

Weak numbers on an adverse product mix

Sterling (STL) reported weak results in Q4FY19. The revenue/EBITDA fell 10/22% YoY in the quarter, due to the slowdown in the automobile segment (especially CVs). The EBITDA margins was 13.7% (-205bps YoY/-77bps QoQ), on account of a weak product mix, commodity inflation, and negative operating leverage. Given the overall tepid demand for vehicles, higher inventory levels with dealers, and production cuts by the OEMs, we believe STL will likely remain under pressure for Q1FY20. However, we expect earnings will improve from Q2FY20, due to pre-buying on account of BS VI and a likely revival in economic activities. As STL focuses on specialized fasteners and the new manufacturing facility in Kolar becomes operational, we expect the margins to recover in coming quarters. We recommend Accumulate, with a TP of ₹ 234 (based on 16x FY21E EPS).

Capacity expansion

STL had planned a new manufacturing facility in Kolar, Karnataka, with a capacity of 5000-6000 MT and a capital outlay of ₹ 900mn. This facility is expected to start operations from H1FY20. STL has diversified segmental revenue with almost all the OEMs. As the CV segment contributes ~27% of revenue and is a high-margin business, revival in volume in the 2HFY20 will likely increase both volume and margin. We expect an 8% EPS CAGR over FY19-21E, led by a 7% revenue growth and 100bps margin expansion, offset by an increase in interest and depreciation cost.

Recovery in margin likely

Although Steel prices eased in 4QFY19(-4.7% QoQ) however, the gross margins remained under pressure. We believe the larger benefit of a decline in raw material price are yet to be reflected in the company's earnings. Hence, we expect an improvement in operating margin going forward. In addition to this, pre-buying in the CV segment in 2Q and 3Q of FY20 will also help add to margins.

Q4FY19 Result (₹ Mn)

Particulars	Q4FY19	Q4FY18	YoY (%)	Q3FY19	QoQ (%)
Revenue	1,183	1,312	(9.8)	1,233	(4.0)
Total Expense	1,021	1,106	(7.6)	1,055	(3.2)
EBITDA	162	206	(21.6)	178	(9.2)
Depreciation	50	42	18.7	48	4.4
EBIT	111	164	(32.1)	130	(14.2)
Other Income	17	15	11.8	11	56.1
Interest	16	10	66.8	6	146.7
EBT	113	170	(32.1)	134	(16.2)
Tax	39	52	(24.4)	52	(24.5)
RPAT	74	118	(37.7)	83	(11.1)
APAT	74	118	(37.7)	83	(11.1)
			(bps)		(bps)
Gross Margin (%)	58.4	60.8	(245)	61.7	(330)
EBITDA Margin (%)	13.7	15.7	(206)	14.4	(77)
NPM (%)	6.2	9.0	(278)	6.7	(49)
Tax Rate (%)	34.7	30.4	424	38.5	(378)
EBIT Margin (%)	9.4	12.5	(308)	10.5	(112)

CMP	₹ 204
Target / Upside	₹ 234 / 15%
BSE Sensex	39,439
NSE Nifty	11,844

Scrip Details

Equity / FV	₹ 72mn / ₹ 2
Market Cap	₹ 7bn
	US\$ 105mn
52-week High/Low	₹ 409/₹ 175
Avg. Volume (no)	10,953
NSE Symbol	STERTOOLS
Bloomberg Code	STRT IN

Shareholding Pattern Mar'19(%)

Promoters	65.3
MF/Banks/FIs	7.6
FIIIs	0.0
Public / Others	27.1

Valuation (x)

	FY19A	FY20E	FY21E
P/E	16.4	15.1	13.9
EV/EBITDA	9.1	7.8	6.9
ROE (%)	16.9	16.1	15.3
RoACE (%)	13.8	13.8	13.8

Estimates (₹ mn)

	FY19A	FY20E	FY21E
Revenue	5,122	5,580	5,887
EBITDA	859	983	1,045
PAT	449	487	527
EPS (₹)	12.5	13.5	14.6

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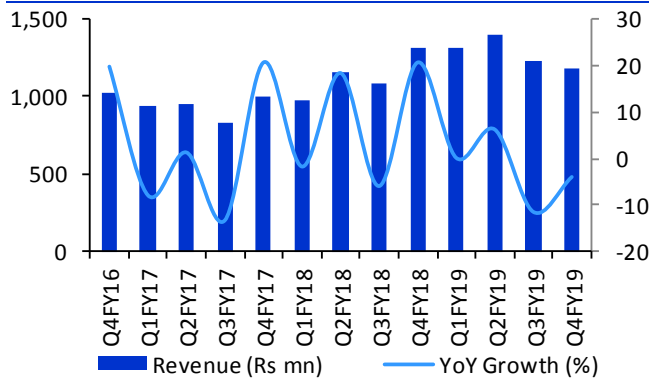
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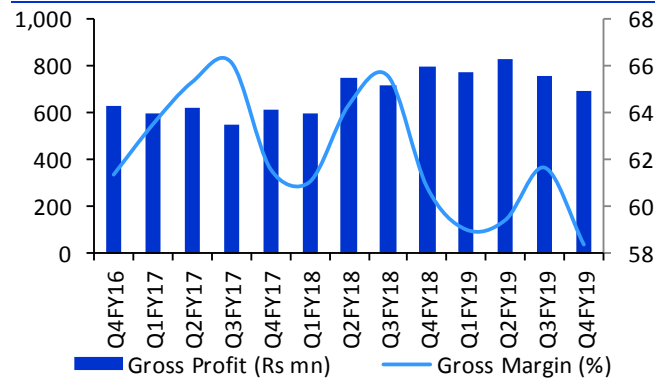
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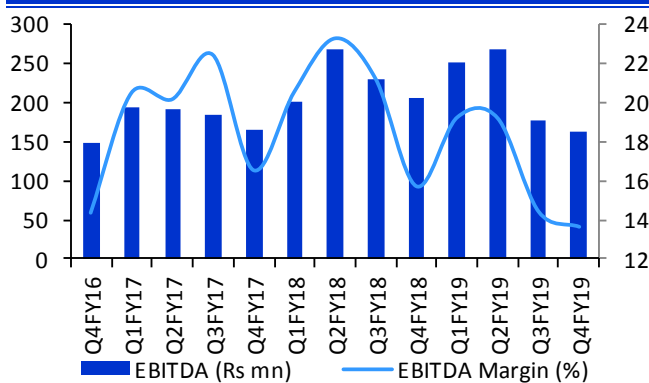
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Exhibit 1: Revenue declining on slowdown in OEMs


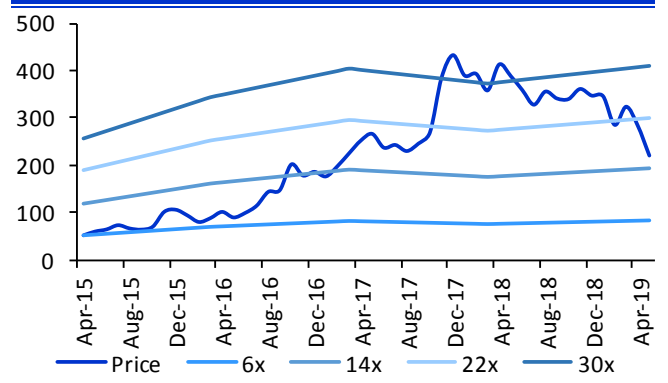
Source: DART, Company

Exhibit 2: Gross Margin Under Pressure


Source: DART, Company

Exhibit 3: EBITDA Margins Impacted on Weaker Mix


Source: DART, Company

Exhibit 4: P/E Band


Source: DART, Company

Profit and Loss Account

(₹ Mn)	FY18A	FY19A	FY20E	FY21E
Revenue	4,529	5,122	5,580	5,887
Total Expense	3,622	4,263	4,597	4,842
COGS	1,683	2,068	2,204	2,308
Employees Cost	335	358	412	474
Other expenses	1,605	1,836	1,981	2,060
EBIDTA	907	859	983	1,045
Depreciation	176	191	223	247
EBIT	731	669	760	798
Interest	38	37	76	58
Other Income	56	64	65	70
Exc. / E.O. items	0	0	0	0
EBT	749	696	749	810
Tax	263	247	262	284
RPAT	487	449	487	527
Minority Interest	0	0	0	0
Profit/Loss share of associates	0	0	0	0
APAT	487	449	487	527

Balance Sheet

(₹ Mn)	FY18A	FY19A	FY20E	FY21E
Sources of Funds				
Equity Capital	72	72	72	72
Minority Interest	0	0	0	0
Reserves & Surplus	2,408	2,770	3,152	3,573
Net Worth	2,480	2,842	3,224	3,645
Total Debt	364	1,039	839	639
Net Deferred Tax Liability	152	164	50	50
Total Capital Employed	2,996	4,045	4,113	4,334

Applications of Funds

Net Block	1,486	1,817	2,094	2,247
CWIP	98	468	400	250
Investments	189	229	179	179
Current Assets, Loans & Advances	1,775	2,103	2,037	2,306
Inventories	545	825	764	726
Receivables	455	422	459	500
Cash and Bank Balances	550	533	483	752
Loans and Advances	31	64	61	58
Other Current Assets	193	259	270	270
Less: Current Liabilities & Provisions	551	572	597	647
Payables	365	421	474	500
Other Current Liabilities	187	151	123	147
Net Current Assets	1,224	1,531	1,440	1,659
Total Assets	2,996	4,045	4,113	4,334

E – Estimates

Important Ratios

Particulars	FY18A	FY19A	FY20E	FY21E
(A) Margins (%)				
Gross Profit Margin	62.9	59.6	60.5	60.8
EBIDTA Margin	20.0	16.8	17.6	17.8
EBIT Margin	16.1	13.1	13.6	13.6
Tax rate	35.1	35.5	35.0	35.0
Net Profit Margin	10.7	8.8	8.7	8.9
(B) As Percentage of Net Sales (%)				
COGS	37.1	40.4	39.5	39.2
Employee	7.4	7.0	7.4	8.0
Other	35.4	35.8	35.5	35.0
(C) Measure of Financial Status				
Gross Debt / Equity	0.1	0.4	0.3	0.2
Interest Coverage	19.3	18.3	10.1	13.9
Inventory days	44	59	50	45
Debtors days	37	30	30	31
Average Cost of Debt	9.9	5.2	8.0	7.8
Payable days	29	30	31	31
Working Capital days	99	109	94	103
FA T/O	3.0	2.8	2.7	2.6
(D) Measures of Investment				
AEPS (₹)	13.5	12.5	13.5	14.6
CEPS (₹)	18.4	17.7	19.7	21.5
DPS (₹)	2.0	2.0	2.5	2.5
Dividend Payout (%)	14.8	16.1	18.5	17.1
BVPS (₹)	68.9	78.9	89.5	101.2
RoANW (%)	23.6	16.9	16.1	15.3
RoACE (%)	20.2	13.8	13.8	13.8
RoAIC (%)	31.7	22.5	21.3	22.1
(E) Valuation Ratios				
CMP (₹)	204	204	204	204
P/E	15.1	16.4	15.1	13.9
Mcap (₹ Mn)	7,338	7,338	7,338	7,338
MCap/ Sales	1.6	1.4	1.3	1.2
EV	7,151	7,844	7,695	7,225
EV/Sales	1.6	1.5	1.4	1.2
EV/EBITDA	7.9	9.1	7.8	6.9
P/BV	3.0	2.6	2.3	2.0
Dividend Yield (%)	1.0	1.0	1.2	1.2
(F) Growth Rate (%)				
Revenue	22.1	13.1	9.0	5.5
EBITDA	19.8	(5.2)	14.4	6.3
EBIT	23.8	(8.5)	13.6	5.0
PBT	24.1	(7.1)	7.7	8.1
APAT	24.1	(7.8)	8.6	8.1
EPS	24.1	(7.8)	8.6	8.1

Cash Flow

(₹ Mn)	FY18A	FY19A	FY20E	FY21E
CFO	544	363	712	882
CFI	(356)	(932)	(382)	(250)
CFF	261	555	(381)	(363)
FCFF	191	(529)	280	632
Opening Cash	28	550	533	483
Closing Cash	550	533	483	752

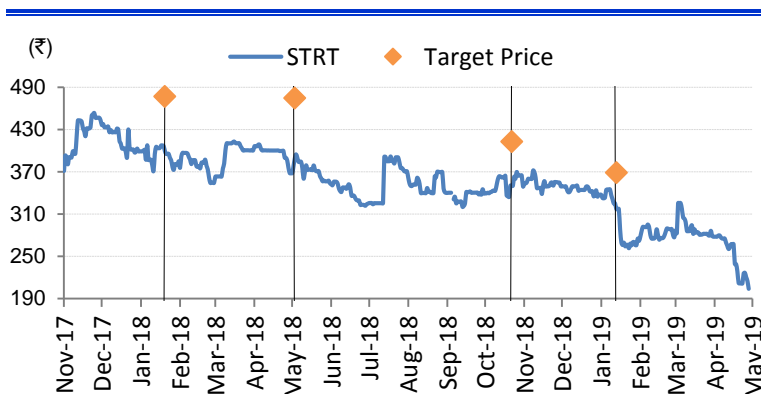
E – Estimates

DART RATING MATRIX

Total Return Expectation (12 Months)

Buy	> 20%
Accumulate	10 to 20%
Reduce	0 to 10%
Sell	< 0%

Rating and Target Price History



Month	Rating	TP (₹)	Price (₹)
Feb-18	Accumulate	477	399
May-18	Buy	475	389
Nov-18	Accumulate	413	350
Feb-19	Accumulate	369	317

*Price as on recommendation date

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