



## Mahindra & Mahindra

<i>STOCK INFO.</i>	<i>BLOOMBERG</i>
BSE Sensex: 18,167	MM IN
	<i>REUTERS CODE</i>
S&P CNX: 5,452	MAHM.BO

13 August 2010

Buy

Previous Recommendation: Buy

Rs628

Diluted Eq. Shares (m)	573.5
52-Week Range (Rs)	670/367
1,6,12 Rel.Perf.(%)	-2/17/41
M.Cap. (Rs b)	355.2
M.Cap. (US\$ b)	7.7

YEAR	N. SALES	S/A PAT	CON PAT	ADJ.EPS	CONS.	P/E	CONS.	ROE	ROCE	EVI	EVI
END	(RS M)	(RS M)	(RS)	(RS)	EPS (RS)	(X)	P/E (X)	(%)	(%)	SALES	EBITDA
3/09A	130,937	9,297	15,047	16.2	26.2	38.7	23.9	17.7	12.9	2.4	28.3
3/10A	186,021	20,451	24,402	35.7	42.6	17.6	14.8	26.1	25.8	1.7	10.2
3/11E	225,577	24,287	33,212	42.3	57.9	14.8	10.8	23.1	23.7	1.3	8.9
3/12E	262,678	27,978	24,402	48.8	68.3	12.9	9.2	22.0	23.9	1.1	7.1

### Preferred bidder for Ssangyong Motors (SYMC); purchase consideration to determine value creation

#### SYMC offers complementary portfolio and access to technology...

Ssangyong Motors (SYMC) has six models under five brands, including a luxury sedan, four SUVs and one MPV. Its portfolio complements M&M's, which has entry and mid-level products. The possible acquisition of SYMC will add a premium SUV and a luxury car to M&M's portfolio. It will give M&M access to a good SUV product portfolio and marketing network of over 1,400 dealers (of which 138 are in South Korea) in South Korea, Europe, Russia and other Asian countries. The combined entity will, thus, have a larger market and expanded product basket.

#### ...with synergies in operations, coupled with technical strength

M&M will leverage its India advantage of low-cost component sourcing as well as economies of scale for global sourcing. SYMC's ~600 R&D staff and modern R&D infrastructure will significantly enhance M&M's R&D efforts. Joint R&D program will enable optimization of investments in product development. This coupled with product lifecycle experience accumulated by SYMC over 40 years will supplement M&M's product lifecycle management.

#### Focused management, financial stability will help normalize SYMC's operations

Change in ownership (twice till 2004), coupled with financial instability resulted in underinvestment/lack of investment in SYMC's product development and business. This in turn resulted in volumes declining at a compounded rate of ~29% since CY05. With M&M acquiring SYMC, we expect reduction in debt and interest burden. Focus will return to business and product development.

#### Cost rationalization, pick-up in volumes to aid cash breakeven for SYMC

With pick-up in volumes, reduction in staff cost and other cost cutting initiatives, SYMC turned EBITDA positive in 1QCY10, with volumes of ~16,000 units and EBITDA margin of 2.5%. With expected launch of 'C-200', volumes are expected to pick up further. With fund infusion by M&M to retire long-term debt, we estimate significant reduction in its interest burden (~US\$10m in 1QCY10), thereby enabling cash breakeven. Further, cost-cutting initiatives coupled with operational synergies with M&M would enable turnaround of SYMC at PAT level.

#### Deal appears favorable for M&M; reiterate Buy

The deal looks favorable for M&M; it will get access to new products, distribution network, technology and potential to generate value due to operational synergies. However, the extent of value creation will depend on the price paid. We remain positive on M&M's prospects, given its market dominance in core business of UVs and Tractors, coupled with cheap valuations. The stock trades at 10.8x FY11E consolidated EPS of Rs57.9 and 9.2x FY12E consolidated EPS of Rs68.3. We maintain **Buy**, with an SOTP-based (FY11E) target price of Rs760.

**SYMC - a good fit at the right price**

M&M has been selected as the preferred bidder for South Korean SUV and car maker, Ssangyong Motors (SYMC) on the basis of: (1) financial bid submitted, (2) long-term strategy, (3) strong management, and (4) guarantee of employment, with no further downsizing (~37% downsizing done in CY09).

*Though the price that M&M will have to pay to acquire SYMC is not finalized, the deal appears favorable*

SYMC indicated that it plans to sign a preliminary agreement with M&M by end-August and aims to sign a contract for the sale in November 2010. The deal appears favorable for M&M, as it will get access to new products, distribution network, technology and potential to generate value due to operational synergies.

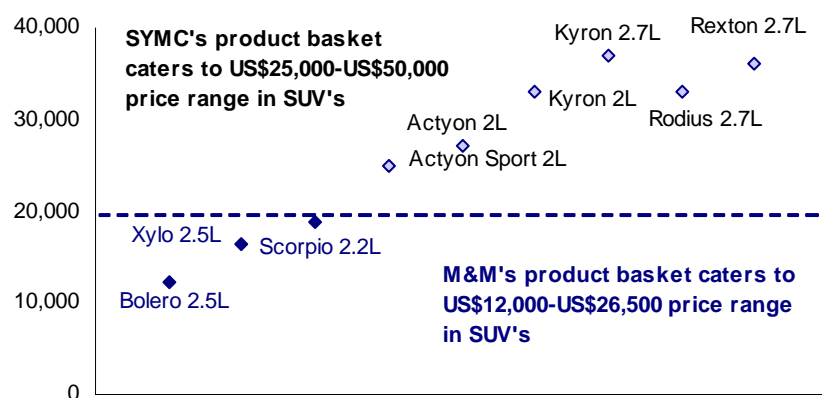
M&M will bid for a majority stake (>51% stake). The consideration paid by M&M will be used to pay-off existing long-term debt (net debt of US\$639m as at December 2009), making SYMC free of long-term debt. However, M&M will assume working capital liabilities. According to media reports, M&M may have to pay US\$400m-500m. M&M has a strong balance sheet with net cash of ~US\$340m (March 2011).

**SYMC offers complementary portfolio and access to technology...**

*SYMC's product portfolio complements M&M's; M&M will get a premium SUV and a luxury car*

SYMC has six models under five brands, including a luxury sedan, four SUVs and one MPV. It is a significant player in the SUV segment in Korea, having recorded SUV volumes of 1.3m over 1990-2009. Its portfolio complements M&M's, which has entry and mid-level products (up to Rs1m price range). The possible acquisition of SYMC will add a premium SUV (above Rs1m) and a luxury car to M&M's portfolio. M&M will be able to leverage SYMC's product portfolio to enhance its dominance in the Indian UV market, as well as enter other global markets through SYMC's product portfolio and distribution network (~1,300 dealers outside Korea). The combined entity will, thus, have a larger market and expanded product basket.

**SYMC: PRODUCT BASKET COMPLEMENTS M&M'S**



Source: MOSL

**...with synergies in operations, coupled with technical strength**

*Besides economies of scale and operational synergies, SYMC's acquisition will significantly enhance M&M's R&D*

M&M will leverage its India advantage of low-cost component sourcing, as well as economies of scale for global sourcing. Sharing of product platforms and powertrains will help reduce cost of product development and time to market. SYMC's ~600 R&D staff and modern R&D infrastructure will significantly enhance M&M's R&D efforts. Joint R&D program will enable optimization of investments in product development. This coupled

with product lifecycle experience accumulated by SYMC over 40 years will supplement M&M's product lifecycle management. SYMC already uses engines developed in-house and will enhance M&M's capabilities in engine development. It will also give M&M access to petrol powertrain, along with its diesel powertrains.

**Will also give access to high potential export markets**

*M&M will also be able to leverage SYMC's international network of 1,400 dealers*

SYMC has a presence in Europe, Russia, South America, the Middle East, Africa and Asia. It has a marketing network of over 1,400 dealers (of which 138 are in South Korea) in South Korea, Europe, Russia and other Asian countries. Export markets offer significant potential for SYMC's products. In the last six months, it has already signed two long-term contracts totaling to annual volumes of ~26,000 units. These contracts increase the visibility of SYMC's export volumes and will aid its turnaround.

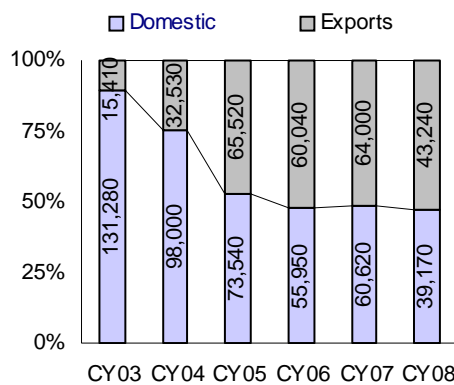
*SYMC has contracts for exports to Russia till 2017 and to Vietnam till 2014, totalling to ~26,000 units p.a*

SYMC has signed a long-term export agreement with its Russian partner Sollers, to export 160,000 SUVs to Russia until 2017. It already had a distributorship contract with Sollers since 2005 and has exported 40,000 units to Russia since then. Shipments will be in knocked-down form, and Sollers will assemble the SUVs at its new assembly unit.

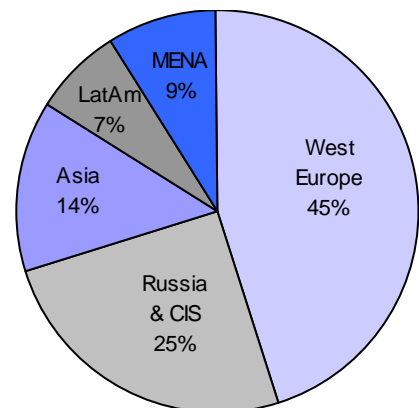
Similarly, it has entered into a deal to export 16,000 units of Kyron to Vietnam in completely knocked-down (CKD) form till 2014. This will also generate additional revenues, including technology assistance fee by providing manpower to assist local assembly lines. This contract will further enhance SYMC's presence in the Asian market.

In CY08, Western Europe accounted for 45% of SYMC's exports, Russia & CIS countries for ~25%, Asia for ~14%, South America for ~7% and MENA for 9-10%. It does not have any exports to the US market.

**SYMC: TREND IN MARKET MIX**



**SYMC: EXPORT MIX**



Source: Ssangyong Motors/M&M/MOSL

*The share of exports in SYMC's sales volumes has consistently increased to over 50% currently*

**Focused management, financial stability will help normalize SYMC's operations**

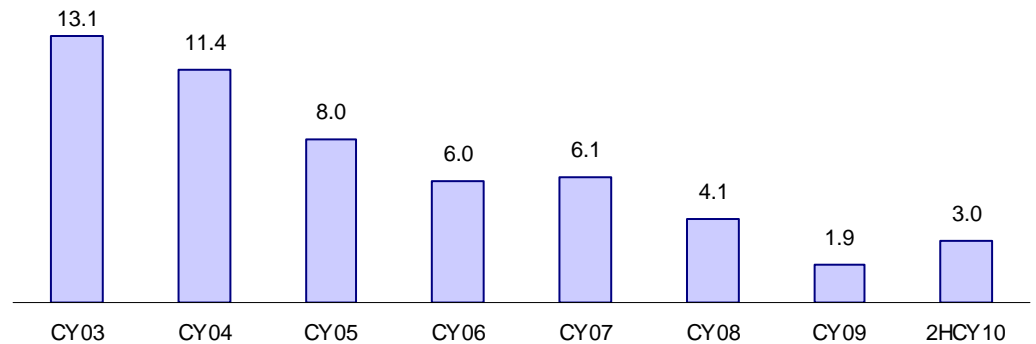
*Frequent change in ownership and financial instability have impacted SYMC's performance*

SYMC has undergone change in ownership twice since 1997. In 1997, Daewoo Motors bought a controlling stake from the Ssangyong Group, only to sell it off again in 2000, because the conglomerate ran into deep financial troubles. In late 2004, the Chinese automobile manufacturer, SAIC took 51% stake in SYMC. SAIC was blamed for stealing technology and failure to make continued investments.

*We expect focus to return to business and product development after M&M acquires SYMC*

Frequent change in ownership coupled with financial instability resulted in underinvestment/lack of investment in SYMC's product development and business. This in turn resulted in volumes declining at a compounded rate of ~29% since CY05. With M&M acquiring SYMC, we expect reduction in debt and interest burden. Focus will return to business and product development. With stable management and improvement in financials, we expect normalcy in operations to return.

**SYMC: MARKET SHARE IN DOMESTIC PV SEGMENT DECLINING SINCE CY03**



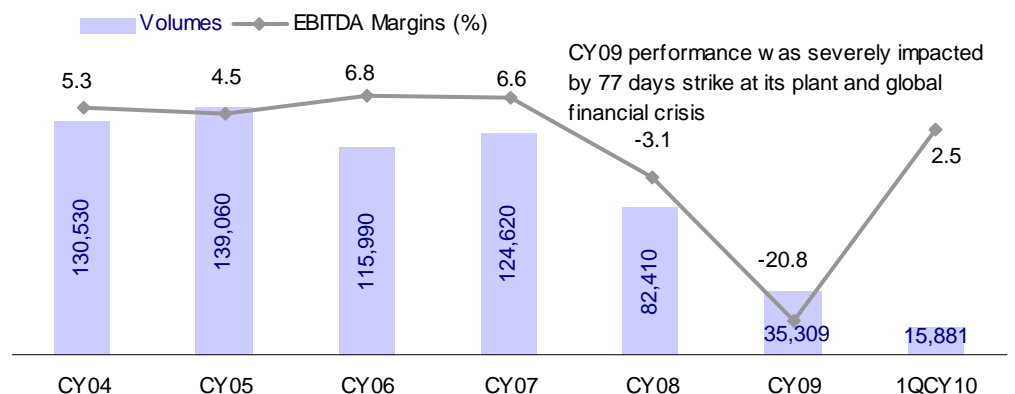
Source: KAMA

*SYMC is already on the path to recovery; with M&M taking management control, the recovery will be expedited*

**Cost rationalization, pick-up in volumes to aid cash breakeven for SYMC**

SYMC has witnessed significant financial duress, especially since CY08. It got accentuated during CY09 due to 77 days strike at its plant. As part of the settlement with workers, it reduced its manpower by 37% (~2,500 people) to 4,400 people, coupled with wage reduction. In CY08, it incurred EBITDA loss of 3%, with volume of ~82,400 units. Following the pick-up in volumes, reduction in staff cost and other cost cutting initiatives, SYMC turned EBITDA positive in 1QCY10, with volumes of ~16,000 units and EBITDA margin of 2.5%. Subsequently, its volumes have picked up further, with a monthly run-rate of 7,000 units since April 2010. Post the expected launch of 'C-200', volumes are likely to pick up further. With fund infusion by M&M to retire long-term debt, we estimate significant reduction in its interest burden (~US\$10m in 1QCY10), thereby enabling cash breakeven. Further, cost-cutting initiatives coupled with operational synergies with M&M would enable turnaround of SYMC at PAT level.

**SYMC: EBITDA BREAKEVEN IN 1QCY10**



Source: Bloomberg/MOSL

**SYMC: VOLUME PICK-UP, DEBT RETIREMENT HELP ACHIEVE CASH BREAKEVEN**

US\$ M	CY04	CY05	CY06	CY07	CY08	CY09	1QCY10
Volumes	130,530	139,060	115,990	124,620	82,410	35,309	15,881
Change (%)	-11.0	6.5	-16.6	7.4	-33.9	-57.2	NA
<b>Net Sales</b>	<b>2,884</b>	<b>3,355</b>	<b>3,093</b>	<b>3,357</b>	<b>2,311</b>	<b>841</b>	<b>349</b>
Change (%)	4.7	16.3	-7.8	8.5	-31.1	-63.6	NA
Gross Margins (%)	19.2	18.4	19.1	18.8	12.4	6.0	
SG&A (% of sales)	13.9	13.8	12.4	12.2	15.5	26.8	
<b>EBITDA</b>	<b>153</b>	<b>152</b>	<b>210</b>	<b>221</b>	<b>-73</b>	<b>-175</b>	<b>9</b>
EBITDA Margins (%)	5.3	4.5	6.8	6.6	-3.1	-20.8	2.5
Depreciation	126	154	182	174	138	56	20
Interest Expense	33	31	40	34	39	84	10
Other Income	53	-40	-52	10	-415	43	0
<b>Reported PAT</b>	<b>10</b>	<b>-101</b>	<b>-205</b>	<b>12</b>	<b>-657</b>	<b>-273</b>	<b>-22</b>

Source: Bloomberg, MOSL

**Low capex requirements to support existing operations**

The management indicated that SMYC has manufacturing capacity of ~120,000 vehicles and ~150,000 engines (on one-shift basis). Based on current manpower of ~4,400 people, its current manned capacity of 100,000 vehicles is more than adequate to meet its current run rate of ~7,000 vehicles/month.

It plans to launch a new product named 'C-200' in CY10. The majority of the investment in tooling and product development has already been incurred. However, SYMC will have to invest in its product development program, as after launch of 'C-200' it does not have any product available for launch for another 1.5-2 years.

**'C-200' BUILT ON NEW PLATFORM, TO BE LAUNCHED BY END-CY10**

Source: MOSL

**Valuation and view**

*We remain positive on  
M&M's prospects;  
maintain Buy*

We remain positive on M&M's prospects, given its market dominance in core business of UVs and Tractors, coupled with cheap valuations. It will be one of the biggest beneficiaries of normal monsoon, given its high dependence on rural market demand. Pending valuation consideration for SYMC, we are not yet factoring SYMC's acquisition in our estimates. The stock trades at 10.8x FY11E consolidated EPS of Rs57.9 and 9.2x FY12E consolidated EPS of Rs68.3. We maintain **Buy**, with an SOTP-based (FY11E) target price of Rs760.

**M&M: SUM-OF-THE-PARTS (RS/SHARE)**

	FY11E	FY12E
<b>Value of core business</b>		
Core EPS (excl. subsidiary dividend)	40.8	47.0
PE attributable (x)	14	14
Target price	571	657
<b>Value of listed subsidiaries</b>		
1. Tech Mahindra		
Value per share of M&M	63	70
Value p.s. of M&M after 20% disc.	50	56
2. M&M Financial Services		
Value per share of M&M	39	39
Value p.s. of M&M after 20% disc.	31	31
3. Mahindra Lifespaces		
Value per share of M&M	13	13
Value p.s. of M&M after 20% disc.	11	11
4. Mahindra Holidays		
Value per share of M&M	66	66
Value p.s. of M&M after 20% disc.	53	53
5. Others - Value per share of M&M		
	44	50
<b>Target price (after 20% discount)</b>	<b>760</b>	<b>858</b>

Source: MOSL



## Appendix

### Ssangyong Motors: a brief history

Ssangyong Motors (SYMC) is a South Korean company making SUVs and cars. Founded in 1954, it began its business as a manufacturer of commercial vehicles. In 1986, the SsangYong Group acquired Keohwa Motors, a specialized UV manufacturer, with the brand Korando. In 1988, it developed a compact 4WD SUV in the Korando family, which was the first SUV manufactured in Korea. In early 1990s, SYMC established a strategic alliance with Mercedes-Benz AG, through which it gained competence to develop vehicles (including engines) employing advanced technologies and to launch them in global markets.

#### SYMC: PRODUCT PORTFOLIO

##### SUV 'ACTYON' WITH 2L DIESEL ENGINE

PRICE STARTS AT ~US\$27,000



##### SUV 'KYRON' WITH 2L DIESEL ENGINE

PRICE STARTS AT ~US\$33,000



##### SUV 'RODIUS'/'STAVIC' WITH 2.7L DIESEL ENGINE

PRICE STARTS AT ~US\$33,000



##### SUV 'ACTYON SPORT' WITH 2L DIESEL ENGINE

PRICE STARTS AT ~US\$25,000



##### SUV 'REXTON II' WITH 2.7L DIESEL ENGINE

PRICE STARTS AT ~US\$36,000



##### LUXURY SEDAN 'CHAIRMAN W'

PRICE STARTS AT ~US\$60,000



Source: Ssangyong, Industry/MOSL

<b>SSANGYONG MOTORS - INCOME STATEMENT SNAPSHOT</b>							<b>(US\$MILLION)</b>
	<b>CY04</b>	<b>CY05</b>	<b>CY06</b>	<b>CY07</b>	<b>CY08</b>	<b>CY09</b>	<b>1QCY10</b>
Volumes	130,530	139,060	115,990	124,620	82,410	35,309	15,881
<i>Change (%)</i>	-11.0	6.5	-16.6	7.4	-33.9	-57.2	NA
Net Realization	22,094	24,127	26,663	26,938	28,048	23,811	21,999
<i>Change (%)</i>	17.6	9.2	10.5	1.0	4.1	-15.1	NA
<b>Net Sales</b>	<b>2,884</b>	<b>3,355</b>	<b>3,093</b>	<b>3,357</b>	<b>2,311</b>	<b>841</b>	<b>349</b>
<i>Change (%)</i>	4.7	16.3	-7.8	8.5	-31.1	-63.6	NA
<b>Expenditure</b>							
COGS	2,331	2,739	2,501	2,725	2,026	791	
<i>COGS (% of Sales)</i>	80.8	81.6	80.9	81.2	87.6	94.0	
<b>Gross Profit</b>	<b>553</b>	<b>617</b>	<b>592</b>	<b>632</b>	<b>286</b>	<b>50</b>	
<i>Gross Margins (%)</i>	19.2	18.4	19.1	18.8	12.4	6.0	
SG&A	400	464	382	411	358	225	
<i>SG&amp;A (% of sales)</i>	13.9	13.8	12.4	12.2	15.5	26.8	
Total Costs	2,731	3,203	2,882	3,136	2,384	1,016	340
<b>EBITDA</b>	<b>153</b>	<b>152</b>	<b>210</b>	<b>221</b>	<b>-73</b>	<b>-175</b>	<b>9</b>
<i>EBITDA Margins (%)</i>	5.3	4.5	6.8	6.6	-3.1	-20.8	2.5
Depreciation	126	154	182	174	138	56	20
Interest Expense	33	31	40	34	39	84	10
Other Income	53	-40	-52	10	-415	43	0
<b>PBT before EO items</b>	<b>47</b>	<b>-73</b>	<b>-64</b>	<b>24</b>	<b>-665</b>	<b>-273</b>	<b>-21</b>
Forex Losses (Gains)	-2	-15	-3	11	-8	0	1
<b>PBT</b>	<b>49</b>	<b>-58</b>	<b>-60</b>	<b>12</b>	<b>-657</b>	<b>-273</b>	<b>-22</b>
Tax	39	43	145	0	0	0	0
<i>Effective Tax Rate (%)</i>	79.7	-74.5	-239.5	0.3	0.0	0.0	0.0
<b>Reported PAT</b>	<b>10</b>	<b>-101</b>	<b>-205</b>	<b>12</b>	<b>-657</b>	<b>-273</b>	<b>-22</b>
<i>Change (%)</i>	-98.0	-1113.6	103.4	-106.1	-5379.6	-58.5	NA

<b>SSANGYONG MOTORS - BALANCE SHEET</b>							<b>(USD Million)</b>
<b>Y/E DECEMBER</b>	<b>CY04</b>	<b>CY05</b>	<b>CY06</b>	<b>CY07</b>	<b>CY08</b>	<b>CY09</b>	
Share Capital	598	613	666	662	492	468	
Reserves	580	497	329	371	(287)	(208)	
<b>Net Worth</b>	<b>1,179</b>	<b>1,110</b>	<b>995</b>	<b>1,033</b>	<b>205</b>	<b>260</b>	
Long-Term Borrowings	238	410	322	401	287	349	
Other Long-Term Liabilities	215	234	243	256	180	302	
Loan Funds	454	644	565	657	467	651	
<b>Total Funds Employed</b>	<b>1,633</b>	<b>1,754</b>	<b>1,560</b>	<b>1,690</b>	<b>671</b>	<b>910</b>	

**APPLICATION OF FUNDS**

Gross Fixed Assets	2,556	2,785	3,175	3,047	1,881	2,030
Less: Depreciation	1,094	1,263	1,554	1,534	1,192	1,336
<b>Net Fixed Assets</b>	<b>1,462</b>	<b>1,522</b>	<b>1,621</b>	<b>1,513</b>	<b>689</b>	<b>694</b>
Capital WIP	333	275	145	176	155	142
Investments	9	11	16	109	22	15
<b>Curr.Assets, L &amp; Adv.</b>	<b>717</b>	<b>874</b>	<b>746</b>	<b>785</b>	<b>488</b>	<b>348</b>
Cash & cash Balances	11	258	144	73	62	11
Sundry debtors & Notes Receivable	205	212	189	287	90	77
Inventory	352	333	360	315	291	185
Other Current Assets	149	71	53	111	46	75
<b>Current Liabilities</b>	<b>889</b>	<b>928</b>	<b>968</b>	<b>893</b>	<b>683</b>	<b>289</b>
Sundry creditors	449	506	563	318	177	59
Other Liabilities	439	422	405	575	506	230
<b>Net Current Assets</b>	<b>(172)</b>	<b>(54)</b>	<b>(222)</b>	<b>(108)</b>	<b>(195)</b>	<b>59</b>
<b>Application of Funds</b>	<b>1,633</b>	<b>1,754</b>	<b>1,560</b>	<b>1,690</b>	<b>671</b>	<b>910</b>







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**Mahindra & Mahindra**

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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