

SELL

TP: Rs 160 | ▼ 8%

APOLLO TYRES

| Auto Components

| 24 November 2020

Positives priced in; downgrade to SELL

Apollo Tyres (APTY) delivered a Q2FY21 beat and has rallied 40% in the last three months due to domestic volume visibility, a better Europe performance and steady margin outlook. In our view, these positives are priced in even as rising prices of natural rubber (up ~30% over the last three months) and crude derivatives are likely to squeeze margins despite stronger volumes. We find current valuations at 17.4x Sep'22E EPS rich despite our earnings upgrade post Q2 and cut the stock to SELL from ADD. Our Sep'21 TP stays at Rs 160.

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Strong volume growth and steady margins already factored in: We build in volume growth of 13% each in MHCV, LCV & 2W/3W tyres and 16% in PV tyres over FY21-FY23. The spike in natural rubber prices from Rs 120/kg to Rs 155/kg over the last three months is broadly in line with our expectations, though any further price increase is likely to have an adverse impact on margins. We expect India operations to clock a revenue CAGR of 16% and forecast steady overall EBITDA margins at ~13% and an earnings CAGR of 26% for APTY through to FY23.

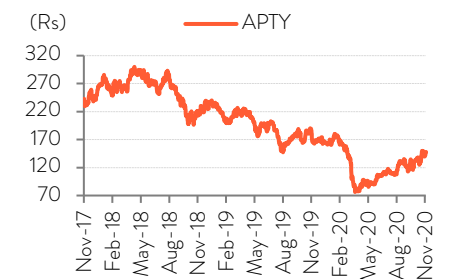
Leverage, return ratio outlook healthy: APTY's product profile spanning MHCV, LCV and PV tyres, strong branding and high exposure to the domestic replacement market makes for a healthy growth outlook. With lower borrowings than earlier planned, we expect net debt/equity to remain steady at 0.5x. We also pencil in 100-150bps improvement in ROE and ROCE over FY21-FY23.

Valuations full, downgrade to SELL: The stock has rallied 40% during the last three months and is now trading at 17.4x Sep'22E EPS. In our view, most optimism over volumes, margins and Europe sales is in the price. We maintain our TP at 16x Sep'22E EPS but downgrade the stock to SELL (from ADD) on expensive valuations.

Ticker/Price	APTY IN/Rs 174
Market cap	US\$ 1.3bn
Shares o/s	572mn
3M ADV	US\$ 14.7mn
52wk high/low	Rs 182/Rs 73
Promoter/FPI/DII	41%/23%/17%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue (Rs mn)	175,488	163,270	162,817	188,673	206,034
EBITDA (Rs mn)	17,762	19,155	21,988	24,755	27,090
Adj. net profit (Rs mn)	6,798	4,764	4,364	5,922	6,914
Adj. EPS (Rs)	15.4	8.3	7.6	9.3	10.9
Adj. EPS growth (%)	(6.1)	(29.9)	(8.4)	22.2	16.7
Adj. ROAE (%)	6.8	4.8	3.8	5.0	5.5
Adj. P/E (x)	11.3	20.9	22.8	18.7	16.0
EV/EBITDA (x)	7.6	7.4	6.8	6.3	5.6

Source: Company, BOBCAPS Research

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FIG 1 – Q2FY21 QUARTERLY PERFORMANCE – CONSOLIDATED

(Rs mn)	Q2FY21	Q2FY20	YoY (%)	Q1FY21	QoQ (%)	H1FY21	H1FY20	YoY (%)
Net Revenues	42,827	39,858	7.4	28,734	49.0	71,561	83,171	(14.0)
Total Income (A)	42,827	39,858	7.4	28,734	49.0	71,561	83,171	(14.0)
Operating Expenses:								
Raw materials consumed	23,014	22,442	2.5	16,308	41.1	39,321	46,967	(16.3)
Employee Expenses	6,233	5,943	4.9	5,370	16.1	11,603	12,361	(6.1)
Other Expenses	6,632	7,154	(7.3)	4,684	41.6	11,316	14,775	(23.4)
Total Expenditure (B)	35,879	35,538	1.0	26,362	36.1	62,241	74,102	(16.0)
EBITDA (A-B)	6,948	4,320	60.8	2,373	192.8	9,320	9,069	2.8
Other Income	384	40	859.9	268	43.2	653	315	107.5
Depreciation	3,308	2,742	20.7	3,091	7.0	6,400	5,415	18.2
EBIT	4,024	1,618	148.6	(450)	NA	3,574	3,969	(10.0)
Finance Costs	1,167	640	82.4	1,172	(0.4)	2,339	1,223	91.2
PBT before excep items	2,857	979	191.9	(1,622)	NA	1,235	2,746	(55.0)
Exceptional loss/ (profit)	59	-	NA	-	NA	59	-	NA
PBT after excep items	2,797	979	185.9	(1,622)	NA	1,176	2,746	(57.2)
Tax expense	798	148	438.9	(276)	NA	522	500	4.4
Reported PAT	1,999	831	140.7	(1,346)	NA	654	2,246	(70.9)
Adjusted PAT	2,059	831	147.9	(1,346)	NA	713	2,246	(68.2)
Adj EPS (Rs)	3.5	1.5	140.7	(2.4)	NA	1.1	3.9	(70.9)

Source: Company, BOBCAPS Research

FIG 2 – KEY PARAMETERS – CONSOLIDATED

(%)	Q2FY21	Q2FY20	YoY (bps)	Q1FY21	QoQ (bps)	H1FY21	H1FY20	YoY (bps)
Gross Margin	46.3	43.7	257	43	302	45.1	43.5	152
EBITDA Margin	16.2	10.8	538	8	796	13.0	10.9	212
EBIT Margin	9.4	4.1	534	(2)	1,096	5.0	4.8	22
PBT Margin	6.7	2.5	422	(6)	1,231	1.7	3.3	(158)
Tax Rate	28.5	15.1	1,339	NA	NA	44.4	18.2	2,619
Adj PAT Margin	4.8	2.1	272	(5)	949	1.0	2.7	(170)

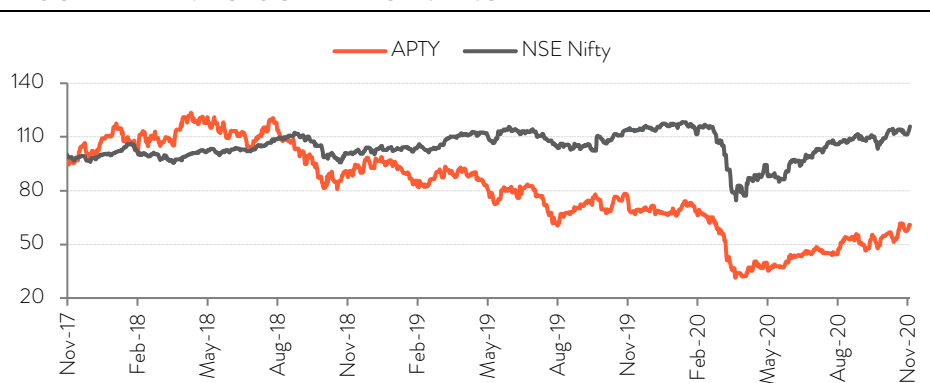
Source: Company, BOBCAPS Research

Valuation methodology

We expect APTY’s India revenue to register a 16% CAGR over FY21-FY23 and its European subsidiary to grow at 12%. Overall, we project a revenue/EBITDA/PAT CAGR of 13%/11%/26% for the company, with operating margins sustaining at ~13% levels.

Based on the strong domestic volume visibility, a better European performance and steady margin outlook, the stock has rallied 40% during the last three months and is now trading at 17.4x Sep’22E EPS. In our view, most optimism is in the price. We maintain our TP at 16x Sep’22E EPS but downgrade the stock to SELL (from ADD) on expensive valuations.

FIG 3 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

- Above-expected volume growth can improve profitability and enhance operating performance.
- A meaningful decline in rubber and crude oil prices can support operating margins and impact our profitability estimates.

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue	175,488	163,270	162,817	188,673	206,034
EBITDA	17,762	19,155	21,988	24,755	27,090
Depreciation	8,127	11,381	13,177	14,321	15,465
EBIT	10,868	8,243	10,011	11,783	13,125
Net interest income/(expenses)	(1,986)	(2,808)	(4,416)	(4,191)	(4,261)
Other income/(expenses)	1,232	469	1,200	1,350	1,500
Exceptional items	2,000	0	0	0	0
EBT	10,881	5,434	5,595	7,592	8,864
Income taxes	2,083	670	1,231	1,670	1,950
Extraordinary items	0	0	0	0	0
Min. int./Inc. from associates	0	0	0	0	0
Reported net profit	8,798	4,764	4,364	5,922	6,914
Adjustments	(2,000)	0	0	0	0
Adjusted net profit	6,798	4,764	4,364	5,922	6,914

Balance Sheet

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Accounts payables	22,102	23,090	23,071	29,056	27,197
Other current liabilities	8,960	16,980	13,544	20,120	17,539
Provisions	3,466	4,421	4,991	5,609	5,808
Debt funds	49,304	65,799	60,373	59,373	62,373
Other liabilities	7,975	15,433	15,433	15,433	15,433
Equity capital	572	572	572	635	635
Reserves & surplus	99,826	98,728	113,630	118,719	124,734
Shareholders' fund	100,398	99,300	114,202	119,354	125,369
Total liabilities and equities	192,206	225,023	231,614	248,944	253,718
Cash and cash eq.	5,627	7,496	6,519	6,711	5,015
Accounts receivables	11,547	9,399	12,211	13,207	13,392
Inventories	34,841	32,069	32,563	37,735	39,147
Other current assets	5,275	8,282	8,141	9,434	9,272
Investments	60	194	194	194	194
Net fixed assets	117,540	154,484	161,307	170,985	175,520
CWIP	15,393	16,420	14,000	14,000	14,500
Intangible assets	0	0	0	0	0
Deferred tax assets, net	(7,707)	(7,032)	(7,032)	(7,032)	(7,032)
Other assets	9,630	3,711	3,711	3,711	3,711
Total assets	192,205	225,023	231,614	248,944	253,718

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Net income + Depreciation	16,925	16,145	17,541	20,243	22,379
Interest expenses	1,986	2,808	4,416	4,191	(4,261)
Non-cash adjustments	(1,232)	(469)	(1,200)	(1,350)	(1,500)
Changes in working capital	(13,466)	25,253	(6,050)	5,718	(5,676)
Other operating cash flows	(1,929)	(286)	0	0	0
Cash flow from operations	2,284	43,451	14,707	28,802	10,943
Capital expenditures	(13,988)	(49,352)	(17,580)	(24,000)	(20,500)
Change in investments	13,365	(134)	0	0	0
Other investing cash flows	1,232	469	1,200	1,350	1,500
Cash flow from investing	609	(49,017)	(16,380)	(22,650)	(19,000)
Equities issued/Others	0	0	10,800	0	0
Debt raised/repaid	2,693	16,494	(5,426)	(1,000)	3,000
Interest expenses	(1,986)	(2,808)	(4,416)	(4,191)	(4,261)
Dividends paid	(2,069)	(4,310)	(262)	(770)	(899)
Other financing cash flows	(1,896)	(1,941)	0	0	0
Cash flow from financing	(3,258)	7,435	696	(5,961)	(2,160)
Changes in cash and cash eq.	(365)	1,869	(977)	191	(10,217)
Closing cash and cash eq.	5,627	7,496	6,519	6,711	5,015

Per Share

Y/E 31 Mar (Rs)	FY19A	FY20A	FY21E	FY22E	FY23E
Reported EPS	15.4	8.3	7.6	9.3	10.9
Adjusted EPS	15.4	8.3	7.6	9.3	10.9
Dividend per share	3.0	3.0	0.5	1.2	1.4
Book value per share	175.5	173.6	199.6	187.9	197.4

Valuations Ratios

Y/E 31 Mar (x)	FY19A	FY20A	FY21E	FY22E	FY23E
EV/Sales	0.8	0.9	0.9	0.8	0.7
EV/EBITDA	7.6	7.4	6.8	6.3	5.6
Adjusted P/E	11.3	20.9	22.8	18.7	16.0
P/BV	1.0	1.0	0.9	0.9	0.9

DuPont Analysis

Y/E 31 Mar (%)	FY19A	FY20A	FY21E	FY22E	FY23E
Tax burden (Net profit/PBT)	80.9	87.7	78.0	78.0	78.0
Interest burden (PBT/EBIT)	100.1	65.9	55.9	64.4	67.5
EBIT margin (EBIT/Revenue)	6.2	5.0	6.1	6.2	6.4
Asset turnover (Revenue/Avg TA)	112.9	96.5	87.9	98.2	103.7
Leverage (Avg TA/Avg Equity)	1.6	1.7	1.7	1.6	1.6
Adjusted ROAE	8.9	4.8	4.1	5.1	5.7

Source: Company, BOBCAPS Research | Note: TA = Total Assets

Ratio Analysis

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
YoY growth (%)					
Revenue	18.2	(7.0)	(0.3)	15.9	9.2
EBITDA	6.5	7.8	14.8	12.6	9.4
Adjusted EPS	(6.1)	(29.9)	(8.4)	22.2	16.7
Profitability & Return ratios (%)					
EBITDA margin	10.1	11.7	13.5	13.1	13.1
EBIT margin	6.2	5.0	6.1	6.2	6.4
Adjusted profit margin	3.9	2.9	2.7	3.1	3.4
Adjusted ROAE	6.8	4.8	3.8	5.0	5.5
ROCE	5.7	4.3	4.2	4.8	5.2
Working capital days (days)					
Receivables	27	23	24	25	24
Inventory	67	75	72	68	68
Payables	85	91	95	92	91
Ratios (x)					
Gross asset turnover	1.1	1.5	1.6	1.5	1.5
Current ratio	1.7	1.3	1.4	1.2	1.3
Net interest coverage ratio	5.5	2.9	2.3	2.8	3.1
Adjusted debt/equity	0.5	0.7	0.5	0.5	0.5

Source: Company, BOBCAPS Research

Disclaimer

Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

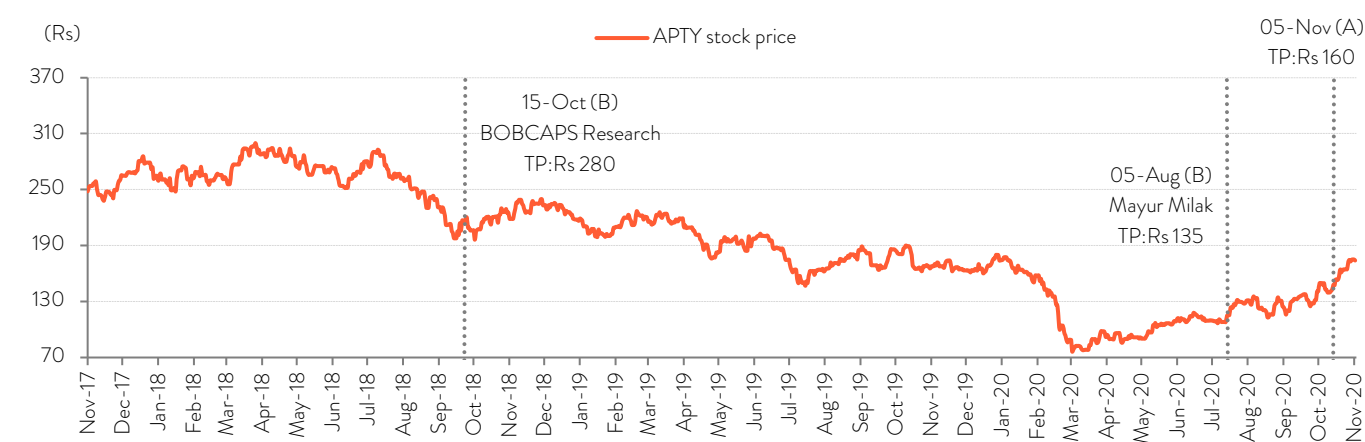
ADD – Expected return from >+5% to +15%

REDUCE – Expected return from -5% to +5%

SELL – Expected return <-5%

Note: Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

RATINGS AND TARGET PRICE (3-YEAR HISTORY): APOLLO TYRES (APTY IN)



B – Buy, A – Add, R – Reduce, S – Sell

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