India Auto Sector --- Maintain MARKET WEIGHT

Vulnerability to segments and markets – how exposed are auto ancillaries?

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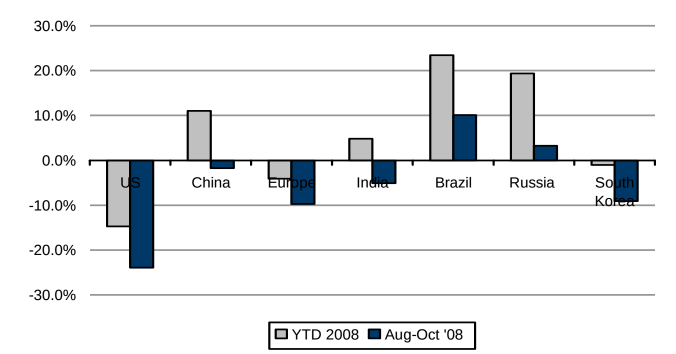
- We analyse the exposure of India's auto ancillaries to a slowdown in various business segments and global markets. Exports account for c20% of India's component manufacturers.
- Global auto markets have declined 2-30% in the past three months (both passenger vehicles (PVs) and commercial vehicles (CVs).
- Vendors with high exposure to domestic auto manufacturers (OEs) and to exports (75% of which is to OEs) are vulnerable. Such vendors face double-digit decline in sales and severe margin pressure. Working capital cycle will also likely stretch due to liquidity issues.
- Vendors with strong exposure to the domestic replacement market (growing at c. 8-12%) like tyre and battery manufacturers, are better placed. However, we do fear threat from imports (especially from China) would take away most of the benefits in industries such as tyres.
- In the short term, vendors are likely to gain from rupee depreciation and lower commodity prices, but this will likely be competed away over a quarter or two. We see lower component prices benefiting domestic OEs, especially two-wheeler manufacturers.

We analyse the exposure of India's auto ancillaries to a slowdown in business segments and end-user markets. Global auto markets have slowed down considerably in CY08 (and declined sharply in the past three months) – developed markets (US and Europe) have seen the largest decline. In India too, PVs have declined 2.2%, while CVs have declined 14.5% during August-October 2008.

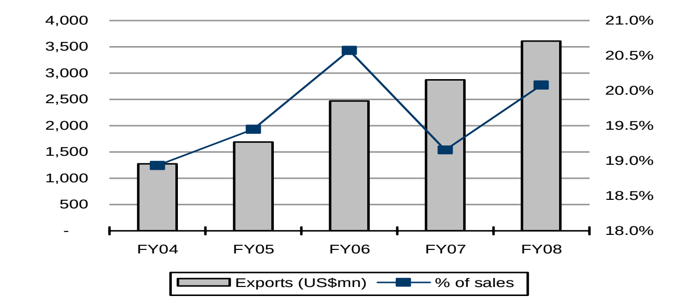
Figure 1: Demand in global auto markets has slowed down in CY08



Source: CEIC, ACEA, Credit Suisse estimates. Europe, S Korea data is YTD Sep '08

Exports account for c20% of India's component manufacturers.Given severe demand pressure in most global auto markets, vendors with high exposure to domestic and global OEs are likely most vulnerable to a drop in sales and profitability. Receivables and inventory days are likely to increase due to possible liquidity issues faced by OEs and lower demand.

Figure 2: Exports account for c20% of sales for Indian auto ancillaries



Source: ACMA

Figure 3: Sales split of auto ancillaries in India

		Domestic			
Rs mn	M. Cap	OEM	Replacement	Others	Exports
Bosch	95,353	56.2%	18.5%	9.6%	15.7%
Exide	34,880	25.0%	33.4%	37.0%	4.6%
Bharat Forge	21,876	56.2%	0.0%	0.0%	43.8%
Motherson Sumi	18,041	66.5%	0.0%	11.0%	22.5%
Apollo Tyres	11,215	22.0%	70.0%	0.0%	8.0%
Kirloskar Oil Engines	8,806	6.3%	0.0%	86.5%	7.2%
SKF India	7,794	27.2%	18.1%	45.3%	9.5%
MRF	7,432	20.7%	62.1%	6.0%	11.2%
Asahi India Glass	6,725	37.2%	9.3%	46.5%	7.0%
Tube Investments	6,652	43.8%	10.0%	37.4%	8.8%

Source: Company data, Credit Suisse estimates.

Companies with strong exposure to the domestic replacement market (growing at 8-12% across segments), though, are likely better placed to weather the demand slump. Indian tyre and battery manufacturers (30-70% of sales via replacement demand) are likely to be least impacted; however, Chinese imports could be a threat for tyre companies. While vendors will likely benefit from lower commodity prices and rupee depreciation in the near term, their realisations could drop as demand pressure flows through the supply chain – consequently, domestic OEs (especially two-wheeler manufacturers) will likely benefit from lower component prices.

Valuation metrics

		CS	Price		EPS chg (%)		TP (%)	Up/dn	EPS		EPS grth (%)		P/E (x)		Div. yld (%)	ROE	P/B
Company	Ticker	Rating	Local	Target	T+1	T+2	Chg	(%)	T+1	T+2	T+1	T+2	T+1	T+2	T+1	(%)	(x)
Bajaj Auto Limited	BJAUT IN	O	366	687	0	0	0	88	54.7	63.1	(9)	15	6.7	5.8	6.8	39.2	2.6
Hero Honda	HH IN	O	749	982	0	0	0	31	63.4	76.3	31	20	11.8	9.8	3.4	33.8	4.0
Maruti Suzuki	MSIL IN	O	517	666	0	0	0	29	58.4	70.8	(8)	21	8.8	7.3	1.2	16.9	1.5
Bosch	BOS IN	O	2,963	4,166	0	0	0	41	198	260	4	31	14.9	11.4	0.7	20.3	3.0
Bharat Forge	BHFC IN	O	98.15	193	0	0	0	97	12.9	14.5	(5)	12	7.6	6.8	4.6	13.1	1.0

Note: O = OUTPERFORM, N = NEUTRAL, U = UNDERPERFORM; Source: Company data, Credit Suisse estimates

Companies Mentioned *(Price as of 20 Nov 08)*
Ashok Leyland Ltd (ASOK.BO, Rs14.50, NEUTRAL [V], TP Rs32.16)
Bajaj Auto Limited (BAJA.BO, Rs365.75, OUTPERFORM [V], TP Rs687.14)
Hero Honda Motors Ltd (HROH.BO, Rs748.55, OUTPERFORM, TP Rs981.71)
Mahindra & Mahindra (MAHM.BO, Rs303.50, NEUTRAL, TP Rs539.85)
Maruti Suzuki India Ltd (MRTI.BO, Rs516.50, OUTPERFORM, TP Rs666.43)
Bosch Limited (BOSH.BO, Rs2962.50, OUTPERFORM, TP Rs4166.10)
Bharat Forge Limited (BFRG.BO, Rs98.15, OUTPERFORM, TP Rs193.12)
Apollo Tyres (APLO.BO, Rs21.85, NOT RATED)
MRF (MRF.BO, Rs1744.55, NOT RATED)
Exide Industries (CHLR IN, Rs42.3, NOT RATED)
Motherson Sumi Ltd (MSS IN, Rs52.05, NOT RATED)
Kirloskar Oil Engines Ltd (KKOE IN, Rs47, NOT RATED)
Tube Investments of India Ltd. (TUBE.BO, Rs36, NOT RATED)

Disclosure Appendix

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