

Force Motors

JV divestment a key trigger

Force Motors Ltd. (FML) is an integrated automobile company manufacturing light commercial vehicles and tractors in India. FML's brands include *Traveller*, *Trax*, *Trump* and *Balwan*. Recently, the company sold its stake in MAN Force Trucks Pvt. Ltd. (MFTL), 50:50 JV for an estimated EUR150mn (~₹1,014cr). We believe FML's recent entry into the SUV segment with the launch of *Force One* will enable it to post a top-line CAGR of 22% over FY2011-14E. FML is trading at an attractive PE of 8.7x and EV/Sales of 0.2x on FY2014E. We recommend Buy on FML with a target price of ₹678, based on target PE of 11x and implied EV/Sales of 0.3x for FY2014E.

Investment rationale

MFTL divestment may lead to higher dividend or buyback

FML sold off its entire stake in MAN Force Trucks Pvt. Ltd. (MFTL), 50:50 JV between MAN and FML, in March 2012. This has provided FML with cash inflow of EUR150mn (~₹1,014cr) which is almost equal to FML's enterprise value. This may potentially lead to higher dividend or buy-back.

Exhibit 1: Core PE post cash adjustment

Particulars	₹ cr
Current Mcap	710
Debt	329
Cash	17
Pre cash adjusted EV	1,022
Gross cash inflow (EUR @ ₹67.6)	1,014
Assumed Capital gain tax (20%)	203
Net cash inflow	811
Expected Mcap	210
PAT (9 months ending December 2011)	26
Annualized PAT	35
Core PE (x)	6.1

Source: Angel Research

Outlook and valuation

FML's revenue and net profit are expected to post a CAGR of 22% and 12%, respectively, over FY2011-14E. The stock is currently trading at PE of 10.6x and 8.7x for FY2013E and FY2014E, respectively, which makes it attractive.

We recommend Buy on FML with a target price of ₹678, based on target PE of 11x and implied EV/Sales of 0.3x, offering an upside of 26% from current levels.

Exhibit 2: Key financials

	Sales (₹cr)	OPM (%)	PAT (₹ cr)	EPS (₹)	ROE (%)	P/E (x)	P/BV (x)	EV/ EBITDA (x)	EV/ Sales (x)
FY2011	1,525	6.7	59	44	17.5	12.1	2.1	8.9	0.6
FY2012E	1,939	6.6	45	34	3.8	15.8	0.6	2.3	0.2
FY2013E	2,346	6.7	67	51	5.4	10.6	0.6	3.0	0.2
FY2014E	2,753	7.0	81	62	6.2	8.7	0.5	3.3	0.2

Source: Company Website, Angel Research

BUY

CMP	₹539
Target Price	₹678

Investment Period	12 months
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Stock Info

Sector	Automobile
Market Cap (₹ cr)	710
Beta	0.5
52 Week High / Low	825 / 388
Avg. Daily Volume	9,931
Face Value (₹)	10
BSE Sensex	17,207
Nifty	5,223
Reuters Code	FORC.BO
Bloomberg Code	FML.IN

Shareholding Pattern (%)

Promoters	51.8
Corporate Holding	24.6
FII / NRIs / OCBs	6.1
Indian Public / Others	17.6

Abs.(%)	3m	1yr	3yr
Sensex	18.6	37.3	294.3
FML	1.6	(7.2)	7.7

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After adjusting for the cash due to the stake sell, the core PE of FML arrives at 6.1x, which makes it quite attractive. The earnings considered for the calculation are the annualized earnings for the nine months ending December 2011.

Exhibit 3: Core PE post cash adjustment

Particulars	₹ cr
Current Mcap	710
Debt	329
Cash	17
Pre cash adjusted EV	1,022
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Force One powered by Mercedes engine

FML has recently entered the SUV segment with the launch of *Force One*. The engine installed in *Force One* is of Mercedes Benz S-Class range, made under license from Daimler AG, Germany, which is known for its latest technology. The company has signed Mr. Amitabh Bachchan as the brand ambassador of *Force One*. We have not considered a major increase in revenue due to this launch as the response to the vehicle has been only marginally positive. However, any major success of the new variant which is likely to hit the market by mid-2013 is likely to provide further upside in the stock.

Restructuring on the marketing and branding front

FML has currently restructured its marketing and branding team aggressively. The company has recently appointed Mr. Naresh Ratan (ex. Marketing Head at Honda Motorcycles and Scooters India) as its Chief Operating Officer for the tractor business and as President of Corporate Sales and Marketing. Moreover, with substantial cash surplus in hand, FML is expected to invest considerable amount on the branding and marketing of its products.

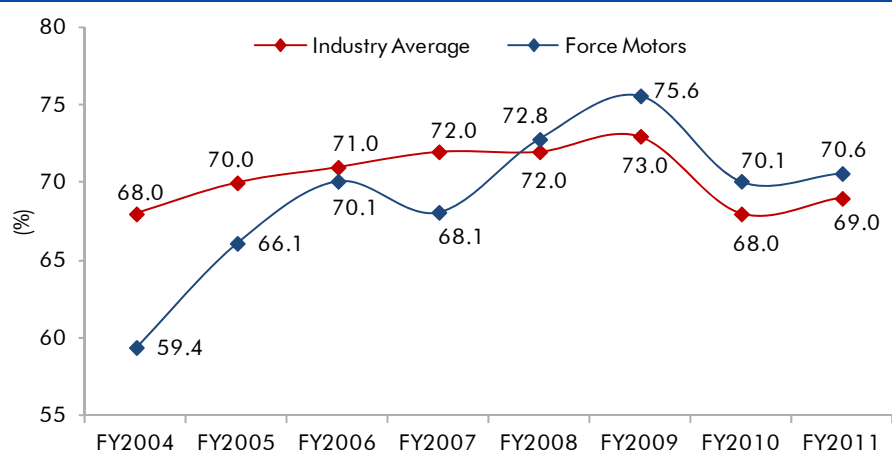
Growth linked to the economy's health

The interest rate cycle has become benign on account of recent repo rate cut of 50bp to 8% by the RBI, which is likely to drive the economy's growth northwards. The correlation between freight movement (demand for LCV) and aggregate GDP is at ~0.98 times from 1970-71 to 2010-11. Considering the above facts, we expect the future outlook for the industry to be bright.

Sufficient levers to enable margin expansion

Considering the consistent improvement in capacity utilization, which is currently at 48%, we expect the company to benefit from its operating leverage.

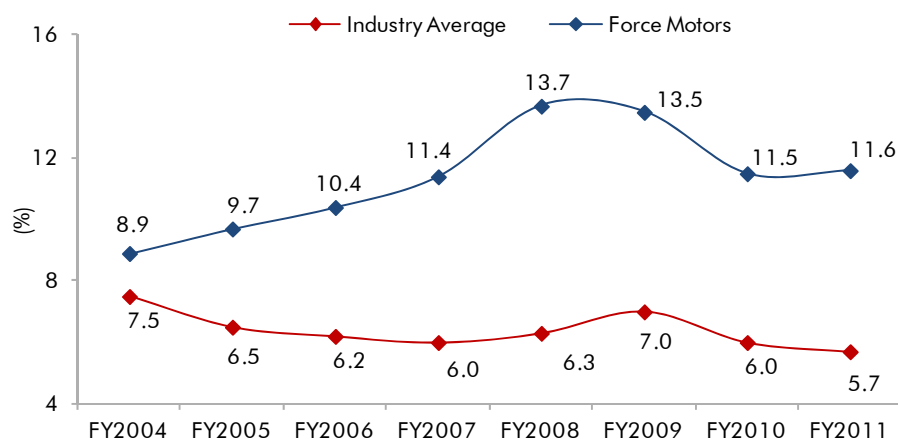
Exhibit 4: Raw-material cost as % of net sales



Source: Company Website, CRISIL Research

Raw-material cost of FML is at 76.4% (industry average ~74.8%) and employee cost is at ~13.7% (industry average of ~7%), both for the latest four quarters ending December 2011, thereby providing a lever on the expenditure front and scope to improve margins there on.

Exhibit 5: Employee cost as % of net sales



Source: Company Website, CRISIL Research

Company financials

Key assumptions

Following are the key assumptions made for forecasting the financials of the company.

Exhibit 6: Key assumptions

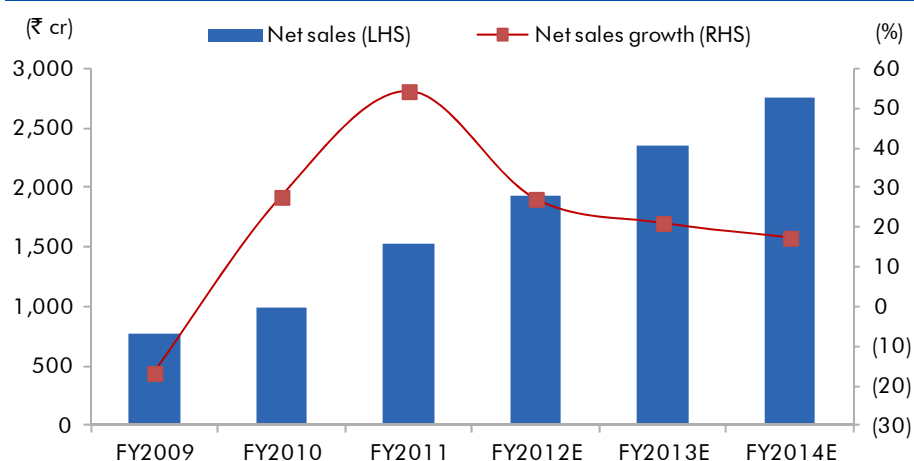
	FY2011	FY2012E	FY2013E	FY2014E
Finished goods volume growth % (yoy)				
On-road automobiles	30.3	25.0	22.0	18.0
Tractors – Agricultural	65.1	25.0	22.0	18.0

Source: Company Website, Angel Research

Net sales expected to post a 22% CAGR over FY2011-14E

With new developments in capacity and extended avenues (i.e., launch of SUV, Force One), we expect FML's sales to post a 22% CAGR over FY2011-14E to ₹2,753cr in FY2014E.

Exhibit 7: Net sales and net sales growth

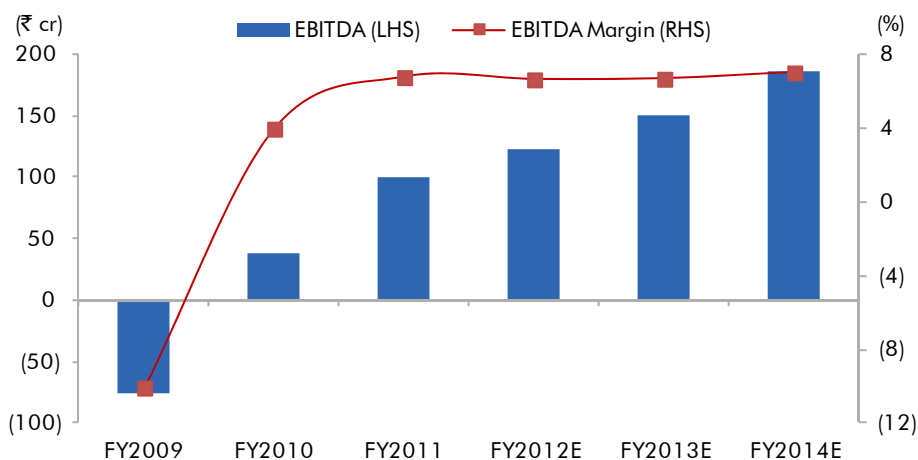


Source: Company Website, Angel Research

EBITDA to post a 23% CAGR over FY2011-14E

The company's EBITDA is expected to rise from ₹100cr in FY2011 to ₹186cr in FY2014E. EBITDA margin is expected to grow from 6.7% in FY2011 to 7.0% in FY2014E, mainly due to reduction in the raw-material cost and employee cost per head owing to increased capacity utilization.

Exhibit 8: EBITDA and EBITDA margin

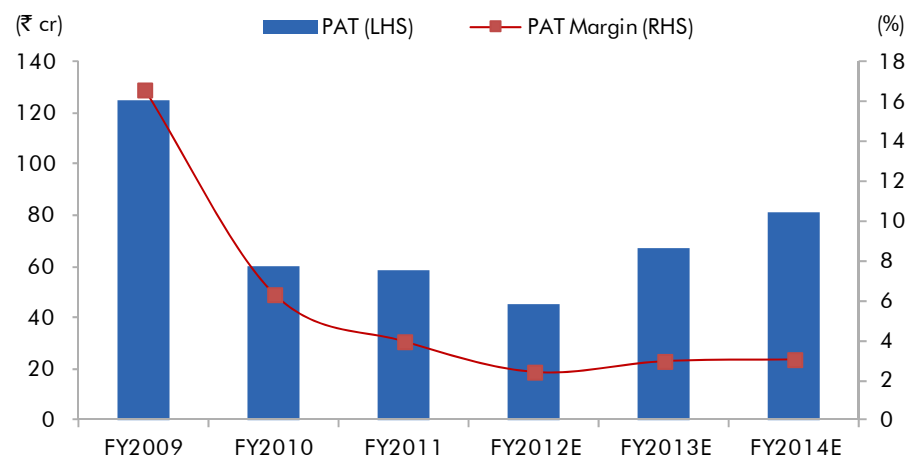


Source: Company Website, Angel Research

Net profit to post a 12% CAGR over FY2011-13E

We expect FML’s bottom line to report a 12% CAGR over FY2011-14E to ₹81cr on the back of remarkable top-line growth. Further, with huge cash surplus, the company is expected to either repay the debt on its books (which would reduce its interest expense) or use that money to earn substantial other income – which would reflect positively in its bottom line.

Exhibit 9: PAT and PAT growth

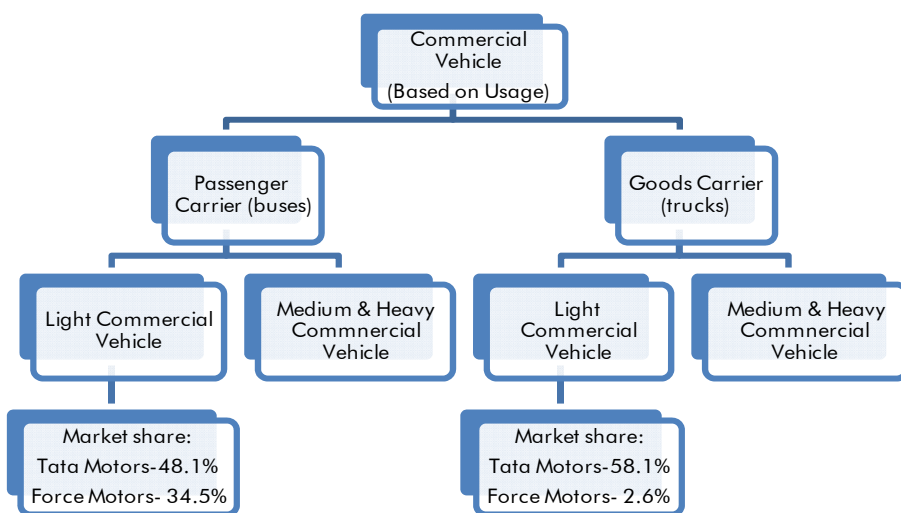


Source: Company Website, Angel Research

Commercial vehicle industry

The commercial vehicle industry in India can be broadly divided on the basis of usage in two segments: a) passenger carrier (buses) and b) goods carrier (trucks). Further, depending on the basis of gross vehicle weight, commercial vehicles are bifurcated as light commercial vehicles (LCV) and medium and heavy commercial vehicles (MHCV).

Exhibit 10: Commercial vehicle industry's structure



Source: CRISIL Research

The company

FML is an integrated automobile company manufacturing light commercial vehicles and tractors in India. The company has recently entered into SUV segment with launch of *Force One*. FML's five business segments are as follows:

Exhibit 11: Segments and products

Segments	Brands/ Products
SCV	Trump 15/ 40
LCV	Passenger Carrier: Traveller Smooth, Traveller Luxury, Traveller 3050WB/ 3350WB/ 3700WB. Traveller
	Goods Carrier: Tarveller Delivery Van, Traveller Shaktiman
	Special Purpose Vehicles: Traveller Ambulance, Traveller Scholar
MUV	Trax GAMA, Trax Cruiser, Trax Kargo King, Trax Gurkha
Tractors	Balwan, Orchard
SUV	Force One

Source: Company Website

FML operates two plants, as follows:

- Akurdi, Pune, Maharashtra: Produces three-wheelers like tractors.
- Pithampur, District Dhar, Madhya Pradesh: Produces four-wheeler LCVs like *Traveller* and *Trax*.

Competition

On the valuation front, FML seems to be fairly valued at 8.7x on PE basis, but the stock looks attractive on the P/BV and EV/EBITDA front at 0.5x and 3.3x, compared to peers' average of 2x and 4.6x, respectively.

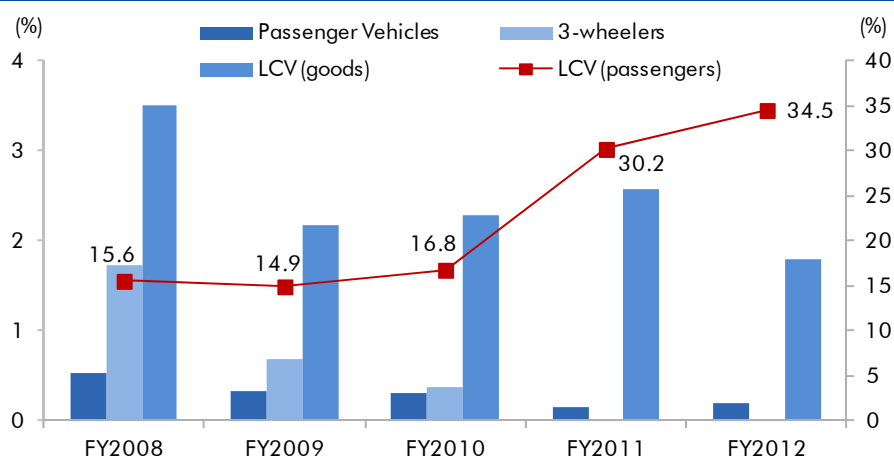
Exhibit 12: Peer comparison

FY2014E	Sales (₹ cr)	OPM (%)	PAT (₹ cr)	EPS (₹)	ROE (%)	P/E (x)	P/BV (x)	EV/EBITDA (x)
Force Motors	2,753	7.0	81	62	6.2	8.7	0.5	3.3
Tata Motors	208,773	14.2	14,801	45	32	6.9	1.9	4.1
Ashok Leyland	16,392	10.1	854	3	19	9.6	1.7	5.0
Eicher Motors	9,987	11.2	549	203	23	10.9	2.3	4.8

Source: Angel Research, Bloomberg

FML has been consistently raising its market share in the LCV segment for passenger carriers. The company has almost doubled its market share from mere 15.6% in FY2008 to ~34.5% in FY2012. While in other segments like commercial vehicle, utility vehicle and three-wheelers, the company has been losing its share over the years.

Exhibit 13: FML's market share



Source: SIAM

Risk factors

- Increasing competition in the auto industry.
- Cyclical nature of the industry.
- Rising raw-material prices.

Standalone Profit and Loss Account

Y/E March (₹ cr)	FY2009	FY2010	FY2011	FY2012E	FY2013E	FY2014E
Gross sales	867	1,076	1,693	2,116	2,582	3,046
Less: Excise duty	116	120	211	264	322	380
Net Sales	751	956	1,481	1,852	2,259	2,666
Other operating income	24	32	43	87	87	87
Total operating income	774	988	1,525	1,939	2,346	2,753
% chg	(16.8)	27.6	54.3	27.1	21.0	17.3
Net raw materials	598	678	1,017	1,297	1,587	1,871
% chg	(7.6)	13.3	50.1	27.6	22.3	17.9
Other Mfg costs	70	83	131	155	182	211
% chg	(29.5)	18.6	59.0	18.0	17.5	16.0
Personnel	120	125	197	252	294	329
% chg	(15.8)	4.1	57.1	28.0	16.8	12.0
Other	69	72	101	119	139	161
% chg	(23.3)	4.1	39.9	18.0	17.0	16.0
Pre-operative Exp. Capitalized	7	7	21	7	7	7
Total Expenditure	850	951	1,425	1,816	2,196	2,566
EBITDA	(76)	38	100	123	150	186
% chg	58.3	(149.9)	164.8	22.6	22.8	23.9
(% of Net Sales)	(10.1)	3.9	6.7	6.6	6.7	7.0
Depreciation & Amortisation	42	42	45	60	73	85
EBIT	(117)	(4)	55	63	78	101
% chg	35.3	(96.4)	(1,390.4)	14.1	23.9	29.7
(% of Net Sales)	(15.7)	(0.4)	3.7	3.4	3.4	3.8
Interest & other charges	35	17	23	35	26	23
Other Income	343	64	50	35	42	36
(% of Net Sales)	44	6	3	2	2	1
Recurring PBT	(153)	(21)	32	28	52	78
% chg	26.0	(86.2)	(250.2)	(12.4)	86.3	50.3
Extraordinary expense/(Inc.)	242	1	0	(811)	0	0
PBT (reported)	190	43	82	63	94	114
Tax	66	(18)	23	18	27	32
(% of PBT)	34.5	(41.4)	28.5	28.5	28.5	28.5
PAT (reported)	366	61	59	856	67	82
PAT after MI (reported)	366	61	59	856	67	82
ADJ. PAT	125	60	59	45	67	81
% chg	(248.9)	(51.5)	(3.0)	(23.3)	49.4	21.4
(% of Net Sales)	16.6	6.3	4.0	2.4	3.0	3.1
Basic EPS (₹)	95	46	44	34	51	62
Fully Diluted EPS (₹)	95	46	44	34	51	62
% chg	(248.9)	(51.5)	(3.0)	(23.3)	49.4	21.4
Dividend	-	4	7	7	7	7
Retained Earning	366	57	52	850	61	75

Standalone Balance Sheet

Y/E March (₹ cr)	FY2009	FY2010	FY2011	FY2012E	FY2013E	FY2014E
SOURCES OF FUNDS						
Equity Share Capital	13	13	13	13	13	13
Preference Capital	-	-	-	-	-	-
Reserves & Surplus	214	270	321	1,171	1,232	1,307
Shareholders' Funds	228	283	334	1,184	1,245	1,320
Minority Interest	-	-	-	-	-	-
Total Loans	161	148	250	250	175	150
Deferred Tax Liability	34	31	34	34	34	34
Total Liabilities	422	463	617	1,467	1,453	1,503
APPLICATION OF FUNDS						
Gross Block	901	938	1,089	1,389	1,689	1,989
Less: Acc. Depreciation	612	653	697	756	829	915
Net Block	289	284	393	633	860	1,075
Capital Work-in-Progress	20	12	14	14	14	14
Goodwill	47	47	47	47	47	47
Investments	57	57	57	-	-	-
Current Assets	407	434	584	1,435	1,319	1,261
Cash	17	26	15	677	429	241
Loans & Advances	71	65	97	120	147	172
Inventory	196	194	311	375	420	480
Debtors	123	150	161	263	323	367
Current liabilities	351	348	448	681	806	912
Net Current Assets	56	87	136	755	513	349
Deferred Tax Asset	-	23	18	18	18	18
Total Assets	422	463	617	1,467	1,453	1,503

Key ratios

Y/E March	FY2009	FY2010	FY2011	FY2012E	FY2013E	FY2014E
Valuation Ratio (x)						
P/E (on FDEPS)	5.7	11.8	12.1	15.8	10.6	8.7
P/CEPS	4.3	6.9	6.9	6.8	5.1	4.3
P/BV	3.1	2.5	2.1	0.6	0.6	0.5
Dividend yield (%)	-	0.6	0.9	0.9	0.9	0.9
EV/Sales	1.1	0.8	0.6	0.2	0.2	0.2
EV/EBITDA	(10.5)	20.5	8.9	2.3	3.0	3.3
EV / Total Assets	1.9	1.7	1.4	0.2	0.3	0.4
Per Share Data (₹)						
EPS (Basic)	94.5	45.9	44.5	34.1	50.9	61.9
EPS (fully diluted)	94.5	45.9	44.5	34.1	50.9	61.9
Cash EPS	126.3	77.7	78.5	79.4	106.0	126.7
DPS	-	3.0	5.0	5.0	5.0	5.0
Book Value	172.7	215.0	253.7	898.6	944.7	1,001.7
DuPont Analysis						
EBIT margin	(15.7)	(0.4)	3.7	3.4	3.4	3.8
Tax retention ratio	0.7	1.4	0.7	0.7	0.7	0.7
Asset turnover (x)	2.7	3.0	3.1	2.5	2.3	2.2
ROIC (Post-tax)	(27.3)	(1.9)	8.1	6.2	5.8	6.0
Cost of Debt (Post Tax)	14.4	16.2	6.7	10.0	10.7	11.0
Leverage (x)	0.4	0.2	0.5	(0.4)	(0.2)	(0.1)
Operating ROE	(43.3)	(6.0)	8.9	7.6	6.8	6.4
Returns (%)						
ROCE (Pre-tax)	(27.8)	(0.9)	8.9	4.3	5.4	6.7
Angel ROIC (Pre-tax)	(41.7)	(1.3)	11.4	8.6	8.1	8.4
ROE	54.7	21.3	17.5	3.8	5.4	6.2
Turnover ratios (x)						
Asset Turnover	0.8	1.0	1.4	1.3	1.3	1.3
Inventory / Sales (days)	95	74	77	74	68	66
Receivables (days)	60	57	40	52	52	50
Payables (days)	151	134	115	137	134	130
WC cycle (ex-cash) (days)	19	23	30	15	14	15
Solvency ratios (x)						
Net debt to equity	0.4	0.2	0.5	(0.4)	(0.2)	(0.1)
Net debt to EBITDA	(1.2)	1.7	1.8	(3.5)	(1.7)	(0.5)
Int. Coverage (EBIT / Int.)	(3.3)	(0.3)	2.4	1.8	3.0	4.4

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Disclosure of Interest Statement	Force Motors
1. Analyst ownership of the stock	No
2. Angel and its Group companies ownership of the stock	No
3. Angel and its Group companies' Directors ownership of the stock	No
4. Broking relationship with company covered	No

Note: We have not considered any Exposure below ₹ 1 lakh for Angel, its Group companies and Directors

Ratings (Returns):	Buy (> 15%) Reduce (-5% to 15%)	Accumulate (5% to 15%) Sell (< -15%)	Neutral (-5 to 5%)
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