

AMARA RAJA BATTERIES

Strong auto volumes; weak industrial drags margin

India Equity Research | Automobiles

Amara Raja Batteries' (AMRJ) Q4FY18 sales jumped 18% YoY led by strong ~30% spurt in the auto segment. Slowdown in telecom dragged overall industrial volumes (down ~2-3% YoY). AMRJ hiked prices ~5% in the auto segment to combat rising lead prices. However, it faced pricing pressure in the industrial segment, leading to OPM margin falling 230bps QoQ to 13.3% (5% below estimate). We expect uptick in the auto segment to sustain led by market share shift to organised players, deeper OEM penetration, scale up in home UPS batteries, opportunities in emerging applications & capacity addition across segments. Hence, we estimate 22% PAT CAGR over FY18-20. Maintain 'BUY' with TP INR1,013 (25x FY20E EPS).

Strong growth in auto; telecom drags industrial

Sales grew 18% YoY led by robust ~30% YoY spurt in the auto segment on account of strong volume surge of ~25% YoY, driven by four wheelers (~up 25%), two wheelers (~32%) and home UPS & tubular batteries (up ~22%). The company expects the volume growth momentum in the auto segment to sustain in FY19. While volume in industrial UPS was healthy, slowdown in telecom led to ~2-3% YoY dip in the industrial segment's volumes. On the realisation front, pricing challenges remained in the industrial segment. AMRJ's market share in telecom has dipped to ~50% from ~60%. EBITDA margin fell 230bps QoQ to 13.3% leading to EBITDA growth of ~14% YoY. FY18 revenue grew ~14% led by ~31% YoY growth in auto. Industrials remained subdued with overall volume down ~8-9% led by ~10% dip in telecom volume. Management has guided for margin to sustain at 14-16% (versus 14.6% in FY18). Softening lead price (down ~5% in 1MQ1FY19) creates a buffer, though partially mitigated by INR/USD appreciation.

Key growth drivers

We expect growth to be led by: i) demand shift to organised players post GST, aiding spurt in replacement market; ii) cyclical upturn in auto OEM sales across categories iii) anticipated demand uptick in telecom (volumes were stable QoQ for the past two quarters), iv) scale up in home UPS batteries, v) opportunities in emerging applications such as e-rickshaws; and vi) robust capacity additions to meet increased demand.

Outlook and valuations: Positive; maintain 'BUY'

Led by sustained growth in the auto segment, scale up in home UPS batteries and potential opportunities in emerging applications, we estimate 22% PAT CAGR over FY18-20. Maintain 'BUY' with TP of INR1,013. At CMP, the stock trades at 19.8x FY20 EPS.

Financials

Year to March	Q4FY18	Q4FY17	% change	Q3FY18	% change	FY18	FY19E	FY20E
Net revenues	15,807	13,445	17.6	15,535	1.8	60,585	69,699	78,654
EBITDA	2,107	1,844	14.3	2,416	(12.8)	8,823	10,582	12,446
Adj. net profit	1,098	992	10.7	1,345	(18.3)	4,688	5,606	6,924
Dil. EPS (INR)	6.4	5.8	10.7	7.9	(18.3)	27.4	32.8	40.5
Diluted PE (x)							24.4	19.8
EV/EBITDA (x)							12.6	10.4
ROE (%)							17.5	18.6

Edelweiss Research is also available on www.edelresearch.com, Bloomberg EDEL <GO>, Thomson First Call, Reuters and Factset.

EDELWEISS RATINGS	
Absolute Rating	BUY
Investment Characteristics	Growth

MARKET DATA (R: AMAR.BO, B: AMRJ IN)	
CMP	: INR 832
Target Price	: INR 1,013
52-week range (INR)	: 935 / 665
Share in issue (mn)	: 170.8
M cap (INR bn/USD mn)	: 142 / 2,188
Avg. Daily Vol. BSE/NSE ('000)	: 579.4

SHARE HOLDING PATTERN (%)			
	Current	Q3FY18	Q2FY18
Promoters *	52.1	52.1	52.1
MF's, FI's & BKs	11.3	13.1	12.1
FII's	19.0	16.7	17.9
Others	17.7	18.2	17.9
* Promoters pledged shares (% of share in issue)	:		NIL

PRICE PERFORMANCE (%)			
	BSE Midcap Index	Stock	Stock over Index
1 month	(5.2)	(2.0)	3.2
3 months	(4.3)	2.0	6.2
12 months	7.8	(8.8)	(16.6)

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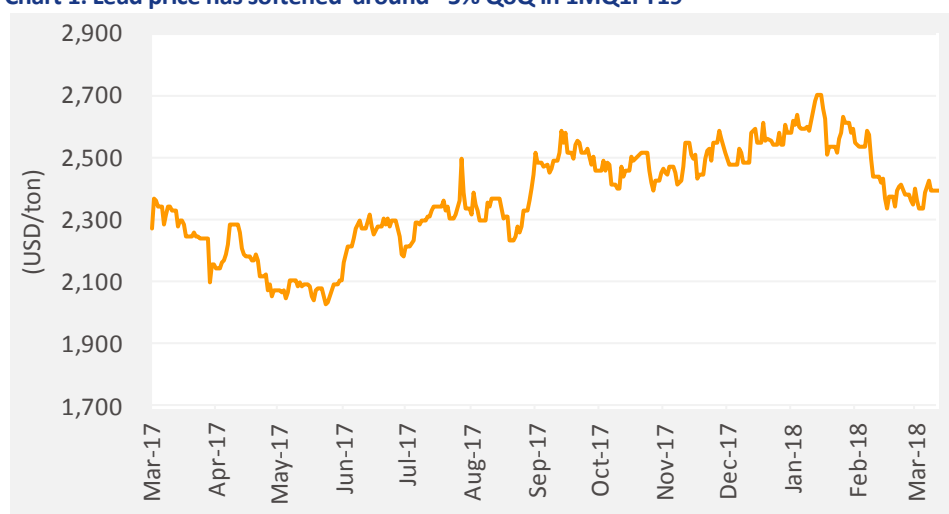
May 18, 2018

Q4FY18: Key highlights

- The INR15.8bn revenue, in line with our estimate, grew 18% YoY after a similar growth rate in Q3FY18. FY18 revenue grew ~14% YoY.
- **Automotive division**
 - Automotive battery business achieved strong volume growth of ~25% YoY in Q4FY18 helped by buoyant auto sector growth and healthy demand in the replacement market in passenger cars as well as motor cycles. On the realisation front, the company effected price hike of 5-6% and has almost fully passed on the spike in lead prices. Overall growth in the automotive segment stood at ~30% YoY, in value terms.
 - Within automotive, four wheelers grew ~25% YoY, two wheelers ~32% and others (home UPS, Tubular batteries, etc) ~22% YoY.
 - AMARON and POWER ZONE brands continued to perform exceptionally well with increased market reach and strong consumer preference. The company is anticipating traction in the replacement market with shift from unorganised to organised players post GST implementation.
 - FY18 volumes in four wheelers grew ~15% YoY, two wheelers ~18% and others (home UPS, tubular batteries, etc.) ~40%. The company had taken price hikes to offset the impact of ~15-16% spike in lead prices in FY18. In value terms, the overall automotive segment grew ~31%. Management expects volume growth in the automotive segment to continue to be healthy in FY19.
- **Industrial division**
 - Industrial battery business witnessed muted demand growth as a result of consolidation in the telecom industry. However, volume growth across UPS and railway segments was healthy and helped increase market share in these segments.
 - On volume basis, the overall segment saw a dip of 2-3% YoY. The company continued to see pricing challenges and hence was not able to pass on the spike in lead prices.
 - The telecom battery industry continues to largely dominated by three players (AMJ, Exide and HBL), accounting for ~80-85% of the organised segment. Currently, AMRJ holds ~50% market share (down from ~60%).
 - For FY18, overall industrial volumes dipped ~8-9% YoY led by ~10% YoY dip in telecom volumes. Management highlighted that it sees stability in telecom volumes on a sequential basis and expects volume from this segment to pick up from Q4FY19.
- **Margin and pricing**
 - Gross margin fell marginally to 31.3% in the current quarter. EBITDA margin also remained largely flat at ~13.4% (13.7% in Q4FY17 & 15.6% in Q3FY18) leading to EBITDA growth of 14% YoY (5% below our estimate). For FY18, EBITDA margin dipped ~150bps to ~14.6% leading to EBITDA growth of mere 4% YoY.

- Management has guided to maintain margin in the range of 14-16% depending on movement in lead price.
 - While lead price, which had spike sharply in FY18 (up ~17% YoY), is softening (down ~5% 1MQ1FY19), its positive impact has been partially mitigated by INR/USD appreciation. While lead price volatility is a cause of concern, the company can offset it by pricing actions.
 - PAT grew by 11% YoY (~7% below estimate) to INR1.1bn on account of higher effective tax rate. For FY18, PAT dipped marginally by 2%.
- **Capex and capacity addition**
 - Of the 14mn units planned capacity addition in two wheelers, first phase of 4mn units (11mn currently) has been commissioned, taking the total installed capacity to 15mn units and the second phase is commencing in Q1FY19. The company did a capex of ~INR4bn in FY18 and plans to invest another ~INR4bn in FY19.
 - AMRJ recently added 2.25mn units capacity in four wheelers, taking capacity to 10.5mn units; it will add further 1.5-2 mn units in FY19.
 - The company has around ~80,000 units per month of capacity in home UPS segment and it is currently operating at ~85-90% utilization. It has plans of expanding capacity in this segment.
 - **Others**
 - Management is working on a pilot project for e-rickshaws and e-bus. However, it is not investing in the project currently and will build capacity at an appropriate time.
 - The management highlighted that it still does not see significant capex commitment from auto OEMs in the EV segment.

Chart 1: Lead price has softened around ~5% QoQ in 1MQ1FY19



Source: Company, Edelweiss research

Automobiles

Financial snapshot

(INR mn)

Year to March	Q4FY18	Q4FY17	% change	Q3FY18	% change	FY18	FY19E	FY20E
Net revenues	15,807	13,445	17.6	15,535	1.8	60,585	69,699	78,654
Dec/(inc) in stock	(50)	(471)	NA	(879)	NA			
Raw material	10,434	9,349	11.6	10,867	(4.0)	40,002	46,406	52,379
Purchase of finished goods	483	266	81.2	402	20.2	1,160	695	481
Staff costs	783	705	11.0	758	3.3	3,090	3,485	3,854
Other expenses	2,051	1,752	17.1	1,972	4.0	7,510	8,531	9,494
Total expenditure	13,700	11,601	18.1	13,119	4.4	51,762	59,117	66,208
EBITDA	2,107	1,844	14.3	2,416	(12.8)	8,823	10,582	12,446
Depreciation	588	499	17.9	587	0.2	2,303	2,663	2,982
EBIT	1,519	1,345	13.0	1,828	(16.9)	6,520	7,919	9,464
Interest	13	15	(12.7)	11	15.9	47	32	21
Other income	237	151	57.4	168	41.3	646	626	1,071
Add: Prior period items								
Profit before tax	1,743	1,480	17.7	1,985	(12.2)	7,119	8,513	10,515
Provision for taxes	645	489	32.0	640	0.7	2,431	2,907	3,591
Minority interest								
Associate profit share								
Add: Exceptional items								
Profit- Discontinued Ops								
Reported net profit	1,098	992	10.7	1,345	(18.3)	4,688	5,606	6,924
Adjusted Profit	1,098	992	10.7	1,345	(18.3)	4,688	5,606	6,924
Diluted shares (mn)	171	171		171		171	171	171
Reported EPS (INR)	6.4	5.8	10.7	7.9	(18.3)	27.4	32.8	40.5
Adjusted Diluted EPS	6.4	5.8	10.7	7.9	(18.3)	27.4	32.8	40.5
Diluted P/E (x)						29.2	24.4	19.8
EV/EBITDA (x)						15.4	12.6	10.4
ROAE (%)						16.8	17.5	18.6
Raw material	68.7	68.0		66.9		66.0	66.6	66.6
Employee cost	5.0	5.2		4.9		5.1	5.0	4.9
Other expenses	13.0	13.0		12.7		12.4	12.2	12.1
EBITDA	13.3	13.7		15.6		14.6	15.2	15.8
Adjusted net profit	6.9	7.4		8.7		7.7	8.0	8.8
Tax rate	37.0	33.0		32.3		34.1	34.1	34.1

Company Description

AMRJ is the second largest automotive battery manufacturer and the largest supplier of industrial storage batteries in India. It is a joint venture between the Galla family and US based Johnson Control (JCI) with 26% each. JCI, the global leader in lead-acid automotive batteries and advanced batteries for start-stop, hybrid and electric vehicles, provides technical support to AMRJ. The company has been a technology leader in the Indian market, having introduced VRLA (valve-regulated lead acid) batteries for the first time for industrial applications and two wheelers. In the automotive segment too, AMRJ was first to introduce batteries with five-year warranties and zero maintenance fully charged batteries. Its business model is derisked as it caters to automotive as well as industrial segments. Sales are well diversified among automotive and industrial segments at 60% and 40%, respectively.

Investment Theme

Having established its strong foothold in the auto replacement space, the company is increasing its capacity in OEMs by 47% in 4-wheelers and 75% in 2-wheelers, which will provide the scale and operational efficiency. Also company is expanding capacity by 32% in telecom segment and 100% in UPS segment which will set a base to capture industrial growth over next three years.

Key Risks

Prolonged slowdown in OEM

Ongoing slowdown in OEM sales starting FY12 could last till FY14. The current weakness in auto OEM sales has raised concerns on auto replacement growth starting FY16 (3.0-3.5% year replacement cycle). We note that first-time replacement accounts for only about ~45% of total replacement demand for auto batteries. Thus, overall replacement battery demand could slowdown, but to a lesser extent. However, a prolonged slowdown in OEM can impact the industry's and AMRJ's growth.

Increased competition

The battery space could get competitive in the future; there are a number of players vying to be a credible No. 3 in the next two-three years.

Exit of Johnson Controls

Johnson Controls which has 26% stake in AMRJ brings technology advantage with 36% share globally. Thereby, the exit of JCI could be a risk for further innovation.

Financial Statements

Key Assumptions

Year to March	FY17	FY18	FY19E	FY20E
Macro				
GDP(Y-o-Y %)	6.6	6.5	7.1	7.6
Inflation (Avg)	4.5	3.8	4.5	5.0
Repo rate (exit rate)	6.3	6.0	6.0	6.5
USD/INR (Avg)	67.1	64.5	66.0	66.0
Company				
Raw Material (% net rev)	65.6	67.9	67.6	67.2
Capacity (mn units)				
4W	10.5	10.5	10.5	10.5
2W	10.8	15.0	15.0	15.0
Medium VRLA (UPS)	4.3	4.9	5.5	6.1
Large VRLA (Telecom)	1,200.0	1,440.0	1,728.0	2,073.6
4W OEM	43	44	47	49
2W OEM	16	17	18	20
4W Replacement	34	36	38	40
2W Replacement	32	33	34	34
Medium VRLA (UPS)	42	42	42	42
Large VRLA (Telecom)	61	55	57	58
4W OEM	10.6	11.6	11.8	12.0
2W OEM	2.1	2.4	2.6	2.7
4W Replacement	28.7	30.9	31.4	31.9
2W Replacement	7.6	8.4	8.5	8.7
Trading	0.8	1.0	1.0	0.9
Auto	49.8	54.3	55.3	56.3
Medium VRLA (UPS)	12.3	11.8	10.9	10.3
Large VRLA (Telecom)	24.9	18.6	17.4	16.2
Railway and Others	4.9	4.7	4.6	4.8
Industrial	49.5	45.0	44.0	43.0
Trade batteries	2.7	1.4	0.7	0.3
Trade Home UPS	0.5	0.5	0.3	0.3
Cost assumptions				
Other exp (% net rev)	18.4	17.5	17.2	17.0
Depreciation rate (%)	11.6	11.3	11.1	11.0
Dividend payout (%)	17.4	18.0	811.0	18.0
Tax rate (%)	31.9	34.1	34.1	34.1
Capex (INR mn)	(5,415)	(5,415)	(4,000)	(4,000)

Income statement

(INR mn)

Year to March	FY17	FY18	FY19E	FY20E
Income from operations	53,172	60,585	69,699	78,654
Materials costs	34,885	41,162	47,101	52,861
Manufacturing expenses	2,605	2,787	3,136	3,461
Employee costs	2,778	3,090	3,485	3,854
Administration expenses	1,382	1,484	1,673	1,848
Selling & Advt. exp	3,022	3,238	3,722	4,184
Total operating expenses	44,672	51,762	59,117	66,208
EBITDA	8,499	8,823	10,582	12,446
Depreciation	1,912	2,303	2,663	2,982
EBIT	6,587	6,520	7,919	9,464
Less: Interest Expense	58	47	32	21
Add: Other income	492.4	645.95	625.78	1,071.32
Profit Before Tax	7,022	7,119	8,513	10,515
Less: Provision for Tax	2,237	2,431	2,907	3,591
Reported Profit	4,785	4,688	5,606	6,924
Adjusted Profit	4,785	4,688	5,606	6,924
Shares o/s (mn)	171	171	171	171
Adjusted Basic EPS	28.0	27.4	32.8	40.5
Diluted shares o/s (mn)	171	171	171	171
Adjusted Diluted EPS	28.0	27.4	32.8	40.5
Adjusted Cash EPS	39.2	40.9	48.4	58.0
Dividend per share (DPS)	4.2	4.2	5.0	6.2
Dividend Payout Ratio(%)	17.4	18.0	18.0	18.0

Common size metrics

Year to March	FY17	FY18	FY19E	FY20E
Materials costs	65.6	67.9	67.6	67.2
Administration expenses	2.6	2.5	2.4	2.4
Operating expenses	84.0	85.4	84.8	84.2
Depreciation	3.6	3.8	3.8	3.8
EBITDA margins	16.0	14.6	15.2	15.8
Interest Expense	0.1	0.1	-	-
Net Profit margins	9.0	7.7	8.0	8.8

Growth ratios (%)

Year to March	FY17	FY18	FY19E	FY20E
Revenues	15.1	13.9	15.0	12.8
EBITDA	3.3	3.8	19.9	17.6
PBT	(2.8)	1.4	19.6	23.5
Adjusted Profit	(2.7)	(2.0)	19.6	23.5
EPS	(2.7)	(2.0)	19.6	23.5

Balance sheet		(INR mn)			
As on 31st March	FY17	FY18	FY19E	FY20E	
Share capital	171	171	171	171	
Reserves & Surplus	25,760	29,604	34,201	39,879	
Shareholders' funds	25,931	29,775	34,372	40,049	
Long term borrowings	690	584	284	284	
Total Borrowings	690	584	284	284	
Long Term Liabilities	404	452	452	452	
Deferred revenue	815	719	719	719	
Sources of funds	27,840	31,530	35,827	41,505	
Gross Block	18,104	22,538	25,538	28,538	
Net Block	14,870	17,001	17,338	17,356	
Capital work in progress	2,403	2,264	3,264	4,264	
Intangible Assets	51	32	32	32	
Total Fixed Assets	17,324	19,297	20,634	21,652	
Non current investments	189	198	198	198	
Cash and Equivalents	2,987	2,132	4,385	7,359	
Inventories	8,170	10,497	9,535	10,763	
Sundry Debtors	5,705	7,825	8,020	9,051	
Loans & Advances	134	144	144	144	
Other Current Assets	1,338	1,835	1,835	1,835	
Current Assets (ex cash)	15,346	20,301	19,535	21,792	
Trade payable	4,184	5,923	4,450	5,023	
Other Current Liab	3,821	4,475	4,475	4,475	
Total Current Liab	8,006	10,398	8,925	9,498	
Net Curr Assets-ex cash	7,340	9,903	10,610	12,295	
Uses of funds	27,840	31,530	35,827	41,505	
BVPS (INR)	151.8	174.3	201.2	234.5	

Free cash flow		(INR mn)			
Year to March	FY17	FY18	FY19E	FY20E	
Reported Profit	4,785	4,688	5,606	6,924	
Add: Depreciation	1,912	2,303	2,663	2,982	
Interest (Net of Tax)	39	32	22	14	
Others	(69)	(127)	(22)	(14)	
Less: Changes in WC	(1,137)	(2,586)	(707)	(1,685)	
Operating cash flow	5,529	4,310	7,562	8,221	
Less: Capex	5,415	5,415	4,000	4,000	
Free Cash Flow	114	(1,105)	3,562	4,221	

Cash flow metrics				
Year to March	FY17	FY18	FY19E	FY20E
Operating cash flow	5,529	4,310	7,562	8,221
Financing cash flow	(20)	(950)	(1,309)	(1,246)
Investing cash flow	(5,349)	(5,415)	(4,000)	(4,000)
Net cash Flow	160	(2,055)	2,253	2,974
Capex	(5,415)	(5,415)	(4,000)	(4,000)
Dividend paid	-	(844)	(1,009)	(1,246)

Profitability and efficiency ratios				
Year to March	FY17	FY18	FY19E	FY20E
ROACE (%)	29.2	25.2	26.3	28.1
ROAE (%)	20.3	16.8	17.5	18.6
Inventory Days	74	83	78	70
Debtors Days	40	41	41	40
Payable Days	40	45	40	33
Cash Conversion Cycle	74	79	79	77
Current Ratio	2.3	2.2	2.7	3.1
Gross Debt/EBITDA	0.1	0.1	-	-
Gross Debt/Equity	-	-	-	-
Adjusted Debt/Equity	-	-	-	-
Interest Coverage Ratio	114.2	138.3	246.4	456.0

Operating ratios				
Year to March	FY17	FY18	FY19E	FY20E
Total Asset Turnover	2.1	2.0	2.1	2.0
Fixed Asset Turnover	3.7	3.8	4.1	4.5
Equity Turnover	2.3	2.2	2.2	2.1

Valuation parameters				
Year to March	FY17	FY18	FY19E	FY20E
Adj. Diluted EPS (INR)	28.0	27.4	32.8	40.5
Y-o-Y growth (%)	(2.7)	(2.0)	19.6	23.5
Adjusted Cash EPS (INR)	39.2	40.9	48.4	58.0
Diluted P/E (x)	28.6	29.2	24.4	19.8
P/B (x)	5.5	4.8	4.1	3.5
EV / Sales (x)	2.5	2.2	1.9	1.7
EV / EBITDA (x)	15.9	15.4	12.6	10.4
Dividend Yield (%)	0.5	0.5	0.6	0.7

Peer comparison valuation

Name	Market cap (USD mn)	Diluted P/E (X)		EV / EBITDA (X)		ROAE (%)	
		FY19E	FY20E	FY19E	FY20E	FY19E	FY20E
Amara Raja Batteries	2,188	25.3	20.5	13.0	10.8	17.5	18.6
Exide Industries	3,237	25.2	21.3	13.7	11.8	14.7	15.4
Median	-	25.3	20.9	13.4	11.3	16.1	17.0
AVERAGE	-	25.3	20.9	13.4	11.3	16.1	17.0

Source: Edelweiss research

Additional Data

Directors Data

Dr Ramchandra Galla	Chairman	Jaydev Galla	Vice Chairman & Managing Director
Raphael John Shemanski	Non Executive Director	Nagarjun Valluripalli	Non Executive Independent Director
N Sri Vishnu Raju	Non Executive Independent Director	T R Narayanaswamy	Non Executive Independent Director
Bhairavi Tushar Jani	Non Executive Independent Director	Trent Moore Nevill	Non Executive Director

Auditors - Deloitte Haskins & Sells LLP

**as per last available data*

Holding Top -10

	Perc. Holding		Perc. Holding
NALANDA INDIA EQUITY FUND	5.14	WASATCH ADVISORS INC	1.94
FRANKLIN TEMPLETON ASSET MANAGEMENT	2.58	BARON CAPITAL INC	1.23
RELIANCE CAPITAL TRUSTEE CO LTD	2.48	UTI ASSET MANAGEMENT CO LTD	1.20
ICICI PRUDENTIAL ASSET MGMT CO	2.44	JO HAMBRO CAPITAL MANAGEMENT	1.09
CAPITAL GROUP COMPANIES INC	2.39	KOTAK MAHINDRA	0.84

**as per last available data*

Bulk Deals

Data	Acquired / Seller	B/S	Qty Traded	Price
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No Data Available

**as per last available data*

Insider Trades

Reporting Data	Acquired / Seller	B/S	Qty Traded
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No Data Available

**as per last available data*

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Coverage group(s) of stocks by primary analyst(s): Automobiles

Ashok Leyland, Amara Raja Batteries, Bajaj Auto, Ceat Ltd, Eicher Motors, Exide Industries, Hero MotoCorp, Minda Corporation, Mahindra & Mahindra Ltd, Maruti Suzuki India Ltd, Motherson Sumi Systems, Suprajit Engineering, Tata Motors Ltd

Recent Research

Date	Company	Title	Price (INR)	Recos
30-Dec-99	Bajaj Auto	Muted quarter; outlook improving; <i>Result Update</i>	2788	Hold
30-Dec-99	Automobiles (Speeds & Bumps)	Will they, won't they?; <i>Sector Update</i>		
30-Dec-99	Eicher Motors	In-line numbers; demand uptick to sustain; <i>Result Update</i>	30316	Buy

Distribution of Ratings / Market Cap

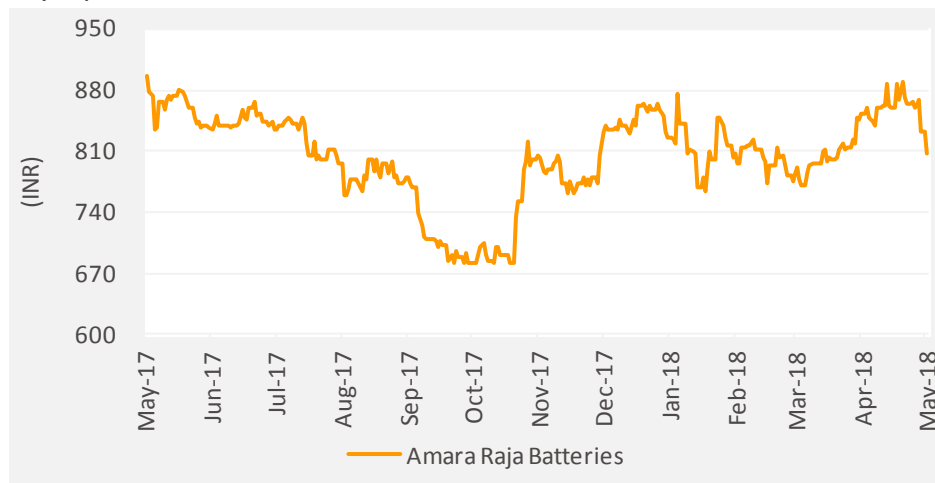
Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution*	161	67	11	240
* 1stocks under review				
	> 50bn	Between 10bn and 50 bn	< 10bn	
Market Cap (INR)	156	62	11	

Rating Interpretation

Rating	Expected to
Buy	appreciate more than 15% over a 12-month period
Hold	appreciate up to 15% over a 12-month period
Reduce	depreciate more than 5% over a 12-month period

One year price chart



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