

# SKF India Limited

Industry Auto Ancillary  
Bloomberg SKF IN  
BSE CODE 500472

## Softness in demand and higher mix of traded goods impacted margins

<b>RATING</b>	<b>HOLD</b>
<b>CMP</b>	<b>1926</b>
<b>Price Target</b>	<b>2027</b>
<b>Potential Upside</b>	<b>5%</b>

<b>Rating Change</b>	
<b>Estimate Change</b>	
<b>Target Change</b>	

### Stock Info

52wk Range H/L	2,000/1,610
Mkt Capital (Rs Cr)	9889
Free float (%)	48%
Avg. Vol 1M (,000)	40
No. of Shares (Cr.)	5.13
Promoters Pledged %	0%

### Research Analyst

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### 3QFY19 Result Update

- ❑ SKFINDIA posted decent set of numbers with revenue growth of 9.6% YoY to Rs.768 crores (vs. our estimates of Rs.760 crores).
- ❑ Higher raw material cost, adverse product mix and higher composition of traded goods led to 230bps QoQ contraction in the gross margins. However, reduction in EBITDA margin was limited because of lower employee cost and other expenses.
- ❑ PAT margins were expanded by 50bps QoQ to 11.5% on account of higher other income arising from foreign exchange gain of Rs.7 crores in 3QFY19.
- ❑ HUB-3 bearing plant will commence production from March 2019. However, it has a capacity to produce 350000 bearings per annum which is expected to go upto 500000 bearing per year after de-bottlenecking of plant.
- ❑ The bearing market has Rs. 800 crores of opportunity in the railway space, 60% in freight and 40% in passenger coaches and locomotives. Introduction of DFC and new metro project will increase the contribution from railway segment which is currently 7% of total sales.
- ❑ Electrification in India will speed up in 3W under automotive segment, then 2W and buses (intercity buses) and then PV segment.

### View and Valuation

Gross margins declined sharply by 230bps on a sequential basis because of adverse product mix and higher composition of traded goods. The recent slowdown in automobile industry resulted in lower automotive revenues in 3QFY19. The OEMs continue to maintain a neutral stance on the recovery of the industry in near term. Softness in demand will lead to higher mix of traded goods which may result in margins pressure in 4QFY19 as well. The introduction of Hub-3 bearings passenger cars (1.75x higher realization than traditional bearing), implementation of ABS in 2Ws coupled with Rs.800 crores opportunity in railways space gives us better growth opportunity in the long run going ahead. Although, the company has been developing ceramic bearings for EVs which are higher in value quotient but the content per vehicle will reduce going ahead. The overall growth in the industrial space will be driven by healthy investments in construction, heavy industries and defense segment. We largely maintain our FY20 EPS estimate but considering the demand headwinds and margin compression due to higher mix of traded goods we remain cautious in the near term growth prospects of the company. Hence we value SKFINDIA at 28x FY20e EPS (earlier 30x) to arrive at a target price of Rs.2027 and recommend HOLD.

### Key Risks to our rating and target

- ❑ Shift towards trading goods will lead to reduction in margins
- ❑ Continued slowdown in demand

KEY FINANCIAL/VALUATIONS	FY16	FY17	FY18	FY19E	FY20E
Net Sales	2998	2631	2750	3058	3377
EBITDA	364	336	435	481	554
EBIT	296	288	389	436	500
PAT	257	244	296	331	358
EPS (Rs)	49	46	58	67	72
EPS growth (%)	27%	-5%	25%	16%	8%
ROE (%)	16%	13%	16%	19%	18%
ROCE (%)	19%	16%	21%	26%	25%
BV	298	344	358	343	399
P/B (X)	4.2	3.7	4.9	5.6	4.8
P/E (x)	25.9	27.3	30.2	28.8	26.6

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## 3QFY19 Results

## Revenue In line with expectation

Financials	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	YoY %	QoQ%	FY17	FY18	YoY %
Net Sales	700	704	755	764	768	10%	0%	2,631	2,750	4.5%
Other Income	20	19	23	21	34	69%	58%	87	71	-18.3%
Total Income	721	722	777	786	801	11%	2%	2,719	2,822	3.8%
COGS	402	404	443	435	455	13%	4%	1,625	1,607	-1.1%
Staff Cost	60	60	61	70	64	6%	-8%	222	237	6.6%
Other Exp.	116	134	135	137	128	10%	-7%	448	472	5.4%
Expenditure	577	598	639	642	646	12%	1%	2,295	2,316	0.9%
EBITDA	123	106	116	123	122	-1%	-1%	336	435	29.4%
Depreciation	11	12	12	12	11	2%	-1%	48	46	-4.5%
EBIT	112	95	104	111	110	-1%	-1%	288	389	35.0%
Interest	2	2	2	2	2	29%	0%	-	5	
PBT	130	112	125	130	142	9%	9%	376	455	21.3%
Excpt. Item	-	-	-	-	-			-	-	
Tax	44	40	44	46	53	21%	16%	132	160	21.2%
PAT	86	72	81	84	88	3%	5%	244	296	21.3%

**Revenue growth of 9.6% YoY led by Industrial segment**

Net sales grew by 9.6% YoY to Rs.768 crores (vs. our estimates of Rs.760 crores) largely driven by growth in Industrial segment of 21% YoY. Revenue contribution by Industrial, Automotive and Exports stood at 54%, 40% and 6% respectively. Growth in Industrial segment came largely on account of heavy investments in the industrials side (construction, off highway vehicles, cement industry), Railways (7% of revenue), Energy (5% of Revenue) and metals (steel, copper and mining). Automotive segment posted growth of 7%YoY while exports de-grew by 34% YoY during the quarter.

**Higher proportion of traded goods and adverse product mix hampered margins**

Higher raw material cost, adverse product mix and higher composition of traded goods led to 230bps QoQ contraction in the gross margins. The ratio of traded goods and manufacturing goods stood at 70:30. However, reduction in EBITDA margin was limited to 20bps on sequential basis because of lower employee cost and other expenses.

**PAT margins expanded led by higher other income**

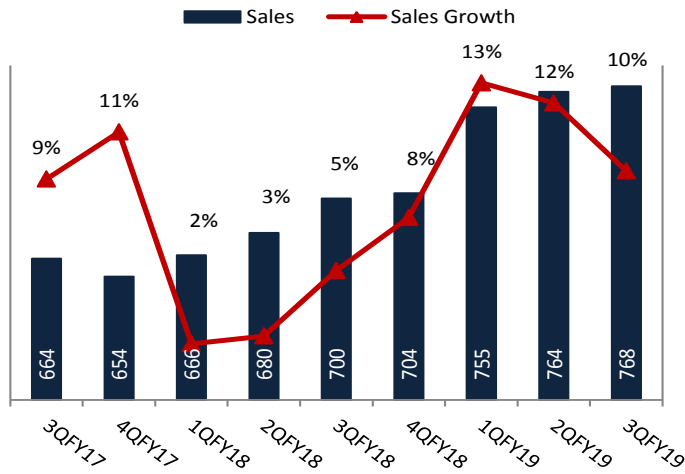
PAT for the quarter stood at Rs.88 crores during the quarter. The PAT margins improved by 50 bps QoQ to 11.5% largely on account of higher other income of Rs.34 crores which included foreign exchange gain of Rs.7 crores.

**Concall highlights**

- Revenue growth in automotive segment: 2W grew by 13%, after market grew by 6% and OE segment refers to 4W shown a slight decline in growth during the quarter.
- Industrial Segment revenue grew by 20% YoY which consists of 54% of total revenue.
- Within industrial segment Railways has come up with the approval in the freight side which is expected to generate more revenue. Change in norms in railways in terms of field trials, development trials which were there earlier are now removed since last two months which helps to come up with revenues.
- Gross margins came down during the quarter due to automotive share in total revenue was reduced. However, traded material was higher compare to manufacturing material.
- HUB-3 bearing will start up its production from March 2019. However, it has a capacity to produce 350000 bearings in a year which is expected to go up till 500000 bearing per year after debottlenecking of plant.
- Electrification in India will speed up in 3W under automotive segment, then 2W and buses (intercity buses) and then PV segment. Company will further have negotiations with OEM's in who will soon come up with new launches in the EV segment.
- After electrification, bearings per vehicle will go down. In value terms, it vary based on company offerings.
- Forex gain during the quarter was Rs. 7 crores largely due to rupee appreciation.
- Trading and Manufacturing ratio stands at 70:30 during the quarter.

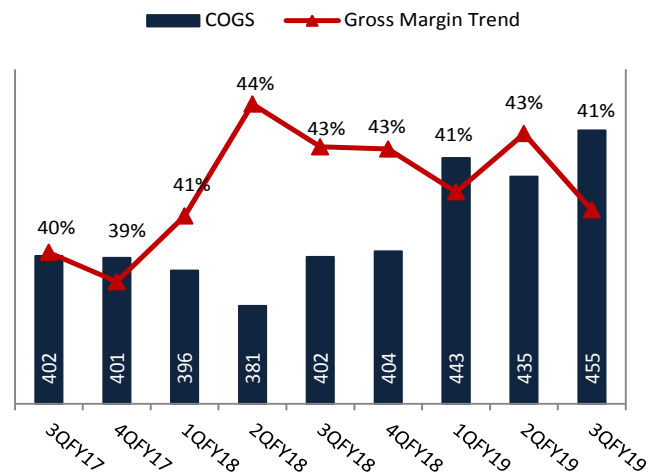
## Exhibit: Sales (Rs. Crores) and Sales Growth Trend

Sales grew by 10% YoY largely driven by growth in industrial segment.



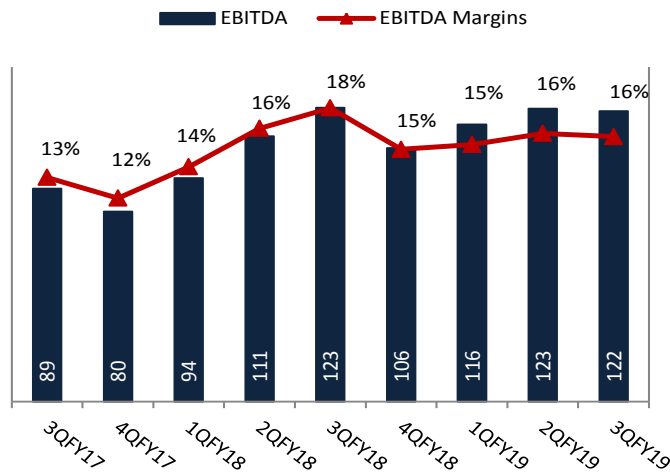
## Exhibit: COGS (Rs. Crores) & Gross Margin Trend

Gross margins declined by 230 bps QoQ due to higher composition of traded goods



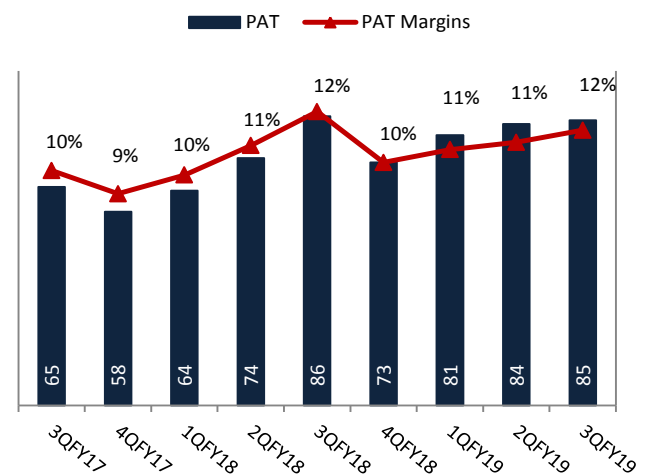
## Exhibit: EBITDA (Rs. Crore) and EBITDA Margin Trend

EBITDA margins reduced by 20bps QoQ to 15.8% in 3QFY19.



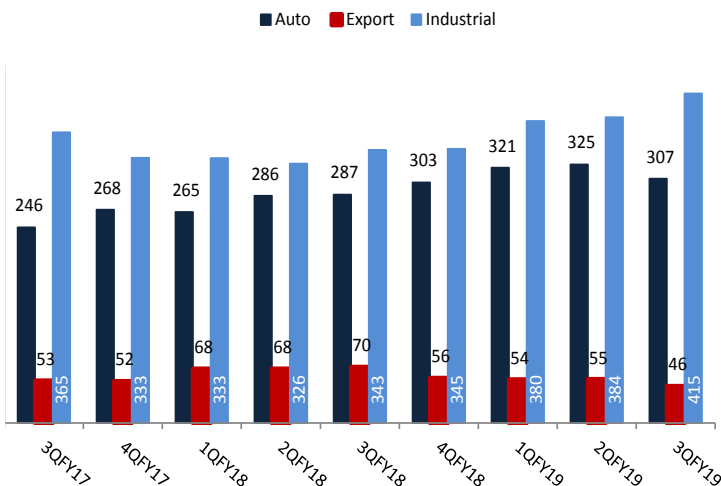
## Exhibit: PAT (Rs. Crore) and PAT Margin Trend

Higher other income enhanced PAT margins during the quarter.



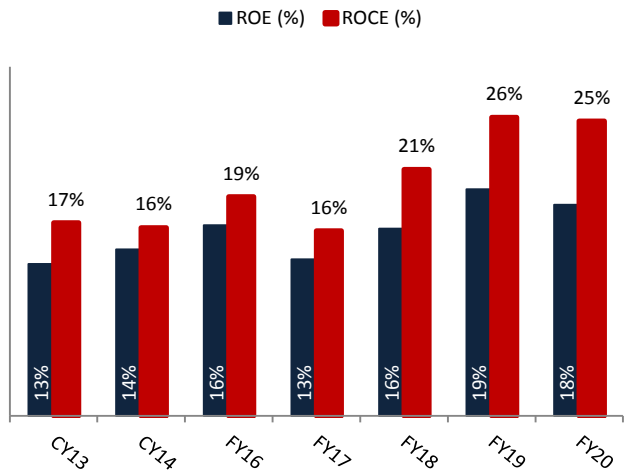
## Exhibit: Segmental Revenue

Industrial and Automotive segment grew by 21% and 7% whereas exports de-grew by 34% YoY.



## Exhibit: Return Ratios

Growth across automotive and industrial segment will lead to improvement in profitability ratios.



## Financial Details

## Balance Sheet

Y/E March	CY12	CY13	CY14	FY16	FY17	FY18	FY19E	FY20E
Share Capital	53	53	53	53	53	51	49	49
Reserves	1,103	1,223	1,363	1,517	1,758	1,786	1,648	1,923
Networth	1,155	1,276	1,416	1,569	1,811	1,837	1,698	1,972
Debt	-	-	-	-	34	85	85	85
Other Non Cur Liab	28	26	27	27	29	28	22	22
Total Capital Employed	1,155	1,276	1,416	1,569	1,845	1,922	1,783	2,057
Net Fixed Assets (incl CWIP)	407	401	385	310	334	330	378	474
Non Cur Investments	-	-	-	19	-	-	-	-
Other Non Cur Asst	650	655	617	517	484	551	599	695
Non Curr Assets	650	655	617	536	484	551	599	695
Inventory	249	255	293	335	417	403	448	495
Debtors	320	330	373	418	514	491	546	603
Cash & Bank	307	376	535	697	591	743	429	503
Other Curr Assets	74	80	93	98	297	257	310	357
Curr Assets	950	1,041	1,294	1,548	1,820	1,893	1,732	1,958
Creditors	268	251	337	293	304	390	419	463
Provisons (both)	94	90	72	149	21	22	18	19
Other Curr Liab	55	52	59	45	104	82	90	92
Curr Liabilities	417	394	468	487	429	493	526	574
Net Curr Assets	532	647	826	1,061	1,390	1,400	1,206	1,384
Total Assets	1,600	1,695	1,911	2,084	2,304	2,444	2,331	2,653

## Income Statement

Y/E March	CY12	CY13	CY14	FY16	FY17	FY18	FY19E	FY20E
Revenue from Operation	2,228	2,275	2,416	2,998	2,631	2,750	3,058	3,377
Change (%)	-9%	2%	6%	24%	-12%	5%	11%	10%
Other Income	68	63	77	101	87	71	89	59
EBITDA	258	261	283	364	336	435	481	554
Change (%)	-13%	1%	8%	29%	-8%	29%	11%	15%
Margin (%)	11.6%	11.5%	11.7%	12.1%	12.8%	15.8%	15.7%	16.4%
Depr & Amor.	44	49	54	68	48	46	45	54
EBIT	215	212	229	296	288	389	436	500
Int. & other fin. Cost	-	-	-	-	-	5	9	9
EBT	283	275	306	396	376	455	516	551
Exp Item	-	22	-	-	-	-	-	-
Tax	93	86	103	139	132	160	185	193
Minority Int & P/L share of Ass.	-	-	-	-	-	-	-	-
Reported PAT	190	167	203	257	244	296	331	358
Adjusted PAT	190	167	203	257	244	296	331	358
Change (%)	-9%	-12%	22%	27%	-5%	21%	12%	8%
Margin(%)	8.5%	7.3%	8.4%	8.6%	9.3%	10.8%	10.8%	10.6%

## Financial Details

## Key Ratios

Y/E March	CY12	CY13	CY14	FY16	FY17	FY18	FY19E	FY20E
ROE	16%	13%	14%	16%	13%	16%	19%	18%
ROCE	19%	17%	16%	19%	16%	21%	26%	25%
Asset Turnover	1.39	1.34	1.26	1.44	1.14	1.13	1.31	1.27
Debtor Days	7	7	6	7	5	6	6	6
Inv Days	41	41	44	41	58	53	53	53
Payable Days	8	9	7	10	9	7	7	7
Int Coverage	-	-	-	78	51	59	-	-
P/E	19	17	21	26	27	30	29	27
Price / Book Value	3.2	2.3	3.0	4.2	3.7	4.9	5.6	4.8
EV/EBITDA	13	10	13	16	18	19	19	16
FCF per Share	54	33	48	23	30	81	80	102

## Cash Flow Statement

Y/E March	CY12	CY13	CY14	FY16	FY17	FY18	FY19E	FY20E
PBT	283	275	306	396	376	455	516	551
(inc)/Dec in Working Capital	11	(46)	32	(152)	(105)	94	(82)	(65)
Non Cash Op Exp	44	49	54	68	48	46	45	54
Int Paid (+)	0	-	-	-	-	5	9	9
Tax Paid	(89)	(87)	(112)	(142)	(141)	(173)	(185)	(193)
others	(50)	(69)	(62)	(80)	(62)	(60)	-	-
CF from Op. Activities	199	122	218	91	115	367	303	356
(inc)/Dec in FA & CWIP	(88)	(51)	(37)	(32)	(42)	(50)	(93)	(150)
Free Cashflow	111	71	180	59	73	317	210	206
(Pur)/Sale of Inv	-	-	-	-	(149)	(5)	(44)	(39)
others	(13)	(114)	35	(142)	338	(210)	-	-
CF from Inv. Activities	(101)	(165)	(3)	(174)	147	(265)	(137)	(189)
inc/(dec) in NW	-	-	-	-	-	(209)	-	-
inc/(dec) in Debt	-	-	-	-	(31)	51	-	-
Int. Paid	-	-	-	-	-	(5)	(9)	(9)
Div Paid (inc tax)	(46)	(46)	(93)	(16)	(95)	(62)	(71)	(83)
others	-	-	-	-	-	-	-	-
CF from Fin. Activities	(46)	(46)	(93)	(16)	(126)	(225)	(80)	(92)
Inc(Dec) in Cash	52	(89)	123	(99)	136	(123)	85	75
Add: Opening Balance	108	160	71	193	95	230	743	429
Closing Balance	160	71	193	95	230	108	828	504

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