

New launches and export recovery to drive growth

Q3 FY18 in line with expectations

Bajaj Auto posted better than expected numbers at the topline as 17.6% yoy growth in volumes and 1% rise in realisations led to an 18.7% growth at the top line. This was on the back of low base of last year and recovery in the exports markets. Although domestic volumes declined 6.5% YTD, exports volumes grew by 11.3% YTD on strong surge in markets like Nigeria, ASEAN countries and other African markets. Margins came in at 19.7% as RM prices grew yoy as metal prices and other expenses grew on higher CSR expenses at ₹400 mn. Lower other income and higher tax rate at 31.1% with lower benefits from PN plant led to net profits slightly lower than street expectations at ₹9.52 bn which was 14% lower yoy.

New launches, 3W permits to drive volumes beyond FY18

Bajaj is currently at 4% fall YTD by the end of January on the domestic motorcycle business. Rising competition, low growth rate on the product portfolio and lesser success on the recent launches had led to this kind of performance. Going forward, new launches and upgrades may pour life into the dragging business of motorcycle in the domestic markets. Expansion of the Avenger family with two new products, an all new Discover and V family upgrade with fill in Bajaj's stable. The existing products of CT100 and Platina are expected to do well in Q1 of FY19 on marriage season demand and the Pulsar higher cc model is expected to do well. The company which off late has lost market share and currently has about 17-18%; targets to reach 21% by FY18E end on the back of new Discover, averaging 210,000 units per month for the last quarter. The existing Discover portfolio has also started looking up strongly as it grew by 31% yoy from 119,000 units. On the 3W front too, opening of permits in Delhi and Karnataka will be the biggest kickers and small quantum opening in Kolkata Na TN shall add little volumes to it further. Diesel 3W market share has gone up from 24% to 31% yoy and is expecting to move further ahead. We therefore expect recovery in demand hereon in the overall domestic business.

Exports business witnesses strong tailwinds

Exports sales in Q3 had seen green shoots post huge double digit dips in FY17. Q1 onwards, exports sales jumped significantly. Entry into new geographies such as Turkey, Iran and SE Asia and success of 3W in Nepal, Bangladesh, South East Asia, Philippines and Egypt led to a 16% YTD growth in exports. African continent(42%) that too mainly Nigeria is driving the sales from Q3. Since the dismally low numbers over there, the company has risen from it and has sold ~27,000 2W and ~7,000 3W in Q3. Furthermore, ASEAN markets like Philippines, Cambodia, Malaysia, Myanmar and Middle East markets such as Iraq and Turkey are behaving strongly as new markets. Management expects 10-12% growth in FY18E and then on a sustainable basis, which we think is quite possible.

Management's estimate of 19-20% margins for FY18E seems quite achievable

The company posted lower than expected 19.7% margins in Q3 as CSR expenses moved up. However, price hikes planned in 2W business and product mix will start showing its impact from Q4. Stable rupee will prevent any gain to fall from exports realizations. Expected 3W sales bump up will enable margins to move up from current levels. Exports surge will further lead to strengthening of margins. Shift of demand from Boxer 100 to Boxer 150 in Africa will stop fall in margins in exports as low margin Boxer sales in increases. So hereon we expect a strong margin surge negating the impact of RM costs hike. Management's guidance of 19-20% margins for FY18E seems very much within the reach. We have still factored in conservative margins at 19.4%/19.9%/20.6% margins for FY18E/19E/20E respectively.

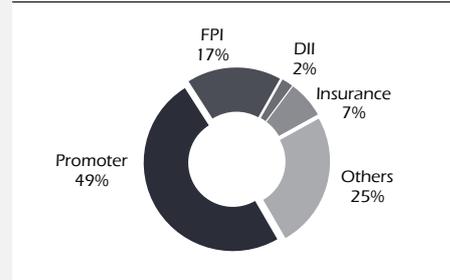
Stock Data

| | |
|--------------------------|---------------|
| Current Market Price (₹) | 3,174 |
| Target Price (₹) | 3,641 |
| Potential upside (%) | 15 |
| Reuters | BAJA.BO |
| FV (₹) | 10 |
| Bloomberg | BJAUT IN |
| Market Cap (₹ bn) | 920 |
| 52-Week Range (₹) | 3,473 / 2,695 |

What's changed

| | |
|---------------------------|---------------------|
| 12 month Price Target (₹) | From 3,120 to 3,641 |
| FY2018E EPS (₹) | From 143 to 143.7 |
| FY2019E EPS (₹) | From 159 to 158.4 |
| FY2020E EPS (₹) | 181.6 |

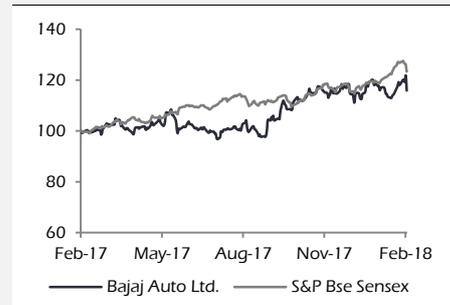
Shareholding Pattern



Fiscal YE

| YE Mar | FY17 | FY18E | FY19E | FY20E |
|--------------------|-------|-------|-------|-------|
| Revenues(₹ bn) | 217.7 | 251.8 | 280.6 | 318.6 |
| EBITDA (%) | 20.3 | 19.4 | 19.9 | 20.6 |
| PAT (%) | 17.9 | 16.8 | 16.6 | 16.7 |
| EPS (₹) | 132.3 | 143.7 | 158.4 | 181.6 |
| EPS growth (%) | 4.8% | 8.7% | 10.2% | 14.7% |
| P/E (x) | 24.1 | 22.2 | 20.1 | 17.6 |
| P/B(x) | 5.4 | 4.4 | 3.7 | 3.1 |
| EV/EBITDA (x) | 21.0 | 19.1 | 16.7 | 14.2 |
| ROE (%) | 22.5% | 20.0% | 18.4% | 17.7% |
| Dividend yield (%) | 0.2% | 0.5% | 0.5% | 0.6% |

Relative Price Performance



Ashwin Patil

ashwin_patil@lkpsec.com

+91 22 6635 1271

Financial Highlights

| All fig in (₹mn) | Q3 FY18 | Q2 FY18 | % qoq | Q3 FY17 | % yoy |
|-------------------|----------|----------|-----------|----------|-----------|
| Net sales | 62,462.3 | 64,747.8 | -3.5% | 49,755.6 | 25.5% |
| Other op. income | 1,231.1 | 1,051.3 | 17.1% | 913.3 | 34.8% |
| Total income | 63,693 | 65,799 | -3.2% | 50,669 | 25.7% |
| RM cost | 43,547 | 45,492 | -4.3% | 33,841 | 28.7% |
| Employee cost | 2,652 | 2,644 | 0.3% | 2,427 | 9.3% |
| Other expenses | 5,180 | 4,679 | 10.7% | 3,962 | 30.7% |
| EBITDA | 12,315 | 12,984 | -5.2% | 10,439 | 18.0% |
| EBITDA Margins % | 19.7 | 20.1 | (40 bps) | 21.0 | (130 bps) |
| Other income | 2,269 | 2,964 | -23.5% | 3,193 | -28.9% |
| Depreciation | 747 | 770 | -3.0% | 772 | -3.2% |
| Interest | 3 | 5 | N/A | 3 | N/A |
| PBT | 13,833 | 15,174 | -8.8% | 12,858 | 7.6% |
| Tax | 4,309 | 4,055 | 6.3% | 3,612 | 19.3% |
| Adj PAT | 9,524 | 11,119 | -14.3% | 9,246 | 3.0% |
| Adj PAT Margins% | 15.0 | 16.9 | (190 bps) | 18.2 | (320 bps) |
| Exceptional items | - | - | - | - | - |
| Reported PAT | 9,524 | 11,119 | -14.3% | 9,246 | 3.0% |

Outlook and valuation

On the domestic motorcycle front we believe that the company will perform well hereon through the comeback of Discover model sales and new launches of Discover, Avenger refreshes and V family upgrades. We expect market share to move up from the current levels, as seen in January. On the 3W business front, triggers from Karnataka, Delhi, Kolkata and TN will lead to the passenger 3W segment sales moving up. On the exports front, we are seeing a strong growth through entry into new geographies like Turkey and Iran. The most heartening sign is Nigeria coming back to normalcy, with volumes surging in both 2w as well as 3W business. Egypt too has gain stability. On the back of this, margins are expected to move up on high margin 3W and exports and price hikes taken recently. Extinction of the Pantnagar (~25% of domestic production) tax benefits from Q4 may lead to increase in tax rate(~30%) from the ensuing quarters, which may result into bottomline getting a bit depressed. The effect of that was seen in Q3 as well. On the other hand, higher other income expectations on regular FMP maturity may augur well for the bottomline on and off. We believe the risk to reward ratio is high for this company considering good bottomline growth despite the negatives stated above, clean cash rich balance sheet, robust return ratios and above all, a proxy to the domestic as well as global 2W industry. We maintain **BUY** rating on the stock with a rolled over target price of ₹3, 641 on FY20E, more or less maintaining our FY18E and FY19E estimates.

| All figs in ₹ | Q3 FY18 | Q2 FY18 | Q1 FY18 | Q4 FY17 | Q3 FY17 | Q2 FY17 | Q1 FY17 | Q4 FY16 |
|--------------------------------|---------|---------|---------|---------|---------|---------|---------|---------|
| Gross Realisation per Unit (₹) | 62,371 | 60,302 | 64,611 | 65,012 | 61,796 | 61,313 | 60,161 | 64,775 |
| Net Realisation per Unit (₹) | 62,371 | 60,428 | 59,976 | 61,006 | 58,424 | 57,652 | 56,735 | 60,793 |
| Total Cost per unit (₹) | 51,304 | 49,291 | 50,696 | 49,736 | 47,238 | 46,111 | 45,958 | 48,826 |
| Material Cost per unit (₹) | 43,483 | 42,457 | 42,876 | 42,155 | 39,736 | 39,315 | 38,832 | 40,498 |
| Staff Cost per unit (₹) | 2,648 | 2,467 | 3,067 | 2,886 | 2,850 | 2,507 | 2,697 | 2,324 |
| Other Expn per unit (₹) | 5,251 | 4,405 | 4,804 | 4,792 | 4,707 | 4,344 | 4,472 | 6,064 |
| EBITDA per unit (₹) | 12,296 | 12,118 | 10,561 | 12,442 | 12,258 | 12,560 | 11,826 | 13,199 |
| PAT per unit (₹) | 9,510 | 10,377 | 10,759 | 11,119 | 10,857 | 10,881 | 9,836 | 9,204 |

Financials
Income statement

| YE Mar (₹.mn) | FY17 | FY18E | FY19E | FY20E |
|-----------------------|----------------|----------------|----------------|----------------|
| Total Revenues | 217,667 | 251,838 | 280,600 | 318,609 |
| Raw Material Cost | 146,242 | 173,347 | 191,061 | 212,830 |
| Employee Cost | 9,971 | 10,648 | 11,596 | 12,870 |
| Other Exp | 17,231 | 18,665 | 21,664 | 26,782 |
| EBITDA | 44,223 | 48,732 | 55,833 | 65,527 |
| EBITDA Margin(%) | 20.3 | 19.4 | 19.9 | 20.6 |
| Other income | 12220 | 13000 | 13500 | 14000 |
| Depreciation | 3,073 | 3,136 | 3,835 | 4,420 |
| Interest | 14 | 15 | 20 | 25 |
| PBT | 53,356 | 58,582 | 65,479 | 75,082 |
| PBT Margin(%) | 25.0 | 23.7 | 23.7 | 23.9 |
| Exceptional items | 0 | 0 | 0 | 0 |
| Tax | 15,081 | 16,989 | 19,644 | 22,525 |
| APAT | 38,275 | 41,593 | 45,835 | 52,557 |
| APAT Margins (%) | 17.6 | 16.5 | 16.3 | 16.5 |
| PAT | 38,275 | 41,593 | 45,835 | 52,557 |
| PAT Margin (%) | 17.9 | 16.8 | 16.6 | 16.7 |

Key Ratios

| YE Mar | FY17 | FY18E | FY19E | FY20E |
|---------------------------------|-------|-------|-------|--------|
| Per Share Data (₹) | | | | |
| Adj. EPS | 132.3 | 143.7 | 158.4 | 181.6 |
| CEPS | 136.8 | 142.9 | 154.6 | 171.6 |
| BVPS | 588.6 | 718.0 | 860.5 | 1023.9 |
| DPS | 7.0 | 14.4 | 15.8 | 18.2 |
| Growth Ratios (%) | | | | |
| Total revenues | -4.1% | 15.7% | 11.4% | 13.5% |
| EBITDA | -7.5% | 10.2% | 14.6% | 17.4% |
| PAT | 4.8% | 8.7% | 10.2% | 14.7% |
| EPS Growth | 4.8% | 8.7% | 10.2% | 14.7% |
| Valuation Ratios (x) | | | | |
| PE | 24.1 | 22.2 | 20.1 | 17.6 |
| P/CEPS | 22.3 | 20.6 | 18.6 | 16.2 |
| P/BV | 5.4 | 4.4 | 3.7 | 3.1 |
| EV/Sales | 4.2 | 4.4 | 3.8 | 3.4 |
| EV/EBITDA | 21.0 | 19.1 | 16.7 | 14.2 |
| Operating Ratios (Days) | | | | |
| Inventory days | 12.4 | 15.0 | 16.0 | 17.0 |
| Receivable Days | 16.3 | 18.0 | 20.0 | 24.0 |
| Payables day | 38.2 | 36.0 | 34.0 | 31.0 |
| Net Debt/Equity (x) | 0.04 | 0.04 | 0.03 | 0.03 |
| Profitability Ratios (%) | | | | |
| ROE | 22.5% | 20.0% | 18.4% | 17.7% |
| Dividend yield | 0.2% | 0.5% | 0.5% | 0.6% |

Source: Company, LKP Research

Balance sheet

| YE Mar (₹mn) | FY17 | FY18E | FY19E | FY20E |
|-------------------------------------|----------------|----------------|----------------|----------------|
| EQUITY AND LIABILITIES | | | | |
| Shareholder's funds | | | | |
| Share capital | 2,894 | 2,894 | 2,894 | 2,894 |
| Reserves and surplus | 167,448 | 204,881 | 246,133 | 293,435 |
| Total networkth | 170,341 | 207,775 | 249,027 | 296,328 |
| Non current liabilities | | | | |
| Long term borrowings and provisions | 2,545 | 2,695 | 2,845 | 2,945 |
| Deferred tax liabilities | 3,136 | 3,276 | 3,416 | 3,616 |
| Current liabilities | | | | |
| Current liabilities and provisions | 23,567 | 25,782 | 27,232 | 28,381 |
| Other current liabilities | 8,559 | 10,855 | 12,859 | 15,480 |
| Total equity and liabilities | 208,148 | 250,383 | 295,379 | 346,751 |
| ASSETS | | | | |
| Net block | 18,986 | 20,851 | 27,016 | 31,596 |
| Capital work in progress | 106 | 306 | 506 | 706 |
| Intangible assets | 762 | 1,323 | 1,523 | 1,723 |
| Non current investments | 87,398 | 97,398 | 107,398 | 122,398 |
| Long term loans and advances | 297 | 397 | 497 | 597 |
| Other non current assets | 6,684 | 6,684 | 6,684 | 6,684 |
| Total non current assets | 114,234 | 126,960 | 143,625 | 163,706 |
| Current assets | | | | |
| Current investments | 60,501 | 80,501 | 100,501 | 120,501 |
| Inventories | 7,283 | 10,177 | 12,103 | 14,620 |
| Trade receivables | 9,533 | 12,212 | 15,129 | 20,641 |
| Cash and cash bank | 2,937 | 5,364 | 6,842 | 8,094 |
| Short term loans and advances | 65 | 75 | 85 | 95 |
| Other current assets | 13,595 | 15,095 | 17,095 | 19,095 |
| Total current assets | 93,913 | 123,423 | 151,754 | 183,045 |
| Total Assets | 208,148 | 250,383 | 295,379 | 346,751 |

Cash Flow

| YE Mar (₹ mn) | FY17 | FY18E | FY19E | FY20E |
|--------------------------------------|-----------------|-----------------|-----------------|-----------------|
| PBT | 53,356 | 58,582 | 65,479 | 75,082 |
| Depreciation | 3,073 | 3,136 | 3,835 | 4,420 |
| Interest | 14 | 15 | 20 | 25 |
| Chng in working capital | 2,533 | (2,572) | (3,398) | (6,269) |
| Tax paid | (15,026) | (16,989) | (19,644) | (22,525) |
| Other operating activities | 0 | 0 | 0 | 0 |
| Cash flow from operations (a) | 33,393 | 37,893 | 43,990 | 48,282 |
| Capital expenditure | (1,994) | (5,200) | (10,200) | (9,200) |
| Chng in investments | (28,243) | (30,000) | (30,000) | (35,000) |
| Other investing activities | 0 | 0 | 0 | 0 |
| Cash flow from investing (b) | (36,883) | (34,702) | (41,615) | (45,615) |
| Free cash flow (a+b) | (3,491) | 3,191 | 2,375 | 2,667 |
| Inc/dec in borrowings | 0 | 0 | 0 | 0 |
| Dividend paid (incl. tax) | (1,728) | (4,159) | (4,583) | (5,256) |
| Other financing activities | 0 | 0 | 0 | 0 |
| Cash flow from financing (c) | (1,886) | (618) | (897) | (1,415) |
| Net chng in cash (a+b+c) | (5,376) | 2,572 | 1,478 | 1,252 |
| Closing cash & cash equiv | 2,791 | 5,364 | 6,842 | 8,094 |

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