

CMP: ₹ 130

Target: ₹ 135 (4%)

Target Period: 12 months

HOLD

August 10, 2022

Sustainable margin recovery still sometime away...

About the stock: JK Tyre (JKT) is a leading tyre manufacturer with annual capacity pegged at 5.97 lakh MT. It serves various automotive segments via India, Mexico plants with dominance in truck/bus radial (TBR) space domestically.

- FY22 segment mix – truck/bus ~55%, PCR ~26%, 2-W, 3-W ~4%
- FY22 channel mix – aftermarket ~59%, OEM ~20%, exports ~21%

Q1FY23 Results: The company reported a healthy performance in Q1FY23.

- Consolidated net sales were up 10% QoQ to ₹ 3,643 crore
- EBITDA margins rose 90 bps QoQ to 7.8% amid positive operating leverage
- Consequent PAT was at ₹ 37.2 crore, down 7% QoQ

What should investors do? JKT's share price has de-grown at ~2.6% CAGR over the past five years (~₹ 147 levels in August 2017), underperforming Nifty Auto index

- With muted margin commentary due to elevated commodity costs along with limited b/s de-leveraging due to fresh capex spend, we maintain **HOLD** rating and await margin recovery before turning decisively positive

Target Price and Valuation: Revising our estimates, we now value JKT at ₹ 135 i.e. 6x EV/EBITDA on FY24E basis (earlier target price ₹ 120)

Key triggers for future price performance:

- Beneficiary of domestic CV upswing & high share of aftermarket sales (60%)
- Substantial decline in input prices namely natural rubber & crude derivatives to lead to gross margin expansion as well as healthy cash flow generation
- Reduction of debt on b/s (term loans) amid normalised working capital need
- Building in the visible positives, we build 14.8% net sales CAGR in FY22-24E with margins seen at 9% in FY24E on the base of higher focus on export markets along with continued focus on premiumisation of products

Alternate Stock Idea: Besides JKT, in our auto coverage we like M&M.

- Focused on prudent capital allocation, UV differentiation & EV proactiveness
- BUY with a target price of ₹ 1,550



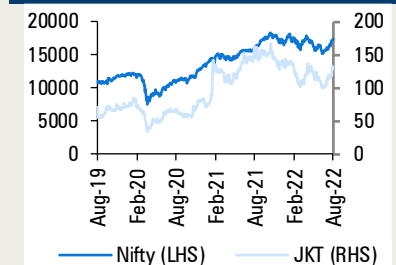
Particulars

Particular	₹ crore
Market Capitalization	3,201.3
Total Debt (FY22)	5,115.2
Cash & Investments (FY22)	175.7
EV (₹ Crore)	8,140.8
52 week H/L (₹)	172 / 95
Equity capital (₹ crore)	₹ 49.3 Crore
Face value (₹)	₹ 2

Shareholding pattern

	Sep-21	Dec-21	Mar-22	Jun-22
Promoter	55.9	55.9	56.3	56.3
FII	7.8	8.1	8.2	7.4
DII	1.3	1.3	1.2	1.2
Other	35.0	34.7	34.4	35.2

Price Chart



Recent event & key risks

- Posted healthy Q1FY23 results
- Key Risk:** (i) Delay in gross margin recovery amid elevated RM costs, (ii) Healthy CFO generation and consequent repayment of debt

Research Analyst

Shashank Kanodia, CFA
shashank.kanodia@icicisecurities.com

Raghvendra Goyal
raghvendra.goyal@icicisecurities.com

Key Financial Summary

Key Financials	FY19	FY20	FY21	FY22	5 year CAGR (FY17-22)	FY23E	FY24E	2 year CAGR (FY22-24E)
Net Sales	10,369.9	8,724.9	9,102.2	11,983.0	9.3%	14,422.7	15,785.6	14.8%
EBITDA	1,114.1	987.6	1,306.3	1,073.3	-1.1%	1,076.5	1,424.2	15.2%
EBITDA Margins (%)	10.7	11.3	14.4	9.0		7.5	9.0	
Net Profit	176.4	150.8	319.4	210.0	-11.0%	149.3	360.1	31.0%
EPS (₹)	7.8	6.1	13.0	8.5		6.1	14.6	
P/E	16.7	21.2	10.0	15.2		21.4	8.9	
RoNW (%)	7.7	6.5	11.9	7.4		5.0	11.0	
RoCE (%)	9.2	7.4	11.8	8.1		7.4	10.4	

Source: Company, ICICI Direct Research

Key takeaways of recent quarter & conference call highlights

Q1FY23 Results

- Among geographies, growth for the quarter was led by Mexican geographies. India revenues increased 9% QoQ to ₹ 3,058.6 crore while Mexico operations posted increase of 15% to ₹ 673.3 crore
- As per management commentary, the company continues to focus on all three channels i.e. OEM, aftermarket and exports and is taking price hikes across product categories. Also, focus on premiumisation would improve margins. Capacity utilisation for the quarter was ~90%
- On the margin front, gross margin decline was ~50 bps sequentially with savings across employee express & other expense being the reason for rise in EBITDA margins. India EBIT margins recovered ~96 bps QoQ to 4.7%, with Mexico EBIT margins up ~125 bps QoQ to 7%

Q1FY23 Earnings Conference Call highlights

- The management guided about recovery in automotive industry largely led by a revival in the CV space with bus segment benefiting from opening up of educational institutions and workplaces
- The company undertook debottlenecking activity in PCR segment in Q4FY23 in Banmore, Madhya Pradesh plant. Further, JKT is focusing on EV technology and developing products related to EV. The company has developed 139 tyre models for e-buses and e-trucks and ~75% tyre models developed for BS VI vehicles have been approved while 50% is for BS VI buses and EVs
- Cavendish revenue for Q1FY23 was at ₹ 942 crore vs. ₹ 848 crore in Q4FY22. Export sales are seen at ₹ 458 crore vs. ₹ 307 crore in Q4FY22. Mexican operation Q1FY23 revenue was at ₹ 673 crore vs. ₹ 586 crore in Q4FY22. Operating profit for Mexican operation was at ₹ 60 crore, up 36% YoY
- Utilisation at JK Tornell was at ~90% with similar utilisation levels for Indian operations as well
- Out of growth capex ~₹ 766 crore (including ₹ 530 crore for PCR capacity expansion and ~₹ 236 for TBR capacity expansion) ~40% would be incurred in FY23
- The company remains committed to deleveraging b/s with targets of ~₹ 400 crore of annual repayment with target to deduce term debt by ~₹ 1,200 crore by FY25E
- Raw material price hike was ~4-5% in Q1FY23 with further 3-4% price hike expected in Q2FY23. Correspondingly the company has taken ~4% price hike in Q1FY23 with further 2-3% price hike planned in Q2FY23

Out of total debt outstanding working capital loan is ~₹1,800 crores which remains elevated due to increased RM prices and is expected to reduce be ~₹200-300 crores post normalization of input prices.

Maintenance capex is expected to be around ₹150 crores per year.

In Mexican market RM led price hike was completely passed on to customers.

Peer comparison

Exhibit 1: Peer Comparison (tyres)

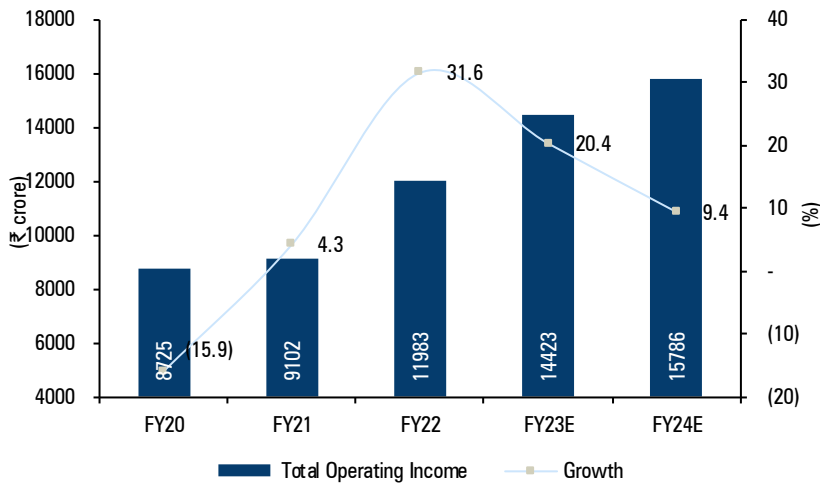
Company	CMP	TP	Rating	Mcap	EBITDA margin (%)			Debt to Equity (x)			RoCE (%)			EV/EBITDA (x)		
	₹	₹			₹ crore	FY22	FY23E	FY24E	FY22	FY23E	FY24E	FY22	FY23E	FY24E	FY22	FY23E
Apollo Tyres (APOTYR)	229	230	Buy	14,533	12.3	11.9	13.3	0.5	0.4	0.3	6.3	7.3	10.3	7.4	6.5	5.0
Balkrishna Inds (BALIND)	2,150	2,550	Buy	41,563	23.9	18.2	23.5	0.4	0.3	0.2	15.9	13.1	19.7	21.9	22.9	15.1
JK Tyre (JKTYRE)	130	135	Hold	3,201	9.0	7.5	9.0	1.8	1.8	1.7	8.1	7.4	10.4	7.6	7.8	5.9

Source: Company, ICICI Direct Research

With muted margin in the offering due to elevated commodity costs along with limited b/s de-leveraging due to fresh capex spend we maintain **HOLD** rating and await margin recovery before turning decisively positive.

Financial story in charts

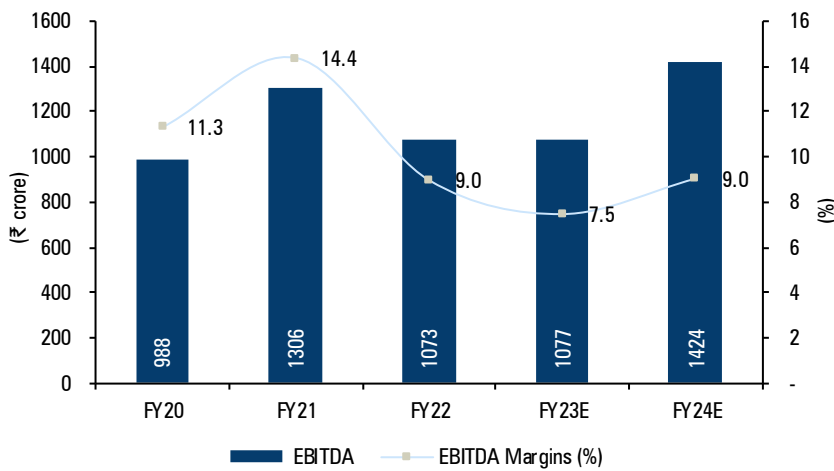
Exhibit 2: Topline trend



We expect sales to grow at a CAGR of 14.8% over FY22-24E to ₹ 15,786 crore in FY24E

Source: Company, ICICI Direct Research

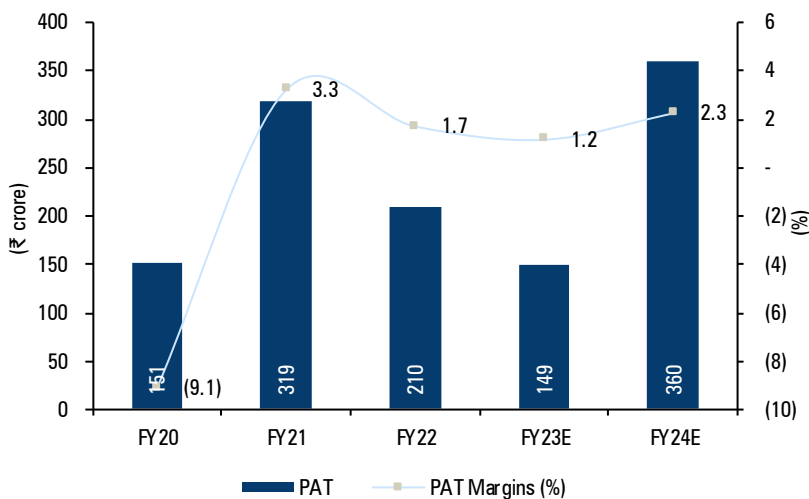
Exhibit 3: Margin trend



Margins are expected at 9.0% by FY24E vs. 7.5% expected in FY23E.

Source: Company, ICICI Direct Research

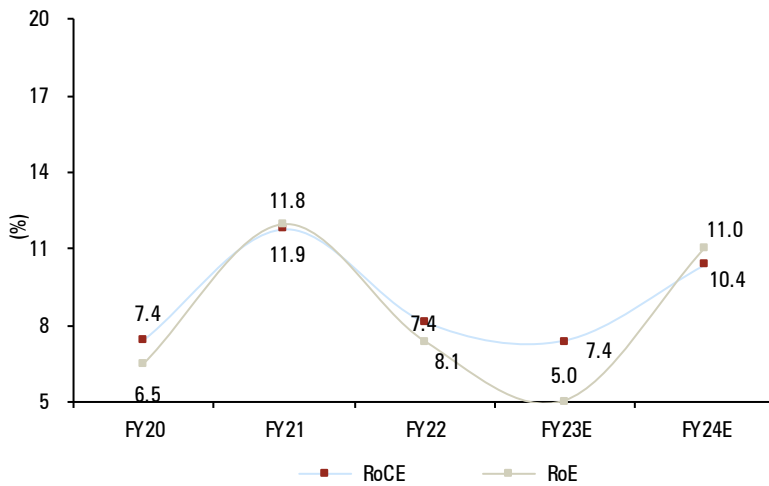
Exhibit 4: Trend in profitability



PAT is expected to grow at 31% CAGR over FY22-24E.

Source: Company, ICICI Direct Research

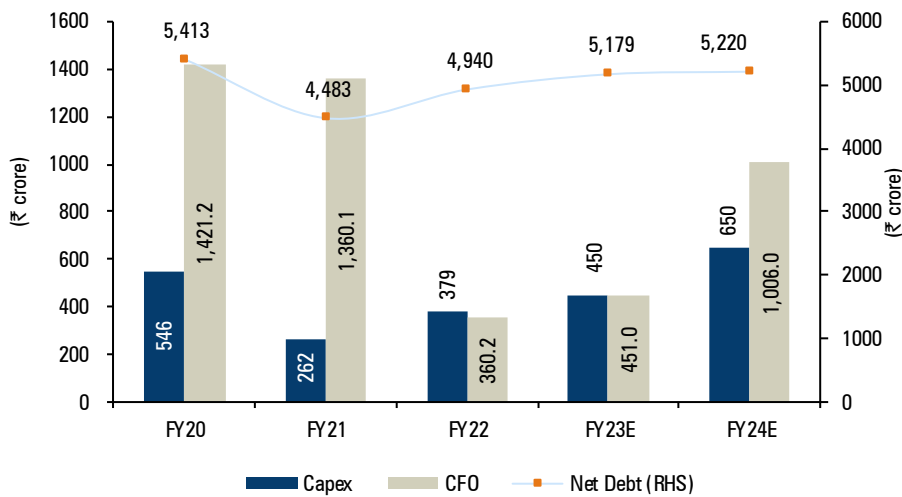
Exhibit 5: Trend in return ratios



Return ratios are seen rising to ~10-11% by FY24E

Source: Company, ICICI Direct Research

Exhibit 6: Debt, capex and CFO trend



Net debt is seen rising to ~₹ 5,200 crore by FY24E

Source: Company, ICICI Direct Research

Exhibit 7: Valuation Summary

	Sales (₹ cr)	Growth (%)	EPS (Diluted) (₹)	Growth (%)	PE (x)	EV/EBITDA (x)	RoNW (%)	RoCE (%)
FY19	10,369.9	25.4	7.8	167.1	16.7	7.9	7.7	9.2
FY20	8,724.9	(15.9)	6.1	(21.3)	21.2	8.7	6.5	7.4
FY21	9,102.2	4.3	13.0	111.8	10.0	5.9	11.9	11.8
FY22	11,983.0	31.6	8.5	-34.2	15.2	7.6	7.4	8.1
FY23E	14,422.7	20.4	6.1	-28.9	21.4	7.8	5.0	7.4
FY24E	15,785.6	9.4	14.6	141.3	8.9	5.9	11.0	10.4

Source: Company, ICICI Direct Research

Financial Summary

Exhibit 8: Profit and loss statement		₹ crore			
(Year-end March)	FY21	FY22	FY23E	FY24E	
Total operating Income	9,102.2	11,983.0	14,422.7	15,785.6	
Growth (%)	4.3	31.6	20.4	9.4	
Raw Material Expenses	5,468.7	8,039.3	10,166.3	10,880.5	
Employee Expenses	922.7	1,065.4	1,171.7	1,296.6	
Other Expenses	1,404.4	1,805.1	2,008.1	2,184.4	
Total Operating Expenditure	7,795.9	10,909.7	13,346.2	14,361.5	
EBITDA	1306.3	1073.3	1076.5	1424.2	
Growth (%)	32.3	-17.8	0.3	32.3	
Depreciation	386.7	385.4	418.3	457.8	
Interest	465.9	419.1	421.1	446.8	
Other Income	43.1	36.6	28.1	31.6	
Exceptional Items	-37.5	-3.6	34.5	0.0	
PBT	496.9	305.4	265.3	551.2	
Total Tax	200.9	108.7	84.0	192.9	
PAT	319.4	210.0	149.3	360.1	
Growth (%)	111.8	-34.2	-28.9	141.3	
EPS (₹)	13.0	8.5	6.1	14.6	

Source: Company, ICICI Direct Research

Exhibit 9: Cash flow statement		₹ crore			
(Year-end March)	FY21	FY22	FY23E	FY24E	
Profit after Tax	319.4	210.0	149.3	360.1	
Add: Depreciation & Int	852.5	804.5	839.3	904.5	
(Inc)/dec in Current Assets	150.5	-1,240.0	-1,073.8	-588.9	
Inc/(dec) in CL and Provisions	37.6	585.7	536.2	330.2	
CF from operating activities	1360.1	360.2	451.0	1006.0	
(Inc)/dec in Investments	-6.8	14.3	-10.0	-10.0	
(Inc)/dec in Fixed Assets	-262.2	-379.1	-450.0	-650.0	
Others	282.6	1.4	217.3	121.4	
CF from investing activities	13.6	-363.5	-242.7	-538.6	
Issue/(Buy back) of Equity	0.0	0.0	0.0	0.0	
Inc/(dec) in loan funds	-892.6	458.7	250.0	50.0	
Dividend paid & dividend tax	-49.3	-36.9	-27.1	-61.6	
Others (incl Interest costs)	-394.6	-416.6	-421.1	-446.8	
CF from financing activities	-1336.4	5.2	-198.1	-458.3	
Net Cash flow	37.3	1.9	10.2	9.1	
Opening Cash	136.5	173.8	175.7	185.9	
Closing Cash	173.8	175.7	185.9	195.0	

Source: Company, ICICI Direct Research

Exhibit 10: Balance Sheet		₹ crore			
(Year-end March)	FY21	FY22	FY23E	FY24E	
Liabilities					
Equity Capital	49.3	49.3	49.3	49.3	
Reserve and Surplus	2,623.5	2,799.1	2,921.3	3,219.8	
Total Shareholders funds	2672.8	2848.3	2970.5	3269.1	
Total Debt	4,656.5	5,115.2	5,365.2	5,415.2	
Deferred Tax Liability	368.3	405.1	487.6	533.7	
Other non-current liabilities	809.9	821.2	988.4	1,081.8	
Minority Interest	106.3	99.2	99.2	99.2	
Total Liabilities	8613.8	9289.1	9910.9	10399.0	
Assets					
Gross Block	10,061.9	10,626.9	10,926.9	11,776.9	
Less: Acc Depreciation	3,806.8	4,192.2	4,610.5	5,068.2	
Net Block	6255.1	6434.7	6316.4	6708.6	
Capital WIP	286.4	100.6	250.6	50.6	
Total Fixed Assets	6,541.5	6,535.2	6,567.0	6,759.2	
Investments	147.0	132.8	142.8	152.8	
Inventory	1,789.3	2,432.6	2,766.0	3,027.4	
Debtors	1,575.4	1,979.9	2,568.4	2,811.1	
Loans and Advances	136.0	208.8	251.4	275.1	
Other current assets	417.5	536.9	646.2	707.3	
Cash	173.8	175.7	185.9	195.0	
Total Current Assets	4,092.0	5,333.9	6,417.9	7,015.9	
Creditors	1,574.1	2,188.5	2,568.4	2,811.1	
Provisions	7.8	17.4	20.4	22.4	
Other current liabilities	791.0	752.7	905.9	991.5	
Total Current Liabilities	2,372.9	2,958.6	3,494.8	3,825.1	
Net Current Assets	1719.1	2375.3	2923.1	3190.8	
Others	207.5	235.8	237.5	209.3	
Application of Funds	8613.8	9289.1	9910.9	10399.0	

Source: Company, ICICI Direct Research

Exhibit 11: Key ratios					
(Year-end March)	FY21	FY22	FY23E	FY24E	
Per share data (₹)					
EPS	13.0	8.5	6.1	14.6	
Cash EPS	28.7	24.2	23.0	33.2	
BV	108.5	115.7	120.6	132.8	
DPS	2.0	1.5	1.1	2.5	
Cash Per Share	7.1	7.1	7.5	7.9	
Operating Ratios (%)					
EBITDA Margin	14.4	9.0	7.5	9.0	
PBIT / Net sales	10.1	5.7	4.6	6.1	
PAT Margin	3.3	1.7	1.2	2.3	
Inventory days	71.8	74.1	70.0	70.0	
Debtor days	63.2	60.3	65.0	65.0	
Creditor days	63.1	66.7	65.0	65.0	
Net Working Capital days	71.8	67.7	70.0	70.0	
Return Ratios (%)					
RoE	11.9	7.4	5.0	11.0	
RoCE	11.8	8.1	7.4	10.4	
RoIC	12.5	8.4	7.8	10.7	
Valuation Ratios (x)					
P/E	10.8	15.4	18.7	8.9	
EV / EBITDA	5.9	7.6	7.8	5.9	
EV / Net Sales	0.8	0.7	0.6	0.5	
Market Cap / Sales	0.4	0.3	0.2	0.2	
Price to Book Value	1.2	1.1	1.1	1.0	
Solvency Ratios					
Debt/Equity	1.7	1.8	1.8	1.7	
Current Ratio	2.5	2.3	2.4	2.4	
Quick Ratio	1.3	1.2	1.3	1.3	

Source: Company, ICICI Direct Research

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Reduce: -15% to -5%;

Sell: <-15%



Pankaj Pandey

Head – Research

pankaj.pandey@icicisecurities.com

ICICI Direct Research Desk,
ICICI Securities Limited,
1st Floor, Akruiti Trade Centre,
Road No 7, MIDC,
Andheri (East)
Mumbai – 400 093
research@icicidirect.com

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