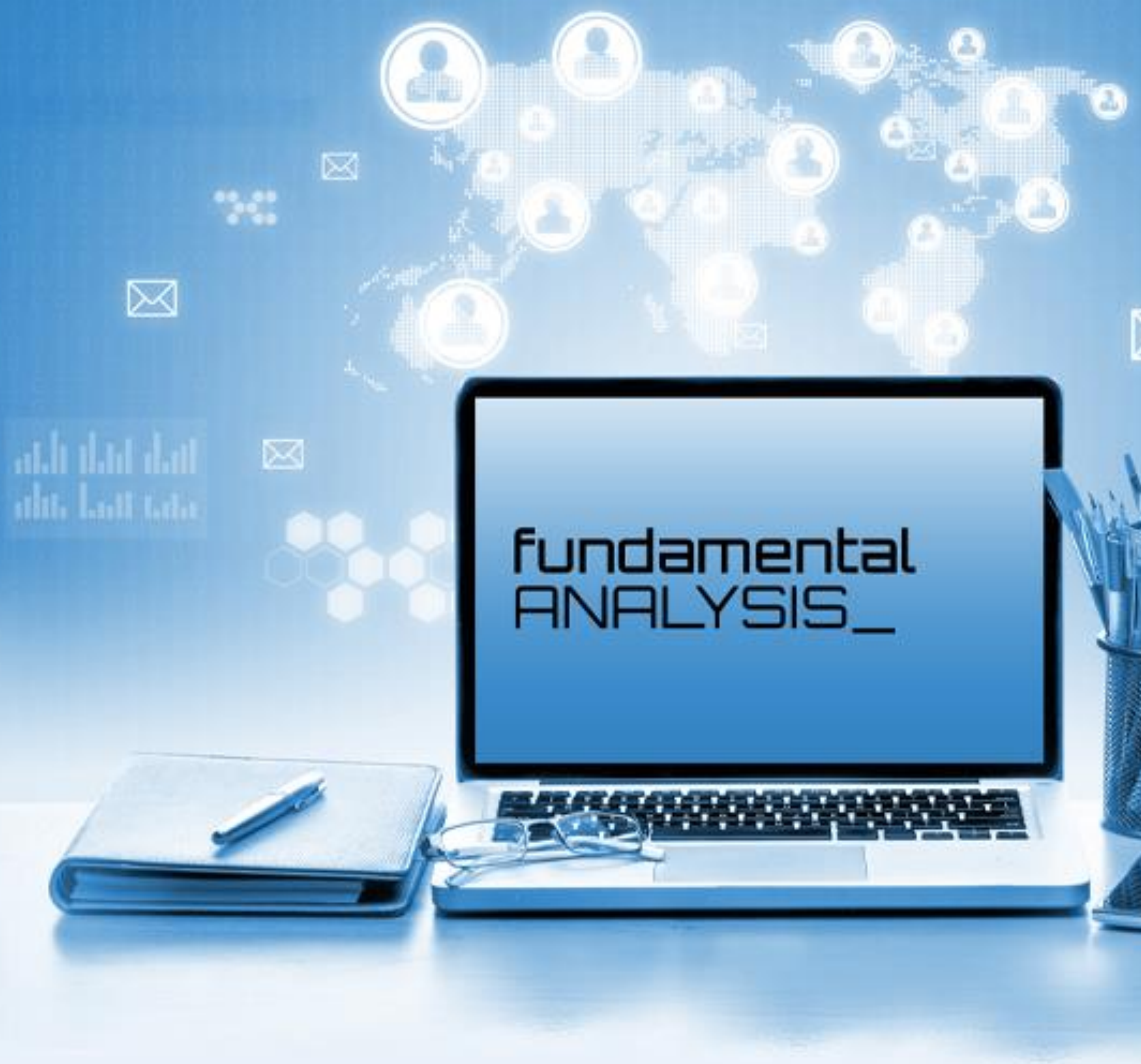
# Initiating Coverage

# Syrma SGS Technology Ltd.

March 06, 2023

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# Syrma SGS Technology Ltd.

| Industry | LTP | Recommendation | Base Case Fair Value | Bull Case Fair Value | Time Horizon |
|---|---|---|---|---|---|
| Contract Manufacturer | Rs 269.6 | Buy in the band of Rs 267-272 & add more on dips to Rs 238-242 band | Rs 294 | Rs 319 | 2-3 quarters |

| | |
|---|---|
| HDFC Scrip Code | SYRMASGS |
| BSE Code | 543573 |
| NSE Code | SYRMA |
| Bloomberg | SYRMA IN |
| CMP Mar 03, 2023 | 269.6 |
| Equity Capital (Rs cr) | 176.8 |
| Face Value (Rs) | 10 |
| Equity Share O/S (cr) | 17.7 |
| Market Cap (Rs cr) | 4,766 |
| Book Value (Rs) | 82.1 |
| Avg. 52 Wk Volumes | 1400822 |
| 52 Week High | 342.8 |
| 52 Week Low | 248.1 |

| Share holding Pattern % (Dec 2022) | |
|---|---|
| Promoters | 47.3 |
| Institutions | 12.5 |
| Non Institutions | 40.2 |
| Total | 100.0 |


* Refer at the end for explanation on Risk Ratings

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## Our Take:

Syrma SGS Technology Ltd is technology-focused engineering and design EMS (Electronics Manufacturing Services) company specialising in precision manufacturing of PCBAs (printed circuit board assembly). The company provides integrated services and solutions to OEMs, from the initial product concept stage to volume production through concept co-creation and product realization. Syrma is a high-mix flexible-volume player with diverse product offerings such as PCBA, RFID tags and magnetics catering industries such as automotive, industrial, consumer, healthcare, IT etc. Syrma currently operates through 13 strategically located manufacturing facilities in north India and south India. The company serves marquee customers including global OEMs in 20+ countries including USA, Germany, UK. It has a robust supplier network with long standing relationship with global vendors. Company's focus on high mix low volume product segment sets it apart from industry peers; which is clearly reflected in its margin profile. Continuous focus on R&D and innovation has enabled it to drive higher ODM (Original Design Manufacturer) revenues (27% of FY22 revenue) which drives customer stickiness and provides scope for increasing wallet share. Recent acquisition of SGS Tekniks and Perfect ID has strengthened its position as major EMS service provider, expanding its product profile and widening its geographic reach. The company is well positioned in the EMS industry, which is expected to grow at CAGR of 41.4% over FY22-26E.

Syrma SGS is one of the leading manufacturers of PCBAs, contributing ~77% of topline. The business segment enjoys strong demand outlook given the extensive usage of PCBA in daily applications and domestic production falling short of demand. Strong growth in added value, increasing demand for electronic products, requirement for high-speed assembly and miniaturization makes a case for robust demand outlook for PCBA which is expected to grow at 38.4% CAGR over FY22-FY26E. The company has announced brownfield and greenfield expansion that would double the existing production capacity to 30 assembly lines (surface mount technology (SMT) lines); and is expected to be operationalise gradually by FY24 adding incremental revenue to the tune of Rs 2000cr at its peak capacity. Timely capacity expansion amid strong demand outlook provides a runway for higher revenue growth going ahead.

## Valuation & Recommendation:

Syrma SGS, over the years, has diversified and expanded its product portfolio, and evolved its operations to provide design and engineering services and ODM services, that cater to various industries, including automotive, healthcare, IT, industrial appliances and consumer products industries. The company intends to focus on lighting, medical electronics, aerospace and defence industry; which corresponds to its philosophy of high margin and flexible volume business. The company has increased its customer base through new products and segments, strategic acquisitions and through expanded services offerings. Participation in high-value ODM business drives client engagement and repeated business providing scope for increasing customer's wallet share and command better margins. The company is well positioned to capitalize on strong industry tailwinds (Make in India, import substitution, PLI, adoption of China+1 strategy etc) with its strong R&D, healthy client relationships and foray into new segments. **We think the base case fair value of the stock is Rs 294 (29.5x Dec'24E EPS) and the bull case fair value is Rs 319 (32x Dec'24E EPS) over the next two-three quarters. Investors can buy the stock in the band of Rs 267-272 (27x Dec'24E EPS) and add more on dips to Rs 238-242 band (24x Dec'24E EPS).**

## Financial Summary

| Particulars (Rs cr) | Q3FY23 | Q3FY22 | YoY-% | Q2FY23 | QoQ-% | FY21 | FY22 | FY23E | FY24E | FY25E |
|---|---|---|---|---|---|---|---|---|---|---|
| Total Operating Income | 512.6 | 301.7 | 69.9 | 466.9 | 9.8 | 438.3 | 1,019.7 | 1,866.5 | 2,436.9 | 3,046.8 |
| EBITDA | 47.8 | 37.2 | 28.6 | 47.2 | 1.4 | 46.8 | 94.4 | 166.1 | 229.1 | 301.6 |
| PAT | 34.2 | 20.2 | 69.5 | 28.8 | 18.7 | 28.6 | 54.1 | 104.5 | 138.9 | 186.1 |
| Adjusted PAT | 33.2 | 19.7 | 68.1 | 28.2 | 17.6 | 32.0 | 55.5 | 105.8 | 140.2 | 187.3 |
| Diluted EPS (Rs) | 1.9 | 1.4 | 30.9 | 1.6 | 17.2 | 4.3 | 5.0 | 6.0 | 8.0 | 10.6 |
| RoE-% | | | | | | 18.7 | 13.7 | 10.0 | 8.6 | 10.5 |
| P/E (x) | | | | | | 63.0 | 54.2 | 44.9 | 33.9 | 25.4 |
| EV/EBITDA (x) | | | | | | 43.8 | 41.2 | 30.3 | 20.9 | 15.5 |

(Source: Company, HDFC sec)

## Q3FY23 Result Review:

Syrma SGS reported robust revenue of Rs 512.6cr, up 9.8% QoQ supported by healthy topline growth in consumer and automotive segments. Consolidation of numbers of the recent acquisition - SGS Tekniks and Perfect ID – resulted in sharp increase in topline growth on annual basis. Gross margin contracted ~397bps QoQ to 25.4% impacted mainly by due to change in sales mix. The company reported EBITDA margin 9.3% vs 10.1% in the previous quarter. Higher share of low margin consumer segment and muted offtake in healthcare segment impacted the margin, while better operating leverage softened the blow at EBITDA level (down 78bps QoQ). The company reported adjusted PAT of Rs 33.2cr (+17.6% QoQ).

Auto/Consumer/Healthcare/Industrials/IT and Railways contributed 21%/40%/1.8%/31.5%/5.7% of the topline respectively. Exports contribute 26% of revenue which was in earlier in the range of 35-40%. Lower discretionary spends by the consumer amid likely global recession environment could pose headwinds in the short term. The demand outlook in Industrial, automotive and consumer remains robust. In auto, the transition to electric vehicles remains a key factor fueling growth. Company's healthcare vertical is largely export-oriented and is witnessing subdued demand. The management is confident on rebound in exports after couple of quarters.

The orderbook remains healthy at Rs 2100cr as of Dec'22 vs Rs 1700cr as of Sep'22, which will support healthy topline growth in Q4FY23 and FY24. Order inflows during the quarter was ~Rs 900cr from the industrial, consumer and auto verticals. The revenue share of ODM was 11% in Q3FY23 vs 26% in Q3FY22, impacted by lower exports. The management continues to guide for revenue growth in line with the industry over the next couple of years and aims to achieve low double digit EBITDA margin on a sustainable basis.

## Key Triggers:

**Syrma SGS - leading comprehensive EMS solutions provider; well-positioned to drive growth:**

Syrma SGS is one-stop-solution electronics manufacturing services provider offering services including product design, quick prototyping, PCB assembly, Box build, repair & rework and automatic tester development services. Syrma SGS also offers OEM solutions for RFID tags & inlays and high-frequency magnetic components. Company's focus on high mix low volume product segment sets it apart from industry peers; which is clearly reflected in its margin profile. Also continuous focus on R&D and innovation has enabled it to drive higher ODM revenues (27% of FY22 revenue) which drives customer stickiness and provides scope for increasing wallet share. Its state of the art manufacturing facilities at multiple locations has a track record of low defect ratios and can handle customer requirement due to flexible production infrastructure. Backed by robust supplier network; the company leverages global sourcing capabilities to optimize costs while maintaining the quality of the products resulting in lower lead time to the market. It won two PLIs (telecom and white goods) which further improves its standing as emerging EMS player. Recent acquisition of SGS Tekniks and Perfect ID has strengthened its position as major EMS service provider, expanding its product profile and widening its geographic reach. The company is well positioned in the EMS industry which is expected to grow at CAGR of 41.4% over FY22-26E (source: Frost and Sullivan). Strong manufacturing and R&D capabilities, presence across multiple industries, marquee clientele and experienced management has enabled it grow at faster rate. Favourable sectoral tailwinds by way of the government's PLI scheme, China+1, import substitution and increased investments has improved the future growth prospects of the company.

**Riding on strong growth in PCBAs & Radio Frequency Identification Tags (RFID) coupled with the PLI scheme related benefits:**

Printed Circuit Board Assembly (PCBA) is key product segment accounting for ~76% of topline. The company has capability of manufacturing various types of PCB, ranging from flexible PCBs to 28-layer PCB and their assembly using surface-mount technology (SMT). Syrma has gradually upgraded its PCBA processes to add value to operations and addresses additional customer requirements. The business segment enjoys strong demand outlook given the extensive usage of PCBA in daily applications and domestic production falling short of demand. PCBAs are used in products manufactured in the automotive, medical, industrial, IT and consumer products industries (mobiles, computers, television), home appliances (ACs, washing machines, refrigerators) and other industrial applications. PCBA is the core of an electronic device, which includes flash memory, application processor, graphics processor, other semiconductor-based active and passive subcomponents; constituting 10-50% of the bill of materials. Strong growth in added value vertical, increasing demand for electronic products, requirement for high-speed assembly and miniaturization has improved the demand outlook for PCBA. Investing in

PCBA is critical for maintaining the domestic manufacturing impetus. The Indian PCBA market is expected to grow at 38.4% CAGR over FY22-FY26E to Rs 6,556 bn in FY26.

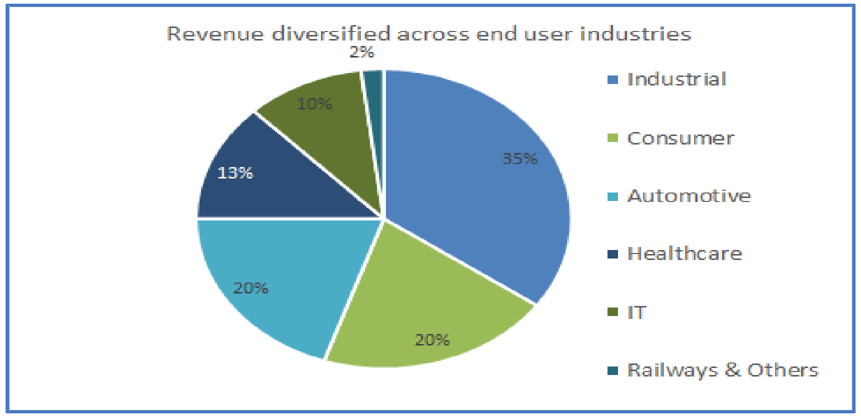
RFID segment contributed ~23% of topline in FY22 and has seen stellar growth of 44% CAGR over FY18-22. RFID has applications in asset tracking and authentication procedures. RFID products are used in shipping, healthcare, manufacturing, retail and fintech industries. It has various applications, including pet and livestock tracking, inventory management, asset tracking and equipment tracking, inventory control, cargo and supply chain logistics, vehicle tracking, among others. Syrma is working with multiple customers for various opportunities of tags in the future.

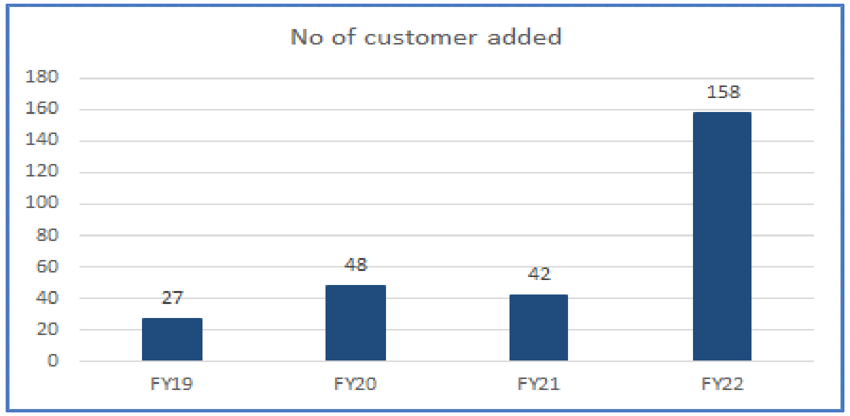
Syrma SGS is a beneficiary of PLI scheme announced by the Government to boost domestic manufacturing. The company has received approvals for Telecom & Networking Products; and White Goods (Air Conditioners & LED lights) as it supplier PCBAs to both. Under the Telecom PLI, the company manufactures access & customer premise equipment (CPE), IOT access devices, modems, routers and other wireless equipment. Investments for Telecom PLI is on track at its new facility at Manesar which has been commissioned in Q2FY23. It has already achieved threshold capex and turnover limits for this fiscal and the management expects huge traction in this business going forward. Under the white goods PLI, the company would manufacture control assemblies for ACs and LEDs. It has not started with any capex for this PLI. Products under scheme is undergoing validation and expected to come online in couple of quarters. Syrma plans to do capex of ~Rs 150cr over FY22-27; expanding its facilities in Manesar, Haryana. Although some portion of the benefits would be passed on to its customers; such benefits would incrementally improve its bottomline.

**Diversifying and expanding product portfolio with strong clientele:**

Syrma SGS, over the years, has diversified and expanded its product portfolio, and evolved its operations to provide design and engineering services and ODM services, that cater to various industries, including automotive, healthcare, IT, industrial appliances, energy management, water purification, power supply, and consumer products industries. Diverse application of its products has de-risked its revenue dependence on a particular sector. Its range of products includes printed circuit boards (PCBs), custom RFID (Radio frequency identification) tags, magnetic disk drives and coils. While the company supplies its PCBAs to automotive, medical, industrial and consumer industries, its RFIDs are procured by shipping, healthcare, manufacturing and retail industries. The diversification and expansion of the product portfolio is primarily driven by the continuously evolving needs of the customers and technological advancements in the industry; supported by its R&D capabilities. The company supplies controllers to renewable energy companies. Electric charging infrastructure and energy storage are two verticals that would gain significant in the coming years, and the management is evaluating plans to grab a pie of this booming segments. Customers' evolving portfolio has led to fast-paced growth which has helped them to retain their existing clients and win new clients across industries.

Syrma's strong product suite, quality, track record of technical innovation and focus on responsiveness has enabled to build strong customer relationships with key brands. Providing integrated services and solutions to OEMs, from the initial product concept stage to volume production through concept co-creation and product realization has helped to serve well-known customers across the end-use industries. Its marquee customers include TVS Motor, A. O. Smith India Water Products, Robert Bosch Engineering, Eureka Forbes, Hindustan Unilever Limited, and Total Power Europe B.V. The products are sold in over 24 countries, including the USA, Germany, Austria, and UK. It offers high value-added and integrated design and manufacturing solutions for internationally recognized OEMs. Association with large brands ensures steady revenue stream for the company, and builds credibility to on-board new customers. The company has a history of strong customer retention. During FY22, it catered to over 200 customers of which 16 customers have been associated for over a period of 10 years. The company is number 1 or 2 vendor for most of their customers. Around 65% of FY22 revenues from customers who have been associated for over 3 years, with no single customer contributing to ~10% of revenues. Syrma SGS has increased its customer base through new products and segments, strategic acquisitions and through expanded services offerings.




(Source: Company, HDFC sec)

**Higher ODM share backed by its R&D capabilities:**

Syrma has been able to evolve its product portfolio and service offerings on the back of its R&D capabilities. The company has three dedicated R&D facilities, two of which are located in India at Chennai and Gurgaon and one is located in Stuttgart, Germany. Their R&D efforts are focused on (i) development of new products and improvement of the quality of its existing products; and (ii) driving the design and engineering capabilities and ODM capabilities. The focus is on taking early advantage of technological advancements and optimize current product offerings by improving cost efficiencies and making value additions through inclusion of additional or improved features. Its R&D focus has helped to drive ODM business share (27% of FY22 conso proforma revenue). The company's ODM entails end-to-end product design and development; which starts from the product concept design and navigates the entire value chain (prototyping, sample batch and series production) and lifecycle management and support. Participation in high-value ODM business drives client engagement and repeat business providing scope for increasing customer's wallet share and command better margins. Company's focus on higher ODM business resulted in industry leading EBITDA margin (10-11% vs 4-7% of peers). Although ODM share has fallen to 11% in Q3FY23 on account of lower exports, the management strives to maintain ODM contribution of 25-30%. We model healthy growth in ODM sales going ahead.

**Strong manufacturing capabilities coupled with Global supplier network:**

Syrma currently operate through 13 strategically located manufacturing spread across five states with facilities in North India (i.e. Himachal Pradesh, Haryana and Uttar Pradesh) and South India (i.e. Tamil Nadu and Karnataka) with 2 facilities added in H1FY23. The company has strategically chosen these locations to stay in proximity of their customers and to avail tax & other benefits of special economic zones. The manufacturing facilities in Tamil Nadu and Haryana help the company to cater to export customers. The plants are equipped with state of the art modern and automated equipment. For PCBA products, the manufacturing facilities are equipped with modern and high speed equipment that can handle surface mount components and through hole components. RFID products that require specialized equipment for winding high and low frequency coils. Syrma has invested in automated, high speed, high accuracy winding machines; which require minimal manual intervention and has the capacity to produce 2.5 million tags a month. Also, manufacturing lines across plants provides flexibility to migrate production between facilities based on the demand. The company is focused on vertical integration. Syrma as part of its product portfolio is increasing focus on manufacturing of various electromagnetic components parts such as transformers and chokes, which are required for the manufacture of PCBA products; thereby improving its cost efficiencies and avoid long lead time. Syrma has a robust global supply chain network. The suppliers are separately audited and verified by supplier quality engineers. It is not reliant on any single supplier for any of its raw materials or components. On the back of its global sourcing capabilities, it can optimize costs and lower lead time to market.

| Manufacturing Facility | Aggregate annual installed capacity | Capacity Utilisation | | |
|---|---|---|---|---|
| | | FY22 | FY21 | FY20 |
| Chennai – Unit 1 | 10,120 Million (M) Components per Annum (CPA) and 3.6 M assemblies | 87% | 75% | 65% |
| Chennai – Unit 2 | 300 M tags | 77% | 70% | 65% |
| Bargur | 6 M Coils | 85% | 75% | 65% |
| Bawal | 7.2 M modules | 80% | 70% | 50% |
| Manesar | 180M CPA | 80% | 75% | 65% |
| Gurgaon | 1,500,000 Tags per month | 83% | 75% | 65% |
| Bengaluru – Unit 1<br>Bengaluru – Unit 2 | 10,120 Million (M) Components per Annum (CPA) and 3.6 M assemblies & 300 M tags | 86% | 70% | 60% |
| Baddi – Unit 1<br>Baddi – Unit 2 | 6 M Coils<br>7.2 M modules | 86% | 75% | 50% |
| Ghaziabad | 180M CPA | 75% | 55% | 35% |

**Focus on catering to more end-user industries and expanding customer base:**

Syrma has a strong track record of meeting customer expectation to the changing technology needs. Their focus on design, engineering coupled with strong R&D capabilities has provided the ability to transition and launch new products. The company has increased its customer base through new products and segments, strategic acquisitions and through expanded services offerings which include prototyping services, tester development, and repair and rework services. Syrma currently caters to various industries - automotive, healthcare, IT and telecom hardware, industrial products, household appliances, energy management and consumer industries. The company intends to focus on lighting, medical electronics, aerospace and defence industry; which corresponds to its philosophy of high margin and flexible volume business. Syrma is adding several products to address the fast-growing smart devices and consumer appliance segment catering to marquee customer base. Telecom is another industry where the company has received PLI license. It has entered into contracts with clients to provide PCBAs for products like Wifi routers, modems, etc. The company has set foot in the EV space; it has commenced manufacturing of controllers of the EV battery management system. Medical device space is witnessing strong growth due to emergence of advanced technologies, evolving clinical and administrative needs, and the introduction of new policies and regulations. Syrma has plans to enter this sector, which is expected to grow at ~43% CAGR over FY22-26. The company also wants a piece of aerospace and defence sector given the increasing trend of indigenization and modernizing equipment.

**Focus on increasing wallet share with existing customers:**

Syrma SGS has continuous focus on working closely with existing customers to develop broader portfolio of products which meet their requirements. The evolution of product portfolio and service offerings have been driven by its R&D capabilities, engineering capabilities and quality control. The company intends to leverage their long-standing relationships with their customers for cross-selling and up-selling opportunities through their diversified product portfolio. The management has plans to get into box build more aggressively, currently 15% of revenue. Through its concreted efforts, it saw an increase in wallet share from top 20 customers; registering ~26% CAGR over FY20-22. Supplying a box build product would lead to backward integration moving up value chain of its offerings, thereby improving its margins. Higher ODM share improves customer stickiness and provides room for margin expansion. Moreover, the company has strong exports customer base; having presence across 24 countries to various end user industries. Exports account for ~44% of proforma consolidated revenues in FY22. Setting up subsidiary in Germany and having R&D center facilitates expansion of overseas operations. Clouds of global recession remains a headwind in the near term; we expect export revenues to accelerate in the long run on the back of wide application of PCBA supported by its engineering capabilities and China+1 strategy.

**Capacity expansion supported by strong industry tailwinds:**

Syrma SGS has shifted its gears on the capital expansion backed by its IPO proceeds. The company plans to utilise funds from IPO to setup R&D facility in Chennai (Rs 38cr); setting up new facilities in Hyderabad (Rs 52cr), in Bawal (Rs 62cr), in Hosur (Rs 83cr); and expanding existing manufacturing facilities in Chennai (Rs 108cr) and in Manesar (Rs 228cr). These brownfield and greenfield expansion would double the existing production capacity to 30 assembly lines (surface mount technology (SMT) lines); and is expected to be operationalise gradually by FY24 adding incremental revenue to the tune of Rs 2000cr at its peak capacity. The company has commissioned 2 SMT lines in H1FY23 and is on track to operationalize 3 more SMT lines in H2FY23. Plans for such high capacity outlay indicates that the management is confident in securing new customers and orders. The new facility commissioned in Manesar and Chennai are would have more ODM product offering are witnessing ongoing plant audits by marquee customers. As per industry reports, domestic electronic manufacturing services (EMS) industry is expected to see a robust growth of 41% CAGR, with ODM growing faster at 43% over FY21-26. Timely capacity expansion amid strong demand outlook provides a runway for higher revenue growth going ahead.

**Plans to expand inorganically to enhance scale and market position:**
Syrma has made conscious effort to diversify its product portfolio which would allow it to cater to customer across various end-use industries and geographies. The company intends to strengthen its existing product portfolio and diversify into products with strong growth and profitability. Syrma, in the past, have taken inorganic route to strengthen its position as an EMS player. It acquired Tovya Automation in Dec’14, and acquired SGS Tekniks in Sep’21 and Perfect ID in Oct’21.

Acquisition of SGS Tekniks has helped in expanding its manufacturing facilities footprint across India and inhouse R&D capabilities in Germany. It also helped to consolidate & optimize its manufacturing network and component purchases for various clients which led to higher bargaining power. As per management, there is no overlap between Syrma and SGS, thereby diversifying the segment and client profile. Further, it also provided cross-selling and up-selling opportunities of Syrma’s RFID products to SGS’s existing customers. With the acquisition of Perfect ID, it acquired the infrastructure and know-how for the manufacture of RFID label tags and passive inlay tags; expanding its RFID products portfolio. The company is open to pursue similar opportunities that would allow it to enhance its scale & market position; provide access to new clients and enter high growth geographies. The management is looking for companies that would have backward integration & forward integration and full box build capabilities.

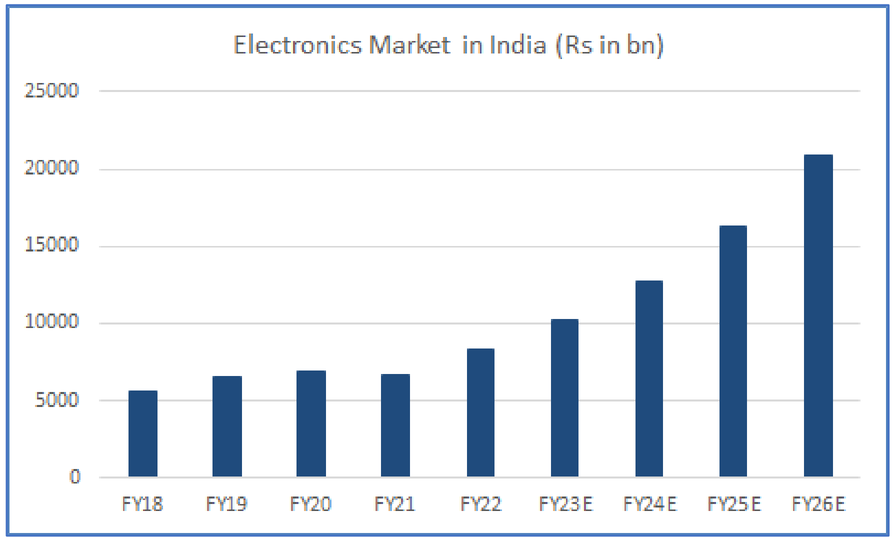
## Industry Insights:

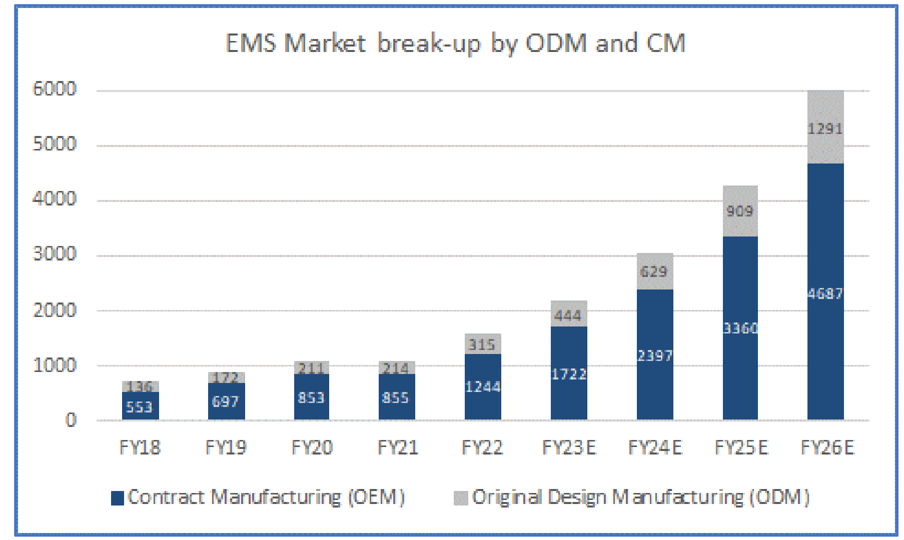
Market size and Opportunity:

The global electronics manufacturing services market traditionally comprised companies that manufacture electronic products, predominantly assembling components on printed circuit boards (PCBs) and box builds for major brands. Brands are now seeing more value from EMS companies, leading to involvement beyond manufacturing services to product design and development, testing, and aftersales services such as repair, remanufacturing, marketing and product lifecycle management. China leads the global EMS business with almost 45.5% market share. Its dominance in the global market is attributed to a blend of cost effectiveness and technological leadership in electronics manufacturing. However, post COVID-19, many global electronics manufacturers are contemplating the ‘China +

1’ strategy and looking for alternative manufacturing locations for exports business. This is creating tremendous investment potential for countries like India, Vietnam, Philippines, etc. India contributed to approximately 1.8% of the global EMS market in 2020.

Electronics is one of the fastest growing industries in the country. The total electronics market in India, which includes domestic electronics production and imports of electronic finished goods, is valued at Rs 6,711 billion (USD 91 billion) in FY21, which is expected to grow at a CAGR of 25.5% to reach Rs 20,873 billion (USD 282 billion) in FY26. Domestic production accounts for approximately 74% of the total electronics market in FY21, valued at Rs 4,975 billion (USD 67 billion), and is expected to grow at CAGR of 32.3% to reach Rs 20,133 billion (USD 272 billion) in FY26, owing to various government initiatives and the development of India's electronic ecosystem. With the global landscape of electronics design and manufacturing changing, India is being looked at as an attractive destination for various MNCs.




(Source: Company, HDFC sec)

The total addressable EMS market in India was valued at Rs 2,654 billion (USD 36 billion) in FY21 and is expected to grow to Rs 9,966 billion (USD 135 billion) in FY26 with a CAGR of 30.3%. Contribution of Indian EMS companies is around 40% with a value of Rs 1,069 billion (USD 14 billion) in FY21. This is expected to grow at 41.1% CAGR to reach Rs 5,980 billion (USD 81 billion) by FY26. India is one of the biggest markets in the world for white goods with a very low penetration. The demand is showing a major uptrend due to factors like - rapid urbanisation, increasing affordability, growing working-class population, higher rural demand and changing consumer behaviour.

Consumers have shifted their attitudes about electronic durables from leisure products to necessities. The growth for contract manufacturers is due to dual benefit of Under-penetration and Import-substitution.

PLI & Other Incentives – shifting gears for EMS players

The government of India has been proactively building a base for electronics manufacturing in India and it has launched numerous incentive schemes, which have allowed manufacturing growth, reduced dependence on the imports and promoted the exports. The Indian government is attempting to enhance manufacturing capabilities across multiple electronics sectors and to establish the missing links in order to make the Indian electronics sector globally competitive. The Government is using multiple levers to enhance domestic production of electronic items through 1) incentives such as PLI (Production-linked incentive) schemes; 2) dedicated sector-focused programs—the Phased Manufacturing Program (PMP), Modified Electronics Manufacturing Clusters (EMC 2.0) Scheme, and Scheme for Promotion of manufacturing of Electronic Components and Semiconductors; and 3) tariffs—the progressive increase in tariffs of key finished goods and raw materials and intermediaries along with a large consumer base create a favourable environment in our view for both brands and contract manufacturers to increase their domestic manufacturing presence. PLI scheme offers incentives to promote the EMS industry and pushes companies to rethink their local supply chain and aim for export-led growth. PLI scheme is expected to yield total production of Rs 11,500 billion is expected including Rs 7,000 billion exports in the next five years. The ambitious expansion plans and an increase in capacity of Indian EMS players to capitalize on favourable policy initiatives ensure that the India EMS sector will witness heightened growth over the next few years.

Electronics industry - strategic choice for domestic manufacturing

The outsourcing decision is a strategic one that brands/manufacturers have to take in relation to market developments. In the electronics industry, decreasing product life cycles (with new innovations) and increasing demand for diversity puts significant pressure on the resources of a manufacturer and drives the various degrees of outsourcing. Production of mass electronics like TVs, consumer durables, laptops etc. are better done through the outsourcing model.

Bigger EMS providers are slowly evolving to offer complete design services on top of contract manufacturing. This acts as a win-win situation for both EMS players as well as OEMs; EMS players obtain higher margins through this model, and OEMs benefit by outsourcing manufacturing and design activities, enabling them to focus on other expansion activities. Embracing the ODM model of partnership coupled with venturing into new product segments is propelling OEMs to pursue this engagement. High volumes will influence EMS companies to bring in the component ecosystem locally and enhance domestic capabilities for component sourcing, making the electronics ecosystem stronger.

Many brands are focusing more on brand positioning rather than in-house manufacturing, which puts players like Syrma SGS in a sweet spot. EMS players are likely to pass on the PLI incentive to the brand to get incremental business as well as keeping the brand away from manufacturing. While there is an investment threshold which may not be challenging for most willing participants, the incentive is based on incremental sales on the base year which most likely could only be achieved by larger focused players. In the next two years, winners of PLI scheme would be clearer and throw light on the leading contract manufacturer in India.

## Concerns:

**Competition Risk:** The domestic consumer electronics market is intensely competitive on account of entry of several large players over the past few years. Some of the international players with strong economies of scale still have a high cost advantage over domestic players. Major players in the EMS space are Flextronics, Jabil, Dixon, SFO, Resolute, Elin and Foxconn. In addition, OEMs have begun to manufacture some products themselves to avail of PLI benefits. The EMS landscape is likely to witness higher competition going ahead.

**No long-term customer contracts:** The company’s clients do not enter into long-term commitments; may change or cancel their production requirements. Such order changes or cancellations could impact company’s operational performance

**Volatility in raw material prices:** Volatility in commodity prices and currency can impact the company’s margins in a short timeframe. Majority of the components (62%) are imported. Further disruption in global supply chain for critical components may impact volumes. Although raw material costs are pass through, it happens at certain lags.

**Delay in expansion**: The company has announced aggressive capital outlay plan; any delay in launch of new plants would impact company financials.

**Technological obsolescence risk:** EMS industry is constantly exposed to obsolescence risk, which requires the company to keep up with the changes and advancements by constantly upgrading its products and technologies. R&D capabilities are also critical to their success. Any failure to derive results from its R&D efforts or failure in new product launch may hurt its competitiveness and profitability.

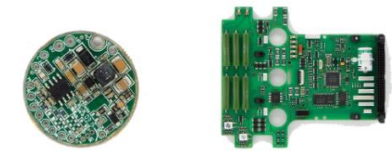
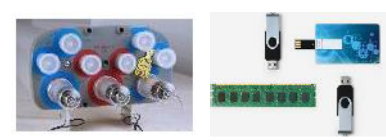
**Economic Slowdown:** Around 44% of company revenue come from exports. Global slowdown would impact company’s growth prospects in the near term.

## About the company:

Syrma SGS Technology Ltd (SSTL) is technology-focused engineering and design company engaged in turnkey electronics manufacturing services (EMS). Syrma is one of the leading PCBA (printed circuit board assembly) manufacturers in India, supplying to various OEMs and assemblers in the market. Its range of products includes printed circuit boards (PCBs), custom RFID (Radio frequency identification) tags, magnetic disk drives and coils. It is one-stop-solution electronics manufacturing services (EMS) includes product design, quick prototyping, PCB assembly, Box build, repair & rework and automatic tester development services. The company provides integrated services and solutions to OEMs, from the initial product concept stage to volume production through concept co-creation and product realization.

Syrma SGS is one of the leaders in high-mix low-volume product management that specialises in precision manufacturing for diverse end-use industries, including industrial appliances, automotive, healthcare, consumer products and IT industries. Its high mix and low volume approach distinguishes itself from industry peers which is reflected in its margin profile. Syrma currently operates through 13 strategically located manufacturing facilities in north India (i.e. Himachal Pradesh, Haryana and Uttar Pradesh) and south India (i.e. Tamil Nadu and Karnataka). Its manufacturing infrastructure allows to undertake a high mix of products with flexible production volume requirements. The company is focused on technological innovation through R&D capabilities and has 3 dedicated R&D facilities, two in India and one is located in Stuttgart, Germany. The company serves marquee customers including global OEMs in 20+ countries including USA, Germany, UK. It has a robust supplier network with long standing relationship with global vendors.

To expand its market share in the EMS sector, company acquired SGS Tekniks in Sep 2021 and Perfect ID in Oct 2021. The company initially bought 20% stake in SGS Tekniks in Oct 2020 and later acquired 100%. SGS is an Indian EMS company that primarily assembles PCBs for its clients. In terms of customer and geographical profile, there is no overlap between Syrma and SGS, thereby providing ample headroom for growth diversifying the segment and client profile at a group level. Syrma acquired 75% stake in Perfect ID India Private Limited which manufactures RFID label tags and passive inlay tags; thereby expanding the RFID products portfolio.

| Products | Applications | Annual capacity | Capacity Utilisation | |
|---|---|---|---|---|
| **Printed circuit board assemblies (PCBA)** | PCBAs are used in products manufactured in the automotive, medical, industrial, IT and consumer products industries, and also include box-build products. It finds application in cars, tractors, X-ray machines, computers and laptops, telecommunication, networking, power supply, electric mobility, etc. | 10.12 mn Components per Annum (CPA) and 3.6 M ASSEMBLIES | 87% |  |
| **Radio frequency identification (RFID) products** | RFID products are used in products manufactured in the shipping, healthcare, manufacturing, retail and fintech industries. | RFID: 300 mn tags<br>RFID label tags: 1,500,000 Tags per month | 86% / 75% |  |
| **Electromagnetic and electromechanical parts** | Magnetic products like chokes, inductors, magnetic filters, transformer as well as high volume manufacturing assemblies. These parts are used in products manufactured in the automotive, industrial appliances, consumer appliances and healthcare industries, among others. | Magnetics: 6 mn Coils | 83% |  |
| **Other products** | Include motherboards, DRAM modules, solid state drives, USB drives and other memory products. | - | - |  |

(Note: Capacity Utilisation is for FY22, Source: Company, HDFC sec)

**Peer Comparison:**

| | Mcap (Rs cr) | Revenue | | | | EBITDA Margin (%) | | | | PAT | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | FY22 | FY23E | FY24E | FY25E | FY22 | FY23E | FY24E | FY25E | FY22 | FY23E | FY24E | FY25E |
| **Syrma SGS Technology** | **4,766** | **1020** | **1867** | **2437** | **3047** | **9.3** | **8.9** | **9.4** | **9.9** | **54** | **105** | **139** | **186** |
| Dixon Technologies | 17,736 | 10,697 | 12,325 | 17,985 | 22,267 | 3.5 | 4.0 | 4.1 | 4.1 | 190 | 247 | 413 | 545 |
| Amber Enterprises | 6,751 | 4,206 | 5,972 | 7,383 | 8,796 | 6.5 | 6.2 | 6.9 | 7.2 | 111 | 137 | 222 | 309 |

| | RoE (%) | | | | P/E | | | |
|---|---|---|---|---|---|---|---|---|
| | FY22 | FY23E | FY24E | FY25E | FY22 | FY23E | FY24E | FY25E |
| **Syrma SGS Technology** | **13.7** | **10.0** | **8.6** | **10.5** | **54.2** | **44.9** | **33.9** | **25.4** |
| Dixon Technologies | 21.9 | 21.6 | 29.4 | 29.4 | 92.2 | 71.4 | 42.6 | 32.3 |
| Amber Enterprises | 6.5 | 7.3 | 11.4 | 14.0 | 61.8 | 49.3 | 30.4 | 21.9 |

(Source: Bloomberg estimates, Company, HDFC sec)

## Financials

### Income Statement

| (Rs Cr) | FY21 | FY22 | FY23E | FY24E | FY25E |
|---|---|---|---|---|---|
| **Net Revenues** | **438.3** | **1019.7** | **1866.5** | **2436.9** | **3046.8** |
| **Growth (%)** | **10.4** | **132.7** | **83.0** | **30.6** | **25.0** |
| Operating Expenses | 391.6 | 925.3 | 1700.4 | 2207.8 | 2745.2 |
| **EBITDA** | **46.8** | **94.4** | **166.1** | **229.1** | **301.6** |
| **Growth (%)** | **-24.7** | **102.0** | **75.9** | **37.9** | **31.7** |
| **EBITDA Margin (%)** | **10.7** | **9.3** | **8.9** | **9.4** | **9.9** |
| Depreciation | 12.1 | 19.4 | 30.7 | 48.0 | 61.2 |
| **EBIT** | **34.7** | **75.0** | **135.5** | **181.1** | **240.4** |
| Other Income | 6.2 | 12.7 | 29.9 | 34.1 | 39.6 |
| Interest expenses | 4.5 | 6.8 | 21.8 | 26.2 | 28.3 |
| **PBT** | **36.3** | **80.9** | **143.6** | **189.0** | **251.8** |
| Tax | 7.7 | 26.8 | 39.1 | 50.1 | 65.7 |
| **RPAT** | **28.6** | **54.1** | **104.5** | **138.9** | **186.1** |
| **APAT** | **32.0** | **55.5** | **105.8** | **140.2** | **187.3** |
| **Growth (%)** | **-16.4** | **73.4** | **90.5** | **32.5** | **33.6** |
| EPS | 4.3 | 5.0 | 6.0 | 8.0 | 10.6 |

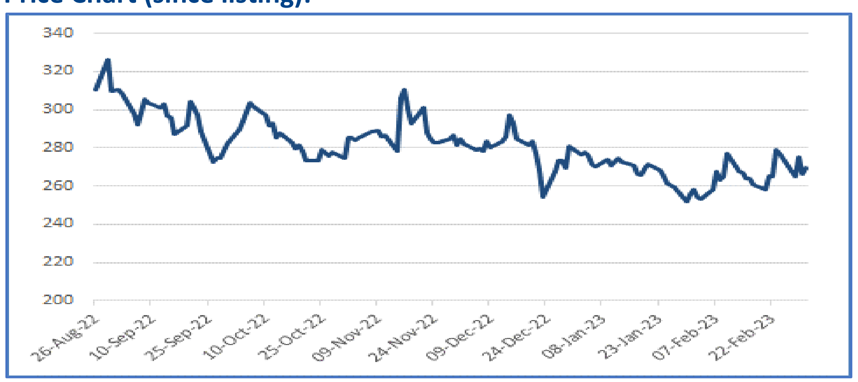
### Balance Sheet

| As at March (Rs Cr) | FY21 | FY22 | FY23E | FY24E | FY25E |
|---|---|---|---|---|---|
| **SOURCE OF FUNDS** | | | | | |
| Share Capital | 0.8 | 137.6 | 176.8 | 176.8 | 176.8 |
| Reserves | 240.8 | 434.4 | 1377.6 | 1517.9 | 1705.2 |
| **Shareholders' Funds** | **241.6** | **572.1** | **1554.4** | **1694.6** | **1882.0** |
| Minority's Interest | 0.0 | 10.8 | 13.3 | 16.9 | 21.7 |
| Long Term Debt | 28.7 | 25.8 | 25.8 | 25.8 | 25.8 |
| Net Deferred Taxes | 0.2 | 12.3 | 12.3 | 12.3 | 12.3 |
| Long Term Provisions & Others | 3.9 | 10.3 | 17.6 | 22.9 | 28.7 |
| **Total Source of Funds** | **274.4** | **631.2** | **1623.3** | **1772.5** | **1970.4** |
| **APPLICATION OF FUNDS** | | | | | |
| Net Block & Goodwill | 81.4 | 261.5 | 440.8 | 572.8 | 661.7 |
| CWIP | 0.0 | 39.1 | 39.1 | 39.1 | 39.1 |
| Other Non-Current Assets | 117.2 | 152.3 | 822.8 | 427.5 | 244.8 |
| **Total Non Current Assets** | **198.6** | **452.9** | **1302.7** | **1039.4** | **945.5** |
| Current Investments | 0.0 | 36.3 | 36.3 | 36.3 | 36.3 |
| Inventories | 77.1 | 291.3 | 506.3 | 654.3 | 818.0 |
| Trade Receivables | 127.9 | 272.2 | 460.2 | 587.5 | 717.9 |
| Cash & Equivalents | 30.2 | 36.9 | 37.2 | 309.7 | 460.2 |
| Other Current Assets | 29.7 | 64.5 | 138.1 | 166.9 | 208.7 |
| **Total Current Assets** | **264.8** | **701.3** | **1178.1** | **1754.8** | **2241.1** |
| Short-Term Borrowings | 32.7 | 192.5 | 287.5 | 317.5 | 352.5 |
| Trade Payables | 114.8 | 240.5 | 460.2 | 574.2 | 701.2 |
| Other Current Liab & Provisions | 41.5 | 89.9 | 109.8 | 130.0 | 162.6 |
| **Total Current Liabilities** | **189.1** | **522.9** | **857.6** | **1021.7** | **1216.3** |
| Net Current Assets | 75.8 | 178.4 | 320.5 | 733.0 | 1024.8 |
| **Total Application of Funds** | **274.4** | **631.2** | **1623.3** | **1772.5** | **1970.4** |

### Cash Flow Statement

| (Rs Cr) | FY21 | FY22 | FY23E | FY24E | FY25E |
|---|---|---|---|---|---|
| Reported PBT | 36.3 | 80.9 | 143.6 | 189.0 | 251.8 |
| Non-operating & EO items | -1.7 | -3.1 | -665.5 | 401.6 | 190.4 |
| Interest Expenses | 3.6 | 6.8 | 21.8 | 26.2 | 28.3 |
| Depreciation | 12.1 | 19.4 | 30.7 | 48.0 | 61.2 |
| Working Capital Change | -16.4 | -65.9 | -230.9 | -166.1 | -172.1 |
| Tax Paid | -10.0 | -23.2 | -39.1 | -50.1 | -65.7 |
| **OPERATING CASH FLOW ( a )** | **23.9** | **14.9** | **-739.4** | **448.7** | **293.8** |
| Capex | 0.0 | 0.4 | -210.0 | -180.0 | -150.0 |
| Free Cash Flow | 23.9 | 15.3 | -949.4 | 268.7 | 143.8 |
| Investments | 0.0 | 1.2 | 0.0 | 0.0 | 0.0 |
| Non-operating income | -88.7 | -311.1 | 0.0 | 0.0 | 0.0 |
| **INVESTING CASH FLOW ( b )** | **-88.7** | **-309.5** | **-210.0** | **-180.0** | **-150.0** |
| Debt Issuance / (Repaid) | -21.7 | 76.9 | 95.0 | 30.0 | 35.0 |
| Interest Expenses | -6.7 | -8.4 | -21.8 | -26.2 | -28.3 |
| FCFE | -4.5 | 83.8 | -876.2 | 272.5 | 150.5 |
| Share Capital Issuance | 33.1 | 271.5 | 876.0 | 0.0 | 0.0 |
| Dividend | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Others | 63.3 | 18.3 | 0.0 | 0.0 | 0.0 |
| **FINANCING CASH FLOW ( c )** | **68.0** | **358.3** | **949.2** | **3.8** | **6.7** |
| **NET CASH FLOW (a+b+c)** | **3.1** | **63.8** | **-0.2** | **272.5** | **150.5** |

### Price Chart (since listing):




(Source: Company, HDFC sec)

### Key Ratios

| | FY21 | FY22 | FY23E | FY24E | FY25E |
|---|---|---|---|---|---|
| **PROFITABILITY RATIOS (%)** | | | | | |
| EBITDA Margin | 10.7 | 9.3 | 8.9 | 9.4 | 9.9 |
| EBIT Margin | 9.3 | 8.6 | 8.9 | 8.8 | 9.2 |
| APAT Margin | 7.3 | 5.4 | 5.7 | 5.8 | 6.1 |
| RoE | 18.7 | 13.7 | 10.0 | 8.6 | 10.5 |
| RoCE | 16.5 | 16.0 | 12.4 | 11.0 | 13.0 |
| **Solvency Ratio (x)** | | | | | |
| Debt/EBITDA | 1.3 | 2.3 | 1.9 | 1.5 | 1.3 |
| D/E | 0.3 | 0.4 | 0.2 | 0.2 | 0.2 |
| **PER SHARE DATA (Rs)** | | | | | |
| EPS | 4.3 | 5.0 | 6.0 | 8.0 | 10.6 |
| CEPS | 5.9 | 5.4 | 7.7 | 10.6 | 14.1 |
| Dividend | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| BVPS | 32.3 | 41.6 | 87.9 | 95.9 | 106.5 |
| **Turnover Ratios (days)** | | | | | |
| Debtor days | 102 | 72 | 72 | 78 | 78 |
| Inventory days | 61 | 66 | 78 | 87 | 88 |
| Creditors days | 92 | 64 | 69 | 77 | 76 |
| **VALUATION** | | | | | |
| P/E (x) | 63.0 | 54.2 | 44.9 | 33.9 | 25.4 |
| P/BV (x) | 8.3 | 6.5 | 3.1 | 2.8 | 2.5 |
| EV/EBITDA (x) | 43.8 | 41.2 | 30.3 | 20.9 | 15.5 |
| EV/Revenues (x) | 4.7 | 3.8 | 2.7 | 2.0 | 1.5 |
| Dividend Yield (%) | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Dividend Payout (%) | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |

(Source: Company, HDFC sec)

HEMANSHU VIJAY PARMAR

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## HDFC Sec Retail Research Rating description

### Green Rating stocks

This rating is given to stocks that represent large and established business having track record of decades and good reputation in the industry. They are industry leaders or have significant market share. They have multiple streams of cash flows and/or strong balance sheet to withstand downturn in economic cycle. These stocks offer moderate returns and at the same time are unlikely to suffer severe drawdown in their stock prices. These stocks can be kept as a part of long term portfolio holding, if so desired. This stocks offer low risk and lower reward and are suitable for beginners. They offer stability to the portfolio.

### Yellow Rating stocks

This rating is given to stocks that have strong balance sheet and are from relatively stable industries which are likely to remain relevant for long time and unlikely to be affected much by economic or technological disruptions. These stocks have emerged stronger over time but are yet to reach the level of green rating stocks. They offer medium risk, medium return opportunities. Some of these have the potential to attain green rating over time.

### Red Rating stocks

This rating is given to emerging companies which are riskier than their established peers. Their share price tends to be volatile though they offer high growth potential. They are susceptible to severe downturn in their industry or in overall economy. Management of these companies need to prove their mettle in handling cyclicality of their business. If they are successful in navigating challenges, the market rewards their shareholders with handsome gains; otherwise their stock prices can take a severe beating. Overall these stocks offer high risk high return opportunities.



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