



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

Updated May 08, 2023

22.23

Medium Risk

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

Source: Morningstar

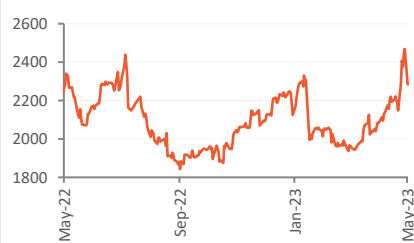
Company details

Market cap:	Rs. 44,154 cr
52-week high/low:	Rs. 2,451 / 1,682
NSE volume: (No of shares)	2.9 lakh
BSE code:	502355
NSE code:	BALKRISIND
Free float: (No of shares)	8.1 cr

Shareholding (%)

Promoters	58.3
FII	12.4
DII	20.3
Others	9.0

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	10.8	11.0	15.8	10.6
Relative to Sensex	7.2	8.1	14.6	-4.9

Sharekhan Research, Bloomberg

Balkrishna Industries Ltd

Destocking continued, Maintain Hold

Automobiles

Sharekhan code: BALKRISIND

Reco/View: Hold



CMP: Rs. 2,284

Price Target: Rs. 2,446



Upgrade



Maintain



Downgrade

Summary

- We retain a Hold rating on the stock with a revised target price of Rs. 2,446 due to continued destocking in European markets and premium valuation.
- The benefit of a decline in freight cost and partial clearance of high raw material inventory supported the operating performance in Q4FY23.
- A significant improvement would be led more by the volume uptick than a correction in input cost as the partial pass on cost benefits in a competitive market cannot be ruled out.
- Stock trades at a P/E multiple of 24.7 and EV/EBITDA multiple of 15.6x its FY2025E estimates.

Q4FY23 performance beat estimates as revenues exceed our estimates by 3% and EBITDA margin was 450 bps ahead of estimates on higher-than-expected correction in the input matrix. Revenues rose by 8.2% q-o-q to Rs. 2318 crore (vs estimate of Rs. 2249 crore) on the back of 9.3% q-o-q increase in volumes and 1.0% q-o-q decline in realizations. EBITDA increased by 83.0% q-o-q to Rs. 471 crore (against estimate of 355 crore). EBITDA margins rose by 830 bps q-o-q to 20.3% (vs expectation of 15.8%) on account of 220 bps q-o-q expansion in gross margins and 340 bps q-o-q contraction in freight rates as percentage of sales. The company has recorded a forex gain of Rs. 27 crore in Q4FY23 compared to forex loss of Rs. 87 crore. On excluding the unrealised forex loss of Rs. 3 crore the APAT has increased by 17.2% q-o-q to Rs. 253 crore (against estimate of Rs. 205 crore). With soft RM cost, correction in freight costs and sequential improvement in volumes, BKT has reported operating performance ahead of estimates. Going forward, the management has indicated that the destocking in its key markets is expected to be completed by June-July and shared a positive outlook for FY24 and shared its optimism for FY24E.

Key positives

- Volumes increased by 9.3% q-o-q to 72,676 MT.
- Gross margins expanded by 220 bps q-o-q to 49.1% on account of partial clearing of high-cost inventory of raw materials.
- Other expenses as percentage of sales contracted by 550 bps q-o-q due to sharp correction in freight cost. Freight cost came down by 32.2% q-o-q in Q4FY23.

Key negatives

- ASPs declined by 1% q-o-q to Rs. 318,889 /MT
- Destocking of inventory in its key market is continue and expected to be ease out by June-July
- Europe is expected to register subdued performance in H1FY24.

Management Commentary

- Destocking of channel inventory is expected to normalize by June- July 2023.
- The US and Indian market would continue to maintain their growth trend while European market is expected to recover in H2FY24.
- Correction in raw material costs and decline in freight cost to translate into 200- 300 bps EBITDA margin expansion from 20.3% reported in Q4FY23.

Our Call

Valuation – Maintain Hold rating with revised PT Rs. 2,446: While the management has not guided for a volume growth for FY24 but indicated that it has achieved the achievable capacity of 360,000 MT. Further, the US and Indian markets are expected to maintain their traction, but European market is assumed to register muted performance in H1FY24. The management expects European market to recover in H2FY24. Although RM cost and ocean freight has been coming down, but BKT would have to partially pass on the soft input cost to end-customers to remain competitive in the market. Hence the return of operating leverage led by volume recovery would be more necessitate than mere correction in input cost for return of EBITDA margin in previous upcycles. Given the end of a large capex cycle and benign RM basket coupled with its brand equity, the structural story is intact amidst near term clouds. Considering the near-term volatility in demand and challenging business situation in European market, we retain our Hold rating on the stock with a revised PT of Rs. 2,446.

Key Risks

Given BKT follows export-oriented business model and hence any adverse movement in the macro environment of overseas markets or forex fluctuation could impact the company's financial performance.

Valuation (Standalone)

Rs cr

Particulars	FY21	FY22	FY23P	FY24E	FY25E
Net sales (Rs cr)	5,758	8,267	9,811	10,701	11,904
Growth (%)	17.6	43.6	18.7	9.1	11.2
EBITDA (Rs cr)	1,786	1,976	1,716	2,440	2,821
OPM (%)	31.0	23.9	17.5	22.8	23.7
APAT (Rs cr)	1,141	1,383	1,144	1,511	1,784
Growth (%)	20.8	21.2	-17.2	32.1	18.1
AEPS (Rs)	59.0	71.5	59.2	78.2	92.3
P/E (x)	38.7	31.9	38.6	29.2	24.7
P/B (x)	7.4	6.4	5.8	5.1	4.5
EV/EBITDA (x)	24.4	22.6	26.4	18.5	15.6
RoE (%)	19.0	20.0	15.1	17.5	18.0
RoCE (%)	16.9	15.1	10.3	13.0	13.8

Source: Company; Sharekhan estimates

Demand trend: Near term concern on Europe continue

- ◆ Given a higher channel inventory and reduction in lead time due to better availability of containers the de stocking in the overseas market has been continue and the management hopes that the de-stocking would continue till June-July 2023.
- ◆ Retail demand has been better than wholesale volumes in European market.
- ◆ While Indian and US markets are expected to maintain their volume growth trajectory the Euro-pean market is expected to recover in H2FY24.

Capex of Rs. 500-600 crore scheduled for FY24

- ◆ Company has guided for a Rs. 500 – Rs. 600 crore of capex for Fy24 including maintenance capex of Rs. 250-300 crore.
- ◆ BKT targets to expand its market share in global from 5% currently to 10% in next 4-5 years and hence would have to schedule a next phase of capex, although the company has not decided the details of its long-term capex plan yet.

Margin trends: Cost correction would lead for EBITDA margin expansion in FY24

- ◆ Margin profile in Indian business is same as that of in overseas market.
- ◆ Raw material costs may come down by 1-2% in coming quarters.
- ◆ Ocean freight cost has been coming down and the company would pass on the correction in cost to the customers.
- ◆ Management expects the EBITDA margin to expand by 200 bps to 300 bps in FY24 from its reported EBITDA margin at 20.3% in Q4FY23.

Others

- ◆ With cash of Rs. 2000 crore and gross debt of Rs. 3200 crore the net cash stood at Rs. 1200 crore. The company has no plan to utilise the existing cash to repay debt as it has been making war chest for a suitable investment opportunity (if comes) in future.
- ◆ Currently the achievable manufacturing capacity has reached to 360,000 MT/ annum.
- ◆ Pricing gap between BKT's products and key players in overseas market has come down to 12- 15%.
- ◆ Not facing any competition from Chinese players in overseas markets.

Results (Standalone)

Particulars	Rs cr				
	Q4FY23	Q4FY22	YoY%	Q3FY23	QoQ%
Revenues	2,318	2,374	-2.4	2,142	8.2
Total operating expenses	1,847	1,874	-1.5	1,885	-2.0
EBITDA	471	500	-5.7	257	83.0
Depreciation	151	117	29.8	145	4.5
Interest	25	2	1,067.8	14	83.8
Other income	54	108	-49.9	43	25.2
PBT	348	488	-28.7	142	145.6
Tax	93	115	-19.1	42	119.8
Reported PAT	256	374	-31.6	100	156.5
Adjusted PAT	253	390	-35.0	216	17.2
Adjusted EPS	13.1	20.2	-35.0	11.2	17.2

Source: Company; Sharekhan Research

Key ratios (Standalone)

Particulars	Rs cr				
	Q4FY23	Q4FY22	YoY (bps)	Q3FY23	QoQ (bps)
Gross margin (%)	49.1	53.5	-440	46.9	220
EBIDTA margin (%)	20.3	21.0	-70	12.0	830
Net profit margin (%)	10.9	16.4	-550	10.1	80
Effective tax rate (%)	26.6	23.5	320	29.8	-310

Source: Company; Sharekhan Research

Outlook and Valuation

■ Sector View – Indian tyre market is recovering, destocking likely to complete soon in overseas market

We expect the domestic tyres industry to naturally benefit from the sharp recovery in automobile sales post normalisation of the economy in India. The automobile sector has witnessed broad-based recovery across segments, driven by pent-up demand, preference for personal mobility 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. Further the de stocking in overseas market is likely to complete soon, given overseas markets are observing de stocking due to reduction in overseas transportation due to increase in availability of containers.

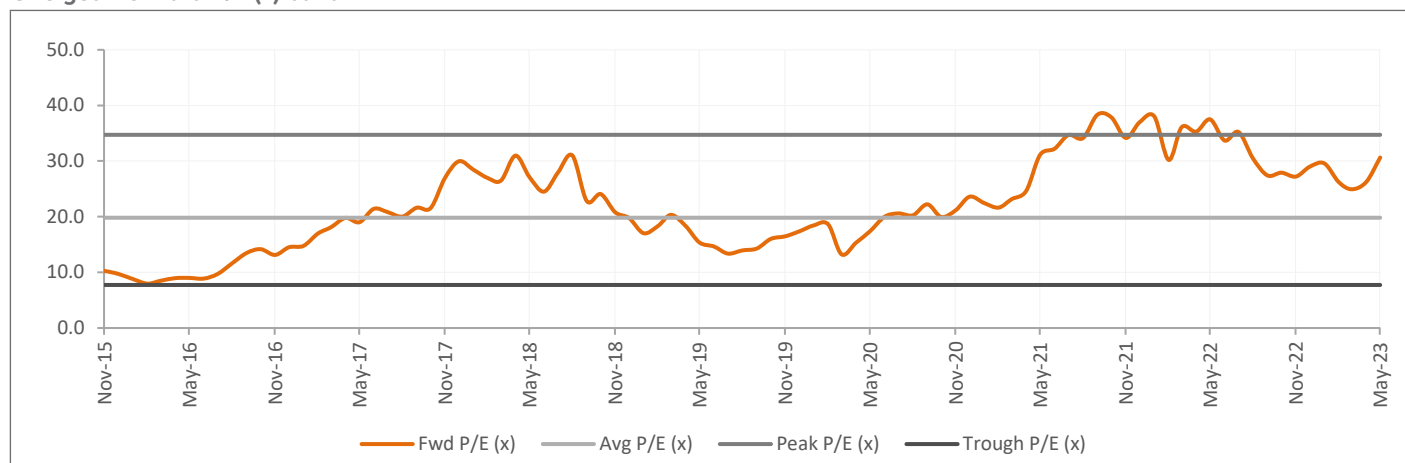
■ Company Outlook – Cautious outlook on demand, focus on profitability

BKT remains a dominant player in the global OHT segment supported by its strong distribution network, quality of product and relatively low-cost production, however BKT is expected to face demand headwinds in near term owing to ongoing destocking in European market. The company expects that correction in RM basket and decline in freight cost would help it in registering better operating performance in FY24. The US market is performing better than that of European market. In Europe agri segment has more impacted than industrial segment. The manufacturing capacity has reached to 360,000 MT/ annum.

■ Valuation – Maintain Hold rating with revised PT Rs. 2,446

While the management has not guided for a volume growth for FY24 but indicated that it has achieved the achievable capacity of 360,000 MT. Further, the US and Indian markets are expected to maintain their traction, but European market is assumed to register muted performance in H1FY24. The management expects European market to recover in H2FY24. Although RM cost and ocean freight has been coming down, but BKT would have to partially pass on the soft input cost to end-customers to remain competitive in the market. Hence the return of operating leverage led by volume recovery would be more necessitate than mere correction in input cost for return of EBITDA margin in previous upcycles. Given the end of a large capex cycle and benign RM basket coupled with its brand equity, the structural story is intact amidst near term clouds. Considering the near-term volatility in demand and challenging business situation in European market, we retain our Hold rating on the stock with a revised PT of Rs. 2,446.

One-year forward P/E (x) band



Source: Sharekhan Research

Peer Comparison

Particulars	CMP	P/E (x)			EV/EBITDA (x)			RoCE (%)		
	Rs/Share	FY22	FY23E	FY24E	FY22	FY23E	FY24E	FY22	FY23E	FY24E
Balkrishna Industries	2,284	31.9	38.6	29.2	22.6	26.4	18.5	15.1	10.3	13.0
Apollo Tyres	391	38.5	23.0	16.5	11.8	9.1	7.6	5.1	7.6	9.1

Source: Company, Sharekhan estimates

About company

BKT 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. BKT is a global player present in Europe, US, and India. While European markets account for ~50% of sales, US and India account for 18% and 21% 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 moulding plant in Dombivli (near Mumbai). The manufacturing capacity has reached at 3.6 lakh MT by end-FY2023.

Investment theme

BKT 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 stronghold 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 a 10% market share globally in the tyres market, with new product launches and expansion into new geographies. The company is self-reliant in carbon black along with multiple sourcing arrangements for other raw materials, which keep its margins firm. The company has a robust balance sheet strength. Rising concerns related with European market may impact its performance in near term.

Key Risks

Given BKT follows export-oriented business model and hence any adverse movement in the macro environment of overseas markets or forex fluctuation could impact the company's financial performance.

Additional Data

Key management personnel

Arvind Poddar	Chairman & Managing Director
Rajiv Poddar	Joint Managing Director
Vipul Shah	Wholetime Director & Company Secretary
Madhu Sudan Bajaj	Chief Financial Officer

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Poddar Rajiv A	27.7
2	VKP Enterprises LLP	25.0
3	Life Insurance Corp of India	4.3
4	Poddar Khushboo	3.9
5	HDFC Asset Management Co Ltd	2.7
6	Kotak Mahindra Asset Management Co Ltd/India	2.5
7	Norges Bank	1.7
8	Vanguard Group Inc/The	1.6
9	Poddar Rishabh Sureshkumar	1.4
10	BlackRock Inc	1.4

Source: Bloomberg

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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 deteriorating 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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Compliance Officer: Ms. Binkle Oza; Tel: 022-61169602; email id: complianceofficer@sharekhan.com

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