

August 23, 2013

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Reuters Code: BAJA.NS

Bloomberg Code: BJAUT

Bajaj Auto Ltd (BAJAJAUTO) is the world's largest three-wheeler (3W) manufacturer having domestic market share of 31.4% (FY13). Set up in 1930, the company is the largest 3W, the largest premium motorcycle, and the second largest two-wheeler (2W) maker in the Indian passenger vehicle market. BAJAJAUTO is the largest exporter of 2W and 3W in the country with exports forming 18% of its total sales. The company has two subsidiaries, namely Bajaj Auto International Holdings BV and PT Bajaj Indonesia. The company operates in two segments namely, Automotive and Investments.

Investor's Rationale

Despite the slowdown in the local auto industry, BAJAJAUTO has posted a growth of 2% YoY and 3.4% QoQ to ₹48.1 bn (in line consensus of ₹48.3 bn) during Q1FY14. The firm's performance has shown that it has met the street forecast on all parameters, on the back of better realization in export due to weaker rupee, offsetting sluggish sales volumes. Net profit that grew 2.7% YoY to ₹7.3 bn, could have been much better but impacted by the forex loss of ₹0.9 bn. With a strategy to focus on international markets, BAJAJAUTO has reported higher realization with exports earnings growing from ₹17.10 bn in Q1FY13 to ₹18.76 bn in Q1FY14. We believe that good monsoon, and festive season around the corner will help to boost the sales.

BAJAJAUTO during the last fiscal has sold 25,000 units (including exports of 18,000 units) of KTM motorcycles. Further for FY14, it believes to deliver 35,000 (including 25,000 units of exports).

On the operating front, the EBITDA margin remained stable in FY13. Bajaj Auto was able to maintain its EBITDA that grew by 19.6% (highest in the auto industry) of net sales and stood at ₹39.90 bn in FY13. Looking ahead, we expect that the firm will be able to upgrade its margin further to 19.8% by FY14 aided by offering differentiated products in the front-end and focus on cost and productivity improvements at the back-end.

BAJAJAUTO performed better than the industry in FY13. The Company's domestic sales grew by 11.4% to 226,131 units. This growth was largely driven by growth in Diesel segment where the company witnessed a growth of 25% as against the industry growth of 9%. Consequently, the market share stabilizes at 31.4% in FY13 and is likely to rise 1-2% going ahead.

Key Risk:

Sluggish export: The Company has clocked a lower export in FY13 at 1.55 mn units from 1.58 mn in FY12 led by its key market Sri Lanka, which substantially raised import tariffs on motorcycles and 3W. Such disturbance is likely to hurt the overall result of the company.

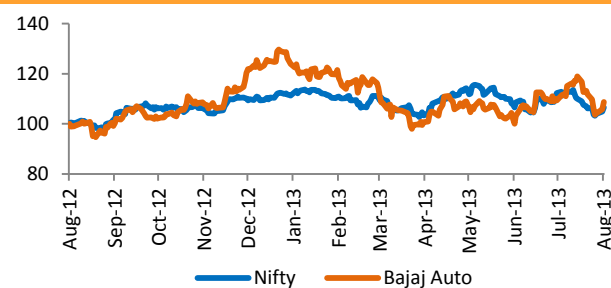
Market Data

Rating	BUY
CMP (₹)	1,780
Target (₹)	2,000.0
Potential Upside	~12.0%
Duration	Long Term
Face Value (₹)	10
52 week H/L (₹)	2,229/1,605
Decline from 52WH (%)	(20.1)
Rise from 52WL (%)	11.4
Beta	0.9
Mkt. Cap (₹ bn)	515.2
Enterprise Value (₹ bn)	511.4

Fiscal Year Ended

Y/E	FY12A	FY13A	FY14E	FY15E
Revenue (₹ bn)	19.6	20.0	21.5	24.0
EBITDA (₹ bn)	37.1	36.4	42.6	50.3
Net Profit (₹ bn)	30.5	31.3	36.0	41.9
Adj EPS (₹)	105.2	108.3	124.3	144.8
P/E (x)	16.9	16.4	14.3	12.3
P/BV (x)	8.5	6.4	5.6	4.9
EV/EBITDA (x)	13.5	14.0	12.0	10.1
ROCE (%)	64.2	50.3	51.1	52.1
ROE (%)	50.1	38.8	39.2	39.8

One year Price Chart



Shareholding Pattern

Shareholding Pattern	Jun'13	Mar'13	Diff.
Promoters	50.0	50.0	-
FII	17.4	18.2	(0.8)
DII	7.7	7.3	0.4
Others	24.7	24.3	0.4

BAJAJAUTO is the largest exporter of 2W and 3W in the country with exports forming 18% of its total sales.

The company has 3 plants namely Waluj, Chakan and Pantnagar with total production capacity of 5,400,000 units in FY13.

BAJAJAUTO: the world's largest 3W manufacturer

Bajaj Auto Ltd (BAJAJAUTO) is the dominant player in the premium motorcycle segment which is the leader in the economy. Set up in 1930, the company is the largest three-wheeler (3W), the largest premium motorcycle, and the second largest two-wheeler (2W) maker in the Indian passenger vehicle market. BAJAJAUTO is the largest exporter of 2W and 3W in the country with exports forming 18% of its total sales.

The Company operates three plants, two at Waluj and Chakan in Maharashtra and one at Pant Nagar in Uttranchal, western India. From these plants it offers its 2W products under the Avenger, Pulsar, Discover, Platina, and Ninja brands. It also provides commercial goods and passenger carriers. The Bajaj brand is well-known across several countries in Latin America, Africa, Middle East, South and South East Asia. The Company is a market leader in motorcycles in overseas market as well like Colombia, Central America, Sri Lanka, Bangladesh, Philippines etc.

The Company's current installed capacity is 6.36 million units per annum. For FY13, total income from operations grew by 2.28% YoY to ₹2.0 bn. BAJAJAUTO'S operations at its Waluj, Chakan and Pantnagar plants have continued to achieve superior results in productivity, product quality, cost reduction and company culture improvement. The use of optimised resources and improved efficiencies at all levels has helped the Company to continue achieving industry-leading EBITDA margins inspite significant pricing pressures in the markets.

Plant-wise Capacities and Product Range

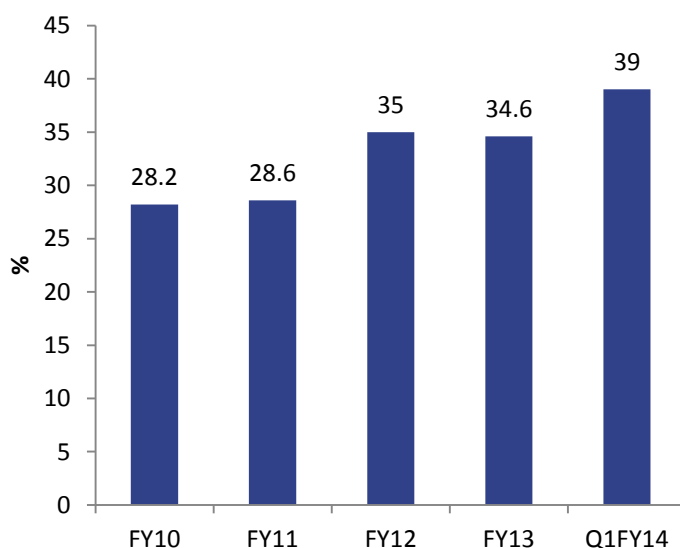
Plant	FY12	FY13	Product Range
	As on 31 March 2012	As on 31 March 2013	
Waluj	Motorcycles : 1,500,000 Three Wheelers : 600,000	Motorcycles : 1,800,000 Three Wheelers : 600,000	Boxer, Platina, Discover, Pulsar and 3W
Waluj Subtotal	2,100,000	2,400,000	
Chakan	1,200,000	1,200,000	Pulsar, Avenger, Ninja and KTM
Pantnagar	1,800,000	1,800,000	Platina, Discover, Boxer
Grand Total	5,100,000	5,400,000	

BAJAJAUTO is tapping new growth markets, with an aim to expand more by reducing prices.

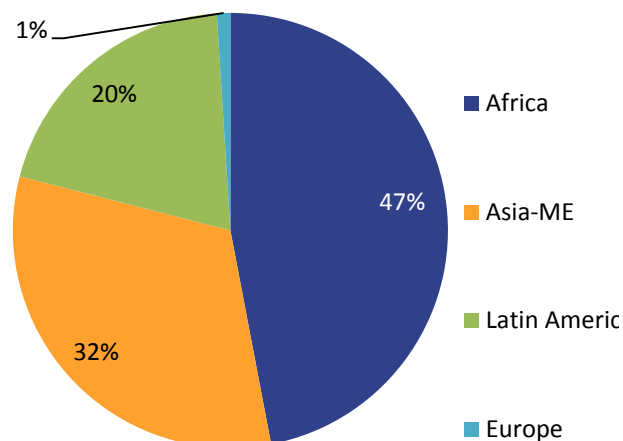
Extending position globally to strengthen presence

BAJAJAUTO is geographically diversified with strong presence in Africa, SE Asia and Middle East. BAJAJAUTO's strategy to focus on international markets has delivered improved results, with exports earnings growing from ₹17.1 bn in Q1FY13 to ₹18.76 bn in Q1FY14. The company is tapping new growth markets, like Ivory Coast, Uganda and Tanzania in Africa, with an aim to expand more by reducing prices. We believe that the firm's rising export and premium motorcycle business should enhance revenue growth in the following years to come. The company is enjoying a healthy geographical spread including Africa, Asia and Middle East, Europe, Latin America and accounted for ~35% of Net Sales and 47% of the total exports. Africa accounts for the largest share by volume for both motorcycles and 3W, followed by Asia and Middle East at 32%.

BAJAJAUTO's Export Performance (% to Net Sales)



Geographical spread of Export



With a strategy to focus on international markets, Bajaj Auto has reported higher realization with exports earnings growing from ₹17.10 bn in Q1FY13 to ₹18.76 bn in Q1FY14. With growth being led largely by Africa, the company expects ~5% growth in exports in volume terms in FY14E. We expect that hedging future earnings from exports will continue to ensure the company's ability to leverage the rupee depreciation with respect to its earnings from abroad. The company also intends to enter newer countries like Brazil going ahead.

Considering the rupee unsteadiness, it bodes well for the company's business as the total foreign exchange earnings of the firm are far greater than their forex expenditure. Taking into account the current trend of the rupee against the US dollar and the current position of hedged contracts, a further benefit on account of depreciating rupee would accrue to the company in the coming quarters.

BAJAJAUTO is looking to tap into KTM and Kawasaki's vast expertise overseas to double sales volumes and achieve 10 million sales a year by 2016. This will also help BAJAJAUTO in doubling its turnover and achieve 50% of its sales through exports. The company's focus continues to remain on motorcycles, where it is investing high amount in R&D, rather than on production.

New launches to improve market share in premium segment

With a leading market share in the high-margin premium motorcycles segment, BAJAJAUTO is well-positioned to benefit from its six new launches under the Discover brand in the market in the next six months, which in turn would help it in improving market share. Further, strategic partnership with KTM of Europe and Kawasaki of Japan has enabled BAJAJAUTO to bring relevant products. Recently, BAJAJAUTO has launched its premium bike from the KTM platform at a price of ₹1.8 lakh. The KTM 390 Duke is the second offering from the KTM portfolio as BAJAJAUTO had launched the first KTM offering, KTM 200 Duke, in January 2012. The premium segment accounts for 1,000 units per month and Bajaj auto commands nearly 75% share in it. With this new launch, the company expects its premium segment to clock higher sales and volumes to grow in double-digits in FY14E.

BAJAJAUTO's dominant leadership position in the executive motorcycle segment has compelled it to launch 6 new variants of Discover motorcycle (to be priced between ₹40-50,000) in FY14 in the local market. It also plans to launch few premium motorcycles (KTM, Pulsar) to maintain its leadership with 47-48% share in the domestic premium motorcycle segment. Separately, on the capacity front, the management is planning to increase the 3W capacity in FY14 to 60,000/month from the current levels of 50,000/month.

Export, in Units and revenue, for BAJAJAUTO

	FY2012	FY2013	Growth %
Motorcycles (nos.)	1,267,648	1,293,231	2.0%
Three-wheelers (nos.)	312,176	253,926	(18.7%)
Total (nos.)	1,579,824	1,547,157	(2.1%)
Exports in USD (million)	1,369	1,309	(4.4%)

The 3W market leader is also focusing on tapping new markets, like Ivory Coast, Uganda and Tanzania in Africa, which it feels will be the new growth markets. Thus, we believe that these new launches during festive season coupled with plans of foraying in new markets would result in to volume growth, which in turn will increase its market share by 1-2% by end of FY14E.

We believe increased rural market penetration, customers' increased purchasing power, and expected strong replacement demand will contribute to a rebound for the premium motorcycle segment. With such premium launches it would focus on providing value for money to customers though offering better style, features, technology at competitive prices.

Q1FY'14 performance stabilized on better export realizations

The company has posted a decline of 9% in its total unit sales to 9,79,275 units. The domestic motorcycle sale posted an 8% YoY drop to 5,71,655 units, while exports fell 21% to 2,88,496 units. However, in the same segment it grew by 2.8% QoQ while export fell by 5.0% QoQ. Moving ahead, in the commercial vehicle space, domestic sales were steady at 45,000 units in the first quarter. Exports, however, rose 44% to 74,000 units. Further, a 250 bps rise in EBITDA margin to 20.4% has led to a 15.0% increase in EBITDA to ₹10.03 bn. The rise in EBITDA margin was also due to falling raw material cost. The raw material costs including traded goods cost, as a percentage to sales net stock adjusted, fell by 260 bps to 64.7%. On the other hand, staff cost grew by 40 bps to 3.8% while other expenditure fell by a marginal 10 bps to 6.9%.

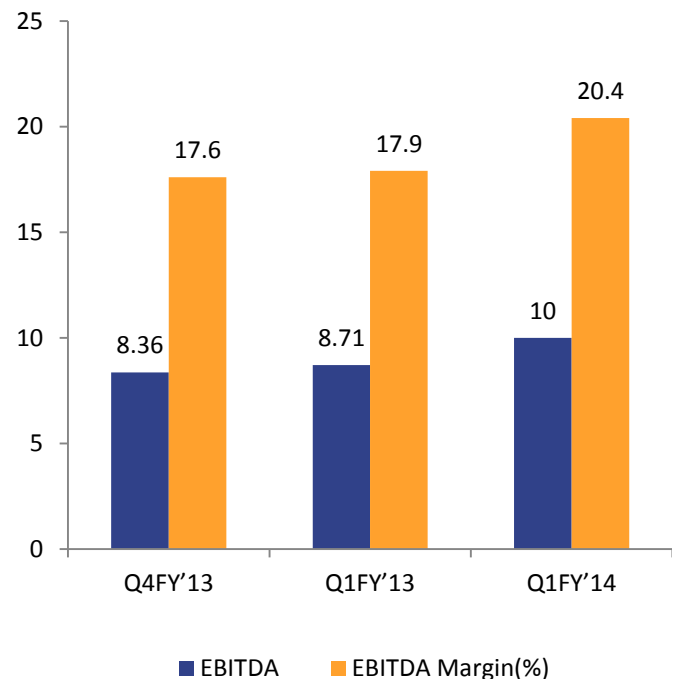
Looking ahead, the firm after witnessing a drop in local motorcycle sales, its focus is highly centralized to grow the discover platform sales in FY14 with six new launches lined up around the festive season. In 3Ws the scenario is far healthier with a lot of new permits opening up in domestic market (20K permits in Hyderabad; 35K expected in Maharashtra) and export markets like Sri-Lanka normalizing.

The PBT before forex gain/loss grew by a healthy 11.3% to ₹11.34 bn on account of overall favorable non-operating performance. The other income de-grew 3.5% YoY to ₹1.76 bn, while interest cost totaled ₹0.001 bn, for the quarter. Depreciation charges however increased by 26% to ₹0.44 bn. But it was a forex loss of ₹0.96 bn against a profit of ₹0.33 bn in corresponding quarter of previous year that actually put a brake on bottom-line growth. PBT before EO thereafter witnessed a mere 2% rise to ₹10.37 bn. With steady tax provision (50 bps drop in tax rate), net profit grew by 3% to ₹7.37 bn. Besides, devaluation of the domestic currency has helped the company in boosting its bottom-line during Q1FY14, despite recording a 9% decline in the number of units sold and marginal growth in income.

Segmental Snapshot (YoY)

Segment	Q1FY14	Q1FY13	YoY%
Motorcycles			
Domestic	571,655	618,489	(7.6)
Export	288,496	364,134	(20.8)
Three-wheelers			
Domestic	45,057	44,837	0.5
Export	74,067	51,511	43.8

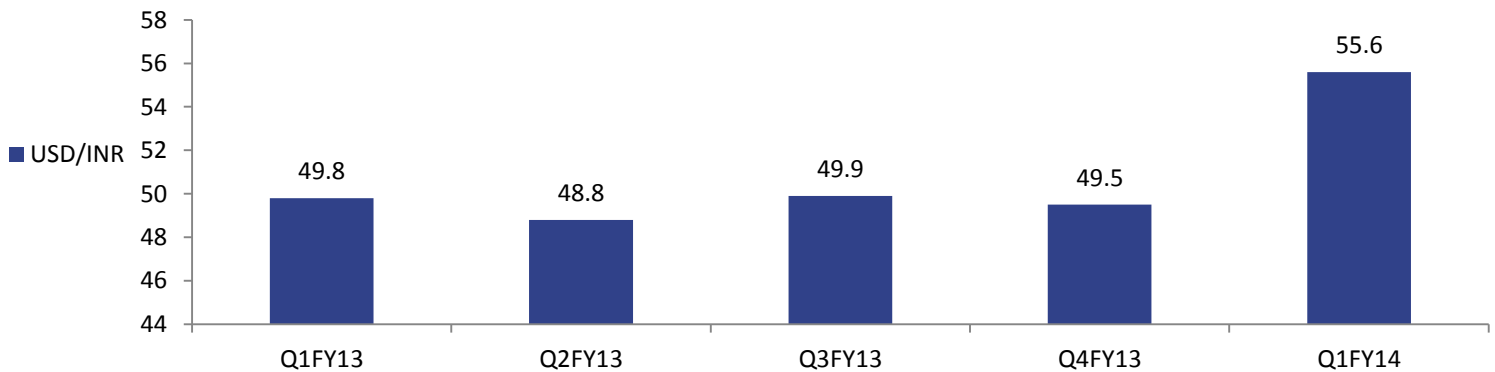
EBITDA (in ₹ bn) & EBITDA Margin



Favourable currency fluctuation bodes well for margin growth

The current trend in the Indian rupee and the US dollar has changed substantially in recent periods and may continue to fluctuate substantially in the future. Despite the fact that BAJAJAUTO's export volumes, which account for about a third of total sales, fell about 13% in the quarter, but the company reaped the benefits of a weak rupee that lost nearly 9% against the US dollar during the period. Taking into account the current trend of the rupee to the US dollar and the current position of hedged contracts, a further benefit on account of depreciating rupee would accrue to the company in the coming quarters. Also, a prudent and well thought out strategy to hedge future earnings from exports has ensured the company's ability to leverage the rupee depreciation with respect to its earnings from abroad.

Aided by favourable currency realizations



The company acknowledged the concerns that near-term demand outlook remains muted across both domestic/export markets and management guidance on volumes broadly points to FY14 being a 'no growth year'. However, it believes that the launch of the Discover platform should help improve the market share. Also, demand could see some improvement on good monsoons and new permits issued for 3Ws. However, favorable currency would augur well for margins.

Peer Comparison: BAJAJAUTO running ahead

In ₹billion	Bajaj Auto	Hero Motor Corp.
Net sales	49.1	61.6
% change YoY	0.9	(1.4)
PBIDT	10.8	10.3
% change YoY	2.7	(1.3)
Net profit	7.4	5.5
% change YoY	2.7	(10.9)

Balance Sheet (Consolidated)

Y/E (₹mn)	FY12A	FY13A	FY14E	FY15E
Share Capital	289	289	289	289
Reserve and surplus	5,792	7,776	8,877	10,245
Net Worth	6,082	8,065	9,167	10,535
Loan	255	193	221	255
Deferred tax liability	48	115	120	124
Long Term Provisions	113	136	139	142
Current liabilities	4,667	4,166	4,457	4,991
Capital Employed	11,165	12,676	14,103	16,047
Fixed assets	1,527	2,101	2,521	3,025
Goodwill	434	548	614	687
Deferred Tax Assets	39	33	33	33
Loan & Advances (LT)	602	463	505	550
Non-current Assets	3,378	3,349	3,416	3,552
Current Assets	5,185	6,182	7,014	8,199
Capital Deployed	11,165	12,676	14,103	16,047

Key Ratios (Consolidated)

Y/E	FY12A	FY13A	FY14E	FY15E
EBITDA Margin (%)	18.9	18.2	19.8	20.9
EBIT Margin (%)	21.3	21.3	23.0	24.0
NPM (%)	15.5	15.6	16.8	17.4
ROCE (%)	64.2	50.3	51.1	52.1
ROE (%)	50.1	38.8	39.2	39.8
EPS (₹)	105.2	108.3	124.3	144.8
P/E (x)	16.9	16.4	14.3	12.3
BVPS	210.2	278.7	316.8	364.1
P/BVPS (x)	8.5	6.4	5.6	4.9
EV/Operating Income (x)	11.6	11.5	10.0	8.6
EV/EBITDA (x)	13.5	14.0	12.0	10.1
EBITDA Margin (%)	18.9	18.2	19.8	20.9

Profit & Loss Account (Consolidated)

Y/E (₹mn)	FY12A	FY13A	FY14E	FY15E
Total Income	1,95,947	2,00,420	2,14,602	2,40,354
Expenses	1,58,847	1,63,963	1,72,014	1,90,080
EBITDA	37,100	36,457	42,588	50,274
Other Income	6,066	7,971	8,450	9,295
Depreciation	1,467	1,650	1,766	1,977
EBIT	41,698	42,778	49,272	57,591
Interest	227	11	11	11
Profit Before Tax	41,471	42,766	49,260	57,579
Exceptional	(1,340)	-	-	-
Tax	10,197	12,172	14,039	16,410
Deferred tax asset	32	114	116	118
Share of Profit/ (Loss) of associates	551	844	853	861
Minority interest	(1.4)	(1.7)	(1.7)	(1.7)
Net Profit	30,454	31,327	35,960	41,914

Valuation and view

Bajaj Auto bestowed by its varied geographical presence, product mix, and greater product pipeline visibility is all set to compete with tough market environment. Further, low commodity price and higher export realization can be strong margin drivers ahead. Thus, we believe that festive season round the corner with the launch of 6 new variants in the Discover family; Bajaj Auto is expected to perform well in the coming quarters.

At a current CMP of ₹1,780.3, the company is attractively placed at P/E of ~14.3x FY14E. Considering the above aspects, we rate the stock as 'BUY', with a potential upside of ~12% for the coming 12 months.



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