



Optimistic on US Recovery and Long-Term Growth Potential....

Avalon's FY24 performance was weak due to macro issues in the US. Management has guided for conservative revenue growth of 14-18% for FY25, but long-term levers are in place for topline doubling in the next 3 years.

Greenshoots have appeared in the US with 13% QoQ revenue growth, along with the restocking cycle, a strong order book, and major new order wins.

Management expects recovery in H1 FY25, with momentum picking up in H2 FY25 in the US business.

- INR revenue came in at INR 2,168 Mn, -20.2% YoY / +1.2% QoQ.
- EBITDA stood at INR 172 Mn, -58% YoY / +4% QoQ.
- EBITDA margins: 7.9%, vs 15.1% / 7.7% in Q4FY23 / Q3FY24 respectively
- PAT came in at INR 71 Mn, -68.9% YoY / +7.4% QoQ.
- PAT margins: 3.2%, vs 8.2% / 3.0% in Q4FY23 / Q3FY24 respectively
- EPS at INR 1.1 in Q4FY24 vs 3.9/ 1.0 in Q4FY23 / Q3FY24 respectively

Geography-wise

- India contributed 46% of revenue in FY24 vs 41% of revenue in FY23.
- US contributed to 54% of revenue in FY24 vs 59% of revenue in FY23.
- India manufacturing contributed to 77% in FY24 vs 72% in FY23
- US manufacturing contributed to 23% in FY24 vs 28% in FY23

Y/E Mar (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Net sales	8,407	9,447	8,672	10,256	14,358
EBIDTA	975	1,128	625	1,029	1,884
Margins	11.6	11.9	7.2	10.0	13.1
PAT (adj)	632	525	280	588	1,227
Growth (%)	192.3	-22.2	-46.7	109.9	108.8
EPS	79.16	9.06	4.26	8.94	18.68
P/E (x)	6	54	115	55	26
P/B (x)	4	5	6	5	4
EV/EBITDA (x)	3	27	51	31	17
RoE (%)	55	10	5	10	17
ROCE (%)	24	13	8	13	22
RoIC (%)	19	18	8	12	19
Gross Fixed Asset Turn	8	8	6	6	7

Source: Dalal and Broacha

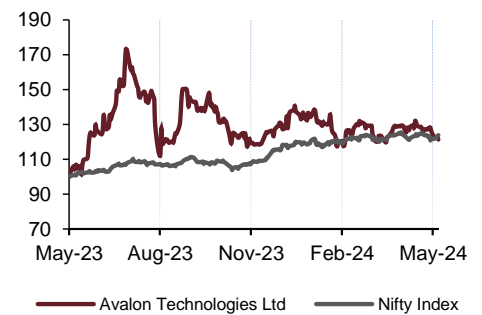
Rating	TP (Rs)	Up/Dn (%)
BUY	654	34

Market data

Current price	Rs	489
Market Cap (Rs.Bn)	(Rs Bn)	32
Market Cap (US\$ Mn)	(US\$ Mn)	385
Face Value	Rs	2
52 Weeks High/Low	Rs	732.1 / 366.05
Average Daily Volume	('000)	111
BSE Code		543896
Bloomberg		AVALON .IN

Source: Bloomberg

One Year Performance



Source: Bloomberg

% Shareholding	Mar-24	Dec-23
Promoters	50.91	50.97
Public	49.09	49.03
Total	100	100

Source: BSE

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Concall Highlights

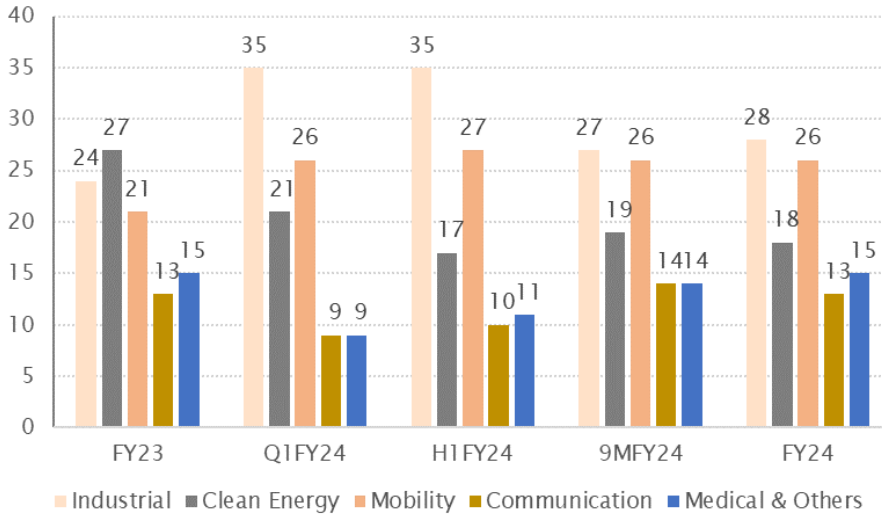
- **The order book stands at INR 1366 cr, +11% YoY/+7.1% QoQ (executable over the next 12 to 14 months). An additional INR 949 cr, 58% YoY/ +12.6% QoQ contracts and LOIs are also in place, with execution expected over the next 2 to 3 years.**
- **Gross margins stood at 37.5%, (-111 bps YoY/+71 bps QoQ).** Management is focused on optimizing production costs by shifting the majority of manufacturing from the US to India, while maintaining clean energy manufacturing in the US to take advantage of the Inflation Reduction Act. This strategic move is expected to help Avalon sustain its industry-leading gross margins. Additionally, the majority of Avalon's costs below material costs are fixed, allowing operating leverage to enhance profitability as revenue ramps up in H2 FY25. Avalon's dedicated focus on improving working capital should free up some cash, further supporting their growth and profitability.
- Avalon is in the final stages of completing their new factory in Chennai, which is set to go live in Q2 FY25 to cater to export demand. To address additional domestic demand, Avalon's phase 1 of their brownfield plant expansion in Chennai is expected to go live in Q1 FY25, with phase 2 following in H2 FY25. Avalon has received approvals to transfer production from their US plant to the India plant for nearly 50% of existing US manufacturing customers during FY25. Production transfer has already begun for 30-35% of these customers. **The management aims for an 85%-15% manufacturing mix, with 85% production in India and the remaining 15%, primarily final assembly, to be conducted in the US (currently at 77%-23% in FY24).**
- **The management anticipates an improvement in the working capital cycle by 10 to 15 days in the next 9 to 12 months compared to FY24. In the long run, the management aims to achieve pre-COVID working capital days.**
- Avalon has surplus cash of INR 118 crores in short-term investments, of which 50 crores are earmarked for debt repayments in US subsidiaries (Sienna). **Avalon is maintaining existing working capital lines amounting to INR 185 crore, providing flexibility to aggressively bid for and execute substantial orders in the pipeline.**
- FY24 results were influenced by challenging economic conditions in the US mitigated by robust domestic demand and acquisitions of marquee global customers. Indian manufacturing operations, contributing 77% of their business, achieved robust operating margins of 12.7% and PAT margins of 8.5 % in FY24. However, macro issues in the US led to losses of 30 cr in their US operations IN FY24.
- Avalon is realigning its business strategy to adapt to the current macro situation, with a focus on increasing its presence in the Indian market. The company aims to achieve a 50-50 revenue ratio between the US and Indian markets while maintaining a strong presence in the highly profitable US market.
- Avalon has onboarded Mr. Venky Venkatesh as the Group Chief Sales Officer, strengthening their focus on growth for the coming years. This strategic move underscores Avalon's commitment to expanding their market presence and driving revenue growth through enhanced sales leadership. Mr. Venkatesh brings over 30 years of experience in leading high-performance sales teams and closing large deals in their target verticals, which will be instrumental in achieving Avalon's ambitious growth objectives across various sectors.
- Major investments in facilities and larger factories have been completed, with management anticipating a capital expenditure of 35-45 crore rupees over the next three years to sustain growth.

- The three growth engines Avalon is focusing on, which are gaining momentum in FY25 after a challenging FY24:
 - a. **New customers in the US:** A major clean energy customer has received long-pending product compliance certification for their home electrification system. Commercial launch is expected in late Q2 FY25, with production ramp-up in H2 FY25 and significant scale-up in FY26. Avalon has secured major wins with industry-leading companies in the industrial and automotive segments, starting with box build, PCB, and cable assembly. Prototypes have been ordered, with commercial production expected in H2 FY25. These established products have significant scale-up potential in FY26, including a market leader in motion control systems for mobility and a major backup power generation product for residential and industrial markets.
 - b. **Existing Customers in the US:** Avalon serves industry-leading, well-established companies across various verticals. In FY24, this growth area faced challenges due to inventory destocking and macro uncertainties. Avalon indicated that the inventory destocking cycle has bottomed out, and the restocking cycle has begun for their US customers. Avalon's efforts to gain wallet share with certain US customers will be beneficial as the restocking cycle gains momentum, becoming more prominent in H2 FY25. For aerospace customers, Avalon has entered the cable harness and lighting products market and signed a 15-year Master Term Agreement with a global aerospace major. Recent order wins in the aerospace segment are expected to commence execution in Q4 FY25 and ramp up significantly in FY26.
 - c. **India Customers:** Over the past 18 months, Avalon has transitioned from being predominantly export-focused to actively targeting the Indian market. Significant inroads have been made in the industrial, rail, and EV verticals. Major wins in the last quarter include securing a major Japanese customer in the railway sector, recently approved by Indian Railways for an advanced signaling and interlocking system, as well as the Kavach system. Avalon has also achieved significant successes in the industrial and energy segments, with prototype orders expected to ramp up production in FY25. These partnerships have the potential to contribute significantly to revenue in late FY25 and FY26. Additionally, Avalon has made inroads into the defense and communication sectors, with meaningful orders expected from the second half of FY25 and execution anticipated in FY26.

Vertical-wise updates:

- **Clean Energy (18% of topline in FY24).** The clean energy sector is seeing green shoots as the restocking cycle begins after a temporary slowdown due to destocking. A home electrification project, which had been delayed, is now set to gain momentum starting in Q2 FY25, as certification and compliance requirements are now in place for the client. Full production is expected to commence in H2 FY25. Over the next three years, this vertical is anticipated to grow much faster than the industry average.
- **Mobility/ Transportation (26% of topline in FY24).** In the aerospace sector, Avalon has signed a 15-year multi-year agreement. Previously focused on lighting, Avalon has expanded its aerospace offerings to include cable assembly and is also entering the wiper blade market. They have already shipped a couple of prototypes and are set to start production on 153 types of wiper blades over the next 12 to 18 months. This expansion into new product lines presents a substantial growth opportunity for Avalon over the next 10-15 years.

Rev Mix Industry wise %

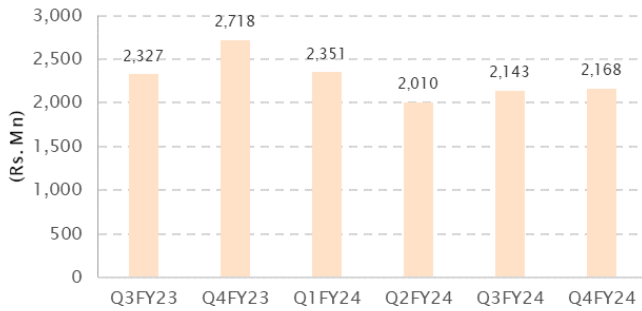


Source: Company, D&B Research

FY25e Outlook

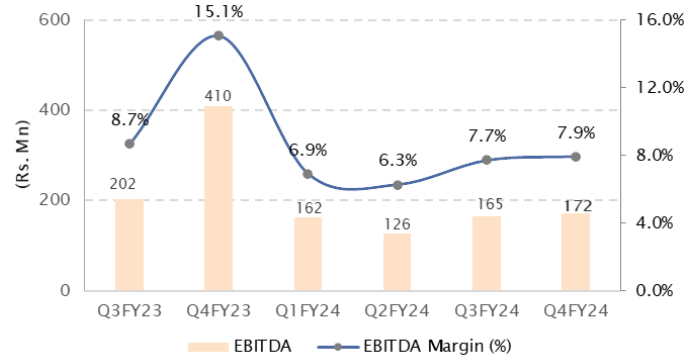
- Avalon remains cautiously optimistic for FY25 guiding for 14-18% Revenue growth, With the US market recovering in H1FY25 and gaining momentum in H2FY25.
- Avalon are confident of doubling their revenue over the next 3 years.
- Working Capital to improve by 10-15 days over the next 9 to 12 months.

Net Sales Trajectory



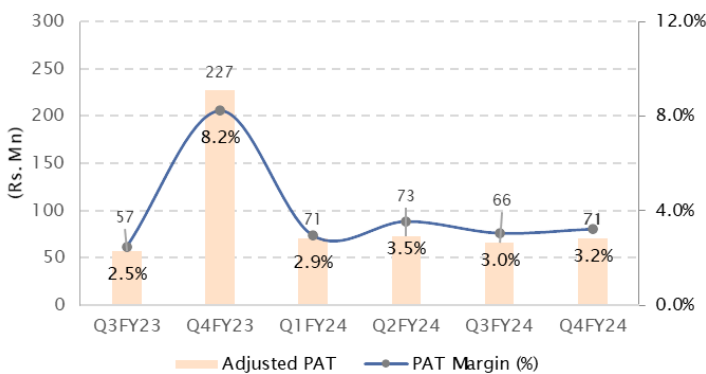
Source: Company, D&B Research

EBITDA & EBITDA Margin Trajectory



Source: Company, D&B Research

Adj. PAT (Exc. Exceptional) Trajectory



Source: Company, D&B Research

Quarterly Deviation Sheet

(Rs.Mn)	Q4FY24	Q4FY23	YoY Growth (%)	Q3FY24	QoQ Growth (%)	FY24	FY23	Growth %
Revenue from Operations	2,168	2,718	-20.2%	2,143	1.2%	8,672	9,447	-8.2%
Other Income	28	39	-28.1%	22	29.4%	149	144	3.7%
COGS	1,354	1,667	-18.8%	1,353	0.1%	5,523	5,947	-7.1%
Employee Benefits Expense	451	466	-3.0%	459	-1.6%	1,850	1,714	8.0%
Other Expenses	191	176	8.7%	166	15.3%	673	659	2.2%
Total Expenses	1,996	2,308	-13.5%	1,977	0.9%	8,047	8,319	-3.3%
EBITDA (Excl Other Income)	172	410	-58.0%	165	4.0%	625	1,128	-44.6%
Depreciation	61	52	17.8%	60	1.9%	229	197	16.5%
EBIT / PBIT	139	397	-65.0%	127	9.4%	545	1,075	-49.3%
Finance Costs	39	95	-58.5%	36	8.7%	164	348	-52.9%
EBT/ PBT	99	302	-67.0%	91	9.7%	381	727	-47.6%
Tax Expense	29	75	-61.4%	25	15.6%	101	202	-50.1%
Net Profit after Tax	71	227	-68.9%	66	7.4%	280	525	-46.7%
Adj Earning Per Share	1.1	3.9	-72.6%	1.0	7.3%	4.3	9.1	-53.1%
No of Shares Diluted (mn)	65.7	58.0		65.6		65.7	57.8	
Margins Analysis (%)			bps		bps			bps
Gross Margins	37.5%	38.7%	-111	36.8%	71	36.3%	37.1%	-75
EBITDA Margins (Excl Other Income)	7.9%	15.1%	-714	7.7%	22	7.2%	11.9%	-473
PAT Margins	3.2%	8.2%	-502	3.0%	18	3.2%	5.5%	-230
Effective Tax Rate %	29.0%	24.7%	423	27.5%	148	26.4%	27.8%	-133
Cost Analysis (%)			bps		bps			bps
COGS as a % to sales	62.5%	61.3%	111	63.2%	-71	63.7%	62.9%	75
EE Cost as a % to sales	20.8%	17.1%	369	21.4%	-59	21.3%	18.1%	319
Other exps as a % to sales	8.8%	6.5%	234	7.7%	107	7.8%	7.0%	79

Source: Company, D&B Research

Valuation & Outlook

Avalon Technologies is currently trading at 54.7x / 26.2x FY25e / FY26e EPS.

FY24 was impacted by macro challenges and a destocking cycle in the US, but the numbers aligned with management's guidance. The management is now seeing positive signs in the US business with the beginning of the restocking cycle and the normalization of the supply chain. As revenue grows in the coming years, optimizing and integrating the current team and infrastructure should significantly enhance operating leverage, leading to profit growth outpacing revenue growth.

Avalon maintains industry-leading gross margins (36.3% in FY24) by avoiding low-margin businesses. Management expects to sustain these margins depending on the product mix and ramp-ups. The majority of Avalon's costs below material costs are fixed, allowing operating leverage to boost profitability achieving double digit EBITDA margins in H2 FY25. Avalon's focus on improving working capital should free up cash, further supporting growth and profitability.

To enhance margins, Avalon is implementing various initiatives, including optimizing production allocation, strategically relocating some production activities from the US to India, rationalizing costs in US operations, and leveraging operating efficiencies. The company aims for a balanced split between Indian and US markets, with 85% of manufacturing in India and 15% in the US from 77% and 23% currently. With a strong order book (INR 13,660 Mn) and LOI (INR 9,490 Mn), Avalon anticipates favorable performance in the medium to long term, supported by solid long-term fundamentals.

We believe the management's guidance of 14-18% revenue growth is conservative. Looking at the long-term levers in place, management is confident in their ability to double their topline in the next three years. **We maintain our BUY rating on the stock, assigning a target multiple of 35x FY26e to arrive at a target price of INR 654, indicating a 34% upside.**

Financials

P&L (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E	Cashflow (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Net Sales	8,407	9,447	8,672	10,256	14,358	PBT	856	727	381	811	1,693
Operating Expenses	-5,541	-5,947	-5,523	-6,461	-9,046	Depreciation	180	197	229	248	250
Employee Cost	-1,314	-1,714	-1,850	-2,035	-2,442	Net Chg in WC	-760	-936	-234	-359	-1,147
Other Expenses	-577	-659	-673	-731	-987	Taxes	-125	-194	-164	-223	-466
Operating Profit	975	1,128	625	1,029	1,884	Others	6	74	-385	110	80
Depreciation	-180	-197	-229	-248	-250	CFO	157	-132	-173	586	410
PBIT	795	931	396	781	1,633	Capex	-177	-274	-355	-450	-354
Other income	109	144	149	149	149	Net Investments made	-6	2	15	-	-
Interest	-248	-348	-164	-119	-89	Others	-	18	-1,121	-	-
PBT	656	727	381	811	1,693	CFI	-184	-254	-1,461	-450	-354
(post exceptional)	856	727	381	811	1,693	Change in Share capital	-68	4,815	4,642	-	-
Provision for tax	-182	-202	-101	-223	-466	Change in Debts	86	48	-1,961	-450	-300
Reported PAT	675	525	280	588	1,227	Div. & Div Tax	-38	-55	-41	-	-
MI	-43	-	-	-	-	Others	-189	-262	-5,148	-72	-24
Owners PAT	632	525	280	588	1,227	CFF	-209	4,546	-2,508	-522	-324
(excl Exceptionals)	485	525	280	588	1,227	Total Cash Generated	-236	4,159	-4,141	-386	-267
						Cash Opening Balance	335	101	4,222	1,065	680

Balance Sheet (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E	Ratios	FY22	FY23	FY24E	FY25E	FY26E
Equity capital	16	116	131	131	131	OPM	11.6	11.9	7.2	10.0	13.1
Reserves	872	5,254	5,342	5,930	7,157	NPM	5.7	5.5	3.2	5.6	8.5
Net worth	888	5,370	5,473	6,061	7,289	Tax rate	-21.2	-27.8	-26.4	-27.5	-27.5
Non Current Liabilities	1,016	1,074	1,030	887	794	Growth Ratios (%)					
Current Liabilities	3,990	5,443	2,804	2,761	3,180	Net Sales	21.8	12.4	-8.2	18.3	40.0
TOTAL LIABILITIES	5,894	11,887	9,308	9,709	11,263	Operating Profit	47.5	15.6	-44.6	64.6	83.1
Non Current Assets	1,391	1,767	2,220	2,318	2,293	PBIT	57.8	17.1	-57.5	97.2	109.1
Fixed Assets	918	1,086	1,257	1,263	1,170	PAT	192.3	-22.2	-46.7	109.9	108.8
Right of Use Assets	244	342	409	478	520	Per Share (Rs.)					
Financial Assets	53	53	219	230	242	Net Earnings (EPS)	79.16	9.06	4.26	8.94	18.68
Deferred Tax Asset	159	132	180	185	190	Cash Earnings (CPS)	101.70	12.45	7.75	12.71	22.49
Other Non Current Assets	18	153	155	162	171	Dividend	-	-	-	-	-
Current Assets	4,503	10,120	7,088	7,391	8,970	Book Value	111.19	92.66	83.29	92.23	110.91
Current investments	-	-	755	830	913	Free Cash Flow	-7.90	-5.17	-4.05	0.07	-1.01
Inventories	2,330	3,179	3,163	3,435	4,313	Valuation Ratios					
Trade Receivables	1,774	2,062	1,869	2,210	3,094	P/E(x)	6	54	114.7	54.7	26.2
Cash and Bank Balances	101	4,222	1,065	680	413	P/B(x)	4	5	6	5	4
Other Financial Assets	13	37	7	7	8	EV/EBIDTA(x)	3	27	51	31	17
Other Current Assets	284	619	229	229	229	Div. Yield(%)	-	-	-	-	-
TOTAL ASSETS	5,894	11,887	9,308	9,709	11,263	FCF Yield(%)	-1.62	-1.06	-0.83	0.01	-0.21
						Return Ratios (%)					
						ROE	55%	10%	5%	10%	17%
						ROCE	24%	13%	8%	13%	22%
						RoIC	19%	18%	8%	12%	19%

	FY22	FY23	FY24E	FY25E	FY26E		FY22	FY23	FY24E	FY25E	FY26E
ROA	8.2	4.4	3.0	6.1	10.9	Equity	16	116	131	131	131
Current Assets	4,401	5,898	5,267	5,881	7,643	Face Value	2	2	2	2	2
Net Debt	2,839	-1,160	-179	-319	-435	CMP	489	489	489	489	489
Gross Fixed Asset Turn	8	8	6	6	7	Mcap	-	31,928	32,135	32,135	32,135
Net Fixed Asset Turn	9	10	8	10	15	Debt	2,941	3,063	1,642	1,192	892
						Cash	120	4,376	1,975	1,673	1,497
						EV	2,821	30,615	31,801	31,653	31,529

Source: Company, Dalal & Broacha Research

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