CD EquisearchPvt Ltd

CHANGING DIMENSIONS
CD EQUISEARCH

October 28, 2021

MM Forgings Ltd. (MMFL)	
No. of shares (m)	24.14
Mkt cap (Rscrs/$m)	2108/281.0
Current price (Rs/$)	873/11.6
Price target (Rs/$)	936/12.5
52 W H/L (Rs.)	955/302
Book Value (Rs/$)	217/2.9
Beta	0.6
Daily NSE volume (avg. monthly)	23390
P/BV (FY22e/23e)	3.6/3.1
EV/EBITDA (FY22e/23e)	12.6/11.0
P/E (FY22e/23e)	23.1/18.7
EPS growth (FY21/22e/23e)	0.8/95.6/23.9
OPM (FY21/22e/23e)	16.7/17.3/17.5
ROE (FY21/22e/23e)	9.6/16.9/17.9
ROCE(FY21/22e/23e)	6.8/10.4/11.4
D/E ratio (FY21/22e/23e)	1.2/1.0/0.9
BSE Code	522241
NSE Code	MMFL
Bloomberg	MMFG IN
Reuters	MMFO.NS

Shareholding Pattern%	
Promoters	56.3
MFs / Banks /FIs	21.1
Foreign Portfolio Investors	0.5
Govt. Holding	-
Public& Others	22
Total	**100.0**

As on September 30, 2021

Recommendation

HOLD

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Company Overview

MM Forgings is a manufacturer of automotive components. It manufactures steel forgings in raw, semi-machined and fully machined stages in various grades of carbon, alloy, micro-alloy and stainless steels.

Quarterly Highlights

- Favorable monetary policies and government support packages for stressed sectors have immensely supported revival in demand. With the easing of the lockdown restrictions, automakers have carefully resumed operations in a phased manner. On a low-base of the last fiscal year, total domestic sales in PV and CV were 6.46 lakh and 1.06 lakh units, respectively in Q1FY22 as against 1.54 lakhs and 0.32 lakhs in Q1FY21.
- On the back of a lower base, MM Forgings reported a massive top-line growth of 213.3% y-o-y in Q1FY22, largely assisted by the resilience observed in global CV market. With this increased sales velocity, operating profits jumped by a dazzling 521.2% to Rs43.42crs compared to a mere Rs 6.99crs in the same quarter a year ago, thus bolstering OPMs by a pleasing 899 bps to 18.1%. On the contrary, MMFL's net sales in Q1 fell by 16.1% from an all-time high Rs 285.80 crs in Q4. The company lost some grounds in the month of May when the second wave of the pandemic struck and governments were forced to enforce localized lockdown, thereby hurting its volume off-take.
- A favorable environment could uplift overall revenues by 42.8% this fiscal to Rs 1036 cr and by some 14.8% next fiscal to Rs 1189 cr. EPS is expected improve by a massive 95.6% this fiscal and by 23.9% the next one. This impressive earning growth coupled with rising asset-turnover ratio could push ROE to almost 17%, though it will below its peak FY19 levels.
- The stock currently trades at 23.1x FY22e EPS of Rs 37.77 and 18.7x FY23e EPS of Rs 46.78. Earning recovery in FY22 rests on the assumption of barely weakish growth in domestic CV industry - which has faced some sort of demand inertia in last few years - and rebound in exports. Since a handful of clients contribute to the majority of top-line, incremental growth seems likely to come from existing clients. MMFL's growing entrenchment in overseas markets with new product developments and efficient supply chain could help get round the cyclicality in OEM sector. Yet, any abrupt raw material price inflation, especially in steel, and delay in passing the high freight costs could weaken sentiments. On balance, we recommend 'HOLD' rating on the stock with target price of Rs 936 based on 20x FY23e EPS of Rs 46.78 over a period of 9-12 months.

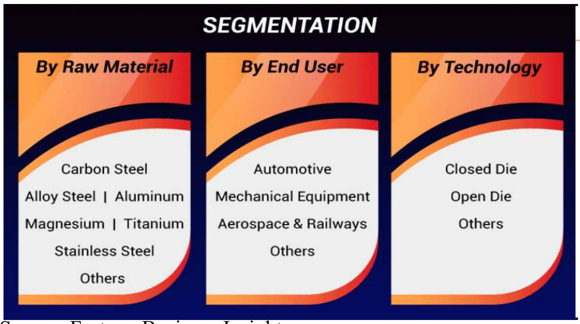
Standalone figures in Rs crs	FY19	FY20	FY21	FY22e	FY23e
Income from operations	903.92	727.29	725.65	1036.00	1189.00
Other Income	15.87	18.51	21.59	22.80	22.98
EBITDA (other income included)	189.12	143.70	142.89	201.64	231.05
PAT after EO	81.33	46.23	46.61	91.17	112.93
EPS(Rs)	33.69	19.15	19.31	37.77	46.78
EPS growth (%)	18.9	-43.2	0.8	95.6	23.9

Outlook & Recommendation

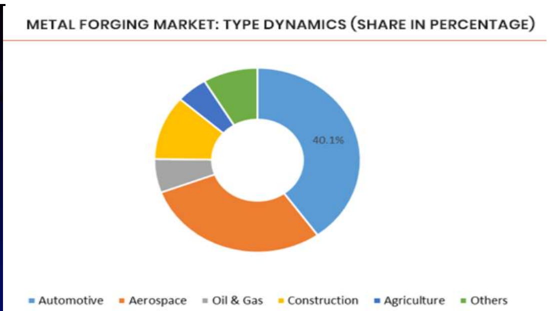
Global Forging Industry

With the emergence of coronavirus in November 2019, the industrial production across the globe was severely impacted, as a result the global metal forging industry witnessed almost a stunted growth and was valued at $87.42 billion in 2020 according to a report published by Market Research Future. The automotive sector, a major consumer of metal forging, was one of the most affected sectors because of this pandemic. Due to the temporary suspension of their operations, the entire value chain took a hit ranging from raw material suppliers to auto-component manufacturers. Now with the deteriorating conditions of the semiconductor shortage, many global OEMs have started cutting-back their production. Though, any major impact of this chip crisis on the metal forging market is yet to be seen.

However, since the second half of 2020, there has been a steady recovery with the economic activities picking-up pace and a sharp rebound in all end markets. The demand for Class 8 trucks in the US has been surging despite supply chain disruptions and shortage of raw materials and components, largely supported by government stimulus and recovering economy. The European commercial vehicle market is also witnessing positive growth in new CV registrations. Improving consumer goods spending continues to drive demand for new trucks with the easing of the pandemic. Freight growth also remains vibrant as fleet operators are rushing to add capacity to keep pace with the growing demand. Further, electric vehicles are likely to take center-stage in 2021. Global EV sales are expected to rise sharply, particularly in Europe, supported by numerous government incentives, increasingly stringent emission regulations, and newer launches. This growth in production of electric vehicles is anticipated to buoy demand for metal forging over the coming years.

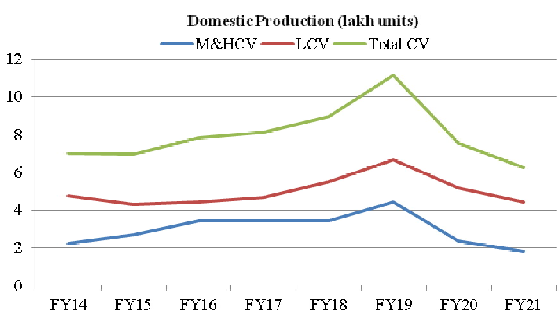


Source: Fortune Business Insights

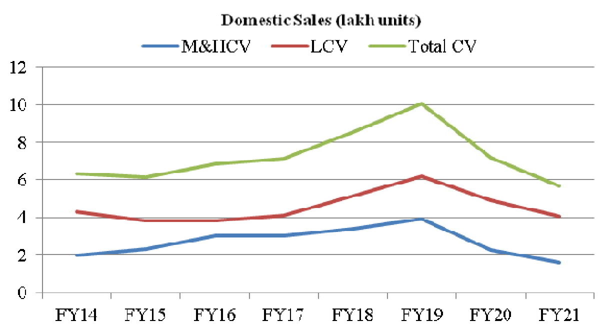


Source: www.reportsanddata.com

The durability, strength and reliability of the forged components have made them a preferred choice in sectors where stress, load, tension and human safety are key considerations. Market Research Future pegs the metal forging market to be worth $130.51 billion by 2028, registering a CAGR of 6.34% during 2021-28. Increasing urbanization, large working-age population, rising incomes and strong impetus on infrastructure and construction sectors are likely to be the key factors driving the industry's growth over the coming years. Other drivers of growth include rising commercial aircraft production, increasing defense spending and growing demand for metal forged parts in the nuclear power industry.



Source: ACE Equity, SIAM

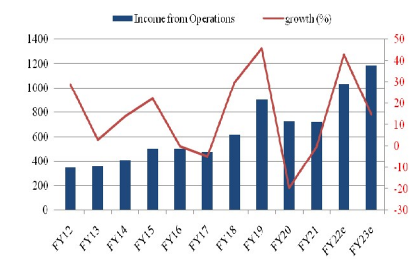


Source: ACE Equity, SIAM

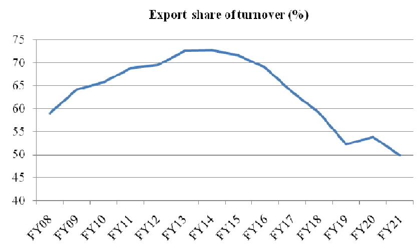
India, on the other hand, is increasingly addressing opportunities arising out of the growing trend among global automotive OEMs to outsource components from manufacturers in low-cost countries. Indian forging industry has a capability to forge variety of raw materials like carbon steel, steel, titanium, aluminium, etc. and is contributing significantly to country's growing exports. Further the government's thrust on increasing infrastructure spending aimed at increasing the contribution of the manufacturing sector to GDP is expected to be the key driver for growth in the heavy-duty truck space in the medium to long term. Active support under the PLI scheme, Atmanirbhar Bharat Abhiyan policy and the scrappage policy coupled with investment in road infrastructure points to a long runway for the MHCV sector.

Financials & Valuation

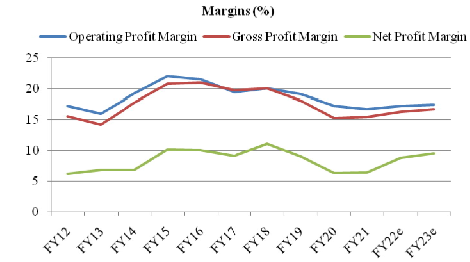
On account of subdued demand from the automotive sector, MMFL's volume off-take took a hit as against an overall revenue decline in FY21 to Rs. 725.65 cr (vsRs 727.29 cr in FY20) with production of some 48000 tons of which exports accounted for almost 50%. Notwithstanding the economic crisis, MMFL ensured business continuity and was able to bounce back strongly in second half of the last fiscal. In Q1FY22, despite the stressful period in the month of May, company's volume off-take stood at some 14,000 tons, which is well in line to meet the FY22 guidance of 60,000 tons.



Sources: M M Forgings Ltd; CD Equisearch



Source: M M Forgings Ltd

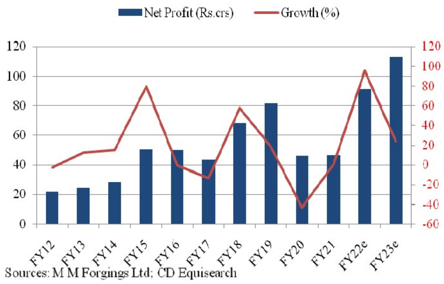


Sources: M M Forgings Ltd; CD Equisearch

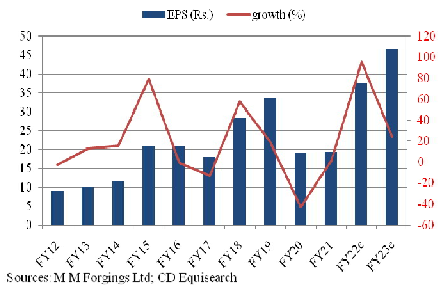
Currently, the scarce availability of semiconductors is a major concern plaguing the automotive industry, not only in India but globally. The prevalent supply-side headwinds are likely to slow down the PV sales. Fortunately, despite the chip shortage, MMFL continues to see robust order flows given the fact that the company has more than 70% exposure to medium and heavy commercial vehicle segment, where chip usage is presumably low compared to passenger vehicles. Any major impact of this crisis on the financials of the company is likely to be observed in the coming quarters.

MM Forgings has earmarked capex of Rs 75 cr this fiscal and another Rs. 50 cr next fiscal. The management has guided this planned capex to be machining related with some part to be utilized for minor debottlenecking that will aid in improving productivity, though production capacity will remain unaffected. Further, MMFL has recently acquired CAFOMA Autoparts Pvt Ltd, a major supplier of machined crankshafts to the tractor and industrial sectors with a capacity to produce 15,000 crankshafts per month. The pandemic has brought forth some structural changes wherein many OEMs are now directly sourcing machined ancillaries and hiving off their captive machining facilities. Hence, MMF expects to unlock synergies by supplying forged crankshafts to CAFOMA. This company marks the latest in a string of acquisitions of crankshaft machining lines taking up MMFL's capacity of machined crankshafts to 60,000 per month.

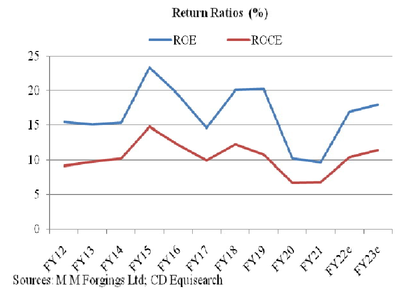
Although the domestic CV industry is expected to recover vigorously in the current fiscal, but ocean freight rates have surged unprecedently during the last couple of quarters, affecting shipment schedules and margins adversely. These challenges may continue to linger for a few more quarters as well. MMF has been continuously adapting to the emerging situation with resilience through years of expertise in manufacturing and quality control. Yet lurching uncertainty of Covid19 have muddled economic outlook for much of the global economy, precipitating the risk of missing the guidance as set by management.



Sources: M M Forgings Ltd; CD Equisearch

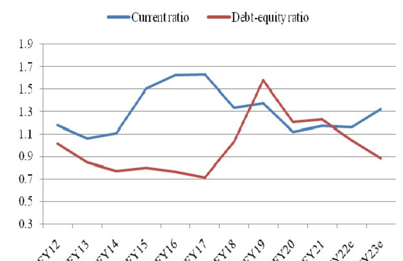


Sources: M M Forgings Ltd; CD Equisearch

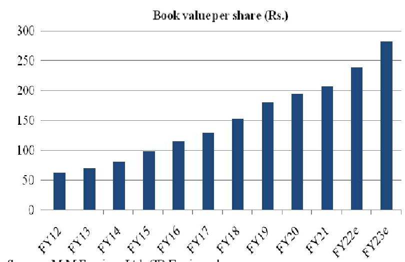


Sources: M M Forgings Ltd; CD Equisearch

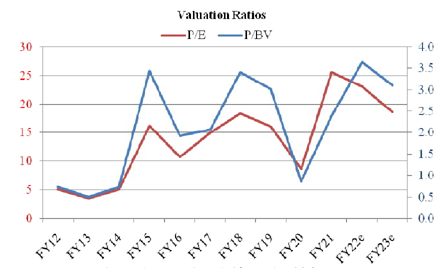
The stock currently trades at 23.1x FY22e EPS of Rs 37.77 and 18.7x FY23e EPS of Rs 46.78. MM Forgings' proximity to ports giving it a logistical edge with regards to international supplies is a barely puny competitive advantage. The management's focus on improving capacity utilization, cost optimization initiatives and timely execution of orders would help the company increase its market share in the midst of a sudden shift in supply side dynamics. Moreover, India's successful mass vaccination drive and medical preparedness have greatly improved mobility and reduced the possibility of a hostile third wave of Covid-19. Though a barely subdued debt-equity ratio does not leave a major scope for PE expansion, but impressive earnings growth would push ROCE to 16.9% this fiscal and to 17.9% in FY23. On balance, we recommend 'HOLD' rating on the stock with target price of Rs 936 based on 20x FY23e EPS of Rs 46.78 over a period of 9-12 months. For more information, refer to our October 2020 report.



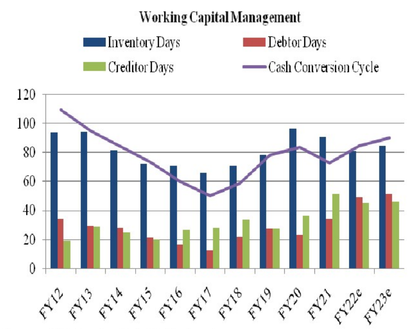
Sources: M M Forgings Ltd; CD Equisearch



Sources: M M Forgings Ltd; CD Equisearch



Sources: M M Forgings Ltd; CD Equisearch; *forward multiple



Sources: M M Forgings Ltd; CD Equisearch

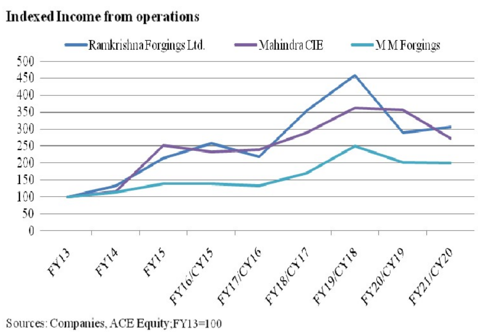
Cross Sectional Analysis

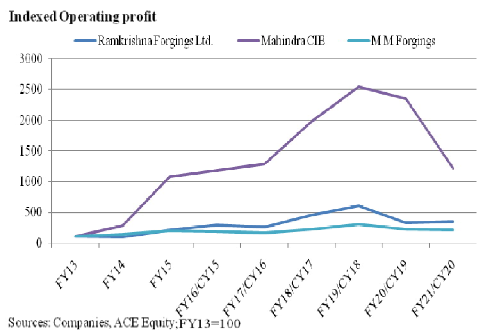
Company	Equity*	CMP	MCAP*	Sales*	Profit*	OPM (%)	NPM (%)	Int Cov	ROE (%)	Mcap/Sales	P/BV	P/E
M M Forgings	24	873	2108	889	75	17.7	8.5	3.8	15.3	2.4	4.0	28.0
Ramkrishna Forgings	32	1165	3726	1923	118	21.3	6.1	3.2	13.3	1.9	3.9	31.6
Mahindra CIE	379	279	10589	8280	425	13.0	5.1	16.4	33.5	1.3	7.4	24.9

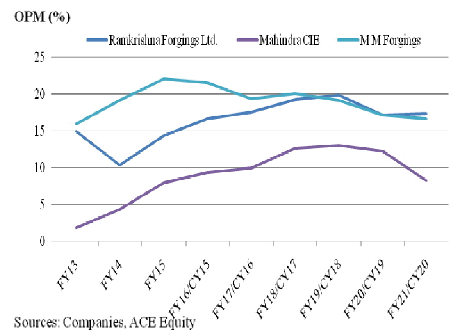
*figures in crores; calculations on ttm basis; standalone or consolidated data as available.

Despite the prevailing stress in the automotive market, Mahindra CIE delivered a steady top-line growth of 2.4% at Rs 2090.69 cr in Q3CY21 on a sequential basis, with the domestic market growing 21.9% to Rs 1157.36 cr. Yet the ongoing semiconductor shortage severely affected its European business, resulting in a revenue de-growth of 14.2% to Rs 951.17 cr on q-o-q basis. However, banking upon the revival of the PV market, revenues for the nine months ended September 30 surged by 54.5% to Rs 6322.56 cr, thereby pushing-up operating profits to an impressive Rs. 815.14 cr in the same period - its operating margins expanded to a robust 12.9% from 5.8% in 9MCY20. Presently, Mahindra CIE's business operations appear to be back on track with its cost cutting efforts and new product developments in pipeline. Recently, Metalcastello, a subsidiary company, has secured a large size order for EV parts worth €20 million per annum from an American customer. Another subsidiary, Bill Forge, has also secured orders of a similar quantum for driveline parts. Any such significant order win could improve its product mix and act as a rerating factor.

Ramkrishna Forgings witnessed a strong growth momentum in its top-line in Q2FY22 on the back of a recovering domestic CV market and new customer wins across its business segments. Its overall revenues grew by 37.4% to Rs. 578.82 cr on a sequential basis (standalone revenues grew by over 40% with domestic turnover comprising 51.5%; 39.9% growth in overall volumes). This robust top-line performance aided the operating profits to climb up by 36.8% q-o-q to Rs 131.07 cr, yielding an OPM of 22.6%. Furthermore, despite the global chip crisis, the company continued to see healthy export orders that raked in some Rs 286.74 cr in Q2FY22, up 28.9% sequentially. With major capital expenses in plan, the company's already strong global foothold and relationships with OEMs across sectors could help it attain higher geographical penetration and further increase its market share. However, risks related to semiconductors supply crunch, increase of input and freight costs could impact margins.







Note: Graphs on standalone or consolidated data as applicable; Mahindra CIE changed its financial year to calendar year in 2015.

Financials

Standalone Quarterly Results

Figures in Rs crs

	Q1FY22	Q1FY21	% chg	FY21	FY20	% chg
Income From Operations	**239.37**	**76.40**	**213.3**	**725.65**	**727.29**	**-0.2**
Other Income	4.46	8.04	-44.5	21.59	18.51	16.7
Total Income	**243.83**	**84.44**	**188.8**	**747.24**	**745.80**	**0.2**
Total Expenditure	195.95	69.41	182.3	604.35	602.10	0.4
EBITDA (other income included)	**47.88**	**15.03**	**218.6**	**142.89**	**143.70**	**-0.6**
Interest	6.54	6.97	-6.2	31.22	33.05	-5.5
Depreciation	15.00	13.00	15.4	56.73	53.23	6.6
PBT	**26.34**	**-4.95**	**-**	**54.93**	**57.42**	**-4.3**
Tax	2.50	0.00	-	8.32	11.19	-25.6
PAT	**23.84**	**-4.95**	**-**	**46.61**	**46.23**	**0.8**
Extraordinary Item	-	-	-	-	-	-
Adjusted Net Profit	**23.84**	**-4.95**	**-**	**46.61**	**46.23**	**0.8**
EPS (Rs)	9.87	-2.05	-	19.31	19.15	0.8

Standalone Income Statement

Figures in Rs crs

	FY19	FY20	FY21	FY22e	FY23e
Income From Operations	**903.92**	**727.29**	**725.65**	**1036.00**	**1189.00**
Growth (%)	45.6	-19.5	-0.2	42.8	14.8
Other Income	15.87	18.51	21.59	22.80	22.98
Total Income	**919.79**	**745.80**	**747.24**	**1058.80**	**1211.98**
Total Expenditure	730.67	602.10	604.35	857.15	980.93
EBITDA (other income included)	**189.12**	**143.70**	**142.89**	**201.64**	**231.05**
Interest	26.14	33.05	31.22	33.28	33.49
Depreciation	54.41	53.23	56.73	59.83	63.11
PBT	**108.57**	**57.42**	**54.93**	**108.54**	**134.44**
Tax	27.21	11.19	8.32	17.37	21.51
PAT	**81.35**	**46.23**	**46.61**	**91.17**	**112.93**
Extraordinary Item	0.02	-	-	-	-
Adjusted Net Profit	**81.33**	**46.23**	**46.61**	**91.17**	**112.93**
EPS (Rs)	33.69	19.15	19.31	37.77	46.78

Balance Sheet

Figures in Rs crs

	FY19	FY20	FY21	FY22e	FY23e
Sources of Funds					
Share Capital	24.14	24.14	24.14	24.14	24.14
Reserves & Surplus	412.11	444.16	476.22	555.33	656.19
Total Shareholders' Funds	**436.25**	**468.31**	**500.36**	**579.47**	**680.33**
Long Term Debt	396.29	334.70	297.32	264.56	236.79
Total Liabilities	**832.53**	**803.01**	**797.68**	**844.02**	**917.12**
Application of Funds					
Gross Block	1032.12	1150.08	1171.42	1255.89	1297.89
Less: Accumulated Depreciation	444.07	497.18	553.91	613.73	676.85
Net Block	**588.06**	**652.91**	**617.51**	**642.15**	**621.04**
Capital Work in Progress	39.19	8.71	17.47	8.00	16.00
Investments	4.88	4.88	4.88	32.88	32.88
Current Assets, Loans & Advances					
Inventory	187.50	130.73	168.60	210.31	242.56
Trade Receivables	79.25	12.46	121.67	155.40	178.35
Cash and Bank	171.56	174.36	187.06	129.56	191.50
Other current assets	39.51	23.67	28.59	35.14	40.13
Total CA & LA	**477.82**	**341.22**	**505.91**	**530.41**	**652.53**
Current Liabilities	339.70	303.87	416.82	456.29	493.80
Provisions-Short term	7.09	0.00	14.55	0.00	0.00
Total Current Liabilities	**346.79**	**303.87**	**431.37**	**456.29**	**493.80**
Net Current Assets	131.03	37.35	74.55	74.12	158.74
Net Deferred Tax	-18.64	-29.81	-30.88	-32.65	-33.75
Net long term assets	88.01	128.96	114.16	119.52	122.21
Total Assets	**832.53**	**803.01**	**797.68**	**844.02**	**917.12**

Key Financial Ratios

	FY19	FY20	FY21	FY22e	FY23e
Growth Ratios (%)					
Revenue	45.6	-19.5	-0.2	42.8	14.8
EBITDA	38.4	-24.0	-0.6	41.1	14.6
Net Profit	18.9	-43.2	0.8	95.6	23.9
EPS	18.9	-43.2	0.8	95.6	23.9
Margins (%)					
Operating Profit Margin	19.2	17.2	16.7	17.3	17.5
Gross Profit Margin	18.0	15.2	15.4	16.3	16.6
Net Profit Margin	9.0	6.4	6.4	8.8	9.5
Return (%)					
ROCE	10.8	6.8	6.8	10.4	11.4
ROE	20.2	10.2	9.6	16.9	17.9
Valuations					
Market Cap/ Sales	1.5	0.6	1.6	2.0	1.8
EV/EBITDA	9.7	5.5	11.3	12.6	11.0
P/E	16.2	8.7	25.6	23.1	18.7
P/BV	3.0	0.9	2.4	3.6	3.1
Other Ratios					
Interest Coverage	5.2	2.7	2.8	4.3	5.0
Debt Equity	1.6	1.2	1.2	1.0	0.9
Current Ratio	1.4	1.1	1.2	1.2	1.3
Turnover Ratios					
Fixed Asset Turnover	1.9	1.2	1.1	1.6	1.9
Total Asset Turnover	1.3	0.9	0.9	1.3	1.4
Debtors Turnover	13.3	15.9	10.8	7.5	7.1
Inventory Turnover	4.7	3.8	4.0	4.5	4.3
Creditor Turnover	13.4	10.1	7.1	8.1	8.0
WC Ratios					
Debtor Days	27.4	23.0	33.7	48.8	51.2
Inventory Days	78.1	96.5	90.4	80.7	84.3
Creditor Days	27.3	36.2	51.3	45.1	45.5
Cash Conversion Cycle	78.2	83.3	72.9	84.4	89.9

Cumulative Financial Data

Rs crs	FY15-17	FY18-20	FY21-23e
Income from operations	1483	2252	2951
Operating profit	312	423	508
EBIT	220	320	396
PBT	193	248	298
PAT	144	196	251
Dividends	25	42	36
Sales growth (%)	-	51.8	31.0
PAT growth (%)	-	36.0	27.9
OPM (%)	21.0	18.8	17.2
GPM (%)	20.4	17.7	16.2
NPM (%)	9.7	8.7	8.5
Interest coverage	8.0	4.5	4.0
ROE (%)	18.8	16.7	14.6
ROCE (%)	12.4	10.7	9.6
Debt-Equity ratio*	0.7	1.2	0.9
Fixed asset turnover	1.9	1.5	1.5
Total asset turnover	1.5	1.2	1.1
Debtors turnover	21.4	50.5	10.3
Creditors turnover	17.6	12.1	8.0
Inventory turnover	5.5	6.2	4.4
Debtor days	17.1	7.2	35.4
Creditor days	20.8	30.1	45.4
Inventory days	66.5	58.9	83.7
Cash conversion cycle	62.7	36.0	73.7
Dividend payout ratio (%)	17.5	21.6	14.4

FY 15-17 implies three year period ending fiscal 17; *as on terminal year

Barely tepid recovery in the commercial vehicle space and strong OEM dispatches explains much of the 31% rise in cumulative income from operations during FY21-23e when compared to that in the preceding three year period. Yet OPMs would not likely grow apace with top-line given the prevalent volatility in raw material prices and sky-high freight costs (see table). Driven by this robust revenue growth in cumulative FY22-23 period, EBIT would grow some 23.8% in FY21-23e. Interest coverage ratio will decline from 4.5 to 4(see table).

Higher stocking of finished products at its warehouses won't do much but debase its inventory turnover ratio to 4.4 in FY21-23e period from 6.2 - inventory days estimated to rise to some 83.7 days in the cumulative three-year period (see table). Moreover, this high inventory days aided by growing debtor days would be barely counterbalanced by rising creditor days leading to rise in cash conversion cycle (see table).

Financial Summary- US Dollar denominated

million $	FY19	FY20	FY21	FY22e	FY23e
Equity capital	3.5	3.2	3.3	3.2	3.2
Shareholders' funds	63.1	62.1	68.1	77.2	90.7
Total debt	99.4	75.1	83.7	80.8	79.8
Net fixed assets (including CWIP)	90.7	87.8	86.4	86.7	84.9
Investments	0.7	0.6	0.7	4.4	4.4
Net current assets	18.9	5.0	10.1	9.9	21.2
Total assets	120.4	106.5	108.5	112.5	122.3
Revenues	129.3	102.6	97.8	138.1	158.5
EBITDA	27.1	20.3	19.3	26.9	30.8
EBDT	23.3	15.6	15.0	22.4	26.3
PBT	15.5	8.1	7.4	14.5	17.9
PAT	11.6	6.5	6.3	12.2	15.1
EPS($)	0.48	0.27	0.26	0.50	0.62
Book value ($)	2.61	2.57	2.82	3.20	3.76

Income statement figures translated at average rates; balance sheet at year end rates; projections at current rates (Rs 75.02/$).
All dollar denominated figures are adjusted for extraordinary items.

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buy: >20%	accumulate: >10% to ≤20%	hold: ≥-10% to ≤10%	reduce: ≥-20% to <-10%	sell: <-20%

Exchange Rates Used- Indicative

Rs/$	FY18	FY19	FY20	FY21
Average	64.45	69.89	70.88	74.20
Year end	65.04	69.17	75.39	73.50

All $ values mentioned in the write-up translated at the average rate of the respective quarter/ year as applicable. Projections converted at current exchange rate. Cumulative dollar figure is the sum of respective yearly dollar value.