December 29, 2014

Tyre Sector

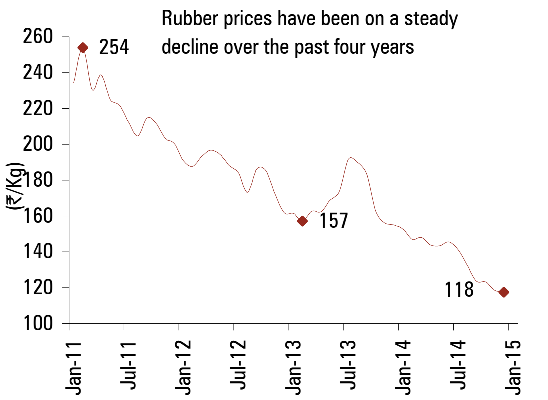
Sector View

Overweight

Stocks performance (returns as on December 29, 2014)

	Return (%)		
Company	1 month	3 months	1 year
BSE Sensex	-3	3	30
BSE Auto	-1	4	52
JK Tyres	3	38	337
Apollo Tyres	25	4	225
Balkrishna Industries	-6	-20	91
Ceat	-7	13	179
MRF Tyres	12	20	87
Goodyear India	9	39	113

Natural rubber price trend …



Prices of natural rubber is of RSS-4 grade

Natural rubber estimates (₹/kg)

	FY15E		FY16E	
	Old	Revised	Old	Revised
JK Tyres	153	153	155	155
Apollo Tyres	143	143	143	143
Balkrishna Industries	136	136	137	137

Standalone: Apollo Tyres, JK Tyres

EBIDTA margins movement (%)

	Q3FY14	Q4FY14	Q1FY14	Q2FY14
JK Tyres	10.8	10.0	10.3	12.4
Apollo Tyres	14.0	14.3	13.2	14.9
Balkrishna Industries	25.9	25.8	24.8	23.5

Research Analyst

Nishant Vass
nishant.vass@icicisecurities.com

Focus shifts to dissect future demand trends

In the auto ancillary universe, tyre companies have enjoyed possibly a *unique sweet spot* keeping in mind both demand and cost angles. Demand growth remains tepid throughout in domestic automotive market with major expectations of growth in coming periods. On the cost side, global rubber prices have spiralled downward, benchmark Bangkok RSS-4 rubber prices declined to <$1.6-1.7 levels ($2.2/kg in March).

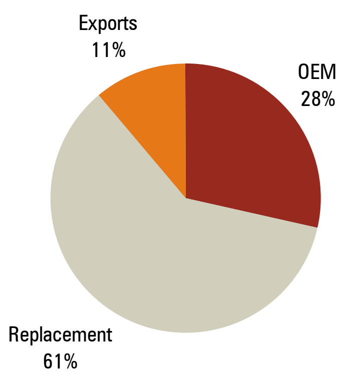
We believe the price fall has seen the worst and investor focus needs to shift away from costs. Thus, in this series of tyre sector analysis, we focus on possible demand pockets that could provide the thrust to sales!

Demand outlook:

Indian tyre market:

The size of the Indian tyre industry (production), as per our analysis, is estimated at ~ ₹ 46,000 crore (FY14) with exports contributing ~9-10% of the stated industry size. In terms of total tonnage, we estimate the industry at ~ 1.6 million MT, in terms of production volume with exports at ~7-8% of the same. The market size of the domestic tyre industry, in value terms, has grown at a CAGR of ~12% FY10-14P. However, in the recent past, the CAGR has been a meagre 3% in FY12-14P, mainly driven by mixed trends in automotive growth.

Exhibit 1: India tyre sales breakup



Source: Company, ATMA, CEAT PD, ICICIdirect.com Research

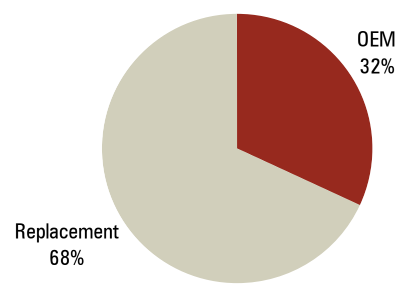
The key question is which pockets would lead the demand?

On the basis of end-user categories:

Tyre demand originates from two end-user categories, namely OEMs and the replacement segment. Consumption by OEMs is dependant on fresh vehicle sales trend while the replacement segment is linked to economic growth, usage characteristics and replacement cycles. On an overall basis, demand from the replacement segment always dominates the Indian tyre market contributing ~68% of demand, in terms of tonnage. The major reason for high replacement share is due to the fact that the number of registered vehicles/annual sales remains at ~10 x at close to ~20.3 crore registered vehicles (our estimates) vis-à-vis ~2.1 crore annual vehicle sales.

However, in recent years, FY13/14, the demand has been hurt by weak automobile demand from the OEMs side, resulting in an average de-growth of ~5% in OEM tyre consumption in India. On the other hand, tyre consumption by the replacement segment has grown on average by ~5-6% in the same period providing relief to overall growth. On an overall basis, growth has been ~2-3% from a tonnage perspective in the domestic market.

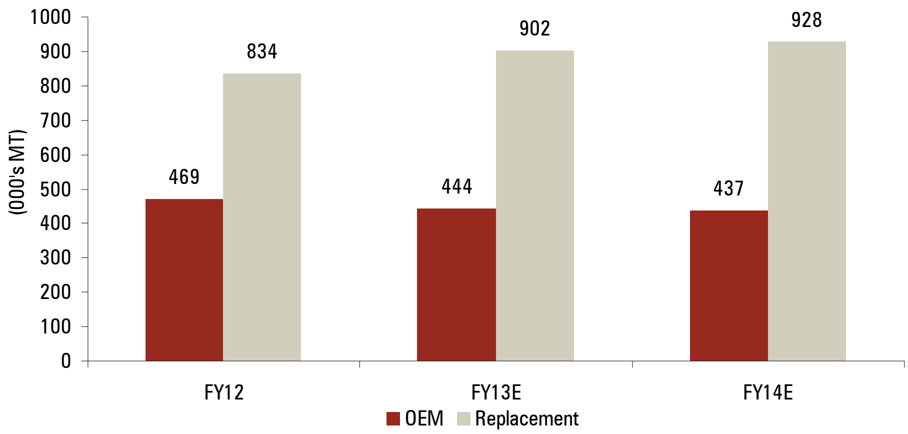
Exhibit 2: India share of sales between OEM & replacement



Source: Company, ATMA, CEAT PD, ICICIdirect.com Research

We expect the overall domestic tyre industry to grow at 9-11% in FY16E as OEM demand is expected to grow ~14-15% while replacement demand may stay at ~6-8%. In the current year, replacement demand has mitigated the overall tepid nature in OE demand. We believe the overall industry share of replacement and OEM would fall to ~65%, 35% from ~68%, 32%, respectively, as volume growth is going to be faster in the latter.

Exhibit 3: Domestic share of sales between OEM & replacement

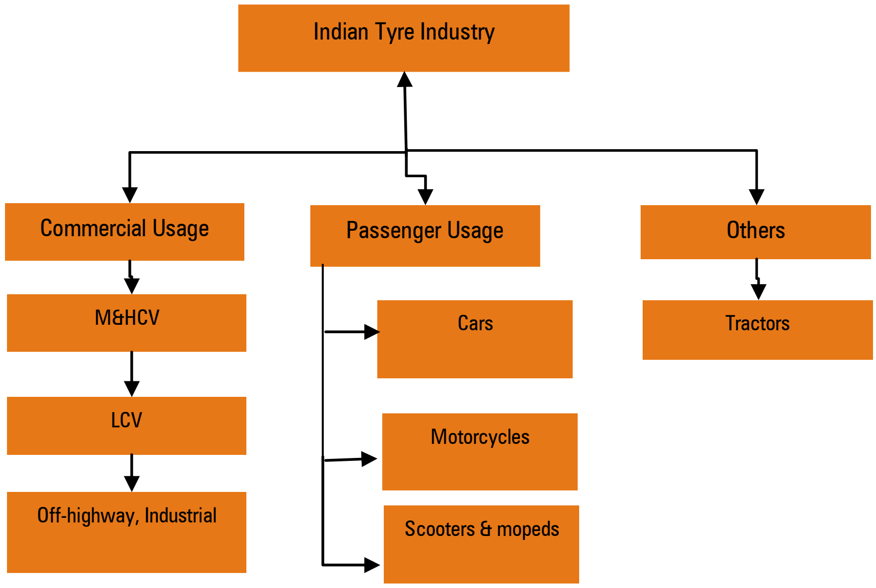


Source: Company, ATMA, CEAT PD, ICICIdirect.com Research

On basis of product categories:

The Indian tyre industry can be broadly divided into three broad product categories, namely, commercial vehicles (CV), passenger vehicles (PV), two-wheelers (2-W) and others. The structure of the Indian tyre industry can be illustrated as follows:

Exhibit 4: Product category wise break-up of Indian tyre industry



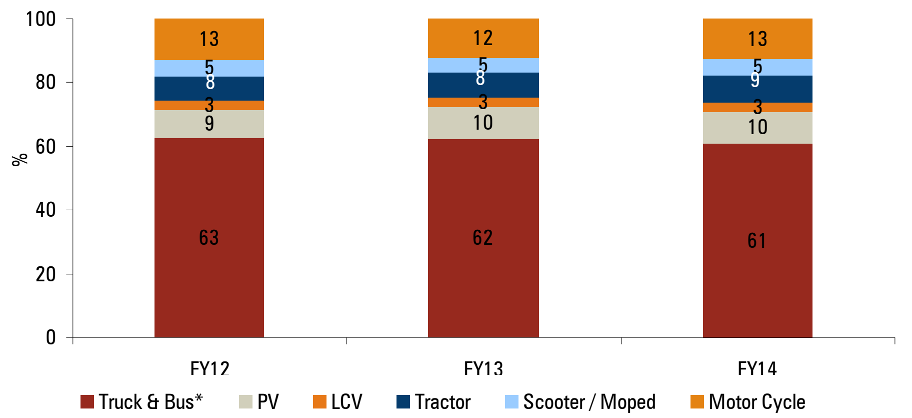
Source: Company, ATMA, CEAT PD, ICICIdirect.com Research

On the product side, the demand recovery is showing some green shoots that are being led by the M&HCV space (~12% production growth YTD) while PV (~3% YTD production growth) is also showing slow signs of a revival. In the 2-W segment, demand remains better off (~13% YTD production growth) among passenger usage. However, there are pockets that have underperformed like tractors, LCV (down 5%, 12% YTD) respectively.

We believe the economic pick-up is catalysing the higher tonnage (>20 T) space in the M&HCV space that had seen a severe decline in previous years. We still believe this space would witness the strongest growth in FY15E, FY16E and FY17E. From a tyre manufacturer's perspective, another parameter that remains very crucial is the fact that radialisation is a key trend that will grow rapidly in the truck & bus side (TBR). The industry expects the same to rise from ~28-30% currently to ~50% in a couple of years. Thus, players with higher market share and capacity in the TBR space like JK Tyres, Apollo Tyres (market share between these two stands at ~60% in the TBR space) would stand to potentially gain strongly. On the OEM M&HCV front, we expect industry volumes to witness ~20-25% growth in FY16E while radialisation change could incrementally also push up replacement demand.

On other segments, the pick-up in tyre demand is expected to improve non-linearly from the OEM side from FY16E onwards. Relative outperformance on the OEM PV front (~15% YoY) growth is expected along with stable (8-10% YoY) growth in the 2-W space. Tractors remain difficult to forecast considering various outliers from monsoons to minimum support prices still considering the weaker base year expectation of ~10% growth are not unfounded. We expect the overall tyre industry to grow between 9% and 11% in terms of volumes in FY16E.

Exhibit 5: India share of sales between OEM & replacement

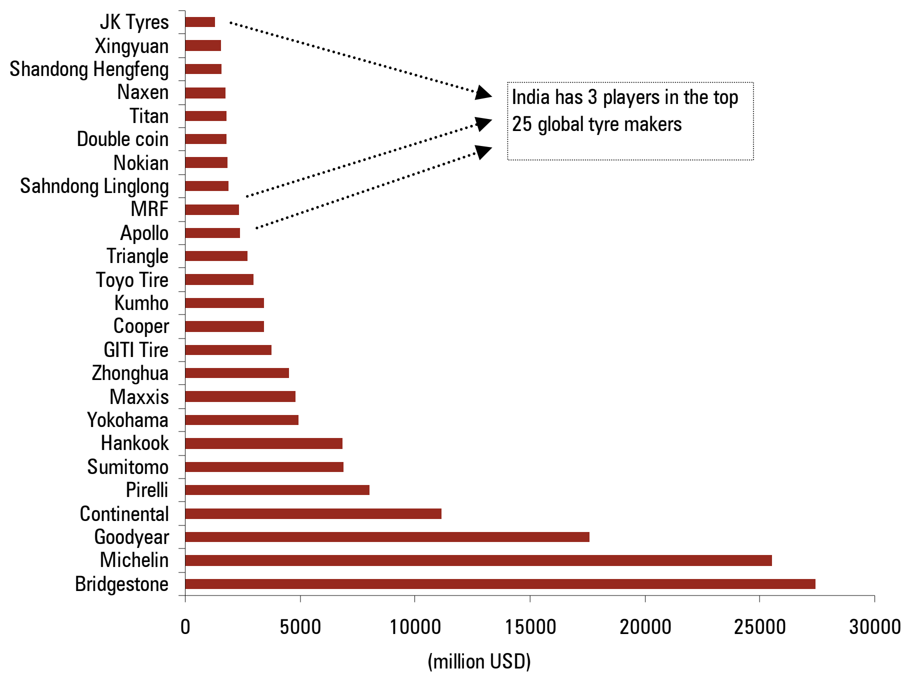


Source: Company, ATMA, CEAT PD, ICICIdirect.com Research

Global tyre market & exports

On the demand side, global studies and major manufacturers' commentary suggests automotive tyre demand will grow ~4-5% in volume terms. This would be split with demand rising well in the North American region while Europe and Japan would remain sluggish. Emerging markets like India and China are expected to see a moderate recovery.

Exhibit 6: Global companies by revenues in AY14*

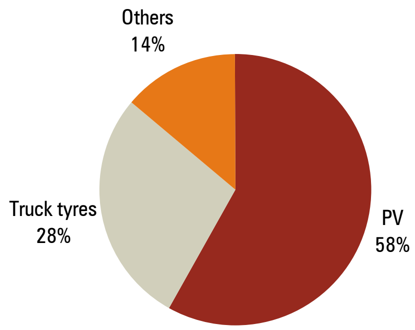


*Source: Company, CEAT PD ICICIdirect.com Research *AY14 ~Accounting Year*

In terms of product categories, the passenger cars and utility vehicles category represented a majority of the global tyre market, in terms of sales value, in FY14, followed by the M&HCVs category, which contributed ~28% of the global tyre sales.

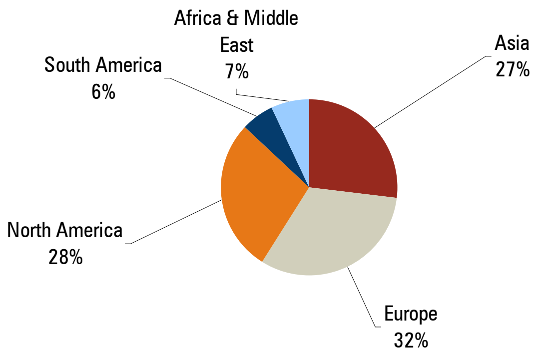
The production volume of the passenger car and utility vehicle tyres amounted to ~ 1,100 million units in CY09, with ~ 32% contributed by tyre manufacturers based in Europe. The following chart illustrates the breakdown of production volume of passenger car and utility vehicle tyres, by geographical base of manufacturers, in terms of units, in CY09.

Exhibit 7: India share of sales between OEM & replacement



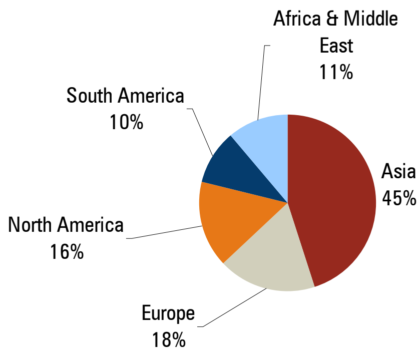
Source: Company, ATMA, CEAT PD, ICICIdirect.com Research

Exhibit 8: Passenger vehicle global sales share



Source: Company, ATMA, CEAT PD, ICICIdirect.com Research

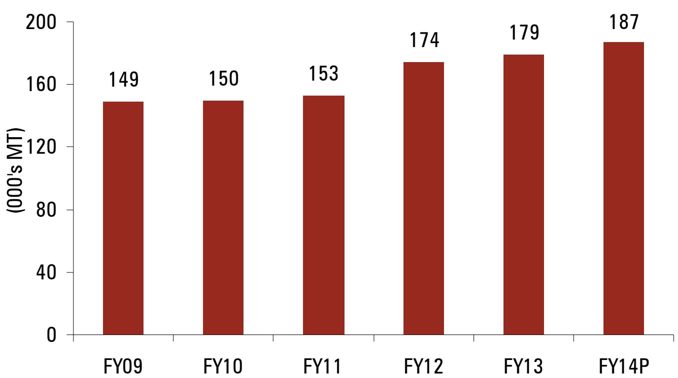
Exhibit 9: Commercial vehicle global sales share



Source: Company, ATMA, CEAT PD, ICICIdirect.com Research

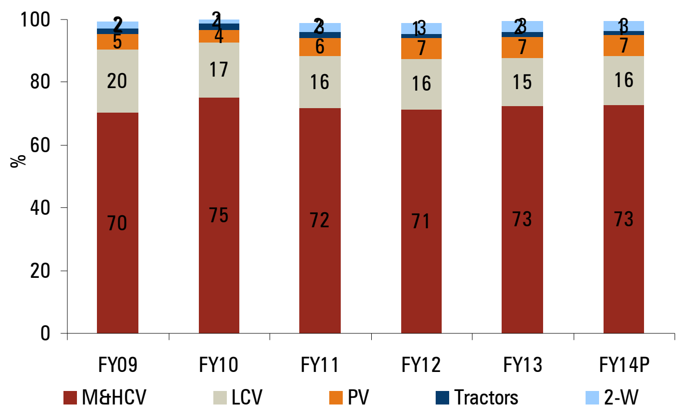
Indian exports of tyres are largely made to developing countries, such as the Asean region, Middle East and Africa. In FY13, ~ 40% of exports were made to Asean countries while ~21%, 17% were made to Middle East and Africa, respectively.

Exhibit 10: Trend of total exports from India



Source: Company, ATMA, CEAT PD, ICICIdirect.com Research

Exhibit 11: Share of product mix in exports from India



Source: Company, ATMA, CEAT PD, ICICIdirect.com Research

Other key tyre sector parameters and outlook for the same

Raw material trends: Rubber prices continued to fall (down 11% QoQ). Though auguring well for OEMs, this created a stir in terms of farmer's sustenance in India. Therefore, due to the farmer stir we saw a new 5% purchase tax being levied on Kerala rubber till March 2014, which was accepted by ATMA. However, the key point remains that considering that tapping season is nearly over and inventory remains high at manufacturers' end this increase in cost probably would have a limited impact in terms of overall cost. The global production and demand trends still remain in favour of a glut in the medium-term. However, considering the price fall has been steep, we believe RSS-4 prices would improve to ~$1.8/kg (Bangkok), ~₹ 135/-140kg in the domestic market.

Exhibit 12: World natural rubber production and consumption trends

Rubber production (000's MT)	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Natural rubber	6,811	6,913	7,317	7,986	8,726	8,921	9,850	10,057	10,098	9,723	10,393	11,230	11,603	12,036
Synthetic rubber	10,870	10,483	10,906	11,414	11,979	12,025	12,700	13,367	12,738	12,393	14,115	15,073	15,142	15,495
Total rubber	17,681	17,396	18,223	19,400	20,705	20,946	22,550	23,424	22,836	22,116	24,508	26,303	26,745	27,531
Rubber consumption (000's MT)	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Natural rubber	7,108	7,039	7,515	7,797	8,562	9,049	9,513	10,133	10,181	9,361	10,773	11,007	11,027	11,322
Synthetic rubber	10,830	10,253	10,679	11,177	11,693	11,731	12,434	13,087	12,517	12,129	13,984	14,803	14,925	15,483
Total rubber	17,938	17,292	18,194	18,974	20,255	20,780	21,947	23,220	22,698	21,490	24,757	25,810	25,952	26,805
Supply demand surplus/deficit	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Natural rubber	-297	-126	-198	189	164	-128	337	-76	-83	362	-380	223	576	714
Synthetic rubber	40	230	227	237	286	294	266	280	221	264	131	270	217	12
Total rubber	-257	104	29	426	450	166	603	204	138	626	-249	493	793	726

Source: International Rubber Study Group (IRSG), ICICIdirect.com Research

As per the study conducted by the International Rubber Study Group, natural rubber production has doubled from the levels in the year 2000. In the past 14 years, rubber production has been surplus for six years. However, the supply demand surplus has not exceeded two years until 2013, which has seen increasing surpluses. Also, in 2014, the same situation is likely to persist. Furthermore, for the next 15-18 months, natural rubber prices are likely to remain muted as supply outstrips demand

For Q3FY14, domestic tyre manufacturers saw another quarter of favourable raw material prices mostly as natural rubber (NR) prices saw a decline to ~₹ 120/kg (QoQ 10% fall) in the domestic market. The price fall has been faster than the global peers as supplies increased post monsoons. As the tapping season comes to a close and tyre makers are stocked with inventory, we feel prices may remain moderately higher in the coming quarter if supply remains tight. However, the recent crude price decline (~25% QoQ on average basis to ~$75/bbl) may see crude linked derivatives like synthetic rubber and nylon tyre cord softening. Rubber contributes ~50% in volume terms and ~55% of the total raw material cost for tyre companies, depending on the product mix. Crude-linked derivatives constitute another 20-25% of the raw material basket for tyre companies.

Exhibit 13: Sensitivity analysis

	EBITDA margin change (%) FY15E			EPS impact (%) FY15E		
NR* price change (₹/Kg)	JK Tyres`	Apollo Tyres`	Balkrishna Industries	JK Tyres`	Apollo Tyres`	Balkrishna Industries
20	-4	-4	-2	-60	-40	-13
10	-2	-2	-1	(30)	(20)	(7)
0	0	0	0	0	0	0
-10	2	2	1	30	20	7
-20	4	4	2	60	40	13

Source: Company, ICICIdirect.com Research `standalone

As per our analysis, for every ₹ 10 change in natural rubber prices (other things remaining constant), EBITDA margins could likely change in varying degrees from 100 bps to 400 bps, clearly showing that Balkrishna Industries would benefit the least from a rubber price fall. On the earnings front, JK Tyres is expected to see ~30% change on every ₹ 10 change in natural rubber prices.

Pricing discipline in industry: On the pricing front, so far, even with the slowdown and natural rubber price corrections, the pricing discipline shown by the tyre industry in the replacement market has been strong. On the OEM side, however, pricing contracts are more quarterly or bi-annual, which would see price reductions for the OEM side of the business. Thus, the demand increase in terms of OEMs would have twin impacts. One would be on the increase in utilisation and mix improvements. However, this would be coupled with a decline in terms of overall blended pricing as we witnessed a higher OEM share. In this also, companies that are placed in the TBR space would benefit as pricing in terms of OEM would be higher (~15-25%) vis-à-vis a similar bias product.

Balkrishna Industries (BALIND)

₹ 600

New capacity to aid OTR segment growth!

Rating matrix

Rating	:	Buy
Target	:	₹ 734
Target Period	:	12-15 months
Potential Upside	:	22%

What's Changed?

Target	Unchanged
EPS FY16E	Unchanged
EPS FY17E	Unchanged
Rating	Changed from HOLD to BUY

Quarterly Performance

(₹ Crore)	Q2FY15	Q2FY14	YoY	Q1FY15	QoQ
Revenues	881.3	839.6	5.0	959.0	-8.1
EBITDA	207.5	202.4	2.5	236.6	-12.3
EBITDA (%)	23.5	24.1	-56 bps	24.7	-113 bps
Reported PAT	90.2	107.9	-16.5	113.4	-20.5

Key Financials

₹ Crore	FY14	FY15E	FY16E	FY17E
Net Sales	3,536	3,699	4,269	5,100
EBITDA	893.9	903.2	1,099.0	1,268.4
Net Profit	488.4	426.6	545.6	645.4
EPS (₹)	50.5	44.1	56.5	66.8

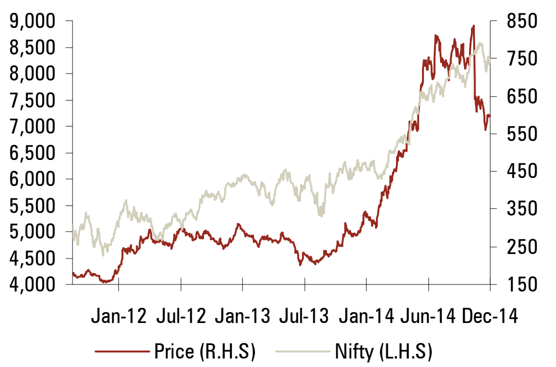
Valuation summary

	FY14	FY15E	FY16E	FY17E
P/E (x)	11.9	13.6	10.6	9.0
Tgt P/E (x)	14.5	16.6	13.0	11.0
EV/EBITDA (x)	9.1	8.7	6.6	5.4
P/BV (x)	3.1	2.5	2.1	1.7
RoNW (%)	25.9	18.7	19.5	18.9
RoCE (%)	17.2	14.4	17.6	19.9

Stock data

Market Capitalization (₹ Crore)	₹ 5799.5 Crore
Total Debt (FY14) (₹ Crore)	₹ 2344 Crore
Cash & Investments (FY14) (₹ Crore)	₹ 9.8 Crore
EV (₹ Crore)	₹ 8133.7 Crore
52 week H/L (₹)	856/294
Equity capital (₹ crore)	₹ 19.3 Crore
Face value (₹)	₹ 2

Price performance



Research Analyst

Nishant Vass
nishant.vass@icicisecurities.com

Focused OHT player with room to increase market share in global pie

BIL is a focused off-highway tyre (OHT) manufacturer with contribution of agricultural and OTR segments at 63% and 37%, respectively. With the OHT segment forming only 10-15% of revenues for global players like Bridgestone and Michelin, BIL's focus on this niche segment augurs well for the company as it currently enjoys ~5% market share in a ~$15-billion global market. Also, the only focused global player, Titan commands a hefty brand premium (~25%) over BIL's products. Hence, this outlines the headroom for volume growth for BIL in this highly capital and labour intensive segment characterised by large number of SKUs and frequent mould changes due to high degree of customisation.

Best in-class margins led by significant labour cost arbitrage

Despite selling at ~25% discount to the industry leader, BIL enjoys strong margins as its products are competitive due to lower labour costs in India, compared to significantly higher wage and benefits/entitlement structure present in European facilities. For BIL, labour costs form 4-5% of revenue whereas for companies like Titan having plants in North America, labour costs are ~20% of revenues. In the past few quarters, BIL has benefitted from a weakness in natural rubber prices (which form 40% of total raw material cost). Also, with ~90% of revenues coming from exports, the weakness in the rupee has aided margins. Going ahead, as the new Bhuj capacity ramps up, higher volumes will offset the increase in other expenses due to initial start-up costs.

Capacity expansion to cater to OTR segment, extend geographical reach

BIL is setting up a plant at Bhuj with a capacity of 140,000 MT, which will be fully commissioned by the end of FY16E in a phased manner. This would take BIL's total capacity to 300,000 MT in FY16E and cater mainly to the OTR segment (that forms only 37% of revenues) where BIL's presence was constrained by a lack of capacity. The main focus is likely to be on large diameter tyres for use in the construction and mining segments. The new capacity will also facilitate an entry in markets like CIS, Russia where management expects strong offtake in coming years.

RM price benefits vs. currency swings, OEM share increases

BIL's performance on the margins front over the past year has been best in class with margins scaling beyond the highs of 2009-10. This has been fuelled by favourable raw material prices. Going forward, the outlook on raw material prices remains favourable but global currency swings may affect realisations. On the business side, the strategy has shifted to a more OEM centric approach (lower margin, higher costs in initial phase). This may lead to a modification of the business model. BIL is a modest working capital requiring company supplying on dedicated replacement orders that could now change as it moves towards warehousing and just in time (JITs) for OEMs.

Earnings take knock on uncertainty but investors need to be patient!

BIL's huge capacity has raised fears it may lead to deteriorating earnings and return ratios in next two years as a global recovery remains elusive and pricing trends remain extremely weak. We give BIL the benefit of doubt and expect it to clock strong volumes of ~180,000, 210,000 MT in FY16E, FY17E, respectively. We like the export dominated, niche play that BIL offers. We value BIL at 11.5x FY17E rolling EPS, maintain our target price of ₹ 734. However, recent sharp price fall makes it attractive in terms of risk reward and, thus, we upgrade BIL to BUY from HOLD.

Financial summary

Profit and loss statement				₹ Crore
(Year-end March)	FY14	FY15E	FY16E	FY17E
Total operating Income	3,576.7	3,736.7	4,316.0	5,156.3
Growth (%)	12.1	4.5	15.5	19.5
Raw Material Expenses	1,721.0	1,880.1	2,147.4	2,603.0
Employee Expenses	138.6	179.8	196.2	231.8
Other Expenses	732.3	835.4	883.5	1,053.1
Total Operating Expenditure	2,682.8	2,833.6	3,217.0	3,887.9
EBITDA	893.9	903.2	1,099.0	1,268.4
Growth (%)	34.5	1.0	21.7	15.4
Depreciation	165.0	237.3	266.2	287.6
Interest	25.5	49.5	48.3	41.1
Other Income	13.8	16.7	30.0	23.7
PBT	717.8	636.3	814.4	963.3
Total Tax	229.3	209.8	268.8	317.9
PAT	488.4	426.6	545.6	645.4
Growth (%)	37.3	-12.7	27.9	18.3
EPS (₹)	50.5	44.1	56.5	66.8

Source: Company, ICICIdirect.com Research

Cash flow statement				₹ Crore
(Year-end March)	FY14	FY15E	FY16E	FY17E
Profit after Tax	488.4	426.6	545.6	645.4
Add: Depreciation	165.0	237.3	266.2	287.6
(Inc)/dec in Current Assets	-234.5	-51.2	-302.3	-283.7
Inc/(dec) in CL and Provisions	120.2	-8.2	82.2	94.5
CF from operating activities	539.0	604.5	591.7	743.9
(Inc)/dec in Investments	0.0	0.0	0.0	0.0
(Inc)/dec in Fixed Assets	-747.6	-251.0	-300.6	-300.0
Others	-305.7	-35.0	354.9	4.9
CF from investing activities	-1,053.4	-286.0	54.3	-295.1
Inc/(dec) in loan funds	280.4	0.0	-410.0	-410.0
Dividend paid & dividend tax	-22.5	-28.2	-28.2	-39.4
Others	0.0	0.0	0.0	0.0
CF from financing activities	257.9	-28.2	-438.2	-449.4
Net Cash flow	-256.4	290.4	207.8	-0.6
Opening Cash	266.2	9.8	300.2	508.0
Closing Cash	9.8	300.2	508.0	507.4

Source: Company, ICICIdirect.com Research

Balance sheet				₹ Crore
(Year-end March)	FY14	FY15E	FY16E	FY17E
Liabilities				
Equity Capital	19.3	19.3	19.3	19.3
Reserve and Surplus	1,865.6	2,264.0	2,781.5	3,387.5
Total Shareholders funds	1,884.9	2,283.3	2,800.8	3,406.8
Total Debt	2,344.0	2,344.0	1,934.0	1,524.0
Deferred Tax Liability	172.2	187.2	202.2	217.2
Minority Interest / Others	40.4	50.4	60.4	70.4
Total Liabilities	4,441.5	4,864.9	4,997.4	5,218.4
Assets				
Gross Block	2,996.9	3,573.2	3,873.2	4,173.2
Less: Acc Depreciation	668.2	905.0	1,170.5	1,457.5
Net Block	2,328.7	2,668.2	2,702.7	2,715.8
Capital WIP	476.3	150.0	150.0	150.0
Total Fixed Assets	2,805.9	2,819.5	2,853.9	2,866.3
Investments	34.1	427.4	467.8	117.8
Inventory	529.1	545.2	694.5	786.6
Debtors	618.5	638.5	736.8	880.3
Loans and Advances	273.9	275.1	332.9	362.9
Cash	9.8	300.2	508.0	507.4
Other current assets	0.2	14.0	10.9	29.0
Total Current Assets	1,431.5	1,773.0	2,283.1	2,566.2
Creditors	343.1	334.4	386.0	461.1
Provisions	28.4	27.7	31.9	38.1
Other current liabilities	0.0	0.0	0.0	0.0
Total Current Liabilities	432.6	424.4	506.6	601.1
Net Current Assets	998.9	1,348.6	1,776.6	1,965.1
Others	210.2	230.2	250.4	270.4
Application of Funds	4,441.5	4,864.9	4,997.4	5,218.4

Source: Company, ICICIdirect.com Research

Key ratios				
(Year-end March)	FY14	FY15E	FY16E	FY17E
Per share data (₹)				
EPS	50.5	44.1	56.5	66.8
Cash EPS	67.6	68.7	84.0	96.5
BV	195.0	236.2	289.8	352.5
DPS	2.0	2.5	2.5	3.5
Cash Per Share	1.0	31.1	52.6	52.5
Operating Ratios (%)				
EBITDA Margin	25.3	24.4	25.7	24.9
PBT / Net sales	20.3	17.2	19.1	18.9
PAT Margin	15.0	9.6	9.5	11.2
Inventory days	49.6	53.0	53.0	53.0
Debtor days	63.8	63.0	63.0	63.0
Creditor days	35.4	33.0	33.0	33.0
Return Ratios (%)				
RoE	25.9	18.7	19.5	18.9
RoCE	17.2	14.4	17.6	19.9
RoIC	11.8	10.3	13.2	14.8
Valuation Ratios (x)				
P/E	11.9	13.6	10.6	9.0
EV / EBITDA	9.1	8.7	6.6	5.4
EV / Net Sales	2.3	2.1	1.7	1.3
Market Cap / Sales	1.6	1.6	1.4	1.1
Price to Book Value	3.1	2.5	2.1	1.7
Solvency Ratios				
Debt/EBITDA	2.6	2.6	1.8	1.2
Debt / Equity	1.2	1.0	0.7	0.4
Current Ratio	3.3	4.2	4.5	4.3
Quick Ratio	3.3	3.5	3.5	3.4

Source: Company, ICICIdirect.com Research

Apollo Tyres (APOTYR)

₹ 218

Rating matrix

Rating	:	Buy
Target	:	₹ 275
Target Period	:	12 months
Potential Upside	:	26%

What's Changed?

Target	Unchanged
EPS FY16E	Unchanged
EPS FY17E	Unchanged
Rating	Unchanged

Quarterly Performance

(₹ Crore)	Q2FY15	Q2FY14	YoY	Q1FY15	QoQ
Revenues	3,315.2	3,433.5	-3.4	3,247.6	2.1
EBITDA	493.6	452.1	9.2	428.7	15.1
EBITDA (%)	14.9	13.2	172 bps	13.2	169 bps
Reported PAT	258.0	219.6	17.5	227.9	13.2

Key Financials

₹ Crore	FY14	FY15E	FY16E	FY17E
Net Sales	13,311	13,703	15,070	16,740
EBITDA	1,876.2	2,011.5	2,231.2	2,519.2
Net Profit	1,005.8	1,098.9	1,259.6	1,425.1
EPS (₹)	20.0	21.8	25.0	28.3

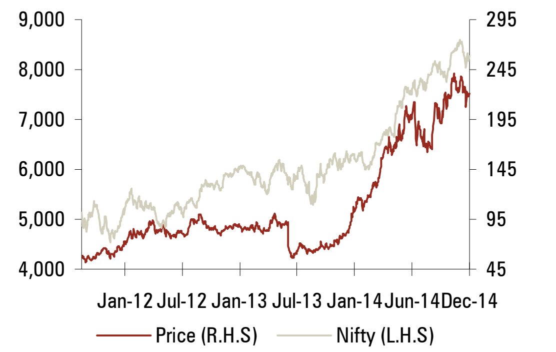
Valuation summary

	FY14	FY15E	FY16E	FY17E
P/E (x)	10.9	10.0	8.7	7.7
Tgt P/E (x)	13.8	12.6	11.0	9.7
EV/EBITDA (x)	6.4	6.1	5.5	4.9
P/BV (x)	2.4	2.0	1.6	1.3
RoNW (%)	22.0	19.5	18.5	17.4
RoCE (%)	23.7	20.0	18.7	17.7

Stock data

Particular	Amount
Market Capitalization (₹ Crore)	₹ 11126 Crore
Total Debt (FY14) (₹ Crore)	₹ 1613 Crore
Cash & Investments (FY14) (₹ Crore)	₹ 654 Crore
EV (₹ Crore)	₹ 11948 Crore
52 week H/L (₹)	243 / 97
Equity capital (₹ crore)	₹ 50.4 Crore
Face value (₹)	₹ 1

Price performance



Research Analyst

Nishant Vass
nishant.vass@icicisecurities.com

Capex in high margin businesses augurs well

ATL unique combo of domestic & global tyre play!

While the deal with Cooper failed to materialise, ATL's focus on geographically de-risking the business augurs well for the future. With the radialisation trend in the T&B segment likely to improve radial volumes, a revival in economic demand augurs well for domestic capacity utilisation levels that are at ~75%. With the European business doing well, capex planned for expanding capacity in Eastern Europe augurs well as existing capacity in Europe is operating at ~90% utilisation. We believe by benchmarking the R&D budget to industry leaders and focusing on corporate branding, the management is on the right track to become a serious competitor to global tyre players.

Major capacity addition in high margin segments major positive

Vredestein (more than a century old brand) is a highly profitable business for ATL specialising in high performance summer and winter tyres. VBV's operating margin profile (last 10 quarter average margins at ~18%) is far superior to that of the domestic business. The ~30% RoCE business is operating at ~90% capacity utilisation. With little scope to expand, the board's decision to set up a greenfield plant in Eastern Europe at an estimated spend of €500 million is on track to fatten ATL's bottomline even further. On the domestic front, a capex cycle revival is likely to aid tyre markers as the bulk of revenues are from the truck & bus (T&B) segment. Hence, ATL has embarked on capacity expansion at its Chennai TBR plant as the rapid rise of radialisation in the T&B segment is likely to create capacity shortfall (existing utilisation for TBR capacity ~80%).

Favourable raw material prices likely to keep margins firm!

In the domestic business, with raw material prices (especially rubber that represents >60% of total raw material cost for ATL) remaining favourable, ATL's margin profile is likely to remain stable. Also, with the fall in crude oil prices and crude-linked derivatives (synthetic rubber, chemicals, carbon black), there would be a significant reduction in the recipe cost for tyre manufacturers, thereby boosting margins. We also expect the pricing discipline shown by the industry in the past two years to continue, going forward, thereby aiding growth in profitability.

Economic recovery holds key for volume growth!

The improvement in profitability in the past couple of years has been largely on account of a decline in raw material costs even as volume growth has been low (driven by steady replacement demand). However, with expectation of an industrial recovery, volumes are also likely to improve for both OEMs and the replacement segments. Vredestein (VBV) has contributed handsomely to the overall profitability for ATL (~36% contribution to consolidated EBIT) and is likely to continue in the same vein as Europe also recovers after four or five years.

Strong business case for premium to historic multiples! Maintain BUY

With a low D/E profile, decent return ratios and strong operating cash flow visibility in the near term, ATL is placed much better in this business cycle vis-à-vis previous up cycles due to its largely diversified and global scale of business. This, we believe, lends additional room for valuation multiples to expand as the demand scenario improves and the outlook on raw material prices remains stable. Thus, we increase our valuation multiple, positioning ATL at a premium to peers and value ATL at 10x FY17E rolling EPS to arrive at a target price of ₹ 275. We maintain our BUY recommendation on the stock.

Financial summary

Profit and loss statement ₹ Crore

(Year-end March)	FY14	FY15E	FY16E	FY17E
Total operating Income	13,412.6	13,754.1	15,118.4	16,788.1
Growth (%)	4.8	2.5	9.9	11.0
Raw Material Expenses	7,772.0	7,805.1	8,730.8	9,720.0
Employee Expenses	1,614.6	1,672.7	1,725.0	1,877.4
Other Expenses	2,149.8	2,264.9	2,431.4	2,671.5
Total Operating Expenditure	11,536.4	11,742.7	12,887.2	14,268.9
EBITDA	1,876.2	2,011.5	2,231.2	2,519.2
Growth (%)	28.8	7.2	10.9	12.9
Depreciation	410.9	440.8	462.8	527.8
Interest	283.8	213.2	235.2	280.2
Other Income	97.8	143.1	204.2	254.5
PBT	1,232.6	1,500.5	1,737.3	1,965.7
Exceptional items	0.0	0.0	-46.8	0.0
Total Tax	226.9	401.6	477.8	540.6
PAT	1,005.8	1,098.9	1,259.6	1,425.1
Growth (%)	64.2	9.3	14.6	13.1
EPS (₹)	20.0	21.8	25.0	28.3

Source: Company, ICICIdirect.com Research

Cash flow statement ₹ Crore

(Year-end March)	FY14	FY15E	FY16E	FY17E
Profit after Tax	1,005.8	1,098.9	1,259.6	1,425.1
Add: Depreciation	410.9	440.8	462.8	527.8
(Inc)/dec in Current Assets	-187.8	-81.6	-582.5	-336.4
Inc/(dec) in CL and Provisions	304.8	-360.3	393.4	149.3
CF from operating activities	1,533.7	1,097.8	1,533.2	1,765.8
(Inc)/dec in Investments	0.0	0.0	0.0	0.0
(Inc)/dec in Fixed Assets	-423.9	-1,320.0	-1,420.0	-1,820.0
Others	78.9	-6.5	-50.0	-100.0
CF from investing activities	-345.0	-1,326.5	-1,470.0	-1,920.0
Issue/(Buy back) of Equity	0.0	0.0	0.0	0.0
Inc/(dec) in loan funds	-1,292.8	700.0	400.0	500.0
Dividend paid & dividend tax	-44.2	-50.1	-64.9	-76.7
Others	467.7	-99.4	0.0	0.0
CF from financing activities	-869.3	550.5	335.1	423.3
Net Cash flow	319.3	321.7	398.4	269.2
Opening Cash	334.8	654.1	975.9	1,374.2
Closing Cash	654.1	975.9	1,374.2	1,643.4

Source: Company, ICICIdirect.com Research

Balance sheet ₹ Crore

(Year-end March)	FY14	FY15E	FY16E	FY17E
Liabilities				
Equity Capital	50.4	50.4	50.4	50.4
Reserve and Surplus	4,513.5	5,562.9	6,757.6	8,106.0
Total Shareholders funds	4,563.9	5,613.3	6,808.0	8,156.4
Total Debt	1,613.4	2,213.4	2,613.4	3,113.4
Deferred Tax Liability	535.8	535.8	535.8	535.8
Total Liabilities	6,867.5	8,520.4	10,115.1	11,963.5
Assets				
Gross Block	9,169.3	9,769.3	10,469.3	12,769.3
Less: Acc Depreciation	4,812.3	5,214.6	5,636.4	6,120.9
Net Block	4,455.7	4,635.0	4,892.2	6,684.3
Capital WIP	46.5	746.5	1,446.5	946.5
Total Fixed Assets	4,502.2	5,381.5	6,338.7	7,630.8
Investments	63.7	73.7	123.7	223.7
Goodwill on consolidation	137.6	137.6	137.6	137.6
Inventory	2,066.4	2,063.3	2,395.9	2,557.3
Debtors	1,042.7	1,107.5	1,259.3	1,421.8
Loans and Advances	370.7	424.1	480.1	524.3
Other current assets	59.4	25.9	67.9	36.3
Cash	654.1	975.9	1,374.2	1,643.4
Total Current Assets	4,193.3	4,596.6	5,577.5	6,183.0
Creditors	1,253.8	1,201.4	1,280.0	1,421.8
Provisions	568.9	509.1	529.6	574.1
Total Current Liabilities	1,822.7	1,710.5	1,809.5	1,995.8
Net Current Assets	2,370.6	2,886.2	3,768.0	4,187.2
Application of Funds	6,867.5	8,520.4	10,115.1	11,963.5

Source: Company, ICICIdirect.com Research

Key ratios

(Year-end March)	FY14	FY15E	FY16E	FY17E
Per share data (₹)				
EPS	20.0	21.8	25.0	28.3
Cash EPS	28.1	30.5	34.2	38.7
BV	90.8	111.6	135.3	162.0
DPS	0.7	0.9	1.1	1.3
Cash Per Share	13.0	19.4	27.3	32.6
Operating Ratios (%)				
EBITDA Margin	14.1	14.7	14.8	15.0
PBT / Net sales	9.3	11.0	11.5	11.7
PAT Margin	8.0	5.0	3.4	4.8
Inventory days	56.2	55.0	54.0	54.0
Debtor days	28.6	29.5	30.5	31.0
Creditor days	34.4	32.0	31.0	31.0
Return Ratios (%)				
RoE	22.0	19.5	18.5	17.4
RoCE	23.7	20.0	18.7	17.7
RoIC	30.7	23.8	20.2	19.3
Valuation Ratios (x)				
P/E	10.9	10.0	8.7	7.7
EV / EBITDA	6.4	6.1	5.5	4.9
EV / Net Sales	0.9	0.9	0.8	0.7
Market Cap / Sales	0.8	0.8	0.7	0.7
Price to Book Value	2.4	2.0	1.6	1.3
Solvency Ratios				
Debt/Equity	0.4	0.4	0.4	0.4
Current Ratio	1.9	2.5	2.5	2.6
Quick Ratio	1.6	2.0	1.9	1.9

Source: Company, ICICIdirect.com Research

JK Tyres and Industries (JKIND) ₹ 132

Explosive CV radialisation + valuation safety

M&HCV radialisation trend on full throttle to benefit radial leader!

The CV tyre segment is clearly witnessing a secular radialisation trend with the share of radial tyres in the M&HCV segment increasing from 4% in FY07 to ~29% in FY14. Penetration of truck & bus radial tyres in the OEM segment is ~55% while the replacement segment radialisation currently stands at ~25%. JK Tyres' market share in India in the M&HCV TBR segment stands > 30% and in the passenger car radial segment > 12%. Going forward, as radialisation in the truck and bus segment increases rapidly, we believe JK Tyres' would be a major beneficiary leading to higher capacity utilisation levels in the TBR space.

Capex programme seems well-timed as economy on cusp of recovery

With expectations of a revival in the economy, JKTIL's capacity expansion plan seems to be perfectly timed to benefit from the economic recovery. We believe the government's focus on a revival of the capex cycle will benefit the truck segment, which forms the bulk of sales for tyre makers. Thus, capacity constraints faced by the company are likely to ease as the new facility will enhance TBR capacity by 8 lakh tyres per annum to 22.7 lakh and also increase the PCR capacity by 15 lakh tyres per annum to 97.9 lakh. Also, JKTIL is focusing strongly on exports as evidenced by strong growth (~doubling of exports from FY12 levels).

Favourable raw material prices amid strong pricing discipline

Natural rubber prices have declined to ~₹ 120/kg levels this year from the highs of ~₹ 250/kg in 2011. Rubber, which contributes ~60% of total raw material costs, thus swings the gross/operating margins. The major difference in this cycle vis-à-vis previous business cycle has been the pricing discipline shown by the industry, which has led to an increase in profitability for the overall industry. JKTIL's margins have also significantly improved to double digit levels due to the favourable impact of operating leverage as capacity utilisation levels have hit ~80%. Going ahead, with economic revival, capacity utilisation for most players is likely to remain high, thereby ensuring industry pricing discipline.

Tornel business to improve on increasing OEM penetration

On the Mexican business front, with penetration into OEMs like Nissan, Chrysler and Volkswagen, the business profile and market share are likely to improve in both Mexico and North American export markets. Enhancement of capacity at Tornel for increasing passenger car radial tyres is also likely to improve production from next year. Earnings consistency from the Tornel business is likely to smoothen earnings as dependency on the Indian market reduces slightly.

Alluring valuations in clear cyclical play give margin of safety!

With an expectation of a revival in capex cycle, we are optimistic about the revenue/earnings growth possibilities for JKTIL – the leader and pioneer in the TBR segment. With net debt levels appearing to have hit a peak and likely to ease downwards, we believe the major market concern is likely to be alleviated. Post FY16E, strong FCF generation makes us positive on the business as the next phase of growth begins. With a strong rise in peer valuations on demand recovery and favourable rubber prices, JK's valuation at <4x EV/EBITDA is alluring. Thus, we upgrade our valuation multiple and value JKTIL at 4.5x FY17E EV/EBITDA to arrive at a target price of ₹ 171. We maintain our BUY rating on the stock.

Rating matrix

Rating	:	Buy
Target	:	₹ 171
Target Period	:	12 months
Potential Upside	:	29%

What's Changed?

Target	Changed from ₹ 125 to ₹ 171
EPS FY16E	Unchanged
EPS FY17E	Unchanged
Rating	Unchanged

Quarterly Performance

(₹ Crore)	Q2FY15	Q2FY14	YoY	Q1FY15	QoQ
Revenues	1,872.4	1,806.6	3.6	1,864.2	0.4
EBITDA	232.6	210.2	10.7	192.3	20.9
EBITDA (%)	12.4	11.6	79 bps	10.3	211 bps
Reported PAT	76.4	65.8	16.2	55.4	37.9

Key Financials

₹ Crore	FY14	FY15E	FY16E	FY17E
Net Sales	7,599	7,700	8,689	10,027
EBITDA	871.3	1,006.4	1,198.5	1,365.6
Net Profit	263.0	380.6	491.4	557.6
FDEPS (₹)	11.6	16.8	21.7	24.6

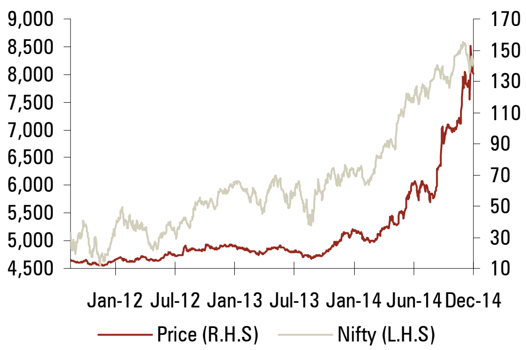
Valuation summary

	FY14	FY15E	FY16E	FY17E
P/E (Dil.) (x)	11.4	7.9	6.1	5.4
EV/EBITDA (x)	5.7	5.2	4.4	3.6
Tar. EV/EBITDA (x)	7.0	6.3	5.4	4.5
P/B (x)	2.5	1.8	1.4	1.1
RoNW (%)	24.0	25.6	25.3	22.5
RoCE (%)	19.2	20.1	21.6	22.5

Stock data

Particular	Amount
Market Capitalization (₹ Crore)	₹ 2710 Crore
Total Debt (FY14) (₹ Crore)	₹ 2506 Crore
Cash & Investments (FY14) (₹ Crore)	₹ 248.7 Crore
EV (₹ Crore)	₹ 4967.2 Crore
52 week H/L (₹)	167/28
Equity capital (₹ crore)	₹ 41.1 Crore
Face value (₹)	₹ 2

Price performance



Research Analyst

Nishant Vass
nishant.vass@icicisecurities.com

Financial summary

Profit and loss statement				₹ Crore
(Year-end March)	FY14	FY15E	FY16E	FY17E
Total operating Income	7,651.8	7,761.0	8,752.3	10,093.3
Growth (%)		1.4	12.8	15.3
Raw Material Expenses	4,891.9	4,888.6	5,510.6	6,407.0
Employee Expenses	755.0	715.3	771.2	863.5
Other Expenses	0.0	0.0	0.0	0.0
Total Operating Expenditure	6,780.5	6,754.6	7,553.9	8,727.8
EBITDA	871.3	1,006.4	1,198.5	1,365.6
Growth (%)		15.5	19.1	13.9
Depreciation	179.5	161.3	216.0	280.0
Interest	276.2	286.3	284.0	284.0
Other Income	18.3	14.1	14.2	14.4
Exceptional Items	59.52	7.29	0.0	0
PBT	374.4	565.7	712.7	816.0
Total Tax	118.8	190.3	228.0	265.2
PAT	263.0	380.6	491.4	557.6
Growth (%)	29.4	44.7	29.1	13.5
FDEPS (₹)	11.6	16.8	21.7	24.6

Source: Company, ICICIdirect.com Research

Cash flow statement				₹ Crore
(Year-end March)	FY14	FY15E	FY16E	FY17E
Profit after Tax	263.0	380.6	491.4	557.6
Add: Depreciation	179.5	161.3	216.0	280.0
(Inc)/dec in Current Assets	-252.2	-70.5	-259.6	-382.6
Inc/(dec) in CL and Provisions	237.1	14.9	173.5	184.8
CF from operating activities	427.4	486.3	621.4	639.8
(Inc)/dec in Investments	1.1	1.1	50.0	-30.0
(Inc)/dec in Fixed Assets	-256.3	-750.0	-700.0	-350.0
Others	25.0	2.2	28.6	33.6
CF from investing activities	-230.2	-746.8	-621.5	-346.5
Issue/(Buy back) of Equity	0.0	4.3	0.0	0.0
Inc/(dec) in loan funds	-28.7	200.0	-100.0	-250.0
Dividend paid & dividend tax	-24.0	-26.4	-26.4	-28.8
Others	-324.5	-253.1	-299.0	-274.0
CF from financing activities	-377.3	-75.2	-425.4	-552.8
Net Cash flow	96.2	-49.4	-141.5	24.6
Opening Cash	140.0	236.1	186.7	45.2
Closing Cash	236.1	186.7	45.2	69.8

Source: Company, ICICIdirect.com Research

Balance sheet				₹ Crore
(Year-end March)	FY14	FY15E	FY16E	FY17E
Liabilities				
Equity Capital	41.1	45.4	45.4	45.4
Reserve and Surplus	1,043.6	1,430.9	1,880.9	2,419.6
Total Shareholders funds	1,084.6	1,476.3	1,926.3	2,465.0
Total Debt	2,506.0	2,706.0	2,606.0	2,356.0
Net Deferred Tax Liability	252.4	284.4	306.4	338.4
Other non-current liabilities	434.6	456.1	472.7	484.2
Total Liabilities	4,277.6	4,922.8	5,311.3	5,643.6
Assets				
Gross Block	4,675.6	5,425.6	6,125.6	6,475.6
Less: Acc Depreciation	1,985.3	2,146.7	2,362.7	2,642.7
Net Block	2,690.3	3,279.0	3,763.0	3,833.0
Capital WIP	177.1	177.1	177.1	177.1
Total Fixed Assets	2,867.4	3,456.1	3,940.1	4,010.1
Investments	102.8	101.8	51.8	81.8
Inventory	936.8	1,012.7	1,190.2	1,346.0
Debtors	1,335.1	1,286.9	1,356.9	1,565.8
Loans and Advances	313.3	356.0	366.9	383.3
Other current assets	8.5	8.6	9.7	11.1
Cash	236.1	186.7	45.2	69.8
Total Current Assets	2,829.7	2,850.8	2,968.9	3,376.0
Creditors	1,053.2	1,086.5	1,190.2	1,373.5
Provisions	167.6	172.9	177.5	191.1
Other current liabilities	531.7	508.0	573.2	561.2
Total Current Liabilities	1,752.5	1,767.4	1,940.9	2,125.8
Net Current Assets	1,077.2	1,083.4	1,028.0	1,250.3
Others	333.0	383.3	343.3	383.3
Application of Funds	4,277.6	4,922.8	5,311.3	5,643.6

Source: Company, ICICIdirect.com Research

Key ratios				
(Year-end March)	FY14	FY15E	FY16E	FY17E
Per share data (₹)				
EPS	12.8	18.5	23.9	27.2
Cash EPS	21.6	26.4	34.5	40.8
BV	53.4	72.5	94.4	120.7
DPS	1.0	1.1	1.1	1.2
Cash Per Share	11.5	9.1	2.2	3.4
Operating Ratios (%)				
EBITDA Margin	11.4	13.0	13.7	13.5
PBT / Net sales	4.9	7.3	8.2	8.1
PAT Margin	3.4	4.9	5.6	5.5
Inventory days	45.0	48.0	50.0	49.0
Debtor days	64.1	61.0	57.0	57.0
Creditor days	50.6	51.5	50.0	50.0
Return Ratios (%)				
RoE	24.0	25.6	25.3	22.5
RoCE	19.2	20.1	21.6	22.5
RoIC	18.1	18.9	19.7	20.5
Valuation Ratios (x)				
P/E	10.3	7.1	5.5	4.9
EV / EBITDA	5.7	5.2	4.4	3.6
EV / Net Sales	0.7	0.7	0.6	0.5
Market Cap / Sales	0.4	0.4	0.3	0.3
Price to Book Value	2.5	1.8	1.4	1.1
Solvency Ratios				
Debt/Equity	2.3	1.8	1.3	1.0
Current Ratio	1.6	1.6	1.5	1.6
Quick Ratio	1.1	1.0	0.9	1.0

Source: Company, ICICIdirect.com Research

ICICIdirect.com Research Universe (Auto)

Sector / Company	CMP (₹)	TP(₹)	Rating	M Cap (₹ Cr)	EPS (₹) FY15E	FY16E	FY17E	P/E (x) FY15E	FY16E	FY17E	EV/EBITDA (x) FY15E	FY16E	FY17E	RoCE (%) FY15E	FY16E	FY17E	RoE (%) FY15E	FY16E	FY17E
Amara Raja (AMARAJ)	825	813	Hold	14,092	26.4	36.7	45.8	31.2	22.5	18.0	15.4	11.7	9.1	34.5	35.7	34.3	26.0	27.6	26.5
Apollo Tyre (APOTYR)	218	275	Buy	11,145	21.8	25.0	28.3	10.1	8.8	7.8	6.1	5.5	4.9	20.0	18.7	17.7	19.5	18.5	17.4
Ashok Leyland (ASHLEY)	51	48	Hold	14,422	0.8	1.9	2.9	66.2	26.7	17.5	22.9	13.0	10.1	4.0	9.8	13.0	4.2	9.7	13.5
Bajaj Auto (BAAUTO)	2,492	2,833	Buy	72,111	111.8	155.5	180.0	22.3	16.0	13.8	11.8	9.1	7.3	38.0	39.4	40.4	29.9	34.8	33.7
Balkrishna Ind. (BALIND)	600	734	Buy	5,801	44.1	56.5	66.8	13.6	10.6	9.0	8.7	6.6	5.4	14.4	17.6	19.9	18.7	14.4	17.6
Bosch (MICO)	19,051	18,500	Hold	59,821	373.1	494.1	600.0	42.9	32.4	26.7	28.9	21.5	17.1	16.2	18.3	18.7	16.5	19.5	20.9
Eicher Motors (EICMOT)`	15,298	15,000	Hold	41,320	253.0	443.9	682.2	60.5	34.5	22.4	31.5	17.8	11.2	24.7	33.8	37.9	26.2	32.8	34.7
Escorts (ESCORT)*	128	103	Sell	1,525	20.5	11.9	17.1	5.7	9.9	6.8	4.1	5.9	4.4	13.7	8.3	10.7	13.4	7.3	9.7
Exide Industries (EXIIND)	180	220	Buy	15,304	5.7	7.6	10.6	31.4	23.5	17.0	15.2	11.9	8.7	18.5	21.7	25.6	13.1	15.6	18.7
Hero Mototcorp (HERHON)	3,138	3,078	Hold	62,667	105.6	145.8	185.0	29.7	21.5	17.0	15.1	16.9	15.6	43.4	51.0	54.5	37.7	42.4	43.7
JK Tyre & Ind (JKIND)	132	171	Buy	2,694	16.8	21.7	24.6	7.8	6.1	5.3	5.2	4.4	3.6	20.1	21.6	22.5	25.6	25.3	22.5
M&M (MAHMAH)	1,262	1,457	Buy	74,504	59.3	74.5	84.8	21.3	16.9	14.9	14.0	8.6	7.5	18.9	20.1	20.6	19.8	19.3	18.9
Mahindra CIE (MAHAUT)*	208	260	Buy	6,768	6.2	10.3	13.9	33.3	20.2	14.9	11.9	9.3	7.4	8.0	12.8	16.1	7.8	11.9	15.9
Maruti Suzuki (MARUTI)	3,358	3,700	Buy	101,476	117.9	156.4	205.6	28.5	21.5	16.3	15.3	11.8	9.0	15.1	18.1	20.3	14.9	17.0	19.0
Motherson (MOTSUM)	447	512	Buy	39,456	11.2	20.5	26.9	40.0	21.8	16.6	12.4	9.3	7.0	26.3	32.1	37.4	28.8	39.3	38.0
Tata Motors (TELCO)	497	600	Buy	152,461	65.0	80.2	89.8	8.4	6.8	6.1	4.5	3.8	3.2	24.1	23.8	22.7	24.7	23.8	21.2
Wabco India (WABTVS)	4,600	4,750	Buy	8,740	75.1	128.2	169.7	61.3	35.9	27.1	30.4	19.8	14.7	16.1	22.0	22.9	20.1	26.2	28.2

*Source: ICICIdirect.com Research `Calendar Year ending *Mahindra CIE Auto financial numbers incorporate post merger numbers on annualised basis*

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Pankaj Pandey Head – Research pankaj.pandey@icicisecurities.com

ICICIdirect.com Research Desk,
ICICI Securities Limited,
1st Floor, Akruti Trade Centre,
Road No 7, MIDC,
Andheri (East)
Mumbai – 400 093
research@icicidirect.com

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