

MAY 11, 2010

UPDATE

Coverage view: **Cautious**

Price (Rs): **2,121**

Target price (Rs): **2,170**

BSE-30: **17,331**

**Did Bajaj fire the first salvo?** Bajaj launched the Discover 150cc bike at a very aggressive price of Rs46,000 ex-showroom Delhi. The bike's power is close to the existing Discover 135, which has been struggling and may be discontinued. Discover 150cc is more than 20% cheaper than current 150cc models and comparable in price to Hero Honda's Glamour, Super Splendor. Some cannibalization from the Pulsar is possible despite its different positioning.

#### Company data and valuation summary

Bajaj Auto

##### Stock data

52-week range (Rs) (high,low)	2,167-659
Market Cap. (Rs bn)	306.9

##### Shareholding pattern (%)

Promoters	49.6
FIs	16.0
MFs	4.3

##### Price performance (%)

	1M	3M	12M
Absolute	2.6	19.6	212.0
Rel. to BSE-30	6.1	9.9	113.8

##### Forecasts/Valuations

	2010	2011E	2012E
EPS (Rs)	112.3	149.0	160.8
EPS growth (%)	148.2	32.7	7.9
P/E (X)	18.9	14.2	13.2
Sales (Rs bn)	114.4	151.2	166.3
Net profits (Rs bn)	16.2	21.6	23.3
EBITDA (Rs bn)	25.3	30.5	31.6
EV/EBITDA (X)	12.3	10.1	9.6
ROE (%)	64.6	53.0	39.0
Div. Yield (%)	0.9	0.9	0.9

#### Company data and valuation summary

Hero Honda

##### Stock data

52-week range (Rs) (high,low)	2,050-1,118
Market Cap. (Rs bn)	377.1

##### Shareholding pattern (%)

Promoters	55.0
FIs	28.7
MFs	3.2

##### Price performance (%)

	1M	3M	12M
Absolute	(4.5)	20.4	60.3
Rel. to BSE-30	(1.2)	10.6	9.8

##### Forecasts/Valuations

	2010	2011E	2012E
EPS (Rs)	111.8	121.5	135.7
EPS growth (%)	74.1	8.7	11.7
P/E (X)	16.9	15.5	13.9
Sales (Rs bn)	157.6	182.4	204.8
Net profits (Rs bn)	22.3	24.3	27.1
EBITDA (Rs bn)	26.6	29.3	31.8
EV/EBITDA (X)	12.2	11.2	9.7
ROE (%)	59.2	54.8	43.8
Div. Yield (%)	1.6	1.7	1.9

#### Bajaj launches the cheapest Indian (150cc bike)

Bajaj Auto launched its new Discover 150cc bike at an aggressive price point of Rs46,000. We think this is more of a variant of the Discover 135, given similar power, and incremental volumes might depend on the marketing muscle put behind the new product. Prior to this, most 150cc bikes started at a price point in the Rs58,000 range. At the Rs46,000 price point, the Discover 150cc would compete with Hero Honda's Glamour and Super Splendor, both of which are 125cc bikes and Bajaj's own Discover 135. Exhibit 1 shows the comparisons for the different bikes in the market. The Discover 150cc offers just 10% lower power than other 150cc bikes while offering similar features such as self-start, 5-speed gear box and front disc brakes.

#### Incremental volumes could hurt Hero Honda's share and Bajaj's margins

We see risks to sales of Hero Honda's Glamour, Super Splendor. The Discover 150 offers 40% more power than Glamour and Super Splendor, standard self-start, standard front disk brakes and a 5-speed gear box for a similar price. Hero Honda sells close to 17,000 units of the Glamour every month. Within Bajaj, we think the company would discontinue the Discover 135. Bajaj currently sells close to 10,000 units of Discover 135 and we believe it would aim at selling at least 30,000 units of Discover 150 + Discover 135. The risks to Bajaj are two-fold (1) reduced incremental margins on the Discover 150 could drag overall margins down and (2) cannibalization into Pulsar sales, would negatively impact realizations.

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### Maintaining our earnings estimates and ADD rating for Bajaj

We are maintaining our ADD rating and EPS estimates for Bajaj Auto, ahead of the company's quarterly results on May 12 and conference call on May14, where we hope to get more clarity on margins and the company's product strategy.

Additionally, our FY2011E EPS of Rs149 largely reflects the risks we discussed earlier. We have assumed a 200 bps decline in margins from FY2010E and our volume estimate is also 5% below the company's target.

#### Discover 150 would be the cheapest 150cc bike by a wide margin Feature-wise comparison of motorcycles

	Bajaj Auto				Hero Honda		
	Discover 150	Discover 135	Pulsar 135	Pulsar 150	Super Splendour	Glamour	CBZ
Price ex-showroom Delhi (Rs)	46,000	45,943	51,000	58,500	45,150	46,250	58,550
Displacement (cc)	144.8	134.2	134.7	149.0	124.7	124.7	149.2
Maximum power (bhp)	12.8	12.9	13.3	13.9	9.0	9.0	14.2
Front disk brakes	Standard	Standard	Standard	Standard	NA	Optional	Standard
Self start	Standard	Optional	Optional	Optional	Standard	Optional	Optional
Gear box	5-speed	4-speed	5-speed	5-speed	4-speed	4-speed	5-speed
Kerb weight (kgs)	121	133	122	143	121	129	143

Source: Company, Kotak Institutional Equities estimates

#### Bajaj Auto, Volume assumptions, March fiscal year ends, 2006-2012E

	2007	2008	2009	2010E	2011E	2012E
<b>Volumes (# vehicles)</b>						
<b>Motorcycles</b>	<b>2,376,519</b>	<b>2,139,633</b>	<b>1,907,810</b>	<b>2,506,845</b>	<b>3,461,388</b>	<b>3,807,526</b>
Domestic	2,078,860	1,658,084	1,276,427	1,800,876	2,614,225	2,875,647
Exports	297,659	481,549	631,383	705,969	847,163	931,879
<b>Scooters</b>	<b>20,480</b>	<b>21,294</b>	<b>11,772</b>	<b>4,851</b>	—	—
Geared	5,254	—	—	—	—	—
Ungeared	15,226	20,817	9,692	3,873	—	—
Exports	-	477	2,080	978	—	—
<b>Total 2-wheelers</b>	<b>2,396,999</b>	<b>2,160,927</b>	<b>1,919,582</b>	<b>2,511,696</b>	<b>3,461,388</b>	<b>3,807,526</b>
<b>Domestic 3-Wheelers</b>						
Passenger 3-wheelers	138,759	127,379	125,273	169,119	194,486	213,935
Goods 3-wheelers	42,374	26,607	10,197	9,177	9,636	9,636
Exports	140,663	136,315	139,056	162,640	187,036	205,740
<b>Total 3-wheelers</b>	<b>321,796</b>	<b>290,301</b>	<b>274,526</b>	<b>340,936</b>	<b>391,159</b>	<b>429,311</b>
<b>Total vehicles</b>	<b>2,718,795</b>	<b>2,451,228</b>	<b>2,194,108</b>	<b>2,852,632</b>	<b>3,852,546</b>	<b>4,236,837</b>
<b>Growth rates (yoy %)</b>						
<b>Motorcycles</b>	<b>24.2</b>	<b>(10.0)</b>	<b>(10.8)</b>	<b>31.4</b>	<b>38.1</b>	<b>10.0</b>
Domestic	18.9	(20.2)	(23.0)	41.1	45.2	10.0
Exports	80.1	61.8	31.1	11.8	20.0	10.0
<b>Scooters</b>	<b>(82.3)</b>	<b>4.0</b>	<b>(44.7)</b>	<b>(58.8)</b>	—	—
Geared	(91.6)	(100.0)	—	—	—	—
Ungeared	(71.1)	36.7	(53.4)	(60.0)	—	—
Exports	—	—	336.1	(53.0)	—	—
<b>Total 2-wheelers</b>	<b>18.2</b>	<b>(9.8)</b>	<b>(11.2)</b>	<b>30.8</b>	<b>37.8</b>	<b>10.0</b>
<b>Domestic 3-Wheelers</b>						
Passenger 3-wheelers	2.5	(15.0)	(12.0)	31.6	14.5	9.5
Goods 3-wheelers	(1.8)	(8.2)	(1.7)	35.0	15.0	10.0
Exports	19.7	(37.2)	(61.7)	(10.0)	5.0	-
Exports	86.9	(3.1)	2.0	20.0	15.0	10.0
<b>Total 3-wheelers</b>	<b>27.7</b>	<b>(9.8)</b>	<b>(5.4)</b>	<b>24.2</b>	<b>14.7</b>	<b>9.8</b>
<b>TOTAL Vehicles</b>	<b>19.2</b>	<b>(9.8)</b>	<b>(10.5)</b>	<b>30.0</b>	<b>35.1</b>	<b>10.0</b>

Source: Company, Kotak Institutional Equities estimates

## Bajaj Auto, Profit model and Balance Sheet, March fiscal year-ends, 2008-2012E (Rs mn)

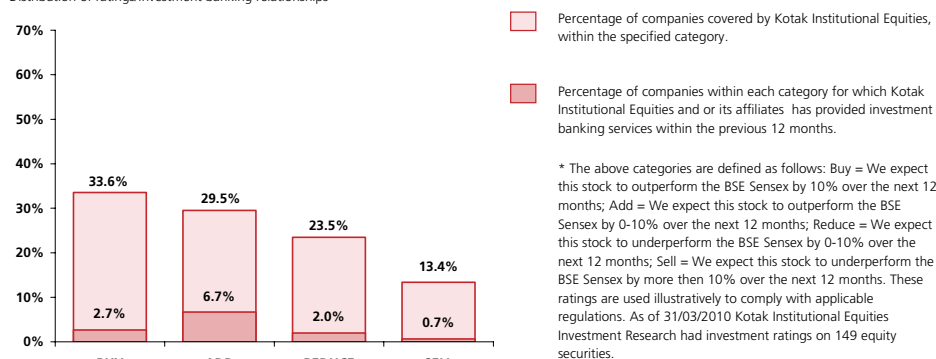
	2008	2009E	2010E	2011E	2012E
<b>Profit model (Rs mn)</b>					
Net sales	86,633	84,369	114,370	151,234	166,290
<b>Operating profit</b>	<b>12,900</b>	<b>12,097</b>	<b>25,346</b>	<b>30,456</b>	<b>31,636</b>
Other income	1,262	1,043	1,275	2,329	3,720
Interest	(52)	(210)	(60)	(60)	(60)
Depreciation	(1,740)	(1,298)	(1,406)	(1,488)	(1,580)
<b>Profit before tax</b>	<b>12,371</b>	<b>11,632</b>	<b>25,155</b>	<b>31,237</b>	<b>33,715</b>
Extra-ordinary items	(1,025)	(2,071)	(1,615)	-	-
Taxes	(3,788)	(3,016)	(7,298)	(9,683)	(10,452)
<b>Net profit</b>	<b>7,558</b>	<b>6,545</b>	<b>16,243</b>	<b>21,553</b>	<b>23,263</b>
<b>Earnings per share (Rs)</b>	<b>54.2</b>	<b>45.2</b>	<b>112.3</b>	<b>149.0</b>	<b>160.8</b>
<b>Balance sheet (Rs mn)</b>					
Equity	15,876	18,697	31,554	49,722	69,600
Deferred tax liability	110	42	-	-	-
Total borrowings	13,343	15,700	14,379	13,189	12,119
Current liabilities	18,773	24,376	28,039	33,293	35,396
<b>Total liabilities</b>	<b>48,102</b>	<b>58,814</b>	<b>73,972</b>	<b>96,204</b>	<b>117,115</b>
Net fixed assets	12,928	15,481	15,825	16,587	17,257
Investments	18,571	18,085	25,560	41,533	56,504
Cash	561	1,369	10,030	12,245	15,907
Other current assets	15,936	21,884	22,142	25,031	26,215
Miscellaneous expenditure	105	1,996	163	163	163
Deferred tax assets	-	-	254	646	1,069
<b>Total assets</b>	<b>48,102</b>	<b>58,814</b>	<b>73,972</b>	<b>96,204</b>	<b>117,115</b>
<b>Ratios</b>					
Operating margin (%)	14.3	13.7	21.4	19.5	18.4
PAT margin (%)	8.4	7.4	31.0	13.8	13.6
Debt/equity (X)	0.8	0.8	0.5	0.3	0.2
Net debt/equity (X)	0.0	0.2	(0.4)	(0.7)	(0.8)
Book Value (Rs/share)	114.6	129.5	218.1	343.6	481.0
RoAE (%)	21.0	37.7	64.6	53.0	39.0
<b>RoACE (%)</b>	<b>72.5</b>	<b>44.1</b>	<b>83.9</b>	<b>95.7</b>	<b>89.0</b>

Source: Company, Kotak Institutional Equities estimates

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Source: Kotak Institutional Equities

As of March 31, 2010

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