# Maruti Suzuki

## Expectedly Disappointing!

31 January 2011

### Result highlights

Revenues were in-line with our estimates, up 26% YoY and 4% QoQ. EBIDTA margins stood at 7.9% (down 575bps YoY; 94bps QoQ). Sequentially, operating leverage coupled with cost cutting initiatives helped mitigate the input cost pressures and higher discounts during the quarter (cyclical phenomenon).

Staff costs grew 75bps QoQ as it included a restructured annual employee cost of ~INR510m which was entirely expensed during the quarter. Adjusting for the same, margins and PAT were in-line with our estimates at 8.3% and INR6bn, respectively. Reported PAT at INR5.65bn was down 18% YoY (6% QoQ).

### Our view – Strong volumes to offset margin woes…

With high localisation levels and economies of scale, the cost of spares, servicing, etc. are extremely economical and consequently the ownership cost of a Maruti Suzuki vehicle remains relatively lower than the competition (an enviable advantage in a cost-conscious market like India). The unmatched service and distribution network is an added advantage.

Hence, we expect the company to whither the storm as far as volumes and market-share are concerned. However, post the revision in royalty computation coupled with increased competition and higher input costs, we see limited scope for margin expansion from these levels.

### Valuation and outlook

Maruti Suzuki has underperformed the benchmark by over 20% over the last 12 months on account of market share concerns coupled with the higher royalty. While some market share loss in the longer term is inevitable, we believe that the current valuations capture most of the negatives.

At the CMP of INR1,234, the stock is attractively valued - trading at a P/E of 13.8x and Cash P/E of 9.7x, discounting our FY12e earnings. We upgrade our recommendation from HOLD to BUY in light of the attractive valuations. Our target price of INR1,450 (11x FY12e Cash EPS + INR50 for the subsidiaries) provides an 18% upside from the current levels.

### Quarterly financials

| (INRm) | 3QFY11 | 3QFY10 | YoY (%) | 2QFY11 | QoQ (%) |
|---|---|---|---|---|---|
| Net sales | 93,261 | 73,727 | 26 | 89,774 | 4 |
| - Raw material | 74,455 | 55,901 | 33 | 70,756 | 5 |
| (% of net sales) | 80 | 76 | 401 | 79 | 102 |
| - Staff expenditure | 2,325 | 1,325 | 76 | 1,568 | 48 |
| (% of net sales) | 2 | 2 | 70 | 2 | 75 |
| - Other expenditure | 9,147 | 6,464 | 42 | 9,545 | (4) |
| (% of net sales) | 10 | 9 | 104 | 11 | (82) |
| Total expenditure | 85,927 | 63,689 | 35 | 81,870 | 5 |
| EBITDA | 7,335 | 10,037 | (27) | 7,904 | (7) |
| EBITDA margin (%) | 7.9 | 13.6 | (575) | 8.8 | (94) |
| PAT | 5,652 | 6,875 | (18) | 5,982 | (6) |
| EPS | 19.6 | 23.8 | (18) | 20.7 | (6) |
| Total volumes | 330,687 | 258,026 | 28 | 313,654 | 5 |
| EBITDA/Vehicle | 22,180 | 38,900 | (43) | 25,200 | (12) |

Source: Company, Antique

| | | |
|---|---|---|
| **Current Reco** | : | **BUY** |
| **Previous Reco** | : | **HOLD** |
| **CMP** | : | **INR1,234** |
| **Target Price** | : | **INR1,450** |
| **Potential Return** | : | **18%** |

### Market data

| | | |
|---|---|---|
| Sector | : | Automobiles |
| Market Cap (INRbn) | : | 355 |
| Market Cap (USDbn) | : | 8 |
| O/S Shares | : | 289 |
| Free Float (m) | : | 100 |
| 52-wk HI/LO (INR) | : | 1600/1127 |
| Avg Daily Vol ('000) | : | 278 |
| Bloomberg | : | MSIL IN |
| Reuters | : | MRTI.BO |

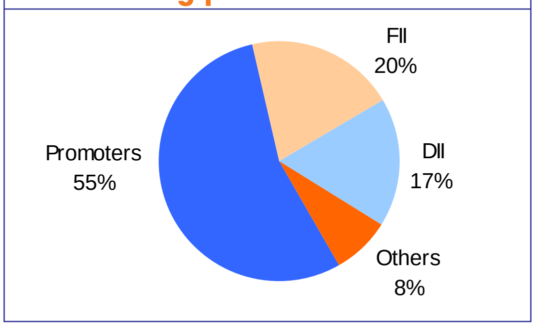
Source: Bloomberg

### Returns (%)

| | 1m | 3m | 6m | 12m |
|---|---|---|---|---|
| Absolute | 8 | 29 | 21 | 11 |
| Relative | 10 | 15 | 6 | (12) |

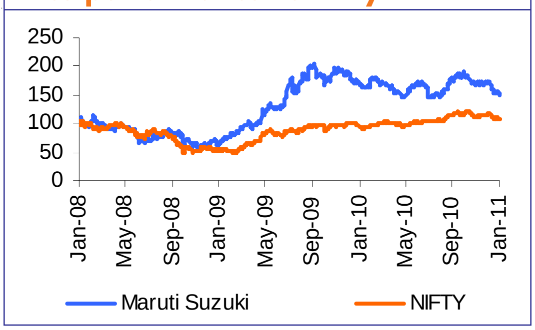
Source: Bloomberg

### Shareholding pattern




Source: BSE

### Price performance *vs* Nifty




Source: Bloomberg

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## 3QFY11 results review

- Net sales were broadly in-line with estimates, up 26% YoY (4% QoQ), driven by a 28% YoY growth in volumes (up 5% QoQ) and 1.3% YoY decline in realisations (down 1.5% QoQ). The lower realisations were a function of a weaker product mix coupled with lower export realisations (weaker Euro).
- EBIDTA margins (excluding other operating income) were at 7.9% (down 575bps YoY; 94bps QoQ). On a sequential basis, operating leverage from the higher volumes coupled with cost cutting initiatives helped mitigate some of the input cost pressures (RM to sales up 102bps QoQ; other expenses to sales down 82bps QoQ). However, higher discounts during the quarter (cyclical phenomenon) coupled with adverse currency movements and higher staff costs (up 75bps QoQ) led to a disappointing operational performance.
- The sequential increase in staff costs included a restructured annual employee cost to the tune of INR510m, wherein the entire amount was expensed during the quarter (as against being amortized over all four quarters). Adjusting for the same, margins were in-line at 8.3% (down 50bps QoQ).
- Reported PAT stood at INR5.65bn (down 18% YoY; 6% QoQ), however adjusting for the one-time staff expenditure, PAT stood at INR6bn, which was in-line with our estimates.

## Other highlights during the quarter

- Royalty during the quarter stood at 5.2% (up 150bps YoY; down 30bps QoQ). The sequential decline in royalty costs were driven by lower contribution from exports (which attract a higher royalty) coupled with the domestic product mix tilting towards lower royalty models during the quarter.
- The company has hedged its Euro exposure for the next six months, but its Yen exposure only till the end of February. Going ahead, the management wants to keep its Yen exposure open as they expect it to depreciate against the Dollar.
- Lower exports during the quarter (down 13% QoQ) resulted in savings on ocean freight costs, which has helped the company mitigate some of the input cost pressures and adverse currency movement.
- At the end of the quarter, the company had a sales network of 889 outlets covering 631 cities. Service network stood at 2,879 workshops, covering 1,373 cities.

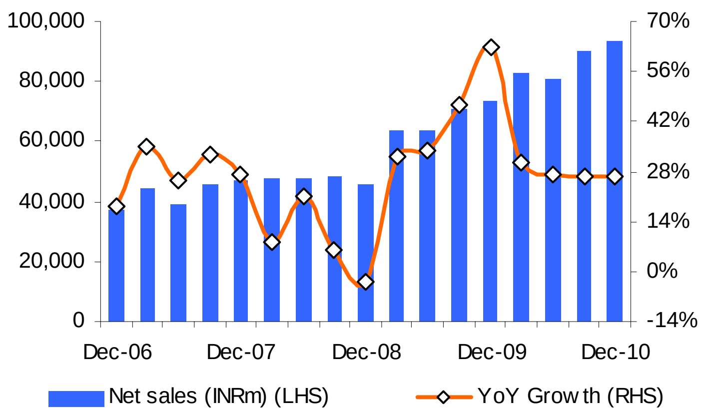
### Volumes

| In nos. | 3QFY11 | 3QFY10 | YoY (%) | 2QFY11 | QoQ (%) |
|---|---|---|---|---|---|
| A1 - M800 | 6,869 | 8,738 | (21) | 5,207 | 32 |
| A2 - Alto / Swift / A Star | 216,057 | 159,678 | 35 | 198,953 | 9 |
| A3 - SX4 / Dzire | 32,098 | 25,388 | 26 | 31,362 | 2 |
| MPV - Omni / Eeco | 43,612 | 24,426 | 79 | 41,596 | 5 |
| MUV's - Gypsy / Grand Vitara | 891 | 680 | 31 | 818 | 9 |
| **Total Domestic Volumes** | **299,527** | **218,910** | **37** | **277,936** | **8** |
| Exports | 31,160 | 39,116 | (20) | 35,718 | (13) |
| **Total Volumes** | **330,687** | **258,026** | **28** | **313,654** | **5** |

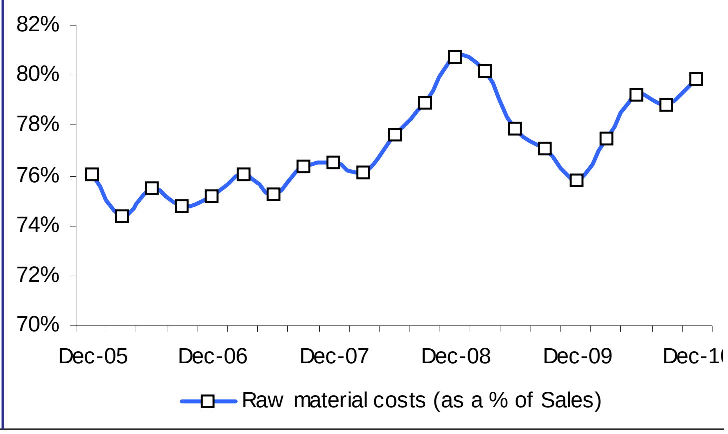
Source: Company, Antique

## Quarterly trends

### Revenue growth remains strong… Record-high dispatches off-set weaker realisations

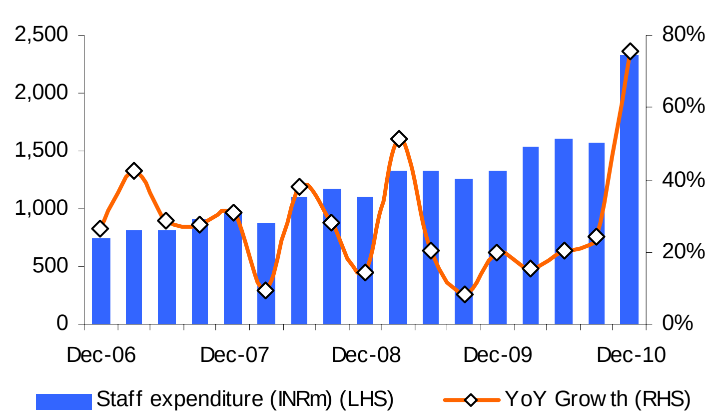



### Raw material costs up 401bps YoY; 102 bps QoQ

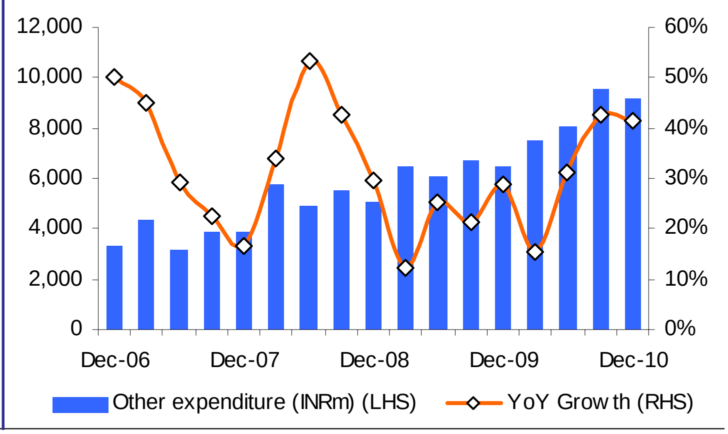



Source: Company, Antique

### Staff expenditure up 76% YoY (48% QoQ) on account of one-off costs to the tune of INR510m

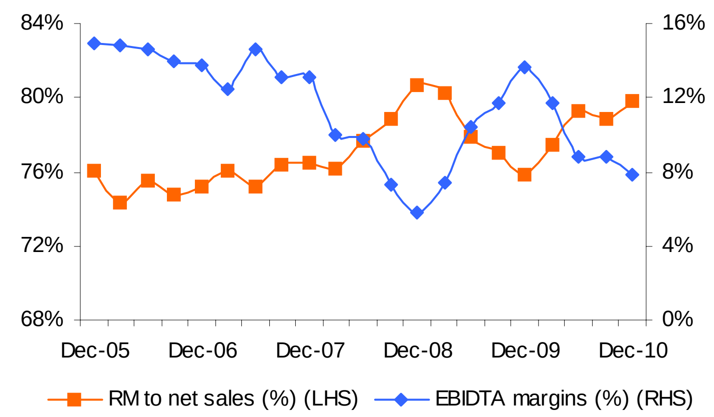



### Sequential decline in other expenditure driven by cost cutting measures coupled with lower exports and royalty costs

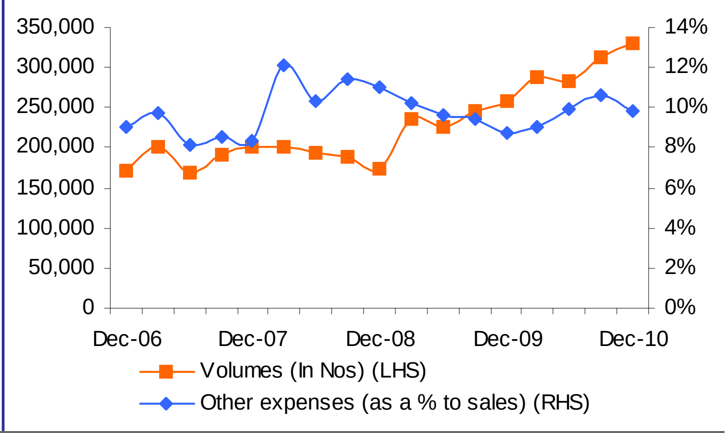



Source: Company, Antique

### EBIDTA margins impacted on all fronts (input costs, seasonal discounts, royalty, adverse currency)… Adjusting for one-off staff costs margins stood at 8.3%

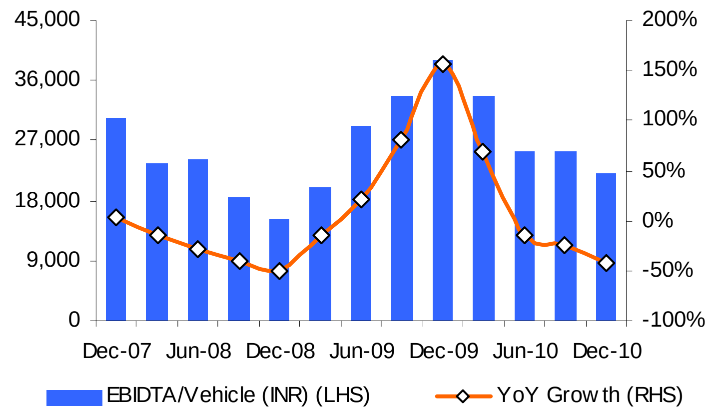



### Cost reduction helped mitigate some of input cost pressures

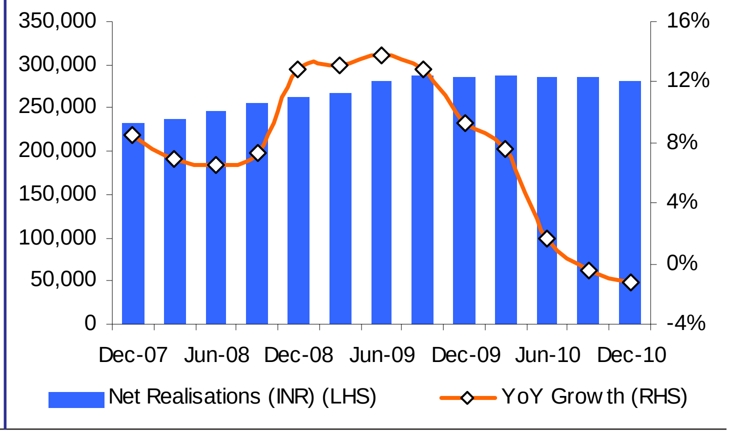



Source: Company, Antique

## EBITDA/vehicle lower by 43% YoY (12% QoQ)

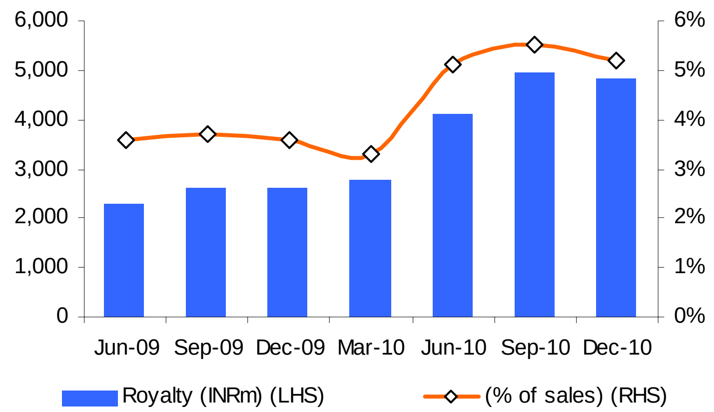



## Realisations down 1.3% YoY (1.5% QoQ) due to weaker product mix coupled with lower export realisations

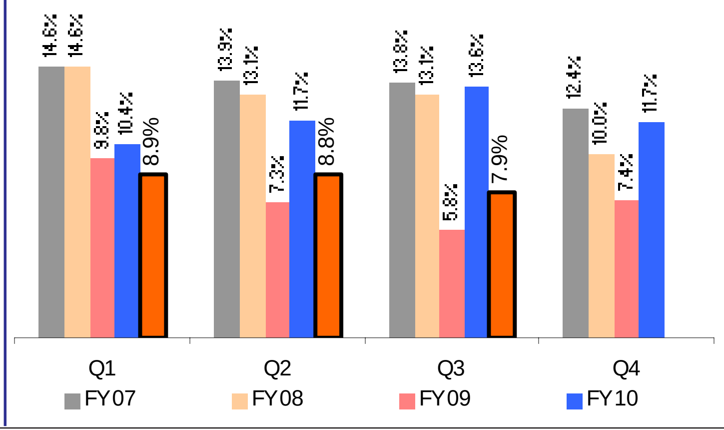



Source: Company, Antique

## Royalty rate lower by 30bps QoQ due to lower exports coupled with domestic product mix tilting towards lower royalty models

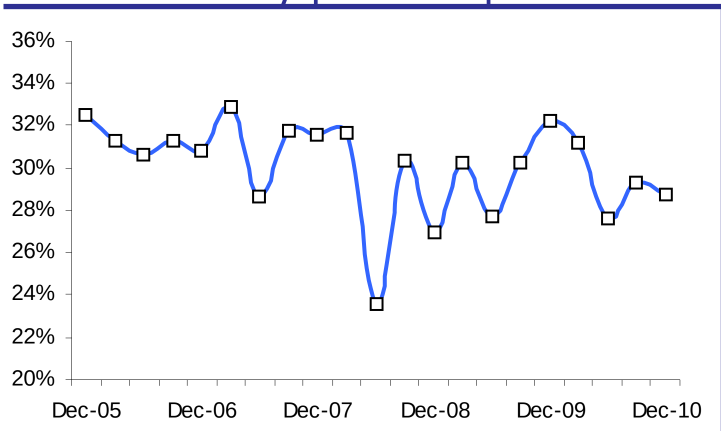



## EBIDTA margins trend - Close to historic lows

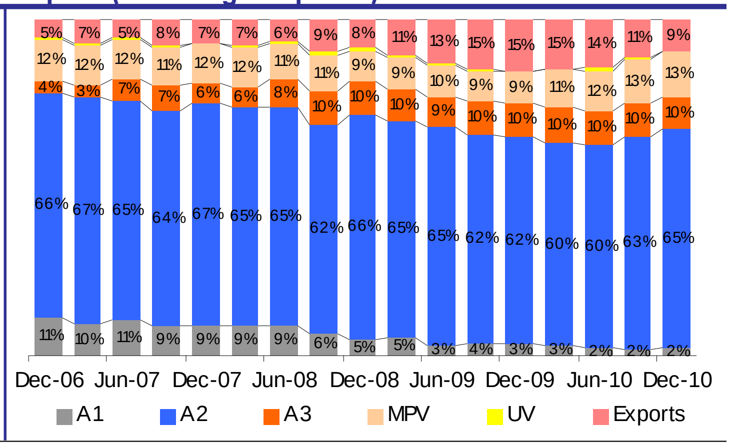



Source: Company, Antique

## Lower tax rates driven by uptick in R&D expenses

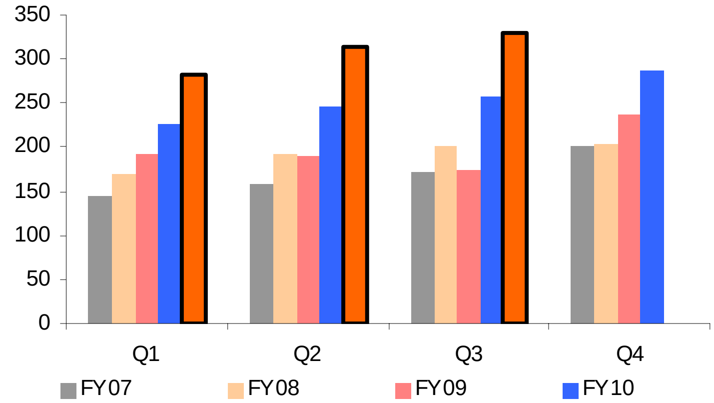



## Strong domestic volumes leads to lower contribution from exports (9% during the quarter)

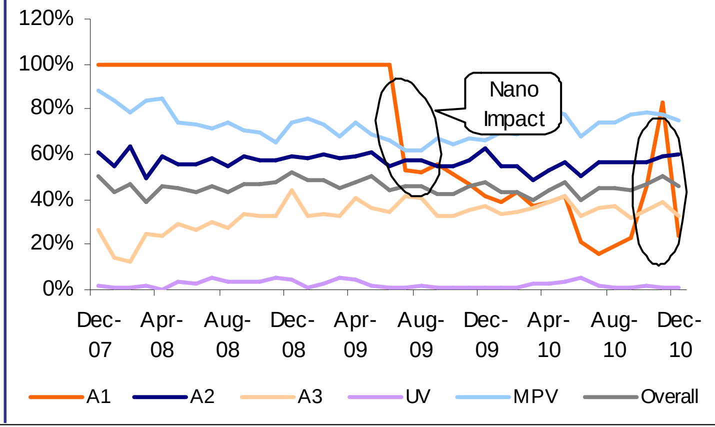



Source: Company, Antique

## Volumes growth remains intact… six day plant shut-down affects December dispatches

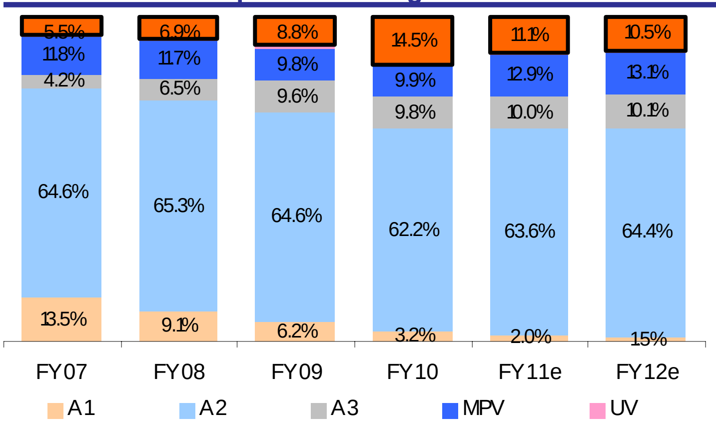



## Maruti Suzuki market share trends - Barring A1 segment, market share remains firm across all segments

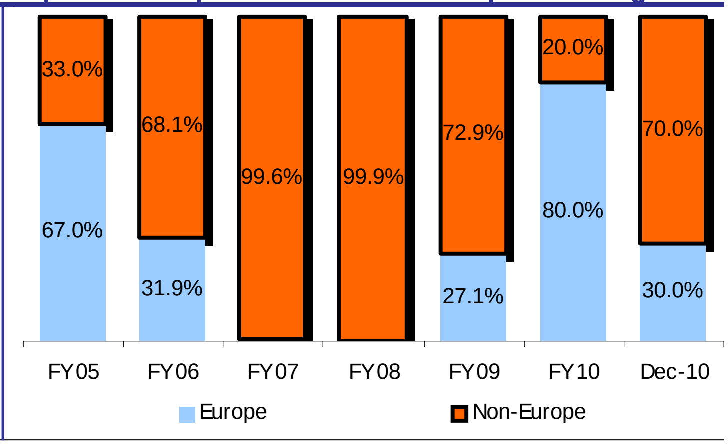



Source: Company, Antique

## Contribution from exports is reducing

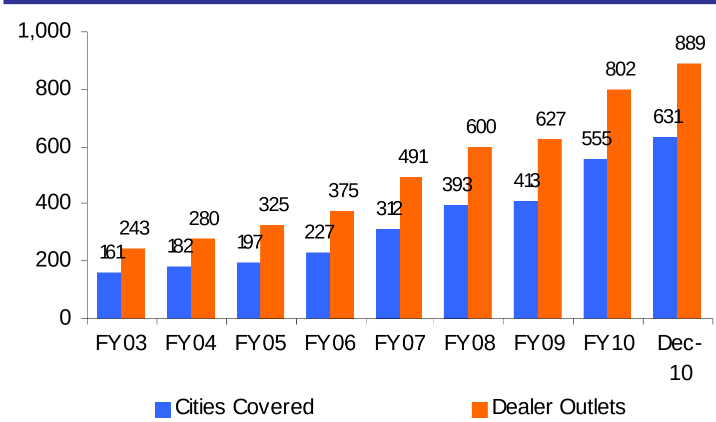



## Exports Break-up - Contribution from Europe decreasing

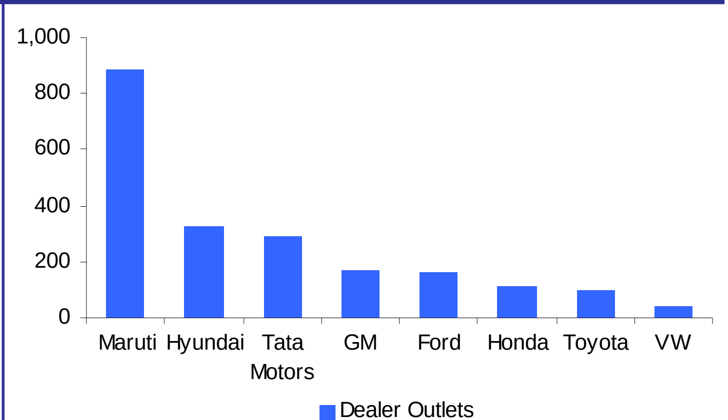



Source: Company, Antique

## Dealer network only gets stronger…




## … and remains miles ahead of competition




Source: Company, Antique

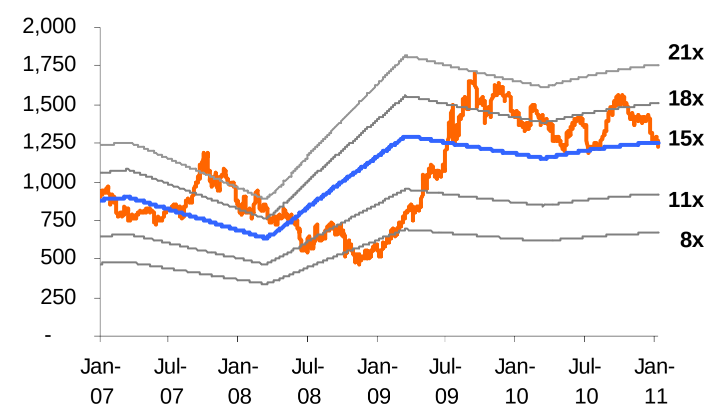
## Our view – Strong volumes to offset margin woes…

- With high localisation levels and economies of scale, the cost of spares, servicing, etc. are extremely economical and consequently the ownership cost of a Maruti Suzuki vehicle remains relatively lower than the competition (an enviable advantage in a cost-conscious market like India).
- The unmatched service and distribution network is an added advantage. At the end of the quarter, the company had a sales network of 889 outlets covering 631 cities. Service network stood at 2,879 workshops, covering 1,373 cities.
- Hence we expect the company to whither the storm as far as volumes and market-share are concerned. However, post the revision in royalty computation coupled with increased competition and and higher input costs we see limited scope for margin expansion from these levels.

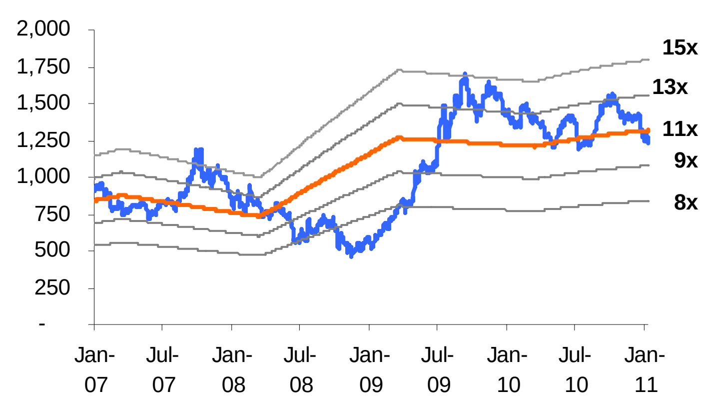
## Upgrade to BUY on attractive valuations

- Maruti Suzuki has underperformed the benchmark by over 20% over the last 12 months on account of market share concerns coupled with the higher royalty. While some market share loss in the longer term is inevitable, we believe that the current valuations capture most of the negatives.
- At the CMP of INR1,234, the stock is attractively valued - trading at a P/E of 13.8x and Cash P/E of 9.7x, discounting our FY12e earnings. We upgrade our recommendation from HOLD to BUY in light of the attractive valuations. Our target price of INR1,450 (11x FY12e Cash EPS + INR50 for the subsidiaries) provides an 18% upside from the current levels.

**Maruti Suzuki: 1-year-forward PE band**




**Maruti Suzuki: 1-year-forward CASH PE band**




Source: Company, Antique

# Financials

## Profit and loss account (INRm)

| Year ended 31st Mar | 2008 | 2009 | 2010 | 2011e | 2012e |
|---|---|---|---|---|---|
| **Revenues** | **179,362** | **204,553** | **290,989** | **357,669** | **417,180** |
| Expenses | 156,425 | 188,363 | 256,688 | 327,532 | 383,006 |
| **EBITDA** | **22,937** | **16,190** | **34,301** | **30,137** | **34,174** |
| Depreciation & amortisation | 5,682 | 7,065 | 8,250 | 9,572 | 11,005 |
| **EBIT** | **17,255** | **9,125** | **26,051** | **20,565** | **23,169** |
| Interest expense | 596 | 510 | 335 | 254 | 179 |
| Other income | 8,371 | 9,985 | 10,209 | 11,431 | 12,802 |
| **Profit before tax** | **25,030** | **18,600** | **35,925** | **31,741** | **35,792** |
| Taxes incl deferred taxation | 7,722 | 4,571 | 10,949 | 8,892 | 10,022 |
| Profit after tax | 17,308 | 12,187 | 24,976 | 22,198 | 25,770 |
| **Adjusted profit after tax** | **17,308** | **14,029** | **24,976** | **22,850** | **25,770** |
| **EPS (INR)** | **59.9** | **42.2** | **86.4** | **76.8** | **89.2** |

## Balance sheet (INRm)

| Year ended 31st Mar | 2008 | 2009 | 2010 | 2011e | 2012e |
|---|---|---|---|---|---|
| Share Capital | 1,445 | 1,445 | 1,445 | 1,445 | 1,445 |
| Reserves & Surplus | 82,709 | 92,004 | 116,906 | 136,949 | 160,216 |
| **Networth** | **84,154** | **93,449** | **118,351** | **138,394** | **161,661** |
| Debt | 9,002 | 6,989 | 8,214 | 3,498 | 2,278 |
| **Capital Employed** | **93,156** | **100,438** | **126,565** | **141,891** | **163,940** |
| Gross Fixed Assets | 72,853 | 87,206 | 104,067 | 126,067 | 149,067 |
| Accumulated Depreciation | 39,888 | 46,498 | 53,820 | 63,392 | 74,397 |
| Capital work in progress | 7,363 | 8,613 | 3,876 | 6,876 | 8,876 |
| **Net Assets** | **40,328** | **49,321** | **54,123** | **69,551** | **83,546** |
| Investments | 51,807 | 31,733 | 71,766 | 72,484 | 79,732 |
| **Current Assets, Loans & Advances** | | | | | |
| Inventory | 10,380 | 9,023 | 12,088 | 14,699 | 17,144 |
| Debtors | 6,555 | 9,378 | 8,099 | 10,779 | 12,573 |
| Cash & Bank balance | 3,305 | 19,390 | 982 | 8,790 | 10,677 |
| Loans & advances and others | 10,739 | 17,309 | 16,555 | 17,703 | 18,592 |
| **Current Liabilities & Provisions** | | | | | |
| Liabilities | 24,562 | 30,358 | 29,394 | 45,683 | 52,357 |
| Provisions | 3,695 | 3,807 | 6,284 | 5,341 | 5,235 |
| **Net Current Assets** | **2,722** | **20,935** | **2,046** | **947** | **1,394** |
| Deferred tax (assets)/liabilities | 1,701 | 1,551 | 1,370 | 1,090 | 732 |
| **Application of Funds** | **93,156** | **100,438** | **126,565** | **141,891** | **163,940** |

## Per share data

| Year ended 31st Mar | 2008 | 2009 | 2010 | 2011e | 2012e |
|---|---|---|---|---|---|
| No. of shares (m) | 289.0 | 289.0 | 289.0 | 289.0 | 289.0 |
| BVPS (INR) | 291.2 | 323.4 | 409.5 | 478.9 | 559.4 |
| CEPS (INR) | 79.6 | 66.6 | 115.0 | 109.9 | 127.3 |
| DPS (INR) | 5.0 | 3.5 | 6.0 | 6.4 | 7.4 |

## Margins (%)

| Year ended 31st Mar | 2008 | 2009 | 2010 | 2011e | 2012e |
|---|---|---|---|---|---|
| EBITDA | 12.8 | 7.9 | 11.8 | 8.4 | 8.2 |
| EBIT | 9.6 | 4.5 | 9.0 | 5.7 | 5.6 |
| PAT | 9.6 | 6.9 | 8.6 | 6.4 | 6.2 |

Source: Company, Antique

## Key assumptions (Nos.)

| YE 31st Mar | 2008 | 2009 | 2010 | 2011e | 2012e |
|---|---|---|---|---|---|
| A1 | 69,553 | 49,383 | 33,028 | 24,771 | 21,055 |
| A2 | 499,280 | 511,396 | 633,190 | 797,819 | 917,492 |
| A3 | 49,334 | 75,928 | 99,315 | 125,137 | 143,907 |
| MPV | 89,729 | 77,948 | 101,325 | 162,120 | 186,438 |
| MUV | 3,927 | 7,489 | 3,932 | 5,505 | 6,331 |
| **Total Domestic** | **711,823** | **722,144** | **870,790** | **1,115,352** | **1,275,224** |
| Exports | 53,024 | 70,023 | 147,575 | 138,721 | 149,818 |
| **Total Volumes** | **764,847** | **792,167** | **1,018,365** | **1,254,073** | **1,425,042** |
| Growth (%) | 7% | 4% | 29% | 23% | 14% |

## Cash flow statement (INRm)

| Year ended 31st Mar | 2008 | 2009 | 2010 | 2011e | 2012e |
|---|---|---|---|---|---|
| **EBIT** | **17,255** | **9,125** | **26,051** | **20,565** | **23,169** |
| Depreciation & amortisation | 5,017 | 7,065 | 8,250 | 9,572 | 11,005 |
| Interest expense | 596 | 510 | 335 | 254 | 179 |
| (Inc)/Dec in working capital | 201 | 2,128 | (481) | (8,907) | (1,439) |
| Tax paid | 7,696 | 4,721 | 11,130 | 9,172 | 10,380 |
| **CF from operating activities** | **13,779** | **8,831** | **23,317** | **29,619** | **25,054** |
| Capital expenditure | 16,359 | 15,603 | 12,124 | 25,000 | 25,000 |
| Inc/(Dec) in investments | 17,715 | (20,074) | 40,033 | 718 | 7,248 |
| Income from investments | 8,371 | 9,985 | 10,209 | 11,431 | 12,802 |
| **CF from investing activities** | **(25,703)** | **14,456** | **(41,948)** | **(14,287)** | **(19,446)** |
| Inc/(Dec) in debt | 2,694 | (2,013) | 1,225 | (4,716) | (1,219) |
| Dividends paid | (1,693) | (2,892) | (74) | (2,156) | (2,503) |
| **CF from financing activities** | **1,001** | **(4,905)** | **1,151** | **(6,872)** | **(3,722)** |
| **Net cash flow** | **(10,923)** | **16,085** | **(18,408)** | **7,808** | **1,886** |
| Opening balance | 14,228 | 3,305 | 19,390 | 982 | 8,790 |
| **Closing balance** | **3,305** | **19,390** | **982** | **8,790** | **10,677** |

## Growth indicators (%)

| Year ended 31st Mar | 2008 | 2009 | 2010 | 2011e | 2012e |
|---|---|---|---|---|---|
| Revenue | 22 | 14 | 42 | 23 | 17 |
| EBITDA | 15 | (29) | 112 | (12) | 13 |
| PAT | 11 | (19) | 78 | (9) | 13 |
| EPS | 11 | (30) | 105 | (11) | 16 |

## Valuation (x)

| Year ended 31st Mar | 2008 | 2009 | 2010 | 2011e | 2012e |
|---|---|---|---|---|---|
| P/E | 20.6 | 29.3 | 14.3 | 16.1 | 13.8 |
| Cash P/E | 15.5 | 18.5 | 10.7 | 11.2 | 9.7 |
| P/BV | 4.2 | 3.8 | 3.0 | 2.6 | 2.2 |
| EV/EBITDA | 12.5 | 17.7 | 8.4 | 9.5 | 8.4 |
| EV/Sales | 1.6 | 1.4 | 1.0 | 0.8 | 0.7 |
| Dividend Yield (%) | 0.4% | 0.3% | 0.5% | 0.5% | 0.6% |

## Financial ratios

| Year ended 31st Mar | 2008 | 2009 | 2010 | 2011e | 2012e |
|---|---|---|---|---|---|
| RoE (%) | 21 | 15 | 21 | 17 | 16 |
| RoCE (%) | 30 | 21 | 30 | 24 | 23 |
| Debt/Equity (x) | 0.1 | 0.1 | 0.1 | 0.0 | 0.0 |
| EBIT/Interest (x) | 29.0 | 17.9 | 77.8 | 80.9 | 129.5 |

Source: Company Antique

## Important Disclaimer:



| | |
|---|---|
| Analyst ownership in stock | No |

ANTIQUE

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