

May 27, 2023

Q4FY23 Result Update

☒ Change in Estimates | ☒ Target | ☒ Reco

Change in Estimates

	Current		Previous	
	FY24E	FY25E	FY24E	FY25E
Rating	ACCUMULATE		BUY	
Target Price	475		440	
Sales (Rs. m)	15,296	17,504	14,698	16,948
% Chng.	4.1	3.3		
EBITDA (Rs. m)	2,311	2,834	2,204	2,643
% Chng.	4.9	7.2		
EPS (Rs.)	17.1	21.6	16.1	20.0
% Chng.	6.1	8.0		

Key Financials - Consolidated

Y/e Mar	FY22	FY23	FY24E	FY25E
Sales (Rs. m)	13,215	13,640	15,296	17,504
EBITDA (Rs. m)	1,690	1,893	2,311	2,834
Margin (%)	12.8	13.9	15.1	16.2
PAT (Rs. m)	919	1,233	1,555	1,966
EPS (Rs.)	11.9	13.5	17.1	21.6
Gr. (%)	31.0	13.8	26.1	26.4
DPS (Rs.)	-	1.0	2.6	4.3
Yield (%)	-	0.2	0.6	1.0
RoE (%)	19.4	15.5	13.7	15.3
RoCE (%)	21.7	17.2	16.5	18.4
EV/Sales (x)	2.8	2.8	2.5	2.1
EV/EBITDA (x)	21.9	20.4	16.4	13.1
PE (x)	36.7	32.2	25.5	20.2
P/BV (x)	6.5	3.7	3.3	2.9

Key Data

HRSH.BO | HARSHA IN

52-W High / Low	Rs.528 / Rs.309
Sensex / Nifty	62,502 / 18,499
Market Cap	Rs.40bn/ \$ 481m
Shares Outstanding	91m
3M Avg. Daily Value	Rs.99.34m

Shareholding Pattern (%)

Promoter's	74.61
Foreign	3.84
Domestic Institution	9.04
Public & Others	12.51
Promoter Pledge (Rs bn)	-

Stock Performance (%)

	1M	6M	12M
Absolute	1.7	6.5	-
Relative	(1.8)	6.2	-

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Harsha Engineers International (HARSHA IN)

Rating: ACCUMULATE | CMP: Rs436 | TP: Rs475

Revival in margins; outlook remains intact

Quick Pointers:

- Better product mix, lower commodity costs & reduced losses in Romania drive margin expansion.
- Healthy order book for Bronze Bushes; revival expected in H2FY4.

We revise our FY24/25E EPS estimates by +6.1%/+8.0% to factor in Romania & China's improving profitability over the medium to long term, but downgrade the rating to 'Accumulate' from Buy with a TP of Rs475 (Rs439 earlier) valuing it at 22x on FY25E EPS (same as earlier) given the recent run-up in the stock price. Harsha Engineers International (HARSHA) reported a 6.8% YoY decline in revenue, while EBITDA margin expanded by 172bps YoY due to falling material costs. The presently weak bronze bushes market should recover in H2FY24, while we expect margins in China and Romania to significantly improve this year. The company has multiple levers for future growth, including i) bearing cage outsourcing, ii) significant capex by global bearing players in India, iii) opportunity in large-size cages, iv) wallet share gains in Japan, and v) long-term demand for wind bronze bushes.

We remain positive on HARSHA given 1) market leadership in bearing cages, 2) strong wallet share with leading bearing players, 3) multiple levers for long-term growth, and 4) expected improvement in operations in Romania. We estimate FY23-25E Revenue/EBITDA/PAT CAGR of 13.3%/22.4%/26.3%. The stock is currently trading at a PE of 25.5x/20.2x FY24/25E. Downgrade to 'Accumulate'.

Revenue declines but margins improve: Consolidated revenue fell 6.8% YoY to Rs3.4bn (PL estimate of Rs3.1bn) due to pass-through of falling commodity prices and a weak demand environment in Europe. Gross margin expanded by 284bps YoY to 46.6%, owing to a better product mix and lower material costs. EBITDA grew 5.5% YoY to Rs508mn (PL estimate of Rs448mn), with EBITDA margin increasing by 172bps to 14.8%, on account of lower other expenses (down 397bps YoY as a % of sales), despite employee costs rising 63.5% YoY (up 509bps YoY as a % of sales). PAT rose 8.7% YoY to Rs326mn, (PL estimate of Rs275mn) aided by healthy profitability in India and considerable reduction in losses in Romania.

Engineering margins increase while Solar EPC segment lags: Consolidated Engineering revenue dipped 2.5% YoY to Rs3.2bn, India Engineering revenue fell 4.8% YoY to Rs2.3bn, and Solar EPC revenue slid 46.9% YoY to Rs189mn. In terms of EBITDA margins (including other income), Consolidated Engineering came in at 17.4% (+106bps YoY), India Engineering at 24.6% (+161bps YoY), and Solar EPC at 0.8% (-78bps YoY).

Exhibit 1: Falling commodity prices lead to a decline in revenue but an improvement in margins

Y/e March (Rs mn)	Q4FY22	Q1FY23	Q2FY23	Q3FY23	Q4FY23	YoY gr. (%)	QoQ gr. (%)	FY23	FY22	YoY gr. (%)
Revenue	3,689	3,977	3,220	3,007	3,437	(6.8)	14.3	13,640	13,215	3.2
Total Revenues	3,689	3,977	3,220	3,007	3,437	(6.8)	14.3	13,640	13,215	3.2
Expenditure	3,207	3,482	2,740	2,597	2,929	(8.7)	12.8	11,747	11,525	1.9
<i>as % of sales</i>	<i>86.9</i>	<i>87.5</i>	<i>85.1</i>	<i>86.4</i>	<i>85.2</i>			<i>86.1</i>	<i>87.2</i>	
Consumption of RM	2,076	2,334	1,667	1,521	1,837	(11.5)	20.8	7,359	7,397	(0.5)
<i>as % of sales</i>	<i>56.3</i>	<i>58.7</i>	<i>51.8</i>	<i>50.6</i>	<i>53.4</i>			<i>53.9</i>	<i>56.0</i>	
Employee Cost	249	420	409	387	407	63.5	5.1	1,562	1,452	7.6
<i>as % of sales</i>	<i>6.7</i>	<i>10.6</i>	<i>12.7</i>	<i>12.9</i>	<i>11.8</i>	<i>509</i>		<i>11.5</i>	<i>11.0</i>	
Other expenditure	882	727	665	689	685	(22.3)	(0.5)	2,827	2,676	5.6
<i>as % of sales</i>	<i>23.9</i>	<i>18.3</i>	<i>20.6</i>	<i>22.9</i>	<i>19.9</i>	<i>(397)</i>		<i>20.7</i>	<i>20.3</i>	
EBITDA	482	495	480	410	508	5.5	23.8	1,893	1,690	12.0
Depreciation	90	88	90	92	92	2.1	(0.5)	361	354	2.2
EBIT	392	407	390	318	417	6.3	30.9	1,532	1,337	14.6
Other Income	68	62	43	135	58	(13.9)	(56.9)	298	175	70.1
Interest	55	54	56	23	26	(53.6)	11.3	158	246	(35.5)
PBT	404	415	377	430	449	11.1	4.4	1,671	1,266	32.0
Total Tax	104	107	96	113	123	17.9	9.0	438	347	26.4
Adjusted PAT	300	309	281	317	326	8.7	2.8	1,233	919	34.1
(Profit)/loss from MI	-	-	-	-	-	-	-	-	-	-
PAT after MI	300	309	281	317	326	8.7	2.8	1,233	919	34.1
Extra ordinary items	-	-	-	-	-	-	-	-	-	-
Reported PAT	300	309	281	317	326	8.7	2.8	1,233	919	34.1
Adjusted EPS	3.3	3.4	3.1	3.5	3.6	8.7	2.8	13.5	10.1	34.1
Margins (%)	Q4FY22	Q1FY23	Q2FY23	Q3FY23	Q4FY23	bps	bps	FY23	FY22	bps
EBITDA	13.1	12.5	14.9	13.6	14.8	172	114	13.9	12.8	(109)
EBIT	10.6	10.2	12.1	10.6	12.1	149	154	11.2	10.1	(111)
EBT	11.0	10.4	11.7	14.3	13.1	210	(124)	12.3	9.6	(267)
PAT	8.1	7.8	8.7	10.6	9.5	135	(106)	9.0	7.0	(208)
Effective Tax rate	25.8	25.7	25.5	26.2	27.4	159	115	26.2	27.4	115

Source: Company, PL

Conference Call Highlights

- HARSHA witnessed **~8% consolidated volume growth in FY23**, but falling commodity prices led to a moderation in revenue growth for the year.
- **Steep inflation and a sharp increase in energy prices** had a significant impact on revenue from Europe.
- Sales in India grew **~20% in FY23**, and **can continue to grow in double digits**, driven by significant capex by bearing players in India, and growing shift from insourcing to outsourcing of cage production.
- **Demand for bronze bushes softened since Q3FY23** due to a weak wind market, but based on customer indications, management is **confident of a revival in H2FY24 and is conservatively targeting ~Rs450mn in sales in FY24** (vs ~Rs300mn in FY23, which was Rs100mn short of their expectations).
- **Romania updates:**
 - High energy costs, very muted demand and sub-optimal utilization (~50% for castings and 40-50% for cages) significantly impacted the business.
 - Management is confident of EBTDA margin revival to 5-6% in FY24 and 7-8% in FY25, driven by higher volumes and an increasing share of finished cage sales from ~20% of the mix to 30-40% at optimal volumes.
 - Semi-finished castings (~80% of Romania mix) have a 6-7% margin while cages can command a 14-15% margin.
- **Strict lockdown conditions and slowdown in the automotive market** impacted business in China. Also, the company had to incur a **significant one-time cost** in China due to issues with slag recovery equipment. However, **EBITDA margins in China can increase to 12-13%** from 6-7% currently owing to improving market conditions.
- HARSHA saw **strong growth in sales to Japanese customers** (up ~34% YoY to ~Rs600mn), and **this momentum can continue for a few years** as the company looks to increase its wallet share from 2-3% to 10-12%.
- Precision Stamped Component sales **grew ~19% in FY23 to ~Rs536mn**.
- The company **developed ~330 new products in FY23** covering outsourcing projects, large-size cages, Japan customer products, and bushes, which indicates a strong pipeline going forward.
- Commissioned 3.71MW hybrid captive power project, which **should generate ~Rs40mn of after-tax benefits** from FY24 onwards.
- HARSHA will **invest ~Rs3.5bn in tranches over the next 3-4 years** in its new wholly owned subsidiary, **Harsha Engineers Advantek**, to setup a new greenfield project. This will enhance capacities to **cater to additional demand** in the next ~3 years. More clarity will be provided in a few quarters.
- **Planned capex of over Rs1bn per year** for the next 3 years includes investments in the subsidiary as well as existing facilities.

Financials

Income Statement (Rs m)

Y/e Mar	FY22	FY23	FY24E	FY25E
Net Revenues	13,215	13,640	15,296	17,504
YoY gr. (%)	51.2	3.2	12.1	14.4
Cost of Goods Sold	7,397	7,359	8,141	9,209
Gross Profit	5,818	6,282	7,156	8,295
Margin (%)	44.0	46.1	46.8	47.4
Employee Cost	1,452	1,562	1,705	1,879
Other Expenses	779	805	918	1,050
EBITDA	1,690	1,893	2,311	2,834
YoY gr. (%)	38.7	12.0	22.1	22.6
Margin (%)	12.8	13.9	15.1	16.2
Depreciation and Amortization	354	361	381	412
EBIT	1,337	1,532	1,930	2,421
Margin (%)	10.1	11.2	12.6	13.8
Net Interest	246	158	118	117
Other Income	175	298	289	353
Profit Before Tax	1,266	1,671	2,102	2,657
Margin (%)	9.6	12.3	13.7	15.2
Total Tax	347	438	546	691
Effective tax rate (%)	27.4	26.2	26.0	26.0
Profit after tax	919	1,233	1,555	1,966
Minority interest	-	-	-	-
Share Profit from Associate	-	-	-	-
Adjusted PAT	919	1,233	1,555	1,966
YoY gr. (%)	102.3	34.1	26.1	26.4
Margin (%)	6.9	8.8	10.0	11.0
Extra Ord. Income / (Exp)	-	-	-	-
Reported PAT	919	1,233	1,555	1,966
YoY gr. (%)	102.3	34.1	26.1	26.4
Margin (%)	7.0	9.0	10.2	11.2
Other Comprehensive Income	14	-	-	-
Total Comprehensive Income	934	1,233	1,555	1,966
Equity Shares O/s (m)	77	91	91	91
EPS (Rs)	11.9	13.5	17.1	21.6

Source: Company Data, PL Research

Balance Sheet Abstract (Rs m)

Y/e Mar	FY22	FY23	FY24E	FY25E
Non-Current Assets				
Gross Block	7,231	7,895	9,036	10,139
Tangibles	7,123	7,787	8,928	10,031
Intangibles	108	108	108	108
Acc: Dep / Amortization	4,385	4,746	5,127	5,539
Tangibles	4,294	4,651	5,028	5,436
Intangibles	91	95	99	104
Net fixed assets	2,846	3,149	3,909	4,600
Tangibles	2,829	3,136	3,900	4,595
Intangibles	18	13	9	5
Capital Work In Progress	21	116	122	53
Goodwill	711	718	718	718
Non-Current Investments	7	365	355	346
Net Deferred tax assets	(40)	(66)	(66)	(66)
Other Non-Current Assets	197	127	138	156
Current Assets				
Investments	64	1,610	1,850	2,200
Inventories	3,757	3,769	3,981	4,316
Trade receivables	2,828	2,804	3,059	3,357
Cash & Bank Balance	393	1,336	1,667	2,049
Other Current Assets	527	345	535	613
Total Assets	11,583	14,451	16,466	18,555
Equity				
Equity Share Capital	772	910	910	910
Other Equity	4,446	9,807	11,129	12,702
Total Networth	5,219	10,718	12,040	13,613
Non-Current Liabilities				
Long Term borrowings	1,378	79	64	49
Provisions	111	84	102	103
Other non current liabilities	22	27	31	35
Current Liabilities				
ST Debt / Current of LT Debt	2,406	1,690	1,690	1,690
Trade payables	1,828	1,187	1,760	2,158
Other current liabilities	524	558	670	798
Total Equity & Liabilities	11,583	14,451	16,466	18,555

Source: Company Data, PL Research



Cash Flow (Rs m)

Y/e Mar	FY22	FY23	FY24E	FY25E
PBT	1,266	1,671	2,102	2,657
Add. Depreciation	354	361	381	412
Add. Interest	246	158	118	117
Less Financial Other Income	175	298	289	353
Add. Other	24	(152)	(170)	(220)
Op. profit before WC changes	1,890	2,039	2,430	2,966
Net Changes-WC	(1,214)	(338)	(24)	(203)
Direct tax	(311)	(375)	(546)	(691)
Net cash from Op. activities	365	1,327	1,860	2,073
Capital expenditures	(495)	(764)	(1,147)	(1,033)
Interest / Dividend Income	16	74	170	220
Others	(39)	(2,389)	(377)	(608)
Net Cash from Invt. activities	(518)	(3,079)	(1,354)	(1,421)
Issue of share cap. / premium	-	4,343	-	-
Debt changes	282	(2,027)	(15)	(15)
Dividend paid	-	-	(233)	(393)
Interest paid	(246)	(158)	(118)	(117)
Others	1	5	4	4
Net cash from Fin. activities	37	2,163	(362)	(521)
Net change in cash	(116)	410	143	131
Free Cash Flow	(131)	563	713	1,040

Source: Company Data, PL Research

Key Financial Metrics

Y/e Mar	FY22	FY23	FY24E	FY25E
Per Share(Rs)				
EPS	11.9	13.5	17.1	21.6
CEPS	16.5	17.5	21.3	26.1
BVPS	67.6	117.7	132.2	149.5
FCF	(1.7)	6.2	7.8	11.4
DPS	-	1.0	2.6	4.3
Return Ratio(%)				
RoCE	21.7	17.2	16.5	18.4
ROIC	17.0	18.9	17.5	20.2
RoE	19.4	15.5	13.7	15.3
Balance Sheet				
Net Debt : Equity (x)	0.6	(0.1)	(0.1)	(0.2)
Net Working Capital (Days)	131	144	126	115
Valuation(x)				
PER	36.7	32.2	25.5	20.2
P/B	6.5	3.7	3.3	2.9
P/CEPS	26.5	24.9	20.5	16.7
EV/EBITDA	21.9	20.4	16.4	13.1
EV/Sales	2.8	2.8	2.5	2.1
Dividend Yield (%)	-	0.2	0.6	1.0

Source: Company Data, PL Research

Quarterly Financials (Rs m)

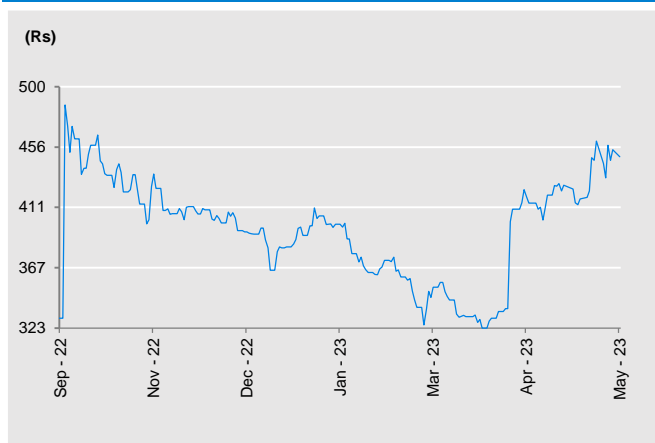
Y/e Mar	Q1FY23	Q2FY23	Q3FY23	Q4FY23
Net Revenue	3,977	3,220	3,007	3,437
YoY gr. (%)	29.9	(0.4)	(18.5)	(13.6)
Raw Material Expenses	2,334	1,667	1,521	1,837
Gross Profit	1,643	1,553	1,486	1,600
Margin (%)	41.3	48.2	49.4	46.6
EBITDA	495	480	410	508
YoY gr. (%)	19.6	22.8	(14.8)	2.6
Margin (%)	12.5	14.9	13.6	14.8
Depreciation / Depletion	88	90	92	92
EBIT	407	390	318	417
Margin (%)	10.2	12.1	10.6	12.1
Net Interest	54	56	23	26
Other Income	62	43	135	58
Profit before Tax	415	377	430	449
Margin (%)	10.4	11.7	14.3	13.1
Total Tax	107	96	113	123
Effective tax rate (%)	25.7	25.5	26.2	27.4
Profit after Tax	309	281	317	326
Minority interest	-	-	-	-
Share Profit from Associates	-	-	-	-
Adjusted PAT	309	281	317	326
YoY gr. (%)	19.6	56.6	5.8	5.7
Margin (%)	7.8	8.7	10.6	9.5
Extra Ord. Income / (Exp)	-	-	-	-
Reported PAT	309	281	317	326
YoY gr. (%)	19.6	56.6	5.8	5.7
Margin (%)	7.8	8.7	10.6	9.5
Other Comprehensive Income	-	-	-	-
Total Comprehensive Income	309	281	317	326
Avg. Shares O/s (m)	77	79	91	91
EPS (Rs)	4.0	3.6	3.5	3.6

Source: Company Data, PL Research



Price Chart

Recommendation History



No.	Date	Rating	TP (Rs.)	Share Price (Rs.)
1	11-Apr-23	BUY	440	414
2	28-Feb-23	BUY	439	325

Analyst Coverage Universe

Sr. No.	Company Name	Rating	TP (Rs)	Share Price (Rs)
1	ABB India	Accumulate	4,119	3,719
2	Apar Industries	BUY	3,832	3,056
3	Bharat Electronics	BUY	125	109
4	BHEL	Sell	36	71
5	Cummins India	Accumulate	1,750	1,649
6	Engineers India	BUY	85	74
7	GE T&D India	Hold	184	188
8	Harsha Engineers International	BUY	440	414
9	Kalpataru Power Transmission	BUY	625	527
10	KEC International	Accumulate	559	514
11	Larsen & Toubro	BUY	2,615	2,364
12	Praj Industries	BUY	495	343
13	Siemens	Accumulate	4,018	3,723
14	Thermax	BUY	2,613	2,280
15	Triveni Turbine	Accumulate	416	398
16	Voltamp Transformers	Hold	3,056	2,905

PL's Recommendation Nomenclature (Absolute Performance)

Buy	: > 15%
Accumulate	: 5% to 15%
Hold	: +5% to -5%
Reduce	: -5% to -15%
Sell	: < -15%
Not Rated (NR)	: No specific call on the stock
Under Review (UR)	: Rating likely to change shortly



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