Research
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Nano Nivesh

Key risks to investing in Nano stocks

- Nano stocks may not be in the limelight and inherently being micro cap in nature will have a high risk return profile

- We advise clients to be disciplined in investing at all times. Allocate only a small proportion of your investible income to these stocks and diversify well

- Try to diversify your exposure within the Nano stocks as well by investing equal proportions in several picks

- These stocks may have low volumes and trade infrequently

- Micro cap stocks the world over are, to a large extent, affected by the "Pump and Dump" phenomenon of inflated price buying and depressed price selling

- As explained above, the clients should be patient and trade only through limit orders on any side of the trade.

- The risk of volatility remains in such micro cap stocks as they can move up or down with large buy/sell orders

- The fair value of Nano stocks are subject to expected growth potential in the future. Though due diligence has been done to a fair extent, the actualisation of growth still has a degree of uncertainty attached to it

Nano stocks report tries to highlight companies with good and scaleable business models, dependable management and sound financials. However, these stocks may not be in the limelight and have a high risk high return potential. Please watch out for the following factors before investing in these stocks:

Allocate a small proportion of your investible income to these stocks and diversify well. If you choose to invest in these stocks, most of your assets allocated towards equity should remain in more stable investments like stocks of large companies. Moreover, try to diversify your exposure within the nano stocks as well by investing equal proportions in several picks. This will help you avoid losing too much of your total wealth if the investments do not turn out well. When you invest in micro-cap stocks there is a higher risk of impairment.

These stocks may have low volumes and trade infrequently. This can create a situation in which you may not be able to find any willing buyers for your stocks when you wish to sell. We advise our clients to be patient and trade only though limit orders to avoid volatile fluctuations, both while putting a buy and sell order in these stocks.

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Atul Auto (ATUAUT)

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Atul Auto is a Rajkot-based three-wheeler manufacturer primarily catering to the non-urban market providing mobility and logistic solutions. The company differentiates itself with customised product offerings, low maintenance, and strong after-sales service to buyers in form of service warranties of 24-months.

Price
₹ 97

Recommendation
Buy

Fair Value
₹ 160-180

Highlights:

- **An undiscovered OEM with "rural" play.** Atul Auto is one of the few listed OEMs, which has grown well in the last couple of years but has remained away from the market eye. This despite it being attached with the rural theme, which remained much in favour
- **Expansion plans to help market share gains.** The company is in the process of doubling the capacity to ~48,000 units by FY14E. This would lead to strong market share gains (~6% currently) as the order book remains healthy with export target also opening up.
- **Decent margins/strong RoEs/zero net debt/good dividend yield.** On the financials front, EBITDA margins have remained well above 9% in a challenging environment for the past three years. RoEs of 25%+ coupled with dividend yield of ~5% and negligible debt makes this an attractive company in financial terms on a longer term as well.
- **Topline/EPS CAGR (FY12-14E) at ~17%/26%.** We believe the company would improve on its volume growth (~17% CAGR12-14E) aided by fresh capacity expansion coming on-stream. The margin profile is expected to remain on the up considering lower input costs and a better operational performance.
- **The three-wheeler segment is a tale of urban vs. rural demand, which is a tale of two halves with the former weak and the latter strong. Atul Auto remains poised to improve its market share driven by its rural focus and new products in passenger as well as goods segment. This is coupled with attractive valuations of PEG ~0.1x (CAGR FY12-14E) and 1.1x PBV/dividend yield of ~5%. This stock ticks all the right boxes for long term investors.**

Key risks-

Business specific

The three-wheeler segment future growth prospects remain mixed. The strong growth of the small commercial vehicle space has led to lower volume growth for this segment. The future trend of this industry will depend on the kind of rural demand growth as the demand in urban markets remains weak due to low new permit issuances on the passenger side.

Company specific

Strategy failures on product developments or expansion would not be spared. Atul auto is much smaller company in terms of volumes and turnover relative to other major competitors like Bajaj Auto, Piaggio thus the room for failure remains low in terms of new products and new market expansions. Even though the management has till now been cautious in expansion and growth initiatives as company tries to go pan-India and bring in new products this risk intrinsically increases.

Description

The company set up its present plant at Shapar village in Rajkot district with financial assistance from GSFC in 1992. Atul Auto is currently engaged in manufacture of diesel three wheelers like six-seater auto rickshaws, pick-up vans and chassis of passenger vehicles. These vehicles are marketed under the brand name Khushbu that is well established and very popular. Over 150,000 Khushbu-branded vehicles ply on the roads of Gujarat.
Atul has already obtained CMVR and roadworthiness certificates for the existing range of products viz. chassis for goods carriage/six-passenger auto rickshaws with steering wheel and pick-up.

History and track record

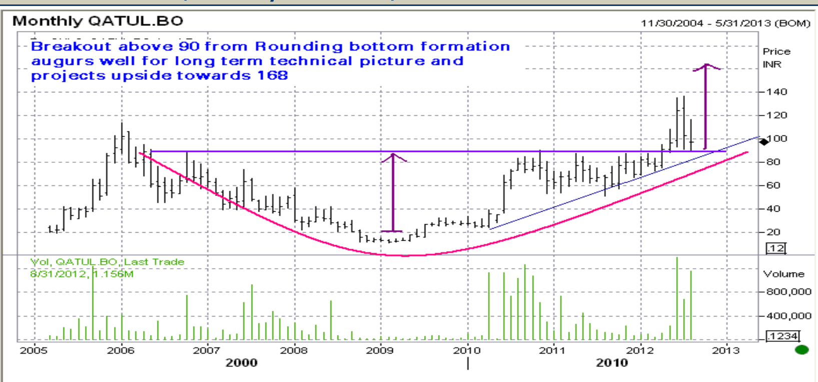
- Atul Auto, (incorporated in 1986 and turned public in 1994) is a manufacturer of three-wheeler vehicles based in Gujarat. It is currently engaged in manufacture of three-wheelers like six-seater auto rickshaws, pick-up vans, delivery vans and passenger vehicles' chassis
- The recently launched Smart, an upgraded version of Shakti, will be the first Atul product to be introduced in Tamil Nadu and Madhya Pradesh. The company is in the process of doubling its three-wheeler capacity at the Rajkot plant to 48,000 units per annum. It is also working on two new models; a sub-1-tonne four-wheeler & a small three-wheeler
- The company has grown its domestic market share in the goods carrier segment from 5% in FY09 to 12% in FY12 while growing at a CAGR of 44%. In FY13 (YTD), its market share was 15% in this segment. Overall, Atul Auto's share in the domestic carrier space has increased nearly three-fold from 2% in FY09 to ~6% in FY13 (YTD)
- In the last 10-12 years, Atul Auto has issued bonus shares to its shareholders twice and has been a consistent dividend payer in last seven or eight years. This shows a pro-minority shareholder outlook that is uncommon in small cap companies

Earning estimates

₹ crore	FY10	FY11	FY12	FY13E	FY14E
Net Sales	119	201.6	298.3	339.6	409.8
EBITDA	13.0	19.4	27.5	31.5	40.9
EBITDA margin (%)	10.9	9.6	9.2	9.3	10.0
PAT	4.5	9.4	15.6	18.5	24.6
FDEPS*	4.1	8.6	14.2	16.9	22.5

*Source: Company, ICICIdirect.com Research * Fully diluted EPS*

Technical Chart (Monthly Bar chart)



Source: Reuters, ICICIdirect.com Research

Stock data

Market Capitalisation (₹ crore)	₹ 106 crore
52 Week High / Low (₹)	137 / 58
Promoter Holding (%)	61%
FII Holding (%)	0%
DII Holding (%)	0%
Dividend Yield (%)	5%
12M / 6M stock return (%)	48% / 21%
Debt	₹ 4 Crore
Cash and Cash Equivalent	₹ 11.4 Crore
Enterprise Value	₹ 98 crore
5 Year Revenue CAGR (%)FY08-12	25%
5 Year EBITDA CAGR (%)FY08-12	33%
5 Year PAT CAGR (%)FY08-12	20%

Valuation table

	FY11	FY12	FY13E	FY14E
P/E(x)	6.2	4.7	5.7	4.3
Target P/E(x)	10.1	7.6	9.3	7.0
EV / EBITDA(x)	5.5	3.8	2.9	2.0
P/BV (x)	1.5	1.3	1.4	1.1
RoNW(%)	23.4	27.8	24.6	26.3
RoCE(%)	35.0	38.8	34.4	36.8

Source: ICICIdirect.com Research

Quarterly performance

(₹ Crore)	Q2FY12	Q3FY12	Q4FY12	Q1FY13
Total Operating Income	75.3	79.7	82.9	77.3
EBITDA	7.5	5.8	7.1	6.7
EBITDA Margin (%)	10.0	7.3	8.5	8.7
Depreciation	1.0	1.0	1.1	1.1
Interest	0.2	0.1	0.1	0.1
Other Income	1.3	0.3	0.2	0.1
Reported PAT	4.3	3.8	4.2	3.9
EPS (₹)	7.0	5.0	5.5	3.5

Source: ICICIdirect.com Research

Shareholding trend (%)

Key Shareholders	Q2FY12	Q3FY2	Q4FY12	Q1FY13
Promoter group	60.8	60.8	60.8	60.8
Vijay Kedia	5.4	5.7	5.7	5.7
Kedia Securities	8.5	9.0	9.0	9.0

Source: ICICIdirect.com Research

Technical View

The share price of Atul Auto embarked upon a sustainable rally post its lifetime low around ₹ 12 during March 2009. The stock rallied in a manner of rising peaks and troughs to hit an all-time high of ₹ 136 during July 2012.
The most dominating pattern on the chart is the break out from bullish Rounding Bottom pattern in April 2012 with rising volumes. The pattern implication considering the depth of the pattern (90-12) projects upsides towards ₹ 168 over the next several months.
The long term technical picture post the breakout has turned positive.

What's the story?

Atul Auto is a three-wheeler OEM, which has positioned itself as primarily catering to the non-urban market providing mobility and logistic solutions. It has a decent product portfolio encompassing products like six-seater auto rickshaws, pick-up vans and delivery vans (diesel, CNG, LPG variants). The company differentiates itself with customised product offerings to rural buyers, which other larger players like Bajaj Auto and Piaggio do not provide. On the service front also, it remains the only three-wheeler player with a 24-month service warranty, thereby differentiating in after sales too. In terms of brands, currently it has three models - Shakti, Smart and Gem, the last of which is the most popular product.
The company is in the process of doubling the capacity to ~48,000 units by FY14-15E. This would lead to strong market share gains (~6% currently) as the order book remains healthy with export targets also opening up. At present, it is a strong player in a few states like Gujarat, Karnataka and Rajasthan and is a looking like a strong second player in many newer markets. With the dealer network being expanded to ~150 dealers in 15 states the target audience increase in terms of number of states is a positive strategy.

We have grown confident on the brand/offerings of the company on account of the fact that even after entering late into newer markets like Andhra Pradesh it has gained market share from strong incumbents like Piaggio. This would provide a strong stepping stone into forays towards more markets and a future pan-India presence.

On the industry side, the three-wheeler segment growth prospects remain mixed with rural based demand growing well and urban demand floundering due to a lack of fresh permit issuances on the passenger side. The growth of the sub-1 tonne SCV has dented the growth prospects in the three-wheeler space. Thus, product differentiation remains a major strategy for players to gain volumes considering strong competition from the likes of Tata Motors and M&M.

On these fronts, Atul's target markets at present remains in the growth phase driven by the "rural" theme. However the company is working on a four-wheeler product, which would be needed to compete in the fast growing SCV market. At present, with a competitive product performance, strong after sales, low maintenance and specialised products the company would continue to improve volumes as it targets going pan-India. On the exports front, as expansion comes in full by December 2012, the company is working on restarting exports in the South East Asian/Saarc markets like Bangladesh and Sri Lanka in the immediate term along with newer African markets.

Fundamentals sound; valuations need to rise!

On the financials front also, it has been able to maintain EBITDA margins well above 9% in a challenging environment for the past three years. RoEs of >25% and a dividend yield of ~5% even as it continued to undertake fresh capital expenditure signifies the strong fundamentals. The negligible debt level signals the nature of business working as the management believes in internal accruals for business growth rather than the easier route of debt.

We believe the company would improve its volume growth (~17% CAGR FY12-14E) aided by fresh capacity expansion coming on stream. The margin profile is expected to remain on the rise considering lower input costs and a better operational performance.

The attractive valuations of PEG ~0.1x (CAGR FY12-14E) and1.1x PBV FY14E means market participants are not paying any attention to the sound fundamentals of the stock. However, with the expected growth potential and coupled with a clean balance sheet this mispricing would not stay for long. We believe that being an OEM and with the aforesaid characteristics, the fair multiple range for PE and EV/EBIDTA would be ~7-8x and ~3.5-4x, respectively. This brings our fair value target for Atul Auto in the region of ₹ 160-180, providing a significant upside potential to the stock.

However, on a cautionary note, though the upside seems lucrative, still considering the various impediments faced by small cap stocks, we believe this should be looked at as a medium to long term investment, which has inherent risks of higher price volatilities.

Financial summary

Profit and loss statement

(₹ Crore)

(Year-end March)	FY11	FY12	FY13E	FY14E
Total Volumes (Units)	19,406	27,000	30,819	36,947
Total operating Income	202.0	298.8	339.6	409.8
Growth (%)	68.6	47.9	13.7	20.6
Raw Material Expenses	158.5	237.6	269.5	323.3
Employee Expenses	11.6	16.5	20.9	22.7
Other Expenses	12.5	17.2	17.7	22.9
Total Operating Expenditure	182.6	271.3	308.1	368.9
EBITDA	19.4	27.5	31.5	40.9
Growth (%)	50.0	41.7	14.4	29.8
Depreciation	4.3	4.3	4.3	4.9
Interest	1.8	0.8	0.2	0.2
Other Income	0.6	0.6	0.6	0.9
PBT	14.0	23.2	27.6	36.6
Others	0.0	0.0	0.0	0.0
Total Tax	4.5	7.7	9.0	12.0
PAT	9.4	15.6	18.5	24.6
Growth (%)	107.5	64.8	19.2	33.0
EPS (₹)	15.5	20.6	16.9	22.5
FDEPS (₹)	8.6	14.2	16.9	22.5

Source: Company, ICICIdirect.com Research, FDEPS: Fully diluted EPS

Cash flow statement

(₹ Crore)

(Year-end March)	FY11	FY12	FY13E	FY14E
Profit after Tax	9.4	15.6	18.5	24.6
Add: Depreciation	4.3	4.3	4.3	4.9
(Inc)/dec in Current Assets	3.5	-15.5	-5.5	-6.3
Inc/(dec) in CL and Provisions	8.5	5.8	7.4	6.3
CF from operating activities	25.7	10.1	24.7	29.6
(Inc)/dec in Investments	0.0	-6.5	-3.0	-5.0
(Inc)/dec in Fixed Assets	-3.9	-3.3	-8.0	-10.0
Others	2.2	0.7	0.0	0.0
CF from investing activities	-1.6	-9.1	-11.0	-15.0
Issue/(Buy back) of Equity	0.0	1.5	3.4	0.0
Inc/(dec) in loan funds	-20.2	0.9	0.0	0.0
Dividend paid & dividend tax	-2.7	-4.3	-6.2	-6.2
Others	-1.8	2.2	3.2	-0.2
CF from financing activities	-24.7	0.3	0.5	-6.4
Net Cash flow	1.2	2.0	14.4	8.4
Opening Cash	1.6	2.8	4.8	19.2
Closing Cash	2.8	4.8	19.2	27.6

Source: Company, ICICIdirect.com Research

Balance sheet

(₹ Crore)

(Year-end March)	FY11	FY12	FY13E	FY14E
Liabilities				
Equity Capital	6.1	7.6	11.0	11.0
Reserve and Surplus	34.3	48.5	64.3	82.8
Total Shareholders funds	40.3	56.0	75.3	93.7
Total Debt	3.0	3.9	3.9	3.9
Deferred Tax Liability	5.4	4.7	4.7	4.7
Others	2.3	2.7	2.7	2.7
Total Liabilities	51.1	67.3	86.5	104.9
Assets				
Gross Block	63.1	61.1	69.1	79.1
Less: Acc Depreciation	20.7	21.2	25.5	30.5
Net Block	42.4	39.9	43.6	48.7
Capital WIP	0.0	1.6	1.6	1.6
Total Fixed Assets	42.4	41.5	45.2	50.2
Investments	2.3	7.7	10.7	15.7
Inventory	19.2	29.8	35.1	38.8
Debtors	5.4	6.1	7.9	9.0
Loans and Advances	2.2	6.5	4.8	6.4
Other current assets	0.2	0.1	0.3	0.2
Cash	2.8	4.8	19.2	27.6
Total Current Assets	29.9	47.4	67.3	82.0
Creditors	10.8	15.5	17.6	22.4
Provisions	4.2	7.5	8.5	10.9
Other current liability	8.6	6.3	10.6	9.8
Total Current Liabilities	23.6	29.3	36.8	43.1
Net Current Assets	6.3	18.0	30.5	38.9
Application of Funds	51.1	67.3	86.5	104.9

Source: Company, ICICIdirect.com Research

Key ratios

(Year-end March)	FY11	FY12	FY13E	FY14E
Per share data (₹)				
EPS	15.5	20.6	16.9	22.5
Cash EPS	22.5	26.3	20.8	27.0
BV	66.4	74.2	68.6	85.4
DPS	3.8	4.8	4.8	4.8
Cash	4.7	6.4	17.5	25.2
Operating Ratios (%)				
EBITDA Margin	9.6	9.2	9.3	10.0
PBT / Net sales	6.9	7.8	8.1	9.0
PAT Margin	3.8	4.7	5.2	5.5
Inventory days	34.2	30.0	35.0	33.0
Debtor days	9.8	7.4	8.5	8.0
Creditor days	19.6	19.0	19.0	20.0
Return Ratios (%)				
RoE	23.4	27.8	24.6	26.3
RoCE	35.0	38.8	34.4	36.8
RoIC	31.5	37.3	40.5	46.5
Valuation Ratios (x)				
P/E	6.2	4.7	5.7	4.3
EV / EBITDA	5.5	3.8	2.9	2.0
EV / Net Sales	0.5	0.4	0.3	0.2
Market Cap / Sales	0.5	0.4	0.3	0.3
Price to Book Value	1.5	1.3	1.4	1.1
Solvency Ratios				
Debt/Equity	0.1	0.1	0.1	0.0
Current Ratio	1.3	1.6	1.8	1.9
Quick Ratio	0.5	0.6	0.9	1.0

Source: Company, ICICIdirect.com Research

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Buy: > 10%/ 15% for large caps/midcaps, respectively;
Hold: Up to +/-10%;
Sell: -10% or more;

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