

1 August 2019

## Apollo Tyres

*Strong replacement-business growth; maintaining a Buy*

Rating: **Buy**

Target Price: ₹255

Share Price: ₹155

We continue to expect strong growth in the domestic replacement market across categories and in the European business. The pass-through of raw-material cost shows the underlying strength in the replacement market. We maintain our Buy call, at a revised TP of ₹255 (earlier ₹258).

**India business growth to continue, albeit slower.** Replacement volume grew 12% y/y in Q1 FY20, driven by 25% growth in TBR replacements, over 10% in PCR replacements and 30% in two-wheeler growth. However, in the next two years, we expect increase in competitive intensity in the TBR business from MRF.

The earlier plan of phase-1 production (of 3,000tpd of TBRs and 15,000tpd in PCRs in Andhra) has been halved; thus only 1,500tpd and 7,500tpd respectively are expected to be commissioned in Q4 FY20 and scaled up in FY21.

**European business to grow strong.** The company expects 13% volume growth to 7.5m units driven by deeper penetration. We expect the Europe EBIT to be positive at end-FY20. From the current 8.5% Europe manufacturing margin, we expect the margin to increase in FY20 with continued favourable product-mix and strong growth

**Q1 FY20 takeaways.** 1) IND AS 116 impact is ₹330m and the impact on depreciation is ₹260m. 2) One-time exceptional item of ₹330m toward donation. 3) TBR capacity utilisation in India is 90%, and PCR at 80%. 4) Europe PCR utilisation at 70% and TBR less than 50%. 5) Price increase of 1-1.5% from August across product categories in the domestic market

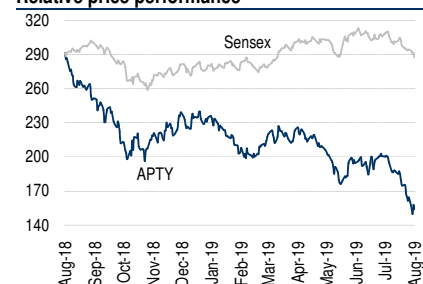
**Valuation.** We expect revenue to clock a 12% CAGR over FY19-21, and earnings 13% to ₹11.23bn, leading to an EPS of ₹19.6. We maintain our Buy rating, at a price of ₹255 (13x FY21e EPS), earlier ₹258. **Risks:** 1) Lower volume growth in India and Europe. 2) Higher RM costs.

Key data	APTY IN / APLO.BO
52-week high/low	₹300 / 145
Sensex/Nifty	36980 / 10970
3-m average volume	\$9.8m
Market cap	₹88bn / \$1275.5m
Shares outstanding	572m

Shareholding pattern (%)	Jun'19	Mar'19	Dec'18
Promoters	40.9	40.9	40.8
- of which, Pledged	15.0	15.1	12.7
Free float	59.1	59.1	59.2
- Foreign institutions	23.7	19.4	20.0
- Domestic institutions	15.5	21.9	22.6
- Public	19.9	17.9	16.6

Estimates revision (%)	FY20	FY21
Sales	-1.1	-0.4
EBITDA	0.2	0.9
EPS	-2.1	-1.0

### Relative price performance



Source: Bloomberg

Key financials (YE Mar)	FY17	FY18	FY19	FY20e	FY21e
Sales (₹m)	1,31,800	1,48,405	1,75,374	2,03,675	2,21,076
Net profit (₹m)	10,990	7,239	8,797	10,616	11,231
EPS (₹)	21.6	12.7	15.4	18.6	19.6
PE (x)	9.7	21.8	10.0	8.3	7.9
EV / EBITDA (x)	7.2	11.2	6.8	5.8	5.3
PBV (x)	1.5	1.6	0.9	0.8	0.7
RoE (%)	15.8	8.5	6.9	10.0	9.6
RoCE (%)	12.0	6.3	6.3	7.3	7.1
Dividend yield (%)	3.1	3.8	2.1	1.6	1.7
Net debt / equity (x)	0.4	0.3	0.4	0.5	0.4

Source: Company, Anand Rathi Research

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## Quick Glance – Financials and Valuations

**Fig 1 – Income statement (₹m)**

Year-end: Mar	FY17	FY18	FY19	FY20e	FY21e
Net revenues	1,31,800	1,48,405	1,75,374	2,03,675	2,21,076
Growth (%)	11.2	12.6	18.2	16.1	8.5
Direct costs	68,901	83,955	1,01,022	1,17,113	1,27,119
SG&A	44,412	47,937	54,880	62,414	67,746
<b>EBITDA</b>	<b>18,487</b>	<b>16,513</b>	<b>19,472</b>	<b>24,148</b>	<b>26,211</b>
EBITDA margins (%)	14.0	11.1	11.1	11.9	11.9
- Depreciation	4,618	5,926	8,127	9,622	10,749
Other income	1,518	1,165	1,345	1,345	1,345
Interest expenses	1,029	1,629	1,811	2,003	2,135
Extraordinary items	-	-	-2,000	-	-
PBT	14,359	10,123	8,880	13,869	14,673
Effective tax rate (%)	23	28	23	23	23
+ Associates / (Minorities)					
Net income	10,990	7,239	6,797	10,616	11,231
Adjusted income	10,990	7,239	8,797	10,616	11,231
WANS	509	572	572	572	572
FDEPS (₹ / sh)	21.6	12.7	15.4	18.6	19.6

**Fig 2 – Balance sheet (₹ m)**

Year-end: Mar	FY17	FY18	FY19	FY20e	FY21e
Share capital	509	572	572	572	572
Net worth	72,900	97,767	1,00,398	1,12,266	1,22,015
Debt	34,366	46,611	49,304	56,804	56,304
Minority interest	-	-	-	-	-
DTL/(Assets)	7,032	7,433	7,707	7,707	7,707
<b>Capital employed</b>	<b>1,14,297</b>	<b>1,51,811</b>	<b>1,57,409</b>	<b>1,76,777</b>	<b>1,86,026</b>
Net tangible assets	60,382	95,287	1,08,839	1,28,217	1,34,468
Net intangible assets	4,760	6,683	6,708	7,042	7,042
Goodwill	1,774	2,061	1,993	1,993	1,993
CWIP (tang. &intang.)	29,151	23,041	15,393	11,201	9,201
Investments (strategic)					
Investments (financial)	3,962	13,425	60	60	60
Current assets (ex cash)	48,978	54,088	61,292	66,646	71,067
Cash	3,369	5,992	5,627	4,716	5,421
Current liabilities	38,079	48,766	42,503	43,098	43,226
Working capital	10,900	5,323	18,789	23,549	27,841
<b>Capital deployed</b>	<b>1,14,297</b>	<b>1,51,811</b>	<b>1,57,409</b>	<b>1,76,777</b>	<b>1,86,026</b>

**Fig 3 – Cash-flow statement (₹m)**

Year-end: Mar	FY17	FY18	FY19	FY20e	FY21e
PBT	13,869	10,587	9,345	14,526	15,463
+ Non-cash items	4,618	5,926	8,127	9,622	10,749
Oper. prof. before WC	15,608	13,164	14,924	20,237	21,980
- Incr./decr.) in WC	-3,949	-5,577	13,467	4,759	4,292
Others incl. taxes	2,764	2,389	2,083	3,253	3,442
Operating cash-flow	19,672	19,701	1,923	16,136	18,477
- Capex (tang. + intang.)	38,612	36,931	13,988	25,141	15,000
Free cash-flow	-18,939	-17,230	-12,066	-9,005	3,477
Acquisitions	-	-	-	-	-
- Div.(incl. buyback& taxes)	2,456	3,342	1,859	1,401	1,483
+ Equity raised		15,006	-	-	-
+ Debt raised	18,899	12,246	2,693	7,500	-500
- Fin investments	-1,098	9,463	-13,365	-	-
- Misc. (CFI + CFF)	1,174	(5,406)	2,498	(1,996)	790
Net cash-flow	-2,573	2,623	-365	-911	705

Source: Company, AnandRathi Research

**Fig 4 – Ratio analysis**

Year-end: Mar	FY17	FY18	FY19	FY20e	FY21e
P/E (x)	9.7	21.8	10.0	8.3	7.9
EV / EBITDA (x)	7.2	11.2	6.8	5.8	5.3
EV / Sales (x)	1.0	1.2	0.8	0.7	0.6
P/B (x)	1.5	1.6	0.9	0.8	0.7
RoE (%)	15.8	8.5	6.9	10.0	9.6
RoCE (%) - after tax	12.0	6.3	6.3	7.3	7.1
RoIC (%) - after tax	12.6	6.6	6.5	7.6	7.3
DPS (₹ / sh)	4.8	5.8	3.3	2.4	2.6
Dividend yield (%)	3.1	3.8	2.1	1.6	1.7
Dividend payout (%) - incl. DDT	22.3	46.2	27.4	13.2	13.2
Net debt / equity (x)	0.4	0.3	0.4	0.5	0.4
Receivables (days)	31	35	24	22	22
Inventory (days)	140	128	126	123	123
Payables (days)	78	89	72	75	75
CFO :PAT%	179.0	272.1	21.9	152.0	164.5

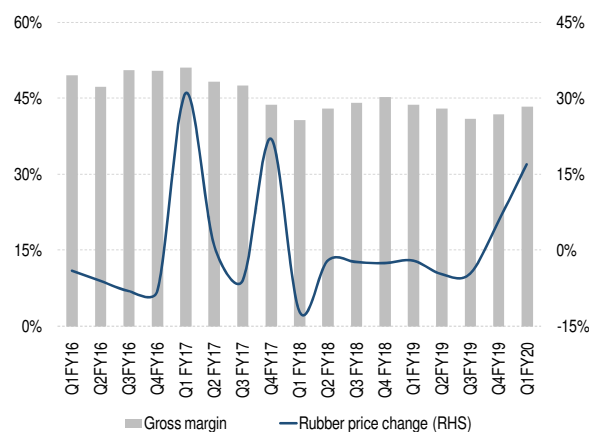
Source: Company, AnandRathi Research

**Fig 5 – Price movement**



Source: Bloomberg

**Fig 6 – Rubber-price change vs gross margin**



Source: Company

## Result highlights

Fig 7 – Quarterly performance

(₹m)	Q2 FY17	Q3 FY17	Q4 FY17	Q1 FY18	Q2 FY18	Q3 FY18	Q4 FY18	Q1 FY19	Q2 FY19	Q3 FY19	Q4 FY19	Q1 FY20
<b>Net Sales/Income from oper.</b>	<b>30,849</b>	<b>34,579</b>	<b>33,256</b>	<b>32,825</b>	<b>34,767</b>	<b>40,501</b>	<b>40,313</b>	<b>42,880</b>	<b>42,574</b>	<b>47,183</b>	<b>42,737</b>	<b>43,313</b>
Y/Y (%)	2.4	17.3	11.2	(0.9)	12.7	17.1	21.2	30.6	22.5	16.5	6.0	1.0
Q/Q (%)	(6.8)	12.1	(3.8)	(1.3)	5.9	16.5	(0.5)	6.4	(0.7)	10.8	(9.4)	1.3
(Incr.) / Decr. in stockand WIP	(317)	(247)	(827)	(1,594)	(251)	611	(240)	(1,758)	(2,769)	(1,167)	991	(1,226)
Consumption of R.M & Comp.	16,232	18,356	19,519	21,067	20,078	21,992	22,292	25,846	27,001	29,020	23,859	25,750
% of sales	51.6	52.4	56.2	59.3	57.0	55.8	54.7	56.2	56.9	59.0	58.1	56.6
Y/Y (%)	0.2	24.4	26.4	20.3	24.6	24.8	18.0	23.7	22.2	23.2	12.7	1.8
Q/Q (%)	(1.7)	13.8	3.2	4.2	1.8	14.0	(2.4)	9.2	0.6	14.9	(10.8)	(1.3)
Gross margins (%)	48.4	47.6	43.8	40.7	43.0	44.2	45.3	43.8	43.1	41.0	41.9	43.4
<b>Staff cost</b>	<b>4,543</b>	<b>4,506</b>	<b>4,134</b>	<b>4,517</b>	<b>4,903</b>	<b>5,302</b>	<b>6,036</b>	<b>6,067</b>	<b>6,072</b>	<b>6,485</b>	<b>6,181</b>	<b>6,418</b>
% of sales	14.7	13.0	12.4	13.8	14.1	13.1	15.0	14.1	14.3	13.7	14.5	14.8
Y/Y (%)	14.4	13.6	-4.4	0.6	7.9	17.7	46.01	34.3	23.8	22.3	2.4	5.8
Q/Q (%)	1.2	-0.8	-8.3	9.3	8.5	8.1	13.8%	0.5	0.1	6.80	-4.69	3.8
<b>Other expenditure</b>	<b>6,004</b>	<b>6,971</b>	<b>6,732</b>	<b>6,082</b>	<b>6,392</b>	<b>7,632</b>	<b>7,073</b>	<b>7,445</b>	<b>7,598</b>	<b>7,573</b>	<b>7,460</b>	<b>7,621</b>
% of sales	19.5	20.2	20.2	18.5	18.4	18.8	17.5	17.4	17.8	16.0	17.5	17.6
Y/Y (%)	10.7	18.1	11.2	-13.8	6.5	9.5	5.1	22.4	18.9	-0.8	5.5	2.4
Q/Q (%)	-14.9	16.1	12.1	-9.7	5.1	19.4	-7.3	5.3	2.1	-0.3	-1.5	2.2
<b>Total expenditure</b>	<b>26,462</b>	<b>29,586</b>	<b>29,557</b>	<b>30,072</b>	<b>31,123</b>	<b>35,537</b>	<b>35,160</b>	<b>37,599</b>	<b>37,902</b>	<b>41,910</b>	<b>38,491</b>	<b>38,564</b>
<b>Operating profit</b>	<b>4,387</b>	<b>4,993</b>	<b>3,699</b>	<b>2,753</b>	<b>3,644</b>	<b>4,964</b>	<b>5,153</b>	<b>5,281</b>	<b>4,672</b>	<b>5,273</b>	<b>4,246</b>	<b>4,749</b>
Y/Y (%)	(9.8)	(1.2)	(21.8)	(48.9)	(16.9)	(0.6)	39.3	91.8	28.2	6.2	(17.6)	(10.1)
Q/Q (%)	(18.6)	13.8	(25.9)	(25.6)	32.4	36.2	3.8	2.5	(11.5)	12.8	(19.5)	11.8
OPM (%)	14.2	14.4	11.1	8.4	10.5	12.3	12.8	12.3	11.0	11.2	9.9	11.0
Other income	387	373	500	67	197	464	437	406	123	332	485	275
Interest	228	283	248	340	402	410	476	430	461	485	434	584
Depreciation	1,058	1,135	1,366	1,258	1,385	1,514	1,768	1,841	1,962	2,011	2,314	2,673
<b>Profit before except items &amp; tax</b>	<b>3,488</b>	<b>3,948</b>	<b>2,585</b>	<b>1,221</b>	<b>2,054</b>	<b>3,503</b>	<b>3,346</b>	<b>3,416</b>	<b>2,372</b>	<b>3,108</b>	<b>1,984</b>	<b>1,767</b>
<b>Profit before tax</b>	<b>3,486</b>	<b>3,948</b>	<b>2,585</b>	<b>1,221</b>	<b>2,054</b>	<b>3,503</b>	<b>3,346</b>	<b>3,416</b>	<b>1,972</b>	<b>2,509</b>	<b>984</b>	<b>1,767</b>
Less: Provision for taxation	891	990	303	338	652	1,050	844	898	512	529	144	351
<b>Tax rate</b>	<b>25.6</b>	<b>25.1</b>	<b>11.7</b>	<b>27.7</b>	<b>31.8</b>	<b>30.0</b>	<b>25.2</b>	<b>26.3</b>	<b>26.0</b>	<b>21.1</b>	<b>14.6</b>	<b>19.9</b>
<b>Profit after tax</b>	<b>2,595</b>	<b>2,958</b>	<b>2,282</b>	<b>883</b>	<b>1,402</b>	<b>2,453</b>	<b>2,502</b>	<b>2,518</b>	<b>1,460</b>	<b>1,980</b>	<b>840</b>	<b>1,415.6</b>
Y/Y (%)	(7.6)	6.2	(8.7)	(72.0)	(46.0)	(17.1)	9.6	185.2	4.2	(19.3)	(66.4)	(43.8)
Q/Q (%)	(17.8)	14.0	(22.8)	(61.3)	58.8	75.0	2.0	0.6	(42.0)	35.5	(57.6)	68.5
EPS(₹)	5.1	5.8	4.5	1.7	2.8	4.3	4.4	4.4	2.6	3.5	1.5	2.5
Adjusted EPS (₹)	5.1	5.8	4.5	1.7	2.8	4.3	4.4	4.4	3.3	4.5	3.2	2.5

Source: Company

## Valuations

We expect revenue to clock a 12% CAGR over FY19-21, and earnings 13% to ₹11.23bn, leading to an EPS of ₹19.7. We maintain our Buy rating, at a price of ₹255 (13x FY21e EPS), earlier ₹258.

**Fig 8 – Change in estimates**

(₹m)	Old estimates		Revised Estimates		Change	
	FY20	FY21	FY20	FY21	FY20	FY21
Revenue	2,05,986	2,21,940	2,03,675	2,21,076	-1.1%	-0.4%
EBITDA	24,100	25,967	24,148	26,211	0.2%	0.9%
Adj. PAT	10,844	11,350	10,616	11,231	-2.1%	-1.0%
EPS (₹)	19	20	19	20	-2.1%	-1.0%

Source: Anand Rathi Research

**Fig 9 –Standard deviation of PE Band**



Source: Bloomberg, Anand Rathi Research

### Risks

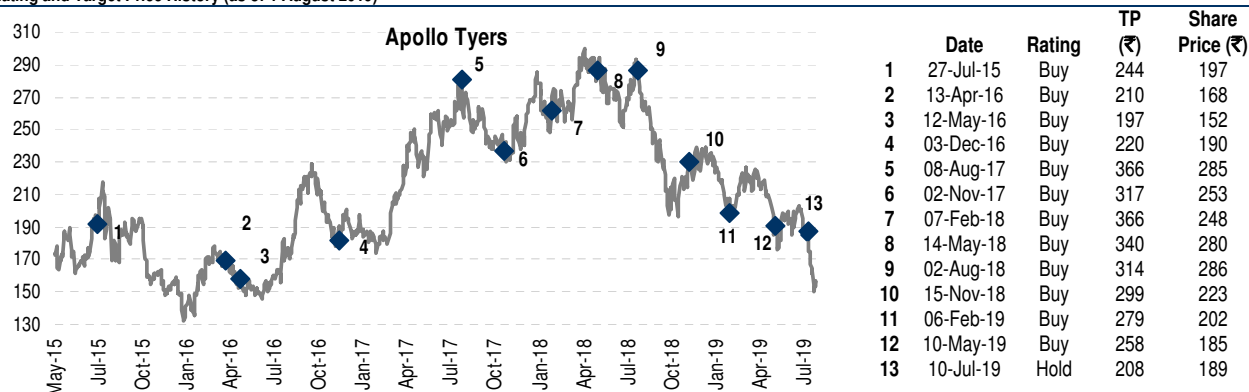
- Lowering of prices in the event of stable RM costs and lower volume growth.
- Higher rubber costs.

## Appendix

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