11TH AUGUST,2021

Q1 FY2021 Result Update and Conference Call Highlights

Shareholding Pattern

Promoter Holding:	44.02%
Mutual Funds:	6.53%
FPI:	13.29%
Public:	36.16%

CMP:	Rs. 1707.45
Market Cap (Rs. in crores):	5369.34

Gunjan Kabra
www.gunjankabra.com
info@gunjankabra.com

The lockdown did impact the company in a meaningful way. The revenue fell by 79% yoy. Higher overhead expenses and significant fall in volumes impacted EBITDA. However, as guided by the management there was pent up demand experienced in May and June resulting in fall in inventory. The rise in demand was from Tier 2 and Tier 3 cities and also through the e-commerce route. The capacity utilisation is expected to be 60-65% in Q2 FY21.

Conference Call Highlights

Industry Dynamics

The **RAC market** contracted by 65% during the current quarter and full recovery is expected to come in Q4 FY21, as per the management of Blue Star. The next two quarters are seasonally weak quarters for the industry.

Inventory: There were 20-23 lakh ACs in inventory at the start of Q2 FY2021. As per the management, 15,00,000 units got liquidated from the system in last 2.5 months. The industry did go for a price cut in order to move out the inventory.

China +1 strategy is playing out quite well for them. The company is getting enquires from international companies.

Recent Developments and Opportunities in the Industry

- **Governments push on Atmanirbhar Bharat and making AC industry as one of the priority sectors**

Currently, 30% of the finished RAC are being imported in India which is valued at ~Rs. 4200-4500 crores in FY2019. Equal values of components are being imported in India with respect to RACs. The value is expected to reach 2-2.5x of current levels by FY 25.

As per the draft plan of PMP for ACs, while fully finished indoor (IDU) and outdoor (ODU) AC units now attract 20% duty, it will be raised to 30% by the fifth year. Compressors will attract 20% duty from the fourth year onwards against 12.5% now. Among other components, duty on circuit board controller, motor, cross flow fan and evaporators will rise from 10% now to proposed 20% by the fifth year.

As per my understanding of the industry dynamics, management of different RAC brands did realise that adopting higher localization strategy does curb cost and improve operating efficiency. Some companies have adopted the strategy of localisation to some extent and some aim to reduce import content to drive higher value addition wherever possible. With the

Phased Manufacturing Policy of government, this trend is likely to accelerate in future at least for some components.

With any increase in domestic sourcing, the company is expected to benefit because of its strong presence.

Compressors: It is the major contributor to cost. The management guided that the compressor ecosystem is building up slowly. But, it is difficult for compressor companies to become viable with the demand numbers of India and become competitive at the global level. Highly, GMCC and a Japanese firm plans to start building compressors in India. Within 2-3 years, it is expected 70-80% demand can be met in India. The entire compressor component ecosystem is highly import dependent. If that isn't build up properly, then it can go wrong for the industry. Going forward, need to watch on how this trend is carried out.

Motors: There are 3 companies, PICL (Amber's subsidiary), Japanese and a US company. Only 32% of the market is sourced locally. When they acquired PICL, 90% amount was imported but now the raw materials are 100% domestically sourced.

PCB Boards: 35% of the total boards are sourced domestically. Here, also the raw material to quite an extent is dependent on imports.

Performance of Subsidiaries and Outlook

Sidwal: The company acquired new orders worth Rs.115 crores which needs to be executed over 1-2 year period. The company did Rs. 30 crores revenue and Rs. 4.9 crores of EBITDA in Q1 FY2021. Being, in the tender business, Sidwal was least impacted during the lockdown.

PICL: The company did a revenue of Rs. 8 crores and incurred EBITDA loss of Rs. 1.8cr in Q1 FY21. It launched motors for washing machine, commercial air conditioners. The management guided that they expect to double revenue in next 2 years.

The reliability cycle for motors is over for some companies and the company has started shipping to 3 customers in the US and Middle East. There are 16 more clients to be addressed. Going forward, in motor business, 30-35% of revenue is expected to come from exports which was 10% last year.

If there is an increase in exports, the company doesn't have to build up new capacities. The export order comes from May-Sept which is an off season in India. This becomes complementary for the business.

ILJIN: The company did a revenue of Rs. 16.7 crores and EBITDA loss of Rs. 1.7 crores.

EVER: The company did a revenue of Rs. 16.8 crores and EBITDA loss of Rs. 1.2 crores.

The management guided that they expect to add Rs. 250-280 crores more business in ILJIN and EVER.

The company has made an enabling provision of Rs. 500 crores. This would be used for bringing up new units as the policy is announced.

Financials

(Rs. in cr)	June-20	June-19	Mar-20
Revenue	259.5	1235.9	1315.18
EBITDA	-5.5	116.4	101.9
EBITDA Margins	-2.1	9.4%	7.7%
PBT	-35.6	91.5	70.08
Tax	-11.7	27.2	7.3
PAT	-23.9	64.3	62.82
EPS	-7.61	19.47	20

Conclusion

There are structural tailwinds for the industry in terms of focus on domestic production by the government and China +1 strategy. The company has built up a competitive ecosystem for some component business and is trying to do the same for the others. Also, I believe that outsourcing as a theme can play out well especially during these times when the companies are taking efforts to minimise costs.

Being a discretionary product and considering the seasonality factor and impact of COVID-19, demand is expected to remain soft in near term and achieve normalcy by Q4 FY21.