

**SELL**

TP: Rs 67,000 | ▼ 26%

**MRF**

Auto Components

11 February 2021

## Near-term headwinds persist; maintain SELL

**MRF delivered Q3FY21 revenue as per projections but above-expected gross margins led to a beat on both EBITDA (+58% YoY to Rs 9.6bn) and operating margins (21.1% vs. 16.2% estimated). Adj. PAT more than doubled to Rs 5.1bn. MRF's board has approved NCD borrowings of Rs 10bn in one or more tranches. We expect near-term pressure on operating performance from rising rubber & crude prices and estimate ~350bps EBITDA margin contraction over FY21-FY23. Our Mar'22 TP remains at Rs 67,000 based on 22x one-year fwd EPS.**

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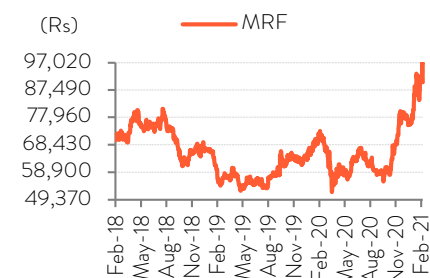
**Healthy Q3:** MRF's revenue was in line with projections at Rs 45.7bn (+14% YoY). Gross margin was far better than expected, improving 50bps QoQ against our estimate of a 460bps QoQ decline, while better operating efficiencies further supported EBITDA performance (+58% YoY to Rs 9.6bn). EBITDA margin thus expanded 590bps YoY to 21.1% (vs. 16.2% est.). Adj. PAT increased 116% YoY to Rs 5.1bn. MRF's board has approved raising funds via the issue of non-convertible debentures not exceeding Rs 10bn in one or more tranches.

Ticker/Price	MRF IN/Rs 90,085
Market cap	US\$ 5.2bn
Shares o/s	4mn
3M ADV	US\$ 55.4mn
52wk high/low	Rs 98,600/Rs 49,915
Promoter/FPI/DII	28%/5%/14%

Source: NSE

**Near-term headwinds:** With the >30% rise in both rubber and Brent crude prices from Q2FY21 levels, we anticipate gross margin deterioration for tyre companies (see our recent report [Spiking RM costs to puncture earnings](#)). To mitigate this impact, players will have to effect price hikes of over 15% which looks difficult. We forecast an EBITDA margin decline of ~350bps for MRF over FY21-FY23 (from 18.5% in FY21E).

## STOCK PERFORMANCE



**Maintain SELL:** Our revenue/EBITDA/earnings CAGR projections remain at 16%/4%/2% over FY21-FY23 and we maintain our Mar'22 TP at Rs 67,000, based on an unchanged 22x target P/E. The stock has rallied 18% over the last three months, raising valuations to 32x FY22E EPS which limits upsides. SELL.

## KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue (Rs mn)	158,370	159,911	157,078	192,002	212,354
EBITDA (Rs mn)	22,504	23,237	29,088	28,394	31,763
Adj. net profit (Rs mn)	10,969	13,950	12,429	11,737	12,983
Adj. EPS (Rs)	2,587.0	3,290.0	2,931.4	2,768.3	3,062.1
Adj. EPS growth (%)	0.4	27.2	(10.9)	(5.6)	10.6
Adj. ROAE (%)	10.3	11.6	9.4	8.2	8.3
Adj. P/E (x)	34.8	27.4	30.7	32.5	29.4
EV/EBITDA (x)	17.6	17.0	13.3	13.4	12.1

Source: Company, BOBCAPS Research

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**FIG 1 – QUARTERLY PERFORMANCE**

(Rs mn)	Q3FY21	Q3FY20	YoY (%)	Q2FY21	QoQ (%)	9MFY21	9MFY20	YoY (%)
Net Revenues	45,668	40,089	13.9	41,864	9.1	111,837	123,660	(9.6)
<b>Total Income (A)</b>	<b>45,668</b>	<b>40,089</b>	<b>13.9</b>	<b>41,864</b>	<b>9.1</b>	<b>111,837</b>	<b>123,660</b>	<b>(9.6)</b>
<b>Operating Expenses:</b>								
Raw materials consumed	25,230	23,933	5.4	23,334	8.1	63,149	74,365	(15.1)
Employee Expenses	3,929	3,380	16.3	3,331	18.0	10,358	9,764	6.1
Other Expenses	6,877	6,675	3.0	6,654	3.4	16,839	21,993	(23.4)
<b>Total Expenditure (B)</b>	<b>36,036</b>	<b>33,987</b>	<b>6.0</b>	<b>33,319</b>	<b>8.2</b>	<b>90,346</b>	<b>106,122</b>	<b>(14.9)</b>
<b>EBITDA (A-B)</b>	<b>9,632</b>	<b>6,102</b>	<b>57.8</b>	<b>8,544</b>	<b>12.7</b>	<b>21,491</b>	<b>17,538</b>	<b>22.5</b>
Other Income	634	733	(13.6)	443	43.1	1,507	2,730	(44.8)
Depreciation	2,831	2,490	13.7	2,839	(0.3)	8,400	7,142	17.6
EBIT	7,435	4,346	71.1	6,148	20.9	14,599	13,126	11.2
Finance Costs	638	704	(9.5)	528	20.8	1,902	2,051	(7.3)
PBT before excep items	6,797	3,641	86.7	5,620	20.9	12,697	11,075	14.6
PBT after excep items	6,797	3,641	86.7	5,620	20.9	12,673	11,063	14.5
Tax expense	1,680	1,275	31.8	1,590	5.7	3,379	3,820	(11.6)
Reported PAT	5,117	2,366	116.3	4,030	27.0	9,294	7,243	28.3
<b>Adjusted PAT</b>	<b>5,117</b>	<b>2,366</b>	<b>116.3</b>	<b>4,030</b>	<b>27.0</b>	<b>9,318</b>	<b>7,255</b>	<b>28.4</b>

Source: Company, BOBCAPS Research

**FIG 2 – KEY PARAMETERS**

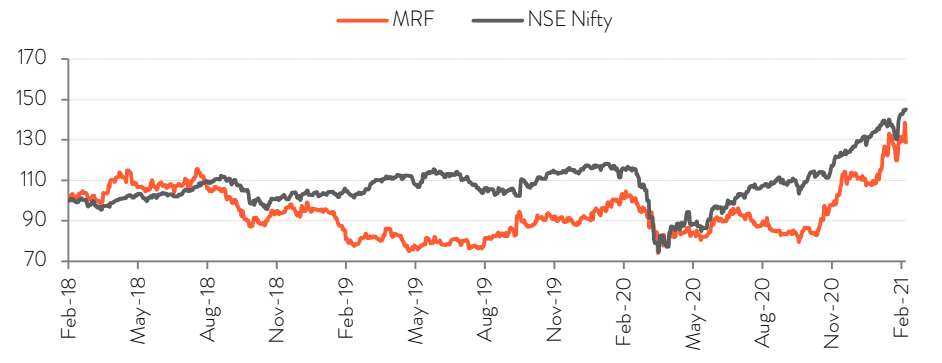
(%)	Q3FY21	Q3FY20	YoY (bps)	Q2FY21	QoQ (bps)	9MFY21	9MFY20	YoY (bps)
Gross margin	44.8	40.3	445	44	49	43.5	39.9	367
EBITDA margin	21.1	15.2	587	20	68	19.2	14.2	503
EBIT margin	16.3	10.8	544	15	159	13.1	10.6	244
PBT margin	14.9	9.1	580	13	146	11.4	9.0	240
Tax rate	24.7	35.0	(1,030)	28	(357)	26.7	34.5	(787)
Adj PAT margin	11.2	5.9	530	10	158	8.3	5.9	246

Source: Company, BOBCAPS Research

## Valuation methodology

We bake in a revenue/EBITDA/earnings CAGR of 16%/4%/2% for MRF over FY21-FY23 and maintain our Mar'22 target price at Rs 67,000, based on an unchanged 22x one-year forward P/E. The stock has rallied 18% over the last three months, raising valuations to 32x FY22E EPS which limits upsides. Maintain SELL.

**FIG 3 – RELATIVE STOCK PERFORMANCE**



Source: NSE

## Key risks

- Faster recovery in OE demand may positively impact sales.
- A fall in prices of natural rubber or crude derivatives could take margins ahead of estimates.

## FINANCIALS

### Income Statement

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
<b>Total revenue</b>	<b>158,370</b>	<b>159,911</b>	<b>157,078</b>	<b>192,002</b>	<b>212,354</b>
EBITDA	22,504	23,237	29,088	28,394	31,763
Depreciation	8,063	9,806	11,420	13,545	15,882
EBIT	18,616	16,736	19,594	17,632	18,923
Net interest income/(expenses)	(2,528)	(2,743)	(2,450)	(1,940)	(1,566)
Other income/(expenses)	4,175	3,305	1,926	2,782	3,042
Exceptional items	(1,356)	0	0	0	0
EBT	14,733	13,993	17,144	15,692	17,357
Income taxes	5,120	43	4,714	3,954	4,374
Extraordinary items	0	0	0	0	0
Min. int./Inc. from associates	0	0	0	0	0
<b>Reported net profit</b>	<b>9,613</b>	<b>13,950</b>	<b>12,429</b>	<b>11,737</b>	<b>12,983</b>
Adjustments	1,356	0	0	0	0
<b>Adjusted net profit</b>	<b>10,969</b>	<b>13,950</b>	<b>12,429</b>	<b>11,737</b>	<b>12,983</b>

### Balance Sheet

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Accounts payables	23,276	23,401	23,430	32,218	30,603
Other current liabilities	21,389	24,404	22,646	36,497	34,410
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	132,342	143,803	156,480
Shareholders' fund	106,533	120,044	132,385	143,845	156,522
<b>Total liabilities and equities</b>	<b>173,885</b>	<b>187,263</b>	<b>197,875</b>	<b>231,974</b>	<b>238,949</b>
Cash and cash eq.	601	11,068	4,246	4,802	4,587
Accounts receivables	23,616	22,570	25,132	32,640	31,853
Inventories	29,509	28,527	29,845	40,320	38,224
Other current assets	1,775	151	471	576	531
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
<b>Total assets</b>	<b>173,885</b>	<b>187,263</b>	<b>197,875</b>	<b>231,974</b>	<b>238,949</b>

Source: Company, BOBCAPS Research

### Cash Flows

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Net income + Depreciation	17,675	23,756	23,849	25,282	28,866
Interest expenses	2,528	2,743	2,450	1,940	(1,566)
Non-cash adjustments	(4,175)	(3,305)	(1,926)	(2,782)	(3,042)
Changes in working capital	(7,962)	10,584	(5,929)	4,551	(774)
Other operating cash flows	1,356	0	0	0	0
<b>Cash flow from operations</b>	<b>9,422</b>	<b>33,778</b>	<b>18,444</b>	<b>28,990</b>	<b>23,484</b>
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	1,926	2,782	3,042
<b>Cash flow from investing</b>	<b>(11,073)</b>	<b>(7,549)</b>	<b>(22,728)</b>	<b>(26,218)</b>	<b>(22,958)</b>
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)	(2,450)	(1,940)	(1,566)
Dividends paid	0	(509)	(88)	(277)	(306)
Other financing cash flows	1,724	(4,044)	0	0	0
<b>Cash flow from financing</b>	<b>866</b>	<b>(15,760)</b>	<b>(2,538)</b>	<b>(2,217)</b>	<b>(3,872)</b>
<b>Changes in cash and cash eq.</b>	<b>(786)</b>	<b>10,468</b>	<b>(6,823)</b>	<b>556</b>	<b>(3,346)</b>
<b>Closing cash and cash eq.</b>	<b>601</b>	<b>11,068</b>	<b>4,246</b>	<b>4,802</b>	<b>4,587</b>

### Per Share

Y/E 31 Mar (Rs)	FY19A	FY20A	FY21E	FY22E	FY23E
Reported EPS	2,587.0	3,290.0	2,931.4	2,768.3	3,062.1
Adjusted EPS	2,587.0	3,290.0	2,931.4	2,768.3	3,062.1
Dividend per share	0.0	100.0	20.7	65.3	72.2
Book value per share	25,125.7	28,312.1	31,222.8	33,925.8	36,915.7

### Valuations Ratios

Y/E 31 Mar (x)	FY19A	FY20A	FY21E	FY22E	FY23E
EV/Sales	2.5	2.5	2.5	2.0	1.8
EV/EBITDA	17.6	17.0	13.3	13.4	12.1
Adjusted P/E	34.8	27.4	30.7	32.5	29.4
P/BV	3.6	3.2	2.9	2.7	2.4

### DuPont Analysis

Y/E 31 Mar (%)	FY19A	FY20A	FY21E	FY22E	FY23E
Tax burden (Net profit/PBT)	74.4	99.7	72.5	74.8	74.8
Interest burden (PBT/EBIT)	79.1	83.6	87.5	89.0	91.7
EBIT margin (EBIT/Revenue)	11.8	10.5	12.5	9.2	8.9
Asset turnover (Revenue/Avg TA)	130.5	121.3	110.5	124.6	128.6
Leverage (Avg TA/Avg Equity)	1.2	1.2	1.1	1.1	1.1
Adjusted ROAE	10.8	12.3	9.8	8.5	8.6

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

### Ratio Analysis

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
<b>YoY growth (%)</b>					
Revenue	7.2	1.0	(1.8)	22.2	10.6
EBITDA	1.0	3.3	25.2	(2.4)	11.9
Adjusted EPS	0.4	27.2	(10.9)	(5.6)	10.6
<b>Profitability &amp; Return ratios (%)</b>					
EBITDA margin	14.2	14.5	18.5	14.8	15.0
EBIT margin	11.8	10.5	12.5	9.2	8.9
Adjusted profit margin	6.9	8.7	7.9	6.1	6.1
Adjusted ROAE	10.3	11.6	9.4	8.2	8.3
ROCE	9.4	12.0	9.7	8.3	8.3
<b>Working capital days (days)</b>					
Receivables	52	53	55	55	55
Inventory	59	66	68	67	68
Payables	76	90	95	88	90
<b>Ratios (x)</b>					
Gross asset turnover	0.6	0.8	0.9	0.9	0.9
Current ratio	1.2	1.2	1.2	1.1	1.1
Net interest coverage ratio	7.4	6.1	8.0	9.1	12.1
Adjusted debt/equity	0.2	0.1	0.1	0.1	0.1

Source: Company, BOBCAPS Research

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### Recommendations and Absolute returns (%) over 12 months

**BUY** – Expected return >+15%

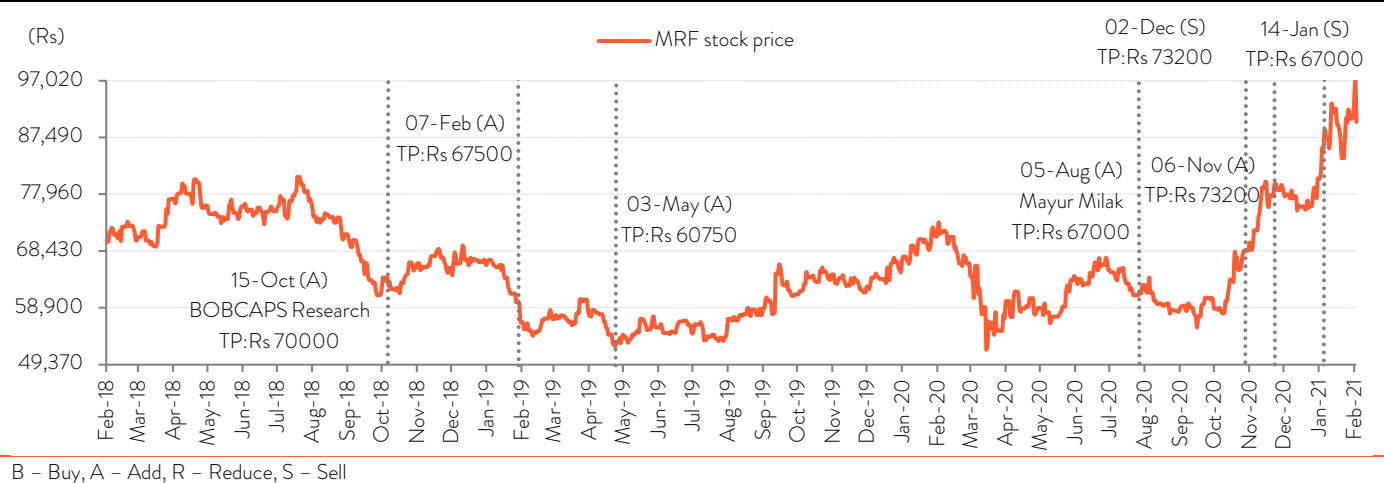
**ADD** – Expected return from >+5% to +15%

**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): MRF (MRF IN)



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