

M&M acquires further stake, to be sole promoter entity

About stock: Swaraj Engines (SEL) is involved in manufacturing diesel engines (20-85 hp) for M&M's Swaraj brand of tractors. Installed capacity - 1.5 lakh units (FY22).

- Steady ~10% 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

Key Highlights:

- M&M has informed exchanges about acquisition of 21,14,349 equity shares constituting 17.41% of the paid up equity share capital of the company (SEL) from Kirloskar Industries for ₹ 296 crore i.e. ₹ 1,400 per share
- Post this acquisition, M&M's stake in Swaraj Engines will increase to 52.13% vs. 34.72% earlier with SEL now being classified as a subsidiary of M&M. With this acquisition M&M now becomes the sole promoter at SEL
- Structurally, in terms of decision making, we do not foresee any change as the top management at SEL were all M&M veterans with automotive division head always on SEL board. We expect SEL's growth to largely mirror the tractor growth at Swaraj brand of tractors at M&M, as was the case in past

What should investors do? The stock has largely been flat in a five-year period from ~₹ 2000 in September 2017, underperforming the broader Nifty Auto index.

- We maintain **HOLD** rating tracking muted growth prospects in tractor space on high base of FY21 and await structural positives before turning positive

Target Price and Valuation: Upgrading our estimates, we now value SEL at ₹ 2,075 i.e. 18x P/E on FY24E EPS of ~₹ 115/share (earlier target price ₹ 1,680).

Key triggers for future price performance:

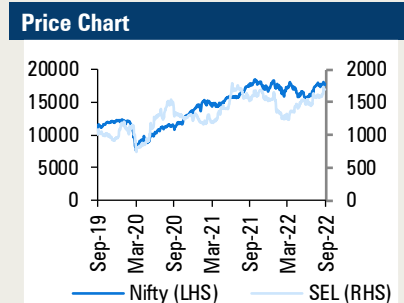
- Play on farm mechanisation courtesy ~33% volume share of M&M's tractor sales via Swaraj brand. Beneficiary of positive monsoons
- Superlative return ratios (RoCE: ~50%, RoIC: ~100%) along with positive CFO, FCF generation & high dividend yield (~5%)

Alternate Stock Idea: In our auto- ancillary coverage, we like Apollo Tyres.

- Walking the talk on b/s deleveraging, sweating of assets & capital efficiency
- BUY with target price of ₹335

Particulars	
Particular	₹ crore
Market Capitalization	2,303.8
Total Debt (FY22)	0.0
Cash & Invt. (FY22)	158.9
EV	2,144.8
52 week H/L (₹)	1926 / 1292
Equity capital	12.1
Face value (₹)	10.0

Shareholding pattern				
	Sep-21	Dec-21	Mar-22	Jun-22
Promoter	52.2	52.2	52.1	52.1
FII	1.5	1.9	1.8	1.9
DII	9.1	8.9	8.9	8.9
Other	37.3	37.1	37.1	37.1



Recent event & key risks

- SEL to become M&M's subsidiary
- Key Risk:** (i) Lower than expected tractor sales volumes, going forward, (ii) Higher than expected margin recovery over FY22-24E

Research Analyst

Shashank Kanodia, CFA
shashank.kanodia@icicisecurities.com

Raghvendra Goyal
raghvendra.goyal@icicisecurities.com

Key Financial Summary

Key Financials	FY20	FY21	FY22	5 year CAGR (FY17-22)	FY23E	FY24E	2 year CAGR (FY22-24E)
Net Sales	773.3	986.6	1,138.2	11.3%	1,304.2	1,407.3	11.2%
EBITDA	100.4	135.7	155.4	8.2%	170.4	197.0	12.6%
EBITDA Margins (%)	13.0	13.8	13.7		13.1	14.0	
Net Profit	71.0	92.6	109.5	9.7%	120.2	140.0	13.1%
EPS (₹)	58.6	76.2	90.2		99.0	115.3	
P/E	32.4	24.9	21.1		19.2	16.5	
RoNW (%)	30.1	33.0	35.8		38.0	42.5	
RoCE (%)	34.0	41.3	44.9		47.6	53.4	

Source: Company, ICICI Direct Research

Financial Summary

Exhibit 1: Profit and loss statement				
	₹ crore			
(Year-end March)	FY21	FY22	FY23E	FY24E
Net Sales	986.6	1,138.2	1,304.2	1,407.3
Other Operating Income	-	-	-	-
Total Operating Income	986.6	1,138.2	1,304.2	1,407.3
Growth (%)	27.6	15.4	14.6	7.9
Raw Material Expenses	765.7	890.2	1,026.8	1,097.7
Employee Expenses	42.9	43.9	46.9	49.3
Other Operating Expense	42.3	48.7	60.1	63.3
Total Operating Expenditure	850.9	982.8	1,133.7	1,210.3
EBITDA	135.7	155.4	170.4	197.0
Growth (%)	35.1	14.5	9.7	15.6
Depreciation	19.8	18.1	19.6	21.1
Interest	-	0.1	-	-
Other Income	8.6	9.7	10.5	12.0
PBT	124.5	146.8	161.4	187.9
Exceptional Item	-	-	-	-
Total Tax	31.9	37.4	41.2	47.9
PAT	92.6	109.5	120.2	140.0
Growth (%)	30.3	18.3	9.8	16.5
EPS (₹)	76.2	90.2	99.0	115.3

Source: Company, ICICI Direct Research

Exhibit 2: Cash flow statement				
	₹ crore			
(Year-end March)	FY21	FY22	FY23E	FY24E
Profit after Tax	92.6	109.5	120.2	140.0
Add: Depreciation	19.8	18.1	19.6	21.1
(Inc)/dec in Current Assets	(94.2)	6.9	(18.1)	(17.3)
Inc/(dec) in CL and Provisions	62.6	(21.5)	16.9	13.7
Others	-	0.1	-	-
CF from operating activities	80.8	113.0	138.5	157.5
(Inc)/dec in Investments	76.9	(2.1)	(5.0)	(5.0)
(Inc)/dec in Fixed Assets	(5.9)	(21.9)	(20.0)	(20.0)
Others	(4.8)	(31.0)	-	-
CF from investing activities	66.3	(55.0)	(25.0)	(25.0)
Issue/(Buy back) of Equity	0.0	-	-	-
Inc/(dec) in loan funds	-	-	-	-
Dividend paid & dividend tax	(48.5)	(97.1)	(109.2)	(127.5)
Inc/(dec) in Share Cap	-	-	-	-
Others	0.5	12.7	0.0	-
CF from financing activities	(48.0)	(84.4)	(109.2)	(127.5)
Net Cash flow	99.0	(26.4)	4.3	5.0
Opening Cash	18.2	117.3	90.9	95.2
Closing Cash	117.3	90.9	95.2	100.2

Source: Company, ICICI Direct Research

Exhibit 3: Balance Sheet				
	₹ crore			
(Year-end March)	FY21	FY22	FY23E	FY24E
Liabilities				
Equity Capital	12.1	12.1	12.1	12.1
Reserve and Surplus	268.4	293.5	304.5	317.0
Total Shareholders funds	280.5	305.7	316.6	329.2
Total Debt	-	-	-	-
Deferred Tax Liability	0.6	0.1	0.1	0.1
Minority Interest / Others	-	-	-	-
Total Liabilities	281.1	305.8	316.7	329.3
Assets				
Gross Block	265.6	287.2	307.2	327.2
Less: Acc Depreciation	174.4	192.5	212.1	233.2
Net Block	91.1	94.7	95.1	94.0
Capital WIP	1.3	1.6	1.6	1.6
Total Fixed Assets	92.5	96.3	96.7	95.6
Investments	34.9	36.5	41.5	46.5
Inventory	61.7	62.1	71.5	77.1
Debtors	113.4	103.6	107.2	115.7
Loans and Advances	13.4	12.5	14.3	15.4
Other Current Assets	19.2	22.7	26.0	28.1
Cash	117.3	90.9	95.2	100.2
Total Current Assets	325.0	291.7	314.1	336.4
Current Liabilities	168.7	145.1	160.8	173.5
Provisions	8.5	10.6	11.7	12.7
Current Liabilities & Prov	177.2	155.6	172.5	186.2
Net Current Assets	147.8	136.1	141.6	150.3
Others Assets	5.9	36.9	36.9	36.9
Application of Funds	281.1	305.8	316.7	329.3

Source: Company, ICICI Direct Research

Exhibit 4: Key ratios				
(Year-end March)	FY21	FY22	FY23E	FY24E
Per share data (₹)				
EPS	76.2	90.2	99.0	115.3
Cash EPS	92.5	105.1	115.1	132.7
BV	231.1	251.8	260.8	271.2
DPS	69.0	80.0	90.0	105.0
Cash Per Share (Incl Invst)	125.3	104.9	112.6	120.8
Operating Ratios (%)				
EBITDA Margin	13.8	13.7	13.1	14.0
PAT Margin	9.4	9.6	9.2	9.9
Inventory days	22.8	19.9	20.0	20.0
Debtor days	41.9	33.2	30.0	30.0
Creditor days	62.4	46.5	45.0	45.0
Return Ratios (%)				
RoE	33.0	35.8	38.0	42.5
RoCE	41.3	44.9	47.6	53.4
RoIC	94.7	98.0	106.4	121.9
Valuation Ratios (x)				
P/E	24.9	21.1	19.2	16.5
EV / EBITDA	15.9	14.0	12.7	10.9
EV / Net Sales	2.2	1.9	1.7	1.5
Market Cap / Sales	2.3	2.0	1.8	1.6
Price to Book Value	8.2	7.5	7.3	7.0
Solvency Ratios				
Debt/EBITDA	-	-	-	-
Debt / Equity	-	-	-	-
Current Ratio	1.2	1.3	1.3	1.3
Quick Ratio	0.8	0.9	0.9	0.9

Source: Company, ICICI Direct Research

RATING RATIONALE

ICICI Direct endeavours 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 Raghvendra Goyal, 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.

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 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 or its associates might have received any compensation for products or services other than investment banking or merchant banking or brokerage services from the companies mentioned in the report in the past twelve months.

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 actual/ beneficial ownership of one percent or more or other material conflict of interest 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.