

# Mahindra & Mahindra | Auto & Farm Equipment

Start of a new beginning!

# LKP

## Great set of numbers in Q3

M&M reported strong numbers in line with our expectations. Net revenues came in at ₹140.6 bn (+15.2% yoy). This growth was led by (1) 12% yoy increase in realizations and (2) 3% yoy increase in volumes. Automotive division revenues came in at ₹83.1 bn, an increase of 12% yoy led by (a) 21% yoy increase in ASPs due to BS-VI transition and (b) 8% yoy decline in volumes in Q3 FY21. Tractor division revenues increased by 24% yoy led by (a) 20% yoy increase in volumes and (b) 3% yoy increase in ASPs in Q3 FY21. Automotive EBIT margin came in at 7.4% (+10 bps yoy), due to cost-cutting initiatives and one-time gain of ₹900 mn due to prior-period incentives. Tractor EBIT margins came in at 23.4% (+400 bps yoy, -100 bps qoq). Overall EBITDA margin came in at 16% (+260 bps yoy, -10 bps qoq) due to (1) RM headwinds and (2) higher-than expected employee cost. The company reported net profit of ₹5.3 bn (+40% yoy) which included exceptional loss of ₹12.1 bn related to exposure in Ssangyong in Q3 FY21. Consolidated EBIT (excluding Ssangyong) came in at ₹15.6 bn (-2% yoy). PAT adjusted for this loss came in at ₹17.2 bn, which was 90% up yoy. The company has exited Ssangyong Motors and substantially reduced losses in overseas subsidiaries. Management expects only ₹3 bn loss in FY2022 from loss making subsidiaries and has taken steps to achieve 18% RoE target in the next few years.

## Tractor industry remains the main driver of growth

Tractors business of M&M remained the star performer in Q3 as well. The company did not give any guidance for domestic tractor industry volumes for FY2022E. The company expects domestic tractor industry to grow by 20% yoy in FY2021E. M&M highlighted that tractor segment fundamentals continue to remain strong led by (1) strong Kharif procurement (+27% yoy), (2) higher Rabi acreage (+4% yoy), (3) higher reservoir levels and (4) strong agricultural credit growth. The system stock level (factory plus dealer inventory) is 85% of normalized levels (taking Q1 FY18 as a base) in the tractor business

## New Thar launch brings cheer in the SUV business, new launches to bolster growth

M&M witnessed 41% yoy retail growth in the UV segment in Q3 FY21. The company has received a good response from new Thar launch. They have received 39,000+ bookings (45% of the bookings were for automatic variants) since launch on October 2, 2020. Also, the company received 6,000+ bookings in January 2021. The company expects to launch two new SUVs in FY2022E and intends to launch differentiated and profitable products and not compete on market share. In automotive segment, shortage of semiconductors remained an area of concern for the company. Dealer level stock is less than 1,000 units currently.

## Tighter Capital Allocation Norms

Over the past four years, losses in subsidiaries increased from ₹530 mn in FY2017 to ₹52.6 bn in FY2020. The company highlighted that it will focus on realigning its capital allocation norms.

| YE Mar             | FY 19 | FY 20 | FY 21E | FY 22E | FY 23E |
|--------------------|-------|-------|--------|--------|--------|
| Total Sales (₹ bn) | 536   | 455   | 413    | 491    | 585    |
| EBITDA Margins (%) | 12.4  | 12.7  | 15.7   | 15.8   | 16.2   |
| PAT Margins (%)    | 9.0   | 7.4   | 10.0   | 10.0   | 10.2   |
| EPS (₹)            | 40.6  | 28.1  | 34.7   | 41.1   | 50.3   |
| P/E (x)            | 21.3  | 30.8  | 24.9   | 21.1   | 17.2   |
| P/BV (x)           | 3.0   | 3.0   | 2.7    | 2.5    | 2.3    |
| EV/EBITDA (x)      | 12.6  | 14.7  | 13.0   | 10.7   | 8.5    |
| ROE (%)            | 14.1  | 9.7   | 11.0   | 11.8   | 13.1   |
| Dividend Yield (%) | 1.0   | 1.2   | 1.0    | 1.2    | 1.5    |

|                          |     |
|--------------------------|-----|
| Rating                   | Buy |
| Current Market Price (₹) | 859 |
| 12 M Price Target (₹)    | 974 |
| Potential upside (%)     | 13  |

## Stock Data

|                                         |              |
|-----------------------------------------|--------------|
| FV (₹)                                  | 5            |
| Market Cap Full (₹ bn)                  | 1,068        |
| Market Cap Free Float (₹ bn)            | 813          |
| 52-Week High / Low (₹)                  | 952 / 245    |
| 2-Year High / Low (₹)                   | 952 / 245    |
| 1 Year Avg. Dly Traded Volume (in lakh) | 70           |
| BSE Code / NSE Symbol                   | 500520 / M&M |
| Bloomberg Code                          | MM IN        |

## Shareholding Pattern (%)

|           | Dec-20 | Sep-20 | Jun-20 | Mar-20 |
|-----------|--------|--------|--------|--------|
| Promoter  | 19.44  | 19.58  | 19.60  | 19.89  |
| FPIs      | 37.90  | 34.72  | 34.61  | 33.88  |
| MFs       | 10.77  | 10.98  | 10.85  | 10.42  |
| Insurance | 10.74  | 12.94  | 13.81  | 13.86  |
| Others    | 21.15  | 21.78  | 21.13  | 21.95  |

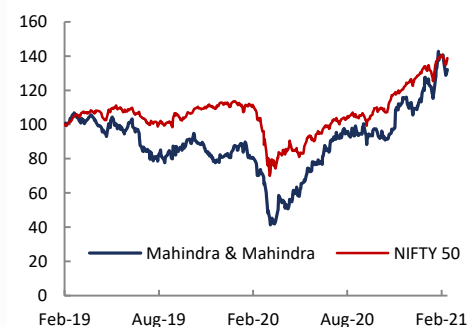
Source: BSE

## Price Performance (%)

| (%)      | 1M   | 3M    | 6M    | 1YR   |
|----------|------|-------|-------|-------|
| M&M      | 8.1% | 19.3% | 41.0% | 68.8% |
| Nifty 50 | 6.0% | 17.4% | 31.6% | 28.0% |

\* To date / current date : February 25, 2021

## M&M vs Nifty 50



However, over the past three quarters, the company has taken several decisions to correct its capital allocation strategy (1) no infusion of further capital into Ssangyong and is aggressively looking for strategic investors to reduce their stake in the company. As a part of its turnaround plan, the company has taken a complete write-off on its investments in Ssangyong Motors during the quarter and will cease consolidating the results of Ssangyong as a subsidiary. (2) complete exit from Genze business, (3) the company has pulled out from the bid to manufacture small delivery trucks for the United States' Postal Service, which would have required investment worth US\$500 mn, (4) the company has also shut down the aerospace business in Australia, (5) divestment of entire stake held in Mahindra First Choice Services Limited and its subsidiary Auto Digitech Private Limited to TVS Automobile Solutions Private Limited (TASL) in a share swap deal, (6) called off the proposed JV with Ford India due to higher investments required, which would have impacted return ratios, (7) is scouting for strategic investors for Mahindra Electric Mobility and Automobili Pininfarina and (8) complete exit from Ssangyong Motors.

### Way Forward – Mahindra 3.0 Strategy

Walk, Run and Fly - The company highlighted its strategy in both automotive and farm sectors. During H1 FY21 (Walk strategy), the company has focused on managing cash, gradually ramping-up of operations with safety first, support dealers and suppliers and focus on high growth segments such as rural, goods mobility and B2B. During H2 FY21 (Run strategy), the company will focus on its core business with launch of new models in SUV segment, capex and investment prioritization and work towards aggressive cost optimization. From FY2022E onwards (Fly strategy), the company will launch two new models (W601 and Z101), focus on EV portfolio, focus on SUV core brand differentiation and will build path to profitability for global subsidiaries. Also, the company highlighted that it will focus on 10 sectors which can be multi-bagger over the long term – (1) Powerol, (2) Mahindra Rural Housing Finance, (3) Farm Implements, (4) Mahindra Accelo, (5) Mahindra Electric, (6) Mahindra two-wheeler (premium motorcycle segment), (7) Mobility segment, (8) Mahindra Susten, (9) Aftermarket segment and (10) Bristlecone. The combined revenues of these 10 businesses is ₹10.3 bn in FY2020 and profit of ₹172 mn

### Quarterly Financial Snapshot

| All fig in ₹ mn    | Q3 FY21  | Q2 FY21  | % qoq    | Q3 FY20  | % yoy   |
|--------------------|----------|----------|----------|----------|---------|
| Net Sales          | 1,42,159 | 1,17,105 | 21.4%    | 1,23,453 | 15.2%   |
| Raw Material Costs | 1,00,426 | 80,923   | 24.1%    | 86,492   | 16.1%   |
| Employee Costs     | 7,561    | 7,012    | 7.8%     | 7,594    | -0.4%   |
| Other Expenses     | 11,395   | 10,272   | 10.9%    | 12,872   | -11.5%  |
| EBITDA             | 22,778   | 18,898   | 20.5%    | 16,495   | 38.1%   |
| EBITDA Margins (%) | 16.0%    | 16.1%    | (10 bps) | 13.4%    | 260 bps |
| Other Income       | 5,699    | 3,926    | 45.2%    | 2063     | 176.3%  |
| Depreciation       | 5,714    | 5,545    | 3.0%     | 5537     | 3.2%    |
| Interest Expenses  | 997      | 1,091    | -8.6%    | 224      | 344.9%  |
| PBT                | 21,766   | 16,188   | 34.5%    | 12796    | 70.1%   |
| Tax                | 4,542    | 3,922    | 15.8%    | 3725     | 21.9%   |
| Reported PAT       | 309      | 772      | N/A      | 3065     | N/A     |
| Exceptional Items  | (16,915) | (11,495) | N/A      | -6006    | N/A     |
| Adjusted PAT       | 17,224   | 12,267   | 40.4%    | 9071     | 89.9%   |
| Adj EPS            | 14.55    | 10.36    | 40.4%    | 7.7      | 89.9%   |

Source: Company, LKP Research

### Outlook and Valuation

We have increased our FY2021-22E EPS by 5-10% due to higher volume and EBIT margin assumptions for the automotive business. We also expect tractor segment demand to remain buoyant given a strong rural economy amid normal monsoon and increased government spending. The company has identified several pillars of growth, which can leverage the core strength of M&M group and accelerate the growth for the company over the medium term, which we are currently not building in our assumptions. Maintain BUY rating on attractive valuations; SoTP-based target price increased to ₹974 as we expect margins to improve on increase in value of UV and LCV segments on higher volume and margin assumptions and rolling over to FY 23E estimates. M&M is set for a new beginning as they have taken multiple steps to improve the capital allocation strategy by selling stakes in loss making subsidiaries, exiting certain subsidiaries or walking out from certain JVs or deals, which would have consumed capital.

| SOTP                                 |                              |               |                    |
|--------------------------------------|------------------------------|---------------|--------------------|
| Particulars                          | Basis                        | Subs Discount | Value per share(₹) |
| <b>M&amp;M</b>                       | <b>P/E (@13x FY 23E EPS)</b> | -             | <b>654</b>         |
| M&M Financial Services               | Market cap                   | 25%           | 40                 |
| Tech Mahindra                        | Market cap                   | 20%           | 221                |
| Mahindra Lifespaces                  | Market cap                   | 30%           | 6                  |
| Mahindra CIE Automotives             | Market cap                   | 30%           | 28                 |
| Mahindra Logistics                   | Market cap                   | 30%           | 12                 |
| Mahindra Holiday & Resorts           | Market cap                   | 30%           | 8                  |
| Swaraj Engines                       | Market cap                   | 30%           | 5                  |
| Ssangyong                            | Market cap                   | 30%           | 7                  |
| <b>Subsidiaries Total SOTP value</b> |                              |               | <b>320</b>         |
| <b>Total</b>                         |                              |               | <b>974</b>         |

Source: Company, LKP Research

## Consolidated Financials

| Income Statement           |                 |                 |                 |                 |                 |
|----------------------------|-----------------|-----------------|-----------------|-----------------|-----------------|
| YE Mar (₹ mn)              | FY 19           | FY 20           | FY 21E          | FY 22E          | FY 23E          |
| <b>Total Revenues</b>      | <b>5,36,140</b> | <b>4,54,878</b> | <b>4,13,084</b> | <b>4,90,918</b> | <b>5,85,070</b> |
| Raw Material Cost          | 3,82,565        | 3,16,326        | 2,87,093        | 3,43,643        | 4,08,379        |
| Employee Cost              | 29,802          | 28,801          | 23,959          | 27,001          | 32,179          |
| Other Exp                  | 57,377          | 51,771          | 37,178          | 42,710          | 49,731          |
| <b>EBITDA</b>              | <b>66,396</b>   | <b>57,981</b>   | <b>64,854</b>   | <b>77,565</b>   | <b>94,781</b>   |
| EBITDA Margin(%)           | 12.4            | 12.7            | 15.7            | 15.8            | 16.2            |
| Other Income               | 16,890          | 16,678          | 14,000          | 16,000          | 18,000          |
| Depreciation               | 18,604          | 22,226          | 21,291          | 25,791          | 30,291          |
| Interest                   | 1134            | 1132            | 3200            | 3500            | 3700            |
| <b>PBT</b>                 | <b>63,548</b>   | <b>51,300</b>   | <b>54,363</b>   | <b>64,274</b>   | <b>78,790</b>   |
| PBT Margin(%)              | 11.9            | 11.3            | 13.2            | 13.1            | 13.5            |
| Tax                        | 15,290          | 17,855          | 13,047          | 15,426          | 18,910          |
| Adj PAT                    | 48,258          | 33,445          | 41,316          | 48,848          | 59,881          |
| <b>Adj PAT Margins (%)</b> | <b>9.0</b>      | <b>7.4</b>      | <b>10.0</b>     | <b>10.0</b>     | <b>10.2</b>     |
| Exceptional items          | -297            | -20140          | 0               | 0               | 0               |
| <b>Reported PAT</b>        | <b>47,961</b>   | <b>13,305</b>   | <b>41,316</b>   | <b>48,848</b>   | <b>59,881</b>   |
| Rep. PAT Margins (%)       | 8.9             | 2.9             | 10.0            | 10.0            | 10.2            |

| Key Ratios                      |       |       |        |        |        |
|---------------------------------|-------|-------|--------|--------|--------|
| YE Mar                          | FY 19 | FY 20 | FY 21E | FY 22E | FY 23E |
| <b>Per Share Data (₹)</b>       |       |       |        |        |        |
| Adj. EPS                        | 40.6  | 28.1  | 34.7   | 41.1   | 50.3   |
| CEPS                            | 55.9  | 29.9  | 52.6   | 62.7   | 75.8   |
| BVPS                            | 287.5 | 289.7 | 315.7  | 346.5  | 384.2  |
| DPS                             | 8.5   | 10.0  | 8.7    | 10.3   | 12.6   |
| <b>Growth Ratios(%)</b>         |       |       |        |        |        |
| Total revenues                  | 10.1  | -15.2 | -9.2   | 18.8   | 19.2   |
| EBITDA                          | 6.7   | -12.7 | 11.9   | 19.6   | 22.2   |
| PAT                             | 23.0  | -30.7 | 23.5   | 18.2   | 22.6   |
| EPS Growth                      | 23.0  | -30.7 | 23.5   | 18.2   | 22.6   |
| <b>Valuation Ratios (X)</b>     |       |       |        |        |        |
| PE                              | 21.3  | 30.8  | 24.9   | 21.1   | 17.2   |
| P/CEPS                          | 15.5  | 29.0  | 16.4   | 13.8   | 11.4   |
| P/BV                            | 3.0   | 3.0   | 2.7    | 2.5    | 2.3    |
| EV/Sales                        | 1.6   | 1.9   | 2.0    | 1.7    | 1.4    |
| EV/EBITDA                       | 12.6  | 14.7  | 13.0   | 10.7   | 8.5    |
| <b>Operating Ratios (Days)</b>  |       |       |        |        |        |
| Inventory days                  | 36.6  | 39.2  | 42.0   | 44.0   | 48.0   |
| Receivable Days                 | 24.0  | 27.0  | 28.0   | 28.0   | 29.0   |
| Payables day                    | 87.2  | 95.0  | 98.0   | 99.0   | 100.0  |
| Net Debt/Equity (x)             | 0.06  | 0.06  | 0.06   | 0.06   | 0.06   |
| <b>Profitability Ratios (%)</b> |       |       |        |        |        |
| ROE                             | 14.1  | 9.7   | 11.0   | 11.8   | 13.1   |
| Dividend payout                 | 21.0  | 35.5  | 25.0   | 25.0   | 25.0   |
| Dividend yield                  | 1.0   | 1.2   | 1.0    | 1.2    | 1.5    |

Source: Company, LKP Research

| Balance Sheet                          |                 |                 |                 |                 |                 |
|----------------------------------------|-----------------|-----------------|-----------------|-----------------|-----------------|
| YE Mar (₹ mn)                          | FY 19           | FY 20           | FY 21E          | FY 22E          | FY 23E          |
| <b>Equity and Liabilities</b>          |                 |                 |                 |                 |                 |
| Equity Share Capital                   | 5,958           | 5,958           | 5,958           | 5,958           | 5,958           |
| Reserves & Surplus                     | 3,36,134        | 3,38,713        | 3,69,700        | 4,06,337        | 4,51,247        |
| <b>Total Networth</b>                  | <b>3,42,092</b> | <b>3,44,671</b> | <b>3,75,658</b> | <b>4,12,295</b> | <b>4,57,205</b> |
| Total debt                             | 36,536          | 36,532          | 38,032          | 40,032          | 42,033          |
| Deferred tax liabilities               | 6,341           | 14,082          | 14,082          | 14,082          | 14,083          |
| <b>Current liabilities &amp; Prov.</b> | <b>1,42,001</b> | <b>1,09,735</b> | <b>1,20,960</b> | <b>1,39,084</b> | <b>1,59,762</b> |
| <b>Total Liabilities</b>               | <b>5,26,971</b> | <b>5,05,021</b> | <b>5,48,732</b> | <b>6,05,493</b> | <b>6,73,083</b> |
| <b>Assets</b>                          |                 |                 |                 |                 |                 |
| Fixed assets                           | 1,25,015        | 1,44,041        | 1,74,750        | 1,99,459        | 2,19,668        |
| Non current Investments                | 1,90,321        | 1,77,485        | 1,75,485        | 1,72,485        | 1,68,485        |
| Other non current assets               | 30,924          | 32,080          | 32,080          | 32,080          | 32,080          |
| <b>Current Assets</b>                  | <b>1,80,710</b> | <b>1,51,415</b> | <b>1,66,417</b> | <b>2,01,469</b> | <b>2,52,848</b> |
| Cash and bank(i)                       | 22,379          | 23,235          | 35,512          | 55,203          | 84,477          |
| Bank deposits other than(i)            | 14,937          | 19,130          | 21,130          | 22,130          | 23,130          |
| Inventories                            | 38,393          | 34,009          | 33,035          | 41,425          | 53,705          |
| Sundry Debtors                         | 39,463          | 29,990          | 31,689          | 37,659          | 46,485          |
| Loan, Advances & others                | 6,734           | 5,120           | 5,120           | 5,120           | 5,120           |
| Other current assets                   | 73,741          | 59,061          | 61,061          | 62,061          | 63,061          |
| <b>Total Assets</b>                    | <b>5,26,971</b> | <b>5,05,021</b> | <b>5,48,732</b> | <b>6,05,493</b> | <b>6,73,083</b> |

| Cash Flow                                  |                |                |                |                |                |
|--------------------------------------------|----------------|----------------|----------------|----------------|----------------|
| YE Mar (₹ mn)                              | FY 19          | FY 20          | FY 21E         | FY 22E         | FY 23E         |
| PBT                                        | 63,548         | 51,300         | 54,363         | 64,274         | 78,790         |
| Depreciation                               | 18,604         | 22,226         | 21,291         | 25,791         | 30,291         |
| Interest                                   | 1,134          | 1,132          | 3,200          | 3,500          | 3,700          |
| Chng in working capital                    | -5,060         | -13,260        | 8,499          | 1,764          | -2,427         |
| Tax paid                                   | -14,341        | -10,823        | -13,047        | -15,426        | -18,910        |
| Other operating activities                 | -14,645        | -13,797        | 1,500          | 2,000          | 2,000          |
| <b>Cash flow from operations (a)</b>       | <b>49,240</b>  | <b>36,778</b>  | <b>75,806</b>  | <b>81,903</b>  | <b>93,444</b>  |
| Capital expenditure                        | -30,316        | -39,437        | -52,000        | -50,500        | -50,500        |
| Chng in investments                        | -17,942        | -13,037        | 2,000          | 3,000          | 4,000          |
| Other investing activities                 | 22,774         | 26,717         | -2,000         | -1,000         | -1,000         |
| <b>Cash flow from investing (b)</b>        | <b>-25,485</b> | <b>-25,757</b> | <b>-52,000</b> | <b>-48,500</b> | <b>-47,500</b> |
| <b>Free cash flow (a+b)</b>                | <b>23,755</b>  | <b>11,021</b>  | <b>23,806</b>  | <b>33,403</b>  | <b>45,944</b>  |
| Equity raised/(repaid)                     | 0              | 0              | 0              | 0              | 0              |
| Inc/dec in borrowings                      | -3,725         | 3,289          | 2,000          | 2,000          | 2,000          |
| Dividend paid (incl. tax)                  | -10,117        | -11,874        | -10,329        | -12,212        | -14,970        |
| Other financing activities                 | -456           | -456           | 0              | 0              | 0              |
| <b>Cash flow from financing (c)</b>        | <b>-15,552</b> | <b>-10,155</b> | <b>-11,529</b> | <b>-13,712</b> | <b>-16,670</b> |
| <b>Net chng in cash (a+b+c)</b>            | <b>8,203</b>   | <b>866</b>     | <b>12,277</b>  | <b>19,691</b>  | <b>29,274</b>  |
| <b>Closing cash &amp; cash equivalents</b> | <b>22,379</b>  | <b>23,235</b>  | <b>35,512</b>  | <b>55,203</b>  | <b>84,477</b>  |

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