Autos & Auto Parts | India

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SECTOR QUICK COMMENT

Based on our channel checks we expect Indian OEMs to report strong volume numbers in November 2011. Strong wholesale numbers should also be helped by a low base in November 2010 because of Diwali holidays. Retail demand remains strong for rural-focused sectors like two-wheelers, tractors and UVs for M&M. We expect cars to remain weak though, plagued by sharp increases in petrol prices, and CVs to maintain growth despite a slowdown in economic growth. We believe that MM, TVSL and BJAUT in particular could react positively to strong volume numbers.

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Expect robust volume growth in November 2011

Erratum: The volume dates in Figure 1 were incorrect in the earlier published note. The columns should read Nov-11, Oct-11 and Nov-10. We apologise for any inconvenience caused.

Figure 1: Volume expectations

Volumes (units)	Nov-11	Oct-11	Nov-10	Y/Y	Comments
Maruti					
Domestic	82,000	51,458	102,503	**-20.0%**	Volumes to remain weak as production at Manesar plant will be completely ramped-up only by Jan & retail demand for petrol segment remains weak
Exports	10,000	4,137	10,051	**-0.5%**	
Total	92,000	55,595	112,554	**-18.3%**	
Bajaj Auto	**Nov-11**	**Oct-11**	**Nov-10**	**YoY**	
Motorcycles	310,000	351,083	265,036	**17.0%**	Strong growth momentum in both domestic and export markets and low base effect to lead to 17% y/y growth in 2-wheelers in Nov-11
CV	43,000	44,191	34,195	**25.7%**	
Total	353,000	395,274	299,231	**18.0%**	
of which Exports	126,000	141,913	110,387	**14.1%**	
Hero Honda	**Nov-11**	**Oct-11**	**Nov-10**	**YoY**	
Domestic	515,000	497,105	409,306	**25.8%**	Volume growth to remain strong partly due to inventory build up post strong festive season and low base effect
Exports	15,000	15,133	12,060	**24.4%**	
Total	530,000	512,238	421,366	**25.8%**	
M&M	**Nov-11**	**Oct-11**	**Nov-10**	**YoY**	
Passenger vehicles	17,000	18,756	12,433	**36.7%**	Higher XUV500 volumes to lead to strong growth in UVs. Growth momentum in LCVs to remain strong on demand for Maximo and pick-ups. Tractor segment to
LCV/ M&HCVs	12,300	14,264	8,377	**46.8%**	
Exports	1,870	2,154	1,500	**24.7%**	
3 wheelers	5,400	6,332	4,468	**20.9%**	

Tractors	20,000	31,838	17,993	**11.2%**	grow at 11% y/y
Total	56,570	73,344	44,771	**26.4%**	
Tata Motors	**Nov-11**	**Oct-11**	**Nov-10**	**YoY**	
Passenger vehicles	24,550	25,459	16,129	**52.2%**	We expect growth in CVs to remain strong in Nov-11. However, absolute volumes in passenger vehicles segment will continue to remain weak. Growth will largely be helped by low base
Commercial vehicles	45,600	42,550	38,493	**18.5%**	
MHCVs	17,100	17,890	15,873	**7.7%**	
LCVS	28,500	24,660	22,620	**26.0%**	
Total	70,150	68,009	54,622	**28.4%**	
of which exports	5,150	4,171	4,203	**22.5%**	
Jaguar	5,958	5,231	5,621	**6.0%**	Strong growth in JLR is largely driven by the launch of Evoque
Land Rover	23,723	20,927	17,336	**36.8%**	
JLR - Total	29,681	26,158	22,957	**29.3%**	
TVS	**Nov-11**	**Oct-11**	**Nov-10**	**YoY**	
Two-wheeler	192,000	180,006	153,882	**24.8%**	We expect robust growth in 2-wheelers on strong growth across segments particularly in scooters and also partly due to low base effect
Three-wheeler	3,200	3,712	3,159	**1.3%**	
Total	195,200	183,718	157,041	**24.3%**	
of which Exports	26,385	22,129	15,850	**66.5%**	
Ashok Leyland	**Nov-11**	**Oct-11**	**Nov-10**	**YoY**	
Domestic	6,400	5,892	3,884	**64.8%**	Growth to be largely driven by low base effect.
Exports	850	570	1,252	**-32.1%**	
Total	7,250	6,462	5,136	**41.2%**	

Source: Company data, SIAM, Nomura estimates

Dealer feedback

TVS

Location: Mumbai, Bangalore

- **The company has taken a price increase of INR600-1,200 across all models (except Star City) effective 3 November, 2011. This implies a price hike of 1.2-1.4%.**
- **Volumes of the Star City model have picked up this month with the launch of bikes with the signature of M.S. Dhoni. The company has also introduced new colors and made minor changes in design which has also helped demand.**
- **Overall, as expected demand is slightly weak this month post the strong festive season.**
- **The company continues to offer discount in terms of free accessories worth around INR2,300 across all models.**
- **Inventory levels remain stable at around 10-12 days.**

M&M (Automotive)

Location: Mumbai

- **Demand for Scorpio remains strong despite the launch of XUV500; Xylo and Verito also continue to do well despite higher competition in these segments**

- According to the dealer, supply of pick-ups as well as Bolero has been low over the past few months possibly owing to capacity constraint in MDi engines. The dealer has also seen some shortages in supply of spare parts particularly for Maximo
- Dealer has not received XUV500 since launch owing to internal issues, however, inquiry levels are very strong suggesting high customer interest
- However, as per the dealer, some customers are deferring purchases till December in anticipation of higher discounts
- The last price revision was done in Aug-Sep when prices were increased between 0.5% and 1.0% across models

M&M (Farm Equipment)

Location: Thane

Key points

- Volume growth over the past six months is in the 20-40% range; sees no slowdown in the next 3-6 months
- 40-45hp category is doing particularly well in the area
- Around 20% of the volumes come from farming and 80% from commercial (construction) activities
- Interest rates have increased from 14-16% around 6-8 months back to around 18-22% in case of private banks;
- Recently finance availability has reduced to some extent; however, given strong underlying demand, volume growth has not been affected

Location: Bhopal

Key points

- Volume growth is around 18-20%; a good monsoon this year has led to strong growth in the region
- As per the dealer, strong soybean and wheat harvesting season should lead to strong volume growth
- Loan availability has improved significantly this year because of a good monsoon; PSU banks in particular are lending quite easily
- M&M has increased prices by 1.5-2% in the past 2-3 months

Location: Ahmedabad

Key points

- Volumes have almost doubled this year primarily due to strong growth in trucks used in haulage activities
- Farming accounts for 20% of M&M's volumes, whereas, 80% comes from haulage
- M&M has a market share of 80-90% in the haulage category, as per the dealer; while market share in the 45 hp category is relatively lower (John Deere is doing well in this space)
- 26 DI and 275 DI models are doing extremely well in the region
- M&M has increased prices three times by around 2% each in the past 6-8 months; the last hike of around 2% was done in October 2011

Bajaj Auto

Location: Mumbai, Bangalore

- Volumes remain slower in November 2011 after a stronger-than- expected festival season this year. Some customers are deferring purchases to the next calendar year (January 2012)
- Overall retail volume growth is around 8-10% y/y in November 2011.
- All the models are doing well; especially, Discovery 125cc in the executive segment, which has witnessed strong growth
- Inventory levels are around 15-16 days as against around 21 days before the festive season.

Hero MotoCorp

Location: Mumbai

- **Retail sales growing at 15% in November 2011; customer enquiries remain high**
- **The dealer mentioned that there is no impact on volumes post separation from Honda**
- **Inventory levels are at 18 days, marginally higher than 15 days usually maintained by the dealer**
- **Recently-launched Impulse has received strong initial response from customers**

Maruti Suzuki

Location: Mumbai, Chennai

- **Post the end of labor strike, supply of Swift and Dzire models has improved, however, because of new bookings, the waiting period remains high.**
- **Waiting period in Swift and Dzire diesel variants is around 12-16 weeks, whereas, for petrol variants, the waiting period is 8-12 weeks**
- **Discounts have declined slightly in some models (Wagon R, Alto, etc) in November 2011; however, the company is now offering INR7,000 discount on the Eeco model from nil earlier.**
- **Sales of Wagon R and Alto models have seen some pick-up in November 2011 as compared to weak volumes in October 2011**
- **Overall y/y volume growth is negative in November 2011, partly due to higher petrol prices and high interest rates**
- **Inventory levels are within the normal range of 10-15 days.**

Valuation Methodology and Investment Risks: M&MValuation Methodology We value MM at INR896 based on a sum-of-the-parts (SOTP) methodology. We value the standalone auto business at INR653 based on 12x one-year forward (average of FY13F and FY14F) standalone EPS (ex-subsidiary dividends) of INR54.4. We value MVML at INR55 based on 12x one-year forward (average of FY13F and FY14F) EPS of INR4.6. We value the investments in other subsidiaries at INR188/share, after a 20% holding discount.Risks that may impede the achievement of the target price Key risks • Impact of slower GDP growth — our volume growth expectations are based on Nomura's India GDP growth expectations of 7.9% for FY13F. In the event that GDP growth is slower, there could be a downside risk to our volume estimates. • Higher excise duty on diesel vehicles — in the event that government decides to impose higher excise duty on diesel vehicles (to compensate for higher subsidies on diesel), there could be downside risks to our estimates. • Higher-than-expected raw material costs — we have assumed a scenario of stable commodity prices; however, if commodity prices were to go higher from current levels, there could be downside risks to our estimates.Tata MotorsValuation Methodology We have valued TTMT on a sum-of-the-parts basis to arrive at our TP of INR200/share. We value the standalone business at 8x FY13F EV/EBITDA at INR94.7/share. We value JLR at 2.5x FY13F EV/EBITDA at INR73.1/share and other investments at INR31.8.Risks that may impede the achievement of the target price Upside risks: 1) Emerging markets doing well — JLR has consistently improved its margins and realizations. We believe that if its volumes in China continue to grow sharply, there could be upside risk to our estimates. 2) Success of Evoque — We are building in around 25,000 units of Evoque sales for FY12. If the product sells much more than that, there would be upside risks to our estimates. 3) Growth in developed markets — If developed markets continue to record robust volume growth for Land Rover, there would be upside risks to our estimates. Downside risks: 1) JLR's margin weakening — JLR's margins are highly sensitive to volumes because of its high operating leverage. We assume JLR will be able to sustain volume. If volumes fall short of our assumptions, there could be material downside risk to our estimates. 2) Slowdown in India truck volumes — We assume that the domestic economy will remain stable and Tata Motors' domestic truck volumes will continue to grow. In case of a sharp slowdown, there could be material downside risk to our estimates. 3) Passenger vehicle business may drag — TTMT's PV business has reported volume growth well below industry levels. Nano, which was expected to be a high-volume segment, has seen a sharp fall in sales from a peak of 9,000 in July 2010 to around 1,200 units in August 2011 (retail sales were around 6,500 units). If the PV business continues to face market share pressure, it may remain a drag on earnings growth.TVSValuation Methodology We value TVS based on DCF using 4% terminal growth and 13.1% cost of equity. We have discounted our cashflows back to Oct-12 to arrive at our one year forward target price of INR87.Risks that may impede the achievement of the target price • Slower-than-expected GDP growth: Our FY13F domestic volume growth estimates of 8% are based on Nomura's GDP growth assumption of 7.9% in FY13F. In case GDP growth slows substantially, there would be downside risks to our estimates. • Increased competition: We believe that the intensity of competition will remain low for TVS, especially in the mopeds and scooters segments. In case there are aggressive new entrants, there will be downside risk to our estimates. • Higher-than-expected raw material costs: We have built in some decline in raw material costs due to decline in commodity prices. If commodity prices are higher than expected, there can be downside risks to our estimates.Ashok LeylandValuation Methodology We value Ashok Leyland based on DCF of FCFE at INR34/share. Our methodology is unchanged. We have used an assumption of 4% terminal growth and 13.4% cost of equity. Do note that we have not assigned any value to the group investments worth INR 5/share. This is because there is low visibility on earnings contribution from these investments. As the visibility improves there is a possibility that the market may start to value some of these investments.Risks that may impede the achievement of the target price Key risks a) Slower-than-expected ramp up of new plant – In case AL is not able to produce 35,000 units from the new plant in FY12F, our margin estimates would be at risk. b) Slowdown in industrial growth – In case there is a sharp slowdown in industrial growth, our volume estimates would be at risk. c) New competition – New competition from players like Mahindra and Mahindra could be a risk to our volume estimates for FY13F.Maruti SuzukiValuation Methodology We value MSIL at 14x one-year forward consolidated EPS (average of FY13F and FY14F EPS) of INR82.4, to give a TP of INR 1,153. We note that the stock's five-year average multiple on one-year forward consensus earnings is 14x.Risks that may impede the achievement of the target price Downside risks: (1) Slower-than-expected GDP growth — our FY13F domestic volume growth estimates of 16% is based on Nomura's GDP growth assumption of 7. 9% in FY13F. In case GDP growth slows substantially, there would be downside risks to our estimates. (2) Increases in raw material costs — we have assumed stable commodity prices; in case commodity prices increase from current levels, there would be downside risks to our estimates. (3) Increased competition — there could be downside risks to our volume estimates, if recent launches by competitors especially Hyundai EON are very successful. (4) JPY appreciation against the INR — MSIL imports components worth 16% of net sales in JPY. We estimate that a 5% change in the JPY/INR rate would affect margins by 100bps. If the JPY appreciates further, there could be downside risks to our estimates. We are currently factoring in an average rate of INR1:JPY0.615. Upside risks: (1) Decline in raw material costs — there would be upside risks to our estimates if there is a significant decline in commodity prices. (2) JPY depreciation against the INR — JPY appreciated by around 12% against INR from July-October 2011, to INR1:JPY0.615. If JPY depreciates, there could be upside risks to our estimates. Every 5% depreciation of JPY could lead to around 1% higher EBITDA margins.Bajaj AutoValuation Methodology We value Bajaj Auto at INR1,588, based on a Discounted Cashflow (DCF) method. We have built in an earnings CAGR of 9% over the next two years (FY11-FY13F). We estimate that its top-line will achieve a CAGR of 16% over the same period, but note that reduced DEPB benefits would lead to a decline in margins. We have assumed 5% terminal growth and 12.3% cost of equity.Risks that may impede the achievement of the target price Nano could replace passenger three-wheelers in the medium term; aggressive pricing by Hero Honda; and new small car not succeeding if launched.Hero MotoCorpValuation Methodology We value HMCL at INR2237 based on DCF (methodology unchanged). We have assumed terminal growth of 5% and cost of equity of 13%.Risks that may impede the achievement of the target price Downside • HMCL does not have R&D capabilities to design its own motorcycles at present. We believe the company will be able to develop this over the next few years. If the company is unable to set up a successful R&D facility by June 2014, there could be downside risks to our estimates. • We have assumed a decline in RM/sales due to decline in commodity prices, in case, commodity prices do not decline, there will be downside risk to our operating margin estimates • Macro risks: We have assumed stable macro conditions with GDP growth averaging around 8% over the next few years. In case there is a slowdown leading to lower GDP growth, there will be downside risks to our estimates. Upside • We have assumed that Hero MotoCorp will take around four to five years to establish itself in new export markets. If the company is able to do so faster there may be upside risks to our estimates. • HMCL has booked mark to market losses on license fee payable due to yen appreciation against rupee in 2QFY12. If going ahead, rupee appreciates against yen, then there would be mark to market gains leading to lower outgo on quarterly payments towards license fee; this would pose upside risks to our estimates.

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