

## Growth momentum on track although weak exports impact quarterly performance

Suprajit Engineering (SEL) reported 2QFY17 consol. PAT of ₹ 352mn (+76% YoY), largely driven by higher other income with its EBITDA margin at 16.6% (+110 bps YoY). Consol. net revenues at ₹2.8bn (+7%YoY) was 9% below JMFe due to lower than expected exports at Phoenix lamps (PLL). The recently acquired Wescon controls' revenue momentum is on track to reach \$40mn revenues in FY17. At PLL, the new H7 line would go into commercial production from Q4FY17 and would give a leg-up to exports. In the cable business, SEL expects revenue growth to be led by: a) domestic demand recovery, b) ramp up in supplies to Honda 2W, c) improving momentum in exports and d) increasing traction in the PV/non-auto verticals. Led by leadership consolidation in the cable business, improving PLL performance and Wescon controls, we estimate consol. EPS to witness a CAGR of 24% over FY16-18E. We reiterate BUY with TP of ₹215. Below-expected margin improvement at PLL, prolonged impact of demonetization on 2w/PV demand and sharp contraction in exports are key risks to our call.

- 2QFY17—Weak exports at PLL impacts EBITDA while margin remains healthy:** SEL reported 2QFY17 reported adj. consol. PAT of ₹ 352mn (+76% YoY), largely driven by higher other income (₹185mn vs 15mn JMFe) and reasonable operational performance. Higher other income was due to capital gains of ₹ 147mn on sale of mutual funds. Adj. EBITDA for the quarter stood at ₹468mn (+15%YoY). EBITDA margin stood at 16.6% (110 bps YoY), in-line JMFe. Consol. topline at ₹2.8bn (7%YoY, 11%QoQ) was 9% below JMFe primarily due to lower than expected exports at Phoenix lamps (PLL) while standalone revenues (₹1.7bn) was in-line. Standalone adj. PAT stood at ₹267mn (+93%YoY) largely driven by higher other income while EBITDA margin at 17.5% was 50 bps below estimates due to higher RM costs.
- Healthy outlook and other business updates:** During the conference call, the management highlighted that PLL's revenues were subdued due to weak exports and the same would improve going forward. Most of the investments on the H7 line were completed and commercial production would commence from Q4FY17. Wescon controls is on a healthy footing with annual revenues at \$40mn rate and EBITDA margin in the 16-18% range. SEL has secured new businesses from BMW, VW and Renault and would commence execution soon. HMSI penetration for the Gujarat plant is currently in excess of 40% and would reach 50% by the end of FY17E.
- Maintain BUY:** We estimate SEL's earnings to increase at a CAGR of 24% over FY16-18E, driven by a healthy revenue CAGR of 34% and stable margin. We maintain BUY with TP of ₹215 (20x average of FY18E and FY19E EPS)

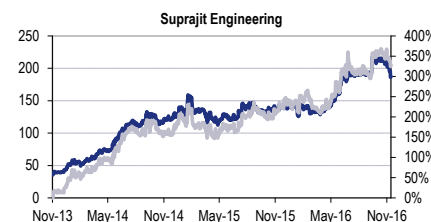
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### Key data

|                          |                   |
|--------------------------|-------------------|
| Market cap (bn)          | ₹ 24.6 / US\$ 0.4 |
| Shares in issue (mn)     | 131.3             |
| Diluted share (mn)       | 131.3             |
| 3-mon avg daily val (mn) | ₹ 16.7/US\$ 0.2   |
| 52-week range            | ₹ 238.0/120.0     |
| Sensex/Nifty             | 26,299/8,112      |
| ₹/US\$                   | 67.8              |

### Daily performance



| %         | 1M    | 3M   | 12M  |
|-----------|-------|------|------|
| Absolute  | -13.1 | -6.0 | 30.0 |
| Relative* | -8.2  | 0.3  | 27.9 |

\* To the BSE Sensex

### Shareholding pattern (%)

|                 | Jun-16 | Mar-16 |
|-----------------|--------|--------|
| Promoters       | 47.4   | 47.4   |
| FII             | 7.5    | 5.9    |
| DII             | 6.3    | 8.4    |
| Public / others | 38.8   | 38.4   |

JM Financial Research is also available on: Bloomberg - JMFR <GO>, Thomson Publisher & Reuters, S&P Capital IQ and FactSet.

Please see Appendix I at the end of this report for Important Disclosures and Disclaimers and Research Analyst Certification.

### Exhibit 1: Financial summary

(₹ mn)

| Y/E March            | FY15A | FY16A | FY17E  | FY18E  | FY19E  |
|----------------------|-------|-------|--------|--------|--------|
| Net sales            | 6,118 | 9,525 | 13,409 | 17,337 | 19,911 |
| Sales growth (%)     | 12.2  | 55.7  | 40.8   | 29.3   | 14.8   |
| EBITDA               | 961   | 1,593 | 2,143  | 2,785  | 3,178  |
| EBITDA (%)           | 15.7  | 16.7  | 16.0   | 16.1   | 16.0   |
| Adjusted net profit  | 503   | 835   | 1,055  | 1,291  | 1,559  |
| EPS (₹)              | 4.2   | 6.4   | 8.0    | 9.8    | 11.9   |
| EPS growth (%)       | -1.0  | 51.8  | 26.3   | 22.4   | 20.7   |
| ROIC (%)             | 16.6  | 18.4  | 16.2   | 16.5   | 17.4   |
| ROE (%)              | 22.6  | 24.3  | 21.5   | 21.9   | 22.1   |
| PE (x)               | 44.6  | 29.4  | 23.3   | 19.0   | 15.8   |
| Price/Book value (x) | 9.3   | 5.5   | 4.6    | 3.8    | 3.2    |
| EV/EBITDA (x)        | 23.9  | 16.0  | 13.2   | 10.0   | 8.7    |

Source: Company data, JM Financial. Note: Valuations as of 16/11/2016

## Exhibit 2. Quarterly financial results (consolidated)

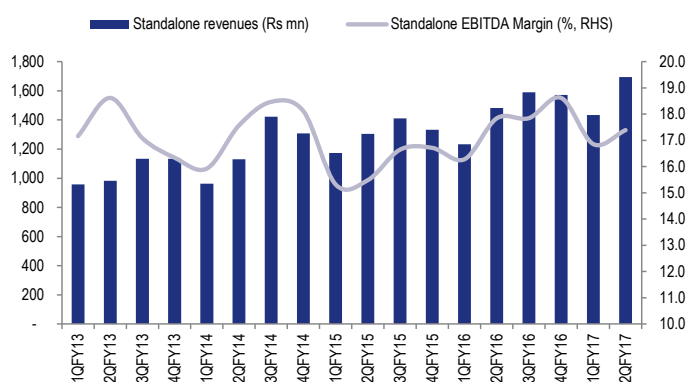
(₹ mn)

|                | 2QFY17 | 2QFY16 | % YoY   | 1QFY17 | % QoQ   | 2QFY17E | % A/E  |
|----------------|--------|--------|---------|--------|---------|---------|--------|
| Sales          | 2,816  | 2,624  | 7.3     | 2,544  | 10.7    | 3,096   | -9.0   |
| Expenditure    | 2,348  | 2,217  | 5.9     | 2,134  | 10.0    | 2,575   | -8.8   |
| EBITDA         | 468    | 408    | 14.8    | 410    | 14.2    | 520     | -10.0  |
| EBITDA margin  | 16.6   | 15.5   | 109bps  | 16.1   | 51bps   | 16.8    | -19bps |
| Other income   | 185    | 19     | 854.9   | 15     | 1094.7  | 15      | 1131.5 |
| Interest       | 69     | 63     | 9.1     | 61     | 13.5    | 60      | 14.8   |
| Depreciation   | 53     | 48     | 10.8    | 40     | 33.1    | 46      | 14.5   |
| PBT            | 531    | 316    | 68.0    | 325    | 63.4    | 429     | 23.8   |
| Tax            | 154    | 101    | 53.1    | 102    | 50.8    | 129     | 20.0   |
| Tax rate (%)   | 29.1   | 31.9   | -283bps | 31.5   | -243bps | 30.0    | -92bps |
| PAT (Adjusted) | 352    | 201    | 75.7    | 197    | 78.9    | 272     | 29.5   |
| PAT margin     | 12.5   | 7.6    | 487bps  | 7.7    | 477bps  | 8.8     | 372bps |

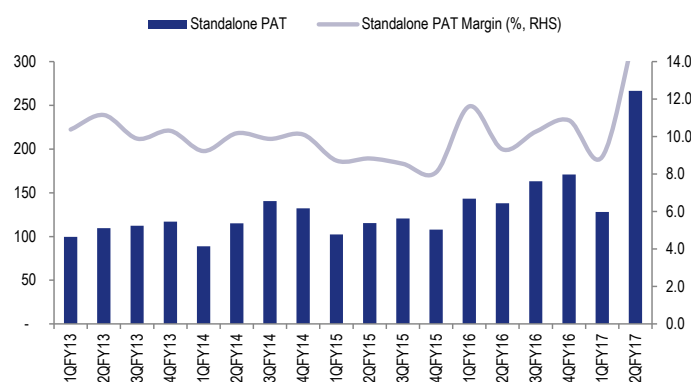
Source: Company, JM Financial. \*includes one-off gain of ₹ 147mn on sale of mutual funds

## Exhibit 4. Standalone financial trends

## Revenue and EBITDA margin



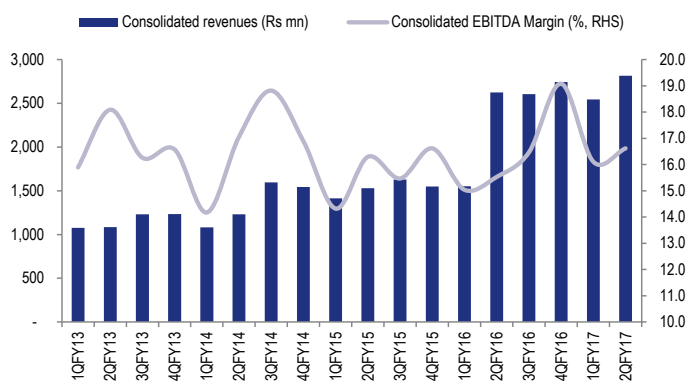
## PAT and PAT margin



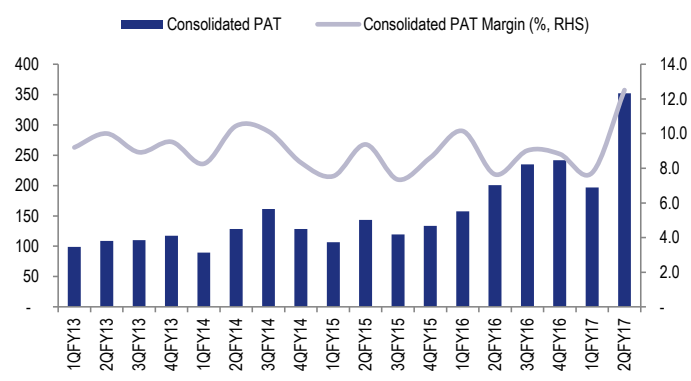
Source: Company, JM Financial

## Exhibit 5. Consolidated financial trends

## Revenue and EBITDA margin



## PAT and PAT margin



Source: Company, JM Financial

## Company background

SEL, a company promoted by K Ajith Kumar Rai in 1985, is the largest manufacturer of automotive cables in India. It is a market leader in automotive control cables in India, the world's largest mechanical cable manufacturer, and among the top-5 in auto cables globally.

With the most competitive manufacturing in India and its technical and logistical supports worldwide, the group provides optimal product development and manufacturing solutions to its domestic and international customers.

SEL acquired Phoenix Lamps Ltd, which is the largest automotive halogen lamp manufacturer in India and has proposed merger with SEL. The company recently acquired Wescon Controls in North America, a leader in off the road cables segment.

| Revenue variables    |              |              |               |               |               |
|----------------------|--------------|--------------|---------------|---------------|---------------|
| Y/E March (₹ mn)     | FY15A        | FY16A        | FY17E         | FY18E         | FY19E         |
| Standalone revenue   | 5,222        | 5,879        | 7,186         | 8,573         | 10,294        |
| Subsidiary revenues  | 896          | 3,646        | 6,223         | 8,765         | 9,617         |
| <b>Total revenue</b> | <b>6,118</b> | <b>9,525</b> | <b>13,409</b> | <b>17,337</b> | <b>19,911</b> |

Source: Company, JM Financial

## Investment rationale

- SEL started as a supplier to a single company (TVS Motor), and now dominates the domestic 2W cable market with c.55% market share. It is the largest supplier of mechanical cables to Bajaj Auto, TVS Motor and Hero Motocorp, while ramping up supplies to Honda 2W (HMSI). Given the dominant position of the company in the domestic 2W cable segment, we believe it is well placed to leverage the medium-long term growth opportunity in the domestic 2W industry.
- While SEL continues to consolidate its position in the 2W segment, it has built significant presence in other segments as well. In the non-auto segment as well, it has gained significant traction in recent years. Consequently, 2W which once accounted for almost 100% of revenues, today accounts for c.52% of standalone revenues.
- The company has embarked on a well-timed capacity expansion, with targeted capacity of c.225mn cables by Mar'17. While a part of this capacity will be dedicated to existing clients, it will help the company leverage the expected recovery in domestic automotive demand.
- Acquisition of Phoenix Lamps would help SEL reduce its exposure to mechanical cables. Furthermore, given Phoenix's strong traction in export markets, it would also help the company penetrate new markets and clients.
- The recent acquisition of Wescon controls would help SEL: a) sectorally de-risk revenues (more into non-Auto), b) diversify geographically, c) add new customers and consolidate relationship/business with existing customers and d) cross-sell products

## Key risks

- Below-expected margin improvement at PLL, prolonged impact of demonetization on 2w/PV demand and sharp contraction in exports

## Financial tables (consolidated)

| Profit & loss              |            |              |              |              |              | (₹ mn) |
|----------------------------|------------|--------------|--------------|--------------|--------------|--------|
| Y/E March                  | FY15A      | FY16A        | FY17E        | FY18E        | FY19E        |        |
| Net sales (Net of excise)  | 6,118      | 9,525        | 13,409       | 17,337       | 19,911       |        |
| Growth (%)                 | 12.2       | 55.7         | 40.8         | 29.3         | 14.8         |        |
| Other operational income   | 0          | 0            | 0            | 0            | 0            |        |
| Raw material (or COGS)     | 3,729      | 5,635        | 7,914        | 10,277       | 11,919       |        |
| Personnel cost             | 826        | 1,253        | 1,753        | 2,192        | 2,473        |        |
| Other expenses (or SG&A)   | 603        | 1,043        | 1,599        | 2,083        | 2,341        |        |
| <b>EBITDA</b>              | <b>961</b> | <b>1,593</b> | <b>2,143</b> | <b>2,785</b> | <b>3,178</b> |        |
| EBITDA (%)                 | 15.7       | 16.7         | 16.0         | 16.1         | 16.0         |        |
| Growth (%)                 | 3.9        | 65.9         | 34.5         | 30.0         | 14.1         |        |
| Other non-op. income       | 41         | 155          | 205          | 45           | 48           |        |
| Depreciation and amort.    | 90         | 158          | 264          | 282          | 302          |        |
| EBIT                       | 911        | 1,591        | 2,084        | 2,548        | 2,924        |        |
| Add: Net interest income   | -164       | -241         | -361         | -425         | -376         |        |
| Pre tax profit             | 747        | 1,350        | 1,723        | 2,124        | 2,547        |        |
| Taxes                      | 245        | 431          | 551          | 680          | 815          |        |
| Add: Extraordinary items   | 0          | -116         | 0            | 0            | 1            |        |
| Less: Minority interest    | 0          | 84           | 117          | 153          | 174          |        |
| Reported net profit        | 503        | 719          | 1,055        | 1,291        | 1,559        |        |
| <b>Adjusted net profit</b> | <b>503</b> | <b>835</b>   | <b>1,055</b> | <b>1,291</b> | <b>1,559</b> |        |
| Margin (%)                 | 8.2        | 8.8          | 7.9          | 7.4          | 7.8          |        |
| Diluted share cap. (mn)    | 120        | 131          | 131          | 131          | 131          |        |
| <b>Diluted EPS (₹)</b>     | <b>4.2</b> | <b>6.4</b>   | <b>8.0</b>   | <b>9.8</b>   | <b>11.9</b>  |        |
| Growth (%)                 | -1.0       | 51.8         | 26.3         | 22.4         | 20.7         |        |
| Total Dividend + Tax       | 135        | 157          | 180          | 225          | 271          |        |

Source: Company, JM Financial

| Balance sheet               |              |              |              |               |               | (₹ mn) |
|-----------------------------|--------------|--------------|--------------|---------------|---------------|--------|
| Y/E March                   | FY15A        | FY16A        | FY17E        | FY18E         | FY19E         |        |
| Share capital               | 120          | 131          | 131          | 131           | 131           |        |
| Other capital               | 0            | 0            | 0            | 0             | 0             |        |
| Reserves and surplus        | 2,288        | 4,344        | 5,219        | 6,285         | 7,572         |        |
| Networth                    | 2,408        | 4,476        | 5,350        | 6,416         | 7,703         |        |
| Total loans                 | 1,660        | 2,586        | 3,956        | 3,756         | 3,356         |        |
| Minority interest           | 0            | 542          | 591          | 591           | 591           |        |
| <b>Sources of funds</b>     | <b>4,068</b> | <b>7,604</b> | <b>9,897</b> | <b>10,763</b> | <b>11,650</b> |        |
| Intangible assets           | 0            | 1,066        | 2,950        | 2,950         | 2,950         |        |
| Fixed assets                | 2,492        | 4,662        | 5,882        | 6,382         | 6,832         |        |
| Less: Deprn. and amort.     | 812          | 2,425        | 3,089        | 3,371         | 3,673         |        |
| Net block                   | 1,680        | 3,303        | 5,743        | 5,961         | 6,109         |        |
| Capital WIP                 | 170          | 178          | 300          | 300           | 200           |        |
| Investments                 | 1,118        | 1,487        | 217          | 217           | 217           |        |
| Def tax assets/- liability  | -91          | -86          | -93          | -93           | -93           |        |
| Current assets              | 2,305        | 4,582        | 6,034        | 7,143         | 8,329         |        |
| Inventories                 | 799          | 1,669        | 2,278        | 2,422         | 2,728         |        |
| Sundry debtors              | 1,250        | 2,096        | 2,939        | 3,800         | 4,582         |        |
| Cash & bank balances        | 56           | 189          | 126          | 161           | 183           |        |
| Other current assets        | 0            | 0            | 0            | 0             | 0             |        |
| Loans & advances            | 200          | 628          | 691          | 760           | 836           |        |
| Current liabilities & prov. | 1,128        | 1,870        | 2,314        | 2,776         | 3,123         |        |
| Current liabilities         | 994          | 1,640        | 2,047        | 2,486         | 2,806         |        |
| Provisions and others       | 134          | 229          | 267          | 290           | 317           |        |
| Net current assets          | 1,178        | 2,712        | 3,720        | 4,367         | 5,207         |        |
| Others (net)                | 13           | 10           | 10           | 10            | 10            |        |
| <b>Application of funds</b> | <b>4,068</b> | <b>7,604</b> | <b>9,897</b> | <b>10,763</b> | <b>11,650</b> |        |

Source: Company, JM Financial

| Cashflow statement              |             |               |               |             |              | (₹ mn) |
|---------------------------------|-------------|---------------|---------------|-------------|--------------|--------|
| Y/E March                       | FY15A       | FY16A         | FY17E         | FY18E       | FY19E        |        |
| Reported net profit             | 503         | 719           | 1,055         | 1,291       | 1,559        |        |
| Depreciation and amort.         | 92          | 1,613         | 664           | 282         | 302          |        |
| -Inc/dec in working cap.        | -107        | -1,340        | -1,095        | -617        | -817         |        |
| Others                          | 0           | 542           | 49            | 0           | 0            |        |
| <b>Cash from operations (a)</b> | <b>488</b>  | <b>1,534</b>  | <b>673</b>    | <b>956</b>  | <b>1,044</b> |        |
| -Inc/dec in investments         | -369        | -370          | 1,270         | 0           | 0            |        |
| Capex                           | -411        | -3,244        | -3,226        | -500        | -350         |        |
| Others                          | 169         | -61           | 24            | 5           | 0            |        |
| <b>Cash flow from inv. (b)</b>  | <b>-610</b> | <b>-3,675</b> | <b>-1,931</b> | <b>-495</b> | <b>-350</b>  |        |
| Inc/-dec in capital             | -7          | 1,505         | 0             | 0           | -1           |        |
| Dividend+Tax thereon            | -135        | -157          | -180          | -225        | -271         |        |
| Inc/-dec in loans               | 238         | 927           | 1,370         | -200        | -400         |        |
| Others                          | 6           | -1            | 7             | 0           | 0            |        |
| <b>Financial cash flow (c)</b>  | <b>103</b>  | <b>2,274</b>  | <b>1,196</b>  | <b>-425</b> | <b>-672</b>  |        |
| Inc/-dec in cash (a+b+c)        | -20         | 133           | -63           | 35          | 23           |        |
| Opening cash balance            | 76          | 56            | 189           | 126         | 161          |        |
| Closing cash balance            | 56          | 189           | 126           | 161         | 183          |        |

Source: Company, JM Financial

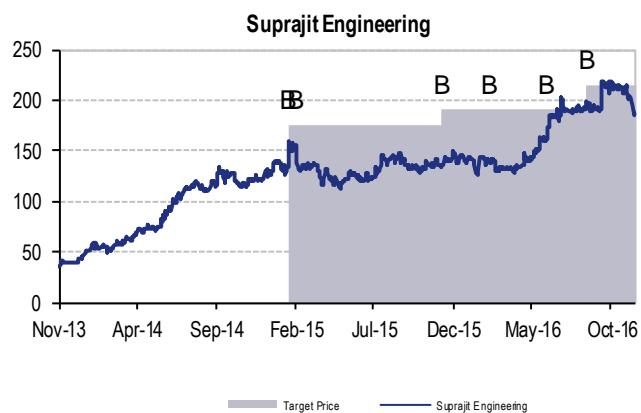
| Key ratios                   |       |       |       |       |       |
|------------------------------|-------|-------|-------|-------|-------|
| Y/E March                    | FY15A | FY16A | FY17E | FY18E | FY19E |
| BV/Share (₹)                 | 20.1  | 34.1  | 40.7  | 48.9  | 58.7  |
| ROCE (%)                     | 16.6  | 18.4  | 16.2  | 16.5  | 17.4  |
| ROE (%)                      | 22.6  | 24.3  | 21.5  | 21.9  | 22.1  |
| Net Debt/equity ratio (x)    | 0.2   | 0.2   | 0.7   | 0.5   | 0.4   |
| <b>Valuation ratios (x)</b>  |       |       |       |       |       |
| PER                          | 44.6  | 29.4  | 23.3  | 19.0  | 15.8  |
| PBV                          | 9.3   | 5.5   | 4.6   | 3.8   | 3.2   |
| EV/EBITDA                    | 23.9  | 16.0  | 13.2  | 10.0  | 8.7   |
| EV/Sales                     | 3.7   | 2.7   | 2.1   | 1.6   | 1.4   |
| <b>Turnover ratios (no.)</b> |       |       |       |       |       |
| Debtor days                  | 75    | 80    | 80    | 80    | 84    |
| Inventory days               | 48    | 64    | 62    | 51    | 50    |
| Creditor days                | 56    | 61    | 60    | 60    | 60    |

Source: Company, JM Financial

## History of earnings estimates and target price

| Date      | FY17E<br>EPS (Rs) | % Chg. | FY18E<br>EPS (Rs) | % Chg. | Target<br>Price | % Chg. |
|-----------|-------------------|--------|-------------------|--------|-----------------|--------|
| 20-Jan-15 | 8.8               |        |                   |        | 175             |        |
| 4-Feb-15  | 8.7               | -1.1   |                   |        | 175             | 0.0    |
| 12-Nov-15 | 7.8               | -10.3  | 11.0              |        | 190             | 8.6    |
| 11-Feb-16 | 7.9               | 1.3    | 10.5              | -4.5   | 190             | 0.0    |
| 31-May-16 | 7.6               | -3.8   | 9.4               | -10.5  | 190             | 0.0    |
| 17-Aug-16 | 7.6               | 0.0    | 9.7               | 3.2    | 215             | 13.2   |

## Recommendation history



## APPENDIX I

## JM Financial Institutional Securities Limited

Corporate Identity Number: U65192MH1995PLC092522

Member of BSE Ltd. and National Stock Exchange of India Ltd. and Metropolitan Stock Exchange of India Ltd.

SEBI Registration Nos.: BSE - INZ010012532, NSE - INZ230012536 and MSEI - INZ260012539, Research Analyst - INH000000610

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|-----------------------|--|
| Rating                | Meaning  |
| Buy                   | Total expected returns of more than 15%. Total expected return includes dividend yields.         |
| Hold                  | Price expected to move in the range of 10% downside to 15% upside from the current market price. |
| Sell                  | Price expected to move downwards by more than 10%  |

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