Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Stock Update

Result Update

Amara Raja Energy & Mobility Ltd

Benefitting from soft RM cost

Automobiles		Sharekhan code: ARE&M	
Reco/View: Buy	↔	CMP: Rs. 618	Price Target: Rs. 717 ↔

↑ 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 20.12

Updated Aug 08, 2023

Medium Risk

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

Source: Morningstar

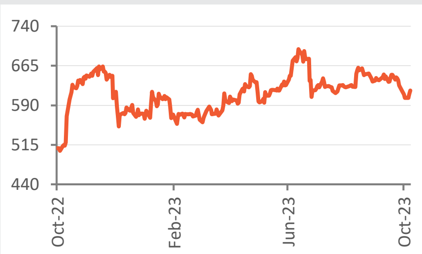
Company details

Market cap:	Rs. 10,556 cr
52-week high/low:	Rs. 708 / 509
NSE volume: (No of shares)	9.1 lakh
BSE code:	500008
NSE code:	ARE&M
Free float: (No of shares)	12.3 cr

Shareholding (%)

Promoters	28.1
FII	24.6
DII	16.8
Others	30.5

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-3.2	-1.0	1.9	21.6
Relative to Sensex	-0.2	2.9	-3.9	14.8

Sharekhan Research, Bloomberg

Summary

- Adjusted EBITDA margin rose 140 bps q-o-q to 14.1% against estimate of 13.1%, as RM costs softened
- With RM costs likely to stay stable for the next two quarters, the management has guided for a 10% revenue growth for FY24.
- We maintain a Buy on the stock with unchanged PT of Rs 717 led by expectation of healthy traction in the replacement market, soft RM cost trend and an opportunity to play in the Li-ion cell business.
- Stock trades at a P/E multiple of 9.7x and EV/EBITDA multiple of 4.3x its FY26E estimates.

With healthy gross margin expansion supported by benign raw material cost trends and in-house cost cutting, Amara Raja Energy & Mobility Ltd (Amara) has beaten our adj. EBITDA margin estimates by 100 bps and hence reported bottom line 5.3% ahead of estimates. Revenue increased by 1.5% q-o-q to Rs. 2811 crore (against estimate of Rs 2950 crore) on the back of healthy performance in automotive aftermarket, telecom, and UPS segment. Adjusted to one time cost of Rs 10 crore pertain to consultancy charges AEBITDA increased by 12.3% q-o-q to Rs 397 crore (against estimate of Rs 385 crore). AEBITDA margin expanded by 140 bps q-o-q to Rs 14.1% (as against an estimate of 13.1%) on a 270-bps q-o-q expansion in gross margin. With strong operating performance APAT increased by 11.3% q-o-q to Rs 214 crore (against estimate of Rs 213 crore. Along with the result the company has also announced an interim dividend of Rs 4.8/ share. Further, the board has also decided to invest an additional Rs. 500 crore in its subsidiary - Amara Raja Advanced Cell Technologies Private Limited (ARCACT). ARACT is setting up a Li-ion battery manufacturing plant. Going forward the company has guided for a 10% revenue growth (in line with our expectations) in FY24 and steady RM cost trend for the next two quarters.

Key positives

- Gross margin rose 270 bps q-o-q on account of steady RM cost trend
- Adjusted EBITDA margin rose 140 bps q-o-q to 14.1% led by healthy traction in aftermarket and industrial segment along with soft RM cost trend.
- New energy business is gaining traction and reported revenues of Rs 150 crore in Q2FY24 compared to Rs 108 crore in Q1FY24.

Key negatives

- Export volumes were hit by change in the name of the company (legal reasons).
- OEM and export volumes grew 2-3%, slower than after market segment (8%).
- Company has been facing capacity constraints in the tubular battery segment.

Management Commentary

- New energy business is performing well and looking to expand beyond three-wheeler segment in new energy segment.
- The company is aiming for a 10% revenue growth in FY24.
- No pricing action was taken in aftermarket segment in Q2FY24 and Steady RM cost trend is expected to support EBITDA margin performance

Our Call

Valuation – Maintain Buy with a unchanged PT of Rs.717: Despite subdued performance in OEM and export segments, Amara surpassed our AEBITDA margin expectations and reported 140 bps q-o-q expansion in EBITDA margin on account of benign RM cost trend. Further, the management is expecting 10% revenue growth for FY24 which is in line with our expectations. New energy business is registering healthy traction and the management indicates that profitability in new energy may improve further on increase in localisation. Merger of the plastic business with the company is on track. The merger of the plastic business would be margin and EPS accretive. Further, the lithium ion (Li-ion) battery project is expected to begin deliveries from FY2026. We believe that lead acid batteries to continue to remain in demand for the next few years in the replacement market, while LI ion battery segment would expand from current levels. With incorporation of Q2Fy24 performance and introduction of FY26 earnings estimates, we maintain a Buy rating on the stock with unchanged PT of Rs 717 account of expectation of healthy traction in replacement, soft RM cost trends and an opportunity to play in the Li-ion cell business.

Key Risks

Volatile RM cost trend, delayed recovery in replacement demand and a rise in competition are key risks. Along with that the company is investing heavily in Li ion project and hence carries a project execution risk with uncertainty of demand.

Valuation (Standalone) Rs cr

Particulars	FY22	FY23	FY24E	FY25E	FY26E
Revenues (Rs cr)	8,696	10,386	11,425	12,567	13,824
Growth (%)	21.6	19.4	10.0	10.0	10.0
AEBIDTA (Rs cr)	1,023	1,355	1,519	1,697	1,935
OPM (%)	11.8	13.0	13.3	13.5	14.0
Adj Net Profit (Rs cr)	511	742	847	944	1,092
Growth (%)	-21.0	45.2	14.0	11.5	15.6
AEPS	29.9	43.5	49.6	55.3	63.9
P/E (x)	20.6	14.2	12.5	11.2	9.7
P/BV (x)	2.3	2.0	1.7	1.5	1.3
EV/EBIDTA (x)	10.2	7.4	6.4	5.4	4.3
ROE (%)	11.7	15.1	14.9	14.6	14.9
ROCE (%)	11.9	15.3	15.2	14.9	15.1

Source: Company; Sharekhan estimates

Q2FY24 performance

- Aftermarket segment registered 8% y-o-y growth, while exports and OEM segment registered mere 2-3% y-o-y growth.
- The export volumes were impacted due to change in the name of the company (legal reasons) and volumes would be delivered in coming quarter.
- Four-wheeler segment grew 7% y-o-y, while two wheeler segment registered a 9% y-o-y growth.
- Industrial segment has registered 8-9% y-o-y growth.
- Cost savings in raw materials supported margins, but there were increased expenses due to a fire incident, insurance premiums, consultant fees, and warranty expenses.
- High power costs have largely stabilized on commencement of solar power projects.

New energy business

- The business doubled its revenue year-on-year in both battery packs and charger segments.
- It clocked a turnover of Rs 150 crore in Q2FY24 compared to Rs 108 crore in Q1FY24.
- Amara plans to expand its new energy business beyond 3-wheelers.
- Currently new energy business is delivering 7-8% EBIDTA margin but there is room for expansion in EBITDA margin once the indigenization level would increase.
- Amara is open to collaborate with a large technology player if it requires to grow in new technology space.

Others

- Amara completed the acquisition of charging business, which would enhance its capabilities to offer charging solutions.
- Plastic business integration is nearing completion.
- First phase of recycling plant with capacity of 1 lakh tonnes is expected to start by Q1 FY25. This would increase the inhouse recycled lead procurement for the company.

Outlook

- Amara aims to maintain 35-36% market share in OEM space.
- The management expects a 6-7% volume growth in four-wheeler after market segment and low double digit volume growth in two-wheeler aftermarket in FY24.
- Amara targets for a 10% revenue growth in FY24.
- Company may opt to participate for PLI scheme based on the favourable conditions for the same.
- Raw material price trend is expected to stable for next two quarters.

Change in earnings estimates Rs cr

Particulars	New		Earlier		% change		Introduction
	FY24E	FY25E	FY24E	FY25E	FY24E	FY25E	FY26E
Revenue	11,425	12,567	11,425	12,567	-	-	13824
EBITDA	1,519	1,697	1,519	1,697	-	-	1935
EBITDA margin (%)	13.3	13.5	13.3	13.5			14.0
PAT	847	944	847	944	-	-	1092
EPS (Rs)	49.6	55.3	49.6	55.3	-	-	63.9

Source: Company; Sharekhan Research

Results (Standalone) Rs cr

Particulars	Q2FY24	Q2FY23	Y-o-Y %	Q1FY24	Q-o-Q %
Net sales	2,811	2,699	4.1	2,770	1.5
Total operating expenses	2,414	2,339	3.2	2,416	(0.1)
EBITDA	397	360	10.2	353	12.3
Depreciation	115	102	12.7	111	3.4
Interest	6	5	14.5	6	10.5
Other Income	28	24	16.3	22	27.7
PBT	293	277	6.1	258	13.6
Tax	79	74	6.4	66	20.1
RPAT	214	202	6.0	192	11.3
Adjusted PAT	224	202	11.0	192	16.5
Adjusted EPS	13.1	11.8	10.9	11.3	16.5

Source: Company; Sharekhan Research

Key Ratios (Standalone) Rs cr

Particulars	Q2FY24	Q2FY23	Y-o-Y (bps)	Q1FY24	Q-o-Q (bps)
Gross margin (%)	31.6	30.5	110	28.9	270
EBIDTA margin (%)	14.1	13.3	80	12.8	140
Net profit margin (%)	8.0	7.5	50	6.9	100
Effective tax rate (%)	27.0	26.9	10	25.5	150

Source: Company; Sharekhan Research

Outlook and Valuation

■ Sector Outlook – Demand is picking up in the automotive and industrial sector

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

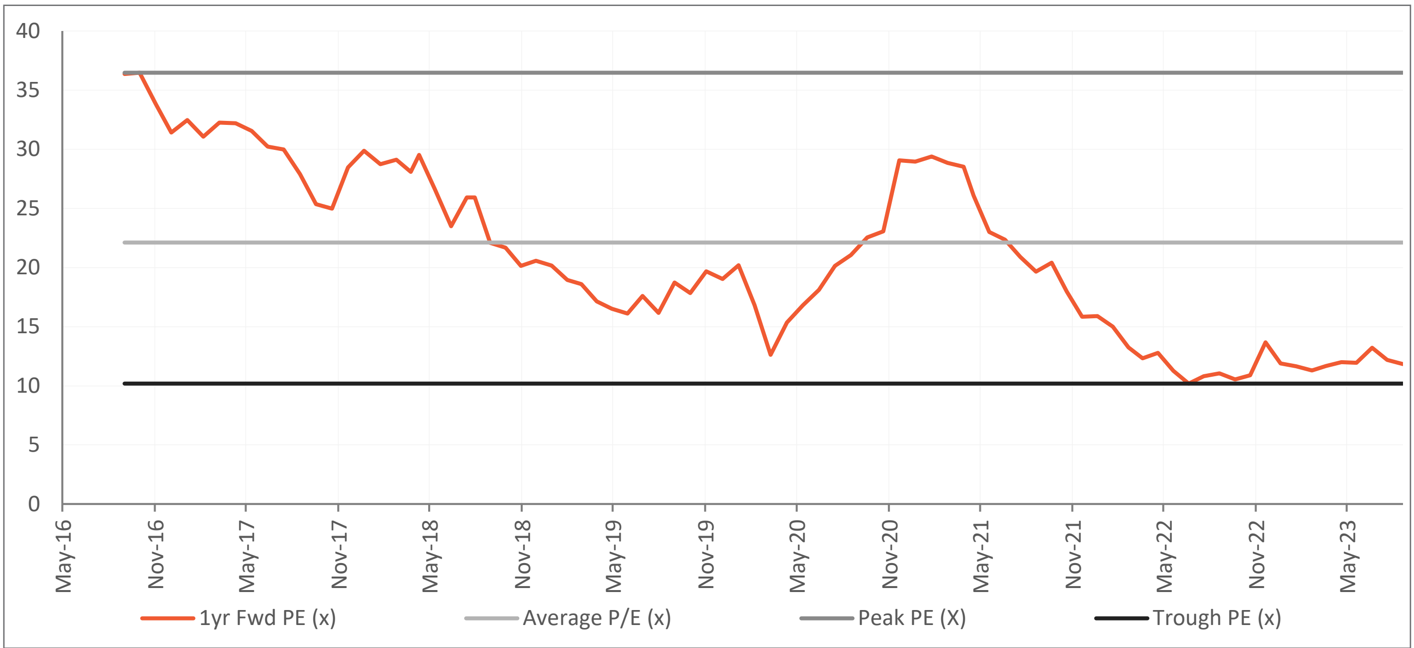
■ Company Outlook – Set for a steady ride

We expect Amara to continue to outpace the organised lead-acid battery industry, led by new client acquisitions, new product launches, and benefit from its extensive distribution network. Current capacities (batteries): 4W – 50 million, 2W- 30 million, industrial batteries – 2.3bnAh. The company has a large distribution network comprising over 1 lakh plus point of sales, 1000 plus power zone retail stores and 2000 plus extensive service hubs. The company has a strong long-term revenue visibility, given its focus on the aftermarket segment. Further the company is investing in Li ion battery cell manufacturing to drive its long-term growth.

■ Valuation – Maintain Buy with an unchanged PT of Rs.717

Despite subdued performance in OEM and export segments, Amara surpassed our AEBITDA margin expectations and reported 140 bps q-o-q expansion in EBITDA margin on account of benign RM cost trend. Further, the management is expecting 10% revenue growth for FY24 which is in line with our expectations. New energy business is registering healthy traction and the management indicates that profitability in new energy may improve further on increase in localisation. Merger of the plastic business with the company is on track. The merger of the plastic business would be margin and EPS accretive. Further, the lithium ion (Li-ion) battery project is expected to begin deliveries from FY2026. We believe that lead acid batteries to continue to remain in demand for the next few years in the replacement market, while LI ion battery segment would expand from current levels. With incorporation of Q2Fy24 performance and introduction of FY26 earnings estimates, we maintain a Buy rating on the stock with unchanged PT of Rs 717 account of expectation of healthy traction in replacement, soft RM cost trends and an opportunity to play in the Li-ion cell business.

One-year forward P/E (x) band



Source: Sharekhan Research

About company

Amara is the flagship company of 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 automotive space. In the automotive segment, the company makes batteries for 4Ws and 2Ws and caters to the OEM as well as aftermarket segments. 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, the UPS sector (OEM and replacement), Indian Railways, and to power, oil, and gas segments, among others. The company has a commendable share in the telecom and UPS batteries segment. Amara's manufacturing plants are located in the Chittor district in Andhra Pradesh and are equipped with state-of-the-art manufacturing plants.

Investment theme

Amara is one of the leading battery manufacturers in the duopolistic Indian lead acid battery space. The company is present in the automobile as well as industrial segments. Having a strong brand equity and extensive distribution network, we expect Amara to grow strongly in the battery industry. The company is working on several cost-control measures to improve profitability, such as increasing backward integration, diversifying the supplier base, enhancing automation, increasing the share of renewable power, and enhancing digital initiatives. Amara is also upgrading its technology and working on import substitution of raw materials to enable cost reduction. We expect the company to outperform the battery industry, driven by new client additions in the OEM space and market share gains in the auto replacement segment, driven by network expansion.

Key Risks

- A steep rise in lead prices, a key raw material, can impact profitability.
- Delay in completion or failure LI ion project may impact its future growth potential

Additional Data

Key management personnel

Jayadev Galla	CEO MD
Delli Babu Y	Chief Financial Officer
Vikas Sabarwal	Compnay Secretary & Compliance officer

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Rngalla Family Pvt Ltd	28.06
2	Clarios ARBL Holding LLP	14.00
3	Nalanda India Equity Fund Ltd	9.88
4	Life Insurance Corporation of India	7.23
5	Kotak Mahindra Asset Management Co Ltd/India	3.74
6	Vanguard Group Inc/The	2.83
7	Nippon Life India Asset Management Ltd	1.21
8	BlackRock Inc	1.14
9	Dimensional Fund Advisors LP	1.11
10	Norges Bank	0.67

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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