

Muted margin, volume commentary amid uncertain global economic cues, recovery seen from FY24E...

About the stock: Balkrishna Industries (BIL) is the leader in the niche tyre segment used in heavy machinery for mining and agriculture purposes.

- Exports form lion's share of its sales at ~80% of its revenues
- Channel mix: replacement account for ~70% while OEM share is pegged at ~28%. Agriculture accounts for ~63% of volumes with OTR share at ~34%
- It has consistently operated with high margins & return ratios

Q3FY23 Results: BIL reported a dismal set of numbers for Q3FY23.

- Standalone net sales for the quarter were at ₹ 2,142 crore, down 20.8% QoQ
- Tonnage for the quarter was at 66,480 tonnes, down 15.7% QoQ
- EBITDA margins in Q3FY23 came in at 12%, down 443 bps QoQ
- PAT was at ₹ 99.6 crore, down 75% QoQ, impacted by notional forex loss

What should investors do? BIL's share price has grown at 13.5% CAGR in the past five years, (~₹ 1,123 in February 2018), vastly outperforming the Nifty Auto index.

- We downgrade the stock from BUY to **HOLD** amid slower than expected margin and volume recovery amidst uncertain global economic cues

Target Price and Valuation: Introducing FY25E, we now value BIL at revised target price of ₹ 2,170 i.e., 25x P/E on average FY24-25E EPS of ~₹ 87 (earlier TP ₹ 2,200).

Key triggers for future price performance:

- Demand recovery in key international markets and across segments as recession fears fades away. Strong manufacturing capabilities and distribution network to result in 5.5% sales volume CAGR over FY22-25E
- Persistent focus to attain global market share of ~10% vs. ~5-6% currently
- With thoughtful capacity expansion, cost efficiencies & backward integration at bay we expect sales, PAT to grow at a CAGR of 11.5%, 9.5%, respectively, over FY22-25E. Margins are seen recovering to 24% in FY25E
- Strong cash flow generation of ~₹ 1,000+ crore amid calibrated capex spend to result in healthy FCF generation and consequent b/s deleveraging

Alternate Stock Idea: Leaving aside Balkrishna Industries, we like M&M.

- Focused on prudent capital allocation, UV differentiation & EV proactiveness
- BUY with a target price of ₹ 1,665



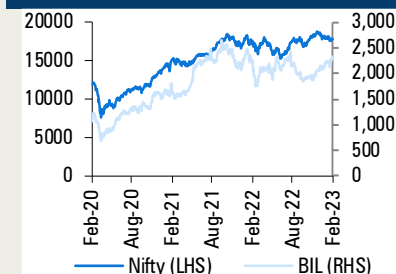
Particulars

Particular	₹ crore
Market Capitalization	39,823
Total Debt (FY22)	2,443
Cash & Inv (FY22)	1,933
EV (₹ Crore)	40,333
52 week H/L (₹)	2451 / 1682
Equity capital (₹ crore)	38.7
Face value (₹)	2.0

Shareholding pattern

	Mar-22	Jun-22	Sep-22	Dec-22
Promoter	58.3	58.3	58.3	58.3
FII	14.1	14.3	13.0	12.5
DII	11.8	11.2	18.8	20.1
Other	15.9	16.2	9.9	9.1

Price Chart



Recent event & key risks

- Posted muted Q3FY23
- Key Risk:** (i) Sooner than expected sales volume recovery going forward, (ii) delay in margin recovery despite benign commodity price outlook (RM)

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Key Financial Summary

Key Financials	FY19	FY20	FY21	FY22	5 year CAGR (FY17-22)	FY23E	FY24E	FY25E	3 year CAGR (FY22-25E)
Net Sales	5,244.5	4,782.5	5,757.9	8,266.7	16.9%	9,686.6	10,433.0	11,455.7	11.5%
EBITDA	1,311.1	1,249.3	1,785.5	1,975.5	11.8%	1,475.0	2,298.7	2,744.7	11.6%
EBITDA Margins (%)	25.0	26.1	31.0	23.9		15.2	22.0	24.0	
Net Profit	782.0	945.0	1,155.4	1,410.7	14.6%	1,007.9	1,499.2	1,853.9	9.5%
EPS (₹)	40.5	48.9	59.8	73.0		52.1	77.5	95.9	
P/E	50.9	42.1	34.5	28.2		39.5	26.6	21.5	
RoNW (%)	16.7	18.8	19.2	20.4		13.2	17.3	18.7	
RoCE (%)	16.7	14.4	19.3	15.9		8.6	15.8	19.2	

Key takeaways of recent quarter & conference call highlights

Q3FY23 Results:

- Balkrishna Industries (BIL) reported a dismal performance in Q3FY23
- Standalone revenues at ₹ 2,142 crore, down 20.8% QoQ. Tonnage for the quarter was down ~15.7% QoQ to 66,480 MT
- EBITDA in Q3FY23 was at ₹ 257.3 crore with corresponding EBITDA margins at 12% down 443 bps QoQ. Gross margin erosion was sharp at ~250 bps QoQ and was further aggravated by negative operating leverage
- Consequent PAT for the quarter came in at ₹ 99.6 crore, down 75.3% QoQ, primarily tracking lower-than-expected margins and lower other income. Lower PAT was also driven by forex loss amounting to ₹ 88 crore reported for Q3FY23 against profit on both QoQ as well as YoY basis
- The company announced an interim dividend of ₹ 4/ share

BIL- ESG Disclosure Score*			
Score	FY20	FY21	FY22
Environmental	15.5	15.5	16.0
Social	21.8	21.8	21.8
Governance	78.6	78.6	78.6
Overall ESG Score	38.7	38.7	38.8

Source: Bloomberg, ICICI Direct Research, *Score ranges from 0 - 100 with a higher score indicating higher ESG disclosures

Q3FY23 Earnings Conference Call highlights

- The management informed about high channel inventory in key foreign market impacting margins and expects destocking to continue in Q4FY23E also, with meaningful margin recovery to extent of 300 bps to be witnessed in FY24E incorporating RM benefits. Further, the management expects lower raw material and freight costs, better hedge rate, better end market situation to lead to a margin recovery in FY24
- Management commentary on end demand remained steady with channel inventory dampening the overall volume offtake. The management informed about the demand scenario being relatively better in North America but recession fears continue to impact demand. Overall the management expects low single digit volume growth in the near term (QoQ in Q4FY23)
- During the quarter, the company informed about passing on of surcharge on freight cost to end customers leading to lower ASPs by ~6% QoQ. However, a steep reduction in freight cost led to a slight recovery in overall margins and expects this benefit to continue further till Q1FY24E
- The management said domestic demand was stable during Q3FY23
- Inventory at dealer levels is currently prevailing at ~2.5 months vs. about three months as of Q2FY23 end with target to reduce it to about two months
- The company has done ~₹ 1,300 crore of capex in 9MFY23E with minimal capex expected in Q4FY23E. Further, the company plans to spend ~₹ 300-400 crore in FY24E
- BIL has not taken price hike, nor did it moderated its prices during Q3FY23
- Carbon black constituted ~5% of sales in Q3FY23
- Current RM inventory was at 60 days with target of reducing it to 45 days
- Average rate of borrowing on short to long term debt was at 3.5-4%
- Net debt as of December 31, 2022 was at ~₹ 1,350 crore

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	FY24E
Apollo Tyres (APOTYR)	330	390	Buy	20,956	12.3	13.3	15.5	0.5	0.4	0.3	6.3	10.0	13.8	9.9	7.6	5.9
Balkrishna Inds (BALIND)	2,060	2,170	Hold	39,823	23.9	15.2	22.0	0.4	0.4	0.2	15.9	8.6	15.8	21.0	28.6	17.9
JK Tyre (JKTYRE)	155	190	Buy	3,817	9.0	9.0	10.8	1.8	1.7	1.3	8.1	10.5	13.5	8.2	6.7	5.1

Source: Company, ICICI Direct Research

We assign HOLD rating to BIL amid company specific demand and margin recovery issues vs. other tyre players reaping the timely benefits on RM price decline.

Exhibit 2: Variance Analysis

	Q3FY23	Q3FY23E	Q3FY22	YoY (%)	Q2FY23	QoQ (%)	Comments
Total Operating Income	2,142.3	2,345.4	2,030.0	5.5	2,704.3	-20.8	Topline came in below our estimates tracking sequential 6% decline in ASPs amid ~16% QoQ volume decline
Raw Material Expenses	1,138.0	1,180.0	965.9	17.8	1,369.0	-16.9	RM as a percentage of sales came in higher by 250 bps QoQ to 53.1% but in ₹/kg it was broadly flat on QoQ basis
Employee Expenses	99.9	93.8	96.7	3.3	102.2	-2.3	
Other expenses	647.2	703.6	524.0	23.5	788.5	-17.9	Other expenses were a tad higher at 30.2% of sales
EBITDA	257.3	367.9	443.4	-42.0	444.5	-42.1	
EBITDA Margin (%)	12.0	15.7	21.8	-984 bps	16.4	-443 bps	EBITDA margins came in as a big negative surprise given QoQ decline in ASPs as well as rise in other costs
Other Income	43.1	119.1	111.6	-61.4	226.0	-80.9	
Depreciation	144.9	133.9	114.5	26.6	134.1	8.1	Depreciation was at a tad higher than anticipated
Interest	13.6	3.6	1.8	659.8	4.3	215.5	
Tax	42.2	88.1	110.1	-61.7	128.3	-67.1	
PAT	99.6	261.5	328.6	-69.7	403.8	-75.3	PAT came in much lower due to lower than anticipated margin profile as well as forex loss at play (unrealised)
EPS	5.2	13.5	17.0	-69.7	20.9	-75.3	
Key Metrics							
Volume (MT)	66,480	66,804	70,320	-5.5	78,872	-15.7	Sales volume for Q3FY23 was at 66,480 tonne, down 16% QoQ tracking inventory destocking at its key export market

Source: Company, ICICI Direct Research

Exhibit 3: Change in estimates

₹ Crore	FY23E			FY24E			FY25E		Comments
	Old	New	% Change	Old	New	% Change	Introduced		
Revenue	10,466	9,687	-7.4	11,893	10,433	-12.3	11,456	Lower our topline estimates for FY23-24E tracking 9MFY23 performance and management commentary on continued inventory de-stocking at its key markets. Introduce FY25E numbers. We expect topline to grow at a CAGR of 11.5% over FY22-25E	
EBITDA	1,879	1,475	-21.5	2,806	2,299	-18.1	2,745		
EBITDA Margin (%)	18.0	15.2	-272 bps	23.6	22.0	-156 bps	24.0	Lower margin estimates for FY23-24E tracking muted Q2FY23 results. Introduce FY25E margins at 24%	
PAT	1,400	1,008	-28.0	1,935	1,499	-22.5	1,854		
EPS (₹)	72	52	-28.0	100	78	-22.5	96	Decline in topline and margin estimates leads to high double digit earnings downgrade for FY23-24E. Introduce FY25E. We expect PAT to grow at a CAGR of 9.5% over FY22-25E	

Source: ICICI Direct Research

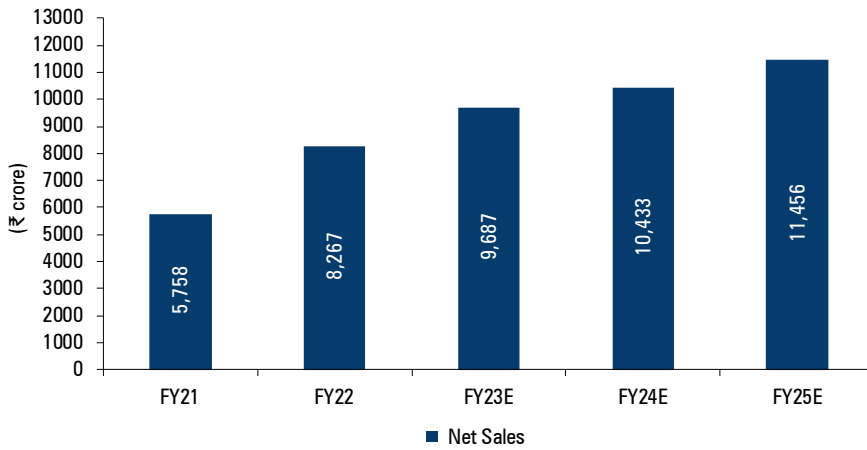
Exhibit 4: Assumptions

	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E	Comments
Capacity (MT)	300,000	300,000	300,000	280,000	285,000	335,000	360,000	360,000	Total volumes at the company are seen growing at a CAGR of 5.5% over FY22-25E to 3.4 lakh tonne in FY25E (capacity pegged at 3.6 lakh tonne) amid normalisation of ASPs post decline in ocean freight costs/surcharge
Sales volume (MT)	199,213	211,261	201,760	227,132	288,795	296,370	317,099	339,296	
Volume growth (% YoY)		6%	-4%	13%	27%	3%	7%	7%	
Average realisation (₹/kg)	222	246	237	254	286	327	329	338	

Source: ICICI Direct Research

Financial story in charts

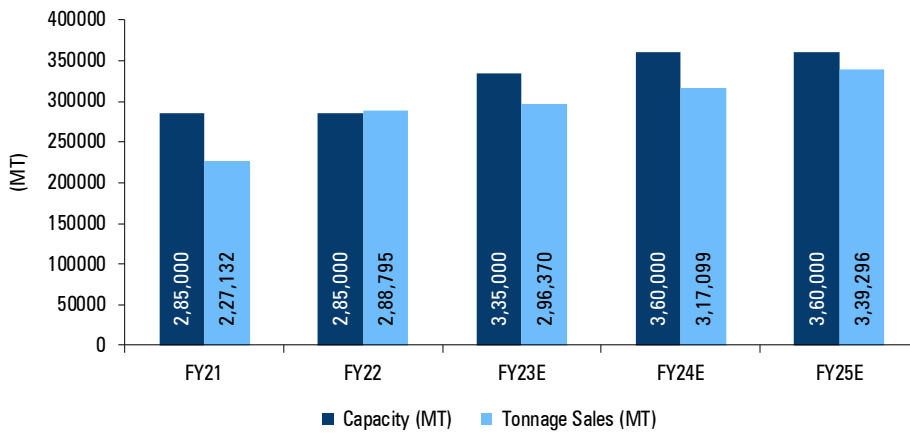
Exhibit 5: Topline trend



We expect sales to grow at a CAGR of 11.5% over FY22-25E to ₹ 11,456 crore in FY25E

Source: Company, ICICI Direct Research

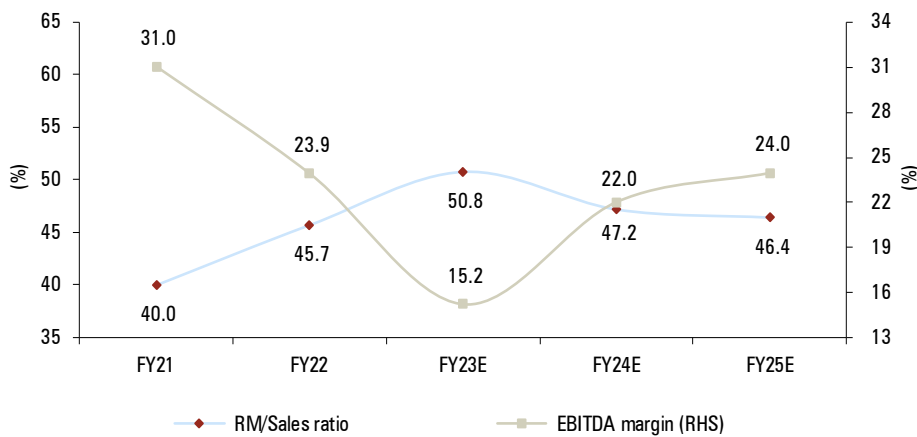
Exhibit 6: Capacity and volume trend



We expect tonnage volumes to grow at 5.5% CAGR over FY22-25E to 3.39 lakh MT in FY25E

Source: Company, ICICI Direct Research

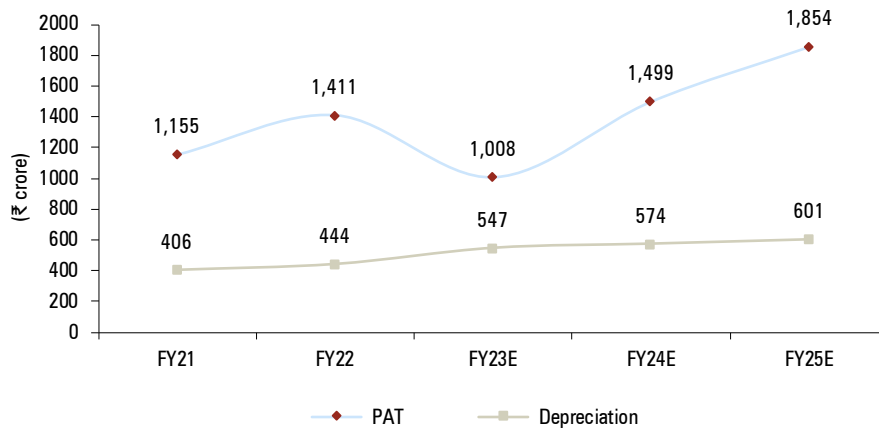
Exhibit 7: Trend in EBITDA margins



Margins are seen improving to 24% by FY25E vs. ~15% in FY23 amid backward integration benefits, cooling of commodity prices and better operating leverage

Source: Company, ICICI Direct Research

Exhibit 8: Trend in profitability



PAT seen growing at 9.5% CAGR in FY22-25E

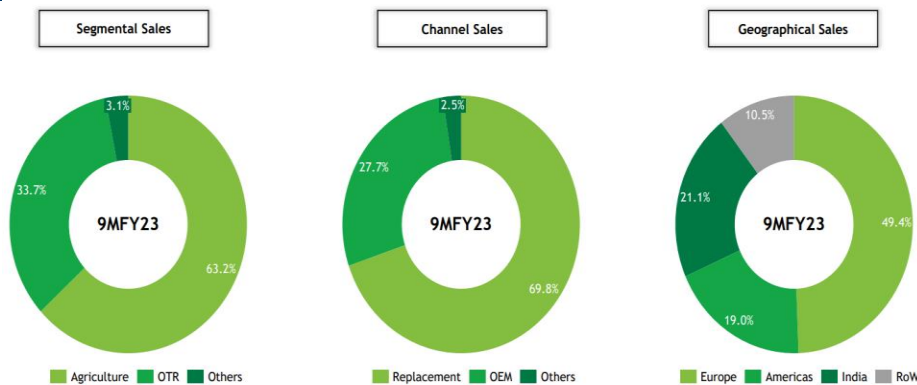
Source: Company, ICICI Direct Research

Exhibit 9: Valuation Summary

	Sales (₹ cr)	Growth (%)	EPS (₹)	Growth (%)	PE (x)	EV/EBITDA (x)	RoNW (%)	RoCE (%)
FY18	4,464	17.8	38.2	3.4	53.9	36.1	18.1	15.7
FY19	5,245	17.5	40.5	5.8	50.9	30.4	16.7	16.7
FY20	4,782	-8.8	48.9	20.8	42.1	32.2	18.8	14.4
FY21	5,758	20.4	59.8	22.3	34.5	22.6	19.2	19.3
FY22	8,267	43.6	73.0	22.1	28.2	21.0	20.4	15.9
FY23E	9,687	17.2	52.1	(28.6)	39.5	28.6	13.2	8.6
FY24E	10,433	7.7	77.5	48.7	26.6	17.9	17.3	15.8
FY25E	11,456	9.8	95.9	23.7	21.5	14.6	18.7	19.2

Source: Company, ICICI Direct Research

Exhibit 10: Volume Profile at BKT during 9MFY23



Source: Company, ICICI Direct Research

Exhibit 11: Important management commentary - snippet

Currently, experiencing channel inventory clearance in end markets. The distribution channel across global markets had excess inventory not only in OHT segment but other tire segments as well.

Along with this, the slow lowering of raw material prices and improvement in delivery timelines owing to better availability of containers has led to slower ordering cycle by the channel.

The end demand is still holding up, but the channel issues of ordering continue to impact the volumes.

As expected Q3 volumes were 66,480 MT.

The Company continues to face challenges of de-stocking in Q4 however the intensity of the situation is receding on month-on-month basis.

The situation has been relatively better in North America however recession fears continue to impact demand.

India continues to be stable supported by better economic environment.

The freight cost correction witnessed in the last few months has led to improvement in margins which is reflected in freight costs which now stand at -9% of sales in Q3.

Expect further benefits on account of freight to reflect in Q4 and fully in Q1FY24.

The Company has lowered the surcharge to end customers on account of freight and the same is reflected in our ASP which has moved down -6% on QoQ basis.

The aspect which impacted margins negatively and almost negated the impact of freight costs were raw material costs. While raw material prices have corrected, the Company not fully enjoy the benefits due to high-cost raw material inventory in the system.

Further, lower volumes clocked in Q3 led to lower absorption of fixed costs as against the expectation of higher volumes built in at the start of the financial year.

Lower Raw material and freight costs, better hedge rate, better end market situation gives hope for a margin recovery in FY24.

Source: Company, ICICI Direct Research

Financial Summary

Exhibit 12: Profit and loss statement				
	₹ crore			
(Year-end March)	FY22	FY23E	FY24E	FY25E
Total operating Income	8,266.7	9,686.6	10,433.0	11,455.7
Growth (%)	43.6	17.2	7.7	9.8
Raw Material Expenses	3,778.6	4,917.3	4,922.3	5,316.6
Employee Expenses	380.4	408.0	423.2	446.8
Other Expenses	2,132.2	2,886.4	2,788.8	2,947.6
Total Operating Expenditure	6,291.2	8,211.7	8,134.3	8,711.0
EBITDA	1975.5	1475.0	2298.7	2744.7
Growth (%)	10.6	-25.3	55.9	19.4
Depreciation	443.8	547.3	573.8	601.4
Interest	7.9	24.9	22.4	20.2
Other Income	430.6	447.1	301.7	355.4
PBT	1954.5	1349.8	2004.2	2478.5
Total Tax	543.8	341.9	505.1	624.6
Reported PAT	1410.7	1007.9	1499.2	1853.9
Growth (%)	22.1	-28.6	48.7	23.7
EPS (₹)	73.0	52.1	77.5	95.9

Source: Company, ICICI Direct Research

Exhibit 13: Cash flow statement				
	₹ crore			
(Year-end March)	FY22	FY23E	FY24E	FY25E
Profit after Tax	1,410.7	1,007.9	1,499.2	1,853.9
Add: Depreciation	443.8	547.3	573.8	601.4
(Inc)/dec in Current Assets	-1,140.9	-246.3	-256.5	-351.5
Inc/(dec) in CL and Provisions	305.2	57.4	95.6	131.0
CF from operating activities	1018.8	1366.3	1912.1	2234.9
(Inc)/dec in Investments	-292.5	125.0	50.0	-50.0
(Inc)/dec in Fixed Assets	-1,506.1	-1,500.0	-400.0	-400.0
Others	-295.3	-176.2	-78.2	-122.9
CF from investing activities	-2093.8	-1551.2	-428.2	-572.9
Inc/(dec) in loan funds	1,549.2	500.0	-1,000.0	-1,000.0
Dividend paid & dividend tax	-541.3	-309.3	-464.0	-580.0
Others	47.9	0.0	0.0	0.0
CF from financing activities	1055.9	190.7	-1464.0	-1580.0
Net Cash flow	-19.2	5.8	19.9	82.0
Opening Cash	54.5	35.3	41.1	61.1
Closing Cash	35.3	41.1	61.1	143.1

Source: Company, ICICI Direct Research

Exhibit 14: Balance Sheet				
	₹ crore			
(Year-end March)	FY22	FY23E	FY24E	FY25E
Liabilities				
Equity Capital	38.7	38.7	38.7	38.7
Reserve and Surplus	6,885.9	7,584.5	8,619.7	9,893.7
Total Shareholders funds	6924.6	7623.2	8658.4	9932.3
Total Debt	2,442.6	2,942.6	1,942.6	942.6
Deferred Tax Liability	250.9	250.9	250.9	250.9
Minority Interest / Others	0.0	0.0	0.0	0.0
Total Liabilities	9673.3	10871.9	10907.1	11181.0
Assets				
Gross Block	6,355.7	8,764.1	9,414.1	9,814.1
Less: Acc Depreciation	2,449.3	2,996.6	3,570.4	4,171.8
Net Block	3906.4	5767.5	5843.7	5642.3
Capital WIP	1,258.4	350.0	100.0	100.0
Total Fixed Assets	5,164.8	6,117.5	5,943.7	5,742.3
Investments	1,977.0	1,927.0	1,902.0	2,002.0
Inventory	1,639.4	1,645.4	1,772.2	1,945.9
Debtors	1,097.7	1,326.9	1,429.2	1,569.3
Loans and Advances	68.5	80.3	86.5	95.0
Cash	35.3	41.1	61.1	143.1
Other current assets	277.5	276.7	298.0	327.3
Total Current Assets	3,118.4	3,370.5	3,647.0	4,080.5
Creditors	807.5	849.2	914.7	1,004.3
Provisions	4.5	4.7	5.1	5.6
Other current liabilities	371.8	387.3	417.1	458.0
Total Current Liabilities	1,183.8	1,241.2	1,336.8	1,467.9
Net Current Assets	1934.6	2129.3	2310.1	2612.7
Others	596.5	697.6	750.8	823.7
Application of Funds	9673.3	10871.9	10907.1	11181.0

Source: Company, ICICI Direct Research

Exhibit 15: Key ratios				
(Year-end March)	FY22	FY23E	FY24E	FY25E
Per share data (₹)				
EPS	73.0	52.1	77.5	95.9
Cash EPS	95.9	80.4	107.2	127.0
BV	358.2	394.3	447.9	513.8
DPS	28.0	16.0	24.0	30.0
Cash Per Share	37.2	31.1	29.5	36.3
Operating Ratios (%)				
EBITDA Margin	23.9	15.2	22.0	24.0
PBT / Net sales	18.5	9.6	16.5	18.7
PAT Margin	17.1	10.4	14.4	16.2
Inventory days	72.4	62.0	62.0	62.0
Debtor days	48.5	50.0	50.0	50.0
Creditor days	35.7	32.0	32.0	32.0
Return Ratios (%)				
RoE	20.4	13.2	17.3	18.7
RoCE	15.9	8.6	15.8	19.2
RoIC	20.0	9.4	16.9	20.7
Valuation Ratios (x)				
P/E	28.2	39.5	26.6	21.5
EV / EBITDA	21.0	28.6	17.9	14.6
EV / Net Sales	5.0	4.4	3.9	3.5
Market Cap / Sales	4.8	4.1	3.8	3.5
Price to Book Value	5.8	5.2	4.6	4.0
Solvency Ratios				
Debt/EBITDA	1.2	2.0	0.8	0.3
Debt / Equity	0.4	0.4	0.2	0.1
Current Ratio	3.8	3.9	3.9	3.9
Quick Ratio	1.8	2.0	2.0	2.0

Source: Company, ICICI Direct Research

Exhibit 16: ICICI Direct coverage universe (Auto & Auto Ancillary)

Sector / Company	CMP	TP	Rating	M Cap	EPS (₹)			P/E (x)			EV/EBITDA (x)			RoCE (%)			RoE (%)		
	(₹)	(₹)		(₹ Cr)	FY22	FY23E	FY24E	FY22	FY23E	FY24E	FY22	FY23E	FY24E	FY22	FY23E	FY24E	FY22	FY23E	FY24E
Apollo Tyre (APOTYR)	330	390	Buy	20,956	10.1	15.9	25.2	32.8	20.7	13.1	9.9	7.6	5.9	6.3	10.0	13.8	5.4	8.1	11.8
Ashok Leyland (ASHLEY)	149	185	Buy	43,614	1.8	3.9	6.8	80.7	38.4	22.0	45.0	17.0	12.0	2.1	15.9	23.3	0.2	14.1	22.0
Bajaj Auto (BAAUTO)	3,889	4,100	Hold	1,12,536	173.4	197.5	240.9	22.4	19.7	16.1	17.4	14.5	11.7	18.4	24.2	29.0	17.6	22.3	26.1
Balkrishna Ind. (BALIND)	2,060	2,170	Hold	39,823	73.0	52.1	77.5	28.2	39.5	26.6	21.0	28.6	17.9	15.9	8.6	15.8	20.4	13.2	17.3
Bharat Forge (BHAFOR)	889	1,050	Buy	41,389	23.1	17.5	28.2	38.4	50.7	31.5	22.1	23.5	17.0	9.6	8.4	12.6	15.2	11.4	16.4
Eicher Motors (EICMOT)	3,236	4,310	Buy	88,440	61.3	101.4	124.6	52.8	31.9	26.0	36.8	22.2	17.9	13.3	20.5	21.6	13.3	19.2	20.4
Escorts Kubota (ESCORT)	2,077	2,165	Hold	27,404	58.0	45.1	60.7	35.8	46.1	34.2	23.7	30.3	24.1	10.4	6.9	8.4	9.7	8.0	9.0
Hero Moto (HERHON)	2,569	2,770	Hold	51,303	123.8	137.2	169.7	20.7	18.7	15.1	12.7	11.3	9.1	16.3	18.4	22.2	15.7	16.6	19.5
M&M (MAHMAH)	1,348	1,665	Buy	1,67,583	41.4	54.9	66.3	32.6	24.6	20.3	23.1	15.8	13.5	9.3	13.1	14.3	13.1	16.6	15.9
Maruti Suzuki (MARUTI)	8,835	11,200	Buy	2,66,888	124.7	261.9	369.0	70.9	33.7	23.9	39.5	20.6	14.7	5.1	12.9	16.9	7.0	13.3	16.7
Uno Minda (MININD)	533	630	Buy	30,474	6.2	11.5	15.6	85.7	46.4	34.1	35.1	24.2	19.2	10.2	15.2	18.0	10.3	16.3	18.4
Tata Motors (TATMOT)	446	530	Buy	1,70,773	-29.9	-3.1	24.3	-14.9	-145.6	18.4	7.3	6.4	4.3	4.8	7.9	15.1	-23.5	-2.5	16.3

Source: Company, ICICI Direct Research

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Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



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