

## VOLTAS

ENGINEERING

# HOLD

Target Price: Rs 500

### Strong execution in a tough quarter

Voltas indicated that Q1 A/C industry primary sales were marginally down YoY due to de-stocking, while secondary sales were up 15-17% YoY due to discounting and promotions ahead of GST transition. Despite uncertainties, Voltas sustained its leadership position with an increased market share of 22.2%. In addition to negative operating leverage in Q1, UCP margin withstood rising input costs, new ad campaign and trade support measures as well as price disruption from competition and remained strong at 14%. EMP<sup>^</sup> business, despite the Qatar slowdown (exposure of Rs 6 bn), sustained EBIT margin at 5.3%.

We fine tune estimates to reflect a higher margin trajectory and revise TP to Rs 500 (Rs 460 earlier). However, much of this upside has been priced in; hence, maintain **HOLD**.

CMP : Rs 541  
Potential Upside : -8%

#### MARKET DATA

No. of Shares : 331 mn  
Free Float : 70%  
Market Cap : Rs 179 bn  
52-week High / Low : Rs 555 / Rs 287  
Avg. Daily vol. (6mth) : 1.9 mn shares  
Bloomberg Code : VOLT IB Equity  
Promoters Holding : 30%  
FII / DII : 19% / 28%

### Segment-wise analysis

- ◆ **Unitary cooling (65% of Q1FY18 revenue):** Sales growth was lackluster at 1% YoY at Rs 12.1 bn. While Q1 started off well led due to hot weather and strong demand, the growth was restricted owing to unseasonal rains in South India as well as the uncertainty around GST. Voltas remains the market leader with a 22% share with ~900 bps gap with the nearest competitor (LG). EBIT margin declined 80 bps to 14.1%; we believe that in a tough environment, the margin has held well compared to that of other consumer durables peers. Management continues to guide sustainable EBIT margin at 10-12%
- ◆ Air cooler sales were flat YoY given erratic monsoon and uncertainty regarding GST. Voltas cut air cooler prices by 5-6% (in line with GST rates) to pass on the benefit to the consumer
- ◆ As per the management, restocking should pick up ahead of the second summer and upcoming festival season. With reference to Arcelik JV, Voltas indicated that it was a bit pre-mature to talk about specific product launches

### Financial summary (Consolidated)

Y/E March	FY16	FY17	FY18E	FY19E
Sales (Rs mn)	57,198	60,328	68,974	78,939
EBITDA (Rs mn)	4,330	5,791	6,802	8,022
Adj PAT (Rs mn)	3,580	5,074	5,308	6,360
Con. EPS* (Rs)	-	-	17.1	19.6
EPS (Rs)	10.8	15.3	16.0	19.2
Change YOY (%)	5.9	41.7	4.6	19.8
P/E (x)	50.0	35.3	33.7	28.1
RoE (%)	15.9	17.8	15.1	16.0
EV/E (x)	41.5	30.7	26.2	22.0
DPS (Rs)	2.6	3.0	4.0	5.0

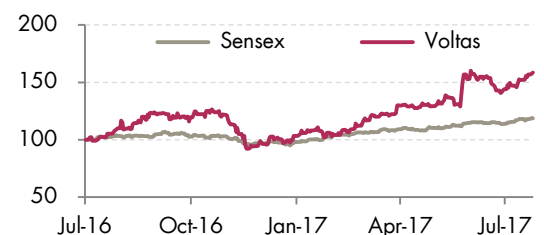
Source: \*Consensus broker estimates, Company, Axis Capital

Note: ^Electro-Mechanical Projects

### Key drivers

EBIT margin (%)	FY17	FY18E	FY19E
MEP	3.2	5.8	6.0
Engg Prod & Services	28.8	28.8	30.0
Unitary Cooling	14.5	14.0	14.3

### Price performance



**Exhibit 1: Results update**

(Rs mn)	Quarter ended					12 months ended		
	Jun-17	Jun-16	% Chg	Mar-17	% Chg	FY18E	FY17	% Chg
<b>Net sales</b>	<b>19,681</b>	<b>18,552</b>	<b>6</b>	<b>20,351</b>	<b>(3)</b>	<b>68,974</b>	<b>60,328</b>	<b>14.3</b>
EBITDA	2,123	1,995	6	2,219	(4)	6,802	5,791	17.5
Other income	559	357	57	386	45	1,500	1,998	(24.9)
<b>PBIDT</b>	<b>2,682</b>	<b>2,353</b>	<b>14</b>	<b>2,605</b>	<b>3</b>	<b>8,302</b>	<b>7,789</b>	<b>6.6</b>
Depreciation	61	66	(7)	56	9	301	245	23.1
Interest	35	48	(27)	58	(39)	125	160	(22.1)
<b>PBT</b>	<b>2,586</b>	<b>2,239</b>	<b>16</b>	<b>2,491</b>	<b>4</b>	<b>7,876</b>	<b>7,384</b>	<b>6.7</b>
Tax	727	651	12	496	47	2,363	2,085	13.3
Profit from associates	23	21	-	14	-	0	0	-
<b>Adjusted PAT</b>	<b>1,836</b>	<b>1,567</b>	<b>17</b>	<b>1,982</b>	<b>(7)</b>	<b>5,313</b>	<b>5,082</b>	<b>4.6</b>
Extra ordinary income/ (exp.)	20	9	-	9	-	0	0	-
<b>Reported PAT</b>	<b>1,856</b>	<b>1,576</b>	<b>18</b>	<b>1,991</b>	<b>(7)</b>	<b>5,313</b>	<b>5,090</b>	<b>4.4</b>
No. of shares (mn)	331	331	-	331	-	331	331	-
EBITDA margin (%)	10.8	10.8	-	10.9	-	9.9	9.6	-
PBIDT margin (%)	13.6	12.7	-	12.8	-	12.0	12.9	-
<b>EPS - annualized (Rs)</b>	<b>22.2</b>	<b>19.0</b>	<b>17</b>	<b>24.0</b>	<b>(7)</b>	<b>16.1</b>	<b>15.4</b>	<b>4.6</b>

Source: Company, Axis Capital

(...continued from page 1)

- ♦ **EMP (31% of Q1FY18 revenue):** Sales grew 14% YoY to Rs 6.6 bn. Order book stood at Rs 49 bn up 11% YoY. EBIT margin improved 370 bps to 5.3% reflecting better quality of orders and efficient execution
  - **International operations:** As per management commentary, spending related to the mega events (Expo 2020 and FIFA 2022) has started picking up with projects being awarded to main contractors. The company has initiated number of measures to enhance labor productivity and build execution capabilities. It is monitoring situation in Qatar on a regular basis and steps have been taken to mitigate likely delays in project execution
  - **Domestic projects:** Performance was encouraging with over Rs 7 bn of new orders booked in Q1
- ♦ **Engineering products (4% of Q1FY18 revenue):** Sales grew 31% YoY at Rs 904 mn driven by higher capital machinery sales. EBIT margin was up 60 bps YoY to 28.4%

**Exhibit 2: Q1FY18 segmental performance**

(Rs mn)	Q1FY18	Q1FY17	% Chg	Q4FY17	% Chg	FY18E	FY17	% Chg
<b>Sales</b>								
Electro-Mechanical	6,608	5,802	14	8,290	(20)	29,205	26,550	10
Engg Prod & Services	904	691	31	1,068	(15)	3,816	3,318	15
Unitary Cooling	12,117	11,956	1	10,860	12	35,953	30,469	18
<b>EBIT</b>								
Electro-Mechanical	352	97	265	477	(26)	1,694	849	99
Margin (%)	5.3	1.7	-	5.7	-	6	3	-
Engg Prod & Services	257	193	34	259	(1)	1,099	956	15
Margin (%)	28.5	27.9	-	24.2	-	29	29	-
Unitary Cooling	1,706	1,779	(4)	1,781	(4)	5,033	4,403	14
Margin (%)	14.1	14.9	-	16.4	-	14	14	-

Source: Company, Axis Capital

## Financial summary (Consolidated)

### Profit & loss (Rs mn)

Y/E March	FY16	FY17	FY18E	FY19E
Net sales	57,198	60,328	68,974	78,939
Other operating income	-	-	-	-
<b>Total operating income</b>	<b>57,198</b>	<b>60,328</b>	<b>68,974</b>	<b>78,939</b>
Cost of goods sold	(40,871)	(42,359)	(48,972)	(56,046)
Gross profit	16,327	17,969	20,002	22,892
<i>Gross margin (%)</i>	<i>28.5</i>	<i>29.8</i>	<i>29.0</i>	<i>29.0</i>
Total operating expenses	(11,997)	(12,178)	(13,200)	(14,871)
<b>EBITDA</b>	<b>4,330</b>	<b>5,791</b>	<b>6,802</b>	<b>8,022</b>
<i>EBITDA margin (%)</i>	<i>7.6</i>	<i>9.6</i>	<i>9.9</i>	<i>10.2</i>
Depreciation	(264)	(245)	(301)	(331)
<b>EBIT</b>	<b>4,066</b>	<b>5,546</b>	<b>6,501</b>	<b>7,691</b>
Net interest	(158)	(160)	(125)	(110)
Other income	1,367	1,998	1,500	1,800
<b>Other pretax items</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>Profit before tax</b>	<b>5,275</b>	<b>7,384</b>	<b>7,876</b>	<b>9,381</b>
<i>Total taxation</i>	<i>(1,696)</i>	<i>(2,089)</i>	<i>(2,363)</i>	<i>(2,814)</i>
<i>Tax rate (%)</i>	<i>32.1</i>	<i>28.3</i>	<i>30.0</i>	<i>30.0</i>
Profit after tax	3,580	5,296	5,513	6,566
Minorities	1	(221)	(206)	(207)
Adjusted net profit	3,580	5,074	5,308	6,360
<i>Adj. PAT margin (%)</i>	<i>6.3</i>	<i>8.4</i>	<i>7.7</i>	<i>8.1</i>
Net non-recurring items	289	11	-	-
Reported net profit	3,869	5,085	5,308	6,360

### Balance sheet (Rs mn)

Y/E March	FY16	FY17	FY18E	FY19E
Paid-up capital	331	331	331	331
Reserves & surplus	23,621	32,735	36,926	41,838
Net worth	23,952	33,066	37,256	42,169
Borrowing	2,603	1,709	1,709	1,709
Other non-current liabilities	(511)	(198)	(198)	(198)
<b>Total liabilities</b>	<b>26,303</b>	<b>34,863</b>	<b>39,253</b>	<b>44,366</b>
Gross fixed assets	5,117	5,717	6,317	6,917
Less: Depreciation	(2,894)	(3,138)	(3,439)	(3,770)
Net fixed assets	2,224	2,579	2,878	3,147
Add: Capital WIP	-	-	-	-
Total fixed assets	2,224	2,579	2,878	3,147
Total Investment	15,257	20,683	20,683	20,683
Inventory	8,927	9,070	9,449	10,381
Debtors	13,066	14,541	15,118	17,302
Cash & bank	1,971	3,131	2,653	4,251
Loans & advances	2,856	2,747	3,022	3,324
Current liabilities	29,156	28,536	25,495	25,668
Net current assets	8,099	11,175	14,969	19,812
Other non-current assets	723	425	723	723
<b>Total assets</b>	<b>26,303</b>	<b>34,863</b>	<b>39,253</b>	<b>44,366</b>

Source: Company, Axis Capital

### Cash flow (Rs mn)

Y/E March	FY16	FY17	FY18E	FY19E
Profit before tax	5,275	7,384	7,876	9,381
Depreciation & Amortisation	264	245	301	331
<i>Chg in working capital</i>	<i>(806)</i>	<i>(517)</i>	<i>(4,405)</i>	<i>(3,387)</i>
<b>Cash flow from operations</b>	<b>2,661</b>	<b>1,797</b>	<b>169</b>	<b>1,962</b>
<i>Capital expenditure</i>	<i>(524)</i>	<i>(600)</i>	<i>(600)</i>	<i>(600)</i>
<b>Cash flow from investing</b>	<b>(3,475)</b>	<b>(4,028)</b>	<b>900</b>	<b>1,200</b>
<i>Equity raised/ (repaid)</i>	<i>-</i>	<i>-</i>	<i>-</i>	<i>-</i>
<i>Debt raised/ (repaid)</i>	<i>1,383</i>	<i>(894)</i>	<i>-</i>	<i>-</i>
<i>Dividend paid</i>	<i>(1,016)</i>	<i>(992)</i>	<i>(1,323)</i>	<i>(1,654)</i>
<b>Cash flow from financing</b>	<b>63</b>	<b>(2,051)</b>	<b>(1,452)</b>	<b>(1,767)</b>
Net chg in cash	(752)	(4,282)	(383)	1,395

### Key ratios

Y/E March	FY16	FY17	FY18E	FY19E
<b>OPERATIONAL</b>				
FDEPS (Rs)	10.8	15.3	16.0	19.2
CEPS (Rs)	12.5	16.1	17.0	20.2
DPS (Rs)	2.6	3.0	4.0	5.0
Dividend payout ratio (%)	22.2	19.5	24.9	26.0
<b>GROWTH</b>				
Net sales (%)	10.4	5.5	14.3	14.4
EBITDA (%)	5.6	33.8	17.5	17.9
Adj net profit (%)	5.9	41.7	4.6	19.8
FDEPS (%)	5.9	41.7	4.6	19.8
<b>PERFORMANCE</b>				
RoE (%)	15.9	17.8	15.1	16.0
RoCE (%)	6.8	8.5	8.8	10.2
<b>EFFICIENCY</b>				
Asset turnover (x)	2.6	2.1	2.0	2.0
Sales/ total assets (x)	1.1	1.0	1.1	1.2
Working capital/ sales (x)	0.1	0.1	0.1	0.2
Receivable days	83.4	88.0	80.0	80.0
Inventory days	61.6	60.7	55.5	53.4
Payable days	-	-	-	-
<b>FINANCIAL STABILITY</b>				
Total debt/ equity (x)	0.1	0.1	-	-
Net debt/ equity (x)	-	-	-	(0.1)
Current ratio (x)	1.3	1.4	1.6	1.8
Interest cover (x)	25.7	34.6	52.0	69.9
<b>VALUATION</b>				
PE (x)	50.0	35.3	33.7	28.1
EV/ EBITDA (x)	41.5	30.7	26.2	22.0
EV/ Net sales (x)	3.1	2.9	2.6	2.2
PB (x)	7.5	5.4	4.8	4.2
Dividend yield (%)	0.5	0.6	0.7	0.9
Free cash flow yield (%)	1.2	0.7	(0.2)	0.8

Source: Company, Axis Capital

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