

October 28, 2018

Q2FY19 Result Update

☑ Change in Estimates | ☑ Target | ■ Reco

Change in Estimates

	Current		Previous	
	FY19E	FY20E	FY19E	FY20E
Rating	ACCUMULATE		ACCUMULATE	
Target Price	1,255		1,451	
Sales (Rs. m)	67,454	81,467	67,709	82,388
% Chng.			(0.4)	(1.1)
EBITDA (Rs. m)	6,739	8,219	7,122	8,789
% Chng.			(5.4)	(6.5)
EPS (Rs.)	74.5	83.7	82.1	96.7
% Chng.			(9.3)	(13.5)

Key Financials

	FY17	FY18	FY19E	FY20E
Sales (Rs. m)	57,665	62,308	67,454	81,467
EBITDA (Rs. m)	6,568	6,148	6,739	8,219
Margin (%)	11.4	9.9	10.0	10.1
PAT (Rs. m)	3,745	2,719	3,013	3,385
EPS (Rs.)	92.6	67.2	74.5	83.7
Gr. (%)	(16.6)	(27.4)	10.8	12.3
DPS (Rs.)	11.5	11.5	13.0	14.0
Yield (%)	1.0	1.0	1.2	1.3
RoE (%)	16.8	10.8	11.1	11.5
RoCE (%)	17.0	13.1	11.5	12.0
EV/Sales (x)	0.9	0.8	0.9	0.8
EV/EBITDA (x)	8.1	8.5	9.0	7.6
PE (x)	11.9	16.5	14.8	13.2
P/BV (x)	1.9	1.7	1.6	1.5

Key Data

CEAT.BO | CEAT IN

52-W High / Low	Rs.2,030 / Rs.984
Sensex / Nifty	33,349 / 10,030
Market Cap	Rs.45bn / \$ 610m
Shares Outstanding	40m
3M Avg. Daily Value	Rs.1526.9m

Shareholding Pattern (%)

Promoter's	51.00
Foreign	21.49
Domestic Institution	10.42
Public & Others	17.09
Promoter Pledge (Rs bn)	-

Stock Performance (%)

	1M	6M	12M
Absolute	(10.5)	(28.3)	(33.8)
Relative	(1.9)	(25.4)	(34.2)

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Short term cost pressures to continue!

CEAT's Q2FY19 reported consolidated operating margin at 9.1%, down 240bps YoY / 120bps QoQ, was below our expectations of 9.9%. While the rise in RM costs for Q2FY19 (crude derivatives up ~15% YoY, carbon black higher 20% YoY, natural rubber down 2% YoY) was more or less offset through price hikes and mix improvement over the quarter with gross margins dipping a mere 10bps YoY (flat QoQ), other expenses as a % of sales surged 160bps YoY on account of higher production activities as well as increased ad spend during the quarter leading to the margin disappointment.

Given the uncertainty regarding crude as well as short term slowdown in core product portfolio coupled with expected ramp up of new capacities and adverse market mix, we remain cautious on the stock. With a target price of Rs1,255, based on 15x Mar'20E consolidated EPS. The stock currently trades at 14.6x/13.2x FY19/20E EPS.

- Consolidated performance:** Consolidated sales growth for the quarter was at 15.2% YoY (up ~3% QoQ) to Rs17.5bn (PLe: Rs16.6bn). EBITDA margin came in at 9.1% (PLe: 9.9%), lower 240bps YoY / 120bps QoQ. Absolute EBITDA declined ~9% YoY to Rs1.6bn (PLe: Rs1.65bn). With average rubber prices for the quarter stable at benign levels of ~130/kg (higher ~5% QoQ/down 2% YoY), gross margins dipped just 10bps YoY / flat QoQ (despite the rise in crude price, which forms ~45% of the RM basket). Staff costs as well as other expenses as a % of sales however were up 80bps & 160bps YoY respectively. Share of profit from associate was lower 10% YoY / up 21% QoQ at Rs58mn. Adjusting for the one-off expenses towards VRS, net profit for the quarter stood at Rs644mn, lower 14% YoY / 9% QoQ. (PLe: Rs667mn).
- Standalone performance:** Revenue growth for the standalone entity stood at 13.6% YoY (up 2.6% QoQ) to Rs17.2bn (PLe: Rs16.6bn). EBITDA margin was lower at 9.1% (down 290bps YoY / 130bps QoQ; PLe: 10.4%); EBITDA plummeted ~13.5% YoY to ~Rs1.6bn. Adjusted profit for the quarter was lower 8% YoY to Rs771mn.
- Key takeaways from the con-call:** (1) Volume growth for CEAT over the quarter has been strong at 12.4% YoY / 1.4% QoQ. (2) Absolute increase in RM costs over Q2FY19 has been 2.5% QoQ, however, gross margins have remained intact because of difference in the stock of finished goods which included some non-material costs. Adjusted gross margins are down 1.2% QoQ. (3) The management expects RM costs to rise sequentially by 4-5% till Dec'18 on account of crude price rise as well as rupee depreciation. (4) The company has taken an average price hike of 4% for its 2W segment in Oct'18 (2W margins have come-off from earlier levels). Management is looking at further price increase across segments in Nov-Dec. (5) CEAT has reduced its working capital by Rs400mn over Q2FY19 and the company expects working capital reduction of ~Rs1bn per year. (6) YTD CV segment growth has been ~30-35% for the tyre industry. (7) The company has been able to expand its PCR capacity by 10-12% on a QoQ basis through debottlenecking and expects further 10% expansion in the same by Jan'18. (8) YTD capex spend for FY19 has been ~Rs4.4bn, while overall capex for FY19 is expected to be ~Rs13-15bn (earlier guidance for FY19e was at Rs15-17bn). The 3Yr capex guidance stands at earlier levels of ~Rs35bn (additional Rs5bn for Specialty tyre segment).

Exhibit 1: Q2FY19 Result Overview – Standalone (Rs m)

Y/e March	Q2FY19	Q2FY18	YoY gr. (%)	Q1FY19	H1FY19	H1FY18	YoY gr. (%)
Net Revenues	17,182	15,118	13.6	16,742	33,923	29,629	14.5
Raw Materials	10,577	9,198	15.0	10,281	20,858	18,849	10.7
<i>% of Net Sales</i>	<i>61.6</i>	<i>60.8</i>		<i>61.4</i>	<i>61.5</i>	<i>63.6</i>	
Personnel	1,317	1,052	25.2	1,103	2,419	2,013	20.2
<i>% of Net Sales</i>	<i>7.7</i>	<i>7.0</i>		<i>6.6</i>	<i>7.1</i>	<i>6.8</i>	
Manufacturing & Other Exp	3,721	3,056	21.8	3,617	7,338	6,414	14.4
<i>% of Net Sales</i>	<i>21.7</i>	<i>20.2</i>		<i>21.6</i>	<i>21.6</i>	<i>21.6</i>	
Total Expenditure	15,614	13,305	17.4	15,001	30,615	27,277	12.2
EBITDA	1,567	1,813	(13.5)	1,741	3,308	2,352	40.6
<i>EBITDA Margin (%)</i>	<i>9.1</i>	<i>12.0</i>		<i>10.4</i>	<i>9.8</i>	<i>7.9</i>	
Depreciation	435	406	7.2	414	849	800	6.2
EBIT	1,132	1,407	(19.5)	1,327	2,459	1,553	58.3
Interest Expenses	127	233	(45.4)	150	277	454	(39.0)
Non-operating income	122	84	45.4	56	178	398	(55.3)
Extraordinary Income	(20)	(6)	255.4	(23)	(43)	(9)	370.3
PBT	1,107	1,252	(11.6)	1,210	2,317	1,488	55.7
Tax-Total	354	417	(15.2)	431	785	461	70.1
<i>Tax Rate (%) - Total</i>	<i>32.0</i>	<i>33.3</i>	<i>(4.1)</i>	<i>35.6</i>	<i>33.9</i>	<i>31.0</i>	<i>9.2</i>
Reported PAT	753	835	(9.8)	779	1,532	1,026	49.3
Adj. PAT	771	840	(8.2)	799	1,570	1,034	51.8

Source: Company, PL

Exhibit 2: Q2FY19 Result Overview - Consolidated (Rs m)

Y/e March	Q2FY19	Q2FY18	YoY gr. (%)	Q1FY19	H1FY19	H1FY18	YoY gr. (%)
Net Revenues	17,546	15,230	15.2	17,063	34,609	29,828	16.0
Raw Materials	10,648	9,230	15.4	10,350	20,998	18,839	11.5
<i>% of Net Sales</i>	<i>60.7</i>	<i>60.6</i>		<i>60.7</i>	<i>60.7</i>	<i>63.2</i>	
Personnel	1,417	1,110	27.6	1,189	2,606	2,113	23.4
<i>% of Net Sales</i>	<i>8.1</i>	<i>7.3</i>		<i>7.0</i>	<i>7.5</i>	<i>7.1</i>	
Manufacturing & Other Exp	3,889	3,143	23.7	3,766	7,655	6,583	16.3
<i>% of Net Sales</i>	<i>22.2</i>	<i>20.6</i>		<i>22.1</i>	<i>22.1</i>	<i>22.1</i>	
Total Expenditure	15,954	13,484	18.3	15,305	31,259	27,534	13.5
EBITDA	1,592	1,747	(8.8)	1,758	3,351	2,294	46.1
<i>EBITDA Margin (%)</i>	<i>9.1</i>	<i>11.5</i>		<i>10.3</i>	<i>9.7</i>	<i>7.7</i>	
Depreciation	477	409	16.6	460	937	805	16.4
EBIT	1,116	1,338	(16.6)	1,298	2,414	1,489	62.1
Interest Expenses	186	237	(21.5)	204	390	463	(15.8)
Non-operating income	33	65	(49.3)	37	69	168	(58.6)
Extraordinary Expenses	20	80		23	43	83	(48.6)
PBT	944	1,086	(13.1)	1,108	2,051	1,111	84.7
Tax-Total	370	421	(12.0)	442	812	468	73.5
<i>Tax Rate (%) - Total</i>	<i>39.2</i>	<i>38.7</i>	<i>1.3</i>	<i>39.9</i>	<i>39.6</i>	<i>42.1</i>	<i>(6.0)</i>
Reported PAT	573	665	(13.8)	666	1,239	643	92.8
Adj. PAT	587	721	(18.6)	682	1,269	701	81.0
Minority Interest/Share of associates	57	28	102.1	42	100	63	59.5
PAT after MI	644	749	(14.1)	709	1,338	705	89.8

Source: Company, PL

Financials

Income Statement (Rs m)

Y/e Mar	FY17	FY18	FY19E	FY20E
Net Revenues	57,665	62,308	67,454	81,467
YoY gr. (%)	5.2	8.1	8.3	20.8
Cost of Goods Sold	33,998	38,100	40,944	49,532
Gross Profit	23,667	24,208	26,509	31,935
Margin (%)	41.0	38.9	39.3	39.2
Employee Cost	4,063	4,383	4,931	5,793
Other Expenses	13,037	13,677	14,840	17,923
EBITDA	6,568	6,148	6,739	8,219
YoY gr. (%)	(15.1)	(6.4)	9.6	22.0
Margin (%)	11.4	9.9	10.0	10.1
Depreciation and Amortization	1,431	1,686	2,057	2,510
EBIT	5,137	4,462	4,682	5,709
Margin (%)	8.9	7.2	6.9	7.0
Net Interest	817	974	1,217	1,819
Other Income	186	295	331	373
Profit Before Tax	4,373	3,443	3,457	3,923
Margin (%)	7.6	5.5	5.1	4.8
Total Tax	1,064	1,340	1,106	1,256
Effective tax rate (%)	24.3	38.9	32.0	32.0
Profit after tax	3,309	2,103	2,351	2,668
Minority interest	(19)	(47)	(52)	(57)
Share Profit from Associate	284	230	272	320
Adjusted PAT	3,745	2,719	3,013	3,385
YoY gr. (%)	(16.6)	(27.4)	10.8	12.3
Margin (%)	6.5	4.4	4.5	4.2
Extra Ord. Income / (Exp)	(133)	(340)	(340)	(340)
Reported PAT	3,612	2,380	2,674	3,045
YoY gr. (%)	(17.5)	(34.1)	12.4	13.9
Margin (%)	6.3	3.8	4.0	3.7
Other Comprehensive Income	-	-	-	-
Total Comprehensive Income	3,612	2,380	2,674	3,045
Equity Shares O/s (m)	40	40	40	40
EPS (Rs)	92.6	67.2	74.5	83.7

Source: Company Data, PL Research

Balance Sheet Abstract (Rs m)

Y/e Mar	FY17	FY18	FY19E	FY20E
Non-Current Assets				
Gross Block	27,017	31,294	46,300	52,300
Tangibles	26,155	30,198	45,198	51,198
Intangibles	862	1,096	1,102	1,102
Acc: Dep / Amortization	2,492	4,056	6,113	8,623
Tangibles	2,322	3,762	5,819	8,328
Intangibles	170	294	294	294
Net fixed assets	24,525	27,238	40,187	43,677
Tangibles	23,833	26,436	39,379	42,869
Intangibles	692	802	808	808
Capital Work In Progress	3,263	3,100	-	-
Goodwill	-	-	-	-
Non-Current Investments	1,732	1,786	1,799	1,799
Net Deferred tax assets	(2,133)	(1,893)	(1,993)	(2,093)
Other Non-Current Assets	1,914	1,340	1,340	1,090
Current Assets				
Investments	643	401	401	401
Inventories	9,435	7,846	8,131	9,821
Trade receivables	6,138	7,472	7,762	9,374
Cash & Bank Balance	359	863	2,255	(71)
Other Current Assets	1,695	1,465	1,215	965
Total Assets	50,533	52,932	64,512	68,478
Equity				
Equity Share Capital	405	405	405	405
Other Equity	23,745	25,656	27,804	30,283
Total Network	24,150	26,061	28,209	30,688
Non-Current Liabilities				
Long Term borrowings	8,660	6,761	16,761	15,761
Provisions	363	344	344	344
Other non current liabilities	-	-	-	-
Current Liabilities				
ST Debt / Current of LT Debt	580	1,956	1,956	1,956
Trade payables	7,582	8,705	7,762	9,374
Other current liabilities	5,927	5,624	5,849	6,524
Total Equity & Liabilities	50,533	52,932	64,512	68,478

Source: Company Data, PL Research

Cash Flow (Rs m)

Y/e Mar	FY17	FY18	FY19E	FY20E
PBT	4,373	3,443	3,457	3,923
Add. Depreciation	1,431	1,686	2,057	2,510
Add. Interest	817	974	1,217	1,819
Less Financial Other Income	186	295	331	373
Add. Other	759	274	323	377
Op. profit before WC changes	7,380	6,376	7,054	8,629
Net Changes-WC	(2,164)	1,782	(993)	(414)
Direct tax	(513)	(1,581)	(1,006)	(1,156)
Net cash from Op. activities	4,702	6,577	5,055	7,060
Capital expenditures	(5,907)	(4,236)	(11,907)	(6,000)
Interest / Dividend Income	-	-	-	-
Others	(361)	181	(13)	-
Net Cash from Invst. activities	(6,268)	(4,055)	(11,919)	(6,000)
Issue of share cap. / premium	-	-	-	-
Debt changes	2,608	(523)	10,000	(1,000)
Dividend paid	(465)	(465)	(526)	(566)
Interest paid	(817)	(974)	(1,217)	(1,819)
Others	-	-	-	-
Net cash from Fin. activities	1,326	(1,962)	8,257	(3,386)
Net change in cash	(240)	561	1,392	(2,326)
Free Cash Flow	(1,205)	2,342	(6,852)	1,060

Source: Company Data, PL Research

Key Financial Metrics

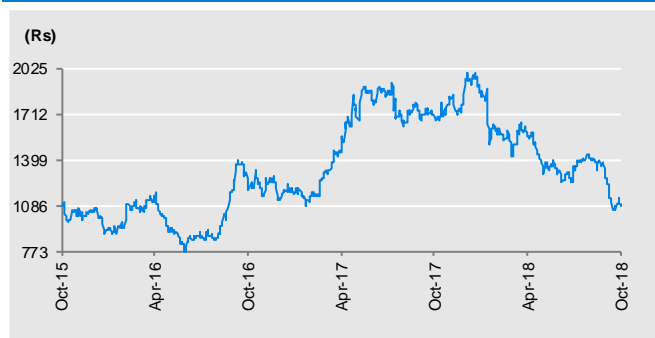
Y/e Mar	FY17	FY18	FY19E	FY20E
Per Share(Rs)				
EPS	92.6	67.2	74.5	83.7
CEPS	127.9	108.9	125.3	145.7
BVPS	597.0	644.3	697.4	758.6
FCF	(29.8)	57.9	(169.4)	26.2
DPS	11.5	11.5	13.0	14.0
Return Ratio(%)				
RoCE	17.0	13.1	11.5	12.0
ROIC	13.3	8.3	8.3	8.2
RoE	16.8	10.8	11.1	11.5
Balance Sheet				
Net Debt : Equity (x)	0.3	0.3	0.6	0.6
Net Working Capital (Days)	51	39	44	44
Valuation(x)				
PER	11.9	16.5	14.8	13.2
P/B	1.9	1.7	1.6	1.5
P/CEPS	105.0	89.4	102.8	119.6
EV/EBITDA	8.1	8.5	9.0	7.6
EV/Sales	0.9	0.8	0.9	0.8
Dividend Yield (%)	1.0	1.0	1.2	1.3

Source: Company Data, PL Research

Quarterly Financials (Rs m)

Y/e Mar	Q3FY18	Q4FY18	Q1FY19	Q2FY19
Net Revenue	15,742	16,739	17,063	17,546
YoY gr. (%)	12.6	13.7	16.9	15.2
Raw Material Expenses	9,161	10,100	10,350	10,648
Gross Profit	6,580	6,639	6,713	6,898
Margin (%)	41.8	39.7	39.3	39.3
EBITDA	1,870	1,976	1,758	1,592
YoY gr. (%)	7.0	5.7	(11.0)	(9.4)
Margin (%)	11.9	11.8	10.3	9.1
Depreciation / Depletion	433	448	460	477
EBIT	1,436	1,528	1,298	1,116
Margin (%)	9.1	9.1	7.6	6.4
Net Interest	273	238	204	186
Other Income	66	69	37	33
Profit before Tax	1,220	1,113	1,108	943
Margin (%)	7.7	6.6	6.5	5.4
Total Tax	475	397	442	370
Effective tax rate (%)	38.9	35.7	39.9	39.3
Profit after Tax	745	716	666	572
Minority interest	5	-	-	-
Share Profit from Associates	76	-	-	-
Adjusted PAT	826	962	689	592
YoY gr. (%)	(0.8)	23.6	4,524.8	(23.4)
Margin (%)	5.2	5.7	4.0	3.4
Extra Ord. Income / (Exp)	(10)	(246)	(23)	(20)
Reported PAT	816	716	666	572
YoY gr. (%)	(2.0)	9.3	5,743.9	(17.5)
Margin (%)	5.2	4.3	3.9	3.3
Other Comprehensive Income	-	-	-	-
Total Comprehensive Income	816	716	666	572
Avg. Shares O/s (m)	40	40	40	40
EPS (Rs)	20.4	23.8	17.0	14.6

Source: Company Data, PL Research

Price Chart
Recommendation History


No.	Date	Rating	TP (Rs.)	Share Price (Rs.)
1	16-Nov-17	Accumulate	1,973	1,746
2	10-Jan-18	Accumulate	1,973	2,003
3	5-Feb-18	Accumulate	1,954	1,650
4	13-Apr-18	Accumulate	1,954	1,593
5	2-May-18	Accumulate	1,711	1,596
6	11-Jun-18	Accumulate	1,711	1,596
7	15-Jun-18	Accumulate	1,451	1,348
8	10-Jul-18	Accumulate	1,451	1,258
9	23-Jul-18	Accumulate	1,451	1,324
10	5-Oct-18	Accumulate	1,451	1,055

Analyst Coverage Universe

Sr. No.	CompanyName	Rating	TP (Rs)	Share Price (Rs)
1	Ashok Leyland	BUY	146	118
2	Atul Auto	Accumulate	397	303
3	Bajaj Auto	Reduce	2,394	2,478
4	Bharat Forge	Accumulate	786	592
5	CEAT	Accumulate	1,451	1,055
6	Eicher Motors	Accumulate	30,296	21,908
7	Exide Industries	Accumulate	282	252
8	Hero Motocorp	Accumulate	3,385	2,895
9	Mahindra & Mahindra	BUY	1,058	795
10	Maruti Suzuki	BUY	8,510	6,723
11	Motherson Sumi Systems	Accumulate	348	242
12	Tata Motors	BUY	352	223
13	TVS Motors	Accumulate	618	535
14	Wabco India	Accumulate	7,111	6,422

PL's Recommendation Nomenclature (Absolute Performance)

Buy	: > 15%
Accumulate	: 5% to 15%
Hold	: +5% to -5%
Reduce	: -5% to -15%
Sell	: < -15%
Not Rated (NR)	: No specific call on the stock
Under Review (UR)	: Rating likely to change shortly

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