

January 18, 2012

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Rating	Accumulate
Price	Rs1,108
Target Price	Rs1,170
Implied Upside	5.6%
Sensex	16,466
Nifty	4,967

(Prices as on January 17, 2012)

Trading data

Market Cap. (Rs bn)	320.2
Shares o/s (m)	288.9
3M Avg. Daily value (Rs m)	840.5

Major shareholders

Promoters	54.21%
Foreign	19.24%
Domestic Inst.	17.70%
Public & Other	8.85%

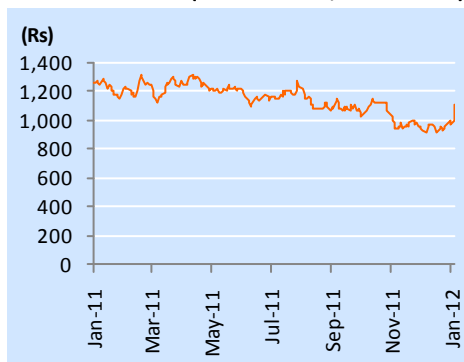
Stock Performance

(%)	1M	6M	12M
Absolute	19.0	(5.9)	(12.7)
Relative	12.7	5.4	0.1

How we differ from Consensus

EPS (Rs)	PL	Cons.	% Diff.
2012	55.3	65.5	-15.6
2013	77.9	84.7	-8.0

Price Performance (RIC: MRTI.BO, BB: MSIL IN)



Source: Bloomberg

Our positive stance on MSIL, leading to an upgrade from 'Reduce' to 'Accumulate' on September 8, 2011 by us and reiterated in our *Top Picks presentation* released on December 9, 2011, was mainly driven by the following key arguments:

- Double-digit volume growth at 15%+ in FY13E, driven by diesel engine capacity expansion to 24K/month by January 2012 from 20K/month, resumption of operations at Manesar and the new 'Swift' garnering over 1 lac bookings.
- MSIL getting RBI approval to hedge its vendor imports (Yen-denominated indirect imports account for ~12% of Net Sales), starting Q4FY12E, which we had communicated to our clients.
- Valuations attractive after the stock had corrected 30%+ (till September 2011) in the last one year; thereby, risk-reward turning favourable.
- One of the arguments we had used while pitching for MSIL was that vendors' exposure, which till now was unhedged, will soon be hedged. On January 17, 2012, the management interview in media mentioned that MSIL has taken the step of hedging currency exposure on behalf of 25-30 vendors who together import about Rs50bn worth of Japanese components every year.
- **Our view:** Currently, with Yen appreciating by ~22% YTD FY12E, MSIL is under severe margin pressure as total Yen-denominated import content (Direct +indirect) stands at 23% of Net Sales. While the hedging for direct imports was in place, the unhedged exposure of vendors was a big uncertainty (overhang on the stock). This move, currently being implemented, is in line with our arguments, driving our positive stance on MSIL.

Cont...2

Key financials (Y/e March)	2010	2011	2012E	2013E
Revenues (Rs m)	296,229	370,402	346,681	414,773
Growth (%)	42.1	25.0	(6.4)	19.6
EBITDA (Rs m)	39,761	36,439	26,783	35,909
PAT (Rs m)	25,194	23,181	15,980	22,522
EPS (Rs)	87.2	80.2	55.3	77.9
Growth (%)	106.7	(8.0)	(31.1)	40.9
Net DPS (Rs)	6.0	7.5	8.5	10.5

Profitability & Valuation	2010	2011	2012E	2013E
EBITDA margin (%)	13.4	9.8	7.7	8.7
RoE (%)	23.8	18.1	11.0	14.0
RoCE (%)	22.4	17.4	10.9	13.9
EV / sales (x)	1.1	0.8	0.9	0.7
EV / EBITDA (x)	8.2	8.2	11.1	8.3
PE (x)	12.7	13.8	20.0	14.2
P / BV (x)	2.7	2.3	2.1	1.9
Net dividend yield (%)	0.5	0.7	0.8	0.9

Source: Company Data; PL Research

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- **Hedging on behalf of vendors – A big positive:** With the hedging for vendors now in place, we believe MSIL has cushioned itself against the volatile currency fluctuations which impacted its profitability in FY12E. EBITDA margins are likely to be impacted by ~200bps YoY in FY12E, purely on account of the Yen-Rupee movement.
- **Price increase of 0.3-3.4% across various models:** MSIL has also taken a price increase to the extent of 0.3-3.4% on vehicles across the board on account of commodity cost pressures. The price hike has been in the range of Rs2,400-17,000 across models, except the '*Swift Dzire*', effective from January 16, 2012.
- **Advice investors to accumulate the stock post Q3FY12E results:** The stock has given 19.0% absolute returns in the last one month. With Q3FY12E profit likely to be lower by 60%+ YoY and a recent run-up in the stock price, we advise caution to the investors, as absolute upside from hereon is capped at ~6%. Any disappointment in the quarterly result, would lead to correction in the stock price, which could provide an entry point to long-term investors. Hence, one can accumulate the stock post Q3FY12E results scheduled on January 23, 2012.
- **We reiterate our positive stance on MSIL:** We expect a volume growth of 15%+ in FY13E, driven by strong order backlog for the new '*Swift*' and augmentation of diesel capacity by 20%. At the CMP, the stock is trading at 14.2x FY13E EPS, which in our view is attractive, given the 40%+ growth in PAT in FY13E (albeit from a lower base). We reiterate our '**Accumulate**' rating on the stock.

Income Statement (Rs m)

Y/e March	2010	2011	2012E	2013E
Net Revenue	296,229	370,402	346,681	414,773
Raw Material Expenses	224,134	288,801	274,044	326,103
Gross Profit	72,095	81,601	72,637	88,671
Employee Cost	5,456	7,035	7,809	8,410
Other Expenses	26,878	38,127	38,045	44,351
EBITDA	39,761	36,439	26,783	35,909
Depr. & Amortization	8,250	9,635	10,628	11,524
Net Interest	335	244	260	250
Other Income	4,749	4,170	4,940	6,300
Profit before Tax	35,925	30,730	20,835	30,436
Total Tax	10,949	8,201	5,615	7,913
Profit after Tax	24,976	22,529	15,220	22,522
Ex-Od items / Min. Int.	(218)	(652)	(760)	—
Adj. PAT	25,194	23,181	15,980	22,522
Avg. Shares O/S (m)	289.0	289.0	289.0	289.0
EPS (Rs.)	87.2	80.2	55.3	77.9

Cash Flow Abstract (Rs m)

Y/e March	2010	2011	2012E	2013E
C/F from Operations	28,874	32,856	31,909	29,627
C/F from Investing	(47,833)	(1,655)	(27,972)	(27,379)
C/F from Financing	551	(7,098)	(2,428)	(2,707)
Inc. / Dec. in Cash	(18,408)	24,103	1,510	(458)
Opening Cash	19,390	982	25,085	26,595
Closing Cash	982	25,085	26,595	26,136
FCFF	17,064	11,064	757	1,616
FCFE	18,289	5,943	757	1,616

Key Financial Metrics

Y/e March	2010	2011	2012E	2013E
Growth				
Revenue (%)	42.1	25.0	(6.4)	19.6
EBITDA (%)	102.3	(8.4)	(26.5)	34.1
PAT (%)	106.7	(8.0)	(31.1)	40.9
EPS (%)	106.7	(8.0)	(31.1)	40.9
Profitability				
EBITDA Margin (%)	13.4	9.8	7.7	8.7
PAT Margin (%)	8.5	6.3	4.6	5.4
RoCE (%)	22.4	17.4	10.9	13.9
RoE (%)	23.8	18.1	11.0	14.0
Balance Sheet				
Net Debt : Equity	0.1	(0.2)	(0.2)	(0.1)
Net Wrkng Cap. (days)	(18)	(18)	(26)	(19)
Valuation				
PER (x)	12.7	13.8	20.0	14.2
P / B (x)	2.7	2.3	2.1	1.9
EV / EBITDA (x)	8.2	8.2	11.1	8.3
EV / Sales (x)	1.1	0.8	0.9	0.7
Earnings Quality				
Eff. Tax Rate	30.5	26.7	26.9	26.0
Other Inc / PBT	13.7	15.4	26.4	20.7
Eff. Depr. Rate (%)	7.9	7.5	6.6	6.1
FCFE / PAT	72.6	25.6	4.7	7.2

Source: Company Data, PL Research.

Balance Sheet Abstract (Rs m)

Y/e March	2010	2011	2012E	2013E
Shareholder's Funds	118,351	138,328	151,157	170,108
Total Debt	8,214	3,093	3,093	3,093
Other Liabilities	1,370	1,644	1,644	1,644
Total Liabilities	127,935	143,065	155,894	174,845
Net Fixed Assets	54,123	69,580	90,828	106,180
Goodwill	—	—	—	—
Investments	71,766	50,677	46,773	46,276
Net Current Assets	2,046	22,809	18,293	22,389
<i>Cash & Equivalents</i>	982	25,085	26,595	26,136
<i>Other Current Assets</i>	36,742	38,522	42,626	47,994
<i>Current Liabilities</i>	35,678	40,798	50,927	51,742
Other Assets	—	—	—	—
Total Assets	127,935	143,065	155,894	174,845

Quarterly Financials (Rs m)

Y/e March	Q4FY11	Q1FY12	Q2FY12	Q3FY12E
Net Revenue	100,922	85,293	78,316	75,316
EBITDA	9,597	7,644	5,702	4,529
<i>% of revenue</i>	9.5	9.0	7.3	6.0
Depr. & Amortization	2,467	2,425	2,664	2,650
Net Interest	64	58	109	4
Other Income	1,199	1,800	1,178	1,340
Profit before Tax	8,266	7,462	3,347	3,216
Total Tax	1,667	1,970	942	868
Profit after Tax	6,599	5,492	2,405	2,348
Adj. PAT	6,599	4,992	3,165	2,348

Key Operating Metrics

Y/e March	2010	2011	2012E	2013E
A2 Seg. Vol. (nos)	633,190	808,552	693,196	786,777
Total Domestic Vol. (nos)	870,790	1,132,739	982,992	1,147,473
Export Vol. (nos)	147,575	138,266	124,969	125,000
Total Vol. (nos)	1,018,365	1,271,005	1,107,961	1,272,473
Net Realization/Unit (Rs)	290,887	291,424	312,900	325,958
RM Cost/Unit (Rs)	220,092	227,223	247,341	256,275
Other Exp./Unit (Rs)	26,393	29,997	34,338	34,854
EBITDA/Unit (Rs)	39,044	28,669	24,173	28,220
Net Profit/Unit (Rs)	24,526	17,725	14,188	17,700
Royalty (Rs m)	10,182	18,554	18,438	22,870
Royalty/Unit (Rs)	9,998	14,598	16,641	17,973

Source: Company Data, PL Research.