

SELL

TP: Rs 67,000 | ▼ 19%

MRF

| Auto Components

| 07 June 2021

Margin headwinds to persist; maintain SELL

- MRF's Q4 revenue grew 4% QoQ to Rs 47bn, EBITDA margin shrank 530bps on gross margin pressure and adj. PAT fell 38% QoQ to Rs 3.2bn
- We expect EBITDA margin to remain stressed led by RM inflation, higher share of CV tyres and rising OEM share in sales
- We maintain our EPS estimates and continue to value MRF at 22x FY23E P/E for a Mar'22 TP of Rs 67,000 – we retain SELL

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Q4 gross margin plummets: MRF's revenue was in line with projections at Rs 47.4bn (+4% QoQ). Gross margin fell sharply by 630bps QoQ led by rising raw material cost pressures, fuelling a 530bps decline in EBITDA margin to 15.7% (14.2% est.). EBITDA decreased 23% QoQ to Rs 7.5bn and adj. PAT fell 38% QoQ to Rs 3.2bn.

FY21 performance muted: MRF's revenue growth was flattish in FY21 at Rs 159.2bn. EBITDA margin expanded 370bps YoY, supported by a 150bps rise in gross margin as raw material prices remained soft in H1FY21. Higher depreciation (+29% YoY) and lower other income (-37% YoY) led to a 10% dip in adj. PAT to Rs 12.5bn. MRF has paid out dividend of Rs 150/sh for the year.

Near-term headwinds: With a 12% QoQ cost rise in the raw material basket in Q4, a further expected increase of ~10% sequentially in Q1FY22 (per industry experts) and the inability of tyre companies to fully pass on the cost burden, we anticipate gross margin deterioration for our tyre coverage. We forecast a gross margin decline of ~350bps for MRF over FY21-FY23 (from 42% in FY21).

Maintain SELL: While our revenue estimates for FY22/FY23 are in line with consensus, we are ~12% below on EBITDA as we bake in 200bps lower gross margins due to raw material cost pressure and inability of tyre companies to fully pass on the cost. Our EPS estimates remain 25-30% below the street.

We continue to expect MRF to clock a revenue/EBITDA/earnings CAGR of 16%/6%/2% over FY21-FY23 and maintain our Mar'22 TP at Rs 67,000, based on an unchanged 22x target P/E. Our target multiple is in line with the stock's long-term average as well as the premium it has historically commanded against peers. SELL.

Key changes

Target	Rating
◀ ▶	◀ ▶

Ticker/Price	MRF IN/Rs 82,401
Market cap	US\$ 4.8bn
Free float	72%
3M ADV	US\$ 25.6mn
52wk high/low	Rs 98,600/Rs 55,300
Promoter/FPI/DII	28%/5%/14%

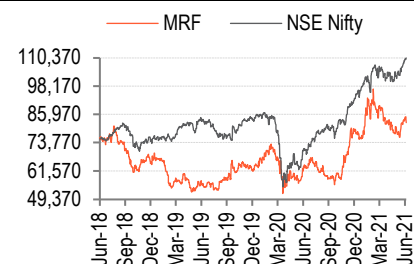
Source: NSE | Price as of 7 Jun 2021

Key financials

Y/E 31 Mar	FY21P	FY22E	FY23E
Total revenue (Rs mn)	159,214	192,643	213,721
EBITDA (Rs mn)	28,947	28,662	32,381
Adj. net profit (Rs mn)	12,491	11,741	13,060
Adj. EPS (Rs)	2,945.9	2,769.2	3,080.1
Consensus EPS (Rs)	2,946.0	3,514.0	4,332.0
Adj. ROAE (%)	9.5	8.2	8.4
Adj. P/E (x)	28.0	29.8	26.8
EV/EBITDA (x)	12.3	12.2	10.9
Adj. EPS growth (%)	(10.5)	(6.0)	11.2

Source: Company, Bloomberg, BOBCAPS Research | P – Provisional

Stock performance



Source: NSE



Fig 1 – Quarterly performance

(Rs mn)	Q4FY21	Q4FY20	YoY (%)	Q3FY21	QoQ (%)	FY21	FY20	YoY (%)
Net Revenues	47,377	36,252	30.7	45,668	3.7	159,214	159,911	(0.4)
Total Income (A)	47,377	36,252	30.7	45,668	3.7	159,214	159,911	(0.4)
Operating Expenses:								
Raw materials consumed	29,139	20,724	40.6	25,230	15.5	92,288	95,089	(2.9)
Employee Expenses	3,521	3,441	2.3	3,929	(10.4)	13,879	13,205	5.1
Other Expenses	7,261	6,387	13.7	6,877	5.6	24,100	28,380	(15.1)
Total Expenditure (B)	39,921	30,553	30.7	36,036	10.8	130,267	136,674	(4.7)
EBITDA (A-B)	7,456	5,699	30.8	9,632	(22.6)	28,947	23,237	24.6
Other Income	565	575	(1.7)	634	(10.8)	2,072	3,305	(37.3)
Depreciation	2,970	2,665	11.5	2,831	4.9	11,369	9,806	29
EBIT	5,051	3,610	39.9	7,435	(32.1)	19,650	16,736	17.4
Finance Costs	745	692	7.8	638	16.9	2,647	2,743	0
PBT before excep items	4,306	2,918	47.6	6,797	(36.6)	17,003	13,993	21.5
PBT after excep items	4,306	2,918	47.6	6,797	(36.6)	17,003	13,993	21.5
Tax expense	1,134	(3,777)	(130.0)	1,680	(32.5)	4,512	43	10296.5
Reported PAT	3,173	6,695	(52.6)	5,117	(38.0)	12,491	13,950	(10.5)
Adjusted PAT	3,173	6,695	(52.6)	5,117	(38.0)	12,491	13,950	(10.5)

Source: Company, BOBCAPS Research

Fig 2 – Key parameters

(%)	Q4FY21	Q4FY20	YoY (bps)	Q3FY21	QoQ (bps)	FY21	FY20	YoY (bps)
Gross margin	38.5	42.8	(434)	45	(626)	42.0	40.5	150
EBITDA margin	15.7	15.7	2	21	(535)	18.2	14.5	365
EBIT margin	10.7	10.0	70	16	(562)	12.3	10.5	188
PBT margin	9.1	8.0	104	15	(579)	10.7	8.8	193
Tax rate	26.3	(129.4)	15574	25	161	26.5	0.3	2623
Adj PAT margin	6.7	18.5	(1,177)	11	(451)	7.8	8.7	(88)

Source: Company, BOBCAPS Research

Valuation methodology

While our revenue estimates for FY22/FY23 are in line with consensus, we are ~12% below on EBITDA as we bake in 200bps lower gross margins due to raw material cost pressure. Our EPS estimates remain 23-30% below the street.

We continue to expect MRF to clock a revenue/EBITDA/earnings CAGR of 16%/6%/2% over FY21-FY23 and maintain our Mar'22 TP at Rs 67,000, based on an unchanged 22x target P/E. Our target multiple is in line with the stock's long-term average as well as the premium it has historically commanded against peers. SELL.

Fig 3 – Peer comparison

Company	Rating	Target Price (Rs)	Revenue CAGR FY21-23E (%)	EPS (Rs)		ROE (%)		Target P/E (x)
				FY22E	FY23E	FY22E	FY23E	
Apollo Tyres	SELL	140	11	7.6	8.9	4.0	4.6	16
Balkrishna Industries	SELL	1,550	12	64.8	70.3	17.9	16.8	22
CEAT	SELL	840	16	57.5	59.9	7.0	6.8	14
JK Tyres	SELL	90	16	8.0	12.6	6.6	9.6	7
MRF	SELL	67,000	16	2,769	3,080	8.5	8.7	22
TVS Srichakra	SELL	1,200	17	75.0	85.9	6.7	7.3	14

Source: BOBCAPS

Key risks

Key upside risks to our estimates are:

- above-expected volume growth,
- softening raw material prices, and
- market share gains

Financials

Income Statement

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21P	FY22E	FY23E
Total revenue	158,370	159,911	159,214	192,643	213,721
EBITDA	22,504	23,237	28,947	28,662	32,381
Depreciation	8,063	9,806	11,369	13,432	15,668
EBIT	18,616	16,736	19,650	17,146	18,909
Net interest inc./(exp.)	(2,528)	(2,743)	(2,647)	(1,449)	(1,449)
Other inc./(exp.)	4,175	3,305	2,072	1,917	2,197
Exceptional items	(1,356)	0	0	0	0
EBT	14,733	13,993	17,003	15,697	17,460
Income taxes	5,120	43	4,512	3,956	4,400
Extraordinary items	0	0	0	0	0
Min. int./Inc. from assoc.	0	0	0	0	0
Reported net profit	9,613	13,950	12,491	11,741	13,060
Adjustments	1,356	0	0	0	0
Adjusted net profit	10,969	13,950	12,491	11,741	13,060

Balance Sheet

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21P	FY22E	FY23E
Accounts payables	23,276	23,401	42,449	49,803	52,570
Other current liabilities	21,389	24,404	26,970	35,468	38,100
Provisions	1,571	3,422	4,110	4,110	4,110
Debt funds	18,675	10,210	8,526	8,526	8,526
Other liabilities	2,441	5,781	4,969	4,969	4,969
Equity capital	42	42	42	42	42
Reserves & surplus	106,491	120,001	131,746	143,211	155,962
Shareholders' fund	106,533	120,044	131,789	143,253	156,005
Total liab. and equities	173,885	187,263	218,811	246,127	264,279
Cash and cash eq.	601	11,069	1,053	1,150	1,131
Accounts receivables	23,616	22,570	22,205	26,970	29,921
Inventories	29,509	28,527	28,803	36,602	38,470
Other current assets	1,775	151	94	193	214
Investments	38,484	15,402	58,762	54,762	62,762
Net fixed assets	67,675	88,492	93,911	110,479	116,811
CWIP	14,032	17,346	10,010	12,000	11,000
Intangible assets	0	0	0	0	0
Deferred tax assets, net	(8,392)	(4,278)	(3,785)	(3,785)	(3,785)
Other assets	6,585	7,985	7,756	7,756	7,756
Total assets	173,885	187,263	218,811	246,127	264,279

Cash Flows

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21P	FY22E	FY23E
Cash flow from operations	9,422	33,778	46,187	27,896	25,642
Capital expenditures	(18,228)	(33,937)	(9,453)	(31,990)	(21,000)
Change in investments	2,980	23,082	(43,360)	4,000	(8,000)
Other investing cash flows	4,175	3,305	2,072	1,917	2,197
Cash flow from investing	(11,073)	(7,549)	(50,741)	(26,073)	(26,803)
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	1,669	(8,465)	(1,684)	0	0
Interest expenses	(2,528)	(2,743)	(2,647)	(1,449)	(1,449)
Dividends paid	0	(509)	(636)	(277)	(308)
Other financing cash flows	1,724	(4,044)	(493)	0	0
Cash flow from financing	866	(15,761)	(5,461)	(1,726)	(1,757)
Chg in cash & cash eq.	(786)	10,468	(10,015)	97	(2,918)
Closing cash & cash eq.	601	11,069	1,053	1,150	1,131

Per Share

Y/E 31 Mar (Rs)	FY19A	FY20A	FY21P	FY22E	FY23E
Reported EPS	2,587.0	3,290.0	2,945.9	2,769.2	3,080.1
Adjusted EPS	2,587.0	3,290.0	2,945.9	2,769.2	3,080.1
Dividend per share	0.0	100.0	150.0	65.3	72.6
Book value per share	25,125.7	28,312.1	31,082.2	33,786.1	36,793.6

Valuations Ratios

Y/E 31 Mar (x)	FY19A	FY20A	FY21P	FY22E	FY23E
EV/Sales	2.3	2.3	2.2	1.8	1.7
EV/EBITDA	16.1	15.6	12.3	12.2	10.9
Adjusted P/E	31.9	25.0	28.0	29.8	26.8
P/BV	3.3	2.9	2.7	2.4	2.2

DuPont Analysis

Y/E 31 Mar (%)	FY19A	FY20A	FY21P	FY22E	FY23E
Tax burden (Net profit/PBT)	74.4	99.7	73.5	74.8	74.8
Interest burden (PBT/EBIT)	79.1	83.6	86.5	91.5	92.3
EBIT margin (EBIT/Revenue)	11.8	10.5	12.3	8.9	8.8
Asset turnover (Rev./Avg TA)	130.5	121.3	113.2	127.6	131.0
Leverage (Avg TA/Avg Equity)	1.2	1.2	1.1	1.1	1.1
Adjusted ROAE	10.8	12.3	9.9	8.5	8.7

Ratio Analysis

Y/E 31 Mar	FY19A	FY20A	FY21P	FY22E	FY23E
YoY growth (%)					
Revenue	7.2	1.0	(0.4)	21.0	10.9
EBITDA	1.0	3.3	24.6	(1.0)	13.0
Adjusted EPS	0.4	27.2	(10.5)	(6.0)	11.2
Profitability & Return ratios (%)					
EBITDA margin	14.2	14.5	18.2	14.9	15.2
EBIT margin	11.8	10.5	12.3	8.9	8.8
Adjusted profit margin	6.9	8.7	7.8	6.1	6.1
Adjusted ROAE	10.3	11.6	9.5	8.2	8.4
ROCE	9.4	12.0	9.9	8.3	8.4
Working capital days (days)					
Receivables	52	53	51	47	49
Inventory	59	66	66	62	64
Payables	76	90	130	142	142
Ratios (x)					
Gross asset turnover	0.6	0.8	0.9	0.9	0.9
Current ratio	1.2	1.2	0.7	0.7	0.7
Net interest coverage ratio	7.4	6.1	7.4	11.8	13.0
Adjusted debt/equity	0.2	0.1	0.1	0.1	0.1

Source: Company, BOBCAPS Research | Note: TA = Total Assets

Disclaimer

Recommendation scale: Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

ADD – Expected return from >+5% to +15%

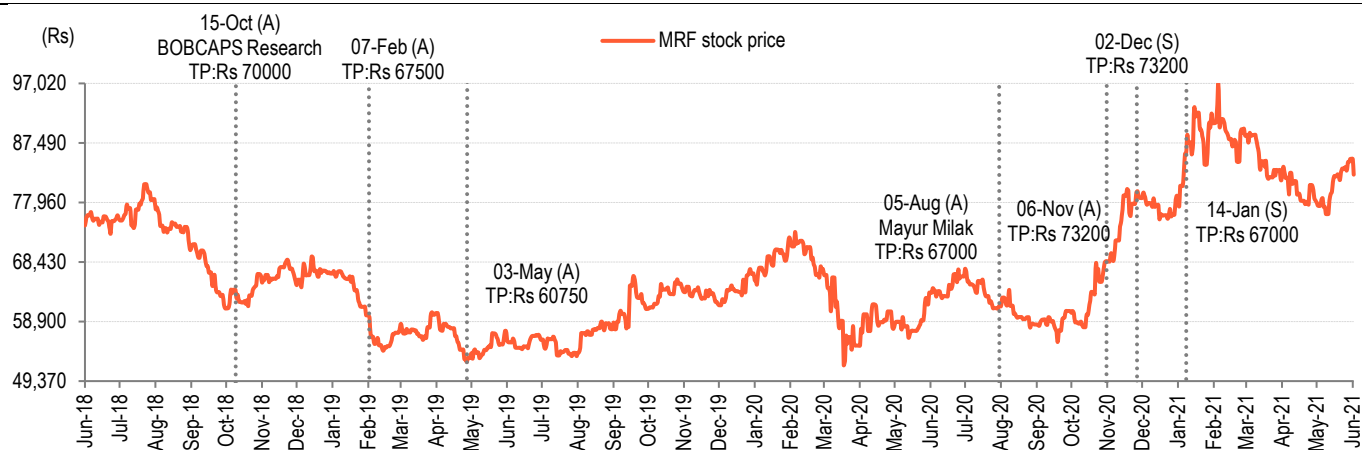
REDUCE – Expected return from -5% to +5%

SELL – Expected return <-5%

Note: Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

Our recommendation scale does not factor in short-term stock price volatility related to market fluctuations. Thus, our recommendations may not always be strictly in line with the recommendation scale as shown above.

Ratings and Target Price (3-year history): MRF (MRF IN)



B – Buy, A – Add, R – Reduce, S – Sell

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