India

ADD *(no change)*

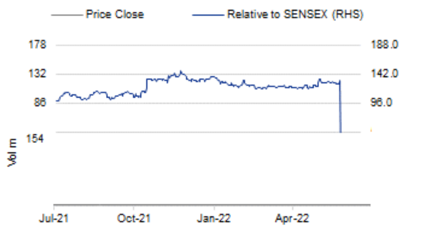
Consensus ratings*:	Buy 5	Hold 2	Sell 2

Current price:	Rs3,731
Target price: ▲	Rs4,200
Previous target:	Rs3,100
Up/downside:	12.6%
InCred Research / Consensus:	20.6%
Reuters:	
Bloomberg:	SKF IN
Market cap:	US$2,540m
	Rs184,475m
Average daily turnover:	US$2.0m
	Rs148.1m
Current shares o/s:	49.4m
Free float:	47.4%

Source: Bloomberg

Key changes in this note

- Raise FY23F-24F EBITDA by 6-9%.
- Raise FY23F-24F PAT by 5-9%.



Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	17.0	8.6	45.2
Relative (%)	10.2	12.5	40.0

Major shareholders	% held
Promoter	52.6
HDFC Mutual Fund	7.5
MIRAE Mutual Fund	6.3

SKF India Ltd

FY22 annual report analysis

- Sustaining end-market demand in FY23F, increased market penetration, focus on REP, and continuous recovery in gross margin gel well for earnings growth.
- Gross margin pressure in FY22 was higher in traded goods, whose share was up by 50bp yoy. Operating leverage and pricing supported EBITDA margin.
- Maintain Add rating on the stock with a higher target price of Rs4,200.

Operating leverage offsets gross margin dip - mainly in traded goods

SKF India's strong FY22 financial performance was led by end-market demand, pricing, and enhanced penetration driving market share gains with disciplined cost control limiting the margin decline, despite inflationary and supply chain pressure. Of FY22 sales growth of 36.5% yoy, sales of traded/manufactured goods grew 38%/35% yoy, respectively. Traded goods sales' share inched up by a mere 50bp yoy to 43.9% in FY22 considering higher industrial segment's share. FY22 gross margin dip (279bp yoy) was impacted by 359bp/254bp yoy decline in gross margin on traded/manufactured goods, respectively, because of commodity cost pressure. Traded goods' gross margin was weak, but manufactured goods' gross margin was still in line with its historical level.

New product launches, strong demand led to strong export growth

FY22 domestic sales/exports rose 31%/112% yoy, respectively, due to robust exports (formed 11.8% of FY22 sales vs. 7.6% in FY21) because of new products launched for Asian and European automobile customers and also meeting strong demand from the SKF group's factories. New business wins in FY22 includes supply of wheel-end bearings for a light commercial vehicle maker and a global customer, and bearings for dual clutch transmission and HBU3 modular unit of a renowned electric vehicle or EV manufacturer. SKF India is optimistic about sustaining its growth in FY23F. It expects the bearings market to grow from US$1.8bn in 2021 to US$3.4bn by 2027F (CAGR of 10.9%).

Increased focus on aftermarket and REP segments

Increased market penetration has been a focus area for SKF India, while it has also introduced five new products in the auto aftermarket segment. SKF India recently indicated its higher focus on increasing its market share in the aftermarket segment. SKF India wants its plants to be close to its customers to ensure shorter lead time (aims higher localization for industrial products). Its remanufacturing and lubrication solutions enhance cost savings for customers and drives the circular economy. Acceleration in rotating equipment performance (REP), in our view, gels well for margins.

Maintain Add rating with higher target price of Rs4,200

We raise our FY23F-24F EPS by 6-9% led by higher sales and raise the target price to Rs4,200 (from Rs3,100 earlier), based on 32x year-ending Sep 2024F EPS (+1SD 10-year average vs. 30x earlier). Downside risks are inability to sustain demand revival, and higher commodity prices.

Financial Summary	Mar-21A	Mar-22A	Mar-23F	Mar-24F	Mar-25F
Revenue (Rsm)	26,329	36,036	43,344	48,944	54,892
Operating EBITDA (Rsm)	4,201	5,557	6,769	7,918	9,122
Net Profit (Rsm)	2,977	3,951	4,968	5,953	6,905
Core EPS (Rs)	60.2	79.9	100.5	120.4	139.7
Core EPS Growth	3.0%	32.7%	25.7%	19.8%	16.0%
FD Core P/E (x)	61.96	46.69	37.14	30.99	26.72
DPS (Rs)	130.0	14.5	17.0	18.0	20.0
Dividend Yield	3.48%	0.39%	0.46%	0.48%	0.54%
EV/EBITDA (x)	42.76	32.50	26.38	22.13	18.77
P/FCFE (x)	23.63	623.04	68.36	43.34	37.13
Net Gearing	(30.9%)	(20.5%)	(25.7%)	(33.0%)	(39.0%)
P/BV (x)	11.80	9.78	8.03	6.58	5.43
ROE	19.0%	21.0%	21.6%	21.2%	20.3%
% Change In Core EPS Estimates			5.44%	9.17%	
InCred Research/Consensus EPS (x)					

SOURCE: INCRED RESEARCH, COMPANY REPORTS

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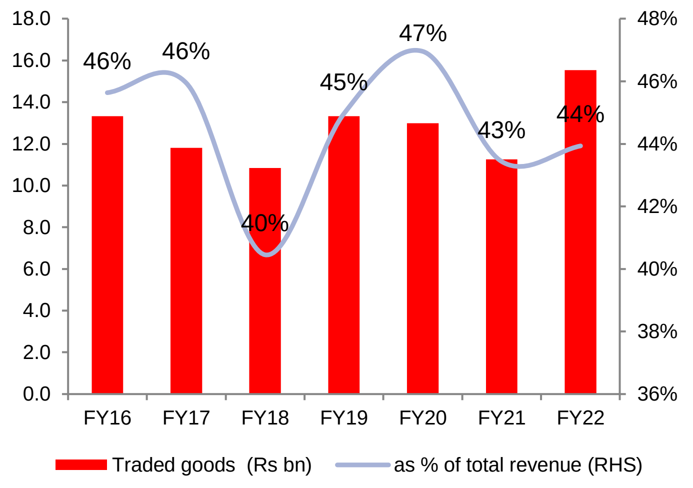
FY22 annual report analysis

Strong end-market demand, increased market penetration and cost-saving measures led to overall better financials, despite various challenges ›

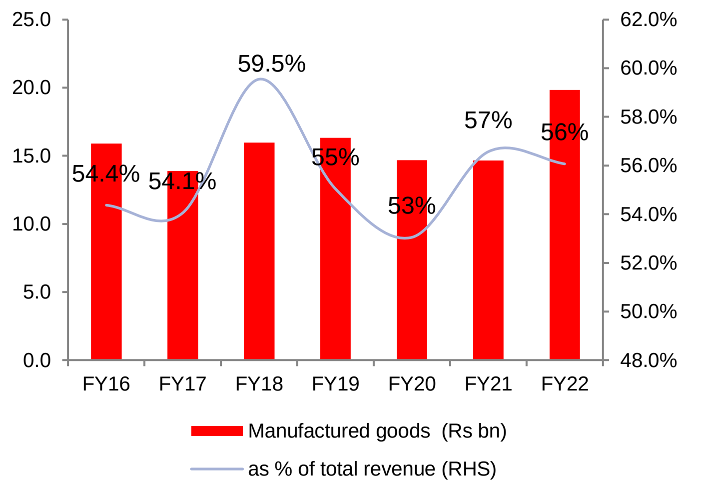
- **FY22 sales:** Overall sales grew 36.5% yoy aided by market share gains which, along with strong cost discipline and cost efficiency, led to strong financial performance.
- **Traded goods' share in overall sales increased marginally from 43.4% in FY21 to 43.9% in FY22 compared to higher growth and a rise in share of the industrial segment yoy;**
  - **Traded goods: Of the overall 36.5% rise in overall sales during FY22, sales of traded goods rose by 38% yoy and that of manufacturing goods by 35%yoy.** This is likely because of a higher rise in sales in the industrial segment by ~39% yoy (which largely depends on traded goods) vs. ~37% rise in the auto segment (largely manufactured goods).
  - As per management, recently, automotive/industrial lines have been localized to the extent of 95%/35%, respectively. Localization of raw materials like high quality steel and components would also be key drivers for rise in the level of localization going ahead.
  - Domestic sales rose by 31% yoy, while exports grew by 112% yoy on a low base (grew by a 19% CAGR over FY20-22).
  - Sales of services grew 61% yoy (three-year CAGR of 27%) to Rs661m (1.8% of sales in FY22 vs. 1.6% in FY21 and averaging at 1.1% over FY17-20).
  - **Exports formed 11.8% of sales in FY22 vs. 7.6% in FY21** (export share average was 8.5% in last 10 years). Robust exports in FY22 were because of the following: **a) In FY22, the company developed and launched many new products for European and Asian automotive customers, and volume was ramped up from 2HFY22. b) SKF factories in the SEA region and Europe were witnessing strong demand and these factories requested SKF India's factories to support production.** The company continues to explore a new product range for overseas customers. Major exports are to automotive OEMs, the industrial aftermarket segment in Europe, and to automotive and industrial aftermarket customers in Asia, Brazil, and USA. However, management hinted that the SKF group globally has always believed that it should be as close to its customers as possible and hence, domestic market would be a key focus area and not export market.

Figure 1: Sales of traded goods, as a % of total sales, increased by 50bp yoy to 43.9% in FY22



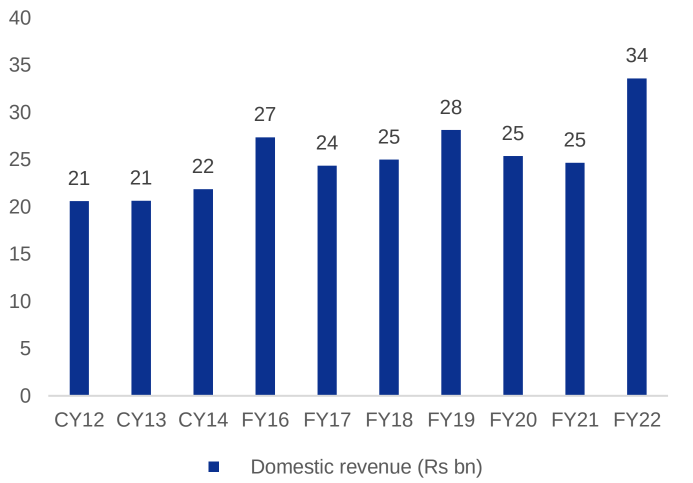
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 2: Sales of manufactured goods grew 35% yoy in FY22



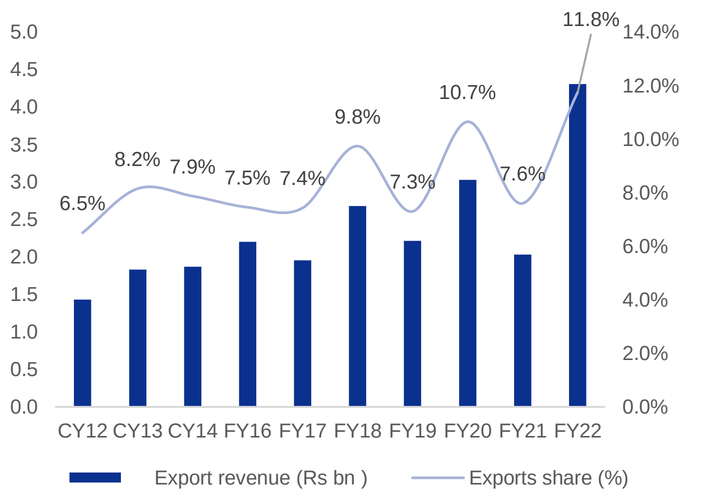
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 3: Domestic revenue grew 31% yoy in FY22



SOURCE: INCRED RESEARCH, COMPANY REPORTS

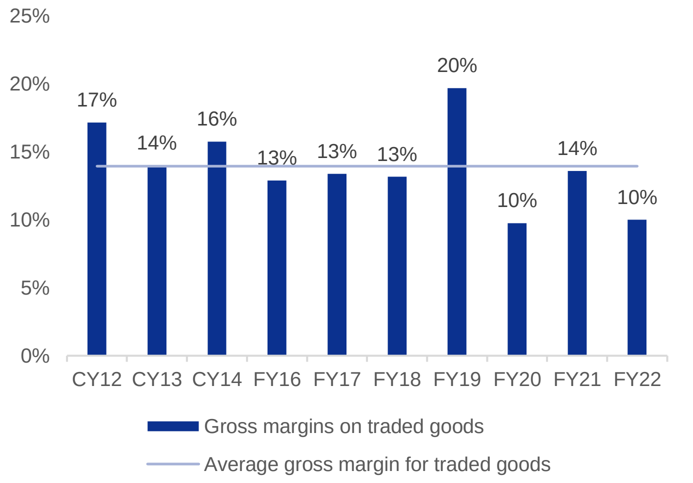
Figure 4: FY22 exports grew 112% yoy led by launch of new products and increased demand from sister companies



SOURCE: INCRED RESEARCH, COMPANY REPORTS

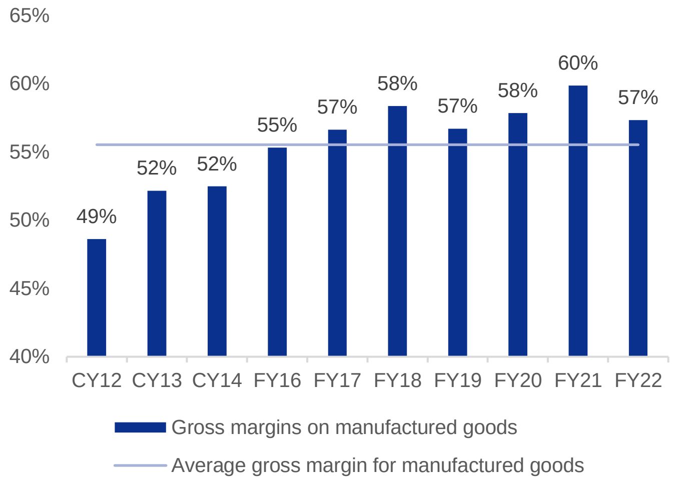
- **Gross margin:** FY22 gross margin declined by 279bp yoy due to the decline in gross margin on traded goods (359bp yoy) and manufacturing goods (254bp yoy on a high base) mostly due to elevated commodity prices and supply chain problems. Traded goods' margins stood at 10% in FY22 vs. 13.6% in FY21 and was also lower than the 10-year average of 13.9% over FY12-22. **Traded goods inventory stood at an all-time high of Rs1.19bn in FY22. The company's manufactured goods' gross margin declined by 254bp on a high base to 57.3%, which was still in line with the average gross margin trend over FY16-20, despite commodity pressure on likely support of high exports.**
  - As per management, the company implemented price hikes to mitigate some of the input cost inflation impact, and it will continue to implement more of these hikes, as needed, to recover from the impact of raw material cost inflation. The company also worked to mitigate supply chain constraints and related inefficiencies. However, full cost recovery will take time, given the persistent inflationary trend and the uncertainty created by the current global geopolitical situation.

Figure 5: Gross margin on traded goods declined by 359bp yoy and has been volatile since last four years



SOURCE: INCRED RESEARCH, COMPANY REPORTS

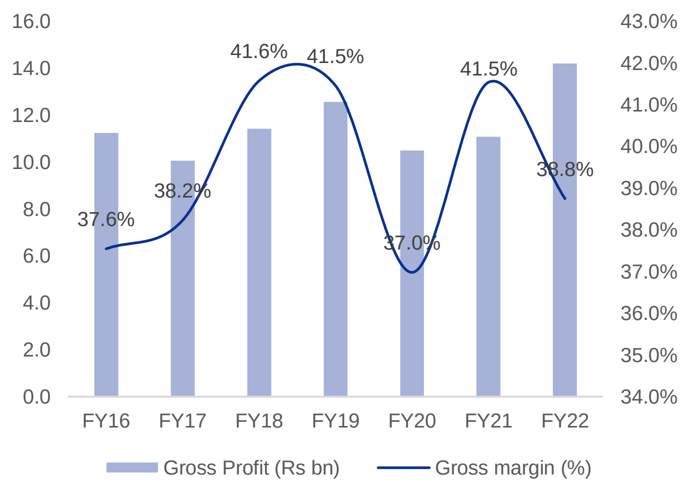
Figure 6: Gross margin on manufactured goods was down by 254bp yoy on a high base but still in line with the historical trend, despite commodity pressure



SOURCE: INCRED RESEARCH, COMPANY REPORTS

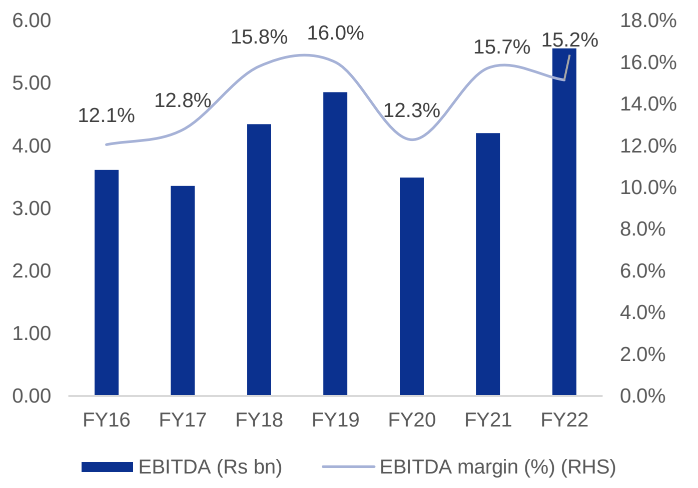
- **EBITDA margin:** It stood at 15.2% (-57 bp yoy) in FY22, despite a sharp decline in gross margin (-279bp) aided by operating leverage as personnel/ other expenses increased by 16%/30.7%, respectively, vs. sales growth of 37%. The number of employees declined by 4.5% in FY22, and their average salary increased by 21.5% yoy. Among other expenses, as a % of sales, the costs were lower yoy in case of power & fuel, repair, IT services, legal fees, and logistics.

Figure 7: Gross profit margin declined sharply in FY22



SOURCE: INCRED RESEARCH, COMPANY REPORTS

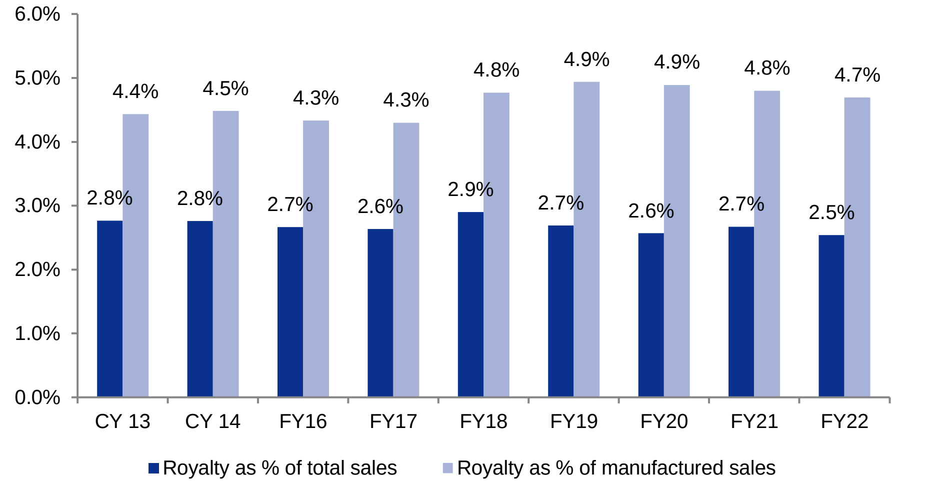
Figure 8: Operating leverage aided EBITDA margin decline by a mere 57bp, despite a sharp gross margin fall



SOURCE: INCRED RESEARCH, COMPANY REPORTS

- **Other income:** It declined by 5% yoy to Rs344m as the cash balance reduced due to a high one-time dividend payout during FY21 and increased working capital requirement in FY22.
- **Royalty & trademark fees:** SKF India's royalty and trademark fees have been stable over the last few years, at 2.6% of overall sales in FY22 (vs. 2.7% of sales in FY21) and at **4.7% of manufactured goods (4.8% in FY21).**

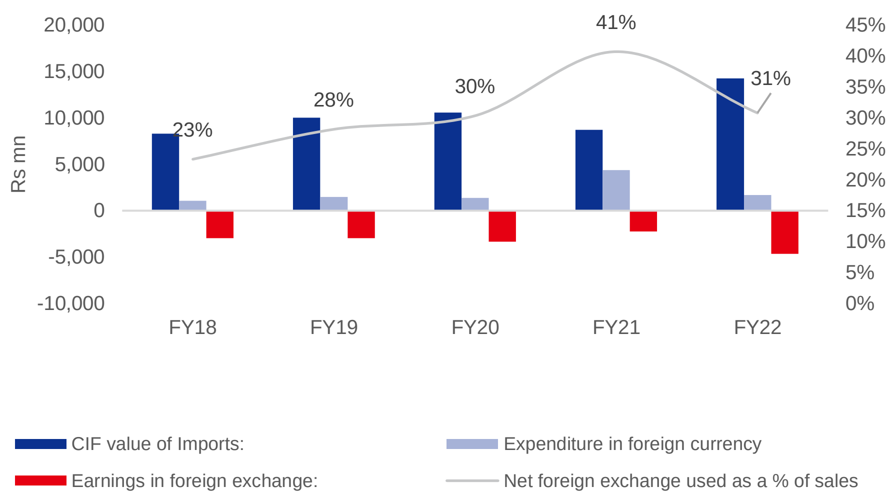
Figure 9: Royalty as a % of total sales & manufactured goods sales has been stable since last few years



SOURCE: INCRED RESEARCH, COMPANY REPORTS

- **Net forex outgo at Rs11.3bn (+4% yoy) formed 30% of FY21 sales vs. 41% of FY21 sales (which included a large one-time dividend remittance, excluding which it stood at ~29% of sales) and 30% of sales in FY20. Overall imports in FY21 grew 63% led by purchase of traded goods (but traded goods' inventory was also high at Rs1.2bn), which was** offset by increase in exports by 112% and a 62% decline in other foreign expenditure (due to one-time large dividend remittance last year).

Figure 10: FY22 forex outgo increased by 3.9% yoy due to a substantial increase in imports of traded goods by 71%, which was offset by strong growth in exports at 112%



SOURCE: INCRED RESEARCH, COMPANY REPORTS

- **Technology absorption/ product development/ import substitution:**
  - a) Truck HUB Unit (THU1) developed for commercial vehicle and series production has started operations. The launch has been done with a complete local supply chain and robotic technology assembly set-up developed in India.
  - b) New channel mDGBB Range (52-100mm) based on low-noise technology has been installed and series production has started.
  - c) mDGBB (100-140mm) capacity addition done by adding new machines.
  - d) Pinion unit developed for truck ramp-up done with robotic assembly set-up.

- e) New DGBB manufacturing transfer channel installation, which will increase the capacity by 10m bearings, has been completed**.**

- **Remuneration:** The percentage increase in median remuneration of employees in FY22 was 8.8% vs. 59% for managing director and 6.7% for chief financial officer.
- **Net working capital (ex-cash and loans & advances to related parties) stood at Rs9.4bn (+67% yoy) and at 93 days of sales in FY22 vs. 77 days of sales in FY21 due to higher inventory days (from 64 in FY21 to 67 in FY22) offset by a sharp decline in creditor days which has normalized after a high base last year** (from 79 days in FY21 to 52 in FY22). **Traded goods inventory stood at an all-time high of Rs1.19bn in FY22.** Net working capital (ex-cash and loans & advances to related parties) increased from 33-38 days of sales in CY10-14 to ~61-75 in FY16-20 due to higher inventory and debtor days (apart from the change in revenue accounting post goods and services tax or GST). Loans & advances of SKF Engineering and Lubrication India Pvt Ltd (previously SKF Technologies) stood at Rs856m in FY22 vs. Rs871m in FY21, Rs1.27bn in FY20 and Rs1.45bn in FY19.

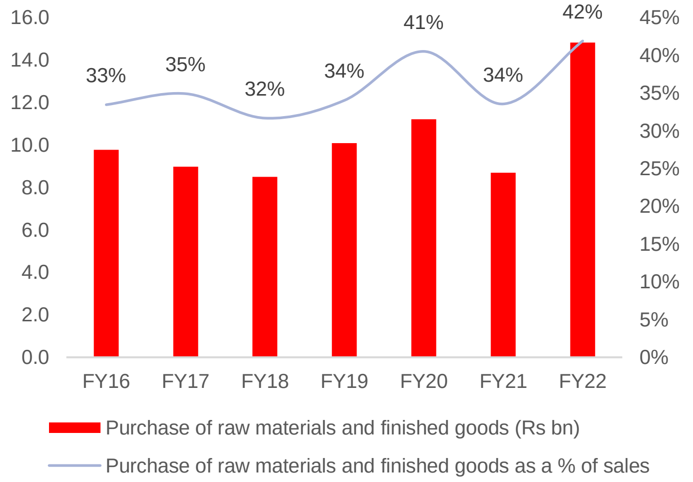
Figure 11: Net working capital ex-cash (on days of sales)

NWC (ex-cash) (on days of sales)	CY14	FY16	FY17	FY18	FY19	FY20	FY21	FY22
Inventories	44	51	58	53	55	58	64	67
Sundry Debtors	56	73	71	65	63	56	80	68
Loans and Advances:	10	23	23	21	17	16	12	9
Others:	2	16	17	20	18	29	32	30
Current Assets	**113**	**163**	**169**	**159**	**154**	**160**	**187**	**174**
Sundry Creditors	51	44	42	52	42	53	79	52
Provisions:	11	7	8	7	7	9	7	2
Operating Other Current Liabilities	13	12	14	11	12	8	12	18
Current liabilities	**75**	**64**	**64**	**69**	**61**	**70**	**99**	**72**
NWC (ex-cash)	**38**	**100**	**105**	**90**	**93**	**90**	**89**	**102**
Net working capital (excluding L&A to related party) (Rs m)	**2,494**	**5,023**	**5,966**	**5,209**	**6,251**	**5,748**	**5,616**	**9,358**
Net working capital days	**38**	**61**	**83**	**69**	**75**	**74**	**77**	**93**
Net working capital - % of sales	**10%**	**17%**	**23%**	**19%**	**21%**	**20%**	**21%**	**26%**

SOURCE: INCRED RESEARCH, COMPANY REPORTS

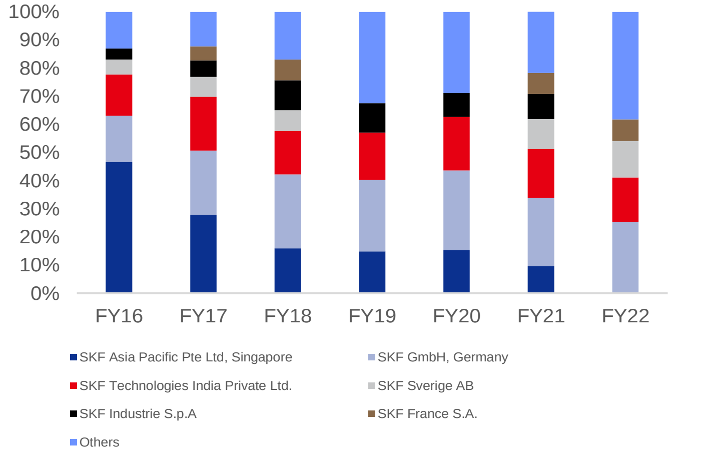
- **SKF Engineering and Lubrication India Pvt Ltd (formerly SKF Technologies India Private Ltd), Ahmedabad (a 100% subsidiary of the parent):** Almost 16% of its traded goods came from Ahmedabad unit in FY22 vs. 17% in FY20 and an average 17% over FY17-22. Management recently said that about 25% of industrial bearings sold were manufactured in Ahmedabad (big bearings mainly for railway and wind segments) and rest of them were manufactured in Pune and Bengaluru units.
- **Other related-party transactions:**
  - Raw material/ finished goods purchased increased by 70% yoy, with purchases from SKF Germany (+78% yoy) forming 25% of raw materials purchased in FY22, in line with the historical average of 25% over FY17-22, and purchases from SKF Sverige AB increased by 106% yoy, forming 13% of total purchases.
  - Sales of goods to related parties from SKF India were up 120% yoy in FY22 on a low base (up 41% from FY20) with a major increase to SKF European Distribution Centre (+218% yoy), forming 24% of total sales of goods vs. 17% in FY21 and 11% in FY20. Also, sales to SKF do Brasil Ltd increased by 196% yoy and formed 12% of total sales of goods to related parties in FY22 vs. 9% in FY21. Sales of goods to SKF Germany formed 12% (vs. 14% in FY21), SKF USA accounted for 10% (vs. 16% in FY21) and SKF Industrie Spa accounted for 7%. **SKF factories in the SEA region and Europe witnessed strong demand and they requested SKF India's factories to provide support in production**.

Figure 12: Purchases from related parties as a % of sales increased to 42% of sales in FY22 vs. 34% in FY21



SOURCE: INCRED RESEARCH, COMPANY REPORTS

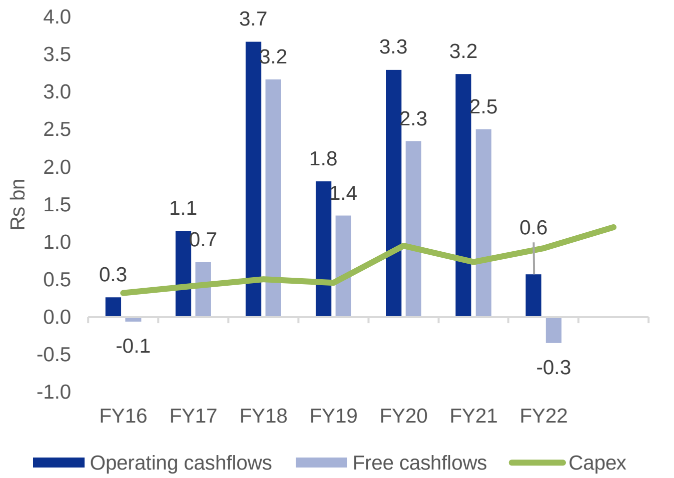
Figure 13: SKF Technologies' share in overall purchases in FY22 stood at 15.9%, almost in line with last six-year average of 16.9%



SOURCE: INCRED RESEARCH, COMPANY REPORTS

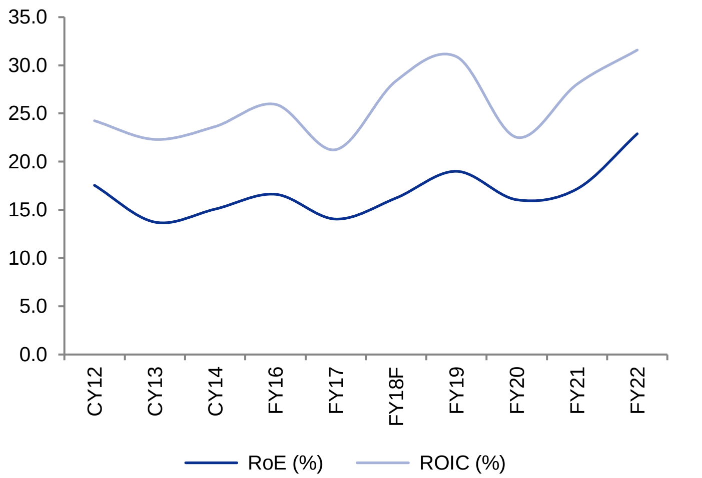
- **Capex** stood at Rs916m in FY22 vs. Rs736m in FY21, while the average capex spending was ~Rs870m over FY20-22 vs. ~Rs460 m over FY17-19. SKF is continuously devising new ways to improve its facilities by investing in flexible, automated, and connected factories, as well as localizing production on a region-by-region basis. The company is aiming at greater localization of industrial products.
- **Net cashflow** from operations declined to Rs571m in FY22 vs. Rs3.2bn in FY21 due to deterioration in net working capital, mainly led by high inventory, which is expected to normalize in FY23F.
- **RoE improved to 22.9% in FY22** from 17.2% in FY21 and the recent peak of 19% in FY19, led by a 33% yoy growth in PAT and a large dividend payout in FY21.

Figure 14: Operating and free cashflow saw a significant decline in FY22 due to deterioration in working capital



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 15: Return ratios improved due to strong PAT growth and a large dividend payout



SOURCE: INCRED RESEARCH, COMPANY REPORTS

- **Environmental sustainability: SKF's global strategy is to become carbon neutral by 2030F** at all its manufacturing sites across the globe. SKF India has framed strategies for lean, green, and digital operations, and formed partnerships to purchase power from renewable sources **(42% of its energy requirement is met from renewable sources and the target is to touch 75% by FY25F).**
- **SKF group's strategic framework:** SKF group continues to stride towards its 2025F strategy, which revolves around **six focus areas – digitalization, new business models, innovation, world-class manufacturing,**

cleantech, and the future workforce. The focus remains on turning more innovative, growth-focused and a profitable industrial player by **targeting segments and products where it can provide significant value** to customers. It **plans to double the business by 2030F, with improved margins.** The strategic framework is based on two concepts**: intelligent** (connected and tailored offerings) and **clean** (enable a more sustainable industry) driven by focusing on high-growth segments, new technologies, services and aftermarket, and portfolio management.

- **SKF to identify key market drivers and solutions for the same which includes: a) sustainability** whereby SKF helps customers to move towards a circular economy by providing condition monitoring, rotation-as-a-service, and remanufacturing services, b) **electrification** which enables robust and efficient e-power train drives, of which bearings are an essential component, c) **digitalization** - its investments in connecting the value chain are helping improve the ease of doing business with SKF, and d) **regionalization** - customization of business strategy and approach is becoming essential coupled with a continued shift in economic power, making it necessary **to adopt a region-specific approach. SKF is making regular investments in automation and regionalization of its manufacturing footprint and product development**.
- **Rotating equipment performance (REP) segment's value proposition** is a commercial relationship where SKF provides the customer with functionality at a fixed recurring fee, leveraging the full SKF portfolio: bearings, seals, lubrication systems, remanufacturing, oil regeneration and many other engineering services.
  - The company meets product application needs as well as performance requirements on specific metrics such as speed, load, noise, and physical environment for customers to maximize the performance.
  - SKF offers tailored and asset-aware machine service through its lifecycle to customers via comprehensive performance-based agreements.
  - SKF has, in recent years, accelerated its REP business growth across Asia, including India. It offers different service levels to choose from, which are aligned to meet the unique performance needs of customers.
- **Key innovations in FY22:**
  - **SKF Unitized Solution - Wheel unit** used SKF tapered bearing unit, having integral premium quality rubber seals and filled with grease, which is sealed for life, and it is used on wheels of the pallet car used in a steel sintering plant. It reduced the need for maintenance, increased uptime and reliability, led to savings in grease usage, is environmentally friendly, safer to handle and comes as a ready mount unit. It can reduce grease consumption from 3,200kg/year to 920 kg/year and the solution will increase the bearing Mean Time Between Failures - (MTBF) to two years from three-to-six months currently. It will go into field validation in the first quarter of FY23F.
  - **Quiet-running deep-groove ball bearings:** SKF India launched low-noise and low-vibration bearings for electrical motors. New deep-groove ball bearings are designed to reduce vibration, friction, and noise in electric motors used in a range of applications such as elevators, healthcare, and EV.
- **New business wins:**
  - **Wheel-end business win for Intermediate and Light Commercial Vehicle (ILCV)-** A SKF global customer, who implemented THU1S in its heavy-duty trucks, has also decided to implement THU1S for its ILCV range of vehicles.
  - **Automatic dual clutch transmission business –** SKF India won a contract to cater to bearings and seals requirement to support manufacturing of dual clutch transmission for the passenger vehicle segment in India of a global customer having a strong presence in the EU and China, who established a powertrain assembly plant in India.

- **Wheel-end bearings and seals:** SKF India is supplying wheel-end bearings and seals for wheel-end and engine under the customer's global sourcing programme from India, catering to Europe, Africa, and other geographies.
- **HBU3 modular unit for a renowned EV manufacturer:** A renowned light electric commercial vehicle (ECV) manufacturer was facing problems with wheel-hub mounting and fitment in its load carrier electric three-wheeler, a field-related issue. SKF proposed its HBU3 modular unit which is an integrated 'ready to mount' unitized application for wheel-ends addressing all problems of customers.

- **Manufacturing:** SKF wants its operations close to customers to ensure a shorter lead time and transportation. It is working on modernization of its factories and footprint transformation to provide the right products at the right quality, at the right cost and at the right time to its customers.
  - Bearings produced in FY22: 135m vs. 118.2m in FY21.
  - New products in pipeline: 50 in FY22 vs. 113 in FY21.
  - Customer delivery lead time for stock items: 1-3 days
  - Refurbished/remanufactured bearings for customers: 20,179.
  - Total capacity is 183m.
- **Remanufacturing:** Remanufacturing can offer considerable benefits, including lower life-cycle cost and less unwanted downtime, especially if remanufacturing is combined with other SKF services and technologies for many medium-to-large-size bearings used in several demanding industries. Significant amount of energy savings (up to 90%) and cost savings can be achieved with remanufacturing depending on bearing size and complexity. Indian Railways used the TBU 130 X 230 product for its LHB coach's axle bearing. SKF India has recycled 564 tonnes of steel and 20,000 bearings which benefitted Indian Railways in terms of increased profitability, enhanced machine uptime, lower opex and reduced maintenance**.**
- **Aftermarket service:** Increased market penetration has been a focus area for SKF India. SKF automotive aftermarket business unit has launched five new products. As per management, in recent client interactions the company has put a lot of efforts to get into the large distribution model and create pull model from mechanics and retailers. The company aspires to increase its market share from low digit or high single digit currently to mid-20% by facilitating availability, distribution reach, pricing, product etc. **New products include:**
  - Chain and sprockets for motorcycles.
  - Steering and suspension for passenger cars.
  - Timing belt for passenger cars.
  - CVT belt for scooters.
  - Poly V belt for passenger cars.
- **Industrial reach**: Currently, the company's distributors serve about 10,000 postal pin code areas out of 20,000 in India and would increase the number of distributors serving in the pin code areas not being served yet.
- **Lubrication business**: SKF's innovative lubrication solutions are helping customers improve the lifetime of their bearings. SKF lubrication solutions range from specialized lubricants to state-of-the-art lubrication systems.
  - **Roll gap lubrication system for a steel major** was introduced to address the latter's major problem of premature failure of bearings because of steep temperature increase at the rollers in its hot strip mills. The system consists of two electrically-driven pumps to spray oil and water, as and when required, for proper and consistent lubrication and cooling as per the set time intervals. It helps to reduce the roller temperature and minimize the wear and tear, leading to lower maintenance and equipment breakdown, and higher ROI.
  - **RecondOil**: With RecondOil, SKF delivers an innovative product to turn the environmentally harmful use of industrial oil into an asset that can be used repeatedly with maintained performance. Taking the circular

approach one step further, SKF introduced its patented Double Separation Technology (DST), which turns industrial oil from a costly consumable into a reliable, circular asset.

- **Bearings market:**
  - The total Indian bearings market, comprising both ball bearings and roller bearings, was valued at US$1.8bn in 2021. The market for bearings has gained significant impetus led by growing usage of bearings in motors and the rising popularity of electric vehicles (EVs), apart from push to manufacturing due to government initiatives such as 'Make in India'. The automotive segment dominated the market and held ~50% share in 2021.
  - The Indian bearings industry is expected to grow at a 10.9% CAGR to touch US$3.4bn by 2027F. Robust demand in automotive, construction and mining equipment markets is expected to boost the ball bearings market. Rising demand for high-precision bearings in specific applications and various end-user requirement for insulation against an extreme environment.
  - **Opportunities:** Improved demand for bearings from passenger vehicle or PV, commercial vehicle or CV, three-wheeler or 3W segments and from other large industries, thrust on local production, rising demand from aerospace and corresponding industries, usage of miniature bearings in robots and technological evolution in automation and medical equipment sectors may drive growth for the bearings sector. Also, the integration of sensors with bearings has evolved into demand for smart bearings.
- **Outlook:**
  - **Auto segment outlook:** Federation of Automobile Dealers Associations (FADA) expects the Indian auto industry to reach pre-pandemic highs by FY24F. Supply chain disruption due to global semiconductor shortage may not dent demand for cars in the PV segment but is expected to impact the extremely price-sensitive 2W segment. On the other hand, the 3W segment is also witnessing a shrinking market due to the tactical shift from Internal Combustion Engine (ICE) to EV, as reflected by 45% of the 3W market being driven by EVs. The uptick in the CV segment indicates early signs of economic recovery at large, driven by increased government spending on infrastructure activity in both rural and urban areas. The near-term outlook will continue to remain challenging due to the ongoing Russia-Ukraine war and rising fuel prices. The government's thrust on capital expenditure in FY23F can act as a game changer by enhancing productive capacity, crowding in private investment, and strengthening aggregate demand.
  - **Railways:** In FY22, Indian Railways set new milestones in various categories, including freight loading, electrification, new lines and locomotive production. Indian Railways is looking at electrification of its entire network by 2023F, 2,843km of dedicated freight corridors by Jun 2022F, and 400 new-generation Vande Bharat Trains are to be manufactured. The National Rail Plan (NRP) is aimed to formulate strategies based on both operational capacity and commercial policy initiatives to increase the modal share of railways in freight. The objective of the plan is to create capacity ahead of demand.
  - **Capital goods industry:** With a gradual improvement in fresh announcements of capex and execution of existing projects on the ground, demand for short-cycle products such as bearings, pumps, material handling equipment, construction equipment, abrasives, etc. is likely to witness an uptick. Increased budgetary outlay for capital expenditure would have a cascading effect, in our view, and boost order backlog of industrial companies.
  - **Overall outlook**: SKF India is optimistic about sustaining its growth momentum across both automotive and industrial segments considering the buoyancy in the Indian economy. Despite challenges such as supply

chain constraints and rising commodity prices, the industry is showing positivity on the back of favourable government policies and consumer sentiment.

SKF global company's CY21 annual report highlights

Parent's regionalization strategy gels well for SKF India

SKF (parent company) presented a new strategic framework 2030 based on two broad concepts- intelligent and clean - which will be the guiding factors to become a more focused, innovative, and profitable player. **The company aims to grow faster and double its business, with improved margins, by 2030F**. It has laid emphasis on profitable growth by targeting industries with high potential, re-positioning auto business (take the lead in growing EV, CV, and aftermarket segments), developing products for emerging industries, strengthening its service business and trim low-return businesses. Technology, digitalization, regionalization, and efficiency were the enabling factors to achieve its target.

SKF (parent company) aims regionalization in Asia to increase from around 60% to more than 85%, so to be closer to its customers and be competitive, which gels well for SKF India (where traded goods accounts for ~45% of overall sales). New model structure places end-to-end operational and financial accountability as close to its customers as possible, where India is one of key growth potential markets.

- **Strategic Framework 2030:**
- SKF's Strategic Framework 2030 is based on two concepts: **a) intelligent** - means providing connected and tailored offerings for customers and using technology to make operations more efficient (portfolio management, digital value chain & processes, capital allocation), and **b) clean -** reflects the ability to enable a more sustainable industry, while running its own business in a transparent and responsible manner (tech applications, minimize friction and eliminate waste). These concepts will serve as a guide to become an **even more focused, innovative, and a profitable industrial player.**
- **Target by 2030F: Aims to grow faster and double its business, with improved margins.**
- **Prioritizes growth areas for acceleration of profitable growth by laying emphasis on:**
  - Targeting industries with high growth potential, where the company has a strong market position and competitive edge, e.g. high-speed machinery, electric drives, agriculture, wind energy equipment, railways, food & beverage and robotics & automation.
  - Repositioning the automotive business to profitable and growing segments where the company has a lead, including electric vehicles, commercial vehicles, and aftermarket parts business.
  - Developing offers for emerging industries such as hydrogen processing and carbon capture, where the company is already well positioned through existing technologies such as magnetic bearings.
  - **Strengthening the foundation for recurring revenue by simplifying service offering, addressing a wider market**. New technology and partnerships will provide scale and easy access to the company's data analysis and machine performance competence.
  - **Would be either improving or trimming** the parts of its business which are not generating sufficient returns.
- **Enablers for growth agenda:**
  - **Accelerate technology development** - plans to increase R&D expenditure by around 50% over time.
  - **Digitalize full value chain** - connecting the value chain: customers, sales, logistics, manufacturing, supply chain and R&D.
  - **Regionalized and competitive supply chain - regionalization in Asia will grow from around 60% to more than 85%,** and for Americas from around 40% to around 60%, further improving competitiveness.

Investment would be funded by improving working capital and cost reduction.

  - **Operate more efficiently** – closer to customers: New model structure places end-to-end operational and financial accountability as close to its customers as possible- a) **Four industrial regions - Americas, EMEA, India & Southeast Asia, and China & Northeast Asia -** further enhancing the ability to serve customers with increased speed and responsiveness, b) One global automotive business: Creating the accountability and transparency needed to improve profitability and refocus the portfolio, c) Six independent and emerging businesses: Seals, Lubrication, Aerospace, Marine, Magnetic Bearings, RecondOil, and creating the focus needed to seek growth opportunities also beyond the rotating shaft, and d) lean central function, providing global support.

- **Trends and drivers**: Sustainability (move to circular economy), electrification (e-powertrain drive solutions), digitalization (shorter lead time, faster development cycle, lower inventories, connecting overall value chain for efficiency), and regionalization (close to customer).
- **CY21 performance:** It has shown a rebound in post-pandemic demand within industrial, but also exceptional pressure throughout the supply chain, logistics constraints and significant cost inflation, while the automotive segment has added uncertainty of large OEM customers cancelling orders at very short notice. The company invested in making factories more automated, more digitalized and added manufacturing capability closer to customers in both Americas and Asia.
- **EV business segment:** The company is partnering with key OEMS and Tier-1 pioneers for the launch of full EVs by providing a complete package offering of bearings and seals featuring high speed, thin sections, and electric current insulation options. The company's leading low-friction solutions (reducing power loss by 35%) for EV motors, drivetrains and wheel bearings are key enablers to increase the vehicle range, and technology transformation towards a CO2-neutral vehicle market.
- **Long-term revenue growth/margin target:** The company aims at achieving target operating margin of 14%. Acceleration of footprint optimization, automation, regionalization, and cost competitiveness, supported by new ways of working would help in achieving the long-term target margin. Targets revenue CAGR of 5% aided by increasing value to the customer, new businesses like cleantech, RecondOil, electrification and new acquisitions.
- Sustainability objectives: The company announced two important milestones in future work with regards to its operations- achieving net zero emission from own operations by 2030F as well as achieving a net zero supply chain by 2050F. The company is already working on fossil-free steel, which is the biggest source for change in emission. It offers products, solutions and services that help machines run smoother, with less emission, enabling the growth of clean technologies such as renewable energy and electric vehicles as well as enable significant energy and carbon savings for customers by making products lighter, more efficient, longer lasting, and repairable.
- **Enabling circular economy with new technology through acquisition**: Acquiring the Belgian-based Laser Cladding Venture N.V. (LCV) specialized in various laser cladding technologies and processes will support SKF's service and remanufacturing offering. Laser cladding makes it possible to repair metal surfaces and to mix various types of metals for tailored surface layers.

Global bearings market and SKF's position

- **Industrial segment sales, accounting for 72% of total sales** (accessible bearings market size of SEK 275 –295bn (US$27.8-30bn), grew at 12-14% in CY21).
- **Auto sales forms 28% of total sales** (accessible market SEK 125 –145 bn (US$15.8-17bn), which grew 5-7% yoy in CY21.

- **Geographical market size**: Total estimated global bearing market size is SEK410bn-430bn (estimated to have grown by 10%-12% during 2021). Europe - SEK 80-90bn (20% share, of which Germany accounts for 31%), North America - SEK 75-85bn (19% share), Asia and Pacific- SEK 220-240bn (56% share, of which China has a 34% share of the total world), Latin America at 2%, and Middle East & Africa at 3%.
- **Overall bearings market**: Industrial OEMs account for 40%, auto OEMs 30% and distribution accounts for the balance 30%.
- **SKF's leading position globally**- Industrial: railway, heavy industries industrial distribution market; Auto: one of the leaders in components for automotive electrification and wheel-end solutions and a strong position in application-driven powertrain solutions, aftermarket.
- **Market drivers: For industrial-** reliable rotations, climate change-led industrial portfolio, low friction, energy use, maintenance-free solutions, digital monitoring, and predictive maintenance. **For auto**: electrification, energy efficiency and reduction of emissions for light vehicle market, total cost of ownership, integrated system for truck, and changing buying patterns, new channels, cost optimization for aftermarket.
- **Competition: SKF estimates that top six world bearings manufacturers represent about 55% of global roller bearings market.** The group of Chinese bearings companies, including small and larger ones, represents around 25%, with the main portion of their sales in Asia. The remaining 20% includes many smaller regional and niche bearings companies.
- Market value by region: Europe/ North America/ Asia Pacific/ Latin America/ Middle East & Africa have 20%/19%/56%/ 2%/ 3% share, respectively, in world bearings market. Asia's share of the world's bearings market has continued to grow rapidly and now accounts for around 55%, compared with less than 40% almost 20 years ago.

Figure 16: Earnings revision summary

Rs (m)	Old Estimates		New Estimates		Change	
	FY23F	FY24F	FY23F	FY24F	FY23F	FY24F
Revenue	37,265	41,868	43,344	48,944	16.3%	16.9%
EBITDA	6,405	7,298	6,769	7,918	5.7%	8.5%
PAT	4,711	5,453	4,968	5,953	5.4%	9.2%
EPS	95	110	100	120	5.4%	9.2%

SOURCE: INCRED RESEARCH ESTIMATES, COMPANY REPORTS

Figure 17: Peer comparison

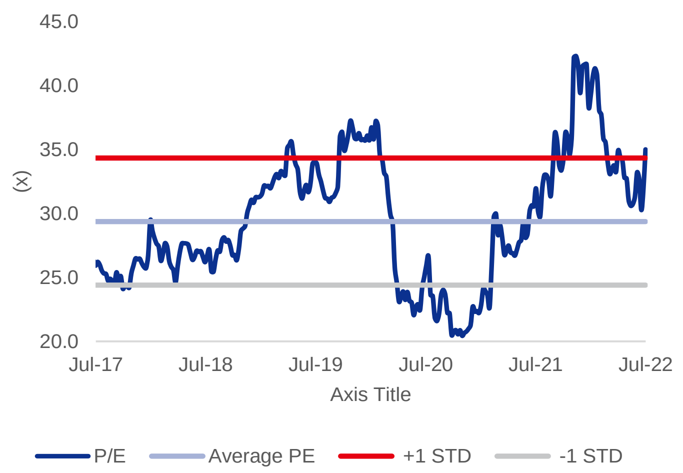
Company	Bloomberg Ticker	Recom.	Price Rs	TP Rs	Mkt cap (US$ m)	P/E (x)			P/BV (x)			EV/EBITDA (x)			Dividend Yield (%)		
						FY22F	FY23F	FY24F	FY22F	FY23F	FY24F	FY22F	FY23F	FY24F	FY22F	FY23F	FY24F
SKF	SKF IN	Add	3,732	4,200	2,306	47	37	31	9.8	8.0	6.6	33	26	22	0.4	0.5	0.5
Schaeffler	SCHFL IN	Add	2,531	2,440	4,675	63	48	41	10.8	9.3	8.0	40	31	27	0.3	0.6	0.7
Timken	TMKN IN	Hold	2,637	2,320	2,401	61	48	41	12.0	9.6	7.9	38	31	28	0.1	0.1	0.1

SOURCE: INCRED RESEARCH ESTIMATES, COMPANY REPORTS. PRICED AS ON 6 JUL 2021

Figure 18: SKF India – One-year forward P/E

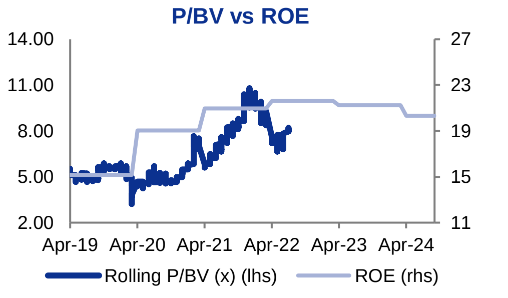
SOURCE: INCRED RESEARCH, COMPANY REPORTS

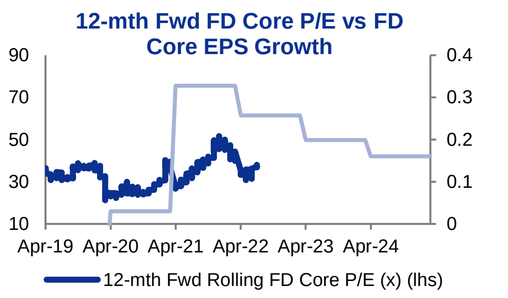
Figure 19: SKF India – current P/E above +1SD



SOURCE: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS





Profit & Loss

(Rs mn)	Mar-21A	Mar-22A	Mar-23F	Mar-24F	Mar-25F
Total Net Revenues	**26,707**	**36,659**	**43,344**	**48,944**	**54,892**
Gross Profit	**11,095**	**14,207**	**16,687**	**19,088**	**21,573**
Operating EBITDA	**4,201**	**5,557**	**6,769**	**7,918**	**9,122**
Depreciation And Amortisation	(580)	(571)	(631)	(643)	(727)
Operating EBIT	**3,622**	**4,986**	**6,139**	**7,275**	**8,396**
Financial Income/(Expense)	(21)	(21)			
Pretax Income/(Loss) from Assoc.					
Non-Operating Income/(Expense)	362	344	536	724	883
Profit Before Tax (pre-EI)	**3,963**	**5,310**	**6,675**	**8,000**	**9,279**
Exceptional Items					
Pre-tax Profit	**3,963**	**5,310**	**6,675**	**8,000**	**9,279**
Taxation	(986)	(1,358)	(1,708)	(2,047)	(2,374)
Exceptional Income - post-tax					
Profit After Tax	**2,977**	**3,951**	**4,968**	**5,953**	**6,905**
Minority Interests					
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	**2,977**	**3,951**	**4,968**	**5,953**	**6,905**
Recurring Net Profit	2,977	3,951	4,968	5,953	6,905
Fully Diluted Recurring Net Profit	**2,977**	**3,951**	**4,968**	**5,953**	**6,905**

Cash Flow

(Rs mn)	Mar-21A	Mar-22A	Mar-23F	Mar-24F	Mar-25F
EBITDA	4,201	5,557	6,769	7,918	9,122
Cash Flow from Invt. & Assoc.	(239)	(248)	(94)	82	156
Change In Working Capital	(16)	(3,614)	(1,538)	(1,140)	(1,463)
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense	580	571	631	643	727
Other Operating Cashflow	(231)	(209)	(536)	(724)	(883)
Net Interest (Paid)/Received	(21)	(21)			
Tax Paid	(1,057)	(1,486)	(1,708)	(2,047)	(2,374)
Cashflow From Operations	**3,218**	**550**	**3,523**	**4,732**	**5,286**
Capex	(736)	(916)	(1,200)	(1,200)	(1,200)
Disposals Of FAs/subsidiaries	43	9			
Acq. Of Subsidiaries/investments					
Other Investing Cashflow	5,282	654	536	724	883
Cash Flow From Investing	**4,589**	**(254)**	**(664)**	**(476)**	**(317)**
Debt Raised/(repaid)			(161)		
Proceeds From Issue Of Shares					
Shares Repurchased					
Dividends Paid	(6,427)	(717)	(840)	(890)	(989)
Preferred Dividends					
Other Financing Cashflow	(21)	(21)			
Cash Flow From Financing	**(6,448)**	**(738)**	**(1,001)**	**(890)**	**(989)**
Total Cash Generated	1,359	(442)	1,858	3,367	3,980
Free Cashflow To Equity	**7,807**	**296**	**2,699**	**4,256**	**4,969**
Free Cashflow To Firm	**7,828**	**317**	**2,860**	**4,256**	**4,969**

SOURCES: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS…cont'd

Balance Sheet

(Rs mn)	Mar-21A	Mar-22A	Mar-23F	Mar-24F	Mar-25F
Total Cash And Equivalents	5,003	4,019	5,899	9,266	13,246
Total Debtors	5,834	6,871	7,956	8,716	9,775
Inventories	4,680	6,768	8,002	9,036	10,135
Total Other Current Assets	3,185	3,841	4,386	4,842	5,326
Total Current Assets	**18,703**	**21,499**	**26,243**	**31,859**	**38,481**
Fixed Assets	4,100	4,540	5,110	5,667	6,140
Total Investments	25	25	25	25	25
Intangible Assets					
Total Other Non-Current Assets	199	222	200	200	200
Total Non-current Assets	**4,324**	**4,787**	**5,334**	**5,892**	**6,365**
Short-term Debt					
Current Portion of Long-Term Debt					
Total Creditors	5,769	5,244	6,200	7,001	7,852
Other Current Liabilities	1,444	2,023	2,391	2,700	3,028
Total Current Liabilities	**7,213**	**7,267**	**8,592**	**9,702**	**10,881**
Total Long-term Debt	176	161			
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities					
Total Non-current Liabilities	**176**	**161**			
Total Provisions					
Total Liabilities	**7,388**	**7,428**	**8,592**	**9,702**	**10,881**
Shareholders Equity	15,638	18,859	22,986	28,050	33,966
Minority Interests					
Total Equity	**15,638**	**18,859**	**22,986**	**28,050**	**33,966**

Key Ratios

	Mar-21A	Mar-22A	Mar-23F	Mar-24F	Mar-25F
Revenue Growth	(5.8%)	36.9%	20.3%	12.9%	12.2%
Operating EBITDA Growth	20.2%	32.3%	21.8%	17.0%	15.2%
Operating EBITDA Margin	16.0%	15.4%	15.6%	16.2%	16.6%
Net Cash Per Share (Rs)	97.64	78.03	119.32	187.41	267.91
BVPS (Rs)	316.30	381.45	464.93	567.35	687.01
Gross Interest Cover	170.04	239.73			
Effective Tax Rate	24.9%	25.6%	25.6%	25.6%	25.6%
Net Dividend Payout Ratio	215.9%	18.1%	16.9%	14.9%	14.3%
Accounts Receivables Days	69.64	63.25	62.43	62.17	61.48
Inventory Days	107.52	93.06	101.12	104.15	105.00
Accounts Payables Days	(115.60)	(89.52)	(78.35)	(80.70)	(81.36)
ROIC (%)	33.6%	33.3%	36.0%	38.8%	40.6%
ROCE (%)	22.9%	26.2%	26.7%	25.9%	24.7%
Return On Average Assets	13.0%	15.1%	15.7%	15.8%	15.4%

Key Drivers

	Mar-21A	Mar-22A	Mar-23F	Mar-24F	Mar-25F
Auto OEM	0.7%	16.5%	20.2%	12.2%	10.0%
Auto aftermarket	10.0%	33.0%	16.0%	12.0%	10.0%
Exports (largely Auto)	(33.0%)	111.7%	N/A	10.0%	10.0%
Total auto	(4.3%)	36.7%	14.0%	11.7%	10.0%
Industrial OEM	(10.0%)	38.0%	22.0%	14.0%	14.0%
Industrial after market	(6.0%)	39.0%	22.0%	14.0%	14.0%
Total Industrials	(10.0%)	38.0%	22.0%	14.0%	14.0%
Total sales	(8.0%)	38.5%	22.0%	14.0%	14.0%

SOURCES: INCRED RESEARCH, COMPANY REPORTS

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Corporate Governance Report of Thai Listed Companies (CGR). CG Rating by the Thai Institute of Directors Association (Thai IOD) in 2021, Anti-Corruption 2021

ADVANC – Excellent, Certified, **AMATA** – Excellent, Certified, **ANAN** – Excellent, n/a, **AOT** – Excellent, n/a, **AP** – Excellent, Certified, **ASP** – Excellent, n/a, **AWC** – Excellent, Declared, **AU** – Good, n/a, **BAM** – Very Good, Certified, **BAY** – Excellent, Certified, **BBL** – Excellent, Certified, **BCH** – Very Good, Certified, **BCP** - Excellent, Certified, **BCPG** – Excellent, Certified, **BDMS** – Excellent, n/a, **BEAUTY** – Good, n/a, **BEM** – Excellent, n/a **BH** - Good, n/a, **BJC** – Very Good, n/a, **BLA** – Very Good, Certified, **BTS** - Excellent, Certified, **CBG** – Very Good, n/a, **CCET** – n/a, n/a, **CENTEL** – Excellent, Certified, **CHAYO** – Very Good, n/a, **CHG** – Very Good, n/a, **CK** – Excellent, n/a, **COM7** – Excellent, Certified, **CPALL** – Excellent, Certified, **CPF** – Excellent, Certified, **CPN** - Excellent, Certified, **CPNREIT** – n/a, n/a, **CRC** – Excellent, Declared, **DELTA** - Excellent, Certified, **DDD** – Excellent, n/a, **DIF** – n/a, n/a, **DOHOME** – Very Good, Declared, **DREIT** – n/a, n/a, **DTAC** – Excellent, Certified, **ECL** – Excellent, Certified, **EGCO** - Excellent, Certified, **EPG** – Excellent, Certified, **ERW** – Very Good, Certified, **GFPT** - Excellent, Certified, **GGC** – Excellent, Certified, **GLOBAL** – Excellent, n/a, **HANA** - Excellent, Certified, **HMPRO** - Excellent, Certified, **HUMAN** – Good, n/a, **ICHI** – Excellent, Certified, **III** – Excellent, Declared, **INTUCH** - Excellent, Certified, **IRPC** – Excellent, Certified, **ITD** – Very Good, n/a, **IVL** - Excellent, Certified, **JASIF** – n/a, n/a, **JKN** – n/a, Certified, **JMT** – Very Good, n/a, **KBANK** - Excellent, Certified, **KCE** - Excellent, Certified, **KEX** – Very Good, Declared, **KKP** – Excellent, Certified, **KSL** – Excellent, Certified, **KTB** - Excellent, Certified, **KTC** – Excellent, Certified, **LH** - Excellent, n/a, **LPN** – Excellent, Certified, **M** – Very Good, Certified, **MAKRO** – Excellent, Certified, **MC** – Excellent, Certified, **MEGA** – Very Good, n/a, **MINT** - Excellent, Certified, **MTC** – Excellent, Certified, **NETBAY** – Very Good, n/a, **NRF** – Very Good, Declared, **OR** – Excellent, n/a, **ORI** – Excellent, Certified, **OSP** – Excellent, n/a, **PLANB** – Excellent, Certified, **PRINC** – Very Good, Certified, **PR9** – Excellent, Declared, **PSH** – Excellent, Certified, **PTT** - Excellent, Certified, **PTTEP** - Excellent, n/a, **PTTGC** - Excellent, Certified, **QH** – Excellent, Certified, **RAM** – n/a, n/a, **RBF** – Very Good, n/a, **RS** – Excellent, Declared, **RSP** – Good, n/a, **S** – Excellent, n/a, **SAK** – Very Good, Declared, **SAPPE** – Very Good, Certified, **SAWAD** – Very Good, n/a, **SCB** - Excellent, Certified, **SCC** – Excellent, Certified, **SCGP** – Excellent, Declared, **SECURE** – n/a, n/a, **SHR** – Excellent, n/a, **SIRI** – Excellent, Certified, **SPA** – Very Good, n/a, **SPALI** - Excellent, Certified, **SPRC** – Excellent, Certified, **SSP** - Good, Certified, **STEC** – Excellent, n/a, **SVI** – Excellent, Certified, **SYNEX** – Very Good, Certified, **TCAP** – Excellent, Certified, **THANI** – Excellent, Certified, **TIDLOR** – n/a, Certified **TISCO** - Excellent, Certified, **TKN** – Very Good, n/a, **TOP** - Excellent, Certified, **TRUE** – Excellent, Certified, **TTB** - Excellent, Certified, **TU** – Excellent, Certified, **TVO** – Excellent, Certified, **VGI** – Excellent, Certified, **WHA** – Excellent, Certified, **WHART** – n/a, n/a, **WICE** – Excellent, Certified, **WORK** – Good, n/a.

- CG Score 2021 from Thai Institute of Directors Association (IOD)
- Companies participating in Thailand's Private Sector Collective Action Coalition Against Corruption programme (Thai CAC) under Thai Institute of Directors (as of August 5, 2021) are categorised into: companies that have declared their intention to join CAC, and companies certified by CAC.

Recommendation Framework

Stock Ratings	Definition:
Add	The stock's total return is expected to exceed 10% over the next 12 months.
Hold	The stock's total return is expected to be between 0% and positive 10% over the next 12 months.
Reduce	The stock's total return is expected to fall below 0% or more over the next 12 months.

The total expected return of a stock is defined as the sum of the: (i) percentage difference between the target price and the current price and (ii) the forward net dividend yields of the stock. Stock price targets have an investment horizon of 12 months.

Sector Ratings	Definition:
Overweight	An Overweight rating means stocks in the sector have, on a market cap-weighted basis, a positive absolute recommendation.
Neutral	A Neutral rating means stocks in the sector have, on a market cap-weighted basis, a neutral absolute recommendation.
Underweight	An Underweight rating means stocks in the sector have, on a market cap-weighted basis, a negative absolute recommendation.

Country Ratings	Definition:
Overweight	An Overweight rating means investors should be positioned with an above-market weight in this country relative to benchmark.
Neutral	A Neutral rating means investors should be positioned with a neutral weight in this country relative to benchmark.
Underweight	An Underweight rating means investors should be positioned with a below-market weight in this country relative to benchmark.