

Maruti Suzuki

Expectedly Disappointing!

Result highlights

Revenues were in-line with our estimates, up 26% YoY and 4% QoQ. EBITDA 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



31 January 2011

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

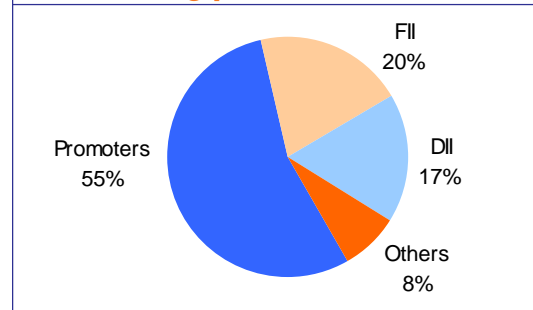
Source: Bloomberg

Returns (%)

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

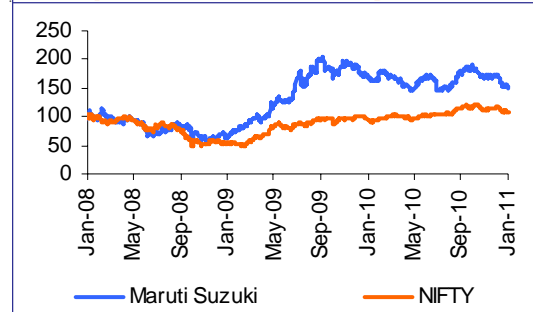
Source: Bloomberg

Shareholding pattern



Source: BSE

Price performance vs Nifty



Source: Bloomberg

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.

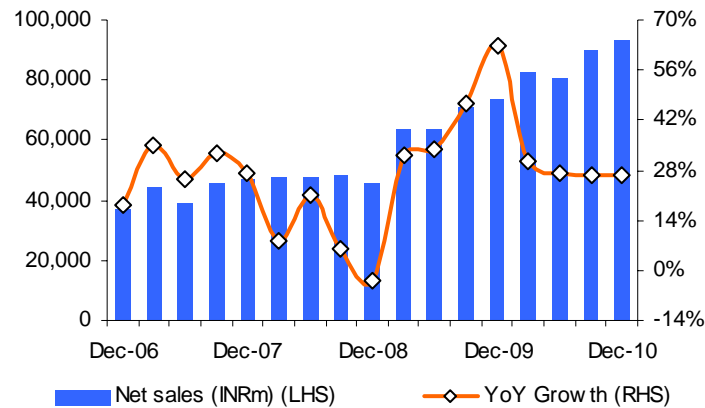
Volumes

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

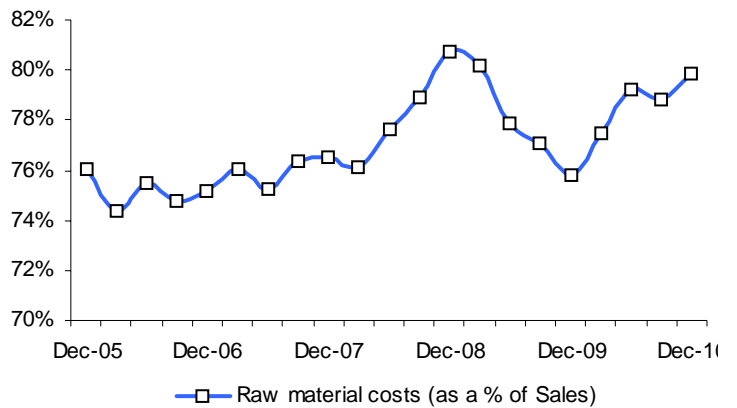
Quarterly trends

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

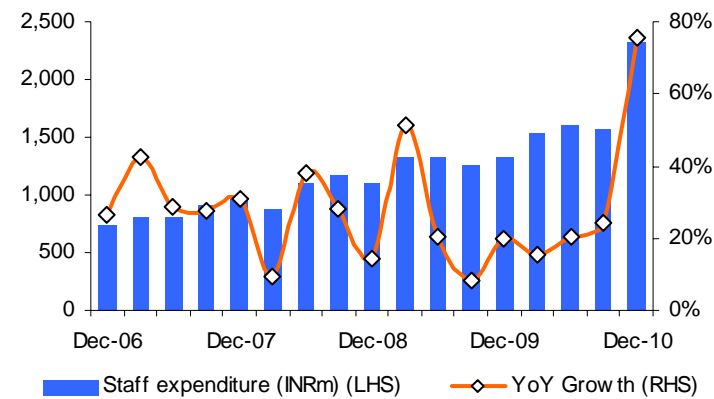


Source: Company, Antique

Raw material costs up 401bps YoY; 102 bps QoQ

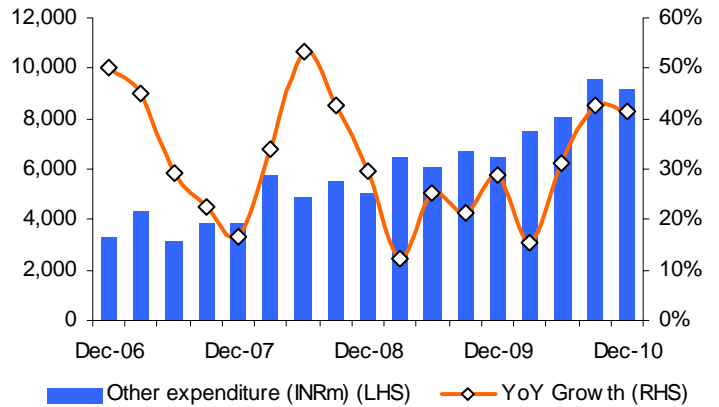


Staff expenditure up 76% YoY (48% QoQ) on account of one-off costs to the tune of INR510m

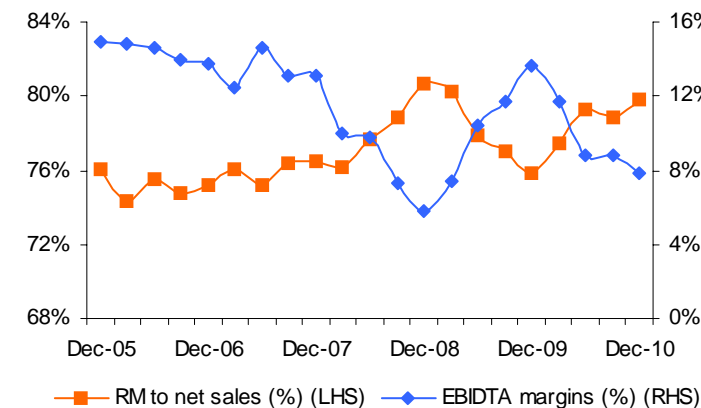


Source: Company, Antique

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

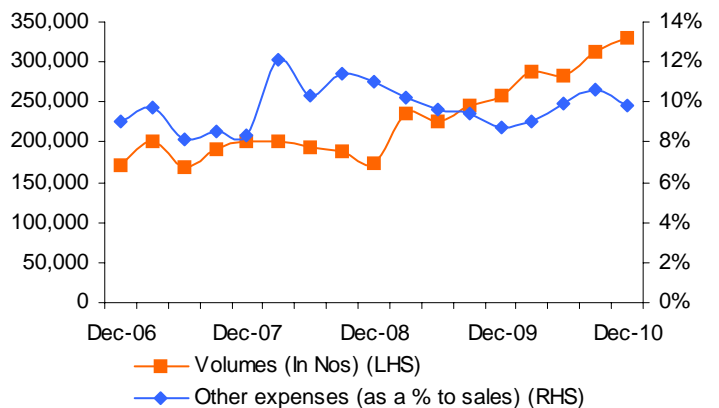


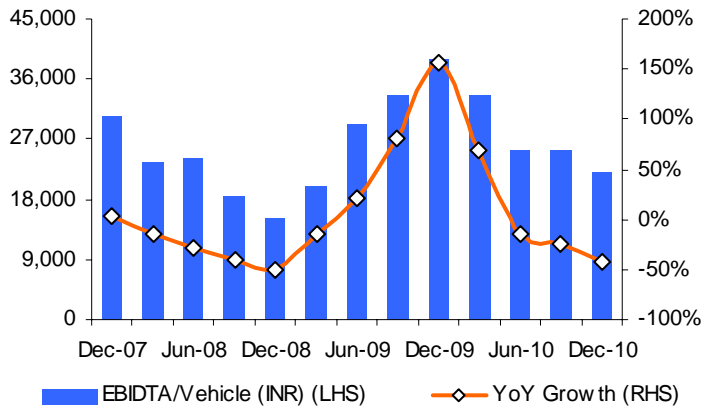
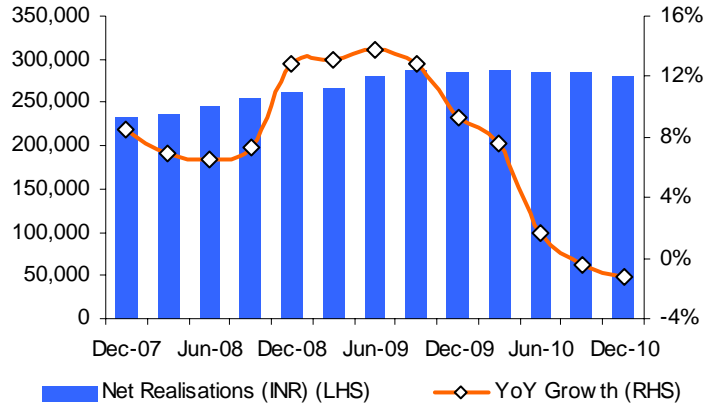
EBIDTA margins impacted on all fronts (input costs, seasonal discounts, royalty, adverse currency)... Adjusting for one-off staff costs margins stood at 8.3%



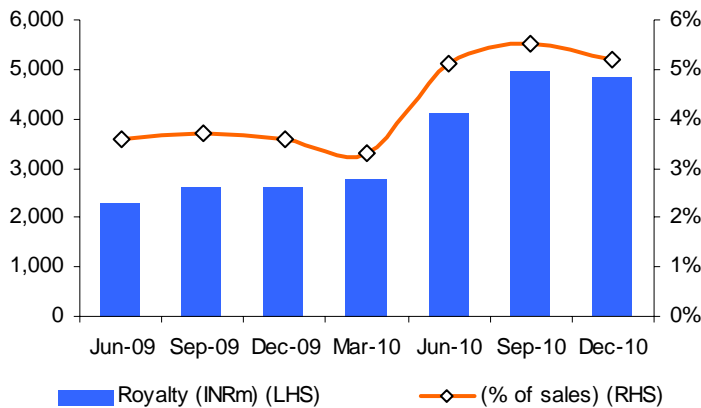
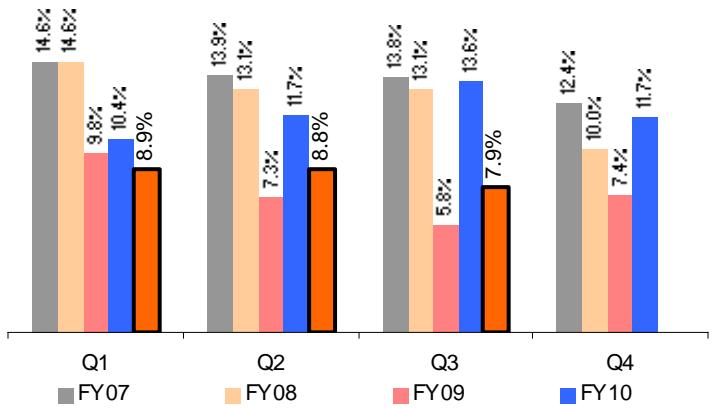
Source: Company, Antique

Cost reduction helped mitigate some of input cost pressures

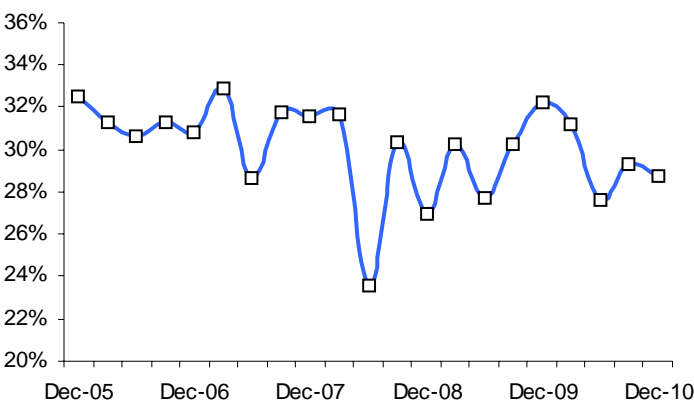
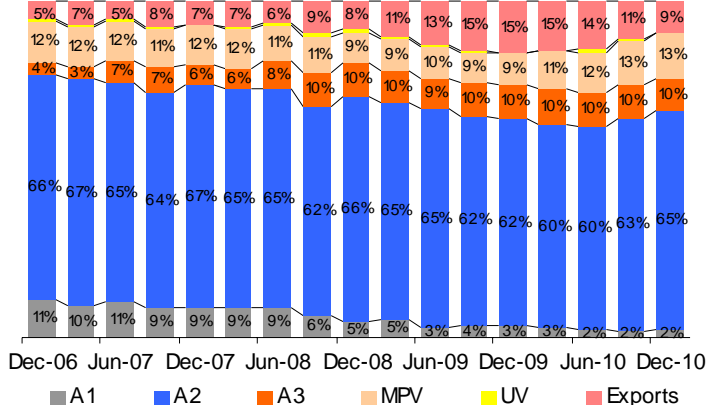


EBITDA/vehicle lower by 43% YoY (12% QoQ)

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


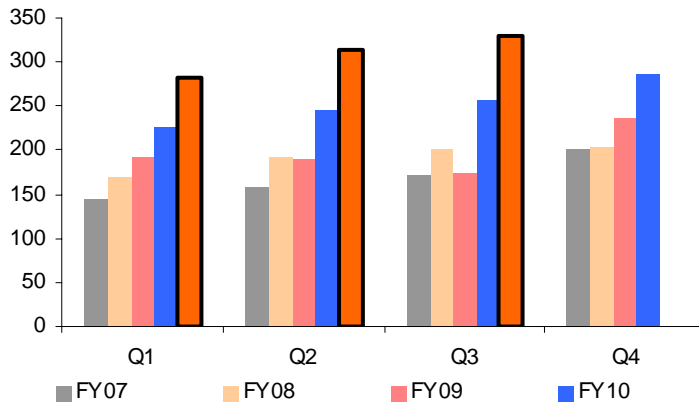
Source: Company, Antique

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

EBITDA margins trend - Close to historic lows


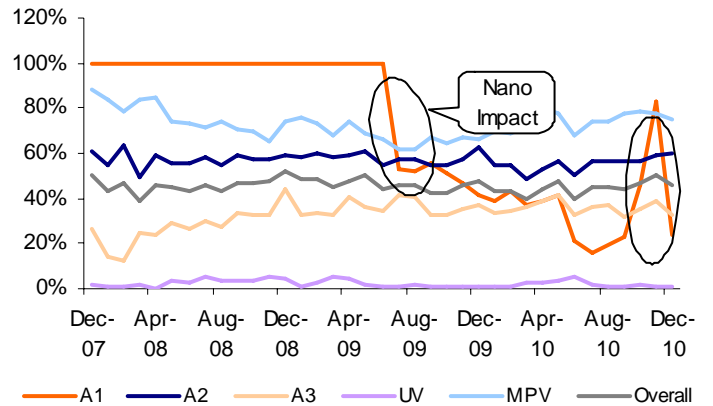
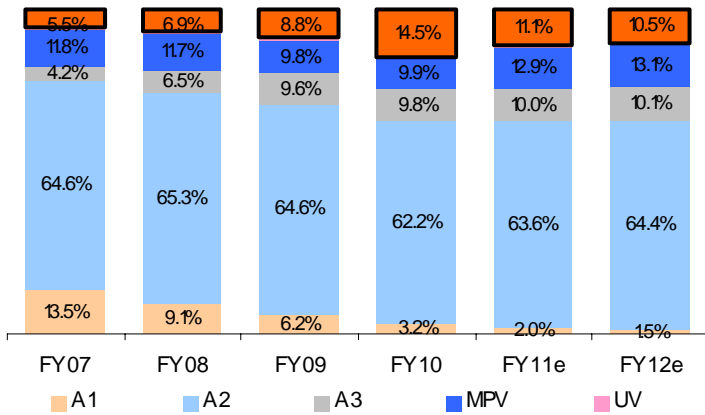
Source: Company, Antique

Lower tax rates driven by uptick in R&D expenses

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


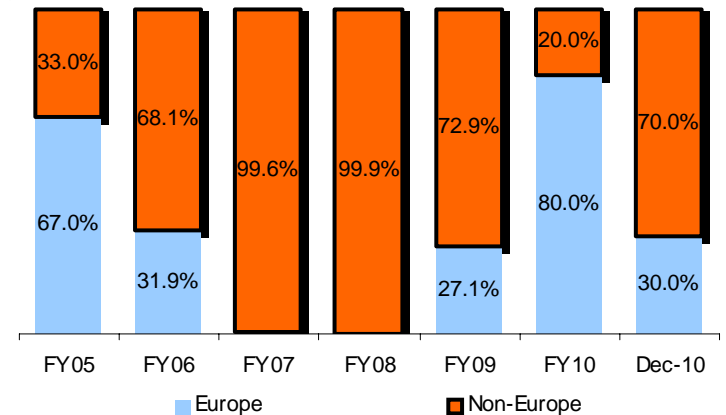
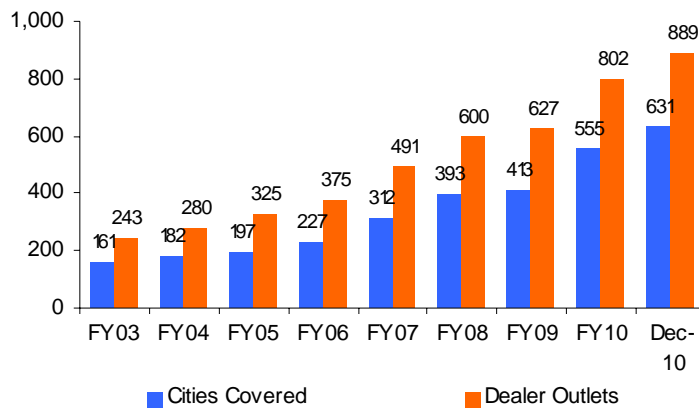
Source: Company, Antique

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


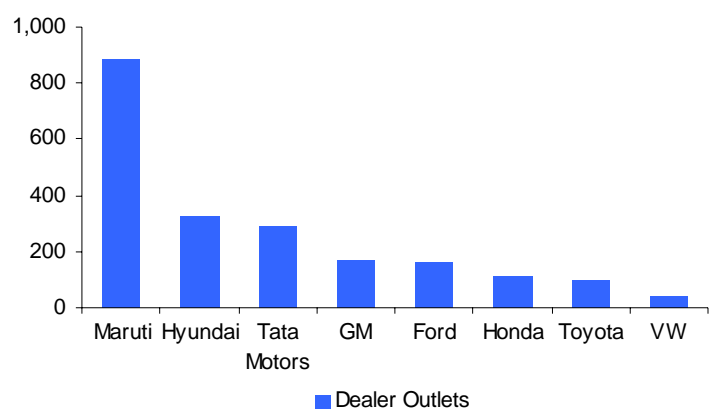
Source: Company, Antique

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

Contribution from exports is reducing


Source: Company, Antique

Exports Break-up - Contribution from Europe decreasing

Dealer network only gets stronger...


Source: Company, Antique

... and remains miles ahead of competition


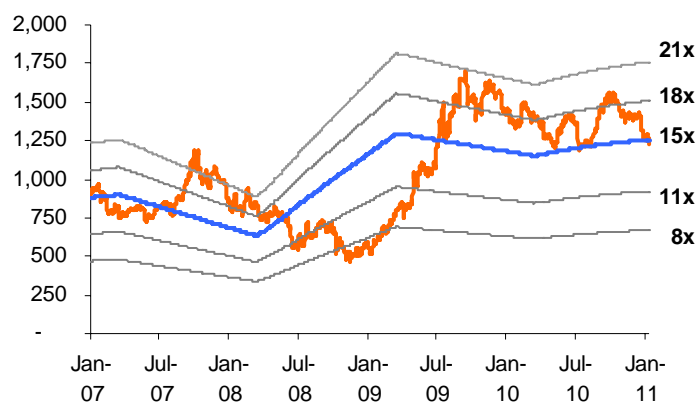
Our view – Strong volumes to offset margin woes...

- 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 higher input costs we see limited scope for margin expansion from these levels.

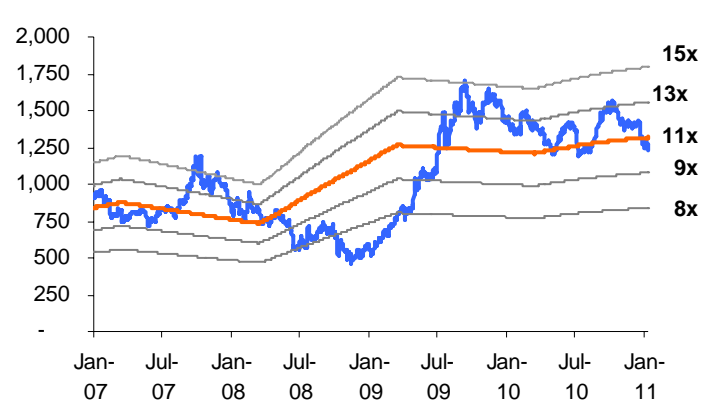
Upgrade to BUY on attractive valuations

- 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

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