

Demerger Plan Could Lift HSIL Stock by 20%

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Mumbai: Shares of HSIL could rally 20% in the next two-three months as the company decides to unlock value by demerging its consumer products, distribution and marketing business into a new entity Somany Home Innovation (SHIL). Typically, consumer products businesses are traded at a higher PE than manufacturing businesses, according to analysts.

HSIL will retain the manufacturing of all the building and consumer products in addition to manufacturing and sales of packaging products. The companies will have a mirror shareholding of 1:1 ratio for HSIL and SHIL, and the management reckons that it will take between two and three quarters for the process to be completed.

“Stocks can see a run-up on shareholders’ approval as was seen in recent demergers such as Reliance Capital and Tube Investments,” said Niraj Kabra, analyst, Emkay Global. “The valuation of these two businesses together, based on the FY20 estimated earnings, is expected to be at ₹4,327 crore with SHIL at ₹3,276 crore and HSIL at ₹1,051 crore.”

Currently, the combined business is trading at a market capitalisation of ₹3,276 crore. The HSIL stock has rallied 74% so far this year to close at ₹496 on Wednesday.

Also, the branding, marketing, sales, distribution of building products will be transferred to a new company called Brilloca which will be a wholly-owned step-down subsidiary of SHIL. Post sanction of this scheme, SHIL will apply for listing on the stock exchanges.

Projections

| FY 2020 Estimated | SHIL | HSIL |
|----------------------|-------|-------|
| EBIDTA (₹ Cr) | 180 | 280 |
| PAT (₹ Cr) | 109 | 70 |
| PE (X) | 30 | 15 |
| Valuation (₹ Cr) | 3,276 | 1,051 |

SOURCE: Emkay Global

“Our quick view is that SHIL will emerge as a low capital employed, high return trading business post the demerger; but HSIL will remain a low return business,” said Samar Sarda, analyst, Kotak Securities.

HSIL is the market leader in the sanitaryware segment with 32% market

share and is the second largest container glass player in India after HNG.

HSIL always traded at a discount to its peers despite its strong brand franchise, but now the situation will change, said analysts.

“The company’s RoE is lower than that of its peers, however HSIL is likely to see higher RoE expansion than peers, given its entry into a few high-margin segments and reduction in losses in consumer products,” said Kritika Subramanian, analyst, IIFL. “We expect growth in sanitaryware to accelerate, led by overall improvement in the economy and capacity expansion; glass segment is likely to see improved outlook in the medium term. However, we are awaiting clarity on the balance sheet charges for post-demerger valuation of both companies.”