

1 August 2023

India | Equity Research | Q1FY24 result review

ZF Commercial Vehicle Control Systems

Auto Ancillaries

Gross margin uptick helps EBITDAM beat seasonality effect

ZFCVCS (ZFI) has delivered a 10-quarter high gross margin, driven by improving mix and lagged price hikes, resulting in flat EBITDAM QoQ. ZFI's revenue from domestic OEMs was up ~20% YoY, driven by new business generation from electronic stability control system sales to buses, electronic braking system applications, electronic compressors and driver assistance systems. Going ahead, ZFI is planning to ramp-up EBITDAM, led by improving mix of new complex products at the cost of lower margin commoditised products, improving productivity and tighter control on pricing. We are building in ~24% revenue CAGR for FY23-25E with mean EBITDAM of ~15.5%. We downgrade ZFI to **HOLD** from **Add** post 40% return in the past 6 months with a revised DCF-based target price of INR 12,810 (earlier INR 11,433), implying 40x FY25E earnings.

Conference call takeaways and our views

- OEM/export/after market segment revenue came in at INR 4.4bn/INR 3.9bn/INR 1.4bn, up ~20%/~18%/~15% YoY, respectively, driving overall revenue by 21% YoY, as new product segment continued to add to revenue growth beyond the traditional larger segments. OEM segment growth was driven by rising penetration of ESC, EBS, electronic compressors and rising trailer adoption. Aftermarket growth was driven by rising demand in mining segment (up 60% YoY), strong off-take from Southern India state STUs and rising demand for vacuum boosters/actuators etc. Exports were boosted by rising demand for air compressor units from BMW/DAF, air disc brake levers etc. from customers in EU/US. Nearly 50%/45% of exports came in from EU/NA. Shifting trend of sourcing from India from EU customers like Volvo, BMW, Daimler to help exports continue to grow ahead other than new product addition, in order to defy domestic CV cyclicality. As against value addition of ~Euro 600/CV in India vs 4x business/unit in Europe, ZFI is looking forward to a gradual transformation in domestic portfolio for driving sustainable growth ahead, in addition to rising exports. ZFI is looking forward to exceed its monthly offtake of ~2k units of ESC from H2FY24, driven by rising penetration in school buses and rising demand of electric buses, with value delta per vehicle being to the extent of Rs20k/unit for pneumatic ESC systems.

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Market Data

Market Cap (INR)	245bn
Market Cap (USD)	2,977mn
Bloomberg Code	ZCVCS IN
Reuters Code	ZFCV BO
52-week Range (INR)	13,100 /8,494
Free Float (%)	25.0
ADTV-3M (mn) (USD)	1

Price Performance (%)	3m	6m	12m
Absolute	26.5	39.5	51.3
Relative to Sensex	9.6	12.7	17.0

ESG Disclosure	2021	2022	Change
ESG score	0.0	0.0	0.0
Environment	0.0	0.0	0.0
Social	0.0	0.0	0.0
Governance	0.0	0.0	0.0

Note - Score ranges from 0 - 100 with a higher score indicating higher ESG disclosures.

Source: Bloomberg, I-sec research

Earnings Revisions (%)	FY24E	FY25E
Revenue	-	-
EBITDA	-	-
EPS	1.6	1.9

Previous Reports

27-05-2023: [Q4FY23 results review](#)

04-02-2023: [Q3FY23 results review](#)

Financial Summary

Y/E March (INR mn)	FY22A	FY23A	FY24E	FY25E
Net Revenue	25,434	34,442	43,907	52,719
EBITDA	2,525	4,704	6,806	8,435
EBITDA %	9.9	13.7	15.5	16.0
Net Profit	1,421	3,177	4,804	6,026
EPS (INR)	74.9	167.5	253.3	317.7
EPS % Chg YoY	36.9	123.6	51.2	25.4
P/E (x)	172.2	77.0	50.9	40.6
EV/EBITDA (x)	94.2	49.5	33.6	26.7
RoCE (%)	7.6	15.2	19.8	21.1
RoE (%)	6.7	13.2	16.8	17.7

- 160bps QoQ rise in gross margin led to a 10-quarter high level, though limited triggers for operating leverage QoQ, resulted in flat margin sequentially. ZFI is looking forward to reserve the improving gross margin trend, driven by continued improvement in portfolio mix as it is trying to reduce executing lower margin commoditised products and add more complex and better margin products. Also, ZFI is looking forward to improve its plant productivity and material yield in order to improve margin other than having a better pricing policy ahead. Larger customer base of ESC, EBS, ADAS and emergency braking system in trucks would drive profitable growth in coming years, with ZFI being the key beneficiary of the introduction of these components across CVs (including cargo trucks). Capex is planned at Rs2.5bn for FY24, including Rs1bn of maintenance capex.

Exhibit 1: Q1FY24 result summary

INR mn	Q1FY24	Q1FY23	YoY (%)	Q4FY23	QoQ (%)
Total operating income	9,668	7,984	21	9,769	-1
Raw material costs	5,993	5,196	15	6,214	-4
As a % of sales	62.0%	65.1%	-309 bps	63.6%	-161 bps
Gross Profit	3,675	2,788	32	3,556	3
Gross margin (%)	38.0%	34.9%	309 bps	36.4%	161 bps
Employee costs	1,146	880	30	1,026	12
As a % of sales	11.9%	11.0%	83 bps	10.5%	136 bps
Other expenditures	1,116	921	21	1,090	2
As a % of sales	11.5%	11.5%	1 bps	11.2%	39 bps
Total operating expenses	8,255	6,997	18	8,329	-1
EBITDA	1,413	987	43	1,440	-2
EBITDA margin (%)	14.6%	12.4%	225 bps	14.7%	-13 bps
Depreciation & Amortization	277	227	22	267	3
Other income	213	111	91	180	18
Interest costs	13	11	20	5	183
PBT	1,336	861	55	1,349	-1
Taxes	339	237	43	337	1
Reported PAT	997	624	60	1,012	-1

Source: I-Sec research, Company data

Exhibit 2: Q1FY24 segmental summary

(INR mn)	Q1FY24	Q1FY23	YoY (%)	Q4FY23	QoQ (%)
OEM	4,370	3,727	17.3	4,700	(7.0)
Exports	2,970	2,591	14.6	2,950	0.7
Aftermarket	1,207	1,025	17.8	1,250	(3.4)
Total	8,547	7,343	16.4	8,900	(4.0)

Source: I-Sec research, Company data

Exhibit 3: Segmental revenue assumptions

(INR mn)	FY20	FY21	FY22	FY23	FY24E	FY25E
OEM	7,695	6,847	10,311	14,951	17,941	19,735
Aftermarket	6,985	2,597	3,340	4,342	5,428	6,513
Exports	2,599	7,219	9,443	12,276	15,959	20,746
Services	2,017	1,972	2,340	3,392	4,580	5,725
Total	19,296	18,635	25,434	34,961	43,907	52,719

Source: I-Sec research, Company data

Downside risks

- Peaking out of CV cycle in FY24 itself.
- New products having higher elements of imports, impacting GM in FY24-25.
- Exports-related revenue expansion not getting executed seamlessly as expected.
- Rising mix of complex electronic products resulting in risk to profitability on the back of higher bargaining from OEMs.
- Rising competition in new product segments, impacting the pricing power of ZFI.

Upside risks

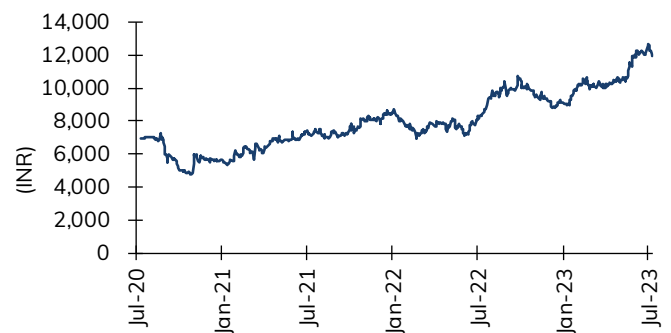
- CV upcycle getting prolonged beyond FY25.
- Inclusion of ZF products in overall portfolio happening at a rapid pace.
- Exports out of Oragadam (in Tamil Nadu) adding to revenue growth much higher than expected.
- Significant improvement in product mix led by new gen portfolio replacing legacy commoditised products.

Exhibit 4: Shareholding pattern

%	Dec'22	Mar'23	Jun'23
Promoters	75.0	75.0	75.0
Institutional investors	17.4	17.4	17.4
MFs and other	15.0	15.0	15.0
FIs/ Banks	0.0	0.0	0.0
Insurance Cos.	1.1	1.1	1.0
FIIIs	1.3	1.3	1.4
Others	7.6	7.6	7.6

Source: Bloomberg, I-Sec research

Exhibit 5: Price chart



Source: Bloomberg, I-Sec research

Financial Summary

Exhibit 6: Profit & Loss

(INR mn, year ending March)

	FY22A	FY23A	FY24E	FY25E
Net Sales	25,434	34,442	43,907	52,719
Operating Expenses	6,475	7,773	9,879	11,598
EBITDA	2,525	4,704	6,806	8,435
EBITDA Margin (%)	9.9	13.7	15.5	16.0
Depreciation & Amortization	924	1,048	1,150	1,250
EBIT	1,601	3,656	5,656	7,185
Interest expenditure	19	57	20	20
Other Non-operating Income	375	670	770	870
Recurring PBT	1,957	4,269	6,405	8,035
Profit / Loss from Associates	-	-	-	-
Less: Taxes	537	1,092	1,601	2,009
PAT	1,421	3,177	4,804	6,026
Less: Minority Interest	-	-	-	-
Extraordinaries (Net)	-	-	-	-
Net Income (Reported)	1,421	3,177	4,804	6,026
Net Income (Adjusted)	1,421	3,177	4,804	6,026

Source Company data, I-Sec research

Exhibit 7: Balance sheet

(INR mn, year ending March)

	FY22A	FY23A	FY24E	FY25E
Total Current Assets	15,566	21,387	28,281	34,112
of which cash & cash eqv.	6,691	11,694	16,013	19,402
Total Current Liabilities & Provisions	4,985	5,358	9,177	10,706
Net Current Assets	10,581	16,030	19,104	23,406
Investments	3,991	1,001	1,001	1,001
Net Fixed Assets	5,357	5,868	7,218	8,468
ROU Assets	-	-	-	-
Capital Work-in-Progress	203	770	770	770
Total Intangible Assets	-	-	-	-
Other assets	874	793	793	793
Deferred Tax assets	-	-	-	-
Total Assets	21,382	24,866	29,291	34,843
Liabilities				
Borrowings	-	-	-	-
Deferred Tax Liability	-	-	-	-
Provisions	239	158	158	158
Other Liabilities	3	617	617	617
Equity Share Capital	95	95	95	95
Reserves & Surplus	21,046	23,996	28,421	33,973
Total Net Worth	21,141	24,091	28,516	34,068
Minority Interest	-	-	-	-
Total Liabilities	21,382	24,866	29,291	34,843

Source Company data, I-Sec research

Exhibit 8: Quarterly trend

(INR mn, year ending March)

	FY22A	FY23A	FY24E	FY25E
Tax Burden (Adjusted PAT/PBT)	72.6	74.4	75.0	75.0
Interest Burden (PBT/EBIT)	122.3	116.8	113.3	111.8
EBIT Margin (EBIT/Sales)	6.3	10.6	12.9	13.6
Asset Turnover (Sales/Total Assets)	118.9	138.5	149.9	151.3
Financial Leverage (Total Assets/Equity)	101.1	103.2	102.7	102.3
ROE	6.7	13.2	16.8	17.7

Source Company data, I-Sec research

Exhibit 9: Cashflow statement

(INR mn, year ending March)

	FY22A	FY23A	FY24E	FY25E
Operating Cashflow	1,645	3,836	7,218	6,384
Working Capital Changes	(719)	(445)	1,244	(913)
Capital Commitments	(1,665)	(2,127)	(2,500)	(2,500)
Free Cashflow	(20)	1,709	4,718	3,884
Other investing cashflow	2,401	3,577	-	-
Cashflow from Investing Activities	737	1,450	(2,500)	(2,500)
Issue of Share Capital	-	-	-	-
Interest Cost	-	-	-	-
Inc (Dec) in Borrowings	-	-	-	-
Dividend paid	(228)	(247)	(379)	(474)
Others	(35)	(37)	(20)	(20)
Cash flow from Financing Activities	(263)	(283)	(399)	(494)
Chg. in Cash & Bank balance	2,119	5,003	4,319	3,389
Closing cash & balance	6,691	11,694	16,013	19,402

Source Company data, I-Sec research

Exhibit 10: Key ratios

(Year ending March)

	FY22A	FY23A	FY24E	FY25E
Per Share Data (INR)				
Reported EPS	74.9	167.5	253.3	317.7
Adjusted EPS (Diluted)	74.9	167.5	253.3	317.7
Cash EPS	123.6	222.7	313.9	383.6
Dividend per share (DPS)	12.0	13.0	20.0	25.0
Book Value per share (BV)	1,114.6	1,270.1	1,503.4	1,796.1
Dividend Payout (%)	16.0	7.8	7.9	7.9
Growth (%)				
Net Sales	52.6	35.4	27.5	20.1
EBITDA	22.7	86.2	44.7	23.9
EPS (INR)	36.9	123.6	51.2	25.4
Valuation Ratios (x)				
P/E	172.2	77.0	50.9	40.6
P/CEPS	104.3	57.9	41.1	33.6
P/BV	11.6	10.2	8.6	7.2
EV / EBITDA	94.2	49.5	33.6	26.7
EV / Sales	9.4	6.8	5.2	4.3
Profitability Ratios				
Gross Profit Margins (%)	35.4	36.2	38.0	38.0
EBITDA Margins (%)	9.9	13.7	15.5	16.0
EBIT Margins (%)	6.3	10.6	12.9	13.6
Net Profit Margins (%)	5.6	9.2	10.9	11.4
RoCE (%)	7.6	15.2	19.8	21.1
RoE (%)	6.7	13.2	16.8	17.7
Dividend Yield (%)	0.1	0.1	0.2	0.2
Operating Ratios				
Fixed Asset Turnover (x)	4.6	5.2	5.5	5.7
Inventory Turnover Days	21	17	17	17
Receivables Days	96	80	80	80
Payables Days	58	38	60	60
Effective Tax Rate (%)	27.4	25.6	25.0	25.0
Net Debt / Equity (x)	(0.3)	(0.5)	(0.6)	(0.6)
Net Debt / EBITDA (x)	(2.6)	(2.5)	(2.4)	(2.3)

Source Company data, I-Sec research

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