

Management Discussion and Analysis

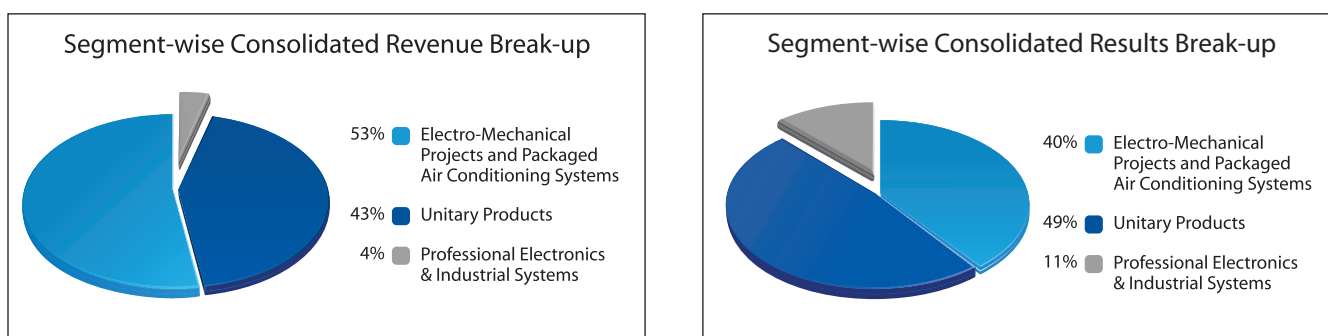
In the context of Blue Star's business operations and strategic positioning that are fully described in the Board's Report and Integrated Report, a detailed analysis of the operating business as well as financial performance is enumerated in the ensuing sections of this report.

INDUSTRY STRUCTURE AND DEVELOPMENTS

Blue Star is a leading player in the air conditioning and refrigeration industry in India. An overview of the industry and the current market dynamics are described in detail in the Integrated Report (refer Industry Structure and Developments on page no. 22).

SEGMENT-WISE ANALYSIS

The consolidated revenue and results break-up in terms of business segments were as follows:



ELECTRO-MECHANICAL PROJECTS AND PACKAGED AIR CONDITIONING SYSTEMS

The Electro-Mechanical Projects and Packaged Air Conditioning Systems business accounted for 53% of the Company's Total Revenue from Operations.

In the Electro-Mechanical Projects business, growth was mainly driven by Buildings & Factories, Infrastructure, and Industrial segments, amongst others. New order acquisitions gained momentum compared to the previous year with Buildings & Factories together contributing to around 90% of the total order bookings. In particular, the market witnessed a moderate upswing in the office space consumption. The business continued to expand into the Hospital and IT spaces as well. For the third year in a row, more than 50% of the orders were multi-service orders and the Company continues to lead the industry in this category.

Blue Star won the 'MEP Contractor of the Year 2018' award from Construction Week India in recognition of MEP services provided for the Delhi Metro across overhead stations and depots. With this award, the Company was recognised for the fourth time in a row by Construction Week India. Earlier, Blue Star had won this award twice; in 2017, the Company had bagged this award for providing MEP services to Delhi Metro for underground stations and likewise, in 2015, for Mumbai International Airport. Besides, in 2016, Blue Star was declared as a runner-up for the services provided for the Bengaluru Metro.

Some significant orders secured by the Electro-Mechanical Projects Business during the year include Apollo Tyres, Chennai; Brookefield, NCR; Mumbai Metro; Amrita Hospital, Faridabad; Wipro, Hyderabad and Chennai; RMG, Chennai; All India Institute of Medical Sciences, Guntur; Karle, Bengaluru; Kohinoor, Mumbai; Deloitte, Hyderabad; Indiabulls, Mumbai; DLF, Gurugram; Myntra, NCR; Meenakshi Group, Hyderabad; Public Works Department, Mumbai; Barclays, Pune; Biocon, Mangaluru; Embassy Group, Bengaluru; and Radisson Blu, Nashik; amongst others.

With a commitment to remain true to its value proposition of 'Superior Project Delivery' through intelligent engineering, modern execution practices, and committed teams, the Electro-Mechanical Projects Business established, during the year, a Resource Management Group that works towards ensuring modern and best-in-class project management practices across projects under execution.

In the Commercial Air Conditioning segment (erstwhile Central Plant Equipment segment), the Company registered healthy growth across product categories including ducted systems, VRF systems, and chillers, thereby significantly increasing its market share in each. In particular, VRF systems and screw chillers gained significant traction with market shares ramping up to around 17% and 15%, respectively, while ducted systems and scroll chillers maintained a market share of 39% during the year.

During the year, the Company launched configured oil free centrifugal chillers with a wide capacity ranging from 80 TR to 450 TR, which are capable of delivering an IPLV of 11.7, one of the best efficiency levels in the industry.

Blue Star also embarked on several initiatives to strengthen its outreach in the existing markets and to penetrate into unrepresented markets as well as to manage and motivate its channel partners. The Company conducted micro meets in numerous Tier 2 and 3 cities. To expand its distribution network in this category, the Company deployed more than 100 channel partners in 40 unrepresented towns. A VRF sales software tool was rolled out to assist the channel partners in offering technically correct solutions, and is expected to give phenomenal support to the new channel partners, especially in smaller towns.

Some of the notable orders received during the year were from Meenakshi Infrastructure, Noida Stadium, Niruvi Hospital, CEAT Tyres, Siemens, BHEL, Xavier University, Fantasia Mall, Poddar School, GITAM University, Deloitte Consulting, Reliance Retail, and Avenue Supermarkets, amongst others.

UNITARY PRODUCTS

This business segment comprises room air conditioners as well as commercial refrigeration products and systems, apart from water purifiers, air coolers and air purifiers.

During the period under review, the room air conditioners industry was impacted by multiple headwinds due to soft summer conditions, increase in commodity prices, depreciation of the Rupee and increase in customs duty. Soft summer conditions coupled with lukewarm demand during the festival season led to higher than normal inventory holding across the industry and resulted in pressure on margins. In such a challenging year, the Room Air Conditioners business outperformed the market, thereby increasing the Company's market share to 12.3% in value terms. Blue Star launched 75 new superior and stylish AC models including energy-efficient inverter ACs capable of delivering 30% extra cooling over and above its rated capacity. This enables faster temperature pull-down even in crowded rooms as well as larger rooms during peak summers, thereby consuming less power and leading to significant savings on electricity bills.

Blue Star's share in the 5-star air conditioners segment is higher than that of the industry, signifying that the Company enjoys a preference amongst discerning consumers who purchase premium products. The complete range of inverter models is equipped with eco-friendly refrigerants. The new range also comprises 5-star rated inverter split air conditioners with built-in Air Purification Technology.

Besides, the Company also launched a new smart customer-centric mobile application which in addition to its capability to remotely monitor and control the machine, allows the consumers to personalise their AC profile, group the ACs for better control, optimise settings as well as integrate this app with home automation systems. Blue Star's smart inverter split ACs also come with a unique smart Wi-Fi App based on Internet of Things (IoT). This app has a feature of 'Smart Budget Management' embedded in it which enables the users to manage their budget smartly, track their AC usage trends, as well as schedule their AC with respect to different time and sleep curve management. Users can also update the latest features through 'Over the Air' (OTA) programming in their smart phone.

Blue Star also added several new customers in its National Accounts Business during the period under review. The year saw healthy order booking traction amongst customers in retail, restaurants, healthcare, and industrial segments.

The Company also launched a new range of air coolers under its sub-brand, 'Windus' which is equipped with a unique Cross Drift Technology that helps in faster cooling in harsh and dry summers. The range comes with different water tank capacities starting from 35 litres to 75 litres.

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The Commercial Refrigeration products business surpassed and outperformed the market with its wide spectrum of offerings including deep freezers, bottle coolers, visi coolers, visi freezers, water coolers, and bottled water dispensers as well as commercial kitchen refrigeration products, healthcare refrigeration products, supermarket refrigeration products and modular cold rooms. During the year, the Company successfully catered to diverse needs across various customer segments such as Dairy, Ice-cream, Processed Foods, Pharmaceutical, Hotels, Restaurants, Fast Food chains, Retail outlets, and several institutional clients. Blue Star's foray into adjacencies such as commercial kitchen refrigeration and healthcare refrigeration products and solutions evoked a good response and gained traction in the market during the year with the Company winning several notable orders from Foodpanda, Indian School of Hospitality, Andhra Pradesh Medical & Infrastructure Development Corporation, Chittaranjan National Cancer Institute in Kolkata, and the technical wing of Uttar Pradesh Police, amongst others. In addition, the Company's recent inroads into the supermarket refrigeration equipment and solution segment has gained quick market acceptance with several major retail players such as Metro Cash & Carry, SPAR, Spencers, and 24X7, amongst others, who have placed orders with the Company.

The Company's deep freezers and modular cold rooms witnessed steady growth underpinned by demand from Havmor, Amul, Hatsun, Creambell, Vadilal, and Dinshaws, to name a few. Expansion of e-tailers and portals such as Big Basket, Swiggy and Zomato accompanied by aggressive expansion plans from Quick Service Restaurants such as Domino's, McDonalds, KFC, Pizza Hut, and Sapphire Foods, amongst others, resulted in increase in demand for the Company's modular cold rooms.

The Company regularly launches new products and solutions in the commercial refrigeration space to cater to the emerging needs of varied customer segments and is a preferred partner for several reputed brands across segments. Besides, the Company is reckoned for robust distribution, as well as swift and timely after-sales service support. Overall, the Company's commercial refrigeration business was successful in reaping in good performance during the year and contributed significantly to the overall growth and profitability of the Company.

To combat the rising pollution levels in many cities across India, Blue Star also introduced a new range of innovative air purifiers with Sens Air Technology, along with Nano-e, Plasma, and UV purification systems.

During FY19, Blue Star made significant progress in the residential water purifiers business with the revenues in FY19 doubling over FY18. The water purifiers business expanded its product portfolio to add new series of products in the RO/RO+UV range in the entry/mid-level segment including an aggressively priced product range for e-commerce platforms. With the addition of these series, Blue Star now has a comprehensive range of models across various price points from ₹10,900 to ₹46,900 in the RO range. In addition, it launched Immuno Boost technology in select variants which offers alkaline antioxidant water that boosts metabolism, reduces acidity, improves hydration and enhances immunity.

The Company also launched a range of commercial RO+UF as well as commercial UV water purifiers which are targeted to water cooler customers of Blue Star as well as offices, restaurants, clinics, and other commercial establishments. In addition, it launched India's first point-of-use instant UV LED purifier, which offers pure water instantly without waiting for the warm up time of the UV lamp, as this model is powered by an eco-friendly non-mercury UV LED. Moreover, it offers a lifetime warranty on the UV LED which makes this product a unique and differentiated offering in markets which have fresh water supplies.

During the year, the Company consolidated its distribution and began focusing on enhancing channel effectiveness as well as identifying new channel partners who can strengthen the availability of the products in the markets it operates in. Aggressive sales and marketing initiatives coupled with a comprehensive product range across price points helped to enhance its market share to 2%. Blue Star water purifiers are present in 2800 touch-points across 150 towns and cities. It also engaged over 400 star water consultants (in-store demonstrators) who are available at retail outlets to highlight the superior features of Blue Star's water purifier range. These personnel carry out activations and other field marketing activities for brand awareness and lead generation as well. The Company also made significant inroads in the e-commerce market which is showing a lot of potential to grow, with the Company having strong presence in leading portals such as Amazon, Flipkart, Paytm and Tata CLiQ.

In Feb 2019, Blue Star won the prestigious Water Digest Award for the third time in a row for the 'Best RO+UV Domestic Purifier'. The Company had won this award in 2017 as well as 2018. This year it highlighted its Immuno Boost technology that provides alkaline and antioxidant water. In addition, it also won another award 'Best Water R&D and Technological Breakthrough' for its instant UV LED purifier. Water Digest Awards are considered amongst the most prestigious in the water industry and this initiative is supported by the Ministry of Water Resources and UNESCO. These awards were evaluated by an eminent jury comprising heads of several NGOs involved with the water industry, apart from TERI and UNESCO.

PROFESSIONAL ELECTRONICS AND INDUSTRIAL SYSTEMS

For over six decades, the Professional Electronics and Industrial Systems business has been the exclusive distributor in India for many internationally renowned manufacturers of hi-tech professional electronic equipment and services, as well as for industrial products and systems. Over the years, the Company has significantly scaled up operations in this business and has moved up the value chain by changing its business model from being merely a distributor to that of a system integrator and value-added re-seller. This business is handled by Blue Star Engineering & Electronics Limited, a wholly owned subsidiary of the Company. The business operates in two broad segments: Professional Electronics that comprises Healthcare Systems, Data Security Solutions, Infra Security Solutions and Communication Systems; and Industrial Systems that encompasses Testing Machines, Non Destructive Testing (NDT) Systems and Industrial Automation, NDT Products and Industrial Products. The business has been successful in capturing the pulse of the market and has carved out profitable niches for itself in most of the specialised markets that it operates in.

During the review period, while Industrial Systems, with some significant order wins, gradually regained traction from the sluggish market conditions, Professional Electronics grew, propelled by increased orders in the Data Security Systems and Healthcare businesses. The Healthcare Systems business performed well and registered good growth driven by a significant large order of CT scanners from the Government, Medical and Health Services sector. The Data Security business continued on the growth path aided by digitisation initiatives with orders from major banks, certificate authorities, telecom and payment technology companies. The Infra Security business, which predominantly revolves around video surveillance, was majorly engaged in project execution. The Communication Systems business that predominantly deals with radio frequency, microwave as well as avionics test and measuring equipment, also secured a few orders from the defence, space and aerospace sectors.

Research centres and agricultural universities continued to place orders for a wide range of inspection equipment including universal testing machines and customised plant growth chambers enabling the Testing Machines business to clock good performance through the year. The Non-Destructive Testing Systems and Industrial Automation business augmented its automation offerings and booked substantial orders in the latter part of the year from steel and defence segments. The Non-Destructive Testing Products business, with a highly diversified portfolio including technologies such as ultrasound, RVI, X-ray, industrial CT, radioscopy, portable radiography, eddy-current, and metrology, secured orders from the automotive, aerospace and inspection sectors. The Industrial Products business, which mainly deals in industrial valves and filters, despite a slowdown, was able to sustain itself by securing orders from the Oil & Gas industry.

Further, with the intent to improve focus on its chosen customer segments, the business continued to reorient its internal organisation structure. The business unleashed its value proposition 'Superior Technology Solutions' thereby reinforcing its core capability. Besides, it revamped its corporate website and launched a service management tool called, 'Dart' for service engineers and managers. This business continues to exert greater thrust on business development, sales automation, service management and project execution functions.

MEDIUM-TERM AND LONG-TERM STRATEGY

Strategy formulation for medium to long term as well as its execution and review have always been a part of the Company's planning process. The Company regularly monitors and evaluates its internal strategies vis-à-vis the dynamic external environment (refer Strategy Planning and Development on page no. 54).

FINANCIAL PERFORMANCE ANALYSIS

Effective April 1, 2018, Blue Star Limited has adopted Ind AS 115 and accordingly, has realigned its revenue recognition policies appropriately. The accounting changes have been applied with retrospective effect to each of the prior reporting periods presented.

Following are the financial highlights of the Company for the year ended March 31, 2019 on a comparable consolidated basis.

1. INCOME

Total Income for the year ended March 31, 2019 was ₹5259.53 crores as compared to ₹4665.08 crores in the previous year, an increase of 12.7%.

2. COST OF SALES, WORK BILLS AND SERVICES

The cost of sales, work bills and services during the year was ₹3931.18 crores as compared to ₹3464.13 crores in the previous year. This cost was 75.1% of the Revenue from operations as compared to 74.5% in the previous year.

3. EMPLOYEE REMUNERATION AND BENEFITS

Employee cost for the year at ₹421.49 crores increased by 6.0% as compared to ₹397.72 crores in the previous year. The employee cost was 8.0% of the Total Income as compared to 8.5% in the previous year.

4. OPERATING AND GENERAL EXPENSES

Operating and general expenses increased to ₹535.63 crores from ₹520.38 crores in the previous year. As a percentage of Total Income, the Operating and general expenses for the year were at 10.2% as compared to 11.2% in the previous year.

5. FINANCIAL EXPENSES

Finance cost for the year was at ₹47.87 crores as compared to ₹28.74 crores in the previous year. The financial cost for the year increased to 0.9% of the Total Income as compared to 0.6% in the previous year.

6. DEPRECIATION

Depreciation charge for the year increased to ₹74.90 crores as compared to ₹63.81 crores in the previous year.

7. PROFIT BEFORE TAX AND EXCEPTIONAL ITEMS

Profit before tax and exceptional items for FY19 increased by 30.6% to ₹248.46 crores as compared to ₹190.30 crores in FY18. Profit before tax and exceptional items was 4.7% of the Total Income as compared to 4.1% in the previous year.

8. EXCEPTIONAL ITEMS

There was a net exceptional income of ₹2.68 crores during the year. Profit on sale of property of ₹15.18 crores which was offset by spend on Platinum Jubilee expenses of ₹12.50 crores.

9. PROFIT BEFORE TAX AND AFTER EXCEPTIONAL ITEMS

Profit before tax and after exceptional items for FY19 increased by 28.4% to ₹251.14 crores as compared to ₹195.57 crores in FY18. Profit before tax and after exceptional items was 4.8% of the Total Income as compared to 4.2% in the previous year.

KEY FINANCIAL RATIOS

SR NO	RATIO	UOM	FY18	FY19	% change
1	Debtors Turnover Ratio	Times	5.2	5.1	-2%
2	Inventory Turnover Ratio	Times	3.9	4.2	6%
3	Interest Coverage Ratio	Times	7.6	6.2	-19%
4	Current Ratio	Times	1.1	1.1	-
5	Debt Equity Ratio	Times	0.37	0.28	-24%
6	Operating Profit Margin (%)	(%)	5.9	6.6	13%
7	Net Profit Margin (%)	(%)	4.2	4.7	13%
8	Return on Net Worth	(%)	17.8	21.4	20%

There have not been significant changes in the key financial ratios in the current year as compared to the previous year.

Return on net worth for the year improved to 21.4% from 17.8% in the previous year driven by the following:

- A growth of 13% in Revenue from Operations
- Management of fixed cost at a reasonable level
- Reduction of tax expenses due to a one-time deferred tax credit
- Marginal increase in capital employed compared to growth in Revenue from Operations

INTERNAL CONTROL SYSTEMS AND THEIR ADEQUACY

The Company has established an internal control system, commensurate with the size, scale and complexity of its operations. In order to enhance the standards of controls and governance, the Company has adopted the COSO 2013 framework to ensure that robust internal financial controls exist in relation to operations, financial reporting and compliance. In addition, the internal audit function reviews and reports to the Audit Committee around compliance with internal controls, the efficiency and effectiveness of operations as well as key process risks. During the year, as part of the Management's control testing initiative, the internal controls were tested and found effective.

RISKS AND CONCERNS

RISKS

The primary operating risks which could impact the Company relate to dependence on room air conditioners products sales, volatile exchange rates, interest rates, credit risks, procurement concentration risk, volatile commodity prices risks, changes in tax and other legislations as well as risks arising out of higher input costs, especially in the case of fixed price contracts, health and site safety, and changes in technology which impact the Company's product offerings. In addition, a general slowdown in the global and local economy tends to aggravate risks faced by the Company. Blue Star lays great emphasis on risk management, and has put in place a robust system for risk identification, assessment and mitigation with strong internal controls, at both business groups and corporate level. Significant risks across the entity are reviewed periodically by the Risk Committee. Further, the mitigation action plans are integrated with the internal audit plans and embedded in the strategic business plan of each business group (refer Risks and Mitigation Strategies on page no. 56).

CONCERNS

A confluence of factors on the global and local front such as usage of tariff and non-tariff barriers to address trade imbalances, volatility in crude oil and commodity prices, and the outcome of general elections in India, could impact business and consumer confidence. The Company will continue to closely monitor the macro and micro level trends in the global and Indian economy, and will take necessary steps to address these challenges.

OPPORTUNITIES

The Company's presence in multiple segments across the industry, low penetration levels in the segments in which the Company operates, increasing urbanisation and investments driven by the Government in the infrastructure space, provide the Company with opportunities to grow. These opportunities have been elaborated in the Integrated Report. (refer Opportunities on page no. 59)

HUMAN RESOURCES

The Company remains committed to nurturing and empowering its people. With caring for its people a way of life at Blue Star, the Company has been successful in fostering a people-centric cohesive trust based culture within the organisation that has been instrumental in creating and retaining its diverse pool of intellectual capital. The Company continues in its endeavour towards embarking on employee friendly initiatives and practices. (refer Integrated Report on page no. 40)

CORPORATE OUTLOOK

Increased opportunities from the commercial real estate market and factory segments besides continuing thrust on infrastructure projects are expected to drive growth in the Electro-Mechanical Projects business. Room airconditioners segment is expected to grow faster than FY19 with the onset of summer in most parts of the country in April. The continued growth momentum in the ice-cream and frozen foods segments is expected to unleash opportunities for commercial refrigeration products. The Company also intends to maintain the pace of revenue growth in the Professional Electronics & Industrial Systems segment.