1 May 2007 | 6 pages

Maruti Udyog (MRTI.BO)

Buy: April Sales +17% YoY, Spurred by Promotions

- Apr sales up +17% y/y — Domestic sales rose c17% YoY due to benign base effect. Maruti has been able to show steady growth despite higher interest rates – albeit aided by aggressive promotion schemes. MUL offered financing at 7.99% in select cities; also offered aggressive discounts on select models (WagonR and Esteem) amounting to 4-5.8% of vehicle on-road prices.

- Exports — Registered sedate c10% y/y growth – we expect exports to grow at 15% over FY08E, on the back of better penetration in non European markets and easing of capacity constraints.

- Segmental analysis — A2 segment remains mainstay – accounting for c70% of domestic sales; the segment grew by 20% y/y benefiting from new models (Zen Estilo, Swift diesel, Wagon R Duo). Maruti's segmental market share rose to around 61% Q407 (from 55% in 1Q07), on the back of new models. M800 sales also rose ~10%y/y, benefiting from low base effect.

- Market share trends — MUL's overall domestic market share declined to 49% in Mar 07, (vs. 55% in Feb07) as Hyundai and Tata Motors gained share in the A2 segment. Management has indicated that near term, market share remains the focus – we thus expect margin pressures to continue on account of a changing model mix and higher promotional expenses.

- Reiterate Buy (1L) — Key risk factors are rising rates (that could curb volume growth), changing model mix (which affects margins adversely) and higher promotional spends/discounts (which also adversely affect margins).

Buy/Low Risk	**1L**
Price (30 Apr 07)	Rs795.30
Target price	Rs945.00
Expected share price return	18.8%
Expected dividend yield	0.6%
Expected total return	**19.5%**
Market Cap	Rs229,770M
	US$5,632M

Figure 1. Maruti – Apr 2007 Sales

	Apr-07 Nos	% chg YoY	% chg over Mar
A1 (M800)	6,324	9.8	3.0
C (Omni, Versa)	6,118	21.1	(29.4)
A2 (Alto, Wagon-R, Zen, Swift)	33,878	20.3	(28.0)
A3 (Baleno, Esteem)	2,124	(12.7)	(12.0)
MUV (Gypsy, Vitara)	208	19.5	(23.5)
Total Domestic	**48,652**	**17.0**	**(24.6)**
Exports	1,700	9.5	(76.4)
Overall	**50,352**	**16.8**	**(29.8)**

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See Appendix A-1 for Analyst Certification and important disclosures.

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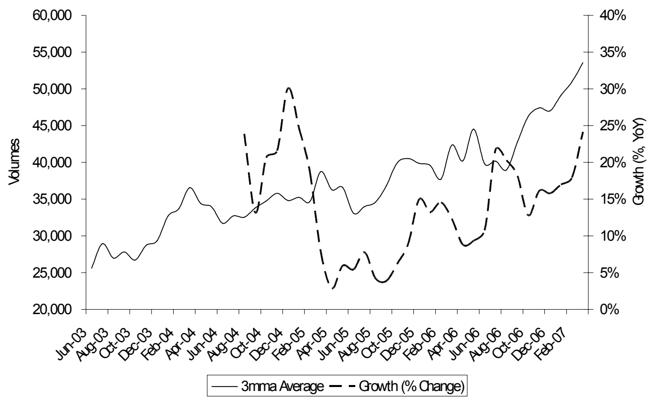
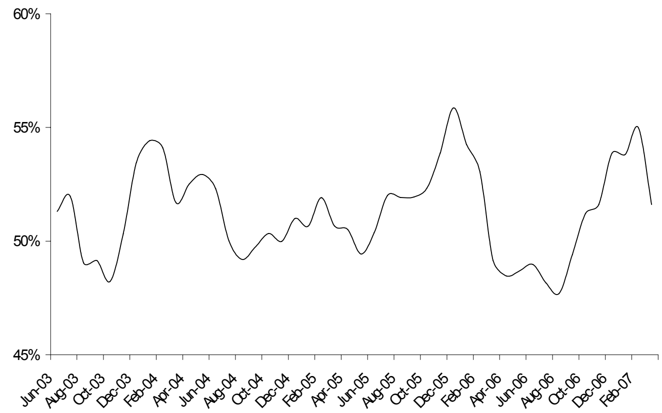
Figure 2. Maruti – Domestic Volumes (3mma) and Growth



Source: Company Reports, SIAM

Note: Volumes on LHS, Growth (%) on RHS

Figure 3. Maruti – Domestic Market Share (3mma), %



Source: Company Reports, SIAM

Other Points:

1) New Model launches – Dealer sources indicate that dispatches for SX4 has started, and we believe that this will improve Maruti's market share in A3 segment, which has fallen to around 12% Q407 from 15% in 1Q07.

2) Government's stake sale – Government is expected to divest its residual c10.3% stake by mid – May 07, according to press reports (source: Rediff).

Maruti Udyog

Company description

Maruti is a subsidiary of Suzuki Motor Corp (holds a 54% equity stake). The government of India remains a significant equity stakeholder (10%). With its early-mover advantage in the Indian market, Maruti retains a dominant market share despite increasing competition.

Investment thesis

We rate the stock as Buy/Low Risk (1L). The Indian car market is on a structural growth path (estimated CAGR of 12-15% over the medium term), driven by low penetration levels, improved demographics and infrastructure, tax cuts and availability of consumer finance at relatively low interest rates. Despite the presence of most global majors, Maruti has managed to remain the dominant India player. Its competitive advantage stems from an early start, a balanced product portfolio targeted at the sweet spot of the market, its having the largest distribution and service network, and its consistently high quality ratings. While competitive pressures increase, we expect market share erosion to be gradual and growth in absolute terms to be robust for Maruti. We estimate earnings growth and cash earnings growth of 12.3% and 16.3% CAGR respectively over FY07-09, driven by unit sales CAGR of 17%. We expect margins to contract around 50bps over this period, given cost pressures, a changing product mix and increasing competition, which will keep pricing pressure subdued.

Valuation

Our 12-month target price of Rs945 is based on 11x P/CEPS FY09E. We believe the multiple compares favorably with the cash earnings CAGR of c16.3% over FY07E-09E. At our target price, the stock would trade at the mid-point of the current trading band.

Maruti has a relatively short trading history. Our multiple of 11x is at a marginal discount to the 11.4x trailing 2 year average - but merited, since competitive intensity will escalate going forward, and the macro economic environment is less conducive to growth (rising interest rates impact volumes growth across the car industry, given that 80% of vehicles are bought with finance). We prefer price/cash earnings as a valuation metric for the automobile sector, given the relatively high capital intensity (both on capacity and product development) of the business.

Risks

We rate Maruti as Low Risk based on our quantitative risk-rating system, which tracks 260-day historical share price volatility. Risks that could prevent the stock from reaching our target price and rating include: (1) sales of passenger vehicles are sensitive to economic variables - an appreciable rise in interest rates could impact volumes growth across the auto sector; (2) revised emission and safety norms could bring cost pressures; and (3) competitive pressures in the Indian market continue to increase, which could impact margins over the longer term.

Appendix A-1

Analyst Certification

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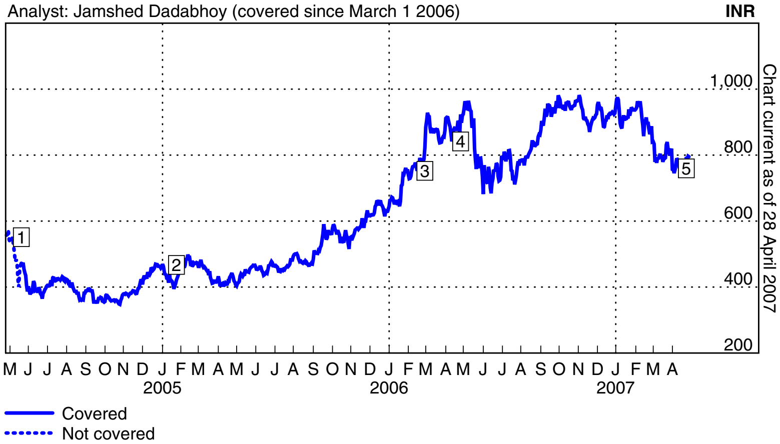
Maruti Udyog (MRTI.BO)

Ratings and Target Price History - Fundamental Research

Analyst: Jamshed Dadabhoy (covered since March 1 2006)



#	Date	Rating	Target Price	Closing Price
1:	20 May 04	1L	593.00	472.10
2:	25 Jan 05	*1M	593.00	421.50
3:	28 Feb 06	*1L	*966.00	822.60
4:	26 Apr 06	1L	*1,107.00	923.45
5:	24 Apr 07	1L	*945.00	794.40

*Indicates change.

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