

BUY

TP: Rs 85 | ▲ 17%

JK TYRE & INDUSTRIES

Auto Components

23 October 2020

Strong Q2FY21; focus on debt reduction continues

JK Tyre (JKI) surprised positively on both revenue and earnings in Q2FY21, led by strong replacement demand and above-expected operating efficiencies. Revenue was up 6% YoY to Rs 22.7bn while operating margins expanded 180bps YoY. Through efficient working capital management, JKI also reduced debt by Rs 6bn in H1FY21. With no major capex lined up in the near term, we expect better leverage ratios going ahead. Maintain BUY with an unchanged Sep'21 TP of Rs 85, set at 7x Sep'22E EPS.

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Strong Q2FY21: At Rs 22.7bn (+6% YoY), consolidated revenue was 10% ahead of our estimate, led by strong traction in the farm and MHCV segments. Replacement volumes grew 22% YoY, ahead of overall volume growth of ~12%. Softer raw material costs and better operating efficiencies further boosted EBITDA margins to 15.6%, up 180bps YoY. Adj. PAT for Q2 declined 59% YoY to Rs 890mn due to a one-off tax reversal gain in Q2FY20.

Ticker/Price	JKI IN/Rs 73
Market cap	US\$ 243.4mn
Shares o/s	246mn
3M ADV	US\$ 1.1mn
52wk high/low	Rs 88/Rs 32
Promoter/FPI/DII	56%/3%/1%

Source: NSE

Potential rerating in sight: Despite negative earnings growth in FY20, JKI managed to reduce its net D/E to 2.1x (from 2.4x in FY19). Further, led by efficient working capital management, the company also reduced its debt by Rs 6bn in H1FY21 (overall debt reduction of Rs 12bn in the last one year). While we currently value the stock at 7x one-year forward EPS, a discount of 60% to the market leader, we see a case for rerating as leverage ratios improve.

STOCK PERFORMANCE



Source: NSE

Maintain BUY: We forecast a revenue/EBITDA/PAT CAGR of 9%/11%/13% for JKI over FY20-FY23, backed by strong replacement demand, reviving offtake from OEMs and benign raw material prices. Maintain BUY with a Sep'21 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)	10.5	7.3	20.2	6.9	5.0
EV/EBITDA (x)	7.1	7.5	7.2	5.5	4.8

Source: Company, BOBCAPS Research

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FIG 1 – QUARTERLY PERFORMANCE – CONSOLIDATED

(Rs mn)	Q2FY21	Q2FY20	YoY (%)	Q1FY21	QoQ (%)	H1FY21	H1FY20	YoY (%)
Net Revenues	22,748	21,550	5.6	11,308	101.2	34,056	47,303	(28.0)
Total Income (A)	22,748	21,550	5.6	11,308	101.2	34,056	47,303	(28.0)
Operating Expenses:								
Raw materials consumed	13,327	12,507	6.6	7,738	72.2	21,065	29,647	(28.9)
Employee Expenses	2,154	2,205	(2.3)	1,753	22.9	3,906	4,514	(13.5)
Other Expenses	3,718	3,874	(4.0)	1,855	100.4	5,573	7,782	(28.4)
Total Expenditure (B)	19,198	18,586	3.3	11,346	69.2	30,544	41,944	(27.2)
EBITDA (A-B)	3,550	2,964	19.8	(38)	NA	3,513	5,360	(34.5)
Other Income	117	67	73.6	73	58.7	190	128	48.5
Depreciation	965	916	5.4	967	(0.2)	1,932	1,828	5.7
EBIT	2,702	2,115	27.8	(931)	(390.1)	1,771	3,660	(51.6)
Finance Costs	1,235	1,396	(11.5)	1,306	(5.4)	2,540	2,781	(8.7)
PBT before excep items	1,467	719	104.0	(2,237)	NA	(770)	879	NA
Exceptional items	207	(503)	NA	(329)	NA	(122)	(456)	NA
PBT after excep items	1,674	216	673.9	(2,566)	NA	(892)	423	(310.7)
Tax expense	585	(1,470)	NA	(544)	NA	41	(1,420)	NA
Share of Associates	8	(9)	-	(20)	-	(13)	(5)	-
Reported PAT	1,097	1,677	(34.6)	(2,042)	NA	(945)	1,838	NA
Adjusted PAT	890	2,180	(59.2)	(1,713)	NA	(823)	2,294	NA
EPS (Rs)	3.9	9.6	(59.2)	(7.6)	NA	(3.6)	10.1	NA

Source: Company, BOBCAPS Research

FIG 2 – KEY PARAMETERS

(%)	Q2FY21	Q2FY20	YoY (bps)	Q1FY21	QoQ (bps)	H1FY21	H1FY20	YoY (bps)
Gross Margin	41.4	42.0	(55)	31.6	985	38.1	37.3	82
EBITDA Margin	15.6	13.8	185	(0.3)	1594	10.3	11.3	(102)
EBIT Margin	11.9	9.8	206	(8.2)	2011	5.2	7.7	(254)
PBT Margin	6.4	3.3	311	(19.8)	2623	(2.3)	1.9	(412)
Tax Rate	34.9	(679.6)	NA	21.2	1373	(4.6)	(335.5)	NA
Adj PAT Margin	3.9	10.1	(620)	(15.1)	1906	(2.4)	4.8	(727)

Source: Company, BOBCAPS Research

Earnings call highlights

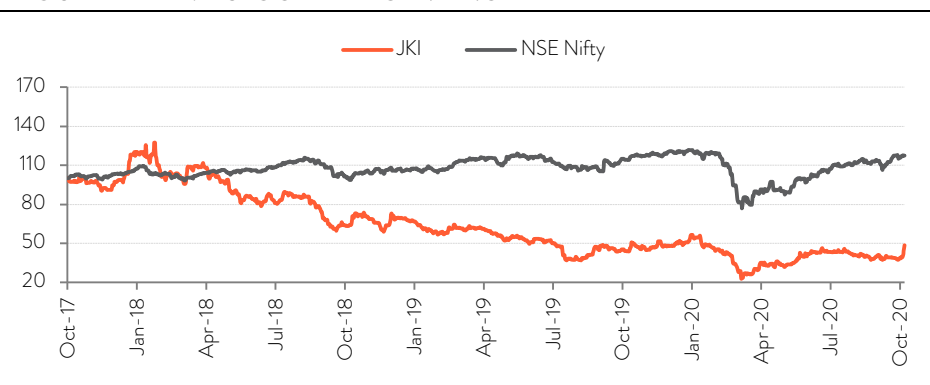
- Sales in the domestic market have been improving MoM since Jun'20 supported by pent-up demand, restrictions on Chinese imports and buildup to the festive season.
- Dealer inventory has reduced due to strong replacement demand, indicating healthy production levels in coming months.
- Per-tonne ASPs across segments have been in line with those reported in FY20.
- Passenger car radial (PCR) supplies have been on par with domestic and export demand and 2W/3W capacities are witnessing a steady increase in production. Farm/agriculture tyres are in high demand and plants continue to operate at 100%. Truck & bus radial (TBR) capacities are running at ~84% which will rise to full utilisation once OEM demand revives.
- The India business revenue mix for Q2FY21 was as follows: replacement 71%, OEM 12%, and exports 17%.
- JKI managed to reduce working capital by another Rs 5bn in Q2FY21, resulting in improved cash flow and reduced interest burden.
- Management indicated that all capex going ahead will be incurred only for maintenance purposes. The company does not plan to add any debt or incur major capex in the near term.
- JKI indicated that it has added 900 dealers in H1FY21, taking its total touchpoints to ~6,000 by Sep'20.

Valuation methodology

We forecast a revenue/EBITDA/PAT CAGR of 9%/11%/13% for JKI over FY20-FY23, backed by strong replacement demand, reviving offtake from OEMs and benign raw material prices. Management has indicated that no major capex will be incurred in the medium term and all cash flows generated from operating profit and better working capital management will be used to reduce debt over the next 2-3 years (Rs 12bn debt reduction over last 12 months).

While we continue to value the stock at 7x Sep'22E EPS, a discount of 60% to the market leader, we see a case for rerating as leverage ratios improve. Maintain BUY with an unchanged Sep'21 target price of Rs 85.

FIG 3 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

- Slower growth in MHCV tyres will impact revenues.
- A spike in natural rubber or crude derivatives will negatively affect margins.

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	2,988

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	0.9	0.8	0.7	0.6
EV/EBITDA	7.1	7.5	7.2	5.5	4.8
Adjusted P/E	10.5	7.3	20.2	6.9	5.0
P/BV	0.8	0.8	0.7	0.7	0.6

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

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): JK TYRE & INDUSTRIES (JKI IN)



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

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