Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

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. 3,735**	
Price Target: **Rs. 4,327**	↑

↑ Upgrade ↔ Maintain ↓ Downgrade

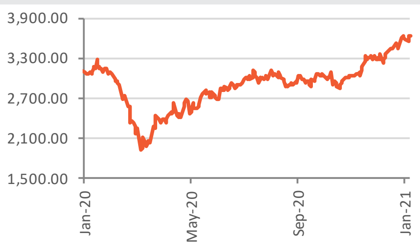
Company details

Market cap:	Rs. 1,06,506 cr
52-week high/low:	Rs. 3,808 / 1,793
NSE volume: (No of shares)	9.5 lakh
BSE code:	532977
NSE code:	BAJAJ-AUTO
Free float: (No of shares)	13.4 cr

Shareholding (%)

Promoters	53.7
FII	13.1
DII	12.0
Others	21.2

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	11.2	22.0	23.6	16.7
Relative to Sensex	5.0	-1.1	-12.9	-2.0

Sharekhan Research, Bloomberg

Stock Update

Bajaj Auto Limited

Positive outlook promising strong recovery

Automobiles | Sharekhan code: BAJAJ-AUTO | Result Update

Summary

- We maintain our Positive stance on Bajaj Auto Limited (BAL) and has upgraded our estimates and price target to factor in improved operational efficiencies. We recommend BUY with PT of Rs. 4,327.
- BAL reported robust PAT growth of 23.4% y-o-y at Rs. 1,556 crore, driven by better-than-expected improvement in operating profit margin.
- We expect BAL to benefit from growth in the premium bikes segment, where BAL continues to gain market shares, aided by premiumisation trend and new launches. Moreover, we expect BAL to gain market share in exports, driven by its brand equity and enhanced distribution network in export destinations.
- The stock trades at P/E multiple of 17.1x and EV/EBITDA multiple of 11.5x its FY2023E estimates.

Bajaj Auto Limited (BAL) has reported better-than-expected improvements in operating profit margin (OPM), which led to robust PAT growth of 23.4% y-o-y at Rs. 1,556 crore in Q3FY2021. Net revenue grew by 16.6% y-o-y at Rs. 8,909 crore in Q3FY2021, driven by 8.7% growth in volumes and 7.3% growth in average realisation. Average realisation was driven by price hikes due to BS-VI transition. Volumes were driven by 16.2% growth in two-wheelers (2W), despite a 35.6% decline in three-wheelers (3W). EBITDA margin improved by 152 bps y-o-y and 172 bps q-o-q to 19.4%, leading to EBITDA growth of 26.5% y-o-y and 36.6 q-o-q, respectively, at Rs. 1,730 crore. Improvement in EBITDA margin was driven by richer product mix, operating leverage, and cost reductions. In FY2022, we expect demand to arise from urban markets as well, where we believe BAL will be a major beneficiary in the 2W space, given its dominant position in the premium bike segment. Demand for 3Ws is also expected to improve. This will help BAL to improve its margin aided by richer product mix and operating efficiencies. BAL will also benefit from new launches in the premium segment, which it has lined up in the premium segment over the next 12-18 months. Management continues to focus on new launches and expects to launch at least one model (either new or upgraded model) every quarter. BAL has positioned itself strongly in export markets with focus on Nigeria, Bangladesh, Philippines, and Colombia, which accounts for ~50% of its 2W export revenue. In the 3W exports, BAL has a strong presence in Nigeria, Egypt, Cambodia, and Iraq. Products are well diversified and have favourable sales mix in under-penetrated markets such as Africa. BAL has improved its brand equity in these markets, which will help to improve its market share. In Q3FY2021, more than 85% of export revenue was generated from geographies where BAL is either No. 1 or No. 2 player. Export growth is organic and will continue to be a long-term driver for BAL. The company aims to outpace the industry in international operations, driven by increased distribution reach. BAL's export volumes are recovering and have reached at pre-COVID levels in most markets. BAL expects positive growth in these markets in Q4FY2021. Demand in the domestic motorcycle industry is also improving with positive sales growth from August 2020. BAL expects the trend of premiumisation to continue in the domestic 2W industry, which would enable it to gain market share, especially in 125cc+ markets. 3W volumes are also improving on m-o-m basis, as the economy is moving towards normalcy. Domestic 3W sales are expected to improve with the opening of schools, colleges, other educational institutions, and corporates. Moreover, BAL is aiming to protect its margins as rising input costs are offset by price hikes, better product mix, and cost-control measures. We expect EBITDA margin to remain above 18% in the medium term. The company is debt-free and generates strong cash flows, which are enough to expand capacity through internal accruals. The company has a strong long-term revenue visibility, given its leadership position in the premium bikes segment and key export destinations. We expect BAL's earnings to grow by 14.1% in FY2022E and 15.3% in FY2023E, driven by a 14.8% CAGR (FY2021-FY2023) in revenue and 40 bps expansion EBITDA margin. We remain positive on BAL and retain our Buy rating on the stock with a revised PT of Rs. 4,327.

Our Call

Valuation - Maintain Buy with a revised PT of Rs. 4,327: BAL is witnessing strong recovery in domestic 2Ws and exports demand, while a slow recovery in 3Ws demand. The outlook remains positive with strong recovery expected from FY2022, driven by normalisation of economic activities. OPM would expand because of richer product mix, operating leverage, and cost-control measures. We have increased our earnings estimates to factor in improved business outlook. We value the stock at 20x its FY2023E earnings and have arrived at a PT of Rs. 4,327. The stock is valued at a P/E multiple of 17.1x and EV/EBITDA multiple of 11.5x its FY2023E estimates. We retain our Buy rating on the stock with a revised PT of Rs. 4,327.

Key Risks

BAL can lose its market share, if EVs in the domestic 3W market rise faster than we expect. Moreover, BAL has significant exposure to export markets. Any slowdown in export markets and unfavourable forex fluctuations can affect the company's profits adversely.

Valuations (Consolidated) Rs cr

Particulars	FY19	FY20	FY21E	FY22E	FY23E
Net Sales	30,358	29,919	28,370	32,779	37,419
Growth (%)	20.4	-1.4	-5.2	15.5	14.2
EBIDTA	5,192	5,096	5,205	6,104	6,998
OPM (%)	17.1	17.0	18.3	18.6	18.7
Recurring PAT	4,333	5,100	4,802	5,481	6,320
Growth (%)	5.7	17.7	-5.8	14.1	15.3
EPS (Rs.)	150	176	166	190	219
PE (x)	24.9	21.2	22.5	19.7	17.1
P/BV (x)	5.0	5.4	4.9	4.3	3.8
EV/EBIDTA (x)	17.2	18.3	16.8	13.8	11.5
RoCE (%)	28.3	32.1	27.7	28.4	28.8
RoNW (%)	19.9	25.6	21.6	21.7	22.0

Source: Company; Sharekhan estimates

Operating performance improved better than expectations, while PAT was in-line: BAL has reported better-than-expected improvement in its OPM, which led to robust PAT growth of 23.4% y-o-y at Rs. 1,556 crore in Q3FY2021. Net revenue grew by 16.6% y-o-y to Rs. 8,909 crore in Q3FY2021, driven by 8.7% growth in volumes and 7.3% growth in average realisation. Average realisation was driven by price hikes due to BS-VI transition. Volumes were driven by 16.2% growth in 2W, despite a 35.6% decline in 3W. EBITDA margin improved by 152 bps y-o-y and 172 bps to 19.4%, leading to EBITDA growth of 26.5% y-o-y and 36.6 q-o-q, respectively, at Rs. 1,730 crore. Improvement in EBITDA margin was driven by richer product mix, operating leverage, and cost reductions.

Domestic outlook remains firm: In FY2022, we expect demand to arise from urban markets as well, where we believe BAL will be a major beneficiary in the 2W space, given its dominant position in the premium bike segment. Demand for 3W is also expected to improve and help BAL to improve its margin because of richer product mix and operating efficiencies. BAL will also benefit from new launches in the premium segment, which it has lined up in the premium segment over the next 12-18 months. Management continues to focus on new launches and expects to launch at least one model (either new or upgraded model) every quarter. Demand in the domestic motorcycle industry is also improving with positive sales growth from August 2020. BAL expects the trend of premiumisation to continue in the domestic 2W industry, which would enable it to gain market share, especially in 125cc+ markets. 3W volumes are also improving on m-o-m basis, as the economy is moving towards normalcy. Domestic 3W sales are expected to improve with the opening of schools, colleges, other educational institutions and corporates.

Focus on high-end premium and super premium bikes: During Q3FY2021, BAL has signed an MOU with the Government of Maharashtra to set a facility in Chakan expected to commence production in 2023. Investment in the proposed facility is estimated to be around Rs. 650 crore and the facility will be primarily used for manufacturing high-end bikes such as KTM, Husqvarna, and Triumph. Moreover, BAL plans to manufacture electric vehicles starting with Chetak from this plant. At Chakan, the company already has a facility, which has installed capacity of 12 lakh units and manufactures premium bikes such as Pulsar, Avenger, KTM, Dominar, Husqvarna, and Chetak. BAL's total installed capacity stands at 66.3 lakh units per annum currently.

Well positioned in export destination markets to increase its market share: BAL has positioned itself strongly in export markets with focus on Nigeria, Bangladesh, Philippines, and Colombia, which accounts for ~50% of its 2W export revenue. In 3W exports, BAL has a strong presence in Nigeria, Egypt, Cambodia, and Iraq. Products are well diversified and have favourable sales mix in under-penetrated markets such as Africa. BAL has improved its brand equity in these markets, which will help to improve its market share. In Q3FY2021, more than 85% of export revenue was generated from geographies where BAL is either No. 1 or No. 2 player. Export growth is organic and will continue to be a long-term driver for BAL. The company has gained market share in all international destinations and aims to further improve its market share, driven by increased distribution reach. BAL's export volumes are recovering and have reached pre-COVID levels in most markets. BAL expects positive growth in these markets in Q4FY2021. BAL is focussing to increase the proportion of high-end Pulsar bikes and other bikes in the export market to improve its product mix.

EBITDA margin to remain above 18%: BAL is aiming to protect its margins as rising input costs are offset by price hikes, better product mix, and cost-control measures. BAL's EBITDA margin of 19.4% in Q3FY2021 may not be sustainable at this level, but we expect margins to be comfortably in excess of 18% going forward.

Strong balance sheet to drive stability in cash flow generation: The company is debt-free and generates strong cash flows, which are enough to expand capacity through internal accruals. The company has a strong long-term revenue visibility, given its leadership position in the premium bikes segment and key export destinations. We expect BAL's earnings to grow by 14.1% in FY2022E and 15.3% in FY2023E, driven by a 14.8% CAGR (FY2021-FY2023) in revenue and 40 bps expansion in EBITDA margin.

Q3FY21 Results Rs cr

Particulars	Q3FY21E	Q3FY20	YoY %	Q2FY21	QoQ %
Net Revenue	8,910	7,640	16.6	7,156	24.5
EBIDTA	1,730	1,367	26.5	1,266	36.6
EBIDTA Margin (%)	19.4	17.9	152 bps	17.7	172 bps
Depreciation	65	62	5.4	64	1.1
Interest	1	0	117.0	3	-61.5
Other Income	369	366	0.8	286	29.2
PBT	2,033	1,671	21.6	1,485	36.9
Tax	477	410	16.3	347	37.4
Reported PAT	1,556	1,262	23.4	1,138	36.7
EPS (Rs.)	53.8	43.6	23.4	39.4	36.7
Adjusted PAT	1,556	1,262	23.4	1,138	36.7

Source: Company; Sharekhan Research

Outlook and Valuation

■ **Sector outlook - Demand picking up in domestic as well as export markets**

2W demand has been improving on m-o-m basis and the trend has continued through the festive season in October-November. Recent commentary from industry leaders suggests that demand is coming even after the festive season. We expect growth momentum to continue in Q4FY2021, driven by strong rural sentiments, supported by higher kharif sowing. The government's reform measures coupled with increased preference for personal transport are expected to improve volumes. We expect strong recovery from FY2022, driven by normalisation of economic activity and pent-up demand (the industry has been in the downcycle for the past seven to eight quarters). Export markets have witnessed notable recovery in volume sales offtake across regional markets - ASEAN, South Asia, Middle East, and Africa. Indian OEMs are positive on recovery and expect these markets to improve.

■ **Company outlook - Strong earnings growth; Upgraded earnings estimates**

BAL is India's second largest motorcycle player with market share of about 20%. The company is the market leader in the premium motorcycle segment (125cc-200cc) with market share of 41%. With new launches, BAL aims to increase its market share further and is targeting market share of around 25% over the next few years. With network expansion, BAL aims to retain its leadership position in motorcycle exports. BAL has a strong balance sheet with zero debt. The company has cash and cash equivalents worth Rs. 16,240 crore with strong return ratios. BAL has healthy dividend pay-out ratio of 40%-45%. BAL is uniquely positioned to benefit from domestic 2W demand and export market, driven by its brand equity and value proposition. We have upgraded our estimates largely due to improvement in operational efficiency. We expect BAL's earnings to grow by 14.1% in FY2022E and 15.3% in FY2023E, driven by a 14.8% CAGR (FY2021-FY2023) in revenue and 40 bps expansion in EBITDA margin.

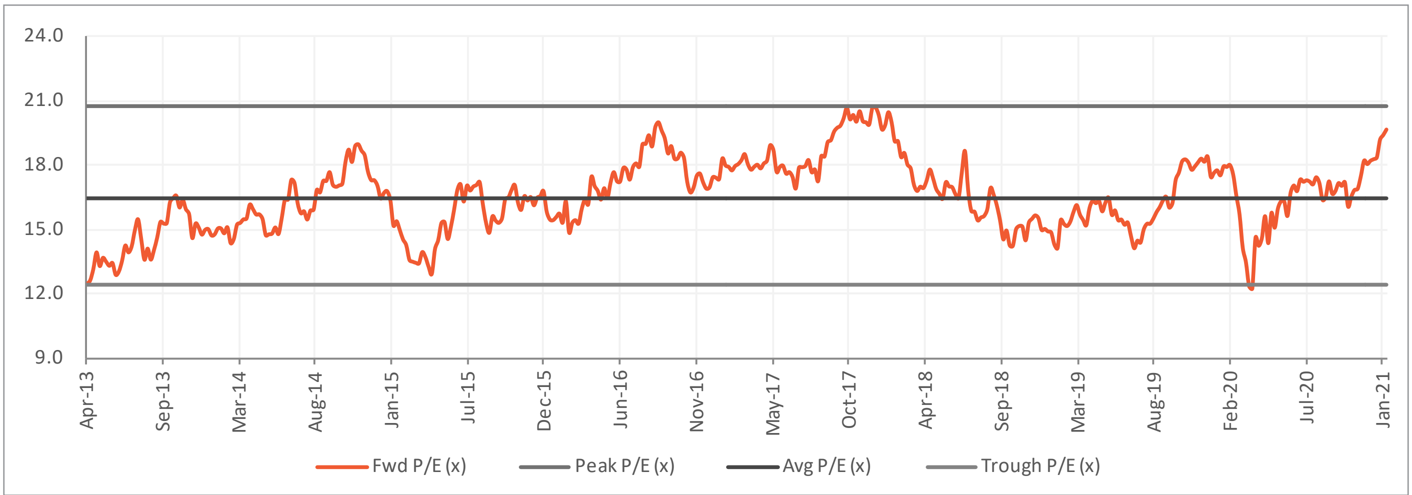
■ **Valuation - Maintain Buy with a revised PT of Rs. 4,327**

BAL is witnessing recovery in domestic (2W and 3W) and export demand. The outlook remains positive with strong recovery expected from FY2022, driven by normalisation of economic activities. OPM would expand because of richer product mix, operating leverage, and cost-control measures. We have increased our earnings estimates to factor in improved business outlook. We value the stock at 20x its FY2023E earning and have arrived at a PT of Rs. 4,327. The stock is attractively valued at a P/E multiple of 17.1x and EV/EBITDA multiple of 11.5x its FY2023E estimates. We retain our Buy rating on the stock with a revised PT of Rs. 4,327.

Target Price Calculation	
FY23E EPS (Rs. per share)	218.5
Target P/E Multiple (x)	20
Target Price (Rs. per share)	4,327
CMP (Rs.)	3,735
Upside (%)	16%

Source: Company Data; Sharekhan Research

One-year forward P/E (x) band



Source: Sharekhan Research

Peer Comparison

Particulars	P/E (x)				EV/EBIDTA (x)				RoCE (%)			
	FY20	FY21E	FY22E	FY23E	FY20	FY21E	FY22E	FY23E	FY20	FY21E	FY22E	FY23E
Bajaj Auto	21.2	22.5	19.7	17.1	18.3	16.8	13.8	11.5	32.1	27.7	28.4	28.8
Hero MotoCorp	20.4	24.3	18.7	16.0	14.2	15.5	11.6	9.3	26.5	23.1	28.2	26.5
TVS Motor	38.9	60.5	29.1	23.3	19.2	22.3	14.6	12.0	15.0	11.8	19.4	21.9

Source: Company, Sharekhan estimates

About company

BAL is one of the leading automobile manufacturers in India and is a leader in the premium motorcycle segment with a lion's share. The company also makes 3W and is a leader in the 3W segment. Motorcycles constitute around 85% of the overall volumes, while 3W contribute around 15% share.

Investment theme

BAL has reported better-than-expected improvement in its OPM, which led to robust PAT growth of 23.4% y-o-y to Rs. 1,556 crore in Q3FY2021. In FY2022, we expect demand to arise from urban markets as well, where we believe BAL will be a major beneficiary in the 2W space, given its dominant position in the premium bike segment. Demand for 3W is also expected to improve and help BAL to improve its margin because of richer product mix and operating efficiencies. BAL is well positioned in export markets to increase its market share. BAL has positioned itself strongly in export markets with focus on Nigeria, Bangladesh, Philippines, and Colombia, which accounts for ~50% of its 2W export revenue. In 3W exports, BAL has a strong presence in Nigeria, Egypt, Cambodia, and Iraq. Products are well diversified and have favourable sales mix in under-penetrated markets such as Africa. BAL has improved its brand equity in these markets, which will help to improve its market share. In Q3FY2021, more than 85% of export revenue was generated from geographies where BAL is either No. 1 or No. 2 player. Export growth is organic and will continue to be a long-term driver for BAL. BAL is expected to benefit from growth in the premium bikes segment, which is recovering, aided by premiumisation trend, new launches, and recovery in urban areas. Moreover, we expect BAL to gain market share in exports, driven by its brand equity and enhanced distribution network. BAL is witnessing recovery in domestic (2W and 3W) and export demand. The outlook remains positive with strong recovery expected from FY2022, driven by normalisation of economic activities. OPM would expand because of richer product mix, operating leverage, and cost-control measures We expect BAL's earnings to grow by 14.1% in FY2022E and 15.3% in FY2023E, driven by a 14.8% CAGR (FY2021-FY2023) in revenue and 40 bps expansion EBITDA margin.

Key Risks

- BAL can lose its market share if EVs in the domestic 3W market rise faster than we expect.
- BAL has significant exposure to export markets. Any slowdown in export markets and unfavourable forex fluctuations can affect the company's profits adversely.

Additional Data

Key management personnel

Rahul Bajaj	Chairman Executive
Rajiv Bajaj	MD & CEO
Rakesh Sharma	Executive Director
Soumen Ray	CFO

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Bajaj Holdings & Investment Ltd	33.43
2	Jamnalal Sons Pvt Ltd	9.08
3	Life Insurance Corp of India	4.76
4	Jaya Hind Industries Ltd	3.35
5	Maharashtra Scooters Ltd	2.34
6	Bajaj Sevashram Pvt Ltd	1.54
7	SBI Funds Management	1.36
8	Bachhraj & Co Pvt Ltd	1.26
9	Norges Bank	1.09
10	Vanguard Group Inc	1.08

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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by BNP PARIBAS

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