

# Setco Automotive

**NOT RATED**

INDUSTRY	AUTOS		
<b>CMP (as on 24 Dec 2014)</b>	<b>Rs 239</b>		
<b>Target Price</b>	<b>NA</b>		
Nifty	8,174		
Sensex	27,209		
<b>KEY STOCK DATA</b>			
Bloomberg	SETC IN		
No. of Shares (mn)	27		
MCap (Rs bn) / (\$ mn)	6.4/100.6		
6m avg traded value (Rs mn)	7		
<b>STOCK PERFORMANCE (%)</b>			
<b>52 Week high / low</b>	<b>Rs 264/68</b>		
	3M	6M	12M
Absolute (%)	34.9	101.8	231.6
Relative (%)	33.2	94.6	202.2
<b>SHAREHOLDING PATTERN (%)</b>			
Promoters	63.01		
FIs & Local MFs	0.03		
FIIIs	4.05		
Public & Others	32.91		
<i>Source : BSE</i>			

## Geared up for the CV upcycle

*We hosted the management of Setco Automotive for a series of investor meetings. Setco is a leading supplier of MHCV clutches with 85% market share in the domestic market. The company's strategy of setting up an independent aftermarket channel and backward integrating into ferrous castings products could act as strong earnings growth drivers over the next 2-3 years. Management has set an ambitious target of scaling revenues to Rs 10bn by FY17-18. Current valuations at 24.3x P/E on an LTM basis appear attractive, considering the company's earnings are at near trough levels.*

### Below are key takeaways from these interactions

- **Market leadership in domestic market:** Setco is a market leader for supply of clutches to the MHCV segment with an 85% market share. The company's LIPE brand of clutches is well recognised across OEM and aftermarkets. Setco is a preferred supplier to all leading CV makers and has recently added customers such as Bharat Benz, MTBL and MAN Trucks.
- **Strengthening its business model:** High dependence on MHCV segment which saw a cyclical downturn in past two years has resulted in a 50% drop in sales to OEMs from FY12 peak levels. Setco's future strategy entails building counter cyclical and high growth revenue streams which include expanding its product offerings to LCV/Tractor segments and growing its independent aftermarket business.
- **Backward integration efforts underway:** Setco has entered into a 80:20 joint-venture with Lingotes

Especiales, Spain for setting up a ferrous foundry with a capacity of 30,000 MT and total investments of Rs 1.6bn. About 1/3<sup>rd</sup> of the output would cater to Setco's captive requirement and balance would be available for sale to outside customers. Besides achieving an important strategic objective of ensuring steady supply of castings for its internal requirements, the management believes the project is fairly lucrative with a potential to generate around Rs 2.3bn of revenues and above 20% EBITDA margins at peak utilisation.

- **Subsidiaries' performance to remain soft:** Setco's two key subsidiaries in UK and USA were essentially formed during its acquisition of the LIPE Clutch division from Dana Corp and Haldex's facility in USA. Both the subsidiaries are currently incurring losses. These subsidiaries undertake assembly and marketing activities for Setco's products, while bulk of the value addition and margins are retained by the parent entity.
- **Competitive landscape:** Competition is largely from global players who have set up operations in India. Component majors such as Eaton Corp (USA), Valeo (France), Sachs (Germany) and LUK (Germany) have presence in India; but they have a larger focus on PV, LCV and Tractor segments.
- **Capex plans:** Setco has already invested ~60-65% of the total Rs 1.6bn investment for its ferrous foundry facility with the balance likely to be invested by Mar'15. Over FY16/17, Setco's capex spends are likely to be moderate in the range of Rs 100-150mn/year towards maintenance capex, technology upgradation and any de-bottlenecking efforts.

**INCOME STATEMENT : CONSOLIDATED**

Year ending March (Rs mn)	FY12	FY13	FY14	1H14*	1H15*
<b>Net Sales</b>	<b>4,176</b>	<b>3,994</b>	<b>3,899</b>	<b>1,376</b>	<b>2,145</b>
<b>Growth (%)</b>	<b>18.3%</b>	<b>-4.4%</b>	<b>-2.4%</b>	<b>-8.0%</b>	<b>55.8%</b>
Material Expenses	2,358	2,220	2,187	802	1,296
Employee Expenses	401	463	522	154	187
Other Operating Expenses	664	744	813	274	392
<b>EBIDTA</b>	<b>752</b>	<b>567</b>	<b>378</b>	<b>146</b>	<b>270</b>
<b>EBIDTA (%)</b>	<b>18.0%</b>	<b>14.2%</b>	<b>9.7%</b>	<b>10.6%</b>	<b>12.6%</b>
<b>EBIDTA Growth (%)</b>	<b>15.8%</b>	<b>-24.7%</b>	<b>-33.4%</b>	<b>-34.2%</b>	<b>85.2%</b>
Other Income	33	49	94	126	67
Depreciation	108	123	136	49	62
EBIT	677	492	336	223	276
Interest	187	197	234	95	111
PBT	490	295	102	128	164
Tax	6	33	(4)	18	20
PAT	455	262	183	110	145
EO items (net of tax)	(28)	-	77	-	-
<b>APAT</b>	<b>483</b>	<b>262</b>	<b>106</b>	<b>110</b>	<b>145</b>
<b>APAT Growth (%)</b>	<b>44.3%</b>	<b>-45.8%</b>	<b>-59.6%</b>	<b>-12.0%</b>	<b>31.0%</b>
<b>Adj EPS</b>	<b>27.4</b>	<b>9.8</b>	<b>4.0</b>	<b>4.1</b>	<b>5.4</b>
<b>EPS Growth (%)</b>	<b>44.3%</b>	<b>-64.2%</b>	<b>-59.6%</b>	<b>-12.0%</b>	<b>31.0%</b>

Source: Company, HDFC sec Inst Research

\* Half year financials based on standalone numbers

**BALANCE SHEET : CONSOLIDATED**

Year ending March (Rs mn)	FY12	FY13	FY14	1H14*	1H15*
<b>SOURCES OF FUNDS</b>					
Share Capital	176	267	267	267	267
Reserves	1,160	1,552	1,628	1,561	1,743
<b>Total Shareholders Funds</b>	<b>1,336</b>	<b>1,818</b>	<b>1,895</b>	<b>1,828</b>	<b>2,009</b>
Long Term Debt	106	111	211	128	745
Short Term Debt**	1,484	1,698	1,636	1,261	1,002
<b>Total Debt</b>	<b>1,590</b>	<b>1,808</b>	<b>1,847</b>	<b>1,389</b>	<b>1,747</b>
Deferred Taxes	57	66	73	77	84
Long Term Provisions & Others	5	8	6	10	6
<b>TOTAL SOURCES OF FUNDS</b>	<b>2,988</b>	<b>3,701</b>	<b>3,821</b>	<b>3,304</b>	<b>3,846</b>
<b>APPLICATION OF FUNDS</b>					
<b>Net Block</b>	<b>1,029</b>	<b>1,370</b>	<b>1,501</b>	<b>1,287</b>	<b>1,378</b>
CWIP	119	139	76	-	-
Investments, LT Loans & Adv	337	560	766	792	1,202
Inventories	889	1,111	1,193	670	730
Debtors	886	795	699	675	768
Cash & Equivalents	88	28	53	5	25
ST Loans & Advances, Others	206	204	212	386	421
<b>Total Current Assets</b>	<b>2,407</b>	<b>2,698</b>	<b>2,923</b>	<b>2,529</b>	<b>3,146</b>
Creditors	410	326	480	297	503
Other Current Liabilities & Provns	157	180	200	214	176
<b>Total Current Liabilities</b>	<b>567</b>	<b>506</b>	<b>679</b>	<b>511</b>	<b>679</b>
<b>Net Current Assets</b>	<b>1,840</b>	<b>2,192</b>	<b>2,243</b>	<b>2,018</b>	<b>2,467</b>
Misc Expenses & Others	-	-	-	-	-
<b>TOTAL APPLICATION OF FUNDS</b>	<b>2,988</b>	<b>3,701</b>	<b>3,821</b>	<b>3,304</b>	<b>3,846</b>

Source: Company, HDFC sec Inst Research

\* Half year financials based on standalone numbers

\*\* Short term debt for FY includes current maturities on long term debt. HY does not include the same as details not available

**CASH FLOW : CONSOLIDATED**

Year ending March (Rs mn)	FY12	FY13	FY14
Reported PAT	483	262	106
Non-operating & EO items	-	-	-
PAT from Operations	483	262	106
Interest expenses	187	197	234
Depreciation	108	123	136
Working Capital Change	(405)	(263)	117
Others	(16)	(13)	3
<b>OPERATING CASH FLOW ( a )</b>	<b>358</b>	<b>307</b>	<b>569</b>
Capex	(244)	(173)	(88)
Free cash flow (FCF)	114	134	481
Investments	(125)	(150)	(146)
Others	3	14	24
<b>INVESTING CASH FLOW ( b )</b>	<b>(366)</b>	<b>(308)</b>	<b>(210)</b>
Debt Issuance	323	221	39
Interest expenses	(187)	(197)	(234)
Share capital Issuance	5	10	0
Dividend	(82)	(83)	(83)
Others	(2)		
<b>FINANCING CASH FLOW ( c )</b>	<b>57</b>	<b>(50)</b>	<b>(278)</b>
<b>NET CASH FLOW (a+b+c)</b>	<b>49</b>	<b>(52)</b>	<b>82</b>
Non-operating and EO items	-	-	-
Closing Cash & Equivalents	88	28	53

Source: Company, HDFC sec Inst Research

**KEY RATIOS : CONSOLIDATED**

	FY12	FY13	FY14	1H14*	1H15*
<b>PROFITABILITY (%)</b>					
GPM	43.5	44.4	43.9	41.7	39.6
EBITDA Margin	18.0	14.2	9.7	10.6	12.6
APAT Margin	11.6	6.6	2.7	8.0	6.7
RoE	42.8	16.6	5.7	11.9	15.1
RoIC or Core RoCE	21.9	10.7	6.6	5.0	9.6
RoCE	22.4	11.8	9.1	11.6	12.6
<b>EFFICIENCY</b>					
Tax Rate (%)	1.3	11.2	(3.4)	13.7	12.0
Asset Turnover (x)	1.4	1.1	1.0	0.8	1.1
Inventory (days)	78	102	112	89	62
Debtors (days)	77	73	65	90	65
Payables (days)	36	30	45	39	43
Cash Conversion Cycle (days)	119	144	132	139	85
Debt/EBITDA (x)	2.1	3.2	4.9	4.8	3.2
Net D/E (x)	1.33	1.13	0.97	0.74	0.90
Interest Coverage	3.6	2.5	1.4	2.3	2.5
<b>PER SHARE DATA</b>					
EPS (Rs/sh)	27.4	9.8	4.0	4.1	5.4
CEPS (Rs/sh)	33.5	14.4	9.1	6.0	7.7
DPS (Rs/sh)	4	3	3	-	-
BV (Rs/sh)	66	58	61	59	65
<b>VALUATION</b>					
P/E	8.9	24.9	61.6	29.5	22.5
P/BV	3.7	4.2	4.0	4.2	3.7
EV/EBITDA	7.7	14.6	22.0	27.1	15.2
OCF/EV (%)	6.2	3.7	6.9	-	-
FCF/EV (%)	2.0	1.6	5.8	-	-
FCFE/mkt cap (%)	5.8	2.4	4.4	-	-
Dividend Yield (%)	1.6	1.1	1.1	-	-

Source: Company, HDFC sec Inst Research

\* Half year financials based on standalone numbers and ratios have been calculated on annualised basis wherever applicable

### Rating Definitions

BUY	:	Where the stock is expected to deliver more than 10% returns over the next 12 month period
NEUTRAL	:	Where the stock is expected to deliver (-)10% to 10% returns over the next 12 month period
SELL	:	Where the stock is expected to deliver less than (-)10% returns over the next 12 month period

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