NALANDA RESEARCH

Institutional Research

February 07, 2019

Minda Industries

A Strong Play on the Changing Regulations

Strong Buy*

Downside Scenario	Current Price	Price Target	Upside Scenario
	290	359	
		23.7% ▲	

Robust Growth Continues; Despite Tough Environment

Minda Industries robust growth performance continues even during muted show from the OEMs. Its top line grew by 39% YoY to Rs. 1,470 crores in Q3FY19 led by superior performance in its 'Switches' (+71% YoY growth to Rs. 534 crores) as well as 'Others' segment (+50% YoY to Rs. 431 crores).The company's aftermarket as well as the inorganic inclusion of MRPL and I-Sys supported well in the overall growth. Mindarika and Minda Kosei, the two most important businesses have seen some volume impact on account of lower sales for 4W OEMs. This was offset by improvement in some other businesses.

Despite of increase in the commodity costs & subdued demand environment, the margins improved by 30bps YoY to 12.3% in Q3FY19. During the past few years, the company managed to improve the margins every year and we believe this improvement would continue gradually in the coming years as the company keeps on launching new higher margin products and its rigorous cost rationalization efforts will aid in achieving margin trajectory. Additionally, the company has set up a new R&D centre in Pune, which is focused on developing innovative products, which can further sharpen its competitive edge.

EBITDA Increased by 43% YoY to Rs. 180 crores for the quarter, while bottom line has shown a growth of 23% YoY to Rs. 81 crores for the same period. The lower growth in the profits was on account of decrease in other income (-65% YoY to Rs. 2.7 crores) and increase in the finance costs (+107% YoY to Rs. 14.5 crores) was on account of organic as well as inorganic acquisitions. In addition, the profits from the Associates/JVs declined by 65% YoY to Rs. 1.9 crores led by subdued automotive demand & margin pressure. While on the other side, the effective tax rate was lower by 230bps YoY to 26.3% in Q3FY19.

Temporary Blips in the Automotive Industry

The last six months automotive industry witnessed poor demand environment led by various macro factors, Despite of this, Minda Industries posted a strong set of results. We believe all these events came together and there was a temporary blip in the market. The GoI's focus on rural improvement and the middle class, would provide a boost to the consumption and we think small cars, 2Ws as well as tractors sales to improve in the short term. The company's growth was 3x *(excluding consolidation)* of the industry's growth in the 3rd quarter and we believe, the company has the potential to grow at least twice the industry growth in the coming years.

Minda's Moat along with Regulatory Push and Premiumization to Drive Growth

The Triple Combination of a 'Large Customer Base' + 'Strong Tie-ups with the Global Technology Giants' + 'Diversified Product Portfolio' with improving market share in the majority of the products provides a strong 'MOAT' & entry barrier for Minda Industries.

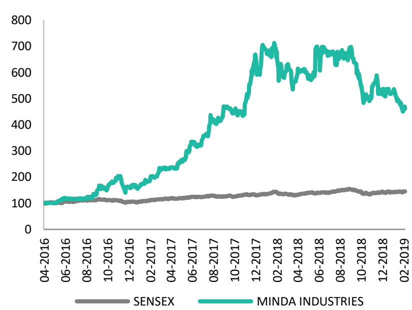
Enormous Opportunity due to Changing Regulations

As the industry has mandated to move towards BS6, we see strong demand for Sensors *(including engine related sensors)*, Advance filtration, etc. Apart from this, the Enhanced Safety Norms to further push higher demand for Reverse Parking Sensors, Air Bags, Seat belts/reminders, etc. The company is already manufacturing all these products and has a strong collaboration with the global technology leaders.

Market Data	
Industry	Auto Ancillaries
Sensex	36,975
Nifty	11,062
Bloomberg Code	MINDA:IN
Eq. Cap. (INR Crores)	53
Face Value (INR)	2
52-w H/L	455/274
Market Cap (INR Crores)	7,611

Valuation Data	FY19E	FY20E	FY21E
OPM	12.3%	12.7%	13.1%
NPM	6.1%	6.4%	6.7%
P/E (x)	22.0	18.3	15.1
EV/EBITDA (x)	9.5	8.1	7.3

Minda Industries vs. SENSEX



Shareholding Pattern (%)	Dec-17	Mar-18	Dec-18
Promoters	71%	71%	71%
FII	8%	9%	11%
DII	7%	6%	4%
Retail	14%	13%	14%
Total	**100**	**100**	**100**

(INR Crores)	FY17	FY18	FY19E	FY20E	FY21E
Revenue	3,386	4,471	6,068	7,038	8,012
Growth (%)	*34.0%*	*32.0%*	*35.7%*	*16.0%*	*13.8%*
EBITDA	374	534	749	897	1,051
Growth (%)	*57.3%*	*42.8%*	*40.3%*	*19.8%*	*17.1%*
EBITDA Margin (%)	11.0%	11.9%	12.3%	12.7%	13.1%
PAT	185	331	373	447	541
Growth (%)	*68.2%*	*78.8%*	*12.7%*	*20.0%*	*20.9%*
EPS (INR)	6.2	11.7	13.2	15.8	19.2
P/E (x)	15.6	25.2	22.0	18.3	15.1
EV/EBITDA (x)	6.6	13.8	9.5	8.1	7.3

Source: Company, NSPL Research

** Read last page for disclaimer & rating rationale*

Head of Research
Vaibhav Chowdhry
vaibhav.chowdhry@nalandasecurities.com

Analyst
Amit Hiranandani
amit.hiranandani@nalandasecurities.com

NALANDA SECURITIES PRIVATE LIMITED
310-311 Hubtown Solaris, NS Phadke Marg, Opp Teli Gali, Andheri East, Mumbai 69
+91-22-6281-9649 | research@nalandasecurities.com | www.nalandasecurities.com

All the Segments are on Fast Lane

Switches Division

The switches segment *(contributed 36% in Q3FY19 vs. 30% in Q3FY18 in the net revenues)* has seen a robust jump of 71% YoY to Rs. 534 crores. Along with the company's strong performance, this growth was also higher, as it also includes inorganic inclusion of MRPL. This segment has grown by 24% in the past three years on a CAGR basis. We expect it would continue to see double digit growth on account of changes in the regulatory norms & continued growth in the automotive industry. The BS6 implementation will give a push to the growth of Sensors *(including engine related sensors)*. Also, it continues to make high margin products such as Music System and Power Windows Switches. We expect more premiumization to continue in it.

Lamps Division

The Lamps segment *(contributed 23% in Q3FY19 vs. 28% in Q3FY18)* has posted 15% YoY growth to Rs. 337 crores in the 3rd quarter. Its EBITDA Margin too improved by 160bps YoY to 10.1% for the quarter. The past growth has been substantial in the Lighting Segment *(~63% CAGR FY16-FY18)* and we conservatively expect lower double digit growth to continue as the company keeps adding newer customers especially in the 2Ws segment and innovating products under lighting segment. We believe all this along with premiumization of products should help the company to grow the revenue in double digit. Further, lower PV penetration, should help Minda to grow its products like Headlamp Levelling Motors.

Horns Division

The Horns segment *(contributed 11.5% in Q3FY19 vs. 15.5% in Q3FY18)* reported marginal growth of 3.3% YoY to Rs. 169 crores in the 3rd quarter. The EBITDA Margin too fell by 130bps YoY to 7.5% for the same period. The issue was majorly with its subsidiary *Clarton Horns* in Europe. A lot of inventories were piled up with the OEMs, hence, sales were depressed, resulting in lower volumes as well as margins. The management remained optimistic and guided 8-9% as a sustainable margin for the medium term. We remained conservative due to on going subdued global automotive performance and projected lower than the guided range for the next few years.

The company is a market leader and has 47% market share in 2W+4W Horns. We expect it to gradually improve its market share and grow inline with the automotive vehicles growth of 10% CAGR in the coming three years. The growth and margins will improve gradually, as the industry is moving from Electromechanical Horns to Electronic Horns, which is a high margin product.

Other Business

This segment contains majorly Alloy wheels, Aluminium Die Casting, Blow Moulding, etc. and it contributed about 29.3% in Q3FY19 vs. 27.2% in Q3FY18. The 'Others' segment reported a revenue growth of 50% YoY to Rs. 431 crores in Q3FY19, but, the margins fell by 280bps YoY to 17.1% for the same period.

It has many products under it and we think due to regulatory push, safety norms and premiumization, there are certain products, which should see higher growth. These products are Advanced Filters, Alloy Wheels, Seat Belts/Reminders, Air Bags, Combi Braking Systems, Battery Management, Advanced Driving Assistance System, Infotainment System, Telematics, Wireless Chargers, AMT, etc. Hence, we expect a continued high double digit growth in it. The Alloy Wheels margins are high and the penetration level is lower. Maruti being the largest customer for Minda in Alloy Wheels should continue to drive growth in the coming years.

Trading at Eye-Catching Valuations

We strongly believe in the company's business model and its potential growth in the medium to long term on account of its competitive positioning, this along with its continued strategy of introduction of newer products in its kitty. Minda Industries is a direct beneficiary of the automotive industry growth and has enormous opportunity led by the changing regulations and premiumization. Overall, we trust that the combination of Regulatory Norms, Enhanced Safety Requirements, Premiumization and Electrification will eventually have a positive impact on the company's performance.

At CMP of 290, the stock is trading at a very attractive level of 18.3x FY20E EPS of Rs. 15.8. We have adjusted the financials looking at the poor demand outlook of OEMs in domestic as well as overseas. ***We recommend a Strong Buy on Minda Industries with an average target price of Rs. 359 per share***, valuing the company with DCF and EV/EBITDA Methodology. We have assigned 11.4x to its FY20E EBITDA, in-line to its last two years average EV/EBITDA on account of huge potential and growth opportunities in the $49bn domestic auto ancillary industry.

Source: Company, NSPL Research

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Vaibhav Chowdhry
vaibhav.chowdhry@nalandasecurities.com

Analyst
Amit Hiranandani
amit.hiranandani@nalandasecurities.com

NALANDA SECURITIES PRIVATE LIMITED
310-311 Hubtown Solaris, NS Phadke Marg, Opp Teli Gali, Andheri East, Mumbai 69
+91-22-6281-9649 | research@nalandasecurities.com | www.nalandasecurities.com

Q3FY19 Result Analysis

(INR Crores)	Q3FY19	Q3FY18	YoY (%)	Q2FY19	QoQ (%)	9MFY19	9MFY18	YoY (%)
Net sales	**1,470**	**1,056**	**39.2%**	**1,522**	**-3.4%**	**4,422**	**3,100**	**42.6%**
COGS	903	647	39.6%	938	-3.7%	2,724	1,918	42.0%
Employee Expenses	205	141	44.9%	195	4.9%	589	410	43.5%
Other Expenses	181	141	28.6%	199	-9.1%	570	407	39.9%
EBITDA	**180**	**126**	**42.8%**	**189**	**-4.7%**	**540**	**364**	**48.2%**
D&A	61	42	44.9%	56	8.5%	166	116	43.3%
Other income	3	8	-64.8%	5	-43.3%	14	21	-33.4%
EBIT	**122**	**92**	32.8%	**138**	-11.4%	**388**	**269**	43.9%
Interest Expense	15	7	107.0%	15	-3.6%	43	21	101.7%
PBT	**108**	**85**	**26.7%**	**123**	**-12.3%**	**345**	**248**	**39.0%**
Tax	28	24	16.7%	39	-26.8%	101	75	33.9%
PAT	**81**	**66**	**23.0%**	**89**	**-8.4%**	**255**	**191**	**33.4%**
EPS in INR	**2.7**	**2.3**	**16.7%**	**2.7**	**-3.3%**	**8.0**	**6.7**	**19.0%**

Margin Analysis	Q3FY19	Q3FY18	YoY (%)	Q2FY19	QoQ (%)	9MFY19	9MFY18	YoY (%)
Material Expenses % Net Sales	61.4%	61.3%	0.2%	61.6%	-0.2%	61.6%	61.9%	-0.3%
Gross Margin	38.6%	38.7%	-0.2%	38.4%	0.2%	38.4%	38.1%	0.3%
Employee Expenses % Net Sales	13.9%	13.4%	0.5%	12.8%	1.1%	13.3%	13.2%	0.1%
Other Expenses % Net Sales	12.3%	13.4%	-1.0%	13.1%	-0.8%	12.9%	13.1%	-0.3%
EBITDA Margin (%)	12.3%	12.0%	0.3%	12.4%	-0.2%	12.2%	11.8%	0.5%
Tax Rate (%)	26.3%	28.6%	-2.3%	31.5%	-5.2%	29.2%	30.3%	-1.1%
PAT Margin (%)	5.5%	6.3%	-0.7%	5.8%	-0.3%	5.8%	6.2%	-0.4%

Source: Company, NSPL Research

Key Quarterly Highlights:

- Minda acquired KPIT Engineering Ltd's telematics hardware products business, which consists of VTS - AIS 140, OBITS (On Bus Integrated Telematics Systems complying to UBS-II specifications) and telematics products for School buses. The company has paid Rs. 25 crores as a initial consideration and would pay the balance amount once it achieves certain milestones.

- Earlier Roki Minda's 'Filters' product was expected to get impacted due to transition to BS6, however, due to product R&D and innovations, the company has built BS6 complaint 'Filters'.

- The company has a gross debt of about Rs. 850 crores, which increased from Rs. 609 crores as of 31st March 2018. The company keeps on looking for inorganic opportunities and hence, we expect in spite of the good FCF generation in the coming years, the company's D/E (x) would sustain at 0.4x levels. The company's finance costs increased by 107% YoY to Rs. 14.5 crores for the quarter on account of organic as well as inorganic acquisitions.

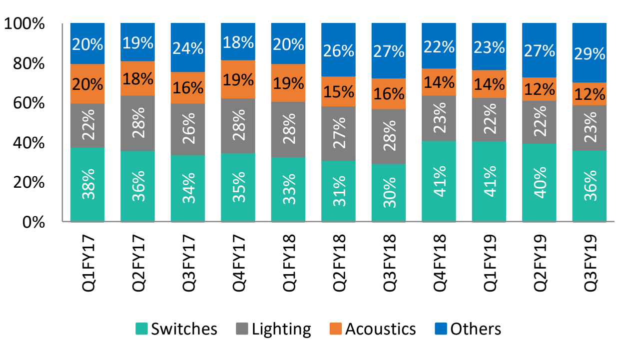
- D&A increased by 45% YoY to Rs. 61 crores in Q3FY19 on account of capitalization of new projects in the state of Gujarat. The profits for some of the JVs and associates declined due to delay in getting export orders. However, the management expects the momentum to be positive very soon and will see better profitability in the 4th quarter. Additionally, due to higher inventories, the costs increased.

- Minda Industries has finished 95% of the consolidation. The capital expenditure in FY19E and FY20E is expected to be Rs. 450 crores and Rs. 400 crores respectively.

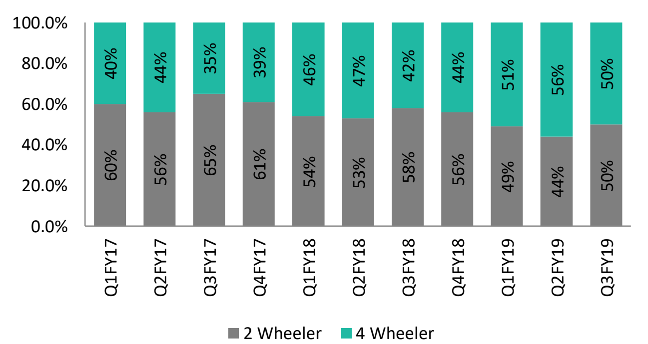
- Minda Industries entered into 2W alloy wheels and is in the process of setting up the facility for the same, which will get commissioned by March 2020 and will gradually ramp up.

- The company has stated that they will keep on improving its dividend payout to reward shareholders and in this quarter, the management has declared an interim dividend of Rs. 0.45 per share vs. Rs. 0.40 per share in the last year.

Division Breakup (%)



Segment Breakup (%)



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Key Quarterly Highlights:

The management has been working sharply in improving margins, which is clearly visible in the past several years of the performance. Along with adding newer, higher margin products, it is also taking internal measures like cost optimization and continues to look each and every aspects of the costs. The company aspires to keep improving its margin in the coming years.

Investments Rationale

Well-built Competitive Advantage

Minda Industries has created a strong competitive edge with a triple combination of 'Large Diversified Product Base' + 'More Than 50 OEMs are its Clients' + 'Tie-ups with 12 Global Technology Leaders'. We think no other auto ancillary company has this level of superiority, which itself has created a Strong Moat and an Entry Barrier. Another mastery is that the company is a Tier 1 supplier to almost all the largest OEMs in India as well as Internationally, and we believe with an ease, Minda has the ability to cross sell its products to OEMs.

Direct Beneficiary of Growth in the Automotive Industry

Minda Industries in the past several years has grown more than 2.5x-3.5x of the automotive industry growth driven by the introduction of newer products, addition of OEMs & its new launches and increasing content per vehicle. We have conservatively estimated Minda Industries topline to grow by at least 2x of the automotive industry growth. The company is present across all the sub-segments of automotive industry viz. 2W, 3W, PV, CV & Off-road segments, which we believe gives a widespread exposure towards the industry and makes Minda a direct beneficiary of the growth in the automotive industry.

Enormous Opportunity led by Changing Regulations and Premiumization

As the industry has mandated to move towards BS6 and higher safety standards, we see strong demand for Sensors *(including engine related sensors)*, Advance Filtration, Air Bags, Seat Belts Reminders, etc. The penetration level of Airbags, Reverse Parking Sensors and Seat Belt Reminders is low in India vis-à-vis developed nations and these products are going to get mandatory from 1st July 2019. Additionally, the market itself is moving towards premium components viz. LEDs, Advanced Driving Assistance System, Alloy Wheels, Infotainment System, Telematics, Wireless Chargers & AMT. All these products have enormous opportunity and high margin too. Minda Industries already manufactures all these products and we see a huge opportunity in it.

Risks

- **Quality Compromise:** To reduce quality risk, skilled workforce has provided job skill enhancement training. Additionally, the company regularly interacts with its suppliers and supervises by conducting periodical audits in their plants. Hence, the raw material plus processes meets the quality standards.

- **Competition:** To offset this, the company undertakes continuous R&D activities and has strong technical tie-ups.

- **Technology obsolescence:** Minda is associated with its JVs and associations with the global majors to deliver cutting edge technology products.

- The **on-going trade wars** between the major economies can disrupt the global automotive demand and in-turn impact the financials of Minda Industries.

- The sudden and continuous **increase in the commodities** and major raw material prices can bring down its overall margins. Although, the company has some pass through clause with its major customers.

- **Any divorce with the its global technology tie-ups.**

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Minda Industries – *SWOT Analysis*

STRENGTHS

Minda Industries has a wide distribution reach at about 30,000 touch points, which gives us confidence that its products would reach the farthest corners of India.

We strongly believe that the company's strategic tie-ups with the technology leaders globally would provide strong competitive edge. It has alliances with global leaders like Tokai Rika, Emer, Toyoda Gosei, Kyoraku, Torica, Kosei, etc.

It has strong, long standing relationships with OEMs, which resulted in a Tier 1 preferred supplier status to Minda Industries. The company has over 50 OEMs as its clients.

Minda Industries has strategically placed its manufacturing locations near to the automotive hubs in India, which resulted in efficient supply chain distribution and lower logistics cost.

The company continues to work on its R&D and keep introducing innovative products. It has six R&D centers globally and spends ~4% of its revenues for R&D activities.

OPPORTUNITIES

The Government has mandated to shift to BS6 norms by April 2020, which would reduce NOx emissions. This transition will present the Auto Component manufacturers with the opportunity to participate in New/Complex/Futuristic products, which provides better margins.

The Indian Government's push for Electric Cars to meet the emission reduction targets could provide new opportunities for auto component players. The EVs requires newer lightweight and more premium products as compared to the normal ICE engine vehicles.

The OEMs product life cycle is getting shorter, which could provide auto component players an added advantage as new models will require new, better & premium parts. This will provide a continued growth for the auto component industry.

Due to regulatory requirements, technology changes, high costs, etc. the global OEMs prefer to outsource the component manufacturing to low cost countries like India.

WEAKNESSES

The Exports contribute about ~18% in the last financial year and the management expects it to increase to 25% in the coming years. Any slowdown in the major economies can impact it's financials.

In a few of its segments viz. 4W Switches, 2W Switches, Alloy Wheels and Die Casting, the company majorly depends on one-two customers for its revenues. Any breakup in the association with the largest customers can impact the company's performance.

THREATS

Although, Minda Industries has its separate R&D, but it majorly depends upon its technology partners for new innovations. A separation with the global technology partners can possibly lose its competitive advantage and in turn impact its performance.

MIL's growth is dependent on the Automotive Industry, which in turn depends upon the macro-economic stability. Any decline in the growth of the automotive industry can impact the performance of Minda Industries.

Source: Company, NSPL Research

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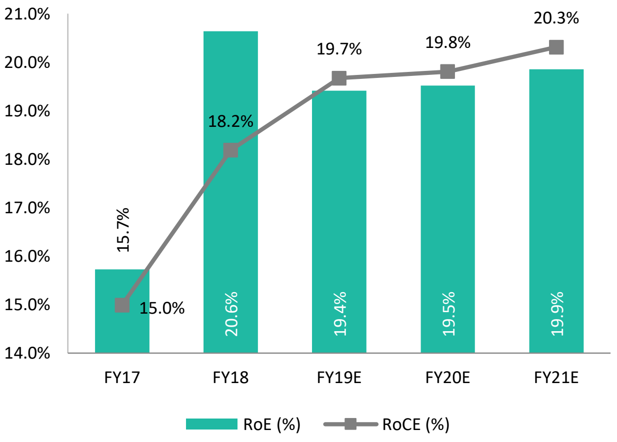
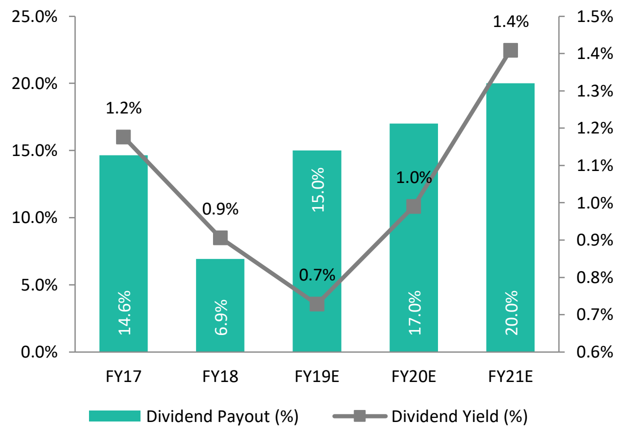
Story in Charts

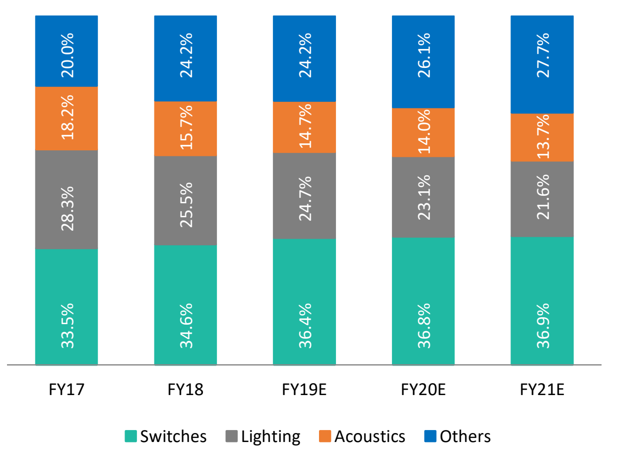
Return Ratios Continues to Improve



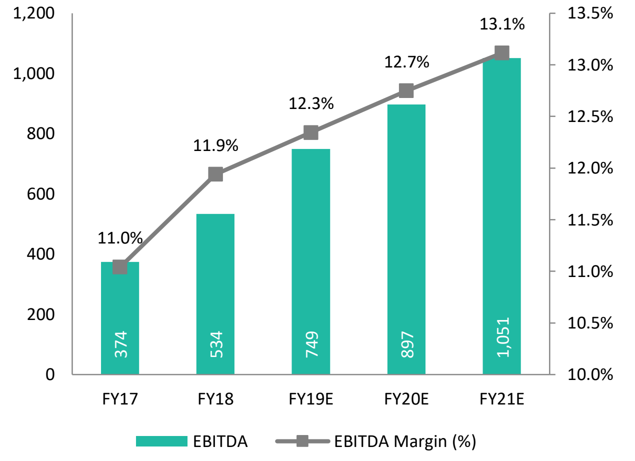
Dividend Payout to Improve Going Forward



Switches and Others Segment to Lead Growth



EBITDA Margin to remain Healthy



Robust Past High Double Digit Growth Performance

	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E	FY21E
Net Sales Growth (%)	27.3%	30.8%	13.2%	34.0%	32.0%	35.7%	16.0%	13.8%
EBITDA Margin (%)	5.1%	6.9%	9.4%	11.0%	11.9%	12.3%	12.7%	13.1%

Source: Company, NSPL Research

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Profit & Loss (INR Crores)	FY17	FY18	FY19E	FY20E	FY21E
Net Sales	**3,386**	**4,471**	**6,068**	**7,038**	**8,012**
COGS	2,116	2,763	3,738	4,348	4,963
Employee Expenses	451	587	790	895	997
Other Expenses	445	587	792	897	1,002
EBITDA	**374**	**534**	**749**	**897**	**1,051**
D&A	136	165	215	260	282
Other income	14	33	21	26	29
EBIT	**252**	**402**	**555**	**664**	**798**
Interest Expense	40	35	51	59	67
PBT	**212**	**367**	**504**	**604**	**731**
Exceptional Items	0	38	0	0	0
PBT (Including exceptional items)	212	405	504	604	731
Tax	46	98	146	175	212
PAT	**165**	**308**	**358**	**429**	**519**
Add:- Share of profit of associates and joint ventures	20	23	15	18	22
Total Profit After Share of Profit of Associates and Joint Ventures	**185**	**331**	**373**	**447**	**541**
Adj. EPS in INR	6.2	11.7	13.2	15.8	19.2

Balance Sheet (INR Crores)	FY17	FY18	FY19E	FY20E	FY21E
Share Capital	16	17	53	53	53
Net Worth	**1,176**	**1,603**	**1,919**	**2,290**	**2,723**
Long Term Borrowings	177	240	348	400	448
Other Financial Liabilities	54	51	70	81	92
Long Term Provisions	59	104	141	163	186
Total Non Current Liabilities	**290**	**395**	**559**	**645**	**727**
Short Term Borrowings	261	303	454	545	627
Trade Payables	486	798	1,085	1,275	1,469
Other Financial Liabilities	120	155	219	256	291
Other Current Liabilities	48	92	114	126	152
Short Term Provisions	9	15	20	23	27
Current tax liabilities (net)	7	4	5	6	7
Total Current Liabilities	**931**	**1,367**	**1,897**	**2,230**	**2,572**
Total Equity and Liabilities	**2,398**	**3,365**	**4,375**	**5,165**	**6,022**
Fixed and Intangible Assets	1,002	1,561	1,805	1,979	1,939
Long Term Financial Assets	129	187	260	310	362
Deferred tax assets (net)	30	19	0	0	0
Other tax assets	15	31	39	46	56
Other non-current assets	20	40	55	64	72
Total Non-Current Assets	**1,196**	**1,838**	**2,159**	**2,400**	**2,429**
Inventories	238	418	553	631	707
Short Term Financial assets					
Trade receivables	500	790	1,072	1,243	1,415
Cash and cash equivalents	358	126	340	605	1,149
Bank balances other than those included under cash and cash equivalents	16	34	34	34	34
Loans	1	2	2	3	3
Other current financial assets	8	18	24	28	32
Other current assets	82	141	191	222	252
Total Current Assets	**1,202**	**1,527**	**2,216**	**2,765**	**3,593**
Total Assets	**2,398**	**3,365**	**4,375**	**5,165**	**6,022**

Source: NSPL Research

Head of Research
Vaibhav Chowdhry
vaibhav.chowdhry@nalandasecurities.com

Analyst
Amit Hiranandani
amit.hiranandani@nalandasecurities.com

NALANDA SECURITIES PRIVATE LIMITED
310-311 Hubtown Solaris, NS Phadke Marg, Opp Teli Gali, Andheri East, Mumbai 69
+91-22-6281-9649 | research@nalandasecurities.com | www.nalandasecurities.com

Cash Flow (INR Crores)	FY17	FY18	FY19E	FY20E	FY21E
PBT	212	405	504	604	731
Operating Profit before Working Capital Changes	382	550	746	892	1,044
Cash Generated from Operations	390	447	685	872	1,044
Less: income tax paid	-56	-85	-146	-175	-212
Cash Flow from Operating	**334**	**362**	**539**	**697**	**832**
(Incr)/ Decr in Gross PP&E	-254	-517	-450	-400	-200
Cash Flow from Investing	**-271**	**-641**	**-512**	**-439**	**-242**
(Decr)/Incr in Debt	-3	84	259	143	130
Finance costs	-39	-35	-51	-59	-67
Cash Flow from Financing	**253**	**46**	**188**	**8**	**-46**
Incr/(Decr) in Balance Sheet Cash	320	-232	215	265	545
Cash at the Start of the Year	38	358	125	340	605
Cash at the End of the Year	**358**	**125**	**340**	**605**	**1,149**

RATIOS	FY17	FY18	FY19E	FY20E	FY21E
Profitability:					
Return on Capital (%)	15.0%	18.2%	19.7%	19.8%	20.3%
Return on Equity (%)	15.7%	20.6%	19.4%	19.5%	19.9%
Margin Trend:					
EBITDA Margin (%)	11.0%	11.9%	12.3%	12.7%	13.1%
Net profit Margin (%)	5.5%	7.4%	6.1%	6.4%	6.7%
Solvency:					
Total Debt / Equity	0.4	0.4	0.5	0.5	0.4
Valuation Ratios:					
P/E	15.6	25.2	22.0	18.3	15.1
EV/EBITDA	6.6	13.8	9.5	8.1	7.3
P/B	2.2	4.9	4.0	3.4	2.8

Source: NSPL Research

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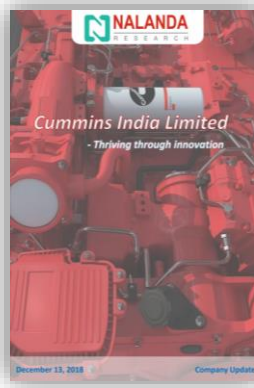

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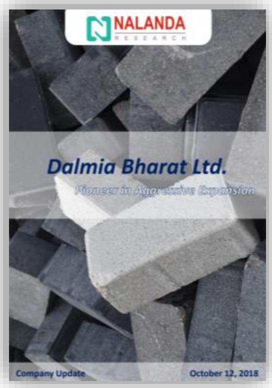

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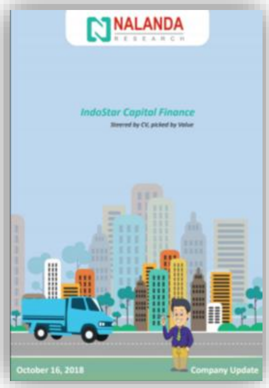

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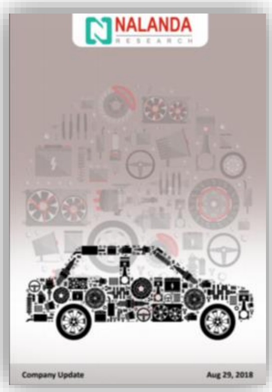
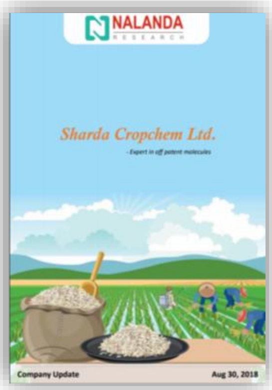


Minda Industries



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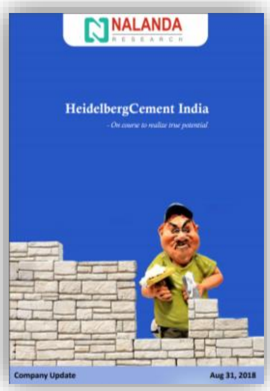

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Minda Industries			
Date	**CMP (INR)**	**Target Price (INR)**	**Recommendation**
February 07, 2019	290	359	Strong Buy
November 06, 2018	340	474	Strong Buy
August 29, 2018 (Company Update)	424	521	Strong Buy

Rating Legend	
Strong Buy	**More than 15%**
Buy	**5% - 15%**
Hold	**0 – 5%**
Reduce	**-5% - 0**
Sell	**Less than -5%**

Following table contains the disclosure of interest in order to adhere to utmost transparency in the matter;

Disclosure of Interest Statement	
Details of Nalanda Securities Pvt. Limited (NSPL)	• NSPL is a Stock Broker registered with BSE, NSE and MCX - SX in all the major segments viz. Cash, F & O and CDS segments. Further, NSPL is a Registered Portfolio Manager and is registered with SEBI • **SEBI Registration Number: INH000004617**
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Other disclosures	NO

Head of Research
Vaibhav Chowdhry
vaibhav.chowdhry@nalandasecurities.com

Analyst
Amit Hiranandani
amit.hiranandani@nalandasecurities.com

Vaibhav Chowdhry
Digitally signed by Vaibhav Chowdhry
DN: c=IN, o=Personal, postalCode=400067, st=Maharashtra, 2.5.4.20=c44ae119d8d0e0355f921ec5b5b16b20a503a0432064c67c6686fe4e91a20b4c, pseudonym=e92965821e484f5b8fe916fd5d5cc70d, 2.5.4.45=034900303130303038333931797972575468495041657862414254325432536445687348654E414F7143435666764B736A5634346461707248774662666933626732 2B49685841484D7A38, serialNumber=9d8b3451c82c6d07db54ced05db1c660f14016eb7623697f23fea259e7e71187, cn=Vaibhav Chowdhry
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NALANDA SECURITIES PRIVATE LIMITED
310-311 Hubtown Solaris, NS Phadke Marg, Opp Teli Gali, Andheri East, Mumbai 69
+91-22-6281-9649 | research@nalandasecurities.com | www.nalandasecurities.com