Bajaj Corp. | BUY

Disappointing quarter

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Bajaj Corp's 3QFY18 report was disappointing as volume growth recovery turned out to be well-below our expectations. While the headline numbers were impacted by lower international turnover, domestic business volume growth of 8% was also quite subdued given a highly favourable base (BAD volumes declined 4%, overall volumes down 6.5% in 3Q LY). Reported operating performance for the quarter was partially aided by prior period income (CGST refund pertaining to earlier excise-exempt zones). Excluding this, EBITDA growth was just 2-3% due to the impact of sharp increase in SG&A (+23.7%). The company attributed the disappointment in performance to weakness in the wholesale and CSD channels. Domestic performance of skin-care (Nomarks) has improved significantly, though, and is expected to sustain. We expect the stock to face some pressure in the near-term given the weak results. Given sharp stock-price run-up in recent months (+24% in 3M), signs of a sustained recovery in volume growth trajectory would be a pre-requisite for stock to further perform, despite reasonable valuation (currently trading at 40% discount to the sector), in our view.

- **Recovery in domestic volume growth below expectations:** Bajaj Corp's 3QFY18 reported revenue and EBITDA grew 11.3% and 10.8% to INR2bn and INR678mn respectively but net profit declined 4.6% to INR552mn. Headline numbers benefited from refund of CGST credits in lieu of area-based exemptions pertaining to the Jul-Sep period. Excluding this, EBITDA growth was merely 2-3%, as per our workings, while adjusted net profit was actually down 11-12%. The company reported a volume growth of mere 5.2% on a base of 6.5% decline – a key disappointment. Volumes were impacted by sharp underperformance in the International business while domestic business volume growth was relatively better at 8.2% (remains below our expectations of 12% given a weak base). Furthermore, retail offtakes for Bajaj Almond Drops also decelerated to 4% in 3Q vs 5% in 2Q and 12% in 1Q. It has, however, managed to increase its volume/value market share by 50/30bps within the light hair-oil category for the period April-Dec'17. Nomarks' domestic volumes grew at a healthy 33%, as per management, though overall volumes fell 6.7% on account of steep decline in International business.

- **Operating margin compressed 281bps on investments behind A&P spends:** Gross margin (adjusted for prior period items as mentioned above) expanded 270bps despite steep inflation in Light Liquid Paraffin prices (26% of COGS – prices up 32% YoY) – this was aided by input-tax credit on raw materials that have now become available under GST (not available earlier as the company was enjoying excise exemption).However, EBITDA (on adjusted basis) grew a mere 2.3% as EBITDA margin compressed 281bps on sharp increase in investments behind A&P spends (+31.4%) and high staff cost inflation (+22.6%). Adjusted net profit decline was even steeper at 11.6% on 69% decline in net financial income (impacted by lower treasury income and unrealised M2M losses). Bajaj Corp has declared an interim dividend of INR12/share.

Recommendation and Price Target	
Current Reco.	BUY
Previous Reco.	BUY
Current Price Target (12M)	520
Upside/(Downside)	+3%
Previous Price Target	475
Change	+9.5%

Key Data – BJCOR IN	
Current Market Price	INR504
Market cap (bn)	INR75.1/US$1.2
Free Float	33%
Shares in issue (mn)	147.5
Diluted share (mn)	147.5
3-mon avg daily val (mn)	INR61.0/US$1.0
52-week range	525/341
Sensex/Nifty	34,503/10,651
INR/US$	63.7

Price Performance			
%	1M	6M	12M
Absolute	10.6	28.2	37.0
Relative*	7.3	17.9	7.8

* To the BSE Sensex

Financial Summary					(INR mn)
Y/E March	FY16A	FY17A	FY18E	FY19E	FY20E
Net Sales	7,975	7,948	8,439	9,904	11,616
Sales growth (%)	-3%	0%	6%	17%	17%
EBITDA	2,737	2,636	2,620	3,163	3,762
EBITDA (%)	34%	33%	31%	32%	32%
Adjusted net profit	2,333	2,327	2,240	2,636	3,063
EPS (INR)	15.8	15.8	15.2	17.9	20.8
EPS growth (%)	11%	0%	-4%	18%	16%
ROIC (%)	131%	137%	124%	122%	123%
ROE (%)	48%	48%	44%	48%	51%
PE (x)	31.9	32.0	33.2	28.2	24.3
Price/Book Value (x)	15.5	15.0	14.1	13.1	11.8
EV/EBITDA (x)	26.0	26.9	27.1	22.4	18.8
Dividend Yield (%)	3%	3%	3%	3%	3%

Source: Company data, JM Financial. Note: Valuations as of 11/Jan/2018

Exhibit 1. 3Q & 9MFY18 results snapshot (INR mn)

	3QFY18	3QFY17	YoY %	3QFY18E	% var	9MFY18	9MFY17	YoY %
Revenue	2,081	1,869	11.3%	2,100	-0.9%	6,096	5,880	3.7%
COGS	644	644	0.0%	714	-9.9%	2,005	2,009	-0.2%
Gross Profit	**1,437**	**1,225**	17.2%	**1,385**	3.7%	**4,091**	**3,871**	5.7%
Gross Profit Margin %	69.0%	65.6%	349 bps	66.0%	307 bps	67.1%	65.8%	128 bps
Staff Cost	193	157	22.6%	193	-0.3%	555	442	25.7%
Advertisement	327	249	31.4%	152	114.5%	892	783	14.0%
Other Expenses	239	207	15.2%	374	-36.0%	775	653	18.8%
EBITDA	678	612	10.8%	666	1.8%	1,868	1,994	-6.3%
EBITDA margin %	32.6%	32.8%	-15 bps	31.7%	88 bps	30.6%	33.9%	-326 bps
Depreciation	19	13	50.7%	16	20.6%	50	34	49.1%
EBIT	659	600	10.0%	651	1.4%	1,818	1,960	-7.2%
Interest Expense	3	2		2		8	7	
Financial Other Income	45	138	-67.4%	84	-46.7%	235	370	-36.6%
PBT pre-exceptional	**701**	**735**	**-4.5%**	**732**	**-4.2%**	**2,045**	**2,324**	**-12.0%**
PBT post exceptional	701	735	-4.5%	732	-4.2%	2,045	2,140	-4.4%
Taxes	150	157	-4.4%	156	-3.9%	437	457	
Net Profit	**552**	**578**	**-4.6%**	**576**	**-4.2%**	**1,609**	**1,683**	**-4.4%**
Adjusted Profit	552	578	-4.6%	576	-4.2%	1,609	1,827	-12.0%

Source: Company, JM Financial

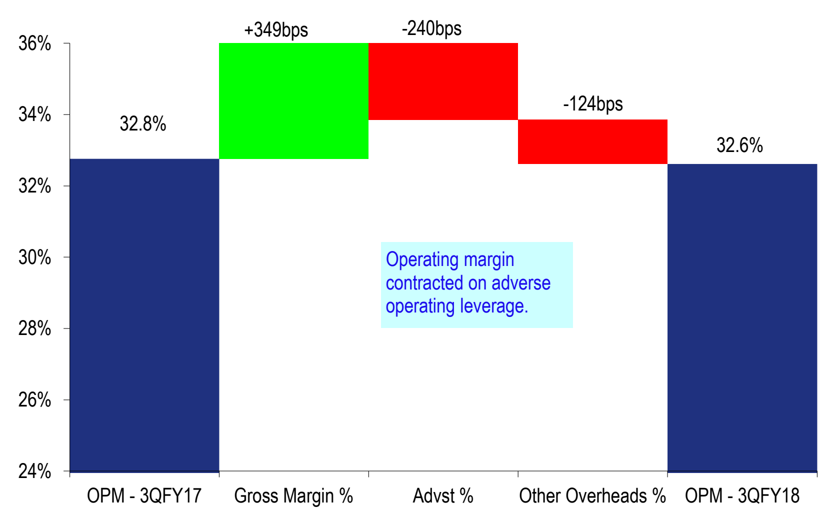
Adjusted for prior-period items	3QFY18	3QFY17	YoY %
EBITDA	626	612	2.3%
EBITDA margin - %	30.9%	33.7%	-281 bps
Net Profit	511	578	-11.6%

Exhibit 2. Costs breakdown (%)

% of revenue	3QFY18	3QFY17	3QFY18E	9MFY18	9MFY17
Cost of Goods Sold	31.0%	34.4%	34.0%	32.9%	34.2%
Staff Cost	9.3%	8.4%	9.2%	9.1%	7.5%
Advertisement	15.7%	13.3%	7.3%	14.6%	13.3%
Other Expenses	11.5%	11.1%	17.8%	12.7%	11.1%

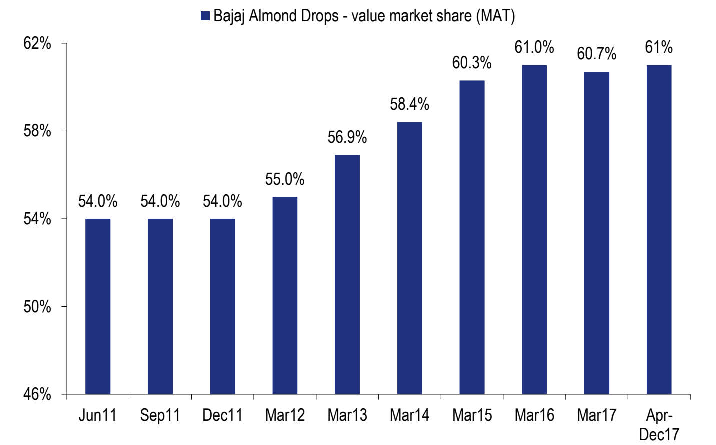
Source: Company, JM Financial

Exhibit 3. 3QFY18 Operating Margin Movement



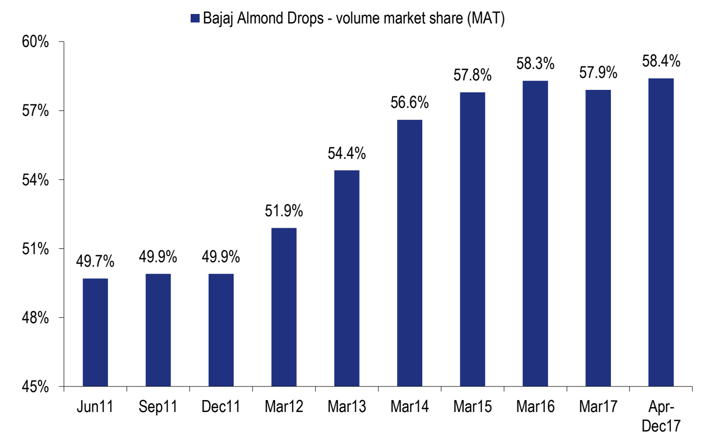
Source: Company, JM Financial

Exhibit 4. Value market share trend



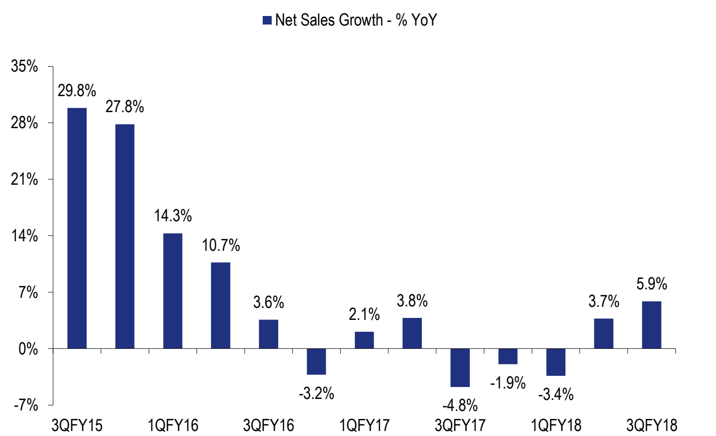
Source: Company, JM Financial

Exhibit 5. Volume market share trend



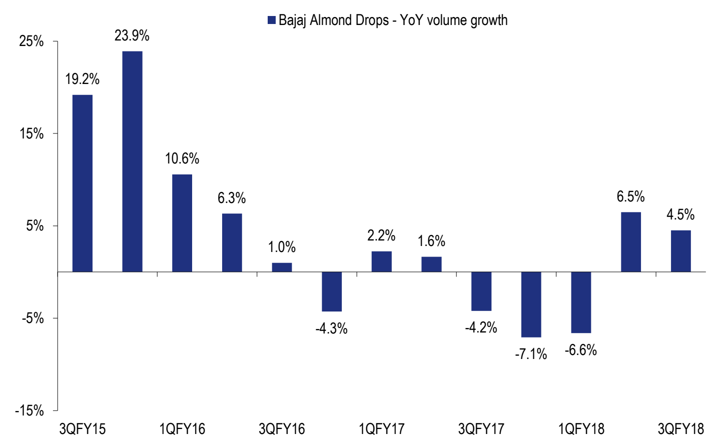
Source: Company, JM Financial

Exhibit 6. Quarterly trend – net sales growth



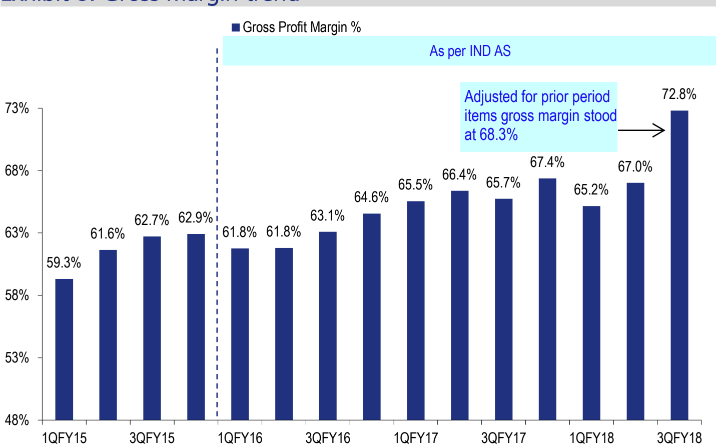
Source: Company, JM Financial

Exhibit 7. Quarterly volume growth trend



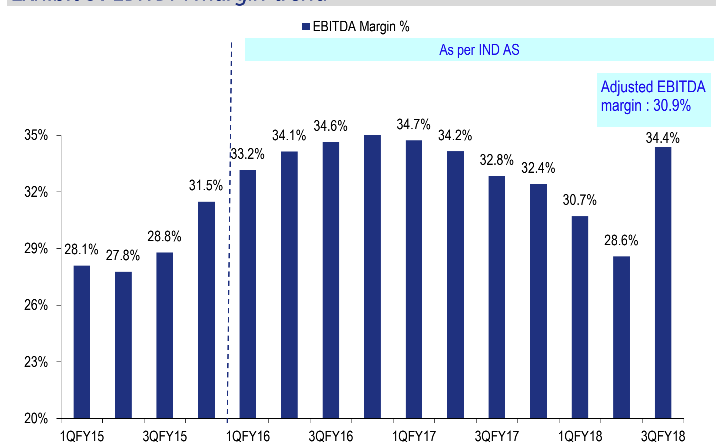
Source: Company, JM Financial

Exhibit 8. Gross margin trend



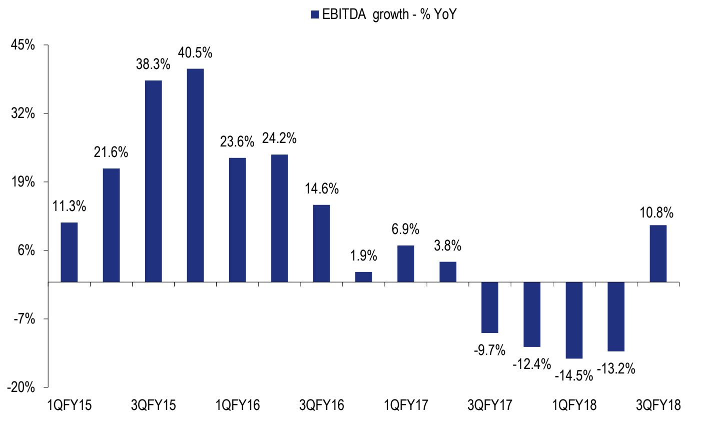
Source: Company, JM Financial

Exhibit 9. EBITDA margin trend



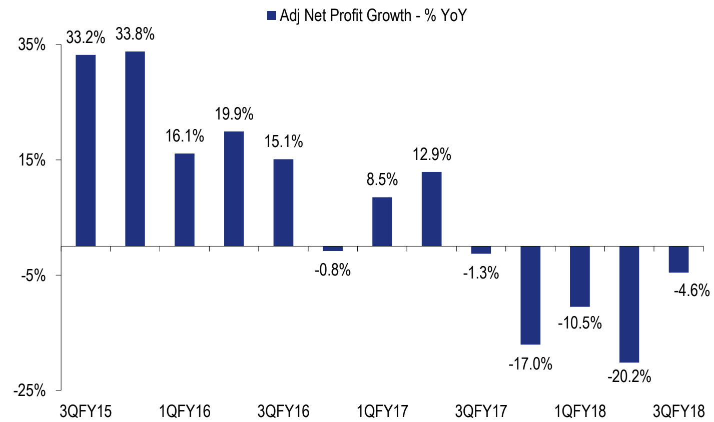
Source: Company, JM Financial

Exhibit 10. EBITDA growth trend



Source: Company, JM Financial

Exhibit 11. Adjusted net profit growth trend



Source: Company, JM Financial

Exhibit 12. Bajaj Corp – one year forward PE band

Source: Company, Bloomberg, JM Financial

Financial Tables (Consolidated)

Profit & Loss Statement					(INRmn)
Y/E March	FY16A	FY17A	FY18E	FY19E	FY20E
Net sales	**7,975**	**7,948**	**8,439**	**9,904**	**11,616**
Growth (%)	-3%	0%	6%	17%	17%
Other operational income	22	20	22	26	30
Total Revenue	**7,997**	**7,969**	**8,461**	**9,929**	**11,646**
Cost of Goods Sold / Op. Exp	2,980	2,691	2,838	3,331	3,907
Personnel cost	475	614	749	854	990
Other expenses (SG&A)	1,805	2,028	2,255	2,582	2,987
EBITDA	**2,737**	**2,636**	**2,620**	**3,163**	**3,762**
EBITDA Margin	34.2%	33.1%	31.0%	31.9%	32.3%
EBITDA Growth	14.4%	-3.7%	-0.6%	20.7%	18.9%
Depn & Amort	49	53	65	76	87
EBIT	2,688	2,583	2,554	3,086	3,675
Other income	287	394	333	353	371
Finance cost	2	10	14	13	13
PBT before Excep & Forex	2,973	2,966	2,874	3,426	4,033
Excep & Forex Inc/Loss(-)	-470	-184	0	0	0
PBT	2,503	2,782	2,874	3,426	4,033
Taxes	539	600	634	790	970
Extraordinary Inc / Loss (-)	0	0	0	0	0
Assoc Profit/Min Interest (-)	0	0	0	0	0
Net profit	1,964	2,182	2,240	2,636	3,063
Adjusted net profit	**2,333**	**2,327**	**2,240**	**2,636**	**3,063**
Net Margin (%)	29.2	29.2	26.5	26.6	26.3
Diluted share capital (mn)	148	148	148	148	148
Diluted EPS (INR)	**15.8**	**15.8**	**15.2**	**17.9**	**20.8**
Diluted Growth (%)	11.2	-0.3	-3.7	17.7	16.2
Total Dividend + tax	2,042	2,042	1,904	2,241	2,450
Dividend Per Share (Rs)	11.5	11.5	10.7	12.6	13.8

Source: Company, JM Financial

Balance Sheet					(INRmn)
Y/E March	FY16A	FY17A	FY18E	FY19E	FY20E
Shareholders' fund	**4,811**	**4,942**	**5,278**	**5,673**	**6,286**
Share capital	148	148	148	148	148
Reserves & surplus	4,663	4,794	5,130	5,526	6,138
Preference Share Capital	0	0	0	0	0
Total loans	100	150	150	150	150
Minority Interest	0	0	0	0	0
Def tax assets / (-) liability	8	8	8	8	8
Sources of Funds	**4,918**	**5,100**	**5,436**	**5,831**	**6,443**
Net-Fixed Assets	1,402	1,616	1,950	2,274	2,587
Gross Fixed assets	1,482	1,940	2,340	2,740	3,140
Intangible Assets	430	430	430	430	430
Less: Dep / Amort.	519	755	820	896	983
CWIP	9	0	0	0	0
Investments	2,751	3,385	3,385	3,385	3,385
Current assets	1,510	894	961	1,167	1,629
Inventories	502	425	486	570	668
Sundry debtors	254	274	277	326	382
Cash & bank balance	603	124	116	178	471
Loans & advances	112	23	81	94	108
Other current assets	40	47	0	0	0
Current Liabilities & Prov	744	796	861	995	1,158
Current liabilities	744	783	848	983	1,145
Provisions and others	0	13	13	13	13
Net current assets	766	98	100	172	471
Application of Funds	**4,918**	**5,100**	**5,436**	**5,831**	**6,443**

Source: Company, JM Financial

Note: FY16 growth rates impacted by Ind-AS transition. FY16 Sales, EBITDA and adjusted net profit on LTL basis grew 6.1%, 14.4% and 11.2% respectively

Cash Flow Statement					(INRmn)
Y/E March	FY16A	FY17A	FY18E	FY19E	FY20E
Profit before tax	2,503	2,782	2,874	3,426	4,033
Deprn and Amortn	-939	236	65	76	87
Net Interest Exp. /Inc	-285	-384	-320	-340	-358
Inc/dec in working cap.	-276	71	-9	-10	-7
Others	1,457	-1	0	0	0
Taxes Paid	-532	-585	-634	-790	-970
Net cash from operations (a)	**1,929**	**2,120**	**1,977**	**2,362**	**2,785**
Capex	-168	-359	-400	-400	-400
Free Cash Flow	1,761	1,761	1,577	1,962	2,385
Inc(-)/dec in investments	-24	-78	0	0	0
Others	252	284	333	353	371
Cash flow used in invst (b)	**60**	**-153**	**-67**	**-47**	**-29**
Inc/(dec) in capital	0	0	0	0	0
Dividend+Tax Thereon	-2,041	-2,042	-1,904	-2,241	-2,450
Inc/dec in loans	100	50	0	0	0
Other assets	-2	-8	-14	-13	-13
Financial cash flow (c)	**-1,943**	**-2,000**	**-1,917**	**-2,254**	**-2,463**
Net inc/dec in cash (a+b+c)	46	-33	-8	62	293
Opening cash balance (adjusted)	557	157	124	116	178
Closing cash balance	602	124	116	178	471

Source: Company, JM Financial

Dupont analysis					
Y/E March	FY16A	FY17A	FY18E	FY19E	FY20E
Net Margin	26.6%	29.2%	26.5%	26.6%	26.3%
Asset Turnover	1.8	1.6	1.6	1.8	1.9
Leverage Factor	1.0	1.0	1.0	1.0	1.0
RoE	48.1%	47.7%	43.8%	48.1%	51.2%

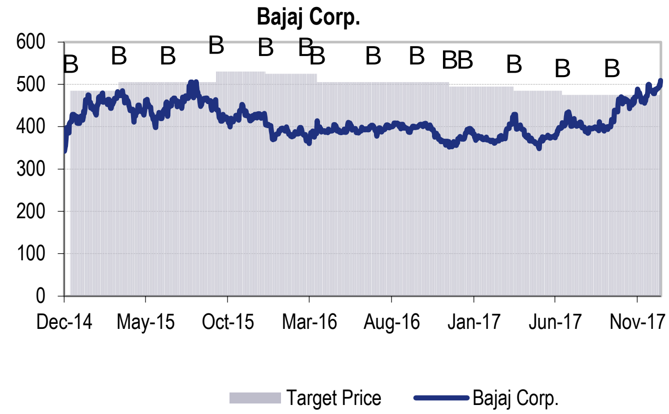
Key Ratios					
Y/E March	FY16A	FY17A	FY18E	FY19E	FY20E
BV/Share (Rs)	32.6	33.5	35.8	38.5	42.6
ROIC (%)	130.6%	137.1%	124.1%	122.2%	123.0%
ROE (%)	48.1%	47.7%	43.8%	48.1%	51.2%
Net Debt-equity ratio (x)	-0.7	-0.7	-0.7	-0.6	-0.6
P/E (x)	31.9	32.0	33.2	28.2	24.3
P/B (x)	15.5	15.0	14.1	13.1	11.8
EV/EBITDA (x)	26.0	26.9	27.1	22.4	18.8
EV/Net Sales (x)	8.9	8.9	8.4	7.2	6.1
Debtor days	11	13	12	12	12
Inventory days	21	19	21	21	21
Creditor days	45	54	53	53	53

Source: Company, JM Financial

History of Earnings Estimate and Target Price

Date	FY18E EPS (INR)	% Chg.	FY19E EPS (INR)	% Chg.	Target Price	% Chg.
16-Oct-14					305	
9-Jan-15					485	59.0
9-Apr-15					505	4.1
9-Jul-15	23.1				505	0.0
7-Oct-15	22.5	-2.6			530	5.0
7-Jan-16	21.7	-3.6			525	-0.9
22-Mar-16	21.1	-2.8			525	0.0
12-Apr-16	20.1	-4.7			505	-3.8
25-Jul-16	19.4	-3.5	22.2		505	0.0
14-Oct-16	19.0	-2.1	21.5	-3.2	505	0.0
14-Dec-16	18.1	-4.7	20.4	-5.1	495	-2.0
12-Jan-17	18.1	0.0	20.4	0.0	495	0.0
13-Apr-17	17.2	-5.0	19.4	-4.9	485	-2.0
12-Jul-17	16.4	-4.7	18.4	-5.2	475	-2.1
12-Oct-17	15.9	-3.0	18.0	-2.2	475	0.0

Recommendation History



APPENDIX I

JM Financial Institutional Securities Limited

Corporate Identity Number: U65192MH1995PLC092522
Member of BSE Ltd. and National Stock Exchange of India Ltd. and Metropolitan Stock Exchange of India Ltd.
SEBI Registration Nos.: BSE - INZ010012532, NSE - INZ230012536 and MSEI - INZ260012539, Research Analyst – INH000000610
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Rating	Meaning
Buy	Total expected returns of more than 15%. Total expected return includes dividend yields.
Hold	Price expected to move in the range of 10% downside to 15% upside from the current market price.
Sell	Price expected to move downwards by more than 10%

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