Emkay Research

Mahindra and Mahindra Ltd

Result Update

Below expectation, rating revision

3rd February 2009

REDUCE

Price	Target Price
Rs291	**Rs264**

Sensex - 9,067

Price Performance

(%)	1M	3M	6M	12M
Absolute	1	(22)	(44)	(57)
Rel. to Sensex	11	(16)	(10)	(13)

Source: Bloomberg

Stock Details

Sector	Automobiles
Reuters	MAHM.BO
Bloomberg	MM@IN
Equity Capital (Rs mn)	2586
Face Value (Rs)	10
No of shares o/s (mn)	259
52 Week H/L (Rs)	721/236
Market Cap (Rs bn/USD mn)	75/1,533
Daily Avg Vol (No of shares)	780181
Daily Avg Turnover (US$ mn)	4.8

Shareholding Pattern (%)

	31/12/08	30/09/08	30/06/08
Promoters	26.5	26.5	22.7
FII/NRI	31.9	32.5	32.9
Institutions	26.7	26.5	28.0
Private Corp	5.0	4.7	6.0
Public	9.9	9.9	10.5

Source: Capitaline

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M&M's 3QFY09 performance was below our expectation. Net sales at Rs 25.2 bn were marginally below our expectation. Adjusted EBIDTA at Rs 2.3 bn was below our expectation by 8%. The pressure on operating performance was largely due to inventory reduction activity, which is equivalent to the inventory accretion during 1HFY09 of Rs 2.7 bn. However, we believe still there is a high cost inventory of around 1.5 bn with the company.

Net profits (adjusted for MTM loss on forex liabilities of Rs 461 mn) declined by 85% YoY to 377 mn. The drastic decline in net profits is attributable to Rs 1.4 bn of forex loss on cancellation of forward contracts for probable exports in 3QFY09. If Rs 1.4 bn is treated as extraordinary expense, net profits declined by 43% to Rs 1.2 bn. *However, considering the recurring nature of cancellation of forward contracts for next three to four quarters, we have treated the same as recurring expense.*

We have revised our FY09 and FY10 adjusted net profits estimates by 16% and 4% respectively. *Our net profit estimates does not factor in potential gain/loss due to cancellation of forward contracts over next three to four quarters.* We have valued the company on SOTP basis. We have valued the standalone business at Rs 205 (7.5x FY10 FDEPS). Considering the significantly high implied discount for the subsidiaries, we have increased our discount rate from 50% to 70% for subsidiaries. We have valued subsidiaries at Rs 59 per share. We downgrade our rating from HOLD to REDUCE.

Realisation drives the sales performance

M&M registered a 23% YoY decline in volumes to 61225 units in 3QFY09. Average realizations improved by 7.3% YoY to Rs 409,352. This is despite of adverse volumes mix. While the company has not made any significant price hikes in the UVs segment, Tractors witnessed a pricing action of around 12% to 15%. Also, company has not passed on the completely the benefits of reduction in excise duty.

Product mix %	3QFY09	3QFY08	2QFY09
Uvs	47.7	51.0	48.8
Three wheelers	13.9	11.3	18.2
Tractors	33.6	31.3	26.7
Export	4.8	6.5	6.4

EBIDTA at Rs 2.3 (8% below expectation) due to inventory reduction activity

EBIDTA (adjusted for forex loss of Rs 1.8 bn and one time dealer compensation of Rs 100 mn) was at Rs 2.3 bn, 8% below our expectation. We attribute this primarily inventory reduction activity undertaken by the company. Of the total inventory accretion of Rs 4.2 bn since march 2008, (Rs 1.5 bn as at end FY08 and Rs 2.7 bn during 1HFY09), the company has shown a reduction of Rs 2.7 bn of inventory.

Forex loss – dents net profit in 3QFY09, can dent profits for next 4 quarters

M&M reported a forex loss of Rs 1.4 bn on cancellation of forward contracts for exports due in 3QFY09. While we were surprised by the nature and extent of transaction, the worrisome part is likelihood of repetition of similar business transaction for next three to four quarters. The matter got compounded as the management did not share any details of contracts that have been cancelled and more importantly, the amount of forward contracts that are outstanding. Our analysis indicates that value of cancelled contracts could range from USD 146 mn to USD 318 mn (or 80% to 180% of FY08 exports).

Valuation and View

We have revised our FY09 and FY10 estimates by 16% and 4% as indicate below. Our net profit estimates does not factor in potential gain/loss due to cancellation of forward contracts over next three to four quarters.

	FY09E			FY10E		
Rs mn	Earlier	Revised	Change	Earlier	Revised	Change
Sales	119,570	117,160	-2.0	131,596	128,984	-2.0
EBIDTA	9,647	9,502	-1.5	11,597	11,103	-4.3
EBIDTA margins (%)	8.1	8.1		8.8	8.6	
Net Profits	7,405	6,205	-16.2	8,338	7,968	-4.4

We have valued the stock based on SOTP as indicated below. We have determined the SOTP value based on fully diluted equity of 292 mn shares.

Valuation Summary (based on fully diluted equity of 292 mn share)

Particulars	Basis	Discount	Value per share (Rs)
M&M	PER		205
Punjab Tractors	CMP		13
Total			**218**
Listed Subsidiaries			
Mahindra Finance	CMP	70	10
Mahindra Forgings	CMP	70	1
Mahindra Life	CMP	70	2
Mahindra Ugine	CMP	70	0
Tech Mahindra	CMP	70	14
Unlisted subsidiaries			
Mahindra Resort	0.5x PE deal	70	18
Total			**264**

Quarterly results summary

Rs mn	3QFY08	3QFY09	% change	9MFY08	9MFY09	% change
Net Sales	29,401	25,193	-14.3	82,711	89,237	7.9
Operating Expenses						
Raw Materials	19,768	18,019	-8.8	55,497	63,076	13.7
% of Sales	67.2	71.5		67.1	70.7	
Staff Costs	2,161	2,299	6.4	6,377	7,095	11.3
% of Sales	7.3	9.1		7.7	8.0	
Other Expenses	4,158	2,569	-38.2	11,733	11,064	-5.7
% of Sales	14.1	10.2		14.2	12.4	
Forex loss/(gain)	0.0	460.5		62	1,240	
EBIDTA	3,315	1,845	-44.3	9,042	6,763	-25.2
EBIDTA %	11.3	7.3		10.9	7.6	
Adj EBIDTA	3,315	2,306	-30.4	9,104	8,002	-12.1
Adj EBIDTA %	11.3	9.2		11.0	9.0	
Depreciation	590	653	10.5	1,738	1,912	10.0
EBIT	2,724	1,193	-56.2	7,304	4,850	-33.6
Other Income	401	-923	-330.0	1,409	604	-57.1
Interest	72	141	95.2	104	391	277.5
PBT	3,053	129	-95.8	8,609	5,064	-41.2
Extraordinary inc/(exp)	1,548.4	-100.0		2,442	683	
Tax	550	17	-96.9	2,197	907	-58.7
Net Profit	4,051	12	-99.7	8,854	4,840	-45.3
Net Margin %	13.8	0.0		10.7	5.4	
Adj Net Profit	2,495	377	-84.9	6,771	4,960	
Net Margin %	8.5	1.5		8.2	5.6	
EPS	15.5	0.0		33.9	18.5	
Adj EPS	10.4	1.6		28.4	19.5	

Financials

Profit & Loss Account - Standalone

Mar ending (Rs mn)	FY07	FY08	FY09E	FY10E
Net Sales	98,161	112,058	117,160	128,984
Growth YoY %	*20.9*	*14.2*	*4.6*	*10.1*
Operating Expenses				
Raw Materials	68,498	77,441	82,759	89,696
% of sales	69.8	69.1	70.6	69.5
Staff Costs	6,662	8,525	9,121	10,252
% of sales	6.8	7.6	7.8	7.9
Other Expenses	12,715	15,625	15,778	17,932
% of sales	13.0	13.9	13.5	13.9
EBIDTA	10,287	10,468	9,502	11,103
Growth %	*18.9*	*1.8*	*(9.2)*	*16.9*
EBIDTA %	*10.5*	*9.3*	*8.1*	*8.6*
Depreciation	2,096	2,387	2,426	3,001
EBIT	8,191	8,082	7,076	8,103
Other Income	4,050	4,064	2,816	4,338
Interest	198	876	1,619	1,817
PBT	12,043	11,270	8,274	10,624
Extraordinary inc/(exp)	1,622	2,877	683	0
Tax	3,501	3,034	2,068	2,656
Net Profit	10,164	11,114	6,888	7,968
NPM %	*10.4*	*9.9*	*5.9*	*6.2*
Adj Net Profits	*8,722*	*8,567*	*6,205*	*7,968*
NPM %	*8.9*	*7.6*	*5.3*	*6.2*
EPS	40.9	44.5	26.4	30.5
Adj EPS	35.1	34.3	23.7	30.5

Balance Sheet - Standalone

Mar ending (Rs mn)	FY07	FY08	FY09E	FY10E
Share Capital	2,486	2,497	2,613	2,613
Reserves	33,044	41,003	50,638	54,377
Misc Exp	(176)	(135)	0	0
Owned Funds	35,354	43,365	53,251	56,990
Secured Loans	1,067	6,173	6,173	6,173
Unsecured Loans	15,294	19,698	26,198	34,198
Loan Funds	16,360	25,871	32,371	40,371
Deferred Tax Liability	198	567	567	567
Total	51,912	69,803	86,188	97,928
Gross Fixed Assets	32,297	36,561	42,561	54,561
Acc. Depreciation	16,391	18,417	20,843	23,844
Net Fixed Assets	15,906	18,145	21,719	30,718
Capital WIP	2,806	5,465	11,000	13,000
Net Block	18,712	23,609	32,719	43,718
Investments	22,375	42,151	47,651	53,651
Sundry Debtors	7,009	10,049	9,823	10,485
Inventory	8,785	10,841	10,875	11,609
Cash & Bank	13,261	8,612	10,039	5,308
Advances	8,394	6,919	8,323	9,568
Other Current Assets	33	133	133	133
Current Assets	37,482	36,554	39,193	37,102
Liabilities	19,502	23,076	24,454	26,776
Provisions	7,154	9,435	8,920	9,767
Current Liabilities	26,656	32,510	33,374	36,543
Net Current Assets	10,825	4,044	5,819	560
Total	51,911	69,803	86,188	97,928

Cash Flow

Mar ending (Rs mn)	FY07	FY08	FY09E	FY10E
Net Profit before tax	12,043	11,270	8,274	10,624
Add: Depreciation	2,096	2,387	2,426	3,001
Add: Interest exp	198	876	1,619	1,817
Less: Other income	4,050	4,064	2,816	4,338
Dec/ (Inc) in Working capital	1,978	(2,472)	(349)	529
Other non operating items	(2,859)	(3,039)	(1,435)	(1,570)
Less: Tax paid	3,434	2,777	2,068	2,656
Cash from operations	11,689	8,258	5,650	7,406
Capex	(4,819)	(7,171)	(11,536)	(14,000)
Investments and Others	(6,680)	(14,926)	(5,500)	(6,000)
Other income	1,995	1,346	2,816	4,338
Cash from Investing activities	(9,504)	(20,751)	(14,220)	(15,662)
Borrowings/Equity raising	9,293	10,095	13,757	8,000
Interest paid	(278)	(801)	(1,619)	(1,817)
Dividend paid	(4,530)	(823)	(2,142)	(2,659)
Cash from financing activities	4,486	8,470	9,996	3,525
Cash generation during the year	6,671	(4,022)	1,427	(4,731)
Opening Balance	7,303	13,261	8,612	10,039
Forex (loss) / gain	(357)	-627		
Closing balance	13,617	8,612	10,039	5,308

Valuation Summary

Mar ending	FY07	FY08	FY09E	FY10E
Per Share Data				
EPS	35.1	34.3	23.7	30.5
Cash EPS	43.5	43.9	33.0	42.0
BVPS	142.2	173.6	203.8	218.1
*based on current equity capital of 261 mn shares				
Valuation ratios				
P/E	8.3	8.5	12.3	9.5
Cash P/E	6.7	6.6	8.8	6.9
P/BV	2.0	1.7	1.4	1.3
EV/EBIDTA	12.2	11.5	13.3	12.0
Return Ratios (%)				
AROE	31.6	28.2	14.3	14.5
AROCE	26.9	20.0	12.7	13.5
DuPont				
NPM (%)	10.4	9.9	5.9	6.2
Sales/TA	1.2	1.1	1.0	1.0
TA/Equity	2.2	2.4	2.2	2.4
Other key ratios				
D/E	0.5	0.6	0.6	0.7
NCA/Sales (%)	11.0	3.6	5.0	0.4

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