

## MOTHERSON SUMI SYSTEMS

AUTO

06 DEC 2017

Visit Note

**BUY**

Target Price: Rs 403

### On course to meet high targets

In its Vision 2020 update meeting, the management of Motherson Sumi (MSS) highlighted that it is on course to achieve its ambitious 2020 revenue target of USD 18 bn (vs. USD 8 bn currently) and RoCE of 40% (~28% currently); in fact, it could meet 2020 target a year earlier. Moreover, it is foraying into the non-auto space (medical, defense, aerospace, security systems) which can drive growth beyond FY20.

MSS remains one of our preferred picks among Auto ancillaries. The India business is a good play on India PVs due to rising premiumization and electronics, more so going into BS-VI emission norms. Overseas subsidiaries have strong growth avenues with new technologies and product/customer synergies from acquisitions. Reiterate BUY with TP of Rs 403 (27x FY19E P/E).

CMP : Rs 343  
Potential Upside : 18%

#### MARKET DATA

No. of Shares : 2,105 mn  
Free Float : 37%  
Market Cap : Rs 722 bn  
52-week High / Low : Rs 373 / Rs 190  
Avg. Daily vol. (6mth) : 2.8 mn shares  
Bloomberg Code : MSS IB Equity  
Promoters Holding : 63%  
FII / DII : 20% / 8%

### Key takeaways

- ♦ **Inorganic strategy:** The management reiterated that it remains on track to achieve target of USD 18 bn before 2020. The key criterion is to achieve the 40% RoCE target over the next 3-5 years. Its OEM customers are very critical in the entire scheme of things, as all acquisitions are done at the behest of OEMs. MSS will prefer products which are complimentary in nature (over a new component), as synergies enable it to achieve RoCE target early. Thus, the company will not chase top line growth for the sake of it
- ♦ **On rising trend of EVs:** The management does not expect EVs to become a significant part of industry in near to medium term. It also sees this shift as a huge prospect for acquisitions, as there will be numerous opportunities to buy companies/assets which are shifting focus to EVs

(Continued on page 2...)

### Financial summary (Consolidated)

Y/E March	FY16	FY17	FY18E	FY19E
Sales (Rs mn)	372,163	424,752	566,340	671,079
Adj PAT (Rs mn)	13,228	16,335	23,945	31,395
Con. EPS* (Rs)	-	-	10.5	14.2
EPS (Rs)	6.3	7.8	11.4	14.9
Change YOY (%)	50.4	23.5	46.6	31.1
P/E (x)	54.6	44.2	30.1	23.0
RoE (%)	34.3	25.8	26.2	28.0
RoCE (%)	24.4	20.9	21.9	26.8
EV/E (x)	21.7	18.7	13.2	10.1
DPS (Rs)	1.6	1.3	3.0	3.0

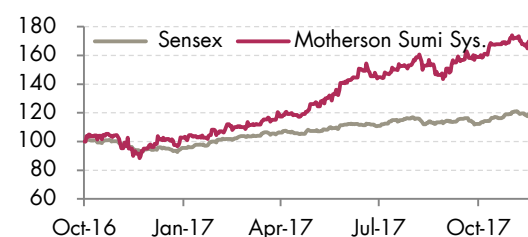
Source: \*Consensus broker estimates, Company, Axis Capital

^ SMRP BV – Samvardhana Motherson Automotive Systems Group BV

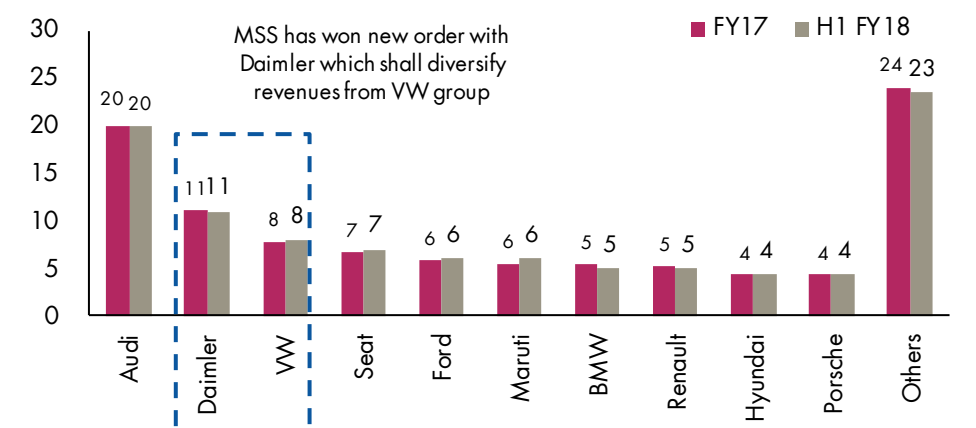
### Key drivers

(%)	FY17	FY18E	FY19E
Standalone EBITDA margin	19.7	19.5	19.6
SMR EBITDA margin	10.9	11.2	11.8
SMP EBITDA margin	6.4	6.5	8.0

### Price performance



## Exhibit 1: Consolidated OEM-wise revenue break-up



Source: Company, Axis Capital

## Meeting RoCE more important than topline

- ♦ The company's 2020 revenue target of USD 18 bn hinges on finding acquisitions which helps it meet RoCE target of 40%. It has come across many acquisitions which will help it meet the revenue target, but did not give it confidence on meeting the RoCE target. Also, an acquisition should support its 3Cx15 stance – that no customer/ component/ country should account for more than 15% of the consolidated revenue
- ♦ The chairman sees several acquisition opportunities and is confident of meeting this target. In fact, it is likely that it will meet the target in 2019 itself. Before acquiring PKC, MSS was the 31st largest auto component maker in the world; it is probably 28-29th now

## Exhibit 2: MSS five year targets

Year	FY05 (Rs mn)		FY10 (Rs bn)		FY15 (Rs bn)		FY20 (Rs bn)
	Target	Actual	Target	Actual	Target	Actual	Target
Revenue	10.0	10.3	1.0	1.5	5.0	5.9	18.0
RoCE	40%	39%	40%	16%/31%*	40%	26%/41%*	40%
Export sales	30%	29%	60%	70%	70%	80%	80%
Div. payout	40%	43%	40%	32%	40%	34%	40%

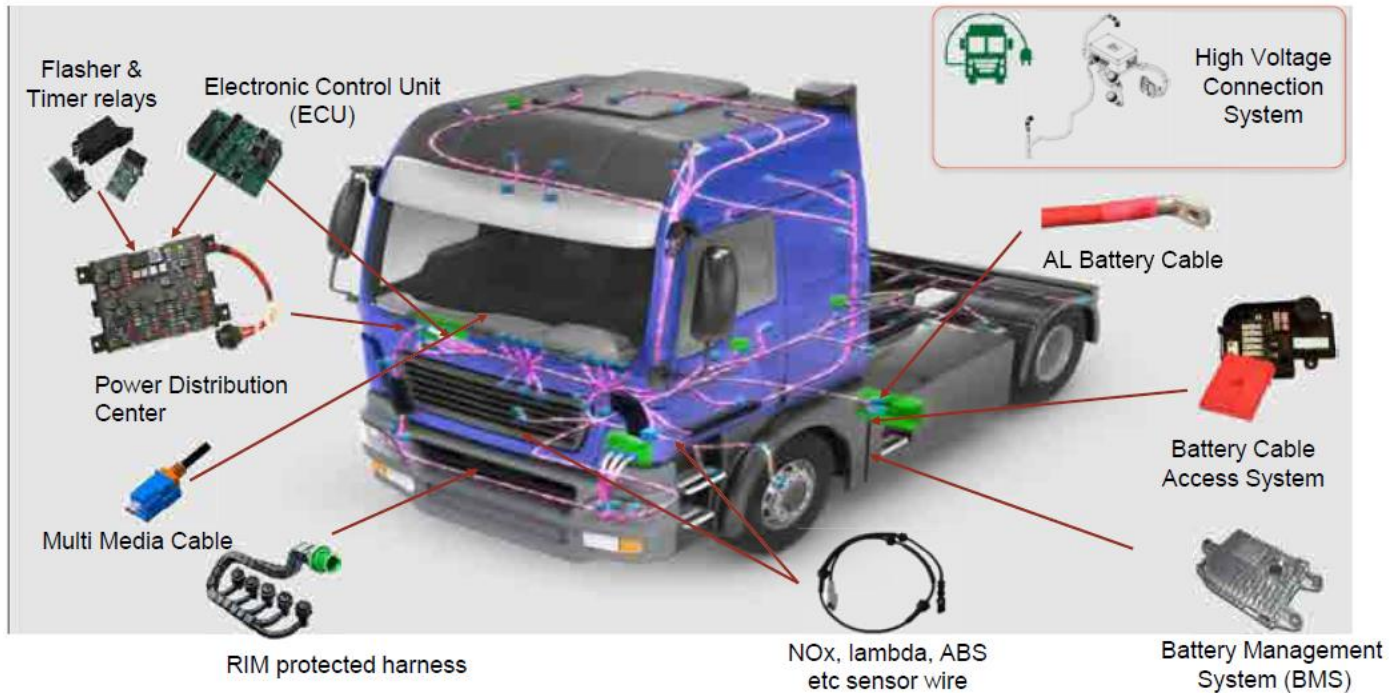
Source: Company, Axis Capital

\*Standalone business

## Wiring harness division

- ♦ MSS' wiring harness division is the **market leader** in India PV segment and North America CVs (through PKC group and Stoneridge wiring harness). With acquisition of PKC, the company has added new customers in farm equipment space, rolling stock and construction equipment
- ♦ **Synergies:** The management expects PKC to benefit from various insourcing and outsourcing policies of MSS (perfected over years), while MSS benefits from PKC's knowledge base in managing complex wiring harness and high level customization

### Exhibit 3: New content addition in CV space to aid growth



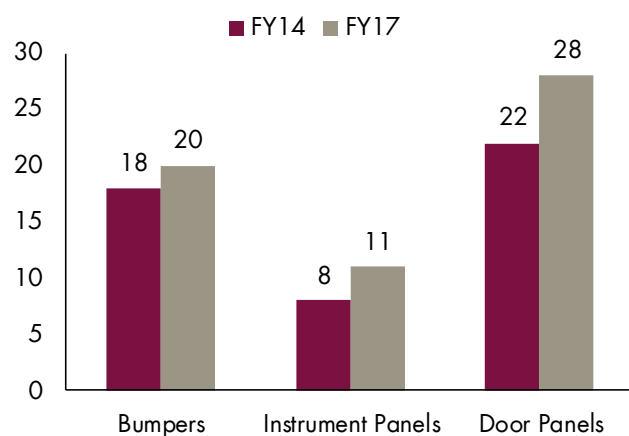
Source: Company

- ♦ **Significant content addition:** The company expects significant content addition (anywhere between 20-50%), as India moves to BS-VI norms. This will be driven by increasing complexity (higher use of electronics and sensors). Further, with PKC, the company has added many new products (see chart below) which will aid growth

### SMP (Samvardhana Motherson Peguform):

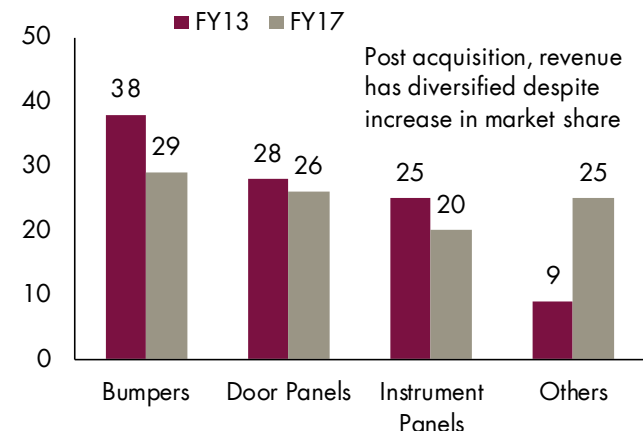
- ♦ SMP has added **new technologies** (acquisition of S&T and Kobek) and diversified revenue/ region mix. Further, it's FCF cycle is improving – it has invested heavily in last 3 years and sees capex tapering after FY19

### Exhibit 4: SMP – Global premium market share has increased



Source: Company, Axis Capital





### Exhibit 5: SMP – Diversifying product segments



Source: Company, Axis Capital

- Most of the new order wins has led to **new greenfield plants with focus to increase penetration in North America** (~75% capex spent for growth in North America). As per management's estimates, the 3 plants which will start commercial production in next 12 months will contribute EUR 1 bn to revenue (~28% growth from current base)
- The capex has also increased receivables for engineering; thus, working capital at SMP is bloated. However, this should come down once plants starts normal production, thereby improving RoCE
- SMP is working on various **new products**: (1) dashboard integrated with screens (to replace mirror eventually); (2) light weight door panels using natural fibers (25% weight reduction); and (3) premium interiors and exteriors in autonomous and connected mobility with various features

#### Exhibit 6: SMP – Opportunities to increase market share with top 8 OEMs

Key Customers	Key Models	Key Products supplied			Key Geographies	Relationship length
		Bumpers	Inst. Panels	Door Panels		
	A B C D E F	✓ ✓	✓ ✓	✓ ✓ ✓ ✓	Europe, China, Brazil, Mexico	> 30 years
	A B C D E F	✓ ✓ ✓ ✓	✓	✓	Europe, China, Mexico, Brazil	> 40 years
	A B C D	✓ ✓ ✓	✓	✓	Europe	> 30 years
	A B C D E F G	✓ ✓ ✓ ✓	✓	✓	Europe, Mexico	> 30 years
	A B C D E F	✓ ✓ ✓ ✓		✓ ✓	Europe, China, Hungary, USA	> 30 years
	A B C D E	✓ ✓	✓	✓ ✓ ✓	Europe	> 20 years
	A B C D	✓ ✓ ✓			Europe, Brazil	> 20 years
	A	✓			Europe	> 30 years

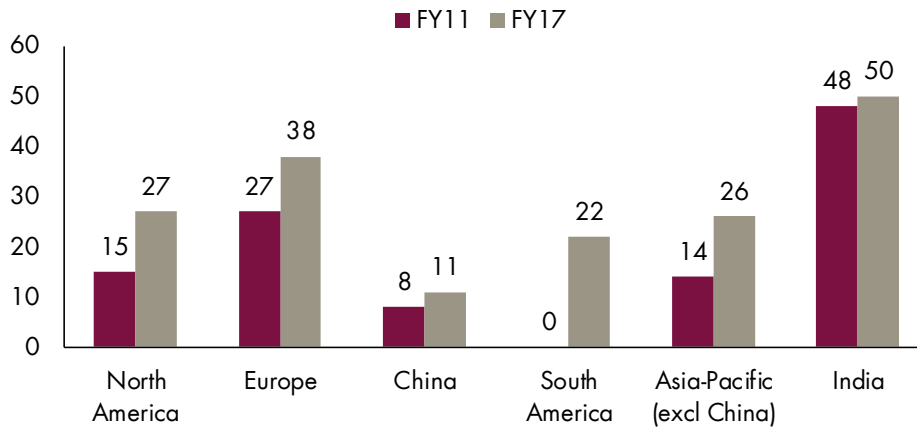
Source: Company

#### SMR (Samvardhana Motherson Reflectec)

- SMR remains one of the **largest exterior mirror players with market share of 25%** currently, up from 22% in 2015 and 21% in 2009. The company has incurred significant capex in new paint shop, process improvement which has driven such improvement

- ♦ The company's **content per vehicle** has doubled in last decade driven by increasing electric content and is expected to increase 50% in next decade as industry shifts to camera-based mirrors (for autonomous driving and EVs) vs. conventional ones

### Exhibit 7: SMR – Market share across key geographies



Source: Company, Axis Capital

- ♦ In terms of **product mix**, the medium and premium segment accounts for ~90% of the revenue. The company enjoys >30% share in premium segment (10% of car production) and expects this segment to drive next generation products

### MATE division

- ♦ This division **serves dual role**: (1) back end support for the group by supplying critical child parts and (2) leveraging the group's technical capabilities by winning orders from both domestic and global OEMs
- ♦ The division supplies connectors for wiring harness division and various plastic components (smaller size) to SMRP BV. It is setting up a new Hungary plant to supply parts to SMP

### Pivot strategy

- ♦ The company is developing products in non-automotive, medical segment where it sees huge potential. The company believes, after 2020, once it reaches USD 26 bn turnover on group level, it will look beyond auto segment to spread its wings
- ♦ MSS has zeroed in **different new focus segments beyond 2020**: (1) Aerospace, (2) Defense, (3) Security systems (leveraging on its current IT division); and (4) medical equipment

### Our view

#### India business a good way to play domestic four-wheeler industry

- ♦ MSS' India business might be 14-15% of FY17 consolidated turnover, but it is 50% of consolidated profits (and presumably a higher share of market cap)
- ♦ Historically, standalone revenue growth has outpaced underlying car industry growth driven by rising electronic content per vehicle and premiumization. Hence, it is a good way to play the growth in domestic PVs

- With BS-VI emission norms, there is a significant rise in electronic content across segments, which will also increase wiring harness content

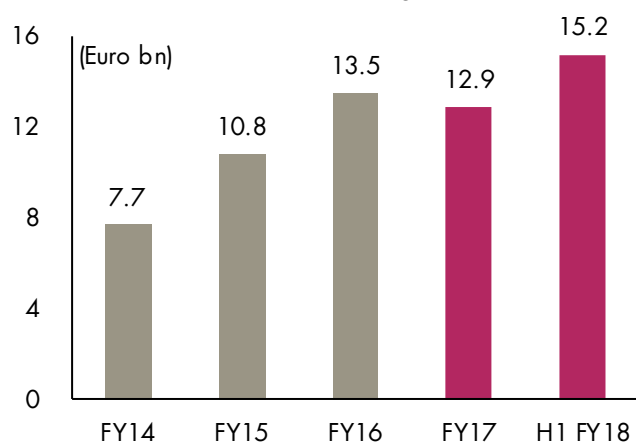
### Strengthening global wiring harness business

Going into BS-VI, an advantage for MSS is that it already has Euro-6 expertise due to its exposure to OEMs in EU/UK/US. MSS' recent acquisitions have strengthened its position in global wiring harness (14% of consolidated revenue currently, but on course to increase):

- In May 2014, it acquired the wiring harness business of Stoneridge Inc (supplies in North America) at transaction value of USD 65.7 mn. The wiring harness division had sales of USD 300 mn at the time and was EBITDA break-even (mid-single digit margin now)
- In January 2017, Motherson announced acquisition of Finland based PKC Group, supplier of wiring harness and electronics to CVs and locomotive for Eur 571 mn. CY16 financial details: Revenue Euro 850 mn (66% N America, 28% Europe, 5% S America), EBITDA Euro 64 mn (7.5% margin) and RoCE 9%

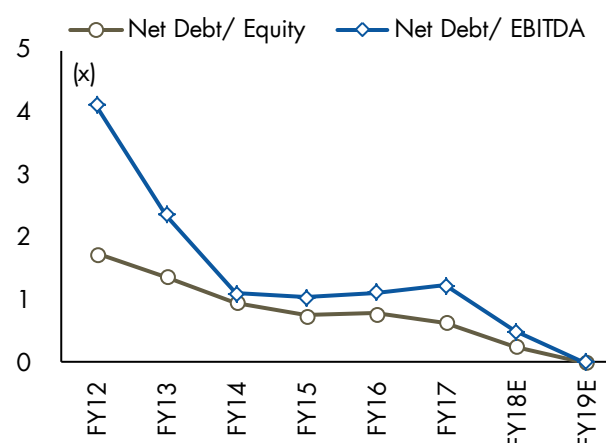
These acquisitions will help MSS consolidate its global share in wiring harness segment, as it supplies to complicated Euro 6 vehicles in these regions.

### Exhibit 8: SMRP BV order book strong at Euro 15 bn



Source: Company, Axis Capital

### Exhibit 9: Leverage is down despite acquisitions & capex



Source: Company, Axis Capital

### Global businesses on strong footing

- MSS globally has geographical gaps given its high exposure to Europe and India. It is now increasing presence in the relatively untapped North America and China markets (cumulatively >50% of global car volumes). New investments in Mexico/China for SMR/SMP and recent acquisition of Stoneridge's wiring harness business in US, and the PKC acquisition are steps in these directions
- With acquisitions on behest of customers, MSS is able to command better operational terms – generally it gets 2-year working capital support, payment in advance, right to first refusal on orders, etc. This helps it understand the business even though it is a new product

### Focus on new technologies bodes well for pricing power

- ♦ Use of advanced electronics to make cars safer is the future, and MSS hopes to play a big role in it. With sharp decline in camera prices, radars are being replaced by cameras, which help detect crashes faster and deploy airbags when crash looks imminent
- ♦ Some of the new technologies the company is working on are: (1) Cameras replacing mirrors; (2) Intelligent surround view (fish-eye cameras); and (3) Driver assists. MSS is best-placed to be a complete solution provider (vs. a component supplier) for many of these features given its dominance in bumpers and mirrors (both of which provide a 360 degree view of the car) and dashboards (which would display the images)

### Reiterate BUY

The company has over last few years transformed from a domestic player to a global ancillary player of scale. While India business will benefit from BS-VI emission norms and premiumization, the overseas subsidiaries are directionally focusing more on new technologies and providing complete solutions; this bode well for pricing power and is also a catalyst for growth. Reiterate BUY with unchanged TP of Rs 403 (27x FY19E P/E; 10% premium to 5 year average).

### Exhibit 10: Standalone financial assumptions

(Rs mn)	FY13	FY14	FY15	FY16	FY17	FY18E	FY19E
Revenues	43,217	45,245	49,850	52,829	63,129	76,520	93,973
EBITDA	7,746	9,096	9,170	10,206	12,411	14,943	18,425
EBITDA margin %	17.9	20.1	18.4	19.3	19.7	19.5	19.6
Adjusted PAT	4,696	5,738	5,194	7,085	7,925	10,142	12,650
Adjusted EPS (Rs)	2.2	2.7	2.5	3.4	3.8	4.8	6.0
RoE (%)	28.9	30.1	24.7	28.9	13.7	16.7	19.2
RoCE (%)	33.8	40.0	40.7	41.9	44.4	50.0	53.2
Fixed asset turns (x)	1.9	1.9	1.9	1.9	2.2	2.5	2.8

Source: Company, Axis Capital

### Exhibit 11: SMR financial assumptions

(Rs mn)	FY13	FY14	FY15	FY16	FY17	FY18E	FY19E
Revenues	69,510	90,690	98,890	100,786	115,920	128,205	143,590
EBITDA	4,480	8,673	9,686	10,556	12,586	14,359	16,944
EBITDA margin %	6.4	9.6	9.8	10.5	10.9	11.2	11.8
Adjusted PAT (post minority)	630	2,017	2,405	2,696	3,252	3,716	4,489

Source: Company, Axis Capital

### Exhibit 12: SMP financial assumptions

(Rs mn)	FY13	FY14	FY15	FY16	FY17	FY18E	FY19E
Revenues	127,820	155,412	172,200	189,281	219,770	265,157	312,885
EBITDA	4,830	8,429	10,640	10,845	14,058	17,235	25,031
EBITDA margin %	3.8	5.4	6.2	5.7	6.4	6.5	8.0
Adjusted PAT (post minority)	(210)	(602)	1,614	1,624	2,415	3,193	5,681

Source: Company, Axis Capital



**Exhibit 13: Consolidated financial assumptions**

(Rs mn)	FY13	FY14	FY15	FY16	FY17	FY18E	FY19E
Revenues	253,124	306,363	347,301	372,163	424,752	566,340	671,079
<b>EBITDA</b>	<b>14,767</b>	<b>27,936</b>	<b>29,123</b>	<b>35,788</b>	<b>42,665</b>	<b>59,170</b>	<b>75,586</b>
<b>EBITDA margin %</b>	<b>5.8</b>	<b>9.1</b>	<b>8.4</b>	<b>9.6</b>	<b>10.0</b>	<b>10.4</b>	<b>11.3</b>
Adjusted PAT	4,445	9,530	8,794	13,228	16,335	23,945	31,395
<b>Adjusted EPS (Rs)</b>	<b>2.1</b>	<b>4.5</b>	<b>4.2</b>	<b>6.3</b>	<b>7.8</b>	<b>11.4</b>	<b>14.9</b>
P/E	168.1	78.4	84.9	56.5	45.7	31.2	23.8
EV/EBITDA	76.6	39.8	40.5	30.9	26.8	17.6	13.4
RoE (%)	19.4	32.2	26.5	30.1	19.7	23.9	25.3
RoCE (%)	12.8	31.3	27.4	28.5	19.5	27.0	33.2
Fixed asset turns (x)	4.8	5.2	5.7	5.2	3.5	4.4	5.1

Source: Company, Axis Capital



## Financial summary (Consolidated)

### Profit & loss (Rs mn)

Y/E March	FY16	FY17	FY18E	FY19E
Net sales	372,163	424,752	566,340	671,079
Other operating income	-	-	-	-
<b>Total operating income</b>	<b>372,163</b>	<b>424,752</b>	<b>566,340</b>	<b>671,079</b>
Cost of goods sold	(224,093)	(257,507)	(356,794)	(422,780)
Gross profit	148,070	167,246	209,546	248,299
<i>Gross margin (%)</i>	<i>39.8</i>	<i>39.4</i>	<i>37.0</i>	<i>37.0</i>
Total operating expenses	(112,282)	(124,581)	(150,376)	(172,713)
<b>EBITDA</b>	<b>35,788</b>	<b>42,665</b>	<b>59,170</b>	<b>75,586</b>
<i>EBITDA margin (%)</i>	<i>9.6</i>	<i>10.0</i>	<i>10.4</i>	<i>11.3</i>
Depreciation	(10,872)	(10,590)	(13,114)	(14,791)
<b>EBIT</b>	<b>24,916</b>	<b>32,075</b>	<b>46,056</b>	<b>60,795</b>
Net interest	(3,450)	(3,749)	(2,531)	(2,446)
Other income	392	1,463	419	632
<b>Profit before tax</b>	<b>21,858</b>	<b>29,789</b>	<b>43,944</b>	<b>58,980</b>
Total taxation	(5,193)	(9,103)	(13,243)	(17,672)
<i>Tax rate (%)</i>	<i>23.8</i>	<i>30.6</i>	<i>30.1</i>	<i>30.0</i>
Profit after tax	16,665	20,685	30,700	41,308
Minorities	(4,814)	(6,181)	(6,753)	(9,910)
Profit/ Loss associate co(s)	1,377	1,831	(2)	(2)
Adjusted net profit	13,228	16,335	23,945	31,395
<i>Adj. PAT margin (%)</i>	<i>3.6</i>	<i>3.8</i>	<i>4.2</i>	<i>4.7</i>
Net non-recurring items	(306)	(793)	-	-
Reported net profit	12,922	15,543	23,945	31,395

### Balance sheet (Rs mn)

Y/E March	FY16	FY17	FY18E	FY19E
Paid-up capital	1,323	1,404	2,105	2,105
Reserves & surplus	42,648	81,323	97,879	121,884
Net worth	43,971	82,727	99,984	123,990
Borrowing	57,416	101,418	89,628	78,724
Other non-current liabilities	(1,210)	(763)	(763)	(763)
<b>Total liabilities</b>	<b>115,300</b>	<b>205,703</b>	<b>217,926</b>	<b>240,940</b>
Gross fixed assets	147,492	207,643	227,423	245,483
Less: Depreciation	(76,023)	(86,614)	(99,728)	(114,519)
Net fixed assets	71,469	121,030	127,695	130,964
Add: Capital WIP	13,970	19,349	19,349	19,349
Total fixed assets	85,439	140,378	147,044	150,313
Total Investment	5,897	5,632	7,473	9,532
Inventory	22,850	30,716	36,163	42,880
Debtors	46,537	66,065	67,386	80,919
Cash & bank	17,717	48,866	60,253	78,647
Loans & advances	384	710	742	778
Current liabilities	80,137	112,970	127,968	149,540
Net current assets	23,964	59,692	63,408	81,095
Other non-current assets	-	-	-	-
<b>Total assets</b>	<b>115,300</b>	<b>205,703</b>	<b>217,926</b>	<b>240,940</b>

Source: Company, Axis Capital

### Cash flow (Rs mn)

Y/E March	FY16	FY17	FY18E	FY19E
Profit before tax	21,858	29,789	43,944	58,980
Depreciation & Amortisation	10,872	10,590	13,114	14,791
<i>Chg in working capital</i>	<i>(4,629)</i>	<i>(4,580)</i>	<i>7,671</i>	<i>707</i>
<b>Cash flow from operations</b>	<b>27,685</b>	<b>57,902</b>	<b>53,598</b>	<b>58,621</b>
<i>Capital expenditure</i>	<i>(25,464)</i>	<i>(65,529)</i>	<i>(19,780)</i>	<i>(18,060)</i>
<b>Cash flow from investing</b>	<b>(30,320)</b>	<b>(63,802)</b>	<b>(21,202)</b>	<b>(19,487)</b>
<i>Equity raised/ (repaid)</i>	<i>441</i>	<i>81</i>	<i>702</i>	-
<i>Debt raised/ (repaid)</i>	<i>8,311</i>	<i>44,002</i>	<i>(11,789)</i>	<i>(10,904)</i>
<i>Dividend paid</i>	-	-	-	-
<b>Cash flow from financing</b>	<b>1,432</b>	<b>37,049</b>	<b>(21,008)</b>	<b>(20,740)</b>
Net chg in cash	(1,202)	31,149	11,387	18,395

### Key ratios

Y/E March	FY16	FY17	FY18E	FY19E
<b>OPERATIONAL</b>				
FDEPS (Rs)	6.3	7.8	11.4	14.9
CEPS (Rs)	11.3	12.4	17.6	21.9
DPS (Rs)	1.6	1.3	3.0	3.0
Dividend payout ratio (%)	25.6	18.1	26.4	20.1
<b>GROWTH</b>				
Net sales (%)	7.2	14.1	33.3	18.5
EBITDA (%)	22.9	19.2	38.7	27.7
Adj net profit (%)	50.4	23.5	46.6	31.1
FDEPS (%)	50.4	23.5	46.6	31.1
<b>PERFORMANCE</b>				
RoE (%)	34.3	25.8	26.2	28.0
RoCE (%)	24.4	20.9	21.9	26.8
<b>EFFICIENCY</b>				
Asset turnover (x)	4.3	3.3	3.6	4.2
Sales/ total assets (x)	2.0	1.7	1.7	1.8
Working capital/ sales (x)	-	-	-	-
Receivable days	45.6	56.8	43.4	44.0
Inventory days	24.8	29.3	26.0	26.3
Payable days	56.0	69.9	61.4	61.1
<b>FINANCIAL STABILITY</b>				
Total debt/ equity (x)	1.1	1.2	0.8	0.5
Net debt/ equity (x)	0.8	0.6	0.3	-
Current ratio (x)	1.3	1.5	1.5	1.5
Interest cover (x)	7.2	8.6	18.2	24.9
<b>VALUATION</b>				
PE (x)	54.6	44.2	30.1	23.0
EV/ EBITDA (x)	21.7	18.7	13.2	10.1
EV/ Net sales (x)	2.1	1.9	1.4	1.1
PB (x)	16.4	8.7	7.2	5.8
Dividend yield (%)	0.5	0.4	0.9	0.9
Free cash flow yield (%)	-	-	-	0.1

Source: Company, Axis Capital

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