East India Securities Ltd
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INDIA

Suprajit Engineering Ltd.

Strong fundamentals and de-risking strategy to lead future growth

An exceptional operational beat, while PAT impacted due to impairment provision for Wescon of Rs ~166mn. Also, provision of Rs ~109mn (~10% of invested amount) was created on its investments. Yearly performance was commendable looking at subdued auto industry performance. For FY21, we expect a poor demand from Indian OEMs, while incremental growth to come from the combination of aftermarket, exports and an increase in the content per vehicle. Major Global OEMs plans to de-risk from China & results are already visible in the strong export pipeline of Suprajit Engineering (SEL). The management is fully geared up to provide the required focus for its strategically important SENA strategy, while Phoenix Lamps incremental growth will majorly come from Osram's orders and aftermarket. Stringent cost rationalisation measures, softness in commodity prices, better product mix and strong aftermarket to provide required support to the margins. We believe SEL would maintain its dominant leadership and has enormous growth potential in all of its three segments in the domestic as well as exports. Maintain Buy.

Auto cables outperformance to continue in FY21e

- Global OEMs started working on derisking from China's supplies. Thiu is likely to benefit Suprajit. The results are already visible in the strong exports order pipeline for the company.
- It is a dominant leader in 2W cable market and has been gaining market share in 4W cables, where volumes as well as realisation is higher. With growth from aftermarket (20% YoY in FY20) & exports, Suprajit is set to outbeat the industry.
- Due to changes in the technical specification post BS6 & introduction of CBS, the value per cable to increase by 2-3%. Additional business to flow in due to CF issues in a few of its competitors.

Geared up for strategically important SENA

- The performance since acquisition was not upto the mark majorly due to leadership issues.
- The management is fully geared up to provide all the required focus, made changes in the top management and is providing proper road-path for future.
- Now, the core three-member team from India is guiding the management of Wescon to expedite changes and aid in the transformation.

Commendable margin performance to get further support

- Stringent cost rationalisation exercise, salary cuts, reduction in capex & curtailing all possible discretionary spends would bring down its break-even levels and will be a long term positive.
- Softness in commodity prices, better product/geographic mix, strong aftermarket (where margins are higher) to give a further push to the margins in subdued environment.

Trading at a favourable valuation

- We are strongly convinced on SEL's business model, its competitive positioning & growth potential in the medium to long term. Year on year outperformance is noticeable. We believe it should get a scarcity premium for its dominant leadership and is a strong re-rating candidate.
- **We have assigned 16x (~30% discount to its 1-year forward PE due to near term uncertainty) to its FY22e EPS of Rs 9.7 to arrive at a target price of Rs 156. Hence, we maintain 'Buy'.**

Rating: **Buy**	Upside/(Downside): **19.3%**
Current Price: **131**	Target Price: **156**

|Market data

Bloomberg:	SEL IN
52-week H/L (Rs):	220/100
Mcap (Rs bn/USD bn):	18.3/0.2
Shares outstanding (mn):	140
Free float:	56.0%
Daily vol. (3M Avg. – '000):	377
Face Value (Rs):	1.0
Group:	BSE 500

Source: Bloomberg, EISEC Research

|Shareholding pattern (%)

	Mar-20	Dec-19	Sep-19	Jun-19
Promoter	44.6	44.6	44.6	44.5
FIIs	8.1	11.3	13.0	12.0
DIIs	9.2	6.8	5.5	5.1
Public/others	38.1	37.3	36.9	38.4

Source: BSE

|Price performance (%)*

	1M	3M	12M	36M
BSE 500	9.0	3.7	-15.9	-2.5
SEL	9.0	-21.6	-40.6	-55.7

*as on 15th June 2020; Source: AceEquity, EISEC Research

Consolidated (Rs mn)	Q4FY20	Q4FY19	YoY (%)	Q3FY20	QoQ (%)	Q4FY20e	Var. (%)
Total Income	**3,890**	**4,311**	**-9.8**	**4,123**	**(5.6)**	**3,460**	**12.4**
Op. cost	3,434	3,573	-3.9	3,622	(5.2)	3,005	14.3
EBITDA	**549**	**635**	**-13.6**	**501**	**9.7**	**455**	**20.7**
EBITDA margin (%)	14.1	14.7	(62) bps	12.1	197 bps	13.2	97 bps
Other income	42	125	-66.2	53	(19.6)	107	(60.3)
PBT	**115**	**594**	**-80.6**	**353**	**(67.3)**	**426**	**(73.0)**
Taxes paid	86	177	-51.6	41	108.2	133	(35.5)
Effective tax rate (%)	74.2	29.8	4,448 bps	11.6	6,258 bps	31.1	4,310 bps
Adj. PAT	**244**	**417**	**-41.5**	**312**	**(21.7)**	**294**	**(16.8)**
Adj. PAT margin (%)	6.3	9.7	(340) bps	7.6	(128) bps	8.5	(221) bps

Soure: Company, EISEC Research

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Y/E Mar (Rs mn)	Revenue	YoY (%)	EBITDA	EBITDA (%)	PAT	YoY (%)	EPS	RoE (%)	RoCE (%)	P/E (x)	EV/EBITDA (x)
FY18	14,311	19.0	2,365	16.5	1,385	21.8	9.9	23.5	16.6	28.4	17.9
FY19	15,899	11.1	2,328	14.6	1,338	-3.4	9.6	18.7	14.0	25.0	15.7
FY20	15,628	-1.7	2,187	14.0	1,040	-22.3	7.4	12.8	12.1	17.6	9.4
FY21e	13,212	-15.5	1,584	12.0	760	-26.9	5.4	8.6	7.3	24.1	11.8
FY22e	17,102	29.4	2,409	14.1	1,362	79.3	9.7	14.0	11.5	13.4	7.5

Source: Company, EISEC Research Estimates

Q4FY20 Analysts Call Highlights

Q4FY20 – a quick overview

- ✓ **Operational beat:** Revenues as well as margin beat were led by strong performance in auto cable as well as non-auto cable division, while Phoenix segment revenues were a little lower than the expectation.
- ✓ **PAT impacted due to one-off provisions and lower other income,** which was higher in the base quarter due to forex benefits, accrued appreciation of funds.
- ✓ **Exceptional items relate to** 1) impairment provision created for its subsidiary Wescon Controls LLC of Rs 165.85mn and 2) Provision of Rs 108.53mn (~10% of invested amount) on investments in Franklin Templeton fixed-income debt scheme. Overall, a superior operational performance in a challenging environment.
- ✓ Apart from this, there were few one-off costs incurred by its subsidiaries to the tune of Rs 200mn. These costs are related to cleaning up of inventories, restructuring & modification of plant layouts, setting up new warehouses, etc.
- ✓ **Yearly performance much ahead of overall industry:** Considering dismal auto industry performance in FY20, Suprajit's yearly performance is commendable. Its FY20 revenue marginally declined by 1.7% YoY to Rs 15.6bn, while EBITDA Margin held strongly in the guided range at 14.0% and Adj. PAT declined marginally by 1.9% YoY to Rs 1.3bn in FY20. This performance came when domestic automobile industry reported a decline of 15%.

Auto cables division

- ✓ In the 4th quarter, the company generates a good amount of revenues, but due to Covid situation, ***the revenues were lower (-10% to Rs 3.9bn), still substantially outperformed the auto industry (which degrew by 22% in Q4FY20).*** Also, OEM sales were affected due to transition from BS4 to BS6.
- ✓ ***The company sees incremental revenues to come from the combination of Aftermarket, exports and an increase in the content per vehicle.***
- ✓ There has been an increase in the content due to extra cable required for CBS, also due to changes in the specification & length of a cable (post BS6), the value per cable to increase. Aftermarket to report strong numbers (FY20 seen 20% YoY growth), while good pipeline of orders is there in exports as well.
- ✓ Overall, incrementally there would be an additional 2-3% increase in the revenues only due to increase in content.

Non-auto cables division

- ✓ Since last 6-9 months, Suprajit management expedited the strategy to improve the SENA division. The core three-member team from India is guiding the management team of Wescon to expedite changes and aid in the transformation. The management claimed that results are visible and the confidence has been improved.
- ✓ The revenues are largely at similar levels since last few years as the management could not able to give required focus on the same. There were leadership issues as well in that business.
- ✓ ***The management is now fully geared up to provide all the required focus. Leadership has been changed and the company is going to provide proper road-path going ahead. Giving a strategic three plants option to the customers for winning new businesses. Now, we expect things to improve.***

Phoenix Lamps division

- ✓ Osram is happy with the performance of Phoenix. The company has recently commissioned exports in Europe through Osram.
- ✓ Restructuring exercise conducted in subsidiaries of Phoenix (Trifa & Luxlite). One-time costs incurred like consolidation costs of warehouse into a single

larger newly located warehouse, one-time employee settlements, inventory provisions, etc.

- ✓ The onetime restructuring exercise and lower operating leverage, resulted in a decline of 600bps YoY to 4.3% in EBITDA Margin for the 4th quarter.

Exports

- ✓ The management sees positive benefits due to vendor consolidation and continuously sees increasing export business opportunities in auto cables.
- ✓ ***The opportunity is coming as Global OEMs have plans to reduce their vendors and to derisk from China. Suprajit could be a possible beneficiary of derisking exercise.***
- ✓ The results are already visible as Suprajit started getting a larger share of business from existing clients and getting orders as well from a new set of clients.

Margin

- ✓ Employees as well as management team decided to take a voluntary pay cut from 5% to 40% depending upon seniority.
- ✓ The company has reduced discretionary expenses. All the major capex was over in FY20 and hence only maintenance capex is required for the next two years. The strategically important expense like automation, etc will continue.
- ✓ Micro managing the company to curtail all the unnecessary spends, trying to improve productivity per man-day, etc.
- ✓ ***All these cost restructuring exercise to bring down the break-even level and will be a long term positive as cost structure will come down.***
- ✓ Going forward, all this will support margins. This, along with the ***softness in commodity prices, better product mix and strong aftermarket to give a further push to the margins.***
- ✓ The margin in FY21e is guided in the range of 10-14%, this is majorly due to significant uncertainties especially in India. The company would continue to outbeat the industry on the revenue growth front, but its difficult to predict margin trajectory for FY21e.

Acquisition plans

- ✓ The management is always hunt for a value acquisition and it sees good opportunities due to Covid as liquidity and cash flows of many auto component players have become weak.
- ✓ The company sees additional business could flow in to Suprajit as some of the company's competitors are facing CF issues.

Other highlights

- ✓ The company reviews its critical investments once in 2-3 years. The valuation exercise done by the 3rd party. These are a one-time exercise and all done & dusted.
- ✓ Suprajit has sufficient cash and undrawn facilities. The company has got some minor support from the US and Europe Governments due to Covid.

Valuation and Recommendations

Exceptional operational beat, while PAT impacted due to impairment provision for Wescon of Rs ~166mn and provision of Rs ~109mn (~10% of invested amount), created on its investments. Yearly performance was commendable looking at subdued auto industry performance.

We expect poor demand from Indian OEMs, while incremental growth to come from the combination of aftermarket, exports and an increase in the content per vehicle. Major Global OEMs plans to de-risk from China & results are already visible in the strong export pipeline of Suprajit.

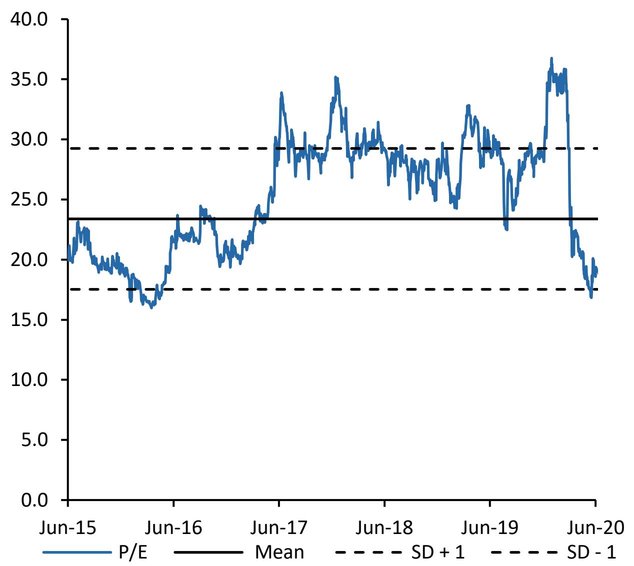
The management is fully geared up to provide the required focus for its strategically important SENA strategy, while Phoenix Lamps incremental growth will majorly come from Osram's orders and aftermarket.

Stringent cost rationalisation measures, softness in commodity prices, better product mix and strong aftermarket to provide required support to the margins. We believe the company to maintain its dominant leadership and has enormous growth potential in all of its three segments in the domestic as well as exports.

We are strongly convinced on SEL's business model, its competitive positioning & growth potential in the medium to long term. Year on year outperformance is noticeable. We believe it should get a scarcity premium for its dominant leadership and is a strong re-rating candidate.

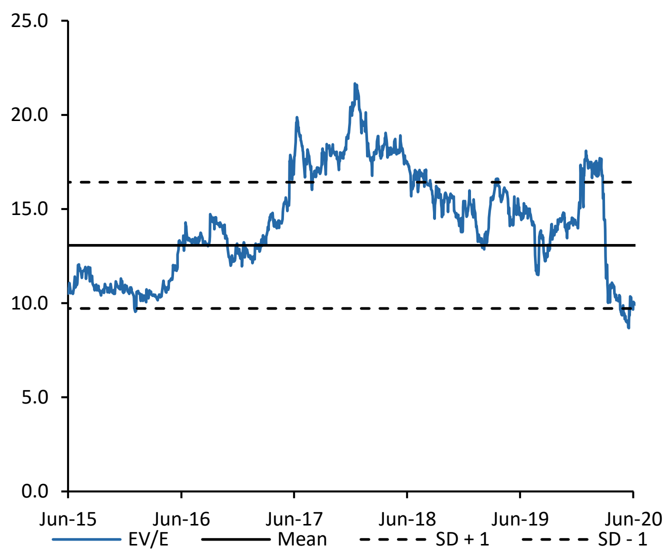
We have assigned 16x (~30% discount to its 1-year forward PE due to near term uncertainty) to its FY22e EPS of Rs 9.7 to arrive at a target price of Rs 156. Hence, we recommend 'Buy'.

Fig 1: 1-year forward P/E



Source: AceEquity, EISEC Research

Fig 2: 1-year forward EV/EBITDA



Source: AceEquity, EISEC Research

Quarterly financials, operating metrics and key performance indicators

Fig 3: Quarterly Financials

Consolidated (Rs mn)	Q1FY19	Q2FY19	Q3FY19	Q4FY19	Q1FY20	Q2FY20	Q3FY20	Q4FY20
Net Sales	**3,618**	**3,914**	**4,056**	**4,311**	**3,634**	**3,982**	**4,123**	**3,890**
Raw Materials	2,012	2,265	2,347	2,524	2,073	2,366	2,430	2,283
Employee Costs	712	764	762	798	720	725	770	712
Other Expenditure	339	353	340	354	329	334	422	347
EBITDA	**554**	**531**	**607**	**635**	**513**	**558**	**501**	**549**
Depreciation	99	102	104	107	128	159	149	145
Interest	64	64	58	60	66	52	52	57
Other Income	41	30	184	125	62	134	53	42
Exceptional items								-274
PBT	**433**	**396**	**630**	**594**	**380**	**480**	**353**	**115**
Tax	145	155	238	177	132	30	41	86
Tax rate (%)	33	39	38	30	35	6	12	74
Reported PAT	288	241	392	417	249	450	312	30
Adj. PAT	**288**	**241**	**392**	**417**	**249**	**450**	**312**	**244**
YoY Growth (%)								
Revenue	*4.7*	*16.3*	*10.7*	*6.1*	*0.4*	*1.7*	*1.6*	*-9.8*
EBITDA	*20.8*	*-5.1*	*0.9*	*-13.5*	*-7.5*	*4.9*	*-17.4*	*-13.6*
Adj. PAT	*27.4*	*-23.1*	*38.8*	*-25.9*	*-13.7*	*86.9*	*-20.4*	*-41.5*
QoQ Growth (%)								
Revenue	*-11.0*	*8.2*	*3.6*	*6.3*	*-15.7*	*9.6*	*3.5*	*-5.6*
EBITDA	*-24.5*	*-4.1*	*14.2*	*4.7*	*-19.3*	*8.7*	*-10.2*	*9.7*
Adj. PAT	*-48.9*	*-16.5*	*62.9*	*6.5*	*-40.5*	*80.9*	*-30.6*	*-21.7*
Margin (%)								
EBITDA	*15.3*	*13.6*	*15.0*	*14.7*	*14.1*	*14.0*	*12.1*	*14.1*
Adj. PAT	*8.0*	*6.1*	*9.7*	*9.7*	*6.8*	*11.3*	*7.6*	*6.3*

Source: Company, EISEC Research

Fig 4: Key Assumptions

Key assumptions	FY18	FY19	FY20P	FY21e	FY22e
Auto cable division					
Revenue (Rs mn)	**8,081**	**9,319**	**9,199**	**7,770**	**10,505**
YoY Growth (%)	*34.7%*	*15.3%*	*-1.3%*	*-15.5%*	*35.2%*
% of total revenues	*56.5%*	*58.6%*	*58.9%*	*58.8%*	*61.4%*
EBITDA Margin (%)	**17.1%**	**15.7%**	**15.5%**	**13.5%**	**15.6%**
Non-Auto cable division					
Revenue (Rs mn)	**3,000**	**3,395**	**3,396**	**3,052**	**3,453**
YoY Growth (%)	*7.1%*	*13.2%*	*0.0%*	*-10.1%*	*13.1%*
% of total revenues	*21.0%*	*21.4%*	*21.7%*	*23.1%*	*20.2%*
EBITDA Margin (%)	**16.3%**	**14.6%**	**14.1%**	**10.4%**	**11.9%**
Phoenix lamps division					
Revenue (Rs mn)	**3,230**	**3,184**	**3,033**	**2,390**	**3,144**
YoY Growth (%)	*0.0%*	*-1.4%*	*-4.8%*	*-21.2%*	*31.6%*
% of total revenues	*22.6%*	*20.0%*	*19.4%*	*18.1%*	*18.4%*
EBITDA Margin (%)	**12.1%**	**11.6%**	**11.1%**	**9.2%**	**11.5%**

Source: Company, EISEC Research Estimates

Consolidated Financial Statements

Income Statement					
YE March (Rs mn)	**FY18**	**FY19**	**FY20P**	**FY21e**	**FY22e**
Revenues	**14,311**	**15,899**	**15,628**	**13,212**	**17,102**
% Growth	19.0	11.1	(1.7)	(15.5)	29.4
Raw Materials	8,007	9,148	9,151	7,826	10,010
% of sales	55.9	57.5	58.6	59.2	58.5
Personnel	2,568	3,037	2,927	2,705	3,281
% of sales	17.9	19.1	18.7	20.5	19.2
Manufacturing & Other Expenses	1,371	1,386	1,364	1,096	1,401
% of sales	9.6	8.7	8.7	8.3	8.2
EBITDA	**2,365**	**2,328**	**2,187**	**1,584**	**2,409**
EBITDA Margin (%)	16.5	14.6	14.0	12.0	14.1
Depreciation & Amortization	372	410	581	607	646
EBIT	**1,993**	**1,918**	**1,606**	**977**	**1,763**
Finance Cost	271	246	227	207	190
PBT From Operations	**1,722**	**1,672**	**1,379**	**770**	**1,573**
Other Income	212	380	224	245	247
Exceptional Income/(Expense)	0	0	-274	0	0
PBT	**1,934**	**2,052**	**1,329**	**1,015**	**1,820**
Tax-Total	549	714	289	256	458
Effective tax rate (%)	28.4	34.8	21.8	25.2	25.2
Reported PAT	**1,385**	**1,338**	**1,040**	**760**	**1,362**
PAT Margin	9.7	8.4	6.7	5.7	8.0
% Growth	21.8	(3.4)	(22.3)	(26.9)	79.3

Source: Company, EISEC Research Estimates

Key Ratios					
YE March	**FY18**	**FY19**	**FY20P**	**FY21e**	**FY22e**
Growth Ratios (%)					
Net Sales	19.0	11.1	(1.7)	(15.5)	29.4
EBITDA	17.1	(1.6)	(6.0)	(27.6)	52.0
Adjusted Net Profit	21.8	(3.4)	(22.3)	(26.9)	79.3
Margin Ratio (%)					
EBITDA Margin	16.5	14.6	14.0	12.0	14.1
EBIT Margin	15.4	14.5	11.7	9.3	11.8
PBT margins	12.0	10.5	8.8	5.8	9.2
PAT Margin	9.7	8.4	6.7	5.7	8.0
Return Ratios					
ROE	23.5	18.7	12.8	8.6	14.0
ROCE	16.6	14.0	12.1	7.3	11.5
ROIC	14.6	11.7	11.6	7.4	13.0
Turnover Ratios (days)					
Gross Block Turnover (x)	2.4	2.5	2.3	1.8	2.2
Inventory	108	108	110	108	106
Debtors	74	67	64	63	61
Creditors	83	70	85	86	87
Cash Conversion Cycle	98	105	89	85	80
Solvency ratio (x)					
Debt-equity	0.5	0.5	0.4	0.4	0.3
Net Debt-Equity	0.3	0.2	0.1	(0.0)	(0.1)
Gross Debt/EBITDA	1.5	1.6	1.7	2.2	1.3
Current ratio	1.5	1.7	1.5	1.7	1.9
Interest coverage ratio	7.4	7.8	7.1	4.7	9.3
Dividend					
DPS (Rs.)	1.4	1.6	1.8	0.9	1.9
Dividend Yield (%)	1.1	1.2	1.3	0.7	1.5
Dividend Payout (%)	14.1	16.2	23.5	16.0	20.0
Per share (Rs.)					
Basic EPS (reported)	9.9	9.6	7.4	5.4	9.7
FDEPS (Adjusted)	9.9	9.6	7.4	5.4	9.7
CEPS	12.6	12.5	11.6	9.8	14.4
BV	46.8	55.4	61.0	65.6	73.4
Valuation					
P/E	28.4	25.0	17.6	24.1	13.4
P/BV	6.0	4.3	2.1	2.0	1.8
EV/EBITDA	17.9	15.7	9.4	11.8	7.5
EV/Sales	3.0	2.3	1.3	1.4	1.1

Source: Company, EISEC Research Estimates

Balance Sheet					
YE March (Rs mn)	**FY18**	**FY19**	**FY20P**	**FY21e**	**FY22e**
Sources of funds					
Capital	140	140	140	140	140
Reserves & Surplus	6,409	7,611	8,398	9,036	10,126
Shareholders' Funds	**6,549**	**7,751**	**8,538**	**9,176**	**10,265**
Total Loan Funds	**3,455**	**3,621**	**3,781**	**3,462**	**3,171**
Deffered tax liabilities	521	635	563	476	616
Other liabilities	2,494	2,466	2,924	2,476	3,405
Total Liabilities	**13,018**	**14,472**	**15,805**	**15,589**	**17,457**
Application of funds					
Gross Block	6,080	6,576	7,266	7,480	7,811
Accumulated Dep.	632	1,038	1,388	1,995	2,641
Net Block	5,448	5,539	5,878	5,485	5,170
Capital WIP	25	266	145	145	136
Net Assets	**5,473**	**5,805**	**6,023**	**5,631**	**5,306**
Investments	**0**	**0**	**890**	**890**	**890**
Other non current assets	**274**	**377**	**407**	**382**	**434**
Inventories	2,365	2,710	2,762	2,316	2,907
Sundry Debtors	2,890	2,916	2,750	2,280	2,858
Cash & Bank Balances	328	534	694	2,165	2,569
Loans and Advances	6	6	10	8	11
Other current Assets	1,683	2,124	2,268	1,918	2,482
Total Current Assets	**7,272**	**8,290**	**8,484**	**8,687**	**10,827**
Sundry Creditors	**1,824**	**1,751**	**2,140**	**1,844**	**2,386**
Other Current Liabilities	2,835	3,159	3,531	3,175	3,251
Provisions	95	102	118	100	129
Total Current Liabilities	**4,754**	**5,012**	**5,789**	**5,118**	**5,766**
Net Current Assets	**2,518**	**3,278**	**2,695**	**3,569**	**5,061**
Total Assets	**13,018**	**14,472**	**15,805**	**15,589**	**17,457**

Source: Company, EISEC Research Estimates

Cash Flow					
YE March (Rs mn)	**FY18**	**FY19**	**FY20P**	**FY21e**	**FY22e**
Operating profit before WC changes	**2,449**	**2,651**	**2,134**	**1,828**	**2,654**
Net chg in working capital	37	(526)	(159)	421	(318)
Income taxes paid	(314)	(677)	(289)	(256)	(458)
Cash flow from operating activities (a)	**2,173**	**1,448**	**1,686**	**1,994**	**1,878**
Capital expenditure	(250)	(587)	(1,068)	(214)	(321)
Free Cash Flow	1,923	860	618	1,780	1,556
Cash flow from investing activities (b)	**(1,250)**	**(890)**	**(1,218)**	**(225)**	**(804)**
Cash flow from financing activities (c)	**(845)**	**(418)**	**(64)**	**(544)**	**(685)**
Net chg in cash (a+b+c)	**77**	**140**	**405**	**1,225**	**389**

Source: Company, EISEC Research Estimates

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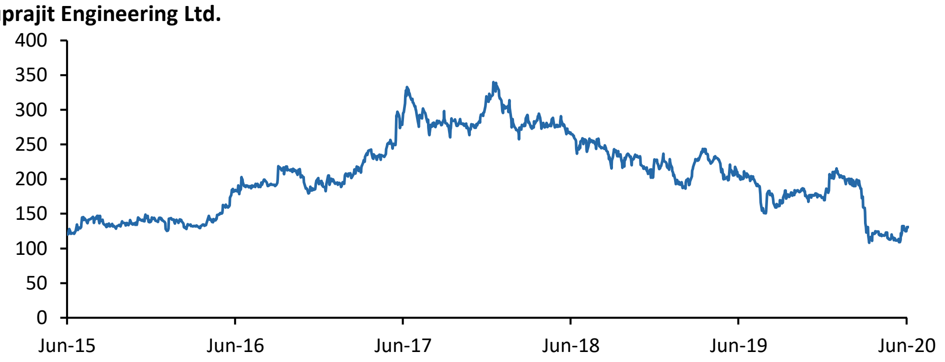
Suprajit Engineering Ltd.



Source: ACEEquity, EISEC Research

Analyst holding in stock: **NO**

Key to EISEC Investment Rankings

Buy: Upside by>15%, Accumulate: Upside by 5%to 15%, Hold: Downside/Upside by -5% to +5%, Reduce: Downside by 5% to 15%, Sell: Downside by>15%

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