

Amber Enterprises India Ltd (AEL)

**- Strong demand & Industry leadership to drive
growth**

Amber Enterprises India Ltd (AEL)

08-11-2018

Recommendation	:	Buy
CMP	:	Rs 864
Sector	:	Misc

NSE Code	:	AMBER
BSE Code	:	540902

Financial break up

Market Cap (Rs. Cr)	:	2733
EPS (FY18)	:	19.81
PE	:	43.61
Face Value	:	Rs.10/-

Share Holding Pattern:

Promoters	:	44.02
Others	:	55.98

Background: AEL is a market leader in the RAC OEM/ODM industry in India with a market share of 55.4% in terms of volume in Fiscal 2017. They are a one-stop solutions provider for the major brands in the RAC industry and currently serve eight out of the 10 top RAC brands in India. The company has about 10 manufacturing facilities with a total installed capacity to manufacture up to 1.59 million ODUs, 1.37 million IDUs and 0.59 million WACs annually. The company's leadership position can be attributed to its experience in the development and manufacturing of RACs and components and their ability to excel in measurable quality, cost, delivery and technology.

Industry Leader

AEL is the market leader in the RAC OEM/ODM industry in India with a market share of 55.4% in terms of volume in Fiscal 2017 .Further, their share of the overall RAC market in India in terms of volumes has grown from 14.7% in Fiscal 2015 to 19.1% in Fiscal 2017.

Favorable industry trend - Growth Driver

AEL is in a sweet spot, as the RAC industry is growing at 10%+CAGR. The growth of this industry is driven by the increase in disposable income, humid climate of India, urbanization and easy consumer financing. The RAC volumes are expected to increase from 4.7 million units in FY2017 to reach 8.6 million units by FY2022E

Strong relationship with leading brands

AEL has strong and established relationships with their customers, which includes eight out of the 10 top RAC brands in India. AEL's key customers include leading RAC brands such as Daikin, Hitachi, LG, Panasonic, Voltas and Whirlpool. AEL's customers command around 75% share in the Indian RAC market.

Outlook & Valuation

We recommend a **Buy** on AEL for long term investors. Given the Industry leadership , strong track record, Favourable industry trends, Increasing margins, and strong relationship with leading brands are key positives for the stock. At the CMP of INR 864, the stock trades at 43.61x EPS of FY18.The key risks to the business include Client Concentration risk, Slowdown in GDP growth which will impact consumption spend and change in technology.

Investment Arguments

Company Profile: AEL is a market leader in the RAC OEM/ODM industry in India with a market share of 55.4% in terms of volume in Fiscal 2017 .They are a one-stop solutions provider for the major brands in the RAC industry and currently serve eight out of the 10 top RAC brands in India.

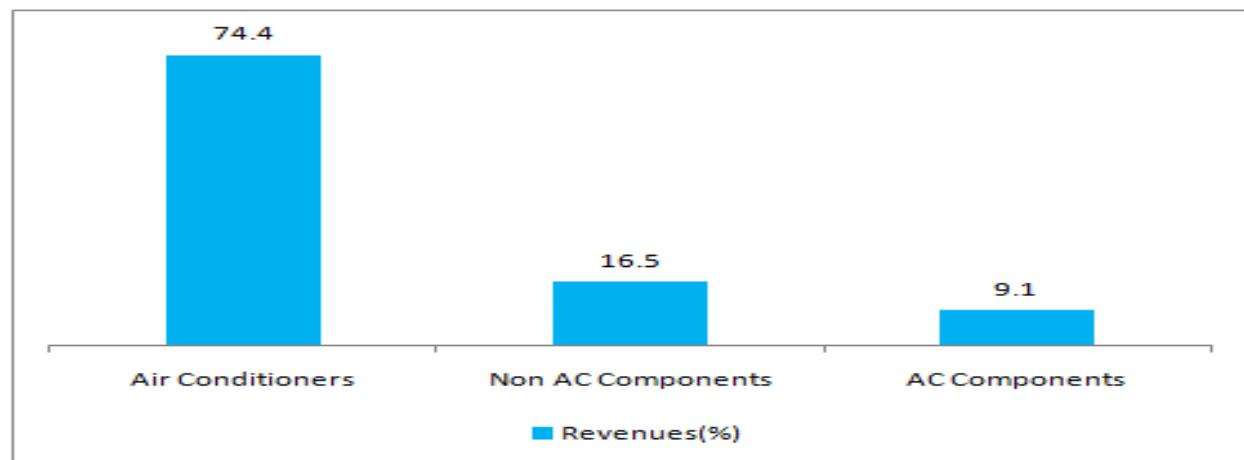
AEL has a diversified product portfolio which is discussed below:

RACs: AEL designs and manufactures complete RACs including window air conditioners (“WACs”) and indoor units (“IDUs”) and outdoor units (“ODUs”) of split air conditioners (“SACs”) with specifications ranging from 0.75 ton to 2 ton, across energy ratings and types of refrigerant. They also design and manufacture Inverter RACs on ranging from 1 ton to 2 ton.

RAC Components: AEL also manufactures critical and reliability functional components of RACs such as heat exchangers, motors and multi-flow condensers. We manufacture other RAC components such as sheet metal components, copper tubing and injection molding components.

Other Components: AEL manufacture components for other consumer durables and automobiles such as case liners for refrigerator, plastic extrusion sheets for consumer durables and automobile industry, sheet metal components for microwave, washing machine tub assemblies and for automobiles and metal ceiling industries.

AEL is focused on consistently upgrading the technology used in their products as well as the processes used in manufacturing them through their research and development (“R&D”) efforts. The company has a dedicated R&D centre located at their Rajpura facility. The R&D centre is equipped with a psychometric lab which is accredited by National Accreditation Board for Testing and Calibration Laboratories (“NABL”) with ISO/IEC 17025:2005 certification and facilities for 3D modelling, quality and product testing and a dedicated team. Through their R&D and innovation capabilities, backed by an in-house tool room, the company has successfully designed and developed a portfolio of wide ranging RACs and components. AEL has the ability to manufacture most of their products from the concept and design stage till the final delivery thereby covering the entire manufacturing value chain.

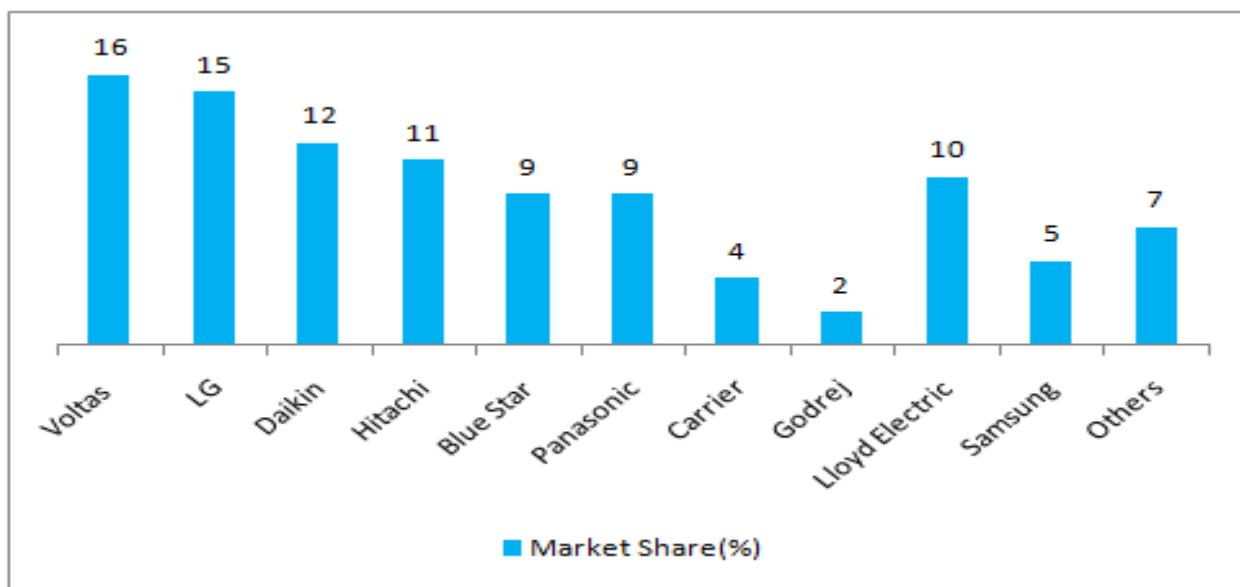


Industry Leader

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Over the years, the company has demonstrated its ability and expertise in manufacturing RACs and components that has enabled them to become a trusted solutions provider to major RAC brands operating in India. The company has about 10 manufacturing facilities with a total installed capacity to manufacture up to 1.59 million ODUs, 1.37 million IDUs and 0.59 million WACs annually. The company's leadership position can be attributed to its experience in the development and manufacturing of RACs and components and their ability to excel in measurable quality, cost, delivery and technology.

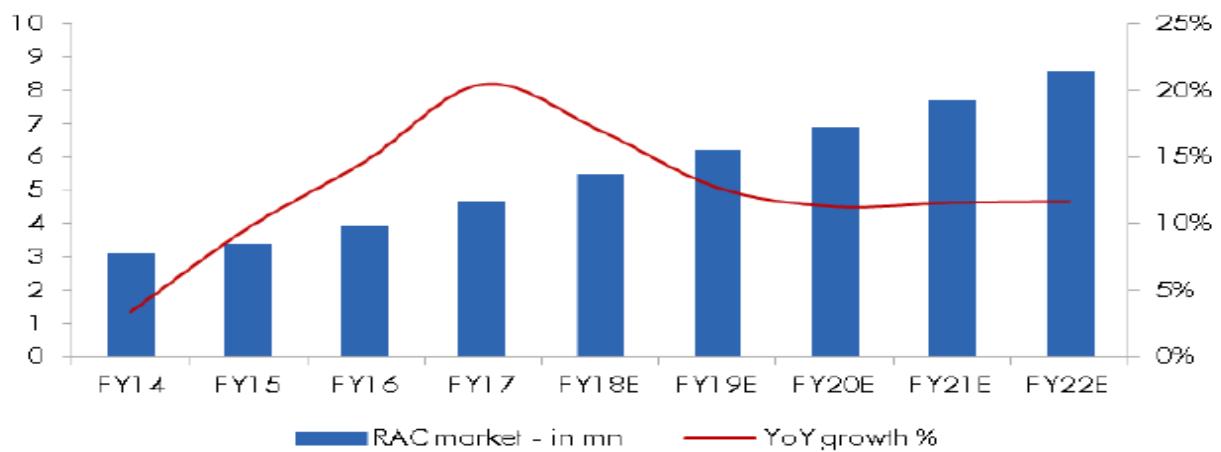
AEL has the capability to develop, design and manufacture models of RACs across energy ratings specified by the Bureau of Energy Efficiency, Ministry of Power, GoI ("BEE") and by using various types of refrigerant including green refrigerants. The company also develops and manufactures complete WAC and SAC kits and components according to the designs and specifications required by the customers and is also one of the few Indian manufacturers with the capability to design and manufacture Inverter RACs.



Favorable industry trend

AEL is in a sweet spot, as the RAC industry is growing at 10%+CAGR. The growth of this industry is driven by the increase in disposable income, humid climate of India, urbanization and easy consumer financing. The RAC volumes are expected to increase from 4.7 million units in FY2017 to reach 8.6 million units by FY2022E.

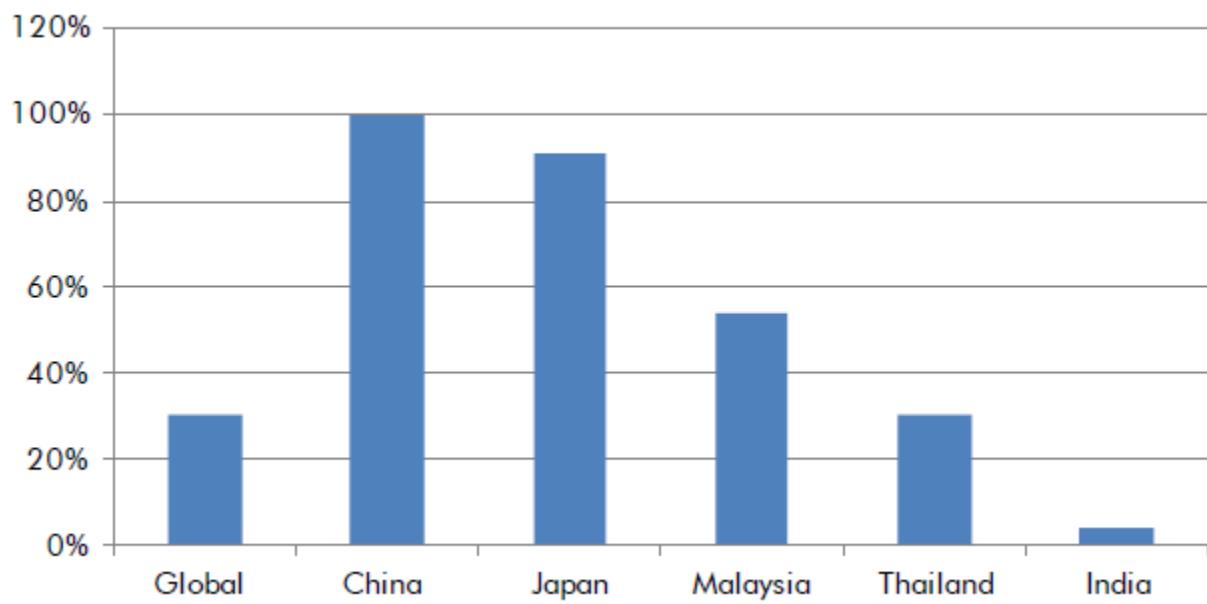
ACs volume growth to remain buoyant



Lower penetration provides opportunity

Due to the current low penetration of 4% versus (53% in China/ global average- 30%), the Indian RAC market presents huge opportunity for players to garner larger share of the market. Viewed as a luxury product in the recent past, the sweltering and longer summers in the country have led to creation of new demand for RACs not only in the larger cities, but also in Tier II/III cities amid better affordability.

RAC penetration level across countries



One stop solution provider

AEL's product development expertise and capabilities in the manufacturing of RACs and components, has enabled them to become a one-stop solutions provider in India for the RAC industry. In addition to designing and manufacturing complete WAC, IDUs and ODUs, the company offers their customers manufacturing solutions ranging from critical components such as heat exchangers, multi-flow condensers and motors to non-critical components such as sheet metal and injection molding. In terms of bill of material, depending on the model of RAC, they manufacture up to 49% of the ODUs, 62% of the IDUs and 54% of WAC, which includes most of the critical components except compressors, which are largely imported for the RAC industry in India.

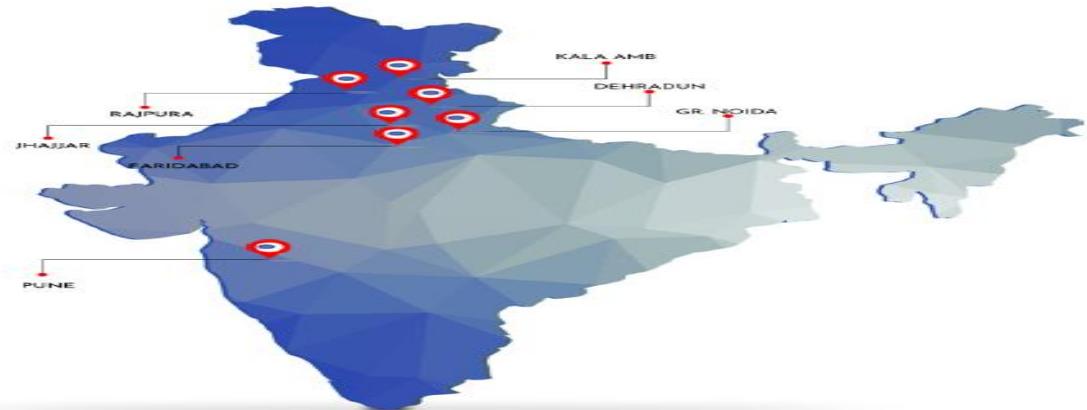
AEL has the capacity to offer product development and manufacturing solutions from designing, tooling and validating to final assembling and testing. Most of the company's operations are backward-integrated and the processes are carried out inhouse. This backward integration gives the company flexibility to control their manufacturing processes and reduces dependence on external suppliers. This helps to make them to be a consistent and reliable OEM/ODM supplier. AEL's backward integrated capability to manufacture most of the critical components to be used in their manufacturing chain which makes them uniquely competitive in the RAC manufacturing industry in India.

Strong relationship with leading brands

AEL has strong and established relationships with their customers, which includes eight out of the 10 top RAC brands in India. AEL's key customers include leading RAC brands such as Daikin, Hitachi, LG, Panasonic, Voltas and Whirlpool. AEL's customers command around 75% share in the Indian RAC market. AEL provides their customers with a range of additive manufacturing solutions at their doorsteps. Majority of their top 10 customers have been associated with them for more than five years and these long term relationships have enabled them to understand and cater to diverse requirements of such customers and to develop new products with and for these customers.

Product approval cycle, especially for leading brands, can be as long as 2-3 years for certain critical components. Further, acquisition of customers in the RAC industry requires persistent and continued investment of time, effort and capital. AEL has gained the confidence of their customers by initially supplying certain components to their customers, and then moving to reliability functional components and eventually to complete RACs. AEL's established relationships with existing customers also presents them with cross selling opportunity. While maintaining and strengthening their relationships with the existing customers, over the last three years the company has also been successful in acquiring large MNC customers such as Daikin and Hitachi.

AEL strategically sets up their manufacturing facilities in proximity to their customers, which allows them greater interaction and gives them the ability to respond quickly to the needs their customers. In addition, locating their manufacturing facilities near customers' production centers reduces logistical and operating costs, which allows the company to produce cost-competitive products for their customers. Given their experience in supplying components to the majority of leading international and domestic RAC brands in India, the company is well positioned to seek new clients in India and across the globe.



Manufacturing Locations

Economies of Scale

AEL's multiple manufacturing locations allow them optimal utilisation of facilities and enable them to distribute manufacturing across them. This helps them to ease the pressure of seasonality and simultaneous demand schedules of multiple customers. Further, their assembly lines are flexible and can shift from assembling WACs to ODUs of SACs within a short time. The flexibility of their assembly lines provide them with a major competitive advantage as they are able to cater to changes in market demands in an efficient manner. AEL's scale provides them with greater resources to support their fixed costs, such as R&D expenses, and permits the use of shared services to eliminate duplicative business functions and administrative expenses. The company believes that this also helps them to compete with imports from countries such as China as they are able to make more efficient deliveries to their customers.

The large scale of production has also strengthened their relationship with raw material suppliers and provided them better insight into the markets for procuring material. AEL has a centralised system across their manufacturing facilities for procurement of raw material, ensuring cost efficiency and timely delivery of supplies. This has also resulted in reducing the overall cost of production.

Expanding domestic customer base and growing exports

The RAC demand in India is growing, owing to low penetration of RACs, rising disposable income, increased urbanisation, changing lifestyle trends, longer hot weather season and shortening of replacement cycle. The Indian RAC market volumes are expected to grow at a CAGR of 12.8% from Fiscal 2017 to Fiscal 2022.

Such growth may result in expansion of existing RAC brands as well as entry of new consumer durable brands in the RAC segment. Further, the management believes that this growth will require RAC brands to focus on marketing aspects and will result in greater share of manufacturing being outsourced to OEM/ODM. In Fiscal 2017, 34% of the total value of Indian RAC market was catered by OEM/ODM players which is anticipated to grow to 56% by Fiscal 2022. This provides the company with an opportunity to increase their sales and expand their customer base. Moreover, being among few players with complete ODM offering in the RAC segment in India and with their experience in providing customer-centric additive manufacturing solutions, the company believes they are well placed to tap into this growth.

Further, with 'Make in India' initiative of GoI and the growing advantage of domestic manufacturers compared to import markets due to lower lead time and working capital cycle, greater flexibility to adjust with market trends and improving cost competitiveness, the company believes that they are well poised to grow their domestic and export sales. The company also seeks to expand their global reach through increased customer acceptance of their products in international markets. As the globalisation trend continues and barriers to trade in various markets are reduced across the world, the management believes that an export oriented strategy offer them business advantages. Indian manufacturing is increasingly becoming competitive with China, coupled with the strong relationship with reputed international RAC brands will provide them with opportunities to further grow their export sales.

AEL currently exports to Saudi Arabia, Oman, Sri Lanka, Nigeria and Maldives. AEL intends to leverage the low cost advantages of manufacturing in India and aim to initiate RACs exports into others countries in Middle East, South and South East Asia as well as Europe. India's geographic location helps in exporting competitively to these countries, as compared to other regional hubs such as China. An increase in their exports will also lower seasonal volatility of their business leading to higher capacity utilisation of their manufacturing facilities. Further, the export revenue will act as a natural foreign currency hedge against imports of several components.

Key-Risks

Client concentration: AEL's business is dependent on certain principal customers and the loss of or a significant reduction in their purchases could adversely affect its business. Its top five and 10 customers contributed 74.8% and 92.5% respectively to sales and any slowdown in sales could adversely impact the company.

Adverse trend in OEM/ODM: In recent years, RAC brands have increasingly outsourced the manufacturing of their products to OEM/ODM players like AEL. However, there can be no assurance that they will continue to do so in the future.

Slowdown in GDP Growth: Any slowdown in the economy is likely to result in reduction in consumer spending which will impact the company's growth and profitability.

Changing preferences, advancement in technology: The markets in which company's customers compete are characterized by consumers and their rapidly changing preferences, advancement in technology and other related factors including lower manufacturing costs. Hence, the company may be affected by any disruptions in the industry.

Financials

P&L

Consolidated Profit & Loss account(Rs.Cr)	Mar '14	Mar '15	Mar '16	Mar '17	Mar '18
Income					
Sales Turnover	1,014.50	1,281.02	1,145.20	1,735.81	2,171.51
Excise Duty	41.12	50.76	56.17	83.95	43.42
Net Sales	973.38	1,230.26	1,089.03	1,651.86	2,128.09
Other Income	6.32	6.2	3.09	8.73	9.06
Stock Adjustments	-4.06	5.64	6.4	27.51	-16.78
Total Income	975.64	1,242.10	1,098.52	1,688.10	2,120.37
Expenditure					
Raw Materials	793.84	1,019.03	864.9	1,398.71	1,752.06
Power & Fuel Cost	14.07	17.91	14.89	20.42	21.64
Employee Cost	32.03	33.53	36.53	43.66	49.77
Miscellaneous Expenses	54.51	62.88	65.37	86.05	104.29
Total Expenses	894.45	1,133.35	981.69	1,548.84	1,927.76
Operating Profit	74.87	102.55	113.74	130.53	183.55
PBDIT	81.19	108.75	116.83	139.26	192.61
Interest	32.27	42.79	53.25	63.52	53.83
PBDT	48.92	65.96	63.58	75.74	138.78
Depreciation	18.42	25.57	30.86	40.11	49.02
Profit Before Tax	30.5	40.39	32.72	35.63	89.76
PBT (Post Extra-ord Items)	30.5	40.39	32.72	35.63	89.76
Tax	8.31	11.63	8.61	13.56	27.1
Reported Net Profit	22.2	28.77	24.1	22.14	62.31
Earning Per Share (Rs)	10.23	13.26	11.11	9.3	19.81

Balance Sheet

Consolidated Balance Sheet(Rs.Cr)	Mar '14	Mar '15	Mar '16	Mar '17	Mar '18
Sources Of Funds					
Total Share Capital	21.7	21.7	21.7	23.81	31.45
Equity Share Capital	21.7	21.7	21.7	23.81	31.45
Reserves	187.78	216.83	240.93	338.85	861.31
Networth	209.48	238.53	262.63	362.66	892.76
Secured Loans	117.61	147.04	161.42	374.14	105.51
Unsecured Loans	139.67	159.65	165.2	0	0
Total Debt	257.28	306.69	326.62	374.14	105.51
Minority Interest	3.66	0	0	0	0
Total Liabilities	470.42	545.22	589.25	736.8	998.27
Application Of Funds					
Gross Block	420.33	509.74	616.84	704.63	893.37
Less: Accum. Depreciation	71.71	91.52	116.38	147.86	183.35
Net Block	348.62	418.22	500.46	556.77	710.02
Capital Work in Progress	52.17	51.85	35.65	21.34	29.75
Investments	0	0	0	0	5.71
Inventories	174.19	189.43	225.77	268.5	395.65
Sundry Debtors	158.43	231.59	247.95	310.09	378.57
Cash and Bank Balance	50.64	28.9	18.36	35.24	133.81
Total Current Assets	383.26	449.92	492.08	613.83	908.03
Loans and Advances	77.03	85.85	86.81	58.8	75.02
Total CA, Loans & Advances	460.29	535.77	578.89	672.63	983.05
Current Liabilities	382.5	452.15	519.22	510.02	725.24
Provisions	8.16	8.48	6.52	3.91	5.02
Total CL & Provisions	390.66	460.63	525.74	513.93	730.26
Net Current Assets	69.63	75.14	53.15	158.7	252.79
Total Assets	470.42	545.21	589.26	736.81	998.27

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