AXIS SECURITIES

PPAP AUTOMOTIVE LTD

AUTO ANCILLARY

7 JUN 2019 Quarterly Update

BUY

Target Price: Rs. 324

Q4FY19: RM headwinds, slowdown in Auto impact growth

PPAP's consol Revenues were ↓22% YoY at Rs. 99.1cr thus missing our estimates ~9%. Decline in core part sales impacted the overall performance as PPAP's large customer Maruti witnesses' slowdown in its volumes. GMs/Op. Margins contracted 70bps/500bps due to sharp rise in costs, forex volatility and RM inflation (steel, crude volatility). EBITDA Margin at 17.4% was amongst lowest in the last 8 quarters. **23% Parts Revenues in Q4FY19 came in from new launches like New Honda Civic, New Maruti Baleno, Nissan Kick etc.**

Owing to dependence on PVs and Maruti we expect PPAP report sluggish growth in Revenues/PAT growth with some improvement in Op. Margin led by improving product mix, growing strong product development pipeline (25 projects in pipeline) across OEMs executable over next 24 months. Going forward, we believe, challenging demand environment for PVs and difficult macro-economic factors (liquidity issues, volatile crude oil prices etc) could be potential risk to our estimates. **We revise our FY20E and lower our TP to Rs. 324 valuing it at 10.5x FY21E EPS. Retain "BUY"**

CMP	: Rs 275
Potential Upside	: 17.9%
Relative to Sector	: Cautiously Positive

MARKET DATA

No. of Shares	: 1.4 Cr
FV (Rs)	: 10
Market Cap (Rs Cr.)	: 385
52-week High / Low	: Rs 620/ Rs 229
Avg. Daily vol. (6mth)	: 6,307 shares
Bloomberg Code	: PPAP IN
Reuters Code	: PPAP.NS
BSE Code	: 532934
NSE Code	: PPAP

Valuations

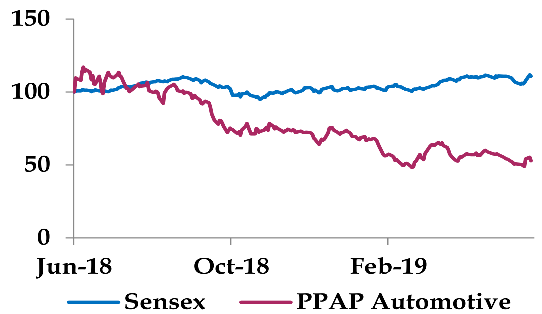
- In the near term there are impending challenges of auto sector slowdown plagued by liquidity crunch, relatively high real interest rates in the economy could dampen earnings growth. However, we believe, over the medium to long term PPAP Automotive could report ahead of industry growth over FY19-21E. This is owing to the fact that PPAP is the supplier of choice for PV manufacturers like Maruti which owns over 50% share in the domestic PV market and is the largest customer for PPAP. Besides Maruti Suzuki, PPAP also caters to OEMs like Hyundai the 2nd largest in Indian PV maker, Tata Motors, Renault Nissan, TKML, Volkswagen being some of them. With relationship for Hyundai having begun we believe, it will only gather momentum over FY20-21E and thereby de-risk revenue concentration risk for the company. However, owing to near term challenges our earnings estimates for FY20/21E see a sharp revision. We now expect PPAP to report Revenues/EBITDA/PAT CAGR of 7%/9%/13% over FY19-21E largely driven by new business contribution (majority being towards sealing systems) as new projects where PPAP is developing parts stands at ~25, focus on growing share of value added assemblies (ready-to-fit parts in vehicles). **Valuing the stock at 10.5x FY21E EPS, we arrive at a revised price target of Rs. 324 from a long term perspective.**

FINANCIAL SUMMARY (Consolidated)

Y/E March	Sales (Rs Cr)	EBITDA (Rs Cr)	PAT (Rs Cr)	EPS (Rs)	Change (YoY %)	P/E (x)	RoE (%)	RoCE (%)	EV/EBITDA (x)	DPS (Rs)
FY19	411	77	34	24.1	-14.2	11.4	6.6	9.7	5.1	4.5
FY20E	436	82	39	28.2	16.9	9.8	7.6	11.1	4.4	4.7
FY21E	470	92	43	30.9	9.7	8.9	7.8	11.4	3.6	4.8

Source: Company, Axis Securities; CMP as on 6th June 2019

PRICE PERFORMANCE



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Key Highlights (Cont'd)

- **Muted topline growth amid challenges:** In Q4FY19, PPAP Automotive reported a 22% YoY revenue de-growth at Rs. 99.1cr versus Rs. 127.6cr reported in Q4FY18 led by de-growth of 4% in Part Sales. The de-growth in Part sales is owing to sharp production cuts announced by OEMs led by Maruti (largest customer for PPAP). Tool Sales during Q4FY19 were Rs. 5.39cr as against Rs. 30.86cr in Q4FY18. Revenues from new part sales formed 23% of total revenues. During the quarter, the company started supplies to new models launched by Honda, Maruti, MG Motors (MG Hector model launched) and Nissan (Renault Nissan Kicks). For FY19, however, 9% topline has been reported by PPAP with total revenues at Rs. 388.6cr compared to Rs. 355.1cr in FY18. For FY19, Maruti along with Suzuki Motor Corp (SMG) continued to be the largest customer with 48% revenue share. This was followed by Honda Cars (31%), Nissan (7%) Toyota (5%), Tata (3%). Given that Hyundai was added only in FY19, revenue contribution was marginal. However, management has guided for 3% revenue contribution coming from Hyundai which has increased its focus on content localization thus benefiting PPAP Automotive.

- **EBITDA Margins contract 510bps much below PPAP's +20% margin profile:** Consecutively for 2nd quarter PPAP reported EBITDA Margin much lower than its 20% margin profile (more than 20% margins reported in over 8 quarters in the past). The contraction in EBITDA Margin in Q4FY19 was on account of higher RM prices (steel, crude), forex volatility which PPAP wasn't able to pass on to its customers. Typically, RM costs and Forex is passed onto OEM customers with a quarter lag. Rise in staff costs/other expenses (420bps/240bps) impacted overall operating margins. EBITDA Margins at 17.4% were lower than 22.5% a contraction of 510bps YoY. Management guided to maintain its EBITDA Margin between 18-20% going forward. We believe, during FY20 EBITDA Margin could remain under pressure owing to overall challenging environment in the auto sector. We estimate EBITDA Margin in FY20 to be 18.9%.

- **Strong product development pipeline:** PPAP has been working with its OEMs customers on new model development. As a result, the company is working on developing parts for 25 new models which are likely to be launched over the next 2 years. These are primarily for Hyundai, MG Motors and other OEMs. This we believe augurs well over the long term volume growth and thus gives us confidence on PPAP reporting ahead of industry volume/revenue growth over FY19-21E. We note, new models launched in the last 1 year have contributed to ~23% of toal Part Revenues which is healthy.

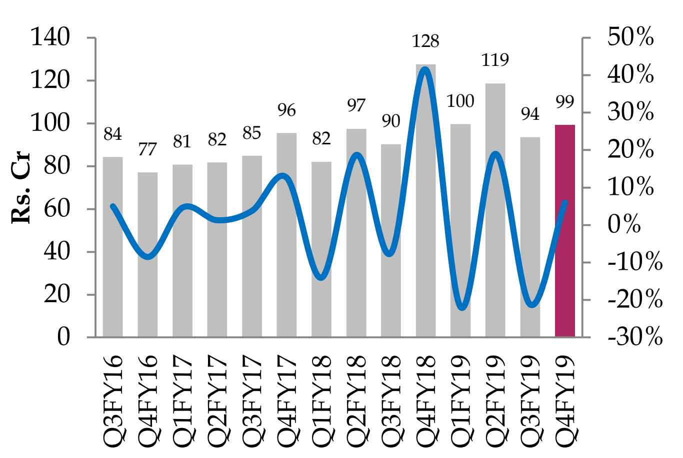
- **Industry Growth:** Domestic PV Segment reported a YoY de-growth of 4% in Q4FY19 i.e. 1.03 million PVs were produced in domestic market as against 1.07 million units in Q4FY18. The CV production remained flat on a YoY basis, while 2Ws production was 10% lower YoY at 5.4million units produced.

- Outlook: In the near term earnings growth looks challenging given the slowing down in volume sales by its key PV OEMs and uncertain RM environment (albeit crude at lows currently) thus we revise our earnings estimates and price target alongwith our rating on the stock. However, over the long term PPAP could deliver ahead of industry growth led by factors like 1) consistent focus on core competencies 2) improving product mix 3) grow content per vehicle with existing clients and new business with new clients 4) new client addition and 5) strong product development pipeline. In lieu of above mentioned factors in the near term, we revise our estimates downwards on Volumes/ Revenues / PAT for FY20/21. We expect PPAP to report 7%/13% Revenues/PAT CAGR over FY19-21E. Our revised TP now stands at Rs. 324 (10.5x FY21E) with a 'BUY' rating.

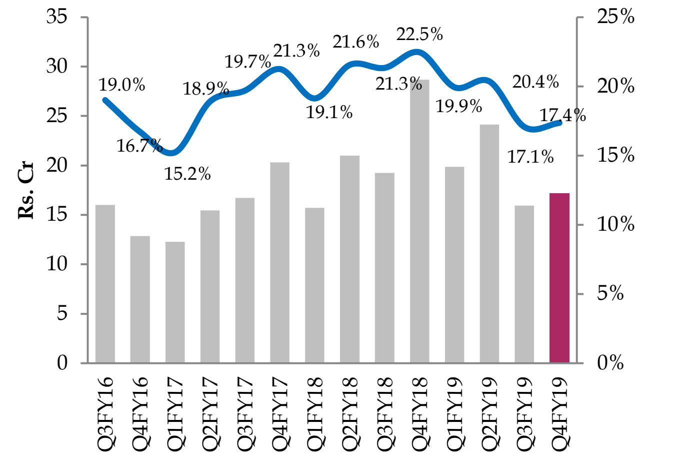
Key Con-call Highlights:

- **Capex:** FY19 total capex incurred by PPAP stood at Rs. 44cr which was utilized towards commissioning of Gujarat plant and maintenance capex. For FY20 capex requirements are likely to be much lower than FY19 and the management guided for a maintenance capex of Rs. 15-20crore going forward. However, if Suzuki Motor Gujarat (SMG) expands its capacity then PPAP may have to consider capacity expansion as per SMG which is the key client that PPAP services from its Viramgam facility. All capex going forward will be funded through internal accruals.
- PPAP Tokai India Rubber Pvt. Ltd. reported 18% growth in its topline which came in at Rs. 74.3cr vs Rs. 62.9cr. However, both EBITDA and PAT reported de-growth on a YoY basis given the initial set up costs. Management expects the JV company to start yielding to overall company profitability from FY20 onwards.
- **Debt: Equity (D:E)**: FY19 D:E stood at 0.08x vis-à-vis 0.11x reported in FY18.
- **Capacity Utilization:** In Q4FY19 overall utilization stood at 80%.

Revenue growth impacted on YoY basis



EBITDA Margin miss +20% as reported in FY18



Source: Company, Axis Securities

Results Update

	Quarterly Performance					Financial Year Ending			
(Rs.Cr.)	Q4FY19	Q4FY18	% Change (YoY)	Q3FY19	% Change (QoQ)	FY18	FY19	FY20E	FY21E
Sales	**99.1**	**127.6**	(22)	**93.5**	6	**397.6**	**411.0**	**435.6**	**470.5**
Other Op. Inc	0.0	0.0		0.0		0.0	0.0	0.0	0.0
Total Revenue	**99.1**	**127.6**	(22)	**93.5**	6	**397.6**	**411.0**	**435.6**	**470.5**
GM	**48.0**	**46.5**		**48.7**					
Expenditure									
Net Raw Material	51.5	68.3	(25)	48.0	7	199.0	210.6	224.4	242.3
Employee expenses	18.2	17.9	1	17.3	5	63.2	71.3	74.1	77.6
Other Exp	12.3	12.7	(4)	12.3	(0)	50.5	51.9	54.9	58.8
Total Expenditure	**81.9**	**98.9**	(17)	**77.6**	6	**312.7**	**333.8**	**353.3**	**378.7**
EBIDTA	**17.2**	**28.7**	(40)	**16.0**	8	**84.9**	**77.2**	**82.3**	**91.7**
EBITDA Margin (%)	**17.4%**	**22.5%**		**17.1%**		**21.3%**	**18.8%**	**18.9%**	**19.5%**
Oth. Inc.	0.3	0.5	(26)	0.2	40	2.6	1.1	2.8	2.8
Interest	0.9	1.0	(14)	0.8	1	4.4	4.0	3.8	3.7
Depreciation	6.6	6.7	(2)	6.5	2	26.0	26.0	24.4	28.4
Exceptional Item	0.0	0.0		0.0		0.0	0.0	0.0	0.0
PBT	**10.1**	**21.4**	(53)	**8.9**	14	**57.1**	**48.2**	**56.9**	**62.4**
Tax	3.1	7.3	(58)	3.0		19.6	14.8	17.5	19.2
PAT	**7.1**	**14.1**	(50)	**5.9**	19	**37.4**	**33.4**	**39.4**	**43.2**
Share of profit of Associates	0.0	0.0		0.0		0.0	2.9	1.9	0.0
Adjusted PAT	**7.1**	**14.1**	(50)	**5.9**	19	**37.4**	**36.3**	**41.3**	**43.2**
EPS (Rs.)	5.0	10.1		4.2		10.0	20.0	28.1	28.2

Source: Company, Axis Securities

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