Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Apollo Tyres Ltd

Strong performance in tough environment

Automobiles	Sharekhan code: APOLLOTYRE
Reco/View: Buy ↔	CMP: **Rs. 250** / Price Target: **Rs. 303** ↑

↑ 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 Jan 08, 2022

Medium Risk

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

Source: Morningstar

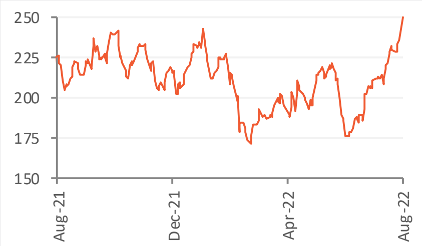
Company details

Market cap:	Rs. 15,578 cr
52-week high/low:	Rs. 257 / 165
NSE volume: (No of shares)	33.2 lakh
BSE code:	500877
NSE code:	APOLLOTYRE
Free float: (No of shares)	39.8 cr

Shareholding (%) as on Jun 30, 2022

Promoters	37.3
FII	20.7
DII	19.0
Others	22.9

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	20.7	18.9	11.8	16.2
Relative to Sensex	8.9	5.9	9.7	6.5

Sharekhan Research, Bloomberg

Summary

- We maintain a Buy rating on Apollo Tyres Limited (ATL) with an unchanged PT of Rs303, led by the company's dominant position in key markets, expected market share gains across segments, and attractive valuations.
- ATL is expected to benefit from its strategy of deleveraging its balance sheet, improving operating leverage and focusing on firm capital allocation and cash management going forward. Management maintains its long-term goals.
- We expect ATL's earnings to clock a 57.6% CAGR during FY2022-FY2024E, driven by a 13.1% revenue CAGR and a 130 bps EBITDA margin expansion to 14.2% in FY2024E.
- Stock trades attractively at P/E multiple of 9.9x and EV/EBITDA multiple of 4.9x its FY2024E estimates.

Apollo Tyres Limited's (ATL's) Q1FY23 results exceeded expectations driven by better-than-expected EBITDA margin expansion, with consolidated revenues, EBITDA, and PAT growing by 6.5% q-o-q, 10.1% q-o-q, and 67.9% q-o-q respectively. Consolidated revenue grew by 29.6% y-o-y to Rs5,942 crore, driven by double-digit volume growth in both, Indian and Europe business verticals, and price hikes taken by the company during the year. Consolidated EBITDA margin for Q1 stood at 11.6%, expanding 40bps q-o-q, led by improving product mix, positive operating leverage, and costs reductions. EBITDA and PAT grew by 21.7% y-o-y and 49.2% y-o-y to Rs690 crore and Rs191 crore respectively. Standalone EBITDA margin improved 20bps q-o-q to 9.7%, led by cost reductions and price hikes, partially mitigated by input cost inflation. EBIT margin for Europe business remain flat q-o-q to 4.9%, while EBIT margin for Asian region expanded 70bps q-o-q to 4.8%. We continue to maintain our positive stance on ATL and believe it is well positioned to leverage market opportunities in India and abroad. ATL has been able to pass on the costs to its retail as well as OEM customers very comfortably while maintaining its robust revenue growth. We remain positive about the company's growth prospects and expect it to benefit from its strategy of deleveraging its balance sheet, improving operating leverage, and focusing on firm capital allocation and cash management going forward. Strong growth coupled with a leadership position in key markets and segments is likely to help ATL to achieve its long-term targets of $5 billion by FY2026.

Key positives

- Business continues to increase across geographies, with Indian revenues up 37.8% y-o-y and European revenues up by 13.8% y-o-y. Both the key regions continued to witness double-digit volume growth.
- In Q1FY23, the company took 8% price hikes for the domestic replacement market and 6-9% price hikes in the European passenger car market.
- ATL continues to gain market share across (PCLT, TBR, and OHT) segments in Europe, with a share of UHP/UUHP tyres in the sales mix improving to ~41% in Q1FY23 from 38% in Q1FY22.
- Consolidated EBITDA margin for Q1 stood at 11.6%, expanding 40bps q-o-q, led by improving product mix, positive operating leverage, and costs reductions.

Key negatives

- Shortage of semiconductors impacting passenger vehicle demand, while weakness in agriculture segment impacted tyre sales.
- Consolidated gross margins increased 10bps q-o-q to 39.7%, driven by an increase in raw material prices.

Management Commentary

- The management has maintained 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.
- The company maintains its Capex for FY23 at Rs900 crore for Indian business and Euro 40mn for European facilities. The CAPEX is largely allocated towards de-bottlenecking existing capacities, digitalization and judicious brownfield expansions. ATL's capacity utilization during Q1FY23 was 81% for India facilities and 88% for European facilities.
- Raw material prices are expected to remain stable and start softening from Q3FY23 onwards. The company would most likely take pricing action to mitigate any rise in raw material costs.

Our Call

Valuation – Maintain Buy rating with an unchanged PT of Rs.303: 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 utilization, and focusing on firm capital allocation and cash management in the near 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 9.9x and an EV/EBITDA multiple of 4.9x its FY2024E estimates. We retain our Buy rating on the stock with an unchanged PT of Rs303.

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.

Valuations (Consolidated) Rs cr

Particulars	FY21	FY22	FY23E	FY24E
Revenues	17,376	20,948	23,981	26,813
Growth (%)	6.4	20.6	14.5	11.8
EBIDTA	2,777	2,574	3,245	3,799
OPM (%)	16.0	12.3	13.5	14.2
Adjusted PAT	958	644	1,182	1,601
% YoY growth	101.1	(32.7)	83.4	35.5
Adjusted EPS (Rs)	15.1	10.1	18.6	25.2
P/E (x)	16.6	24.6	13.4	9.9
P/B (x)	1.5	1.4	1.3	1.2
EV/EBITDA (x)	6.7	7.3	5.8	4.9
RoE (%)	9.3	5.9	10.2	12.6
RoCE (%)	7.8	5.4	7.7	9.6

Source: Company; Sharekhan estimates

Q1FY23 results beat expectations: Apollo Tyres Limited's (ATL's) Q1FY23 results exceeded expectations driven by better-than-expected EBITDA margin expansion, with consolidated revenue, EBITDA, and PAT growing by 6.5% q-o-q, 10.1% q-o-q and 67.9% q-o-q respectively. Consolidated revenue grew by 29.6% y-o-y to Rs5,942 crore, driven by double-digit volume growth in both, Indian and Europe business verticals, and price hikes taken by the company during the year. Business continues to increase across geographies, with Indian revenues up 37.8% y-o-y and European revenues up by 13.8% y-o-y. Both the key regions continued to witness double-digit volume growth. ATL continues to gain market share across (PCLT, TBR and OHT) segments in Europe, with a share of UHP/UUHP tyres in the sales mix improving to ~41% in Q1FY23 from 38% in Q1FY22. In Q1FY23, the company took 8% price hikes for the domestic replacement market and 6-9% price hikes in the European passenger car market. Consolidated EBITDA margin for Q1 stood at 11.6%, expanding 40bps q-o-q, led by improving product mix, positive operating leverage, and cost reductions. EBITDA and PAT grew by 21.7% y-o-y and 49.2% y-o-y to Rs690 crore and Rs191 crore respectively. Standalone EBITDA margin improved 20bps q-o-q to 9.7%, led by cost reductions and price hikes, partially mitigated by input cost inflation. EBIT margin for Europe business remain flat q-o-q to 4.9%, while EBIT margin for Asian region expanded 70bps q-o-q to 4.8%.

Market share gains: The company has a leadership position in the truck and bus segment, which is the largest market segment in the country. In addition, the company holds the top position in the passenger vehicle segment. ATL has improved its market share across the segments in Europe markets. It has expanded its distribution footprint significantly over the last two years, with increasing touchpoints in rural markets by more than four times. The Vredestein brand continues to hold its dominant position in the fast-growing PCLT segment in Europe. The company is gaining a share in focused categories such as UHP/UUHP PCR, TBR, agri in the overseas markets.

Increase in share of UHP/UUHP segments: ATL is focussing 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 has increased its share of premium UHP and UUHP tyres to ~41% in Q1FY23 from 38% in Q1FY22.

Positive outlook: The management remains positive on the business outlook, though the company highlighted a few challenges such as chips shortage, geo-political tension, and raw material inflation going forward. The management has maintained 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. 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, digitalization and judicious brownfield expansions. ATL's capacity utilization during Q1FY23 are at 81% for India facilities and 88% for Europe facilities. Pricing remains stable and the company would most likely take pricing action to mitigate the rise in raw material costs.

Management remains committed to achieving long-term goals: The management remains committed to long-term targets to achieve revenue of $5 billion by FY2026, EBITDA margins of at least 15%, ROCE of 12-15%, and net debt to EBITDA of less than 2x. ATL's management was confident of achieving targets, as the company is well-positioned to enter into the growth phase through optimising processes and delivering differentiating products. The company has made significant investments in building brand, plant infrastructure, distribution, and R&D capability over the past decade. The Management reiterated that the company will continue to focus on core and profitable business. The near-term focus will be on increasing business through product differentiation, enhancing penetration in new markets (both domestic and exports), investments in brand building, R&D, and ramping up capacity. Key drivers for improving margins would be increasing share of premium products, cost control, rationalization, thrust on digitisation, rationalization of raw material sourcing, and focus on FCF, capex, and balance sheet. The company has also discussed its efforts on raising focus on sustainability, technology and innovation.

Results (Consolidated) Rs cr

Particulars	Q1FY23	Q1FY22	% YoY	Q4FY22	% QoQ
Revenue	5,942	4,584	29.6	5,578	6.5
Total Expenses	5,252	4,018	30.7	4,952	6.1
EBITDA	690	567	21.7	626	10.1
Depreciation	344	340	1.0	375	(8.4)
Interest	118	105	13.1	128	(7.6)
PBT	238	161	47.8	160	48.8
Tax	48	34	42.3	47	2.2
Share Of profit from Associates	0	0	NA	0	NA
Reported PAT	191	128	49.2	114	67.9
Adj Net Profit	191	128	49.2	114	67.9
Adjusted EPS (Rs)	3.0	2.0	49.2	1.8	67.9

Source: Company; Sharekhan Research

Key Ratios (Consolidated)

Particulars	Q1FY23	Q1FY22	YoY (bps)	Q4FY22	QoQ (bps)
Gross margin (%)	39.7	42.8	(310)	39.8	(10)
EBIDTA margin (%)	11.6	12.4	(80)	11.2	40
EBIT margin (%)	5.8	4.9	90	4.5	130
Net profit margin (%)	3.2	2.8	40	2.0	120
Effective tax rate (%)	20.0	20.8	(80)	29.2	(910)

Source: Company; Sharekhan Research

Results (Standalone) Rs cr

Particulars	Q1FY23	Q1FY22	% YoY	Q4FY22	% QoQ
Revenue	4,436	3,220	37.8	3,988	11.2
Total Expenses	4,007	2,886	38.8	3,612	10.9
EBITDA	429	334	28.6	376	14.0
Depreciation	344	340	1.0	375	(8.4)
Interest	118	105	13.1	128	(7.6)
PBT	136	89	53.4	72	88.1
Tax	32	21	52.7	18	76.1
Reported PAT	104	68	53.6	54	92.2
Adj Net Profit	104	68	53.6	54	92.2
Adjusted EPS (Rs)	1.6	1.1	53.6	0.9	92.2

Source: Company; Sharekhan Research

Key Ratios (Standalone)

Particulars	Q1FY23	Q1FY22	YoY (bps)	Q4FY22	QoQ (bps)
Gross margin (%)	29.6	34.2	(450)	30.6	(100)
EBIDTA margin (%)	9.7	10.4	(70)	9.4	20
EBIT margin (%)	1.9	(0.2)	NA	0.0	190
Net profit margin (%)	2.4	2.1	20	1.4	100
Effective tax rate (%)	23.5	23.6	(10)	25.1	(160)

Source: Company; Sharekhan Research

Outlook and Valuation

Sector View – 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.

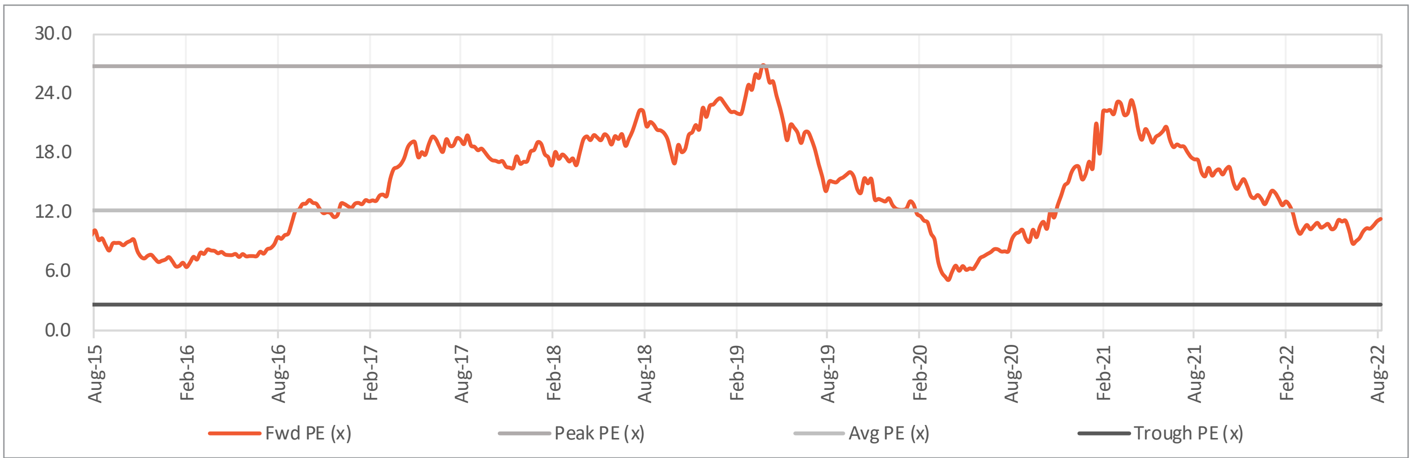
Company Outlook – Convincing strategy to achieve a profitable growth model

The management has laid down its long-term targets to achieve revenue of US$5 billion by FY2026, an 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 an expected recovery in volumes post normalization of economic activities. The overseas business is expected to do well because of a richer product mix and gradual capacity additions.

Valuation – Maintain Buy rating with an unchanged PT of Rs.303

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 near 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 9.9x and EV/EBITDA multiple of 4.9x its FY2024E estimates. We retain our Buy rating on the stock with an unchanged PT of Rs303.

One-year forward P/E (x) band



Source: Sharekhan Research

Peer Comparison

Particulars	CMP (Rs / Share)	P/E (x)			EV/EBITDA (x)			RoCE (%)		
		FY22	FY23E	FY24E	FY22	FY23E	FY24E	FY22	FY23E	FY24E
Apollo Tyres	250	24.6	13.4	9.9	7.3	5.8	4.9	5.4	7.7	9.6
Balkrishna Industries	2,207	30.2	26.0	20.7	22.5	18.2	15.0	25.3	24.4	25.8

Source: Company, Sharekhan estimates

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 the 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 a strong brand, R&D, technology, and distribution network. In addition, the company will operationally improve its margin, aided by specialization of Dutch plant (through a significant uptick in cost competitiveness, given ramping up production in Hungary); cost reductions through digitalization 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 the INR-Euro pair would impact its financial performance.

Additional Data

Key management personnel

Onkar Singh Kanwar	Chairman & Managing Director
Mr Neeraj Kanwar	Vice Chairman & Managing Director
Sunam Sarkar	President & 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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Registered Office: Sharekhan Limited, The Ruby, 18th Floor, 29 Senapati Bapat Marg, Dadar (West), Mumbai – 400 028, Maharashtra, INDIA, Tel: 022 - 67502000/ Fax: 022 - 24327343. Sharekhan Ltd.: SEBI Regn. Nos.: BSE / NSE / MSEI (CASH / F&O / CD) / MCX - Commodity: INZ000171337; DP: NSDL/CDSL-IN-DP-365-2018; PMS: INP000005786; Mutual Fund: ARN 20669; Research Analyst: INH000006183.