Maruti Suzuki India

Multiple Roadblocks to Scuffle through

WAY2WEALTH a COFFEE DAY venture

27th July 2011

Key Take Away

CMP	Rs 1206
Recommendation	HOLD

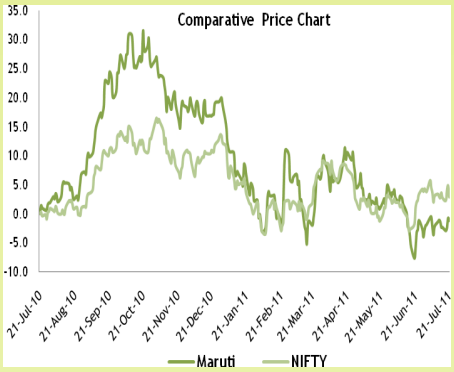
Scrip Details

Market Cap (Rs cr)	34,853
P/E (x) – FY13E	14
Equity Capital (Rs cr)	144.5
Face Value (Rs)	5.0
52 Week High/Low (Rs)	1599 / 1087
Website: www.marutisuzuki.com	
NSE Code	MARUTI
Sensex	18432
Nifty	5546

Shareholding Pattern (%)

As on June 2011	%
Promoters	54.21
MFs, FIs & Banks	18.0
FII	18.71
Other Bodies corporate	6.31
Public and others	2.77

Comparative Price Movement



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Maruti Suzuki India (MSIL) Q1FY12 Results were above our expectations with EBIDTA margin coming in as a surprise mainly on account of a lower Royalty Payout. Domestic growth has fallen to single digits as there has been lower conversion to sales despite healthy enquiries, on the back of the dismal macro-economic situation. Exports have seen a decline as the company has been focusing on diversifying its presence from European countries to Non –European countries. On the Domestic front we have the new Swift being launched in August, which is to compete with Toyota's Liva, Ford Figo and Hyundai's Brio. New Swift is cannibalizing Old Swift to a certain extent as the production of the latter has been stopped. Initial monthly runrate expected from this model is 15k-17k units, but much would depend upon consumer sentiment and company's pricing power in this segment. There was higher proportion of Diesel in the product mix to the tune of 21% of Domestic Sales as the arbitrage opportunity between Diesel and Petol prices has gone up by 35%-40% on a/c of petrol deregulation. This led to the Realisation being higher by 4% on a YoY Basis. Bulk of the Input cost inflation has been reflective in Q1, but going forward the fluctuation in Yen would put its margins under pressure as MSIL is not hedged post Q2FY12.

RBI's hawkish stance of anti-inflation has curtailed the growth in the sector with Retail numbers lagging Wholesale Billings, while attractive product launches at aggressive price points has curtailed MSIL's market share. There has been clear signs of interest rate hikes with consumers reacting to the higher costs by deferring their purchases. It is a broad-based slowdown with flat growth in the Top 10 cities & degrowth in the next 10 cities. Rural demand is growing, but at a slower pace. As the quantum of hike in this cycle has been higher than the earlier cycles, the impact on demand has been deeper with MSIL's inventory at 4-5 weeks as against its normal levels of 3-4 weeks. Additionally, the recent rate hike is expected to hurt demand in Q3, which would be minimized with the Festive Season. Our estimates factors in a volume CAGR of 6%from FY11-FY13E for MSIL, which, is below our PV estimates of a 9% CAGR during the same period.

At the CMP of Rs 1206, the stock discounts its FY12E & FY13E earnings of Rs83.1/Rs95.4 by a P/E multiple of 14.5x/12.6x respectively. We have lowered our Target Multiple from 15.5x to 14x (FY13E), given the demand related macro concerns. This is at a discount of 17% to its 5 year average multiple of 16.9x. Though valuations are compelling we are of the view that the company would outperform only once the macro related concerns are negated. We advise Investors to HOLD.

Result Highlights: Margin Pressure Clearly Visible

Realisations improve by 4% YoY on account of a richer mix

MSIL caters to Gasoline, Diesel & CNG Models. Alternate fuel like CNG has seen a 50% jump for MSIL, after the petrol deregulation. For models pertaining to Diesel there has been a growth from 60% to 80%. Diesel engines are used in SX4, Ritz and Swift Dzire. The capacity is at 2.5lakh pa, which is expected to be at 2.9lakh in the next 2-3 months. New plant for the Diesel engine would be put through Suzuki Powertrain India. Discounts given by MSIL has increased by Rs1200 on a YoY Basis, but remains lower on a QoQ basis. Going forward discounts are looking up, which would keep its realizations under pressure.

We expect a 6% CAGR in MSIL's volumes from FY11-FY13E

Capacity Expansion plan of its Manesar plant by 2.5lakh units is on schedule and is expected to see higher numbers by September. Total capacity would be expanded to 1.65mn units as against 1.4mn units. Production at Manesar has resumed to normal levels. But the overall sentiment of the Industry has been hit with the demand for small cars being hit the most. Customer profile has shifted with a higher share of 1st time buyers at 47%. Additional car buyers have declined by 300bps at 28% and replacement constitutes 25%. Rural contribution for MSIL remains at 25%, same as that seen in Q1FY11. In terms of regions, North zone has been effected the most. The East and South Regions have witnessed moderation, while the Western Region holds well. Festive Season can only prove to be the saviour at this point of time.

We expect the margins to remain under pressure from FY11-FY13E, with higher levels of localization and reduced import content being reflective from FY14E.

Margin surprises – with it flat YoY, as against our expectations of a 120bps dip

Royalty has come lower at 4.8% of sales as export volumes have dipped and the mix has changed with the proportion of royalty paying models lower. The management has indicated that there has been no one off's in this item and that going forward it would remain at its usual levels of 5%-5.5% of sales. In terms of forex, Yen contracts are fully hedged for Q1 & Q2, but kept open thereafter as the management expects a correction. We are of the view that the uncertainty in Yen would be reflective in Q3 & Q4, which would keep its margins under pressure. 15% of the net sales are indirect imports to vendors, which is likely to be reduced by 2%-3% every year on account of efforts for localization. So by FY14E , we should see imports at 9% of sales, which would be a positive trigger for the margins. The quarter witnessed appreciation of the Euro, which enabled the company to get stable realizations despite the fact that the volumes were lower. The item of other expenses was also lower as selling and distribution expenses was lower on account of reduced Ad costs and lower Ocean Freight. We expect the margins to remain under pressure from FY11-FY13E, with higher levels of localization being reflective from FY14E.

PAT Margin to trend downwards from FY11-FY13E, further expansion would be led by better volume growth & easing of forex uncertainties

Higher Other Income and lower Depreciation boost PAT margin by 80bps

- Other income in Q1 has gone up as there was a Capital Gain on its Long term Investments. This includes a Rs40cr one time benefit relating to Treasury Gains. Also, the yield on cash has gone up.

- Depreciation was lower this quarter as the change in accounting policy was taken in the previous quarter, impact of which was 1off in nature. Capex plans of FY12 is at Rs4k cr, the bulk (2/3rd) of which would be reflective as Gross Block and 1/3rd as CWIP. CWIP would be in the nature of capex relating to R&D, Manesar Expensiture and new model R&D. FY13E capex is at Rs3k cr. This would put pressure on its cash flows in FY12.

On account of the above, the PAT margin has come at 6.4% improving on a YoY basis from 5.6%. **We expect the margin to trend downwards and be stable at 5.9% for both FY12E & FY13E. Further expansion in margin would be led by better volume growth and easing of forex uncertainties.**

Q1FY12 Financials – Actuals versus Expectations

MSIL (In Rs cr)	Q1FY12A	Q1FY11	YoY% Chg	% Variance	QoQ%Chg	FY11	FY10	YoY% Chg
Vehicles Sold (No of Units)	***2,81,526***	***2,83,324***	***-0.6***	***-***	***-18.0***	***1,271,005***	***1,018,365***	***24.8***
Net Sales	8529.3	8309.2	2.6	*3.8*	-15.5	37040.1	29263.0	25.0
Total Expenditure	7714.9	7516.9	2.6	*2.5*	-15.1	33375.7	25672.1	30.0
Operating Profit	814.4	792.3	2.8	*18.1*	-19.3	3664.4	3950.9	-7.3
OPM(%)	*9.5*	*9.5*	*-*	*110bps*	*-50bps*	*9.9*	*13.3*	*-340bps*
PBT	746.2	643.0	16.1	*33.6*	-9.7	3108.8	3592.5	-13.5
PBT(%)	*8.7*	*7.7*	*100bps*	*190bps*	*50bps*	*8.4*	*12.1*	*-370bps*
Profit After Tax	549.2	465.4	18.0	*34.7*	-16.7	2288.6	2497.6	-8.4
PAT(%)	*6.4*	*5.6*	*80bps*	*140bps*	*-10bps*	*6.2*	*8.4*	*-220bps*
EPS(Rs)	19.0	16.1	18.0	*34.8*	-16.6	79.2	86.4	-8.4

Financials – Estimates

MSIL In Rs cores	FY08	FY09	FY10	FY11	FY12E	FY13E
Volume sold (units)	***7,64,842***	***7,92,167***	***1,018,365***	***1,271,005***	***1,347,265***	***1,522,409***
Net Sales	**18375.8**	**20852.5**	**29623.0**	**37040.1**	**40999.0**	**47067.0**
Total Expenditure	15642.4	19020.5	25668.7	33375.7	37165.1	42715.5
Operating Profit	2733.4	1832.1	3954.3	3664.4	3833.9	4351.5
OPM(%)	***14.9***	***8.8***	***13.3***	***9.9***	***9.4***	***9.2***
PBT	**2503.1**	**1675.9**	**3592.5**	**3108.8**	**3289.9**	**3774.5**
PBT(%)	***13.6***	***8.0***	***12.1***	***8.4***	***8.0***	***8.0***
PAT	**1730.8**	**1218.7**	**2497.6**	**2288.6**	**2401.6**	**2755.4**
PAT(%)	***9.4***	***5.8***	***8.4***	***6.2***	***5.9***	***5.9***
Equity Share Capital	144.5	144.5	144.5	144.5	144.5	144.5
EPS	59.9	42.2	86.4	79.2	83.1	95.4

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4. Way2Wealth ownership of any stock related to the information contained	: NIL
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