



Elecon Engineering is positioned favorably with a strong free cash flows & debt-free balance sheet, a dominant share in the domestic market, and emerging opportunities for exports. The company anticipates a strong performance in the coming years, backed by enhanced capacity utilization, effective working capital management, and inventory optimization.

Key Projections

The company's management has projected **20% Y-o-Y growth for the next three years until FY27**. Also looking ahead to **FY30, a sustained 15% year-on-year growth appears quite achievable**, contingent upon geopolitical scenarios remaining relatively stable.

The company has also increased their **sustainable EBITDA margin guidance to 23.5% from 22% earlier** - provided there is not much volatility in RM prices

The company **remains committed to generate an ROCE of 25%+ levels in the coming years**, owing to debt reduction, working capital & inventory optimization.

Financial Summary

Y/E Mar (Rs mn)	FY21	FY22	FY23	FY24E	FY25E	FY26E
Net sales	10,447	12,119	15,297	20,345	24,414	29,296
EBIDTA	1,856	2,464	3,389	4,687	5,735	7,010
Margins (%)	17.8	20.3	22.2	23.0	23.5	23.9
Adjusted net profit	576	1,405	2,375	3,288	4,105	5,102
EPS (Rs)	5.1	12.5	21.2	29.30	36.59	45.5
P/E (x)	185	76	45	32	26	21
EV/EBITDA (x)	58	43	31	23	18	14
RoCE (%)	15.40%	21.42%	26.49%	24.26%	24.76%	24.95%
RoE (%)	6.27%	13.38%	18.57%	20.77%	20.87%	20.83%

Source: Company, Dalal & Broacha Research

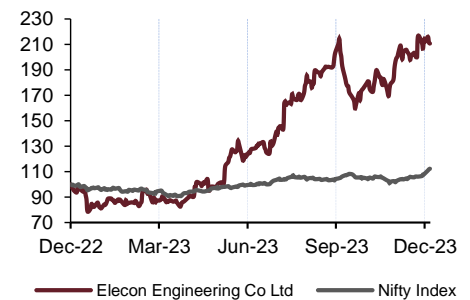
Rating	TP (Rs)	Up/Dn (%)
BUY	1,137	20

Market Data

Current price	Rs	930
Market Cap (Rs.Bn)	(Rs Bn)	104
Market Cap (US\$ Mn)	(US\$ Mn)	1,252
Face Value	Rs	2
52 Weeks High/Low	Rs	989.8 / 331.25
Average Daily Volume	('000)	352
BSE Code		505700

Source: Bloomberg

One Year Performance



Source: Bloomberg

% Shareholding	Sep-23	Jun-23
Promoters	59.29	59.29
Public	40.71	40.71
Total	100	100

Source: Bloomberg

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Elecon primarily has 2 segments- Gears segment & MHE Segment.

MHE Segment guidance:

In FY23 company clocked a revenue of 200 Cr in MHE Business; For FY24 they have guided for a 300Cr- 400Cr topline - **expected to grow at 25% CAGR till FY25 with target to cross 500 Cr topline. Margins in MHE to also improve from 15%-16% band to 20%+ in the coming years due to tailwinds in the sector.**

Gears Segment Guidance:

The current Exports- Domestic split in the gears segment is ~70:30.

Elecon is now ready to transition from a local to Global Gears Solution Company- Exports to be the key lever of growth:

Key Guidance for exports:

- **Total Global Addressable market** ~1 Lac Crore (growing at 3-4% CAGR annually) - Elecon's current global market share being less than 1% - the company sees huge growth potential in exports. The company targets to *achieve atleast a 5% market share in the global industrial gears market thus will grow at ~26% CAGR in exports. Eventually they plan to have an even domestic to exports ratio of 50:50 by 2030 for the gears segment.
- **Elecon first started establishing export presence** in 2010 through their acquisition of Radicon & Benzler. However they haven't been able to occupy a sizeable share in the global market due to variety of macro factors as well as some challenges at the financial & technical level. Currently global players like **Flender, Bonfiglioli, SEW & Nord occupy 30% of the global market share** & will be the key competitors for Elecon.
- **Currently Elecon generates ~200 Cr of revenue from UK & Europe & ~80-100 Cr of revenue from the US.**
- Elecon identifies the **following changes** they have made over the years to **act as enablers to propel growth in exports:**
 - **Better financial stability** - Currently the company is zero-debt, until 3 years back upto March 2020 - they used to have borrowings to the extent of 400 Cr- which now stand fully repaid. Their cash balance in the same period has grown from 107 Cr to 309 Cr in Sep 2023.
 - **More standardization** - Elecon has now launched a EON-2 series which offers a comprehensive range of right angle and parallel shaft combinations with ratios to suit all major 50/60 Hz motor across sectors - thus bringing almost 50% standardization in terms of inputs & design- eventually leading to improved operational efficiency, reduced operational costs, and inventory optimization.
 - **Signed-off Five OEM Business** in European market, having annual estimated business volume of ~Euro 5 Million (~50 Crore p.a) . Dealing with OEM's of the like of Continental AG, will create a ripple effect for them in Europe & other continents.

Elecon's Dominance in Domestic Industrial Gears Market expected to continue

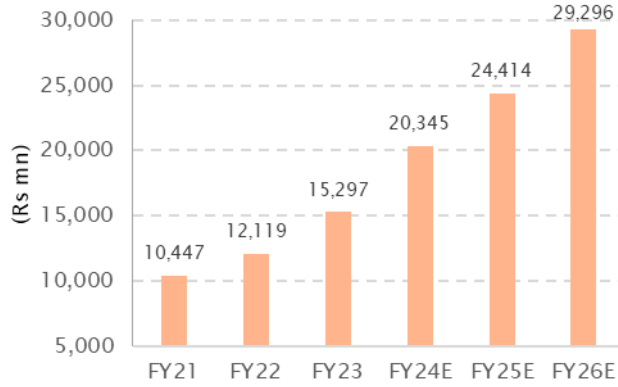
The domestic organized industrial gears market which is ~3000-4000 Cr (growing between 4-5% CAGR) – Elecon commands a 39-40% market share. Premium Gears & Shanthi Gears (2nd biggest player in the Indian market) are the other major peers for Elecon in industrial gearboxes in India. However, Elecon operates at a formidable scale, nearly four times that of Shanthi Gears. Leveraging its leading market share in the domestic market, Elecon with its vast variety in gearboxes, superior technology & expertise is poised for consistent double-digit growth in India.

Consistent improvement in Margins:

In the past 3 years from March 2020 to March 23 they have improved their margins from 11% to as 23% on account of the following:

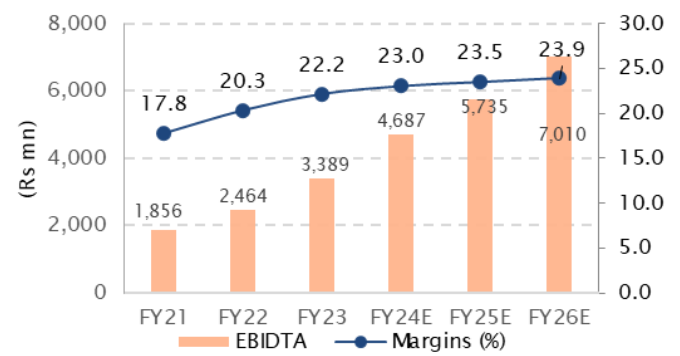
- **Improving Capacity Utilisation** - Elecon has ramped up from ~60% utilization to **76% current utilization levels** within a year's time, with further scope to touch around **85-90% peak capacity utilization levels**. Margins have steadily improved along with better capacity utilization.
- **Better product Mix:** Over the years their Engineered gears' mix in the volume has gone up from 38% in FY19 to 55% in H1FY24 – which has led to margin expansion
- **Reducing operating cycle & faster delivery:** For standardised/ catalogue gears –they have trimmed their delivery time to as low as 15 days, also for the engineered gearboxes they have brought down their lead times from 9-12 months historically to 4-6 months currently
- **Reducing working capital:** Their debtor days have improved from 177 days in FY21 to 83 days in FY22, also on account of standardization their inventory has been optimized i.e. Inventory days have gone down from 87 days in FY21 to 67 days in FY23. Thus leading to better working capital cycles & higher margins.

Exhibit 1: Revenues growing at 24% CAGR for FY23-26E



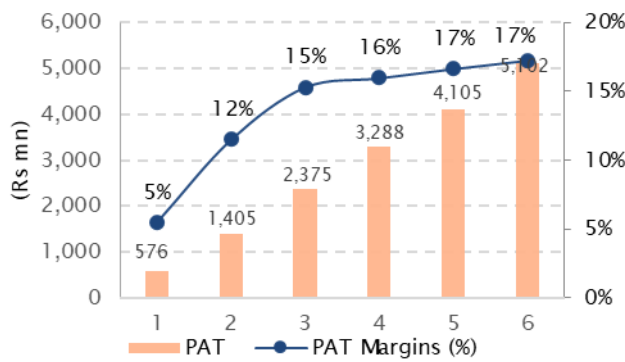
Source: Company, Dalal & Broacha Research

Exhibit 2: EBITDA growing at 27% CAGR for FY23-26E



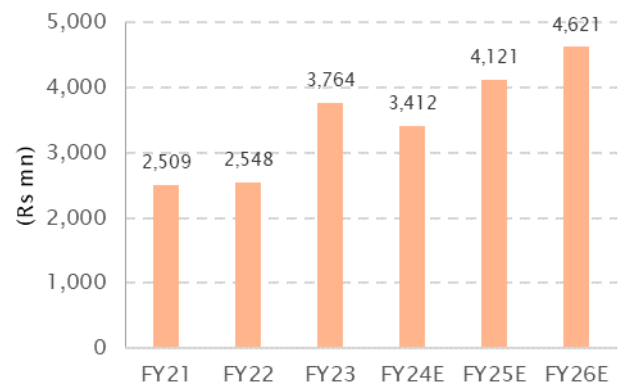
Source: Company, Dalal & Broacha Research

Exhibit 3: PAT growing at 29% CAGR for FY23-26E



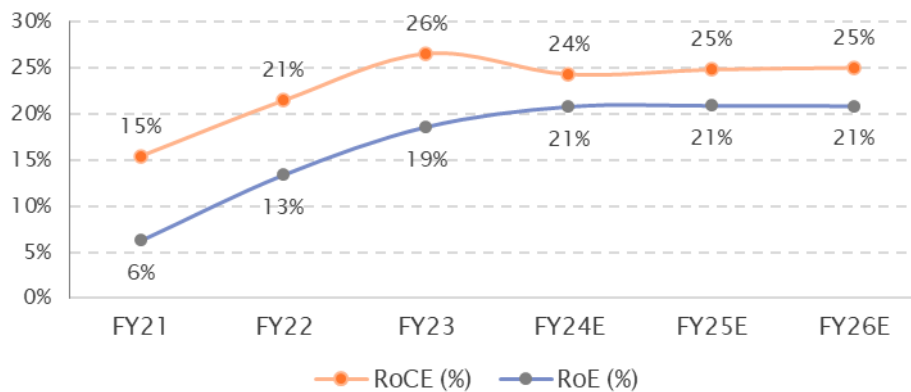
Source: Company, Dalal & Broacha Research

Exhibit 4: Rising Free Cash Flows



Source: Company, Dalal & Broacha Research

Exhibit 5: Strong RoCE & RoE



Source: Company, Dalal & Broacha Research

Valuation & Outlook

Elecon has delivered a 12% CAGR in terms of Revenue, 34% in terms of EBITDA & 38% in terms of PAT in the last 3 years. At the same time it has achieved a consistent 20%+ EBITDA margins in the last 6 quarters. The company is now debt-free, generating an RoE of 18.57% & RoCE of 26.49% & an FCFF yield of 2.7%.

As compared to one of its key listed peers i.e. Shanthi Gears, Elecon is 4x in terms of Revenue, generating similar 3-Yr CAGR for EBITDA & PAT ~30%+. Shanthi Gears currently trades at a 50x TTM P/E.

With growth to continue for Elecon in the domestic market coupled with strong focus now to expand presence in the overseas market – Elecon looks geared for double-digit growth till FY30. Considering strong execution history of the company & strong tailwinds in manufacturing & industrials sector, **We remain positive on the stock in the medium-to-long-term as well – hence recommend a “BUY” on the stock. At the CMP of 950 - it is valued at 32x FY24E EPS of Rs 29; 26x FY25E EPS of 36.5; 21x on FY26E EPS of 45.5– we have assigned a target of Rs 1137 at a 25x FY26E EPS (20% upside).**

Note: Also attached below is our plant visit note for your reference purpose.

Financial Summary

P&L (Rs mn)	FY21	FY22	FY23	FY24E	FY25E	FY26E
Net Sales	10,447	12,119	15,297	20,345	24,414	29,296
Total Operating Expenses	5,621	6,613	8,357	11,088	13,281	15,908
Employee Cost	1,179	1,282	1,497	1,722	1,980	2,277
Other Expenses	1,790	1,761	2,054	2,848	3,418	4,102
Operating Profit	1,856	2,464	3,389	4,687	5,735	7,010
Depreciation	521	486	490	448	472	484
PBIT	1,335	1,979	2,898	4,238	5,262	6,526
Other income	57	86	201	211	221	232
Interest	598	373	133	100	50	-
PBT (Before share of JV/associates)	794	1,691	2,966	4,349	5,434	6,758
Share of JV/Associates	19	14	32	35	40	45
PBT	813	1,705	2,998	4,384	5,474	6,803
Provision for tax	237	300	623	1,096	1,368	1,701
PAT (From continuing operations)	576	1,405	2,375	3,288	4,105	5,102
PAT (From Discontinuing operations)	-	-	-	-	-	-
MI						
Reported PAT	576	1,405	2,375	3,288	4,105	5,102
Adjusted Profit	576	1,405	2,375	3,288	4,105	5,102

Balance Sheet (Rs mn)	FY21	FY22	FY23	FY24E	FY25E	FY26E
Equity capital	224	224	224	224	224	224
Reserves	8,968	10,278	12,567	15,608	19,444	24,265
Net worth	9,192	10,502	12,791	15,832	19,668	24,490
Minority Interest	-	-	-	-	-	-
Non Current Liabilities	2,346	1,287	1,004	844	989	1,138
Current Liabilities	8,389	5,395	3,525	4,411	5,261	6,279
Other Liabilities(associated with discontinued operations/ assets held for sale)	-	-	-	-	-	-
TOTAL LIABILITIES	19,933	17,185	17,320	21,088	25,918	31,906
Non Current Assets	8,591	8,319	8,443	8,688	8,739	8,493
Fixed Assets	6,256	6,087	6,261	6,498	6,521	6,240
Goodwill	1,071	1,057	1,028	1,028	1,028	1,028
Non Current Investments	789	796	829	828	828	828
Loans						
Non-current assets tax (net)	202	229	104	104	104	104
Deferred Tax Asset	50	38	21	21	21	21
Other Financial Assets	105	19	85	70	70	70
Other Non Current Assets	118	94	117	140	168	202
Current Assets	11,336	8,865	8,876	12,400	17,179	23,414
Current investments		-	191	-	-	-
Inventories	2,502	2,617	2,788	3,623	4,348	5,217
Trade Receivables	5,077	4,151	3,458	4,180	5,017	6,020
Cash and Bank Balances	961	844	823	2,796	5,704	9,744
Other bank balances	453	278	1,280	1,500	1,750	2,000
Short Term Loans and Advances						
Other Financial Assets	1,961	681	86	-	-	-
Other current assets tax (net)						
Other current assets	380	296	250	300	361	433
Other Assets(associated with discontinued operations/ assets held for sale)	-	-	-	-	-	-
TOTAL ASSETS	19,933	17,185	17,320	21,088	25,918	31,906

Cash Flow St. (Rs. mn)	FY21	FY22	FY23	FY24E	FY25E	FY26E
PBT (excluding JV/Associates)	794	1,691	2,966	4,349	5,434	6,758
Add: Dep. & Amort.	521	486	490	448	472	484
Add: Interest Expenses	598	373	133	100	50	-
Operating profit before working capital change	1,913	2,550	3,589	4,897	5,956	7,242
(Inc)/Dec in						
Working capital adjustment	658	(727)	(47)	(906)	(1,003)	(1,204)
Gross cash generated from operations	2,571	1,823	3,542	3,992	4,952	6,038
Direct taxes paid	(237)	(300)	(623)	(1,096)	(1,368)	(1,701)
Others	146	710	181	(169)	42	80
CF from Oper. activities	2,480	2,232	3,100	2,726	3,626	4,417
CF from Inv. activities	(187)	150	(1,668)	(685)	(495)	(204)
CF from Fin. activities	(2,105)	(2,500)	(1,452)	(70)	(223)	(173)
Cash generated/(utilised)	189	(118)	(20)	1,972	2,908	4,040
Cash at start of the year	773	961	844	823	2,796	5,704
Cash at end of the year	961	844	823	2,796	5,704	9,744
Balance sheet	961	844	823	2,796	5,704	9,744
Ratios	FY21	FY22	FY23	FY24E	FY25E	FY26E
OPM	17.77%	20.33%	22.15%	23.04%	23.49%	23.93%
NPM	5.49%	11.51%	15.32%	16.00%	16.66%	17.28%
Tax Rate	29.12%	17.61%	20.79%	25.00%	25.00%	25.00%
Growth Ratios (%)						
Net Sales	-4.02%	16.01%	26.22%	33.00%	20.00%	20.00%
Operating Profit	32.22%	32.77%	37.51%	38.30%	22.36%	22.24%
PBT	316.66%	109.77%	75.82%	46.21%	24.86%	24.28%
PAT	-35.74%	143.81%	69.04%	38.44%	24.86%	24.28%
Per Share (Rs.)						
Net Earnings (EPS)	5.14	12.52	21.17	29.30	36.59	45.47
Cash Earnings (CPS)	9.78	16.85	25.54	33.30	40.80	49.79
Payout ratio	0%	0%	2%	2%	1%	1%
Dividend	0.00	0.00	0.50	0.50	0.50	0.50
Book Value per share (BVPS)	81.93	93.60	114.00	141.11	175.29	218.27
Free Cash Flow	2,509	2,548	3,764	3,412	4,121	4,621
Valuation Ratios						
P/E(x)	184.98	75.87	44.88	32.42	25.96	20.89
P/B(x)	11.60	10.15	8.33	6.73	5.42	4.35
EV/EBIDTA(x)	58.45	43.32	31.21	22.89	18.20	14.33
Div. Yield(%)	-	-	0.05	0.05	0.05	0.05
FCFF Yield(%)	2.35	2.39	3.53	3.20	3.87	4.34
Return Ratios (%)						
ROE	6.27%	13.38%	18.57%	20.77%	20.87%	20.83%
ROCE	15.40%	21.42%	26.49%	24.26%	24.76%	24.95%

Source: Company, Dalal & Broacha Research

Elecon Plant Visit Note

- We visited Elecon Engineering's plant as well as corporate office which is located in Vallabh Vidyanagar in Anand, Gujarat.
- Elecon has one of Asia's largest facility for gear manufacturing & bulk material handling equipment(MHE) manufacturing which is **spread over 650,000 sq. metres.**
- **In-House R&D:** Elecon has state of the art manufacturing facilities with DSIR approved In-House R&D facility for new product development & improvising of existing product designs to suit better for customer needs. The R&D team consists of more than 60 engineers & they use 20+ softwares for design analysis & value engineering
- **Patents applied/ approved :** As on date, Elecon has applied for 5 global patents- 4 product patents & 1 process patent. 2 patents have been approved till date & the remaining three are in still in process for approval.
- **Divisions:** Elecon has separate plants for Gearboxes & gear components, for bulk material handling equipment manufacturing & a separate foundry & fabrication facility for heavy engineering works.
- **Gears Division:** For Gearboxes, gears & components itself they have two separate facilities – one for the standardized/ catalogue gears & a separate facility for engineered & customized gears for their clients. Elecon manufactures a wide variety of gearboxes from planetary, helical, marine & worm gearboxes as well as loose gears, couplings, shafts, etc. For manufacturing these products, Elecon use highly automated machines known as CNC machines - these are imported from Germany. Overall, Elecon has around 150-200 such CNC machines, each costing around Rs 9-10 Cr. Thus overall manufacturing focus is on quality, precision, efficiency & delivering best products for their customers.
- **Key RM used-** chromium steel
- **Standardized/catalogue Gears Division:** In the standardized/ catalogue products plant itself Elecon manufactures the light weight gears (max. 5 tons)- in the range of 50mm diameter – 700 mm diameter – Capacity being ~1000 gearboxes per month. Life of these gearboxes generally in the range of 5 to 7 years. The turnaround time for manufacturing these gears is quite short i.e within 10-15 days of receiving order.
- **Customised Gears/ Engineered Products Division:**The customized & engineered products are built-to-suit customer needs & are heavy-weight in nature varying from 1kg to as large as 115 tons. The turnaround time for these machines is slightly more i.e. around 8-12 months, however these kind of machines are where Elecon enjoys MOAT & is able to command premium margins.

➤ Industry Level Drivers

Steel Sector:

- 1) **Per capita steel consumption** still much lower than China & World Average: India's apparent per capita steel consumption grew at 3.5% CAGR to 81 kg; much lower than China average of 646 kg and world average of 223 kg.
- 2) Steel consumption to grow at **9% CAGR** on the back of government's thrust on infra, supported by private capex by domestic & MNC's in India
- 3) Elecon has some marquee clients for their gears in the steel sector such as **JSW Steel, ArcelorMittal, British Steel, etc.**

Sugar Sector

- 1) In last five years, the government has been able to increase ethanol blending with petrol from 1.5% in 2018 to 11.5% in 2023. The government targets to **increase ethanol blending to 20% levels by 2025-26**, which is expected to result in further capacity addition in next few years.
- 2) Elecon is the **leading Planetary Sugar mill gearboxes manufacturer** with a market share of ~60% and also trying to capture overseas market like in South East Asia.

Defense & Marine Sector

- 1) **Growth in Capital Outlay:** India now has the 3rd largest defense budget. The budget for FY22-23 has been increased by 10% from 4.78 trillion to 5.25 trillion – out of which budget for capex itself is 1.52 trillion. Capex Budget for Navy is ~30% of the full defense capex budget of ~47,590 Crore.
- 2) **Import substitution & rise in Exports** - Ministry of defence has already indigenized 2,736 items till Dec'22 with total import substitution value of Rs. 2,570 crores. This opens up opportunities for Tier-2 & Tier-3 defence goods supplier like Elecon.
- 3) **Cochin Shipyard**- one of the oldest & leading shipbuilders of the country is one of the key clients for Elecon.

Cement Sector

- 1) Demand for cement sector expected to grow on account of a better demand outlook led by government's push towards infra and demand for housing to drive growth.
- 2) The trend in the Cement Industry is shift towards Roller Press Gearboxes for Raw mill & Cement mill application and **Elecon is the only Indian manufacturer for Roller press gearboxes**

Power Sector

- 1) **De-carbonisation as a theme** will require building a **lot of renewable capacity** in future along with gradual addition thermal capacity as well due to the growing power demand in the country. **Higher power generation** will open a greater opportunity for Elecon in the large sized gears segment.
- 2) Elecon is the **leading supplier in India for Coal Pulverizer VRM gearboxes** and also has major share in the FGD business in Power sector.

➤ Company's Growth Levers:

▪ **Dominant market share & growth in Domestic:**

India's steel industry is expected to grow at ~9% CAGR ; cement industry expected to grow at 6-7% CAGR; sugar production expected to grow on account of higher demand for ethanol & power production will be augmenting due to demand for renewable energy. On account of such robust & secular demand coupled with a dominant share of domestic market share of 39-40%, even beyond FY24, management sees potential to grow at a 20%+ growth rate on a Y-o-Y basis.

▪ **Focus on expansion overseas:**

The Indian gears market which is currently ~30Bn-40Bn market – Elecon already commands a 39-40% of the Indian market. Whereas the relevant global addressable market currently for Elecon is ~800Bn with potential to grow to ~1000Bn. Elecon currently earns 30% of its revenue from exports - longer term strategy is to have a domestic-export split of 50-50 by 2030. Elecon has already built a brand for itself in overseas market especially Europe, through its acquisition of Radicon & Benzler , however currently it has less than 1% market share of the overseas market. Recently in Q1FY24 , they also won an order.

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