



HAPPY FORGINGS LIMITED

Happy Forgings Ltd. is the fourth largest engineering-led manufacturer of complex and safety critical, heavy forged and high precision machined components in India as of Fiscal 2023 in terms of forgings capacity. The company, through its vertically integrated operations, is engaged in engineering, process design, testing, manufacturing, and supply of a variety of components that are both margin accretive and value-additive. It primarily caters to domestic and global original equipment manufacturers (OEMs) manufacturing commercial vehicles in the automotive sector, while in the non-automotive sector, it caters to manufacturers of farm equipment, off-highway vehicles and manufacturers of industrial equipment and machinery for oil and gas, power generation, railways and wind turbine industries. The company's current forging capacity is 107,000 MTPA and machining capacity of 46,000 MTPA. The company has India's second-largest production capacity for high-powered industrial crankshaft. It makes crankshafts of 10-210 kg that are used in diverse application fields. Sales to commercial-vehicle customers account for 43% of revenue, followed by farm equipment (37%) and off-highway (16%), with the balance coming from industries. Customers include Ashok Leyland, VE Commercial Vehicles, Dana India, JCB India and Mahindra & Mahindra. It exports to nine countries, including Sweden, Turkey and Italy.

Investment Rationale:

Increasing share of machined components business volume boosting margins:

- The share of machined parts - a segment that enjoys higher realisation in forging - in the company's total volume has been consistently increasing and it has been able to source raw materials at a lower rate. This helped Happy Forgings enjoy the highest operating margin among peers.
- As of FY23, Happy Forging is only the second company in India to have a 14,000-tonne forging press or higher and is among four companies in India that possess an 8,000-tonne forging press or higher. The company has consistently delivered EBITDA margins in the range of 27-28% over FY21-23.
- We expect improvement in margins by another 200-300bp over the coming quarters led by cost increasing share of machined parts revenue and also optimisation due to lower steel prices.

Expanding capacity at existing manufacturing facilities:

- Happy Forging operates three manufacturing facilities with two located at Kanganwal in Ludhiana, Punjab, and one at Dugri in Ludhiana, Punjab. While one of the manufacturing facilities at Kanganwal is dedicated to forging operations, the other two are equipped with both forging and machining capabilities.
- The company proposes to purchase new machinery and equipment to build up additional capacity for forging and machining operations from the Net Offer Proceeds. Happy Forging is in the process of commissioning a new 6,300-tonne forging press line, expected to be installed by June 2024.
- The company has also previously strategically increased capacity without compromising on return ratio, although 33% of its gross value of fixed assets was a result of capex incurred between FY22 and FY23.
- There is ample room for export growth - exports accounted for 20% of revenue in the first half of FY24 and that was significantly lower than its peers. The company offers an attractive value proposition for overseas customers by offering 15-20% lower prices than the current landed cost.

Long-standing relationships with customers across industries:

- The company has, through over 40 years of business operations, established long-standing relationships with several Indian and global customers across industries.
- It is among the few companies in India that manufacture and supply high precision safety critical components to leading OEMs including manufacturers of commercial vehicles, farm equipment, off-highway vehicles and industrial equipment and machinery for oil and gas, power generation, railways and wind turbine industries.
- It has a diversified customer base and it has served 66 customers in Fiscal 2023 and 59 customers in the six months ended September 30, 2023.

Valuation and Outlook: We are positive upon Happy Forging due to: i. The company has better margins with lower valuation when compared with its peers. ii. The share of machined parts has been consistently increasing in the company's total volume, a segment that enjoys higher realisation in forging. It has also been able to source raw materials at a lower rate. This helped Happy Forgings enjoy the highest operating margin among peers. iii. The company's current forging capacity is 107,000 MTPA and machining capacity of 46,000 MTPA. The range of tonnage press is between 2,500 – 14,000T. A 6,300T press line is expected by FY24 while another 10,000T press is expected by FY25. iv. Barriers to entry in their business are very high due to heavy weight, closed tolerance and stringent quality requirements of OEMs. v. Happy Forgings has 66 large clients and 70% of its revenue is contributed by top 10 clients with whom the company has a relationship of 14-21 years. The company's total income increased by 38.81% YoY to INR 12,022.71 million in FY23. The company's PAT for FY22 was INR 1,422.89 million compared to INR 2,087.01 million in FY23. We recommend a subscribe to the issue as with the capex undertaken and to be undertaken has the potential to double earnings of the company as the utilisation ramps up to optimum levels coupled with interest savings on debt repayments, at the upper end of the price band the company is demanding a P/E multiple of 38x on the trailing 12-month earnings which is inline or below the valuations of comparable peers.

Key Financial & Operating Metrics (Consolidated)

In INR mn	Revenue	YoY (%)	EBITDA	EBITDA %	PAT	EPS	ROE	ROCE
FY21	5849.58	-	1587.439	27.14%	864.46	965.88	14.36	17.46
FY22	8600.45	47.03	2308.877	26.85%	1422.82	15.90	19.86	21.81
FY23	11965.29	39.12	3409.362	28.49%	2087.01	22.15	23.50	26.18

Issue Snapshot

Issue Open	19-Dec-23
Issue Close	21-Dec-23
Price Band	INR 808 - 850
Issue Size (Shares)	1,21,10,415
Market Cap (INR mln)	INR 33913.75

Particulars

Fresh Issue (INR mln)	INR 4000
OFS Issue (mln)	INR 6085.932
QIB	50%
Non-institutionals	15%
Retail	35%

Capital Structure

Pre Issue Equity	89499000
Post Issue Equity	9,42,04,882
Bid Lot	17 shares
Minimum Bid amount @ 808	INR 13736
Maximum Bid amount @ 850	INR 14450

Share Holding Pattern

	Pre Issue	Post Issue
Promoters	88.24%	87.40%
Public	11.7600%	12.60%

Particulars

Face Value	INR 2
Book Value	INR 147.36
EPS, Diluted	INR 22.15

Objects of the Issue

1. Purchase of equipment, plant and machinery- INR 1,711.26 million
2. Payment of borrowings - INR 1,527.60 million
3. General corporate purposes

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Investment Rationale:

Increasing share of machined components business volume boosting margins: The share of machined parts - a segment that enjoys higher realisation in forging - in the company's total volume has been consistently increasing and it has been able to source raw materials at a lower rate. This helped Happy Forgings enjoy the highest operating margin among peers. Happy Forging expanded capabilities to manufacture complex and safety-critical parts, resulting in a diverse product portfolio of machined parts such as crankshaft, transmission parts, suspension products, and other products for commercial vehicles, farm equipment, and off-highway vehicles. In addition, the company expanded capabilities to manufacture and supply components with applications in industries including oil and gas, power generation, railways, and wind turbines. As of FY23, Happy Forging is only the second company in India to have a 14,000-tonne forging press or higher and is among four companies in India that possess an 8,000-tonne forging press or higher. The diverse range of products and continuous efforts to develop new products have allowed the company to serve a wide range of industries and customers, strengthening its ability to attract new customers. Furthermore, Happy Forging has emerged as a leading player in the domestic crankshaft manufacturing industry with the second-largest production capacity for commercial vehicle and high horsepower industrial crankshafts. The company is focused on developing heavier high-precision critical and value-added products for multiple end-use industries, which typically have extremely closed tolerances. The company has consistently delivered EBITDA margins in the range of 27-28% over FY21-23. We expect improvement in margins by another 200-300bp over the coming quarters led by cost increasing share of machined parts revenue and also optimisation due to lower steel prices. Also there are strong barriers to entry in their business due to stringent quality requirements of OEMs. The products for HCV and Industrials are much more complex than passenger vehicles and hence margins are higher. Moreover, the growth of battery powered EVs are unlikely to impact the business as batteries are not capable of powering such heavy-duty off-highway vehicles. Additionally, customer and product approval processes are extremely lengthy.

Particulars	Fiscal 2023 Consolidated		Fiscal 2022 Consolidated		Fiscal 2021 Standalone		CAGR (Fiscal 2021 to Fiscal 2023)
	Amount (₹ million)	Percentage of Revenue from Sale of Products	Amount (₹ million)	Percentage of Revenue from Sale of Products	Amount (₹ million)	Percentage of Revenue from Sale of Products	
Revenue from Sale of Forged Products	2,277.15	21.34%	1,935.15	24.63%	1,485.38	27.12%	23.82%
Revenue from Sale of Machined Products	8,392.33	78.66%	5,920.50	75.37%	3,992.02	72.88%	44.99%
Revenue from Sale of Products	10,669.49	100.00%	7,855.65	100.00%	5,477.40	100.00%	39.57%

Expanding capacity at existing manufacturing facilities: Happy Forging operates three manufacturing facilities with two located at Kanganwal in Ludhiana, Punjab, and one at Dugri in Ludhiana, Punjab. While one of the manufacturing facilities at Kanganwal is dedicated to forging operations, the other two are equipped with both forging and machining capabilities. The company proposes to purchase new machinery and equipment to build up additional capacity for forging and machining operations from the Net Offer Proceeds. Some of the machineries intended for purchase include (i) hot forging press type GLF 10000R and (ii) automatic die holder, cassettes & die change system for forging press type GLF 10000 R. The new

machineries will allow Happy Forging to provide contingent backup to existing customers served with 8,000 and 14,000 tonne presses. The installation of new machinery and equipment will enable the company to increase production capacity, scale operations, onboard new customers, introduce new products, better serve existing customers, address the business requirements of large customers, improve customer service, and facilitate the growth strategy. Additionally, Happy Forging is in the process of commissioning a new 6,300-tonne forging press line, expected to be installed by June 2024. The company has also previously strategically increased capacity without compromising on return ratio, although 33% of its gross value of fixed assets was a result of capex incurred between FY22 and FY23. There is ample room for export growth - exports accounted for 20% of revenue in the first half of FY24 and that was significantly lower than its peers. The company offers an attractive value proposition for overseas customers by offering 15-20% lower prices than the current landed cost.

Long-standing relationships with customers across industries: The company has, through over 40 years of business operations, established long-standing relationships with several Indian and global customers across industries. It is among the few companies in India that manufacture and supply high precision safety critical components to leading OEMs including manufacturers of commercial vehicles, farm equipment, off-highway vehicles and industrial equipment and machinery for oil and gas, power generation, railways and wind turbine industries. It has a diversified customer base and it has served 66 customers in Fiscal 2023 and 59 customers in the six months ended September 30, 2023. Its focus on quality, providing customised solution to its customers and timely delivery of its product offerings have helped it establish and maintain long term relationships with its customers. During this process, it assisted this manufacturer with converting their cast iron crankshaft into a forged version. Additionally, it recommended the suitable steel that would match the mechanical properties of the casted version. As a result, it became a single source supplier of crankshaft to this manufacturer. 70% of its revenue is contributed by top 10 clients with whom the company has a relationship of 14-21 years. Its major commercial vehicle clients include M&M, American Axle and Manufacturing and SML ISUZU. Some of its major non-automotive segment clients are Kubota, Dana, Hendrickson, JCB, IBCC and Liebherr.

Valuation and outlook: We are positive upon Happy Forging due to: i. The company has better margins with lower valuation when compared with its peers. ii. The share of machined parts has been consistently increasing in the company's total volume, a segment that enjoys higher realisation in forging. It has also been able to source raw materials at a lower rate. This helped Happy Forgings enjoy the highest operating margin among peers. iii. The company's current forging capacity is 107,000 MTPA and machining capacity of 46,000 MTPA. The range of tonnage press is between 2,500 – 14,000T. A 6,300T press line is expected by FY24 while another 10,000T press is expected by FY25. iv. Barriers to entry in their business are very high due to heavy weight, closed tolerance and stringent quality requirements of OEMs. v. Happy Forgings has 66 large clients and 70% of its revenue is contributed by top 10 clients with whom the company has a relationship of 14-21 years. The company's total income increased by 38.81% YoY to INR 12,022.71 million in FY23. The company's PAT for FY22 was INR 1,422.89 million compared to INR 2,087.01 million in FY23. We recommend a subscribe to the issue as with the capex undertaken and to be undertaken has the potential to double earnings of the company as the utilisation ramps up to optimum levels coupled with interest savings on debt repayments, at the upper end of the price band the company is demanding a P/E multiple of 38x on the trailing 12-month earnings which is inline or below the valuations of comparable peers.

Income Statement				Balance Sheet			
Y/E (INR mn)	FY21	FY22	FY23	Y/E (INR mn)	FY21	FY22	FY23
Revenue	5849.58	8600.45	11965.29	Source of funds			
Expenses:				Equity Share Capital	89.50	179.00	179.00
Employee Cost	489.99	686.76	877.78	Reserves	6362.07	7697.14	9703.96
Total Expenses	4262.14	6291.58	8555.93	Total Share holders funds	6451.56	7876.13	9882.96
EBITDA	1587.44	2308.88	3409.36	Total Debt	72.09	88.00	110.43
EBITDA Margin %	27.14%	26.85%	28.49%	Current Liabilities	1755.44	2452.57	2566.44
Interest	117.84	71.59	124.76	Trade Payables	379.34	442.31	477.38
Depreciation	357.57	377.42	541.82	Total Non-Current Liabilities	534.87	969.89	812.22
Other Income	58.55	60.59	57.51	Total Liabilities	8741.88	11298.60	13261.61
PBT	1170.59	1920.46	2800.29	Application of funds			
PAT	864.46	1422.82	2087.01	Fixed Assets	4146.52	4561.91	6784.41
EPS	965.88	15.90	23.32	Capital Work in Progress	394.22	2122.55	747.52
				Cash and Bank	277.83	14.60	3.41
				Other current assets	108.82	87.87	33.93
				Inventory	1215.67	1839.84	1696.03
				Sundry Debtors	1655.69	2220.36	3080.58
				Total Assets	8741.88	11298.60	13261.61

Cash Flow				Key Ratios			
Y/E (INR cr)	FY21	FY22	FY23	Y/E (INR cr)	FY21	FY22	FY23
Profit Before Tax	1170.59	1920.46	2800.29	Growth Ratio			
Adjustment	456.21	401.95	712.04	Net Sales Growth(%)	4.81	47.03	39.12
Changes In working Capital	-789.13	-1088.56	-779.40	EBITDA Growth(%)	10.28	43.95	46.31
Cash Flow after changes in Working Capital	837.67	1233.85	2732.93	PAT Growth(%)	8.14	64.59	46.68
Tax Paid	-339.12	-431.08	-638.36	Margin Ratios			
Cash From Operating Activities	498.54	802.77	2094.57	Gross Profit	56.99	54.84	53.95
Cash Flow from Investing Activities	-586.85	-1656.63	-1724.54	PBIDTM	28.14	27.55	28.97
Cash from Financing Activities	96.72	825.19	-370.10	EBITM	22.03	23.16	24.45
Net Cash Inflow / Outflow	8.41	-28.67	-0.07	PBT	20.01	22.33	23.40
Opening Cash & Cash Equivalents	20.46	28.87	0.20	PAT	14.78	16.54	17.44
Closing Cash & Cash Equivalent	28.87	0.20	0.13	Return Ratios			
				ROA	10.56	14.20	17.00
				ROE	14.36	19.86	23.50
				ROCE	17.46	21.81	26.18
				Turnover Ratios			
				Asset Turnover(x)	0.71	0.86	0.97
				Inventory Turnover(x)	5.93	5.63	6.77
				Debtors Turnover(x)	3.86	4.44	4.51
				Fixed Asset Turnover (x)	1.39	1.57	1.66
				Solvency Ratios			
				Total Debt/Equity(x)	0.24	0.31	0.22
				Current Ratio(x)	1.91	1.73	1.91
				Quick Ratio(x)	1.21	0.98	1.25
				Interest Cover(x)	10.93	27.83	23.45

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