

Rico Auto Industries Ltd

BSE: 520008 | Sector: AUTO COMPONENTS

27th January, 2016

vScore : 62 | Gain%: **112.4%**

Buy Date: 27-Jan-2016 | Buy Price : Rs. 37.50

Exit Date: 13-July-2017 | Exit Price : Rs. 79.65

BUSINESS BACKGROUND

Incorporated in March 1983, Rico Auto Industries Ltd (RAIL) manufactures and sells high-pressure aluminum die cast components and spheroidal graphite (SG) iron castings for the automotive sector. RAIL currently operates from 9 locations at Dharuhera, Haridwar, Sanand and Gurgaon, manufacturing automotive components for both the 2-wheelers and 4-wheeler segments like wheel hubs, panels, clutch assemblies, cylinder covers, cylinder head, cylinder block, center housing, exhaust manifolds, fly wheels and brake drum among others.

Further RAIL has a diverse product range and supplies a broad range of high-precision fully machined aluminum and ferrous components and assemblies to OEMs across the globe.

RAIL's key positives are via its integrated services which include design, development, tooling, casting, machining, assembly and research and development across aluminium and ferrous products.

INVESTMENT HIGHLIGHTS

Strong Q2 & FY15 Performance –

RAIL reported a sales of Rs 243 crs in Q2 FY16 from Rs 388 crs in Q2 last year largely due to the sale of FCC Rico. This was reflected in a EBIDTA of Rs 26 crs from Rs 37 crs in Q2 last year and a PAT for Q2FY16 standing at Rs 9.42 crs from Rs 1.70 crs in Q2 last year. For H1 of FY16 Topline has totalled Rs 495 crs, a EBIDTA of Rs 48 crs and a PAT of Rs 13.70 crs.

vScore: vScore (Value Score) is our proprietary company rating system

For FY15 the company has recorded a topline of Rs 1346 crs a EBIDTA of Rs 97 crs while PAT is placed at Rs 153 crs. However this includes profit on sale of FCC Rico of Rs 194 crs. RAIL has paid a dividend of 200% for FY15.

KEY DATA

FACE VALUE	Rs.1
DIVD YIELD %	4.34
52 WK HI/LOW	65/35
NSE CODE	RICOAUTO
MARKET CAP	Rs. 625 Cr

SHAREHOLDING PATTERN

PROMOTERS	-	50.00%
BANKS, MFs & DIs	-	4.00%
FIs	-	1.00%
Others	-	45.00%

KEY FUNDAMENTALS

Year Ending	FY17E	FY18E
Rev Gr%	22	25
EBIDTA Gr%	23	26
PBT Gr%	40	42
PAT Gr%	55	44
EPS Gr%	55	44
Roe %	9	12
RoCE %	11	13
EPS (Rs)	3.3	4.8
P/E (x)	14	10

RAIL enjoys a strong clientele base

RAIL is a well established auto component Tier 1 supplier to both the 2 wheeler, 4 wheeler and industrial segments. Notable large OEM customers include Bajaj Auto Hero Motor Yamaha Honda Suzuki, TVS, Tata Motors, GM, Renault, Nissan, Ford, Jaguar, Volvo, Caterpillar, Perkins, Tata Cummins, Magna, Honeywell, Continental and Jatco. We expect that a strong relationship with OEMs offers a big opportunity for RAIL to expand its product offerings and increase content per vehicle. RAIL has won a new Differential Housing Business order from GKN and BMW. Also ramp up in exports to Jatco and Renault is expected to add to FY16 sales. All customers have continued to show their keen intent to engage with RAIL as their preferred supplier and work as a long term strategic partner. This intent is based on RAIL's demonstrated ability to supply superior quality critical and complex parts at most competitive prices and manage an extended supply chain to deliver just in time

RAIL enjoys a diverse product basket catering to large Auto Customers

RAIL offers oil pump assemblies, fuel system parts, lube oil filter heads, exhaust manifolds, turbine housings, center housings, back plates, crank cases and covers, cylinder head covers, oil pans, intake manifold covers, front covers, valve covers, side covers, balance shafts assemblies, gear housings, main bearing caps, flywheels, timing cases, and oil filter adapters. It also provides engine brackets, cylinder blocks, cylinder heads, clutch assemblies, automatic transmission bracket assemblies, differential case housings, gear shift forks, wheel hubs assemblies, brake panel assemblies, brake discs, drums, and steering knuckles, as well as water and air connections and pressure plates

Further RAIL supplies a broad range of high-precision fully machined aluminum and ferrous components and assemblies to Original Equipment Manufacturers across the globe. Its integrated services include design, development, tooling, casting, machining, assembly and research and development across aluminium and ferrous products

RAIL to focus on Exports going ahead

The RAIL management has been focusing more on export revenues and has been successful in getting some very good export orders from existing and new clients. Currently domestic revenue is almost about 78-80% and export is 20% (including export through OEM in India). The exports market in US and Europe is stabilizing and expected to grow by mid single digits in FY16 and FY17. RAIL is working towards leveraging this uptrend and will keep launching critical programs to strengthen its position.

Recently RAIL has won a new Differential Housing Business order from GKN and BMW. Also ramp up in exports to Jatco and Renault is expected to add to FY16 sales. All customers have continued to show their keen intent to engage with RAIL as their preferred supplier and work as a long term strategic partner.

Volume jump possible over FY16 and FY17 without much capex

All the current plants of RAIL are currently working at 55-60% capacity and can easily be ramped up to 80-85% capacity once working capital becomes easily available and orders pour in. RAIL is working extensively towards expanding operations by way of commissioning new plants and adding production capacity and latest technology to the existing facilities. In this regard, the production facilities at Bawal plant were upgraded to provide a better output to handle growing global demands. Similarly, Chennai plant is soon to start operations which will further add production capacity, contributing to a wider consumer and product portfolio. RAIL is also in the process of attaining

new corporate contracts to better utilize the capacity of Sanand plant which are not utilizing this days since Tata Nano demand is sluggish

Steady improvement in financial performance - topline growth and margin expansion

We estimate RAIL's earnings to witness a CAGR of 30-35% over FY16-18E. This will be driven by a steady revenue growth (20-22% CAGR over FY16-18E) and a steady EBITDA margin expansion over the same period. Over the next 24 months RAIL is likely to improve its operational performance with operating margins getting impacted positively on the back of lower commodity prices and higher top line growth from both new and existing products and from acquisition of new customers.

Going ahead we expect EBITDA margins to improve to around 10% by FY17. Also it will be generating a higher a return on equity of 12% and ROCE of 13% in FY18. Also, considering the fact that RAIL's business requires large working capital, it has a reasonably low net D :E of 0.39:1 as on Sept 2015 on a net worth of Rs 465 crs as on Sept 2015 which we believe looks low which is a positive for RAIL. Further the RAIL management has reduced its debt level quite significantly to Rs 146 crs in FY15 from Rs 409 crs in FY13 which will also further improve the ROE going ahead.

Business Outlook & Stock Valuation

On a rough cut basis, in FY16, Topline will see a steady rise wherein Topline is expected to touch Rs 995 crs in FY16E.

On the bottomline level we expect the company to record a PAT of Rs 29 crs in FY16E. Thus on a conservative basis, RAIL should record a EPS of Rs 2.14 for FY16E. For FY17E and FY18E our expectation is that earnings traction for RAIL would continue to be strong wherein we expect a EPS of Rs 3.33 and Rs 4.80 respectively.

Also another attractive point for RAIL is that EPS growth over the next three years between FY16 to FY18 is expected to average 35% plus YoY but valuation multiples look quite low between 14x on FY17 and 10x on FY18E. To add to this at the current market cap of RAIL at Rs 625 crs, the RAIL stock trades a market cap to sales multiple of just 0.62x on FY16E whereas the potential revenue over the next 2 years is over Rs 1500 crs. Also with the balance sheet size of Rs 950 crs by FY16 end, the current valuation looks undervalued.

Looking at RAIL's steady financial track record, strong product domain and dominant market share and strong promoters we expect the stock to get re rated in future.

Hence we believe that the RAIL stock should be purchased at the current price for a price target of around Rs 82 over the next two years.

Another positive fact for RAIL is that the RAIL promoters hold a sizeable 50% and earlier pledged shares have now been reduced to zero from 52% last year

FINANCIALS

For the Year Ended March RsCr	FY15A	FY16E	FY17E	FY18E
Net Sales	1346.5	995.0	1213.9	1517.37
EBIDTA	96.99	99.0	121.39	153.25
EBIDTA %	7.20	9.95	10.00	10.10
Interest	52.76	25.0	24.0	22.0
Depreciation	84.6	48.0	55.0	65.0
Non Operational Other Income	226.92	15.0	15.0	15.0
Profit Before Tax	186.55	41.0	57.39	81.25
Profit After Tax	153.43	29.0	45.0	65.0
Actual EPS (Rs)	-	2.14	3.33	4.80
Equity Capital	13.53	13.53	13.53	13.53
Reserves	437.47	466.47	511.47	576.47
Borrowings	146.0	155.0	130.0	105.0
GrossBlock	432.0	467.0	517.0	567.0
Investments	48.5	48.5	48.5	48.5

Key Risks and Concerns:

- Any sharp down turn in the Automobile Industry can impact RAIL's financials adversely.
- Also any negative development in the new product launches of OEMs could also impact RAIL's financials negatively. Any downturn in the pigments or Agro-chemicals demand can impact company's financials adversely.
- Competitors can create pressure on the margins which can ultimately affect the financials of the company.
- Exports demand slowdown can create growth problems for the company.
- Any adverse policies introduced by government in terms of taxes and other majors can affect the overall sector and hence a company.

vScore (Value Score) is our proprietary company rating system for NSE and BSE stocks with value investing philosophy at its core. Technical analysis, macroeconomic indicators and recent developments provide it 360 degree view.

vScore algorithm crunches hundreds of numbers along with the current market price from quarterly and yearly financial results like balance sheet, profit and loss statement, cash flow statement etc. for last 5 years.

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**Duration of investment can be varied according to market conditions and growth potential of the stock under review.*

Source: Niveza Research Desk