

Disappointing performance, subdued outlook...

Balkrishna Industries (BIL) reported weak Q4FY19 results. Standalone revenues for the quarter were at ₹ 1,351 crore (up 9.7% YoY) wherein volumes grew 2.5% YoY to 55,388 MT. EBITDA rose 8.3% YoY to ₹ 320 crore with attendant EBITDA margins at 23.7% (down 31 bps YoY & 127 bps QoQ), primarily tracking a 296 bps sequential increase in raw material costs as a percentage of sales although operating leverage benefit mitigated some of the adverse impact. Consequent PAT came in at ₹ 184.7 crore (down 4.6% YoY). The company declared a final dividend of ₹ 2/share for FY19.

Volume worries appear; growth prospects subdued!

BIL delivered healthy 12.5% CAGR volume growth in FY16-19P. Total tonnage increased from 1.5 lakh MT to 2.1 lakh MT during that time, driving BIL's emergence as a dominant player in the niche off-highway tyre space. With exports forming ~82% of revenues (India presence established meaningfully just three years back), BIL's fortunes remain tied majorly to demand conditions in the key markets of the Americas and Europe. During H2FY19, demand in the agri segment, in particular, was adversely impacted by a combination of trade war-led souring of sentiment, production cut at a large client and unusual weather patterns (including heat wave in Europe) in these geographies, with the management providing a cautious outlook, going forward, into FY20E as well. While it expects industry to suffer flat to negative growth for the year, BIL's volumes could rise 3-5% and modestly outperform peers. We build 6% volume CAGR for BIL in FY19-21E factoring in double digit India business growth on a small base and increasingly favourable mix (higher off highway share).

Capex execution on track; gradual margin benefits on cards!

Through backward integration plans (₹ 425 crore set aside for setting up a carbon black plant), BIL hopes to achieve ~100 bps of margin benefit upon full ramp up in FY21E. Combined with other greenfield and brownfield plans remaining on track and incrementally improving product mix, we estimate ~300 bps margin expansion to 28.1% over FY19-21E, in line with the company's longer term sustainable margin band of 25-28%.

Valuation & Outlook

We expect sales, EBITDA and PAT to grow at 7.8%, 14.3% & 6.5% CAGR, respectively, over FY19-21E. We feel that with modest growth on the horizon and gradual revival in margins, current high valuation multiples have room for some correction. We value the company at 16x its FY21E EPS of ₹ 46 to arrive at a target price of ₹ 740 per share. We maintain our **HOLD** rating on the stock. We derive comfort from BIL's debt free balance sheet, healthy double digit return ratios and ~8% CFO yield.

Key Financial Summary

Key Financials	FY17	FY18	FY19P	FY20E	FY21E	CAGR (FY19P-21E)
Net Sales	3,788.3	4,464.5	5,244.5	5,527.1	6,099.7	7.8%
EBITDA	1,131.9	1,106.7	1,311.1	1,479.6	1,714.3	14.3%
EBITDA Margins (%)	29.9	24.8	25.0	26.8	28.1	
Net Profit	715.1	739.3	782.0	778.6	887.7	6.5%
EPS (₹)	37.0	38.2	40.5	40.3	45.9	
P/E	21.0	20.3	19.2	19.3	16.9	
RoNW (%)	20.2	18.1	16.7	14.8	14.9	
RoCE (%)	23.0	22.4	20.4	18.8	19.5	

Source: ICICI Direct Research, Company



Particulars

Particular	Amount
Market Capitalization	₹ 15040.1 Crore
Total Debt (FY19P) (₹ Crore)	829.3
Cash & Investments (FY19P) (₹ Crore)	342.4
EV (₹ Crore)	15,527.0
52 week H/L (₹)	1467 / 741
Equity capital (₹ crore) (FY19P)	₹ 38.7 Crore
Face value (₹)	₹ 2

Key Highlights

- For Q4FY19, 2.5% YoY volume growth supports 9.7% topline growth with disappointment being witnessed on the margin front, which came in at 23.7%, down 127 bps QoQ
- A 3-5% volume guidance for FY20E in face of flat to negative industry outlook; sustainable margin levels seen at 25-28%
- Muted growth prospects offer scope for valuation multiple correction
- Maintain HOLD with revised target price of ₹ 740

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Exhibit 1: Variance Analysis

	Q4FY19	Q4FY19E	Q4FY18	YoY (%)	Q3FY19	QoQ (%)	Comments
Total Operating Income	1,351.0	1,317.1	1,231.8	9.7	1,205.6	12.1	Volume growth of 2.3% accompanied by currency benefit
Raw Material Expenses	659.5	592.9	573.7	15.0	552.9	19.3	
Employee Expenses	59.4	69.8	68.9	-13.8	68.0	-12.6	
Other expenses	312.1	312.1	293.6	6.3	283.8	10.0	
EBITDA	320.0	342.3	295.6	8.3	300.9	6.4	Gross margins contracted due to higher raw material prices but operating leverage benefit helped mitigate some damage
EBITDA Margin (%)	23.7	26.0	24.0	-31 bps	25.0	-127 bps	
Other Income	40.2	59.6	83.7	-52.0	1.0	4,039.2	
Depreciation	82.3	83.2	78.3	5.1	83.4	-1.3	
Interest	2.0	2.6	3.4	-40.8	2.0	2.0	
Tax	91.1	107.5	104.0	-12.3	71.8	26.9	
PAT	184.7	208.6	193.6	-4.6	144.7	27.7	Lower margins and other income drag profitability
EPS	9.6	10.8	10.0	-4.6	7.5	27.7	
Key Metrics							
Volume (MT)	55,388	52,652	54,002	2.6	46,780	18.4	
Realization (per/kg)	243.9	250.1	228.1	6.9	257.7	-5.4	ASP impacted by adverse mix and demand pressure
RM/Sales	48.8	45.0	46.6	224 bps	45.9	296 bps	
Gross Margin	51.2	55.0	53.4	-2.24	54.1	-2.96	
Employee Expenses	4.4	5.3	5.6	-1.20	5.6	-1.24	
Other expenses	23.1	23.7	23.8	-0.74	23.5	-0.44	

Source: Company, ICICI Direct Research

Exhibit 2: Change in estimates

(₹ Crore)	FY20E		FY21E		Comments
	Old	New	% Change	Introduced	
Revenue	5,633	5,527	-1.9	6,100	Marginally lower sales estimates keeping in mind muted demand outlook. Introduce FY21E numbers
EBITDA	1,648	1,480	-10.2	1,714	
EBITDA Margin (%)	29.3	26.8	-249 bps	28.1	Margin profile revised lower as demand conditions and pricing pressure weighs
PAT	963	779	-19.1	888	
EPS (₹)	49.8	40.3	-19.1	45.9	

Source: Company, ICICI Direct Research

Exhibit 3: Assumptions

	Current		Earlier		Introduced	Comments
	FY18	FY19P	FY20E	FY20E		
Capacity (MT)	300,000	300,000	300,000	300,000	300,000	
Sales volume (MT)	199,213	211,261	221,042	222,468	235,784	Estimate 6% volume CAGR over FY19-21E
Average realisation (₹/kg)	222	246	248	252	257	Modest realisation growth seen
Depreciation	311	333	387	377	427	

Source: Company, ICICI Direct Research

Conference Call Highlights

Management outlook/guidance and demand

- For the industry, the management expects flat to negative growth in FY20E, with BIL seen outperforming by delivering 3-5% growth
- Demand across product categories and geographies was impacted by trade war concerns and unusual weather patterns
- The India business is expected to grow at 10-15% CAGR over the next few years on account of the low base.

Sales, costs and margins

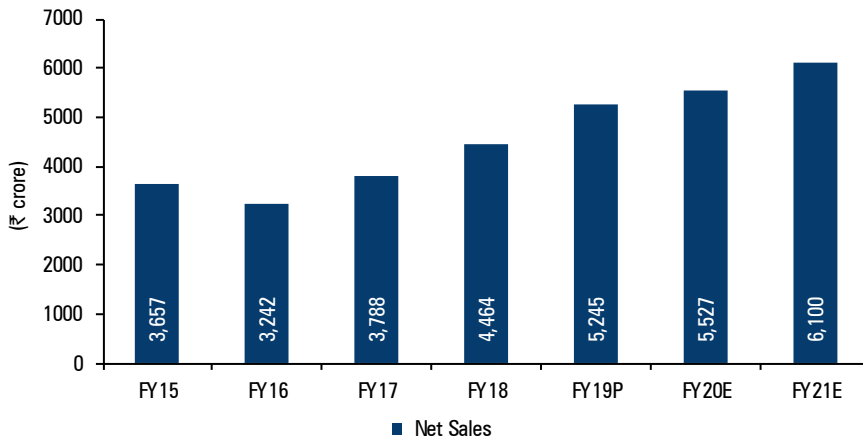
- Margin trajectory expected to be in the 25-28% range for FY20E
- Margins impacted during Q4FY19 due to lower realisations, sales promotion expenses and BIL being unable to pass on raw material prices
- ASP hit was on account of a decline in prices caused by demand pressure and adverse product mix. The company expects pricing pressure to continue for some more time
- Input costs have softened while material cost benefits should accrue to BIL in coming quarters
- The company's products are at 10-15% pricing gap when compared to peers
- Cost benefits on account of backward integration (carbon black plant) would be retained by the company and, thus, be margin accretive to the tune of ~100 bps from full ramp up in FY21E (~50-60 bps currently). Total capex for the plant is ₹ 425 crore of which ₹ 175 crore has been incurred already on Phase I (60,000 MT)

Others

- FY19 capex was at ₹ 757 crore with FY20E capex expected to be ~ ₹ 700 crore excluding the US greenfield capex of ~US\$80 million
- Geographical mix in FY19 was at 51% Europe, 17% Americas, 18% India (up 17% YoY) and balance others. Segment mix was at 61% agri, 36% off highway (OTR); channel mix was at 27% OEM, 71% replacement
- BIL's global market share as of FY19 was at 5% (overall); 8% in agri segment and ~2.5% in OTR segment

Financial story in charts

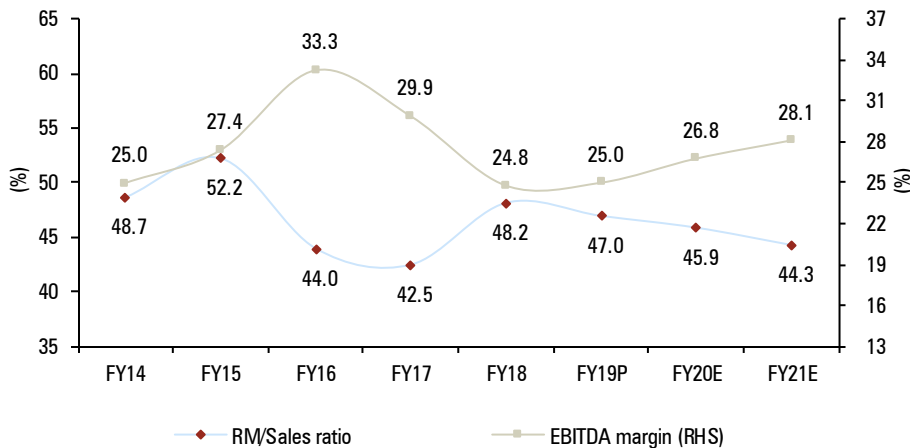
Exhibit 4: Topline trend



We expect sales to grow at a CAGR of 7.8% over FY19-21E led by 6% CAGR volume growth during this time

Source: Company, ICICI Direct Research

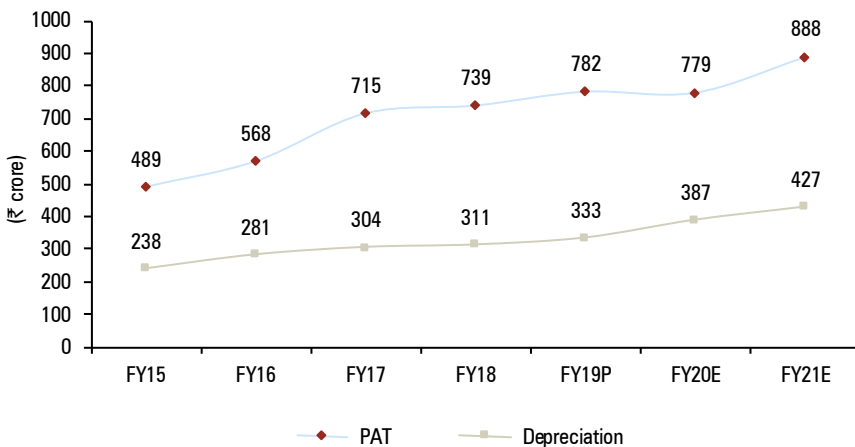
Exhibit 5: Input costs and EBITDA margin trend



EBITDA margins are expected to improve to 28.1% by FY21E owing to benefit of backward integration

Source: Company, ICICI Direct Research

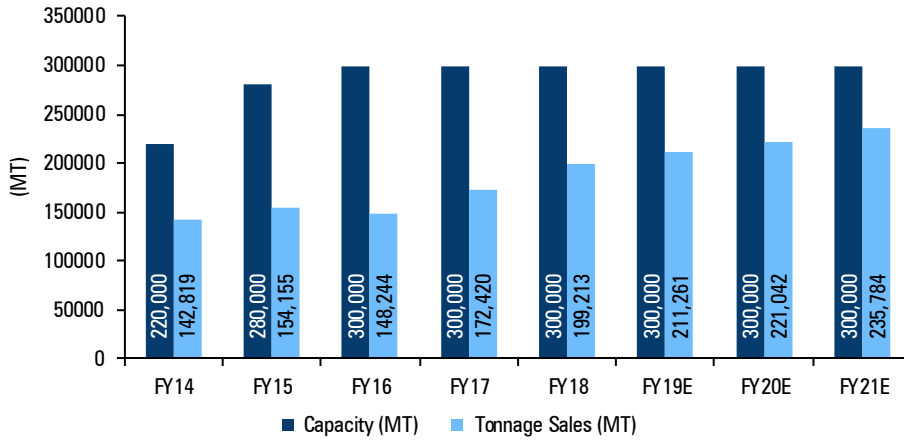
Exhibit 6: Profitability trend



We expect PAT to grow at 6.5% CAGR over FY19-21E to ₹ 888 crore

Source: Company, ICICI Direct Research

Exhibit 7: Capacity and utilisation levels



We expect volumes to grow at 6% CAGR over FY19-21E to 2.35 lakh MT

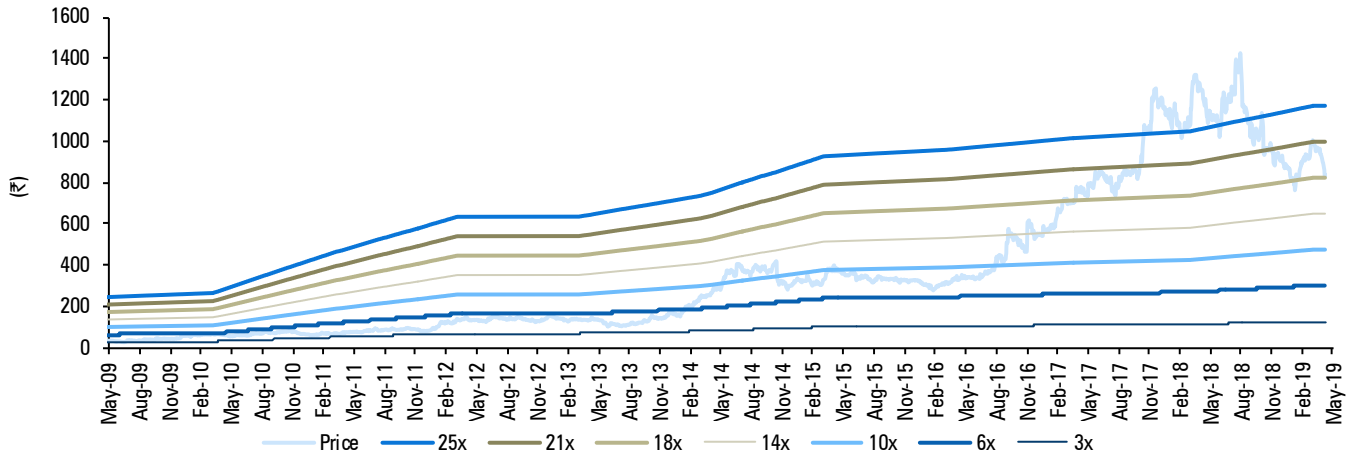
Source: Company, ICICI Direct Research

Exhibit 8: Valuation Summary

	Sales (₹ cr)	Growth (%)	EPS (₹)	Growth (%)	PE (x)	EV/EBITDA (x)	RoNW (%)	RoCE (%)
FY17	3,788	16.9	37.0	26.0	21.0	13.5	20.2	23.0
FY18	4,464	17.8	38.2	3.4	20.3	13.7	18.1	22.4
FY19P	5,245	17.5	40.5	5.8	19.2	11.8	16.7	20.4
FY20E	5,527	5.4	40.3	(0.4)	19.3	10.6	14.8	18.8
FY21E	6,100	10.4	45.9	14.0	16.9	9.0	14.9	19.5

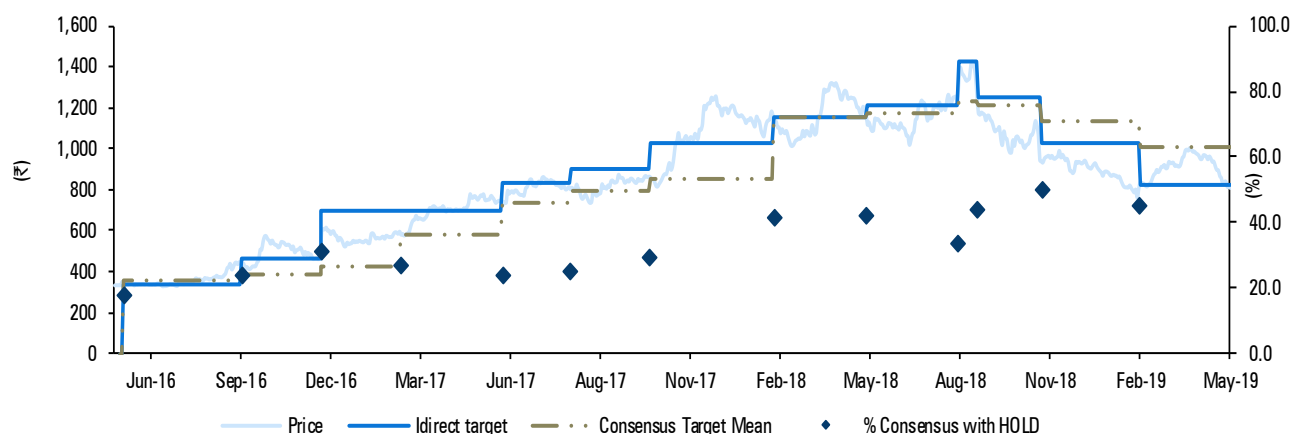
Source: Bloomberg, ICICI Direct Research

Exhibit 9: Currently trading at ~17x FY21E EPS, above its long term average multiple



Source: Reuters, ICICI Direct Research

Exhibit 10: Recommendation history vs. consensus



Source: Reuters, ICICI Direct Research

Exhibit 11: Top 10 shareholders

Rank	Name	Latest Filing Date	% O/S	Position (m)	Change (m)
1	Poddar (Rajiv Arvindkumar)	31-Mar-19	27.7	53.6	0.00
2	VKP Enterprises, L.L.P.	31-Mar-19	25.0	48.2	0.00
3	HDFC Asset Management Co., Ltd.	31-Mar-19	8.4	16.3	0.43
4	Poddar (Khushboo Rajiv)	31-Mar-19	3.9	7.6	0.00
5	Amansa Capital Pte Ltd.	31-Mar-19	1.7	3.4	0.31
6	Norges Bank Investment Management (NBIM)	31-Mar-19	1.5	3.0	0.01
7	HDFC Life Insurance Company Limited	31-Mar-19	1.4	2.8	0.35
8	Poddar (Rishabh S)	31-Mar-19	1.4	2.8	2.79
9	Poddar (Rishabh Sureshkumar)	31-Mar-19	1.4	2.8	0.00
10	UTI Asset Management Co. Ltd.	31-Mar-19	1.2	2.4	0.13

Source: Reuters, ICICI Direct Research

Exhibit 12: Recent activity

Buys			Sells		
Investor name	Value (\$mn)	Shares(mn)	Investor name	Value (\$mn)	Shares(mn)
Poddar (Rishabh S)	40.15	2.79	American Century Investment Management, Inc.	-16.32	-1.13
Caisse de Depot et Placement du Quebec	10.63	0.80	Mawer Investment Management Ltd.	-14.75	-1.11
HDFC Asset Management Co., Ltd.	6.17	0.43	Matthews International Capital Management, L.L.C.	-7.05	-0.53
HDFC Life Insurance Company Limited	5.00	0.35	HSBC Global Asset Management (Hong Kong) Limited	-4.90	-0.33
Amansa Capital Pte Ltd.	4.44	0.31	Union Investment Luxembourg S.A.	-2.21	-0.17

Source: Reuters, ICICI Direct Research

Exhibit 13: Shareholding pattern

(in %)	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19
Promoter	58.3	58.3	58.3	58.3	58.3
FII	17.7	15.8	14.3	12.6	11.5
DII	11.0	12.5	12.9	13.6	15.0
Others	13.1	13.5	14.5	15.5	15.2

Source: Company, ICICI Direct Research

Financial Summary

Exhibit 14: Profit and loss statement				
	₹ crore			
(Year-end March)	FY18	FY19P	FY20E	FY21E
Total operating Income	4,464.5	5,244.5	5,527.1	6,099.7
Growth (%)	17.8	17.5	5.4	10.4
Raw Material Expenses	2,149.9	2,462.8	2,535.9	2,701.8
Employee Expenses	248.8	263.6	281.9	311.1
Other Expenses	959.2	1,206.9	1,229.6	1,372.4
Total Operating Expenditure	3,357.8	3,933.4	4,047.4	4,385.3
EBITDA	1106.7	1311.1	1479.6	1714.3
Growth (%)	-2.2	18.5	12.9	15.9
Depreciation	311.3	332.6	386.9	427.0
Interest	13.1	9.8	10.3	10.8
Other Income	336.2	214.2	97.3	68.4
PBT	1118.5	1183.0	1179.7	1345.0
Total Tax	379.2	401.0	401.1	457.3
Reported PAT	739.3	782.0	778.6	887.7
Growth (%)	3.4	5.8	-0.4	14.0
EPS (₹)	38.2	40.5	40.3	45.9

Source: Company, ICICI Direct Research

Exhibit 15: Cash flow statement				
	₹ crore			
(Year-end March)	FY18	FY19P	FY20E	FY21E
Profit after Tax	739.3	782.0	778.6	887.7
Add: Depreciation	311.3	332.6	386.9	427.0
(Inc)/dec in Current Assets	-238.3	-141.3	-99.8	-177.8
Inc/(dec) in CL and Provisions	-276.6	-217.4	33.2	61.7
CF from operating activities	535.8	755.9	1098.9	1198.6
(Inc)/dec in Investments	-24.0	153.2	200.0	-100.0
(Inc)/dec in Fixed Assets	-277.7	-757.0	-1,000.0	-750.0
Others	119.1	-177.2	-11.2	-22.6
CF from investing activities	-182.6	-781.0	-811.2	-872.6
Inc/(dec) in loan funds	-149.3	211.3	-100.0	-100.0
Dividend paid & dividend tax	-128.0	-186.2	-186.2	-186.2
Others	-64.8	-12.1	0.0	0.0
CF from financing activities	-342.1	13.0	-286.2	-286.2
Net Cash flow	11.0	-12.1	1.5	39.8
Opening Cash	13.7	24.7	12.6	14.1
Closing Cash	24.7	12.6	14.1	53.9

Source: Company, ICICI Direct Research

Exhibit 16: Balance Sheet				
	₹ crore			
(Year-end March)	FY18	FY19P	FY20E	FY21E
Liabilities				
Equity Capital	38.7	38.7	38.7	38.7
Reserve and Surplus	4,056.3	4,640.0	5,232.4	5,933.9
Total Shareholders funds	4095.0	4678.7	5271.1	5972.6
Total Debt	618.0	829.3	729.3	629.3
Deferred Tax Liability	329.0	325.5	325.5	325.5
Minority Interest / Others	0.0	0.0	0.0	0.0
Total Liabilities	5063.6	5867.2	6359.6	6961.1
Assets				
Gross Block	3,693.8	3,983.3	5,168.8	6,118.8
Less: Acc Depreciation	898.8	1,231.3	1,618.2	2,045.2
Net Block	2795.0	2752.0	3550.5	4073.5
Capital WIP	118.0	585.4	400.0	200.0
Total Fixed Assets	2,913.0	3,337.4	3,950.5	4,273.5
Investments	1,358.8	1,157.0	1,160.3	960.3
Inventory	594.0	713.0	757.1	835.6
Debtors	502.0	568.1	605.7	668.5
Loans and Advances	102.0	61.9	65.2	71.9
Cash	24.7	12.6	14.1	53.9
Other current assets	165.5	277.0	273.3	288.0
Total Current Assets	1,388.2	1,632.6	1,715.4	1,917.9
Creditors	397.0	356.6	378.6	417.8
Provisions	7.0	7.4	7.9	8.7
Other current liabilities	687.6	376.0	198.6	209.3
Total Current Liabilities	1,091.6	740.0	585.1	635.8
Net Current Assets	296.6	892.6	1130.4	1282.1
Others	197.2	273.5	302.9	314.0
Application of Funds	5063.6	5867.2	6359.6	6961.1

Source: Company, ICICI Direct Research

Exhibit 17: Key ratios				
(Year-end March)	FY18	FY19P	FY20E	FY21E
Per share data (₹)				
EPS	38.2	40.5	40.3	45.9
Cash EPS	54.3	57.7	60.3	68.0
BV	211.8	242.0	272.7	309.0
DPS	5.5	8.0	8.0	8.0
Cash Per Share	1.3	0.7	0.7	2.8
Operating Ratios (%)				
EBITDA Margin	24.8	25.0	26.8	28.1
PBT / Net sales	17.8	18.7	19.8	21.1
PAT Margin	16.6	14.9	14.1	14.6
Inventory days	48.6	49.6	50.0	50.0
Debtor days	41.0	39.5	40.0	40.0
Creditor days	32.5	24.8	25.0	25.0
Return Ratios (%)				
RoE	18.1	16.7	14.8	14.9
RoCE	22.4	20.4	18.8	19.5
RoIC	17.7	20.6	19.4	20.5
Valuation Ratios (x)				
P/E	20.3	19.2	19.3	16.9
EV / EBITDA	13.7	11.8	10.6	9.0
EV / Net Sales	3.4	3.0	2.8	2.5
Market Cap / Sales	3.4	2.9	2.7	2.5
Price to Book Value	3.7	3.2	2.9	2.5
Solvency Ratios				
Debt/EBITDA	0.6	0.6	0.5	0.4
Debt / Equity	0.2	0.2	0.1	0.1
Current Ratio	3.7	4.4	4.4	4.4
Quick Ratio	2.2	2.5	2.5	2.5

Source: Company, ICICI Direct Research

Exhibit 18: ICICI Direct Coverage Universe (Auto & Auto Ancillary)

Sector / Company	CMP			M Cap (₹ Cr)	EPS (₹)			P/E (x)			EV/EBITDA (x)			RoCE (%)			RoE (%)		
	(₹)	TP(₹)	Rating		FY18	FY19E	FY20E	FY18	FY19E	FY20E	FY18	FY19E	FY20E	FY18	FY19E	FY20E	FY18	FY19E	FY20E
Amara Raja (AMARAJ)	637	590	Reduce	10888	27.6	28.3	30.0	22.8	22.3	21.0	12.0	11.0	10.2	23.3	21.2	20.2	16.0	14.5	13.9
Apollo Tyre (APOTYR)	183	180	Hold	10468	12.7	11.9	15.3	14.9	15.8	12.3	7.5	7.5	7.3	7.8	8.2	8.0	7.4	8.3	8.2
Ashok Leyland (ASHLEY)	89	85	Hold	26037	5.3	6.4	7.8	16.7	13.9	11.4	7.3	6.6	5.0	28.1	28.2	31.9	21.9	23.2	24.3
Bajaj Auto (BAAUTO)	2988	2800	Reduce	86477	140.6	161.6	165.6	21.7	18.9	18.4	15.2	14.3	13.0	22.9	21.0	20.0	21.5	19.9	19.7
Balkrishna Ind. (BALIND)	778	740	Hold	15040	40.5	40.3	45.9	19.2	19.3	16.9	11.8	10.6	9.0	20.4	18.8	19.5	16.7	18.8	19.5
Bharat Forge (BHAFOR)	471	535	Buy	32590	16.2	23.6	27.6	29.0	19.9	17.1	13.9	11.5	9.9	18.2	21.1	23.3	17.3	20.8	21.4
Bosch (MICO)	17520	17565	Hold	53472	449.1	545.6	622.9	40.4	33.2	29.1	25.1	22.4	18.9	14.4	14.9	15.2	21.4	22.2	22.6
Eicher Motors (EICMOT)	20870	19000	Hold	56892	718.9	808.1	912.5	26.1	23.2	20.5	16.8	16.6	14.3	39.1	32.5	29.6	29.9	24.8	22.8
Escorts (ESCORT)	600	600	Hold	7355	28.1	39.6	43.1	23.5	16.7	15.3	13.1	10.6	8.9	18.8	19.6	19.8	13.5	16.0	15.0
Exide Industries (EXIIND)	212	200	Reduce	17982	8.2	9.1	10.1	27.3	21.7	21.2	14.5	12.7	11.2	19.0	18.4	18.7	12.9	12.9	12.9
Hero Moto (HERHON)	2699	2700	Hold	53897	185.1	169.5	171.2	13.6	14.8	14.7	8.2	9.2	8.7	42.4	37.1	34.2	31.4	26.3	24.1
JK Tyre & Ind (JKIND)	80	100	Buy	1811	2.9	7.8	8.2	27.5	10.3	9.8	9.3	6.3	6.2	7.8	10.9	10.7	3.7	10.3	9.8
Mahindra CIE (MAHAUT)	227	275	Buy	8589	13.2	15.1	17.4	17.1	14.9	12.9	8.9	7.6	6.5	12.4	11.8	12.0	13.2	13.9	14.9
Maruti Suzuki (MARUTI)	7033	5815	Sell	212460	255.6	248.3	256.3	27.0	27.8	26.9	14.5	15.8	14.4	21.1	16.3	15.9	18.5	16.3	15.2
Motherson (MOTSUM)	122	125	Hold	38622	5.1	5.3	7.0	25.7	24.5	18.6	9.3	8.5	6.8	16.3	15.2	18.0	17.4	15.7	18.0
Tata Motors (TELCO)	180	145	Hold	53239	26.8	-83.4	16.6	5.6	NA	9.1	2.4	3.3	2.6	9.1	5.1	9.9	10.3	5.9	12.6
Wabco India (WABTVS)	6115	7000	Hold	11599	143.8	172.2	212.3	46.9	39.2	31.8	30.4	26.2	20.8	17.9	17.8	18.2	25.1	25.7	26.0

Source: Reuters, ICICI Direct Research

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Buy: >15%

Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



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