

## Margin bottom not yet in sight, lacks imminent triggers

**About the stock:** Bajaj Auto (BAL) is the second largest motorcycle manufacturer and largest 3-W OEM domestically (FY21 market share at 18%, 50.6%, respectively).

- Exports comprised ~52% of FY21 volumes; >125 cc motorcycles constituted ~28% of FY21 volumes with Pulsar 125 enjoying good success
- Strong b/s with ~₹ 20,000 crore surplus cash on books, history of >20% return ratios & one of the highest dividend yields among Nifty stocks

**Q1FY22 Results:** BAL reported steady Q1FY22 results under the circumstances.

- Net sales were down 14% QoQ to ₹ 7,386 crore, decline being volume-led
- EBITDA margins fell 257 bps QoQ to 15.2% on higher RM, employee costs
- Consequent standalone PAT at ₹ 1,061 crore was lower by 20.3% QoQ

**What should investors do?** BAL's stock price has outperformed the Nifty Auto index in the past five years, having grown at ~8% CAGR (~₹ 2,700 in July 2016).

- We downgrade from BUY to **HOLD** on margin pressures, EV transition risk.

**Target Price and Valuation:** We value BAL at ₹ 4,350 on SOTP basis (22x PE on FY23E standalone EPS, 2x P/B on KTM investment; earlier target price ₹ 4,500)

**Key triggers for future price performance:**

- We expect volume, net sales CAGR of 13.3%, 19.4% over FY21-23E (2-W CAGR 12.4%, 3-W CAGR 21.4%) aided by low base, pent-up demand
- Under-recovery of cost increases, elevated employee costs to pressurise margins over medium term; margins seen stabilising ~16% by FY23E
- Revised dividend distribution policy (up to 90% payout for surplus funds in excess of ₹ 15,000 crore) to ensure high dividend yield in future
- Well charted transition strategy encompassing switch to electrification

**Alternate Stock Idea:** In our auto OEM coverage we also like M&M.

- Focused on prudent capital allocation, UV differentiation & EV proactiveness
- BUY with a target price of ₹ 1,000



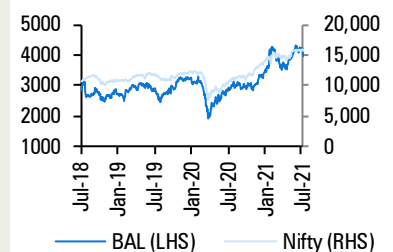
### Particulars

Particular	₹ crore
Market Capitalization	1,11,494
Total Debt (FY21)	0.0
Cash & Liquid Invests (FY21)	21,925
EV	89,569
52 week H/L (₹)	4,361 / 2,363
Equity capital (₹)	289.4
Face value (₹)	₹ 10

### Shareholding pattern

	Sep-20	Dec-20	Mar-21	Jun-21
Promoter	53.7	53.7	53.7	53.7
FII	13.6	13.1	12.0	11.8
DII	10.4	9.1	12.3	12.7
Other	22.3	24.1	22.0	21.8

### Price Chart



### Recent event & key risks

- Calibrated price hikes underway
- Key Risk:** (i) Prolonged slowdown in domestic 3-W, (ii) Export incentives reinstatement could boost margins

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### Key Financial Summary

Key Financials	FY19	FY20	FY21	5 year CAGR (FY16-21)	FY22E	FY23E	2 year CAGR (FY21-23)
Net Sales	30,250.0	29,918.6	27,741.1	4.2%	34,836.2	39,538.7	19.4%
EBITDA	4,982.0	5,096.2	4,928.5	0.6%	5,317.4	6,316.5	13.2%
EBITDA Margins (%)	16.5	17.0	17.8		15.3	16.0	
Net Profit	4,675.1	5,100.0	4,554.6	3.0%	4,853.9	5,602.9	10.9%
EPS (₹)	161.6	176.2	157.4		167.7	193.6	
P/E	23.8	21.9	24.5		23.0	19.9	
RoNW (%)	19.9	25.6	18.1		18.9	21.4	
RoCE (%)	21.1	23.9	18.2		19.3	22.5	

Source: Company, ICICI Direct Research

## Key takeaways of recent quarter & conference call highlights

### Q1FY22 Results:

- Total volumes for the quarter were at 10.06 lakh units, down 14% QoQ. The 2-W volumes fell 14.2%, with 3-W decline at 12.6% (3-W comprised ~10% of total volumes, unchanged QoQ). Domestic volumes were down ~33% QoQ, with exports up ~2% QoQ
- Blended ASPs at ₹ 73,419/unit were nearly flat QoQ
- Gross margins declined ~110 bps QoQ, with employee costs rising 130 bps QoQ on percentage of sales basis
- BAL informed it would be setting up a wholly-owned subsidiary for manufacturing electric 2-W, 3-W and light 4-W

### Q1FY22 Earnings Conference Call highlights

- The company expects to retain present exports run rate (~2 lakh units per month) in coming months. Near term retail performance for domestic 2-W would run ahead of wholesales amid higher inventory and consequently be flattish YoY. Domestic 3-W performance in Q2FY22E is set to be higher QoQ
- Africa, Latin America and Middle East markets are near normalcy while Asean region is still grappling with Covid related weakness
- BAL's global market share in 2-W, 3-W has risen 2%, 6% QoQ, respectively. The company is deriving >85% of exports revenue from markets where it is a top-2 player and is thereby finding success in its pricing actions.
- For BAL, >= 125 cc motorcycle segment constitutes 60% of sales vs. 45% for industry, with the growth being driven by Pulsar 125. BAL's market share in the segment is at an all-time high of 28%
- The 3-W performance in June 2021 was better-than-expected. The company is now market leader in each 3-W segment
- The company reiterated that present CNG 3-W provide a much better business case than electric 3-W. The government's CNG push (envisages setting up 9,000 CNG stations by 2025 vs. 1,600 at present) is set to be a significant driver for the space. It is estimated that installation of 100 CNG stations creates demand for 10,000 3-W. BAL has ~90% market share in CNG 3-W and is likely to launch its electric 3-W by end CY21
- BAL expects electrification penetration in 2-W to be at a significant level only after three to five years
- Supply chain preparedness is healthy at present but container shortage related issues persist and are adding to cost escalation

Of 3.7% QoQ cost increase in Q1FY22, BAL recovered ~1.5% via price hikes. Lower operating leverage impacted margins by 160 bps. The company expects further ~3% QoQ cost increase in Q2FY22E, of which two-third would be recovered by July price hikes. Employee cost run rate, going forward, is expected to be ~₹ 360 crore

## Peer comparison

Exhibit 1: ICICI Direct coverage universe (2-W OEMs)

Company	CMP	TP	Rating	Mcap	2-W Lakh volumes			EBITDA margin (%)			RoCE (%)			Dividend yield (%)			P/E		
	₹	₹			₹ crore	FY21	FY22E	FY23E	FY21	FY22E	FY23E	FY21	FY22E	FY23E	FY21	FY22E	FY23E	FY21	FY22E
Bajaj Auto (BAAUTO)	3,853	4,350	Hold	1,11,482	36	41	46	17.8	15.3	16.0	18.2	19.3	22.5	3.6	3.9	4.5	24.5	23.0	19.9
Hero Moto (HERHON)	2,838	3,440	Buy	56,700	58	67	73	13.0	12.5	13.0	20.8	23.1	24.5	3.7	3.7	4.2	19.1	16.6	14.4
Eicher Motors (EICMOT)	2,560	2,970	Hold	69,978	6	7	8	20.4	21.5	23.4	11.3	13.5	15.8	0.7	0.8	1.0	51.9	38.4	29.3

Source: Company, ICICI Direct Research

Exhibit 2: Variance Analysis

	Q1FY22	Q1FY22E	Q1FY21	YoY (%)	Q4FY21	QoQ (%)	Comments
Total Operating Income	7,386	7,394	3,079	139.9	8,596	-14.1	Net sales came in line with our estimates amid 14% QoQ total volume decline and nearly flat blended ASPs
Raw Material Expenses	5,394	5,366	2,067	161.0	6,177	-12.7	
Employee Expenses	362	307	337	7.2	307	17.8	Employee costs stood higher than anticipated
Other Expenses	512	554	269	90.8	594	-13.7	
EBITDA	1,119.8	1,172.9	408.5	174.1	1,524.1	-26.5	
EBITDA Margin (%)	15.2	15.9	13.3	189 bps	17.7	-257 bps	Margins at 15.2% were lower by 257 bps sequentially amid ~110 bps gross margin depletion and 130 bps increase in employee costs on percentage of sales basis.
Other Income	329.3	322.3	337.9	-2.5	283.6	16.1	
Depreciation	64.1	66.1	63.8	0.4	66.2	-3.2	Depreciation was on expected lines
Interest	2	0	1	141.1	2	12.3	
PBT	1383	1429	682	102.8	1739	-20.5	
Total Tax	322	336	154	109.3	407	-21.1	
Reported PAT	1061.2	1093.2	528.0	101.0	1332.1	-20.3	Reported PAT was broadly in line with estimates
EPS (₹)	36.7	37.8	18.2	101.0	46.0	-20.3	
<b>Key Metrics</b>							
Blended ASP (₹/ unit)	73419	73499	69493	5.6	73492	-0.1	Blended ASP's were flat QoQ at ₹ 73.4k/unit

Source: Company, ICICI Direct Research

Exhibit 3: Change in estimates

(₹ Crore)	FY22E			FY23E			Comments
	Old	New	% Change	Old	New	% Change	
Revenue	36,764	34,836	-5.2	41,429	39,539	-4.6	We trim our revenue estimates on the back of Covid impact in Q1FY22 and delayed recovery expected in key export markets.
EBITDA	6,034	5,317	-11.9	7,053	6,317	-10.4	
EBITDA Margin (%)	16.4	15.3	-115 bps	17.0	16.0	-105 bps	Rise in commodity costs to impact margins in near term. We trim our margin estimates by ~100 bps for FY22E, FY23E
PAT	5,309	4,854	-8.6	6,077	5,603	-7.8	
EPS (₹)	183.5	167.7	-8.6	210.0	193.6	-7.8	PAT estimates are revised downwards tracking lower sales and margin estimates

Source: ICICI Direct Research

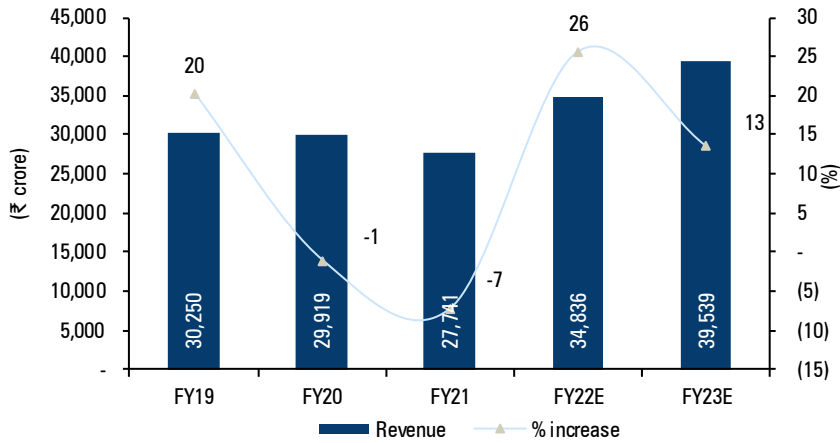
Exhibit 4: Assumptions

Units (lakh)	Current				Earlier				Comments
	FY18	FY19	FY20	FY21	FY22E	FY23E	FY22E	FY23E	
Motorcycle volumes	33.7	42.4	39.5	36.1	41.4	45.6	43.7	47.6	Total volume CAGR for FY21-23E is expected at 13.3%, led by 21.4% growth in 3-W on diminished base. We expect exports to carry the burden, with growth CAGR placed at 16.2%. Our ASP estimates are revised upwards building in product mix improvement and price hikes across geographies.
Three-Wheeler volumes	6.4	7.8	6.7	3.7	4.6	5.4	5.0	5.8	
Total volumes	40.1	50.2	46.2	39.7	46.0	51.0	48.7	53.4	
Export volumes	16.6	20.8	21.7	20.5	24.8	27.7	25.0	27.5	
Domestic revenues (₹ crore)	15,396	18,099	17,169	14,609	17,713	19,851	19,793	22,137	
Export revenues (\$ mn)	1,400	1,642	1,677	1,694	2,209	2,512	2,186	2,453	
US\$INR Realisation rate	67	70	71	74	74	75	74	75	
Export ASP (\$/unit)	872	790	772	822	890	906	874	892	
Blended ASP (₹/unit)	62,640	58,905	63,077	68,295	74,043	75,880	73,899	75,916	

Source: ICICI Direct Research

Financial story in charts....

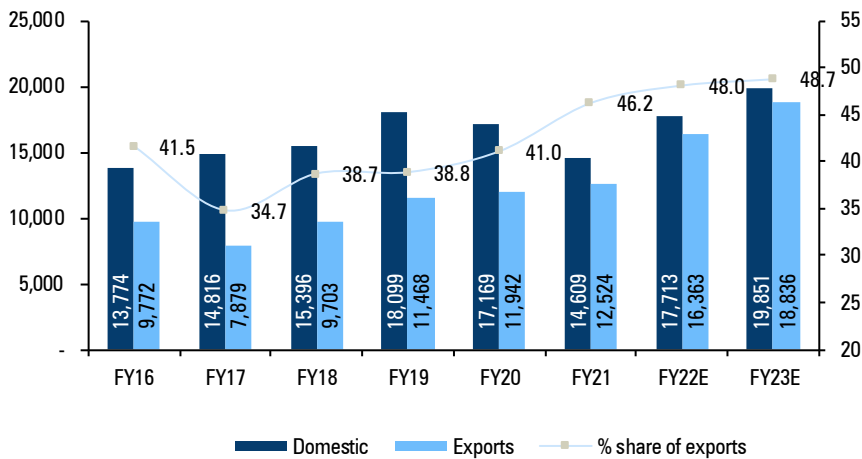
Exhibit 5: Trend in topline



Source: Company, ICICI Direct Research

We expect net sales to grow at 19.4% CAGR over FY21-23E on the back of 13.3% volume CAGR

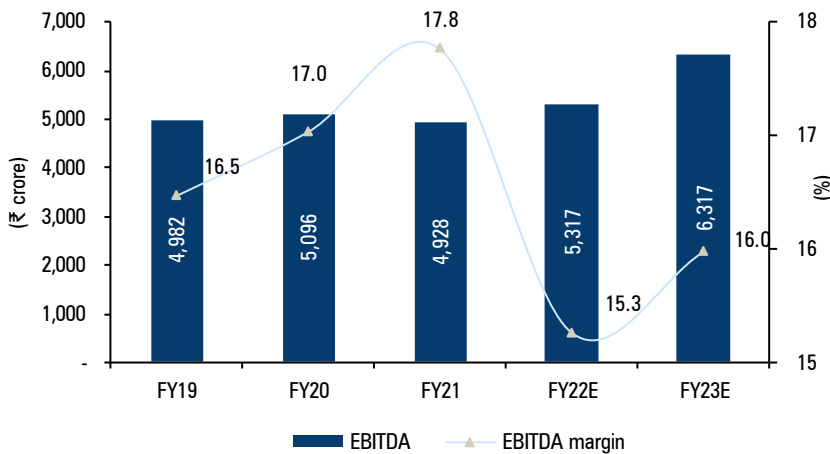
Exhibit 6: Trend in domestic and exports revenue mix



Source: Company, ICICI Direct Research

Exports are expected to grow to 48.7% of overall revenues by FY23E

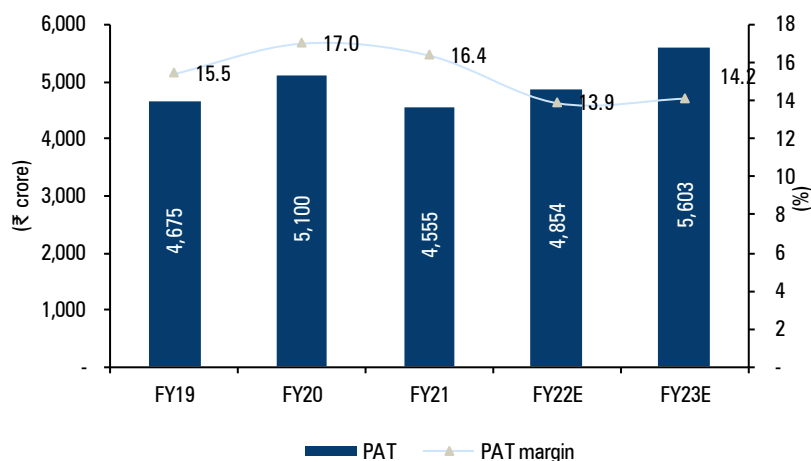
Exhibit 7: Trend in EBITDA and EBITDA margins



Source: Company, ICICI Direct Research

Inability to recover increased input costs via price hikes and higher trajectory of employee costs, going forward, are set to result in margins stabilising at ~16% levels by FY23E

Exhibit 8: Trend in profitability



PAT is expected to grow at 10.9% CAGR over FY21-23E to ₹ 5,603 crore

Source: Company, ICICI Direct Research

Exhibit 9: Valuation summary

	Sales (₹ cr)	Growth (%)	EPS (₹)	Growth (%)	PE (x)	EV/EBITDA (x)	RoNW (%)	RoCE (%)
FY19	30,250.0	20.2	161.6	14.9	23.8	18.6	19.9	21.1
FY20	29,918.6	(1.1)	176.2	9.1	21.9	18.5	25.6	23.9
FY21	27,741.1	-7.3	157.4	-10.7	24.5	18.2	18.1	18.2
FY22E	34,836.2	25.6	167.7	6.6	23.0	16.9	18.9	19.3
FY23E	39,538.7	13.5	193.6	15.4	19.9	14.2	21.4	22.5

Source: Company, ICICI Direct Research

Exhibit 10: SOTP valuation

SOTP Valuation	Estimated value	Per share (₹)	Remark
<b>Core Business</b>			
FY23E EPS (₹)	193.6		
Multiple (x)	22.0		2x PEG to 11% earnings CAGR over FY21-23E
<b>Value per share (₹)</b>		<b>4,260</b>	
<b>Stake in KTM (48%)</b>			
KTM value derived back to Bajaj (₹ crore)	2562		~2x of Invested Capital (₹ 1220 crore)
Value per share		<b>90</b>	
<b>Total Value per Share (₹)</b>		<b>4,350</b>	

Source: ICICI Direct Research

## Financial Summary

Exhibit 11: Profit and loss statement				
	₹ crore			
(Year-end March)	FY20	FY21	FY22E	FY23E
Total operating Income	29918.6	27741.1	34836.2	39538.7
Growth (%)	-1.1	-7.3	25.6	13.5
Raw Material Expenses	21,008.3	19,609.7	25,677.0	28,946.8
Employee Expenses	1,389.2	1,286.0	1,438.2	1,538.5
Other expenses	2,454.9	1,929.3	2,412.0	2,746.1
Total Operating Expenditure	24,822.4	22,812.6	29,518.8	33,222.2
<b>EBITDA</b>	<b>5096.2</b>	<b>4928.5</b>	<b>5317.4</b>	<b>6316.5</b>
Growth (%)	2.3	-3.3	7.9	18.8
Depreciation	246.4	259.3	261.3	284.7
Interest	3.2	6.7	5.1	2.6
Other Income	1,733.6	1,276.5	1,289.6	1,294.8
PBT	6,580.2	5,939.0	6,340.6	7,324.1
Total Tax	1,480.2	1,384.4	1,486.6	1,721.2
<b>PAT</b>	<b>5100.0</b>	<b>4554.6</b>	<b>4853.9</b>	<b>5602.9</b>
Growth (%)	9.1	-10.7	6.6	15.4
<b>EPS (₹)</b>	<b>176.2</b>	<b>157.4</b>	<b>167.7</b>	<b>193.6</b>

Source: Company, ICICI Direct Research

Exhibit 12: Cash flow statement				
	₹ crore			
(Year-end March)	FY20	FY21	FY22E	FY23E
Profit after Tax	5,100.0	4,554.6	4,853.9	5,602.9
Add: Depreciation	246.4	259.3	261.3	284.7
Sub: Other Income	1,733.6	1,276.5	1,289.6	1,294.8
(Inc)/dec in Current Assets	1,054.4	-2,110.7	-444.5	-818.6
Inc/(dec) in CL and Provisions	-569.6	1,368.5	-288.2	599.1
<b>CF from operating activities</b>	<b>4050.0</b>	<b>2823.3</b>	<b>3248.4</b>	<b>4482.2</b>
(Inc)/dec in Investments	973.7	-4,434.7	450.0	-50.0
(Inc)/dec in Fixed Assets	-193.7	-181.0	-515.0	-515.0
Others	-216.8	19.7	-95.0	-95.0
Add: Other Income	1,733.6	1,276.5	1,289.6	1,294.8
<b>CF from investing activities</b>	<b>2296.7</b>	<b>-3319.5</b>	<b>1129.6</b>	<b>634.8</b>
Inc/(dec) in loan funds	0.0	0.0	0.0	0.0
Dividend paid & dividend tax	-4,186.2	-4,051.2	-4,340.6	-5,064.0
Inc/(dec) in Sec. premium	0.0	0.0	0.0	0.0
Others	-2,771.4	4,766.6	-19.1	-16.6
<b>CF from financing activities</b>	<b>-6957.6</b>	<b>715.4</b>	<b>-4359.7</b>	<b>-5080.5</b>
Net Cash flow	-610.8	219.3	18.3	36.5
Opening Cash	918.8	308.0	527.3	545.6
<b>Closing Cash</b>	<b>308.0</b>	<b>527.3</b>	<b>545.6</b>	<b>582.1</b>

Source: Company, ICICI Direct Research

Exhibit 13: Balance Sheet				
	₹ crore			
(Year-end March)	FY20	FY21	FY22E	FY23E
<b>Liabilities</b>				
Equity Capital	289.4	289.4	289.4	289.4
Reserve and Surplus	19,636.1	24,912.8	25,412.2	25,937.2
<b>Total Shareholders funds</b>	<b>19,925.5</b>	<b>25,202.2</b>	<b>25,701.6</b>	<b>26,226.5</b>
Total Debt	-	-	-	-
Deferred Tax Liability	346.4	522.1	522.1	522.1
Other non-current liabilities	0.8	0.5	0.5	0.5
<b>Total Liabilities</b>	<b>20,520.1</b>	<b>25,886.9</b>	<b>26,396.3</b>	<b>26,931.3</b>
<b>Assets</b>				
Gross Block	4,090.9	4,248.7	4,464.7	4,664.7
Less: Acc Depreciation	2,435.0	2,631.1	2,892.4	3,177.1
Net Block	1,655.9	1,617.6	1,572.3	1,487.7
Capital WIP	46.5	16.0	300.0	600.0
<b>Total Fixed Assets</b>	<b>1,702.5</b>	<b>1,633.6</b>	<b>1,872.3</b>	<b>2,087.7</b>
Investments	18,196.3	22,631.0	22,231.0	22,331.0
Inventory	1,063.5	1,493.9	1,431.6	1,624.9
Debtors	1,725.1	2,716.9	2,863.2	3,249.8
Loans and Advances	6.1	5.7	7.2	8.2
Other current assets	714.3	1,403.2	1,762.1	1,999.9
<b>Cash</b>	<b>308.0</b>	<b>527.3</b>	<b>545.6</b>	<b>582.1</b>
Total Current Assets	3,817.0	6,147.0	6,609.7	7,464.8
Creditors	3,199.7	4,573.8	4,294.9	4,874.6
Provisions	158.0	152.4	143.1	162.4
Other current liabilities	347.3	509.6	639.9	726.3
Total Current Liabilities	4,253.3	5,643.2	5,505.3	6,210.8
<b>Net Current Assets</b>	<b>(436.3)</b>	<b>503.7</b>	<b>1,104.4</b>	<b>1,254.0</b>
Deferred Tax asset	-	-	-	-
<b>Application of Funds</b>	<b>20,520.1</b>	<b>25,886.9</b>	<b>26,396.3</b>	<b>26,931.3</b>

Source: Company, ICICI Direct Research

Exhibit 14: Key ratios				
(Year-end March)	FY20	FY21	FY22E	FY23E
<b>Per share data (₹)</b>				
EPS	176.2	157.4	167.7	193.6
Cash EPS	184.8	166.4	176.8	203.5
BV	688.6	870.9	888.2	906.3
DPS	120.0	140.0	150.0	175.0
Cash Per Share	10.6	18.2	18.9	20.1
<b>Operating Ratios (%)</b>				
EBITDA Margin	17.0	17.8	15.3	16.0
PBT / Net sales	16.2	16.8	14.5	15.3
PAT Margin	17.0	16.4	13.9	13.9
Inventory days	13.0	19.7	15.0	15.0
Debtor days	21.0	35.7	30.0	30.0
Creditor days	39.0	60.2	45.0	45.0
<b>Return Ratios (%)</b>				
RoE	23.9	18.2	19.3	22.5
RoCE	25.6	18.1	18.9	21.4
RoIC	164.1	123.4	114.1	132.0
<b>Valuation Ratios (x)</b>				
Core P/E	21.9	24.5	23.0	19.9
EV / EBITDA	18.5	18.2	16.9	14.2
EV / Net Sales	3.1	3.2	2.6	2.3
Market Cap / Sales	3.7	4.0	3.2	2.8
Price to Book Value	5.6	4.4	4.3	4.3
<b>Solvency Ratios</b>				
Current Ratio	0.9	1.1	1.2	1.2
<b>Quick Ratio</b>	<b>0.7</b>	<b>0.8</b>	<b>0.9</b>	<b>0.9</b>

Source: Company, ICICI Direct Research

**Exhibit 15: ICICI Direct coverage universe (Auto & Auto Ancillary)**

Sector / Company	CMP	TP	Rating	M Cap	EPS (₹)			P/E (x)			EV/EBITDA (x)			RoCE (%)			RoE (%)		
	(₹)	(₹)		(₹ Cr)	FY21P	FY22E	FY23E	FY21P	FY22E	FY23E	FY21P	FY22E	FY23E	FY21P	FY22E	FY23E	FY21P	FY22E	FY23E
Apollo Tyre (APOTYR)	221	275	Buy	14,034	5.5	9.9	16.2	40.1	22.4	13.6	6.7	6.9	5.0	7.6	6.1	9.1	6.4	5.3	8.2
Ashok Leyland (ASHLEY)	124	150	Buy	36,296	-1.1	1.1	4.4	-116.0	112.5	28.2	73.3	29.9	14.6	-1.9	4.8	15.7	-4.4	4.5	16.5
<b>Bajaj Auto (BAAUTO)</b>	<b>3,853</b>	<b>4,350</b>	<b>Hold</b>	<b>1,11,494</b>	<b>157.4</b>	<b>167.7</b>	<b>193.6</b>	<b>24.5</b>	<b>23.0</b>	<b>19.9</b>	<b>18.2</b>	<b>16.9</b>	<b>14.2</b>	<b>18.2</b>	<b>19.3</b>	<b>22.5</b>	<b>18.1</b>	<b>18.9</b>	<b>21.4</b>
Balkrishna Ind. (BALIND)	2,331	2,250	Buy	45,062	59.8	68.2	80.5	39.0	34.2	29.0	25.5	21.9	18.6	19.3	20.4	21.6	19.2	19.0	19.4
Bharat Forge (BHAFOR)	802	875	Buy	37,318	-2.7	15.9	25.0	NM	50.5	32.1	46.0	24.7	17.6	2.2	8.0	12.1	3.3	12.3	16.9
Eicher Motors (EICMOT)	2,560	2,970	Hold	69,776	49.3	66.7	87.4	51.9	38.4	29.3	34.9	26.7	20.3	11.3	13.5	15.8	11.8	14.3	16.6
Escorts (ESCORT)	1,168	1,140	Hold	14,317	71.2	62.0	76.9	16.4	18.8	15.2	10.0	11.5	9.0	18.7	13.8	14.8	16.2	12.6	13.7
Hero Moto (HERHON)	2,838	3,440	Buy	56,675	148.4	170.8	196.5	19.1	16.6	14.4	12.1	10.3	8.8	20.8	23.1	24.5	19.5	20.7	21.7
M&M (MAHMAH)	758	1,000	Buy	94,247	2.3	29.9	37.8	336.7	25.4	20.1	14.0	14.7	11.8	9.5	8.2	10.5	2.7	9.6	11.1
Maruti Suzuki (MARUTI)	7,296	6,080	Reduce	2,20,392	140.0	172.9	225.1	52.1	42.2	32.4	33.1	24.7	18.4	4.3	6.6	9.1	8.2	9.5	11.4
Minda Industries (MININD)	728	725	Buy	19,791	7.6	10.9	19.1	95.8	66.9	38.0	28.4	23.8	16.8	9.1	10.6	16.7	10.4	14.2	19.6
Motherson (MOTSUM)	237	300	Buy	74,922	3.3	7.4	10.0	NM	31.9	23.8	16.5	10.0	8.1	6.7	16.2	20.5	8.8	16.7	19.7
Tata Motors (TATMOT)	303	375	Buy	1,08,866	-35.0	5.5	37.6	NM	55.4	8.0	4.9	5.2	3.3	6.4	6.6	14.3	-23.6	3.6	19.6

Source: Company, ICICI Direct Research

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Buy: >15%

Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



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