



21 Dec 2017

Fundamental Report on **EQUITY**

[Bajaj Auto]



Sensex	33,779.10
Nifty	10,449.40
Action	Buy
Scrip	Bajaj Auto
Current Price	3285.00
Target Price	3915.00

Distinctly Ahead



Fundamental Outlook

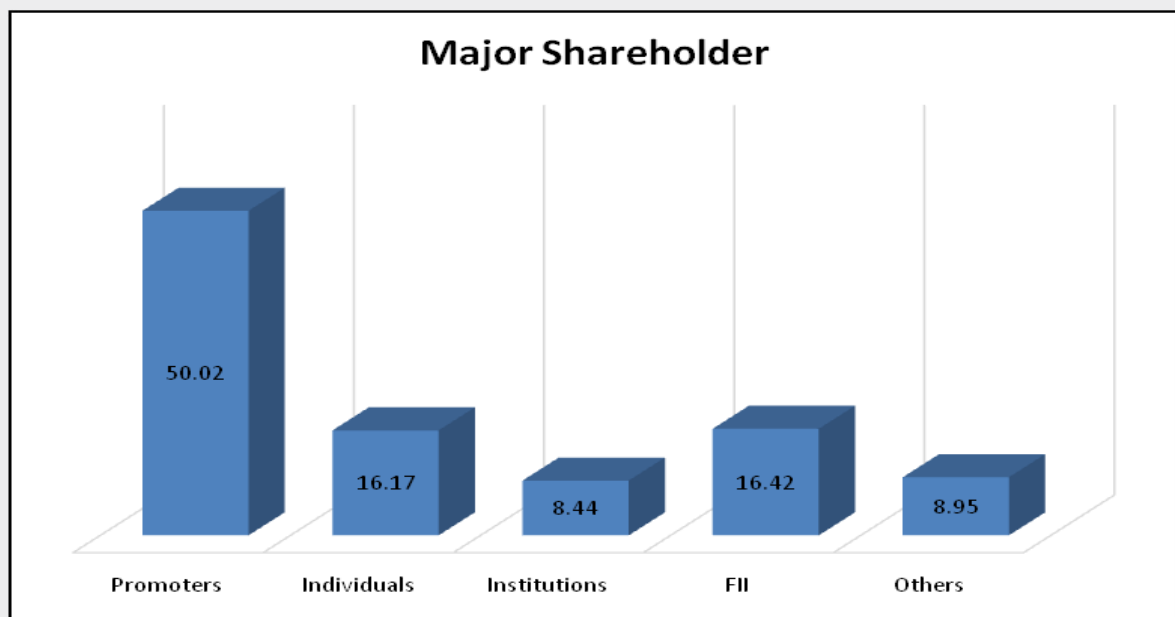
Bajaj Auto Ltd (BAL) is one of the leading two & three wheeler manufacturers in India. The company is well known for its R&D, product development, process engineering and low-cost manufacturing skills. The company is the largest exporter of two and three-wheelers in the country. The company has two subsidiaries, namely Bajaj Auto International Holdings BV and PT Bajaj Indonesia. Bajaj Auto obtained licence from the Government of India to manufacture two- and three-wheelers. In the year 1960, Bajaj Auto became a public limited company. The Company has also received Bike of the Year BBC Top gear Awards. In 2015, Bajaj Auto has introduced the all-new Platina electric start 100 cc bike to the long-distance commuter. On 8 August 2017, Bajaj Auto and Triumph Motorcycles UK announced global partnership whereby Bajaj will gain access to the iconic Triumph brand, and its great motorcycles, enabling it to offer a wider range of motorcycles within its domestic market and other international markets.

Bajaj Auto Ltd. Current market Price 3285.00 company trading at PE of 19.4x and 17.2x its FY 18E and FY 19E. According to our Valuation Bajaj Auto Ltd 3915 per share. We expect Bajaj Auto Ltd. To generate free cash flow greater than `50bn/annum in the Coming years. With no major capex around, there is considerable scope for increasing payouts. We initiate coverage on Bajaj Auto Ltd. with a BUY rating for a target price of `3,915 (upside increasing percentage around 20%).

Sensex	33,779.10
Nifty	10,449.40
Market Cap	95385.75
Book Value	589
Price to Book	5.59
Current Price	3285.00
Target Price	3915.00
Recommendation	Buy

Major shareholders

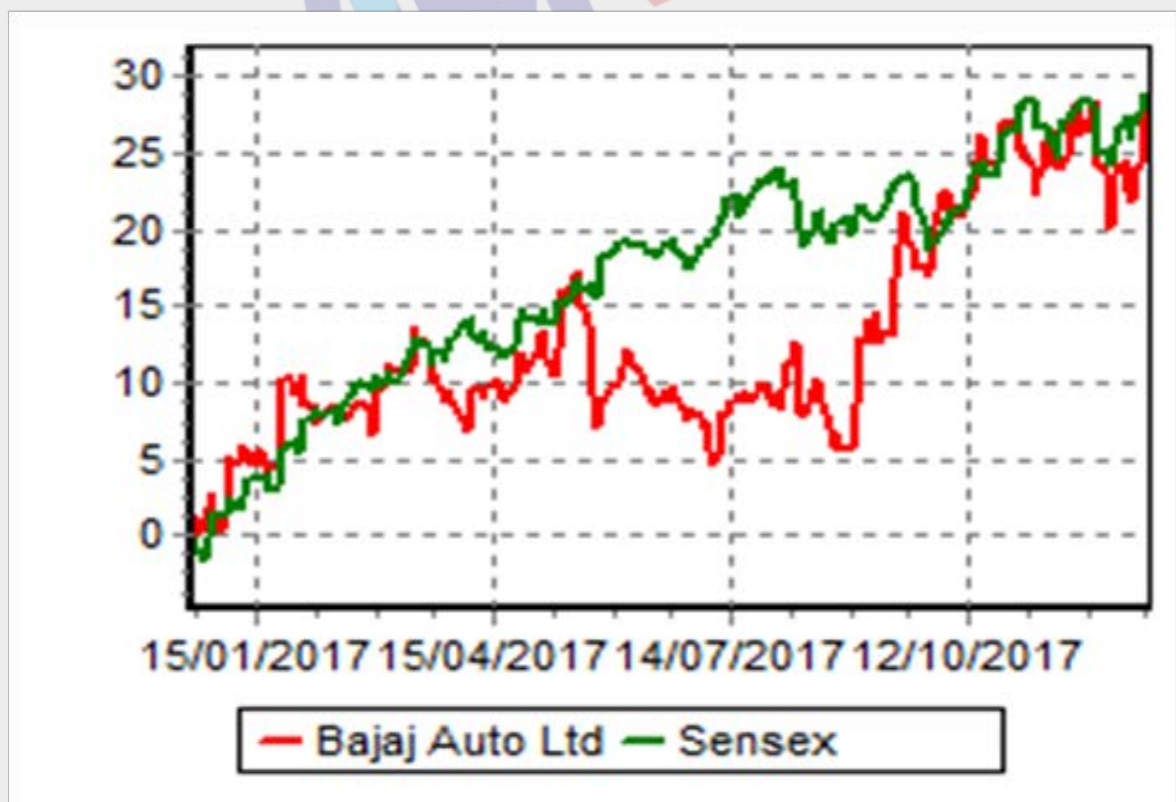
Category	Percentage
Promoters	50.02%
individual	16.17%
Institutions	8.44%
FII	16.42%
Others	8.95%



Fundamental Outlook

Estimate Change	Increase
Target price Change	Increase
Rating	Neutral

Financial & Valuation Point			
EPS	179.25	197.25	213.6
ROE	23.25	24.65	25.75
ROCE (%)	21.25	26.32	32.55
P/E	21.2x	17.2x	15.2x
EBITDA Margin	51.25	55.65	60.25
P/BV	5.1	4.6	4.1



Management Discussion

On 28 February 2017, the Central Statistical Organisation of the Government of India has pegged its advance estimate of India's real GDP growth for 2016-17 (or FY2017) at 7.1%. While better than all developed and most emerging markets of the world, including China, it was not as good as the 7.9% GDP growth achieved in FY2016. Qualitatively, the results were similar when measured in terms of gross value added (GVA) at constant prices. Real GVA growth for FY2017 is estimated at 6.7% versus 7.8% in FY2016.

There are three main reasons for this deceleration of growth. The first is insufficient investments which translate to additional income and employment. Gross fixed capital formation (GFCF) for FY2017 as a share of GDP has steadily fallen: from 31.7% in FY2015 to 31.1% in FY2016 to a low of 29.2% for FY2017.

The second has to do with the substantial overhang of non-performing loans across the banking system, especially the public sector banks. This has significantly reduced the banks' appetite for making large term loans, without which there can be no investment-led growth.

The third reason may be related to the temporary effects of demonetising Rs. 500 and Rs. 1,000 notes, which came into effect on 8 November 2016. Although the third quarter estimates (for October-December 2016) show no appreciable dip in either real GDP or GVA, there is no doubt that removing over 86% of the value of currency in circulation and substituting it with a slower injection of new notes created demand and cash constraints throughout the economy. It remains to be seen what the overall effect of this will be on growth for the second half of FY2017.

How was FY2017 for India's two-and three-wheeler industry? The market for motorcycles has continued to remain sluggish. Though domestic sales grew by 3.7% in the year, it was after a de-growth of 0.4% in the previous year. Compared to FY2015, the growth in FY2017 was a mere 1.6% per annum – from 10.7 million units two years earlier to 11.1 million in the current year. In fairness, it needs to be told that ungeared scooters have continued to do well. Leveraging urban commuter demand especially among younger women, these have grown at 11.5% in FY2017 and currently account for almost 30% of total two-wheeler domestic sales and exports.

Not surprisingly, given the sluggish growth of economy and the impact of cash shortages due to demonetisation, overall three-wheeler sales have been negatively affected: domestic sales were down by almost 5% to 511,658 units in FY2017. Exports, too, were lower on account of major depreciation of currencies of key importing nations plus the fact that many of them faced acute shortage of hard currencies. More of this is discussed in the section on exports.

In such a difficult scenario, how did Bajaj Auto Ltd. ('Bajaj Auto' or 'BAL') perform?

Sales and profits fell, but BAL continued to earn the highest operating margins in the industry and grew its net surplus by 36%. This is best seen by a quick look at the financials

Comparable Company Analysis										EPS			P/E (x)		EV / EBITDA (x)		
	Price (INR)	# of shares	Debt (INR)	Cash (INR)	Market Cap (INR)	Enterprise Value (INR)	EBITDA (INR)	Net Income (INR)	FY2017A	FY2018E	FY2019E	FY2017A	FY2018E	FY2019E	FY2017A	FY2018E	FY2019E
Automobile Sector																	
Maruti Suzuki	9716.5	302.08	483.60	23.50	2,75,839.82	2,76,299.92	10127.2	7511	248.71	270.2	295.5	39.1x	36.0x	32.9x	27.3x	19.8x	18.0x
Tata Motors	422.50	2,155	74,489.12	36,077.88	1,29,152.07	1,67,563.31	8200.23	6063.56	17.85	25.5	32.2	23.7x	16.6x	13.1x	20.4x	27.6x	59.0x
Hero Motocorp	3,785.00	199.7	247.98	195.39	68,733.17	68,785.76	4568.39	3229.29	159.87	150.8	170.35	23.7x	25.1x	22.2x	15.1x	208.9x	40.0x
TVS Motor Company	778.70	475	1,242.08	51.26	36,117.10	37,307.92	657.76	509.09	10.21	15.25	19.23	76.3x	51.1x	40.5x	56.7x	10.3x	7.9x
Eicher Motors	30,295.00	27	44.41	25.06	77,893.31	77,912.66	2243.91	1523.61	612.67	675.25	690.3	49.4x	44.9x	43.9x	34.7x	21.4x	17.0x
Mean									209.9	227.4	241.5	42.4	34.7	30.5	30.8	57.6	28.4
Median									159.9	150.8	170.4	39.1	36.0	32.9	27.3	21.4	18.0
Bajaj Auto	3,285.0	28.9	119.9	301.4	95,043.4	1,13,100.8	4,352.9	4,352.9	169.2	190.5	213.6	19.4	17.2	15.4	26.0	24.4	23.5

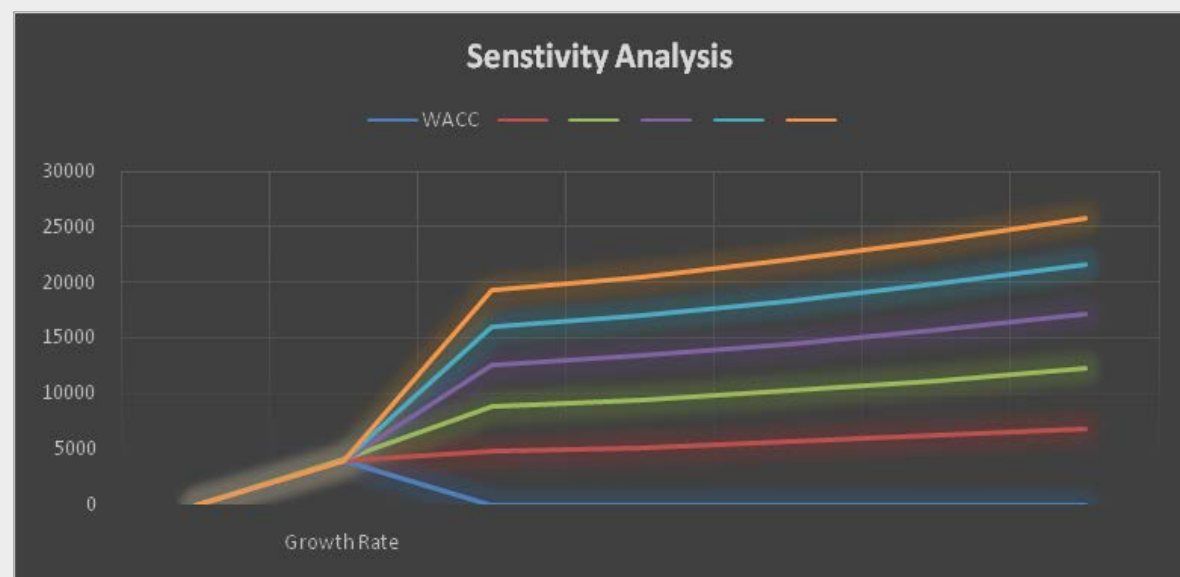
Bajaj Auto's Financial Performance for FY2017

- Net sales de-grew by 3.5% to Rs. 21,374 crore. Total operating income (net sales plus other operating income) decreased by 3.2% to Rs. 22,026 crore.
- Operating earnings before interest, taxes, depreciation and amortisation (EBITDA) reduced by 5.3% to Rs. 4,778 crore.
- The operating EBITDA margin was 21.7% of net sales and other operating income, which continues to remain the highest in the industry.
- Operating profit reduced by 5.6% to Rs. 4,470 crore.
- At 20.3%, the operating profit margin to net sales plus other operating income was also the highest in the industry.
- Profit before tax (PBT) de-grew by 3.8% to Rs. 5,336 crore.
- Profit after tax (PAT) declined by 2.6% to Rs. 3,828 crore.
- Surplus cash and cash equivalents as on 31 March 2017 was up by 36% at Rs. 12,368 crore.
- Consolidated Profit after tax remained flat at Rs. 4,079 crore.

Outlook and Valuation: The stock is trading at 15.2x FY19E earnings. We believe that a strong order book and improving margin profile will help Baja Auto Ltd.. Recommendation "BUY".

Pros: Company has reduced debt.

SENSITIVITY ANALYSIS						
WACC						
Growth Rate	3915.39	11.00%	12.00%	12.50%	13.05%	13.50%
	5.00%	4693.48	4015.44	3744.48	3485.48	3298.62
	5.50%	5077.63	4288.70	3979.03	3685.96	3476.28
	6.00%	5538.62	4607.51	4249.67	3914.88	3677.62
	6.50%	6102.04	4984.28	4565.42	4178.75	3907.72
	7.00%	6806.33	5436.40	4938.57	4486.23	4173.23



Fundamental Outlook



International Business

Bajaj Auto's international business was somewhat muted in FY2017, for reasons that have been touched upon earlier – specifically, continuing economic and political uncertainties in several importing countries, often accompanied by sharp devaluation of currencies and the inability of many to repatriate dollars because of acute currency and balance of payment crises. Consequently, motorcycle exports de-grew by 16.5%; while three-wheeler (including quadricycle) exports fell by 31.2%. In terms of US dollars, exports shrank by 23.2% to \$1.09 billion.

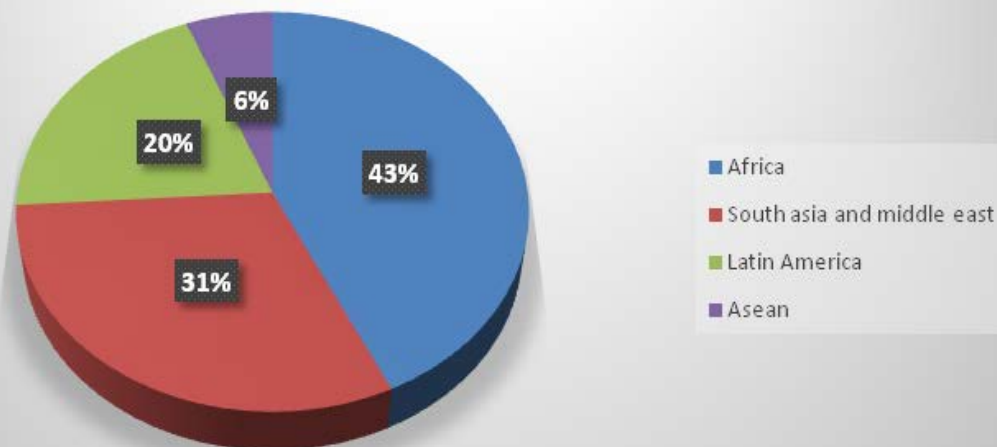
Stock Price Graph

Months	Price
21-08-2017	2764.00
21-09-2017	3075.00
21-10-2017	3218.00
21-11-2017	3242.00
21-12-2017	3285.00

Geographical spread of exports (% of Vehicles)

Country	Percentage
Africa	43%
South Asia and middle east	31%
Latin America	20%
Asian	6%

Geographical Spread



R&D

Bajaj Auto's R&D had a very productive year, helping the Company launch one product after another and meeting the new regulatory requirements. The key highlights are given below.

New Products

Dominar 400

Inspired by the stance of a lion, the distinctive design principles of the Dominar 400 are visible from the aggressive naked face to the large contoured tank. It incorporates advanced LED lighting technology, with a first of its kind, mosaic shaped, full LED headlamp with a vertical Auto Headlamp On feature.

The Dominar 400's engineering highlight is its massive perimeter frame which provides exceptional torsional rigidity and lateral strength and the wide rear tyre gives the bike a dominating look and latches on to the tarmac with superior grip.

The 373 cc, fuel injected, triple-spark four-valve DTS-i engine has been designed for a refined performance across the entire revolution band. With an enormous 35PS of power and 35Nm of torque, the Dominar 400 propels itself from 0 to 100 km/h in just 8.23 seconds. Its slipper clutch provides precise gear shifts at any rpm and a complete rider control whilst decelerating.

KTM Duke & RC

KTM models have been upgraded with several enhanced features such as optimal illumination of the near field with maximum light output, use of the latest open-cartridge technology in upside-down fork for easy maintenance, light weight, ruggedness and a broad spectrum of use for all demands – from relaxed cruising to hammering around on closed circuits.

Use of Drive-by-Wire, CAN system, LED headlamp, additional DRL features, auto lamp control based on ambient light setting and connectivity feature with Bluetooth in mobile adds to its customer friendliness.

Adjustable clutch and brake levers added to suit different persons' hand reach in Duke 390 cc and 125 cc. It comes with larger tank capacity for longer distance coverage. The models have been upgraded to meet the Euro 4 regulatory requirement.

V12

The 'neo retro' styling of the Bajaj V15 has a new sibling on the same platform. The V12 comes with an all new 125 cc, air cooled single-cylinder DTS-i engine which offers a maximum output of 10.6PS power at 7,500 rpm and a peak torque of 1.12 Kg-m at 5,500 rpm. Its power train consists of five-speed gear box. The throaty exhaust note differentiates this vehicle from others and gives it a unique character. The double cradle frame combined with 30 mm dia fork gives an edge to the handling of the bike.

Pulsar NS 160

The Pulsar NS 160 is developed on the platform of NS 150 and is powered by an all-new 160 cc oil-cooled single-cylinder engine with an improved low end torque for better drivability and generates maximum power of 15.5 PS at 8,500 rpm and maximum torque of 14.3 Nm at 6,500 rpm.

BM 125

The BM 125 is a new variant of Boxer family. This entry level commuter bike with its 124.6 cc engine, produces 9.0 PS power at 7,500 rpm and torque of 1.02 Kg-m at 5,000 rpm. It meets the customer expectations of comfort and reliability, with a strong visual appeal comprising a flat, longer and comfortable seat and round head lamp. The bike has a conventional telescopic suspension in the front and SNS suspension at the rear.

CT 125

The CT 125 is designed with tubular semi double cradle frame. Its SNS suspension is carried from the proven model of the CT 100. The 125 cc engine delivers 10PS power and solid torque of 1.02 Kg-m. It comes with additional twin shocker mounting provision and specifically built for side-car application in the Philippines. It meets the latest Euro 3 regulation of the Philippines.

Platina UG

Platina ES is upgraded to achieve 'ComforTec' with superior front and rear suspensions. The unique foam structure of the seat provides better cushioning and comfort. The pillion footrest is modified to platform type from rod type to improve pillion comfort. It is made to provide the best-in-class mileage.

Investment Rational:-

- Growth was mainly due to increase in demand for CT ES and Platina in the 100-150 cc segment.
- BAL is targeting export volumes of close to 1.7 million for FY18, growth of 21% from the previous year.
- BAL plans to launch new variant of Avenger by end of FY18 and introduce another brand in its mid-commuter segment.
- BAL's Dominar is doing 2,000 to 2,500 units per month currently in domestic market which the company plans to expand upto 6,000 unit per month.
- In exports BAL expects Dominar to achieve 7,000 to 7,500 units per month.
- Among the export markets, Nigeria market has witnessed strong revival and the company plans to export 25,000 vehicles to Nigeria which had dropped down to 7,000 units.
- BAL is looking at Australia and Thailand as new export markets. These new markets are expected to contribute about 14% to 15% of company's total exports.
- The company plans to maintain its EBITDA margins at ~20.5 to 21%.
- BAL plans to pass on the increase in input costs resulting out of hike in prices of aluminium and steel.
- BAL plans to achieve growth of 11% in its commercial vehicle segment on yoy basis.
- The company has seen increase in demand in its 3-wheeler segment on back of permits given by Maharashtra and Karnataka governments.
- BAL plans to do 30,000 vehicles per month in the CV segment by end of FY18

Discussion on DCF Valuation

- Terminal Value of the firm is calculated at FY21E end. Terminal perpetual Growth rate is assumed as 6% keeping it around GDP growth rate of India.
- DCF Valuation gives fair value of share price as Rs.3285.00 Market share price is trading below the calculated fair value (3915.00). It clearly indicates that the share is currently undervalued in the market.

Hence, Buy is recommended.

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