

BAJAJ AUTO*Growth trajectory maintained*

- PAT marginally ahead of estimates**

Bajaj Auto's (BAL) Q2FY11 PAT of INR 6.8 bn was 4% ahead of our estimate of INR 6.6 bn. The variance was on account of higher-than-expected revenue, which benefited from a 4% sequential increase in realizations per vehicle.

- Net revenue jumps 50% Y-o-Y**

The company's net revenue, at INR 43.4 bn (up 50% Y-o-Y) was driven by the volume growth with total units sold crossing the 1-mn mark (motorcycle sales increasing 47% Y-o-Y; three wheeler sales registering 37% Y-o-Y growth) during the quarter. Further, the healthy revenue growth was aided by improvement in average realisation per vehicle (up ~3% Y-o-Y and Q-o-Q) largely on account of better product mix (higher proportion of three wheelers and lower proportion of the low end *Platina* in volumes) along with a marginal price hike.

- EBITDA margins, at 20.7%, up 70bps Q-o-Q**

BAL's EBITDA margins, at 20.7%, jumped 70bps sequentially on the back of marginal decline in commodity prices, better operating leverage, and a better product mix. This was broadly in line with our estimate of 20.5%. Other non operating income rose 3% Q-o-Q and 285% Y-o-Y led by increasing liquid investments (up INR 5.7 bn over FY10). Overall net profit at INR 6.8 bn (Edelweiss estimate at INR 6.5 bn) increased 70% Y-o-Y and 16% Q-o-Q.

- FY11 volume guidance maintained at 4 mn units**

Management has reiterated its guidance for FY11 at 4 mn units (3.6 mn two wheelers, 0.4 mn three wheelers). Capacity constraints could ease post the festival season. For FY12, capacity will be increased to 5.0 mn units (from 4.3 mn). The company expects pressure on EBITDA margins in H2FY11 on account of higher commodity prices, stronger conversion costs from auto ancillaries, and increased promotion expenses in Q4FY11. For FY11, BAL has maintained EBITDA margin of 20% (versus 20.3% in H1FY11).

- Outlook and valuations: Positive; maintain 'HOLD'**

At CMP of INR 1,514, the stock is trading at 18.0x FY11E and 15.5x FY12E revised earnings of INR 85 and INR 98, respectively. Hence, while the outlook remains positive, we maintain 'HOLD' recommendation on the stock with a target price of INR 1,570 i.e., 16x FY12E. On a relative return basis we rate the stock 'Sector Performer'.

October 19, 2010

Reuters: BAJA.BO Bloomberg: BJAUT IN

EDELWEISS 4D RATINGS

Absolute Rating	HOLD
Rating Relative to Sector	Performer
Risk Rating Relative to Sector	High
Sector Relative to Market	Equalweight

Note:
Please refer last page of the report for rating explanation

MARKET DATA

CMP	:	INR 1,514
52-week range (INR)	:	1,615 / 683
Share in issue (mn)	:	289.4
M cap (INR bn/USD mn)	:	438 /9,901
Avg. Daily Vol. BSE/NSE ('000):	:	601.0

SHARE HOLDING PATTERN (%)

Promoters*	:	49.7
MFs, FIs & Banks	:	6.1
FIIIs	:	18.6
Others	:	25.6
* Promoters pledged shares (% of share in issue)	:	0.9

PRICE PERFORMANCE (%)

	Stock	Nifty	EW Auto Index
1 month	5.1	3.2	6.8
3 months	26.2	12.6	17.3
12 months	107.0	18.2	46.5

Financials**(INR mn)**

Year to March	Q2FY11	Q2FY10	% Chg	Q1FY11	% Chg	FY10	FY11E
Net revenues	43,418	28,875	50.4	38,901	11.6	118,106	165,302
EBITDA	8,972	6,365	41.0	7,769	15.5	24,822	31,902
Adjusted net profit	6,821	4,487	52.0	5,902	15.6	18,651	24,679
Diluted P/E (x)						23.5	17.8
EV/EBITDA (x)						16.5	12.5
ROACE (%)						60.4	53.9

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- Key takeaways from conference call

Capacity constraints to resolve post festive season

Management indicated that post the festival season capacity constraints are likely to ease. To meet the underlying demand trend, BAL will be raising total capacity from the current 4.3 mn units to 5.0 mn by March 2011.

Table 1: Capacity expansion

Plant	Products	2009-10	2010-11
Waluj (Aurangabad)	Motor Cycles	1,500,000	1,500,000
Waluj (Aurangabad)	Three wheeers	420,000	500,000
Chakan (Pune)	Motor Cycles	1,200,000	1,200,000
Pantnagar (Uttarakhand)	Motor Cycles	1,200,000	1,800,000
		4,320,000	5,000,000

Source: Company, Edelweiss research

Comfortable on exports front

For H2FY11, the company has hedged 90% of its exports at the exchange rate of INR47.5/USD. Further, for FY12, as indicated by the management, 70% of exports are hedged at INR46.5/USD. With exports contributing ~35% to revenues, the exchange rates/ hedges materially impact the company's profitability.

Table 2: Volume analysis

Year to March	Q2FY11	Q2FY10	% change	Q1FY11	% change	Edel Comments
Total two Wheelers	883,472	601,481	46.9	828,418	6.6	Strong volumes of Pulsar and Discover
Three wheelers	117,076	85,246	37.3	99,918	17.2	Led by city and semi-urban markets, particularly Tamil nadu
Total units sold (nos)	1,000,548	686,727	45.7	928,336	7.8	
Exports(of the above)	307,332	224,334	37.0	323,899	(5.1)	Growth driven by South Asia and African markets
Realisation (INR)	41,786	40,674	2.7	40,258	3.8	Led by better product mix and price hikes.

Financial analysis

Year to March	Q2FY11	Q2FY10	% change	Q1FY11	% change	Edel Comments
Total revenues	43,418	28,875	50.4	38,901	11.6	Marginally higher than our estimates by 2.5%
Raw material	30,712	19,124	60.6	27,682	10.9	Decline in metal costs partially offset by rise in conversion costs
Staff costs	1,142	1,074	6.3	1,264	(9.7)	
Other expenses	2,618	2,346	11.6	2,195	19.3	Higher on account of interest subvention expenses and one off losses
Less: Expenses capitalisec	(25)	(34)	26.9	(9)	(174.4)	
Total expenditure	34,447	22,510	53.0	31,131	10.6	
EBIDTA	8,972	6,365	41.0	7,769	15.5	Limited benefit of operating leverage flowing through
Interest	7	0	-	6	3.2	
Depreciation	300	336	(10.8)	318	(5.9)	Depreciation declines on incrementally lower capex
Other income	837	217	285.2	817	2.5	On higher treasury income
PBT	9,503	6,247	52.1	8,262	15.0	
Tax	2,682	1,760	52.4	2,360	13.6	
Adjusted net profit	6,821	4,487	52.0	5,902	15.6	
Extraordinary exp	0	458	(100.0)	0	-	
Net profit	6,821	4,028	69.3	5,902	15.6	4% above Edel estimates

Margin analysis**As % of net revenues**

Year to March	Q2FY11	Q2FY10	% change	Q1FY11	% change	Edel Comments
Raw material	70.7	66.2	451	71.2	(42.5)	Improved on declining commodity prices
Staff costs	2.6	3.7	(109)	3.2	(62.0)	
Other expenses	6.0	8.1	(210)	5.6	38.8	
EBIDTA	20.7	22.0	(138)	20.0	69.1	Margins in line with estimates
Adjusted net profit	15.7	15.5	17	15.2	53.9	
Tax rate	28.2	28.2	5	28.6	(34.3)	To be maintained in the range of 28%

Source: Company, Edelweiss research

Financial snapshot							(INR mn)		
Year to March	Q2FY11	Q2FY10	% Change	Q1FY11	% Change	FY10	FY11E	FY12E	
Two-wheelers	883,472	601,481	46.9	828,418	6.6	2,511,696	3,489,906	3,961,721	
Three-wheelers	117,076	85,246	37.3	99,918	17.2	340,914	441,517	485,669	
Total units sold (nos)	1,000,548	686,727	45.7	928,336	7.8	2,852,610	3,931,423	4,447,390	
Exports	307,332	224,334	37.0	323,899	(5.1)	891,098	1,145,457	1,305,322	
Realization	41,786	40,674	2.7	40,258	3.8	40,344	41,130	41,640	
Net revenues	43,418	28,875	50.4	38,901	11.6	118,106	165,302	189,149	
Raw material costs	30,712	19,124	60.6	27,682	10.9	80,704	113,191	130,187	
Staff costs	1,142	1,074	6.3	1,264	(9.7)	3,995	6,468	7,517	
Expenses capitalized	(25)	(34)	NA	(9)	NA	(157)	(165)	(173)	
Other expenses	2,618	2,346	11.6	2,195	19.3	8,742	13,906	15,926	
Total expenditure	34,447	22,510	53.0	31,131	10.6	93,284	133,400	153,457	
EBITDA	8,972	6,365	41.0	7,769	15.5	24,822	31,902	35,692	
Depreciation	300	336	(10.8)	318	(5.9)	1,365	1,516	1,675	
Other income	837	217	285.2	817	2.5	2,329	3,947	5,293	
Interest	7	-		6	3.2	60	57	55	
Profit before tax	9,503	6,247	52.1	8,262	15.0	25,726	34,277	39,256	
Tax	2,682	1,760	52.4	2,360	13.6	7,075	9,597	10,992	
Extraordinary items	-	458	(100.0)	-		1,650	-	-	
Reported net profit	6,821	4,028	69.3	5,902	15.6	17,001	24,679	28,264	
Adjusted net profit	6,821	4,487	52.0	5,902	15.6	18,651	24,679	28,264	
Equity capital	2,894	2,894		2,894		2,894	2,894	2,894	
No. of shares (mn)	289	289		289		289	289	289	
Adj. EPS (INR)	23.6	15.5		20.4		64.5	85.3	97.7	
Reported eps (INR)	23.6	13.9		20.4		58.8	85.3	97.7	
ROACE (%)	-	-		-		60.4	53.9	44.6	

As % of net revenues

Raw material	70.7	66.2		71.2		68.3	68.5	68.8
Employee cost	2.6	3.7		3.2		3.4	3.9	4.0
Other expenditure	6.0	8.1		5.6		7.4	8.4	8.4
EBITDA	20.7	22.0		20.0		21.0	19.3	18.9
Adjusted net profit	15.7	15.5		15.2		15.8	14.9	14.9
Tax rate	28.2	28.2		28.6		27.5	28.0	28.0

- **Company Description**

BAL is the second largest two-wheeler manufacturer in India with a domestic market share of 28%. It offers products in all motorcycle segments—Platina (entry), Discover (executive) and Pulsar (premium). It is also the largest three-wheeler manufacturer in India. Post the demerger in May 2008, BAL has been solely focused on the automobile business. In the past few years, the company has shown strong growth in exports that now forms nearly 40% of its total volumes.

- **Investment Theme**

BAL has substantially improved its marketshare and profitability in the past few quarters. The company's new models—notably the executive level motorcycle, Discover—have been extremely well received. Exports have been robust. With a reasonably strong product portfolio we expect the company's volumes to be on a growth trajectory. However, with the stock trading at ~16x FY12E EPS, we believe the positives have been adequately priced in.

- **Key Risks**

Stronger than expected volume growth with incremental marketshare gains would lead to an upside to our EPS estimates and target price. The company might also be a beneficiary of a split between the joint venture partner in Hero Honda. On the negative side, an appreciation in the INR vis- a – vis the USD and an increase in competitive intensity from new players (such as M&M) pose a downside risk to our estimates.

Financial Statements

Income statement					(INR mn)
Year to March	FY08	FY09	FY10	FY11E	FY12E
Total volume (nos)	2,451,228	2,194,108	2,852,610	3,931,423	4,447,390
<i>% Growth</i>		(10)	30	38	13
Income from operations	88,286	86,963	118,106	165,302	189,149
Materials costs	66,204	64,635	80,704	113,191	130,187
Manufacturing expenses	747	605	672	970	1,111
Staff costs	3,416	3,544	3,995	6,468	7,517
S G & A expenses	7,390	7,544	8,070	12,936	14,815
Less: Expenses capitalised	230	144	157	165	173
Total operating expenses	77,526	76,183	93,284	133,400	153,457
EBITDA	10,760	10,780	24,822	31,902	35,692
Depreciation and amortisation	1,740	1,298	1,365	1,516	1,675
EBIT	9,020	9,482	23,457	30,386	34,017
Interest	52	210	60	57	55
Non-Operational income	3,402	2,360	2,329	3,947	5,293
Profit before tax	12,371	11,632	25,726	34,277	39,256
Provision for tax	3,788	3,016	7,075	9,597	10,992
Current taxes	3,961	3,084	7,126	9,597	10,992
Deferred taxes	(173)	(68)	(51)	0	0
Adjusted profit	8,583	8,616	18,651	24,679	28,264
Prior period adjustments (net)	(2)	(20)	(9)	0	0
Extraordinary income/ (loss)	(1,024)	(2,051)	(1,641)	0	0
Reported Profit after tax	7,557	6,545	17,001	24,679	28,264
Shares outstanding	289	289	289	289	289
Adjusted Earnings per share (EPS)	29.7	29.8	64.5	85.3	97.7
Diluted shares outstanding	289	289	289	289	289
Adjusted Diluted EPS	29.7	29.8	64.5	85.3	97.7
Cash EPS	35.1	34.0	69.0	90.5	103.5
Dividend per share	10.0	11.0	20.0	11.0	11.0
Dividend payout (%)	38.3	48.6	34.0	12.9	11.3

Common size metrics- as % of net revenues

Year to March	FY08	FY09	FY10	FY11E	FY12E
Operating expenses	87.8	87.6	79.0	80.7	81.1
Materials costs	75.0	74.3	68.3	68.5	68.8
Staff costs	3.9	4.1	3.4	3.9	4.0
S G & A expenses	8.4	8.7	6.8	7.8	7.8
Depreciation	2.0	1.5	1.2	0.9	0.9
Interest expenditure	0.1	0.2	0.1	0.0	0.0
EBITDA margins	12.2	12.4	21.0	19.3	18.9
Net profit margins	9.7	9.9	15.8	14.9	14.9

Growth metrics (%)

Year to March	FY08	FY09	FY10	FY11E	FY12E
Revenues		(1.5)	35.8	40.0	14.4
EBITDA		0.2	130.3	28.5	11.9
PBT		(6.0)	121.2	33.2	14.5
Adjusted Net profit		0.4	116.5	32.3	14.5
Adjusted EPS		0.4	116.5	32.3	14.5

Balance sheet**(INR mn)**

As on 31st March	FY08	FY09E	FY10	FY11E	FY12E
Equity capital	1,447	1,447	1,447	2,894	2,894
Reserves & surplus	14,429	17,250	27,837	47,345	71,885
Shareholders funds	15,876	18,697	29,283	50,239	74,779
Secured loans	70	0	130	130	130
Unsecured loans	13,273	15,700	13,256	13,256	13,256
Borrowings	13,342	15,700	13,386	13,386	13,386
Deferred tax (Net)	110	42	17	17	17
Deferred tax liability	1,419	1,648	1,918	1,918	1,918
Deferred tax assests	1,310	1,606	1,901	1,901	1,901
Sources of funds	29,328	34,439	42,686	63,641	88,181
Gross block	29,842	33,339	33,793	36,708	41,208
Depreciation	17,261	18,079	18,997	20,512	22,188
Net block	12,581	15,260	14,796	16,196	19,021
Capital work in progress	347	221	415	0	0
Technical know-how	105	163	0	0	0
Investments	18,571	18,085	40,215	50,048	72,486
Inventories	3,496	3,388	4,462	6,202	7,103
Sundry debtors	2,753	3,587	2,728	5,759	6,088
Cash and bank balance	561	1,369	1,014	1,617	1,852
Loans and advances	9,686	14,909	21,805	22,895	22,895
Other current assets	0	0	0	0	0
Total current assets	16,496	23,253	30,009	36,474	37,938
Sundry creditors	8,788	8,000	15,712	15,063	17,250
Others current liabilities	1,645	4,134	4,551	4,551	4,551
Provisions	8,340	12,242	22,487	19,463	19,463
Total current liab. & provisions	18,773	24,376	42,750	39,076	41,263
Net current assets	(2,277)	(1,123)	(12,740)	(2,602)	(3,325)
Misc expenditure	0	1,833	0	0	0
Uses of funds	29,328	34,439	42,686	63,641	88,181
Book value per share (BV) (INR)	55	58	101	174	258

Free cash flow

Year to March	FY08	FY09	FY10	FY11E	FY12E
Net profit		6,546	17,001	24,679	28,264
Depreciation		1,298	1,365	1,516	1,675
Deferred tax		(68)	(51)	0	0
Others		68	51	0	0
Gross cash flow		7,843	18,365	26,195	29,939
Less: Changes in WC		684	(8,238)	6,511	(958)
Operating cash flow		7,159	26,603	19,684	30,897
Less: Capex		3,908	933	2,500	4,500
Free cash flow		3,251	25,671	17,184	26,397

Cash flow metrics

Year to March	FY08	FY09	FY10	FY11E	FY12E
Operating cash flow		7,159	26,603	19,684	30,897
Financing cash flow		(1,028)	(6,038)	(6,749)	(3,724)
Investing cash flow		(3,422)	(23,063)	(12,332)	(26,938)
Net cash flow		2,709	(2,497)	603	235
Capex		(3,908)	(933)	(2,500)	(4,500)
Dividend paid		(3,386)	(3,724)	(6,749)	(3,724)

Profitability & liquidity ratios

Year to March	FY08	FY09	FY10	FY11E	FY12E
ROAE (%)	54.1	52.6	80.8	62.1	45.2
ROACE (%)	42.4	34.4	60.4	53.9	44.6
Inventory days	19	19	20	20	20
Debtors days	11	15	8	13	12
Payable days	41	38	61	41	41
Cash conversion cycle (days)	(11)	(4)	(33)	(8)	(9)
Current ratio	0.9	1.0	0.7	0.9	0.9
Debt/EBITDA	1.2	1.5	0.5	0.4	0.4
Fixed asset turnover (x)	3.0	2.6	3.5	4.5	4.6
Debt/Equity	0.8	0.8	0.5	0.3	0.2
Adjusted debt/equity	0.8	0.8	0.5	0.3	0.2

Operating ratios

Year to March	FY08	FY09	FY10	FY11E	FY12E
Total asset turnover	3.0	2.7	3.1	3.1	2.5
Fixed asset turnover	7.0	6.2	7.9	10.7	10.7
Equity turnover	5.6	5.0	4.9	4.2	3.0

Du pont analysis

Year to March	FY08	FY09	FY10	FY11E	FY12E
NP margin (%)	9.7	9.9	15.8	14.9	14.9
Total assets turnover	3.0	2.7	3.1	3.1	2.5
Leverage multiplier	1.8	1.9	1.7	1.3	1.2
ROAE (%)	54.1	52.6	80.8	62.1	45.2

Valuations parameters

Year to March	FY08	FY09	FY10	FY11E	FY12E
Adjusted EPS (INR)	29.7	29.8	64.5	85.3	97.7
Y-o-Y growth (%)	0.0	0.4	116.5	32.3	14.5
CEPS (INR)	35.1	34.0	69.0	90.5	103.5
Adjusted P/E (x)	51.0	50.8	23.5	17.8	15.5
Price/BV (x)	27.6	26.0	15.0	8.7	5.9
EV/Sales (x)	4.9	5.0	3.5	2.4	2.0
EV/EBITDA (x)	40.2	40.3	16.5	12.5	10.6
Dividend yield (%)	0.7	0.7	1.3	0.7	0.7



Company	Absolute reco	Relative reco	Relative risk	Company	Absolute reco	Relative reco	Relative Risk
Ashok Leyland	BUY	SO	M	Bajaj Auto	HOLD	SP	H
Hero Honda Motors Ltd	BUY	SO	L	Mahindra & Mahindra Ltd	BUY	SO	M
Maruti Suzuki India Ltd	HOLD	SU	L	Tata Motors Ltd	BUY	SO	H

ABSOLUTE RATING

Ratings	Expected absolute returns over 12 months
Buy	More than 15%
Hold	Between 15% and - 5%
Reduce	Less than -5%

RELATIVE RETURNS RATING

Ratings	Criteria
Sector Outperformer (SO)	Stock return > 1.25 x Sector return
Sector Performer (SP)	Stock return > 0.75 x Sector return
	Stock return < 1.25 x Sector return
Sector Underperformer (SU)	Stock return < 0.75 x Sector return

Sector return is market cap weighted average return for the coverage universe within the sector

RELATIVE RISK RATING

Ratings	Criteria
Low (L)	Bottom 1/3rd percentile in the sector
Medium (M)	Middle 1/3rd percentile in the sector
High (H)	Top 1/3rd percentile in the sector

Risk ratings are based on Edelweiss risk model

SECTOR RATING

Ratings	Criteria
Overweight (OW)	Sector return > 1.25 x Nifty return
Equalweight (EW)	Sector return > 0.75 x Nifty return
	Sector return < 1.25 x Nifty return
Underweight (UW)	Sector return < 0.75 x Nifty return

Edelweiss
Ideas create, values protect



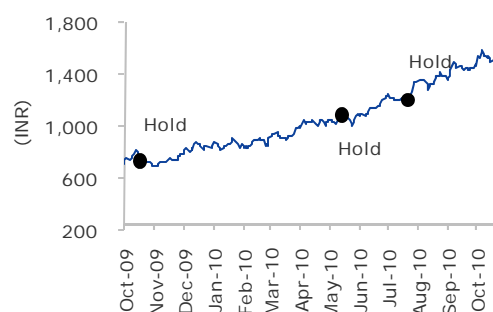
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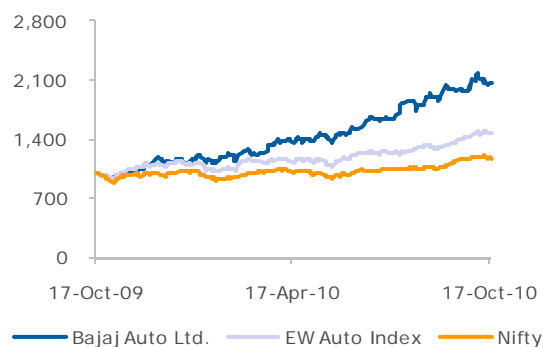
Coverage group(s) of stocks by primary analyst(s): Automobiles

Ashok Leyland, Bajaj Auto, Hero Honda Motors Ltd, Mahindra & Mahindra Ltd, Maruti Suzuki India Ltd, Tata Motors Ltd

Bajaj Auto



EW Indices



Distribution of Ratings / Market Cap

Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution*	116	45	12	176
* 3 stocks under review				
	> 50bn	Between 10bn and 50 bn	< 10bn	
Market Cap (INR)	110	53	13	

Recent Research

Date	Company	Title	Price (INR)	Recos
01-Oct-10	Auto Sales Update	Omens of a strong festival season; <i>Monthly Update</i>		
14-Sep-10	Ashok Leyland	Growth on track; <i>Company Update</i>	77	Buy
01-Sep-10	Auto Sales Update	Robust trends sustain; <i>Monthly Update</i>		

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