Sharekhan by BNP PARIBAS

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Stock Update

Annual Report Review

Apollo Tyres Ltd

Rolling ahead on growth path

Automobiles	Sharekhan code: APOLLOTYRE		
Reco/View: Buy ↔	CMP: Rs. 176	Price Target: Rs. 222 ↓	

↑ Upgrade ↔ Maintain ↓ Downgrade

3R MATRIX	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)	✓		

+ Positive = Neutral – Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↔	

ESG Disclosure Score NEW

ESG RISK RATING 28.15

Updated Feb 08, 2022

Medium Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

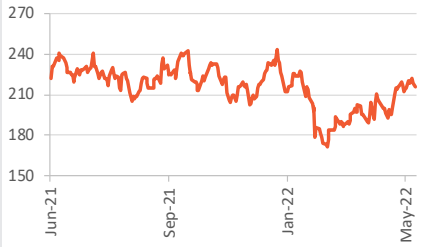
Company details

Market cap:	Rs. 10,924 cr
52-week high/low:	Rs. 250 / 165
NSE volume: (No of shares)	35.5 lakh
BSE code:	500877
NSE code:	APOLLOTYRE
Free float: (No of shares)	39.8 cr

Shareholding (%)

Promoters	37.3
FII	19.4
DII	20.1
Others	23.1

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-2.6	1.4	2.8	2.8
Relative to Sensex	-1.9	10.8	14.2	9.5

Sharekhan Research, Bloomberg

Summary

- Apollo Tyres Ltd's (ATL's) management stays committed to achieve its long-term goal of revenues of $5 billion by FY2026, EBITDA margin of at least 15%, ROCE of 12-15%, and net debt to EBITDA of less than 2x.
- ATL is set to benefit from its strategy of deleveraging its balance sheet, improving operating leverage and focusing on firm capital allocation and cash management going forward.
- Stock trades attractively at a P/E multiple of 7.9x and EV/EBITDA multiple of 4.1x its FY2024E estimates.
- We maintain a Buy rating on Apollo Tyres with a revised PT of Rs. 222, led by the company's dominant position in key markets, expected market share gains across segments, and attractive valuations.

Apollo Tyres Ltd (ATL) held its Corporate Day 2022 to share progress for achieving long-term strategic goals announced last year as Vision 2026. Management remain committed and is working towards achieving its long-term goals of achieving revenues of $5billion by FY2026, EBITDA margin profile to reach at least 15%, ROCE of 12-15%, and net debt to EBITDA of less than 2x. The management remains focused on its strategic and financial goals and delivered strong performance in H2FY22, despite unprecedented challenges of raw material price escalation, supply chain disruptions, container unavailability, and increase in ocean freight rates. We continue to maintain our positive stance on ATL and believe it is well-positioned to leverage market opportunities in India and abroad. ATL is to improve its OEM and replacement market sales, given the improvement in rural and semi-urban demand, and an improvement in economic activities in the medium term. The company is expected to improve its EBITDA margin, by deleveraging its balance sheet, improving in operating leverage and focus on firm capital allocation and cash management going forward, despite raw material headwinds likely to continue. Strong growth and a leadership position in key markets and segments is likely to help ATL to achieve its long-term targets of $5 billion by FY2026.

- **Beneficiary of better automobile demand and global revenues:** We expect the domestic tyre industry to benefit from a recovery in automobile sales in rural and semi-urban markets, driven by pent-up demand, preference for personal mobility amid COVID-19, and faster-than-expected recovery in infrastructure, mining, and other economic activities. The tyre industry is well positioned to gain momentum going forward backed by higher OEM offtake and the ripple effect of OEM demand is likely to result in steady growth for the replacement demand.
- **Focus on improving product mix and brand building:** ATL is focusing on increasing its share of premium tyres, i.e. UHP/UUHP segments, in Europe and US markets. The Vredestein brand is an established premium tyre brand in Europe. The company aims to increase its share of premium UHP and UUHP tyres to more than 45% revenue contribution over the next five years by FY2026, through new launches, brand building, and focus on increasing its presence in southwest Europe, while adding on to its healthy presence in western and central Europe.
- **Management remains committed to achieving long-term goals:** The management remains committed to long-term targets to achieve revenue of US$5 billion by FY2026, EBITDA margin profile to reach at least 15%, ROCE of 12-15%, and net debt to EBITDA of less than 2x. In addition, the company targets to be carbon neutral by 2050, for which it has ramped its ESG activities. ATL has approached the end of a major capex cycle with a continued focus on brand building, marketing, and distribution network. The company is operating at an 80-85% capacity utilization. The company's growth will be achieved through minimal capex, which would be spent on debottlenecking and technology in the medium term.

Our Call

Valuation – Maintain Buy rating with a revised PT of Rs. 222: Tyre demand has improved significantly in both domestic as well as European operations. ATL is well-positioned to gain market share in India and Europe, given its strong brand, R&D, technology, and distribution network. We expect the company to benefit from its strategy by deleveraging its balance sheet, improving capacity utilisation, and focusing on firm capital allocation and cash management in the medium term. Strong growth coupled with a leadership position in key markets and segments is likely to re-rate valuation multiples. The stock trades at attractive valuations at P/E multiple of 7.9x and EV/EBITDA multiple of 4.1x its FY2024E estimates. We retain our Buy rating on the stock with a revised PT of Rs. 222.

Key Risks

Apollo derives about 30% of its revenue from its European operations, which exposes it to currency risks. Any adverse movement in the INR-Euro pair would affect financial performance.

Valuation (Consolidated) Rs cr

Particulars	FY21	FY22	FY23E	FY24E
Revenues	17,376	20,948	22,832	25,118
Growth (%)	6.4	20.6	9.0	10.0
EBIDTA	2,777	2,574	3,083	3,545
OPM (%)	16.0	12.3	13.5	14.1
Adjusted PAT	958	644	1,062	1,413
% YoY growth	101.1	(32.7)	64.8	33.1
Adjusted EPS (Rs)	15.1	10.1	16.7	22.2
P/E (x)	11.7	17.3	10.5	7.9
P/B (x)	1.0	1.0	0.9	0.9
EV/EBITDA (x)	5.2	5.6	4.7	4.1
RoE (%)	9.3	5.9	9.2	11.3
RoCE (%)	7.8	5.4	7.1	8.7

Source: Company; Sharekhan estimates

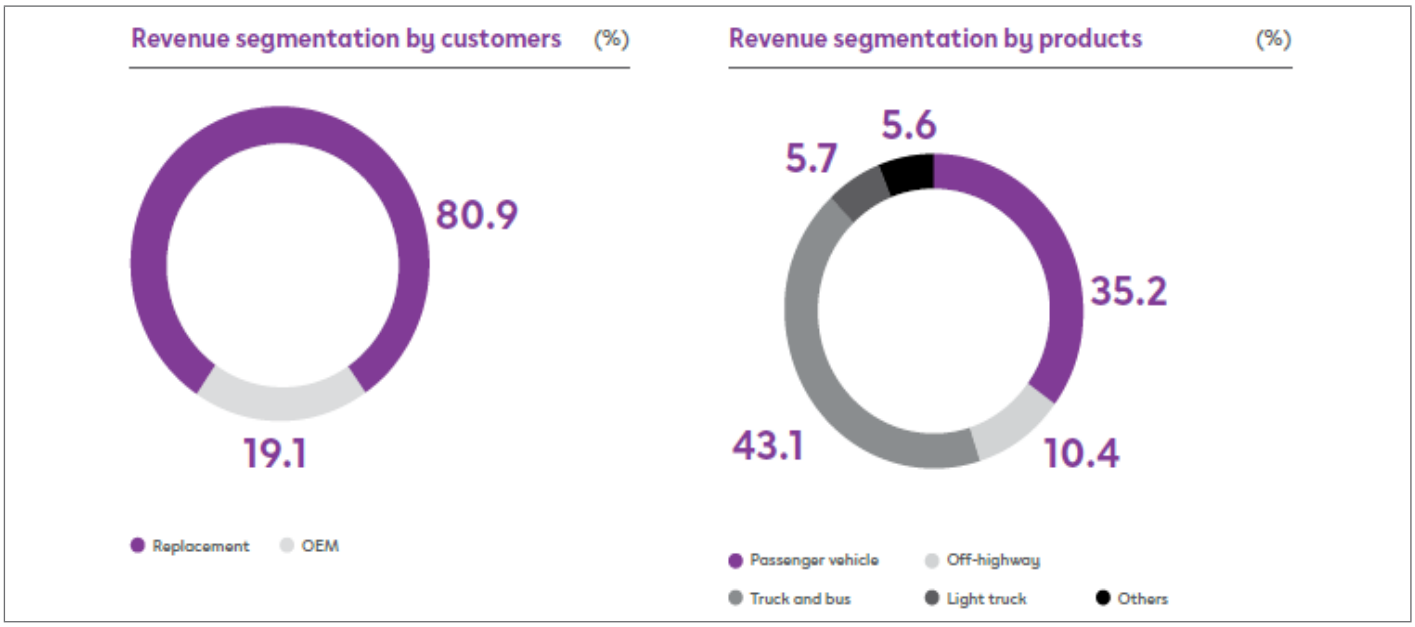
Key Highlights of Corporate Day/ Annual Report 2022

Apollo Tyres Ltd. (ATL) held Corporate Day 2022 to share the progress on its achieving long-term strategic goals announced last year as Vision 2026. Management remain committed and is working towards achieving its long-term goals of achieving revenue of US$5billion by FY2026, EBITDA margins of at least 15%, ROCE of 12-15%, and net debt to EBITDA of less than 2x. Here are the key highlights of the Corporate Day and the Annual Report -

FY22 – The Year gone by

- The tyres industry witnessed a sharp 30% escalation in their overall raw material costs. Also, driven by COVID-19, the industry saw supply chain disruptions due to global port congestions, container shortages and blank sailings. Ocean Freight rates rose over five times on most shipping routes during FY22.
- Oil prices continued to surge during the year, scaling a peak of USD 140/bbl on account of geopolitical factors, supply disruptions, inability of OPEC members to increase oil supply as per agreement, and rise in natural gas prices.
- Despite challenges in the macro scenario (supply constraints, high commodity prices and subdued demand environment), the company remained committed profitable growth path, led by enrichment of product mix and well-timed pricing actions.
- Focus on research & innovation, especially on achieving ultra-low rolling resistance and low noise tyres for electric vehicle segments.
- The company continues to work towards achieving Vision 2026 targets, with emphasis on Digitalisation, Technology and Innovation, People, Brand and Sustainability.
- The company's FY22 revenue grew 20% y-o-y to Rs20,948 crore, led by 25% growth in Indian operations and 18% growth in European operations.

Diversified revenue streams



Source: Annual Report FY22; Sharekhan Research

Indian Business

- Indian operations closed the year on a positive note, across its key categories – commercial and passenger vehicles. Importantly, the company witnessed growth across OEMs and the replacement market segments.
- The company has leadership in the commercial vehicle segment in India, with a market share of ~30%. It launched TBR products in Europe and North America, where it received a positive response.

- Apollo Tyres maintained its overall leadership across the radial segments in the M&HCV category, driven by new launches or refreshing the range, investing in expanding the distribution network, investing in dealer relationship. Also, the company is expected to maintain its leadership position in the truck radial and PV segment and drive growth.
- In the passenger car segment, the company has a market share of ~20% in India. The company has launched the Vredestein brand in India and is gaining traction in premium segment in Europe (UHP/UUHP) and North America
- In the two-wheeler tyre segment, the company is focussing on premium end of market with its Alpha range.

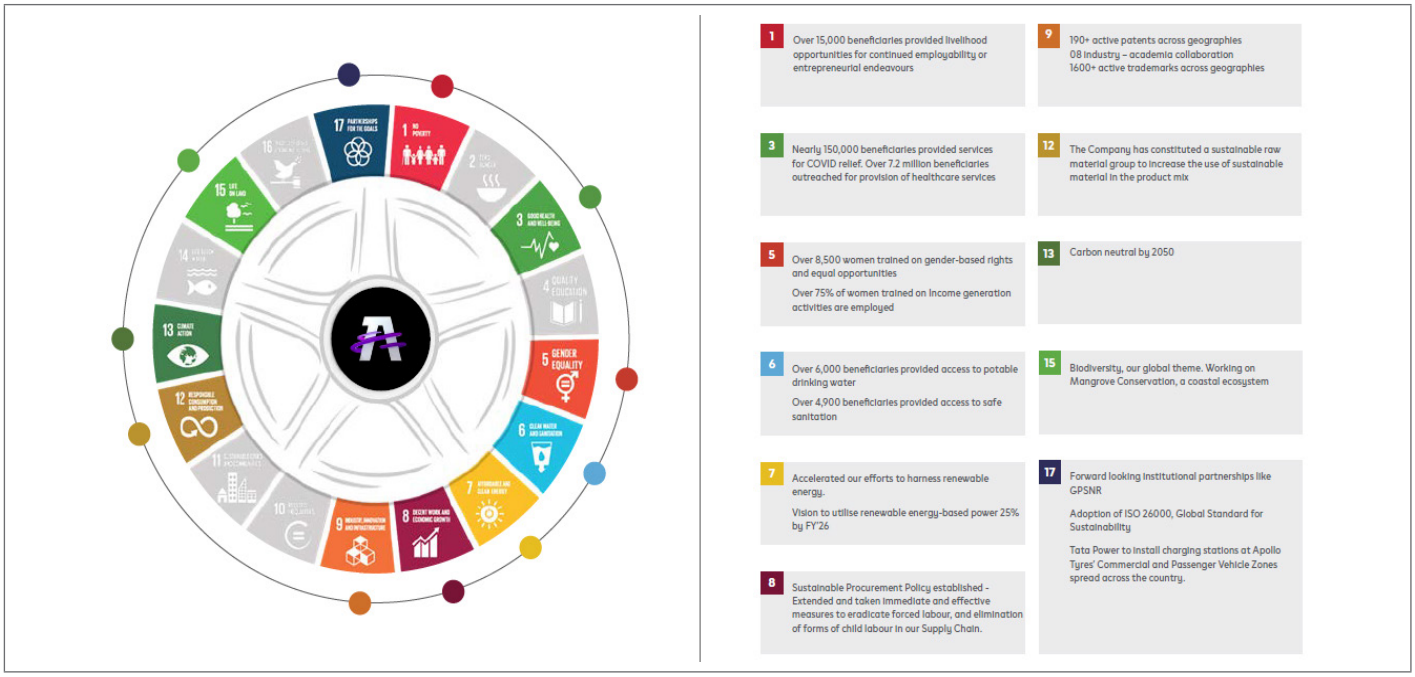
Global Business

- The company continues to strengthen on its brands, 'Apollo Tyres' and 'Vredestein Tyres' across more than 100 countries. The company has seven manufacturing plants across India and Europe, and two global R&D centres.
- Apollo Tyres sells tyres across auto segments such as trucks, buses, light trucks, passenger vehicles, off-highway vehicles and two-wheelers.
- In the Europe region, the company has focus on premiumization products such as agriculture tyres and high value premium passenger car tyres segment. The company has scaled up its brand value in the region and make higher margins to its overall product profile.
- In FY22, the company focussed on adding new sizes to its product lines introduced in FY21 and consolidate the market offering. The year saw the product launches and marketing initiatives in line with this strategy as it added 24 sizes in the ultra-high performance (UUHP) tyre segment (19 inches and above).
- ATL is focussing on increasing its share of premium tyres, i.e. UHP/UUHP segments, in Europe and the US. The Vredestein brand is an established premium tyre brand in Europe. The company has increased its share of premium UHP and UUHP tyres to 43% revenue contribution in FY22 as compared to 40% contribution in FY21.
- The company has launched truck tyres in Europe, which would enhance revenue and market presence.
- Europe saw good traction for the commercial vehicle category, while in the passenger car segment, it was replacement market sales that lifted Europe's overall business performance.
- The company has entered the CV tyre segment in North America, after a successful launch of its passenger vehicle range in this market.
- Apollo Tyres has started deliveries to European OEM manufacturers endorsing the premium position of its Vredestein brand. This will help to generate replacement demand going forward.
- Anti-dumping measures in EU against Chinese imports will support the expansion of Apollo's truck tyre footprint.

ESG Roadmap

- Apollo Tyres has aligned its sustainability with UN's Sustainable Development Goals (SDGs). The company has been rated among India's 50 most sustainable companies based on SDG by 2021 Capri Global Capital Hurun India.
- The company aspires to be carbon neutral by 2050 and is investing in advanced processes and systems to pursue its objective. The company is developing a decarbonisation roadmap and short-term goals for FY26 and FY30.
- In order to support EV development in India, the company has developed an EV range, which offers a low-rolling resistance coefficient, reduced noise and better comfort without losing structural durability and wear performance. In FY22, the rolling resistance of the PCR was reduced from 7 Kg/T to 6.3 Kg/T translating into a reduction of rolling loss and reduced fuel consumption.
- The company has improved on re-treading techniques of truck tyres to provide extended life cycle of the tyre body material to 2-3 times, thus, restraining the need for frequent replacements.

Apollo Tyres's sustainability goals aligned to UN's SDGs revenue streams



Source: Company's Annual Report FY22; Sharekhan Research

Key improvements achieved in ESG parameters during FY22

- Rolling resistance of PCR was reduced from 7 Kg/T to 6.3 Kg/T in FY22
- Water consumption (Litre/Kg) PCR & TBR at Chennai manufacturing location dropped by 14%
- Steam consumption (kg/kg) dropped by 6.8 and 6.5 % for TBR and PCR, respectively.
- Progressive reduction of tyre weight in PCR up to ~8% by redesigning the product, resulting in reduced carbon footprint per tyre.
- Silica based tyre production for PCR category was ~ 28%, which reduced the consumption of carbon black, a fossil fuel based reinforcing agent.
- 'Smart Cure Technology' was introduced in TBR based on real time heat input and termination of cure cycle and achieve right cure level for all tyres. Also, early Detection system established for TBR Tyre by measuring green tyre uniformity, which resulted in rejection of cured tyres.
- 9.4% of renewable energy (RE) in total power share with an aim to increase RE share to 25% by FY26

Strengthening brand

- Branding has been a key driver to the company's success. The company has two established brands, viz., Apollo Tyres and Vredestein Tyres.
- The digital platform continued to be key for brand-building as it gave a larger exposure to the Company's marketing and communication initiatives and other brand building content.
- Bringing Vredestein into India, was the biggest highlight of the year.
- The Company also focussed on its other global brand, Apollo, in Europe. It introduced four new TBR SKUs and 18 new OHT SKUs for the Europe region.
- The company's focus on strengthening the Vredestein brand and the UUHP segment has seen the brand grow in double digits during FY22.

Well positioned to benefit from its brands

			Passenger Car Tyres						
Pricing Segment	Brand	Brand Positioning	Summer Tyres	Winter Tyres	All Season Tyres	Commercial Vehicle Tyres	Farm/Off Highway Tyres	Two Wheeler Tyres	Bicycle Tyres
Top	VREDESTEIN TIRES	Global Niche Premium	✓	✓	✓		✓	✓	✓
Medium	apollo TYRES	Global	✓	✓	✓	✓	✓	✓	

Source: Company's Investor Presentation; Sharekhan Research

Thrust on digitalisation, branding and R&D

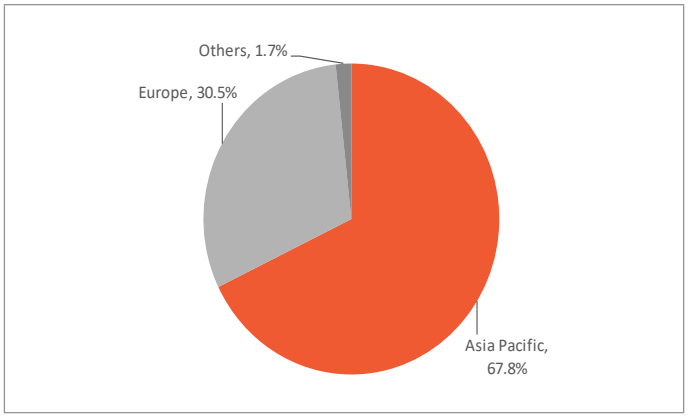
Digitalisation and branding are the company's key growth enablers. ATL has invested significantly in building up the brand, plant infrastructure, and R&D capability over the past decade. The company has invested in building tyre capacity in India and Europe. In the past few years, the company's focus has been ramping up capacity in plants situated in Chennai, Hungry, and Andhra Pradesh. ATL's has two key brands viz., Apollo Tyres and Vredestein in India. The company has a strong recall for both brands. The company has gradually increased its focus on brand building, marketing, and customer engagement, by increasing it spending to 2-2.5% of revenue currently from ~1% in FY2014. It has been institutionalising marketing platforms (Manchester United and ISL) for brand building, the brand ambassadorship of Sachin Tendulkar and creation of communities such as Bad Road Buddies.

Management Outlook

The company has maintained its vision for FY26. The company aims to receive revenue of US$ 5 billion, EBITDA margin higher than 15%, ROCE between 12-15% and net debt to EBITDA less than 2 times. The key drivers for achieving FY26 goals would include sweating of assets, strengthening balance sheet, generating robust cash flow and improving return ratios. In the near-term, the company expects raw material prices to remain firm on the back of geopolitical situation and rising demand. The automotive demand is strong and would benefit the company, given its strong brand recall, robust distribution network and dominant market share in CV and PV tyre segments. Pricing remains stable and the company would most likely take pricing action to mitigate rise in raw material costs. The management commits to focus on profitable growth path. The capex for FY22 was Rs. 1,800 crore, while it allocated Rs. 900 crore for Indian business and 40 million euros for European facilities. The capex is largely allocated towards de-bottlenecking existing capacities, digitalisation and judicious brownfield expansions. ATL's capacity utilisation during FY22 are at 80% for India facilities and 85% for Europe facilities.

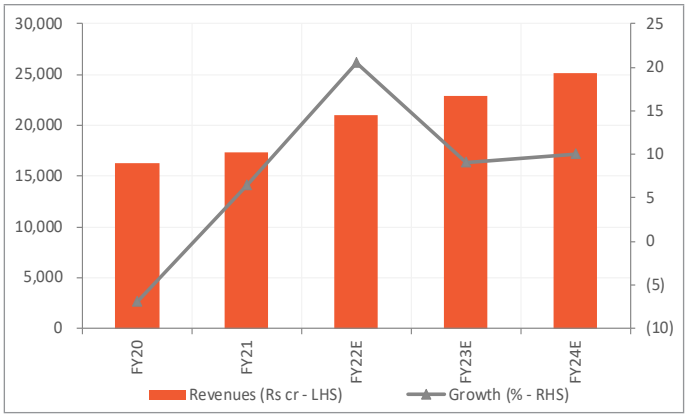
Financials in charts

Geographical Mix (%)



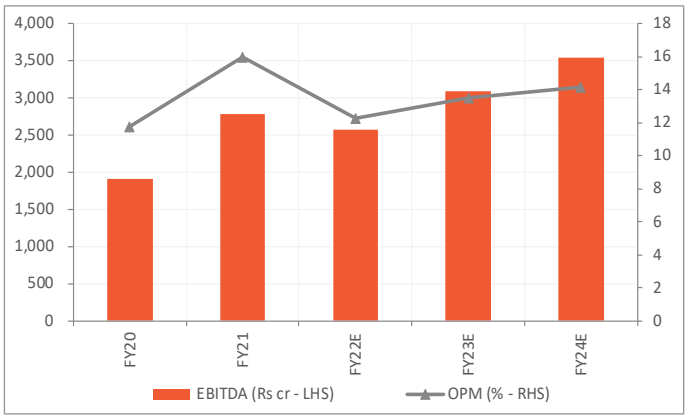
Source: Company, Sharekhan Research

Revenue and Growth Trend



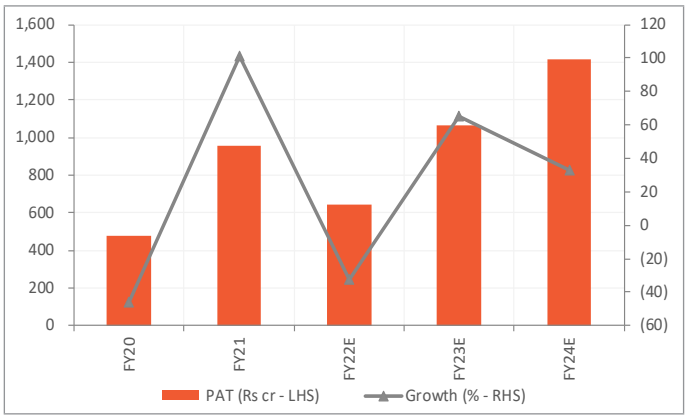
Source: Company, Sharekhan Research

EBITDA and OPM Trend



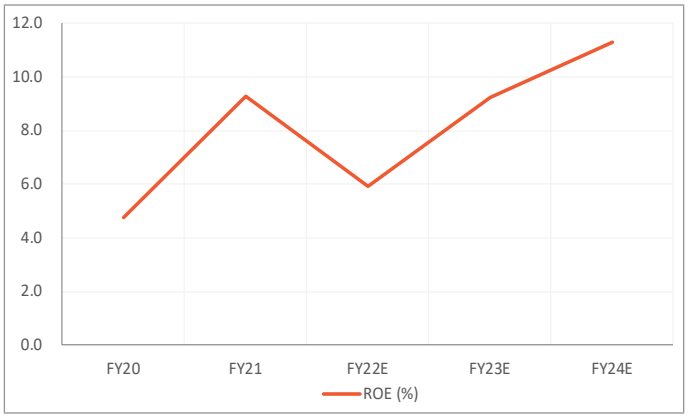
Source: Company, Sharekhan Research

PAT and Growth Trends



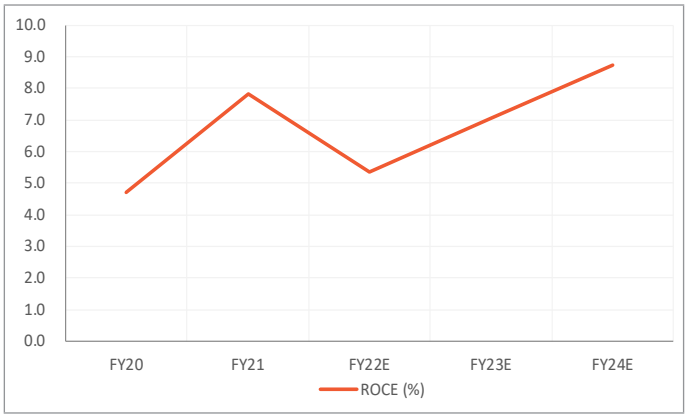
Source: Company, Sharekhan Research

RoE Trend



Source: Company, Sharekhan Research

RoCE Trend



Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector Outlook – Strong recovery eyed

We expect the domestic tyre industry to benefit from a recovery in automobile sales in rural and semi-urban markets, driven by pent-up demand, preference for personal mobility amid COVID-19, and faster-than-expected recovery in infrastructure, mining, and other economic activities. The tyre industry is well positioned to gain momentum going forward, backed by higher OEM offtake and the ripple effect of OEM demand is likely to result in steady growth for the replacement demand.

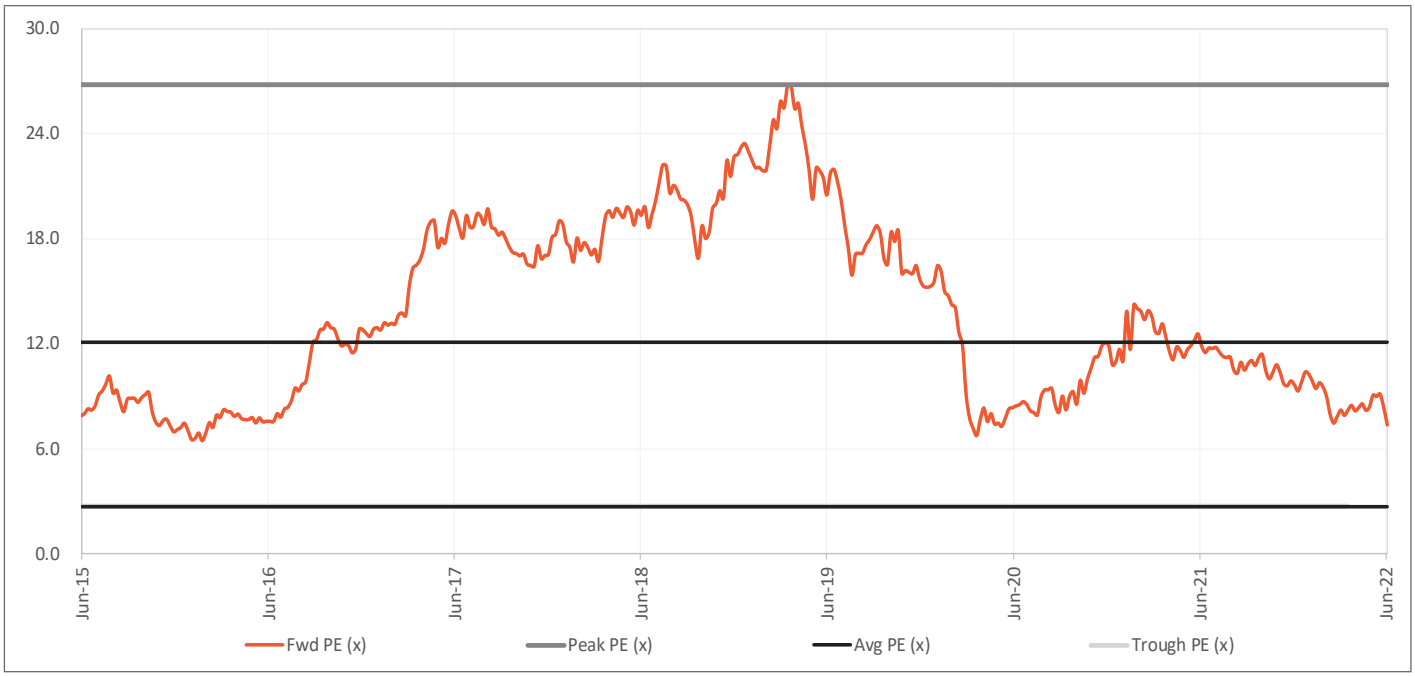
■ Company Outlook – Convincing strategy to achieve a profitable growth model

The management has set its long-term targets to achieve revenue of US$5 billion by FY2026, EBITDA margin profile to reach at least 15%, ROCE of 12-15%, and net debt to EBITDA of less than 2x. Moreover, the company has maintained revenue growth guidance of 20-22% for FY2022E, driven by expected recovery in volumes post normalisation of economic activities. The overseas business is expected to do well because of richer product mix and gradual capacity additions.

■ Valuation – Maintain Buy rating with a revised PT of Rs. 222

Tyre demand has improved significantly in both domestic as well as European operations. ATL is well-positioned to gain market share in India and Europe, given its strong brand, R&D, technology, and distribution network. We expect the company to benefit from its strategy by deleveraging its balance sheet, improving capacity utilisation, and focusing on firm capital allocation and cash management in the medium term. Strong growth coupled with a leadership position in key markets and segments is likely to re-rate valuation multiples. The stock trades at attractive valuations at P/E multiple of 7.9x and EV/EBITDA multiple of 4.1x its FY2024E estimates. We retain our Buy rating on the stock with a revised PT of Rs. 222.

One-year forward P/E (x) band



Source: Company, Sharekhan Research

Peer Comparison

Particulars	CMP	P/E (x)			EV/EBIDTA (x)			RoCE (%)		
	Rs/Share	FY22	FY23E	FY24E	FY22	FY23E	FY24E	FY22	FY23E	FY24E
Apollo Tyres	176	17.3	10.5	7.9	5.6	4.7	4.1	5.4	7.1	8.7
Balkrishna Industries	2,076	28.4	24.4	19.5	21.2	17.2	14.1	25.3	24.4	25.8

Source: Company, Sharekhan Research

About company

ATL is the second largest tyre manufacturer in India. ATL is a diversified player present in India as well as Europe. Indian business contributes about 70% to revenue, while European business contributes about 30%. With its recent entry into the two-wheeler space, ATL has become a full-fledged tyre player present across automotive categories viz. passenger vehicles, commercial vehicles, and two wheelers. The OEM segment contributes about 27% to revenue, while the replacement segment accounts for the balance 73%.

Investment theme

ATL is one of the leading tyre companies in India, with a leadership position in the largest truck and bus tyre segment. The company is also one of the leading players in passenger vehicle segment in India. Over the past few years, ATL has been increasing its presence globally and acquired businesses in Europe, which has not only opened up new markets for the company but has also strengthened its R&D capabilities globally. ATL is expected to gain market share in other segments and in multiple geographies (e.g. Vredestein in passenger vehicles and Apollo in truck and bus segments), driven by strong brand, R&D, technology, and distribution network. In addition, the company will operationally improve its margin, aided by specialisation of Dutch plant (through significant uptick in cost competitiveness, given ramping up production in Hungary); cost reductions through digitalisation of its businesses, and improvement in passenger vehicle mix.

Key Risks

ATL derives about 30% of its revenue from European operations, which exposes it to currency risks. Any adverse movement in INR-Euro pair would impact its financial performance.

Additional Data

Key management personnel

Onkar Singh Kanwar	Chairman and Managing Director
Mr Neeraj Kanwar	Vice Chairman and Managing Director
Sunam Sarkar	President and Chief Business Officer
Gaurav Kumar	Chief Financial Officer

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Sunrays Properties & Investment	19.9
2	Emerald Sage Investment	9.9
3	Hdfc Trustee Company	8.3
4	White Iris Investment	8.0
5	Osiatic Consultants & Investments	6.2
6	Apollo Finance Ltd.	5.9
7	Classic Industries & Exports Ltd.	2.8
8	Custodian A/c - Ashwin Shantilal Mehta	2.1
9	PTL Enterprises	1.7
10	ICICI Prudential Equity Savings Fund	1.5

Source: Bloomberg

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

Sharekhan

by BNP PARIBAS

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