11 December 2024

Ceat

Rating: **Buy**
Target Price: Rs.3,800
Share Price: Rs.3,149

Camso's acquisition positive over medium to long term; maintaining a Buy

Ceat's takeover of Camso would expand its presence in the higher profitability OHT segment. Further, it would also strengthen its presence in construction equipment (CE) globally. It would also add OEMs and distributors (key for success). Initially, the company would expand in compact CE, but later opportunities in other industrial segments like agriculture, harvester, mining and powersport would also open by leveraging the Camso brand. In the near term, due to a muted OEM segment and transition, acquisition would not be EPS accretive; however, on a steady state, acquisition would be EPS accretive. We estimate PAT to see losses of Rs150m in FY26 and then on better margins, a slight profit of Rs236m in FY27. We like Ceat for its market-share gains in India aftermarket, led by superior products and marketing. The standalone EBITDA margin would improve, led by lower input costs and price hikes.

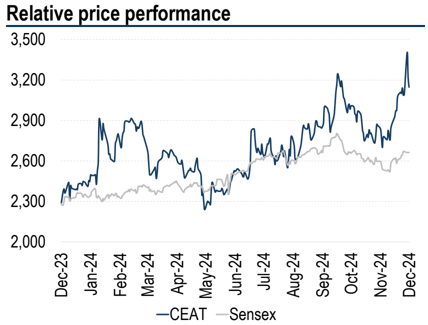
We maintain a Buy rating, with a TP of Rs3,800 (earlier Rs3,700), 16x FY27e P/E for the current business and Camso at ~Rs100, 18x FY27e P/E (EPS of Rs5.8). The applied multiple for Camso's valuation is higher than that of current stream due to better operating margins and RoCE profile. We are not overly optimistic regarding the acquisition due to the risk of slower underlying industry growth (increasing radialization), competitive pressure on the value segment and higher debt.

Key details. Acquisition includes Camso brand, two factories in Sri Lanka, normal working capital and brand licensing fee (three years). After the end of the licensing period, the company can also enter Camso's other portfolios like agri, harvester, mining, solid tyres and powersport (a portfolio, which Michelin has retained). Cost of acquisition is US$225m (~Rs19bn), which is equivalent to that of setting up a similar capacity. Key customers include JCB, CNH, Meritor, Renault and Kubota. Michelin would completely exit the bias compact CE. The acquisition would be completed by Q1 FY26.

Key data	CEAT IN / CEAT.BO
52-week high / low	R3,581/2,211
Sensex / Nifty	81510 / 24610
3-m average volume	$10.0m
Market cap	Rs.127bn / $1501m
Shares outstanding	40m

Shareholding pattern (%)	Sept'24	Jun'24	Mar'24
Promoters	47.2	47.2	47.2
- of which, Pledged	-	-	-
Free float	52.8	52.8	52.8
- Foreign institutions	16.7	18.8	20.2
- Domestic institutions	19.7	17.1	15.9
- Public	16.4	16.9	16.7

Relative price performance



Source: Bloomberg

Key financials (YE Mar) – C (Camso not consolidated)	FY23	FY24	FY25e	FY26e	FY27e
Sales (Rs m)	1,13,149	1,19,435	1,30,913	1,44,214	1,57,453
Net profit (Rs m)	2,196	7,008	5,568	7,927	9,361
EPS (Rs)	54.3	173.3	137.7	196.0	231.4
P/E (x)	58.0	18.2	22.9	16.1	13.6
EV / EBITDA (x)	15.2	8.7	9.7	7.8	6.9
P/BV (x)	3.7	3.2	2.9	2.5	2.1
RoE (%)	3.3	11.2	9.3	11.8	12.4
RoCE (%)	7.0	15.1	11.7	14.1	14.5
Dividend yield (%)	0.4	1.0	1.1	0.9	1.1
Net debt / equity (x)	0.6	0.4	0.4	0.3	0.3

Source: Company, Anand Rathi Research

Mumuksh Mandlesha
Research Analyst

Shagun Beria
Research Associate

Quick Glance – Financials and Valuations (Consol)

Fig 1 – Income statement (Rs m)

Year-end: Mar	FY23	FY24	FY25e	FY26e	FY27e
Revenues	1,13,149	1,19,435	1,30,913	1,44,214	1,57,453
Growth (%)	20.8	5.6	9.6	10.2	9.2
Raw material cost	73,854	69,244	81,166	87,250	94,472
Direct costs + SG&A	29,557	33,669	34,941	38,491	42,024
EBITDA	**9,738**	**16,522**	**14,806**	**18,474**	**20,957**
EBITDA margins (%)	8.6	13.8	11.3	12.8	13.3
- Depreciation	4,693	5,088	5,529	5,999	6,508
Other income	169	197	217	239	263
Interest expense	2,421	2,691	2,464	2,608	2,753
PBT	2,793	8,941	7,031	10,105	11,959
Effective tax rates (%)	26	25	25	25	25
+ Associates / (Minorities)	120	282	296	325	358
Adjusted income	**2,196**	**7,008**	**5,568**	**7,927**	**9,361**
Extraordinary item Profit/(Loss)	-334	-582	74	-	-
Reported PAT	1,862	6,427	5,642	7,927	9,361
WANS	40	40	40	40	40
FDEPS (Rs)	54.3	173.3	137.7	196.0	231.4
Growth (%)	161.1	219.1	-20.5	42.4	18.1

Fig 2 – Balance sheet (Rs m)

Year-end: Mar	FY23	FY24	FY25e	FY26e	FY27e
Share capital	405	405	405	405	405
Net worth	34,396	40,426	44,676	51,415	59,371
Debt	20,927	16,289	17,789	18,289	19,789
Minority interest	174	97	97	97	97
DTL / (Assets)	3,873	4,509	4,509	4,509	4,509
Capital employed	**59,370**	**61,322**	**67,072**	**74,310**	**83,767**
Net tangible assets	60,083	61,738	66,209	72,210	80,703
Net intangible assets	878	742	742	742	742
Goodwill	-	231	231	231	231
CWIP (tang. & intang.)	5,961	6,835	6,835	6,835	6,835
Investments (strategic)	1,696	1,821	1,821	1,821	1,821
Investments (financial)	-	-	-	-	-
Current assets (excl. cash)	26,929	27,987	31,869	34,358	37,040
Cash	719	591	1,559	1,844	1,962
Current liabilities	36,895	38,623	42,194	43,732	45,567
Working capital	-9,966	-10,636	-10,326	-9,373	-8,527
Capital deployed	**59,370**	**61,322**	**67,072**	**74,310**	**83,767**

Fig 3 – Cash-flow statement (Rs m)

Year-end: Mar	FY23	FY24	FY25e	FY26e	FY27e
PBT	2,459	8,359	7,401	10,431	12,317
+ Non-cash items	4,693	5,088	5,529	5,999	6,508
Oper. prof. before WC	7,152	13,447	12,930	16,429	18,824
- Incr. / (decr.) in WC	-2,211	-2,674	311	952	846
Others incl. taxes	2,692	1,014	705	105	-203
Operating cash-flow	12,055	17,136	13,324	15,582	17,775
- Capex (tang. + intang.)	8,779	8,668	10,000	12,000	15,000
Free cash-flow	**3,276**	**8,468**	**3,324**	**3,582**	**2,775**
Acquisitions	-	-	-	-	-
- Div. (incl. buyback & taxes)	126	485	1,392	1,189	1,404
+ Equity raised	-	-	-	-	-
+ Debt raised	-41	-4,638	1,500	500	1,500
- Fin investments	-24	-117	-	-	-
- Misc. (CFI + CFF)	-2,730	-3,412	-2,464	-2,608	-2,753
Net cash-flow	356	-185	969	285	118

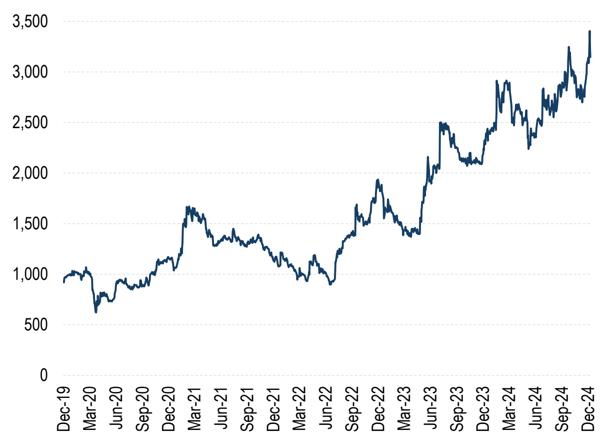
Note: Camso not consolidated. Source: Company, Anand Rathi Research

Fig 4 – Ratio analysis

Year-end: Mar	FY23	FY24	FY25e	FY26e	FY27e
P/E (x)	58.0	18.2	22.9	16.1	13.6
EV / EBITDA (x)	15.2	8.7	9.7	7.8	6.9
EV / Sales (x)	1.3	1.2	1.1	1.0	0.9
P/B (x)	3.7	3.2	2.9	2.5	2.1
RoE (%)	3.3	11.2	9.3	11.8	12.4
RoCE (%) - after tax	7.0	15.1	11.7	14.1	14.5
RoIC	7.0	15.3	11.9	14.5	14.9
DPS (Rs)	12.0	30.0	34.4	29.4	34.7
Dividend yield (%)	0.4	1.0	1.1	0.9	1.1
Dividend payout (%)	26.1	7.6	24.7	15.0	15.0
Net debt / equity (x)	0.6	0.4	0.4	0.3	0.3
Receivables (days)	42	39	39	39	39
Inventory (days)	56	61	64	64	64
Payables (days)	112	123	121	119	117
CFO: PAT %	549	245	239	197	190

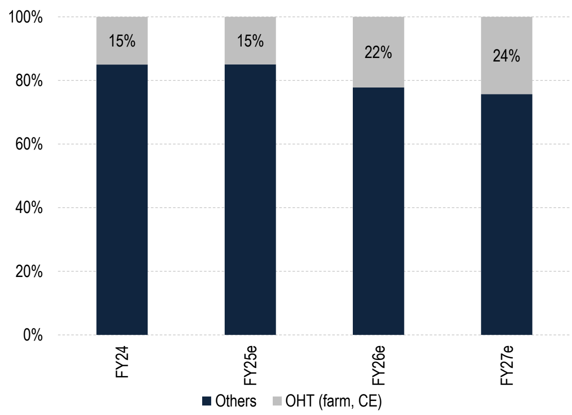
Source: Company, Anand Rathi Research

Fig 5 – Price movement



Source: Bloomberg

Fig 6 – High-margin OHT's revenue share to increase on Camso's takeover



Source: Company

Call takeaways

- **Key revenue growth drivers** are cross-selling products through respective distribution and targeting Camso's other segments (~US$1bn revenue has been retained by Michelin) like agri by leveraging the brand. The company expects Camso's acquisition and dual brand strategy to support market-share gains in OEM and aftermarket in agri and CE segments. Sri Lanka, Nashik/Bhandup plants would be capable of serving the market. The high-margin OHT segment's share would increase to ~25-26% of Ceat's revenue post-acquisition.
- **Acquisition** includes Camso brand, two factories in Sri Lanka, normal working capital and brand licensing fee (three years). After the end of the licensing period, the company can also enter Camso's other portfolios like agri, harvester, mining, solid tyres and powersport (a portfolio which Michelin has retained). Cost of acquisition is US$225m (~Rs19bn), which is equivalent to that of setting up a similar capacity. Key customers are JCB, CNH, Meritor, Renault and Kubota. Michelin would completely exit the bias CE segment. Acquisition to be completed by Q1 FY26.
- Product development teams are part of acquisition and involve Sri Lankan and outside employees. No layoffs are expected and there is an established plan of 100 days' business continuity, with Michelin transferring the entire value chain.
- **Michelin's rationale** for sale of asset could be due to radialization (as this asset is mainly in the bias segment) and on emergence of value segment in bias tyre.
- **Ceat's strategy** is based on three pillars: increasing shares from premium, international and speciality (OHT) segments. Camso's products are in speciality and premium, with realization of US$5.5-7 per kg vs/ Ceat's US$3-4/kg in similar category.
- **CY24 revenue and margins** to see a decline owing to a weak OEM segment and transition due to acquisition. The company expects recovery with complete transfer of supply chain by FY27. Currently, the EBITDA margin is in mid-teens and has the potential of ~20% on a steady state. Acquisition to be EPS accretive over 1-2 years.
- **Market size (compact CE tyres)** is US$2bn, equally split between bias tyres and tracks. The underlying industry has been growing for tyres at 2-3% and for tracks at 5-7% historically. Tracks to remain bias forever, while tyres would see some radialization, but core segments would remain bias.
- Camso broadly covers well in product range (SKUs ~750) and market reach (200 distributors). It has minimal overlap with Ceat in terms of products and distributors. Also, it supplies to 40 OEMs. Employees are ~1,600. Camso grew at 5-7% in the past.
- **Revenue** is split equally between tyres (1/3rd of market is premium) and track (50% of market is premium) segments. OEM's share is 53% and aftermarket's 47%. US' share is 60%, Europe's 30%, South America's 4% and RoW's 6%. Overall market share is in double digits in the premium segment, with second position (~20% share) in rubber tracks (mainly the premium segment with higher margins and involves proprietary technologies) and ~10% share in tyres.

- **Capex**. Current utilization is 65%, with capacity of 200m tonnes/day equally split between tyres and tracks. Ahead, for the current plants, capex would be minimal, with some hardware capex to become completely independent of the supply chain. Plants have upgraded over the last few years, hence no major capex is required. The capacity is not fungible between tyres and tracks. The RoCE is higher than that of the Indian business. Depreciation would not be more than 5-6% of gross block.
- **Debt/equity** would increase from 0.5x to 1x and debt/EBITDA from 1.2x to 3x.

Valuations

Current business

Healthy volume outlook for replacements, OEMs and exports. Price hikes are expected in FY25, to mainly cover higher input costs. We expect a 10% revenue CAGR over FY24-27. Ceat to outpace the industry, led by premium product positioning and marketing.

Margins to improve. The EBITDA margin would improve, led by lower input costs and price hikes. We expect a post-tax RoCE of >10% and the EBITDA margin at >10%. We have factored in Rs12.3bn annual capex for FY24-27.

Camso

The takeover would expand the company's presence in the higher profitability OHT segment. Further, it would strengthen its presence in agriculture to CE. It would also add OEMs and distributors (key for success). Initially, it would allow expansion in compact CE, but later open opportunities in other industrial segments like agriculture, harvester, mining and powersport, thus, leveraging the Camso brand. In the near term, due to a muted OEM segment and transition, acquisition would not be EPS accretive; however, on a steady state, acquisition would be EPS accretive. We estimate PAT to see losses of Rs150m in FY26 and then on better margins, a slight profit of Rs236m in FY27.

Valuation

We maintain a Buy rating, with a TP of Rs3,800, 16x FY27e P/E for the current business (Rs3,700) and Camso at ~Rs100, 18x FY27e P/E (EPS of Rs5.8). The applied multiple for Camso's valuation is higher than that of current stream due to better operating margins and RoCE profile.

Fig 7 – Camso's financial assumptions – small profit in FY27

Camso financials (Rs m)	FY26e*	FY27e
Revenues	17,000	17,850
y/y (%)		***5***
EBITDA	2,550	3,035
(% of revenues)	***15.0***	***17.0***
Interest cost	1,900	1,900
(% of debt)	***10.0***	***10.0***
Depreciation cost	800	820
(% of gross block)	***4.0***	***4.0***
PBT	(150)	315
Tax	0	79
(% of PBT)	***0***	***25***
PAT	(150)	236
EPS (Rs)	***(3.7)***	***5.8***
Consolidated PAT (Rs m)	**7,777**	**9,597**
Consolidated EPS (Rs)	**192.3**	**237.2**
Gross block	20,000	21,000
Debt	19,000	19,000

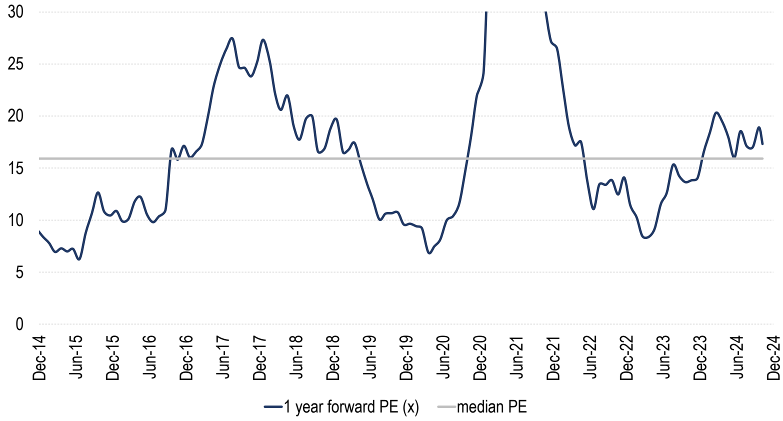
*Source: Anand Rathi Research Note: *Consolidation would be after Q1 FY26, hence for 9M financials would be consolidated.*

Fig 8 – Key assumptions – current business

Revenue (Rs m)	FY23	FY24	FY25e	FY26e	FY27e	CAGR FY24-27 (%)
Trucks and Buses	33,995	37,086	40,053	43,658	47,150	8.3
Y/Y (%)	20.9	9.1	8.0	9.0	8.0	
Two-wheelers	29,463	32,301	36,823	40,873	44,961	11.7
Y/Y (%)	12.2	9.6	14.0	11.0	10.0	
PCs	22,664	23,926	25,601	27,905	30,138	8.0
Y/Y (%)	34.3	5.6	7.0	9.0	8.0	
LCVs	9,065	8,374	8,877	9,676	10,450	7.7
Y/Y (%)	7.4	-7.6	6.0	9.0	8.0	
Farm	18,131	17,945	19,560	22,103	24,755	11.3
Y/Y (%)	28.9	-1.0	9.0	13.0	12.0	
Total	**1,13,318**	**1,19,632**	**1,30,913**	**1,44,214**	**1,57,453**	**9.6**
Y/Y (%)	20.9	5.6	9.4	10.2	9.2	

Source: Anand Rathi Research

Fig 9 – One-year-forward P/E – median is 16x



Source: Company, Anand Rathi Research

Downside risks

- Less-than-anticipated growth.
- Keener competition.
- Adverse commodity prices.

Appendix

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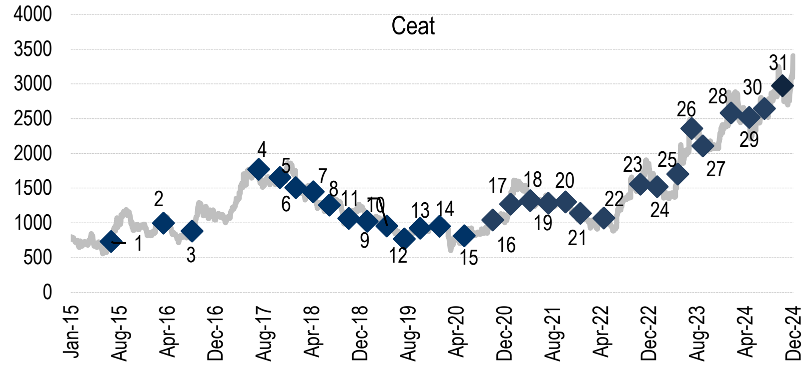

	Date	Rating	TP (Rs)	Share Price (Rs)
18	6-May-21	**Sell**	1,306	1,340
19	22-Jul-21	**Sell**	1,306	1,367
20	26-Oct-22	**Sell**	1,178	1,296
21	20-Jan-22	**Sell**	1,052	1,104
22	6-May-22	**Sell**	907	1,092
23	8-Nov-22	**Sell**	1,268	1,615
24	27-Jan-23	**Sell**	1,030	1,585
25	6-May-23	**Buy**	2,170	1,714
26	26-Jul-23	**Hold**	2,600	2,493
27	17-Oct-23	**Buy**	2,550	2,226
28	29-Jan-24	**Buy**	3,150	2,725
29	4-May-24	**Buy**	2,950	2,545
30	21-Jul-24	**Hold**	2,950	2,676
31	20-Oct-24	**Buy**	3,700	2,973

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