Voltas

UCP segment to drive the future earnings

Voltas is a market leader in the domestic air conditioning space. The Unitary Cooling Products (UCP) division dealing in air conditioning products contributes dominantly to the company's overall revenues. The other two divisions are the Electro-Mechanical Projects (EMP) division and the Engineering Products Solutions division.

Growth in Unitary Cooling Products segment to continue: Voltas has maintained 20%+ market share in the domestic air-conditioning (AC) market, despite stiff competition from MNC players. Its 'numero uno' position is owing to its (1) wide distribution network (over 10,000 touch-points), (2) wide portfolio of 50+ models (new launches scheduled in 4QFY2016), (3) strong post-sale support (inc. 5-year warranty on compressor), and (4) strong advertising focus (Top 5 Media spender amongst AC players). With economic indicators turning favorable and summers ahead, the company's competitive positioning should help UCP segment to report 12.2% top-line and 10.0% EBIT CAGR, respectively, during FY2015-18E.

Gradual recovery in the EMP business: Voltas' EMP business is adversely affected due to the prevalent weak awarding environment, slow execution and cost over-runs. In run-up to Qatar World Cup 2022 and Dubai Expo 2020, we expect international awarding activity to gradually catch-up from FY2017E onwards. Surge in order book should translate to uptick in execution (we expect 7.3% top-line CAGR during FY2015-18E). With legacy projects nearing completion and contribution of high margin projects kicking-in, we expect segment margins to expand from 1.0% in FY2015 to 5.0% in FY2018E.

Balance Sheet strength: Voltas pursues an asset light business model, and in the due course of business, it resorts to outsourcing and strategic tie-ups, thereby enables it to control its operating costs and generate high profitability. As a result, we expect Voltas to revert to it its earlier trend of higher RoEs. Given the asset light business model, the company has been generating strong cash flows (it generated ₹618cr of cash flows from business during FY2013-15). As of 2QFY2016-end, Voltas is a debt free company (on net basis), with cash balance of ₹247cr.

Attractive Valuations: At the current market price of ₹304, Voltas is trading at FY2017E and FY2018E P/E multiple of 22.1x and 18.1x, respectively. With economic cues turning favorable, and given Voltas' strong market positioning within the AC space, coupled with an expected gradual recovery in its EMP segment, we expect the company to report 9.5% top-line and 13.1% bottom-line CAGR during FY2015-18E. Considering high contribution of UCP segment (72% of FY2015 EBIT) to overall profitability, and limited left-over legacy orders in the EMP segment, we have compared Voltas to Hitachi (which is trading at FY2018 P/E multiple of ~36.0x). **We assign Voltas a 21.0x P/E multiple to our FY2018E EPS estimate of ₹16.8 to arrive at a price target of ₹353. Given the upside, we initiate coverage on Voltas with a Buy rating.**

Key Financials

Y/E March (₹ cr)	FY13	FY14	FY15	FY16E	FY17E	FY18E
Net Sales	**5,531**	**5,266**	**5,183**	**5,363**	**5,963**	**6,808**
% chg	*6.7*	*(4.8)*	*(1.6)*	*3.5*	*11.2*	*14.2*
Net Profit	**208**	**245**	**384**	**364**	**455**	**556**
% chg	*28.2*	*18.1*	*56.6*	*(5.4)*	*25.2*	*22.1*
EBITDA (%)	4.4	5.0	7.9	8.0	9.1	9.8
EPS (₹)	**6.3**	**7.4**	**11.6**	**11.0**	**13.8**	**16.8**
P/E (x)	48.3	40.9	26.1	27.6	22.1	18.1
P/BV (x)	6.2	5.5	4.8	4.2	3.7	3.2
RoE (%)	12.8	14.2	19.6	16.2	17.9	19.1
RoCE (%)	19.3	22.4	36.4	35.9	37.3	38.3
EV/Sales (x)	1.8	1.9	1.9	1.8	1.6	1.4
EV/EBITDA (x)	40.8	37.7	24.2	22.7	17.7	13.9

Source: Company, Angel Research; Note: CMP as of December 18, 2015

BUY

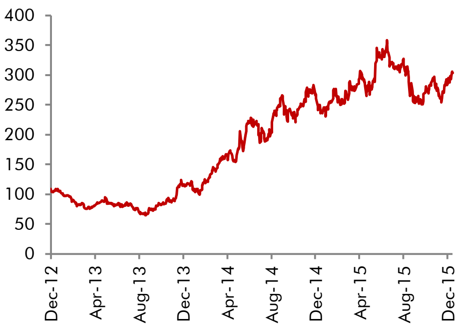
CMP	₹304
Target Price	₹353
Investment Period	12 Months

Stock Info	
Sector	Construction & Eng.
Market Cap (₹ cr)	10,054
Net debt (₹ cr)	(325)
Beta	1.3
52 Week High / Low	360/227
Avg. Daily Volume	1,683,183
Face Value (₹)	1
BSE Sensex	25,519
Nifty	7,762
Reuters Code	VOLT.BO
Bloomberg Code	VOLT@IB

Shareholding Pattern (%)	
Promoters	30.3
MF / Banks / Indian FIs	26.8
FII / NRIs / OCBs	21.1
Indian Public / Others	21.8

Abs. (%)	3m	1yr	3yr
Sensex	(2.6)	(7.9)	31.2
Voltas	17.1	21.5	179.7

3-Year Daily price chart



Source: Company, Angel Research

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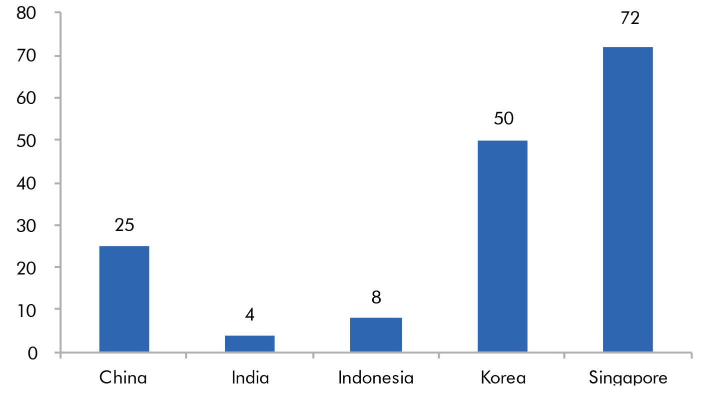
Investment Rationale

AC business growth story intact....

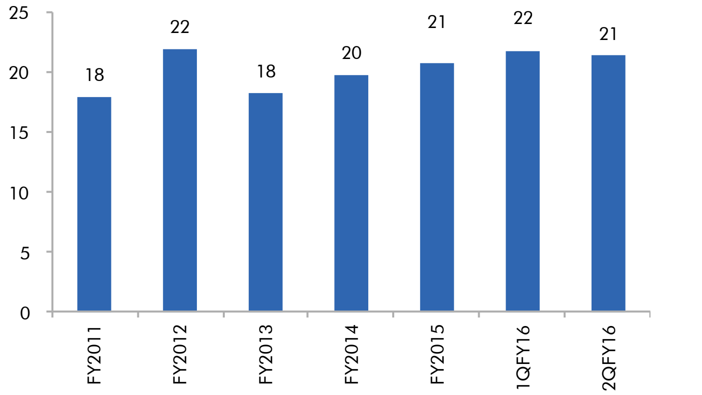
AC sales in India have been in the range of 3.5-3.75mn units annually for the last 2-3 years, lower than the commensurate sale in China of 55mn units. Currently, AC penetration in India stands at ~4% vs ~25% in China and ~50% in Korea. Various industry participants indicate that AC sales should see a strong 10-15% growth for the next 3-5 years, given the current low penetration levels.

Exhibit 1: AC Sales Penetration (%)



Source: Company, Angel Research

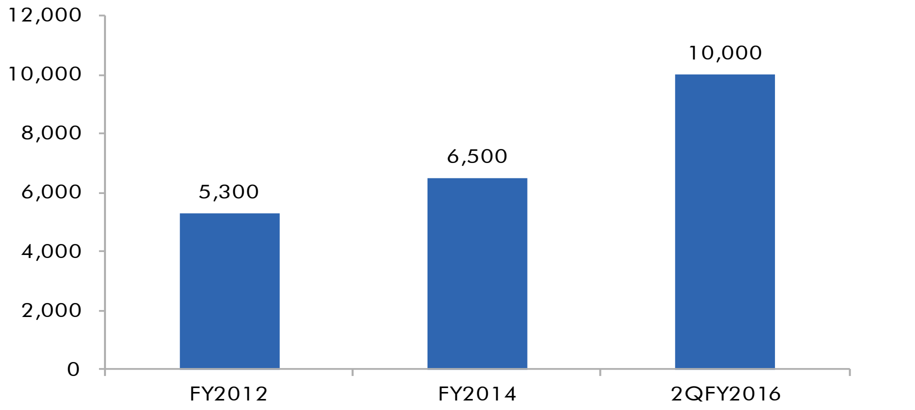
Exhibit 2: Voltas' Market share



Source: Company, Angel Research

The UCP segment reported 16.9% top-line CAGR during FY2013-15 to ₹2,510cr. Voltas' market share grew from ~18% in FY2013 to 21% levels as of 2QFY2016-end. The market share gain, as per our sense, came on the back of the following reasons, (1) growth in dealership/touch points network from 5,300 in FY2012 to over 10,000 as of 2QFY2016-end, (2) strong penetration into multi-brand dealers' network (where it enjoys high market share), (3) strong sales network in Tier II and III cities (account for almost half of the total AC sales), (4) successful poaching of top talent from its peers, (5) focus on post sale support (which includes 5-year warranty on compressors), (6) initiating strong advertising campaigns to create a distinct brand (Voltas is among the top-5 spenders on television and print media advertising among the AC players), (7) focus on product innovation, and (8) tie-ups with more financing firms.

Exhibit 3: Voltas- Number of sale touch-points

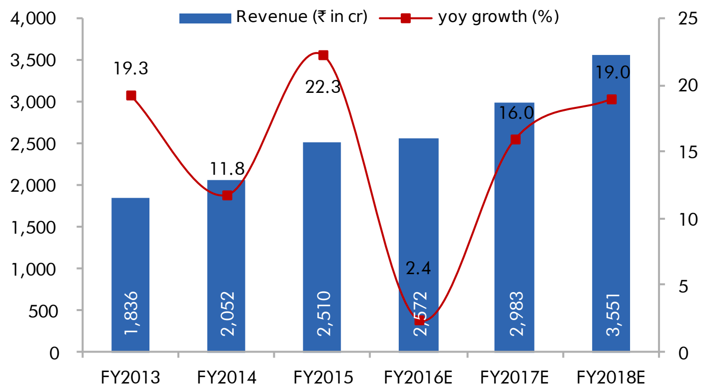


Source: Company, Angel Research

Unfavorable climate for the AC business in North India (accounts for 50% of Voltas' AC sales) led to ~10% yoy de-growth in the company's sales across North India in 1HFY2016. Despite weak North India sales, in a cut throat competitive scenario with some players resorting to price cutting, Voltas maintained 21% of the market share as of 2QFY2016.

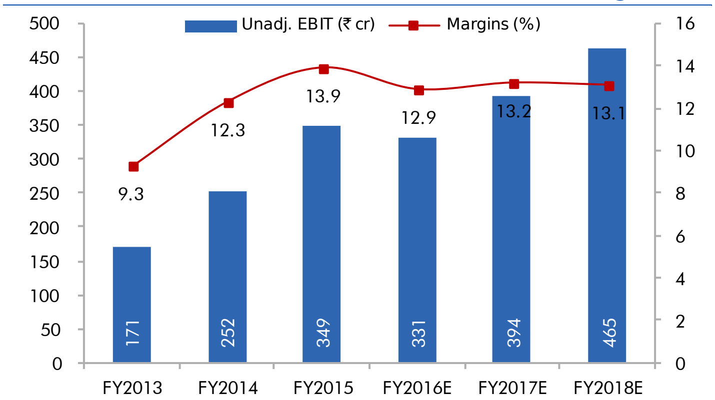
Given the low AC penetration in India, gradual uptick in the economy and rising urbanization, we expect AC sales to report strong 10-15% yoy growth for the next 3-5 years. Considering Voltas' strong market positioning and its entry into the Air-Coolers segment, we expect its sales to grow at par with the industry. This should lead to Voltas sustaining its over-20% market share. On the whole, we expect the UCP segment to report 12.2% top-line CAGR during FY2015-18E.

Exhibit 4: To maintain leadership position in AC business



Source: Company, Angel Research

Exhibit 5: EBIT % to stabilise at ~13% levels in UCP segment



Source: Company, Angel Research

In the last few years, consumer buying preferences have shifted towards Split ACs in comparison to Window ACs, which were more in demand earlier. Over the years, this has resulted in a shift in the segment product mix, with increased contribution of Split ACs vs Window ACs. The company in delivering products of superior quality. There have been provision write-backs, thereby contributing to segment margin expansion (from 10.1% in FY2010 to 13.9% in FY2015). Despite, correction in raw material prices, we expect Voltas to feel the heat of competition from MNCs. Accordingly we expect Voltas to report segment margins of ~13.0% levels during FY2016-18E.

EMP business to recover gradually....

Weak awarding activity, payment delays, client specific issues at some large ticket projects (these projects were won on fixed cost basis, and they experienced cost escalations on account of client side design changes and other business reasons), led Voltas to report a negative 16.9% top-line CAGR during FY2013-15 to ₹2,209cr. Similarly, segment margins during the same period were under pressure owing to (1) zero level margins being booked from SIDRA project, (2) higher provisions for some of the projects in order to comply with AS-7, (3) execution of fixed cost projects in international markets, which were won at cut throat competition, and (4) execution delays (owing to design changes from the client side).

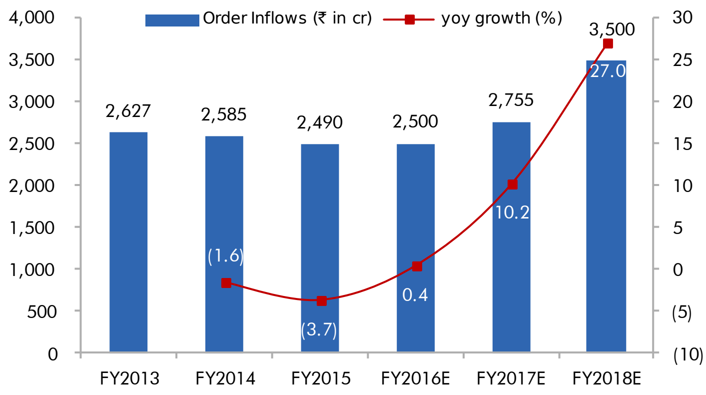
The Management highlighted that currently the domestic market is characterised by limited awarding activity, high competition from the local players and stretched working capital cycles. Realising the emerging business dynamics, Voltas is following selective business strategy, with emphasis on cash flow profile and project level profitability. Management expects recovery in capex and gradual uptick in the domestic EMP segment awarding scenario from FY2017E onwards.

In the Middle East markets, correction in oil prices has raised concerns of a slowdown in the capex cycle in the region. 2 mega events are slated in the Middle East, going forward, ie the Dubai Expo 2020 and the Qatar Football World Cup 2022. In the run-up to preparation for these 2 events, we expect awarding to pick-up in Qatar and UAE from FY2017E onwards. We do not expect awarding activity to be affected due to the corrective trend in oil prices as both of these countries are gas dependent and are borrowing economies.

Voltas restructured its business approach as well as its operations. The company (1) has made leadership changes and strengthened its operations team by defining the business boundaries, (2) defined new parameters, which would indicate whether or not to bid for a project, and (3) is now resolving to a selective approach while bidding for new projects with a focus on accruing reasonable margins rather than following a turnover based growth approach.

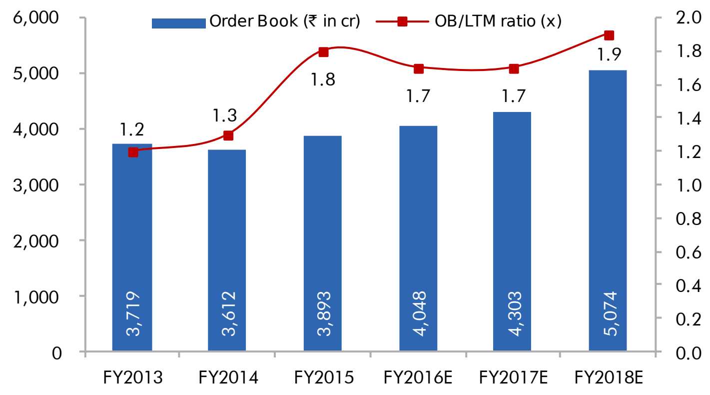
Given the company’s resolve to follow a selective bidding strategy, we expect it to report 5.2% order inflow CAGR during FY2015-17E. With uptick in awarding activity in the Middle East, we expect Voltas to report a 27.0% yoy increase in its FY2018E order inflows to ₹3,500cr.

Exhibit 6: Order Inflows to gradually catch-up...



Source: Company, Angel Research

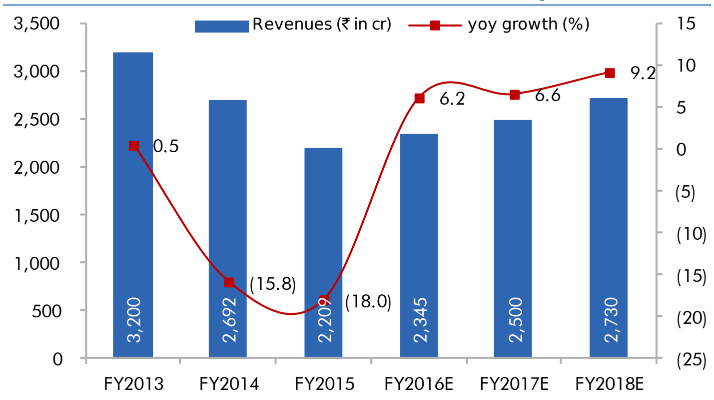
Exhibit 7: OB/LTM sales ratio to improve to 1.9x...



Source: Company, Angel Research

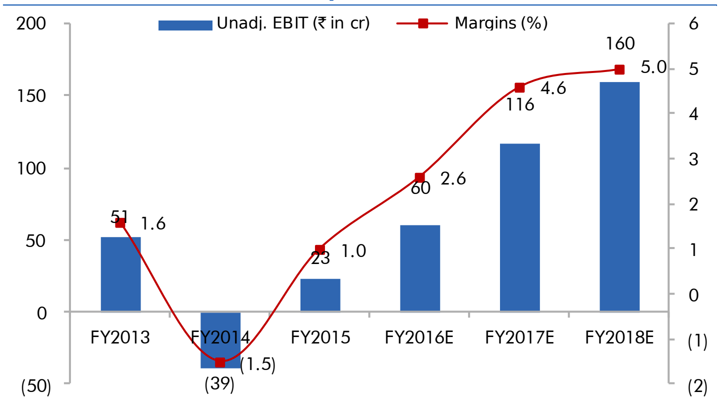
The EMP segment's order book as of 2QFY2016-end stands at ₹3,599cr, reflecting order book to Last Twelve Month (LTM) sales ratio of 1.6x. Domestic orders constituted ~52%, whereas the remaining orders are from the international markets (mainly from Middle East countries like Qatar, UAE and Oman). Despite weak near-term awarding trends, we expect gradual recovery in the domestic and international business from FY2017E onwards. Recovery in order wins should be followed by uptick in execution. Accordingly, we expect a 9.2% order book CAGR during FY2015-18E to ₹5,074cr.

Exhibit 8: Execution momentum to catch-up...



Source: Company, Angel Research

Exhibit 9: EBIT % set to expand from here-on...



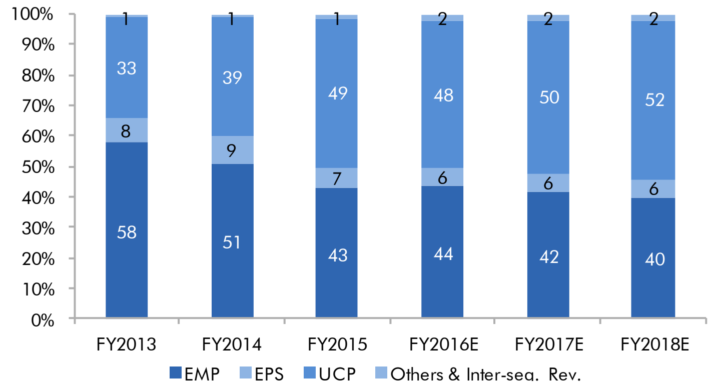
Source: Company, Angel Research

At the back-drop of uptick in new order wins, we expect execution to catch-up, resulting in 7.3% top-line CAGR during FY2015-18E to ₹2,730cr. Voltas' Management has highlighted that all the legacy projects in the order book would get completed in FY2016E. Post completion of these projects, the Management would be executing the recently won good margin orders (4-5% EBIT margins), which in their view have come at reasonable commercial terms. Accordingly, we expect the EMP segment to report 91.4% EBIT CAGR during FY2015-18E (EBIT margins to expand from 1.0% in FY2015 to 5.0% in FY2018E).

Earnings growth to be driven by UCP segment...

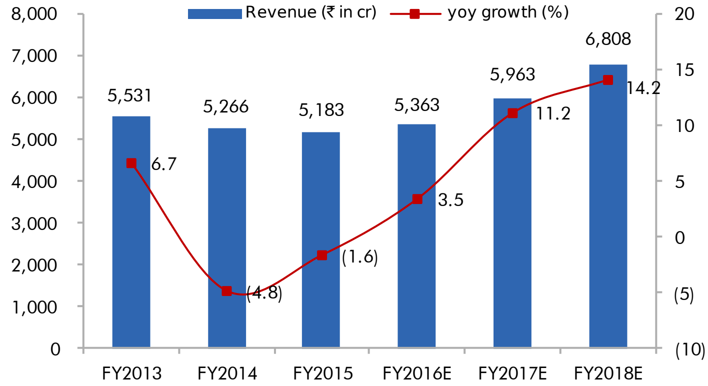
Growth across Voltas during FY2013-15 has been driven by the UCP segment, which reported 16.9% top-line and 42.7% EBIT CAGR, respectively. Negative 33.3% EBIT CAGR from the EMP segment, during the same period, was offset by a favorable performance from the UCP segment. In other words, the EMP segment's contribution to EBIT mix in the last few years has declined from 16.7% in FY2013 to 4.7% in FY2015. We expect the EMP segment to report 6.2% revenue CAGR during FY2015-17E and from there-on, on the back of new order wins, the segment is expected to report a revenue growth of 9.2% yoy in FY2018E.

Exhibit 10: Segment-wise Revenue mix movement



Source: Company, Angel Research

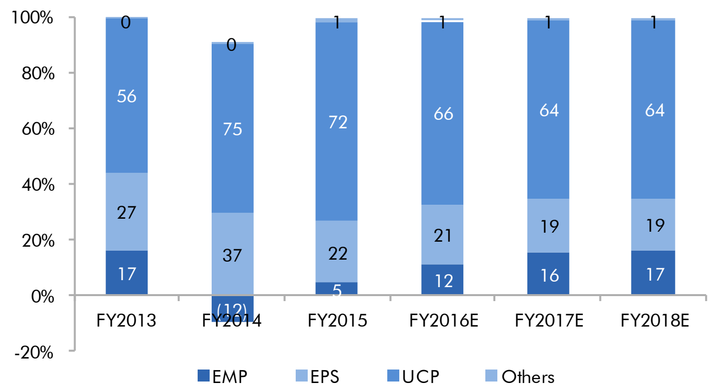
Exhibit 11: Consol. Revenue & yoy growth



Source: Company, Angel Research

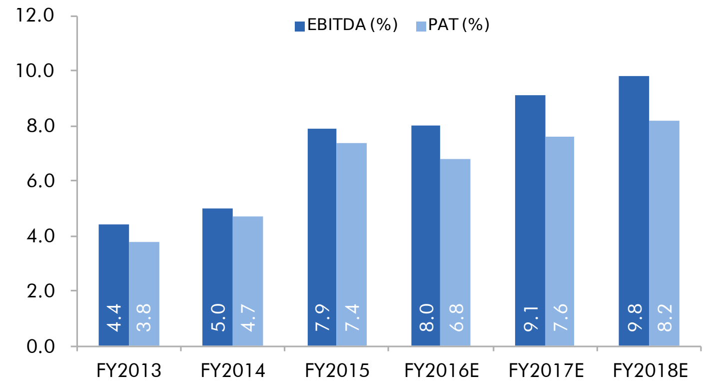
On considering (1) expected structural uptick in domestic AC industry for next 3-5 years, (2) strong market positioning of Voltas within the domestic AC industry, (3) wide pan-India distribution network (with over 10,000 touch points), and (4) strong brand perception enjoyed by Voltas, we are optimistic that the UCP segment's contribution to overall business would remain so. We expect the UCP segment to report a 12.2% top-line and 10.0% bottom-line CAGR during FY2015-18E, respectively. With legacy projects nearing completion (by FY2016E) and possible increase in contribution of newly won projects at 4-5% EBIT margins, we are optimistic that the EMP segment would make a meaningful 17% contribution to the consol. EBIT in FY2018E.

Exhibit 12: Segment-wise EBIT mix movement



Source: Company, Angel Research

Exhibit 13: Consol. EBITDA & PAT Margins



Source: Company, Angel Research

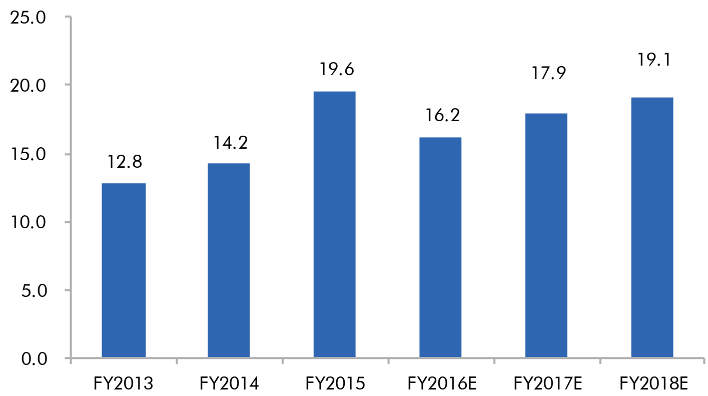
In a highly competitive AC sales environment, characterized by competitors resorting to price cuts, we expect Voltas to be less affected. Our view stems on account of the following, (1) Voltas' ACs are competitively priced vis-a-vis its peers (which until now have focused on maintaining higher realizations), (2) sharp fall in commodity prices, especially copper, (3) emphasis on advertising (Voltas has been among the top-5 ad spenders in the AC industry), and (4) one of the few players with strong post-sale support (offers 5-year warranty for compressors). We expect the UCP segment to maintain its EBIT margins ~13.0% levels during FY2016-18E.

On a whole, UCP segment should help Voltas report a 9.5% top-line and 13.1% bottom-line CAGR during FY2015-18E.

Strong Balance Sheet & Return ratios…

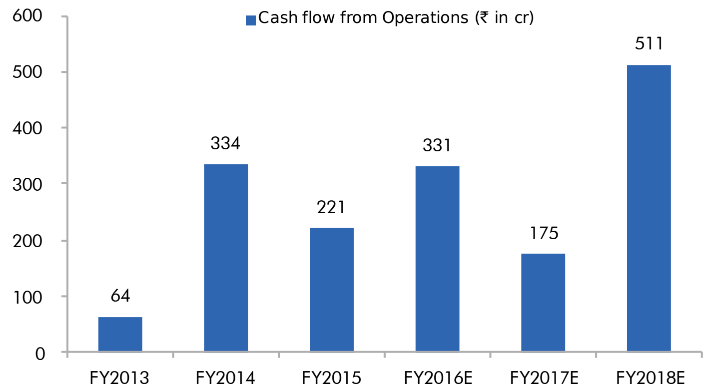
Voltas pursues an asset light business model, and in the due course of business, it does outsourcing and strategic tie-ups, thereby helping it in controlling operating costs and generating high profitability ratios (vs other infrastructure & EMP players). As a result, the company has been able to maintain higher RoEs. Given the asset-light nature of Voltas' business, the company has generated ₹618cr of cash flow from operations during FY2013-15. At 2QFY2016-end, Voltas is a debt free company (on net basis), sitting on a cash balance of ₹247cr. Its strong balance sheet position gets reflected in its RoEs, which expanded from 12.8% in FY2013 to 19.6% in FY2015. Considering that the cash flow generating potential of the company would be maintained going forward, we expect Voltas to report 16-19% RoEs for FY2016-18E.

Exhibit 14: Return on Equity (%)



Source: Company, Angel Research

Exhibit 15: Cash flow from Operations

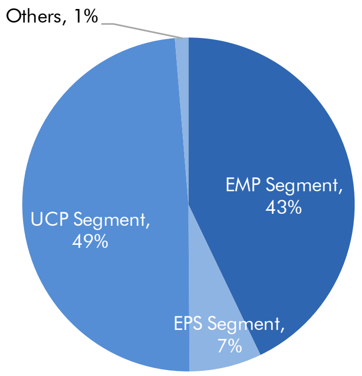


Source: Company, Angel Research

Understanding the Business Model

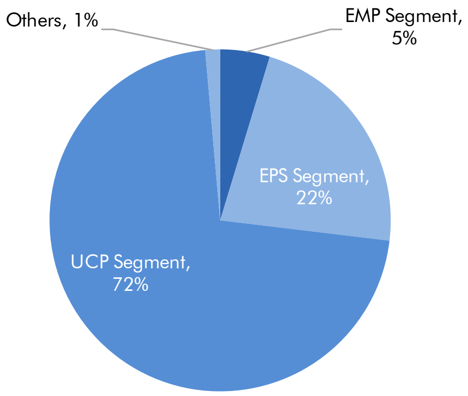
Voltas conducts its entire business under 3 key heads, namely Unitary Cooling Products (UCP), Electro Mechanical Projects & Services (EMP) and Engineering Products & Services (EPS). Amongst the 3 business segments, UCP is the largest one, with it having contributed ~49% and ~72% of FY2015 consolidated revenues and EBIT, respectively.

Exhibit 16: FY2015- Consol. Revenue Mix



Source: Company, Angel Research

Exhibit 17: FY2015- Consol. unadj. EBIT Mix



Source: Company, Angel Research

(A) Electro Mechanical Projects & Services (EMP) segment

Voltas, in the last two decades, has transformed itself from being a HVAC (Heating, Ventilation and Air-Conditioning) player to EMP (Electro Mechanical Projects & Services) player. With larger ticket size projects being awarded, the trend of awarding the entire MEP project to a single vendor has gained prominence. The current scope of work under the EMP segment includes Heating, Ventilation, Air Conditioning, Power Management, Control Systems, Lightning Systems, Fire Detection & Alarm, Water Treatment Systems, Rain Gutter Systems, Sewerage Removal System and Fire Fighting System. For a given Building/ Hospital Building/ Education Building, the scope of MEP works account for ~35% of the project cost in India. Whereas in the developed world, the share of MEP works in a complex project can increase up to 40-45% of the total project cost.

If we look at the geographical split within the segment, then the international business contributed 60%+ of segment revenues, with the remaining contribution coming in from domestic markets. Again, within international markets, a substantial chunk of revenues would flow-in from the Middle East markets (especially Qatar, UAE and Oman).

The EMP business is a key business for Voltas, as this segment contributed ~49% of average consol. revenues over FY2013-15. Despite strong top-line contribution, large cost overruns across international business led to segmental EBIT level losses in FY2012 and FY2014.

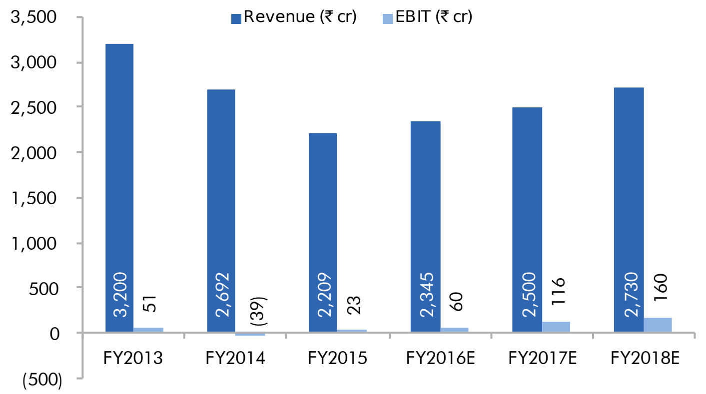
OB/ LTM sales ratio at 1.6x gives revenue visibility...

The EMP segment's order book as of 2QFY2016-end stands at ₹3,599cr, reflecting order book to Last Twelve Months (LTM) sales ratio of 1.6x. Domestic orders constitute ~52%, whereas remaining orders are from international markets (mainly from Middle East countries like Qatar, UAE and Oman). Despite weak near-term awarding trends, we expect recovery going forward led by international business from FY2017E onwards. Our assumption on recovery from international markets is on factoring an expected catch-up in awarding in run-up to FIFA 2022 and Dubai Expo 2020 events.

During FY2012-15, the segment's performance (mainly the international business) was impacted due to ongoing disputes with clients (as projects were won on fixed cost basis, and were experiencing cost escalations, on account of client side design changes and other business reasons). On the whole, cut-throat competition in a weak awarding environment led to weak execution and payment delays. As a result, Voltas' Management went ahead and restructured its operations as well as its business.

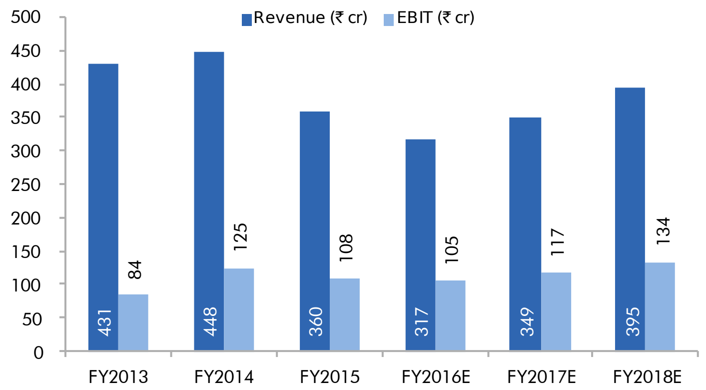
Voltas' Management has (1) made leadership changes and strengthened its operations team by defining business boundaries, (2) defined new parameters, which would indicate whether or not to bid for a project, (3) resolved to a selective bidding strategy (focusing on new projects with reasonable margins instead of following a turnover growth approach). These initiatives coupled with declining proportion of low margin legacy projects indicate that margins are likely to expand. Accordingly, we expect the segment's EBIT margins to expand from 1.0% in FY2015 to 5.0% in FY2018E.

Exhibit 18: EMP Segment Financials



Source: Company, Angel Research

Exhibit 19: EPS Segment Financials



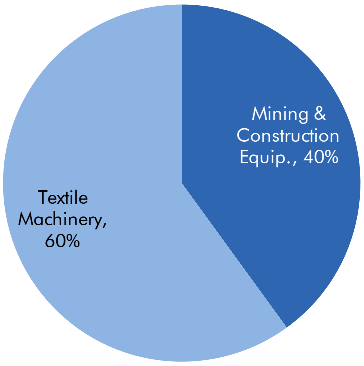
Source: Company, Angel Research

(B) Engineering Products & Services (EPS) segment

The Engineering Products and Services (EPS) segment sells machinery and equipment across 2 sub-verticals, namely, (1) Textile Machinery, and (2) Mining & Construction Equipment. Voltas generates revenues from this segment in the form of commission and non-commission revenues. Commission income comes from the distribution of textiles as well as mining & construction equipment, as the company does not manufacture these equipments. Non-commission income mainly includes income from maintenance contract services drawn from equipments sold.

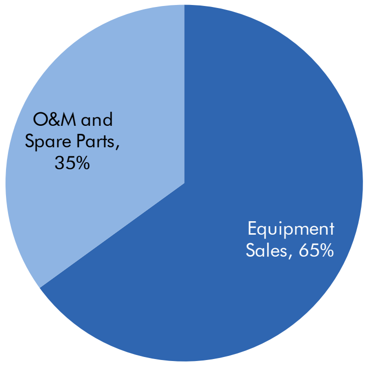
This segment showed flattish yoy revenue growth trend during FY2013-14, except in FY2015-1QFY2016, when the company reported yoy de-growth. This de-growth was owing to slowdown seen across the domestic mining industry, impact of regulatory clam-downs on the mining sector and loss of clients (such as Caterpillar) owing to global consolidation.

Exhibit 20: Sub-Segment Revenue mix (as of FY2015)



Source: Company, Angel Research

Exhibit 21: Business-wise Revenue mix (as of FY2015)



Source: Company, Angel Research

Voltas acts as an agent for sale of machinery (Indian as well as foreign) across the entire value chain of the textile industry, namely spinning, weaving, knitting, processing and finishing applications. The company's key principals include- Lakshmi Machine Works (LMW; which has a major chunk of market share in the domestic textile equipment industry) from India, and Terrot and Thies GmbH from the international market.

The textile industry in India is currently undergoing tough times given the exports decline in China, excess capacity in the domestic markets, muted yarn prices and technological advancements happening within the sector (especially weaving, knitting & processing and finishing divisions). Lack of clarity on the government plan to extend support towards Technology Up gradation Fund Scheme (TUFS) is leading to subdued demand. Despite these adversaries, spurt in demand from some states held the sub-segment revenue growth in 2QFY2016.

After a few quarters of muted performance, the Mining & Construction Equipment sub-segment has reported some signs of growth in 2QFY2016. The mining equipment sector has been impacted due to re-tendering activity and delays in uptick in the capex cycle.

Within the Mining & Construction Equipment sub-segment, low contribution from the domestic business was offset up to a certain extent by high revenue contribution from the African markets (especially from the Mozambique business). In-line with the Management's commentary, we expect FY2016 to be a weak year for the company. Thereafter, we expect gradual uptick in the segment's business. The Management has highlighted that strategic focus on the spare parts and servicing business, maintaining strong customer relations, uptick in construction activity, as well as diversification into the post spinning space (within the Textiles Machinery space) should help the segment report growth, going forward. On the whole, we expect this segment to report a 3.1% top-line CAGR during FY2015-18E to ₹395cr.

Despite a weak 1HFY2016 in terms of revenues, the reported EBIT margin stood impressive at ~35% levels, owing to strong service business contribution from the Mozambique markets. We expect the segment's EBIT margin to be at ~33% levels going forward during FY2016-18E (vs 30.0% in FY2015).

(C) Unitary Cooling Products (UCP) segment

Voltas has built a strong brand name and has emerged as one of the largest air conditioner players with in the domestic AC markets. At 2QFY2016-end, as per a report by AC Neilson, Voltas enjoys 21% market share of the Indian AC market, with the second nearest competitor having a market share lower by ~400bp.

Apart from being present in the domestic AC market, Voltas has gone ahead and deployed cooling solutions expertise towards Cold Chain Storage, Retail and Food Processing industries. The Commercial Refrigeration sub-segment's offerings include Package and Ductable Air conditioners, VRF Technology, and Chillers. The current product range includes Voltas' in-house manufactured product range: ie Package and Ductable Air conditioners: 5.5-22 TR (Ton of refrigeration); Chillers range include- Screw Chiller Packages: 80-500 TR; Scroll Chillers: 12-100 TR and Vapour Absorption Machines: 40-1,450 TR.

Home AC penetration in India currently stands at ~4%, well below 50-70% levels across developed nations and 25-40% levels across some of developing nations (includes countries like Thailand and Malaysia). On account of growing disposable incomes, upcoming summer season, declining maintenance costs, attractive consumer financing options and increased availability of power, we expect penetration levels in the Indian AC market to reach 10% over the next 5 years. Expected surge in the penetration levels translates to ~10-15% increase in the market size over the next 3-5 years.

The UCP segment contributed ~49% of the FY2015 consol. revenues and ~72% of the FY2015 consol. EBIT. Of the FY2015 UCP segment sales, the AC business contributed ~75.0% of segment sales (total of ~0.4cr ACs were sold vs assembly line capacity of ~0.7cr ACs) and remaining ~25.0% were from the Commercial Refrigeration business.

UCP segment has reported impressive 16.9% revenue CAGR during FY2013-15, reflecting (1) market leadership position in domestic AC market, (2) wide pan-India distribution network (with over 10,000 touch points), and (3) strong brand perception being enjoyed by Voltas. The AC market in India reported de-growth in 1HFY2016, owing to ~10% de-growth seen across one of the largest AC markets in India, ie North India. Strong market positioning in a growing AC market, coupled with new product launches (scheduled in 4QFY2016), wide distribution reach, entry into Air-Coolers space (expect to sell 1 lakh units p.a. by third year), and strong post-sales support should help the UCP segment report 12.2% revenue CAGR (on a high base) during FY2015-18E. Our assumptions capture a muted 2.4% yoy segment growth for FY2016, reflecting 1H numbers and strong sales witnessed in the festive season. Seasonality aspect to AC sales has been declining as urban India is looking upon ACs as a necessity. Accordingly, we expect 16.0% and 19.0% yoy revenue growth in FY2017-18E.

Owing to shift in the product mix and higher sales of better quality product mix, the company has reversed its provisions, resulting in improvement in the EBIT margins. EBIT margins of the segment improved from 9.3% in FY2013 to 13.9% in

FY2015. Despite stiff competition, correction in raw material prices should support EBIT margins at 13%+ levels.

Valuation

At the current market price of ₹304, based on our estimates, the stock is trading at FY2017E and FY2018E P/E of 22.1x and 18.1x, respectively.

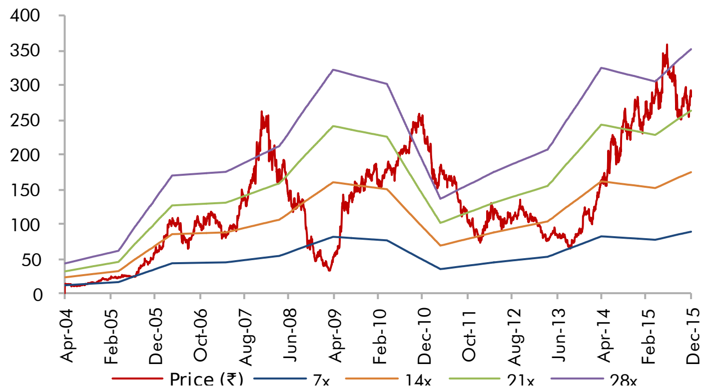
With inflation under control, rate cuts announced, when coupled with Voltas' strong positioning in the lowly penetrated AC market, comforts us that AC sales should continue to report strong growth, going forward. In FY2015, the UCP segment contributed ~72% of the consol. EBIT.

Also, completion of low margin EMP projects and increased contribution of high margin projects indicate that the EBIT margins of the EMP segment would improve from 1.0% in FY2015 to 5.0% in FY2018E.

On the whole, we expect Voltas to report a top-line and bottom-line CAGR growth of 9.5% and 13.1% during FY2015-18E, respectively. Our growth assumption captures (a) pick-up in international award activity, which should lead top-line growth as well as EMP segment EBIT margin expansion, (b) continued growth in domestic AC sales, with Voltas being able to retain its 'Numero Uno' status.

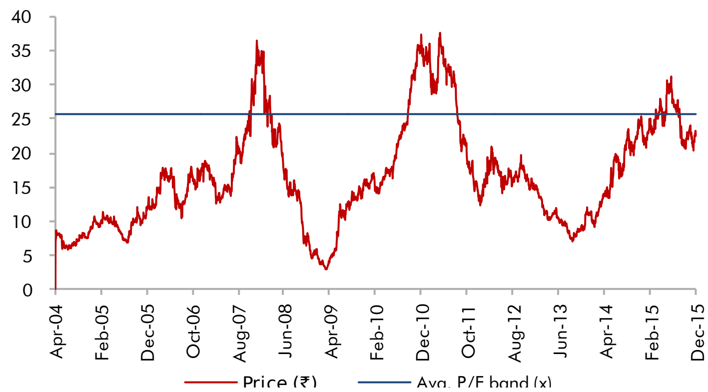
Noticeably in the last few years, the EBIT mix of Voltas has shifted from being heavily dependent on the EMP segment to a now dominant share of the UCP segment. The contribution of the UCP segment in the consol. EBIT has increased from 32% in FY2011 to 72% in FY2015. We expect the same to be over 64% levels during FY2016-18E. Considering the shift in the consol. EBIT mix, positive cues, and case for improvement in the business segments' performances, we expect scope for improved profitability and better investment return ratios, going forward. Considering the higher dependency on the UCP segment, we have compared Voltas to Hitachi (which is trading at a FY2018 P/E multiple of ~36.0x). We assign Voltas a 21.0x PE multiple to our FY2018E EPS estimate of ₹16.8/share and arrive at a price target of ₹353. This reflects 16% upside potential from the current levels. **We initiate coverage on Voltas with a BUY rating from a 12-month perspective and price target of ₹353.**

Exhibit 22: 1-year forward P/E band (x)



Source: Angel Research

Exhibit 23: 1-year forward Avg. P/E band (x)



Source: Angel Research

Risks to our Estimates

- AC sales contributed ~36% of FY2015 consolidated revenues. Given that Voltas is present only in the AC business across the entire Consumer Durables space, loss of major market share could act as a risk to our estimates. Any such development could lead to lower than expected EBIT contribution to the consol. profits and our estimates.
- Revenues from EPS segment are based on agreement for supplying Textile, Mining & Construction equipment. Any termination of such agreements shall impact our forecasted revenues for the segment.
- Most of the long term international projects are fixed price contracts and in the due course of its business, Voltas also imports. Any, adverse currency fluctuations may impact the raw material pricing as well as margins.
- Cancellation of Qatar World Cup 2022 or Expo 2020 could affect our EMP segment assumptions.

Profit and Loss Statement

Y/E March (₹ cr)	FY13	FY14	FY15	FY16E	FY17E	FY18E
Net Sales	**5,531**	**5,266**	**5,183**	**5,363**	**5,963**	**6,808**
% Chg	*6.7*	*(4.8)*	*(1.6)*	*3.5*	*11.2*	*14.2*
Total Expenditure	**5,287**	**5,000**	**4,773**	**4,935**	**5,419**	**6,141**
Cost of Raw Mat. Consumed	4,167	3,854	3,597	3,728	4,094	4,665
Employee benefits Expense	633	595	590	612	671	763
Other Expenses	487	551	586	594	654	713
EBITDA	**244**	**266**	**410**	**428**	**544**	**667**
% Chg	*(27.5)*	*8.9*	*54.4*	*4.4*	*27.1*	*22.6*
EBIDTA %	*4.4*	*5.0*	*7.9*	*8.0*	*9.1*	*9.8*
Depreciation	28	25	28	27	30	32
EBIT	**216**	**241**	**382**	**401**	**513**	**635**
% Chg	*(28.6)*	*11.4*	*58.7*	*4.9*	*28.1*	*23.6*
Interest and Financial Charges	38	23	23	17	13	8
Other Income	90	100	109	111	131	142
PBT	268	318	467	495	631	768
Exceptional Items	12	22	46	11	0	0
Prior Period Adjustments	0	0	0	0	0	0
Tax	73	94	128	142	177	215
% of PBT	*27.2*	*29.6*	*27.3*	*28.6*	*28.0*	*28.0*
PAT from ordinary activities	207	246	386	364	454	553
Share of Profit / (loss of Ass.) & Minority Int. in (profit)/ loss	1	(0)	(2)	(1)	1	3
PAT	**208**	**245**	**384**	**364**	**455**	**556**
% Chg	*28.2*	*18.1*	*56.6*	*(5.4)*	*25.2*	*22.1*
PAT %	*3.8*	*4.7*	*7.4*	*6.8*	*7.6*	*8.2*
Diluted EPS	6.3	7.4	11.6	11.0	13.8	16.8
% Chg	*28.2*	*18.1*	*56.6*	*(5.4)*	*25.2*	*22.1*

Balance Sheet

Y/E March (₹ cr)	FY13	FY14	FY15	FY16E	FY17E	FY18E
Sources of Funds						
Equity Capital	33	33	33	33	33	33
Reserves & Surplus Total	1,593	1,786	2,069	2,340	2,674	3,075
Networth	**1,626**	**1,819**	**2,102**	**2,373**	**2,707**	**3,108**
Total Debt	261	263	122	185	85	70
Minority Interest	12	14	16	18	18	18
Long-term Liabilities & Prov.	120	122	130	150	153	156
Total Liabilities	**2,019**	**2,218**	**2,370**	**2,725**	**2,963**	**3,351**
Application of Funds						
Gross Block	406	459	455	496	521	548
Accumulated Depreciation	195	251	266	293	324	355
Net Block	**211**	**209**	**189**	**203**	**198**	**192**
Capital WIP	0	2	4	8	6	7
Goodwill	89	80	80	80	80	80
Investments	**407**	**732**	**1,094**	**1,068**	**1,078**	**1,083**
Deferred Tax Assets	24	26	37	46	46	46
Inventories	978	901	867	923	1,042	1,190
Sundry Debtors	1,362	1,335	1,339	1,304	1,465	1,673
Cash and Bank Balance	350	282	252	510	484	851
Loans & Advances & Oth. Current Assets	1,041	1,027	922	1,057	1,151	1,317
Current Liabilities	2,548	2,527	2,519	2,609	2,732	3,226
Net Current Assets	**1,183**	**1,018**	**861**	**1,186**	**1,410**	**1,806**
Other Assets	104	152	105	135	145	136
Total Assets	**2,019**	**2,218**	**2,370**	**2,725**	**2,963**	**3,351**

Cash Flow Statement

Y/E March (₹ cr)	FY13	FY14	FY15	FY16E	FY17E	FY18E
Profit before tax	243	257	434	495	631	768
Depreciation	22	19	22	27	30	32
Other Adjustments	(147)	(40)	(248)	14	(61)	(61)
Change in Working Capital	21	164	83	(76)	(257)	(17)
Interest & Financial Charges (net)	17	8	10	12	8	4
Direct taxes paid	(92)	(74)	(80)	(142)	(177)	(215)
Cash Flow from Operations	**64**	**334**	**221**	**331**	**175**	**511**
(Inc)/ Dec in Fixed Assets	8	(20)	210	(44)	(23)	(27)
(Inc)/ Dec in Invest. & Int. received	36	(273)	(269)	26	56	62
Cash Flow from Investing	**44**	**(292)**	**(59)**	**(19)**	**33**	**34**
Inc./ (Dec.) in Borrowings	34	(19)	(140)	63	(100)	(15)
Issue/ (Buy Back) of Equity	0	0	0	0	0	0
Dividend Paid (Incl. Tax)	(61)	(57)	(64)	(93)	(121)	(155)
Finance Cost	(26)	(17)	(16)	(17)	(13)	(8)
Cash Flow from Financing	**(53)**	**(93)**	**(221)**	**(46)**	**(234)**	**(178)**
Inc./(Dec.) in Cash	**54**	**(51)**	**(59)**	**266**	**(27)**	**367**
Opening Cash balances	**200**	**255**	**203**	**144**	**410**	**384**
Closing Cash balances	**255**	**203**	**144**	**410**	**384**	**751**

Key Ratios

Y/E March	FY13	FY14	FY15	FY16E	FY17E	FY18E
Valuation Ratio (x)						
P/E (on FDEPS)	48.3	40.9	26.1	27.6	22.1	18.1
P/CEPS	42.6	37.2	24.4	25.7	20.7	17.1
Dividend yield (%)	0.6	0.6	0.7	0.8	1.0	1.3
EV/Sales	1.8	1.9	1.9	1.8	1.6	1.4
EV/EBITDA	40.8	37.7	24.2	22.7	17.7	13.9
EV / Total Assets	4.9	4.5	4.2	3.6	3.3	2.8
Per Share Data (₹)						
EPS (Diluted)	6.3	7.4	11.6	11.0	13.8	16.8
Cash EPS	7.1	8.2	12.5	11.8	14.7	17.8
DPS	1.9	1.9	2.3	2.4	3.2	4.0
Book Value	49.1	55.0	63.5	71.7	81.8	93.9
Returns (%)						
RoCE (Pre-tax)	19.3	22.4	36.4	35.9	37.3	38.3
Angel RoIC (Pre-tax)	16.2	16.4	22.1	20.0	23.1	24.4
RoE	12.8	14.2	19.6	16.2	17.9	19.1
Turnover ratios (x)						
Asset Turnover (Gross Block) (x)	13.6	12.2	11.3	11.3	11.7	12.7
Inventory / Sales (days)	65	65	62	61	60	60
Receivables (days)	90	93	94	90	85	84
Payables (days)	113	116	112	108	101	98
NWC days	41	43	45	43	44	46
Leverage Ratios (x)						
Net D/E ratio (x)	(0.1)	(0.0)	(0.1)	(0.1)	(0.1)	(0.3)

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Disclosure of Interest Statement	Voltas
1. Analyst ownership of the stock	No
2. Angel and its Group companies ownership of the stock	No
3. Angel and its Group companies' Directors ownership of the stock	No
4. Broking relationship with company covered	No

Note: We have not considered any Exposure below ₹1 lakh for Angel, its Group companies and Directors

Ratings (Based on expected returns over 12 months investment period):	Buy (> 15%)	Accumulate (5% to 15%)	Neutral (-5 to 5%)
		Reduce (-5% to -15%)	Sell (< -15)