

ONE YEAR OUTLOOK

BUSINESS & EARNINGS ◀▶

- Revise our rating on TMKN to ADD, constrained by the recent, sharp run-up in prices. Revenue growth in 2QFY18 (+10% YoY) was constrained by the sale of traded bearings (~26% of revenue) being recorded net of indirect taxes post GST. Over the near term, expect revenue growth to be led by the 1) aftermarket demand normalising 2) pick-up in domestic CV demand and 3) a strong order book in the exports market, led by pick up in both the HCV and farm equipment segment in N. America. Expect railway ordering to be muted in FY18E, before recovering strongly from FG19E led by the conversion of Schlieren coaches and commencement of DFC ordering.
- With existing facilities running at full tilt, actualization of aforesaid revenue drivers would be enabled by the recent coming on-stream of the capacity doubling, brownfield expansion (from 2QFY18).
- Expect ABC's merger with TMKN to be carried through in 4QFY18; ABC, with its significant presence in the domestic CV wheel-end bearings segment and considerable unutilized capacities (~60%), would be a key growth driver. Expect revenue CAGR of ~28% through FY17-FY20E
- Expect improving utilization levels and increasing proportion of exports to continue to aid improvement in margin trajectory. With the superimposition of TMKN's technology and processes on ABC's operations, and other cost control measures (importantly on ABC's employee costs) expect consol margins to come in at ~19% in FY20E.
- Expect FY18E PAT to be aided by refund of spl. duty on imported bearings (refund of ~Rs.120mn in 2QFY18, expected to sustain through FY18E)

VALUATION MULTIPLES ◀▶

- Our TP of Rs. 860 is basis 30x consol Sep19 EPS.** We factor in TMKN's strong growth prospects across segments and the acquisition of ABC/brownfield capacities enhancing its ability to actualise them. While the latter could cause RoCE's to dip marginally in FY18, expect a revival led by strong earnings growth. While ops. would continue to be WC intensive, expect ABC's unutilized capacities to help generate strong FCFs through FY20.

FINANCIAL SUMMARY

Year	Revenue (Rs. mn)	EBITDA (%)	PAT (Rs.mn)	EPS (Rs.)	P/E (x)	EV/ EBITDA (x)
FY17	10,562	15.0%	972	14.3	54.6	36.2
FY18E*	13,547	17.3%	1,446	20.6	37.8	24.3
FY19E*	18,578	18.0%	1,910	25.4	30.8	16.7

* Represent consolidated numbers of TMKN and ABC w.e.f 4QFY18

THREE YEAR OUTLOOK

BUSINESS & EARNINGS ◀▶

- Expect exports to continue to be a strong growth driver, with the Timken group directionally focused on ceasing operations in high cost countries, and increasing sourcing from TMKN.
- The acquisition of ABC bearings opens up the wheel-end bearings market both domestically (where ABC is a dominant player) and in exports (given TMKN's global presence).
- Importantly, ABC's acquisition also opens up the possibility of import substitution of industrial bearings for TMKN. This, coupled with the organic increase in the proportion of manufactured bearings with the commissioning of the brownfield capacities, would enable TMKN enjoy higher margins (Gross margin% on Traded and manufactured bearings are ~15% and ~45% respectively)
- We believe that new opportunities in railways would also drive revenue growth through FY21. These include, 1) DFC (including more DFCs on the anvil), 2) locomotives (India is poised to become the loco export hub for MENA and SAARC regions) 3) bearings re-manufacturing 4) conversion of Schlieren wagons to LHB wagons.
- Expect the latter to pick up pace beginning FY19E as the government has expressed its intent to speed up conversion to LHB wagons, particularly in the light of the spate of recent accidents/derailments
- Expect revenue and PAT CAGR of ~26% and ~34% through FY16-FY21E.

VALUATION MULTIPLES ◀▶

- Our multiples factor in the longer term growth opportunities for TMKN particularly in exports (TMKN's exports are still miniscule compared to the Timken group's size) and railways (DFCs + other drivers on the anvil)
- Expect TMKN to continue to maintain RoCE ratios at elevated levels over the longer term (beyond 2021 as well), aided by strong reinvestment opportunities in the business enabled by sustenance of strong demand

KEY ESTIMATES REVISION*

Rs. mn	FY18E			FY19E		
	Old	New	Change	Old	New	Change
Revenue	14,182	13,547	-4.5%	19,581	18,578	-5.1%
EBITDA	2,436	2,339	-4.0%	3,503	3,347	-4.5%
Margin (%)	17.2%	17.3%	9 bps	17.9%	18.0%	12 bps
PAT	1,415	1,446	2.2%	2,078	1,910	-8.1%
PAT (%)	10.0%	10.7%	70 bps	10.6%	10.3%	-33 bps
EPS	20.2	20.6	2.3%	27.6	25.4	-8.0%

OUTLOOK REVIEW 2QFY18 20 NOVEMBER 2017

Industry	AUTOMOBILE
CMP	Rs. 781
Target Price	Rs. 860
Key Stock Data	
Bloomberg	TMKN IN
Shares o/s	68mn
Market Cap	Rs. 53bn
52-wk High-Low	Rs. 820-514
3m ADV	Rs. 17mn
Index	BSE 500

	Mar'17	Jun'17	Sep'17
Promoters	75.0	75.0	75.0
Institutions	11.1	11.6	12.1
Public	13.9	13.4	12.9
Pledge	-	-	-

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Quarterly Financial Statement

TMKN's revenue growth in 2QFY18 (10% YoY) was constrained by the sale of traded bearings (~26% of revenue) being recorded net of indirect taxes post GST.

Gross margin improved ~140bps QoQ and came in at ~44%.

As % of revenue, employee costs and other expenses declined ~30bps QoQ and 150bps QoQ.

EBITDA margin came in at 17.3%, up 320bps QoQ

Other income came in at Rs.148mn, up 770% YoY. This is inclusive of refund of spl. duty on imported bearings

STANDALONE FINANCIAL RESULTS

Rs. mn\Period	2QFY18	2QFY17	yoy Growth	1QFY18	qoq Growth	1HFY17	1HFY18	yoy Growth
Revenue	3,102	2,822	9.9%	2,999	3.4%	5,648	6,101	8.0%
Raw Material	1,737	1,628	6.7%	1,721	0.9%	3,272	3,458	5.7%
Employee cost	214	189	13.4%	216	-0.8%	372	431	15.8%
Other cost	613	514	19.2%	638	-4.0%	1,037	1,251	20.6%
Total Expenditure	2,564	2,331	10.0%	2,575	-0.4%	4,682	5,139	9.8%
EBITDA	538	491	9.6%	424	26.9%	966	961	-0.5%
<i>Margin %</i>	17.3%	17.4%	-5 bps	14.1%	321 bps	17.1%	15.8%	-135 bps
D&A	116	70	66.4%	112	4.1%	140	228	63.2%
EBIT	421	421	0.2%	312	35.1%	826	733	-11.2%
Other income	148	17	787.4%	20	637.3%	34	168	399.4%
Net Interest exp (inc)	4	2	52.2%	2	52.2%	4	6	48.7%
PBT	566	435	30.1%	330	71.6%	856	896	4.6%
Tax provision	194	152	27.7%	111	75.0%	274	304	11.0%
Tax rate %	34.2%	34.8%	-64 bps	33.5%	66 bps	32.0%	34.0%	195 bps
PAT (Reported)	373	284	31.4%	219	69.9%	582	592	1.6%
<i>Adjusted PAT Margin %</i>	12.0%	10.0%	196 bps	7.3%	470 bps	10.3%	9.7%	-61 bps
Shares Outstanding	68	68		68		68	68	
EPS (Reported)	5.5	4.2	31.4%	3.2	69.9%	8.6	8.7	1.6%

Financial Summary

Abridged Financial Statements								
Rs. mn	FY13	FY14	FY15	FY16	FY17	FY18E*	FY19E*	FY20E*
Profit & Loss								
Revenue	6,885	7,201	9,290	10,508	10,562	13,547	18,578	21,921
Gross profit	2,711	2,745	3,761	4,194	4,322	5,867	8,141	9,817
EBITDA	735	716	1,337	1,622	1,580	2,339	3,347	4,111
Depreciation	139	158	168	225	289	494	614	663
EBIT	596	558	1,169	1,398	1,291	1,845	2,732	3,448
Other Income	55	108	59	58	99	368	184	203
Interest expense	13	9	6	9	8	23	33	21
Exceptional items	0	0	0	30	0	0	0	0
PBT	637	657	1,223	1,416	1,382	2,191	2,884	3,630
Reported PAT (after minority interest)	442	447	807	918	972	1,446	1,910	2,404
Adj PAT	442	447	807	918	972	1,446	1,910	2,404
EPS (Rs.)	6.9	6.6	11.9	13.5	14.3	20.6	25.4	32.0
Balance Sheet								
Net Worth	3,415	3,823	4,384	5,300	6,178	10,459	12,097	14,139
Deferred Tax	0	0	0	0	0	173	173	173
Total debt	0	32	25	43	84	342	84	84
Other liabilities and provisions	558	411	585	557	977	1,330	1,758	1,742
Total Networth and liabilities	3,973	4,267	4,994	5,901	7,240	12,304	14,112	16,137
Gross Fixed assets	2,516	2,807	3,057	3,585	4,809	8,595	9,295	10,095
Net fixed assets	792	965	1,069	1,372	2,306	4,077	4,017	3,993
Capital work-in-progress	257	256	268	211	581	612	612	612
Goodwill	0	0	0	0	0	1,917	1,917	1,917
Investments	319	233	167	384	906	1,306	2,000	1,979
Cash and bank balances	140	201	237	334	184	304	210	678
Loans & advances and other assets	382	443	657	899	910	1,013	1,013	1,013
Net working capital	2,039	2,123	2,557	2,667	2,321	3,345	4,590	5,989
Total assets	3,973	4,267	4,994	5,901	7,240	12,304	14,112	16,137
Capital Employed	3,415	3,856	4,410	5,343	6,262	10,974	12,353	14,395
Invested Capital (CE - cash - CWIP)	3,017	3,398	3,904	4,799	5,497	10,057	11,531	13,105
Net debt	-459	-403	-379	-675	-1,005	-1,268	-2,127	-2,574
Cash Flows								
Cash flows from Operations (Pre-tax)	311	697	886	969	2,038	2,244	2,599	3,123
Cash flows from Operations (post-tax)	131	457	447	1,014	1,642	1,500	1,625	1,898
Capex	302	307	264	665	1,310	788	700	800
Free cashflows	-170	150	183	349	332	712	925	1,098
Free cashflows (post interest costs)	-183	141	177	340	324	689	892	1,077
Cash flows from Investing	-170	-300	-256	-669	-1,251	-1,188	-1,395	-779
Cash flows from Financing	-158	-159	-257	13	-47	176	-439	-272
Total cash & liquid investments	140	201	237	334	184	304	210	678

* Represent consolidated numbers of TMKN and ABC w.e.f 4QFY18

Financial Summary

	FY13	FY14	FY15	FY16	FY17	FY18E*	FY19E*	FY20E*
Growth ratios								
Revenue	-17.1%	4.6%	29.0%	13.1%	0.5%	28.3%	37.1%	18.0%
EBITDA	-30.9%	-2.6%	86.8%	21.3%	-2.6%	48.0%	43.1%	22.8%
Adj PAT	-45.1%	1.2%	80.3%	13.8%	5.9%	48.8%	32.0%	25.9%
Margin ratios								
Gross	39.4%	38.1%	40.5%	39.9%	40.9%	43.3%	43.8%	44.8%
EBITDA	10.7%	9.9%	14.4%	15.4%	15.0%	17.3%	18.0%	18.8%
Adj PAT	6.4%	6.2%	8.7%	8.7%	9.2%	10.7%	10.3%	11.0%
Performance ratios								
Pre-tax OCF/EBITDA	42.3%	97.3%	66.2%	59.7%	129.0%	96.0%	77.7%	76.0%
OCF/IC (%)	4.4%	13.4%	11.4%	21.1%	29.9%	14.9%	14.1%	14.5%
RoE (%)	13.5%	12.4%	19.7%	19.0%	16.9%	17.4%	16.9%	18.3%
RoCE (%)	13.5%	12.5%	19.6%	19.3%	16.9%	14.1%	15.5%	17.2%
RoCE (Pre-tax)	19.4%	18.3%	29.7%	29.9%	24.0%	25.7%	25.0%	27.3%
RoIC (Pre-tax)	19.6%	17.4%	32.0%	32.1%	25.1%	23.7%	25.3%	28.0%
Fixed asset turnover (x)	2.8	2.7	3.2	3.2	2.5	2.0	2.1	2.3
Total asset turnover (x)	1.8	1.7	2.0	1.9	1.6	1.4	1.4	1.4
Financial stability ratios								
Net Debt to Equity (x)	(0.1)	(0.1)	(0.1)	(0.1)	(0.2)	(0.1)	(0.2)	(0.2)
Net Debt to EBITDA (x)	(0.6)	(0.6)	(0.3)	(0.4)	(0.6)	(0.5)	(0.6)	(0.6)
Interest cover (x)	10.2	51.4	77.7	110.4	196.2	65.8	49.5	92.6
Cash conversion days	108	108	100	93	80	90	90	100
Working capital days	99	109	103	105	78	82	76	88
Valuation metrics								
Fully Diluted Shares (mn)	63.7	68.0	68.0	68.0	68.0	75.2	75.2	75.2
Market cap (Rs.mn)	49,765	53,100	53,100	53,100	53,100	58,738	58,738	58,738
P/E (x)	112.5	118.7	65.8	57.8	54.6	37.8	30.8	24.4
P/OCF(x)	447	129	132	58	36	39	36	31
EV (Rs.mn) (ex-CWIP)	58,022	58,080	58,091	57,853	57,151	56,858	55,999	55,552
EV/ EBITDA (x)	79.0	81.2	43.4	35.7	36.2	24.3	16.7	13.5
EV/ OCF(x)	441.7	127.1	130.1	57.0	34.8	37.9	34.5	29.3
FCF Yield	-0.3%	0.3%	0.3%	0.7%	0.6%	1.2%	1.6%	1.9%
Price to BV (x)	17.2	15.4	13.4	11.1	9.5	5.6	4.9	4.2
Dividend pay-out (%)	30.7%	98.8%	25.3%	7.4%	7.0%	9.7%	12.3%	12.5%
Dividend yield (%)						0.3%	0.4%	0.5%

* Represent consolidated numbers of TMKN and ABC w.e.f 4QFY18

Crystal Ball Gazing

Expect revenue and PAT CAGR of ~25% and ~38% through FY17-FY21E. Growth drivers continue to be robust across segments, particularly in exports. Increase in utilisation levels of recent brownfield expansion and the amalgamation of ABC would enable steady improvement in margins.

Expect revenue and PAT CAGR of 25% and 38% respectively, through FY17-FY21E



Increase in utilisation levels of recent brownfield expansion and the amalgamation of ABC would enable steady improvement in margins.



Expect TMKN to trade at elevated multiples given strong its strong growth prospects and sustenance of margins at elevated levels.

Standalone	CY09-CY10	CY10-FY14	FY14-FY17	FY18-FY21E
Revenue CAGR	47%	15%	14%	24%
Gross Margin	49%	42%	40%	45%
EBITDA CAGR	66%	0%	30%	33%
EBITDA margin	14%	12%	14%	19%
EPS CAGR	57%	-4%	30%	35%
Total Asset Turnover (x)	1.1	1.7	1.8	1.4
Total WC days	89	89	99	83
Pre-tax OCF/EBITDA (%)	129%	73%	88%	85%
Post Tax OCF as a % of IC	15%	10%	19%	18%
Debt/EBITDA	(0.1)	(0.3)	(0.5)	(0.6)

Standalone	CY09-CY10	CY10-FY14	FY14-FY17	FY18-FY21E
RoE (%)	12.4%	15.9%	17.0%	18.8%
RoCE (%)	12.7%	16.0%	17.1%	17.1%
RoIC (%)	14.3%	20.3%	26.7%	28.4%
Average 1 yr fwd				
PE (x)	n/a	n/a	n/a	n/a
EV/EBITDA (x)	n/a	n/a	n/a	n/a
Peak 1 yr fwd				
PE (x)	n/a	n/a	n/a	n/a
EV/EBITDA (x)	n/a	n/a	n/a	n/a

P/E multiple	FY21E EPS (mn)	Price target
30	46.9	1,410

Entry = Rs. 781@ 30.8x
FY19E EPS



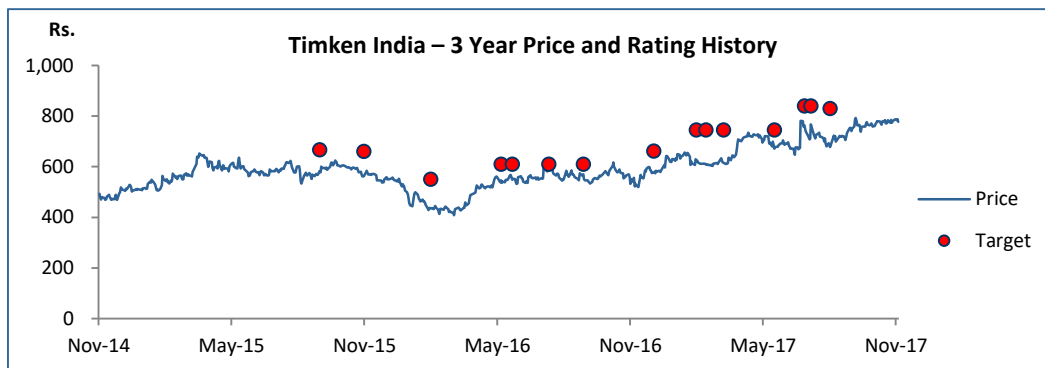
Cumulative Dividends of
Rs.9



PAT CAGR of ~38%, exit
multiple of 30x on FY21E
EPS



Spark Recommendation History



Absolute Rating Interpretation

BUY	Stock expected to provide positive returns of >15% over a 1-year horizon
ADD	Stock expected to provide positive returns of >5% – <15% over a 1-year horizon
REDUCE	Stock expected to provide returns of <5% – -10% over a 1-year horizon
SELL	Stock expected to fall >10% over a 1-year horizon

Symbol Interpretation

◀▶ No Change | ▼ Downgrade | ▲ Upgrade

Report Date	Price	Target	Reco.
11/Aug/17	683	830	Buy
19/Jul/17	710	840	Buy
10/Jul/17	759	840	Buy
30/May/17	692	745	Buy
22/Mar/17	623	745	BUY
23/Feb/17	609	745	Buy
13/Feb/17	630	745	Buy
15/Dec/16	575	661	Buy
09/Sep/16	567	610	Buy
27/Jul/16	588	610	Buy
07/Jun/16	550	610	Buy
23/May/16	532	610	Buy
17/Feb/16	440	550	Buy
18/Nov/15	561	660	Buy
16/Sep/15	564	666	Buy

Disclosure of Interest Statement

Analyst financial interest in the company	No
Group/directors ownership of the subject company covered	No
Investment banking relationship with the company covered	No
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