

Honeywell Automation India

BUY

CMP Rs42,500

Target Rs48,258

Upside 14%

Broadly in-line with estimates; Retain BUY

Key highlights from Q3FY21 results

- ✓ Revenues came in at Rs8.7bn, up 15% qoq & down 3% yoy (in-line with estimates).
- ✓ Gross margin was at ~47.3%, contraction of ~183bps yoy led by unfavorable sales mix.
- ✓ However, EBITDA margin expanded by 53bps yoy as Honeywell Automation (HWA) continues to focus on rationalization of discretionary spends, productivity drives etc.
- ✓ Employee cost & other expenses declined by 74bps/162bps yoy respectively. EBITDA was largely flat yoy, 7.2% ahead of estimates.
- ✓ Other income increased by 48% yoy to Rs285mn (+1.6% vs our est.)
- ✓ PAT marginal beat (+5.5% vs our estimates) & it came in at Rs1.5bn, up 3.6% yoy.

Exhibit 1: Quarterly Results Table

(Rs mn)	Q3FY21	Q3FY20	% yoy	Q2FY21	% qoq	YSEC est.	vs our est.
Total sales	8,742	9,012	(3.0)	7,597	15.1	8,749	(0.1)
EBITDA	1,876	1,886	(0.6)	1,443	30.0	1,750	7.2
EBITDAM (%)	21.5	20.9	52.8	19.0	246.2	20.0	145.5
Depreciation	(127)	(115)	10.2	(114)	11.1	(114)	10.7
Interest	(13)	(18)	(27.9)	(18)	(25.0)	(15)	(12.0)
Other income	285	192	48.3	144	98.1	280	1.6
PBT	2,020	1,944	3.9	1,455	38.8	1,900	6.3
Tax	(521)	(497)	4.9	(374)	39.2	(479)	8.8
Adjusted PAT	1,499	1,447	3.6	1,081	38.7	1,421	5.5
Exceptional item	0	0		0		0	
Reported PAT	1,499	1,447	3.6	1,081	38.7	1,421	5.5
PATM (%)	17.1	16.1	108.6	14.2	292.4	16.2	90.0
EPS (Rs)	170	164	3.6	122	38.7	161	5.5

Source: Company, YES Sec - Research

Our View: We like HWA based on its ongoing product portfolio upgradation, focus on software industrial business model, faster adoption of automated solutions by domestic market post Covid-19 episode & relentless execution on cost control. As India moves to add more smart cities, drive a gas - based economy, and build digital infrastructure for the future, HWA would have tremendous business opportunities. We believe domestic market recovery to happen at faster rate than exports as its parent indicated that performance of the Global Services segment would improve in H2CY21. We expect domestic revenue CAGR of 16% over FY21E-23E led by, i) Planned investments into Data Centers, Metro, Airport & Smart Infra projects, ii) HWA's focus on double digit connected software growth, iii) Major beneficiary of India's move to build energy security, drive gas-based economy by encouraging digital solutions & iv) Gaining traction from buoyant sectors like Pharma & Chemical sectors via new product launches. Export revenue CAGR of 13% over FY21E-23E driven by, i) Business integration with Parent's entities by leveraging cost efficient services,

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Honeywell Automation India

ii) New portfolios, offerings and geographic expansion supporting Honeywell's global growth agenda & ii) Supply chain localization. Average OCF/EBITDA ratio was strong at 0.67x (one of the best in industry) during FY15-20, expect it to ~1x by FY22E. HWA's continued earnings outperformance among its peers, asset light tech model & robust return ratios (RoE ex-cash/ RoIC at 71%/58% in FY20) justify its valuations. Retain 'BUY' rating on the stock with TP of Rs48,258 at 55x FY23E EPS as we introduce FY23 estimates.

Exhibit 2: Financial Summary

Y/e 31 Mar (Rs mn)	FY19	FY20	FY21E	FY22E	FY23E
Revenues	31,747	32,900	32,552	37,091	43,061
yoy growth (%)	18.0	3.6	(1.1)	13.9	16.1
EBITDAM (%)	15.9	19.3	20.0	20.5	21.5
Adjusted PAT	3,588	4,915	5,109	6,349	7,756
yoy growth (%)	43.7	37.0	4.0	24.3	22.2
EPS (Rs)	405.9	556.0	578.0	718.2	877.4
P/E (x)	104.7	76.4	73.5	59.2	48.4
P/BV (x)	21.5	17.2	14.2	11.6	9.5
EV/EBITDA (x)	72.2	56.7	54.8	46.1	37.1
Net D/E (x)	(0.7)	(0.7)	(0.7)	(0.8)	(0.8)
ROE (%)	22.7	25.0	21.2	21.6	21.5
ROIC (%)	52.9	58.3	53.7	62.7	72.4

HWA will continue to accelerate India's move towards automation, digitalization & smart infra through best-in-class tech offerings:

- ✓ **Remote Monitoring:** Connected buildings can play an important role in managing a crisis like Covid-19. One important thing to consider with many people working from home – including facility management teams – is remote management. Remote monitoring tools allow a facility team to remotely diagnose issues with a building, conduct preventative maintenance and improve building performance and help reduce downtime.
- ✓ **Security:** Using access control and video analytics, companies can ensure the right people are in the right part of a building as well as to understand a person's access history to understand where a person has traveled throughout a building campus. Space utilization tools can also help companies implement social distancing guidelines within a building.
- ✓ **Tech protection:** Protecting the utility plant's operational technology (OT) environments from cyberattacks is equally important as the security of facilities. OT environments comprise the machinery, sensors, actuators and other building automation equipment forming the backbone of operations but have not traditionally connected to the Internet. Within smart building environments, control systems act as easy targets. Common cyber threat scenarios to consider when evaluating vulnerabilities include: accessing building control systems, disrupting power management functions, tampering with temperature settings on HVAC systems and improper network segregation using OT systems (allowing hackers potentially to access to other, more secure environments).
- ✓ **Resource optimization:** Honeywell Forge platform helps building owners and building portfolio owners to decrease operating expenses, improve energy consumption, implement predictive maintenance and manage space optimization across an entire building portfolio while also enhancing the individual occupant experience. Honeywell Forge is a hardware agnostic platform which can help building owners optimize non-Honeywell systems using the platform. This software-focused approach allows to help reduce electronic waste because there's no need to rip and replace current systems.

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