AMSEC Raising the bar

Asian Markets Securities Pvt. Ltd.

Institutional Research

CMP (₹)	**701**
Target (₹)	**922**

Nifty: 8,105 Sensex: 27,061

Key Stock Data	
BSE Code	500250
NSE Code	LGBROSLTD
Bloomberg	LGBB IN
Shares O/s mn (FV ₹10)	15.6
Market cap (₹bn)	11.1
52-week high/low	720/81
3-m daily avg vol.	80,804

Rel. Performance

(%)	1m	3m	12m
LGBB	50.0	86.9	775.1
NIFTY	6.0	6.0	36.7
SENSEX	5.8	6.0	35.0

Shareholding Pattern

(%)	Jun14	Mar14	Dec13
Promoter	46.5	45.7	45.7
FII	0.0	0.0	7.0
DII	6.8	5.3	0.0
Others	46.7	49.0	47.3

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L.G. Balakrishnan & Bros Ltd

Buy

The best play on the two-wheeler growth story

Set up in 1937, L.G. Balakrishnan & Bros Ltd (LGBL) is the largest automobile chain manufacturer in India with ~70% market share in the two-wheeler OEM and ~50% market share in the replacement segment. Automotive chains (under the brand 'Rolon') contribute ~70% to consol revenues, making LGBL the prime beneficiary of the two-wheeler industry revival. Metal forming division benefiting from broad based auto sector recovery coupled with steady growth in GFM will further aid revenue growth. Despite 20% capacity expansion (over FY15-17) we expect utilization to improve to 60% from 55% currently which will aid margin expansion (188bp over FY14-17) translating in PAT CAGR of 22%. With strong cash flow, healthy return ratios and excellent growth prospects, we expect the stock to get re-rated. We initiate with a BUY rating

A proxy to the two-wheeler growth story: With ~70% revenues coming from automotive chains business there is a strong correlation between motorcycle volume growth and sales growth of LGBL. With 70% market share in two-wheeler OEM and 50% in the replacement market, LGBL is best placed to benefit from a recovery in motorcycle volume growth backed by economic recovery and export push by most OEMS. We expect consol revenues to grow at 13% CAGR over FY14-17 driven primarily by the transmission segment (16% CAGR).

Metal Forming segment to benefit from broad based auto sector recovery: The metal forming business (14% revenues) concentrates on hot, warm & cold forging, fine blanking & precision machined parts etc where LGBL supplies components to two and four wheeler players in the domestic market, either directly or through a Tier I supplier. With broad based auto sector recovery we expect this segment to also do well.

GFM acquisition: Joker in the pack: LBGL had acquired GFM (produces metal stamping products for seating applications for leading 4W OEMs in USA) in 2012 to get access to their technology "Grip Flow Method" (considered superior to fine blanking). LGBL plans to leverage on GFM's supplier status with USA OEMs and introduce its products in India which can become a significant revenue contributor in the future.

Higher capacity utilisation to aid margin expansion The company is expanding its automotive chains capacity by 20% (10mn chains) in Jalna, Maharashtra over FY15-17 which will help in saving significant logistics and sourcing costs (~100-200bp EBITDA margin accretive). Also, despite increased capacity (20%), utilization increase form current 55% to 60% in FY17 which will aid margin expansion (we build 188bp margin expansion over FY14-17)

Strong cash flows and return ratios are compelling: LBGL will generate robust average annual CFO (₹1.1bn) and with FY15-17 capex pegged at ₹2bn it will generate average annual FCF to the tune of ₹400mn. We expect net debt to equity to reduce to 0.1x by FY17 from the current 0.5x. LGBL will generate strong return ratios (average ROEs of 21.5% and ROCE of 24.5%) in FY14-17 while maintain its 20% dividend payouts.

Our target price of ₹922 is based on 13x FY17 EEPS of ₹70.9. With strong cash flow, healthy return ratios and excellent growth prospects, we expect the stock to get re-rated. At CMP the stock trades at 11.8x FY16E and 10x FY17E EPS which is cheap considering the strong return ratios and earnings growth visibility. Initiate with a Buy rating.

Exhibit 1: Key Financials (Consolidated)

Y/E Mar (₹mn)	FY14	FY15E	FY16E	FY17E
Sales	10,383	11,669	13,293	15,218
yoy (%)	*15.1*	*12.4*	*13.9*	*14.5*
Operating Profit	1,261	1,500	1,772	2,168
yoy (%)	*41.2*	*18.9*	*18.1*	*22.3*
PAT	619	765	943	1,113
yoy (%)	*89.2*	*23.5*	*23.3*	*18.0*
Equity	157	157	157	157
EPS (₹)	39.4	48.7	60.1	70.9

Source: Company, AMSEC Research

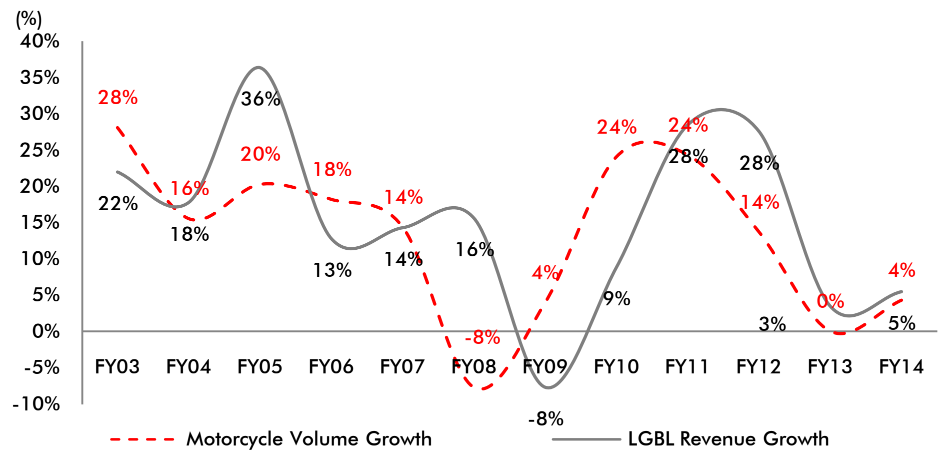
Exhibit 2: Key Indicators

Y/E Mar	FY14	FY15E	FY16E	FY17E
OPM (%)	11.4	12.0	12.5	13.3
NPM (%)	5.6	6.1	6.6	6.8
PER (x)	18.0	14.6	11.8	10.0
P/BV (x)	3.6	3.0	2.4	2.0
EV/Sales (x)	1.2	1.1	0.9	0.8
EV/ EBITDA (x)	10.0	8.2	6.9	5.5
RoACE (%)	21.3	23.2	24.2	26.1
RoANW (%)	21.8	22.4	22.6	22.0

Transmission business a proxy to the motorcycle growth

LGBL has a strong brand - 'ROLON' in the automotive chains segment which contributes nearly ~68% to the company's consol revenue. In automotive chains, the company commands a ~70% market share in the OEM segment and around ~50% market share in the replacement segment. The company also has part of its replacement revenues come through OEM. Thus the OEM: Replacement revenue mix stands at 60%:40%. There is a strong correlation between motorcycle volume growth and sales growth of LGBL. We expect this trend to continue going forward. Thus, in our view, LGBL is best placed to benefit from a recovery in motorcycle volume growth on back of economic recovery and export push by most OEMS.

Exhibit 3: LBGL revenue growth has a strong correlation with motorcycle volume growth

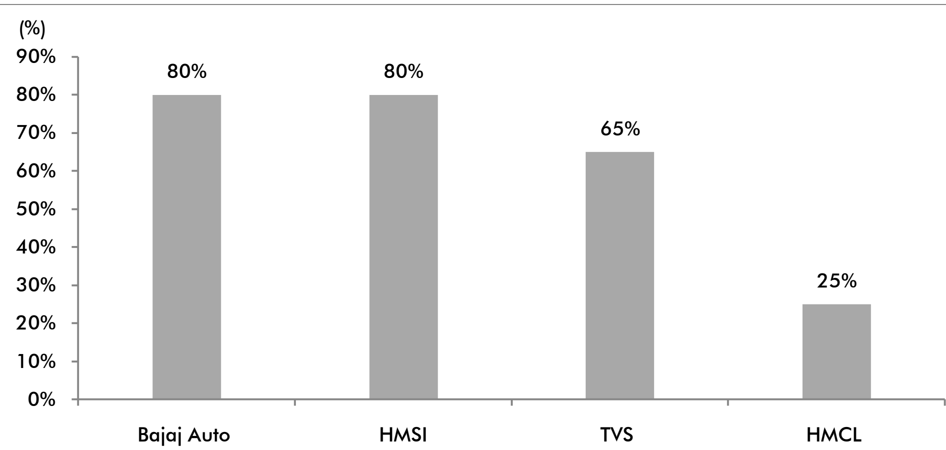


Source: Company, SIAM, AMSEC Research

Capacity Expansion by Major 2W OEMs bodes well for the transmission business revenue growth

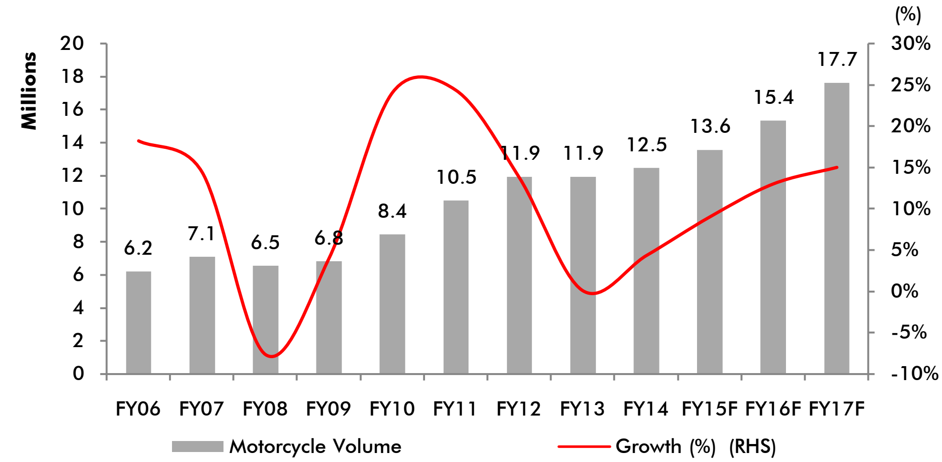
LGBL caters to 80% of Bajaj Auto and HMSI, 65% of TVS motors and 25% of Hero Motocorp requirements which translates into 70% OEM market share. With many major two-wheeler OEMs increasing their capacity and also entering into new geographies, would help drive the industry's growth going forward. We are factoring a 12.5% CAGR Motorcycle Volume growth FY14-17 which is in line with (FY00-FY14 CAGR of 13%).

Exhibit 4: OEM wallet share translates into 70% OEM market share



Source: Company, AMSEC Research

Exhibit 5: Motorcycle volume growth to pick up going ahead (12.5% CAGR over FY14-17)



Source: SIAM, AMSEC Research

Exhibit 6 : Upcoming Capacity Expansion plans of clients

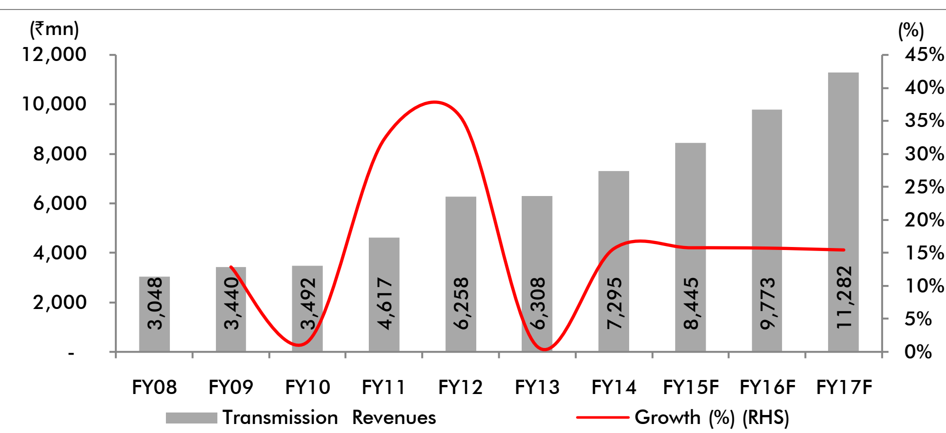
(Units)	Current Capacity	Expected Capacity	Total Capacity	Entry in new markets
Bajaj Auto	5.8mn	0.2mn	6.0mn	Argentina, Turkey Afghanistan, Lebanon, Guinea, Togo, Mali, Burkina Faso and Liberia
Hero MotoCorp	7.7mn	Gujarat - 1.8mn	9.5mn	Asia, Africa and South America
Honda Motorcycle and Scooter India	4.6mn	Gujarat - 1.2mn	5.8mn	Latin Americans and Africa
Yamaha Motor	1mn	Chennai - 1.8mn	2.8mn	US and Japan

Source: Company, AMSEC Research

Aftermarket a lucrative segment

On an average motorcycle chain needs to be replaced at 40,000Kms (average life of 3 years). LGBL makes healthy 15-16% EBITDA margins in the replacement segment since its products are priced higher than competition (5% higher than Tube Investments diamond chains and 10-15% higher than chains manufactured by unorganized players). LGBL has 50% market share in the organized replacement segment (~75% of total replacement market).The rest is controlled by Tube investments. Also some amount of replacement revenue is driven through OEMs.

Exhibit 7: Transmission segment revenue to grow 16% CAGR over FY14-17



Source: Company, AMSEC Research

4-wheeler Engine timing chains – an opportunity yet to be tapped

Small proportion of its transmission revenue (5%) also comes from products like timing B belts, vari speed belts, cogged belts, poly v belts etc which it supplies to LCVs, cars/jeeps, three-wheelers, trucks and tractors.

Timing belts and timing chains are the devices that make the connection between the crankshaft and camshaft(s) in the engine. Globally most 4Ws have a timing chain in their engines which is yet to catch up in India where OEMs prefer the belt. Timing chains have benefits over the timing belt which makes us believe that the shift to timing chains by Indian OEMs will happen sooner or later which will benefit LGBL since it is the leader in automobile chain manufacturing

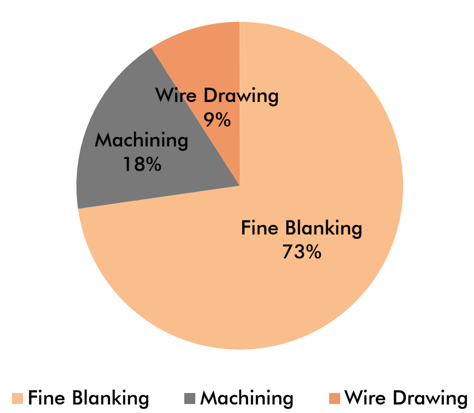
Automotive timing belts are made of rubber, often with fiberglass or Kevlar woven into them for extra strength. They are known to be very quiet as they rotate, but they do wear out over time. Most vehicle manufacturers recommend that timing belts are changed between 60,000 and 100,000 miles, though there are exceptions, both higher and lower. Timing chains on the other hand looks just like the chain on a bicycle, but much cleaner. The beauty of the timing chain is that it typically lasts a very long time. Some car manufacturers recommend replacing it at certain mileage or time intervals, while others claim that the chain is good for the life of the automobile. It really depends on the make and model of the car or truck

Metal forming segment to continue its strong performance:

Metal forming segment comprises 14% of its FY14 consol revenues. LGBL metal forming business concentrates on hot, warm & cold forging, fine blanking & precision machined parts etc. In the fine blanking segment, LGBL supplies components to two and four wheeler players in the domestic market, either directly or through a Tier I supplier. LGBL also exports its components to marquee customers including Schneider and Inteva.

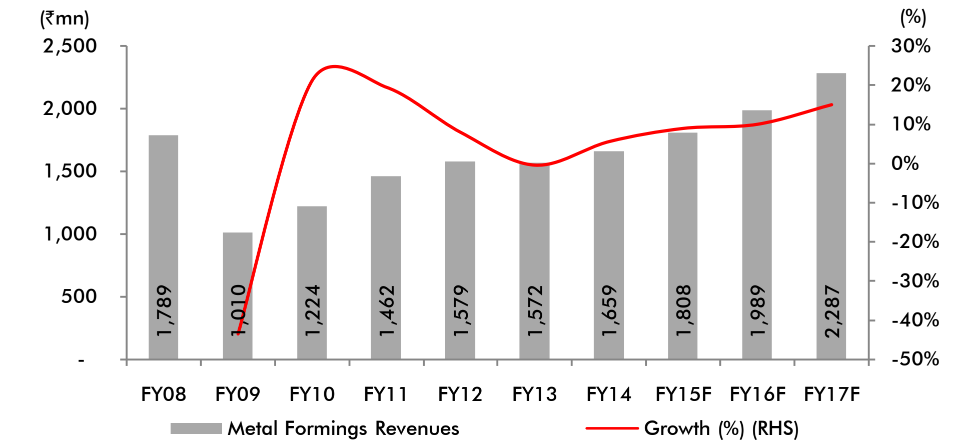
Fine blanking is the major contributor to the Metal forming revenues (73%) where LGBL caters to 80+ clients. Machining business caters exclusively to BOSCH's CRDi fuel injection system where LGBL is a sole supplier of one of the parts. Wire drawing is another business for the metal forming segment. With automotive growth to recover going ahead we believe the metals forming business will continue to do well.

Exhibit 8: Revenue mix Metal forming



Source: Company, AMSEC Research

Exhibit 9: Metals Forming revenue to grow 12% CAGR over FY14-17



Source: Company, AMSEC Research

LCV Business - the only headwind

LGBL has an exclusive LCV dealership for Tata Motors with 20 outlets across Coimbatore, Erode and Tripur districts. With the decline in LCV volumes, the segment reported revenue decline of 38% yoy at ₹ 925mn and EBIT loss of ₹ 38mn in FY14. Management wants to rationalize the dealership count to 13. With the cyclical downturn in the LCV business to continue, through the entire of FY15 and only possibly reviving from FY16. Accordingly, we believe LGB's dealership business would remain under stress till we see meaningful demand recovery.

GFM (Grip Flow Method) Acquisition – Joker in the pack

In 2012, LGBL acquired a USA based fine blanking company GFM (Grip Flow method) for $5.5mn. GFM is held through LGB USA Inc (LGBL has 74.2% holding), which in turn owns 90.9% of GFM Acquisition LLC, which is a holding company of GFM LLC. This translates into 66.7% holding in GFM for LBGL.

GFM's core competency includes precision metal stamping techniques with other managed services including heat-treatment, finishing, molding, welding and light subassembly. It's product applications primarily caters to automotive seat mechanisms, brakes and window regulators. Its FY14 revenues are $18m with a PAT of $1.8m. LBGL has acquired this company to get access to this technology and leverage on GFM's supplier status with USA OEMs and introduce the products in India.

GFM a better technology than Fine blanking

Grip Flow Method is a different technology to Fine blanking which allows GFM to produces parts with the characteristics of fine blanking at a lower cost. Gripflow leverages the merits of conventional stamping and fine blanking processes to derive an economical alternative yet high-quality product. It has many benefits over the conventional fine blanking namely.

1) Gripflow tooling is less than fine blanking dies due to the elimination of the V-ring.
2) Gripflow unit prices are typically less than fine blanking as a result of greater material utilization and tonnage efficiency.
3) Gripflow tooling is significantly less than conventional stamping with progressive stations. With multiple operations performed in a single-station die.

We are building a 7.5% CAGR Revenue translating into 11% PAT CAGR for GFM over FY14-17. We are not factoring any exports from GFM to India in our numbers.

Renold India – Industrial chains JV with Renold PLC

In September 2008, Renold plc and LGBL formed a new Joint Venture company, Renold Chain India Pvt Ltd ("Renold India") where LGBL has a 25% stake. Renold plc is headquartered in the UK, and has been a leading global supplier of all types of industrial chain since it invented the bush roller chain in 1880. The JV has 50% of its revenues exported to Europe. We expect 14% earnings CAGR over FY14-17E for Renold India on back of economic recovery in the domestic markets and continued demand from Europe.

Consolidated revenue CAGR pegged at 13% in FY14-17E

In FY14-17E, we are factoring in a 13% CAGR in revenue growth on the back of transmission segment growing by 16% CAGR (proxy to motorcycle volume growth of 12.5% CAGR and robust replacement market sales), Metals forming revenues will grow by 12% CAGR. The LCV distribution business will have a tepid 2% CAGR (management wants to reduce the number of distribution points from 20 to 13). We are conservative on our GFM revenue estimates (8% CAGR in FY14-17) and are not building any revenues for its product exports to India while we factor 14% CAGR revenue growth for its industrial chains JV entity Renold India. Thus consol revenues will grow by 13% CAGR.

Exhibit 10: Standalone Revenue Trend

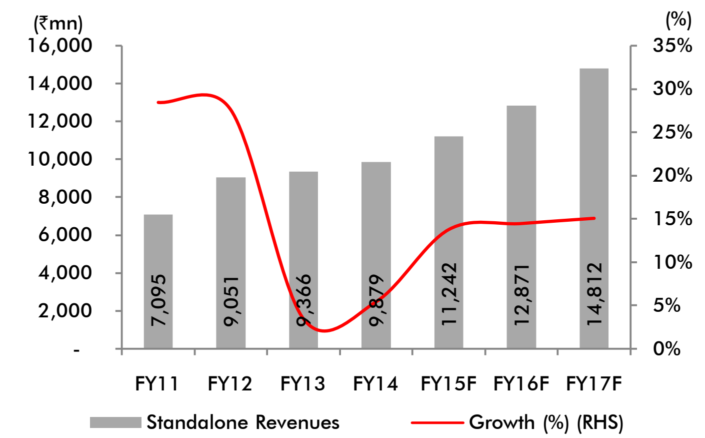


Exhibit 11: GFM Revenue Trend (66.7% holding)

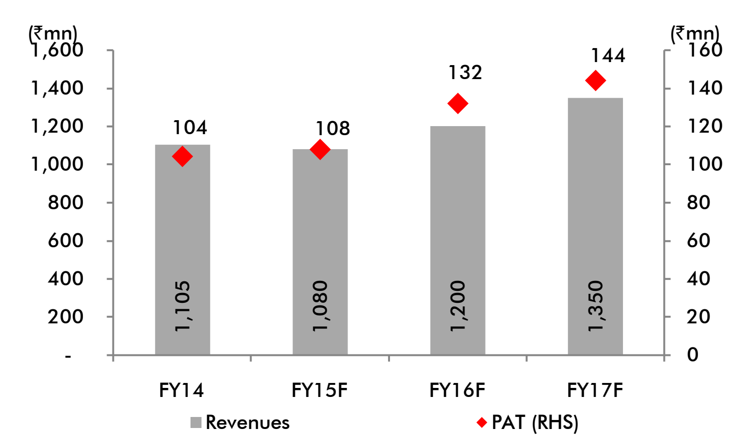


Exhibit 12: Renold India Revenue Trend (25% holding)

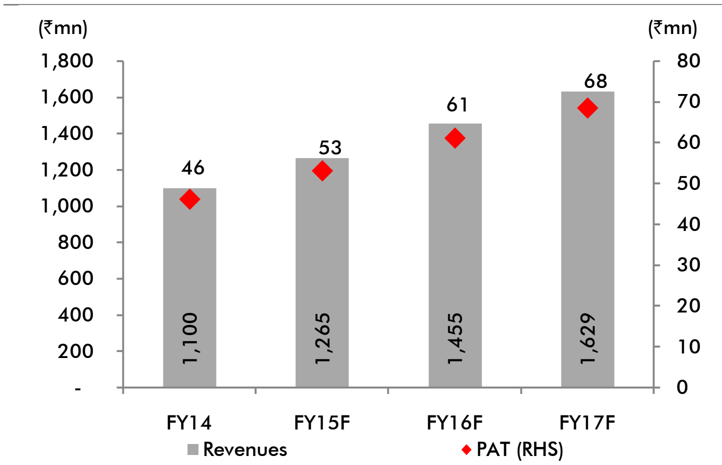
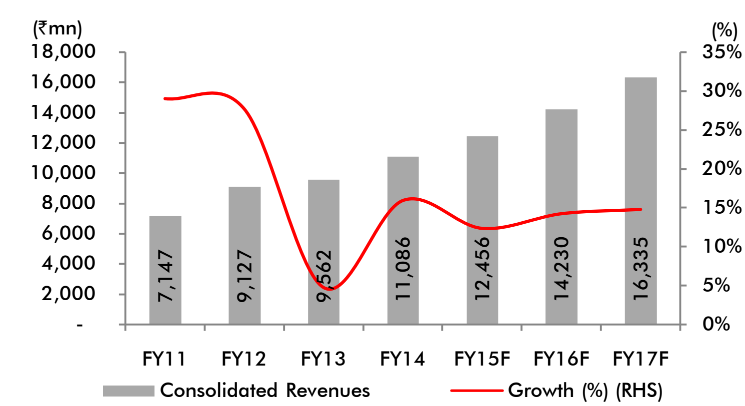


Exhibit 13: Consolidate Revenue Trend



Source: Company, AMSEC Research

Margin expansion to be aided by operating leverage benefits

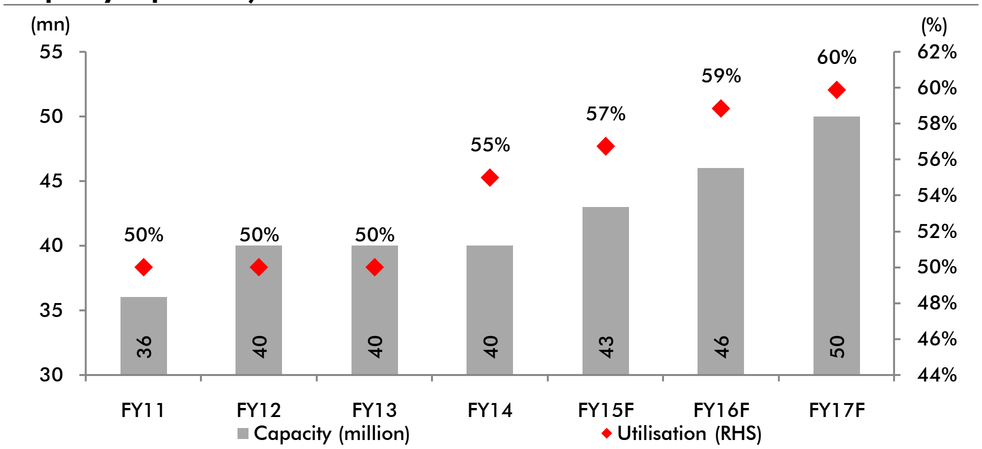
Currently the company operates at 55% utilization which can be improved to around 60% by FY17 despite a capacity expansion of 20% (10mn automotive chains at Jalna Plant) which will lead to operating leverage benefits aiding margin expansion.

Capacity expansion at Maharashtra (Jalna Plant) to aid margins

Current annual capacity is pegged at 40mn chains and 80mn sprocket and LGBL is setting up a 10mn chain and 20mn sprocket capacity plant in Jalna Maharashtra at the cost of ₹1.5bn which will be commissioned in phases over FY15-17.

The plant will help reduce sourcing costs and improve margins by at least 100bps once fully commissioned. Under a special scheme, Maharashtra government will refund 70% of the ₹1.5bn capital costs by the way of a VAT refund over 7 years which will start flowing in from FY17 onwards. We build a margin expansion of 188bp over FY14-17

Exhibit 14: Capacity utilization to improve to 60% by FY17 (despite 20% capacity expansion)



Source: Company, AMSEC Research

Exhibit 15: Operating leverage benefits to improve EBITDA margins by 188bp over FY14-17

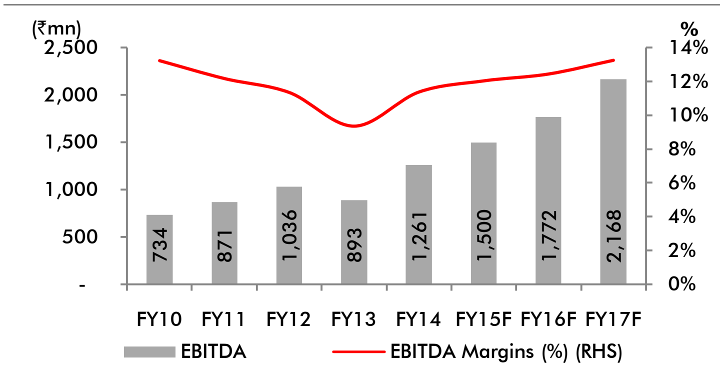
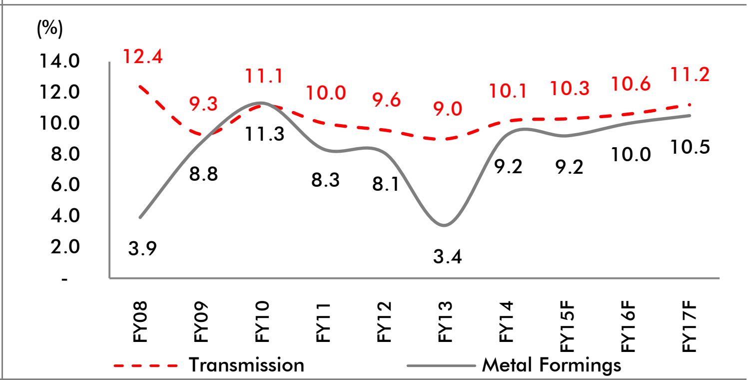


Exhibit 16: Segment EBIT trend

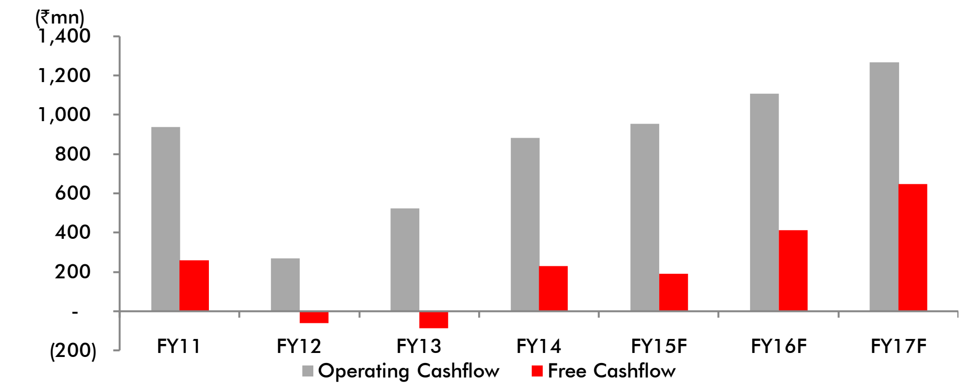


Source: Company, AMSEC Research

Strong Cash flows and High return ratios are compelling

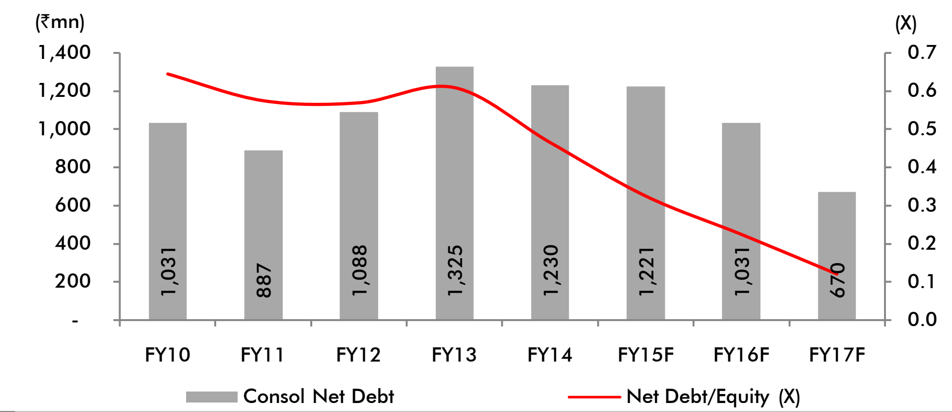
The company has a history of strong Cash flow generation. LGBL will generate ~₹1.1bn annual operating cash flow. After factoring in capex of ₹2bn over FY15-17 the company will generate average free cash of ₹400mn. The Net-debt to Equity will come down from 0.5x in FY14 to 0.1x in FY17. Company will maintain average ROEs of 21.5% and ROCE of 24.5% in FY14-17.

Exhibit 17: Strong Operating Cash and Free Cash flow generation



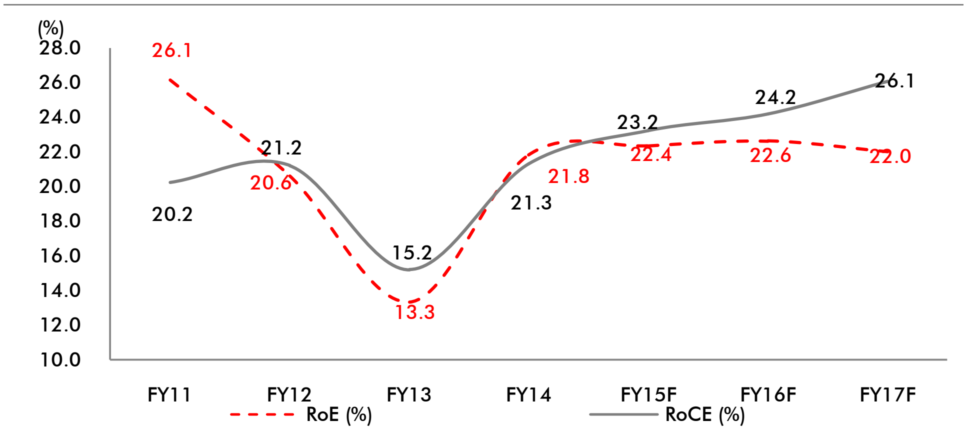
Source: Company, AMSEC Research

Exhibit 18: Net-debt to Equity to reduce substantially going ahead



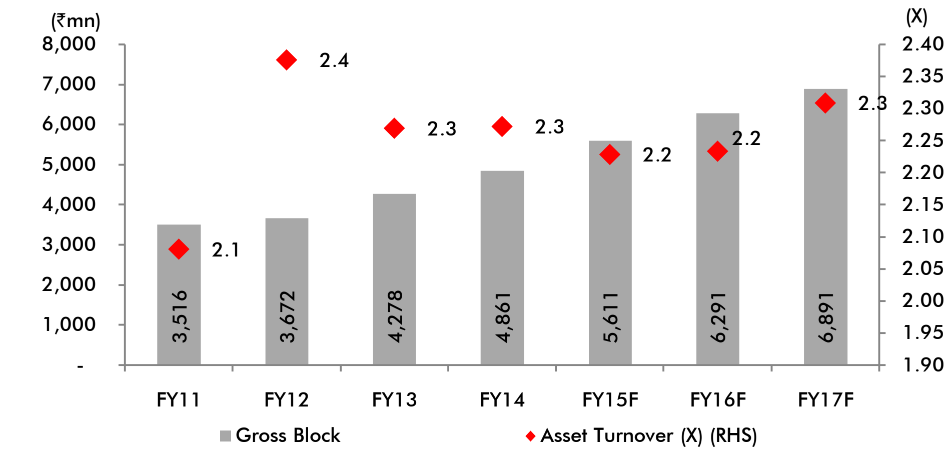
Source: Company, AMSEC Research

Exhibit 19: Strong return ratios over FY14-17 is compelling



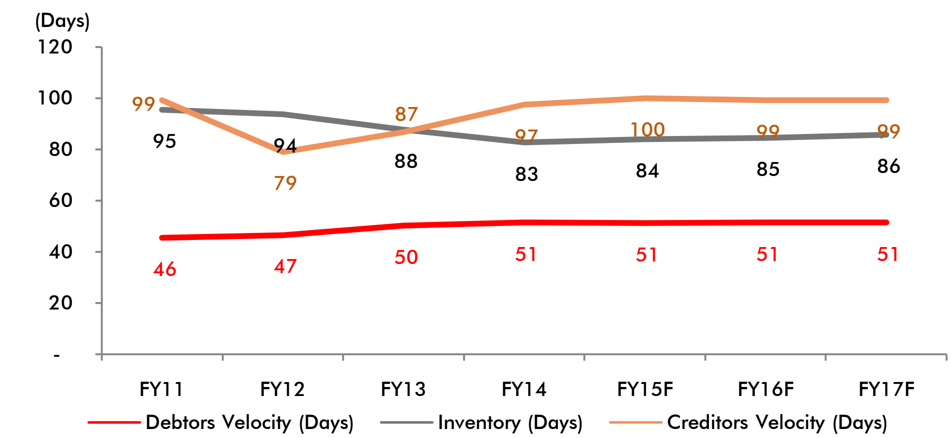
Source: Company, AMSEC Research

Exhibit 20: LGBL will maintain strong asset turns



Source: Company, AMSEC Research

Exhibit 21: Working Capital Trend



Source: Company, AMSEC Research

Company Snapshot

Snapshot (Rsm)	FY04	FY05	FY06	FY07	FY08	FY09	FY10	FY11	FY12	FY13	FY14
Sales	2,706	3,689	4,161	4,756	5,499	5,076	5,540	6,743	8,540	9,021	10,383
EBIDTA	392	510	575	735	721	543	734	871	1,036	893	1,261
PAT	136	165	136	230	149	391	244	466	442	326	619
Cash Flow from Operations	220	371	297	279	715	963	287	936	268	522	881
Net Worth	753	852	957	1,355	1,448	1,416	1,597	1,969	2,325	2,584	3,089
Debt	498	1,190	1,761	3,000	2,366	1,515	1,077	936	1,144	1,428	1,295
Gross Block	1,516	1,992	2,824	3,333	3,870	2,802	2,965	3,516	3,672	4,278	4,861
Cash & Current Investments	20	112	102	1,067	53	376	46	49	55	107	65
Key Ratios	**FY04**	**FY05**	**FY06**	**FY07**	**FY08**	**FY09**	**FY10**	**FY11**	**FY12**	**FY13**	**FY14**
EPS	8.7	10.5	8.6	13.6	9.5	24.9	15.5	29.7	28.2	20.9	39.4
ROE%	18.1	19.4	14.2	17.0	10.6	27.3	30.5	26.1	20.6	13.3	21.8
ROCE%	19.4	11.7	6.7	7.0	10.7	11.0	38.8	20.2	21.2	15.2	21.3
Debt Equity	0.8	1.2	1.8	2.2	1.6	1.1	0.7	0.6	0.6	0.6	0.5
Asset Turn (x)	2.1	2.4	2.0	1.8	1.5	1.5	3.7	2.1	2.4	2.3	2.3
WC Days	79	78	92	179	103	102	86	67	74	78	66
Dividend Payout %	17.7	42.1	17.8	18.9	21.6	64.8	24.0	19.9	23.1	20.3	20.3
Cost Matrix	**FY04**	**FY05**	**FY06**	**FY07**	**FY08**	**FY09**	**FY10**	**FY11**	**FY12**	**FY13**	**FY14**
RM/Sales%	48.7	53.9	50.0	52.6	51.3	51.4	50.9	57.7	60.7	55.6	52.9
Employee cost/Sales%	8.2	6.6	7.0	8.0	8.3	8.9	8.2	9.8	10.3	11.1	12.9
Power & Fuel/Sales%	3.7	3.9	4.1	4.2	4.3	3.4	3.0	3.7	3.8	4.1	4.1
Gross Margin%	43.2	39.5	43.1	39.4	40.3	39.6	40.9	35.7	33.1	32.3	34.6
EBIDTAM%	14.5	13.8	13.8	15.5	13.1	10.7	13.2	12.9	12.1	9.9	12.1
PATM%	5.0	4.5	3.3	4.8	2.7	1.7	4.4	6.5	4.8	3.4	5.6
Segment			**FY06**	**FY07**	**FY08**	**FY09**	**FY10**	**FY11**	**FY12**	**FY13**	**FY14**
Revenues											
Transmission			2,853	2,897	3,048	3,440	3,492	4,617	6,258	6,308	7,295
Metal Forming			1,550	1,569	1,789	1,010	1,224	1,462	1,579	1,572	1,659
Others			328	398	692	626	807	1,015	1,214	1,486	925
EBIT											
Transmission			342	427	377	320	389	463	599	567	739
Metal Forming			44	53	70	88	138	122	128	54	153
Others			32	112	14	(17)	46	40	29	26	(38)
EBIT - Margins											
Transmission			12.0	14.7	12.4	9.3	11.1	10.0	9.6	9.0	10.1
Metal Forming			2.8	3.3	3.9	8.8	11.3	8.3	8.1	3.4	9.2
Others			9.7	28.2	2.0	(2.8)	5.7	4.0	2.4	1.7	(4.1)

Source: Company, AMSEC Research

Over the last decade the company had a revenue growth of 14.5% CAGR which has translated into a PAT CAGR of 16.4%. Its 10 year average EBITDA margins stand at 13%. It has maintained strong return ratios (20% average RoE over the last decade) backed by strong cash flow generation and high asset turns (2.2x). It has maintained dividend payout ratio of 20%.

In FY09 LGBL sold off its industrial chains business to Renold PLC and formed a JV Renolds India Private Limited with a 25% stake. As per the arrangement LGBL transferred its Industrial Chain Divisions including the manufacturing plant at Dindigul District to Renold Chain India Private Limited for a consideration of Rs575mn. The net profit of Rs. 306mn due to this sale is reflected in the exceptional item for the year.

Exhibit 22: Quarterly Financials

Y/E March (₹mn)	2QFY13	3QFY13	4QFY13	1QFY14	2QFY14	3QFY14	4QFY14	1QFY15	yoy (%)	qoq (%)
Net sales	2,207	2,308	2,282	2,093	2,343	2,406	2,408	2,332	*11.4*	*(3.2)*
Other operating income	145	114	144	141	153	139	197	172	*22.2*	*(12.7)*
Total income	2,352	2,422	2,426	2,233	2,496	2,545	2,605	2,504	*12.1*	*(3.9)*
Consumption of raw materials	1,265	1,300	1,285	1,113	1,246	1,234	1,239	1,174	*5.5*	*(5.2)*
Employee cost	240	248	256	248	264	315	324	306	*23.6*	*(5.5)*
Other expenditure	593	641	682	641	683	694	757	711	*10.9*	*(6.0)*
Total expenditure	2,098	2,189	2,224	2,002	2,192	2,244	2,321	2,192	*9.5*	*(5.5)*
EBITDA	254	233	202	231	304	301	284	312	*34.9*	*9.7*
add: Other income	7	(1)	28	3	5	35	4	12	*304.1*	*179.7*
Interest	70	52	49	48	43	39	39	44	*(8.6)*	*11.2*
Depreciation	71	74	75	75	78	79	82	95	*26.0*	*16.0*
Profit before tax	120	105	106	111	189	218	167	185	*66.8*	*10.5*
Provision for taxation	29	21	16	23	42	48	29	32	*41.4*	*8.4*
Reported PAT	**91**	**84**	**90**	**88**	**147**	**170**	**138**	**153**	*73.3*	*11.0*
Segment Revenues										
Transmission	1,550	1,655	1,683	1,588	1,806	1,909	1,992	1,905	*19.9*	*(4.4)*
Metal Forming	411	359	386	360	420	419	461	446	*23.9*	*(3.3)*
Segment EBIT										
Transmission	147	176	130	159	214	196	171	198	*24.8*	*16.0*
Metal Forming	11	1	10	38	42	48	25	54	*42.9*	*116.6*
Segment EBIT Margins										
Transmission	9.5	10.7	7.7	10.0	11.9	10.3	8.6	10.4	*41bp*	*183bp*
Metal Forming	2.8	0.3	2.6	10.6	10.0	11.4	5.4	12.2	*162bp*	*676bp*
Equity capital (FV ₹10)	157.0	157.0	157.0	157.0	157.0	157.0	157.0	157.0		
Basic EPS (in ₹)	5.8	5.4	5.7	5.6	9.4	10.8	8.8	9.8	*73.3*	*11.0*
Gross Profit/ Net sales (%)	*39.9*	*41.6*	*40.6*	*43.8*	*43.9*	*45.4*	*44.8*	*46.0*	*220bp*	*122bp*
EBITDA/ Net sales (%)	*10.8*	*9.6*	*8.3*	*10.4*	*12.2*	*11.8*	*10.9*	*12.5*	*233bp*	*157bp*
PAT/ Total income (%)	*3.9*	*3.5*	*3.7*	*3.9*	*5.9*	*6.6*	*5.3*	*6.1*	*213bp*	*80bp*
Tax / PBT (%)	*24.3*	*20.1*	*15.3*	*20.3*	*22.3*	*21.9*	*17.6*	*17.2*	*(310bp)*	*(34bp)*
Raw Material / Net sales (%)	*57.3*	*56.3*	*56.3*	*53.2*	*53.2*	*51.3*	*51.5*	*50.4*	*(282bp)*	*(110bp)*

Source: Company, AMSEC Research

1Q performance aided by higher other operating income and lower taxes:

In, 1QFY15 LGBL reported net sales of Rs2.5bn up 12.1% yoy on back of higher operating income (up 22% yoy due to higher scrap sales in 1Q which will normalize over the year). This led to higher EBITDA margins of 12.5% (+233bp yoy, +157bp qoq) which coupled with lower taxes led to PAT of Rs153mn.

Quarterly trend

Exhibit 23: Revenue trend

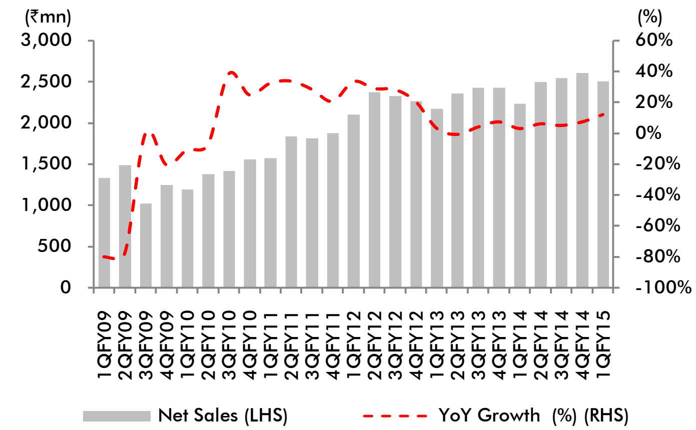


Exhibit 24: EBITDA trend

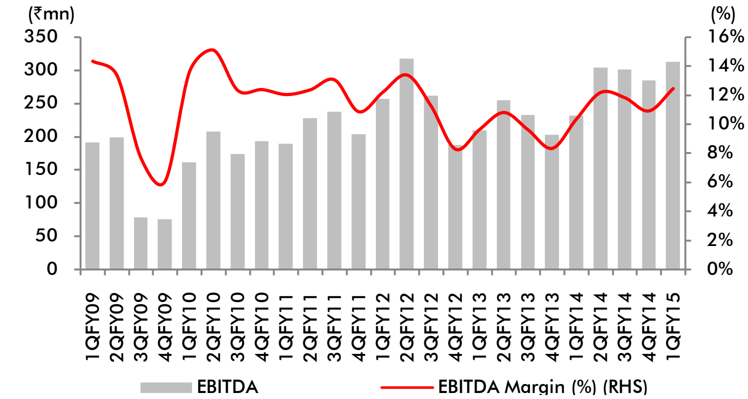


Exhibit 25: PAT trend

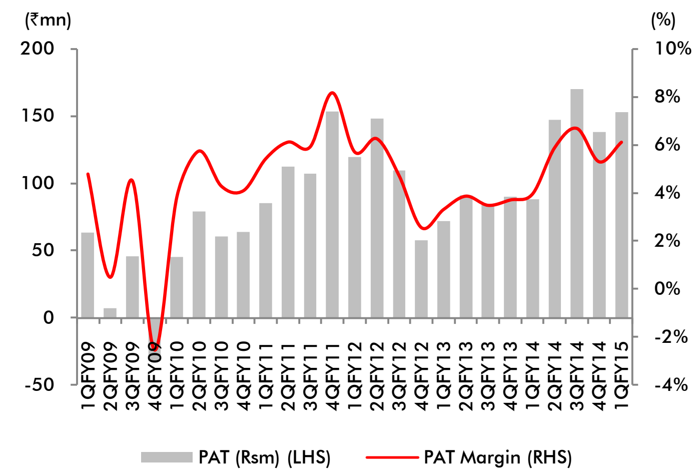


Exhibit 26: Segment Revenue Trend

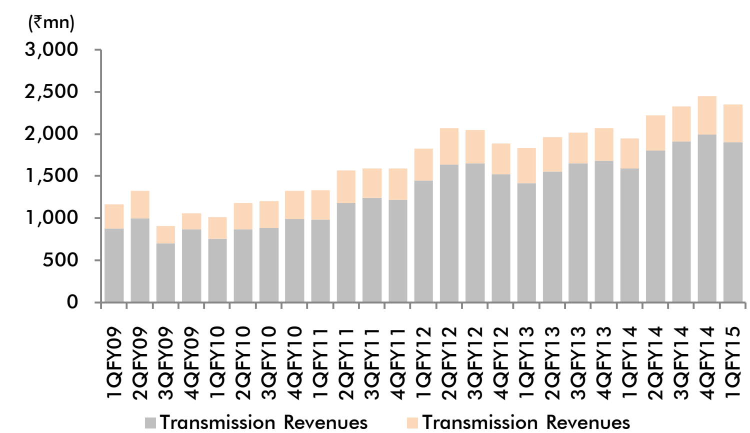


Exhibit 27: Transmission EBIT margins

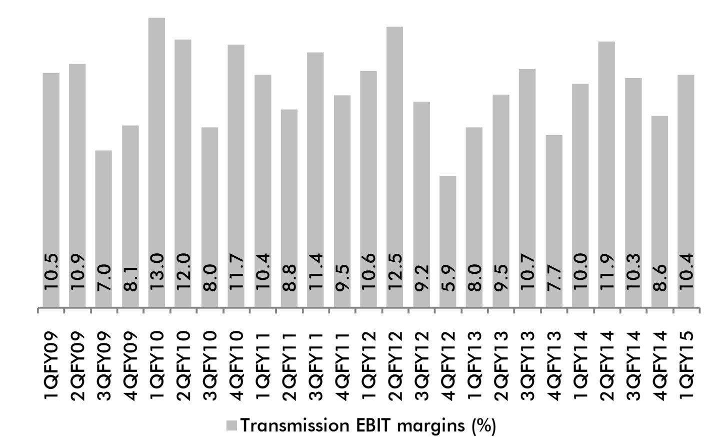
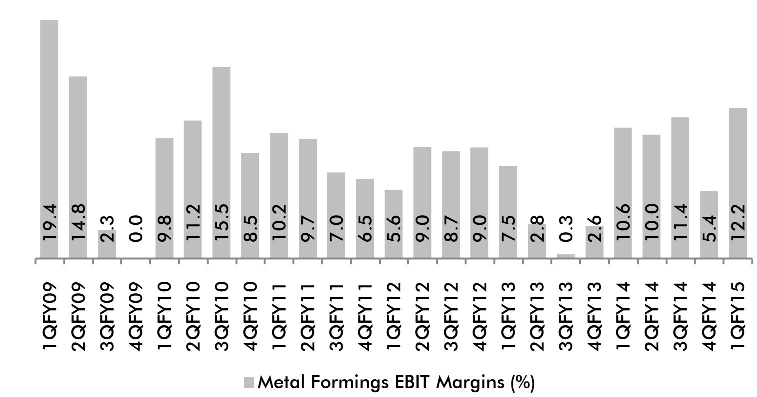


Exhibit 28: Metal Forming EBIT margins



Source: Company, AMSEC Research

Key Financials

Standalone (₹mn)	FY12	FY13	FY14	FY15F	FY16F	FY17F
Total Income	9,051	9,366	9,879	11,242	12,871	14,812
EBITDA	1,021	897	1,121	1,354	1,609	1,985
EBITDA Margin(%)	11.3	9.6	11.3	12.0	12.5	13.4
PBT	582	422	685	882	1,104	1,456
PAT	435	337	543	697	872	1,034
Subsidiaries (₹mn)	**FY12**	**FY13**	**FY14**	**FY15F**	**FY16F**	**FY17F**
Total Income	76	196	1,206	1,214	1,359	1,522
EBITDA	15	(3)	141	146	163	183
EBITDA Margin(%)	19.5	(1.7)	11.7	12.0	12.0	12.0
PBT	8	(19)	115	118	131	145
PAT After Minority Interest	7	(10)	76	68	71	80
Consolidated (₹mn)	**FY12**	**FY13**	**FY14**	**FY15F**	**FY16F**	**FY17F**
Total Income	9,127	9,562	11,086	12,456	14,230	16,335
EBITDA	1,036	893	1,261	1,500	1,772	2,168
EBITDA Margin (%)	11.4	9.3	11.4	12.0	12.5	13.3
PBT	589	403	800	1,000	1,234	1,601
PAT	442	326	619	765	943	1,113

Source: Company, AMSEC Research

Standalone - Segment Performance

Segment (₹mn)	FY12	FY13	FY14	FY15F	FY16F	FY17F
Revenue	**9,051**	**9,366**	**9,879**	**11,242**	**12,871**	**14,812**
Metal Forming	1,579	1,572	1,659	1,808	1,989	2,287
Others	1,214	1,486	925	989	1,109	1,244
Transmission	6,258	6,308	7,295	8,445	9,773	11,282
EBIT	756	647	854	1,060	1,295	1,655
Metal Forming	128	54	153	166	199	240
Others	29	26	(38)	24	61	140
Transmission	599	567	739	870	1,036	1,275
EBIT Margins (%)						
Metal Forming	8.1	3.4	9.2	**9.2**	**10.0**	**10.5**
Others	2.4	1.7	(4.1)	**2.4**	**5.5**	**11.3**
Transmission	9.6	9.0	10.1	**10.3**	**10.6**	**11.3**

Source: Company, AMSEC Research

Peer Comparison

Tube Investments competes with LGBL in the automotive chains segment with 29% market share in the OEM segment and 50% in the organized replacement segment. Automotive chains form 7% of its total consol revenues. The company sells its chains under the 'diamond' brand.

Tube Investments Financial snapshot (₹mn)	**FY11**	**FY12**	**FY13**	**FY14**
Revenues	**32,716**	**38,226**	**38,132**	**40,404**
Cycles / Components / Scooters	11,226	13,011	12,655	11,850
Engineering	11,951	14,566	14,713	16,224
Gears and Gear Products			632	1,557
Metal Formed Products	**9,539**	**10,648**	**10,132**	**10,773**
EBIT	**2,922**	**3,268**	**2,506**	**2,659**
Cycles / Components / Scooters	771	749	508	380
Engineering	1,127	1,311	1,098	1,359
Gears and Gear Products			62	223
Metal Formed Products	**1,024**	**1,208**	**839**	**697**
Metal Form Products as % of Revenues	29%	28%	27%	27%
Automotive Chains as % Metal form Revenues	23%	25%	26%	28%
Automotive Chains as % of Revenues	7%	7%	7%	8%
EBIT Margins	**8.9%**	**8.5%**	**6.6%**	**6.6%**
Cycles / Components / Scooters	6.9%	5.8%	4.0%	3.2%
Engineering	9.4%	9.0%	7.5%	8.4%
Gears and Gear Products			9.8%	14.3%
Metal Formed Products	**10.7%**	**11.3%**	**8.3%**	**6.5%**

Source: Company, AMSEC Research

Peer Valuation

	Mcap	**P/E**		**P/BV**		**RoCE (%)**	
Peer Comparision	**(₹bn)**	**FY15E**	**FY16E**	**FY15E**	**FY16E**	**FY15E**	**FY16E**
LGBL	**11.0**	**14.6**	**11.8**	**3.0**	**2.4**	**23.2**	**24.2**
Tube Investments	62.8	18.2	16.6	2.8	2.4	22.0	22.1
Suprajit Engineering	15.2	23.0	18.5	6.0	4.8	27.9	27.8
Sundram Fasteners	30.7	17.1	12.8	3.2	2.6	18.0	20.2
Gabriel	11.8	18.1	13.5	3.6	3.0	20.6	23.2

Source: Bloomberg, AMSEC Research

On a relative basis LGBL appears cheap on current valuation and considering the earnings growth trajectory, Return ratios and dominant player status in its business rerating is on the cards.

Valuation and outlook

For LGB, 13% revenue CAGR over FY14-17E on back of Motorcycle growth revival and steady growth in GFM and Metal forming revenues will translate into 22% PAT CAGR. With operating leverage benefits (capacity utilization of 60% in FY17 from 55% in FY14 despite a 20% capacity expansion) bodes well for margins (we build 188bp expansion over FY14 -17). At CMP LGBL trades at 11.8x FY16 and 10x FY17 EEPS. With strong cash flow, healthy return ratios and excellent growth prospects, we expect the stock to get re-rated. Based on 13x FY17E EPS of ₹70.9, we arrive at a target price of ₹922 which provides a 31% upside from the current levels. BUY

Financials (Consolidated) (₹mn)

Profit and Loss Account

Y/E (Mar)	FY14	FY15E	FY16E	FY17E
Net sales	10,383	11,669	13,293	15,218
Other operating income	703	787	937	1,116
Consumption of materials	5,454	6,078	7,006	8,042
Staff Expenses	1,340	1,498	1,691	1,865
Other operating expenses	3,030	3,380	3,760	4,260
Total Expenditure	9,824	10,956	12,458	14,167
EBITDA	**1,261**	**1,500**	**1,772**	**2,168**
Depreciation	328	371	423	470
Operating profit	**933**	**1,129**	**1,349**	**1,698**
Other income	46	59	89	116
EBIT	**979**	**1,189**	**1,438**	**1,813**
Interest	179	188	204	213
Exceptional items	-	-	-	-
Profit before tax	**800**	**1,000**	**1,234**	**1,601**
Tax	149	199	247	440
Share in profit of associate cos	-	-	-	-
Minority interest	32	36	44	48
Net profit	**619**	**765**	**943**	**1,113**
EO Items	-	-	-	-
Adjusted net profit	**619**	**765**	**943**	**1,113**
EPS ₹	39.4	48.7	60.1	70.9

Cash Flow Statement

Particulars	FY14	FY15E	FY16E	FY17E
PBT	800	1,000	1,234	1,601
Non-cash adjustments	328	371	423	470
Changes in working capital	(58)	(174)	(248)	(301)
Tax Paid	(190)	(245)	(304)	(504)
Cashflow from operations	**881**	**951**	**1,105**	**1,265**
Capital expenditure	(653)	(763)	(696)	(620)
Change in investments	5	(15)	(25)	(25)
Other investing cashflow	(45)	(28)	(35)	(56)
Cashflow from investing	**(694)**	**(806)**	**(756)**	**(701)**
Issue of equity	-	-	-	-
Issue/repay debt	(133)	270	122	130
Interest Paid	-	-	-	-
Increase/(Decrease)Loan Funds	-	-	-	-
Dividends paid	(110)	(136)	(158)	(202)
Other financing cashflow	-	-	-	-
Cashflow from financing	**(243)**	**134**	**(36)**	**(72)**
Change in cash & cash eq	**(56)**	**279**	**313**	**492**
Opening cash & cash eq	**103**	**65**	**343**	**655**
Closing cash & cash eq	**65**	**343**	**655**	**1,146**
Free cash flow to firm	228	188	409	645

Balance sheet

Y/E (Mar)	FY14	FY15E	FY16E	FY17E
SOURCES OF FUNDS :				
Share Capital	157	157	157	157
Reserves	2,932	3,597	4,426	5,386
Total Shareholders Funds	**3,089**	**3,754**	**4,583**	**5,543**
Minority Interest	**97**	**133**	**177**	**225**
Non-Current Liabilities	**830**	**1,131**	**1,270**	**1,405**
Long term borrowings	660	970	1,120	1,270
Deferred tax liability	170	161	150	135
Other long term liabilities	-	-	-	-
Long-term provisions	-	-	-	-
Current Liabilities	**2,885**	**3,120**	**3,412**	**3,766**
Short term borrowings	635	595	566	547
Trade payables	1,464	1,663	1,901	2,184
Other current liabilities	722	794	873	961
Short term provisions	64	67	71	74
Total Equity & Liabilities	**6,901**	**8,138**	**9,442**	**10,939**
APPLICATION OF FUNDS :				
Non Current Assets	**3,161**	**3,635**	**4,009**	**4,274**
Gross block (Total)	4,861	5,611	6,291	6,891
Less : accumulated depreciation (Total)	2,314	2,672	3,078	3,527
Net block (Total)	2,547	2,940	3,213	3,364
Capital work in progress	90	90	90	90
Noncurrent investment	182	197	222	247
Deferred tax assets	-	-	-	-
Long term loans and advances	337	399	473	561
Other non-current assets	5	9	10	11
Current Assets	**3,739**	**4,502**	**5,433**	**6,665**
Current investment	-	-	-	-
Inventories	2,075	2,351	2,688	3,089
Sundry debtors	1,461	1,635	1,866	2,141
Cash and bank	65	343	655	1,146
Short loans and advances	134	173	224	289
Others current assets	4	-	-	-
Total Assets	**6,901**	**8,138**	**9,442**	**10,939**
Net Working Capital*	1,884	1,986	2,598	3,457
Total Debt*	1,503	1,565	1,686	1,817
Capital Employed*	4,762	5,480	6,420	7,495

*WC = CA - CL (Excl short term & Curr. Mat. long term debt)

*Total Debt=Long Term + short Term + Cur mat. long term debt

*Cap Emp = NW + Total Debt

Ratios

Particulars	FY14	FY15E	FY16E	FY17E
PER SHARE				
EPS ₹	39.4	48.7	60.1	70.9
CEPS ₹	60.3	72.3	87.0	100.8
Book Value ₹	196.8	239.2	292.0	353.1
VALUATION				
EV / Net Sales	1.2	1.1	0.9	0.8
EV / EBITDA	10.0	8.2	6.9	5.5
P / E Ratio	18.0	14.6	11.8	10.0
P / BV Ratio	3.6	3.0	2.4	2.0
GROWTH YOY%				
Sales Growth	15.1	12.4	13.9	14.5
EBITDA Growth	41.2	18.9	18.1	22.3
Net Profit Growth	89.2	23.5	23.3	18.0
Gross Fixed Asset Growth	13.6	15.4	12.1	9.5
PROFITABILITY				
Gross Profit/ Net sales (%)	34.6	35.1	34.6	34.9
EBITDA / Net Sales (%)	11.4	12.0	12.5	13.3
EBIT / Net sales(%)	9.4	10.2	10.8	11.9
NPM / Total income (%)	5.6	6.1	6.6	6.8
Raw Material/Net Sales(%)	52.9	52.1	52.7	52.8
Int/PBIT (%)	18.3	15.9	14.2	11.7
ROE (%)	21.8	22.4	22.6	22.0
ROCE (%)	21.3	23.2	24.2	26.1
Tax / PBT (%)	18.6	19.9	20.0	27.5
TURNOVER				
Net Woking Cycle	66	62	71	83
Debtors Velocity (Days)	51	51	51	51
Inventory (Days)	83	84	85	86
Creditors Velocity (Days)	97	100	99	99
Current Ratio	1.9	1.8	1.9	2.1
Quick Ratio	0.9	0.9	1.0	1.1
LIQUIDITY				
Gross Asset Ratio	2.3	2.2	2.2	2.3
Total Asset Ratio	1.6	1.6	1.5	1.5
Net Debt-Equity Ratio	0.5	0.3	0.2	0.1
Interest Coverage	5.5	6.3	7.1	8.5
PAYOUT				
Payout %	20	19	18	20
Dividend %	60	72	86	110
Yield %	0.8	1.0	1.2	1.5

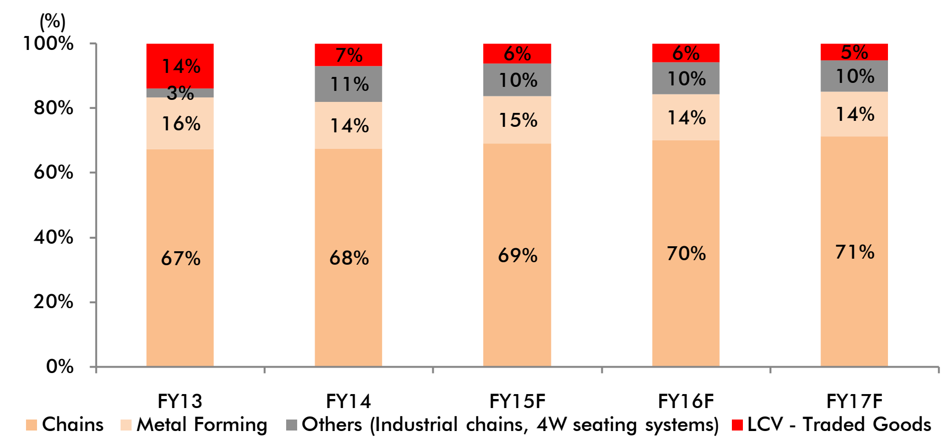
*Source: Company, AMSEC Research** Due to change in Schedule VI format, the numbers for earlier years are not furnished.*

Background

LGB was incorporated as a private limited company (in 1956) and was converted into a public limited company (in 1975). The company is was promoted by Late L G Varadarajulu. The company is a roller chain manufacturer and it manufactures automotive chains like motorcycle and moped chains, heavy duty chains, timing chains and automotive kits. The products are marketed under the brand name 'Rolon'.

The company also does metal forming, which includes fine blanking, rolled strips & profiles, hot & cold forging and precision machine parts. Head quartered in Coimbatore, the company has 20 chain manufacturing units (13 big and 7 small) spread across Tamil Nadu, Maharashtra, Uttrakhand, Karnataka and Haryana and employees around 4,000 employees.

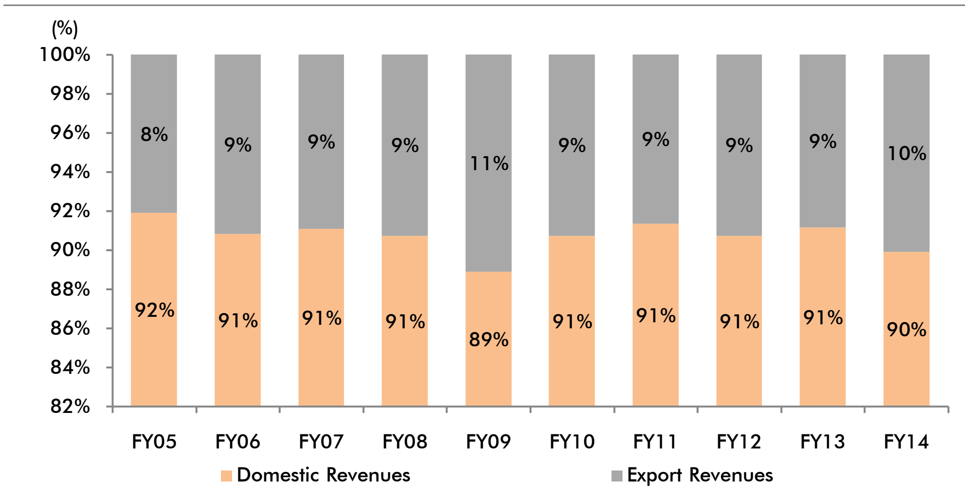
Exhibit 29: Revenue Mix – Automotive chains is the bread and butter business



Source: Company, AMSEC Research

LGBL's bread and butter business is automotive chains – primarily Motorcycle and Moped chains (~68% of FY14 consol Revenues). It also has presence in other 3 segments where it operates namely Metal Forming (~14%), Others (industrial chains, 4W seating systems ~11%) and Tata LCV dealership (~7%). Around 10% of its consol revenues comprise exports and rest is domestic.

Exhibit 30: Exports is ~10% of consolidated revenues



Source: Company, AMSEC Research

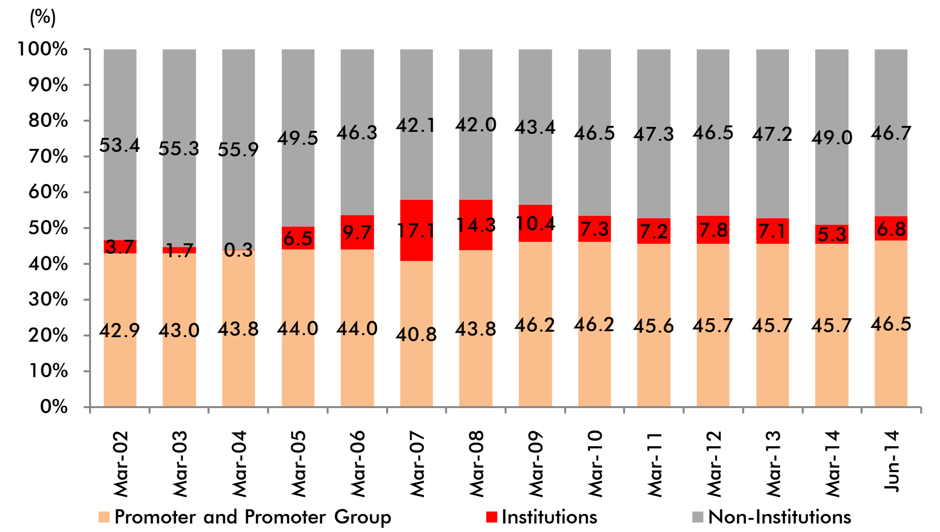
In 2008, it sold its industrial chain business to Renold Plc, a leading global supplier of all types of industrial chain (headquartered in UK) and formed a Joint Venture with a 25% stake. In 2012, LGBL acquired a USA based fine blanking company GFM (Grip Flow Method) for $5.5mn. The company manufactures metal stamping products for seating applications for leading 4W OEMs in USA. Its 100% owned subsidiary BCW V Tech India, is a supplier of machined components for export markets.

Management Profile

B. Vijaya kumar: is an Executive Chairman of the Board, Managing Director of LG Balakrishnan & Bros Ltd. He has 40 years experience as Industrialist and more than 20 years as the Managing Director of the Company. Under his stewardship the company has grown from strength to strength.

P. Prabakaran: is Deputy Managing Director, Executive Director of LG Balakrishnan & Bros Ltd. He has 23 years of experience in this business

Exhibit 31: Shareholding: Promoters maintained their holding over the last decade



Source: Company, AMSEC Research

Recommendation rationale

Buy: Potential upside of	>+15% (absolute returns)
Accumulate:	>+5 to +15%
Reduce:	+5 to -5%
Sell:	< -5%
Not Rated (NR):	No investment opinion on the stock

Sector rating

Overweight:	The sector is expected to outperform relative to the Sensex.
Underweight:	The sector is expected to underperform relative to the Sensex.
Neutral:	The sector is expected to perform in line with the Sensex.

Disclosure of Interest

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2. Qualifications of the analyst:	MBA CFA FRM	B.Com(Financial Markets)
3. Analysts' ownership of any stock related to the information contained:	Nil	Nil
4. AMSEC ownership of any stock related to the information contained:	None	None
5. Broking relationship with company covered:	None	None
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