

# Buy

## Mahindra & Mahindra



Industry: Auto and Auto Components

Industry View: Neutral

Result Update

### “Consistent performance”

#### Q3 results in-line with our expectations

M&M's Q3FY13 revenues were robust at Rs 106bn, a growth of 27.8% yoy, and 10.2%qoq. Volumes in the quarter grew by 11% yoy and 10.8% qoq. Auto volumes have grown by 4% qoq and 18% yoy in the quarter, while FES volumes have declined by 1% yoy, while have shown a robust growth of 30% qoq. M&M's topline was mainly lifted by a 16% yoy growth in realizations which has remained in the vicinity of 20-25% over the last few quarters. This was due to favorable product mix coming from the higher sales of XUV 500 and the launch of Quanto. The growth in realizations was also in line with the price hikes of 4.5% taken YTD on the FES side and 2% in auto segment in December. Also, the company is out of the race of giving any discounts on any of its vehicles except the trucks. This has also led to a good growth in pricing, while maintaining volume growth. On profitability front, EBITDA margins slightly went down to 11.2% from 11.4% qoq and 12.2% yoy. RM to sales grew yoy to 75.9% from 74.94%qoq, while slightly reducing from 75.1% sequentially. Other expenses however have come down to 8.2% from 8.82% qoq.

Though FES volumes have slightly fallen by 1% yoy, they have firmed up sequentially by 30%, in spite of which the EBIT margins on FES side have increased to 15.5% from 14.8% qoq while remaining stable yoy, thus showing pricing power remaining in M&M's hands. Auto margins shrunk to 8.5% qoq, from 9.4%, while grew from 8.2% yoy. Depreciation expenses grew by 42% yoy, while remaining flat qoq at Rs1,789mn. Tax rate came down at 21.1%, which provided some boost to the bottomline. PAT grew by 26% yoy, while fell by 7% to Rs8.36bn.

#### Volumes to show some softness on the Auto side

The company has launched a number of products like the XUV, Quanto, Maximo van and a few tractors in FY 13. In FY 14, M&M will launch the electric car Reva and a sub 4m Verito as fresh new launches. Apart from this they will launch only refreshes and variants on the auto side. In the last one year, with the launches of new competitive products, M&M have lost market share close to 800 bps on the UV side. With new launches from competition coming up like the Ford Ecosport, Nissan Evalia, Ashok Leyland Stile along with the existing rival products like Renault Duster, Maruti Ertiga etc, M&M may have a tough time to gain back their market share. However, ramp up of capacities on the XUV side and higher demand for Quanto along with consistent performance from Bolero and Scorpio will arrest any steep decline in market share of M&M. We expect the phase by phase increase in diesel prices to impact the UV industry structurally upto some extent. We estimate the UV business of M&M to grow at 22% in FY 13E and at a slower growth of 12% in FY14E.

#### Stock Data

|                          |         |
|--------------------------|---------|
| Current Market Price (₹) | 882     |
| Target Price (₹)         | 1,019   |
| Potential upside (%)     | 16      |
| Reuters                  | MAHM.BO |
| Bloomberg                | MM IN   |

#### What's Changed

|                      |                  |
|----------------------|------------------|
| 12 month PriceTarget | ₹1,040 to ₹1,019 |
| F2013 EPS            | From ₹52 to ₹52  |
| F2014 EPS            | From ₹62 to ₹59  |

#### Key Data

|                                |           |
|--------------------------------|-----------|
| Market Cap (₹bn)               | 883       |
| 52-Week Range (₹)              | 975 / 622 |
| Avg. Daily Trading Value (₹mn) | 1,115     |
| Promoters (%)                  | 25        |
| FII Holding (%)                | 33        |
| DII Holding (%)                | 16        |
| Public & Others Holding (%)    | 25        |

| Fiscal YE         | FY11    | FY12    | FY 13E  | FY14E   |
|-------------------|---------|---------|---------|---------|
| Total sales       | 234,937 | 318,536 | 393,081 | 447,667 |
| EBITDA margins(%) | 14.7    | 11.8    | 11.5    | 12.1    |
| PAT margins(%)    | 10.8    | 8.7     | 8.1     | 8.1     |
| EPS               | 41.4    | 45.1    | 51.8    | 59.4    |
| P/E               | 21.3    | 19.5    | 17.0    | 13.0    |
| P/BV              | 5.3     | 4.4     | 3.7     | 2.9     |
| EV/EBITDA         | 13.1    | 11.9    | 9.1     | 6.8     |
| ROE%              | 24.7    | 22.8    | 22.0    | 21.3    |
| Dividend yield %  | 1.3     | 1.4     | 1.5     | 1.7     |

#### Relative Price Performance



#### One Year Indexed

| (%)          | 1 Month | 3 Months | 12 Months |
|--------------|---------|----------|-----------|
| Absolute     | (8)     | (3)      | 29        |
| BSE Relative | (7)     | (7)      | 19        |

Ashwin Patil

ashwin\_patil@lkpsec.com

+91 22 6635 1271

#### Disclaimer:

The information in this document has been printed on the basis of publicly available information, internal data and other reliable sources believed to be true and is for general guidance only. While every effort is made to ensure the accuracy and completeness of information contained, the company makes no guarantee and assumes no liability for any errors or omissions of the information. No one can use the information as the basis for any claim, demand or cause of action. LKP Securities Ltd., and affiliates, including the analyst who have issued this report, may, on the date of this report, and from time to time, have long or short positions in, and buy or sell the securities of the companies mentioned herein or engage in any other transaction involving such securities and earn brokerage or compensation or act as advisor or have other potential conflict of interest with respect to company/ies mentioned herein or inconsistent with any recommendation and related information and opinions. LKP Securities Ltd., and affiliates may seek to provide or have engaged in providing corporate finance, investment banking or other advisory services in a merger or specific transaction to the companies referred to in this report, as on the date of this report or in the past.

### FES segment may see an improvement with a good rabi crop

The company in Q3 was successful in somewhat gaining back its lost market share in the FES segment. The FES segment for M&M has seen YTD decline of about 5% which is a recovery of 200 bps as compared to 3 months back as the company is making up for the weak markets in south by north and central pockets of the country. With somewhat late recovery in monsoon, some revival in demand was seen lately along with a hike in kharif prices, thus fuelling expectations of increase in demand for tractors. A decent rabi crop has also triggered hopes of a good recovery in tractor demand in the ensuing quarters. Management has guided for a 2% industry growth for tractors in FY 13E. We expect tractor volumes to grow at 1%/5% for FY13/14E.

### Improved product mix, price hikes and softening in commodities to improve margins

EBITDA margins in the quarter came at 11.2%, which was a slight drop qoq as well as yoy mainly due to higher RM costs. Going forward, there is an expectation of RM costs softening further while other expenses may remain stable as new competitive launches may keep M&M on their toes although they will be able to cut the ad expenses as there are no major new launches coming up in the next 12 months. However, success of high margin products like XUV 500 and expectations of FES segment revival may pull up margin performance. Pricing discipline on FES segment was seen in Q3, which we expect to continue with M&M dictating the FES industry on pricing front as well. Furthermore, the company has taken a price hike of 4.5% YTD on FES side and 2% on autos in December. We expect FY13E/14E margins to come at 11.5%/12.1% respectively. M&M + MVML margins were much better at 13.5% for the quarter.

### Financial Highlights

| (₹mn)                  | Q3 FY13 | Q2 FY13 | % qoq    | Q3 FY12 | % yoy     |
|------------------------|---------|---------|----------|---------|-----------|
| Net sales              | 106,426 | 96,592  | 10.2%    | 83,272  | 27.8%     |
| Other operating income | 1,317   | 1,538   | -14.4%   | 596     | 120.9%    |
| Total income           | 107,743 | 98,130  | 9.8%     | 83,868  | 28.5%     |
| Raw material costs     | 81,791  | 73,543  | 11.2%    | 62,354  | 31.2%     |
| Employee costs         | 4,982   | 4,743   | 5.0%     | 4,497   | 10.8%     |
| Other expenses         | 8,858   | 8,654   | 2.4%     | 6,809   | 30.1%     |
| EBITDA                 | 12,113  | 11,190  | 8.2%     | 10,208  | 18.7%     |
| EBITDA margins %       | 11.2%   | 11.4%   | (20 bps) | 12.2%   | (100 bps) |
| Other income           | 742     | 3,229   | -77.0%   | 408     | 82.0%     |
| Depreciation           | 1,790   | 1,784   | 0.3%     | 1408    | 27.1%     |
| Interest expenses      | 466     | 475     | -1.9%    | 68      | 588.2%    |
| Tax                    | 2,238   | 3,142   | -28.8%   | 2519    | -11.2%    |
| Adjusted PAT           | 8,362   | 9,019   | -7.3%    | 6622    | 26.3%     |
| Adj EPS                | 13.57   | 14.64   | -7.3%    | 10.8    | 25.9%     |

|                             | Q1 FY12 | Q2 FY12 | Q3 FY12 | Q4 FY12 | Q1 FY13 | Q2 FY13 | Q3 FY13 |
|-----------------------------|---------|---------|---------|---------|---------|---------|---------|
| <b>Revenues (₹mn)</b>       |         |         |         |         |         |         |         |
| Auto                        | 38579   | 45177   | 51164   | 66137   | 62787   | 71498   | 73605   |
| FES                         | 28615   | 28260   | 32513   | 27611   | 30783   | 26534   | 34040   |
| Other                       | 205     | 246     | 249     | 196     | 170     | 151     | 144     |
| Total                       | 67399   | 73683   | 83925   | 93944   | 93739   | 98184   | 107789  |
| <b>EBIT (₹mn)</b>           |         |         |         |         |         |         |         |
| Auto                        | 4139    | 4481    | 4179    | 5759    | 5528    | 6718    | 6254    |
| FES                         | 4574    | 4325    | 5084    | 4342    | 4824    | 3921    | 5274    |
| Other                       | 21      | 21      | 36      | 31      | 40      | 34      | 12      |
| Total                       | 8734    | 8827    | 9299    | 10132   | 10392   | 10672   | 11540   |
| <b>EBIT Margins%</b>        |         |         |         |         |         |         |         |
| Auto                        | 10.7%   | 9.9%    | 8.2%    | 8.7%    | 8.8%    | 9.4%    | 8.5%    |
| FES                         | 16.0%   | 15.3%   | 15.6%   | 15.7%   | 15.7%   | 14.8%   | 15.5%   |
| Other                       | 10.1%   | 8.5%    | 14.5%   | 16.1%   | 23.5%   | 22.3%   | 8.5%    |
| Total                       | 13.0%   | 12.0%   | 11.1%   | 10.8%   | 11.1%   | 10.9%   | 10.7%   |
| <b>Volumes</b>              |         |         |         |         |         |         |         |
| Auto                        | 101997  | 121454  | 124989  | 134806  | 126029  | 141237  | 146878  |
| FES                         | 60152   | 57394   | 65754   | 52075   | 59578   | 49840   | 64800   |
| <b>Realizations(₹/unit)</b> |         |         |         |         |         |         |         |
| Auto                        | 378241  | 371970  | 409344  | 490609  | 498191  | 506230  | 501130  |
| FES                         | 475708  | 492379  | 494460  | 530214  | 516682  | 532392  | 525304  |

## Outlook and Valuation

With softer expectations on the volume front from the auto side, we are slightly cutting our volume estimates. We see improvement in FES segment albeit on a slow basis. With pricing discipline seen on the FES side with zero discounting and price hikes taken, we see margin picture improving for M&M. Also increasing sales of high margin SUVs will help the cause. Softening of RM costs and stable ad spend will result in better margins. In line with these positive factors, we believe that softening UV sales may have somewhat negative bearing on the stock. Hence, we cut our target price from Rs 1,040 to Rs 1,019. We value the company on FY 14E earnings of Rs60 at 14x times arriving at a value of Rs 843 from standalone business and Rs188 from its various subsidiaries. We maintain our BUY rating on the stock with an upside of 17% from current levels. M&M along with Tata Motors remains our preferred bet in the auto sector.

| Particulars                | Basis      | Discount | Value per share |
|----------------------------|------------|----------|-----------------|
| M&M                        | P/E (@14x) | -        | 831             |
| M&M Financial Services     | Market cap | 30%      | 69              |
| Tech Mahindra              | Market cap | 30%      | 67              |
| Mahindra Lifespaces        | Market cap | 30%      | 10              |
| Mahindra UGINE             | Market cap | 30%      | 1               |
| Mahindra Forging           | Market cap | 30%      | 1               |
| Mahindra Holiday & Resorts | Market cap | 30%      | 22              |
| Swaraj Engines             | Market cap | 30%      | 1               |
| Ssangyong                  | Market cap | 30%      | 17              |
| <b>Total</b>               |            |          | <b>1019</b>     |

## Financial Summary (Standalone)

### Income statement

| YE Mar (Rs.mn)              | FY11           | FY12           | FY 13E         | FY 14E         |
|-----------------------------|----------------|----------------|----------------|----------------|
| <b>Total Revenues</b>       | <b>234,937</b> | <b>318,536</b> | <b>393,081</b> | <b>447,667</b> |
| Raw Material Cost           | 162,639        | 234,998        | 294,811        | 333,512        |
| Employee Cost               | 14,456         | 17,018         | 19,654         | 22,383         |
| Other Exp                   | 23,789         | 29,548         | 33,412         | 37,604         |
| <b>EBITDA</b>               | <b>34,562</b>  | <b>37,708</b>  | <b>45,204</b>  | <b>54,168</b>  |
| <i>EBITDA Margin(%)</i>     | <i>14.7</i>    | <i>11.8</i>    | <i>11.5</i>    | <i>12.1</i>    |
| Other Income                | 3,095          | 4,658          | 5,300          | 5,500          |
| Depreciation                | 4,139          | 5,761          | 6,427          | 8,592          |
| Interest                    | -503           | 1628           | 2044           | 2462           |
| <b>PBT</b>                  | <b>34,021</b>  | <b>34,977</b>  | <b>42,033</b>  | <b>48,613</b>  |
| <i>PBT Margin(%)</i>        | <i>14.5</i>    | <i>11.0</i>    | <i>10.7</i>    | <i>10.9</i>    |
| Tax                         | 8,575          | 7,270          | 10,214         | 12,153         |
| <b>Adj PAT</b>              | <b>25,446</b>  | <b>27,707</b>  | <b>31,819</b>  | <b>36,460</b>  |
| Adj PAT Margins (%)         | 10.8           | 8.7            | 8.1            | 8.1            |
| Exceptional items           | 1175           | 1083           | 0              | 0              |
| <b>Reported PAT</b>         | <b>26,621</b>  | <b>28,790</b>  | <b>31,819</b>  | <b>36,460</b>  |
| <i>Rep. PAT Margins (%)</i> | <i>11.3</i>    | <i>9.0</i>     | <i>8.1</i>     | <i>8.1</i>     |

### Key Ratios

| YE Mar                          | FY11  | FY12  | FY 13E | FY 14E |
|---------------------------------|-------|-------|--------|--------|
| <b>Per Share Data (Rs)</b>      |       |       |        |        |
| Adj. EPS                        | 41.4  | 45.1  | 51.8   | 59.4   |
| CEPS                            | 50.1  | 56.3  | 62.3   | 60.0   |
| BVPS                            | 168.0 | 198.2 | 235.3  | 240.0  |
| DPS                             | 11.5  | 12.5  | 13.0   | 14.5   |
| <b>Growth Ratios(%)</b>         |       |       |        |        |
| Total revenues                  | 26.3  | 35.6  | 23.4   | 13.9   |
| EBITDA                          | 16.9  | 9.1   | 19.9   | 19.8   |
| PAT                             | 27.4  | 8.9   | 14.8   | 14.6   |
| EPS Growth                      | 27.4  | 8.9   | 14.8   | 14.5   |
| <b>Valuation Ratios (X)</b>     |       |       |        |        |
| PE                              | 21.3  | 19.5  | 17.0   | 13.0   |
| P/CEPS                          | 17.6  | 15.7  | 14.2   | 11.0   |
| P/BV                            | 5.3   | 4.4   | 3.7    | 2.9    |
| EV/Sales                        | 2.0   | 1.4   | 1.1    | 0.8    |
| EV/EBITDA                       | 13.1  | 11.9  | 9.1    | 6.8    |
| <b>Operating Ratios (Days)</b>  |       |       |        |        |
| Inventory days                  | 38.0  | 38.0  | 38.0   | 38.0   |
| Receivable Days                 | 20.2  | 19.0  | 23.0   | 24.0   |
| Payables day                    | 80.9  | 85.0  | 78.0   | 75.0   |
| Net Debt/Equity (x)             | 0.22  | 0.26  | 0.29   | 0.26   |
| <b>Profitability Ratios (%)</b> |       |       |        |        |
| ROE                             | 24.7  | 22.8  | 22.0   | 21.3   |
| Dividend payout                 | 27.7  | 27.7  | 25.1   | 24.7   |
| Dividend yield                  | 1.3   | 1.4   | 1.5    | 1.7    |

Source: Company, LKP Research

### Balance sheet

| YE Mar (Rs. mn)               | FY11           | FY12           | FY 13E         | FY 14E         |
|-------------------------------|----------------|----------------|----------------|----------------|
| <b>Equity and Liabilities</b> |                |                |                |                |
| Equity Share Capital          | 2,936          | 2,954          | 2,954          | 2,954          |
| Reserves & Surplus            | 100,198        | 118,766        | 141,545        | 167,835        |
| Total Networth                | 103,134        | 121,720        | 144,499        | 170,789        |
| Total debt                    | 29,205         | 38,536         | 48,831         | 52,655         |
| Deferred tax liabilities      | 3,544          | 5,271          | 6,000          | 6,400          |
| Current liabilities & Prov.   | 59,514         | 73,598         | 87,626         | 95,385         |
| <b>Total Liabilities</b>      | <b>195,397</b> | <b>239,125</b> | <b>286,956</b> | <b>325,229</b> |
| <b>Assets</b>                 |                |                |                |                |
| Fixed assets                  | 39,066         | 50,808         | 52,426         | 53,434         |
| Non current Invest.s          | 82,054         | 92,736         | 102,736        | 109,736        |
| Other non current assets      | 19,852         | 15,670         | 13,131         | 11,131         |
| <b>Current Assets</b>         | <b>54,427</b>  | <b>79,912</b>  | <b>118,663</b> | <b>150,456</b> |
| Cash and Bank                 | 6,146          | 11,884         | 46,458         | 67,718         |
| Inventories                   | 16,942         | 23,584         | 30,693         | 34,722         |
| Sundry Debtors                | 12,603         | 19,884         | 24,770         | 29,436         |
| Loan, Advances & others       | 8,379          | 9,310          | 11,792         | 13,430         |
| Other current assets          | 10,356         | 15,251         | 4,951          | 5,151          |
| <b>Total Assets</b>           | <b>195,398</b> | <b>239,125</b> | <b>286,956</b> | <b>325,229</b> |

### Cash Flow

| YE Mar (Rs mn)                        | FY11         | FY12          | FY13E         | FY 2014E      |
|---------------------------------------|--------------|---------------|---------------|---------------|
| PBT                                   | 34,021       | 34,977        | 42,033        | 0             |
| Depreciation                          | 4,139        | 5,761         | 6,427         | 8,592         |
| Interest                              | 725          | 1,628         | 2,044         | 2,462         |
| Chng in working capital               | 2,074        | (4,843)       | 12,021        | 255           |
| Tax paid                              | (7,725)      | (7,432)       | (10,214)      | (12,153)      |
| Other operating activities            | (3,435)      | (2,741)       | (1,470)       | 39,212        |
| CF from operations (a)                | 29,798       | 27,351        | 50,841        | 38,369        |
| Capital expenditure                   | (12,070)     | (13,404)      | (8,645)       | (3,600)       |
| Chng in investments                   | (29,709)     | (10,643)      | (10,000)      | (7,000)       |
| Other investing activities            | 4,428        | 4,682         | 0             | 0             |
| CF from investing (b)                 | (37,350)     | (19,365)      | (18,645)      | (10,600)      |
| Free cash flow (a+b)                  | (7,552)      | 7,985         | 32,196        | 27,769        |
| Equity raised/(repaid)                | 87           | 0             | 0             | 0             |
| Inc/dec in borrowings                 | 3,311        | 6,442         | 9,693         | 3,200         |
| Dividend paid (incl. tax)             | (6,223)      | (8,008)       | (9,040)       | (10,170)      |
| Other financing activities            | (587)        | (460)         | (459)         | (458)         |
| CF from financing (c)                 | (3,413)      | (2,026)       | 194           | (7,428)       |
| Net chng in cash (a+b+c)              | (10,965)     | 5,959         | 32,389        | 20,341        |
| <b>Closing cash &amp; cash equiv.</b> | <b>6,142</b> | <b>11,884</b> | <b>46,458</b> | <b>67,718</b> |

---

**Team LKP**

---

|                 |                  |             |           |                           |
|-----------------|------------------|-------------|-----------|---------------------------|
| Pratik Doshi    | Director         | 98210 47676 |           | pratik_doshi@lkpsec.com   |
| S. Ranganathan  | Head of Research | 98212 22510 | 6635 1270 | s_ranganathan@lkpsec.com  |
| Ashwin Patil    | Research Analyst | 98195 78395 | 6635 1271 | ashwin_patil@lkpsec.com   |
| Chirag Dhaifule | Research Analyst | 98679 80172 | 6635 1220 | chirag@lkpsec.com         |
| Rajeev Gupta    | Head of Sales    | 98203 07797 | 6635 1230 | rajeev@lkpsec.com         |
| Hardik Mehta    | Sales            | 98190 66569 | 6635 1246 | hardik_mehta@lkpsec.com   |
| Varsha Jhaveri  | Sales            | 93241 47566 | 6635 1296 | varsha_jhaveri@lkpsec.com |
| Hitesh Doshi    | Sales            | 93222 45130 | 6635 1281 | hitesh_doshi72@lkpsec.com |
| Bharat Shah     | Dealing          | 98337 97256 | 6635 1210 | bharat_shah@lkpsec.com    |
| Kaushik Doshi   | Dealing          | 93205 23595 |           | kaushik_doshi@lkpsec.com  |

---