

Avalon Technologies

Estimate change	↓
TP change	↓
Rating change	↔

Bloomberg	AVALON IN
Equity Shares (m)	66
M.Cap.(INRb)/(USDb)	32.1 / 0.4
52-Week Range (INR)	732 / 366
1, 6, 12 Rel. Per (%)	-7/-11/1
12M Avg Val (INR M)	214

Financials & Valuations (INR b)

Y/E Mar	FY24	FY25E	FY26E
Sales	8.7	10.8	14.1
EBITDA	0.6	1.1	1.6
Adj. PAT	0.3	0.6	1.0
EBITDA Margin (%)	7.2	10.1	11.5
Cons. Adj. EPS (INR)	4.3	9.7	15.8
EPS Gr. (%)	(53.0)	127.7	62.8
BV/Sh. (INR)	83.3	93.0	108.8
Ratios			
Net D:E	(0.0)	(0.1)	(0.1)
RoE (%)	5.2	11.0	15.6
RoCE (%)	5.2	10.1	14.4
Valuations			
P/E (x)	114.6	50.3	30.9
EV/EBITDA (x)	51.0	29.0	19.4

Shareholding pattern (%)

As on	Mar-24	Dec-23	Mar-23
Promoter	50.9	51.0	70.7
DII	22.5	17.1	0.0
FII	2.4	5.7	0.0
Others	24.2	26.3	29.3

Note: FII includes depository receipts

CMP: INR489

TP: INR570 (+17%)

Buy

The US business drags overall performance; recovery visible

Earnings lower than our estimate

- Avalon Technologies (Avalon) reported a weak quarter, with revenue declining 20%/8% YoY in 4QFY24/FY24, led by a continued slowdown in the US business (reported a loss of ~INR300m in FY24) and muted growth of only ~3% YoY in the India business in FY24.
- The order book exhibited some resilience, with order inflows at ~INR3.1b across sectors (such as Industrial, Clean energy, Automotive, and Railways). The inflows led to an 11% YoY increase in the closing order book to INR13.7b as of Mar'24.
- Factoring in the weak 4QFY24 performance and lower growth guidance for FY25, we reduce our EPS estimates for FY25/FY26 by 6%/7%.

Reiterate BUY with a TP of INR570.

Weak margins due to adverse operating leverage

- Consolidated revenue declined 18% YoY, while it was up only 1% QoQ to INR2.2b (in line) in 4QFY24, due to challenges within the US business. EBITDA margin contracted 720bp/20bp YoY/QoQ to 7.9% (est. 8.3%), dragged down by operating deleverage. EBITDA declined 58% YoY (up 4% QoQ) to INR172m (est. INR181m). Adjusted PAT was down 69% YoY, while it grew 7% QoQ to INR71m (est. of INR77m).
- During FY24, Avalon's revenue/EBITDA/Adj. PAT declined 8%/45%/47% YoY to INR8.7b/INR626m/INR280m.
- The Indian market's revenue for FY24 grew only 3% YoY, but challenging conditions in the US market led to a decline in the US business revenue by 16% YoY. As a result, overall revenue declined 8% YoY during the period.
- Net debt as of Mar'24 stood at INR576m vs. net cash of INR1.2b as of Mar'23. Net working capital days increased to 161 from 144 in Mar'23, primarily led by higher inventory days (up 12 days).

Highlights from the management commentary

- **Guidance:** Management guided revenue growth of ~14-18% YoY in FY25, with major growth likely to be in 2HFY25. Profitability is likely to be notably higher than FY24 led by favorable operating leverage and the shift of a part of the production to India from the US. Avalon expects to double the revenue in the next three years.
- **Revival in the US business:** Management highlighted that weakness in the US business has bottomed out and it is expecting a strong recovery in 2HFY25.
- The company's large US home electrification customer in the clean energy segment has finally received the license from the US government. The company is expecting strong order flows as the customer will carry out the commercial launch of the project in late 2QFY25, and ramp up production in 2HFY25.

Valuation and view

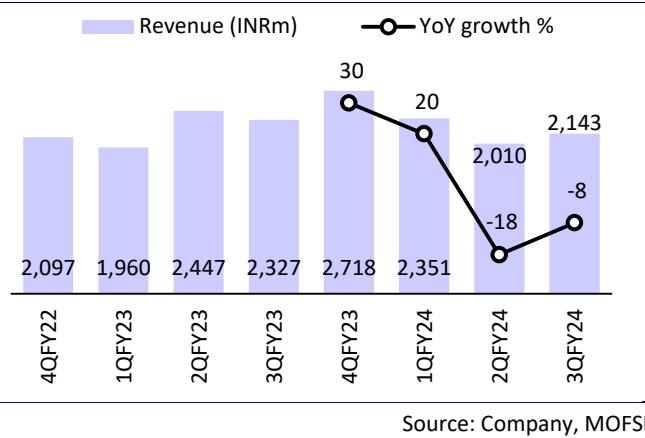
- With the recovery of the US operations in sight, we believe Avalon's revenue and profitability will improve in FY25. We also believe the long-term trajectory of the company continues to be strong, backed by: 1) addition of new customers in the US and Indian markets; and 2) order inflows from the high-growth/high-margin industries, such as Clean Energy and Aerospace.
- Factoring in the weak 4QFY24 performance and lower growth guidance for FY25, we reduce our EPS estimates for FY25/FY26 by 6%/7%. **Reiterate BUY with a TP of INR570 (premised on 36x FY26E EPS).**

Consolidated - Quarterly Earnings Model

Y/E March	FY23								FY24				FY23	FY24	FY24E	(INR m) Var	
	1Q		2Q		3Q		4Q		1Q		2Q		3Q		4Q		
	1Q	2Q	1Q	2Q	1Q	2Q	1Q	2Q									
Gross Sales	1,960	2,447	2,327	2,718	2,351	2,010	2,143	2,168	9,447	8,672	2,174	0					
YoY Change (%)	NA	NA	NA	NA	19.9	-17.9	-7.9	-20.2	350.4	-8.2	-20.0						
Total Expenditure	1,765	2,161	2,125	2,307	2,189	1,884	1,977	1,996	8,319	8,046	1,994						
EBITDA	195	286	202	411	162	126	165	172	1,128	626	181	-5					
Margins (%)	10.0	11.7	8.7	15.1	6.9	6.3	7.7	7.9	11.9	7.2	8.3						
Depreciation	46	49	50	52	53	55	60	61	197	229	65						
Interest	71	100	86	95	56	32	36	39	348	164	40						
Other Income	66	64	12	38	51	47	22	28	144	148	30						
PBT before EO expense	145	201	78	302	105	86	91	99	727	381	106						
Extra-Ord expense	0	0	0	0	0	0	0	0	0	0	0						
PBT	145	201	78	302	105	86	91	99	727	381	106						
Tax	52	53	21	75	34	13	25	29	202	101	29						
Rate (%)	35.8	26.6	26.7	24.7	32.4	15.2	27.5	29.0	27.8	26.5	27.0						
Minority Interest & Profit/Loss of Asso. Cos.	0	0	0	0	0	0	0	0	0	0	0						
Reported PAT	93	148	57	227	71	73	66	71	525	280	77						
Adj PAT	93	148	57	227	71	73	66	71	525	280	77	-9					
YoY Change (%)	NA	NA	NA	NA	-23.9	-50.7	14.7	-68.9	NA	-46.7	-66.0						
Margins (%)	4.7	6.0	2.5	8.4	3.0	3.6	3.1	3.3	5.6	3.2	3.6						

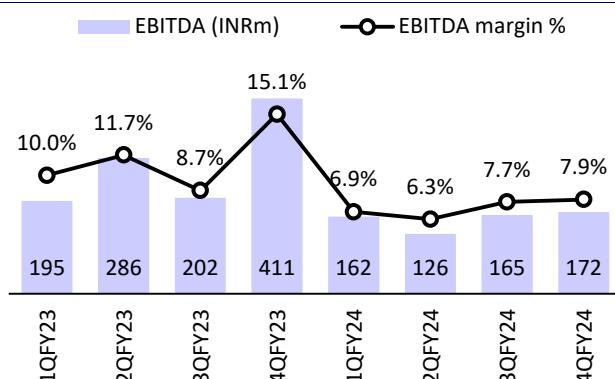
Key exhibits

Exhibit 1: Consolidated revenue trend



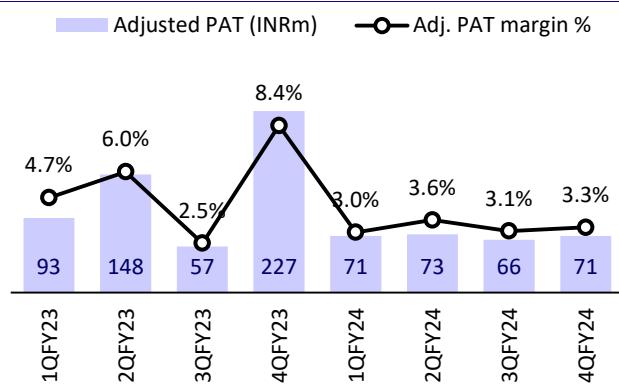
Source: Company, MOFSL

Exhibit 2: Consolidated EBITDA trend



Source: Company, MOFSL

Exhibit 3: Consolidated Adj. PAT trend



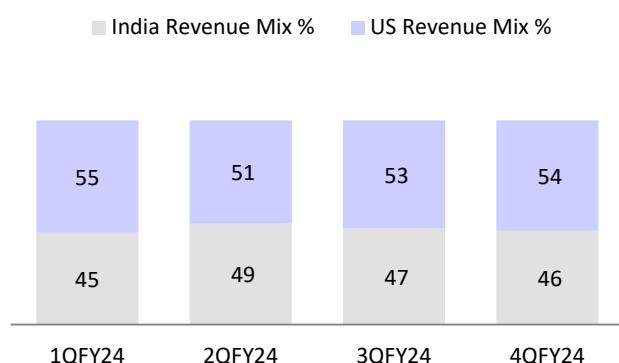
Source: Company, MOFSL

Exhibit 4: Order book trend



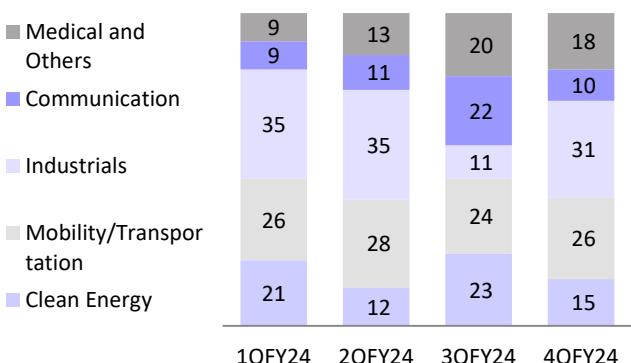
Source: Company, MOFSL

Exhibit 5: Region mix



Source: Company, MOFSL

Exhibit 6: End-user industry mix



Source: Company, MOFSL



Highlights from the management commentary

Indian business

- Indian operations witnessed ~3% YoY revenue growth in FY24.
- The Indian manufacturing segment (~77% of total manufacturing) continues to remain profitable, with EBITDA margin of ~12.7% and PAT margin of 8.5% in FY24.
- However, losses in the US operations are temporarily outweighing the healthy performance of Indian operations, and are affecting the consolidated results.
- Growth within the domestic business of Avalon is lesser as compared to that of the industry as traditionally, Avalon has an export-oriented business (with ~70% of exports). It has started focusing on domestic business over the last few years.
- Management believes that the growth story in India has just begun, and it will accelerate going ahead.
- The company expects a strong traction from railways (Signaling system, Kavach, and Vande Bharat), Industrial, and Energy industry in the domestic market. It is also witnessing a traction within the EV space.

US business

- The US operations continued to witness significant challenges and accordingly recorded a loss of INR300m in FY24.
- Avalon is actively addressing the challenges. Accordingly, it is focusing on shifting production from the US to India and rationalizing cost within the US business.
- The company began the production transfer of ~30-35% of total US manufacturing to India. This will be completed in next one to two quarters
- Of the total customers in US, ~55-60% of the customers agreed to move their production to India. While the customers are benefiting from the Inflation Reduction Act (IRA), they will want Avalon to keep their production in the US only to avail the benefit. This is more applicable to clean energy customers, which are the key beneficiaries of IRA
- The company witnessed 13% QoQ growth in revenue from the US, showing initial signs of recovery
- Going ahead, the US market is expected to witness a recovery in demand in 1HFY25m, which will be further accelerated in 2HFY25.

Guidance

- Management guided revenue growth of ~14-18% YoY in FY25, with major growth likely to be in 2HFY25. Profitability is likely to be notably higher than FY24 led by favorable operating leverage and the shift of a part of the production to India from the US.
- The management indicated that this is a conservative guidance looking at the closing order book of INR13.7b, which is executable in the next 12 to 14 months.
- It wants to maintain 50:50 mix of US and India revenue in the long term.
- Avalon expects to double the revenue in the next three years.
- The company will reduce the WC days by 10-15 over the next 9-12 months.
- It has reached the bottom and is expecting to recover from hereon.
- The company has been able to maintain its industry leading gross margins.

Outlook: Three growth engines for the company

Acquiring new customers in the US

- A major clean energy customer after 12 months of delay finally got the home electrification license approved and is expecting commercial launch in late 2QFY25, and scale up of production in 2HFY25. Scale up will be more significant in FY26E.
- There was temporary slowdown in the US in this segment (which got delayed by ~12 months) and with the approval of license now, it can see recovery
- Avalon have won several big order wins from large industrial companies in the Industrials and automotive segments. Some orders are for box builds, while others are for PCB and cable assemblies
- The company also received prototype orders now with commercial production expected to be done in 2HFY25. These are existing products with established companies. They can significantly scale up in FY26E and become among the top 10 customers of Avalon. For example, one of them is a market leader in the motion control system in mobility segment, while the other is a major backup power generation product for the residential and industrial markets. More update will be available in the coming quarters.
- With the Inflation Reduction Act (IRA) and China+1 opportunity will play a key role in company's growth in the US market.

Increasing wallet share with existing customers in US

- The inventory destocking has bottomed out and restocking has started now and will become more prominent in 2HFY25
- The company is gaining wallet share with some customers
- Avalon has signed long term agreement with key Aerospace company. The company already does sheet metals, cables etc. in the Aerospace segment.

Acquiring new customers in India

- In Railways, the company is associated with major Japanese customer who recently got approval from Indian railways for advance interlocking system. This customer is also actively working on Kavach system.
- In the Industrial & Energy segment, the company is currently working with some customers and also doing a lot of prototyping work for large industrial customers. This can result in a good revenue flow in future.
- Railways, Infrastructure, and 2W EV will be the key growth drivers for the company in India.
- The company has orders in EV for the next 12-15 months, which is expected to get launched in 2QFY25.
- **All three of the growth engines are gaining momentum and contributing significantly.**

Capacity expansion

- The new factory in Chennai SEZ to be operational in 1QFY25, which will cater to export demand. It is spread across three acres of land and is of 100,000sft area. Total capex for this is ~INR30crs which is mostly spent

- Another expansion is of brownfield capacity of which Phase 1 is expected to be operational in 1QFY25 and Phase 2's building construction will start in 2HFY25. This will cater to domestic demand.
- The management has guided ~INR350-450m capex p.a.

Orders

- The order book as on Mar'24 stood at ~INR13.7b. The orders are executable over the next 12-14 months. It does not include long duration orders of ~INR9.5b i.e. grew 50% YoY, which will be executed over 14 months to three years.
- It has registered major wins in the US and India across sectors such as Power, Industrial, Clean energy, Automotive and Rail

Others

- The most profitable business for the company is making products from India to the US customer
- Majority of the debt is in US and will bring down in 1HFY24. The company took INR300m of Debt in the month of Mar'24 to fund working capital
- The company has reduced US headcount substantially
- The company targets a 10x asset turnover

Valuation and View

- With the recovery of the US operations in sight, we believe Avalon's revenue and profitability will improve in FY25. We also believe the long-term trajectory of the company continues to be strong backed by: 1) an increase in the mix of box build through new orders and increasing the wallet share from existing customers; 2) addition of new customers in the US and Indian markets; 3) increasing wallet share with existing customers; and 4) order inflows from the high-growth/high-margin industries, such as Clean Energy and Aerospace.
- We estimate Avalon to deliver a CAGR of 27%/61%/93% in revenue/EBITDA/Adj. PAT over FY24-26 on the back of strong recovery and order inflows.
- Factoring in the weak 4QFY24 performance and lower growth guidance for FY25, we reduce our EPS estimates for FY25/FY26 by 6%/7%. **Reiterate BUY with a TP of INR570 (premised on 36x FY26E EPS).**

Exhibit 7: Changes to our estimates

Earnings change (INR m)	Old		New		Change	
	FY25E	FY26E	FY25E	FY26E	FY25E	FY26E
Revenue	11,108	14,440	10,840	14,091	-2%	-2%
EBITDA	1,144	1,704	1,095	1,621	-4%	-5%
Adj. PAT	677	1,117	637	1,037	-6%	-7%

Financials and valuations

Consolidated - Income Statement

Y/E March	FY20	FY21	FY22	FY23	FY24	FY25E	FY26E
Total Income from Operations	6,419	6,905	8,407	9,447	8,672	10,840	14,091
Change (%)	NA	7.6	21.8	12.4	-8.2	25.0	30.0
RM Cost	4,128	4,574	5,552	6,067	5,545	6,905	8,976
Employees Cost	1,162	1,192	1,314	1,605	1,815	2,027	2,508
Other Expenses	484	478	566	647	685	813	986
Total Expenditure	5,774	6,243	7,432	8,319	8,046	9,745	12,471
% of Sales	90.0	90.4	88.4	88.1	92.8	89.9	88.5
EBITDA	645	662	975	1,128	626	1,095	1,621
Margin (%)	10.0	9.6	11.6	11.9	7.2	10.1	11.5
Depreciation	155	158	172	197	229	271	319
EBIT	490	504	803	931	397	824	1,302
Int. and Finance Charges	450	270	248	348	164	118	75
Other Income	113	54	309	144	148	173	204
PBT bef. EO Exp.	153	288	864	727	381	879	1,431
EO Items	0	0	0	0	0	0	0
PBT after EO Exp.	153	288	864	727	381	879	1,431
Total Tax	30	58	183	202	101	242	393
Tax Rate (%)	19.4	19.9	21.1	27.8	26.5	27.5	27.5
Minority Interest	8	16	50	0	0	0	0
Reported PAT	115	215	632	525	280	637	1,037
Adjusted PAT	115	215	632	525	280	637	1,037
Change (%)	NA	86.1	193.9	-16.9	-46.7	127.7	62.8
Margin (%)	1.8	3.1	7.5	5.6	3.2	5.9	7.4

Consolidated - Balance Sheet

(INRm)

Y/E March	FY20	FY21	FY22	FY23	FY24	FY25E	FY26E
Equity Share Capital	15	16	16	116	131	131	131
Preference Capital	356	388	388	0	0	0	0
Total Reserves	450	584	856	5,254	5,342	5,979	7,017
Net Worth	822	988	1,260	5,370	5,473	6,111	7,148
Minority Interest	-431	-317	0	0	0	0	0
Total Loans	2,388	2,775	2,789	3,063	1,642	1,142	742
Deferred Tax Liabilities	-263	0	0	0	15	15	15
Capital Employed	2,515	3,445	4,049	8,433	7,129	7,267	7,904
Gross Block	1,126	1,335	1,512	1,861	2,285	2,642	3,033
Less: Accum. Deprn.	139	295	390	586	815	1,086	1,405
Net Fixed Assets	987	1,041	1,123	1,275	1,470	1,556	1,629
Goodwill on Consolidation	0	0	0	0	0	0	0
Capital WIP	27	0	20	153	196	239	248
Total Investments	24	0	0	0	755	755	755
Current Investments	0	0	0	0	755	755	755
Curr. Assets, Loans&Adv.	3,197	4,084	4,738	10,375	6,886	7,501	8,583
Inventory	1,553	1,458	2,330	3,179	3,163	3,500	4,058
Account Receivables	1,138	1,819	1,774	2,062	1,869	2,376	2,896
Cash and Bank Balance	266	335	101	4,222	1,065	758	643
Loans and Advances	241	472	532	912	789	867	986
Curr. Liability & Prov.	1,719	1,680	1,831	3,370	2,178	2,785	3,310
Account Payables	1,369	1,289	1,242	1,418	974	1,419	1,844
Other Current Liabilities	216	253	449	1,823	1,048	1,192	1,268
Provisions	134	138	141	130	156	173	197
Net Current Assets	1,478	2,404	2,906	7,005	4,708	4,717	5,273
Misc Expenditure	0	0	0	0	0	0	0
Appl. of Funds	2,516	3,445	4,049	8,433	7,129	7,267	7,904

Financials and valuations

Ratios

Y/E March	FY20	FY21	FY22	FY23	FY24	FY25E	FY26E
Basic (INR)							
EPS	2.0	3.7	10.9	9.1	4.3	9.7	15.8
Cash EPS	4.7	6.4	13.9	12.5	7.7	13.8	20.6
BV/Share	14.2	17.0	21.7	92.7	83.3	93.0	108.8
DPS	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Payout (%)	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Valuation (x)							
P/E	244.9	131.6	44.8	53.9	114.6	50.3	30.9
Cash P/E	104.5	76.0	35.2	39.2	63.0	35.3	23.7
P/BV	34.4	28.6	22.5	5.3	5.9	5.2	4.5
EV/Sales	4.7	4.4	3.7	2.9	3.7	2.9	2.2
EV/EBITDA	46.5	46.0	31.8	24.0	51.0	29.0	19.4
Dividend Yield (%)	0.0	0.0	0.0	0.0	0.0	0.0	0.0
FCF per share	8.4	-2.4	-0.4	-7.0	-2.8	2.1	2.4
Return Ratios (%)							
RoE	14.1	23.8	56.2	15.8	5.2	11.0	15.6
RoCE	15.1	12.8	22.5	12.4	5.2	10.1	14.4
RoIC	21.4	17.7	20.2	17.7	6.4	11.2	16.0
Working Capital Ratios							
Fixed Asset Turnover (x)	5.7	5.6	5.9	5.6	4.2	4.4	5.0
Asset Turnover (x)	1.5	1.3	1.4	0.8	0.9	1.1	1.3
Inventory (Days)	98	120	125	166	209	185	165
Debtor (Days)	65	78	78	74	83	80	75
Creditor (Days)	87	106	83	80	79	75	75
Leverage Ratio (x)							
Current Ratio	1.9	2.4	2.6	3.1	3.2	2.7	2.6
Interest Cover Ratio	1.1	1.9	3.2	2.7	2.4	7.0	17.3
Net Debt/Equity	2.6	2.5	2.1	-0.2	0.0	-0.1	-0.1

Consolidated - Cash Flow Statement

(INRm)

Y/E March	FY20	FY21	FY22	FY23	FY24	FY25E	FY26E
OP/(Loss) before Tax							
OP/(Loss) before Tax	153	288	856	727	381	879	1,431
Depreciation	155	158	180	197	229	271	319
Interest & Finance Charges	434	222	209	244	113	-55	-129
Direct Taxes Paid	-47	-35	-125	-189	-164	-242	-393
(Inc)/Dec in WC	-121	-561	-805	-1,125	-414	-315	-672
CF from Operations	574	72	315	-147	145	538	555
Others	83	-17	-158	13	28	0	0
CF from Operating incl EO	657	55	157	-133	173	538	555
(Inc)/Dec in FA	-170	-192	-177	-273	-355	-400	-400
Free Cash Flow	487	-137	-21	-406	-182	138	155
(Pur)/Sale of Investments	-24	29	0	0	-1,121	0	0
Others	2	-104	-6	2	15	173	204
CF from Investments	-192	-267	-184	-271	-1,461	-227	-196
Issue of Shares	0	73	0	798	8	0	0
Inc/(Dec) in Debt	-296	461	158	128	-1,580	-500	-400
Interest Paid	-426	-217	-189	-283	-88	-118	-75
Dividend Paid	-4	-37	-38	-37	-41	0	0
Others	302	22	-138	3,915	-807	0	0
CF from Fin. Activity	-424	301	-207	4,522	-2,508	-618	-475
Inc/Dec of Cash	42	89	-234	4,118	-3,796	-307	-116
Opening Balance	204	246	335	101	4,219	1,065	758
Other cash & cash equivalent	20	0	0	3	643	0	0
Closing Balance	266	335	101	4,222	1,065	758	643

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Explanation of Investment Rating	
Investment Rating	Expected return (over 12-month)
BUY	>=15%
SELL	< - 10%
NEUTRAL	< - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

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