Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

| 3R MATRIX | + | = | - |
|---|---|---|---|
| Right Sector (RS) | ✓ | | |
| Right Quality (RQ) | ✓ | | |
| Right Valuation (RV) | ✓ | | |

\+ Positive = Neutral – Negative

**What has changed in 3R MATRIX**

| | Old | | New |
|---|---|---|---|
| RS | | ⇔ | |
| RQ | | ⇔ | |
| RV | | ↑ | |

## ESG Disclosure Score NEW

**ESG RISK RATING** 20.57
Updated Feb 08, 2022

**Medium Risk**

| NEGL | LOW | MED | HIGH | SEVERE |
|---|---|---|---|---|
| 0-10 | 10-20 | 20-30 | 30-40 | 40+ |

*Source: Morningstar*

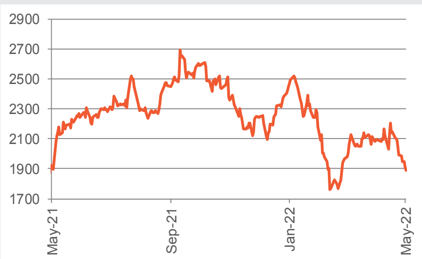
### Company details

| | |
|---|---|
| Market cap: | Rs. 36,498 cr |
| 52-week high/low: | Rs. 2,724 / 1,682 |
| NSE volume: (No of shares) | 2.7 lakh |
| BSE code: | 502355 |
| NSE code: | BALKRISIND |
| Free float: (No of shares) | 8.1 cr |

### Shareholding (%)

| | |
|---|---|
| Promoters | 58.3 |
| FII | 14.1 |
| DII | 11.8 |
| Others | 15.9 |

### Price chart




### Price performance

| (%) | 1m | 3m | 6m | 12m |
|---|---|---|---|---|
| Absolute | -10.8 | -15.9 | -25.0 | 3.0 |
| Relative to Sensex | 0.4 | -7.5 | -13.0 | -4.3 |

*Sharekhan Research, Bloomberg*

# Balkrishna Industries Ltd

## Q4 ahead of expectation; robust growth outlook

| Automobiles | Sharekhan code: BALKRISIND |
|---|---|

| Reco/View: Buy | ⇔ | CMP: Rs. 1,888 | Price Target: Rs. 2,450 | ↓ |
|---|---|---|---|---|

↑ Upgrade ⇔ Maintain ↓ Downgrade


**Summary**

- We maintain our Buy rating on Balkrishna Industries Limited's (Balkrishna) with a revised PT of Rs. 2,450 given robust outlook and earnings growth. The stock trades at P/E multiple of 17.7x and EV/EBITDA multiple of 12.9x its FY2024E estimates.
- For Q4FY22, Balkrishna's results were results ahead of expectations, led by higher-than-expected sales volume growth, though EBITDA margin got impacted due to higher freight costs.
- We expect Balkrishna continue to deliver robust double-digit volume growth in FY23E, driven by increase in infrastructure activity and pick-up in economic activity and continued market share gains.
- Timely execution of capex plans, market share gains and entry in new markets would be key growth drivers for the company.


**Balkrishna Industries Limited (Balkrishna) reported Q4FY22 results ahead of expectations, led by higher-than-expected sales volume growth, though EBITDA margin got impacted due to higher freight costs. Net revenue grew by 36% y-o-y to Rs. 2,374 crore in Q4FY22, driven by 13.4% volume growth at 77,119 MT of tyres and 19.9% growth in average sales realization. Average realisation improved by price hikes and a better product mix. EBITDA margin declined by 80 bps q-o-q to 21% in Q4FY22, impacted by higher freight costs. The management has witnessed strong demand in the agriculture segment across geographie, but highlighted the geo-political tension could further aggravate supply chain problems. In other segments, demand has seen an uptick because of increased commodity prices, infrastructure creation, and a pick-up in economic activity. The company has decided to keep the investment of Rs 350 crore at old Walnuj plant as announced in Nov.'21, on hold due to strong demand, which would help the plant to continue the production unhindered and meet the schedule demanded by customers.**

**Other capex programs are on track. Further, the management has guided double-digit volume growth in FY23E. We maintain a positive stance on the company's growth and margin prospecs, and a BUY rating on the stock with a revised PT of Rs2,450.**

**Key positives**

- Quarterly volumes rose to record highs at 77,119 MT, led by robust growth across segments and geographies.
- The capex programs remain intact, except at the old Walnuj plant, which is been put on hold, due to strong demand which would help the plant to continue the production unhindered and meet the schedule demanded by customers.

**Key negatives**

- EBITDA margin declined by 80 bps q-o-q to 21% in Q4FY22, impacted by higher freight costs.

**Management Commentary**

- Volume growth guidance is given at 10.8-14% in FY23E on strong demand, while margins are expected to improve led by product mix and operating leverage benefits.
- The company took price hikes of 2-3% during the month of February and will take further price hike of 3-4% in the month of June. Also, the company expects RM basket to further increase by 3-4% in Q1FY23.

**Our Call**

**Valuation – Maintain Buy rating with a revised PT of Rs. 2,450:** Balkrishna is witnessing strong demand traction across segments and geographies. The company has a capex plan of Rs. 1,700 crore towards ramping up production over the next 2-3 years, investing in capacity expansion, backward integration, automation, and modernisation of plants. We have fine-tuned our estimates to build in the impact higher freight cost in the near term, triggered by the ongoing geopolitical situation. The management has given FY23E volume guidance of 320,000-330,000MT, implying 11-14% y-o-y growth in FY23E. Also, BKT expects to achieve 10% global market share in tyres in the medium term from 7-8% currently. The market shareis likely to increase, driven by new launches and entry into new geographies. Post stock correction of 25% over the last six months, the stock is available at comfortable valuations of P/E of 17.6x and EV/EBITDA of 11.3x. Thus, we have maintained our BUY rating on the stock with a revised price target of Rs. 2,450, given robust outlook and earnings growth.

**Key Risks**

Balkrishna derives ~23% of its revenue from India, while it derives 50% from Europe, 15% from America, and 13% from rest of the world (FY2021). Any adverse movement in the macro environment of these countries or forex fluctuation could impact the company's financial performance.

**Valuation (Standalone)** Rs cr

| Particulars | FY21 | FY22 | FY23E | FY24E |
|---|---|---|---|---|
| Revenues | 5,758 | 8,267 | 10,130 | 11,504 |
| Growth (%) | 17.6 | 43.6 | 22.5 | 13.6 |
| EBIDTA | 1,786 | 1,976 | 2,430 | 2,924 |
| OPM (%) | 31.0 | 23.9 | 24.0 | 25.4 |
| Net Profit | 1,155 | 1,411 | 1,643 | 2,059 |
| Growth (%) | 22.3 | 22.1 | 16.5 | 25.3 |
| EPS | 59.8 | 73.0 | 85.0 | 106.5 |
| P/E | 31.6 | 25.9 | 22.2 | 17.7 |
| P/BV | 6.2 | 5.5 | 4.6 | 3.8 |
| EV/EBIDTA | 20.8 | 19.4 | 15.7 | 12.9 |
| ROE (%) | 19.5 | 21.1 | 20.6 | 21.3 |
| ROCE (%) | 22.1 | 25.3 | 24.4 | 25.8 |

*Source: Company; Sharekhan estimates*

Stock Update
Result Update

**Q4 results higher than expectations:** Balkrishna Industries Limited (Balkrishna) reported Q4FY22 results ahead of expectations, led by higher-than-expected sales volume growth, though EBITDA margin got impacted due to higher freight costs. Net revenue grew by 36% y-o-y to Rs. 2,374 crores in Q4FY22, driven by 13.4% volume growth at 77,119 MT of tyres and 19.9% growth in average sales realisation. Average realisation improved by price hikes and a better product mix. EBITDA margin declined by 80 bps q-o-q to 21% in Q4FY22, impacted by higher freight costs. On the other hand, the company's gross margins improved 110 bps q-o-q to 53.5%, driven by price hikes and product mix. The company took price hikes of 2-3% during the month of February and will take further price hikes of 3-4% in the month of June. Also, the company expects the RM basket to further increase by 3-4% in Q1FY23. For FY2022, the segmental revenue mix remained at 65.5% from agriculture, 31.1% from OTR, and balance 3.3% from others. Replacement demand continues to dominate with revenue share of 69.1%, while original equipment manufacturers' (OEMs) share remained at 27.7% and other channels at 3.3% in FY2022. As per the geographical mix, Europe sales contributed 53.9%, India contributed 17.6%, America contributed 17.3%, and ROW contributed 11.2%.

**Positive guidance:** Volume growth guidance given at 10.8-14% in FY23E on strong demand, while margins are expected to improve led by product mix and operating leverage benefits. The company took price hikes of 2-3% during the month of February and will take further price hikes of 3-4% in the month of June. Also, the company expects the RM basket to further increase by 3-4% in Q1FY23. The Capex programs remain intact, except at the old Walnuj plant, which is been put on hold, due to strong demand which would help the plant to continue the production unhindered and meet the schedule demanded by customers. The geopolitical situation has aggravated supply chain problems, which has led to an increase in the prices and availability of raw materials. End user markets continue to remain strong in spite of inflationary trends. The OHT industry continues to see higher offtake on account of healthy demand across mining and agriculture markets; BKT brand is continuing to gain market share. Similarly, Logistics and freight costs have continued to remain at elevated levels.

**Capex plan:** The capex programs remain intact except at the old Walnuj plant, which is been put on hold, due to strong demand which would help the plant to continue the production unhindered and meet the schedule demanded by customers. Moreover, Balkrishna will use capex for automation and technology upgradation. The Brownfield tyre project at the Bhuj plant would add ~50,000 MTPA capacity, which is expected to be complete- ramp-up in production H2FY23. Post the Brownfield capex, capacity of the tyre plant will stand at 335,000 MTPA. This would require an investment of Rs. 800 crore. The company is planning to increase its capacity for carbon black and captive power by commissioning for 55,000 MTPA Carbon Black capacities along with Power Plant in the next 2-3 months. The project of advanced carbon material for 30,000 MTPA will be commissioned in H2FY23. Capex for this purpose would amount to Rs. 650 crore. The third part of capex would be invested in modernisation, automation, and technology upgradation at its Bhuj and Gujarat plants. Capex cost for this purpose is estimated around Rs. 450 crore and is expected to be completed by end-H1FY23. Capex plans are embarked, given the current market demand, both domestic and global.

**Key focus areas:** Management continues to focus on market reach through existing sales channels, increased share of business in US markets by increasing supplies from India, expansion in the product portfolio by adding large-size tyres, strengthening distribution channels within Indian markets, and reaching 100% capacity utilisation at its Bhuj plant.

**Strong demand to drive growth:** The company continues to maintain its target to achieve a 10% global market share in tyres in the medium term from ~6% currently. Excluding China, the company has a global market share of 7-8%. We expect Balkrishna to gain market share, driven by new product introductions and entry into new geographies. We expect strong double-digit volume growth in FY2023E, driven by infrastructure creation, pick-up in economic activity, and continued market share gains. We expect BKT's earnings to report a 20.8% CAGR during FY2022-FY2024E, largely driven by volume growth.

**Results (Standalone)** Rs cr

| Particulars | Q4FY22 | Q4FY21 | YoY% | Q3FY22 | QoQ% |
|---|---|---|---|---|---|
| Revenues | 2,373.9 | 1,745.9 | 36.0 | 2,030.0 | 16.9 |
| Total operating expenses | 1,874.4 | 1,204.1 | 55.7 | 1,586.5 | 18.1 |
| EBITDA | 499.5 | 541.8 | -7.8 | 443.4 | 12.6 |
| Depreciation | 116.7 | 103.4 | 12.8 | 114.5 | 1.9 |
| Interest | 2.1 | 2.3 | (7.0) | 1.8 | 19.6 |
| Other income | 107.7 | 58.4 | 84.4 | 111.6 | -3.5 |
| PBT | 488.4 | 494.5 | -1.2 | 438.7 | 11.3 |
| Tax | 114.7 | 122.3 | -6.2 | 110.1 | 4.1 |
| Reported PAT | 15.5 | 7.3 | 112.3 | (1.2) | NA |
| Adjusted PAT | 373.7 | 372.2 | 0.4 | 328.6 | 13.7 |
| Adjusted EPS | 19.3 | 19.3 | 0.4 | 17.0 | 13.7 |

*Source: Company; Sharekhan Research*

**Key ratios (Standalone)** Rs cr

| Particulars | Q4FY22 | Q4FY21 | YoY (bps) | Q3FY22 | QoQ (bps) |
|---|---|---|---|---|---|
| Gross margin (%) | 53.5 | 58.7 | -510 | 52.4 | 110 |
| EBIDTA margin (%) | 21.0 | 31.0 | -1,000 | 21.8 | -80 |
| EBIT margin (%) | 16.1 | 25.1 | -900 | 16.2 | -10 |
| Net profit margin (%) | 15.7 | 21.3 | -560 | 16.2 | -40 |
| Effective tax rate (%) | 23.5 | 24.7 | -120 | 25.1 | -160 |

*Source: Company Data; Sharekhan Research*

## Outlook and Valuation

### Sector outlook – Double digit growth in FY23E, led by faster growth in OEM markets

We expect the domestic tyre industry to naturally benefit from the sharp recovery in automobile sales post normalisation of the economy. The automobile sector has witnessed broad-based recovery across segments, driven by pent-up demand, preference for personal mobility amid COVID-19, and faster-than-expected recovery in infrastructure, mining, and other economic activities. The tyre industry is well positioned to gain momentum in the medium term, backed by higher OEM offtake and ripple effect of the same, which are likely to result in steady growth for replacement demand. The scenario in Europe and Americas is also recovering significantly, with sales and volumes nearing pre-COVID levels.

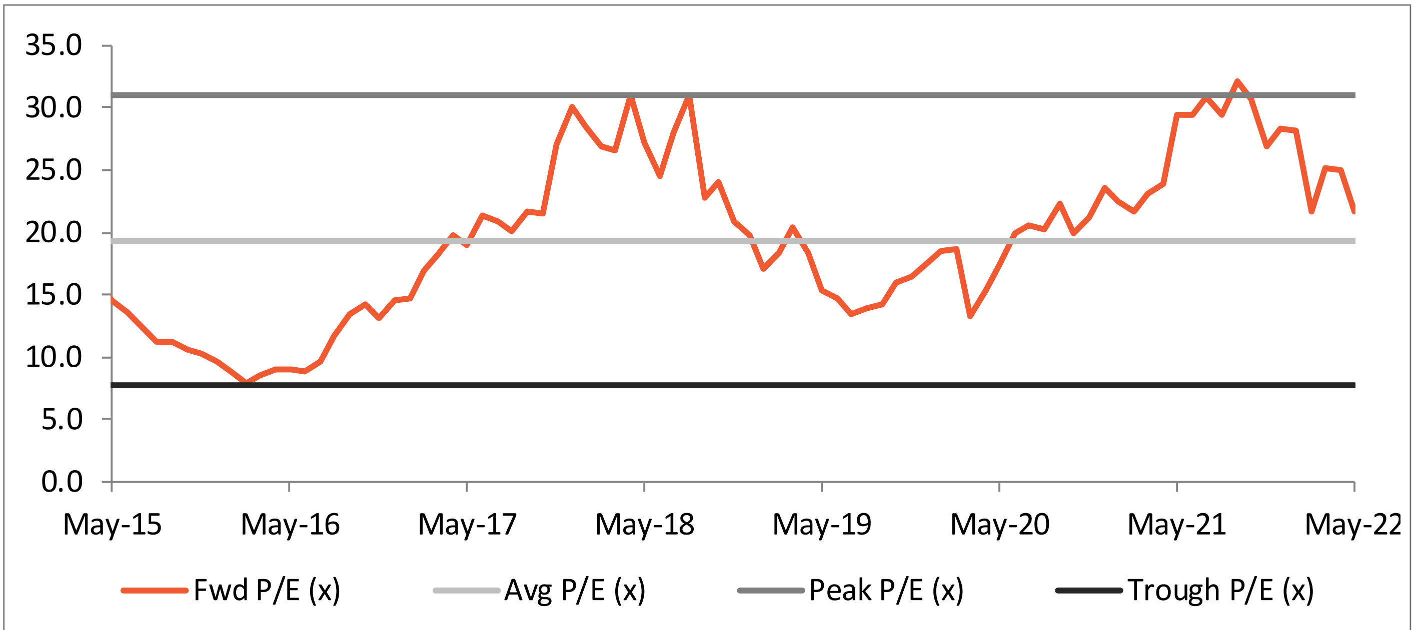
### Company outlook – Strong demand and margin profile

Balkrishna has given volume growth guidance of 10.8-14% in FY23E on strong demand, while margins are expected to improve led by product mix and operating leverage benefits. Further, the management expects margins to sustain 28-30% going forward. The company continues to maintain its target to achieve 10% global market share in tyres in the medium term from ~6% currently. We expect Balkrishna to gain market share, driven by product launches and entry into new geographies. We expect strong double-digit volume growth in FY2023E, driven by infrastructure creation, pick-up in economic activity, and continued market share gains. We expect BKT's earnings to report a 20.8% CAGR during FY2022-FY2024E, largely driven by volume growth.

### Valuation – Maintain Buy rating with a revised PT of Rs. 2,450

Balkrishna is witnessing strong demand traction across segments and geographies. The company has capex plan of Rs. 1,700 crore towards ramping up production over the next 2-3 years, investing in capacity expansion, backward integration, automation, and modernisation of plants. We have fine-tuned our estimates to build in the impact higher freight cost in the near term, triggered by ongoing geo-political situation. The management has given FY23E volume guidance of 320,000-330,000MT, implying 11-14% y-o-y growth in FY23E. Also, BKT expects to achieve 10% global market share in tyres in the medium term from 7-8% currently. Market share likely to increase, driven by new launches and entry into new geographies. Post stock correction of 25% over the last six months, the stock is available at comfortable valuations of P/E of 17.6x and EV/EBITDA of 11.3x. Thus, we have maintained our BUY rating on the stock with a revised price target of Rs. 2,450, given robust outlook and earnings growth.

**One-year forward P/E (x) band**




*Source: Sharekhan Research*

**Peer Comparison**

| Companies | CMP (Rs / Share) | P/E (x) | | | EV/EBITDA (x) | | | RoCE (%) | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | | FY21 | FY22E | FY23E | FY21 | FY22E | FY23E | FY21 | FY22E | FY23E |
| Balkrishna Industries | 1,888 | 31.6 | 25.9 | 22.2 | 20.8 | 19.4 | 15.7 | 22.1 | 25.3 | 24.4 |
| Apollo Tyres | 200 | 13.3 | 19.7 | 9.5 | 5.7 | 6.2 | 4.6 | 7.8 | 5.4 | 8.5 |

*Source: Company, Sharekhan estimates*

## About the company

Balkrishna is one of the leading manufacturers of over-the-highway tyres. The company makes tyres that are used in various applications, including agricultural, construction, and industrial vehicles as well as earthmoving, port, mining, ATV, and gardening. Balkrishna is a global player present in Europe, US, and India. While European markets account for ~50% of sales, US and India account for 15% and 23% of sales, respectively. The company has a well-spread distribution network that supports sales to 160 countries. The company has three manufacturing plants in India – in Aurangabad and Bhuj (western India), Bhiwadi, and Chopanki (in North India). In addition to this, the company operates a mould plant in Dombivli (near Mumbai). The current achievable production capacity across all plants stands at 3,00,000 MTPA, comprising a widespread product portfolio of 2,700 SKUs.

## Investment theme

Balkrishna is one of the leading tyre companies, having a well-diversified product portfolio, spread across niche segments, including agriculture, industrial, construction, earthmoving, mining, port, lawn and garden, and ATV tyres. The company has superior margin and return ratio profiles to its domestic counterpart due to its product positioning and strong hold in overseas market. The company has built a resilient business model and is expected to emerge as a stronger global player. The company aims to achieve 10% market share globally in the tyres market, with new product launches and expansion in new geographies. The company is self-reliant in carbon black along with multiple sourcing arrangements for other raw materials, which keeps its margins firm. The company has robust balance sheet strength and strong cash and cash equivalents at Rs. 1,475 crore as of FY2021-end. Management has recently increased its capex commitment for carbon black, which will lead to sale of excess carbon black to third party. We believe this will impact the company's margin and return ratio profile in the long run.

## Key Risks

- Balkrishna derives ~23% of its revenue from India, while it derives 49% from Europe, 15% from America, and 13% from ROW (FY2021). Any adverse movement in the macro-environment of these countries or forex fluctuation could impact the company's financial performance.

## Additional Data

**Key management personnel**

| | |
|---|---|
| Arvind Poddar | Chairman and Managing Director |
| Rajiv Poddar | Joint Managing Director |
| Vipul Shah | Wholetime Director andCompany Secretary |
| Madhu Sudan Bajaj | President (Commercials) and Chief Financial Officer |

*Source: Company Website*

**Top 10 shareholders**

| Sr. No. | Holder Name | Holding (%) |
|---|---|---|
| 1 | Rajiv A Poddar | 27.7 |
| 2 | Vkp Enterprises | 25.0 |
| 3 | Khushboo Rajiv Poddar | 3.9 |
| 4 | Rishabh Sureshkumar Poddar | 1.4 |
| 5 | HDFC Trustee Co. | 4.2 |
| 6 | Kotak Esg Opportunities Fund | 2.4 |
| 7 | Dsp Quant Fund | 1.9 |
| 8 | Government Pension Fund Global | 1.6 |
| 9 | HDFC Life Insurance Company Limited | 1.5 |
| 10 | Mirae Asset Equity Savings Fund | 1.4 |

*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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by BNP PARIBAS

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Compliance Officer: Mr. Joby John Meledan; Tel: 022-61150000; email id: compliance@sharekhan.com;

For any queries or grievances kindly email igc@sharekhan.com or contact: myaccount@sharekhan.com

**Registered Office:** Sharekhan Limited, 10th Floor, Beta Building, Lodha iThink Techno Campus, Off. JVLR, Opp. Kanjurmarg Railway Station, Kanjurmarg (East), Mumbai – 400042, Maharashtra. Tel: 022 - 61150000. Sharekhan Ltd.: SEBI Regn. Nos.: BSE / NSE / MSEI (CASH / F&O / CD) / MCX - Commodity: INZ000171337; DP: NSDL/CDSL-IN-DP-365-2018; PMS: INP000005786; Mutual Fund: ARN 20669; Research Analyst: INH000006183;