

RESEARCH
Building Materials

Expert call – Demand moderation, cost rise may hurt Q2 margins

Syrma SGS Tech | NOT RATED

Niche player in EMS

SUMMARY
Building Materials

- Rising gas costs compelling Morbi ceramic manufacturers to switch to propane (~10% cheaper), with 300 of 850 units already converted
- Tile exports set to improve in Q3FY23 led by better container availability but could lose steam in FY24 owing to new global capacities
- Domestic demand slowdown and rising costs to hurt ceramic margins near term; retain KJC (leader) and SOMC (undervalued) as top picks

[Click here for the full report.](#)

Syrma SGS Tech

- Leading EMS player with best-in-class EBITDA margins of 11-13% vs. 4-8% for listed peers
- Offers a diverse product suite across industrial, auto, consumer electronic and medical applications
- FY23 revenue guided to grow on par with industry at 40%, with ODM share in the mix stable at >25%

[Click here for the full report.](#)

Daily macro indicators

Indicator	20-Sep	21-Sep	Chg (%)
US 10Y yield (%)	3.56	3.53	(3bps)
India 10Y yield (%)	7.26	7.23	(3bps)
USD/INR	79.76	79.98	(0.3)
Brent Crude (US\$/bbl)	90.6	89.8	(0.9)
Dow	30,706	30,184	(1.7)
Hang Seng	18,781	18,445	(1.8)
Sensex	59,720	59,457	(0.4)
India FII (US\$ mn)	19-Sep	20-Sep	Chg (\$ mn)
FII-D	(0.1)	(31.1)	(31.0)
FII-E	91.9	226.4	134.5

Source: Bank of Baroda Economics Research

BOBCAPS Research

research@bobcaps.in



BUILDING MATERIALS

22 September 2022

Expert call: Demand moderation, cost rise may hurt Q2 margins

- Rising gas costs compelling Morbi ceramic manufacturers to switch to propane (~10% cheaper), with 300 of 850 units already converted
- Tile exports set to improve in Q3FY23 led by better container availability but could lose steam in FY24 owing to new global capacities
- Domestic demand slowdown and rising costs to hurt ceramic margins near term; retain KJC (leader) and SOMC (undervalued) as top picks

Ruchitaa Maheshwari
 research@bobcaps.in

We interacted with Kiritbhai Patel, President – Sanitaryware Division, Morbi Ceramics Association, to gain a perspective on industry prospects and gas costs. Takeaways:

Morbi industry switching from gas to propane: With propane prices at a 10% discount to gas in Q2FY23, the ceramics industry has embarked on a transition to propane-based capacities. Out of the 850 manufacturing units in Morbi, Gujarat, +300 have already moved to a propane-based facility and 400-500 units intend to follow suit (manufacturing remains uncompromised).

Gas cost to remain elevated: Gas cost is hovering at Rs 60/scm (similar to Q1), and the industry expects prices to remain steady in the short run given long-term supply contracts and slower tile demand. However, gas prices are expected to rise in winter on higher consumption in Europe, halting supply from Russia and a depreciating rupee.

Tile exports could rebound to Rs 120bn-150bn in FY23...: India is the second largest tile manufacturer after China with a Rs 500bn market (up >10% from last year), of which Rs 13bn-14bn is branded (40% met through Morbi). Though the Morbi cluster had just Rs 11bn worth of tile exports in Q1FY23, Patel expects resurgent demand to help the industry close the year at Rs 120bn-150bn.

...but likely to slow in FY24: The outlook for FY24 is weaker as new capacities are set to mushroom in markets such as Vietnam, China, Turkey and Saudi Arabia plus increasing ADD (anti-dumping duty) activities in these countries.

Rise of Morbi brands a risk: Morbi is turning aggressive on brands building (Varmora, Simpolo, Lexus, Millennium), aided by foreign investment, which can pose a threat to incumbent domestic brands such as Kajaria and Somany. Further, KJC and SOMC have ~50% of production through job work (outsourcing), which may be unsustainable in FY24 as Morbi might cater to local demand via its own brands amid lower exports.

KJC, SOMC our top picks: We prefer market leader KJC (TP: Rs 1,460, BUY) for its strong brand and ability to hike prices. We like SOMC (TP: Rs 830, BUY) for its ~50% cheaper valuations than KJC, sanitaryware presence and strong demand base.

Recommendation snapshot

Ticker	Price	Target	Rating
KJC IN	1,234	1,460	BUY
SOMC IN	592	830	BUY

Price & Target in Rupees | Price as of 21 Sep 2022



**NOT
RATED**
SYRMA SGS TECH

| Consumer Durables

| 22 September 2022

Niche player in EMS

- **Leading EMS player with best-in-class EBITDA margins of 11-13% vs. 4-8% for listed peers**
- **Offers a diverse product suite across industrial, auto, consumer electronic and medical applications**
- **FY23 revenue guided to grow on par with industry at 40%, with ODM share in the mix stable at >25%**

Vinod Chari | Nilesh Patil
 Tanay Rasal
 research@bobcaps.in

We interacted with the Syrma SGS (SYRMA, Not Rated). Key takeaways are:

Niche player: SYRMA is a leading electronics engineering and design manufacturer that distinguishes itself from industry peers via its high mix and low-volume approach, diverse industry offerings and focus on high-margin products.

Differentiated ODM capabilities: Unlike listed peers DIXON and AMBER, SYRMA generates significant contribution as an original design manufacturer (ODM). Its product design segment contributed 27% of FY22 revenue and is guided to hold at similar levels ahead. Further, SYRMA offers diverse products across industrial, auto, consumer electronic and medical applications, whereas DIXON (majorly mobiles, electronics) and AMBER (air conditioners) are limited to select verticals.

Bright future for EMS: India's electronics manufacturing services (EMS) sector is witnessing rapid growth and looks set to outpace the global EMS market with a 41% CAGR to US\$ 81bn in FY26 from US\$ 14bn in FY21 (~6x growth), as per the company. Favourable sectoral tailwinds by way of the government's performance-linked incentive scheme, China Plus One, import substitutions and increased investments are catalysing demand.

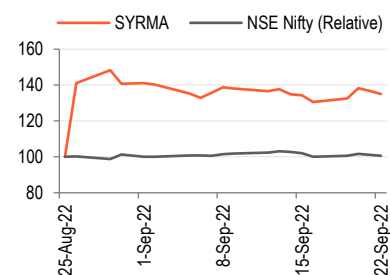
Expanding ahead of expected demand boom: Besides its existing manufacturing plants, SYRMA is establishing greenfield capacity at Manesar (Haryana). It has also announced brownfield/greenfield capacity additions to be commissioned by H2FY23/Q1FY24. The company expects expansion to yield an added ~Rs 20bn (FY22: Rs 12.6bn) in revenue at peak capacity, enabling it to replicate industry growth (~40%).

Margin guided to settle in early double digits: SYRMA expects operating margins to stabilise post a deterioration from the mid-teens in FY20 to early double-digits in FY22 (still ahead of DIXON/AMBER: 3.5%/6.5%). The addition of a marquee client in FY20 had resulted in a spike in margins. The company expects to maintain an 11-13% threshold over the long term and believes its focus on high-value products would help sustain its margin outperformance vis-à-vis peers.

Ticker/Price	SYRMA IN/Rs 297
Market cap	US\$ 668mn
Free float	15%
3M ADV	US\$ 0.01mn
52wk high/low	Rs 343/Rs 256
Promoter/FPI/DII	47%/4%/7%

Source: NSE | Price as of 21 Sep 2022

Stock performance



Source: NSE



Disclaimer

Recommendation scale: Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

HOLD – Expected return from -6% to +15%

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

Our recommendation scale does not factor in short-term stock price volatility related to market fluctuations. Thus, our recommendations may not always be strictly in line with the recommendation scale as shown above.

Rating distribution

As of 31 August 2022, out of 119 rated stocks in the BOB Capital Markets Limited (BOBCAPS) coverage universe, 67 have BUY ratings, 30 have HOLD ratings, 5 are rated ADD*, 1 is rated REDUCE* and 16 are rated SELL. Of these, 2 companies rated BUY and 1 rated ADD have been investment banking clients in the last 12 months. (*Our ADD and REDUCE ratings are in the process of being migrated to the new recommendation structure.)

Analyst certification

Each of the analysts mentioned in this research report certify, with respect to the sections of the report for which they are responsible, that (1) all of the views expressed in this report accurately reflect his/her personal views about the subject company or companies and its or their securities, and (2) no part of his/her compensation was, is, or will be, directly or indirectly, related to the specific recommendation(s) or view(s) in this report. Analysts are not registered as research analysts by FINRA and are not associated persons of BOBCAPS.

Important disclosures

This product is a compilation of previously published research notes. To view the complete report along with the associated Analyst certifications and Company-specific disclosures, please click on the hyperlink accompanying each excerpt.

General disclaimers

BOBCAPS is engaged in the business of Stock Broking and Investment Banking. BOBCAPS is a member of the National Stock Exchange of India Limited and BSE Limited and is also a SEBI-registered Category I Merchant Banker. BOBCAPS is a wholly owned subsidiary of Bank of Baroda which has its various subsidiaries engaged in the businesses of stock broking, lending, asset management, life insurance, health insurance and wealth management, among others.

BOBCAPS's activities have neither been suspended nor has it defaulted with any stock exchange authority with whom it has been registered in the last five years. BOBCAPS has not been debarred from doing business by any stock exchange or SEBI or any other authority. No disciplinary action has been taken by any regulatory authority against BOBCAPS affecting its equity research analysis activities.

BOBCAPS has obtained registration as a Research Entity under SEBI (Research Analysts) Regulations, 2014, having registration No.: INH000000040 valid till 03 February 2025. BOBCAPS is also a SEBI-registered intermediary for the broking business having SEBI Single Registration Certificate No.: INZ000159332 dated 20 November 2017. BOBCAPS CIN Number: U65999MH1996GOI098009.

BOBCAPS prohibits its analysts, persons reporting to analysts, and members of their households from maintaining a financial interest in the securities or derivatives of any companies that the analysts cover. Additionally, BOBCAPS prohibits its analysts and persons reporting to analysts from serving as an officer, director, or advisory board member of any companies that the analysts cover.

Our salespeople, traders, and other professionals may provide oral or written market commentary or trading strategies to our clients that reflect opinions contrary to the opinions expressed herein, and our proprietary trading and investing businesses may make investment decisions that are inconsistent with the recommendations expressed herein. In reviewing these materials, you should be aware that any or all of the foregoing, among other things, may give rise to real or potential conflicts of interest. Additionally, other important information regarding our relationships with the company or companies that are the subject of this material is provided herein.

This material should not be construed as an offer to sell or the solicitation of an offer to buy any security in any jurisdiction where such an offer or solicitation would be illegal. We are not soliciting any action based on this material. It is for the general information of BOBCAPS's clients. It does not constitute a personal recommendation or take into account the particular investment objectives, financial situations, or needs of individual clients. Before acting on any advice or recommendation in this material, clients should consider whether it is suitable for their particular circumstances and, if necessary, seek professional advice.

The price and value of the investments referred to in this material and the income from them may go down as well as up, and investors may realize losses on any investments. Past performance is not a guide for future performance, future returns are not guaranteed and a loss of original capital may occur. BOBCAPS does not provide tax advice to its clients, and all investors are strongly advised to consult with their tax advisers regarding any potential investment in certain transactions — including those involving futures, options, and other derivatives as well as non-investment-grade securities — that give rise to substantial risk and are not suitable for all investors. The material is based on information that we consider reliable, but we do not represent that it is accurate or complete, and it should not be relied on as such. Opinions expressed are our current opinions as of the date appearing on this material only. We endeavour to update on a reasonable basis the information discussed in this material, but regulatory, compliance, or other reasons may prevent us from doing so.

We and our affiliates, officers, directors, and employees, including persons involved in the preparation or issuance of this material, may from time to time have "long" or "short" positions in, act as principal in, and buy or sell the securities or derivatives thereof of companies mentioned herein and may from time to time add to or dispose of any such securities (or investment). We and our affiliates may assume an underwriting commitment in the securities of companies discussed in this document (or in

related investments), may sell them to or buy them from customers on a principal basis, and may also perform or seek to perform investment banking or advisory services for or relating to these companies and may also be represented in the supervisory board or any other committee of these companies.

For the purpose of calculating whether BOBCAPS and its affiliates hold, beneficially own, or control, including the right to vote for directors, one per cent or more of the equity shares of the subject company, the holdings of the issuer of the research report is also included.

BOBCAPS and its non-US affiliates may, to the extent permissible under applicable laws, have acted on or used this research to the extent that it relates to non-US issuers, prior to or immediately following its publication. Foreign currency denominated securities are subject to fluctuations in exchange rates that could have an adverse effect on the value or price of or income derived from the investment. In addition, investors in securities such as ADRs, the value of which are influenced by foreign currencies, effectively assume currency risk. In addition, options involve risks and are not suitable for all investors. Please ensure that you have read and understood the Risk disclosure document before entering into any derivative transactions.

In the US, this material is only for Qualified Institutional Buyers as defined under rule 144(a) of the Securities Act, 1933. No part of this document may be distributed in Canada or used by private customers in the United Kingdom.

No part of this material may be (1) copied, photocopied, or duplicated in any form by any means or (2) redistributed without BOBCAPS's prior written consent.

Other disclosures

BOBCAPS does not have any financial interest in the subject company. BOBCAPS does not have actual/beneficial ownership of one per cent or more securities in the subject company at the end of the month immediately preceding the date of publication of this report.

BOBCAPS is not engaged in any market making activities for the subject company.

BOBCAPS or its associates may have material conflict of interest at the time of publication of this research report.

BOBCAPS's associates may have financial interest in the subject company. BOBCAPS's associates may hold actual / beneficial ownership of one per cent or more securities in the subject company at the end of the month immediately preceding the date of publication of this report.

BOBCAPS or its associates may have managed or co-managed a public offering of securities for the subject company or may have been mandated by the subject company for any other assignment in the past 12 months.

BOBCAPS may have received compensation from the subject company in the past 12 months. BOBCAPS may from time to time solicit or perform investment banking services for the subject company. BOBCAPS or its associates may have received compensation from the subject company in the past 12 months for services in respect of managing or co-managing public offerings, corporate finance, investment banking or merchant banking, brokerage services or other advisory services in a merger or specific transaction. BOBCAPS or its associates may have received compensation for products or services other than investment banking or merchant banking or brokerage services from the subject company in the past 12 months.