Company

23 July 2009 | 10 pages

Maruti Suzuki India (MRTI.BO)

Equity

Hold: 1QFY10 Results – Overall, a Solid Quarter

- **Recurring PAT was above expectations** — at Rs 5.84 bn, up 25% y/y and 38% above our expectations. This quarter had everything – volume growth, market share gains, mix improvement and margin expansion. EBITDA margins at 10.4% (+60 bps y/y, 390 bps q/q), were 140 bps above our estimates.
- **Exports/mix shift drove realizations** — 1) Realizations rose 4% sequentially, due to a richer product mix and a 17% q/q increase in exports. We got our export realizations wrong – they are c12% higher than our expectations, a quick sensitivity reveals that FY10 estimates could be increased by cRs7/share if export realizations remain at current levels (ceteris paribus).
- **Costs/FX move in the same direction** — Material costs as a % of sales declined 270 bps q/q; MSIL also benefited from the rupee strengthening against the yen (~60bps benefit on margins).
- **Cash flows/capex in-line with expectations** — inventories are in check – <1mth of sales. Working capital remains tight. FY10 capex is targeted at Rs21bn; the company's cash surplus is ~Rs47bn. Escalating spends on R&D could further cut the effective tax rate (~27% in 1Q).
- **Overall, mgmt remains cautiously optimistic** — Mgmt noted that a) financing has improved (66% today, vs ~60% commencement of fiscal), b) consumer confidence is improving (reflected in richer mix), c) Discounts/car have trended down to Rs9k from Rs12k/car. Risks are macro in nature – muted monsoons, higher rates. We maintain Hold (2L), given expensive valuations.

Hold/Low Risk	2L
Price (23 Jul 09)	Rs1,238.70
Target price	Rs1,079.00
Expected share price return	-12.9%
Expected dividend yield	0.4%
Expected total return	**-12.4%**
Market Cap	Rs357,873M
	US$7,391M

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

Statistical Abstract

Year to 31 Mar	Net Profit (RsM)	Diluted EPS (Rs)	EPS growth (%)	P/E (x)	P/B (x)	ROE (%)	Yield (%)
2007A	15,620	54.07	28.8	22.9	5.2	25.4	0.4
2008A	17,308	59.91	10.8	20.7	4.3	22.7	0.4
2009E	12,187	42.18	-29.6	29.4	3.8	13.7	0.4
2010E	17,788	61.57	46.0	20.1	3.3	17.6	0.4
2011E	21,819	75.52	22.7	16.4	2.8	18.3	0.5

Source: Powered by dataCentral

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

Fiscal year end 31-Mar	2007	2008	2009E	2010E	2011E
Valuation Ratios					
P/E adjusted (x)	22.9	20.7	29.4	20.1	16.4
EV/EBITDA adjusted (x)	16.1	14.0	21.8	12.9	9.9
P/BV (x)	5.2	4.3	3.8	3.3	2.8
Dividend yield (%)	0.4	0.4	0.4	0.4	0.5
Per Share Data (Rs)					
EPS adjusted	54.07	59.91	42.18	61.57	75.52
EPS reported	54.07	59.91	42.18	61.57	75.52
BVPS	237.23	291.28	322.91	377.98	446.43
DPS	4.50	5.00	5.00	5.50	6.00
Profit & Loss (RsM)					
Net sales	146,539	179,362	204,553	239,920	278,425
Operating expenses	-129,349	-162,612	-197,270	-223,894	-257,198
EBIT	**17,190**	**16,751**	**7,283**	**16,026**	**21,227**
Net interest expense	-376	-596	-510	-450	-500
Non-operating/exceptionals	5,984	8,876	9,985	10,972	11,839
Pre-tax profit	**22,798**	**25,030**	**16,759**	**26,549**	**32,566**
Tax	-7,178	-7,722	-4,571	-8,761	-10,747
Extraord./Min.Int./Pref.div.	0	0	0	0	0
Reported net income	**15,620**	**17,308**	**12,187**	**17,788**	**21,819**
Adjusted earnings	15,620	17,308	12,187	17,788	21,819
Adjusted EBITDA	19,904	22,432	14,349	24,050	30,255
Growth Rates (%)					
Sales	21.2	22.4	14.0	17.3	16.0
EBIT adjusted	24.9	-2.6	-56.5	120.0	32.5
EBITDA adjusted	19.8	12.7	-36.0	67.6	25.8
EPS adjusted	28.8	10.8	-29.6	46.0	22.7
Cash Flow (RsM)					
Operating cash flow	**22,740**	**22,724**	**16,691**	**25,985**	**29,813**
Depreciation/amortization	2,714	5,682	7,065	8,024	9,028
Net working capital	4,406	-266	-2,562	174	-1,035
Investing cash flow	**-27,408**	**-34,739**	**-11,007**	**-18,435**	**-17,336**
Capital expenditure	-13,828	-17,024	-16,000	-18,000	-12,000
Acquisitions/disposals	-13,580	-17,715	4,993	-435	-5,336
Financing cash flow	**3,984**	**1,001**	**-4,448**	**-1,880**	**-7,646**
Borrowings	5,591	2,694	-1,397	-5	-5,600
Dividends paid	-1,519	-1,691	-1,705	-1,875	-2,045
Change in cash	**-684**	**-11,014**	**1,236**	**5,671**	**4,831**
Balance Sheet (RsM)					
Total assets	**101,537**	**123,044**	**132,866**	**153,598**	**170,209**
Cash & cash equivalent	14,228	3,240	4,476	10,147	14,978
Accounts receivable	7,474	6,555	7,590	8,723	10,101
Net fixed assets	28,986	40,328	49,263	59,239	62,210
Total liabilities	**32,998**	**38,890**	**39,575**	**44,395**	**41,232**
Accounts payable	9,096	8,549	10,422	11,828	13,598
Total Debt	6,308	9,002	7,605	7,600	2,000
Shareholders' funds	**68,539**	**84,154**	**93,291**	**109,204**	**128,977**
Profitability/Solvency Ratios (%)					
EBITDA margin adjusted	13.6	12.5	7.0	10.0	10.9
ROE adjusted	25.4	22.7	13.7	17.6	18.3
ROIC adjusted	40.3	26.5	6.0	12.9	16.6
Net debt to equity	-11.6	6.8	3.4	-2.3	-10.1
Total debt to capital	8.4	9.7	7.5	6.5	1.5

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1QFY10 Results – Overall, a Solid Quarter

Export volumes buoyed by scrappage incentives in EU – mgmt indicated that A-Star customer response has been above expectations

Domestic market share gains and growth driven by new models - Ritz and A-Star.

In the domestic market, mgmt is positively surprised that the Ritz has a) not cannibalized the Swift volumes, b) has positively surprised internal expectations on volume growth and c) a petrol–diesel of 50-50 is also an encouraging trend.

Mgmt indicated that while financing penetration has increased to 66% (was ~60% early CY09), demand in top 10 cities remains lackluster; demand in the next 10 cities has modestly improved.

Rural India continues to drive MSIL's domestic growth – now accounts for 12% of volumes vs. 9% last year. Monsoons are a macro risk from a sentiment perspective. Mgmt noted that it sells to teachers/bank employees in rural India, rather than farmers

Figure 1. Quarterly Trend

	1QFY09	2QFY09	3QFY09	4QFY09	1QFY10
Volumes (units) – Domestic	180,093	171,706	158,860	211,485	197,415
Volumes (units) – Exports	12,491	17,745	14,634	25,153	29,314
Average Realizations (Rs mn)	246,832	253,695	260,104	267,682	280,719
Material Cost/Vehicle (Rs)	191,608	201,109	211,057	214,712	218,545
Other Expenses/Vehicle (Rs)	25,376	29,106	32,101	29,988	26,958
EBITDA Margins (%)	9.8	7.3	4.6	6.5	10.4
EBITDA/Vehicle (Rs)	24,075	18,599	11,994	17,359	29,325

Source: Citi Investment Research and Analysis

Figure 2. Maruti Operational Results – 1QFY10

	1Q FY09	1Q FY10	% chg	CIRA Comments
Passenger Vehicles (Nos)	192,584	226,729	17.7	
Average realization Net (Rs/vehicle)	246,832	280,719	13.7	Realizations improved due to richer product mix and increase in exports in the overall mix
Market share (Cars %)	45.4	48.2		

Source: Citi Investment Research and Analysis, Company

Figure 3. Maruti Financial Results – 1QFY10

	1Q FY09	1Q FY10	% chg	CIRA Comments
Total income from operations	**47,536**	**63,647**	**33.9**	**2% above estimates, due to higher realizations**
Decrease/(Increase) in Stocks	334	(596)		
Raw Materials	36,567	50,147	37.1	We estimate decline in commodity costs positively impacted margins by 130 bps y/y after netting off impact of FX on vendor imports
Staff costs	1,112	1,336	20.1	Slightly below estimates
Other Expenses	4,887	6,112	25.1	Cut costs by 1) Lower Selling and Administrative expenses, 2) Lower power and fuel costs
Total Expenditure	42,899	56,998	32.9	
EBITDA	4,636	6,649	43.4	19% above estimates mainly due to 1) Raw material benefit, 2) Increase in realizations due to richer mix and increase in exports, 3) No negative impact of currency on input costs
Interest	168	63	-62.5	
Other income	3,288	3,448	4.9	Significantly above estimates due to 1) higher spare part sales and 2) investment income
EBDT	7,756	10,034	29.4	
Depreciation	1,661	1,961	18.1	In line with estimates
PBT	6,095	8,073	32.4	
Tax	1,437	2,238	55.7	
PAT	4,659	5,835	25.3	
PAT (pre exceptionals)	**4,659**	**5,835**	**25.3**	**38% above estimates**
Profit Margins (%)				
OPM (%) (Net income)	9.8	10.4		140 bps above estimates, 390 bps up q/q, 60 bps up y/y
Pre tax margins (%)	12.8	12.7		
Tax / PBT (%)	23.6	27.7		
Net profit margins (%)	9.8	9.2		
Cost ratios (%)				
Raw materials / sales	77.6	77.9		90 bps above estimates
Staff costs / sales	2.3	2.1		30 bps below estimates
Other expenses / sales	10.3	9.6		200 bps below estimates
Excise / sales	13.0	8.9		

Source: Citi Investment Research and Analysis, Company

Key takeaways from the conference call

1. **Volume Guidance:** Management maintained their guidance of 5% y/y volume growth in domestic sales in FY10 and exports volumes of 130,000 units. However management did indicate that poor monsoons could affect their rural sales (which form around 12% of 1QFY10 volumes).

2. **FX exposure and policy:** Company indicated that it has hedged 50% of its direct raw material import exposure from Japan. However, the vendor imports (~15% of net revenues) have not been hedged. Mgmt also indicated that it would look to reduce forex volatility in the business by increasing localization and working with vendors to hedge their forex exposure.

3. **Discounts trend down:** Management indicated that the average discounts/vehicle has come down to Rs 9,500/vehicle in this quarter vs. Rs 12,000/vehicle in 4QFY09.

4. **Increase in diesel sales aid realizations:** Diesel sales increased by 66% y/y and 10% q/q, which positively affected realizations.

5. **New Models drive growth:** Management indicated that the new models are selling well – sales of old models have been flat. Around 26,000 units of A-Star (~11% of total sales) and 14,000 units of Ritz (6% of total sales) were sold in this quarter.

6. **Inventory levels at normal levels:** Mgmt stated that its inventory levels are at normal levels (within 30 days).

Maruti Suzuki India

Company description

Maruti is a subsidiary of Suzuki Motor Corp (holds a 54% equity stake). With its early-mover advantage in the Indian market, Maruti is a dominant player in the domestic passenger car market with a c.50% market share. It is re-positioning itself to become a global production hub of Suzuki over the medium term.

Investment strategy

We rate Maruti Hold/Low Risk. Over FY10-12e, we expect the Indian car market to resume growth at the trend rate of 10-12%, driven by a) low penetration levels, b) the resumption of financing, and c) a decline of c10% in the overall cost of ownership. Maruti is best positioned to benefit from this growth, in our view, given its dominance in the domestic car market. The company's rising penetration in the diesel car market gives it a more balanced product mix than two years ago, while export initiatives will reduce its dependence on the domestic car market. We estimate earnings and cash earnings CAGRs of 34% and 27%, respectively, over FY09-11e, driven by unit sales CAGR of 12% and margin expansion resulting from a decline in commodity costs. However, the sharp run-up in the stock price over the past few months factors in a fair degree of upside, without adequately discounting downside risks on FX/macro-related concerns.

Valuation

Our target price for Maruti of Rs1,079 is based on 11x Sep 10e cash earnings (CEPS = PAT + depreciation). At 11x, we value MSIL slightly higher than its historical average of 10x. We estimate a cash earnings CAGR of 27% over FY09-FY11E, which should support valuations, in our view. Our 11x multiple is in line with both regional and domestic peers. On our target multiple, Maruti would trade at FY10/11E P/Es of 17.5x and 14.3x, in line with broader Sensex valuations and merited, in our view, given the improving outlook for the auto sector as interest rates decline. We prefer price/cash earnings as a valuation metric for the automobile sector, given the industry's high capital intensity (both in terms of capacity and product development).

Risks

We rate Maruti Low Risk. This is below our quantitative risk-rating system, which tracks 260-day historical share price volatility, but warranted by improving macro trends for the auto sector, in our view. Upside risks that could prevent the stock from reaching our target price include: 1) greater than forecast increase in volumes and realizations; and 2) decline in competitive intensity. Downside risks include: 1) sales of passenger vehicles are sensitive to economic variables with an appreciable rise in interest rates potentially hitting volume growth across the auto sector; 2) revised emission and safety norms could bring cost pressures; 3) competitive pressures in the Indian market continue to increase, which could impact margins over the longer term; 4) higher than forecast increase in commodity costs.

Appendix A-1

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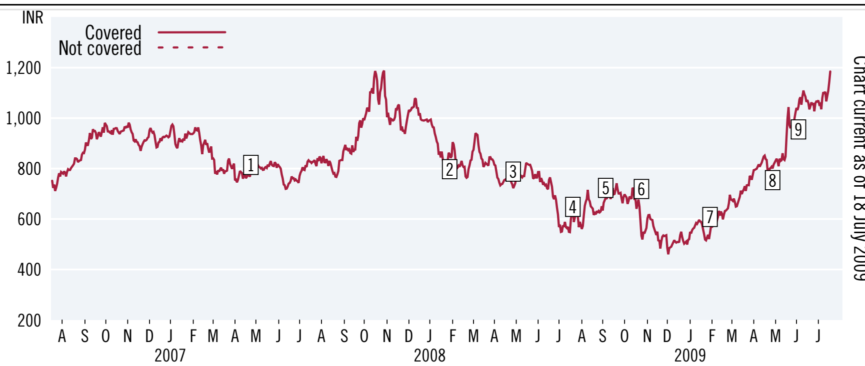
Maruti Suzuki India (MRTI.BO)

Ratings and Target Price History
Fundamental Research

Analyst: Jamshed Dadabhoy



	Date	Rating	Target Price	Closing Price
1	24-Apr-07	1L	*945.00	794.40
2	29-Jan-08	1L	*1,012.00	857.20
3	28-Apr-08	*2L	*807.00	722.35
4	21-Jul-08	2L	*713.00	648.20
5	4-Sep-08	2L	*716.00	683.90
6	24-Oct-08	*2M	*633.00	533.55
7	29-Jan-09	2M	*596.00	544.80
8	28-Apr-09	*2L	*863.00	800.65
9	3-Jun-09	2L	*1,079.00	1,045.70

* Indicates change

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