

Industry **Auto Ancillary**
 Bloomberg **SKF IN**
 BSE CODE **500472**

HUB-3 bearing plant to help maintain margins ahead.

RATING	HOLD
CMP	2170
Price Target	2335
Potential Upside	8%

Rating Change	↓
Estimate Change	↓
Target Change	↓

STOCK INFO	
52wk Range H/L	2290/1743
Mkt Capital (Rs Cr)	10729
Free float (%)	48%
Avg. Vol 1M (,000)	18
No. of Shares (Crs)	4.94
Promoters Pledged %	0%

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2QFY20 Result update

- SKFINDIA reported a revenue of Rs. 747 Cr. (vs our estimate of Rs. 768 Cr.) de-grew by 2.2% YoY on account of decline in automotive segment by 20% YoY.
- Revenue contribution by automotive, industrials and exports in 2QFY20 stood at 35%, 51% and 14% respectively.
- Trading and manufacturing mix during the quarter stood at 58:42 (which was 54:46 in 1QFY20).
- Gross margin contracted by 360bps QoQ to 36% in 2QFY20 due to i) change in mix of traded and manufacturing goods ii) production level was lower by 20%YoY which increased the cost of production iii) Margins of traded products went down iv) Decline in the replacement market of automotive segment business.
- EBITDA margins were at 12.7% decline by 270 bps QoQ on account of lower gross margin. However employee cost and other expenses reduced during the quarter.
- PAT during the quarter stood at Rs. 85 Cr. with the PAT margin of 11.3% (up by 130bps QoQ) led by higher other income and reduced tax expense.
- Hub-3 wheel bearing plant will commission in 3QFY20 with the capacity of 350000 bearing. Orders are lined up with the management for 4QFY20 up to a capacity of 175000 bearings and by 1HFY21 it's expected to reach at full capacity utilization.

View and Valuation

The domestic automotive industry continues to face challenging demand environment. However, commissioning of HUB-3 bearing plant in 3QFY20 is likely to help improve the margins along with the growth in the automotive segment going ahead. In addition to that increasing localization on industrial segment will further add to the margins. Going ahead we expect the industrial segment coupled with growth opportunities in freight bearings on railways will drive the growth ahead. Based on adverse product mix and higher depreciation cost we reduce our EPS estimates by 10%/6% for FY20/FY21. We value the stock at 26x FY21e EPS to arrive at a target price of Rs.2335 and recommend HOLD.

Key Risks to our rating and target

- Traded and manufacturing mix.
- Level of production going ahead.

Fig in Rs Cr

KEY FINANCIAL/VALUATIONS	FY17	FY18	FY19	FY20E	FY21E
Net Sales	2631	2750	3035	3123	3405
EBITDA	336	435	486	453	543
EBIT	288	389	440	390	470
PAT	244	296	336	365	444
EPS (Rs)	46	58	68	74	90
EPS growth (%)	-5	25	18	9	22
ROE (%)	13	16	20	18	19
ROCE (%)	16	21	26	20	20
BV	344	358	343	400	473
P/B (X)	3.7	4.9	5.4	5.4	4.6
P/E (x)	27.3	30.2	27.3	29.5	24.2

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2QFY20 Results

Revenue below expectation

Fig in Rs Cr

FINANCIALS	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	YoY %	QoQ%	FY18	FY19	YoY %
Net Sales	764	768	748	777	747	-2%	-4%	2,750	3,035	10.3%
Other Income	21	34	29	17	23	8%	35%	71	92	29.3%
Total Income	786	801	778	794	770	-2%	-3%	2,822	3,127	10.8%
COGS	435	455	444	469	478	10%	2%	1,607	1,776	10.6%
Staff Cost	70	64	63	64	60	-15%	-7%	237	258	9.0%
Other Exp.	137	128	130	124	115	-16%	-7%	472	514	8.9%
Expenditure	642	646	637	657	652	2%	-1%	2,316	2,549	10.1%
EBITDA	123	122	111	120	95	-22%	-21%	435	486	11.8%
Depreciation	12	11	12	14	14	21%	2%	46	46	1.2%
EBIT	111	110	100	106	81	-27%	-24%	389	440	13.0%
Interest	2	2	2	3	2	18%	-7%	5	8	
PBT	130	142	127	121	102	-22%	-16%	455	524	15.1%
Excpt. Item	-	-	-	-	-			-	-	
Tax	46	53	45	43	17	-63%	-60%	160	188	18.1%
PAT	84	88	82	78	85	1%	9%	296	336	13.5%

Revenue de-grew by 2.2% YoY led by degrowth in automotive segment

Net sales de-grew by 2.2% YoY to Rs. 747 Cr. largely on account of decline in revenue from automotive segment by 20% YoY. Moreover industrial segment also de-grew by 1% YoY in 2QFY20. However, exports contributed 14% of share in revenue increased by 5% on QoQ basis. And automotive and industrials are at 35% and 51% respectively. Total revenue contribution of 2W, PV, truck, tractor others and replacement market within Automotive segment is 12%, 4%, 2%, 2%, 4% and 11% respectively.

Higher cost of material hampered margins

Gross margins declined by 360 bps QoQ to 36% on account of unfavorable change in mix, lower production level, lower demand of higher margin product (replacement market in automotive segment). Trading and manufacturing mix stood at 58:42. Management is focusing to change the mix by bring more localization product and the plant for the same is expected to come in by FY21.

Lower tax expense and higher other income provided cushion to PAT margins

PAT during the quarter stood at Rs. 85 Cr. with the PAT margin of 11.3% led by higher other income and reduced tax expense. Forex gain of Rs. 6 cr. was due to rupee strengthening against Euro increased the other income in 2QFY20.

Concall highlights

- Revenue contribution by automotive, industrials and exports in 2QFY20 stood at 35%, 51% and 14% respectively.
- Trading and manufacturing mix during the quarter stood at 58:42 (which was 54:46 in 1QFY20).
- Exports are largely from the automotive segment is temporarily increased the share in revenue due to control over the fixed cost with the lower level of production. Once the automotive will start ramping up, Exports will be in the range of 9-10% of revenue contribution.
- Exports business contributes higher margins than automotive OE business.
- Employee cost and other expenses reduced on account of lower production level the variable cost of production reduced during the quarter.
- Railways freight segment Class-E bearings no orders are lined up currently with the company (just the trial orders are there). As they are imported from Europe and localization is still pending for approval and will take around 3-6 month time for localization approval.
- Within automotive OEM and replacement market reduced by 25% and 8% YoY respectively.
- CAPEX planned by the management is around Rs. 80-130 Cr. for FY20 and the management is looking for more localization within industrial and is expected to commission in 1QFY21. Moreover in FY21 management is expecting more capacity additions for localization to change the mix more favorable towards industrials.

Exhibit: Sales (Rs. crore) and Sales Growth Trend

Sales de-grew by 2.2% YoY largely driven by de-growth in automotive segment.

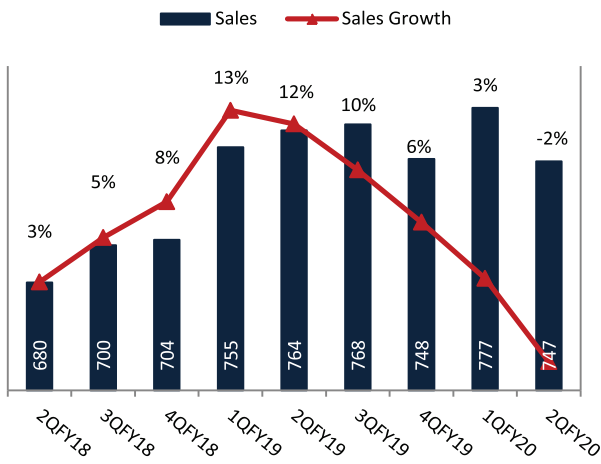


Exhibit: COGS (Rs. crore) and Gross Margin Trend

Gross margins decline on account of higher raw material to sales.

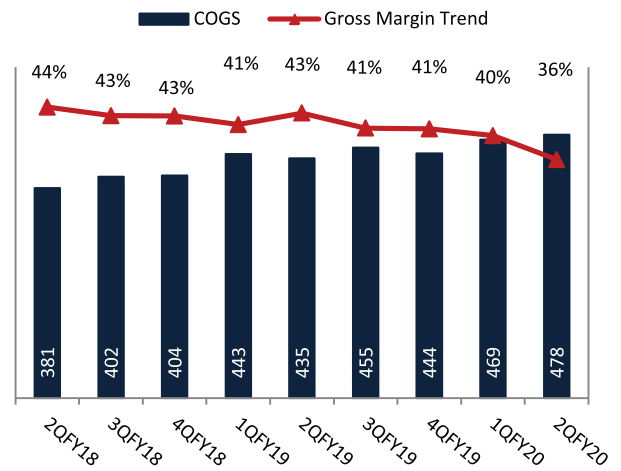


Exhibit: EBITDA (Rs. Crore) and EBITDA Margin Trend

EBITDA margins reduced led by lower gross margins in 2QFY20.

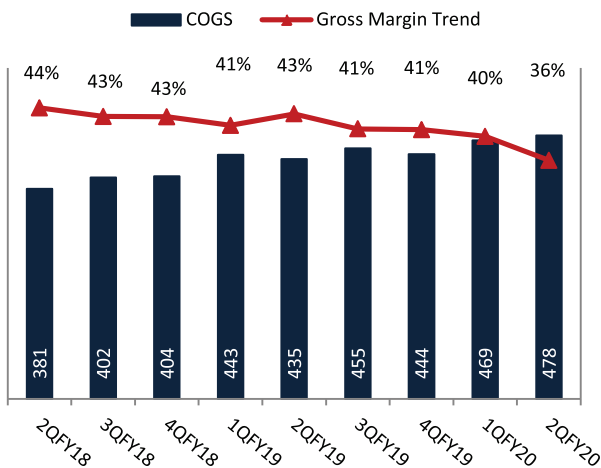


Exhibit: PAT (Rs. Crore) and PAT Margin Trend

Higher other income and reduced tax expense expanded PAT margins during the quarter.

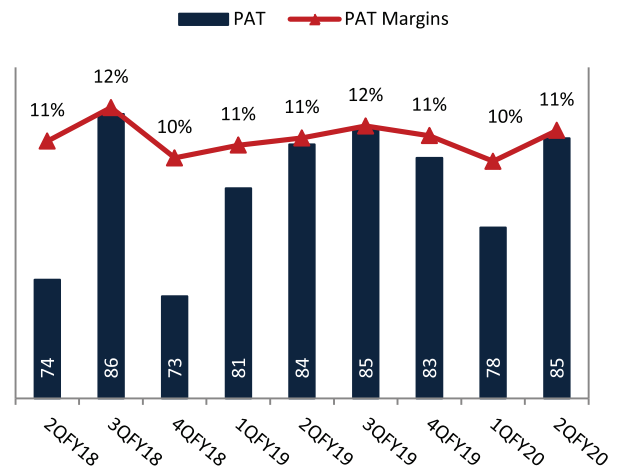


Exhibit: Segmental Revenue (Rs. crore)

Industrial and Automotive segment de-grew by 1% and 20%YoY whereas exports grew by 90% YoY.

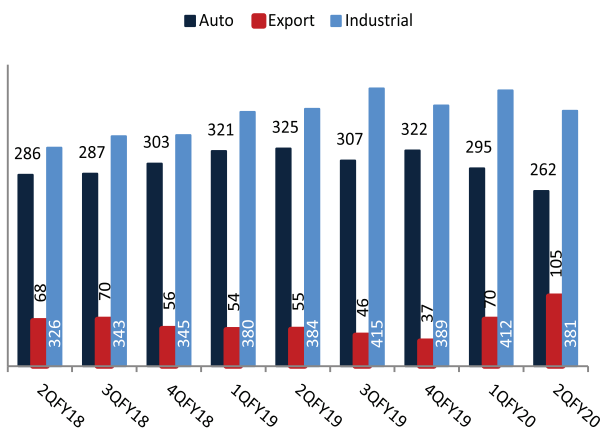
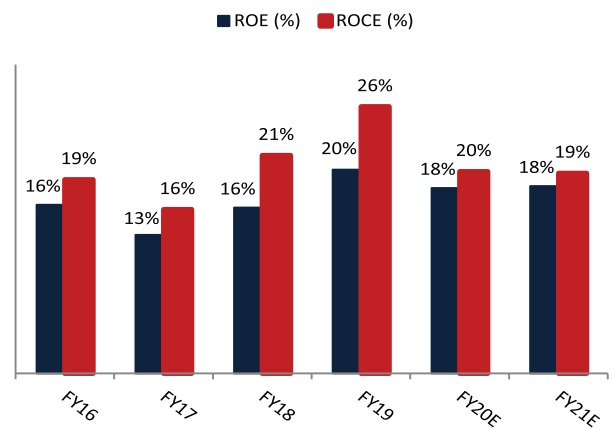


Exhibit: Return Ratios

Growth across automotive and industrial segment leads to profitability.



Financial Details

Balance Sheet

Fig in Rs Cr

Y/E March	CY13	CY14	FY16	FY17	FY18	FY19	FY20E	FY21E
Share Capital	53	53	53	53	51	49	49	49
Reserves	1,223	1,363	1,517	1,758	1,786	1,648	1,929	2,290
Networth	1,276	1,416	1,569	1,811	1,837	1,697	1,979	2,340
Debt	-	-	-	34	85	90	90	80
Other Non Cur Liab	26	27	27	29	28	32	32	32
Total Capital Employed	1,276	1,416	1,569	1,845	1,922	1,787	2,069	2,420
Net Fixed Assets (incl CWIP)	401	385	310	334	330	346	372	448
Non Cur Investments	-	-	19	-	-	-	-	-
Other Non Cur Asst	655	617	517	484	551	585	611	687
Non Curr Assets	655	617	536	484	551	585	611	687
Inventory	255	293	335	417	403	461	474	517
Debtors	330	373	418	514	491	521	536	585
Cash & Bank	376	535	697	591	743	603	630	645
Other Curr Assets	80	93	98	297	257	125	338	542
Curr Assets	1,041	1,294	1,548	1,820	1,893	1,711	1,978	2,289
Creditors	251	337	293	304	390	349	359	392
Provisions (both)	90	72	149	21	22	26	27	29
Other Curr Liab	52	59	45	104	82	102	102	104
Curr Liabilities	394	468	487	429	493	477	488	525
Net Curr Assets	647	826	1,061	1,390	1,400	1,234	1,490	1,765
Total Assets	1,695	1,911	2,084	2,304	2,444	2,296	2,589	2,977

Income Statement

Fig in Rs Cr

Y/E March	CY13	CY14	FY16	FY17	FY18	FY19	FY20E	FY21E
Revenue from Operation	2,275	2,416	2,998	2,631	2,750	3,035	3,123	3,405
Change (%)	2%	6%	24%	-12%	5%	10%	3%	9%
Other Income	63	77	101	87	71	92	106	132
EBITDA	261	283	364	336	435	486	453	543
Change (%)	1%	8%	29%	-8%	29%	12%	-7%	20%
Margin (%)	11.5%	11.7%	12.1%	12.8%	15.8%	16.0%	14.5%	16.0%
Depr & Amor.	49	54	68	48	46	46	62	73
EBIT	212	229	296	288	389	440	390	470
Int. & other fin. Cost	-	-	-	-	5	8	8	8
EBT	275	306	396	376	455	524	488	594
Exp Item	22	-	-	-	-	-	-	-
Tax	86	103	139	132	160	188	124	150
Minority Int & P/L share of Ass.	-	-	-	-	-	-	-	-
Reported PAT	167	203	257	244	296	336	365	444
Adjusted PAT	167	203	257	244	296	336	365	444
Change (%)	-12%	22%	27%	-5%	21%	14%	9%	22%
Margin(%)	7.3%	8.4%	8.6%	9.3%	10.8%	11.1%	11.7%	13.0%

Financial Details

Key Ratios

Y/E March	CY13	CY14	FY16	FY17	FY18	FY19	FY20E	FY21E
ROE	13%	14%	16%	13%	16%	20%	18%	19%
ROCE	17%	16%	19%	16%	21%	26%	20%	20%
Asset Turnover	1.3	1.3	1.4	1.1	1.1	1.3	1.2	1.1
Debtor Days	6.9	6.5	7.2	5.1	5.6	5.8	5.8	5.8
Inv Days	41	44	41	58	53	55	55	55
Payable Days	9.1	7.2	10.2	8.7	7.1	8.7	8.7	8.7
Int Coverage	-	-	78	57	48	-	-	-
P/E	17.4	21.1	25.9	27.3	30.2	27.3	29.5	24.2
Price / Book Value	2.3	3.0	4.2	3.7	4.9	5.4	5.4	4.6
EV/EBITDA	9.7	13.2	16.4	18.1	18.9	17.6	22.3	18.6
FCF per Share	33	48	23	30	81	46	102	125

Cash Flow Statement

Fig in Rs Cr

Y/E March	CY13	CY14	FY16	FY17	FY18	FY19	FY20E	FY21E
PBT	275	306	396	376	455	524	488	594
(inc)/Dec in Working Capital	(46)	32	(152)	(105)	94	(107)	(19)	(60)
Non Cash Op Exp	49	54	68	48	46	46	62	73
Int Paid (+)	-	-	-	-	5	8	8	8
Tax Paid	(87)	(112)	(142)	(141)	(173)	(212)	(124)	(150)
others	(69)	(62)	(80)	(62)	(60)	(78)	-	-
CF from Op. Activities	122	218	91	115	367	181	416	466
(inc)/Dec in FA & CWIP	(51)	(37)	(32)	(42)	(50)	(46)	(88)	(150)
Free Cashflow	71	180	59	73	317	135	329	316
(Pur)/Sale of Inv	-	-	-	(149)	(5)	109	(211)	(200)
others	(114)	35	(142)	338	(210)	243	-	-
CF from Inv. Activities	(165)	(3)	(174)	147	(265)	306	(299)	(350)
inc/(dec) in NW	-	-	-	-	(209)	(400)	-	-
inc/(dec) in Debt	-	-	-	(31)	51	5	-	(10)
Int. Paid	-	-	-	-	(5)	(8)	(8)	(8)
Div Paid (inc tax)	(46)	(93)	(16)	(95)	(62)	(74)	(83)	(83)
others	-	-	-	-	-	-	-	-
CF from Fin. Activities	(46)	(93)	(16)	(126)	(225)	(477)	(91)	(101)
Inc(Dec) in Cash	(89)	123	(99)	136	(123)	11	27	15
Add: Opening Balance	160	71	193	95	230	108	603	630
Closing Balance	71	193	95	230	108	118	630	645

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