India Equity Research
Auto Ancillary

August 12, 2009

HOLD

Apollo Tyres

Target price (INR) 39

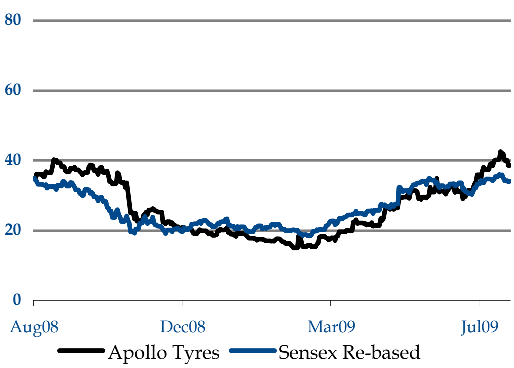
European operations not as profitable as earlier expected

Company Update

Last Price (INR)	38.6
Bloomberg code	APTY IN
Reuters code	APLO.BO
Avg. Vol. (3m)(mn)	6.23
Avg. Val.(3m)(INRmn)	212
52-wk H/L (INR)	44.0 / 13.6
Sensex	15,075
MCAP (INRbn/USDmn)	18.86 / 393

Shareholding (%)	03/09	06/09
Promoters	39.3	39.4
MFs, FIs, Banks	17.5	17.1
FIIs	14.8	12.3
Public	14.7	9.7
Others	13.7	21.7

Stock Chart (Relative to Sensex)



Stock Perfm. (%)	1m	6m	1yr
Absolute	22.7	124.4	11.6
Rel. to Sensex	11.1	65.2	12.5

Financials (INRmn)	03/09	03/10	03/11
Sales	49,949	70,735	78,229
YoY (%)	6	42	11
EBITDA (%)	8.3	12.4	12.6
A.PAT	1,390	2,103	2,277
Sh o/s (diluted)	504	504	504
A.EPS (INR)	2.8	4.2	4.5
YoY (%)	(48)	51	8
D/E (x)	0.5	1.5	1.3
P/E (x)	14.0	9.3	8.5
EV/E (x)	6.4	5.7	5.0
RoCE (%)	9	10	8
RoE (%)	11	13	11

Quarterly Trends	09/07	12/08	03/09	06/09
Sales (INRmn)	9,819	9,033	11,106	11,803
PAT (INRmn)	78	55	462	947

Contrary to earlier expectations, the Apollo Vredestein BV acquisition is unlikely to be a growth driver for Apollo Tyres till 2011. We forecast AVBV's revenues to fall by 11.8% in 2009, against our previous estimate of 8.5% growth. EBITDA margins are likely to be at 10.1%, against 12% earlier. AVBV is likely to report a loss of INR185mn in 2009f, compared to our previous expectations of net PAT of INR380mn. As a result, we decrease our PAT estimate for APTY by 12% for FY10f and 13% for FY11f. We rollover our target price to Jun10 from Mar10. We arrive at a target price of INR39, leaving our P/E of 8.1x unchanged. This presents an upside of 1%. The risk to our call is the limited information currently disclosed by the company. We downgrade our rating on the stock from Buy to Hold.

Robust operational performance, excluding AVBV, likely in FY10f

APTY reported strong standalone performance in 1QFY10. Net profit increased by 95% y-o-y, led by 13% y-o-y decline in the average rubber cost to INR87/kg. We forecast APTY's average rubber cost in FY10f at INR105/kg, compared to INR124/kg in FY09. Net PAT for operations, excluding AVBV, is forecast to rise by 55% y-o-y to INR2,155mn in FY10. This includes interest of INR980mn on the AVBV acquisition cost. APTY has announced various capex programs, with an outlay of cINR29.6bn during FY10f-FY12f. However, due to lower growth, we forecast the company to spend only INR16.9bn during this period.

AVBV acquisition to contribute only from FY11f

APTY acquired AVBV on May 15, 2009, for an undisclosed amount. Based on media reports, we estimate the cost of acquisition at INR11,760mn. After factoring in this cost, we forecast APTY to report consolidated net PAT of INR2,103mn and INR2,277mn in FY10 and FY11, respectively. If the cost of acquisition is INR5bn, the consolidated net PAT is likely to be INR2,475mn and INR2,729mn, respectively. European tyre companies have a higher fixed-cost structure compared to APTY. Hence, based on our forecast of an 11.8% decline in revenues in 2009, AVBV is likely to report a net loss of INR185mn. We forecast AVBV to report net PAT of INR248mn in 2010 and INR489mn in 2011.

Reduce TP to INR39, based on cut in FY10f and FY11f EPS estimates

We downgrade our earnings forecast for APTY, on account of lower contribution from the AVBV acquisition and higher interest cost. AVBV's revenues are forecast to decline by 11.8% in 2009 and rise by only 2.8% in 2010. We had earlier forecast AVBV's revenues to grow by 8.5% in both 2009 and 2010. Our consolidated earnings forecast for APTY has been lowered by 12% for FY10 and by 13% for FY11. We downgrade our rating on the stock from Buy to Hold. We reduce our target price from INR42, due to downward revision in EPS for FY10f and FY11f. Our P/E of 8.1x remains unchanged and we arrive at a target price of INR39 for Jun10. The risk to our call is the limited information currently disclosed by the company.

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Please refer to the disclaimer towards the end of the document.

Robust performance in FY10f in operations, excluding AVBV

Apollo Tyres (APTY IN, Hold) reported strong standalone performance in 1QFY10, with net profit increasing by 95% y-o-y due to 13% y-o-y reduction in the average rubber cost to INR87/kg. The average spot rubber price has increased by 35% q-o-q to INR97/kg in 1QFY10f. We expect rubber prices to continue rising. We estimate APTY's average rubber cost at INR105/kg in FY10f compared to INR124/kg in FY09. The contribution per kg of tyres sold is likely to increase by 34% to INR53.6 in FY10f. Hence, net PAT for operations, excluding Apollo Vredestein BV (AVBV), is forecast to rise by 55% y-o-y to INR2,155mn in FY10f. This includes interest of INR980mn on the AVBV acquisition cost. However, in FY11f, owing to lower EBITDA margin and higher interest costs, we expect net profit for operations, excluding AVBV, to decrease by 8.6% y-o-y to INR1,969mn. APTY has announced various capex programs, with an outlay of cINR29.6bn during FY10f-FY12f. However, due to lower growth, we forecast the company to spend only INR16.9bn during this period.

APTY reports better standalone performance in 1QFY10

Exhibit 1: 1QFY10 results table

(INRmn)	Standalone	Consolidated
Revenue	11,803	16,350
y-o-y growth (%)	10	24
Profit after tax	947	738
y-o-y growth (%)	95	26

Source: Company, Avendus Research

Normally, APTY reports similar standalone and consolidated performance. However, with consolidation of AVBV's revenues, the company reported strong standalone performance in 1QFY10. Standalone revenues increased by 10% y-o-y, to INR11.8bn, on account of a c7% y-o-y increase in realizations. EBITDA increased 77% y-o-y to INR1.9bn, led by lower raw material cost. APTY's rubber cost decreased by c13% y-o-y to INR87/kg in 1QFY10. Standalone PAT increased by 94.7% y-o-y to INR946.7mn.

Consolidated revenue increased by 24% y-o-y due to consolidation of AVBV's accounts for 45 days during the quarter. In 1QFY10, the company incurred a cost of cINR200mn as consultancy charges for the merger. Consolidated PAT increased by 26% y-o-y to INR738mn.

Recent increase in import of Chinese radials to negatively impact APTY

Import of Chinese truck and bus (T&B) radial tyres has been on the restricted list from November 24, 2008. Thus, the share of imports from China declined to 35% in Feb09 (c89% in FY09). However, there has been an increase in licenses for imports. Though official figures of current imports are unavailable, our interactions with industry sources suggest that c20,000 tyres were imported from China in Jun09, from 7,392 in Feb09. This is likely to negatively impact demand in the T&B segment for APTY.

Exhibit 2: Monthly import of radial tyres

	FY07	FY08	FY09	Feb09
Total imports	20,681	49,802	60,322	21,088
Imports from China	18,442	47,016	53,696	7,392
Chinese tyres in total tyre imports (%)	89	94	89	35

Source: Director General of Commercial Intelligence and Statistics

Robust performance likely in FY10f in operations, excluding AVBV

Excluding AVBV, operations for APTY include the standalone operations and those for Dunlop. We expect APTY, excluding AVBV, to report revenue growth of 8.4% y-o-y (INR54.1bn) in FY10f, led by 7% volume growth in Indian operations. Realizations in standalone operations are likely to increase by 4% each in FY11f and FY12f, owing to better product mix and price increases. The improved product mix is on account of higher revenue from off-the-road (OTR) tyres and higher sales of radial tyres. Thus, we expect revenues from operations, excluding AVBV, to increase by 7.6% in FY11f and 7.9% in FY12f.

APTY reported a standalone EBITDA margin of 16.5% in 1QFY10f, with average rubber cost of INR87/kg. We expect APTY's average rubber cost for the remaining quarters of FY10f to be higher. However, we forecast the average rubber cost for APTY to reduce by 15% y-o-y to INR105/kg in FY10.

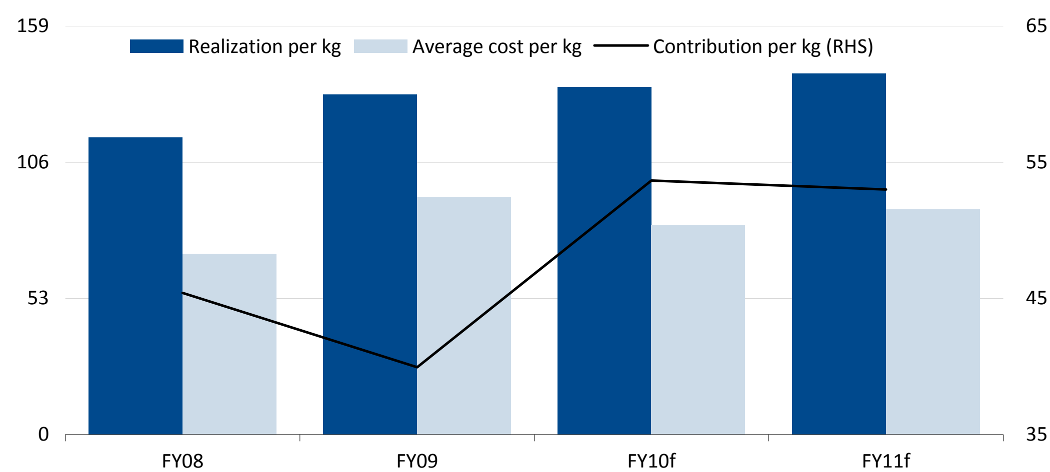
On account of lower commodity prices, we expect the contribution per kg to increase by 34.3% y-o-y to INR53.7 in FY10f. Despite a 7.4% likely increase in average raw material cost in FY11f, we expect the contribution per kg to decline by only 1.2% y-o-y to INR53. This is on account of increased demand from the high-margin OTR and the T&B radial segments. EBITDA margins for operations, excluding AVBV, are estimated at 12.9%, 12.6% and 12.5% for FY10f, FY11f and FY12f, respectively.

Exhibit 3: Financials, excluding AVBV

(INRmn)	1QFY10e	FY09	FY10f	FY11f	FY12f
Total operating income	14,253	49,949	54,133	58,269	62,876
Total operating expenses	12,361	45,788	47,161	50,928	55,017
EBITDA	1,892	4,161	6,973	7,341	7,859
Other income	8	230	147	179	219
Depreciation	395	1,285	1,708	2,179	2,384
EBIT	1,505	3,105	5,411	5,341	5,693
Interest	347	973	2,153	2,402	2,291
Recurring PBT	1,158	2,133	3,258	2,940	3,402
Net extraordinary items	-	0	0	0	0
PBT (reported)	1,158	2,133	3,258	2,940	3,402
Total taxes	397	742	1,103	971	1,121
PAT (reported)	760	1,391	2,155	1,969	2,281
Dividend		265	324	354	354
Internal accruals		2,410	3,539	3,794	4,311
Interest as a percentage of average debt		12.7	13.3	10.4	10.5
Depreciation to average gross block (%)		6.1	5.9	5.9	5.9
EBITDA margins (%)	13.3	8.3	12.9	12.6	12.5

Source: Avendus Research

Exhibit 4: Contribution analysis of APTY (standalone; INR)



Source: Avendus Research

Net PAT for operations, excluding AVBV, is expected to rise by 55% y-o-y to INR2,155mn in FY10f. This includes interest of INR980mn on the AVBV acquisition cost. However, in FY11f due to lower EBITDA margins and higher interest costs, net profit is likely to decrease by 8.6% y-o-y to INR1,969mn.

Revenue growth to be slower than the rise in capex

Exhibit 5: Vehicle sales, excluding two-wheeler growth

(%)	FY09	Apr09-Jul09	Aug09-Mar10f	FY10f	FY11f	FY12f
Commercial vehicles	-21.8	-10.7	9.3	1.7	10.0	10.0
Passenger vehicles	9.5	16.6	4.1	8.1	10.0	8.0
Three-wheelers	-1.6	3.5	4.2	4.0	4.0	4.0
Tractors	-1.1	-11.8	-9.5	-10.0	10.0	8.0
Vehicle sales	0.4	7.3	3.0	4.3	9.0	7.6

Source: Society of Indian Automobile Manufacturers, Avendus Research

Commercial vehicles (CV): In the first four months of FY10f, CV sales volumes have declined by 10.7% y-o-y. Assuming the same average volume of 36,160 vehicles per month for the period between Aug09 and Mar10 as in the first four months of FY10f, we expect the CV industry to report a growth of 1.7% in FY10f. We expect an improvement in freight activity, leading to 10% growth in CV sales in FY11f and FY12f.

Passenger vehicles: In the first four months of FY10f, the industry has grown at 16.6% y-o-y. Based on a slowdown in demand (due to weak monsoons) and hardening of interest rates for the remainder of the year, we expect sales in the segment to grow by 8% in FY10f. Car sales are expected to rise by 10% y-o-y and 8% y-o-y in FY11f and FY12f, respectively, due to incremental sales from Tata Nano.

Three-wheelers: In the first four months of FY10f, the three-wheeler industry has grown at 4% y-o-y. We assume three-wheeler sales to grow at 4% each for FY10f, FY11f and FY12f.

Tractors: We assume sales in the tractor segment to follow a similar trend as Mahindra and Mahindra's (MM IN, NR) tractor sales. Thus, we estimate sales in the segment to have declined by 11.8% y-o-y in the first four months of FY10f. Based on a slowdown in demand (due to weak monsoons) and hardening of interest rates for the remainder of the year, we expect sales in the segment to decline by 10% in FY10f. Assuming normal monsoon in 2010, we expect tractor sales to grow at 10% in FY11f.

Exhibit 6: Relationship between growth in APTY's volumes (in tonnes) and vehicle population

(%)	FY07	FY08	FY09	FY10f	FY11f	FY12f
APTY's volume growth as measured in tonnes	6.7	7.8	-5.1	7.0	3.6	3.8
Vehicle population, excluding two-wheelers (y-o-y)	11.9	11.2	10.0	9.4	9.6	9.7
New vehicle sales, excluding two-wheelers (y-o-y)	23.7	5.1	0.4	4.3	9.0	7.6

Source: Avendus Research

We base our sales forecast on its relationship with vehicle population, excluding two-wheelers. The vehicle population is estimated as follows:

- Vehicle population for the year is the sum of sales for the past 19 years, including the current year.
- Vehicles sold 20 years ago are assumed to be scrapped in the current year.

In FY09, the company's sales volumes (as measured in tonnes) declined by 5.1%, led by underutilization of the existing vehicle population. Volumes declined by 22.3% y-o-y in 3QFY09 to 59,055 tonnes, but increased to 72,414 tonnes in 4QFY09 and 79,150 tonnes in 1QFY10. We expect some slowdown in volumes from 1QFY10-levels. Assuming average quarterly volumes of 71,804.4 tonnes for the remainder of FY10f, we expect volumes to grow by 7% in FY10f.

Exhibit 7: APTY's sales volumes

	1QFY09	2QFY09	3QFY09	4QFY09	1QFY10	Jul08-Mar09	Jul09-Mar10f	FY09	FY10f
Volumes (in tonnes)	77,530	66,202	59,055	72,414	79,150	197,671	215,413	275,201	294,564
y-o-y growth (%)	14.0%	-1.2%	-22.3%	-2.8%	2.1%	-9.1%	9.0%	-5.1%	7.0%

Source: Company, Avendus Research

Volumes (as measured in tonnes) are likely to rise by 7% in FY10f, based on a 9.4% increase in vehicle population. We believe the rampant retreading of tyres has led to the slower growth in volumes. Despite our estimates of a 9.6% and 9.7% increase in vehicle population, APTY's sales volumes are likely to rise by just 3.6% and 3.8% in FY11f and FY12f, respectively.

Exhibit 8: APTY's (standalone) capex plan during FY10f-FY12f

(INRmn)	
Passenger car radial (PCR) expansion	2,000
T&B radial	20,000
Greenfield project for small PCR	7,000
OTR	600
Total capital expenditure	29,600
Avendus estimate of capital expenditure	16,851

Source: Company, Avendus Research.

APTY has announced various capex programs, with an outlay of cINR29.6bn during FY10f-FY12f. However, due to lower growth, we believe the company is likely to spend only INR16.9bn during this period.

Exhibit 9: Details of APTY's capex forecast in India

(INRmn)	**Location**	**FY10f**	**FY11f**	**FY12f**
Capex plans				
PCR expansion	Baroda	1,921	-	-
T&B radials	Chennai	6,000	500	500
Greenfield for small PCR	Chennai	2,000	3,324	2,306
OTR	Baroda	300		
Total capex in India		**10,221**	**3,824**	**2,806**
Incremental sales				
Revenue from current plants		3,903	575	-811
PCR expansion	Baroda	-	1,373	686
T&B radials	Chennai	-	1,257	2,932
Greenfield for small PCR	Chennai		158	686
OTR	Baroda	282	317	634
Total incremental sales		**4,184**	**3,679**	**4,127**
Funding of capex		44,997	48,676	52,803
Internal accruals		4,319	3,824	2,806
Debt and available cash		5,901	-	-
Total funding of capital expenditure		**10,221**	**3,824**	**2,806**

Source: Avendus Research

We expect APTY to spend INR10.2bn on various capex programs in FY10f. The company is expected use internal accruals of INR4.3bn to fund the capex in FY10f. As both the T&B radials and the small PCR capacities are likely to be commissioned in 4QFY10f, we have not factored in any incremental revenue from these facilities for FY10f. We expect APTY to incur a capex of INR3.8bn and INR2.8bn in FY11f and FY12f, respectively.

We expect incremental revenues of INR2,629mn from the PCR and T&B radial facilities in Chennai in FY11f. Incremental revenues of INR4.1bn are likely in FY12f. This includes a revenue reduction of INR811mn from the current plants due to a decline in utilization of the bias capacity in the T&B segment. Utilization is likely to decline due to a shift in demand for the T&B radial segment.

AVBV acquisition to only contribute from FY11f

APTY acquired AVBV on May 15, 2009, for an undisclosed amount. Based on media reports, we estimate the cost of acquisition at INR11,760mn. After factoring in this cost, we forecast APTY to report consolidated net PAT of INR2,103mn and INR2,277mn in FY10 and FY11, respectively. If the cost of acquisition is INR5bn, then the consolidated net PAT is likely to be INR2,475mn and INR2,729mn, respectively. European tyre companies have a higher fixed-cost structure compared to APTY. Hence, based on our forecast of an 11.8% decline in revenues in 2009, AVBV is likely to report a net loss of INR185mn. We forecast AVBV to report net PAT of INR248mn and INR489mn in 2010 and 2011, respectively.

Sensitivity of earnings to cost of acquisition

Exhibit 10: Sensitivity of APTY's earnings to cost of acquisition (INRmn)

Cost of acquisition	------------------------ Net PAT ------------------------	
	FY10f	FY11f
5,000	2,475	2,729
10,000	2,200	2,394
11,760	2,103	2,277
15,000	1,924	2,060

Source: Avendus Research

APTY acquired 100% stake in European tyre manufacturer Vredestein Banden BV on May 15, 2009. The company has been rechristened Apollo Vredestein B.V. Due to certain legal issues, APTY has not disclosed the acquisition cost and balance sheet details.

Based on certain media reports, we estimate the cost of acquisition at INR11,760mn. The company had announced that the acquisition would be funded through internal accruals and debt. However, given the company's capital expenditure within India in FY10f, we believe the acquisition would be entirely funded through debt. In case the cost of acquisition is INR5bn, APTY's net PAT is likely to be INR2,475mn in FY10f and INR2,729mn in FY11f.

APTY raised debt in May09 for funding the acquisition. Assuming an interest rate of 10%, we estimate the interest cost to be INR980mn in FY10f.

AVBV's performance likely to be subdued in 2009f

Exhibit 11: Financials of AVBV (INRmn)

(INRmn)	2007	2008	2009f	2010f	2011f
Total operating income	19,056	21,312	19,005	19,544	21,205
Total operating expenses	16,272	18,960	17,078	17,109	18,564
EBITDA	2,784	2,352	1,927	2,435	2,642
Other income	48	-	-	-	-
Depreciation	1,344	1,488	1,383	1,399	1,446
Impairment of long-lived assets		6,192			
EBIT	1,488	-5,328	544	1,036	1,196
Interest	528	720	730	682	498
Recurring PBT	960	-6,048	-185	354	698
Net extraordinary items					
PBT (reported)	960	-6,048	-185	354	698
Total taxes	288	96	0	106	210
PAT (reported)	672	-6,144	-185	248	489

Source: Avendus Research

We base our 2009 and 2010 revenue and EBITDA forecasts for AVBV on Bloomberg consensus forecasts for Compagnie Generale des Etablissements Michelin (ML FP, NR) and Pirelli & C SpA (PC IM, NR). These companies operate in similar geographies as AVBV. We forecast AVBV's revenue to decline by 11.8% y-o-y to INR19bn in 2009 and increase by 2.8% y-o-y to INR21.2bn in 2010. EBITDA margins are forecast at 10.1% and 12.5% in 2010 and 2011, respectively. AVBV's revenue has increased at a CAGR of 8.5% in the past five years. Based on this, in 2011f, we expect revenue growth to be 8.5%.

Exhibit 12: Revenue and EBITDA margin forecast for AVBV

Year	(%)	Basis
Revenue growth		
2009f	-11.8	Consensus forecast for ML and PC
2010f	2.8	Consensus forecast for ML and PC
2011f	8.5	Five-year revenue CAGR of AVBV till 2008
EBITDA margins		
2009f	10.1	Consensus forecast for ML and PC
2010f	12.5	Consensus forecast for ML and PC
2011f	12.5	Same as 2010

Source: Bloomberg, Avendus Research

Exhibit 13: Margins of APTY and European tyre companies

(%)	------------European average----------		----------APTY standalone---------	
	2007	2008	FY08	FY09
Employee expenses	23	27	6	5
Other operational expenses	66	65	82	87
EBITDA	11	9	13	8
PAT	5	-4	6	3

Note: We have considered ML and PC for calculating the European average

Source: Bloomberg, Avendus Research

European tyre companies like ML and PC have a higher fixed-cost structure compared to APTY. The company's employee expenses as a proportion of sales were at 27% in 2008 compared to 5% in FY09. This indicates APTY's relative flexibility compared to European tyre companies. These companies had a net loss margin of 4% in 2008 compared to 3% net profit margins for APTY in FY09. Hence, based on our forecast of an 11.8% decline in revenues in 2009, AVBV is likely to report a net loss of INR185mn. The company is likely to report net PAT of INR248mn in 2010f and INR489mn in 2011f. In 2012f, we expect AVBV to report net PAT of INR756mn.

We consolidate AVBV's results with that of APTY on the following basis.

- **FY10f**: In the income statement, we include the proportional financials from May 16, 2009, to December 31, 2009, and one-fourth of the financials in 2010f. In the balance sheet, we include the financials at end 2009 and one-fourth of the difference between the end-2010 and end-2009 financials.
- **FY11f:** In the income statement, we include three-fourth of the 2010f financials and one-fourth of the 2011 financials. In the balance sheet, we include the financials at end 2009 and one-fourth of the difference between the end-2011f and end-2010f financials.
- **FY12f:** In the income statement, we include three-fourth of the 2011f financials and one-fourth of the 2011f financials. In the balance sheet, we include the financials at end 2010 and one-fourth of the difference between the end-2012f and end-2011f financials.

Exhibit 14: Addition from AVBV to APTY's consolidated P&L

(INRmn)	FY10f	FY11f	FY12f
Total operating income	16,601	19,960	21,656
Total operating expenses	14,805	17,473	18,958
EBITDA	1,797	2,486	2,698
Other income	0	0	0
Depreciation	1,202	1,410	1,463
EBIT	595	1,076	1,235
Interest	620	636	441
Recurring PBT	-26	440	794
Net extra ordinary items	0	0	0
PBT (reported)	-26	440	794
Total taxes	27	132	238
PAT (reported)	-52	308	556

Source: Avendus Research

We expect AVBV to report a net loss of INR52mn in FY10f, net profit of INR308mn in FY11f and net profit of INR556mn in FY12f.

Reduce TP to INR39, based on cut in FY10f and FY11f EPS estimates

We downgrade our consolidated earnings forecast for APTY, on account of lower contribution from the AVBV acquisition and higher interest costs. AVBV's revenues are forecast to decline by 11.8% in 2009 and rise by only 2.8% in 2010. We had earlier forecast AVBV's revenues to grow by 8.5% in both 2009 and 2010. Our earnings forecast for APTY has been reduced by 12% for FY10 and 13% for FY11. We downgrade our rating on the stock from Buy to Hold. We reduce our target price from INR42, due to downward revision in EPS for FY10f and FY11f. Our P/E of 8.1x remains unchanged and we arrive at a target price of INR39 for Jun10. The risk to our call is the limited information currently disclosed by the company.

Cut profit forecasts due to lower contribution from AVBV

Exhibit 15: Earnings estimate revision for APTY (consolidated)

	-------------------- FY10f--------------------			-------------------- FY11f --------------------		
(INRmn)	**Old**	**New**	**% change**	**Old**	**New**	**% change**
Revenue	63,823	70,735	11	80,596	78,229	-3
EBITDA	7,845	8,769	12	9,954	9,828	-1
EBIT	5,496	6,006	9	6,944	6,417	-8
PBT	3,586	3,232	-10	3,949	3,380	-14
PAT	2,388	2,103	-12	2,624	2,277	-13
EPS (INR)	4.7	4.2	-12	5.2	4.5	-13

Source: Avendus Research

Following are the major changes in assumptions for the FY10 and FY11 forecasts:

- Consolidation of AVBV with APTY from May 16, 2009, against earlier assumption of October 1, 2009.
- Revenue decline of 11.8%, against a previous estimate of 8.5% growth, for AVBV in 2009f.
- Revenue growth of 2.8%, against a previous estimate of 8.5% growth, for AVBV in 2010f.
- EBITDA margins of 10.1%, against a previous estimate of 12%, for AVBV in 2009f.
- EBITDA margins of 12.5%, against a previous estimate of 12%, for AVBV in 2010f.
- Interest cost of INR2.8bn in FY10f, against a previous estimate of INR1.9bn. This revision is based on higher interest cost for debt taken for acquisition and other capital expenditure programs.

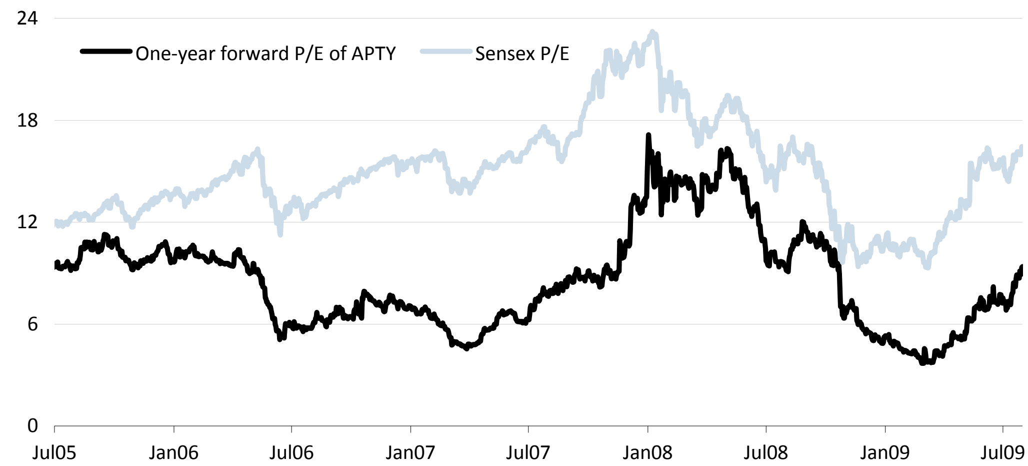
Exhibit 16: Change in estimates for different segments

	---------------- Old estimates ----------------			---------------- New estimates ----------------		
(INRmn)	**AVBV**	**Non-AVBV**	**Consolidated**	**AVBV**	**Non-AVBV**	**Consolidated**
FY10f						
Revenue	11,668	52,155	63,823	16,601	54,133	70,735
EBITDA	1,400	6,445	7,845	1,797	6,973	8,769
PAT	198	2,190	2,388	-52	2,155	2,103
FY11f						
Revenue	24,803	55,793	80,596	19,960	58,269	78,229
EBITDA	2,976	6,977	9,954	2,486	7,341	9,828
PAT	422	2,202	2,624	308	1,969	2,277
FY12f						
Revenue	26,911	59,653	86,564	21,656	62,876	84,532
EBITDA	3,229	7,531	10,760	2,698	7,859	10,557
PAT	457	2,309	2,766	556	2,281	2,837

Source: Avendus Research

Based on 12-month rolling P/E, reduce target price to INR39

Exhibit 17: One-year forward P/E ratio of APTY and the BSE Sensex



Source: Avendus Research

We rollover our target price to Jun10 from Mar10. We reduce our target price from INR42, due to 12% downward revision in EPS for FY10f and FY11f. We maintain our target P/E on the stock at 8.1x. Our Jun10 target price of INR39 presents a 1% upside.

Risk factors

- **Adverse disclosure on AVBV acquisition:** The risk to our call is the limited information currently disclosed by the company.
- **Changes in rubber price and volume growth:** Any significant increase in the rubber price will have a negative impact on APTY. Also, any softening in tyre demand due to either underutilization of commercial vehicles or lower demand for new vehicles is likely to lead to downward revision of our volume estimates.

Financials and valuations

Income statement (INRmn)

Fiscal year ending	03/09e	03/10f	03/11f	03/12f
Total operating income	**49,949**	**70,735**	**78,229**	**84,532**
Total operating expenses	**45,788**	**61,965**	**68,401**	**73,976**
EBITDA	**4,161**	**8,769**	**9,828**	**10,557**
Other income	230	147	179	219
Depreciation	1,285	2,911	3,589	3,847
EBIT	**3,105**	**6,006**	**6,417**	**6,928**
Interest	973	2,773	3,037	2,732
Recurring PBT	2,133	3,232	3,380	4,196
Net extra ordinary items	-	-	-	-
PBT (reported)	2133	3,232	3,380	4,196
Total taxes	742	1,130	1,103	1,360
PAT (reported)	1391	2,103	2,277	2,837
(+) Share in assoc. earnings	0	-	-	-
Less: Minority interest	0	-	-	-
Prior period items	-	-	-	-
Net income (reported)	1,390	2,103	2,277	2,837
Avendus net income	**1,390**	**2,103**	**2,277**	**2,837**
Shares outstanding (mn)	504.1	504.1	504.1	504.1
Avendus dil. shares (mn)	504.1	504.1	504.1	504.1
Avendus EPS (INR)	**2.8**	**4.2**	**4.5**	**5.6**

Growth ratios (%)

Total operating income	6.4	41.6	10.6	8.1
EBITDA	-30.3	110.8	12.1	7.4
EBIT	-37.1	93.4	6.9	8.0
Recurring PBT	-47.4	51.5	4.6	24.2
Avendus net income	-48.4	51.2	8.3	24.6
Avendus EPS	-48.4	51.2	8.3	24.6

Operating ratios (%)

EBITDA margin	8.3	12.4	12.6	12.5
EBIT margin	6.2	8.5	8.2	8.2
Net profit margin	2.8	3.0	2.9	3.3
Other income/PBT	10.8	4.6	5.3	5.2
Effective Tax rate	34.8	35.0	32.6	32.4

Balance sheet (INRmn)

Fiscal year ending	03/09e	03/10f	03/11f	03/12f
Equity capital	504	504	504	504
Preference capital	-	-	-	-
Reserves and surplus	12,959	19,337	22,047	25,318
Net worth	**13,464**	**19,841**	**22,551**	**25,822**
Minority interest	-	-	-	-
Total debt	8,907	29,422	27,337	23,745
Deferred tax liability	1,942	2,191	2,416	2,663
Total liabilities	**24,312**	**51,453**	**52,303**	**52,230**
Gross block	22,809	56,084	60,408	63,214
less: Acc. depreciation	8,822	24,119	27,708	31,555
Net block	13,988	31,965	32,699	31,658
CWIP	2,814	1,000	500	500
Goodwill	235	8,292	8,292	8,292
Investments	48	3,760	3,760	3,760
Cash	3,621	877	478	588
Inventories	6,302	10,591	11,238	12,114
Debtors	2,247	9,350	9,792	10,568
Loans and advances	2,057	3,347	3,825	4,461
less: Current liabilities	5,860	13,644	14,265	15,427
less: Provisions	1,139	4,085	4,018	4,285
Net working capital	7,228	6,435	7,051	8,019
Total assets	**24,312**	**51,453**	**52,303**	**52,230**

Cash flow statement (INRmn)

Fiscal year ending	03/09e	03/10f	03/11f	03/12f
Net profit	1,390	2,103	2,277	2,837
Depreciation	1,285	2,911	3,589	3,847
Deferred tax	154	97	101	126
Working capital changes	317	-1,951	-1,015	-858
Less: Other income	230	147	179	219
Cash flow from operations	**2,916**	**3,012**	**4,774**	**5,733**
Capital expenditure	-5,151	-31,461	-3,824	-2,806
Strategic investments	4	-3,713	0	0
Marketable investments	0	0	0	0
Change in other loans & adv.	0	0	0	0
Goodwill paid	-20	-8,057	0	0
Other income	230	147	179	219
Cash flow from investing	**-4,937**	**-43,084**	**-3,645**	**-2,588**
Equity raised	1,656	6,375	2,710	3,271
Change in borrowings	2,446	20,514	-2,085	-3,592
Dividends paid (incl. tax)	0	0	0	0
Others	-1,308	10,438	-2,153	-2,715
Cash flow from financing	**2,794**	**37,328**	**-1,528**	**-3,036**
Net change in cash	**774**	**-2,744**	**-399**	**110**

Key Ratios

Fiscal year ending	03/09e	03/10f	03/11f	03/12f
Valuation ratios (x)				
P/E (on Avendus EPS)	14.0	9.3	8.5	6.9
P/E (on basic, reported EPS)	14.0	9.3	8.5	6.9
P/CEPS	7.3	3.9	3.3	2.9
P/BV	1.4	1.0	0.9	0.8
Dividend yield (%)	-	-	-	-
Market cap. / Sales	0.4	0.3	0.2	0.2
EV/Sales	0.5	0.7	0.6	0.5
EV/EBITDA	6.4	5.7	5.0	4.3
Net Cash / Market cap.	18.6	4.5	2.5	3.0
Per share ratios (INR)				
Avendus EPS	2.8	4.2	4.5	5.6
EPS (Basic, reported)	2.8	4.2	4.5	5.6
Cash EPS	5.3	9.9	11.6	13.3
Book Value	26.7	39.4	44.7	51.2
Dividend per share	0.0	0.0	0.0	0.0
Total assets / equity (x)	1.8	2.3	2.4	2.2
Return ratios (%)				
ROCE	9.1	10.3	8.3	9.0
ROIC	11.9	11.6	8.6	9.1
ROE	11.0	12.6	10.7	11.7
ROA	6.3	5.6	4.4	5.4
OCF/Sales	5.8	4.3	6.1	6.8
FCF/Sales	-4.5	-40.2	1.2	3.5
Turnover ratios (x)				
Asset turnover (x)	2.3	1.9	1.5	1.6
Gross asset turnover	2.2	1.3	1.3	1.3
Inventory / Sales (days)	49.2	43.6	50.9	50.4
Receivables (days)	19.6	29.9	44.7	44.0
Payables (days)	62.7	77.4	93.0	92.2
Working capital cycle (days)	27.5	23.6	28.3	30.2
Solvency ratios (x)				
Gross debt to equity	0.8	1.6	1.3	1.0
Net debt to equity	0.5	1.5	1.3	1.0
Net debt to EBITDA	2.1	3.4	2.8	2.2
Interest Coverage (on EBIT)	3.2	2.2	2.1	2.5

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