

SELL

TP: Rs 90 | ▼ 44%

JK TYRE & INDUSTRIES

Auto Components

06 August 2021

Weak Q1; maintain SELL

- Q1 revenue in line but gross margin fell short of our estimate, denting operating performance. Adj. PAT a miss at Rs 567mn
- We continue to expect a 300bps YoY gross margin hit in FY22 and FY23. Despite deleveraging efforts, balance sheet concerns persist
- TP maintained at Rs 90 based on a 60% discount to peers to account for high leverage; reiterate SELL

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Operating performance disappoints: At Rs 26.1bn (-11% QoQ), JKI's Q1FY22 revenue was in line with our estimate, but EBITDA margin came in 160bps lower at 10.7% led by a below-estimated gross margin. EBITDA declined 39% QoQ to Rs 2.8bn and an above-expected tax rate (at 41%) further pulled down adj. PAT to Rs 567mn (Rs 1bn est.).

High commodity prices to depress margins: Given the 12% QoQ cost increase in the raw material basket during both Q4FY21 and Q1FY21 (per management), along with the inability of tyre companies to fully pass on the burden, we anticipate gross margin deterioration across the sector in FY22. We model for a decline of ~300bps in JKI's FY22 gross margin over FY21 levels, eroding its operating margin.

Balance sheet concerns persist: JKI's leverage remains high at 1.5x D/E, which is ~4x the industry average. Though improved working capital management aided a reduction of Rs 9.3bn in net debt to Rs 45bn in FY21 along with a 15% decline in interest cost, we expect overall debt reduction of only Rs 1bn in FY22, much lower than the Rs 6bn cut targeted by management.

Maintain SELL: We maintain our revenue and earnings estimates for FY22/FY23 and introduce forecasts for FY24. Our revenue/EBITDA/adj. PAT CAGR projections stand at +11%/+1%/+8% over FY21-FY24, with FY22/FY23 EPS estimates at Rs 8/Rs 13. Given gross margin weakness and persisting balance sheet concerns, we continue to value the stock at a steep ~60% discount to peers – i.e. at 7x FY23E EPS, in line with JKI's 10-year mean. We maintain our Mar'22 TP of Rs 90 and reiterate SELL.

Key changes

Target	Rating
◀ ▶	◀ ▶

Ticker/Price	JKI IN/Rs 161
Market cap	US\$ 534.4mn
Free float	44%
3M ADV	US\$ 5.9mn
52wk high/low	Rs 166/Rs 55
Promoter/FPI/DII	56%/3%/1%

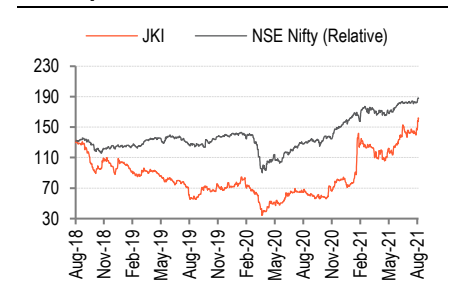
Source: NSE | Price as of 6 Aug 2021

Key financials

Y/E 31 Mar	FY21A	FY22E	FY23E
Total revenue (Rs mn)	91,022	104,021	115,831
EBITDA (Rs mn)	13,064	10,678	12,133
Adj. net profit (Rs mn)	2,819	1,960	3,070
Adj. EPS (Rs)	11.4	8.0	12.5
Consensus EPS (Rs)	11.4	12.7	19.1
Adj. ROAE (%)	10.1	6.6	9.5
Adj. P/E (x)	14.1	20.2	12.9
EV/EBITDA (x)	7.1	7.8	6.4
Adj. EPS growth (%)	9.8	(30.5)	56.6

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE



Fig 1 – Quarterly performance – Consolidated

(Rs mn)	Q1FY22	Q1FY21	YoY (%)	Q4FY21	QoQ (%)	FY21	FY20	YoY (%)
Net Revenues	26,084	11,308	130.7	29,273	(10.9)	91,022	87,249	4.3
Total Income (A)	26,084	11,308	130.7	29,273	(10.9)	91,022	87,249	4.3
Operating Expenses:								
Raw materials consumed	16,865	7,738	117.9	17,808	(5.3)	54,687	53,370	2.5
Employee Expenses	2,541	1,753	45.0	2,665	(4.7)	9,227	9,232	0.0
Other Expenses	3,884	1,855	109.4	4,253	(8.7)	14,044	14,772	(4.9)
Total Expenditure (B)	23,289	11,346	105.3	24,726	(5.8)	77,959	77,373	0.8
EBITDA (A-B)	2,795	(38)	(7533.5)	4,547	(38.5)	13,063	9,876	32.3
Other Income	100	73	36.0	174	(42.5)	431	284	51.7
Depreciation	962	967	(0.5)	957	0.6	3,867	3,778	2.3
EBIT	1,933	(931)	NA	3,764	(48.7)	9,627	6,381	50.9
Finance Costs	1,079	1,306	(17.3)	1,053	2.5	4,659	5,490	(15.1)
PBT before excep items	853	(2,237)	NA	2,711	(68.5)	4,969	891	457.3
Exceptional items	(106)	(329)	NA	95	(211.7)	375	(1,059)	(135.4)
PBT after excep items	747	(2,566)	NA	2,806	(73.4)	5,344	(168)	(3290.1)
Tax expense	308	(544)	NA	845	(63.6)	2,009	(1,658)	(221.2)
Share of Associates	22	(20)	NA	(11)	-	(25)	(77)	(67.4)
Reported PAT	461	(2,042)	NA	1,950	(76.3)	3,309	1,413	134.2
Adjusted PAT	567	(1,713)	NA	1,855	(69.4)	2,935	2,819	18.7
EPS (Rs)	2.5	(7.6)	NA	7.9	(68.3)	11.4	10.9	16.3

Source: Company, BOBCAPS Research

Fig 2 – Key parameters

(%)	Q1FY22	Q1FY21	YoY (bps)	Q4FY21	QoQ (bps)	FY21	FY20	YoY (bps)
Gross Margin	35.3	31.6	378	39.2	(382)	39.9	38.8	109
EBITDA Margin	10.7	(0.3)	1,105	15.5	(482)	14.4	11.3	303
EBIT Margin	7.4	(8.2)	1,564	12.9	(545)	10.6	7.3	326
PBT Margin	3.3	(19.8)	2,305	9.3	(599)	5.5	1.0	444
Tax Rate	41.2	21.2	1,996	30.1	1,104	37.6	NA	NA
Adj PAT Margin	2.2	(15.1)	1,732	6.3	(416)	3.2	2.8	39

Source: Company, BOBCAPS Research

Valuation methodology

We maintain our revenue and earnings estimates for FY22/FY23 and introduce forecasts for FY24. Our revenue/EBITDA/adj. PAT CAGR projections stand at +11%/+1%/+8% over FY21-FY24, with FY22/FY23 EPS estimates at Rs 8/Rs 13.

Apart from gross margin weakness due to rising input costs and lagging price hikes, JKI's leverage remains a concern at 1.5x D/E, which is ~4x the industry average. Though improved working capital management aided a reduction of Rs 9.3bn in net debt to Rs 45bn in FY21 along with a 15% decline in interest cost, we expect overall debt reduction of only Rs 1bn in FY22, much lower than the Rs 6bn cut targeted by management.

Given profitability and balance sheet concerns, we continue to value the stock at a steep ~60% discount to peers – i.e. at 7x FY23E EPS, in line with JKI's 10-year mean. We maintain our Mar'22 TP of Rs 90 and reiterate SELL.

Fig 3 – Key assumptions

(Rs mn)	FY21	FY22E	FY23E	FY24E
Revenues	91,022	104,021	115,831	126,146
EBITDA	13,064	10,678	12,133	13,203
OPM (%)	14.4	10.3	10.5	10.5
Adj. PAT	2,819	1,960	3,070	3,562
EPS (Rs)	11.4	8.0	12.5	14.5

Source: Company, BOBCAPS Research

Fig 4 – Peer comparison

Company	Ticker	Rating	Target Price (Rs)	Revenue CAGR FY21-23E (%)	EPS (Rs)		ROE (%)		Target P/E (x)
					FY22E	FY23E	FY22E	FY23E	
CEAT	CEAT IN	SELL	840	15.7	57.5	59.9	7.0	6.8	14
Apollo Tyres	APTY IN	SELL	140	11.3	7.9	9.0	4.0	4.2	16
Balkrishna Industries	BIL IN	SELL	1,550	12.4	64.8	70.3	17.9	16.8	22
MRF	MRF IN	SELL	67,000	15.9	2,769.2	3,080.1	7.7	7.9	22
TVS Srichakra	SRTY IN	SELL	1,200	15.2	78.3	85.2	6.8	7.1	14
JK Tyres	JKI IN	SELL	90	12.8	8.0	12.6	6.6	9.6	7

Source: BOBCAPS Research

Key risks

Key upside risks to our estimates are:

- faster growth in MHCV tyres which will impact our revenue forecasts,
- softening of natural rubber or crude derivative prices which will positively affect margins, and
- significant debt reduction which can improve balance sheet strength and push up valuations.

Sector recommendation snapshot

Company	Ticker	Market Cap (US\$ bn)	Price (Rs)	Target (Rs)	Rating
Apollo Tyres	APTY IN	1.7	223	140	SELL
Balkrishna Industries	BIL IN	6.4	2,449	1,550	SELL
Ceat	CEAT IN	0.7	1,342	840	SELL
Eicher Motors	EIM IN	10.1	2,747	2,200	SELL
Escorts	ESC IN	2.0	1,200	1,350	BUY
GNA Axles	GNA IN	0.1	745	540	HOLD
JK Tyre & Industries	JKI IN	0.5	161	90	SELL
Minda Corporation	MDA IN	0.4	133	140	BUY
MRF	MRF IN	4.5	79,160	67,000	SELL
Swaraj Engines	SWE IN	0.3	1,777	1,600	SELL
TVS Srichakra	SRTY IN	0.2	2,177	1,200	SELL

Source: BOBCAPS Research, NSE | Price as of 6 Aug 2021

Financials

Income Statement

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Total revenue	87,249	91,022	104,021	115,831	126,146
EBITDA	9,876	13,064	10,678	12,133	13,203
Depreciation	3,778	3,867	4,007	4,063	4,308
EBIT	6,381	9,627	6,965	8,393	9,204
Net interest inc./(exp.)	(5,490)	(4,659)	(4,165)	(4,007)	(4,115)
Other inc./(exp.)	284	431	294	323	309
Exceptional items	(1,059)	375	0	0	0
EBT	(168)	5,344	2,800	4,386	5,088
Income taxes	(1,658)	2,009	840	1,316	1,527
Extraordinary items	(95)	116	0	0	0
Min. int./Inc. from assoc.	0	0	0	0	0
Reported net profit	1,508	3,193	1,960	3,070	3,562
Adjustments	1,059	(375)	0	0	0
Adjusted net profit	2,567	2,819	1,960	3,070	3,562

Balance Sheet

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Accounts payables	16,884	15,741	17,909	20,175	21,148
Other current liabilities	10,467	14,312	16,104	16,758	16,603
Provisions	1,196	1,117	0	0	0
Debt funds	51,241	40,163	39,163	37,163	37,663
Other liabilities	6,055	7,060	7,060	7,060	7,060
Equity capital	493	493	493	493	493
Reserves & surplus	23,768	27,285	29,088	31,790	34,924
Shareholders' fund	24,261	27,777	29,580	32,282	35,417
Total liab. and equities	110,103	106,171	109,817	113,439	117,891
Cash and cash eq.	1,365	1,721	1,265	1,112	1,322
Accounts receivables	18,484	15,754	19,379	21,262	23,156
Inventories	16,178	17,893	19,949	22,214	24,192
Other current assets	6,025	6,733	7,125	7,616	8,295
Investments	1,402	1,470	1,470	1,470	1,470
Net fixed assets	63,888	62,551	61,044	59,980	59,673
CWIP	2,772	2,864	2,400	2,600	2,600
Intangible assets	0	0	0	0	0
Deferred tax assets, net	(2,030)	(3,221)	(3,221)	(3,221)	(3,221)
Other assets	2,018	405	405	405	405
Total assets	110,103	106,171	109,817	113,439	117,891

Cash Flows

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Cash flow from operations	20,288	17,196	6,607	9,099	7,944
Capital expenditures	(5,464)	(2,622)	(2,036)	(3,200)	(4,000)
Change in investments	(91)	(68)	0	0	0
Other investing cash flows	(131)	547	294	323	309
Cash flow from investing	(5,686)	(2,144)	(1,742)	(2,877)	(3,691)
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	(6,334)	(11,078)	(1,000)	(2,000)	500
Interest expenses	(5,490)	(4,659)	(4,165)	(4,007)	(4,115)
Dividends paid	(216)	(225)	(157)	(368)	(427)
Other financing cash flows	(2,892)	1,265	0	0	0
Cash flow from financing	(14,933)	(14,697)	(5,321)	(6,376)	(4,043)
Chg in cash & cash eq.	(331)	356	(456)	(153)	210
Closing cash & cash eq.	1,365	1,721	1,265	1,112	1,322

Per Share

Y/E 31 Mar (Rs)	FY20A	FY21A	FY22E	FY23E	FY24E
Reported EPS	10.4	11.4	8.0	12.5	14.5
Adjusted EPS	10.4	11.4	8.0	12.5	14.5
Dividend per share	0.7	0.9	0.6	1.5	1.7
Book value per share	94.7	108.5	115.8	126.8	139.5

Valuations Ratios

Y/E 31 Mar (x)	FY20A	FY21A	FY22E	FY23E	FY24E
EV/Sales	1.1	1.0	0.8	0.7	0.6
EV/EBITDA	9.7	7.1	7.8	6.4	5.8
Adjusted P/E	15.4	14.1	20.2	12.9	11.1
P/BV	1.7	1.5	1.4	1.3	1.2

DuPont Analysis

Y/E 31 Mar (%)	FY20A	FY21A	FY22E	FY23E	FY24E
Tax burden (Net profit/PBT)	(1530.5)	52.7	70.0	70.0	70.0
Interest burden (PBT/EBIT)	(2.6)	55.5	40.2	52.3	55.3
EBIT margin (EBIT/Revenue)	7.3	10.6	6.7	7.2	7.3
Asset turnover (Rev./Avg TA)	103.8	116.3	138.0	152.1	161.1
Leverage (Avg TA/Avg Equity)	3.6	3.1	2.7	2.5	2.4
Adjusted ROAE	11.1	11.3	7.1	10.3	10.9

Ratio Analysis

Y/E 31 Mar	FY20A	FY21A	FY22E	FY23E	FY24E
YoY growth (%)					
Revenue	(15.9)	4.3	14.3	11.4	8.9
EBITDA	(3.7)	32.3	(18.3)	13.6	8.8
Adjusted EPS	50.4	9.8	(30.5)	56.6	16.0
Profitability & Return ratios (%)					
EBITDA margin	11.3	14.4	10.3	10.5	10.5
EBIT margin	7.3	10.6	6.7	7.2	7.3
Adjusted profit margin	2.9	3.1	1.9	2.7	2.8
Adjusted ROAE	10.6	10.1	6.6	9.5	10.1
ROCE	7.6	7.7	6.5	7.7	8.2
Working capital days (days)					
Receivables	79	69	62	64	64
Inventory	69	68	66	66	67
Payables	112	109	93	94	94
Ratios (x)					
Gross asset turnover	1.1	1.1	1.0	0.9	0.9
Current ratio	1.5	1.4	1.4	1.4	1.5
Net interest coverage ratio	1.2	2.1	1.7	2.1	2.2
Adjusted debt/equity	2.2	1.5	1.4	1.2	1.1

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

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Recommendation scale: Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

HOLD – Expected return from -6% to +15%

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

Our recommendation scale does not factor in short-term stock price volatility related to market fluctuations. Thus, our recommendations may not always be strictly in line with the recommendation scale as shown above.

Ratings and Target Price (3-year history): JK TYRE & INDUSTRIES (JKI IN)



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

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