

Bajaj Auto

21 July 2017

Reuters: BAJA.BO; Bloomberg: BJAUT IN

Weak Operational Performance

Bajaj Auto's 1QFY18 earnings at the operating level were disappointing as lower-than-expected EBITDA margin resulted in 5% miss on the EBITDA front. EBITDA margin at 17.2% was the lowest in several years because of higher raw material costs as well as advertisement spending and expiry of excise duty benefit at Pantnagar plant. Margins at 17.2% fell 322bps YoY and 126bps QoQ. During the quarter, the company also compensated dealers for liquidation of inventory ahead of Goods and Service Tax or GST implementation which resulted in one-time expense of Rs320mn, reported as an extraordinary item. Gross margin for the quarter took a big knock because of the increase in raw material costs as gross margin fell 300bps YoY and 240bps QoQ for the quarter. The company went for a price hike in domestic and exports markets which should result in margins improving going forward. The company has given EBITDA margin guidance of 19.5%-20.0% for FY18. On the volume front, the company expects to clock 1.6mn in exports for FY18, while for three-wheelers it expects the momentum to continue because of the removal of new permit restrictions in Maharashtra clubbed with the release of new permits in Delhi along with the requirement of mandatory conversion of two-stroke vehicles to four-stroke ones in Bengaluru. In the two-wheeler segment, the company reduced its sales guidance for Avenger and V-series models. We have marginally reduced our earnings estimates by 1% for FY18/FY19 each as we factor in lower domestic volume. We have retained our existing margin guidance, which is in line with company guidance. We have also retained Accumulate rating on the stock with a revised target price of Rs3,022 (17x FY19E EPS + Rs160/share for stake in KTM subsidiary) from Rs3,117 earlier.

Higher input costs and sales promotions costs hurt margins: BAL's 1QFY18 margins were the lowest in many years as higher commodity prices as well as sales promotion costs and expiry of excise duty benefit at Pantnagar plant led to lower margins. The company, during the quarter, compensated dealers for clearing stocks because of GST, amounting to Rs320mn, which was reported as an extraordinary item. EBITDA margin at 17.2% was down 322bps YoY and 126bps QoQ. Consequently, absolute EBITDA at Rs9.6bn was down 20% YoY and 5% below our estimate. The company went for price hike during the quarter which should result in margins improving further in the coming quarters.

Expects decent exports and three-wheeler sales to do well: The company expects its three-wheeler business to do well on removal of new permit restrictions in Maharashtra clubbed with the release of new permits in Delhi along with the requirement of mandatory conversion of two-stroke vehicles to four-stroke ones in Bengaluru. Also, the company expects cargo three-wheelers to do well. The company believes that the industry will remain flat while it will register YoY growth in FY18. On the exports front, the company believes it will record export volumes of 1.6mn vehicles in FY18E as negative growth in Nigeria and Sri Lanka will be offset by traction gained in markets like Nepal, Latin America, and the Philippines.

Limited upside in stock price, retain Accumulate rating: BAL stock currently trades at 20x/17x FY18E/FY19E earnings, respectively, and in our view is fairly valued as there are no triggers for significant volume expansion in the coming quarters. We have retained Accumulate rating on BAL with a revised target price of Rs3,022 (17x FY19E EPS + Rs160/share for stake in KTM subsidiary) from Rs3,117 earlier.

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ACCUMULATE

Sector: Automobile

CMP: Rs2,815

Target Price: Rs3,022

Upside: 7%

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Key Data

Current Shares O/S (mn)	289.4
Mkt Cap (Rsbn/US\$bn)	815.3/15.4
52 Wk H / L (Rs)	3,122/2,510
Daily Vol. (3M NSE Avg.)	278,516

Price Performance (%)

	1 M	6 M	1 Yr
Bajaj Auto	(0.0)	4.3	1.7
Nifty Index	2.4	18.2	15.9

Source: Bloomberg

Y/E March (Rsmn)	1QFY16	4QFY17	1QFY18	YoY (%)	QoQ (%)
Net revenues	57,480	48,973	54,424	(5.3)	11.1
Raw material costs	38,628	33,203	38,093	(1.4)	14.7
Staff costs	2,683	2,273	2,725	1.6	19.9
Other expenses	4,405	4,438	4,222	(4.2)	(4.9)
Total expenditure	45,716	39,913	45,040	(1.5)	12.8
EBITDA	11,763	9,060	9,384	(20.2)	3.6
EBITDAM (%)	20.5	18.5	17.2	(322bps)	(126bps)
Depreciation	774.7	757.0	752.6	(2.9)	(0.6)
Interest costs	2	2	2	9.1	-
Other income	2,671	2,936	4,573	71.2	55.7
PBT	13,657	11,236	13,201	(3.3)	17.5
Extraordinary items	0	0	320	-	-
Tax	3,873	3,218	3,642	(6.0)	13.2
Net profit	9,784	8,018	9,239	(5.6)	15.2
NPM (%)	17.0	16.4	17.4	3bps	7bps
EPS (Rs)	33.8	27.7	32.8	(2.9)	18.4

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 1: Financial summary

Y/E March (Rsmn)	FY15	FY16	FY17	FY18E	FY19E
Revenues	2,11,039	2,21,517	2,13,735	2,40,847	2,74,471
YoY (%)	7.3	4.5	(3.6)	12.5	14.0
EBITDA	41,166	47,819	44,224	48,149	57,427
EBITDA (%)	19.0	21.2	20.3	19.7	20.6
Adj. PAT	31,539	39,297	38,276	41,573	48,715
YoY (%)	(13.2)	39.7	(2.6)	8.6	17.2
EPS (Rs)	109.0	135.8	132.3	143.7	168.3
RoE (%)	31.1	32.8	25.3	23.1	23.9
RoCE (%)	36.5	36.1	26.3	24.2	25.9
P/E (x)	25.9	20.8	21.3	19.6	16.7
EV/EBITDA (x)	18.3	16.6	17.0	15.2	12.5
EV/Sales (x)	3.5	3.5	3.5	3.0	2.6

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 2: Change in our earnings estimates

(Rsmn)	New estimates		Old estimates		Change (%)	
	FY18E	FY19E	FY18E	FY19E	FY18E	FY19E
Volume	40,44,076	45,27,281	40,84,103	45,70,911	(1.0)	(1.0)
Net sales	2,40,847	2,74,471	2,42,710	2,76,540	(0.8)	(0.7)
EBITDA	48,149	57,427	48,391	57,740	(0.5)	(0.5)
EBITDA margin (%)	19.7	20.6	19.6	20.5	5bps	4bps
PAT	41,573	48,715	41,751	48,942	(0.4)	(0.5)
EPS (Rs)	144	168	144	169	(0.4)	(0.5)

Source: Nirmal Bang Institutional Equities Research

Exhibit 3: Deviation of our estimates from actual performance in 4QFY17

(Rsmn)	Actual 1QFY18	Our estimate 1QFY18	Deviation %
Net sales	54,424	53,117	2.5
EBITDA	9,384	9,880	(5.0)
Net profit	9,239	8,603	7.4

Source: Nirmal Bang Institutional Equities Research

Conference-call key takeaways

Market share: The company's market share in the domestic motorcycle space shrunk during the quarter because of its compliance with BS-IV norms in the preceding quarter and the resulting rise in vehicle prices, thereby leading it to cede some market share to competitors who continued with the sale of BS-III vehicles at a big discount.

GST impact: The company incurred total expenses of Rs320mn as compensation to dealers for transition to GST. The same is accounted for as an extraordinary item. The reduction in ex-showroom prices on account of GST implementation will be in the range of Rs200-Rs6,500/motorcycle.

Exports: Revenues from exports stood at Rs24.8bn (US\$347mn) in 1QFY18 against Rs17.8bn (US\$247mn) in 4QFY17 and Rs20.1bn (US\$286mn) in 1QFY17. The average Indian rupee/US dollar exchange rate stood at Rs66.8/US\$ in the current quarter versus Rs67.1/US\$ each in 4QFY17 and 1QFY17. The company's efforts in diversifying revenues from its export market has fructified as it has reduced dependence on geographies like Sri Lanka and Nigeria with incremental volume coming from Turkey, Iran & South East Asia. The management has given guidance of achieving sales of 800,000 units in 1HFY18 while retaining its guidance of 1.6mn units for FY18. A price hike was done across its two-wheeler and three-wheeler models in July 2017.

Volume: Domestic motorcycle sales during the quarter were affected by GST implementation wherein the company reduced stocks in its network – billing for 108,000 units to factor in customers’ delaying purchases in anticipation of lower prices. KTM’s sales in India are likely to be close to 50,000 vehicles for FY18. BAL has lowered its volume guidance and is now targeting monthly run-rate for V-12 & V-15 models of close to 25,000 units/month from October 2017 against its previous guidance of 35,000-40,000 units/month. It expects to register Avenger bike sales in the range of 10,000-12,000 units/month from October 2017. Sales in the first fortnight of July 2017 have been subdued because of customers’ advance purchases in June 2017.

EBITDA margin: Destocking in June 2017 affected profitability of the motorcycle business, thereby dragging down EBITDA margin for the quarter. The company has given FY18 margin guidance in the range of 19% – 20%.

Three-wheelers: BAL currently enjoys a market share of 50% in domestic market. Its share in the petrol/diesel segments is ~90%/17%, respectively, while that in the cargo segment stands at ~33%. The company anticipates good growth in the sale of domestic three-wheelers with the removal of new permit restrictions in Maharashtra clubbed with the release of new permits in Delhi along with the requirement of mandatory conversion of two-stroke vehicles to four-stroke ones in Bengaluru. The company expects sales in the range of 20,000-21,000 units/month going forward versus an average of 17,000-18,000 units/month posted in 1QFY18.

Spare part sales: Revenues from the sale of spare parts stood at Rs6,510 (Rs4,600mn - domestic; Rs1,900-exports) against Rs6,370mn registered in 1QFY17.

New vehicle launches: BAL will not go for any new vehicle launches in the current year.

Price hike: BAL has undertaken price hikes across its two-wheeler and three-wheeler models. The increase in case of two-wheelers is in the range of Rs500-Rs1,500/vehicle and for three-wheelers it is between Rs1,500 – Rs2,000/vehicle.

Raw material prices: BAL attributed higher raw material prices (70% of sales versus 68% in the preceding quarter) to higher input cost of steel etc - contributing 1.1%, discontinuation of excise duty benefit at Pantnagar plant - contributing 0.5% and sales promotion for CT100 & Platina models in April and May 2017- contributing 0.3%. The company went for a price hike in May 2017 to cover 90% of the rise in cost.

Dealers: BAL currently has primary dealer network base of 650 dealers and 2,300 touchpoints across India.

Exhibit 4: P/E charts



Source: Nirmal Bang Institutional Equities Research

Source: Nirmal Bang Institutional Equities Research

Financials (standalone)
Exhibit 5: Income statement

Y/E March (Rsmn)	FY15	FY16	FY17	FY18E	FY19E
Net sales	2,11,039	2,21,517	2,13,735	2,40,847	2,74,471
% growth	7.3	4.5	(3.6)	12.5	14.0
Raw material costs	1,48,498	1,50,569	1,46,242	1,67,531	1,88,672
Staff costs	8,973	9,171	9,971	10,968	12,284
Other expenses	17,484	18,306	17,231	18,280	20,806
Total expenditure	1,74,955	1,78,046	1,73,443	1,96,778	2,21,762
EBITDA	41,166	47,819	44,224	48,149	57,427
% growth	0.3	16.2	(7.5)	8.9	19.3
EBITDA margin (%)	19.0	21.2	20.3	19.7	20.6
Other income	5,824	10,736	12,220	14,098	15,327
Interest costs	65	11	14	6	6
Gross profit	62,541	70,949	67,494	73,316	85,799
% growth	7.1	13.4	(4.9)	8.6	17.0
Depreciation	2,675	3,072	3,073	3,200	3,328
Profit before tax	44,250	55,473	53,356	59,041	69,421
% growth	(4.5)	25.4	(3.8)	10.7	17.6
Tax	12,711	16,177	15,081	17,468	20,706
Effective tax rate (%)	28.7	29.2	28.3	29.6	29.8
Net profit	31,539	39,297	38,276	41,573	48,715
% growth	(2.7)	24.6	(2.6)	8.6	17.2
Extraordinary items	3,403	-	-	-	-
Reported net profit	31,539	39,297	38,276	41,573	48,715
% growth	(13.2)	39.7	(2.6)	8.6	17.2
EPS (Rs)	109.0	135.8	132.3	143.7	168.3
% growth	(13.2)	39.7	(2.6)	8.6	17.2
DPS (Rs)	50.0	100.0	5.0	60.0	60.0
Payout (%)	45.9	73.6	3.8	41.8	35.6

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 7: Balance sheet

Y/E March (Rsmn)	FY15	FY16	FY17	FY18E	FY19E
Equity	2,894	2,894	2,894	2,894	2,894
Reserves	1,04,027	1,29,772	1,67,448	1,87,133	2,14,952
Net worth	1,06,920	1,32,666	1,70,341	1,90,027	2,17,845
Net deferred tax liabilities	1,416	2,028	3,136	3,136	3,136
LT liabilities/provisions	1,400	1,183	1,347	854	854
Long-term loans	1,118	1,179	1,199	1,199	1,199
Total loans	1,118	1,179	1,199	1,199	1,199
Liabilities	1,10,854	1,37,055	1,76,023	1,95,216	2,23,035
Gross block	41,009	44,349	45,332	47,332	49,332
Depreciation	21,837	24,092	25,900	29,099	32,427
Net block	19,172	20,257	19,433	18,233	16,905
Capital work-in-progress	2,549	522	422	422	422
Long-term investments	33,528	90,011	87,399	87,399	97,399
Other long-term assets	5,111	6,823	6,982	6,982	9,936
Inventories	8,142	7,191	7,284	7,495	9,294
Debtors	7,170	7,179	9,533	9,416	10,731
Cash	5,862	8,595	2,937	5,023	5,989
Cash & cash equivalents	5,751	8,176	2,798	5,023	5,989
Other bank balances	111	420	139	0	0
Liquid Investments	58,006	13,199	60,501	80,501	92,501
Other current assets	16,085	11,088	13,659	13,745	18,176
Total current assets	95,263	47,253	93,914	1,16,180	1,36,690
Creditors	25,672	26,680	30,917	32,673	36,821
Other current liabilities/provisions	19,096	1,130	1,209	1,327	1,495
Total current liabilities	44,768	27,810	32,126	34,000	38,317
Net current assets	50,495	19,443	61,788	82,180	98,373
Total Assets	1,10,855	1,37,055	1,76,023	1,95,216	2,23,035

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 6: Cash flow

Y/E March (Rsmn)	FY15	FY16	FY17	FY18E	FY19E
EBIT	40,600	55,180	53,087	58,312	67,447
(Inc.)/Dec in working capital	(5,825)	5,753	2,533	(18,424)	(15,395)
Cash flow from operations	34,775	60,932	55,620	39,888	52,052
Other income	3,814	9,514	10,439	14,098	15,327
Other expenses	692	272	164	-	-
Depreciation	2,674	3,072	3,073	3,200	3,328
Tax paid	12,854	18,195	15,026	17,468	20,706
Net cash from operations	21,473	36,568	33,392	11,522	19,347
Capital expenditure	(2,697)	(2,651)	(1,994)	(2,000)	(2,000)
Net cash after capex	18,777	33,917	31,398	9,522	17,347
Other investing activities	(1,447)	2,463	(34,889)	14,098	4,522
Cash from Financial Activities	(16,442)	(33,841)	(1,901)	(21,395)	(20,902)
Opening cash balance	4,863	5,751	8,176	2,798	5,023
Effects of exchange rate differences	-	(114)	15	-	-
Closing cash balance	5,751	8,176	2,798	5,023	5,989
Change in cash balance	888	2,425	(5,377)	2,224	966

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 8: Key ratios

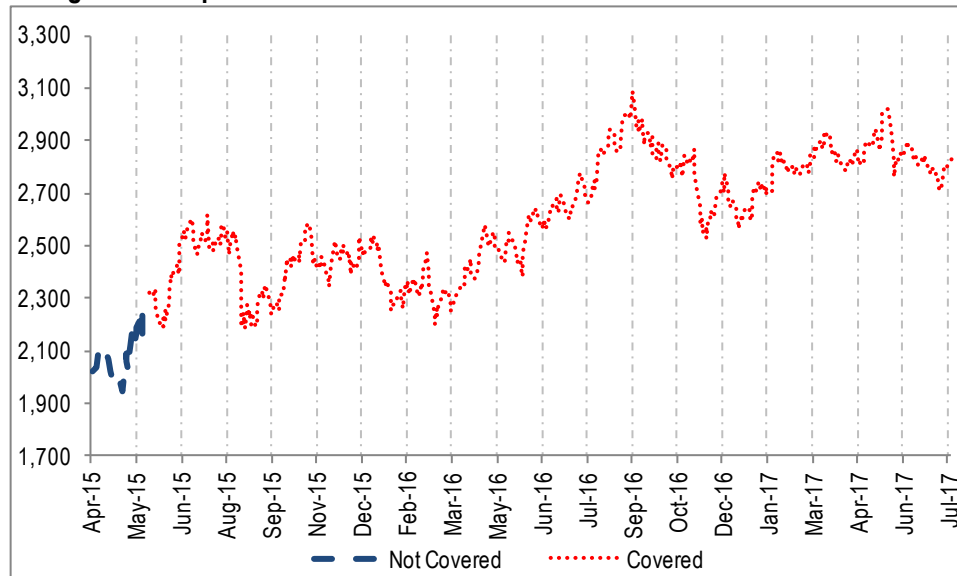
Y/E March	FY15	FY16	FY17	FY18E	FY19E
Profitability & return ratios					
EBITDA margin (%)	19.0	21.2	20.3	19.7	20.6
EBIT margin (%)	17.8	19.8	18.9	18.4	19.4
Net profit margin (%)	14.6	17.4	17.6	17.0	17.4
RoE (%)	31.1	32.8	25.3	23.1	23.9
RoCE (%)	36.5	36.1	26.3	24.2	25.9
Working capital & liquidity ratios					
Receivables (days)	13	12	14	14	14
Inventory (days)	13	13	12	11	12
Payables (days)	57	54	61	61	61
Cash conversion cycle (WC days)	(31)	(29)	(34)	(35)	(34)
Current ratio (x)	2.1	1.7	2.9	3.4	3.6
Quick ratio (x)	1.9	1.4	2.7	3.2	3.3
Valuation ratios					
EV/Sales (x)	3.5	3.5	3.5	3.0	2.6
EV/EBITDA (x)	18.3	16.6	17.0	15.2	12.5
P/E (x)	25.9	20.8	21.3	19.6	16.7
P/BV (x)	7.6	6.1	4.8	4.3	3.7

Source: Company, Nirmal Bang Institutional Equities Research

Rating track

Date	Rating	Market price (Rs)	Target price (Rs)
26 May 2015	Accumulate	2,302	2,401
27 July 2015	Accumulate	2,497	2,451
9 October 2015	Accumulate	2,431	2,451
26 October 2015	Accumulate	2,516	2,472
27 May 2016	Accumulate	2,505	2,594
29 July 2016	Accumulate	2,655	2,702
1 November 2016	Accumulate	2,884	3,042
1 February 2017	Accumulate	2,833	2,950
14 February 2017	Accumulate	2,801	3,117
19 May 2017	Accumulate	2,973	3,035
21 July 2017	Accumulate	2,815	3,022

Rating Track Graph



Disclaimer

Stock Ratings Absolute Returns

BUY > 15%

ACCUMULATE -5% to 15%

SELL < -5%

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