

# Mahindra & Mahindra

Rs570

## Ssangyong bid attractive, but challenging

BUY

### Ssangyong buy to strengthen M&M UV presence

We believe Mahindra & Mahindra's (M&M's) bid to acquire Ssangyong Motors, a South Korean utility vehicle (UV) manufacturer, would strengthen the company's UV presence globally as it is likely to benefit from Ssangyong's technology, market reach, and production facilities. Ssangyong exports to Russia, Europe, China, Middle East, Africa, North & South America and Asia-Pacific, which will help M&M to increase reach for its own products as well.

### Declining sales, high debt major concerns

While car sales in South Korean market have been declining, large players have been able to maintain their margin. Comparatively, Ssangyong (being a small player) has not only lost sales, but also incurred losses, during last three years. Ssangyong with market capitalisation of ~Rs19bn has incurred cumulative operational loss of Rs40bn over CY07-09. Sales declined 66% to Rs41bn in CY09 from Rs120bn in CY07. Gross profit margin in CY09 came down to 6% compared to 19% in CY07. Debt/equity ratio at ~3.6x is steep as compared to Indian peers. (See Exhibit 1 and 2 on Page 2).

### Ssangyong turnaround would be a challenge

While Ssangyong's valuation v/s South Korean peers is attractive on Bloomberg CY11E EV/EBITDA and price/sales, M&M may face a challenge in turning around operations, given shrinking demand in South Korean and global auto market. Servicing Ssangyong debt would also strain M&M financials.

### M&M well placed to fund the acquisition

M&M is well placed to fund the acquisition with Rs17bn cash and D/E ratio of 0.4x. If Ssangyong bid goes through, it would increase M&M's consolidated revenue (Ssangyong's CY09 sales) by ~13%, but impact on bottomline would be negative (M&M's FY10 consolidated PAT Rs29bn and Ssangyong's CY09 loss Rs13bn). However, Bloomberg estimates for Ssangyong suggest overall improvement in financials over CY10-11, which would lower impact on M&M financials. According to our scenario analysis, if M&M buys Ssangyong at current market cap, then D/E ratio is likely to go up to 0.7x which is manageable.

### Exhibit 1: Scenario analysis - D/E ratio

	Discount /Premium to current market cap of Rs19bn				
	0.8x	0.9x	1x	1.2x	1.4x
Debt/Equity (x)	0.68	0.71	0.74	0.80	0.86

Source: BRICS Research

We would be revisiting our estimates if M&M wins the Ssangyong bid. Maintain Buy.

KEY FINANCIALS					
Y/E 31 March	2008	2009	2010	2011E	2012E
Revenue	107,426	130,937	186,021	219,598	256,796
EBITDA	6,908	10,905	29,510	33,539	37,304
EBITDA margin (%)	6.4	8.3	15.9	15.3	14.5
PAT	2,926	8,244	19,928	23,837	26,362
FDEPS (Rs)	6.0	14.8	34.3	41.0	45.3
% growth	(73.1)	145.2	131.8	19.5	10.6
P/E (x)	96.9	39.5	17.1	14.3	12.9
ROCE (%)	6.5	8.6	24.1	24.3	23.9

Source: BRICS Research, Company Data

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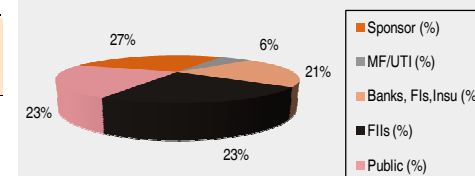
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### KEY DATA

Bloomberg	MM@IN
Reuters	MAHM.BO
52-wk H/L(Rs)	598.35/321.65
6-m avg trd value	US\$25.6mn
Market cap	Rs330.3bn/US\$7.1bn
Shares o/s	578.4mn
Face value	Rs5

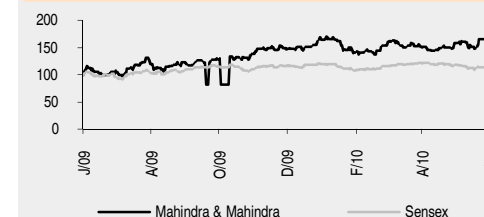
Source: Bloomberg

### SHAREHOLDING (%)



Source: CMIE

### PRICE PERFORMANCE



Source: Bloomberg

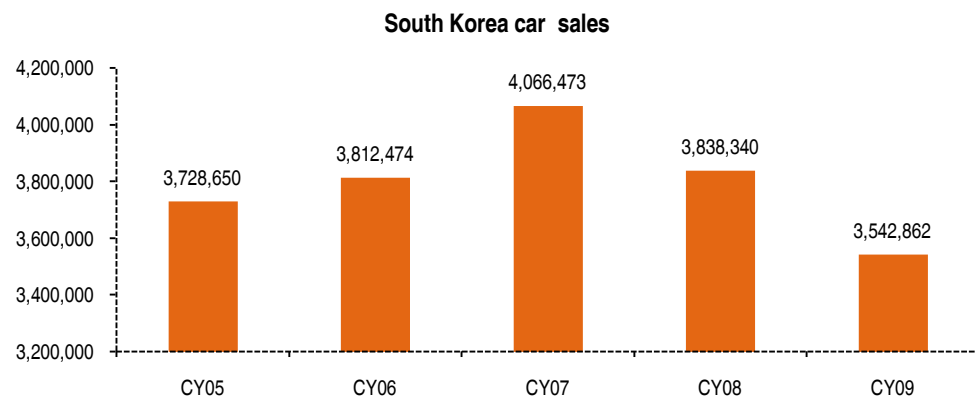
Exhibit 2: Ssangyong - P&L (Rs mn)				Exhibit 3: Ssangyong - Balance sheet (Rs mn)			
Particulars	CY07	CY08	CY09	Particulars	CY07	CY08	CY09
Sales	120,749	96,590	41,296	Current assets	32,317	23,792	15,591
Cost of sales	98,019	84,651	38,829	Cash and cash equivalents	20,908	9,604	7,301
Gross profit	22,730	11,939	2,467	Inventory	11,409	14,188	8,291
Gross profit (%)	19	12	6	Non- current assets	61,254	42,219	38,156
S&A expenses	21,023	20,741	13,826	Investments	1,142	1,822	1,992
Operating income	1,707	(8,802)	(11,358)	Property, plant	54,818	33,591	31,114
Other income	5,065	9,981	16,016	Intangible assets	3,661	5,229	3,980
Other expences	6,323	28,651	18,062	Others	1,632	1,577	1,070
Income before Income taxes expenses	449	(27,472)	(13,404)	Total assets	93,571	66,012	53,748
Tax expenses	1	-	-	Current liabilities	32,342	33,279	12,937
Net income	448	(27,472)	(13,404)	Non-current-liabilities	23,818	22,751	29,174
Source: Company, BRICS Research Note: Figures have been converted into Rs mn				Total liabilities	56,160	56,030	42,111
				Total shareholders' equity	37,411	9,982	11,637
				Total liabilities and shareholders' Equity	93,571	66,012	53,748
				Source: Company, BRICS Research Note: Figures have been converted into Rs mn			

### Ssangyong: Earlier sell off attempts unsuccessful

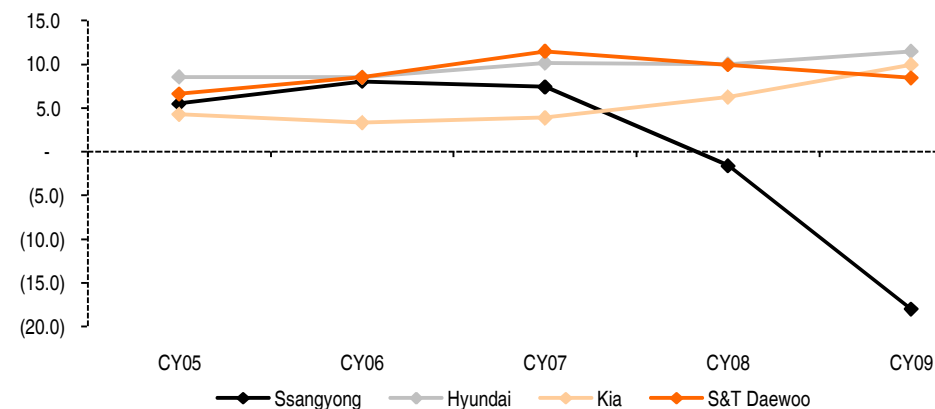
Ssangyong commenced business as a manufacturer of commercial vehicles such as trucks, buses, and special purpose vehicles including mixers and fire-fighting trucks in 1954. Ssangyong has 4,821 employees across two plants in South Korea. In terms of infrastructure, it has a R&D center, design center, and engine and rear axle manufacturing facilities. It acquired Keohwa Motors - specialising in manufacturing jeeps under the brand of Korando – in 1986 to enter the UV market. In early 1998, due to the economic downturn that affected all Asian countries, Ssangyong was merged with Daewoo Group. In 2000, after the crisis was over, the company separated from Daewoo Group and established itself as an independent automobile manufacturer again.

### South Korean auto market under pressure

Ssangyong holds 2% market share in the 3.5mn-vehicle South Korean auto market. Hyundai and Kia hold the largest share (80%). South Korean auto players face issues like (1) labour unrest in the country, (2) tightening of rules and regulations in South Korean credit markets, which have made it tough for consumers to get access to loans, and (3) declining exports as a result of global slowdown.

**Exhibit 4: South Korean car market shrinking...**

Source: Bloomberg, BRICS Research

**Exhibit 5: ...but large companies maintaining margins**

Source: Bloomberg, BRICS Research

**Exhibit 6: Peer valuation - South Korean auto companies**

Company	Market cap	Net sales		Net profit		EPS (Rs)		EV/EBIDTA		P/E (x)		Price/Sales	
		CY10E	CY11E	CY10E	CY11E	CY10E	CY11E	CY10E	CY11E	CY10E	CY11E	CY10E	CY11E
Ssangyong	19,156	70,180	79,222	(8,985)	(3,676)	(610)	(249)	42.9	5.1	N.A.	N.A.	0.3	0.2
Hyundai	1,142,605	1,326,208	1,390,441	142,663	152,932	545	583	5.9	5.6	9.5	8.9	0.9	0.8
Kia	495,647	776,004	811,985	58,486	64,474	150	162	7.5	7.1	8.5	7.8	0.6	0.6
S&T Daewoo	12,142	23,743	26,170	1,649	1,677	119	149	4.8	4.0	8.7	7.0	0.5	0.5

Source : Bloomberg

**INCOME STATEMENT (CONSOLIDATED)**

Y/E 31 March	2008	2009	2010	2011E	2012E
<b>Revenue</b>	<b>107,426</b>	<b>130,937</b>	<b>186,021</b>	<b>219,598</b>	<b>256,796</b>
Operating exp	100,519	120,032	156,511	186,058	219,492
<b>EBITDA</b>	<b>6,908</b>	<b>10,905</b>	<b>29,510</b>	<b>33,539</b>	<b>37,304</b>
Depreciation	2,387	2,915	3,708	4,242	4,772
<b>EBIT</b>	<b>4,521</b>	<b>7,990</b>	<b>25,802</b>	<b>29,298</b>	<b>32,532</b>
Other income	1,682	2,703	1,994	3,300	3,300
Interest paid	242	453	278	248	202
<b>PBT</b>	<b>5,960</b>	<b>10,241</b>	<b>27,518</b>	<b>32,350</b>	<b>35,630</b>
Tax	3,034	1,997	7,590	8,513	9,268
<b>APAT</b>	<b>1,356</b>	<b>8,346</b>	<b>20,835</b>	<b>23,837</b>	<b>26,362</b>
Minority interest	—	—	—	—	—
EO inc / (exp)	1,570	(103)	(908)	—	—
<b>PAT</b>	<b>2,926</b>	<b>8,244</b>	<b>19,928</b>	<b>23,837</b>	<b>26,362</b>
Shares o/s (mn nos)	578	578	578	578	578
Revenue growth (%)	8.8	21.9	42.1	18.0	16.9
PAT growth (%)	(72.6)	181.7	141.7	19.6	10.6
EBITDA margin (%)	6.4	8.3	15.9	15.3	14.5
<b>FDEPS (Rs) recurring</b>	<b>6.0</b>	<b>14.8</b>	<b>34.3</b>	<b>41.0</b>	<b>45.3</b>
<b>FDEPS (Rs) reported</b>	<b>5.1</b>	<b>14.3</b>	<b>34.5</b>	<b>41.2</b>	<b>45.6</b>

**BALANCE SHEET (CONSOLIDATED)**

Y/E 31 March	2008	2009	2010	2011E	2012E
<b>Net fixed assets</b>	<b>23,609</b>	<b>32,143</b>	<b>37,027</b>	<b>50,785</b>	<b>61,014</b>
<b>Investments</b>	<b>42,151</b>	<b>57,864</b>	<b>63,980</b>	<b>71,980</b>	<b>82,980</b>
<b>Current assets</b>	<b>36,444</b>	<b>50,629</b>	<b>60,424</b>	<b>58,571</b>	<b>62,884</b>
<b>Inventories</b>	<b>10,841</b>	<b>10,607</b>	<b>11,888</b>	<b>13,040</b>	<b>14,391</b>
Sundry debtors	10,049	10,437	12,581	14,640	17,120
Cash & bank balance	8,612	15,744	17,432	9,025	5,803
Loans & advances	6,942	13,842	18,523	21,866	25,570
<b>Total assets</b>	<b>102,339</b>	<b>140,762</b>	<b>161,472</b>	<b>181,378</b>	<b>206,919</b>
Networth	43,501	52,621	78,268	99,613	123,483
Share capital	2,431	2,792	2,910	2,910	2,910
Reserves & surplus	41,070	49,829	75,358	96,703	120,573
Minority interest	—	—	—	—	—
<b>Total debt</b>	<b>25,871</b>	<b>40,528</b>	<b>28,802</b>	<b>20,802</b>	<b>12,802</b>
Secured loans	19,698	30,718	18,992	10,992	2,992
Unsecured loans	6,173	9,810	9,810	9,810	9,810
<b>Current liabilities &amp; prov</b>	<b>32,400</b>	<b>48,159</b>	<b>51,931</b>	<b>58,491</b>	<b>68,163</b>
Current liabilities	22,966	35,383	33,965	49,576	58,492
Provisions	9,435	12,776	17,965	8,915	9,671
<b>Net deferred tax liab</b>	<b>567</b>	<b>(183)</b>	<b>2,403</b>	<b>2,403</b>	<b>2,403</b>
<b>Total liabilities</b>	<b>102,339</b>	<b>140,762</b>	<b>161,473</b>	<b>181,378</b>	<b>206,919</b>

**CASH FLOW STATEMENT (CONSOLIDATED)**

Y/E 31 March	2008	2009	2010	2011E	2012E
Net Profit	2,926	8,244	19,928	23,837	26,362
Depreciation	2,387	2,915	3,708	4,242	4,772
Amortisation	—	—	—	—	—
Interest paid	242	453	278	248	202
Chg in working capital	2,857	8,524	(4,119)	6	2,136
Other op activities	—	—	—	—	—
Cash flow from op (a)	8,412	20,135	19,795	28,333	33,472
Capital expenditure	(6,923)	(13,380)	(8,592)	(18,000)	(15,000)
Chg in investments	(19,776)	(15,714)	(6,116)	(8,000)	(11,000)
Other investing act	—	—	—	—	—
Cash flow from inv. (b)	(26,699)	(29,094)	(14,708)	(26,000)	(26,000)
Free cash flow (a+b)	1,489	6,755	11,203	10,333	18,472
Equity raised/(repaid)	959	7,077	4,244	—	—
Debt raised/(repaid)	9,511	14,657	(11,726)	(8,000)	(8,000)
Interest paid	(242)	(453)	(278)	(248)	(202)
Dividend (incl. tax)	(3,215)	(3,210)	(2,510)	(2,510)	(2,510)
Other fin. activities	6,617	(590)	3,517	—	—
Cash flow from fin. (c)	13,630	17,481	(6,752)	(10,758)	(10,711)
Net chg in cash (a+b+c)	(4,657)	8,522	(1,665)	(8,425)	(3,239)

**KEY RATIOS**

Y/E 31 March	2008	2009	2010	2011E	2012E
Raw material to sales	0.7	0.7	0.7	0.7	0.7
SGA to sales	—	—	—	—	—
Effective tax rate	50.9	19.5	27.6	26.3	26.0
Dividend yield (%)	2.0	1.7	1.3	1.3	1.3
ROE (%)	3.1	15.9	26.6	23.9	21.3
ROCE (%)	6.5	8.6	24.1	24.3	23.9
Net debt/Equity (%)	0.4	0.5	0.1	0.1	0.1
PAT margin (%)	2.7	6.3	10.7	10.9	10.3
Inventory (days)	36.8	29.6	23.3	21.7	20.5
Payable (days)	107.5	137.2	99.6	122.3	122.5
Receivable (days)	34	29	25	24	24

**VALUATIONS**

Y/E 31 March	2008	2009	2010	2011E	2012E
EV/op. cash flow (x)	42.1	18.0	17.6	12.3	10.3
PER (x)	96.9	39.5	17.1	14.3	12.9
PCE (x)	76.0	29.0	13.9	12.1	10.9
Price/Book (x)	7.8	6.4	4.3	3.4	2.7
EV/EBITDA (x)	51.5	33.3	11.9	10.4	9.3

#### BRICS RECOMMENDATION SCALE

<b>BUY:</b>	> 10% outperformance to Sector
<b>SELL:</b>	> 10% underperformance to Sector
<b>Outperform:</b>	0 to 10% outperformance to Sector
<b>Underperform:</b>	0 to 10% underperformance to Sector

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