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Updates

Energy: Downstream stocks look inexpensive even assuming unfavorable subsidy-sharing scenarios

Automobiles: Auto tracker—September 2009

News Round-up

- ▶ **Yes Bank** will raise US\$150 mn (around Rs 750 crore) through private placement of equity in the current financial year. The bank will also raise around US\$100 mn (around Rs500 crore) through bond issues. As part of its fund raising plans, French financial institution **Proparco** will invest US\$20 mn in the bonds of the bank. (ET)
- ▶ **Future Logistics Solutions**, an arm of Kishore Biyani's **Future Group**, has forayed into third-party logistics (3 PL) operations by signing leading electronic and fast moving consumer goods (FMCG) players such as **Hitachi** and **Nestle**. (BS)
- ▶ The US\$13 bn **Ingersoll Rand** plc has earmarked about US\$100 mn investment in its Indian operations during the next three years and expects to source products and services of an equal amount. (BL)
- ▶ Foreign lender **Standard Chartered Bank** plans to hire around 2,000 employees in India in the current financial year. Foreign lender Standard Chartered Bank plans to hire around 2,000 employees in India in the current financial year. The banking major has also plans to open an office of its knowledge process outsourcing network -- Scope International-- in Bangalore by October. (ET)
- ▶ In an attempt to secure coal supplies for its fuel-starved power projects in India, state-run **NTPC Ltd** may spend an estimated US\$1 bn (Rs4,870 crore) to acquire a South African coal mining firm. (Mint)
- ▶ **Corus, Tata Steel's** European unit, will soon restart its mothballed Port Talbot plant in South Wales, a month after reopening its Llanwern strip mill at Newport. As demand picks up in the West, the company said it was preparing to re-ignite one of its two blast furnaces at the Port Talbot plant. However, a company official said the company was pressing ahead with a plan to cut 528 jobs in South Wales. Corus, which Tata Steel acquired for US\$12 bn in 2007, has laid off 5,545 employees, bringing announced job cuts, since the collapse in steel demand, to 14.4 per cent of its worldwide work force. (BS)
- ▶ **Tata Motors**, India largest truck maker, raised Rs236.5 crore on Monday by selling nearly half of its current investment in group firm Tata Steel. In a block deal on the Bombay Stock Exchange, the company sold five million shares of **Tata Steel** to group holding firm **Tata Sons** for Rs473 a share. (BS)

Source: ET= Economic Times, BS = Business Standard, FE = Financial Express, BL = Business Line.

EQUITY MARKETS

India	Change %			
	14-Sep	1-day	1-mo	3-mo
Sensex	16,214	(0.3)	5.2	9.0
Nifty	4,809	(0.4)	5.0	7.2
Global/Regional indices				
Dow Jones	9,627	0.2	3.3	11.8
Nasdaq Composite	2,092	0.5	5.4	15.2
FTSE	5,019	0.1	6.5	16.0
Nikkie	10,200	(0.0)	(3.7)	1.6
Hang Seng	20,932	(1.1)	0.2	13.2
KOSPI	1,646	0.7	3.4	16.6
Value traded - India				
Cash (NSE+BSE)	189.2		231.0	241.1
Derivatives (NSE)	580.3		638.9	755
Deri. open interest	1,019.6		783	849

Forex/money market

	Change, basis points			
	14-Sep	1-day	1-mo	3-mo
Rs/US\$	48.7	24	48	101
10yr govt bond, %	7.3	(12)	13	35
Net investment (US\$m)				
	11-Sep		MTD	CYTD
FIs	68		278	8,474
MFs	(70)		54	1,066

Top movers -3mo basis

Best performers	Change, %			
	14-Sep	1-day	1-mo	3-mo
TTMT IN Equity	564.3	2.5	20.7	64.7
ABAN IN Equity	1558.1	3.8	32.7	62.6
HCLT IN Equity	313.0	0.0	15.9	56.0
SCS IN Equity	118.5	(0.9)	14.5	54.4
TCS IN Equity	559.1	(0.2)	7.2	43.7
Worst performers				
BJFIN IN Equity	253.0	(0.5)	(13.3)	(36.8)
ICEM IN Equity	126.2	0.8	(5.8)	(20.8)
RNR IN Equity	87.4	(1.1)	5.7	(19.3)
RPWR IN Equity	162.7	(0.2)	(0.1)	(18.7)
SUEL IN Equity	94.8	(1.0)	7.3	(18.7)

SEPTEMBER 15, 2009

UPDATE

BSE-30: 16,214

Downstream stocks look inexpensive even if subsidy-sharing is unfavorable.

Our scenario analysis reveals inexpensive valuations for downstream oil companies under various subsidy-sharing formulas. The stocks look attractive (7X-10X FY2010E P/E) even if the companies were to bear 50% of auto fuel subsidy. We assume that (1) the government will bear the entire subsidy burden on cooking fuels and (2) the government and upstream companies will bear auto fuels subsidy equally.

Company data and valuation summary

Bharat Petroleum

Stock data		Forecasts/Valuations			
		2009	2010E	2011E	
52-week range (Rs) (high,low)	601-226	EPS (Rs)	20.6	79.8	65.0
Market Cap. (Rs bn)	185.8	EPS growth (%)	(50.1)	287.1	(18.5)
Shareholding pattern (%)		P/E (X)	27.5	7.1	8.7
Promoters	54.9	Sales (Rs bn)	1,340.7	910.6	935.1
FIs	8.3	Net profits (Rs bn)	7.5	28.8	23.5
MFs	7.6	EBITDA (Rs bn)	27.5	55.4	50.5
Price performance (%)		EV/EBITDA (X)	11.6	6.1	6.3
Absolute	1M 3M 12M	ROE (%)	5.3	18.9	13.8
Rel. to BSE-30	3.1 27.9 41.8	Div. Yield (%)	1.2	5.6	4.6

Company data and valuation summary

Hindustan Petroleum

Stock data		Forecasts/Valuations			
		2009	2010E	2011E	
52-week range (Rs) (high,low)	426-163	EPS (Rs)	17.0	73.1	58.5
Market Cap. (Rs bn)	133.7	EPS growth (%)	(49.3)	330.9	(19.9)
Shareholding pattern (%)		P/E (X)	23.3	5.4	6.7
Promoters	51.1	Sales (Rs bn)	1,249.3	852.2	876.9
FIs	8.9	Net profits (Rs bn)	4.8	24.8	19.8
MFs	10.8	EBITDA (Rs bn)	28.7	58.0	52.5
Price performance (%)		EV/EBITDA (X)	10.8	5.5	5.8
Absolute	1M 3M 12M	ROE (%)	4.4	17.7	12.8
Rel. to BSE-30	2.2 22.1 46.0	Div. Yield (%)	1.3	7.6	6.1

Company data and valuation summary

Indian Oil Corporation

Stock data		Forecasts/Valuations			
		2009	2010E	2011E	
52-week range (Rs) (high,low)	688-299	EPS (Rs)	19.7	101.8	79.3
Market Cap. (Rs bn)	750.3	EPS growth (%)	(67.9)	416.7	(22.1)
Shareholding pattern (%)		P/E (X)	32.3	6.3	8.0
Promoters	78.9	Sales (Rs bn)	3,041.3	2,333.9	2,398.6
FIs	0.9	Net profits (Rs bn)	23.5	123.4	96.3
MFs	2.0	EBITDA (Rs bn)	106.6	241.2	221.3
Price performance (%)		EV/EBITDA (X)	8.6	4.4	4.3
Absolute	1M 3M 12M	ROE (%)	4.8	22.6	15.6
Rel. to BSE-30	6.5 7.5 34.8	Div. Yield (%)	1.2	6.1	4.8

Subsidy-sharing scheme remains a puzzle but manageable for FY2010E

We see the valuations of downstream companies as reasonable under various scenarios of subsidy-sharing scheme for FY2010E assuming crude price at US\$65/bbl. We note continued uncertainty over the sharing of auto fuel subsidy for FY2010E between the upstream companies, downstream companies and the government. As per the petroleum secretary, the government will bear the entire subsidy on cooking fuels and downstream companies may bear a portion of the subsidy on auto fuels with the majority being borne by the government-owned upstream oil companies. We do not see large subsidy on auto fuels in a scenario of moderate crude oil prices (US\$55-70/bbl).

QUICK NUMBERS

- BPCL, HPCL and IOCL to trade at a P/E of 8X, 6.1X and 6.8X on FY2010E EPS even if they share a 20% subsidy on auto fuels
- BPCL, HPCL and IOCL to trade at a P/E of 8.8X, 6.6X and 7X on FY2010E EPS if they share 33.3% subsidy on auto fuels

Valuations of downstream companies look fine even under unfavorable subsidy-sharing scenarios

Exhibit 1 shows the earnings and valuations of downstream companies under different scenarios of auto fuel subsidy-sharing. Our scenario analysis reveals that the valuations of BPCL, HPCL and IOCL look reasonable on FY2010E P/E under all our assumed scenarios. We assume crude price (Dated Brent) at US\$65/bbl for FY2010E and we calculate very low under-recoveries on auto fuels at current domestic selling prices and our assumed crude oil price. We assume that the government will bear the entire subsidy on cooking fuels under all scenarios. Exhibit 2 shows the historical 12-month forward P/E chart for BPCL, HPCL and IOCL and reveals that the stocks have traded at similar multiples as compared to our worst-case scenario of 50% auto fuel subsidy burden on downstream companies.

- ▶ **Scenario 1: 20% sharing of auto fuel subsidy.** Based on FY2010E EPS, BPCL, HPCL and IOCL will trade at a P/E multiple of 8X, 6.1X and 6.8X, respectively, if downstream companies were to bear 20% of the subsidy on auto fuels.
- ▶ **Scenario 2: 33.3% sharing of auto fuel subsidy.** Based on FY2010E EPS, BPCL, HPCL and IOCL will trade at a P/E multiple of 8.8X, 6.6X and 7X, respectively, if downstream companies were to bear 33.3% of the subsidy on auto fuels. We assume that the remaining subsidy on auto fuels will be borne by the government and upstream companies.
- ▶ **Scenario 3: 50% sharing of auto fuel subsidy.** Based on FY2010E EPS, BPCL, HPCL and IOCL will trade at 8.8X, 6.6X and 7X, respectively, if downstream companies were to bear 50% of the subsidy on auto fuels. However, we do not expect downstream companies to bear 50% of the auto fuel subsidy as the subsidy-sharing is normally worked out on the relative profitability of companies and we expect the combined earnings of upstream companies (ONGC, GAIL and OIL India) to be significantly higher than the earnings of downstream companies (BPCL, HPCL and IOCL). Also, the oil minister had stated that a majority of the subsidy on auto fuels will be borne by upstream companies.

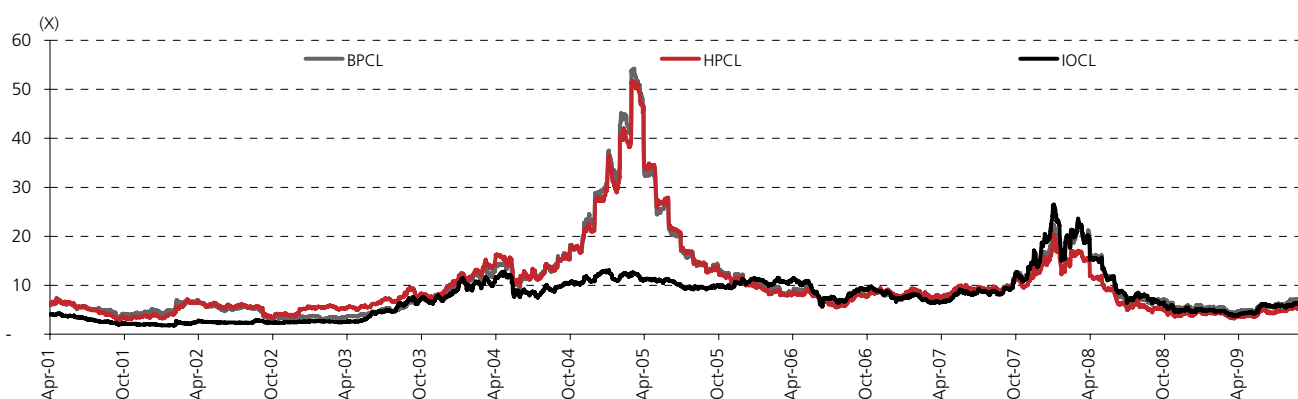
Oil marketing companies remain attractive even if they were to bear a portion of subsidy on auto fuels

Price/earnings (price to current year-end EPS) ratio for BPCL, HPCL and IOCL (X)

	Base case	Subsidy-burden on auto fuels (%)		
		20.0	33.3	50.0
BPCL				
Company's share of subsidy-burden (Rs mn)	—	5,059	8,431	12,647
FY2010E EPS (Rs)	79.8	70.5	64.4	56.7
P/E (X)	7.1	8.0	8.8	10.0
HPCL				
Company's share of subsidy-burden (Rs mn)	—	4,571	7,618	11,427
FY2010E EPS (Rs)	73.1	64.2	58.2	50.8
P/E (X)	5.4	6.1	6.8	7.8
IOCL				
Company's share of subsidy-burden (Rs mn)	—	9,203	15,338	23,007
FY2010E EPS (Rs)	101.8	96.8	93.4	89.3
P/E (X)	6.3	6.6	6.8	7.1

Source: Kotak Institutional Equities estimates

12-month forward P/E for BPCL, HPCL and IOCL (X)



Source: Bloomberg, Kotak Institutional Equities estimates

Consolidated profit model, balance sheet, cash model of BPCL, March fiscal year-ends, 2006-2012E (Rs mn)

	2006	2007	2008	2009	2010E	2011E	2012E
Profit model (Rs mn)							
Net sales	755,333	965,569	1,102,081	1,340,734	910,620	935,127	970,212
EBITDA	9,407	35,362	28,472	27,507	55,357	50,478	55,560
Other income	4,653	7,332	13,954	15,087	12,413	9,072	7,188
Interest	(2,474)	(4,774)	(6,725)	(21,664)	(13,931)	(12,002)	(9,461)
Depreciation	(7,680)	(9,041)	(10,982)	(10,755)	(10,145)	(11,927)	(12,444)
Pretax profits	3,906	28,879	24,719	10,176	43,694	35,622	40,842
Extraordinary items	176	(68)	—	—	—	—	—
Tax	(140)	(9,286)	(9,059)	(5,103)	(12,530)	(10,313)	(12,756)
Deferred taxation	(1,025)	(268)	(1,108)	2,421	(2,322)	(1,795)	(1,126)
Net profits	2,916	18,055	15,806	7,359	28,843	23,514	26,960
Net profits after minority interests	2,916	18,055	15,806	7,359	28,843	23,514	26,960
Earnings per share (Rs)	7.6	50.1	43.7	20.4	79.8	65.0	74.6
Balance sheet (Rs mn)							
Total equity	91,394	102,735	116,768	121,281	136,588	149,067	163,375
Deferred taxation liability	13,558	13,826	14,814	12,392	14,714	16,509	17,635
Total borrowings	83,736	108,292	150,224	211,714	206,153	163,653	124,403
Current liabilities	94,070	112,767	145,803	128,313	111,143	119,599	121,904
Total liabilities and equity	282,758	337,620	427,608	473,701	468,599	448,829	427,318
Cash	4,921	8,640	9,616	4,416	4,595	4,068	4,280
Current assets	128,208	127,698	187,457	148,469	140,624	144,803	146,647
Goodwill	—	—	—	—	—	—	—
Total fixed assets	110,855	118,334	127,354	140,033	166,393	167,970	169,404
Investments	38,774	82,949	103,182	180,784	156,988	131,988	106,988
Total assets	282,758	337,621	427,608	473,701	468,599	448,829	427,318
Free cash flow (Rs mn)							
Operating cash flow, excl. working capital	9,275	29,920	22,988	19,717	28,897	28,163	33,343
Working capital	1,577	11,451	(25,161)	20,585	(7,810)	5,531	461
Capital expenditure	(19,945)	(17,908)	(20,665)	(23,323)	(36,505)	(13,504)	(13,878)
Investments	(28,146)	(45,481)	(21,684)	(82,456)	23,796	25,000	25,000
Other income	1,785	4,337	6,434	6,655	10,897	7,818	7,188
Free cash flow	(35,455)	(17,682)	(38,088)	(58,822)	19,275	53,008	52,113
Ratios (%)							
Debt/equity	91.6	105.4	128.7	174.6	150.9	109.8	76.1
Net debt/equity	86.2	97.0	120.4	170.9	147.6	107.1	73.5
RoAE	3.3	16.3	12.7	5.5	20.2	14.8	15.6
RoACE	4.1	11.0	7.9	5.1	11.7	9.9	10.9
Key assumptions (standalone until FY2005)							
Crude throughput (mn tons)	17.2	19.8	20.9	20.0	20.2	22.7	22.7
Effective tariff protection (%)	2.9	1.6	1.4	2.4	2.4	2.4	2.4
Net refining margin (US\$/bbl)	2.1	3.1	5.6	5.0	3.1	3.8	4.4
Sales volume (mn tons)	23.3	24.5	26.7	28.1	29.1	30.2	31.4
Marketing margin (Rs/ton)	(671)	(1,140)	(3,010)	(5,944)	665	1,440	1,435
Subsidy under-recoveries (Rs mn)	(31,847)	(20,159)	(26,680)	(27,706)	—	—	—

Source: Company, Kotak Institutional Equities estimates

Profit model, balance sheet, cash model of HPCL, March fiscal year-ends, 2006-2012E (Rs mn)

	2006	2007	2008	2009	2010E	2011E	2012E
Profit model (Rs mn)							
Net sales	708,609	889,959	1,043,130	1,249,348	852,192	876,930	926,556
EBITDA	8,056	24,036	15,757	28,707	58,033	52,476	61,677
Other income	3,285	6,845	11,980	9,057	5,014	4,466	2,401
Interest	(1,587)	(4,230)	(7,925)	(20,828)	(14,705)	(15,569)	(16,250)
Depreciation	(6,902)	(7,040)	(8,508)	(9,813)	(10,812)	(11,323)	(11,919)
Pretax profits	2,851	19,611	11,303	7,122	37,531	30,050	35,910
Extraordinary items	2,201	3,030	—	—	—	—	—
Tax	(898)	(6,625)	(1,799)	(2,416)	(11,536)	(7,829)	(10,003)
Deferred taxation	(97)	(365)	(2,025)	(343)	(1,220)	(2,385)	(2,202)
Prior period adjustment	—	61	3,870	1,387	—	—	—
Net profits	4,056	15,712	11,349	5,750	24,774	19,836	23,704
Earnings per share (Rs)	6.6	40.0	33.5	17.0	73.1	58.5	69.9
Balance sheet (Rs mn)							
Total equity	87,357	95,987	105,633	107,306	120,183	130,490	142,811
Deferred tax liability	13,844	14,209	15,960	16,034	17,254	19,639	21,841
Total borrowings	66,638	105,175	167,867	227,552	239,552	207,673	160,173
Current liabilities	79,549	101,195	124,337	117,558	94,965	99,203	100,927
Total liabilities and equity	247,389	316,566	413,797	468,450	471,954	457,006	425,753
Cash	426	868	2,940	6,083	1,540	1,484	1,480
Current assets	109,674	113,779	190,034	153,844	140,139	144,590	148,063
Total fixed assets	97,013	130,644	152,452	166,558	179,255	179,914	180,190
Investments	40,276	71,275	68,371	141,965	151,018	131,018	96,018
Total assets	247,389	316,566	413,796	468,450	471,953	457,007	425,751
Free cash flow (Rs mn)							
Operating cash flow, excl. working capital	10,126	23,966	(18,679)	(12,139)	29,321	28,155	35,424
Working capital changes	(5,351)	8,936	(6,504)	48,461	(7,656)	729	(1,749)
Capital expenditure	(25,298)	(38,510)	(31,638)	(19,275)	(21,038)	(11,058)	(12,195)
Investments	(22,884)	(31,704)	(1,851)	(70,386)	(9,054)	20,000	35,000
Other income	941	2,067	4,692	3,187	3,782	3,524	2,401
Free cash flow	(42,466)	(35,246)	(53,980)	(50,151)	(4,645)	41,350	58,881
Ratios (%)							
Debt/equity	65.8	95.4	138.1	184.5	174.3	138.3	97.3
Net debt/equity	65.4	94.7	135.6	179.6	173.2	137.3	96.4
RoAE	4.1	14.9	9.8	4.7	19.0	13.8	15.1
RoACE	2.5	8.8	6.4	5.8	9.9	9.2	11.0
Key assumptions							
Crude throughput (mn tons)	14.0	16.7	16.8	15.8	18.0	19.3	19.3
Effective tariff protection (%)	3.1	1.4	1.3	2.4	2.4	2.4	2.4
Net refining margin (US\$/bbl)	3.9	4.3	6.6	4.3	3.2	3.5	4.5
Sales volume (mn tons)	20.1	23.4	26.2	27.0	28.1	29.3	31.1
Marketing margin (Rs/ton)	(463)	(710)	(2,345)	(5,021)	797	1,424	1,415
Subsidy under-recoveries (Rs mn)	(29,671)	(18,899)	(28,549)	(28,432)	—	—	—

Source: Company, Kotak Institutional Equities estimates

Consolidated profit model, balance sheet, cash model of IOCL, March fiscal year-ends, 2006-2012E (Rs mn)

	2006	2007	2008	2009	2010E	2011E	2012E
Profit model (Rs mn)							
Net sales	1,729,474	2,149,428	2,444,378	3,041,265	2,333,855	2,398,593	2,515,212
EBITDA	82,044	110,451	120,872	61,445	202,393	178,692	197,459
Other income	21,310	27,451	43,748	45,155	38,821	42,630	33,941
Interest	(12,101)	(17,058)	(17,556)	(41,758)	(22,098)	(24,821)	(18,308)
Depreciation	(24,711)	(28,686)	(29,918)	(31,389)	(34,869)	(47,026)	(49,958)
Pretax profits	66,542	92,157	117,145	33,453	184,246	149,475	163,133
Extraordinary items	5,590	24,757	5,374	—	—	—	—
Tax	(19,975)	(25,834)	(38,293)	(13,316)	(50,296)	(38,118)	(51,772)
Deferred taxation	(1,282)	(8,040)	(473)	1,435	(7,318)	(12,773)	(3,762)
Net profits	51,125	82,729	83,430	25,523	126,633	98,583	107,599
Net profits after minority interests	45,362	62,469	74,573	27,437	123,424	96,307	104,541
Earnings per share (Rs)	38.8	52.4	62.5	23.0	101.8	79.3	86.1
Balance sheet (Rs mn)							
Total equity	317,977	378,117	450,449	470,654	548,282	602,426	662,039
Deferred tax liability	50,602	59,859	60,331	58,876	66,946	79,693	83,613
Total borrowings	292,395	290,215	382,818	465,250	604,326	511,941	266,829
Current liabilities	286,716	330,791	386,724	376,107	383,098	406,346	418,446
Total liabilities and equity	947,691	1,058,981	1,280,322	1,370,888	1,602,652	1,600,406	1,430,927
Cash	8,080	9,385	8,413	8,076	15,155	19,899	27,937
Current assets	413,904	437,178	599,256	473,965	551,932	567,956	578,742
Total fixed assets	383,717	415,014	460,307	565,545	705,661	732,647	694,344
Investments	141,990	197,403	212,345	318,208	329,904	279,904	129,904
Total assets	947,691	1,058,981	1,280,322	1,365,795	1,602,652	1,600,406	1,430,927
Free cash flow (Rs mn)							
Operating cash flow, excl. working capital	(10,334)	(44,660)	(107,263)	(345,677)	123,589	109,973	123,534
Working capital changes	(8,136)	2,237	(1,414)	76,881	(60,869)	7,450	4,869
Capital expenditure	(49,042)	(50,969)	(79,586)	(135,923)	(139,810)	(57,647)	(12,112)
Investments	(17,778)	99,768	92,665	299,410	(10,894)	49,073	150,015
Other Income	10,317	13,582	18,253	16,413	29,010	35,093	33,011
Free cash flow	(74,973)	19,958	(77,346)	(88,896)	(58,973)	143,941	299,317
Ratios (%)							
Debt/equity	79.3	66.3	74.9	87.9	98.2	75.1	35.8
Net debt/equity	77.1	64.1	73.3	86.3	95.8	72.1	32.0
RoAE	13.7	16.1	16.3	5.5	22.3	15.4	15.1
RoACE	9.3	11.3	11.2	4.8	13.5	10.8	11.2
Key assumptions (IOC standalone)							
Crude throughput (mn tons)	38.5	44.0	47.4	51.3	52.4	53.4	53.4
Effective tariff protection (%)	3.1	1.6	1.3	2.8	2.8	2.8	2.8
Net refining margin (US\$/bbl)	4.8	4.2	8.2	3.6	4.0	4.2	5.1
Sales volume (mn tons)	50.4	53.4	57.4	61.0	63.7	65.9	68.3
Marketing margin (Rs/ton)	26	(633)	(2,203)	(5,253)	923	1,394	1,393
Subsidy under-recoveries (Rs mn)	(95,361)	(34,041)	(64,486)	(55,535)	—	—	—

Source: Company, Kotak Institutional Equities estimates

SEPTEMBER 15, 2009

UPDATE

BSE-30: 16,214

Auto tracker – September 2009. August saw good growth in 2-wheelers and passenger car sales, on the back of strong demand recovery. M&HCV sales showed yoy growth as demand for goods vehicles improved. Channel checks indicate a sharp rebound in 2HFY10 for commercial vehicles, aided by strong industrial production and changes in emission regulations. Motorcycle sales showed stronger than expected sequential growth of 12%, partly driven by inventory build-up ahead of festive season.

2-wheeler volumes increase 12% sequentially on strong demand and festival inventory

2-wheeler sales broke out of the low-700,000 range in August, growing 12% from July. Some of this was driven by inventory build-up ahead of the festival season. Motorcycles gained some share of the 2-wheeler market, making up 79% of 2-wheeler volumes versus 76% in July. Hero Honda outperformed by a wide margin as sales grew 37% yoy while Bajaj grew 4% and TVS sales were 12% yoy. Hero Honda's market share grew 510 bps yoy to 63.8%. Industry 3W sales increased 23% yoy, primarily driven by strong demand for passenger carriers. Bajaj Auto remains the biggest beneficiary of this trend with their 3-wheeler sales up 33% yoy.

Domestic passenger car sales grew 25% yoy off a low base; no sign of inventory build-up in cars

Industry car sales grew 25% yoy led mainly by strong growth in the compact car segment, which grew 34% yoy. Sequentially, growth was muted and in line with seasonality at 3.6%. Maruti's market share grew 210 bps to 53% versus 50.9% a year ago and was flat from July. Maruti's share of the compact segment was flat at 57.3% in August from 57.4% in July and was up 230 bps on a yoy basis. Industry UV sales increased 7% yoy in August with Mahindra seeing a 47% yoy increase.

M&HCV volumes show yoy improvement on goods demand; LCVs continue to show strength

Industry CV sales improved 18.5% yoy in August. LCVs continued to outperform with 32% yoy growth while M&HCVs were up 4% yoy. Sequentially, both M&HCVs and LCVs saw an 8% increase. We expect CV volumes to pick up further in 2HFY10E on the back of recent pick up seen in industrial production, as depicted by IIP. Apart from easy comparisons, growth rates in 2HFY10 would be buoyed by emission regulation changes effective from April 2010, which could result in pre-buy. Bus segment volumes continued to show yoy declines but we expect these to pick up as JNNURM orders get delivered.

Stocks: Monsoon concerns abate; peak valuations keep us cautious and selective

Steady rainfall in the past few weeks have allayed some of the concerns regarding an impending drought. We expect industry volumes to continue to grow at a healthy pace for the rest of the fiscal year, given the strong demand environment and easy year-ago comparisons. We expect demand to stay strong on (1) payout from the Sixth Pay Commission (arrears), (2) easier and cheaper financing and (3) improvement in urban markets. We believe that these positives are largely factored in the stocks as reflected by valuations at the higher end of the historical range. We remain selective and prefer Bajaj Auto over Hero Honda in the 2-wheeler universe and Ashok Leyland over Tata Motors in the CV space. Peak valuation at the time of peak margins and peak product cycle keeps us away from Maruti. Uncertainties regarding the strength of a rebound in luxury car volumes globally and poor cash generation at Jaguar Land Rover keeps us cautious on Tata Motors.

QUICK NUMBERS

- Passenger car sales were up 25% yoy in August
- CV sales were up 18.5% yoy with M&HCVs up 4% yoy and LCVs up 32% yoy

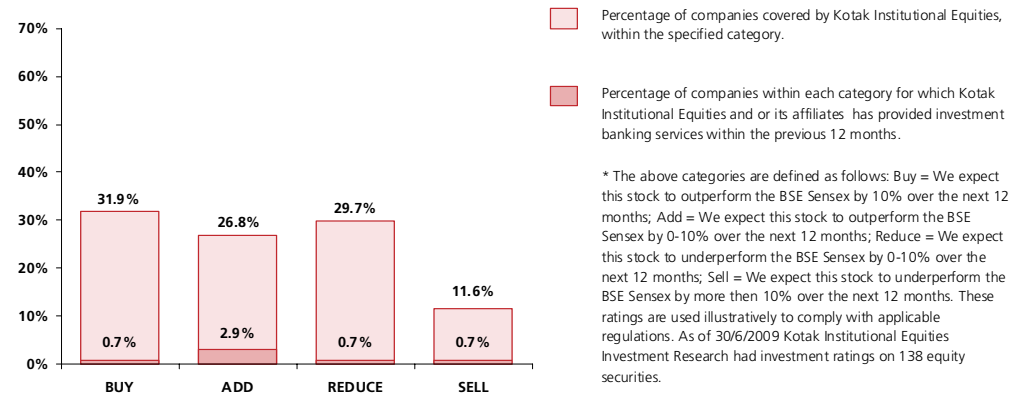
Automobile Industry Summary: August 2009

	YOY			MOM			YTD		
	Aug-09	Aug-08	% chg yoy	Aug-09	Jul-09	% chg mom	FY2010	FY2009	% chg yoy
Industry: domestic sales (units)									
Scooters	118,694	96,441	23.1	118,694	123,259	(3.7)	559,327	464,615	20.4
Motorcycles	611,173	485,270	25.9	611,173	546,245	11.9	2,847,149	2,431,148	17.1
Mopeds	46,878	35,683	31.4	46,878	49,550	(5.4)	223,103	179,114	24.6
Total two-wheelers	776,777	620,883	25.1	776,777	719,668	7.9	3,632,304	3,086,019	17.7
Three-wheelers	39,201	31,959	22.7	39,201	36,184	8.3	166,672	148,732	12.1
M&HCVs	17,345	16,679	4.0	17,345	16,138	7.5	72,346	95,368	(24.1)
LCVs	23,279	17,612	32.2	23,279	21,486	8.3	102,737	84,386	21.7
Total CVs	40,624	34,291	18.5	40,624	37,624	8.0	175,083	179,754	(2.6)
Passenger cars	131,421	104,910	25.3	131,421	126,815	3.6	609,406	537,618	13.4
Utility vehicles	20,679	19,328	7.0	20,679	20,827	(0.7)	102,384	102,430	(0.0)
Company: domestic sales (units)									
Hero Honda: motorcycles	389,814	284,752	36.9	389,814	342,042	14.0	1,780,857	1,396,697	27.5
Bajaj Auto: motorcycles	121,644	116,887	4.1	121,644	109,161	11.4	560,999	618,655	(9.3)
Bajaj Auto: three-wheelers	15,810	11,866	33.2	15,810	14,573	8.5	68,019	54,176	25.6
TVS Motor: motorcycles	40,509	36,092	12.2	40,509	31,916	26.9	196,236	203,863	(3.7)
Maruti: passenger cars	69,629	53,351	30.5	69,629	67,314	3.4	332,968	284,138	17.2
Tata Motors: passenger cars	18,906	14,506	30.3	18,906	18,983	(0.4)	85,393	73,801	15.7
Tata Motors: M&HCVs	10,661	10,143	5.1	10,661	10,658	0.0	47,945	56,833	(15.6)
Tata Motors: LCVs	14,802	10,594	39.7	14,802	13,139	12.7	63,153	49,049	28.8
Ashok Leyland: M&HCVs	4,161	4,227	(1.6)	4,161	3,490	19.2	14,318	26,613	(46.2)
M&M: utility vehicles	11,443	7,700	48.6	11,443	11,660	(1.9)	58,134	41,503	40.1
Domestic market shares (%)									
Hero Honda: motorcycles	63.8	58.7	5.1	63.8	62.6	1.2	62.5	57.5	5.1
Bajaj Auto: motorcycles	19.9	24.1	(4.2)	19.9	20.0	(0.1)	19.7	25.4	(5.7)
Bajaj Auto: three-wheelers	40.3	37.1	3.2	40.3	40.3	0.1	40.8	36.4	4.4
TVS Motor: motorcycles	6.6	7.4	(0.8)	6.6	5.8	0.8	6.9	8.4	(1.5)
Maruti: passenger cars	53.0	50.9	2.1	53.0	53.1	(0.1)	54.6	52.9	1.8
Tata Motors: passenger cars	14.4	13.8	0.6	14.4	15.0	(0.6)	14.0	13.7	0.3
Tata Motors: M&HCVs	61.5	60.8	0.7	61.5	66.0	(4.6)	66.3	59.6	6.7
Tata Motors: LCVs	63.6	60.2	3.4	63.6	61.2	2.4	61.5	58.1	3.3
Ashok Leyland: M&HCVs	24.0	25.3	(1.4)	24.0	21.6	2.4	19.8	27.9	(8.1)
M&M: utility vehicles	55.3	39.8	15.5	55.3	56.0	(0.6)	56.8	40.5	16.3

Source: SIAM, Kotak Institutional Equities

Kotak Institutional Equities Research coverage universe

Distribution of ratings/investment banking relationships



Source: Kotak Institutional Equities

As of June 30, 2009

Ratings and other definitions/identifiers

Rating system

Definitions of ratings

BUY. We expect this stock to outperform the BSE Sensex by 10% over the next 12 months.

ADD. We expect this stock to outperform the BSE Sensex by 0-10% over the next 12 months.

REDUCE. We expect this stock to underperform the BSE Sensex by 0-10% over the next 12 months.

SELL. We expect this stock to underperform the BSE Sensex by more than 10% over the next 12 months.

Our target price are also on 12-month horizon basis.

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