Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Stock Update

Result Update

Schaeffler India Ltd

Strong quarter; Maintain Hold on expensive valuation

Automobiles	Sharekhan code: SCHAEFFLER		
Reco/View: Hold ↔	CMP: Rs. 3,187	Price Target: Rs. 3,328 ↑	

↑ Upgrade ↔ Maintain ↓ Downgrade

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		↔	

ESG Disclosure Score NEW

ESG RISK RATING 22.37

Updated July 08, 2022

Medium Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

Company details

Market cap:	Rs. 49,814 cr
52-week high/low:	Rs. 3,969/ 1,434
NSE volume: (No of shares)	1.50 lakh
BSE code:	505790
NSE code:	SCHAEFFLER
Free float: (No of shares)	4 cr

Shareholding (%) as on Sep 30, 2022

Promoters	74.1
FII	4.9
DII	15.5
Others	5.4

Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	-10.2	30.2	57.1	103.1
Relative to Sensex	-10.6	20.2	56.8	105.8

Sharekhan Research, Bloomberg

Summary

- Given limited upside and expensive valuation, we maintain our Hold rating on Schaeffler India Limited (SIL) with a revised PT of Rs. 3,328. The stock is trading at a premium to its historical average at P/E of 43.3x and EV/EBITDA of 27.9x its CY2023E.
- During Q3CY2022, the company's revenue was slightly below expectations, which was recovered by higher-than-expected EBITDA margin. The company continues to grow on a q-o-q basis.
- Exports is a high-growth area for SIL, given the company's strong relationship with the parent with leading global OEMs and tier-I suppliers.
- Greater localisation and focus on market share gains would aid revenue and EBITDA growth going forward. We expect its earnings to report a 35.2% CAGR during CY2021-CY2023E

Schaeffler India Limited's (SIL) Q3CY2022 results continue to be strong. Revenue was slightly below expectations, which was recovered by higher-than-expected EBITDA margin. The company continues to maintain its sales and profitability growth. Revenue, EBITDA, and PAT grew by 18.1% y-o-y, 20.6% y-o-y, and 26.1% y-o-y, respectively, in Q3CY2022. SIL's sales mix remains robust with automotive, industrial, and exports contributing 49.4%, 34.5%, and 16.1%, respectively, during the quarter. EBITDA margin contracted 20bps q-o-q to 18.2% in Q3CY2022, led by commodity inflation, partially offset by improved product mix and focus on cost reduction. The company's management has given a positive outlook for its business, led by volume growth across its verticals. SIL would continue to benefit from the industrial and automobile aftermarket segments, strong growth traction in export markets, and better prospects for the bearings business. However, management highlighted global events are causing disruptions in supply chain and are affecting its wind energy business vertical. In terms of valuation, the stock is trading at a premium to its historical average at a P/E of 43.3x and EV/EBITDA of 27.9x its CY2023E. Given limited upside and expensive valuations, we maintain our Hold rating with a revised price target (PT) of Rs. 3,328.

Key positives

- SIL continues to report record sales in Q3CY2022, outpacing the automobile industry's growth in a tough environment. EBITDA margin stood at 18.2% in Q3, higher by 40bps than expectations.
- SIL has won significant business orders in both automotive and industrial businesses and has consolidated its leadership position.

Key negatives

- EBIT margin of the mobility components division contracted by 30bps q-o-q to 4.3% in Q3CY2022.

Management Commentary

- The company's management has given a positive outlook for its business, led by volume growth across its verticals. However, management highlighted global events are causing disruptions in supply chain and are affecting its wind energy business vertical.
- The company is delivering on its capex strategy, which was 4.8% of sales in Q3CY2022.

Our Call

Valuation – Maintain Hold with a revised PT of Rs. 3,328: SIL has been consistently outperforming the industry's growth rate, driven by its technological edge and established relationships with leading OEMs/ clients in India and globally. After a dip in performance led by COVID-induced lockdown in Q2CY2020, the company's performance has improved steadily, aided by strong recovery in the automotive and industrial segments. Exports continue to do well and contributed ~16% to revenue in Q3CY2022. We expect a robust performance by the company going forward, driven by normalisation of economic activity, improvement in content per vehicle, strong growth in the wind power and railways businesses, and launch of new products in the aftermarket segment. We expect its earnings to report a 35.2% CAGR during CY2021-CY2023E, driven by a 29.4% revenue CAGR and a 110-bps improvement in EBITDA margin from 17.5% in CY2021 to 18.6% in CY2023E. In terms of valuation, the stock is trading at a premium to its historical average at a P/E of 43.3x and EV/EBITDA of 27.9x its CY2023E estimates. Given limited upside and expensive valuation, we maintain our Hold rating with a revised PT of Rs. 3,328.

Key Risks

Weakening global outlook and uncertainties can disrupt supply chain and increase costs, which may affect our future estimates.

Valuation (Standalone) Rs cr

Particulars	CY20	CY21	CY22E	CY23E	CY24E
Net Sales	3,762	5,561	7,507	9,308	10,705
Growth (%)	(13.7)	47.8	35.0	24.0	15.0
EBIDTA	536	972	1,366	1,731	2,012
OPM (%)	14.3	17.5	18.2	18.6	18.8
Recurring PAT	291	629	895	1,150	1,351
Growth (%)	(20.9)	116.2	42.3	28.4	17.5
EPS (Rs)	18.6	40.3	57.3	73.5	86.4
PE (x)	171.2	79.2	55.6	43.3	36.9
P/BV (x)	16.8	15.9	19.0	14.1	10.7
EV/EBIDTA (x)	90.6	50.9	35.9	27.9	24.8
RoE (%)	9.3	23.9	25.4	24.6	22.4
RoCE (%)	12.4	30.9	32.9	32.0	29.3

Source: Company; Sharekhan estimates

Key results highlights

- **Strong performance continues:** SIL's Q3CY2022 results continue to be strong. Revenue was slightly below expectations, which was recovered by higher-than-expected EBITDA margin. The company continues to maintain its sales and profitability growth. Revenue, EBITDA, and PAT grew by 18.1% y-o-y, 20.6% y-o-y, and 26.1% y-o-y, respectively, in Q3CY2022. SIL's sales mix remains robust with automotive, industrial, and exports contributing 49.4%, 34.5%, and 16.1%, respectively, during the quarter. SIL's revenue was up 18.1% y-o-y (0.4% q-o-q) to Rs. 1,756 crore, driven by 28.4% y-o-y (5.5% q-o-q) growth in automotive technologies, 3.8% y-o-y (0.9% q-o-q) growth in automotive aftermarket, 26.8% y-o-y (6.3% q-o-q) growth in industrial business, and 60.8% y-o-y (11.8% q-o-q) growth in exports and others. EBITDA margin contracted by 20 bps q-o-q to 18.2% in Q3CY2022, led by commodity inflation, partially offset by improved product mix and focus on cost reductions. EBITDA and PAT were up 20.6% y-o-y and 26.1% y-o-y to Rs. 319 crore and Rs. 215 crore in Q3CY2022, respectively.
- **Increasing market coverage:** SIL continues to focus on increasing its market coverage through new launches, expansion of new product range, and an improvement in service levels. The company's performance has improved, aided by better mix and sustained countermeasures. SIL continues to win new contracts in both automotive and industrial businesses. Key wins during the quarter include double clutch systems for the CV segment and needle bearing for the PV segment. The company has increased its product coverage by newly launched products – centre joint support. Mobility business and focus on technology are the company's key focus areas.
- **Capex plan remains intact:** The capex strategy remains intact at 4.8% of sales in Q3CY2022. The company generated strong cash flow of Rs. 72.4 crore during Q3CY2022.
- **Positive management guidance:** The company's management has given a positive outlook for its business, led by volume growth across its verticals. However, management highlighted global events are causing disruptions in supply chain and are affecting its wind energy business vertical. The company is delivering on its capex strategy, which was 4.8% of sales in Q3CY2022. The company has a robust order book outlook, led by strong customer engagement. The company has won significant business orders in both automotive and industrial businesses and has consolidated its leadership position during Q3CY2022. Management expects sustained operational performance across its plants and normal capacity utilisation. However, it highlighted headwinds due to geopolitical situations and increasing inflation.
- **Strong growth prospects:** SIL would benefit from industrial and automobile aftermarket segments, strong growth traction in export markets, and better prospects for the bearings business. The company is focusing on introducing new products in the industrial and automotive aftermarkets by bringing in localisation and boosting its market share. SIL will be the key beneficiary of this trend, as it focuses on increasing content per vehicle. In the industrial OEM segment, the company is witnessing strong growth in the railways segment with the introduction of new products and supplies to Metro Rail projects.

Results (Standalone) Rs cr

Particulars	Q3CY22	Q3CY21	%YoY	Q2CY22	%QoQ
Net revenue	**1,756**	**1,488**	**18.1**	**1,749**	**0.4**
Operating expenses	**1,437**	**1,223**	**17.5**	**1,427**	**0.7**
EBIDTA	**319**	**264**	**20.6**	**322**	**(0.9)**
Depreciation	52	50	4.2	51	0.9
Interest	1	1	(14.1)	1	(8.6)
Other Income	23	16	47.0	16	43.0
PBT	290	230	26.1	286	1.3
Tax	74	59	26.2	75	(1.0)
Reported PAT	215	171	26.1	226	(4.6)
Adjusted PAT	**215**	**171**	**26.1**	**211**	**2.2**
EPS	**13.8**	**10.9**	**26.1**	**13.5**	**2.2**

Source: Company, Sharekhan Research

Key Ratios (Standalone)

Particulars	Q3CY22	Q3CY21	YoY (bps)	Q2CY22	QoQ (bps)
Gross margin (%)	37.0	37.5	(50)	37.1	(20)
EBIDTA margin (%)	18.2	17.8	40	18.4	(20)
EBIT margin (%)	15.2	14.4	80	15.5	(20)
Net profit margin (%)	12.3	11.5	80	12.1	20
Effective tax rate (%)	25.6	25.6	-	26.2	(60)

Source: Company, Sharekhan Research

Segment-wise performance (Standalone) Rs cr

Segment Revenue	Q3CY22	Q3CY21	%YoY	Q2CY22	%QoQ
(a) Mobility components and related solutions	**1,410.9**	**1,099.0**	**28.4**	**1,330.0**	**6.1**
- Automotive Technologies	717.1	560.0	28.0	679.5	5.5
- Automotive Aftermarket	150.6	145.1	3.8	149.3	0.9
- Industrial	335.3	264.5	26.8	315.3	6.3
- Exports & Others	208.0	129.4	60.8	186.0	11.8
(b) Others	**345.5**	**388.6**	**(11.1)**	**418.8**	**(17.5)**
- Industrial	270.5	342.3	(21.0)	325.3	(16.8)
- Exports & Others	75.0	46.4	61.7	93.5	(19.8)
Net revenue	**1,756.4**	**1,487.6**	**18.1**	**1,748.8**	**0.4**
EBIT (Rs cr)	**Q3CY22**	**Q3CY21**	**%YoY**	**Q2CY22**	**%QoQ**
(a) Mobility components and related solutions	202.0	147.0	37.4	194.3	4.0
(b) Others	65.3	67.9	(3.8)	76.2	(14.3)
Total	**267.3**	**214.9**	**24.4**	**270.5**	**(1.2)**
EBIT Margin (%)	**Q3CY22**	**Q3CY21**	**YoY (bps)**	**Q2CY22**	**QoQ (bps)**
(a) Mobility components and related solutions	14.3	13.4	94	14.6	(29)
(b) Others	18.9	17.5	144	18.2	71
Total	**15.2**	**14.4**	**77**	**15.5**	**(25)**

Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector View – Demand picking up in the automotive and industrial sector

The passenger segment, both for two-wheelers and four-wheelers, is expected to remain strong amid COVID-19, as a preference for personal transport. Rural demand is expected to recover, given positive rural sentiments. We expect sequential improvement in M&HCV sales to continue, driven by rise in e-commerce, agriculture, infrastructure, and mining activities. We expect multi-year upcycle in the CV segment, driven by improved economic activities, low-interest rate regime, and better financing availability. We expect M&HCVs to outpace other automobile segments in the medium term, followed by growth in the tractor, PV, and 2W segments. Moreover, exports provide a 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. Auto component exports are expected to grow from $15 billion to $80 billion by FY2027.

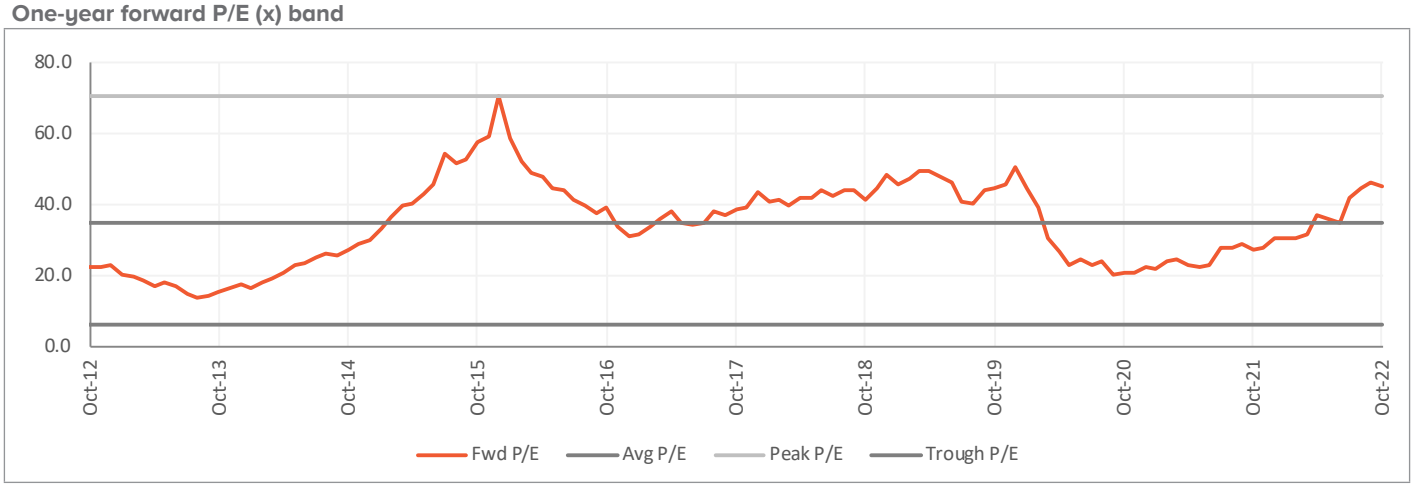
■ Company Outlook – MNC company with a strong technological parentage and robust balance sheet

SIL is part of the German Schaeffler Group. The Schaeffler Group has a strong research and development (R&D) DNA. In CY2019, the group filed 2,400 patents, making it the second most innovative company in Germany. The company has established strong relationships with global OEMs worldwide. SIL would benefit from its strong parentage and is expected to receive new businesses going forward. Moreover, SIL's parent has identified it as a manufacturing base for supply to Asia-Pacific region. This provides a huge growth potential for the company. SIL is a debt-free company with strong return ratio profile. The company is expected to generate strong FCF of Rs. 1,200 crore over the next three years. We remain positive on the company's growth prospects.

■ Valuation – Maintain Hold rating with a revised PT of Rs. 3,328

SIL has been consistently outperforming the industry's growth rate, driven by its technological edge and established relationships with leading OEMs/clients in India and globally. After a dip in performance led by COVID-induced lockdown in Q2CY2020, the company's performance has improved steadily, aided by strong recovery in the automotive and industrial segments. Exports continue to do well and contributed ~16% to revenue in Q3CY2022. We expect robust performance by the company going forward, driven by normalisation of economic activity, improvement in content per vehicle, strong growth in wind power and railways businesses, and launch of new products in the aftermarket segment. We expect its earnings to report a 35.2% CAGR during CY2021-CY2023E, driven by a 29.4% revenue CAGR and a 110-bps improvement in EBITDA margin from 17.5% in CY2021 to 18.6% in CY2023E. In terms of valuation, the stock is trading at a premium to its historical average at a P/E of 43.3x and EV/EBITDA of 27.9x its CY2023E estimates. Given limited upside and expensive valuation, we maintain our Hold rating with a revised PT of Rs. 3,328.

One-year forward P/E (x) band



Source: Sharekhan Research

Peer Comparison

Companies	CMP (Rs/Share)	P/E (x)			EV/EBITDA (x)			ROCE (%)		
		FY22*	FY23E*	FY24E*	FY22*	FY23E*	FY24E*	FY22*	FY23E*	FY24E*
Schaeffler India	3,187	79.2	55.6	43.3	50.9	35.9	27.9	30.9	32.9	32.0
Sundram Fasteners	903	41.1	26.9	21.6	23.9	17.5	13.8	21.4	22.0	24.0
Suprajit Engineering	328	26.2	23.0	17.0	18.1	15.3	11.5	16.2	17.6	20.9
Bosch	15,672	37.9	28.8	23.8	28.3	20.4	15.9	13.9	17.1	18.3

*Source: Company; Sharekhan Research; *Note: For Schaeffler the years are CY21, CY22E and CY23E*

About company

SIL (erstwhile FAG Bearings), with four plants and 11 sales offices, has a significant presence in India with three major widely known product brands – FAG, INA, and LuK. SIL produces a wide range of ball bearings, cylindrical roller bearings, deep groove balls, spherical roller bearings, and wheel bearings sold under the brand name of FAG. The company manufactures engine and transmission components for front accessory drive systems, chain drive systems, valve train, shift systems, and a range of needle roller bearings and elements under the brand, INA. SIL also produces clutch systems and dual mass flywheels for passenger cars, LCVs, heavy commercial vehicles, and tractors, which are sold under the brand of LuK. In addition to this, SIL has dedicated engineering and R&D support based in India to augment its product teams. SIL also has one of the largest aftermarket networks serving industrial and automotive markets. SIL derives 47% of its revenue from the automotive segment, 42% from the industrial segment, and 11% revenue from exports.

Investment theme

SIL is among the largest automotive and industrial suppliers with a strong parentage of the Schaeffler Group. The company is present in India since the past 50 years and has established strong relationships with leading OEMs in India and globally. Having strong manufacturing capabilities and R&D, SIL's parent company has identified it as a manufacturing base for supply to Asia-Pacific region. This provides a strong opportunity to the company to expand its export business. With the Indian Government focussing on 'Make in India,' 'Atma-Nirbhar,' and PLI programmes, SIL is well positioned to benefit from these programmes. Moreover, the company has a diversified portfolio – with automotive, industrial, and export businesses contributing 48%, 42%, and 10%, respectively, to revenue. The company's strategies to increase content per vehicle through product innovation and launches, while identifying new business divisions in the industrial sector, are likely to keep growth traction intact. The company's strong technological parentage and established relationships with global OEM clients would continue to provide growth opportunities. We remain positive on SIL and expect strong earnings growth, driven by revenue growth and margin expansion.

Key Risks

- Delayed approval from industrial customers and late launches by automotive players can impact growth.
- Pricing pressures from automotive OEM clients can impact profitability.
- Weakening global outlook and uncertainties can disrupt supply chain and increase costs, which may affect our future estimates.

Additional Data

Key management personnel

Avinash Gandhi	Chairman
Harsha Kadam	Managing Director & CEO
Satish Patel	Director Finance & CFO
Ashish Tiwari	Company Secretary

Source: Company Website

Top shareholders

Sr. No.	Holder Name	Holding (%)
1	Fag Kugelfischer Gmbh	27.3
2	Schaeffler Buhl Verwaltungs Gmbh	20.6
3	Schaeffler Verwaltungsholding Sechs Gmbh	15.0
4	Industriewerk Schaeffler Ina-ingenieurdienst Gmbh	11.3
5	Kotak Emerging Equity Scheme	4.2
6	Uti Flexi Cap Fund	2.3
7	Sbi Magnum Global Fund	2.2
8	Sundaram Mutual Fund	1.4
9	Hdfc Life Insurance Co Ltd	1.2

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

Sharekhan

by BNP PARIBAS

Know more about our products and services

For Private Circulation only

Compliance Officer: Ms. Binkle Oza; Tel: 022-61150000; email id: compliance@sharekhan.com;

For any queries or grievances kindly email igc@sharekhan.com or contact: myaccount@sharekhan.com

Registered Office: Sharekhan Limited, The Ruby, 18th Floor, 29 Senapati Bapat Marg, Dadar (West), Mumbai – 400 028, Maharashtra, INDIA, Tel: 022 - 67502000/ Fax: 022 - 24327343. Sharekhan Ltd.: SEBI Regn. Nos.: BSE / NSE / MSEI (CASH / F&O / CD) / MCX - Commodity: INZ000171337; DP: NSDL/CDSL-IN-DP-365-2018; PMS: INP000005786; Mutual Fund: ARN 20669; Research Analyst: INH000006183.