

July 14, 2011

Reco	Previous Reco
Accumulate	Accumulate
CMP	Target Price
Rs231	Rs260
EPS change FY12E/13E (%)	NA
Target Price change (%)	NA
Nifty	5,585
Sensex	18,596

Price Performance

(%)	1M	3M	6M	12M
Absolute	(0)	8	28	55
Rel. to Nifty	(2)	11	35	50

Source: Bloomberg

Relative Price Chart



Source: Bloomberg

Stock Details

Sector	Auto Ancillaries
Bloomberg	MSS@IN
Equity Capital (Rs mn)	387
Face Value(Rs)	1
No of shares o/s (mn)	387
52 Week H/L	256/148
Market Cap (Rs bn/USD mn)	89/1,997
Daily Avg Volume (No of sh)	89491
Daily Avg Turnover (US\$mn)	0.5

Shareholding Pattern (%)

	Mar-11	Dec-10	Sep-10
Promoters	65.2	65.2	65.2
FII/NRI	10.2	9.4	8.2
Institutions	9.4	9.5	10.8
Private Corp	8.1	8.2	7.8
Public	7.0	7.7	7.9

Source: Capitaline

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- Peguform's (PF) acquisition appears a strategic fit in terms of product, clients and geography
- SWS' (25% equity in MSSL) resistance for 100% exposure in PF (non core business) could be the reason for 51:49 JV between MSSL and SMFL (parent of MSSL) to acquire PF
- Expect acquisition price to be ~Euro 235mn (3.5x CY10 EV/EVIDTA or 0.18x EV/Sales). SMR was acquired at 0.12x EV/Sales. Expect debt attributable to PF ~Euro150 to 200mn
- Acquisition can be EPS accretive from first year. Retain Accumulate rating

About Peguform Group

Peguform (PF) is a leading full service supplier of differentiated high quality plastic products. It is a leading player in bumper, vehicle exteriors and cockpits, dashboard and interior trims for automotive and related industries. It is among top 8 players globally in its segments. It has a strong presence in Europe and commands a significant share of business of German OEM's like Volkswagen, Audi, BMW etc.

PF had filed for bankruptcy in Oct 2002 and has changed hands five times since then. Cerebrus, private equity player, acquired the company from bankruptcy proceedings in 2005. Polytec group, a key player in plastic materials, natural fibre composites etc, acquired it from Cerebrus after 3 years in 2008. Thereafter, Pierer-Knünz Group took over its reins in 2009 which was finally overtaken by Cross Industries in Dec 2009.

About the deal

Motherson Sumi Systems Ltd. (MSSL) along with SMFL (parent of MSSL) will acquire 80% stake in PF through a SPV in which MSSL will hold 51% and balance will be held by SMFL. The balance 20% in PF will be retained by existing investor (Cross Industries). As PF holds 50% in Wethje Carbon Composite, MSSL and SMFL will also acquire stake in this company indirectly.

Why 51:49 JV for the deal??

It seems street is concerned with this JV arrangement. We believe that this could be due to resistance of Sumitomo Wiring Systems (SWS) who holds 25% in MSSL. SWS is a leader in wiring harnesses. Polymers do not fit in list of core focus area for SWS. This along with the size of the company (equivalent to MSSL consolidated) could be the reason why SWS would not have preferred to take 100% ownership in the company. It should be noted that the structure is similar to that of acquisition of SMR.

Valuations

YE-	Net	EBITDA		EPS	EPS	RoE		EV/		
Mar	Sales	(Core)	(%)	APAT	(Rs)	% chg	(%)	P/E	EBITDA	P/BV
FY10	69,022	6,104	8.8	2,696	7.2	28.8	24.1	32.1	14.9	7.4
FY11P	83,460	8,918	10.7	3,868	10.0	38.7	29.0	23.1	10.6	5.8
FY12E	102,774	10,943	10.6	5,142	13.1	31.4	30.4	17.6	8.5	4.9
FY13E	109,502	12,534	11.4	6,178	15.8	20.2	30.4	14.7	7.2	4.1

Complimentary product profile

PF is largely a plastic molding/polymer company. Its strength lies in creating new applications of plastics. We believe that the biggest advantage that Motherson (MSSL) has is access to technology. MSSL has identified Polymer products (current revenue ~ Euro 165mn) as one of the key growth drivers for its 2015 vision of USD 5bn turnover. However, currently MSSL lacks technological edge. PF provides access to latest technology and should help MSSL in accelerated growth and global ambitions.

Product profile

MSSL	Peguform
Wiring Harness, bumpers	Bumper systems and frontend modules
Cockpit modules, HVAC systems	Car body and outer skin components
Injection molded, blow molded, liquid Silicone rubber molded products	Cockpits and instrument panels, Interior Systems

Source: Company, Emkay Research

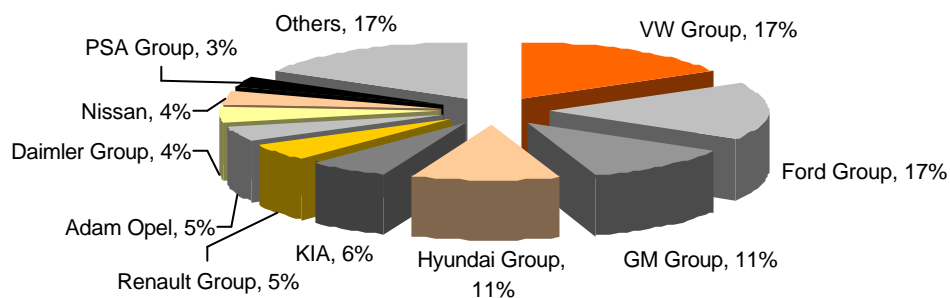
Market leadership	Comments
Bumper systems and front end modules	Market leader in painted bumpers in Germany and Spain
Car body and outer skin components	Market leader in complete car bodies

Source: Company, Emkay Research

Complimentary customer profile

PF also commands a premium clientele which derives strong synergy with existing clients of SMR. It should be noted that both PF and SMR have a strong presence in Europe. It receives ~2/3rd of its revenue from Volkswagen group and ~50% of Audi's requirement. Other notable clients include BMW, Porsche, Renault Nissan, Daimler and GM. There exists a synergy in garnering higher business from existing clients given SMR's client profile (see chart below).

Global customer profile for SMR



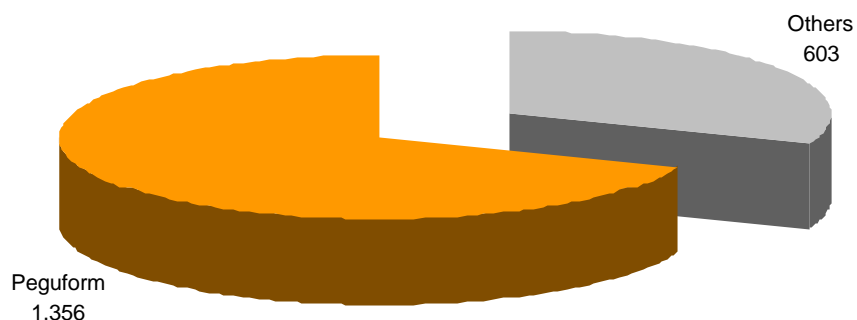
* for March 2009

Source: Company, Emkay Research

PF – the largest contributor to Cross Industries revenues

Peguform accounts for 69% of CI's revenue. PF was acquired in December 2009.

Cross Industries revenue break up (Euro mn CY10)



Source: Company, Emkay Research

PF margins – has been on an uptrend

PF has been reporting margins improvement since CY08. Its EBITDA margins increased from 3.5% in CY08 to 5% in CY10.

Peguform Group (Euro mn)	CY2008	CY2009	CY2010
Revenues	1435.7	1172	1335.5
EBITDA	49.7	49.1	66.9
EBITDA Margin	3.5	4.2	5.0
EBIT	-54.1	-1	21.8
EBIT Margin	-3.8	-0.1	1.6
Net Profit	-69.4	-21.4	

Source: Company, Emkay Research

Debt attributable PF – not more than Euro 200mn

We estimate PF's debt for CY10 by analyzing consolidated balance sheet financials of Cross Industries. We note that total consolidated long term debt in Cross Industries is Euro 641 mn in Dec 2010. Attributing Euro 200 mn debt to KTM (as per annual report 2010) and assuming Euro 275 mn debt for Cross Motorsports & others (increase in line with that of KTM), we estimate total debt for Peguform to be ~Euro 166mn in Dec 2010. If we assume flat debt levels of Euro 228mn, PF's debt amounts to Euro 214mn in CY10

Total Debt (Euro mn)	SY07	SY08	SY09	CY10
Cross Industries	333	290	394	641
KTM	143	35	166	200
Cross Motorsports & Others#	190	254	228	275
Peguform				166

SY indicates year ending September;

Assuming Euro 275mn debt in CY10 for Cross Motorsports; If we assume flat debt levels of Euro 228mn, Peguform debt amounts to Euro 214mn in CY10

Source: Company, Emkay Research

Acquisition can be EPS accretive from first year itself

The management has not yet disclosed the purchase price. We expect the valuation to be around 3.5x EV/EBIDTA (based on CY10 financials). This implies a EV of ~Euro 235 mn (0.18x CY10 EV/sales. These valuations are higher than that of acquiring SMR (Euro 80 mn EV for revenue of 660m or ~0.12x EV/Sales). Based on the above assumptions, we expect the acquisition to be earnings accretive in the first of year of acquisition (refer to table below).

Euro Mn	CY11E	CY11E	CY11E	Comments
Sales	1600	1600	1600	Target of the company
EBIDTA	64	80	96	
Margin	4%	5%	6%	Assumption
Depreciation	46	46	46	As per CY10
EBIT	18	34	50	
Interest	12	12	12	Euro 235 mn @ 5%
PBT	6.3	22.3	38.3	
Tax (30%)	2	7	11	Assumed at 30%
Net profit	4.4	15.6	26.8	
MI	0.9	3.1	5.4	
Profit for the group	3.5	12.5	21.4	
MSSL share (51%)	1.8	6.4	10.9	
Exchange rate	65	65	65	
Profit in Rs mn	116	413	710	
No of shares	392	392	392	
EPS (Rs)	0.3	1.1	1.8	
Current FY12 EPS (Rs)	13.5	13.5	13.5	
% existing EPS	2.2%	7.8%	13.4%	

Source: Emkay Research

Valuations and View

We retain our ACCUMUATE rating on the stock. We expect earnings upgrade to our FY13 EPS estimate of Rs 15.8 due to the acquisition of Peguform. At the current juncture, we are not incorporating PF due to limited information (acquisition price, turnaround plan, etc). At Rs 231 the stock trades at PER of 14.7x and EV/EBITDA of 7.2x our FY13 estimates.

Financials

Income Statement

Y/E, Mar (Rs. mn)	FY10	FY11P	FY12E	FY13E
Net Sales	69,022	83,460	102,774	109,502
<i>Growth (%)</i>				
Expenditure	62,918	74,542	91,832	96,968
Materials Consumed	41,659	51,454	63,405	67,537
Employee Cost	12,004	12,588	15,144	15,442
Other Exp	9,255	10,500	13,283	13,989
EBITDA	6,104	8,918	10,943	12,534
<i>Growth (%)</i>				
EBITDA margin (%)	8.8	10.7	10.6	11.4
Depreciation	2,601	2,465	2,844	3,123
EBIT	3,503	6,454	8,098	9,411
EBIT margin (%)	5.1	7.7	7.9	8.6
Other Income	812	378	465	550
Interest expenses	493	576	562	539
PBT	3,822	6,256	8,001	9,421
Tax	1,219	1,866	2,160	2,544
Effective tax rate (%)	31.9	29.8	27.0	27.0
Adjusted PAT	2,603	4,389	5,841	6,877
<i>Growth (%)</i>				
Net Margin (%)	3.8	5.3	5.7	6.3
(Profit)/loss from JV's/Ass/MI	(94)	521	699	699
Adj. PAT After JV's/Ass/MI	2,696	3,868	5,142	6,178
E/O items	268	(39)	0	0
Reported PAT	2,428	3,907	5,142	6,178
<i>Growth (%)</i>	37	60.9	31.6	20.2

Cash Flow

Y/E, Mar (Rs. mn)	FY10	FY11P	FY12E	FY13E
PBT (Ex -Other income)	3,010	5,878	7,536	8,871
Depreciation	2,601	2,465	2,844	3,123
Interest Provided	493	576	562	539
Other Non-Cash items	(503)			
Chg in working cap	(291)	(1,137)	(900)	(445)
Tax paid	(1,219)	(1,866)	(2,160)	(2,544)
Operating Cashflow	4,090	5,915	7,883	9,545
Capital expenditure	(3,780)	(6,192)	(4,000)	(4,000)
Free Cash Flow	310	(277)	3,883	5,545
Other income	812	418	465	550
Investments	(790)	0	0	0
Investing Cashflow	(3,758)	(5,774)	(3,535)	(3,450)
Equity Capital Raised		(0)	4	0
Loans Taken / (Repaid)	1,176	(670)	0	0
Interest Paid	(493)	(576)	(562)	(539)
Dividend paid (incl tax)	(786)	(1,243)	(1,979)	(2,522)
Income from investments				
Others	409			
Financing Cashflow	305	(2,489)	(2,537)	(3,061)
Net chg in cash	637	(2,347)	1,811	3,034
Opening cash position	2,766	3,431	1,083	2,893
Closing cash position*	3,403	1,083	2,893	5,927

Source: Company. Emkay Research

Balance Sheet

Y/E, Mar (Rs. mn)	FY10	FY11P	FY12E	FY13E
Equity share capital	375	388	392	392
Reserves & surplus	11,274	14,941	18,103	21,759
Net worth	11,648	15,328	18,495	22,151
Minority Interest	2,027	2,550	3,250	3,950
Secured Loans	6,519	5,849	5,849	5,849
Unsecured Loans	1,660	538	538	538
Loan Funds	8,179	6,387	6,387	6,387
Net deferred tax liability	40	145	145	145
Total Liabilities	21,895	24,411	28,277	32,633
Gross Block	31,821	38,821	42,821	46,821
Less: Depreciation	17,273	19,738	22,582	25,705
Net block	14,548	19,083	20,239	21,116
Capital work in progress	1,808	1,000	1,000	1,000
Investment	470	470	470	470
Current Assets	20,971	24,483	31,657	36,988
Inventories	6,752	8,215	10,060	10,824
Sundry debtors	7,688	9,579	11,921	12,790
Cash & bank balance	3,431	1,083	2,893	5,927
Loans & advances	3,101	5,607	6,783	7,447
Other current assets				
Current lia & Prov	15,921	20,643	25,107	26,959
Current liabilities	13,060	18,795	21,973	23,352
Provisions	2,861	1,848	3,134	3,607
Net current assets	5,051	3,840	6,550	10,029
Misc. exp	18	18	18	18
Total Assets	21,895	24,411	28,277	32,633

Key Ratios

Y/E, Mar	FY10	FY11P	FY12E	FY13E
Profitability (%)				
EBITDA Margin	8.8	10.7	10.6	11.4
Net Margin	3.8	5.3	5.7	6.3
ROCE	20.8	29.5	32.5	32.7
ROE	24.1	29.0	30.4	30.4
RoIC	22.3	34.0	35.4	38.3
Per Share Data (Rs)				
EPS	7.2	10.0	13.1	15.8
CEPS	14.1	16.3	20.4	23.7
BVPS	31.0	39.5	47.1	56.5
DPS	1.8	2.8	4.2	5.3
Valuations (x)				
PER	32.1	23.1	17.6	14.7
P/CEPS	16.3	14.1	11.3	9.7
P/BV	7.4	5.8	4.9	4.1
EV / Sales	1.3	1.2	0.9	0.9
EV / EBITDA	14.9	10.6	8.5	7.2
Dividend Yield (%)	0.8	1.2	1.8	2.3
Gearing Ratio (x)				
Net Debt/ Equity	0.4	0.3	0.2	(0.0)
Net Debt/EBITDA	0.7	0.5	0.3	(0.0)
Working Cap Cycle (days)	7.3	(4.4)	0.0	0.9

Recommendation History: Motherson Sumi Systems – MSS IN

Date	Reports	Reco	CMP	Target
26/05/2011	Motherson Sumi Q4FY11 Result Update	Accumulate	226	260
07/02/2011	Motherson Sumi Q3FY11 Result Update	Accumulate	186	210
02/11/2010	Motherson Sumi Q2FY11 Result Update	Accumulate	186	200
12/08/2010	Motherson Sumi Q1FY11 Result Update	Buy	176	205

Recent Research Reports

Date	Reports	Reco	CMP	Target
30/05/2011	Mahindra & Mahindra 4QFY11 Result Update	Buy	665	810
26/05/2011	Tata Motors Q4FY11 Conso Result Update	Buy	1,161	1,450
25/05/2011	JK Tyre & Industries Q4FY11 Result Update	Accumulate	92	118
20/05/2011	Ashok Leyland Q4FY11 Result Update	Accumulate	51	63

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