

24 December 2020

## Amber Enterprises

*Scale-up measures further supported by PLI; maintaining a BUY*

Rating: **Buy**

Target Price: Rs3,012

Share Price: Rs2,312

Amber is set to emerge as the primary beneficiary of the government's steps on air-conditioner imports. The industry estimates ~ 2.7m units are imported, of which ~70% are filled with refrigerants. After the notification, Amber added four OEM clients and is adding a few more. The full benefits of an expanding client list will be visible in FY22. With its two new factories expected to be commissioned by FY22, Amber can benefit from further policy support in the form of production-linked incentives (PLI) for components. We raise our estimates significantly and move our target to 30x FY23e EPS (from SOTP earlier), taking into account synergy/interlinks of the integrated model.

**Industry growth to be ~15%, Amber to outperform:** The room AC industry in 2020 was characterised by chaos and uncertainty with regard to availability of critical components sourced from China and higher international logistics cost due to Covid-19. The situation is now turning normal and we expect re-stocking to be strong in Q4, for next year's summer.

**Expanding capacity to benefit from policy support:** Because of strong policy support, Amber will be setting up two factories to benefit from added demand. One plant would be set up near Pune in Maharashtra; the other in South India. On commissioning of these plants, Amber's capacity to assemble IDUs and ODU's can increase by 2m (from 4.5m now) along with greater capacity for components.

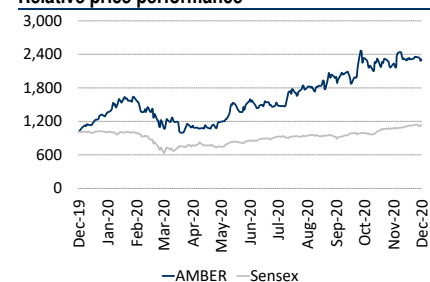
**Valuation.** We have raised our FY21e and FY23e to factor in greater volumes as the two factories would be operational by Q4FY22. We now model FY21-FY23 revenue/PAT CAGRs of 36%/86%, resulting in RoCE (after tax) rising to 13.5% (from 6.6% in FY21). We value the stock at a consolidated PE of 30x FY23 EPS of Rs100.4 (from SOTP earlier). We maintain a Buy. **Risks:** (a) inability to ramp up component manufacturing; (b) predatory pricing and longer credit terms being offered by global vendors.

Key data	AMBER IN / AMBE.BO
52-week high / low	Rs2545 / 921
Sensex / Nifty	46444 / 13601
3-m average volume	\$7.7m
Market cap	Rs78bn / \$1055.1m
Shares outstanding	34m

Shareholding pattern (%)	Sep'20	Jun'20	Mar'20
Promoters	40.3	44.0	44.0
- of which, Pledged	-	-	-
Free float	59.7	55.9	56.0
- Foreign institutions	25.4	13.3	12.4
- Domestic institutions	9.5	6.5	7.2
- Public	24.8	36.2	36.4

Estimates revision (%)	FY21e	FY22e
Sales (\$)	8	12
EBITDA	6	5
Net Profit	31	(5)

### Relative price performance



Source: Bloomberg

Key financials (YE: Mar)	FY19	FY20#	FY21e	FY22e	FY23e
Sales (Rs m)	27,520	39,628	37,646	51,785	69,252
Net income (Rs m)	937	1,584	981	2,190	3,383
EPS (Rs)	29.8	50.4	29.1	65.0	100.4
PE (x)	27.9	45.9	78.4	35.1	22.7
EVEBITDA (x)	13.1	24.2	31.2	16.8	12.2
PBV (x)	2.6	6.4	4.7	4.2	3.5
RoE (%)	10.0	15.0	7.1	12.6	16.8
RoCE (%) (post tax)	8.6	12.3	6.6	11.0	13.5
Dividend yield (%)	-	0.1	-	-	-
Net debt/equity (x)	0.2	0.3	0.3	0.3	0.3

Source: Company, Anand Rathi Research # - Figures are not comparable on YoY basis, post acquisition of Sidhwal

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## Quick Glance – Financials and Valuations

**Fig 1 – Income statement (Rsm)**

Year-end: Mar	FY19	FY20 (#)	FY21e	FY22e	FY23e
Net revenues (Rs m)	27,520	39,628	37,646	51,785	69,252
Growth (%)	26.7	44.0	-3.0	37.6	33.7
Direct costs	23,132	33,017	31,527	42,932	57,557
SG&A	2,259	3,518	3,598	4,073	5,179
<b>EBITDA</b>	<b>2,129</b>	<b>3,093</b>	<b>2,520</b>	<b>4,780</b>	<b>6,517</b>
EBITDA margins (%)	7.7	7.8	6.7	9.2	9.4
- Depreciation	623	848	991	1,295	1,387
Other income	99	82	287	198	256
Interest expenses	246	419	538	697	801
PBT	1,359	1,907	1,280	2,986	4,584
Effective tax rate (%)	30.3	13.9	22.1	26.0	26.0
+ Associates / (Minorities)	11	57	16	29	57
Net income	937	1,584	981	2,190	3,383
Adjusted income	937	1,584	981	2,190	3,383
WANS	31	31	34	34	34
FDEPS (Rs/ sh)	29.8	50.4	29.1	65.0	100.4
FDEPS growth (%)	28.6	69.1	-37.8	123.2	54.5
Gross margins (%)	15.9	16.7	16.3	17.1	16.9

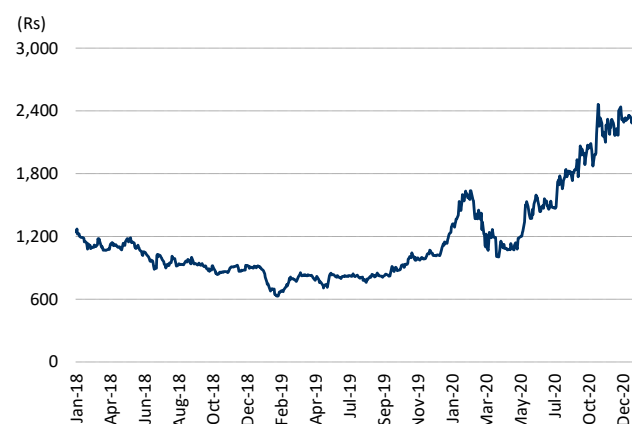
**Fig 3 – Cash-flow statement (Rsm)**

Year-end: Mar	FY19	FY20#	FY21e	FY22e	FY23e
PBT	1,359	1,907	1,280	2,986	4,584
+ Non-cash items	787	1,418	1,241	1,794	1,933
Oper. prof. before WC	2,146	3,325	2,520	4,780	6,517
- Incr. / (decr.) in WC	-2,477	44	-1,636	-2,625	-2,605
Others incl. taxes	-300	-488	-282	-767	-1,144
Operating cash-flow	-630	2,882	602	1,389	2,767
- Capex (tang. + intang.)	-1,182	-3,083	-2,515	-2,600	-1,300
Free cash-flow	-1,812	-201	-1,913	-1,211	1,467
Acquisitions					
- Div.(incl. buyback & taxes)	-	-121	-	-	-
+ Equity raised	-	-	4,000	-	-
+ Debt raised	1,176	1,209	930	990	1,223
- Fin investments	41	-197	-1,400	-	-
- Misc. (CFI + CFF)	-234	-439	-248	-499	-546
Net cash-flow	-829	250	1,370	-720	2,144

Source: Company, Anand Rathi Research

(# - Figures are not comparable on YoY basis, post acquisition of Sidhwal)

**Fig 5 – Price movement**



Source: Bloomberg

**Fig 2 – Balance sheet (Rsm)**

Year-end: Mar	FY19	FY20 (#)	FY21e	FY22e	FY23e
Share capital	314	314	337	337	337
Net worth	9,861	11,284	16,265	18,456	21,839
Debt	2,529	3,790	4,135	5,125	6,348
Minority interest	190	348	364	393	450
DTL/(Assets)	459	808	810	810	810
<b>Capital employed</b>	<b>13,040</b>	<b>16,229</b>	<b>21,575</b>	<b>24,784</b>	<b>29,447</b>
Net tangible assets	6,511	7,475	8,597	10,073	10,165
Net intangible assets	915	2,361	2,198	2,027	1,849
Goodwill	669	1,223	1,223	1,223	1,223
CWIP (tang. & intang.)	337	143	122	122	122
Investments (strategic)	21	23	1,423	1,423	1,423
Investments (financial)	-	-	-	-	-
Current assets (ex cash)	14,808	16,583	18,503	25,266	33,622
Cash	447	1,202	2,571	1,851	3,996
Current liabilities	10,668	12,780	13,064	17,202	22,953
Working capital	4,140	3,803	5,439	8,064	10,669
<b>Capital deployed</b>	<b>13,040</b>	<b>16,229</b>	<b>21,574</b>	<b>24,784</b>	<b>29,447</b>
Contingent liabilities	961	1,192	-	-	-

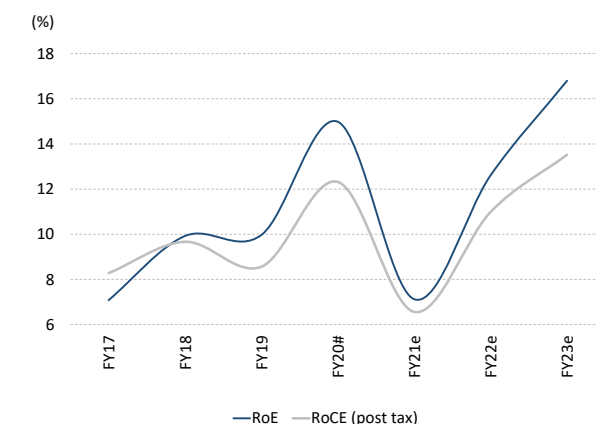
**Fig 4 – Ratio analysis**

Year-end: Mar	FY19	FY20 (#)	FY21e	FY22e	FY23e
P/E (x)	27.9	45.9	78.4	35.1	22.7
EV / EBITDA (x)	13.1	24.2	31.2	16.8	12.2
EV / Sales (x)	1.0	1.9	2.1	1.5	1.1
P/B (x)	2.6	6.4	4.7	4.2	3.5
RoE (%)	10.0	15.0	7.1	12.6	16.8
RoCE (%) - after tax	8.6	12.3	6.6	11.0	13.5
RoIC	8.9	13.3	7.4	11.9	15.6
DPS (Rs / sh)	-	1.6	-	-	-
Dividend yield (%)	-	0.1	-	-	-
Dividend payout (%) - incl. DDT	-	3.2	-	-	-
Net debt / equity (x)	0.2	0.3	0.3	0.3	0.3
Receivables (days)	104	79	85	85	85
Inventory (days)	74	60	80	80	80
Payables (days)	125	102	105	100	100
CFO : PAT %	-67.3	182.0	61.4	63.4	81.8

Source: Company, Anand Rathi Research

(# - Figures are not comparable on YoY basis, post acquisition of Sidhwal)

**Fig 6 – Return ratio to expand going forward**

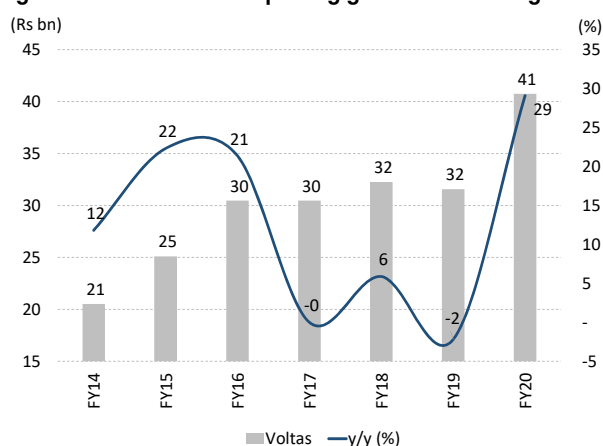


Source: Company

## Management call takeaways:

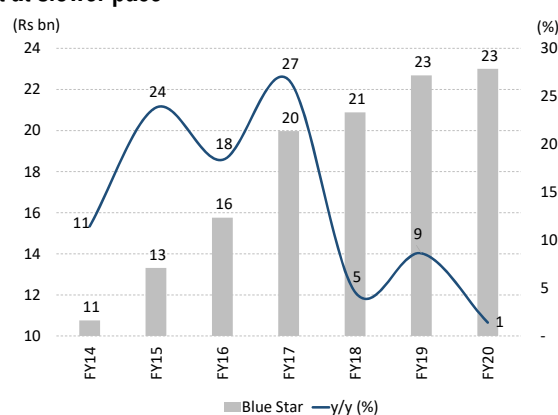
**Overall industry growth expected to be around 15%:** The overall room AC industry last year was characterised by chaos and uncertainty with regard to availability of critical components sourced from China and greater international logistics cost as the impact of the Covid-19 virus was being felt. While the situation turned normal gradually, the trade channel continued to be loaded with inventory, expected to be cleared in the rest of CY20 before re-stocking for next year's summer. Despite challenging times, Amber expects overall industry growth in the summer of CY21 to be around 15%, as most OEMs are geared to make the most of opportunities then arising.

**Fig 7 – Voltas has been reporting growth in UCP segment**



Source: Company, Anand Rath Research

**Fig 8 – Blue Star has also been growing in product segment but at slower pace**

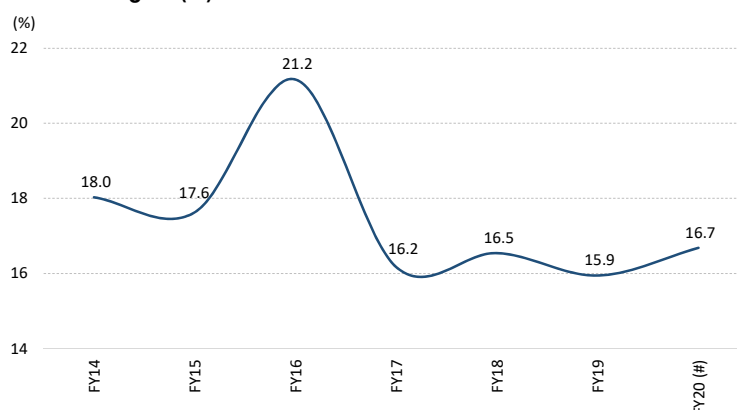


Source: Company, Anand Rath Research

**Energy rating revision postponed to Jan'22:** The Bureau of Energy Efficiency (BEE) has revised the date for implementation of energy-rating norms for air conditioners to Jan'22 (earlier Jul'20). Further details regarding the revised BEE norms are now expected around Jun-Jul'21. Based on this, production can be planned for the CY22 summer. Further updates need to be watched, after the CY21 summer.

**Rising commodity prices to be passed on in phased manner:** Amber expects to pass on the impact of rising commodity prices to its OEMs in a phased manner. Typically, cost increases are received from OEMs with a quarterly lag, a standard operating practice.

**Fig 9 – Gross margins (%)**

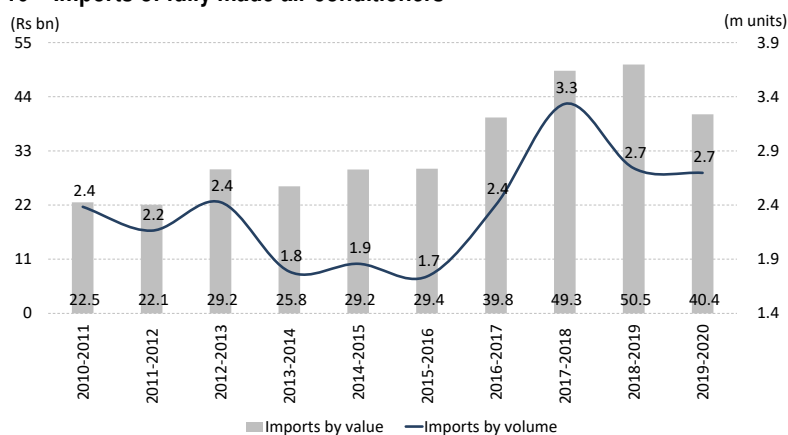


Source: Company, Anand Rath Research

**Gas-filling solutions aids on-boarding of OEMs:** The recent notification of the Indian government bans imports of air conditioners filled with refrigerant gases. This step was taken primarily to put import entry barriers on countries with whom India has signed free-trade agreements (FTA), as import duties cannot be increased as per World Trade Organisation (WTO) regulations.

For FY11–FY20, imports of fully-made air conditioners in India recorded a 7% CAGR. In value, imports of fully-made ACs in India were Rs40.4bn at end-FY20 down from a peak of Rs50.5bn in FY19. In volumes, 2.7m room ACs were imported in FY20, flat y/y (vs peak imports of 3.3m units in FY18).

**Fig 10 – Imports of fully made air conditioners**

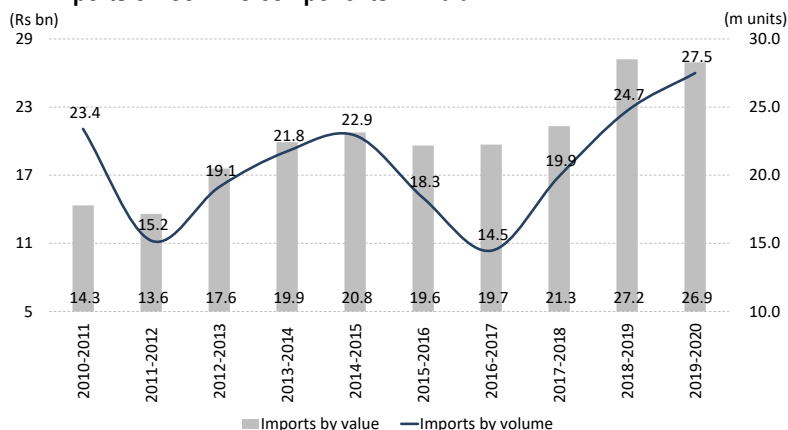


Source: Ministry of Commerce, Anand Rathi Research

Amber is offering gas-filling solutions to several OEMs which were importing fully-made machines to India. It has already on boarded four OEMs for gas-filling solutions, while talks are underway with two more OEMs. Courtesy its size and scale, Amber aims at the lion's share of the gasification requirements of these OEMs.

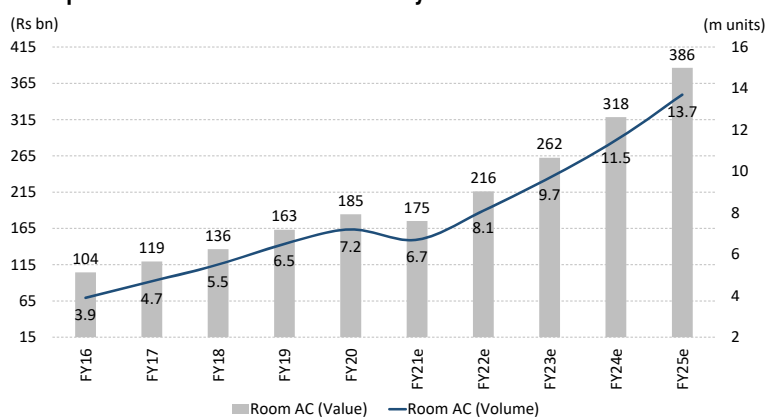
Effective from summer CY22, OEMs which were dependent primarily on imports would now have to set up factory or get it manufactured via contract manufacturers. This augurs well for Amber as it can offer components to these OEMs for the new factories and offer fully made machines to them, thereby widening its customer base.

**Well-designed policy framework for import substitution destroys economics of imports:** The government's policy to lower imports and encourage make in India seems to be finalised on sound economic policies and is being implemented in phased manner. After creating entry barriers to fully-made room ACs, the focus is now on creating an entire eco system of components in India, which might provide incentives for manufacturing and exports of components, like PLI is being offered for mobile phones. Proposed incentives can compel OEMs to shift procurement to India and can lead to global supply-chain rebalancing. The government's focus on increasing customs duties on components can further destroy economic viability of component imports. Longer credit terms provided by Chinese contract manufacturers can pose the biggest risk to contract manufacturer like Amber. However, incentives for component manufacturing and exports can negate that risk.

**Fig 11– Imports of room AC components in India**

Source: Ministry of Commerce, Anand Rathi Research

**Analysing the domestic market for components in India:** The potential market for split air-conditioner components in India (excl. compressors and sundry assembly items) in FY22 is Rs61.6bn and can clock a 15% CAGR resulting in a potential market of Rs188.4bn by FY30, based on steady price (excl. the inflationary impact of commodities). Amber is well placed to be dominant in this segment based on its all-India based manufacturing capabilities and empanelment with leading OEMs. It is well placed to cross-sell components to existing OEMs for other categories of white goods, thereby, leveraging its existing OEM relationships, which can further expand its addressable market.

**Fig 12 – Expected increase in overall industry size for room ACs**

Source: Company reports, Frost &amp; Sullivan

**New plants likely to benefit from favourable government policy for component manufacturing:** After putting barriers to import of air conditioners, the government is keen on establishing a component manufacturing ecosystem under production-linked incentive schemes (PLI). A policy framework can be expected to be released in Q1CY21. Further details need to be watched. Amber is in the process of setting up two plants to diversify and expand its manufacturing capabilities, one near Pune in Maharashtra, the other in south India. Capex would be ~Rs2.7bn and funds have been raised via the recently concluded QIP.

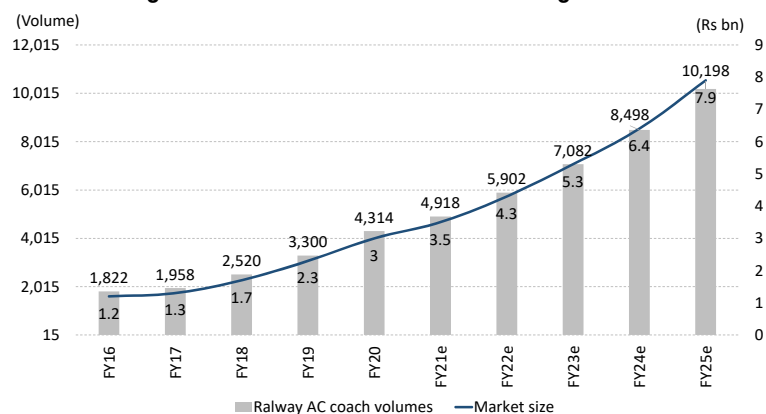
**Sidwal scaling up for coming opportunities:** The pending order book with Sidwal at end-Q2FY20 was Rs3.5bn, to be executed over the next 18-24 months. The outlook for Sidwal is robust based on:

- Increase in the metro rail network and strengthening of the existing

network (Sidwal's scope of work in metro tenders can be around 2% of the tender value).

- Greater focus of The Indian Railways on air-conditioning passenger coaches. The Railways' proposal to have all coaches air-conditioned for trains running at over 120km per hour can augur well for Sidwal. Amber is already supplying air-conditioning systems to coaches of Vande Bharat trains.
- Sidwal has launched new models for air conditioning for buses, expected to be rolled out in FY21.

**Fig 13 – Increasing volume of air conditioned coaches augurs well for Amber**



Source: Company reports, Frost & Sullivan

**All growth levers to deliver in FY23 and FY24:** To maximise its growth outlook Amber has been building multiple levers, which are expected to deliver in FY23 and FY24. Key levers would include:

- After becoming dominant in the domestic market, it is strengthening its customer base by offering gas-filling solutions, which can aid on - boarding OEMs as they will have to procure from Indian manufacturers for the summer of CY22 or set up their assembly plants which would aid component sales.
- Amber's export markets targeted are primarily American and Saudi Arabian. It is also in process of being integrated in the global supply chain of leading OEMs. Exports of components have started and can expand rapidly once the testing phase is over. Initial orders can be expected in FY22/FY23. Amber is well placed to cross-sell its components to its OEMs for other categories globally, which can be a major growth lever.
- Exports of indoor units (IDUs), outdoor units (ODUs) can also pick up by FY23, as reliability tests are underway and take longer for fully-made units.

## Valuation & Outlook

### Estimates revised; maintaining our Buy rating with a higher TP:

After the management interaction, we have increased estimates for FY21 and FY23 to factor in greater volumes as two new factories would be operational by Q4FY22. Increase in estimates for FY21 can be attributed to increase in other income as we have also incorporated the impact of capital infusion of Rs4bn, after the recent QIP. Amber has acquired remaining stake from the promoter of Sidwal. As a result, Sidwal is now a fully-owned subsidiary of Amber. Adjustments with regard to this are being incorporated by us.

After increasing estimates for FY23, we now model revenue/PAT to register 36%/ 86% CAGRs over FY21–FY23, resulting in post-tax RoCE rising from 6.6% to 13.5%. We have change the method of valuing the stock from sum-of-parts (the standalone business and each subsidiary separately) to PE of 30x being assigned to the FY23e consolidated EPS of Rs100.4. Thus we derive a TP of Rs3,012 (30x FY23e EPS of Rs100.4) and maintain our Buy rating on the stock. At the CMP of Rs2,312, the stock trades at 35x/23x its FY22e/FY23e EPS of Rs65/100.

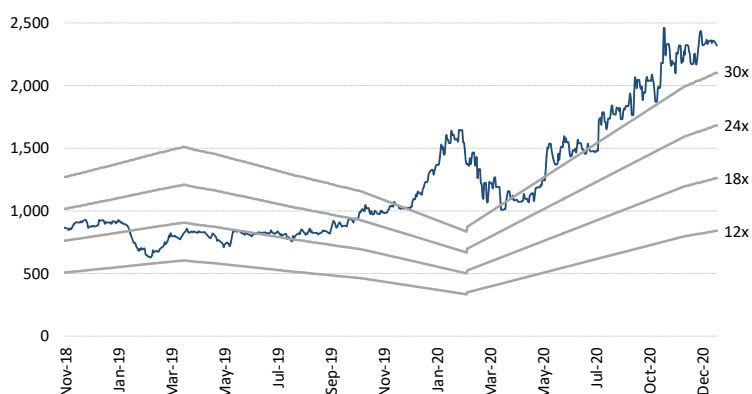
**Fig14 – Change in estimates**

(Rsm)	Revised Estimates			Old Estimates			Change (%)		
	FY21e	FY22e	FY23e	FY21e	FY22e	FY23e	FY21e	FY22e	FY23e
Revenue	37,646	51,785	69,252	34,920	46,063	60,152	8	12	15
EBITDA	2,520	4,780	6,517	2,375	4,560	5,775	6	5	13
EBITDA-(%)	6.7	9.2	9.4	6.8	9.9	9.6			
Dep	991	1,295	1,387	956	1,045	1,295	4	24	7
EBIT	1,530	3,485	5,130	1,419	3,515	4,480	8	(1)	15
PBT	1,280	2,986	4,584	1,026	3,104	3,949	25	(4)	16
Tax	282	767	1,144	262	776	987	8	(1)	16
PAT	997	2,220	3,440	764	2,328	2,961	31	(5)	16
EPS (Rs)	29.1	65.0	100.4	21.4	69.2	88.3	36	(6)	14

Source: Anand Rathi Research

Key risks to our BUY rating on the stock would include (a) inability to ramp up its components business despite support from the PLI scheme; (b) Increased credit terms along with predatory pricing being offered by Chinese vendors and (c) delays in pace of project execution by Sidwal.

**Fig 15 –PER band has been expanding consistently**



Source: Bloomberg, Anand Rathi Research

### **Risk**

- Inability to ramp up component manufacturing
- Predatory pricing and longer credit terms being offered by global vendors



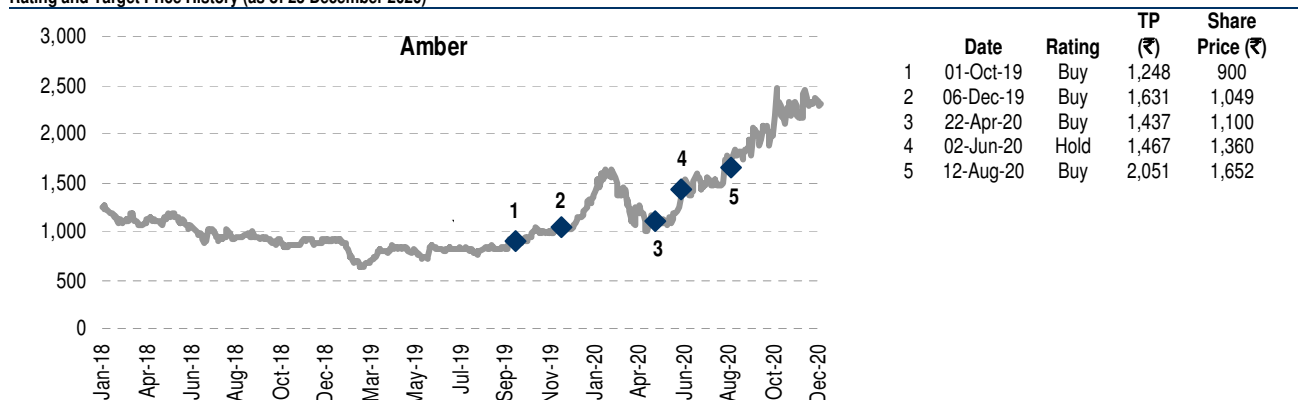
## Appendix

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