Sharekhan by BNP PARIBAS

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Stock Update

Suprajit Engineering Limited

Robust Q4; riding on new growth paths

Automobiles	Sharekhan code: SUPRAJIT	Result Update

Summary

- We reiterate our Buy rating on Suprajit Engineering Limited with a revised PT of Rs. 329, factoring its robust value proposition to its domestic and global clients, aided by its leadership position in the domestic cables business and locational advantage vis-à-vis global peers.
- Q4FY21 numbers were strong, with revenue, EBIDTA and PAT improving 31.9%, 48.8% and 89.1%, respectively
- We expect Suprajit's earnings to report a 26.3% CAGR during FY2021E-FY2023E, driven by a 19.2% revenue CAGR and 130 bps improvement in EBITDA margin, with its ROCE improving back to ~20% in FY23E.
- The stock trades at a 25-30% discount to its average historical P/E multiple of 16.2x and EV/EBITDA multiple of 10.4x its FY2023E estimates.

Suprajit Engineering Limited reported strong numbers in Q4FY21, with revenue, EBIDTA and PAT improving 31.9%, 48.8% and 89.1%, respectively. EBITDA slightly lagged estimates owing to a rise in input costs and higher freight rates. Net revenue grew by 32% y-o-y at Rs 513 crore in Q4FY21, as compared to Rs 389 crore in Q4FY20, led by a recovery in automotive and non-automotive businesses. Sequentially, revenues rose by 1.1%. OPM stood at 15.9%, rising by 180 bps y-o-y driven by product mix, cost reduction initiatives and operating leverage benefits. The subsidiary business' performance also helped in improving consolidated margins. As a result, EBITDA improved by 48.8% y-o-y. On q-o-q basis, EBITDA margin declined by 110 bps in Q4FY21, showing EBITDA decline of 5.4% q-o-q to Rs. 82 crore. PAT grew by 89.1% y-o-y and 11.4% q-o-q to Rs 58 crore. The Phoenix Lamps division (Including Trifa and Luxlite) saw revenue grow by 39% y-o-y, while the SENA (Suprajit non-automotive) and cable division saw a revenue growth of 20.4% y-o-y and 33.9% y-o-y respectively. While the divisional EBITDA margin for Phoenix lamp and SENA divisions improved by 230 bps q-o-q and 890 bps q-o-q to 13.8% and 20.8% respectively in Q4. The EBITDA margin for cable division declined by 530 bps q-o-q to 15% in Q4FY21, impacted by higher freight costs. Suprajit continues to strengthen its value proposition to its domestic and global clients, aided by a leadership position in the domestic cable business and locational advantage to its global peers. Key drivers for Suprajit's success are its ability to produce low-cost cables among domestic players, aided by its operational efficiency and dedicated plants for respective clients. Among global peers, the company benefits from its locational cost advantage. The company has a strong foothold in the cable business in the automotive segment, where it holds a 30-35% market share. The company has a dominant 60-65% market share in the two-wheelers (2W) cable business. We expect Suprajit to benefit from strong demand witnessed in the domestic as well as export markets. The company will also benefit from its capex plans, which will help it to capitalise further in the next peak season. We remain positive on Suprajit's growth prospects and thus, retain a Buy rating on the stock.

Key positives

- Strong revenue growth across divisions with cable, phoenix lamps and SENA divisions showing revenue growth of 33.9% y-o-y, 39% y-o-y and 20.4% y-o-y respectively in Q4FY21.
- The management continues to witness business traction in India as well as around the globe, aided by introduction of new products to existing clients and selling old products to new clients.

Key negatives

- Consolidated EBITDA margin saw a decline of 110 bps q-o-q to 15.9% in Q4FY21, impacted by to rise in input costs and higher freight rates.
- Chips supply shortage remains a key concern for the management, as the production of its clients get impacted.

Our Call

Valuation - Maintain Buy with an unchanged PT of Rs. 329: Suprajit would continue to gain wallet share from customers in the cable segment (domestic PV segment and higher sourcing by global OEM) and Phoenix Lamps (increased sourcing by Osram). Further, the company would continue to enter new segments in the non-automotive cable division. We expect FY2022 to be a strong year, driven by normalisation of economic activity and improving demand. Operating leverage coupled with cost-control measures would help in margin improvement. We have maintained our earnings estimates, driven by the company's leadership position in cable business. Propelled by robust business outlook and prudent capital allocation, we expect Suprajit's consolidated earnings to report a 26.3% CAGR during FY2021E-FY2023E, driven by an 19.2% revenue CAGR and 130 bps improvement in EBITDA margin, with its ROCE improving back to ~20% in FY23E. The stock is trading at 25-30% discount to its average historical P/E multiple of 16.2x and EV/EBITDA multiple of 10.4x its FY2023E estimates. We retain our Buy rating on the stock with an unchanged PT of Rs. 329.

Key Risks

Chips supply shortage, rising commodity prices and prolonged lockdowns due to COVID wave-2 remains a key concerns. Moreover, delayed approval from OEMs for incremental business may impact performance.

Valuation (Consolidated) Rs cr

Particulars	FY19	FY20	FY21	FY22E	FY23E
Revenues	1,590	1,563	1,641	2,028	2,330
Growth (%)	11.1	(1.7)	5.0	23.6	14.9
EBIDTA	233	219	237	306	366
OPM (%)	14.6	14.0	14.4	15.1	15.7
Net Profit	134	104	143	185	228
Growth (%)	(3.4)	(22.3)	37.3	29.5	23.2
EPS	9.6	7.4	10.3	13.4	16.5
P/E	27.9	35.9	25.9	20.0	16.2
P/BV	4.8	4.4	3.8	3.4	2.9
EV/EBIDTA	17.1	18.2	16.7	12.8	10.4
ROE (%)	17.3	12.2	14.9	16.8	17.9
ROCE (%)	20.0	14.7	16.0	18.4	19.9

Source: Company; Sharekhan estimates

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. 267**	
Price Target: **Rs. 329**	↔

↑ Upgrade ↔ Maintain ↓ Downgrade

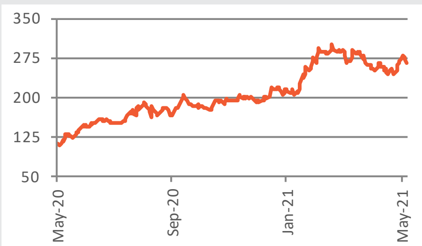
Company details

Market cap:	Rs. 3,725 cr
52-week high/low:	Rs. 310 / 109
NSE volume: (No of shares)	2.0 lakh
BSE code:	532509
NSE code:	SUPRAJIT
Free float: (No of shares)	7.8 cr

Shareholding (%)

Promoters	44.6
FII	3.5
DII	12.8
Others	39.2

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	2.1	-4.3	36.8	135.9
Relative to Sensex	-3.0	-5.3	18.9	73.2

Sharekhan Research, Bloomberg

Key Highlights of Q4FY21 results and conference call

- **Strong performance in Q4FY21, with EBITDA margin falls below expectations marginally:** Net revenue grew by 32% y-o-y at Rs 513 crore in Q4FY21, as compared to Rs. 389 crore in Q4FY20, on the back of recovery in automotive and non-automotive business. On q-o-q basis, the revenues were up 1.1%. OPM for the Q4FY21 stood at 15.9% showing an improvement of 180 bps y-o-y driven by product mix, cost-reduction initiatives and operating leverage benefits. The subsidiary business performance also helped in improving consolidated margins. As a result, EBITDA improved by 48.8% y-o-y. On q-o-q basis, the EBITDA margin declined 110 bps in Q4FY21, showing EBITDA decline of 5.4% q-o-q to Rs. 82 crore. PAT grew by 89.1% y-o-y and 11.4% q-o-q to Rs 58 crore. The company also benefitted from the increase in components per unit and improvement in wallet share with key customers.
- **Strong operational improvement in Phoenix and SENA divisions:** The Phoenix Lamps division (Including Trifa and Luxlite) saw a revenue of Rs101.8 crore in Q4FY21, showing a growth of 39% y-o-y and 1.2% q-o-q. The EBITDA margin of the Phoenix lamp division shown an improvement of 950 bps y-o-y and 230 bps q-o-q to 13.8% in Q4FY21. The SENA (Suprajit non-automotive) division witnessed a revenue growth of 20.4% y-o-y and 14.5% q-o-q to Rs 104.4 crore in Q4FY21, with EBIDTA improving 106% y-o-y and 100% q-o-q at Rs. 20.8 crore. The cables division also seen a strong revenue growth of 33.9% y-o-y to Rs. 306.8 crore, but EBITDA margin declined 300 bps y-o-y and 530 bps q-o-q to 15% in Q4FY21. The EBITDA margin were impacted by higher freight rates during Q4FY21.
- **Positive management commentary:** The management was cautiously optimistic about the recovery in medium term, though the management cautioned near term challenges of COVID wave-2 in India and chips supply shortage globally. The company expects domestic demand to gradually recover from Q2FY22 onwards, on the back of normalisation of economic activities. However, the company do not expect a sharp recovery in automobile as witnessed last year after lockdowns. The company expects to grow at faster pace than the industry, given its leadership and dominant positions in its businesses. The management expects robust business traction in medium-term, aided by introducing new products to existing clients and selling old products to new clients. The company is operating at more than a 90% capacity in all its plans, aided by strong pick-up in both OEM as well as replacement markets. Suprajit witnessed encouraging sales in South India. Considering the buoyant demand and continued business traction, management has planned to increase its capacity of lamps and cable businesses to be ready for the coming peak season. Capex requirement would be marginal at an additional Rs. 20-25 crore for this part of expansion. The company has taken up extension in the Narspura plant to meet the increased demand from one of its key customers. In addition, the company is comfortable position to increase its capacity at comfortable if its get new business orders at higher pace than expected.
- **Beneficiary of value proposition to its established and potential clients:** Suprajit continues to strengthen its value proposition to its domestic and global clients. The company has a strong foothold in the cable business in the automotive segment, where it holds 30%-35% market share. The company has a dominant 60%-65% market share in the two-wheeler cable business. As per estimates shared by the company, Suprajit has a 40%-45% market share in the cable business in Indian markets, including the non-automotive business. Key drivers for Suprajit's success are its ability to produce low-cost cables among domestic players, aided by its operational efficiency and dedicated plants for respective clients. Among global peers, the company benefits from its locational cost advantage. Corresponding to the cable business, Suprajit has similar cost advantages in its lamps division, where its key global competitors include Philips India Limited. The lean and low-cost employee structure and scale of operations help Suprajit maintain its competitive benefits across its product lines – automotive cable, non-automotive cables, and lamp business division.
- **Announcement of buyback and final dividend:** Suprajit announced share buyback of 15 lakhs shares at a price of Rs. 320/share in FY21. Strong cash generation during FY2021 led the company to cheer shareholders through announcing share buyback at a premium price and final dividend of 175%.
- **Strong financial performance:** Suprajit's financial performance has been strong throughout and has outperformed with its revenue outpacing growth of the underlying Indian automotive market. The company has also been able to generate healthy margins, return on capital employed, and generate healthy free

cash flows consistently. The company's earnings CAGR of 5% and average RoCE of 19% over FY2018-FY2020 are better than most auto-ancillary companies, given the sharp decline in automobile sales in FY2019 and FY2020, impacted by COVID-19 pandemic.

- **Reduction in debt levels:** The company has reduced its debt further to Rs. 327.7 crore as on March 31, 2020 from Rs. 380.3 crore as on March 31, 2020.
- **Strong broad-based growth; Expect robust double-digit growth in FY2022:** The company has a strong long-term revenue visibility, given its strong position in the cable and lamps business. We expect Suprajit's earnings to report a 26.3% CAGR during FY2021E-FY2023E, driven by an 19.2% revenue CAGR and 130 bps improvement in EBITDA margin, with its ROCE improving back to ~20% in FY23E. The company is open to grow inorganically in the auto ancillary space and diversify its portfolio. The company has a history of acquiring companies for its expansion of customer base, new geographies, and increasing dominancy in its core business.

Results (Consolidated) Rs cr

Particulars	Q4FY21	Q4FY20	Y-o-Y %	Q3FY21	Q-o-Q %
Revenues	513.0	389.0	31.9	507.3	1.1
EBITDA	81.7	54.9	48.8	86.4	-5.4
EBITDA Margins (%)	15.9	14.1	180 bps	17.0	(110 bps)
Depreciation	14.3	14.5	-1.2	14.3	(0.3)
Interest	2.8	5.7	(51.6)	5.4	(48.8)
Other income	12.2	4.2	187.8	7.0	73.6
PBT	76.8	39.0	97.2	73.6	4.3
Tax	19.3	8.6	125.7	22.0	-12.2
Adjusted PAT	57.5	30.4	89.1	51.6	11.4
Reported PAT	57.5	3.0	1835.8	51.6	11.4
Adjusted EPS (Rs)	4.1	2.2	89.1	3.7	11.4

Source: Company; Sharekhan Research

Divisional Performance

Particulars	Q4FY21	Q4FY20	Y-o-Y %	Q3FY21	Q-o-Q %
Phoenix Lamps Division (Including Trifa & Luxlite)					
Operating revenue	101.8	73.2	39.0	100.6	1.2
EBITDA (Operational)	14.0	3.2	345.1	11.6	21.1
EBITDA margin (%)	13.8	4.3	950 bps	11.5	230 bps
SENA Division (including India and Wescon US)					
Operating revenue	104.4	86.7	20.4	91.2	14.5
EBITDA (Operational)	21.7	10.5	106.0	10.9	100.1
EBITDA margin (%)	20.8	12.2	860 bps	11.9	890 bps
Automotive Cable division					
Operating revenue	306.8	229.1	33.9	315.5	(2.8)
EBITDA (Operational)	46.0	41.2	11.5	63.9	(28.1)
EBITDA margin (%)	15.0	18.0	(300 bps)	20.3	(530 bps)

Source: Company; Sharekhan Research

Outlook and Valuation

■ Sector Outlook – Demand remains strong in both domestic and export markets, while near-term supply disruption remain a challenge

Business outlook for the automotive segment is expected to improve with normalisation of economic activities. Automotive demand is expected to witness recovery in two-wheeler and four-wheeler segments, aided by pent-up demand and increased personal mobility transport. Rural and semi-urban remain buoyant on robust farm income previous year, large reservoir and early arrival of monsoon. Recovery in export destinations is auguring well for the sector. Moreover, exports provide huge growth potential, given India's cost-effective manufacturing, being geographically closer to key markets of Middle East and Europe and being the second largest producer of key raw material, steel. Rollout of COVID-19 vaccination programmes in many countries is keeping the overall outlook positive for the coming months, following the respective approval of various vaccines. Auto component exports are expected to grow from $15 billion to $80 billion by FY2027.

■ Company outlook – Beneficiary of two-wheeler and PV demand

Suprajit is one of the largest manufacturers of mechanical control cables with a presence in both automotive and non-automotive segments. Revenue growth has been healthy in the pre-COVID regime, driven by a steady offtake and diversification into aftermarket and exports segments. The company has entered segments such as lamps and has started catering to non-automotive segments through acquisitions and has augmented capacities in the cables business. The company has been gaining market share in the domestic cable division with increased share of business with automotive clients. The company's market share in two-wheelers is 60-65%, while that for the automotive business is at 30%-35%. Market share for the Indian market is at 40%-45%. The aftersales market, both at Suprajit and Phoenix Lamps division, has been strong along with encouraging offtake from OEMS. The company is in talks with leading PV players such as Maruti Suzuki to further increase sourcing. In non-automotive cables, the company is planning to enter into new segments such as medical device equipment, consumer durables, and agriculture and construction equipment, which would drive growth. Under the lighting segment, Suprajit has recently acquired Osram manufacturing facility for halogen lamps to become the world's third largest player and is expanding its presence in the aftermarket segment by entering into new geographies. We expect Suprajit to continue outpacing the domestic automotive OEM industry.

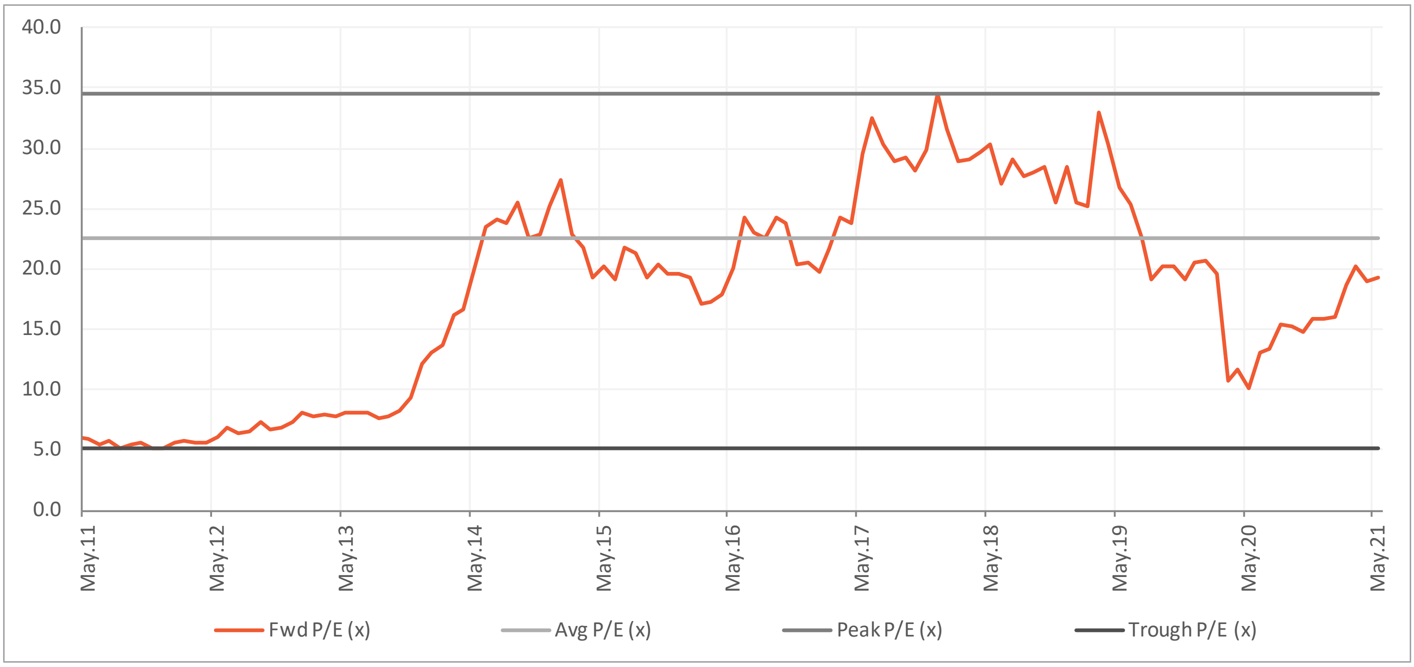
■ Valuation – Maintain Buy with an unchanged PT of Rs. 329

Suprajit would continue to gain wallet share from customers in the cable segment (domestic PV segment and higher sourcing by global OEM) and Phoenix Lamps (increased sourcing by Osram). Further, the company would continue to enter new segments in the non-automotive cable division. We expect FY2022 to be a strong year, driven by normalisation of economic activity and improving demand. Operating leverage coupled with cost-control measures would help in margin improvement. We have maintained our earnings estimates, driven by the company's leadership position in cable business. Propelled by robust business outlook and prudent capital allocation, we expect Suprajit's consolidated earnings to report a 26.3% CAGR during FY2021E-FY2023E, driven by an 19.2% revenue CAGR and 130 bps improvement in EBITDA margin, with its ROCE improving back to ~20% in FY23E. The stock is trading at 25-30% discount to its average historical P/E multiple of 16.2x and EV/EBITDA multiple of 10.4x its FY2023E estimates. We retain our Buy rating on the stock with an unchanged PT of Rs. 329.

Price Target Calculation	Rs/Share
FY23E EPS	16.5
Target P/E Multiple (x)	20
Target Price	329
CMP	267
Upside (%)	23

Source: Company; Sharekhan Research

One-year forward P/E (x) band



Source: Sharekhan Research

Peer Comparison

Particulars	CMP Rs/ Share	P/E (x)			EV/EBIDTA (x)			RoCE (%)		
		FY21	FY22E	FY23E	FY21	FY22E	FY23E	FY21	FY22E	FY23E
Suprajit Engineering	267	25.9	20.0	16.2	16.7	12.8	10.4	16.0	18.4	19.9
Schaeffler India Limited*	5300	56.9	37.7	28.6	28.6	20.6	15.8	12.4	16.7	18.9
Sundram Fasteners Limited	793	46.1	37.4	27.5	25.0	21.1	16.4	16.0	18.2	21.6

*Source: Company, Sharekhan estimates; * Financial are for CY20, CY21E and CY22E*

About company

Suprajit is a global leader in the automotive cable and halogen bulb industry. With a competitive manufacturing base in India, UK, US, and Mexico, along with technical and logistical supports worldwide, the company provides optimal product development and manufacturing solutions to its domestic and international customers. With a CAGR of over 25%, Suprajit has one of the largest manufacturing capacities in the world with 300+ million cables per year and 110+ million bulbs per year. Suprajit is a well-diversified company deriving 60% of its revenue from global operations, while 40% of revenue is derived domestically. 2W is the largest segment contributing 37% to revenue, while 20% revenue is derived from the automotive (4W) segment. Aftermarket constitutes 23% of revenue, while the non-automotive segment constitutes 20% of revenue.

Investment theme

Suprajit is one of the largest manufacturers of mechanical control cables with a presence in both automotive and non-automotive segments. Revenue growth has been healthy in the pre-COVID regime, driven by steady offtake and diversification into aftermarket and exports segments. The company continues to strengthen its value proposition to its domestic and global clients, aided by its leadership position in the domestic cable business and locational advantage to its global peers. Key drivers for Suprajit's success are its ability to produce low-cost cables among domestic players, aided by its operational efficiency and dedicated plants for respective clients. The company has entered segments such as lamps and has started catering to non-automotive segments through acquisitions and has augmented capacities in the cables business. The company has been gaining market share in the domestic cable division with increased share of business with automotive clients. The company's market share in 2W is 60%-65%, while that for automotive business at 30%-35%. Market share in the Indian market is 40%-45%. The aftersales market both at Suprajit and Phoenix Lamps division has been strong along with encouraging offtake from OEMS. We expect Suprajit to benefit from strong demand witnessed in domestic as well as export markets, aided by recovery in economic activities. The company will also benefit from its capex plan strategy, which will help it capitalise further in the next peak season.

Key Risks

- Chips supply shortage, rising commodity prices and prolonged lockdowns due to COVID wave-2 remains a key concerns.
- Delayed approval from OEMs for incremental business could impact performance.

Additional Data

Key management personnel

Ajith Rai	Executive Chairman
Mohan N.S	Managing Director & Group CEO
Peter Greensmith	CEO-Suprajit Europe
Steve Fricker	CEO-Wescon Controls
Medappa Gowda J	CFO & Company Secretary

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	SUPRIYAJITH FAMILY TRUST	38.0
2	DSP Small Cap Fund	5.3
3	HDFC Small Cap Fund	5.2
4	Sundaram-Clayton Ltd.	4.1
5	Kula Ajith Kumar Rai	2.7
6	TVS Motor Co. Ltd.	2.1
7	Shobita Punja	1.4
8	Emerging Securities Pvt. Ltd.	1.4
9	India Capital Fund Limited	1.4
10	Kula Ramprasad Rai	1.3

Source: Bloomberg

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