

AMARA RAJA BATTERIES

Robust volumes across segments

India Equity Research | Automobiles

Amara Raja Batteries' (AMRJ) Q2FY19 sales jumped 23% YoY on robust auto and industrial volumes. On a low base, industrial grew a strong ~35% YoY led by telecom (up ~70% YoY and ~12% QoQ). Within auto, four wheelers grew ~19% YoY and two wheelers ~13%. While there is uncertainty on change of control at Johnson Control's power solution business, AMRJ highlighted that the association will continue and India will continue to be a key market. We envisage growth and profitability momentum to sustain led by: i) improving auto replacement cycle; ii) boost to industrials with telecom showing signs of improvement; and iii) soft lead price scenario (down 6-7% YoY in ongoing quarter). Hence, we estimate 16% PAT CAGR over FY18-20. Maintain 'BUY' with TP of INR928.

Industrial rebounds on a low base; auto healthy

Revenue grew ~23% YoY (Exide's 15%) driven by healthy volumes in industrial & automotive and 6-7% increase in realisation. Within auto, volume growth was healthy in four wheelers (up 19% YoY led by OEM growth of 20%, aftermarket 10-12% and exports 40%) and two wheelers (up 13% YoY led by aftermarket growth of 14-15% and 9% in OEM); while others (home UPS) were muted due to seasonality and lower capacity. Industrial volume growth was a strong ~35% YoY on a low base led by surge in telecom (up ~70% YoY and ~12% QoQ after multiple quarters of subdued growth), railways and UPS. Management expects telecom volumes to stabilise, while pricing pressure persists.

Higher input and others costs impact margin

In INR terms, lead was up 13-14% YoY in Q2FY19 due to INR depreciation. Consequently, AMRJ's gross margin fell ~220bps YoY to 30.9%. EBITDA margin dipped ~320bps YoY, on a high base, led by input cost, high employee and other expenses (higher freight and fuel) leading to flat EBITDA growth. However, gross margin jumped 242bps and EBITDA margin rose 111bps QoQ (versus Exide's Gross/EBITDA margin decline of 50/194bps QoQ, respectively). Management expects benefit of 6-7% softening in landed lead price to flow in Q3FY19. AMRJ reiterated margin guidance of 14-16% in coming quarters.

Outlook and valuations: Positive; maintain 'BUY'

Led by sustained growth in the auto replacement segment, scale up in home UPS batteries and potential rebound in telecom, we estimate 16% PAT CAGR over FY18-20. Maintain 'BUY' with TP of INR928. At CMP, the stock trades at 20.8x FY20E EPS.

Financials

(INR mn)

Year to March	Q2FY19	Q2FY18	% change	Q1FY19	% change	FY18	FY19E	FY20E
Net revenues	17,531	14,275	22.8	17,787	(1.4)	60,592	70,447	82,707
EBITDA	2,366	2,381	(0.6)	2,203	7.4	8,833	9,715	11,938
Adj. net profit	1,202	1,272	(5.5)	1,130	6.4	4,714	5,155	6,342
Dil. EPS (INR)	7.0	7.4	(5.5)	6.6	6.4	27.6	30.2	37.1
Diluted PE (x)							25.6	20.8
EV/EBITDA (x)							13.2	10.8
ROE (%)							16.3	17.6

EDELWEISS RATINGS

Absolute Rating	BUY
Investment Characteristics	Growth

MARKET DATA (R: AMAR.BO, B: AMRJ IN)

CMP	: INR 772
Target Price	: INR 928
52-week range (INR)	: 908 / 682
Share in issue (mn)	: 170.8
M cap (INR bn/USD mn)	: 132 / 1,813
Avg. Daily Vol. BSE/NSE ('000)	: 591.0

SHARE HOLDING PATTERN (%)

	Current	Q1FY19	Q4FY18
Promoters *	52.1	52.1	52.1
MF's, FI's & BKs	9.7	10.3	11.3
FII's	20.4	20.3	19.0
Others	17.8	17.3	17.7
* Promoters pledged shares (% of share in issue)	:		NIL

PRICE PERFORMANCE (%)

	BSE Midcap Index	Stock	Stock over Index
1 month	5.8	7.0	1.2
3 months	(8.6)	(5.7)	2.8
12 months	(11.3)	11.5	22.8

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Q2FY19: Key highlights

Revenue growth and margin

- Revenue at INR17.5bn (5% above our estimate) grew a strong 23% YoY after 19% YoY growth in Q1FY19. Revenue growth was driven by healthy volumes in industrial (~up 35% YoY) and automotive. Spike in lead price (up 13-14% YoY in INR terms) contributed 6-7% to overall revenue growth. For H1FY19 revenue growth came in at 21% YoY.
- In INR terms, lead was up 13-14% YoY in Q2FY19 due to INR depreciation. Consequently, gross margin contracted ~220bps YoY to 30.9% and EBITDA margin ~320bps leading to flat EBITDA (in line with estimate).
- EBITDA margin fell on account of gross margin contraction, higher employee (due to higher gratuity payout of INR70mn) and other expenses (due to higher primary and secondary freight cost on surge in fuel cost). For H1FY19, EBITDA margin contracted 180bps YoY leading to EBITDA growth of 6% YoY.
- Management sees 6-7% softening in landed price of lead in Q3FY19 and expects a significant portion of the benefit to flow in Q3FY19. Management reiterated margin guidance of 14-16%.
- PAT declined 5.5% YoY (in line with estimate) due to higher effective tax rate and operating margin contraction. For H1FY19, PAT grew 3% YoY.

Automotive segment

- Within auto, volume growth was healthy in four wheelers (up 19% YoY led by OEM growth of 20%, exports 40% and aftermarket 10-12%) and two wheelers (up 13% YoY led by OEM growth of 9% and aftermarket 14-15%), while others (home UPS) were muted.
- OEM platforms to which the company supplies in four wheeler did not see any demand slowdown.
- AMRJ has maintained market share in aftermarket across segments. It has not taken any price hike in the segment since Feb 2018.

Industrial segment

- Overall industrial volume growth was healthy at ~35% YoY on a favourable base as the base quarter was impacted by slowdown in telecom and other industrials.
- Within industrial, growth was broad based with surge in telecom, railways and UPS. Telecom grew strongly at ~70% YoY and ~12% QoQ. Management expects telecom volumes to sustain at 190-200mnAh while there is pricing pressure. Management highlighted that AMRJ has regained market share in telecom to around 50%.

Capital expenditure

- AMRJ has approved capex of INR5.4bn for FY19 towards deployment of advanced stamped grid technology, second punching line for two-wheeler battery plant in a phased manner and debottlenecking in MVRLA plant.
- Management has guided for capex of INR10-12bn over FY19 and FY20 (including maintenance capex of INR1.0-1.5bn p.a)

Table 1: Planned investments

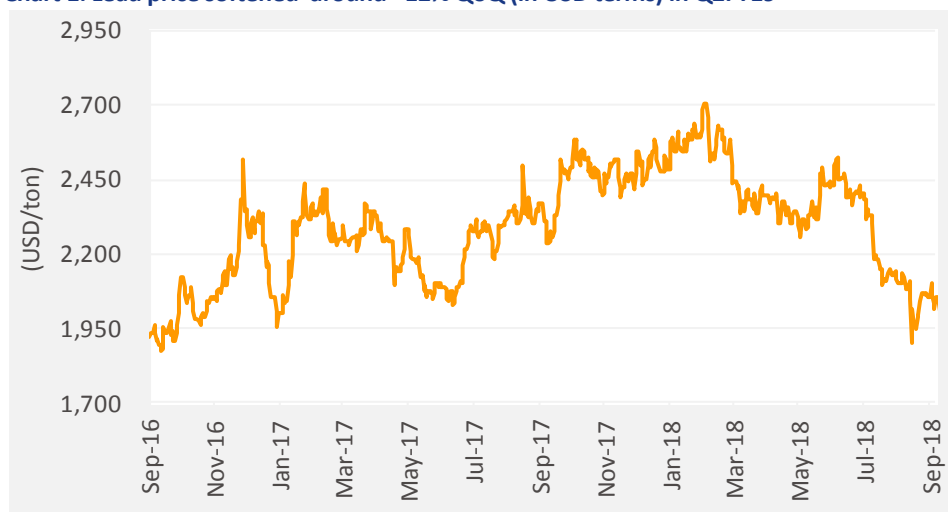
	FY19-20
Expansion of two wheelers	INR1.5bn
Expansion of four wheelers	~INR2bn in phase 1
Second punching line for two-wheeler battery plant	INR2bn
Central coil making plant (total capex - INR4.4bn)	INR2.5bn in phase 1
Maintenance Capex	INR1-1.5bn pa
Total capex	INR10-12bn

Source: Company

- AMRJ invested ~INR100mn in lithium ion pilot project. Pilot operations have commenced and no other investment is planned for now in this.

Johnson Control selling its power solution business

- As per a recent news articles, Johnson Controls is nearing a deal to sell its power solutions business, which makes car batteries, to Brookfield Asset Management for between USD13bn and USD14bn. While there is uncertainty over control of the business by an asset management company, AMRJ highlighted that the association between them will continue and India will continue to be a key market for Johnson Controls.

Chart 1: Lead price softened around ~12% QoQ (in USD terms) in Q2FY19

Source: Company, Edelweiss research

Automobiles

Financial snapshot

(INR mn)

Year to March	Q2FY19	Q2FY18	% change	Q1FY19	% change	YTD18	FY19E	FY20E
Net revenues	17,531	14,275	22.8	17,787	(1.4)	35,317	70,447	82,707
Dec/(inc) in stock	(426)	341	NA	141	NA	(285)	-	-
Raw material	12,163	8,642	40.7	11,812	3.0	23,975	46,630	55,018
Purchase of finished goods	374	437	(14.4)	766	(51.1)	1,140	1,879	1,690
Staff costs	928	742	25.2	843	10.2	1,771	3,522	4,053
Other expenses	2,125	1,732	22.7	2,023	5.0	4,148	8,700	10,008
Total expenditure	15,164	11,894	27.5	15,584	(2.7)	30,748	60,731	70,769
EBITDA	2,366	2,381	(0.6)	2,203	7.4	4,569	9,715	11,938
Depreciation	643	584	10.1	630	2.1	1,272	2,603	3,072
EBIT	1,724	1,797	(4.1)	1,573	9.6	3,297	7,112	8,867
Interest	18	13	45.6	15	22.1	33	46	30
Other income	142	122	16.4	137	3.9	280	486	484
Add: Prior period items								
Add: Exceptional items								
Profit before tax	1,848	1,907	(3.1)	1,695	9.0	3,543	7,553	9,321
Provision for taxes	646	635	1.7	565	14.3	1,211	2,398	2,978
Minority interest								
Associate profit share								
Profit- Discontinued Ops								
Reported net profit	1,202	1,272	(5.5)	1,130	6.4	2,333	5,155	6,342
Adjusted Profit	1,202	1,272	(5.5)	1,130	6.4	2,333	5,155	6,342
Diluted shares (mn)	171	171		171		171	171	171
Reported EPS (INR)	7.0	7.4		6.6		13.7	30.2	37.1
Adjusted Diluted EPS	7.0	7.4	(5.5)	6.6	6.4	13.7	30.2	37.1
Diluted P/E (x)							25.6	20.8
EV/EBITDA (x)							13.2	10.8
ROAE (%)							16.3	17.6
Raw material	69.1	66.0		71.5		67.9	66.2	66.5
Employee cost	5.3	5.2		4.7		5.0	5.0	4.9
Other expenses	12.1	12.1		11.4		11.7	12.3	12.1
EBITDA	13.5	16.7		12.4		12.9	13.8	14.4
Adjusted net profit	6.9	8.9		6.4		6.6	7.3	7.7
Tax rate	34.9	33.3		33.3		34.2	31.7	32.0

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 %)	7.1	6.7	7.3	7.6
Inflation (Avg)	4.5	3.6	4.5	4.5
Repo rate (exit rate)	6.3	6.0	6.8	6.8
USD/INR (Avg)	67.1	64.5	70.0	72.0
Company				
Raw Material (% net rev)	65.6	67.9	68.9	68.6
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	50	57
2W OEM	16	17	17	19
4W Replacement	34	36	37	39
2W Replacement	32	33	35	36
Medium VRLA (UPS)	42	42	42	42
Large VRLA (Telecom)	61	55	51	53
4W OEM	10.6	11.6	12.7	13.5
2W OEM	2.1	2.4	2.5	2.6
4W Replacement	28.7	30.9	31.2	30.6
2W Replacement	7.6	8.4	8.8	9.0
Trading	0.8	1.0	1.0	0.9
Auto	49.8	54.4	56.2	56.7
Medium VRLA (UPS)	12.3	11.8	11.9	11.9
Large VRLA (Telecom)	24.9	18.6	15.3	14.1
Railway and Others	4.9	4.7	4.7	4.7
Industrial	49.5	45.0	43.1	42.7
Trade batteries	3.0	2.0	1.5	1.1
Trade Home UPS	0.5	1.3	1.3	1.1
Other exp (% net rev)	18.4	17.5	17.4	17.0
Cost assumptions				
Depreciation rate (%)	11.6	11.8	11.4	11.3
Tax rate (%)	31.9	34.0	34.0	34.0
Dividend payout (%)	17.4	18.0	-	16.4
Capex (INR mn)	(5,415)	(2,579)	(5,400)	(5,500)

Income statement

(INR mn)

Year to March	FY17	FY18	FY19E	FY20E
Income from operations	53,172	60,592	70,447	82,707
Materials costs	34,885	41,163	48,509	56,708
Manufacturing expenses	2,528	2,744	3,170	3,639
Employee costs	2,778	3,090	3,522	4,053
Aministration expenses	1,641	1,701	1,937	2,233
Selling & Advt. exp	2,841	3,062	3,593	4,135
Total operating expenses	44,672	51,759	60,731	70,769
EBITDA	8,500	8,833	9,715	11,938
Depreciation	1,912	2,303	2,603	3,072
EBIT	6,588	6,530	7,112	8,867
Less: Interest Expense	58	51	46	30
Add: Other income	492.4	663.7	486.34	484.05
Profit Before Tax	7,023	7,143	7,553	9,321
Less: Provision for Tax	2,237	2,429	2,398	2,978
Reported Profit	4,785	4,714	5,155	6,342
Adjusted Profit	4,785	4,714	5,155	6,342
Shares o/s (mn)	171	171	171	171
Adjusted Basic EPS	28.0	27.6	30.2	37.1
Diluted shares o/s (mn)	171	171	171	171
Adjusted Diluted EPS	28.0	27.6	30.2	37.1
Adjusted Cash EPS	40.9	41.5	45.4	55.1
Dividend per share (DPS)	4.2	4.2	4.2	5.2
Dividend Payout Ratio(%)	17.4	18.0	16.2	16.4

Common size metrics

Year to March	FY17	FY18	FY19E	FY20E
Materials costs	65.6	67.9	68.9	68.6
Aministration expenses	3.1	2.8	2.8	2.7
Operating expenses	84.0	85.4	86.2	85.6
Depreciation	3.6	3.8	3.7	3.7
Interest Expense	0.1	0.1	0.1	-
EBITDA margins	16.0	14.6	13.8	14.4
Net Profit margins	9.0	7.8	7.3	7.7

Growth ratios (%)

Year to March	FY17	FY18	FY19E	FY20E
Revenues	15.1	14.0	16.3	17.4
EBITDA	3.3	3.9	10.0	22.9
PBT	(2.8)	1.7	5.7	23.4
Adjusted Profit	(2.7)	(1.5)	9.4	23.0
EPS	(2.7)	(1.5)	9.4	23.0

Balance sheet		(INR mn)			
As on 31st March	FY17	FY18	FY19E	FY20E	
Share capital	171	171	171	171	
Reserves & Surplus	25,760	29,625	33,441	38,181	
Shareholders' funds	25,931	29,796	33,612	38,352	
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	31,551	35,067	39,807	
Gross Block	18,104	20,703	24,903	29,403	
Net Block	14,870	15,165	16,762	18,190	
Capital work in progress	2,403	2,264	3,464	4,464	
Intangible Assets	51	32	32	32	
Total Fixed Assets	17,324	17,461	20,258	22,686	
Non current investments	189	198	198	198	
Cash and Equivalents	2,987	3,989	3,890	3,872	
Inventories	8,170	10,497	9,581	11,305	
Sundry Debtors	5,705	7,825	8,106	9,517	
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	19,667	22,801	
Trade payable	4,184	5,923	4,471	5,276	
Other Current Liab	3,821	4,475	4,475	4,475	
Total Current Liab	8,006	10,398	8,946	9,751	
Net Curr Assets-ex cash	7,340	9,903	10,720	13,050	
Uses of funds	27,840	31,551	35,067	39,807	
BVPS (INR)	151.8	174.4	196.8	224.5	

Free cash flow		(INR mn)			
Year to March	FY17	FY18	FY19E	FY20E	
Reported Profit	4,785	4,714	5,155	6,342	
Add: Depreciation	1,912	2,303	2,603	3,072	
Interest (Net of Tax)	39	34	31	20	
Others	(70)	(361)	(532)	(582)	
Less: Changes in WC	(1,137)	(3,475)	(817)	(2,330)	
Operating cash flow	5,529	3,216	6,439	6,522	
Less: Capex	5,415	2,579	5,400	5,500	
Free Cash Flow	114	636	1,039	1,022	

Cash flow metrics				
Year to March	FY17	FY18	FY19E	FY20E
Operating cash flow	5,529	3,216	6,439	6,522
Financing cash flow	(20)	(1,382)	(1,138)	(1,040)
Investing cash flow	(5,349)	(2,443)	(5,400)	(5,500)
Net cash Flow	160	(609)	(98)	(18)
Capex	(5,415)	(2,579)	(5,400)	(5,500)
Dividend paid	-	(1,285)	(838)	(1,040)

Profitability and efficiency ratios				
Year to March	FY17	FY18	FY19E	FY20E
ROAE (%)	20.3	16.9	16.3	17.6
ROACE (%)	29.2	25.2	23.6	25.8
Inventory Days	74	83	76	67
Debtors Days	40	41	41	39
Payable Days	40	45	39	31
Cash Conversion Cycle	74	79	78	75
Current Ratio	2.3	2.3	2.6	2.7
Gross Debt/EBITDA	0.1	0.1	-	-
Gross Debt/Equity	-	-	-	-
Adjusted Debt/Equity	-	-	-	-
Interest Coverage Ratio	114.2	129.0	156.0	297.0

Operating ratios				
Year to March	FY17	FY18	FY19E	FY20E
Total Asset Turnover	2.1	2.0	2.1	2.2
Fixed Asset Turnover	3.7	4.0	4.4	4.7
Equity Turnover	2.3	2.2	2.2	2.3

Valuation parameters				
Year to March	FY17	FY18	FY19E	FY20E
Adj. Diluted EPS (INR)	28.0	27.6	30.2	37.1
Y-o-Y growth (%)	(2.7)	(1.5)	9.4	23.0
Adjusted Cash EPS (INR)	40.9	41.5	45.4	55.1
Diluted P/E (x)	27.6	28.0	25.6	20.8
P/B (x)	5.1	4.4	3.9	3.4
EV / Sales (x)	2.4	2.1	1.8	1.6
EV / EBITDA (x)	15.3	14.6	13.2	10.8
Dividend Yield (%)	0.5	0.5	0.5	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	1,813	25.6	20.8	13.2	10.8	16.3	17.6
Exide Industries	2,996	27.4	22.4	14.8	12.2	13.8	15.2
Median	-	26.5	21.6	14.0	11.5	15.0	16.4
AVERAGE	-	26.5	21.6	14.0	11.5	15.0	16.4

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	UTI ASSET MANAGEMENT CO LTD	1.55
WASATCH ADVISORS INC	2.55	BARON CAPITAL INC	1.23
CAPITAL GROUP COMPANIES INC	2.39	RELIANCE CAPITAL TRUSTEE CO LTD	1.02
ICICI PRUDENTIAL ASSET MGMT CO	2.36	VANGUARD GROUP	0.79
TEMPLETON ASSET MANAGEMENT	1.61	KOTAK MAHINDRA	0.67

**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

Amara Raja Batteries, Exide Industries

Recent Research

Date	Company	Title	Price (INR)	Recos
06-Nov-18	Exide Industries	Robust volumes keep growth charged; <i>Result Update</i>	253	Buy
13-Aug-18	Amara Raja Batteries	Auto volumes zoom; margin limps; <i>Result Update</i>	829	Buy
02-Aug-18	Exide Industries	Robust volumes sustain growth momentum; <i>Result Update</i>	271	Buy

Distribution of Ratings / Market Cap

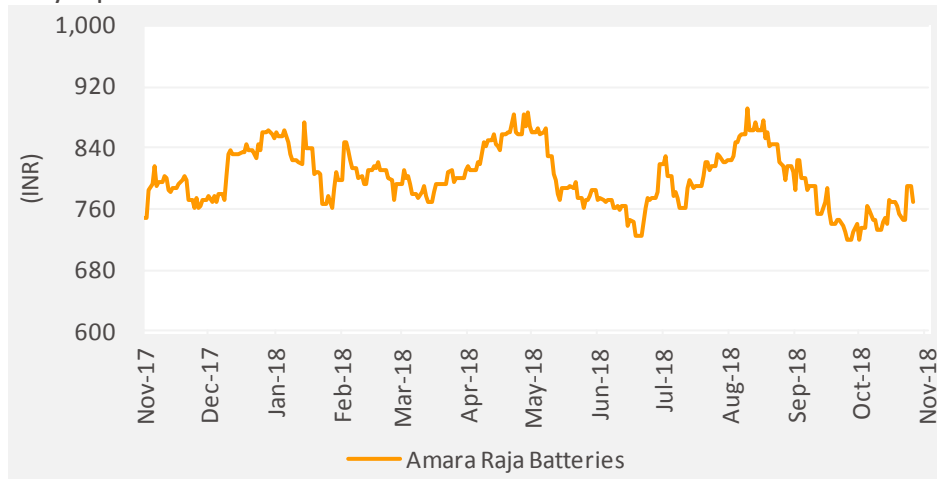
Edelweiss Research Coverage Universe

	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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