

# FIRST LIGHT

28 September 2020

## RESEARCH

### [Initiation] Swaraj Engines | Target: Rs 1,300 | -10% | SELL

Healthy prospects but valuations full – initiate with SELL

## SUMMARY

### Swaraj Engines

Swaraj Engines (SWE) is the sole supplier of engines for M&M-owned Swaraj tractors which command ~12% market share in the 800,000-unit p.a. tractor industry. A successful rabi harvest, signs of healthy kharif cultivation and aggressive tractor financing bolster growth prospects. Given its strong support from M&M, debt-free status, government thrust on farm mechanisation and a growing rural economy, we value the stock at Rs 1,300, set at 18x Sep'22E EPS. However, the ~60% share price rally since Apr'20 prices in most positives; initiate with SELL.

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

## TOP PICKS

### LARGE-CAP IDEAS

Company	Rating	Target
<a href="#">Bajaj Finance</a>	Buy	4,000
<a href="#">Cipla</a>	Buy	850
<a href="#">GAIL</a>	Buy	155
<a href="#">Petronet LNG</a>	Buy	310
<a href="#">Tech Mahindra</a>	Buy	910

### MID-CAP IDEAS

Company	Rating	Target
<a href="#">Alkem Labs</a>	Buy	3,600
<a href="#">Chola Investment</a>	Buy	280
<a href="#">Laurus Labs</a>	Buy	1,200
<a href="#">Transport Corp</a>	Buy	270
<a href="#">Mahanagar Gas</a>	Sell	750

Source: BOBCAPS Research

## DAILY MACRO INDICATORS

Indicator	Current	2D (%)	1M (%)	12M (%)
US 10Y yield (%)	0.67	(1bps)	1bps	(103bps)
India 10Y yield (%)	5.99	0bps	(17bps)	(72bps)
USD/INR	73.91	(0.5)	0.6	(4.3)
Brent Crude (US\$/bbl)	41.94	0.4	(7.1)	(33.2)
Dow	26,815	0.2	(5.3)	(0.3)
Shanghai	3,223	(1.7)	(4.8)	10.0
Sensex	36,554	(3.0)	(5.8)	(6.2)
India FII (US\$ mn)	23 Sep	MTD	CYTD	FYTD
FII-D	25.6	475.7	(14,614.3)	(4,854.8)
FII-E	(527.3)	4.5	4,811.8	11,414.8

Source: Bank of Baroda Economics Research

## BOBCAPS Research

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**SELL**

TP: Rs 1,300 | ▼ 10%

**SWARAJ ENGINES**

| Auto Components

| 25 September 2020

## Healthy prospects but valuations full – initiate with SELL

**Swaraj Engines (SWE) is the sole supplier of engines for M&M-owned Swaraj tractors which command ~12% market share in the 800,000-unit p.a. tractor industry. A successful rabi harvest, signs of healthy kharif cultivation and aggressive tractor financing bolster growth prospects. Given its strong support from M&M, debt-free status, government thrust on farm mechanisation and a growing rural economy, we value the stock at Rs 1,300, set at 18x Sep'22E EPS. However, the ~60% share price rally since Apr'20 prices in most positives; initiate with SELL.**

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**Rural recovery to catalyse growth:** After a successful rabi crop harvest, we are seeing early signs of stronger kharif cultivation as well. Mahindra & Mahindra-controlled Swaraj Division manufactures tractors and is a key player in the agriculture belts of Central and North India (~12% market share). SWE, being the sole engine supplier for M&M's Swaraj tractors, will be a direct beneficiary.

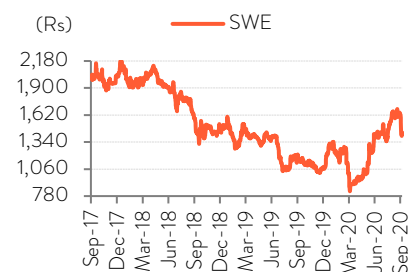
**Tractor industry expected to log 5% CAGR over FY20-FY23:** After declining in FY20, we expect a steady recovery in domestic tractor industry volumes, backed by a growing rural economy, favourable base, aggressive infrastructure spends and revival in the mining, aviation and agriculture sectors. We estimate a 5% CAGR in industry volumes during FY20-FY23, with SWE keeping pace, aiding a revenue/EBITDA/PAT CAGR of 8%/10%/9% for the company.

**Valuations full:** SWE has been a zero-debt company, clocking healthy ROE and ROCE of ~30% each for the last decade. Given steady growth prospects and a healthy balance sheet, we value the stock at 18x Sep'22E EPS, in line with its 10Y average P/E multiple. Strong demand visibility in the tractor space has led the stock to rally ~60% since Apr'20, taking valuations to 21x FY22E EPS. We believe most optimism is in the price – initiate with SELL and a Sep'21 TP of Rs 1,300.

Ticker/Price	SWE IN/Rs 1,441
Market cap	US\$ 237.3mn
Shares o/s	12mn
3M ADV	US\$ 0.2mn
52wk high/low	Rs 1,700/Rs 803
Promoter/FPI/DII	52%/1%/11%

Source: NSE

## STOCK PERFORMANCE



Source: NSE

## KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue (Rs mn)	8,717	7,733	8,161	8,764	9,749
EBITDA (Rs mn)	1,317	1,004	1,108	1,174	1,321
Adj. net profit (Rs mn)	824	711	770	826	928
Adj. EPS (Rs)	67.9	58.6	63.5	68.1	76.5
Adj. EPS growth (%)	2.9	(13.8)	8.4	7.2	12.4
Adj. ROAE (%)	34.6	30.1	27.9	28.9	31.9
Adj. P/E (x)	21.2	24.6	22.7	21.2	18.8
EV/EBITDA (x)	12.9	17.1	15.6	14.6	12.9

Source: Company, BOBCAPS Research



## Disclaimer

### Recommendations and Absolute returns (%) over 12 months

**BUY** – Expected return >+15%

**ADD** – Expected return from >+5% to +15%

**REDUCE** – Expected return from -5% to +5%

**SELL** – Expected return <-5%

**Note:** Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

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