

## Equities

11 November 2011 | 7 pages

# Voltas (VOLT.BO)

## Alert: 2QFY12 Conference Call Takeaways

We attended the Voltas 2QFY12 conference call. The following are the key takeaways.

- **What's New?** (1) Voltas has recently secured Lol for a large retail project in Abu Dhabi of ~Rs5bn, which is not included in its order book; (2) Management expects margins in the international business to be under pressure for the next two quarters due to cost overruns in the Qatar projects; (3) Rohini subsidiary may marginally miss its EBIT breakeven in FY12; (4) Competitive intensity in the AC industry remains high, largely due to adverse weather, higher Japanese competition and higher inventory levels.
- **Electro-mechanical Projects** – Management mentioned that there were difficulties in the Qatar projects due to faster execution and consequent cost escalations. The company is hopeful of settling certain variations towards the end of the execution. The ~Rs9bn Sidra project is ~60% completed and is expected to be finished by June 2012. The ~Rs5.5bn Barwa City project is ~90% complete, and is expected to be finished by March. The reduction in order inflows has resulted in lesser customer advances. The company is also seeing a lengthening in debtor days. Voltas mentioned that it was bidding with margins of ~7-8% in domestic and ~5% in international orders, and will try to improve margins to ~7% by cost cutting, economies of scale, better design and procurement.
- **Engineering Products & Services** – Revenues declined by ~5% YoY largely due to the transfer of the material handling business. Management mentioned that margins in the mining and construction business were under pressure due to the recent interest rate hikes. Delay in securing environmental clearances for mines has also resulted in lower sales and commissions.
- **High Competition in Unitary Cooling Products** – Management mentioned that there has been a sharp industry-wide decline in volumes due to the adverse weather. This has been compounded by (1) Renewed Japanese competition with aggressive price cuts – Daikin by ~40%, Hitachi by ~10% and Panasonic by ~15%; (2) High inventory maintained by other competitors anticipating ~30% YoY volume growth. **Strategies to counter the same** – Voltas has limited the impact to ~18% drop in volumes (maintaining its #2 position in the AC market) and ~7% drop in revenues by (1) increased focus on water coolers and commercial refrigerators, (2) expanding distribution network into Tier II and Tier III towns, (3) increasing ad spends, (4) and leveraging its brand to maintain price levels.

### Company Update

<b>Neutral/High Risk</b>	<b>2H</b>
Price (11 Nov 11)	Rs95.50
Target price	Rs121.00
Expected share price return	26.7%
Expected dividend yield	2.2%
<b>Expected total return</b>	<b>28.9%</b>
Market Cap	Rs31,599M US\$632M

### Price Performance (RIC: VOLT.BO, BB: VOLT IN)



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## Voltas

### Valuation

Our target price for Voltas of Rs121 is based on PE of 12x Dec-FY12 E. We value Voltas at a discount to its historical PE of 15x given the macro headwinds faced by the company in the Middle East and muted order inflows impacting earnings growth. We choose P/E as our valuation methodology for Voltas, as this is in line with other E&C companies in our coverage.

### Risks

We rate Voltas shares High Risk, reflecting the vulnerability of Voltas' business to the global slowdown, especially in the Middle East. Key downside risks to our target price include: International projects risks; termination of principal-agent relationships; increasing competition in domestic and international markets; manpower shortages; and material prices. Key upside risks to our target price include: stronger-than-expected performance driven by the international business; and turnaround of the domestic operating environment. These risks could impede the stock from achieving our target price.

## Appendix A-1

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#### Voltas (VOLT.BO)

#### Ratings and Target Price History Fundamental Research

Analyst: Deepal Delivala



Chart current as of 5 November 2011

Date	Rating	Target Price	Closing Price
1 25-Jan-09	*3H	*38.00	41.15
2 12-Jun-09	*3M	*142.00	132.90
3 3-Aug-10	*2M	*241.00	209.70
4 3-Feb-11	2M	*189.00	181.10

Date	Rating	Target Price	Closing Price
5 22-May-11	2M	*182.00	162.35
6 1-Aug-11	2M	*157.00	135.10
7 26-Sep-11	2M	*131.00	117.50
8 5-Oct-11	2M	*121.00	102.55

Date	Rating	Target Price	Closing Price
9 7-Oct-11	Stock rating system changed		
10 7-Oct-11	*2H	121.00	104.70

\* Indicates change

Rating/target price changes above reflect Eastern Standard Time

**Volta (VOLT.BO)**  
**Ratings and Target Price History**  
**Best Ideas Research**  
**Relative Call (3 Month)**

Analyst: Deepal Delivala



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**Data current as of 10 Oct 2011**

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	Buy	Hold	Sell	Buy	Hold	Sell
% of companies in each rating category that are investment banking clients	45%	42%	37%	50%	43%	46%

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