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Stock Update

Maruti Suzuki India Ltd

Growth prospects stay bright despite dim Q2

Automobiles		Sharekhan code: MARUTI		
Reco/View	Reco: **Buy**	↔	CMP: **Rs. 7,353**	Price Target: **Rs. 8,251** ↑

↑ Upgrade ↔ Maintain ↓ Downgrade

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		↔	

ESG Disclosure Score NEW

ESG RISK RATING 26.89

Updated Oct 08, 2021

Medium Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

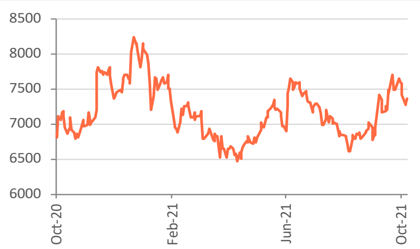
Company details

Market cap:	Rs. 2,22,119 cr
52-week high/low:	Rs. 8,400 / 6,301
NSE volume: (No of shares)	6.84 lakh
BSE code:	532500
NSE code:	MARUTI
Free float: (No of shares)	13.2 cr

Shareholding (%)

Promoters	56.4
FII	22.5
DII	16.0
Others	5.1

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	5.8	1.6	10.7	7.1
Relative to Sensex	4.0	-14.1	-17.5	-43.1

Sharekhan Research, Bloomberg

Summary

- We retain Buy on Maruti Suzuki India Limited (MSIL) with a revised PT of Rs. 8,251.
- Maruti Suzuki India Limited (MSIL) reported weak operational performance during Q2FY22, led by adverse commodity prices and lower volumes.
- We expect volume recovery ahead as the supply constraints is expected to improve gradually in H2FY2022, which would improve revenue and profitability of the company.
- MSIL is likely to benefit from buoyant PV demand, driven by rising demand in tier-2 and tier-3 cities and rural areas. MSIL is expected to sustain its dominant market share, aided by strong product portfolio and position, brand appeal, and ability to frequently launch new models.
- Earnings to post a 40.1% CAGR during FY2021-FY2023E, driven by 21% revenue CAGR and 360-bps improvement in EBITDA margin.

Maruti Suzuki India Limited (MSIL) reported weak operational performance during Q2FY22, led by adverse commodity prices. The volume sales during the quarter was impacted by the shortage of electronic components leading to lower capacity utilisation. Net revenue was up 9.6% y-o-y to Rs 20,539 crore, led by 13.5% growth in average realisation, partially mitigated by 3.5% decline in volumes. EBITDA margin contracted sharper than our expectations. EBITDA margin for the Q2FY22 stood at 4.2%, which is 50 bps q-o-q and 620 bps y-o-y decline. As a result, the EBITDA and PAT declined 55.8% y-o-y and 65.3% y-o-y to Rs855 crore and Rs475 crore respectively. The management commentary was cautiously positive, as the company expects supply constraints due to electronic component shortage to improve gradually going forward. We continue to remain positive on the company and expects demand for passenger vehicles (PV) to remain buoyant, driven by rising demand in tier-2 and tier-3 cities and rural areas. MSIL is expected to sustain its dominant market share, aided by strong product portfolio and position, brand appeal, and ability to frequently launch new models. We reiterate Buy rating on the company with a revised PT of RS 8,251.

Key positives

- Improvement in average realization of 13.5% y-o-y to Rs. 5,41,151 per vehicle helped the revenue growth, despite a 3.5% y-o-y decline in volumes. Price hikes and better product mix boosted the average realization.
- A strong order book of more than 200,000 vehicles and lower inventory at dealer levels

Key negatives

- EBITDA margin contracted sharper than our expectations at 4.2%, which is 50 bps q-o-q and 620 bps y-o-y decline.
- Losing market share in the mid-SUV segment due to stronger performance by its competitor.

Management Commentary

- The management was cautiously optimistic on growth prospects. The company maintains its capex programme for the year at Rs. 4,500 crore and has allocated an additional Rs2,200 crore capex for further capacity expansion.
- CNG variants and exports continue to remain buoyant, and the management expects the trend to continue going forward.

Our Call

Valuation – Maintain Buy with a revised PT of Rs. 8,251: MSIL is expected to witness a recovery in domestic demand with sales volumes sustaining growth, despite the near-term challenges of electronic component shortage. Sales enquiries remain strong with orderbook currently more than 2,00,000 units. We expect strong recovery from FY2022, driven by normalisation of economic activity. Margins are expected to improve from 7.5% in FY2021 to 11.1% in FY2023E, driven by operating leverage and cost-control measures. We remain positive on the company on account of its structural growth outlook (which remains intact), healthy balance sheet, and comfortable valuations. The stock is trading at P/E of 26.7x and EV/EBITDA of 19.5x its FY2023E estimates. We retain our Buy rating on MSIL with a revised PT of Rs. 8,251.

Key Risks

The fear arising of new variants and the third wave of COVID-19 remains a potential concern. Any significant delay in improvement of chips shortage could impact our volume estimates.

Valuation (standalone) Rs cr

Particulars	FY21	FY22E	FY23E	FY24E
Net sales	70,333	84,410	1,02,894	1,15,241
Growth (%)	(7.0)	20.0	21.9	12.0
EBITDA	5,287	6,808	11,391	12,920
EBIDTA %	7.5	8.1	11.1	11.2
PAT	4,230	4,866	8,308	9,466
Growth (%)	(25.1)	15.0	70.7	13.9
FD EPS (Rs)	140.0	161.1	275.0	313.3
P/E (x)	52.5	45.6	26.7	23.5
P/B (x)	4.3	4.1	3.7	3.3
EV/EBITDA (x)	41.8	32.7	19.5	17.7
RoE (%)	8.2	8.9	13.7	14.1
RoCE (%)	9.4	11.0	16.9	17.4

Source: Company; Sharekhan estimates

Key Highlights of Conference Call

Weak Q2FY2022 quarter for Maruti led by poor operational performance:

The company reported weak operational performance during Q2FY22, led by adverse commodity prices. The volume sales during the quarter was impacted by shortage of electronic components leading to lower capacity utilisation. Net revenue was up 9.6% y-o-y to Rs 20,539 crore, led by 13.5% growth in average realisation, partially mitigated by 3.5% decline in volumes. The increase in average realisation was on the back of price hikes taken by the company during the year, due to rise in raw material costs. The decline in volumes was impacted by chips shortage. EBITDA margin contracted sharper than our expectations. EBITDA margin for the Q2FY22 stood at 4.2%, which is 50 bps q-o-q and 620 bps y-o-y decline. The EBITDA margins were adversely impacted by negative operating leverage and rise in raw material cost. There was decline of 110 bps q-o-q on the gross margins. Against the increase of 7.7% q-o-q in average realisation, the raw material cost per vehicle and operating expenses per vehicle increased 9.2% q-o-q and 8.2% q-o-q respectively. As a result, the EBITDA and PAT declined 55.8% y-o-y and 65.3% y-o-y to Rs855 crore and Rs475 crore respectively .

Management is cautiously optimistic on demand outlook:

The Management was cautiously optimistic on demand outlook for domestic as well as export markets. The company is witnessing pick-up in demand with the enquiries and bookings going up month-on-month. The company has witnessed strong demand from rural and semi-urban areas, where MSIL's distribution network and product portfolio fit aptly. Improving income levels of individuals, firms, and corporates are likely to keep demand strong in the medium term. The government's decision to expedite the vaccination programme will help to revive the economy sooner. We expect FY2022 to be a stronger year for MSIL, driven by strong volume growth. Volume growth will be aided by new product launches, a quick economic recovery, upside from COVID-19 vaccines, and a low base. MSIL's strong distribution network in the segment and rural penetration are likely to drive strong revenue growth going forward.

Enquiries and orders at record levels:

The company has a current order of more than 200,000 vehicles with inventories at dealers less than two weeks. The difference in strong demand and supply constraint has led to high orders. MSIL is likely to benefit from buoyant demand for PVs, driven by rising demand in Tier 2 and 3 cities and rural areas. Rural sales will continue to improve, driven by strong farm sentiments because of higher rainfall and kharif sowing. We also expect the share of first-time buyers to increase going forward, aided by a preference for personal transportation. Despite intense competition in the PV segment, MSIL is expected to sustain its dominant market share, aided by a strong product portfolio and position, brand appeal, and ability to launch new models frequently. MSIL has a stronghold in small and mid-size segments with over 50% market share and high success rates of its new launches. The company's brand position as value-for-money products is likely to remain intact due to its products' best fuel efficiency and lower maintenance cost. Moreover, the high resale value of its products attracts customers.

Exports continue to remain buoyant:

Management expects export to be a key growth driver going forward, given the improving scenario in other geographies. The company is operating at full capacity, which will keep driving profitability. The company is receiving strong response for its Jimny SUV in the export markets. The exports have more than doubled over the previous year- driven by strong sales in Africa, South Africa, Latin America, Chile and Egypt. The company benefitted from the Toyota's distribution network globally.

Earnings estimates reduced:

We have slashed our margin estimates for FY22E to build in the impact of low margins in H1FY22. However, we expect MSIL's EBITDA margin to retract to ~11.2% by FY2024, driven by increasing capacity utilisation and controlling marketing costs through digitalisation and productivity gains. We have estimated EBITDA margin to be at 11.1% in FY2023E.

Change in estimates (Rs crore)

Particulars	Revised		Earlier		% Change	
	FY22E	FY23E	FY22E	FY23E	FY22E	FY23E
Revenue	84,410	1,02,894	84,410	1,01,075	-	1.8
EBITDA	6,808	11,391	7,315	11,018	(6.9)	3.4
EBITDA margin (%)	8.1	11.1	8.7	10.9	(60 bps)	20 bps
PAT	4,866	8,308	5,245	8,028	(7.2)	3.5
EPS (Rs)	161.1	275.0	173.6	265.8	(7.2)	3.5

Source: Company Data; Sharekhan Research

Strong earnings growth:

MSIL's strong distribution network in the PV segment and rural penetration are likely to drive strong revenue growth going forward. Volumes are expected to recover from FY2022 with expectations of strong double-digit growth, aided by robust exports as well. MSIL would benefit from operating leverage, driven by robust volume growth. We expect its earnings to post a 40.1% CAGR during FY2021-FY2023E, driven by a 21% revenue CAGR and a 360-bps improvement in EBITDA margin. We expect RoCE to improve to 16.9% in FY2023E from 9.4% in FY2021.

Results (Standalone) Rs cr

Particulars	Q2FY22	Q2FY21	%YoY	Q1FY22	%QoQ
Revenues	20,538.9	18,744.5	9.6	17,770.7	15.6
Operating Expenses	19,684.0	16,810.9	17.1	16,949.6	16.1
EBIDTA	854.9	1,933.6	-55.8	821.1	4.1
Depreciation	756.1	765.9	-1.3	743.2	1.7
Interest	22.5	22.4	0.4	22.2	1.4
Other Income	522.7	602.5	-13.2	507.8	2.9
PBT	599.0	1,747.8	-65.7	563.5	6.3
Tax	123.7	376.2	-67.1	122.7	0.8
Adjusted PAT	475.3	1,371.6	-65.3	440.8	7.8
EPS	15.7	45.4	-65.3	14.6	7.9

Source: Company; Sharekhan Research

Key Ratios (standalone) Rs cr

Particulars	Q2FY22	Q2FY21	YoY (bps)	Q1FY22	QoQ (bps)
Gross margin (%)	24.2	30.2	-600	25.2	-110
EBIDTA margin (%)	4.2	10.3	-620	4.6	-50
EBIT margin (%)	0.5	6.2	-570	0.4	0
Net profit margin (%)	2.3	7.3	-500	2.5	-20
Effective tax rate (%)	20.7	21.5	-90	21.8	-110

Source: Company; Sharekhan Research

Volume Analysis (Rs per Vehicle)

Particulars	Q2FY22	Q2FY21	%YoY	Q1FY22	%QoQ
Revenue/Vehicle	5,41,151	4,76,802	13.5	5,02,545	7.7
RMC/Vehicle	4,10,417	3,33,012	23.2	3,75,848	9.2
Gross profit/Vehicle	1,30,734	1,43,790	(9.1)	1,26,697	3.2
Operating exp/Vehicle	5,18,626	4,27,617	21.3	4,79,325	8.2
EBITDA/Vehicle	22,525	49,185	(54.2)	23,220	(3.0)
PAT/Vehicle	12,523	34,889	(64.1)	12,466	0.5

Source: Company; Sharekhan Research

Outlook and Valuation

■ Sector view – Expect recovery in PV demand

The passenger vehicle segment is expected to remain strong amid COVID-19, as a preference for personal transport, pent-up demand and strong rural sentiments. Supply-side headwinds related to semi-conductor shortage are expected to slow down domestic PV sales to 17-20% in FY2022E. We expect the scenario of chips shortage to improve from H2FY2022E gradually and normalise by CY2023. Also, recovery in export destinations are expected to keep growth momentum favourable.

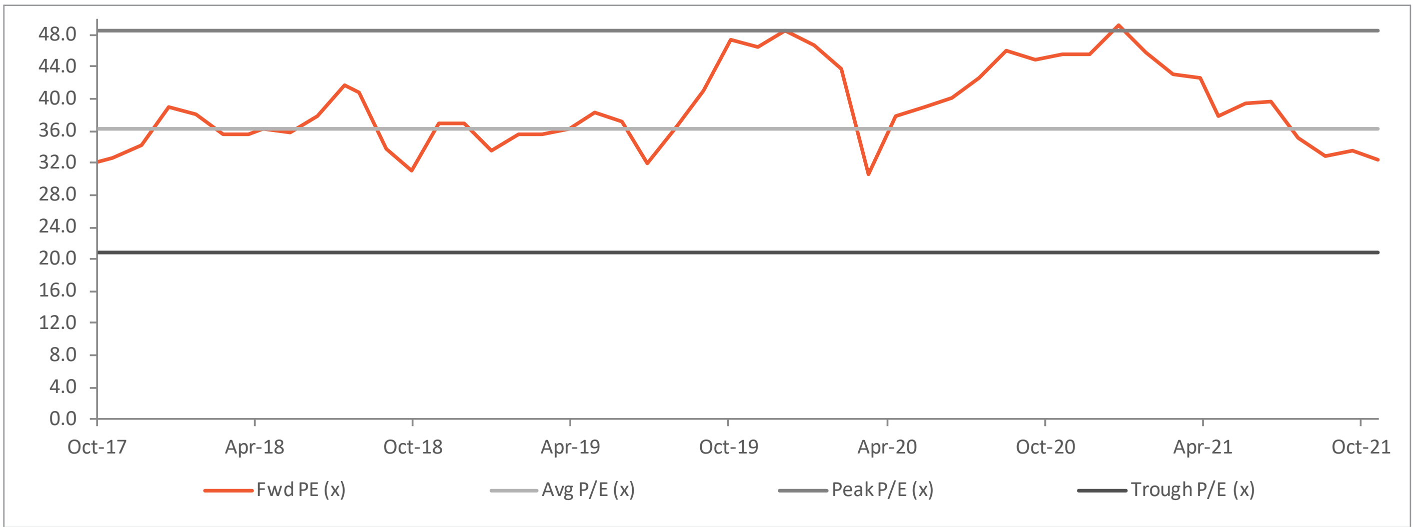
■ Company outlook – Strong earnings growth from the core business

Management was cautiously optimistic on demand outlook for domestic as well as export markets. The company has witnessed strong demand from rural and semi-urban areas, where MSIL's distribution network and product portfolio fit aptly. Improving income levels of individuals, firms, and corporates are likely to keep demand strong in the medium term. However, near-term growth would be affected by shortage of electronic components. We expect FY2022 to be a stronger year for MSIL, driven by strong volume growth. Volume growth will be aided by new product launches, a quick economic recovery, upside from COVID-19 vaccines, and a low base. MSIL's strong distribution network in the segment and rural penetration are likely to drive strong revenue growth going forward.

■ Valuation – Maintain Buy with a revised PT of Rs. 8,251

MSIL is expected to witness a recovery in domestic demand with sales volumes sustaining growth, despite the near term challenges of electronic component shortage. Sales enquiries remain strong with orderbook currently more than 2,00,000 units. We expect strong recovery from FY2022, driven by normalisation of economic activity. Margins are expected to improve from 7.5% in FY2021 to 11.1% in FY2023E, driven by operating leverage and cost-control measures. We remain positive on the company on account of its structural growth outlook (which remains intact), healthy balance sheet, and comfortable valuations. The stock is trading at P/E of 26.7x and EV/EBITDA of 19.5x its FY2023E estimates. We retain our Buy rating on MSIL with a revised PT of Rs. 8,251.

One-year forward P/E (x) band



Source: Sharekhan Research

Peer Comparison

Particulars	CMP (Rs)	P/E (x)			EV/EBITDA (x)			RoCE (%)		
	FY21E	FY21E	FY22E	FY23E	FY21	FY22E	FY23E	FY21	FY22E	FY23E
Maruti Suzuki	7,353	52.5	45.6	26.7	41.8	32.7	19.5	9.4	11.0	16.9
M&M	885	26.9	20.8	17.8	15.0	11.7	9.9	13.8	15.7	16.8
Tata Motors	498	NA	28.4	17.2	8.0	6.1	5.2	4.7	6.6	8.5

Source: Company Data; Sharekhan Research

About company

MSIL is India's largest PV car company accounting for ~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. MSIL's market share in passenger cars stands at 62%, UV at 25%, and vans at 90%. MSIL has been steadily ramping up its presence in the hinterlands, with rural sales currently contributing about 41% to overall sales. MSIL is a subsidiary of Suzuki Motor Corporation of Japan. The Japanese car major holds 56.2% stake in MSIL. The company has manufacturing plants in Gurgaon and Manesar.

Investment theme

MSIL 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 because of higher rainfall and kharif sowing. We also expect the share of first-time buyers to increase going forward, aided by preference for personal transportation. MSIL is expected to sustain its dominant market share, despite intense competition in the PV segment, aided by its strong product portfolio and position, brand appeal, and ability to launch new models frequently. MSIL 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 position as value-for-money products is likely to remain intact due to its products' best fuel efficiency and lower maintenance cost. In addition, the high resale value of its products attracts customers. Moreover, MSIL has the strongest distribution network and rural penetration in the PV segment that drives its revenue growth. We expect MSIL to be the beneficiary of rising rural demand, driven by its reach and low maintenance services costs.

Key Risks

- MSIL 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 MSIL 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, MSIL's margin may get impacted negatively.

Additional Data

Key management personnel

R C Bhargava	Chairman
Kenichi Ayukawa	Managing Director and CEO
Ajay Seth	Chief Financial Officer
Shashank Srivastava	Executive director, marketing and sales

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Suzuki Motor Corp	56.3
2	Life Insurance Corp of India	6.8
3	SBI Funds Management Pvt. Limited	1.7
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	1.2
9	GIC Pte Ltd.	1.1
10	Nomura Holdings Inc.	0.9

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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