

A Study on Fundamental Analysis of Select Automobile Companies

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Abstract – Fundamental analysis is stock valuation method used to find the financial healthiness of the company by analysing the impact of macroeconomic variables on stock market, considering the various trends, opportunities, challenges of the industry in which the company operates and assessing the projected performance of the company. This study not only restricted to financials but also focused on other Qualitative factors of the company.

The study selected four automobile companies viz., Ashok Leyland, Tata motors, Mahindra & Mahindra and Force motors and analysed their financial data from 2015-19 with help of various financial ratios and finally selected Mahindra & Mahindra for conducting fundamental analysis. The study considered variables like Earnings Multiples, Growth, EPS etc.

Keywords: Intrinsic Value, Financial Ratios

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INTRODUCTION

Fundamental analysis is used to calculate the true intrinsic value of a share and to find opportunities where that share value differs from its current market price. In order to do this, fundamental analysis looks at economic factors, known as fundamentals. These fundamentals are mainly found in the company's financial reports, as well as reports about various macro-economic indicators and variables.

Fundamental approach is also known as E – I – C approach. Researchers have found that stock price changes can be attributed to the various factors.

E – Economic analysis (30 – 35%)

I – Industrial analysis (16 – 20%)

C – Company analysis (30 – 35%)

Other factors (15 – 25%)

Based on the above evidence, a commonly advocated procedure of fundamental analysis, which is a three steps examination, calls for: Understanding the macroeconomic environment and developments.

Analysing the prospects of the industry to which the firm belongs. Assessing the projected performance of the company.

OBJECTIVES OF THE STUDY

- To understand the macroeconomic variables this makes an impact on the company progress.
- To study the various trends, opportunities, challenges of the industry in which the company operates.
- To identify with the various policies of the company this makes an impact on the financial narration of the company.
- To find the inherent value of the select automobile companies stock viz., Mahindra & Mahindra, Ashok Leyland, Tata motors, and Force motors and evaluate with market value of the study.

RESEARCH METHODOLOGY

Exploratory: the study is exploratory since the same is based on secondary sources

Analytical:

- Ratio analysis of four companies 2) In accordance to the performance one of four companies is derived from ratio analysis is selected for the valuation

Assumptions:

- The primary assumption of Fundamental Analysis is that the price on the stock market may not fully reflect a stock's "real" value.
- The second major assumption of Fundamental Analysis is that in the long run, the stock market will reflect the intrinsic value.

Sources of Data:

Majority of the data used for the study has been collected from secondary sources like Company Annual Reports, NSE India, Journals etc.

Sample size

Four companies are selected from the automobile sector because they have registered large performance together in domestic and foreign market (Ashok Leyland, Tata motors, Mahindra & Mahindra and Force motors and therefore finance data is collected from 2015-19 (5 year's data)

LIMITATIONS OF THE STUDY

The study has been done on the basis of 4 companies from the automobile sector. for this reason results cannot be generalized to other companies in the same sector. Long-term investment. Need another tools to know the entry point

Since fundamental analysis is based on the past data, all the results cannot be taken as full proof to take future decisions. If a stock looks financially healthy and is relatively cheap compared to its peers, that doesn't mean that it will always rise in value.

REVIEW OF LITERATURE

Meena & Preeti study on prediction of stock returns for growth firms concluded that investment strategies based on traditional and growth fundamentals are effective in identifying extreme performers and also effective in identifying excess return earned by high group firms in one and two years ahead period.

Viswantha & Viswa study on Intrinsic value Estimation through Fundamental Analysis examined stock prices changes can be attributed to the various factors, such as Economy-wide factors:30-35%; Industry factors:15-20%; Company factors:30-35%; Other factors:15-25%. The researcher in this study is

confined to the third phase of fundamental company analysis and assessed the projected performance of the company and find the intrinsic value of the company by using two principle methods dividend discount model and the earnings multiplier.

Baresa & Bogdan study on stock valuation by using Fundamental analysis examined future and present data in order to estimate the fair stock market value and to predict future value. It usually begins by analyzing the macroeconomic environment, analyzing sectors and then financial statements in order to determine the real value of the company.

Garg & Karla study on impact of macroeconomic factors on Indian Stock Market investigated the impact of macroeconomic variables and concluded that the govt. and the policy makers need to make strategies and policies that complement with macroeconomic framework and further support the Indian stock market.

DATA ANALYSIS

The following part examines the financial ratios of select automobile companies in the study. In this section, four categories of financial ratios are considered for analysis viz., Liquidity Ratios, Activity Ratios, Solvency Ratios, Profitability Ratios, Growth rates.

Table 1: Financial Ratios (2015-19) –Overall Framework

S. No		ASHK	M&M	TML	FORCE	Industry Avg.	Ideal Ratio
A	Liquidity Ratios						
1	Current ratio	1.01	1.25	1.01	1.64	1.31	2.00
2	Quick ratio	0.79	1.00	0.71	0.98	1.00	1.00
B	Activity Ratios						
3	Inventory turnover	10.54	9.00	8.11	6.60	14.44	
5	Asset turnover	1.26	0.75	1.01	1.29	1.15	2.00
6	Working capital turnover	13.76	5.20	60.74	5.13	8.69	
7	Avg. Collection period	20.30	31.53	18.89	13.99		30 to 36
C	Solvency Ratios						
8	Debt-to-assets ratio	0.43	0.37	0.28	0.08	0.21	Low
9	Debt-to-capital ratio	0.78	0.70	0.61	0.12	0.40	Low
10	Debt-to-equity ratio	1.85	1.36	1.19	0.12	0.78	Low
D	Profitability Ratios (%)						
13	Gross Profit Margin (GP)	32.19	39.10	43.10	23.07	36.36	High
14	Operating profit margin (EBIDTA)	8.68	10.74	7.21	3.95	8.41	High
15	Profit before tax margin (PBT)	5.12	7.96	5.90	5.87	7.45	High
16	Net profit margin (PAT)	3.62	5.51	4.18	4.61	5.54	High
17	Return on assets (ROA)	3.43	4.51	4.50	6.30	7.12	High
18	Return on equity (ROE)	15.26	16.81	18.51	9.52	22.26	High
19	Return on Investment (ROI)	5.88	7.61	7.82	9.02	11.93	High
E	Growth Rate (%)						
20	Earnings per share (EPS)	29.96	15.58	-2.88	59.14	14.29	
21	Sales	19.09	6.31	9.37	12.35	16.05	

Interpretation of Ratio Analysis (Table 1)

As per the analysis MAHINDRA & MAHINDRA stands out to be the best among the four sample companies, because M&M has convincing Profitability ratios with 1st position even having less growth in sales among the peer, the company is enjoying considerable profits even though the average collection period is more but this is offset with less inventory holding period among the peer companies.

PROCESS OF ANALYSIS:

When compared with the various ratios during the year 2018. M&M has maintained consistency its

second position in terms of all the ratios, compared to the sample.

M&M had a less sales growth during the study period, but it could maintain a steady growth in terms of profitability.

M&M having less operating expenses when compared to the peer companies that's why it is achieving more growth in profitability ratios.

When the performance was compared with industry average, it indicates that M&M in case of many ratios, it had maintained above the industry average. This is an indication of less risk for the investors.

When compared with ideal ratio, especially the ratios which are below the industry average, it shows that the performance is either on par or above the ideal ratio. Hence investors can be assured of less risk in their investment.

Based on the ratio analysis, M&M selected for conducting fundamental analysis.

Table 2: Valuation of Mahendr & Mahendra

Particulars	Mar'14		Mar'15		Mar'16		Mar'17		Mar'18		Mar'20 Projections	
	Mar'14	Mar'15	Mar'16	Mar'17	Mar'18	Mar'19	Mar'20	Mar'20	Mar'20	Mar'20	Mar'20	Mar'20
Net Sales	68,735.66	74,000.93	71,948.59	75,841.42	83,773.05	92,093.95	97,746.34					
Other Income	841.44	822.94	799.93	521.05	730.10	631.03						
Stock Adjustments	220.36	238.97	(274.13)	458.51	13.83	83.33						
Total Income	69,797.46	75,062.84	72,474.39	76,820.98	84,516.98	92,808.31	97,746.34					
Raw Materials	42,531.00	45,593.78	42,982.35	45,904.25	50,080.50	53,457.29	55,913.74					
Power & Fuel Cost	936.88	923.38	786.96	639.97	657.06	986.32	981.84					
Employee Cost	6,819.07	6,885.94	7,146.55	7,689.40	8,910.63	10,004.62	9,198.45					
S&A Expenses	-	-	-	871.93	723.40	760.94	807.64					
Miscellaneous Expenses	9,553.28	10,716.64	11,965.31	11,111.94	12,345.58	13,736.33	14,544.50					
Total Expenses	59,840.23	64,119.74	62,881.17	66,217.49	72,717.17	78,945.50	81,446.17					
Operating Profit	8,895.43	9,881.19	9,067.42	9,623.93	11,055.88	13,148.45	16,300.18					
PBDIT	9,957.23	10,943.10	9,593.22	10,603.49	11,799.81	13,862.81	16,300.18					
Interest	2,297.00	2,953.93	3,156.69	3,367.59	3,648.46	3,987.09	4,463.68					
PBDT	7,660.23	7,989.17	6,436.53	7,235.90	8,151.35	9,875.72	11,836.50					
Depreciation	2,079.86	2,169.57	2,123.83	2,441.65	2,809.11	3,279.90	2,851.89					
PBT	5,580.37	5,819.60	4,312.70	4,826.00	5,789.35	6,595.82	8,984.60					
Tax	1,934.63	1,496.22	1,720.02	2,117.53	2,299.73	2,367.73	2,695.38					
Net Profit	3,645.74	4,323.38	2,592.68	2,708.47	3,489.62	4,228.09	6,289.22					
EPS (Rs)	59.38	70.20	41.74	47.58	61.30	37.14	55.24					
P/E Ratio		12.96	29.48	26.20	21.63	32.22						

Table 3: Growth Performance of M&M

Year	Return On Equity (%)	Retention Ratio (%)	Book Value per share (Rs.)	Earnings per share (Rs.)	Dividend Pay-out Ratio (%)	Dividend per share (Rs.)
2014	20.12	64.58	78.963	39.53	35.42	14.00
2015	10.61	54.77	87.42	26.53	45.23	12.00
2016	10.4	58.78	97.97	29.11	41.22	12.00
2017	11.28	61.91	109.77	34.13	38.09	13.00
2018	20.74	89.15	67.7	69.14	10.85	7.50
Average	14.63	65.838	88.3646	39.688	34.162	11.7

Table:4 Compounded Annual Growth Rate of M&M

CAGR of Sales	4%
CAGR of EPS	12%
CAGR of DPS	13%
CAGR of BV Per share	3%
CAGR of Net worth	1%

Explanation from Table 4:

The compound annual growth rate in sales was recorded at 4 %.

The CAGR in EPS was recorded at 12.00 % over the study period.

The CAGR in dividend per share is 13.00%, as the company doesn't have stable dividend policy. But from the past 5 years' company is giving on an average 230 % dividend

Book value per share grew at the CAGR of 3 % over the study period.

The net worth of the company grew at the CAGR of 1% over the study period

Table 5: Sustainable Growth rate of M&M

Year	Retention Ratio (%)	Return On Equity (%)	SWR=Avg RR*Avg ROE
2014	0.6458	20.12	
2015	0.5477	10.61	
2016	0.5878	10.4	
2017	0.6191	11.28	
2018	0.8915	20.74	
Average	0.65838	14.63	9.63

Calculation of Intrinsic Value of M&M

Table 6: Constant growth Dividend Model of M&M

particulars	Ratios
Avg Dividend Pay-out ratio	34.16
Required Rate of Return	29.57
Expected Growth Rate in Dividends	9.63
PE Ratio	1.71

Table 7: Historical Analysis of M&M

particulars	Ratios
Avg. PE Ratio	26.68
Weighted PE Ratio	14.20
Intrinsic Value (At 10% Growth)	906.14
At 9% Growth	815.92

Intrinsic value range B/W 815.526<906.14>996.75

OBSERVATIONS

Growing steel price and other inputs has the major concern for the company from its margins point of view. So company may have control over the steel prices.

As the company is active in the overseas markets, an appreciation of Rupee against the foreign currencies, especially dollar would adversely affect the profit margin of the company.

Increase in the fuel prices on account of rising global crude oil prices would affect the domestic demand especially for CVs.

Discounts, special editions and festival based offers may be manoeuvred to boost the sales of the company.

Various new products launches have helped retain customer focus on the new auto market, so the company may focus on this particular aspect.

Another trend that would have been in the near future is rise in the EVs and HEVs vehicle sales. With infrastructure facilities increasing more people may prefer the EVs and Government also might be supporting through subsidies and tax reduction etc. for EVs and hence the company may try to specialize in that particular segment.

CONCLUSION

The most important strength in today's volatile financial market is information. Investors always confused on the information as to where to invest, when to invest and how much to invest their money.

From the above Value anchor and value range, the following decision rules can be considered. If the share price is Less than Rs.815.526; Buy the stock of M&M Between Rs.815.526 to Rs.996.75; Hold the stock of M&M

More than Rs.996.75; sell the stock of M&M

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