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Equity Research Analysis On Tyre Industry In India With Special Reference To MRF Tyres And Apollo Tyres

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Abstract

Auto ancillary sector fortunes are closely related to those of the auto sector. Market fluctuations in each of the segments (cars, two-wheelers, commercial vehicles) have an impact on the demand for ancillary cars. Demand is derived from both the original equipment manufacturer (OEM) and the replacement market. The Indian Auto Ancillary Industry is one of India 's crucial industries with greater prospects for growth. Some Auto Ancillary Industries examples are: Tyre Industries, Battery Industries, Gears, Engines etc. The Tyre sector is closely connected with the automobile industry. Tyre Industry is intensive on raw materials. The cost of raw materials is 63 % of industrial turnover and 72 % of manufacturing costs. Obviously, rubber, 80 % of which is natural rubber, and 20 % is synthetic rubber, is the primary raw material. Thus, the market for tyre and rubber is completely inseparable. Tyre Industry isn't very sensitive to price. Functionality of the tyres produced is nearly homogeneous, quality and price excepting a few foreign players, like Bridgestone. In India MRF Tyres holds the major market share & Apollo Tyres are also a key player in the sector. We will study their position in the market based on their financial position, country analysis and Fundamental analysis.

Keywords: Fundamental analysis, MRF tyres, APOLLO tyres, Equity research

Introduction:

The Indian rubber industry produces a wide variety of rubber products serving sectors such as the three wings of defence, civil, aviation, aeronautics, railways, agriculture , transport as well as textiles, engineering industries, pharmaceuticals, mines, steel plants, ports, family planning services, hospitals, sports, i.e. literally for every area under the sun.

Under the Ministry of Trade and Industry, rubber act 1947, Rubber board is GOI's statutory body for the development of the country's rubber industry.

- India is that the third largest producer of rubber within the world.
- It's the fourth largest consumer of natural rubber.
- It's the fifth largest consumer of natural rubber and artificial rubber together within the world.
- India is that the world's largest manufacturer of reclaim rubber.

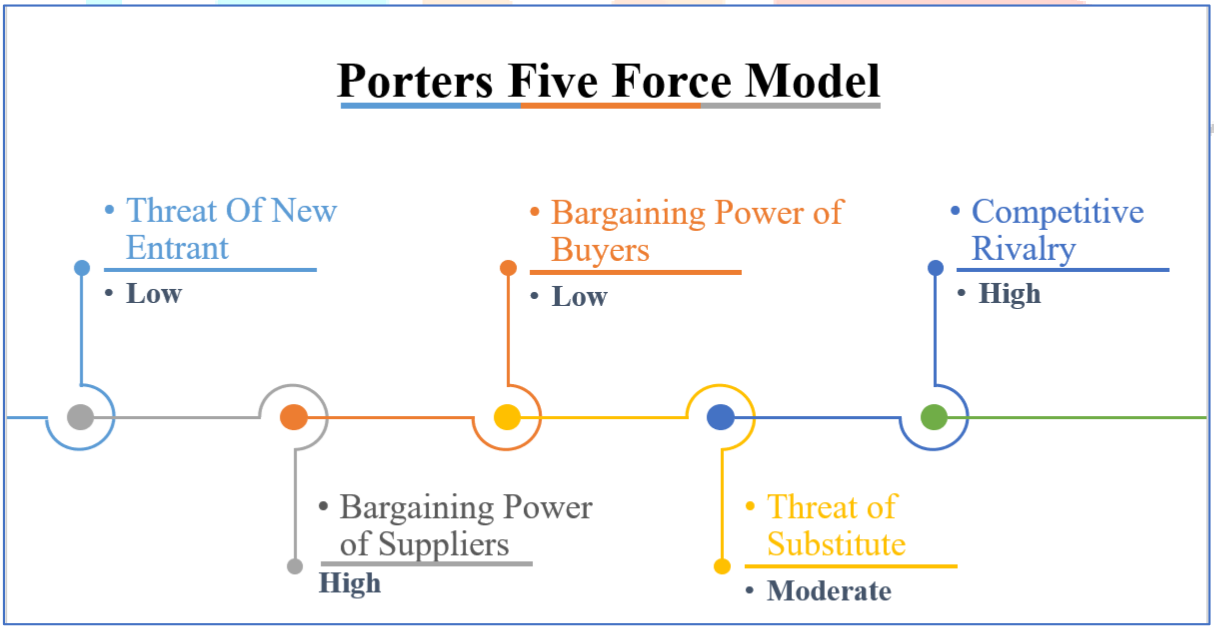
- India and China are the sole two countries within the world which have the capacity to consume the whole indigenous production of natural rubber.

Majorly three types of rubber are in use: Natural rubber, Synthetic rubber, and Reclaimed rubber:

Natural rubber is used mostly in automobiles. The automotive industry consumes nearly 65 % of natural rubber. The primary component in heavy duty tyres is natural rubber. In addition, NR is used to manufacture bicycle tyres, tubes, hoses, conveyor belts, foam mattresses, footwear, balloons, toys and several other daily-use products.

Synthetic rubber can mostly be used as a single polymer or in mixtures with natural rubbers. Between 65 and 70 % of all rubber goes into tyre production.

The Indian Tyre Industry came into being in 1926 when Dunlop Rubber Limited set up West Bengal's first tyre firm, followed in 1946 by MRF. Tyre Industry is primarily regulated by the organized industry, while the unorganized sector is made up of tyres. Indian tyres are made so that they are compatible with village roads of kutcha as well as with new roads of pakka. They are also intended and required to operate in dry, cold, and humid climatic conditions.
Tyre Industry is heavy on raw materials. The cost of raw materials is 63 % of industrial turnover and 72 % of manufacturing costs. Obviously, rubber, 80 % of which is natural rubber, and 20 % is synthetic rubber, is the main raw material.



The objective of the study:

1. To do Equity analysis of Tyre sector which focuses on studying and analyzing financials of MRF Tyres and APOLLO Tyres and looking at all the qualitative and quantitative aspects for taking various decisions.
2. To analyze the Tyre sector in India and justifying whether it is a good sector to invest or not, considering MRF Tyres and APOLLO Tyres.
3. To do the fundamental analysis of Tyre Sector specifically analyzing MRF Tyres and APOLLO Tyres LTD.

Literature Review:

1) Mr. Suresh A.S. (May, 2013) In This Paper Titled "A Study On Fundamental And Technical Analysis" Researcher found that the companies' fundamental factors are vital for investment decision and economic as well as industry factor that investment decision is also persuaded.
2) Dir. Sreemoyee Guha Roy (2013) Had Examined The Title "Researcher" Equity Research: Fundamental And Technical Analysis "examined that most of the time depends on fundamental stock analysis for investor judgement. Fundamental analysis focuses on the identification and analysis of the factors that persuade security pricing while analysing market behaviour exclusively concerned with technical analysis.
3) Mrs. Vimala. S, Mrs. Saranya P.B. And Ms. Saranya. R. (April 2014) Had Made "A Study On Analysis Of Equity Share Price Behaviour Of the chosen Industries" Researcher Has Studies That The stock exchange Is Extremely Volatile In Nature. Despite Its Volatility. The Investor Has Probability To Make Comfortable Profits With The Help Of Moving Average, Trend Line And The Relative Strength Index Trend Lines.
4) Waworuntu, Stephanus & Suryanto, Hendra. (2012). Indonesia's Complementary Nature of Fundamental and Technical Analysis Evidence.

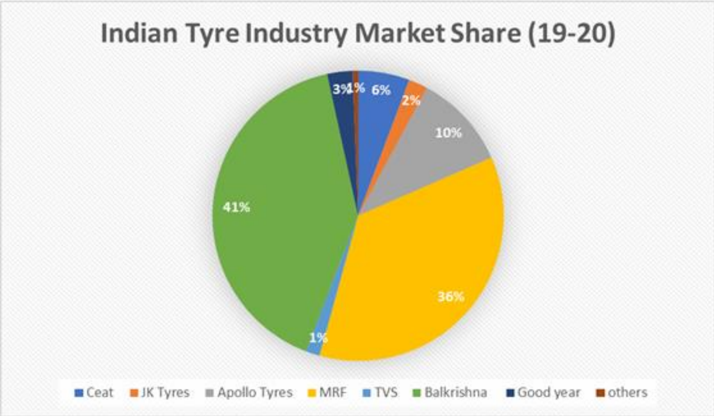
   The results of this study could have a considerable impact on our understanding of valuation techniques, particularly in emerging markets, in the context of the investment decision process. In particular, for market participants, especially those in the investment management space, the results are expected to be of significance.

   The results show that the two valuation methods explain that price movements are fairly good in isolation, but consistent with some previous literature. The two techniques are complementary. A higher explanatory power is possessed by the hybrid model and therefore both the basic analysis and therefore the technical analysis outperform.

Methodology:

- The project focuses on the study of market research in the Tyre field. The study must, therefore, be carried out on the basis of information and news available on the sector, i.e. secondary data by different modes. This research was completed by a fundamental analysis of the respective companies, MRF Tyres and APOLLO Tyres.
- Secondary data was collected from the websites of the company. However, the key source of information is the annual report released by the businesses and also the quarterly results of the same year reflecting their success in the present business scenario.
- In the first instance, data was evaluated on the basis of industry. The Tyre business, that is the Tyre sector was focused on, and its performance and relationship with the Indian economy was monitored, and then specific stocks were chosen to be invested in, depending on the fundamentals of the company's stock.
- Research on the Tyre sector and two companies in the sector is explained in the later part of the report.
- The collection of primary data for the preparation of this project was not possible due to time and money constraints. Therefore, supplementary data processing has been used.
- During this report, daily stock market prices were tracked, and the company's annual reports analysed and taken into account for the assessment of company performance.
- The company's websites have been a major source for collecting the company's annual reports.
- While preparing the project, the Internet was a major source of information, as most of the data collected from different websites were gathered. The knowledge gained from the preliminary study thus forms the basis for detailed descriptive research in the future

Market Share of Tyre Industry:



Quantitative Analysis:

MRF Tyres Financial Analysis

MRF TYRES					
Financials (in crs)	**2020**	**2019**	**2018**	**2017**	**2016**
Revenues	16239.36	16062.46	15364.97	14922.8	22491.02
Gross profit	6622	6353	6256	7428	11217
EBITDA	2374	2305	2281	2643	4422
EBIT (Operating income)	1392	1498	1575	2023	3685
Interest expense	292.32	267.31	253.12	251.47	352.56
Net Income	12004.35	10653.3	9604.2	8544.42	7161.21
Total assets	19442.34	18441.26	16478.48	15083	13253.81
Total equity	12214.84	10837.47	9738.31	8640.76	7224.34
Total Debt	7227.5	7603.79	6740.17	6442.09	6029.35
Total cash and equivalents	1076.57	-91.11	-53.48	125.4	-152.03
Current assets (excl cash)	6969.63	8361.85	7681.44	7067.1	6197.85
Current liabilities (excl debt)	5252.24	5464.43	4589.89	4502.04	4028.82
Cash flow from operations	2272.61	1252.85	2412.98	1954.91	3043.47
Cash flow from investment	-163.69	-1386.15	-2013.88	- 1391.88	-3407.81
Cash flow from financing	-1032.35	42.19	-452.58	-437.63	212.31

Sales growth yoy	2020	2019	2018	2017	2016
Revenue growth rate	1%	5%	3%	-34%	N/A

Profitability margins	2020	2019	2018	2017	2016
Gross Profits as % of Revenues	41%	40%	41%	50%	50%
EBITDA as % of Revenues	15%	14%	15%	18%	20%
EBIT as % of Revenues	9%	9%	10%	14%	16%

Leverage ratios	2020	2019	2018	2017	2016
Net Debt / Equity	0.592	0.702	0.692	0.746	0.835
Net Debt / EBITDA	3.0444	3.2988	2.9549	2.4374	1.3635

Coverage ratio	2020	2019	2018	2017	2016
EBITDA / Interest	8.1212	8.6229	9.0115	10.5102	12.5425
EBIT / Interest	4.7619	5.6040	6.2223	8.0447	10.4521

Liquidity ratio	2020	2019	2018	2017	2016
Current Assets to Current Liabilities	1.33	1.53	1.67	1.57	1.54
Cash to Total Assets	0.0554	-0.0049	-0.0032	0.0083	-0.0115
Is CFO > CFI?	yes	yes	yes	yes	yes

Interpretations:

- The revenues have clearly increased over the past ten years, it seems that there is a 34 percent drop in FY 2017, but it is because of section 2(41) of the Companies Act , 2013, all companies are required to have a uniform financial year ending every year on 31 March. This requirement is to be fulfilled within two years of the start of the 2013 Companies Act. The Board of Directors has therefore extended the financial year beginning on 1 October 2014 to an eighteen-month period ending on 31 March 2016. Consequently, this report, which is annexed to the financial statements, runs from 1 October 2014 to 31 March 2016 for a period of 18 months. Consequently, the figures for the period under review are not comparable with those for the preceding financial year ending on 30 September 2014.
- The company's revenue is gradually increasing, and in the last five years, we have observed this trend for all the years.
- Usually, the greater the gross profit margin, the better. By raising sales prices or decreasing sales costs, the gross profit margin can be improved. We can see that there is a relatively stable gross profit margin.
- A higher number compared to its peers is a good EBITDA margin. The relatively high figure also represents a good EBIT or EBITA margin. MRF tyres are efficient compared to Apollo tyres.
- The reason for the decrease in the debt equity ratio is the repayment of 403 crores of long-term debt by the company during the year. In addition to the above, the Company also reversed the remaining 115.53 crores in the Debenture Redemption Reserve during the year along with the addition of this year's profit to the General Reserve. This resulted in a debt equity ratio reduction from 0.702 percent to 0.592 percent.
- There is no substantial change (i.e. 25% or more) in the main financial ratios, i.e. Coverage ratio of interest.

- The net tax provision (current tax and deferred tax) for the year is '4 crores (previous year 512 crores) because, as introduced by the Taxation Laws (Amendment) Ordinance, 2019, the Company chose to exercise the option allowed under section 115BAA of the Income Tax Act, 1961. The Company has therefore recognised the income tax provision for the year ended 31 March 2020 and has re-measured the deferred tax liabilities / assets at the rates prescribed in that section. The net profit for the year ended 31 March 2020 after making provision for Income Tax is '1395 crores as against' 1097 crores in the previous year ended 31 March 2019.

- MRF has made substantial capex investments of ~Rs. In the past three years, 5,000 crores. This had an impact on the company’s profitability (ROCE) from the top of 24.5 percent in FY2017 to 16.3 percent in FY2019, along with rising raw material prices and other overhead costs. The adjusted ROCE levels also decreased from 34.3 percent over to 21.7 percent over the same period, it continues to remain healthy.

- With healthy fund flows from operations and cash and liquid balances of Rs. 3,956.6 crore as of March 31, 2019, the liquidity position of MRF is superior. The average utilisation of working capital by MRF was low at ~15.7 percent of the scrutinised limits over the past year. Given the stable accruals and healthy cash reserves, the repayment obligations for Rs. 403 crores in FY2020, Rs. 341 crores in FY2021 and Rs. 266 crore FY2022 are likely to be serviced comfortably.
- The operational profile of MRF is strongly supported by a well-balanced mix of products and a diversified segmental mix (more than two-thirds of replacement revenue). Higher revenue share from the relatively stable substitute segment continues to support revenue from MRF

Apollo Tyres Financial Analysis:

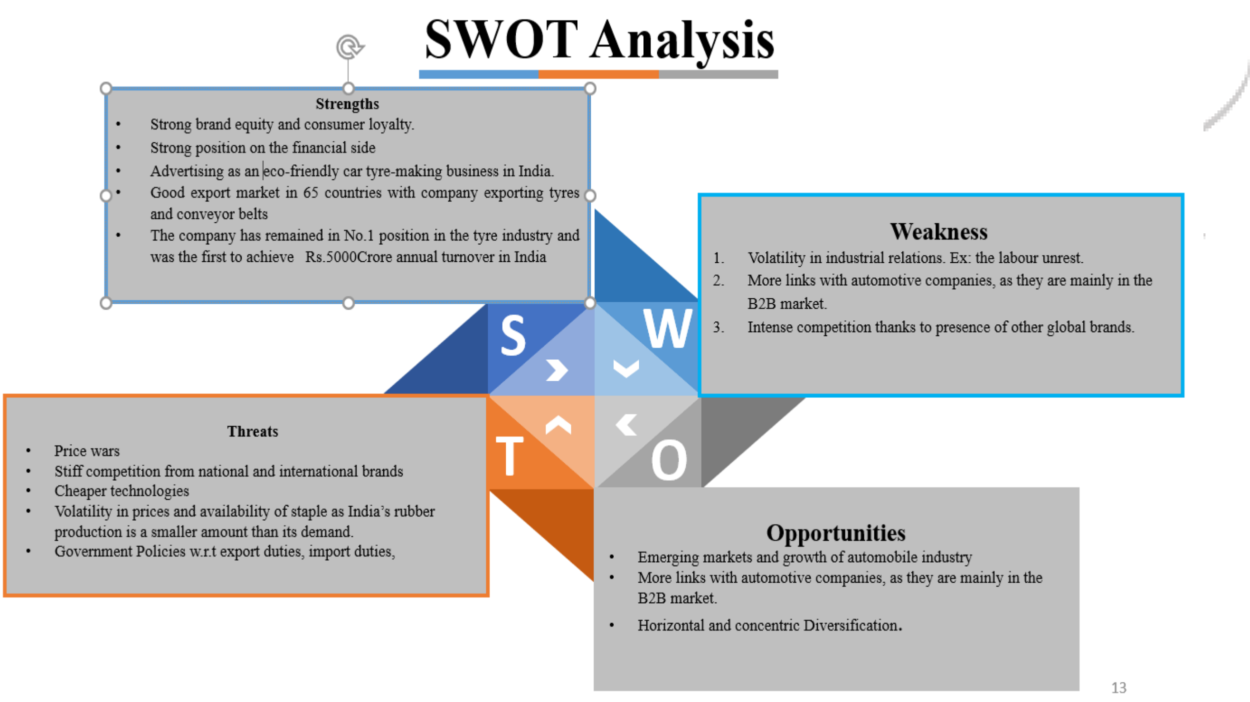
APOLLO TYRES					
Financials (in mn)	**2020**	**2019**	**2018**	**2017**	**2016**
Revenues	1,63,269.95	175488.43	150977.44	99,236.89	97,601.49
Gross profit	72514.04	74223.67	67022.41	47076.59	47679.9
EBITDA	19155.13	19586.31	16535.94	13272.83	15660.14
EBIT (Operating income)	7773.95	11459.6	10610.4	10390.84	13008.77
Interest expense	2,808.33	1,810.70	1,629.20	887.84	901.41
Net Income	4763.96	6798.4	7238.8	8027.58	10021.49
Total assets	2,32,499.87	2,02,033.97	2,01,532.45	98,803.71	75,195.53
Total equity	99,300.14	1,00,398.19	97,766.72	53,311.89	46,578.35
Total Debt	1,33,199.73	1,01,635.78	103765.73	45491.82	28617.18
Total cash and equivalents	7,386.41	5,554.66	5,931.17	1,340.88	2,867.68
Current assets (excl cash)	54,814.78	58,885.87	63,058.42	30,461.98	21,345.59
Current liabilities (excl debt)	57,134.31	43,744.20	49,619.96	29,009.31	20,788.18
Cash flow from operations	25,173.60	10,711.16	17,196.73	3,298.49	17,849.01
Cash flow from investment	-27,958.66	-9,959.25	-38,628.14	-13,953.81	-10,775.97
Cash flow from financing	4,724.68	-622.09	23,208.81	9,060.48	-6,409.82
Sales growth yoy	**2020**	**2019**	**2018**	**2017**	**2016**
Revenue growth rate	-7%	16%	52%	2%	N/A
Profitability margins	**2020**	**2019**	**2018**	**2017**	**2016**
Gross Profits as % of Revenues	44%	42%	44%	47%	49%
EBITDA as % of Revenues	12%	11%	11%	13%	16%
EBIT as % of Revenues	5%	7%	7%	10%	13%
Leverage ratios	**2020**	**2019**	**2018**	**2017**	**2016**
Net Debt / Equity	1.3414	1.0123	1.0614	0.8533	0.6144
Net Debt / EBITDA	6.9537	5.1891	6.2752	3.4274	1.8274
Coverage ratio	**2020**	**2019**	**2018**	**2017**	**2016**
EBITDA / Interest	6.8208	10.8170	10.1497	14.9496	17.3729
EBIT / Interest	1.6318	1.6856	1.4658	1.2944	1.2981
Liquidity ratio	**2020**	**2019**	**2018**	**2017**	**2016**
Current Assets to Current Liabilities	0.959	1.346	1.271	1.050	1.027
Cash to Total Assets	0.0318	0.0275	0.0294	0.0136	0.0381
Is CFO > CFI?	YES	YES	YES	YES	YES

Interpretations:

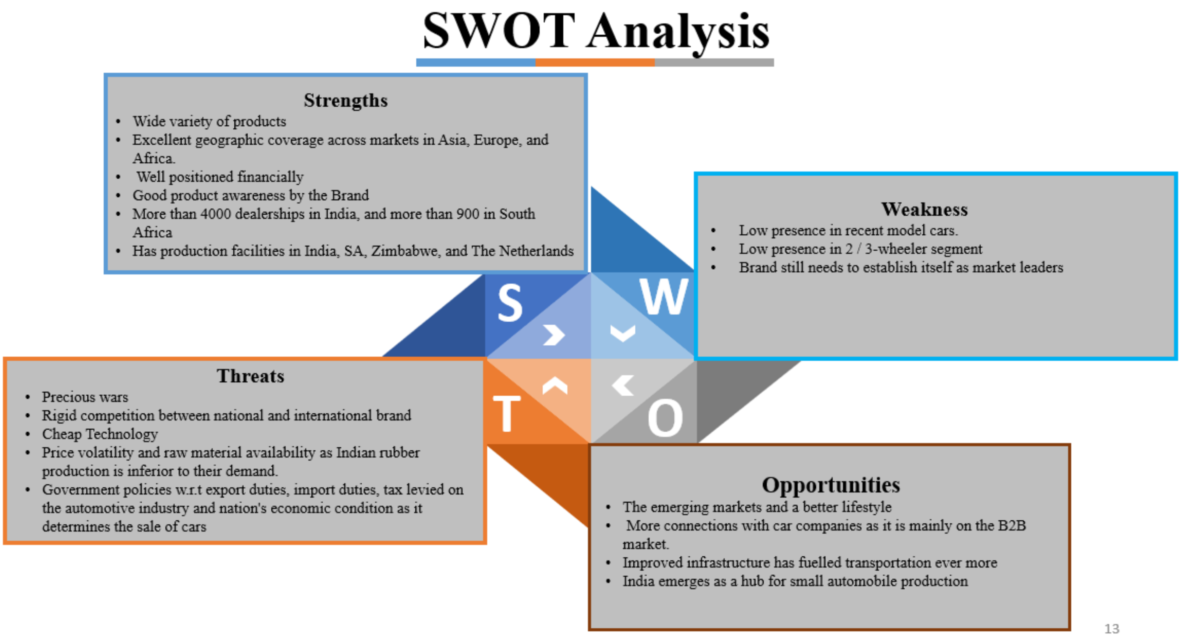
- EBITDA including other earnings (consolidated operating profit) is 19,623 million. There is' 25,173.60 million cash generated by operating activities. Net EBITDA debt (ratio) is 3.00. Net debt (ratio) to equity is 0.59. Earnings per share were 8.33 per share. The return on equity is 4.80%.
- Please note that in Key Ratios viz., there is no significant change of 25 percent or more. Turnover of debtors, inventory turnover, margin of operating profit and margin of net profit as compared to the previous year.
- The reduction in the interest coverage ratio is due to the increase in the cost of finance, the reduction in the current ratio is due to working capital optimization, the increase in the debt equity ratio due to the increase in borrowings.
- The decrease in Net Worth 's return is mainly due to the decrease in net profit from Rs 5921.09 million to Rs 5,086.24 million.

<u>Qualitative Analysis:</u>

MRF TYRES



APOLLO TYRES



- Natural rubber is an agricultural commodity and is subject to price volatility and concerns about production. The movement in crude prices affects most other raw materials. The price of some of the raw materials may be impacted by any volatility in crude oil prices. The external environment controls both natural rubber and crude prices and is, therefore, beyond the reasonable control of management. To some extent, India's tyre industry has been helped by the falling cost of materials for some of its key raw materials. In FY20, these raw material prices decreased by ~5 percent over the previous year, supported by a decrease in the prices of carbon black, synthetic rubber, nylon fabric and chemicals. However, during the same period, domestic natural rubber prices saw an increase of ~7 percent.
- In Europe, the company's (Apollo tyre) winter sales are subject to seasonal requirements, which may have a negative impact in the event of a mild winter season.
- Slower than anticipated increase in the level of radialisation in Indian activities may be affected by the truck tyre section. The Excess Strength can lead to competitive pressures and a decrease in profit.
  At the same time, an unforeseen faster rise in the level. Radialisation may result in faster cross-ply redundancy. Capabilities and the need to create new investments.
- Lower profitability due to some of the factors mentioned above affects theThe capacity to invest in growth in the future. Growth may also be hampered by increased competition from global players like Michelin, Bridgestone and others in India. Because of COVID-19, continued lockdown can lead to a serious impact on the organisation, including a significant drop in demand, decrease in profitability, liquidity issues, and others.
- Due to the entry of global majors into the Indian tyre industry, retaining qualified staff may become increasingly difficult in India.
- The production of tyres depends considerably on the availability of skilled labour. Any labour unrest, labour shortage, labour diversion to other industries can affect the production of tyres.
- For the fiscal year 2020, the overall growth outlook for the auto industry is pegged at moderate. The tyre industry has stood out over the past few years for the substantial investments made to support the growth of the automotive business. Natural rubber dominates the raw material mix of the Indian tyre industry compared to developed countries and, in this context, the gap between domestic rubber production and demand will continue to be an area of concern. The severe flooding in Kerala that disrupted the supply of natural rubber aggravated this. To secure India's ever-growing appetite for energy, a judicious mix of pragmatism and diplomacy is key. The geopolitical situation in the Middle East and the US sanctions against Iran are just some of the factors that could serve as headwinds to keep fuel prices volatile

Conclusion:

- The industry is mainly covered by four vehicle categories, namely Commercial Vehicle (CV) including Truck and Buses (T&B), Passenger Vehicles (PV), Two-Wheeler and others including Tractors and Off the Road (OTR), for Original Equipment Manufacturers (OEM), Export and Replacement markets.
- Of these three distinct markets, about 56 percent of the industry accounts for the replacement market, with institutional / OEM and exports making up 44 percent of the balance, respectively. While replacement sales form a major chunk in the Commercial and Farm categories, in the Passenger category, both Institutional/ OEM and Replacement sales play an almost equal role.
- Compliance with BS-VI standards will require higher investment in technology by automakers to upgrade stock vehicles and produce new vehicles. Furthermore, due to compliance with BS VI standards, volatile fuel prices and rising insurance costs, the anticipated increase in scooter prices is only expected to add to the overall cost of ownership.
- Given the uncertainties caused by the pandemic, the way forward for the automotive sector and the tyre industry is not clear. Given the impact on disposable incomes, consumer behaviour and credit availability, the road to recovery will not be smooth. The rural and semi urban areas would be the bright spot. Tractors and 2 wheelers are more likely than other segments to do better.
- The business environment and economy were severely affected by the COVID 19 pandemic. To reduce the impact of the pandemic, the Government announced a national lockdown on 24 March 2020 and consequently closed the Plants, Offices and Godowns of the Company. Most of the company's operations have resumed following the lifting of the lockdown. The Company has a strong Net Worth as of the date of approval of the financial statements and has serviced all its debt obligations in a timely manner. It does not foresee any incremental risk about asset recoverability and financial service obligation

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