# Maruti Suzuki India Ltd.

**August 14th 2014**

| BSE Code: | 532500 | NSE Code: | MARUTI | Reuters Code: | MRTI.NS | Bloomberg Code: | MSIL:IN |
|---|---|---|---|---|---|---|---|

**Maruti Suzuki India Ltd (Maruti), India's largest passenger car company accounting for around 40% share of the domestic passenger car market, is a subsidiary of the Japanese automaker, Suzuki Motor Corporation. Established in 1981, the company is engaged in the business of manufacturing, purchase and sale of motor vehicles and spare parts (automobiles). With five plants in Gurgaon and Manesar areas of Haryana and a production capability of around 1.5 mn units per annum, Maruti offers around 200 variants across the industry segments like passenger cars, utility vehicles and vans. The company is also planning to come up with a new manufacturing facility in Gujarat by FY15 and it intends to expand its manufacturing capacity to 1.8 mn units by FY15.**

## Investor's Rationale

**Robust pipeline of new vehicles to revive growth in FY15:** Maruti's earnings growth visibility appears high in FY15 on the back of its wide dealership network, a long reach in rural areas and a strong pipeline of new vehicles. We expect the company's volume growth to revive in FY15 led by three new upcoming launches (Celerio, Ciaz in Q2FY15 and compact SUV in Q4FY15) and a gradual recovery in demand after three years of weak performance across the industry.

**Eyeing to increase its PV market share to ~45% in FY15E:** Despite challenging times and intense competition across segments, Maruti is targeting around 15% sales volume growth in FY15E and also looking to increase its market share in the passenger vehicle market to ~45%. With the company lined-up with new launches in FY15 and is equally focused towards product up-gradation, we expect the company is well placed to take benefit from an upturn in passenger vehicle (PV) demand, given its leadership position in the PV segment.

**Higher volumes and favourable foreign exchange aided profitability in Q1FY15:** Maruti has reported a strong set of numbers in Q1FY15, with the standalone net profit surged more than 20% at ₹7,622.8 mn on the back of strong sales and higher other income. Further, the net sales also grew 11% to ₹1,10,735.1 mn in Q1FY15 supported by sales volumes growth of 12.6%. We expect revenue growth at ~16% CAGR in FY14-16E reaching ₹6,03,194 mn in FY16E on demand recovery and new launches, which is expected to boost volumes.

**Wide network and entry in to newer market to improve earning visibility in the coming year -** Given the strong brand positioning, expanding portfolio, and extensive rural/semi-urban network, Maruti is well positioned among its peers. Rural sales continue to grow at a strong pace of ~16% and accounted for ~32% of total volumes in FY14 and the company has expanded its reach to 93,000 villages from around 44,000 villages in FY2013 and expects to increase it further going ahead. While, on the back of entry into new markets like Africa, Latin America and Middle East, Maruti is targeting 10% export growth in FY15E.

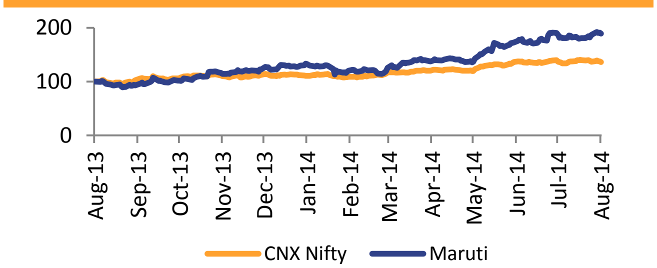
### Market Data

| | |
|---|---|
| **Rating** | **BUY** |
| **CMP (₹)** | 2,672.0 |
| **Target (₹)** | **3,150** |
| **Potential Upside** | ~18% |
| **Duration** | Long Term |
| Face Value (₹) | 5.0 |
| 52 week H/L (₹) | 2,693.0/1,215.0 |
| Adj. all time High (₹) | 2,643.0 |
| Decline from 52WH (%) | 0.8 |
| Rise from 52WL (%) | 119.9 |
| Beta | 1.0 |
| Mkt. Cap (₹bn) | 807.2 |
| Enterprise Value (₹bn) | 809.5 |

### Fiscal Year Ended

| Y/E | FY13A | FY14A | FY15E | FY16E |
|---|---|---|---|---|
| Revenue (₹bn) | 443.0 | 444.5 | 511.2 | 603.2 |
| EBITDA (₹bn) | 43.3 | 52.0 | 62.2 | 77.0 |
| Net Profit (₹bn) | 24.7 | 28.5 | 34.7 | 44.0 |
| EPS (₹) | 81.7 | 94.4 | 114.8 | 145.8 |
| P/E (x) | 32.7 | 28.3 | 23.3 | 18.3 |
| P/BV (x) | 4.2 | 3.8 | 3.4 | 3.1 |
| EV/EBITDA (x) | 18.7 | 15.6 | 13.0 | 10.5 |
| ROCE (%) | 15.9 | 16.9 | 18.6 | 21.6 |
| ROE (%) | 13.0 | 13.3 | 14.7 | 17.1 |

### One year Price Chart




| Shareholding Pattern | Jun'14 | Mar'14 | Diff. |
|---|---|---|---|
| Promoters | 56.2 | 56.2 | - |
| FII | 22.0 | 22.4 | (0.4) |
| DII | 14.0 | 13.6 | 0.4 |
| Others | 7.8 | 7.8 | - |

*Maruti derives ~60% of its overall sales from the passenger car segment and has a dominant position in the segment with a market share of ~40%, led by popular models like Alto, Wagon R and Swift.*

## Maruti Suzuki India Ltd – India's largest passenger car company

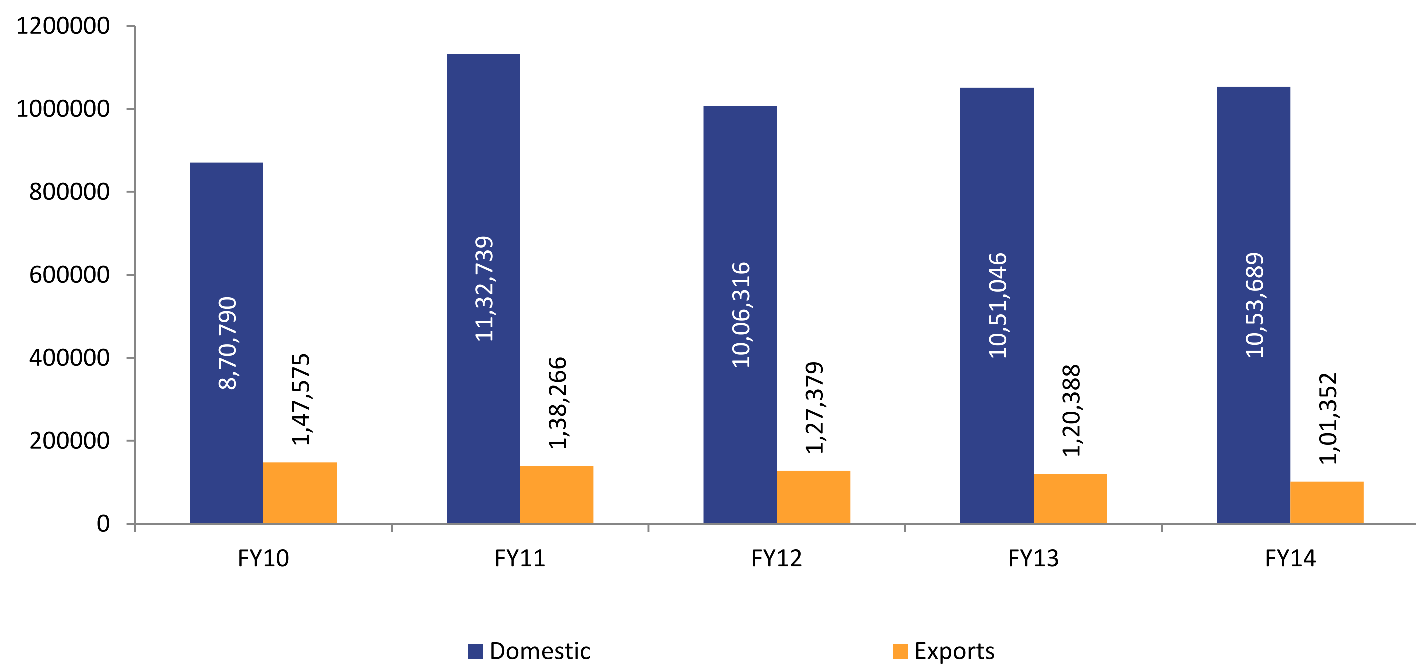
Maruti Suzuki India Ltd. (MSIL), a subsidiary of Suzuki Motor Corporation (SMC), Japan (which holds a 54.2% stake), is the largest passenger car company in India, accounting for ~40% of the domestic passenger car market. The company is engaged in the business of manufacturing, purchase and sale of motor vehicles and spare parts (automobiles). The other activities of the company include facilitation of pre-owned car sales, fleet management and car financing. Maruti offers 14 brands and over 150 variants ranging from Alto 800 to the Life Utility Vehicle Maruti Suzuki Ertiga.

The company derives ~60% of its overall sales from the small car segment and has a dominant position in the segment with a market share of ~40%, led by popular models like Alto, Wagon R and Swift. The company operates from two facilities in India (Gurgaon and Manesar) with an installed capacity of 1.5 mn units and is in the process of expanding its manufacturing capacity to 1.8 mn units by FY15E.

Currently, exports account for ~9% of its overall sales volume and the company is striving hard to expand its market in the non-European countries (thereby reducing its dependency on the deteriorating European markets). The company offers a full range of cars from entry level Maruti 800 & Alto to stylish hatchback Ritz, A-star, Swift, Wagon R, Estillo and sedans DZire, SX4 and Sports Utility vehicle Grand Vitara.

In FY14, Maruti's domestic sales rose just 0.3% to 10.53 lakh units while the entire PV industry fell 6% — its market share in the fiscal stood at 42.08%. In FY13, MSIL's volumes were up 4.44% to 10.51 lakh units — market share stood at 39.1%.

### Maruti's sales volume trend



## Strong volume growth and other income triggered 21% YoY rise in Q1FY15 net profit

*Maruti's cost reduction and localization initiatives, growth in volumes and favorable foreign exchange helped improve the profitability in Q1FY15.*

Maruti, India's largest carmaker by sales, saw business taking a ride in Q1FY15 as its earnings beats street estimates on the back of strong sales and higher other income. The auto major has reported a growth of 20.7% in its standalone net profit at ₹7,622.8 mn in Q1FY15 as against a net profit of ₹6,316.0 mn in the same period a year ago. The company's cost reduction and localization initiatives, growth in volumes and favorable foreign exchange helped to improve the profitability. The other income also rose significantly by 45% YoY to ₹2,965.3 mn. Further, the company reported 11% rise in its net sales to ₹1,10,735.1 mn in Q1FY15, against ₹99,951.2 mn in Q1FY14 supported by sales volumes growth of 12.6%.

Material Cost to Net Sales was higher by 20 basis points due to higher discounts (net of selling price increase) but was to some extent offset by favorable foreign exchange. Meanwhile, OPM improved 30 basis points to 11.7%, as a result, the operating profit grew 14% to ₹13,282 mn. Apart from this, the depreciation charges also grew modestly by ~22% YoY to ₹5,836.4 mn mainly due to addition of Manesar-C line and Gurgaon diesel engine plant and change in useful life of assets pursuant to the new Companies Act, 2013.

**Financial Performance trend (Standalone)**

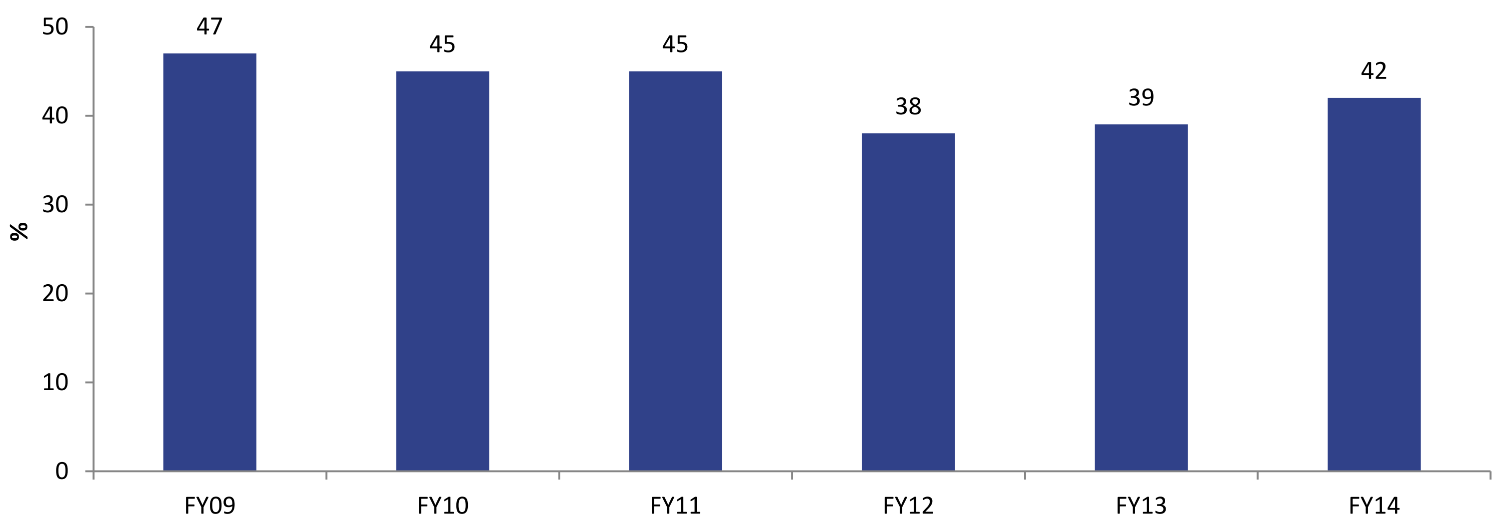
| In ₹mn | Q1FY15 | Q1FY14 | YoY (%) | Q4FY14 | QoQ (%) |
|---|---|---|---|---|---|
| **Net Revenue** | **113,696.4** | **102,373.4** | **11.1** | **121,013.9** | **(6.0)** |
| **EBITDA** | **13,282.0** | **11,661.50** | **13.9** | **12,475.30** | **6.5** |
| **EBITDA Margin (%)** | **11.7** | **11.4** | **29bps** | **10.3** | **137bps** |
| Other Income | 2,965 | 2,043 | 45.1 | 4,066 | (27.1) |
| Depreciation | 5,836 | 4,802 | 21.6 | 5,637 | 3.5 |
| Interest | 386 | 442 | (12.8) | 434 | (11.2) |
| Tax | 2,403 | 2,145 | 12.0 | 2,470 | (2.7) |
| **PAT** | **7,622.8** | **6,316.0** | **20.7** | **8,000.5** | **(4.7)** |
| **PAT Margin %** | **6.5** | **6.0** | **48bps** | **6.4** | **14bps** |
| EPS (₹) | 25.2 | 20.9 | 20.6 | 26.5 | (4.9) |

## Continues to maintain its leadership position with ~42% PV market share

*Given its leadership position and three new launches (Celerio, Ciaz in Q2FY15 and compact SUV in Q4FY15), we expect Maruti is well placed to take benefit from an upturn in PV demand.*

With the government mandating petrol diesel price gap rationalization, there has been a shift towards petrol cars, which in turn helped Maruti to regain its ~42% passenger vehicle market share in FY14. In FY13, the company's market share had reduced to ~39% from ~47% in FY09 due to the rising gap in petrol-diesel prices and shifting customer preference for diesel cars. The market share was further lost on account of the persistent labor troubles at Manesar in both FY12 and FY13, which halted production. With strong brand equity, low cost of ownership, a complete product portfolio and a broader based dealer network, Maruti is well placed to sustain its ~42% PV market share over the medium term. Reduction in interest rates and respite in petrol prices would drive recovery in demand in PV segment going forward. Moreover, the company is best placed amongst competitors if the diesel car demand remains strong. In an intensely competitive industry struggling with demand slowdown, Maruti being the market leader has also been forced to give incentives in order to ward off competition and retain market share. However, we believe, the new products and improved product mix are effective in reducing the impact of the demand slowdown, which saw strong sales of the newly launched Celerio in Q4FY14, which had no discounts. Going ahead, as the industry recovers on the back of an improvement in overall economic scenario and interest rate cuts, discounting levels are likely to taper off, thereby aiding profitability.

**Maruti's PV market share trend**




*With equally focused towards product up-gradation and launch of new products, Maruti is targeting around 15% sales volume growth and also to increase its market share in passenger vehicle market to 45% in FY15E.*

## Product pipeline to support growth

Given its leadership position in the PV segment, Maruti remains an attractive play on the discretionary purchase recovery among consumers and consequent improvement in economic outlook. Maruti is riding high on newly-launched cars. (Maruti's market share in the PV industry stood at around 42% in FY14). The company has now lined up a major new model onslaught for FY15. New vehicle launch, the Ciaz mid-size sedan, a light commercial vehicle and the S-Cross crossover/compact SUV, will be added to Maruti's current portfolio of 12 vehicle brands in FY15E. Ciaz launch is expected to happen in September this year, however S-Cross is anticipated to break cover by 2015. Meanwhile, the popular Swift, Dzire, Alto K10 and Ertiga models, are also expected to get refreshed with a facelift to boost volumes as consumer sentiment improves under the new government. We expect the volume growth of the company to revive in FY15E led by the new launches and a gradual recovery in demand after three years of weak performance that the industry has witnessed. Further, continuous up-gradation of existing products is expected to give the company a competitive advantage. With equally focused towards product up-gradation and launch of new products embedded with latest technology, the company is targeting around 15% sales volume growth in FY15E as it looks for a 300 basis point jump in its market share in the country's 25 lakh unit PV market to 45%.

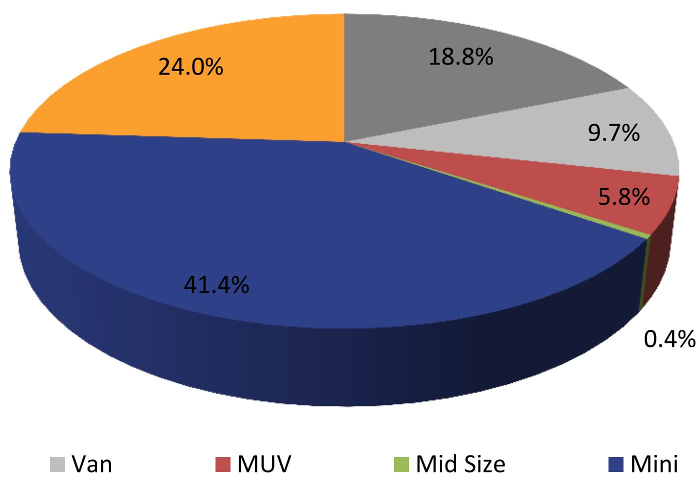
## Eyeing double digit volume growth in FY15

Despite of de-growth in the automobile industry on the whole, Maruti managed to report a 10.3% YoY growth in its sales volume in the domestic market at 2,70,643 units in Q1FY15, while the exports grew 38.7% YoY to 29,251 units during the period. The overall sales volume

*With gradual economic recovery and a strong product pipeline, Maruti is hopeful of an overall double digit volume growth in the domestic market in FY15.*

of the company during the quarter under consideration grew ~13% to 2,99,894 vehicles. The volumes growth was led by successful launch of Celerio in February 2014 and revival in demand for petrol cars and higher discounts offered during the quarter. According to the management during the conference call, the company has witnessed sales growth of ~12% in urban markets while, the rural market sales rose 26% in Q1FY15. Further, the company remains confident of sustaining its growth trajectory in future and is hopeful of an overall double digit volume growth in the domestic market this year. With improved economic outlook, we expect Maruti to be a key beneficiary of the upturn in PV demand, given its leadership position.

**Domestic sales contribution in FY14**




## Gujarat plant to provide operational efficiency

*The recent announcement of contract manufacturing terms by Suzuki for the Gujarat facility are favorable for Maruti in the longer term.*

Suzuki has outlined plans to set up a 100% subsidiary in India under Suzuki Motors Corporation (SMC), Suzuki Motor Gujarat (SMG) in Gujarat, which would hold the Gujarat plant and manufacture and sell vehicles solely to Maruti. In a major relief to the minority shareholders of the company, the board of directors of the company has approved a new proposal that entails the entire capex for the Gujarat subsidiary would be funded by depreciation and equity brought in by Suzuki Motor Corporation. Further, the land required by SMG for manufacturing the volumes would be leased by Maruti to SMG. The lease would be co-terminus with the contract manufacturing agreement (CMA). In case of termination of the contract, the facilities of the Gujarat subsidiary would be transferred to Maruti at book value and not at fair value, as was envisaged earlier. The entire capex for the Gujarat subsidiary in the initial phase is expected to be ~₹185 bn. SMG would operate on a “no profit, no loss basis” and would be done by adjusting the selling price of products. In March 2014, the Board of Maruti decided, as a measure of good corporate governance, to seek minority shareholders’ approval as stipulated in Section 188 of the Companies Act, 2013 of India even though it was not then legally required (Section 188 has now come into force as on April 1, 2014).

The deal would enable Maruti to save ₹105 bn, assuming post tax return of 8.25% p.a. for the 15-year contract period. The additional funds available with Maruti could enable the company to strengthen its marketing and sales infrastructure, R&D, and overseas market penetration.

## Revival in demand for petrol cars provide further growth impetus

*The rationalisation of diesel-petrol price gap would provide a fillip to Maruti's petrol-dominated product portfolio.*

High interest rates and petrol pricing and partial deregulation of diesel has added to the auto industry's woes during FY14. A significant increase in the petrol prices severely impacted the sales of petrol based vehicle models in the past. Petrol vehicles after declining for two years turned slightly positive and grew by 4% in FY14. With this domestic unit sales posted a decline of 6% during the year, the highest year-on-year decline in a decade.

But the recent partial deregulation of diesel price is a step to narrow down the gap between price per litre of diesel and petrol. Given Maruti's higher exposure to entry-level/petrol models, Maruti would be the key beneficiary of this trend. The narrowing of fuel price gap between petrol and diesel price, would further revive demand for petrol cars. Diesel vehicle sales declined by 14% in FY14 on account of rise in diesel prices and share of diesel vehicles in total industry came down from 58% in FY13 to 53% in FY14. Going forward, we expect the sales growth of the petrol based vehicle model to further increase in the coming quarters.

However, despite of declining sales of diesel vehicles, the company expects demand for diesel cars to remain robust. The company has undertaken various cost reduction initiatives with localization being one of the initiatives, which helped the company to improve its operational performance. During FY14, the company has set up a diesel engine plant in Gurgaon with an annual capacity of 150,000 engines. Apart from this, the company is buying 100,000 diesel engines a year from the FIAT plant in India.

## Aims to reduce import exposure to ~12% by the end of FY15E

*In order to reduce the dependence on imports, Maruti has undertaken a strong localisation drive and been able to reduce the exposure from 19.5% to 16% in four or five quarters.*

With ~22% import exposure, Maruti's operating performance has improved considerably due to weak Japanese currency. The company's profit margins are set to show even stronger gains in the coming quarters as India's biggest car maker reaps an even greater windfall from cheaper yen-denominated imports of components. Besides, sound business knowledge and decade long industry expertise of its other board members has gone a long way in helping Maruti to stage better performance even in a tough economic environment.

In order to reduce the dependence on imports, Maruti has undertaken a strong localisation drive and been able to reduce the exposure from 19.5% to 16% in four or five quarters. With the management target to reduce the same to ~12%, we feel, going ahead, currency risk will reduce significantly. Other currency exposures like USD and euro have more or less a natural hedge due to exports and, thus, have little forex risk.

## Balance Sheet (Consolidated)

| Y/E (₹mn) | FY13A | FY14A | FY15E | FY16E |
|---|---|---|---|---|
| Share Capital | 1,510 | 1,510 | 1,510 | 1,510 |
| Reserve and surplus | 188,769 | 213,454 | 234,729 | 256,626 |
| **Net Worth** | **190,279** | **214,964** | **236,240** | **258,136** |
| Minority Interest | 106 | 122 | 122 | 122 |
| Loans | 8,170 | 8,749 | 8,322 | 9,244 |
| Long term provisions | 2,259 | 2,007 | 2,241 | 2,644 |
| Deferred tax liability | 4,176 | 5,962 | 5,962 | 5,962 |
| Current Liabilities | 69,719 | 82,310 | 94,674 | 111,715 |
| **Capital Employed** | **274,709** | **314,115** | **347,561** | **387,824** |
| Fixed Assets | 119,896 | 136,732 | 154,644 | 171,827 |
| Long term investments | 21,460 | 15,212 | 17,037 | 19,082 |
| Loans and advances | 12,865 | 16,540 | 22,009 | 30,495 |
| Other non-current assets | 8,946 | 95 | 95 | 95 |
| Current Assets | 111,542 | 145,537 | 153,775 | 166,326 |
| **Capital Deployed** | **274,709** | **314,115** | **347,561** | **387,824** |

## Profit & Loss Account (Consolidated)

| Y/E (₹mn) | FY13A | FY14A | FY15E | FY16E |
|---|---|---|---|---|
| **Net Sales** | **443,043** | **444,506** | **511,182** | **603,194** |
| Expenses | 399,764 | 392,467 | 449,021 | 526,189 |
| **EBITDA** | **43,278** | **52,039** | **62,161** | **77,005** |
| Other Income | 8,301 | 8,305 | 8,471 | 8,641 |
| Depreciation | 18,898 | 21,160 | 23,487 | 26,071 |
| **EBIT** | **32,682** | **39,184** | **47,145** | **59,575** |
| Interest | 1,978 | 1,846 | 1,809 | 1,899 |
| **Profit Before Tax** | **30,703** | **37,339** | **45,336** | **57,676** |
| Tax | 6,215 | 9,023 | 10,881 | 13,842 |
| Share of P&L in associate/MI | 206 | 213 | 213 | 213 |
| **Net Profit** | **24,693** | **28,529** | **34,669** | **44,047** |

## Key Ratios (Consolidated)

| Y/E | FY13A | FY14A | FY15E | FY16E |
|---|---|---|---|---|
| EBITDA Margin (%) | 9.8 | 11.7 | 12.2 | 12.8 |
| EBIT Margin (%) | 7.4 | 8.8 | 9.2 | 9.9 |
| NPM (%) | 5.6 | 6.4 | 6.8 | 7.3 |
| ROCE (%) | 15.9 | 16.9 | 18.6 | 21.6 |
| ROE (%) | 13.0 | 13.3 | 14.7 | 17.1 |
| EPS (₹) | 81.7 | 94.4 | 114.8 | 145.8 |
| P/E (x) | 32.7 | 28.3 | 23.3 | 18.3 |
| BVPS(₹) | 629.9 | 712.0 | 782.4 | 854.9 |
| P/BVPS (x) | 4.2 | 3.8 | 3.4 | 3.1 |
| EV/Operating Income (x) | 15.7 | 13.4 | 11.4 | 9.4 |
| EV/EBITDA (x) | 18.7 | 15.6 | 13.0 | 10.5 |

## Valuation and view

We continue to remain bullish on the long-term growth prospects of Maruti, given its leadership position coupled with a strong product pipeline in the next two to three years. We expect Maruti's revenue to grow at ~16% CAGR in FY14-16E on demand recovery and new launches, which is expected to boost volumes. Further, the rationalisation of diesel-petrol price gap would provide a fillip to Maruti's petrol-dominated product portfolio. A strong product brand with an extensive distribution network places the company ahead of its peers.

At a current CMP of ₹2,672.0, the stock trades at P/E of 18.3 FY16E. We recommend 'BUY' with a target price of ₹3,150, which implies potential upside of ~18% to the CMP from a long term perspective.

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