Stock Update

Rico Auto Industries Ltd.

October 18, 2023

RETAILRESEARCH

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Industry	LTP	Recommendation	Base Case Fair Value	Bull Case Fair Value	Time Horizon
Auto Ancillaries	Rs 87	Buy in Rs 86-89 band & add on dips in Rs 78-80 band	Rs 96	Rs 104	2-3 quarters

HDFC Scrip Code	RICAUTEQNR
BSE Code	520008
NSE Code	RICOAUTO
Bloomberg	RAI IN
CMP Oct 17, 2023	86.8
Equity Capital (Rs cr)	13.5
Face Value (Rs)	1
Equity Share O/S (cr)	13.5
Market Cap (Rs cr)	1174
Book Value (Rs)	50.9
Avg. 52 Wk Volumes	15,53,000
52 Week High (Rs)	111.5
52 Week Low (Rs)	54.5

Share holding Pattern % (Sep, 2023)	
Promoters	50.3
Institutions	1.1
Non Institutions	48.5
Total	100.0

* Refer at the end for explanation on Risk Ratings

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Our Take:

Rico Auto Industries Ltd. (Rico) is an established player in the auto ancillaries industry, with a track record of over three decades. It enjoys a strong market position in its key product segments: high-pressure aluminium and ferrous die cast components. The domestic market is doing well with higher PV and CV sales. Monsoons have picked up after a lull in August and should benefit 2W sales going in the festival season. Export market have also witnessed developments with a lot of sampling taking place and should result in strong export orders in the coming years. Also the new hybrid SUV launches from Toyota and Maruti have received good response (components supplied by Rico – and capex incurred for this). Toyota has already indicated higher offtake. With the growing demand for electric vehicles and the government's push for EV adoption, Rico Auto is positioning itself to take full advantage of the opportunities in the EV market while still maintaining a strong presence in the ICE market.

Rico has received approvals from Suzuki, Honda and Royal Enfield at better pricing as compared to that from its main customer Hero. Further it has taken steps towards renewable energy in both solar and wind which would reduce power & fuel expenses. Solar power would be available from Q3 at all its plants and wind from Q4 at its Chennai plant. The management has guided for Rs 2600cr of revenue in FY24 including defence revenue of Rs 80-100cr and double-digit EBITDA margin.

On September 12, 2022, we had released a Stock Update report (Link) with a recommendation to 'Buy in Rs 55.5-57.5 band & add on dips to Rs 50-51 band' for base case fair value of Rs 62.5 and bull case fair value of Rs 68.5 in 2-3 quarters. The targets were achieved within the given time frame.

Valuation & Recommendation:

Visibility of revenues for Rico continue to remain strong with regular order wins. The stock has corrected ~25-30% from the recent highs. The company has been benefited from its ability to develop new critical auto components for diversified automobile segments and their long established business relationships with diversified customer base. The managements' business acumen has helped the company to be the sole supplier for many auto components for BMW and several semi-electric vehicle (EV) components for Toyota. Improvement in operating margins would further be supported by efficiencies gained through stability of capital expenditure already incurred and focus of management to manufacture high value critical components.

The valuation looks attractive given the strong growth potential. We expect RICO's Revenue/EBITDA/PAT to grow at 12/19/46% CAGR over FY23-FY25E, led by increased demand from end user industries. We believe investors can buy the stock in Rs 86-89 band and add on dips in Rs 78-80 band (10x FY25E EPS) for a base case fair value of Rs 96 (12.25x FY25E EPS) and bull case fair value of Rs 104 (13.25x FY25E EPS) over the next 2-3 quarters.

Financial Summary

Particulars (Rs cr)	Q1FY24	Q1FY23	YoY (%)	Q4FY23	QoQ (%)	FY22	FY23	FY24E	FY25E
Revenues	534	563	-5.2	603	-11.5	1,860	2,302	2,577	2,864
EBITDA	51	47	8.4	67	-24.5	152	221	278	312
APAT	7	9	-22.4	26	-74.5	21	50	77	106
Diluted EPS (Rs)	0.5	0.6	-22.4	1.9	-74.5	1.5	3.7	5.7	7.8
RoE (%)						3.4	7.5	10.7	13.4
P/E (x)						56.1	23.6	15.2	11.1
EV/EBITDA (x)						11.4	8.4	6.2	5.4

(Source: Company, HDFC sec)

Q1FY24 Result Update

Revenues of the company were muted in Q1FY24 on account of sharp decline in sales to Renault and Hero Motocorp. Share of revenue from Renault fell from 12% to 6% due to lower offtake of its cars while Hero revenue fell on account of conscious decision taken by the company due to a dispute in pricing. Consolidated revenue degrew by 5.2/11.5% YoY/QoQ in Q1FY24 to Rs 534cr. Domestic revenue degrew 6% YoY to Rs 410cr while exports were down by 1.5% to Rs 128cr. Cooling raw material inflation and decline in other expenses resulted in 8% YoY increase in EBITDA to Rs 51r and 120bps expansion in EBITDA margin to 9.5%. Management expects double-digit EBITDA margins from Q2 onwards as it is confident of price settlement with Hero and higher volumes. PAT came in at Rs 6.6cr as compared to Rs 8.6cr in Q1FY23 as commissioning of Chennai plant expansion and higher borrowing led to increased depreciation and finance costs.

As mentioned in the press release for Q1FY24 results, Rico has been nominated for new business of program value of Rs 57cr in Q1FY24 with annualized peak value of Rs 198cr. In FY23 it won orders of Rs 1880cr with peak value of Rs 380cr. The management has guided for Rs 60-70cr of capex for FY24 comprising of maintenance capex and some balancing equipment. 85% of the components are fungible and the company can shift manufacturing between normal/electric/hybrid components without any further capex.

EV growth momentum remains strong

India saw 120% growth in electric vehicles (EVs) in the second quarter of this year, driven by a 400% surge in hybrid vehicles. By the end of this year, over 5% of passenger vehicles are likely to be fully electric and equipped with ADAS features. Rico expects the EV segment to play an increasingly significant role in the company's revenues, with EV contribution to revenues projected to increase by 4-5% every year going forward. Globally, BMW which is one of Rico's major export client is looking to double its EV sales in 2023. It is targeting 15% of its sales to be battery EVs in 2023.

Revenue from defence vertical to pick up

Rico's subsidiary AAN Engineering is a "Manufacturer of Precision Machined Components & Assemblies" for the Aerospace and Defence Industry. AAN is empaneled and registered with the Special Products division of Electronics Corporation of India Limited (ECIL), Hyderabad, Bharat Electronics Limited (BEL), Pune, Bharat Earth Movers Limited (BEML), Bangalore, Engine Divisions of Hindustan Aeronautical Limited (HAL) (Bangalore, Nasik and Koraput), Heavy Vehicles Factory (HVF) Avadi, Army Base Workshop and Army Directorate of Indigenization and various Ordnance Factories.

In FY23, AAN has been marked and shortlisted as a new supplier by BEML to bid for supply of Track Link Assembly for T-72 tanks. It has also signed Memorandum of Understanding (MOU) with Global Vehicle OEM for Assembly and Supply of Special Mobility Vehicle (SMV) to the Infantry wing of Indian Army. This particular technical engagement for Make in India procurement places the company as a preferred OEM for Indian Army.

The management has guided for Rs 80-100cr revenue from the defence segment in FY24. With the Indian Government pushing for Atma Nirbhar Bharat more and more defence orders are likely to be placed with domestic companies and defence vertical revenues could see a sharp uptick in the coming years.

Expansion of alloy wheel capacity

Rico Auto has increased its alloy wheels capacity from 3.5 million units to 4.5 million units. The company has potential revenue from capacity addition of ~Rs 500cr.

EBITDA to reach double-digits

Rico reported EBITDA margins of 9.6% in FY23. However, with the stabilizing of material cost and pass through of past raw material inflation, increase in volumes driving higher capacity utilization and improving efficiency, the management is confident of achieving double-digit operating margins FY24 onwards. It has guided for revenue of Rs 2600cr in FY24 (down from Rs 2700cr earlier).

Risks & Concerns

Slowdown in automobile industry

Rico supplies to automobile manufacturers and any slowdown in the automobile industry could impact its growth.

Concentration risk

Although the company is diversifying its customer base, almost 25-30% of its revenues came from supplies to Hero Motocorp, which exposes RAL to concentration risk.

Currency fluctuation

RAL derives ~22% of its revenues from supplies to overseas clients mainly in Europe and North America. Any changes in the exchange rate could impact earnings of the company.

Delays in merger of subsidiaries

RICO is looking to merge its subsidiaries with itself to have a better control over costs. Delays in merging the subsidiaries could result in higher expenses as well as take management time.

High Leverage

Rico has undertaken largely debt-funded capex of Rs 135cr over FY22-FY23 for a unit in Chennai catering to the Toyota Group, along with maintenance and certain other capex. Its debt to equity ratio has risen from 0.5:1 to 1.1:1 between FY19 and FY23 due to capex and insufficient profits. This situation needs to be remedied.

Low Return ratios

Rico has low return ratios due to low fixed asset turnover and low PAT margins. It is making efforts to improve both.

Company Background:

RICO is a world-class engineering company supplying a wide range of high precision fully machined aluminum and ferrous components and assemblies to automotive OEMs across the globe for electric vehicles, electrified vehicles and ICE engine. It has strong in-house R&D capabilities. RICO's multiple, flexible, fully integrated production facilities are equipped to offer complete spectrum of services from designing to development of tools, casting and precision machining and assembly of components making RICO a preferred supplier to the EV & Hybrid vehicle market.

RICO has earned a reputation of being a reliable source for the most complex components and assemblies. It is committed to manufacture products of uncompromising quality with highest standards of excellence backed by its ability to engineer the most demanding products as well as deliver global volumes across the world to cater the increasing demand of electrification.

Rico has its manufacturing plants at 15 locations and nearby major auto manufacturing hubs. For aluminium it has over 100 High Pressure Die Casting machines (up to 2700 Tns locking force). Its Die Casting capacity in India is among the most modern including GDC and LPDC. For ferrous products it has the 4 molding lines - 2 DISA & 2 Horizontal (SINTO & DISA). It has one of the largest machining facility in India with over 2500 machines for CNCs and SPMs. The strong manufacturing capabilities provides an edge to the company over some of its peers.

Subsidiaries & JVs

Rico Fluidtronics Ltd

Rico Fluidtronics is involved in the business of manufacturing oil & water pumps. It has won Maruti Suzuki Oil Pump & Water Pump (K15C) business, supplies of which have started in FY22. In FY22 it recorded a turnover of Rs 68.0cr and PAT of Rs 5.9cr. The company has enough orders from Maurti Suzuki and others in hand to cross Rs 130cr turnover in FY23. RICO owns 100% in the company.

Rico Jinfei Wheels Ltd.

Rico Jinfei is involved in the manufacture of Aluminum Alloy Wheels for two wheelers with a capacity of 1mn wheels. It has started supply of alloy wheels to Hero MotoCorp Limited which would help it to increase its turnover and improve margins. It recorded a turnover of Rs 221.1cr in FY22 and PAT of Rs 2.1cr. RICO has 94.8% stake in the company.

AAN Engineering

AAN Engineering is a Wholly Owned Subsidiary of RICO. It is a Defence venture/Business arm and it is 100% Indian Company and a world class Engineering Group supplying a wide range of High Precision Fully Machined Aluminium, Ferrous & certain Non-Ferrous and Assemblies to the Automotive OEM's across the Globe. AAN currently manufactures machined metal components for Mechanical and Electronic Fuse Assembly having installed capacity of 25,000 units per month. AAN reported revenue of Rs 11.7cr and loss of Rs 0.6cr in FY22.

Rico Auto Industries Inc., USA (RAII), wholly owned subsidiary of Rico, is engaged in trading of Auto Components and providing warehousing and logistics support to the OEM's and Tier I customers of Rico for the markets of United States of America.

Rico Auto Industries (UK) Limited (RAIUL), wholly owned subsidiary of Rico and is engaged in trading of Auto Components and providing Warehousing and logistics support to the OEM's and Tier I customers of Rico for the North America and Brazilian Markets.

Rico Friction Technologies Private Limited (RFTPL) is 70% held by Rico and manufactures friction materials for clutches and other applications.

Consolidated revenue trend (Rs cr)

Particulars	2022-23	2021-22 ^	2020-21	2019-20	2018-19
Total Revenue	**2,321.5**	**1,881.3**	**1,488.4**	**1,423.8**	**1,412.1**
Rico Auto Industries Limited	1,896.7	1,625.6	1,304.7	1,226.3	1,224.5
Rico Auto Industries Inc. USA	238.2	168.9	133.6	138.5	140.5
Rico Auto Industries (UK) Limited UK	0.4	5.2	5.9	5.9	97.3
Rico Fluidtronics Limited **	138.3	68.0	53.9	80.9	-
Rico Jinfei Wheels Limited #	302.8	232.9	149.7	119.7	136.5
Rasa Autocom Limited @	-	-	55.3	72.5	53.1
Rico Aluminium and Ferrous Auto Components Limited @	-	-	171.6	193.6	253.5
Rico Investments Limited @	-	-	4.7	5.9	5.9
AAN Engineering Industries Limited	15.7	11.6	9.1	2.0	4.2
Rico Friction Technologies Limited $	4.0	3.0	1.3	-	-
Less : Inter Company Sales	(274.6)	(234.0)	(401.3)	(421.5)	(503.4)
Rico Group Consolidated	**2,321.5**	**1,881.3**	**1,488.4**	**1,423.8**	**1,412.1**

(Source: Company, HDFC Sec)

Financials (Consolidated)

Income Statement

(Rs cr)	FY21	FY22	FY23	FY24E	FY25E
Net Revenues	**1470**	**1860**	**2302**	**2577**	**2864**
Growth (%)	***4.9***	***26.5***	***23.8***	***11.9***	***11.2***
Operating Expenses	1381	1708	2081	2298	2552
EBITDA	**89**	**152**	**221**	**278**	**312**
Growth (%)	***-22.1***	***71.1***	***46.0***	***25.7***	***12.2***
EBITDA Margin (%)	***6.0***	***8.2***	***9.6***	***10.8***	***10.9***
Depreciation	80	91	112	126	129
Other Income	19	19	19	18	23
EBIT	**27**	**80**	**129**	**170**	**207**
Interest expenses	39	42	54	64	63
PBT	**-16**	**32**	**74**	**106**	**144**
Tax	-2	14	23	28	37
PAT	**-14**	**18**	**51**	**77**	**106**
Share of Asso./Minority Int.	0	0	-2	0	0
Adj. PAT	**-10**	**21**	**50**	**77**	**106**
Growth (%)	***-145.7***	***-302.6***	***137.9***	***55.5***	***37.2***
EPS	-0.8	1.5	3.7	5.7	7.8

Balance Sheet

As at March (Rs cr)	FY21	FY22	FY23	FY24E	FY25E
SOURCE OF FUNDS					
Share Capital	14	14	14	14	14
Reserves	592	628	676	738	823
Shareholders' Funds	**606**	**642**	**689**	**752**	**836**
Minority Interest	3	0	2	2	2
Total Debt	448	581	729	624	519
Net Deferred Taxes	-3	-3	7	7	7
Other Non-curr. Liab.	13	25	19	26	30
Total Sources of Funds	**1066**	**1246**	**1447**	**1412**	**1396**
APPLICATION OF FUNDS					
Net Block & Goodwill	733	890	1005	971	917
CWIP	63	89	79	48	38
Investments	0	16	16	16	16
Other Non-Curr. Assets	102	68	69	110	122
Total Non Current Assets	**899**	**1063**	**1169**	**1145**	**1093**
Inventories	264	290	281	424	471
Debtors	352	364	395	501	565
Cash & Equivalents	21	27	36	64	9
Other Current Assets	96	78	54	67	82
Total Current Assets	**734**	**759**	**766**	**1056**	**1127**
Creditors	362	448	386	572	636
Other Current Liab & Provisions	205	129	102	217	189
Total Current Liabilities	**567**	**576**	**489**	**789**	**824**
Net Current Assets	167	182	278	267	302
Total Application of Funds	**1066**	**1246**	**1447**	**1412**	**1396**

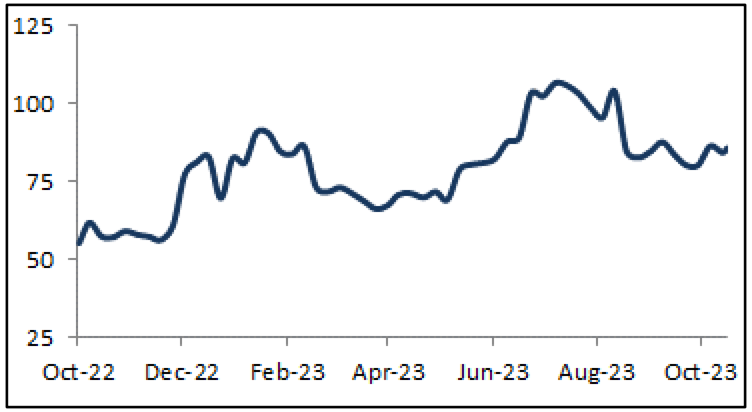
Cash Flow Statement

(Rs cr)	FY21	FY22	FY23	FY24E	FY25E
Reported PBT	-16	36	74	106	144
Non-operating & EO items	1	-3	0	-34	-8
Interest Expenses	30	44	54	64	63
Depreciation	80	91	112	126	129
Working Capital Change	-67	54	-68	39	-91
Tax Paid	-5	-6	-12	-28	-37
OPERATING CASH FLOW (a)	**23**	**216**	**160**	**273**	**199**
Capex	-118	-199	-200	-60	-65
Free Cash Flow	-95	17	-40	213	134
Investments	0	-2	0	0	0
Non-operating income	17	7	-33	0	0
INVESTING CASH FLOW (b)	**-100**	**-195**	**-233**	**-60**	**-65**
Debt Issuance / (Repaid)	124	31	146	-105	-105
Interest Expenses	-38	-45	-58	-64	-63
FCFE	8	8	15	44	-34
Share Capital Issuance	0	0	0	0	0
Dividend	-4	-3	-5	-15	-22
Others	0	-11	-6	0	0
FINANCING CASH FLOW (c)	**81**	**-16**	**83**	**-184**	**-190**
NET CASH FLOW (a+b+c)	**3**	**5**	**10**	**29**	**-56**

Key Ratios

	FY21	FY22	FY23	FY24E	FY25E
Profitability Ratios (%)					
EBITDA Margin	6.0	8.2	9.6	10.8	10.9
EBIT Margin	1.8	4.3	5.6	6.6	7.2
APAT Margin	-0.7	1.1	2.2	3.0	3.7
RoE	-1.7	3.4	7.5	10.7	13.4
RoCE	2.6	7.0	9.7	12.2	15.1
Solvency Ratio (x)					
Net Debt/EBITDA	4.8	3.7	3.1	2.0	1.6
Net D/E	0.7	0.9	1.0	0.7	0.6
PER SHARE DATA (Rs)					
EPS	-0.8	1.5	3.7	5.7	7.8
CEPS	5.2	8.2	11.9	15.0	17.3
BV	44.8	47.4	50.9	55.6	61.8
Dividend	0.2	0.4	0.8	1.1	1.6
Turnover Ratios (days)					
Inventory days	77	70	60	63	68
Debtor days	56	54	45	50	57
Creditors days	76	79	66	68	77
VALUATION (x)					
P/E	NA	56.1	23.6	15.2	11.1
P/BV	1.9	1.8	1.7	1.6	1.4
EV/EBITDA	18.1	11.4	8.4	6.2	5.4
EV/Revenues	1.1	0.9	0.8	0.7	0.6
Dividend Yield (%)	0.2	0.5	0.9	1.3	1.8
Dividend Payout (%)	-26.2	25.9	20.4	19.2	20.4

Price chart



HDFC Sec Retail Research Rating description

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This rating is given to stocks that represent large and established business having track record of decades and good reputation in the industry. They are industry leaders or have significant market share. They have multiple streams of cash flows and/or strong balance sheet to withstand downturn in economic cycle. These stocks offer moderate returns and at the same time are unlikely to suffer severe drawdown in their stock prices. These stocks can be kept as a part of long term portfolio holding, if so desired. This stocks offer low risk and lower reward and are suitable for beginners. They offer stability to the portfolio.

Yellow Rating stocks

This rating is given to stocks that have strong balance sheet and are from relatively stable industries which are likely to remain relevant for long time and unlikely to be affected much by economic or technological disruptions. These stocks have emerged stronger over time but are yet to reach the level of green rating stocks. They offer medium risk, medium return opportunities. Some of these have the potential to attain green rating over time.

Red Rating stocks

This rating is given to emerging companies which are riskier than their established peers. Their share price tends to be volatile though they offer high growth potential. They are susceptible to severe downturn in their industry or in overall economy. Management of these companies need to prove their mettle in handling cyclicality of their business. If they are successful in navigating challenges, the market rewards their shareholders with handsome gains; otherwise their stock prices can take a severe beating. Overall these stocks offer high risk high return opportunities.

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Disclosure:

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