



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 Updated July 08, 2022 **22.37**

Medium Risk

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

Source: Morningstar

Company details

Market cap:	Rs. 42,733 cr
52-week high/low:	Rs. 3,969/ 1,600
NSE volume: (No of shares)	1.80 lakh
BSE code:	505790
NSE code:	SCHAEFFLER
Free float: (No of shares)	4 cr

Shareholding (%)

Promoters	74.1
FII	5.7
DII	14.2
Others	5.9

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-1.7	-14.2	21.4	58.5
Relative to Sensex	0.9	-20.9	6.1	52.4

Sharekhan Research, Bloomberg

Schaeffler India Ltd

Poised to race ahead

Automobiles

Sharekhan code: SCHAEFFLER

Reco/View: Buy



Upgrade

CMP: Rs. 2,734

Price Target: Rs. 3,328



Maintain

Downgrade

Summary

- We upgrade our rating on Schaeffler India Limited (SIL) to Buy with a 12-month price target of Rs. 3,328, led by strong outlook for its automotive and industrial businesses, and comfortable valuations, post correction in stock price.
- SIL is expected to perform strongly in Q4CY22E, with record sales and growth in profitability growth, led by order wins and margin improvement.
- SIL's robust parental ecosystem provides access to advance technology and export visibility.
- 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.

We upgrade our rating on Schaeffler India Limited (SIL) to Buy with an unchanged 12-month price target (PT) of Rs. 3,328, led by strong outlook for its automotive and industrial businesses, and comfortable valuations, post 18% correction in stock prices. We remain positive on the company's growth prospects, driven by a strong outlook for its automotive and industrial businesses and improving content per vehicle. The company has a strong R&D and technology bandwidth, which makes it well placed to garner benefit from the electrification and hybridization trend in the domestic automobile sector. The company has strong support from its parent company and has access to latest advanced technologies and relationships with global OEMs & Tier I suppliers. In addition, the company's presence in would benefit from the industrial and automobile aftermarket segments, strong growth traction in export markets, and better prospects for the bearings business. 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.

- Well-positioned to benefit from electrification and hybridization trend:** The company is likely to be a key beneficiary of electrification and hybridization trend for the domestic business, as India is expected to witness faster growth in the electric and hybrid vehicles going forward. The company expects electrification to be at high single digit by 2030, while hybridization to be 25-35%. The company has a strong product portfolio and is well-placed to benefit from this trend.
- Multiple growth levers:** In the automotive OEM segment, SIL is witnessing increased content per vehicle in the petrol passenger vehicle (PV) segment post the implementation of BS-VI emission norms; while in the industrial OEM segment, the company is expected to see strong growth from the railways and construction segments. We expect SIL to continue its better-than-industry performance, given its strong pedigree of parent, which gives access to latest technologies and relationships with global OEMs & Tier I suppliers.
- Strong earnings growth:** Given the robust outlook for SIL's business, we expect its earnings to post 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.

Our Call

Valuation – Upgrade to Buy with unchanged PT of Rs. 3,328: SIL has been consistently outperforming industry 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 a COVID induced lockdown in CY20, the company's performance has continued to improve steadily, aided by strong performance 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 industrial 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. The stock price has corrected 18% from the peak in the last four months and thus, the valuation metrics are comfortable at P/E of 31.6x and EV/EBITDA of 21.2x its CY2024E estimates. The premium valuations are justified, given the pedigree of its parent company and its capability to outperform industry and peers. We upgrade SIL to Buy rating with a 12-month of PT of Rs. 3,328.

Key Risks

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

Valuation

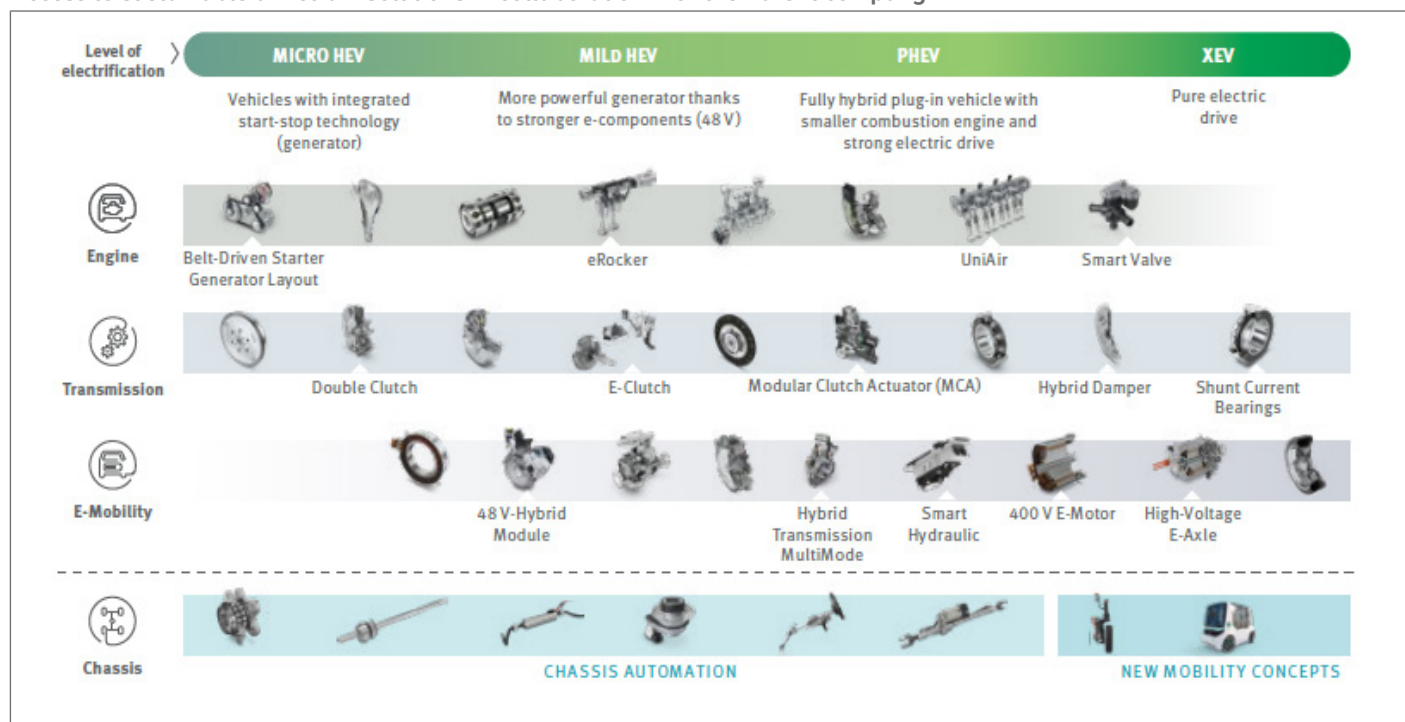
Particulars	CY20	CY21	CY22E	CY23E	CY24E
Net Sales	3,762	5,561	7,507	9,308	10,705
Growth (%)	(13.7)	47.8	35.0	24.0	15.0
EBIDTA	536	972	1,366	1,731	2,012
OPM (%)	14.3	17.5	18.2	18.6	18.8
Recurring PAT	291	629	895	1,150	1,351
Growth (%)	(20.9)	116.2	42.3	28.4	17.5
EPS (Rs)	18.6	40.3	57.3	73.5	86.4
PE (x)	146.9	67.9	47.7	37.2	31.6
P/BV (x)	14.4	13.6	16.3	12.1	9.1
EV/EBIDTA (x)	77.4	43.6	30.7	23.9	21.2
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

Well-positioned to benefit from electrification and hybridization trend

The company is likely to be a key beneficiary of electrification and hybridization trend for the domestic business, as India is expected to witness faster growth in the electric and hybrid vehicles going forward. The company expects electrification to be at high single digit by 2030, while hybridisation is expected to be at 25-35%. The company has a strong product portfolio and is well-placed to benefit from this trend. The internal combustion engine (ICE) technology is expected to remain a significant driver for the industry going forward. The company will continue to benefit from its existing product portfolio. Since all hybrids will also have an ICE, there will be continuous improvement in the technology of internal combustion engines, which will drive content per car for the company, given its technological edge over peers and established relationships with OEMs. In addition, the company has exposure to all the key markets, viz. North America, Europe, China and Indian markets, which provides revenue diversification. The company is well-positioned to benefit from the electrification trend in the mass markets of these geographies. In addition, the management expects to the two-wheeler and three-wheeler markets to witness faster electrification compared to other segments.

Access to sustainable drivetrain solutions in collaboration with the Parent company



Source: Company Annual report; Sharekhan Research

Q4CY22 results expected to remain strong

SIL would maintain strong growth momentum going forward. We expect a PAT of Rs. 215 crore in Q4CY22E, a growth of 17.7% y-o-y, led by 18.1% growth in revenues and 16.4% growth in EBITDA. The capex strategy remains intact at 9.2% of sales in 9MCY2022.

The management is positive on delivering growth

The 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 Q3CY22. The company has a robust order book outlook, led by strong customer engagement, robust business growth prospects of its key clients, improving content per vehicle and new product launches. The company continues to win significant business orders in both automotive and industrial businesses through market share gains during 9MCY2022. The management expects sustained operational performance across its plants and normal capacity utilisation.

Key business wins across segments in Q3CY22



Source: Company Investor Presentation; Sharekhan Research

Increased market coverage

SIL continues to focus on increasing its market coverage through new launches, expansion of product range, and better 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. The company continues to focus on service-level improvement and range extension in Schaeffler TruPower.

Multiple growth levers

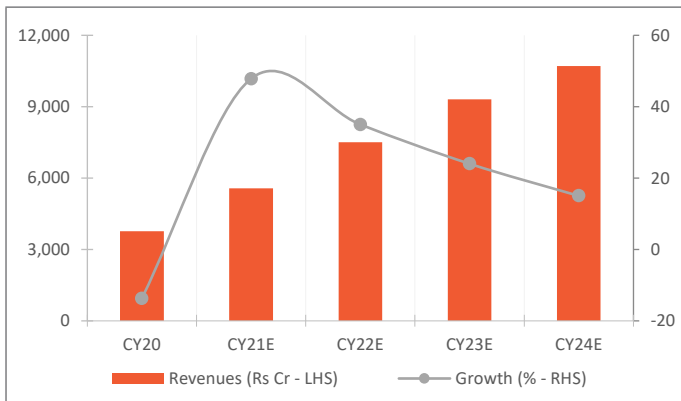
In the automotive OEM segment, SIL is witnessing increased content per vehicle in the petrol passenger vehicle (PV) segment post the implementation of BS-VI emission norms; while in the industrial OEM segment, the company is witnessing strong growth from the railways segment and wind power division. The railway division's business is driven by new products and supplies to Metro Rail, while the wind power business is aided by new client acquisitions. Besides the OEM segment, aftermarket is also poised for healthy growth, driven by new product introductions. The company aims to introduce more products in the segment. 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 in the long run. The company has a strong access to e-mobility technology through its parent, which has a strong presence in Europe. The company is developing technology for two-wheelers, working jointly with the parent company.

Strong growth prospects

SIL would benefit from industrial and automobile aftermarket segments, strong growth traction in export markets, and better prospects for 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. With new additions of customers in the wind power business, we expect SIL to report strong growth in this space. Exports is a high-growth area for SIL, given the pedigree of its parent company. We expect SIL to benefit from industrial and automobile aftermarkets, strong growth traction in railways and export segments, and better prospects for the bearings business amid stricter norms. Given the robust outlook for SIL's business, we expect its earnings to post 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.

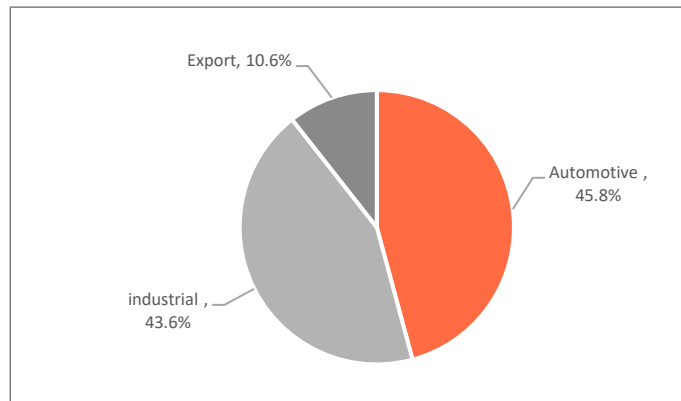
Financials in charts

Revenue and Growth Trend



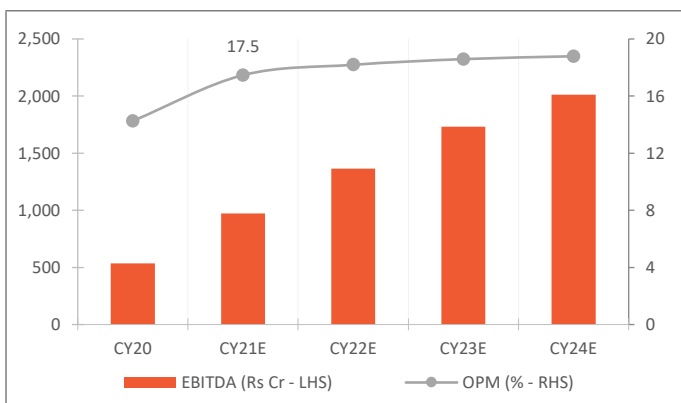
Source: Company, Sharekhan Research

Revenue Mix (%)



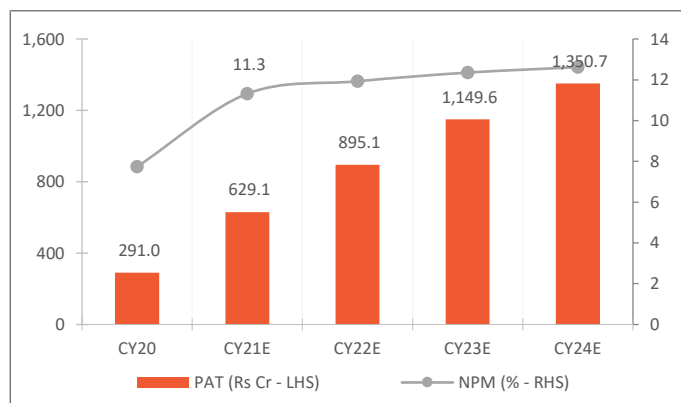
Source: Company, Sharekhan Research

EBITDA and OPM Trend



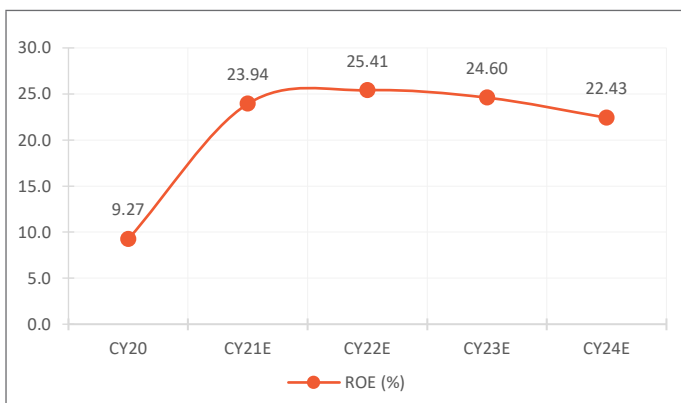
Source: Company, Sharekhan Research

Net Profit and NPM Trend



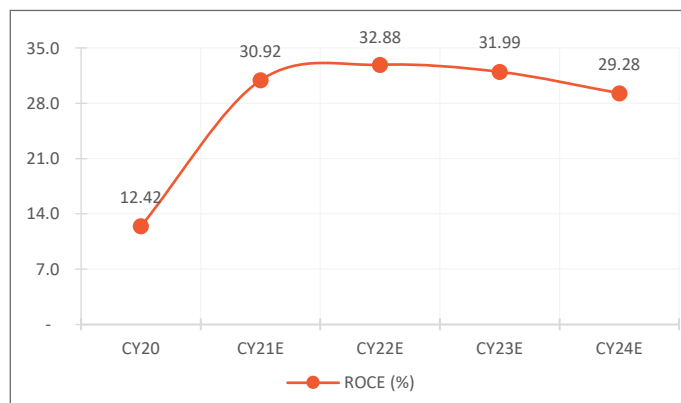
Source: Company, Sharekhan Research

RoE Trend



Source: Company, Sharekhan Research

RoCE Trend



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, as preference for personal transport rises. Rural demand is expected to improve, on positive sentiments. We expect sequential improvement in M&HCV sales to continue, driven by rise in e-commerce, agriculture, infrastructure, and mining activities. We expect a 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.

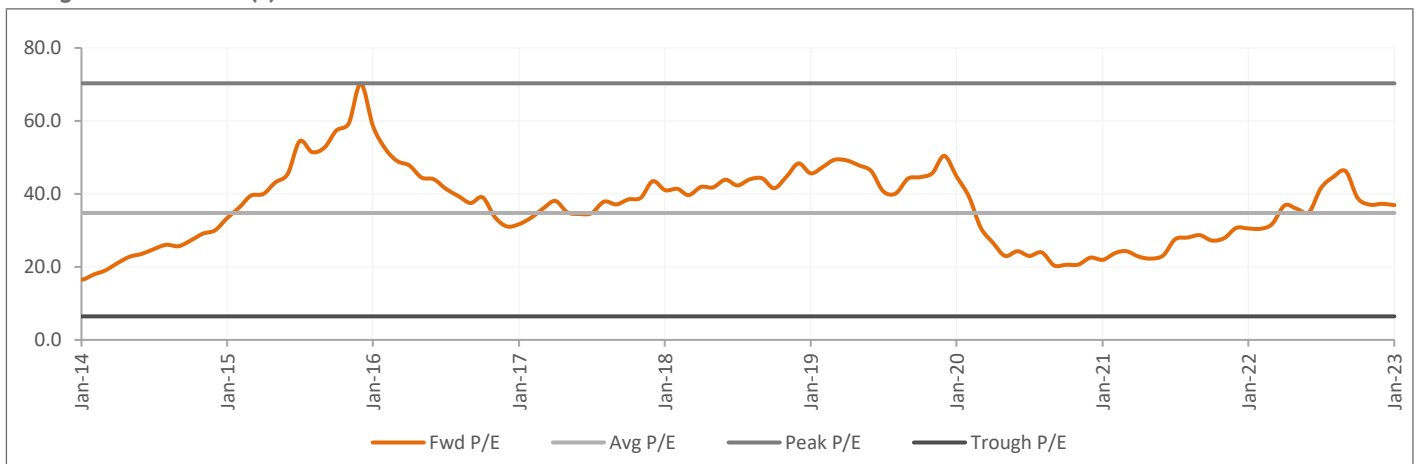
■ Company Outlook – MNC with strong technological parentage and robust balance sheet

SIL is part of Germany's Schaeffler Group. The Schaeffler Group has a strong research and development (R&D) DNA. In CY2021, the group filed 1,784 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 – Upgrade to Buy with unchanged PT of Rs. 3,328

SIL has been consistently outperforming industry 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 a COVID induced lockdown in CY20, the company's performance has continued to improve steadily, aided by strong performance 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 industrial 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. The stock price has corrected 18% from the peak in the last four months and thus, the valuation metrics are comfortable at P/E of 31.6x and EV/EBITDA of 21.2x its CY2024E estimates. The premium valuations are justified, given the pedigree of its parent company and its capability to outperform industry and peers. We upgrade SIL to Buy rating with a 12-month of PT of Rs. 3,328.Rs.

One-year forward P/E (x) band



Source: Company, 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	2,734	67.9	47.7	37.2	43.6	30.7	23.9	30.9	32.9	32.0
Sundram Fasteners	965	43.9	29.6	23.4	25.5	19.2	15.0	21.4	21.4	23.5
Suprajit Engineering	334	26.7	23.5	17.3	18.4	15.6	11.7	16.2	17.6	20.9
Bosch	16,859	40.8	29.1	23.8	30.7	22.1	17.6	13.9	18.1	19.3

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

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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 deteriorating 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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