

## Company Flash

1 November 2007 | 7 pages

# Amtek Auto (AMTK.BO)

 Results 

## Buy: 2QFY08 Weak Quarter, Input Cost Pressures Impact Margins

- Consolidated PAT +1.6% Y/Y** — Recurring PAT (excluding derivative gains) rose 1.6% y/y (significantly below our estimates) as strong growth in top line (+26% Y/Y) was offset by increase in input and capital costs. The results also reflect impact of consolidation of Benda, Siccardi and JLFrench subsidiaries. Consolidated margins at 17.6% (-40 bps y/y) were impacted by margin pressure in domestic operations
- Standalone PAT declines 9% Y/Y** — Standalone PAT at Rs453 million (excluding derivative gains) declined 9% Y/Y due to 360 bps y/y reduction in margins, lower other income and increase in capital costs. Margins declined due to increase in steel costs and shift in mix (share of higher margin machined components formed about 57% of total sales in this quarter vs. 62% in 1QFY07). Capital costs have increased due to increase in forging capacity and increase in debt levels.
- Subsidiary imputed performance** — Margins improved by 40 bps y/y while declining marginally by 10 bps QoQ due to benefits accruing from the consolidation of Benda Amtek and Amtek Siccardi, which are higher-margin businesses. Revenues rose by 24% Y/Y and 2% QoQ.
- Outlook** — Management reiterated that there are 2-3 acquisitions in the pipeline and seemed confident of acquiring companies at valuations of <4.5x EV/EBITDA multiples. Maintain Buy (1M). Key risks are margin pressures, F/X pressures.

<b>Buy/Medium Risk</b>	<b>1M</b>
Price (31 Oct 07)	Rs505.85
Target price	Rs521.00
Expected share price return	3.0%
Expected dividend yield	0.7%
<b>Expected total return</b>	<b>3.7%</b>
Market Cap	Rs66,859M
	US\$1,699M

### Price Performance (RIC: AMTK.BO, BB: AMTK IN)



### Statistical Abstract

Year to	Net Profit	Diluted EPS	EPS growth	P/E	P/B	ROE	Yield
30 Jun	(RsM)	(Rs)	(%)	(x)	(x)	(%)	(%)
2005A	1,475	11.15	22.8	45.4	6.0	24.7	0.3
2006A	2,564	15.82	41.9	32.0	3.8	20.6	0.4
2007E	3,623	22.36	41.3	22.6	3.1	18.6	0.5
2008E	4,708	29.05	29.9	17.4	2.6	19.1	0.7
2009E	5,633	34.76	19.6	14.6	2.2	19.3	0.9

Source: Powered by dataCentral

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Figure 1. Amtek Auto – 2QFY08 Consolidated Results

	1QFY07	1QFY08	YoY	Comments
Net sales/Income from others	9,028	11,366	25.9%	Benefits from Organic growth and consolidation of Benda Amtek Siccardi and JLFrench subsidiaries
Total Expenditure	7,275	9,103	25.1%	
EBITDA	1,753	2,263	29.1%	Includes other income, excluding other income we estimate margins declined by 40 bps y/y
Interest	171	228	33.5%	
Gross Profit	1,582	2,035	28.7%	
Depreciation	330	460	39.5%	Escalating capital costs reflected by increase in gross block
PBT	1,252	1,575	25.8%	
Tax	293	412	40.6%	
Net profit after tax	959	1,163	21.3%	
Minority Interest	87	102	17.1%	
PAT After Minority Interest	872	1,061	21.7%	
Extraordinaries net of tax	13	250		Derivative income of Rs 250 million vs. 12.5 million in 1QFY07
<b>Reported Pat after Minority Interest</b>	<b>863</b>	<b>876</b>	<b>1.6%</b>	<b>20% below are estimates</b>
EBITDA Margin	19.4%	19.9%		Includes other income
PBT Margin	13.9%	13.9%		
PAT Margin	10.6%	10.2%		
Tax Rate	23.4%	26.2%		

Source: Company, Citi Investment Research

Figure 2. Amtek Auto- 2QFY08 - Parent Results

	1QFY07	1QFY08	YoY	Comments
Net sales/Income from others	2,363	3,117	31.9%	6% below estimates, 49% y/y growth in exports vs. 25% y/y growth in domestic
Raw Material Costs	1,383	1,908	38.0%	
Staff Cost	115	145	26.0%	
Other Expenditure	138	216	56.6%	Expenses gone up due to consolidation of Benda Amtek, Siccardi and JL French
Total Expenses	1,636	2,269	38.7%	
EBITDA	727	848	16.6%	Margins impacted due to input cost pressures and unfavorable mix
Other Income	151	319	111.1%	Includes derivative trading income gain of Rs 250 million
Interest	48	77	59.8%	
Depreciation	133	226	70.6%	Due to expansion in forging capacity
PBT	697	863	23.8%	
Tax	189	225	19.4%	
Net Profit after Tax	509	638	25.4%	
Exceptional Items	13	250		Derivative income of Rs 250 million vs. 12.5 million in 1QFY07
<b>Pre exceptional PAT</b>	<b>499</b>	<b>453</b>	<b>-9.3%</b>	<b>13% below are estimates, Adjusted for derivative trading gains</b>
<b>Margin Ratios (%)</b>				
EBITDA	30.8	27.2		Margins declined 360 bps y/y, 40 bps lower than our forecast
EBIT w/out Other Income	25.2	19.9		
PBT	29.5	27.7		
PAT Margin	21.5	20.5		
Tax Rate	27.1	26.1		
<b>Costing Ratios (%)</b>				
Raw Materials	58.5	61.2		270 bps y/y increase, 50 bps above our estimates
Staff	4.9	4.7		In line with estimates
Other Expenses	5.8	6.9		In line with estimates

Source: Company, Citi Investment Research

Figure 3. Ahmednagar Forgings- 2QFY08

	1QFY07	1QFY08	YoY	Comments
Net sales/Income from others	1,220	1592	30%	
Raw Material Costs	815	1109	36%	
Staff Cost	37	59	60%	
Other Expenditure	133	100	-24%	
Total Expenses	984	1268	29%	
EBITDA	236	324	37%	Margins improved 100 bps y/y, declined 60 bps QoQ
Interest	26	33	24%	
Depreciation	12	43	249%	
PBT	197	248	26%	
Tax	62	77	24%	
<b>Net Profit after Tax</b>	<b>135</b>	<b>171</b>	<b>27%</b>	
<b>Margin Ratios (%)</b>				
EBITDA	19.3	20.3		
PBT	16.2	15.6		
PAT Margin	11.1	10.7		
Tax Rate	31.5	31.1		
<b>Costing Ratios (%)</b>				
Raw Materials	66.8	69.7		287 bps up y/y, 140 bps up QoQ
Staff	3.0	3.7		
Other Expenses	10.9	6.3		

Source: Company, Citi Investment Research

## Amtek Auto

### Company description

Amtek Auto began operations in 1987 and is the flagship of the Amtek Group. Amtek Auto is India's second-largest forging player with annual capacity of 85,000MT forgings (at end-FY06) and 25m machined auto components. Its products include forgings, castings, machined parts and sub-assemblies for engines, transmission systems and suspension components. It is the world's largest manufacturer of ring gears through subsidiary Smith Jones. The company has a large customer base that straddles most segments of the auto industry. Over the past few years, Amtek Auto has undertaken several acquisitions, which have given it a large global footprint. The company has plants in India, the US, the UK and Germany. It has seven subsidiaries, of which two are in the US and one each in the UK and Germany.

### Investment strategy

We rate Amtek Auto shares Buy / Medium Risk (1M). We forecast 25% earnings CAGR over the next two years, mirroring revenue growth. Despite factoring in margin compression (on account of changing product mix and input cost pressures), we expect earnings will keep pace with revenues, as capital costs (notably interest) decline. We also forecast a decline in the effective tax rate, in line with management's guidance. India's advantages in auto parts are well documented: highly skilled engineers and relatively lower wages. Amtek Auto looks well-positioned to benefit from the trend of increased outsourcing of auto parts to low-cost countries. For Amtek Auto, we forecast exports will account for around 40% of FY07E standalone sales (a CAGR of 86% over FY04-07E). Its scale, cost advantages and technical capabilities

imply a structural growth opportunity. Our concerns on Amtek's inorganically driven strategy, with its attendant risks of integration and execution continue.

## **Valuation**

Our target price of Rs521 is based on 15x FY09E fully diluted EPS estimates. We think the current multiple is well supported by earnings CAGR of 25% over FY07E-09E. We use P/E to value Amtek Auto because it is the most common measure to value auto parts companies. Over the past year, the stock has traded at an average 14.2x one-year forward EPS, at a discount to its competitor Bharat Forge, which has traded at an average of c19x. We don't expect Amtek Auto to re-rate further over the near term, though we would not sharp movements in the stock price, based on news flow concerning inorganic initiatives.

## **Risks**

We rate Amtek Auto shares Medium Risk, which differs from the Low Risk rating accorded by our quantitative risk-rating system that tracks 260-day share price volatility. Our risk rating reflects the attendant risks with Amtek Auto's acquisition strategy. Moreover, its overall complex corporate structure obscures earnings drivers. Downside risks to our target price include: 1) deterioration in economic variables such as GDP, interest rates and fuel prices; 2) integration risks; 3) complex group structure; 4) customer concentration; and 5) product liability claims 6) currency risk. Upside risks to our target price include: 1) favorable acquisitions; 2) faster than expected turnaround of acquired companies; and 3) a steady decline in input costs.

# Appendix A-1

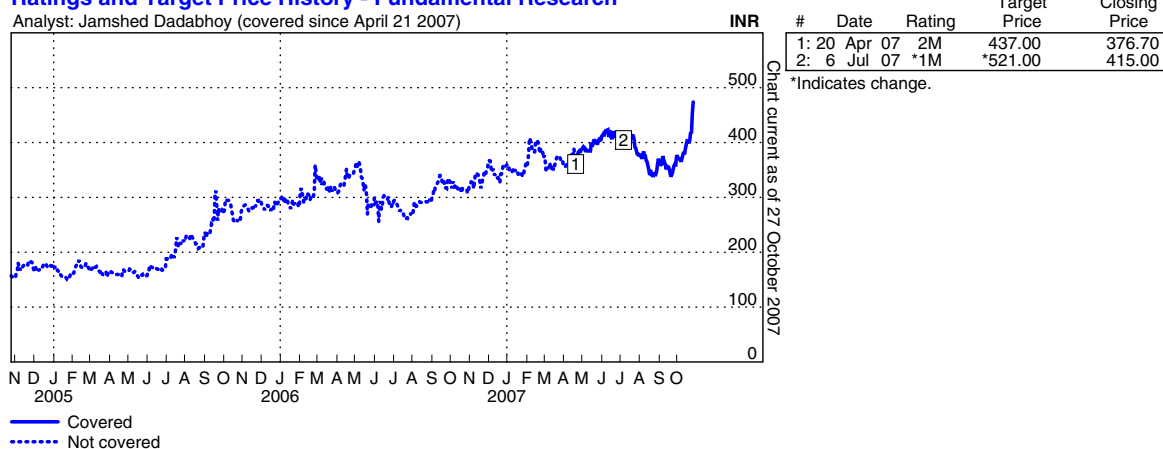
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Analyst: Jamshed Dadabhoy (covered since April 21 2007)



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