



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. 3,901	
Price Target: Rs. 4,589	↔

↑ Upgrade ↔ Maintain ↓ Downgrade

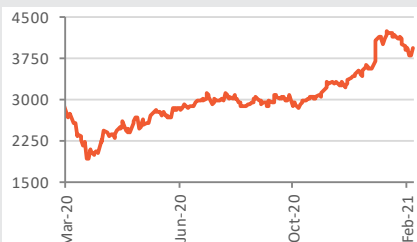
Company details

Market cap:	Rs. 1,12,872 cr
52-week high/low:	Rs. 4,361 / 1,793
NSE volume: (No of shares)	9.8 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	-1.5	24.5	28.1	34.4
Relative to Sensex	-10.1	10.5	-0.6	7.9

Sharekhan Research, Bloomberg

Automobiles

Sharekhan code: BAJAJ-AUTO

Company Update

Summary

- We interacted with the management of Bajaj Auto Limited (BAL) to discuss its plans for electric two-wheelers (e-2Ws) and readiness to benefit from increasing e-2W penetration in the medium to long term. The company is well positioned both in terms of capacity and capability to roll out faster e-2Ws, if the adoption of electric vehicles succeeds at a faster rate.
- BAL is expected to benefit from growth in the premium bikes segment, which is recovering, aided by premiumization trend and new launches. Moreover, we expect BAL to gain market share in exports, driven by its brand equity and enhanced distribution network.
- Improvement in operating profit margin (OPM) witnessed in Q2 & Q3 of FY21 is likely to stay, driven by cost and operational efficiency.
- The stock is trading at P/E multiple of 17.9x and EV/EBITDA multiple of 12.2x its FY2023E estimates and is at below its long-term average multiples. We retain our Buy rating on the stock.

We interacted with the management of Bajaj Auto Limited (BAL) to discuss its plans for electric two-wheelers (e-2Ws) and its readiness to benefit from increasing e-2W penetration in the medium to long term. Bajaj Auto has launched its e-2W scooter with its iconic brand name "Chetak" in January 2020 in two cities, Pune and Bangalore. It plans to launch it in 30 cities over the next 18-24 months. After the phase-I of its expansion plan, BAL will roll a full-scale nationwide rollout, thanks to its significant increase in production capacity after opening its second facility in Chakan. Also, BAL holds 48% stake of its technology partner KTM, which sells around 50,000 e-motorcycles globally. The company is well positioned both in terms of capacity and capability to roll out faster e-2Ws, if the adoption of electric vehicles succeeds at faster rate. We expect Bajaj Auto Limited (BAL) to benefit from the expected recovery from urban markets, where we believe BAL will be a major beneficiary in the two-wheeler (2W) space, given its dominant position in the premium bike segment. Demand for three-wheelers (3Ws) is also expected to improve going forward, as COVID-19 vaccination rolls throughout the country. 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. The 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 its 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. During Q3FY2021, more than 85% of its 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. 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 mix of volume growth and margin expansion. We remain positive on BAL and retain our Buy rating on the stock.

Our Call

Valuation - Maintain Buy with a PT of Rs. 4,589: BAL is witnessing strong recovery in domestic 2Ws and exports demand, while there is slow recovery in 3W demand. The outlook remains positive with strong recovery expected from FY2022, driven by normalisation of economic activities. OPM is likely to 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 have maintained our PT to Rs. 4,589 on 21x its FY2023E estimated earnings. The stock is trading at P/E multiple of 17.9x and EV/EBITDA multiple of 12.2x its FY2023E estimates. We retain our Buy rating on the stock.

Key Risks

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

Valuation (Standalone)

Particulars	FY19	FY20	FY21E	FY22E	Rs cr 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)	149.8	176.3	166.1	189.5	218.5
PE (x)	26.0	22.1	23.5	20.6	17.9
P/BV (x)	5.2	5.7	5.1	4.5	3.9
EV/EBIDTA (x)	18.1	19.3	17.7	14.6	12.2
RoNW (%)	19.9	25.6	21.6	21.7	22.0
RoCE (%)	28.3	32.1	27.7	28.4	28.8

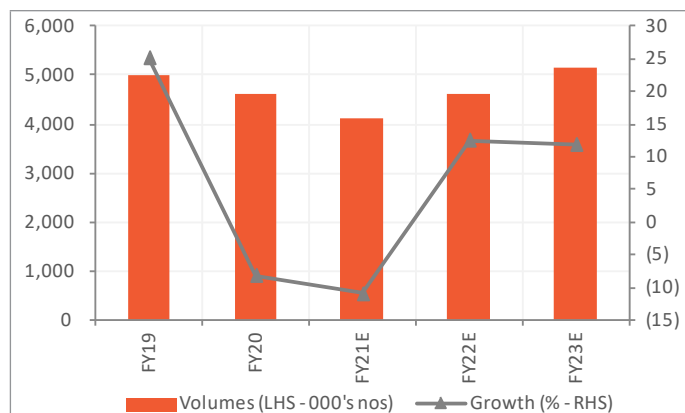
Source: Company; Sharekhan estimates

We interacted with the management of Bajaj Auto Limited (BAL) to discuss its plans for electric two-wheelers (e-2Ws) and readiness to benefit from increasing e-2W penetration in the medium to long term. The key highlights of the interactions are as follows,

- ♦ The e-2W industry is at nascent stage in India with penetration less than 1% of domestic 2W market. The adoption of e-2W would require major push from the government – not just incentivising electric vehicles but also discouraging ICE vehicles.
- ♦ Despite multiple initiatives taken by the Government and serious investments made by OEMs, the EV penetration in the two-wheeler markets has not been picked up as initially planned. There are few concerns that slowed down the e-2W penetrations.
- ♦ At present, the e-2W purchasers are mostly early adopters having decent personal disposable incomes and environment consciousness. Customers normally buy e-2W as additional vehicles. E-2W adoption by mass consumer is expected to take time till get comfort of infrastructure, technology comfort and pricing between the ICE and electric 2Ws narrows.
- ♦ The potential customer has two main challenges while buying e-2W – the cost of e-2W vehicles, which is 50% higher than the comparable ICE technology two-wheeler and secondly, customers' anxiety over the resale value and shorter battery life. An ICE 2W runs for a longer duration and maintenance costs are lower after 4-5 years of use. In case of e-2W, the battery life is around 3-4 years and the cost of replacing battery is as high as 60-70% of the price of new e-2Ws.
- ♦ Bajaj Auto has launched its e-2W scooter with its iconic brand name "Chetak" in January 2020 in two cities, Pune and Bangalore. The product has received a strong response from customers. There is pending registration for more than 50,000 e- scooters. The company has been facing supply issues due to the COVID-19 pandemic earlier and now on back of shortage of semi-conductors.
- ♦ The 'Chetak' is slated to be launched in additional 30 cities over the next 18-24 months. After the phase-I of its expansion plan, BAL will roll a full-scale nationwide rollout, thanks to its significant increase in production capacity after opening of second facility in Chakan.
- ♦ BAL holds 48% stake of its technology partner KTM, which sells around 50,000 e-motorcycles globally. The company is well positioned both in terms of capacity and capability to roll out faster e-2Ws, if the adoption of electric vehicles succeeds at faster rate.

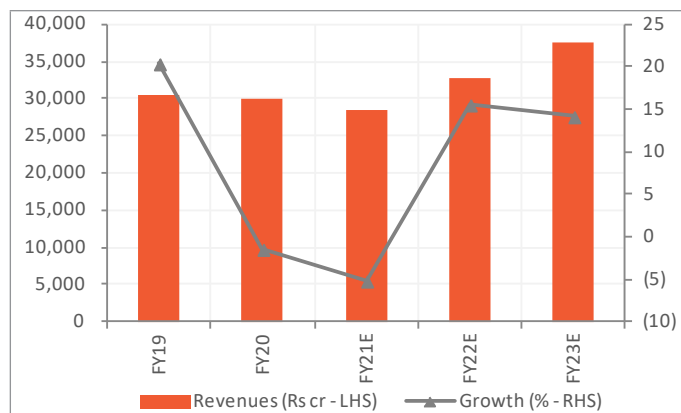
Financials in charts

Volumes Trends



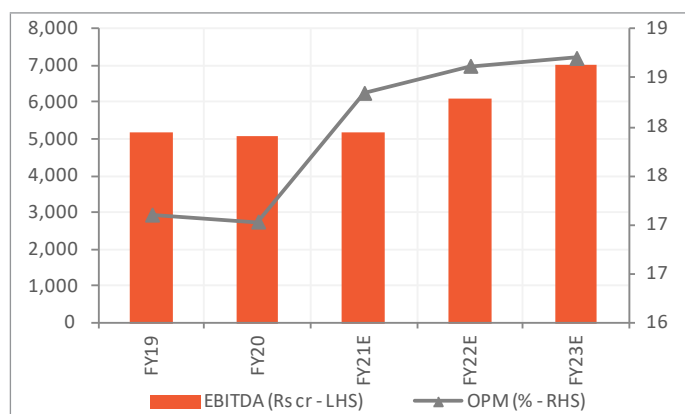
Source: Company, Sharekhan Research

Revenue and Growth trend



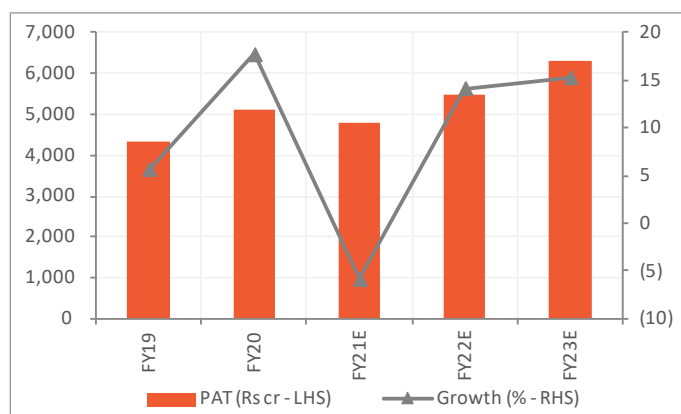
Source: Company, Sharekhan Research

EBITDA and OPM Trend



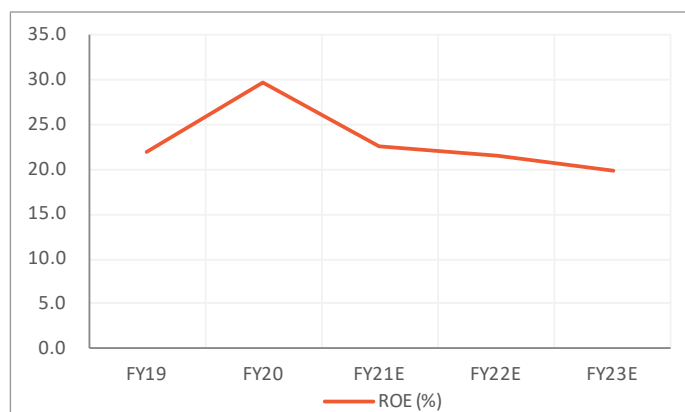
Source: Company, Sharekhan Research

PAT and Growth Trends



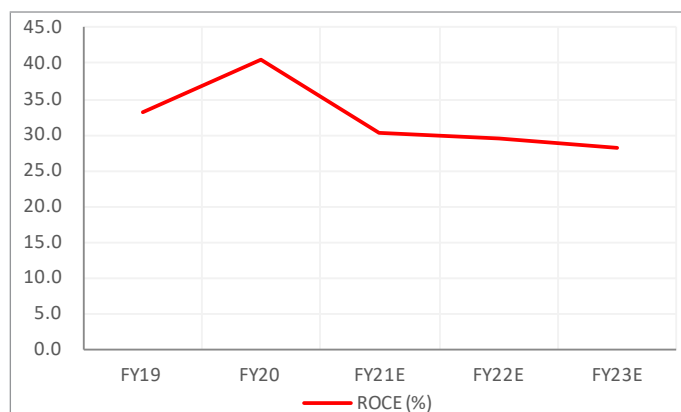
Source: Company, Sharekhan Research

ROE Trend



Source: Company, Sharekhan Research

ROCE Trend



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 a m-o-m basis and the trend has continued through the festive season in October-November 2020. We expect this growth momentum to continue in Q4FY2021, driven by strong rural sentiments, supported by higher kharif sowing. The government's reform measures coupled with the 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. 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.

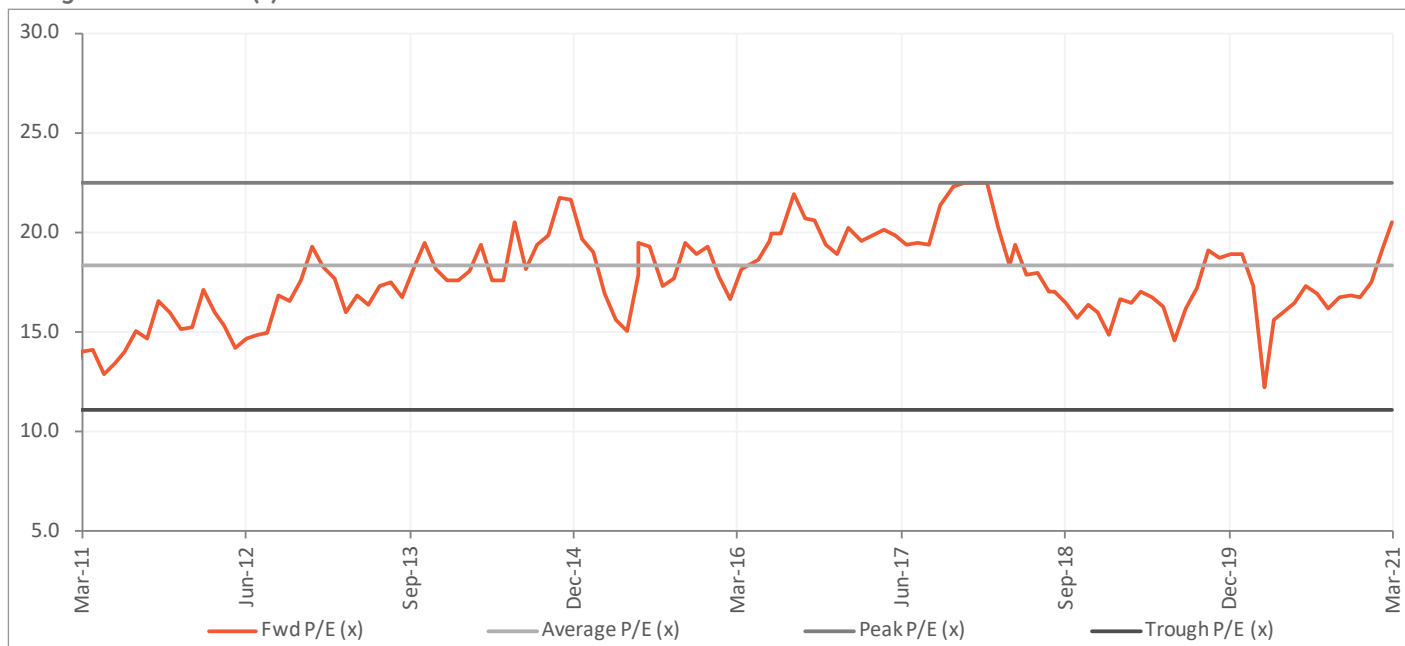
■ Company outlook - Strong earnings growth

BAL is India's second largest motorcycle player with a market share of about 20%. The company is the market leader in the premium motorcycle segment (125cc-200cc) with a 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%. The company is thus uniquely positioned to benefit from domestic 2W demand and export market, driven by its brand equity and value proposition. We expect BAL's earnings to grow by 14.1% in FY2022E and 15.3% in FY2023E, driven by a mix of volume growth and margin expansion.

■ Valuation - Maintain Buy with a PT of Rs. 4,589:

BAL is witnessing strong recovery in domestic 2Ws and exports demand, while there is a slow recovery in 3W demand. The outlook remains positive with strong recovery expected from FY2022, driven by the 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 have maintained our PT to Rs. 4,589 on 21x its FY2023E estimated earnings. The stock is trading at P/E multiple of 17.9x and EV/EBITDA multiple of 12.2x its FY2023E estimates. We retain our Buy rating on the stock.

One-year forward P/E (x) band



Source: Sharekhan Research

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 is the second largest motorcycle manufacturer in India with a market share of about 20%. Over the years, BAL has created a strong brand not only domestically but also in export markets. BAL is the leader in the premium motorcycle segment having a market share of 41%. Apart from premium motorcycles, BAL is also the leader in the 3W segment, commanding a market share of about 57%. Motorcycles constitute about 85% of overall volumes, while 3W contribute 15% share. BAL is well positioned in the domestic as well as in global markets to deliver sustained growth in the long term. The company is a leader in the premium segment bikes such as Pulsar, Avenger, KTM, Dominar, and Husqvarna. Exports currently constitute about 45% of overall volumes, with Africa, Southeast Asia, and Latin America amongst the key markets. During 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. We remain positive on the company's growth prospects going forward.

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

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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 deteriorating 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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