

SEPTEMBER 13, 2011

UPDATE

Coverage view: **Cautious**

Price (Rs): **132**

Target price (Rs): **120**

BSE-30: **16,467**

**Competitive pressures mounting; downgrade to SELL.** Exide's recent pricing actions in both automotive and industrial business reflect rising competitive pressures which are likely to moderate earnings growth for the company, in our view. We believe the company's ability to price its products at a premium is under threat, which is likely to impact profitability. We downgrade the company to SELL (from REDUCE), maintaining our negative stance on the company.

### Company data and valuation summary

Exide Industries

#### Stock data

52-week range (Rs) (high,low)	188-110
Market Cap. (Rs bn)	111.9

#### Shareholding pattern (%)

Promoters	46.0
FIs	16.1
MFs	4.2

#### Price performance (%)

	1M	3M	12M
Absolute	(16.6)	(15.8)	(17.8)
Rel. to BSE-30	(14.7)	(6.6)	(4.1)

#### Forecasts/Valuations

	2011	2012E	2013E
EPS (Rs)	7.5	6.8	7.9
EPS growth (%)	18.0	(8.9)	17.0
P/E (X)	17.7	19.4	16.6
Sales (Rs bn)	45.5	50.3	56.6
Net profits (Rs bn)	6.3	5.8	6.7
EBITDA (Rs bn)	8.8	8.1	9.3
EV/EBITDA (X)	12.7	13.8	12.0
ROE (%)	25.5	19.4	19.5
Div. Yield (%)	1.1	1.0	1.0

### Market share loss coupled with slowdown in inverter volumes to impact earnings

We expect Exide to lose market share to Amara Raja over the next two years in the automotive replacement market due to better product quality and higher warranty offered by Amara Raja. Exide has lost 4% market share to Amara Raja in the organized replacement 4 wheeler segment in the past year. Amara Raja has also gained 20% market share in the past three years in the two wheeler organized automotive battery segment. We expect another 3% loss in market share for Exide in FY2012 and FY2013E. Inverter battery volumes are also declining at a sharp pace, driven by reduction in power cuts in India. Exide is also facing stiff competition from Luminous, Sukam and Microtec which have cut prices significantly to protect their volumes.

### Margins could be under pressure in both automotive and industrial battery segments

Exide has cut automotive and inverter battery prices by 10-15%, respectively, in September 2011, in line with market prices. We believe this pricing actions could reduce profitability of both businesses. We factor in 3% decline in EBITDA margins over the next two years led by industrial battery business. We expect flat margins in the automotive battery business as pricing pressure in automotive business could be offset by increased sourcing from captive lead smelters.

### We reduce earnings estimates by 17-21% over FY2012-2013E

We have revised our estimates by 17-21% over FY2012-2013E, which reflects a (1) 4-6% cut in the automotive battery volumes and automotive battery revenues by 2-7% over FY2012-2013E to reflect market share loss to competitors, and (2) we also cut industrial battery revenues by 5-8% over FY2012-2013E to factor in a sharp slowdown in the inverter battery segment and further increase in competition in UPS segment as excess capacities will be used in the growing UPS segment.

We reduce our target price to Rs120 (from Rs160) based on a sum-of-the-parts valuation methodology. We have cut our target multiple on a standalone business from 15X to 14X PE on our FY2013E earnings estimate to factor in slower earnings growth and lower returns than earlier forecasted. We keep our Rs 12/share value for insurance business unchanged.

Hitesh Goel  
hitesh.goel@kotak.com  
Mumbai: +91-22-6634-1327

Kotak Institutional Equities Research  
kotak.research@kotak.com  
Mumbai: +91-22-6634-1100

### Competitive pressures evident; Downgrade to SELL

We downgrade Exide to SELL (from REDUCE) for several reasons.

- (1) We expect to see Exide lose market share in the organized replacement automotive battery segment. Exide has lost 7% market share to in the organized replacement 4-wheeler segment in the past year. Amara Raja has also gained 20% market share in the past three years in the two wheeler organized automotive battery segment. We expect another 3% loss in market share for Exide in FY2012 and FY2013E.
- (2) Significant slowdown in the inverter battery segment due to lower power cuts. In 1QFY12, Exide's inverter battery volumes declined by 26% yoy.
- (3) Threat to Exide's pricing power. Exide has cut automotive battery prices by 10% and inverter battery prices by 15% in September 2011. Average lead prices have not changed much since 1QFY12 but have fallen by 9% from peak levels. Lead cost forms 65% of net sales for Exide and hence a 9% correction would have led to a 6% price correction if it was a case of only passing of lead prices to the customer.

Our channel checks also suggest that Exide batteries were retailing at a premium to competitors like Amara Raja and with the price cuts Exide has aligned its prices with Amara Raja prices. Amara Raja is also offering higher replacement warranty batteries in the market of close to 60 months while Exide gives maximum 36 month warranty on its products.

We have revised our estimates by 17-21% over FY2012-2013E which reflects (1) 4-6% cut in the automotive battery volumes and automotive battery revenues by 2-7% over FY2012-2013E to reflect market share loss to competitors and (2) our cut in industrial battery revenues by 5-8% over FY2012-2013E to factor in a sharp slowdown in inverter battery segment and further increase in competition in UPS segment as excess capacities will be used in the growing UPS segment.

#### We cut our earnings by 17-21% over FY2012-2013E

Earnings revision table, March fiscal year-ends (Rs mn)

	New estimates		Old estimates		% change	
	2012E	2013E	2012E	2013E	2012E	2013E
Net sales	50,262	56,613	51,875	61,071	(3.1)	(7.3)
EBITDA	8,094	9,282	9,543	11,587	(15.2)	(19.9)
EBITDA margin (%)	16.1	16.4	18.4	19.0		
Adjusted PAT (standalone)	5,768	6,747	6,915	8,501	(16.6)	(20.6)
<b>EPS standalone</b>	<b>6.8</b>	<b>7.9</b>	<b>8.1</b>	<b>10.0</b>	<b>(16.6)</b>	<b>(20.6)</b>

Source: Kotak Institutional Equities estimates

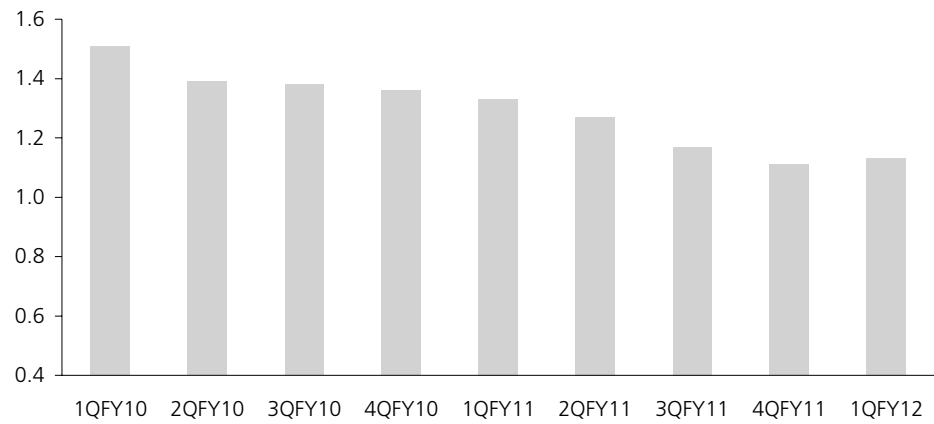
#### Exide Industries - sum-of-the-parts valuation methodology

Valuation methodology, March fiscal year-ends (Rs mn)

	EPS (Rs)	PE (X)	Per share value
Standalone FY2013 EPS	7.9	14	111
ING Vysya (50% stake value)			12
<b>SOTP based value</b>			<b>123</b>
<b>SOTP based value</b>			<b>120</b>

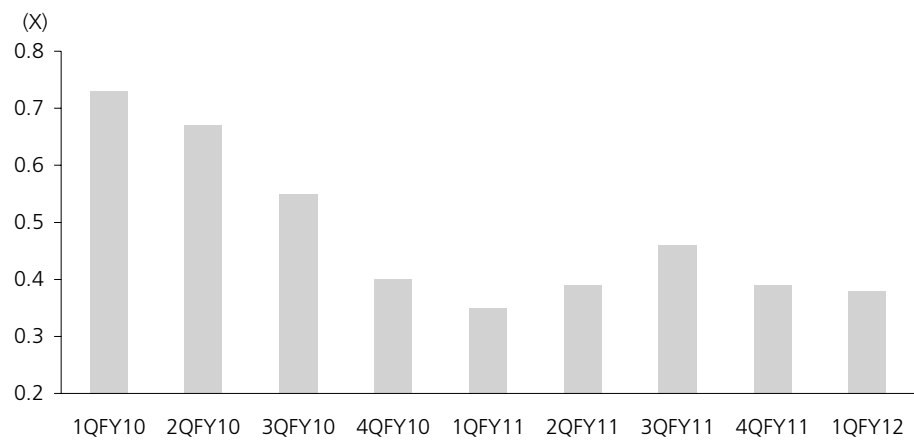
Source: Kotak Institutional Equities estimates

**Replacement/OEM volume mix has been declining over the last two years**  
four-wheeler volume mix, March fiscal year-ends, 1QFY10-1QFY12 (X)



Source: Company

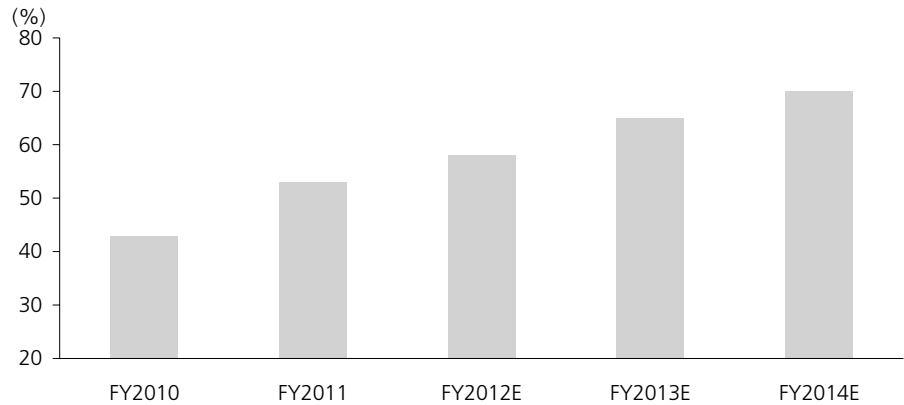
**Replacement/OEM volume mix in two-wheelers has also declined sharply**  
Two-wheeler volume mix, March fiscal year-ends, 1QFY10-1QFY12



Source: Company

**We expect lead contribution to improve to 65% in FY2012E**

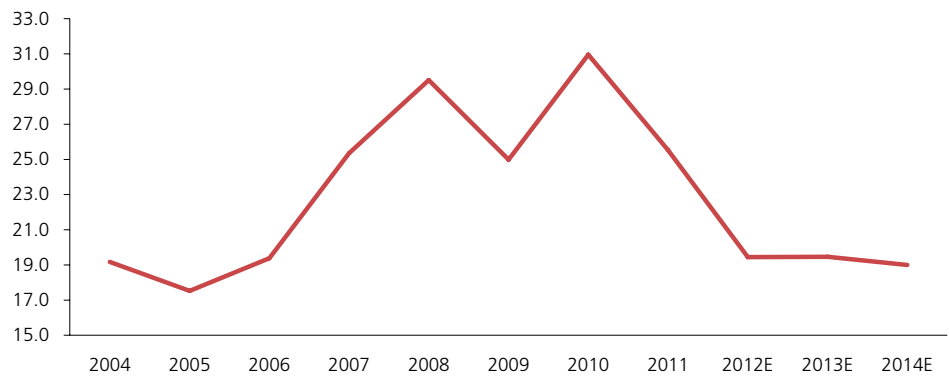
Lead smelter contribution to lead sourced from Exide, March fiscal year-ends (%)



Source: Company, Kotak Institutional Equities estimates

**Return on equity is likely to decline sharply due to moderate growth in earnings**

Return on equity, March fiscal year-ends, 2004-2014E (%)



Source: Company, Kotak Institutional Equities estimates

We expect Exide's automotive battery volumes to increase at a 13% CAGR over the next two years  
Volume assumptions, March fiscal year-ends, 2010-2014E (units)

	2010	2011	2012E	2013E	2014E
<b>4 wheeler volumes (mn units)</b>					
4wh - OEM	3.1	3.8	4.1	4.5	5.1
YoY change (%)		23.7	6.0	12.0	12.0
4 wh - Replacement	4.3	4.7	4.7	5.1	5.7
YoY change (%)		8.5	0.8	9.1	10.0
<b>Total 4 wheeler volumes</b>	<b>7.4</b>	<b>8.5</b>	<b>8.8</b>	<b>9.7</b>	<b>10.7</b>
YoY change (%)		14.9	3.1	10.4	10.9
Replacement/OEM mix (X)	1.39	1.22	1.16	1.13	1.11
<b>2 wheeler volumes (mn units)</b>					
2wh - OEM	5.5	7.8	10.2	11.7	13.5
YoY change (%)		42.4	30.0	15.0	15.0
2 wh - Replacement	3.2	3.1	3.9	4.3	4.9
YoY change (%)		(4.2)	26.7	12.0	11.9
<b>Total 2 wheeler volumes</b>	<b>8.7</b>	<b>10.9</b>	<b>14.1</b>	<b>16.1</b>	<b>18.3</b>
YoY change (%)		25.3	29.1	14.2	14.2
Replacement/OEM mix (X)	0.58	0.39	0.38	0.37	0.36
<b>Overall automotive volumes (mn units)</b>					
Total OEM volumes	8.6	11.7	14.3	16.3	18.6
Total Replacement volumes	7.5	7.7	8.6	9.5	10.5
<b>Total auto volumes</b>	<b>16.1</b>	<b>19.4</b>	<b>22.8</b>	<b>25.7</b>	<b>29.1</b>
YoY change (%)		20.5	17.7	12.7	13.0
<b>Automotive revenues (Rs mn)</b>	<b>23,650</b>	<b>29,180</b>	<b>34,346</b>	<b>39,495</b>	<b>45,503</b>
YoY change (%)		23.4	17.7	15.0	15.2
Automotive ASPs (Rs/unit)	1,469	1,504	1,504	1,534	1,565
YoY chg (%)		2.4	-	2.0	2.0
<b>Industrial battery volumes (mn units)</b>					
Industrial battery volumes	5.7	4.4	4.4	4.6	5.0
YoY change (%)		(22.8)	-	5.0	8.0
<b>Industrial revenues (Rs mn)</b>	<b>13,789</b>	<b>15,996</b>	<b>15,516</b>	<b>16,617</b>	<b>18,306</b>
YoY change (%)		16.0	(3.0)	7.1	10.2
Industrial ASPs (Rs/unit)	2,419	3,635	3,526	3,597	3,669
YoY change (%)		50.3	-3.0	2.0	2.0
Submarine battery revenues (Rs mn)	500	360	400	500	550
<b>Total volumes (mn units)</b>	<b>21.8</b>	<b>23.8</b>	<b>27.2</b>	<b>30.4</b>	<b>34.1</b>
YoY change (%)		9.2	14.4	11.5	12.2
<b>Net revenues (Rs mn)</b>	<b>37,940</b>	<b>45,536</b>	<b>50,262</b>	<b>56,613</b>	<b>64,359</b>
YoY change (%)		20.0	10.4	12.6	13.7

Source: Company, Kotak Institutional Equities estimates

Average lead prices for Aug-Sep 2011 period haven't declined much since 1QFY12  
Average LME Lead prices (\$/ton)



Source: Bloomberg

We expect earnings to increase at a muted 3% CAGR over the next two years  
Financial summary, March fiscal year-ends, 2009-2014E (Rs mn)

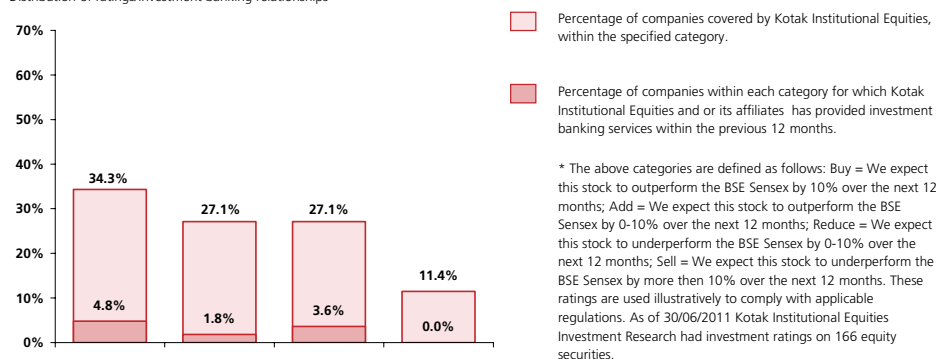
	2009	2010	2011	2012E	2013E	2014E
<b>Profit model (Rs mn)</b>						
Net sales	33,930	37,940	45,536	50,262	56,613	64,359
<b>EBITDA</b>	<b>5,448</b>	<b>8,894</b>	<b>8,788</b>	<b>8,094</b>	<b>9,282</b>	<b>10,461</b>
Other income	65	121	1,038	1,008	1,345	1,613
Interest	(479)	(103)	(57)	(31)	(34)	(9)
Depreciation	(679)	(807)	(835)	(946)	(1,090)	(1,209)
<b>Profit before tax</b>	<b>4,354</b>	<b>8,106</b>	<b>8,934</b>	<b>8,124</b>	<b>9,503</b>	<b>10,856</b>
Tax expense	(1,510)	(2,735)	(2,740)	(2,356)	(2,756)	(3,148)
<b>Adjusted net profit</b>	<b>2,844</b>	<b>5,371</b>	<b>6,335</b>	<b>5,768</b>	<b>6,747</b>	<b>7,708</b>
<b>Adjusted earnings per share (Rs)</b>	<b>3.6</b>	<b>6.3</b>	<b>7.5</b>	<b>6.8</b>	<b>7.9</b>	<b>9.1</b>
<b>Balance sheet (Rs mn)</b>						
Equity	12,504	22,198	27,425	31,918	37,390	43,823
Total Borrowings	3,172	900	22	300	50	50
Deferred Tax Liability	412	590	675	675	675	675
Current liabilities	4,866	5,929	7,964	7,830	8,578	9,491
<b>Total liabilities</b>	<b>20,954</b>	<b>29,616</b>	<b>36,086</b>	<b>40,723</b>	<b>46,693</b>	<b>54,039</b>
Net fixed assets	6,853	7,144	9,018	11,772	13,182	13,973
Investments	6,682	13,354	13,780	13,940	18,180	21,840
Cash	337	29	148	202	234	1,100
Other current assets	7,082	9,089	13,140	14,809	15,097	17,127
<b>Total assets</b>	<b>20,954</b>	<b>29,616</b>	<b>36,086</b>	<b>40,723</b>	<b>46,693</b>	<b>54,039</b>
<b>Free cash flow (Rs mn)</b>						
Operating cash flow	3,456	6,355	7,115	6,715	7,837	8,917
Working capital changes	488	(637)	(2,015)	(1,804)	460	(1,117)
Capital expenditure	(1,515)	(1,098)	(2,708)	(3,700)	(2,500)	(2,000)
Change in investments	(1,499)	(6,672)	(426)	(160)	(4,240)	(3,660)
<b>Free cash flow</b>	<b>1,804</b>	<b>3,683</b>	<b>1,209</b>	<b>11</b>	<b>4,597</b>	<b>4,600</b>
<b>Ratios</b>						
EBITDA margin (%)	16.1	23.4	19.3	16.1	16.4	16.3
PAT margin (%)	8.4	14.2	13.9	11.5	11.9	12.0
Net debt/equity (X)	0.2	0.0	(0.0)	0.0	(0.0)	(0.0)
Book Value (Rs/share)	15.6	26.1	32.3	37.6	44.0	51.6
RoAE (%)	25.0	31.0	25.5	19.4	19.5	19.0
<b>RoACE (%)</b>	<b>34.3</b>	<b>38.1</b>	<b>34.9</b>	<b>27.7</b>	<b>27.9</b>	<b>27.1</b>

Source: Company, Kotak Institutional Equities estimates

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Distribution of ratings/investment banking relationships



Source: Kotak Institutional Equities

As of June 30, 2011

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## Corporate Office

Kotak Securities Ltd.  
Bakhtawar, 1st Floor  
229, Nariman Point  
Mumbai 400 021, India  
Tel: +91-22-6634-1100

## Overseas Offices

Kotak Mahindra (UK) Ltd  
6th Floor, Portsoken House  
155-157 The Minories  
London EC 3N 1 LS  
Tel: +44-20-7977-6900 / 6940

Kotak Mahindra Inc  
50 Main Street, Suite No.310  
Westchester Financial Centre  
White Plains, New York 10606  
Tel:+1-914-997-6120

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