

CMP: ₹ 360

Target: ₹ 425 (18%)

Target Period: 12 months

May 29, 2020

BUY

Covid may offer opportunity, robust capital efficiency

Tube Investments of India (TII), part of renowned Murugappa Group, has a diversified manufacturing presence across segments of cycles & accessories, engineering (precision steel tubes, strips), metal forming (door frames, fine blanking products, chains), gears & gearboxes. These four divisions contributed ~16%, ~46%, ~33%, ~5%, respectively, to gross consolidated revenue in FY20P. On overall basis, TII derives ~50% of revenues from auto space and remaining ~50% from non-auto space, including Railways. It is among top few players in each of its business divisions, including special gears through listed subsidiary Shanthi Gears. TII has, over the years, shown continuous improvement in capital efficiency (FY20P RoCE: ~18%) and cash generation (FY20P CFO: ₹ 600 crore, 10% yield).

Triggers

Sole credible listed play in domestic bicycle space

With global economies beginning to reopen post easing of Covid-19 related quarantine restrictions, **some western countries are seeing increase in demand for bicycles owing to rising early preference for personal mobility over public transport. The same trend could gain traction in India as curbs get lifted, with the affordability quotient of modes (~₹ 3,300/unit industry ASP) and heightened awareness around personal health and social distancing, putting the industry on a solid footing to capture such an opportunity.** In our view, TII, as the **sole credible listed bicycle player within the domestic bicycle space, would benefit.** The Indian bicycle industry (second largest in the world after China) is estimated to be worth ~₹ 5,500 crore in size (FY19), with output of ~1.65 crore units. Standard bicycles form 39% of the overall industry with specials (including premium) constituting 61%. TII is the second player domestically (23% overall market share, 28% specials market share as of FY19) and serves the space through popular brands like **Hercules, BSA, Ladybird and Roadeo.** Its distribution footprint covered 10,000+ touchpoints and 239 retail stores as in FY19. Moreover, **TII has restructured operations in this division with segmental RoCE improving to 12.8% in FY20P vs. 0.2% in FY18.**

Continued cost focus, impressive return ratios, cash generation

During FY20P, consolidated revenues fell 18% in a weak year for the entire auto space. Contrary to peers, however, margins, profitability showed resilience (EBITDA margins up 280 bps YoY to 12.2%, PAT up 26%). TII is reducing dependence on government cycle orders (suffer from competitive pricing) and increasing retail sales alongside improving efficiencies in other divisions. Hence, its **consolidated RoCE improved from ~13% in FY18 to ~18% in FY20P.** It has also constantly focussed on cash generation through operational efficiencies as well as tight control over working capital cycle (~30 days). **It generated a CFO of ~₹ 600 crore (CFO yield at ~10%) and FCF of ~₹ 380 crore (FCF yield at ~6%) in FY20P.** Consequent to robust cash flow generation, the company has been retiring debt with gross debt as of FY20P at ~₹ 433 crore vs. ~₹ 850 crore in FY17.

Valuation & Outlook

Going forward, with TII being the sole credible bicycle player in the listed space, its strong focus on return ratios matrix (RoE, RoCE at ~18%) and cash generation ability (CFO yield at ~10%, FCF yield at ~6%), lead us to build a positive stance on the company. Consequently, **we assign BUY rating on TII with a target price of ₹ 425, valuing it at 26x P/E on FY20P EPS of ₹ 16.3/share. Key risk** to our call is more than expected delay in demand recovery in domestic automobile place and certain portion of TII's topline susceptible to EV risk.



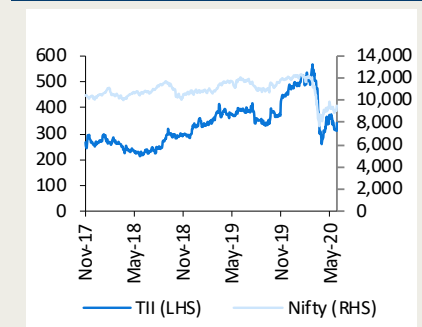
Particulars

Particulars	Amount
Market capitalisation (₹ crore)	6,750.0
Debt (FY20P, ₹ crore)	432.9
Cash & Inv. (FY20P, ₹ crore)	180.0
EV (₹ crore)	7,002.9
52 Week High/Low (₹)	577 / 255
Equity capital (₹ crore)	18.8
Face value (₹)	1.0
Promoter holding (%)	48.0
D II holding (%)	19.2
F II holding (%)	17.8

Key Highlights

- Part of the reputed Murugappa Group; sole credible listed play on bicycle opportunity in India (16% of consol sales)
- Margins, return ratios to continue to benefit from cost focus and other strategic initiatives
- Assign BUY with target price of ₹ 425 i.e. 26x FY20P EPS of ₹ 16.3/share

Price Chart



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Key Financial Summary

P&L Account (₹ crore)	FY17	FY18	FY19	FY20P
Sales	4,493.0	5,000.0	5,774.8	4,750.4
EBITDA	406.1	370.5	538.7	578.5
EBITDA margin (%)	9.0	7.4	9.3	12.2
PAT	167.6	147.4	240.4	306.0
EPS (₹)	8.9	7.9	12.8	16.3
Balance Sheet (₹ crore)				
Equity	18.7	18.8	18.8	18.8
Net Worth	1,187.6	1,272.3	1,475.4	1,734.0
Debt	850.6	776.4	607.9	432.9
Debt: Equity (x)	0.7	0.6	0.4	0.2
Return Ratios (%)				
RoE	14.1	11.6	16.3	17.6
RoCE	14.0	12.8	19.9	18.4
Valuations (x)				
P/E	40.2	45.8	28.1	22.1
EV/EBITDA	18.4	19.9	13.4	12.1
P/B	5.7	5.3	4.6	3.9

Source: Capitaline, ICICI Direct Research

Exhibit 1: Segmental financials (Revenue, EBIT margins, RoCE)

Sales (₹ crore)	Q4FY20	Q4FY19	YoY (%)	Q3FY20	QoQ (%)	FY20	FY19
Cycle and accessories	129	251	-49%	148	-13%	781	1,240
Metal Products	356	423	-16%	422	-16%	1,635	1,608
Engineering	545	659	-17%	502	9%	2,258	2,896
Industrial Gears	42	58	-29%	58	-28%	242	241
Total	1,031	1,347	-23%	1,087	-5%	4,750	5,773

EBIT (₹ crore)							
Cycle and accessories	5.2	-6.5	-180%	0.2	2376%	22.4	14.4
Metal Products	9.6	30.0	-68%	31.0	-69%	116.0	125.0
Engineering	75.0	65.0	15%	60.0	25%	264.0	254.0
Industrial Gears	0.5	7.7	-94%	7.7	-94%	32.7	42.5

EBIT Margins (%)							
Cycle	4.0%	-2.6%		0.1%		2.9%	1.2%
Metal Products	2.7%	7.1%		7.3%		7.1%	7.8%
Engineering	13.8%	9.9%		12.0%		11.7%	8.8%
Industrial Gears	1.2%	13.2%		13.3%		13.5%	17.6%

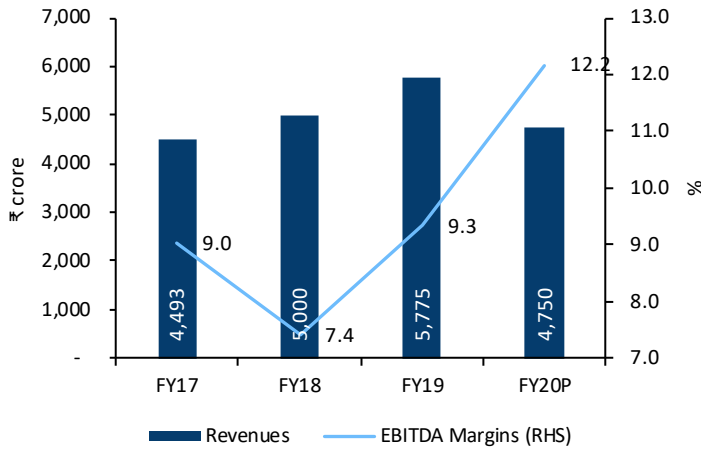
Capital Employed (₹ crore)							
Cycle and accessories	175	220		184		175	220
Metal Products	622	605		635		622	605
Engineering	639	687		619		639	687
Industrial Gears	225	297		244		225	297

RoCE (%)							
Cycle and accessories	11.9%	-11.8%		0.5%		12.8%	6.5%
Metal Products	6.2%	19.8%		19.5%		18.7%	20.7%
Engineering	46.9%	37.8%		38.8%		41.3%	37.0%
Industrial Gears	0.9%	10.4%		12.6%		14.5%	14.3%

Source: Company, ICICI Direct Research

Story in charts

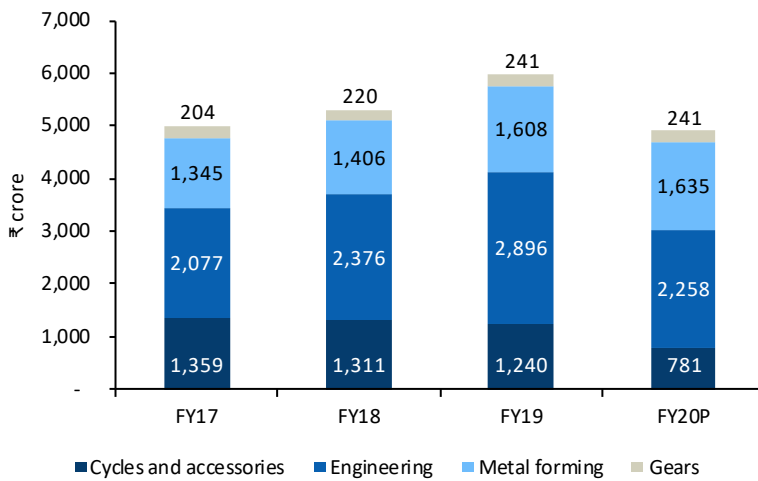
Exhibit 2: Trend in revenues and margins



An 18% YoY revenue decline during the past year has reduced FY17-20P CAGR to 1.9%. EBITDA margins, however, have grown from 9% to 12.2% in this time frame aided by improving product mix, better operating efficiencies and cost initiatives

Source: Company, ICICI Direct Research

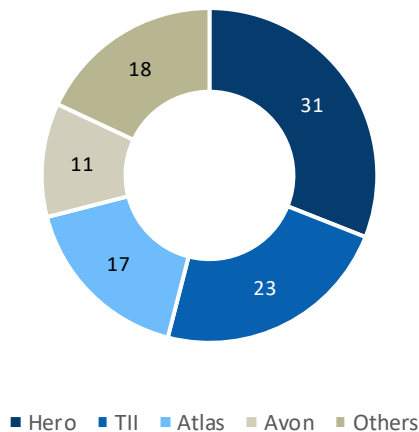
Exhibit 3: Segment wise breakup of gross consolidated revenues



As of FY20P, engineering division formed 46% of gross consolidated sales while metal forming, cycles and accessories and gears formed 33%, 16% and 5%, respectively

Source: Company, ICICI Direct Research

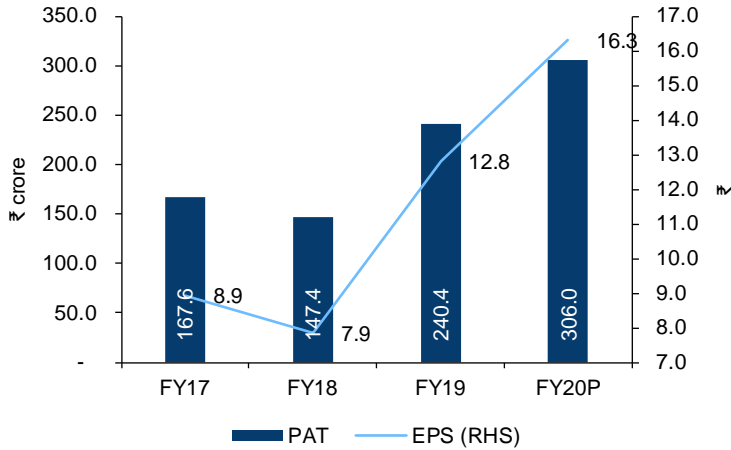
Exhibit 4: FY19 domestic cycle industry market share (%)



TII was the second largest player in the domestic bicycle industry as of FY19 with 23% overall market share. It is the only credible listed player in the space.

Source: Company, ICICI Direct Research

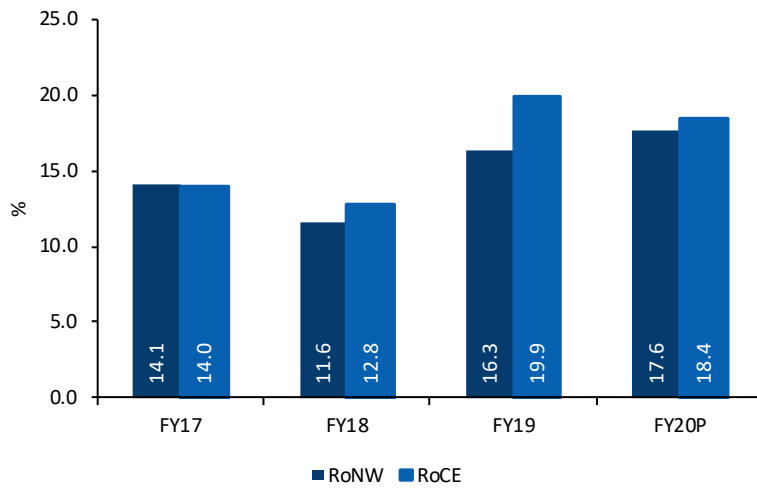
Exhibit 5: PAT and EPS trend



PAT levels have improved considerably amid bettering of margin profile and reduction in debt levels at TII

Source: Company, ICICI Direct Research

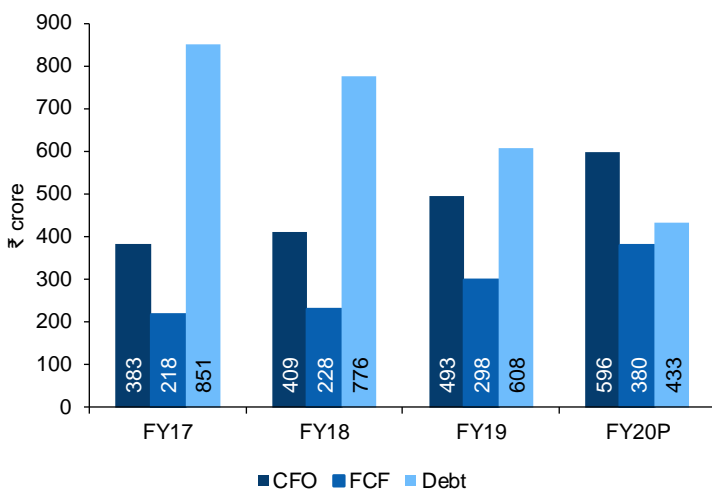
Exhibit 6: Trend in return ratios



The company has improved its return ratio profile across segments amid >2x asset turns and ~12% margins accompanied by sharp lowering of debt on books

Source: Company, ICICI Direct Research

Exhibit 7: CFO, FCF and debt levels



Strong CFO and FCF generation has been a hallmark of TII over the years, with present FCF yield at ~6%

Source: Company, ICICI Direct Research

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Buy: >15%

Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



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