

CMP: ₹ 1,770

Target: ₹ 2,135 (21%)

Target Period: 12 months

BUY

July 19, 2021

## Superior financial strength set to persist

**About the stock:** Swaraj Engines (SEL) is involved in manufacturing diesel engines for M&M's Swaraj brand of tractors.

- Steady ~13% compounding of revenues, EBITDA, PAT over past five years
- Net cash positive b/s; consistent cash flow generation; highly capital efficient player with history of >30% return ratios & high dividend payouts

**Q1FY22 Results:** SEL reported healthy Q1FY22 results

- Diesel engine volumes were flattish QoQ at 33,747 units
- Net sales rose 3.2% QoQ to ₹ 315 crore tracking 3.5% ASP increase
- Margins dipped minimally to 15%; PAT up 3.3% QoQ to ₹ 33.7 crore

**What should investors do?** The stock appreciated at ~9% CAGR from ~₹ 1,150 in July 2016 over the past five years, outperforming the broader Nifty Auto index.

- We retain **BUY** on expectation of continued industry-leading financials

**Target Price and Valuation:** We value SEL at 19x P/E on FY23E EPS to arrive at revised target price of ₹ 2,135 per share (earlier target price ₹ 1,650).

**Key triggers for future price performance:**

- Play on farm mechanisation courtesy ~30-33% volume share of M&M's tractor sales via Swaraj brand of tractors
- Consistent >30% return ratios along with positive CFO, FCF generation
- Attractive dividend play, with present dividend yield at ~4%
- Sales, PAT to grow at 13.1%, 21.4% CAGR respectively over FY21-23E, building in 8.5% volume CAGR & 120 bps improvement in EBITDA margins

**Alternate Stock Idea:** Apart from SEL in our ancillary coverage we also like JK Tyre.

- Walking the talk on B/S deleveraging, sweating of assets & capital efficiency.
- BUY with target price of ₹180

# SWARAJ

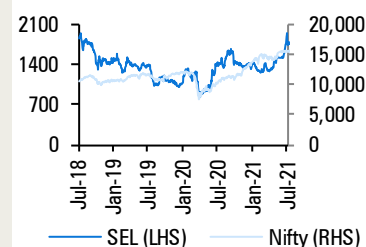
### Particulars

Particular	₹ crore
Market Capitalization	2,146.1
Total Debt (FY21)	0.0
Cash & Investments (FY21)	151.4
EV (FY21)	1,994.7
52 week H/L (₹)	1990 / 1255
Equity capital	12.1
Face value (₹)	10.0

### Shareholding pattern

	Sep-20	Dec-20	Mar-21	Jun-21
Promoter	52.2	52.2	52.2	52.2
FII	1.2	1.2	1.6	1.9
DII	13.0	12.1	10.4	10.7
Other	33.7	34.6	35.8	35.3

### Price Chart



### Recent event & key risks

- Posted healthy Q1FY22 results.
- Key Risk:** (i) Lower gross margin trajectory than earlier, (ii) Earlier than expected electrification in tractor segment

### Research Analyst

Shashank Kanodia, CFA  
shashank.kanodia@icicisecurities.com

Jaimin Desai  
jaimin.desai@icicisecurities.com

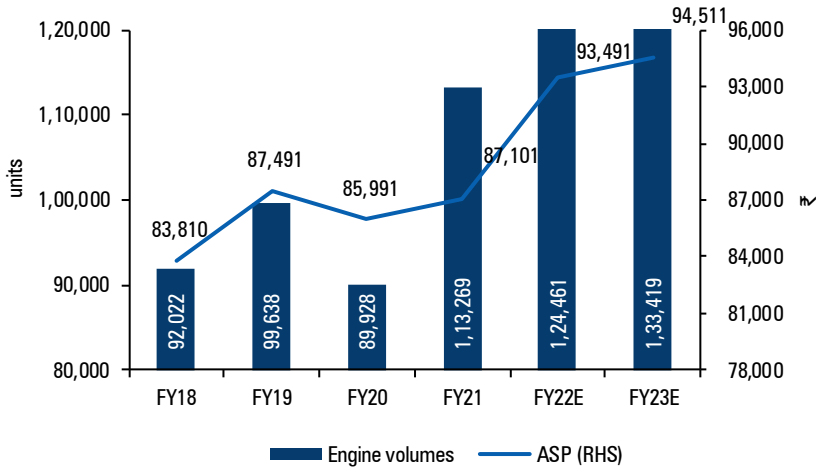
### Key Financial Summary

Key Financials	FY19	FY20	FY21	5 year CAGR (FY16-21)	FY22E	FY23E	2 year CAGR (FY21-23E)
Net Sales	871.7	773.3	986.6	13.4%	1,163.6	1,260.9	13.1%
EBITDA	131.7	100.4	135.7	13.0%	165.5	189.4	18.2%
EBITDA Margins (%)	15.1	13.0	13.8		14.2	15.0	
Net Profit	82.4	71.0	92.6	12.6%	117.7	136.4	21.4%
EPS (₹)	67.9	58.6	76.2		97.0	112.4	
P/E	26.0	30.2	23.2		18.3	15.7	
RoNW (%)	34.6	30.1	33.0		37.6	38.7	
RoCE (%)	47.1	34.0	41.3		46.1	47.3	

Source: Company, ICICI Direct Research

Financial story in charts

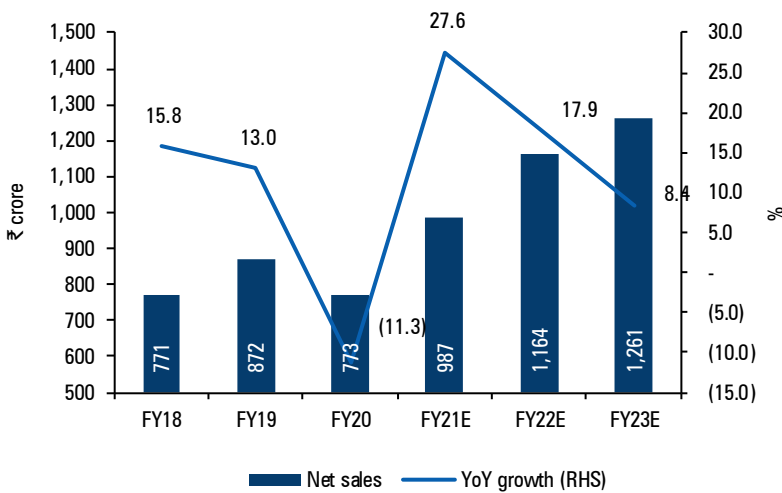
Exhibit 1: Trend in volumes and ASPs



SEL is seen posting 8.5% volume CAGR in FY21-23E with ASP seen increasing at 4.2% CAGR in that time

Source: Company, ICICI Direct Research

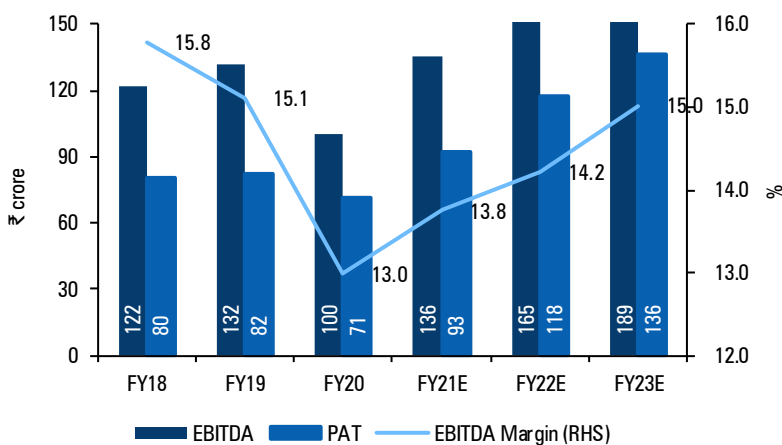
Exhibit 2: Trend in top line



Net sales are expected to grow at 13.1% CAGR over FY21-23E to ₹ 1,261 crore

Source: Company, ICICI Direct Research

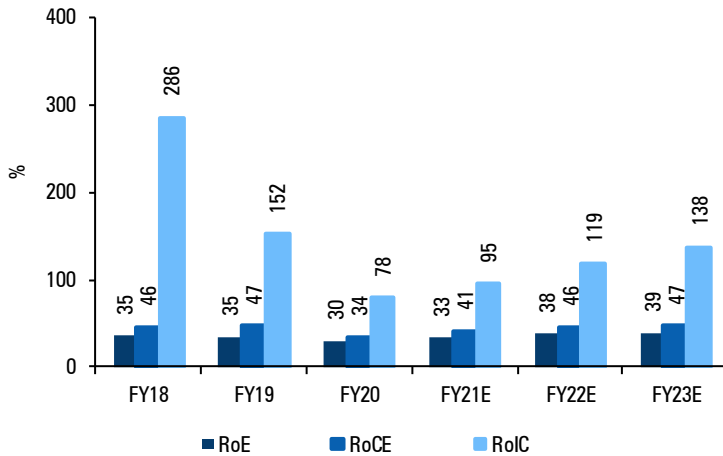
Exhibit 3: Trend in margins and profitability



We expect margins to reach 15% by FY23E on higher operating leverage, with PAT seen growing at 21.4% CAGR over FY21-23E to ₹ 136 crore

Source: Company, ICICI Direct Research

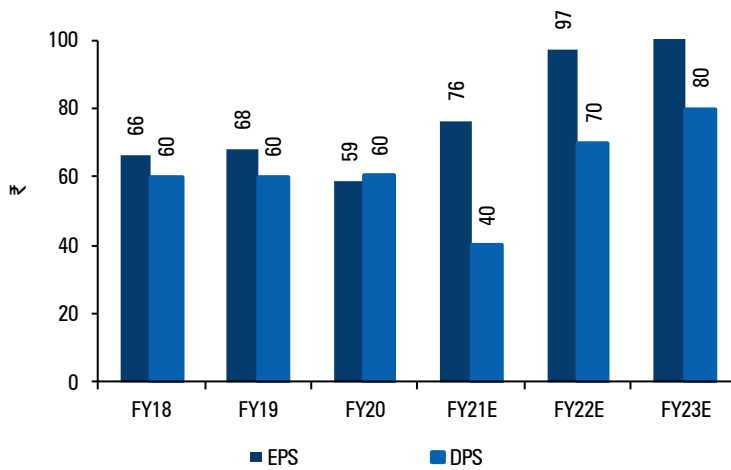
Exhibit 4: Trend in return ratios



With healthy double-digit return ratios and high cash on books, SEL is poised to continue to post industry-leading return ratios in future

Source: Company, ICICI Direct Research

Exhibit 5: Trend in EPS and DPS



Dividend payout ratio is expected to be at ~70% in FY22E and FY23E; thereby offering a healthy dividend yield of ~4%

Source: Company, ICICI Direct Research

Exhibit 6: Valuation Summary

	Sales (₹ cr)	Growth (%)	EPS (₹)	Growth (%)	PE (x)	EV/EBITDA (x)	RoNW (%)	RoCE (%)
FY19	871.7	13.0	67.9	2.8	26.0	15.1	34.6	47.1
FY20	773.3	-11.3	58.6	-13.8	30.2	20.1	30.1	34.0
FY21	986.6	27.6	76.2	30.2	23.2	14.7	33.0	41.3
FY22E	1163.6	17.9	97.0	27.2	18.3	11.8	37.6	46.1
FY23E	1260.9	8.4	112.4	15.9	15.7	10.1	38.7	47.3

Source: Company, ICICI Direct Research

## Financial Summary

Exhibit 7: Profit and loss statement				
	₹ crore			
(Year-end March)	FY20	FY21	FY22E	FY23E
<b>Net Sales</b>	<b>773.3</b>	<b>986.6</b>	<b>1,163.6</b>	<b>1,260.9</b>
Other Operating Income	-	-	-	-
Total Operating Income	773.3	986.6	1,163.6	1,260.9
Growth (%)	47.0	27.6	17.9	8.4
Raw Material Expenses	592.5	765.7	901.6	970.9
Employee Expenses	41.8	42.9	45.0	47.0
Other Operating Expense	38.6	42.3	51.5	53.6
Total Operating Expenditure	672.9	850.9	998.1	1,071.5
<b>EBITDA</b>	<b>100.4</b>	<b>135.7</b>	<b>165.5</b>	<b>189.4</b>
Growth (%)	36.5	35.1	22.0	14.5
Depreciation	20.1	19.8	20.9	22.7
Interest	0.0	-	-	-
Other Income	12.8	8.6	13.5	16.4
<b>PBT</b>	<b>93.1</b>	<b>124.5</b>	<b>158.0</b>	<b>183.1</b>
Exceptional Item	-	-	-	-
Total Tax	22.0	31.9	40.3	46.7
<b>PAT</b>	<b>71.0</b>	<b>92.6</b>	<b>117.7</b>	<b>136.4</b>
Growth (%)	38.8	30.3	27.2	15.9
<b>EPS (₹)</b>	<b>58.6</b>	<b>76.2</b>	<b>97.0</b>	<b>112.4</b>

Source: Company, ICICI Direct Research

Exhibit 8: Cash flow statement				
	₹ crore			
(Year-end March)	FY20	FY21	FY22E	FY23E
<b>Profit after Tax</b>	<b>71.0</b>	<b>92.6</b>	<b>117.7</b>	<b>136.4</b>
Add: Depreciation	20.1	19.8	20.9	22.7
(Inc)/dec in Current Assets	(28.7)	(94.2)	9.8	(16.6)
Inc/(dec) in CL and Provisions	(6.6)	62.6	(9.7)	14.0
Others	0.0	-	-	-
<b>CF from operating activities</b>	<b>55.9</b>	<b>80.8</b>	<b>138.8</b>	<b>156.6</b>
(Inc)/dec in Investments	(27.3)	76.9	(30.0)	(35.0)
(Inc)/dec in Fixed Assets	(16.1)	(5.9)	(20.0)	(20.0)
Others	1.0	(4.8)	-	-
<b>CF from investing activities</b>	<b>(42.4)</b>	<b>66.3</b>	<b>(50.0)</b>	<b>(55.0)</b>
Issue/(Buy back) of Equity	0.0	0.0	-	-
Inc/(dec) in loan funds	-	-	-	-
Dividend paid & dividend tax	(73.1)	(48.5)	(85.0)	(97.1)
Inc/(dec) in Share Cap	-	-	-	-
Others	0.0	0.5	-	-
<b>CF from financing activities</b>	<b>(73.1)</b>	<b>(48.0)</b>	<b>(85.0)</b>	<b>(97.1)</b>
Net Cash flow	(59.6)	99.0	3.8	4.5
Opening Cash	77.9	18.2	117.3	121.1
<b>Closing Cash</b>	<b>18.2</b>	<b>117.3</b>	<b>121.1</b>	<b>125.5</b>

Source: Company, ICICI Direct Research

Exhibit 9: Balance Sheet				
	₹ crore			
(Year-end March)	FY20	FY21	FY22E	FY23E
<b>Liabilities</b>				
Equity Capital	12.1	12.1	12.1	12.1
Reserve and Surplus	223.8	268.4	301.1	340.4
<b>Total Shareholders funds</b>	<b>236.0</b>	<b>280.5</b>	<b>313.3</b>	<b>352.6</b>
Total Debt	-	-	-	-
Deferred Tax Liability	4.6	0.6	0.6	0.6
Minority Interest / Others	-	-	-	-
<b>Total Liabilities</b>	<b>240.6</b>	<b>281.1</b>	<b>313.8</b>	<b>353.2</b>
<b>Assets</b>				
Gross Block	257.0	265.6	285.6	305.6
Less: Acc Depreciation	154.7	174.4	195.4	218.1
Net Block	102.3	91.1	90.2	87.5
Capital WIP	4.0	1.3	1.3	1.3
<b>Total Fixed Assets</b>	<b>106.4</b>	<b>92.5</b>	<b>91.5</b>	<b>88.8</b>
Investments	112.2	34.9	64.9	99.9
Inventory	37.0	61.7	63.8	69.1
Debtors	4.1	113.4	95.6	103.6
Loans and Advances	53.2	13.4	15.8	17.2
Other Current Assets	19.2	19.2	22.7	24.6
<b>Cash</b>	<b>18.2</b>	<b>117.3</b>	<b>121.1</b>	<b>125.5</b>
Total Current Assets	131.8	325.0	319.0	340.0
Current Liabilities	105.4	168.7	159.4	172.7
Provisions	9.1	8.5	8.1	8.7
Current Liabilities & Prov	114.6	177.2	167.5	181.5
<b>Net Current Assets</b>	<b>17.2</b>	<b>147.8</b>	<b>151.5</b>	<b>158.5</b>
Others Assets	4.7	5.9	5.9	5.9
<b>Application of Funds</b>	<b>240.6</b>	<b>281.1</b>	<b>313.8</b>	<b>353.2</b>

Source: Company, ICICI Direct Research

Exhibit 10: Key ratios				
(Year-end March)	FY20	FY21	FY22E	FY23E
<b>Per share data (₹)</b>				
EPS	58.6	76.2	97.0	112.4
Cash EPS	75.1	92.5	114.2	131.1
BV	194.5	231.1	258.1	290.5
DPS	40.0	69.0	70.0	80.0
Cash Per Share (Incl Invst)	107.5	125.3	153.2	185.7
<b>Operating Ratios (%)</b>				
EBITDA Margin	13.0	13.8	14.2	15.0
PAT Margin	9.2	9.4	10.1	10.8
Inventory days	17.5	22.8	20.0	20.0
Debtor days	2.0	41.9	30.0	30.0
Creditor days	49.8	62.4	50.0	50.0
<b>Return Ratios (%)</b>				
RoE	30.1	33.0	37.6	38.7
RoCE	34.0	41.3	46.1	47.3
RoIC	78.3	94.7	119.1	137.6
<b>Valuation Ratios (x)</b>				
P/E	30.2	23.2	18.3	15.7
EV / EBITDA	20.1	14.7	11.8	10.1
EV / Net Sales	2.6	2.0	1.7	1.5
Market Cap / Sales	2.8	2.2	1.8	1.7
Price to Book Value	9.1	7.7	6.9	6.1
<b>Solvency Ratios</b>				
Debt/EBITDA	-	-	-	-
Debt / Equity	-	-	-	-
Current Ratio	1.0	1.2	1.2	1.2
Quick Ratio	0.7	0.8	0.8	0.8

Source: Company, ICICI Direct Research

## RATING RATIONALE

ICICI Direct endeavors to provide objective opinions and recommendations. ICICI Direct assigns ratings to its stocks according to their notional target price vs. current market price and then categorizes them as Buy, Hold, Reduce and Sell. The performance horizon is two years unless specified and the notional target price is defined as the analysts' valuation for a stock

Buy: >15%

Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



**Pankaj Pandey**

**Head – Research**

**pankaj.pandey@icicisecurities.com**

**ICICI Direct Research Desk,  
ICICI Securities Limited,  
1st Floor, Akruiti Trade Centre,  
Road No 7, MIDC,  
Andheri (East)  
Mumbai – 400 093  
research@icicidirect.com**

## ANALYST CERTIFICATION

I/We, Shashank Kanodia, CFA, MBA (Capital Markets) and Jaimin Desai, CA, Research Analysts, authors and the names subscribed to this report, hereby certify that all of the views expressed in this research report accurately reflect our views about the subject issuer(s) or securities. We also certify that no part of our compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report. It is also confirmed that above mentioned Analysts of this report have not received any compensation from the companies mentioned in the report in the preceding twelve months and do not serve as an officer, director or employee of the companies mentioned in the report.

## Terms & conditions and other disclosures:

ICICI Securities Limited (ICICI Securities) is a full-service, integrated investment banking and is, inter alia, engaged in the business of stock brokering and distribution of financial products.

ICICI Securities is Sebi registered stock broker, merchant banker, investment adviser, portfolio manager and Research Analyst. ICICI Securities is registered with Insurance Regulatory Development Authority of India Limited (IRDAI) as a composite corporate agent and with PFRDA as a Point of Presence. ICICI Securities Limited Research Analyst SEBI Registration Number – INH000000990. ICICI Securities Limited SEBI Registration is INZ000183631 for stock broker. ICICI Securities is a subsidiary of ICICI Bank which is India's largest private sector bank and has its various subsidiaries engaged in businesses of housing finance, asset management, life insurance, general insurance, venture capital fund management, etc. ("associates"), the details in respect of which are available on [www.icicibank.com](http://www.icicibank.com).

ICICI Securities is one of the leading merchant bankers/ underwriters of securities and participate in virtually all securities trading markets in India. We and our associates might have investment banking and other business relationship with a significant percentage of companies covered by our Investment Research Department. ICICI Securities and its analysts, persons reporting to analysts and their relatives are generally prohibited from maintaining a financial interest in the securities or derivatives of any companies that the analysts cover.

Recommendation in reports based on technical and derivative analysis centre on studying charts of a stock's price movement, outstanding positions, trading volume etc. as opposed to focusing on a company's fundamentals and, as such, may not match with the recommendation in fundamental reports. Investors may visit [icidirect.com](http://icidirect.com) to view the Fundamental and Technical Research Reports.

Our proprietary trading and investment businesses may make investment decisions that are inconsistent with the recommendations expressed herein.

ICICI Securities Limited has two independent equity research groups: Institutional Research and Retail Research. This report has been prepared by the Retail Research. The views and opinions expressed in this document may or may not match or may be contrary with the views, estimates, rating, and target price of the Institutional Research.

The information and opinions in this report have been prepared by ICICI Securities and are subject to change without any notice. The report and information contained herein is strictly confidential and meant solely for the selected recipient and may not be altered in any way, transmitted to, copied or distributed, in part or in whole, to any other person or to the media or reproduced in any form, without prior written consent of ICICI Securities. While we would endeavour to update the information herein on a reasonable basis, ICICI Securities is under no obligation to update or keep the information current. Also, there may be regulatory, compliance or other reasons that may prevent ICICI Securities from doing so. Non-rated securities indicate that rating on a particular security has been suspended temporarily and such suspension is in compliance with applicable regulations and/or ICICI Securities policies, in circumstances where ICICI Securities might be acting in an advisory capacity to this company, or in certain other circumstances.

This report is based on information obtained from public sources and sources believed to be reliable, but no independent verification has been made nor is its accuracy or completeness guaranteed. This report and information herein is solely for informational purpose and shall not be used or considered as an offer document or solicitation of offer to buy or sell or subscribe for securities or other financial instruments. Though disseminated to all the customers simultaneously, not all customers may receive this report at the same time. ICICI Securities will not treat recipients as customers by virtue of their receiving this report. Nothing in this report constitutes investment, legal, accounting and tax advice or a representation that any investment or strategy is suitable or appropriate to your specific circumstances. The securities discussed and opinions expressed in this report may not be suitable for all investors, who must make their own investment decisions, based on their own investment objectives, financial positions and needs of specific recipient. This may not be taken in substitution for the exercise of independent judgment by any recipient. The recipient should independently evaluate the investment risks. The value and return on investment may vary because of changes in interest rates, foreign exchange rates or any other reason. ICICI Securities accepts no liabilities whatsoever for any loss or damage of any kind arising out of the use of this report. Past performance is not necessarily a guide to future performance. Investors are advised to see Risk Disclosure Document to understand the risks associated before investing in the securities markets. Actual results may differ materially from those set forth in projections. Forward-looking statements are not predictions and may be subject to change without notice.

ICICI Securities or its associates might have managed or co-managed public offering of securities for the subject company or might have been mandated by the subject company for any other assignment in the past twelve months.

ICICI Securities or its associates might have received any compensation from the companies mentioned in the report during the period preceding twelve months from the date of this report for services in respect of managing or co-managing public offerings, corporate finance, investment banking or merchant banking, brokerage services or other advisory service in a merger or specific transaction.

ICICI Securities encourages independence in research report preparation and strives to minimize conflict in preparation of research report. ICICI Securities or its associates or its analysts did not receive any compensation or other benefits from the companies mentioned in the report or third party in connection with preparation of the research report. Accordingly, neither ICICI Securities nor Research Analysts and their relatives have any material conflict of interest at the time of publication of this report.

Compensation of our Research Analysts is not based on any specific merchant banking, investment banking or brokerage service transactions.

ICICI Securities or its subsidiaries collectively or Research Analysts or their relatives do not own 1% or more of the equity securities of the Company mentioned in the report as of the last day of the month preceding the publication of the research report.

Since associates of ICICI Securities and ICICI Securities as a entity are engaged in various financial service businesses, they might have financial interests or beneficial ownership in various companies including the subject company/companies mentioned in this report.

ICICI Securities may have issued other reports that are inconsistent with and reach different conclusion from the information presented in this report.

Neither the Research Analysts nor ICICI Securities have been engaged in market making activity for the companies mentioned in the report.

We submit that no material disciplinary action has been taken on ICICI Securities by any Regulatory Authority impacting Equity Research Analysis activities.

This report is not directed or intended for distribution to, or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject ICICI Securities and affiliates to any registration or licensing requirement within such jurisdiction. The securities described herein may or may not be eligible for sale in all jurisdictions or to certain category of investors. Persons in whose possession this document may come are required to inform themselves of and to observe such restriction.