

Momentum maintained

30 January 2008

BUY

Price	Target Price
Rs 845	Rs 1200

Sensex – 17,759

Price Performance

(%)	1M	3M	6M	12M
Absolute	(13)	(28)	2	(9)
Rel. to Sensex	(3)	(20)	(13)	(28)

Source: Bloomberg

Stock Details

Sector	Automobiles
Reuters	MRTI.BO
Bloomberg	MSIL@IN
Equity Capital (Rs mn)	1445
Face Value (Rs)	5
52 Week H/L (Rs)	1252/700
Market Cap (Rs bn)	247
Daily Avg Vol (No of shares)	749852
Daily Avg Turnover (US\$ mn)	18.7

Shareholding Pattern (%) (30th Dec.'07)

Promoters	54.2
FII/NRI	15.9
Institutions	23.8
Private Corp.	3.6
Public	2.5

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Maruti reported its 3QFY08 results. Net sales grew by 27% YoY to Rs 46.7 bn backed by 17% YoY volume growth and improving product mix. However, operating margins declined by 70 bps YOY to 13.1% on account of higher raw material expenses. EBIDTA grew by 21% YoY to 6.1 bn. There has been significant increase in other income during the quarter due to increase in both operational (scrap sales, cash discounts, etc) and treasury income. As a result, net profits grew by 24% YoY to Rs 4.7 bn

The results were in line with our expectations, except for better than expected performance at the net sales level. We expect the company to continue to outperform the industry growth in FY09 backed by strong brand equity and also new product line ups. However, there are concerns with respect to the likely impact on the company's performance post the commercial launch of Tata Motors' NANO. We believe that the concerns on account of NANO are overdone and the actual impact on Maruti's performance may not as severe as it has been perceived. Also, at current valuations the concerns are factored in. Having said that we have factored in a significant lower growth for Maruti in FY10, largely factoring the decline in the growth for ALTO. Also we have factored in significant decline in EBIDTA margins. At Rs 845, the stock trades at PER of 10.7 times and 9.4 times our FY09 and FY10 earnings estimates. Also, the company has surplus cash of Rs 145 per share.

The potential trigger in the stock could come from faster ramp up at its Manesar plant, an update on its export model for European market and contract manufacturing for Nissan. Also, we expect the company to continue to announce new launches (at least one per year) apart from introduction of variants of its existing offerings.

Realizations drive the performance

Maruti registered a 17% YoY growth in volumes to 201629 units in 3QFY08. However, net sales grew by 27% YoY to Rs 46.7 bn on account of significant improvement in average realizations. Average realizations registered an improvement of 8.5% YoY to Rs 231,818 per vehicle sold.

Better Product mix aiding realizations growth

The improvement in realization has largely come for improving product mix, rather than pricing action. Apart from rising sales of new launches, there is higher demand for Vxi and Zxi models. Company is selling around 3000 units of SX4 and 3000 units of Swift diesel per month. But for the capacity constraints at its Manesar plant, the mix could have been more favorable.

Product mix %	3QFY08	3QFY07	2QFY08
M-800	8.6	11.6	8.7
Omni, versa	11.6	12.6	11.2
Alto, Wagon -R, Zen, Swift	66.6	67.3	64.1
Esteem, Baleno SX4	5.8	4.1	7.4
Gypsy, Vitara	0.5	0.4	0.6
Exports	6.8	4.2	7.9

Source: Company, Emkay Research

Operating margins continue to decline

Despite, improving average realizations, operating margins declined by 70 bps to 13.1% YoY (in line with our expectations), largely driven by raw material expenses. Rising raw material expenses can be attributed to improving product mix. Power and fuel costs have increased significantly (by 50% YoY to Rs 364 mn), largely due to renegotiations of gas price contracts at significantly higher rates. There has been increase in royalty expenses (27% YoY to Rs 1210 mn) due to rising share of royalty bearing models in the portfolio. The share of royalty bearing models increased from 65.5% in 3QFY07 to 75.4% in 3QFY08. Also, company had to spend on higher sales and promotion expenses.

Other income aids the bottomline

Other income has increased by 33% YoY to Rs 1.7 bn. This is on account of higher operational income (scrap sales, cash discounts and sales tax benefits) and higher treasury income in 3QFY08. Scrap sales and cash discounts stood at Rs 620 mn, YoY growth of 48%.

Introducing FY10 numbers

We are factoring a significant lower growth in volumes in FY10 vis-a-vis the domestic industry growth (see table below). We have factored in a 15% decline in the sales of ALTO and 10% decline in sales of 800, to account for the potential impact of NANO. Having said that, considering the price difference between NANO and ALTO, the potential impact of NANO on Maruti's performance may not be as severe as it is perceived. Also, we believe that the key driver for the company will be progress on European exports front. We have factored in 70,000 units as exports of 'A – Star' concept to European market in FY10.

Volume Summary

	FY07	FY08E	FY09E	FY10E
Maruti				
Domestic	632,408	738,020	847,016	916,533
% growth	21.0	16.7	14.8	8.2
Exports	39,090	53,775	72,192	153,601
% growth	12.7	37.6	34.2	112.8
Industry				
Domestic	1,159,499	1,318,345	1,498,929	1,697,716
% growth	22.3	13.7	13.7	13.3

Valuation and View

Maruti has outperformed the industry growth comprehensively in 9MFY08. We expect the out performance to continue in FY09. However, capacity constraints at its Manesar plant would restrict the ability of the company to capitalize on the strong brand premium on the Swift as well as SX4 as the capacity expansion is likely to fructify by end FY09. Secondly, with rising exports, we believe that margins could come under pressure. s

As stated earlier, we have factored in lower volume growth in the domestic market to factor in probable impact of the NANO. Having said that, considering the price difference between NANO and ALTO, the potential impact of NANO on Maruti's performance may not be as severe as it is perceived. Also, we believe that the key driver for the company will be progress on European exports front. We have factored in 70,000 units as exports of 'A – Star' concept to European market in FY10.

At Rs 860, the stock trades at 10.7 times and 9.4 times our estimated EPS of Rs 79.2 and Rs 89.6 for FY09 and FY10 respectively. Also, the company has surplus cash of Rs 145 per share. *We believe that the current price adequately discounts the probable impact of NANO. We do not foresee any downside to stock price from the current levels. We maintain our **BUY** rating on the stock with a target price of Rs 1200.*

The key triggers in the stock could come from a faster ramp up at its Manesar plant, an update on the contract manufacturing for Nissan (expected to commence production by end FY09) and its strategy for European market with the launch of its Europe dedicated offering. Also, we expect the company to continue to launch new model (atleast one model per annum) apart from introduction of variants for its existing offerings.

Quarterly and annual results summary

Rs mn	3QFY07	3QFY08	% CHG	9MFY07	9MFY08	% CHG
Net Sales	36,794	46,741	27.0	102,241	131,523	28.6
Operating Expenses						
Raw Materials	27,662	35,762	29.3	76,827	100,053	30.2
<i>% of Sales</i>	75.2	76.5		75.1	76.1	
Staff Costs	738	968	31.0	2,078	2,681	29.1
<i>% of Sales</i>	2.0	2.1		2.0	2.0	
Other Expenses	3,323	3,879	16.7	8,943	10,930	22.2
<i>% of Sales</i>	9.0	8.3		8.7	8.3	
EBIDTA	5,071	6,133	20.9	14,393	17,859	24.1
EBIDTA %	13.8	13.1		14.1	13.6	
Depreciation	759	867	14.3	1,995	2,571	28.8
EBIT	4,312	5,266	22.1	12,398	15,289	23.3
Other Income	1,284	1,707	32.9	3,934	5,824	48.0
Interest	157	144	-8.8	221	435	97.1
PBT	5,439	6,829	25.6	16,111	20,678	28.3
Extraordinary inc/(exp)	0.0	0.0		0.0	0.0	
Tax	1,676	2,158	28.8	4,978	6,345	27.5
Net Profit	3,764	4,671	24.1	11,134	14,332	28.7
<i>Net Margin %</i>	10.2	10.0		10.9	10.9	
EPS	13.0	16.2	24.1	38.5	49.6	28.7
CEPS	15.7	19.2	22.5	45.4	58.5	28.7

Profit & Loss Account

Mar ending (Rs mn)	FY07	FY08E	FY09E	FY10E
Net Sales	145,922	185,558	224,881	266,338
Growth YoY %	21.6	27.2	21.2	18.4
Operating Expenses				
Raw Materials	110,637	141,612	172,027	204,383
% of sales	75.8	76.3	76.5	76.7
Staff Costs	2,884	4,212	5,019	5,945
% of sales	2.0	2.3	2.2	2.2
Other Expenses	13,198	15,772	19,115	22,905
% of sales	9.0	8.5	8.5	8.6
EBIDTA	19,203	23,961	28,720	33,105
Growth %	21.7	24.8	19.9	15.3
EBIDTA %	13.2	12.9	12.8	12.4
Depreciation	2,714	3,968	5,092	6,387
EBIT	16,489	19,993	23,627	26,718
Other Income	6,601	8,326	9,995	11,290
Interest	376	998	924	1,024
PBT	22,714	27,321	32,698	36,984
Extraordinary inc/(exp)	0	0	0	0
Tax	7,178	8,196	9,809	11,095
Net Profit	15,536	19,124	22,889	25,889
NPM %	10.6	10.3	10.2	9.7
EPS	53.8	66.2	79.2	89.6
CEPS	63.2	79.9	96.9	111.7

Cash Flow

Mar ending (Rs mn)	FY07	FY08E	FY09E	FY10E
Net Profit before tax	22,714	27,321	32,698	36,984
Add: Depreciation	2,714	3,968	5,092	6,387
Add: Interest	376	998	924	1,024
Less: Other income	6,601	8,326	9,995	11,290
Dec/ (Inc) in Working capital	4,292	(4,870)	(2,929)	(2,542)
Other non operating items	(3,137)			
Less: Tax paid	6,352	8,196	9,809	11,095
Cash from operations	20,280	10,895	15,982	19,468
Capex	(13,832)	(14,845)	(17,990)	(23,970)
Investments and Others	(13,191)	(4,000)	(4,000)	(4,000)
Other income	2,655	8,326	9,995	11,290
Cash from Investing activities	(24,368)	(10,519)	(11,996)	(16,681)
Borrowings	5,591	4,740	1,000	1,500
Interest paid	(280)	(998)	(924)	(1,024)
Dividend paid	(1,011)	(1,899)	(2,140)	(2,420)
Cash from financing activities	4,300	1,843	(2,063)	(1,944)
Cash generation during the year	212	2,219	1,923	844
Opening Balance	14,016	14,228	16,447	18,370
Closing Balance	14,228	16,447	18,370	19,213

Balance Sheet

Mar ending (Rs mn)	FY07	FY08E	FY09E	FY10E
Share Capital	1,445	1,445	1,445	1,445
Reserves	67,094	84,319	105,068	128,537
Owned Funds	68,539	85,764	106,513	129,982
Secured Loans	635	4,035	5,035	6,535
Unsecured Loans	5,673	7,013	7,013	7,013
Loan Funds	6,308	11,048	12,048	13,548
Deffered Tax Liability	1,675	1,675	1,675	1,675
Total	76,522	98,487	120,236	145,205
Gross Fixed Assets	61,468	76,313	94,303	118,273
Acc. Depreciation	34,871	38,839	43,932	50,318
Net Fixed Assets	26,597	37,473	50,371	67,955
Capital WIP	2,389	2,389	2,389	2,389
Net Block	28,986	39,862	52,760	70,344
Investments	34,092	38,092	42,092	46,092
Sundry Debtors	7,474	10,751	13,017	15,323
Inventory	7,132	8,959	12,294	15,323
Cash & Bank	14,228	16,447	18,370	19,213
Advances	9,241	13,080	16,629	20,507
Other Current Assets	384	384	384	384
Current Assets	38,459	49,620	60,693	70,751
Liabilities	20,110	21,008	25,501	30,320
Provisions	4,905	8,080	9,808	11,662
Current Liabilities	25,015	29,087	35,309	41,982
Net Current Assets	13,444	20,533	25,384	28,769
Total	76,522	98,487	120,236	145,205

Valuation Summary

Mar ending (Rs mn)	FY07	FY08E	FY09E	FY10E
Per Share Data				
EPS	53.8	66.2	79.2	89.6
Cash EPS	63.2	79.9	96.9	111.7
BVPS	237	297	369	450
Valuation ratio				
P/E	15.7	12.8	10.7	9.4
Cash P/E	13.4	10.6	8.7	7.6
P/BV	3.6	2.8	2.3	1.9
EV/EBIDTA	10.5	8.4	6.8	5.8
Return Ratios %				
AROE	25.2	24.8	23.8	21.9
AROCE	24.0	23.0	21.8	20.3
Dupont				
NPM %	10.6	10.3	10.2	9.7
Sales/TA	1.4	1.5	1.4	1.4
TA/Equity	1.5	1.5	1.5	1.4
Other key ratios				
D/E	0.1	0.1	0.1	0.1
NCA/Sales %	9.2	11.1	11.3	10.8

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