Rational Investment Research Pvt. Ltd.
7A, Birat Complex, Boring Road, Patna 800 013
www.rirlimited.com

An Auto Ancillary

The company manufactures parts largely for commercial vehicles and to a much lesser extent for passenger cars. It is a joint collaboration between a multinational and Indian promoter. The company has grown consistently over last ten years. The foreign collaborator has been helpful in terms of transferring the expertise and helping the company to grow. It has become the most dominant supplier for parts in its segment. It has to compete mainly with in house products of its customers. Chinese imports are emerging risks.

Recommendation

We recommend that company shares should be bought at present level with a holding period of six years. In case the stock does not appreciate by more than 10 per cent per annum even the dividend should be reinvested. If the economy continues to grow at current levels the returns in the stock would substantial. Even if economy grows at 5-6 per cent the returns would remain attractive. If the economy grows at even slower pace there could some problems for the company. We expect a return of 20 per cent per annum at the end of six year period. (18th December 2007)

Investment Thesis

- **Track record of growth**: Revenue of the company has grown over six times in last 10 years. The profits have grown more than twenty fold. The market share of the company has also grown. This growth has been managed without any equity dilution. The level of debt has also gone down. Shareholders equity has increased at a fast pace during this period.
- **Steady growth in business expected**: The products made by the company are used by Commercial vehicles (trucks, tractors). Currently high interest rates have lead to fall in demand of commercial vehicles. If India's GDP continues to grow at current pace (or even slightly slower) sales of commercial vehicles will rise. In that case revenue and profits of company will continue to rise.
- **High dividend yield, high cash on book, low utilization of capacity**: The Company's shares offer a good dividend yield of 4 per cent. The dividend yield is itself attractive. Dividend yield can go up. The company has close to 20 per cent of its share price as cash equivalent. Currently the utilization of capacity is only 60 per cent. So company does not have to go for expansion for a sometime. By the time it will have to go for expansion the profits would have increased considerably, increasing the potential to pay dividends.
- **Low valuation**: The Company's share trades at less than 8 times trailing twelve months profits. This implies a negative growth expectation. The company is well placed to much better that. Even if the profit growth stagnates the valuation of the company should be higher. In case there is moderate growth, as we expect, the returns would be very attractive.

Phone No. : 0612-2570270
Email: info@rirlimited.com

Risks

- **Low demand of Commercial Vehicles**: If the demand of commercial vehicles remains low then the company would not be able to grow. Also in that case pricing power of the company would be reduced leading to lower profits.
- **Chinese imports**: Chinese imports are of inferior quality at this time. Still Chinese imports exert pricing pressure on products of the company. The company has to continually invest in research to stay ahead of Chinese imports.
- **Liquidity risk**: The shares are thinly traded. If one has to buy large number of shares then one has to be patient. In case a large number of shares are to be sold in a short period of time it can lead to large fall in price of shares.