



Stock Note

India Nippon Electricals Ltd.

June 18, 2024



Industry	LTP	Recommendation	Base Case Fair Value	Bull Case Fair Value	Time Horizon
Auto Ancillaries	Rs 792	Buy in Rs 785-800 band and add on dips in Rs 700-715 band	Rs 863	Rs 932	2-3 quarters

HDFC Scrip Code	INDNIPQNR
BSE Code	532240
NSE Code	INDNIPPON
Bloomberg	INE IN
CMP Jun 11, 2024	792.2
Equity Capital (Rs Cr)	11.3
Face Value (Rs)	5
Equity Share O/S (Cr)	2.3
Market Cap (Rs Cr)	1792
Book Value (Rs)	275.5
Avg. 52 Wk Volumes	63,000
52 Week High	812.9
52 Week Low	386.1

Share holding Pattern % (Mar 2024)	
Promoters	70.4
Institutions	0.1
Non Institutions	29.5
Total	100.0



* Refer at the end for explanation on Risk Ratings

Fundamental Research Analyst

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Our Take:

India Nippon Electricals Ltd. (INEL) is a prominent manufacturer within the automotive industry, specializing in producing cutting edge electronic ignition systems. INEL's product offerings cover all custom-built ignition system parts for various applications to meet the whole range of OEMs in the vehicle industry and enjoys a market leadership position in the electronic ignition system products, and has also recently entered the market for electric vehicles. Its primary emphasis lies on the domains of two-wheelers and three-wheelers that account for 86% of revenues. It is gradually diversifying its product portfolio by launching new products for EV segment. It is actively developing a next-generation starter generator system to enhance efficiency and reducing emissions in internal combustion engines. The Indian auto-components industry is set to become the third-largest in the world by 2025.

The domestic 2W market is seeing signs of recovery and is expected to report a growth of 7-9% in FY25 (as per ICRA) bolstered by stable fuel prices, a favourable monsoon outlook, festive demand and the marriage season. Ignition System Market is estimated to grow at 8% CAGR to reach USD 16.4 Bn by 2029 over the next 5 years. INEL has undertaken expansion of its capacities at its 3 plants. The Company is strategically enhancing IC Engine content to cater to emerging customer segments while expanding its footprint through aftermarket engagement.

Valuation & Recommendation:

INEL is a debt free company with strong operational cash flows and high dividend payout. Considering the growth potential and expanding margins due to increasing export and aftermarket share we believe it is available at a compelling valuation. We expect INEL's Revenue/PAT to grow at 12/15% CAGR over FY24-FY26. Investors can buy the stock in the band of Rs 785-800 and add on dips in Rs 700-715 band (20.5x FY26E EPS) for a base case fair value of Rs 863 (25x FY26E EPS) and bull case fair value of Rs 932 (27x FY26E EPS) over the next 2-3 quarters.

Financial Summary:

Particulars (Rs cr)	Q4FY24	Q4FY23	YoY-%	Q3FY24	QoQ-%	FY23	FY24	FY25E	FY26E
Operating Income	196	158	23.9	179	9.4	656	724	807	908
EBITDA	22	15	45.0	15	42.2	53	66	77	89
APAT	20	14	43.7	12	69.0	48	59	68	78
Diluted EPS (Rs)	9.0	6.3	43.7	5.3	69.0	21.3	26.2	30.2	34.5
RoE-%						9.1	10.0	10.6	11.3
P/E (x)						37.2	30.2	26.2	23.0
EV/EBITDA						30.6	24.0	20.5	17.3

Q4FY24 Result Update

INEL posted strong results with 24% YoY topline growth in Q4FY24 to Rs 196cr outpacing industry growth. EBITDA for the quarter grew by 45% YoY to Rs 22cr while EBITDA margin expanded 160bps to 11%. Adj. PAT grew by 44% YoY to Rs 20cr and PAT margin expanded 144bps to 10.4%. Working capital days reduced from 57 to 42 days in FY24.

INEL is diversifying into products for commercial vehicles and off-highway segment. It has added one off-highway customer for export market in FY24. It is also looking to expand its capacities for future growth.

Key Triggers

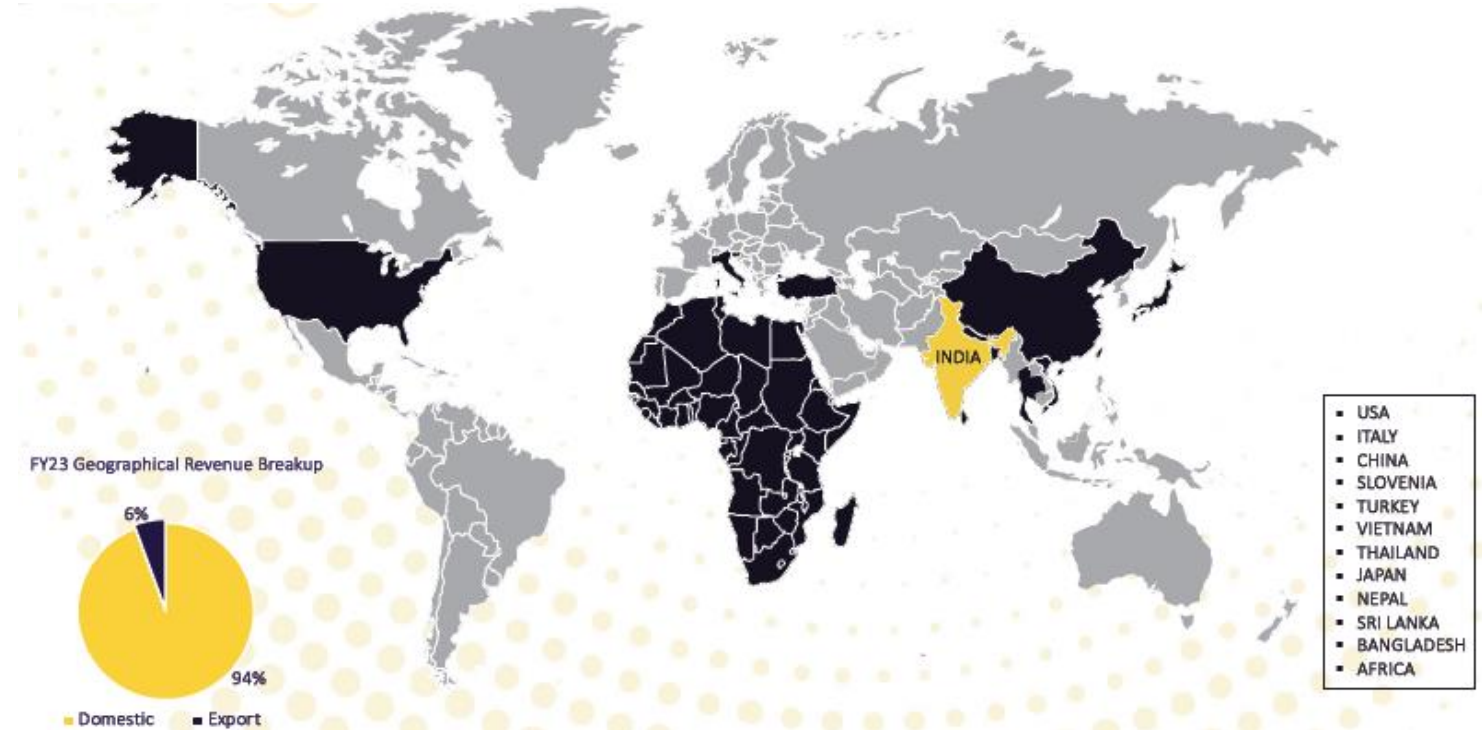
2W sales volume expected to remain robust in FY25

Sales of 2W are on a recovery path and the growth is expected to remain robust in FY25 after falling to seven-year low of 15.9mn units in FY23. 2W sales rose by 10% YoY to 1.6 million units in May'24 due to improved supply and the increasing demand for entry level models. Positive market sentiments, bolstered by stable fuel prices, a favourable monsoon outlook, festive demand and the marriage season, contributed to this rise. Several senior industry executives said normal monsoons, better agricultural output, higher minimum support prices for farm commodities and availability of water for irrigation because of healthy reservoir levels would help increase the disposable income, and further improve the consumer sentiment, in rural India. ICRA estimates 2W volumes to grow by 7-10% YoY in FY25 even as dealer inventory remains at controlled levels. INEL is a Tier 1 supplier to OEMs. Its market share for key customers has risen from 33% in FY19 to 41% in FY23.

Expanding into new geographies

INEL has developed off-highway solutions for North American OEMs, the results of which will be visible in the coming years. It is looking to venture into newer geographies and has assembled a dedicated marketing team specifically tasked with overseeing export developments. It has also entered the Sri Lankan market which opens up new avenues for growth. Currently exports account for ~6% of revenue.

Geographical presence



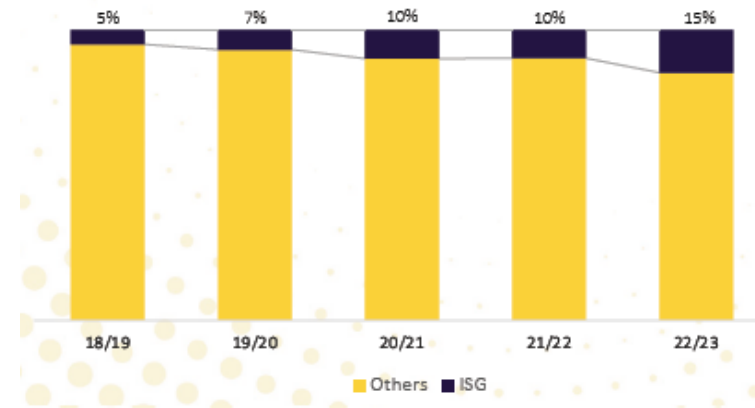
(Source: Company, HDFC sec)

Growing product portfolio

INEL is actively pursuing expansion into the realm of other segments of the automotive market, marking a significant diversification in its product portfolio. With the share of EV 2W/3W increasing, it is developing a comprehensive product base tailored specifically for EVs. Furthermore, it is also looking to target other industries and reduce dependence on automotive industry. INEL has developed 1) an EFI ECU for two-wheeler applications which is ready for production; 2) ISG (Integrated starter generator) controller to eliminate starter motor and EV motor controller 3) sensors for tyre pressure monitoring systems, reverse parking and speed sensors.

Additionally, it is working on safety-critical steering angle sensors and mid-range pressure sensors. Other products include low-pressure sensors, oil-level sensors, side-stand sensors, and TMAP sensors. ISG Systems share in sales has been rising over the years and stood at 15% in FY23. It has also added an off highway customer for exports in FY24. It has also diversified into commercial vehicles.

ISG system share

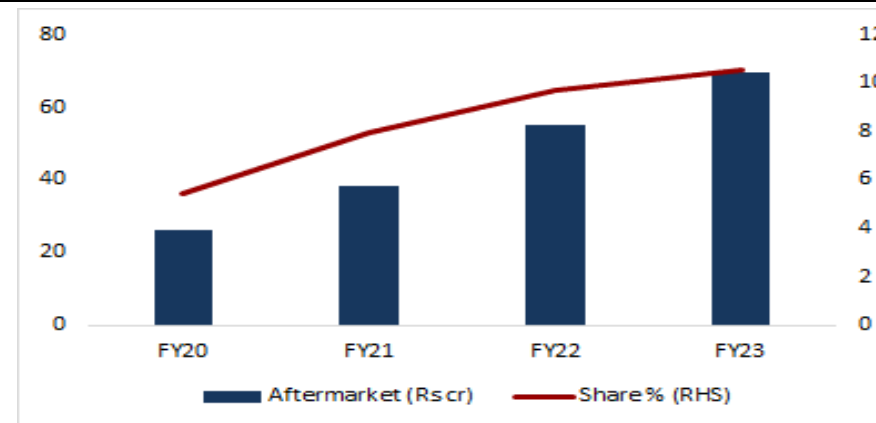


(Source: Company, HDFC sec)

Growing share of Aftermarket business

INEL has identified the Aftermarket business with strong growth potential and is working towards increasing its share in the overall revenue pie. It has a dedicated team working to implement various strategic measures that strengthen its product range and distribution network. Currently, Aftermarket sales contribute to ~10% of overall sales (growing @24% CAGR over FY20-23) and the management intends to reach 15% levels by FY25.

Increasing share of Aftermarket sales



(Source: Company, HDFC sec)

Encouraging financial parameters

Over the years, INEL has demonstrated strong growth, and remained ahead of industry growth by expanding its product portfolio and geographic reach. The company has remained debt free generating healthy operating cash flows. Average dividend payout has been over 30%. The increasing share of margin accretive replacement market and new product launches for EV is likely to drive higher operating margin in the coming years. We expect margins to expand from 9.2% to 9.8% over FY24-FY26. As of FY24, INEL was net debt free with cash and investments of ~Rs 450cr (~25% of market cap). INEL also managed to reduce the working capital days from 57 to 42 days in FY24.

Risks & Concerns

High dependence on the 2W segment

INEL is highly dependent on the two-wheeler industry with ~85% of revenues coming from this segment. Its long standing relationship with OEMs and strong presence in replacement market mitigates the risk to an extent.

Dependent on economic growth in the country

The automotive sector is directly dependent on the general economic conditions in both Indian and in other key global markets. Prolonged slowdown could impact revenue and profit growth of the company.

Obsolescence of key products

Some of the key products of the company like flywheel magneto, stator, rotor, etc. are not required in EV. Rapid adoption of EV in 2W could render them obsolete and impact revenue growth. INEL is developing new products for EV which should aid in topline growth. Also the anticipated EV penetration of only 16% of new vehicle sales by FY26 mitigate the risk to an extent.

High commodity prices

Sustained high level of commodity prices can have an adverse impact of the operating performance of the company. Moderate pricing power with OEMs due to the stiff competition and volatility in commodity prices exposes the profit margins to volatility. However, the price pass through with negotiation mitigates the risk to an extent.

Forex fluctuations

INEL exports about 6% of its sales and is looking to expand into newer geographies. Any sharp fluctuations in USD/Euro rates vis-à-vis INR could impact its revenue and margins.

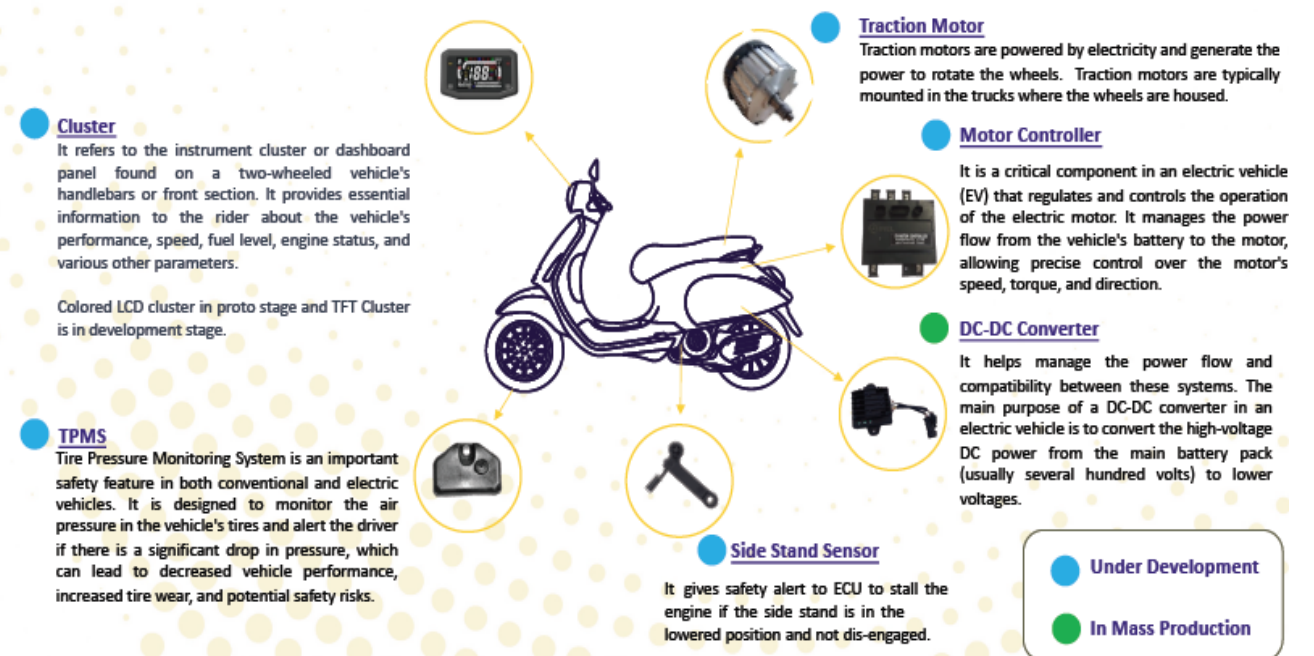
Company Background

INEL was incorporated in 1984 and converted into a joint venture in 1986 between Lucas Indian Service Ltd., a wholly-owned subsidiary of Lucas-TVS Ltd. and MAHLE Electric Drives Japan Corporation, Japan – a company of MAHLE Group, Germany, to manufacture Electronic Ignition Systems for two-wheelers, three wheelers and portable engines. The company specializes in manufacturing mechatronic products primarily for the automotive sector. Over the years the company has enlarged its customer base and now supplies to most of the manufacturers of two-wheelers, three wheelers and gensets. Lucas-TVS Group increased their holding in the company to 50.8% in FY22 and 70.3% in Q1FY24 by buying the stake of MAHLE Group making it a subsidiary of the company.

INEL is looking to expand its product portfolio by developing a comprehensive product base tailored specifically for electric vehicles (EVs). Its manufacturing units are located in strategic locations, specifically Tamil Nadu, Puducherry, and Haryana. The company is further looking at increasing capacities across these three facilities.

Key clientele

EV product developments



(Source: Company, HDFC sec)

Financials

Income Statement

(Rs cr)	FY22	FY23	FY24	FY25E	FY26E
Net Revenues	566	656	724	807	908
Growth (%)	17.7	15.9	10.3	11.5	12.5
Operating Expenses	517	603	658	731	819
EBITDA	50	53	66	77	89
Growth (%)	9.3	6.7	25.5	15.5	16.1
EBITDA Margin (%)	8.8	8.1	9.2	9.5	9.8
Depreciation	13	15	15	17	18
Other Income	25	23	25	28	30
EBIT	62	61	76	88	101
Interest expenses	0	0	0	1	1
PBT	62	60	76	88	101
Tax	11	12	16	20	23
PAT	50	48	59	68	78
Growth (%)	26.7	-4.0	23.0	15.3	14.1
EPS	22.2	21.3	26.2	30.2	34.5

Balance Sheet

As at March (Rs cr)	FY22	FY23	FY24	FY25E	FY26E
SOURCE OF FUNDS					
Share Capital	11	11	11	11	11
Reserves & Surplus	494	549	612	654	702
Shareholders' Funds	505	560	623	665	713
Total Debt	0	0	0	0	0
Net Deferred Taxes	22	30	38	38	38
Other Non-curr. Liab.	3	3	2	2	3
Total Sources of Funds	530	593	663	705	753
APPLICATION OF FUNDS					
Net Block & Goodwill	130	134	143	158	169
CWIP	5	13	13	7	3
Investments	278	355	432	452	477
Other Non-Curr. Assets	7	2	2	2	3
Total Non-Current Assets	420	504	590	619	651
Inventories	50	56	69	72	82
Debtors	118	119	142	158	174
Cash & Equivalents	37	23	19	15	22
Other Current Assets	17	15	17	20	22
Total Current Assets	221	213	247	266	299
Creditors	90	96	138	144	156
Other Current Liab & Provisions	21	29	36	35	42
Total Current Liabilities	111	125	174	179	197
Net Current Assets	110	89	73	87	102
Total Application of Funds	530	593	663	705	753

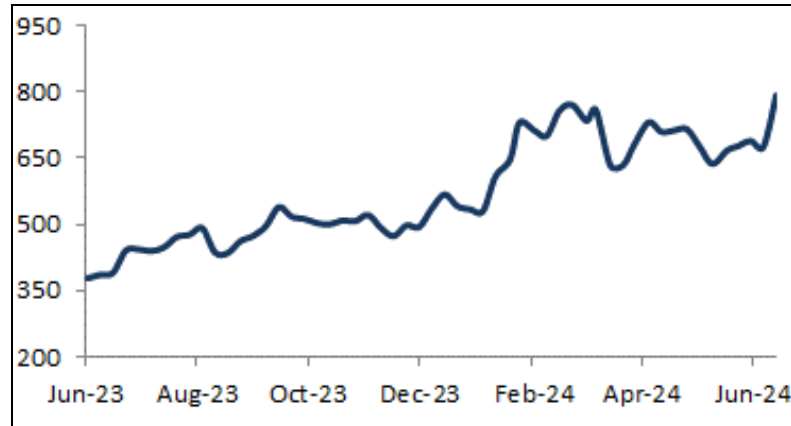
Cash Flow Statement

(Rs cr)	FY22	FY23	FY24	FY25E	FY26E
PBT	62	60	59	88	101
Non-operating & EO items	-22	-16	-6	0	0
Interest Expenses	-2	-2	-1	1	1
Depreciation	13	15	15	17	18
Working Capital Change	-34	11	11	-18	-8
Tax Paid	-9	-11	-16	-20	-23
OPERATING CASH FLOW (a)	7	57	63	68	88
Capex	-3	-25	-24	-25	-25
Free Cash Flow	4	32	39	43	63
Investments	12	-28	-22	-20	-25
Non-operating income	20	7	8	0	0
INVESTING CASH FLOW (b)	28	-46	-39	-45	-50
Debt Issuance / (Repaid)	0	0	0	0	0
Interest Expenses	0	0	0	-1	-1
FCFE	35	11	24	22	37
Share Capital Issuance	0	0	0	0	0
Dividend	-14	-21	-23	-26	-31
Others	-1	-1	-1	0	0
FINANCING CASH FLOW (c)	-15	-21	-24	-27	-31
NET CASH FLOW (a+b+c)	21	-10	1	-4	7

Key Ratios

	FY22	FY23	FY24	FY25E	FY26E
Profitability Ratios (%)					
EBITDA Margin	8.8	8.1	9.2	9.5	9.8
EBIT Margin	11.0	9.3	10.5	10.9	11.2
APAT Margin	8.9	7.3	8.2	8.5	8.6
RoE	10.5	9.1	10.0	10.6	11.3
RoCE	13.0	11.4	12.9	13.7	14.7
Solvency Ratio (x)					
Net Debt/EBITDA	-0.7	-0.4	-0.3	-0.2	-0.2
Net D/E	-0.1	0.0	0.0	0.0	0.0
PER SHARE DATA (Rs)					
EPS	22.2	21.3	26.2	30.2	34.5
CEPS	27.9	27.8	32.9	37.6	42.3
BV	223.3	247.7	275.5	294.1	315.1
Dividend	6.3	9.3	10.3	11.6	13.5
Turnover Ratios (days)					
Inventory days	73	66	66	68	67
Debtor days	30	29	32	32	31
Creditors days	59	52	59	64	60
VALUATION (x)					
P/E	35.7	37.2	30.2	26.2	23.0
P/BV	3.5	3.2	2.9	2.7	2.5
EV/EBITDA	32.7	30.6	24.0	20.5	17.3
EV/Revenues	2.9	2.5	2.2	2.0	1.7
Dividend Yield (%)	0.8	1.2	1.3	1.5	1.7
Dividend Payout (%)	28.1	43.4	39.1	38.4	39.1

Price chart



HDFC Sec Retail Research Rating description

Green Rating stocks

This rating is given to stocks that represent large and established business having track record of decades and good reputation in the industry. They are industry leaders or have significant market share. They have multiple streams of cash flows and/or strong balance sheet to withstand downturn in economic cycle. These stocks offer moderate returns and at the same time are unlikely to suffer severe drawdown in their stock prices. These stocks can be kept as a part of long term portfolio holding, if so desired. These stocks offer low risk and lower reward and are suitable for beginners. They offer stability to the portfolio.

Yellow Rating stocks

This rating is given to stocks that have strong balance sheet and are from relatively stable industries which are likely to remain relevant for long time and unlikely to be affected much by economic or technological disruptions. These stocks have emerged stronger over time but are yet to reach the level of green rating stocks. They offer medium risk, medium return opportunities. Some of these have the potential to attain green rating over time.

Red Rating stocks

This rating is given to emerging companies which are riskier than their established peers. Their share price tends to be volatile though they offer high growth potential. They are susceptible to severe downturn in their industry or in overall economy. Management of these companies need to prove their mettle in handling cyclicity of their business. If they are successful in navigating challenges, the market rewards their shareholders with handsome gains; otherwise their stock prices can take a severe beating. Overall these stocks offer high risk high return opportunities.

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