MARUTI SUZUKI INDIA LTD.

November 04, 2011

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Maruti Suzuki India Ltd (MSIL) is the largest car manufacturing company of India, which has been ruling the Indian auto market for more than two decades. A subsidiary of Japanese auto giant, Suzuki Motor Corp, the company has two manufacturing facilities in India with a capacity to produce over a 1.2 million vehicles annually. MSIL is also coming up with a new manufacturing facility in Gujarat by 2015. Offering 15 brands in over 150 variants, the company intends to expand its manufacturing capacity to 1.75 million by 2013.

Investor's Rationale

After being crippled by endless tool down and strikes by workers, production halt, consecutive rate hikes etc in the first half of the fiscal, MSIL is gearing up to make up for the losses by ramping up the productivity at both its manufacturing facilities, working on full shifts to achieve a set target over 100,000 vehicles for Oct'11. Beside, the first phase completion of MSIL's proposed Gujarat unit in 2015 will help the company to lead its peers with a productive capacity of 1.85 million units.

With rising yen pressure, MSIL has witnessed significant increase of 10-13% production cost in recent times. Addressing the issue, the company has chalked out a three-year-long indigenization programme to safeguard it against yen fluctuation and reduce its import dependency by encouraging vendors for local manufacturing of auto components. To begin with, the company has set aside ₹60 billion to be used for the expansion of ancillary units in ~400 acres of land in Gujarat.

To cater the increasing demand of diesel cars in India, the country's largest passenger carmaker is working to enhance its Diesel engine capacity to ~25k /month by January 2012 from its current capacity of ~20k/month. This move of the company would also go a long way in raising proportion of diesel vehicles in product mix, bring down its average blended discount and thereby result higher blended net realization.

Though the attractiveness of the Indian auto market and intense competition has caused significant downfall in the MSIL's market share, it continues to dominate passenger car segment with ~40% share in the 2.5 million unit Indian auto market. However, to cater to the changing market dynamics, MSIL plans to launch at least seven models in the next two-three years as it bids to regain market share and also to double its dealer network to 2,000 outlets across 800 cities by 2015.

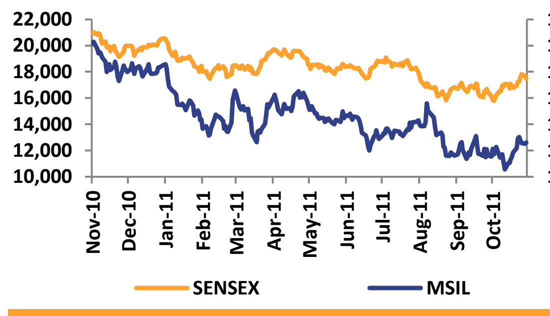
Market Data

Rating	**BUY**
CMP (₹)	1,123
Target (₹)	**1,300**
Potential Upside	~15%
Duration	Long Term
52 week H/L (₹)	1,599.9/1,010.4
All time High (₹)	1,740
Decline from 52WH (%)	476.9
Rise from 52WL (%)	112.6
Beta	0.48
Mkt. Cap (₹ bn)	32.5
Enterprise Val (₹ bn)	30.3

Fiscal Year Ended

	FY10A	FY11A	FY12E	FY13E
Revenue (₹bn)	296.2	370.4	357.6	408.3
Net Profit(₹bn)	24.9	22.8	19.8	25.1
Share Capital	1.4	1.4	1.4	1.4
EPS (₹)	86.1	78.9	68.4	86.9
PE (x)	13.0	14.2	16.4	12.9
P/BV (x)	2.8	2.3	2.1	1.8
EV/EBITDA (x)	8.4	8.3	9.3	7.0
ROE (%)	21.1	16.5	12.5	13.7
ROCE (%)	24.4	18.5	13.1	15.3

One year Price Chart



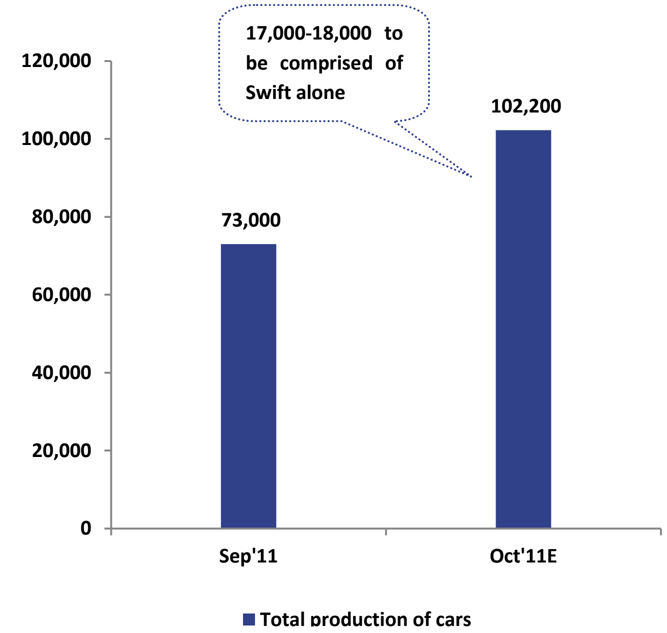
Shareholding Pattern	Sep'11	Jun'11	Diff.
Promoters	54.2%	54.2%	-
Institutional	36.9%	36.7%	(1.40)
General Public	2.4%	2.5%	(2.00)
Others	6.4%	6.6%	3.50

MSIL gears up to tackle accumulated backlogs

After witnessing losses to the tune of ₹22 billion due to labour unrest in Q2FY12, the India's biggest carmaker is racing ahead to clock its highest production of over 100,000 vehicles in Oct'11, ensuring timely deliveries and promises to its customers.

Endless tool down and strikes by workers of MSIL at both Manesar and Gurgaon plant has resulted in 24% decline in Jul-Sep'11 production, the steepest percentage decline in the company's 29-year history. As a result, backlog of bookings witnessed high accumulation, especially for its hatchback Swift for which the waiting list has grown to more than 100,000 units. However, with Manesar strike being resolved conditions have come back to normal and the company is working on full shifts, to meet the pent-up demand. As a special effort to meet the exceptional demand for Swift, MSIL is also streamlining operations of all three plants, in Gurgaon and in the two plants in Manesar, to roll out maximum cars to meet domestic demand and export commitments. MSIL is also pacing up to save its domestic market share that plunged under 40% for the first time ever in this fiscal, forcing it to focus on new product launches.

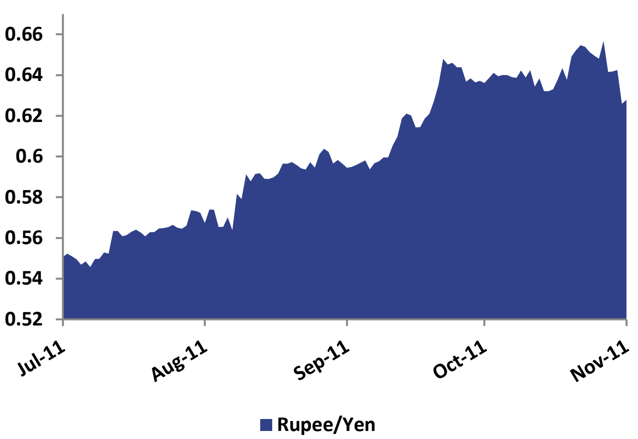
MSIL aims 30-40% higher production for Oct'11 to meet accumulated order backlog



Strategic reduction in imports to hedge against rising Japanese Yen pressure in long run

MSIL, the nation's biggest car maker's direct import of raw material content swings in the range of 8-9% of net sales while it has ~15% import dependency on indirect content from its Japanese parent Suzuki Motor Corp. MSIL has a high localization of ~95-96% but its vendors imprt components and the company pays vendors for the cost incurred because of currency fluctuations. Besides, the company makes royalty payments of ~5-6% of its net sales to its parent company in Japan. As a result, MSIL has a total exposure of ~30% to the Japanese Yen while, it generates only about 9% of its revenue from exports.

Japanese Yen rises 20% against Indian rupee in Jul-Sep'11



In the quarter ended September 2011, yen has strengthened 20% against the Indian currency, resulting in ~ ₹270 million growth in MSIL's import cost. The recent run in the Japanese currency has significantly increased production costs of the passenger car manufacturer by 10-13%. The impact of the stronger yen has turned more worry some for MSIL because rising competition is preventing the company from raising car prices to offset cost increases at a time when growth in car sales is slowing because of higher fuel prices and rising interest rates on automobile loans.

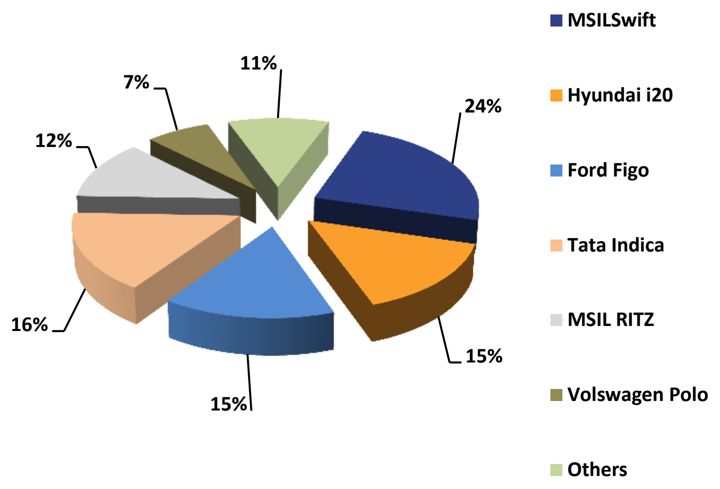
Addressing the issue of rising import cost of components, the company has started a three-year-long indigenization programme to reduce its dependency on imports and safeguard it against a rising yen. Under the proposed strategy, MSIL would encourage vendors to produce more parts locally by helping them in doing more and more research and development activity in India and asking the joint venture partners of Indian vendors to produce more and more components in India. This will help the company to reduce import of parts to 7-8% over the next three years and also save at least ₹1.50 billion every year. The proposed move in long run will not only help the company to minimize the impact of yen fluctuation in its earnings but will also eliminate the import duty and freight expenses from its cost basket.

Increased focus on Swift diesel version to lead the momentum

India is a price sensitive market and the sudden upturn in the prices of petrol has soared up the sales volume of diesel variants small cars in the country. In the first half of the current fiscal, the auto makers of the country has seen the diesel to petrol ratio go up from 60:40 to 85:15.

To cater the increasing demand of diesel cars in India, the country's largest passenger carmaker is working to enhance its Diesel engine capacity to ~25k /month by January 2012 from its current capacity of ~20k/month. The company also intends to increase the production of diesel vehicle proportionately from its current ~21% to ~26% of the overall production volume in FY13E, thereby, enhancing the product mix. With higher proportion of diesel vehicles in its portfolio, MSIL will also be able to bring down its average blended discount in the coming quarters.

MSIL Swift dominates the premium hatchback segment in India

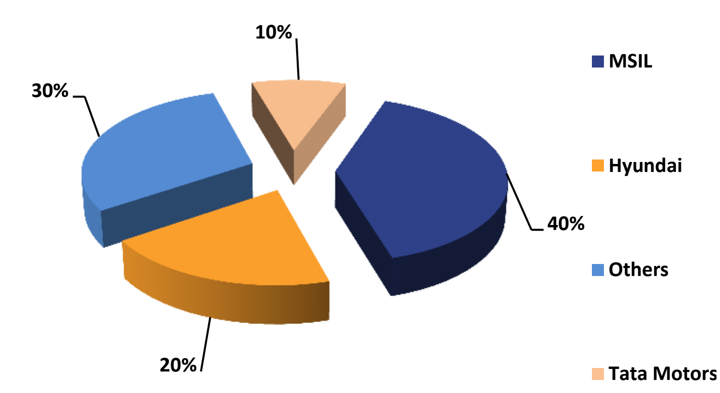


MSIL's newly launched Swift has received a good response in the domestic market and it already has an order backlog of ~1 lac units, out of which ~88% is diesel. To meet the pent-up demand for its diesel swift, MSIL has decided to significantly reduce the exports of diesel engine of ~35K to 45K diesel engines to Hungary to almost negligible levels in the next six months and move the additional engines after export cut for enhanced production of Swift. Besides, MSIL is also working on an agreement with Fiat to source diesel engines in the next two months for increasing the production of its popular compact car Swift. On the materialization of the deal, the company intends to roll out ~20,000 units of Swift every month against it's before strike productivity level of 18,000 units per month.

Dominant market position

After rolling out its first car, the little Maruti 800, in 1984, MSIL has dominated the Indian passenger car market for almost two decades. Though the attractiveness of the Indian auto market and intense competition caused a significant downfall in the MSIL's market share, it continues to dominate passenger car segment with ~40% share in the 2.5 million unit Indian auto market. However, to cater to the changing market dynamics, MSIL plans to launch at least seven models in the next two-three years as it bids to regain market share. The company also wants to double its dealer network to 2,000 outlets across 800 cities by 2015 and enhance its footprints in all places with a population in excess of 50,000. At present, MSIL has ~970 outlets covering 643 cities, which is almost three times that of second-placed Hyundai's 340 dealers in 224 cities.

MSIL leads the race in the domestic passenger car segments



New plant in Gujarat to cause two-fold growth in productivity

India's largest car maker intends to purchase ~1400 acres of land in Gujarat to establish a new plant with an initial capacity to produce1 million units by 2015. Under the proposed investment of approximately ₹180 billion in the region to build additional capacity, ₹60 billion are likely to be used for the expansion of ancillary units in ~400 acres of land. This move of the company would not give MSIL proximity to the ports in Gujarat, ensuring quicker and more efficient exports but will also help the company to strengthen its market position by increasing its production capacity to 3 million units by 2015 from around 1.4 million at present.

Capacity addition at Manesar unit to strengthen market position

After rolling out out nearly 9.5 lakh units from its Gurgaon facility and 3.5 lakh units from the existing Manesar plant in FY11, MSIL is working set up two new plants in Manesar with 2.5 lakh annual capacity each at a total investment of ₹36 billion. The first phase expansion of its Manesar unit was completed in October this year, while other assembly line is expected to be completed by September 2012. After the completion of the capacity enhancement at all the three units of the company, MSIL's output at Manesar is expected to reach 850,000 units a year. Beside, the first phase completion of its proposed Gujarat unit in 2015, MSIL will lead its peers with a productive capacity of 1.85 million units.

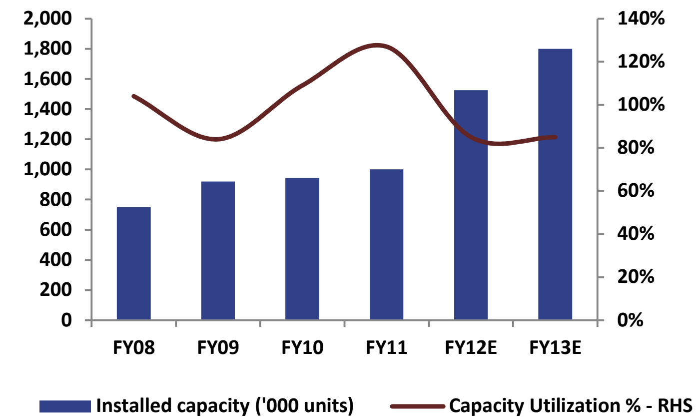
Proposed investment of ₹60 billion to augment growth

MSIL is planning a medium term investment of ₹60 billion, of which a capital expenditure of ₹40 billion are likely to be set aside in FY12 to boost its productive capacity and launch one new model every year. Part of the proposed investment will also be used to build five vehicle stock yards in the country within one to two years. The company has spent ~₹18 billion in upgrading the capacity of second manufacturing unit at Manesar, near Delhi while the third unit, which will also come up at Manesar, will attract an investment of ~₹19 billion. Remaining funds would be utilized on a R&D facility at Rohtak (Haryana), stock yards and brand centers.

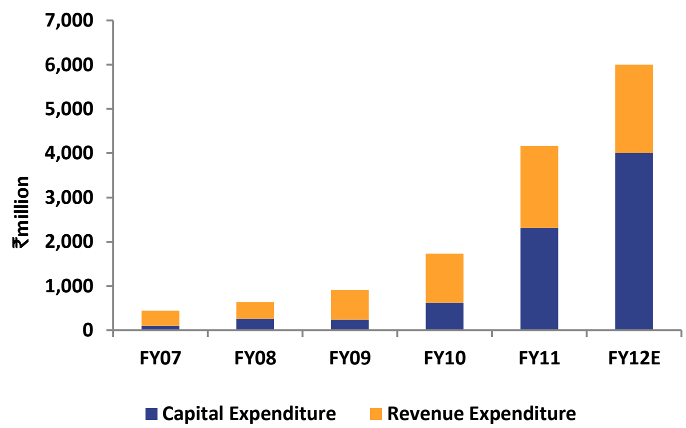
Improved net realization to be sustained in coming quarters

During Q2FY12, MSIL sold 252,307 units of vehicles of which only 12% accounted for export sales. Passenger car sales accounted for ~82% of the total sales volume in India led by Mini passenger cars like M800, Alto, A-Star and WagonR. Though MSIL's sales volume during the quarter declined ~20% on y-o-y basis, blended net realization of the company during the period came higher by 4.8% YoY and 1.1% QoQ to ₹298,741 per unit, due to higher proportion of diesel vehicles in product mix (around 22% vs. 21% QoQ). Average discounts per vehicle for MSIL in Q2FY12 were also higher at ₹13,500 per vehicle vs. ₹9,000 per vehicle QoQ due to lower contribution from Swift and Dzire as MSIL do not offer any discount on these two models. Going further, with higher proportion of diesel vehicles in its portfolio, MSIL is expected to record high net realization and bring down its average blended discount in the coming quarters.

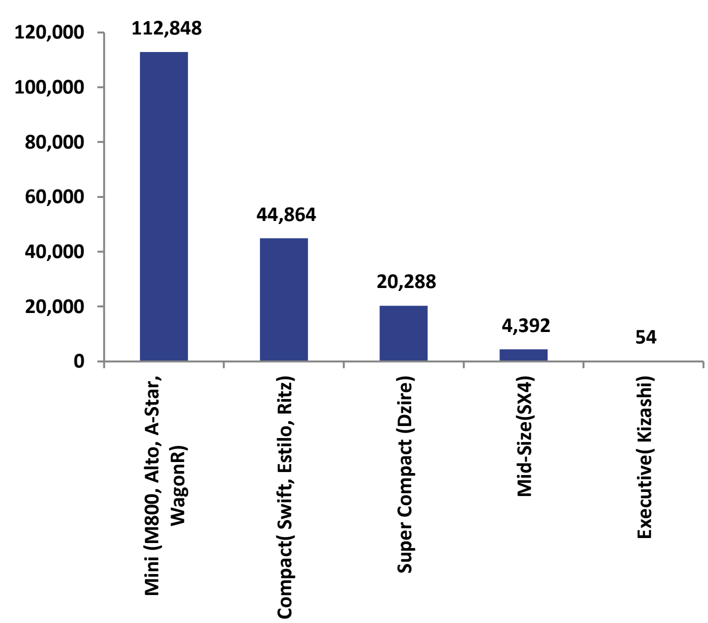
Capacity expansion



Capital expenditure to grow ~two-fold in FY12



Q2FY12 sales volume across MSIL's passenger car segment

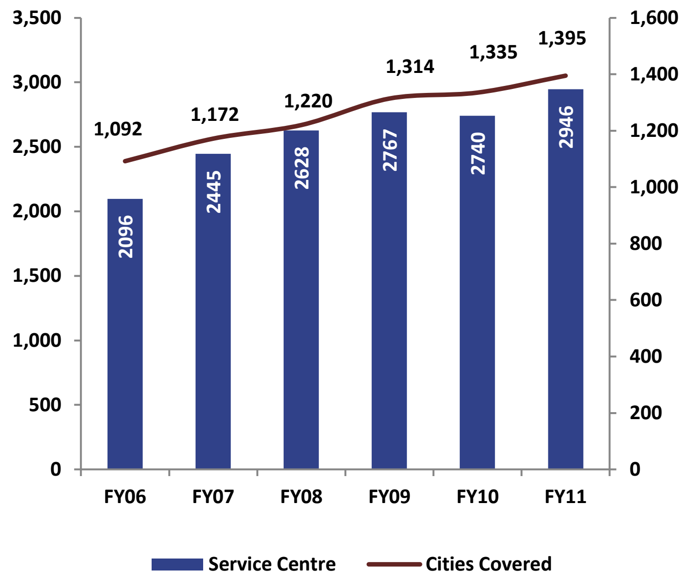


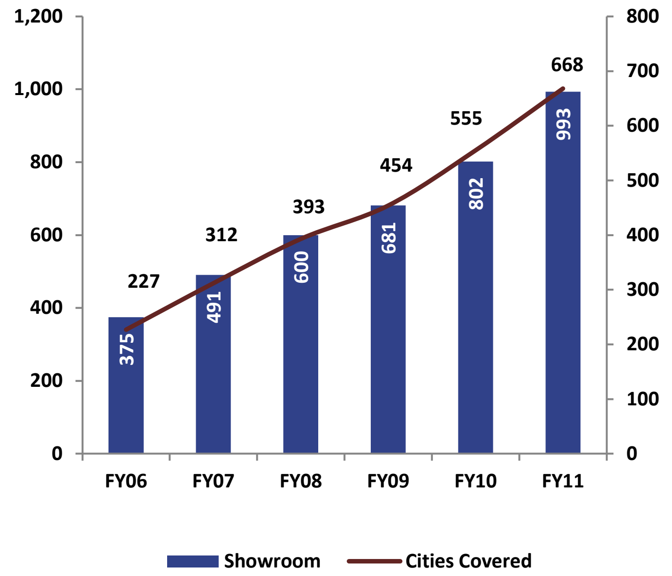
Service Center ~ an unparallel edge

Maruti is aggressively widening its sales and service network, providing the unparallel edge over its other peers. In FY'11 the company added over 191 sales outlets taking the total tally just below 1,000 marks at 993 outlets covering over 660 cities across India. It increased service outlets by 206 to 2,946 outlets in 1,395 cities. While the arch rival Hyundai motors have over 400 sales outlooks tied with 700 service networks. Over the past several years, contribution from rural sales witnessed a sequential increment, contributing over 20% to domestic sales. About 40% of MSIL's sales outlets are in the rural format, with scaled-down investment, enabling viability on lower volumes.

MSIL's network services ~1.2m vehicles a month. With an increasing service load, MSIL turned its focus to impart training and initiated tie-ups with 28 ITIs (Industrial Training Institutes) to increase technical staff at workshops.

Unparallel edge of wide sales and service network

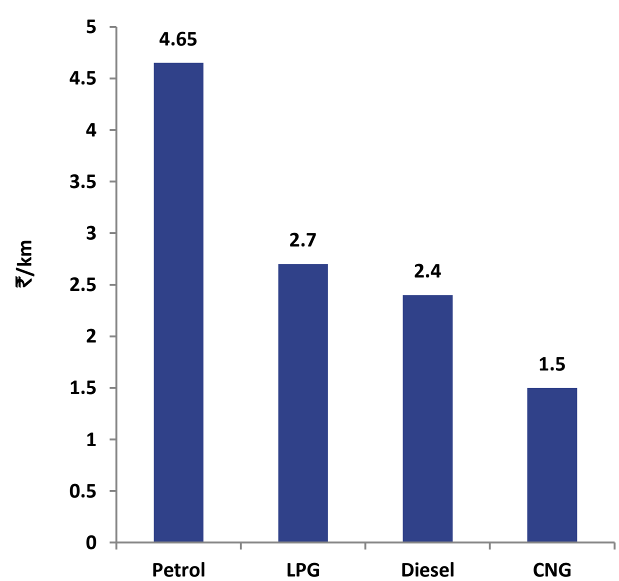




Increased focus on alternative fuel technology

To counter the ever rising fuel cost, the company has been continuously focusing on fuel efficient cars and simultaneously incorporating alternative fuel technology. Sales have risen of vehicles powered by alternative fuels due to rising petrol prices. The diesel proportion of volumes increased from 60% to over 80% among available models. Considering capacity constraints for diesel engines, MSIL will increase its diesel-engine capacity (in the SPV - Suzuki Powertrain) from 0.25m to 0.29m units. The company is focused on promoting CNG cars. It's i-GPI CNG technology delivers higher fuel efficiency than conventional CNG cars. Besides, the loss of power, compared with gasoline engine cars is negligible in the case of i-GPI, a shortcoming of conventional CNG technology. MSIL believes that once CNG availability improves in India, it could become a popular option due to its low cost and environment friendliness. MSIL also launched an LPG version of WagonR with SET (Smart Efficient Technology) and a diesel version of the SX4 with a super-turbo diesel engine.

Alternative fuel cost



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Indian Automobile Industry

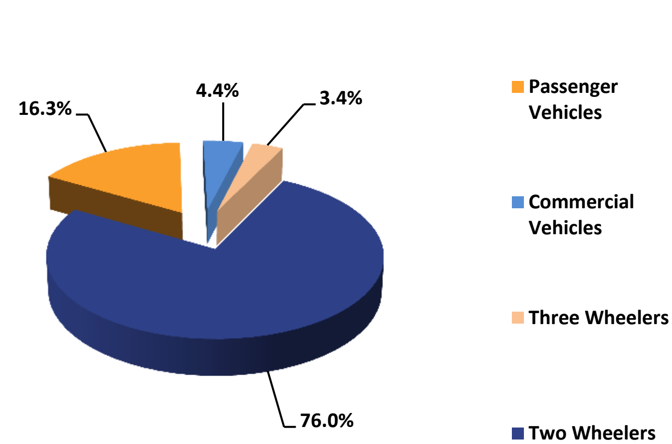
An overview of Indian Automobile Industry

The Indian automobile industry, with an estimated current turnover of ₹1,821 billion, stands out to be the seventh largest in the world, accounting for nearly 6% of the country's GDP. The sector has witnessed phenomenal growth over the last ten years, supported by a slew of new product introductions by vehicle manufacturers and growing consumer confidence. A robust transportation system plays a key role in the country's rapid economic and industrial development, and the well-developed Indian automotive industry justifies this catalytic role by manufacturing over 17.5 million vehicles and exporting about 2.33 million every year, with 76% dominance of two-wheelers in the market share of the industry.

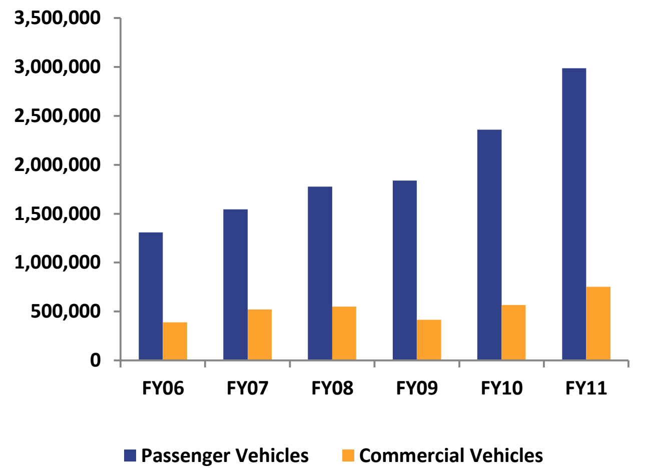
YTD sales growth moderates on rising consumer borrowing cost

In the first five months of FY12, the industry witnessed cumulative production growth of 15.92% despite persistent pressure of high finance cost, high commodity prices and high fuel prices. Meanwhile, sales growth on home ground reported sluggish at 13.26% due to rising consumer borrowing cost. During April-August 2011, the passenger vehicles segment of the country grew marginally at 1.94% while commercial Vehicles segment registered growth of 17.80%, pushed by 27.44% growth Light Commercial Vehicles sales. Three Wheelers sales recorded de-growth of 0.27% while two wheelers growth numbers fueled up to 15.94%, helped by 13.64% and 15.71% sales growth in Scooters and Motorcycles segment, respectively. At the same time, overall automobile exports rose 30.93%.

Domestic market share in FY11



5 year production trend



India pool global auto manufacturers as the favourite destination

In recent times India has emerged as one of the favorite investment destinations of global automobile manufacturers like Nissan and Ford due to the availability of trained and skilled manpower at competitive costs. French car maker, Renault SA is planning to make India an exclusive manufacturing and export hub for its sport utility vehicle, Duster. To occupy the top position in the Indian luxury segment, German auto major, Mercedes Benz is planning to introduce up to 10 new brands in the next three years in India. Meanwhile, leading luxury car brand, BMW has lined up a series of new brands to be launched in the Indian sub-continent.

Outlook

In FY11, the industry registered a turnover of ₹1821 billion, reflecting a growth of 34.2 per cent with sales of 15,513,156 units. In FY12, though some moderation in the growth rates is expected due to the successive increases in the interest rates that have made it more expensive for the customers to purchase vehicles, the Indian automobile industry is expected to clock turnover in the range of ₹2,040 billion to ₹2,100 billion, up by 12-15 per cent. As per Society of Indian Automobile Manufacturers (SIAM) the size of the domestic passenger vehicles market is likely to touch 5.6 million units by 2017, up from 2.2 million units per annum currently. The industry body, which has projected a domestic sales growth of 11-13% also, hopes to see export of 1.3 million units in the next 5 years.

Balance Sheet (Consolidated)

(₹million)	FY10A	FY11A	FY12E	FY13E
Share Capital	1,450.0	1,450.0	1,450.0	1,450.0
Reserve and surplus	116,910.0	137,230.0	157,074.2	182,263.4
Net Worth	118,360.0	138,680.0	158,524.2	183,713.4
Loan funds	8,210.0	3,090.0	7,750.0	7,750.0
Deferred Tax Liability	1,370.0	1,640.0	1,640.0	1,640.0
Capital Employed	**127,940.0**	**143,410.0**	**167,914.2**	**193,103.4**
Gross fixed assets	104,070.0	129,540.0	160,100.0	187,320.0
Less: acc. depreciation	53,820.0	63,960.0	75,170.0	88,056.7
Net Fixed assets	50,250.0	65,580.0	84,930.0	99,263.3
Capital WIP	3,880.0	4,000.0	4,500.0	4,500.0
Total Fixed Assets	54,130.0	69,580.0	89,430.0	103,763.3
Investment	71,770.0	51,070.0	51,070.0	51,070.0
Net Current Assets	2,050.0	22,760.0	27,414.0	38,270.0
Capital Deployed	**127,940.0**	**143,410.0**	**167,914.2**	**193,103.4**

Profit & Loss Account (Consolidated)

(₹million)	FY10A	FY11A	FY12E	FY13E
Operating Income	**296,230.0**	**370,400.0**	**357,691.5**	**408,311.7**
Operating Expenses	256,720.0	333,760.0	324,550.0	365,910.0
EBITDA	**39,510.0**	**36,640.0**	**33,141.5**	**42,401.7**
EBITDA Margin (%)	13.6	10.1	9.5	10.7
Depreciation	8,250.0	10,140.0	11,210.0	12,886.7
EBIT	**31,260.0**	**26,500.0**	**21,931.5**	**29,515.0**
EBIT Margins (%)	10.8	7.3	6.3	7.4
Interest	340.0	240.0	370.0	530.0
Other Income	5,000.0	4,820.0	6,000.0	6,000.0
PBT	**35,920.0**	**31,080.0**	**27,561.5**	**34,985.0**
Tax	10,950.0	8,200.0	7,717.2	9,795.8
Net Profit	**24,970.0**	**22,880.0**	**19,844.2**	**25,189.2**
Net Profit Margin (%)	8.6	6.3	5.7	6.3

Key Ratios

	FY10A	FY11A	FY12E	FY13E
EBITDA Margin (%)	13.6	10.1	9.5	10.7
EBIT Margin (%)	10.8	7.3	6.3	7.4
NPM (%)	8.6	6.3	5.7	6.3
ROCE (%)	24.4	18.5	13.1	15.3
ROE (%)	21.1	16.5	12.5	13.7
EPS (₹)	86.1	78.9	68.4	86.9
CEPS(₹)	114.6	113.9	107.1	131.3
P/E (x)	13.0	14.2	16.4	12.9
BVPS	408.1	478.2	546.6	633.5
P/BVPS (x)	2.8	2.3	2.1	1.8
EV/Operating Income (x)	1.1	0.8	0.9	0.8
EV/EBITDA (x)	8.4	8.3	9.3	7.0

Valuation

The worst seems to be over for the company, with prolonged labour problems at both Manesar and Gurgaon plant finally comes to an end, the management is confident to bring the production level back on track by December 2011, with festive season going on, the sales volumes are expected to catch on.

MSIL has a long term strategy to capitalize on the prevailing strong and steady demand for passenger vehicles in India, driven by economic growth and lower level of penetration, particularly in rural part of the country. The company's strategy to aggressively expand its capacity, increased focused on alternative fuel technology, and unparallel network of sales & service infrastructure would augurs well for the company in ensuring days.

MSIL is attractively placed at P/E of ~12.9.x FY13E. Considering the above aspects, we rate the stock as 'BUY' at the current market price of ₹1,123.

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