

## Salora International Limited

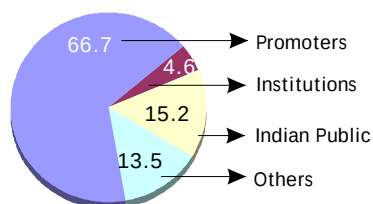
CMP : Rs. 218.05 | Target Rs. 312.0 | BUY

### Stock Codes

|           |              |
|-----------|--------------|
| Bloomberg | : SLI.IN     |
| Reuters   | : SALI.BO    |
| BSE Code  | : 500370     |
| NSE Code  | : SALORAINTL |
| BSE Group | : A          |

### Share Holdings (%)

As on 30th September, 2007.



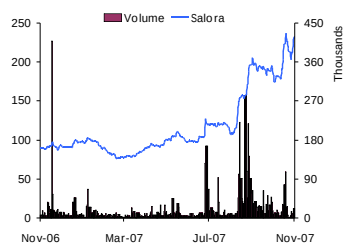
### Stock Data

|                 |            |
|-----------------|------------|
| Sensex          | : 19633.36 |
| Nifty           | : 5907.65  |
| 52 W High Rs.   | : 248.0    |
| 52 W Low Rs.    | : 74.0     |
| Mkt Cap Rs. Mn. | : 2061.0   |
| Face Value Rs.  | : 10.0     |

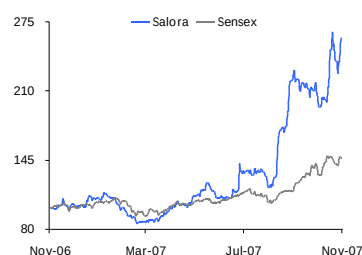
### Absolute Returns

| %      | 1M    | 3M    | 6M     |
|--------|-------|-------|--------|
| Salora | 17.67 | 83.30 | 130.18 |
| Sensex | 6.52  | 29.30 | 42.25  |

### Price/Volume



### Price Comparison



Salora International Ltd a manufacturer of CTV Parts has transformed its self from a manufacturer to a distributor of Telecom and Infocom products. Salora International Ltd's management has been able to grow steadily in the field of distribution over the years and has achieved a critical mass in terms of revenue to march into the big league. The stock on the other hand is still valued in terms of the company's legacy business, which is considerably lower than the true value that the stock should command. The company is poised to gross revenues of over Rs. Thousand crores (for the distribution business) by this financial year in terms of topline. We feel sooner than later the relative valuation gap that exists for the scrip will eventually narrow down. We initiate coverage on the stock with a buy rating and a target price of Rs. 312.

- The company derives 85% of its revenues from the telecom & infocom distribution business and more than 90% of the EBIT from the business of distribution, thus making it a clear contender for a re-rating from a CTV components manufacturer to a full-fledged distributor. We recommend a strong buy with an upside of close to 30% from the current level.
- A sustained growth outlook on the back of a booming consumer spending which has been showing a consistent growth, in our estimates this trend in consumer spend is bound to continue representing a huge opportunity for a company like Salora International Ltd. The prime reason for the above assumption remains the demographics of our country; India in terms of population is one of the youngest nations with the majority of its population falling between the age group of 19 to 40 years.
- Salora International Ltd plays a critical role by acting as a bridge in the long chain of operations that link the manufacture with the main retailer. Backed by an excellent standing relationship that the company has had with its vendors like Sony Ericsson, BenQ, Acer to name a hand few, the company has managed to build a very strong distribution network of 30 offices touching over 25000 retailers.
- The company has active plans to get into retailing of products that it is already distributing; the modalities of the same will be out very shortly. The company is very well placed to show a topline growth of above 35% for some time in our expectations. The restructuring that the company has initiated in its CTV components business will keep that business profitable as well keeping the overall profitability intact.
- In our estimates the fair value of the stock stands at Rs. 312. Salora (7.2x FY09E) trades at a relative discount when we compare it with its peer groups like a Redington India (13.7x FY09E) & HCL Infosystems (9.4 x FY09E). The above estimated target value that has been attributed to the stock implies that it would trade at a P/E multiple of 7.2x on FY09E.

|       | Net Sales | EBITDA | PAT   | OPM (%) | EPS (Rs.) | P/E (x) | EV/EBITDA (x) | RONW (%) |
|-------|-----------|--------|-------|---------|-----------|---------|---------------|----------|
| FY06  | 5,884.3   | 232.9  | 113.0 | 3.72%   | 12.8      | 17.0    | 8.7           | 10.77%   |
| FY07  | 8,873.7   | 309.6  | 143.0 | 3.36%   | 16.2      | 13.4    | 7.7           | 12.22%   |
| FY08E | 12,856.9  | 414.3  | 198.7 | 3.14%   | 22.5      | 9.7     | 6.2           | 15.02%   |
| FY09E | 16,942.6  | 542.5  | 268.7 | 3.14%   | 30.5      | 7.2     | 5.1           | 17.39%   |
| FY10E | 21,558.7  | 656.9  | 323.4 | 3.00%   | 36.7      | 5.9     | 4.7           | 17.75%   |

## Company Overview

The company under our coverage is Salora International Ltd. ( hence forth referred to as SIL) which was incorporated in 1968 as Electronic Consortium Pvt Ltd as a manufacturer of color and black & white television sets to be marketed under the brand name “Salora”. As the policies changed and with the passage of time, giants of home entertainment business entered the Indian market, it became difficult for Salora to remain competitive in the business and thus began the slide of the company both in terms of profits and in terms of market share.

### *Shift from Legacy business*

In the year 1992 SIL ventured into the business of distribution and with this began the story of the company's transformation both in terms of top line and bottom line. Even with the above stated things happening within the company one thing that did not change with this company is the reputation of the company that of a feebly performing CTV and components manufacturer and it is because of this image that the company has not been able to shed the markets have neglected this company and have grossly undervalued the stock as compared to the companies that are operating in the same space. We initiate our coverage on the stock with a buy recommendation on the stock.

Over the last five years SIL has clocked a CAGR growth of 52%. In the business of distribution in which the company operates a certain level of critical mass needs to be achieved before one can reach an inflection point and leverage on ones strength. SIL over the years has grown in size and now we feel that the time has arrived has come for the company to reap higher benefits from the same amount of effort which in simple terms means that the company has come to a stage where company will reap the benefits for the hard work done in the earlier years.

### *Strong distribution network*

Over the years SIL has become a key player in the telecom & infocom distribution business, its footprint now covering over 20000 retailers, 160 resellers, which is being rapidly widened. SIL's distribution network covers over 1000 towns. SIL has consistently been winning awards from its principals for the kind of performance it has been showing a testimony of the capability of the company and competencies.

SIL has got aggressive plans to scale up its operations both in terms of new product offerings to come out of its distribution basket, as well as to leverage its position to diversify into different vertical (direct retailing of the products it distributes).

The company derives 85% of its revenues from the telecom & infocom distribution business and more than 90% of the EBIT from the business of distribution, thus making it a clear contender for a re-rating from a CTV components manufacturer to a full-fledged distributor. We reiterate a strong buy with an upside of close to 30% from the current level.

SIL operates in four different segments which are as follows:

- Infocom & Telecom Distribution
- Retail (Proposed)
- CTV Components
- Wind Energy

## Business Segments

### Infocom & Telecom Distribution

SIL, in the infocom & telecom distribution space is engaged in both distribution and after-sales-service of the products it sells. The company has national distribution licenses for Sony Ericsson, BenQ etc in the telecom space and in the IT hardware space it has brands like Acer, Fujitsu and other brands under its belt.

*Two big accounts bagged on the back of strong performance*

The company has been able to get the rights to distribute HP's "Pavilion" and "Presario" brand of desk tops and laptops as well. This is due to SIL's consistent performance achieved not only for HP but for other brands as well and in this business vendors are always on the lookout for good distributors. SIL has been able to crack this account on the strong performance it has been able to achieve over the years.

The business of distribution thrives on volumes and is pretty much a low margin business hence it is very important for a distributor to have as many like products under its kitty as the additional cost attached for the sale of every additional product diminishes at an increasing rate. In our estimates by FY08 the infocom business of SIL will cross one thousand crores, what this means for a company like SIL is that it is nicely poised to break into the other dimension and start to grow at an even faster pace. We feel that the time taken for SIL to clock the first one thousand crores for the distribution business will not be equal for the next thousand.

*State of the art ERP system*

The company has an Oracle based ERP system in place which connects all sales, warehousing and service locations in real time. This system is backed by a twenty two member team for the maintenance and up gradation of the system. All the processes are being ramped up in this area so as to make it into an independent vertical

SIL has an added advantage in addition to the positives already mentioned and that is that it has three hundred service centers spread over the country which plays a very important role in strengthening the support which the company can offer and this is one thing that retailers constantly look for in their distributors, what it means in simple terms is that there is some amount of faith that the retailer attributes to a vendor (SIL is a vendor for a retailer) who will be able to help him even after the sales have been done. Of the three hundred service centers that the company boasts of, eighty are company owned and operated while the rest are franchisee service centers. We feel this edge that the company has, will be helpful in a long way in the future as these are some of the extra points that newer principals will consider while awarding newer contracts to the company.

*Long standing relationships*

SIL has had excellent relations with its principals and it has been consistently winning awards from them. Sony Ericsson India for whom SIL and Ingram Micro are the distribution partners roughly account for equal volumes in terms of handset sales. SIL has an exclusive license for after-sales-service; here SIL is even better placed in terms of Ingram Micro as well. Apart from the wide distribution network that SIL has, it also has about one hundred and seventy service centers for Sony Ericsson. What we deduce out of this that SIL is on a very good wicket as far as Sony Ericsson is concerned.

Today Acer accounts for roughly 10% of total infocom revenue for SIL. In India SIL is one of the four major distributors for SIL. With the kind of advertising thrust that Acer is applying to capture the market it is very clear that the India market is one of the key focuses for the company which augers very well for SIL for the next 3-4 years to come. And the outlook on this front is very encouraging for SIL.

### Existing Strong Relationships

| Recd From     | Particulars                       | Year |
|---------------|-----------------------------------|------|
| Acer          | Most Consistent Distributor       | 2005 |
| Sony Erricson | Outstanding Sales Performance     | 2006 |
| Sony Erricson | Best Global Service Partner       | 2006 |
| Sony Erricson | Best Asia Pacific Service Partner | 2006 |
| BenQ- Siemens | Best Sales Performance            | 2007 |

Source: PPFAS Research

### Retail Foray

SIL wants to leverage on the expertise that it has been able to garner over the years from the distribution business. The next logical step in this direction we feel is to sell the products it distributes and this is exactly what SIL has in stored for itself in the future. SIL intends to enter the retail segment in the very near future, as the explicit plans for the same are still on the drawing board stage the exact modalities of the same will be much clearer in the next quarter. Our discussions with the management have revealed the following:

- To set up six hundred stores of different sizes in the next 4-5 years.
- The format of the stores would range from 500sq ft to 5000sq ft, with majority of them being the smaller stores catering in tier II cities.
- For the above mentioned venture the company intends to do an \$80 million capex, the exact details of the funding will be finalized by the next quarter.
- 3 pilot Sony Ericsson stores ready and the results from them are very encouraging.
- 5 more Sony Ericsson stand alone stores to get operational in another 10 day.
- The multi brand stores to get operational by the Q1 of the next year.
- This venture will be done in a 100% owned subsidiary.

The management is very clear in terms of the format it wants to get into and does not intend to venture into anything where it feels it doesn't have the required capabilities and the expertise. We feel in due course of time this venture initiated by the company if harnesses well by the company will pay rich dividends for the company. Looking at the way organized retailing is shaping up in our country we have our hopes positively pegged to this venture by the company, it is just a matter of time when the modalities of this venture will be more lucid to us and then we will be in a better position to give our point on it.

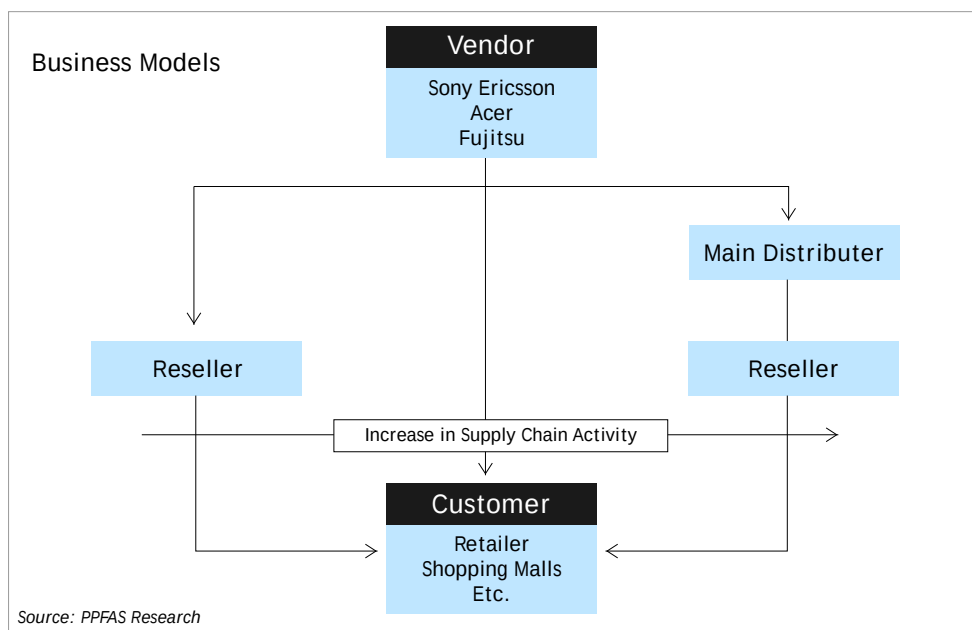
## IT Distribution Industry Overview

IT distributors typically are the middle men who act as a bridge between a manufacturer and a retailer. The idea behind having a distributor for its products can be explained as follows:

- To concentrate on manufacturing activity, product development and innovation.
- To benefit from an existing large distribution network (of the distributor) and its reach without getting into the hassle of building one and deploying the company's resources on building a network.
- Huge benefit of having to deal with one single party for payments and feedback then to run from pillar to post and to deal with an army of retailers who internally would want a customised service to satisfy its own needs.

The whole onus of logistics is on the distributor as the business of IT products is a volume driven business and it is the reach of a distributor that is very helpful in flooding the market with the manufacturer's products.

Logistics play a very important role in this industry and as the complexities increase in terms of number of products, product categories etc the layers between the manufacturer and the retailer increase. Broadly there are three different models of distribution that usually work in this industry. A manufacturer can choose between any of them or choose all of them depending upon the need it feels. The different models of distribution are as follows:



The key challenges that a distributor faces are on the inventory management front as it is very typical of this industry to face very high product obsolescence which in turn heightens the credit risk. The above mentioned risks are covered to a certain extent by the manufacturer for some very large distributors through facilities like accepting unsold goods, replacing old models with new etc. As this industry is a low margin high volume business (gross margins are in the range of 3-5% and operating margins range between 1-2%) it is critical for any distributor to have a very quick cash conversion cycle (days of inventory plus sundry debtor's days, less days of payables), for this it is very important for the distributor to have very robust processes and a highly stable IT system.

*High Volume - Low Margin Business*

## IT Distribution Industry in India

The IT distribution industry is directly dependent on the growth of IT industry. Due to the transition of India from a developing nation to a developed nation, the It industry is growing at a very fast pace and from the look of thing it is safe to assume that this growth is still sustainable as the penetration of IT products are very low.

| Country | PC Penetration (Per 100 People) |
|---------|---------------------------------|
| America | 35.0                            |
| Asia    | 7.0                             |
| Europe  | 30.0                            |
| Oceania | 51.0                            |
| World   | 13.0                            |
| China   | 4.1                             |
| India   | 2.0                             |

Source: World Bank Development Indicators, PPFAS Research

### Existing Product Portfolio

| Segment          | Brand         | Product                       | Nature of Relationship                               |
|------------------|---------------|-------------------------------|------------------------------------------------------|
| Telecom          | Sony Erricson | Mobile Handsets               | National Distribution and Global Service Partner     |
|                  | BenQ          | Mobile Handsets               | National Distributor and Authorised Service Provider |
|                  | HP            | PDAs, Presario, Pavillion     | National Distributor                                 |
|                  | Jabra         | Mobile Handsets accessories   | National Distributor                                 |
| IT & Peripherals | Acer          | Laptops, Desktops, Projectors | National Distributor                                 |
|                  | Fujitsu       | Laptops, Desktops             | National Distributor                                 |
|                  | Moser Baer    | USB Drives, Memmory Cards     | National Distributor                                 |
| Lifestyles       | I River       | MP3 Players                   | National Distributor                                 |
|                  | Fusion        | Car Audio Systems             | National Distributor                                 |
|                  | TEAC          | LCD/ Plasma TVs, DVD Players  | National Distributor                                 |

Source: PPFAS Research

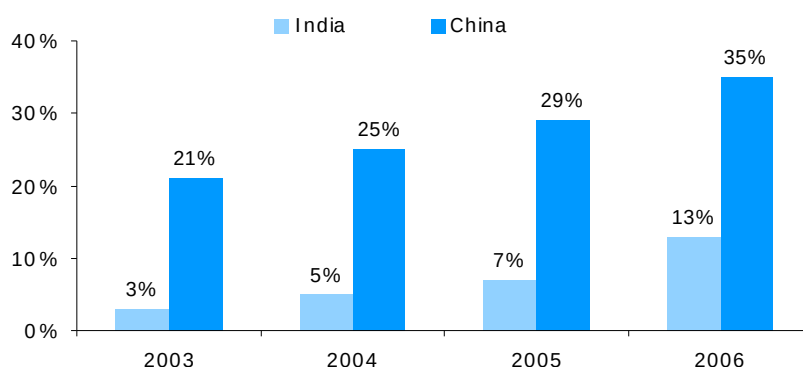
## Telecom Industry Overview in India

One of the biggest beneficiaries of liberalization in India has been the telecom sector. The kind of growth that has been witnessed in this sector is second to none and in spite of a steady growth in the mobile subscribers which has been upwards of 70% yoy the tele-density in India is still very low and the fast pace of growth can be achieved for some time to come. From our estimates we feel that the mobile subscriber base will grow upwards of 35% yoy for some time to come, what this means is that there will be an exponential growth in this sector, making it a huge opportunity for a telecom products distributor.

Like computers the rate of change in technology in mobile handsets is extremely fast. The technology tends to change in the higher price segment and more and more people tend to graduate to a higher end model much faster than what they used to earlier. Our estimates show that the replacement market would again grow at an exponential pace for some time to come.

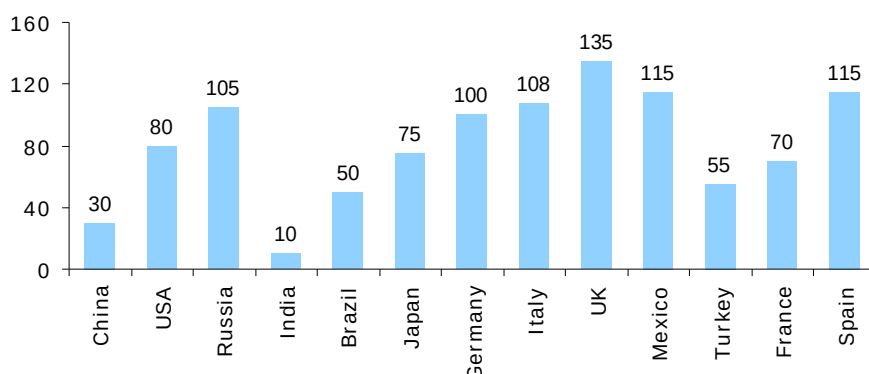
All these facts about the telecom industry auger very well for a telecom distributor like SIL who not only distributes mobile phones but also accessories. Like in any other business it becomes very important for a distributor to have extremely cordial relations with its principles because this is a business which grows over the years and it is very important to have a long standing relationship with the principals, this is absolutely important to get into newer relationships. The company in review has a long standing relationship with its principals and it is safe to assume that SIL is in a position to leverage this relationship into bagging newer principals.

Tele-density growth in India



Source: [www.idate.org](http://www.idate.org), PPFAS Research

Tele-density in major world markets (2006)



Source: [www.idate.org](http://www.idate.org), PPFAS Research

## CTV Components

SIL has two manufacturing facilities in Noida and one each in Gandhi Nagar and Pune. SIL manufactures three types of components for the CTV industry i.e. Flyback transformers (FBT), Deflection yokes (DY) and Loudspeakers (LSP). Out of the three products manufactured by the company only LSP are the only components that are used in both flat and conventional CTVs and the other two products are used exclusively for conventional or round picture tube CTVs.

The demand for FBT and DY has been continuously on the decline since the last few years as the product category they are used in is witnessing a de-growth in demand thus the company is continuously seeing this division not making the kind of profits that it used to as this division is hit severely by Chinese imports. In the year 2007 the management decided to reduce the number of shifts from three to two keeping the number of units produced at the same level, this has resulted in some cost reductions due to better optimization of production capacities. In spite of the management's efforts in this division we do not see great upside from this division as the tables below will try to make our point a little more clearer.

In spite of the de-growth witnessed in this business segment, the company still makes money in this division thus the management has still not decided to shut this business totally but as we do not see much upside in this business our take on this business is that eventually this business will be shut down with further growth in their distribution business. The management on its part has taken some steps to revive this business which are as follows:

- The company has got into a technical collaboration and license agreement with TEAC, Japan to manufacture and sell their range of Liquid Cristal Display TVs (LCD TV).
- SIL on its own has developed a low-cost CTV brand "Champion": the company intends to increase its margin with this new product.
- The company has also reorganized its sales force and has got its sight on the retail market thus trying for some market share.

All the above efforts taken on by the company will definitely yield some positive results for the company but one has to realize that the company is fighting an uphill battle both on the macro and micro level some of the challenges which are very evident are listed below:

- Stiff competition from imports due to ever reducing duties.
- Continuous rise in input cost.

If the company has to get into the mainstream CTV manufacturing business then it has to formulate a dedicated strategy for the business and also has to setup a state of the art R&D facility and then deploy a lot of time money and effort into the business which means again shifting its focus from a distributor to a manufacturer. This we do not see happening as the above is not what the management wants to achieve as there is a huge opportunity that the company has in front of it with respect to the distribution business. From the discussions with the management it is very clear that the distribution business is the sole focus of the company, hence betting big on a dying manufacturing business does not seem very prudent.



## CTV Industry composition - Changing from conventional to flat CTVs

*Lossing markets for conventional players*

| Particulars | Conventional CTVs (%) | Flat CTVs (%) |
|-------------|-----------------------|---------------|
| 2001-02     | 97.3                  | 2.7           |
| 2002-03     | 92.4                  | 7.6           |
| 2003-04     | 85.9                  | 14.1          |
| 2004-05     | 71.4                  | 28.6          |
| 2005-06     | 53.1                  | 46.9          |

Source: CRIS Infac, PPFAS Research

## Components Division - Key Performance Indicators

|                              | 2006  | 2007  |
|------------------------------|-------|-------|
| Flyback Transformers (mn)    | 2.5   | 2.4   |
| Deflection Yokes (mn)        | 1.9   | 1.9   |
| Loud Speakers (mn)           | 7.5   | 7.7   |
| Flyback Transformers (Rs mn) | 246.0 | 237.0 |
| Deflection Yokes (Rs mn)     | 236.0 | 255.0 |
| Loud Speakers (Rs mn)        | 260.0 | 242.0 |
| Realizations (Rs)            |       |       |
| Flyback Transformers         | 100.0 | 97.0  |
| Deflection Yokes             | 125.0 | 132.0 |
| Loud Speakers                | 34.0  | 31.0  |

Source: Company, PPFAS Research

## A shift-cut has improved utilization in 2007

*Better utilisation of existing capacity*

|                                  | 2006     |            |                 | 2007     |            |                 |
|----------------------------------|----------|------------|-----------------|----------|------------|-----------------|
|                                  | Capacity | Production | Utilisation (%) | Capacity | Production | Utilisation (%) |
| TV Sets & Sub Assemblies thereof | 300000   | 86842      | 29              | 300000   | 123046     | 41              |
| Electronic Components            | 19600000 | 11561774   | 59              | 15100000 | 12087236   | 80              |

Source: Company

## Wind Energy

As per our discussion with management, the sole reason for the company to get into the business of wind energy was solely for the tax efficiency. This business is not something that the company intends to focus in a big way; hence this business should be looked as investment and not a business opportunity.

Under this venture SIL has set up a 25MW wind energy plant in Dhule, in Maharashtra. This project is fully backed by the Maharashtra State Electricity Board (MSEB); there is an escalation of 15 paise/unit in the purchase price every year. The management and operation of the power plant is with Suzlon Energy Ltd.

SIL has already taken 80% of the overall accrued tax benefit in FY07. This investment gives a positive NPV and an IRR upward 20%.

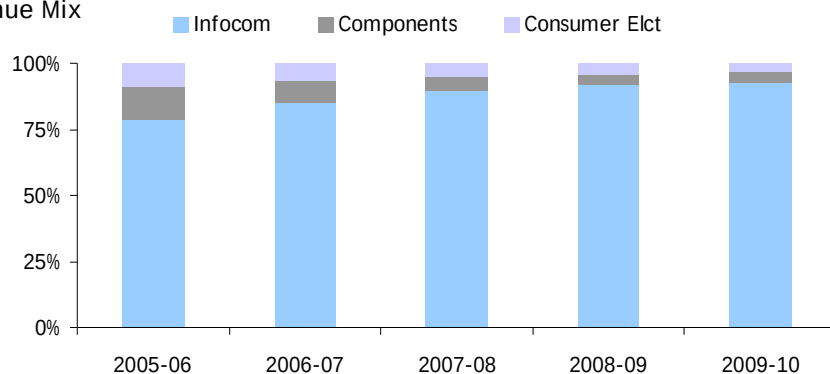
## Quarterly Financials

| (Rs. Mn)               | Q208    | Q108    | Q-Q (%)   | Q207    | Y-Y (%)   | H108    | H107    | Y-Y (%)   |
|------------------------|---------|---------|-----------|---------|-----------|---------|---------|-----------|
| Total Revenues         | 2,842.1 | 2,448.7 | 16.1%     | 2,053.4 | 38.4%     | 5,290.7 | 3,698.8 | 43.0%     |
| Total Expenditure      | 2,730.2 | 2,302.3 | 18.6%     | 1,967.1 | 38.8%     | 5,032.5 | 3,579.1 | 40.6%     |
| Operating Profit       | 111.9   | 146.3   | -23.5%    | 86.2    | 29.8%     | 258.3   | 119.7   | 115.8%    |
| Other Income           | 5.8     | 3.2     | 83.3%     | 1.2     | 372.4%    | 9.0     | 2.5     | 260.6%    |
| EBITDA                 | 117.7   | 149.5   | -21.3%    | 87.5    | 34.6%     | 267.2   | 122.2   | 118.7%    |
| Depreciation           | 13.1    | 13.2    | -0.8%     | 13.7    | -4.3%     | 26.3    | 23.7    | 10.9%     |
| PBIT                   | 104.6   | 136.3   | -23.2%    | 73.8    | 41.8%     | 240.9   | 98.5    | 144.6%    |
| Interest               | 9.0     | 55.9    | -83.9%    | 11.5    |           | 64.9    | 13.5    | 379.5%    |
| PBT                    | 95.7    | 80.4    | 19.0%     | 62.3    | 53.5%     | 176.0   | 85.0    | 107.2%    |
| Tax                    | 32.8    | 29.7    | 10.5%     | 26.9    | 22.1%     | 62.6    | 34.9    | 79.3%     |
| PAT                    | 62.8    | 50.6    | 24.0%     | 35.4    | 77.3%     | 113.5   | 50.1    | 126.7%    |
| Equity Capital         | 88.2    | 88.2    |           | 88.2    |           | 88.2    | 88.2    |           |
| EPS (in Rs.)           | 7.1     | 5.7     | 24.0%     | 4.0     | 77.3%     | 12.9    | 5.7     | 126.7%    |
| Profitability          | Q208    | Q108    | Q-Q (bps) | Q207    | Y-Y (bps) | H108    | H107    | Y-Y (bps) |
| OPM %                  | 3.9%    | 6.0%    | (203.84)  | 4.2%    | (26.2)    | 4.9%    | 3.2%    | 164.51    |
| EBITDA %               | 4.1%    | 6.1%    | (196.34)  | 4.3%    | (11.7)    | 5.1%    | 3.3%    | 174.76    |
| PBIT %                 | 3.7%    | 5.6%    | (188.49)  | 3.6%    | 8.8       | 4.6%    | 2.7%    | 189.14    |
| PAT %                  | 2.2%    | 2.1%    | 14.19     | 1.7%    | 48.4      | 2.1%    | 1.4%    | 79.13     |
| Operational Parameters | Q208    | Q108    | Q-Q (bps) | Q207    | Y-Y (bps) | H108    | H107    | Y-Y (bps) |
| RM Consumed            | 90.8%   | 88.7%   | 212.4     | 88.9%   | 186.6     | 89.8%   | 89.9%   | (10.8)    |
| Staff Cost             | 1.7%    | 1.7%    | 2.5       | 2.2%    | (50.0)    | 1.7%    | 2.4%    | (68.6)    |
| Other Expenditure      | 3.5%    | 3.7%    | (11.0)    | 4.7%    | (110.4)   | 3.6%    | 4.5%    | (85.1)    |
| Effective Tax Rate     | 34.3%   | 37.0%   | (264.9)   | 43.1%   | (881.1)   | 35.5%   | 41.1%   | (553.2)   |

## Segmental Summary

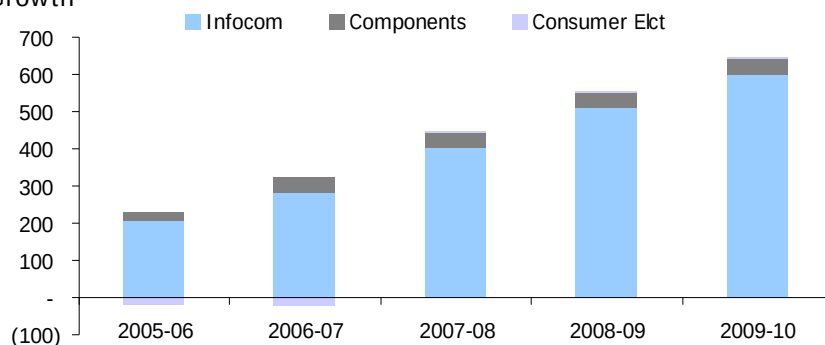
*Increasing share of  
Distribution Business*

Revenue Mix



Source: PPFAS Research

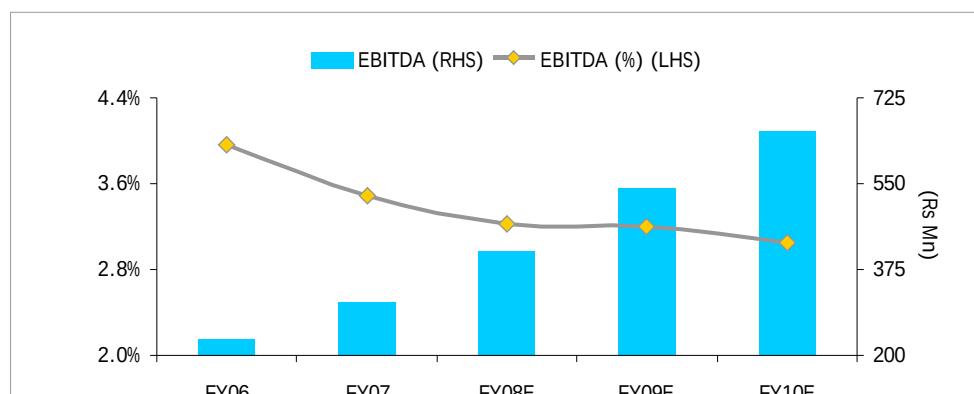
Profit Growth



Source: PPFAS Research

## Investment Argument

Being a low margin business small deep in margins can have a big effect on the bottomline. We have factored a squeeze in the margins. In spite of this, we see the EBITDA still growing.



The space in which SIL operates is comparable to Redington India (in the Infocom space) & HCL Infosystems (in the Telecom space). If one looks at the valuations that these two companies get and then compares it with what SIL is quoted at it becomes very easy to realize that SIL is trading at a very steep discount to these companies and it is safe to assume that it is just a matter of time before SIL is re-rated in terms of valuations. SIL in comparison is a much smaller company when compared with the other two above mentioned companies. One thing which is very clear in this industry is that the companies operating in this space have to reach a critical mass and then the company can leverage from a given platform. Over the years SIL has scaled up its operations to a stage (one thousand crores by the end of this fiscal year), from where it can really increase its top line at a much faster pace. The clear valuation discount that SIL is quoted as can be seen in the table below.

| PE Ratios                              | FY07  | FY08E | FY09E |
|----------------------------------------|-------|-------|-------|
| Redington                              | 24.54 | 18.48 | 13.68 |
| HCL                                    | 11.76 | 10.99 | 9.35  |
| <i>Consensus Estimates : Bloomberg</i> |       |       |       |
| Salora                                 | 13.44 | 9.67  | 7.15  |
| <i>PPFAS Estimates</i>                 |       |       |       |

The stock from the current levels has a fair bit of upside in our view. The stock trades at 7.2x on FY09 estimates which is clearly an indication of the fact that sooner than latter the stock will surprise (upside) from these levels. We have given a discount of 30% (when compared to Redington) in arriving at our valuations, as Redington is fully comparable to SIL, while HCL Infosystems is also in the business of manufacturing. The price target for the stock stands at Rs. 312 giving an upside to the stock of over 40%.

| FY07 (Rs Mn)     | Salora | Redington | HCL Infosystem |
|------------------|--------|-----------|----------------|
| Revenues         | 8873.7 | 90614     | 11658.3        |
| Operating Profit | 297.8  | 1927      | 395.49         |
| OPM              | 3.36%  | 2.19%     | 3.39%          |
| PAT              | 143.0  | 1017      | 315.95         |
| NPM              | 1.61%  | 1.12%     | 2.71%          |

## Financials

| Earnings Statement |         |         |          |          |          |
|--------------------|---------|---------|----------|----------|----------|
| YE March (Rs. Mn.) | FY06    | FY07    | FY08E    | FY09E    | FY10E    |
| Total Revenues     | 5,884.3 | 8,873.7 | 12,856.9 | 16,942.6 | 21,558.7 |
| Cost of Materials  | 5,229.2 | 8,046.1 | 11,681.2 | 15,424.1 | 19,665.7 |
| Total Expenditure  | 5,665.4 | 8,575.9 | 12,452.6 | 16,410.1 | 20,911.8 |
| Operating Profit   | 218.9   | 297.8   | 404.3    | 532.5    | 646.9    |
| Other Income       | 14.0    | 11.8    | 10.0     | 10.0     | 10.0     |
| EBITDA             | 232.9   | 309.6   | 414.3    | 542.5    | 656.9    |
| Depreciation       | 51.4    | 53.5    | 58.0     | 60.8     | 63.6     |
| EBIT               | 181.5   | 256.1   | 356.3    | 481.7    | 593.3    |
| Interest           | 11.4    | 27.5    | 54.2     | 73.2     | 101.7    |
| PBT                | 170.1   | 228.6   | 302.1    | 408.5    | 491.6    |
| Tax                | 56.1    | 85.1    | 102.7    | 138.8    | 167.1    |
| PAT Before MI      | 114.0   | 143.5   | 199.4    | 269.6    | 324.5    |
| Minority Interest  | 1.0     | 0.5     | 0.7      | 1.0      | 1.2      |
| PAT After MI       | 113.0   | 143.0   | 198.7    | 268.7    | 323.4    |

| Ratio Analysis           |         |         |         |         |         |
|--------------------------|---------|---------|---------|---------|---------|
| YE March (Rs. Mn.)       | FY06    | FY07    | FY08E   | FY09E   | FY10E   |
| OPM (%)                  | 3.7%    | 3.4%    | 3.1%    | 3.1%    | 3.0%    |
| EBITDA (%)               | 4.0%    | 3.5%    | 3.2%    | 3.2%    | 3.0%    |
| PBIT (%)                 | 3.1%    | 2.9%    | 2.8%    | 2.8%    | 2.8%    |
| PAT (%)                  | 1.9%    | 1.6%    | 1.5%    | 1.6%    | 1.5%    |
| Interest Cover Ratio     | 1586.8% | 931.4%  | 657.5%  | 658.1%  | 583.5%  |
| EPS (Rs.)                | 12.8    | 16.2    | 22.5    | 30.5    | 36.7    |
| P/E (x)                  | 17.0    | 13.4    | 9.7     | 7.2     | 5.9     |
| P/BV (x)                 | 1.8     | 1.6     | 1.5     | 1.2     | 1.1     |
| BVPS (Rs.)               | 119.0   | 132.8   | 150.1   | 175.3   | 206.7   |
| Market Cap (Rs. Mn.)     | 1,922.0 | 1,922.0 | 1,922.0 | 1,922.0 | 1,922.0 |
| M Cap/Sales (x)          | 0.3     | 0.2     | 0.2     | 0.1     | 0.1     |
| EV (Rs. Mn.)             | 2,035.2 | 2,378.2 | 2,578.2 | 2,778.2 | 3,078.2 |
| EV/EBITDA (x)            | 8.7     | 7.7     | 6.2     | 5.1     | 4.7     |
| EV/Sales (x)             | 0.4     | 0.3     | 0.2     | 0.2     | 0.1     |
| ROCE (%)                 | 15.2%   | 14.8%   | 17.1%   | 19.2%   | 19.2%   |
| RONW (%)                 | 10.8%   | 12.2%   | 15.0%   | 17.4%   | 17.7%   |
| Debt/Equity Ratio (x)    | 0.1     | 0.4     | 0.5     | 0.6     | 0.6     |
| Inventory T/o Days       | 39.2    | 37.7    | 37.0    | 37.0    | 37.0    |
| Debtors T/o Days         | 32.4    | 39.1    | 40.0    | 40.0    | 40.0    |
| Advances T/o Days        | 10.0    | 7.5     | 7.1     | 7.1     | 7.1     |
| Creditors T/o Days       | 32.7    | 45.1    | 45.7    | 45.7    | 45.7    |
| Working Cap T/o Days     | 53.0    | 44.0    | 40.8    | 40.5    | 42.0    |
| Fixed Assets T/o (Gross) | 8.2     | 8.9     | 12.2    | 15.4    | 15.4    |
| DPS (Rs.)                | 4.5     | 4.5     | 4.5     | 4.5     | 4.5     |
| Dividend Payout (%)      | 35.1%   | 27.7%   | 20.0%   | 14.8%   | 12.3%   |
| Dividend Yield (%)       | 2.1%    | 2.1%    | 2.1%    | 2.1%    | 2.1%    |

| Balance Sheet             |         |         |         |         |         |
|---------------------------|---------|---------|---------|---------|---------|
| YE March (Rs. Mn.)        | FY06    | FY07    | FY08E   | FY09E   | FY10E   |
| Equity Capital            | 88.1    | 88.1    | 88.1    | 88.1    | 88.1    |
| Reserves                  | 960.8   | 1,082.6 | 1,234.9 | 1,457.1 | 1,734.1 |
| Shareholders Funds        | 1,049.0 | 1,170.7 | 1,323.0 | 1,545.3 | 1,822.2 |
| Minority Interest         | 3.6     | 4.1     | 4.8     | 5.8     | 7.0     |
| Borrowed Funds            | 113.2   | 456.2   | 656.2   | 856.2   | 1,156.2 |
| Deferred Tax Liability    | 30.4    | 104.3   | 104.3   | 104.3   | 104.3   |
| Total Liabilities         | 1,196.2 | 1,735.4 | 2,088.4 | 2,511.6 | 3,089.7 |
| Fixed Assets              | 306.8   | 569.6   | 561.6   | 550.8   | 537.2   |
| Investments               | 51.7    | 113.0   | 113.0   | 113.0   | 113.0   |
| Current Assets            |         |         |         |         |         |
| Inventory                 | 631.7   | 917.1   | 1,303.3 | 1,717.5 | 2,185.4 |
| Sundry Debtors            | 523.1   | 951.7   | 1,409.0 | 1,856.7 | 2,362.6 |
| Loans & Advances          | 157.4   | 180.0   | 246.6   | 324.9   | 413.5   |
| Cash & Bank Balance       | 61.5    | 134.0   | 115.2   | 136.5   | 262.0   |
| Current Liabilities       |         |         |         |         |         |
| Sundry Creditors          | 512.8   | 1,078.9 | 1,585.1 | 2,088.8 | 2,657.9 |
| Provisions                | 30.8    | 51.2    | 75.1    | 99.0    | 126.0   |
| Net Current Assets        | 830.2   | 1,052.8 | 1,413.8 | 1,847.8 | 2,439.5 |
| Miscellaneous Expenditure | -       | -       | -       | -       | -       |
| Total Assets              | 1,196.2 | 1,735.4 | 2,088.4 | 2,511.6 | 3,089.7 |

| Cash Flow                    |         |         |         |         |         |
|------------------------------|---------|---------|---------|---------|---------|
| Particulars                  | FY06    | FY07    | FY08E   | FY09E   | FY10E   |
| Opening Cash & Bank          | 31.9    | 61.5    | 134.0   | 115.2   | 136.5   |
| Profit After Tax             | 113.0   | 168.1   | 198.7   | 268.7   | 323.4   |
| Less : Invnt Income          | (14.0)  | (11.8)  | (10.0)  | (10.0)  | (10.0)  |
| Miscellaneous Exp W/Off      | 0.0     | 0.0     | 0.0     | 0.0     | 0.0     |
| Depreciation                 | 51.4    | 53.5    | 58.0    | 60.8    | 63.6    |
| Deferred Taxation            | (9.7)   | 73.9    | 0.0     | 0.0     | 0.0     |
| Others                       | 28.5    | (26.5)  | 0.0     | 0.0     | 0.0     |
| Change in Working Cap        | 48.5    | (150.1) | (379.8) | (412.7) | (466.2) |
| CF - Operating Activities    | 217.7   | 107.1   | (133.1) | (93.2)  | (89.3)  |
| Change in Fixed Assets       | (34.0)  | (282.2) | (50.0)  | (50.0)  | (50.0)  |
| Change in Investments        | 24.4    | (61.3)  | 0.0     | 0.0     | 0.0     |
| Investment Income            | 14.0    | 11.8    | 10.0    | 10.0    | 10.0    |
| CF - Investing Activities    | 4.3     | (331.8) | (40.0)  | (40.0)  | (40.0)  |
| Increase in Equity           | 0.0     | 0.0     | 0.0     | (0.0)   | 0.0     |
| Changes in Borrowings        | (151.0) | 343.1   | 200.0   | 200.0   | 300.0   |
| Dividend Paid                | 3.6     | 0.5     | 0.7     | 1.0     | 1.2     |
| Changes in Minority Interest | (45.2)  | (46.4)  | (46.4)  | (46.4)  | (46.4)  |
| CF - Financing Activities    | (192.5) | 297.2   | 154.3   | 154.6   | 254.8   |
| Net Change in Cash           | 29.5    | 72.5    | (18.8)  | 21.4    | 125.5   |
| Closing Cash & Bank Bal      | 61.5    | 134.0   | 115.2   | 136.5   | 262.0   |

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Notes

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