



VISIT NOTE

SUPRAJIT ENGINEERING

Ready to soar



Edelweiss
Ideas create, values protect

India Equity Research | Automobiles

Our recent interaction with Mr. Ajith Rai, Chairman & Managing Director, Suprajit Engineering (SEL), reinforces our conviction on its long-term prospects. Our optimism is anchored by: (1) SEL's inorganic growth strategy to take advantage of the consolidation in the global ancillary space; (2) sustained momentum in automotive cables exports—management estimates revenue to jump 2x over FY18-21E; (3) Wescon's expanding product basket & geographical footprint beyond US; and (4) resolution of Phoenix Lamps' issues. We believe, inorganic initiatives will continue to add value (five successful acquisitions ample testimony) as SEL further diversifies its customer and regional mix. Maintain 'BUY' with TP of INR340 (21x FY20E PER).

Key takeaways:

- Inorganic opportunities:** SEL will continue to scout for acquisitions to plug gaps in customer profile, distribution, technology, etc. Focus will primarily be on buying assembly-type businesses which entail lower capex and higher human intervention. The company is focusing on expanding its international presence given the consolidation that's underway in the auto ancillary space.
- Cables business:** In the automotive cables business, exports to existing customers have gained strong traction. Efforts are underway to further widen the customer base. In the domestic market, while SEL's penetration in two wheelers remains high, efforts are being made to penetrate Maruti, Hyundai and Toyota in passenger vehicles. In the non-automotive space, management is focusing on expanding customer base as well regional reach.
- Phoenix Lamps:** As the H7 line issues have been resolved, management expects improvement in the plant's utilisation—at ~40% at FY18 end from ~20% at the beginning of FY18.

Outlook and valuations: Gaining momentum; maintain 'BUY'

We like SEL's focus on FCF & sustainable growth and believe the company is well placed to capitalise on recovery in its domestic and international businesses. We estimate consolidated EPS to clock 28% CAGR and RoCE to improve 760bps to ~32% over FY18-20. We maintain 'BUY'. At CMP, the stock trades at FY20E PE of 16.5x.

Financials

(INR mn)

Year to March	FY17	FY18	FY19E	FY20E
Revenues	12,028	14,311	17,010	20,338
Rev. growth (%)	26.3	19.0	18.9	19.6
Adjusted Profit	1,137	1,385	1,765	2,259
Basic shares outstanding (mn)	140	140	140	140
Adjusted diluted EPS (INR)	8.1	9.9	12.6	16.1
EPS Growth (%)	27.0	21.8	27.5	28.0
Diluted P/E (x)	32.8	26.9	21.1	16.5
EV/EBITDA (x)	19.9	16.3	12.9	10.1
ROAE (%)	22.2	23.5	24.4	25.8

EDELWEISS RATINGS

Absolute Rating	BUY
Investment Characteristics	Growth

MARKET DATA (R: SUPE.BO, B: SEL IN)

CMP	: INR 266
Target Price	: INR 340
52-week range (INR)	: 349 / 227
Share in issue (mn)	: 139.9
M cap (INR bn/USD mn)	: 37 / 552
Avg. Daily Vol. BSE/NSE ('000)	: 97.2

SHARE HOLDING PATTERN (%)

	Current	Q3FY18	Q2FY18
Promoters *	44.5	44.5	44.5
MF's, FI's & BKs	4.6	4.6	4.6
FII's	10.4	10.4	9.7
Others	40.5	40.5	41.1
* Promoters pledged shares (% of share in issue)	:		NIL

PRICE PERFORMANCE (%)

	BSE Midcap Index	Stock	Stock over Index
1 month	(3.7)	9.2	4.8
3 months	(0.1)	24.3	27.3
12 months	-4.8	18.0	22.8

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Other takeaways:

- **Inorganic opportunities**
 - SEL will continue to explore acquisitions to plug gaps in customer profile, distribution, technology, etc.
 - The company is focusing on expanding international presence given ongoing consolidation in the auto ancillary space.
- **Automotive cables:**
 - Management envisages exports to be key growth driver.
 - Mr. Ajith Rai estimates export revenue to jump 2x over FY18–21 given order book visibility. Having said that, most of the order book is from existing customers.
 - Management has sharpened focus on widening customer base. The company is keen on bagging Japanese OEMs.
 - In India, SEL has nearly 75% market share in two wheelers. In passenger vehicles, efforts are underway to deepen penetration in Maruti, Hyundai and Toyota.
- **Non-automotive cables (Wescon):**
 - A key long-term strategy is to enter new product areas in the US and expand the business in Europe. The company has successfully bagged Europe business from an existing customer (Wescon supplies to it in the US).
 - Besides, the aim is to offer two solutions to customers—Made in USA and Made in India—with differential pricing. The objective is to move mass manufacturing to India and focus on low volume/high value manufacturing in the US.
- **Lamps (Phoenix):**
 - Issues facing the lamps business have been largely resolved. Focus is on ramping up the H7 line.
 - What went wrong? Demand shift to H7 bulbs was quicker than anticipated and Phoenix (pre-acquisition) had not invested in this business. In addition, machinery imports took a long time (due to unavailability), leading to loss of a few business opportunities. However, utilisation was ramped up to ~40% by FY18 end from ~20% at the beginning of FY18.
- **New products:**
 - SEL is not averse to portfolio expansion. However, management is clear that any addition must meet certain criteria—assembly business, labour-intensive, strong cash flows, etc.
 - Besides, the company has been developing products in-house, e.g. parking brake levers, which are currently offered in international markets as part of the non-automotive cables business.

Company Description

The Suprajit Group (SEL) comprises Suprajit Engineering, Suprajit Automotive, Suprajit Europe and Phoenix Lamps. Incorporated in 1985, it is India's largest automotive cable maker with an annual cable capacity of 250mn. Through acquisition of Phoenix Lamps, the company has also entered automotive lighting. The company's customer list includes most Indian automotive majors. It also exports to many marquee global customers.

Investment Theme

SEL has clocked a robust (>20%) revenue/APAT CAGR over FY08-18, further complemented by best-in-class RoCE (>30%). This has been driven by customer diversification, prudent cost control, market share gains and high capital efficiency. The company's strategy to diversify its customer base and geography has been key catalyst for the above industry growth over the past decade. The replacement market holds immense potential. We expect GST to be a key growth driver going forward. Exports is also a key focus area—well entrenched clients, superior quality, expanding footprint and attractive value proposition to accelerate client addition and new business orders. SEL supplies ~60% of the two wheeler industry's cable requirements; ramp up in supplies to Honda and replacement market are envisaged to drive growth. Four-wheeler potential also remains huge (SEL's current share at mere ~30%).

Key Risks

Slowdown in demand: SEL derives ~90% revenue from OEMs. Hence, any slowdown in the overall industry can impact the company's revenue. Similarly, slowdown in demand in US/Europe can impact SEL's revenue.

Commodity risk: Steel is a major raw material for SEL which is sourced locally as well as from China. While any steep changes in input costs are passed on to domestic OEMs (with a lag), the arrangement in exports markets are different with risk largely borne by SEL.

Currency risk: SEL derives ~17% revenue from exports (of which ~7% revenue is billed in INR). Also, it imports ~10% of revenue and thus has a natural hedge. With exports becoming a key growth driver, we believe it will lose the natural hedge, exposing the company to currency risks.

Financial Statements

Key Assumptions

Year to March	FY17	FY18	FY19E	FY20E
Macro				
GDP(Y-o-Y %)	6.6	6.5	7.1	7.6
Inflation (Avg)	4.5	3.8	4.5	5.0
Repo rate (exit rate)	6.3	6.0	6.0	6.5
USD/INR (Avg)	67.1	64.5	65.0	66.0
Sector				
4W - domestic vol (% YoY)	4.0	8.0	13.0	11.0
2W - domestic vol (% YoY)	8.0	10.0	10.0	10.0
Company				
4W	12.0	15.0	18.0	20.0
2W	5.0	12.0	16.0	20.0
Aftermarket - Revenue assumptions	12	15	18	20
Non-Auto	10.0	10.0	12.0	12.0
Export - Revenue assumptions	24	18	15	15
Net borrowings (INR mn)	2,895	887	(393)	(1,844)
Avg. Interest rate (%)	8.8	14.8	14.1	14.1
Depreciation rate (%)	3.0	-	-	-
Dividend payout (%)	12.9	16.6	17.1	18.2
Tax rate (%)	28.7	28.3	28.3	28.3
Debtor days	68	60	56	56
Inventory days	83	71	66	65
Payable days	54	50	51	50
Cash conversion cycle	97	82	71	70
Capex (INR mn)	2,864	300	300	300

Income statement

(INR mn)

Year to March	FY17	FY18	FY19E	FY20E
Income from operations	12,028	14,311	17,010	20,338
Materials costs	6,899	8,007	9,462	11,211
Manufacturing expenses	1,128	1,371	1,609	1,949
Employee costs	1,983	2,568	3,032	3,576
Total operating expenses	10,009	11,945	14,103	16,735
EBITDA	2,020	2,365	2,907	3,603
Depreciation	274	372	485	505
EBIT	1,746	1,993	2,423	3,097
Less: Interest Expense	291	271	240	240
Add: Other income	201.9	212.28	279.85	293.69
Profit Before Tax	1,642	1,934	2,463	3,151
Less: Provision for Tax	504	549	697	892
Add: Exceptional items	(15)	-	-	-
Reported Profit	1,137	1,385	1,765	2,259
Exceptional Items	(10)	-	-	-
Adjusted Profit	1,137	1,385	1,765	2,259
Shares o/s (mn)	140	140	140	140
Adjusted Basic EPS	8.1	9.9	12.6	16.1
Diluted shares o/s (mn)	140	140	140	140
Adjusted Diluted EPS	8.1	9.9	12.6	16.1
Adjusted Cash EPS	10.1	12.6	16.1	19.8
Dividend per share (DPS)	1.0	1.9	2.5	3.2
Dividend Payout Ratio(%)	14.8	22.1	23.6	23.3

Common size metrics

Year to March	FY17	FY18	FY19E	FY20E
Materials costs	57.4	55.9	55.6	55.1
Staff costs	16.5	17.9	17.8	17.6
S G & A expenses	9.4	9.6	9.5	9.6
Operating expenses	83.2	83.5	82.9	82.3
Depreciation	2.3	2.6	2.9	2.5
EBITDA margins	16.8	16.5	17.1	17.7
Interest Expense	2.4	1.9	1.4	1.2
Net Profit margins	9.5	9.7	10.4	11.1

Growth ratios (%)

Year to March	FY17	FY18	FY19E	FY20E
Revenues	26.3	19.0	18.9	19.6
EBITDA	30.9	17.1	22.9	23.9
PBT	33.0	17.8	27.3	28.0
Adjusted Profit	35.2	21.8	27.5	28.0
EPS	27.0	21.8	27.5	28.0

Balance sheet		(INR mn)			
As on 31st March	FY17	FY18	FY19E	FY20E	
Share capital	140	140	140	140	
Reserves & Surplus	5,103	6,409	7,758	9,491	
Shareholders' funds	5,242	6,549	7,898	9,631	
Long term borrowings	1,927	1,076	263	263	
Short term borrowings	1,368	1,742	1,488	1,488	
Total Borrowings	3,295	2,818	1,750	1,750	
Def. Tax Liability (net)	659	521	521	521	
Sources of funds	9,196	9,888	10,170	11,903	
Gross Block	5,488	5,697	6,197	6,697	
Net Block	4,246	4,083	4,098	4,093	
Capital work in progress	24	33	33	33	
Intangible Assets	1,318	1,358	1,358	1,358	
Total Fixed Assets	5,589	5,473	5,488	5,483	
Cash and Equivalents	431	1,605	1,520	2,728	
Inventories	2,018	2,365	2,284	2,730	
Sundry Debtors	2,442	2,890	2,796	3,343	
Loans & Advances	46	48	466	557	
Other Current Assets	826	637	451	451	
Current Assets (ex cash)	5,332	5,940	5,997	7,082	
Trade payable	1,053	1,824	1,491	1,783	
Other Current Liab	1,103	1,306	1,344	1,607	
Total Current Liab	2,156	3,131	2,836	3,390	
Net Curr Assets-ex cash	3,177	2,809	3,161	3,691	
Uses of funds	9,196	9,888	10,170	11,903	
BVPS (INR)	37.5	46.8	56.5	68.9	

Free cash flow		(INR mn)			
Year to March	FY17	FY18	FY19E	FY20E	
Reported Profit	1,137	1,385	1,765	2,259	
Add: Depreciation	274	372	485	505	
Interest (Net of Tax)	202	194	172	172	
Others	(98)	(135)	(212)	(226)	
Less: Changes in WC	643	(367)	352	530	
Operating cash flow	872	2,184	1,858	2,180	
Less: Capex	2,382	257	500	500	
Free Cash Flow	(1,510)	1,927	1,358	1,680	

Peer comparison valuation

Name	Market cap (USD mn)	Diluted P/E (X)		EV / EBITDA (X)		ROAE (%)	
		FY19E	FY20E	FY19E	FY20E	FY19E	FY20E
Suprajit Engineering	552	21.1	16.5	12.9	10.1	24.4	25.8
Amara Raja Batteries	1,990	24.0	19.4	12.3	10.2	17.5	18.6
Exide Industries	3,255	25.6	21.7	14.0	12.0	14.7	15.4
Motherson Sumi Systems	9,670	26.2	20.7	10.7	8.5	25.2	27.0
Median	-	24.8	20.0	12.6	10.1	21.0	22.2
AVERAGE	-	24.2	19.6	12.5	10.2	20.5	21.7

Source: Edelweiss research

Cash flow metrics

Year to March	FY17	FY18	FY19E	FY20E
Operating cash flow	872	2,184	1,858	2,180
Financing cash flow	258	(1,054)	(1,723)	(765)
Investing cash flow	(919)	(1,123)	(370)	(356)
Net cash Flow	212	6	(235)	1,058
Capex	(2,382)	(257)	(500)	(500)
Dividend paid	169	306	416	526

Profitability and efficiency ratios

Year to March	FY17	FY18	FY19E	FY20E
ROACE (%)	24.1	24.6	28.4	32.2
ROAE (%)	22.2	23.5	24.4	25.8
Inventory Days	84	85	77	70
Debtors Days	69	68	61	55
Payable Days	53	66	64	53
Cash Conversion Cycle	100	88	74	71
Current Ratio	2.7	2.4	2.7	2.9
Gross Debt/EBITDA	1.6	1.2	0.6	0.5
Gross Debt/Equity	0.6	0.4	0.2	0.2
Adjusted Debt/Equity	0.6	0.4	0.2	0.2
Net Debt/Equity	0.5	0.2	-	(0.1)
Interest Coverage Ratio	6.0	7.4	10.1	12.9

Operating ratios

Year to March	FY17	FY18	FY19E	FY20E
Total Asset Turnover	1.4	1.5	1.7	1.8
Fixed Asset Turnover	2.7	2.6	3.1	3.7
Equity Turnover	2.3	2.4	2.4	2.3

Valuation parameters

Year to March	FY17	FY18	FY19E	FY20E
Adj. Diluted EPS (INR)	8.1	9.9	12.6	16.1
Y-o-Y growth (%)	27.0	21.8	27.5	28.0
Adjusted Cash EPS (INR)	10.1	12.6	16.1	19.8
Diluted P/E (x)	32.8	26.9	21.1	16.5
P/B (x)	7.1	5.7	4.7	3.9
EV / Sales (x)	3.5	2.8	2.3	1.9
EV / EBITDA (x)	19.9	16.3	12.9	10.1
Dividend Yield (%)	0.4	0.7	1.0	1.2

Additional Data

Directors Data

Mr K Ajith Kumar Rai	Chairman & MD	Mr Diwakar S Shetty	Non-Executive Independent Director
Mr Ian Williamson	Non-Executive Independent Director	Mr B S Patil	Non-Executive Independent Director
Mr M Jayarama Shetty	Non-Executive Independent Director	Mohan Srinivasan Nagamangala	Executive Director
Suresh Shetty	Non-Executive Independent Director	Supriya Rai	Non-Executive Director

Auditors - S.R. Batliboi & Associates LLP

**as per last available data*

Holding – Top10

	Perc. Holding		Perc. Holding
Rai k ajith kumar	31.65	Rai supriya a	10.26
Sundaram clayton ltd	4.13	Dsp blackrock invest	2.82
Tvs motor company lt	2.07	Punja shobita	1.47
Bajaj allianz life i	1.47	Rai kula ramaprasad	1.29
Malabar india fund l	1.25	Mondrian em mrk sm c	1.07

**as per last available data*

Bulk Deals

Data	Acquired / Seller	B/S	Qty Traded	Price
21 Jun 2017	Smallcapworld Fund Inc	Buy	760000	326.00
16 Jun 2017	Smallcapworld Fund Inc	Buy	1122289	297.00

**as per last available data*

Insider Trades

Reporting Data	Acquired / Seller	B/S	Qty Traded
19 Jun 2017	Vanijya Investment & Trading	Sell	112000.00
19 Jun 2017	Emerging Securities Pvt Ltd	Buy	71847.00
19 Jun 2017	Vanijya Investment & Trading	Buy	112000.00

**as per last available data*

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Coverage group(s) of stocks by primary analyst(s): Automobiles

Ashok Leyland, Amara Raja Batteries, Bajaj Auto, Ceat Ltd, Eicher Motors, Exide Industries, Hero MotoCorp, Minda Corporation, Mahindra & Mahindra Ltd, Maruti Suzuki India Ltd, Motherson Sumi Systems, Suprajit Engineering, Tata Motors Ltd

Recent Research

Date	Company	Title	Price (INR)	Recos
06-Jun-18	Tata Motors	The awakening; <i>Event Update</i>	296	Hold
31-May-18	Suprajit Engineering	Weak quarter; outlook remains strong; <i>Result Update</i>	279	Buy
29-May-18	Minda Corporation	Muted performance; upbeat guidance; <i>Result Update</i>	184	Buy

Distribution of Ratings / Market Cap

Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution*	161	67	11	240

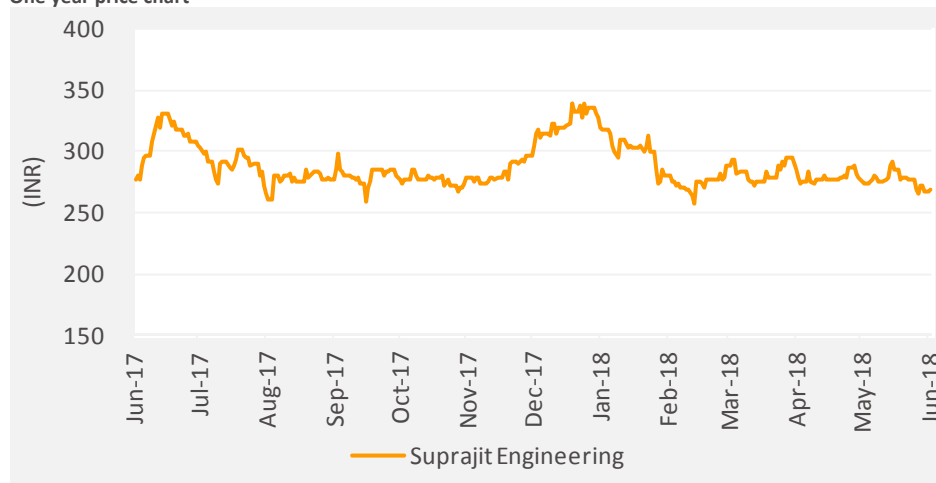
* 1stocks under review

	> 50bn	Between 10bn and 50 bn	< 10bn
Market Cap (INR)	156	62	11

Rating Interpretation

Rating	Expected to
Buy	appreciate more than 15% over a 12-month period
Hold	appreciate up to 15% over a 12-month period
Reduce	depreciate more than 5% over a 12-month period

One year price chart



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