



Consumer Durables Sector In India

A Case For Business Reorganization To Enhance Capital Efficiency

2018

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\$59 bn

Indian Consumer Durables Sector

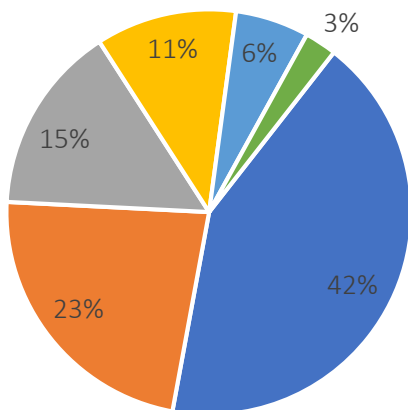
20%

Expected CAGR growth

Consumer Durables Sector In India

Consumer appliance / durable sector is amongst the fastest growing sector in India. The sector is expected to continue double digit growth and grow at CAGR 20% for FY17-22. (21% CAGR FY12-17). This growth is driven mainly by the rise of consumerism, growth in per capita income surplus, urbanization and electrification.

India's middle-class population is fast expanding and set to double over FY16-26E. Coupled with this, we are experiencing rising disposable incomes, mainly by youth and newly affluent segments. Additional income is more spent discretionary on items other than the basic needs – food, apparel, housing, health and education. Next decade we may witness high growth rate in consumption lead industries. Government focus on housing, rural electrification and other infrastructure is going to push consumerism. Electrification in rural India has moved rapid pace in the current government term. By 2020, near 100% rural electrification would not be an exaggeration



- Communication Devices
- Entertainment Electronics
- Lighting & Accessories
- Home Aid Appliance
- Air Cooling Appliance
- Cooking Aid Appliances

Source: Edelweiss, CEAMA, IBEF, Estimates (FY17E)

Mobile And Television Are Fastest Growing Segments

Smartphone has been the most disruptive force worldwide. Markets like India have rapidly adapted the smartphone technology. Nearly 500+mn smartphones users are expected to present in India by end of 2018. Communication devices including mobile phones forms 42% of the consumer durables market.

Consumption of entertainment finds priority on needs of Indians households. This has been evident from high share of entertainment electronics goods – Television, Set top boxes, Audio video players and others, which contribute to nearly one fourth of the consumer durables sector.

Lighting and accessories which includes LED, cables, switchgear, etc. is expanding as we see push on housing and electrification. The growth is expected to continue driven by government push and availability of cheaper power. This segment forms one seventh of the sector.

Home aid (refrigerators, washing machines, water purifiers) and cooking aid segment (Oven, microwave, induction cookers, others) are the key segments driven by brands and consumerism. This is growing because of product innovation and market segmentation by brands. The goods however fall in luxury needs and hence growing lower than sector average.

Air Cooling appliances which includes Air conditioners, Air coolers, air purifiers, fans form just 6% of the sector. However, this sector is highly under penetrated as compared to other developing countries in tropical zone. With changing climatic conditions and availability of power, we can expect supply disruptions in the sector led by rapidly changing consumer preferences.

Penetration Levels Still Low

While penetration of consumer durables across various categories has been steadily increasing, it is still lower as compared to other emerging economies.

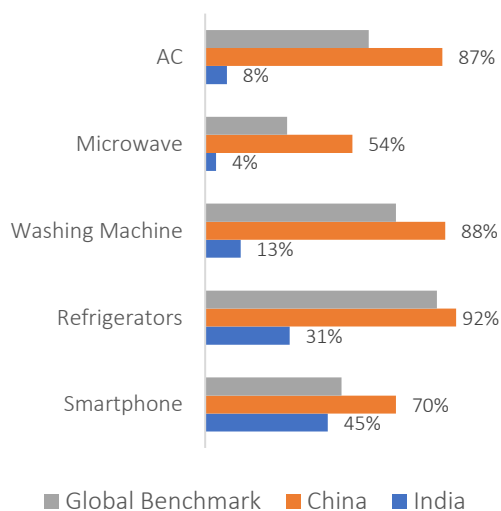
Indian markets have been highly cost sensitive while adopting technology. Hence the challenge for brands is to come up with frugal product for Indian consumers through cost effective supply chain to overcome these penetration issues and high service capabilities. Infrastructure issues like lack of electricity, power load shedding, water shortage, etc shall take time to overcome. However, with infra push by Government outlook seems to be positive.

The growing penetration is expected to fuel the robust growth in the sector over the next 5-7 years.

Consumer Becoming The Emperor

Technology has been a disruptive force. We are more connected and more globalized today. Social media has been driving and influencing customer preferences. Pressure is on brands to meet consumer needs, especially in case of consumer durables. We have seen birth and death of many categories in this sector. Air Conditioners with inverters, air purifiers, wall mounted air coolers, electronic drive remote operated fans, are just to name few newly emerging sub categories to meet needs of consumer.

Penetration



Source: PWC / CEAMA

Private labels launched

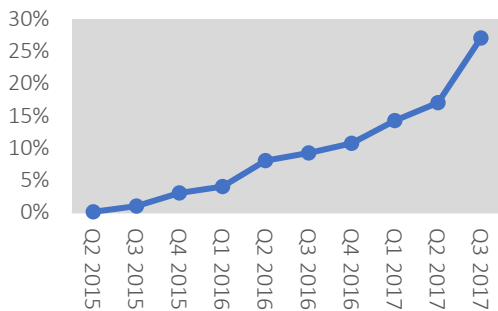
- Flipkart – MarQ , Billion
- Future – Koryo, Sensei
- Trent – Croma
- Reliance – Rconnect
- Next Retail – Hyundai
- Amazon – Echo

Rise Of Distribution Channels And Their Private Labels

Last five years, we have seen rapid rise of modern retail and ecommerce platforms. Croma, Next, Ezone, Dmart, Reliance Digital, Vijay sales, Digi1 are few domestic modern retail formats in consumer durables space grown in last decade. With easing of FDI, international modern retailers can soon join the party. Amazon, Flipkart and PayTM have emerged as top three horizontal ecommerce players with distinct customer acquisition advantage. These new distribution formats have made easy for brands to reach out to customers. Exclusive online launches have seen an attractive way for new brands to launch in India.

Shoppers' confidence in online/modern retail and online payment / finance solutions have supported these platforms further. This pull of customers to these platforms have resulted in the growing interest of private labels. Many retailers have been importing consumer durables from other Asian manufacturers and marketing in India. With local contract manufacturing space improving, private labels are competing with established brands in established market segments.

Market Share of Xiaomi in India



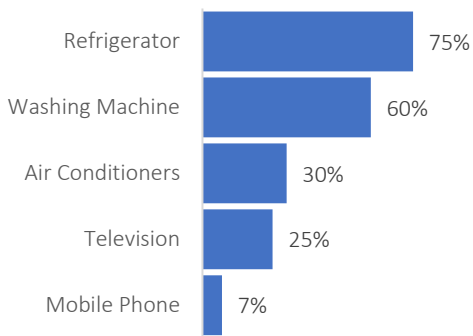
Source: IDC

Entry Of International Brands

India is now more open to International brands. In the last three years, there has been drastic increase in number of international brands who have jumped into Indian consumer markets. India has witnessed advantages of ease of doing business; providing conducive environment to more brands to launch their product range catering to Indian markets.

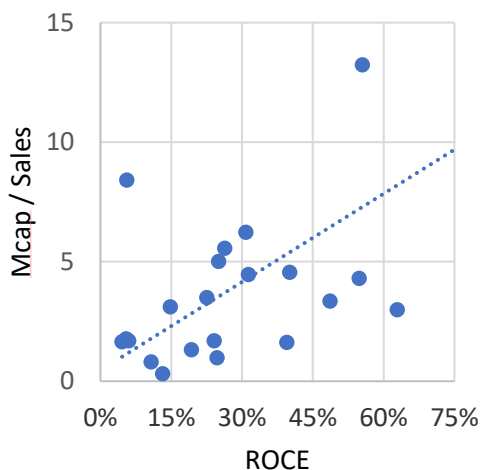
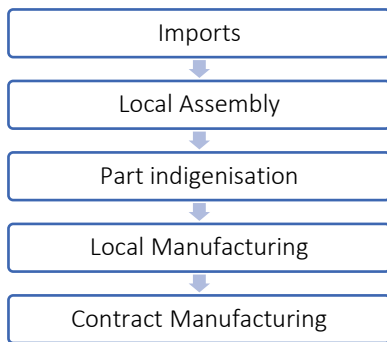
For example, we have seen rapid growth of Xiaomi in India. It has taken 27% (Q32017) of the ₹1.6tn mobile market from nowhere in 3 years leaving behind established brands. Entry barriers for launching a new brand in India has virtually vanished! It is possibly time that just like mobile, consumer durable brands from other categories shift manufacturing focused strategies and rather focus on product innovation and customer experience through distributed contract manufacturing and enhance after-sales service.

Value Addition in India



Source: PWC / CEAMA

Value addition = Value of bill of material sourced from India



Source: Capitaline (12 Jan, 2018)

Based on FY17 audited numbers

Greater Value Addition In India

With the competitive business environment, it is imperative for brands to innovate. Speed to market and cost competitiveness are critical. Business models have been evolving over time. Today brands are selling locally manufactured product as compared to a complete imported product, a decade ago. However, scope of value addition through local manufacturing still exists in multiple categories. Supply side constraints are slowly fading as local manufacturers have developed varied manufacturing competencies including sheet metal work, plastic moulding, PCB design and manufacturing.

Evolution Of Contract Manufacturing Ecosystem

Globally in matured markets, most brands have limited or no own manufacturing facility and widely rely on contract manufacturing. Brands focus on controlling quality and enhancing customer experience. In India, domestic contract manufacturing ecosystem has evolved over past 5 years and companies like Dixon and Amber are leading the pack of Indian contract manufacturers. Many global contract manufacturers like JABIL, Foxconn, Flextronics have also set up facilities in India.

Capital Market Investors Prefer High ROCE for Consumer Oriented Companies

Investors prefer Asset Light business over asset heavy business models. Asset light businesses are better equipped to handle dynamic changing markets and competition. What delights investors? —high growth, strong profitability, rising capital efficiency and brand consolidation suggesting profitable leadership. Such companies generate high cash and provides opportunity for inorganic growth. This is evident if we look at Market capitalization to sales versus ROCE of listed companies in Consumer durable space. Symphony with fully outsourced manufacturing commands highest valuation premium and is a testimony to this thesis.

Contract manufacturing offers brands benefits of better capital efficiency, ability to augment product portfolio with greater speed to market.

Preferred Strategy For Brands

Contract Manufacturing seems to be preferred strategy for many listed players in consumer durables sector. Given the investor preference on high ROCE business, companies are trying to be lean on capital resources through contract manufacturing. Brands are focusing on product design, innovation, product quality, sales and marketing.

Contract manufacturing as a strategy has also helped brands augment their product portfolio. Speed to market of any product in its life cycle has increased. Even companies with inhouse manufacturing facilities are using this approach. For example, Whirlpool India has manufacturing facilities for washing machines and refrigerators in Faridabad, Pune and Puducherry while manufacturing of Air conditioners is completely outsourced. Benefits of Product diversification and Speed to market

USD mn	Mcap	Sales	P/E	Mcap/Sales
Dixon	667	378	77	1.6
PG Electroplast	107	56	104	1.8
Amber Enterprises*	415	254	96	1.6
*IPO in Jan 2018, expected minimum valuation				

Attractive Valuation Of Contract Manufacturers

Market seem to be valuing the greater need for contract manufacturers in current market conditions. Hence few listed players in India are enjoying rich valuation. Indian contract manufacturers also have potential to leverage India location as export manufacturing hub for global consumer durable brands.

Players like Dixon Technologies and Amber Enterprises have potential, organically or inorganically, to become larger multi-product platform for undertaking contract manufacturing for domestic and international brands. Their recent capital raise and market valuations provides them with currency for acquisition and rapid growth.

At IMAP, we believe that there will be an urgent need as well as an opportunity for consumer durable / brand owners to increasingly shift to contract manufacturing and this would result in significant deal activity on this front in 2018 & 2019.

4. M&A and PE Transactions (2010-17)

Year	Investee / Target	Investors	Sub Sector	Amt (\$mn)	Deal Type
2017	Consumer Division of Llyod Electric	Havells	Consumer Durables	250.0	Acquisition
2017	Bharat Refrigeration	Ice Make Refrigeration	B2B refrigeration equipment	NA	Acquisition
2017	Guts Electromech	V-Guard	Switchgears	NA	Acquisition
2017	Voltas	Arcelik	White goods	NA	JV
2017	Morphy Richards	Bajaj Electricals	Kitchen Appliances	NA	Trademark Agreement
2017	Starlite Lighting	Bajaj Electricals	Lighting	NA	Acquisition
2017	F1 Info Solutions	Flipkart	Mobile Repair Services	NA	Acquisition
2015	Munters Keruilai, China	Symphony	Air Coolers	0.4	Acquisition
2015	Promptec	Havells	Lighting Solutions	10.3	Acquisition
2014	La Opala	WestBridge	Consumer Goods (Tableware)	9.2	PIPE
2014	Avni Energy Solutions	SIDBI VC	LED Lighting	NA	PE
2014	TTK Prestige	Nalanda Capital	Consumer Durables (Kitchen Appliances)	7.7	PIPE
2014	V-Guard Industries	MCap Fund	Consumer Durables	3.2	PIPE
2013	Bajaj Electricals	WestBridge	Consumer Durables (Electrical Appliances)	1.1	PIPE
2013	Blue Star	SAIF	Air Conditioning	0.3	PIPE
2013	TTK Prestige	Cartica Capital	Consumer Durables (Kitchen Appliances)	21.9	PIPE
2013	TTK Prestige	Cartica Capital	Consumer Durables (Kitchen Appliances)	18.8	PIPE
2012	Amber Enterprises India	Reliance Equity	Contract Manufacturing (Consumer Durables)	12.6	Late
2012	Blue Star	SAIF	Air Conditioning	9.0	PIPE
2012	Blue Star	SAIF	Air Conditioning	3.0	PIPE

Year	Investee / Target	Investors	Sub Sector	Amt (\$mn)	Deal Type
2012	Butterfly Gandhimathi	Reliance Equity	Consumer Durables (Kitchen Appliances)	20.0	PIPE
2012	Carrier	Midea, China	Air Conditioning	NA	JV
2011	Amber Enterprises India	IFCI Ventures	Contract Manufacturing (Consumer Durables)	7.0	PE
2011	IMPCO Mexico	Symphony	Air coolers	NA	Acquisition
2011	Maya Appliances (Preethi brand)	Phillips	Kitchen Appliances	NA	Acquisition
2010	NTL Electronics India	CX Partners	Equipment (Electronic)	20.0	PE
2010	Stovekraft	Sequoia Capital India	Consumer Durables (Kitchen Appliances)	11.0	PE

Source: Multiple Industry News

191

Deals closed in 2017

\$12+ bn

Transaction value of deals closed in 2017

36%

Cross border transactions share in 2017

About IMAP

IMAP is a global network of investment banking firms with presence in 35 countries. IMAP closed over 2100 transactions valued at \$90+bn in last 10 years. IMAP is ranked 7th in the world in the mid-market segment by Thomson Reuters and has executed 191 transactions worth US\$12 billion in 2017. IMAP has 48 offices in more than 35 countries, > 400 M&A professionals. IMAP India is exclusive India partner of IMAP.

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