

Sterling Tools (STL) continues to strengthen its relationship with OEMs enabling it to expand product portfolio. Higher grade / specialised fasteners proportion are on a constant rise and margin expansion was the logical outcome. We expect the proportion of specialised fasteners to rise gradually for the foreseeable future. Volatility in raw material prices can impact margins for a couple of quarters as the raw material impact is passed on with a lag. Meidoh tie up will open up significant opportunities for STL. The capacity augmentation through a greenfield capacity in Karnataka will support revenue growth. As the stock has corrected to certain extent, this can be considered a buying opportunity from a 12 month plus perspective. Recommend BUY with a TP of ₹ 477.

### Margin Outlook

STL generally passes on the increase in the raw material price with a quarter lag. With raw material prices on an upward trajectory, we believe that gross margins can have some pressure in the coming quarters. This would be negated to a certain extent with increasing proportion of specialised fasteners in the product mix. However, our long-term view on margin remains intact driven by increasing proportion of specialised fasteners.

### Automobile Industry Outlook

Fastener industry can grow at a higher rate than the growth of Automobile Industry. With an expectation of 8% - 10% growth for the Automobile sector, fastener industry is expected to grow at 10% - 12%. STL with thrust on adding new products is expected to grow ahead of fastener industry. The higher growth rate would also be aided by increasing proportion of specialised fasteners as they offer higher realisations.

### Meidoh Traction

STL will get the technical know-how from Meidoh for all its facilities that will enable STL to manufacture specialised fasteners. Meidoh already has global tie ups with Suzuki that will enable STL to push for specialised fastener supply to Maruti Suzuki. STL will also get entry to Japanese players like Toyota and the vendor certification process is already under process.

### Capital Expenditure

The capex for the new greenfield project is at ₹ 800mn. This will be funded by term loans to the tune of ₹ 400mn and the remaining ₹ 400mn would be funded by the cash in books. This cash in books is from the 5% stake taken by Meidoh in STL in May'17. This facility should be ready by Q1FY20.

**View:** We believe that it's a structural story and with new products getting added, STL would grow faster than the industry along with margin expansion. The return ratios remain strong and will support expensive valuations. Due to the recent correction, we believe this can be a buying opportunity from a long-term perspective. We recommend BUY with a target price of ₹ 477.

## FINANCIALS (₹ Mn)

Particulars	FY16	FY17	FY18E	FY19E	FY20E
<b>Net Sales</b>	<b>3,643</b>	<b>3,701</b>	<b>4,188</b>	<b>4,816</b>	<b>5,779</b>
Growth (%)	9.5	1.6	13.2	15.0	20.0
<b>EBITDA</b>	<b>619</b>	<b>738</b>	<b>921</b>	<b>1,075</b>	<b>1,312</b>
OPM (%)	16.7	19.6	21.7	22.1	22.6
<b>PAT</b>	<b>284</b>	<b>389</b>	<b>480</b>	<b>572</b>	<b>717</b>
Growth (%)	33.3	36.8	23.5	19.1	25.3
EPS (₹)	8.3	11.4	13.4	15.9	19.9
Growth (%)	33.3	36.8	17.7	19.1	25.3
PER(x)	46.1	33.7	28.7	24.1	19.2
ROANW (%)	22.7	26.2	26.9	22.8	25.2
ROACE (%)	23.1	26.7	32.3	31.6	36.0

CMP	₹ 383
Target / Upside	₹ 477/25%
BSE Sensex	33,807
NSE Nifty	10,381

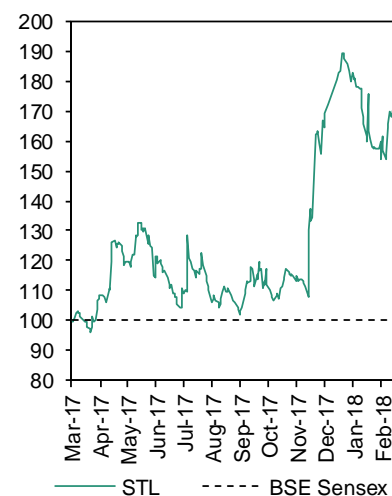
### Script Details

Equity / FV	₹ 72mn/₹ 2/-
Market Cap	₹ 14bn
	USD 212mn
52-week High/Low	₹ 478/189
Avg. Volume (no)	33,785
NSE Symbol	STERTOOLS
Bloomberg Code	STRT IN

### Shareholding Pattern Dec'17(%)

Promoters	65.3
MF/Banks/FIs	5.2
FIIIs	0.0
Public / Others	29.5

### STL Relative to Sensex



— STL      - - - - BSE Sensex

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### Income Statement (₹ mn)

Particulars	Mar17	Mar18E	Mar19E	Mar20E
<b>Net Sales</b>	<b>3,701</b>	<b>4,188</b>	<b>4,816</b>	<b>5,779</b>
Other Operating Income	38	30	30	11
Total Income	3,739	4,218	4,846	5,790
Total Expenditure	3,002	3,317	3,791	4,498
Cost of materials consumed	1,339	1,529	1,758	2,081
Employee Benefits Exp	351	386	444	510
Other Expenses	1,312	1,403	1,589	1,907
Other Income	26	20	20	20
<b>EBIDTA (Excl. OI)</b>	<b>738</b>	<b>901</b>	<b>1,055</b>	<b>1,292</b>
<b>EBIDTA (Incl. OI)</b>	<b>764</b>	<b>921</b>	<b>1,075</b>	<b>1,312</b>
Interest	55	30	25	20
Depreciation	153	171	190	209
PBT & EO Items	555	719	860	1,083
Extra Ord. Exps/(Income)	44	0	0	0
Profit Before Tax	599	719	860	1,083
Tax	211	259	308	386
<b>Net Profit</b>	<b>388</b>	<b>460</b>	<b>552</b>	<b>697</b>

### Balance Sheet (₹ mn)

Particulars	Mar17	Mar18E	Mar19E	Mar20E
<b>Sources of Funds</b>				
Equity Capital	68	72	72	72
Other Reserves	1,571	2,302	2,580	2,960
<b>Net Worth</b>	<b>1,640</b>	<b>2,374</b>	<b>2,652</b>	<b>3,032</b>
Secured Loans	402	302	252	202
<b>Loan Funds</b>	<b>402</b>	<b>302</b>	<b>252</b>	<b>202</b>
Deferred Tax Liability	156	100	50	50
<b>Total Capital Employed</b>	<b>2,198</b>	<b>2,776</b>	<b>2,954</b>	<b>3,284</b>
<b>Applications of Funds</b>				
Gross Block	2,443	2,743	3,043	3,343
Less: Accumulated Depre.	1,011	1,194	1,384	1,593
<b>Net Block</b>	<b>1,431</b>	<b>1,548</b>	<b>1,658</b>	<b>1,749</b>
Capital Work in Progress	0	21	23	25
<b>Investments</b>	<b>179</b>	<b>179</b>	<b>179</b>	<b>179</b>
<b>Current Assets, Loans &amp; Advances</b>				
Inventories	459	485	531	603
Sundry Debtors	342	381	398	476
Cash and Bank Balance	28	368	408	549
Loans and Advances	142	135	128	122
Other Current Assets	9	10	10	10
<i>sub total</i>	981	1,380	1,475	1,760
<b>Less: Current Liabilities &amp; Provisions</b>				
Current Liabilities	352	314	352	399
Provisions	41	38	30	30
<i>sub total</i>	394	352	382	429
Net Current Assets	588	1,028	1,094	1,331
<b>Total Assets</b>	<b>2,198</b>	<b>2,776</b>	<b>2,954</b>	<b>3,284</b>

E – Estimates

### Cash Flow (₹ mn)

Particulars	Mar17	Mar18E	Mar19E	Mar20E
<b>Profit before tax</b>	599	739	880	1,103
Depreciation & w.o.	153	171	190	209
Net Interest Exp	51	30	25	20
Direct taxes paid	(183)	(259)	(308)	(386)
Change in Working Capital	6	(100)	(26)	(95)
Other	(36)	(56)	(50)	0
<b>(A) CF from Opt. Activities</b>	<b>590</b>	<b>526</b>	<b>711</b>	<b>851</b>
Capex	(134)	(321)	(302)	(302)
<b>Free Cash Flow</b>	<b>456</b>	<b>205</b>	<b>409</b>	<b>548</b>
Inc./ (Dec.) in Invnt.	(122)	(0)	0	0
Other	7	0	0	0
<b>(B) CF from Invnt. Activities</b>	<b>(249)</b>	<b>(321)</b>	<b>(302)</b>	<b>(302)</b>
Inc./ (Dec.) in Equity	0	422	0	0
Inc./ (Dec.) in Debt	(289)	(100)	(50)	(50)
Interest exp net	(51)	(30)	(25)	(20)
Dividend Paid (Incl. Tax)	(82)	(168)	(294)	(336)
Other	0	12	0	0
<b>(C) CF from Financing</b>	<b>(422)</b>	<b>136</b>	<b>(369)</b>	<b>(407)</b>
Net Change in Cash	(82)	340	39	142
Opening Cash balances	107	28	368	408
Closing Cash balances	26	368	408	549

### Important Ratios

Particulars	Mar17	Mar18E	Mar19E	Mar20E
<b>(A) Measures of Performance (%)</b>				
EBIDTA Margin (excl. O.I.)	19.6	21.7	22.1	22.6
EBIDTA Margin (incl. O.I.)	20.3	22.2	22.5	22.9
Interest / Sales	1.5	0.7	0.5	0.3
Tax/PBT	35.2	35.0	35.0	35.0
Net Profit Margin	10.3	11.3	11.8	12.3
<b>(B) As Percentage of Net Sales</b>				
Cost of Material Consumed	36.8	36.2	36.3	35.9
Employee Benefits Expense	9.4	9.1	9.2	8.8
Other Expenses	35.1	33.3	32.8	32.9
<b>(C) Measures of Financial Status</b>				
Debt / Equity (x)	0.2	0.1	0.1	0.1
Interest Coverage (x)	13.8	31.1	43.4	65.9
Average Cost Of Debt (%)	10.1	6.5	9.1	8.9
Debtors Period (days)	33.4	33.0	30.0	30.0
Closing stock (days)	44.8	42.0	40.0	38.0
Inventory Turnover Ratio (x)	8.1	8.7	9.1	9.6
Fixed Assets Turnover (x)	1.5	1.5	1.6	1.7
WC Turnover (x)	6.4	4.1	4.4	4.3
Non Cash WC (₹ Mn)	560	660	686	782
<b>(D) Measures of Investment</b>				
EPS (₹) (excl EO)	12.6	13.4	15.9	19.9
CEPS (₹)	15.8	18.1	21.2	25.8
DPS (₹)	2.0	4.0	7.0	8.0
Dividend Payout (%)	17.6	29.9	44.0	40.1
Profit Ploughback (%)	82.4	70.1	56.0	59.9
Book Value (₹)	48	66	74	84
RoANW (%)	26.2	26.9	22.8	25.2
RoACE (%)	26.7	32.3	31.6	36.0
RoAIC (%)	28.9	34.5	36.5	42.5
<b>(E) Valuation Ratios</b>				
CMP (₹)	383	383	383	383
P/E (x)	33.7	28.7	24.1	19.2
Market Cap. (₹ Mn)	13,107	13,763	13,763	13,763
MCap/ Sales (x)	3.5	3.3	2.8	2.4
EV (₹ Mn)	13,482	13,697	13,607	13,416
EV/Sales (x)	3.6	3.2	2.8	2.3
EV/EBDITA (x)	18.3	14.9	12.7	10.2
P/BV (x)	8.0	5.8	5.2	4.5
Dividend Yield (%)	0.5	1.0	1.8	2.1

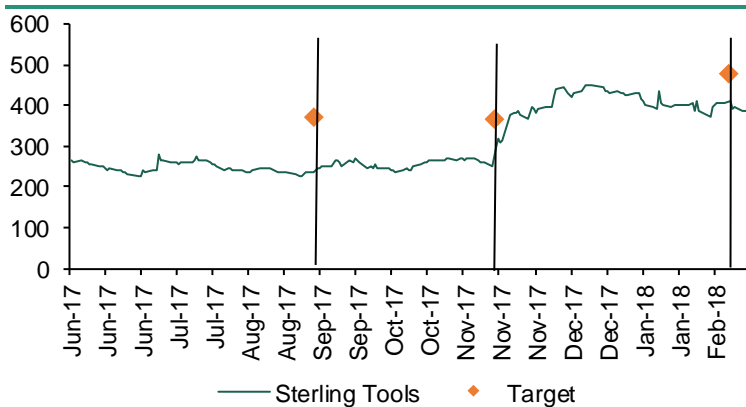
E – Estimates

## DART RATING MATRIX

Total Return Expectation (12 Months)

<b>Buy</b>	<b>&gt; 20%</b>
<b>Accumulate</b>	<b>10 to 20%</b>
<b>Reduce</b>	<b>0 to 10%</b>
<b>Sell</b>	<b>&lt; 0%</b>

## Rating and Target Price History



Month	Rating	TP (₹)	Price (₹)*
Sep-17	Buy	368	239
Nov-17	Buy	364	252
Feb-18	Accumulate	477	411

\* As on Recommended dated

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