Stock Update

Margin pressure to sustain; Downgrade to Hold

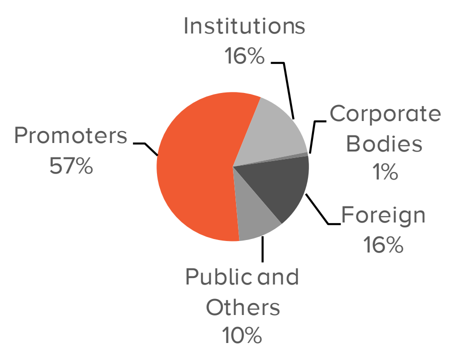
TVS Motors

Reco: Hold | CMP: Rs491

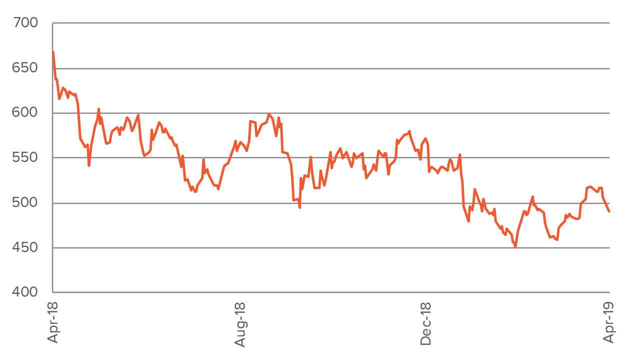
Company details

Price target:	Rs530
Market cap:	Rs23,334 cr
52-week high/low:	Rs693/449
NSE volume: (No of shares)	14.1 lakh
BSE code:	532343
NSE code:	TVSMOTOR
Sharekhan code:	TVSMOTOR
Free float: (No of shares)	20.2 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	9.7	2.1	-3.2	-21.6
Relative to Sensex	7.4	-6.0	-17.6	-31.2

Key points

- **Disappointing operating performance in Q4FY2019:** TVS Motor Company (TVSM) posted dismal Q4FY2019 operating results. Operating margins shrank on a y-o-y basis and were below our as well as the consensus estimate. Topline at Rs 4,384 crore grew 9% y-o-y on the back of growth of 7% growth in realizations due to increasing share of nonmopeds and price hikes undertaken. Volume growth slowed down sharply to 2% driven by weak retail demand due to slowing economic growth and rural stress. Operating margins at 7% declined 40 bps y-o-y and were below our estimates of 7.9%. Operating deleverage due to subdued volumes, higher commodity costs and discounting led to drop in margins. The EBITDA at Rs 308 cr is up 4.4% y-o-y and is below the estimated Rs 339 crore. The tax rate for the quarter at 27.2% is up as against 14% in Q4FY2018. Consequently, the PAT at Rs134 cr dropped 19% y-o-y and missed our estimates of Rs 149 cr.

- **TVS to continue outpacing industry but at cost of margins; double-digit margin highly unlikely:** We expect TVSM to continue outpacing industry growth driven by new product launches and increasing distribution reach. However, market share gains will come at the cost of margins. TVSM has historically preferred market share gains at the expense of margins and we expect the strategy to continue. Domestic 2W industry forming 80% of volumes is likely to remain subdued in FY2020 (company expects marginal growth). Higher inventory levels, rural distress (lower rabi sowing) and increased prices on account of regulatory changes (ABS/CBS and BS6 emission norms) will continue to impact volumes. Moreover, competitive intensity has increased and is expected to remain elevated as rivals launch products at aggressive prices to gain share in a subdued industry environment. Also, regulatory cost increases will lead to prices increasing steeply by 10-12% which cannot be fully passed onto the end consumer in the wake of muted industry demand. We expect TVSM margin pressures to sustain and expect 40 bps y-o-y contraction to 7.5% in FY2020. This is a far cry from the management aspirational target of a double digit margin.

- **Outlook: Margin declining trend to sustain; Valuations expensive:** TVSM margins dropped

40 bps y-o-y in Q4FY2019. We expect the cost pressure points to sustain as industry demand is expected to remain muted. Further steep increase in prices due to regulations and increased discounting by peers to gain market share will continue to put margin pressure. We expect 40 bps margin contraction in FY2020. At CMP, the stock is trading at 24x FY2021 core business earnings (after adjusting Rs 40/share assigned for TVS Credit Services) which is at the higher end of its long term historical multiples, leaving scope of limited upside from the current levels.

- **Valuations: Cut estimates to factor margin pressure; Downgrade to Hold:** TVSM reported lower than estimated Q4 FY2019 margins. We have reduced our FY2020 estimates by about 30% as we believe TVSM's aim of reaching the 10% margin mark is highly improbable given the muted industry volumes and increased competition. We have introduced FY2021 estimates in this note. We downgrade our recommendation on the stock to "Hold" from "Buy" with a revised PT of Rs 530.

Results Rs cr

Particulars	Q4FY19	Q4FY18	YoY %	Q3FY19	QoQ %
Total Income	4384.0	4007.2	9.4	4664.0	-6.0
Adj EBIDTA	308.1	295.2	4.4	375.7	-18.0
EBIDTA Margins (%)	7.0	7.4	(40) bps	8.1	(110) bps
Depreciation	103.1	94.4	9.3	101.2	1.8
Interest	24.7	18.3	35.3	16.7	47.9
Other Income	3.6	9.5	-62.4	0.7	450.8
PBT	183.9	192.1	-4.2	258.5	-28.8
Tax	50.1	26.4	89.5	80.1	-37.4
Adj PAT	133.8	165.6	-19.2	178.4	-25.0
EPS	2.8	3.5	-19.2	3.8	-25.0

Valuations Rs cr

Particulars	FY17	FY18	FY19E	FY20E	FY21E
Revenues (Rs cr)	12135.3	15175.4	18209.9	21318.8	24857.7
Growth (%)	7.9%	25.1%	20.0%	17.1%	16.6%
EBIDTA (Rs cr)	857.1	1175.0	1433.3	1596.4	1862.5
OPM (%)	7.1%	7.7%	7.9%	7.5%	7.5%
PAT (Rs cr)	558.1	662.6	670.1	745.0	899.8
Growth (%)	27.5%	18.7%	1.1%	11.2%	20.8%
FD EPS (Rs)	11.7	13.9	14.1	15.7	18.9
P/E (x)	41.8	35.2	34.8	31.3	25.9
P/B (x)	9.7	8.1	7.0	6.1	5.3
EV/EBIDTA (x)	27.2	19.7	16.3	14.4	12.1
RoE (%)	23.2%	23.0%	20.2%	19.6%	20.5%
RoCE (%)	20.2%	22.7%	23.5%	23.3%	24.9%

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