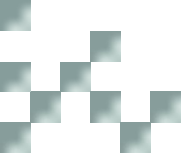


CRISIL SME IER Independent Equity Research

Veto Switchgears and Cables Ltd

FY13 Result Update

Enhancing investment decisions



Explanation of CRISIL SME Fundamental and Valuation (CFV) matrix

The CRISIL SME CFV Matrix (CRISIL Fundamental and Valuation Matrix) addresses the two important analysis of an investment making process – Analysis of Fundamentals (addressed through SME Fundamental Grade) and Analysis of Returns (SME Valuation Grade) The SME fundamental grade is assigned on a five-point scale from grade 5 (indicating Excellent fundamentals) to grade 1 (Poor fundamentals). The SME valuation grade is assigned on a five-point scale from grade 5 (indicating strong upside from the current market price (CMP)) to grade 1 (strong downside from the CMP). This opinion is a relative assessment in relation to other SMEs in India. The assessment is based on a grading exercise carried out by industry specialists from CRISIL Research.

CRISIL SME Fundamental Grade	Assessment	CRISIL SME Valuation Grade	Assessment
5/5	Excellent fundamentals	5/5	Strong upside (>25% from CMP)
4/5	Superior fundamentals	4/5	Upside (10-25% from CMP)
3/5	Good fundamentals	3/5	Align (+-10% from CMP)
2/5	Moderate fundamentals	2/5	Downside (negative 10-25% from CMP)
1/5	Poor fundamentals	1/5	Strong downside (<-25% from CMP)

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Last updated: May, 2013

Analyst Disclosure

Each member of the team involved in the preparation of the grading report, hereby affirms that there exists no conflict of interest that can bias the grading recommendation of the company.

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Veto Switchgears and Cables Ltd

Business under pressure, inventory days rise sharply



SME Fundamental Grade 4/5 (Superior fundamentals)
SME Valuation Grade 2/5 (CMP has downside)

Veto Switchgears and Cables Ltd's (Veto's) FY13 results were below CRISIL Research's expectations. Revenues grew by 8.1% y-o-y to ₹741 mn. EBITDA margin contracted by 116 bps y-o-y to 15%. Tax rate increased to 22% from 4% in FY12 as its 100% tax exemption benefit expired. As a result, adjusted PAT declined by 15% y-o-y to ₹61 mn. Weak demand and lower-than-expected expansion in the dealer network impacted Veto's performance; these remain key monitorables going forward. We maintain the SME Fundamental Grade of 4/5 on Veto, indicating that its fundamentals are **superior** relative to other SMEs in India.

Revenue growth slows down

Veto's FY13 revenue growth slowed down to 8% compared to CAGR of 18% over FY09-12. Revenues from the wires and cables segment contributed ~60% to overall sales and those from the accessories segment contributed ~40%. According to the management, weak demand impacted sales during the year. Further, the company added only 50 dealers during the year, which also slowed sales growth.

EBITDA margin impacted by high advertising, branding and sales promotion expenses

Veto's EBITDA margin declined by 116 bps y-o-y to 15% in FY13. This decline was due to 75% increase in other expenses y-o-y as the company increased its advertising, branding and sales promotion expenses. It has started advertising on local transport buses in Jaipur and on radio in Rajasthan as well as in other states in which it is present. The company plans to spend ₹17.5 mn on advertising, branding and sales promotion in FY14, up from ₹13.6 mn spent in FY13.

Inventory days rose sharply due to increase in product range

Veto's inventory days increased to 159 days in FY13 from 119 days in FY12. According to the management, the company has added new products and increased the range in existing products. Since inventory of all products needs to be maintained at the depots, overall inventory has increased. The inventory may have also increased as sales were low. We expect inventory to increase going forward as the company is continuously increasing its product portfolio and have factored in inventory of 160 days for FY14 and 165 days for FY15.

Update on utilisation of IPO funds

Veto raised ₹250 mn through an IPO in December 2012. As on March 31, 2013, the company has utilised ₹189 mn of the IPO proceeds in modernisation of existing facilities, working capital requirements, brand building and IPO expenses. The balance ₹61 mn is temporarily invested in bank fixed deposits and will be deployed in FY14 towards brand building, incremental working capital requirement and for capex of ₹20 mn for purchasing plastic moulding machinery to reduce dependence on outsourced moulded material.

Reduce FY14 and FY15 earnings estimates, revise fair value to ₹41

We have reduced FY14 and FY15 earnings estimates by 5% each. We continue to use the discounted cash flow (DCF) method to value Veto and revise the fair value to ₹41 per share from ₹45 earlier mainly due to increase in working capital requirements. This fair value implies P/E multiples of 7.5x FY14E and 6.7x FY15E EPS. The assigned valuation grade is 2/5.

KEY FORECAST

(₹ mn)	FY11	FY12	FY13#	FY14E	FY15E
Operating income	532	686	741	859	986
EBITDA	71	111	111	127	144
Adj net income	49	72	61	91	101
Adj EPS (₹)	4.6	6.7	3.7	5.5	6.1
EPS growth (%)	4.9	47.1	(45.2)	49.2	11.0
RoCE (%)	15.9	23.0	18.1	17.0	17.3
RoE (%)	28.8	30.8	14.1	14.4	14.2

*Computed on post initial public offering basis; CMP: Current market price

Based on abridged financials

Source: Company, CRISIL Research estimates



June 11, 2013

Fair Value ₹41
 CMP ₹50

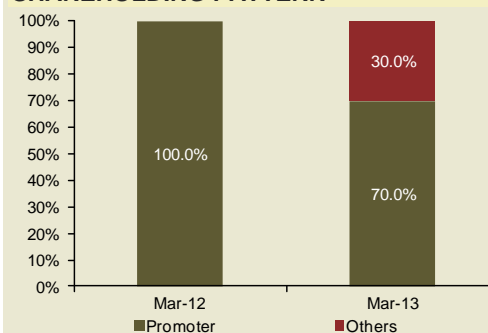
SME CFV MATRIX

SME Fundamental Grade	Excellent	Strong Upside	SME Valuation Grade
	5/5	5/5	
4/5	4/5		
3/5	3/5		
2/5	2/5		
1/5	1/5		
Poor	Strong Downside		

KEY STOCK STATISTICS

NIFTY	5878
NSE EMERGE ticker	VETO
Face value (₹ per share)	10
Shares outstanding (mn)	17
Market cap (₹ mn)/(US\$ mn)	840/14
Enterprise value (₹ mn)/(US\$ mn)	792/14
Free float (%)*	30%

SHAREHOLDING PATTERN



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Client servicing desk

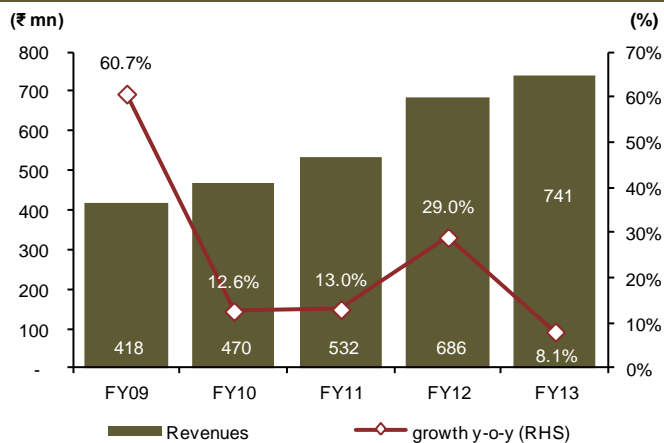
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FY13 Results Summary

	FY13	FY12	y-o-y (%)
Net sales	741	686	8.1%
Raw material cost	511	491	4.0%
Raw material cost (% of net sales)	68.9%	71.6%	-268bps
Employee cost	47	42	10.3%
Other expenses	72	42	74.5%
EBITDA	111	111	0.3%
EBITDA margin	15.0%	16.1%	-116bps
Depreciation	11	11	0.8%
EBIT	100	100	0.2%
Interest and finance charges	25	26	-4.8%
Operating PBT	76	74	2.0%
Other income	3	1	NM
Extra-ordinary expenses	2	-	NM
PBT	79	75	4.4%
Tax	17	3	452.3%
PAT	59	72	-18.5%
Adj PAT	61	72	-15.1%
Adj PAT margin	8.3%	10.5%	-226bps
No of equity shares (mn)	16.7	10.8	54.8%
Adj EPS (₹)	3.7	6.7	-45.2%

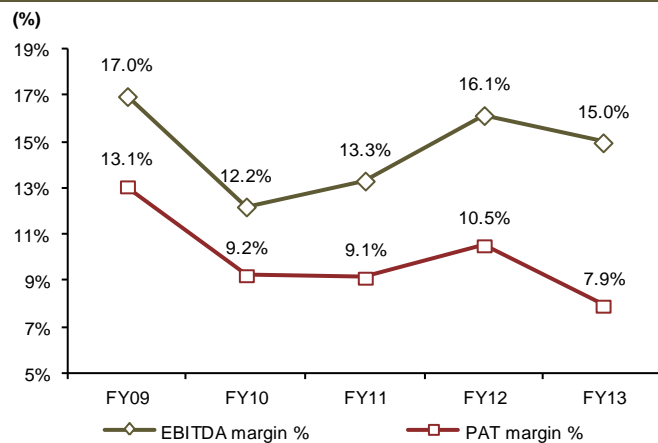
Source: Company, CRISIL Research

Revenues grew by 8.1% y-o-y and were below expectations



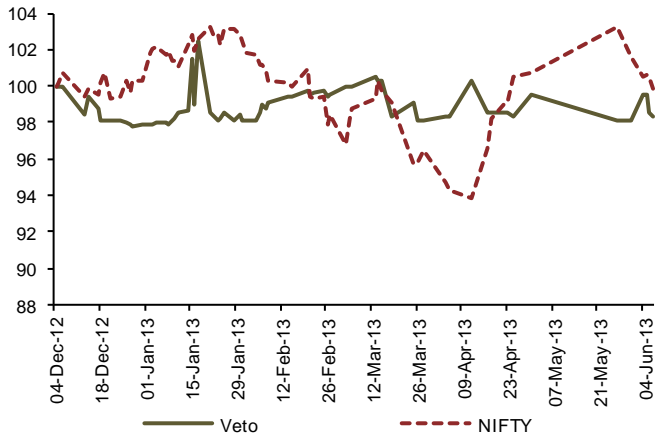
Source: Company, CRISIL Research

EBITDA and PAT margins were below expectations



Source: Company, CRISIL Research

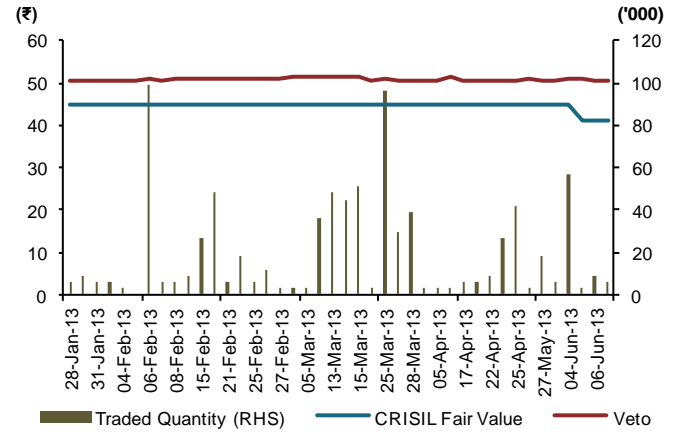
Share price movement



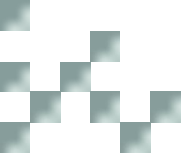
-Indexed to 100

Source: NSE, CRISIL Research

Fair value movement since initiation



Source: NSE, BSE, CRISIL Research



Earnings Estimates Revised Downwards

	Unit	FY14E			FY15E		
		New	Old	% change	New	Old	% change
Revenue	(₹ mn)	859	924	-7.0%	986	1,061	-7.1%
EBITDA	(₹ mn)	127	139	-8.2%	144	155	-7.1%
EBITDA margin	%	14.8%	15.0%	-20bps	14.6%	14.6%	0bps
Depreciation	(₹ mn)	14	16	-10.0%	16	17	-7.3%
Interest	(₹ mn)	4	15	-70.7%	4	10	-62.4%
Other income	(₹ mn)	5	9	-40.5%	3	6	-55.6%
Tax rate	%	20.0%	18.0%	200bps	20.0%	20.0%	0bps
PAT	(₹ mn)	91	96	-4.8%	101	107	-5.2%
PAT margin	%	10.6%	10.4%	24bps	10.3%	10.1%	21bps

Source: CRISIL Research estimates

Reasons for changes in estimates

Line item	FY14E	FY15E
Revenues	Revised downwards due to weak demand and lower-than-expected expansion in distributor network	
EBITDA margins	Revised downwards as increase in advertising and promotion expenses is expected to impact EBITDA margin	No change
PAT margins	Revised upwards due to: <ul style="list-style-type: none"> ■ Significant reduction in interest as the company's debt has reduced to ₹43 mn in FY13 from ₹204 mn in FY12 since it has repaid most of the working capital debt using the IPO funds ■ Reduction in depreciation due to lower-than-expected depreciation rate 	

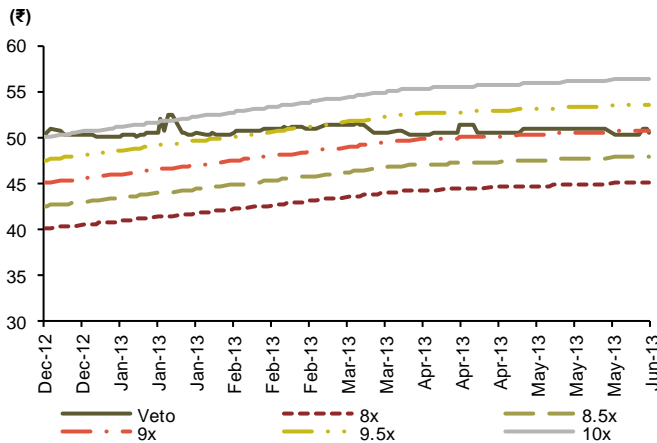
Valuation

Grade: 2/5

We continue to use the DCF method to value Veto and have revised the fair value to ₹41 per share from ₹45 earlier due to significant increase in working capital requirements. This fair value implies P/E multiples of 7.5x FY14E and 6.7x FY15E EPS. At the current market price of ₹50, the valuation grade in 2/5.

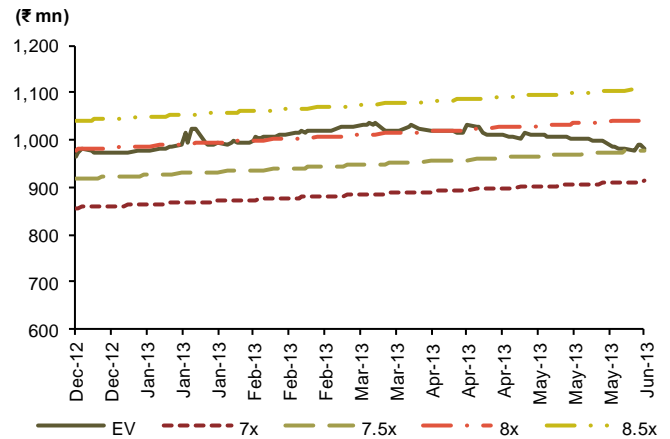
Fair value revised to ₹41 per share

One-year forward P/E band



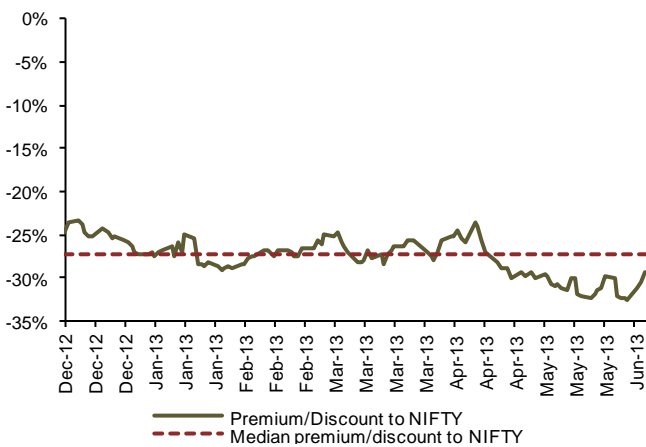
Source: NSE, CRISIL Research

One-year forward EV/EBITDA band



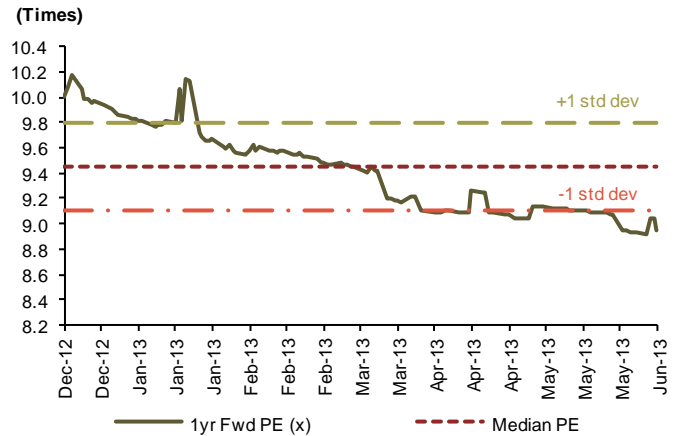
Source: NSE, CRISIL Research

P/E – premium / discount to Nifty



Source: NSE, CRISIL Research

P/E movement



Source: NSE, CRISIL Research

CRISIL SME IER reports released on Veto Switchgears and Cables Ltd

Date	Nature of report	Fundamental grade	Fair value	Valuation grade	CMP (on the date of report)
29-Jan-13	Initiating coverage	4/5	₹45	3/5	₹50
11-Jun-13	FY13 Result Update	4/5	₹41	2/5	₹50

Annexure: Financials

Income statement						Balance Sheet					
(₹ mn)	FY11	FY12	FY13#	FY14E	FY15E	(₹ mn)	FY11	FY12	FY13#	FY14E	FY15E
Operating income	532	686	741	859	986	Liabilities					
EBITDA	71	111	111	127	144	Equity share capital	53	54	167	167	167
EBITDA margin	13.3%	16.1%	15.0%	14.8%	14.6%	Reserves	145	217	428	509	583
Depreciation	9	11	11	14	16	Minorities	-	-	0	0	0
EBIT	62	100	100	113	128	Net worth	198	271	594	676	750
Interest	13	26	25	4	4	Convertible debt	-	-	-	-	-
Operating PBT	49	74	76	109	124	Other debt	200	204	43	16	32
Other income	0	1	3	5	3	Total debt	200	204	43	16	32
Exceptional inc/(exp)	(0)	-	(2)	-	-	Deferred tax liability (net)	2	2	2	2	2
PBT	49	75	76	114	127	Total liabilities	400	477	639	694	784
Tax provision	1	3	17	23	25	Assets					
Minority interest	-	-	-	-	-	Net fixed assets	88	95	93	104	112
PAT (Reported)	49	72	59	91	101	Capital WIP	6	5	5	5	5
Less: Exceptionals	(0)	-	(2)	-	-	Total fixed assets	94	100	98	109	117
Adjusted PAT	49	72	61	91	101	Investments	1	3	0	0	0
Ratios						Current assets					
	FY11	FY12	FY13#	FY14E	FY15E	Inventory	142	179	243	304	357
Growth						Sundry debtors	164	208	201	276	343
Operating income (%)	13.0	29.0	8.1	15.9	14.8	Loans and advances	37	56	100	60	64
EBITDA (%)	23.4	56.3	0.2	14.5	13.2	Cash & bank balance	21	18	91	44	15
Adj PAT (%)	11.9	48.5	(15.3)	49.2	11.0	Marketable securities	-	-	-	-	-
Adj EPS (%)	4.9	47.1	(45.2)	49.2	11.0	Total current assets	364	461	636	683	779
						Total current liabilities	59	87	95	98	113
Profitability						Net current assets	305	374	541	585	666
EBITDA margin (%)	13.3	16.1	15.0	14.8	14.6	Intangibles/Misc. expenditure	0	0	-	-	-
Adj PAT Margin (%)	9.1	10.5	8.3	10.6	10.3	Total assets	400	477	639	694	784
RoE (%)	28.8	30.8	14.1	14.4	14.2	Cash flow					
RoCE (%)	15.9	23.0	18.1	17.0	17.3	(₹ mn)	FY11	FY12	FY13#	FY14E	FY15E
RoIC (%)	16.8	23.8	17.7	16.9	15.2	Pre-tax profit	49	75	79	114	127
						Total tax paid	(1)	(3)	(18)	(23)	(25)
Valuations						Depreciation	9	11	11	14	16
Price-earnings (x)	11.1	7.5	13.7	9.2	8.3	Working capital changes	(11)	(72)	(94)	(91)	(110)
Price-book (x)	2.7	2.0	1.4	1.2	1.1	Net cash from operations	46	11	(23)	14	8
EV/EBITDA (x)	10.1	6.6	7.1	6.4	6.0	Cash from investments					
EV/Sales (x)	1.3	1.1	1.1	0.9	0.9	Capital expenditure	(11)	(17)	(8)	(25)	(25)
Dividend payout ratio (%)	-	-	-	-	23.3	Investments and others	(1)	(1)	3	-	-
Dividend yield (%)	-	-	-	-	2.8	Net cash from investments	(13)	(18)	(6)	(25)	(25)
						Cash from financing					
B/S ratios						Equity raised/(repaid)	10	0	254	(0)	-
Inventory days	119	119	159	160	165	Debt raised/(repaid)	(38)	4	(161)	(26)	16
Creditors days	45	54	55	48	48	Dividend (incl. tax)	-	-	-	-	(27)
Debtor days	113	111	99	110	119	Others (incl extraordinary)	-	0	8	(10)	-
Working capital days	195	189	222	216	227	Net cash from financing	(29)	4	101	(36)	(11)
Gross asset turnover (x)	4.6	5.4	5.4	5.5	5.5	Change in cash position	5	(3)	73	(47)	(29)
Net asset turnover (x)	5.9	7.5	7.9	8.8	9.1	Closing cash	21	18	91	44	15
Sales/operating assets (x)	5.7	7.1	7.5	8.3	8.7						
Current ratio (x)	6.2	5.3	6.7	7.0	6.9						
Debt-equity (x)	1.0	0.8	0.1	0.0	0.0						
Net debt/equity (x)	0.9	0.7	(0.1)	(0.0)	0.0						
Interest coverage	4.8	3.9	4.1	25.6	35.1						
Per share											
	FY11	FY12	FY13#	FY14E	FY15E						
Adj EPS (₹)	4.6	6.7	3.7	5.5	6.1						
CEPS	5.4	7.7	4.3	6.3	7.1						
Book value	18.6	25.2	35.7	40.6	45.0						
Dividend (₹)	-	-	-	-	1.4						
Actual o/s shares (mn)	10.7	10.8	16.7	16.7	16.7						

Based on abridged financials

Source: CRISIL Research

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