November 10, 2017

Buy

Tata Motors

Industry: Auto and Auto Components | Industry View: Positive

Result Update

Great recovery in profits after a lackluster Q1

Strong margin performance on both the businesses

Q2FY18 consolidated numbers posted 7.2% yoy growth at the topline as both JLR volumes as well as domestic business posted healthy growth. At the standalone level, revenues jumped by 35% yoy on strong volume growth both at CV as well as PV segments. Prudent cost savings coupled with higher volumes led to a sharp sequential surge from 1% to 6.2%. Bottomline at this business witnessed reduced losses which the management expects to breakeven in FY19. At JLR, 5% increase in wholesales volumes came on the back of strong China and UK volumes. JLR EBITDA margins zoomed up to 11.8% from 7.9% qoq as the Fx hedge book losses reduced to GBP343 mn from GBP454 mn qoq on account of favorable currency movement and natural unwinding of the hedges taken earlier. As a result of this the net profits grew by 174% yoy to Rs30.8 bn.

New launches to drive sales, expected softness at UK and US posts a cautious outlook on volumes

JLR wholesale volumes increased by 5.7% yoy in Q2 FY18 excluding sales in China joint venture. On the back of run-down of old Discovery and softness in specific markets like Europe and North America reported a 1% and 8% declines respectively, while this de-growth was negated by a 20% growth in the UK and 19% growth in China. Overseas markets too shrugged off their Q1 losses and reported 7% growth in Q2. We note the poor performances by Jaguar XE, XJ and XF (despite launch of a new model) were offset by robust growth at F-Pace, Range Rover, RR Sport, Evoque and Velar. Concerns remain on the US markets as sited by the management, and also on the UK markets which have shown a slippage in the October retail volumes of 18%. However, considering the strength in Chinese markets and ROW geographies, continuous high demand for RR, RR Sport, Velar, Discovery Sport and F-Pace along with the upcoming pipeline of launches of the E-Pace and I-Pace we expect volumes to post a decent 7%/8% growth though it is slightly lower than what we were expecting earlier. We are very positive and excited about the I-Pace and E-Pace launches as it would mark JLR's entry into the electric vehicle industry which has a tremendous potential to grow. The upcoming plant at Slovakia (end of FY19) with a capacity of 150K units will trigger demand then on. On the domestic front, MHCV business has seen a strong bounce back over the last few months and we expect it to continue to do so hereon as macros are improving and also a favorable lower base is supporting the cause. PV sales are performing very well, gaining market share on the success of the recent launch of Nexon, Tiago, Hexa, and Tigor. We expect 15-20% growth in the company's PV business over the next two years.

Margins elevate on Fx hedge losses reduction at JLR and cost control in Indian business

EBITDA margin at JLR came in at ~12% in Q2, which was significantly higher than the previous quarter. This was on the back of reduction of forex hedge book losses by over GBP 100 mn qoq. This was due to a favorable GBP-USD movement and unwinding of the hedges taken earlier. Total outstanding value of the hedge losses came down at GBP1.09 bn from GBP2.4 bn yoy. This was a significant reduction out of which ~GBP700 mn will mature in the coming one year. Assuming GBP/USD to remain constant at current rate of 1.34, the unwinding may happen at expected pace. If GBP strengthens then it may happen even faster and expedite the

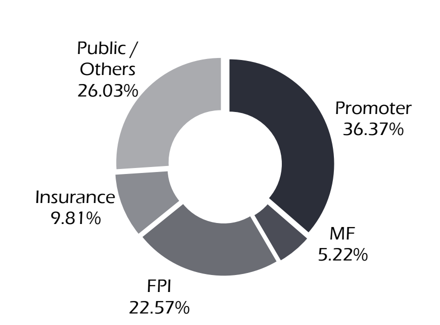
Stock Data

Current Market Price (₹)	422
Target Price (₹)	496
Potential upside (%)	18
FV (₹)	2
Reuters	TAMO.BO
Bloomberg	TTMT IN
Market Cap (₹ bn)	1,217
52-Week Range (₹)	553 / 358

What's changed

12 month Price Target (₹)	From 483 to 496
FY2018E EPS (₹)	From 15.4 to 18.2
FY2019E EPS (₹)	From 35.6 to 42.8

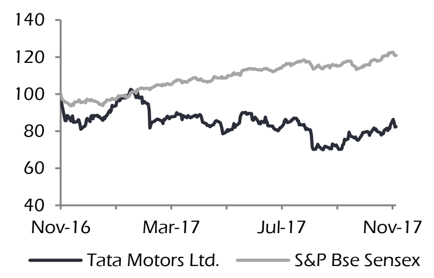
Shareholding Pattern



Fiscal YE

YE Mar	FY 16	FY 17	FY 18E	FY 19E
Revenues (₹ bn)	2,756	2,697	2,752	3,099
EBITDA (%)	13.3	11.0	10.2	12.7
PAT (%)	4.8%	3.3%	2.2%	4.7%
EPS (Rs)	38.7	25.8	18.2	42.8
EPS growth (%)	-14.3	-33.2	-29.7	135.3
P/E (x)	10.9	16.3	23.2	9.9
P/B(x)	1.8	2.4	2.2	1.9
EV/EBITDA (x)	1.7	2.5	2.7	1.6
ROE(%)	17%	15%	10%	19%

Relative Price Performance



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process of margin growth hereon. Management has guided for 8-10% EBIT margins on JLR in the coming 1-2 years. This is on the back of new model launches gaining operating leverage, change in pension scheme payout, material cost reduction program and Slovakia plant launch and ramp up in FY19/20 which will bring up savings up to GBP 2000/unit. On the flip side, firming RM costs, electrification of vehicles and expected lull at UK and US markets may impact margins up to some extent. We have however, increased our margin estimates slightly as the forex hedge losses reduction will significantly impact margins outweighing the concerns on it. Additionally, smart cost cutting at India business along with higher CV sales will help margins to move on up from Q2 levels and bring in PAT breakeven in FY19E.

Financial Highlights

YE Mar (₹.mn)	Q2 FY18	Q1FY18	% qoq	Q2 FY17	% yoy
Total income	706,907	584,934	20.9%	659,004	7.3%
RM costs	438,188	365,758	19.8%	392,758	11.6%
Employee costs	72,563	71,152	2.0%	67,939	6.8%
Other expenses	139,817	137,866	1.4%	178,614	-21.7%
Exp. Trnsfd to cap. Account & Prod. Devt. exp.	43,720	39,490	10.7%	43,133	1.4%
EBITDA	100,058	49,648	101.5%	62,826	59.3%
EBITDA Margins	14.2%	8.5%	550 bps	9.5%	450 bps
Other income	1,888	1,541	22.5%	1,794	5.3%
Interest exp.	11,473	11,089	3.5%	10,249	11.9%
Depreciation	49,698	45,245	9.8%	44,540	11.6%
PBT	41,490	37,370	11.0%	9,993	315.2%
Tax	10,897	12,074	-9.8%	4,246	156.6%
Rep PAT	30,593	25,295	20.9%	11,055	176.7%
Exceptional items	221	(42,515)	N/A	162	36.7%
Adj PAT	30,814	(17,219)	N/A	11,217	174.7%

Outlook and valuation

TAMO reported strong set of numbers in Q2, on the back of surge in profitability at both JLR and India business. On the domestic front, the company gained market share in the PV segment with the launches of Tiago, Hexa and Tigor. MHCV business bounced back post DeMon and BS IV implementation with good monsoon and infrastructure activities inching ahead. New LCV launch and couple of new platforms in the PV space getting launched along with the recent SUV launch of Nexon may act as future growth engines for the company on the domestic side. On JLR front, products such as the recently launched LR Velar, F-Pace, E-Pace and I-Pace EVs and ramping up of recently launched Discovery may act as triggers to growth. Strength in China and ROW countries may somewhat negate the weakness in the UK (seasonal factors and Brexit) and expected softness in the US. China JV is continuously posting strong sales and profitability, which we expect to intensify further. On the profitability front, the deeply negative impact of unwinding of forex hedges felt in Q1 has shown a great revival led by sharp reduction in forex hedge losses. Favorable currency movement may help the cause going forward. More than 70% of hedge book losses getting reduced by FY19E end will lead to a sequential uptick JLR margins hereon negating the impact of higher launch costs and EVs launch and ramp-up costs. Eventual launch and ramp up of Slovakian plant will not only pour volumes but also reduce the per unit vehicle cost due to the geographical advantage it has over UK. Improving product mix in the form of new launches may also provide the impetus. In the domestic business, expected higher CV sales may lift up the margins further. On overall basis, we expect an improved performance from TAMO in the rest of FY18E and FY19E. We have reduced the JLR volumes estimate a bit for FY18/19E on volume concerns in the UK and the US. But on the other had have increased the margin estimates for the same period. We maintain BUY with a slightly raised TP of ₹496.

Financials

Income statement

YE Mar (₹.mn)	FY16	FY17	FY18E	FY19E
Total Revenues	**2,755,611**	**2,696,925**	**2,752,225**	**3,098,569**
Raw Material Cost	1,495,688	1,519,696	1,752,774	1,942,703
Employee Cost	291,989	283,329	280,861	294,058
Other Exp	639,054	627,537	594,356	642,490
Exp. trnsfd to capital a/cs	167,184	168,770	156,000	174,000
EBITDA	**367,562**	**295,887**	**280,235**	**393,318**
EBITDA Margin(%)	13.3	11.0	10.2	12.7
Other Income	9,817	7,545	40,600	51,500
Depreciation	170,142	179,050	201,276	228,713
Interest	46234	42380	32254	34221
PBT	**161,004**	**82,003**	**87,305**	**193,175**
Tax	(28,726)	(32,512)	(25,594)	(47,956)
Rep PAT	**111,083**	**60,636**	**61,711**	**145,219**
Adj PAT	**131,433**	**87,733**	**61,711**	**145,219**
Adj PAT Margins (%)	4.8%	3.3%	2.2%	4.7%

Key Ratios

YE Mar	FY16	FY17	FY18E	FY19E
Per Share Data (₹)				
Adj. EPS	38.7	25.8	18.2	42.8
CEPS	88.8	78.6	77.4	110.1
BVPS	233.8	172.3	187.7	227.0
DPS	-0.3	1.1	1.5	3.4
Growth Ratios(%)				
Total revenues	4.7	-2.1	2.1	12.6
EBITDA	-7.2	-19.5	-5.3	40.4
PAT	-9.6	-33.2	-29.7	135.3
EPS Growth	-14.3	-33.2	-29.7	135.3
Valuation Ratios (X)				
PE	10.9	16.3	23.2	9.9
P/CEPS	4.8	5.4	5.4	3.8
P/BV	1.8	2.4	2.2	1.9
EV/Sales	0.2	0.3	0.3	0.2
EV/EBITDA	1.7	2.5	2.7	1.6
Operating Ratios (Days)				
Inventory days	43	47	51	53
Recievable Days	18	19	19	20
Payables day	247	264	250	253
Net Debt/Equity (x)	0.42	0.80	0.72	0.47
Profitability Ratios (%)				
ROE	17%	15%	10%	19%
Dividend payout	-1%	5%	8%	8%
ROA	5%	3%	2%	5%

Source: Company, LKP Research

Balance sheet

YE Mar (₹. mn)	FY16	FY17	FY18E	FY19E
Equity and Liabilities				
Equity Share Capital	6,792	6,792	6,792	6,792
Reserves & Surplus	782,732	573,827	630,601	764,202
Total Networth	793,852	585,150	637,393	770,994
Total debt	505,103	606,292	586,292	566,292
Deferred tax liabilities	44,747	11,740	10,740	9,740
Other long term liabilities	178,302	288,021	308,021	313,021
Long term provisions	78,910	90,045	102,045	110,045
Minority interest	0	0	0	0
Current Liab & Prov				
Current liabilities	1,012,049	1,098,217	1,200,530	1,346,586
Provisions	58,445	58,078	70,111	81,594
Total Equity & Liabilities	**2,671,408**	**2,737,541**	**2,915,131**	**3,198,271**
Assets				
Net block	649,271	595,945	594,669	565,956
Capital WIP	65,510	101,868	151,868	201,868
Goodwill	7,598	6,733	6,733	6,733
Intangible Assets	609,129	591,882	629,949	654,949
Non current investments	45,340	52,968	55,968	58,968
Deferred tax assets	39,570	44,573	44,573	44,573
Long term assets and loans & adv.	5,038	7,537	10,537	13,537
Other non current assets	150,718	167,717	169,717	171,717
Current Assets				
Current Investments	192,330	150,411	180,411	210,411
Cash and Bank	171,536	139,867	125,298	206,222
Inventories	326,557	350,853	384,557	449,929
Sundry Debtors	135,709	140,755	143,267	169,785
Loan, Advances & others	273,102	386,432	417,584	443,623
Total Assets	**2,671,408**	**2,737,541**	**2,915,131**	**3,198,271**

Cash Flow

YE Mar (₹ mn)	FY16	FY17	FY18E	FY19E
PAT	110,237	75,565	61,711	145,219
Depreciation	170,142	179,050	201,276	228,713
Interest	38,230	36,653	32,254	34,221
Chng in working capital	25,515	32,543	46,978	39,610
Tax paid	28,726	32,512	25,594	47,956
Cash flow from operations (a)	**391,666**	**301,992**	**293,324**	**416,464**
Capital expenditure	(326,232)	(304,668)	(250,000)	(250,000)
Chng in investments	0	0	0	0
Other investing activities	(59,875)	(76,133)	(38,000)	(38,000)
Cash flow from investing (b)	**(386,107)**	**(380,801)**	**(288,000)**	**(288,000)**
Inc/(dec) in borrowings	(51,740)	116,577	11,000	(8,000)
Dividend paid (incl. tax)	(1,739)	(1,212)	1,361	(5,320)
Other financing activities	21,550	(53,311)	(32,254)	(34,221)
Cash flow from financing (c)	**(31,929)**	**62,053**	**(19,893)**	**(47,540)**
Net chng in cash (a+b+c)	**(26,370)**	**(16,755)**	**(14,568)**	**80,924**
Closing cash & cash equiv.	**193,499**	**139,867**	**125,298**	**206,222**

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