

## Weak volumes, RM headwinds continue to hamper bottomline

- Dull festive season and muted participation from rural markets led to subdued volumes in Q3
- RM cost inflation and production challenges due to chip shortage to further dent the bottomline
- We await management commentary on semiconductor supply, inventory levels, new launches and RM cost outlook

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**Lacklustre festive season derails auto volumes:** Amongst our coverage, all OEMs barring AL have posted negative-to-flatish YoY volume growth in Q3FY22. The decline in volumes was primarily due to weak festive demand, semiconductor shortages, sluggish recovery in rural markets as well as a high base from pent-up demand seen in Q3FY21. 2W volumes remain the hardest hit during the quarter, while some green shoots were seen in the CV market.

**Topline to remain soft:** Factoring in poor volumes, we expect revenue growth to be in the range of -22% to +18% YoY for our coverage. AL's revenue is forecast to grow the most by 18% YoY primarily due to recovery in HCVs coupled with higher price realisations and a better product mix. At the other end, HMCL, which has seen a 30% YoY drop in volumes, is likely to post the largest fall in topline by 22% YoY.

**PAT likely to bottom out:** We expect a YoY PAT decline for our entire coverage barring EIM. For EIM, we estimate a 10% rise in PAT led by stronger price realisations and a better product mix. In our view, lower volumes, production challenges due to semiconductor issues coupled with a surge in raw material cost have dented auto OEM profitability. However, we expect input cost to normalise hereon and hence believe PAT will improve in coming quarters, provided volumes move up.

**What to watch for in Q3:** (1) Near-term impact of Omicron, (2) Rising raw material prices and semiconductor shortage issues, (3) Inventory levels both wholesale as well as retail, (4) New product pipeline.

**Mid-to-long-term outlook choppy:** The auto industry has been facing a slew of difficulties in recent years due to emission norms, the pandemic and now the chip shortage. The industry also stands at the cusp of a shift from traditional fuel to EVs. Newer players in the 2W, 3W and bus segments are posing stiff competition to incumbents. Many incumbents have delayed launches in FY22 and hence FY23 will see a large product pipeline for market leaders such as MSIL and Hyundai, which should help them regain market share. In 2Ws, we expect sales to remain choppy, though motorcycle players are likely to be less impacted by electrification than scooters.

### Recommendation snapshot

Ticker	Price	Target	Rating
AL IN	138	121	HOLD
BJAUT IN	3,420	4,231	BUY
EIM IN	2,711	2,981	HOLD
ESC IN	1,869	2,201	BUY
HMCL IN	2,750	3,191	BUY
MM IN	875	1,011	BUY
MSIL IN	8,190	7,771	HOLD
TVSL IN	631	681	HOLD
VSTT IN	2,899	2,300	HOLD

Price & Target in Rupees | Price as of 21 Jan 2022



Fig 1 – BOBCAPS Auto universe: Quarterly preview

Company (Rs mn)	Q3FY22E	Q3FY21	YoY (%)	Q2FY22	QoQ (%)	9MFY22E	9MFY21	YoY (%)	Remarks
<b>MSIL</b>									
Sales	2,30,407	2,34,578	(1.8)	2,05,389	12.2	6,13,503	4,63,088	32.5	Given 13.5% QoQ volume growth and a marginal 1.1% decline ASP (due to a weak product mix, partly offset by price hikes), we expect 12% YoY revenue growth in Q3. EBITDA margin is forecast to expand 225bps QoQ on better operating efficiency. We model for 112% QoQ adj. PAT growth off a low base. Key monitorables are inventory levels, RM prices, semiconductor availability and new launch timelines, especially in the SUV space.
EBITDA	14,761	22261	(33.7)	8,549	72.7	31,521	32,963	(4.4)	
Adj PAT	10,069	19,414	(48.1)	4,753	111.8	19,230	30,636	(37.2)	
EBITDA margin (%)	6.4	9.5	(308bps)	4.2	224bps	5.1	7.1	(198bps)	
PAT margin (%)	4.4	8.3	(391bps)	2.3	206bps	3.1	6.6	(348bps)	
<b>MM</b>									
Sales	1,48,761	1,40,565	5.8	1,33,054	11.8	3,99,443	3,12,363	27.9	Auto volumes declined 4.6% YoY due to strong pent-up demand seen last year in tractors. Strong pricing actions will help the company negate RM inflation QoQ, but we expect YoY EBITDA margin to decline 365bps. Adj. PAT is likely to fall 14% YoY. Key monitorables are distribution plans for key SUV models (Thar, XUV700) that are facing long waiting periods due to chip shortages and launch timelines for the much awaited Scorpio and XUV400 (EV).
EBITDA	19,811	23856	(17.0)	16,598	19.4	52,726	50,161	5.1	
Adj PAT	15,041	17,448	(13.8)	16,867	(10.8)	41,249	30,950	33.3	
EBITDA margin (%)	13.3	17.0	(365bps)	12.5	84bps	13.2	16.1	(286bps)	
PAT margin (%)	10.1	12.4	(230bps)	12.7	(257bps)	10.3	9.9	42bps	
<b>ESC</b>									
Sales	18,694	20,174	(7.3)	16,623	12.5	52,032	47,188	10.3	Tractor volumes declined 20% YoY due to strong pent-up demand seen in Q3FY21. YoY revenue is thus expected to fall by 7%, partly cushioned by strong sales in the railway segment and higher realisations across segments. EBITDA and PAT margins continue to bear the brunt of high RM prices YoY, but should improve by ~65bps QoQ due to operational efficiency and pricing action. Key monitorables are updates on the Kubota acquisition and export plans post closure of the deal. Also, any advancements in development of EV tractors.
EBITDA	2,482	3641	(31.8)	2,101	18.1	6,915	7,846	(11.9)	
Adj PAT	2,114	2,807	(24.7)	1,767	19.6	5,733	6,028	(4.9)	
EBITDA margin (%)	13.3	18.0	(477bps)	12.6	64bps	13.3	16.6	(334bps)	
PAT margin (%)	11.3	13.9	(261bps)	10.6	67bps	11.0	12.8	(176bps)	
<b>HMCL</b>									
Sales	76,494	97,758	(21.8)	84,534	(9.5)	2,15,899	2,21,147	(2.4)	ASP is likely to rise 0.7% QoQ and 11.8% YoY given recent price hikes. However, we expect YoY sales to decline 22% on the back of a 30% drop in volumes. Weaker operating leverage coupled with rising RM cost inflation is expected to shrink EBITDA margin by 290bps, with adj. PAT to decline 39.3% YoY. Key monitorables are inventory levels, new launches especially in EVs after investments made in Ather Energy and Gogoro, and any vendor-side supply challenges.
EBITDA	8,852	14136	(37.4)	10,664	(17.0)	24,664	28,081	(12.2)	
Adj PAT	6,578	10,845	(39.3)	7,944	(17.2)	18,176	20,992	(13.4)	
EBITDA margin (%)	11.6	14.5	(289bps)	12.6	(104bps)	11.4	12.7	(127bps)	
PAT margin (%)	8.6	11.1	(249bps)	9.4	(80bps)	8.4	9.5	(107bps)	
<b>EIM</b>									
Sales	29,582	28,041	5.5	21,819	35.6	70,479	56,966	23.7	Royal Enfield volumes were down in Q3 but timely price hikes and new launches should help ASPs improve, leading to 6% YoY revenue growth. We believe price realisations would help EIM to negate RM cost pressures. Thus, EBITDA and PAT are forecast to improve 5% and 10% YoY respectively. Key monitorables are new launch timelines, inventory levels and studio store performance.
EBITDA	6,912	6580	5.0	4,427	56.2	14,684	11,430	28.5	
Adj PAT	5,371	4,885	10.0	3,434	56.4	11,477	8,617	33.2	
EBITDA margin (%)	23.4	23.5	(10bps)	20.3	308bps	20.8	20.1	77bps	
PAT margin (%)	18.2	17.4	74bps	15.7	242bps	16.3	15.1	116bps	
<b>TVSL</b>									
Sales	54,038	53,914	0.2	56,194	(3.8)	1,49,575	1,14,286	30.9	Despite lower sales volume, strong price realisation and better product mix are expected to help TVSL post flattish YoY revenue growth. RM cost inflation and higher staff cost are likely to dent EBITDA and PAT margins by 38bps/50bps YoY. We expect adj. PAT to decline 10% YoY. Key monitorables are 3W demand, product launch pipeline, export performance and cost-cutting initiatives.
EBITDA	4,917	5111	(3.8)	5,629	(12.6)	13,284	8,924	48.8	
Adj PAT	2,385	2,656	(10.2)	2,776	(14.1)	5,994	3,228	85.7	
EBITDA margin (%)	9.1	9.5	(38bps)	10.0	(92bps)	8.9	7.8	107bps	
PAT margin (%)	4.4	4.9	(51bps)	4.9	(53bps)	4.0	2.8	118bps	

Company (Rs mn)	Q3FY22E	Q3FY21	YoY (%)	Q2FY22	QoQ (%)	9MFY22E	9MFY21	YoY (%)	Remarks
<b>VSTT</b>									Since restrictions were imposed on tiller imports from China, VSTT has witnessed a sharp jump in tiller demand. Tiller volumes were up 6% YoY while tractors declined by 16% YoY due to a high base. We expect revenue to grow 4% YoY while a lower gross margin is likely to cause EBITDA margin contraction of 70bps YoY. Adj. PAT is estimated at Rs 266mn, a YoY decline of 14%. Key monitorables are plans to increase market share in tillers and high-HP tractors as well as in the export market.
Sales	2,113	2,029	4.2	2,335	(9.5)	6,384	5,695	12.1	
EBITDA	296	299	(0.8)	384	(22.9)	934	839	11.3	
Adj PAT	266	308	(13.8)	322	(17.3)	827	778	6.3	
EBITDA margin (%)	14.0	14.7	(70bps)	16.4	(243bps)	14.6	14.7	(11bps)	
PAT margin (%)	12.6	15.2	(262bps)	13.8	(119bps)	13.0	13.7	(71bps)	
<b>AL</b>									Volumes inched up 2% YoY in Q3 as 16% growth in MHCVs was partially set off by a 12% decline in LCVs. We expect AL's revenue to grow higher than volumes primarily due to better price realisation and product mix. Despite a stronger topline, RM cost pressure is likely to hamper EBITDA margins. We expect AL to post a net profit for the first time in several quarters at Rs 31mn.
Sales	56,808	48,135	18.0	44,579	27.4	1,30,897	83,010	57.7	
EBITDA	2,556	2,538	0.7	1,347	89.8	2,502	10	25,433.5	
Adj PAT	31	267	(88.5)	(832)	(103.7)	(3,608)	(5,055)	(28.6)	
EBITDA margin (%)	4.5	5.3	(77bps)	3.0	148bps	1.9	0.0	190bps	
PAT margin (%)	0.1	0.6	(50bps)	(1.9)	192bps	(2.8)	(6.1)	333bps	

Source: Company, BOBCAPS Research

**Fig 2 – Quarterly volume trends**

Company	Q3FY22	Q3FY21	YoY (%)	Q2FY22	QoQ (%)
<b>MSIL</b>	<b>4,30,668</b>	<b>4,95,897</b>	<b>(13.2)</b>	<b>3,79,541</b>	<b>13.5</b>
Domestic	3,65,673	4,67,369	(21.8)	3,20,133	14.2
Exports	64,995	28,528	127.8	59,408	9.4
<b>AL</b>	<b>34,077</b>	<b>33,408</b>	<b>2.0</b>	<b>27,543</b>	<b>23.7</b>
HCVs	19,305	16,584	16.4	13,514	42.9
LCVs	14,772	16,824	(12.2)	14,029	5.3
<b>MM</b>	<b>2,13,634</b>	<b>2,23,978</b>	<b>(4.6)</b>	<b>1,90,600</b>	<b>12.1</b>
Auto	1,20,667	1,22,277	(1.3)	1,01,680	18.7
Tractors	92,967	1,01,701	(8.6)	88,920	4.6
<b>ESC</b>	<b>25,325</b>	<b>31,562</b>	<b>(19.8)</b>	<b>21,073</b>	<b>20.2</b>
Domestic	23,321	30,072	(22.4)	18,950	23.1
Exports	2,004	1,490	34.5	2,123	(5.6)
<b>VSTT</b>	<b>9,179</b>	<b>9,170</b>	<b>0.1</b>	<b>10,951</b>	<b>(16.2)</b>
Power Tillers	7,136	6,734	6.0	8,626	(17.3)
Tractors	2,043	2,436	(16.1)	2,325	(12.1)
<b>HMCL</b>	<b>12,92,136</b>	<b>18,45,274</b>	<b>(30.0)</b>	<b>14,38,623</b>	<b>(10.2)</b>
Motorcycles	12,12,004	16,89,034	(28.2)	13,34,152	(9.2)
Scooters	80,132	1,56,240	(48.7)	1,04,471	(23.3)
Exports (of above)	61,010	53,147	14.8	72,816	(16.2)
<b>BJAUT</b>	<b>11,81,361</b>	<b>13,06,810</b>	<b>(9.6)</b>	<b>11,44,407</b>	<b>3.2</b>
Motorcycles	10,48,545	11,93,867	(12.2)	10,29,915	1.8
3W	1,32,816	1,12,943	17.6	1,14,492	16.0
Exports (of above)	6,58,062	6,87,111	(4.2)	6,12,191	7.5
<b>TVS</b>	<b>8,78,659</b>	<b>9,89,517</b>	<b>(11.2)</b>	<b>9,16,705</b>	<b>(4.2)</b>
2W	8,34,768	9,51,879	(12.3)	8,69,552	(4.0)
3W	43,891	37,638	16.6	47,153	(6.9)
Exports (of above)	2,94,611	2,60,863	12.9	3,15,319	(6.6)
<b>EIM</b>	<b>1,85,570</b>	<b>2,12,470</b>	<b>(12.7)</b>	<b>1,38,561</b>	<b>33.9</b>
2W	1,69,526	1,99,668	(15.1)	1,23,427	37.3
Truck and buses	16,044	12,802	25.3	15,134	6.0

Source: Company, BOBCAPS Research

**Fig 3 – Commodity trends**

Particulars	Units	Q4FY20	Q1FY21	Q2FY21	Q3FY21	Q4FY21	Q1FY22	Q2FY22	Q3FY22
<b>Aluminium LME</b>	<b>(\$/t)</b>	<b>1,687</b>	<b>1,500</b>	<b>1,709</b>	<b>1,924</b>	<b>2,097</b>	<b>2,400</b>	<b>2,651</b>	<b>2,756</b>
YoY (%)		(9.4)	(16.4)	(3.1)	9.5	24.3	60.0	55.2	43.2
QoQ (%)		(4.0)	(11.1)	13.9	12.6	9.0	14.4	10.5	3.9
<b>Lead LME</b>	<b>(\$/t)</b>	<b>1,841</b>	<b>1,679</b>	<b>1,874</b>	<b>1,906</b>	<b>2,010</b>	<b>2,130</b>	<b>2,333</b>	<b>2,327</b>
YoY (%)		(9.5)	(10.8)	(7.8)	(6.4)	9.2	26.8	24.5	22.1
QoQ (%)		(9.6)	(8.8)	11.6	1.7	5.4	6.0	9.5	(0.2)
<b>India CR Coil IS513 1.0mm In warehouse Mumbai</b>	<b>(Rs/t)</b>	<b>42,300</b>	<b>40,735</b>	<b>44,574</b>	<b>54,902</b>	<b>65,633</b>	<b>75,400</b>	<b>77,265</b>	<b>74,182</b>
YoY (%)		(5.8)	(9.3)	7.3	41.7	55.2	85.1	73.3	35.1
QoQ (%)		9.1	(3.7)	9.4	23.2	19.5	14.9	2.5	(4.0)
<b>India HR Coil IS2062 3.0mm In warehouse Mumbai</b>	<b>(Rs/t)</b>	<b>37,915</b>	<b>37,206</b>	<b>39,294</b>	<b>45,961</b>	<b>55,641</b>	<b>64,469</b>	<b>66,192</b>	<b>67,515</b>
YoY (%)		(11.0)	(10.4)	3.2	33.0	46.7	73.3	68.5	46.9
QoQ (%)		9.7	(1.9)	5.6	17.0	21.1	15.9	2.7	2.0
<b>Brent</b>	<b>(USD/bbl)</b>	<b>52</b>	<b>42</b>	<b>47</b>	<b>47</b>	<b>57</b>	<b>66</b>	<b>70</b>	<b>78</b>
YoY (%)		(15.1)	(30.7)	(17.6)	(17.6)	10.1	55.7	48.4	66.9
QoQ (%)		(8.5)	(18.9)	12.2	(1.0)	22.2	14.7	6.9	11.4
<b>Rubber RSS4</b>	<b>(Rs/100kg)</b>	<b>13,333</b>	<b>12,491</b>	<b>13,131</b>	<b>15,265</b>	<b>15,882</b>	<b>16,863</b>	<b>17,344</b>	<b>17,645</b>
YoY (%)		6.1	(9.8)	(7.7)	20.0	19.1	35.0	32.1	15.6
QoQ (%)		4.8	(6.3)	5.1	16.2	4.0	6.2	2.9	1.7
<b>USD/INR</b>		<b>13,333</b>	<b>12,491</b>	<b>13,131</b>	<b>15,265</b>	<b>15,882</b>	<b>16,863</b>	<b>17,344</b>	<b>17,645</b>
YoY (%)		6.1	(9.8)	(7.7)	20.0	19.1	35.0	32.1	15.6
QoQ (%)		4.8	(6.3)	5.1	16.2	4.0	6.2	2.9	1.7

Source: Bloomberg, BOBCAPS Research

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**Note:** Recommendation structure changed with effect from 21 June 2021

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