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Tata Motors Ltd

Driving ahead despite chip challenges

Automobiles	Sharekhan code: TATAMOTORS	Company Update

Summary

- We expect all-round improvement in Tata Motors' business and expect earnings to turn positive in FY2022 and rise by 69.1% in FY2023E, driven by a 16.7% CAGR in revenue during FY2021-FY2023E and a 130 bps improvement in EBITDA margin.
- Management stated that shortage of semiconductor chips would be a near-term concern, but remained positive on product delivery, new launches and capex programs as planned earlier.
- Stock trades at an attractive P/E multiple of 9.6x and EV/EBITDA multiple of 2.9x its FY2023E estimates.
- We maintain a Buy on Tata Motors with an unchanged PT of Rs. 430, factoring improvement in operational performance across businesses and robust FCF generation, led by turnaround in domestic business and a positive outlook for JLR business.

The management of Jaguar Land Rover Automotive Plc (JLR), a subsidiary of Tata Motors (TAMO), raised concerns over a shortage of semiconductor chips in near term that would hit wholesales by 28-30% in H1FY22 due to the resultant supply constraints. Thus, the company expects Q1FY22 and Q2FY22 to report a cash outflow of ~GBP 1 billion with a negative EBIT margin for both quarters. However, the management indicated that shortage of semiconductor chips is likely to improve gradually from H2FY22 onwards, as global capacity of semiconductor chips is expected to increase. Retail sales and orders remain robust, which is likely to keep wholesales strong, as the issue of semiconductor chip shortage is set to improve from Q3FY22 onwards. The management stays positive on product delivery, launches and capex programs as planned earlier. With respect to the global chip shortage, chip-making facilities in Japan and Texas will take time to resume. It is expected that the situation to completely normalize in 12-18 months after which wholesale output would match current retail demand.Production is expected to be higher in H2FY22 versus H1FY21. We continue to remain positive on JLR's operational performance and expects chips shortage to be temporary phenomena. We have cut TAMO's FY22E consolidated earnings estimates by 22% to build the impact of chips shortage but maintained our FY23E estimates, as we believe JLR's volumes will recover with the easing of chipsupply situations. JLR continues to maintain its timelines for launches. Jaguar is expected to be totally electrified by 2025 and the company should launch its first battery electric vehicle (BEV) in 2025. Jaguar is expected to be phase out of pure Internal Combustion Engine (ICE) variants by FY26, with total BEV mix rising over 60% by FY30. In respect of Land Rover, the company plans to introduce six battery-operated vehicle (BEV) variants in the next five years through the family of three models - Defender, Discovery and Range Rover. With the electrification to be the next motivation for the company over the next decade, JLR targets net zero carbon emissions by 2039.The management has maintained its positive guidance for its JLR business, expecting positive cashflow by FY23, net debt to be zero by FY24and EBIT margins greater than 10% by FY26. In respect of TAMO's domestic business, we believe its growth drivers remains intact with the turnaround of passenger vehicle (PV) business and beneficiary of the domestic CV upcycle. The outlook for domestic commercial vehicle (CV) business is positive, with notable demand arising from infrastructure, mining, and e-commerce activities, as the economy normalises. Driven by all-round strong performance, we expect TAMO's earnings to become positive in FY2022E and 69.1% in FY2023E, driven by a 16.7% revenue CAGR during FY2021-FY2023E and a 130 bps rise in EBITDA margin. We reiterate our Buy rating on the stock.

Our Call

Valuation - Maintain Buy with an unchanged PT of Rs.430: TAMO is witnessing improvement in all its business verticals - JLR, CV, and PV businesses. We expect TAMO to benefit from improving macro-environment in India and globally. The company is generating strong FCF, which will help it pursue its business plans and reduce high debts. We expect TAMO's earnings to become positive in FY2022E and 69.1% in FY2023E, driven by a 16.7% revenue CAGR during FY2021-FY2023E and a 130 bps improvement in EBITDA margin. Our SOTP-based valuation provides a PT of Rs. 430 for TAMO. The stock trades at an attractive valuations at P/E multiple of 9.6x and EV/EBITDA multiple of 2.9x its FY2023E estimates. We maintaina Buy on the stock with an unchanged PT of Rs 430.

Key Risks

TAMO's business is dependent upon cyclical industries – commercial vehicles and passenger vehicles.Moreover, the company's business is present across the globe. Any slowdown or cyclical downturn in any of the locations, where the company has a strong presence, can impact its business and profitability.

Valuation (Consolidated) Rs cr

Particulars	FY20	FY21	FY22E	FY23E
Net Sales	2,61,068	2,49,795	3,18,464	3,40,024
Growth (%)	-13.5	-4.3	27.5	6.8
EBIDTA	19,726	30,555	39,145	46,053
OPM (%)	7.6	12.2	12.3	13.5
PAT	(10,156)	(1,366)	7,480	12,649
Growth (%)	NA	NA	NA	69.1
FD EPS (Rs)	-26.5	-3.6	19.5	33.0
P/E (x)	NA	NA	16.2	9.6
P/B (x)	2.4	1.9	1.7	1.5
EV/EBIDTA (x)	11.2	4.5	3.4	2.9
RoE (%)	-20.3	-7.5	7.5	16.9
RoCE (%)	-0.2	2.8	4.5	8.8

Source: Company; Sharekhan estimates

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. 317**	
Price Target: **Rs. 430**	↔

↑ Upgrade ↔ Maintain ↓ Downgrade

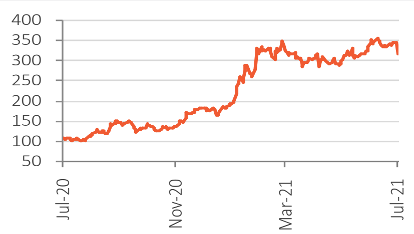
Company details

Market cap:	Rs. 1,05,254 cr
52-week high/low:	Rs. 361 / 101
NSE volume: (No of shares)	776.3 lakh
BSE code:	500570
NSE code:	TATAMOTORS
Free float: (No of shares)	285.6 cr

Shareholding (%)

Promoters	46.4
FII	13.8
DII	12.1
Others	27.8

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-8.2	3.9	70.2	190.9
Relative to Sensex	-9.6	-4.0	58.1	145.5

Sharekhan Research, Bloomberg

Management conference call highlights -

The company hosted a conference call to discuss the shortage of chips supply globally and its impact on the company production and sales. The key highlights of the conference call are as below:

Semiconductor chip shortage to remain near-term risk: The management of Jaguar Land Rover Automotive Plc (JLR), a subsidiary of Tata Motors (TAMO), raised concerns over a shortage of semiconductor chips in near term that would hit wholesales by 28-30% in H1FY22 due to the resultant supply constraints. Thus, the company expects Q1FY22 and Q2FY22 to report a cash outflow of ~GBP 1 billion with a negative EBIT margin for both quarters. However, the management indicated that shortage of semiconductor chips is likely to improve gradually from H2FY22 onwards, as global capacity of chips is expected to increase. Retail sales and orders remain robust, which is likely to keep wholesales strong, as the issue of chip shortage is set to improve from Q3FY22 onwards. The management stays positive on product delivery, launches and capex programs as planned earlier. With respect to the global chip shortage, chip-making facilities in Japan and Texas will take time to resume. It is expected that the situation to completely normalize in 12-18 months after which wholesale output would match current retail demand. Production is expected to be higher in H2FY22 versus H1FY21.The company was not aware of the crisis at the time of the Q4FY21 investor call and was following the production schedule provided by suppliers.

Retail sales and wholesales in Q1FY22:JLR has released retail and wholesale numbers for Q1FY22. The retail sales for Q1FY22 were 124,537 vehicles, 68.1% higher than the 74,067 vehicles sold in Q1FY20. Regional retail sales rose with UK (+186.9%), Europe (+124.0%), Overseas (+71.0%), North America (+50.5%) and China (up 14.0%). The wholesales were at 84,442 units in the quarter (excluding the China JV), up 72.6% y-o-y, which is lower than by 30,000 units than estimated due to semiconductor supply constraints and the impacts of Covid-19. The retail orders remain strong at 1,10,000 units, representing threemonths of sales cover with 5 months in Europe and 4 months in the UK. The order-book does not include China and US demand.Orders for the Defender alone total over 29,000, representing a cover of over four months. We expect the company wholesales to improve as the semi-conductor issues improves going forward. The Total inventory (factory, transit and dealer) levels stands at ~74,000 units at end of June. Inventory and Q2FY22 production (~60,000 units) should cater to retail demand for most products in Q2FY22.

Impact of chip shortage in H1FY22: Based on unaudited results for Q1FY22, the company expects to report a cash outflow of ~GBP1 billion with a negative EBIT margin for the Q1FY22 and Q2FY22. Total liquidity at the end of the first quarter was over GBP 5.6 billion including a GBP 1.9 billion undrawn committed credit facility (RCF). As per the company's vendors, the semi-conductor shortage may further increase in Q2FY22 and impact wholesales by ~50% at 60,000-65,000 units than earlier planned. However, the company expects semiconductor chip shortage to improve gradually from H2FY22 onwards, though have a put a word of caution. JLR expects the broader underlying structural capacity issues will only be resolved as supplier investment in new capacities come online over the next 12-18 months.As a result, the company expects shortages to continue through the end of year. As per the management, JLR will continue to prioritise production of higher margin vehicles for the chip supply available as well as make chip and product specification changes where possible to reduce the impact.

Focus on new launches and product delivery remain unaffected: New launches are not likely to be delayed. The launch of the new Range Rover Sportlaunch is expected in next 9 months, as per the schedule. The management expects no delay or deferment of capex plans due to chips shortage.

Focus on electrification continues with no change in plan: JLR's management has laid down its plans and strategies for electrification of its iconic brands, Jaguar and Land Rover over the next decade.The Jaguarmodel is expected to be totally electrified by 2025 and the company should launch its first battery electric vehicle (BEV) in 2025 on a new dedicated architecture. Jaguar is expected to be phase out of pure Internal Combustion Engine (ICE) variants by FY26, with the total BEV mix rising over 60% by FY30. In respect of Land Rover, the company plans to introduce six BEV variants in the next five years through a family of three models – the Defender, Discovery and Range Rover. With the electrification to be the next motivation for the company over the next decade, JLR targets net zero carbon emission by 2039.

Maintain guidance: The management has maintained its positive guidance for the JLR business, expecting positive cashflow by FY23, net debt to be zero by FY24, and EBIT margins greater than 10% by FY26. The company maintains its capex guidance of GBP 2.5 billion per annum from FY22 onwards, using which it expects to manage to shift from ICE to BEV models efficiently by deploying the GBP 2.5bn capex annually. The company expect double-digit EBIT margin by FY26 to be driven by refocus and reimagine architecture strategy. JLR has underlying EBIT margin of 4% in Q3FY21 and expects 300 bps improvement from refocus strategy and a more than 300 bps improvement from new architectures. The company has also improved its break-even point from 600k units in FY19 to 400,000-450,000 units in FY21 and expects to maintain the break-even point around this range.

JLR maintains its guidance on Capex, profitability and debt profile

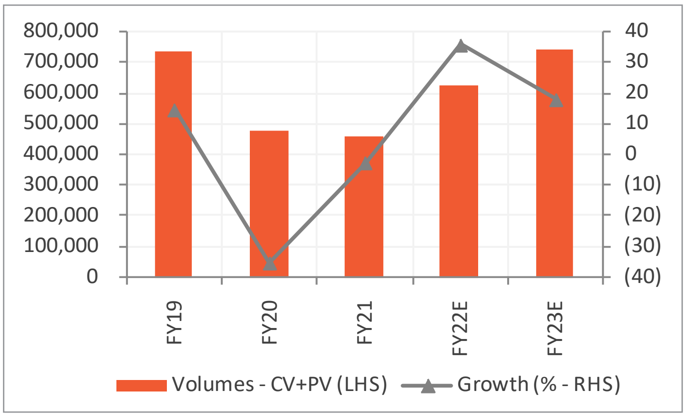
Key metrics	FY21	FY22	FY24	FY26
Revenue	Not guided	Increasing	Increasing	> £30b
EBIT margin *Positive PBT* throughout*	Positive	≥4%	≥7%	≥10%
Investment	< £2.5b	c. £2.5b	c. £2.5b	c. £3b
Free cash flow	Near break-even	Break-even After ~£500m restructuring costs	Positive	Positive
Net cash / (Net debt)	Negative	Negative	0	Positive

*Excluding exceptionals

Source: Company, Sharekhan Research

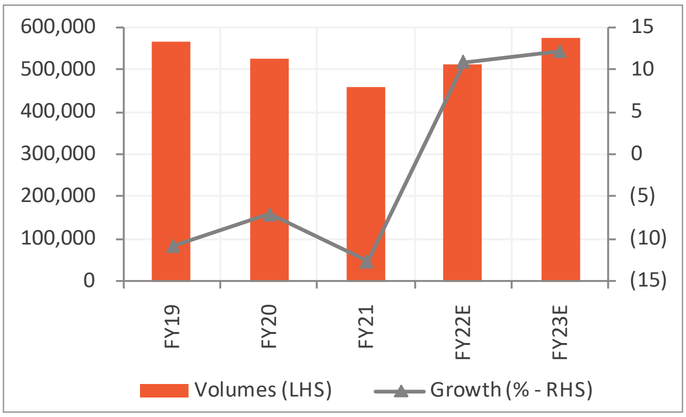
Financials in charts

Volumes Trends (Standalone business)



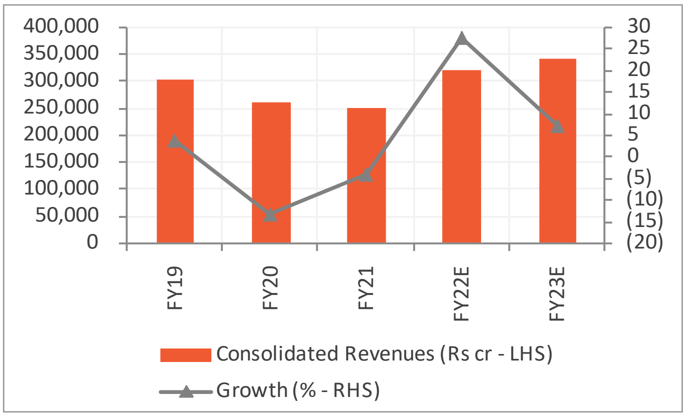
Source: Company, Sharekhan Research

Volumes Trends (JLR, including China JV)



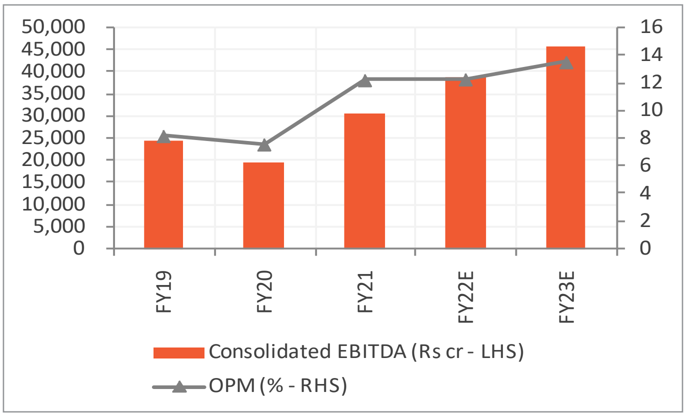
Source: Company, Sharekhan Research

Revenue and Growth Trend



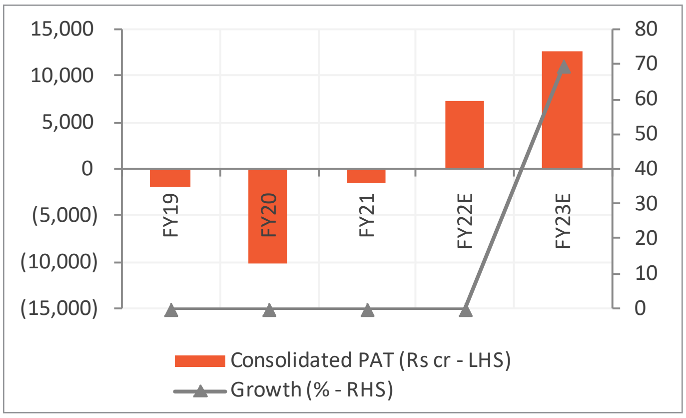
Source: Company, Sharekhan Research

EBITDA and OPM Trend



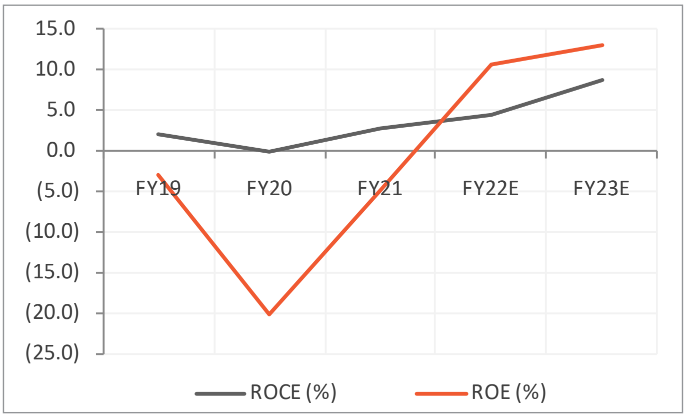
Source: Company, Sharekhan Research

PAT and Growth Trend



Source: Company, Sharekhan Research

ROE and ROCE Trend



Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector view - Positive outlook on the automobile industry in India and globally

The macro-environment is improving in Europe, UK, America, and China. The roll-out of COVID-19 vaccination programmes in many countries is keeping the overall outlook positive over the coming months following the respective approval of various vaccines. Moreover, the Brexit trade deal between UK and European Union has resolved the risk of tariffs on automotive parts and finished vehicles. The medium-term outlook of domestic CV business is strong, with notable demand arising from infrastructure, mining, and e-commerce activities. Volumes of domestic PV recovered strongly, driven by rural and semi-urban demand. However, the nearterm remains challenging due to lockdowns and restrictions posed Government. We expect strong recovery in demand after the normalisation of wave-2 of COVID -19 and speedy roll out of vaccination program in India.

■ Company outlook - Strong outlook

TAMO clocked resilient operational performance in H2FY2021, seeing robust FCF in JLR and standalone businesses, reducing debt amply. Earnings visibility also improved. Results witnessed a strong turnaround in the operational performance on all its three key automotive businesses, JLR, PV business, and CV business. The company has generated positive FCF of GBP 729 million from the JLR business and Rs. 2,900 crore from domestic business in Q4FY21. We expect the company's operational performance to continue to improve, with recovery in all verticals of automotive businesses. The outlook for the JLR business is positive, as the macro-environment improvesin Europe, the UK, US and China. Outlook of domestic CV business is at a cusp of strong recovery post normalisation of Wave-2 of COVID-19, with notable demand arising from infrastructure, mining, and e-commerce activities. TAMO's PV business has transformed significantly because of strong sales momentum with the 'New Forever' portfolio. During FY2021, the company gained 340 bps y-o-y -market share at 8.2% in the PV segment.

■ Valuation - Maintain Buy with an unchangedPT of Rs. 430

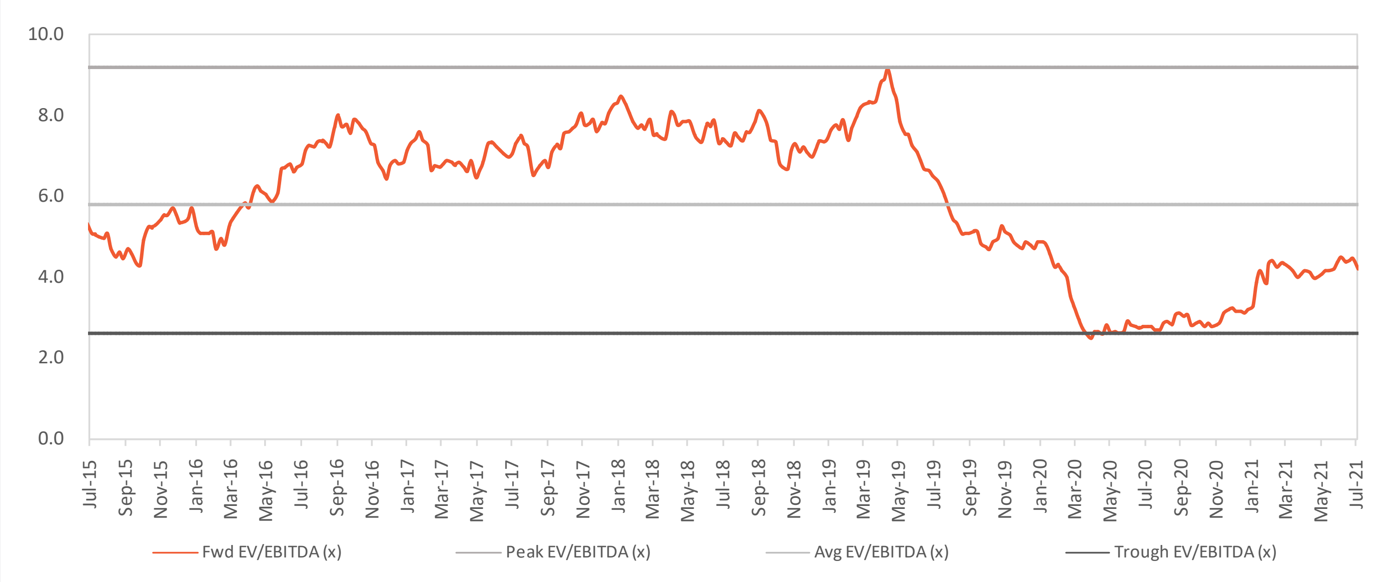
TAMO is witnessing improvement in all its business verticals - JLR, CV, and PV businesses. We expect TAMO to benefit from improving macro-environment in India and globally. The company is generating strong FCF, which will help it pursue its business plans and reduce high debts. We expect TAMO's earnings to become positive in FY2022E and 69.1% in FY2023E, driven by a 16.7% revenue CAGR during FY2021-FY2023E and a 130 bps improvement in EBITDA margin. Our SOTP-based valuation provides a PT of Rs. 430 for TAMO. The stock trades at an attractive valuations at P/E multiple of 9.6x and EV/EBITDA multiple of 2.9x its FY2023E estimates. We maintain a Buy on the stock with an unchanged PT of Rs 430.

SOTP-based PT of Rs. 430

Particulars	Rationale	Value (Rs. crore)	Value per Share (Rs.)
Standalone business	6x EV/EBITDA	47,056	123
JLR UK	4x EV/EBITDA	1,24,230	394
JLR China	5x EV/EBITDA	10,069	26
Total EV		**1,81,355**	**543**
Net Debt		46,654	122
Automotive Business Value		**1,61,322**	**421**
Value of Subsidiaries			**9**
TAMO's Equity Value			**430**
Upside (%)			**36**

Source: Company Data; Sharekhan Research

One-year forward EV/EBITDA (x) band



Source: Company Data; Sharekhan Research

Peer Comparison

Particulars	CMP (Rs)	P/E (x)			EV/EBITDA (x)			ROCE (%)		
		FY21	FY22E	FY23E	FY21	FY22E	FY23E	FY21	FY22E	FY23E
Tata Motors	317	NA	16.2	9.6	4.5	3.4	2.9	2.8	4.5	8.8
Mahindra & Mahindra Limited	777	24.0	17.9	15.3	13.4	10.0	8.4	13.6	16.0	17.1
Ashok Leyland Limited	124	NA	42.0	17.6	69.9	18.0	9.8	-	10.4	21.8
Maruti Suzuki India Limited	7451	53.2	33.4	26.0	42.4	23.9	18.7	9.4	14.9	17.2

Source: Company Data; Sharekhan Research

About company

TAMO manufactures cars and commercial automotive vehicles. The company designs, manufactures, and sells heavy, medium, and small CVs, including trucks, tankers, vans, buses, ambulances, and minibuses. TAMO also manufactures small cars and sports utility vehicles (SUVs). The company is a leading CV manufacturer in India. TAMO acquired Jaguar and Land Rover brands in 2008; and Jaguar and Land Rover brands merged to form one unified company in 2013.

Investment theme

We are positive on TAMO, considering its resilient operational performance lately, robust FCF for JLR, and standalone businesses led by the company's all-round strong performance, falling debt, and better earnings visibility.Q3FY2021 results saw a strong turnaround in operational performance in all three key automotive businesses - JLR, PV, and CV. We expect the company's operational performance to continue in the medium term, with recovery in all verticals of automotive businesses. Outlook for JLR business is positive, aided by macro-environment improving in Europe, UK, America, and China. Outlook of the domestic CV business is at the cusp of a sharp cyclical rebound, with notable demand arising from infrastructure, mining, and e-commerce activities. TAMO's PV business has transformed significantly because of strong sales momentum with the 'New Forever' portfolio. TAMO's management is committed towards reaching zero debt for its automotive business division. Robust result turnaround in key businesses during Q3FY2021 has a strong reason to believe that the company is on the right track towards achieving zero debt level. We expect all-round improvement in the company's business and,hence,recommend Buy on the stock.

Key Risks

TAMO's business is dependent upon cyclical industries – CV and PV. Moreover, the company's business is presentacross the globe. Any slowdown or cyclical downturn in any of the locations, where it has a strong presence, can impact its business and profitability.

Additional Data

Key management personnel

Girish Wagh	Executive Director
Thierry Bolloré	CEO, Jaguar & Land Rover
P B Balaji	Group Chief Financial Officer
Shailesh Chandra	President - Passenger Vehicles Business Unit

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Tata Sons Private Limited	43.7
2	Tata Industries Limited	2.2
3	Tata Investment Corporation Limited	0.3
4	Citibank N.A. New York Nyadr Department	10.7
5	Life Insurance Corporation Of India	4.8
6	Jhunjhunwala Rakesh Radheshyam	1.2
7	SBI Arbitrage Opportunities Fund	1.0
8	Alternate Investment Funds	0.1
9	Ewart Investments Limited	0.1
10	Tata Chemicals Ltd	0.1

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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