Sharekhan
by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Stock Update

Result Update

Amber Enterprises

Improving margins to drive growth

Capital Goods	Sharekhan code: AMBER
Reco/View: Buy ↔	CMP: **Rs. 2,411** — Price Target: **Rs. 2,800** ↑

↑ 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 30.25

Updated Jul 08, 2023

High Risk

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

Source: Morningstar

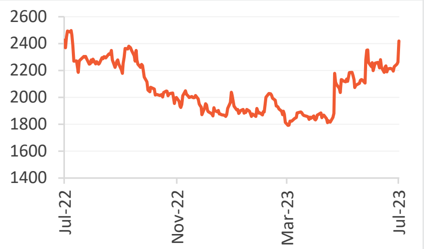
Company details

Market cap:	Rs. 8,124 cr
52-week high/low:	Rs. 2,580/1,762
NSE volume: (No of shares)	1.6 lakh
BSE code:	540902
NSE code:	AMBER
Free float: (No of shares)	2.0 cr

Shareholding (%)

Promoters	40.3
FII	24.2
DII	12.7
Others	22.8

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	7.1	32.1	19.9	-0.3
Relative to Sensex	1.9	21.5	9.1	-19.9

Sharekhan Research, Bloomberg

Summary

- Though revenues dropped sharply in Q1FY24 on poor volumes (of RAC and components division), margins surged.
- Structural changes in the manufacturing landscape of RACs have transformed Amber's business model and the company is pursuing a components-based model, which would drive margin expansion and growth.
- Company expects a 19-21% ROCE in the next 2-3 years as utilisation levels improve. Company has guided for 30% EBITDA CAGR for the next two years.
- We maintain a Buy with a revised PT of Rs. 2,800 (based on FY2025E EPS), as we expect profitability to improve backed by better product profile in RAC division, traction in motors, electronics and mobility division as well as growth in exports.

Q1FY24 revenues declined 7% on y-o-y basis to Rs. 1,702 crore. Muted sales were a result of a weak demand, owing to unseasonal rains and weather patterns. Channel inventory is high and expected to normalise by the end of Q2FY24. Operating profit grew by 33% y-o-y to Rs. 132 crore, while OPM came in at 7.8% (up 232 bps y-o-y) vs our estimate of flat margins. Margins improved on account of component strategy which led to favourable product mix change. Its PAT grew at a slower pace by 8.5% y-o-y to Rs. 46 crore vs Rs. 42 crore in Q1FY23 due to decline in other income and a rise in depreciation and interest cost on y-o-y basis. For H1CY23, RAC industry has declined by ~20-25% and the company expect the industry to grow by 7-8% y-o-y for FY24.

Key positives

- Mobility and electronics divisions reported healthy revenue growth.
- Margins improved significantly on y-o-y basis on account of component strategy, which led to favourable product mix.

Key negatives

- Weak demand for RACs and components due to unseasonal rains dragged down revenues.
- In H1CY23, RAC Industry has declined by ~20%-25%
- EBITDA margins of mobility division declined to 20.2% vs 27.4% in Q1FY23.

Management Commentary

- For FY24, the company plans to incur capex of Rs. 350-380 crore.
- Demand in Q4FY24 would recover and the channel inventory is likely to be depleted in Q2FY24. The company expects RAC industry to grow at 7-8% and clock volumes of ~9 million units in FY24.
- Margin range for finished goods to components vary from 6% - 9%. The proportion of RAC is reducing and now it is less than 50% of the total sales.
- Motors division is expected to grow ~ 25% y-o-y in FY24. The division witnessed 40% y-o-y growth in exports. EBITDA would be at 9-12%.
- Electronics division is expected to grow 35% - 40% in FY24. The margins are in the range of ~5% for this division and the company is moving towards ~6% range.
- Margin profile of various EMS players differ according to the segments/applications and could range from 4-14%.

Revision in estimates – We have marginally tweaked our estimates for FY2024-FY2025E to factor in margin improvement.

Our Call

Valuation – Retain Buy with a revised PT of Rs. 2,800: Despite structural change in the RAC industry, wherein brands are resorting to in-house manufacturing of finished goods, Amber is well placed to capture incremental demand accruing from components ecosystem development. While the share of RAC finished goods is decreasing, the company is concentrating on RAC and non-RAC components to drive growth and profitability. The management remains optimistic about growth in components (including mobility, electronics, and non-RAC components), new customer additions as well as exports in the next 3-4 years. Further, traction in high growth sectors like Railways could augur well. Moreover, in the long term, under penetration of RAC, rising temperatures in India, changing lifestyle patterns, and increasing contribution from Tier II, III, IV cities would drive the RAC industry's growth and benefit Amber indirectly, driving demand for its components. We build in revenue/PAT CAGR of ~14%/~33% (FY23-25E). We maintain a Buy with a revised price target (PT) of Rs. 2,800 based on FY25E EPS.

Key Risks

1) Increased revenue share of components vs. finished goods may impact margin. 2) Increased share of exports to total revenue exposes the company to currency risk. 3) Seasonal nature of the RAC industry.

Valuation (Consolidated) Rs cr

Particulars	FY22	FY23	FY24E	FY25E
Revenue	4,206	6,927	7,758	9,000
OPM (%)	6.5	6.0	6.5	6.9
PAT	109	157	198	277
Growth (%)	33.3	44.5	26.0	40.1
EPS (Rs.)	32.3	46.7	58.8	82.3
P/E (x)	74.7	51.7	41.0	29.3
EV/EBITDA (x)	31.2	21.3	17.7	14.6
RoCE (%)	7.9	10.3	10.7	12.7
RoE (%)	6.5	8.7	10.0	12.5

Source: Company; Sharekhan estimates

Margin expansion the highlight in Q1FY24

Q1FY2024 revenues declined 7% on y-o-y basis to Rs. 1,702 crore. Muted sales were a result of a weak demand, owing to unseasonal rains and weather patterns. Channel inventory is high and expected to come at normalized level of inventory by end of Q2FY24. Operating profit grew by 33% y-o-y to Rs 132 crore, while operating margin came in at 7.8% (up 232 bps y-o-y) vs our estimate of flat margin. Margins during the quarter improved on account of component strategy which led to favourable product mix change. Its PAT grew at a slower pace by 8.5% y-o-y to Rs. 46 crore vs Rs. 42 crore in Q1FY23 due to decline in other income and rise in depreciation and interest cost on y-o-y basis. For H1CY23, RAC industry has declined by ~20-25% and the company expect the industry to grow by 7-8% y-o-y for FY24.

Q1FY24 investor update and conference call highlights

Margin varies for RAC and non-RAC components: The margin range for finished goods to components vary from 6-9%. Proportion of RAC is reducing and now it is less than 50% of the total sales.

RAC industry declined by 20-25%: Q1FY24, which is usually a strong quarter for the RAC industry, was marred by unseasonal rains and weather patterns. Owing to the muted demand that industry witnessed, channel inventories were high and are expected to come down to a normalized level by the end of Q1FY24. In H1CY23, the industry revenue has declined by 20-25%.

RAC Industry to grow by 7-8% in FY24 and clock 9 million in volumes: After a subdued Q1FY24, inventory is getting liquidated in Q2FY24. As per the past trend, the company expects good Q4FY24 and aims to do better than the industry. It expects industry to clock 9 mn volumes in FY24.

Motors division: This division is expected to grow ~ 25% y-o-y in FY24. The division witnessed 40% y-o-y growth in exports. The EBITDA would be in the range of 9-12%.

Electronics division: Electronics division is expected to grow 35% - 40% in FY24. The margins are in the range of ~5% for this division and the company is moving towards the ~6% range. In electronics division - 30% revenue is from wearables/ hearables and telecom, while 70% comes from consumer durables and appliances which include ACs, refrigerator, washing machines, microwave, water purifiers and TVs. The company expects the ratio to tilt in favour of wearables/ hearables and telecom at 40% going forward. This would also help margin expansion. Currently, a large part of the demand of PCBAs for non-smartphone applications is fulfilled via imports. The government's focus on manufacturing electronics locally presents a multi-fold growth opportunity for this division.

Margin profile of EMS players varies: The margin profile of the EMS players depends on the segment and applications. There are 9-10 sectors, in which lowest margin is in consumer durables and home appliances, industrial and healthcare have higher margin; while auto margins are at 7-9%. Defence and railways components margin are in the range of 10-11%. As, the company brings in more applications in its portfolio, the margins are expected to improve gradually if it is able to secure sizeable clients.

Update on Sidwal: The company expects to double Sidwal's revenue, as well as bottom-line in 2-3 years. The sustainable EBITDA margin are at 20-22%.

Strong customer base in Railways: The company supplies to Indian railways as they have their own factories in Kapurthala, Chennai, Raebareli and other places by participating in tenders. In the metro segment, the company supplies to train manufacturers and metro car builders like Alstom, Bombardier and BEML which are making the car bodies.

Capacity utilisation at comfortable levels: In motors, the company would be close to ~50% capacity utilization. In RAC, capacity utilization will be 50-55% as the company has done two greenfield facility expansions. In Sidwal, in mobility application utilization levels are 65%-70%. In components division utilization levels range between 50-70%.

PLI scheme benefit would continue to accrue: The company is one of the largest PLI applicants and has applied for Rs.400 crore of incentives in PLI. As per the PLI structure, the company would be receiving remaining ~ Rs. 270 crore by 2027-28.

Balance sheet is strengthening gradually: The company aims 16.5% RoCE which would scale upto 19-21% in the next two years. Net debt is at ~Rs. 788 crore. The company incurred a capex of Rs. 40 crore in Q1FY24 and will do capex of Rs. 350-380 crore for the rest of FY24.

Results (consolidated) Rs cr

Particulars	Q1FY24	Q1FY23	YoY %	Q4Y23	QoQ %
Sales	**1,702**	**1,826**	**-6.8**	**3,003**	**-43.3**
Operating Profit	**132**	**99**	**32.9**	**204**	**-35.2**
Depreciation	43	32	34.6	39	11.4
Interest	45	21	114.8	37	20.8
Other Income	19	13	50.3	19	3.3
PBT	**63**	**58.9**	**6.5**	**145.9**	**-57.0**
Tax	16.1	16.0	0.7	37.8	-57.5
Reported PAT	46.6	42.9	8.7	108.1	-56.9
Adjusted PAT	**45.6**	**42.1**	**8.5**	**104.0**	**-56.1**
Adjusted EPS (Rs.)	**13.5**	**12.5**	**8.5**	**30.9**	**-56.1**
Margins (%)			**BPS**		**BPS**
OPM	7.8	5.4	232	6.8	97
NPM	2.7	2.3	39	3.6	-86
Tax Rate	25.7	27.1	-148	25.9	-26

Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector view - Demand outlook encouraging, healthy growth prospects

The air-conditioner industry is well poised for growth, given strong pent-up demand post two-year lull. Further, increasing disposable incomes, upgrade in lifestyles, and rising temperatures are the structural growth drivers. Moreover, owing to a shift in manufacturing base outside China and the government's incentives to enhance manufacturing through the Make in India initiative, there are enormous opportunities for well-integrated players such as Amber. An enhanced capacity and wider product offerings and customer penetration are likely to drive the company's performance in addition to a healthy demand outlook for the electronics outsourcing industry.

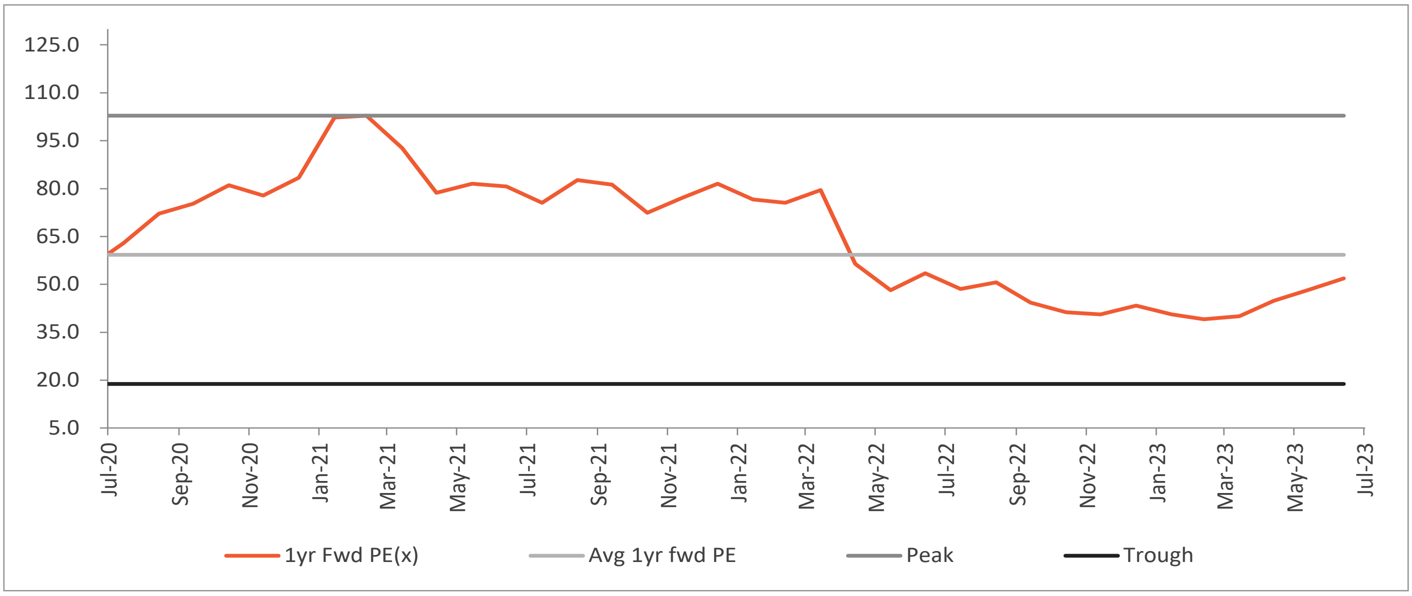
■ Company outlook - Long runway for growth

Amber is well-placed to capture incremental demand accruing from the indigenisation of both fully built-up units and components ecosystem development through reduced imports. It will also be a key beneficiary of PLI schemes for AC and components. The company is expanding capacity through two greenfield projects, one in Supa, Pune, and the other in Chennai. Management remains optimistic about export prospects for both fully built-up units and components that can potentially emerge over the next 3-4 years. Overall, the outlook remains optimistic with the management confident of capturing opportunities with better volume offtake despite short-term challenges, such as tepid volume growth in FY24 and margin pressure in some of the components.

■ Valuation - Retain Buy with a revised PT of Rs. 2,800

Despite structural change in the RAC industry, wherein brands are resorting to in-house manufacturing of finished goods, Amber is well placed to capture incremental demand accruing from components ecosystem development. While the share of RAC finished goods is decreasing, the company is concentrating on RAC and non-RAC components to drive growth and profitability. The management remains optimistic about growth in components (including mobility, electronics, and non-RAC components), new customer additions as well as exports in the next 3-4 years. Further, traction in high growth sectors like Railways could augur well. Moreover, in the long term, under penetration of RAC, rising temperatures in India, changing lifestyle patterns, and increasing contribution from Tier II, III, IV cities would drive the RAC industry's growth and benefit Amber indirectly, driving demand for its components. We build in revenue/PAT CAGR of ~14%/~33% (FY23-25E). We maintain a Buy with a revised price target (PT) of Rs. 2,800 based on FY25E EPS.

One-year forward P/E (x) band



Source: Sharekhan Research

About company

Incorporated in 1990, Amber has emerged as a market leader in the Indian room AC OEM/ODM industry. The company's comprehensive product portfolio includes room AC (indoor and outdoor units as well as window ACs) and reliable critical components, which have a long approval cycle. The company is one of the largest manufacturers and suppliers of critical components such as heat exchangers, PCBs, motors, sheet metal, case liner etc. of RAC and other consumer durables such as refrigerators and washing machines. Amber has emerged as a market leader in the Indian RAC OEM/ODM industry with more than 70% market share and 26.5% market share in the overall RAC market in FY2023. The company has 15 manufacturing facilities strategically located close to customers, enabling faster turnaround. It also has a high degree of backward integration coupled with strong R&D capabilities, resulting in high proportion of ODM. The company has been serving a majority of customers for over five years and has a marquee customer base as eight out of the top 10 RAC brands are its clients.

Investment theme

Amber has a market leadership position in the OEM/ODM segment for branded room ACs. Moreover, the opportunity size seems to be increasing as OEM players are now more focused on the innovation and marketing side of the business and relying on outsourcing for manufacturing their products. We believe enormous growth opportunities would come across going forward, owing to global players shifting their manufacturing base outside China and Government of India to enhance manufacturing through Make in India initiative by providing incentives. Further, Amber remains a strong beneficiary from recently announced PLI schemes for AC and components. A healthy demand outlook for the electronic outsourcing industry and enhanced capacity, increased product offerings, and customer penetration are likely to drive the company's performance.

Key Risks

- Lower demand offtake due to economic slowdown might impact revenue growth momentum and raw-material price volatility and forex rate fluctuation can impact profitability.
- Lack of diversified revenue base in terms of product categories and high revenue concentration with few customers pose a threat to revenue.

Additional Data

Key management personnel

Jasbir Singh	Executive Chairperson and CEO
Daljit Singh	Executive Managing Director
Sudhir Goyal	Chief Financial Officer
Konica Yadav	Company Secretary and Compliance Officer

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Ascent Investment Holdings	9.76
2	Kotak Mahindra Asset Management	5.02
3	Goldman Sachs Group	4.39
4	ICICI Prudential Life Insurance	3.23
5	Vanguard Group Incorporation	1.85
6	Goldman Sachs Fund	1.38
7	State of Kuwait	1.33
8	Wellington Management Group LLP	1.19
9	Newport Asia Institutional	1.18
10	Oxbow Master Fund	1.14

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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