Stock Update

Powered by the Sharekhan 3R Research Philosophy

TVS Motors Limited

Shifting to a speedy gear

Automobiles	Sharekhan code: TVSMOTOR	Result Update

Summary

- TVS Motors Limited's (TVSM) Q2FY2021 results were higher than our as well as consensus estimates, driven by better-than-expected margin performance.
- TVSM is witnessing strong recovery in domestic demand with retail sales turning positive in the initial festive days. Export demand has picked up strongly with strong double-digit growth reported in September 2020.
- Margins improvement is expected to sustain given cost control measures and operating leverage. TVSM is expected to remain the fastest growing two-wheeler (2W) company with strong 20% earnings CAGR over FY2020-FY2023.
- We retain our Buy rating on the stock with an unchanged price target (PT) of Rs. 470.

TVS Motors Limited's (TVSM) Q2FY2021 results were higher than our as well as consensus estimates, driven by better-than-expected margin performance. Overall revenue grew by 6% y-o-y, driven by an 8% y-o-y increase in realisation due to price hikes on account of BS6 norms. Volumes dropped marginally by 2% y-o-y. Operating profit margin (OPM) stood at 9.3%, highest in the past decade and beating our expectation of 8.5%. Margin improved on a y-o-y basis despite cost pressures on account of BS6 norms. Cost-control measures led to margin improvement. Demand in domestic market has improved, driven by strong rural sentiments and increased preference for personal transport. Initial festive sales have turned positive with marginal growth on a y-o-y basis. TVSM expects to continue outpacing the industry, driven by new product launches and enhancing distribution network. Exports have picked up strongly reporting 19% y-o-y growth in September 2020, driven by recovery in key markets and tapping of new geographies. Margin improvement is expected to sustain given cost-control initiatives and benefits of operating leverage. TVSM is expected to remain the fastest growing two-wheeler (2W) company with strong 20% earnings CAGR over FY2020-FY2023.

Key positives

- Domestic demand at the retail level turned positive with the company witnessing marginal growth in the initial festive season of Navratri and Dussehra.
- OPM at 9.3% in Q2FY2021 was the highest ever in the past decade and was better than estimates, primarily driven by cost-control measures.

Key negatives

- The government has discontinued MEIS export incentives with effect from September 2020, which would impact export profitability.

Our Call

Valuations: Retain Buy with an unchanged PT of Rs. 470: TVSM is witnessing strong recovery in domestic demand with retail sales turning positive in the initial festive days. Export demand has picked up strongly with strong double-digit growth reported in September 2020. We expect strong recovery from FY2022, driven by normalisation of economic activity. Margins are expected to improve driven by operating leverage and cost-control measures. We have marginally raised our earnings estimates for FY2021 and FY2022 due to better-than-expected results in Q2FY2021.We have also introduced FY2023 estimates in this note. The stock is currently trading at 16.4x its FY2023 core earnings compared to long-term historical average of 20x. We retain our Buy rating on the stock with an unchanged price target (PT) of Rs. 470.

Key Risks

TVS Group is considering levying royalty on group companies. TVSM is the flagship company of the group and any levy would adversely impact margins. Prolonged slowdown in volumes due to COVID-19 could impact performance.

Valuations Rs cr

Particulars	FY19	FY20	FY21E	FY22E	FY23E
Revenues (Rs. cr)	18209.9	16423.3	14994.3	18469.1	21451.9
Growth (%)	20.0	-9.8	-8.7	23.2	16.2
EBIDTA (Rs. cr)	1433.3	1345.9	1177.3	1781.3	2110.4
OPM (%)	7.9%	8.2%	7.9%	9.6%	9.8%
PAT (Rs. cr)	670.1	624.6	408.7	863.1	1072.2
Growth (%)	1.1	-6.8	-34.6	111.2	24.2
FD EPS (Rs.)	14.1	13.1	8.6	18.2	22.6
P/E* (x)	26.2	28.1	43.0	20.4	16.4
P/B* (x)	5.3	4.9	4.5	3.9	3.3
EV/EBIDTA* (x)	14.9	16.0	18.5	11.9	9.7
RoE (%)	20.0	17.3	10.5	19.1	20.4
RoCE (%)	20.8	15.0	11.9	19.9	22.3

*Source: Company; Sharekhan estimates; * Based on core business*

3R MATRIX

	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)	✓		

\+ Positive = Neutral - Negative

Reco/View	Change
Reco: **Buy**	↔
CMP: **Rs. 422**	
Price Target: **Rs. 470**	↔

↑ Upgrade ↔ Maintain ↓ Downgrade

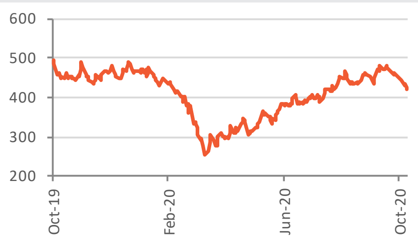
Company details

Market cap:	Rs. 20,060 cr
52-week high/low:	Rs. 503 / 240
NSE volume: (No of shares)	19.04 lakh
BSE code:	532343
NSE code:	TVSMOTOR
Free float: (No of shares)	20.2 cr

Shareholding (%)

Promoters	19.9
FII	34.2
DII	24.6
Others	21.3

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-9.9	5.1	28.7	-14.7
Relative to Sensex	-14.3	-0.3	10.8	-13.7

Sharekhan Research, Bloomberg

Better-than-expected results: TVSM's results were ahead of our as well as consensus expectations, driven by better-than-expected margin performance. Revenue grew by 6% y-o-y. While volumes were down marginally by 2% y-o-y, realisation per vehicle grew by 8% y-o-y (marginally lower than our expectation of 11% growth), driven by price hikes on account of BS6 emission norms. OPM improved by 50 bps y-o-y to 9.3%, which is better than our estimate of 8.5%. Cost-control initiatives in the form of material cost reduction, overall productivity improvement, and controlling fixed costs led to margin outperformance. EBIDTA at Rs. 430 crore grew by 13% y-o-y and was better than our estimate of Rs. 405 crore. TVSM's net profit grew by 10% y-o-y to Rs. 196 crore and was ahead of our estimates of Rs. 181 crore.

Demand improving with marginal growth in the initial festive period; Export growth strong: TVSM stated that demand has been improving on m-o-m basis in both domestic as well as export markets. Opening up of the economy by the government coupled with increasing preference for personal transport is leading to volume recovery. Moreover, robust rural sentiments are driving demand. TVSM stated that domestic demand (75% of volumes) reported marginal growth in the initial festive period of Navratri-Dussehra at the retail level. TVSM is positive about the festive season going ahead. Export volumes have picked up strongly, reporting 19% y-o-y growth in September 2020. Initiatives such as new launches and tapping of new markets are enabling TVSM to report strong export sales.

Margin improvement to sustain: TVSM's margins improved by 50 bps y-o-y to 9.3% in Q2FY2021 despite marginal drop in volumes and cost pressures on account of BS6 emission norms. TVSM's cost control-measures enabled margin improvement. TVSM has been undertaking measures such as better vendor negotiations, increased localisation, fixed cost control, and overall operational efficiency measures to reduce costs. With volumes staging strong recovery in FY2022, driven by normalisation of business activity, TVSM expects margin improvement to sustain. We have factored 160 bps margin improvement over the next three years.

Conference call highlights

- **Domestic Demand:** TVSM stated that domestic demand has improved driven by strong rural sentiments and increased preference for personal transportation. TVSM stated that retail demand in the initial festive season of Navratri-Dussehra has been marginally positive as against a decline in September 2020. The company is positive on the festive demand going ahead. TVSM also stated that urban demand is coming back with opening up of urban areas.
- **Export demand strong:** TVSM stated that demand traction is strong in exports. Exports reported strong 19% y-o-y growth in September 2020 and the company expects robust demand going ahead.
- **Indonesia subsidiary:** TVSM stated that the Indonesian subsidiary has turned around, reporting marginal profit at PBT level in Q2FY2021.
- **Price increases:** TVSM undertook price increase of about 1% in October 2020 to offset rising input costs.
- **Export incentives:** TVSM stated that export incentives under the current MEIS scheme have been discontinued by the government w.e.f. September 2020. TVSM stated that the government is working on a new scheme to replace MEIS, which is likely to come into force from January 2021.
- **Capex:** TVSM has increased FY2021 capex guidance from Rs. 300 crore to Rs. 500 crore. Capex would be directed towards new product development and increasing capacity in export markets.
- **Financing:** TVSM stated that financing has been improving on a sequential basis and has reached 46% in Q2FY2021. While financing is down on a y-o-y basis, it is expected to pick up. The share of captive subsidiary in overall financing is at 50%.
- **Increased cash flow in H2FY2021:** TVSM's cash flow from operations increased to Rs. 1,450 crore in H2FY2021 as against Rs. 543 crore in H1FY2021. Reduction in working capital led to improved cash flow for the company.

Results Rs cr

Particulars	Q2FY21	Q2FY20	%YoY	Q1FY21	%QoQ
Total Income	4605.5	4347.8	5.9	1431.7	221.7
Adj. EBIDTA	430.1	382.0	12.6	-48.8	NA
EBIDTA Margin (%)	9.3	8.8	50 bps	-3.4	1270 bps
Depreciation	133.1	124.1	7.3	91.1	46.1
Interest	40.7	28.5	42.9	52.3	-22.1
Other Income	11.1	4.9	126.3	2.6	328.2
PBT	267.4	234.3	14.1	-189.6	NA
Tax	71.2	55.3	28.6	-50.5	NA
Adj. PAT	196.3	179.0	9.7	-139.1	NA
EPS (Rs.)	4.1	3.8	9.7	-2.9	NA

Source: Company; Sharekhan Research

Outlook and Valuation

■ **Sector Outlook - Retail sales continue to improve; Expect strong recovery from FY2022**

2W demand has been improving on m-o-m basis and the trend has continued in the initial festive days of Navratri and Dussehra. The decline in retail demand has narrowed to 5%-6% in the initial festive season of Navratri and Dussehra as compared to 12% drop in September 2020. Strong rural sentiments due to higher kharif sowing and government reform measures along with increased preference for personal transport is leading to improvement in volumes. Demand is expected to improve further as we approach the main festive season of Diwali. We expect strong recovery from FY2022, driven by normalisation of economic activity and pent-up demand (the industry has been in downcycle for the past seven to eight quarters).

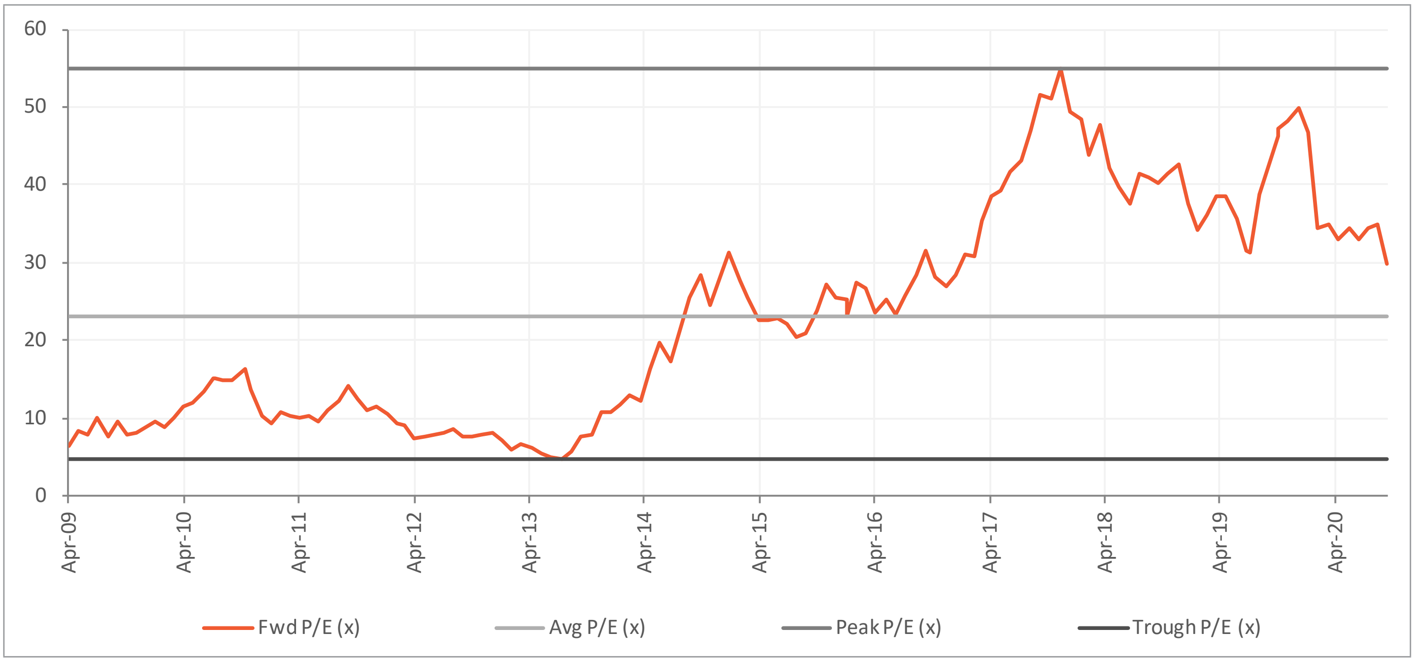
■ **Company outlook - Fastest earnings growing company in the 2W space**

TVSM has gained market share in the 2W industry on the success of new launches and enhancing distribution presence. TVSM's market share has improved from 11.8% in FY2014 to about 13.8% in FY2020. Moreover, the company has been able to strengthen its presence in the high realisation scooters and motorcycles category with share of mopeds coming down from 41% in FY2014 to 26% in FY2020. Cost-control measures, better vendor negotiations, and operating leverage benefits due to better scale have resulted in TVSM emerging as the fastest 2W earnings company with strong 15% earnings CAGR over FY2014 to FY2020. TVSM is expected to remain the fastest growing company going ahead.

■ **Valuation - Retain Buy with unchanged PT of Rs. 470**

TVSM is witnessing strong recovery in domestic demand with retail sales turning positive in the initial festive days. Export demand has picked up strongly with strong double-digit growth reported in September 2020. We expect strong recovery from FY2022, driven by normalisation of economic activity. Margins are expected to improve, driven by operating leverage and cost-control measures. We have marginally raised our earnings estimates for FY2021 and FY2022 due to better-than-expected results in Q2FY2021. We have also introduced FY2023 estimates in this note. The stock is currently trading at 16.4x its FY2023 core earnings compared to long-term historical average of 20x. We retain our Buy rating on the stock with an unchanged PT of Rs. 470.

One-year forward P/E (x) band



Source: Sharekhan Research

About company

TVSM is the flagship company of TVS Group and is the third largest 2W manufacturer in the country. TVSM is the only manufacturer present across all three categories of 2W, viz. motorcycles, scooters, and mopeds. Motorcycles and scooters contribute 40% and 33% of volumes, respectively, while mopeds constitute 23%. TVSM also manufactures three-wheelers (3W, 5% of overall volumes) mainly for the export market. TVSM has been focusing on growing exports with the overseas market contributing about 25% of overall volumes.

Investment theme

Demand in the domestic market has improved, driven by strong rural sentiments and increased preference for personal transport. Initial festive sales have turned positive with marginal growth on a y-o-y basis. TVSM expects to continue outpacing the industry, driven by new product launches and enhancing distribution network. Exports have picked up strongly, reporting 19% y-o-y growth in September 2020, driven by recovery in key markets and tapping of new geographies. Margin improvement is expected to sustain given cost-control initiatives and benefits of operating leverage. TVSM is expected to remain the fastest growing 2W company with strong 20% earnings CAGR over FY2020-FY2023.

Key Risks

- TVS Group is considering levying royalty on group companies. TVSM is the flagship company of the group and any levy would adversely impact margins.
- Prolonged slowdown in volumes due to COVID-19 could impact performance.

Additional Data

Key management personnel

Venu Srinivasan	Chairman and Managing Director
Sudarshan Venu	Joint Managing Director
K.N. Radhakrishnan	Director and CEO
K. Gopala Desikan	CFO

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Sundaram Clayton Ltd.	57.4%
2	ICICI Prudential Asset Management	7.8%
3	Jwalamukhi Investment Holdings	5.7%
4	Reliance Capital Trustee Co. Ltd.	3.5%
5	Cartica Capital Ltd.	2.0%
6	Life Insurance Corp of India	2.0%
7	Franklin Resources Inc.	1.9%
8	Mirae Asset Global Investments Co.	1.8%
9	Tree Line Asia Master Fund	1.4%
10	Invesco Asset Management India Pvt. Ltd.	0.8%

Source: Bloomberg

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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