

Resilient volume outlook; margin topped out

- CEAT posted impressive numbers in Q3FY21 driven by 1) strong revenue traction in replacement market (+35% YoY) led by pick up in fleet utilization, market share gain in PCR and TBR segment and ban on import of Chinese tyres; 2) better product mix (high proportion of replacement volume) and 3) cost cutting measures.
- Revenue grew 26% YoY and EBITDA jumped 79% YoY to Rs 3.28bn. EBITDA margin stood at 14.8% (+435bps YoY, flat QoQ). The management expects RM cost to increase by 10% in 4Q, the company has taken cumulative price hike of ~3% recently while another 3% price hike is required further to mitigate the impact of increase in input cost.
- We expect strong revenue growth to continue in the coming quarter led by recovery in OEMs volume and sustainable replacement demand while margin to see contraction due to 1) sharp up move in natural rubber prices (up ~25% QoQ) and 2) normalization of product mix (likely increase in share of OEMs) and increase in employee cost due to commissioning of new capacity and incentive programs offered.
- Gross debt at the end of Q3FY21 was Rs 15.56bn (decreased by Rs 3.73bn on a sequential basis) due to efficient working capital management. The company has incurred capex ~Rs 3.5bn in 9MFY21. For FY21, CEAT has given a capex guidance of Rs 6bn and Rs 7bn for FY22 and FY23 each.
- Out of the overall planned capex of Rs 40bn, CEAT has incurred a capex of Rs 22bn till date (including Specialty Business capex). With major capex behind, CEAT is likely to start generating FCF from FY23E which will help to reduce its Debt/EBITDA from 2.4x in FY21 to 1.9x in FY23E.
- We maintain our positive view on the stock, premised on 1) uptick in OEMs volume and market share gain in PCR and TBR segments; 2) continued replacement market growth; 3) Strong FCF generation from FY23 onwards and 4) cost optimization measures. We increase our EPS estimates by 23/16% for FY22/23E and maintain an Accumulate rating with TP of Rs 1,444 (based on 15x FY23E Cons EPS).

Q3FY21 Result (Rs Mn)

Particulars	Q3FY21	Q3FY20	YoY (%)	Q2FY21	QoQ (%)
Revenue	22,213	17,618	26.1	19,785	12.3
Total Expense	18,936	15,786	20.0	16,860	12.3
EBITDA	3,277	1,832	78.8	2,925	12.0
Depreciation	873	705	23.8	839	4.0
EBIT	2,404	1,127	113.3	2,085	15.3
Other Income	41	36	13.4	38	7.4
Interest	419	380	10.2	450	(6.9)
EBT	1,903	780	143.9	1,674	13.7
Tax	696	301	131.0	(15)	(4680.9)
RPAT	1,323	525	152.1	1,822	(27.4)
APAT	1,446	528	174.1	1,822	(20.6)
			(bps)		(bps)
Gross Margin (%)	45.5	43.0	257	46.5	(92)
EBITDA Margin (%)	14.8	10.4	435	14.8	(3)
NPM (%)	6.0	3.0	298	9.2	(325)
Tax Rate (%)	36.6	38.6	(205)	(0.9)	3750
EBIT Margin (%)	10.8	6.4	443	10.5	28

CMP	Rs 1,310
Target / Upside	Rs 1,444 / 10%
NIFTY	14,645

Scrip Details

Equity / FV	Rs 405mn / Rs 10
Market Cap	Rs 53bn
	USD 726mn
52-week High/Low	Rs 1,353/ 600
Avg. Volume (no)	3,26,372
Bloom Code	CEAT IN

Price Performance	1M	3M	12M
Absolute (%)	18	27	30
Rel to NIFTY (%)	12	4	10

Shareholding Pattern

	Jun'20	Sep'20	Dec'20
Promoters	46.7	46.8	46.8
MF/Banks/FIs	9.6	16.2	17.1
FIIs	31.7	23.7	24.2
Public / Others	12.0	13.3	11.9

Valuation (x)

	FY21E	FY22E	FY23E
P/E	14.2	16.9	13.5
EV/EBITDA	7.6	8.3	7.2
ROE (%)	12.2	9.4	10.9
RoACE (%)	9.7	7.9	8.8

Estimates (Rs mn)

	FY21E	FY22E	FY23E
Revenue	72,253	79,484	86,377
EBITDA	9,491	8,926	9,924
PAT	3,740	3,135	3,913
EPS (Rs.)	92.5	77.5	96.7

Analyst: Abhishek Jain
 Tel: +9122 40969739
 E-mail: abhishekj@dolatcapital.com

Associate: Ketul Dalal
 Tel: +91 22 4096 9770
 E-mail: ketuld@dolatcapital.com

New Capacities - Next leg of growth driver

Given the new capacities (TBR/PCR/2W) in place, CEAT is now well positioned to benefit from the revival of the OEMs and replacement volume. Commissioning of 2W brownfield facility at Nagpur in August'20, Chennai Greenfield facility for PCR and 2W tyres and ramp up of TBR at the Halol plant commissioned in Q4FY20 would be key drivers for medium to long term growth. This will assist in fulfilling a strong order book from OEMs and further improve its market share in the PCR, 2W and TBR segments. Moreover, ban on import of Chinese tyres will also aid growth in the PCR replacement segment.

Margin to squeeze from 4QFY21

In Q3, the company benefited from lower cost of raw material purchased in earlier quarters. However, December onwards, the company to utilize the entire high cost inventory of raw materials. We expect rise in raw material prices (NR at Rs 160/kg and crude at \$55/barrel) will negatively impact margins. The company has taken price hikes of 1% at the beginning of December and another 2.5% in December end across categories except for 2W tyres. The company may consider taking another 3% price hike in Q4 to offset the increase in RM prices depending on the competitive scenario.

Exhibit 1: Actual vs DART Estimates

Particulars (Rs mn)	Actual	DART Est	Var (%)	Remarks
Sales	22,213	20,031	11	Better than anticipated revival in demand across segments and cost control measures.
EBIDTA	3,277	2,564	28	
EBIDTA Margin (%)	14.8	12.8	195bps	
APAT	1,323	969	37	

Source: DART, Company

Exhibit 2: Change in estimates

Rs Mn	FY22E			FY23E		
	New	Previous	Chg (%)	New	Previous	Chg (%)
Revenue	79,484	72,879	9.1	86,377	81,440	6.1
EBITDA	8,926	8,156	9.4	9,924	9,231	7.5
EBITDA margin(%)	11.2	11.2	4bps	11.5	11.3	15bps
APAT	3,135	2,519	22.9	3,913	3,368	15.6
EPS	77.5	62.3	22.9	96.7	83.3	15.6

Source: Company, DART

Exhibit 3: Assumption Sheet

Standalone revenue mix (%)	FY18	FY19	FY20	FY21E	FY22E	FY23E
Truck & Bus (MHCV)	32	32	32	30	31	32
- TBR	9	11	15	16	17	17
- TBB	23	23	17	14	14	15
2W/3W	31	31	32	31	30	29
PV	14	14	14	15	15	16
LCV	12	12	11	11	11	10
Farm	7	7	6	8	8	8
Specialty	4	4	5	5	5	6

Source: Company, DART

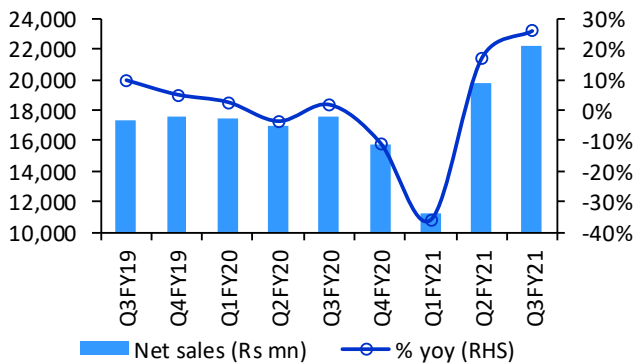
Key Concall Takeaways

- Improvement in revenue was mainly driven by volume gains across segments. Growth was attributed to new capacities across PCR, 2W and farm tyre segments, need for personal mobility and thriving rural demand. OEM demand has seen an uptick in the festive season and replacement demand continues to be strong. 2W OEM demand has slowed down since a month while CV demand is likely to pick up over the coming months, reflected by the increased toll collections.
- The OEM segment grew 15% YoY while replacement segment grew 35% YoY in Q3 with overall growth of 28% YoY. OHT segment reported 42% YoY growth and farm segment has shown robust growth in the domestic and export segments. CV tyres (TBB and TBR) in the replacement market have seen a strong demand with 30% YoY growth in Q3. For 9MFY21, overall volumes have grown by ~3-4% YoY with replacement segment showing positive growth offset by OEM and Exports.
- CEAT expanded its market share on back of expanding dealership network and robust supply chain management and ramping up of capacities. PCR market share grew by 3-5%. CEAT commands ~15% market share in PCR segment (historically 10-11%).
- Company has taken multiple price hikes – 1% in December and another 2.5% at the fag end of December across categories except for 2W. Company requires to take another 3% price hike in Q4 to offset increase in RM prices depending on the competitive scenario.
- For Q3, raw material basket cost (Carbon black, synthetic fiber and natural rubber) increased by 1.5% QoQ. Rise in raw material prices (NR at Rs 160/kg and crude at \$55/barrel) will negatively impact margins. RM prices are likely to increase by 10% by Q4FY21 end.
- Gross margin contracted due to unfavorable channel and product mix. In Q3, segment mix is almost back to normal with Replacement:OEM:Export at 60:25:15.
- Category wise revenue mix: 2W is 30%; PCR is 15%; T&B is ~40% and Farm/OHT is 15%. TBR segment has shown higher growth of 45% YoY with TBR:TBB mix at 60:40.
- Employee expense increased (average Rs 1,700mn/quarter) due to commissioning of new capacities and incentive programs offered. Expect employee costs to increase with increase in volume output.
- On a full year basis, advertising cost to be maintained at 2-3% of revenues.
- Inventory levels are uncomfortably low with channel inventory below one month. Working capital requirement likely to increase with increase in RM stocking and receivables.
- All plants are operating at high capacity levels with good prospects of growth in the upcoming months.
- Gross debt at the end of Q3FY21 was Rs 15.56bn (decreased by Rs 2.5bn on sequential basis). In 9MFY21, CEAT reduced debt by Rs 3.5bn led by reduction in working capital by Rs 3bn. Consolidated Gross Debt: Equity was 0.49x (vs 0.59x in Q2FY21).
- Wef from 1st Sept, 2020, CEAT and CEAT Specialty Tyres Ltd (CSTL) merger has been completed and all numbers have been restated.

Capex guidance

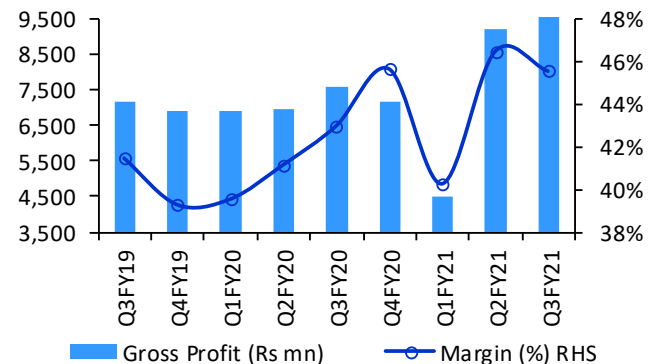
- Capex incurred was ~Rs 3.5bn in 9MFY21. For FY21, CEAT is likely to spend Rs 6bn as capex. Company has given a guidance Rs 7bn each for FY22 and FY23.
- CEAT incurs routine maintenance capex of Rs 1.5bn.
- Out of the overall planned capex of Rs 40bn, CEAT is has completed Rs 22bn of capex.

Exhibit 4: Revenue improved QoQ/YoY



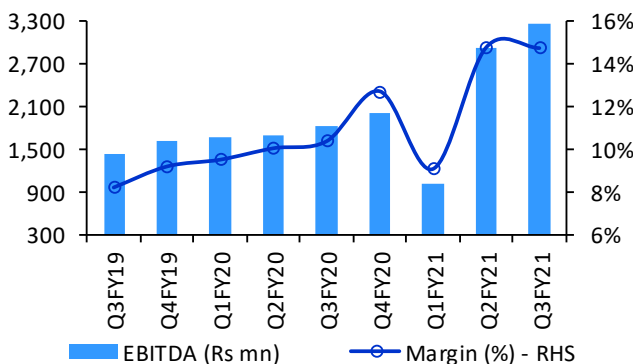
Source: DART, Company

Exhibit 5: Increase in Gross profit and margin



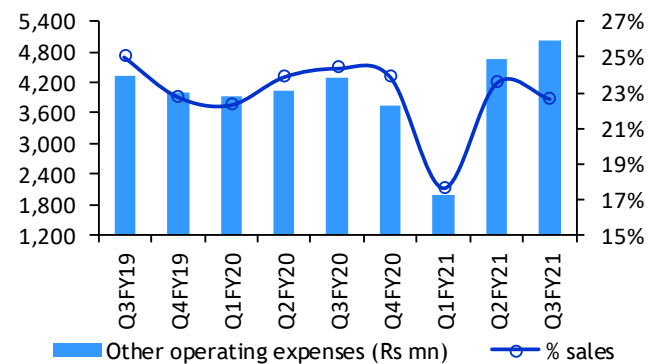
Source: DART, Company

Exhibit 6: Improvement in EBITDA (Rs mn)



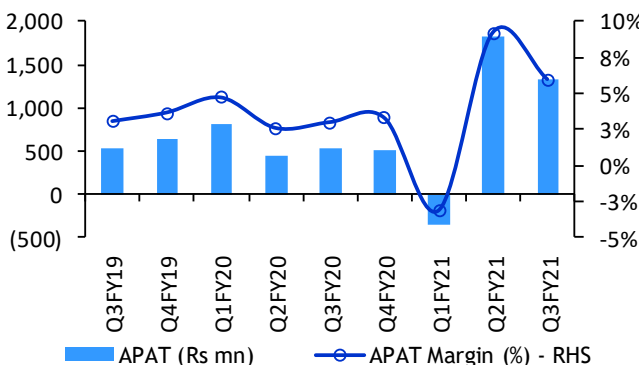
Source: DART, Company

Exhibit 7: Other Expenses (Rs mn vs % of Sales)



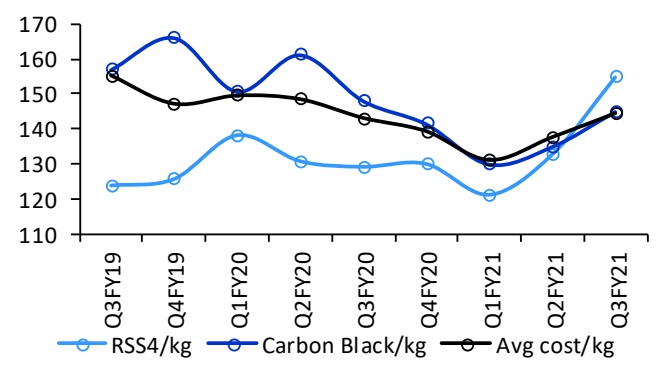
Source: DART, Company

Exhibit 8: APAT (Rs mn) vs Margin (%)



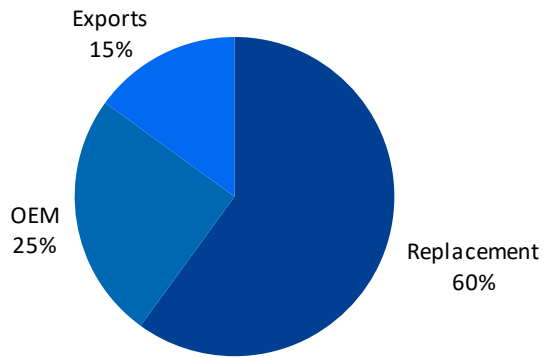
Source: DART, Company

Exhibit 9: Raw Material Prices (Rs/kg)



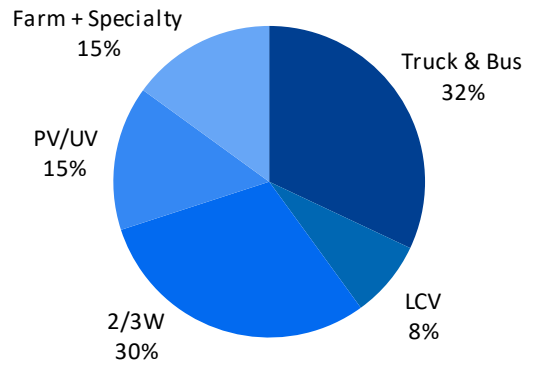
Source: DART, Company

Exhibit 10: Revenue Breakup by Market– Q3FY21 (%)



Source: DART, Company

Exhibit 11: Revenue Breakup by Product– Q3FY21(%)



Source: DART, Company

Profit and Loss Account

(Rs Mn)	FY20A	FY21E	FY22E	FY23E
Revenue	67,788	72,253	79,484	86,377
Total Expense	60,550	62,761	70,558	76,453
COGS	39,151	40,091	45,349	49,358
Employees Cost	5,418	6,507	7,220	7,543
Other expenses	15,981	16,163	17,988	19,552
EBIDTA	7,238	9,491	8,926	9,924
Depreciation	2,765	3,497	3,590	3,740
EBIT	4,473	5,994	5,336	6,185
Interest	1,509	1,684	1,589	1,406
Other Income	205	225	300	320
Exc. / E.O. items	(298)	0	0	0
EBT	2,871	4,535	4,047	5,098
Tax	742	907	1,052	1,326
RPAT	2,313	3,740	3,135	3,913
Minority Interest	(12)	(12)	(20)	(10)
Profit/Loss share of associates	172	100	120	130
APAT	2,611	3,740	3,135	3,913

Balance Sheet

(Rs Mn)	FY20A	FY21E	FY22E	FY23E
Sources of Funds				
Equity Capital	405	405	405	405
Minority Interest	237	225	205	195
Reserves & Surplus	28,675	31,665	34,092	37,165
Net Worth	29,079	32,069	34,497	37,570
Total Debt	20,840	22,340	21,190	18,990
Net Deferred Tax Liability	2,565	2,565	2,565	2,565
Total Capital Employed	52,720	57,198	58,456	59,318

Applications of Funds

Net Block	41,598	46,101	51,111	52,971
CWIP	10,685	8,685	6,685	6,185
Investments	2,679	2,679	2,679	2,679
Current Assets, Loans & Advances	18,388	22,261	21,239	22,759
Inventories	9,257	9,502	10,453	11,359
Receivables	6,744	7,358	8,095	8,797
Cash and Bank Balances	342	2,969	240	180
Loans and Advances	0	0	0	0
Other Current Assets	2,046	2,432	2,452	2,423
Less: Current Liabilities & Provisions	20,630	22,528	23,258	25,276
Payables	18,995	20,785	21,341	23,192
Other Current Liabilities	1,635	1,743	1,918	2,084
		<i>sub total</i>		
Net Current Assets	(2,242)	(267)	(2,019)	(2,517)
Total Assets	52,720	57,198	58,456	59,318

E – Estimates

Important Ratios

Particulars	FY20A	FY21E	FY22E	FY23E
(A) Margins (%)				
Gross Profit Margin	42.2	44.5	42.9	42.9
EBIDTA Margin	10.7	13.1	11.2	11.5
EBIT Margin	6.6	8.3	6.7	7.2
Tax rate	25.9	20.0	26.0	26.0
Net Profit Margin	3.4	5.2	3.9	4.5
(B) As Percentage of Net Sales (%)				
COGS	57.8	55.5	57.1	57.1
Employee	8.0	9.0	9.1	8.7
Other	23.6	22.4	22.6	22.6
(C) Measure of Financial Status				
Gross Debt / Equity	0.7	0.7	0.6	0.5
Interest Coverage	3.0	3.6	3.4	4.4
Inventory days	50	48	48	48
Debtors days	36	37	37	37
Average Cost of Debt	8.5	7.8	7.3	7.0
Payable days	102	105	98	98
Working Capital days	(12)	(1)	(9)	(11)
FA T/O	1.6	1.6	1.6	1.6
(D) Measures of Investment				
AEPS (Rs)	64.6	92.5	77.5	96.7
CEPS (Rs)	132.9	178.9	166.3	189.2
DPS (Rs)	14.4	18.3	17.0	20.5
Dividend Payout (%)	22.3	19.7	21.9	21.2
BVPS (Rs)	718.9	792.8	852.8	928.8
RoANW (%)	8.2	12.2	9.4	10.9
RoACE (%)	8.1	9.7	7.9	8.8
RoAIC (%)	9.3	11.2	9.5	10.5
(E) Valuation Ratios				
CMP (Rs)	1310	1310	1310	1310
P/E	20.3	14.2	16.9	13.5
Mcap (Rs Mn)	52,996	52,996	52,996	52,996
MCap/ Sales	0.8	0.7	0.7	0.6
EV	73,493	72,366	73,946	71,806
EV/Sales	1.1	1.0	0.9	0.8
EV/EBITDA	10.2	7.6	8.3	7.2
P/BV	1.8	1.7	1.5	1.4
Dividend Yield (%)	1.1	1.4	1.3	1.6
(F) Growth Rate (%)				
Revenue	(2.9)	6.6	10.0	8.7
EBITDA	12.7	31.1	(6.0)	11.2
EBIT	(0.6)	34.0	(11.0)	15.9
PBT	(19.4)	58.0	(10.8)	26.0
APAT	(7.4)	43.2	(16.2)	24.8
EPS	(7.4)	43.2	(16.2)	24.8
Cash Flow				
(Rs Mn)	FY20A	FY21E	FY22E	FY23E
CFO	9,563	9,549	7,297	9,476
CFI	(10,755)	(6,000)	(6,600)	(5,100)
CFE	790	(922)	(3,426)	(4,436)
FCFF	(1,536)	3,549	697	4,376
Opening Cash	735	342	2,969	240
Closing Cash	342	2,969	240	180

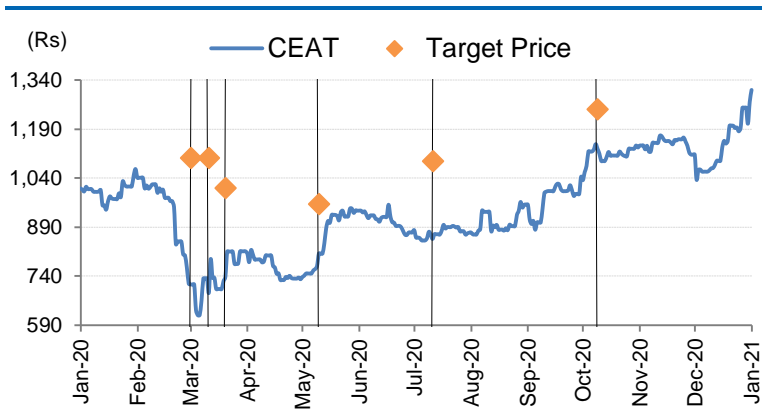
E – Estimates

DART RATING MATRIX

Total Return Expectation (12 Months)

Buy	> 20%
Accumulate	10 to 20%
Reduce	0 to 10%
Sell	< 0%

Rating and Target Price History



Month	Rating	TP (Rs.)	Price (Rs.)
Mar-20	Buy	1,102	715
Mar-20	Buy	1,102	690
Apr-20	Buy	1,009	739
May-20	Accumulate	960	810
Jul-20	Buy	1,092	854
Oct-20	Accumulate	1,250	1,130

*Price as on recommendation date

DART Team

Purvag Shah **Managing Director** **purvag@dolatcapital.com** **+9122 4096 9747**

Amit Khurana, CFA **Head of Equities** **amit@dolatcapital.com** **+9122 4096 9745**

CONTACT DETAILS

Equity Sales	Designation	E-mail	Direct Lines
Dinesh Bajaj	VP - Equity Sales	dineshb@dolatcapital.com	+9122 4096 9709
Kapil Yadav	VP - Equity Sales	kapil@dolatcapital.com	+9122 4096 9735
Yomika Agarwal	VP - Equity Sales	yomika@dolatcapital.com	+9122 4096 9772
Jubbin Shah	VP - Derivatives Sales	jubbins@dolatcapital.com	+9122 4096 9779
Ashwani Kandoi	AVP - Equity Sales	ashwanik@dolatcapital.com	+9122 4096 9725
Lekha Nahar	AVP - Equity Sales	lekhan@dolatcapital.com	+9122 4096 9740
Equity Trading	Designation	E-mail	
P. Sridhar	SVP and Head of Sales Trading	sridhar@dolatcapital.com	+9122 4096 9728
Chandrakant Ware	VP - Sales Trading	chandrakant@dolatcapital.com	+9122 4096 9707
Shirish Thakkar	VP - Head Domestic Derivatives Sales Trading	shirisht@dolatcapital.com	+9122 4096 9702
Kartik Mehta	Asia Head Derivatives	kartikm@dolatcapital.com	+9122 4096 9715
Dinesh Mehta	Co- Head Asia Derivatives	dinesh.mehta@dolatcapital.com	+9122 4096 9765
Bhavin Mehta	VP - Derivatives Strategist	bhavinm@dolatcapital.com	+9122 4096 9705

Dolat Capital Market Private Limited.

Sunshine Tower, 28th Floor, Senapati Bapat Marg, Dadar (West), Mumbai 400013

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SEBI Registration No: BSE - INB010710052 & INF010710052, NSE - INB230710031& INF230710031, Research: INH000000685

Registered office: Office No. 141, Centre Point, Somnath, Daman – 396 210, Daman & Diu

Board: +9122 40969700 | Fax: +9122 22651278 | Email: research@dolatcapital.com | www.dolatresearch.com
