

AIA Engineering Ltd

BUY

CMP Rs1,660

Target Rs1,948

Upside 17%

Growing share via value added offerings; Retain 'BUY': We retain FY22 volume estimates at 296k MT assuming i) Increase in annual grinding media volumes by 20-25k MT on a normalized base of FY20, ii) Approx. 10k MT contribution from mill lining solutions & ~70bps margin expansion over FY20-22 led by benefits of INR depreciation (~75% exports), launch of relatively high margin value added mill lining solutions & operating leverage play. The stock is currently trading at 24x FY22E earnings. It deserves premium multiple due to strong business MOAT. We remain optimistic on the business prospects with adjusted ROE (ex-cash) of 28% by FY22E, healthy FCF generation, prudent capital allocation & strong balance sheet. Retain 'BUY' with TP of Rs1948 at 28x FY22 EPS.

Management outlook: AIAE has ramped up its operations & supply chain arrangements to pre-Covid levels now. Demand continues to improve at decent rate across all geographies. However, its management refrained from giving out guidance for FY21 as 2nd wave of pandemic has started in few countries. Mgmt. seems confident of achieving volume of ~130kMT in H2FY21. (Total volumes of ~250kMT in FY21E).

Growth prospects intact: Mining market continues to be AIAE's growth engine. It represents a large opportunity for conversion of conventional forged grinding media to high chrome grinding media. Management is extremely bullish on medium to long term business prospects from Gold & Copper mining. Annual consumption of grinding media for the mining segment is estimated at 2.5mn tons with less than 20% of the same converted to high chrome, thus offering a sizeable growth opportunity of conversion.

Value added offerings like EEMS product solutions to aid in growth FY22E onwards: AIAE increasing its wallet share with Mill linings which has ~0.3mn tons global market and represents a growth opportunity. It is focusing on effective penetration through, a) Ability to offer significant reduction in the grinding media cost through use of high chrome media in place of forged media resulting in much lower wear rates, b) Reduction of costly consumables in the down process by using high chrome grinding media & thereby improving recoveries, c) Optimization via unique high chrome mill lining solutions resulting into higher throughputs & cost reduction.

Resilient performance in Q2FY21: AIAE has delivered volume growth of 12% yoy in a challenging environment, which in our view is certainly commendable. Brazil & South Africa markets are also opening up gradually like India. Gold plants are running at full throttle, copper is largely linked to electronics customers and consumption there hasn't shrunk as well. Iron ore is linked to infrastructure, and AIAE sees reasonable encouraging signals from its customers on that front.

Exhibit 1: Financial Summary (Consolidated)

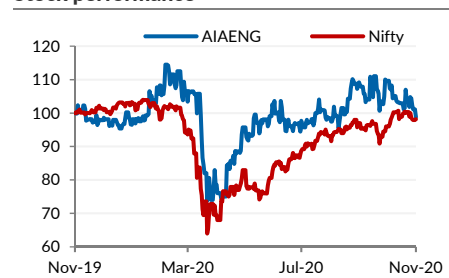
Y/e 31 Mar (Rs mn)	FY18	FY19	FY20	FY21E	FY22E
Revenues	24,451	30,695	29,809	27,596	33,651
yoy growth (%)	8.9	25.5	(2.9)	(7.4)	21.9
EBITDAM (%)	21.9	21.5	22.8	23.0	23.5
Adjusted PAT	4,434	5,108	5,903	5,384	6,562
yoy growth (%)	(2.9)	15.2	15.6	(8.8)	21.9
EPS (Rs)	47.0	54.2	62.6	57.1	69.6
P/E (x)	35.3	30.7	26.5	29.1	23.9
P/BV (x)	5.2	4.5	4.2	3.8	3.4
EV/EBITDA (x)	26.9	21.9	20.8	21.1	17.0
Net D/E (x)	(0.4)	(0.4)	(0.4)	(0.5)	(0.5)
ROE (%)	15.5	15.7	16.4	13.8	15.1
Core ROIC (%)	19.4	19.6	19.8	18.4	22.5

Source: Company, YES Sec - Research

Stock data (as on November 2, 2020)

Nifty:	11,669
52 Week h/l (Rs)	1990 / 1102
Market cap (Rs/USD bn)	156572 / 2103
Outstanding Shares	94
6m Avg t/o (Rs mn):	82
Div yield (%):	1.6
Bloomberg code:	AIAE IN
NSE code:	AIAENG

Stock performance



	1M	3M	1Y
Absolute return	(9.9%)	0.4%	0.5%

Shareholding pattern (As of Sept'20 end)

Promoter	58.5%
FII+DII	38.4%
Others	3.1%

Δ in earnings estimates

	FY21e	FY22e
EPS (New)	57.1	69.6
EPS (Old)	55.9	69.6
% change	2%	0%

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New client acquisition may incur some delay in near term due to travel restrictions:

There will be gradual recovery in developmental activities and customer acquisition in near term for mill liners as crucial activities like exchange of information and physical experimentation on the customer end have not recovered yet fully. Mgmt. believes the activities to gather steam once international travel restrictions are lifted. Mgmt. also expects all countries to come up with an infrastructure stimulus which would ultimately increase the demand for AIAE's customers products as infra stimulus would boost demand for cement and iron ores

Other Highlights

- ✓ Capex planned for FY21: Rs2.5bn, FY22: Rs2.5bn (assuming 50k grinding media expansion)
- ✓ Working capital has come down to Rs9.7bn from Rs12bn in Q4FY20.
- ✓ Cash balance stood at Rs17.5bn
- ✓ It had a foreign exchange gain of Rs45mn for Q2FY21
- ✓ INR realization rate was at 75, up 7% yoy.
- ✓ The company did not see a single customer failing to pay or running in an overdue situation. AIAE also made its payments to vendors on time
- ✓ Tax rate for FY21 would be 22%.
- ✓ MIES Scheme ended on 31st August 2020 & RODTEP scheme expected to be in effect from 1st January 2021.
- ✓ Anti-dumping duties from various countries like Brazil won't have a significant impact on AIA's business prospects as company is following fair business practices with no undercutting of product prices.

Key highlights Q2FY21 Consolidated Results:

- ✓ Consolidated sales increased by 6.6% yoy to Rs7.4bn (+23% vs our est.) as volume grew by 12% yoy while realizations dropped by 5% yoy.
- ✓ Mining/Non-mining volume growth at 15.8%/4.6% yoy respectively.
- ✓ Production volume growth of 30% yoy to 76,936t.
- ✓ EBITDA margin came in at 25.6%, up 352bps yoy (+281bps vs our est.)
- ✓ Absolute EBITDA at Rs1.9bn, up 23.5% & was 38% ahead of our estimates.
- ✓ Other income decreased by 12% to Rs248mn.
- ✓ PBT reported 20% yoy growth, however PAT came in at Rs1.5bn, down 3% yoy (+20% vs our est.) due to unfavorable tax cost base of Q2FY20.
- ✓ Cash flow from operations for H1FY21 was at Rs3.95bn vs Rs4.3bn in H1FY20 & Rs6.8bn in FY20.
- ✓ Debtors/Inventory/Creditors days was at 64/101/20 days respectively (vs 80/95/16 days).

Exhibit 2: Result table (Consolidated)

(Rs mn)	Q2 FY21	Q2 FY20	% yoy	Q1 FY21	% qoq
Total sales	7,423	6,966	6.6	5,803	27.9
EBITDA	1,903	1,541	23.5	1,235	54.1
EBITDAM (%)	25.6	22.1	351.6	21.3	435.5
Depreciation	(233)	(222)	5.0	(251)	(7.1)
Interest	(12)	(15)	(18.2)	(14)	(11.4)
Other income	248	281	(11.8)	748	(66.9)
PBT	1,905	1,584	20.3	1,717	10.9
Tax	(433)	(64)	576.3	(424)	2.3
Minority Interest	5	2	108.6	(1)	(900.9)
Recurring PAT	1,477	1,522	(3.0)	1,293	14.2
Adj. EBITDA	1,948	1,596	22.1	1,615	20.6
Adj. EBITDA/Kg	28.4	26.1	9.0	30.4	(6.5)

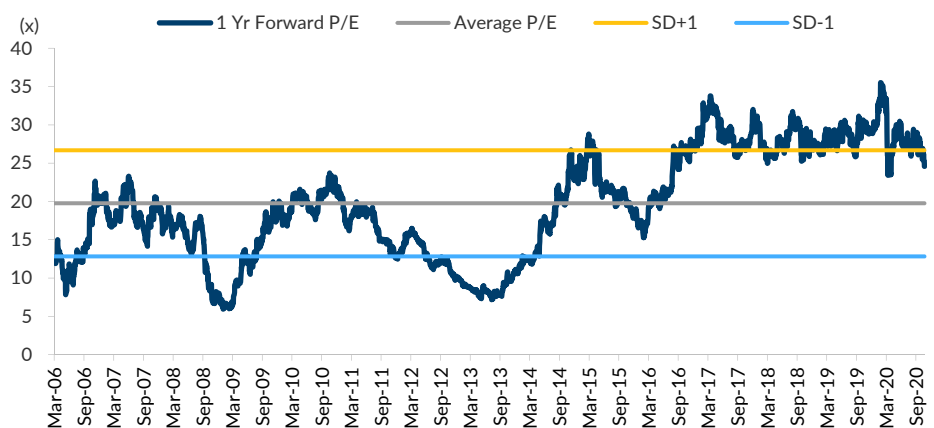
Source: Company, YES Sec – Research

Exhibit 3: Cost analysis (Consolidated)

As a % of net sales	Q2 FY21	Q2 FY20	bps yoy	Q1 FY21	bps qoq
COGS	33.8	39.9	(609.1)	39.3	(544.0)
Employee cost	4.5	4.9	(42.8)	5.7	(121.8)
Other expenses	36.1	33.0	300.3	33.7	230.3
Total costs	74.4	77.9	(351.6)	78.7	(435.5)

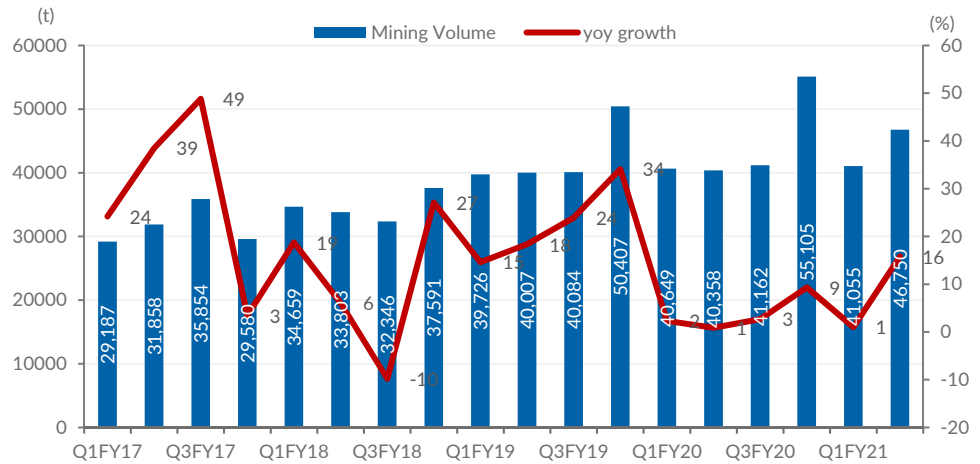
Source: Company, YES Sec – Research

Exhibit 4: AIAE's deserves premium multiple due to strong business MOAT & healthy balance sheet with net cash of Rs17.5bn & Core RoE of 28%



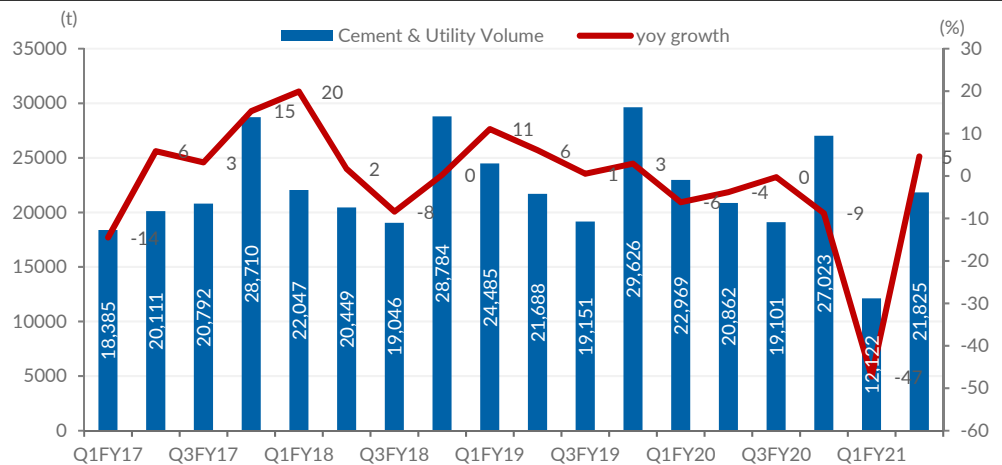
Source: Company, YES Sec – Research

Exhibit 5: Mining segment volume grew 16% yoy in difficult times



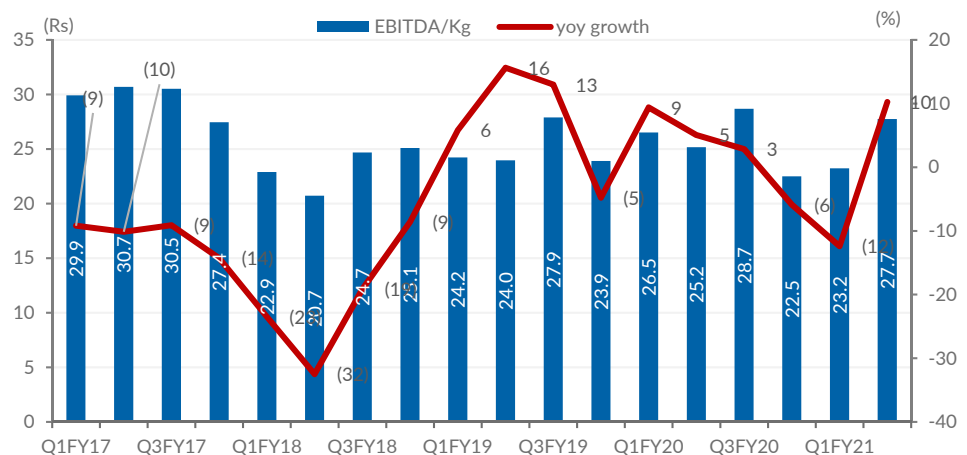
Source: Company, YES Sec – Research

Exhibit 6: Non-mining segment volumes were up 4.6% yoy



Source: Company, YES Sec – Research

Exhibit 7: EBITDA/Kg increased 10% yoy in Q2FY21



Source: Company, YES Sec – Research

FINANCIALS (CONSOLIDATED)

Exhibit 8: Income statement

Y/e 31 Mar (Rs mn)	FY18	FY19	FY20	FY21E	FY22E
Total operating revenues	24,451	30,695	29,809	27,596	33,651
Growth (%)	8.9	25.5	(2.9)	(7.4)	21.9
EBITDA	5,357	6,599	6,803	6,356	7,921
EBITDA margin (%)	21.9	21.5	22.8	23.0	23.5
Growth (%)	(15.6)	23.2	3.1	(6.6)	24.6
Depreciation & amortization	656	788	979	1,080	1,280
EBIT	4,701	5,811	5,824	5,276	6,641
EBIT margin (%)	19.2	18.9	19.5	19.1	19.7
Interest	69	75	56	51	48
Other income	1,218	1,209	1,419	1,755	1,820
Profit before tax	5,850	6,944	7,187	6,981	8,413
Tax	1,414	1,830	1,284	1,596	1,851
Associate income	0	0	0	0	0
Minority interest	(3)	(6)	0	0	0
Reported net profit	4,436	5,114	5,903	5,384	6,562
Extraordinary items	206	65	39	37	0
Adjusted net profit	4,227	5,043	5,864	5,348	6,562
Adjusted net margin (%)	17.3	16.4	19.7	19.4	19.5
Diluted EPS (Rs)	47.0	54.2	62.6	57.1	69.6
Growth (%)	(2.9)	15.2	15.6	(8.8)	21.9

Exhibit 9: Balance sheet

Y/e 31 Mar (Rs mn)	FY18	FY19	FY20	FY21E	FY22E
SOURCE OF FUNDS					
Share capital	189	189	189	189	189
Reserve & Surplus	29,904	34,948	36,824	40,923	45,896
Total shareholder's funds	30,093	35,137	37,013	41,112	46,085
Minority Interest	89	93	93	93	93
Debt	1,231	1,279	969	753	716
Deferred tax liabilities/(assets)	820	962	890	1,130	1,168
TOTAL	32,234	37,471	38,965	43,088	48,061
APPLICATION OF FUNDS					
Fixed assets	11,660	14,184	15,613	18,388	20,888
Less: Depn. and amort.	4,949	5,737	6,716	7,796	9,076
Net block	6,711	8,447	8,897	10,592	11,812
Capital WIP	968	598	323	300	300
Long term investments	9	9	9	8	8
Other long term assets	927	667	925	752	752
Inventories	5,534	7,859	7,781	6,804	8,298
Debtors	6,002	7,103	6,508	6,048	7,376
Cash & cash equivalents	13,560	13,600	15,725	23,214	23,008
Loans & advances	507	794	432	454	369
Other current assets	1,368	1,251	1,022	(2,469)	(555)
Total current liabilities	3,351	2,857	2,657	2,615	3,307
Net current assets	23,620	27,750	28,811	31,435	35,188
TOTAL	32,234	37,471	38,965	43,088	48,061

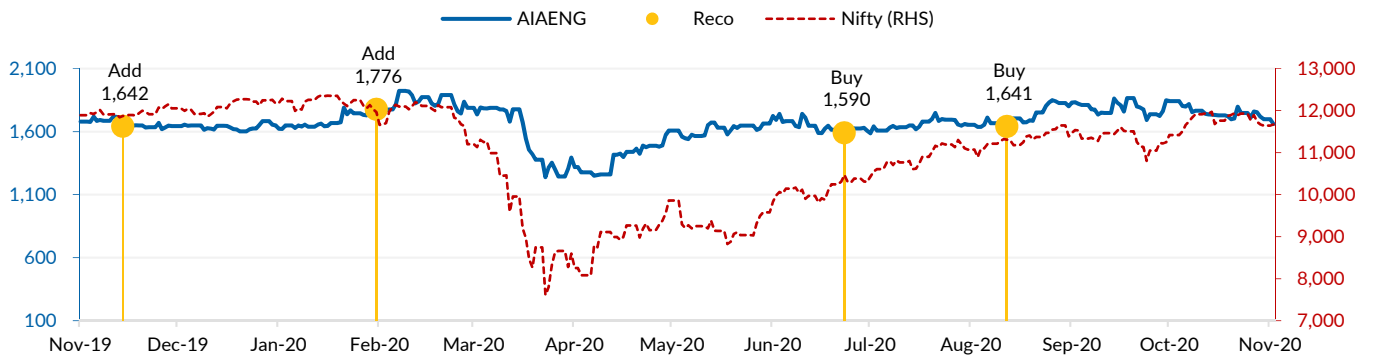
Exhibit 10: Cash flow statement

Y/e 31 Mar (Rs mn)	FY18	FY19	FY20	FY21E	FY22E
PBT	5,850	6,944	7,187	6,981	8,413
Depreciation	656	789	979	1,080	1,280
Others	(902)	(1,038)	(1,108)	(37)	0
Tax Paid	(1,609)	(1,805)	(1,493)	(1,596)	(1,851)
Changes in Working Capital	(1,053)	(2,992)	1,229	4,865	(3,958)
Net Cash from Operations	2,942	1,897	6,793	11,292	3,884
Capex	(1,371)	(2,065)	(1,310)	(2,579)	(2,500)
Change in Investment	(718)	185	(2,045)	1	0
Others	126	241	248	0	0
Net Cash from Investing	(1,964)	(1,638)	(3,107)	(2,578)	(2,500)
Change in debt	0	72	(203)	(216)	(38)
Change in Equity	0	0	0	(0)	(0)
Others	(1,583)	(73)	(4,085)	(1,009)	(1,552)
Net Cash from Financing	(1,583)	(1)	(4,288)	(1,225)	(1,589)
Net Change in Cash	(604)	258	(602)	7,489	(206)
Free cash flow (FCF)	1,031	314	3,732	8,753	1,421

Exhibit 11: Ratio analysis

Y/e 31 Mar (Rs mn)	FY18	FY19	FY20	FY21E	FY22E
PROFITABILITY RATIOS					
EBITDA Margin (%)	21.9	21.5	22.8	23.0	23.5
Adjusted net margin (%)	17.3	16.4	19.7	19.5	19.5
Return on invested capital (%)	19.4	19.6	19.8	18.4	22.5
Return on equity (%)	15.5	15.7	16.4	13.8	15.1
EFFICIENCY RATIOS					
Asset Turnover	3.2	3.4	3.2	2.5	2.8
Debt to equity	0.0	0.0	0.0	0.0	0.0
Net debt to equity	(0.4)	(0.4)	(0.4)	(0.5)	(0.5)
Interest coverage	67.9	77.0	104.2	104.4	138.4
Debtor days	89.6	84.5	79.7	80.0	80.0
Inventory days	82.6	93.5	95.3	90.0	90.0
Payable days	24.4	20.6	16.2	18.0	20.0
PER SHARE DATA					
Diluted EPS (Rs)	47.0	54.2	62.6	57.1	69.6
Book value per share (Rs)	319.1	372.5	392.4	435.9	488.6
DPS (Rs)	8.0	9.0	27.0	11.3	14.3
VALUATION RATIOS					
P/E	35.3	30.7	26.5	29.1	23.9
P/BV	5.2	4.5	4.2	3.8	3.4
EV/EBITDA	26.9	21.9	20.8	21.1	17.0
Dividend Yield (%)	0.5	0.5	1.6	0.7	0.9

Recommendation Tracker



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