Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Stock Update

Bosch Limited

Tepid Q2; riding tech highway to growth

Automobiles	Sharekhan code: BOSCH	Result Update

3R MATRIX	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)	✓		

\+ Positive = Neutral - Negative

Reco/View	Change
Reco: **Buy**	↔
CMP: **Rs. 11,289**	
Price Target: **Rs. 15,970**	↔

↑ Upgrade ↔ Maintain ↓ Downgrade

Company details

Market cap:	Rs. 34,887 cr
52-week high/low:	Rs.17,137/7,874
NSE volume: (No of shares)	43,578
BSE code:	500530
NSE code:	BOSCH
Free float: (No of shares)	86.9 cr

Shareholding (%)

Promoters	70.5
FII	7.5
DII	13.1
Others	8.9

Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	-10.5	-13.5	19.7	-22.4
Relative to Sensex	-15.6	-20.2	-13.5	-25.5

Sharekhan Research, Bloomberg

Summary

- Bosch's operating performance for Q2FY2021 was below estimates on account of lower margins.
- Automotive demand is improving with Bosch expected to reap benefits of increased content per vehicle. Bosch topline grew 7% yoy in Q2; with ongoing festive season, Bosch expects double-digit growth in Q3. We expect strong recovery in FY22 driven by normalization of economic activities.
- Margins are expected to improve going ahead, driven by increased localisation, transformational and restructuring projects, and benefits of operating leverage due to improved demand.
- Hence, we recommend Buy on the stock with a PT of Rs. 15,970. P/E of 20.4x FY23 earnings is lower than long term historical average of 30x.

Bosch's Q2FY2021 operating results were below estimates on account of lower margins. Revenue registered 7% growth, ahead of estimates, driven by improved demand and enhanced content per vehicle due to BS6, while margins dropped by 300 bps y-o-y to 11.6% (missed estimates). Inability to fully pass on BS6 cost increases, adverse forex movement, and higher share of traded products impacted margins. Bosch has a strong orderbook, given the festive season and expects double-digit growth in Q3FY2021. FY2022 is likely to witness strong recovery, driven by normalisation of economic activity and pent-up demand, given automotive demand would witness downturn for two consecutive years of FY2020 and FY2021. The company's order book of Rs. 18,500 crore for BS6 products is likely to be executed over the next five to six years, which provides healthy growth visibility going ahead. Increasing localisation of BS6 components, benefits from investments in transformation and restructuring projects (Bosch has invested about Rs. 1,300 crore in these projects) coupled with operating leverage (due to strong recovery in volumes) would result in margin improvement. Bosch is well prepared to tap on emerging opportunities in electrification and connected vehicles with strong technological support from its parent, Robert Bosch GmbH.

Key positives

- Revenue growth of 7% y-o-y was ahead of estimates. Bosch is witnessing increased content per vehicle on account of BS6 emission norms.
- Order book for Q3FY2021 is strong, given the festive season and further pick up in economic activities. Bosch stated it is likely to witness double-digit growth in Q3.

Key negatives

- OPM at 11.6% declined by 300 bps y-o-y and was lower than estimates. Inability to fully pass on BS6 cost increases, unfavourable foreign exchange movement and higher share of traded products impacted margins.

Our Call

Recommend Buy with a PT of Rs. 15,970: Bosch expects demand to improve further in Q3FY2021, driven by the festive season. Margins are expected to improve going ahead, driven by increased localisation, transformational and restructuring projects, and benefits of operating leverage due to improved demand. We have broadly retained our earnings estimates. Bosch is a strong technological company with robust balance sheet (zero debt) and healthy return ratios. At the CMP, the stock is trading at 20.4x its FY2023 earnings, which is lower than its long-term historical average of 30x. Hence, we recommend Buy on the stock with a PT of Rs. 15,970.

Key Risks

1) Prolonged weakness in automotive sales volumes on account of COVID-19 and weak economic sentiments; 2) Pricing pressures by original equipment manufacturer (OEM) customers can impact margins.

Valuation (Consolidated) Rs cr

Particulars	FY19	FY20	FY21E	FY22E	FY23E
Revenues	12085.0	9841.6	8355.7	11519.9	13247.9
Growth (%)	3.4	-18.6	-15.1	37.9	15.0
EBIDTA	2154.18	1483.3	977.6	1785.6	2185.9
OPM (%)	17.8	15.1	11.7	15.5	16.5
Adj. Net Profit	1593.6	1301.3	971.3	1421.8	1712.7
Growth (%)	16.2	-18.3	-25.4	46.4	20.5
EPS (Rs.)	540.4	441.3	329.4	482.1	580.8
P/E (x)	21.9	26.8	35.9	24.5	20.4
P/BV (x)	3.8	3.8	3.5	3.1	2.8
EV/EBIDTA (x)	13.8	19.4	29.9	16.1	13.1
ROE (%)	17.5	14.1	9.7	12.7	13.7
ROCE (%)	24.8	17.1	10.5	16.5	17.7
ROIC (%)	39.7	30.7	10.9	23.1	23.9

Source: Company; Sharekhan estimates

Note: We now convert Bosch into a stock update; It was earlier a 'Viewpoint' under our coverage

Operating performance misses estimates: Bosch's Q2FY2021 operating performance was lower than expectations as margins missed estimates. Revenue grew by 7% y-o-y (compared to our expectations of 5% drop). Pick up in OEM demand coupled with increased content per vehicle on account of BS6 emission norms boosted the topline. OPM declined by 300 bps y-o-y to 11.6% (compared to our estimate of 13.9%). Gross profit margin dropped by 400 bps y-o-y to 40.6% due to inability to fully pass on cost increases due to BS6 norms, adverse foreign exchange movement, and adverse mix (higher share of traded products). Bosch stated that there were certain one-off expenses related to COVID-19, which also impacted margins. EBIDTA at Rs. 288 crore declined by 14% y-o-y and was lower than our estimate of Rs. 306 crore. During the quarter, Bosch had tax credit of Rs. 27 crore, driven by deferred tax credit of Rs. 76 crore. Adjusted net profit stood at Rs. 335 crore, ahead of our estimate of Rs. 269 crore. Bosch realised exceptional charges of Rs. 400 crore towards restructuring and transformational projects.

Demand improving; Bosch to witness increased content/vehicle: The automotive industry witnessed sharp improvement in demand with production decline narrowing significantly to 5% y-o-y in Q2FY2021, as compared to steep double-digit drop in Q1FY2021. Bosch stated that with the onset of the festive season, order book is strong and the company expects double-digit growth in Q3FY2021. We expect strong recovery from FY2022, driven by normalisation in economic activity. Moreover, with the implementation of BS6 emission norms, Bosch is witnessing increased content per vehicle in the engine and exhaust gas treatment systems. In addition, the supply of fuel-injection systems to the two-wheeler (2W) segment provides additional opportunity for Bosch (Bosch was not present in engine systems for the 2W segment in earlier BS4 era). BS6 order book at Rs. 18,500 crore executable over the next five to six years provides strong visibility for Bosch.

Margins expected to improve driven by increased localisation, savings on account of transformational projects and operating leverage: Bosch is focussing on improving localisation levels for BS6 components. As the BS6 vehicle proliferation improves, Bosch would look at parts that could be manufactured in-house. Bosch stated that it would achieve a significant increase in localisation levels over the next two to three years, which would enable margin improvement. Moreover, the company has so far invested Rs. 1,300 crore on transformational and restructuring projects. These projects are directed towards optimising manpower and enhancing digitisation initiatives. Bosch expects payback period of about five years for these measures, the benefits of which would be started to witness from FY2022. Moreover, the automotive industry is expected to witness strong recovery in FY2022 after two consecutive years of downturn in FY2020 and FY2021. Improvement in volumes would lead to benefits of operating leverage, which would enable margin improvement.

Conference call highlights:

Demand outlook: Bosch stated that recovery in the automotive industry has been better than expected. The company stated that outlook for Q3FY2021 is strong, given the festive season. Bosch expects double-digit growth in Q3FY2021.

Content per vehicle increased: Bosch stated it witnessed increased content/vehicle due to BS6 norms. Bosch's revenue grew by 7% y-o-y in Q2FY2021 as against automotive production decline of 6%. Bosch witnessed double-digit growth in the 2W segment.

Localisation: Bosch stated it would continue to improve on localisation levels in BS6 components. Levels of localisation would improve over the next two to three years, which would enable margin improvement.

Restructuring and transformational expenses: Bosch has so far invested Rs. 1,300 crore over the past six quarters on restructuring the organisation and making it future ready. These investments are primarily towards optimising manpower (through early VRS). Moreover, increasing digitisation and electrification form part of these transformational programmes. Bosch stated that transformational expenses are mostly over, with marginal expenses likely in Q3FY2021. Bosch expects payback period of about five years in these programmes, the benefits of which would be visible in margin improvement starting FY2022.

Increased cash reserves: Bosch's cash and cash equivalents increased to Rs. 1,427 crore in Q2FY2021 as compared to Rs. 960 crore in Q2FY2020, driven by better working capital management.

Capex: Bosch has guided for capex of Rs. 230 crore to Rs. 250 crore for FY2021 as compared to normal capex of Rs. 400 crore.

Investment in Nivaata Systems Private Limited: Bosch is investing in Nivaata Systems Private Limited (Nivaata), which provides software solutions for the mobility business. Bosch will pick up 7% stake in the company for a consideration of Rs. 15 crore.

Aftermarket business continues to improve: Bosch stated the aftermarket business continues to pick up with opening up of the economy. Bosch is concentrating on Tier 2 level of aftermarket (end point sale) in addition to strengthening its dealer network.

Results Rs cr

Particulars	Q2FY21	Q2FY20	YoY %	Q1FY21	QoQ %
Revenue	2479.2	2312.7	7.2	991.5	150.0
EBITDA	288.3	336.9	-14.4	-102.5	-381.4
EBITDA Margin (%)	11.6	14.6	(300 bps)	-10.3	2190 bps
Depreciation	79.6	82.7	-3.8	72.8	9.3
Interest	1.3	0.6	131.6	1.8	-27.1
Other income	101.5	167.5	-39.4	173.4	-41.5
PBT	308.8	421.1	-26.7	-3.7	NA
Tax	-26.6	188.2	NA	-80.1	NA
Adjusted PAT	335.4	232.9	44.0	75.7	343.0
Exceptional charges	400.0	130.2	-	197.2	102.9
Reported PAT	-64.6	102.7	-162.9	-121.5	NA
Adjusted EPS (Rs.)	113.7	79.0		25.7	

Source: Company; Sharekhan Research

Outlook and Valuation

■ Sector view - Strong growth potential for the auto component industry

The Indian automotive component industry grew strongly at a 13% CAGR over FY2014-FY202019 with the industry reaching a size of $57 billion in FY2019. Growth is expected to further accelerate with the component industry expected to grow at a robust 20% CAGR between FY2019 and FY2027. Increasing automotive OEM production in the domestic market on account of growing working population and expanding middle class is expected to drive growth. Moreover, exports provide a huge growth potential given India's cost-effective manufacturing, being geographically closer to key markets of Middle East and Europe, and being the second largest producer of key raw-material steel. Auto component exports are expected to grow from $15 billion to $80 billion by FY2027.

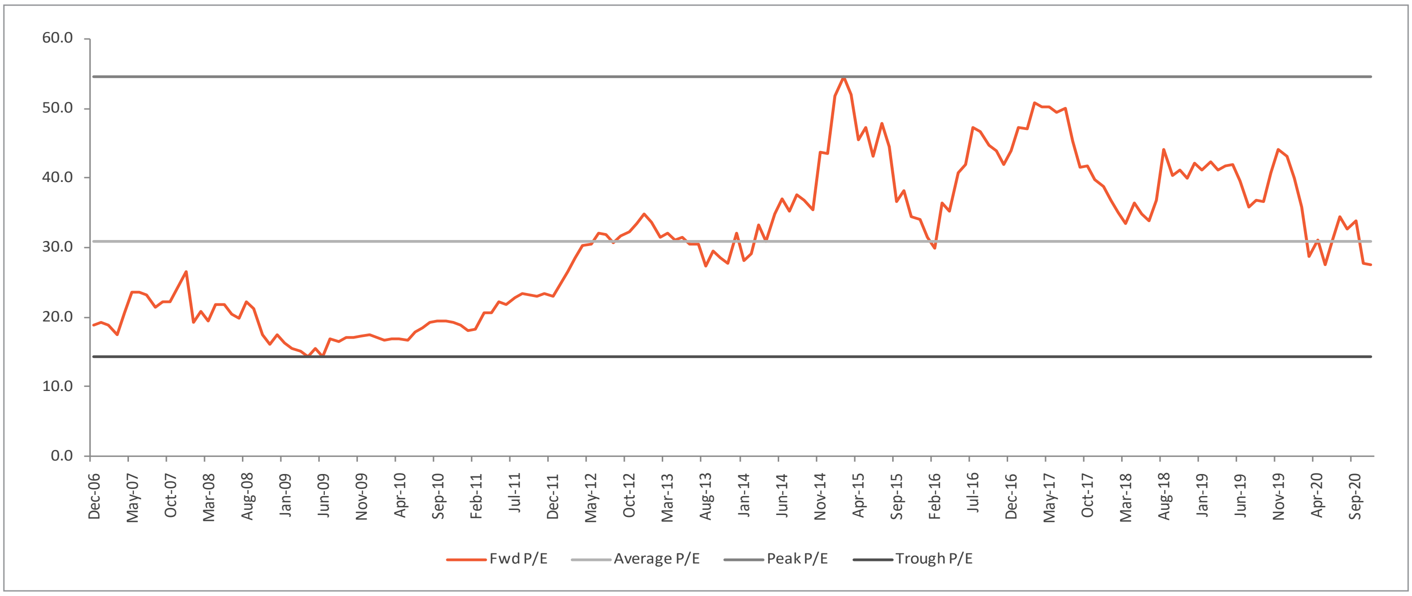
■ Company outlook - Bosch to gain from increased content per vehicle

Bosch's content per vehicle would increase with change from BS4 to BS6 emission norms, commencing supplies in the fast-growing electric vehicle segment and emerging technologies such as connected vehicles. Bosch is witnessing increased offtake in the engine and exhaust gas treatment systems as automotive OEM customers have started rolling BS6 emission norm-compliant vehicles. Moreover, supplies of fuel-injection systems to 2W players provide an incremental opportunity. Bosch has tied up with leading OEM players for supply of BS6 products and the current order book stands at Rs. 18,500 crore to be executed over a time of 5-6 years. Moreover, Bosch has commenced supplies to the electric vehicle segment with supply of the entire drive systems for Bajaj Chetak scooter, in-house hub systems for TVS Qube scooter, and components to Tata Nexon electric SUV. Bosch is readying solutions for emerging trends of connected vehicles (various cars with voice commands) and increasing digitisation in the Indian automotive industry.

■ Valuation - Recommend Buy with a PT of Rs. 15,970

Bosch expects demand to improve further in Q3FY2021, driven by the festive season. Margins are expected to improve going ahead, driven by increased localisation, transformational and restructuring projects, and benefits of operating leverage due to improved demand. We have broadly retained our earnings estimates. Bosch is a strong technological company with robust balance sheet (zero debt) and healthy return ratios. At the CMP, the stock is trading at 20.4x its FY2023 earnings, which is lower than its long-term historical average of 30x. Hence, we recommend Buy on the stock with a PT of Rs. 15,970.

One-year forward P/E (x) band



Source: Sharekhan Research

About company

The Bosch Group is a leading global supplier of technology and services. The company employs roughly 4,03,000 associates worldwide (as of December 31, 2019). According to preliminary figures, the company generated sales of Euros 77.9 billion in 2019. The group's operations are divided into four business sectors: Mobility Solutions, Industrial Technology, Consumer Goods, and Energy and Building Technology. In India, Bosch is a leading supplier of technology and services in the areas of mobility solutions, industrial technology, consumer goods, and energy and building technology. Additionally, in India, Bosch has the largest development centre outside Germany for end-to-end engineering and technology solutions. Bosch Group in India employs over 31,000 associates and generated consolidated revenue of about Rs. 21,450 crore (Euro 2.66 billion) in 2018, of which Rs. 15,824 crore (Euro 1.96 billion) is from third party. In India, Bosch has close to 18,000 research and development associates. In India, Bosch Limited is the flagship company of Bosch Group. The company earned revenue of over Rs. 12,460 crore (Euro 1.54 billion) in 2018. In India, Bosch setup its manufacturing operations in 1951, which has grown over the years to include 18 manufacturing sites and seven development and application centres.

Investment theme

Bosch has stated that automotive demand is expected to continue to improve. The company has a strong order book, given the festive season and expects double-digit growth in Q3FY2021. FY2022 is likely to witness strong recovery, driven by normalisation of economic activity and pent-up demand given that automotive demand would witness downturn for two consecutive years of FY2020 and FY2021. Bosch's order book of Rs. 18,500 crore for BS6 products to be executed over the next five to six years provides healthy growth visibility going ahead. Increasing localisation of BS6 components, benefits from investments in transformation and restructuring projects (Bosch has invested about Rs. 1,300 crore in these projects) coupled with operating leverage (due to strong recovery in volumes) would result in margin improvement. Bosch is well prepared to tap on emerging opportunities in electrification and connected vehicles with strong technological support from parent Robert Bosch GmbH.

Key Risks

- Prolonged weakness in automotive volumes on account of COVID-19 and weak economic sentiments.
- Inability to fully pass on cost increases may impact margins.

Additional Data

Key management personnel

VK Vishwanathan	Chairman
Soumitra Bhattacharya	Managing Director
Andreas Wolf	Joint Managing Director
Jan-Oliver Rohrl	Chief Technical Officer and Executive Director

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Robert Bosch GmbH	67.8
2	General Insurance Corporation of India	3.27
3	Life Insurance Corporation	2.87
4	Robert Bosch Engineering and Business Solution	2.78
5	New India Assurance company Limited	2.71
6	United India Insurance company	1.15
7	Blackrock Inc.	0.72
8	Aditya Birla Sun Life AMC	0.69
9	Vanguard Group Inc.	0.62
10	Standard Life Aberdeen PLC	0.44

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

Sharekhan

by BNP PARIBAS

Know more about our products and services

For Private Circulation only

Disclaimer: This document has been prepared by Sharekhan Ltd. (SHAREKHAN) and is intended for use only by the person or entity to which it is addressed to. This Document may contain confidential and/or privileged material and is not for any type of circulation and any review, retransmission, or any other use is strictly prohibited. This Document is subject to changes without prior notice. This document does not constitute an offer to sell or solicitation for the purchase or sale of any financial instrument or as an official confirmation of any transaction. Though disseminated to all customers who are due to receive the same, not all customers may receive this report at the same time. SHAREKHAN will not treat recipients as customers by virtue of their receiving this report.

The information contained herein is obtained from publicly available data or other sources believed to be reliable and SHAREKHAN has not independently verified the accuracy and completeness of the said data and hence it should not be relied upon as such. While we would endeavour to update the information herein on reasonable basis, SHAREKHAN, its subsidiaries and associated companies, their directors and employees ("SHAREKHAN and affiliates") are under no obligation to update or keep the information current. Also, there may be regulatory, compliance, or other reasons that may prevent SHAREKHAN and affiliates from doing so. This document is prepared for assistance only and is not intended to be and must not alone be taken as the basis for an investment decision. Recipients of this report should also be aware that past performance is not necessarily a guide to future performance and value of investments can go down as well. The user assumes the entire risk of any use made of this information. Each recipient of this document should make such investigations as it deems necessary to arrive at an independent evaluation of an investment in the securities of companies referred to in this document (including the merits and risks involved), and should consult its own advisors to determine the merits and risks of such an investment. The investment discussed or views expressed may not be suitable for all investors. We do not undertake to advise you as to any change of our views. Affiliates of Sharekhan may have issued other reports that are inconsistent with and reach different conclusions from the information presented in this report.

This report is not directed or intended for distribution to, or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject SHAREKHAN and affiliates to any registration or licensing requirement within such jurisdiction. The securities described herein may or may not be eligible for sale in all jurisdictions or to certain category of investors. Persons in whose possession this document may come are required to inform themselves of and to observe such restriction.

The analyst certifies that the analyst has not dealt or traded directly or indirectly in securities of the company and that all of the views expressed in this document accurately reflect his or her personal views about the subject company or companies and its or their securities and do not necessarily reflect those of SHAREKHAN. The analyst further certifies that neither he or its associates or his relatives has any direct or indirect financial interest nor have actual or beneficial ownership of 1% or more in the securities of the company at the end of the month immediately preceding the date of publication of the research report nor have any material conflict of interest nor has served as officer, director or employee or engaged in market making activity of the company. Further, the analyst has also not been a part of the team which has managed or co-managed the public offerings of the company and no part of the analyst's compensation was, is or will be, directly or indirectly related to specific recommendations or views expressed in this document. Sharekhan Limited or its associates or analysts have not received any compensation for investment banking, merchant banking, brokerage services or any compensation or other benefits from the subject company or from third party in the past twelve months in connection with the research report.

Either SHAREKHAN or its affiliates or its directors or employees / representatives / clients or their relatives may have position(s), make market, act as principal or engage in transactions of purchase or sell of securities, from time to time or may be materially interested in any of the securities or related securities referred to in this report and they may have used the information set forth herein before publication. SHAREKHAN may from time to time solicit from, or perform investment banking, or other services for, any company mentioned herein. Without limiting any of the foregoing, in no event shall SHAREKHAN, any of its affiliates or any third party involved in, or related to, computing or compiling the information have any liability for any damages of any kind.

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

---

Registered Office: Sharekhan Limited, 10th Floor, Beta Building, Lodha iThink Techno Campus, Off. JVLR, Opp. Kanjurmarg Railway Station, Kanjurmarg (East), Mumbai – 400042, Maharashtra. Tel: 022 - 61150000. Sharekhan Ltd.: SEBI Regn. Nos.: BSE / NSE / MSEI (CASH / F&O / CD) / MCX - Commodity: INZ000171337; DP: NSDL/CDSL-IN-DP-365-2018; PMS: INP000005786; Mutual Fund: ARN 20669; Research Analyst: INH000006183;