Sharekhan by BNP PARIBAS

Maruti Suzuki

Demand picking up; upgrade to Buy

Sector: Automobiles
Result Update

	Change
Reco: **Buy**	↑
CMP: **Rs. 6,186**	
Price Target: **Rs. 6,925**	↑

↑ Upgrade ↔ No change ↓ Downgrade

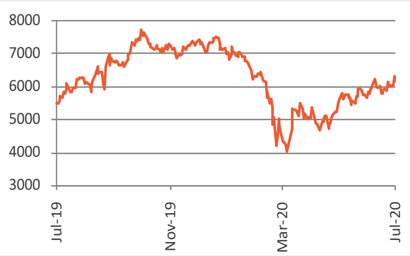
Company details

Market cap:	Rs. 186,855 cr
52-week high/low:	Rs. 7755 / 4002
NSE volume: (No of shares)	8.5 lakh
BSE code:	532500
NSE code:	MARUTI
Sharekhan code:	MARUTI
Free float: (No of shares)	13.2 cr

Shareholding (%)

Promoters	56.3
FII	21.5
DII	17.1
Others	5.2

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	5.9	15.4	-11.9	12.3
Relative to Sensex	-3.1	2.5	-4.9	10.5

Sharekhan Research, Bloomberg

Maruti Suzuki India Limited's (Maruti) Q1FY2021 operating results were lower than estimates impacted by negative operating leverage due to steep fall in volumes and higher fixed cost incidence due to lower production. However, higher other income led to the company posting lower-than-expected loss. Going ahead, the company is witnessing strong pick-up in demand with retailsales reaching 85-90% of pre-COVID levels. Apart from pick-up in rural areas due to strong farm sentiments, urban areas are also witnessing surge in demand, driven by increased preference for personal transportation to ensure social distancing. Moreover, demand shift towards entry-level cars is likely to benefit Maruti, which has a stronghold in the segment. We have raised our earnings estimates to factor in demand recovery. We upgrade our recommendation on the stock to Buy from Hold earlier with a price target (PT) of Rs. 6,925.

Key positives

- Management stated that demand is picking up with retail demand reaching 85-90% of pre-COVID levels.
- Other income stood at Rs. 1,318 crore,growing strongly by 57% y-o-y and was better than estimates. Higher fair value gains on invested surplus boosted other income.
- Demand shift towards entry cars is likely to benefit Maruti Suzuki which has stronghold in the segment.

Key negatives

- During Q1FY2021, Maruti recognisedRs. 110 crore charge on account of higher fixed cost incidence due to lower production.

Our Call

Valuations:Demand picking up; Upgrade to Buy: Maruti stated that retail demand has reached 85-90% of pre-COVID levels recently. Apart from strong rural demand on account of robust farm sentiments, urban demand is also witnessing recovery, driven by preference towards personal transportation. Maruti is witnessing recovery in demand with retail sales fast approaching pre-COVID levels. We expect the upcoming festive season to further boost demand. We expect full-fledged recovery from FY2022, driven by normalisationof economic activities and pent-up demand. We have raised our FY2021 and FY2022 estimates by 13% and 19%, respectively. At the CMP, the stock is trading at 24.1x its FY2022 earnings, which is close to its long-term historical average of 25x-26x. However, given the early recovery cycle scenario in which Maruti currently is in, valuation multiples can expand above historical averages. We have raised our target multiple from 25x to 27x and have arrived at a PT of Rs. 6,925. We upgrade our recommendation to Buy from Hold earlier.

Key Risks

Prolonged COVID-19 infection can weaken consumer sentiments and delay normalcy in demand.

Valuation Rs cr

Particulars	FY18	FY19	FY20	FY21E	FY22E
Net sales	79,763	86,020.3	75,610.6	64,001.8	81,526.5
Growth (%)	17.2	7.8	-12.1	-15.4	27.4
EBITDA	12,062	10,999	7,303	6,072	9,706
EBIDTA %	15.1	12.8	9.7	9.5	11.9
PAT	7,722	7,500.6	5,650.6	5,024.3	7,744.3
Growth (%)	5.1	-2.9	-24.7	-11.1	54.1
FD EPS (Rs.)	255.6	248.3	187.1	166.3	256.4
P/E (x)	24.2	24.9	33.1	37.2	24.1
P/B (x)	4.5	4.0	3.7	3.5	3.1
RoE (%)	18.5	16.3	11.2	9.3	12.9
RoCE (%)	24.8	20.8	13.2	10.8	15.5
EV/Sales(x)	2.3	2.1	2.0	2.3	1.7
EV/EBITDA (x)	15.4	16.5	20.3	24.1	14.5

Source: Company; Sharekhan estimates

Operating performance misses estimates; Higher other income leads to lower-than-expected loss: Maruti's Q1FY2021 operating results were lower than our as well as street estimates,as steep volume drop due to COVID-19pandemic impacted the company's operating profitability. However, higher other income led to the company posting lower-than-expected loss. Revenue declined by 80%y-o-y to Rs. 4,107 crore (but was ahead of estimate of Rs. 3,694 crore). While volumes declined by 81% y-o-y impacted by COVID-19, realisationper vehicle grew by 3% y-o-y. Realisation per vehicle was better than our expectations of 3% drop. Lower-than-anticipated discounting and better mix resulted in higher realisations for the company. Maruti posted operating loss of Rs. 863 crore in Q1, which is higher than our expectations of Rs. 335 crore. Negative operating leverage due to steep fall in topline impacted the operating performance.Moreover, Maruti realisedcharge of Rs. 110 crorein Q1FY2021 on account of higher fixed cost incidence due to lower production as compared to sales (the charge would get reversed in the coming quarters). Other income stood at Rs. 1,318 crore as against Rs. 836 crore in Q1FY2020 and was better than estimates. Higher fair value gains on invested surplus led to increased other income for the company. Net loss at Rs. 249 crore was lower than our expectations of Rs. 360 crore and street estimates of Rs. 445 crore.

Retail demand picking up; Company ramping up production; Shift towards entry cars to benefit Maruti: Maruti stated that retail demand has been picking up post the lockdown announced in April 2020. Retail demand has reached 85-90% of pre-COVID levels recently. Demand in rural areas (~40% of Maruti's volumes) has gained momentum due to strong sentiments on account of bumper rabi harvest, expectations of normal monsoon, and government's reform measures. Moreover, management stated that urban areas are also witnessing pick up. Preference for personal transportation to ensure social distancing is leading to recovery in urban demand. To cater to rising demand, Maruti is enhancing production capacity from current 4,000 units per day to about 4,900 units per day. Moreover, consumers are preferring entry-level cars in difficult times of COVID-19. Maruti, having a stronghold over the entry-car segment, is likely to benefit from the trend .We expect full-fledged recovery in FY2022, driven by normalisation of economic activities and pent-up demand (PV volumes have been under pressure for the past six to seven quarters).

Conference call highlights:

Retail demand: Maruti stated that retail demand has reached 85-90% of pre-COVID levels.

Production update: Maruti is increasing production from 4,000 units per day to 4,900 units per day by opening up second shift at the Gujarat plant.

Financing: Maruti stated that share of financing in overall volumes stood at 80%, which is similar to FY2020 levels. The company has introduced innovative schemes to introduce initial payment burden on car buyers in times of COVID-19.

Inventory levels: Maruti'scurrent inventory levels stood at 25 days, which is lower than the norm of 30 days.

Diesel vehicles: Maruti stated that share of diesel vehicles in the PV industry has come down from 30% in FY2020to 21% in Q1FY2021.

First-time buyers: Maruti witnessed an increase in the share of first-time buyers in Q1FY2021.Theproportion of first-time buyers increased by 5%- 5.5 % in Q1FY2021.

Discounting: Maruti stated that discounting per vehicle stood at Rs. 20,000 in Q1FY2021. Discounts in July 2020 have come down.

Focus on digital initiatives: Maruti is focusing on increasing digitisation. Almost the entire documentation and financing have been digitised to reduce physical contact with customers.

Results Rs cr

Particulars	Q1FY21	Q1FY20	YoY %	Q4FY20	QoQ %
Revenue	4,106.5	19,719.8	-79.2	18,198.7	-77.4
EBIDTA	(863.4)	2,047.8	NA	1,546.4	NA
EBIDTA Margins (%)	-21.0	10.4	(3140 bps)	8.5	(2950 bps)
Depreciation	783.3	918.6	-14.7	823.0	-4.8
Interest	17.3	54.7	-68.4	28.3	-38.9
Other Income	1318.3	836.4	57.6	880.4	49.7
PBT	(345.7)	1,910.9	NA	1,575.5	NA
Tax	-96.3	475.4	NA	283.8	NA
Adjusted PAT	(249.4)	1,435.5	NA	1,291.7	NA
EPS (Rs.)	-8.3	47.5	NA	42.8	NA

Source: Company; Sharekhan Research

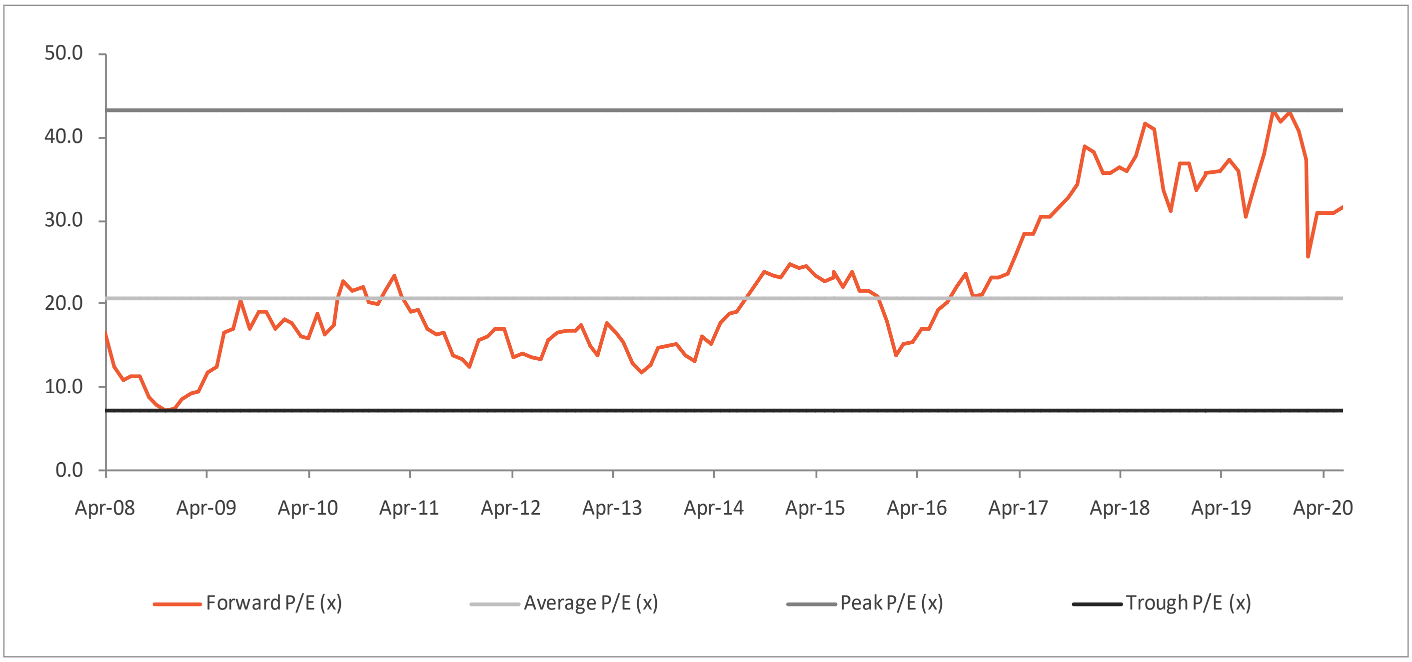
Outlook

Demand picking up; Maruti enhancing capacity: Managementstated that retail demand has reached 85-90% of pre-COVID levels recently. Apart from strong rural demand on account of robust farm sentiments, urban demand is also witnessing recovery, driven by preference towards personal transportation. Maruti is enhancing production capacity by opening second shift at the Gujarat plant. Production would be ramped up from current 4,000 units per day to 4,900 units per day.

Valuation

Raise estimates; Upgrade to Buy: Maruti is witnessing recovery in demand with retail sales fast approaching to pre-COVID levels. We expect the upcoming festive season to further boost demand. We expect full-fledged recovery from FY2022, driven by normalisationof economic activities and pent-up demand. We have raised our FY2021 and FY2022 estimates by 13% and 19%, respectively. At the CMP, the stock is trading at 24.1x its FY2022 earnings, which is close to its long-term historical average of 25x-26x. However, given the early recovery cycle scenario in which Maruti currently is in, valuation multiples can expand above historical averages. We have raised our target multiple from 25x to 27x and have arrived at a PT of Rs. 6,925. We upgrade our recommendation to Buy from Hold earlier.

One year forward P/E band



Source: Sharekhan Research

About company

MSIL is the market leader in the PV segment, commanding a market share of about 50%. In the PV segment, MSIL's market share in passenger cars stands at 58%, utility vehicles at 28% and vans at 82%. Petrol vehicles contribute about 75% to sales, whilst the contribution of diesel vehicles stands at 25%. MSIL has been steadily ramping up its presence in the hinterlands, with rural sales currently contributing about 30% to overall sales.

Investment theme

MSIL is the market leader in the PV segment with a 50% market share. Maruti is witnessing recovery in the PV demand with retail sales reaching 85-90% of Pre-COVID levels.Demand in rural areas (~40% of Maruti volumes) has gained momentum due to strong sentiments on account of bumper rabi harvest, expectations of normal monsoon and government reform measures. Moreover, management stated that urban areas are also witnessing pick up. Preference for personal transportation to ensure social distancing is leading to recovery in the urban demand. In order to cater to the rising demand. Moreover, consumers are preferring entry level cars in difficult times of COVID-19. Maruti having stronghold over the entry car segment is likely to benefit from the trend. Hence, we upgrade our recommendation to "Buy" from "Hold"

Key Risks

Prolonged COVID-19 infection can weaken consumer sentiments and delay normalcy in demand.

Additional Data

Key management personnel

R C Bhargava	Chairman
Kenichi Ayukawa	Managing Director & CEO
A Seth	Sr Executive Officer (Finance)
R S Kalsi	Sr Executive Officer (Marketing & Sales)

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Suzuki Motor Corp	56.2
2	Life Insurance Corp of India	6.8
3	Vanguard Group Inc	1.4
4	Capital Group Cos	1.4
5	Blackrock Inc	1.3
6	JP Morgan Chase	1.1
7	SBI Funds Management Pvt Limited	1.1
8	GIC Pte Ltd	1.1
9	Nomura Holdings Inc	1.0
10	Axis Asset Management Co	0.8

Source: Bloomberg

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