Prabhudas Lilladher

Maruti Suzuki

Operational performance disappoints

July 22, 2008

Rating	**Market Performer**
Price	Rs648
Target Price	Rs715
Implied Upside	10.4%
Sensex	13,850

(Prices as on July 21, 2008)

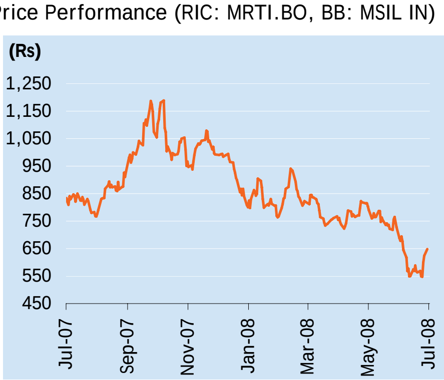
Trading Data	
Market Cap. (Rs bn)	187.3
Shares o/s (m)	289.0
Free Float	45.8%
3M Avg. Daily Vol ('000)	149.3
3M Avg. Daily Value (Rs m)	107.0

Major Shareholders	
Promoters	54.2%
Foreign	14.8%
Domestic Inst.	24.0%
Public & Others	7.0%

Stock Performance

(%)	1M	6M	12M
Absolute	(18.1)	(25.5)	(28.0)
Relative	(15.2)	(10.1)	(18.9)

Price Performance (RIC: MRTI.BO, BB: MSIL IN)



Source: Bloomberg

Q1FY09 Result Update

- **Results:** Maruti Suzuki India (MSIL) reported 21% topline growth to Rs47.5bn in Q1FY09. However, margins continued to be under pressure and were down 449bps for the quarter at 10.1%. Margins were hit primarily due to rising raw material prices, higher import bill due to appreciation of the yen and higher operating expense due to capacity ramp-up at Manesar. However, PAT decline for the quarter was arrested with higher other income of about Rs3.2bn. Adjusted PAT was down about 4% YoY to Rs4.79bn.
- **Capex update:** The company is expected to ramp up its Manesar capacity to about 3L units pa by the year end by which time the total capacity would touch 1mn units pa. The company also intends to launch it's A-Star for the European markets in the current fiscal.
- **Outlook & valuation:** Media reports suggest that steel prices are expected to go up again in August. Capacity ramp-up at Manesar will result in higher operating expenditure over the near term. With new product launches, royalty expense would continue to remain at these high levels. Maruti is now facing a dual challenge of lower volume off-take in a high inflationary environment coupled with rising operational costs impacting its margins.

  Our estimates factor in a 16.0% volume growth and a 194bps YoY hit on margins to 10.5% for FY09. The company is currently trading at 10.0x FY09E EPS of Rs65.0 and 8.0x FY10E EPS of Rs81.0. While the downside risk to the stock is limited, the current high interest rate and inflationary trend compels us to downgrade the stock to Market Performer.

Key financials (Y/e March)	FY07	FY08	FY09E	FY10E
Revenue (Rs m)	146,539	178,603	227,751	282,638
Growth (%)	*21.6*	*21.9*	*27.5*	*24.1*
EBITDA (Rs m)	19,904	22,179	23,862	32,537
PAT (Rs m)	15,619	17,308	18,773	23,416
EPS (Rs)	54.0	61.1	65.0	81.0
Growth (%)	*31.4*	*13.0*	*6.3*	*24.7*
Net DPS (Rs)	4.5	5.0	5.0	6.0

Source: Company Data; PL Research

Profitability & valuation	FY07	FY08	FY09E	FY10E
EBITDA margin (%)	*13.6*	*12.4*	*10.5*	*11.5*
RoE (%)	*25.4*	*22.9*	*20.7*	*21.3*
RoCE (%)	*24.0*	*21.1*	*19.3*	*20.2*
EV / sales (x)	1.2	1.1	0.8	0.7
EV / EBITDA (x)	9.0	8.7	8.0	5.8
PE (x)	12.0	10.6	10.0	8.0
P / BV (x)	2.4	2.0	1.7	1.5
Net dividend yield (%)	*0.7*	*0.8*	*0.8*	*0.9*

Source: Company Data; PL Research

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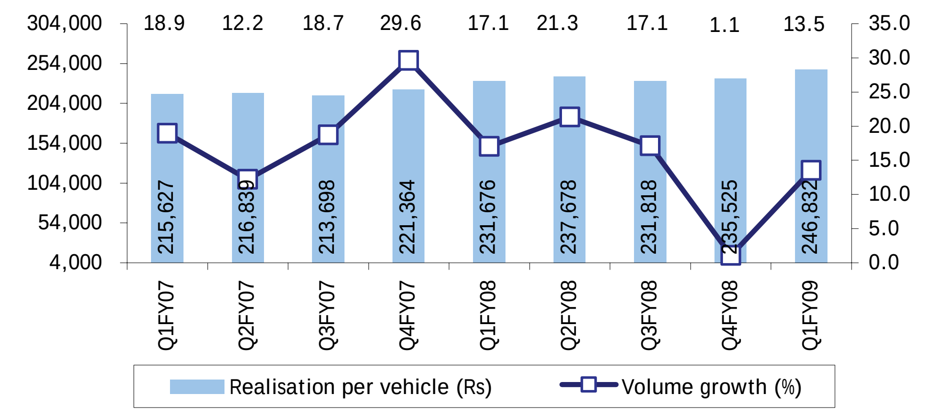
Highlights

Topline growth maintained

Maruti Suzuki posted 21% topline growth to Rs47.5bn. Volume growth for the quarter was at 13.5% YoY. While domestic sales were up 12% YoY, exports during the quarter were up 37.7% YoY. Excise duty reduction and the price hike implemented w.e.f May 17 in the range of Rs1,000–18,000, helped improve the net realisation per vehicle by 6.5% YoY, which boosted topline.

Volume growth, better realisations boost topline

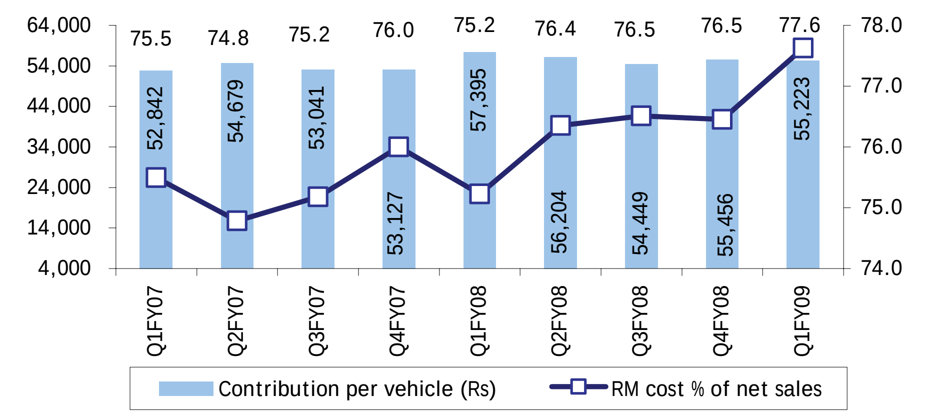


Source: Company Data, PL Research

Rising material cost continues to hit per vehicle contribution

Appreciation of the rupee against the yen increased the import bill to the tune of 14%. This, coupled with the rising raw material cost, resulted in 240bps YoY rise in raw material expense in the quarter. As a result, contribution per vehicle for the quarter was down 3.8% YoY at Rs55,223.

Raw material pressure continues

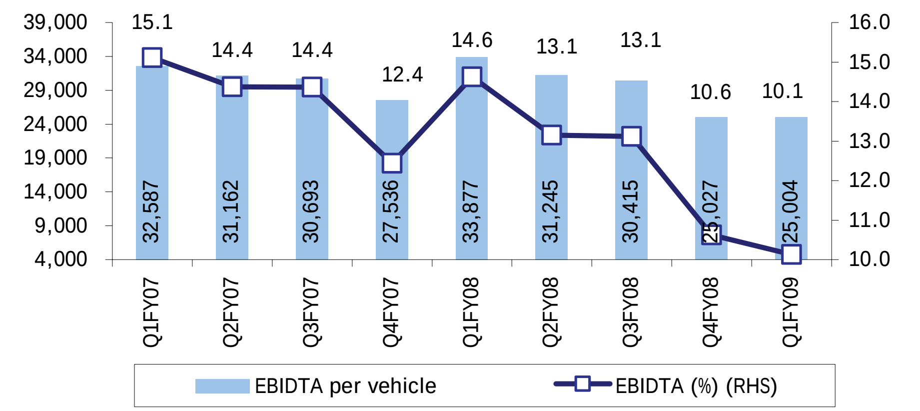


Source: Company Data, PL Research

Operating expenses rise

A new R&D centre, paint shop and capacity ramp-up at Manesar resulted in a 26% QoQ rise in employee costs. With new product launches, royalty cost was higher by about 33% YoY to Rs1.3bn. Power & fuel cost was also up by about 65% YoY on account of the Manesar plant, which currently uses diesel as its operating fuel. Selling & distribution expense went up by a percent to 3.6% of net sales due to higher advertisement and freight expenditure. Rising operating expenditure resulted in 449bps YoY decline in margins to 10.1%. As a result, EBIDTA per vehicle was down 26.2% YoY at Rs25,004.

Per vehicle EBIDTA fails to recover



Source: Company Data, PL Research

Higher other income arrests PAT slide

Absolute EBIDTA during the quarter was down 16.2% YoY to Rs4.8bn. The new depreciation policy resulted in an additional impact of about Rs619m. However, adjusted PAT was down only 4% YoY to Rs4.8bn due to higher other income at Rs3.3bn (up 47% YoY) from an investment book of about Rs48.5bn. PAT has been adjusted for MTM losses to the tune of Rs179m.

Valuation

The company is slated to launch *A-Star* by the end of the year for the European markets, which is expected to be a premium product. The company's latest product offerings – *Swift* diesel, *SX4* and *Dzire* – have been very well accepted in the market, with *Dzire* having a waiting period of about 4-6 months. As a result, Maruti is ramping up capacity at Manesar to 300,000 per annum by the end of the year. Thus, volume off-take is not expected to be a problem for the company going forward. Also, better product mix is expected to provide some cushion to margins. In a period of increasing margin pressure, non-operating income would also boost profitability.

However, media reports suggest that steel prices are expected to go up again in August. Capacity ramp-up at Manesar will result in higher operating expenditure over the near term. With new product launches, royalty expense would continue to remain at these high levels. Maruti is now facing a dual challenge of lower volume off-take in a high inflationary environment coupled with rising operational costs impacting its margins.

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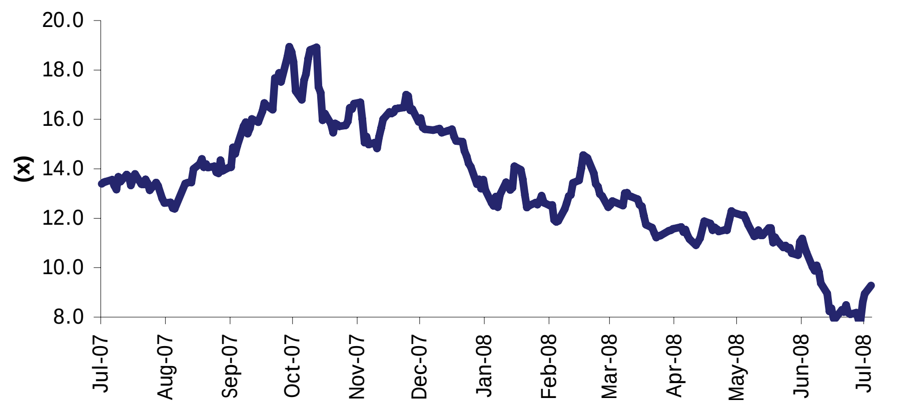
One-year rolling forward PE chart



Source: PL Research

Q1FY09 result overview **(Rs m)**

Y/e March	**Q1FY09**	**Q1FY08**	*YoY gr. (%)*	**Q4FY08**	*QoQ gr. (%)*
Net sales	**47,536**	**39,308**	*20.9*	**47,629**	*(0.2)*
Expenditure					
Raw material	36,567	31,041	*17.8*	38,861	*(5.9)*
Change in stock	334	(1,471)	*(122.7)*	(2,447)	*(113.7)*
as % of net sales	*77.6*	*75.2*		*76.5*	
Personnel cost	1,112	805	*38.2*	880	*26.3*
as % of net sales	*2.3*	*2.0*		*1.8*	
Mfg. expenses	4,708	3,186	*47.8*	5,273	*(10.7)*
as % of net sales	*9.9*	*8.1*		*11.1*	
Total expenditure	42,720	33,560	*27.3*	42,568	*0.4*
EBITDA	**4,815**	**5,748**	*(16.2)*	**5,061**	*(4.9)*
EBITDA margin (%)	*10.13*	*14.62*		*10.63*	
Depreciation	1,661	822	*102.0*	988	*68.0*
EBIT	**3,155**	**4,926**	*(36.0)*	**4,073**	*(22.5)*
Net interest	168	151	*11.5*	161	*4.3*
Non-operating income	3,288	2,233	*47.3*	3,070	*7.1*
PBT before extraord. items	**6,274**	**7,007**	*(10.5)*	**6,982**	*(10.1)*
Extraordinary income	-	-		-	
Extraordinary expenses	179	-		2,628	
PBT post extraordinary items	**6,095**	**7,007**	*(13.0)*	**4,354**	*40.0*
Total tax	1,437	2,011	*(28.6)*	1,377	*4.3*
Total tax rate (%)	*23.6*	*28.7*		*31.6*	
Reported profit	**4,659**	**4,996**	*(6.8)*	**2,977**	*56.5*
Adj. profit after tax	**4,795**	**4,996**	*(4.0)*	**4,774**	*0.5*

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PL's Recommendation Nomenclature					
BUY	:	> 15% Outperformance to BSE Sensex	**Outperformer** (OP)	:	5 to 15% Outperformance to Sensex
Market Performer (MP)	:	-5 to 5% of Sensex Movement	**Underperformer** (UP)	:	-5 to -15% of Underperformace to Sensex
Sell	:	<-15% Relative to Sensex			
Not Rated (NR)	:	No specific call on the stock	**Under Review** (UR)	:	Rating likely to change shortly