Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Amara Raja Batteries Limited

Powered to Perform

Automobiles	Sharekhan code: AMARAJABAT	Company Update

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		↓	

Reco/View	Change
Reco: **Buy**	↔
CMP: **Rs. 922**	
Price Target: **Rs. 1,060**	↑

↑ Upgrade ↔ Maintain ↓ Downgrade

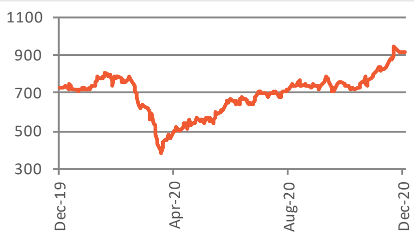
Company details

Market cap:	Rs. 15,710 cr
52-week high/low:	Rs. 964 / 350
NSE volume: (No of shares)	10.0 lakh
BSE code:	500008
NSE code:	AMARAJABAT
Free float: (No of shares)	12.3 cr

Shareholding (%)

Promoters	28.1
FII	18.6
DII	24.0
Others	29.3

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	14.9	24.9	37.1	26.2
Relative to Sensex	4.5	6.2	4.1	13.4

Sharekhan Research, Bloomberg

Summary

- We maintain our Buy rating on Amara Raja Batteries (Amara) with a revised PT of Rs. 1,060, factoring better multiples owing to a better outlook for automotive and select industrial segments (telecom and UPS).
- Amara well-positioned to gain market share in lead acid battery business by adding clients and widening replacement distribution network.
- EBITDA margins to remain strong at 17.5% in FY22E driven by favourable product mix, led by a higher share of revenues from replacement segment, operating leverage and cost-cutting measures.
- Stock attractively valued with P/E multiple of 18.3x and EV/EBITDA multiple of 9.3x its FY2023E estimates, and is at a 20-25% discount to its long-term average multiples.

Amara Raja Batteries Limited (Amara) is expected to benefit from an improving business outlook for automotive and industrial sectors, driven by normalisation of economic activities. Amara's revenue are dependent on the two-wheeler and four-wheeler industries, where we see positive traction and strong recovery in sales on a m-o-m basis. The y-o-y numbers have also started showing positive growth. The automotive aftermarket segment, which contributes more than 85% of Amara's automotive business, is expected to remain buoyant, aided by pent-up demand and increased preference for personal transport. We expect Amara to continue outpace peers, by adding clients, launching products and by benefiting from its extensive distribution network. The company is increasing its automotive battery capacity from 29 million units to 34 million units by the end of FY2021 to benefit from the expected rise in demand. The industrial segment is also witnessing growth driven by recovery in telecom and commercial UPS segments. Amara's focus in commercial UPS and telecom segment is driven by enhanced priorities to keep the data network uptimes near to 100%. Also, exports of automotive and industrial batteries are witnessing huge demand. We expect Amara to sustain its high EBITDA margins as witnessed in Q2FY2021 results due to richer product mix, operating leverage and benefitting from cost-cutting measures. The company is debt-free and generates strong cash flows, enough to expand capacity through internal accruals. The company has a strong long-term revenue visibility, given its focus on aftermarket segment. We expect Amara's earnings to grow by 20.5% in FY2022E and 15.4% in FY2023E, driven by 13% CAGR (FY2021-23) in revenues and 110 bps expansion EBITDA margins.

Our Call

Valuation - Maintain Buy with a revised PT of Rs. 1,060: Amara is witnessing recovery in automotive and industrial demand. The outlook remains positive with strong recovery expected from FY2022, driven by normalisation of economic activities. Operating profit margins would expand on back of operating leverage and cost-control measures. We have retained our earnings estimates, however, have increased target P/E multiple, given improved business outlook. We have valued the stock by assigning P/E multiple of 21x, a slight discount to average long-term P/E multiples, on Amara's FY2023E earnings to arrive at a revised PT of Rs. 1,060. The stock is attractively valued at P/E multiple of 18.3x and EV/EBITDA multiple of 9.3x its FY2023 estimates. We retain our Buy rating on the stock with a revised PT of Rs. 1,060.

Key Risks

A second wave of COVID-19 can lead to a slowdown in economic activities and thus can impact earnings of the company. Also, a steep rise in lead prices, a key raw material, can impact profitability.

Valuation (Standalone) Rs cr

Particulars	FY19	FY20	FY21E	FY22E	FY23E
Net sales (Rs cr)	6,793	6,839	6,907	7,878	8,853
Growth (%)	12.1	0.7	1.0	14.1	12.4
EBIDTA (Rs cr)	952	1,099	1,138	1,374	1,557
OPM (%)	14.0	16.1	16.5	17.4	17.6
PAT (Rs cr)	483	661	620	747	862
Growth (%)	2.6	36.7	(6.1)	20.5	15.4
FD EPS (Rs)	28.3	38.7	36.3	43.8	50.5
P/E (x)	32.6	23.8	25.4	21.1	18.3
P/BV (x)	4.7	4.1	3.7	3.3	2.9
EV/EBITDA (x)	16.5	14.0	13.4	10.8	9.3
RoE (%)	14.5	17.4	14.6	15.7	16.1
RoCE (%)	20.5	21.1	18.7	20.1	20.7

Source: Company; Sharekhan estimates

Beneficiary of improved automotive business outlook: Amara is expected to be beneficiary of improving business outlook for the automotive and industrial sectors, driven by normalisation of economic activities. Amara's revenue is largely dependent on the two-wheeler and four-wheeler industry, where we see positive traction and a strong recovery in sales on a m-o-m basis. The y-o-y numbers have also started showing positive growth. The automotive aftermarket segment, which contributes more than 85% of Amara's automotive business, is expected to remain buoyant, aided by pent-up demand and increased preference for personal transport. We expect Amara to continue outpace the organised lead-acid battery industry, led by new client acquisition, product launches and benefits of its extensive distribution network.

Demand from industrial segment remains strong as well: The industrial segment is also witnessing growth driven by recovery in telecom and commercial UPS segments. Amara's focus in commercial UPS and telecom segment is driven by enhanced priorities to keep the data network uptimes near to 100%.

Traction in export markets: Amara is witnessing an upsurge in demand for exports of automotive and industrial batteries in a number of regions. Penetration in the existing market would continue its export growth. The export contributes ~13% of revenues.

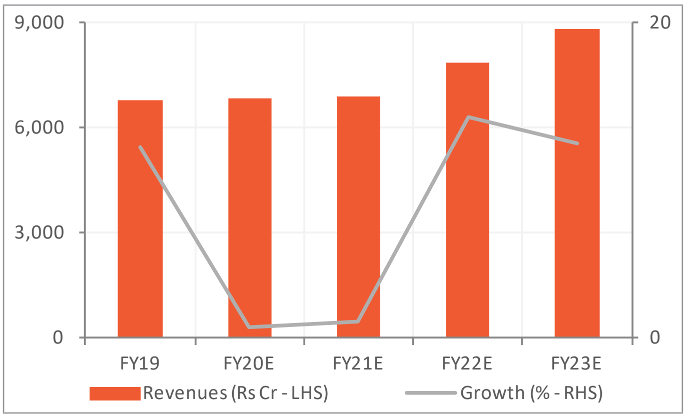
Latest quarterly results surprised; margins improved and likely to sustain: Q2FY21 results were strongly ahead of expectations. Revenues grew strongly 14% y-o-y to Rs. 1,936 crore, with demand getting revived across the key segments. Automotive OEM demand increased y-o-y driven by preference for personal mobility and channel filling ahead of the festive season. Automotive replacement segment witnessed strong traction driven by pent-up demand during lockdown and improved logistics and channel activities post the government's unlocking measures. The Industrial segment witnessed healthy demand driven by telecom and the commercial UPS segments on back of enhanced priorities for keeping data network uptimes close to 100%. Also, the battery exports saw an upsurge as overseas markets started opened up. Operating margins improved by 40 bps y-o-y to 17.6%, highest in the last five years, driven by operating leverage benefits. Tracking strong operating performance, PBT grew 17% y-o-y to Rs 271 crore. Net Profit at Rs 202cr declined 8% y-o-y. Amara generated strong operating cash flows to the tune of Rs 600 crore in the H1FY2021, aided by reduction in working capital.

Capacity expansion plans: Amara is expanding capacity in the automotive segment which forms about 50% of its revenues. Given the strong demand traction in the automotive segment, Amara is increasing capacity of four wheelers batteries from 12 million units to 14 million units, while in case of two-wheeler segment, Amara is enhancing capacity from 17 million units to about 20 million by the end of FY2021. Amara is gaining market share in both the automotive OEM and replacement space. In the replacement segment, the company is strengthening its distribution network in Western and Eastern India where it has relatively lower presence. In the automotive OEM segment, the company is increasing its share of business and also adding new clients in the two-wheeler segment. We expect Amara to continue outpacing industry growth. The company has invested Rs 200 crore in H1FY2021 and further plans to invest Rs. 250 crore in H2FY2021.

Strong broad-based recovery; expect double-digit growth in FY22: The company is debt-free and generates strong cash flows, sufficient enough to expand capacity through internal accruals. The company has a strong long-term revenue visibility, given its focus on aftermarket segment. We expect Amara's earnings to grow by 20.5% in FY2022E and 15.4% in FY2023E, driven by 13% CAGR (FY2021-23) in revenues and 110 bps expansion EBITDA margin. We have retained our earnings estimates.

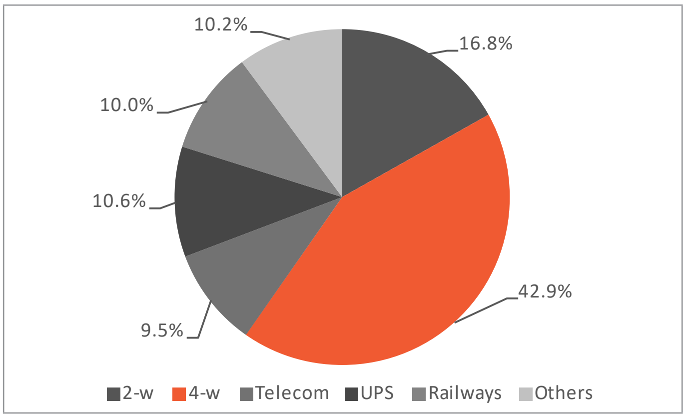
Financials in charts

Revenue and growth trend



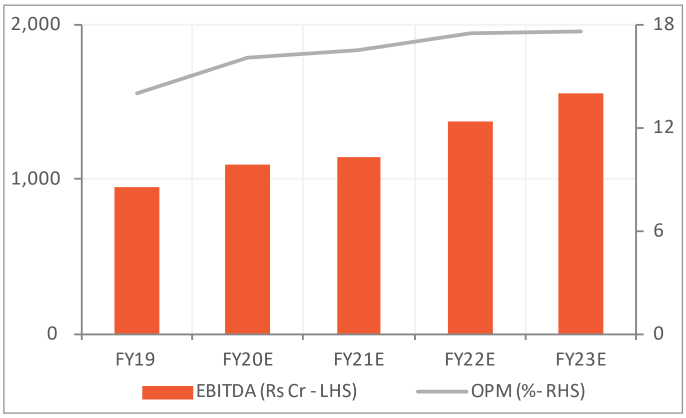
Source: Company, Sharekhan Research

Revenue Mix (%)



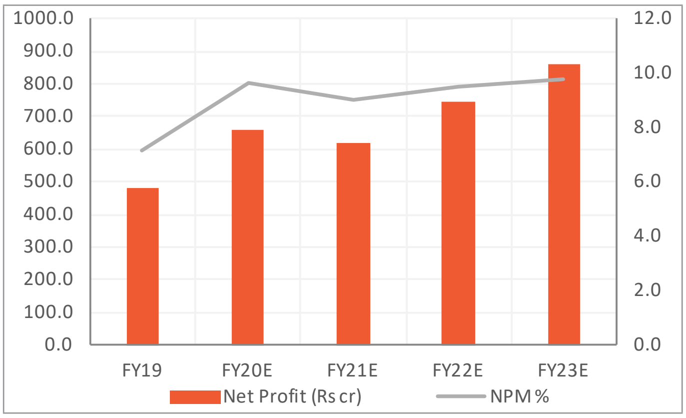
Source: Company, Sharekhan Research

EBITDA and OPM trend



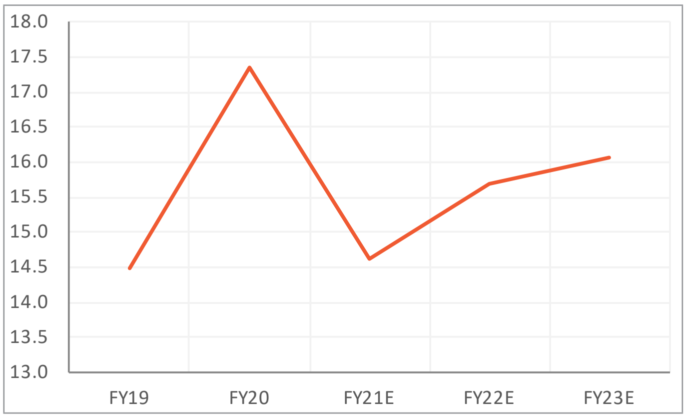
Source: Company, Sharekhan Research

Net profit and growth trend



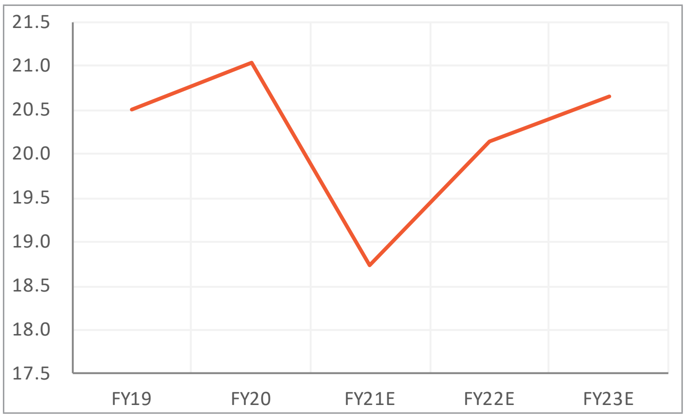
Source: Company, Sharekhan Research

RoE trend



Source: Company, Sharekhan Research

RoCE trend



Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector outlook - Demand picking up in automotive and industrial sector

The business outlook for the automotive and industrial segments is improving with a normalisation of economic activities. The automotive demand is witnessing strong recovery in two-wheeler and four-wheeler segments aided by pent-up demand, and increase in personal mobility transport. The industrial segment is also witnessing growth driven by recovery in telecom and UPS segments. The potential in telecom and UPS industry demand remain buoyant on back of increased data usage and digitalisation.

■ Company outlook - Strong earnings growth

We expect Amara to continue outpace the organised lead-acid battery industry, led by new client acquisition, new product launches and benefitting from its extensive distribution network. The company is increasing its automotive battery capacity from 29 million units to 34 million units by the end of FY2021 to benefit from the expected rise in demand. With the government opening up the economy, the demand in the automotive replacement segment and UPS is recovering. OEM business in both the auto and industrial segments is also recovering with businesses ramping up.

■ Valuation - Maintain Buy with a revised PT of Rs. 1,060, providing an upside room of 15%

Amara is witnessing a recovery in automotive and industrial demand. The outlook remains positive with strong recovery expected from FY2022, driven by normalisation of economic activities. Operating profit margins would expand on back of operating leverage and cost-control measures. We have retained our earnings estimates, however, have increased target P/E multiple, given improved business outlook. We have valued the stock by assigning P/E multiple of 21x, a slight discount to average long-term P/E multiples, on Amara's FY2023E earnings to arrive at a revised PT of Rs. 1,060. The stock is attractively valued at P/E multiple of 18.3x and EV/EBITDA multiple of 9.3x its FY2023 estimates. We retain our Buy rating on the stock with a revised PT of Rs. 1,060.

PT valued at slight discount to average long-term P/E multiple

Price Target Calculation		
FY2023E EPS (Rs. per share)	50.5	
Target P/E Multiple (x)	21x	Slight discount to long-term average
Target Price (Rs.)	1,060	
Upside (%)	15%	

Source: Company Data; Sharekhan Research

One-year forward P/E (x) band

Source: Company Data; Sharekhan Research

About company

Amara is a flagship company of the Amara Raja Group. The company is one of the leading manufacturers of lead acid storage batteries catering to the needs of both industrial as well as the automotive space. In the automotive segment, the company makes batteries for four-wheelers and two-wheelers and caters to the OEM as well as aftermarkets segment. The products for the automotive segment are marketed under the Amaron and Powerzone brands. In the industrial segment, the company is a preferred supplier to major telecom service providers, telecom equipment manufacturers, UPS sector (OEM and Replacement), Indian Railways and to power, oil and gas among others. The company has a commendable share in the telecom and UPS batteries segment. Amara's manufacturing plants are located in Chittor district in Andhra Pradesh and are equipped with state-of-the-art manufacturing plants.

Investment theme

Amara witnessed strong recovery in top-line in Q2FY2021 with 14% y-o-y growth. Growth was across segments viz automotive and industrial. With expected normalisation of economic activities, we expect double digit growth from FY22. Amara is expected to continue outpacing organised lead acid battery industry driven by new client additions in automotive OEM as well as new product launches and expanding network reach in automotive aftermarket. Company is enhancing automotive battery capacity from 29 million units to 34 million units by end of FY21. Key segments of telecom and UPS have recovered strongly and have huge growth potential going ahead driven by increasing data usage and increased digitalisation. Margins are expected to remain at higher end of historical band of 14-17% driven by operating leverage and cost control measures. Amara is a debt free company with strong balance sheet and healthy return ratios.

Key Risks

- The second wave of COVID-19 can lead to slow down in the economic activities and thus can impact earnings of the company.
- A steep rise in lead prices, a key raw material, can impact profitability.

Additional Data

Key management personnel

Ramachandra N Galla	Chairman
Jayadev Galla	Vice - Chairman & Managing Director
Vijayanand S	Chief Executive Officer
Delli Babu Y	Chief Financial Officer

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	RNGALLA FAMILY PVT LTD	28.06
2	PANTHER ARBL HOLD LP	24.0
3	Nalanda India Equity Fund Ltd	7.99
4	ICICI MUTUAL FUND	3.97
5	ICICI Prudential Asset Management	3.76
6	UTI Asset Management Co Ltd	1.72
7	L&T Mutual Fund Trustee Ltd/India	1.63
8	NATIONAL WESTMINSTER BANK	1.35
9	Baron Capital Inc	1.23
10	St James's Place PLC	1.11

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

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