

SELL

TP: Rs 510 | ▼ 15%

**MAHINDRA &
MAHINDRA**

Automobiles

08 August 2020

Tractors save the day; valuations rich – maintain SELL

M&M's (MM) Q1FY21 revenues dropped 56% YoY to Rs 56bn, EBITDA declined 68% to Rs 5.7bn and PAT nosedived 96% to Rs 389mn. Though tractor performance was healthy, the auto segment remains a drag. We expect MM's tractor/auto segments to log a volume CAGR of 5%/1% over FY20-FY23, with EBITDA margins reviving to 14% levels from FY22. Rolling valuations forward, we move to a revised Sep'21 SOTP- based TP of Rs 510 (from Rs 480), valuing the core business at 13x Sep'22E EPS. Maintain SELL.

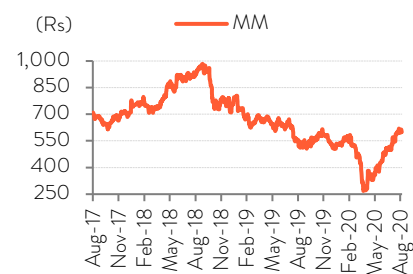
 Mayur Milak | Nishant Chowhan, CFA
 research@bobcaps.in

Dull quarter as expected: Revenues for MM+MVML dropped 56% YoY to Rs 56bn, in line with estimates. Lower RM cost/sales was more than offset by operating inefficiencies due to weak volumes, resulting in an EBITDA decline of 68% YoY to Rs 5.7bn (Rs 8.1bn est.) and EBITDA margin of 10.3% (-370bps YoY, -330bps QoQ). A significant jump in interest burden and fall in other income further dented PAT, which came in at Rs 389mn, down 96% YoY.

Ticker/Price	MM IN/Rs 600
Market cap	US\$ 10.0bn
Shares o/s	1,242mn
3M ADV	US\$ 50.0mn
52wk high/low	Rs 626/Rs 245
Promoter/FPI/DII	20%/34%/24%

Source: NSE

Strong tractor performance but auto remains a drag: We expect MM's tractor segment to witness 4% YoY volume growth in FY21 and post a 5% CAGR over FY20-FY23. However, the pain in its auto segments – UVs, CVs and 3Ws – will continue to mar the overall picture. We model for a mere 1% volume CAGR in the auto business through to FY23.

STOCK PERFORMANCE

Source: NSE

Maintain SELL: We estimate a 4% revenue CAGR for MM over FY20-FY23 coupled with expansion in operating margins, supporting higher 9% earnings growth. Rolling valuations forward, we have a revised Sep'21 TP of Rs 510 (vs. Rs 480 for Mar'21), wherein we value MM at 13x one-year forward core EPS and assign a 30% hold-co discount for subsidiaries. Maintain SELL as we find current valuations rich at 17x FY22E core EPS (adj. for value of subsidiaries).

KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue (Rs mn)	528,482	448,655	379,868	463,238	511,660
EBITDA (Rs mn)	75,301	63,506	49,466	65,415	73,572
Adj. net profit (Rs mn)	54,239	35,509	29,918	40,535	45,525
Adj. EPS (Rs)	43.7	28.6	24.1	32.6	36.7
Adj. EPS growth (%)	29.5	(34.5)	(15.7)	35.5	12.3
Adj. ROAE (%)	16.6	10.2	8.4	10.6	11.1
Adj. P/E (x)	13.8	21.0	24.9	18.4	16.4
EV/EBITDA (x)	9.6	11.1	14.3	11.0	9.8

Source: Company, BOBCAPS Research

BOB Capital Markets Ltd is a wholly owned subsidiary of Bank of Baroda

Important disclosures, including any required research certifications, are provided at the end of this report.



FIG 1 – QUARTERLY PERFORMANCE – MM+MVML

Y/E Mar (Rs mn)	Q1FY21	Q1FY20	YoY (%)	Q4FY20	QoQ (%)
Net Revenues	55,894	128,055	(56.4)	90,046	(37.9)
Raw Materials	36,240	86,971	(58.3)	57,898	(37.4)
% of Net Sales	64.8	67.9	-	64.3	-
Personnel	7,704	8,679	(11.2)	7,127	8.1
% of Net Sales	13.8	6.8	-	7.9	-
Manufacturing & Other Exp	6,219	14,469	(57.0)	12,748	(51.2)
% of Net Sales	11.1	11.3	-	14.2	-
Total Expenditure	50,163	110,119	(54.4)	77,773	(35.5)
EBITDA	5,732	17,936	(68.0)	12,273	(53.3)
EBITDA Margin (%)	10.3	14.0	-	13.6	-
Depreciation	5,813	5,839	(0.4)	6,172	(5.8)
EBIT	(81)	12,097	(100.7)	6,102	(101.3)
Interest Expenses	768	302	154.6	359	114.2
Non-operating income	1,338	1,919	(30.3)	3,155	(57.6)
Extraordinary Expenses/ (Income)	(288)	(13,671)	NA	35,776	NA
PBT	777	27,384	(97.2)	(26,878)	(102.9)
Tax-Total	99	4,787	(97.9)	5,673	(98.3)
Tax Rate (%) - Total	12.7	17.5	(27.2)	(21.1)	-
Reported PAT	678	22,597	(97.0)	(32,551)	(102.1)
Adj. PAT	389	8,927	(95.6)	3,225	(87.9)

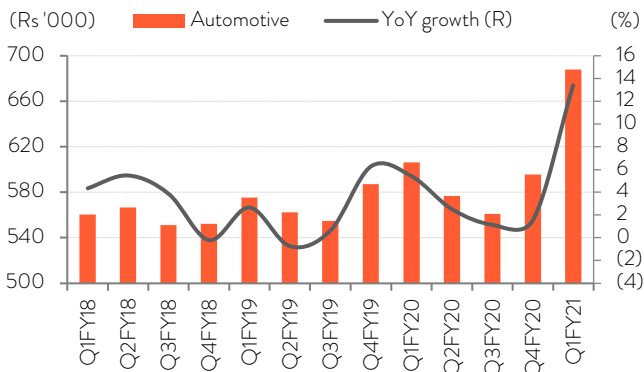
Source: Company, BOBCAPS Research

FIG 2 – SEGMENTAL PERFORMANCE – MM+MVML

Y/E Mar (Rs mn)	Q1FY21	Q1FY20	YoY (%)	Q4FY20	QoQ (%)
Segment Revenue					
Automotive Segment	20,395	79,858	(74.5)	55,058	(63.0)
Farm Equipment Segment	33,408	43,822	(23.8)	31,110	7.4
Other Segments	2,205	5,229	(57.8)	4,518	(51.2)
(Less) Inter-segment revenues	114	854	(86.7)	639	(82.2)
Total	55,894	128,055	(56.4)	90,046	(37.9)
Segment Results (After Exceptional Item)					
Automotive Segment.	(6,192)	5,180	NA	2,253	NA
Farm Equipment Segment	6,823	8,447	(19.2)	5,488	24.3
Other Segments	(54)	285	NA	89	NA
Total	577	13,913	(95.9)	7,831	(92.6)
EBIT Margins (%)					
Automotive Segment.	(30.4)	6.5	-	4.1	-
Farm Equipment Segment	20.4	19.3	-	17.6	-
Other Segments	(2.4)	5.5	-	2.0	-

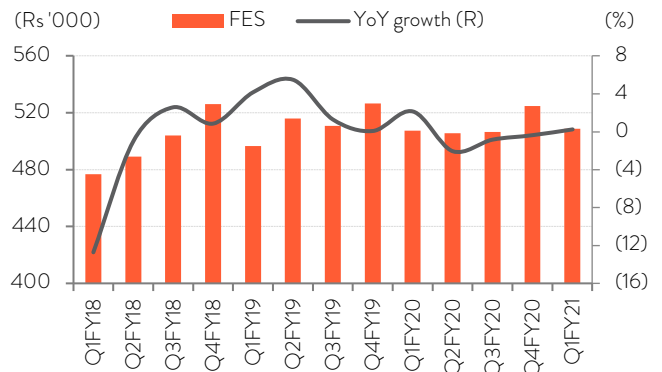
Source: Company, BOBCAPS Research

FIG 3 – AVERAGE SELLING PRICE (ASP) –AUTOMOTIVE



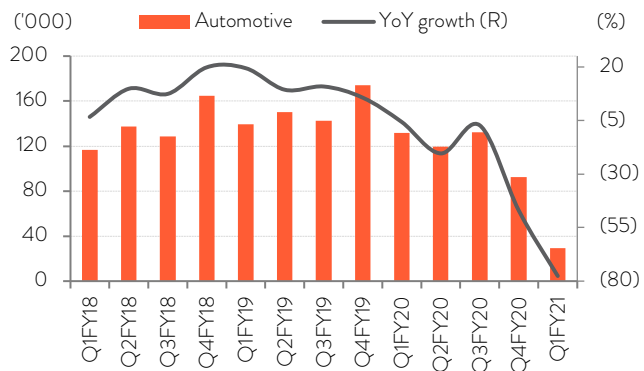
Source: Company, BOBCAPS Research

FIG 4 – AVERAGE SELLING PRICE (ASP) – FES



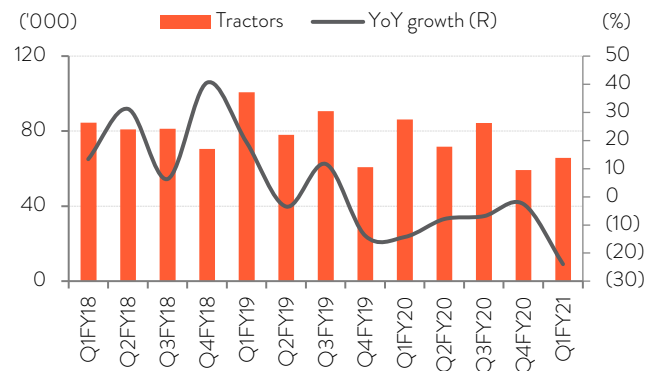
Source: Company, BOBCAPS Research

FIG 5 – VOLUME GROWTH – AUTOMOTIVE



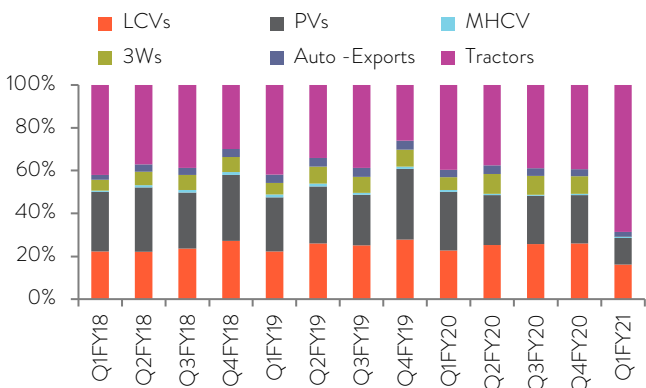
Source: Company, BOBCAPS Research

FIG 6 – VOLUME GROWTH – FES



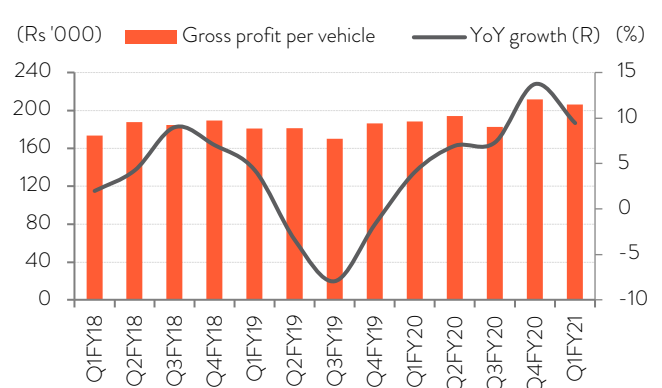
Source: Company, BOBCAPS Research

FIG 7 – MM'S VOLUME MIX – SEGMENT-WISE



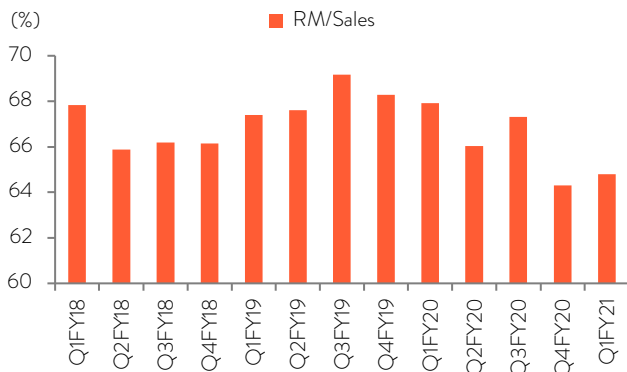
Source: Company, BOBCAPS Research

FIG 8 – GROSS PROFIT PER VEHICLE – MM+MVML



Source: Company, BOBCAPS Research

FIG 9 – RM COST/SALES – MM+MVML



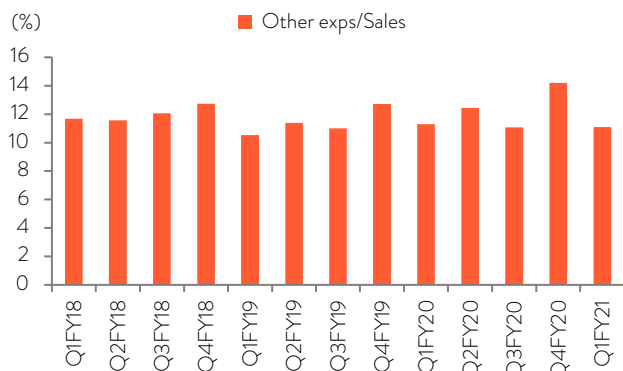
Source: Company, BOBCAPS Research

FIG 10 – EMPLOYEE COST/SALES – MM+MVML



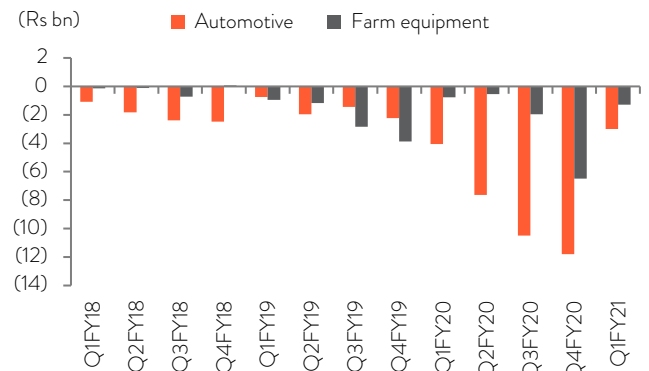
Source: Company, BOBCAPS Research

FIG 11 – OTHER EXPENSES / SALES – MM+MVML



Source: Company, BOBCAPS Research

FIG 12 – IMPLIED EBIT TREND FOR SUBSIDIARIES



Source: Company, BOBCAPS Research | Note: Implied EBIT is derived by subtracting MM+MVML segmental EBIT from consolidated segmental EBIT

Earnings call highlights

- MM faced challenges in acquiring parts as the supply chain remains under pressure due to micro-lockdowns and a fire incident at one of its suppliers.
- Capacity utilisation for tractors remained at 90% in June but was lower at 50% for the auto segment.
- Per management, demand from rural regions has been better than urban areas and hence sales for 'Scorpio' and 'Bolero' remain ahead of urban brands such as 'XUV' and 'Marazzo'.
- Close to 85% of dealers were operational as of June; collections from dealers has not been a challenge
- The company plans to cut back its marketing and advertising spends in FY21.
- MM will be launching three new UVs. Timelines for key launches are: 'Thar' in H2FY21, '601' in Q1FY22 and 'Z101' in H2FY22
- Management was clear that no further investments will be made in Ssangyong (SYMC) and indicated that the investor search is underway.
- The company is actively looking for investment of ~US\$ 100mn in the electric vehicle segment.

Valuation methodology

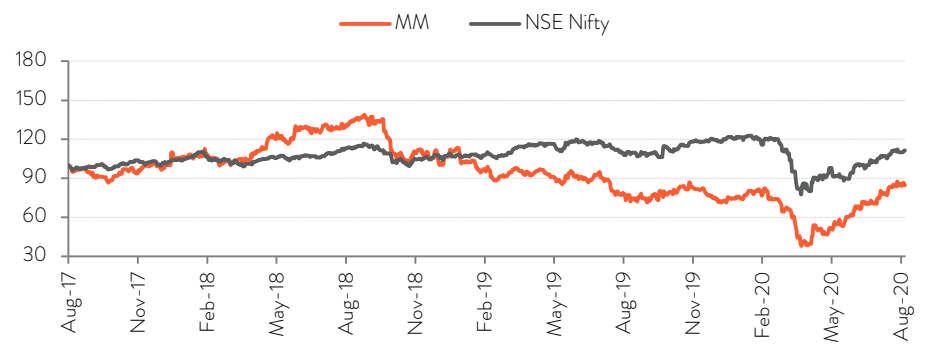
We estimate a 4% revenue CAGR for MM over FY20-FY23 coupled with expansion in operating margins, supporting higher 9% earnings growth. Rolling valuations forward, we have a revised Sep'21 target price of Rs 510 (vs. Rs 480 for Mar'21), wherein we value MM at 13x one-year forward core EPS and assign a 30% holding company discount for subsidiaries. Maintain SELL as we find current valuations rich at 17x FY22E core EPS (adj. for value of subsidiaries)

FIG 13 – SOTP VALUATION

Business	Fair Value (Rs)	Comment
Core business	360	13x Sep'22E Core EPS
Value of subsidiaries	150	30% hold-co discount
Total	510	

Source: Company, BOBCAPS Research

FIG 14 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

- Significant increase in MM’s UV market share led by its upcoming launches can pose upside risks to our estimates.
- Control over losses in subsidiaries and recurring investments therein will help MM’s consolidated earnings/return ratios to improve.
- Softening of raw material prices from current levels can provide a boost to operating margins.

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue	528,482	448,655	379,868	463,238	511,660
EBITDA	75,301	63,506	49,466	65,415	73,572
Depreciation	20,030	23,631	20,008	24,552	27,118
EBIT	55,271	39,875	29,458	40,863	46,454
Net interest income/(expenses)	(1,467)	(1,245)	(1,513)	(1,513)	(1,513)
Other income/(expenses)	16,303	15,391	12,053	14,841	15,921
Exceptional items	(227)	(28,112)	0	0	0
EBT	70,106	54,021	39,998	54,191	60,862
Income taxes	15,867	18,513	10,079	13,656	15,337
Extraordinary items	0	0	0	0	0
Min. int./Inc. from associates	0	0	0	0	0
Reported net profit	54,012	7,397	29,918	40,535	45,525
Adjustments	227	28,112	0	0	0
Adjusted net profit	54,239	35,509	29,918	40,535	45,525

Balance Sheet

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Accounts payables	103,607	72,006	74,933	91,379	102,332
Other current liabilities	38,713	30,229	23,833	33,696	35,816
Provisions	16,151	15,781	11,396	13,897	15,350
Debt funds	26,802	31,530	31,530	31,530	31,530
Other liabilities	6,062	7,274	7,274	7,274	7,274
Equity capital	5,958	5,965	5,965	5,965	5,965
Reserves & surplus	343,979	340,326	361,748	391,664	414,595
Shareholders' fund	349,937	346,291	367,713	397,629	420,561
Total liabilities and equities	541,272	503,111	516,679	575,404	612,863
Cash and cash eq.	70,746	64,262	52,081	66,459	61,047
Accounts receivables	38,119	29,012	29,141	32,998	37,849
Inventories	47,631	40,408	34,344	41,882	47,662
Other current assets	48,700	37,496	34,188	41,691	46,049
Investments	173,836	153,433	173,433	193,433	213,433
Net fixed assets	144,967	169,093	184,086	189,534	197,416
CWIP	0	0	0	0	0
Intangible assets	0	0	0	0	1
Deferred tax assets, net	(7,896)	(15,068)	(15,068)	(15,068)	(15,068)
Other assets	25,168	24,475	24,475	24,475	24,475
Total assets	541,272	503,111	516,679	575,404	612,864

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Net income + Depreciation	74,042	31,028	49,926	65,086	72,643
Interest expenses	(1,467)	(1,245)	(1,513)	(1,513)	(1,513)
Non-cash adjustments	7,900	37,221	1,513	1,513	1,513
Changes in working capital	(11,074)	(12,920)	1,389	9,912	(462)
Other operating cash flows	1,156	(26,899)	0	0	0
Cash flow from operations	70,557	27,184	51,315	74,998	72,181
Capital expenditures	(34,928)	(47,756)	(35,000)	(30,000)	(35,000)
Change in investments	(19,212)	20,403	(20,000)	(20,000)	(20,000)
Other investing cash flows	6,949	10,529	0	0	0
Cash flow from investing	(47,190)	(16,824)	(55,000)	(50,000)	(55,000)
Equities issued/Others	8	7	0	0	0
Debt raised/repaid	(5,339)	4,728	0	0	0
Interest expenses	0	0	0	0	0
Dividends paid	(12,035)	(3,327)	(8,496)	(10,620)	(22,593)
Other financing cash flows	3,078	(7,723)	0	0	0
Cash flow from financing	(14,288)	(6,316)	(8,496)	(10,620)	(22,593)
Changes in cash and cash eq.	9,079	4,045	(12,181)	14,379	(5,412)
Closing cash and cash eq.	77,695	74,791	52,081	66,459	61,047

Per Share

Y/E 31 Mar (Rs)	FY19A	FY20A	FY21E	FY22E	FY23E
Reported EPS	43.5	6.0	24.1	32.6	36.7
Adjusted EPS	43.7	28.6	24.1	32.6	36.7
Dividend per share	8.5	2.4	6.0	7.5	8.5
Book value per share	281.7	278.8	296.1	320.1	338.6

Valuations Ratios

Y/E 31 Mar (x)	FY19A	FY20A	FY21E	FY22E	FY23E
EV/Sales	1.4	1.6	1.9	1.6	1.4
EV/EBITDA	9.6	11.1	14.3	11.0	9.8
Adjusted P/E	13.8	21.0	24.9	18.4	16.4
P/BV	2.1	2.2	2.0	1.9	1.8

DuPont Analysis

Y/E 31 Mar (%)	FY19A	FY20A	FY21E	FY22E	FY23E
Tax burden (Net profit/PBT)	77.0	13.7	74.8	74.8	74.8
Interest burden (PBT/EBIT)	126.8	135.5	135.8	132.6	131.0
EBIT margin (EBIT/Revenue)	10.5	8.9	7.8	8.8	9.1
Asset turnover (Revenue/Avg TA)	97.6	89.2	73.5	80.5	83.5
Leverage (Avg TA/Avg Equity)	1.5	1.5	1.4	1.4	1.5
Adjusted ROAE	16.6	10.2	8.4	10.6	11.1

Source: Company, BOBCAPS Research | Note: TA = Total Assets

Ratio Analysis

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
YoY growth (%)					
Revenue	11.1	(15.1)	(15.3)	21.9	10.5
EBITDA	6.9	(15.7)	(22.1)	32.2	12.5
Adjusted EPS	29.5	(34.5)	(15.7)	35.5	12.3
Profitability & Return ratios (%)					
EBITDA margin	14.2	14.2	13.0	14.1	14.4
EBIT margin	10.5	8.9	7.8	8.8	9.1
Adjusted profit margin	10.3	7.9	7.9	8.8	8.9
Adjusted ROAE	16.6	10.2	8.4	10.6	11.1
ROCE	20.1	14.6	10.7	13.4	14.2
Working capital days (days)					
Receivables	26	24	28	26	27
Inventory	41	41	41	41	9
Payables	83	68	83	84	85
Ratios (x)					
Gross asset turnover	3.8	2.9	2.2	2.5	2.6
Current ratio	1.3	1.5	1.4	1.3	1.3
Net interest coverage ratio	37.7	32.0	19.5	27.0	30.7
Adjusted debt/equity	0.1	0.1	0.1	0.1	0.1

Source: Company, BOBCAPS Research

Disclaimer

Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

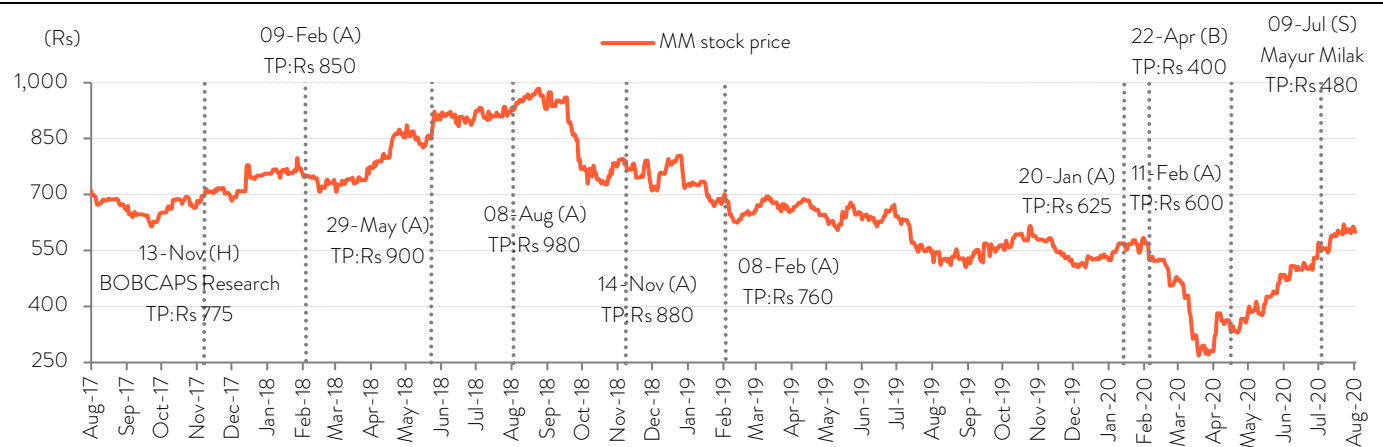
ADD – Expected return from >+5% to +15%

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)

RATINGS AND TARGET PRICE (3-YEAR HISTORY): MAHINDRA & MAHINDRA (MM IN)



B – Buy, A – Add, R – Reduce, S – Sell, H – Hold

Rating distribution

As of 31 July 2020, out of 96 rated stocks in the BOB Capital Markets Limited (BOBCAPS) coverage universe, 46 have BUY ratings, 20 have ADD ratings, 11 are rated REDUCE and 19 are rated SELL. None of these companies have been investment banking clients in the last 12 months.

Analyst certification

The research analyst(s) authoring this report hereby certifies that (1) all of the views expressed in this research report accurately reflect his/her personal views about the subject company or companies and its or their securities, and (2) no part of his/her compensation was, is, or will be, directly or indirectly, related to the specific recommendation(s) or view(s) in this report. Analysts are not registered as research analysts by FINRA and are not associated persons of BOBCAPS.

General disclaimers

BOBCAPS is engaged in the business of Institutional Stock Broking and Investment Banking. BOBCAPS is a member of the National Stock Exchange of India Limited and BSE Limited and is also a SEBI-registered Category I Merchant Banker. BOBCAPS is a wholly owned subsidiary of Bank of Baroda which has its various subsidiaries engaged in the businesses of stock broking, lending, asset management, life insurance, health insurance and wealth management, among others.

BOBCAPS's activities have neither been suspended nor has it defaulted with any stock exchange authority with whom it has been registered in the last five years. BOBCAPS has not been debarred from doing business by any stock exchange or SEBI or any other authority. No disciplinary action has been taken by any regulatory authority against BOBCAPS affecting its equity research analysis activities.

BOBCAPS has obtained registration as a Research Entity under SEBI (Research Analysts) Regulations, 2014, having registration No.: INH000000040 valid till 03 February 2020. BOBCAPS is also a SEBI-registered intermediary for the broking business having SEBI Single Registration Certificate No.: INZ000159332 dated 20 November 2017.

BOBCAPS prohibits its analysts, persons reporting to analysts, and members of their households from maintaining a financial interest in the securities or derivatives of any companies that the analysts cover. Additionally, BOBCAPS prohibits its analysts and persons reporting to analysts from serving as an officer, director, or advisory board member of any companies that the analysts cover.

Our salespeople, traders, and other professionals may provide oral or written market commentary or trading strategies to our clients that reflect opinions contrary to the opinions expressed herein, and our proprietary trading and investing businesses may make investment decisions that are inconsistent with the recommendations

expressed herein. In reviewing these materials, you should be aware that any or all of the foregoing, among other things, may give rise to real or potential conflicts of interest. Additionally, other important information regarding our relationships with the company or companies that are the subject of this material is provided herein.

This material should not be construed as an offer to sell or the solicitation of an offer to buy any security in any jurisdiction where such an offer or solicitation would be illegal. We are not soliciting any action based on this material. It is for the general information of BOBCAPS's clients. It does not constitute a personal recommendation or take into account the particular investment objectives, financial situations, or needs of individual clients. Before acting on any advice or recommendation in this material, clients should consider whether it is suitable for their particular circumstances and, if necessary, seek professional advice.

The price and value of the investments referred to in this material and the income from them may go down as well as up, and investors may realize losses on any investments. Past performance is not a guide for future performance, future returns are not guaranteed and a loss of original capital may occur. BOBCAPS does not provide tax advice to its clients, and all investors are strongly advised to consult with their tax advisers regarding any potential investment in certain transactions — including those involving futures, options, and other derivatives as well as non-investment-grade securities — that give rise to substantial risk and are not suitable for all investors. The material is based on information that we consider reliable, but we do not represent that it is accurate or complete, and it should not be relied on as such. Opinions expressed are our current opinions as of the date appearing on this material only. We endeavour to update on a reasonable basis the information discussed in this material, but regulatory, compliance, or other reasons may prevent us from doing so.

We and our affiliates, officers, directors, and employees, including persons involved in the preparation or issuance of this material, may from time to time have “long” or “short” positions in, act as principal in, and buy or sell the securities or derivatives thereof of companies mentioned herein and may from time to time add to or dispose of any such securities (or investment). We and our affiliates may act as market makers or assume an underwriting commitment in the securities of companies discussed in this document (or in related investments), may sell them to or buy them from customers on a principal basis, and may also perform or seek to perform investment banking or advisory services for or relating to these companies and may also be represented in the supervisory board or any other committee of these companies.

For the purpose of calculating whether BOBCAPS and its affiliates hold, beneficially own, or control, including the right to vote for directors, one per cent or more of the equity shares of the subject company, the holdings of the issuer of the research report is also included.

BOBCAPS and its non-US affiliates may, to the extent permissible under applicable laws, have acted on or used this research to the extent that it relates to non-US issuers, prior to or immediately following its publication. Foreign currency denominated securities are subject to fluctuations in exchange rates that could have an adverse effect on the value or price of or income derived from the investment. In addition, investors in securities such as ADRs, the value of which are influenced by foreign currencies, effectively assume currency risk. In addition, options involve risks and are not suitable for all investors. Please ensure that you have read and understood the Risk disclosure document before entering into any derivative transactions.

In the US, this material is only for Qualified Institutional Buyers as defined under rule 144(a) of the Securities Act, 1933. No part of this document may be distributed in Canada or used by private customers in the United Kingdom.

No part of this material may be (1) copied, photocopied, or duplicated in any form by any means or (2) redistributed without BOBCAPS's prior written consent.

Company-specific disclosures under SEBI (Research Analysts) Regulations, 2014

The research analyst(s) or his/her relatives do not have any material conflict of interest at the time of publication of this research report.

BOBCAPS or its research analyst(s) or his/her relatives do not have any financial interest in the subject company. BOBCAPS or its research analyst(s) or his/her relatives do not have actual/beneficial ownership of one per cent or more securities in the subject company at the end of the month immediately preceding the date of publication of this report.

The research analyst(s) has not received any compensation from the subject company in the past 12 months. Compensation of the research analyst(s) is not based on any specific merchant banking, investment banking or brokerage service transactions.

BOBCAPS or its research analyst(s) is not engaged in any market making activities for the subject company.

The research analyst(s) has not served as an officer, director or employee of the subject company.

BOBCAPS or its associates may have material conflict of interest at the time of publication of this research report.

BOBCAPS's associates may have financial interest in the subject company. BOBCAPS's associates may hold actual / beneficial ownership of one per cent or more securities in the subject company at the end of the month immediately preceding the date of publication of this report.

BOBCAPS or its associates may have managed or co-managed a public offering of securities for the subject company or may have been mandated by the subject company for any other assignment in the past 12 months.

BOBCAPS may have received compensation from the subject company in the past 12 months. BOBCAPS may from time to time solicit or perform investment banking services for the subject company. BOBCAPS or its associates may have received compensation from the subject company in the past 12 months for services in respect of managing or co-managing public offerings, corporate finance, investment banking or merchant banking, brokerage services or other advisory services in a merger or specific transaction. BOBCAPS or its associates may have received compensation for products or services other than investment banking or merchant banking or brokerage services from the subject company in the past 12 months.