

Visit Note

Subros Ltd (SUBR IN)

March 16th, 2011

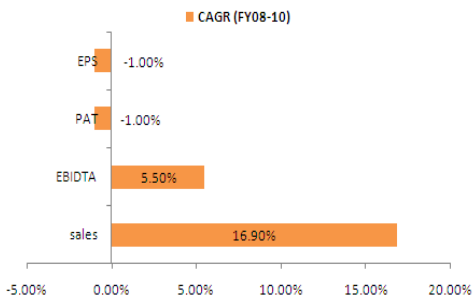
Industry

Auto Ancillary

Betting on market leadership

Not rated (CMP: ₹31)

Market Cap ₹ 1,860mn; USD 41.3mn

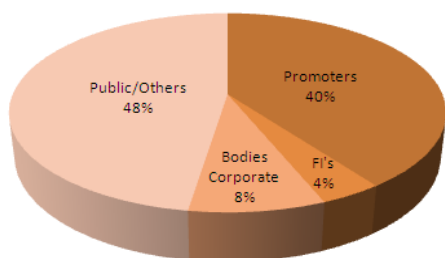


Market Data

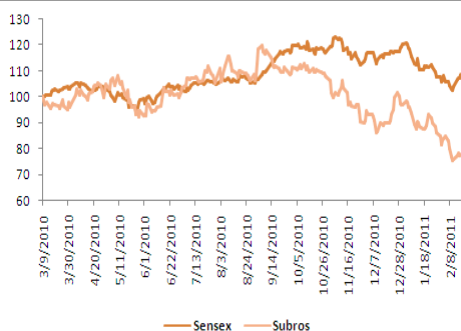
Market Cap.	₹1860 mn/USD 41.3 mn
Share Cap. (₹ mn)	120
52 Wk High/Low	56/31
Avg. Vol. (Weekly)	5650

Shareholding Pattern

(As on 31st March 2011) (%)



(Price Performance (RIC: SUBR.BO, BB: SUBR IN))



Financials (₹ Mn)	FY08	FY09	FY10
Net Sales	6638	6960	9066
EBITDA	845	647	940
PAT	286	134	281
EBITDA Margin	12.7%	9.3%	10.4%
PAT Margin	4.3%	1.9%	3.1%
EPS	4.8	2.2	4.7
P/E	6.5	13.9	6.6
EV/EBITDA	3.4	4.8	3.5
P/BV	1.1	1.0	0.9

We met the management of Subros Ltd. The company manufactures auto airconditioners and enjoys a leadership position in the auto airconditioning segment. Subros provides customized airconditioner kits to its OEM clients. Denso Corp (its vendor) and Suzuki (its customer) hold 13% stake each in Subros Ltd.

Considering its niche business segment (demand for customized products), technological support from Denso corp (Japan) and its long term association with Martuti Suzuki, we build up a positive view on Subros Ltd. Subros is targeting an ambitious 50% jump in its capacities to 1.5mn units by FY12E and is further doubling it to 3mn units by FY14E. Further, Subros is also continuously endeavouring to improve its EBITDA margin via innovation, increasing localization and reducing wastage. Volume growth coupled with EBITDA margin expansion should help Subros to report sustainable earnings growth in the future. At CMP of ₹31/share, the stock trades at 7.6x FY11E EPS of ₹ 4.1/share and 6.0- 5.2x FY12E-13E EPS of ₹ 5.2-6/share.

Largest auto airconditioner manufacturer, enjoys 40% market share

With 40% market share, Subros enjoys a leadership position in the auto air conditioner segment. Air conditioned cars constitute ~90% of the total passenger car segment. Due to the expected healthy growth in the passenger car segment, we believe that a large addressable market is available for Subros to expand its business.

Geographical diversification aimed at addressing client concentration concerns

With three existing plants at Noida, Manesar and Pune, Subros is catering mainly to MSIL (its key customer), M&M and TML. Subros generates ~70 % of its revenues from MSIL and 20% of its revenues from Tata Motors and M&M combined. In order to expand its customer base and business, Subros is setting up an assembly unit at Sanand (to supply Nano) and at Chennai (to supply to south based OEMs).

Targeting three-fold increase in manufacturing capacities by FY14E

The total manufacturing capacity of Subros is 1 mn (FY10) airconditioner kits , which is likely to reach to 1.25 mn by the end of FY11E. In FY10 it sold 7.47 lakh units of airconditioner kits and is currently running at its full capacity. Subros has lined up massive expansion plans to grab the growth in rising auto airconditioner market. It is increasing its manufacturing capacity from 1 Mn kits (FY10) to 1.5 mn kits by the end of FY12E and further to 3 mn kits by FY14E. The capex would be funded by a mix of debt and internal accruals.

Volume growth, margin expansion to drive future earnings growth

Subros expects revenues of ₹ 12bn by FY12E and ₹ 25 bn by FY15E, boosted by expansion of its manufacturing facilities. Subros has been facing pressure on its EBITDA margin due to appreciation of Yen, given ~50% of its raw material is Yen denominated. However, increase in localization and anticipated depreciation of Yen in the near-term augur well for margin expansion. Our back-of-the-envelope calculations indicate an EPS of ₹ 4.1/share in F11E and ₹ 5.2/share in FY12E and ₹ 6.0/share in FY13E. Subros is inexpensive at just 6.0-5.2x FY12E-13E EPS and 0.8x FY11E book value of ₹ 38. Volume growth + margin expansion should result in improvement in its RoE to 12.9% in FY12E and 13.4% in FY13E from 11.2% in FY11E.

Abhishek Gaoshinde

abhishekg@systematixshares.com

(+91 22 3029 8292)

Capacity expansion in line with increase in demand

In India, The demand for passenger cars has witnessed a secular growth, largely tracking the Indian GDP growth. The Indian passenger car segment witnessed a 18.3% CAGR over FY08-10 and is expected to grow by 20.9% CAGR over FY10-12E. According to industry sources, airconditioned cars accounts for 90% of the total passenger car segment. This indicates a total market of airconditioned cars is likely to reach to 2.8 mn units from 1.9 mn units in FY10. This large market offers a huge addressable market for airconditioner kits. Assuming, Subros will maintain its 40% market share in auto airconditioning market, it will require a capacity of more than 1.1 mn units in FY12E. The management indicates that it would enhance its manufacturing capacity from 1mn units to 1.25 mn units by the end of FY11E and further to 1.5 mn in FY12E in first phase of expansion, in line with the rising demand of its airconditioner kits.

Table 1: Demand of auto air-conditioner kits

(Mn)	FY06	FY07	FY08	FY09	FY10	FY11E	FY12E	CAGR (FY08-10)	CAGR (FY10-12)
Total passenger car segment	1.1	1.4	1.5	1.7	2.1	2.6	3.1	18.3%	20.9%
AC cars (assumed 90% of total market)	1.0	1.2	1.4	1.5	1.9	2.4	2.8	18.3%	20.9%
Subros volumes	0.4	0.5	0.5	0.6	0.7	0.9	1.1	21.6%	22.1%
Subros Market share	39.0%	38.5%	37.1%	41.4%	39.2%	40%	40%		

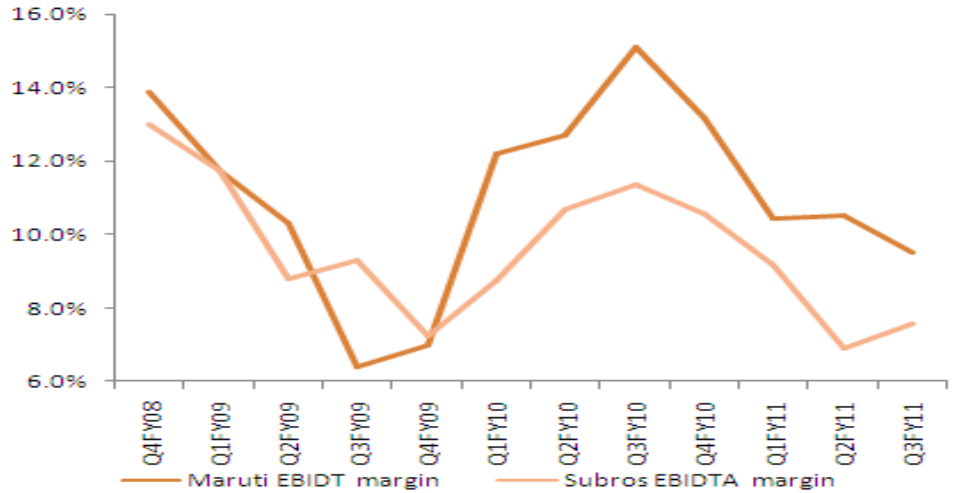
Source: SIAM, Company, Systematix Institutional Research

Focus on EBIDTA margin expansion via localization

While Subros has scheduled a huge capex to fuel growth to its revenue, it is also taking suitable steps internally to improve its EBIDTA margin. Subros has been facing pressure on its EBIDTA margin due to appreciation of Yen, given ~50% of its raw material is Yen denominated. Hence Subros is continuously endeavouring to improve its EBIDTA margin via innovation, increasing localization and reducing wastage. In Q3FY11, its EBIDTA margin contracted by 379bps YoY to 7.6% (due to appreciation of Yen). However going forward, the management expects to report better results in Q4FY11 compared to Q3FY11, because of an increase in localization and expectation of higher volumes. For eg: it has started procuring RS evaporator from domestic market, which would result in an average saving of ₹400/Kit on a monthly order of average 60,000 such kits. This works out to a saving of ₹ 72 mn (3.5% of RM cost in Q3FY10) per quarter. Also, Subros expects to pass on the adverse impact of yen appreciation on Q3FY11 earnings to its OEM customers in Q4. Consequently, its Q4 EBIDTA margins are likely to be better on a QoQ basis.

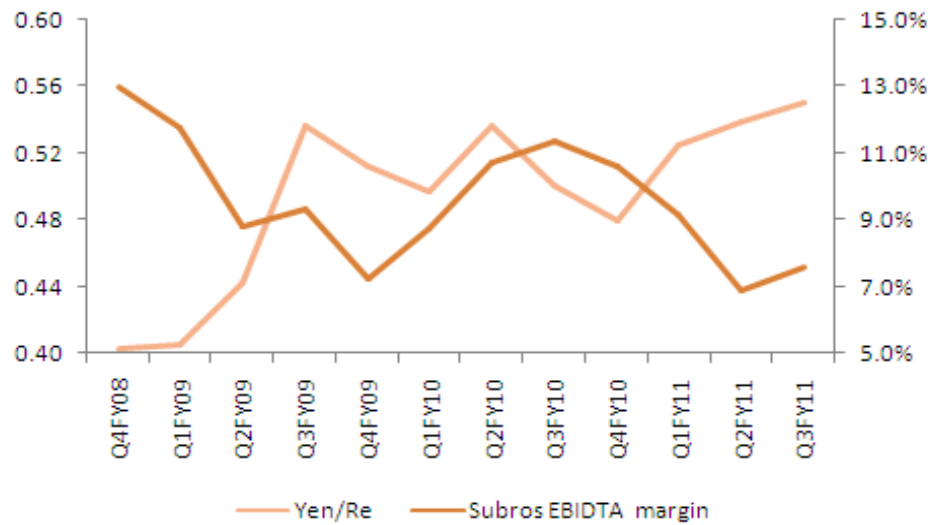
Further, given the strong historical correlation between EBIDTA margins of Subros and its key OEM customer i.e. Maruti, the uptick is expected in Maruti's EBIDTA margins in FY12E is likely to augur well Subros as well.

Chart 1: Subros EBIDTA margin v/s Maruti EBIDTA margin



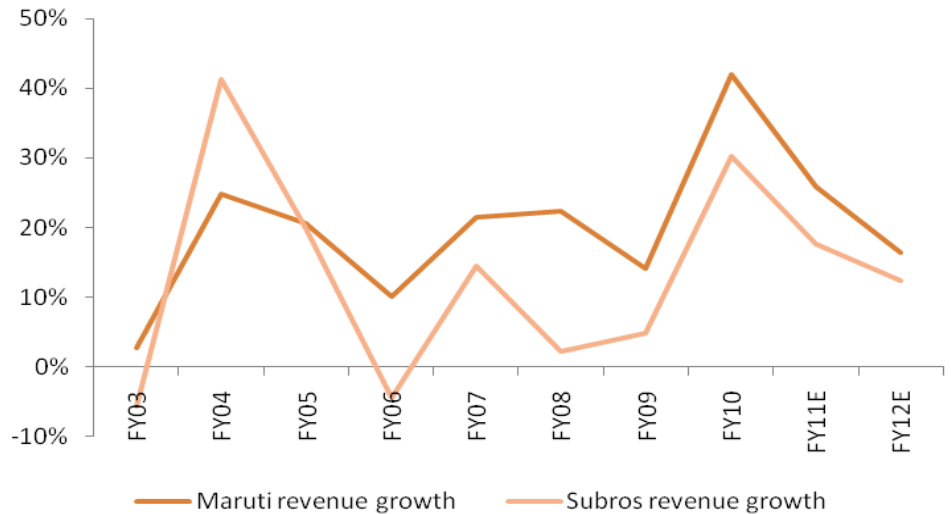
Source: Systematix Institutional Research

Chart 2: Subros EBIDTA margin v/s Yen /Re movement



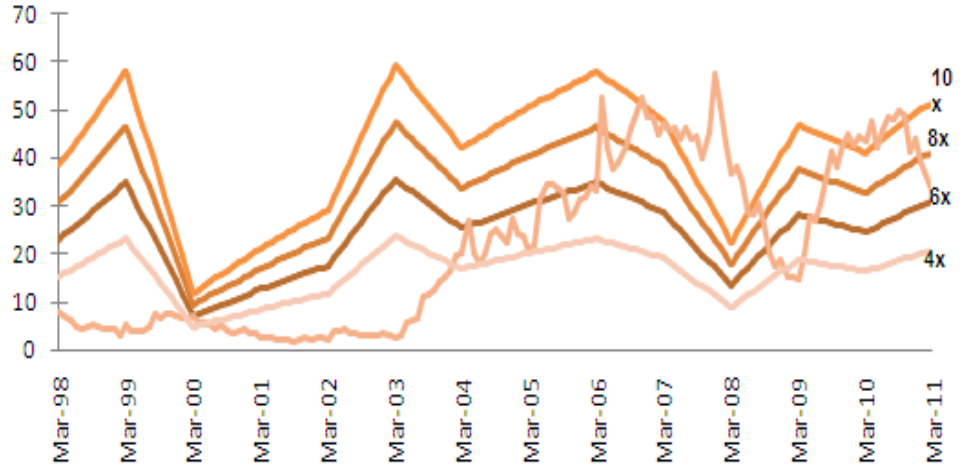
Source: Systematix Institutional Research

Chart 3: Subros revenue growth v/s Maruti revenue growth



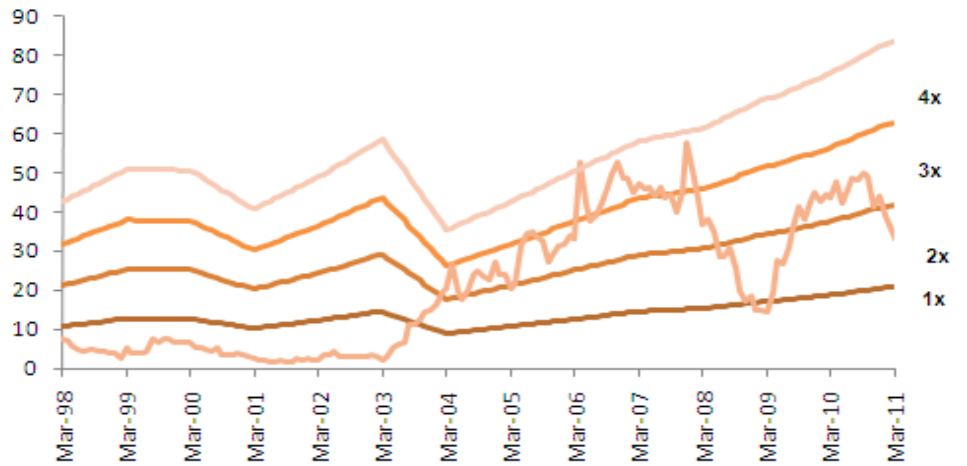
Source: Systematix Institutional Research

Chart 3: Subros P/E band



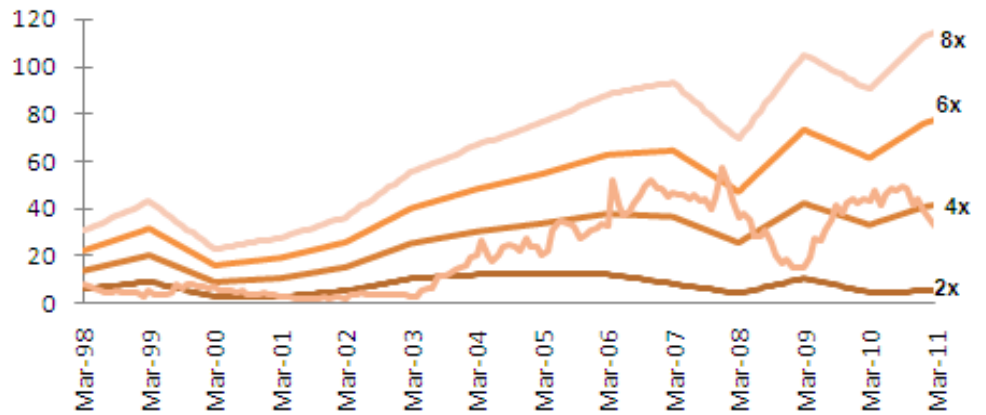
Source: Systematix Institutional Research

Chart 4: Subros P/B band



Source: Systematix Institutional Research

Chart 5: Subros EV/EBIDTA band



Source: Systematix Institutional Research

Table 2: Global peer group comparison

	Denso		Sanden		Subros		Average	
	FY11E	FY12E	FY11E	FY12E	FY11E	FY12E	FY11E	FY12E
P/E (x)	14.2	12.5	6.48	6.01	8.1	6.4	9.6	8.3
P/B (x)	1.1	1.0	0.97	0.83	0.9	0.8	1.0	0.9
EV/EBIDTA (x)	4.7	4.4	NA	NA	4.7	4.1	NA	NA
ROE (%)	7.5	8.0	3.3	4.24	11.2	12.9	7.3	8.4
Dividend yield (%)	1.7	2.0	1.59	1.59	2.1	2.1	1.8	1.9

Source: Bloomberg and Systematix Institutional Research

Promoter Background

Mr. Ramesh Suri

Ramesh Suri, B. Sc. serves as the Managing Director of Rohan Motors Limited.. Mr. Suri served as Managing Director of Subros until May 12, 2008. He serves as a Chairman of Subros since May 2008. He has been a Director of Sona Koyo Steering Systems Ltd., since October 23, 2006. Mr. Suri has been a Director of Bharat Hotels Limited since January 22, 1989. Mr. Suri also serves as the Director of Prima Telecom Limited, Prime Cellular Limited, Udaipur Hotels Limited, Jyoti Limited, Fibcom India Limited, GlobalAutotech Limited, Premium Exports Limited, Deeksha Holding Limited, Premium Farm Fresh Produce Limited, Apollo Zipper India Limited, Jyotsna Holding Pvt. Limited, Responsible Builders Pvt. Ltd., SHSTransport Pvt. Ltd., Tempo Automobiles Pvt. Ltd., Hemkunt Service Station Pvt. Ltd., Tempo Finance (North) Pvt. Ltd., R.R. Holdings Pvt. Ltd., Special Protection Services Pvt. Ltd., Bee Pee Motors Pvt. Ltd., Rohan Auto Sales Pvt. Ltd., Teriot Steels Pvt. Ltd., Sawalka Autotech Pvt. Ltd., Mercantile Capital 6t Financial Services Pvt.Ltd., Trishul Leasing Pvt. Ltd. and Ambros Motors Pvt. Ltd.

Company background

Subros was established in 1985 as a joint venture between the Suri Brothers, Denso Corporation, Japan and Suzuki Motor Corporation, Japan. The company has grown from a capacity of 15,000 AC units in 1985 comprising of largely an assembly operation, into the largest and the only integrated manufacturing unit in India for Auto Air Conditioning systems. The company has the capability to manufacture compressors, condensers, heat exchangers and all the connecting elements that are required to complete the AC Loop. Subros has three plants in Noida, one in Manesar and one in Pune. It also has a R&D centre and Tool room in Noida.

Shareholding more than 1% of the Total no. of shares

Table 3:

Name of the Shareholder	No. of Shares	Shares as % of Total No. of Shares
Deeksha Holding Ltd	10075810	16.8
Denso Corporation	7800000	13
Jyotsna Holding Pvt Ltd	3440000	5.73
Jyotsna Suri	1611200	2.69
R R Holding Pvt Ltd	3200000	5.33
Ramesh Suri	1407840	2.35
Ramesh Suri HUF	3040000	5.07
Ritu Suri	1120000	1.87
Suzuki Motors Corporation	7800000	13
Total - Public Shareholding	15600000	26
Total - Shareholding of Promoter and Promoter Group	24000000	40.01

Source: Systematix Institutional Research

Table 4: Dividend payment history

Year End	Dividend Amount	Dividend %	Dividend Yield %	Dividend per Share(Rs)	Face Value(₹)
Mar-1998	1.50	25.00	3.21	2.50	10.00
Mar-1999	1.50	25.00	4.74	2.50	10.00
Mar-2000	1.50	25.00	3.65	2.50	10.00
Mar-2001	0.90	15.00	5.48	1.50	10.00
Mar-2002	1.08	18.00	7.96	1.80	10.00
Mar-2003	1.32	22.00	8.89	2.20	10.00
Mar-2004	1.50	25.00	1.23	2.50	10.00
Mar-2005	3.60	30.00	2.91	3.00	10.00
Mar-2006	4.20	35.00	2.12	3.50	10.00
Mar-2007	4.80	40.00	1.70	4.00	10.00
Mar-2008	4.80	40.00	2.19	0.80	2.00
Mar-2009	3.00	25.00	3.39	0.50	2.00
Mar-2010	4.20	35.00	1.61	0.70	2.00

Source: Systematix Institutional Research

Quarterly trends

Table 5:

Quarterly Numbers (₹ mn)	Q3FY09	Q4FY09	Q1FY10	Q2FY10	Q3FY10	Q4FY10	Q1FY11	Q2FY11	Q3FY11
Net Sales & Other Operating Income	1361	2157	2099	2185	2285	2497	2343	2787	2738
Growth	-15.00%	14.90%	19.80%	29.80%	67.90%	15.80%	11.60%	27.60%	19.80%
(Increase) / Decrease In Stocks	-8	17	-16	9	-70	44	9	-23	-15
Cost of Services & Raw Materials	1,005	1,719	1,631	1,592	1,744	1,786	1,722	2,184	2,079
Other expenses	138	179	183	218	216	245	243	277	293
Employee Cost	100	86	118	133	136	158	154	156	172
Total Expenditure	1235	2001	1915	1951	2025	2233	2128	2595	2530
EBIDTA	127	156	184	234	260	264	215	192	208
Growth	-38.60%	-36.30%	-10.80%	58.00%	105.40%	69.60%	16.90%	-17.90%	-20.10%
EBIDTA %	9.30%	7.20%	8.70%	10.70%	11.40%	10.60%	9.20%	6.90%	7.60%
Depreciation	69	99	95	95	98	98	94.9	101.6	101.3
PBIT	58	57	89	139	162	166	120	90	107
Interest	46	49	46	43	38	34	37	43	40
Other Income	0	5	0	0	0	0	0	0	0
Exceptional Items									
PBT (after extraordinary)	12	13	43	96	124	131	82	47	66
Tax	4	5	10	29	37	41	11	-1	11
PAT	8	8	33	67	88	90	71	49	55
EPS	0.1	0.1	0.5	1.1	1.5	1.5	1.2	0.8	0.9

Source: Systematix Institutional Research

FINANCIAL DETAILS

Profit & Loss				
Statement (₹ mn)	Mar-07	Mar-08	Mar-09	Mar-10
Net Sales	6484	6638	6960	9066
Growth (%)	14.4%	2.4%	4.8%	30.3%
Expenditure	5,729	5,793	6,312	8,126
Materials Consumed	4,586	4,551	5,163	6,719
Employee Cost	382	462	442	538
Other Exp	761	780	708	869
EBITDA	755	845	647	940
Growth (%)	20%	12%	-23%	45%
EBITDA margin (%)	11.6%	12.7%	9.3%	10.4%
Depreciation	275	325	316	385
EBIT	480	520	332	555
Interest expenses	80	109	146	160
Other Income	0	0	0	0
E/O items				
PBT	400	411	186	395
Tax	122	125	52	115
Effective tax rate (%)	30.5%	30.4%	28.0%	29.1%
Reported PAT	278	286	134	280
Growth (%)	12%	3%	-53%	109%
Net Margin (%)	4.3%	4.3%	1.9%	3.1%

Balance Sheet (₹ mn)				
	Mar-07	Mar-08	Mar-09	Mar-10
Equity share capital	120	120	120	120
Reserves & surplus	1390	1620	1720	1951
Net worth	1510	1740	1839	2071
Secured Loans	961	810	1050	1182
Unsecured Loans	300	300	300	359
Loan Funds	1261	1110	1350	1541
Net deferred tax liability	88	75	117	112
Total Liabilities	2860	2926	3306	3724
Gross Block	3,314	3,631	4,363	4,828
Less: Depreciation	1,665	1,941	2,176	2,563
Net block	1,649	1,690	2,187	2,265
Capital work in progress	226	397	382	692
Investment	0	0	4	4
Current Assets	1,615	1,507	1,817	1,935
Inventories	991	925	855	982
Sundry debtors	281	254	557	476
Cash & bank balance	77	75	113	128
Loans & advances	267	253	292	350
Current lia & Prov	631	668	1,085	1,172
Current liabilities	561	575	1,026	1,097
Provisions	71	92	59	74
Net current assets	984	839	732	763
Misc. exp	0	0	0	0
Total Assets	2,860	2,926	3,305	3,724

Profitability (%)				
	Mar-07	Mar-08	Mar-09	Mar-10
EBITDA Margin	11.6	12.7	9.3	10.4
Net Margin	4.3	4.3	1.9	3.1
ROCE	19.1	18.0	10.6	15.8
ROE	19.9	17.6	7.5	14.3
Per Share Data (₹)				
	Mar-07	Mar-08	Mar-09	Mar-10
DEPS	4.6	4.8	2.2	4.7
DBVPS	25.2	29.0	30.7	34.5
DDPS	0.8	0.8	0.5	0.7
Valuations (x)				
	Mar-07	Mar-08	Mar-09	Mar-10
PER	6.7	6.5	13.9	6.6
P/BV	1.2	1.1	1.0	0.9
EV / Sales	0.5	0.4	0.4	0.4
EV / EBITDA	4.0	3.4	4.8	3.5
Dividend Yield (%)	1.5	1.5	1.0	1.4
Gearing Ratio (x)				
	Mar-07	Mar-08	Mar-09	Mar-10
Net Debt/ Equity	0.8	0.6	0.7	0.7
Net Debt/EBITDA	1.6	1.2	1.9	1.5
Working Cap Cycle (days)	36	28	17	12

Cash Flow				
Statement (₹mn)	Mar-07	Mar-08	Mar-09	Mar-10
PBT	400	411	186	395
Depreciation	275	325	316	385
Interest Provided	80	109	146	160
Other Non-Cash items	28	(13)	57	(18)
Chg in working cap	(189)	144	145	(17)
Tax paid	(122)	(125)	(52)	(115)
Operating Cashflow	472	851	798	791
Capital expenditure	(781)	(488)	(717)	(775)
Others	1	(48)	(81)	3
Investments	0	0	4	0
Investing Cashflow	(780)	(536)	(798)	(772)
Equity Capital Raised	0	0	0	0
Loans Taken / (Repaid)	441	(151)	240	191
Interest Paid	(80)	(109)	(146)	(160)
Dividend paid (incl tax)	(48.0)	(48.0)	(30.0)	(42.0)
Income from investments	(8.2)	(8.2)	(5.1)	(6.9)
Others	9	(1)	(21)	14
Financing Cashflow	314	(317)	38	(4)
Net chg in cash	6	(2)	38	15
Others				
Opening cash position	71	77	75	113
Closing cash position	77	75	113	128

For any queries contact us at: Institutional Team

N. Subramaniam	Head of Sales Trading	+91- 22-3029 8285	nsubramaniam@systematixshares.com
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Equity Sales

Mamta Singh	AVP– Sales	+91-22-3029 8092	mamtasingh@systematixshares.com
Ridhim Thapar	AVP– Sales	+91-22-3029 8265	ridhimt@systematixshares.com

Derivatives

Raghvendra Kedia	VP – Sales (Derivatives)	+91- 22-3029 8091	rkeddia@systematixshares.com
Abhishek Karande	Technical Analyst	+ 91-22-3029 8261	abhishekk@systematixshares.com
Barath Krishnan	Derivatives Strategist	+ 91-22-3029 8249	barathk@systematixshares.com

Sales Trading / Dealing

Sachin Parekh	Sr. Manager	+ 91-22-3029 8291	sachinp@systematixshares.com
Jigar Kamdar	Sales Trader	+ 91-22-3029 8181	jigarkamdar@systematixshares.com
Vinod Bhuvad	Sales Trader	+ 91-22-3029 8267	vinodbhuvad@systematixshares.com
Vijayendra Devadiga	Trader	+ 91-22-3029 8268	vijayendrad@systematixshares.com
Nayan Narnoli	Derivatives Dealer	+ 91-22-3029 8180	nayan@systematixshares.com
Monish Lotia	Derivatives Dealer	+ 91-22-3029 8252	monishlotia@systematixshares.com

Equity Research

Telephone: + 91-22- 3029 8000

RESEARCH ANALYST	SECTOR ALLOCATION	DIRECT Nos.	E-mail
Sudarshan Narasimhan	Sr. VP & Head of Research –Oil & Gas, Petrochemicals	+ 91-22-3029 8293	sudarshan@systematixshares.com
Surya Narayan Patra	AVP - Pharma	+ 91-22-3029 8186	suryapatra@systematixshares.com
Vibhash Prakash Awasthi	AVP - Metals & Mining	+ 91-22-3029 8296	vawasthi@systematixshares.com
Madhu Babu	AVP - IT, Telecom	+ 91-22-3029 8258	madhu@systematixshares.com
Eric Martins	AVP – Metals & Mining, Pipes	+ 91-22-3029 8253	eric@systematixshares.com
Shreegopal Jaju	AVP – Capital Goods	+ 91-22-3029 8187	gopaljaju@systematixshares.com
Vishal Shah	AVP – Banking	+ 91-22-3029 8260	vishalshah@systematixshares.com
Binod Modi	Sr. Analyst – Cement & Construction	+ 91-22-3029 8264	binodmodi@systematixshares.com
Rohit Jain	Analyst - Real Estate	+ 91-22-3029 8269	rohitj@systematixshares.com
Reshma Bathija	Analyst – Oil & Gas, Petrochemicals	+ 91-22-3029 8294	reshmab@systematixshares.com
Abhishek Gaoshinde	Analyst - Automobile	+ 91-22-3029 8292	abhishekg@systematixshares.com
Samruddhi Trivedi	Associate	+ 91-22-3029 8263	samruddhit@systematixshares.com
Nikhil Soneta	Associate	+ 91-22-3029 8257	nikhils@systematixshares.com

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BUY (B)	The stock's total return is expected to exceed 20% over the next 12 months.
ACCUMULATE (A)	The stock's total return is expected to be within 10-20% over the next 12 months.
HOLD (H)	The stock's total return is expected to be within 0-10% over the next 12 months.
SELL (S)	The stock's is expected to give negative returns over the next 12 months.
NOT RATED (NR)	The analyst has no recommendation on the stock under review.

Industry Views

ATTRACTIVE (AT)	Fundamentals /Valuations of the sector is expected to be attractive over the next 12-18 months.
NEUTRAL (NL)	Fundamentals /Valuations of the sector are expected to neither improve nor deteriorate over the next 12-18 months.
CAUTIOUS (CS)	Fundamentals /Valuations of the sector is expected to deteriorate over the next 12-18 months.

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4. Systematix Shares & Stocks (I) Ltd., or its affiliates do not hold any paid up capital in the company

SYSTEMATIX SHARES & STOCKS (I) LTD.

Head Office J. K. Somani Building, 2nd Floor, British Hotel Lane,
Fort, Mumbai, Pin: 400001, Tel: +91 22 66198000, Fax: +91 22 66198029

Registered Office EGA Trade Center, 4th Floor, 809-, Poonamalle High Road,
Kilpauk, Chennai, Pin: 600010 Tel: +91 44 26612184/ 87/ 88 Fax: +91 44 26612190