



Bajaj Auto

STOCK INFO. BLOOMBERG
BSE Sensex: 16,276 BJAUT IN
REUTERS CODE
S&P CNX: 4,860 BJAT.BO

27 May 2008

Buy

Rs596

Previous Recommendation: Buy

| | |
|---------------------|---------|
| Equity Shares (m) | 144.7 |
| 52-Week Range (Rs) | 945/556 |
| 1,6,12 Rel.Perf.(%) | NA |
| M.Cap. (Rs b) | 86.2 |
| M.Cap. (US\$ b) | 2.0 |

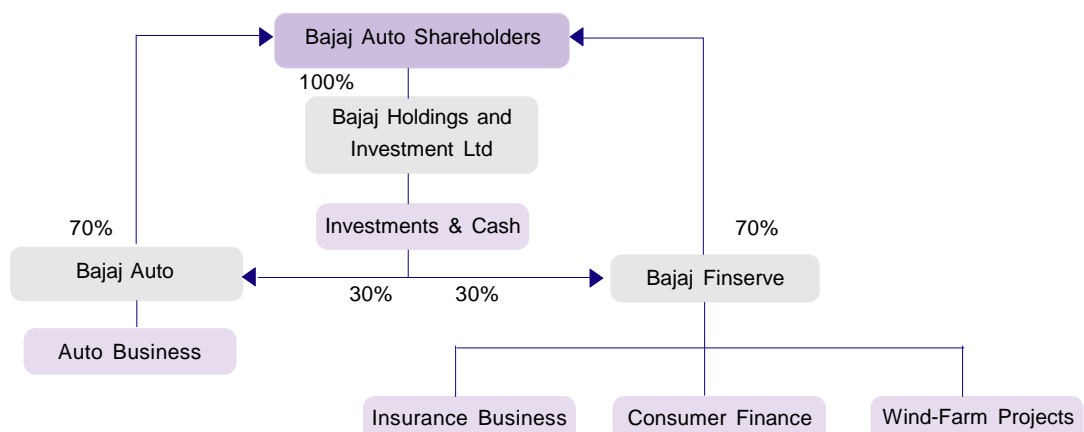
| YEAR | NET SALES | PAT | EPS | EPS | P/E | P/BV | ROE | ROCE | EV/ | EV/ |
|-------|-----------|--------|------|------------|------|------|------|------|-------|--------|
| END | (RS M) | (RS M) | (RS) | GROWTH (%) | (X) | (X) | (%) | (%) | SALES | EBITDA |
| 3/08A | 90,462 | 8,352 | 57.7 | | 10.3 | 5.4 | 47.6 | 41.0 | 0.9 | 6.2 |
| 3/09E | 103,456 | 9,929 | 68.6 | 18.9 | 8.7 | 3.8 | 44.0 | 37.5 | 0.7 | 5.0 |
| 3/10E | 115,963 | 11,549 | 79.8 | 16.3 | 7.5 | 2.8 | 37.9 | 35.5 | 0.5 | 3.7 |

Expect 6% volume growth in FY09: In FY09, we expect Bajaj Auto (BAL) to register volume growth of 6% in motorcycles, 20% in scooters, and 5% in three-wheelers. We estimate 14.4% growth in FY09 total income driven by: (1) continued improvement in product mix towards the executive and premium models, boosted by new launches in these segments, (2) higher production at Uttaranchal plant - up from 275,000 units in FY08 to 500,000 units in FY09 - where BAL has excise duty and income tax benefits (BAL will also manufacture the more profitable XCD at this plant in FY09 in addition to the *Platina*), and (3) improved realizations due to the recent 1-2% increase in prices to combat higher input costs.

19% growth in PAT: We expect BAL to register an EBITDA margin of 14% in FY09 (14.5% in FY08). Although higher input costs would pose a threat to margin, we expect BAL to balance the impact through price increases, higher production at the Uttaranchal plant, productivity improvement, and cost reduction. We expect PAT to grow 18.9% to Rs9.9b in FY09 on the back of a 14.4% growth in revenue.

Reinitiate coverage with Buy: Though the domestic volume growth for the two-wheeler industry looks challenging, we believe export volume growth, revival in three-wheeler volume growth, new product launches, and excise and tax benefits would lead to a 19% growth in PAT for BAL in FY09. The stock trades at 8.7x FY09E EPS of Rs68.6 and 7.5x FY10E EPS of Rs79.8. We reinitiate coverage with a **Buy** and a target price of Rs992 (14x FY09E earnings and Rs31/share investment in KTM Power Sports AG).

STRUCTURE AFTER DEMERGER



Outlook for FY09

In FY09, we expect Bajaj Auto to register volume growth of 6% in motorcycles, 20% in scooters, and 5% in three-wheelers. We estimate 14.4% growth in FY09 total income driven by: (1) continued improvement in product mix towards the executive and premium models, boosted by new launches in these segments, (2) higher production at Uttaranchal plant - up from 275,000 units in FY08 to 500,000 units in FY09 - where BAL has excise duty and income tax benefits (BAL will also manufacture the more profitable XCD at this plant in FY09 in addition to the *Platina*), and (3) improved realizations due to the recent 1-2% increase in prices to combat higher input costs.

The company manufactured 275,000 (*Platina*) units in FY08. In FY09, this would be nearly doubled to 500,000 units with the more profitable XCD also being manufactured. Our current realization assumption does not factor in any price reduction in the model post shifting of production to Uttaranchal.

While the management has guided for flat volumes in FY09, we believe Bajaj Auto will be able to register higher volume growth of 6% in FY09. This will be on the back of higher three-wheeler sales following the launch of two new three-wheeler models (one each in the passenger and the goods segments), further ramp-up of exports, and improvement in the two-wheeler industry volume 2HFY09 onwards due to low base of the previous year and possibly of the pent up demand getting released.

We expect BAL to register an EBITDA margin of 14% in FY09 (14.5% in FY08). Although higher input costs would pose a threat to profitability, we expect BAL to balance the impact through price increases, higher production at the Uttaranchal plant, productivity improvement, and cost reduction. We expect PAT to grow 18.9% to Rs9.9b in FY09 on the back of a 14.4% growth in revenue.

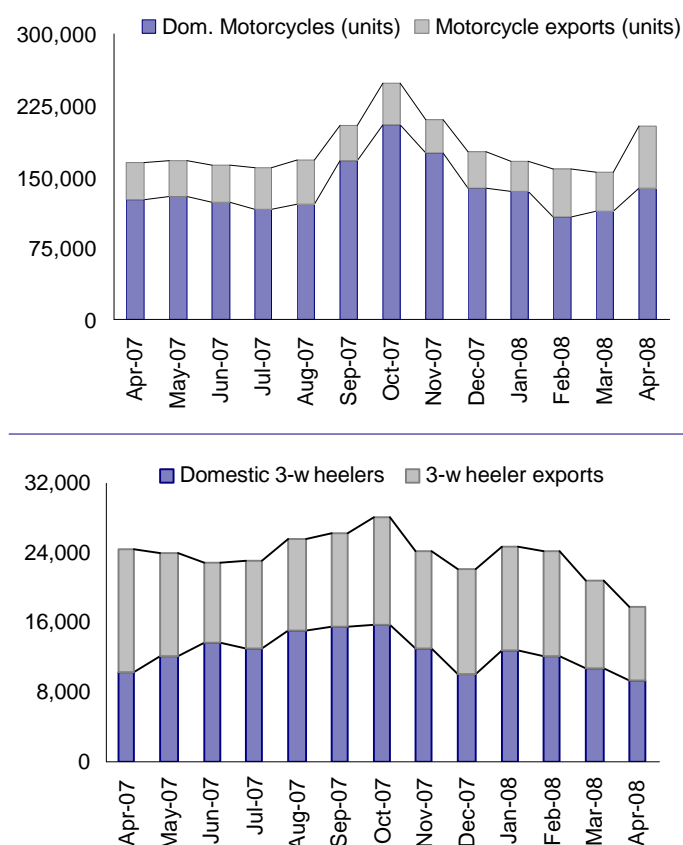
| BAJAJ AUTO SENSITIVITY OF EARNINGS TO VOLUME GROWTH IN FY09 | | | |
|---|------|------|------|
| Overall Volume Growth (%) | 0 | 3 | 6 |
| EPS (Rs) | 65.1 | 66.9 | 68.6 |
| P/E (x) | 14.0 | 14.0 | 14.0 |
| Invest.in KTM Power/ Share Value (after 20% dis.) | 31.0 | 31.0 | 31.0 |
| Target Price (Rs) | 942 | 968 | 991 |

Source: Motilal Oswal Securities

Exports to remain strong growth driver

Bajaj Auto has been registering robust growth in exports - volumes have increased at a 46% CAGR over FY05-08. We expect this growth to continue, driven by Bajaj Auto's reach into various African, South Asian, and Latin American markets. Scaling up of operations in Indonesia will provide further access into the South East Asian markets, which will also drive growth in exports. We expect Bajaj Auto's exports to increase at 22.5% CAGR over FY08-10 to 922,959 units.

TREND IN EXPORTS



Source: SIAM/Company

Bajaj Auto's 4QFY08 performance

Volume decline continues

Volumes declined 12.1% in 4QFY08 (two-wheeler and three-wheeler sales declined 11.2% YoY and 17.7% YoY respectively). However, realization in 4QFY08 increased 2.2% over 9MFY08 due to relatively higher proportion of three-wheeler sales (12.6% as against 11.7% in 9MFY08) during the quarter.

For the full year FY08, BAL's volumes declined 9.9% YoY - 10% decline in two-wheelers and 9.8% decline in three-wheelers. The decline in motorcycles was also 10%. However, there was a shift in the product mix of the company in FY08, as the share of 100cc motorcycles declined from 60.4% in FY07 to 46.1% in FY08. The beneficiary was the 125cc segment, which formed 32.1% of BAL's sales as compared to 19% in FY07.

BAL MOTORCYCLE PRODUCT MIX TREND (%)

| | 4QFY07 | FY07 | 4QFY08 | FY08 |
|--------------|--------------|--------------|--------------|--------------|
| 100cc | 54.1 | 60.4 | 46.7 | 46.1 |
| 125cc | 19.6 | 19.0 | 31.7 | 32.1 |
| 150cc | 26.4 | 20.6 | 21.6 | 21.8 |
| Total | 100.0 | 100.0 | 100.0 | 100.0 |

BAL OVERALL PRODUCT MIX TREND (%)

| | 4QFY07 | FY07 | 4QFY08 | FY08 |
|---------------------------|--------------|--------------|--------------|--------------|
| Motorcycles | 85.3 | 87.4 | 6.9 | 87.3 |
| Other Two-wheelers | 1.3 | 0.8 | 0.5 | 0.9 |
| Total Two-wheelers | 86.5 | 88.2 | 87.4 | 88.2 |
| Three-wheelers | 13.5 | 11.8 | 12.6 | 11.8 |
| Total Sales | 100.0 | 100.0 | 100.0 | 100.0 |

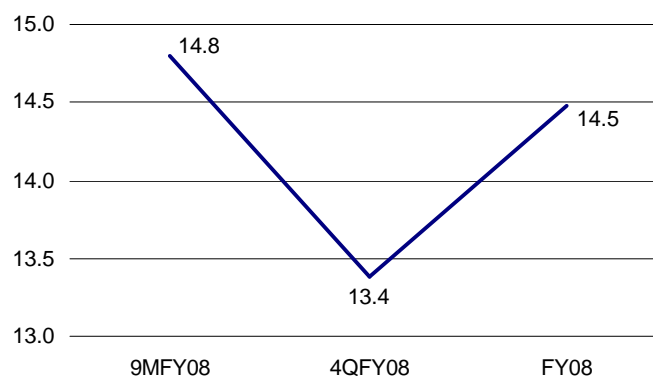
Source: Company/Motilal Oswal Securities

Operating performance below expectations

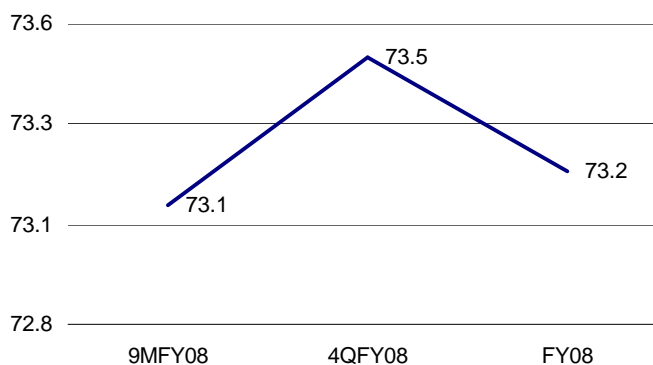
Bajaj Auto reported lower than expected operating performance in 4QFY08, with EBITDA margin of 12.6% as against expectation of 14.7%. The decline was led by a combination of factors: (1) impact of 80bp in EBITDA margin is due to provisioning of mark to market losses of Rs160m on forward cover on dollar exports. Adjusting for this MTM loss, 4QFY08 EBITDA margin for BAL would be 13.4%, (2) fixed costs apportioned over lower sales volume, which declined 12.1% in 4Q, and (3) adverse product mix change, with higher proportion of entry level bikes being sold as compared to the more profitable premium bikes, and decline in volumes of XCD.

The company has provided for VRS provisioning of Rs512m during 4Q. Adjusted PAT is Rs1.7b against reported PAT of Rs1.2b.

EBITDA MARGIN DECLINES IN 4QFY08 (%)



RM COST SLIGHTLY HIGHER (%)



Source: Company

BAJAJ AUTO: STANDALONE PERFORMANCE (RS M)

| | FY08 | | FY08 |
|------------------------|---------------|---------------|---------------|
| | 9M | 4Q | |
| Total Volumes (nos) | 1,898,649 | 552,579 | 2,451,228 |
| Change (%) | -9.3 | -12.1 | -9.9 |
| Total Income | 69,717 | 20,744 | 90,462 |
| Total Cost | 59,398 | 17,969 | 77,366 |
| EBITDA | 10,320 | 2,776 | 13,095 |
| As % of Sales | 14.8 | 13.4 | 14.5 |
| Other Income | 1,022 | 205 | 1,227 |
| Extraordinary Expenses | 515 | 671 | 1,185 |
| Interest | 34 | 18 | 52 |
| Depreciation | 1,326 | 414 | 1,740 |
| PBT | 9,468 | 1,878 | 11,346 |
| Tax | 3,118 | 670 | 3,788 |
| Effective Tax Rate (%) | 32.9 | 35.7 | 33.4 |
| Rep. PAT | 6,350 | 1,208 | 7,558 |
| Adj. PAT | 6,695 | 1,657 | 8,352 |
| EPS (Rs) | 46.3 | 11.5 | 57.7 |
| Core PAT | 5,877 | 1,494 | 7,370 |
| Core EPS (Rs) | 40.6 | 10.3 | 50.9 |

Source: Motilal Oswal Securities

Consolidated performance

Bajaj Auto's consolidated numbers include stake in two overseas subsidiaries:

1. PT. Bajaj Auto Indonesia - BAL has 97.5% shareholding. The company assembles and markets Pulsars in Indonesia. It has a niche presence in the Indonesian market, and has an exclusive dealer network put in place, which gives the company reach into important markets like Jakarta, Java, Sumatra, Bali, and Sulawesi. During FY08, BAL introduced Pulsar variants in the market. FY09 is likely to see introduction of the XCD.
2. Bajaj Auto International Holdings BV - 100% subsidiary. BAL has acquired 24.45% stake in KTM Power Sports AG through this subsidiary. The total cost of investment in this company was Rs5.7b. KTM is the second largest European motorcycle maker, and a worldwide leading manufacturer of power sports vehicles. KTM bikes are likely to be introduced in India shortly through BAL's ProBiking showrooms. The bikes are likely to be marketed as off-the-road kind of two-wheelers.

BAJAJ AUTO: CONSOLIDATED PERFORMANCE (RS M)

| | FY08 | | FY08 |
|------------------------|---------------|---------------|---------------|
| | 9M | 4Q | |
| Total Income | 69,807 | 20,606 | 90,413 |
| Total Cost | 59,801 | 17,914 | 77,715 |
| EBITDA | 10,006 | 2,692 | 12,698 |
| As % of Sales | 14.3 | 13.1 | 14.0 |
| Other Income | 1,022 | 205 | 1,227 |
| Extraordinary Expenses | 515 | 671 | 1,185 |
| Interest | 34 | 18 | 52 |
| Depreciation | 1,329 | 417 | 1,746 |
| PBT | 9,151 | 1,791 | 10,942 |
| SOP from associates | 0 | 231 | 231 |
| Minority Interest | -5 | -1 | -7 |
| PBT after SOP | 9,156 | 2,024 | 11,180 |
| Tax | 3,038 | 647 | 3,684 |
| Effective Tax Rate (%) | 33.2 | 36.1 | 33.7 |
| Rep. PAT | 6,119 | 1,377 | 7,496 |
| Adj. PAT | 6,463 | 1,826 | 8,290 |
| EPS (Rs) | 44.7 | 12.6 | 57.3 |

E: MOST Estimates

Other highlights

- ✍ Though the Nissan JV has been announced, further details will be disclosed only in 2QFY09.
- ✍ BAL has no plans to exit the 100cc segment. However, it does not plan to make any investments in new products in this segment as well.
- ✍ Three-wheeler exports were lower on account of temporary stoppage of despatches to Egypt. The company expects volumes to pick up following the launch of two new three-wheelers.
- ✍ BAL plans to introduce new bikes from the KTM and Kawasaki stables in FY09. These launches are expected in 3-4 months through Bajaj Auto's ProBiking showrooms.
- ✍ VRS plans at the Akurdi plant are likely to be firmed up within six weeks.
- ✍ Operations in Indonesia are progressing steadily, where BAL sells the Pulsar 180 and Pulsar 220. Average monthly sales are 200 units through 20 dealer outlets. The 125cc XCD will be shortly introduced in the country to strengthen BAL's product portfolio. However, the company intends to continue being a niche player in that market (majority of the market is step-through).

BAJAJ AUTO: SOTP VALUATION

| RSSHARE | FY08 | FY09E | FY10E |
|---|------------|------------|--------------|
| Adjusted EPS | 57.7 | 68.6 | 79.8 |
| P/E (x) | 14.0 | 14.0 | 14.0 |
| Target Price | 808 | 961 | 1,118 |
| Investment in KTM Power Sports AG at cost (Rs m) | 5,680 | 5,680 | 5,680 |
| Per Share Value | 39 | 39 | 39 |
| Value of Investments Per Share (after 20% discount) | 31 | 31 | 31 |
| Target Price | 840 | 992 | 1,149 |

COMPARATIVE VALUATIONS

| SOTP VALUATION RSSHARE | BAJAJ AUTO | | HERO HONDA | | TVS MOTOR | |
|---|------------|--------------|------------|------------|-----------|-----------|
| | FY09E | FY10E | FY09E | FY10E | FY09E | FY10E |
| Adj. EPS | 68.6 | 79.8 | 56.4 | 62.6 | 2.2 | 2.6 |
| P/E (x) | 14.0 | 14.0 | 15.0 | 15.0 | 15.0 | 15.0 |
| Target Price | 961 | 1,118 | 846 | 939 | 33 | 39 |
| Investment in KTM Power Sports AG at cost (Rs M) | 5,680 | 5,680 | 0 | 0 | 0 | 0 |
| Per share value | 39 | 39 | 0 | 0 | 0 | 0 |
| Value of Investments per share (after 20% discount) | 31 | 31 | 0 | 0 | 0 | 0 |
| Target Price | 992 | 1,149 | 846 | 939 | 33 | 39 |

Source: Motilal Oswal Securities

Reinitiate coverage with Buy

Though the domestic volume growth for the two-wheeler industry looks challenging, we believe export volume growth, revival in three-wheeler volume growth, new product launches, and excise and tax benefits would lead to a 19%

growth in PAT for BAL in FY09. The stock trades at 8.7x FY09E EPS of Rs68.6 and 7.5x FY10E EPS of Rs79.8. We reinitiate coverage with a **Buy** and a target price of Rs992 (14x FY09E earnings and Rs31/share investment in KTM Power Sports AG).

Bajaj Holdings and Investment FY08 performance

In FY08, on a standalone basis, BHIL had a total income of Rs3.6b, PAT of Rs3.1b and EPS of Rs30.3. On a consolidated basis, BHIL's total income was Rs3.6b, PAT was Rs5.3b (due to Rs2.2b SOP of associates), and EPS was Rs52. The company has announced a DPS of Rs20, a dividend yield of 3%.

BHIL: STANDALONE PERFORMANCE (RS M)

| | FY08 | | FY08 |
|------------------------|--------------|------------|--------------|
| | 9M | 4Q | |
| Total Income | 2,934 | 620 | 3,553 |
| Total Cost | 50 | 7 | 58 |
| EBITDA | 2,884 | 612 | 3,496 |
| As % of Sales | 98.3 | 98.8 | 98.4 |
| Depreciation | 2 | 1 | 2 |
| PBT | 2,882 | 612 | 3,494 |
| Tax | 298 | 126 | 423 |
| Effective Tax Rate (%) | 10.3 | 20.6 | 12.1 |
| PAT | 2,585 | 486 | 3,070 |
| EPS (Rs) | 25.5 | 4.8 | 30.3 |

BHIL: VALUE OF INVESTMENTS (RS M)

| | NO. OF SH. (M) | COST (RS M) | MV (RS M) |
|------------------------------------|----------------|---------------|----------------|
| ICICI Bank | 38.0 | 13,890 | 33,421 |
| MSL | 2.7 | 2 | 774 |
| Bajaj Auto | 43.5 | 435 | 37,628 |
| Bajaj Finserv | 43.5 | 218 | 25,665 |
| Other Equities & Fixed Income | | 17,789 | 17,789 |
| Total | | 32,334 | 115,276 |
| Total excluding BAL and BFL | | 31,681 | 51,983 |

BHIL: CONSOLIDATED PERFORMANCE (RS M)

| | FY08 | | FY08 |
|------------------------|--------------|------------|--------------|
| | 9M | 4Q | |
| Total Income | 3,004 | 626 | 3,630 |
| Total Cost | 80 | 17 | 97 |
| EBITDA | 2,923 | 609 | 3,533 |
| As % of Sales | 97.3 | 97.3 | 97.3 |
| Depreciation | 4 | 1 | 5 |
| PBT | 2,920 | 608 | 3,528 |
| SOP from associates | 1,843 | 313 | 2,155 |
| PBT after SOP | 4,762 | 921 | 5,683 |
| Tax | 299 | 127 | 426 |
| Effective Tax Rate (%) | 10.2 | 20.9 | 12.1 |
| Adj. PAT | 4,464 | 794 | 5,257 |
| Extraordinary Expenses | - | 1 | 1 |
| PAT | 4,464 | 793 | 5,257 |
| EPS (Rs) | 44.1 | 7.8 | 52.0 |

Source: Company/Motilal Oswal Securities

BAJAJ HOLDINGS AND INVESTMENT SOTP (RS M)

| | FY08 |
|------------------------------------|----------------|
| Market Value of Cash & Investments | 51,983 |
| 30% stake in BAL | 25,869* |
| 30% stake in BFL | 24,523* |
| Total Value | 102,375 |
| Value of Investments / Share (Rs) | 1,012 |
| CMP as of 27/05/2008 (Rs) | 596 |
| Discount to Intrinsic Value (%) | -43.7 |

*30% stake in BAL and BJFIN is calculated on CMP of Rs596 and Rs565 respectively

Source: Motilal Oswal Securities

| INCOME STATEMENT | | | | RATIOS | | | |
|-----------------------------|---------------------|----------------|----------------|---------------------------------|-------------|-------------|-------------|
| (Rs Million) | | | | | | | |
| Y/E MARCH | 2008 | 2009E | 2010E | Y/E MARCH | 2008 | 2009E | 2010E |
| Total Income | 90,462 | 103,456 | 115,963 | Basic (Rs) | | | |
| Change (%) | | 14.4 | 12.1 | EPS | 57.7 | 68.6 | 79.8 |
| Total Expenditure | 77,367 | 88,949 | 99,498 | EPS growth (%) | | 18.9 | 16.3 |
| EBITDA | 13,095 | 14,507 | 16,465 | Cash EPS | 64.3 | 812 | 92.7 |
| Change (%) | | 10.8 | 13.5 | Book Value per Share | 109.7 | 155.9 | 210.7 |
| % of Net Sales | 14.5 | 14.0 | 14.2 | DPS | 20.0 | 22.5 | 25.0 |
| Depreciation | 1,740 | 1,821 | 1,858 | Valuation (x) | | | |
| Interest & Finance Charges | 52 | 52 | 52 | P/E | 10.3 | 8.7 | 7.5 |
| Other Income | 1,227 | 1,350 | 1,485 | Cash P/E | 9.3 | 7.3 | 6.4 |
| Non-recurring Expense | 1,185 | 0 | 0 | EV/EBITDA | 6.2 | 5.0 | 3.7 |
| PBT | 11,346 | 13,984 | 16,040 | EV/Sales | 0.9 | 0.7 | 0.5 |
| Tax | 3,788 | 4,055 | 4,491 | Price to Book Value | 5.4 | 3.8 | 2.8 |
| Effective Rate (%) | 33.4 | 29.0 | 28.0 | Dividend Yield (%) | 3.4 | 3.8 | 4.2 |
| PAT | 7,558 | 9,929 | 11,549 | Profitability Ratios (%) | | | |
| Adj. PAT | 8,352 | 9,929 | 11,549 | RoE | 47.6 | 44.0 | 37.9 |
| Change (%) | | 18.9 | 16.3 | RoCE | 41.0 | 37.5 | 35.5 |
| BALANCE SHEET | (Rs Million) | | | Leverage Ratio | | | |
| Y/E MARCH | 2008E | 2009E | 2010E | Debt/Equity (x) | 0.9 | 0.6 | 0.5 |
| Share Capital | 1,447 | 1,447 | 1,447 | | | | |
| Reserves | 14,429 | 21,102 | 29,034 | | | | |
| Net Worth | 15,876 | 22,549 | 30,481 | | | | |
| Deferred Tax | 317 | 317 | 317 | | | | |
| Loans | 14,513 | 14,513 | 14,513 | | | | |
| Capital Employed | 30,706 | 37,379 | 45,311 | | | | |
| Application of Funds | | | | | | | |
| Net Fixed Assets | 12,023 | 12,523 | 13,023 | | | | |
| Technical Know how | 93 | 93 | 93 | | | | |
| Investments | 18,200 | 19,565 | 21,032 | | | | |
| Net Current Assets | 379 | 5,187 | 11,152 | | | | |
| Miscellaneous Expenditures | 11 | 11 | 11 | | | | |
| Application of Funds | 30,706 | 37,379 | 45,311 | | | | |

E: M OSt Estimates



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Disclosure of Interest Statement

Bajaj Auto

- | | |
|---|----|
| 1. Analyst ownership of the stock | No |
| 2. Group/Directors ownership of the stock | No |
| 3. Broking relationship with company covered | No |
| 4. Investment Banking relationship with company covered | No |

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