

# Higher capex induces PO cut to Rs 900



## Impact on free cash to restrict near-term rating

Tata Motors' latest Annual Report discloses a much higher proposed capex programme than built into our assumptions. We believe that the resultant financial impact on free cash flows will restrict valuations over the near term. As such, we are lowering our PO to Rs 900 (Rs 980) to factor in the lower cash position, as well as imputed derating of the stock to reflect increased financial risk. We however retain a positive stance on the company's key operating segments and our Buy rating.

## Proposed capex Rs 100bn

Tata Motors plans to spend Rs 100bn over the next 3-4 years towards capex and product R&D. This is much higher than earlier indications of Rs 60bn built into our assumptions. We believe that the resultant financial impact on free cash flows will reflect on valuations over the near term.

## Slight impact on earnings

Increased capital outlay impacts earnings by 1.5% in FY07E and 3.7% FY08E, due to higher interest outgo. There is however, no revision to EBITDA.

## PO lowered to factor increased financial risk

Our sum of the parts based PO, which is largely EV/EBITDA driven, has been lowered to Rs 900, to factor in the lower cash position, as well as an imputed derating of the stock to reflect increased financial risk.

## Reiterate Buy on growth prospects

We retain a bullish stance on the company's key operating segments. We reiterate Buy rating, albeit with lower 16% return expectations over the next year.

## Estimates (Mar)

(Rs)	2005A	2006A	2007E	2008E	2009
Net Income (Adjusted - mn)	13,939	16,139	22,231	27,255	NA
EPS	38.53	42.15	55.23	67.71	NA
EPS Change (YoY)	49.5%	9.4%	31.0%	22.6%	NA
Dividend / Share	12.50	13.01	14.00	16.00	NA
Free Cash Flow / Share	14.30	(73.50)	35.17	32.16	NA
ADR EPS (US\$)	0.882	0.946	1.20	1.47	NA
ADR Dividend / Share (US\$)	0.286	0.292	0.304	0.347	NA

## Valuation (Mar)

	2005A	2006A	2007E	2008E	2009
P/E	20.15x	18.42x	14.06x	11.47x	NA
Dividend Yield	1.61%	1.67%	1.80%	2.06%	NA
EV / EBITDA*	12.18x	9.95x	7.53x	6.12x	NA
Free Cash Flow Yield*	1.66%	-9.00%	4.53%	4.14%	NA

\* For full definitions of *iQmethod*<sup>SM</sup> measures, see page 4.

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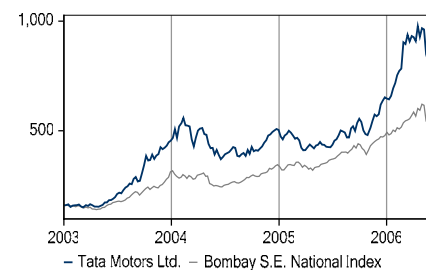
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## Stock Data

Price (Common / ADR)	Rs776.45 / US\$17.15
Price Objective	Rs900.00 / US\$19.57
Date Established	26-Jun-2006 / 26-Jun-2006
Investment Opinion	C-1-7 / C-1-7
Volatility Risk	HIGH / HIGH
52-Week Range	Rs415.10-Rs997.00
Market Value (mn)	US\$6,777
Shares Outstanding (mn)	402.5 / 402.5
Average Daily Volume	689,265
ML Symbol / Exchange	TENJF / BSE
ML Symbol / Exchange	TTM / NYS
Bloomberg / Reuters	TTMT IN / TAMO.BO
ROE (2007E)	32.1%
Net Dbt to Eqty (Mar-2006A)	31.6%
Est. 5-Yr EPS / DPS Growth	20.0% / 20.0%
Free Float	68.0%



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Refer to important disclosures on page 5 to 7. Analyst Certification on page 3. Price Objective Basis/Risk on page 3.

26 June 2006

*iQprofile*<sup>SM</sup> Tata Motors

Key Income Statement Data (Mar)	2005A	2006A	2007E	2008E	2009
<b>(Rs Millions)</b>					
Sales	195,328	237,182	301,327	352,659	NA
Gross Profit	24,966	30,539	40,360	49,693	NA
Sell General & Admin Expense	NA	NA	NA	NA	NA
Operating Profit	18,955	23,588	31,888	39,717	NA
Net Interest & Other Income	(357)	(1,668)	(1,215)	(1,797)	NA
Associates	0	0	0	0	NA
Pretax Income	18,598	21,921	30,673	37,920	NA
Tax (expense) / Benefit	(4,906)	(6,400)	(8,368)	(10,396)	NA
Net Income (Adjusted)	13,939	16,139	22,231	27,255	NA
Average Fully Diluted Shares Outstanding	362	383	403	403	NA

**Key Cash Flow Statement Data**

Net Income (Reported)	13,971	15,712	22,231	27,255	NA
Depreciation & Amortization	6,011	6,951	8,473	9,976	NA
Change in Working Capital	(4,555)	(29,349)	10,288	4,391	NA
Deferred Taxation Charge	NA	NA	NA	NA	NA
Other Adjustments, Net	(117)	1,569	0	0	NA
Cash Flow from Operations	15,440	(5,040)	41,059	41,723	NA
Capital Expenditure	(10,267)	(23,103)	(26,902)	(28,779)	NA
(Acquisition) / Disposal of Investments	2,274	8,649	(5,089)	(5,000)	NA
Other Cash Inflow / (Outflow)	NA	NA	NA	NA	NA
Cash Flow from Investing	(7,993)	(14,454)	(31,991)	(33,779)	NA
Shares Issue / (Repurchase)	50	211	196	0	NA
Cost of Dividends Paid	(5,219)	(5,844)	(6,614)	(7,558)	NA
Cash Flow from Financing	3,852	12,385	(11,528)	(4,533)	NA
Free Cash Flow	5,173	(28,143)	14,157	12,943	NA
Net Debt	6,169	19,927	16,075	14,164	NA
Change in Net Debt	(1,141)	13,758	(3,852)	(1,911)	NA

**Key Balance Sheet Data**

Property, Plant & Equipment	45,816	54,359	72,789	91,592	NA
Other Non-Current Assets	NA	NA	NA	NA	NA
Trade Receivables	12,414	13,537	20,639	25,121	NA
Cash & Equivalents	20,973	13,864	11,404	14,815	NA
Other Current Assets	28,276	59,931	64,931	69,931	NA
Total Assets	150,003	183,398	224,611	267,899	NA
Long-Term Debt	27,142	33,791	27,479	28,979	NA
Other Non-Current Liabilities	NA	NA	NA	NA	NA
Short-Term Debt	NA	NA	NA	NA	NA
Other Current Liabilities	12,453	13,754	16,254	18,754	NA
Total Liabilities	105,617	120,483	145,341	168,163	NA
Total Equity	44,602	63,054	79,342	99,708	NA
Total Equity & Liabilities	150,220	183,537	224,684	267,871	NA

**iQmethod<sup>SM</sup> - Bus Performance\***

Return On Capital Employed	20.7%	18.7%	21.5%	23.1%	NA
Return On Equity	34.6%	30.7%	32.1%	31.3%	NA
Operating Margin	9.7%	9.9%	10.6%	11.3%	NA
EBITDA Margin	12.8%	12.9%	13.4%	14.1%	NA

**iQmethod<sup>SM</sup> - Quality of Earnings\***

Cash Realization Ratio	1.1x	-0.3x	1.8x	1.5x	NA
Asset Replacement Ratio	1.9x	3.7x	3.5x	3.2x	NA
Tax Rate (Reported)	26.4%	29.2%	27.3%	27.4%	NA
Net Debt-to-Equity Ratio	13.8%	31.6%	20.3%	14.2%	NA
Interest Cover	11.2x	9.6x	12.3x	11.4x	NA

**Key Metrics**

\* For full definitions of *iQmethod*<sup>SM</sup> measures, see page 4.

**Company Description**

Tata Motors (est. 1945) is India's leading automobile maker, and is among the top 10 auto manufacturers in the world. The company has more than 130 models spanning a wide range of commercial vehicles, passenger cars and multi-utility vehicles. The company operates out of plants at Jamshedpur, Pune and Lucknow. Key export markets include Europe, Australia, South East Asia, the Middle East and Africa.

**Stock Data**

Shares / ADR	1.00
Price to Book Value	4.1x

## Price Objective Basis & Risk

We reiterate our Buy rating with a PO of Rs 900, which is based on segment-wise imputed multiples on FY08E.

- **Core business.** (1) Commercial Vehicles (CVs) at 7.5x (earlier 8x), equivalent to the high-end of its historical band, given the strong visibility of this business and (2) Passenger Vehicles (PVs) at 6.5x (earlier 7x), which is lower than imputed multiple for dominant player Maruti (at 9x), given the rising competitive intensity in this business
- **For Subsidiaries.** A mix of EV/EBITDA and P/E ratio based on inherent nature of business, and comparative peer group valuation.

**Key risks:** Higher steel and diesel prices, economic slowdown and competition

## Analyst Certification

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26 June 2006

**iQmethod<sup>SM</sup> Measures Definitions**

<b>Business Performance</b>	<b>Numerator</b>	<b>Denominator</b>
Return On Capital Employed	$\text{NOPAT} = (\text{EBIT} + \text{Interest Income}) * (1 - \text{Tax Rate}) + \text{Goodwill Amortization}$	Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill
Return On Equity	Net Income	Shareholders' Equity
Operating Margin	Operating Profit	Sales
Earnings Growth	Expected 5-Year CAGR From Latest Actual	N/A
Free Cash Flow	Cash Flow From Operations – Total Capex	N/A
<b>Quality of Earnings</b>		
Cash Realization Ratio	Cash Flow From Operations	Net Income
Asset Replacement Ratio	Capex	Depreciation
Tax Rate	Tax Charge	Pre-Tax Income
Net Debt-To-Equity Ratio	Net Debt = Total Debt, Less Cash & Equivalents	Total Equity
Interest Cover	EBIT	Interest Expense
<b>Valuation Toolkit</b>		
Price / Earnings Ratio	Current Share Price	Diluted Earnings Per Share (Basis As Specified)
Price / Book Value	Current Share Price	Shareholders' Equity / Current Basic Shares
Dividend Yield	Annualised Declared Cash Dividend	Current Share Price
Free Cash Flow Yield	Cash Flow From Operations – Total Capex	Market Cap. = Current Share Price * Current Basic Shares
Enterprise Value / Sales	$\text{EV} = \text{Current Share Price} * \text{Current Shares} + \text{Minority Equity} + \text{Net Debt} + \text{Sales} + \text{Other LT Liabilities}$	
EV / EBITDA	Enterprise Value	Basic EBIT + Depreciation + Amortization

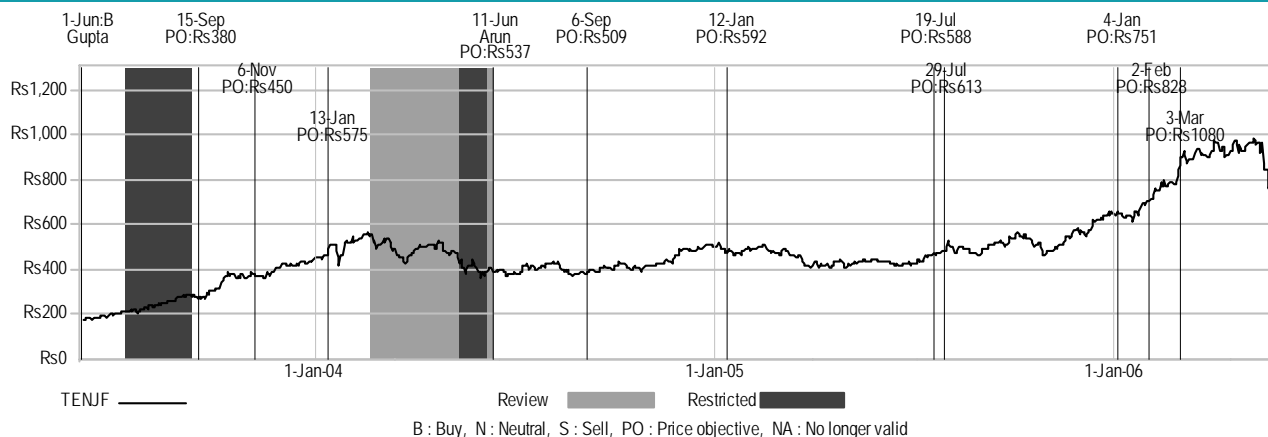
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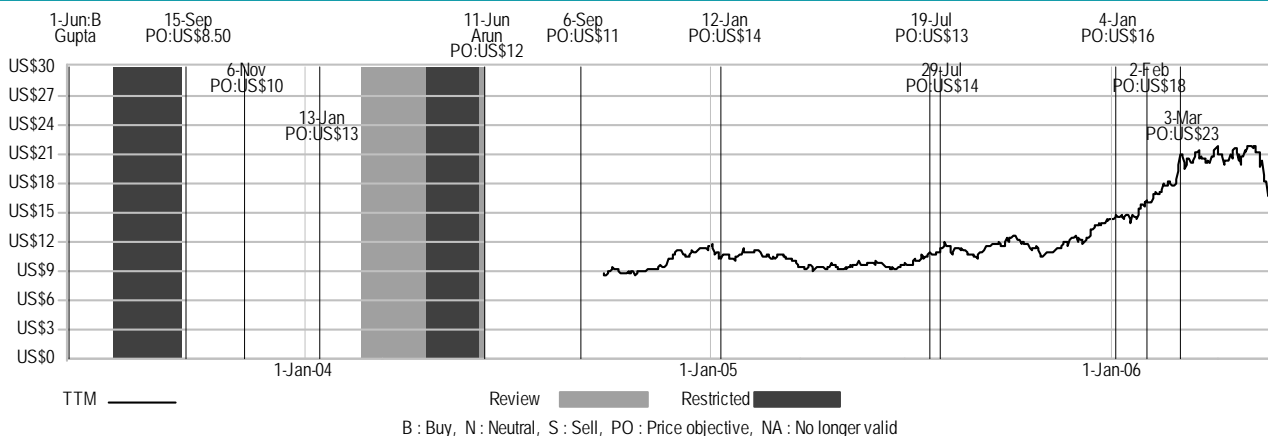
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### TTM Price Chart



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Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	31	40.26%	Buy	8	25.81%
Neutral	31	40.26%	Neutral	8	25.81%
Sell	15	19.48%	Sell	5	33.33%

### Investment Rating Distribution: Global Group (as of 31 Mar 2006)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1145	40.29%	Buy	393	34.32%
Neutral	1474	51.86%	Neutral	430	29.17%
Sell	223	7.85%	Sell	44	19.73%

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