

# SUPRAJIT ENGINEERING

## RESULT UPDATE

### KEY DATA

<b>Rating</b>	<b>HOLD</b>
Sector relative	Neutral
Price (INR)	364
12 month price target (INR)	378
Market cap (INR bn/USD bn)	50/0.7
Free float/Foreign ownership (%)	55.4/2.9
<b>What's Changed</b>	
Target Price	↑
Rating/Risk Rating	—

### QUICK TAKE

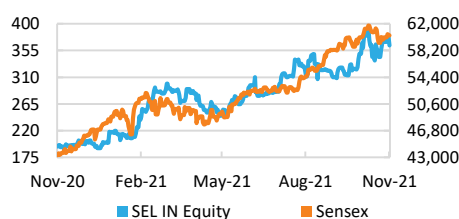
	Above	In line	Below
Profit	●		
Margins	●		
Revenue Growth	●		
Overall	●		

### FINANCIALS

(INR mn)

Year to March	FY21A	FY22E	FY23E	FY24E
Revenue	16,409	19,433	22,442	25,034
EBITDA	2,367	3,073	3,691	4,087
Adjusted profit	1,427	1,935	2,402	2,759
Diluted EPS (INR)	10.2	13.8	17.2	19.7
EPS growth (%)	12.8	35.6	24.1	14.9
RoAE (%)	15.5	18.1	19.2	18.8
P/E (x)	35.7	26.3	21.2	18.5
EV/EBITDA (x)	20.8	15.5	12.5	10.8
Dividend yield (%)	0.5	0.6	0.7	0.8

### PRICE PERFORMANCE



#### Explore:



Financial model



Podcast



Corporate access



Video

## Strong showing

Suprajit Engineering (SEL) reported Q2FY22 EBITDA of INR801mn beating our estimate by 22% due to a strong revenue performance. Acceptance of price hike for earlier quarters by OEMs (~2% of revenue in our assessment) also aided the performance. SEL continues to win business, including for EVs (from traditional OEMs). However, its cables business is engine-agnostic—there is no disruption risk.

Strong traction exists in Wescon, EU exports and bulbs. And the new R&D centre would further boost its capability to diversify product offerings. While we like the business, the stock's current valuation factors in most of the positives. Retain 'HOLD'. Key trigger: more information on the recent [LDC business acquisition](#) from Kongsberg.

### Strong showing, compensates for a weak Q1

SEL's Q2FY22 consolidated revenue of INR4.9bn (up 37% QoQ is ~11% above our estimate. It is a strong showing across businesses as supply chain issues improved QoQ. Gross margin of 42.6% was down 210bps QoQ due to commodity pressure (lag effect in passing on), despite acceptance of price hikes by OEM for earlier quarters. EBITDA of INR801mn (margin of 16.2%) was 22% above our estimate, largely due to realisation of price hikes for earlier periods (~2% in our assessment). Quarterly margin volatility continues across most businesses due to cost pressure, supply chain disruption and lag in passing through cost pressure.

### Profitable market share to drive growth

We like SEL's focus on gaining profitable market share in each of its businesses. Using its low-cost operations as well as value-oriented product proposition, the company continues to deepen penetration among existing customers even as order-wins (typically more profitable) sustain. Besides, as volumes kick in, we expect management efforts on cost-saving activities to be amplified, and provide a further margin boost. Higher raw material costs and INR appreciation versus USD may affect performance. Near-term showing will be also affected by ongoing semiconductor shortages.

### Outlook and valuation: Positives priced in; retain 'HOLD'

Despite near-term weakness, the franchise, in our view, remains robust and well placed to leverage revival. Our 'HOLD' largely reflects high expectations rather than weakness in business fundamentals. The stock is trading at a FY22/23E PE of 26.3x/21.2x.

### Financials

Year to March	Q2FY22	Q2FY21	% Change	Q1FY22	% Change
Net Revenue	4,937	4,431	11.4	3,616	36.5
EBITDA	801	735	8.9	492	62.6
Adjusted Profit	585	481	21.7	109	435.6
Diluted EPS (INR)	4.2	3.4	23.0	0.8	435.6

## Financial Statements

### Income Statement (INR mn)

Year to March	FY21A	FY22E	FY23E	FY24E
Total operating income	16,409	19,433	22,442	25,034
Gross profit	6,861	7,899	9,337	10,419
Employee costs	3,083	3,386	3,899	4,395
Other expenses	1,411	1,440	1,747	1,937
EBITDA	2,367	3,073	3,691	4,087
Depreciation	568	609	635	661
Less: Interest expense	192	230	230	91
Add: Other income	336	352	384	353
Profit before tax	1,943	2,587	3,210	3,687
Prov for tax	516	651	808	928
Less: Other adj	0	0	0	0
Reported profit	1,427	1,935	2,402	2,759
Less: Excp.item (net)	0	0	0	0
Adjusted profit	1,427	1,935	2,402	2,759
Diluted shares o/s	140	140	140	140
Adjusted diluted EPS	10.2	13.8	17.2	19.7
DPS (INR)	1.7	2.3	2.7	3.0
Tax rate (%)	26.6	25.2	25.2	25.2

### Important Ratios (%)

Year to March	FY21A	FY22E	FY23E	FY24E
Gross profit margin (%)	41.8	40.6	41.6	41.6
Staff cost % sales	18.8	17.4	17.4	17.6
Other expenses % sales	8.6	7.4	7.8	7.7
EBITDA margin (%)	14.4	15.8	16.4	16.3
Net profit margin (%)	8.7	10.0	10.7	11.0
Revenue growth (% YoY)	5.0	18.4	15.5	11.5
EBITDA growth (% YoY)	8.2	29.8	20.1	10.7
Adj. profit growth (%)	12.8	35.6	24.1	14.9

### Assumptions (%)

Year to March	FY21A	FY22E	FY23E	FY24E
GDP (YoY %)	(6.0)	7.0	6.0	7.0
Repo rate (%)	3.5	3.5	4.0	5.3
USD/INR (average)	75.0	73.0	72.0	71
4W – dom. vol (% YoY)	(15.0)	18.0	18.0	8.0
2W – dom. vol (% YoY)	(14.0)	15.0	15.0	8.0
Steel prices (INR/t)	40,300.0	40,300.0	40,300.0	NA
Alum. prices (USD/t)	1,880.0	1,880.0	1,880.0	NA

### Valuation Metrics

Year to March	FY21A	FY22E	FY23E	FY24E
Diluted P/E (x)	35.7	26.3	21.2	18.5
Price/BV (x)	5.1	4.4	3.8	3.2
EV/EBITDA (x)	20.8	15.5	12.5	10.8
Dividend yield (%)	0.5	0.6	0.7	0.8

Source: Company and Edelweiss estimates

### Balance Sheet (INR mn)

Year to March	FY21A	FY22E	FY23E	FY24E
Share capital	140	140	140	140
Reserves	9,757	11,377	13,404	15,740
Shareholders funds	9,897	11,516	13,544	15,880
Minority interest	0	0	0	0
Borrowings	2,887	1,944	1,944	1,944
Trade payables	2,476	1,704	1,967	2,195
Other liabs & prov	1,873	2,219	2,477	2,699
Total liabilities	17,133	17,383	19,932	22,718
Net block	4,624	4,516	4,581	4,620
Intangible assets	1,357	1,357	1,357	1,357
Capital WIP	49	49	49	49
Total fixed assets	6,031	5,922	5,987	6,026
Non current inv	0	0	0	0
Cash/cash equivalent	3,966	4,734	6,238	8,140
Sundry debtors	3,320	3,194	3,689	4,115
Loans & advances	68	532	615	686
Other assets	3,749	3,000	3,404	3,752
Total assets	17,133	17,383	19,932	22,718

### Free Cash Flow (INR mn)

Year to March	FY21A	FY22E	FY23E	FY24E
Reported profit	1,427	1,935	2,402	2,759
Add: Depreciation	568	609	635	661
Interest (net of tax)	141	172	172	68
Others	(285)	(294)	(327)	(330)
Less: Changes in WC	(684)	(17)	(459)	(395)
Operating cash flow	1,167	2,406	2,424	2,763
Less: Capex	(574)	(500)	(700)	(700)
Free cash flow	593	1,906	1,724	2,063

### Key Ratios

Year to March	FY21A	FY22E	FY23E	FY24E
RoE (%)	15.5	18.1	19.2	18.8
RoCE (%)	14.7	21.5	23.8	22.7
Inventory days	113	91	78	80
Receivable days	68	61	56	57
Payable days	88	66	51	52
Working cap (% sales)	20.4	17.3	17.0	16.8
Gross debt/equity (x)	0.3	0.2	0.1	0.1
Net debt/equity (x)	(0.1)	(0.2)	(0.3)	(0.4)
Interest coverage (x)	9.4	12.2	14.9	41.4

### Valuation Drivers

Year to March	FY21A	FY22E	FY23E	FY24E
EPS growth (%)	12.8	35.6	24.1	14.9
RoE (%)	15.5	18.1	19.2	18.8
EBITDA growth (%)	8.2	29.8	20.1	10.7
Payout ratio (%)	17.0	16.3	15.6	15.3

## Q2FY22 conference call: Key highlights

### Key highlights

- Commodity cost headwinds continue. Some of the cost increase are steep and OEM many not be willing to accept the same without resistance
- Festive season sales has been muted in passenger and 2Ws due to chip shortage. Expects chip shortage issue to persist by this end of this FY.
- SEL has been able to pass on commodity headwinds to some customers and working on others
- Suprajit Technical Centre (STC) is showing results - have filed 15 patents
- Capex for next 18 months would be ~INR1.2bn. This will be funded through debt and internal accrual in equal proportion.
- Continues to win new businesses including that for EVs from existing customers

### Domestic Cable

- Narsapura plant will get completed by end of this year. And, SEL can start manufacturing from this plant.
- SEL is consolidating its aftermarket manufacturing facilities into one centralized unit. While doing so there will not be any additional capacity expansion
- There has been margin expansion in Q2 also due to price increase of earlier quarters that has now been accepted by OEM.

### Phoenix lamps

- There has been steep inflation in raw material (ex: Gas prices, crypton glass, etc has gone through the roof) in this division.
- In Indian After markets - where SEL is market leader has passed on prices. Which was followed by other players as well
- Issue is with other label market (OLM), OEMs, tier 1 suppliers and exports. Where SEL is continuously working on. So far, able to increase prices for one OLM.
- Sharp price hike demand in lamps business is little unusual and hence it is taking time for pass through

### Trifa and Luxlite (part of Lamps)

- Continues to be a challenging. A provision for impairment of INR1.27bn towards goodwill made. Goodwill came with the acquisition and not recognised by SEL. All the investment in Trifa has already been written down. In Luxlite small part of goodwill is left to be written down. What is now left is largely cash on books
- The initial strategy was to have a great front end team that can help SEL to build relationship with clients and understand their needs. But, Later SEL realized these are aftermarket businesses and price is the main deciding factor. So, to reduce overhead costs and other expense SEL has reduced team size from 30 to 3-4 people to become competitive.
- Very focussed strategy now – direct exports from India with minimum inventory overseas to manage expenses related to warehouse.
- In the one year time SEL should be able to do final restructuring of this operation.

## SENA

- Volumes have been picked up for this segment
- Reaching out to customers for compensation related to cost increase
- SEL is confident that this business will continue to do well and can deliver margins consistently similar to last year.
- Most of the businesses that SEL is winning are manufactured in India (high margin)
- The revised strategy is working which is evident from 20% growth for Wescon as compared to US industry growth of 3%

## STC

- Aim of this unit is to enhance the value proposition within cable division and develop new technological advanced products.
- Established in 2015, recently it moved into a bigger and dedicated space with its on test manufacturing facility. STC has filed for 15 patents
- STC has multiple products under development. Products such as digital speedometer, Throttle position sensor, Rotary sensor, CBS Mechanisms and speeder gear box with electromechanical clutches are in final stage of commercialization over next twelve months.
- Initial businesses won and orders expected on these products on an annualised basis are in excess of INR1.0bn / year, to start with.

## LDC

- Transaction – EV of USD42mn on no debt and no cash basis. SEL expects LDC to clock USD100mn revenue next year with double digit EBITDA
- This is transformational deal for SEL over next 5 years and makes SEL a global player with presence across 3 continents – Asia, US and EU.
- This transaction will help SEL to win clients as certain clients prefer supply chain to be closer to their home market.
- Many Global clients have asked SEL setup plant in China and Mexico. With this acquisition SEL can serve these clients.
- LDC will give SEL exposure to global platform and engineering talent.
- LDC's one of the key customer is Tesla
- Don't see any change in business as industry move to EVs
- No pension liability related to this acquisition
- LDC has much higher overheads. That SEL can restructure and restructuring can take one year time.
- Current utilization level of LDC is 60-65%.
- For SEL, RoCE of this business is similar to India business, though margins are lower. This is due to lower investments.

## Capex

1. Capex of INR1.25bn spread over 18 months.
2. 3 major parts of it: buildings, plant and machinery and others (Green energy)
3. Buildings - Expenses related to unit expansion in Narsapura and one building for centralized production for after markets .
4. SEL will finance it with 50% debt.

## Exhibit 1: Valuation snapshot

Particulars	Mar2023E
March22E Conso EPS	17.2
Target Multiple	22
Target price	378

Source: Edelweiss Research

## Exhibit 2: Quarterly snapshot

Year to March	Q2FY22	Q2FY21	% change	Q1FY22	% change	FY21	FY22E	FY23E	FY24E
Total income	4,937	4,431	11.4	3,616	36.5	16,409	19,433	22,442	25,034
Raw Material	2,836	2,606	8.8	2,001	41.7	9,547	11,534	13,105	14,615
Staff costs	866	730	18.7	778	11.2	3,083	3,386	3,899	4,395
Other expenses	434	361	20.4	344	26.2	1,411	1,440	1,747	1,937
EBITDA	801	735	8.9	492	62.6	2,367	3,073	3,691	4,087
Depreciation	146	144	1.8	143	2.0	568	609	635	661
EBIT	654	591	10.7	349	87.6	1,800	2,465	3,056	3,426
Less: Interest Expense	35	55	(35.9)	47	(25.2)	192	230	230	91
Add: Other income	152	86	76.6	66	129.7	336	352	384	353
Add: Prior period items									
Exceptional loss (gain)	45	-		(161)		-	-	-	-
Profit Before Tax	771	622	23.9	368	109.7	1,943	2,587	3,210	3,687
Less: Provision for Tax	231	141	63.3	97	137.2	516	651	808	928
Reported Profit	496	481	3.1	432	14.8	1,427	1,935	2,402	2,759
Adjusted Profit	451	481	(6.2)	593	(24.0)	1,427	1,935	2,402	2,759
No. of Diluted shares outstanding (mn)	138	140	(1.1)	138	-	140	140	140	140
Adjusted Diluted EPS	3.26	3.44	(5.2)	4.28	(24.0)	10.20	13.84	17.17	19.73
Diluted PE (x)						33.0	24.4	19.6	17.1
EV/EBITDA (x)						19.46	14.43	11.61	10.02
ROACE (%)						17	21	24	23
As % of revenue									
Raw material	57.4	58.8		55.3		58.2	59.4	58.4	58.4
Staff costs	17.5	16.5		21.5		18.8	17.4	17.4	17.6
Other expenses	8.8	8.1		9.5		8.6	7.4	7.8	7.7
EBIDTA	16.2	16.6		13.6		14.4	15.8	16.4	16.3
Adjusted PAT	10.0	10.8		11.9		8.7	10.0	10.7	11.0
PAT after E/o and Minority	9.1	10.8		16.4		8.7	10.0	10.7	11.0
Tax rate	29.9	22.7		26.4		26.6	25.2	25.2	25.2

Source: Company, Edelweiss Research

## Exhibit 3: Change in estimates

INR mn	FY22E	FY23E	FY24E	Change (%)					
				FY22E	FY23E	FY24E			
Revenue	19,433	22,442	25,034	19,214	22,145	24,701	1.1	1.3	1.3
EBITDA	3,073	3,691	4,087	2,991	3,570	3,952	2.8	3.4	3.4
EBITDA margin	15.8	16.4	16.3	15.6	16.1	16.0			
PAT	1,935	2,402	2,759	1,874	2,312	2,658	3.3	3.9	3.8

Source: Company, Edelweiss Research

## 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 close to 300mn. 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.

While the domestic demand environment remains challenging, SEL is banking on exports and Wescon (post restructuring) to drive growth. We continue to like SEL for its focus on 1) expanding the product offering – drop-in-solution for LED lamps, power sports and agri - machinery cables and expanding into mechanism as an extension to its cables and 2) strong traction in exports among European OEMs as reflected from upward revision in cable capacity expansion.

## Key Risks

**Slowdown in demand:** SEL derives a large portion of its 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:** As proportion of exports increases, we believe the natural currency hedge (in form of imports) may not be effective, exposing the company to currency risks.



## Additional Data

### Management

Chariman	K. Ajith Rai
MD & CEO	Mohan Srinivasan Nagamangala
CFO	Medappa Gowda
Other	
Auditor	E&Y

### Holdings – Top 10\*

	% Holding		% Holding
DSP Invst Manag	3.85	Emerging Securi	1.00
First State	3.54	Mitsubishi UFJ	0.67
TVS Motor	2.07	Dimensional Fun	0.51
Bajaj Allianz	1.35	Caisse de Depot	0.27
Malabar India	1.00	BlackRock	0.08

\*Latest public data

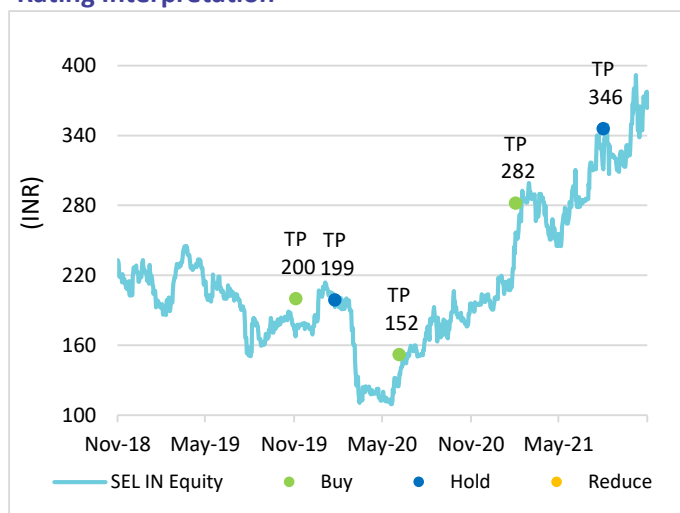
### Recent Company Research

Date	Title	Price	Reco
29-Oct-21	Strategic fit; reasonable valuations; <i>Company Update</i>	338	Hold
11-Aug-21	Solid fundamentals priced in; <i>Result Update</i>	338	Hold
31-May-21	Outperformance sustained; <i>Result Update</i>	267	Buy

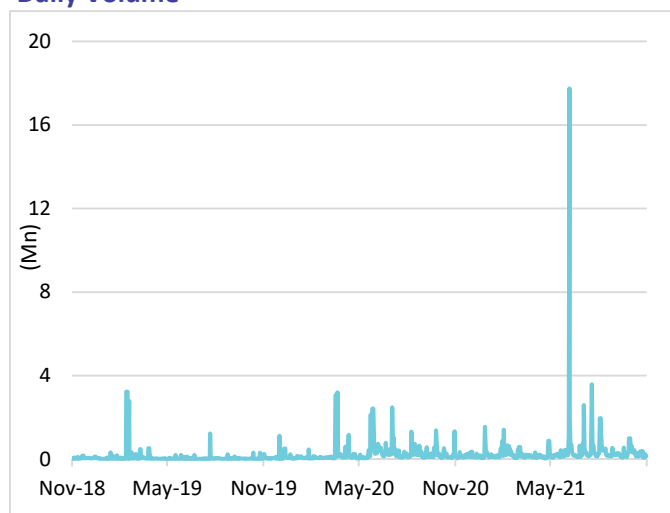
### Recent Sector Research

Date	Name of Co./Sector	Title
02-Nov-21	Minda Corporation	Subdued showing; <i>Result Update</i>
26-Oct-21	CEAT	Results in line; cost pressure to stay; <i>Result Update</i>
08-Oct-21	Motherson Sumi	Breaking into aerospace; <i>Company Update</i>

### Rating Interpretation



### Daily Volume



### Rating Distribution: Edelweiss Research Coverage

	Buy	Hold	Reduce	Total
Rating Distribution*	180	57	17	255
	>50bn	>10bn and <50bn	<10bn	Total
Market Cap (INR)	233	37	3	273

\*1 stocks under review

### Rating Rationale

Rating	Expected absolute returns over 12 months
Buy:	>15%
Hold:	>15% and <-5%
Reduce:	<-5%

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