

CEAT

Sector: Auto-ancillary /Mid-Cap | Earnings Update – 2QFY19

BUY

29 October 2018

Background: CEAT, part of the RPG group, is one among the top four tire manufacturers in India with a total manufacturing capacity of >1000 MT/day & manufacturing plants situated in Nashik, Bhandup (Mumbai), Ambarnath, Halol, and Gujarat, the company manufactures all tires: Truck & Bus (35%), 2W/3W (32%), Passenger vehicles (16%), LCV (7%), Farm (5%), and Specialty (5%). In terms of market, replacement contributed 59% of the sales while OEM and exports make up 29% and 12% of the sales, respectively. CEAT has a robust distribution network consisting of over 4,500 dealers, 33 regional offices and more than 500+ C&F agents. It is also the No.1 player in Sri Lanka in terms of market share.

Sensex	34,067
Nifty	10,250
Price	INR 1,138
Target Price(12 months)	INR 1,760
Recommendation	BUY
52 Week High/Low	INR 2,019/1,227
Bloomberg / Reuters	CEAT IN /CEAT NS
Equity (shares in mn)	40.45
Mkt. Cap in bn	INR 46.0/\$ 0.63
Avg. Daily Vol. ('000)	682
Avg. Daily Vol. (mn)	INR 776/\$ 10.5

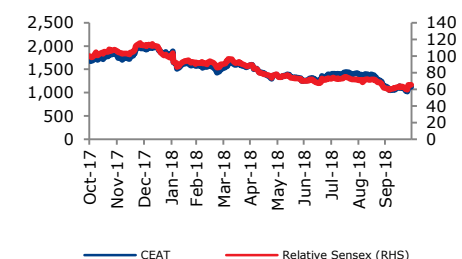
Shareholding	Sep 17	Jun 18	Sep 18
Promoters (%)	50.8	50.8	50.9
FII (%)	25.9	20.2	21.5
DII (%)	8.9	11.7	10.4
Others (%)	14.4	17.3	17.2
Pledge (% of promoter holding)	0.00	0.00	0.00

Valuation Summary (INR bn)

Y/E March	2018	2019E	2020E
Revenue	62.3	71.6	83.8
EBITDA	6.1	7.5	9.7
Adj PAT	2.7	3.6	4.5
Adj EPS*	66.7	89.7	110.0
% growth	-27.0	34.0	23.0
P/E	17.0	12.7	10.3
P/ BV	1.8	1.7	1.5
EV/EBITDA	8.4	7.3	4.9
EV/Sales	0.8	0.7	0.6
Div Yield (%)	1.0	0.7	1.2
ROE (%)	9.5	12.7	13.7

*Consolidated earnings

Performance %	1M	3M	12M
CEAT	-1.2	-18.8	-33.0
Sensex	-5.9	-8.7	2.7



Impressive performance in challenging times

- In 2QFY19, CEAT's consolidated revenue grew by 15.2% YoY to INR 17.5bn and standalone revenues grew by 14% YoY to INR 17.2bn, largely driven by volume growth of 12.5% YoY and realizations growth of ~2.5% YoY. The volume growth was broad-based with all major business segments posting double digit growth.
- EBITDA margins contracted by 240bps YoY and 120bps QoQ on account of higher raw material costs which were up by 3.5% QoQ on a per ton basis. Management expects to see a further increase in Raw material prices in 3QFY19 by 5% over 2QFY19.
- Employee costs were up 100 bps QoQ on account of certain retrospective wage settlements, increments and addition of employees in Nagpur. Input costs increased on account of rise in crude prices and rupee depreciation, which lead to an increase in the price of crude linked derivatives and carbon black.
- The management was able to bring down its working capital by INR400mn in 2QFY19 on account of the cost initiatives taken.
- The company took a price hike of 1.7% in 2QFY19. Further, the company took a price hike of 2% in TBR segment and 4% in two-wheelers in the month of October.
- The capex guidance for FY19-21E stands at ~INR 35bn with ~INR 30bn being spent in FY20E and the balance in FY21E. The management has also guided that the peak debt equity ratio would remain at 1:1 over the next 3 years.
- The TBR capacity would come on stream in 2HFY19 with an initial run rate of 3,000- 5,000 tyres per month and would be ramped up to full capacity (80,000 tyres /month) in 18 months. By July 2019, PCR capacity would become functional.
- Management also stated that there will not be any major immediate technical changes for tyres due to axle load norms. It would only lead to a shift to 22.5 inch tyre from 20 inch tyres used currently.

Valuation: The company has had an impressive volume growth momentum of ~15% in 1HFY19. The price increase of 2%/4% would help in coping up some of the RM pressure on account of rising crude prices. At CMP, the stock is trading at P/E of 12.7X/10.3x on FY19E/FY20E EPS, respectively. We maintain our **BUY** rating on CEAT with revised target price of INR 1,760, assigning a P/E of 16X on FY20 EPS.

Risks: Further increase in rubber & crude prices can negatively impact margins.

Results Summary 2QFY19

Y/E March (INR mn)	2QFY19	2QFY18	YoY Growth	1QFY19	QoQ Growth
Net sales	17,546	15,230	15.2%	16,742	4.8%
EBITDA	1,592	1,747	-8.8%	1,741	-8.5%
Depreciation	477	409	16.6%	414	15.2%
Other Income	33	65	-49.3%	56	-41.6%
PBT	943	1,086	-13.2%	1,210	-22.1%
Tax	370	421	-12.0%	431	-14.1%
PAT	632	665	-5.0%	779	-18.9%
EBITDA Margin (%)	9.1	11.5		10.4	
Tax Incidence (%)	39.3	38.7		35.6	
PAT Margin (%)	3.6	4.4		4.7	

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RESEARCH			
Sathyanarayanan M	Consumption	+91-44 - 3000 7361	sathyanarayananm@chola.murugappa.com
Mugilan K	Technicals	+91-44 - 3000 7353	mugilank@chola.murugappa.com
Keerthi S	Banking & Financial Services	+91-44 - 3000 7363	keerthi@chola.murugappa.com
Sai Lavanya K	IT, Auto & Auto Ancillary	+91-44 - 3000 7266	saik@chola.murugappa.com
Muthu Kumar J	Associate- Research	+91-44 - 3000 7360	muthukumarj@chola.murugappa.com
Sahil Jain	Associate - Cement	+91-44 - 3000 7360	sahilj@chola.murugappa.com
INSTITUTIONAL SALES			
Venkat Chidambaram	Head of FII Business & Corporate Finance*	+91-44 - 24473310	venkatc@chola.murugappa.com
Kishore K Ganti	Mumbai	+91-22-26597239	kishorekg@chola.murugappa.com
Bhavesh Katariya	Mumbai	+91-9860297739	bhaveshgk@chola.murugappa.com
Sudhanshu Kumar	Institutional Equities*	+91 - 9953175955	sudhanshuk@chola1.murugappa.com
Balaji H	Compliance Officer	044 - 30007226	balajih@chola.murugappa.com

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