

July 3, 2020

Mega restructuring: Equity dilution lies ahead...

The board of directors at Motherson Sumi Systems (MSSL) approved a business restructuring plan, which is a tad more inclusive than plans shared earlier. As part of plan in the **first leg of transaction**, MSSL would demerge **domestic wiring harness (DWH)** business into a separate entity, mirroring the shareholding of the listed entity i.e. MSSL. In the **second leg of transaction**, however, MSSL now plans to acquire all other lines of promoter's business in auto ancillary as well as support functions including 49% stake in SMRP BV (SMR+ SMP) hosted in Samvardhana Motherson International (SAMIL) vs. the initial plans on just acquiring the 49% stake in SMRP BV hosted in SAMIL. For the second leg of the transaction, it plans to issue 136 crore new shares to promoters with promoter's stake increasing from 36.4% to 50.4%. **Investors may now find comfort in all promoter's line of businesses being consolidated into one entity (MSSL+SAMIL). The valuation at which SAMIL is envisaged to be merged with MSSL appears to be fair and is not adverse to the interest of minority shareholders. However, we do not see much upside in the stock price of MSSL given the healthy valuations at which it is trading amid complex nature of business with varied geographical and currency risk.**

Demerger of DWH business fulfils partner's long-standing need

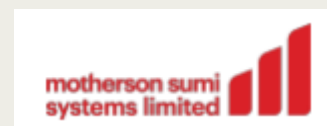
The domestic wiring harness business (DWH) would be demerged into a separate entity and listed on bourses later (MSSL will hold 33.4% stake in the company), with overall shareholding mirroring that of the parent. MSSL shareholders would get one share in DWH for every share in MSSL. The move enables long time JV partner Sumitomo Wiring Systems (SWS) of Japan to retain focus on India PV business (ex-Hyundai and Kia). In FY20, DWH clocked revenue of ~₹ 3,950 crore, EBITDA of ~₹ 530 crore with corresponding margins at 13.4% and RoCE at ~55% and PAT of ₹ 286 crore. The DWH business has potential to command higher P/E multiple vs. the base business at MSSL given its impressive return ratios matrix. Our back of the envelopment calculation suggests a fair value of ~₹ 7,000 crore (~₹ 22/share) for this business.

SAMIL buyout, high equity dilution (~43%) in offing...

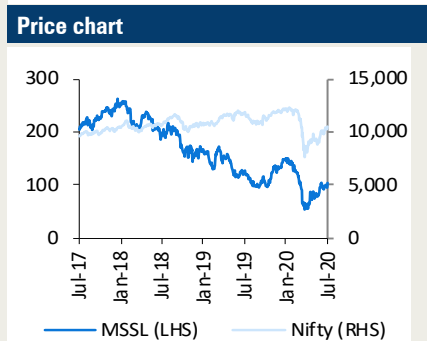
MSSL would acquire & merge promoter group (SAMIL) into itself against earlier proposal to buy out SAMIL's 49% stake in SMRP BV. Effectively, this would consolidate all the group's automotive businesses (ex-DWS) as well as other supporting businesses under the umbrella of the listed entity i.e. MSSL. **MSSL would issue ~136 crore new shares, diluting equity share base by ~43% to 452 crore shares from present 316 crore shares. This would be an effective equity acquisition value of ~₹ 8,300 crore and an EV valuation of ~₹ 9,400 crore (net debt at SAMIL at ~₹ 1,100 crore) for an incremental absolute effective EBITDA of ~₹ 1,500-1,600 crore (large part from SMRP BV) i.e. ~6.0x EV/EBITDA vs. the prevailing MSSL valuation of ~7x EV/EBITDA, all on FY20 numbers. The management felt that the transaction would be EPS accretive from the first year of merger.**

Valuation & Outlook

MSSL is a global auto ancillary player with varied exposure to different geographies, foreign currencies as well as product profile. MSSL is, however, relatively better placed with respect to EV disruption. Given the complexities and healthy valuations at which it trades i.e. ~18x P/E, ~2.5x P/B with the return ratios metrics of mid-teens on FY22E numbers, we see limited upside to our target price calculation. We value MSSL at ₹ 105 i.e. 19x P/E on FY22E EPS of ₹ 5.4 with a **HOLD** rating on the stock.



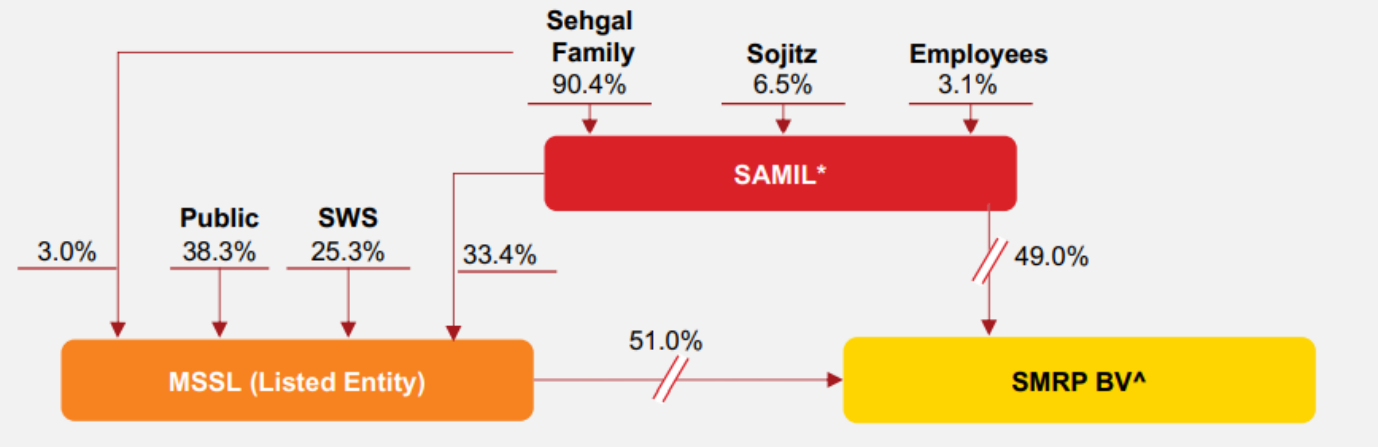
Particulars	
Particular	₹ crore
Market Capitalization	31,579.3
Total Debt (FY 20P)	11,669.1
Cash & Inv. (FY 20P)	4,878.9
EV (₹ Crore)	39,555.2
52 week H/L (₹)	151 / 49
Equity capital	₹ 315.8 Crore
Face value	₹ 1



- #### Key Highlights
- Domestic wiring harness business to be demerged into separate entity with 33.4% MSSL stake and listed on bourses. Overall shareholding to mirror that of MSSL
 - Promoter group SAMIL to be merged into MSSL and would entail ~43% equity dilution on present base. Valuation of merging SAMIL appears to be fair and is not adverse to interest of minority shareholders
 - Investors now to be able to participate in 100% of SMRPBV's expected operational improvement in coming years
 - Maintain **HOLD** with revised target price of ₹ 105

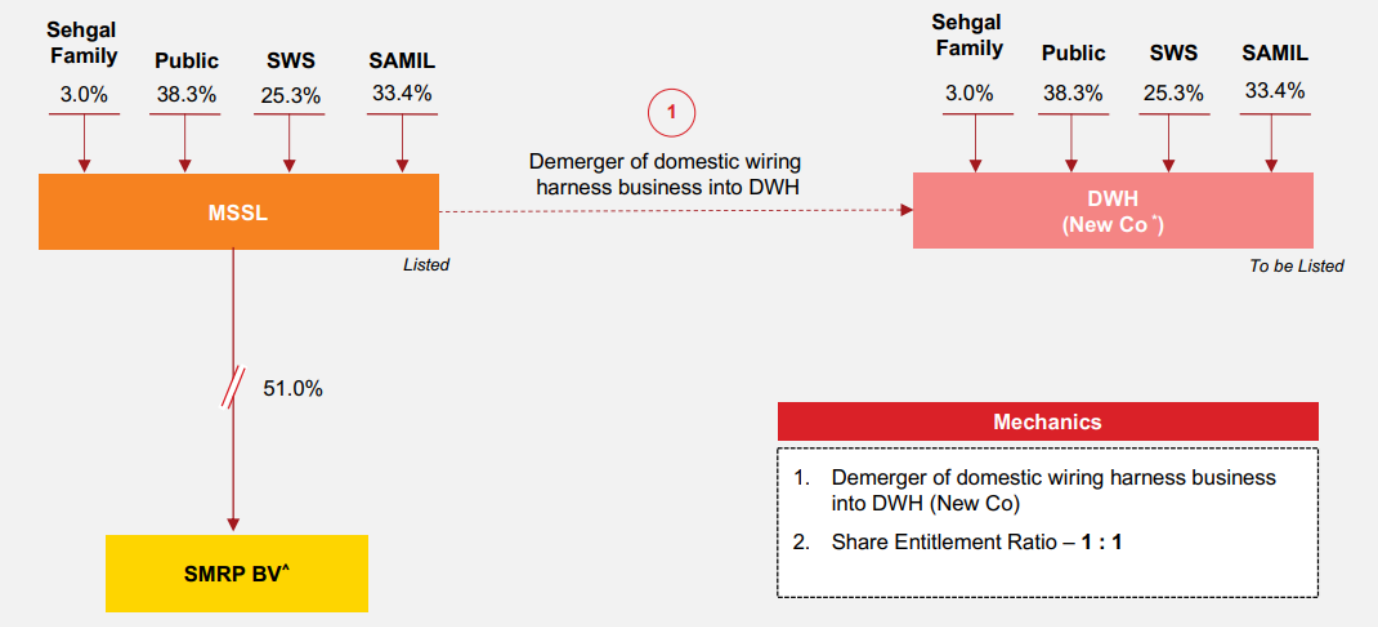
Research Analyst
 Shashank Kanodia, CFA
 shashank.kanodia@icicisecurities.com
 Jaimin Desai
 jaimin.desai@icicisecurities.com

Exhibit 1: Current group holding structure



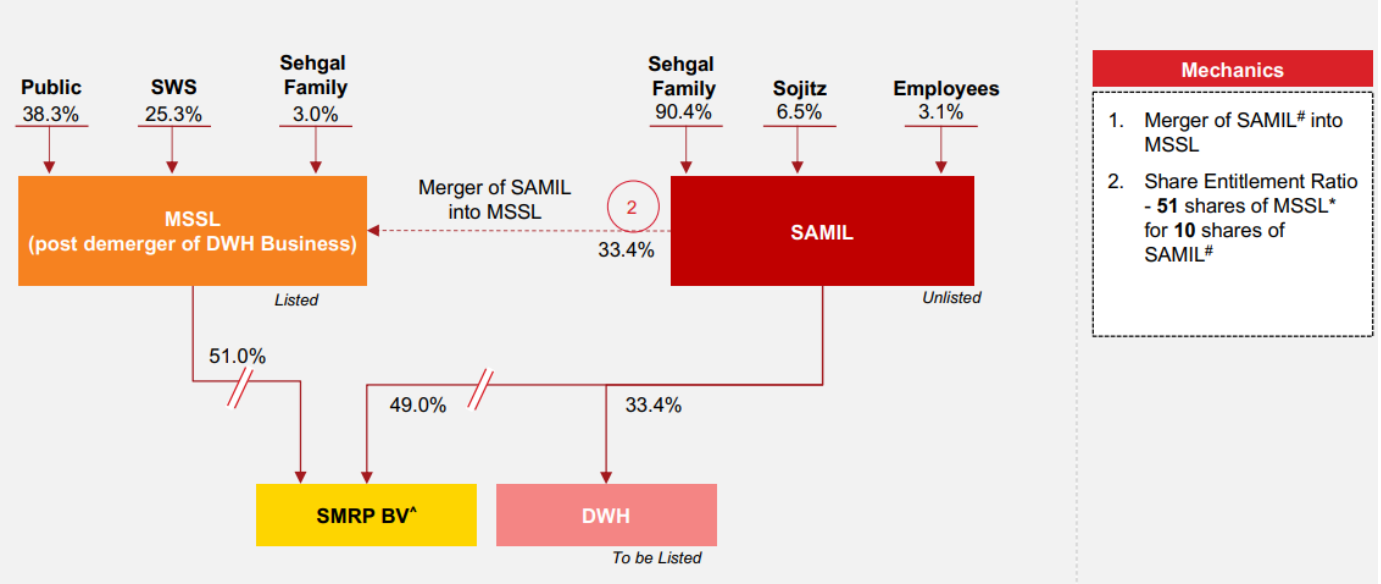
Source: Company, ICICI Direct Research

Exhibit 2: Vertical demerger of domestic wiring harness business into DWH



Source: Company, ICICI Direct Research

Exhibit 3: Merger of SAMIL into MSSL



Source: Company, ICICI Direct Research

Post restructuring transactions, MSSL would hold 100% in SMRPBV, 33.4% in DWS; promoter holding in MSSL is set to increase from 36.4% to 50.4%.

Exhibit 4: Summary proforma financials (₹ crore)

Particulars	MSSL standalone ex DWH (a)		MSSL consolidated ex DWH (b)		SAMIL (c)		Combined (b +c)	
	FY19	FY20	FY19	FY20	FY19	FY20	FY19	FY20
Net revenue	4,369.4	400.9	60,420.6	60,752.9	1,390.7	1,286.3	61,490.6	61,624.8
EBITDA	674.7	689.8	5,254.0	4,917.3	180.0	126.3	5,434.0	5,043.4
EBITDA margin (%)	15.4	17.2	8.7	8.1	12.9	9.8	8.8	8.2
EBIT	484.6	458.5	2,880.2	2,196.3	102.1	32.4	2,982.3	2,228.5
EBIT margin (%)	11.1	11.4	4.8	3.6	7.3	2.5	4.9	3.6
Profit of associates	NA	NA	244.1	153.0	786.3	360.3	282.2	215.3
less Minority interest	NA	NA	-485.0	-124.4	-30.6	-8.0	-253.7	-221.3
PAT (concern share)	398.3	594.3	1,288.8	961.1	759.4	280.8	1,561.9	854.8
PAT margin (%)	9.1	14.8	2.1	1.6	54.6	21.8	2.5	1.4
Gross debt (excl. lease liability)	1,129.4	1,386.1	11,527.9	11,736.8	1,928.2	2,238.1	12,885.8	13,753.3
Cash	113.6	198.8	3,522.3	4,841.1	640.4	1,123.4	3,592.4	5,752.0
Net debt	1,015.8	1,187.3	8,005.6	6,895.7	1,287.8	1,114.7	9,293.4	8,001.3
Lease liability (under Ind AS 116)	78.1	78.0	1,350.0	1,351.5	72.1	88.7	1,422.1	1,440.2
Net leverage (with Ind AS 116)								1.7x
Net leverage (ex Ind AS 116)								1.9x

Source: Company, ICICI Direct Research

Exhibit 5: SMRPBV financials (€ million)

Particulars	FY16	FY17	FY18	FY19	FY20
EBITDA	292.0	362.0	378.0	347.0	336.0
EBIT	170.0	244.0	255.0	179.0	99.0
PBT	143.0	213.0	209.0	148.0	37.0
less Tax	-29.0	-66.0	-71.0	-45.0	-41.0
PAT	114.0	147.0	138.0	103.0	-4.0
Less minority shareholders at SMRPBV	-17.0	-20.0	-30.0	-24.0	-23.0
PAT attributable to SMRPBV shareholders	97.0	127.0	109.0	78.0	-27.0
Attributable to MSSL	50.0	65.0	55.0	40.0	-14.0
Attributable to SAMIL	48.0	62.0	53.0	38.0	-13.0
PAT attributable to SMRPBV shareholders (excluding greenfield impact)				217.0	164.0
Attributable to MSSL				111.0	84.0
Attributable to SAMIL				106.0	80.0

Source: Company, ICICI Direct Research

Exhibit 6: DWH proforma financials

₹ crore	FY19	FY20
Sales	4483.8	3943.9
EBITDA	739.9	529.4
EBITDA margins	16.5%	13.4%
EBIT	642.6	429.4
EBIT Margins	14.3%	10.9%
PAT	392.3	286
PAT Margins	8.7%	7.3%
Gross Debt	6.3	33.3
Net Debt	-14	1.6
Lease Liability (under Ind AS116)	334.6	334.2
RoCE	64%	55%

Source: Company, ICICI Direct Research

Exhibit 7: Post scheme share capital structure – Demerger of domestic wiring business from MSSL into DWH

As of date hereof	no. of shares (crore)
Outstanding equity shares of DWH of face value ₹ 1 each (A)	0.05
Outstanding equity shares of MSSL of face value ₹ 1 each (B)	315.79
New equity shares to be issued by DWH to shareholders of MSSL as per share entitlement ratio (C =B*1)	315.79
Less : Existing equity shares of DWH to be cancelled (D)	0.05
Resultant equity shares of DWH (E =A +C - D)	315.79

Source: Company, ICICI Direct Research

Exhibit 8: Post scheme share capital structure – Merger of SAMIL into MSSL

As of date hereof	no. of shares (crore)
Outstanding equity shares of MSSL of face value ₹ 1 each (A)	315.79
Outstanding equity shares of SAMIL of face value ₹ 10 each (B)	47.36
New equity shares to be issued by MSSL to shareholders of SAMIL (C =B*1)	241.54
Less : Cancellation of equity shares in MSSL held by SAMIL (D)	105.58
Resultant equity shares of MSSL (E =A +C - D)	451.76

Source: Company, ICICI Direct Research

Exhibit 9: Valuation range arrived at by independent valuers

Entity	MSSL (ex DWH)	SAMIL
Value per share (₹)	100.51-101.81	512.81-519.27

Source: Company, ICICI Direct Research

Financial Summary

Exhibit 10: Profit and loss statement				
	₹ crore			
(Year-end March)	FY19	FY20P	FY21E	FY22E
Total operating income	63522.9	63536.9	58164.5	65855.0
Growth (%)	12.8	0.0	-8.5	13.2
Raw Material Expenses	36,738.3	36,271.4	32,502.7	36,941.8
Employee Expenses	14,169.4	15,076.9	14,955.7	15,565.5
Other expenses	7,266.8	6,987.1	6,428.6	6,983.9
Total Operating Expenditure	58,174.5	58,335.4	53,887.0	59,491.3
EBITDA	5348.4	5201.4	4277.4	6363.7
Growth (%)	4.4	-2.7	-17.8	48.8
Depreciation	2,058.2	2,778.0	2,821.0	2,897.6
Interest	423.2	598.6	578.5	473.5
Other Income	220.2	230.7	252.9	228.2
PBT	3087.2	2055.4	1130.9	3220.8
Total Tax	1,102.2	818.4	339.3	966.2
Minority Interest	485.0	124.4	88.1	617.8
Profit from Associates	113.1	57.5	28.7	77.9
Reported PAT	1613.2	1170.1	732.2	1714.7
Growth (%)	1.0	-27.5	-37.4	134.2
EPS (₹)	5.1	3.7	2.3	5.4

Source: Company, ICICI Direct Research

Exhibit 11: Cash flow statement				
	₹ crore			
(Year-end March)	FY19	FY20P	FY21E	FY22E
Profit after Tax	1613.2	1170.1	732.2	1714.7
Add: Depreciation	2,058.2	2,778.0	2,821.0	2,897.6
(Inc)/dec in Current Assets	-2,300.4	1,579.3	939.5	-1,989.5
Inc/(dec) in CL and Provisions	2,913.9	695.6	-1,565.4	1,930.1
CF from operating activities	4284.9	6223.0	2927.2	4552.9
(Inc)/dec in Investments	0.0	0.0	0.0	0.0
(Inc)/dec in Fixed Assets	-4,457.5	-4,782.5	-2,000.0	-2,200.0
Others	300.4	617.0	-74.9	607.9
CF from investing activities	-4157.1	-4165.5	-2074.9	-1592.1
Issue/(Buy back) of Equity	105.3	0.0	0.0	0.0
Inc/(dec) in loan funds	1,171.8	146.2	-200.0	-2,000.0
Dividend paid & dividend tax	-568.4	-1,136.9	-473.7	-947.4
Inc/(dec) in Sec. premium	34.3	265.0	0.0	0.0
Others	-105.3	0.0	0.0	0.0
CF from financing activities	637.7	-725.7	-673.7	-2947.4
Net Cash flow	765.4	1,331.9	178.6	13.4
Opening Cash	2,781.6	3,547.0	4,878.9	5,057.5
Closing Cash	3546.9	4878.9	5057.5	5070.9

Source: Company, ICICI Direct Research

Exhibit 12: Balance Sheet				
	₹ crore			
(Year-end March)	FY19	FY20P	FY21E	FY22E
Liabilities				
Equity Capital	315.8	315.8	315.8	315.8
Reserve and Surplus	10,647.0	10,945.1	11,203.6	11,970.9
Total Shareholders funds	10,962.7	11,260.9	11,519.4	12,286.7
Total Debt	11,522.8	11,669.1	11,469.1	9,469.1
Deferred Tax Liability	576.2	462.8	423.6	479.6
Minority Interest / Others	3,479.7	3,565.0	3,653.1	4,270.9
Total Liabilities	27863.0	29332.9	29239.5	28968.1
Assets				
Gross Block	19,878.9	24,876.4	26,728.2	29,128.2
Less: Acc Depreciation	5,825.0	8,603.0	11,424.0	14,321.6
Net Block	14053.9	16273.4	15304.2	14806.6
Capital WIP	1,066.8	851.8	1,000.0	800.0
Total Fixed Assets	15,120.7	17,125.2	16,304.2	15,606.6
Investments	3,085.2	3,006.7	3,106.7	3,206.7
Goodwill	2211.8	2406.0	2406.0	2406.0
Inventory	4,663.5	5,156.6	4,780.6	5,412.7
Debtors	7,329.2	6,578.2	6,374.2	7,217.0
Loans and Advances	22.6	31.9	29.2	33.0
Other Current Assets	5,550.3	4,219.6	3,862.8	4,373.6
Cash	3546.9	4878.9	5057.5	5070.9
Total Current Assets	21,112.5	20,865.2	20,104.3	22,107.3
Creditors	10,661.3	10,309.1	9,242.6	10,464.6
Provisions	157.9	205.2	184.0	208.3
Other current liabilities	464.8	564.9	517.1	585.5
Total Current Liabilities	15,467.3	16,162.9	14,597.5	16,527.6
Net Current Assets	5645.3	4702.3	5506.8	5579.7
Other non-current Asset	1187.7	1589.8	1455.4	1647.8
Deferred Tax Asset	612.3	503.0	460.4	521.3
Application of Funds	27863.0	29332.9	29239.5	28968.1

Source: Company, ICICI Direct Research

Exhibit 13: Key ratios				
(Year-end March)	FY19	FY20P	FY21E	FY22E
Per share data (₹)				
EPS	5.1	3.7	2.3	5.4
Cash EPS	11.6	12.5	11.3	14.6
BV	34.7	35.7	36.5	38.9
DPS	1.5	3.0	1.5	3.0
Cash Per Share	11.2	15.4	16.0	16.1
Operating Ratios				
EBITDA Margin (%)	8.4	8.2	7.4	9.7
PBIT / Net sales (%)	5.2	3.8	2.5	5.3
PAT Margin (%)	2.5	1.8	1.3	2.6
Inventory days	26.8	29.6	30.0	30.0
Debtor days	42.1	37.8	40.0	40.0
Creditor days	61.3	59.2	58.0	58.0
Return Ratios (%)				
RoE	14.7	10.4	6.4	14.0
RoCE	13.2	9.8	6.3	13.9
RoIC	19.3	14.2	8.7	21.2
Valuation Ratios (x)				
P/E	19.6	27.0	43.1	18.4
EV / EBITDA	7.4	7.4	8.9	5.7
EV / Net Sales	0.6	0.6	0.7	0.5
Market Cap / Sales	0.5	0.5	0.5	0.5
Price to Book Value	2.9	2.8	2.7	2.6
Solvency Ratios				
Debt/EBITDA	2.2	2.2	2.7	1.5
Debt / Equity	1.1	1.0	1.0	0.8
Current Ratio	1.1	1.0	1.0	1.0
Quick Ratio	0.8	0.7	0.7	0.7

Source: Company, ICICI Direct Research

(Note - We have retained our financial statement estimates and not incorporated the restructuring fine prints as on date)

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Pankaj Pandey

Head – Research

pankaj.pandey@icicisecurities.com

ICICI Direct Research Desk,
ICICI Securities Limited,
1st Floor, Akruiti Trade Centre,
Road No 7, MIDC,
Andheri (East)
Mumbai – 400 093
research@icicidirect.com

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