

## RETAIL EQUITY RESEARCH

## L G Balakrishnan &amp; Bros Ltd

## Automobile Ancillaries

BSE CODE:500250

NSE CODE: LGBBROSLTD

Bloomberg CODE: LGBB IN SENSEX: 29,410

Buy

Rating as per Midcap

12months investment period

CMP Rs609 TARGET Rs703 RETURN 15%29<sup>th</sup> March, 2017

## Demonetisation impact to fade away by H1FY18E...

LG Balakrishnan & Bros (LGB) is India's leading manufacturers in 2wheeler chain transmission (Drive chains) and sprockets with a domestic market share of 75% and around 50% in the replacement market.

- 9MFY17 consolidated Revenue & PAT grew by muted 6% & 7%YoY due to the impact of demonetisation in Q3FY17.
- We expect recovery in volume for the 2-Wheeler industry from H1FY18 and the pressure is likely to continue in 4QFY17.
- To account the trickledown effect of demonetisation we lower our Revenue/PAT estimate for FY18 by 7% & 21% respectively.
- We factor consolidated earnings to grow by 17% CAGR over FY17E-FY19E with healthy domestic market and capacity additions.
- We roll-over our valuation to FY19E and maintain our valuation at a P/E of 12x on improved earnings outlook. We maintain our rating as Buy with a revised target price of Rs703.

## 2W industry looks favourable in the medium to long term.

LGB's major revenue comes from 2W industry. We expect the industry to grow by double digit in volume over FY17-19E led by increase in rural income. Higher crop productivity through favorable monsoon and government initiatives will remain the underlined factor. Shift toward premium bikes in the urban sector owing to technological up gradation (like Bajaj, Enfield) has given higher realization and revenue visibility. LGBs revenue from loss making segment like Metal forging and other business have grown by 10% & 9% for 9mFY17.

## Capacity addition to mitigate volume constraints

LGB has invested 80cr for the Chennai plant and the plant is expected to commence in H2FY18. LGB has excellent relationship with OEM's like Bajaj Auto, HMSI, TVS Motors, Eicher Motors and Hero Motor to prop up its transmission & fine blanking businesses. LGB's Greenfield project with capex of ~Rs1.6bn in Jalna (Aurangabad) has already commissioned. The plant would mainly execute orders for Bajaj Auto and replacement market.

## Q4 to remain tepid

We expect Q4FY17 revenue growth to remain tepid due to the extent of demonetisation impact. During 9mFY17, LGB registered a revenue growth of 6% led by 5% segment growth from the Chain and sprockets (used to rotate transmission chains) business. 80% of total revenue is contributed from this segment, out of which 60% is OEM and 40% is aftermarket. Even though there is some sign of improvement in February MoM sales, we expect 2W sales to pick by 1HFY18. Revenue to grow by 13% CAGR during FY17-19E by factoring 13% CAGR growth in transmission chains business.

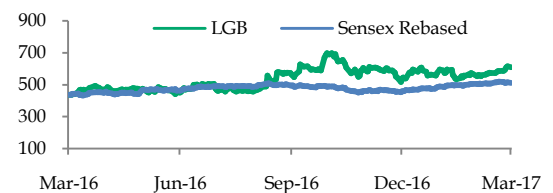
## Valuation...

We expect the earnings to grow by 18% CAGR over FY17-19E on the back pick up in domestic 2-Wheeler market and capacity additions. Considering the near term headwinds due to demonetisation we lower our Revenue/PAT estimate by 9% & 25%. We roll over our valuation to FY19E EPS and value at a P/E 12x (3yr historical average) with a revised target price of Rs703 and maintain our rating as Buy.

Company Data			
Market Cap (cr)	Rs956		
Enterprise Value (cr)	Rs1,095		
Outstanding Shares (cr)	1.6		
Free Float	53%		
Dividend Yield	1.6%		
52 week high	Rs729		
52 week low	Rs419		
6m average volume (cr)	0.01		
Beta	0.84		
Face value	Rs10		
Shareholding %	Q1FY17	Q2FY17	Q3FY17
Promoters	47.5	47.5	47.4
FII's	1.2	1.4	1.5
MFs/Insti	13.8	13.8	13.4
Public	37.5	37.3	37.6
Total	100.0	100.0	100.0

Price Performance	3mth	6mth	1 Year
Absolute Return	11.9%	6.2%	39.5%
Absolute Sensex	12.3%	2.0%	17.1%
Relative Return*	-0.4%	4.1%	19.1%

\*over or under performance to benchmark index



Consolidated (Rs.cr)	FY17E	FY18E	FY19E
Sales	1,245	1,419	1,595
Growth (%)	3.3	14.0	12.4
EBITDA	159	185	207
Margin(%)	12.8	13.0	13.0
PAT Adj	67	81	92
Growth (%)	6.1	20.9	13.0
Adj.EPS	42.9	51.9	58.6
Growth (%)	6.1	20.9	13.0
P/E	14.2	12.0	10.4
P/B	2.0	1.8	1.5
EV/EBITDA	6.7	5.7	5.1
RoE (%)	15.1	15.2	15.5
D/E	0.2	0.2	0.2

Saji John  
Analyst

## Financials (Consolidated)

### Profit & Loss Account

(Rs cr)	9mFY17	9mFY16	YoY Growth %
Net Revenue	858	812	5.7
EBITDA	109	94	15.1
Margin (%)	12.7	11.6	110bps
Depreciation	36	32	16.3
EBIT	72	63	14.5
Interest	11	13	(15.1)
Other Income	2	3	15.0
Exceptional Items	-	0.7	-
PBT	65	52	24.3
Tax	20	11	86.2
Reported PAT	45	41	10.0
Adjustment	0.7	-	-
Adj PAT	44	41	7.3
No. of shares (cr)	1.6	1.6	-
EPS (Rs)	28	26	7.3

## Change in estimates

Year / Rs cr	Old estimates		New estimates		Change %	
	FY17E	FY18E	FY17E	FY18E	FY17E	FY18E
Revenue	1,353	1,525	1,245	1,419	(7.9)	(6.9)
EBITDA	182	215	159	185	(12.6)	(13.9)
Margins (%)	13.5	14.1	12.8	13.0	(70bps)	(110bps)
PAT	82	103	67	81	(18.2)	(21.0)
EPS	52.5	65.4	42.9	51.9	(18.2)	(21.0)

## Consolidated Financials

### Profit & Loss Account

Y.E March (Rs cr)	FY15A	FY16A	FY17E	FY18E	FY19E
<b>Sales</b>	<b>1,173</b>	<b>1,205</b>	<b>1,245</b>	<b>1,419</b>	<b>1,595</b>
% change	5.8	2.8	3.3	14.0	12.4
<b>EBITDA</b>	<b>142</b>	<b>138</b>	<b>159</b>	<b>185</b>	<b>207</b>
% change	12.8	-3.2	15.7	16.0	12.1
Depreciation	39	46	49	57	65
EBIT	103	92	110	121	143
Interest	18	18	15	12	12
Other Income	2	4	4	5	5
<b>PBT</b>	<b>94</b>	<b>78</b>	<b>99</b>	<b>120</b>	<b>136</b>
% change	17.3	-17.2	27.0	21.8	12.7
Tax	20	13	27	36	41
Tax Rate (%)	21.8	16.6	27.5	30.0	30.0
<b>Reported PAT</b>	<b>71</b>	<b>63</b>	<b>67</b>	<b>81</b>	<b>92</b>
Adj*	6.6	0.0	0.0	0.0	0.0
<b>Adj PAT</b>	<b>65</b>	<b>63</b>	<b>67</b>	<b>81</b>	<b>92</b>
% change	4.3	-1.7	6.1	20.9	12.9
No. of shares (mn)	1.6	1.6	1.6	1.6	1.6
<b>Adj EPS (Rs)</b>	<b>41.2</b>	<b>40.4</b>	<b>42.9</b>	<b>51.9</b>	<b>58.6</b>
% change	4.3	-1.7	6.1	20.9	12.9
DPS (Rs)	8.4	7.2	7.0	7.0	7.0
CEPS (Rs)	66.3	69.7	74.3	88.3	99.7

### Cash flow

Y.E March (Rs cr)	FY15A	FY16A	FY17E	FY18E	FY19E
Net inc. + Depn.	133	124	148	177	200
Non-cash adj.	(9.9)	0.8	(24.7)	(33.1)	(37.3)
Changes in W.C	(5.1)	(6.5)	30.2	(30.7)	(32.9)
<b>C.F.O</b>	<b>118</b>	<b>118</b>	<b>154</b>	<b>114</b>	<b>130</b>
Capital exp.	(116)	(78)	(85)	(80)	(70)
Change in inv.	0	(1)	(23)	0.1	(44)
Other invest.CF	2	(8)	-	-	-
<b>C.F - investing</b>	<b>(114)</b>	<b>(87)</b>	<b>(108)</b>	<b>(80)</b>	<b>(114)</b>
Issue of equity	0	0	0	0	0
Issue/repay debt	27	(18)	(30)	(15)	7
Dividends paid	(13)	(11)	(11)	(11)	(11)
Other finance.CF	(19)	(4)	-	-	-
<b>C.F - Financing</b>	<b>(4)</b>	<b>(34)</b>	<b>(41)</b>	<b>(26)</b>	<b>(4)</b>
Chg. in cash	0.5	(2.2)	(1.3)	3	9
Closing cash	7	8	7	10	18

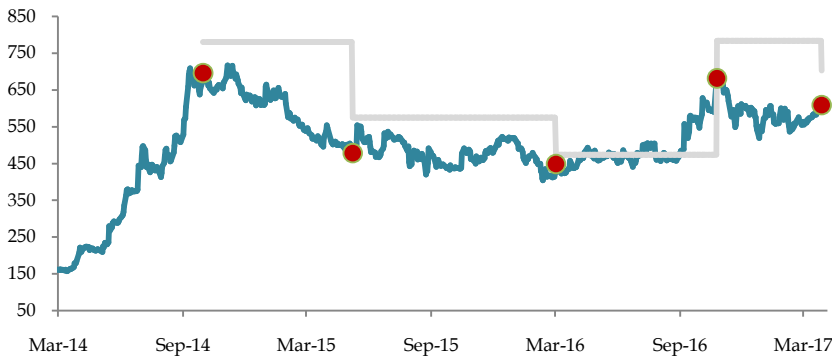
### Balance Sheet

Y.E March (Rs cr)	FY15A	FY16A	FY17E	FY18E	FY19E
Cash	7	8	7	10	18
Accounts Receivable	147	153	157	183	201
Inventories	231	228	206	236	269
Other Cur. Assets	51	62	59	69	86
Investments	18	19	41	41	85
Gross Fixed Assets	560	664	744	824	899
Net Fixed Assets	300	363	394	417	427
CWIP	37	10	15	15	10
Intangible Assets	3	3	3	3	3
Def. Tax (Net)	(17)	(18)	(14)	(12)	(12)
Other Assets	13	14	14	14	14
<b>Total Assets</b>	<b>789</b>	<b>842</b>	<b>883</b>	<b>975</b>	<b>1,102</b>
Current Liabilities	64	79	85	93	106
Provisions	7	2	7	8	4
Debt Funds	157	139	109	94	102
Other Liabilities	183	190	188	214	240
Equity Capital	16	16	16	16	16
Reserves & Surplus	362	416	477	551	635
Shareholder's Fund	365	416	474	544	625
<b>Total Liabilities</b>	<b>789</b>	<b>842</b>	<b>883</b>	<b>975</b>	<b>1,102</b>
<b>BVPS (Rs)</b>	<b>23</b>	<b>26</b>	<b>30</b>	<b>34</b>	<b>40</b>

### Ratios

Y.E March	FY15A	FY16A	FY17E	FY18E	FY19E
<b>Profitab. &amp; Return</b>					
EBITDA margin (%)	12.1	11.4	12.8	13.0	13.0
EBIT margin (%)	8.8	7.6	8.8	9.0	8.9
Net profit mgn.(%)	5.5	5.3	5.4	5.7	5.8
ROE (%)	19.2	16.3	15.1	16.0	15.7
ROCE (%)	12.9	12.5	10.5	10.8	10.9
<b>W.C &amp; Liquidity</b>					
Receivables (days)	45.5	45.3	45.4	43.7	43.9
Inventory (days)	68.2	69.4	63.7	56.8	57.7
Payables (days)	3.5	4.3	5.1	5.4	5.4
Current ratio (x)	6.1	5.6	4.6	4.9	5.2
Quick ratio (x)	2.4	2.0	1.9	2.1	2.1
<b>Turnover &amp; Levlg.</b>					
Gross asset T.O (x)	2.3	2.0	1.8	1.8	1.9
Total asset T.O (x)	1.6	1.5	1.4	1.5	1.5
Int. covge. ratio (x)	5.8	5.1	7.3	10.4	12.0
Adj. debt/equity (x)	0.4	0.3	0.2	0.2	0.2
<b>Valuation ratios</b>					
EV/Sales (x)	0.9	0.9	0.9	0.7	0.7
EV/EBITDA (x)	7.8	8.0	6.7	5.7	5.1
P/E (x)	14.8	15.1	14.2	11.7	10.4
P/BV (x)	2.6	2.3	2.0	1.8	1.5

### Recommendation Summary (last 3 years)



Source: Bloomberg, Geojit Research

Dates	Rating	Target
30-September-14	*Accumulate	780
8-May-15	Accumulate	575
2-March-16	Accumulate	474
25-October-16	Buy	784
29-March-17	Buy	703

\*Initiating Coverage

### Investment Rating Criteria

Large Cap Stocks;		Mid Cap and Small Cap;	
<b>Buy</b>	-	<b>Buy</b>	-
<b>Hold</b>	-	<b>Accumulate*</b>	-
<b>Reduce</b>	-	<b>Hold</b>	-
		<b>Reduce/Sell</b>	-
		To satisfy regulatory requirements, we attribute 'Accumulate' as Buy and 'Reduce' as Sell.	

The recommendations are based on 12 month horizon, unless otherwise specified. The investment ratings are on absolute positive/negative return basis. It is possible that due to volatile price fluctuation in the near to medium term, there could be a temporary mismatch to rating.

\* For reasons of valuations/return/lack of clarity/event we may revisit rating at appropriate time. Please note that the stock always carries the risk of being upgraded to BUY or downgraded to a HOLD, REDUCE or SELL.

### General Disclosures and Disclaimers

#### CERTIFICATION

I, Saji John, author of this Report, hereby certify that all the views expressed in this research report reflect our personal views about any or all of the subject issuer or securities. This report has been prepared by the Research Team of Geojit Financial Services Limited, hereinafter referred to as Geojit.

#### COMPANY OVERVIEW

Geojit Financial Services Limited (hereinafter Geojit), a publically listed company, is engaged in services of retail broking, depository services, portfolio management and marketing investment products including mutual funds, insurance and properties. Geojit is a SEBI registered Research Entity and as such prepares and shares research data and reports periodically with clients, investors, stake holders and general public in compliance with Securities and Exchange Board of India Act, 1992, Securities And Exchange Board Of India (Research Analysts) Regulations, 2014 and/or any other applicable directives, instructions or guidelines issued by the Regulators from time to time.

#### DISTRIBUTION OF REPORTS

This document is not for public distribution and has been furnished to you solely for your information and must not be reproduced or redistributed to any other person. Geojit will not treat the recipients of this report as clients by virtue of their receiving this report.

#### GENERAL REPRESENTATION

The research reports do not constitute an offer or solicitation for the purchase or sale of any financial instruments, inducements, promise, guarantee, warranty, or as an official confirmation of any transaction or contractual obligations of any kind. This report is provided for assistance only and is not intended to be and must not alone be taken as the basis for an investment decision. The information contained herein is from publicly available data or other sources believed to be reliable, but we do not represent that it is accurate or complete and it should not be relied on as such. We have also reviewed the research report for any untrue statements of material facts or any false or misleading information. While we endeavor to update on a reasonable basis the information discussed in this material, there may be regulatory, compliance, or other reasons that prevent us from doing so.

#### RISK DISCLOSURE

Geojit and/or its Affiliates and its officers, directors and employees including the analyst/authors shall not be in any way be responsible for any loss or damage that may arise to any person from any inadvertent error in the information contained in this report. Investors may lose his/her entire investment under certain market conditions so before acting on any advice or recommendation in these material, investors should consider whether it is suitable for their particular circumstances and, if necessary, seek professional advice. This report does not take into account the specific investment objectives, financial situation/circumstances and the particular needs of any specific person who may receive this document. The user assumes the entire risk of any use made of this information. Each recipient of this report should make such investigation as it deems necessary to arrive at an independent evaluation of an investment in the securities of companies referred to in this report (including the merits and risks involved). The price, volume and income of the investments referred to in this report may fluctuate and investors may realize losses that may exceed their original capital.

#### FUNDAMENTAL DISCLAIMER

We have prepared this report based on information believed to be reliable. The recommendations herein are based on 12 month horizon, unless otherwise specified. The investment ratings are on absolute positive/negative return basis. It is possible that due to volatile price fluctuation in the near to medium term, there could be a temporary mismatch to rating. For reasons of valuations/return/lack of clarity/event we may revisit rating at appropriate time. The stocks always carry the risk of being upgraded to buy or downgraded to a hold, reduce or sell. The opinions expressed are subject to change but we have no obligation to tell our clients when our opinions or recommendations change. This report is non-inclusive and does not consider all the information that the recipients may consider material to investments. This report is issued by Geojit without any liability/undertaking/commitment on the part of itself or any of

its entities. We may have issued or may issue on the companies covered herein, reports, recommendations or information which is contrary to those contained in this report.

The projections and forecasts described in this report should be evaluated keeping in mind the fact that these are based on estimates and assumptions and will vary from actual results over a period of time. The actual performance of the companies represented in the report may vary from those projected. These are not scientifically proven to guarantee certain intended results and hence, are not published as a warranty and do not carry any evidentiary value whatsoever. These are not to be relied on in or as contractual, legal or tax advice. Prospective investors and others are cautioned that any forward-looking statements are not predictions and may be subject to change without notice.

#### JURISDICTION

The securities described herein may not be eligible for sale in all jurisdictions or to all categories of investors. The countries in which the companies mentioned in this report are organized may have restrictions on investments, voting rights or dealings in securities by nationals of other countries. Distributing/ taking/sending/dispatching/transmitting this document in certain foreign jurisdictions may be restricted by law, and persons into whose possession this document comes should inform themselves about, and observe any such restrictions. Failure to comply with this restriction may constitute a violation of any foreign jurisdiction laws. Foreign currencies denominated securities are subject to fluctuations in exchange rates that could have an adverse effect on the value or price of or income derived from the investment. Investors in securities such as ADRs, the value of which are influenced by foreign currencies effectively assume currency risk.

#### REGULATORY DISCLOSURES:

Geojit's Associates consists of privately held companies such as Geojit Technologies Private Limited (GPL- Software Solutions provider), Geojit Credits Private Limited (GCPL- NBFC Services provider), Geojit Investment Services Limited (GISL- Corporate Agent for Insurance products), Geojit Financial Management Services Private Limited (GFMSL) & Geojit Financial Distribution Private Limited (GFDPL), (Distributors of Insurance and MF Units). In the context of the SEBI Regulations on Research Analysts (2014), Geojit affirms that we are a SEBI registered Research Entity and in the course of our business as a stock market intermediary, we issue research reports /research analysis etc that are prepared by our Research Analysts. We also affirm and undertake that no disciplinary action has been taken against us or our Analysts in connection with our business activities.

In compliance with the above mentioned SEBI Regulations, the following additional disclosures are also provided which may be considered by the reader before making an investment decision:

#### 1. Disclosures regarding Ownership\*:

*Geojit confirms that:*

- (i) It/its associates have no financial interest or any other material conflict in relation to the subject company (ies) covered herein.
- (ii) It/its associates have no actual beneficial ownership greater than 1% in relation to the subject company (ies) covered herein.

*Further, the Analyst confirms that:*

- (i) he, his associates and his relatives have no financial interest in the subject company (ies) covered herein, and they have no other material conflict in the subject company.
- (ii) he, his associates and his relatives have no actual/beneficial ownership greater than 1% in the subject company covered

#### 2. Disclosures regarding Compensation:

During the past 12 months, Geojit or its Associates:

- (a) Have not received any compensation from the subject company; (b) Have not managed or co-managed public offering of securities for the subject company (c) Have not \* received any compensation for investment banking or merchant banking or brokerage services from the subject company. (d) Have not received any compensation for products or services other than investment banking or merchant banking or brokerage services from the subject company (e) Have not received any compensation or other benefits from the subject company or third party in connection with the research report (f) The subject company is / was not a client during twelve months preceding the date of distribution of the research report.

#### 3. Disclosure by Geojit regarding the compensation paid to its Research Analyst:

Geojit hereby confirms that no part of the compensation paid to the persons employed by it as Research Analysts is based on any specific brokerage services or transactions pertaining to trading in securities of companies contained in the Research Reports.

#### 4. Disclosure regarding the Research Analyst's connection with the subject company:

It is affirmed that the I Saji John Research Analyst(s) of Geojit have not served as an officer, director or employee of the subject company

#### 5. Disclosure regarding Market Making activity:

Neither Geojit/its Analysts have engaged in market making activities for the subject company.

Please ensure that you have read the "Risk Disclosure Documents for Capital Market and Derivatives Segments" as prescribed by the Securities and Exchange Board of India before investing

Geojit Financial Services Ltd. (formerly known as Geojit BNP Paribas Financial Services Ltd.), Registered Office: 34/659-P, Civil Line Road, Padivattom, Kochi-682024, Kerala, India. Phone: +91 484-2901000, Fax: +91 484-2979695, Website: [geojit.com](http://geojit.com). For investor queries: [customercare@geojit.com](mailto:customercare@geojit.com), For grievances: [grievances@geojit.com](mailto:grievances@geojit.com), For compliance officer: [compliance@geojit.com](mailto:compliance@geojit.com).

Corporate Identity Number: L67120KL1994PLC008403, SEBI Regn.Nos.: NSE: INB/INF/INE231337230 I BSE:INB011337236 & INF011337237 | MSEI: INE261337230, INB261337233 & INF261337233, Research Entity SEBI Reg No: INH200000345, Investment Adviser SEBI Reg No: INA200002817, Portfolio Manager:INP000003203, NSDL: IN-DP-NSDL-24-97, CDSL: IN-DP-CDSL-648-2012, ARN Regn.Nos:0098, IRDA Corporate Agent (Composite) No.: CA0226. Research Entity SEBI Registration Number: INH200000345