

Swaraj Engines Ltd

A cherry pick in tough times!

Swaraj Engines (SWE) reported strong volume growth in Q4FY21, ahead of estimates, in-line with good show of overall tractor industry. Based on our recent survey, we believe Swaraj tractors continue to enjoy strong brand equity. The company reported revenues of Rs 3,049mn in Q4FY21, a growth of 74.1% YoY (up 11.9% QoQ), above our estimates. Volumes grew by 62.4% YoY to 33,831 units and blended realisation was higher by 7.2% to Rs 90,127 per unit. Good crop prices and expected normal monsoon should help the demand, but the high FY21 base will restrict the growth in prevailing uncertain economic situation. The company has maintained its track record of rewarding shareholders and declared a handsome dividend of Rs 69 per share for FY21. Considering sound fundamentals of SWE, we maintain our Buy rating on the stock with target price to Rs 1,669 (18.5x FY23e EPS).

Strong volume growth led to the strong operational performance

- Results came in above our expectation as the company reported a strong growth of 74.1% at topline level, led by volume growth of 62.4%.
- EBITDA Margin** came in at 15.1% in Q4FY21, ~180bps higher YoY. This is despite RM cost pressure as RM cost was higher 144 bps on YoY basis. With a higher scale of business, there was effect of positive operating leverage.
- Its persistent focus on operating costs resulted in lower employee costs as well as lower other expenses as a % of sales. Employee cost was lower by ~203bps YoY to 3.6% in Q4FY21, while other expense was at 4.0% as a % of sales, 120 bps lower YoY.
- Bottom line:** EBITDA grew by 97.5% YoY to Rs 462mn, while PAT grew by 105.6% YoY to Rs 326mn. Bottom line was above our estimates as the company posted highest ever quarterly profit.
- Dividend:** The Board has recommended an equity dividend of Rs 50 per share for FY21. Further, the Board, over and above the said normal dividend, has also recommended a special dividend payment of Rs 19 per share, taking the total dividend to Rs. 69 per share for FY21.

Tractor demand to be good on expected good monsoon, but growth capped on high base

- As per our recently concluded check with tractor dealers across zones, there is uncertainty in demand environment. However, ongoing peak season along with upright crop prices continues to support demand in April. The expectation for the month of May and June 2021 is better than March 2021 as crop prices are stable to slightly higher as compared to January-March levels.
- In addition, elections in most of the states will get over, and ongoing Covid vaccination program to reduce fear & uncertainty, which will lead to higher production and demand in the coming months. Reverse migration is also supporting demand. Tractor industry reported record numbers in FY21 and hence, most of the dealers indicated that it would be difficult to break records in FY22. This is despite expectations of normal monsoon, and better crop prices.

Valuation and risks:

- Swaraj has been giving higher dividend payouts and offering buyback schemes. We expect this trend should be continued as there is no major capex requirement and hence, return ratios to improve.
- At the current price of Rs 1,360, the stock is trading at 15.1x FY23e EPS. Assigning 1-year forward P/E of ~18.5x to FY23E, we arrive at a **target price of Rs 1,669 per share**, which indicates an **upside of ~23%**

| Y/E Mar (Rs mn) | Q4 FY21 | Q4 FY20 | YoY (%) | Q3 FY21 | QoQ (%) | Q4 FY21e | Var. (%) |
|--------------------------|--------------|--------------|----------------|--------------|----------------|--------------|----------------|
| Engine Sales (No) | 33,831 | 20,827 | 62.4 | 31,193 | 8.5 | 32,190 | 5.1 |
| Realisation (Rs) | 90,127 | 84,088 | 7.2 | 87,324 | 3.2 | 85,500 | 5.4 |
| Net sales | 3,049 | 1,751 | 74.1 | 2,724 | 11.9 | 2,752 | 10.8 |
| Operating costs | 2,587 | 1,518 | 70.5 | 2,358 | 9.7 | | |
| EBITDA | 462 | 234 | 97.5 | 366 | 26.2 | 380 | 21.4 |
| EBITDA Margin (%) | 15.1 | 13.4 | 180 bps | 13.4 | 171 bps | 13.8 | 133 bps |
| Depreciation | 47 | 49 | (3.9) | 52 | (8.9) | | |
| Interest | 0 | - | NA | 0 | NA | | |
| Other income | 22 | 30 | (24.3) | 22 | 1.4 | | |
| PBT | 437 | 214 | 103.9 | 336 | 29.9 | | |
| Provision for tax | 111 | 56 | 99.3 | 86 | 29.4 | | |
| Effective tax rate (%) | 25.5 | 26.1 | (59) bps | 25.6 | (11) bps | | |
| PAT (Reported) | 326 | 158 | 105.6 | 250 | 30.1 | 259 | 25.8 |
| NPM (%) | 10.7 | 9.0 | 163 bps | 9.2 | 149 bps | 9.4 | 127 bps |

Source: Company, EISEC Research

| Y/E Mar (Rs mn) | Revenue | YoY (%) | EBITDA | EBITDA (%) | Adj PAT | YoY (%) | EPS (Rs) | RoE (%) | RoCE (%) | P/E (x) | EV/EBITDA (x) |
|-----------------|---------|---------|--------|------------|---------|---------|----------|---------|----------|---------|---------------|
| FY19 | 8,717 | 13.0 | 1,316 | 15.1 | 824 | 2.9 | 68.0 | 35.3 | 34.4 | 24.4 | 14.1 |
| FY20 | 7,733 | (11.3) | 1,004 | 13.0 | 710 | (13.8) | 58.6 | 30.0 | 29.3 | 20.7 | 12.8 |
| FY21 | 9,866 | 27.6 | 1,357 | 13.8 | 925 | 30.3 | 76.2 | 35.8 | 35.5 | 17.8 | 10.9 |
| FY22e | 10,500 | 6.4 | 1,466 | 14.0 | 1,012 | 9.4 | 83.4 | 35.0 | 34.9 | 16.3 | 10.0 |
| FY23e | 11,161 | 6.3 | 1,569 | 14.1 | 1,096 | 8.2 | 90.2 | 34.6 | 34.6 | 15.1 | 9.0 |

Source: Company, EISEC Research Estimates



East India Securities Ltd
Excellent | Investment | Solutions

Rating: Buy Upside/(Downside): 22.8%
Current Price: 1,360 Target Price: 1,669

Earlier recommendation

Previous Rating: Buy
Previous Target Price: 1,663

Market data

| | |
|--|---------------------------|
| Bloomberg: | SWE IN |
| 52-week H/L (Rs): | 1,709/925 |
| Mcap (Rs bn/USD mn): | 16.5/219 |
| Shares outstanding (mn): | 12.1 |
| Free float: | 49.0% |
| Avg. daily vol. 3mth (3M Avg - in '000): | 17.0 |
| Face Value (Rs): | 10 |
| Group: | BSE Smallcap |
| Source: | Bloomberg, EISEC Research |

Shareholding pattern

| | Mar-21 | Dec-20 | Sep-20 | Jun-20 |
|---------------|--------|--------|--------|--------|
| Promoter | 52.2% | 52.2% | 52.2% | 52.2% |
| FIIs | 1.6% | 1.2% | 1.2% | 1.2% |
| DIIIs | 10.4% | 12.1% | 12.9% | 10.5% |
| Public/others | 35.8% | 34.6% | 33.7% | 36.1% |
| Source: | BSE | | | |

Price performance (%)*

| | 1M | 3M | 12M | 36M |
|----------------|-----|------|------|-------|
| BSE Smallcap | 1.5 | 10.8 | 90.8 | 14.3 |
| Swaraj Engines | 4.9 | 0.8 | 41.1 | -32.8 |

*as on 20th Apr 2021; Source: AceEquity, EISEC Research

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Valuation and Recommendations

Swaraj has been giving higher dividend payouts and offering buyback schemes. We expect this trend should be continued as there is no major capex requirement and hence, return ratios to improve going forward.

At the current price of Rs 1,360, the stock is trading at 15.1x FY23e EPS. Assigning 1-year forward P/E of ~18.5x to FY23e, we arrive at a target price of Rs 1,669 per share, which indicates an upside of ~23% from the current levels. Hence, we maintain our **'Buy'** rating.

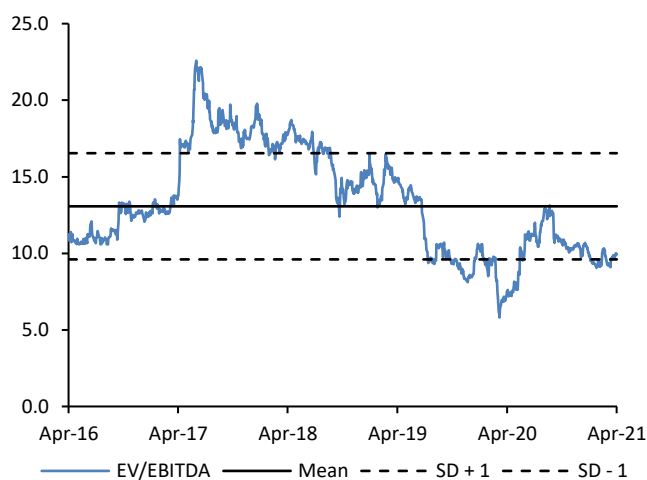
Key risks are company's dependence on a single client and lower than expected growth in the tractor industry.

Fig 1: 1-year forward P/E chart



Source: AceEquity, EISEC Research

Fig 2: 1-year forward EV/EBITDA chart



Source: AceEquity, EISEC Research

Quarterly financials, operating metrics and key performance indicators

Fig 3: Quarterly Financials

| Y/E March (Rs mn) | Q1 FY20 | Q2 FY20 | Q3 FY20 | Q4 FY20 | Q1 FY21 | Q2 FY21 | Q3 FY21 | Q4 FY21 |
|-------------------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|
| Net Sales | 2,054 | 2,227 | 1,701 | 1,751 | 1,170 | 2,923 | 2,724 | 3,049 |
| Raw Materials | 1,576 | 1,713 | 1,309 | 1,327 | 880 | 2,292 | 2,131 | 2,354 |
| Employee Costs | 103 | 109 | 107 | 99 | 95 | 113 | 110 | 111 |
| Other Expenditure | 101 | 105 | 88 | 91 | 67 | 118 | 117 | 122 |
| EBITDA | 274 | 300 | 197 | 234 | 129 | 400 | 366 | 462 |
| Depreciation | 48 | 53 | 51 | 49 | 42 | 56 | 52 | 47 |
| Interest | - | 0 | - | - | - | - | - | - |
| Other Income | 36 | 34 | 28 | 30 | 21 | 21 | 22 | 22 |
| PBT | 262 | 281 | 173 | 214 | 107 | 364 | 336 | 437 |
| Tax | 93 | 27 | 44 | 56 | 29 | 93 | 86 | 111 |
| Tax rate (%) | 35.5 | 9.6 | 25.6 | 26.1 | 26.8 | 25.6 | 25.6 | 25.5 |
| Reported PAT | 169 | 254 | 129 | 158 | 78 | 271 | 250 | 326 |
| YoY Growth (%) | | | | | | | | |
| Revenue | (12.4) | (9.8) | (14.4) | (8.5) | (43.0) | 31.2 | 60.2 | 74.1 |
| EBITDA | (25.3) | (25.2) | (28.4) | (14.7) | (52.9) | 33.3 | 85.9 | 97.5 |
| Adj. PAT | (26.6) | 0.1 | (25.7) | (4.9) | (53.7) | 6.8 | 94.1 | 105.6 |
| QoQ Growth (%) | | | | | | | | |
| Revenue | 7.3 | 8.4 | (23.6) | 3.0 | (33.2) | 149.8 | (6.8) | 11.9 |
| EBITDA | (0.2) | 9.6 | (34.4) | 18.7 | (44.9) | 210.6 | (8.5) | 26.2 |
| Adj. PAT | 1.6 | 50.1 | (49.2) | 22.9 | (50.5) | 245.9 | (7.7) | 30.1 |
| Margin (%) | | | | | | | | |
| EBITDA | 13.3 | 13.5 | 11.6 | 13.4 | 11.0 | 13.7 | 13.4 | 15.1 |
| PAT | 8.2 | 11.4 | 7.6 | 9.0 | 6.7 | 9.3 | 9.2 | 10.7 |
| Key Drivers | | | | | | | | |
| Engine Sales (in Units) | 23,033 | 26,271 | 19,797 | 20,827 | 13,756 | 34,489 | 31,193 | 33,831 |

Source: Company, EISEC Research

Fig 4: Key Assumptions

| (No of units) | FY18 | FY19 | FY20 | FY21 | FY22e | FY23e |
|---------------------------------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|
| Capacity (in units) | 1,05,000 | 1,20,000 | 1,35,000 | 1,35,000 | 1,50,000 | 1,50,000 |
| Engine Sales (in units) | 92,022 | 99,638 | 89,928 | 1,13,269 | 1,17,993 | 1,22,735 |
| Capacity Utilization (%) | 87.6 | 83.0 | 66.6 | 83.9 | 78.7 | 81.8 |
| Engine Realization (Rs) | 81,221 | 84,804 | 83,449 | 85,285 | 86,991 | 88,730 |
| Engine Revenues (Rs mn) | 7,474 | 8,450 | 7,504 | 9,660 | 10,264 | 10,890 |
| Component Revenues (Rs mn) | 34 | 31 | 14 | 9 | 9 | 10 |
| Total (Rs mn) | 7,509 | 8,481 | 7,519 | 9,669 | 10,274 | 10,901 |
| Other operating Income* (Rs mn) | 203 | 237 | 214 | 197 | 227 | 261 |
| Total Operating income (Rs mn) | 7,712 | 8,717 | 7,733 | 9,866 | 10,500 | 11,161 |

Source: Company, EISEC Research Estimates

Note: * includes scrap sales

Financial Statements

| Income Statement | FY19 | FY20 | FY21 | FY22e | FY23e |
|-----------------------------|--------------|--------------|--------------|---------------|---------------|
| YE March (Rs mn) | | | | | |
| Net Sales | 8,717 | 7,733 | 9,866 | 10,500 | 11,161 |
| Raw Materials | 6,566 | 5,925 | 7,657 | 8,127 | 8,628 |
| % of sales | 75.3 | 76.6 | 77.6 | 77.4 | 77.3 |
| Personnel | 393 | 418 | 429 | 455 | 486 |
| % of sales | 4.5 | 5.4 | 4.3 | 4.3 | 4.4 |
| Manufact. & Other Exp. | 442 | 386 | 423 | 453 | 478 |
| % of sales | 5.1 | 5.0 | 4.3 | 4.3 | 4.3 |
| EBITDA | 1,316 | 1,004 | 1,357 | 1,466 | 1,569 |
| EBITDA Margin (%) | 15.1 | 13.0 | 13.8 | 14.0 | 14.1 |
| Depreciation & Amortisation | 195 | 201 | 198 | 218 | 232 |
| EBIT | 1,121 | 803 | 1,159 | 1,247 | 1,337 |
| Interest Expenses | 1 | 0 | - | - | - |
| EBT | 1,120 | 803 | 1,159 | 1,247 | 1,337 |
| Other Income | 154 | 128 | 86 | 106 | 127 |
| PBT | 1,274 | 931 | 1,245 | 1,353 | 1,464 |
| Tax-Total | 450 | 220 | 319 | 341 | 368 |
| Effective tax rate (%) | 35.3 | 23.7 | 25.7 | 25.2 | 25.2 |
| Extraord. items - Adj. | - | - | - | - | - |
| Reported PAT | 824 | 710 | 925 | 1,012 | 1,096 |

Source: Company, EISEC Research Estimates

| Key Ratios | FY19 | FY20 | FY21 | FY22e | FY23e |
|-----------------------------------|--------|--------|-------|-------|-------|
| YE March | | | | | |
| Growth ratios (%) | | | | | |
| Net sales | 13.0 | (11.3) | 27.6 | 6.4 | 6.3 |
| EBITDA | 8.3 | (23.7) | 35.1 | 8.1 | 7.0 |
| Reported PAT | 2.9 | (13.8) | 30.3 | 9.4 | 8.2 |
| Margin Ratio (%) | | | | | |
| EBITDA Margin | 15.1 | 13.0 | 13.8 | 14.0 | 14.1 |
| EBIT Margin | 12.9 | 10.4 | 11.7 | 11.9 | 12.0 |
| PBT Margin | 14.6 | 12.0 | 12.6 | 12.9 | 13.1 |
| PAT Margin | 9.5 | 9.2 | 9.4 | 9.6 | 9.8 |
| Return Ratio (%) | | | | | |
| ROE | 35.3 | 30.0 | 35.8 | 35.0 | 34.6 |
| ROCE | 34.4 | 29.3 | 35.5 | 34.9 | 34.6 |
| ROIC | 107.6 | 86.7 | 99.0 | 81.9 | 95.4 |
| Turnover Ratio days (days) | | | | | |
| Gross Block Turnover (x) | 3.9 | 3.1 | 3.9 | 3.8 | 3.8 |
| Inventory Period | 20 | 17 | 23 | 17 | 17 |
| Debtors Period | 8 | 2 | 42 | 30 | 30 |
| Creditors | 44 | 47 | 61 | 46 | 46 |
| Cash Conversion Cycle | (15.9) | (27.4) | 4.2 | 1.0 | 1.0 |
| Solvency Ratio (%) | | | | | |
| Debt-equity (x) | - | - | - | - | - |
| Net Debt-equity (x) | (0.4) | (0.3) | (0.5) | (0.5) | (0.6) |
| Liquidity ratio (x) | 2.0 | 2.1 | 2.0 | 2.3 | 2.6 |
| Interest coverage ratio (%) | 1,233 | 5,655 | NA | NA | NA |
| Per share (Rs) | | | | | |
| Adjusted EPS | 68.0 | 58.6 | 76.2 | 83.4 | 90.2 |
| CEPS | 84.1 | 75.2 | 92.5 | 101.4 | 109.4 |
| Book value | 196.2 | 194.4 | 231.1 | 245.5 | 275.7 |
| Dividend per share | 50.0 | 50.0 | 40.0 | 69.0 | 60.0 |
| Dividend Payout (%) | 73.6 | 85.4 | 52.4 | 82.7 | 66.5 |
| Dividend Yield (%) | 3.7 | 3.7 | 2.9 | 5.1 | 4.4 |
| Valuation | | | | | |
| P/E | 24.4 | 20.7 | 17.8 | 16.3 | 15.1 |
| P/BV | 8.5 | 6.2 | 5.9 | 5.5 | 4.9 |
| EV/EBITDA | 14.1 | 12.8 | 10.9 | 10.0 | 9.0 |
| EV/Sales | 2.1 | 1.7 | 1.5 | 1.4 | 1.3 |

Source: Company, EISEC Research Estimate

| Balance Sheet | FY19 | FY20 | FY21 | FY22e | FY23e |
|----------------------------------|--------------|--------------|--------------|--------------|--------------|
| YE March (Rs mn) | | | | | |
| Sources of funds | | | | | |
| Capital | 121 | 121 | 121 | 121 | 121 |
| Reserves & Surplus | 2,259 | 2,238 | 2,684 | 2,859 | 3,226 |
| Shareholders' Funds | 2,380 | 2,359 | 2,806 | 2,980 | 3,348 |
| Minority Interest | - | - | - | - | - |
| Total Debt | - | - | - | - | - |
| Deferred Tax Liabilities | 72 | 46 | 6 | 6 | 6 |
| Total Liabilities | 2,451 | 2,405 | 2,812 | 2,986 | 3,353 |
| Application of funds | | | | | |
| Gross Block | 2,400 | 2,518 | 2,599 | 2,862 | 2,942 |
| Accumulated Dep. | (1,300) | (1,483) | (1,681) | (1,899) | (2,131) |
| Capital WIP | 20 | 40 | 13 | 0 | 0 |
| Non-current Asset | 78 | 47 | 59 | 63 | 67 |
| Net Fixed Assets | 1,198 | 1,122 | 990 | 1,025 | 877 |
| Investments | 838 | 1,111 | 342 | 382 | 422 |
| Goodwill | - | - | - | - | - |
| Inventories | 474 | 370 | 617 | 489 | 520 |
| Sundry Debtors | 187 | 41 | 1,134 | 863 | 917 |
| Other Current Assets | 186 | 192 | 192 | 205 | 218 |
| Cash & Bank Balances | 779 | 714 | 1,309 | 1,485 | 1,954 |
| Total Current Assets | 2,465 | 2,428 | 3,594 | 3,423 | 4,031 |
| Creditors | 1,042 | 992 | 1,639 | 1,323 | 1,407 |
| Other Current Liabilities | 88 | 63 | 48 | 48 | 51 |
| Provisions | 81 | 91 | 86 | 91 | 97 |
| Total Current Liabilities | 1,211 | 1,145 | 1,772 | 1,463 | 1,555 |
| Net Current Assets | 1,254 | 1,283 | 1,821 | 1,961 | 2,476 |
| Total assets | 2,451 | 2,405 | 2,812 | 2,986 | 3,353 |

Source: Company, EISEC Research Estimates

| Cash Flow | FY19 | FY20 | FY21 | FY22e | FY23e |
|--|--------------|--------------|--------------|--------------|--------------|
| YE March (Rs mn) | | | | | |
| Operating profit before WC changes | | | | | |
| | 873 | 762 | 1,005 | 1,125 | 1,200 |
| Net change in working capital | (186) | 234 | (725) | 73 | (10) |
| Cash flow from operating activities (a) | 688 | 996 | 280 | 1,198 | 1,191 |
| Adjusted Operating Cash flow | 687 | 996 | 280 | 1,198 | 1,191 |
| Capital expenditure | (340) | (158) | (56) | (250) | (80) |
| Adjusted FCF | 347 | 838 | 224 | 948 | 1,111 |
| Cash flow from investing activities (b) | 38 | (269) | 563 | (184) | 7 |
| Cash flow from financing activities (c) | (729) | (731) | (487) | (825) | (716) |
| Net change in cash (a+b+c) | (3) | (5) | 355 | 188 | 482 |
| Opening cash balance | 30 | 27 | 22 | 378 | 566 |
| Ending cash balance | 27 | 22 | 378 | 566 | 1,049 |
| Other bank balances | 751 | 691 | 931 | 919 | 906 |
| Cash on balance sheet | 779 | 714 | 1,309 | 1,485 | 1,954 |

Source: Company, EISEC Research Estimates

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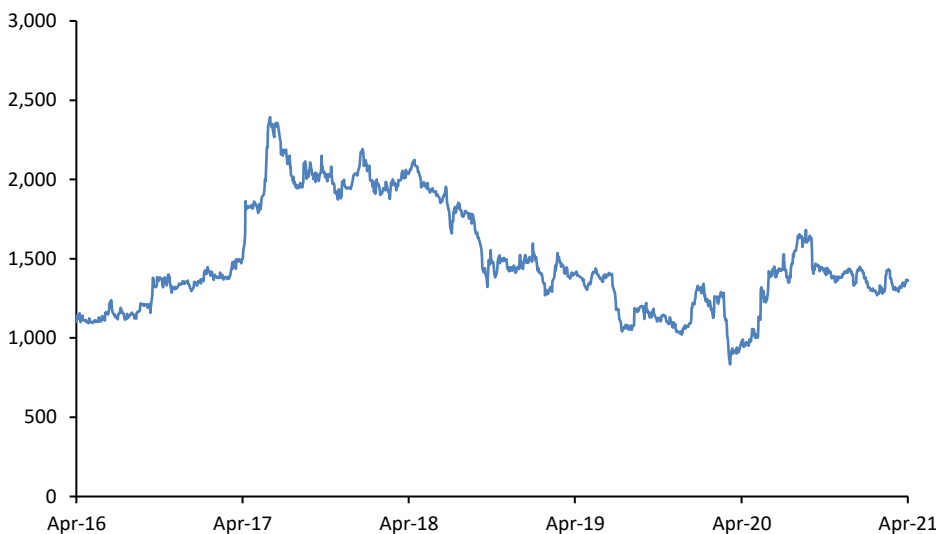
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Swaraj Engines Ltd.



Source: ACEEquity, EISEC Research

Analyst holding in stock: **NO**

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