Stock Update

Multiple growth levers

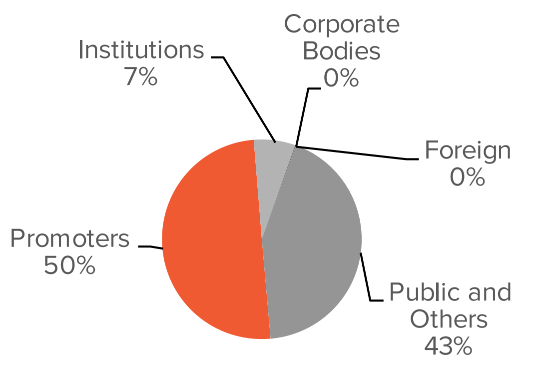
Rico Auto Industries

Reco: Buy | CMP: Rs92

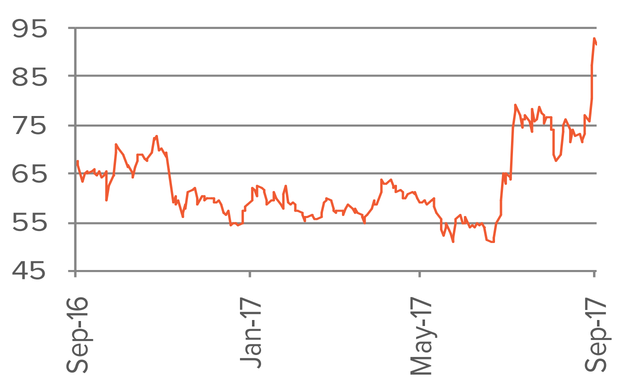
Company details

Price target:	Rs117
Market cap:	Rs1,240 Cr
52-week high/low:	97 / 44
NSE volume: (No of shares)	10.21 lakh
BSE code:	520008
NSE code:	RICOAUTO
Sharekhan code:	RICOAUTO
Free float: (No of shares)	6.75 Cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	21.3	69.6	60.7	40.1
Relative to Sensex	23.5	66.5	45.7	26.3

Key points

- **Improved demand from OEMs coupled with foray into new segments to augment revenue growth:** The demand outlook for the passenger segment (two-wheeler and passenger vehicles) has improved, as key concerns (shift to new emission norms, GST rollout and demonetisation) are behind us. The same is reflected in the strong 10% and 14% growth posted by the two-wheeler and passenger vehicle industry for April–August 2017. Further, early onset of the festive season, positive rural sentiments, successful GST rollout and a slew of new product launches planned by auto OEMs provide ample visibility on auto sales growth going ahead. Cumulatively, this bodes well for Rico Auto Industries (RAI), which derives about 85% of its revenue from the OEM space. Further, RAI has charted out an aggressive growth plan as it has forayed aftermarkets for the two-wheeler and four-wheeler segments (targets revenue of Rs.100 crore over 2-3 years), has increased focus on the defence business with the introduction of new products and planned to re-enter the clutch segment. Given the robust OEM outlook coupled with new growth avenues, we expect RAI's revenue to post a 14% CAGR over FY2017-FY2019.

- **Favourable product mix coupled with operating efficiencies to result in OPM expansion:** RAI's focus on high-margin areas, viz. defence and aftermarket is likely to improvise margins. Further, the company's ongoing exercise to curtail cost and improve operational efficiencies coupled with better pricing on incremental orders would drive margin expansion going ahead. RAI will also gain from operating leverage benefits given its robust topline growth. Based on the above triggers, we have factored in a 150BPS OPM expansion for RAI over FY2017-FY2019.

- **Outlook – Structural growth levers in place; Return ratios to leg-up leading to rerating:** Demand from auto OEMs is expected to remain buoyant over the near to medium term and would have a positive rub-off effect on RAI's revenue. Further, the upcoming regulations for the auto industry and new growth avenues provide ample topline visibility. Moreover, concentrated cost-control efforts and a likely favourable product mix are expected to lead to margin improvement. Consequently, RAI's earnings are expected to grow at a 37% CAGR over the next two years, making it amongst the fastest-growing ancillary companies. In addition, RAI's ROE is estimated to improve from 9.5% in FY2017 to 14.4% in FY2019, which is the key catalyst for rerating.

- **Valuation – Raise estimates; Maintain Buy with a revised PT of Rs.117:** We expect RAI's topline and earnings to report a 15% and 37% CAGR over FY2017-FY2019, respectively. We have raised our earnings estimates by 4% for FY2018 and FY2019, respectively, given the improved OEM outlook and foray into new segments, which would start reflecting in earnings over the next two years. We maintain our Buy recommendation on the stock with a revised price target (PT) of Rs.117 (based on 17x FY2019 earnings).

Valuation (consolidated) Rs cr

Particulars	FY2015	FY2016	FY2017	FY2018E	FY2019E
Net sales (Rs cr)	1,346.3	1,007.0	1,079.2	1,211.2	1,393.8
Growth (%)	-9.0	-25.2	7.2	12.2	15.1
EBITDA (Rs cr)	86.1	98.6	115.0	138.3	170.6
OPM (%)	6.4	9.8	10.7	11.4	12.2
Adjusted PAT (Rs cr)	(7.2)	34.0	49.5	67.2	92.7
Growth (%)	-379.7	-570.4	45.5	35.7	38.0
Adjusted EPS (Rs)	(0.5)	2.5	3.7	5.0	6.9
P/E (x)	n/a	36.6	25.1	18.5	13.4
P/B (x)	2.8	2.6	2.4	2.2	1.9
EV/EBITDA (x)	16.0	14.3	12.3	10.3	8.2
RoE (%)	(1.6)	7.2	9.5	11.8	14.4
RoCE (%)	29.2	9.0	10.7	13.0	15.8

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