

Strong auto segment performance continues, Maintain Buy

We maintain our Buy rating on FIEM Industries with TP of Rs1,260. We expect FIEM's growth to continue aided by strong growth prospects of its two biggest clients namely Honda Motorcycle and Scooter India (HMSI) and TVS Motor. Q1FY18 top-line performance was above estimates as auto segment posted strong growth. Had it not been for issues in LED business, the performance would have looked much stronger. Recently FIEM has faced several issues in its LED business, due to an unfavourable business environment. LED business reported a loss at EBIT level on account of sales returns worth Rs82mn, along with declining sales. Despite slightly lower visibility in the LED business, we remain convinced of FIEM's medium-to-long-term growth opportunity as the company continues to remain a strong 2W auto ancillary company. Also, the management is working on several fronts to get the LED business on track which will provide additional growth in the long run.

- **Auto segment supported well:** FIEM's 1QFY18 revenue was up 18.9% YoY primarily due to a strong growth of 27% in automotive segment. LED business dragged down the sales a bit as the revenue from the business was negative on account of sales return of Rs82mn (1.4mn LED bulbs, earlier supplied to EESL). The good growth in automotive segment was mainly attributed to a strong sales growth posted by its key client HMSI who reported 19% volume growth during the quarter. Its other clients like Royal Enfield and Suzuki also posted a strong growth during the quarter.
- **Profitability was under pressure due to LED related issues:** Due to loss in the LED business and higher RM costs, the company posted a margin contraction of 221bps yoy. Subsequently, EBITDA was down by 1.6%. FIEM's 1QFY18 PAT was down 10%, due to additional overhangs such as higher depreciation, higher interest costs and a higher tax rate (34% in Q1FY18 vs 31% in Q1FY17).
- **Auto business outlook is very strong:** If growth of HMSI and TVS Motors in the first two months of 2QFY18 is any indication, FIEM is set to post a strong growth in its auto business in coming quarters as well. Automatic Headlight On (AHO) regulation will also accelerate the adoption of LED in 2W head lamps. The company has also incorporated a wholly owned subsidiary under the name **Fiem (Thai) Design & Technology Co. Ltd.** to strengthen its in-house design and R&D capabilities in automotive lightning. On LED lightening front, FIEM has been taking several steps on the LED exports side which would help in recovery of LED business after a few quarters.
- **Fiem Industries executes a JV with Kyowa:** The company has executed its JV agreement with Kyowa Co. Ltd. and formed a 50:50 JV in Hong Kong by the name of **Fiem Kyowa (HK) Mould Co. Ltd.** The JV would engage primarily in the business of high class molds/ tools for automotive and other applications and we believe that it will have a revenue potential of Rs1,000mn+.
- **Valuation and Risk:** We remain convinced of FIEM's medium-to-long-term growth opportunity. We value FIEM on our differentiated AOCF/EV methodology and arrive at a TP of Rs1,260. Key downside risk: slower-than-expected growth in HMSI and TVS Motor.

Y/E Mar (Rsmn)	1QFY18	1QFY17	YoY (%)	4QFY17	QoQ (%)	1QFY18E	Var (%)
Total Income	2,907	2,445	18.9	2,451	18.6	2,742	6.0
Op. cost	2,599	2,132	21.9	2,212	17.5	2,432	6.9
EBITDA	308	313	(1.6)	239	29.1	310	(0.7)
EBITDA margin (%)	10.6	12.8	(221) bps	9.7	86 bps	11.3	(72) bps
Depreciation	107	94	14.4	102	5.7	113	(5.2)
Interest	60	55	9.9	55	9.7	52	14.8
Other Income	18	1	NM	21	(13.7)	13	40.6
Taxes paid	55	51	8.3	(22)	(353.2)	47	16.7
-effective tax rate	34.8	30.7		(21.1)		30.0	
Reported PAT	103	115	(9.9)	125	(17.2)	110	(6.2)
Adjusted PAT	103	115	(9.9)	30	246.3	110	(6.2)
Adj PAT margin (%)	3.6	4.7	(114) bps	1.2	234 bps	4.0	(46) bps

Source: Company, Centrum Research Estimates

Y/E Mar (Rsmn)	Rev	YoY (%)	EBITDA	EBITDA (%)	Adj PAT	YoY (%)	EPS	RoE (%)	RoCE (%)	P/E (x)	EV/EBITDA (x)
FY15	8,248	14.8	1,024	12.4	423	13.0	32.1	19.9	14.2	18.5	8.8
FY16	9,870	19.7	1,270	12.9	572	35.3	43.5	22.9	16.8	13.4	7.1
FY17	10,174	3.1	1,174	11.5	424	(25.8)	32.2	12.2	10.6	30.3	12.7
FY18E	12,112	19.0	1,465	12.1	591	39.4	44.9	13.3	10.5	20.9	9.6
FY19E	14,901	23.0	1,874	12.6	869	47.0	66.0	17.3	13.6	14.2	7.3

Source: Company, Centrum Research Estimates

Target Price		Rs1,260	Key Data	
CMP*		Rs928	Bloomberg Code	FIEM IN
Upside		34%	Curr Shares O/S (mn)	13.2
Previous Target		Rs1,260	Diluted Shares O/S(mn)	13.2
Previous Rating		Buy	Mkt Cap (Rsbn/USDmn)	12.2/190.5
Price Performance (%)*			52 Wk H / L (Rs)	1510/821.4
	1M	6M	1Yr	
FIEM IN	5.2	2.1	(10.5)	
NIFTY	(1.1)	11.9	13.0	Daily Vol. (3M NSE Avg.) 20102

*as on 5 September 2017; Source: Bloomberg, Centrum Research

Shareholding pattern (%)*

	Jun-17	Mar-17	Dec-16	Sep-16
Promoter	63.6	63.6	63.6	63.6
FIs	15.1	14.5	15.2	15.2
Dom. Inst.	6.9	7.5	8.9	9.0
Public & Others	14.4	14.4	12.3	12.2

Source: BSE, *as on 5 September 2017

Earning Revisions summary

Particulars (Rs in mn)	FY18E			FY19E		
	New	Old	Chg (%)	New	Old	Chg (%)
Sales	12,112	12,262	(1.2)	14,901	14,980	(0.5)
EBITDA	1,465	1,527	(4.1)	1,874	1,937	(3.2)
EBITDA margin (%)	12.1	12.5	(36) bps	12.6	12.9	(32) bps
PAT	591	641	(7.8)	869	910	(4.6)

Source: Centrum Research Estimates

Centrum vs. Bloomberg Consensus*

Particulars (Rs mn)	FY18E			FY19E		
	Centrum	BBG	Var (%)	Centrum	BBG	Var (%)
Sales	12,112	12,158	(0.4)	14,901	14,001	6.4
EBITDA	1,465	1,476	(0.8)	1,874	1,730	8.3
PAT	591	595	(0.6)	869	748	16.2

Bloomberg Consensus*				Centrum Target Price (Rs)	Variance (%)
BUY	SELL	HOLD	Target Price (Rs)		
6	0	1	1,260	1,260	0.0

*as on 5 September 2017; Source: Bloomberg, Centrum Research Estimates

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Valuation and recommendations

We continue to value FIEM on our differentiated AOCF/EV methodology and arrive at a TP of Rs1,260. We ascribe a small premium to historical multiples and specify the key reasons for the same below.

AOCF/EV valuation – 15% premium ascribed to historical AOCF/EV yield

As per our AOCF/EV based valuation, we note that FIEM's five year average AOCF/EV yield stands at 5.9%. We have ascribed a 15% premium to this average to arrive at a target AOCF/EV yield of 5.1%, and hence, the implied EV/AOCF multiple of 19.6x. We use average AOCF over FY15-19E and a 19.6x EV/AOCF multiple to arrive at our target EV and our TP of Rs1,260/share (Exhibit 1).

Exhibit 1: AOCF/EV based valuation

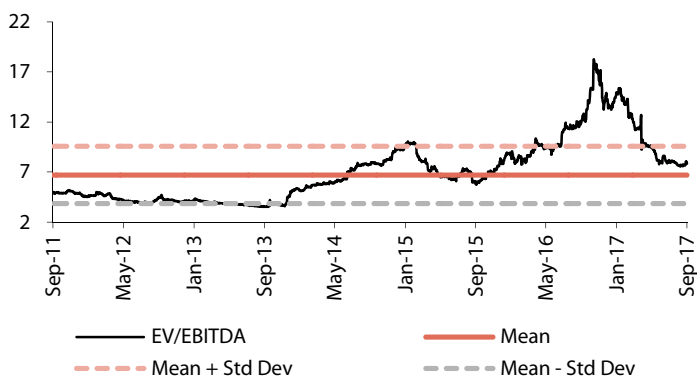
Average 5-yr adj. cash flow yield (FY13-17, %)	5.9
Premium	15%
Average 5-yr adj. cash flow yield (FY13-17, %) after discount	5.1
Implied EV/5 yr AOCF Multiple (x)	19.6
Average Operating cash flow after interest (FY15-19E, Rs mn)	865
Target Enterprise Value (Rs mn)	16,973
Net Debt (FY19, Rs mn)	418
Target Market Cap (Rs mn)	16,555
No of shares	13.2
Target Price (Rs/shr)	1,260

Source: Company, Centrum Research Estimates

We believe that the small premium assigned to the multiple is justified on account of the following reasons:

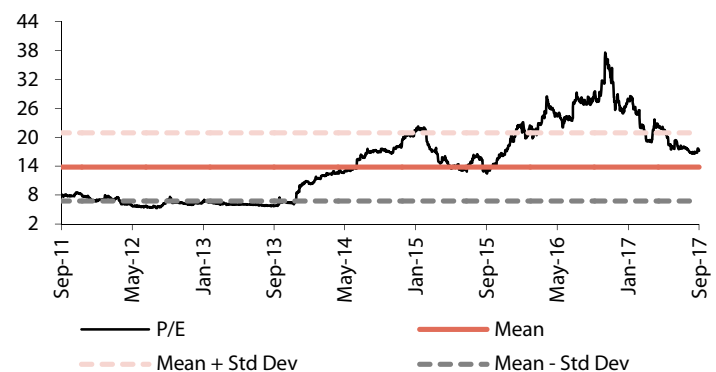
- **Major capex is over:** FIEM has already invested a lot in both its LED and auto businesses recently and does not require any further capex in its core business to grow over the next two years.
- **The LED business has the potential to make it big:** FIEM has faced a lot of issues in its LED business but they have been working on various fronts such as forging an alliance with Su-Kam, planning their own marketing channel, targeting gulf regions for LED exports etc. Also, some price sanity seems to be returning to the LED market which may help FIEM regain some of its lost business.
- **JVs delayed but on the cards:** The company has plans for several JVs which can help to grow its business at higher rates but that got delayed due to various reasons including demonetization. However, the construction of facilities for many of these JVs is nearly complete. We are not taking any revenues from all these efforts in our projections but this remains as an upside risk for our projections. We believe that the recent execution of a JV with Kyowa Co. Ltd. Is very positive development and it indicates that other JVs would be reality in future.

Exhibit 2: 1 year forward EV/EBITDA chart



Source: Bloomberg, Company, Centrum Research Estimates

Exhibit 3: 1 year forward P/E chart



Source: Bloomberg, Company, Centrum Research Estimates

Quarterly financials, Operating Metrics and Key Performance Indicators

Exhibit 4: Quarterly Financials

Y/E March (Rs mn)	2QFY16	3QFY16	4QFY16	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18
Net Sales	2,361	2,586	2,889	2,445	2,918	2,354	2,451	2,907
Raw Materials	1,367	1,514	1,651	1,357	1,697	1,365	1,448	1,746
Employee Costs	317	326	354	360	398	343	355	405
Other Expenditure	384	412	487	414	463	383	409	448
EBITDA	293	334	397	313	360	263	239	308
Depreciation	80	84	88	94	97	100	102	107
Interest	33	42	51	55	63	59	55	60
Other Income	4	6	(3)	1	5	20	21	18
PBT	183	214	254	166	205	124	103	159
Extraordinary items	-	-	-	-	-	-	(142)	-
PBT after EO	183	214	254	166	205	124	(39)	159
Tax	58	57	59	51	64	33	(22)	55
Tax rate (%)	31.6	26.8	23.4	30.7	31.2	26.7	(21.1)	34.8
Reported PAT	125	157	194	115	141	91	(17)	103
YoY Growth (%)								
Revenue	12.2	27.5	24.2	20.2	23.6	(9.0)	(15.2)	18.9
EBITDA	13.3	36.6	31.2	27.1	23.0	(21.4)	(39.8)	(1.6)
PAT	17.5	55.3	44.9	20.6	12.2	(42.2)	(108.7)	(9.9)
QoQ Growth (%)								
Revenue	16.1	9.5	11.7	(15.4)	19.0	(19.4)	4.1	18.6
EBITDA	19.0	14.1	18.6	(21.1)	15.4	(27.1)	(9.1)	29.1
PAT	31.7	24.9	24.1	(41.0)	23.2	(35.7)	(118.7)	(710.1)
Margin (%)								
EBITDA	12.4	12.9	13.7	12.8	12.4	11.2	9.7	10.6
PAT	5.3	6.1	6.7	4.7	4.8	3.8	(0.7)	3.6

Source: Company, Centrum Research

Exhibit 5: Key Assumptions

Particulars (Rs mn)	FY15	FY16	FY17	FY18E	FY19E
Automotive segment					
HMSI	3,948	4,260	4,793	5,965	7,023
YoY Growth (%)	12.6	7.9	12.5	24.4	17.7
TVS Motor	2,307	2,417	2,514	2,923	3,399
YoY Growth (%)	16.3	4.8	4.0	16.3	16.3
Replacement	843	938	980	1,098	1,218
YoY Growth (%)	(4.1)	11.3	4.5	12.0	11.0
Others	1,774	1,958	2,365	3,027	3,742
YoY Growth (%)	17.5	10.3	20.8	28.0	23.6
Total Automotive Gross sales	8,872	9,574	10,652	13,013	15,383
YoY Growth (%)	12.6	7.9	11.3	22.2	18.2
Total LED Gross Sales	131	1,249	592	400	1,100
YoY Growth (%)		857.2	(52.6)	(32.4)	175.0
Total Gross sales	9,003	10,823	11,244	13,413	16,483
Total Net sales	8,195	9,775	10,077	12,006	14,782
YoY Growth (%)	14.8	19.3	3.1	19.1	23.1
Other operating income	53	95	98	106	119
Total revenues	8,248	9,870	10,174	12,112	14,901
YoY Growth (%)	14.8	19.7	3.1	19.0	23.0

Source: Centrum Research Estimates

Financials

Exhibit 6: Income Statement

Y/E March (Rs mn)	FY15	FY16	FY17	FY18E	FY19E
Net Sales	8,248	9,870	10,174	12,112	14,901
% growth	14.8	19.7	3.1	19.0	23.0
Raw Materials	5,092	5,899	6,043	7,258	9,034
% of sales	61.7	59.8	59.4	59.9	60.6
Personnel	983	1,269	1,456	1,660	1,892
% of sales	11.9	12.9	14.3	13.7	12.7
Manufacturing & Other Exp.	1,149	1,432	1,501	1,729	2,101
% of sales	13.9	14.5	14.8	14.3	14.1
EBITDA	1,024	1,270	1,174	1,465	1,874
EBITDA Margin (%)	12.4	12.9	11.5	12.1	12.6
Depreciation	306	330	392	445	470
EBIT	718	940	782	1,019	1,404
Interest Expenses	120	158	232	220	199
PBT From Operations	598	782	550	799	1,205
Other Income	9	10	47	70	73
Exceptional items	-	-	(142)	-	-
PBT	607	792	455	869	1,278
Tax-Total	184	220	126	278	409
Tax Rate (%) - Total	30.3	27.8	27.7	32.0	32.0
Reported PAT	423	572	329	591	869
Adjusted PAT	423	572	424	591	869

Source: Company, Centrum Research Estimates

Exhibit 7: Key Ratios

Y/E March	FY15	FY16	FY17	FY18E	FY19E
Growth ratios (%)					
Net sales	14.8	19.7	3.1	19.0	23.0
EBITDA	15.8	24.0	(7.5)	24.7	27.9
Adjusted Net Profit	13.0	35.3	(25.8)	39.4	47.0
Margin Ratio (%)					
EBITDA Margin	12.4	12.9	11.5	12.1	12.6
EBIT Margin	8.7	9.5	7.7	8.4	9.4
PBT Margins	7.2	7.9	5.4	6.6	8.1
PAT Margin	5.1	5.8	4.2	4.9	5.8
Return Ratio (%)					
ROE	19.9	22.9	12.2	13.3	17.3
ROCE	14.2	16.8	10.6	10.5	13.6
ROIC	14.2	16.8	12.3	11.8	15.8
Turnover Ratio days (days)					
Gross Block Turnover Ratio	1.8	1.8	1.6	1.6	1.8
Inventory Period	23	24	37	36	34
Debtors Period	38	44	43	40	38
Creditors Period	39	56	54	54	54
Cash Conversion Cycle	22	13	25	22	18
Solvency Ratio					
Debt-equity (x)	0.5	0.5	0.5	0.4	0.3
Net Debt-equity (x)	0.5	0.5	0.5	0.4	0.2
Current ratio (x)	1.3	1.1	1.5	1.5	1.5
Interest coverage ratio	6.0	6.0	3.4	4.6	7.0
Gross Debt/EBITDA	1.1	1.1	1.9	1.4	0.9
Dividend					
Dividend per share	6.4	7.3	8.0	9.0	13.2
Dividend Pay-out (%)	19.8	16.7	32.0	20.0	20.0
Dividend Yield (%)	0.7	0.8	0.9	1.0	1.4
Per share (Rs)					
Basic EPS (reported)	35.3	47.8	25.0	44.9	66.0
FDEPS (Adjusted)	32.1	43.5	32.2	44.9	66.0
CEPS	55.4	68.6	62.0	78.7	101.7
Book value	190.0	228.2	321.7	355.8	405.9
Valuation					
P/E	18.5	13.4	30.3	20.9	14.2
P/BV	3.4	3.9	3.2	2.6	2.3
5 Year Average AOCF/EV Yield %	5.2	5.4	4.2	5.4	6.8
EV/EBITDA	8.8	7.1	12.7	9.6	7.3
EV/Sales	1.1	0.9	1.5	1.2	0.9

Source: Company, Centrum Research Estimates

Exhibit 8: Balance Sheet

Y/E March (Rs mn)	FY15	FY16	FY17	FY18E	FY19E
Sources of funds					
Capital	120	120	132	132	132
Reserves & Surplus	2,154	2,611	4,102	4,551	5,210
Shareholders' Funds	2,273	2,730	4,233	4,682	5,342
Minority Interest	-	-	-	-	-
Total Loan Funds	1,171	1,400	2,250	2,050	1,750
Deferred Tax Liabilities-Net	276	297	396	439	503
Total Liabilities	3,721	4,427	6,879	7,171	7,595
Application of funds					
Gross Block	4,796	5,934	7,094	7,750	8,450
Accumulated Dep.	(1,454)	(1,777)	(2,167)	(2,612)	(3,082)
Capital WIP	46	116	56	0	0
Net Fixed Assets	3,388	4,273	4,984	5,138	5,369
Investments	4	7	840	840	840
Goodwill	-	-	-	-	-
Inventories	514	661	1,024	1,195	1,388
Sundry Debtors	867	1,186	1,188	1,327	1,551
Other Current Assets	-	-	-	-	-
Cash & Cash Equivalent	33	37	228	334	492
Loans and Advances	208	421	634	727	894
Total Current Assets	1,621	2,305	3,075	3,582	4,326
Trade Payables	884	1,508	1,504	1,792	2,205
Current Liabilities	266	483	451	537	660
Provisions	142	167	65	61	75
Total Current Liabilities & Provision	1,293	2,158	2,020	2,389	2,939
Net Current Assets	329	147	1,055	1,193	1,386
Miscellaneous Expenditure	-	-	-	-	-
Total Assets	3,721	4,427	6,879	7,171	7,595

Source: Company, Centrum Research Estimates

Exhibit 9: Cash Flow

Y/E March (Rs mn)	FY15	FY16	FY17	FY18E	FY19E
Operating profit before WC changes	1,037	1,282	1,040	1,300	1,602
Net change in working capital	(75)	126	(658)	(32)	(35)
Cash flow from operating activities (a)	821	1,215	382	1,268	1,568
Adjusted Operating Cash flow	700	1,058	150	1,047	1,368
Capital expenditure	(585)	(1,089)	(1,159)	(600)	(700)
Adjusted FCF	115	(31)	(1,010)	447	668
Cash flow from investing activities (b)	(586)	(1,084)	(1,948)	(600)	(700)
Cash flow from financing activities (c)	(220)	(127)	1,758	(563)	(709)
Net change in cash (a+b+c)	15	4	192	105	159

Source: Company, Centrum Research Estimates

Appendix A

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FIEM Industries price chart



Source: Bloomberg, Centrum Research

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