

INDIA, May 10, 2012

## Investor Conference Call

### Fourth Quarter of Financial Year 2011-12

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**Amit Kasat** On behalf of the Standard Chartered Equity team, I welcome all participants and the management of Apollo Tyres to Q4 FY12 post results conference call. From Apollo we have Gaurav Kumar, Group Head, Corporate Strategy and Finance, Rakesh Dewan, Head, Accounts and Ritu Kumar, Head, Financial Planning and Control. Now I invite Gaurav to give us a quick summary.

**Gaurav Kumar** Good afternoon. Allow me to take you through the financials, post which Team Apollo will take on your questions.

On a consolidated basis, sales for the quarter were at Rs 32.3 billion, a growth rate of 18% over the same period last year. Half of this growth came through volumes and the balance through price and mix improvements. The EBITDA margin for the quarter was Rs 3.9 billion at 12% compared to Rs 3.5 billion, but a slightly higher margin figure at 12.8% for the same period last year. The total tonnage sold for the quarter was 136,000 metric tonnes (MT). Overall raw material cost was sequentially down by 5%, however it was up 8% on a year-to-year basis.

The annual sales were at Rs 121.5 billion, a high growth of 37% over the same period last year. Around 22% of this came through volume growth and the balance 15% through price and mix. The EBITDA for the full year was Rs 12 billion at 9.9% as compared to Rs 10.2 billion at 11.5% for the same period last year. The full year tonnage was 511,000 MT. The net debt figure improved from previous quarters as a result of lower Capex showing benefits and improvements in working capital. The net debt was at Rs 27 billion, while the net debt equity ratio was below 1.

In terms of outlook, we are seeing good momentum from various geographies and we expect top-line growth in excess of 15% for FY13. Further as Chennai unit has been completed and its capacity is nearing potential, the total Capex for next year would be significantly lower. As per current plans, next year the total Capex for Apollo should be in the region of Rs 3 billion. We are on the drawing board to chalk out further growth programmes. On the raw material front, while we expect a marginal increase in the next quarter, the broader raw material outlook is fairly stable and expected to be flat on a year-to-year basis, which would provide further positive momentum on the margins. One factor of concern in the current economic environment remains the exchange rate, which at a high level will impact raw material imports and put pressure on the margins.

Moving on to Zonal Operations. For the India operations Q4 sales was Rs 22.6 billion, a growth rate of 28% over the same period last year. Of this, 14% growth came through volumes and 14% through price and mix. EBITDA for the quarter was Rs 2.3 billion at 10.3%, compared to a 9.8% margin last year. Annual sales were Rs 81.6 billion, a growth rate of nearly 50% compared to last year. Around 28% growth came through volumes and the balance through price and mix. EBITDA margin for the full year, in wake of raw material pressure, declined from 10.4% to 8.4%. With inventory reductions and lower Capex, the net debt came down sequentially from Rs 23.8 billion to Rs 20.3 billion, again bringing down the net debt to equity ratio.

In terms of outlook, we're seeing good momentum from the truck segment and expect industry growth rate to be close to double-digits. Passenger car segment should also see a growth rate in high single digits in the next year. Given this momentum, we would be targeting around 20% growth in our topline. The India operation is looking to expand into new geographies. Apollo has already set up an office in the Middle East and is looking at new locations in South East Asia to set up sales and marketing offices.

South Africa operations had a tough quarter. There were a couple of factory shutdowns, both due to national and company level issues. The sales for Q4 FY12 were at Rs 3.4 billion, 4% down vis-à-vis the same period last year, essentially coming from a significant de-growth in volumes, of around 18%; but made up with improvement in price and mix. EBITDA for the quarter was Rs 17 million at negative 0.5%, compared to a profitable figure last year. Annual sales were at Rs 13 billion, a growth of 10% over last year; with 1% coming through volumes, 7% through price and mix and the balance from currency impact. The EBITDA for the full year was Rs 0.3 billion at 2%, compared to a 5% margin last year.

The South African markets including car and truck sales is growing in low to mid single digits and with these improvements we expect the sales to improve next year and we are working towards reaching a breakeven situation in South Africa.

Moving on to Europe operations, the sales for Q4 FY12 were at Rs 6.8 billion, a growth of 9% over the same period last year; with 4% coming through volumes and the balance through price, mix and currency. EBITDA for the quarter was Rs 1.1 billion at 16.8%, compared to a 10% margin last year. Annual sales in Europe were at Rs 28.5 billion, a growth of 28% in the European market, which is generally growing slowly. This reaffirms our faith in this market, and the company has done well riding on its Vredestein and Apollo brands. Just to break down the 28% growth, 8% came through volumes, 8% through price and mix and a significant portion of 12% resulted from the exchange effect. EBITDA margin for the full year, for Europe operations, was at 15.8% compared to 13.7% last year. We expect the market to be flat in the coming year. Growth in the European topline, hence, would be lower than what we would see in our India

and South Africa operations in FY13. The company hopes to sell larger volumes in the Apollo brand. In FY12 Apollo brand tyres were introduced in 3 new European countries – Austria, Switzerland and Denmark.

We have managed to reduce inventories both at India operations and at a consolidated level, further releasing some of the pressure in terms of leveraging. Given the stable raw material scenario, there hasn't been much in terms of price increases. We took a small price increase in May 2012 in the truck segment. In South Africa, given the profitability pressures, the company had taken a 3% price increase in February 2012 and another 3% in April 2012. With regards to our newly constructed plant in Chennai, the average operating capacity was 200 MT per day, though the facility has already reached a capacity in excess of 350 MT per day; it is expected to reach its planned peak capacity by December 2012.

That's all in terms of introduction. We would be happy to take your questions.

**Jaibir Sethi, CLSA** Just a couple of things. First, as I recall in 4<sup>th</sup> quarter of last year, there were some one-off gains in the European business. So excluding those, what would have been sort of year-on-year margin trend and has there been any similar one-off item this year as well? And second, there has been a lot of talk about CCI inquiry into tyre industry so any details you can share on that?

**Gaurav Kumar** Jaibir, we do not have the trend after elimination of one-off gains and will need to check and get back to you. On your second question, which is the CCI inquiry -- this is something which has been ongoing for a number of years and relates to 2008. There are no indications that can lead us to believe that the case has turned against us. Given the tyre industry margins in the last few years and the fact that raw material costs have gone up significantly without adequate price increases, we don't see it as a concern.

**Jaibir Sethi** But in other industries, even in case of sector profitability being under significant stress, what they are basically looking for is just evidence of any sort of collusion in pricing?

**Gaurav Kumar** I understand and I can only say that we believe there is no evidence to that effect and there has been nothing in terms of a judgment which hints towards an unfavourable outcome for us.

**Vaishali Jajoo, Aegon Religare** This is regarding the Capex figure of Rs 3 billion, given for FY13. Can you give me the breakup between India operations and overseas?

**Gaurav Kumar** India operations would account for about Rs 1.1 to 1.2 billion and the balance would be overseas, which is mapped for modernisation, normal Capex and some line balancing in Europe.

- Vaishali Jajoo** Because we have a lower Capex this year do you think that the debt level will be further reduced from the current level?
- Gaurav Kumar** We expect so and that's what we had maintained earlier also.
- Vaishali Jajoo** Any debt to equity target you have for the current year?
- Gaurav Kumar** Apollo's targets are more growth related. The company is preparing its balance sheet for embarking on its next growth plan; a new plant in Europe.
- Vaishali Jajoo** It may not go beyond Rs 3 billion – is that right?
- Gaurav Kumar** For Eastern Europe operations or the new plant that we're looking at?
- Vaishali Jajoo** Yes.
- Gaurav Kumar** There would hardly be any Capex this year as we are still in the stage of finalising the country, and the exact site. The preparation and approvals take almost a year.
- Vaishali Jajoo** So it is not included in the FY13 numbers?
- Gaurav Kumar** That's correct.
- Vaishali Jajoo** You talked about inventory reduction. Could you give some idea how it has reduced over last quarter?
- Gaurav Kumar** In terms of number of days it would have come down by about 5 days.
- Vaishali Jajoo** From Q3 to Q4?
- Gaurav Kumar** Yes.
- Vaishali Jajoo** The rubber prices in the last one month have been consistently below Rs 200 level. But you have indicated marginal increase in raw material cost. Is it because of the currency impact?
- Gaurav Kumar** There would be some degree of currency impact. Other than that, prices for synthetic rubber and carbon black are expected to be higher than previous quarter.
- Vaishali Jajoo** Could you give some indication of the replacement demand?
- Gaurav Kumar** As of now the replacement demand appears to be healthy. We would be expecting a high single digit growth, from what we are seeing in the market now.
- Vaishali Jajoo** OEs are indicating a double-digit growth in truck segment?

**Gaurav Kumar** That's right. OEs are indicating a double-digit growth in the truck segment, and for the passenger car segment, just under a double-digit.

**Raghu Nandan,  
Avendus Securities** What is the quantum of price increase taken in the truck segment in May 2012?

**Gaurav Kumar** That's just over 1%.

**Basudeb Banerjee,  
Quant Capital** You said that there was a reduction in net debt this quarter despite your interest outgo on a consolidated basis moving up by almost Rs 140 million. So can you throw some light on that?

**Gaurav Kumar** Due to a change in accounting norms, there have been some reclassifications. Interest income which was earlier netted off against interest expense, now goes and sits in other income. Similarly, certain upfront financing costs that used to earlier sit in other expenses, now get clubbed with interest expense. These are the cause of the significant increase. There has been some increase in interest expense, since some of the interest for Chennai related borrowings, which were earlier capitalised, is now flowing into the P&L.

**Basudeb Banerjee** So can we assume that a part of the increase in other income is due to this change in accounting norms?

**Gaurav Kumar** That's correct.

**Basudeb Banerjee** Second question is that out of India Capex of Rs 1.2 billion next year, how much is for Chennai?

**Gaurav Kumar** Chennai would be negligible.

**Basudeb Banerjee** So basically, more or less, it is fully maintenance Capex?

**Gaurav Kumar** Yes.

**Basudeb Banerjee** Can you give the average cost for natural rubber, carbon black, tyre cord and synthetic rubber for this quarter?

**Gaurav Kumar** For this quarter the average natural rubber cost was about Rs 210 per kg.

**Basudeb Banerjee** Including freight and duty?

**Gaurav Kumar** Everything. This is consumption cost for the company. Tyre cord fabric was at about Rs 255, carbon black at Rs 75 and synthetic rubber was at Rs 175.

- Basudeb Banerjee** Can one assume that with rupee weakening you might shift to sourcing more rubber from the domestic markets?
- Gaurav Kumar** That's correct.
- Mittul Mehta,  
Lucky Securities** In terms of overall imports, how much of our total of raw material is imported?
- Gaurav Kumar** For India operations nearly 50% of our raw material is imported. This, however, changes quarterly, on the basis of the quantum of natural rubber.
- Mittul Mehta** Is there some hedging practice that we follow?
- Gaurav Kumar** There are operational hedging decisions which are taken on a monthly or a quarterly basis by the treasury desk. But none of our raw materials are currently contracted for more than a quarter and hence a weak rupee would still impact us. You can at best protect yourself for a quarter, if you have hedged it in advance. The buying price would still go up the next quarter.
- Mittul Mehta** For your Europe operations, over next 2-3 years, are you envisaging a bigger Capex, barring the new plant?
- Gaurav Kumar** Barring the new plant that we are talking about, the Europe Capex would in fact comedown. The normal Capex every year is less than Rs 1 billion. There is a small line balancing which will add to the growth Capex this year. Over the next few years there will be no additional Capex.
- Mittul Mehta** Regarding your South Africa operation you did mention that the current year you could see higher growth than last year. Can you help us understand that market and how things are moving there?
- Gaurav Kumar** In South Africa, as I mentioned, both OE and replacement segments are seeing a growth of low or at best mid single digits. A large part of the market, which about a year-and-half or 2 years ago, got captured by the Chinese imports, when the industry had a prolonged shutdown, now has become fairly entrenched. So the domestic players fight for the balance 50% share. The good part is that in the last couple of years the market has grown. And one thing working in favour of all the operations is a much stable raw material scenario. Last year all our operations were struggling with raw material prices. The European markets act in a more stable manner largely because it is dominated by global majors who pass on price increases to consumers far more quickly. In rising raw material scenario, since Chinese imports do not take as many price increases, there has been a further constraint on the domestic industry. As I mentioned 2 price increases have been taken in February 2012 and April 2012 of 3% each which is gives us confidence that profitability should improve next year.

**Jasdeep Walia,  
Kotak**

Your other expenses have gone up sharply quarter-on-quarter. Why?

**Gaurav Kumar**

It is mainly due to changes in accounting norms, which have resulted in reclassification of some of the expenses, as mentioned earlier. In addition, towards the end of the year, we do some reclassification of R&D expenses from staff cost to other expenses.

**Jasdeep Walia**

Has there been any mix change quarter-on-quarter because of which your margins are lower than the margins reported by other players?

**Gaurav Kumar**

It would be very difficult to compare margins with the other Indian players.

**Jasdeep Walia**

What is the status of the anti-dumping case? Anti-dumping duties against Chinese players was taken away and you had appealed against that.

**Gaurav Kumar**

They said duties were never withdrawn. Though there was an order passed, but it is yet to be ratified by relevant authorities. The dumping duty still continues.

**TVK Mohan,  
Principal Mutual  
Fund**

Could you tell us about the sales mix between replacement and OEM? And given the strong replacement demand that you have been suggesting, would this change have a positive rub-off on the margins next year?

**Gaurav Kumar**

For Apollo Tyres, in the financial year 2011-12, replacement was 73%, which was lower in the 4<sup>th</sup> quarter. Yes, with a stronger replacement demand coming in, particularly in India operations, which was weak last year, we would expect the shift to be beneficial. Also, as truck radialisation gets more and more entrenched, where the OE component is very high, the mix would again shift in favour of the tyre industry, as replacement sales pick up. On a product wise basis, about 47% of our revenues came from truck segment and about 33% from car tyres. The balance 20% was from light truck, farm and other segments. For India operations about 34% of the revenues were from OE and the balance from replacement segment, both within and outside the core Indian market. In terms of product category, 65% revenues came from the truck segment, about 16% from car and the balance from light truck farm and other categories.

**TVK Mohan**

In Q4 replacement was lower, how much would that have been? Any numbers?

**Gaurav Kumar**

It was a little lower than 70% for the consolidated operations.

**TVK Mohan**

You had earlier indicated that brand Apollo tyre exports to Europe in FY12 were about 400,000 tyres. What would the numbers be in FY13?

**Gaurav Kumar**

The number would probably jump to around 3/4<sup>th</sup> of a million.

- Saurabh Das, Tata Mutual Fund** You just mentioned India split is 65% commercial vehicle and 16% cars. Is this for the full year?
- Gaurav Kumar** Yes.
- Saurabh Das** And how has each of the individual segments grown on a Y-o-Y basis?
- Gaurav Kumar** In terms of truck, the market was flat even though production grew by 3%. And in the passenger car category, the market grew by 4%.
- Saurabh Das** And are our growth numbers similar?
- Gaurav Kumar** We gained market share in the truck segment. Our growth in that segment has been close to 20%. Chennai was the big driver of our growth this year. In the passenger car segment, on the other hand, we lost market share by about a couple of percentage points.
- Saurabh Das** Can you also give us the market share number?
- Gaurav Kumar** In the truck side we are at 28%. In the passenger cars side we are at 20%.
- Saurabh Das** Do you see the car space getting a little more competitive with the international companies expanding their capacities? Do you see these manufacturers gaining market share structurally or are they more aggressive in terms of pricing?
- Gaurav Kumar** The car tyre market is quite competitive and even imports play a significant role here; unlike the truck segment where imports have a very low share. The share of imports ranges between 15 to 20%. We haven't seen aggressive pricing actions by any of the global majors. They are far more rational in terms of their overall profitability and also conscious as to where their brand should be positioned.
- Saurabh Das** Are Vredestein branded tyres getting exported from India or are they only brand Apollo?
- Gaurav Kumar** It's mostly brand Apollo tyres. We make a very small quantity of Vredestein tyres. India does not have that kind of a surplus capacity, so today almost all of Vredestein sales are manufactured in the Netherlands and all of the Apollo branded sales come out of the Indian facilities.
- Saurabh Das** Currently how would you rank the profitability of passenger cars and commercial vehicles?
- Gaurav Kumar** Passenger cars would be the highest, followed by commercial vehicle tyres.

- Vishal Saraf,**  
**SBI Mutual Fund** You were mentioning that imports in the truck segment are much lower. I just wanted to understand what will be the quantum now. You also mentioned gain in market share. Does it take into account imports as well or this is within the domestic players?
- Gaurav Kumar** The 28% market share is only within domestic players; so if we account for imports, the market share would be slightly lower. Imports today would be comprising somewhere between 5 to 6% of the market share, so to that extent the 28% would come down to may be 27%.
- Vishal Saraf** And what was this 5-6% be a year back?
- Gaurav Kumar** One year back it was 6% upwards. So the number hasn't changed dramatically.
- Vishal Saraf** Just on account of the rupee depreciation how has the cost of imported tyres changed?
- Gaurav Kumar** We would not have data on the prices on a monthly basis. But that could have been one of the reasons why the market share has fallen by 1%.
- Vishal Saraf** But you would not have a sense whether the gap between yours and Chinese tyres would have remained flat or would have reduced?
- Gaurav Kumar** I will have to check if it has changed dramatically in the last quarter.
- Vishal Saraf** And over the last one year or 6 months?
- Gaurav Kumar** Over the last one year or so it has not changed. Any change would have been in the last quarter or so.
- Vishal Saraf** On the export side, how have the margins been and any change there on account of the Rupee depreciation?
- Gaurav Kumar** Exports are far more profitable today. Last year in general has been good because of the weak rupee. But overall, the replacement segment remains by far the most profitable; OE segment would probably be the least profitable. However, there is a certain amount of presence in OEs that we must maintain for brand visibility and product acceptability. Our decisions to sell in the OE segment are not driven by profitability concerns alone.
- Vishal Saraf** Any broad sense of realisations in the export market over last 1 year?
- Gaurav Kumar** We took a 10% price increase in our exports from India in September 2012, which was essentially to counter raw material pressure. Before that we had

taken 2 price increases in April 2012 and June 2012. So in the last one year we have taken 20% price increase.

**Vishal Saraf** So there would be this 20% price increase plus the benefit of rupee depreciation which would have happened over last 1 year?

**Gaurav Kumar** Yes.

**Vishal Saraf** On the export side, can we push in as much volume into the market as we want, in case we have surplus capacity? Or is there some constraint to pushing volumes?

**Gaurav Kumar** There is a constraint to pushing volumes. You can increase it definitely far more than where we are today, but it has to be built up over time. We can't get into a market and suddenly say we want to double volumes. This is also because of the fact that we want to position brand Apollo or any of the brands that we are exporting, at a certain level.

For example, we can look at brand Apollo in Europe. It has been 3 years since we have completed the acquisition. We feel very happy with the kind of volumes we have achieved, but one could look at it and say that we have not even achieved half a million figure in 3 years. We took a year to understand the requirements. Then we introduced brand Apollo gradually and that too in selected countries; all this to be able to position the brand well ahead of Chinese tyres.

So in the short-term one can achieve higher volumes but profitability would suffer; and then to move from one price position to another becomes extremely challenging.

**Vishal Saraf** If the currency does not appreciate, is there scope to further increase overall share of exports in our revenues and hence improve margins?

**Gaurav Kumar** Yes. If we don't see the currency appreciating, we will probably see an increase in exports.

**Vishal Saraf** And what is the exports revenue currently as a percentage of sales?

**Gaurav Kumar** Around 10% of our India revenues.

**Vishal Saraf** And in India this has been 10% for a long time, so we have not seen this change even over the last 1 year?

**Gaurav Kumar** It has changed by about 1.5% to 2% in the last few years. Not a dramatic change, but with our topline growing in excess of 20%, exports too have grown at a similar level.

- Vishal Saraf** Can this 10% reach 15% next year?
- Gaurav Kumar** With revenue growing at a fairly good level of 20%, increasing the share from 10 to 15% would be very difficult, especially if we want to position and establish our brand in a premium space.
- Vishal Saraf** Just in volume terms, 20-25% growth would be possible?
- Gaurav Kumar** Around 15 to 20% volume growth is possible.
- Chirag Shah, Emkay Global** On European margins, you indicated exchange rate fluctuations have brought in some 8% revenue increase. This is largely due to translation?
- Gaurav Kumar** That is the translation gain.
- Chirag Shah** But this would not impact your profitability and your margin would remain the same?
- Gaurav Kumar** The margins are the same; the gain is only on the topline. Otherwise, in Euro terms the revenue growth is 16% for the full year.
- Chirag Shah** Do you have any data on extent of radialisation as of March end?
- Gaurav Kumar** The current level of radialisation is at about 25%. The average radialisation level for the full year would be upward of 20%.
- Chirag Shah** And you indicated raw material cost being stable for you for the entire FY13. Is this the overall basket or are you referring to natural rubber?
- Gaurav Kumar** This is the overall basket and to reemphasise, this is the outlook that is available from the market today.
- Chirag Shah** But if we look at your costing in the first 2 or 3 quarters of FY12, raw material was at significantly higher levels; so that benefit actually should come into your P&L?
- Gaurav Kumar** But what has happened is that while prices of natural rubber have come down, the other part of the basket has gone up.
- Chirag Shah** And even currency would be a part of that?
- Gaurav Kumar** That's correct.

- Sabyasachi Paul, Jet Age Securities** Your staff cost that has gone down sequentially. Is there any exceptional cost over there?
- Gaurav Kumar** A large part of this is a non-cash actuarial gain in our Europe operations, which is approximately Rs 200 million. The rest is on account of various reclassifications.
- Sabyasachi Paul** In terms of taking a foreign currency hit on account of your imports, previously you would be classifying your mark to market hit on your imports along with your raw material cost. Is that right?
- Gaurav Kumar** That is right.
- Sabyasachi Paul** Now are you reclassifying that as other expenses?
- Gaurav Kumar** If it is a gain it will go to other income.
- Sabyasachi Paul** If it is a hit it will go to other expenses?
- Gaurav Kumar** That's right.
- Saurabh Ginodia, Smith Securities** Can you share the present capacity in tonnage across the 3 geographies?
- Gaurav Kumar** The overseas capacities are more in terms of number of tyres. In India, for the last quarter, we were at about 1000 metric tonnes per day.
- Bharat Gyani, Sharekhan** Can you throw some number on the revenue earned on our Apollo branded tyres which we export to Vredestein currently?
- Gaurav Kumar** That today would be just 2 to 3% of the Europe revenues.
- Bharat Gyani** Any target for next year?
- Gaurav Kumar** As I mentioned before, we are expecting the volumes to nearly double and we will continue to work on the price mix. So the revenue would more than double but would still be a very small component of the Europe revenue.
- Amit Kasat** On behalf of Standard Chartered, I thank the management of Apollo Tyres and the participants who were on the call.
- Gaurav Kumar** Thank you.

(ends)