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Automotive Tyres

Safe hub in current storm

August 2020

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AUTOMOTIVE TYRES

05 August 2020

Safe hub in current storm

Despite recent setbacks, we expect the Indian tyre industry to grow at a 7% CAGR to ~Rs 720bn during FY20-FY23. Unlike other auto ancillaries, this industry is largely immune to the losses caused by Covid-19 due to its strong dependence on India's massive replacement market (~70% of sales). Rising aftermarket sales and benign rubber prices are also likely to assist margins. Most tyre manufacturers have cut capex plans for FY21 which will minimise balance sheet pressure. Our top picks in the sector are APTY, TVSS and JKI.

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Steady replacement demand to fuel growth: Following 5% demand growth over the past six years, we now expect domestic tyre demand to log a 7% revenue CAGR through FY20-FY23 to ~Rs 720bn – growth will be aided by a steady uptick in the replacement market, a likely rebound in OEM demand during FY22 and the continued decline in cheap Chinese truck & bus radial (TBR) imports due to heavy duties.

Resilient in the face of Covid-19: Over 70% of revenues for the Indian tyre industry are linked to the replacement market, where demand is largely insulated from Covid-19 headwinds. We estimate that the replacement demand will grow at 8% CAGR over FY20-FY23.

Benign rubber prices to assist margins: Natural rubber comprises 44% of the raw material cost for tyre companies, implying that its price movement is a key determinant of profitability. Prices of crude oil and natural rubber are more a function of geopolitical issues than pure demand and supply. Due to the pandemic, we believe that demand shortage in the broader market would keep natural rubber prices benign over the near term.

Top picks: We prefer Apollo Tyres (APTY) and JK Tyre (JKI) given their higher revenue exposure to the replacement market and robust earnings growth compared to peers – initiate with BUY ratings on both stocks. We also like MRF (ADD) for its all-round leadership and strong balance sheet. In the two-/three-wheeler segments, we prefer TVS Srichakra (TVSS: BUY) over CEAT (REDUCE), as we expect CEAT to deliver negative returns over the next three years, besides clocking a significant increase in its borrowings despite reduced capex. We also initiate coverage on Balkrishna Industries (BIL) with REDUCE as valuations look rich.

RECOMMENDATION SNAPSHOT

Ticker	Price	Target	Rating
APTY IN	108	135	BUY
BIL IN	1,310	1,300	REDUCE
CEAT IN	868	830	REDUCE
JKI IN	65	85	BUY
MRF IN	60,975	67,000	ADD
SRTY IN	1,410	1,780	BUY

Price & Target in Rupees | SRTY IN = TVSS |
 All closing prices as of 3 Aug 2020

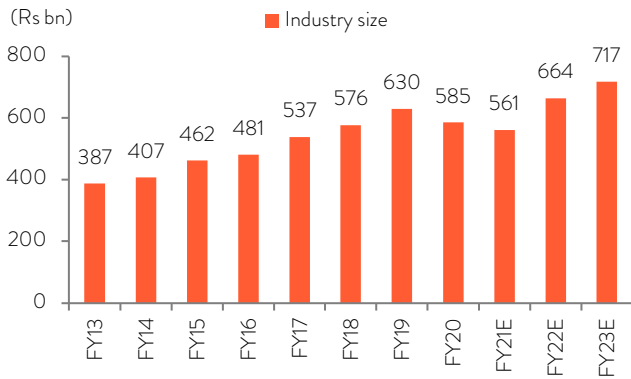


Contents

Focus charts	3
Investment thesis	4
Valuation snapshot.....	5
Domestic demand analysis: FY20-FY23E	6
Key demand drivers.....	7
Segmental demand forecasts	8
Natural rubber: The key to margins	11
Muted rubber price trends over past three years	11
What-if analysis: What if natural rubber prices rise?	12
Outlook and Valuations.....	13
Top picks	13
Key operational trends	13
Companies	
Apollo Tyres	17
Balkrishna Industries	27
CEAT.....	36
JK Tyre & Industries	45
MRF	55
TVS Srichakra	64

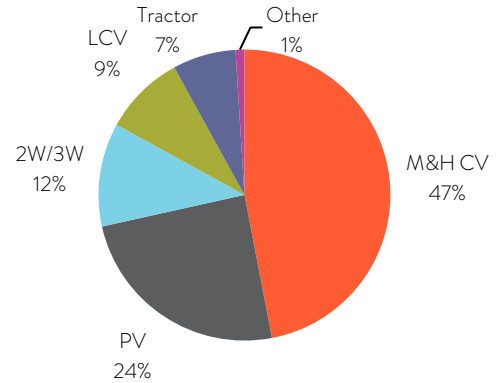
Focus charts

FIG 1 – INDIAN TYRE INDUSTRY EXPECTED TO GROW AT 7% CAGR DURING FY20E-FY23E



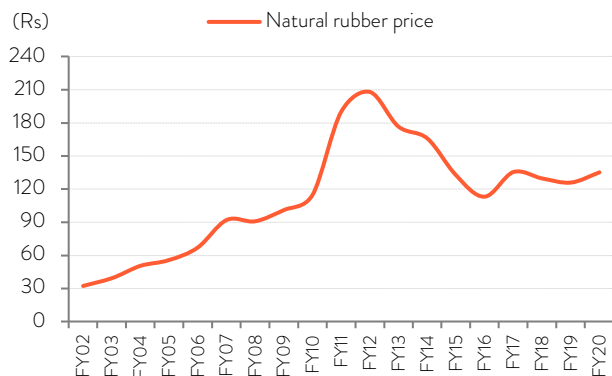
Source: ATMA, BOBCAPS Research, Companies

FIG 2 – MHCV AND PV TYRES DOMINATE THE INDUSTRY IN VALUE TERMS



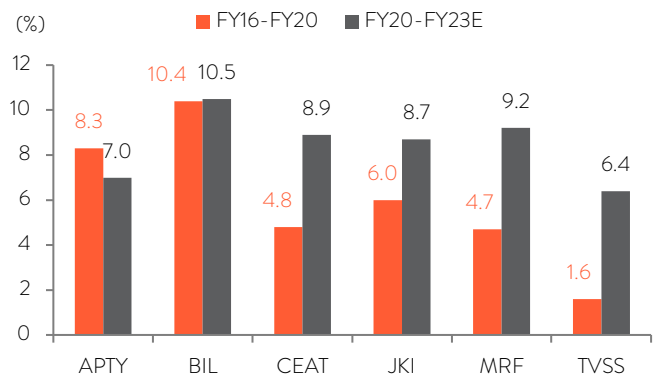
Source: ATMA, BOBCAPS Research

FIG 3 – RUBBER PRICE TREND – RSS4 KOTTAYAM



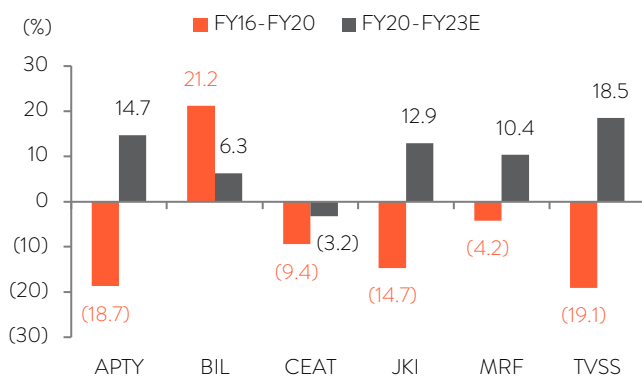
Source: Bloomberg, BOBCAPS Research, Rubber Board of India

FIG 4 – REVENUE CAGR – BIL, MRF AND JKI EXPECTED TO DELIVER HIGHEST REVENUE CAGR OVER FY20-FY23E



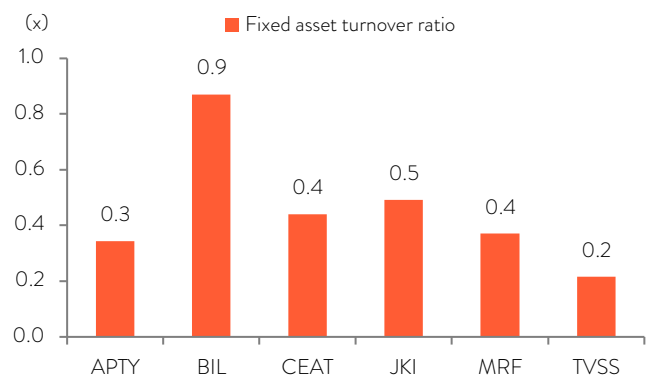
Source: Company, BOBCAPS Research

FIG 5 – ADJ. PAT CAGR – APTY, TVSS AND JKI EXPECTED TO DELIVER HIGH DOUBLE-DIGIT RETURNS



Source: Company, BOBCAPS Research | Note- Adj. PAT CAGR is adjusted for deferred tax adjustments in FY20

FIG 6 – FIXED ASSET TURNOVER RATIO (FY16-FY20) – BIL THE ONLY COMPANY THAT HAS MANAGED TO UTILISE ITS CAPACITY EFFICIENTLY



Source: Company, BOBCAPS Research

Investment thesis

Companies	Investment thesis
<p>Apollo Tyres (APTY) BUY TP: Rs 135 ▲25%</p>	<ul style="list-style-type: none"> Strong branding, higher exposure to the replacement market and a balanced product mix over the PV, MHCV and LCV tyre segments should aid a healthy volume CAGR of ~9% for APTY over FY20-FY23. Intended capex reduction (of ~Rs 10bn for FY21) should help minimise future borrowings and improve the balance sheet position, thus assisting better return ratios and earnings. We expect APTY's India revenue to register a 7% CAGR over FY20-FY23 and its European subsidiary to grow at 2%. Our valuation is set at 15x one-year fwd EPS, in line with the stock's 5Y average.
<p>Balkrishna Industries (BIL) REDUCE TP: Rs 1,300 ▼1%</p>	<ul style="list-style-type: none"> BIL specialises in the manufacture of tyres for the agricultural, industrial and OTR segments, with consistent demand in both Europe and the US. Operations have also been expanded to tap newer markets in Russia and Africa. Phase-II expansion at its carbon plant will take capacity from 80,000mtpa to 140,000mtpa in FY21 and shall give the company better cost control. Steady demand and best-in-class margins make the stock attractive, but premium valuations at 24x/23x FY22E/FY23E EPS leave little upside from current levels.
<p>Ceat (CEAT) REDUCE TP: Rs 830 ▼4%</p>	<ul style="list-style-type: none"> CEAT's lower revenue share of MHCV and PV tyres would hurt growth prospects, whereas higher dependence on OEM sales (~50% in 2W and PV segments) could also act as a hindrance to growth. Operating cash flow generation of ~Rs 22bn estimated over FY21-FY23 would be lower than expected capex plans over this period, warranting external debt borrowings – this could dilute ROE/ROCE by 260-270bps. Valuing the stock at 14x Sep'22E EPS, in line with peers, we arrive at a TP of Rs 830.
<p>JK Tyres (JKI) BUY TP: Rs 85 ▲31%</p>	<ul style="list-style-type: none"> Despite a 15% drop in revenues, JKI has cut debt by ~Rs 6.3bn in FY20 via prudent working capital management – addressing the key concern of high leverage. Being the cheapest and largest player in India's TBR tyre replacement market, JKI is bound to be the biggest beneficiary of the slowdown in Chinese imports due to the anti-dumping duty on China. Backed by steady replacement demand and benign rubber prices, we forecast a revenue/EBITDA/PAT CAGR of 9%/11%/13% over FY20-FY23 and value the stock at 7x one-year fwd EPS.
<p>MRF (MRF) ADD TP: Rs 67,000 ▲10%</p>	<ul style="list-style-type: none"> MRF commands a strong ~25% share in the Indian tyre market and derives ~70% of revenue from the replacement segment which should ensure revenue stability and above-industry margins. We estimate a healthy volume CAGR of 9% in MHCV and LCV tyres (60% share of domestic revenues) and 8% in PV tyres (21% share) for the company over FY20-FY23. We forecast revenue/EBITDA/PAT CAGR projections stand at 9%/10%/10% through FY23 (adj. for DTA) and value the stock at 22x one-yr fwd
<p>TVS Srichakra (TVSS) BUY TP: Rs 1,780 ▲26%</p>	<ul style="list-style-type: none"> TVSS is the largest supplier of 2W tyres to most leading domestic 2W OEMs with ~31% market share in the segment, and should benefit from the anticipated 6% volume CAGR in the 2W industry over FY20-FY23. In addition, management's focus on improving aftermarket sales should aid better margins and profitability. We value the stock at 14x Sep'22E EPS, at par with peers, to arrive at a Sep'21 TP of Rs 1,780.

Valuation snapshot

FIG 7 – VALUATION SUMMARY

Companies	Ticker	Price	Mcap (USD mn)	Rating	Target price	Upside/ Downside (%)	FY20-FY23E		
							Revenue CAGR	EBITDA CAGR	Adj. PAT CAGR
Apollo Tyres	APTY IN	108	828	BUY	135	25	7.0	10.0	14.7
Balkrishna Inds	BIL IN	1,310	3,400	REDUCE	1,300	(1)	10.5	12.2	6.3
CEAT	CEAT IN	868	470	REDUCE	830	(4)	8.9	11.7	(3.2)
JK Tyres	JKI IN	65	213.8	BUY	85	31	8.7	10.8	12.9
MRF Tyres	MRF IN	60,975	3,400	ADD	67,000	10	9.2	10.3	10.4
TVS Srichakra	SRTY IN	1,410	145	BUY	1,780	26	6.4	11.5	18.5

Companies	EPS (Rs)			P/E (x)			EV/EBITDA (x)			ROE (%)		
	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E
Apollo Tyres	5.1	8.4	9.9	21.2	12.9	11.0	5.8	5.1	4.6	2.6	4.5	5.1
Balkrishna Inds	42.6	54.2	58.7	31.0	24.4	22.5	19.8	16.5	14.7	14.3	15.8	15.1
CEAT	43.4	58.8	59.3	20.0	14.8	14.7	7.2	6.1	5.9	5.7	7.1	6.7
JK Tyres	3.6	10.5	14.5	18.0	6.2	4.5	7.0	5.3	4.7	3.5	9.5	12.1
MRF Tyres	2,326.8	2,943.5	3,163.5	26.2	20.7	19.3	11.8	9.3	8.4	7.6	8.8	8.6
TVS Srichakra	72.9	119.7	134.6	19.6	11.9	10.6	6.9	5.2	4.7	6.9	10.3	10.6

Source: Company, BOBCAPS Research

FIG 8 – COST BREAKUP FOR FY23E (AS PERCENTAGE OF SALES)

Companies	Raw material costs	Employee costs	Other expenses	EBIDTA margin
APTY	55.0	14.9	17.4	12.7
BIL	44.0	5.4	23.3	27.3
CEAT	58.3	7.4	22.7	11.6
JKT	60.5	10.5	17.0	12.0
MRF	59.5	8.1	17.4	15.0
TVSS	56.5	13.5	18.0	12.0

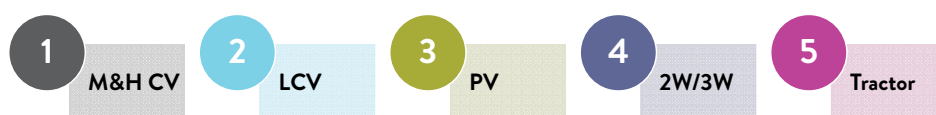
Source: Company, BOBCAPS Research

Domestic demand analysis: FY20-FY23E

Following 5% demand growth during FY15-FY20, we now expect domestic tyre demand to log a 7% revenue CAGR through FY20-FY23 aided by steady replacement market growth, a rebound in OEM demand during FY22 and continued lower imports of cheap Chinese truck & bus radials (TBR) due to duty imposition.

We believe truck, bus and passenger vehicle tyres will help the growth, with added support from the two- and three-wheeler segments. In our view, demand will be relatively immune to Covid-19 headwinds due to the large replacement market for tyres (~70% of industry sales).

FIG 9 – SEGMENT PREFERENCE BY RANK



Source: Company, BOBCAPS Research

FIG 10 – SEGMENT-WISE REVENUE MIX, FY20E

Segment (%)	APTY	BIL	CEAT	JKT	MRF	TVSS
MHCV	48	-	31	61	50	-
PCR	39	-	15	24	21	-
LCV	5	-	11	-	10	-
2W/3W	1	-	31	6	13	100
Others	7	100	12	9	6	-

Source: Company, BOBCAPS Research

- MHCV/LCV:** We expect strong demand revival to aid a 9% volume CAGR in medium and heavy commercial vehicle (MHCV) and light commercial vehicle (LCV) tyres over FY20-FY23. An increase in average daily runs due to e-pass, healthy replacement demand and a lower base will support MHCV tyre sales growth. Investment revival in infrastructure and manufacturing and an overall economic upturn are likely to bolster demand for MHCVs and LCVs over the next 2-3 years.
- PV:** Passenger vehicles are expected to revert to long-term growth trends as the economy starts turning favourable, with the tyre segment logging an estimated 8% CAGR over FY20-FY23.
- 2W:** For the next two years, the two-wheeler tyre subsegment is forecast to grow moderately (6% CAGR), supported by the need to transition from public mobility to private mobility amid coronavirus fears.
- Tractor:** The tractor tyre subsegment is currently growing strong and should clock a 9% volume CAGR during FY20-FY23.

Key demand drivers

Strict implementation of overloading rules

Over 70% of the trucks and heavy goods carriages registered in India indulge in overloading. The Motor Vehicle Amendment Bill 2019 has omitted an earlier provision that allowed extra load after levying a charge. States such as Uttar Pradesh, Rajasthan and Delhi have already started imposing strict penalties which include monetary fines along with impounding of the vehicle for a minimum of 48 hours. Strict implementation will boost vehicle demand.

Cheap Chinese imports no longer a concern

China's tyre industry, the largest in the world, is estimated to experience a rapid 10% CAGR until 2022 as the country's leading manufacturers upgrade technology and scale to meet global norms. India's increasing tyre imports from China were a mounting cause of concern for the domestic industry. Chinese radial tyres are 25-30% cheaper than those manufactured in India and have thus captured a large chunk of the replacement market.

As per ATMA, roughly 25% of domestic replacement demand for TBRs was met through imported tyres. China's share of tyre imports in India stands at ~70%. ATMA was of the view that massive surplus capacities and export subsidies in China led to tyres being dumped in the Indian replacement market.

FIG 11 – CHINESE TBR IMPORTS WERE 25-30% CHEAPER THAN INDIAN RADIALS

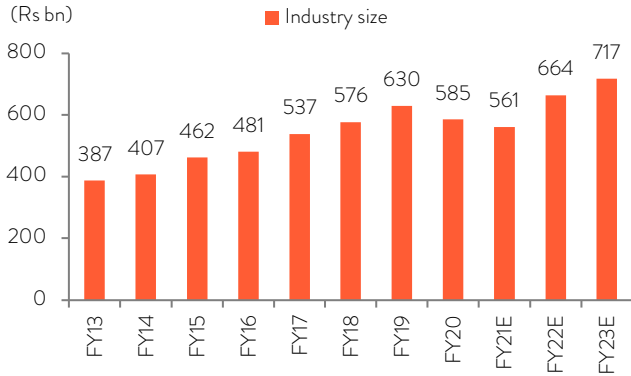
Particulars	China TBR	India TBR
Average import price per tyre	~Rs 9,400 (US\$ 140)	-
Landed price after GST @ 28%	Rs 12,000	-
Distribution costs & retail margin	Rs 1,500-2,000	-
Total price	Rs 13,500-14,000	Rs 18,000

Source: BOBCAPS Research

Whereas Chinese TBRs were priced at Rs 13,500-14,000, Indian TBRs started at a much higher Rs 18,000. Thus, despite a growing market, domestic players struggled to gain volume share in the TBR replacement market. In Sep'19, the Indian government imposed additional countervailing duties on Chinese tyre imports for a period of five years, over and above the existing anti-dumping duty – consequently, this price differential has narrowed to less than 10%, creating a more level playing field for Indian manufacturers.

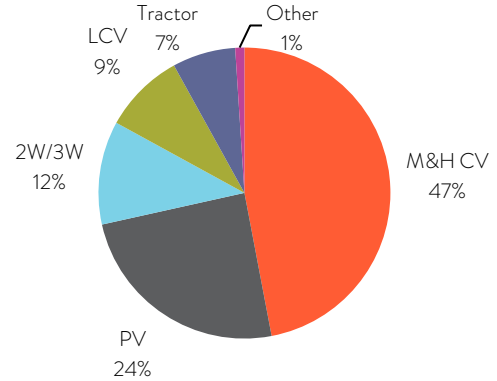
Segmental demand forecasts

FIG 12 – INDIAN TYRE INDUSTRY EXPECTED TO GROW AT 7% CAGR DURING FY20E-FY23E



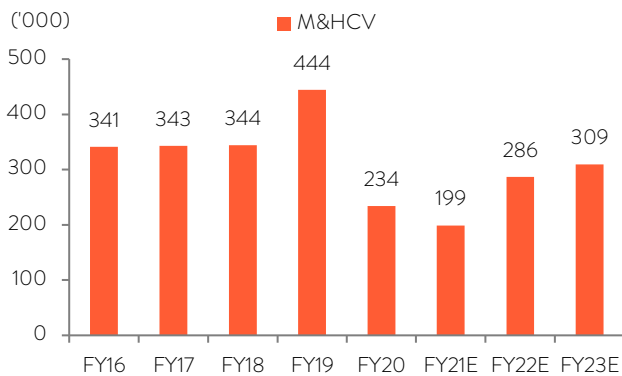
Source: ATMA, BOBCAPS Research, Companies

FIG 13 – MHCV AND PV TYRES DOMINATE THE INDUSTRY IN VALUE TERMS



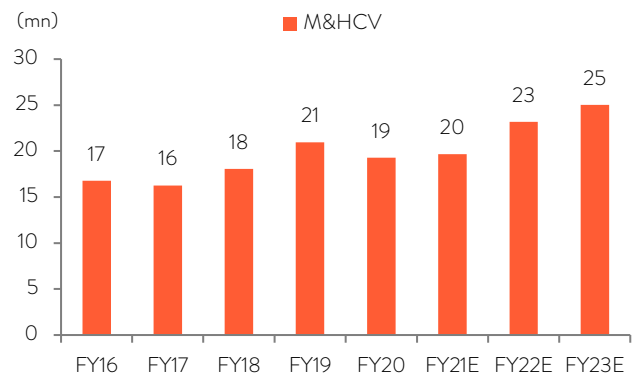
Source: ATMA, BOBCAPS Research

FIG 14 – AFTER SLOWDOWN IN FY20-FY21E, EXPECT SHARP RECOVERY IN MHCV PRODUCTION IN FY22E



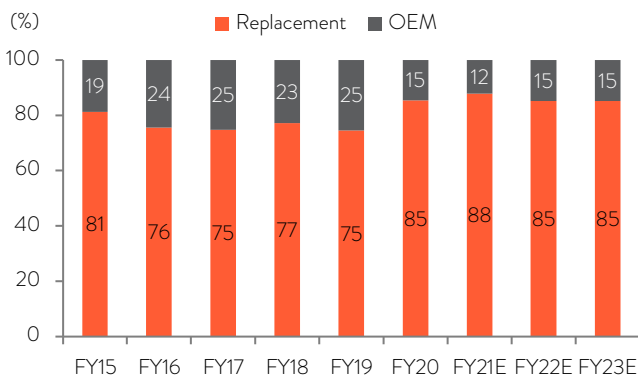
Source: SIAM, BOBCAPS Research

FIG 15 – DESPITE LOW OEM PRODUCTION, MHCV TYRE GROWTH STEADY DUE TO REPLACEMENT DEMAND



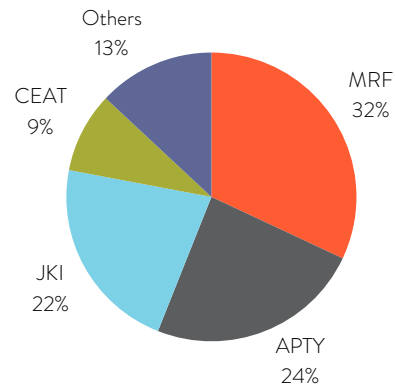
Source: ATMA, BOBCAPS Research

FIG 16 – LOWER OEM OUTPUT HAS TILTED SALES MIX IN FAVOUR OF AFTERMARKET FOR MHCV TYRES



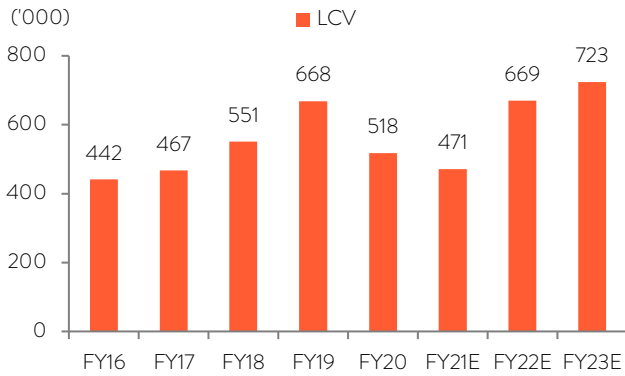
Source: Companies, BOBCAPS Research

FIG 17 – MHCV TYRE MARKET SHARE – MRF, JKI AND APTY DOMINATE THE SEGMENT



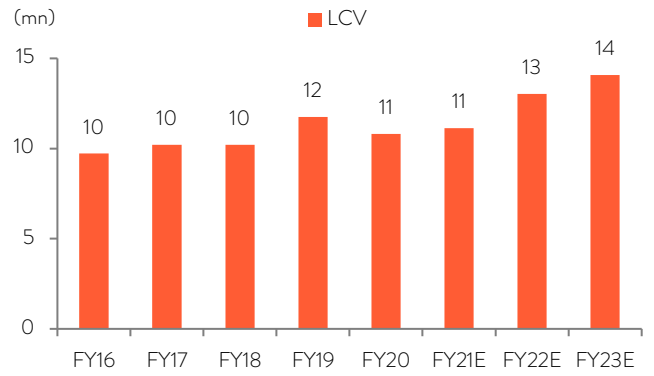
Source: Companies, BOBCAPS Research

FIG 18 – LCV PRODUCTION EXPECTED TO GET BOOST FROM HIGHER E-TRADE, HUB-&-SPOKE FORMATION



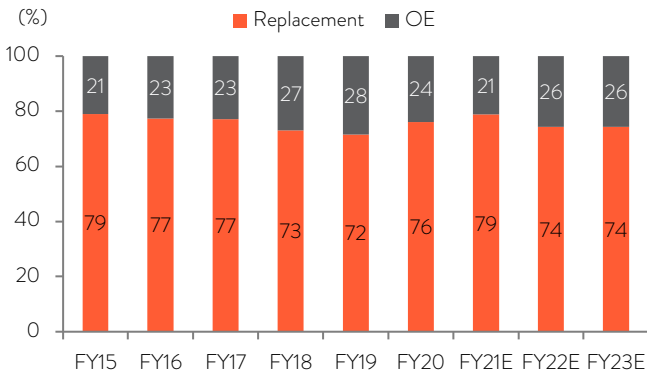
Source: SIAM, BOBCAPS Research

FIG 19 – LCV TYRE PRODUCTION AIDED BY STEADY GROWTH IN REPLACEMENT MARKET



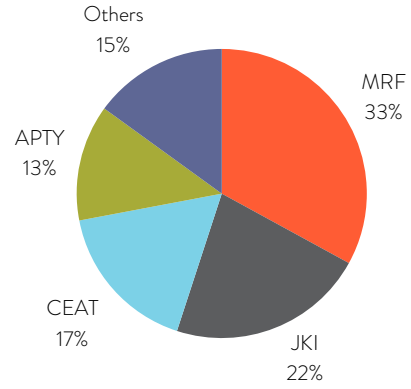
Source: ATMA, BOBCAPS Research

FIG 20 – LCV TYRE CHANNEL MIX SHOWS STEADY MIX



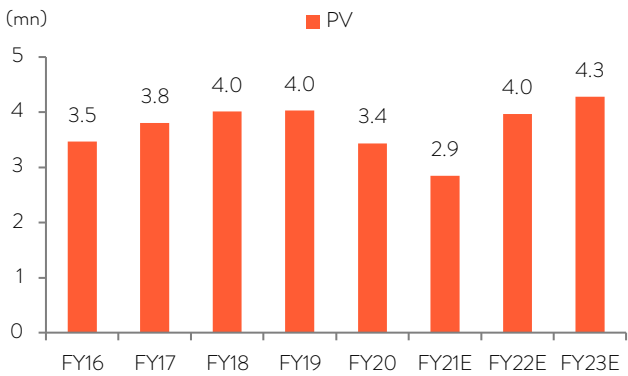
Source: Companies, BOBCAPS Research

FIG 21 – LCV TYRE MARKET SHARE – MRF AND JKI DOMINATE THE SEGMENT



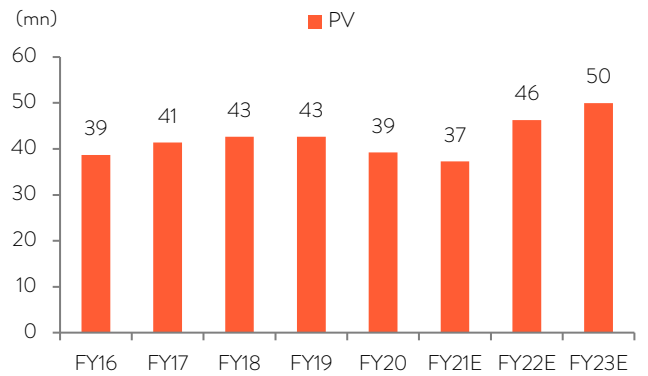
Source: Companies, BOBCAPS Research

FIG 22 – PV PRODUCTION TO REBOUND IN FY22E ON LOW BASE AND ECONOMIC RECOVERY



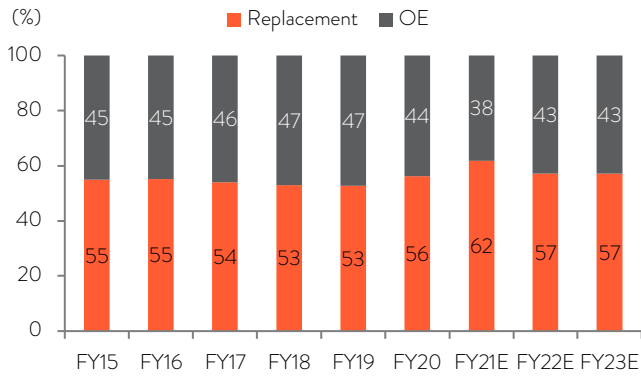
Source: SIAM, BOBCAPS Research

FIG 23 – PV TYRE PRODUCTION AIDED BY STEADY REPLACEMENT DEMAND



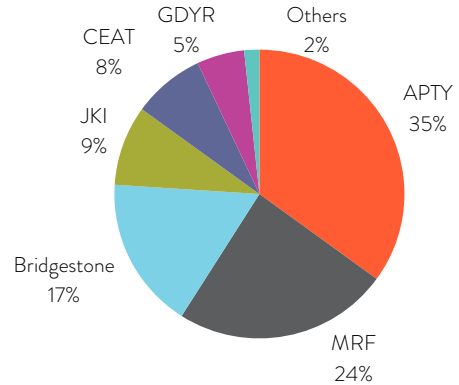
Source: ATMA, BOBCAPS Research

FIG 24 – PV TYRE CHANNEL MIX – UNLIKE T&B, PV TYRE DEMAND MORE EQUALLY SPLIT



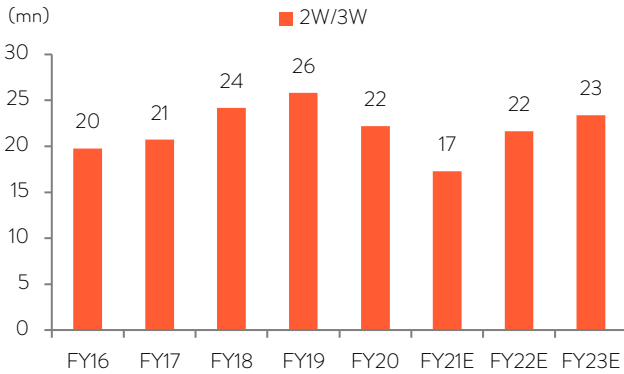
Source: Companies, BOBCAPS Research

FIG 25 – PV TYRE MARKET SHARE – APTY AND MRF DOMINATE THE SEGMENT



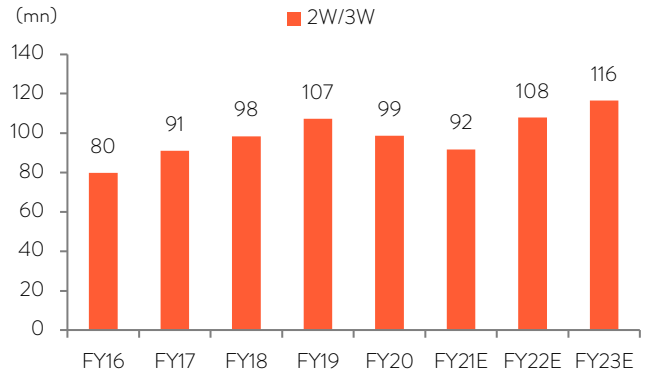
Source: Companies, BOBCAPS Research

FIG 26 – 2W PRODUCTION EXPECTED TO GET BOOST FROM RURAL RECOVERY AND PRIVATE MOBILITY



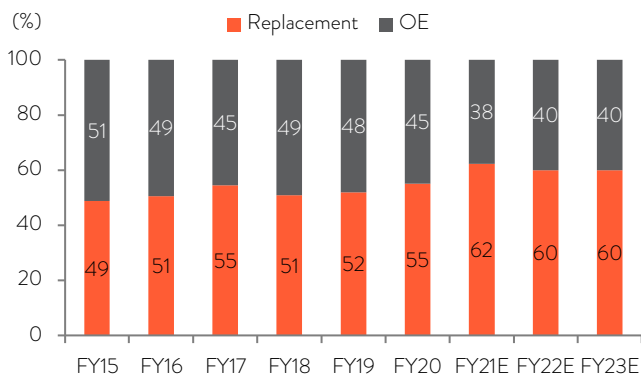
Source: SIAM, BOBCAPS Research

FIG 27 – 2W/3W TYRE PRODUCTION BENEFITS FROM LARGE AFTERMARKET FOR 2Ws



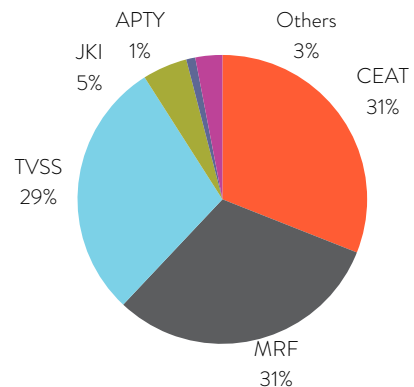
Source: ATMA, BOBCAPS Research

FIG 28 – 2W/3W TYRE CHANNEL MIX CURRENTLY SHOWS SIMILAR DEMAND FROM OEM AND REPLACEMENT MARKET



Source: Companies, BOBCAPS Research

FIG 29 – 2W/3W TYRE MARKET SHARE – CEAT, MRF AND TVSS CONTROL ~90% OF THE MARKET



Source: Companies, BOBCAPS Research

Natural rubber: The key to margins

Since natural rubber comprises 44% of the total raw material cost for tyre companies, its price movement affects profitability to a very large extent. Prices of crude oil and natural rubber are more a function of geopolitical issues than pure demand and supply. Due to the pandemic, we believe that demand shortage in the broader market would keep natural rubber prices benign in the near term.

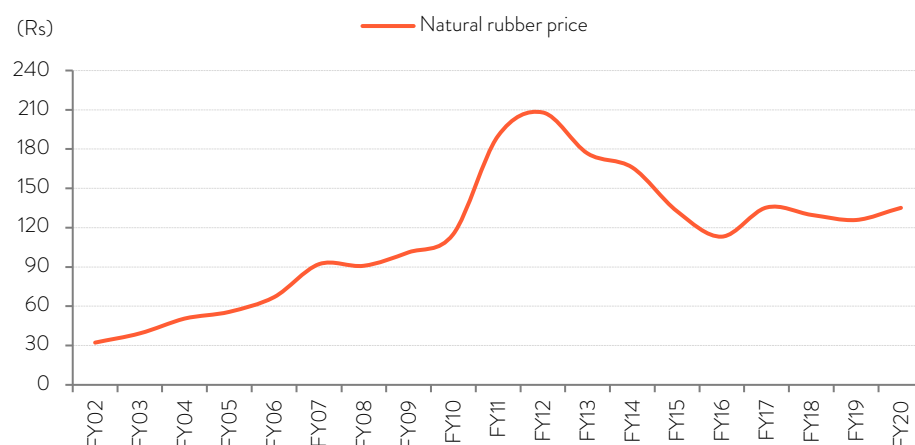
Muted rubber price trends over past three years

In 2018, the global natural rubber industry was at a low ebb as a result of weak economic fundamentals, with prices spiralling into a choppy downtrend and repeatedly hitting record lows. An uptick in the middle of 2018 was not enough to invigorate the sluggish industry. By the year-end, the market still hovered at the bottom and showed no signs of recovery. In 2019, global natural rubber prices continued to set all-time lows. We expect this trend to persist in 2020 before levelling off and perhaps picking up next year.

The regional structure of global natural rubber supply and demand is uneven. China consumes the most natural rubber in the world at 41% of the global total, but its output forms less than 6% of the total, as per a Global and China Natural Rubber Industry Report, 2017-2021. Critical shortages lead to heavy dependence on imports. Yet in 2018, Chinese imports stopped rising and instead declined by 7.1% to 2,600kt on an annualised basis on account of trade tensions between China and the US, as well as lower demand from end-user markets such as cars and heavy trucks.

Thailand, Indonesia, Malaysia, India, Vietnam and China are the world’s top six natural rubber producers, contributing 86.5% to global output in 2018. More than 28mn tonnes of rubber were produced in 2018, of which ~47% was natural. Since the bulk is synthetic, which is derived from petroleum, the price of natural rubber is also determined, to a large extent, by the prevailing global price of crude oil.

FIG 30 – RUBBER PRICE TREND – RSS4 KOTTAYAM



Source: Bloomberg, BOBCAPS Research, Rubber Board of India

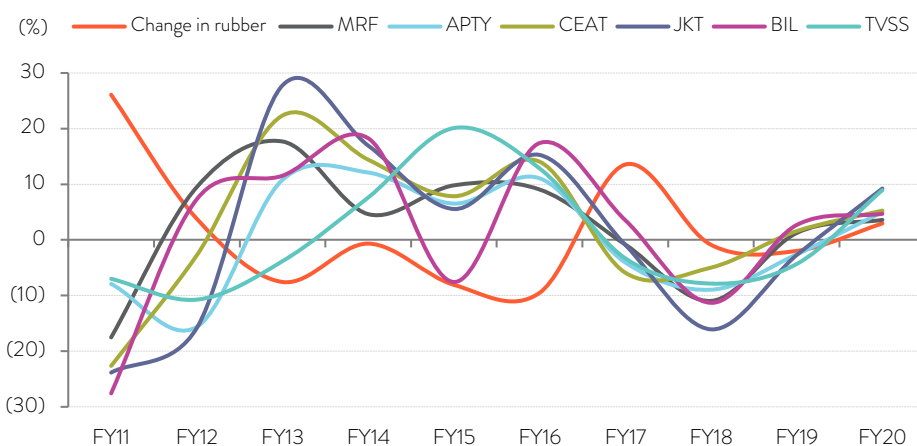
What-if analysis: What if natural rubber prices rise?

Prices of crude oil and natural rubber depend more on geopolitical issues than on pure demand and supply. We take a ‘what-if’ approach to understand the impact of rubber prices on margins. Natural rubber forms ~44% of the total raw material cost of tyre companies and hence its price movement has a substantial impact on tyre company profitability.

The chart below highlights the strong inverse relationship between rubber prices and margins. Historically, tyre companies had not been in a position to pass on any sudden, major change in prices of rubber and thus did not command P/E multiples at par with other auto ancillaries.

In our view, demand shortage due to the pandemic could keep natural rubber prices benign in the near term. One additional buffer that we believe these companies have established is the passing along of price rises. In the last 15 months, prices of tyres have remained steady. So, any slight increase in costs can easily be passed on to end-consumers, shielding margins in the near term.

FIG 31 – GROSS MARGINS OF TYRE COMPANIES INVERSELY CORRELATED TO RUBBER PRICE MOVEMENT



Source: Companies, BOBCAPS Research, Rubber Board of India

Outlook and Valuations

Overall, we estimate that the Indian tyre industry is set to reach a value of ~Rs 720bn by FY23 from ~Rs 590bn in FY20. Unlike other auto ancillaries, this industry is largely immune to the losses caused by Covid-19 due to its strong dependence on India’s large replacement market (~70% of sales). Higher aftermarket sales and benign rubber prices are also expected to assist margins. Most tyre manufacturers have cut capex planned for FY21 which will minimise balance sheet pressure. APTY, TVSS and JKI are our top picks in the sector.

Top picks

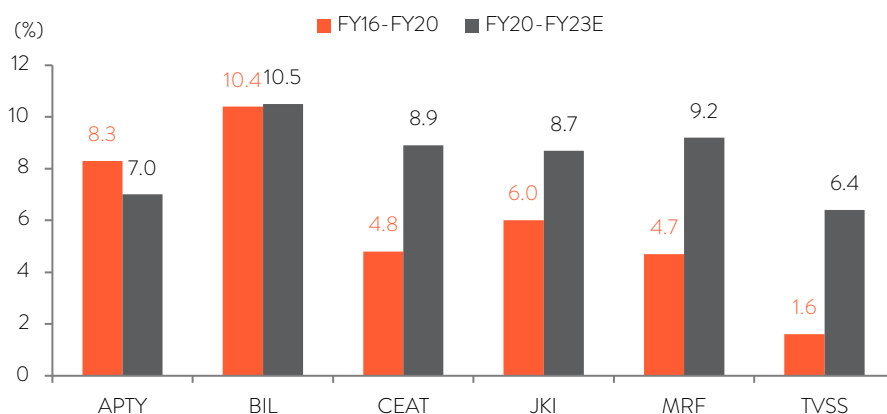
We prefer APTY and JKI due to their higher revenue share from replacement demand (~70%), and initiate on both players with BUY ratings. MRF (ADD) remains the most consistent player given its leadership in several segments, but premium valuations leave little upside from current levels.

In the 2W/3W segments, we believe tyre manufacturers could witness moderate growth. TVSS (BUY) is our preferred pick over CEAT (REDUCE) as we expect the latter to deliver negative returns over the next three years, apart from a significant increase in borrowings despite reduced capex. We also initiate coverage on BIL with REDUCE as valuations look rich.

Key reasons behind all our stock preferences are steady revenue growth, leading market positions and strong brand recall in the replacement segment. Soft rubber prices would benefit all companies but stronger market positioning in different subsegments gives our selected players an advantage on margins. Also, the benefit of lower Chinese imports in the TBR segment will accrue mainly to JKI, APTY and MRF.

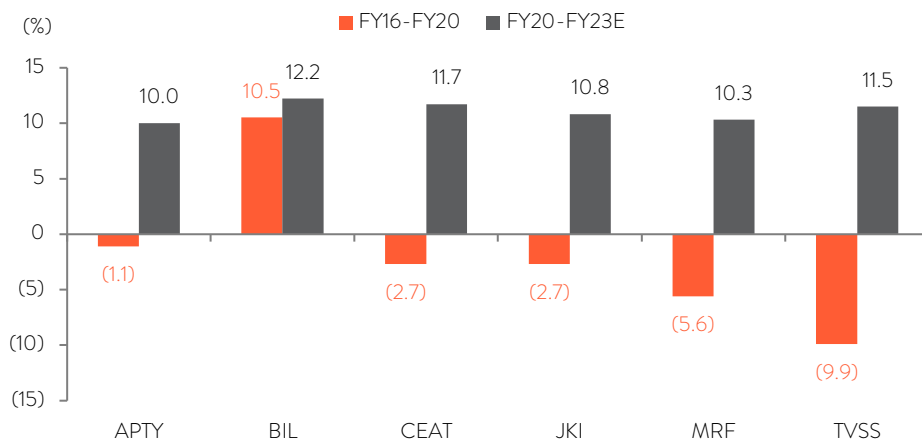
Key operational trends

FIG 32 – REVENUE CAGR – BIL, MRF AND JKI EXPECTED TO DELIVER HIGHEST REVENUE CAGR OVER FY20-FY23E



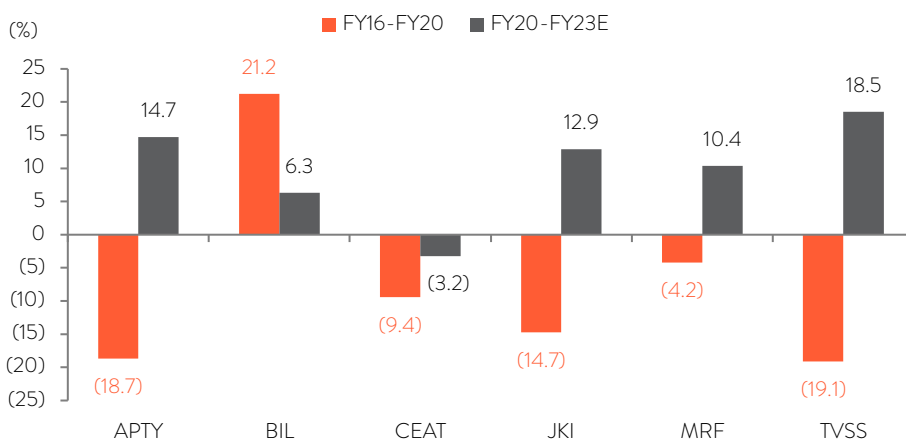
Source: Company, BOBCAPS Research

FIG 33 – EBITDA CAGR – MOST COMPANIES SHOULD DELIVER STEADY EBITDA GROWTH DUE TO LOWER RM COSTS



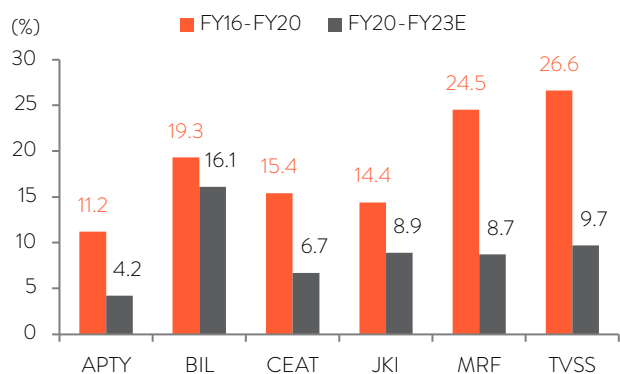
Source: Company, BOBCAPS Research

FIG 34 – ADJ. PAT CAGR – APTY, TVSS AND JKI EXPECTED TO DELIVER HIGH DOUBLE-DIGIT RETURNS



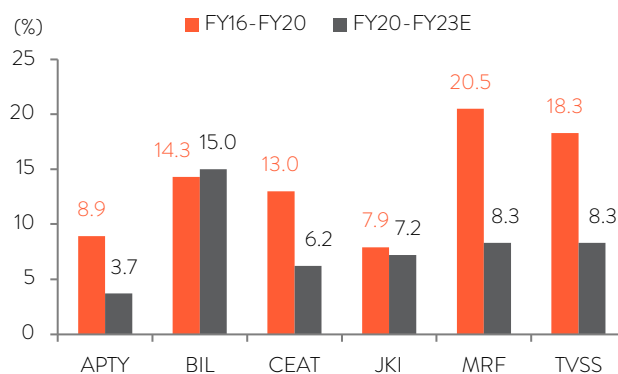
Source: Company, BOBCAPS Research | Note: Adj. PAT CAGR is adjusted for deferred tax adjustments in FY20

FIG 35 – AVERAGE ROE TO DECLINE ACROSS THE BOARD



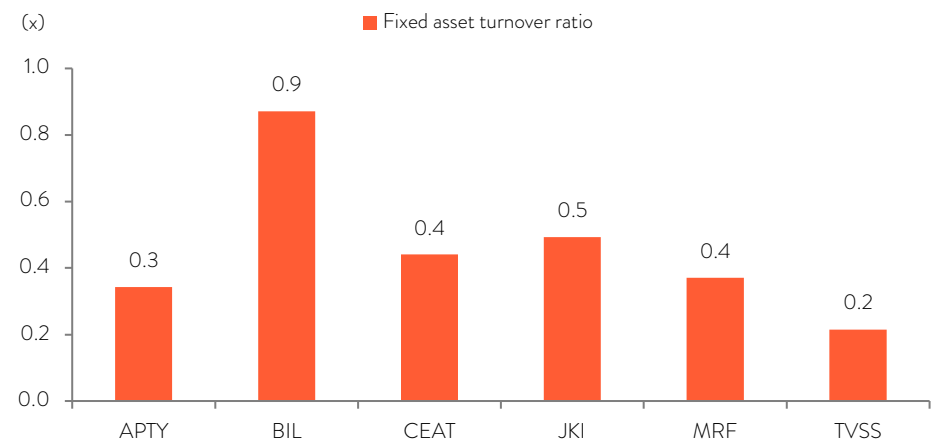
Source: Company, BOBCAPS Research

FIG 36 – AVERAGE ROCE TO SHOW SIMILAR TRENDS



Source: Company, BOBCAPS Research

FIG 37 – FIXED ASSET TURNOVER RATIO (FY16-FY20) – BIL THE ONLY COMPANY THAT HAS MANAGED TO UTILISE ITS CAPACITY EFFICIENTLY



Source: Company, BOBCAPS Research



Companies

BUY

TP: Rs 135 | ▲ 25%

APOLLO TYRES

| Auto Components

| 05 August 2020

Demand recovery, steady margins & slashed capex to aid growth

Deriving ~87% of its revenues from truck bus tyres and passenger vehicle tyres, Apollo Tyres (APTY) is poised to be the largest beneficiary of an anticipated revival in MHCVs & PVs. We expect APTY to clock a 9% volume CAGR over FY20-FY23e, even as replacement demand and benign rubber prices should aid steady EBITDA margins of ~13%. APTY has slashed FY21 capex which will assist net cash flows and return ratios. We are bullish on the tyre sector and APTY is among our top picks – initiate with BUY and a TP of Rs 135.

Mayur Milak | Nishant Chowhan, CFA
 research@bobcaps.in

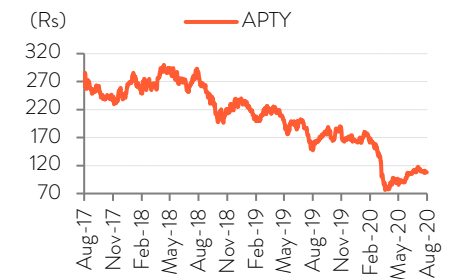
Healthy volume and margin outlook: Considering APTY's product profile spanning MHCV, LCV and PV tyres, strong branding and high exposure to the domestic replacement market, we expect the company to log a brisk 9% volume CAGR over FY20-FY23e. Raw material prices, especially for natural rubber and crude derivatives, are forecast to remain soft – this coupled with high replacement market exposure (>70% of revenue) should sustain operating margins at ~13% levels through to FY23.

Ticker/Price	APTY IN/Rs 108
Market cap	US\$ 822.6mn
Shares o/s	572mn
3M ADV	US\$ 11.9mn
52wk high/low	Rs 197/Rs 73
Promoter/FPI/DII	41%/23%/17%

Source: NSE

Capex cuts to ease balance sheet pressure: Management intends to incur capex of Rs 20bn in FY21 vs. Rs 30bn planned earlier. The company recently raised ~Rs 11bn through a convertible preference share allotment. With lower borrowings than earlier planned, we expect a healthy balance sheet position. This will not only assist return ratios (ROE to improve from 2.8 in FY21e to 5.2 by FY23E) but also augment overall earnings.

STOCK PERFORMANCE



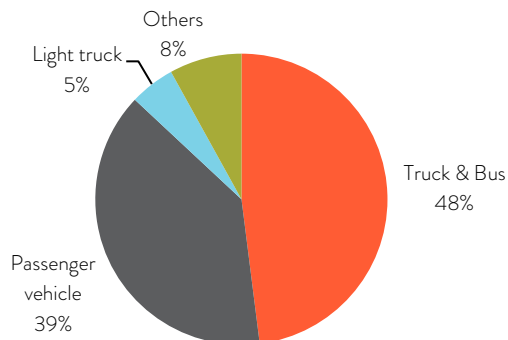
Initiate with BUY: We expect APTY's India revenue to register a 7% CAGR over FY20-FY23 and its European subsidiary to grow at 2%. Overall, we project a revenue/EBITDA/PAT CAGR of 7%/10%/15% (adj for deferred tax in FY20) over FY20-FY23. Valuing the stock at 15x Sep'22 EPS, which is in line with the stock's five-year average, we initiate coverage with BUY and a TP of Rs 135.

KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue (Rs mn)	175,488	163,270	152,170	182,924	199,971
EBITDA (Rs mn)	17,762	19,155	19,407	23,225	25,476
Adj. net profit (Rs mn)	6,798	4,764	2,922	5,333	6,277
Adj. EPS (Rs)	14.5	8.3	5.1	8.4	9.9
Adj. EPS growth (%)	(6.1)	(29.9)	(38.7)	64.4	17.7
Adj. ROAE (%)	6.8	4.8	2.6	4.5	5.1
Adj. P/E (x)	7.4	13.0	21.2	12.9	10.9
EV/EBITDA (x)	5.5	5.4	5.8	5.1	4.6

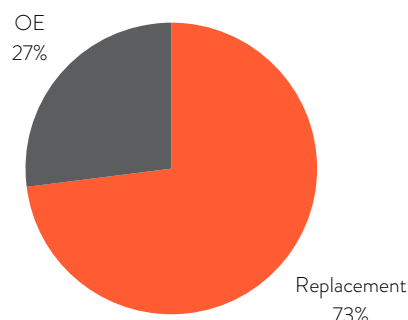
Source: Company, BOBCAPS Research

FIG 1 – RECOVERY IN T&B AND PV TYRES (~87% OF ITS REVENUES) TO BENEFIT REVENUE GROWTH (FY20)



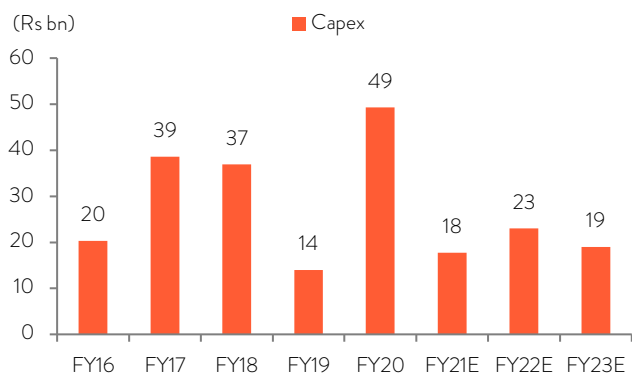
Source: Company, BOBCAPS Research

FIG 2 – HIGH PROPORTION OF SALES FROM REPLACEMENT MARKET TO ASSIST STEADY GROWTH



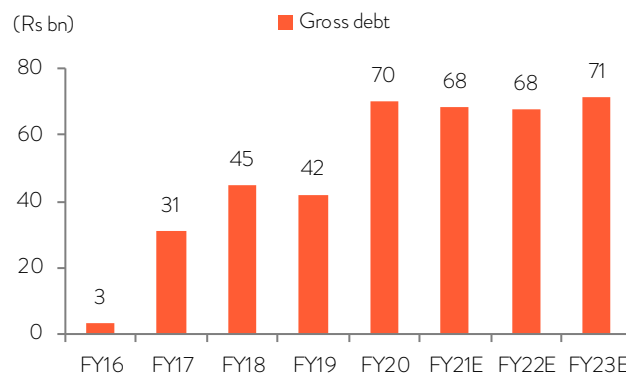
Source: Company, BOBCAPS Research

FIG 3 – SIGNIFICANT SLASH IN CAPEX IN FY21 TO RATIONALISE CASH FLOWS AND RETURN RATIOS



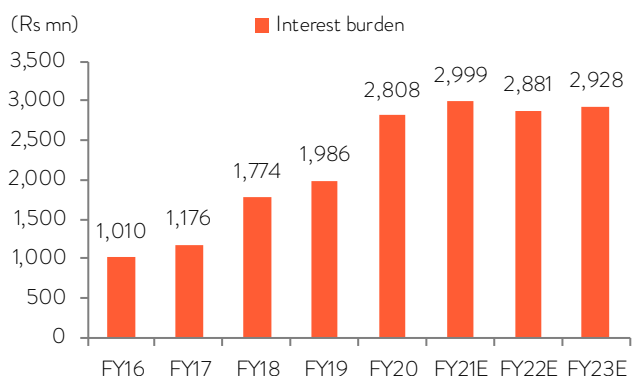
Source: Company, BOBCAPS Research

FIG 4 – RISING GROSS DEBT TO PLATEAU DUE TO LOWER CAPEX AND STEADY GROWTH



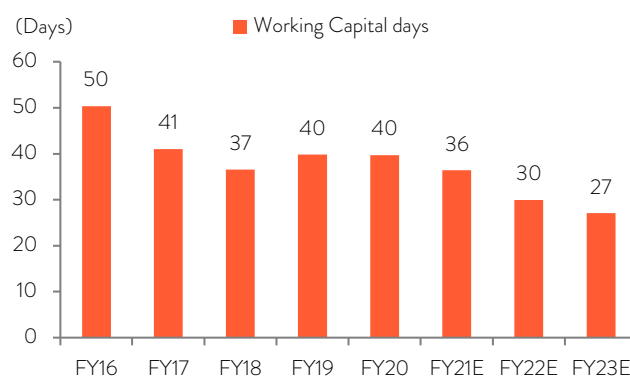
Source: Company, BOBCAPS Research

FIG 5 – INTEREST BURDEN – A CAUSE OF CONCERN



Source: Company, BOBCAPS Research

FIG 6 – EFFICIENT WORKING CAPITAL TREND ASSISTING BETTER CASH MANAGEMENT



Source: Company, BOBCAPS Research

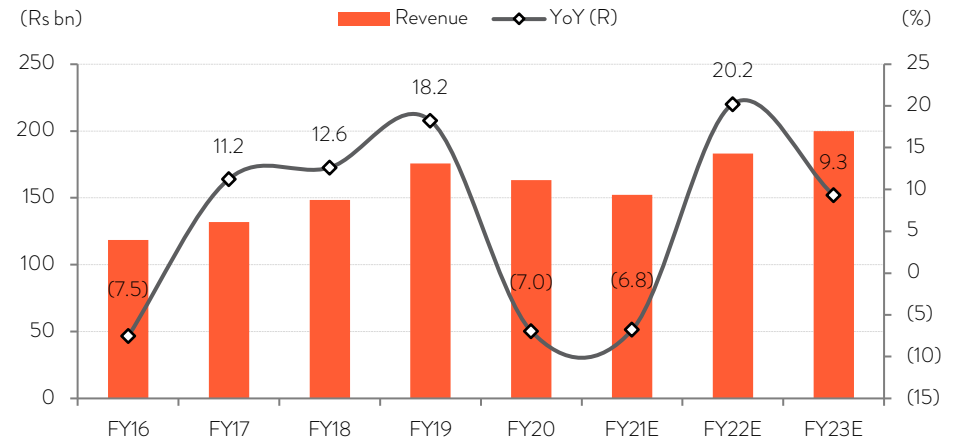
Financial review

Expect a 9% volume CAGR for MHCV & LCV segments (53% of domestic revenue)

PV tyres (39% of domestic revenue) forecast to grow 9%

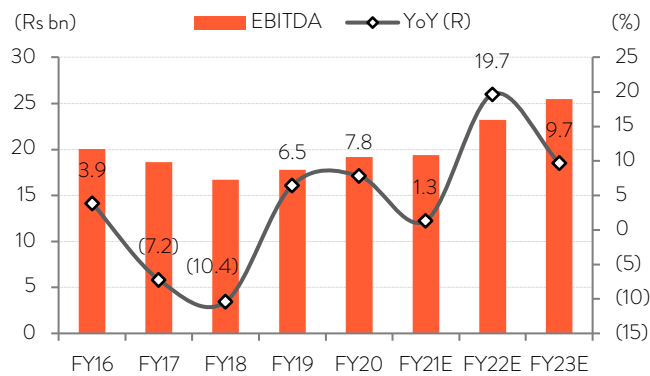
We expect a 2% revenue CAGR from European subsidiaries

FIG 7 – APTY'S CONSOLIDATED REVENUE TO LOG 7% CAGR OVER FY20-FY23E



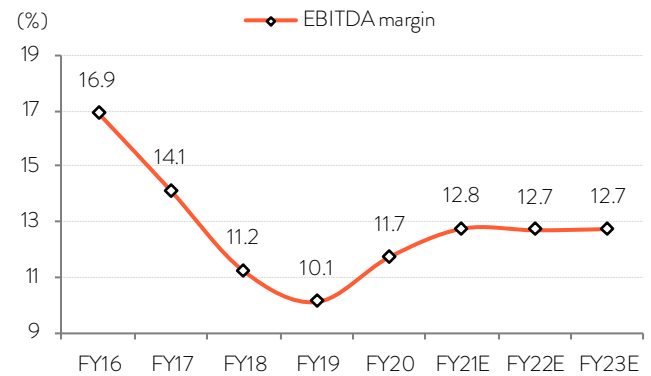
Source: Company, BOBCAPS Research

FIG 8 – EBITDA TO LOG 10% CAGR OVER FY20-FY23E...



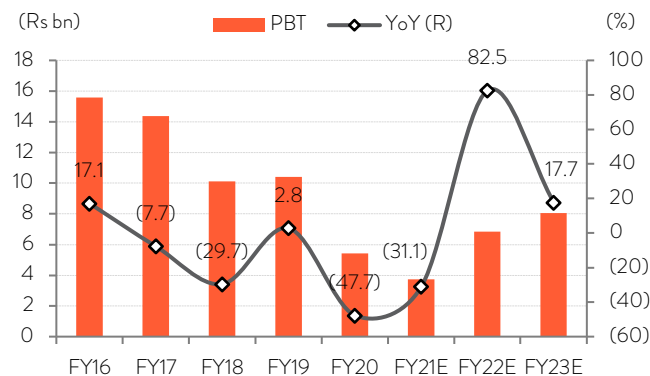
Source: Company, BOBCAPS Research

FIG 9 – ...WITH MARGINS HOLDING AT ~13% BACKED BY LOWER RM PRICES AND BETTER SALES MIX



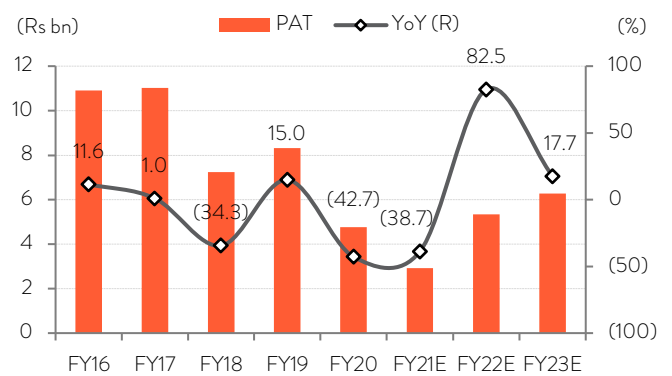
Source: Company, BOBCAPS Research

FIG 10 – EXPECT 14% CAGR IN PBT



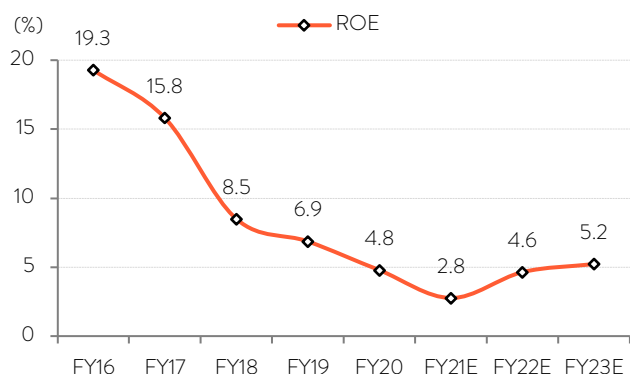
Source: Company, BOBCAPS Research

FIG 11 – EXPECT 15% CAGR IN PAT (POST ADJUSTING DEFERRED TAX ADJUSTMENT OF FY20)



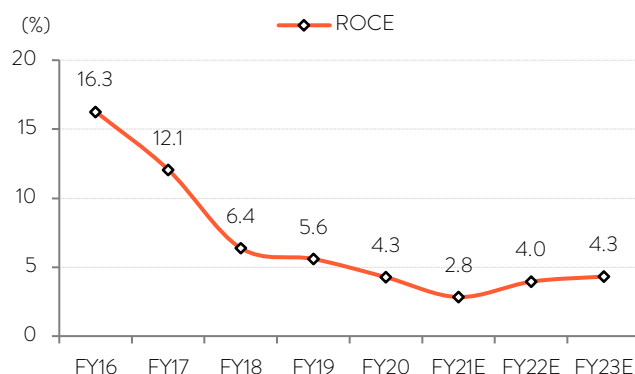
Source: Company, BOBCAPS Research

FIG 12 – ROE EXPECTED TO REVERSE TREND FROM FY22 ONWARDS



Source: Company, BOBCAPS Research

FIG 13 – ROCE ALSO EXPECTED TO IMPROVE FROM FY22 ONWARDS



Source: Company, BOBCAPS Research

FIG 14 – QUARTERLY PERFORMANCE: STEADY MARGIN PERFORMANCE DESPITE DECLINED REVENUES

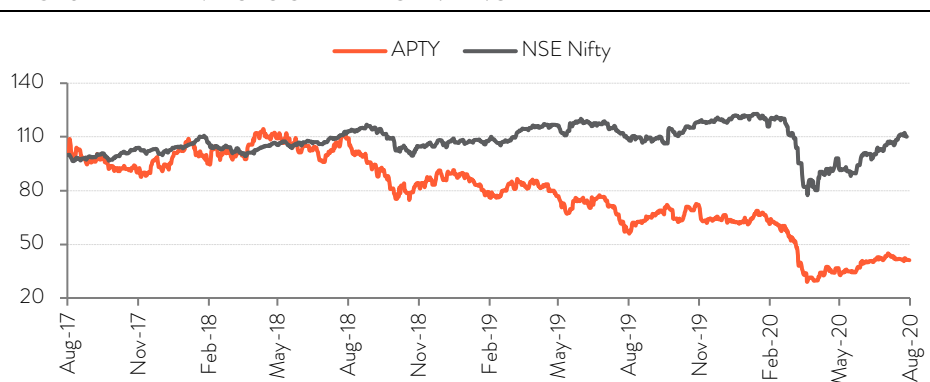
(Rs mn)	Q1FY19	Q2FY19	Q3FY19	Q4FY19	Q1FY20	Q2FY20	Q3FY20	Q4FY20
Net Sales/Income from operations	30,598	31,091	31,232	30,615	31,037	27,747	27,536	24,300
YoY (%)	32.5	25.3	17.0	7.7	1.4	(10.8)	(11.8)	(20.6)
QoQ (%)	7.7	1.6	0.5	(2.0)	1.4	(10.6)	(0.8)	(11.8)
(Inc) / Dec in stock and WIP	(1,238)	(2,073)	(1,204)	1,901	(652)	611	690	480
Raw materials	20,603	22,137	22,164	18,290	20,282	16,854	16,090	14,021
% of sales	63.3	64.5	67.1	66.0	63.2	62.9	60.9	59.7
YoY (%)	24.4	25.6	27.4	15.6	1.4	(13.0)	(19.9)	(28.2)
QoQ (%)	10.8	3.6	4.5	(3.7)	(2.8)	(11.0)	(3.9)	(13.6)
Staff Cost	1,860	1,899	1,801	1,812	2,198	2,004	2,160	1,899
% of sales	6.1	6.1	5.8	5.9	7.1	7.2	7.8	7.8
Other expenditure	5,240	5,405	5,048	5,102	5,602	5,027	5,025	4,401
% of sales	17.1	17.4	16.2	16.7	18.0	18.1	18.2	18.1
Total Expenditure	26,464	27,368	27,809	27,106	27,429	24,496	23,965	20,802
Operating Profit	4,134	3,724	3,423	3,509	3,608	3,252	3,571	3,498
YoY (%)	114.6	30.7	(6.7)	(12.9)	(12.7)	(12.7)	4.3	(0.3)
QoQ (%)	2.6	(9.9)	(8.1)	2.5	2.8	(9.9)	9.8	(2.1)
OPM (%)	13.5	12.0	11.0	11.5	11.6	11.7	13.0	14.4
Other Income	285	106	269	457	215	15	86	33
Interest	370	334	372	302	454	513	549	741
Depreciation	1,012	1,070	1,068	1,314	1,454	1,486	1,528	1,739
Profit before exceptnl itms and tax	3,037	2,426	2,251	2,350	1,915	1,267	1,580	1,052
Exceptional Items	-	400.0	600.0	1,000.0	-	-	-	-
Profit Before Tax	3,037	2,026	1,651	1,350	1,915	1,267	1,580	1,052
Less: Provision for Taxation	868	558	421	296	416	270	273	(232)
Profit After Tax	2,169	1,468	1,230	1,054	1,499	998	1,307	1,283
EPS	3.8	2.6	2.2	1.8	2.6	1.7	2.3	2.2

Source: Company, BOBCAPS Research

Valuation methodology

We expect APTY’s India revenue to register a 10% CAGR over FY20-FY23 and its European subsidiary to grow at 2%. Overall, we project a revenue/EBITDA/PAT CAGR of 7%/10%/15% for the company over FY20-FY23, with operating margins sustaining at ~13% levels. Valuing the stock at 15x Sep’22 EPS, which is in line with the stock’s five-year average, we initiate coverage with BUY and a target price of Rs 135.

FIG 15 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

- Lower-than-expected volume growth can hamper profitability and squeeze operating performance.
- A meaningful increase in rubber and crude oil prices can dent operating margins and adversely impact profitability.

Annexure A: Company profile

Headquartered in Gurgaon, APTY was founded in 1972 and is engaged in the manufacture and sale of tyres. The company caters to over 100 countries across the globe and markets products under two brands – Apollo and Vredestein – through an extensive network of branded, exclusive and multi-product outlets.

APTY has four manufacturing units in India, one in the Netherlands and one in Hungary. In India, its network is spread across ~5,000 dealerships, of which over 2,500 are exclusive outlets. The company derives 69% of revenues from India, 26% from Europe and 5% from other geographies.

The company entered the two-wheeler tyre segment with contract manufacturing in 2016 and is setting up a Rs 18bn tyre factory in Andhra Pradesh to manufacture tyres for 2Ws and pick-up trucks. The plant will come up over a 200-acre site in Chittoor district and produce passenger car radial (PCR) tyres with an initial capacity of 5.5mn tyres per year, catering to both domestic and export markets.

FIG 1 – A BIRD’S EYE VIEW ON ITS CORPORATE GOVERNANCE

Name	Designation	Total Remuneration (Rs mn)	No. of board meetings attended	Attended last AGM	Committees (Y/N)/ No of meetings attended					
					1- Audit	2- Nomination & remuneration	3- Stakeholders relationship	4- CSR Committee	5- Risk Management	6- Business responsibility
Mr Onkar Kanwar	Promoter- Executive	402.5	6	Yes		Y/5	Y/2	Y/2		Y/1
Mr Neeraj Kanwar	Executive	352.2	6	Yes			Y/1			Y/1
Mr Akshay Chudasama	Non- Executive, I	6.3	6	Yes	Y/4	Y/5	Y/1			Y/1
Ms Anjali Bansal	Non- Executive, I	5.6	6	Yes				Y/2		
Gen Bikram Singh	Non- Executive, I	5.6	6	Yes				Y/2		
Mr Frandcesco Gori	Non executive, NI	5.4	6	No					Y/NA	
Dr M Beena	Non executive, NI	4.9	1	Yes						
Mr Nimesh Kampani	Non- Executive, I	4.8	5	Yes	Y/4	Y/5				
Ms Pallavi Shroff	Non- Executive, I	5.5	6	Yes			Y/0			
Mr Robert Steinmetz	Non executive, NI	5.7	5	Yes	Y/4				Y/NA	
Mr Sunam Sarkar	Non executive, NI	5.8	6	Yes			Y/2	Y/2	Y/NA	Y/1
Dr S Narayan	Non- Executive, I	6.1	6	Yes	Y/3	Y/5	Y/0			
Mr Vikram Mehta	Non- Executive, I	5.4	5	Yes						
Mr Vinod Rai	Non- Executive, I	5.4	5	Yes						
Mr Satish Sharma	Executive	0	0	N/A					Y/NA	

Source: Company, BOBCAPS Research | Note: I= Independent, NI= Non-independent

FIG 2 – AUDITORS, BANKERS, CREDIT RATING AND CSR DETAILS

Auditors	M/s Walker Chandio & Co LLP, Chartered Accountants			
Cost Auditors	M/s N.P. Gopalakrishnan & Co, Cost Accountants			
Bankers	Axis Bank	Mizuho Bank	Citibank N.A.	The Bank of Nova Scotia
	Bank of India	Standard Chartered Bank	Federal Bank	MUFG Bank
	BNP Paribas	State Bank of India	ICICI Bank	The Hongkong and Shanghai Banking Corporation Limited
	Canara Bank	Sumitomo Mitsui Banking Corporation	IDBI Bank	Union Bank of India
	Kotak Mahindra Bank Ltd.	RBL Bank		
Credit rating				
Detail of debt	Rating	Rated by		
Long term rating	AA+/Stable	CRISIL		
Short term rating	A1+	CRISIL		
Commercial paper	IND A1+	India Rating & Research		
NCD	IND AA+	India Rating & Research		
CSR				
Prescribed amt (Rs mn)	213.8			
Expensed amt (Rs mn)	213.8			

Source: Company, BOBCAPS Research

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue	175,488	163,270	152,170	182,924	199,971
EBITDA	17,762	19,155	19,407	23,225	25,476
Depreciation	8,127	11,381	13,062	14,206	15,350
EBIT	10,867	8,243	6,745	9,718	10,976
Net interest income/(expenses)	(1,986)	(2,808)	(2,999)	(2,881)	(2,928)
Other income/(expenses)	1,232	469	400	700	850
Exceptional items	1,519	0	0	0	0
EBT	10,400	5,434	3,746	6,837	8,048
Income taxes	2,083	670	824	1,504	1,771
Extraordinary items	0	0	0	0	0
Min. int./Inc. from associates	0	0	0	0	0
Reported net profit	8,317	4,764	2,922	5,333	6,277
Adjustments	(1,519)	0	0	0	0
Adjusted net profit	6,798	4,764	2,922	5,333	6,277

Balance Sheet

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Accounts payables	22,102	23,090	21,365	28,170	26,396
Other current liabilities	8,960	16,980	13,154	19,739	17,228
Provisions	3,466	4,421	2,415	3,103	3,292
Debt funds	49,304	65,799	61,799	60,799	63,799
Other liabilities	7,975	15,433	15,433	15,433	15,433
Equity capital	572	572	572	635	635
Reserves & surplus	99,826	98,728	112,275	116,851	122,312
Shareholders' fund	100,398	99,300	112,847	117,486	122,948
Total liabilities and equities	192,205	225,023	227,012	244,731	249,095
Cash and cash eq.	5,627	7,496	5,061	4,906	4,165
Accounts receivables	11,547	9,399	11,413	12,805	12,998
Inventories	34,841	32,069	30,434	36,585	37,995
Other current assets	5,275	8,282	7,608	9,146	8,999
Investments	60	194	194	194	194
Net fixed assets	117,540	154,685	161,622	171,416	176,066
CWIP	15,393	16,219	14,000	13,000	12,000
Intangible assets	0	0	0	0	0
Deferred tax assets, net	(7,707)	(7,032)	(7,032)	(7,032)	(7,032)
Other assets	9,630	3,711	3,711	3,711	3,711
Total assets	192,205	225,023	227,012	244,731	249,095

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Net income + Depreciation	16,444	16,145	15,984	19,539	21,628
Interest expenses	1,986	2,808	2,999	2,881	(2,928)
Non-cash adjustments	(1,232)	(469)	(400)	(700)	(850)
Changes in working capital	(13,466)	25,253	(7,263)	4,999	(5,552)
Other operating cash flows	(1,447)	(286)	0	0	0
Cash flow from operations	2,284	43,452	11,320	26,719	12,297
Capital expenditures	(13,988)	(49,352)	(17,781)	(23,000)	(19,000)
Change in investments	13,365	(134)	0	0	0
Other investing cash flows	1,232	469	400	700	850
Cash flow from investing	609	(49,017)	(17,381)	(22,300)	(18,150)
Equities issued/Others	0	0	10,800	0	0
Debt raised/repaid	2,693	16,494	(4,000)	(1,000)	3,000
Interest expenses	(1,986)	(2,808)	(2,999)	(2,881)	(2,928)
Dividends paid	(2,069)	(1,716)	(175)	(693)	(816)
Other financing cash flows	(1,896)	(4,535)	0	0	0
Cash flow from financing	(3,258)	7,435	3,626	(4,574)	(744)
Changes in cash and cash eq.	(365)	1,869	(2,435)	(155)	(6,597)
Closing cash and cash eq.	5,627	7,496	5,061	4,906	4,165

Per Share

Y/E 31 Mar (Rs)	FY19A	FY20A	FY21E	FY22E	FY23E
Reported EPS	14.5	8.3	5.1	8.4	9.9
Adjusted EPS	14.5	8.3	5.1	8.4	9.9
Dividend per share	3.0	3.0	0.3	1.1	1.3
Book value per share	175.5	173.6	197.3	185.0	193.6

Valuations Ratios

Y/E 31 Mar (x)	FY19A	FY20A	FY21E	FY22E	FY23E
EV/Sales	0.6	0.6	0.7	0.7	0.6
EV/EBITDA	5.5	5.4	5.8	5.1	4.6
Adjusted P/E	7.4	13.0	21.2	12.9	10.9
P/BV	0.6	0.6	0.5	0.6	0.6

DuPont Analysis

Y/E 31 Mar (%)	FY19A	FY20A	FY21E	FY22E	FY23E
Tax burden (Net profit/PBT)	80.0	87.7	78.0	78.0	78.0
Interest burden (PBT/EBIT)	95.7	65.9	55.5	70.4	73.3
EBIT margin (EBIT/Revenue)	6.2	5.0	4.4	5.3	5.5
Asset turnover (Revenue/Avg TA)	112.9	96.5	82.1	95.3	101.0
Leverage (Avg TA/Avg Equity)	1.6	1.7	1.7	1.7	1.6
Adjusted ROAE	8.4	4.8	2.8	4.6	5.2

Source: Company, BOBCAPS Research | Note: TA = Total Assets

Ratio Analysis

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
YoY growth (%)					
Revenue	18.2	(7.0)	(6.8)	20.2	9.3
EBITDA	6.5	7.8	1.3	19.7	9.7
Adjusted EPS	(6.1)	(29.9)	(38.7)	64.4	17.7
Profitability & Return ratios (%)					
EBITDA margin	10.1	11.7	12.8	12.7	12.7
EBIT margin	6.2	5.0	4.4	5.3	5.5
Adjusted profit margin	3.9	2.9	1.9	2.9	3.1
Adjusted ROAE	6.8	4.8	2.6	4.5	5.1
ROCE	5.6	4.3	2.8	4.0	4.3
Working capital days (days)					
Receivables	27	23	25	24	24
Inventory	67	75	75	67	68
Payables	85	91	99	90	91
Ratios (x)					
Gross asset turnover	1.1	1.5	1.7	1.6	1.5
Current ratio	1.7	1.3	1.5	1.2	1.4
Net interest coverage ratio	5.5	2.9	2.2	3.4	3.7
Adjusted debt/equity	0.5	0.7	0.5	0.5	0.5

Source: Company, BOBCAPS Research

REDUCE

TP: Rs 1,300 | ▼ 1%

**BALKRISHNA
INDUSTRIES**

| Auto Components

| 05 August 2020

Robust business model; initiate with REDUCE

Balkrishna Industries (BIL) is a leading off-highway tyre exporter. The company has a robust business model of making in India and servicing global markets, deriving ~80% of revenue from exports. Despite its products being priced 20-25% lower than those of international peers, we expect EBITDA margins to hold at a robust ~27%. We model for a revenue/EBITDA/PAT CAGR of 11%/12%/11% over FY20-FY23 and value the stock at 23x Sep'22 EPS. Upsides, however, look limited at current valuations – initiate with REDUCE, TP Rs 1,300.

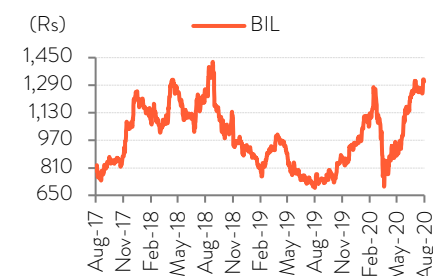
Mayur Milak | Nishant Chowhan, CFA
 research@bobcaps.in

Robust business model: BIL mainly caters to the higher-margin segments (off-road vehicle and agricultural tyres) and benefits from a range of SKUs, its export focus, price advantage over rivals and better margins than domestic peers. A bulk of revenue (~80%) arises from exports, largely to replacement markets in Europe and the US. BIL leverages cost benefits from its India manufacturing base to price products ~25% cheaper than other leading brands while retaining ~27% EBITDA margins. We expect margins to sustain at this level and bake in an 8% volume CAGR through FY23.

Ticker/Price	BIL IN/Rs 1,310
Market cap	US\$ 3.4bn
Shares o/s	193mn
3M ADV	US\$ 12.5mn
52wk high/low	Rs 1,346/Rs 679
Promoter/FPI/DII	58%/12%/18%

Source: NSE

Capacity expansion, new markets to fuel growth: BIL's phase-II expansion at its carbon plant will take capacity from 80,000mtpa to 140,000mtpa in FY21, giving it better control over input costs. The company will also incur capex towards replacement of its older Waluj facilities, besides venturing into radial off-the-road (OTR) tyres at its Bhuj plant. In a bid to tap newer markets, operations are being expanded to high-growth countries such as Africa and Russia.

STOCK PERFORMANCE

Source: NSE

Initiate with REDUCE: We model for ROCE and ROE of 16% each in FY23. Valuing the stock at 23x Sep'22 EPS, we have a TP of Rs 1,300. BIL is currently trading at 24x/23x FY22/23E EPS, which leaves little upside potential – initiate with REDUCE.

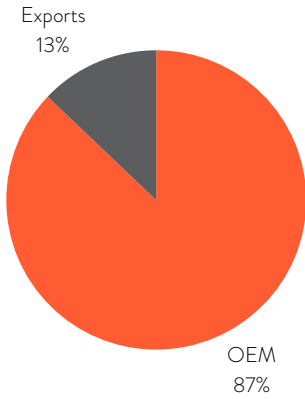
KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue (Rs mn)	52,445	47,825	49,269	58,360	64,604
EBITDA (Rs mn)	13,124	12,494	13,290	15,895	17,650
Adj. net profit (Rs mn)	7,820	9,450	8,242	10,467	11,344
Adj. EPS (Rs)	40.5	48.9	42.6	54.2	58.7
Adj. EPS growth (%)	5.8	20.8	(12.8)	27.0	8.4
Adj. ROAE (%)	16.7	18.8	14.3	15.8	15.1
Adj. P/E (x)	32.4	26.8	30.7	24.2	22.3
EV/EBITDA (x)	20.1	20.9	19.7	16.3	14.5

Source: Company, BOBCAPS Research

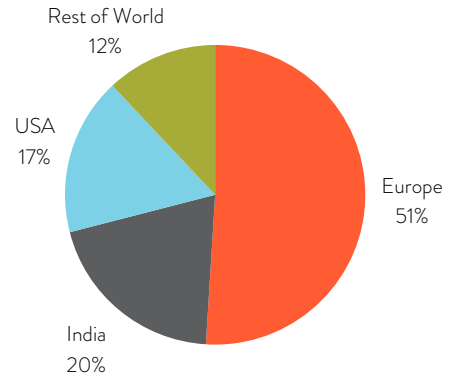
Investment summary

FIG 1 – REVENUE MIX: BIL MAINLY CATERS TO HIGHER-MARGIN OFF-ROAD VEHICLES AND AGRICULTURAL TYRES



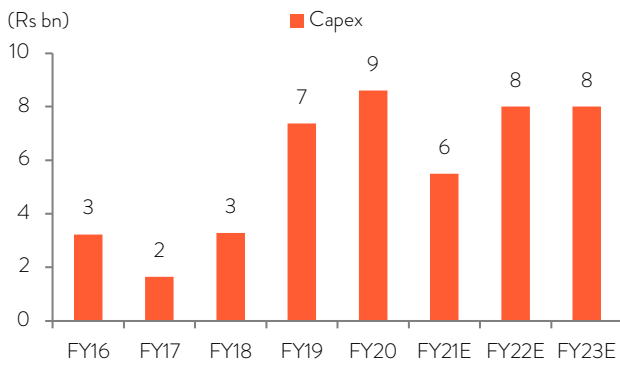
Source: Company, BOBCAPS Research

FIG 2 – REGIONWISE REVENUES: EUROPE AND US ARE PRIME OVERSEAS MARKETS FOR BIL FORMING 68% OF VOLUME SALES



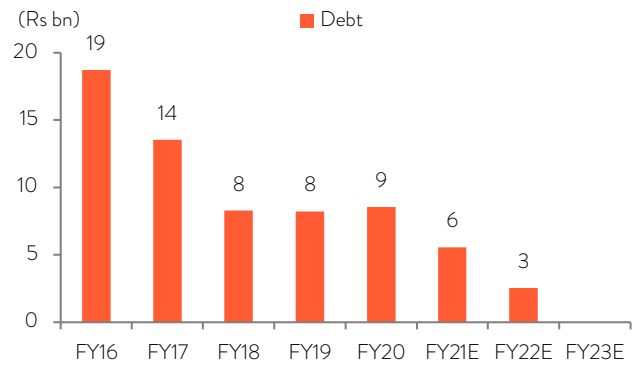
Source: Company, BOBCAPS Research

FIG 3 – TIMELY AND STEADY CAPEX...



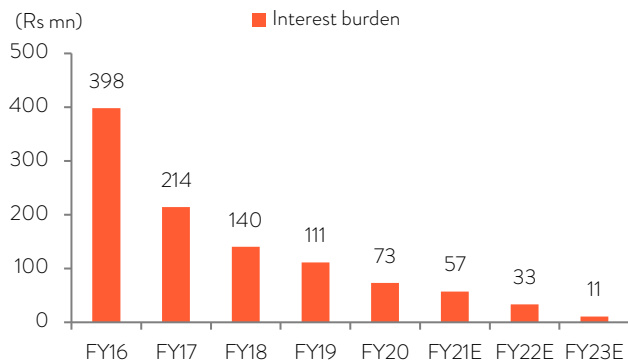
Source: Company, BOBCAPS Research

FIG 4 – ...HAS KEPT GROSS DEBT UNDER CONTROL



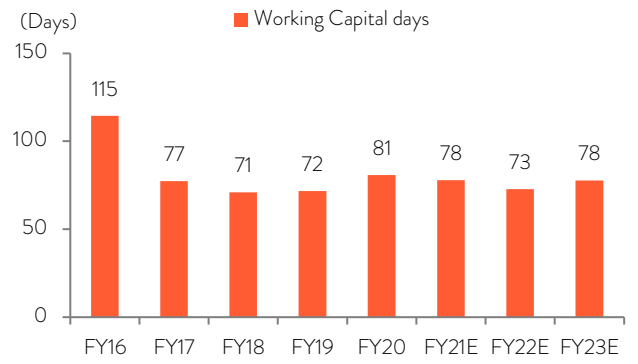
Source: Company, BOBCAPS Research

FIG 5 – DEBT REPAYMENT HAS LOWERED INTEREST BURDEN



Source: Company, BOBCAPS Research

FIG 6 – HIGHER EXPORTS RESULT IN LONGER WORKING CAPITAL CYCLE



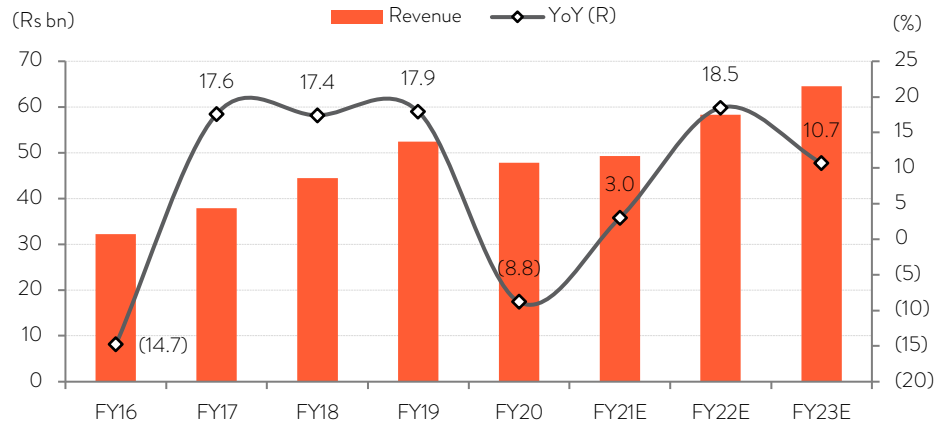
Source: Company, BOBCAPS Research

Financial review

We expect a 11% revenue CAGR, similar to the growth rate over FY16-FY20

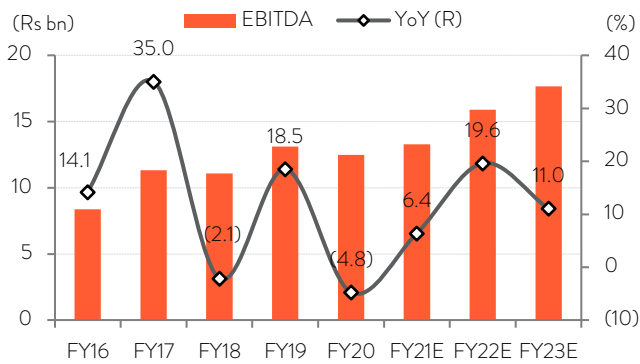
Growth is based on its future roadmap of raising exposure to OEs and focusing on newer territories

FIG 7 – BIL'S REVENUE TO LOG 11% CAGR OVER FY20-FY23E



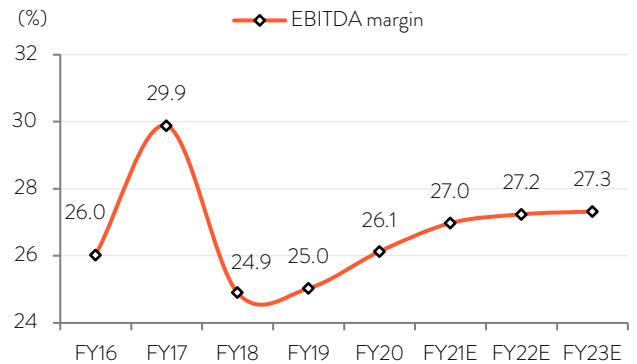
Source: Company, BOBCAPS Research

FIG 8 – EXPECT 12% EBITDA CAGR OVER FY20-FY23E...



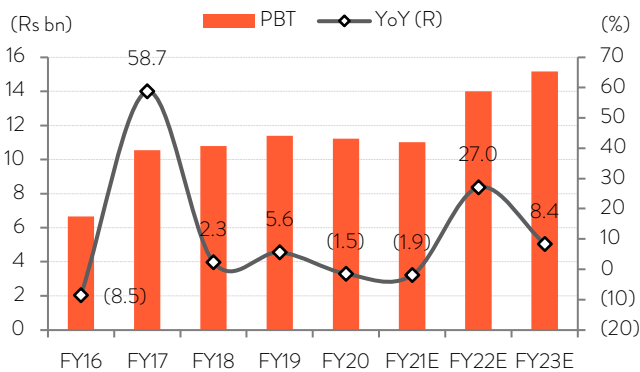
Source: Company, BOBCAPS Research

FIG 9 – ...WITH MARGINS STEADY AT ~27%



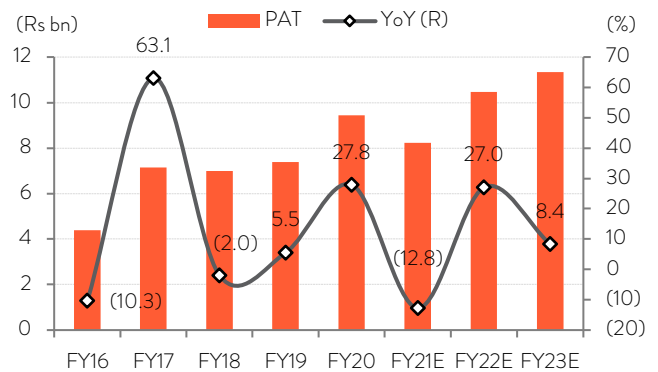
Source: Company, BOBCAPS Research

FIG 10 – EXPECT 11% CAGR IN PBT...



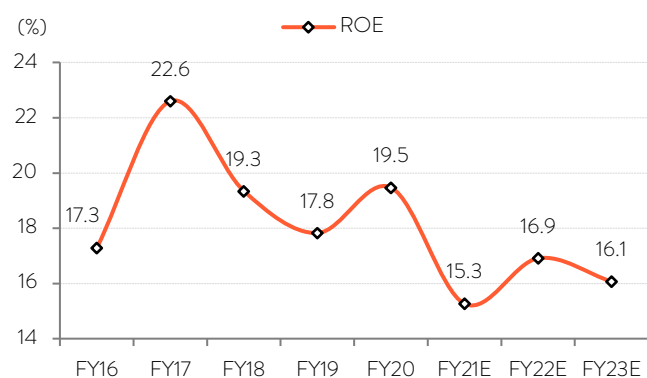
Source: Company, BOBCAPS Research

FIG 11 – ...WHILE PAT GROWS AT 11% CAGR (ADJUSTING FOR DEFERRED TAX ADJ IN FY20)



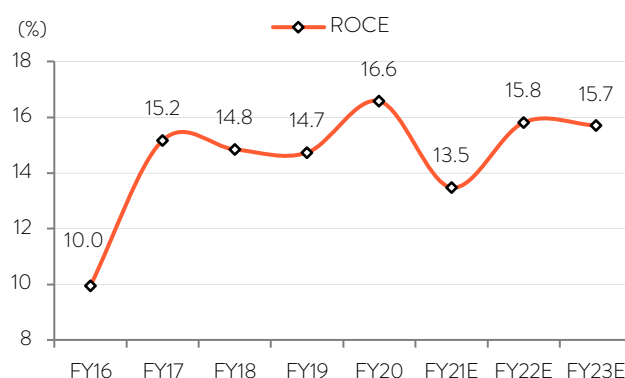
Source: Company, BOBCAPS Research

FIG 12 – ROE PROJECTED TO CLOCK AT 16% IN FY23...



Source: Company, BOBCAPS Research

FIG 13 – ...AND ROCE TO IMPROVE FROM FY21 LEVELS



Source: Company, BOBCAPS Research

FIG 14 – QUARTERLY PERFORMANCE:

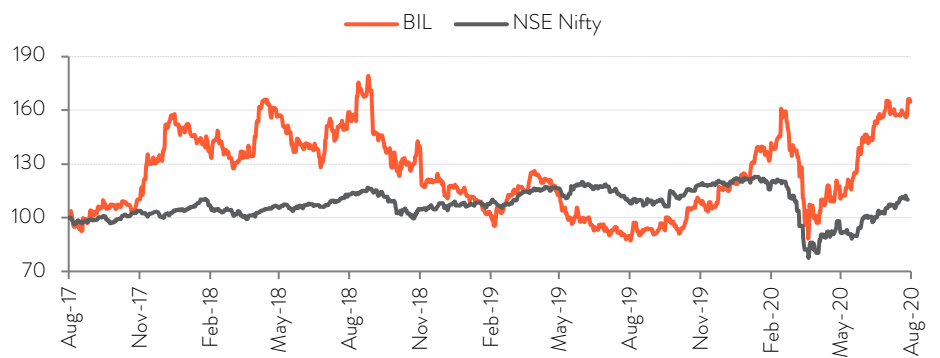
(Rs mn)	Q1FY19	Q2FY19	Q3FY19	Q4FY19	Q1FY20	Q2FY20	Q3FY20	Q4FY20
Volume (MT)	56,754	52,339	46,780	55,388	51,304	45,169	47,321	57,966
YoY (%)	22.5	6.1	(5.6)	2.6	(9.6)	(13.7)	1.2	4.7
Average Realization (Rs/t)	240,036	253,249	257,715	243,923	232,629	237,152	245,240	234,155
YoY (%)	9.8	12.1	15.4	6.9	(3.1)	(6.4)	(4.8)	(4.0)
Net sales	13,623	13,255	12,056	13,510	11,935	10,712	11,605	13,573
YoY (%)	34.5	18.9	9.0	9.7	(12.4)	(19.2)	(3.7)	0.5
QoQ (%)	10.6	(2.7)	(9.0)	12.1	(11.7)	(10.2)	8.3	17.0
(Inc)/dec in stock-in-trade	(106)	(347)	(180)	248	234	(392)	(218)	864
Materials	6,487	6,468	5,709	6,347	5,516	5,070	5,008	5,186
% of sales	46.8	46.2	45.9	48.8	48.2	43.7	41.3	44.6
YoY (%)	22.0	11.7	9.5	15.0	(9.9)	(23.6)	(13.4)	(8.3)
QoQ (%)	11.2	(4.1)	(9.7)	19.3	(12.8)	(18.6)	2.4	26.3
Staff cost	680	681	680	594	696	701	708	754
% of sales	5.0	5.1	5.6	4.4	5.8	6.5	6.1	5.6
YoY (%)	15.8	14.3	10.6	(13.8)	2.3	2.8	4.1	27.0
QoQ (%)	(1.3)	0.2	(0.2)	(12.6)	17.0	0.7	1.0	6.6
Other expenditure	2,985	3,126	2,838	3,121	2,811	2,658	2,692	3,044
% of sales	21.9	23.6	23.5	23.1	23.6	24.8	23.2	22.4
YoY (%)	39.1	54.9	13.5	6.3	(5.8)	(14.9)	(5.2)	(2.5)
QoQ (%)	1.7	4.7	(9.2)	10.0	(9.9)	(5.4)	1.3	13.1
Total expenses	10,046	9,929	9,047	10,310	9,256	8,037	8,190	9,848
EBITDA	3,577	3,326	3,009	3,200	2,678	2,675	3,415	3,725
YoY (%)	65.4	9.1	3.8	8.3	(25.1)	(19.6)	13.5	16.4
QoQ (%)	21.0	(7.0)	(9.5)	6.4	(16.3)	(0.1)	27.7	9.1
OPM (%)	26.3	25.1	25.0	23.7	22.4	25.0	29.4	27.4
Other income	822	909	10	402	716	807	301	664
Interest	33	25	20	20	18	17	19	19
Depreciation	841	828	834	823	841	908	949	983
Profit before tax	3,525	3,382	2,165	2,759	2,536	2,557	2,748	3,388
Provision for taxation	1,221	1,159	718	911	776	(353)	542	815
Tax Rate (%)	34.6	34.3	33.2	33.0	30.6	(13.8)	19.7	24.1
Profit after tax	2,304	2,223	1,447	1,847	1,760	2,910	2,207	2,573

Source: Company, BOBCAPS Research

Valuation methodology

We model for a revenue/EBITDA/PAT CAGR of 11%/12%/11% for BIL over FY20-FY23. ROCE and ROE are forecast at 16% each for FY23. Valuing the stock at 23x Sep'22 EPS, we have a target price of Rs 1,300. The stock is trading at 24x/23x FY22/23E EPS, which leaves little upside potential – initiate with REDUCE.

FIG 15 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

- Above-expected volume growth
- Fall in natural rubber and crude derivative prices could aid better than expected margins

Annexure A: Company profile

Mumbai-based BIL manufactures off-highway tyres used in specialist segments such as mining, earthmoving, agriculture and gardening. The company has five factories located in Aurangabad (Maharashtra), Bhiwadi (Rajasthan), Chopanki (Rajasthan), Dombivali (Maharashtra) and Bhuj (Gujarat).

BIL is currently an OEM vendor for heavy equipment manufacturers including JCB, John Deere and CNH Industrial. The company enjoys ~5% market share in the global off-the-road (OTR) tyre segment and predominantly caters to the replacement market in North America and Europe. About 80% of its business comes from exports to other countries.

FIG 1 – A BIRD’S EYE VIEW ON CORPORATE GOVERNANCE

Name	Designation	Total Remuneration (Rs mn)	No. of board meetings attended	Attended last AGM	Committees (Y/N)/ No of meetings attended						
					1- Audit	2- Nomination & remuneration	3- Stakeholders relationship	4- Risk Management	5- CSR	6 Business responsibility	6- Finance
Mr Arvind Poddar	Chairman & MD	294.6	6	Y				Y/NA		Y/1	Y/6
Mr Rajiv Poddar	Joint MD	294.2	6	Y				Y/NA	Y/4	Y/1	Y/5
Mrs Vijaylaxmi Poddar	Non-executive, Non-independent	0.17	5	N					Y/4		
Mr Vipul Shah	Director & CS	6.10	6	Y			Y/4	Y/NA	Y/4		Y/6
Mr Sanjay Asher	Non-executive, Independent	0.10	3	N		Y/2			Y/2	Y/0	
Mr Ashok Saraf	Non-executive, Independent	0.50	5	Y	Y/4	Y/4	Y/4				
Mr Laxmidas Merchant	Non-executive, Independent	0.20	5	N	Y/3					Y/1	
Mr Pannkaj Ghadiali	Non-executive, Independent	0.30	6	Y	Y/4	Y/5	Y/4	Y/NA		Y/NA	
Mr Khurshed Doongaji	Non-executive, Independent	0.30	5	N	Y/4	Y/4	Y/4			Y/1	
Mrs Shruti Shah	Non-executive, Independent	0.10	2	NA	Y/NA	Y/1	Y/NA				
Mr Rajendra Hingwala	Non-executive, Independent	0.25	1	NA							
Mr Sandeep Junnarkar	Non-executive, Independent	0.25	1	NA							

Source: Company, BOBCAPS Research

FIG 2 – AUDITORS, BANKERS, CREDIT RATING AND CSR DETAILS

Auditors	M/s N G Thakrar & Co	
Cost Auditors	NA	
Bankers	Corporation Bank	IndusInd Bank
	Standard Chartered Bank	Citibank
	State Bank of India	HSBC
	Kotak Mahindra Bank	Barclays Bank
CSR (in FY19)		
Prescribed CSR (Rs mn)	189.3	
CSR expensed (Rs mn)	169.7	

Source: Company, BOBCAPS Research

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue	52,445	47,825	49,269	58,360	64,604
EBITDA	13,124	12,494	13,290	15,895	17,650
Depreciation	3,326	3,680	4,276	4,836	5,500
EBIT	11,941	11,302	11,076	14,027	15,176
Net interest income/(expenses)	(111)	(73)	(57)	(33)	(11)
Other income/(expenses)	2,142	2,488	2,062	2,967	3,026
Exceptional items	(428)	0	0	0	0
EBT	11,402	11,229	11,019	13,994	15,166
Income taxes	4,010	1,779	2,777	3,526	3,822
Extraordinary items	0	0	0	0	0
Min. int./Inc. from associates	4	5	6	7	8
Reported net profit	7,392	9,450	8,242	10,467	11,344
Adjustments	428	0	0	0	0
Adjusted net profit	7,820	9,450	8,242	10,467	11,344

Balance Sheet

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Accounts payables	4,094	3,610	4,110	4,502	4,984
Other current liabilities	1,377	2,605	2,713	2,866	3,171
Provisions	77	77	77	77	77
Debt funds	8,296	8,625	5,625	2,625	35
Other liabilities	410	342	342	342	342
Equity capital	387	387	387	387	387
Reserves & surplus	46,400	49,894	57,312	65,686	74,761
Shareholders' fund	46,787	50,281	57,699	66,073	75,148
Total liabilities and equities	61,042	65,540	70,566	76,485	83,758
Cash and cash eq.	556	455	803	1,154	2,942
Accounts receivables	5,681	6,492	7,019	7,355	8,142
Inventories	7,130	5,803	6,209	7,035	7,788
Other current assets	3,351	3,538	3,915	4,157	4,602
Investments	10,831	10,631	13,631	14,631	15,631
Net fixed assets	27,861	32,782	34,006	37,170	39,669
CWIP	5,854	5,856	5,000	5,000	5,000
Intangible assets	0	0	0	0	0
Deferred tax assets, net	(3,255)	(1,783)	(1,783)	(1,783)	(1,783)
Other assets	3,033	1,767	1,767	1,767	1,767
Total assets	61,042	65,540	70,566	76,485	83,758

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Net income + Depreciation	10,717	13,130	12,518	15,304	16,844
Interest expenses	111	73	57	33	11
Non-cash adjustments	(2,142)	(2,488)	(2,062)	(2,967)	(3,026)
Changes in working capital	(1,592)	2,271	(702)	(859)	(1,197)
Other operating cash flows	(60)	0	0	0	0
Cash flow from operations	7,034	12,986	9,811	11,510	12,631
Capital expenditures	(7,367)	(8,602)	(4,644)	(8,000)	(8,000)
Change in investments	202	200	(3,000)	(1,000)	(1,000)
Other investing cash flows	2,142	2,488	2,062	2,967	3,026
Cash flow from investing	(5,023)	(5,915)	(5,582)	(6,033)	(5,974)
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	(59)	329	(3,000)	(3,000)	(2,590)
Interest expenses	(111)	(73)	(57)	(33)	(11)
Dividends paid	(1,688)	(4,650)	(824)	(2,093)	(2,269)
Other financing cash flows	(272)	(2,779)	0	0	0
Cash flow from financing	(2,129)	(7,173)	(3,881)	(5,126)	(4,869)
Changes in cash and cash eq.	(118)	(101)	348	351	1,788
Closing cash and cash eq.	556	455	803	1,154	2,942

Per Share

Y/E 31 Mar (Rs)	FY19A	FY20A	FY21E	FY22E	FY23E
Reported EPS	40.5	48.9	42.6	54.2	58.7
Adjusted EPS	40.5	48.9	42.6	54.2	58.7
Dividend per share	7.5	20.0	4.3	10.8	11.7
Book value per share	242.0	260.1	298.5	341.8	388.8

Valuations Ratios

Y/E 31 Mar (x)	FY19A	FY20A	FY21E	FY22E	FY23E
EV/Sales	5.0	5.5	5.3	4.5	4.0
EV/EBITDA	20.1	20.9	19.7	16.3	14.5
Adjusted P/E	32.4	26.8	30.7	24.2	22.3
P/BV	5.4	5.0	4.4	3.8	3.4

DuPont Analysis

Y/E 31 Mar (%)	FY19A	FY20A	FY21E	FY22E	FY23E
Tax burden (Net profit/PBT)	68.6	84.2	74.8	74.8	74.8
Interest burden (PBT/EBIT)	95.5	99.4	99.5	99.8	99.9
EBIT margin (EBIT/Revenue)	22.8	23.6	22.5	24.0	23.5
Asset turnover (Revenue/Avg TA)	99.8	83.4	80.2	88.0	89.4
Leverage (Avg TA/Avg Equity)	1.2	1.2	1.1	1.1	1.0
Adjusted ROAE	17.8	19.5	15.3	16.9	16.1

Source: Company, BOBCAPS Research | Note: TA = Total Assets

Ratio Analysis

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
YoY growth (%)					
Revenue	17.9	(8.8)	3.0	18.5	10.7
EBITDA	18.5	(4.8)	6.4	19.6	11.0
Adjusted EPS	5.8	20.8	(12.8)	27.0	8.4
Profitability & Return ratios (%)					
EBITDA margin	25.0	26.1	27.0	27.2	27.3
EBIT margin	22.8	23.6	22.5	24.0	23.5
Adjusted profit margin	14.9	19.8	16.7	17.9	17.6
Adjusted ROAE	16.7	18.8	14.3	15.8	15.1
ROCE	14.7	16.6	13.5	15.8	15.7
Working capital days (days)					
Receivables	37	46	50	45	44
Inventory	45	49	44	41	42
Payables	63	66	66	61	61
Ratios (x)					
Gross asset turnover	0.8	1.0	1.1	1.1	1.1
Current ratio	3.0	2.6	2.6	2.6	2.9
Net interest coverage ratio	107.6	154.8	194.3	425.1	1,426.4
Adjusted debt/equity	0.2	0.2	0.1	0.0	0.0

Source: Company, BOBCAPS Research

REDUCE

TP: Rs 830 | ▼ 4%

CEAT

Auto Components

05 August 2020

Borrowings to weigh on balance sheet; initiate with REDUCE

CEAT's unfavourable sales mix (2W/3W bias) and high revenue share from OEMs will hinder growth, though benign rubber prices should support 11% operating margins. During FY20-FY23, capex required at Rs 31bn will far exceed estimated operating cash flow of Rs 22bn, necessitating external funding and adding pressure on both balance sheet and earnings. Net D/E is expected at 0.8x by FY23-end from 0.5x currently. We value the stock at 14x Sep'22 EPS for a TP of Rs 830 – initiate with REDUCE.

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 research@bobcaps.in

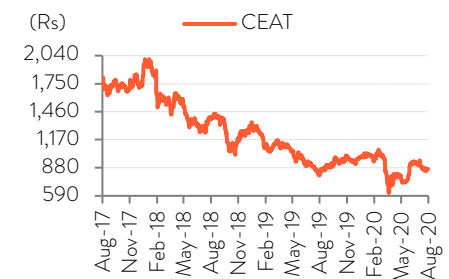
Unfavourable sales mix to hinder growth: About 31% of CEAT's revenues come from the 2W/3W tyre segment where we anticipate the slowest volume growth (~6%) over FY20-FY23. In M&HCV and PV tyres – where we expect steady growth in the replacement market and a strong comeback in OE demand in FY22 – the company has only ~9% market share. Its higher dependence on OEM sales (~50% in 2W and PV segments) also acting as a hindrance in growth.

Ticker/Price	CEAT IN/Rs 868
Market cap	US\$ 467.1mn
Shares o/s	40mn
3M ADV	US\$ 1.9mn
52wk high/low	Rs 1,094/Rs 600
Promoter/FPI/DII	47%/28%/9%

Source: NSE

External borrowings to erode return ratios: We estimate ~Rs 22bn of cumulative operating cash flow from FY21 to FY23. Even the company's reduced capex plan of Rs 31bn for this period clearly warrants external borrowings to the tune of Rs 13bn-14bn. This will shave 260-270bps off ROE and ROCE (to 7% and 6.3% respectively in FY23E), despite assuming significant improvement in working capital cycle. Net D/E of 0.5x is forecast to spike to 0.8x by FY23-end.

STOCK PERFORMANCE



Source: NSE

Initiate with REDUCE: External debt borrowings to fund capex will not only undermine the balance sheet, but also depress profits due to a higher interest burden. We expect CEAT to maintain its EBITDA margin at ~11% and project a revenue/EBITDA/PAT CAGR of +9%/+12%/–4% over FY20-FY23. Valuing the stock at 14x Sep'22 EPS, in line with its peers, we arrive at TP of Rs 830.

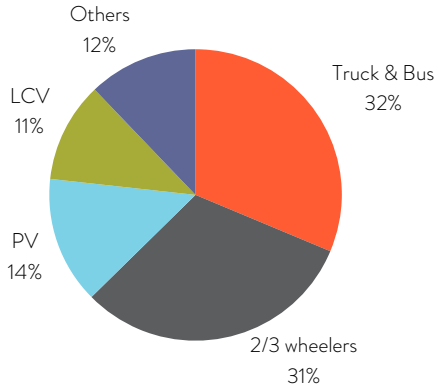
KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue (Rs mn)	68,313	65,811	63,466	76,980	85,085
EBITDA (Rs mn)	5,965	7,053	6,746	8,663	9,841
Adj. net profit (Rs mn)	2,889	3,005	1,755	2,379	2,398
Adj. EPS (Rs)	71.4	74.3	43.4	58.8	59.3
Adj. EPS growth (%)	3.7	4.0	(41.6)	35.6	0.8
Adj. ROAE (%)	10.5	10.3	5.7	7.1	6.7
Adj. P/E (x)	12.2	11.7	20.0	14.8	14.6
EV/EBITDA (x)	7.0	6.2	7.2	6.1	5.9

Source: Company, BOBCAPS Research

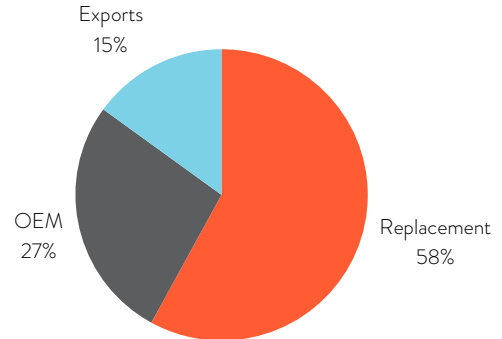
Investment summary

FIG 1 – LOWER EXPOSURE IN T&B AND PV TYRES (~46% OF REVENUES) VS. PEERS TO HAMPER GROWTH (FY20)



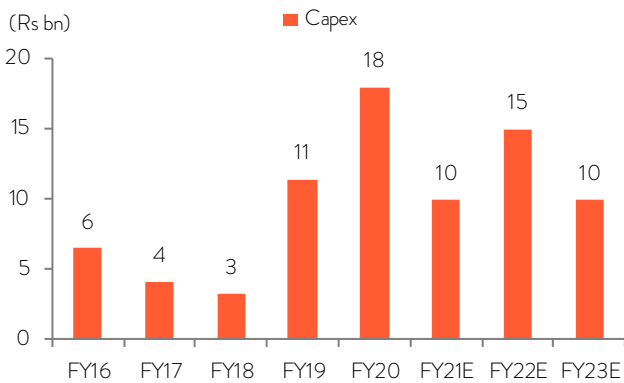
Source: Company, BOBCAPS Research

FIG 2 – LOWER EXPOSURE TO REPLACEMENT MARKET WILL ALSO SLOW GROWTH



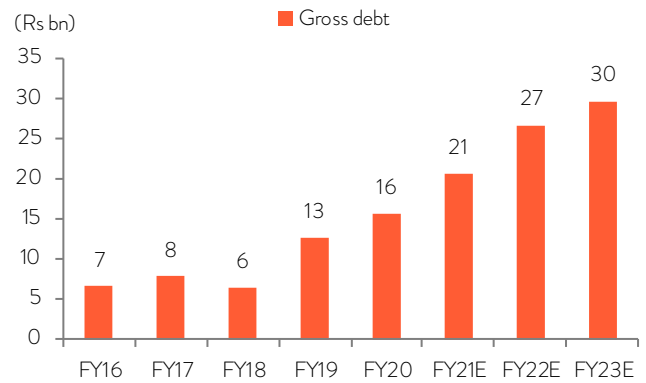
Source: Company, BOBCAPS Research

FIG 3 – FY21 CAPEX SLASHED – IN LINE WITH INDUSTRY DEMAND...



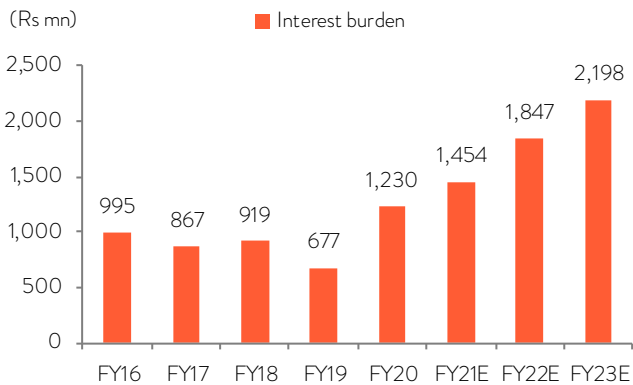
Source: Company, BOBCAPS Research

FIG 4 – ...BUT DEBT STILL ESTIMATED TO DOUBLE OVER FY19-FY23E



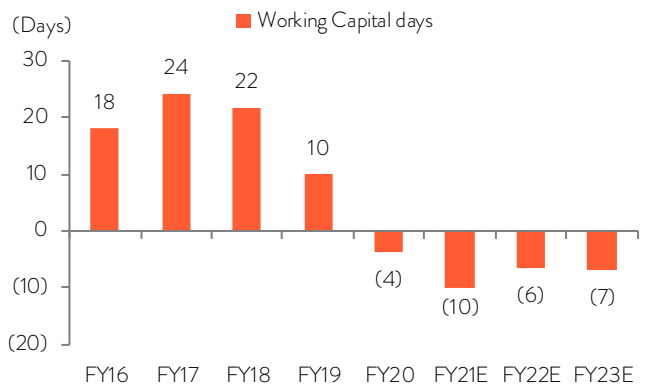
Source: Company, BOBCAPS Research

FIG 5 – SOARING INTEREST BURDEN TO HURT EARNINGS AMID ECONOMIC SLOWDOWN...



Source: Company, BOBCAPS Research

FIG 6 – ...DESPITE EFFICIENT WORKING CAPITAL EXPECTATIONS



Source: Company, BOBCAPS Research

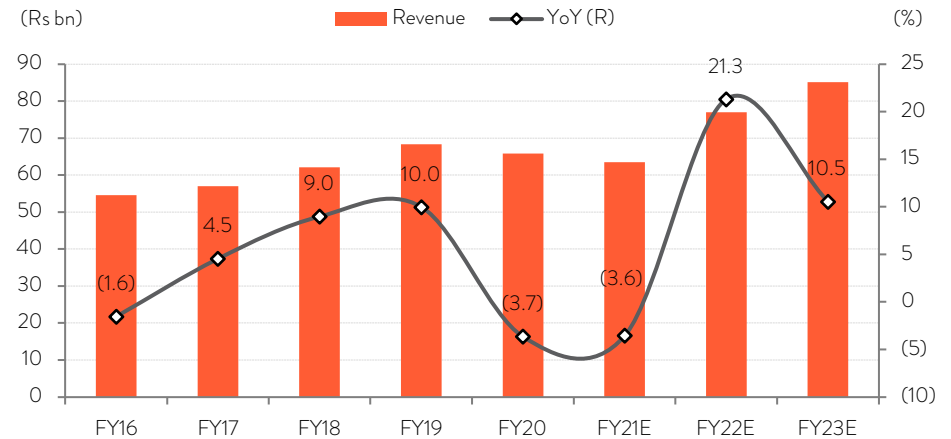
Financial review

M&HCV and LCV segments (44% of domestic revenues) to log 9% volume CAGR

PV tyres (~15% of domestic revenues) to grow at 9%

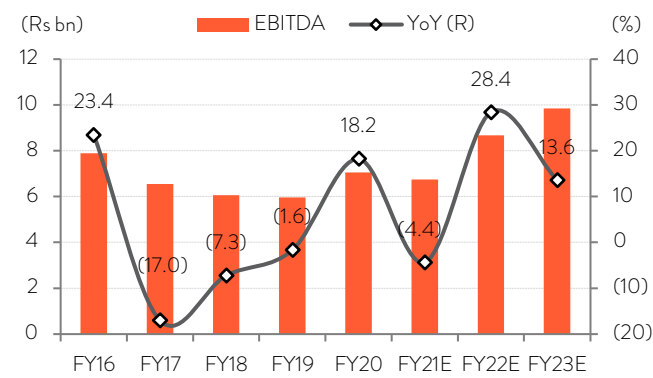
2W/3W tyres (~31% of revenues) to log 6% volume CAGR

FIG 7 – CEAT’S REVENUE TO LOG 9% CAGR OVER FY20-FY23E



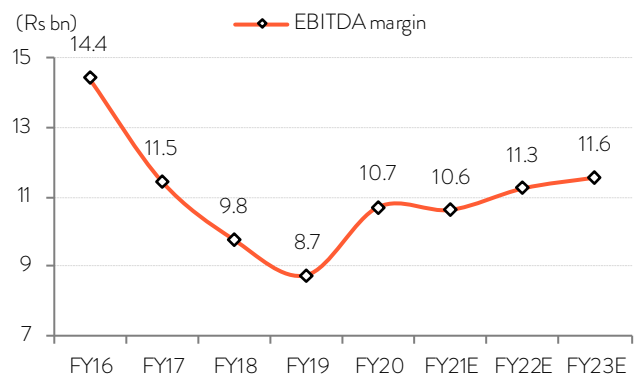
Source: Company, BOBCAPS Research

FIG 1 – EBITDA TO POST 12% CAGR OVER FY20-FY23E...



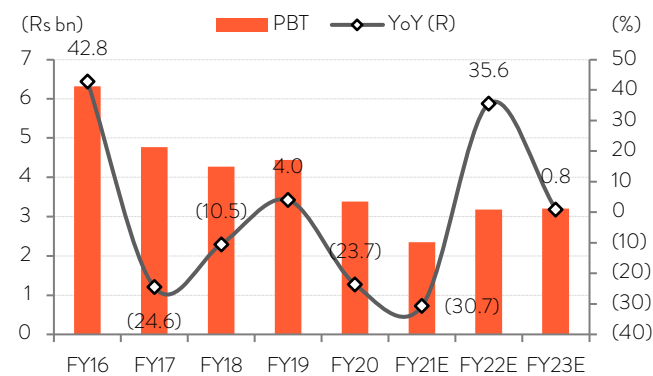
Source: Company, BOBCAPS Research

FIG 2 – ...WITH MARGINS HOLDING AT ~11% BACKED BY LOWER RM PRICES & HIGH-MARGIN 2W/3W TYRES



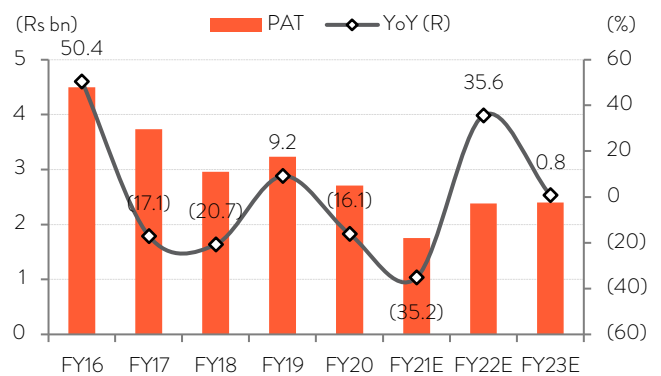
Source: Company, BOBCAPS Research

FIG 3 – EXPECT PBT TO DECLINE AT 2% CAGR

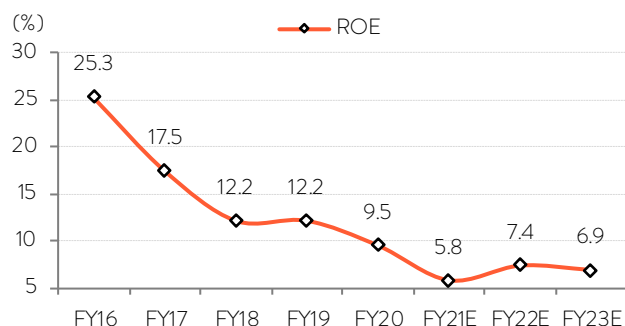


Source: Company, BOBCAPS Research

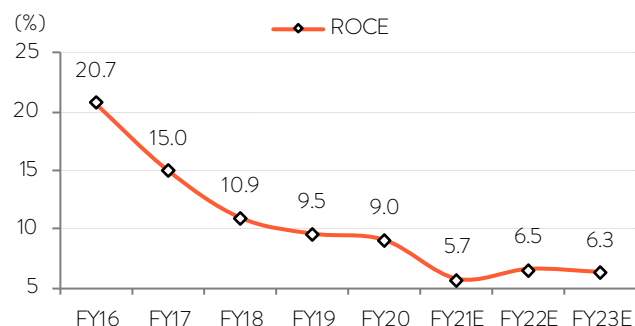
FIG 4 – LOWER OTHER INCOME, HIGHER INTEREST AND DEPRECIATION TO RESULT IN 4% PAT DECLINE



Source: Company, BOBCAPS Research

FIG 5 – LOWER EARNINGS WILL CONTINUE TO EXERT PRESSURE ON ITS ROE DURING FY20-23


Source: Company, BOBCAPS Research

FIG 6 – ...WITH SIMILAR TRENDS FOR ROCE


Source: Company, BOBCAPS Research

FIG 7 – QUARTERLY PERFORMANCE

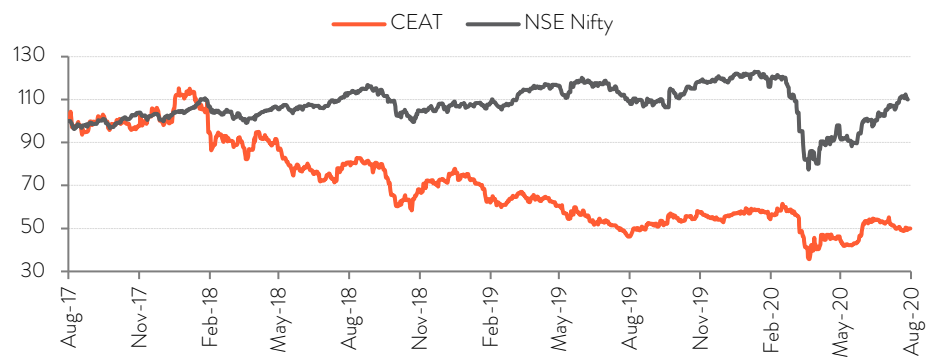
(Rs mn)	Q1FY19	Q2FY19	Q3FY19	Q4FY19	Q1FY20	Q2FY20	Q3FY20	Q4FY20
Net sales	16,742	17,182	16,734	17,175	17,036	16,453	17,086	15,236
YoY (%)	15.4	13.6	8.0	4.2	1.8	(4.2)	2.1	(11.3)
QoQ (%)	1.6	2.6	(2.6)	2.6	(0.8)	(3.4)	3.8	(10.8)
Other income	56	122	64	324	148	171	57	65
Total Income	16,798	17,304	16,798	17,498	17,184	16,624	17,142	15,301
(Inc)/dec in stock-in-trade	105	(576)	(1,840)	368	892	114	(473)	(387)
Materials	10,176	11,152	11,857	10,161	9,583	9,642	10,288	8,860
% of sales	61.4	61.6	59.9	61.3	61.5	59.3	57.4	55.6
YoY (%)	6.5	15.0	10.0	4.4	1.9	(7.8)	(2.0)	(19.5)
QoQ (%)	2.0	2.9	(5.3)	5.1	(0.5)	(6.9)	0.6	(13.7)
Staff cost	1,103	1,317	1,314	1,186	1,240	1,122	1,340	1,303
% of sales	6.6	7.7	7.9	6.9	7.3	6.8	7.8	8.6
YoY (%)	14.7	25.2	24.5	11.6	12.5	(14.8)	2.0	9.9
QoQ (%)	3.8	19.4	(0.2)	(9.7)	4.5	(9.5)	19.4	(2.8)
Other expenditure	3,617	3,721	4,010	3,799	3,715	3,867	4,120	3,561
% of sales	21.6	21.7	24.0	22.1	21.8	23.5	24.1	23.4
YoY (%)	7.7	21.8	17.2	13.5	2.7	3.9	2.7	(6.3)
QoQ (%)	8.1	2.9	7.8	(5.2)	(2.2)	4.1	6.5	(13.6)
Total expenses	15,001	15,614	15,341	15,514	15,429	14,745	15,274	13,337
EBITDA	1,741	1,567	1,394	1,661	1,607	1,708	1,812	1,899
YoY (%)	222.6	(13.5)	(27.3)	(16.8)	(7.7)	9.0	30.0	14.4
QoQ (%)	(12.7)	(10.0)	(11.1)	19.2	(3.2)	6.3	6.0	4.8
OPM (%)	10.4	9.1	8.3	9.7	9.4	10.4	10.6	12.5
Interest	150	127	161	207	296	295	301	338
Depreciation	414	435	434	459	595	619	648	693
Exceptional items	(23)	(20)		(400)	(6)	(8)	(3)	(281)
Profit before tax	1,210	1,107	863	918	859	957	918	652
YoY (%)	413.8	(11.6)	(37.2)	(25.7)	(29.0)	(13.6)	6.4	(29.0)
Provision for taxation	431	354	282	142	(11)	298	297	94
Tax Rate (%)	35.6	32.0	32.7	15.4	(1.3)	31.1	32.4	14.4
Profit after tax	779	753	580	777	870	659	621	558
PAT	779	753	580	777	870	659	621	558
YoY (%)	306.8	(9.8)	(36.2)	(8.8)	11.7	(12.5)	6.9	(28.1)
QoQ (%)	(8.5)	(3.3)	(23.0)	33.8	12.0	(24.3)	(5.8)	(10.0)
Adj PAT	802	773	580	1,176	876	667	623	839
YoY (%)	311.3	(8.0)	(36.8)	7.2	9.3	(13.7)	7.4	(28.6)
QoQ (%)	(27.0)	(3.6)	(24.9)	102.7	(25.5)	(23.9)	(6.6)	34.7

Source: Company, BOBCAPS Research

Valuation methodology

External debt borrowings to support capex will not only weaken the balance sheet, but also depress profits due to a higher interest burden. We expect CEAT to maintain its EBITDA margin at ~11% and project a revenue/EBITDA/PAT CAGR of +9%/+12%/–4% over FY20-FY23. Valuing the stock at 14x Sep'22 EPS, in line with its peers, we arrive at a target price of Rs 830. Initiate with REDUCE.

FIG 8 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

- Above-expected recovery in both replacement and OEM channels can lead to higher volumes, posing an upside risk to our estimates.
- Any further postponement of capex plans can improve cash flows for the company.
- Downward pressure in raw material prices can help profitability and bolster operating performance.

Annexure A: Company profile

Established in 1979, the RPG Group is a diversified conglomerate with interests in the areas of infrastructure, tyres, information technology, pharmaceuticals, energy and plantations. CEAT, established in 1958, is the flagship company of RPG Enterprises and one of India's leading tyre manufacturers. The company produces over 37mn tyres a year for a wide range of vehicle segments (HCV, LCV, PV, SUVs, OHT, tractors, 2Ws) and operates a combination of in-house manufacturing facilities and outsourcing units. It exports to countries across Africa, America, Australia and Asia.

FIG 9 – CORPORATE GOVERNANCE

Name	Designation	Total Remuneration (Rs mn)	No. of board meetings attended	Attended last AGM	Committees (Y/N)/ No of meetings attended					
					1- Audit	2- Nomination & remuneration	3- Stakeholders relationship	4- Risk Management	5- CSR	6- Finance and Banking
Mr H V Goenka	Chairman (Promoter)	39.6	5	Y						Y/6
Mr Anant Goenka	MD (Promoter)	47.3	5	Y					Y/2	Y/7
Mr Arnab Banerjee	Whole time director	29.1	5	Y						Y/7
Mr Atul Choksey	Independent director	1.2	4	N						
Mr Haigreve Khaitan	Independent director	1.2	4	Y						
Mr Hari L Mudra	Non-executive director	1.2	3	N	Y/3			Y/2	Y/3	
Mr Mahesh Gupta	Independent director	1.6	5	Y	Y/5	Y/5	Y/4	Y/2		
Mr Paras Chwodhary	Independent director	1.4	5	N	Y/1	Y/5	Y/4	Y/NA		Y/1
Mr Pierre E Cohade	Non-executive director	1.2	4	Y						
Ms Punita Lal	Independent director	1.3	5	Y					Y/NA	
Mr Ranjit V Pandit	Independent director	0	5	Y						
Mr S Doreswamy	Independent director	1.6	5	Y	Y/5	Y/4	Y/4	Y/2		
Mr Vinay Bansal	Independent director	1.6	5	Y	Y/5	NA	Y/NA	Y/2	Y/3	

Source: Company, BOBCAPS Research

FIG 10 – AUDITORS, BANKERS, CREDIT RATING AND CSR DETAILS

Auditors	M/s S R B C & CO LLP	
Cost Auditors	M/s D C Dave & Co, Cost Accountants	
Bankers	Axis Bank	HDFC Bank
	Bank of Baroda	ICICI Bank
	Bank of India	IDBI Bank
	Citibank	Kotak Mahindra Bank
	Citicorp Financial	RBL Bank
Credit rating		
Detail of debt	Rating	Rating agency
Long term rating	AA/Stable	CARE/India Rating and research
Short term rating	A1+	CARE
Commercial paper	A1+	CARE/India Rating and research
CSR		
Prescribed CSR (Rs mn)	105.9	
CSR expended (Rs mn)	105.9	

Source: Company, BOBCAPS Research

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue	68,313	65,811	63,466	76,980	85,085
EBITDA	5,965	7,053	6,746	8,663	9,841
Depreciation	1,743	2,554	3,287	4,087	4,887
EBIT	4,775	4,912	3,800	5,027	5,404
Net interest income/(expenses)	(677)	(1,230)	(1,454)	(1,847)	(2,198)
Other income/(expenses)	553	413	341	450	450
Exceptional items	340	(298)	0	0	0
EBT	4,438	3,385	2,346	3,180	3,206
Income taxes	1,209	678	591	801	808
Extraordinary items	0	0	0	0	0
Min. int./Inc. from associates	0	0	0	0	0
Reported net profit	3,229	2,708	1,755	2,379	2,398
Adjustments	(340)	298	0	0	0
Adjusted net profit	2,889	3,005	1,755	2,379	2,398

Balance Sheet

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Accounts payables	12,078	11,714	12,242	12,510	13,618
Other current liabilities	4,498	6,933	6,206	7,978	8,491
Provisions	1,436	1,598	1,598	1,598	1,598
Debt funds	12,605	15,676	20,676	26,676	29,676
Other liabilities	414	1,645	1,645	1,645	1,645
Equity capital	405	405	405	405	405
Reserves & surplus	27,106	28,870	30,624	33,003	35,401
Shareholders' fund	27,510	29,274	31,029	33,407	35,805
Total liabilities and equities	58,541	66,839	73,395	83,813	90,833
Cash and cash eq.	597	266	850	525	877
Accounts receivables	7,265	7,047	7,651	8,014	8,858
Inventories	9,652	8,795	8,694	9,491	10,024
Other current assets	2,133	2,066	2,561	3,031	3,208
Investments	3,130	3,202	3,002	3,002	3,002
Net fixed assets	28,463	38,205	44,918	55,831	60,944
CWIP	7,494	9,338	7,800	6,000	6,000
Intangible assets	0	0	0	0	0
Deferred tax assets, net	(2,077)	(2,611)	(2,611)	(2,611)	(2,611)
Other assets	1,884	532	532	532	532
Total assets	58,542	66,839	73,395	83,813	90,833

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Net income + Depreciation	4,972	5,262	5,042	6,466	7,285
Interest expenses	677	1,230	1,454	1,847	2,198
Non-cash adjustments	(553)	(413)	(341)	(450)	(450)
Changes in working capital	954	5,957	(1,196)	409	67
Other operating cash flows	(475)	0	0	0	0
Cash flow from operations	5,575	12,035	4,959	8,271	9,100
Capital expenditures	(11,434)	(14,139)	(8,462)	(13,200)	(10,000)
Change in investments	70	(72)	200	0	0
Other investing cash flows	553	413	341	450	450
Cash flow from investing	(10,811)	(13,798)	(7,921)	(12,750)	(9,550)
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	6,196	3,071	5,000	6,000	3,000
Interest expenses	(677)	(1,230)	(1,454)	(1,847)	(2,198)
Dividends paid	(465)	(485)	0	0	0
Other financing cash flows	49	75	0	0	0
Cash flow from financing	5,103	1,431	3,546	4,153	802
Changes in cash and cash eq.	(133)	(331)	584	(325)	352
Closing cash and cash eq.	597	266	850	525	877

Per Share

Y/E 31 Mar (Rs)	FY19A	FY20A	FY21E	FY22E	FY23E
Reported EPS	71.4	74.3	43.4	58.8	59.3
Adjusted EPS	71.4	74.3	43.4	58.8	59.3
Dividend per share	11.5	12.0	0.0	0.0	0.0
Book value per share	680.1	723.7	767.1	825.9	885.2

Valuations Ratios

Y/E 31 Mar (x)	FY19A	FY20A	FY21E	FY22E	FY23E
EV/Sales	0.6	0.7	0.8	0.7	0.7
EV/EBITDA	7.0	6.2	7.2	6.1	5.9
Adjusted P/E	12.2	11.7	20.0	14.8	14.6
P/BV	1.3	1.2	1.1	1.1	1.0

DuPont Analysis

Y/E 31 Mar (%)	FY19A	FY20A	FY21E	FY22E	FY23E
Tax burden (Net profit/PBT)	65.1	88.8	74.8	74.8	74.8
Interest burden (PBT/EBIT)	92.9	68.9	61.7	63.3	59.3
EBIT margin (EBIT/Revenue)	7.0	7.5	6.0	6.5	6.4
Asset turnover (Revenue/Avg TA)	187.7	151.1	127.0	133.8	132.1
Leverage (Avg TA/Avg Equity)	1.4	1.5	1.7	1.8	1.9
Adjusted ROAE	10.9	10.6	5.8	7.4	6.9

Source: Company, BOBCAPS Research | Note: TA = Total Assets

Ratio Analysis

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
YoY growth (%)					
Revenue	10.0	(3.7)	(3.6)	21.3	10.5
EBITDA	(1.6)	18.2	(4.4)	28.4	13.6
Adjusted EPS	3.7	4.0	(41.6)	35.6	0.8
Profitability & Return ratios (%)					
EBITDA margin	8.7	10.7	10.6	11.3	11.6
EBIT margin	7.0	7.5	6.0	6.5	6.4
Adjusted profit margin	4.2	4.6	2.8	3.1	2.8
Adjusted ROAE	10.5	10.3	5.7	7.1	6.7
ROCE	9.5	9.0	5.7	6.5	6.3
Working capital days (days)					
Receivables	38	40	42	37	36
Inventory	46	51	50	43	42
Payables	92	113	117	100	96
Ratios (x)					
Gross asset turnover	0.5	0.7	0.9	0.9	1.0
Current ratio	1.1	0.9	1.0	1.0	1.0
Net interest coverage ratio	(7.1)	(4.0)	(2.6)	(2.7)	(2.5)
Adjusted debt/equity	0.5	0.5	0.7	0.8	0.8

Source: Company, BOBCAPS Research

BUY

TP: Rs 85 | ▲ 31%

JK TYRE & INDUSTRIES

Auto Components

05 August 2020

Addressing leverage concerns; initiate with BUY

JK Tyre (JKI) derives ~85% of revenues from truck, bus and PV tyres, a favourable mix that should aid an 9% topline CAGR over FY20-FY23. Higher replacement demand (~63% of revenues) and lower rubber prices are likely to aid a slight rise in operating margins to ~12%. By prudent working capital management, JKI has managed to pare its gross debt by Rs 6.3bn in FY20. We expect the net D/E ratio to improve further from 2.1x in FY20 to 1.5x by FY23-end. Initiate with BUY and a Sep'21 TP of Rs 85.

Mayur Milak | Nishant Chowhan, CFA
 research@bobcaps.in

Balance sheet improvement in challenging times: JKI's prime concern remains the high leverage on its balance sheet. Notably, despite a 15% YoY decline in revenues during FY20, the company has reduced its gross debt by Rs 6.3bn to ~Rs 51bn through efficient working capital management. Consequently, its net D/E ratio has declined from a peak of 2.9x in FY18 to 2.1x in FY20 and is expected to come off further to 1.5x by FY23-end.

Ticker/Price	JKI IN/Rs 65
Market cap	US\$ 211.7mn
Shares o/s	246mn
3M ADV	US\$ 0.9mn
52wk high/low	Rs 71/Rs 63
Promoter/FPI/DII	56%/3%/1%

Source: NSE

Biggest beneficiary of anti-dumping duty on China: With the recent imposition of additional import duties along with the earlier anti-dumping duty on Chinese imports of cheaper tyres, domestic players have gained a significant advantage. We believe tyre imports have shrunk to 50,000-60,000 units a month (from an average of 100,000 units a month). Being the cheapest and largest player in India's truck & bus radial (TBR) tyre replacement market, JKI is bound to be the biggest beneficiary of this slowdown in Chinese imports.

STOCK PERFORMANCE



Source: NSE

Initiate with BUY: We forecast a revenue/EBITDA/PAT CAGR of 9%/11%/13% over FY20-FY23, backed by steady replacement demand and benign rubber prices. Factoring in the high leverage, we value the stock at 7x Sep'22 EPS, a discount of 60% to the market leader, and recommend BUY for a TP of Rs 85.

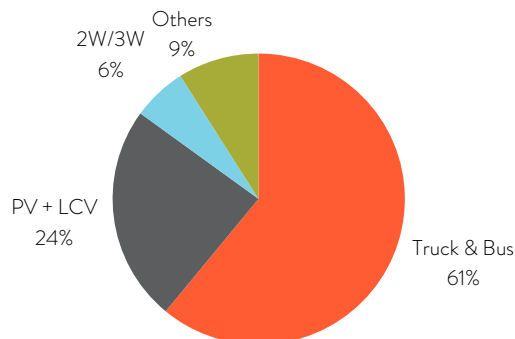
KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue (Rs mn)	103,699	87,249	83,648	101,189	111,931
EBITDA (Rs mn)	10,251	9,876	9,774	12,092	13,441
Adj. net profit (Rs mn)	1,706	2,472	887	2,595	3,561
Adj. EPS (Rs)	6.9	10.0	3.6	10.5	14.5
Adj. EPS growth (%)	137.9	44.9	(64.1)	192.5	37.2
Adj. ROAE (%)	7.0	10.2	3.5	9.5	11.7
Adj. P/E (x)	9.3	6.4	17.9	6.1	4.5
EV/EBITDA (x)	6.9	7.3	7.0	5.3	4.7

Source: Company, BOBCAPS Research

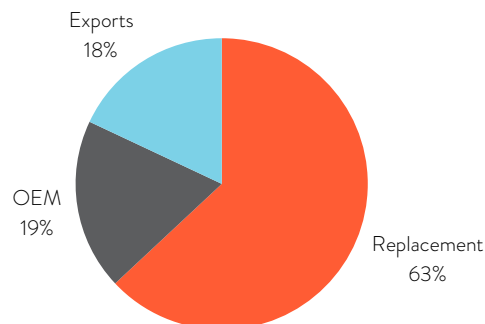
Investment summary

FIG 1 – 85% OF JKI’S REVENUES COME FROM T&B AND PV TYRES; EXPECT 9% CAGR FOR FY20-FY23E



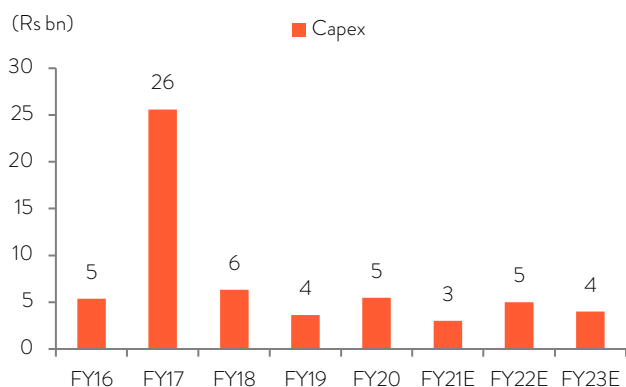
Source: Company, BOBCAPS Research

FIG 2 – HIGHER SHARE IN REPLACEMENT MARKET OFFERS STEADY GROWTH AND BETTER MARGINS



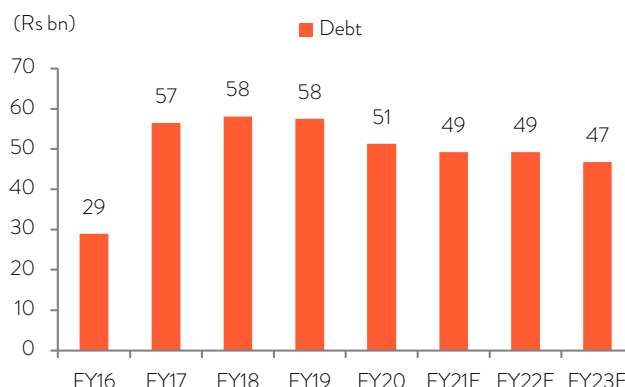
Source: Company, BOBCAPS Research

FIG 3 – AFTER HEAVY CAPEX IN FY17, JKI HAS CONSCIOUSLY RUN CALIBRATED CAPEX PROGRAMS



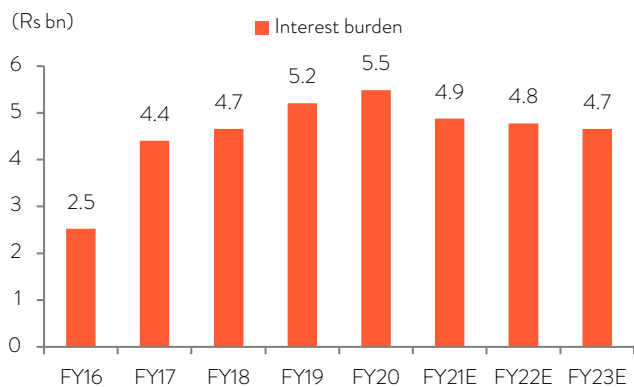
Source: Company, BOBCAPS Research

FIG 4 – WE EXPECT GROSS DEBT REDUCTION TREND TO CONTINUE...



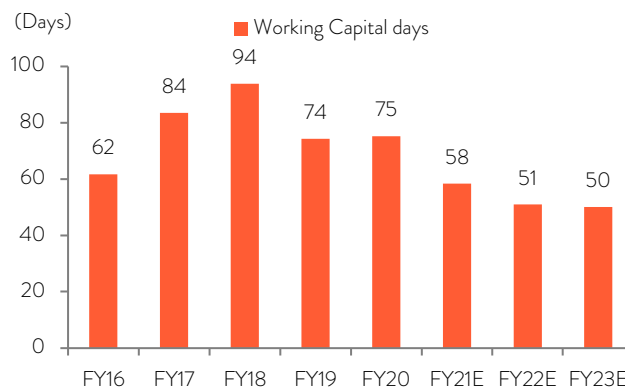
Source: Company, BOBCAPS Research

FIG 5 – ...AIDING DECLINE IN INTEREST BURDEN



Source: Company, BOBCAPS Research

FIG 6 – WORKING CAPITAL EFFICIENCY HAS IMPROVED, ASSISTING CASH MANAGEMENT



Source: Company, BOBCAPS Research

Financial review

MHCV & LCV tyres (74% of domestic revenue) forecast to clock 9% volume CAGR

PV tyres (13% of domestic revenue) to grow at 9%

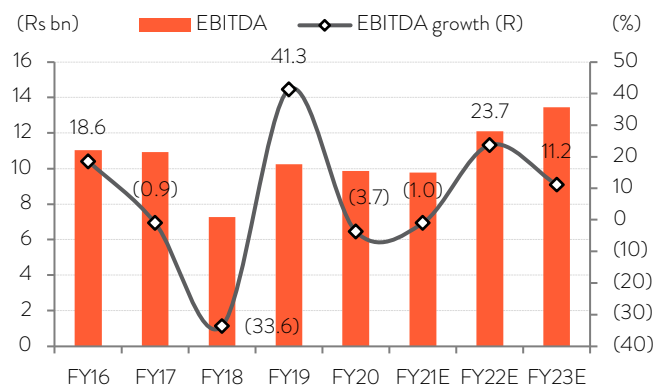
We expect a flattish CAGR from JKI's Mexican subsidiary

FIG 7 – REVENUE PROJECTED TO GROW AT 9% CAGR DURING FY20-FY23E



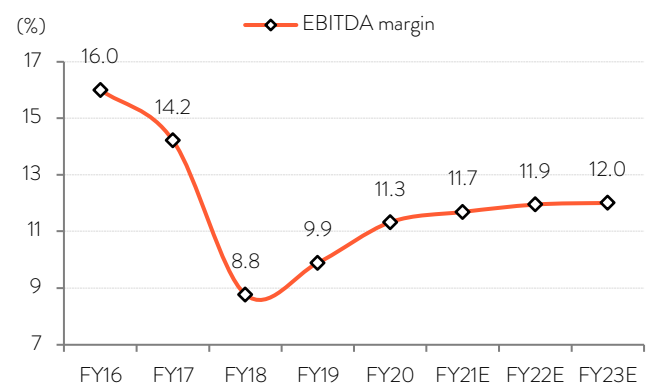
Source: Company, BOBCAPS Research

FIG 8 – EBITDA TO POST 11% CAGR FOR FY20-FY23E



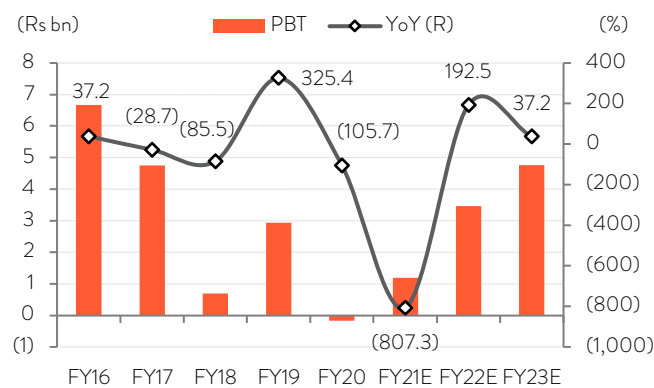
Source: Company, BOBCAPS Research

FIG 9 – EBITDA MARGIN FORECAST AT ~12%



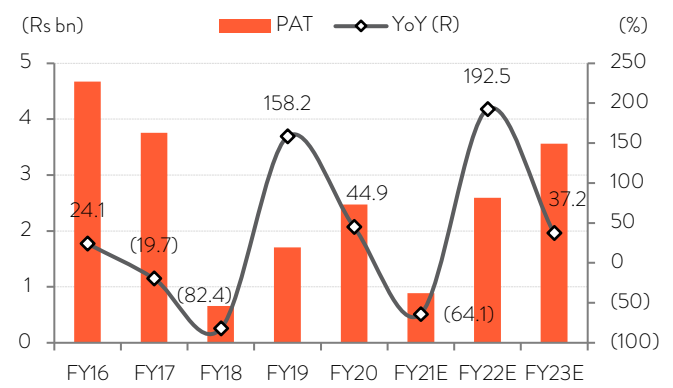
Source: Company, BOBCAPS Research

FIG 10 – EXTRAORDINARY PRE-TAX LOSS OF RS 1BN IN FY20



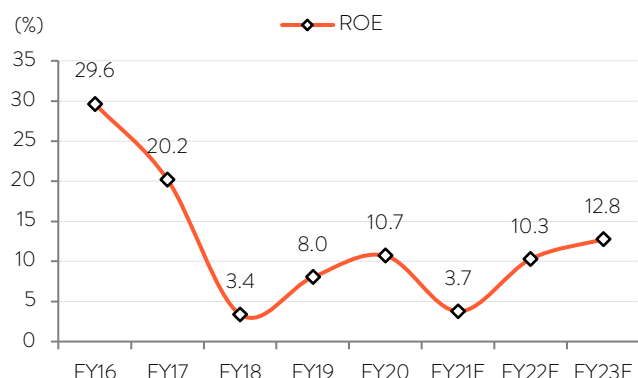
Source: Company, BOBCAPS Research

FIG 11 – PAT CAGR EXPECTED AT 13% OVER FY20-FY23E



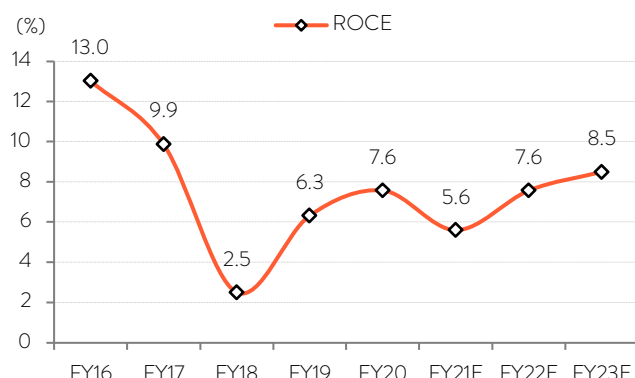
Source: Company, BOBCAPS Research

FIG 12 – ROE PROJECTED TO IMPROVE SHARPLY BETWEEN FY21 AND FY23



Source: Company, BOBCAPS Research

FIG 13 – ROCE TO RECOVER BY END-FY23



Source: Company, BOBCAPS Research

FIG 14 – QUARTERLY PERFORMANCE – CONSOLIDATED RESULTS

(Rs mn)	Q1FY19	Q2FY19	Q3FY19	Q4FY19	Q1FY20	Q2FY20	Q3FY20	Q4FY20
Net sales	24,395	24,938	27,308	27,059	25,754	21,550	21,998	17,948
YoY (%)	35.0	21.2	28.6	18.5	5.6	(13.6)	(19.4)	(33.7)
QoQ (%)	6.8	2.2	9.5	(0.9)	(4.8)	(16.3)	2.1	(18.4)
(Inc)/dec in stock-in-trade	(627)	(1,481)	(1,167)	326	1,241	(545)	720	(1,561)
Materials	15,248	17,204	19,459	17,885	15,899	13,051	12,750	11,814
% of sales	59.9	63.0	67.0	67.3	66.6	58.0	61.2	57.1
YoY (%)	19.9	19.8	34.6	34.0	17.2	(20.5)	(26.4)	(43.7)
QoQ (%)	7.6	7.5	16.3	(0.4)	(5.9)	(27.0)	7.7	(23.9)
Staff cost	2,281	2,432	2,257	2,126	2,310	2,205	2,377	2,340
% of sales	9.4	9.8	8.3	7.9	9.0	10.2	10.8	13.0
YoY (%)	3.3	24.8	20.8	(1.3)	1.2	(9.3)	5.3	10.1
QoQ (%)	5.8	6.6	(7.2)	(5.8)	8.6	(4.5)	7.8	(1.6)
Other expenditure	4,239	4,159	4,107	4,111	3,908	3,874	3,709	3,280
% of sales	17.4	16.7	15.0	15.2	15.2	18.0	16.9	18.3
YoY (%)	15.4	17.2	12.6	8.0	(7.8)	(6.9)	(9.7)	(20.2)
QoQ (%)	11.4	(1.9)	(1.2)	0.1	(4.9)	(0.9)	(4.3)	(11.6)
Total expenses	21,140	22,314	24,656	24,449	23,358	18,586	19,556	15,873
EBITDA	3,255	2,624	2,652	2,610	2,396	2,964	2,442	2,074
YoY (%)	NA	34.0	24.5	(20.7)	(26.4)	12.9	(7.9)	(20.5)
QoQ (%)	(1.2)	(19.4)	1.0	(1.6)	(8.2)	23.7	(17.6)	(15.1)
OPM (%)	13.3	10.5	9.7	9.6	9.3	13.8	11.1	11.6
Other income	66	545	110	101	61	67	73	83
Interest	1,210	1,276	1,310	1,415	1,385	1,396	1,361	1,348
Depreciation	774	791	796	796	912	916	928	1,023
Exceptional items	(237)	(420)	(205)	(29)	47	(503)	8	(611)
Profit before tax	1,101	682	450	472	207	216	233	(824)
YoY (%)	(161.6)	447.2	95.1	(81.1)	(81.2)	(68.3)	(48.2)	(274.7)
Provision for taxation	427	199	203	113	50	(1,470)	117	(355)
Tax Rate (%)	38.8	29.2	45.0	23.9	24.2	(679.6)	50.0	43.0
PAT	674	483	247	359	157	1,686	117	(470)

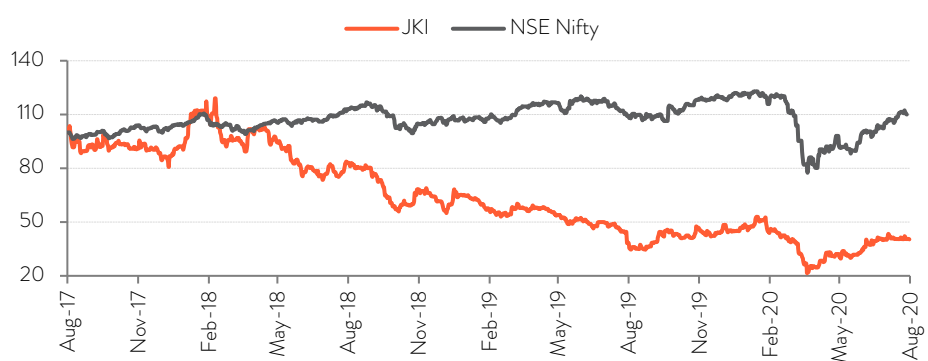
(Rs mn)	Q1FY19	Q2FY19	Q3FY19	Q4FY19	Q1FY20	Q2FY20	Q3FY20	Q4FY20
Shares of Associates	(31)	(25)	22	(22)	4	(9)	(14)	(58)
Consolidated PAT	642	458	269	337	161	1,677	103	(528)
YoY (%)	(154.0)	342.7	137.5	(78.8)	(74.9)	266.3	(61.7)	(256.8)
QoQ (%)	(59.6)	(28.7)	(41.3)	25.2	(52.1)	940.3	(93.9)	(612.9)
Adj PAT	879	877	473	365	114	2,180	95	84
YoY (%)	(174.2)	728.6	120.0	(77.1)	(87.0)	148.4	(80.0)	(77.1)
QoQ (%)	(44.8)	(0.2)	(46.1)	(22.8)	(68.8)	1,810.4	(95.7)	(11.8)
Adj EPS	3.9	3.9	2.1	1.6	0.5	9.6	0.4	0.4

Source: Company, BOBCAPS Research

Valuation methodology

We forecast a revenue/EBITDA/PAT CAGR of 9%/11%/13% for JKI over FY20-FY22, backed by steady replacement demand and benign rubber prices. Factoring in the high leverage, we value the stock at 7x Sep'22 EPS, a discount of 60% to the market leader. Initiate coverage with BUY and a target price of Rs 85.

FIG 15 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

- Slower growth in M&HCV tyres will impact revenues.
- A spike in natural rubber or crude derivatives will impact margins negatively.

Annexure A: Company profile

JKI is one of India's foremost tyre manufacturers and ranks amongst the top 25 manufacturers in the world. The company provides end-to-end solutions across the PV, CV, farming, off-the-road and 2W/3W segments. Pioneers of radial technology, JKI produced the first radial tyre in 1977 and is currently market leader in the TBR segment.

JKI is present in 105 countries with over 180 global distributors. It also has a strong dealer network of over 4,000 dealers and 500+ dedicated brand shops called 'Steel Wheels' and 'Xpress Wheels'. The company has 12 manufacturing facilities – 9 in India and 3 in Mexico, with a capacity of more than 16.6mn tyres per annum.

In Apr'16, JKI acquired Cavendish Industries in Haridwar, Uttarakhand. While the acquisition added three modern plants to its portfolio taking the total count to 12, it helped the tyre major foray into the 2W/3W segment as well.

FIG 1 – A BIRD'S EYE VIEW ON CORPORATE GOVERNANCE

Name	Designation	Total Remuneration (Rs mn)	No. of board meetings attended	Attended last AGM	Committees (Y/N)/ No of meetings attended				
					1- Audit	2- Nomination & remuneration	3- Stakeholders relationship	4- Risk Management	5- CSR
Dr Raghupati Singhania	Chariman & M D	109.7	4	Y					Y
Mr Bharat Hari Singhania	MD	77.1	2	N					
Mr Anshuman Singhania	Whole-time director	45.9	4	Y				Y	
Mr Arun Kumar Bajoria	Director & President	51.2	4	Y	Y/4		Y/1	Y	Y
Mrs Sunanda Singhania	Independent director	1.4	2	N					
Mr Arvind Singh Mewar	Independent director	1.8	3	Y	Y/3	Y/3			Y
Mr Bakul Jain	Independent director	1.7	3	Y	Y/3		Y/1		
Mr Shreekant Somany	Independent director	1.8	4	N	Y/4		Y/1	Y	
Mr Vimal Bhandari	Independent director	1.6	3	Y		Y/2			
Mr Kalpataru Tripathy	Independent director	1.7	4	Y		Y/3		Y	
Dr Wolfgang Holzbach	Independent director	1.6	3	Y					

Source: Company, BOBCAPS Research

FIG 2 – AUDITORS, BANKERS, CREDIT RATING AND CSR DETAILS

Auditors	M/s S S Kothari Mehta & Co	
Cost Auditors	M/s R J Goel & Co	
Bankers	Bank of India	Federal Bank
	Corporation Bank	Indian Bank
	IDBI Bank	State Bank of India
	Punjab National Bank	
Credit rating		
Detail of debt	Rating	Rating agency
Long term rating	A+, Negative	CARE
Short term rating	A1+	CARE
Commercial paper	A1+	CARE
Fixed deposit	A+; Negative	CARE
CSR		
Prescribed CSR (Rs mn)	71.86	
CSR expensed (Rs mn)	71.86	

Source: Company, BOBCAPS Research

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue	103,699	87,249	83,648	101,189	111,931
EBITDA	10,251	9,876	9,774	12,092	13,441
Depreciation	3,157	3,778	3,966	4,126	4,306
EBIT	7,915	6,381	6,060	8,246	9,415
Net interest income/(expenses)	(5,211)	(5,490)	(4,873)	(4,776)	(4,655)
Other income/(expenses)	821	284	252	280	280
Exceptional items	231	(1,059)	0	0	0
EBT	2,936	(168)	1,186	3,470	4,760
Income taxes	942	(1,658)	299	874	1,200
Extraordinary items	0	0	0	0	0
Min. int./Inc. from associates	0	0	0	0	0
Reported net profit	1,937	1,413	887	2,595	3,561
Adjustments	(231)	1,059	0	0	0
Adjusted net profit	1,706	2,472	887	2,595	3,561

Balance Sheet

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Accounts payables	15,990	16,884	17,051	16,813	18,546
Other current liabilities	5,776	10,467	10,272	13,700	13,834
Provisions	223	1,196	0	0	0
Debt funds	57,575	51,241	49,241	49,241	46,741
Other liabilities	4,817	6,055	6,055	6,055	6,055
Equity capital	492	493	493	493	493
Reserves & surplus	23,713	23,768	24,584	26,816	29,878
Shareholders' fund	24,206	24,261	25,077	27,309	30,371
Total liabilities and equities	108,588	110,103	107,695	113,117	115,546
Cash and cash eq.	1,697	1,365	2,312	2,838	2,988
Accounts receivables	19,451	18,484	17,188	19,406	21,160
Inventories	16,891	16,178	14,896	16,634	17,173
Other current assets	6,419	6,025	6,188	6,654	6,747
Investments	1,312	1,402	1,402	1,402	1,402
Net fixed assets	62,276	63,888	62,921	63,795	63,488
CWIP	2,698	2,772	2,800	2,400	2,600
Intangible assets	0	0	0	0	0
Deferred tax assets, net	(4,101)	(2,030)	(2,030)	(2,030)	(2,030)
Other assets	1,945	2,018	2,018	2,018	2,018
Total assets	108,588	110,103	107,695	113,117	115,546

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Net income + Depreciation	5,093	5,191	4,854	6,722	7,867
Interest expenses	5,211	5,490	4,873	4,776	4,655
Non-cash adjustments	(821)	(284)	(252)	(280)	(280)
Changes in working capital	(2,046)	9,796	1,192	(1,232)	(518)
Other operating cash flows	(244)	0	0	0	0
Cash flow from operations	7,194	20,193	10,666	9,985	11,724
Capital expenditures	(3,621)	(5,464)	(3,028)	(4,600)	(4,200)
Change in investments	(30)	(91)	0	0	0
Other investing cash flows	763	(131)	252	280	280
Cash flow from investing	(2,888)	(5,686)	(2,775)	(4,320)	(3,920)
Equities issued/Others	1,969	0	0	0	0
Debt raised/repaid	(538)	(6,334)	(2,000)	0	(2,500)
Interest expenses	(5,211)	(5,490)	(4,873)	(4,776)	(4,655)
Dividends paid	(340)	(208)	(71)	(363)	(498)
Other financing cash flows	202	(2,806)	0	0	0
Cash flow from financing	(3,917)	(14,839)	(6,944)	(5,140)	(7,654)
Changes in cash and cash eq.	390	(331)	947	526	150
Closing cash and cash eq.	1,697	1,365	2,312	2,838	2,838

Per Share

Y/E 31 Mar (Rs)	FY19A	FY20A	FY21E	FY22E	FY23E
Reported EPS	6.9	10.0	3.6	10.5	14.5
Adjusted EPS	6.9	10.0	3.6	10.5	14.5
Dividend per share	1.4	0.7	0.3	1.5	2.0
Book value per share	92.8	94.7	98.0	107.1	119.5

Valuations Ratios

Y/E 31 Mar (x)	FY19A	FY20A	FY21E	FY22E	FY23E
EV/Sales	0.7	0.8	0.8	0.6	0.6
EV/EBITDA	6.9	7.3	7.0	5.3	4.7
Adjusted P/E	9.3	6.4	17.9	6.1	4.5
P/BV	0.7	0.7	0.7	0.6	0.5

DuPont Analysis

Y/E 31 Mar (%)	FY19A	FY20A	FY21E	FY22E	FY23E
Tax burden (Net profit/PBT)	58.1	(1474.1)	74.8	74.8	74.8
Interest burden (PBT/EBIT)	37.1	(2.6)	19.6	42.1	50.6
EBIT margin (EBIT/Revenue)	7.6	7.3	7.2	8.1	8.4
Asset turnover (Revenue/Avg TA)	121.9	103.8	103.3	124.2	135.0
Leverage (Avg TA/Avg Equity)	4.0	3.6	3.4	3.2	3.0
Adjusted ROAE	8.0	10.7	3.7	10.3	12.8

Source: Company, BOBCAPS Research | Note: TA = Total Assets

Ratio Analysis

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
YoY growth (%)					
Revenue	25.4	(15.9)	(4.1)	21.0	10.6
EBITDA	41.3	(3.7)	(1.0)	23.7	11.2
Adjusted EPS	137.9	44.9	(64.1)	192.5	37.2
Profitability & Return ratios (%)					
EBITDA margin	9.9	11.3	11.7	11.9	12.0
EBIT margin	7.6	7.3	7.2	8.1	8.4
Adjusted profit margin	1.6	2.8	1.1	2.6	3.2
Adjusted ROAE	7.0	10.2	3.5	9.5	11.7
ROCE	6.3	7.6	5.6	7.6	8.5
Working capital days (days)					
Receivables	61	79	78	66	66
Inventory	55	69	68	57	55
Payables	75	112	123	101	95
Ratios (x)					
Gross asset turnover	0.9	1.1	1.2	1.0	1.0
Current ratio	2.0	1.5	1.5	1.5	1.5
Net interest coverage ratio	(1.5)	(1.2)	(1.2)	(1.7)	(2.0)
Adjusted debt/equity	2.5	2.2	2.0	1.9	1.6

Source: Company, BOBCAPS Research

ADD

TP: Rs 67,000 | ▲ 10%

MRF

| Auto Components

| 05 August 2020

Market leader; replacement demand to propel growth – ADD

MRF continues to dominate the Indian tyre industry with market share ranging from 24% to 33% in most segments. Per our estimates, MRF derives >80% of its revenues from truck, bus and passenger tyres – segments we expect will recover the fastest over the next two years. High replacement demand (>70% of rev) and benign RM costs will enhance its already best-in-class EBITDA margins (~15%). We expect a brisk 10% earnings CAGR for FY20-FY23 but the current valuation caps upsides. Initiate with ADD; Sep'21 TP Rs 67,000.

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 research@bobcaps.in

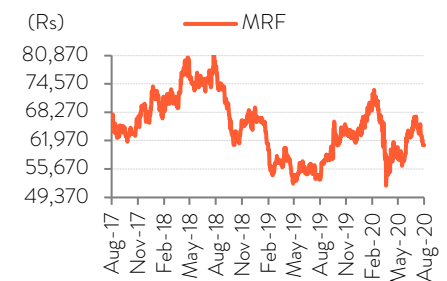
Replacement demand to fuel growth: MRF is India's largest tyre manufacturer commanding ~25% market share. We expect the company to post a 9% revenue CAGR during FY20-FY23, anchored by its strong brand, over 70% revenue share derived from the replacement segment and expected recovery in auto sector demand. We estimate a healthy volume CAGR of 9% in MHCV and LCV tyres (60% of domestic revenues) and 8% in PV tyres (21% share) for MRF over our forecast period, alongside stable EBITDA margins of ~15%.

Ticker/Price	MRF IN/Rs 60,975
Market cap	US\$ 3.4bn
Shares o/s	4mn
3M ADV	US\$ 9.0mn
52wk high/low	Rs 73,566/Rs 49,915
Promoter/FPI/DII	28%/5%/14%

Source: NSE

Scrappage policy, wide distribution network to augment demand: MRF has the widest distribution network in India, covering over 4,500 dealers and 300 franchisees across the country. If the government supports the MHCV industry with an aggressive old-vehicle scrappage policy, MRF's market leadership positions it to best capitalise on the additional demand.

STOCK PERFORMANCE



Source: NSE

Initiate with ADD: Our revenue/EBITDA/PAT CAGR projections stand at 9%/10%/10% over FY20-FY23 (adj. for DTA) and do not bake in demand due to the proposed scrappage policy. The stock currently trades at 20.7x/19.3x FY22E/FY23E EPS and upsides look capped. We arrive at a Sep'21 TP of Rs 67,000, set at 22x Sep'22 EPS. Initiate with an ADD recommendation.

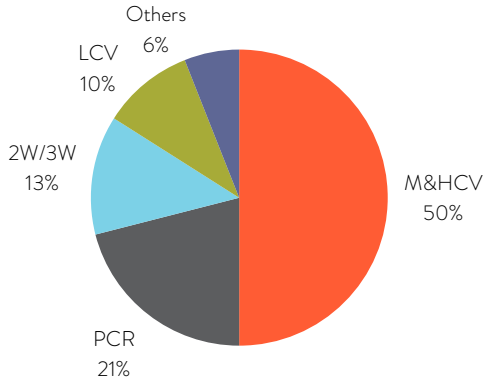
KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue (Rs mn)	158,370	159,911	154,695	188,628	208,497
EBITDA (Rs mn)	22,504	23,237	22,502	27,909	31,218
Adj. net profit (Rs mn)	10,969	13,950	9,866	12,481	13,413
Adj. EPS (Rs)	2,587.0	3,290.0	2,326.8	2,943.5	3,163.5
Adj. EPS growth (%)	0.4	27.2	(29.3)	26.5	7.5
Adj. ROAE (%)	10.3	11.6	7.6	8.8	8.6
Adj. P/E (x)	23.6	18.5	26.2	20.7	19.3
EV/EBITDA (x)	12.1	11.7	11.8	9.3	8.4

Source: Company, BOBCAPS Research

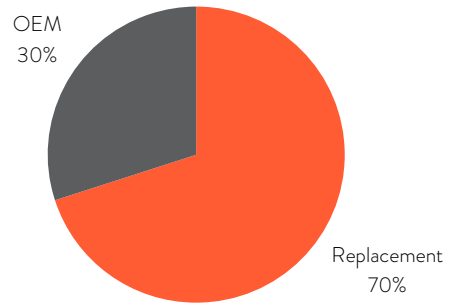
Investment summary

FIG 1 – T&B AND PV TYRES FORM 81% OF REVENUES; WE EXPECT STRONG GROWTH IN THESE SEGMENTS



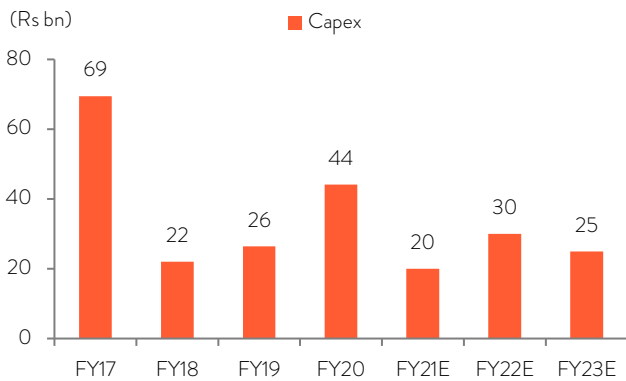
Source: Company, BOBCAPS Research

FIG 2 – HIGHER REPLACEMENT MIX SHOULD SUPPORT REVENUE GROWTH



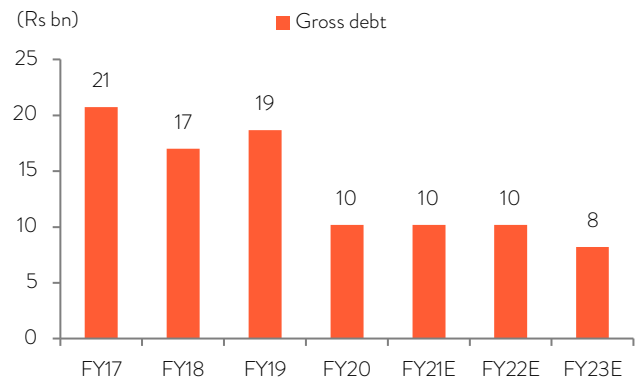
Source: Company, BOBCAPS Research

FIG 3 – BALANCED CAPEX TREND REFLECTS MANAGEMENT FORESIGHT



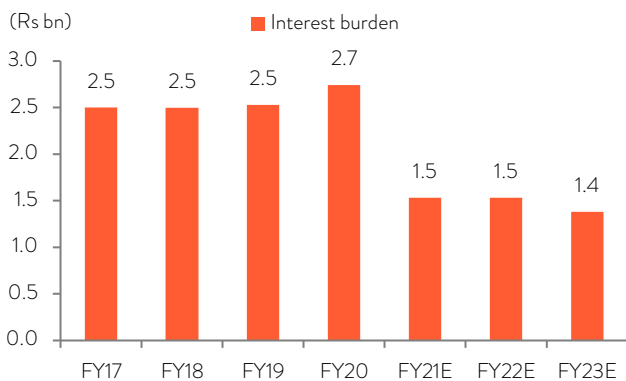
Source: Company, BOBCAPS Research

FIG 4 – MRF THE ONLY TYRE COMPANY TO HAVE STRONG CONTROL OVER GROSS DEBT



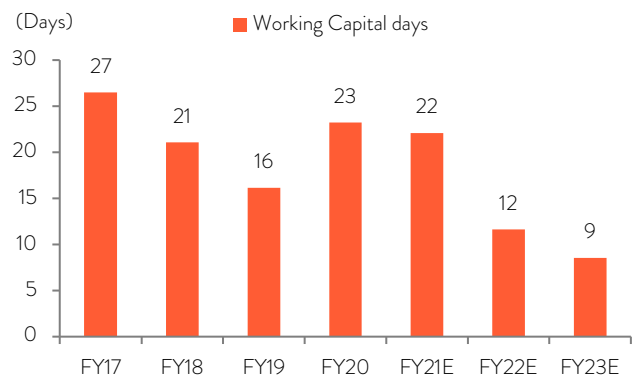
Source: Company, BOBCAPS Research

FIG 5 – INTEREST BURDEN NEGLIGIBLE



Source: Company, BOBCAPS Research

FIG 6 – WORKING CAPITAL TREND STEADY



Source: Company, BOBCAPS Research

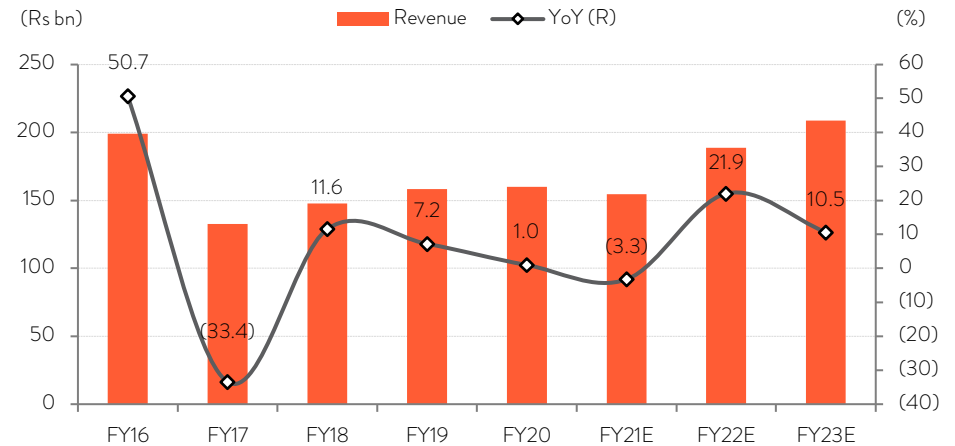
Financial review

FIG 7 – EXPECT 9% REVENUE CAGR OVER FY20–FY23E

M&HCV and LCV segments (60% of domestic revenues) to clock 9% volume CAGR

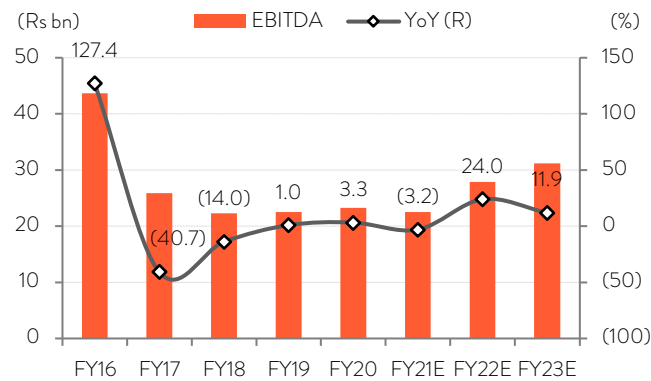
PV tyres (21% of domestic revenues) to grow at 9%

2W/3W tyres (13% of consolidated revenues) to log 6% volume CAGR



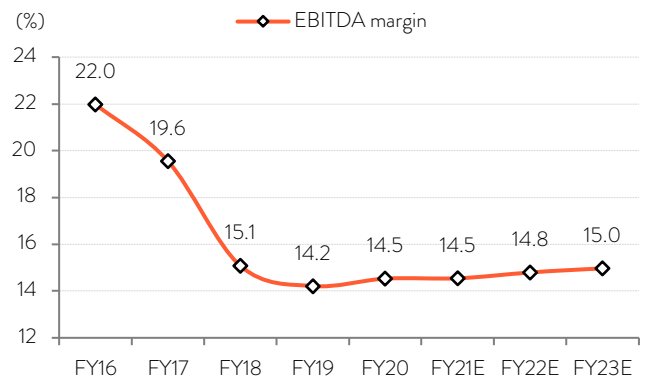
Source: Company, BOBCAPS Research

FIG 8 – EBITDA TO GROW AT 10% CAGR



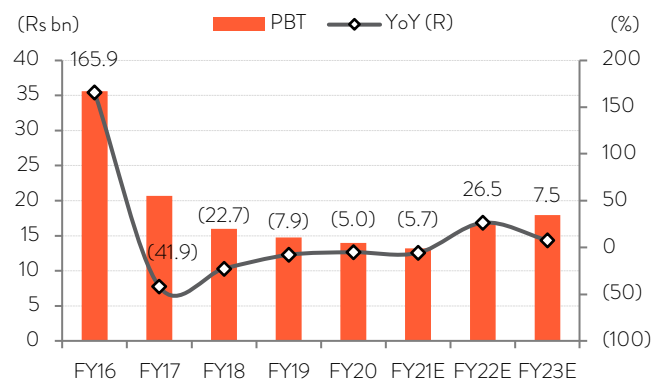
Source: Company, BOBCAPS Research

FIG 9 – BEST-IN-CLASS EBITDA MARGIN FORTIFIED BY PREMIUM PRICING AND BENIGN RM PRICES



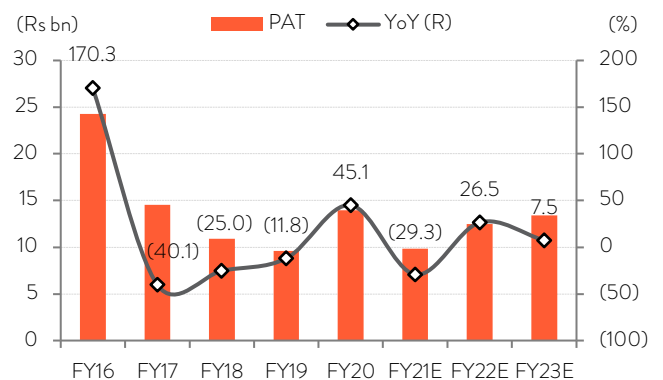
Source: Company, BOBCAPS Research

FIG 10 – PBT PROJECTED TO RISE AT 9% CAGR

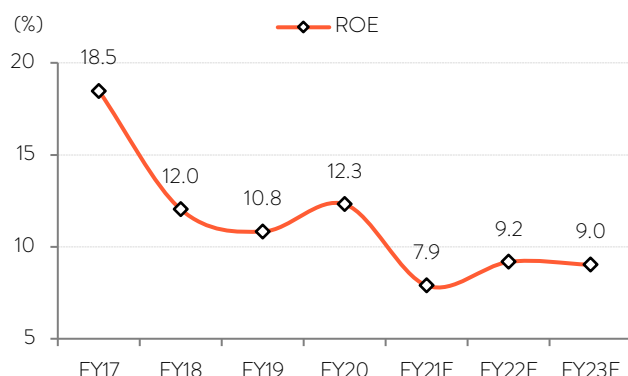


Source: Company, BOBCAPS Research

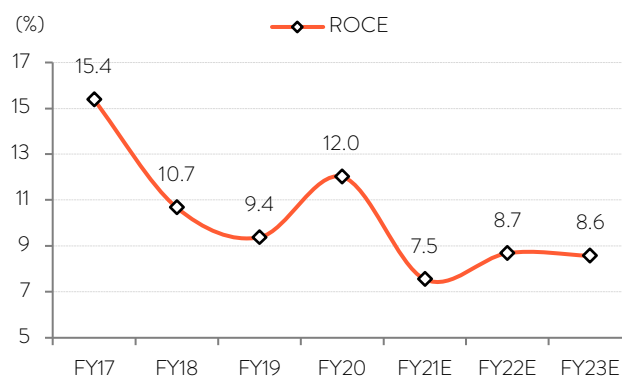
FIG 11 – EXPECT PAT CAGR OF 10% (EX-DEFERRED TAX ASSET BENEFIT OF RS 4BN IN FY20)



Source: Company, BOBCAPS Research

FIG 12 – ROE EXPECTED TO REVERSE TREND FROM FY21 ONWARDS


Source: Company, BOBCAPS Research

FIG 13 – SIMILAR FOR ROCE...


Source: Company, BOBCAPS Research

FIG 14 – QUARTERLY PERFORMANCE:

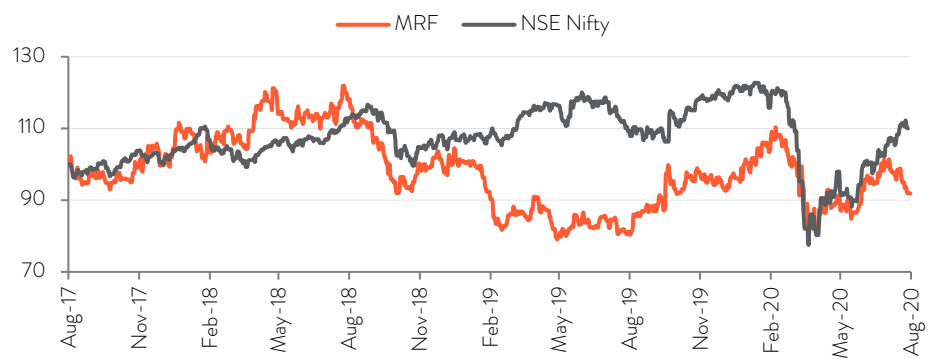
(Rs mn)	Q1FY19	Q2FY19	Q3FY19	Q4FY19	Q1FY20	Q2FY20	Q3FY20	Q4FY20
Net Sales/Income from operations	38,556	39,281	40,338	40,735	44,095	39,476	40,089	36,252
YoY (%)	8.1	9.4	6.2	5.4	14.4	0.5	(0.6)	(11.0)
QoQ (%)	(0.3)	1.9	2.7	1.0	8.2	(10.5)	1.6	(9.6)
(Inc) / Dec in stock and WIP	(114)	(2,431)	(2,448)	(1,093)	873	(664)	762	(721)
Consumption of R.M & Components	23,306	26,102	27,185	25,910	26,090	24,134	23,171	21,446
% of sales	60.2	60.3	61.3	60.9	61.1	59.5	59.7	57.2
YoY (%)	(3.7)	9.9	11.5	8.5	16.3	(0.9)	(3.2)	(16.5)
QoQ (%)	1.4	2.1	4.5	0.3	8.6	(13.0)	2.0	(13.4)
Staff Cost	2,719	2,881	2,979	2,864	3,085	3,300	3,380	3,441
% of sales	7.1	7.3	7.4	7.0	7.0	8.4	8.4	9.5
YoY (%)	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.2
QoQ (%)	(0.0)	0.1	0.0	(0.0)	0.1	0.1	0.0	0.0
Other expenditure	6,692	6,919	7,104	7,342	8,020	7,299	6,675	6,387
% of sales	17.4	17.6	17.6	18.0	18.2	18.5	16.6	17.6
YoY (%)	0.1	0.2	0.2	0.2	0.2	0.1	(0.1)	(0.1)
QoQ (%)	0.1	0.0	0.0	0.0	0.1	(0.1)	(0.1)	(0.0)
Total Expenditure	32,602	33,472	34,819	35,022	38,067	34,068	33,987	30,553
Operating Profit	5,953	5,810	5,518	5,712	6,028	5,408	6,102	5,699
YoY (%)	116.5	(4.1)	(21.5)	(16.8)	1.3	(6.9)	10.6	(0.2)
QoQ (%)	(13.3)	(2.4)	(5.0)	3.5	5.5	(10.3)	12.8	(6.6)
OPM (%)	15.4	14.8	13.7	14.0	13.7	13.7	15.2	15.7
Other Income	516	767	1,258	1,095	1,049	948	733	575
Interest	631	643	631	573	682	665	704	692
Depreciation	1,867	1,998	2,052	2,146	2,280	2,372	2,490	2,665
Profit before excptnl itms and tax	3,971	3,936	4,093	4,088	4,115	3,319	3,641	2,918
Exceptional Items	-	-	-	-	-	-	-	-
Profit Before Tax	3,971	3,936	4,093	4,088	4,115	3,319	3,641	2,918
YoY (%)	195.0	(10.7)	(20.1)	(20.5)	3.6	(15.7)	(11.0)	(28.6)
Less: Provision for Taxation	1,364	1,306	1,300	1,150	1,430	1,115	1,275	(3,777)
Tax Rate (%)	34.3	33.2	31.8	28.1	34.7	33.6	35.0	(129.4)
Profit After Tax	2,607	2,630	2,793	2,938	2,685	2,204	2,366	6,695
YoY (%)	144.8	(12.3)	(18.0)	(15.1)	3.0	(16.2)	(15.3)	127.8
QoQ (%)	(24.6)	0.9	6.2	5.2	(8.6)	(17.9)	7.4	182.9
EPS	615	620	659	693	633	520	558	1,579

Source: Company, BOBCAPS Research

Valuation methodology

We project a revenue/EBITDA/PAT CAGR of 9%/10%/10% for MRF over FY20-FY23 (excludes DTA benefit of ~Rs 4bn in FY20). We have not baked in any additional demand from the proposed scrappage policy or from revival in the CV segment. Despite healthy growth visibility, The stock currently trades at 20.7x/19.3x FY22E/FY23E EPS and upsides look capped. We thus initiate coverage with ADD, assigning the stock a 22x Sep'22 EPS to arrive at our target price of Rs 67,000 for Sep'21.

FIG 15 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

- Slower recovery in OE demand may adversely impact sales.
- A spike in prices of natural rubber or crude derivatives could hurt margins.

Annexure A: Company profile

Headquartered in Chennai, MRF is an Indian multinational that is the largest manufacturer of tyres in India and the fourteenth largest in the world. The company manufactures rubber products including tyres, treads, tubes and conveyor belts, paints and toys. MRF also runs the MRF Pace Foundation, Chennai and MRF Challenge in motorsport. Employee strength as on Mar'19 totalled over 16,500.

FIG 1 – A BIRD'S EYE VIEW ON CORPORATE GOVERNANCE

Name	Designation	Total Remuneration (Rs mn)	No. of board meetings attended	Attended last AGM	Committees (Y/N)/ No of meetings attended				
					1- Audit	2- Nomination & remuneration	3- Stakeholders relationship	4- Risk Management	5- CSR
Mr K M Mammen	Chairman & MD	275.1	4	Y		Y/3	Y/1	Y/3	Y/NA
Mr Arun Mammen	Vice Chairman & MD	222.8	4	Y				Y/3	Y/NA
Mr Rahul Mammen	Executive director	193.6	4	Y				Y/3	Y/NA
Mr Samir Thariyan Mappillai	Executive director	34.2	4	Y					
Mr Varun Mammen	Executive director	34.0	4	Y					
Mr Ashok Jacob	Independent director	0.02	1	N					
Mr V Shridhar	Independent director	0.02	4	Y	Y/4	Y/3	Y/1		
Mr Vijay Kirloskar	Independent director	0.02	1	N					
Mr N Kumar	Independent director	0.08	4	Y					
Mr Ranjit J Jesudasan	Independent director	0.24	4	Y	Y/4	Y/3	Y/1		Y/NA
Dr Salim Joseph	Independent director	0.06	3	Y					
Mr Jacob Kurian	Independent director	0.15	3	Y	Y/3	Y/3			
Mr M Meyyappan	Independent director	0.04	2	N					
Dr Cibi Mammen	Non-executive director	0.08	4	Y					
Mrs Ambika Mammen	Non-executive director	0.08	4	Y					
Mrs Vimla Abraham	Independent director	0.02	1	NA					

Source: Company, BOBCAPS Research

FIG 2 – AUDITORS, BANKERS, CREDIT RATING AND CSR DETAILS

Auditors	M/s SCA and associates	M/s Mahesh, Virender & Sriram
Cost Auditors	Mr C Govindan Kutty	
Bankers	NA	
Credit rating		
Detail of debt	Rating	Rating agency
Long term rating	AAA	CARE
Short term rating	A1+	CARE
Fixed deposit	AAA	CARE
Non-convertible debenture	AAA	ICRA & CARE
CSR - For FY19		
Prescribed CSR (Rs mn)	427.3	
CSR expensed (Rs mn)	263.5	

Source: Company, BOBCAPS Research

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue	158,370	159,911	154,695	188,628	208,497
EBITDA	22,504	23,237	22,502	27,909	31,218
Depreciation	8,063	9,806	11,420	13,545	15,882
EBIT	18,616	16,736	14,721	18,217	19,314
Net interest income/(expenses)	(2,528)	(2,743)	(1,532)	(1,532)	(1,382)
Other income/(expenses)	4,175	3,305	3,638	3,852	3,978
Exceptional items	(1,356)	0	0	0	0
EBT	14,733	13,993	13,189	16,685	17,932
Income taxes	5,120	43	3,324	4,205	4,519
Extraordinary items	0	0	0	0	0
Min. int./Inc. from associates	0	0	0	0	0
Reported net profit	9,613	13,950	9,866	12,481	13,413
Adjustments	1,356	0	0	0	0
Adjusted net profit	10,969	13,950	9,866	12,481	13,413

Balance Sheet

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Accounts payables	23,276	23,401	23,737	31,448	29,764
Other current liabilities	21,389	24,404	23,852	36,054	34,057
Provisions	1,571	3,422	3,422	3,422	3,422
Debt funds	18,675	10,210	10,210	10,210	8,210
Other liabilities	2,441	5,781	5,781	5,781	5,781
Equity capital	42	42	42	42	42
Reserves & surplus	106,491	120,001	129,797	141,983	155,080
Shareholders' fund	106,533	120,044	129,839	142,026	155,122
Total liabilities and equities	173,885	187,263	196,843	228,941	236,357
Cash and cash eq.	601	11,069	4,055	3,061	3,278
Accounts receivables	23,616	22,570	24,751	32,067	31,275
Inventories	29,509	28,527	29,392	39,612	37,530
Other current assets	1,775	151	464	566	521
Investments	38,484	15,402	21,402	21,402	23,402
Net fixed assets	67,675	88,492	97,072	113,527	122,645
CWIP	14,032	17,346	16,000	15,000	14,000
Intangible assets	0	0	0	0	0
Deferred tax assets, net	(8,392)	(4,278)	(4,278)	(4,278)	(4,278)
Other assets	6,585	7,985	7,985	7,985	7,985
Total assets	173,885	187,263	196,843	228,941	236,357

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Net income + Depreciation	17,676	23,756	21,285	26,025	29,295
Interest expenses	2,528	2,743	1,532	1,532	(1,382)
Non-cash adjustments	(4,175)	(3,305)	(3,638)	(3,852)	(3,978)
Changes in working capital	(7,962)	10,584	(3,575)	2,275	(762)
Other operating cash flows	1,356	0	0	0	0
Cash flow from operations	9,422	33,778	15,603	25,980	23,174
Capital expenditures	(18,228)	(33,937)	(18,654)	(29,000)	(24,000)
Change in investments	2,980	23,082	(6,000)	0	(2,000)
Other investing cash flows	4,175	3,305	3,638	3,852	3,978
Cash flow from investing	(11,073)	(7,549)	(21,016)	(25,148)	(22,022)
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	1,669	(8,465)	0	0	(2,000)
Interest expenses	(2,528)	(2,743)	(1,532)	(1,532)	(1,382)
Dividends paid	0	(509)	(70)	(294)	(316)
Other financing cash flows	1,724	(4,044)	0	0	0
Cash flow from financing	866	(15,761)	(1,601)	(1,826)	(3,698)
Changes in cash and cash eq.	(786)	10,468	(7,014)	(994)	(2,546)
Closing cash and cash eq.	601	11,069	4,055	3,061	3,278

Per Share

Y/E 31 Mar (Rs)	FY19A	FY20A	FY21E	FY22E	FY23E
Reported EPS	2,587.0	3,290.0	2,326.8	2,943.5	3,163.5
Adjusted EPS	2,587.0	3,290.0	2,326.8	2,943.5	3,163.5
Dividend per share	0.0	100.0	16.5	69.4	74.6
Book value per share	25,125.7	28,312.1	30,622.5	33,496.6	36,585.5

Valuations Ratios

Y/E 31 Mar (x)	FY19A	FY20A	FY21E	FY22E	FY23E
EV/Sales	1.7	1.7	1.7	1.4	1.3
EV/EBITDA	12.1	11.7	11.8	9.3	8.4
Adjusted P/E	23.6	18.5	26.2	20.7	19.3
P/BV	2.4	2.2	2.0	1.8	1.7

DuPont Analysis

Y/E 31 Mar (%)	FY19A	FY20A	FY21E	FY22E	FY23E
Tax burden (Net profit/PBT)	74.4	99.7	74.8	74.8	74.8
Interest burden (PBT/EBIT)	79.1	83.6	89.6	91.6	92.8
EBIT margin (EBIT/Revenue)	11.8	10.5	9.5	9.7	9.3
Asset turnover (Revenue/Avg TA)	130.5	121.3	109.8	124.2	127.5
Leverage (Avg TA/Avg Equity)	1.2	1.2	1.1	1.1	1.1
Adjusted ROAE	10.8	12.3	7.9	9.2	9.0

Source: Company, BOBCAPS Research | Note: TA = Total Assets

Ratio Analysis

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
YoY growth (%)					
Revenue	7.2	1.0	(3.3)	21.9	10.5
EBITDA	1.0	3.3	(3.2)	24.0	11.9
Adjusted EPS	0.4	27.2	(29.3)	26.5	7.5
Profitability & Return ratios (%)					
EBITDA margin	14.2	14.5	14.5	14.8	15.0
EBIT margin	11.8	10.5	9.5	9.7	9.3
Adjusted profit margin	6.9	8.7	6.4	6.6	6.4
Adjusted ROAE	10.3	11.6	7.6	8.8	8.6
ROCE	9.4	12.0	7.5	8.7	8.6
Working capital days (days)					
Receivables	52	53	56	55	55
Inventory	59	66	68	67	68
Payables	76	90	94	90	90
Ratios (x)					
Gross asset turnover	0.6	0.8	0.9	0.9	1.0
Current ratio	1.2	1.2	1.1	1.1	1.1
Net interest coverage ratio	7.4	6.1	9.6	11.9	14.0
Adjusted debt/equity	0.2	0.1	0.1	0.1	0.1

Source: Company, BOBCAPS Research

BUY

TP: Rs 1,780 | ▲ 26%

TVS SRICHAKRA

| Auto Components

| 05 August 2020

Top play in 2W tyre segment; initiate with BUY

TVS Srichakra (TVSS) is among the top three manufacturers of two-wheeler and three-wheeler tyres in India, commanding ~31% market share. Having aggressively penetrated the OEM segment, the company now intends to focus on improving its footprint in the aftermarket through an elaborate brand building exercise. We expect these efforts to aid an earnings CAGR of 19% over FY20-FY23. Valuing the stock at 14x Sep'22 EPS, we arrive at a TP of Rs 1,780. Initiate with BUY.

Mayur Milak | Nishant Chowhan, CFA
 research@bobcaps.in

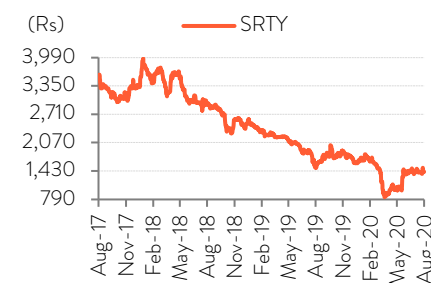
Market leader in OEM sales: TVSS is the largest supplier of two-wheeler tyres to most leading domestic 2W OEMs, with a ~31% market share in the segment. The company's share of business has improved with most OEMs due to its timely turnaround capabilities and consistent performance. With rural India showing signs of a strong recovery, we anticipate a ~6% CAGR in 2W OEM volumes over FY20-FY23.

Ticker/Price	SRTY IN/Rs 1,410
Market cap	US\$ 142.6mn
Shares o/s	8mn
3M ADV	US\$ 0.4mn
52wk high/low	Rs 1,550/Rs 1,350
Promoter/FPI/DII	45%/1%/6%

Source: NSE

Focus on brand building to reap aftermarket benefits: The company manufactures and markets its products under the 'TVS Tyres' and 'Eurogrip' brands. It was the first to introduce radial 2W tyres in the aftermarket segment. Management's strategy to target aftermarket sales will not only improve overall margins but also ensure steady growth going forward. We expect EBITDA margins to expand 150bps over our forecast period to ~12% in FY23.

STOCK PERFORMANCE



Source: NSE

Initiate with BUY: We estimate a revenue CAGR of 6% over FY20-FY23, with stronger margins aiding a higher EBITDA/PAT CAGR of 12%/19%. Net D/E stands at 0.4x and we expect the company to deliver ROE/ROCE of 11.1%/9.4% by FY23-end. We value the stock at 14x Sep'22 EPS – at par with its peers to arrive at a TP of Rs 1,780. Initiate with a BUY.

KEY FINANCIALS

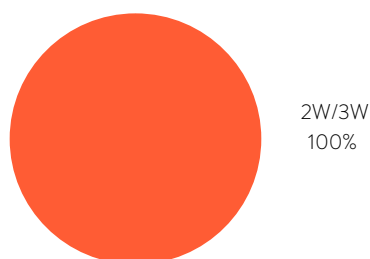
Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue (Rs mn)	23,818	20,522	18,704	22,417	24,694
EBITDA (Rs mn)	2,592	2,139	2,070	2,660	2,965
Adj. net profit (Rs mn)	1,032	844	559	917	1,031
Adj. EPS (Rs)	134.7	110.2	72.9	119.7	134.6
Adj. EPS growth (%)	(12.3)	(18.2)	(33.8)	64.1	12.4
Adj. ROAE (%)	13.9	11.1	6.9	10.3	10.6
Adj. P/E (x)	10.5	12.8	19.3	11.8	10.5
EV/EBITDA (x)	5.3	6.6	6.9	5.2	4.6

Source: Company, BOBCAPS Research

Investment summary

FIG 1 – TVSS IS A PURE PLAY 2W/3W TYRE COMPANY...

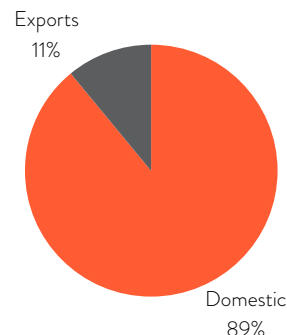
Revenue mix by segment



Source: Company, BOBCAPS Research

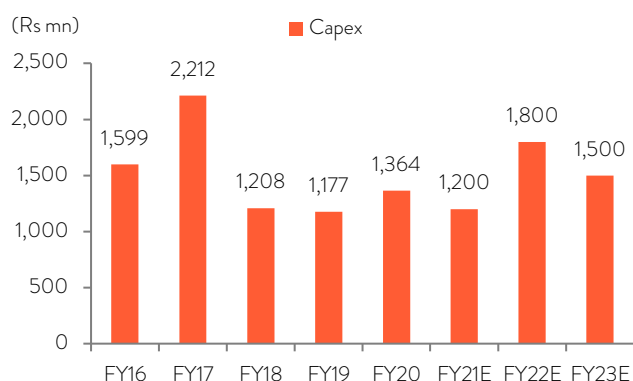
FIG 2 – ...WITH A FOCUS ON THE DOMESTIC MARKET

Revenue mix by market



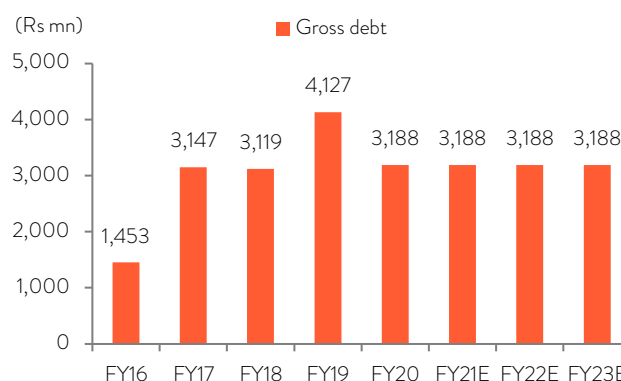
Source: Company, BOBCAPS Research

FIG 3 – STEADY CAPEX – IN LINE WITH INDUSTRY DEMAND



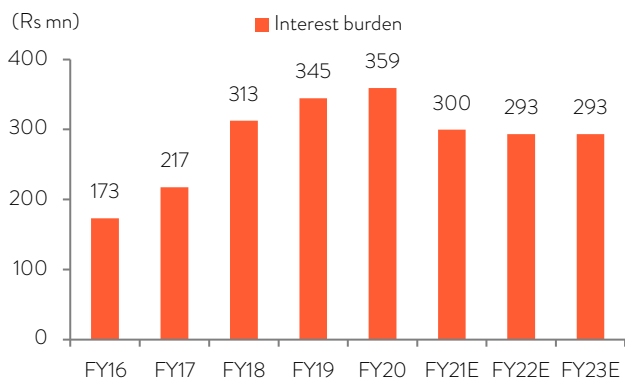
Source: Company, BOBCAPS Research

FIG 4 – GROSS DEBT PARED IN FY20 DUE TO EFFICIENT WORKING CAPITAL MANAGEMENT



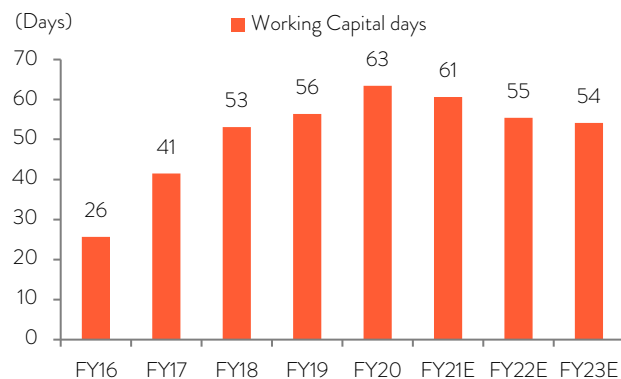
Source: Company, BOBCAPS Research

FIG 5 – INTEREST BURDEN CONTROLLED IN A SLOWDOWN SCENARIO



Source: Company, BOBCAPS Research

FIG 6 – WORKING CAPITAL HAS BEEN ON A RISE..WE EXPECT SIGNIFICANT CORRECTION IN THE SAME DURING FY20-23



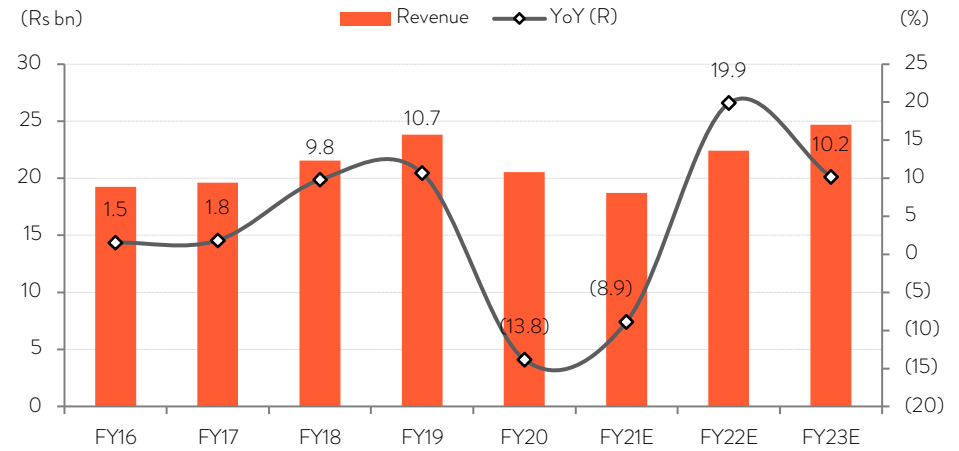
Source: Company, BOBCAPS Research

Financial review

FIG 7 – REVENUE EXPECTED TO REGISTER 6% CAGR DURING FY20-FY23E

OEM and replacement demand split 50:50 in 2W/3W tyre sector

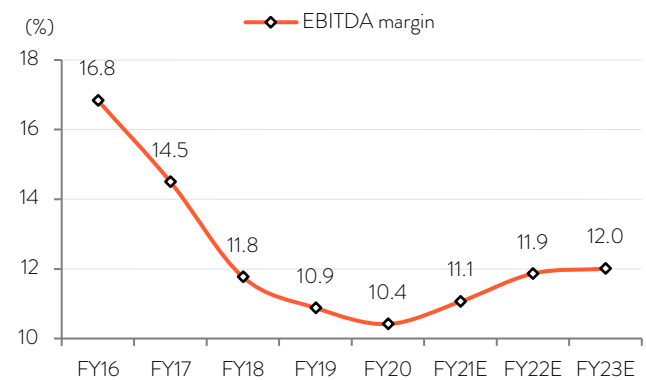
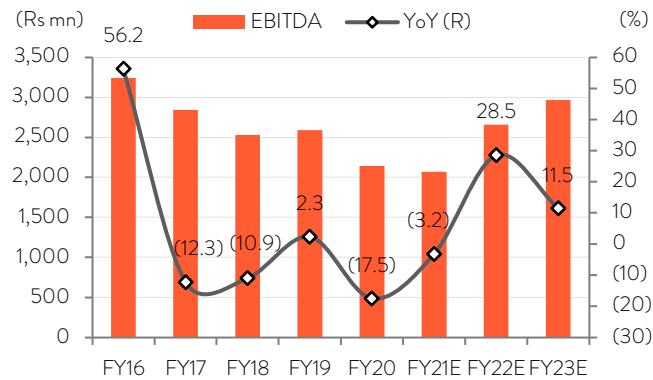
We expect an overall volume CAGR of 6% for TVSS through to FY23



Source: Company, BOBCAPS Research

FIG 8 – EBITDA TO LOG SMART 12% CAGR

FIG 9 – EBITDA MARGIN IMPROVING ON LOWER RM COSTS AND OPERATING EFFICIENCIES

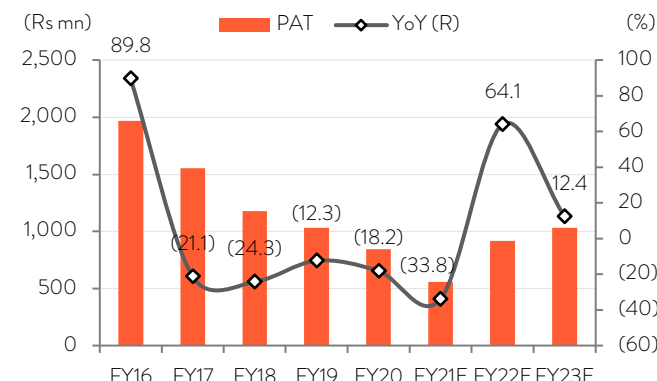
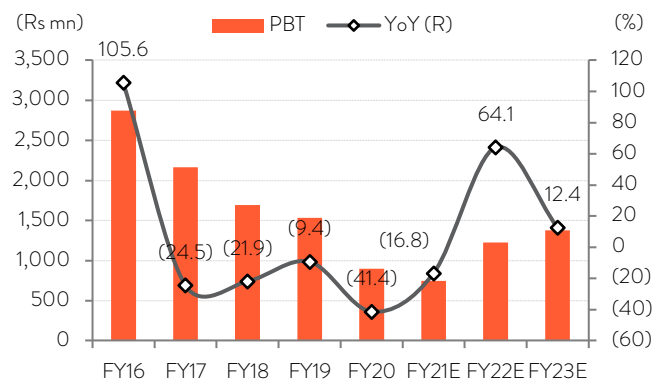


Source: Company, BOBCAPS Research

Source: Company, BOBCAPS Research

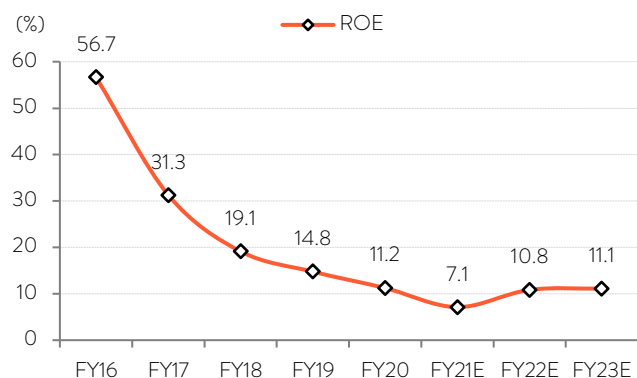
FIG 10 – PBT TO RISE WITH OVERALL RECOVERY IN DEMAND AND BETTER MARGIN PERFORMANCE

FIG 11 – EXPECT 19% PAT CAGR DURING FY20-FY23E

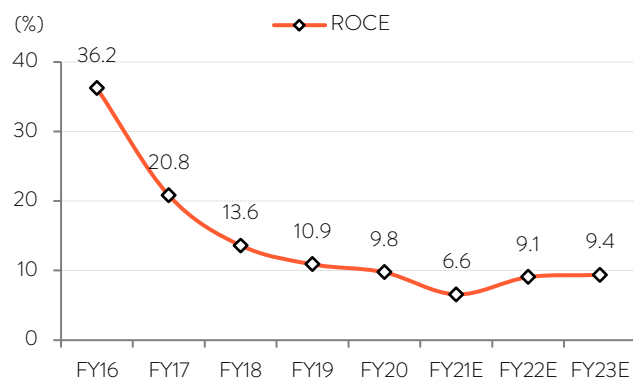


Source: Company, BOBCAPS Research

Source: Company, BOBCAPS Research

FIG 12 – RECOVERY IN ROE BY FY23E-END

Source: Company, BOBCAPS Research

FIG 13 – ROCE TO IMPROVE SIMULTANEOUSLY

Source: Company, BOBCAPS Research

FIG 14 – QUARTERLY PERFORMANCE

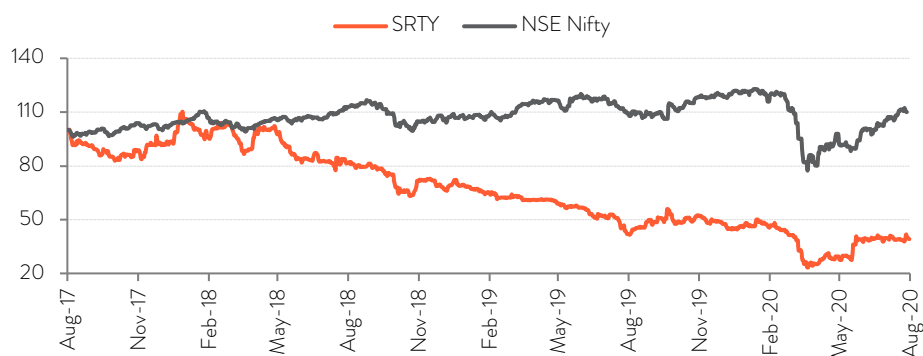
(Rs mn)	Q1FY19	Q2FY19	Q3FY19	Q4FY19	Q1FY20	Q2FY20	Q3FY20	Q4FY20
Net sales	5,878	6,318	5,823	5,799	5,925	5,451	4,975	4,171
YoY (%)	9.0	11.3	18.2	4.9	0.8	(13.7)	(14.6)	(28.1)
QoQ (%)	6.3	7.5	(7.8)	(0.4)	2.2	(8.0)	(8.7)	(16.2)
(Inc)/dec in stock-in-trade	157	(23)	(566)	(232)	237	(118)	(153)	(78)
Materials	3,454	3,980	4,035	3,672	3,354	3,248	2,836	2,431
% of sales	61.4	62.6	59.6	59.3	60.6	57.4	53.9	56.4
YoY (%)	7.9	18.1	23.8	7.5	(0.6)	(20.9)	(22.7)	(31.6)
QoQ (%)	12.8	9.6	(12.3)	(0.8)	4.4	(12.8)	(14.3)	(12.3)
Staff cost	645	721	666	703	722	724	710	667
% of sales	11.0	11.4	11.4	12.1	12.2	13.3	14.3	16.0
YoY (%)	7.7	17.5	11.9	5.5	11.9	0.4	6.6	(5.1)
QoQ (%)	(3.2)	11.8	(7.7)	5.6	2.7	0.3	(2.0)	(6.0)
Other expenditure	876	985	1,061	1,092	888	992	1,102	823
% of sales	14.9	15.6	18.2	18.8	15.0	18.2	22.1	19.7
YoY (%)	(11.4)	7.9	22.5	2.7	1.3	0.8	3.9	(24.6)
QoQ (%)	(17.6)	12.4	7.8	2.9	(18.7)	11.8	11.0	(25.3)
Total expenses	5,132	5,663	5,196	5,235	5,199	4,847	4,494	3,844
EBITDA	746	655	627	564	725	604	481	328
YoY (%)	62.6	(17.8)	(5.4)	(5.9)	(2.8)	(7.7)	(23.2)	(41.9)
QoQ (%)	24.5	(12.3)	(4.2)	(10.0)	28.6	(16.7)	(20.4)	(31.9)
OPM (%)	12.7	10.4	10.8	9.7	12.2	11.1	9.7	7.9
Other income	7	47	(15)	75	7	16	32	40
Interest	70	60	108	107	109	84	80	86
Depreciation	199	202	207	221	220	226	227	305
Profit before tax	485	440	297	311	403	311	207	(23)
YoY (%)	95.7	(22.5)	(32.0)	(29.4)	(16.8)	(29.4)	(30.4)	(107.5)
Provision for taxation	145	145	61	150	141	108	73	(268)
Tax Rate (%)	29.9	32.8	20.5	48.4	34.9	34.8	35.2	1,156.5
Profit after tax	340	296	236	160	262	203	134	245
YoY (%)	90.5	(26.3)	(23.8)	(44.1)	(22.8)	(31.5)	(43.2)	52.8
QoQ (%)	18.5	(13.0)	(20.2)	(32.0)	63.7	(22.8)	(33.9)	82.9
PAT Margin	5.8	4.7	4.1	2.8	4.4	3.7	2.7	5.9

Source: Company, BOBCAPS Research

Valuation methodology

We estimate a revenue CAGR of 6% over FY20-FY23, with stronger margins aiding a higher EBITDA/PAT CAGR of 12%/19%. Net D/E stands at 0.4x and we expect the company to deliver ROE/ROCE of 11.1%/9.4% by FY23-end. We value the stock at 14x Sep'22 EPS – at par with its peers to arrive at a TP of Rs 1,780 for Sep'21. Initiate with a BUY.

FIG 15 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

- Below-expected recovery in both replacement and OEM channels can lead to lower volumes, posing downside risk to our estimates.
- A surge in raw material prices could dent margins and earnings.

Annexure A: Company profile

TVSS is part of the TVS Group, one of India's leading auto ancillary groups. The company has state-of-the-art manufacturing units at Madurai (Tamil Nadu) and Rudrapur (Uttarakhand), sprawling over 290,000sq mtr. It manufactures 2W, 3W and other industrial tyres, and is a major OEM supplier not just to TVS Motor, but to most leading brands. Domestic aftermarket supply is backed by a network of over 2,400 dealers and 34 depots. TVSS exports to over 70 countries and has a presence in the US, Europe, South America, Africa and Australia.

FIG 1 – A BIRD'S EYE VIEW ON CORPORATE GOVERNANCE

Name	Designation	Total Remuneration (Rs mn)	No. of board meetings attended	Attended last AGM	Committees (Y/N)/ No of meetings attended			
					1- Audit	2- Nomination & remuneration	3- Stakeholders relationship	4- CSR
Mr R Naresh	Executive Vice Chairman	65.8	7	Yes				
Mrs Shobhana Ramachandran	Managing Director	67.8	7	Yes			Y/2	Y/3
Mr M S Viraraghavan	Non-executive, Independent	1.7	7	Yes	Y/7	Y/2		
Mr P Vijayaraghavan	Non-executive, Independent	1.8	7	Yes	Y/7	Y/2	Y/2	Y/3
Mr H Janardhan Iyer	Non-executive, Independent	1.7	7	Yes	Y/7	Y/2		
Mr V Ramakrishnan	Non-executive, Independent	1.1	7	Yes			Y/2	
Mr Rashesh R Doshi	Non-executive, Independent	1.7	7	Yes	Y/7			Y/3
Mr V Anantha Nageswaran	Non-executive, Independent	0.4	5	Yes				
Mr A Arumugam	Non-executive, Independent	0.8	1	NA				

Source: Company, BOBCAPS Research

FIG 2 – AUDITORS, BANKERS, CREDIT RATING AND CSR DETAILS

Auditors	PKF Sridhar & Santhanam LLP
Cost Auditors	Dr I Ashok
Bankers	State Bank of India HDFC Bank
CSR	
Prescribed CSR (Rs mn)	43.8
CSR expensed (Rs mn)	44.3

Source: Company, BOBCAPS Research

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue	23,818	20,522	18,704	22,417	24,694
EBITDA	2,592	2,139	2,070	2,660	2,965
Depreciation	828	977	1,103	1,260	1,434
EBIT	1,878	1,257	1,047	1,519	1,672
Net interest income/(expenses)	(345)	(359)	(300)	(293)	(293)
Other income/(expenses)	114	95	80	120	140
Exceptional items	0	0	0	0	0
EBT	1,533	898	747	1,226	1,378
Income taxes	501	54	188	309	347
Extraordinary items	0	0	0	0	0
Min. int./Inc. from associates	0	0	0	0	0
Reported net profit	1,032	844	559	917	1,031
Adjustments	0	0	0	0	0
Adjusted net profit	1,032	844	559	917	1,031

Balance Sheet

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Accounts payables	3,526	2,113	2,741	2,758	3,099
Other current liabilities	1,336	1,840	1,452	2,085	2,122
Provisions	40	137	137	137	137
Debt funds	4,127	3,188	3,188	3,188	3,188
Other liabilities	988	867	867	867	867
Equity capital	77	77	77	77	77
Reserves & surplus	7,355	7,543	8,009	8,787	9,651
Shareholders' fund	7,432	7,620	8,086	8,864	9,728
Total liabilities and equities	17,448	15,765	16,470	17,899	19,141
Cash and cash eq.	165	111	221	215	366
Accounts receivables	3,236	1,970	2,511	2,887	2,977
Inventories	4,888	4,105	3,997	4,606	4,871
Other current assets	753	903	820	860	880
Investments	1,069	1,091	1,291	1,191	1,791
Net fixed assets	6,222	6,467	6,564	7,103	7,170
CWIP	339	482	430	400	450
Intangible assets	0	0	0	0	0
Deferred tax assets, net	(555)	(330)	(330)	(330)	(330)
Other assets	1,332	967	967	967	967
Total assets	17,448	15,765	16,470	17,899	19,141

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Net income + Depreciation	1,860	1,821	1,662	2,177	2,465
Interest expenses	345	359	300	293	(293)
Non-cash adjustments	(114)	(95)	(80)	(120)	(140)
Changes in working capital	(1,270)	1,332	(111)	(374)	3
Other operating cash flows	(93)	0	0	0	0
Cash flow from operations	727	3,418	1,770	1,976	2,034
Capital expenditures	(1,177)	(1,364)	(1,148)	(1,770)	(1,550)
Change in investments	(390)	(22)	(200)	100	(600)
Other investing cash flows	114	95	80	120	140
Cash flow from investing	(1,452)	(1,291)	(1,268)	(1,550)	(2,010)
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	1,008	(939)	0	0	0
Interest expenses	(345)	(359)	(300)	(293)	(293)
Dividends paid	(306)	(185)	(93)	(139)	(167)
Other financing cash flows	379	(696)	0	0	0
Cash flow from financing	735	(2,180)	(392)	(432)	(460)
Changes in cash and cash eq.	10	(53)	110	(6)	(436)
Closing cash and cash eq.	165	111	221	215	366

Per Share

Y/E 31 Mar (Rs)	FY19A	FY20A	FY21E	FY22E	FY23E
Reported EPS	134.7	110.2	72.9	119.7	134.6
Adjusted EPS	134.7	110.2	72.9	119.7	134.6
Dividend per share	40.0	24.2	12.1	18.1	21.8
Book value per share	970.2	994.8	1,055.6	1,157.2	1,270.0

Valuations Ratios

Y/E 31 Mar (x)	FY19A	FY20A	FY21E	FY22E	FY23E
EV/Sales	0.6	0.7	0.8	0.6	0.6
EV/EBITDA	5.3	6.6	6.9	5.2	4.6
Adjusted P/E	10.5	12.8	19.3	11.8	10.5
P/BV	1.5	1.4	1.3	1.2	1.1

DuPont Analysis

Y/E 31 Mar (%)	FY19A	FY20A	FY21E	FY22E	FY23E
Tax burden (Net profit/PBT)	67.3	94.0	74.8	74.8	74.8
Interest burden (PBT/EBIT)	81.6	71.4	71.4	80.7	82.5
EBIT margin (EBIT/Revenue)	7.9	6.1	5.6	6.8	6.8
Asset turnover (Revenue/Avg TA)	205.4	169.5	157.1	178.9	185.0
Leverage (Avg TA/Avg Equity)	1.7	1.6	1.5	1.5	1.4
Adjusted ROAE	14.8	11.2	7.1	10.8	11.1

Source: Company, BOBCAPS Research | Note: TA = Total Assets

Ratio Analysis

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
YoY growth (%)					
Revenue	10.7	(13.8)	(8.9)	19.9	10.2
EBITDA	2.3	(17.5)	(3.2)	28.5	11.5
Adjusted EPS	(12.3)	(18.2)	(33.8)	64.1	12.4
Profitability & Return ratios (%)					
EBITDA margin	10.9	10.4	11.1	11.9	12.0
EBIT margin	7.9	6.1	5.6	6.8	6.8
Adjusted profit margin	4.3	4.1	3.0	4.1	4.2
Adjusted ROAE	13.9	11.1	6.9	10.3	10.6
ROCE	10.9	9.8	6.6	9.1	9.4
Working capital days (days)					
Receivables	43	46	44	44	43
Inventory	63	80	79	70	70
Payables	69	88	85	79	77
Ratios (x)					
Gross asset turnover	0.4	0.5	0.6	0.6	0.6
Current ratio	1.8	1.7	1.7	1.7	1.7
Net interest coverage ratio	5.4	3.5	3.5	5.2	5.7
Adjusted debt/equity	0.6	0.4	0.4	0.4	0.3

Source: Company, BOBCAPS Research

Disclaimer

Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

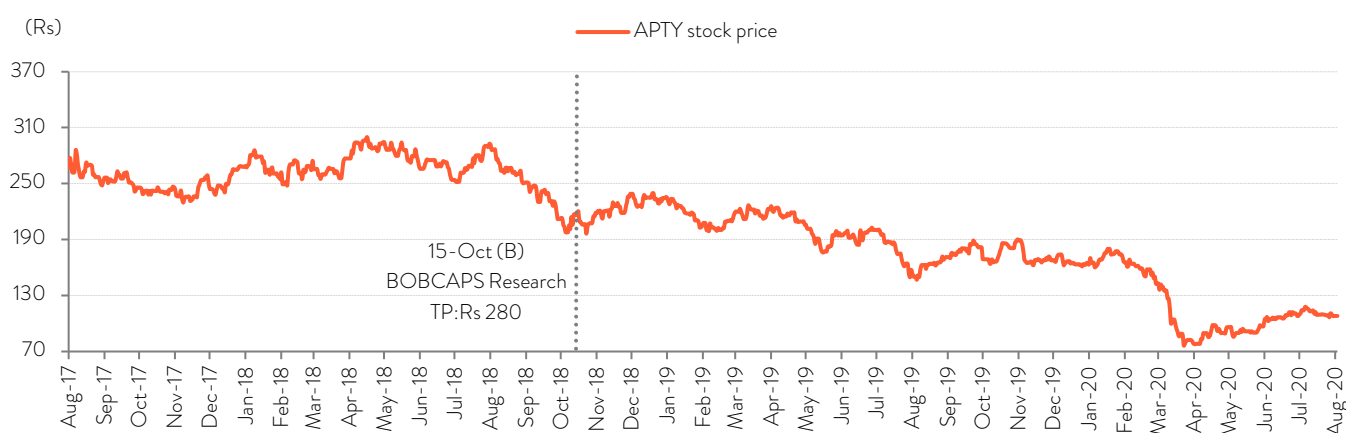
ADD – Expected return from >+5% to +15%

REDUCE – Expected return from -5% to +5%

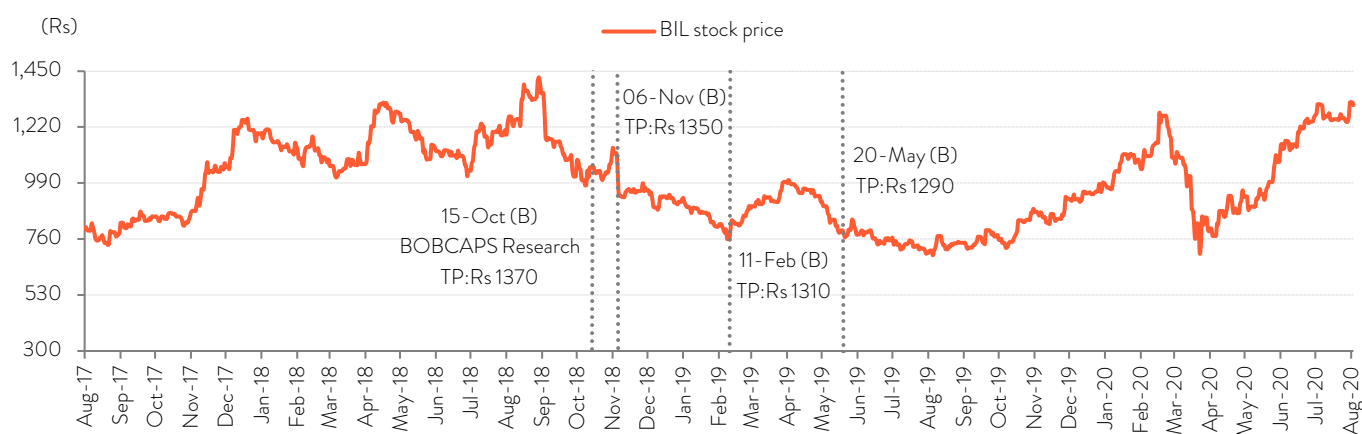
SELL – Expected return <-5%

Note: Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

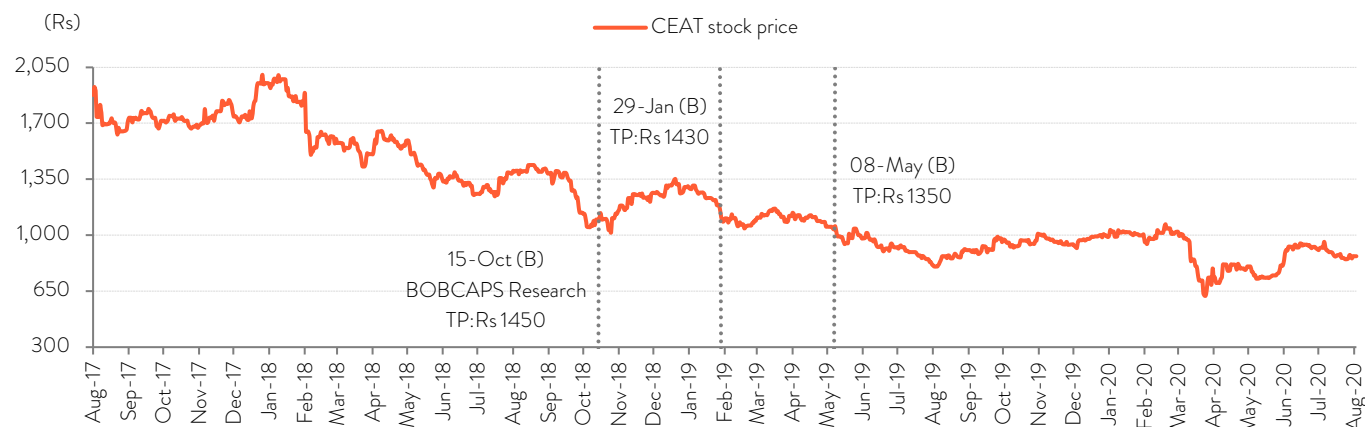
RATINGS AND TARGET PRICE (3-YEAR HISTORY): APOLLO TYRES (APTY IN)



RATINGS AND TARGET PRICE (3-YEAR HISTORY): BALKRISHNA INDUSTRIES (BIL IN)



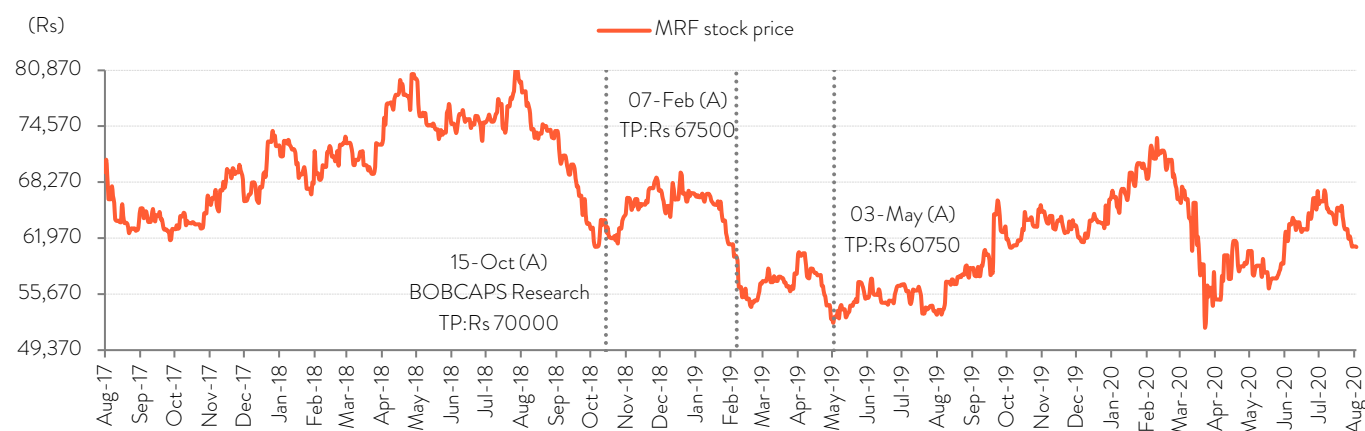
RATINGS AND TARGET PRICE (3-YEAR HISTORY): CEAT (CEAT IN)



RATINGS AND TARGET PRICE (3-YEAR HISTORY): JK TYRE & INDUSTRIES (JKI IN)



RATINGS AND TARGET PRICE (3-YEAR HISTORY): MRF (MRF IN)



RATINGS AND TARGET PRICE (3-YEAR HISTORY): TVS SRICHAKRA (SRTY IN)


B – Buy, A – Add, R – Reduce, S – Sell

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