

AUTOMOBILES

Q2FY21 Preview

13 October 2020

Inventory buildup ahead of festive season; reduce exposure

During Q2FY21, most OEMs have built up dealer inventory on hopes of a strong revival in the upcoming festive season. With higher quarterly dispatches, we expect revenues and margins to expand on account of low-cost inventories and better operating efficiency. Our dealer checks suggest that Q2 retail sales were not very encouraging but hopes are pinned on flattish YoY festive season demand. After a sharp rally, we recommend booking profits in most OEMs. We have SELL ratings on AL, BJAUT, EIM, ESC, MM and TVSL; REDUCE on HMCL.

Mayur Milak | Nishant Chowhan, CFA
 research@bobcaps.in

Inventory built up ahead of Oct-Dec festive season: While the markets have cheered a strong revival in auto sales in Q2FY21 (primary sales from OEMs to dealers), most OEMs have built up dealer inventory – from 18-22 days as of Jun-end to 32-35 days as of Sep-end – on hopes of a strong demand revival in the upcoming festive season.

Mixed sales outlook: For Q2, we expect positive YoY revenue growth for Maruti Suzuki (MSIL), Hero Moto (HMCL), TVS Motor (TVSL), M&M (MM), Escorts (ESC), Swaraj Engines (SWE) and VST Tillers (VSTT). In contrast, we expect negative growth for Bajaj Auto (BJAUT), Eicher Motor (EIM) and Ashok Leyland (AL). Most players are likely to post stronger gross margins due to low-cost inventory and increased operating efficiencies.

Channel checks suggest YoY sales contraction: While monthly dispatches have been better than Q1, we remain cautious. Our channel checks with dealers in Rajasthan, Uttar Pradesh and Madhya Pradesh – constituting ~25% of the auto market – suggest that Q2 retail sales have not been very encouraging. Dealers pointed to significant pandemic-related stress across industries such as hotels, aviation, textiles, jewellery and mining. Agriculture demand remains strong and dealers are hoping for flattish festive period sales YoY.

Maintain cautious view: We believe stable festive sales augur well for the industry. Current inventories are not alarming and we have factored in a significant revival in demand from H2FY21 onwards. However, most auto stocks have rallied sharply in the recent past on strong dispatches and continue to be richly valued – much ahead of their long-term P/E multiples. Despite healthy festive demand expectations, we see no meaningful upside from current levels and hence recommend booking profits in most OEMs. We reiterate SELL on AL, BJAUT, EIM, MM, ESC and TVSL; HMCL remains REDUCE.

RECOMMENDATION SNAPSHOT

Ticker	Rating
APTY IN	BUY
AL IN	SELL
BJAUT IN	SELL
BIL IN	REDUCE
CEAT IN	REDUCE
EIM IN	SELL
ESC IN	SELL
HMCL IN	REDUCE
JKI IN	BUY
MM IN	SELL
MSIL IN	ADD
MDA IN	BUY
MRF IN	ADD
SWE IN	SELL
SRTY IN	BUY
TVSL IN	SELL
VSTT IN	BUY



Company-wise expectations

FIG 1 – QUARTERLY PREVIEW

Company (Rs mn)	Q2FY21E	Q2FY20	YoY (%)	Q1FY21	QoQ (%)	Remarks
Ashok Leyland						
Sales	27,985	39,925	(29.9)	6,509	329.9	AL's volumes declined 33% YoY in Q2 with MHCVs falling by a sharper 53% while LCVs were down 5%. ASPs are expected to improve 6% YoY due to BSVI transition. Overall, revenue is projected to decline 30% YoY. Lower operating efficiencies would hinder EBITDA growth – hence our EBITDA margin estimate of only 0.9%. We expect AL to post a loss of Rs 1.4bn.
EBITDA	263	2,286	(88.5)	(3,332)	NA	
Adj PAT	(1,359)	1,037	(231.1)	(3,871)	NA	
EBITDA margin (%)	0.9	5.7	-	(51.2)	-	
PAT margin (%)	(4.9)	2.6	-	(59.5)	-	
Maruti Suzuki						
Sales	197,093	169,853	16.0	41,065	380.0	Led by a 16% YoY rise in volumes, we expect 16% growth in Q2 revenues. Operating margins are forecast to expand 20bps YoY. Adj. PAT is likely to improve only 1% YoY to Rs 13.7bn given one-off lower taxes in Q2FY20. Key factors to watch are inventory levels, festive demand outlook and new launch timelines.
EBITDA	19,170	16,063	19.3	(8,634)	NA	
Adj PAT	13,668	13,586	0.6	(2,494)	NA	
EBITDA margin (%)	9.7	9.5	-	(21.0)	-	
PAT margin (%)	6.9	8.0	-	(6.1)	-	
Bajaj Auto						
Sales	72,333	77,073	(6.2)	30,792	134.9	Volumes fell 10% YoY in Q2; 3Ws were down 53% while 2Ws fell by only 2%. We expect ASPs to improve ~5% YoY, limiting the fall in revenue to 6% YoY. Operating margins are forecast to expand on the back of better gross margins and normalised production levels. Key monitorables are export market demand, domestic festive demand, inventory levels and launch timelines.
EBITDA	13,548	12,781	6.0	4,085	231.7	
Adj PAT	12,395	14,024	(11.6)	5,280	134.8	
EBITDA margin (%)	18.7	16.6	-	13.3	-	
PAT margin (%)	17.1	18.2	-	17.1	-	
Eicher Motors						
Sales	20,310	21,819	(6.9)	7,692	164.0	Revenue is expected to dip 7% YoY as Royal Enfield volumes were down 10% in Q2 while ASPs are expected to improve 3%. Despite sequential gross margin improvement (by 540bps), expected YoY contraction could drive an EBITDA margin decline of 360bps YoY to 21.4%. Adj. PAT is projected to fall 40% YoY due to one-off tax savings in Q2FY20.
EBITDA	4,344	5,460	(20.4)	12	36,100.0	
Adj PAT	3,407	5,705	(40.3)	123	2,669.9	
EBITDA margin (%)	21.4	25.0	-	0.2	-	
PAT margin (%)	16.8	26.1	-	1.6	-	
Hero MotoCorp						
Sales	86,374	75,707	14.1	29,715	190.7	We expect ASPs to rise 6% YoY given price hikes and BSVI transition even as volumes were up 7% YoY, leading to a 14% jump in revenues. Gross margins are likely to remain flattish QoQ and operating leverage benefits should kick in. Key monitorables are the response to BSVI technology, inventory levels, festive demand outlook and any vendor-side supply challenges.
EBITDA	10,997	11,011	(0.1)	1,081	917.3	
Adj PAT	7,755	9,349	(17.0)	613	1,165.1	
EBITDA margin (%)	12.7	14.5	-	3.6	-	
PAT margin (%)	9.0	12.3	-	2.1	-	
TVS Motor						
Sales	45,328	43,478	4.3	14,317	216.6	Revenues are expected to improve 4% YoY to Rs 45.3bn (volumes -2% YoY, ASPs +6%). 3Ws continue to struggle. We believe margins will return to the green as better operating efficiencies kick in. Key factors to watch for are festive demand and how fast scooter and 3W demand revives.
EBITDA	3,561	3,820	(6.8)	(466)	NA	
Adj PAT	1,575	1,790	(12.0)	(1,391)	NA	
EBITDA margin (%)	7.9	8.8	-	(3.3)	-	
PAT margin (%)	3.5	4.1	-	(9.7)	-	
Mahindra&Mahindra (MM+MVML)						
Sales	111,810	109,351	2.2	55,894	100.0	Auto volumes for MM were down 23% YoY while tractor sales picked up 30% YoY in Q2. Healthy gross margin improvement should offset higher other expenses and employee costs, leading to unchanged EBITDA margins YoY. Adj. PAT would likely be impacted due to lower other income estimated at Rs 3.5bn (vs. Rs 8.2bn in Q2FY20).
EBITDA	15,654	15,408	1.6	5,732	173.1	
Adj PAT	9,801	13,548	(27.7)	389	2,419.5	
EBITDA margin (%)	14.0	14.1	-	10.3	-	
PAT margin (%)	8.8	12.4	-	0.7	-	

Company (Rs mn)	Q2FY21E	Q2FY20	YoY (%)	Q1FY21	QoQ (%)	Remarks
Escorts						
Sales	14,792	13,239	11.7	10,616	39.3	Tractor volumes rose 24% YoY while we expect construction and railway revenue to decline, leading to overall revenue growth of 12% YoY. A gradual increase in utilisation (close to 100% in Sep) should aid better margins, supported by softer RM prices. We expect margins to rise 360bps YoY. Key factors to watch are the supply chain situation and Kubota deal updates.
EBITDA	1,952	1,267	54.1	1,196	63.2	
Adj PAT	1,434	1,138	26.0	922	55.5	
EBITDA margin (%)	13.2	9.6	-	11.3	-	
PAT margin (%)	9.7	8.6	-	8.7	-	
Swaraj Engines						
Sales	2,779	2,227	24.8	1,170	137.5	We expect SWE to capture ~35% of M&M tractor sales and clock revenue growth of ~25% YoY during Q2. With better gross margins and higher operating efficiencies, we model for EBITDA margins of 14.5%, up 100bps YoY. Key factors to watch are demand outlook and market share gains.
EBITDA	404	300	34.7	129	213.2	
Adj PAT	287	254	13.0	78	267.9	
EBITDA margin (%)	14.5	13.5	-	11.0	-	
PAT margin (%)	10.3	11.4	-	6.7	-	
VST Tillers						
Sales	2,109	1,609	31.1	1,462	44.3	Since restrictions were imposed on tiller imports from China, VSTT has witnessed a sharp jump in tiller demand. The company continues to see strong demand in tractors too. We expect higher volumes to assist 31% YoY growth in revenues. Key monitorables are newer subsidy announcements which could further escalate the demand for tillers.
EBITDA	238	39	510.3	164	45.1	
Adj PAT	207	64	223.4	171	21.1	
EBITDA margin (%)	11.3	2.4	-	11.2	-	
PAT margin (%)	9.8	4.0	-	11.7	-	
Apollo Tyres						
Sales	39,000	39,858	(2.2)	28,734	35.7	We have factored the OEM demand for various segments and a steady growth in the replacement market to arrive at APTY's quarterly revenues. With crude costs being at their lowest during the quarter, we expect gross margins to improve for most tyre companies. Steady natural rubber prices, higher volumes and lower imports will all assist margins.
EBITDA	5,292	4,320	22.5	2,373	123.0	
Adj PAT	761	831	(8.4)	(1,346)	NA	
EBITDA margin (%)	13.6	10.8	-	8.3	-	
PAT margin (%)	2.0	2.1	-	(4.7)	-	
Balkrishna Industries						
Sales	12,130	10,712	13.2	9,287	30.6	We assume tonnage volumes will increase 8% YoY with ASPs improving by 5%, leading to a 13% YoY increase in revenues. Operating margins are expected to expand 560bps YoY supported by better gross margins. Adj. PAT is forecast to fall 15% given a one-off tax adjustment in Q2F20.
EBITDA	3,707	2,675	38.6	2,306	60.8	
Adj PAT	2,471	2,910	(15.1)	1,218	102.9	
EBITDA margin (%)	30.6	25.0	-	24.8	-	
PAT margin (%)	20.4	27.2	-	13.1	-	
CEAT						
Sales	17,000	16,453	3.3	10,665	59.4	CEAT stands to benefit from a healthy demand uptick in 2Ws and is expected to post a 3% YoY rise in revenues. EBITDA margins are projected to improve marginally by 60bps while adj. PAT could fall 7% YoY due to higher interest and depreciation. Key factors to monitor are management's views on demand, direction of RM prices and any increase in product prices.
EBITDA	1,874	1,708	9.7	992	88.9	
Adj PAT	622	667	(6.7)	71	776.1	
EBITDA margin (%)	11.0	10.4	-	9.3	-	
PAT margin (%)	3.7	4.1	-	0.7	-	
JK Tyre						
Sales	20,000	21,550	(7.2)	11,308	76.9	Baking in OEM demand for various segments and steady growth in the replacement market, we expect revenue to dip 7% YoY given a higher dependence on the CV segment. Gross margins are likely to improve sequentially due to lower crude and natural rubber prices. However, Adj. PAT remains affected by one-off tax adjustment in Q2FY20, leading to 96% YoY fall.
EBITDA	2,320	2,964	(21.7)	(38)	NA	
Adj PAT	86	2,180	(96.1)	(1,713)	NA	
EBITDA margin (%)	11.6	13.8	-	(0.3)	-	
PAT margin (%)	0.4	10.1	-	(15.1)	-	
MRF						
Sales	39,000	39,476	(1.2)	24,306	60.5	We assume volumes will rise ~5% YoY in the replacement channel which should partially offset the sharp fall in MHCV OEM sales, limiting the revenue decline to 1% YoY. Operating
EBITDA	6,546	5,408	21.0	3,315	97.5	
Adj PAT	2,699	2,204	22.5	171	1,478.4	

Company (Rs mn)	Q2FY21E	Q2FY20	YoY (%)	Q1FY21	QoQ (%)	Remarks
EBITDA margin (%)	16.8	13.7	-	13.6	-	argins are expected to expand 310bps on the back of lower
PAT margin (%)	6.9	5.6	-	0.7	-	RM cost and higher capacity utilisation.
TVS Srichakra						
Sales	5,669	5,451	4.0	2,065	174.5	Given higher exposure to 2W segment tyres, we expect TVSS to grow ahead of peers and clock 4% YoY revenue growth.
EBITDA	787	604	30.3	(161)	NA	Healthy gross margin improvement of 140bps YoY and
Adj PAT	358	203	76.4	(354)	NA	operating leverage benefits should aid EBITDA margin
EBITDA margin (%)	13.9	11.1	-	(7.8)	-	expansion of 280bps YoY. Adj. PAT is expected to jump 76%
PAT margin (%)	6.3	3.7	-	(17.1)	-	YoY supported by a lower tax rate.
Minda Corp						
Sales	5,250	1,373	282.4	1,780	194.9	Strong growth in OEM production, especially 2Ws, will benefit MDA, aiding sharp recovery in quarterly revenues QoQ. With
EBITDA	551	684	(19.4)	(203)	NA	higher operating efficiencies, we expect EBITDA margins of
Adj PAT	276	372	(25.8)	(364)	NA	10.5% (lossmaking plastic division hived off). We also model for
EBITDA margin (%)	10.5	49.8	-	(11.4)	-	a sharp recovery in adj. PAT QoQ.
PAT margin (%)	5.3	27.1	-	(20.4)	-	

Source: Company, BOBCAPS Research

FIG 2 – Q2FY21 VOLUME SNAPSHOT

Company	Q2FY21	Q2FY20	YoY (%)	Q1FY21	QoQ (%)
Ashok Leyland	19,444	28,938	(32.8)	2,394	712.2
HCVs	7,936	16,815	(52.8)	755	951.1
LCVs	11,508	12,123	(5.1)	1,639	602.1
Atul Auto	4,152	12,259	(66)	1,477	181.1
Three-Wheelers	4,152	12,259	(66.1)	1,477	181.1
Bajaj Auto	1,053,337	1,173,591	(10.2)	443,103	137.7
Motorcycles	964,465	984,240	(2.0)	399,929	141.2
3Ws	88,872	189,351	(53.1)	43,174	105.8
Exports (of above)	479,751	544,511	(11.9)	251,840	90.5
Eicher Motors	158,686	178,229	(11.0)	59,307	167.6
RE	150,519	166,859	(9.8)	57,178	163.2
VECV	8,167	11,370	(28.2)	2,129	283.6
Escorts	24,441	21,051	16.1	18,150	34.7
Hero MotoCorp	1,814,683	1,691,420	7.3	563,426	222.1
Mahindra & Mahindra	185,270	191,390	(3.2)	95,308	94.4
Auto	92,024	119,570	(23.0)	29,651	210.4
Tractors	93,246	71,820	29.8	65,657	42.0
Maruti Suzuki	393,130	338,317	16.2	76,599	413.2
Domestic	370,619	312,519	18.6	67,027	452.9
Exports	22,511	25,798	(12.7)	9,572	135.2
TVS Motor	867,834	885,832	(2.0)	267,563	224.3
2Ws	834,346	842,439	(1.0)	256,058	225.8
3Ws	33,488	43,393	(22.8)	11,505	191.1

Source: Companies, BOBCAPS Research

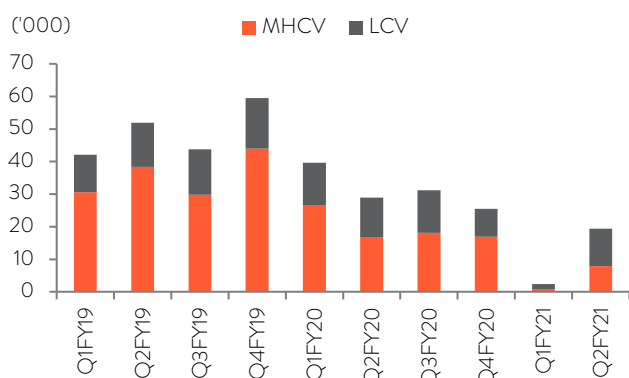
FIG 3 – COMMODITY AND CURRENCY QUARTERLY TRENDS

	Q1FY19	Q2FY19	Q3FY19	Q4FY19	Q1FY20	Q2FY20	Q3FY20	Q4FY20	Q1FY21	Q2FY21
Key Commodities (USD)										
Aluminium	2,264	2,054	1,966	1,862	1,794	1,765	1,756	1,691	1,501	1,704
QoQ (%)	18.8	(9.3)	(4.3)	(5.3)	(3.7)	(1.6)	(0.5)	(3.7)	(11.2)	13.5
Lead	2,384	2,097	1,966	2,034	1,883	2,029	2,042	1,843	1,679	1,875
QoQ (%)	10.6	(12.0)	(6.2)	3.5	(7.4)	7.7	0.6	(9.8)	(8.9)	11.7
Brent oil	75	75	68	63	69	62	63	51	31	43
QoQ (%)	48.7	1.0	(10.1)	(6.8)	8.5	(9.7)	1.2	(19.2)	(37.9)	35.8
Rubber (RS4) (Rs)	12,382	13,071	12,357	12,565	13,899	14,265	12,749	13,423	12,066	13,088
QoQ (%)	(5.4)	5.6	(5.5)	1.7	10.6	2.6	(10.6)	5.3	(10.1)	8.5
Hot rolled steel	4,168	4,300	3,926	3,802	3,949	3,793	3,720	3,602	3,550	3,928
QoQ (%)	28.7	3.2	(8.7)	(3.2)	3.8	(3.9)	(1.9)	(3.2)	(1.4)	10.6
Cold rolled steel	4,606	4,788	4,535	4,313	4,326	4,292	4,307	4,257	3,947	4,480
QoQ (%)	21.4	4.0	(5.3)	(4.9)	0.3	(0.8)	0.4	(1.2)	(7.3)	13.5
Key Currencies										
INR/USD	67.1	70.1	72.1	70.5	69.6	70.3	71.2	72.4	75.9	74.4
QoQ (%)	4.0	4.5	2.9	(2.2)	(1.3)	1.1	1.3	1.6	4.9	(2.0)
INR/EUR	79.9	81.5	82.3	80.1	78.2	78.2	78.9	79.9	83.6	86.9
QoQ (%)	12.4	2.1	0.9	(2.6)	(2.4)	0.1	0.9	1.2	4.7	3.9
INR/GBP	91.2	91.4	92.8	91.7	89.4	86.7	91.7	92.7	94.2	96.1
QoQ (%)	10.5	0.2	1.5	(1.1)	(2.5)	(3.0)	5.7	1.1	1.6	1.9
INR/JPY	0.6	0.6	0.6	0.6	0.6	0.7	0.7	0.7	0.7	0.7
QoQ (%)	5.8	2.4	1.6	0.1	(1.1)	3.7	(0.1)	1.5	6.1	(0.7)
USD/EUR	1.2	1.2	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.2
QoQ (%)	8.2	(2.4)	(1.9)	(0.4)	(1.1)	(1.0)	(0.4)	(0.4)	(0.1)	6.1
USD/GBP	1.4	1.3	1.3	1.3	1.3	1.2	1.3	1.3	1.2	1.3
QoQ (%)	6.3	(4.2)	(1.3)	1.3	(1.3)	(4.1)	4.5	(0.6)	(3.0)	4.1

Source: Bloomberg, BOBCAPS Research

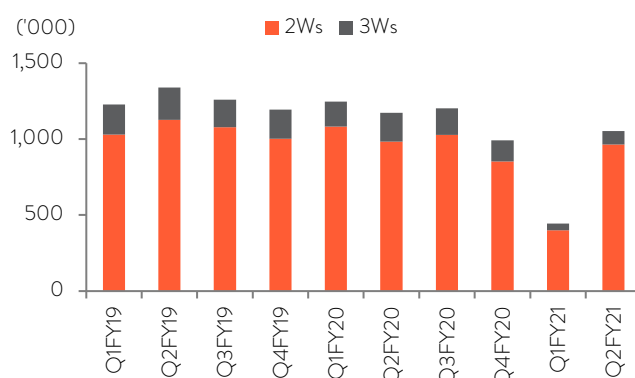
Quarterly volume trends

FIG 4 – ASHOK LEYLAND



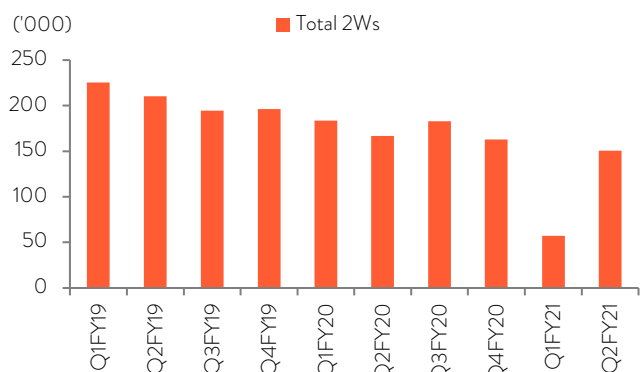
Source: Companies, BOBCAPS Research

FIG 5 – BAJAJ AUTO



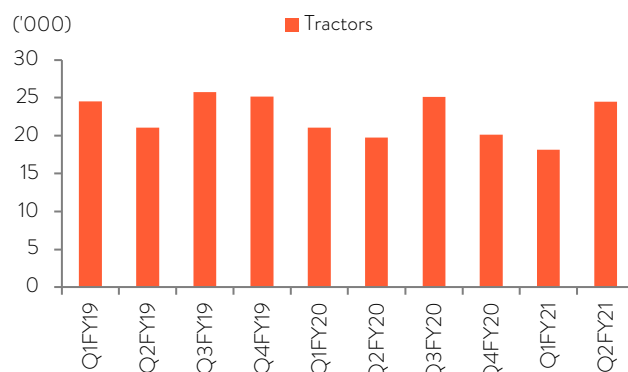
Source: Companies, BOBCAPS Research

FIG 6 – ROYAL ENFIELD



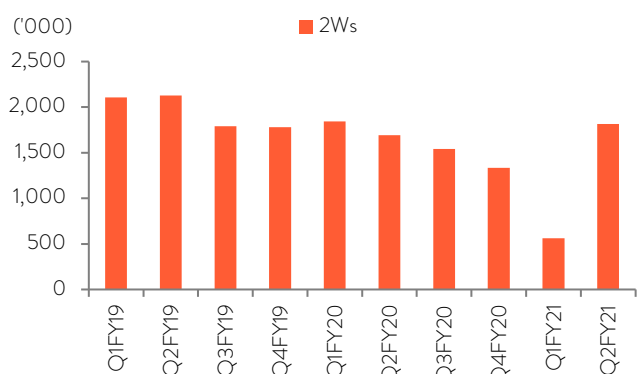
Source: Companies, BOBCAPS Research

FIG 7 – ESCORTS



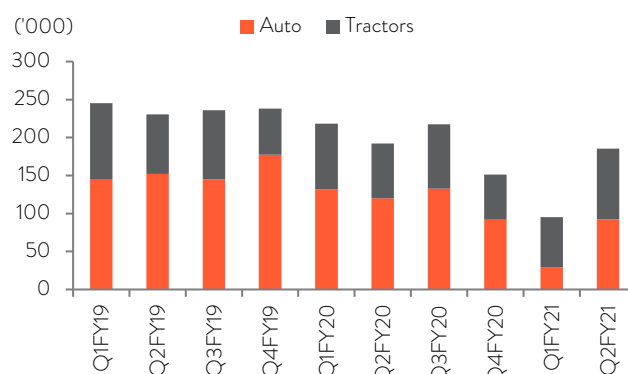
Source: Companies, BOBCAPS Research

FIG 8 – HERO MOTOCORP



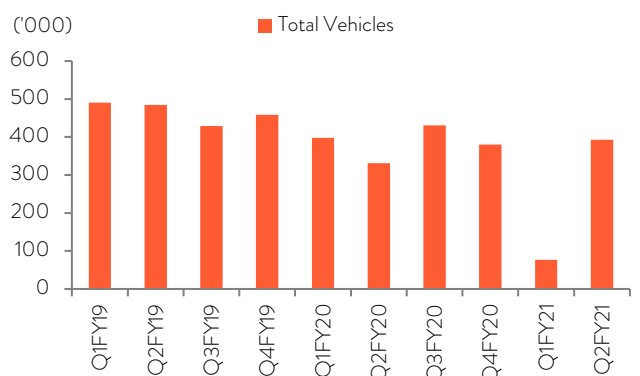
Source: Companies, BOBCAPS Research

FIG 9 – MAHINDRA & MAHINDRA



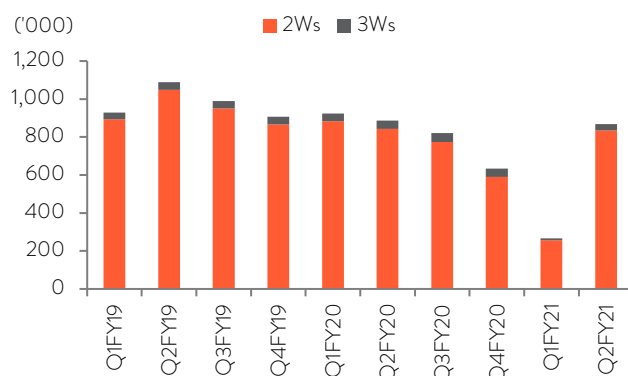
Source: Companies, BOBCAPS Research

FIG 10 – MARUTI SUZUKI



Source: Companies, BOBCAPS Research

FIG 11 – TVS MOTOR



Source: Companies, BOBCAPS Research

Disclaimer

Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

ADD – Expected return from >+5% to +15%

REDUCE – Expected return from -5% to +5%

SELL – Expected return <-5%

Note: Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

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