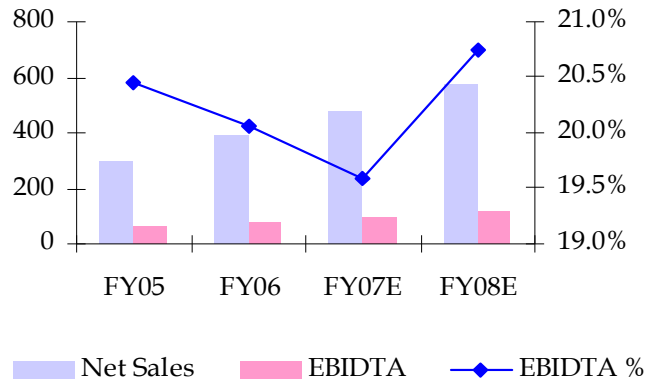
HSIL – EBIDTA



Sources: Company Data & SKP estimates

Earnings growth:

The earnings in FY06 have shown a better growth inspite of an increase in its input costs (power, fuel and some raw materials). The EBITDA margin for FY06 stands to 20.1 % as against 20.4 % in FY05. Going forward, we expect the EBITDA margin of 19.6 % in FY07E and 20.7 % in FY08E.



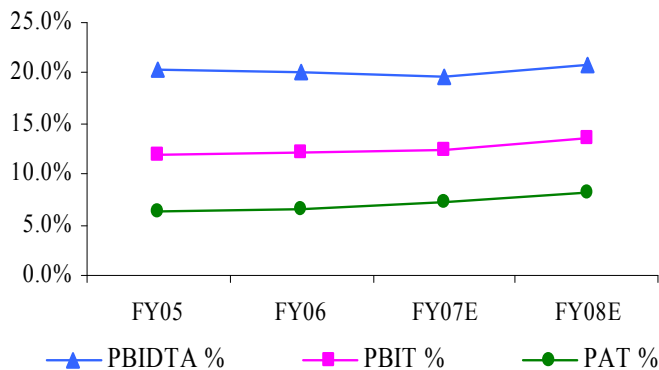
Sources: Company Data & SKP estimates

Key Fundamentals

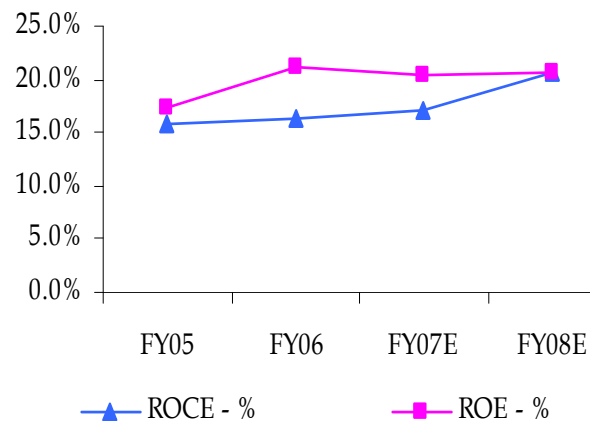
Particulars (%)	FY05	FY06	FY07E	FY08E
EBITDA Margin	20.4	20.1	19.6	20.7
PAT Margin	6.4	6.6	7.2	8.2
RoE	17.3	21.3	20.5	20.7
RoCE	15.7	16.4	17.2	20.6

Sources: Company Data & SKP estimates

Margins



ROCE & ROE



Sources: Company Data & SKP estimates

Valuations

At the current market price of Rs 112.70, the stock is trading at PE of 17.9x FY07E and 13.1x FY08E earnings. The stock trades at an EV/EBITDA of 8.5x FY07E and 6.8x FY08E earnings. We recommend a **BUY** on the stock for **12 months price target of Rs. 152 which discounts FY08E earnings by 17.7 x.**

Company background

A leading player in sanitarywares

HSIL, promoted in 1960 by Somany Group in collaboration with Twyford Ltd of UK to manufacture sanitarywares, is a market leader in sanitaryware. The company diversified into the manufacture of glass containers through the acquisition of The Associated Glass Industries Ltd in 1981.

Business Segment	Location	Capacity
Building Products Div.	Bahadurgarh (Haryana)	14000 TPA
Building Products Div.	Bibinagar (Andhra Pradesh)	18000 TPA*
Container Glass Div.	Sanathnagar (Hyderabad)	953(Pcs in mn)

* including 6000 TPA commissioned from Feb 2006

Building Products Division

HSIL is the second largest manufacturer of sanitaryware products in India. Over the decades, the company has progressed from a simple sanitaryware manufacturer to providing bathroom and kitchen solutions. The company's products are sold under the Hindware and Raasi Brands, the former comprising the 'Art' and 'Italian' collections. The company also markets globally renowned brand 'Keramag' through its distribution channels to capitalize on a growing demand for premium products.

The outsourced products segment contributes around 37% of total sales of building products division

The company has started its outsourced products business in 1998 with the outsourcing of complementary bathroom products like PVC cisterns, seat covers, fittings and internal mechanisms with a view to emerge as a complete bathroom solutions provider. The division outsourced imported bathroom and kitchen products and marketed them under the 'Hindware Italian Collection' brand. The outsourced products business of the company reported a sales growth of 89% in FY06.

Container Glass Division

HSIL is the leading container glass manufacturer in India with a capacity of 953 mn bottles and controls around 15% of the organized container glass market. The glass manufacturing facility is located in Hyderabad comprising of two furnaces, the recent addition being another deep refiner furnace that is the most fuel efficient in India. As freight is the critical element in this business, the company capitalizes on its location advantage and meets the needs of its customers with ease.

Revenue Segment

Building Products Division

The division grew 38% in FY06 on account of higher capacity utilization of 109% as compared to 85% in FY05 resulting in better efficiency, higher production and lower cost of production which were partially offset by higher raw material and power & fuel cost. The expansion of installed capacity by 23% in FY06 and focus on increasing market share will lead to growth in revenues at a CAGR of 20 % over FY06-08.

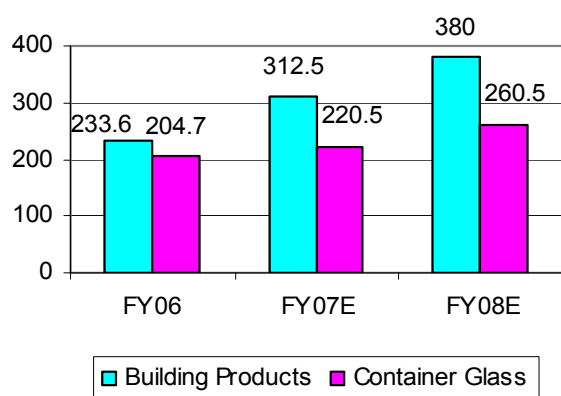
Container Glass Division

This division has registered a growth of 26% in FY06 on account of increase in production by 41%, introduction of 54 new designs and increased exports by 46% with an entry into Middle East and Africa. The division is focusing on increasing realizations from all segments of its business and emphasizing an optimal product mix to partly offset a steep increase in input costs.

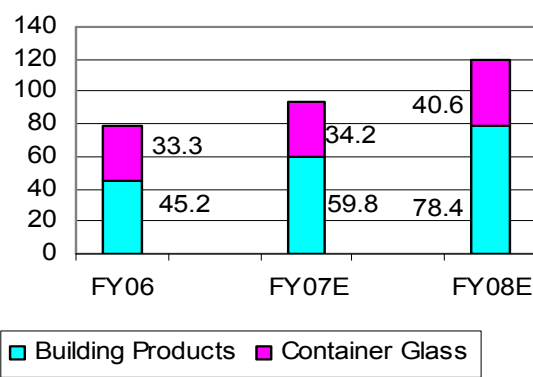
Revenue & EBIT		(RS. in Crs)		
Division	FY06	FY07E	FY08E	
Building Products				
Sales	233.6	312.5	380.0	
EBIT	45.2	59.8	78.4	
Container glass				
Sales	204.7	220.5	260.5	
EBIT	33.3	34.2	40.6	

Source: Company data and SKP Estimates

Segment wise Revenue



Segment wise EBIT



Source: Company data and SKP Estimates

Latest Quarterly Financial Performance

Particulars (Rs. in Crs)	Q2 2007	Q2 2006	Var %	H1 2007	H1 2006	Var %
Total Income	120.35	91.72	31.2	237.88	176.72	34.6
Total Expenditure	100.19	72.40	38.4	196.05	140.86	39.2
PBIDT	20.16	19.32	4.3	41.83	35.86	16.6
Interest	3.39	3.00	13.0	6.90	6.29	9.7
PBDT	16.77	16.32	2.8	34.93	29.57	18.1
Depreciation	5.82	6.07	-4.1	12.47	12.34	1.1
Tax	3.81	3.33	14.41	7.67	5.94	29.1
Profit After Tax	7.14	6.92	3.2	14.79	11.29	31.0
EPS	1.35	3.70	-63.5	2.97	6.04	-50.8
PBIDTM (%)	17.04	21.39		17.82	20.53	
PBDTM (%)	14.17	18.07		14.88	16.93	
PATM (%)	6.03	7.66		6.30	6.46	

Detailed Financials

Income Statement

(Rs. in Crs)		FY05	FY06	FY07E	FY08E
Net Sales		296.84	391.09	480.50	575.75
Other Income		3.54	7.42	4.20	5.25
Incr. /Decr. in stock		13.80	29.69	20.00	22.46
Total Income		314.18	428.20	504.70	603.46
<i>% Growth</i>		19.9%	36.3%	17.9%	19.6%
Total Expenditure		253.50	349.73	410.60	484.06
PBIDTA		60.68	78.47	94.10	119.40
<i>PBIDTA Margins</i>		20.4%	20.1%	19.6%	20.7%
Depreciation		20.82	25.14	27.90	31.40
PBIT		39.86	53.33	66.20	88.00
<i>PBIT Margins</i>		12.0%	12.2%	12.3%	13.7%
Interest		10.89	12.93	11.65	13.58
PBT		28.97	40.40	54.55	74.42
<i>PBT Margins</i>		8.7%	9.2%	10.1%	11.5%
Tax		9.94	14.73	19.88	27.18
PAT		19.03	25.67	34.67	47.24
<i>PAT Margins</i>		6.4%	6.6%	7.2%	8.2%

Balance Sheet

(Rs. in Crs)		FY05	FY06	FY07E	FY08E
Equity Share Capital		9.36	9.36	11.01	11.01
Total Reserves		102.28	120.06	197.80	228.28
Total Net worth		111.64	129.42	208.81	239.29
Secured Loans		94.54	81.30	71.38	74.93
Unsecured Loans		76.19	158.08	121.20	133.32
Total Debt Capital		170.73	239.38	192.58	208.25
Net Deferred Tax		32.57	31.70	30.85	29.75
Total Liability		314.94	400.50	432.24	484.63
Gross Fixed Assets		336.39	365.53	402.08	442.29
Depreciation		137.46	160.65	186.55	212.95
Net Fixed Assets		198.93	204.88	215.53	229.34
Capital Work In Progress		1.34	3.80	--	--
Investments		23.56	57.80	60.69	63.72
Current Assets		171.91	245.53	275.07	335.13
Current Liabilities		80.80	111.51	119.05	143.56
Net Current Assets		91.11	134.02	156.02	191.57
Total Assets		314.94	400.50	432.24	484.63

Cash Flow

(Rs. in Crs)		FY05	FY06	FY07E	FY08E
Opening balance for cash & cash eq.		2.59	8.38	10.33	12.88
Net Cash flow from Operating Act.		30.23	19.13	55.07	58.05
Net Cash Flow from Investing Act.		-64.89	-65.32	-38.79	-42.39
Net Cash from Financing act		40.45	48.14	-13.73	-7.32
Total		5.79	1.95	2.55	8.34
Closing balance for cash & cash eq.		8.38	10.33	12.88	21.21

Key Ratios

Particulars	FY05	FY06	FY07E	FY08E
Valuation Ratios				
CMP - Rs.		112.7		
No of Shares (Crs)	1.9	4.7	5.5	5.5
EPS - Rs.	10.17	5.09	6.30	8.58
Earnings Yield (%)	10	5	6	8
P/E Ratio	11.1	22.1	17.9	13.1
B.V per share	59.6	27.7	37.9	44.8
P/ BV	1.9	4.1	3.0	2.5
Earnings Ratio				
PBIDTA %	20.4	20.1	19.6	20.7
PBIT%	12.0	12.2	12.3	13.7
PBT%	8.7	9.2	10.1	11.5
PAT %	6.4	6.6	7.2	8.2
EV - Rs. Cr.	370	754	800	807
EV/EBIDTA	6.1	9.6	8.5	6.8
EV/Sales	1.2	1.9	1.7	1.4
ROE - %	17.3	21.3	20.5	20.7
ROCE - %	15.7	16.4	17.2	20.6
Dividend %	55.0	65.0	65.0	75.0
Div. Payout (% of PAT)	27.0	23.7	20.7	17.5
Balance Sheet Ratios				
Debt-Equity Ratio	1.53	1.85	0.92	0.84
Current Ratio	2.1	2.2	2.3	2.3
Debtor Days	86	84	81	82
Creditor Days	84	77	71	71
Interest Cover Ratio(x)	3.7	4.1	5.7	6.5
Turnover Ratios				
Fixed Assets (X)	1.0	1.2	1.3	1.5
Inventory(X)	3.9	3.6	3.9	3.9
Debtors(X)	4.2	4.3	4.4	4.4

Risk & Concerns

- The prices of power and fuel and soda ash which together constitute major manufacturing cost had risen sharply. Such price rise in future would impact the earnings of the company.
- Increased competition from existing and new entrants in this business, could negatively impact the profitability of the company.

The above analysis and data are based on last available prices and not official closing rates.	
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