Sharekhan by BNP PARIBAS

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Stock Update

Suprajit Engineering Limited

Strong business outlook driven by automotive segment

Automobiles	Sharekhan code: SUPRAJIT	Result 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. 256**	
Price Target: **Rs. 300**	↑

↑ Upgrade ↔ Maintain ↓ Downgrade

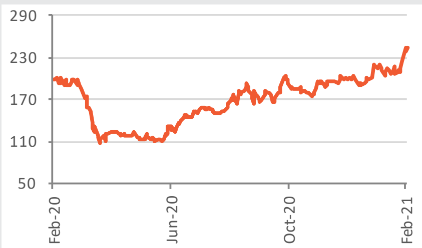
Company details

Market cap:	Rs. 3,581 cr
52-week high/low:	Rs. 252 / 100
NSE volume: (No of shares)	2.23 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	12.6	24.5	53.3	22.0
Relative to Sensex	7.4	4.1	18.4	-2.2

Sharekhan Research, Bloomberg

Summary

- We reiterate our Buy rating on Suprajit Engineering Limited (SUPRAJIT) with a revised PT of Rs. 300, factoring its long-term average multiples, owing to its strong business outlook and earnings upgrade.
- SUPRAJIT reported strong set of numbers in Q3FY21 results, exceeding our estimates on all the key parameters.
- We expect SUPRAJIT's consolidated earnings to grow robust by 40.8% in FY2022E and 23.4% in FY2023E, driven by 19.0% CAGR during FY2021E-FY2023E and 160 bps improvement in EBITDA margin.
- The stock is trading below its average historical multiple at P/E multiple of 15.6x and EV/EBITDA multiple of 10.1x its FY2023E estimates. We retain our Buy rating.

Suprajit Engineering Limited (SUPRAJIT) reported a strong set of numbers in Q3FY21 results, exceeding our estimates on all the key parameters. Revenues was higher by 9.8% from our estimates, while PAT was higher by 43%, mainly due to improved margins. Net revenue grew by 23% y-o-y at Rs 507 crore in Q3FY21, as compared to Rs 412 crore in Q2FY20, on the back of recovery in automotive and non-automotive business. The operating profit margin for the Q3FY21 stood at 17% showing an improvement of 488 bps y-o-y and 44 bps q-o-q 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 72.4% y-o-y and 17.5 q-o-q to Rs 86 crore. PAT grew by 65.6% y-o-y and 7.4% q-o-q to Rs 52 crore. The company also benefitted from the increase in components per unit and improvement in wallet share with key customers. 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 started catering to non-automotive segments, through acquisitions, and augmented capacities in the cables business. The company has been gaining market share in the domestic cable division with an increased share of business with automotive clients. Its market shares in 2Ws is 60-65%, while for automotive business at 30-35% and Indian markets at 40-45%. The aftersales market, both at SUPRAJIT and Phoenix Lamps division have been strong along with encouraging offtake from OEMS. We expect SUPRAJIT to be beneficiary of the strong demand witnessed in the domestic as well as export markets. The company will also benefit from its capex plans, which will help it further to capitalise in the next peak season. We expect SUPRAJIT's consolidated earnings to grow robust by 40.8% in FY2022E and 23.4% in FY2023E, driven by 19.0% CAGR during FY2021E-FY2023E and 160 bps improvement in EBITDA margin. Hence, we retain our Buy rating on the stock.

Our Call

Valuation - Maintain Buy with a revised PT of Rs. 300

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) and enter new segments in the non-automotive cable division. We expect FY2022 to be a strong recovery year, driven by normalisation of economic activity and improvement in demand. Operating leverage coupled with cost-control measures would help in margin improvement. We have increased our earnings estimates to reflect strong growth momentum and impact of improved EBITDA margins. We expect SUPRAJIT's consolidated earnings to grow by 40.8% in FY2022E and 23.4% in FY2023E, driven by 19.0% CAGR during FY2021E-FY2023E and 160 bps improvement in EBITDA margin. The stock is trading below its average historical multiple at P/E multiple of 15.6x and EV/EBITDA multiple of 10.1x its FY2023E estimates. We retain our Buy rating on the stock with revised PT of Rs 300.

Key Risks

The company's performance can be impacted adversely if commodity prices continue to rise in the current pace and the fear of COVID gets more aggravated in Europe and Americas. Also, the delayed approval from OEMs for incremental business may impact performance.

Valuation (Consolidated) Rs cr

Particulars	FY19	FY20	FY21E	FY22E	FY23E
Revenues	1,590	1,563	1,641	2,018	2,322
Growth (%)	11.1	(1.7)	5.0	23.0	15.0
EBIDTA	233	219	231	305	364
OPM (%)	14.6	14.0	14.1	15.1	15.7
Net Profit	134	104	131	184	227
Growth (%)	(3.4)	(22.3)	25.6	40.8	23.4
EPS	9.6	7.4	9.4	13.3	16.4
P/E	26.8	34.4	27.1	19.3	15.6
P/BV	4.6	4.2	3.7	3.3	2.8
EV/EBIDTA	16.5	17.5	16.4	12.3	10.1
ROE (%)	17.3	12.2	13.7	16.9	18.0
ROCE (%)	20.0	14.7	15.0	18.4	20.0

Source: Company; Sharekhan estimates

- **Q3FY21 results ahead of expectations:** Suprajit Engineering Limited (SUPRAJIT) reported a strong set of numbers in Q3FY21 results, exceeding our estimates on all the key parameters. Revenues was higher by 9.8% from our estimates, while PAT was higher by 43%, mainly due to improved margins. Net revenue grew by 23% y-o-y at Rs 507 crore in Q3FY21, as compared to Rs 412 crore in Q2FY20, on the back of recovery in automotive and non-automotive business. The two-wheeler business contributed 37% of total revenues, while aftermarket and non-automotive business contributed 23% and 20% respectively during the Q3. The operating profit margin for the Q3FY21 stood at 17% showing an improvement of 488 bps y-o-y and 44 bps q-o-q 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 72.4% y-o-y and 17.5 q-o-q to Rs 86 crore. PAT grew by 65.6% y-o-y and 7.4% q-o-q to Rs 52 crore. The company also benefitted from the increase in components per unit and improvement in wallet share with key customers.
- **Strong hold in Cable business:** The company continued its strong foothold in the cable business. Its market shares in 2Ws is 60-65%, while for automotive business at 30-35% and Indian markets at 40-45%. The aftersales market, both at SUPRAJIT and Phoenix Lamps division have been strong along with encouraging offtake from OEMS.
- **Management's outlook positive:** The management of SUPRAJIT were positive on the growth registered in the Q3FY21, on the back of robust demand witnessed across its segments. The strong underlying demand pushed the management to expedite its capex plans. The company is operating at more than 90% capacity in all its plans, aided by strong pick-up in both, OEM as well as replacement markets. SUPRAJIT witnessed encouraging sales in Southern India. Considering the buoyant demand and continued business traction, the management has planned to increase its capacity of lamps and cable businesses to be ready for the coming peak season. The capex requirement would be marginal in the range of Rs20-25 crore additional for this part of expansion. The company has taken up an extension in the Narspura plant to meet the increased demand from one of its key customers.
- **Challenges:** Despite advocating strong demand, SUPRAJIT's management was concerned about the unprecedented rise in commodity prices, in-bound & out-bound freight rates and supply shortage of chips/semi-conductors. The company expects the situation to improve going forward but remained cautious. The company has a positive outlook for the Q4FY21 and expects the demand to remain strong. The company expects to marginalise the impact of raw material price rise partially through operating leverage benefit and cost rationalization.
- **Announcement of Buyback and interim dividend:** SUPRAJIT announced share buyback of 15 lakhs shares at a price of Rs 320/shares, almost 31% premium to market price. The strong cash generation during FY21, led the company to cheer shareholders through announcing share buy back at premium price and interim dividend of 75%.
- **Established automotive player, venturing into new businesses:** 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 past few years, driven by steady offtake and diversification into aftermarket and exports segments. The company has entered segments such as lamps, and started catering to non-automotive segments, through acquisitions, and augmented capacities in the cables business. The company is open to grow inorganically.
- **Reduction in debt levels:** The company has reduced its debt further to Rs 312.8 crore as on 31st December'20 from the Rs 380.3 crore as on 31st March'20.
- **Strong broad-based growth; Expect robust double-digit growth in FY2022:** The company has a strong long-term revenue visibility, given its strong positioning in cable and lamps business. We expect SUPRAJIT's consolidated earnings to grow by 40.8% in FY2022E and 23.4% in FY2023E, driven by 19.0% CAGR during FY2021E-FY2023E and 160 bps improvement in EBITDA margin.

Q3FY2021 results (Consolidated) Rs cr

Particulars	Q3FY21	Q3FY20	Y-o-Y %	Q2FY21	Q-o-Q %
Revenues	507.3	412.3	23.0	443.1	14.5
EBITDA	86.4	50.1	72.4	73.5	17.5
EBITDA Margins (%)	17.0	12.1	488 bps	16.6	44 bps
Depreciation	14.3	14.9	-3.8	14.4	(0.3)
Interest	5.4	5.2	4.8	5.5	(1.8)
Other income	7.0	5.3	33.4	8.6	-18.3
PBT	73.6	35.3	108.6	62.2	18.4
Tax	22.0	4.1	435.5	14.1	55.9
Adjusted PAT	51.6	31.2	65.6	48.1	7.4
Reported PAT	51.6	31.2	65.6	48.1	7.4
Adjusted EPS (Rs)	3.7	2.2	65.6	3.4	7.4

Source: Company; Sharekhan Research

Outlook and Valuation

■ Sector outlook – Demand picking up in domestic and export markets

The business outlook for the automotive segment is improving with a normalisation of economic activities. The automotive demand is witnessing strong recovery in two-wheeler and four-wheeler segments aided by pent-up demand, and an increase in personal mobility transport. The rural and semi-urban remains buoyant on robust farm income this year. The recovery in export destinations is auguring well for the sector. Also, exports provide huge growth potential given India's cost-effective manufacturing, being geographically closer to key markets of Middle East and Europe and being second largest producer of key raw material steel. The rolling out of COVID-19 vaccination programmes in many countries are keeping overall outlook positive for the coming months following the respective approval of various vaccines. Auto component exports are expected to grow from USD 15 billion to USD 80 billion by FY2027.

■ Company outlook - Beneficiary of 2W 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 started catering to non-automotive segments, through acquisitions, and 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. Its market shares in 2Ws is 60-65%, while for automotive business at 30-35% and Indian markets at 40-45%. The aftersales market, both at SUPRAJIT and Phoenix Lamps division have been strong along with encouraging offtake from OEMS. The company is in talks with leading passenger vehicle 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 a revised PT of Rs. 300

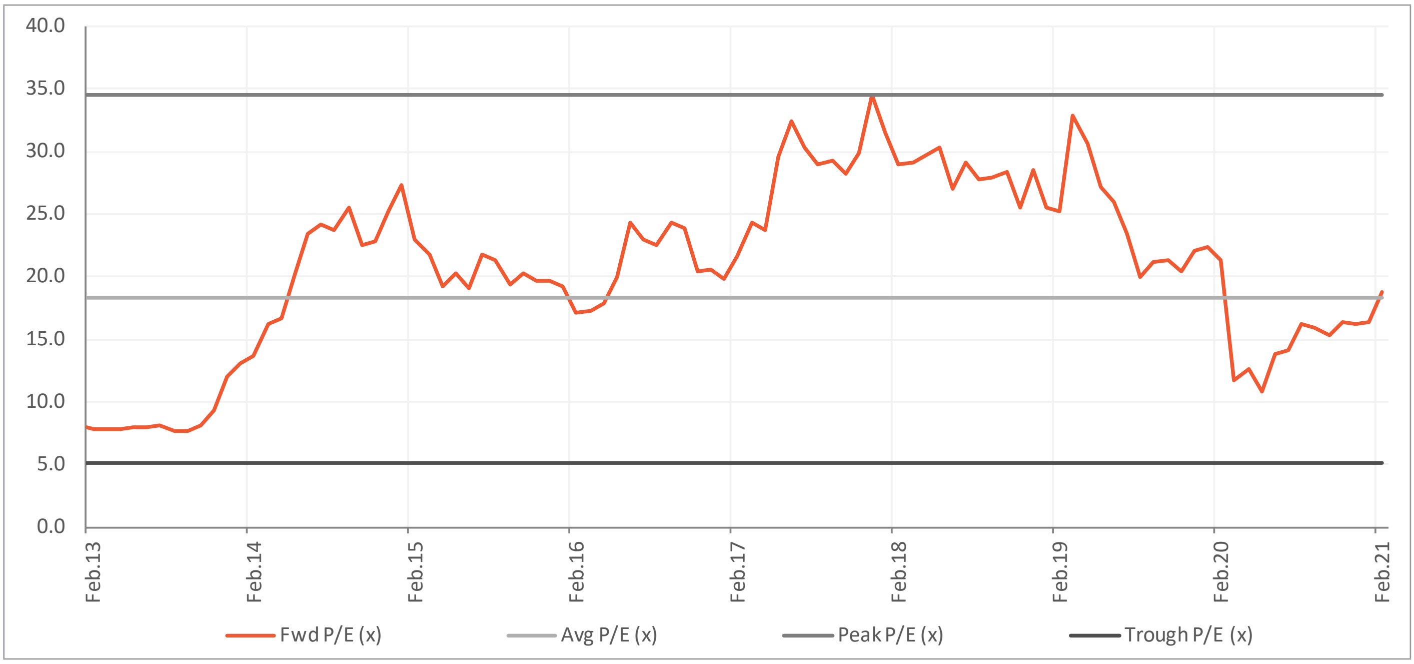
Suprajit would continue to gain wallet share from customers in the cable segment (domestic PV segment and higher sourcing by global OEM) and Phoenix Lamps (increased sourcing by Osram) and enter new segments in the non-automotive cable division. We expect FY2022 to be a strong recovery year, driven by normalisation of economic activity and improvement in demand. Operating leverage coupled with cost-control measures would help in margin improvement. We have increased our earnings estimates to reflect strong growth momentum and impact of improved EBITDA margins. We expect SUPRAJIT's consolidated earnings to grow by 40.8% in FY2022E and 23.4% in FY2023E, driven by 19.0% CAGR during FY2021E-FY2023E and 160 bps improvement in EBITDA margin. The stock is trading below its average historical multiple at P/E multiple of 15.6x and EV/EBITDA multiple of 10.1x its FY2023E estimates. We retain our Buy rating on the stock with revised PT of Rs 300.

Price Target calculation

	Rs/Share
FY23E EPS	16
Target P/E Multiple (x)	18
Target Price	300
CMP	256
Upside (%)	18

Source: Company; Sharekhan Research

One-year forward P/E (x) band



Source: Sharekhan Research

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 compounded annual growth 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% 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 has entered segments such as lamps, and started catering to non-automotive segments, through acquisitions, and 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. Its market shares in 2Ws is 60-65%, while for automotive business at 30-35% and Indian markets at 40-45%. The aftersales market, both at SUPRAJIT and Phoenix Lamps division have been strong along with encouraging offtake from OEMS. We expect SUPRAJIT to be the beneficiary of the strong demand witnessed in the domestic as well as export markets, aided by recovery in economic activities. The company will also benefit from its capex plans, which will help it further to capitalise in the next peak season. We expect SUPRAJIT's consolidated earnings to grow robust by 40.8% in FY2022E and 23.4% in FY2023E, driven by 19.0% CAGR during FY2021E-FY2023E and 160 bps improvement in EBITDA margin. Hence, we retain our Buy rating on the stock.

Key Risks

- The company's performance can be impacted adversely if the commodity prices continue to rise in the current pace and the fear of COVID gets more aggravated in Europe and Americas.
- 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	HDFC Asset Management Co Ltd	5.5
3	First State Investments ICVC	5.0
4	DSP Investment Managers Pvt Ltd	4.7
5	Sundaram-Clayton Ltd	4.1
6	Rai Kula Ajith Kumar	2.7
7	RAI K AJITH KUMAR	2.7
8	TVS Motor Co Ltd	2.1
9	Bajaj Allianz Life Insurance Co Ltd	1.5
10	PUNJA SHOBITA	1.4

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

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