

Ramkrishna Forgings

NEUTRAL

Diversifying beyond CVs

In 2QFY20, RK Forgings' EBITDA margin at 18.1% (-90bps YoY) continued to be impacted by a weak demand environment. The co is diversifying beyond CVs through expansion into new segments/inorganic initiatives. We recently upgraded the stock to NEUTRAL post the sharp stock correction and the risk-reward is more favourable. We are lowering estimates by ~2% and set a revised TP of Rs 275 (@12x Sep-21 EPS).

HIGHLIGHTS OF THE QUARTER

- **Financials:** Total tonnage at 18,517T declined 47/35% YoY/QoQ to 18k tons. Domestic/export volumes declined 58/6% YoY to 11,498/7,019T. Blended realisations at Rs 140k grew 7% QoQ (Domestic flat, exports +9%). Revenue/EBITDA declined 44/52% YoY. EBITDA margin at 18.1% contracted 310/90bps YoY/QoQ due to the drop in utilisation levels. PAT declined 98% YoY.
- **Diversification initiatives:** RK Forgings has bid for the assets of ACIL (under NCLT), which is formerly Amtek Autos' crankshaft subsidiary. The co is into machined crankshafts and supplies components to the tractor/2W segments, primarily. ACIL had revenues of

Rs 1.4bn in FY18 and has achieved a peak turnover of Rs 2.75bn earlier. Management highlights that the CoC approval has come and the deal should be completed in 4QFY20. While we await details of the transaction, the strategic decision to de-risk the co by expanding beyond CVs will reduce volatility in the business.

- **Mixed demand outlook:** Class 8 truck sales are expected to decline 10-15% in CY20. However, supplies to new customers in Europe (Scania and MAN) will commence next year. Further, RK is increasing focus on light trucks/pass cars and railways. In the domestic segment, the announcement of a scrappage scheme will benefit CV sales over FY21. As demand trends remain soft, the co is focusing on expanding product/customer mix.

STANCE

We are NEUTRAL on RK Forgings (1) While the CV segment outlook is mixed, diversification initiatives will de-risk the business model. The expected acquisition of ACIL will provide access to tractor/2W customers (2) The co is sustaining market share in the domestic segment, amidst a sedate demand environment.

Financial Summary: Standalone

YE March (Rs mn)	2QFY20	2QFY19	YoY (%)	1QFY20	QoQ (%)	FY18	FY19	FY20E	FY21E	FY22E
Net Sales	2,607	4,615	(43.5)	3,792	(31.3)	14,355	18,067	15,036	16,388	18,375
EBITDA	473	979	(51.7)	722	(34.5)	2,842	3,795	2,830	3,228	3,657
APAT	7	328	(97.8)	135	(94.7)	947	1,193	476	619	863
Diluted EPS (Rs)	0.2	10.1	(97.8)	4.1	(94.7)	29.0	36.6	14.6	19.0	26.5
APAT Growth (%)						763.4	26.0	(60.1)	30.1	39.5
P/E (x)						9.9	7.9	19.7	15.1	10.9
RoE (%)						15.4	14.6	5.3	6.5	8.5

Source: Company, HDFC sec Inst Research

INDUSTRY	AUTOS
CMP (as on 11 Nov 2019)	Rs 288
Target Price	Rs 275
Nifty	11,913
Sensex	40,345

KEY STOCK DATA	
Bloomberg	RMKF IN
No. of Shares (mn)	33
MCap (Rs bn) / (\$ mn)	9/132
6m avg traded value (Rs mn)	14

STOCK PERFORMANCE (%)	
52 Week high / low	Rs 610/255
	3M 6M 12M
Absolute (%)	(33.9) (40.0) (51.5)
Relative (%)	(41.2) (47.7) (66.3)

SHAREHOLDING PATTERN (%)		
	Jun-19	Sep-19
Promoters	44.3	44.8
FIs & Local MFs	16.4	16.4
FPIs	14.1	11.9
Public & Others	25.3	26.8
Pledged Shares	6.5	7.8

Source : BSE

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In 2Q, tonnage declined -47% YoY, -35% QoQ due to weak demand environment

Blended realization grew ~7% YoY owing to higher exports in the mix (44% of revenue vs. 26% YoY)

EBITDA margin at 18.1% (below 20% now) impacted by lower capacity utilisation & negative operating leverage

The company will continue with the earlier tax regime for the time being

Quarterly financials snapshot: Standalone

Particulars (Rs mn)	2QFY20	2QFY19	YoY (%)	1QFY20	QoQ (%)	1HFY20	1HFY19	YoY (%)
Total Tonnage	18,517	35,038	(47.2)	28,558	(35.2)	47,075	68,074	(30.8)
-Domestic	11,498	27,563	(58.3)	20,484	(43.9)	31,982	53,524	(40.2)
-Exports	7,019	7,475	(6.1)	8,074	(13.1)	15,093	14,550	3.7
Avg realisation	140,552	131,706	6.7	132,677	5.9	135,775	128,087	6.0
Net sales (incl OOI)	2,607	4,615	(43.5)	3,792	(31.3)	6,399	8,719	(26.6)
Material Expenses	1,177	2,356	(50.0)	1,887	(37.6)	3,064	4,359	(29.7)
Employee Expenses	255	266	(4.3)	241	5.8	496	474	4.6
Other Operating Expenses	702	1,013	(30.7)	942	(25.5)	1,644	2,043	(19.5)
Total Expenditure	2,134	3,636	(41.3)	3,070	(30.5)	5,204	6,876	(24.3)
EBITDA	473	979	(51.7)	722	(34.5)	1,195	1,844	(35.2)
Depreciation	284	280	1.5	326	(12.8)	610	547	11.4
EBIT	189	699	(73.0)	396	(52.4)	585	1,296	(54.9)
Other Income	4	6	(33.7)	4	12.7	8	12	(36.3)
Interest Cost	181	206	(12.2)	198	(8.8)	379	381	(0.5)
PBT	12	499	(97.6)	202	(94.0)	214	928	(76.9)
Tax	5	171	(97.0)	67	(92.4)	72	322	(77.8)
RPAT	7	328	(97.8)	135	(94.7)	142	605	(76.5)
EPS	0.2	10.1	(97.8)	4.1	(94.7)	4.4	18.6	(76.5)

Source: Company, HDFC sec Inst Research

Margin Analysis: Standalone

As % of sales	2QFY20	2QFY19	YoY (bps)	1QFY20	QoQ (bps)	1HFY20	1HFY19	YoY (bps)
Material Expenses	45.2	51.1	(590)	49.8	(460)	47.9	50.0	(210)
Employee Expenses	9.8	5.8	401	6.4	342	7.7	5.4	231
Other Operating Expenses	26.9	22.0	497	24.8	207	25.7	23.4	226
Total Expenditure	81.9	78.8	307	81.0	90	81.3	78.9	247
EBITDA	18.1	21.2	(307)	19.0	(90)	18.7	21.1	(247)
RPAT	0.3	7.1	(684)	3.6	(329)	2.2	6.9	(472)
Tax as % of PBT	41.5	34.3	722	33.0	853	33.5	34.7	(127)

Source: Company, HDFC sec Inst Research

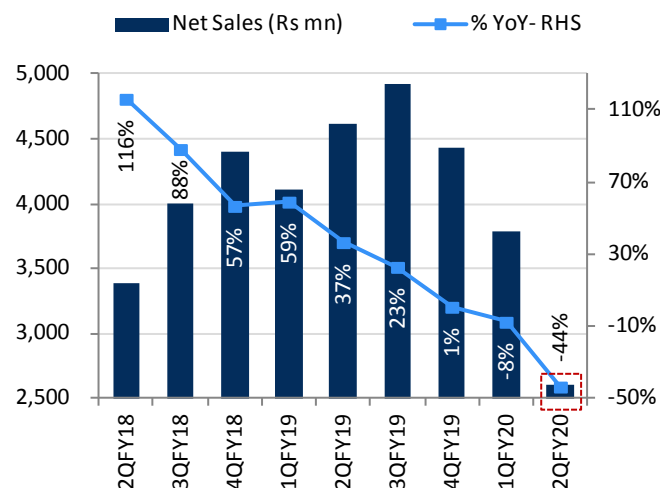
The co is expanding into the European markets and has won orders from the VW Group (Scania and MAN)

New capacity of 20k Tons will be commissioned in 4Q, which will be for supplies to LCV segment

Management expects Class 8 Truck sales to decline 10-15% in CY20

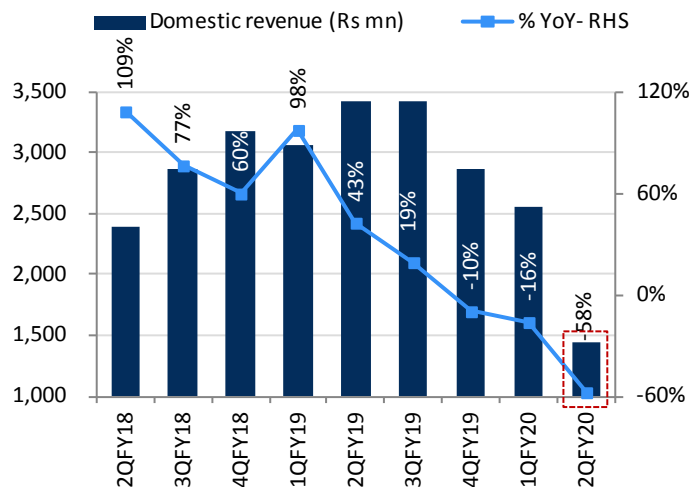
The co expects to increase supplies to Indian Railways in FY21

Weak macros impact revenues



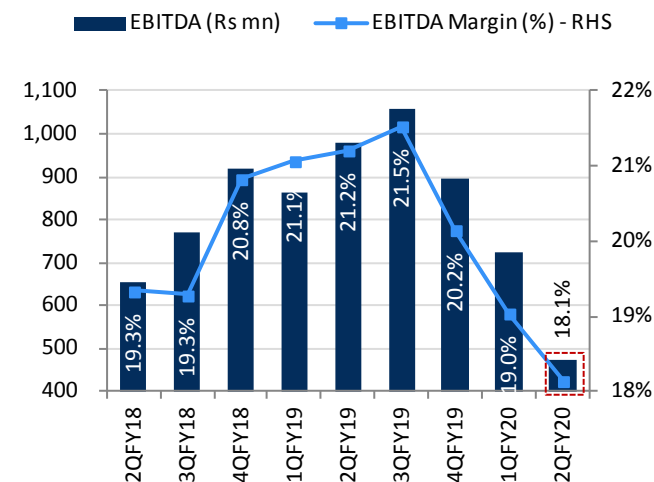
Source: Company, HDFC sec Inst Research

Domestic revenues: Weak trajectory



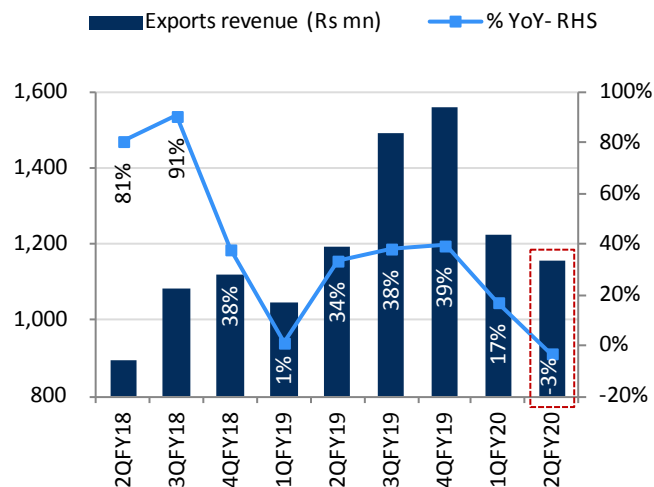
Source: Company, HDFC sec Inst Research

EBITDA margin impacted by sedate demand



Source: Company, HDFC sec Inst Research

Exports are moderating



Source: Company, HDFC sec Inst Research

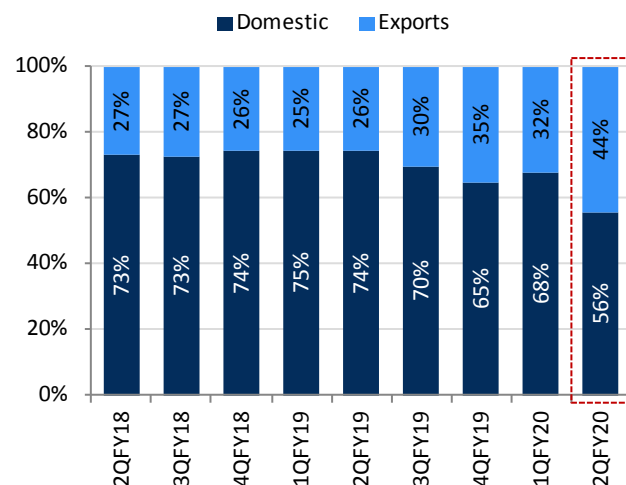
Exports have risen to over 40% of sales due to significant drop in domestic volumes

USA market is 80% of RK Forgings' sales and Europe is 20%. There has been a 5% increase in European exposure

Class 5/8 trucks are ~70% of total exports to USA

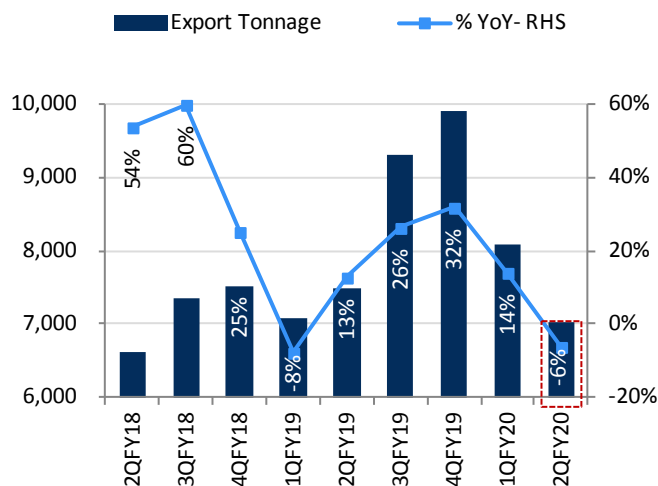
Management aspires to diversify into tractors, 2Ws with the acquisition of ACIL. They will form a 100% subsidiary and will raise debt of Rs 650mn towards the same

Exports were above 40% of sales



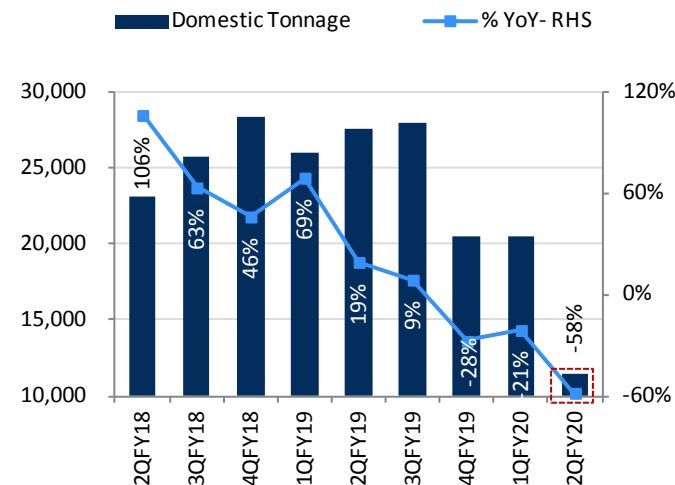
Source: Company, HDFC sec Inst Research

Exports tonnage sales



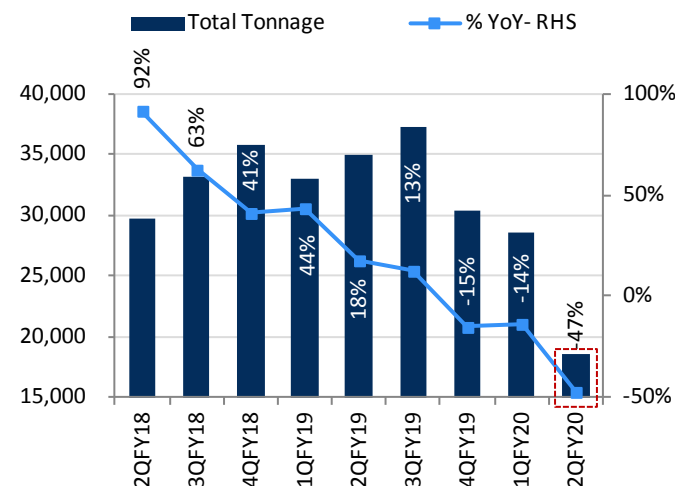
Source: Company, HDFC sec Inst Research

Domestic tonnage declined on weaker product mix



Source: Company, HDFC sec Inst Research

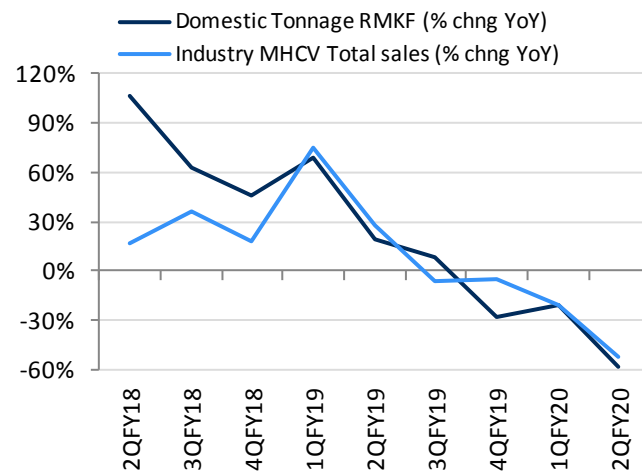
Total tonnage sales



Source: Company, HDFC sec Inst Research

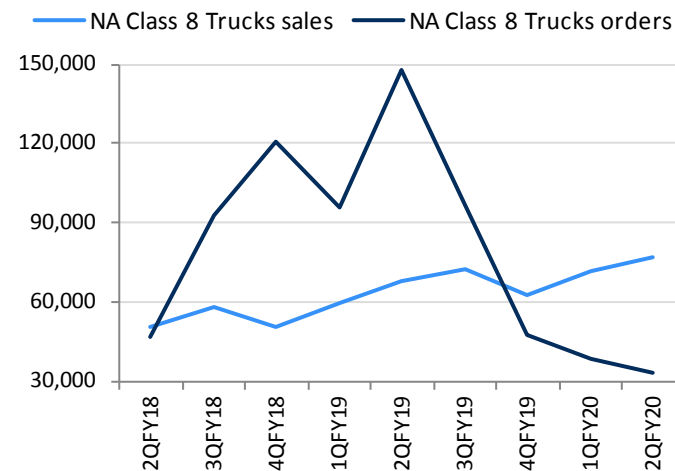
US Class 8 monthly truck orders remain weak over the year

Industry M/HCV sales and RMKF's tonnage growth



Source: Company, SIAM, HDFC sec Inst Research

US Class 8 truck sales and order inflows



Source: Bloomberg, HDFC sec Inst Research

Volume assumptions

(in tons)	FY18	FY19	FY20E	FY21E	FY22E
Domestic Sales	92,503	1,02,033	74,200	78,996	86,467
% YoY	48.9	10.3	(27.3)	6.5	9.5
Exports Sales	29,164	33,758	34,433	36,155	39,047
% YoY	43.9	15.8	2.0	5.0	8.0
Total Volumes	1,21,667	1,35,791	1,08,633	1,15,151	1,25,514
% YoY	47.7	11.6	(20.0)	6.0	9.0
Blended ASP (Rs/T)	1,17,984	1,33,049	1,38,407	1,42,317	1,46,397
% YoY	10.4	12.8	4.0	2.8	2.9

Source: Company, HDFC sec Inst Research

Change in estimates

	NEW			OLD			% CHANGE		
	FY20	FY21	FY22	FY20	FY21	FY22	FY20	FY21	FY22
Net Revenue	15,036	16,388	18,375	15,307	16,676	18,689	(2)	(2)	(2)
EBITDA	2,830	3,228	3,657	2,939	3,285	3,719	(4)	(2)	(2)
EBITDA margin (%)	18.8	19.7	19.9	19.2	19.7	19.9	-38 bps	0 bps	0 bps
PAT	476	619	863	484	636	872	(2)	(3)	(1)
EPS	14.6	19.0	26.5	14.8	19.5	26.8	(1)	(3)	(1)

Source: Company, HDFC sec Inst Research

Peer set comparison

Company	MCap (Rsbn)	CMP	Rating	TP	Adj EPS (Rs/sh)			P/E (x)			ROE (%)		
					FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E
RK Forgings	9.4	288	NEU	275	14.6	19.0	26.5	19.7	15.1	10.9	5.3	6.5	8.5
Subros	15.8	243	BUY	270	9.7	13.3	17.9	25.0	18.2	13.5	8.8	10.9	13.1

Source: HDFC sec Inst Research

Income Statement (Standalone)

(Rs mn)	FY18	FY19	FY20E	FY21E	FY22E
Net Revenues	14,355	18,067	15,036	16,388	18,375
Growth (%)	63.0	25.9	(16.8)	9.0	12.1
Material Expenses	7,138	9,265	7,328	8,243	9,353
Employee Expenses	874	968	977	983	1,066
Other Operating Expenses	3,501	4,039	3,900	3,933	4,300
Total Expenses	11,512	14,272	12,206	13,160	14,718
EBITDA	2,842	3,795	2,830	3,228	3,657
EBITDA Margin (%)	19.8	21.0	18.8	19.7	19.9
EBITDA Growth (%)	80	34	(25)	14	13
Depreciation	844	1,208	1,306	1,441	1,532
EBIT	1,998	2,587	1,524	1,787	2,125
Other Income (Including EO Items)	42	30	42	54	68
Interest	698	792	861	928	947
PBT	1,342	1,824	705	913	1,246
Tax (Incl Deferred)	396	631	229	294	382
Minority Interest	-	-	-	-	-
RPAT	947	1,193	476	619	863
APAT	947	1,193	476	619	863
APAT Growth (%)	763	26	(60)	30	40
Adjusted EPS (Rs)	29.0	36.6	14.6	19.0	26.5
EPS Growth (%)	660	26	(60)	30	40

Source: Company, HDFC sec Inst Research

Balance Sheet (Standalone)

(Rs mn)	FY18	FY19	FY20E	FY21E	FY22E
SOURCES OF FUNDS					
Share Capital - Equity	326	326	326	326	326
Reserves	7,266	8,403	8,850	9,432	10,243
Total Shareholders Funds	7,592	8,729	9,176	9,758	10,569
Long Term Debt	5,330	5,857	6,157	6,157	6,157
Short Term Debt	3,452	3,321	3,521	3,721	3,921
Total Debt	8,781	9,177	9,677	9,877	10,077
Net Deferred Taxes	344	572	663	757	871
TOTAL SOURCES OF FUNDS	16,718	18,478	19,517	20,392	21,518
APPLICATION OF FUNDS					
Net Block	10,679	11,063	10,757	10,616	10,085
CWIP	436	1,296	1,396	1,186	976
Investments	193	193	193	193	193
Total Non-current Assets	11,308	12,552	12,346	11,995	11,253
Cash & Equivalents	4	25	1,743	2,687	3,820
Inventories	2,994	3,313	3,337	3,592	4,027
Debtors	4,722	4,660	4,531	4,714	5,286
Other Current Assets	1,096	938	1,072	1,225	1,401
Total Current Assets	8,816	8,936	10,682	12,219	14,534
Creditors	2,889	2,578	3,048	3,322	3,725
Other Current Liabilities & Provns	517	432	464	500	545
Total Current Liabilities	3,406	3,009	3,512	3,822	4,270
Net Current Assets	5,410	5,926	7,171	8,397	10,264
TOTAL APPLICATION OF FUNDS	16,718	18,478	19,517	20,392	21,518

Source: Company, HDFC sec Inst Research

Cash Flow (Standalone)

(Rs mn)	FY18	FY19	FY20E	FY21E	FY22E
Reported PBT	1,342	1,824	705	913	1,246
Non-operating & EO Items	(42)	(30)	(42)	(54)	(68)
Interest Expenses	698	792	861	928	947
Depreciation	844	1,208	1,306	1,441	1,532
Working Capital Change	(2,018)	(495)	473	(281)	(735)
Tax Paid	(280)	(404)	(137)	(201)	(268)
OPERATING CASH FLOW (a)	545	2,896	3,166	2,746	2,654
Capex	(1,272)	(2,453)	(1,100)	(1,090)	(790)
Free Cash Flow (FCF)	(727)	443	2,066	1,656	1,864
Investments	(0)	-	-	-	-
Non-operating Income	42	30	42	54	68
INVESTING CASH FLOW (b)	(1,230)	(2,423)	(1,058)	(1,036)	(722)
Debt Issuance/(Repaid)	(574)	396	500	200	200
Interest Expenses	(698)	(792)	(861)	(928)	(947)
FCFE	(1,999)	47	1,704	928	1,116
Share Capital Issuance	1,989	3	0	0	(0)
Dividend	(39)	(59)	(29)	(37)	(52)
FINANCING CASH FLOW (c)	678	(452)	(390)	(766)	(799)
NET CASH FLOW (a+b+c)	(8)	21	1,718	945	1,133
Closing Cash & Equivalents	4	25	1,743	2,688	3,820

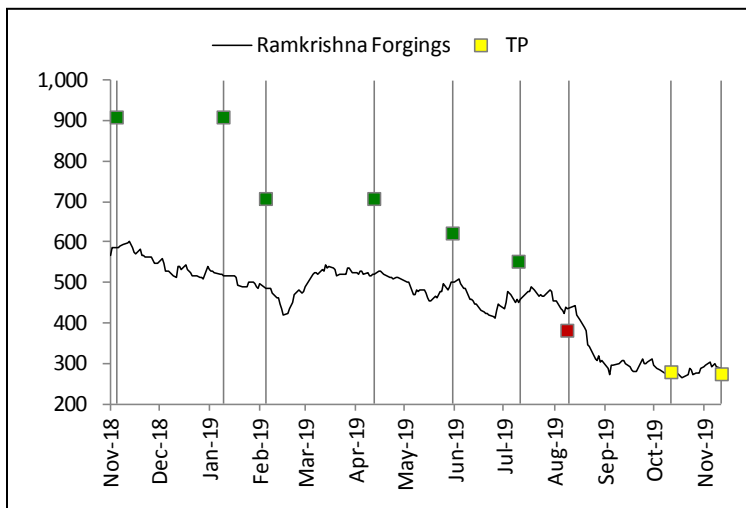
Source: Company, HDFC sec Inst Research

Key Ratios (Standalone)

	FY18	FY19	FY20E	FY21E	FY22E
PROFITABILITY (%)					
GPM	50.3	48.7	51.3	49.7	49.1
EBITDA Margin	19.8	21.0	18.8	19.7	19.9
EBIT Margin	13.9	14.3	10.1	10.9	11.6
APAT Margin	6.6	6.6	3.2	3.8	4.7
RoE	15.4	14.6	5.3	6.5	8.5
RoIC (or Core RoCE)	9.1	9.6	5.7	6.8	8.3
RoCE	9.1	9.6	5.4	6.1	7.0
EFFICIENCY					
Tax Rate (%)	29.5	34.6	32.5	32.2	30.7
Fixed Asset Turnover (x)	1.3	1.5	1.2	1.4	1.7
Inventory (days)	76	67	81	80	80
Debtors (days)	120	94	110	105	105
Other Current Assets (days)	28	19	26	27	28
Payables (days)	73	52	74	74	74
Other Current Liab & Provns (days)	13	9	11	11	11
Cash Conversion Cycle (days)	137	119	132	127	128
Debt/EBITDA (x)	3.1	2.4	2.8	2.2	1.7
Net D/E (x)	1.2	1.0	0.9	0.7	0.6
Interest Coverage (x)	2.9	3.3	1.8	1.9	2.2
PER SHARE DATA (Rs)					
EPS	29.0	36.6	14.6	19.0	26.5
CEPS	54.9	73.6	54.6	63.2	73.4
Dividend	1.0	1.5	0.7	0.9	1.3
Book Value	233	268	281	299	324
VALUATION					
P/E (x)	9.9	7.9	19.7	15.1	10.9
P/BV (x)	1.2	1.1	1.0	1.0	0.9
EV/EBITDA (x)	6.4	4.9	6.1	5.1	4.3
EV/Revenues (x)	1.3	1.0	1.2	1.0	0.9
OCF/EV (%)	3.0	15.6	18.3	16.6	17.0
FCF/EV (%)	(4.0)	2.4	11.9	10.0	11.9
FCFE/Mkt Cap (%)	(21.3)	0.5	18.2	9.9	11.9
Dividend Yield (%)	0.3	0.5	0.3	0.3	0.5

Source: Company, HDFC sec Inst Research

RECOMMENDATION HISTORY



Date	CMP	Reco	Target
5-Nov-18	591	BUY	908
9-Jan-19	515	BUY	908
4-Feb-19	488	BUY	705
12-Apr-19	520	BUY	705
31-May-19	502	BUY	620
10-Jul-19	463	BUY	550
13-Aug-19	440	SELL	380
11-Oct-19	270	NEU	280
13-Nov-19	288	NEU	275

Rating Definitions

BUY : Where the stock is expected to deliver more than 10% returns over the next 12 month period
NEUTRAL : Where the stock is expected to deliver (-)10% to 10% returns over the next 12 month period
SELL : Where the stock is expected to deliver less than (-)10% returns over the next 12 month period

Disclosure:

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