

COMPANY UPDATE

Maruti Suzuki India (MRTI.BO)

Neutral

Equity Research

Cutting ests on continuing strike; longer term concerns on margins**What's changed**

1) Due to the persistent labour strike at Maruti Suzuki's Manesar plant and supplier Suzuki Power Train, we cut our volume estimates for Maruti Suzuki to 1.2mn units for FY12E (from 1.35mn), with further potential downside should the current impasse between labour and management continue beyond Oct'11. 2) We believe this will prevent the company from taking advantage of new capacity at Manesar in the face of demand uptick driven by a) seasonally strong festive season, and b) launch of new Swift model in Aug'11. 3) Due to lower volume estimates, we cut our FY12-14E EPS by 13-15% (revised estimates 20% below Bloomberg consensus), and 12-m FY13E P/E-based TP by 9% to Rs1,071 (from Rs 1,173).

Implications

1) Industry-wide – The Society of Indian Automobile Manufacturers believes rising instances of labour unrest in the industry (e.g. tool-down strikes at MRF Tyres and Bosch India over the last two months) are also due to restrictive employment regulations in India (source: CNBC TV18). As per a study published by the World Bank in Economic Times in Feb'07, there are 47 central laws and 157 state regulations dealing with labour markets, which are at times contradictory and overlapping, preventing efficient framing of employment contracts. **2) Company-specific** – Any worsening in labour disputes could potentially drive structural downside risk to Maruti Suzuki's margins from higher staff costs in the long run, in our view. Maruti Suzuki's current staff cost as a percentage of revenue is one of the lowest among peers in India and Asia.

Valuation

The stock is currently trading at 1.8x FY13E P/B vs global peers trading at 1.5x and 7-year historical average at 2.9x.

Key risks

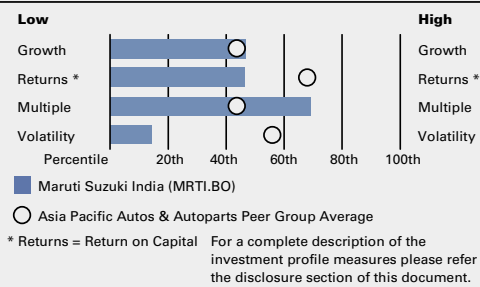
Greater/longer-than-expected impact of labour unrest and competition; interest rate cycle; volatility in commodity and currency markets.

INVESTMENT LIST MEMBERSHIP

Neutral

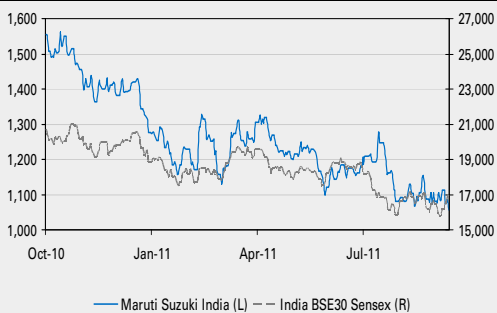
Coverage View: Neutral

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Investment Profile

| Key data | Current |
|------------------------------|---------------------|
| Price (Rs) | 1,056.40 |
| 12 month price target (Rs) | 1,071.00 |
| Market cap (Rs mn / US\$ mn) | 305,204.6 / 6,234.4 |
| Foreign ownership (%) | 30.6 |

| | 3/11 | 3/12E | 3/13E | 3/14E |
|---------------------------|--------------|--------------|--------------|--------------|
| EPS (Rs) New | 79.21 | 64.86 | 73.76 | 84.48 |
| EPS revision (%) | 0.0 | (15.4) | (15.3) | (12.7) |
| EPS growth (%) | (8.4) | (18.1) | 13.7 | 14.5 |
| EPS (dil) (Rs) New | 79.21 | 64.86 | 73.76 | 84.48 |
| P/E (X) | 13.3 | 16.3 | 14.3 | 12.5 |
| P/B (X) | 2.2 | 2.0 | 1.8 | 1.6 |
| EV/EBITDA (X) | 8.1 | 8.6 | 7.0 | 6.0 |
| Dividend yield (%) | 0.7 | 0.6 | 0.7 | 0.8 |
| ROE (%) | 18.0 | 12.7 | 12.9 | 13.2 |
| CROCI (%) | 23.8 | 14.2 | 14.0 | 13.8 |

Price performance chart

| Share price performance (%) | 3 month | 6 month | 12 month |
|-----------------------------|---------|---------|----------|
| Absolute | (9.1) | (17.3) | (32.0) |
| Rel. to India BSE30 Sensex | 0.1 | (3.5) | (16.7) |

Source: Company data, Goldman Sachs Research estimates, FactSet. Price as of 10/13/2011 close.

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Maruti Suzuki India: Summary Financials

| Profit model (Rs mn) | 3/11 | 3/12E | 3/13E | 3/14E | Balance sheet (Rs mn) | 3/11 | 3/12E | 3/13E | 3/14E |
|---|-------------------|-------------------|-------------------|-------------------|---------------------------------------|------------------|------------------|------------------|------------------|
| Total revenue | 361,281.9 | 344,098.5 | 405,733.6 | 469,913.7 | Cash & equivalents | 65,191.0 | 36,656.0 | 46,689.7 | 59,814.7 |
| Cost of goods sold | (308,331.0) | (298,394.6) | (351,946.9) | (406,352.9) | Accounts receivable | 8,933.0 | 14,141.0 | 16,674.0 | 19,311.5 |
| SG&A | (31,146.2) | (30,271.2) | (34,542.1) | (41,645.2) | Inventory | 14,150.0 | 17,552.6 | 20,702.8 | 23,903.1 |
| R&D | 0.0 | 0.0 | 0.0 | 0.0 | Other current assets | 15,395.0 | 15,395.0 | 15,395.0 | 15,395.0 |
| Other operating profit/(expense) | 7,812.0 | 5,679.1 | 6,526.4 | 7,433.4 | Total current assets | 103,669.0 | 83,744.6 | 99,461.4 | 118,424.4 |
| EBITDA | 39,751.7 | 31,666.3 | 37,625.5 | 41,491.5 | Net PP&E | 69,580.0 | 104,025.5 | 112,171.0 | 120,028.4 |
| Depreciation & amortization | (10,135.0) | (10,554.5) | (11,854.5) | (12,142.6) | Net intangibles | 0.0 | 0.0 | 0.0 | 0.0 |
| EBIT | 29,616.7 | 21,111.8 | 25,771.0 | 29,348.9 | Total investments | 10,961.0 | 10,961.0 | 10,961.0 | 10,961.0 |
| Interest income | 0.0 | 0.0 | 0.0 | 0.0 | Other long-term assets | 0.0 | 0.0 | 0.0 | 0.0 |
| Interest expense | (244.0) | (133.5) | (133.5) | (133.5) | Total assets | 184,210.0 | 198,731.1 | 222,593.4 | 249,413.7 |
| Income/(loss) from uncons. subs. | 0.0 | 0.0 | 0.0 | 0.0 | Accounts payable | 29,495.0 | 27,339.3 | 32,236.4 | 37,335.6 |
| Others | 1,715.0 | 4,476.0 | 3,309.6 | 3,937.9 | Short-term debt | 312.0 | 312.0 | 312.0 | 312.0 |
| Pretax profits | 31,087.7 | 25,454.2 | 28,947.1 | 33,153.4 | Other current liabilities | 11,303.0 | 11,303.0 | 11,303.0 | 11,303.0 |
| Income tax | (8,202.0) | (6,715.7) | (7,637.2) | (8,747.0) | Total current liabilities | 41,110.0 | 38,954.3 | 43,851.4 | 48,950.6 |
| Minorities | 0.0 | 0.0 | 0.0 | 0.0 | Long-term debt | 2,781.0 | 2,781.0 | 2,781.0 | 2,781.0 |
| Net income pre-preferred dividends | 22,885.7 | 18,738.5 | 21,309.9 | 24,406.4 | Other long-term liabilities | 1,644.0 | 1,644.0 | 1,644.0 | 1,644.0 |
| Preferred dividends | 0.0 | 0.0 | 0.0 | 0.0 | Total long-term liabilities | 4,425.0 | 4,425.0 | 4,425.0 | 4,425.0 |
| Net income (pre-exceptionals) | 22,885.7 | 18,738.5 | 21,309.9 | 24,406.4 | Total liabilities | 45,535.0 | 43,379.3 | 48,276.4 | 53,375.6 |
| Post-tax exceptionals | 0.0 | 0.0 | 0.0 | 0.0 | Preferred shares | 0.0 | 0.0 | 0.0 | 0.0 |
| Net income | 22,885.7 | 18,738.5 | 21,309.9 | 24,406.4 | Total common equity | 138,675.0 | 155,351.8 | 174,317.1 | 196,038.1 |
| EPS (basic, pre-exception) (Rs) | 79.21 | 64.86 | 73.76 | 84.48 | Minority interest | 0.0 | 0.0 | 0.0 | 0.0 |
| EPS (basic, post-exception) (Rs) | 79.21 | 64.86 | 73.76 | 84.48 | Total liabilities & equity | 184,210.0 | 198,731.1 | 222,593.4 | 249,413.7 |
| EPS (diluted, post-exception) (Rs) | 79.21 | 64.86 | 73.76 | 84.48 | BVPS (Rs) | 479.99 | 537.72 | 603.36 | 678.54 |
| DPS (Rs) | 7.50 | 6.14 | 6.98 | 8.00 | | | | | |
| Dividend payout ratio (%) | 9.5 | 9.5 | 9.5 | 9.5 | | | | | |
| Free cash flow yield (%) | 2.5 | (10.5) | 2.6 | 3.4 | | | | | |
| Growth & margins (%) | 3/11 | 3/12E | 3/13E | 3/14E | Ratios | 3/11 | 3/12E | 3/13E | 3/14E |
| Sales growth | 24.8 | (4.8) | 17.9 | 15.8 | CROCI (%) | 23.8 | 14.2 | 14.0 | 13.8 |
| EBITDA growth | 0.5 | (20.3) | 18.8 | 10.3 | ROE (%) | 18.0 | 12.7 | 12.9 | 13.2 |
| EBIT growth | (5.4) | (28.7) | 22.1 | 13.9 | ROA (%) | 12.9 | 9.8 | 10.1 | 10.3 |
| Net income growth | (8.4) | (18.1) | 13.7 | 14.5 | ROACE (%) | 38.7 | 19.0 | 17.0 | 18.1 |
| EPS growth | (8.4) | (18.1) | 13.7 | 14.5 | Inventory days | 15.7 | 19.4 | 19.8 | 20.0 |
| Gross margin | 14.7 | 13.3 | 13.3 | 13.5 | Receivables days | 11.1 | 12.2 | 13.9 | 14.0 |
| EBITDA margin | 11.0 | 9.2 | 9.3 | 8.8 | Payable days | 39.1 | 34.8 | 30.9 | 31.2 |
| EBIT margin | 8.2 | 6.1 | 6.4 | 6.2 | Net debt/equity (%) | (44.8) | (21.6) | (25.0) | (28.9) |
| | | | | | Interest cover - EBIT (X) | 121.4 | 158.2 | 193.1 | 219.9 |
| Cash flow statement (Rs mn) | 3/11 | 3/12E | 3/13E | 3/14E | Valuation | 3/11 | 3/12E | 3/13E | 3/14E |
| Net income pre-preferred dividends | 22,885.7 | 18,738.5 | 21,309.9 | 24,406.4 | P/E (analyst) (X) | 13.3 | 16.3 | 14.3 | 12.5 |
| D&A add-back | 10,135.0 | 10,554.5 | 11,854.5 | 12,142.6 | P/B (X) | 2.2 | 2.0 | 1.8 | 1.6 |
| Minorities interests add-back | 0.0 | 0.0 | 0.0 | 0.0 | EV/EBITDA (X) | 8.1 | 8.6 | 7.0 | 6.0 |
| Net (inc)/dec working capital | 3,384.0 | (10,766.3) | (786.0) | (738.7) | EV/GCI (X) | 2.3 | 1.4 | 1.2 | 1.0 |
| Other operating cash flow | (4,695.7) | (5,544.2) | (4,397.7) | (5,372.1) | Dividend yield (%) | 0.7 | 0.6 | 0.7 | 0.8 |
| Cash flow from operations | 31,709.0 | 12,982.5 | 27,980.6 | 30,438.2 | | | | | |
| Capital expenditures | (22,078.0) | (45,000.0) | (20,000.0) | (20,000.0) | | | | | |
| Acquisitions | 0.0 | 0.0 | 0.0 | 0.0 | | | | | |
| Divestitures | 0.0 | 5,544.2 | 4,397.7 | 5,372.1 | | | | | |
| Others | 21,328.0 | 0.0 | 0.0 | 0.0 | | | | | |
| Cash flow from investments | (750.0) | (39,455.8) | (15,602.3) | (14,627.9) | | | | | |
| Dividends paid (common & pref) | (1,733.0) | (2,061.7) | (2,344.6) | (2,685.3) | | | | | |
| Inc/(dec) in debt | (5,123.0) | 0.0 | 0.0 | 0.0 | | | | | |
| Common stock issuance (repurchase) | 0.0 | 0.0 | 0.0 | 0.0 | | | | | |
| Other financing cash flows | (27,824.0) | 0.0 | 0.0 | 0.0 | | | | | |
| Cash flow from financing | (34,680.0) | (2,061.7) | (2,344.6) | (2,685.3) | | | | | |
| Total cash flow | (3,721.0) | (28,535.0) | 10,033.7 | 13,125.0 | | | | | |

Note: Last actual year may include reported and estimated data.

Source: Company data, Goldman Sachs Research estimates.

Analyst Contributors

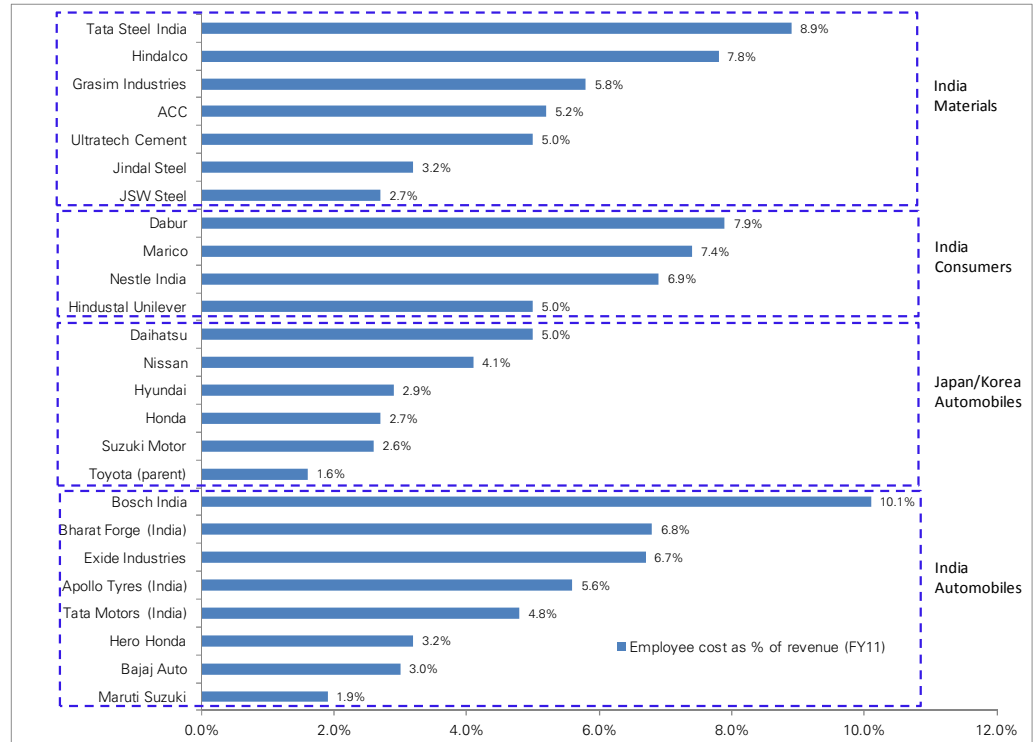
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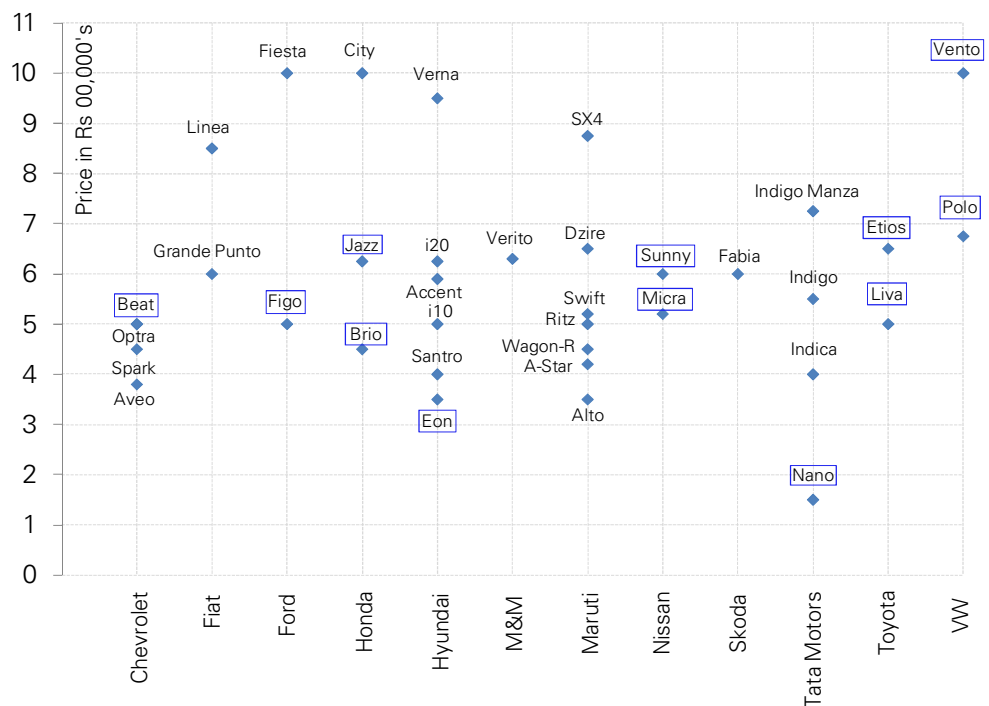
Exhibit 1: We note that Maruti Suzuki's employee cost as percentage of revenues is one of the lowest among large Indian manufacturing and Asian auto peers in our coverage



Source: Company data.

Exhibit 2: The company is also facing a structural increase in competition in the Indian passenger car market

Player-wise model and price (new competitor launches over 2010-2011 highlighted in blue box)



Source: Company data, Autocar India, Goldman Sachs Research.

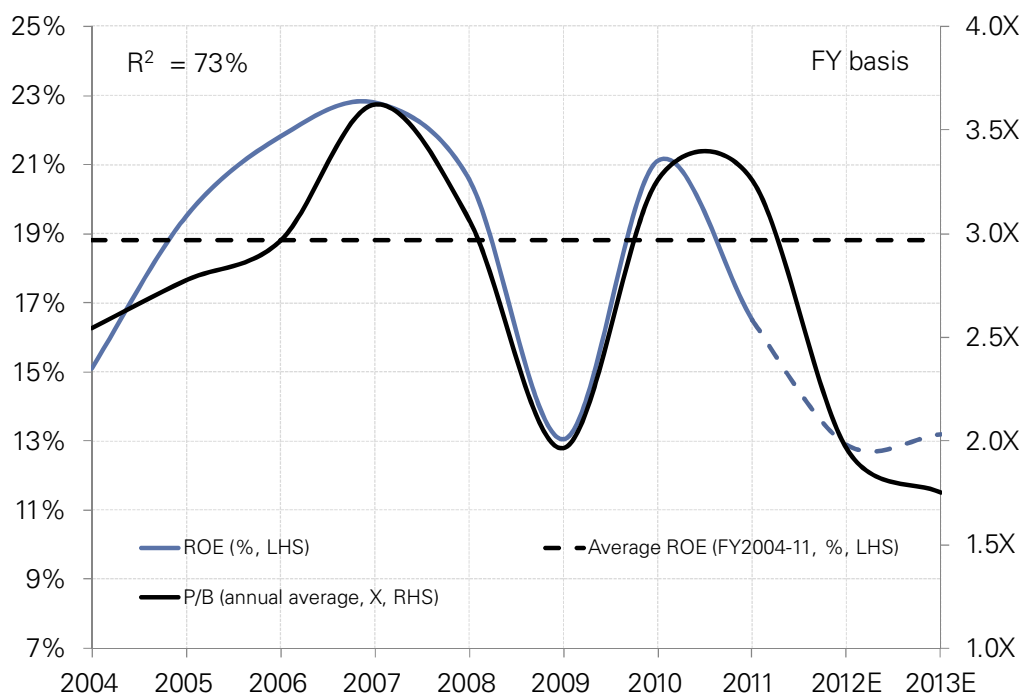
Exhibit 3: Summary of changes to our estimates for Maruti Suzuki

| FY 2012E | | | |
|-----------------|---------|--------|--------|
| Rs mn | Revenue | EBITDA | NI |
| Old | 380,345 | 36,287 | 22,140 |
| Revised | 344,098 | 31,666 | 18,739 |
| Estimate Change | -10% | -13% | -15% |
| YOY Growth % | -5% | -20% | -18% |
| FY 2013E | | | |
| Rs mn | Revenue | EBITDA | NI |
| Old | 448,474 | 42,655 | 25,164 |
| Revised | 405,734 | 37,626 | 21,310 |
| Estimate Change | -10% | -12% | -15% |
| YOY Growth % | 18% | 19% | 14% |
| FY 2014E | | | |
| Rs mn | Revenue | EBITDA | NI |
| Old | 510,276 | 45,947 | 27,971 |
| Revised | 469,914 | 41,492 | 24,406 |
| Estimate Change | -8% | -10% | -13% |
| YOY Growth % | 16% | 10% | 15% |

Source: Goldman Sachs Research estimates.

Exhibit 4: The stock is already trading at trough P/B multiple, but with significantly lower FY12-13E RoE compared with historical average

Historical P/B vs RoE, FY2004-13E



Source: Company data, Datastream, Goldman Sachs Research estimates.

Reg AC

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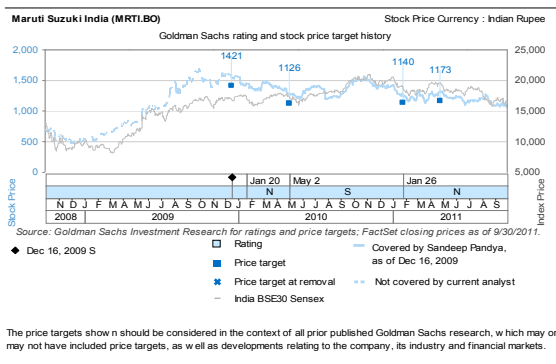
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|--------|---------------------|------|------|----------------------------------|------|------|
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Price target and rating history chart(s)



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