

**GNA Axles Ltd (GNA)**

**- Likely beneficiary of Auto cycle recovery**

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Recommendation : Buy  
CMP : Rs 221.95  
Sector : Auto Ancillary

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NSE Code : GNA  
BSE Code : 540124

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#### Financial break up

Market Cap (Rs. Cr) : 473  
EPS (FY22E) : 23.90  
PE : 9.29  
Face Value : Rs.10/-

#### Share Holding Pattern:

Promoters : 67.48  
Others : 32.52

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**Background:** GNA is a leading player in axle shafts and spindle manufacturing for heavy commercial vehicles and tractors in domestic market and has strong presence in export market. The company is today among the leading manufacturers of rear axle shafts used in on-highway and off-highway vehicular segments in India. GNA manufactures and supplies a diverse range of rear axle shafts, other shafts and spindles for the on-highway segment, i.e. for light commercial vehicles ("LCVs"), medium commercial vehicles ("MCVs") and heavy commercial vehicles ("HCVs") and other transport vehicles such as buses. The company also manufactures and supplies a diverse range of rear axle shafts and other shafts for the off-highway segment, i.e. for agricultural tractors and machinery, forestry and construction equipments, electric carts and other specialty vehicles used in mining and defense sectors.

#### Diverse product range

GNA currently manufactures a large variety of rear axle shafts and have the capacity to manufacture rear axle shafts of up to 165 kg input weight. The company has established a strong presence across various automotive segments including commercial vehicles and off-highway vehicles. In addition, the company also manufactures a range of spindles and other shafts for automotive application.

#### Marquee Clientele

GNA's domestic customers in the on-highway segment include major tier-1 suppliers such as Automotive Axles Limited and Dana Limited and HCV manufacturer such as Meritor HVS AB. In the off-highway segment, the company's domestic customers include major tractor manufacturers such as Mahindra & Mahindra Limited, TAFE, Escorts Limited and Claas India Private Limited. The company also export rear axle shafts, other shafts and spindles to various countries including USA, Sweden, Turkey, Brazil, Italy, Germany, Spain, Mexico, Japan, UK, France, China and Australia. GNA's major global customers include Meritor HVS AB, John Deere, Transaxle Manufacturing of America, Dana Limited and Kubota Corporation.

#### Strong Engineering, Product development & technological capability

GNA places strong emphasis on engineering and product development to enhance their product range and improve their manufacturing processes. The company has in-house metallurgical and metrological laboratories. The company has offered a number of cost reduction and value engineering proposals to their customers on the basis of in-house improvements in manufacturing processes which resulted in low input cost and low operation cost.

#### Outlook & Valuation

We recommend a **Buy** on GNA for long term investors. Given the Market leadership, Diverse product range, Marquee Clientele, Strong Engineering, Product Development & Technological capability, and Increasing Export market share are key positives for the stock. At the CMP of INR 221.95, the stock trades at 9.29x Consolidated EPS of FY22E. The key risks to the business include Steep increase in Raw Material cost, Slowdown in Auto Sector and Currency Fluctuations are the key risks of the company.

## **Investment Arguments**

### **Company Profile:**

GNA Axle (GNA) is a leading player in axle shafts and spindle manufacturing for heavy commercial vehicles and tractors in domestic market and has strong presence in export market. The company is today among the leading manufacturers of rear axle shafts used in on-highway and off-highway vehicular segments in India. Since their first supplies in 1995 and first exports in 2002-2003, the company has grown to production levels of more than 2.26 million components in Fiscal 2016. GNA manufactures and supplies a diverse range of rear axle shafts, other shafts and spindles for the on-highway segment, i.e. for light commercial vehicles (“LCVs”), medium commercial vehicles (“MCVs”) and heavy commercial vehicles (“HCVs”) and other transport vehicles such as buses. The company also manufactures and supplies a diverse range of rear axle shafts and other shafts for the off-highway segment, i.e. for agricultural tractors and machinery, forestry and construction equipments, electric carts and other specialty vehicles used in mining and defense sectors. GNA also manufactures solid and hollow spindles used in the axle assembly for various vehicles and equipments in the on-highway segment which they supply to their export customers. Over last couple of years GNA has increased its wallet share amongst its leading international customers by more than 2x. Further recently company has entered in new product line i.e. SUV which is expected to start contributing meaningfully from FY22. The company believes that with recovery in its key markets in FY22 and healthy financial position provides GNA a strong contender for rerating from the current valuation.

GNA has a large variety of Axle Shafts ranging from 1.5kg to 65kg & having capacity to produce up to 165kg producing about 2 million Axle Shafts annually. GNA’s long-standing global presence is owed to experience in the development and manufacture of Real Axle Shafts.

### **Leading Manufacturers of Axle Shafts in India**

GNA is among the leading manufacturers of axle shafts for commercial vehicles and off-highway vehicles in India. The company also have a considerable presence in export markets which is owed to experience in the development and manufacturing of axle shafts. GNA has been supplying components to domestic customers since 1995 and to overseas customers since 2002. On the basis of their market position and experience, the company believes that they have the ability to compete globally in measurable quality, cost, delivery and technology. With the domestic rear axle shaft market expected to grow at 10% CAGR over the next three years and with new opportunities expected to open up for export-oriented, low cost countries such as India the company believes that their leadership position provides them the platform to benefit from this growth, both domestically and globally.

### **Diverse product range**

GNA currently manufactures a large variety of rear axle shafts and have the capacity to manufacture rear axle shafts of up to 165 kg input weight. The company has established a strong presence across various automotive segments including commercial vehicles and off-highway vehicles. In addition, the company also manufactures a range of spindles and other shafts for automotive application.

GNA believes that they are insulated to a degree against fluctuation in demand for a specific product because of the wide range of products that they currently offer and the company’s

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ability to develop new products required by their customers. The company believes that their in-house engineering department and the research and development activities that they undertake in each of their product divisions which enables them to continuously innovate and develop new products and processes.

Further, within each of the product group (rear axle shaft, other shafts and spindles), the company manufactures a diverse range of products for different vehicle categories as given below:

**Rear axle shafts:**

in the on-highway segment, for SCVs, MCVs, HCVs and buses; and

in the off-highway segment, for agricultural tractors and machinery, forestry and construction equipments, electric carts and other specialty vehicles.

**Spindles:**

in the on-highway segment, for SCVs, MCVs, HCVs and buses; and

in the off-highway segment, for agricultural tractors and machinery, forestry and construction equipments, electric carts and other specialty vehicles;

**other shafts:**

in the on-highway segment, for SCVs, MCVs, HCVs and buses; and

in the off-highway segment, for agricultural tractors and machinery, forestry and construction equipments, electric carts and other specialty vehicles.

**Strong Presence in domestic & Export Markets - A natural hedge**

GNA is the leading player in axle shafts and spindle manufacturing for heavy commercial vehicles and tractors. The company has strong presence in domestic tractor market with market share of ~60% and also has high wallet share in major international CV Axle manufacturers like Meritor, Dana and American Axles. This places GNA in good position to reap the benefits from the revival in both domestic and major international markets like USA and Europe.

**Strong Engineering, Product Development and Technological Capabilities**

GNA places strong emphasis on engineering and product development to enhance their product range and improve their manufacturing processes. The company has in-house metallurgical and metrological laboratories. The company has offered a number of cost reduction and value engineering proposals to their customers on the basis of in-house improvements in manufacturing processes which resulted in low input cost and low operation cost. For example, one of the large customers, Mahindra & Mahindra Limited, has given GNA a cost reduction efficiency (CRE) performance award. GNA has also received Best Supplier award from TAFE and Commendable Performance award from John Deere.

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## **Increasing wallet share**

Over a period of last 1-2 years GNA has increased its wallet share amongst its leading international customers, which will provide significant growth vectors for the company as industry volumes recovers. Dearth of Tier 2 forging component manufacturers (components like drive shafts, axle shafts, spindles, knuckles and other small axle and transmission components) in North America and Europe for heavy truck segment gave GNA the opportunity to scale up its market share. Existing players in the regions are shutting down capacities of smaller products because of financial distress, cost pressure and challenges of technology upgradation. Hence Indian forging companies spear headed by Bharat Forge and other companies like RK Forgings and GNA Axle have been able to gradually establish strong hold and gain share in smaller forging products in North American heavy truck component market.

## **Commercial Vehicle segment**

The commercial vehicle segment is known to be the barometer of a country's economic progress and therefore it comes as no surprise that the last month of FY2020 has seen one of the biggest sales declines in recent times.

The CV segment has been hit with a number of growth impacting factors such as revised axle load norms, the shift to BS VI emission norms and also a demand crunch due to a prolonged economic slowdown. CV OEMs were fervently hoping for a decent uptick in BS IV-compliant vehicle sales in the last month of FY 2020 but Covid-19 pandemic has put brakes to those hopes. OEMs have shuttered their factories, dealers have closed operations and any hopes of discounted truck and bus sales were also dashed. Now, some dealers who still hold unsold BS IV stock will be battling to sell that or face losses. During the year 2019-2020 the total number of CV's manufactured / produced by the various OEM's was 7,52,022 against 11,12,405 thus showing a drop of 32.40 % as per SIAM. This drop has been after 4 years of continuous uptrend witnessed in the Domestic CV markets. GNA as it is in the business of manufacturing Axle Shafts and Spindles for the Commercial Vehicles, this drop in the demand of the Commercial Vehicles has dented the sales of the company also.

## **Marquee Clientele**

GNA's broad customer base for both the on-highway and off-highway segments and their customers are based in India and overseas. GNA's customers primarily include original equipment manufacturers ("OEMs") such as Mahindra & Mahindra Limited, John Deere, Tractors and Farm Equipment Limited ("TAFE"), and tier-1 suppliers to OEMs such as Automotive Axles Limited, Meritor HVS AB and Dana Limited. In Fiscal 2020, their domestic sales and export sales constituted 64.68% and 35.32% of their revenue from operations, respectively, on a consolidated basis. GNA's domestic customers in the on-highway segment include major tier-1 suppliers such as Automotive Axles Limited and Dana Limited and HCV manufacturer such as Meritor HVS AB. In the off-highway segment, the company's domestic customers include major tractor manufacturers such as Mahindra & Mahindra Limited, TAFE, Escorts Limited and Claas India Private Limited. The company also export rear axle shafts, other shafts and spindles to various countries including USA, Sweden, Turkey, Brazil, Italy, Germany, Spain, Mexico, Japan, UK, France, China and Australia. GNA's major global customers include Meritor HVS AB, John Deere, Transaxle Manufacturing of America, Dana Limited and Kubota Corporation.

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## **Manufacturing Facilities**

GNA has two manufacturing facilities: Unit I located in village Mehtiana, district Hoshiarpur, Punjab and Unit II located at village Gulabgarh Jattan, district Kapurthala, Punjab. Both of their manufacturing facilities are ISO/TS 16949:2009 certified for manufacture of rear axle shafts, other shafts and spindles for automotive applications. GNA's manufacturing units have a total annual manufacturing capacity of 2.30 million rear axle shafts, 0.40 million other shafts and 0.30 million spindles.

GNA's manufacturing facilities include machinery imported from various countries including Italy, Germany, Japan, China and Taiwan, used for various processes such as materials testing, forging, heat treatment, machining, induction hardening and packaging. Some of their significant machineries include 13" upsetter, direct drive screw press supported by robots, Lasco extrusion press supported by robots and electric heat treatment furnace, and direct drive screw press supported by robots for heavy axle shafts forgings. The company's machineries enable them to manufacture rear axle shafts up to input weight of 165 kg.

## **Raw Material Suppliers and Utilities**

The primary raw material required for manufacturing of their products is steel. Steel is procured locally from customer approved steel producers in the form of hot rolled bars and round corner squares. Procurement of material grades of steel is done in accordance with specifications/standards provided by the customers.

GNA purchases steel bars of specified quality and dimensions from various suppliers on a spot market basis. The company's steel suppliers include Vardhman Special Steels Limited, Gerdau Steel India Limited, Bhushan Power & Steels Limited, Jayaswal Neco Industries Limited and Aarti Steels Limited. The company believes that they typically enjoy competitive rates for their purchases given the volume of their purchases.

Inputs such as tools, furnace oils, spares and oil and lubricants are procured by the Company from local vendors on spot market basis.

The company has a dedicated high power electricity line from Punjab State Power Corporation Limited for both our manufacturing facilities. The company has installed a 10/12.5 M.V.A. 66/11 K.V. power transformer and 66 KV switch yard for each of their manufacturing units.

GNA's manufacturing facilities are also supported by 6 DG sets with the total aggregate capacity of 3,730 kVA. The company purchases diesel for their DG sets from open market.

GNA purchases the furnace oil required for forging/heat treatment in the spot market.

## **Sales and Marketing**

GNA is currently manufacturing and supplying axle shafts, shafts and spindles to domestic and global OEMs (including tier-1 suppliers to OEMs) spread across 13 countries in five continents. We have established a marketing network for procuring purchase orders from our existing and prospective domestic and international customers. We have entered into long term supply contracts with some of our customers while we supply components on purchase order basis for the rest of our customers.

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GNA has separate divisions for sales and marketing which cater to domestic and export sales, respectively. The company's marketing teams frequently visit the central purchasing offices of our customers and to the facilities of our customers where we supply the components. This mechanism not only helps their teams to be constantly in touch with customers but also keeps them abreast of the latest production levels/ demands of their customers for a particular product. GNA's field teams are constantly in touch with their marketing teams at their corporate office and keep them updated about the prospective demands for the company's products and accordingly the production teams in the company plan the production for a particular product for a particular customer. This also helps in building a long term relationship with their customers.

## Key Risks

**Increase in the Raw Material Prices:** GNA is likely to witness reduction in EBITDA margins in case its raw material cost increases steeply thereby impacting its margins.

**Slowdown in the Auto Sector:** Any slowdown in the Indian economy or global economy will result in lower demand which will impact the company's revenues & profitability.

**Currency rate fluctuations:** The company derives about 35.32% of its revenues from exports. Any significant change in currency rate fluctuations will impact the company.

## Financials

### P&L

P&L (Rs Cr)	FY18	FY19	FY20	FY21E	FY22E
Income from operations	670	928	909	669	846
Direct costs	473	663	550	473	594
Employee costs	32	33	41	32	42
Other expenses	94	120	235	108	133
Total operating expenses	567	783	785	581	727
EBITDA	103	145	125	89	120
Depreciation and amortisation	25	35	42	42	45
EBIT	78	110	82	46	74
Interest expenses	7	8	14	11	7
Other income	3	0	1	1	1
Profit before tax	74	103	70	36	68
Provision for tax	23	37	17	9	17
Profit after tax	51	66	53	27	51
Minority Interest	0	0	0	0	0
Share from associates	0	0	0	0	0
Adjusted Net Profit	51	66	53	27	51
EPS - Diluted	23.7	30.6	24.6	12.7	23.9



## Balance Sheet

Balance Sheet (Rs Cr)	FY18	FY19	FY20	FY21E	FY22E
Equity share capital	21	21	21	21	21
Preference Share Capital	0	0	0	0	0
Reserves & surplus	320	380	425	446	484
Shareholders funds	341	402	447	467	505
Secured loans	118	170	194	0	0
Unsecured loans	24	0	0	0	0
Borrowings	142	170	194	109	89
Minority interest	0	0	0	0	0
<b>Total Liabilities</b>	<b>484</b>	<b>571</b>	<b>641</b>	<b>576</b>	<b>594</b>
Gross block	392	464	521	571	601
Depreciation	201	235	277	319	364
Net block	191	229	244	252	237
Capital work in progress	0	16	61	0	0
Total fixed assets	191	245	306	252	237
Unrealised profit	0	0	0	0	0
Investments	0	0	0	0	0
Inventories	154	161	145	119	151
Sundry debtors	235	312	296	229	290
Cash and equivalents	26	0	21	66	44
Loans and advances	48	30	33	24	31
Other current assets	0	0	0	0	0
Total current assets	463	504	495	438	515
Sundry creditors and others	187	194	169	123	166
Provisions	10	13	11	11	11
Total CL & provisions	197	207	180	135	178
Net current assets	267	296	316	304	337
Net Deferred tax	-2	-3	-1	-1	-1
Misc expenditure	28	34	20	20	20
<b>Total Assets</b>	<b>484</b>	<b>571</b>	<b>641</b>	<b>576</b>	<b>594</b>



## Cash Flow Statement

Cash Flow Statement (Rs Cr)	FY18	FY19	FY20	FY21E	FY22E
Net profit	51	66	53	27	51
Add: Depreciation	25	35	42	42	45
Add: Misc expenses written off	0	0	0	0	0
Add: Deferred tax	0	1	-3	0	0
Add: Others	0	0	0	0	0
Gross cash flow	75	102	92	69	97
Less: Changes in W. C.	77	55	-1	-56	55
Operating cash flow	-2	47	94	126	41
Less: Capex	81	89	103	-11	30
Free cash flow	-83	-42	-10	137	11

## Key Financial ratio's

Key Ratio's	FY18	FY19	FY20	FY21E	FY22E
OPM(%)	15.37	15.63	13.75	13.30	14.18
Net Profit Ratio (%)	7.61	7.11	5.83	4.04	6.03
ROAE(%)	15.9	17.7	12.4	6	10.6
ROACE (%)	20.2	21.4	14	8.4	14.2
Debtors (days)	128	123	119	125	125
Current ratio	2.4	2.4	2.8	3.3	2.9
Debt/Equity	0.4	0.4	0.4	0.2	0.2
Inventory (days)	84	63	58	65	65
Payable (days)	100	74	66	65	70
Cash conversion cycle (days)	112	112	111	125	120
Debt/EBITDA	1.4	1.2	1.6	1.2	0.7
Adjusted debt/Equity	0.3	0.4	0.4	0.1	0.1

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