Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Ramkrishna Forgings Ltd

Robust demand growth; Attractive valuations

Auto Ancillary	Sharekhan code: RKFORGE		
Reco/View: Buy ↔	CMP: Rs. 173	Price Target: Rs. 238 ↔	

↑ Upgrade ↔ Maintain ↓ Downgrade

3R MATRIX	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)	✓		

+ Positive = Neutral – Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↔	

Company details

Market cap:	Rs. 2,127 cr
52-week high/low:	Rs. 252/146
NSE volume: (No of shares)	3.13 lakh
BSE code:	532527
NSE code:	RKFORGE
Free float: (No of shares)	8.6 cr

Shareholding (%)

Promoters	46.2
FII	13.6
DII	4.9
Others	35.3

Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	14.1	-10.2	-12.1	15.6
Relative to Sensex	8.1	-6.4	-3.2	10.9

Sharekhan Research, Bloomberg

Summary

- We maintain a Buy on Ramkrishna Forgings Limited (RKFL) with an unchanged PT of Rs.238, led by strong revenue growth, improving margin profile and attractive valuations.
- Q1FY23 results were robust with revenue, EBITDA and PAT growing by 57.6% y-o-y, 50.8% y-o-y and 92% y-o-y respectively.
- Over FY22-24E, earnings are likely to clock a strong 29.3% CAGR, driven by a 14.7% CAGR in domestic revenue, a 27% CAGR in export revenue and a 15.9% growth in EBITDA.
- Stock trades at attractive valuations of 8x P/E multiple and 4.7x EV/EBITDA multiple on FY24E estimates respectively.

Ramkrishna Forgings Limited (RKFL) continues to grow strongly in Q1FY23, led by the execution of robust order book, new order wins and an increasing share of value-added products. During the quarter, revenue, operating profit and PAT grew by 57.6% y-o-y, 50.8% y-o-y and 92% y-o-y respectively. The company is witnessing demand across geographies, product portfolio and clients, driven by strengthening business with existing clients, acquisition of new clients and increasing share of high-margin business segments. The management maintained its revenue guidance of 20-25% in FY23E and expects EBITDA margins to sustain at current levels. The company's capex is expected to remain light in coming years, while major capex would be utilized in expanding machining capability. The new and value-added segments, such as LCV division, electric vehicle (EV) business vertical, passenger vehicle segments and oil & gas division are witnessing strong traction and would likely to improve content per vehicle of the company. The company reduced its debt by Rs 30 crore during Q1FY23 at Rs 1,300 crore and reiterated to be a net debt-free company by FY25E. We retain our Buy rating on the stock with an unchanged PT of Rs238.

Key positives

- Revenue, operating profit and PAT grew by a robust 57.6% y-o-y, 50.8% y-o-y and 92% y-o-y respectively, led by execution of order book, increase in the share of value-added products and positive operating leverage.
- RKFL received contracts of Rs388 crore from four contracts during Q1FY23 from various geographies and business verticals.
- RKFL's EBITDA margin profile has improvement significantly over the last few years, sustaining well over 20%, driven by focusing on increasing contribution from machining and assemblies' divisions.

Key negatives

- Domestic and export volumes declined 3.4% q-o-q and 7.6% q-o-q in Q1FY23, due to seasonality and supply constraints in CV exports markets.

Management Commentary

- The management maintained its revenue guidance of 20-25% in FY23E and expects EBITDA margins to sustain at current levels, driven by strong demand across geographies and business verticals.
- Management continues to remain positive on new order inflows and expects to maintain the growth momentum.
- The management is positive on its foray into new segments such as oil & gas, electric vehicles and railways to drive growth going forward.
- The company expects to sustain its EBITDA margin at the current levels of 22%, led by an increase in the share of value-added products and moving towards machining and assembling, which are high-margin businesses.

Revision in estimates – We maintain our estimates for FY23E and FY24E. Over FY22-24E, earnings are likely to clock a strong 29.3% CAGR, driven by a 14.7% CAGR in domestic revenue, a 27% CAGR in export revenue and a 15.9% growth in EBITDA.

Our Call

Valuation - Maintain Buy with an unchanged PT of Rs238: We are expecting the CV demand to remain buoyant, led by the recovery in the economy. The outlook of North America and Europe remains positive, as the CY22E is expected to do well as compared to CY21, led by increased demand and the easing of the chips shortage situation going forward. The positive CV demand in India, North America and Europe is highly beneficial for the company such as RKFL, which has a strong domestic and export revenue mix of 55:45 in niche markets. The Indian government is offering various incentives such as PLI scheme, make-in-India and Atmanirbhar Bharat Mission, which will provide a strong platform for automobile suppliers such as RKFL. We believe that RKFL has a strong global footprint and is serving leading OEMs, not only in the automotive segment but in other sectors as well. We expect RKFL to gain market share internationally, as it has completed its major capex program. The stock is available at attractive valuation multiples of P/E of 8x and EV/EBITDA of 4.7x on its FY2024E estimates. We reiterate a Buy rating on the stock with an unchanged PT of Rs238.

Key Risks

RKFL is exposed to the cyclicality inherent in the CV and steel industries. Also, geographically diversified businesses pose forex fluctuation risks. RKFL is well hedged to cover forex movement in any direction from -5% to +5%. If the chips shortage situation further aggravates, this may impact our estimates adversely.

Valuation (Standalone) Rs cr

Particulars	FY21	FY22	FY23E	FY24E
Revenues	1,288	2,281	2,775	3,291
Growth (%)	15.9	77.1	21.7	18.6
EBIDTA	230	526	570	706
OPM (%)	17.8	23.0	20.5	21.5
Net Profit	28	207	246	345
Growth (%)	190.3	638.7	19.0	40.5
EPS	1.8	12.9	15.4	21.6
P/E	98.8	13.4	11.2	8.0
P/BV	3.1	2.6	2.1	1.7
EV/EBIDTA	14.4	6.3	5.8	4.7
ROE (%)	3.2	21.0	20.8	23.9
ROCE (%)	4.7	13.2	13.1	16.0

Source: Company; Sharekhan estimates

Key Highlights of the Q1FY23 conference call

Growth momentum continues in Q1FY23: Ramkrishna Forgings Limited (RKFL) continues to grow strongly in Q1FY23, led by the execution of robust order book, new order wins and increasing share of value-added products. During the quarter, revenue, operating profit and PAT grew by 57.6% y-o-y, 50.8% y-o-y and 92% y-o-y respectively. Revenue grew 57.6% y-o-y to Rs650.7 crore, due to continued recovery in domestic as well as export markets. On a q-o-q basis, the revenues were down 4.8%, led by seasonality impact in domestic markets and supply constraints in export markets. Domestic and export revenues were down 4.4% q-o-q and 5.5% y-o-y, despite the improvement in average sales realization in both markets. EBITDA margin remained flat on q-o-q at 22.1% in Q1FY23, while contracted 100 bps y-o-y. The EBITDA margin was down by 40bps from our expectations owing to higher other operating costs and employee expenses. The gross margin witnessed an improvement of 330 bps q-o-q to 55% in Q1FY23, led by an improved product mix, toward high margin businesses. RKFL's EBITDA margin profile has improved significantly over the last few years, sustaining well over 20%, driven by focusing on increasing contribution from machining and assemblies divisions.

Domestic business: The domestic revenue for Q1FY23 stood at Rs399 crore, reporting an increase of 110% y-o-y growth, led by a 77.4% growth in volumes and a 14.6% growth in average realisations. On q-o-q, the domestic revenue declined 4.4%, led by a 3.4% volume decline, partially offset by a 3.3% increase in average sales realisation. The domestic demand scenario is expected to remain strong going forward. The company is witnessing demand across its product portfolio and clients. The growth is driven by strengthening business with existing clients, acquisition of new clients and a foray into new segments. At present, the company is receiving robust orders.

Export business: The export markets remain buoyant. The export revenue grew by 13.4% y-o-y at Rs247 crore, 12.4% improvement in average sales realisation, partially offset by a 4.4% decline in volumes.

North American market: The existing business is performing strongly in the North America markets. The business is robust with light commercial vehicle (LCV) clients. The oil and gas business are picking up well and is expected to double its revenue to ~Rs 100 crore in FY23E. The company is also focusing to develop its piston businesses.

New order wins: RKFL received contracts of Rs388 crore from four contracts during Q1FY23 from various geographies and business verticals. These orders will start to contribute in revenues from FY24 onwards, executable over 3-4 years. The new wins are entirely export businesses.

Positive guidance: The management maintained its revenue guidance of 20-25% in FY23E and expects EBITDA margins to sustain at current levels, driven by strong demand across geographies and business verticals. Management continues to remain positive on new order inflows and expects to maintain the growth momentum. The management is positive about its foray into new segments such as oil & gas, electric vehicles and railways to drive growth going forward. The company expects to sustain its EBITDA margin at the current levels of 22%, led by an increase in the share of value-added products and moving towards machining and assembling, which are high-margin businesses

Easing chips supply constraints: RKFL continues to see robust export orders, despite chips shortage globally. The company's clients have continued to maintain their production schedule. Also, the company has exposure to M&HCVs, where chips/semi-conductor usage is low as compared to passenger vehicles. The company has forayed into passenger vehicle segments, which is likely to contribute from next year. Besides all these, the company expects a recovery in volumes led by easing chip supply constraints.

Capex update: The company's capex is expected to remain light in coming years, while major capex would be utilized in expanding machining capability. The management indicated capex of ~Rs70-80 crores in FY23E.

Railways division: RKFL is expected to show substantial growth from the railway's division in FY23E, led by government tenders in the medium term. The quarterly run rate is expected to improve on a sequential basis over the next few quarters.

Focus on product development and new markets: The key focus areas of the company are new product development and higher geographical penetration. RKFL expects export contribution to 55-60% over the next 3-4 years from 45% in FY21. The company is growing to grow inorganically by acquiring companies which have aligned product portfolio to its current portfolio.

Other key highlights

- The company has deferred its fundraising plans and plans to reduce its debt by internal accruals in the near-term. The company reduced its debt by Rs 30 crore during Q1FY23 at Rs 1,300 crore and reiterated to be net debt-free company by FY25E. The financing costs are expected to remain at Rs100-105 crore in FY23E, as the increase in interest rate is expected to be mitigated by a reduction in debts.
- The overall capacity utilisation improved to 78% in Q1FY23 on enhanced capacity as compared to 75.7% in Q1FY22, reflecting a continuous increase in demand.
- Improving product mix towards high-margin business verticals is expected to keep gross margins at elevated levels over the next few quarters.
- EV is gaining traction for the company in all its key markets. In North America, the company has five running programs and 3 in order books, while in Asian markets, the company is running six programs with 3 programs in the order book. In Europe, the company has one program in the order book.
- The board has recommended an interim dividend of 25% or Rs0.50 per share.

Results (Standalone) **Rs cr**

Particulars	Q1FY23	Q1FY22	YoY%	Q4FY22	QoQ%
Revenues	650.7	412.9	57.6	683.2	(4.8)
Total operating expenses	507.1	317.5	59.7	532.2	(4.7)
EBITDA	143.7	95.3	50.8	151.0	(4.9)
Depreciation	47.1	38.8	21.2	45.6	3.2
Interest	25.7	20.3	26.8	26.2	(2.0)
Other income	0.7	0.8	(17.2)	-	NA
PBT	71.6	37.0	93.4	79.2	(9.6)
Tax	24.3	12.4	96.1	(7.5)	NA
Reported PAT	47.3	24.6	92.0	86.7	(45.5)
Adjusted PAT	47.3	24.6	92.0	86.7	(45.5)
Adjusted EPS	3.0	1.5	91.8	5.4	(45.5)

Source: Company, Sharekhan Research

Key ratios (Standalone)

Particulars	Q1FY23	Q1FY22	YoY (bps)	Q4FY22	QoQ (bps)
Gross margin (%)	55.0	60.7	(580)	51.6	330
EBIDTA margin (%)	22.1	23.1	(100)	22.1	-
EBIT margin (%)	14.8	13.7	120	15.4	(60)
Net profit margin (%)	7.3	6.0	130	12.7	(540)
Effective tax rate (%)	34.0	33.5	50	(9.4)	NA

Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector view - Strong underline demand for CV in India, Europe and North America

We see strong underlying demand for commercial vehicles domestically. We expect a strong improvement in M&HCV sales to continue, driven by a rise in e-commerce, agriculture, infrastructure, and mining activities post normalization of COVID. Global demand for trucks is buoyant, though the order book in the few months got impacted, led by chips shortage issue. While the demand remains stronger for both medium- and heavy-duty vehicles, the industry's ability to tackle that backlog has been affected by a series of issues such as chip shortages, steel output and plastic resin availability. Most of the global OEMs and auto components suppliers maintain a positive outlook for the commercial vehicle industry. CY22 is expected to remain strong as compared to CY21, as the easing of the chips shortage situation will help to regain volumes in the CV industry.

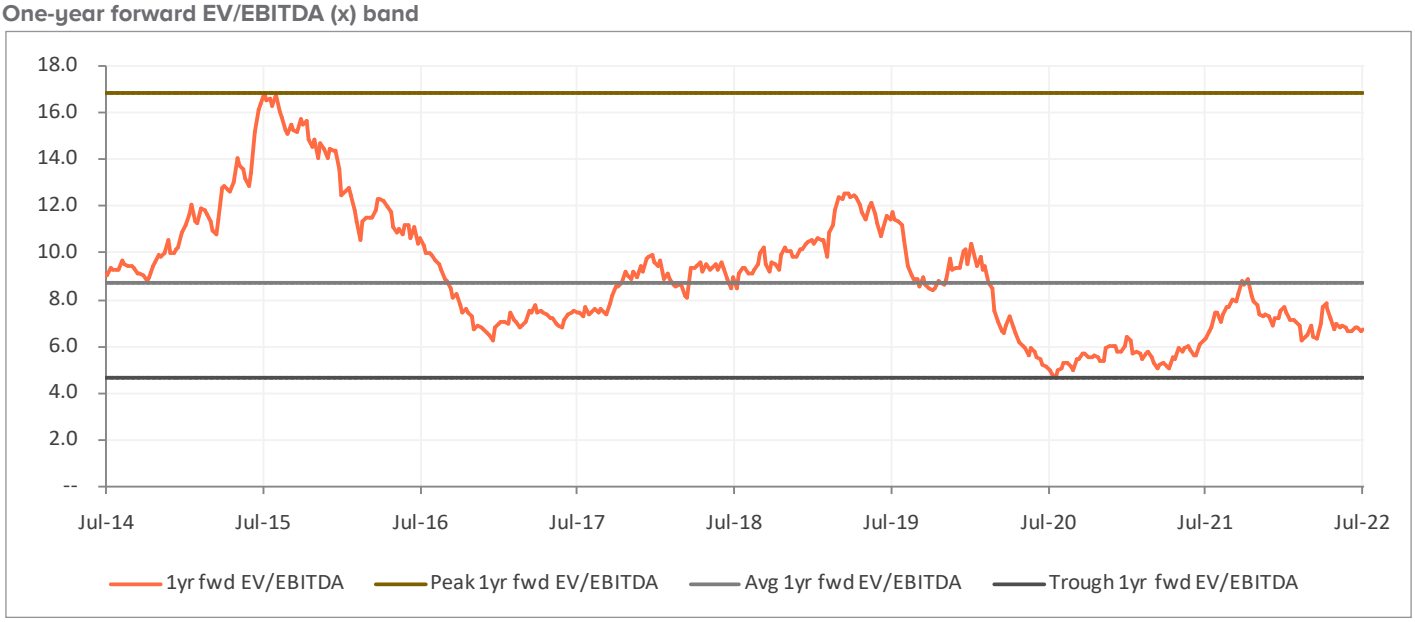
■ Company outlook - Beneficiary of strong demand and margin improvement

We expect RKFL to benefit from the CV upcycle across geographies – India, North America and Europe, led by improved prospects for commercial vehicles globally. Global OEMs and tier-1 suppliers maintain a positive outlook for the commercial vehicle segment. RKFL is committed to growing its business profitably and de-risk its business model through diversifying into new geographies, and sectors and widening its product portfolio. Counterparty risks are low due to the established business position of RKFL's customers from the domestic and export markets, and the criticality of the components manufactured. We expect RKFL to be a beneficiary of improving demand. The company's focus on increasing the share of value-added and critical components will help improve realisations and EBITDA margins.

■ Valuation - Maintain Buy with an unchanged PT of Rs.238

We are expecting the CV demand to remain buoyant, led by the recovery in the economy. The outlook of North America and Europe remains positive, as the CY22E is expected to do well as compared to CY21, led by increased demand and the easing of chips shortage situation going forward. The positive CV demand in India, North America and Europe are highly beneficial for the company such as RKFL, which has a strong domestic and export revenue mix of 55:45 in niche markets. The Indian government is offering various incentives such as the PLI scheme, make-in-India and Atmanirbhar Bharat Mission, which will provide a strong platform for automobile suppliers such as RKFL. We believe that RKFL has a strong global footprint and is serving to lead OEMs, not only in the automotive segment but in other sectors as well. We expect RKFL to gain market share internationally, as it has completed its major Capex program. The stock is available at attractive valuation multiples of P/E of 8x and EV/EBITDA of 4.7x on its FY2024E estimates. We reiterate a Buy rating on the stock with an unchanged PT of Rs238.

One-year forward EV/EBITDA (x) band



Source: Sharekhan Research

Peer Comparison

Companies	CMP (Rs/ Share)	P/E (x)			EV/EBITDA (x)			ROCE (%)		
		FY22	FY23E	FY24E	FY22	FY23E	FY24E	FY22	FY23E	FY24E
Ramkrishna Forgings Ltd	173	13.4	11.2	8.0	6.3	5.8	4.7	13.2	13.1	16.0
Bharat Forge Ltd	689	29.7	28.4	20.9	18.4	16.2	12.9	9.0	8.8	11.5
GNA Axles	612	14.8	11.4	9.4	8.1	6.5	5.3	17.4	19.9	20.7

Source: Company; Sharekhan Research

About company

Ramkrishna Forgings Limited (RKFL), headquartered in Kolkata, is one of the leading forging companies in India catering requirements of OEMs and tier-1 auto-component suppliers worldwide. RKFL, incorporated in 1981, commenced operation in 1984 primarily as a forging manufacturer for the Indian Railways. Started manufacturing from two facilities located in and around Jamshedpur and another small unit near Kolkata, the company has now scaled up its capacity to ~1,87,100 MTPA. The company has five facilities, of which four are located in Jamshedpur and one in Liluah. RKFL's existing forging facility comprises a hammer forge and up-setter forge with a total capacity of 46,000 MTPA and a ring-rolling unit with a capacity of 24,000 MTPA. In addition the company has four press lines having a cumulative capacity of ~80,000 MTPA. The company has a marquee global customer base of 17 OEMs including Tata Motors, Ashok Leyland, VE Commercials and Tier I companies.

Investment theme

RKFL is a proxy play for CV upcycle in India and internationally. We are expecting the CV upcycle in India to coincide with that in North America and Europe. This point of conjunction would be highly beneficial for a company such as RKFL, which has a strong domestic and export revenue mix of 55:45, operating in niche markets. Also, the timing becomes impeccable, as global automakers and tier-1 suppliers are scouting for alternative sourcing hubs outside China. The Indian government is offering various incentives such as the PLI scheme, make-in-India and Atmanirbhar Bharat mission, which will provide a strong platform for automobile suppliers such as RKFL. We believe RKFL has a strong credential global footprint and is servinleadng OEMs, not only in the automotive segment but also in other sectors. We expect RKFL to gain market share internationally, as it has completed its major capex.

Key Risks

- RKFL is exposed to the cyclicality inherent in CV and steel industries. Also, geographically diversified businesses pose forex fluctuation risks. RKFL is well hedged to cover forex movement in any direction from -5% to +5% .
- RKFL's export sales are highly working capital intensive because of the large receivable cycle, particularly for the export sales.
- If the chips shortage situation further aggravates, this may impact our estimates adversely.

Additional Data

Key management personnel

Ms. Anjali Singh	Executive Chairperson
Mr. Manoj Kolhatkar	Managing Director
Mr. Jagdish Kumar	Group President & Group CFO
Mr. Rishi Luharuka	Chief Financial Officer

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Riddhi Portfolio	23.7
2	Eastern Credit Capital	13.5
3	Aditya Birla Sun Life	4.9
4	Ramkrishna Rail And Infrastructure Private Limited	4.1
5	Massachusetts Institute Of Technology	3.8
6	Lata Bhanshali	3.3
7	Pacific Horizon Investment	3.0
8	Akash Bhanshali	2.5
9	Blue Daimond Properties Pvt Ltd	2.4
10	ICG Q Limited	2.0

Source: Bloomberg

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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