Maruti Suzuki India Limited

Near term demand outlook and structural growth prospects provide comfort

Automobiles	Sharekhan code: MARUTI	Result Update

3R MATRIX

	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)		✓	

+ Positive = Neutral - Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↔	

Reco/View	Change
Reco: **Buy**	↔
CMP: **Rs. 7,589**	
Price Target: **Rs. 9,000**	↔

↑ Upgrade ↔ Maintain ↓ Downgrade

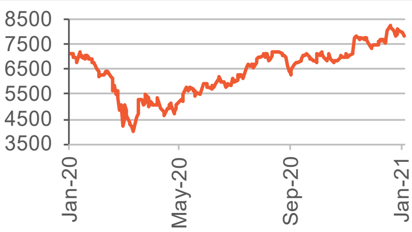
Company details

Market cap:	Rs. 2,29,249 cr
52-week high/low:	Rs. 8,329/4,001
NSE volume: (No of shares)	11.7 lakh
BSE code:	532500
NSE code:	MARUTI
Free float: (No of shares)	13.2 cr

Shareholding (%)

Promoters	56.4
FII	23.1
DII	15.7
Others	4.9

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	5.6	11.5	29.7	10.4
Relative to Sensex	4.7	-6.6	5.4	-3.6

Sharekhan Research, Bloomberg

Summary

- Maruti Suzuki Limited (MSL) reported Q3FY2021 revenues in-line with our estimates but misses on operating performance on back of unfavorable product mix and rise in prices of key raw materials.
- We remain positive on MSL given its near-term demand outlook, structural growth outlook, healthy cash flow generation, and return ratios. The stock is trading at P/E multiple of 24x and EV/EBITDA multiple of 17.1x its FY2023 estimates. Maintain buy rating with TP of Rs 9,000
- MSL is likely to be the beneficiary of buoyant demand in the passenger vehicle (PV) segment, driven by rising demand in tier 2 and 3 cities and rural areas. MSL is expected to sustain its dominant market share, aided by its strong product portfolio and positioning, brand appeal, and ability to launch new models frequently.
- We expect MSL's earnings to grow strongly by 49% and 19.5% in FY2022E and FY2023E, respectively, driven by 21.9% revenue CAGR (FY2021E-FY2023E) and 380 bps improvement in EBITDA margin

Maruti Suzuki Limited (MSL) reported revenues in-line with our estimates but missed on operating performance on back of unfavourable product mix and rise in the prices of key raw materials. Net revenue grew 13.1% y-o-y at Rs 23,458 crore in Q3FY2021, driven by 13.0% growth in domestic volumes and 20.6% growth in exports, while the realization remained flat. EBITDA margins declined 66 bps y-o-y and 83 bps q-o-q at 9.5%, leading to slower EBITDA growth of 5.9% y-o-y and 15.1% q-o-q at Rs 2,226 crore. The reported EBITDA was below expectations due to unfavourable product mix, rise in raw material costs and adverse forex fluctuations. Despite the adverse situations, the EBITDA margin remained firm, aided by improved capacity utilisation and lower marketing expenses. However, the company reported net profit of 1,941 crores, a robust growth of 24.1% y-o-y and 41.5% q-o-q in Q3FY2021, led by higher other income. Other income for the quarter stood at Rs 994 crores, registering a growth of 26.7% y-o-y and 64.9% q-o-q. The management of Maruti Suzuki were cautiously optimistic on the demand outlook for domestic as well as export markets. The company has witnessed strong demand from rural and semi-urban areas, where MSL's distribution network and product portfolio fits aptly. The improving income levels of individuals, firms and corporates after recovery from COVID-19 pandemic is likely to keep the demand strong in the medium term. We expect FY2022 to be a stronger quarter for MSL, driven by strong volume growth. The volume growth will be aided by new product launches, quick economic recovery, upside from COVID-19 vaccines, and low base. MSL's strongest distribution network in the segment and rural penetration are likely to drive strong revenue growth going forward. MSL's volumes are expected to recover from FY2022 with expectations of strong double-digit growth, aided by robust exports as well. MSL would benefit from operating leverage, driven by robust volume growth. We expect MSL's earnings to grow strongly by 49% and 19.5% in FY2022E and FY2023E, respectively, driven by 21.9% revenue CAGR (FY2021E-FY2023E) and 380 bps improvement in EBITDA margin. Moreover, core earnings (excluding earnings from the non-core business) are expected to post a 67.8% CAGR during FY2021E-FY2023E. We expect RoCE to improve to 18.4% in FY2023E from 13.6% in FY2020.

Our Call

Valuation - Maintain Buy with unchanged PT of Rs. 9,000: MSL is witnessing strong recovery in domestic demand with sales volumes sustaining growth in the post-festive season. Sales enquiry is strong even after the festive season, underpinning our view of genuine demand in the PV segment. We expect strong recovery from FY2022, driven by normalisation of economic activity. Margins are expected to improve, driven by operating leverage and cost-control measures. We have maintained our buy rating with TP of Rs 9,000. We are positive on MSL given its near-term demand outlook, structural growth outlook, healthy cash flow generation, and return ratios. The stock is trading at P/E multiple of 24x and EV/EBITDA multiple of 17.1x its FY2023 estimates.

Key Risks

Key raw-material prices have surged steeply in the past six months in the range of 30%-50%. MSL has taken price hikes to mitigate the impact of high input costs this month. However, if raw-material prices continue to rise in the same pace in the near term, the company may not be able to pass on the cost to customers, and impact profitability

Valuation (Consolidated) Rs cr

Particulars	FY19	FY20	FY21E	FY22E	FY23E
Net sales	86,020	75,611	70,510	90,083	1,04,746
Growth (%)	7.8	(12.1)	(6.7)	27.8	16.3
EBITDA	10,999	7,303	6,201	10,719	13,209
EBIDTA %	12.8	9.7	8.8	11.9	12.6
PAT	7,501	5,651	5,369	8,001	9,561
Growth (%)	(2.9)	(24.7)	(5.0)	49.0	19.5
FD EPS (INR)	248.3	187.1	177.7	264.9	316.5
P/E (x)	30.6	40.6	42.7	28.7	24.0
P/B (x)	5.0	4.7	4.4	4.0	3.6
EV/EBITDA (x)	20.4	31.2	36.7	21.2	17.1
RoE (%)	16.3	11.7	10.3	13.8	14.8
RoCE (%)	20.7	13.6	12.3	17.1	18.4

Source: Company; Sharekhan estimates

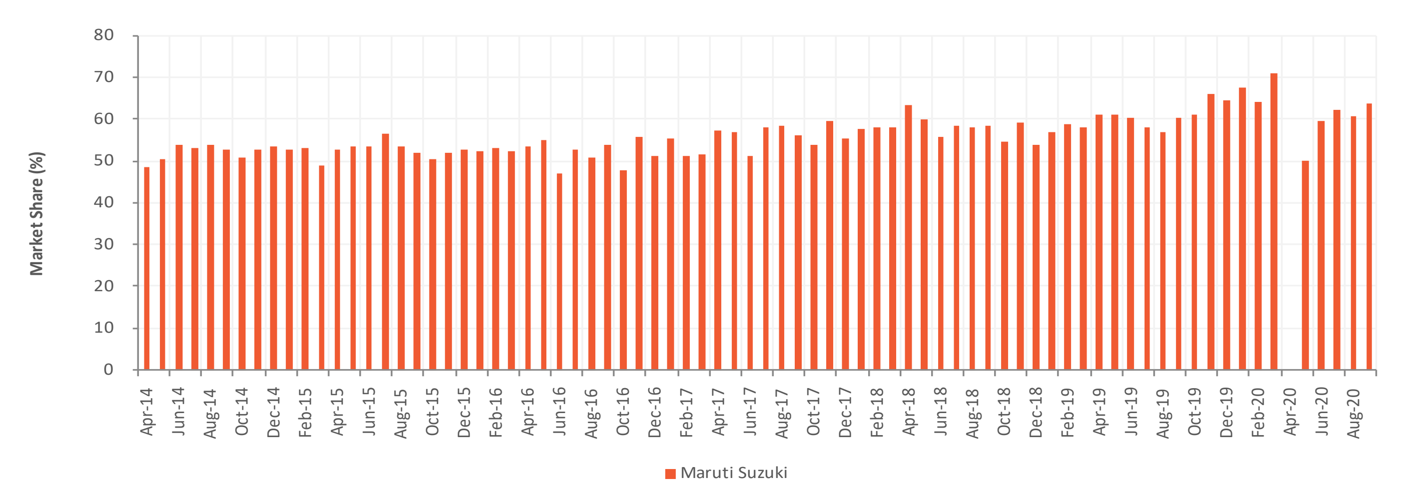
Revenue in-line but operating performance declines on product mix: Maruti Suzuki Limited (MSL) reported revenues in-line with our estimates but missed on operating performance on the back of an unfavourable product mix and rise in prices of key raw materials. Net revenue grew 13.1% y-o-y at Rs 23,458 crore in Q3FY2021, driven by 13.0% growth in domestic volumes and 20.6% growth in exports, while the realization remained flat. EBITDA margins declined 66 bps y-o-y and 83 bps q-o-q at 9.5%, leading to slower EBITDA growth of 5.9% y-o-y and 15.1% q-o-q at Rs 2,226 crore. The reported EBITDA was below expectations due to unfavourable product mix, rise in raw material costs and adverse forex fluctuations. Despite the adversities, EBITDA margin remained firm, aided by improved capacity utilisation and lower marketing expenses. The choice of customers toward smaller cars amidst COVID-19, affected the product mix. The gross profit margin was down by 178 bps y-o-y and 269 bps q-o-q at 27.5% in Q3FY21. However, the company reported net profit of 1,941 crores, a robust growth of 24.1% y-o-y and 41.5% q-o-q in Q3FY2021, led by higher other income. Other income for the quarter stood at Rs 994 crores, registering a growth of 26.7% y-o-y and 64.9% q-o-q.

Management is cautiously optimistic on demand outlook: The management of Maruti Suzuki were cautiously optimistic on the demand outlook for domestic as well as export markets. The company has witnessed strong demand from rural and semi-urban areas, where MSL's distribution network and product portfolio fits aptly. The improving income levels of individuals, firms and corporates after recovery from COVID-19 pandemic is likely to keep the demand strong in the medium term. We expect FY2022 to be a stronger quarter for MSL, driven by strong volume growth. The volume growth will be aided by new product launches, quick economic recovery, upside from COVID-19 vaccines, and a low base. Retail sales continue to register strong growth. As per data released by FADA, MSL reported retail sales growth of 29.6% y-o-y at 1,30,772 units in December 2020, with market share gain of 209 bps at 48.21%. MSL's decision to hike prices from January'21 may have prompted pre-buying in December'20, despite the fact that in December consumers usually avoid purchasing new vehicles as new year's registration date offers a better resale value. Consumer behaviour remains intact and low rate financing regime could augur well for the growth. The financing continues to drive ~80% of sales in the retail market.

Replacement demand fallen but likely to improve: The share of replacement buying demand has fallen to 19% in Q3FY21 from 26% in Q3FY20, due to COVID-19 pandemic. The management expects the replacement buying to bounce back in couple of quarters to around 23%.

MSL's market share to remain intact despite intense competition: MSL is likely to be the beneficiary of buoyant demand in the PV segment, driven by rising demand in Tier 2 and 3 cities and rural areas. Sales from rural areas will continue to improve, driven by strong farm sentiments on account of higher rainfall and kharif sowing. Rural sales have risen from ~38% in Q3FY2020 to 40% in Q3FY2021. We also expect the share of first-time buyers to increase going forward, aided by preference for personal transportation. The share of new buyers has increased to 49% in Q3FY2021 from 43% in Q3FY2020. Despite intense competition in the PV segment, MSL is expected to sustain its dominant market share, aided by its strong product portfolio and position, brand appeal, and ability to launch new models frequently. MSL has a strong hold in small and mid-size segments with over 50% market share and high success rates of its new launches. The company's brand positioning as value-for-money products is likely to remain intact due to its products' best fuel efficiency and lower maintenance cost. Moreover, high resale value of its products attracts customers.

MSL continues its dominancy in the passenger car segment despite fierce competition



Source: Company Data; Sharekhan Research

Exports continue to remain buoyant: The management expects export to be a key growth driver going forward, given the improving scenario in other geographies. The company is operating at more than 90% capacity utilisation, which will keep driving profitability. In January, the company commenced the production of the made-in-India Suzuki 'Jimny' SUV. The first batch has taken off from Mundra port and is headed to Latin American countries like Peru and Colombia. These units are manufactured at the Gurugram facility. MSL is evaluating business prospects for launching 'Jimny' in Indian markets.

Extensive network distribution helps MSL to penetrate rural markets: MSL has the strongest distribution network and rural penetration in the PV segment that drives its revenue growth. We expect MSL to be the beneficiary of rising rural demand, driven by its reach and low maintenance services costs.

Margins to improve on cost-cutting measures: We expect MSL's OPM to remain strong in the quarters ahead. Further, MSL's EBITDA margin is expected to retract to more than 12% by FY2023, driven by increasing capacity utilisation, controlling marketing costs through digitalization and productivity gains. We have estimated EBITDA margin to be at 12.6% in FY2023E from 9.7% in FY2020, driven by operating leverage, increasing localisation levels, and improvement in operational efficiencies.

Strong earnings growth; Revised earnings upwards: We expect MSL's earnings to grow strongly by 49% and 19.5% in FY2022E and FY2023E, respectively, driven by 21.9% revenue CAGR (FY2021E-FY2023E) and 380 bps improvement in EBITDA margin. Moreover, core earnings (excluding earnings from the non-core business) are expected to post a 67.8% CAGR during FY2021E-FY2023E. We expect RoCE to improve to 18.4% in FY2023E from 13.6% in FY2020.

Results — **Rs cr**

Particulars	Q3FY21	Q3FY20	y-o-y (%)	Q2FY21	q-o-q (%)
Revenues	23,458	20,707	13.3	18,745	25.1
EBIDTA	2,226	2,102	5.9	1,934	15.1
EBIDTA Margins (%)	9.5	10.2	-66bps	10.3	-83bps
Depreciation	741	858	-13.6	766	-3.2
Interest	29	22	32.3	22	28.1
Other Income	994	784	26.7	603	64.9
PBT	2450	2006	22.1	1748	40.2
Tax	508	442	15.1	376	35.1
Adjusted PAT	1941	1565	24.1	1372	41.5
EPS	64.3	51.8	24.1	45.4	41.5

Source: Company; Sharekhan Research

Outlook and Valuation

Sector view - PV industry demand improving sequentially; Expect strong recovery from FY2022

The PV industry turned positive in August 2020 and is showing improvement every month. Aggregate volumes registered by key OEMs in the PV segment witnessed growth of 25.3% y-o-y in December 2020. Channel check suggest that strong enquiry and order book post the festive season across OEMs. We expect strong recovery from FY2022, driven by normalisation of economic activity and pent-up demand. Operating leverage and reduction in discounting due to pick-up in volumes would lead to the PV industry posting better margins in the coming quarters.

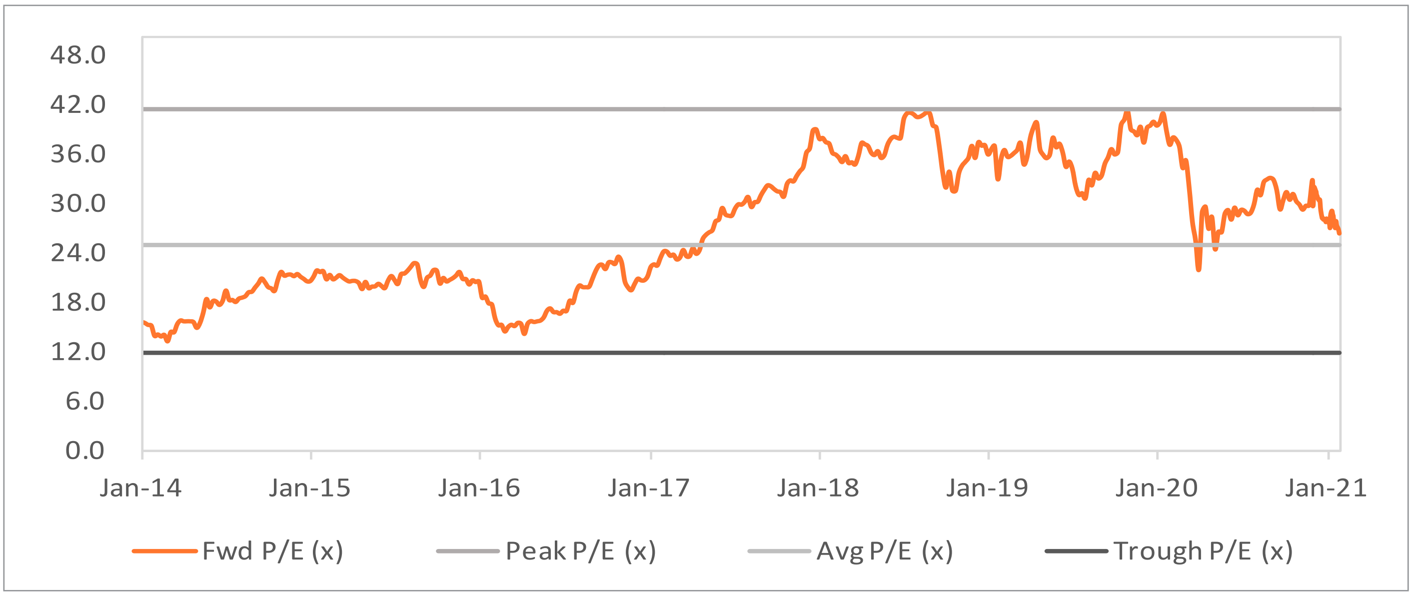
Company outlook - Strong earnings growth from the core business

MSL is witnessing strong recovery in sales volumes and is likely to have flat y-o-y sales volume growth in FY2021E, despite a 36.6% y-o-y decline in H1FY2021. The company has witnessed strong demand from rural and semi-urban areas, where MSL's distribution network and product portfolio fits aptly. The improving income levels of individuals, firms and corporates after recovery from COVID-19 pandemic is likely to keep the demand strong in the medium term. We expect FY2022 to be a stronger quarter for MSL, driven by strong volume growth. The volume growth will be aided by new product launches, quick economic recovery, upside from COVID-19 vaccines, and low base. Retail sales continue to register strong growth. As per the data released by FADA, MSL reported retail sales growth of 29.6% y-o-y at 1,30,772 units in December 2020 with market share gain of 209 bps at 48.21%. We expect the improving scenario in other geographies is likely to help MSL register export growth. However, we expect domestic growth to be the key benefactor for the company.

Valuation - Maintain Buy with an unchanged PT of Rs. 9,000

MSL is witnessing strong recovery in domestic demand with sales volumes sustaining growth in the post-festive season. Sales enquiry is strong even after the festive season, underpinning our view of genuine demand in the PV segment. We expect strong recovery from FY2022, driven by normalisation of economic activity. Margins are expected to improve, driven by operating leverage and cost-control measures. We have maintained our buy rating with TP of Rs 9,000. We are positive on MSL given its near-term demand outlook, structural growth outlook, healthy cash flow generation, and return ratios. The stock is trading at P/E multiple of 24x and EV/EBITDA multiple of 17.1x its FY2023 estimates.

One-year forward P/E (x) band



Source: Sharekhan Research

Peer Comparison

Particulars	CMP (Rs / Share)	P/E (x)			EV/EBIDTA (x)			RoCE (%)		
		FY21E	FY22E	FY23E	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E
Maruti Suzuki	7,589	42.7	28.7	24.0	36.7	21.2	17.1	12.3	17.1	18.4
Hero MotoCorp	3,397	25.4	19.6	16.7	16.3	12.3	9.8	23.1	28.2	26.5
Bajaj Auto	4,136	24.9	21.8	18.9	19.0	15.7	13.2	21.6	21.7	22.0

Source: Company, Sharekhan estimates

About company

MSL (formerly Maruti Udyog Limited) is India's largest PV car company accounting for over 50% of the domestic car market. The company is the undisputed leader in mini and compact car segments in India and offers full range of cars - entry level, compact cars, and SUVs. MSL's market share in passenger cars stands at 62%, utility vehicles at 25%, and vans at 90%. MSL has been steadily ramping up its presence in the hinterlands, with rural sales currently contributing about 41% to overall sales. MSL is a subsidiary of Suzuki Motor Corporation of Japan. The Japanese car major holds 56.2% stake in MSL. The company has manufacturing plants in Gurgaon and Manesar.

Investment theme

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Key Risks

- MSL has a weak SUV portfolio and can restrict growth once urban demand comes back strongly. However, we are more positive on rural demand and believe MSL to be the beneficiary.
- Rising input prices may impact margins, if rising commodity prices could not be passed on to customers. In a scenario of price competition, MSL's margin may get impacted negatively.

Additional Data

Key management personnel

R C Bhargava	Chairman
Kenichi Ayukawa	Managing Director & CEO
Ajay Seth	Chief Financial Officer
Sanjeev Grover	Company Secretary

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Suzuki Motor Corp	56.3
2	Life Insurance Corp of India	5.0
3	SBI Funds Management Pvt Limited	1.9
4	JP Morgan Chase & Co	1.6
5	Vangaurd Group Inc	1.4
6	Blackrock Inc	1.4
7	Capital Group companies	1.2
8	Axis Management Co India	1.5
9	GIC Pte Ltd	1.1
10	European Growth Fund	1.0

Source: Bloomberg

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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Compliance Officer: Mr. Joby John Meledan; Tel: 022-61150000; email id: compliance@sharekhan.com;

For any queries or grievances kindly email igc@sharekhan.com or contact: myaccount@sharekhan.com

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