




SWARAJ ENGINE LTD.

Industry Auto Ancillary
Bloomberg SWE
BSE CODE 500407

Sluggish volume growth and higher fixed cost will drag the profitability

RATING	NEUTRAL
CMP	1492
Price Target	1617
Potential Upside	8%

Rating Change	
Estimate Change	
Target Change	

Stock Info

52wk Range H/L	2,139/1,320
Mkt Capital (Rs Cr)	1810
Free float (%)	49%
Avg. Vol 1M (,000)	2
No. of Shares (Cr.)	1
Promoters Pledged %	0%

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3Q FY19 Result Update

- ❑ SEL reported revenue growth of 8.4% YoY to Rs. 199 Crores which was below our estimates of Rs.215 crores.
- ❑ Engine volumes grew by 2.7% YoY to 22569 units due to subdued demand scenario in the tractor sales during the quarter. Realization grew by 5.7%YoY to Rs.88050 on account of price hikes and better product mix.
- ❑ Gross Margin declined by 80bps QoQ to 24.1% due to continuous increase in commodity prices. Higher manpower, other expense coupled with weaker operating leverage led to 240bps QoQ reduction in EBITDA margin.
- ❑ PAT for the quarter grew marginally by 0.6% YoY at Rs. 17 crores (vs our estimates of Rs. 21 crores) led by higher fixed cost and depreciation expense related to capacity addition.
- ❑ SEL has also finalized another capacity expansion program to increase its capacity to 135000 engines per annum from existing 120000 engines per annum by the end of FY19. This capacity expansion will be fully financed through the internal resources.

View and Valuation

EBITDA margin has contracted by 240bps QoQ due to weaker operating leverage and increasing commodity prices. The tractor demand has been sluggish in 3QFY19 due to subdued festive season and lower than expected rainfall in some of high volume states. The tractor industry is expected to grow at 11-12% in the current fiscal. However, we expect demand scenario in the industry to be strong backed by increase in MSP, ease in finance availability, increased demand from non agriculture sectors and low tractor penetration going ahead. Though, there has been a shift witnessed on the industry level towards below 30HP tractors due to small land available with the farmers and this could soften the realization and margins in the long run. Strong cash flows, negative working capital cycle, healthy return ratios and a payout of 70% gives us confidence of management's commitment towards its business. Factoring the near term softness in tractor demand and management' inability to pass on cost pressure due to stiff competition we tweak our FY19 EPS estimate by 6% but largely maintain our FY20 estimates. We recommend Neutral rating on SEL with a target price of Rs.1617 (20x FY20e EPS).

Key Risks to our rating and target

- ❑ Slowdown in tractor industry.
- ❑ Further increase in commodity prices.

KEY FINANCIAL/VALUATIONS	FY16	FY17	FY18	FY19E	FY20E
Net Sales	526	666	771	893	972
EBITDA	74	105	122	135	154
EBIT	60	88	105	116	134
PAT	51	69	80	84	98
EPS (Rs)	41	55	66	69	81
EPS growth (%)	(0)	34%	19%	5%	17%
ROE (%)	20%	24%	35%	34%	35%
ROCE (%)	23%	31%	46%	46%	47%
BV	212	228	188	206	234
P/B (X)	4.0	6.5	10.6	7.2	6.4
P/E (x)	20.7	26.6	30.3	21.5	18.5

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3QFY19 Results

Below expectation

Financials	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	YoY %	QoQ%	FY17	FY18	YoY %
Net Sales	183	185	235	247	199	8%	-20%	666	771	16%
Other Income	5	4	4	4	4	-18%	4%	17	19	10%
Total Income	188	189	238	251	203	8%	-19%	683	790	16%
COGS	137	138	177	185	151	10%	-19%	496	574	16%
Staff Cost	9	9	10	10	10	12%	-1%	31	35	12%
Other Exp.	11	9	12	11	10	-9%	-9%	35	40	16%
Expenditure	158	157	198	207	171	9%	-17%	561	650	16%
EBITDA	26	29	37	40	27	7%	-31%	105	122	16%
Depreciation	4	4	5	5	5	12%	-2%	16	17	3%
EBIT	21	24	32	35	23	6%	-36%	88	105	19%
Interest	-	1	0	-	-	-	-	0	1	677%
PBT	26	28	36	39	27	2%	-32%	105	123	16%
Excpt. Item	-	-	-	-	-	-	-	-	-	-
Tax	9	10	13	14	9	4%	-32%	37	43	16%
PAT	17	18	23	25	17	1%	-32%	69	80	16%

Slowdown in Revenue growth with reduced Volumes of Swaraj Tractor

The company reported revenue growth of 8.4% YoY to Rs. 199 crores (vs our estimates of Rs.215 crores) led by 3%YoY volume growth and 5.7%YoY realization growth in 3QFY19. The engine volumes stood at 22569 units during the quarter led by subdued festive season and lower than expected rainfall in some of the high volume states like; Gujarat, Maharashtra, Andhra Pradesh and Bihar. M&M expects 11-12% growth in domestic tractor business in FY19. Going ahead the industry has many levers for growth such as; increase in MSP, subsidy support for tractor purchase by several States, successive normal monsoon in large part of the country, ease in availability of retail finance and low tractor penetration has been paving the way for 8-9% growth for next 3-4 years for the domestic tractor industry.

Weaker operating leverage coupled with higher commodity prices impacted margins

Gross Margins reduced by 80 bps on QoQ basis at 24.1% due to higher raw material cost since last two quarters. However, commodities prices have stabilized in 3QFY19 which may result in some improvement in margins 4QFY19 onwards. Weaker operating leverage led by lower volumes resulted in lowest EBITDA margin in 12 quarter.

PAT margins impacted by higher fixed cost and depreciation

PAT for the quarter stood at Rs. 17 crores (vs our estimates of Rs.21 crores) in 3QFY19. PAT margins were reduced by 150 bps on QoQ basis at 8.7% due to higher fixed cost and depreciation related to capacity addition.

31-50 HP segment holds over 80% share

Domestic tractor industry sales trend (%)	FY14	FY15	FY16	FY17	FY18	1HFY19
Below 30 HP	11%	11%	11%	9%	10%	10%
31-40 HP	35%	37%	37%	35%	36%	36%
41-50 HP	49%	46%	46%	49%	47%	47%
Above 50 HP	5%	6%	7%	7%	8%	7%

Exhibit: Volume Trend

Slowdown in volume growth of Swaraj Engines to 3%YoY in 3QFY19

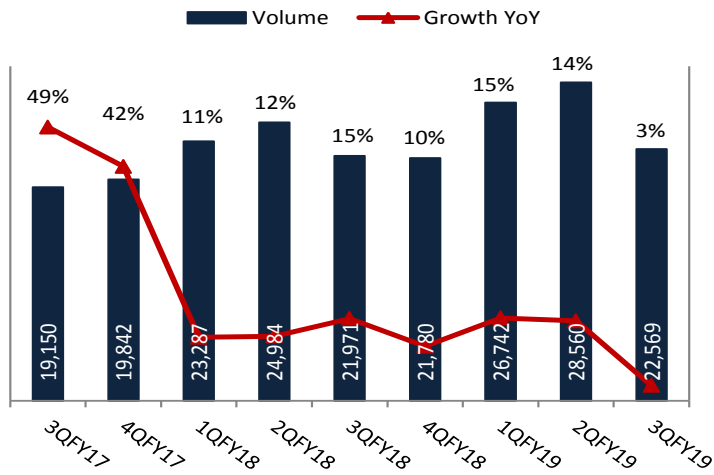


Exhibit: Realization Trend

Realization improved by 2% QoQ during the quarter due to change in mix of higher HP tractor

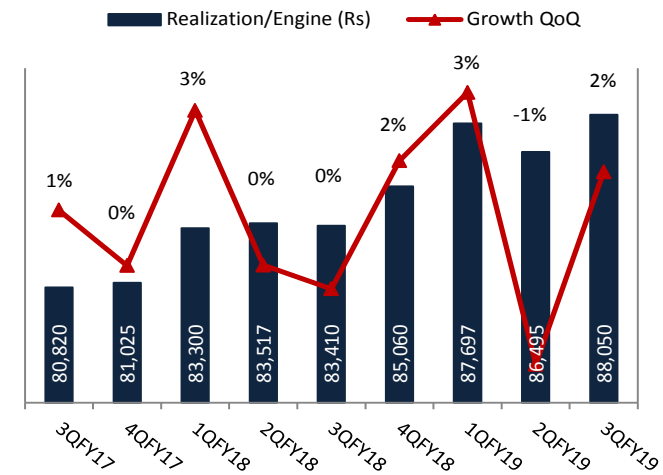


Exhibit: EBITDA (Rs. Crore) and EBITDA Margin Trend

Higher employee and other expenses reduced margins by 240bps on QoQ basis

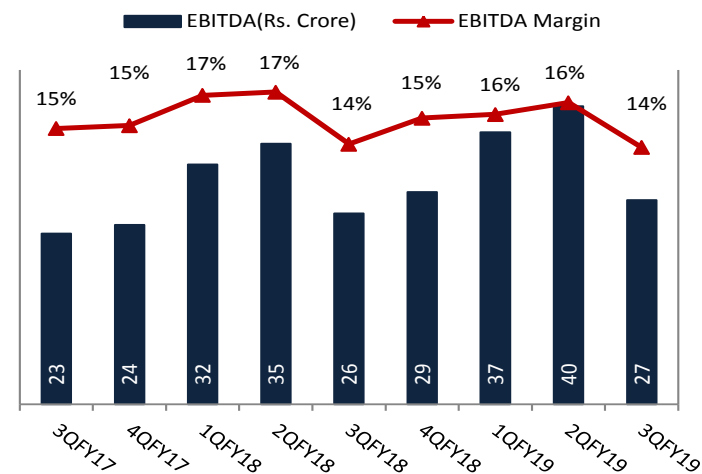


Exhibit: PAT (Rs. Crore) and PAT Margin Trend

PAT margins hampered due to decline in EBITDA margin and higher depreciation expenses

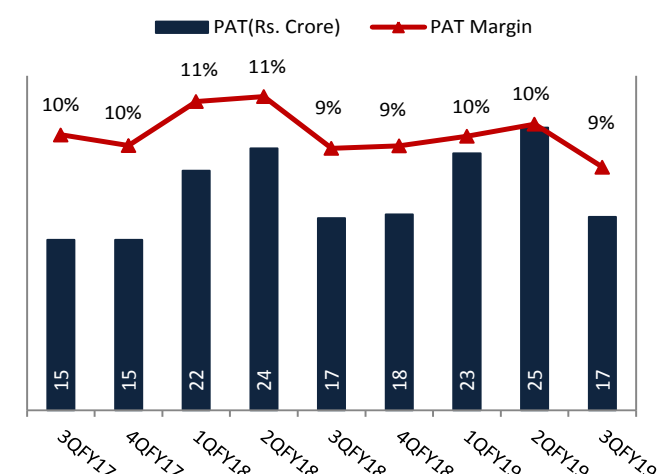


Exhibit: Capacity and Utilization Trend

Constant increase in capacity utilization level leading to growth of business

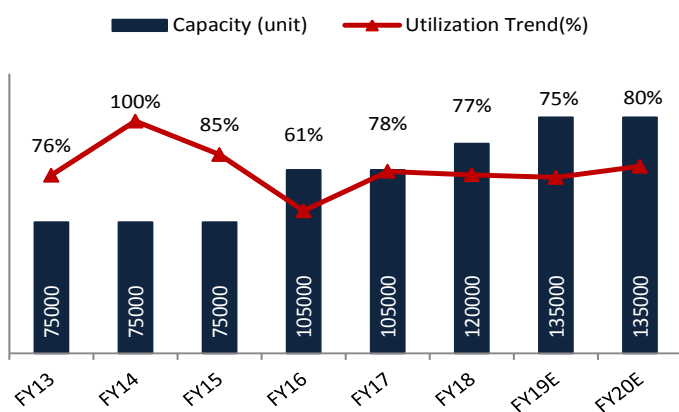
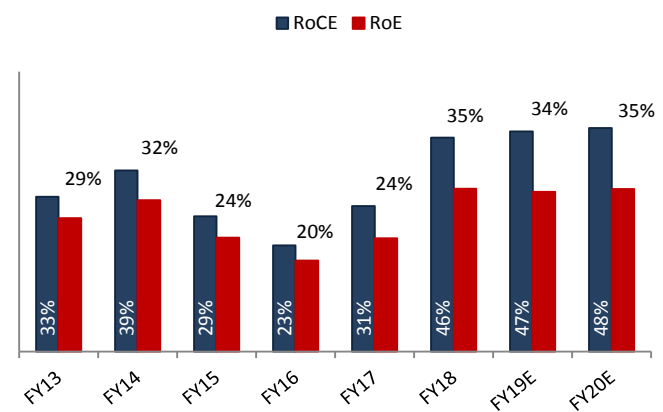


Exhibit: Return Ratios

Return ratios to improve going ahead



Financial Details

Balance Sheet

Y/E March	FY13	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E
Share Capital	12	12	12	12	12	12	12	12
Reserves	181	197	200	251	271	216	238	272
Networth	194	210	212	263	283	229	250	284
Debt	-	-	-	-	-	-	-	-
Other Non Cur Liab	8	9	8	10	9	9	9	9
Total Capital Employed	194	210	212	263	283	229	250	284
Net Fixed Assets (incl CWIP)	83	86	89	102	92	98	99	95
Non Cur Investments	-	-	-	-	-	-	-	-
Other Non Cur Asst	4	4	6	4	4	11	11	11
Non Curr Assets	87	90	94	106	96	109	110	106
Inventory	39	46	33	28	26	32	37	40
Debtors	9	8	7	7	13	15	18	19
Cash & Bank	81	105	140	108	49	47	55	81
Other Curr Assets	84	85	51	87	188	144	161	174
Curr Assets	214	245	231	230	276	239	271	315
Creditors	41	59	48	54	70	98	110	114
Provisons (both)	50	52	52	2	2	4	5	5
Other Curr Liab	9	4	5	7	7	7	7	7
Curr Liabilities	100	116	105	63	80	110	122	127
Net Curr Assets	114	129	126	167	197	129	149	188
Total Assets	301	334	325	337	372	348	381	421

Income Statement

Y/E March	FY13	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E
Revenue from Operation	479	608	540	526	666	771	893	972
Change (%)	7%	27%	-11%	-3%	27%	16%	16%	9%
Other Income	15	17	16	16	17	19	14	17
EBITDA	71	91	75	74	105	122	135	154
Change (%)	3%	27%	-18%	-1%	42%	16%	11%	14%
Margin (%)	15%	15%	14%	14%	16%	16%	15%	16%
Depr & Amor.	7	9	13	14	16	17	19	19
EBIT	64	82	62	60	88	105	116	134
Int. & other fin. Cost	0	0	0	0	0	1	0	-
EBT	80	99	78	76	105	123	130	152
Exp Item	-	1	-	-	-	-	-	-
Tax	24	31	26	25	37	43	46	53
Minority Int & P/L share of Ass.	-	-	-	-	-	-	-	-
Reported PAT	55	68	52	51	69	80	84	98
Adjusted PAT	55	68	52	51	69	80	84	98
Change (%)	5%	23%	-24%	-1%	34%	16%	5%	17%
Margin(%)	12%	11%	10%	10%	10%	10%	9%	10%

Financial Details

Key Ratios

Y/E March	FY13	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E
ROE	29%	32%	24%	20%	24%	35%	34%	35%
ROCE	33%	39%	29%	23%	31%	46%	46%	47%
Asset Turnover	1.6	1.8	1.7	1.6	1.8	2.2	2.3	2.3
Debtor Days	7	5	5	5	7	7	7	7
Inv Days	30	28	22	19	14	15	15	15
Payable Days	31	36	33	37	38	47	45	43
Int Coverage	428	1,979	4,806	1,499	680	104	1,446	-
P/E	8.9	12.6	19.4	20.7	26.6	30.3	21.5	18.5
Price / Book Value	3	4	5	4	6	11	7	6
EV/EBITDA	6	8	12	14	17	20	13	12
FCF per Share	6	45	31	29	61	54	72	84

Cash Flow Statement

Y/E March	FY13	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E
PBT	80	98	78	76	105	123	130	152
(inc)/Dec in Working Capital	(3)	8	8	13	15	11	4	(1)
Non Cash Op Exp	0	3	10	11	16	10	19	19
Int Paid (+)	(8)	(11)	(13)	(14)	(16)	(11)	-	-
Tax Paid	(21)	(30)	(27)	(24)	(38)	(43)	(46)	(53)
others	-	-	-	-	-	-	-	-
CF from Op. Activities	47	67	56	63	82	89	107	116
(inc)/Dec in FA & CWIP	(40)	(12)	(17)	(27)	(6)	(23)	(20)	(15)
Free Cashflow	8	55	39	36	76	66	87	101
(Pur)/Sale of Inv	7	2	30	32	(38)	(25)	(16)	(12)
others	15	(6)	(24)	(18)	13	96	-	-
CF from Inv. Activities	(18)	(16)	(11)	(14)	(32)	47	(36)	(27)
inc/(dec) in NW	-	-	-	-	-	(71)	-	-
inc/(dec) in Debt	-	-	-	(49)	(49)	(64)	-	-
Int. Paid	(0)	(0)	(0)	(0)	(0)	(1)	-	-
Div Paid (inc tax)	(19)	(48)	(51)	-	-	-	(63)	(64)
others	-	-	-	-	-	-	-	-
CF from Fin. Activities	(19)	(48)	(51)	(49)	(49)	(136)	(63)	(64)
Inc(Dec) in Cash	11	3	(6)	0	1	1	8	26
Add: Opening Balance	70	3	6	1	1	2	3	1
Closing Balance	81	6	1	1	2	3	56	81

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