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Initiating Coverage

Mahindra CIE Automotive Ltd.

28-April-2021



Mahindra CIE Automotive Ltd.



Industry	LTP	Recommendation	Base Case Fair Value	Bull Case Fair Value	Time Horizon
Auto Ancillaries	Rs 164.7	Buy at LTP and add on dips in Rs 142-144 band	Rs 178	Rs 192	2 quarters

HDFC Scrip Code	MAHCIE
BSE Code	532756
NSE Code	MAHINDCIE
Bloomberg	MACA IN
CMP Apr 27, 2021 (Rs)	164.7
Equity Capital (cr)	379.0
Face Value (Rs)	10
Eq. Share O/S (cr)	37.9
Market Cap (Rs cr)	6242.7
Book Value (Rs)	129.5
Avg.52 Wk Volume	308,600
52 Week High (Rs)	234.9
52 Week Low (Rs)	78.1

Share holding Pattern % (Mar, 2021)	
Promoters	71.62
Institutions	18.36
Non-Institutions	10.03
Total	100.0

Fundamental Research Analyst

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Our Take:

Mahindra CIE Automotive Ltd. (MHCIE) is a multi-technology automotive component manufacturer catering to top companies like Mahindra, Tata Motors, Maruti, Bajaj and Hero Motocorp in the domestic market and Renault, Ford, JLR, and BMW in the European market. Its products cater to all the segments of the automobile industry. The Indian and European PV market is expected to grow by 10.2% and 4.6% CAGR respectively over FY20-FY25, according to IHS Global, while CRISIL expects domestic 2W market to grow at 5-7%.

MHCIE has a strong diversified presence across processes, which prepares it for any change or shift in demand on account of EV adoption. The technology shift is likely to favor more stamped, plastic and aluminum parts. The company's order book is strong, while it has plans for capacity expansion in many of its verticals. The acquisitions of Bill Forge in 2016 and Aurangabad Electricals in 2019 have added to its product range and helped garner more market share. When the global economy recovers from the pandemic, demand for personal mobility vehicles is likely to go up, thereby benefitting companies like MHCIE. MHCIE's alliance with CIE took place in 2014; more recently in the Sep quarter, the latter increased its stake in the former from 56% to 60%.

Valuations & Recommendation:

We expect MHCIE revenue to grow at 13% CAGR over CY20-CY23, led by the strong India business. Cost rationalization measures, greater operational efficiency, and product and customer diversification would drive EBITDA and PAT margin expansion of 420bps and 440bps during the same period. RoCE/RoE (excl. Goodwill) are expected to improve from 10.1/11.5% in CY20 to 23.7/26.5% by CY23E. MHCIE has added 25 new customers over the last two years, across its product lines and end markets, and it is now targeting at least 25% of its annual revenue (earlier 15%) to come from the new customers. We believe investors can buy the stock at LTP and add on dips to Rs 142-144 band (10x CY23E EPS) for a base case fair value of Rs 178 (12.5x CY23E EPS) and bull case fair value of Rs 192 (13.5x CY23E EPS).

Financial Summary

Particulars (Rs cr)	Q4CY20	Q4CY19	YoY (%)	Q3CY20	QoQ (%)	CY20	CY21E	CY22E	CY23E
Operating Income	1957.6	1722.9	13.6	1694.3	15.5	6,050.1	7,206.3	8,044.4	8,650.5
EBITDA	247.3	204.6	20.9	168.3	47.0	501.6	864.8	933.1	1,081.3
APAT	111.7	19.8	462.6	60.8	83.7	106.4	396.1	437.3	540.4
Diluted EPS (Rs)	2.9	0.5	462.6	1.6	83.7	2.8	10.5	11.5	14.3
RoE (excl. Goodwill-%)						11.5	35.0	28.2	26.5
P/E (x)						58.6	15.7	14.3	11.5
EV/EBITDA (x)						14.8	8.2	7.1	5.6

(Source: Company, HDFC sec)

Recent Triggers

Q4CY20 financials

Consolidated revenue of the company increased by 13.6% yoy to Rs 1,958cr, driven mainly by the domestic business. India business increased by 17.3% yoy to Rs 970cr, led by strong growth in tractors, PV, 2W and CVs. However, revenue from the European business declined 3% yoy (in euro terms) while it increased 7% in rupee terms to Rs 895cr, underperforming the industry growth. Consolidated EBITDA margin improved by 70bps to 12.6% due to the cost reduction, cash protection, and reduction in breakeven point programs initiated at the height of the pandemic in the domestic business (EBITDA margin 15.3% +270bps). Margin improvement was partially offset by the ongoing restructuring exercise (100 bps impact) in the European business (11.9% -90bps). Major restructuring has been completed and going forward the impact of the same will be limited.

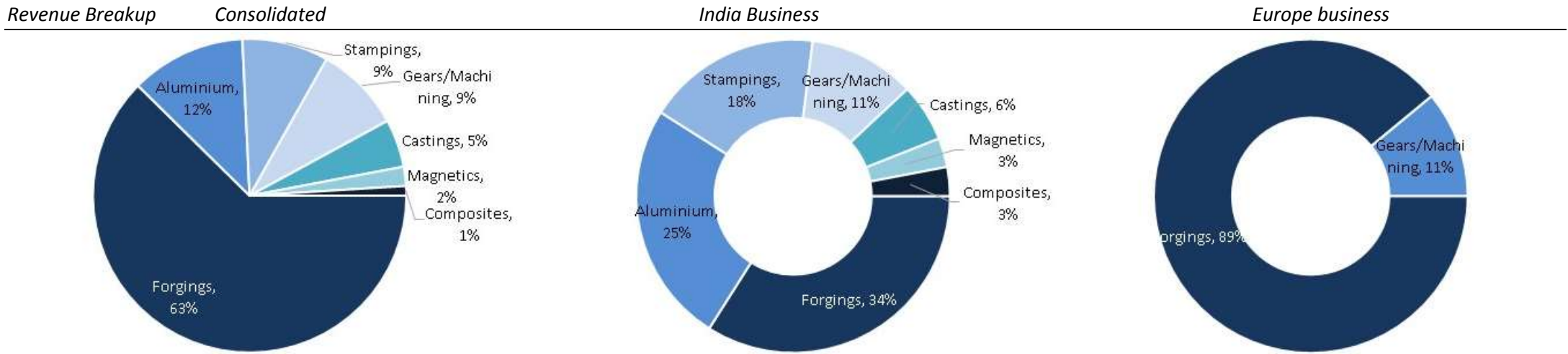
Consolidated PAT grew from Rs 14cr in Q4CY19 to Rs 112cr, mainly on account of the impact of lower tax rates on deferred taxes. At the PBT level, MHCIE reported growth of 31% to Rs 161cr.

In Q4CY20, the share of India business in the consolidated sales was 52% while the share in PBT was 54%, reflecting margin improvement in India. This trend is expected to continue, with the Indian business slated to grow much faster than Europe. The company said it has added more than 25 new customers in the past two years, which should drive revenue and outperformance (over the broader industry).

Long term Triggers

Diversified operations reduce risk

MHCIE operations are diversified in terms of geography, product segments, and end-use segments. The company is amongst the largest auto components suppliers in India. In Europe, it is one of the leading forgings suppliers for PV, CV and off-highway segment. It is present in six business segments—forging, stamping, casting, gears, composite, and magnetic products. Its six business divisions are spread across passenger vehicles, commercial vehicles, tractors, two-wheelers, and off-road segments. The diversified nature of revenue reduces dependence on a particular segment of the automobile industry and reduces the overall risk for the company. MHCIE has overall 31 plants, which includes eight in Europe and one in Mexico.



(Source: Company, HDFC sec)

MHCIE to be at frontend for EV part supplies

The global automotive market is gradually moving towards electric vehicles (EV). Although the EV technology in India is still in nascent stages, the increasing spend on R&D towards EV could change the landscape rapidly. Adoption of EVs has been slow due to the high cost

of technology. However, with wider adoption, economies of scale would kick in and reduce the overall cost. CIE as a group is working closely with Tesla and Renault on EVs. It already supplies parts to these EVs - largely plastic and stamped parts. MCIE supplies to M&M Electric Vehicle platforms and includes E2O and the alfa e-rickshaw. MCIE's Bill Forge division has also bagged orders for supply to KIA motor's electric vehicle.

Concentration on fast growing segments in the domestic market

MHCIE's domestic business is focused on car and utility vehicles, tractors, and two wheelers, which have witnessed faster growth after the pandemic due to (1) growing preference for personal mobility and (2) government's thrust on improving agricultural income. The company is focusing on increasing revenue through increasing (1) the share of value-added products like machined castings, higher grade magnets, complex gears, etc. and (2) exports. The long-term picture for the car market remains healthy, given the current low vehicle penetration levels and, as per capita income continues to grow, it will increase the Indian household's ability to afford a car. IHS Global expects the Indian light vehicles (less than 6T) to grow at a CAGR of 10.2% over 2020-25.

Focus on improving European business margins

In the European business, MHCIE's focus is to sustain and gradually improve profitability in the face of a slowly recovering market demand. The company plans to grow its operations by investing selectively. It is looking to restructure operations in Germany and Italy and bring them in line with the reduced demand in a bid to maintain and improve margins. MHCIE is targeting to increase its market share in crankshafts, introduce aluminium forgings, and focus on non-engine parts with dual use in battery electric vehicles (BEV) like knuckles.

China substitution could benefit MHCIE

Many global auto OEMs are following a China plus one strategy when it comes to their supply chains. The Indian government has announced a Production Linked Incentive (PLI) for the automotive industry, which is aimed at boosting manufacturing in India, the details of which are awaited. This is expected to help high quality automotive component manufacturers in India like MHCIE. European auto OEMs are also looking to offshore some part of their component requirements to low-cost countries. MHCIE is working together with its European counterparts both at MHCIE Europe and CIE to take advantage of these opportunities.

Operational and managerial support from CIE Automotive SA

CIE enjoys a global automotive footprint across multiple product segments (forgings/castings/stamping). Moreover, MCIE enjoys a strategic importance in CIE's global operations as the auto component division for South Asian and South East Asian markets. It is expected

to benefit from CIE's strong technological expertise and established relationships with global OEMs. MCIE has a medium-term plan to introduce CIE's products (such as plastics) to the Indian market, which will further help diversify its product portfolio and client base.

MCIE is CIE's vehicle for forgings worldwide and for other businesses in India and South East Asia. The CIE and MCIE operating teams work seamlessly. Experts from CIE are working in many MCIE plants on joint improvement projects. CIE does not charge any royalty for any knowhow transfer. MCIE has seamlessly integrated into the CIE system and we have not come across any conflict. CIE has increased its stake in MHCIE to 60.18% in Q4CY20, from 56.28% earlier.

What could go wrong?

Slowdown in automobile industry

MHCIE primarily caters to the automobile industry in India and Europe, which are emerging from a major slowdown. Although the improving trends are encouraging, a huge part of the recent growth was on account of pent-up demand. Sustenance of demand would be the key monitorable in the coming quarters.

Rapid adoption of EVs could reduce forged part requirements

On a consolidated basis, MHCIE derives 63% of its revenues from forgings. The shift from ICV to EV would mean reduction in forged, cast, and machined parts and increase in stamped, aluminum, and plastic parts. CIE/MHCIE being a multi-technology group that covers forgings, castings, stampings, machining, Aluminum and Plastics (currently it is not into plastics) is well-positioned to make this transition. Around 25% of MHCIE's revenues would be affected by the growing EV popularity. One-third of MHCIE's European revenues come from crankshafts, which will be at risk because of the shift towards EVs. To offset the increasing risk of EVs in the EU, MHCIE looks to dilute the impact through increased market share in crankshafts, a focus on non-engine parts such as knuckles and motor housing, and aluminum forging.

Foreign exchange risk

The company derives ~52% of its revenue from global operations and, thus, volatility in exchange rates could impact its revenue and profits.

No dividend paid in the past

MHCIE has not paid any dividend in the past as it is a foreign-owned, foreign-operated company in India and is not allowed to avail domestic loans to acquire companies. Since the company may conserve cash for acquisitions, it might not pay dividend for a few years.

Goodwill write-off could reduce profitability

The company has goodwill of Rs 3,755cr on its books, which it might have to write off in the future if its acquisitions don't perform in line with expectations. This would impact its profitability in the year in which it is written off. The removal of tax benefit on the amortisation of goodwill in the latest budget would have no impact on the P&L account. However, cash outflow on tax would increase as it was seeing good benefit from this.

High exposure to EU auto market

52% of MHCIE's consolidated revenue comes from EU markets. Any prolonged slowdown in these markets can impact its overall growth.

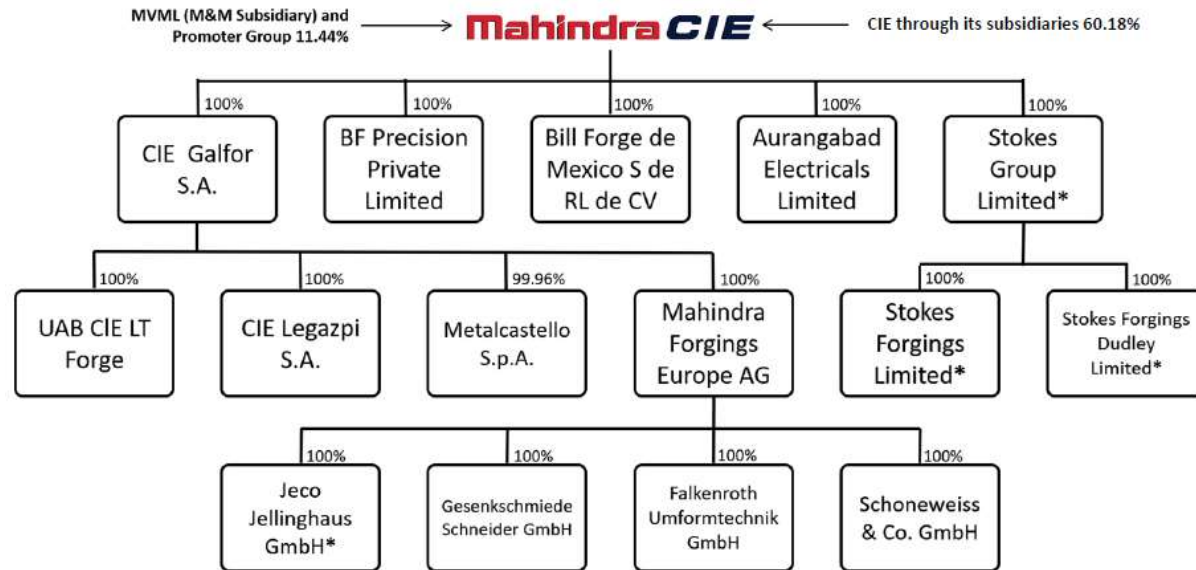
About the company

Mahindra CIE Automotive Ltd (MHCIE) is a multi-locational and multi-technology automotive components company with manufacturing facilities and engineering capabilities in India and in Germany, Spain, Lithuania, and Italy in the Europe as well as a plant in Mexico. It has an established presence in each of these locations and supplies to automotive Original Equipment Manufacturers (OEMs) and their Tier 1 suppliers. Apart from its strong presence in forgings, MHCIE is also among the largest ductile iron casting and compression moulded auto components manufacturers in India.

It is part of the global auto component player, CIE Automotive Group, based out of Spain. MHCIE was earlier known as Mahindra Forgings Ltd (part of Mahindra Systech Division) and was later renamed, following the integration of the Mahindra Group's Systech business with CIE's operations, which was announced in 2013. Mahindra Systech, a division of Mahindra & Mahindra, was created in 2004 to capitalise on the opportunities presented by the growth of the Indian automobile component industry. The Systech auto component division (comprising multiple companies - listed and unlisted) encompassed products across forgings, stampings, castings, gears, magnetic products and composites. Under CIE's parentage, MHCIE has been able to improve its efficiencies, cut costs, and improve profitability.

MHCIE has 31 manufacturing facilities including 8 manufacturing facilities in Europe and 1 in Mexico. The manufacturing locations are generally located close to major automotive manufacturing hubs in order to facilitate supplies to customers. MHCIE largely operates in the automotive markets of Europe and India. In Europe, MHCIE supplies components mainly to the light vehicles and heavy truck markets with a comparatively small business in the off-road sector. In India, MHCIE is more diversified and supplies components to the light vehicles segment (both passenger vehicles and light commercial vehicles), two wheelers, tractors, medium and heavy commercial vehicles, in order of dependence.

Company structure



(Source: Company, HDFC sec)

Financials – Consolidated

Income Statement

(Rs cr)	CY19	CY20	CY21E	CY22E	CY23E
Net Revenues	7907.8	6050.1	7206.3	8044.4	8650.5
Growth (%)	-1.5	-23.5	19.1	11.6	7.5
Operating Expenses	6940.0	5548.5	6341.5	7111.2	7569.2
EBITDA	967.8	501.6	864.8	933.1	1081.3
Growth (%)	-7.9	-48.2	72.4	7.9	15.9
EBITDA Margin (%)	12.2	8.3	12.0	11.6	12.5
Depreciation	316.1	306.4	343.0	375.8	400.8
Other Income	33.1	54.9	64.9	72.4	77.9
EBIT	684.8	250.1	586.6	629.7	758.3
Interest expenses	52.3	54.8	44.0	34.8	28.0
PBT	627.9	195.3	542.6	594.9	730.3
Tax	274.1	88.7	146.5	157.7	189.9
PAT	353.8	106.6	396.1	437.3	540.4
Loss from discontinued oper.	0.0	-0.2	0.0	0.0	0.0
Adj. PAT	353.8	106.4	396.1	437.3	540.4
Growth (%)	-29.0	-69.9	272.3	10.4	23.6
EPS	9.3	2.8	10.5	11.5	14.3

Balance Sheet

As at December (Rs cr)	CY19	CY20	CY21E	CY22E	CY23E
SOURCE OF FUNDS					
Share Capital	379.0	379.0	379.0	379.0	379.0
Reserves	4254.8	4529.0	4925.1	5362.4	5902.8
Shareholders' Funds	4633.8	4908.0	5304.1	5741.4	6281.8
Minority Interest	0.0	0.0	0.0	0.0	0.0
Borrowings	1469.1	1647.6	1497.6	1287.6	1047.6
Net Deferred Taxes	91.2	123.6	123.6	123.6	123.6
Total Source of Funds	6194.1	6679.2	6925.3	7152.6	7453.0
APPLICATION OF FUNDS					
Net Block & Goodwill	6043.5	6741.3	6748.3	6747.5	6746.7
CWIP	54.2	12.3	12.3	12.3	12.3
Investments	95.5	234.0	284.0	384.0	484.0
Other Non-Curr. Assets	283.8	123.7	144.1	152.8	155.7
Total Non Current Assets	6477.0	7111.3	7188.7	7296.6	7398.7
Inventories	1056.6	1006.2	1184.6	1278.3	1327.2
Trade Receivables	736.8	705.4	888.4	947.7	971.7
Cash & Equivalents	149.9	238.1	393.0	498.5	704.3
Other Current Assets	142.4	302.5	335.6	352.6	379.2
Total Current Assets	2085.7	2252.2	2801.7	3077.1	3382.4
Trade Payables	1477.1	1459.0	1678.2	1763.2	1824.9
Other Current Liab & Provisions	891.5	1225.3	1387.0	1458.0	1503.2
Total Current Liabilities	2368.6	2684.3	3065.1	3221.2	3328.1
Net Current Assets	-282.9	-432.1	-263.4	-144.1	54.3
Total Application of Funds	6194.1	6679.2	6925.3	7152.6	7453.0

Cash Flow Statement

(Rs cr)	CY19	CY20	CY21E	CY22E	CY23E
EBIT	627.9	195.3	542.6	594.9	730.3
Non-operating & EO items	-9.4	-43.0	35.4	9.1	8.3
Interest Expenses	52.5	54.8	44.0	34.8	28.0
Depreciation	316.8	306.4	343.0	375.8	400.8
Working Capital Change	155.6	76.1	-69.6	-31.7	-3.8
Tax Paid	-116.1	-50.3	-146.5	-157.7	-189.9
OPERATING CASH FLOW (a)	1,027.3	539.3	749.0	825.3	973.8
Capex	-414.2	-301.6	-350.0	-375.0	-400.0
Free Cash Flow	613.1	237.7	399.0	450.3	573.8
Investments	591.1	-137.6	-50.0	-100.0	-100.0
Non-operating income	-765.9	9.8	0.0	0.0	0.0
INVESTING CASH FLOW (b)	-589.0	-429.4	-400.0	-475.0	-500.0
Debt Issuance / (Repaid)	-354.5	50.6	-150.0	-210.0	-240.0
Interest Expenses	-52.5	-54.8	-44.0	-34.8	-28.0
FCFE	31.3	105.7	154.9	105.5	205.8
Share Capital Issuance	3.0	0.0	0.0	0.0	0.0
Dividend	0.0	0.0	0.0	0.0	0.0
FINANCING CASH FLOW (c)	-404.0	-4.2	-194.0	-244.8	-268.0
NET CASH FLOW (a+b+c)	34.3	105.7	154.9	105.5	205.8

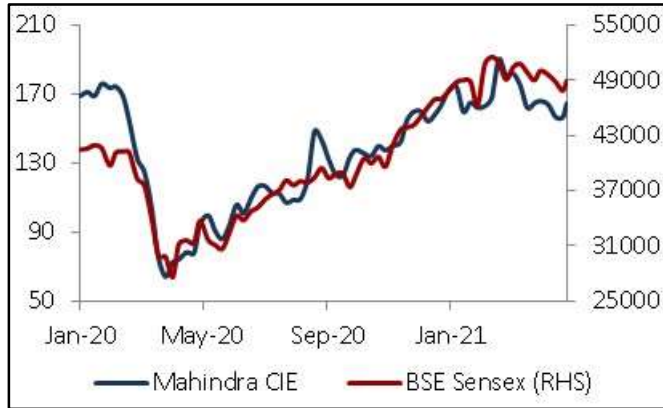
Key Ratios

	CY19	CY20	CY21E	CY22E	CY23E
Profitability Ratios (%)					
EBITDA Margin	12.2	8.3	12.0	11.6	12.5
EBIT Margin	8.7	4.1	8.1	7.8	8.8
APAT Margin	4.5	1.8	5.5	5.4	6.2
RoE (excl. Goodwill)	33.7	11.5	35.0	28.2	26.5
RoCE (excl. Goodwill)	26.4	10.1	21.7	21.4	23.7
Solvency Ratio (x)					
Net Debt/EBITDA	1.4	2.8	1.3	0.8	0.3
Net D/E	0.3	0.3	0.2	0.1	0.1
PER SHARE DATA (Rs)					
EPS	9.3	2.8	10.5	11.5	14.3
CEPS	17.7	10.9	19.5	21.5	24.8
BV	122.3	129.5	139.9	151.5	165.7
Dividend	0.0	0.0	0.0	0.0	0.0
Turnover Ratios (days)					
Inventory days	35.7	45.2	42.0	43.3	42.1
Debtor days	55.1	64.7	57.7	58.1	57.2
Creditors days	76.2	92.1	82.6	81.2	78.7
VALUATION (x)					
P/E	17.6	58.6	15.7	14.3	11.5
P/BV	1.3	1.3	1.2	1.1	1.0
EV/EBITDA	7.7	14.8	8.2	7.1	5.6
EV/Revenues	0.9	1.2	1.0	0.8	0.7
Dividend Yield (%)	0.0	0.0	0.0	0.0	0.0

(Source: Company, HDFC sec Research)



Price chart



Disclosure:

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