Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Triveni Engineering & Industries

Eyeing the right blend for profitability

Miscleneous	Sharekhan code: TRIVENI	Company Update

3R MATRIX	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)	✓		

\+ Positive = Neutral - Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↔	

Reco/View	Change
Reco: **Buy**	↔
CMP: **Rs. 94**	
Price Target: **Rs. 125**	↑

↑ Upgrade ↔ Maintain ↓ Downgrade

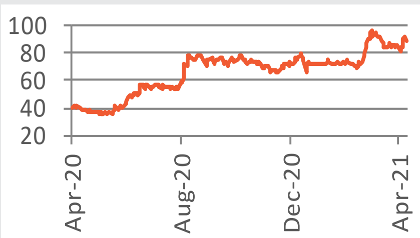
Company details

Market cap:	Rs. 2,272 cr
52-week high/low:	Rs. 88/29
NSE volume: (No of shares)	6.8 lakh
BSE code:	532356
NSE code:	TRIVENI
Free float: (No of shares)	7.6 cr

Shareholding (%)

Promoters	68.4
FII	2.7
DII	3.9
Others	25.0

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	5.8	28.8	27.3	141.0
Relative to Sensex	14.9	30.6	7.8	82.2

Sharekhan Research, Bloomberg

Summary

- We maintain a Buy on Triveni Engineering & Industries (TEIL) with revised target price of Rs. 125. Attractive valuation of 4.7x versus historical average of 6.3x and changing industry dynamics make it better play in the sugar segment.
- With the government focusing on achieving ethanol blending of 20% by CY2025; India's ethanol requirement will increase significantly (4-5 billion litres required for 10% blending). TEIL is adding 160 KLPD B-Heavy/Cane juice and a 40 KLPD grain-based distillery (to be operational by Q3FY22).
- With augmentation of distillery capacity, distillery revenues will clock a 21% CAGR with realisation inching up to Rs. 52 per litre; margins to also improve in the coming years.
- With improvement in profitability and stable working capital; free cash flow (FCF) is expected to improve (cumulative FCF of ~Rs. 2,060 crore likely over FY20-23) and aid better dividend payouts/ prudent buyback policy.

India has been clocking a surplus sugar output since sugar season (SS) 2010-11 (except the drought in SS 2016-17). Last year, India ended with an excess supply of 10.6 million tonnes and there is likely to be a surplus production in the coming years as well because of the improved variety of sugarcane. To support sugar mills and to keep a check on sugar inventory, the government has undertaken various measures such as effectively managing oversupply through adequate export policy (six million tonnes of exports allowed in sugar year 2020-21), monthly quota mechanism and divert excess sugar for ethanol blending. All these measures and a higher sugar MSP aided sugar mills' realisations remain intact despite excess production (currently at Rs. 32 per kg and likely to be at Rs. 33 per kg in FY2022). In a one-of-its-kind move, the government has preponed the target of achieving 20% ethanol blending to 2025 from 2030 earlier (last sugar year blending ratio has reached to 8.0%). Nearly 4-5 billion litres of ethanol will be needed for achieving 10% blending ratio. This will create a strong revenue stream for sugar mills to clear off their dues to farmers . Triveni Engineering & industries (TEIL) is one of top five sugar companies in UP with sugar crushing capacity of 60,500 tonnes per day and distillery capacity of 320 kilolitres per day (KLPD). The company has recently decided to expand distillery capacity by 160KLPD of B-heavy molasses & sugar juice capacity and 40-KLPD of grain-based facilities. A 200 KLPD extended facility is expected to be operational by H2FY2022 and will augment TEIL's distillery capacity to 520 KLPD by FY2022-end. With the augmentation of distillery capacity, the segment's revenues will grow at CAGR of 21% over FY2020-23 to Rs. 700 crore with a realisation of inching up to Rs52 per litre in FY2023 from Rs46 per litre in FY2020 (B-heavy ethanol current realisation is ~Rs58 per litre). The increase in distillery realisation and stable sugar realisations would help OPM to gradually improve in the coming years. Further, with revival in the industrial cycle, we expect the revenues of engineering and water business to gradually increase in the coming years. Thus overall we expect the OPM to reach 12.7% in FY2023 from the expected 11.9% in FY2021. The improvement in operating margins and stable working capital management would help the cash flows to improve further (expect cumulative FCF of Rs. 2,060 crore over FY2020-23). Return ratios are also expected to be strong and stay above 20% in the coming years.

Our Call

View: Retain Buy with revised target price of Rs. 125 - TEIL will be one of the key beneficiaries of the government's revised ethanol blending policy. This will significantly enhance revenues from the distillery segment, which will also get add-on to the profitability in the coming years. Further, a change in the industrial cycle will bode well for its engineering and water business to get better order book and higher revenues in the coming years. Overall, we expect TEIL's PAT to grow at a CAGR of 15% over FY2020-23. The stock is currently trading at 4.7x its FY2023E earnings and EV/EBIDTA of 4.0x. Current valuations are at discount to its historical one-year forward average multiple of 6.3x. Thus, in view of near-term growth prospects and attractive valuations, we maintain our Buy recommendation on TEIL with revised price target of Rs. 125 (valuing stock at 7x its FY2023E EPS).

Key Risks

Any adverse change in the ethanol policy or significant increase in the domestic/international sugar production would act as a key risk to our earnings estimates.

Valuations (Consolidated) Rs cr

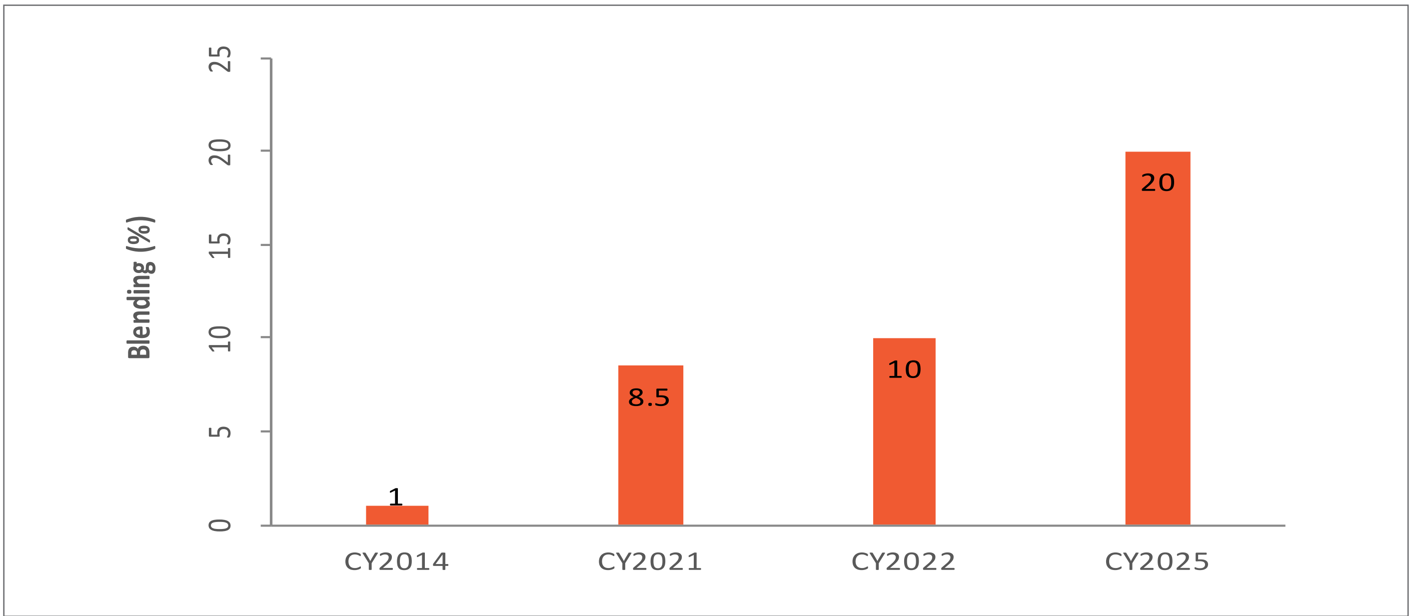
Particulars	FY19	FY20	FY21E	FY22E	FY23E
Revenue	3,152	4,437	5,150	5,174	5,574
OPM (%)	9.8	12.2	11.9	12.4	12.7
Adjusted PAT	196	315	501	536	610
Adjusted EPS (Rs.)	8.72	13.51	16.7	17.9	20.2
P/E (x)	10.8	7.0	5.6	5.2	4.7
P/B (x)	2.1	1.7	1.4	1.2	1.0
EV/EBIDTA (x)	13.5	7.2	5.4	4.8	4.0
RoNW (%)	20.7	27.0	26.8	23.9	23.4
RoCE (%)	12.6	17.0	19.1	19.9	21.9

Source: Company; Sharekhan estimates

India prepones 20% ethanol blending by CY2025

Indian government has preponed the target of achieving 20% ethanol-blending with petrol by five years to CY2025 from CY2030 earlier. The focus is on cutting dependence on costly oil imports. India has seen a surplus production of sugar since SS 2010-11 (other than the drought in SS 2016-17) and there is likely to be surplus output in the coming years as well because of the introduction of improved varieties of sugarcane. The government is targeting to achieve 20% blending of ethanol by 2025 which would largely take care of excess sugar inventory in the system and will also provide additional stream of sustainable revenues in the coming years. In 2014, close to 1% of ethanol was being blended with petrol, which improved to 8.5% in sugar year 2020-21. The industry is targeting a 10% blending by 2021-22 that would require 4-5 billion litres ethanol. The central government has recently come out with a modified scheme for extending financial assistance by way of interest subvention for five years (on the loan availed from banks @ 6% per annum or 50% of the rate of interest charged by banks whichever is lower) for enhancement of ethanol distillation capacity or to set up distilleries for producing first-generation (1G) ethanol 9 from feed stocks or converting molasses-based distilleries to dual feedstock.

Ethanol blending to reach 20% by CY2025

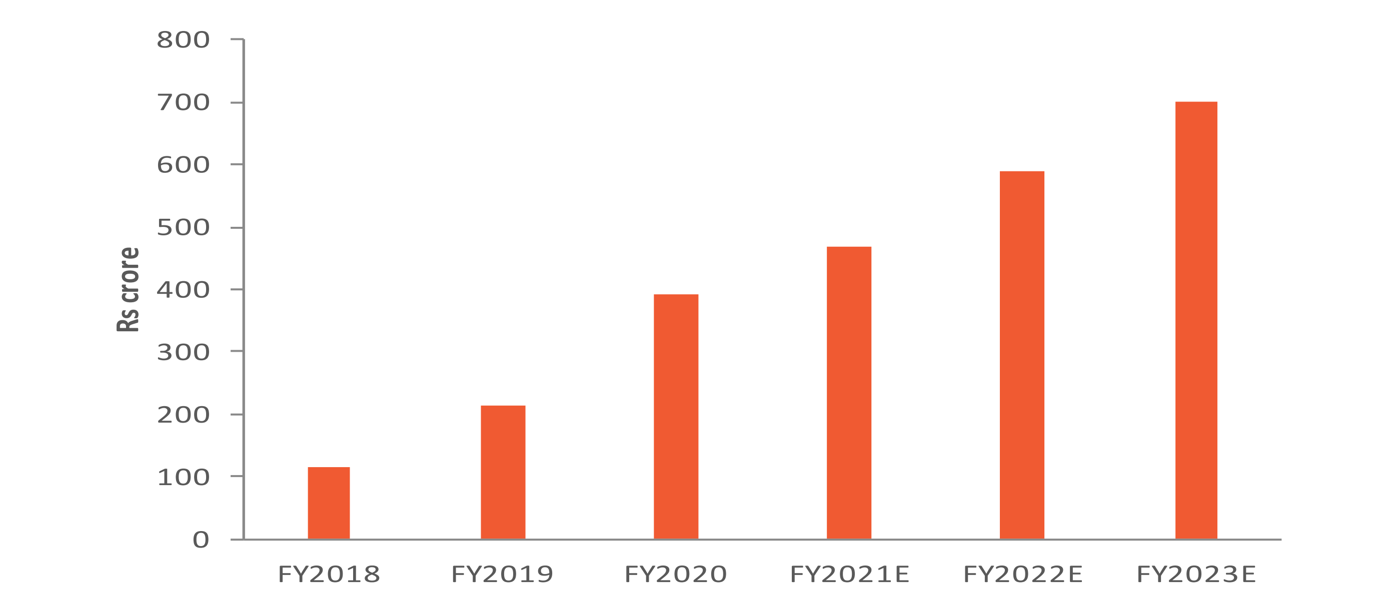


Source: Industry reports; Sharekhan Research

TEIL is augmenting distillery capacity by 200 KLPD

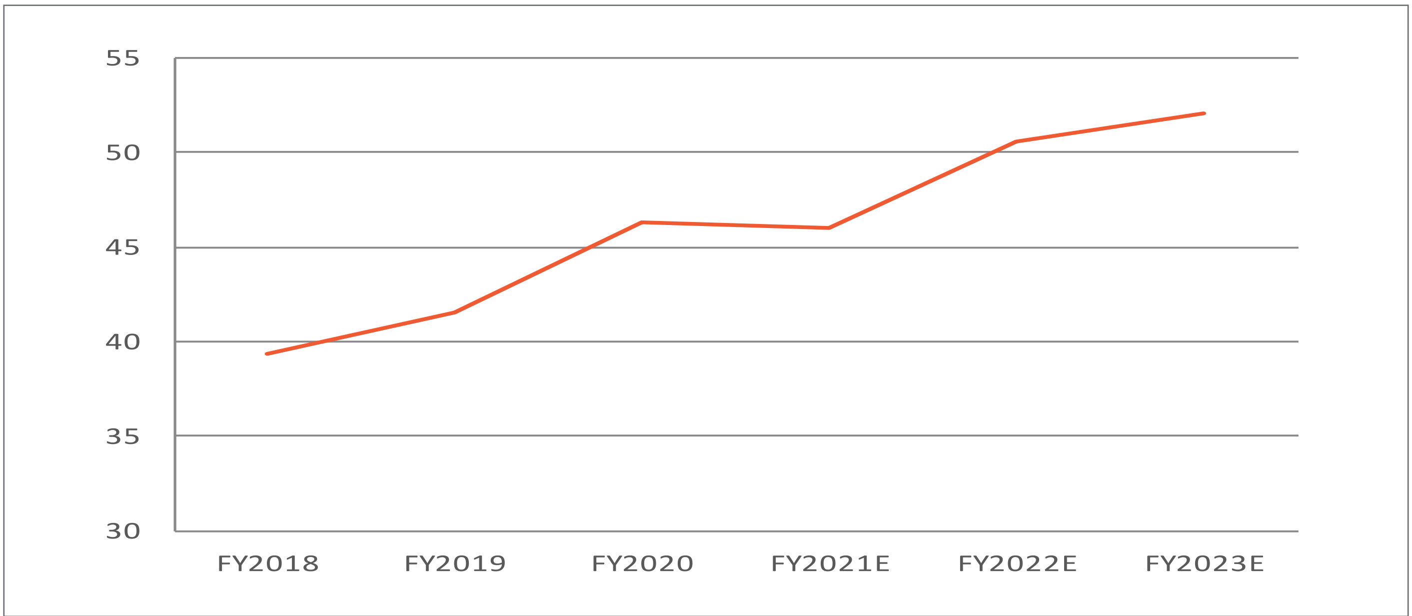
TEIL is planning to come up with two new distilleries of 40 KLPD which is a grain-based plant at Muzaffarnagar and a 160 KLPD molasses, juice, syrup, and grain-based plant at its sugar factory at Milak Narayanpur, district Rampur, Uttar Pradesh. This will raise its total distillation capacity to 520 KLPD by end of FY2022. The cost of this two combined expansion will be Rs. 250 crore, which will be largely done through mix of internal accruals and low cost debt. After this expansion, TEIL's ethanol production capacity would consist of 62% of B-heavy ethanol, 30% of C-heavy ethanol and 10% grain-based ethanol. B-heavy ethanol has better realisation of Rs57.6 per litre as compared to Rs. 45.7 per litre of C-heavy ethanol. Thus increase in the capacity of B-heavy ethanol would help realisation of improve in the coming years. We expect the revenues of distillery division to grow at a CAGR of 21% over FY2020-23 and reach revenues close to Rs. 700 crore by FY2023 from Rs. 391crore in FY2020. Also, sales realisations are expected to go up to Rs. 52.1 per litre in FY2023 from around Rs. 46 per litre in FY2020. The improvement in realisation would also help the overall profitability to improve in the coming years.

Distillery revenues to reach Rs. 700 crore by FY2023



Source: Company; Sharekhan estimates

Distillery realisation to stand at Rs52 per litre by FY2023



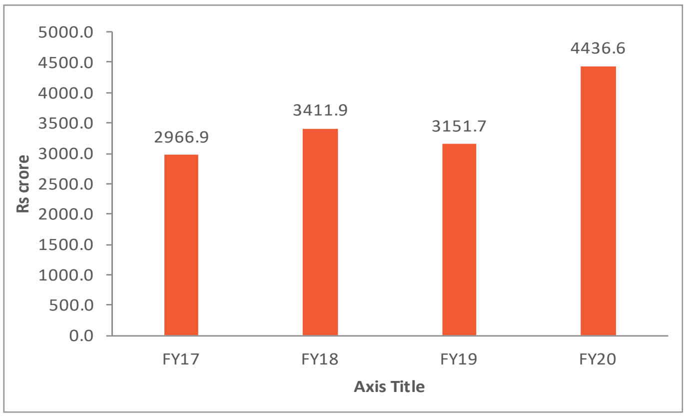
Source: Company; Sharekhan Research

Higher profitability; better working capital management to improve cash flows

The increase distillery realisation and stable sugar realisation would help OPM to gradually improve in the coming years. Further, with a revival in industrial cycle, we expect revenues of engineering and water business to gradually increase in the coming years. Thus, overall, we expect OPM to reach 12.7% in FY2023 from the expected 11.9% in FY2021. The improvement in operating margins and stable working capital management would help cash flows improve further (expect a cumulative FCF of Rs. 2060 crore over FY2020-23). With better cash flows, the company managed to reduce its debt to Rs. 550 crore as on December 31, 2020 as against Rs. 1,544 crore as on December 31, 2019, comprising terms loans of Rs. 412.5 crore (most of the term loan is with interest subvention or at subsidized interest rate). Return ratios are also expected to be strong, at above 20% in the coming years.

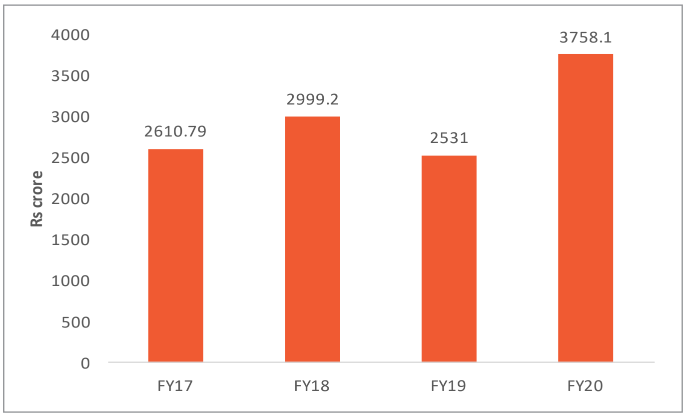
Financials in charts

Trend in consolidated revenues



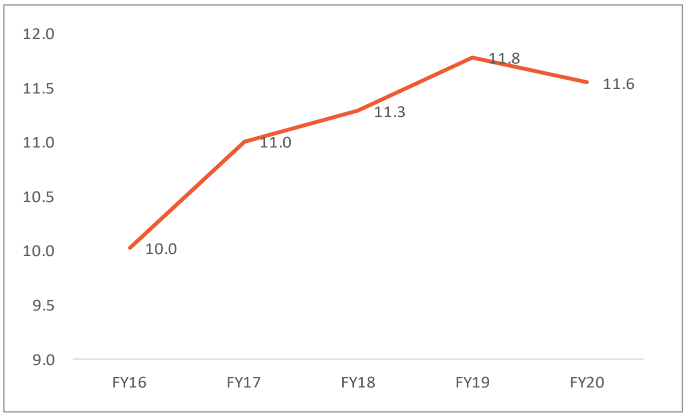
Source: Company, Sharekhan Research

Trend in sugar revenues



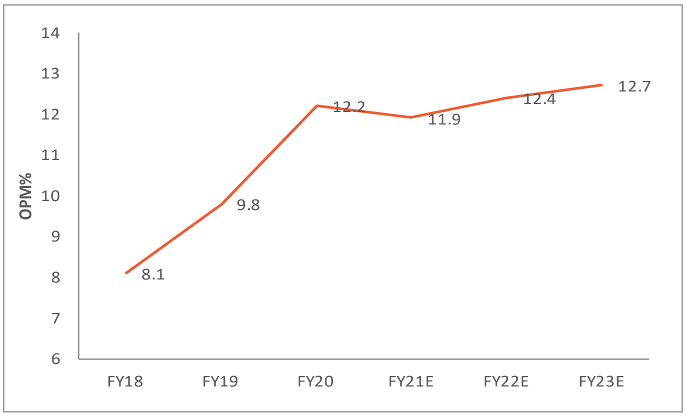
Source: Company, Sharekhan Research

Sugar recovery rate



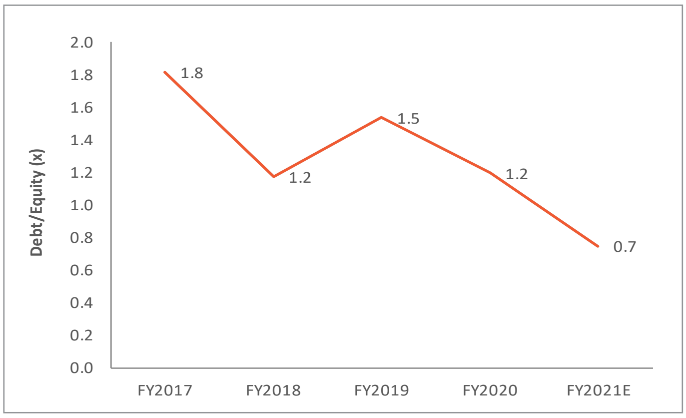
Source: Company, Sharekhan Research

OPM to gradually improve on y-o-y basis



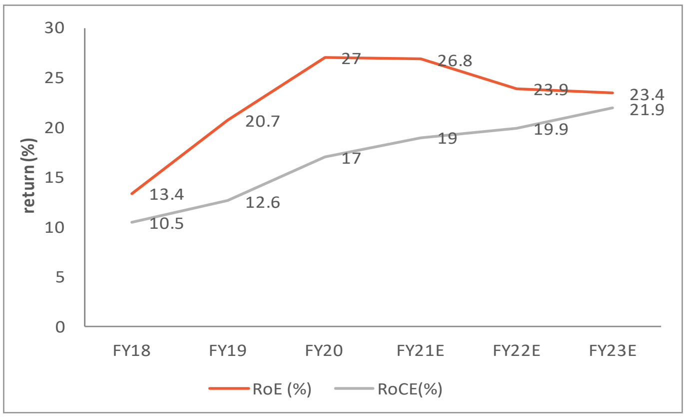
Source: Company, Sharekhan Research

Debt: equity reduced consistently



Source: Company, Sharekhan Research

Return ratios are expected to stay ahead of 20% by FY2023E



Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector view - Rise in supply for ethanol manufacturing and exports will mitigate impact of higher output

As per the ISMA's latest estimates for total sugar production for SY2020-21 based on sugarcane production is estimated at 32.2 million. It is further estimated that due to diversion of sugarcane juice and B-heavy molasses, actual sugar production will drop by 2 million tonnes. Therefore, estimated sugar production (net of diversion) is estimated at 30.2 million tonnes, which is a growth of 10% over the previous sugar season. A revised ethanol policy, recommended increase in MSP by Rs. 2 per kg, quota base sugar distribution and export quota of 6 million tonnes will benefit sugar companies in FY2022 with stable sugar realisation. Increase in the international sugar prices would help the Indian companies to get better export realisation for their produce. The government is targeting to achieve 20% blending of ethanol by 2025 which would largely solve the problem of excess sugar over the medium term.

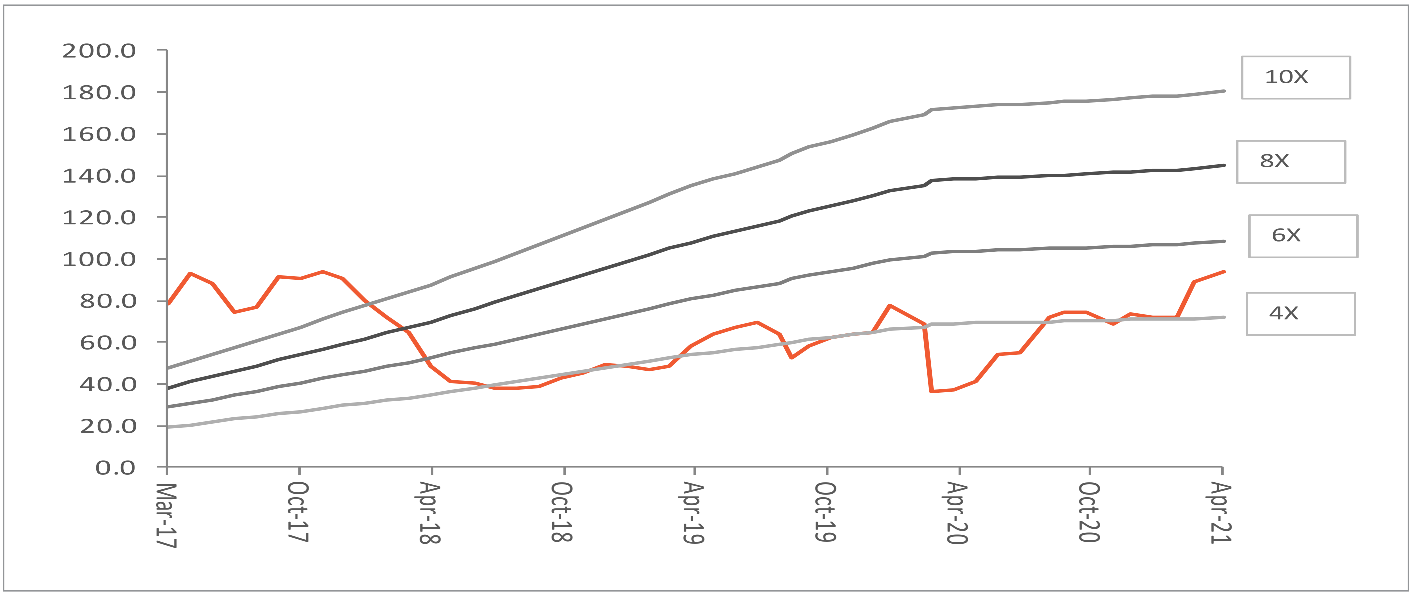
■ Company outlook - Distillery and engineering business to drive performance in FY2022

TEIL expects a recovery of 30 bps less in the sugar business as compared to the previous sugar season (production to be lower by 5%). The company will export 1.82 lakh tonnes in 2020-21 under the MAEQ programme (0.5 lakh tonnes contracted till January 2021). Though exports subsidy is expected at Rs. 6 per kg, higher international sugar prices would keep export realisations comfortable. Sugar inventory stood at 28.2 lakh quintals as December, valued at Rs. 30.9/kg. The distillery division has received a contract of 9.86 crore litres of ethanol supply for year 2020-21 (90% of the contract is for B-heavy molasses which can be realised at Rs. 57.6/litre). The engineering business' order book currently stands slightly lower than Rs. 1,000 crore.

■ Valuation - Retain Buy with revised target price of Rs125

TEIL will be one of the key beneficiaries of the government's revised ethanol blending policy. This will significantly enhance revenues from the distillery segment, which will also get add-on to the profitability in the coming years. Further, a change in the industrial cycle will bode well for its engineering and water business to get better order book and higher revenues in the coming years. Overall, we expect TEIL's PAT to grow at a CAGR of 15% over FY2020-23. The stock is currently trading at 4.7x its FY2023E earnings and EV/EBIDTA of 4.0x. Current valuations are at discount to its historical one-year forward average multiple of 6.3x. Thus, in view of near-term growth prospects and attractive valuations, we maintain our Buy recommendation on TEIL with revised price target of Rs. 125 (valuing stock at 7x its FY2023E EPS).

One-year forward P/E (x) band



Source: Sharekhan Research

Peer Comparison

Particulars	P/E (x)			EV/EBIDTA (x)			RoCE (%)		
	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E
Balrampur Chini Mills	10.0	8.0	7.3	9.4	7.5	6.8	17.3	20.6	22.6
Triveni Engineering	5.6	5.2	4.7	5.4	4.8	4.0	19.1	19.9	21.9

Source: Company, Sharekhan estimates

About company

Triveni Engineering & Industries is the largest integrated sugar manufacturer in India and the market leader in its engineering businesses comprising - high-speed gears, gearboxes, and water & wastewater treatment solutions. Triveni currently has seven sugar mills at Khatauli, Deoband, Sabitgarh, (in western Uttar Pradesh), Chandanpur, Rani Nangal and Milak Narayanpur (in central Uttar Pradesh) and Ramkola (eastern Uttar Pradesh). While the company's gears manufacturing facility is located at Mysuru, the water & wastewater treatment business is located at Noida. The Company currently operates three grid connected cogeneration plants and three incidental co-generation plants located across five sugar units and two molasses-based distilleries in UP, located at Muzaffarnagar and Sabitgarh.

Investment theme

TEIL will be one of the key beneficiaries of improving fundamentals of sugar industry in India with government focusing on reducing the cyclicality in the industry to achieve stable realisation and better profitability in the coming years. The company is focusing on expanding its distillery facility to improve its revenue stream in the coming years. Further, higher MSPs and higher international sugar prices will keep sugar realisations stable despite higher sugar products. This will help OPM to improve from ~12% in FY2020 to 12.7% in FY2023. Higher profitability along with stable working capital management will help cash flows to improve in the coming years. Thus, the company's balance sheet is expected to strengthen further in the coming years. Return ratios are expected to consistently improve and stand ahead of 20% in FY2023.

Key Risks

- Any sharp decline in sugar prices due to significant improvement in global/domestic sugar production would affect earnings of the sugar companies.
- Any change in the sugar export or ethanol blending policies would affect the sugar companies' business fundamentals.

Additional Data

Key management personnel

Dhruv Sawhney	Executive Director-Chairperson-MD
Sureja Taneja	Group CFO
Tarun Sawhney	Eexcutive Director - MD
Geeta Bhalla	Company Secretary & Compliance Officer

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Anil Kumar Goel	2.83
2	DSP Blackrock Mutual Fund	2.74
3	Norges Bank	2.21
4	Government Pension Fund Global	1.98
5	IndiaNivesh Capitals Ltd	1.34
6	Dimensional Fund Advisors LPP	0.94
7	Van Eck Associates Corp	0.11
8	ICICI Prudential Asset Management Co Ltd	0.1
9	Investor Education & Protection Fund	0.03
10	Sundaram Asset Management Co Ltd	0.02

Source: Bloomberg (Old data)

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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