

30 October 2015

MRF

Performance Highlights

Y/E Sept. (₹ cr)	4QFY2016*	4QSY2014	% chg (yoy)	3QFY2016	% chg (qoq)
Net sales	3,330	3,337	(0.2)	3,312	0.5
EBITDA	778	489	59.1	630	23.5
EBITDA margin (%)	23.4	14.7	872bp	19.0	435bp
Reported PAT	461	230	100.1	333	38.5

Source: Company, Angel Research; Note: *The company has extended the current financial year by six months, ie up to 31 March 2016.

For 4QFY2016, MRF beat our estimates on the EBITDA and bottom-line fronts. The top-line for the quarter remained flat on a yoy basis at ₹3,330cr (it declined marginally by 0.9% yoy). Raw material cost as a percentage of sales declined by 589bp yoy to 53.6%, thus aiding EBITDA margin expansion by 530bp yoy to 23.4%. Depreciation expense grew by 12.2% yoy to ₹125cr and other income grew by 209.3% yoy to ₹77cr. As a result, the net profit jumped by 45.4% yoy to ₹461cr.

Replacement market demand affected by Chinese imports, OEM recovery to continue: The recovery in demand from OEMs has been slow despite better numbers from the MHCV side. This is because 2W/3W and tractor performance has been sub-par due to deficient monsoons and dampened rural sentiments. Additionally, surge in import of cheaper Chinese tyres is eating into the share of domestic players, including MRF, in the TBR replacement market. However recovery is expected in MHCV replacement cycle on the back of strong OEM sales in the last one year. We expect MRF to benefit from its diversified product portfolio and strong presence in the replacement market across all segments.

Low rubber prices to aid margins: During 4QFY2016, the price of rubber in the domestic market declined by 5.9% yoy to ₹118/kg; rubber currently trades at ~₹114/kg in the domestic market. Considering the high global inventory levels, cheaper synthetic rubber and lower demand from China, we expect rubber prices to remain at lower levels. This will help the company in maintaining its EBITDA margin.

Outlook and valuation: We expect net sales to be at ₹14,488cr in FY2017E, while the EBITDA margin is expected to be at 21.1% in FY2017E. On the back of better margins, the net profit is expected to be at ₹1,611cr in FY2017E. At the current market price, MRF is trading at a PE of 10.5x its FY2017E earnings and at a P/BV of 2.0x for FY2017E. **We have an Accumulate rating on the stock with a target price of ₹45,575 based on a target P/E of 12.0x for FY2017E.**

Key Financials (Standalone)

Y/E March (₹ cr)	SY2013	SY2014	FY2016E*	FY2017E
Net Sales	12,131	13,198	20,316	14,488
% chg	2.2	8.8	53.9	(28.7)
Net Profit	802	898	2,328	1,611
% chg	40.2	11.9	159.2	(30.8)
EBITDA (%)	14.6	14.6	21.4	21.1
EPS (₹)	1,892	2,117	5,488	3,798
P/E (x)	21.0	18.7	7.2	10.5
P/BV (x)	4.6	3.7	2.5	2.0
RoE (%)	24.7	22.0	41.1	21.2
RoC (%)	28.3	28.8	62.6	36.5
EV/Sales (x)	1.4	1.3	0.8	1.0
EV/EBITDA (x)	9.7	8.8	3.6	4.9

Source: Company, Angel Research; Note: *The company has extended the current financial year by six months, ie up to 31 March 2016.

ACCUMULATE

CMP	₹39,692
Target Price	₹45,575

Investment Period	12 Months
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Stock Info

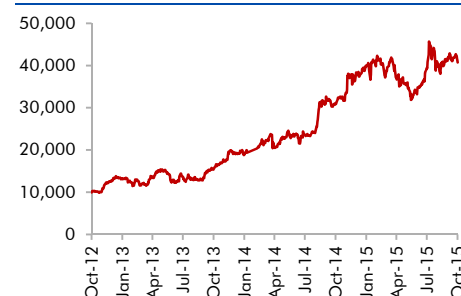
Sector	Tyre
Market Cap (Rs cr)	16,834
Net Debt	(807)
Beta	1.1
52 Week High / Low	46405/30750
Avg. Daily Volume	2,388
Face Value (Rs)	10
BSE Sensex	26,657
Nifty	8,066
Reuters Code	MRF.BO
Bloomberg Code	MRF IN

Shareholding Pattern (%)

Promoters	27.4
MF / Banks / Indian FIs	10.3
FII / NRIs / OCBs	8.7
Indian Public / Others	53.6

Abs. (%)	3m	1yr	3yr
Sensex	(2.6)	(1.0)	44.0
MRF	3.1	31.1	309.0

3-year daily price chart



Source: Company, Angel Research

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Exhibit 1: 4QFY2016 performance

Y/E Sept (₹ cr)	4QFY16	4QSY14	yoy chg (%)	3QFY16	qoq chg (%)	SY2015	SY2014	% chg
Net Sales	3,330	3,361	(0.9)	3,539	(5.9)	13,533	13,198	2.5
Net raw material	1,784	1,999	(10.8)	1,941	(8.1)	7,568	8,379	(9.7)
(% of Sales)	53.6	59.5	(589)bp	54.9		55.9	63.5	
Staff Costs	212	180	17.8	216	(1.7)	830	733	13.3
(% of Sales)	6.4	5.4	102bp	6.1		6.1	5.6	
Other Expenses	555	574	(3.4)	570	(2.7)	2,290	2,158	6.1
(% of Sales)	16.7	17.1	(42)bp	16.1		16.9	16.3	
Total Expenditure	2,551	2,754	(7.3)	2,728	(6.5)	10,688	11,270	(5.2)
Operating Profit	778	608	28.1	811	(4.1)	2,846	1,928	47.6
OPM	23.4	18.1	530bp	22.9	45bp	21.0	14.6	642bp
Interest	53	56		52		229	232	
Depreciation	125	111		117		467	423	
Other Income	77	25	209.3	32		155	66	
PBT	678	465	45.8	674	0.5	2,305	1,339	72.2
(% of Sales)	20.4	13.8		19.0		17.0	10.1	
Tax	217	148	46.6	227	(4.5)	742	441	68.2
(% of PBT)	32.0	31.8		33.7		32.2	32.9	
Extraordinary income	-	-		-		-	-	
Reported PAT	461	317	45.4	447	3.1	1,564	898	74.2
PATM	13.8	9.4		12.6		11.6	6.8	
Adjusted PAT	461	317	45.4	447	3.1	1,564	898	74.2
Equity capital (cr)	4	4		4		4	4	
EPS (₹)	1,087	747	45.4	1,054	3.1	3,688	2,118	74.2

Source: Company, Angel Research

Exhibit 2: Actual vs. Estimate (4QFY2016)

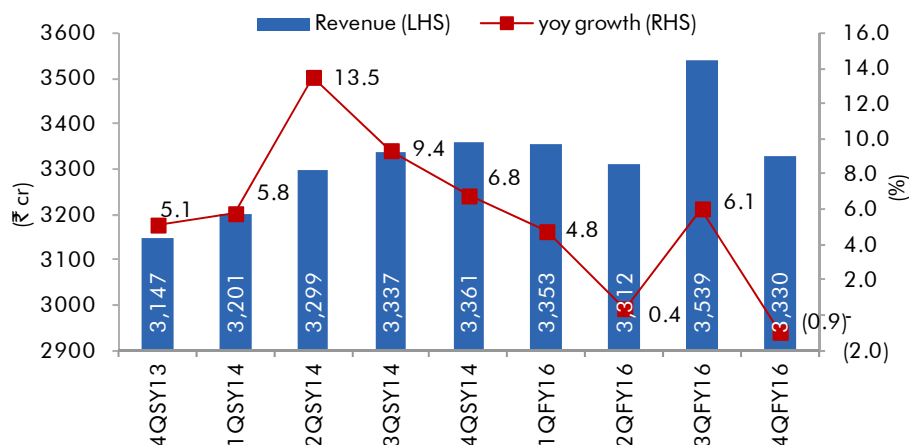
Particulars (₹ cr)	Actual	Estimate	Variation (%)
Total Income	3,330	3,425	(2.8)
EBIDTA	778	639	21.7
EBIDTA margin (%)	23.4	18.7	25.2
Adjusted PAT	461	326	41.1

Source: Company, Angel Research

Top-line below our expectation.

MRF's top-line for the quarter remained flat on a yoy basis at ₹3,330cr (it declined marginally by 0.9% yoy), which is 2.8% lower than our estimate of ₹3,425cr. The Indian tyre sector continues to face the heat from cheaper Chinese imports that have flooded the Indian market in the TBR segment. The flat top-line performance for the quarter could be partially attributable to this factor. Additionally passing on of raw material cost benefits to OEMs may have added to the decline in realizations.

Exhibit 3: Quarterly revenue trend

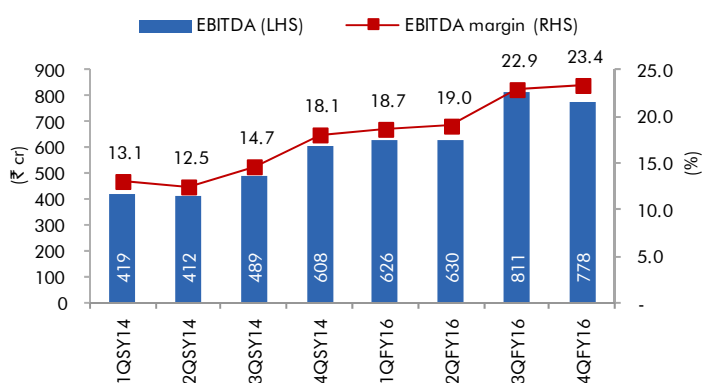


Source: Company, Angel Research

Margins impress resulting in higher bottom-line

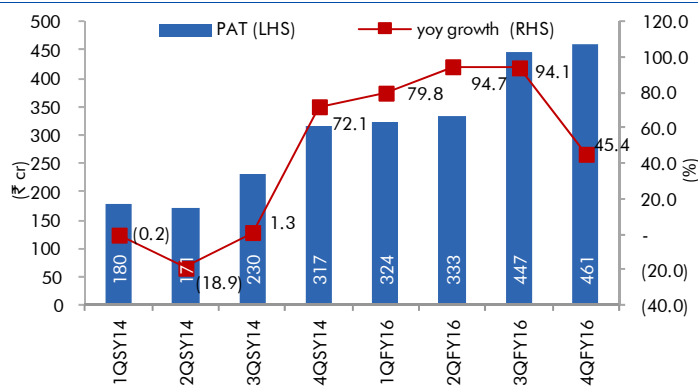
A decline in raw material prices in the latter two months of the past quarter aided in EBITDA margin expansion by 530bp yoy to 23.4% in 4QFY2016. We had estimated for an EBITDA margin of 18.7%; the deviation from our estimate was largely caused by a decline in raw material cost as a percentage of sales. Currently natural rubber trades at ~₹118/kg and ~₹98/kg in the domestic and international markets, respectively. Additionally, other raw materials which are derived from crude oil are trading at lower levels, owing to weaker crude prices. Employee and other expenses as a percentage of sales were mostly stable. The other income grew by 209.3% yoy to ₹77cr and as a result, the net profit jumped by 45.4% yoy to ₹461cr.

Exhibit 4: Lower RM costs aid EBITDA



Source: Company, Angel Research

Exhibit 5: ...thus leading to net profit growth



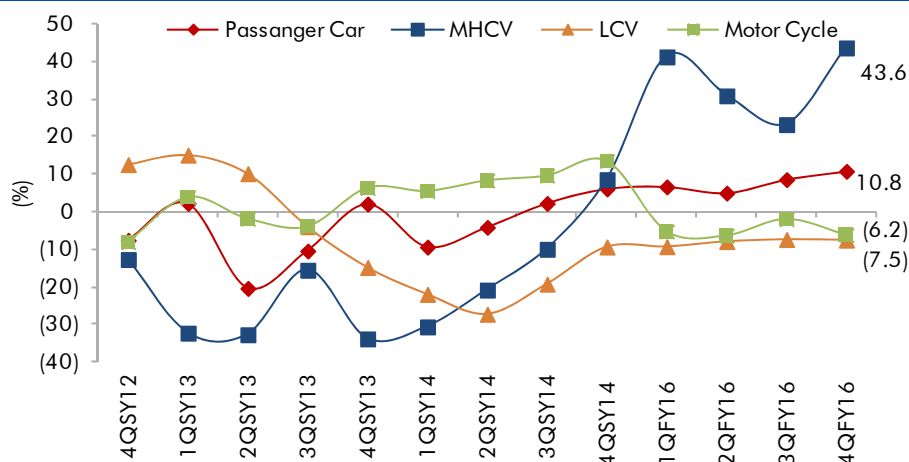
Source: Company, Angel Research

Investment rationale

Replacement market demand affected by Chinese imports; OEM recovery to continue

In the past 4 quarters the MHCV and passenger car segments have posted strong numbers. However tractors, motorcycles and LCVs have disappointed. We expect the recovery in these segments to be at a slower pace. Cheaper Chinese tyres have infiltrated the Indian markets and have hurt replacement market sales of local players, especially in the TBR segment. However, we expect a recovery in the MHCV replacement cycle on the back of strong OEM sales in the last one year. We believe that MRF has a diversified product mix along with a leading position in the replacement tyre market which should enable it to maintain its market share and traverse through the bumpy road in the near term. As far as replacement demand for other segments is concerned, our dealer checks in the recent past have indicated that Chinese tyres are a less of a threat in the passenger and motorcycle tyre segments. Also, dealers raved about the quality of MRF tyres and claimed they enjoy customer preference due to their longer life vis-a-vis competitors' tyres.

Exhibit 6: Domestic vehicle sales trend

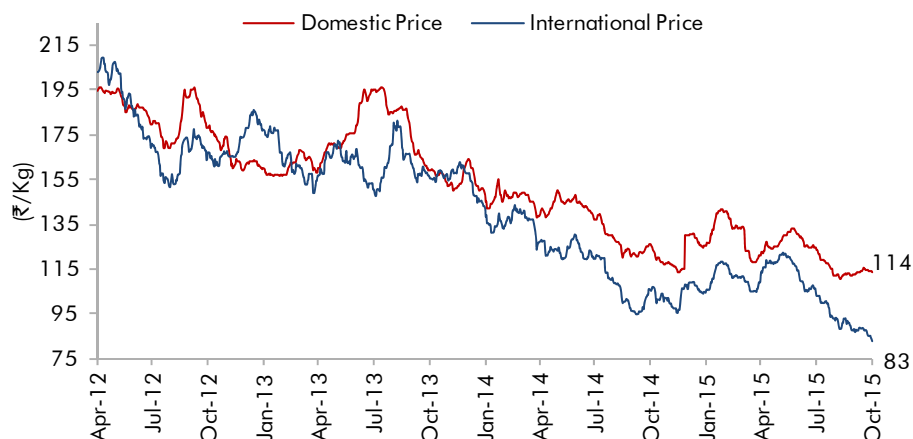


Source: Company, Angel Research

Lower rubber prices to help in sustaining EBITDA margin

MRF's margin expansion during the quarter has been mostly due to lower raw material prices. The prices of both, Styrene Butadiene Rubber (SBR) and Natural Rubber (NR), have corrected on account of weakness in crude and global NR prices. The prices of SBR feedstock, butadiene and natural rubber are likely to remain at current levels owing to higher global inventory of both crude and NR. Domestic NR prices have corrected by 14.6% yoy to ₹124/kg in the past four quarters while international NR prices have dropped by 14.8% yoy. Currently, domestic NR trades at ₹114kg.

Exhibit 7: Domestic and International rubber price trends



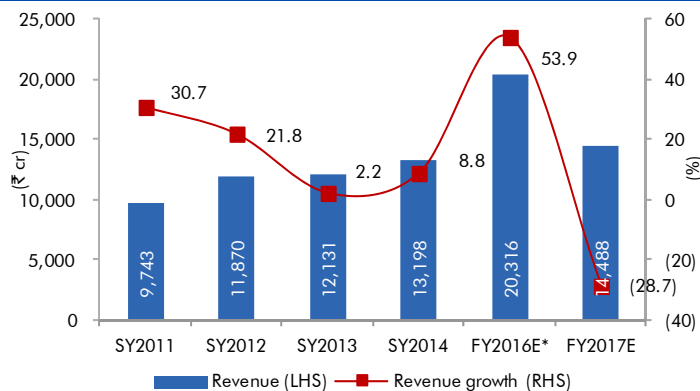
Source: Angel Research

Financials

Revenue to grow at slower rate

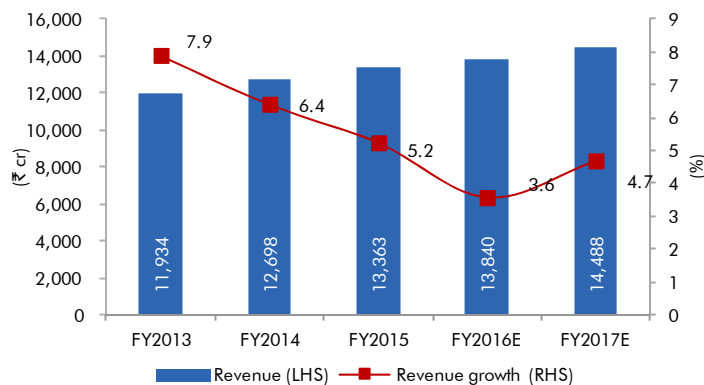
Owing to subdued demand for LCVs, motorcycles and tractors; and on account of lower realizations, the top-line is expected to be at ₹20,316cr for FY2016E (18 month sales) and ₹14,488cr in FY2017E.

Exhibit 8: Sales trend



Source: Company, Angel Research; Note:*FY2016E will have 18 months and hence, numbers post SY2014 are not comparable

Exhibit 9: Adjusted sales comparison

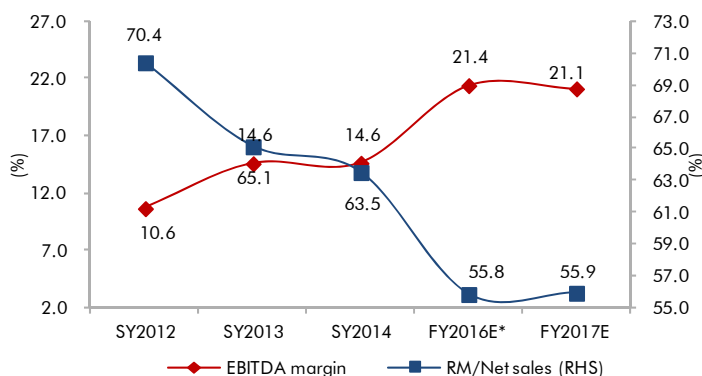


Source: Company, Angel Research

EBITDA and PAT margins to improve

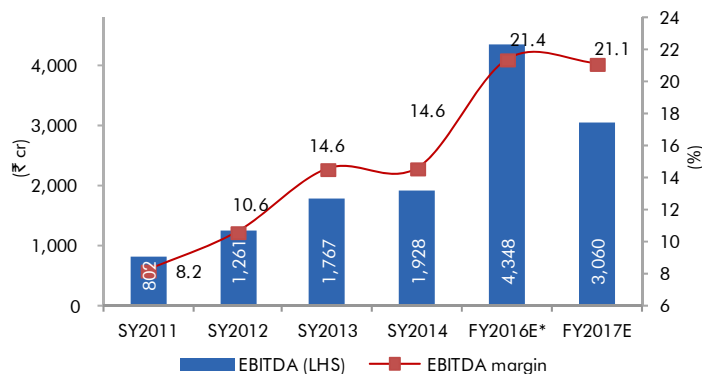
The effect of lower rubber prices is being reflected in the company's current quarter numbers and will carry over into FY2017. We expect EBITDA margins to improve to 21.4% in FY2016E (18 months) and be at 21.1% in FY2017E. Consequently, we estimate the net profit to be at ₹1,611cr in FY2017E.

Exhibit 10: Lower rubber prices to aid EBITDA margin



Source: Company, Angel Research

Exhibit 11: Steady growth in net profit



Source: Company, Angel Research Note: *FY2016E will have 18 months and hence, numbers post SY2014 are not comparable

Outlook and valuation

We expect net sales to be at ₹14,488cr in FY2017E, while the EBITDA margin is expected to be at 21.1% in FY2017E. As a result of better margins, the net profit is expected to be at ₹1,611cr in FY2017E. At the current market price, MRF is trading at a PE of 10.5x its FY2017E earnings and at a P/BV of 2.0x for FY2017E. **We have an Accumulate rating on the stock with a target price of ₹45,850 based on a target P/E of 12.0x for FY2017E.**

Exhibit 12: Relative valuation

	Year end	Sales (₹ cr)	OPM (%)	PAT (₹ cr)	EPS (₹)	ROE (%)	P/E (x)	P/BV (x)	EV/EBITDA (x)	EV/Sales (x)
Apollo Tyres	FY2017E	12,978	16.1	1,012	19.9	13.4	9.2	1.2	5.3	0.8
MRF	FY2017E	14,488	21.1	1,611	3,797.9	21.2	10.5	2.0	4.9	1.0

Source: Company

Risks

Volatile rubber prices: Natural rubber is the key raw material used in the manufacture of tyres. Domestic rubber prices have declined from the level of ₹133/kg in 4QSY2014 to average levels of ₹118/kg in the past quarter. Increase in rubber prices would have a negative impact on the company's EBITDA margin and consequently on its profit.

Hike in import duty on rubber: In the wake of falling domestic rubber prices, the Central Government has increased the import duty on natural rubber to a lower of 20% or ₹30/kg, from the currently lower of 20% or ₹20/kg. Any further upward revision in import duty will have an adverse impact on MRF's profitability.

Slowdown in automobile sector: Automobile demand in India has been declining since SY2011. Of the total tyre consumption in terms of tonnage for the industry, OEMs account for ~36%. If the demand from OEMs continues to be sluggish, it will impact the revenue growth of the company.

Cheaper Chinese Imports: The government has yet to extend the anti-dumping duty, it had levied on imported MHCV tyres, beyond February 2015. In case of further delay in the extension of the duty or in the eventuality of the government altogether not extending the aforementioned anti-dumping duty, MRF's volumes would be adversely impacted.

Company Background

MRF manufactures rubber products such as tyres, tubes, flaps, tread rubber and conveyor belts. The company is present across all categories of tyres. MRF is a market leader in the tyre industry with an ~24% market share as on FY2012. The company is also a leader in the passenger car tyre segment with a 24.8% market share and holds a third position in the MHCV segment with a 22.3% market share. MRF also exports tyres to over 65 countries in America, Europe, Middle East, Japan and the Pacific region.

Profit & Loss Statement (Standalone)

Y/E Sept (₹ cr)	SY2012	SY2013	SY2014	FY2016E*	FY2017E
Gross sales	13,062	13,453	14,649	22,551	16,082
Less: Excise duty	1,192	1,322	1,451	2,235	1,594
Net Sales	11,870	12,131	13,198	20,316	14,488
% chg	21.8	2.2	8.8	53.9	(28.7)
Net Raw Materials	8,353	7,899	8,379	11,336	8,096
Personnel	514	603	733	1,209	877
Other	1,743	1,862	2,158	3,423	2,456
Total Expenditure	10,609	10,365	11,270	15,968	11,428
EBITDA	1,261	1,767	1,928	4,348	3,060
% chg	57.3	40.1	9.1	125.5	(29.6)
(% of Net Sales)	10.6	14.6	14.6	21.4	21.1
Depreciation & Amort.	301	373	423	721	557
EBIT	960	1,394	1,505	3,627	2,503
% chg	73.3	45.2	8.0	141.0	(31.0)
(% of Net Sales)	8.1	11.5	11.4	17.9	17.3
Interest & other charges	159	196	232	336	189
Other Income	32	29	66	183	90
(% of sales)	0.3	0.2	0.5	0.9	0.6
PBT	833	1,227	1,339	3,474	2,404
% chg	73.0	47.3	9.1	159.5	(30.8)
Tax	261	425	441	1,146	793
(% of PBT)	31.3	34.6	32.9	33.0	33.0
PAT (reported)	572	802	898	2,328	1,611
Minority interest	-	-	-	-	-
Extraordinary (Exp)/Inc.	-	-	-	-	-
Tax on extraordinary exp	-	-	-	-	-
ADJ. PAT	572	802	898	2,328	1,611
% chg	32.6	40.2	11.9	159.2	(30.8)
(% of Net Sales)	4.8	6.6	6.8	11.5	11.1
Basic EPS (₹)	1,350	1,892	2,117	5,488	3,798
Fully Diluted EPS (₹)	1,350	1,892	2,117	5,488	3,798
% chg	32.6	40.2	11.9	159.2	(30.8)

Note: *FY2016E will have 18 months and hence, numbers post SY2014 are not comparable

Balance Sheet (Standalone)

Y/E Sept (₹ cr)	SY2012	SY2013	SY2014	FY2016E*	FY2017E
SOURCES OF FUNDS					
Equity Share Capital	4	4	4	4	4
Preference Capital	-	-	-	-	-
Reserves & Surplus	2,854	3,641	4,513	6,816	8,401
Equity share warrants	-	-	-	-	-
Shareholders' Funds	2,858	3,645	4,518	6,820	8,405
Total Loans	1,659	1,562	1,903	1,808	1,717
Deferred Tax Liability	187	222	235	259	259
Other Long Term Liabilities	957	1,080	1,145	1,317	1,195
Long Term Provisions	87	75	92	92	92
Total Liabilities	5,748	6,585	7,892	10,295	11,668
APPLICATION OF FUNDS					
Gross Block	5,063	5,475	6,328	7,593	9,534
Less: Acc. Depreciation	2,149	2,505	2,899	3,620	4,177
Net Block	2,914	2,970	3,429	3,973	5,357
Capital Work-in-Progress	415	359	627	1,250	600
Investments	425	906	1,088	1,856	1,856
Long Term Loans and adv.	57	138	224	244	244
Other noncurrent assets	30	35	42	65	65
Current Assets	3,371	3,850	4,387	4,947	5,738
Cash	61	331	708	1,078	1,605
Loans & Advances	211	167	137	185	188
Inventory	1,646	1,795	1,800	1,913	2,058
Debtors	1,454	1,556	1,708	1,742	1,866
Other current assets	-	-	35	29	21
Current liabilities	1,464	1,672	1,905	2,040	2,192
Net Current Assets	1,907	2,177	2,483	2,907	3,546
Mis. Exp. not written off	-	-	-	-	-
Total Assets	5,748	6,585	7,892	10,295	11,668

Note: *FY2016E will have 18 months and hence, numbers post SY2014 are not comparable

Cash Flow Statement (Standalone)

Y/E Sept (₹ cr)	SY2012	SY2013	SY2014	FY2016E*	FY2017E
Profit before tax	833	1,227	1,339	3,474	2,404
Depreciation	301	373	423	721	557
Change in Working Capital	(294)	(0)	71	(54)	(112)
Other income	443	248	280	(183)	(90)
Direct taxes paid	(261)	(425)	(428)	(1,123)	(793)
Cash Flow from Operations	1,023	1,422	1,685	2,835	1,965
(Inc.)/Dec. in Fixed Assets	(603)	(357)	(1,120)	(1,889)	(1,291)
(Inc.)/Dec. in Investments	(352)	(481)	(182)	(768)	-
(Decr)/Incr in Long term prov.	38	(12)	17	-	-
(Incr)/Decr In L.T loans & adv.	82	(85)	(93)	(42)	-
Other income	32	29	66	183	90
Others	(126)	12	(455)	-	-
Cash Flow from Investing	(929)	(895)	(1,768)	(2,516)	(1,201)
Issue of Equity	-	-	-	-	-
Inc./(Dec.) in loans	241	26	405	77	(212)
Dividend Paid (Incl. Tax)	(12)	(13)	(25)	(25)	(25)
Others	(317)	(315)	(328)	-	-
Cash Flow from Financing	(89)	(301)	52	51	(237)
Inc./(Dec.) in Cash	5	226	(31)	370	527
Fixed Deposit	-	44	408	-	-
Opening Cash balances	56	61	331	708	1,078
Closing Cash balances	61	331	708	1,078	1,605

Note: *FY2016E will have 18 months and hence, numbers post SY2014 are not comparable

Key Ratios

Y/E Sept (₹ cr)	SY2012	SY2013	SY2014	FY2016E*	FY2017E
Valuation Ratio (x)					
P/E (on FDEPS)	29.4	21.0	18.7	7.2	10.5
P/CEPS	19.3	14.3	12.7	5.5	7.8
P/BV	5.9	4.6	3.7	2.5	2.0
Dividend yield (%)	0.1	0.1	0.2	0.2	0.2
EV/Sales	1.5	1.4	1.3	0.8	1.0
EV/EBITDA	14.3	9.7	8.8	3.6	4.9
EV / Total Assets	3.1	2.6	2.1	1.5	1.3
Per Share Data (₹)					
EPS (Basic)	1,349.9	1,892.0	2,117.1	5,488.0	3,797.9
EPS (fully diluted)	1,349.9	1,892.0	2,117.1	5,488.0	3,797.9
Cash EPS	2,060.1	2,771.6	3,114.7	7,188.9	5,110.4
DPS	25.0	30.0	50.0	50.0	50.0
Book Value	6,740	8,597	10,652	16,080	19,818
Dupont Analysis					
EBIT margin	8.1	11.5	11.4	17.9	17.3
Tax retention ratio	0.7	0.7	0.7	0.7	0.7
Asset turnover (x)	2.4	2.4	2.4	3.3	1.9
ROIC (Post-tax)	13.6	18.3	18.4	39.8	22.1
Cost of Debt (Post Tax)	6.8	8.0	9.0	12.1	7.2
Leverage (x)	0.4	0.1	0.0	(0.2)	(0.2)
Operating ROE	16.4	19.2	18.7	35.2	19.0
Returns (%)					
ROCE (Pre-tax)	18.1	22.6	20.8	39.9	22.8
Angel ROIC (Pre-tax)	22.5	28.3	28.8	62.6	36.5
ROE	22.2	24.7	22.0	41.1	21.2
Turnover ratios (x)					
Asset Turnover (Gross Block)	2.7	2.3	2.2	2.9	1.7
Inventory / Sales (days)	49	52	50	52	50
Receivables (days)	42	45	45	47	47
Payables (days)	51	55	58	70	70
WC cycle (ex-cash) (days)	52	56	50	49	47
Solvency ratios (x)					
Net debt to equity	0.4	0.1	0.0	(0.2)	(0.2)
Net debt to EBITDA	0.9	0.2	0.1	(0.3)	(0.6)
Interest Coverage (EBIT / Int.)	6.0	7.1	6.5	10.8	13.2

Note: *FY2016E will have 18 months and hence, numbers post SY2014 are not comparable

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Disclosure of Interest Statement	MRF
1. Analyst ownership of the stock	No
2. Angel and its Group companies ownership of the stock	No
3. Angel and its Group companies' Directors ownership of the stock	No
4. Broking relationship with company covered	No

Note: We have not considered any Exposure below ₹ 1 lakh for Angel, its Group companies and Directors

Ratings (Based on expected returns over 12 months investment period):	Buy (> 15%)	Accumulate (5% to 15%)	Neutral (-5 to 5%)
		Reduce (-5% to -15%)	Sell (< -15)