

10th June 2024

Swaraj Engines Ltd. – BUY

CMP : Rs. 2,590
Target Price : Rs. 3,191
Upside : ~24%
Stop Loss : Rs. 2,327 (Closing basis)

Investment Thesis

- **Swaraj Engines (SWE)** is reporting consistent growth in engine sales every year, with FY20-FY24 CAGR at 9.06%. SWE is poised to grow at a 5-year CAGR of 9.58% for FY21-FY26E on the back of robust monsoon expectations in FY25 leading to positive farmer sentiments and crop growth.
- SWE had grown in engine sales in Q3 despite an industry de-growth, resulting in outperformance. Additionally, despite tractor sales decline of 3.33% YoY in Q4FY24, SWE reported engines sales growth of 1.44% in Q4FY24 YoY. Furthermore, future tailwinds in the form of a good monsoon season indicates better engine sales with FY25E growth at 24%
- SWE sell engines to the swaraj arm of Mahindra, who are leaders in the tractor segments. Mahindra & Mahindra reported volume growth of 1.7% on YoY basis in Apr-24, while other tractor makers reported a decline for the same period. Further tailwinds should favour Mahindra & Mahindra which augurs well for SWE.
- With the exit of Kirloskar industries from ownership of SWE, we believe the volumes to increase further enriching the valuations. We believe Kirloskar exit could provide full autonomy to SWE to increase volumes.
- SWE is expected to improve margins from cost reductions and improved sales mix in FY25E.

Financials

- Total Revenue for FY24 declined by 0.18% owing to an unfavourable monsoon resulting in a negative farmer sentiment. We believe the FY25E Revenue to grow by 30.2% to Rs. 1,847.85 Crs. owing to favourable monsoon which would result in a positive farmer sentiment and engine sales growth of 24% to 1,72,063 units.
- Additionally, the improved PAT profile further translates into a robust EPS growth which is seen at a 5-year CAGR of 13% for FY21-FY26E.

Particulars	FY21	FY22	FY23	FY24	FY25E
Revenue (Rs in Crs)	986.57	1,138.15	1,421.82	1,419.24	1,847.85
EBITDA (Rs in Crs)	135.63	155.39	185.55	188.17	247.61
Adj. PAT (Rs in Crs)	92.54	109.47	133.61	137.87	171.65
Adj. EPS (Rs.)	76.24	90.15	110.01	113.94	141.86
PE Multiple (x)	33.97	28.73	23.54	22.73	18.26
RoE (%)	32.98%	35.81%	39.04%	36.25%	37.96%

Stock Data

Market Cap (Rs. Crs)	2,986
Market Cap (\$ Mn)	358
Shares O/S (in Mn)	12.1
Avg. Volume (3 month)	15,746
52-Week Range (Rs.)	2,650 / 1,902

Shareholding Pattern

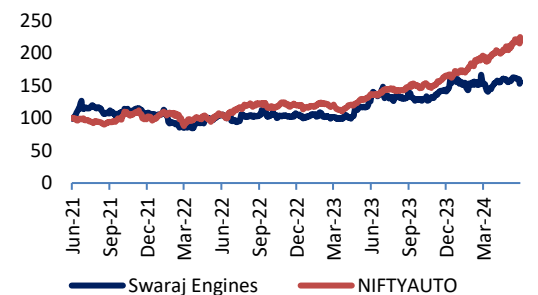
Promoters	52.12%
FII's	2.55%
Institutions	9.54%
Others (incl. body corporate)	35.79%

Key Ratios

Div Yield	3.85%
TTM PE	21.7x
ROE	38.8%
TTM EPS (Rs.)	114

Stock Performance

Performance (%)	1M	6M	1Yr
ABSOLUTE	0.1%	9.1%	23.8%
NIFTYAUTO	7.8%	36.5%	66.7%



- Consequently, the EBITDA is poised to grow 31.59% in FY25E through cost efficiencies and top-line growth expectations.
- The EBITDA margins are expected to increase by 24bps in FY25E to 13.40% as a result.
- The ROE should grow by 171bps to 37.96% in FY25E owing to improved earnings and cost efficiencies.

Key Business Highlights

- SWE was Established in 1985 in Mohali, Punjab, is principally involved in the business of providing engines to Mahindra & Mahindra Ltd.'s Swaraj Division (M&M). SWE produces and distributes diesel engines with displacements ranging from 22 HP to more than 65 HP. The business has extremely accurate and productive quality analysis equipment. Additionally, it produces advanced engine components.
- Over 16,00,000 engines have been provided by SWE to date for use in Swaraj tractors.
- SWE has been promoted jointly by Punjab Tractors Ltd. and Kirloskar Oil Engines Ltd. However, Kirloskar Industries have exited.
- In 1995 it expanded its capacity to 42,000 engines p.a. The services of DLPL are aimed at individual patients, hospitals, healthcare providers and corporate entities as well.
- SWE produces high-tech engine components at its production plant in SAS Nagar, Ropar, Punjab, as well as in its matching shop. It also has capacity for producing high-tech engine components for Swaraj Mazda vehicles. Additionally, it finished the capacity expansion programme that the Board had approved, and the increased capacity is now able to meet the demand for 1,50,000 engines annually.

Valuation

SWE is currently trading at a PE of 22.4x against industry PE of 38.9x signalling a high value unlocking opportunity. Additionally, the EV/EBITDA is trading at 14.3x against the median EV/EBITDA of 11.3x. The SWE has robust cash position that puts them in a position of net cash positive and ability to provide healthy dividends and expansion through internal accruals. We value SWE at a forward looking PE of 22.5x for FY25E.

The future demand scenario owing to robust monsoon expectations makes SWE an attractive opportunity for investment.

Therefore, in light of above, we ascribe a **BUY** rating for **SWE** with a **target price** of **Rs.3,191.00**, translating to an **upside** of **~24%**.

Risk & Concern

- Headwinds from raw material price volatility
- High Dependency on the monsoon season for demand
- Concentration risk since SWE derives majority revenue from a single client.

Graphs & Charts

Figure 1: Net Sales Trend (Rs. In Crs)

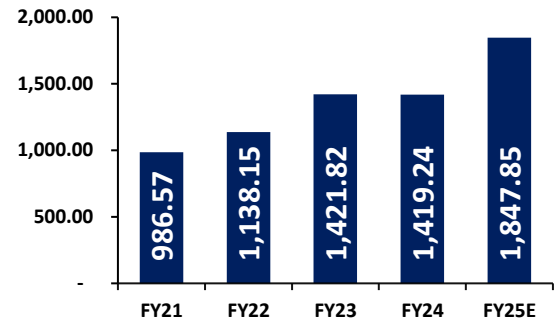


Figure 2: EBITDA & EBITDA Margin Trend

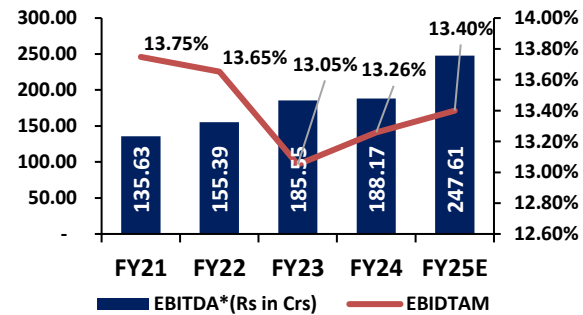


Figure 3: EPS Growth

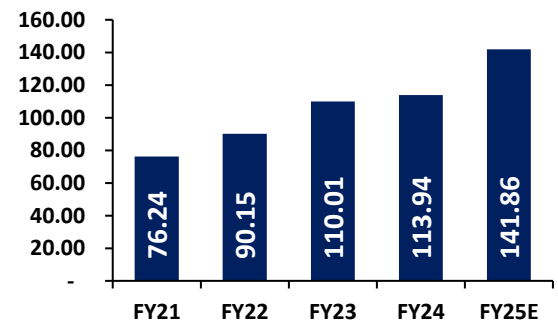
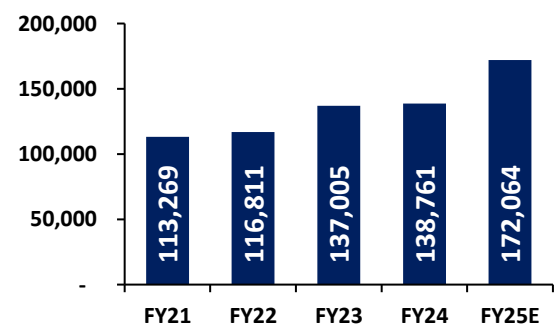


Figure 4: Engine Sales



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