kotak Securities

Company Update

MARUTI SUZUKI INDIA LTD (MSIL)

PRICE RS.7287 **TARGET RS.8522** **BUY**

Passenger vehicle industry witnessed slowdown in 2QFY19 due to floods in Kerala, delayed festive season and some softening in demand. While in the near term, growth is expected to be slow, medium to long term growth outlook for the industry stays intact.

Stock Details

Market cap (Rs mn)	:	2201318
52-wk Hi/Lo (Rs)	:	10000 / 6650
Face Value (Rs)	:	5
3M Avg. daily vol (Nos)	:	760,976
Shares o/s (mn)	:	302

Source: Bloomberg

Financial Summary

Y/E Mar (Rs mn)	FY18	FY19E	FY20E
Revenue	797,627	901,384	1060,457
Growth (%)	17.2	13.0	17.6
EBITDA	120,615	129,303	164,372
EBITDA margin (%)	15.1	14.3	15.5
PAT	77,218	85,561	111,922
EPS	255.6	283.2	370.5
EPS Growth (%)	5.1	10.8	30.8
BV (Rs/share)	1,382	1,569	1,843
Dividend/share (Rs)	80.0	80.0	80.0
ROE (%)	19.8	19.2	21.7
ROCE (%)	28.4	26.9	30.3
P/E (x)	28.5	25.7	19.7
EV/EBITDA (x)	18.2	16.9	13.3
P/BV (x)	5.3	4.6	4.0

Source: Company, Kotak Securities - PCG

Shareholding Pattern (%)

(%)	Jun-18	Mar-18	Dec-17
Promoters	56.2	56.2	56.2
FII	23.7	25.2	25.8
DII	12.7	11.5	11.0
Others	7.4	7.2	7.0

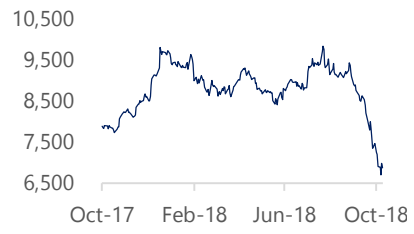
Source: Company

Price Performance (%)

(%)	1M	3M	6M
Maruti Suzuki	(14.2)	(22.0)	(20.8)
Nifty	(7.9)	(5.0)	0.1

Source: Bloomberg

Price chart (Rs)



Source: Bloomberg

Key Highlights

We believe that slowdown in industry sales to have limited impact on MSIL due to production capacity constraint and market share gains. Domestic passenger vehicle industry grew by ~7% in 1HFY19 (de-grew in 2QFY19). MSIL's growth during the same period stood at 11%, market share gain of 170bps. In the past nine months, INR has depreciated against JPY by ~12%. Accordingly we expect adverse forex movement to impact MSIL's EBITDA margin in FY19. In FY20, we expect EBITDA margin to see some improvement on expectation of price hikes, operating leverage and vendor localization at Gujarat plant.

Valuation

In view of adverse forex movement, we cut our EBITDA estimates by 9% for FY19 and 6.7% for FY20. We also lower PE multiple to 23x (from 25x) due to near term slowdown in demand and margin headwinds. We rate the stock as BUY with revised price target of R8,522 (earlier 10,360). Lower than expected volume growth, commodity cost increase and unfavourable currency movement are key risks to our target price.

Industry outlook – near term headwinds; long term remains positive

Domestic passenger vehicle industry slowed down considerably in 2QFY19, in comparison with growth witnessed in recent quarters. Reasons that led to domestic passenger vehicle industry de-growing YoY in 2QFY19 includes floods in Kerala, delayed festive season and some softening in demand.

Post floods, passenger vehicle demand in Kerala (accounts for 8% of domestic volumes) came down significantly in August and September impacting industry sales to certain extent. We expect the demand in Kerala to recover gradually in coming quarters. Furthermore, the base of 2QFY18 was also on the higher side (volume growth in 2QFY18 grew by 13% vs 8% growth in FY18), thereby impacting growth. Festive season dealer inventory build-up happened in 2QFY18 and this year the same is spread out in 2QFY19 and 3QFY19. Higher fuel prices and increase in interest cost is likely to have dampened consumer sentiment to some extent and that is likely to continue in the near term. On the back of above mentioned factors, growth for the passenger car industry is expected to be slightly lower in 2HFY19 as compared with 1HFY19.

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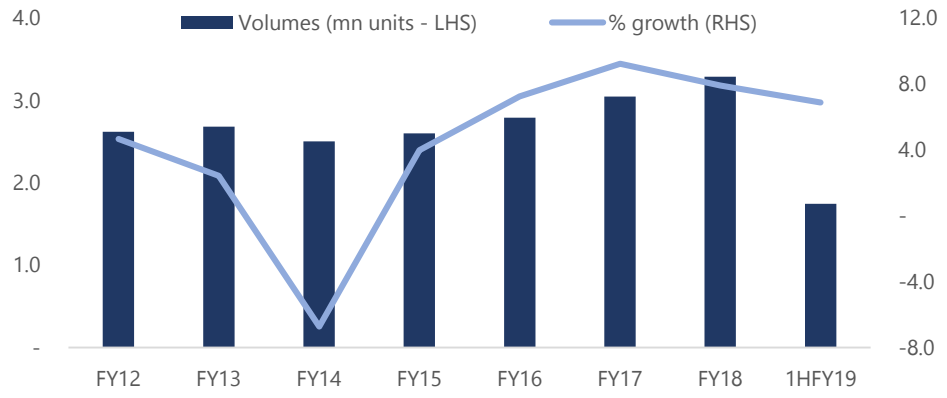
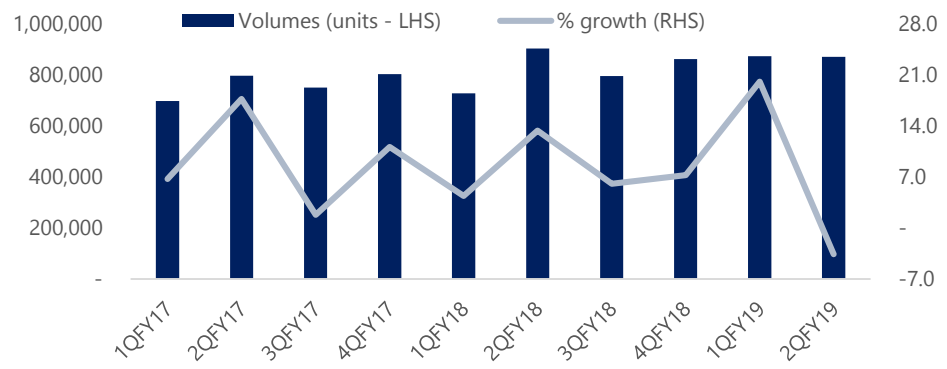
Domestic passenger vehicle industry volumes



Source - SIAM

Domestic passenger vehicle industry - 2QFY19 volume declined partly due to high base



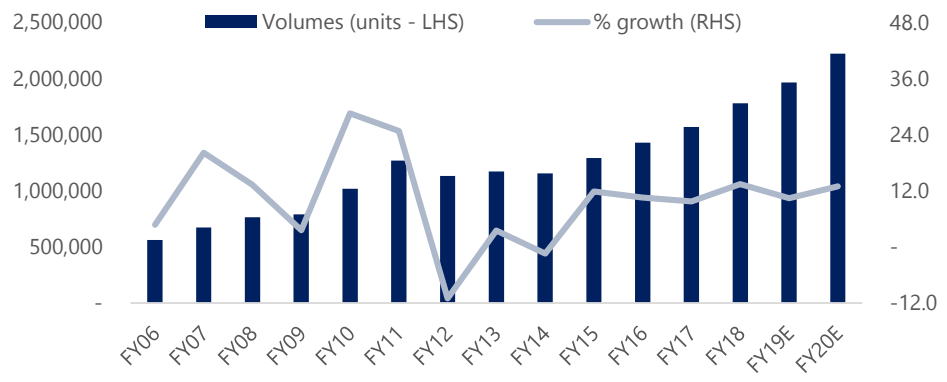
Source - SIAM

In the past seven years (FY12-FY18), volume CAGR in the domestic passenger vehicle industry has been at 4%, much lower than volume CAGR of 16% reported during FY07-FY12. Over the longer term, favourable domestic story (improving income and consumption levels) coupled with low penetration levels provides a huge upside opportunity for the passenger car players in the domestic market.

Slowdown in industry sales to have limited impact on Maruti's volumes

We believe that slowdown in industry sales to have limited impact on MSIL due to production capacity constraint and market share gains. Given capacity constraints, MSIL's production in FY19 is expected to grow by ~10 to 12% and thereby any upside in sales volume growth is restricted. In 1HFY19, MSIL has reported 10% YoY volume growth (11.3% growth in domestic segment) and we expect similar growth for the company going ahead in 2HFY19. Given capacity constraints, MSIL's focus in the past few years has been on the domestic segment. In a scenario of slowdown in domestic demand, MSIL will likely focus on exports (down by 8% in 1HFY19) to utilize spare capacity.

MSIL volume growth

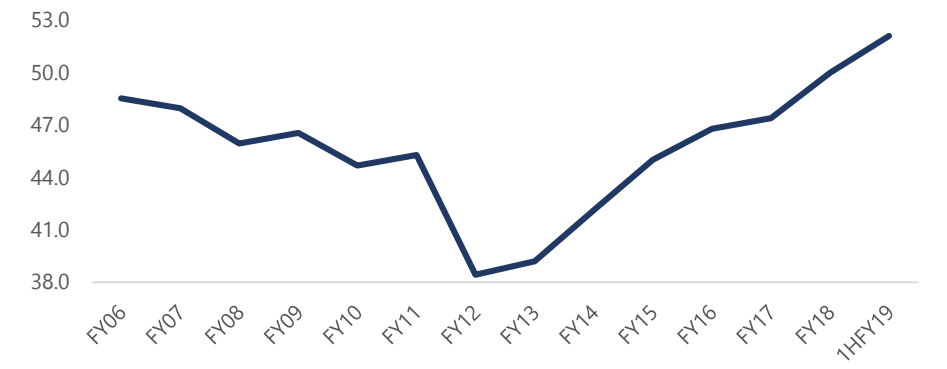


Source: Company, Kotak Securities – Private Client Research

As against competitors, we believe the impact of demand slowdown will be relatively lower on MSIL (and thereby continue to outperform industry growth) on following reasons – strong product portfolio, customer preference for petrol engine and significant volume share from rural segment.

MSIL has widest range in its product portfolio that covers 85% of the industry (in terms of volumes) and makes them less vulnerable to shift in demand within segments. Further, MSIL has least dependence on its top selling model (~16% in FY18). In the past few years, there has been meaningful shift towards petrol vehicles (from 47% in FY14 to 60% in FY18). Given higher fuels prices and emission concerns related to diesel vehicles, we believe demand to stay in favour of petrol vehicles. MSIL is strong player in the petrol vehicle segment (contributes 70% of company volume. Any further shift in demand to petrol vehicle will be positive for MSIL.

MSIL gaining market share for seventh consecutive year



Source: SIAM

Strong presence in rural areas has helped the company tide competitive pressure and demand slowdown in urban areas. Currently, around one third domestic volumes comes through rural sales. In FY18, the top ten cities showed weak demand, whereas non-urban markets witnessed healthy demand. Management had highlighted in 1QFY19 that rural retail demand is growing by 15%. In our view, MSIL will continue concentrating on further improving rural sales on following counts. Firstly, the future growth of the industry will continue to be driven by non-metro cities and rural areas. Secondly, lower penetration levels in rural areas provide with more growth opportunities as compared with metros and large cities. Thirdly, competitive pressure is low as competition's distribution network is largely limited to bigger cities. Fourthly, expanding footprints in rural India is giving MSIL a first mover advantage.

Unfavourable foreign currency movement is near term headwind to margins

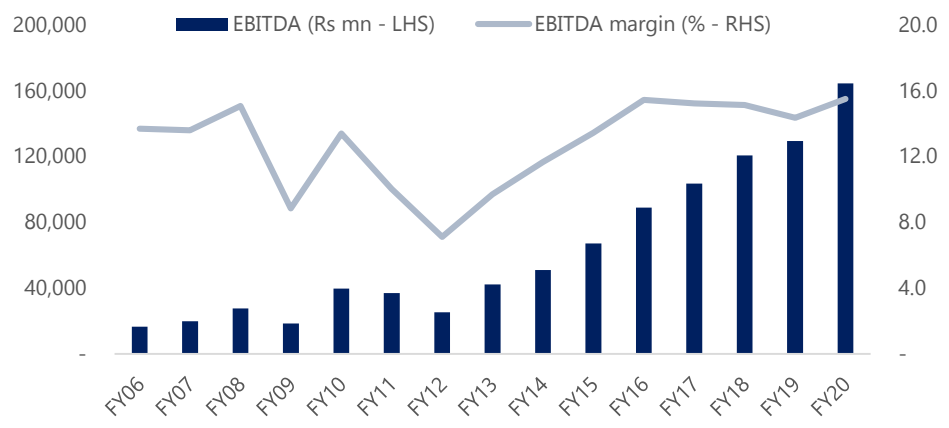
MSIL has foreign currency exposure to currencies like yen, euro and dollar. MSIL's direct forex exposure stands at around 10% of its net sales (relates to raw material imports and royalty payment). Taking into account the exposure of its vendors (raw material imports), the indirect exposure stands at around 10% of the company's net sales. Combined, MSIL's overall gross forex exposure (mainly JPY) is ~20% of its net sales.

For direct imports, MSIL has 50% cover for USD/JPY exposure and for USD/INR exposure, 50% is covered by way of natural hedge and balance 50% exposure there are no hedges. For royalty, two third payments happen in JPY. MSIL compensates its vendors with a lag of one quarter (takes preceding quarters average rate into consideration).

In the past nine months, INR has depreciated against JPY by ~12%. Accordingly we expect adverse forex movement to impact MSIL's EBITDA margin in FY19.

In FY20, we expect EBITDA margin to see some improvement on expectation of price hikes to offset commodity prices and adverse forex movements. Almost all MNC in the passenger vehicle segment operating in India have import content higher as compared to MSIL. Thereby, majority companies in the passenger vehicle segment will be facing pressure on margins from INR depreciation. We thereby see a possibility of price increase in the coming months and that should alleviate pressure on margins. In August 2018, MSIL's announced a price hike owing to increase in commodity cost and adverse foreign exchange rates. Ramp-up at Gujarat plant will provide operating leverage. Further, vendor localization at Gujarat plant is relatively low and is expected to increase over the next few years. Logistics cost will come down with higher vendor localization

MSIL's EBITDA and EBITDA margin



Source: Company, Kotak Securities – Private Client Research

Valuation and Outlook

In view of adverse forex movement, we cut our EBITDA estimates by 9% for FY19 and 6.7% for FY20. We also lower our other income estimates. Accordingly, we cut our net profit estimates by 11.7% for FY19 and 10.6% for FY20. Due to near term slowdown in demand and margin headwinds, we revise our PE multiple to 23x (from 25x) – in line with past four years average one year forward PE multiple. We rate the stock as BUY with revised price target of Rs8,522 (earlier Rs10,360)

Key Risk

Lower than expected volume growth, commodity cost increase and unfavourable currency movement are key risks to our target price.

About the company

Maruti Suzuki India (MSIL), India's largest passenger car company, is a subsidiary of Suzuki Motor Corporation of Japan. Formed as a government owned company, it entered into a JV with Suzuki Motor Corporation. Over the years the company has been one the most successful player in the Indian car market. Currently the company is the market leader with ~50% market share and on a solid footing with a dense sales and service network. MSIL's strong network helps them sell their products to virtually every nook and corner of the country. MSIL's combined annual production capacity is about 1.5mn units in the Gurugram and Manesar facilities. In Gujarat, Suzuki Motor Corporation has set up a facility which it plans to scale-up in the coming years.

Financials: Standalone

Profit and Loss Statement (Rs mn)

(Year-end Mar)	FY17	FY18	FY19E	FY20E
Revenues	**680,348**	**797,627**	**901,384**	**1060,457**
% change YoY	18.2	17.2	13.0	17.6
EBITDA	**103,517**	**120,615**	**129,303**	**164,372**
% change YoY	16.5	16.5	7.2	27.1
Depreciation	26,021	27,579	29,280	32,360
EBIT	**77,496**	**93,036**	**100,023**	**132,011**
% change YoY	27.8	20.1	7.5	32.0
Net interest	894	3,457	750	650
Other Income	23,001	20,455	22,090	27,393
Exceptional income/(loss)	-	-	-	-
Profit before tax	99,603	110,034	121,363	158,754
% change YoY	33.8	10.5	10.3	30.8
Tax	26,101	32,816	35,802	46,833
as % of PBT	26.2	29.8	29.5	29.5
Profit after tax	**73,502**	**77,218**	**85,561**	**111,922**
Adjusted PAT	**73,502**	**77,218**	**85,561**	**111,922**
% change YoY	37.0	5.1	10.8	30.8
Shares outstanding (m)	302	302	302	302
Adjusted EPS (Rs)	**243.3**	**255.6**	**283.2**	**370.5**
DPS (Rs)	75.0	80.0	80.0	80.0

Source: Company, Kotak Securities – Private Client Research

Balance sheet (Rs mn)

(Year-end Mar)	FY17	FY18	FY19E	FY20E
Cash and cash equivalents	21,926	12,884	15,132	13,656
Accounts receivable	11,992	14,618	17,287	20,338
Inventories	32,622	31,608	40,732	47,757
Loans and Adv & Others	37,494	39,013	42,756	46,880
Current assets	104,034	98,123	115,907	128,631
LT investments	263,022	340,729	390,091	480,091
Net fixed assets	145,450	154,849	165,569	173,209
Total assets	**512,506**	**593,701**	**671,567**	**781,930**
Payables	83,673	104,970	116,069	136,552
Other liabilities	50,315	58,596	64,456	70,901
Current Liabilities	133,988	163,566	180,524	207,453
Provisions	4,709	5,865	6,452	7,097
Deferred Tax Liability	4,662	5,589	5,589	5,589
Debt	4,836	1,108	5,000	5,000
Equity	1,510	1,510	1,510	1,510
Reserves	362,801	416,063	472,492	555,281
Total liabilities	**512,506**	**593,701**	**671,567**	**781,930**
BVPS (Rs)	1,206	1,382	1,569	1,843

Source: Company, Kotak Securities – Private Client Research

Cash flow Statement (Rs mn)

(Year-end Mar)	FY17	FY18	FY19E	FY20E
EBIT	77,496	93,036	100,023	132,011
Depreciation	26,021	27,579	29,280	32,360
Change in working capital	9,529	19,685	(694)	10,408
Chg in other net current asset	15,272	7,918	2,703	2,967
Operating cash flow	128,318	148,218	131,311	177,746
Interest	(894)	(3,457)	(750)	(650)
Tax	(23,382)	(31,889)	(35,802)	(46,833)
Other Income	23,001	20,455	22,090	27,393
Deferred Tax Liability	-	-	-	-
Hedge reserves /Others	4,692	3,312	1	-
CF from operations	**131,735**	**136,639**	**116,850**	**157,657**
Capex	(36,302)	(36,978)	(40,000)	(40,000)
(Inc)/dec in investments	(85,488)	(68,092)	(49,362)	(90,000)
CF from investments	**(121,790)**	**(105,070)**	**(89,362)**	**(130,000)**
Proceeds from issue of equities	-	-	-	-
Increase/(decrease) in debt	2,527	(3,728)	3,892	-
Proceeds from share premium	-	-	-	-
Dividends	(12,725)	(27,268)	(29,133)	(29,133)
CF from financing	**(10,198)**	**(30,996)**	**(25,241)**	**(29,133)**
Opening cash	391	138	711	2,959
Closing cash	138	711	2,959	1,483

Source: Company, Kotak Securities – Private Client Research

Ratio Analysis

(Year-end Mar)	FY17	FY18	FY19E	FY20E
Margins				
EBITDA margin (%)	15.2	15.1	14.3	15.5
EBIT margin (%)	11.4	11.7	11.1	12.4
Adj. net profit margin (%)	10.8	9.7	9.5	10.6
Working capital days				
Inventory (days)	18	14	16	16
Receivable (days)	6	7	7	7
Payable (days)	45	48	47	47
Ratios				
Debt/equity ratio (x)	0.0	0.0	0.0	0.0
ROE (%)	22.2	19.8	19.2	21.7
ROCE (%)	29.7	28.4	26.9	30.3
Valuations				
EV/ Sales	3.2	2.7	2.4	2.1
EV/EBITDA	21.1	18.2	16.9	13.3
Price to earnings (P/E)	29.9	28.5	25.7	19.7
Price to book value (P/B)	6.0	5.3	4.6	4.0

Source: Company, Kotak Securities – Private Client Research

RATING SCALE

Definitions of ratings

BUY	–	We expect the stock to deliver more than 12% returns over the next 12 months
ACCUMULATE	–	We expect the stock to deliver 5% - 12% returns over the next 12 months
REDUCE	–	We expect the stock to deliver 0% - 5% returns over the next 12 months
SELL	–	We expect the stock to deliver negative returns over the next 12 months
NR	–	**Not Rated.** Kotak Securities is not assigning any rating or price target to the stock. The report has been prepared for information purposes only.
SUBSCRIBE	-	We advise investor to subscribe to the IPO.
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NA	–	**Not Available or Not Applicable.** The information is not available for display or is not applicable
NM	–	**Not Meaningful.** The information is not meaningful and is therefore excluded.
NOTE	–	Our target prices are with a 12-month perspective. Returns stated in the rating scale are our internal benchmark.

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