IndiaInfoline

Tyre Industry

Smooth drive

April 2007

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Executive summary

Tyres produced to vehicles registered growing continuously for CV and PV segments from 2001

Tyre sales to grow irrespective of short term fluctuations in automobile sales

Automobile sales is the growth driver for tyre industry. But the short term fluctuations in the automobile sales do not affect tyre sales on year on year basis. This is due to strong replacement market (RM) sales for key Commercial Vehicles (CV) segment. CV segment constitutes nearly 70% of tyre sales on value terms even though in number terms it constitutes only 25%. RM and export sales contribute more than 80% to CV segment. Thus, one of the major segments is not affected nearly by 56% in value terms due to short term fluctuation in automobile sales. We find the tyres produced to vehicles registered (a multiplier to show the demand for tyres in the country) growing for CV from 2.99 in 2001 to 3.17 in 2006 despite fluctuations in CV sales. In case of Passenger Vehicles (PV), the same has gone up from 1.13 to 1.25 in this period. RM and export sales contribute more than 60% to PV tyre sales.

Robust growth in automobile sales in the past two years to increase RM demand

Robust growth in last two years for automobile industry to have positive effect on tyre industry

We expect high growth in automobile sales in the past two years to increase demand for tyres in the coming years and improve RM sales. Indian automobile industry has been clocking high growth in the past few years, thanks to high economic growth and improved disposable income. Automobile sales and exports, except tractors, from the country have grown at 15% in FY06 and at 16.3% for April-January 2007 period. Tractor sales for April-December 2006 period rose by 25.6%.

Tyre prices increase by 15-20% in FY07 against 2-4% in previous two years

Series of price hikes reflect reduction in unhealthy competition

From April 2006, tyre producers have hiked the prices to the tune of 15-20%. Tyre companies could increase the prices of tyres by 2-4% only in FY05 and FY06. This was despite continuous increase in key raw materials like Rubber, Carbon Black and NTCF. Stiff competition in the sector to increase market share, even at the cost of reduction in margins, has eroded margins. Producers have passed on the increase in raw material prices and margins are also improving from April 2006. The reason for change in the trend is due to lack of capacity. The present capacities are running at above 90% utilization. Apart from this, the players in the industry are planning to invest in capacity expansion to meet the demand, which would require large outlay of funds and high competition would affect the capex plans.

Margins to improve as unhealthy competition comes down

Margin and PAT expansion on cards

With increase in tyre prices and softening of raw material prices, the margins of tyre producers are improving. Given the low operating margin of 5-8% at which the tyre producers were operating in the past 2-3 years, margin growth of 100 to 200 basis points itself multiplies the profit at net level for these players, which is very low at 0.5-2% at present. We believe, the margins in the industry are still not reasonable. We expect unhealthy competition to come down further among the players to support capex, which can be a surprise element.

Substitution possibility to keep NR price subdued

Rubber price expected to remain subdued

Global Natural Rubber (NR) demand growth was subdued in 2006. This was caused by steep rise in prices and resultant shifting to Synthetic Rubber (SR). We expect the volatility in NR price to reduce going forward as this leads to increased shift towards SR. We have considered average rubber price of Rs94 for FY08 and FY09 in our estimates. Domestic stock position for rubber is comfortable, which is expected to keep rubber in the estimated price band.

Stability in crude oil price to bring stability in crude based raw materials

Crude-based raw material prices also expected to stabilize

SR, Carbon Black and Nylon Tyre Cord Fabric (NTCF) are crude-based products and have strong correlation to crude oil prices. Crude-based raw materials constitute around 30% of operating expenses. In the past 6 months crude oil price has stabilized around $60 per barrel, barring the recent spike. We expect this to bring stability in crude-based raw materials.

Key Concerns

√ Threat of imports, but on quality, Indian tyres have competed well.

√ Volatility in NR prices, as the same is dependant on weather in major rubber producing nations and crude oil prices. In recent months the volatility has reduced as large scale substitution takes place towards SR if NR price spikes. In the event of sharp increase in NR prices, we expect the companies to pass on to end users.

√ Volatility in crude oil-based products and SR. In the event of sharp increase in SR prices, we expect it to be passed on.

√ Retreading to be a major concern, in the event of high tyre prices.

Valuations

Our top pick in the sector is Apollo Tyres (ATL). Tyre majors like Bridgestone and Michelin are quoting at PE of 17x and 20x respectively in the international markets. We have assigned target multiple of 12x on ATL's FY09 earnings giving a discount of 35% for the size of operations and R&D capabilities. CV tyre segment, the largest in revenue terms in India is set to grow faster with increase in road network in India. ATL is the leader in CV segment and enjoys the highest margins among peers. RM constitutes major portion in CV segment sales and possesses higher pricing power.

With economy growing at rapid pace and higher outlays for highway construction, we expect share of road transport to increase substantially in the coming years, providing ample opportunities for growth. This results in higher scope for earnings growth to ATL. We have assigned target multiple of 8x for Dunlop Tyres (DTL) earnings. DTL is having a business mix of nearly 2/3rd in Passenger car radial (PCR) & Light Truck tyres and 1/3 rd in CV tyres. We expect DTL to have a lower growth as no major capacity expansion is planned in the next two years and earnings would have growth rate of 10%. We estimate earnings from DTL to be at Rs2.8 per share in FY09. Our target for 12 month period of Rs 397 estimates Indian operations at EV/EBIDTA at 6.3x and 5.5x for FY08P and FY09P earnings. Initiating coverage with 'BUY'.

We are positive on CEAT and JK Industries (JKIL). CEAT has started focusing on high margin segments like Radial and OTR tyres and expanding tyre capacities in these two. It is modernizing its plants to achieve improvement in productivity. These efforts have started showing results in the recent quarters. The buoyancy in automobile sector and stability in raw material prices with a negative bias is expected to benefit CEAT. The investment portfolio will act as a cushion for price stability of CEAT. We have valued CEAT at 10x of its FY09 EPS of Rs10.6 and its investment portfolio with 70% haircut at Rs29. Our Sum of parts value for CEAT comes to Rs135. Initiating coverage with 'BUY'.

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JKIL is expanding its capacities and is set to benefit from improved demand from automobile sector. JKIL's focus on CV and PV radial and exports bodes well, as RM in these segments is increasing with improvement in profitability. JKIL has hived off its investment portfolio to a separate company, which is expected to re-rate the company. Initiating coverage with 'BUY and a target price of Rs135 based on FY09 earnings per share of Rs13.5 and assigning target PE of 10x.

Universe companies

		ATL	CEAT	JKIL
Net Sales (Rs mn)	FY06	26,255	17,474	26,092
	FY07P	33,446	21,314	30,550
	FY08P	36,415	23,012	33,609
	FY09P	39,175	24,614	-
OPM (%)	FY06	8.5	3.9	5.8
	FY07P	8.7	5.4	6.4
	FY08P	9.2	5.9	6.4
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APAT (Rs mn)	FY06	782	5	170
	FY07P	1,062	240	315
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NPM(%)	FY06	3.0	0.0	0.7
	FY07P	3.2	1.1	1.0
	FY08P	3.7	1.6	1.2
	FY09P	4.0	2.0	-
EPS (Rs)	FY06	20.4	0.1	5.5
	FY07P	21.1	5.3	10.2
	FY08P	27.0	8.2	13.5
	FY09P	31.2	10.6	-
ROCE (%)	FY06	8.6	8.2	6.1
	FY07P	9.7	10.4	7.4
	FY08P	10.4	11.2	8.3
	FY09P	11.1	12.3	-
RONW (%)	FY06	12.3	0.1	2.9
	FY07P	10.9	6.4	5.1
	FY08P	11.3	9.1	6.4
	FY09P	11.7	10.6	-
EV/EBIDTA (x)	FY06	7.4	8.6	7.1
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PE (x)	FY06	13.7	1032.6	20.8
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September ended year for JKIL

Tyre Industry - An overview

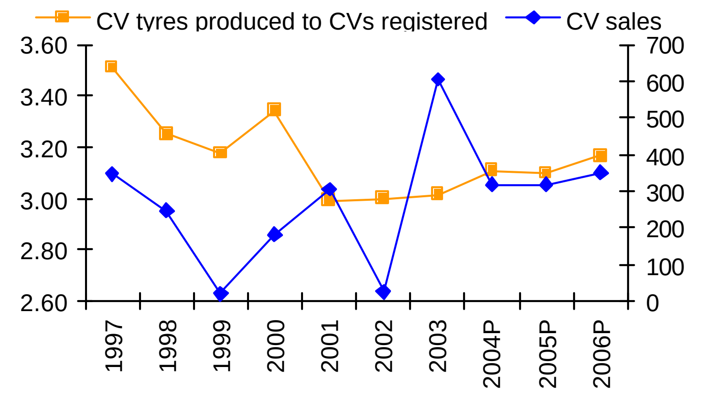
Replacement market demand contributes major portion to total sales

Tyre sales to grow irrespective of short term fluctuations in automobile sales

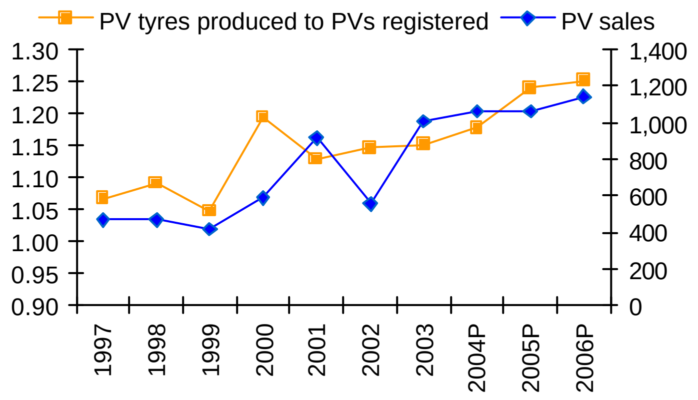
Tyre Industry's growth depends on the growth of automobile industry. But short term ups and downs in automobile sales do not have major effect on tyre production in recent years. This is due to RM sales contributing a major portion to total sales. This is particularly seen in CV segment. RM sales contributed 58.8% and exports contributed 23.3% of CV segment tyre sales in FY06. For PV segment the same was 53.7% and 7.7% respectively. OEM sales from CV segment were 17.9% only in FY06. CV segment and PV segment constitute major portion of revenues to the industry. On value terms CV tyres constitute nearly 70% of revenue to the sector and 56% of the total is from RM and exports. Economic growth is the demand driver for CV segment and short term fluctuations in automobile sales does not affect sales in this segment.

With the economy clocking above 8% growth we expect this trend to continue in the coming years. We find tyres produced to vehicles registered multiplier going up for CV segment and PV segment for recent years. The overall multiplier is coming down due to high number of two-wheeler sales in the country, which is having a very low RM.

CV tyres to CVs registered (LHS) and Domestic CV sales in 000s (RHS)

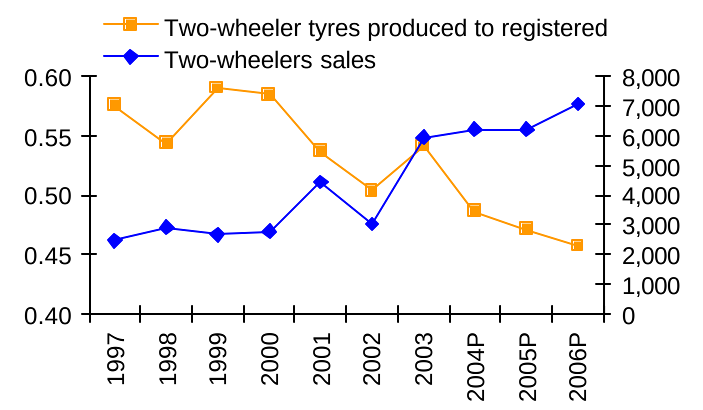


PV tyres to PVs registered (LHS) and Domestic PV sales in 000s (RHS)

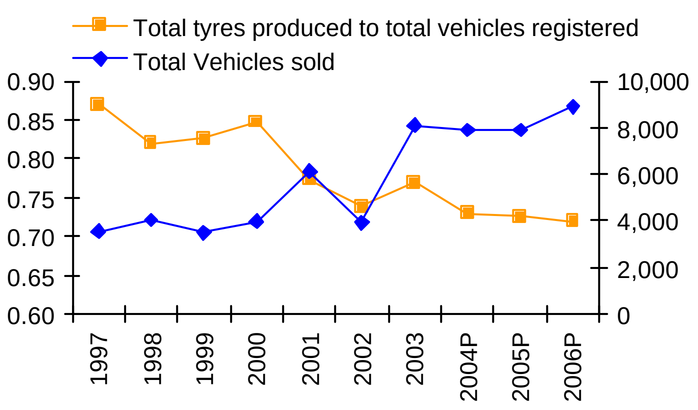


Source: Govt. of India, SIAM, ATMA, India Infoline Estimates

Two-wheeler tyres to Two-wheelers registered (LHS) and Domestic Two-wheeler sales in 000s (RHS)



Total tyres to total vehicles registered (LHS) and Total Domestic Vehicles Sales in 000 (RHS)



Source: Govt. of India, SIAM, ATMA, India Infoline Estimates

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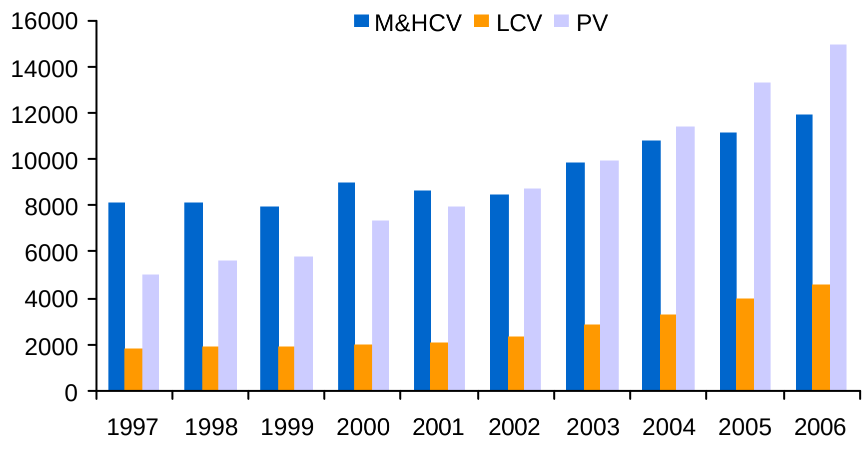
Strong economy and growing disposable income to drive demand for tyres

Demand to grow for CV and PV tyre segments

Tyre demand (Domestic plus Export) in CV segment and PV segment has grown by 9% CAGR and 13.4% CAGR respectively in FY01-FY06. For FY06, the demand for CV and PV has gone up by 9.5% and 12% respectively. We expect the growth rates to pickup from 3.2% and 5.3% in the current year so far to 7% and 12% in the next two years for CV and PV tyre segments respectively as economy continues to be strong and OEM sales clocking good volumes in the current year.

Tyre sales for major segments



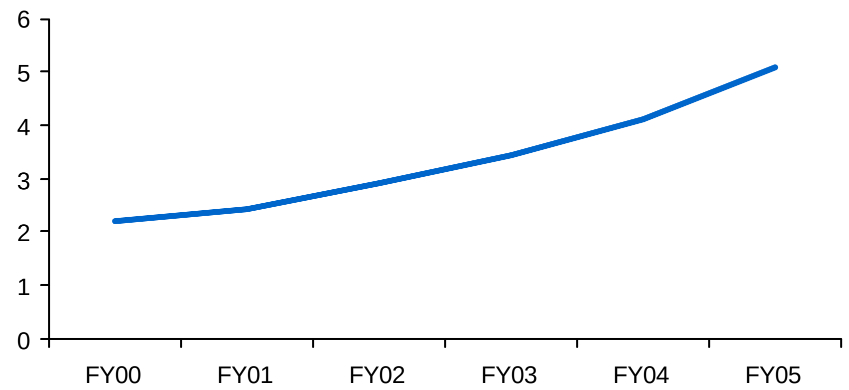
Source: ATMA

Proximity to rubber producing nations and low cost labour to improve tyre exports from India

Huge export potential for Indian players

We expect exports in PCR segment to increase substantially in the coming years although T&B segment may witness reduction due to lack of capacity to cater to the domestic market. The quality of Indian tyres is well accepted in the global market. Closer proximity to rubber producing countries and low cost labour compared to Western countries is helping exports to improve from India. In number terms, exports contributed 8.2% of the total sales in FY06 compared to 6.8% in FY02. T&B segment and PV segment clocked 7.5% and 38.3% CAGR respectively in this period.

Tyre Exports (in mn nos.)



Source: ATMA

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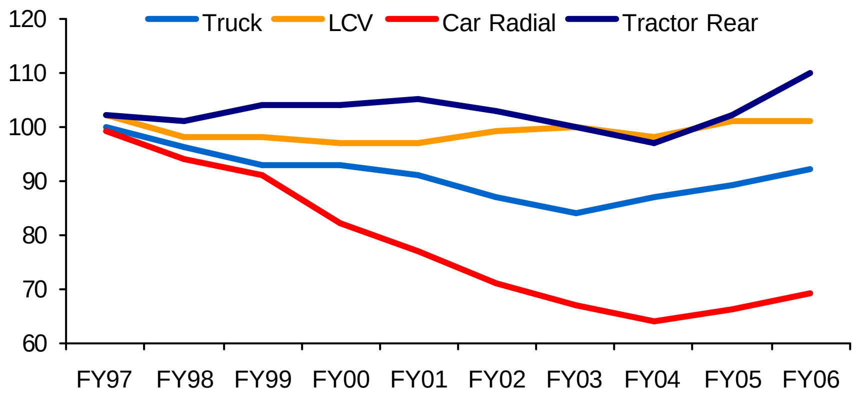
High capacity utilization rates in CV tyres to allow prices to improve

Supply constraints to keep the tyre prices at higher levels

All the players in CV segment are running at 95-100% capacity utilization. We see no major capacities coming to cater to the growth rate of 7% for CV segment as the players who have announced for CV tyres are mostly in radial segment. These new capacities are expected to commence production after 18-24 months. In PV segment, producers are benefited by strong demand for vehicles. We find with high RM sales, producers are able to pass on the cost increases. RM sales in PV segment have shown a 10.6% and 21.4% growth in FY05 and FY06. The tyres produced to vehicles registered in PV segment are also on a continuous rise indicating increasing share of RM in PV tyre segment, which brings better pricing environment for the producers.

High capacity utilization and lesser spare capacity will allow tyre producers to pass the cost increases and improve the margins by nearly 100-200 bps in next two years. Tyre prices in the international market are also firming up which is benefiting domestic companies. In 2006, tyre companies increased tyre prices by 15-20% for RM and 18-22% for OEM segment.

Price index of major segments of tyres



Source: Industry

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Competitiveness in tyre industry

Tyre prices increase by 15-20% in past one year reflects reduction in unhealthy competition to capture market share

Reduction in unhealthy competition another positive

Tyre companies could increase the prices of tyres by 2-4% only in FY04 and FY05. This was despite continuous increase in key raw materials like Rubber, Carbon Black and NTCF. Stiff competition in the sector to increase market share, even at the cost of reduction in margins, has resulted in reduction in margins. From April 2006, tyre producers have hiked the prices to the tune of 15-20%. Producers have passed on the increase in raw material prices and margins are also improving. The reason for change in the trend is due to lack of capacity. The present capacities are running at above 90% utilization. Apart from this the players in the industry are planning to invest in capacity expansion to meet the demand, which would require large outlay of funds and high competition would affect the capex plans.

To cater to the increasing demand for CV tyres, major tyre companies are planning to invest in increasing the capacity. Apollo Tyres, is investing Rs4bn in TamilNadu to increase its CV tyre capacity. This capex includes investment for PV tyre capacity. CEAT is planning to invest Rs7bn over next 3-4 years in expanding capacity, which includes CV tyre capacity. MRF is planning to invest Rs6bn in the next two years including CV tyre capacity.

Stability in key raw material prices to improve margins

Margin expansion on cards

With increase in tyre prices and softening of raw material prices, the margins of tyre producers are improving in the recent quarters. The gap between OEM prices and RM prices has also come down. OEM realisations are historically down by 10-15%, which has reduced by nearly 5% in recent times. Tyre companies have started focusing on increasing exports, where margins are better compared to OEM segment.

We expect margins to improve for tyre producers by 100 to 200 basis points if the current pricing and cost environment continues. Apart from improvement in margin, what is more fascinating is the low margins at which the tyre manufacturers are operating. This leads to explosive growth at PAT levels as PAT margin is in the range of 0.5-2% at present. Margin expansion of 100-200 bps at operating levels could lead to more than doubling PAT. We believe, the margins in the industry are still not reasonable. We expect unhealthy competition to come down further among the players to support capex, which can be a surprise element.

Positive outlook for OEM sales

We expect automobile sales to grow strongly in the coming years as road infrastructure improves in the country. Favorable demographics and increasing disposable income are catalysts for increase in automobile sales. Compliance to loading restrictions is expected to boost demand for CVs. We expect tyre sales for OEM segment for CV and PCR to increase rapidly due to loading restrictions and increasing disposable income. We expect overall demand for CV tyres to grow by 7% and for PV by 12%.

Government's mission to make India as global automotive hub augurs well for tyre industry

Government last year unveiled an ambitious plan to make India a global hub for automobiles and auto components by 2016. Exports have grown 20% CAGR for auto components in the past five years and tyre exports have grown at 18% CAGR. Major companies like Ford, GM, and Toyota already source auto components from India.

Slew of expansions and new facilities in automobile sector in the coming years is expected to perk up demand for Indian tyre manufacturers. Global majors like Volkswagen, Nissan, Renault and BMW have planned to put up facilities in India. Existing majors like Maruti, Toyota, Honda and GM are expanding their capacities.

Raw material scenario

Natural Rubber stock position in India is comfortable at present

Natural Rubber volatility to be temporary

Tyre industry is raw material intensive. Raw materials constitute nearly 70% of the sales realisation. NR accounts for nearly 50% of the total raw materials costs followed by NTCF at 23% and Carbon black at 10%. Prices of these major raw materials depend on demand supply situation and have high correlation with crude oil price movement. NR price spiked sharply in the first half of 2006 as demand outpaced supply in the past two years. NR price increased nearly 200% in the last three years. The volatility in NR prices is expected to come down in the mid term as production is increasing for NR.

India NR demand supply trend (in mn ton)

Particulars	FY04	(%) Growth	FY05	(%) Growth	FY06	(%) Growth	FY07P	(%) Growth
Production	0.71	10	0.75	5	0.80	7	0.85	6
Imports	0.04	69	0.07	57	0.05	(35)	0.08	82
Exports	0.08	37	0.05	(39)	0.07	61	0.05	(31)
Consumption	0.72	3	0.76	5	0.80	6	0.84	5
Closing stock	0.09	(28)	0.11	25	0.08	(25)	0.12	52

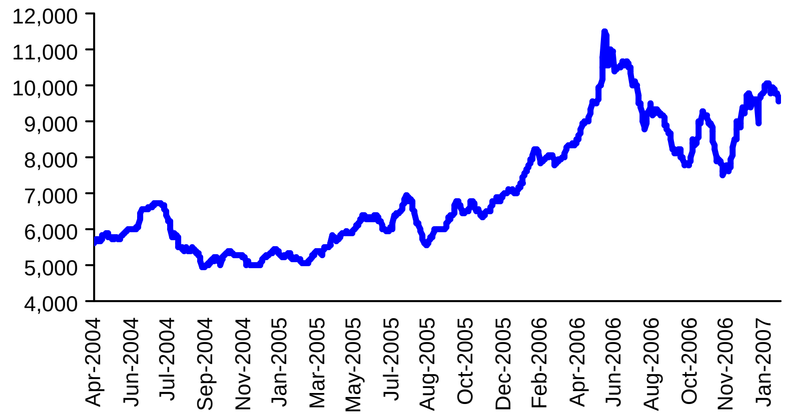
Source: Industry

% of Major producing countries in world NR production

	2001	2002	2003	2004	2005
Thailand	31.9	35.6	36.0	34.5	34.1
Indonesia	22.1	22.2	22.4	23.9	24.8
Malaysia	12.1	12.1	12.3	13.5	13.4
India	8.7	8.7	8.8	8.6	8.7
China	6.4	6.4	6.0	5.6	5.2
Vietnam	4.6	5.1	4.8	4.8	5.2
Others	14.1	9.9	9.6	9.1	8.7

Source: Industry

Domestic rubber price trend (Rs per quintal)



Source: Industry sources, India Infoline Estimates

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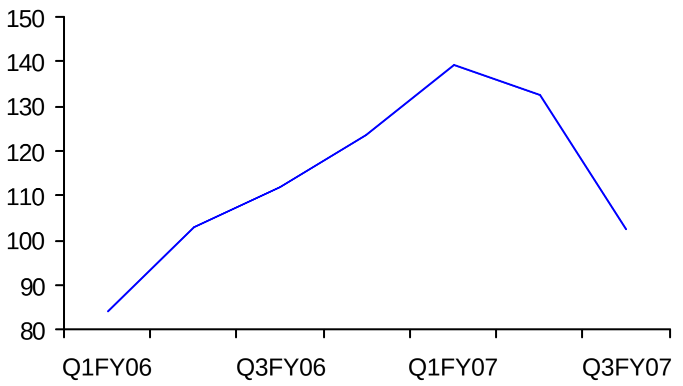
Sharp spikes in Natural Rubber leads to demand shifting to Synthetic Rubber and brings prices down

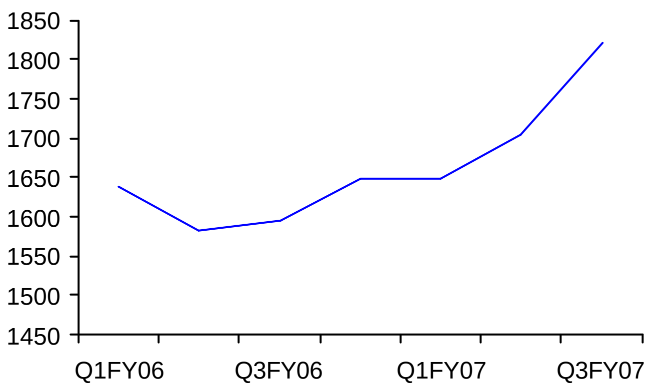
Spike in NR price shifts demand to SR at global level and leads to fall in price

We expect increase in NR production and high NR/SR price trend to keep NR prices at lower levels in the next two years. The sharp increase in NR price has led to more substitution by SR at global levels. NR and SR can be substituted to some extent in tyre manufacturing and have high correlation in their prices. The price of SR has not spiked the way NR prices did in the current year, which led to substitution and later a steep fall in NR prices. In the first half of 2006, global NR demand decreased by 1% but SR demand increased by 4.8%. With NR producers increasing production due to high prices in the past three years, supply is expected to go up.

International NR/SR price trend



International SBR prices

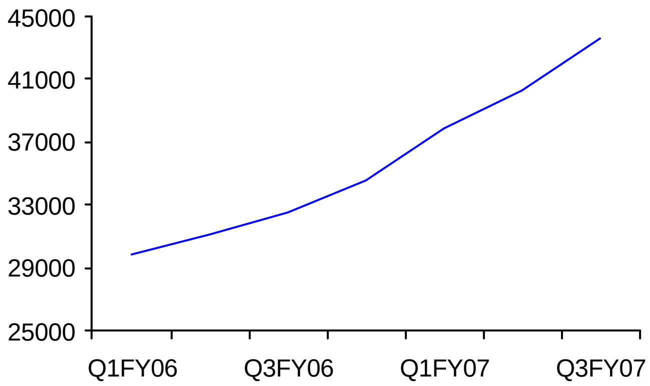


Source: Industry, India Infoline Estimates

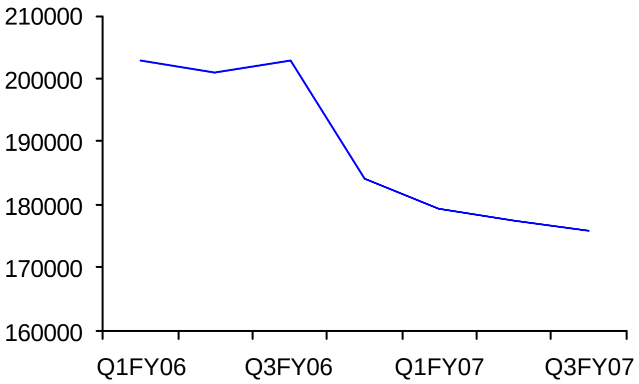
Other crude-based raw materials also expected to remain stable

With crude oil price stabilizing, we expect crude oil-based raw material prices to stabilize going forward. NTCF, Carbon Black and SR are the other three major raw materials after NR in the production of tyres. All the three raw materials have high correlation to crude oil price movements but with a lag as these products require multiple stages of processing. Prices have started stabilizing for these products with a negative bias.

Carbon black price trend (Rs per ton)



NTCF price trend (Rs per ton)



Source: Industry

Key concerns

Unhealthy competition among players to improve market share

Tyre industry is one segment in the gamut of automobile industry, which has suffered margin erosion in the past three years despite a buoyant automobile industry. Unhealthy competition among the players to get higher market share has led to erosion in margins. With high capacity utilization levels and huge capex plans to fund, fierce competition is coming down. We expect the trend to continue for next 2-3 years.

Threat of imports

Imports from China and Thailand at very lower prices can affect the demand for Indian tyres. This assumes more importance due to inverted duty structure between tyres and NR. Import duty on tyres is 10% whereas the import duty on NR, the basic raw material, is 20%. This puts Indian tyre manufacturers at a disadvantage. On quality front, the imported tyres do not match with the quality of Indian tyres, which has kept imports low. Recently, provisional anti-dumping duty was imposed on imports from China and Thailand but the reference price was fixed at $88.82 for non-radial lorry and bus tyres, which is very low to the prevailing prices in the domestic market. This can only be taken as a positive sign for the industry with no immediate benefits.

Volatility in crude oil-based products and SR

Crude oil-based products and SR is having high correlation with crude oil price movement. Crude oil price movement has become highly volatile in the past four years. But in the last six months it is trading in a range. We expect tyre producers to pass on the cost increase if the crude oil-based product prices increases sharply.

Volatility in NR prices

NR, being an agricultural produce tends to get affected by the vagaries of weather God. Pricing also gets affected by crude oil price movement and US$ movement vis a vis Thai Bhat, as Thailand exports nearly 43% of world's natural rubber exports. We expect tyre producers to pass on the cost increase if the rubber price increases sharply.

Retreading to be a major concern in the event of high tyre prices

CV tyre users tend to retread the tyres two to three times to reduce the cost per km for tyres. Retreading is the process of bonding a new flap of pre-vulcanized rubber in the place of the worn-out flap. It is more popular in Southern States compared to Northern States due to road conditions. Retreading becomes a major threat when tyre prices go up sharply. But the multiplier of tyre produced to vehicles registered in CV and PV segment is showing positive trend in the past few years and we find this threat is reducing in recent years.

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September ended year for JKIL

BUY

CMP Rs279

Apollo Tyres

INITIATING COVERAGE

Stock Data

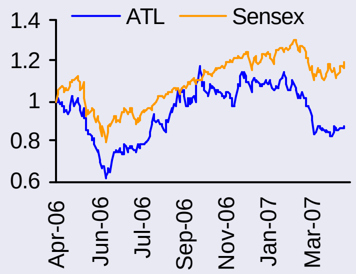
Target Price	Rs397
Upside	42.3%
Sensex	13,384
52 Week H/L	Rs387/194
Average Volumes	24,305
Market Cap	Rs13bn
Face Value	Rs10
BSE Code	500877
NSE Code	APOLLOTYRE

(Price as on 13th Apr' 07)

Share Holding Pattern

Mar'07	(%)
Promoters	32
Institutions	26
Public	8
Others	34

Share Price Trend



Apollo Tyres (ATL), the leading CV tyre player in India is expanding capacity at a rapid pace both organically and inorganically. With automobile sector booming and international automobile majors setting shops in India, we expect ATL to be a major beneficiary. We expect ATL's topline and bottom line to grow by 14.3% and 26.2% respectively between FY06 to FY09. We expect EPS to grow by 15.2% from FY06 to FY09. We find the recent fall in ATL's share price a good opportunity to enter. Initiating coverage with BUY and a target price of Rs 397.

Huge expansion plans augur well for ATL

ATL is expanding PCR tyre capacity by 1.1mn units and LTR tyre capacity by 0.1mn units by the end of FY07 to take the total tyre capacity to 710 mt/day from 660 mt/day in FY06 (does not include tube capacity). It has planned to put up a green field capacity at Tamil Nadu near Chennai with a capex of Rs4bn in the first phase and production to start in the first half of FY09. Chennai facility will produce T&B radials to start with and add PCR later depending upon the market dynamics.

Market leader in CV segment

CV segment is the largest segment in Indian tyre industry on revenue terms. ATL is having 28% market share in T&B segment and 26% in LCV segment in FY 2007. It has recently launched T&B radials, a segment poised to grow above 20% in the coming years.

Robust volume growth with margin expansion

We expect ATL to have volume growth of 10.2% CAGR in number terms and 6.9% CAGR in tonnage terms. Little extra capacity and strong demand growth has led to returning of pricing power to tyre companies. Despite flaring prices of key raw materials like natural rubber and crude-based products ATL has been able to maintain margins in the first nine months of FY07. We expect margins to improve from 8.5% in FY06 to 9.2% and 9.5% respectively in FY08 and FY09.

Strong cash flow to help expansions

We expect ATL to grow organically as well as inorganically in coming years. Strong cash flow generation in the next two years will take care of expansion plans and ATL would be still left with more cash. We expect ATL to use this to grow inorganically the way it did with Dunlop Tyres International (DTL) acquisition, which has a presence in South Africa and Zimbabwe.

Key Financials

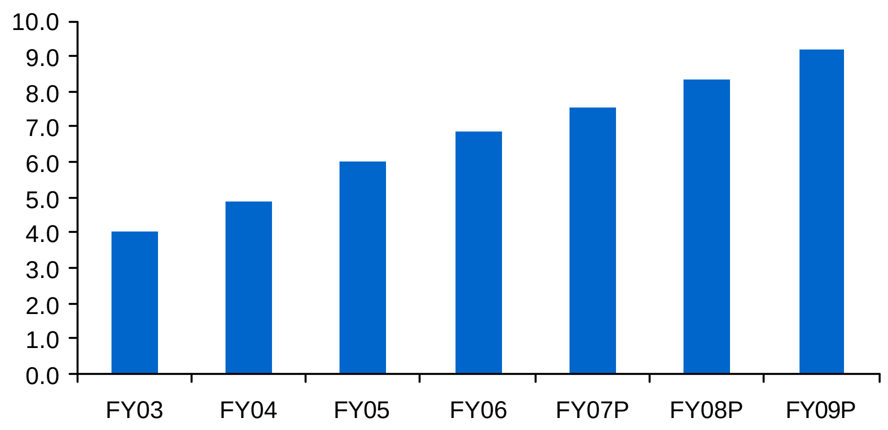
Period	FY05	FY06	FY07P	FY08P	FY09P
Net Sales (Rs mn)	22,255	26,255	33,446	36,415	39,175
Growth %	-	18.0	27.4	8.9	7.6
APAT (Rs mn)	676	782	1,062	1,359	1,572
Growth %	-	15.6	35.9	28.0	15.6
OPM %	7.4	8.5	8.7	9.2	9.5
ROCE (%)	9.0	8.6	9.7	10.4	11.1
RONW (%)	11.7	12.3	10.9	11.3	11.7
Adjusted EPS (Rs)	17.6	20.4	21.1	27.0	31.2
PE(x)	15.8	13.7	13.2	10.3	8.9
EV/EBIDTA (x)	8.4	7.4	5.5	4.8	4.3

ATL's tyre volumes on tonnage expected to grow by 7.4% and 7.0% in FY08 and FY09 respectively

Strong volume growth led by buoyancy in auto sector

Robust growth in economy and automobile sector has helped tyre sector to record impressive numbers in the past few years. We expect ATL's tyre volumes to grow at 11.2% and 9.6% and in tonnage terms by 7.4% and 7.0% in FY08 and FY09 respectively. We expect PCR volumes to grow faster for ATL as this segment is witnessing higher OEM growth. ATL is expanding capacity at its Vadodara plant to cater higher growth in PCR segment. We expect a lower growth of 6% in T&B bias segment due to capacity constraints.

Tyre Sales Volume of ATL (in mn nos.)



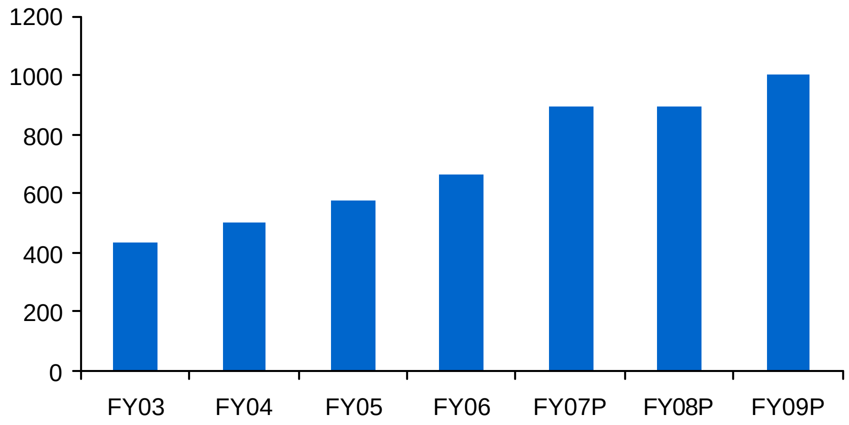
Source: Company, India Infoline Estimates

ATL's Greenfield capacity for T&B and PCR radials is expected to commence production by FY09

Huge capacity expansion on cards

ATL has expanded its tyre capacity from 430 tpd in FY03 to 660 tpd in FY06, an increase of 15.0% CAGR. ATL's domestic capacity is set to touch 710 tpd in FY 07. Apart from this ATL has acquired DTL in current year which having capacity of 150 tpd in South Africa and 30 tpd in Zimbabwe. ATL has planned to put up a Greenfield capacity near Chennai with 110 tpd in the intial phase and with a terminal capacity of more than 200 tpd. Tamil Nadu capacity will have production facility for T&B radial and PCR. Tamil Nadu facility will cater the high growth T&B radial which is expected to grow from the present 4% to 10% by 2010 out of the total T&B tyre sales. ATL has earmarked Rs.4bn for the first phase of this Greenfield expansion. This facility is expected to commence production from the first half of FY09.

ATL's capacity trend



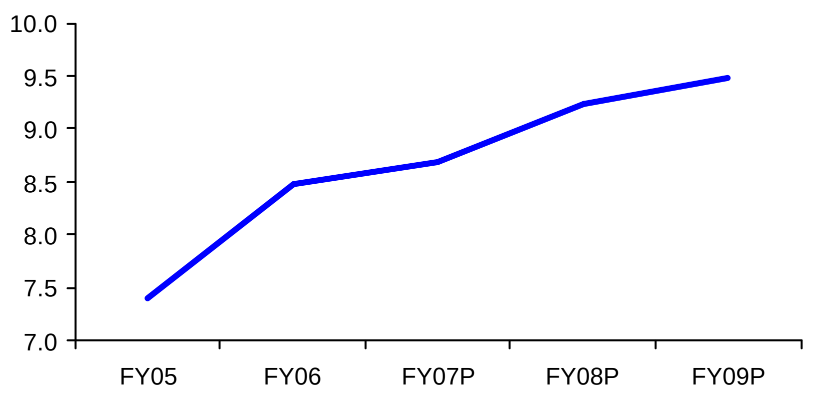
Source: Company, India Infoline Estimates

Higher presence in CV segment has helps ATL improve margins

Improvement in margins despite cost pressures

Prices of key raw materials like NR and crude based raw materials have been going up for the past three years, but the same had little impact on ATL's margins. Margin pressure in CV segment is lesser compared to other segments. Higher presence in CV segment has benefited ATL in improving margins. With natural rubber stabilizing and crude oil price off from its peak, we expect margins to improve in FY08 and FY09. Increased radialisation in T&B segment is also expected to improve the margins.

ATL's operating margin trend (%)



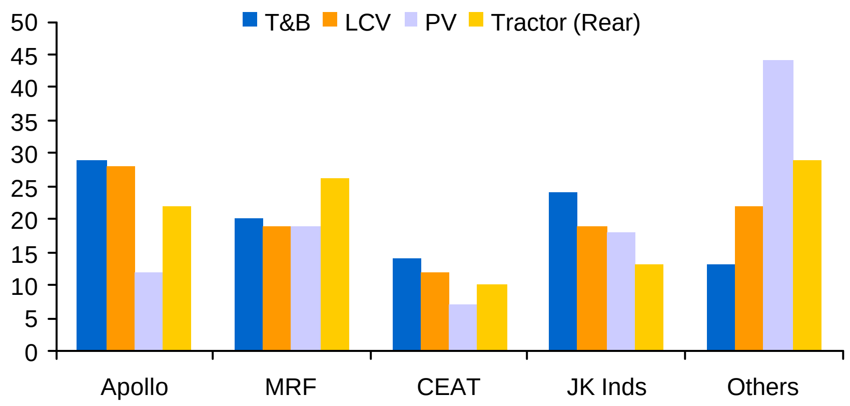
Source: Company, India Infoline Estimates

ATL is the market leader in CV segment in India

Major presence in CV tyre segment

CV tyre is the major segment on the basis of revenues for tyre producers comprising 70% of the industry revenue. ATL is the market leader in both T&B and LCV segments with domestic market share of 28% and 26% respectively in FY 2007. We expect ATL's T&B tyre sales to grow by 6% and LCV tyre sales to grow by 10% from FY06-FY09. ATL's revenues from these two segments accounts to 84%. CV segment has high level of RM business and depends less on OEM sales as compared to PV segment, which brings better pricing power to producers. ATL has built a strong brand name in this segment, which is expected to benefit in the coming years also. Going forward we expect ATL to increase its presence in PV segment by expanding capacities.

Market share of major players in different segments (%)



Source: Industry

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Acquisition of Dunlop Tyres (South Africa) to bring synergies

DTL acquisition to bring in synergies

ATL acquired DTL in April 2006 in an all cash deal for Rs2.9bn. Through DTL acquisition, ATL has become one of the top 15 tyre producers in the world. It made a preferential issue of 8mn shares at Rs310 per share in October 2006 to repay the bridge loan taken last year for DTL's acquisition. This deal has brought ATL presence in South Africa. DTL has a 150 tpd tyre capacity and produces entire range of bias and radial from high-end truck and bus tyres to industrial, farm, light truck, off-road & mining tyres and ultra high performance car tyres. Through this acquisition, ATL got substantial shareholding in National Tyre Services (NTS), Zimbabwe, a major tyre distributor and re-treading company. NTS has a technology tie-up with Bandag, the global leader in the field of re-treading technology.

DTL has turned around in the current year and started making profits. For the nine months period ended December 2006 it made sales of Rs7.5bn. EBIDTA margin for the nine months stood at 8.6% and net profit margin at nearly 1%. Even though DTL acquisition may not bring immediate profits to ATL, we expect synergy benefits to accrue in the long term as this gives greater access to European and Australian markets and radial technology.

Valuations

We have assigned target multiple of 12x on ATL's FY09 India operations. CV tyre segment, the largest in revenue terms in India is set to grow faster with increase in road network in India. ATL is the leader in CV segment and enjoys the highest margins among peers. RM constitutes major portion in CV segment sales and possesses higher pricing power. With economy growing at rapid pace and higher outlays for highway construction we expect share of road transport to increase substantially in the coming years, providing ample opportunities for growth. This results in higher scope for earnings growth to ATL.

We have assigned target multiple of 8x for DTL's estimated FY09 earnings. DTL is having a business mix of nearly 2/3rd in PCR & light truck and 1/3rd in CV tyres. We expect DTL to have a lower growth as no major capacity expansion is planned in the next two years and earnings would have growth rate of 10%. We estimate earnings from DTL to be at Rs2.8 per share in FY09.

	FY07P	FY08P	FY09P
ATL EPS (Indian Operations)	21.1	27.0	31.2
DTL EPS (SA operations)	2.3	2.5	2.8
ATL EPS @ 12x			374
DTL EPS @ 8x			23
Estimated Value (Rs)			397

Our target of Rs 397 for 12 months estimates Indian operations at EV/EBIDTA at 6.6x and 5.9x for FY08P and FY09P earnings. Initiating coverage with 'BUY'.

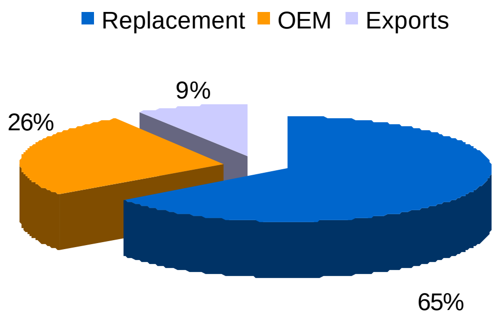
Company background

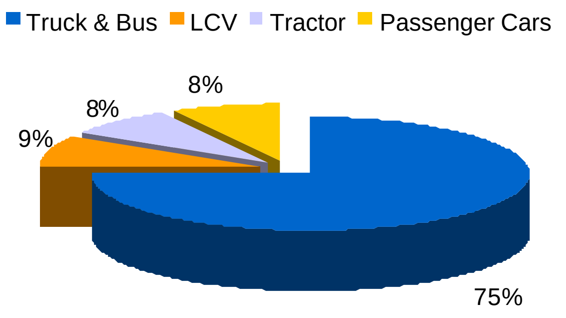
ATL is the largest CV tyre manufacturer in India. It is ranked 15th in the global tyre industry after acquisition of DTL. It has three tyre plants in India, two plants in South Africa and one plant in Zimbabwe with a total capacity of 890 tpd. Its products profile includes T&B bias and radial, LCV bias and radial, PV radial, Farm bias and radial and OTR bias. It does not have a presence in two wheeler tyres. It has a wide product range and sells under various brands including popular brands like XT, Loadstar, Amazer, Accelere.

Country-wise tyre capacity (tpd)

	FY06	FY07P	FY08P	FY09P
India	660	710	710	820
South Africa	150	150	150	150
Zimbabwe	30	30	30	30
Total	**840**	**890**	**890**	**1000**

Revenue segmentation of ATL's India operations





Source: Company

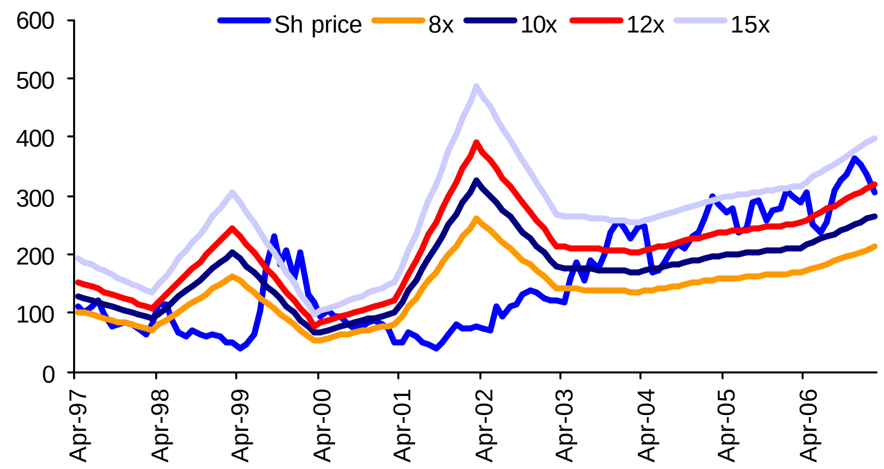
Impact of change in rubber price

Change by	FY08		FY09	
	PAT	EPS	PAT	EPS
+5%	927	18.4	1,102	21.9
+3%	1,100	21.8	1,290	25.6
+2%	1,186	23.5	1,384	27.5
Base Case	1,359	27.0	1,572	31.2
-2%	1,532	30.4	1,760	34.9
-3%	1,619	32.1	1,854	36.8
-5%	1,792	35.6	2,042	40.5

Impact of change in tyre price

Change by	FY08		FY09	
	PAT	EPS	PAT	EPS
+3%	2,069	41.1	2,347	46.6
+2%	1,833	36.4	2,089	41.4
+1%	1,596	31.7	1,830	36.3
Base Case	1,359	27.0	1,572	31.2
-1%	1,123	22.3	1,313	26.1
-2%	886	17.6	1,055	20.9
-3%	649	12.9	796	15.8

One-year forward PE chart of ATL



Source: BSE, India Infoline Estimates

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Financials

Income Statement

(Rs mn)	FY05	FY06	FY07P	FY08P	FY09P
Net Sales	22,255	26,255	33,446	36,415	39175
Total Expenses	(20,607)	(24,028)	(30,544)	(33,050)	(35,458)
Operating Profit	1,648	2,227	2,903	3,365	3,717
Other Income	198	70	5	10	10
Interest	(429)	(506)	(533)	(544)	(569)
Depreciation	(568)	(728)	(740)	(740)	(860)
PBT	849	1,064	1,634	2,091	2,298
Tax	(173)	(282)	(572)	(732)	(727)
PAT	676	782	1,062	1,359	1,572
EPS	17.6	20.4	21.1	27.0	31.2

Balance Sheet

(Rs mn)	FY05	FY06	FY07P	FY08P	FY09P
Sources of Funds					
Share Capital	383	383	464	504	504
Reserves	5,384	5,957	9,241	11,531	12,902
Net Worth	5,767	6,340	9,705	12,035	13,406
Loans	5,439	7,500	5,500	5,000	4,500
Deffered Tax Liability	1,034	1,052	1,302	1,302	1,302
Total	**12,240**	**14,892**	**16,507**	**18,337**	**19,208**
Application of Funds					
Gross Block	11,484	13,106	13,885	13,885	18,185
Less: Depreciation	(3,983)	(4,699)	(5,439)	(6,179)	(7,039)
Net Block	7,501	8,407	8,446	7,706	11,146
Capital WIP	843	779	500	2,500	200
Investments	545	5	2,905	2,905	2,905
Current Assets	7,436	10,105	10,254	11,284	11,457
Current Liabilities	(4,090)	(4,407)	(5,602)	(6,061)	(6,503)
Net Current Assets	3,346	5,698	4,653	5,223	4,954
Deffered Rev Exps	4	3	3	3	3
Total	**12,240**	**14,892**	**16,507**	**18,337**	**19,208**

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Ratios

	FY05	FY06	FY07P	FY08P	FY09P
Per Share Ratios					
EPS (Rs)	17.6	20.4	21.1	27.0	31.2
Div Per Share	4.5	4.5	4.5	4.5	4.5
Book Value Per Share	150.4	165.4	209.1	238.9	266.0
Valuation Ratios					
P/E	15.8	13.7	13.2	10.3	8.9
P/BV	1.9	1.7	1.3	1.2	1.0
M Cap/Sales	0.5	0.4	0.4	0.4	0.4
EV/EBIDTA	8.4	7.4	5.5	4.8	4.3
Dividend Yield	1.6	1.6	1.6	1.6	1.6
Profitability Ratios					
OPM(%)	7.4	8.5	8.7	9.2	9.5
PAT(%)	3.0	3.0	3.2	3.7	4.0
ROCE(%)	9.0	8.6	9.7	10.4	11.1
RONW(%)	11.7	12.3	10.9	11.3	11.7
Liquidity Ratios					
Current Ratio	1.8	2.3	1.8	1.9	1.8
Debtor Days	25.7	24.3	24.3	24.3	24.3
Inventory Days	58.5	63.7	63.7	63.7	63.7
Creditor Days	67.3	63.2	63.2	63.2	63.2
Leverage Ratios					
Debt/ Equity	1.7	1.9	1.1	0.9	0.8
Payout Ratios					
Dividend Payout	29.5	25.5	18.5	14.5	12.8

Cash Flow Statement

(Rs mn)	FY05	FY06	FY07P	FY08P	FY09P
Cash flow from operating activities					
PBT	849	1,064	1,634	2,091	2,298
Depreciation	568	728	740	740	860
Change in WC	(220)	(1,143)	(422)	(176)	(163)
Taxes paid	(6)	(235)	(322)	(732)	(727)
Others	(105)	376	-	-	-
Total (a)	1,086	789	1,630	1,924	2,269
Cash flow from investing activities					
Purchase of fixed assets	(1,982)	(1,594)	(500)	(2,000)	(2,000)
Purchase of investments	-	1	-	-	-
Investment in Subsidiary	-	-	(2,900)	0	0
Others	360	685	-	-	-
Total (b)	(1,622)	(908)	(3,400)	(2,000)	(2,000)
Cash flow from financing activities					
Borrowings	1,589	2,481	1,000	0	0
Loans repaid	(365)	(422)	(3,000)	(500)	(500)
Dividend and tax thereon	(199)	(199)	(197)	(201)	(201)
Equity raised	-	-	2,499	1,172	0
Others	(448)	(531)	-	-	-
Total (c)	577	1,328	302	471	(701)
Net Increase in cash (a+b+c)	41	1,209	(1,468)	395	(432)
Opening cash balance	1,064	1,104	2,314	846	1,240
Closing cash balance	1,104	2,314	846	1,240	808

BUY

CMP Rs117

CEAT

INITIATING COVERAGE

Stock Data

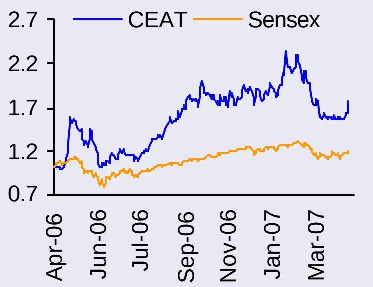
Target Price	Rs130
Upside	15.4%
Sensex	13,384
52 Week H/L	Rs162/64
Average Volumes	168,311
Market Cap	Rs5.4bn
Face Value	Rs10
BSE Code	500878
NSE Code	CEAT

(Price as on 13th Apr' 07)

Share Holding Pattern

Dec'06	(%)
Promoters	43
Institutions	25
Public	18
Others	14

Share Price Trend



CEAT, a diversified tyre major, is ramping up its production facilities to benefit from the uptrend in automobile industry. It has planned to modernize its existing facilities and double its OTR capacity, which will boost volumes in FY08 and FY09. We estimate top line and bottom line to grow by 12.1% and 454.5% respectively from FY06-FY09. The proposed sale of part of land at its Bhandup facility is expected to boost its capex plans of putting up T&B radial tyres in the next two years. Investment portfolio to the tune of Rs95 per share is expected to act as a cushion for the company. Initiating coverage with 'BUY'.

Capacity expansion to boost volume growth

CEAT is ramping up its capacity by modernization and increasing PCR and OTR capacity. We expect CEAT to have volume growth of 11.8% and 6.7% on tonnage terms in FY08 and FY09. We expect PCR, OTR and two-wheeler segments to have higher growth in next two years. CEAT has planned to put a Greenfield T&B radial facility in the next two years. We have not considered this in our estimates as the project is in conceptualization stage.

Modernizing PCR capacity

CEAT has plans to increase its PCR tyre capacity and modernize its existing facilities with a capex of Rs200mn. PCR segment is seeing robust growth in the past few years with rising economy and disposable incomes. CEAT is also focusing on high margin OTR segment and planning to increase its OTR capacity. CEAT has earmarked Rs500mn for more than doubling its OTR capacity from 40,000 tyres per year to 100,000 tyres per year. We expect these measures to boost productivity and improvement in volumes for FY08 and FY09.

Margins to improve as CEAT focuses on exports and OTR segment

Export sales and OTR tyres are getting better margins compared to OEM segment. With focus to improve export and higher OTR tyre sales by CEAT, we expect margins to improve in FY08 and FY09. We estimate operating margins to improve by 230 bps to 6.2 in FY09. PAT margin is expected to improve from negligible levels in FY06 to 2% in FY09.

Land sale to support capex

CEAT plans to sell 7 acres out of total 32 acres at its Bhandup facility. We estimate this to fetch around Rs1bn for the company and help its capex plans. Apart from this, it has raised Rs450mn through ECB issued in October 2006.

Key Financials

Period	FY05	FY06	FY07P	FY08P	FY09P
Net Sales (Rs mn)	15,280	17,474	21,314	23,012	24,614
Growth %	-	14.4	22.0	8.0	7.0
APAT (Rs mn)	(67)	5	240	373	486
Growth %	-	-	4,535.8	55.4	30.3
OPM %	2.6	3.9	5.4	5.9	6.2
ROCE (%)	5.25	8.21	10.35	11.19	12.28
RONW (%)	-1.07	0.15	6.43	9.09	10.59
Adjusted EPS (Rs)	-	0.1	5.3	8.2	10.6
PE(x)	-	1,032.6	22.3	14.3	11.0
EV/EBIDTA (x)	8.1	8.6	6.4	5.5	4.8

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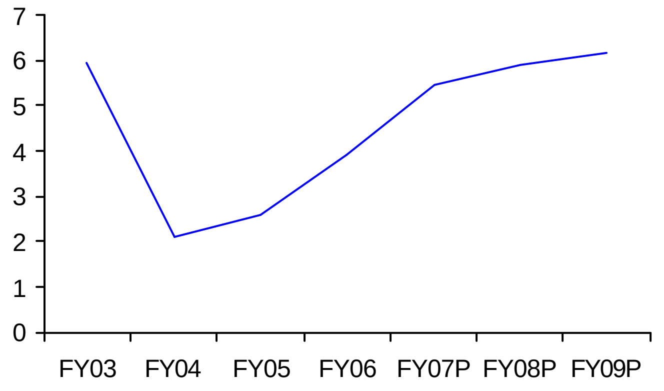
Focus on exports and radialization to improve margins for CEAT

Margins to improve as CEAT focuses on product mix

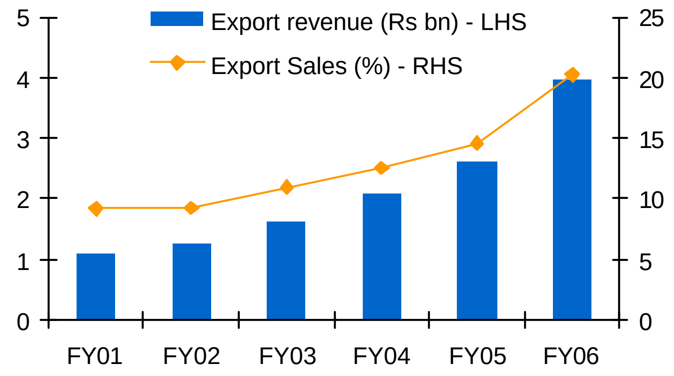
CEAT is doubling its OTR tyre capacity in the next one year at a capex of Rs500mn. CEAT has plans to increase its PCR tyre capacity and modernize its existing facilities with a capex of Rs200mn. It is focusing more on exports to expand margins. Currently, revenues from exports constitute 21%. Increased focus on exports, OTR tyre sales and stability in raw materials are expected to help CEAT improve its margins. CEAT pays Octroi to Maharashtra Government at around 1.5% of its sales. There are indications that Maharashtra Government may abolish this tax, which would boost CEAT's margins. We have not considered this in our estimates and if it materializes this would add to CEAT's margins.

Operating margin of CEAT (%)



Source: Company, India Infoline Estimates

Export trend of CEAT



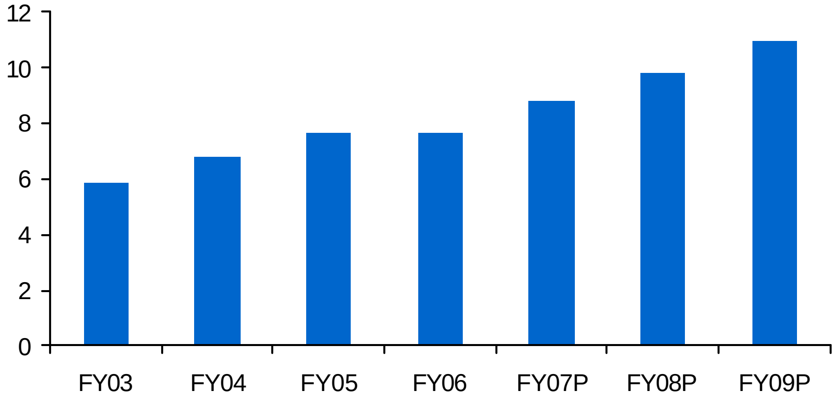
Source: Company

CEAT is modernizing PCR tyre facility and doubling OTR tyre capacity

Volume growth through capacity expansion and modernization

CEAT is expanding its OTR tyre capacity in a phased manner from 40000 tyres to 60,000 in FY07 and to 100,000 tyres by FY08. CEAT has identified OTR segment as high growth segment and ramping up capacity as margins in this segment is double compared to CV and PV segments. CEAT has planned to increase its CV and PV tyre capacity by putting a mixing mill and modernizing PCR facility. The overall capex for these expansions is Rs700mn. CEAT is present in two-wheeler tyre segment through outsourcing model and can expand volumes. We expect 11.8% growth on volume terms and 6.7% growth on tonnage terms for FY08 and FY09.

Sales volume of CEAT (mn units)



Source: Company, India Infoline Estimates

CEAT is having a huge investment portfolio with market value coming close to 80% of CMP

Huge portfolio of investments in CEAT's books

CEAT is holding a huge portfolio of investments in group companies. The per share value of this portfolio comes to Rs95. With a haircut of 70%, at which most of the investment companies are traded per share value still comes to Rs29. We expect this to act as cushion for the price movement of CEAT shares.

CEAT's land sale at Bhandup, Mumbai to help capex plans

Sale of Bhandup property to boost capex plans

CEAT has decided to sell 7 acre land out of its 32 acre property at Bhandup, Mumbai. We expect this to fetch around Rs1bn. As the exact amount of deal is not finalized, we have not assumed this in our cash flows. It has recently raised Rs450mn through ECB also for expansion plans. Apart from this CEAT is also expected to have better operating cash flows due to improved business prospects. We expect these cash flows to help capex plans. CEAT is planning to put up T&B radial facility in next two years at a capex of Rs4.5bn. We have not considered this in our estimates as the plans are not finalized.

Valuations

CEAT has started focusing on high margin segments like OTR tyres and expanding tyre capacities in OTR tyres. It is modernizing its plants to achieve improvement in productivity. These efforts have started showing results in the recent quarters. The buoyancy in automobile sector and stability in raw material prices with a negative bias is expected to benefit CEAT. The investment portfolio will act as a cushion for price stability of CEAT. We have valued CEAT at 10x of its FY09 EPS of Rs10.6 and its investment portfolio with 70% haircut at Rs29. Our Sum of parts value for CEAT comes to Rs135. Initiating coverage with 'BUY'.

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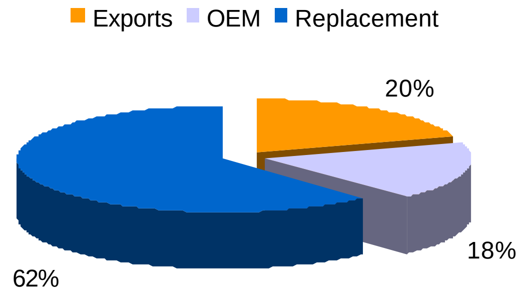
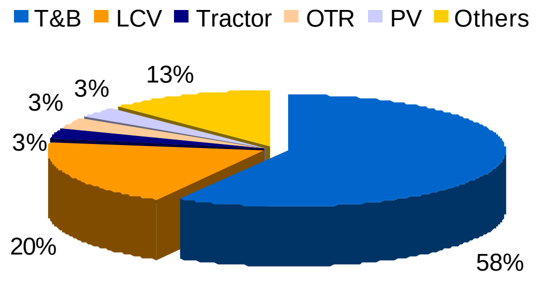
Company background

CEAT is a diversified tyre major with presence in T&B, LCV, PCR, Two-wheeler, Tractor, OTR and others segments. Its popular brands include LUG and RIB in T&B and LCV segments, SAMRAAT in Tractor, ENDURA in PV segment and SECURA in two-wheeler segment. It has a total capacity of 385 tpd in two plants in Maharashtra. It sources two-wheeler tyres from private players.

Revenue segmentation of CEAT





Source: Company, India Infoline Estimates

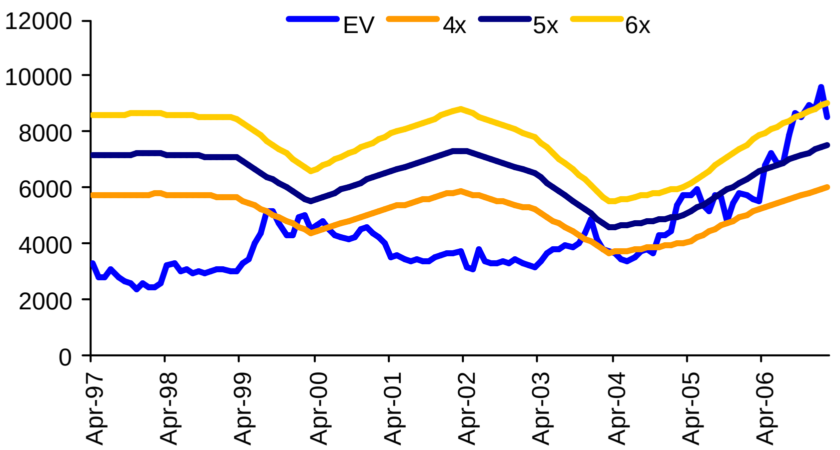
Impact of change in rubber price

Change by	FY08		FY09	
	PAT	EPS	PAT	EPS
+5%	63	1.4	156	3.4
+3%	187	4.1	288	6.3
+2%	249	5.4	354	7.7
Base Case	373	8.2	486	10.6
-2%	497	10.9	618	13.5
-3%	559	12.2	684	15.0
-5%	683	14.9	816	17.9

Impact of change in tyre price

Change by	FY08		FY09	
	PAT	EPS	PAT	EPS
+3%	856	18.7	1,003	22.0
+2%	695	15.2	831	18.2
+1%	534	11.7	658	14.4
Base Case	373	8.2	486	10.6
-1%	212	4.6	314	6.9
-2%	51	1.1	141	3.1
-3%	-110	-2.4	-31	-0.7

One-year forward EV/EBIDTA chart of CEAT



Source: BSE, India Infoline Estimates

IndiaInfoline

Financials

Income Statement

(Rs mn)	FY05	FY06	FY07P	FY08P	FY09P
Net Sales	15280	17474	21314	23012	24614
Total expenses	(14884)	(16788)	(20154)	(21651)	(23,092)
Operating profit	396	686	1160	1361	1523
Other income	389	226	150	160	160
PBIDT	785	912	1310	1521	1683
Interest	(642)	(636)	(645)	(626)	(626)
Depreciation	(221)	(224)	(306)	(362)	(362)
PBT	(77)	52	358	533	694
Tax	10	(47)	(118)	(160)	(208)
PAT before EO	(67)	5	240	373	486
EO	49	-	-	-	-
PAT after EO	(19)	5	240	373	486
EPS	-	0	5.3	8.2	10.6

Balance Sheet

(Rs mn)	FY05	FY06	FY07P	FY08P	FY09P
Sources of Funds					
Share Capital	351	457	457	457	457
Reserves & Surplus	5,950	3,033	3,273	3,646	4,132
Networth	6,301	3,490	3,730	4,103	4,589
Loans	4,506	4,176	4,626	4,626	4,276
Deffered Tax Liability	130	140	193	193	193
Total	**10,938**	**7,806**	**8,549**	**8,922**	**9,058**
Application of Funds					
Fixed Assets	8,898	11,068	11,068	11,711	11,911
Less Depreciation	(3,604)	(3,851)	(4,157)	(4,520)	(4,882)
Net Block	5,294	7,217	6,911	7,191	7,029
Capital WIP	150	43	343	100	100
Investments	1,908	1,278	1,278	1,278	1,278
Current Assets	9,613	5,393	6,293	6,566	6,752
Current Liabilities & Provisions	(6,028)	(6,125)	(6,276)	(6,213)	(6,101)
Net Working Capital	3,585	(732)	18	353	651
Total	**10,938**	**7,806**	**8,549**	**8,922**	**9,058**

IndiaInfoline

Ratios

	FY05	FY06	FY07P	FY08P	FY09P
Per Share Ratios					
EPS (Rs)	-	0.1	5.3	8.2	10.6
Div Per Share	-	-	-	-	-
Book Value Per Share	179.5	76.4	81.7	89.8	100.5
Valuation Ratios					
P/E	-	1,032.6	22.3	14.3	11.0
P/BV	0.7	1.5	1.4	1.3	1.2
M Cap/Sales	0.3	0.3	0.2	0.2	0.2
EV/EBIDTA	8.1	8.6	6.4	5.5	4.8
Dividend Yield	-	-	-	-	-
Profitability Ratios					
OPM(%)	2.6	3.9	5.4	5.9	6.2
PAT(%)	(0.4)	0.0	1.1	1.6	2.0
ROCE(%)	5.3	8.2	10.4	11.2	12.3
RONW(%)	(1.1)	0.1	6.4	9.1	10.6
Liquidity Ratios					
Current Ratio	1.6	0.9	1.0	1.1	1.1
Debtor Days	56.5	52.9	52.9	51.3	49.8
Inventory Days	41.2	39.9	39.9	39.9	39.9
Creditor Days	136.4	124.8	106.7	98.2	90.3
Leverage Ratios					
Debt/ Equity	1.7	3.0	2.9	2.6	2.3

Cash Flow Statement

(Rs mn)	FY05	FY06	FY07P	FY08P	FY09P
Cash flow from operating activities					
PBT	(77)	52	358	533	694
Depreciation	221	224	306	362	362
Change in WC	204	(222)	(773)	(372)	(395)
Direct Taxes paid	(14)	(38)	(65)	(160)	(208)
Others	515	537			
Total (a)	848	554	(174)	363	453
Cash flow from investing activities					
Purchase of Fixed assets	(143)	(121)	(300)	(400)	(200)
Others	85	109			
Total (b)	(58)	(12)	(300)	(400)	(200)
Cash flow from financing activities					
Issue of Share Capital	0	517	0	0	0
Borrowings	572	804	450		
Loans repaid	(771)	(1,134)	0	0	(350)
Others	(668)	(645)			
Total (c)	(866)	(458)	450	0	(350)
Net Increase in Cash (a+b+c)	(77)	84	(24)	(37)	(97)
Opening Balance of Cash	389	312	396	372	335
Closing Balance of Cash	312	396	372	335	238

BUY

CMP Rs115

JK Industries

INITIATING COVERAGE

Stock Data

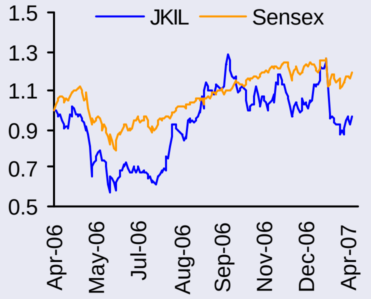
Target Price	Rs135
Upside	17.4%
Sensex	13,384
52 Week H/L	Rs160/65
Average Volumes	80,007
Market Cap	Rs3.6bn
Face Value	Rs10
BSE Code	53007
NSE Code	JKTYRE

(Price as on 13th Apr' 07)

Share Holding Pattern

Mar'07	(%)
Promoters	48
Institutions	9
Public	15
Others	28

Share Price Trend



JK Industries (JKIL), a pioneer in the T&B radial tyres with nearly 70% market share, is expected to benefit from the high growth in this segment. JKIL has hived off its investment portfolio into a separate company. We expect re-rating to the stock as JKIL will become a focused tyre play. With softening in natural rubber prices from the recent peak and buoyancy in automobile sector we expect JKIL to perform better going forward. We expect JKIL's topline and bottom line to grow by 13.5% and 55.9% respectively between FY06 to FY08 (September ended). We expect EPS to grow by 80.0% from FY06 to FY08. We value tyre business of JKIL at Rs135 per share based on 10x of its FY08 earnings of Rs13.5.

Ongoing expansion to lead volume growth

JKIL is expanding its PV and LCV radial capacity from 3.4mn units to 4.8mn units by FY07. It has expanded its T&B radial capacity from 0.26mn units to 0.37mn units last year. This ongoing expansion will help JKIL to boost its tyre volumes in FY07 and FY08. We expect tyre volumes to grow by 12.4% and 13.1% in FY07 and FY08 respectively. On tonnage terms we expect JKIL to post 9.3% and 8.0% growth. We expect better growth in T&B radial for JKIL over bias tyres as it has expanded capacity but lose market share, as other players are also vying in this space.

Better focus on tyre business

JKIL in the past few years has hived off its sugar and agri business segments to focus on tyre business. In a recent restructuring measure, it has hived of its investment portfolio into a separate company 'Netflier Finco'. 3 shares of JKIL shares and 1 share of Netflier Finco was issued for every 4 shares held prior to restructuring. This has brought down the share capital for JKIL by 25%. This will make JKIL a focused tyre player. We expect re-rating in the stock post restructuring and command better valuations.

Thrust on exports to improve topline and margins

JKIL is improving its exports in the past few years. Export constituted 14.7% of the total sales in FY06 compared to 16.1% in FY05. We expect exports to improve in coming years and have a share of more than 16% in total sales. Higher exports are expected to improve topline and margins for JKIL.

Key Financials

Period	FY05	FY06	FY07P	FY08P
Net Sales (Rs mn)	20,791	26,092	30,550	33,609
Growth %	-	25.5	17.1	10.0
APAT (Rs mn)	168	170	315	414
Growth %	-	1.7	84.8	31.5
OPM %	5.5	5.8	6.4	6.4
ROCE (%)	5.0	6.1	7.4	8.3
RONW (%)	2.1	2.9	5.1	6.4
Adjusted EPS (Rs)	4.5	4.5	10.2	13.5
PE(x)	25.7	20.8	11.2	8.5
EV/EBIDTA (x)	7.4	7.1	5.8	5.0

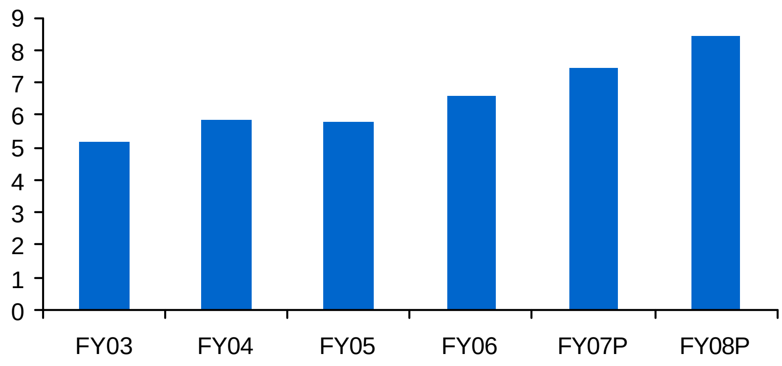
*****September ended*

JKIL to show robust growth in tyre volumes

Tyre volumes to grow with buoyancy in automobile sales

JKIL tyre volumes stood at 6.6mn units in FY06. Domestic sales stood at 57mn and exports at 9mn. JKIL has increased its tyre capacity from 6.4mn numbers to 7.4mn in FY06 and will further ramp up to 8.8mn by the end of FY07. In FY06, T&B radial capacity was increased from 0.3mn units to 0.4mn units and PV & LCV capacity was increased from 2.5mn units to 3.4 mn units. JKIL is expanding PV& LCV radial capacity from 3.4mn units to 4.8mn units in FY07. JKIL is also expanding its OTR tyre capacity by 20000 units. We expect tyre volumes to touch 7.4mn in FY07 and 8.4mn in FY08. We expect T&B radial and PV segment to have higher growth of 18% and 20% respectively whereas T&B bias segment is expected to grow by 6-7% only in this period. Growth based on tonnage is estimated at 9.3% and 8% respectively for FY07 and FY08.

Tyre sales volume of JKIL (mn nos.)



Source: Company, India Infoline Estimates

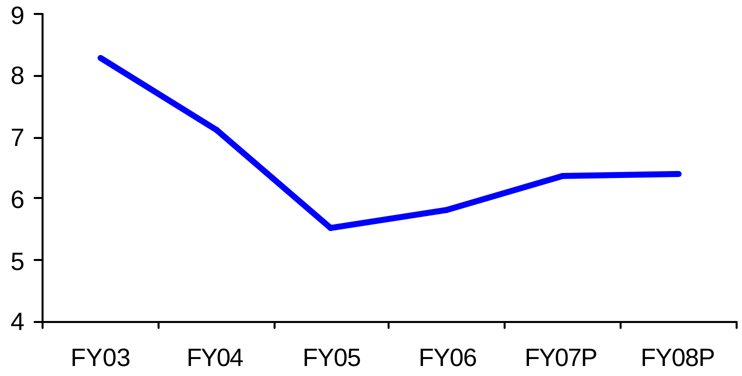
Capacity utilization for JKIL is also strong at 89.4% in FY06, slightly down from 90.6% recorded in FY05 due to capacity expansion and staggered production. Capacity utilization is expected to clock 84.6% and 95.7% in FY08 and FY09 respectively.

Operating margins to improve due to higher capacity utilization

Margins grow despite increase in raw material prices

Key raw materials like NR, SR, Carbon black and NTCF have gone up in the past 2-3 years. Higher capacity utilization and very less spare capacity have resulted in pricing power coming back to tyre producers. This has resulted in operating margins increase in FY06 over FY05 for JKIL. We expect operating margins to improve by 60 bps for FY07 and FY08 over FY06. We estimate 50 bps increase in PAT margin for JKIL in FY08 over FY06. JKIL's PAT margin for FY06 is very low at 0.6%. On absolute terms, PAT will have CAGR of 80% in FY06-FY08.

Operating margin trend of JKIL (%)



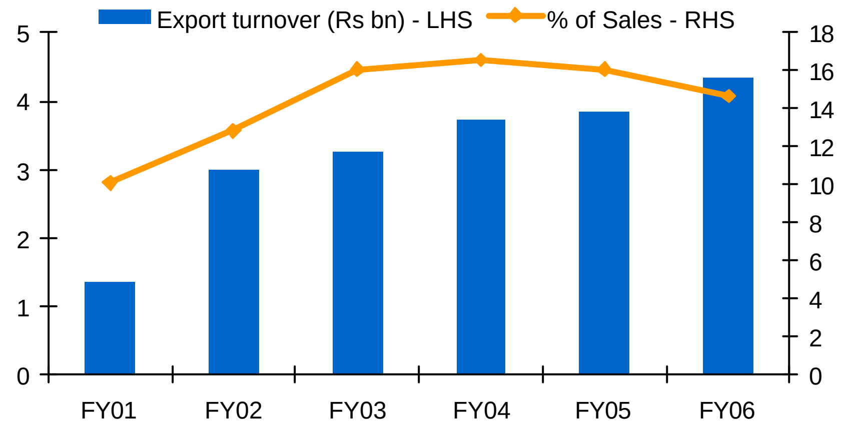
Source: Company. India Infoline Estimates

Export turnover improves continuously for JKIL

Thrust towards exports to continue

JKIL exports tyres to over 60 countries. It mainly exports T&B tyres and LCV tyres. Export turnover is increasing continuously over the last few years but as a percentage of sales it is down from 16.1% in FY05 to 14.7% in FY06. On absolute terms it increased by 13.4% to Rs4.3bn. We expect JKIL to renew the thrust towards exports and going forward percentage of exports is expected to cross 16%, particularly with higher capacities.

Export trend of JKIL



Source: Company

Continuous restructuring has helped JKIL to become a focused tyre player

Restructuring a positive for JKIL

JKIL has hived off its sugar business and agri business in the past and recently hived of its investment portfolio into a separate company. Investment to the tune of Rs1.9bn was hived off into a new company named 'Netflier Finco'. One share for every 4 shares held of JKIL was issued to represent the investment portfolio company and 3 shares were issued for tyre business. The reduced share capital for JKIL is Rs308mn. Hiving off investment portfolio would enable JKIL to focus on its core business.

We expect JKIL to reduce its debt component in the next two years due to improved cash flow and maintain its long term debt to equity ratio at 1.1 in FY08. In FY07, long term D/E would go up to 1.3 due to reduction in net worth as investment portfolio would be hived off to a separate company.

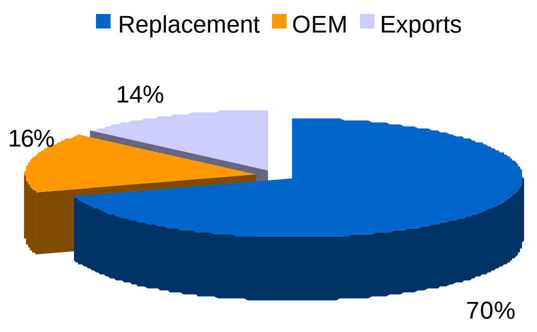
Valuations and view

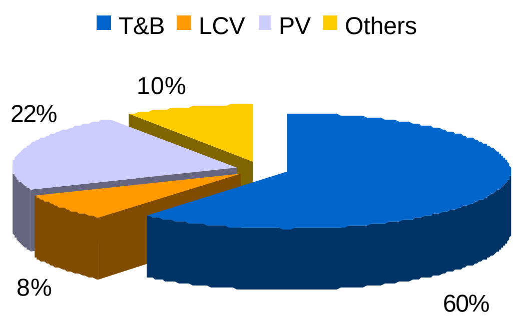
JKIL is expanding its capacities and is set to benefit from improved demand from automobile sector. JKIL's focus on CV and PV radial and exports bodes well as RM in these segments is increasing with improvement in profitability also. JKIL has hived of its investment portfolio to a separate company, which is expected to re-rate the company. Initiating coverage with 'BUY' and a target price of Rs135 based on FY09 earnings per share of Rs13.5 and assigning target PE of 10x.

Company background

JKIL is a leading player in Indian tyre industry with wide product ranges. It is a pioneer in T&B radial segment. Its product portfolio includes T&B bias and radial, LCV bias and radial, PV bias and radial, Tractor tyres and OTR tyres. It sells T&B tyres under 'JET' brand, PV tyres under 'ULTIMA' brand and farm tyres under 'SONA' brand. In FY06 it had domestic sales of 5.7mn units and exports of 0.9mn units. T&B and PV segment constituted 36% each of total volume in FY06 and the balance is distributed between LCV and others.

Revenue segmentation of JKIL





Source: Company, India Infoline Estimates

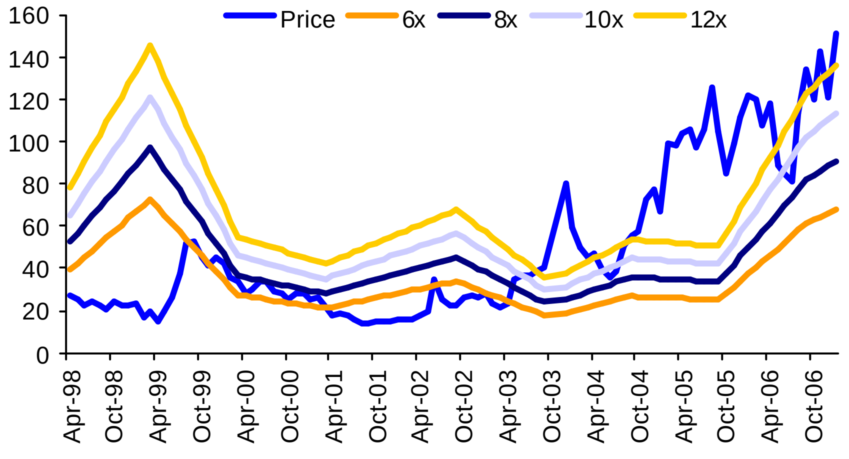
Impact of change in rubber price

Change by	FY07		FY08	
	PAT	EPS	PAT	EPS
+5%	-91	-3.0	-32	-1.0
+3%	72	2.3	147	4.8
+2%	153	5.0	236	7.7
Base Case	315	10.2	414	13.5
-2%	478	15.5	593	19.3
-3%	559	18.2	682	22.2
-5%	721	23.4	861	28.0

Impact of change in tyre price

Change by	FY07		FY08	
	PAT	EPS	PAT	EPS
+3%	929	30.2	1,090	35.4
+2%	724	23.5	865	28.1
+1%	520	16.9	640	20.8
Base Case	315	10.2	414	13.5
-1%	110	3.6	189	6.1
-2%	-94	-3.1	-36	-1.2
-3%	-299	-9.7	-261	-8.5

One-year forward PE chart of JKIL



Source: BSE, India Infoline Estimates

IndiaInfoline

Financials

Income Statement

(Rs mn)	FY05	FY06	FY07P	FY08P
Net Sales	20,791	26,092	30,550	33,609
Total Expenses	19,640	24,579	28,609	31,459
Operating Profit	1,151	1,513	1,941	2,150
Other Income	164	176	70	70
PBIDT	1,315	1,689	2,011	2,220
Interest	(645)	(762)	(796)	(812)
Depreciation	(637)	(709)	(744)	(789)
PBT	34	218	470	618
Tax	133	(48)	(155)	(204)
PAT	168	170	315	414
EPS	4.5	5.5	10.2	13.5

Balance Sheet

(Rs mn)	FY05	FY06	FY07P	FY08P
Source of Funds				
Share Capital	375	308	308	308
Reserves and Surplus	7,451	5,609	5,818	6,125
Net Worth	7,826	5,917	6,126	6,433
Loans	8,305	9,439	8,939	8,239
Deffered Tax	-	-	34	34
Total	**16,131**	**15,356**	**15,099**	**14,707**
Application of Funds				
Fixed Assets	19,387	20,842	21,067	21,617
Depreciation	(7,647)	(8,600)	(9,345)	(10,134)
Net Block	11,740	12,242	11,723	11,483
Capital WIP	616	225	550	450
Investments	2,500	615	615	615
Deffered Tax	30	16	-	-
Current Assets	8,125	10,135	11,349	12,188
Current Liabilities	(7,010)	(7,969)	(9,230)	(10,122)
Working Capital	1,115	2,167	2,119	2,066
Misc Expenses	129	92	92	92
Total	**16,131**	**15,356**	**15,099**	**14,707**

IndiaInfoline

Ratios

	FY05	FY06	FY07P	FY08P
Per Share Ratios				
EPS (Rs)	4.5	5.5	10.2	13.5
Div Per Share	2.0	2.5	2.5	2.5
Book Value Per Share	208.9	192.2	198.9	208.9
Valuation Ratios				
P/E	25.7	20.8	11.2	8.5
P/BV	0.6	0.6	0.6	0.6
M Cap/Sales	0.2	0.1	0.1	0.1
EV/EBIDTA	7.4	7.1	5.8	5.0
Dividend Yield	1.7	2.2	2.2	2.2
Profitability Ratios				
OPM(%)	5.5	5.8	6.4	6.4
PAT(%)	0.8	0.7	1.0	1.2
ROCE(%)	5.0	6.1	7.4	8.3
RONW(%)	2.1	2.9	5.1	6.4
Liquidity Ratios				
Current Ratio	1.2	1.3	1.2	1.2
Debtor Days	72.3	66.9	66.9	66.9
Inventory Days	45.4	54.7	54.7	54.7
Creditor Days	125.5	114.2	114.2	114.2
Leverage Ratios				
Debt/ Equity	2.0	2.9	3.0	2.9
Payout Ratios				
Dividend Payout	44.7	45.1	24.4	18.6

Cash Flow Statement

(Rs mn)	FY05	FY06P	FY07P	FY08P
Cash flow from operating activities				
PBT	34	218	470	618
Depreciation	637	709	744	789
Change in WC	(162)	(1,020)	(160)	(96)
Taxes paid	(7)	(33)	(105)	(204)
Others	357	582	-	-
Total (a)	859	456	950	1,108
Cash flow from investing activities				
Purchase of fixed assets	(1,025)	(1,142)	(550)	(450)
Purchase of investments	-	-	-	-
Others	202	127	-	-
Total (b)	(823)	(1,015)	(550)	(450)
Cash flow from financing activities				
Net Borrowings	740	1,133	(500)	(700)
Dividend and tax thereon	(85)	(86)	(107)	(107)
Equity raised	-	378	-	-
Others	(712)	(834)	-	-
Total (c)	(57)	591	(607)	(807)
Net Increase in cash (a+b+c)	(22)	32	(207)	(149)
Opening cash balance	382	361	393	186
Closing cash balance	361	393	186	38

Company Section - Not rated

MRF

Stock Data

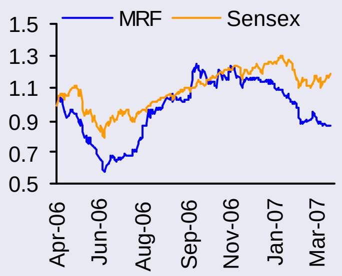
Sensex	13,384
52 Week H/L	Rs4,785/2,025
Average Volumes	1,672
Market Cap	Rs13.8bn
Face Value	Rs10
BSE Code	500290
NSE Code	MRF

(Price as on 13th Apr' 07)

Share Holding Pattern

Dec'06	(%)
Promoters	26
Institutions	13
Public	34
Others	27

Share Price Trend



MRF is the largest tyre producer in India with wide product profile. MRF produces tyres for T&B, LCV, PV, two-wheeler, tractor, OTR etc. MRF was incorporated in 1961 and presently having production facilities in 6 locations. It exports tyres to more than 75 countries. Popular brands of MRF include SUPERMILER, SUPERLUG, ZVTS and NYLOGRIP. MRF has a market share of more than 25% on number terms. MRF is having production capacity of 21.6mn tyres per year.

Highlights

Continuously expanding capacities to cater growth

MRF has expanded capacities continuously in the past few years from 13.1mn tyres in FY01 to 21.6mn tyres in FY06. Its capacity utilization also has clocked more than 90% in most of the years. In FY06 it had a capacity utilisation of 94.3%. MRF plans to invest Rs6bn to expand its capacities in next two years. It is planning to add 0.1mn tyres in PCR segment, 0.1mn tyres in two-wheeler segment and about 20,000 tyres in LCV segment.

Margins pickup in recent quarters

Operating margins of MRF has gone up in December 2006 ended quarter as NR prices and other crude-based raw material prices eased. Operating margin for December 2006 quarter stood at 8.1% against 6.5% in September 2006 quarter. For the full year ended September 2006 MRF had an operating margin of 6.2%. MRF increased tyre prices by 1% in February 2007 to maintain margin, as NR prices crossed Rs100 per kg.

Non-tyre business yet to make major impact

Apart from tyres, MRF has diversified into other rubber related businesses, albeit in a smaller magnitude in various fields like conveyor belts, speciality coatings, pre-cured re-treading system etc. MRF has a conveyor belt plant at Arkonam, Tamil Nadu, with an annual capacity of 3000 ton. Rubber coatings by MRF can be applied to metal, wood, plastics, paper, vinyl, textiles, ceramics and glass. These segments have not developed in terms of revenue generation for MRF in the past few years, but offers good potential in future. Increasing organized retail outlets, airport infrastructure and high end housing offers growth potential for these segments.

IndiaInfoline

Financials

Income Statement

(Rs mn)	FY04	FY05	FY06
Net Sales	25,391	29,499	37,245
Total expenses	(23,856)	(27,923)	(34,933)
Operating profit	1,535	1,575	2,313
Other income	547	450	635
PBIDT	2,083	2,025	2,947
Interest	(282)	(327)	(493)
Depreciation	(959)	(1,103)	(1,457)
PBT	842	595	998
Tax	(141)	(150)	(199)
PAT before EO	701	445	799
EO	(413)	(42)	(306)
PAT after EO	288	403	493
EPS	165.4	104.9	188.5

Balance Sheet

(Rs mn)	FY04	FY05	FY06
Sources of Funds			
Share Capital	42	42	42
Reserves and Surplus	7,192	7,498	8,201
Networth	7,234	7,541	8,243
Loan funds	5,604	7,100	7,289
Total	**12,838**	**14,640**	**15,532**
Application of Funds			
Gross Block	14,105	16,359	18,897
Less: Depreciation	(9,912)	(10,991)	(12,401)
Net Block	4,192	5,368	6,497
Capital Work in Progress	1,240	1,520	663
Investments	762	138	702
Deffered Tax	37	16	(124)
Current Assets	10,538	11,742	12,887
Current Liabilities	(3,931)	(4,144)	(5,092)
Net Working Capital	6,607	7,598	7,794
Total	**12,838**	**14,640**	**15,532**

Key ratios

	FY04	FY05	FY06
Per Share Ratios			
EPS	165.4	104.9	188.5
BV	1,706.2	1,778.4	1,944.1
Profitability Ratios			
OPM(%)	6.0	5.3	6.2
PAT(%)	2.8	1.5	2.1
ROCE(%)	7.7	5.3	8.3
RONW(%)	9.7	5.9	9.7
Leverage Ratio			
Debt/Equity	1.3	1.5	1.5

CMP Rs443

Balkrishna Industries

Stock Data

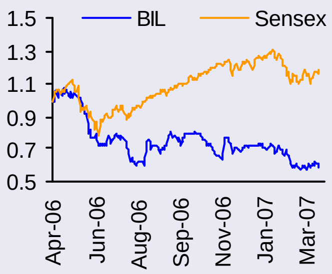
Sensex	13,384
52 Week H/L	Rs835/415
Average Volumes	3,580
Market Cap	Rs8.7bn
Face Value	Rs10
BSE Code	502355
NSE Code	BALKRISIND

(Price as on 13th Apr' 07)

Share Holding Pattern

Dec'06	(%)
Promoters	54
Institutions	11
Public	9
Others	26

Share Price Trend



Balkrishna Industries (BIL), operates in three different business segments – Pneumatic Tyres, Coated / un-coated Paperboards and Processing of Textile fabrics. Tyre segment constitutes more than 80% of revenues 95% of profits for BIL. BIL exports nearly 95% of its production. BIL is focused on wide range of Off Highway Tyres (OHT), All Terrain Vehicle (ATV) tyres and OTR tyres. These are niche segments and command better margins.

Expanding tyre capacity

At the end of FY06 BIL was having 48,000 and 18,000 tpa tyre manufacturing capacity at Bhiwadi and Waluj respectively. It has planned to increase Bhiwadi capacity by 6,000 tpa and Waluj capacity by 4,000 tpa in FY07. It has also planned to put up 30,000 tpa capacity at Chopanki. This will take the total capacity to 0.1mn ton for BIL by the end of FY07. It is also putting up a mixer at Waluj. The estimated capex for the expansion is Rs2.7bn.

Among top 10 producers in OHT globally

BIL is among top 10 producers in OHT comprising earthmover tyres, industrial tyres and agricultural & construction equipment tyres. Global tyre majors like Bridgestone and Michelin have exited the OHT business since it is too fragmented, generates low volumes and is labour-intensive. BIL on the other hand has capitalized on its strength in engineering and lower labour costs to carve out a niche in this specialty tyre segment. BIL's topline has grown at 31.9% CAGR from FY02 - FY06 to Rs6.2bn.

Margins expand in recent quarters as NR price falls

BIL commands better margins amongst Indian tyre manufactures due to focusing on niche segments. For the quarter ended December 2006 BIL posted operating margins of 20% against 17.1% in September 2006 quarter. But this is lesser against the full year OPM of 22.4% in FY06.

Focus on tyre segment

BIL has recently decided to focus on tyre business only. It has approved to transfer assets and liabilities of Paper board division and Textile processing division to wholly owned subsidiaries. This will help BIL to focus on fast expanding tyres business.

IndiaInfoline

Financials

Income Statement

(Rs mn)	FY04	FY05	FY06
Net Sales	3,652	4,884	6,200
Total expenses	(2,973)	(3,759)	(4,800)
Operating profit	679	1,124	1,400
Other income	38	53	58
PBIDT	717	1,177	1,458
Interest	(90)	(78)	(117)
Depreciation	(174)	(215)	(273)
PBT	452	884	1,067
Tax	(137)	(309)	(368)
PAT	315	575	700
EPS	25.4	46.4	36.2

Balance Sheet

(Rs mn)	FY04	FY05	FY06
Sources of Funds			
Share Capital	124	124	193
Reserves and Surplus	965	1,456	2,682
Networth	1,089	1,580	2,875
Loan funds	1,316	1,702	2,969
Deffered Tax	252	331	374
Total	**2,656**	**3,613**	**6,218**
Application of Funds			
Gross Block	2,406	3,238	3,904
Less: Depreciation	(851)	(1,043)	(1,307)
Net Block	1,555	2,195	2,598
Capital Work in Progress	147	213	689
Investments	23	21	51
Current Assets	1,518	2,223	4,127
Current Liabilities	(587)	(1,038)	(1,247)
Net Working Capital	931	1,184	2,880
Total	**2,656**	**3,613**	**6,218**

Key ratios

	FY04	FY05	FY06
Per Share Ratios			
EPS	25.4	46.4	36.2
BV	87.9	127.6	148.7
Profitability Ratios			
OPM(%)	18.6	23.0	22.6
PAT(%)	8.6	11.8	11.3
ROCE(%)	15.3	18.1	13.1
RONW(%)	28.9	36.4	24.3
Leverage Ratio			
Debt/Equity	1.7	1.7	1.5

CMP Rs149

Goodyear India

Stock Data

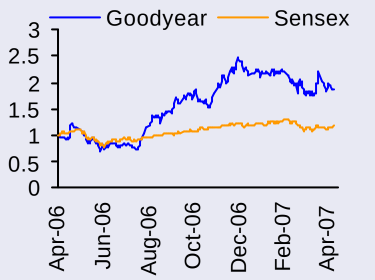
Sensex	13,384
52 Week H/L	Rs207/54
Average Volumes	25,324
Market Cap	Rs3.4bn
Face Value	Rs10
BSE Code	500168
NSE Code	GOODYEAR

(Price as on 13th Apr' 07)

Share Holding Pattern

Dec'06	(%)
Promoters	74
Institutions	2
Public	16
Others	8

Share Price Trend



Goodyear India (GIL), is the Indian subsidiary of 3rd largest global tyre major. GIL is present in PCR, tractor tyres and OTR in India. GIL is the market leader in tractor tyre segment in India. GIL is expanding its PCR capacity from 4,500 tyres per day to 10,000 tyres per day at a capex of Rs800mn. GIL is investing Rs500mn to start the shop-in-shop multi-brand concept where there is trained staff to recommend the tyres good for the cars.

GIL more than doubling PCR capacity

GIL has planned to more than double its PCR capacity to 10,000 tyres per day at a capex of Rs800mn. The expanded capacity is expected to go in for production from 2008. Apart from producing in India GIL also sources tyres from its parent for selling India. It has planned to start shop-in-shop multi brand stores to capture higher RM sales as its major sales is from OEM segment at present.

Top player in tractor tyre segment in India

GIL is the top player in tractor segment in India with market share of around 30%. It supplies to leading tractor producers like Punjab Tractors, TAFE, Escorts, ITL, and Eicher.

Margins surge despite cost pressures

GIL posted 9.6% operating margin for the September 2006 ended quarter against 6% in June 2006 quarter. For CY05 GIL had posted operating margin of 3.6%. Operating margin in OEM segment has increased at a faster pace in the past one year and reduced the gap between OEM and RM. GIL being a major OEM supplier has benefited due to this.

IndiaInfoline

Financials

Income Statement

(Rs mn)	CY03	CY04	CY05
Net Sales	5,747	6,234	6,710
Total expenses	(5,648)	(6,025)	(6,438)
Operating profit	99	209	272
Other income	162	72	92
PBIDT	260	281	364
Interest	(133)	(75)	(90)
Depreciation	(127)	(122)	(139)
PBT	1	84	134
Tax	0	(3)	(17)
PAT before EO	1	81	118
EO	(0)	(30)	(30)
PAT after EO	0	52	88

Balance Sheet

(Rs mn)	FY04	FY05	FY06
Sources of Funds			
Share Capital	231	231	231
Reserves and Surplus	532	579	666
Networth	762	810	896
Loan funds	962	913	950
Total	**1,724**	**1,723**	**1,846**
Application of Funds			
Gross Block	2,288	2,292	2,360
Less: Depreciation	(1,181)	(1,261)	(1,346)
Net Block	1,108	1,031	1,014
Capital Work in Progress	48	22	58
Investments	113	113	113
Current Assets	1,962	2,234	2,417
Current Liabilities	(1,577)	(1,717)	(1,766)
Net Working Capital	385	517	651
Misc exps	69	40	10
Total	**1,724**	**1,723**	**1,846**

Key ratios

	FY04	FY05	FY06
Per Share Ratios			
EPS	0.0	3.5	5.1
BV	33.0	35.1	38.9
Profitability Ratios			
OPM(%)	1.7	3.4	4.0
PAT(%)	0.0	1.3	1.8
ROCE(%)	7.7	9.1	11.2
RONW(%)	0.1	10.0	13.1
Leverage Ratio			
Debt/Equity	3.3	3.2	3.0

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