

Chairman's Letter



Dear Shareholder,

I began the practice of writing the Chairman's letter in the Annual Report of 1998-99. These have been fairly detailed letters, where I have attempted to share with you the results of your company as well as our plans for the future.

Simultaneously, the chapter on Management Discussion and Analysis (MD&A) in every successive annual report has contained increasingly detailed data on markets, operations and financials. Given the kind of detail that you can read in that chapter, I have decided on an abbreviated letter this year — one in which I will share a few of our aspirations.

But before doing so, I would be failing in my duty if I were not to congratulate the management team for Bajaj Auto's excellent results in 2002-03.

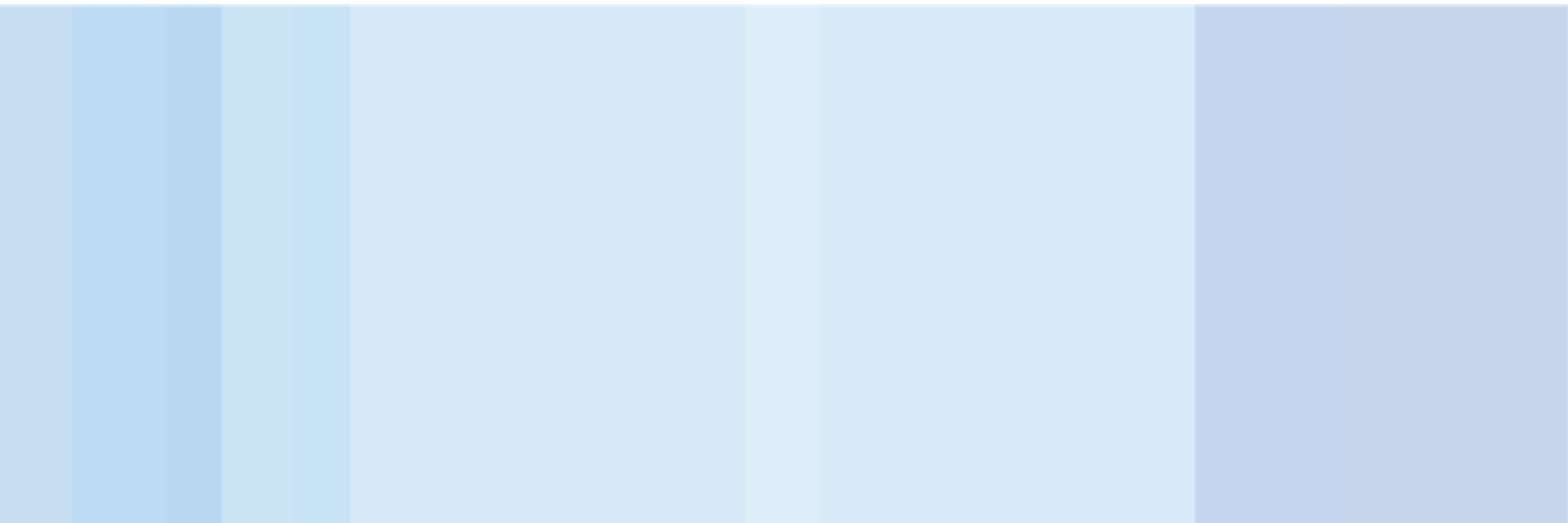
At Rs.50.71 billion, your company's turnover in 2002-03 touched an all time high. So did operating profits (EBITDA) — Rs.8.17 billion in 2002-03. Your company's margins are again the

highest in the industry. Return on operating capital, which had dipped to a low of 14 per cent in 2000-01, has now increased to a healthy 60 per cent. And our exports have more than doubled, making Bajaj Auto a significant net earner of foreign exchange.

We have executed a skilful turnaround from the difficult days of 2000-01, and are poised for a period of rapid growth in sales and profits.

Having said this, let me discuss something about the motorcycle segment. Your company has done excellently in motorcycles. With its Boxers and the newly introduced "BYK", Bajaj Auto is the clear market leader in the entry level / utility segment of motorcycles. And the Pulsar models have made your company the market leader by far in the premium segment as well.

Going forward, our greatest challenge will be to substantially increase our presence in the large and rapidly growing executive segment. Today, we account for only 7 per cent of this segment. To face



tomorrow's competition, we have to substantially increase this share. Hopefully, the new Caliber 115 (popularly called "Hoodibabaa") will be a vanguard of growth in this market. We are also going to introduce a new 125 cc "World Bike" — jointly with Kawasaki. I sincerely hope that these two models, and our other planned launches, will give us a strong position in this executive segment, and thus complement our leading status at the entry and premium levels.

I feel that we have another 15 to 18 months to further strengthen our prime position at the entry level and the premium segments and significantly ramp up our market share in the executive segment. By the end of 2004, virtually every international motorcycle major will treat the Indian market as their playing field, and we at Bajaj Auto have to be proactively prepared for this. Believe me, we will be seeing the "mother of all battles" in the two-wheeler space. My youthful management team and the old combatant in me are relishing the challenge.

Now for a few words on scooters. Last year, in my Chairman's letter, I had predicted that "we have probably succeeded in arresting the decline in the sales of geared scooters". I was wrong. As the chapter on MD&A shows, both the industry's and Bajaj Auto's sale of geared scooters continued to fall in 2002-03.

While I clearly recognise the importance of driving the motorcycle market, I still refuse to believe that the days of scooters are over. We need to combine the qualities of motorcycles and those of scooters in radically new models. Your company is now engaged in such a project. The "scooterwalla" in me is waiting to see the outcome.

Let me end by reiterating my views on future competition. Of the few large markets in the world, only China's and India's GDP have grown at an average rate in excess of 5.5 per cent per year over the last decade. Therefore, India will be a large and attractive market for all international players. It is important to remember that most of them have

deep pockets and, if past experience is an indicator, they are more than willing to take hits for a long time in order to establish a strong market presence.

We at Bajaj Auto recognise this. We also recognise that the only lasting competitive advantage is higher and higher quality at affordable cost. Therefore, we are continuously focusing on the details that make for quality — research and design for products and manufacturing processes. We are concentrating on quantum increases in productivity and throughput as well as vendor improvements so as to reduce costs. And we need to fire on all cylinders — motorcycles, scooters, and three-wheelers.

Bajaj Auto has been around long enough to see many ups and downs. After its successful turnaround from 2001-02, I am confident that your company will deal with tomorrow's competition at least as well as, if not better, than others.

Let me thank you for your constant support to Bajaj Auto. Here's to an even better 2003-04.



Rahul Bajaj

Chairman and Managing Director

Board of Directors

Rahul Bajaj
Chairman and Managing Director

Madhur Bajaj
Vice Chairman and Whole-time Director

D S Mulla
(upto 31 March 2003)

Kantikumar R Podar

Atul C Kirloskar
(upto 23 October 2002)

Shekhar Bajaj

D J Balaji Rao

D S Mehta
Whole-time Director

J N Godrej

S H Khan

Rajiv Bajaj
Joint Managing Director

Suman Kirloskar (Ms)
(w e f 23 October 2002)

Naresh Chandra
(w e f 15 January 2003)

Nanoo Pamnani
(w e f 14 May 2003)

Management

1 Rahul Bajaj
Chairman and Managing Director

2 Madhur Bajaj
Vice Chairman

3 Rajiv Bajaj
Joint Managing Director

D S Mehta
Whole-time Director

4 R A Jain
Executive Director

5 Ranjit Gupta
Vice President (Insurance)

6 C P Tripathi
Vice President (Operations)

7 R L Ravichandran
Vice President (Business
Development and Marketing)

8 N H Hingorani
Vice President (Materials)

9 P B Menon
Vice President (Projects)

10 Sanjiv Bajaj
Vice President (Finance)

Company Secretary

J Sridhar

Auditors

Dalal & Shah
Chartered Accountants

International Accountants

KPMG

Cost Auditor

A P Raman
Cost Accountant

Bankers

Central Bank of India

State Bank of India

Citibank N A

Standard Chartered Bank

Bank of America

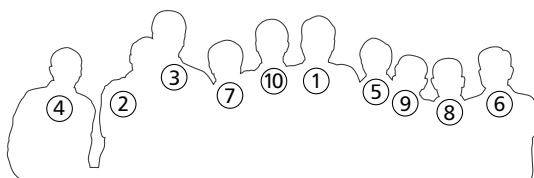
Registered under the
Indian Companies Act, VII of 1913

Registered Office

Akurdi, Pune 411 035

Works

- Akurdi, Pune 411 035
- Bajaj Nagar, Waluj,
Aurangabad 431 136
- Chakan Industrial Area, Chakan,
Pune 410 501



Management Discussion and Analysis

For the last three years, Bajaj Auto's Annual Report and its chapter on Management Discussion and Analysis has focused on the process of "change" — in products, in marketing, in manufacturing operations, in technology and R&D, and in the company's overall business strategy. The objective was to share with you the transformation that was occurring within the company to successfully overcome greater competition in the future.

Change, however, is a journey — a continuous process of re-engineering the DNA of a corporation. It does not stop after three years. Therefore, we want to remain with this theme for 2002-03, and show you how changes that began two to three years ago have begun to yield results. We also want to outline further changes that you can expect from Bajaj Auto in the next few years, and why these are necessary for the company.

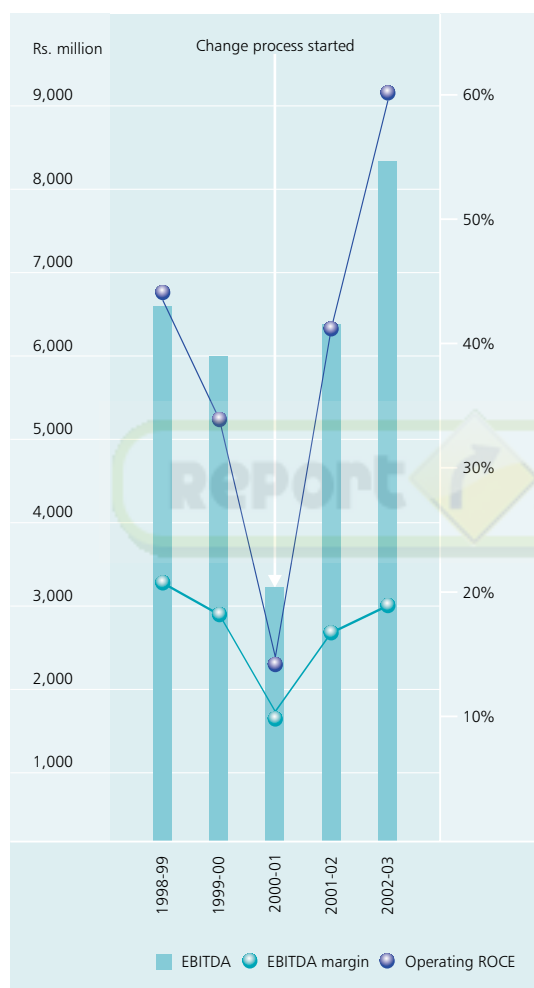
Let's begin with some of Bajaj Auto's results for 2002-03, which relate to the manufacturing side of the business.

- The company has achieved its highest ever sales. Sales grew by 15 per cent — from Rs.41.26 billion in 2001-02 to Rs.47.44 billion in 2002-03.
- Highest ever operating profits. Earnings before interest, taxes, depreciation and amortisation (EBITDA) increased by 32 per cent — from Rs.6.21 billion in 2001-02 to Rs.8.17 billion in 2002-03.
- Operating EBITDA margins increased from a low of 9.8 per cent in 2000-01 to 16.8 per cent in 2001-02 to 19 per cent in 2002-03.
- Pre-tax return on operating capital rose by 19 percentage points — from 41 per cent in 2001-02 to 60 per cent in 2002-03.

These numbers indicate that Bajaj Auto's change process has already begun to yield stronger financial results. Chart A gives a flavour of the turnaround.

We shall be discussing the company's financial performance in a later section. As before, this chapter is in three parts. The first analyses markets and sales across the various product segments; the second part focuses on operations; and the third on the financials.

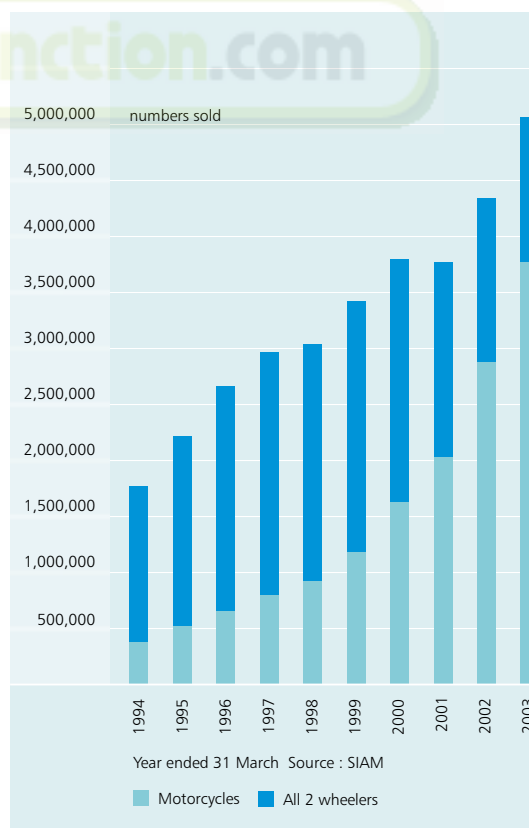
CHART A: Turnaround in profitability



Markets

It will be useful to start this section with the market for two-wheelers. Chart B plots the market for motorcycles and total two-wheelers. As the chart clearly shows, while the two-wheeler market has grown at a compound annual rate of 11.7 per cent between 1994 and 2003, motorcycle sales exploded at a rate of 41 per cent per year. Consequently, from a market share of under 22 per cent in 1993-94, motorcycles now account for over 74 per cent of India's two-wheeler sales. Indeed, this share of motorcycles grew by over 8 percentage points between 2001-02 and 2002-03 — from 66.2 per cent to 74.3 per cent. Simply put, motorcycles is the name of the game. Table 1 and Chart C underscore the point.

CHART B: Industry's sale of two wheelers



Motorcycles

TABLE 1: Changing composition of the two-wheeler market (vehicles sold)

Year ended 31 March	All two-wheelers	Motorcycles	Ung geared scooters	Geared scooters	Mopeds	Step-thrus
1994	1,763,210	21.6%	7.9%	43.3%	17.6%	9.6%
1995	2,208,231	23.9%	8.6%	42.6%	15.1%	9.8%
1996	2,660,005	24.8%	9.1%	40.6%	16.8%	8.7%
1997	2,965,474	27.1%	8.9%	38.4%	16.6%	9.1%
1998	3,042,347	30.0%	8.8%	35.4%	15.5%	10.3%
1999	3,403,471	34.6%	8.3%	32.7%	14.6%	9.8%
2000	3,776,719	42.7%	10.0%	25.9%	14.0%	7.3%
2001	3,745,516	54.1%	10.9%	16.0%	12.9%	6.1%
2002	4,318,531	66.2%	9.5%	12.3%	8.7%	3.3%
2003	5,053,562	74.3%	10.5%	6.6%	6.2%	2.2%

Source : SIAM

Given the critical role of motorcycles, it is important to share what Bajaj Auto has done and proposes to do in this market segment. Since 1997-98, we had to shrug off our image of being a manufacturer of traditional metal-bodied geared scooters by systematically introducing motorcycles that could combine the company's historical selling points of ruggedness, fuel economy and price competitiveness with style, performance and comfort. As Table 2 shows, Bajaj Auto has clearly succeeded in this endeavour. Between 1997-98 and 2002-03, we have increased our share in an explosively growing, highly discerning market from under 15 per cent to over 23 per cent. Today, Bajaj Auto is the clear number two in motorcycles.

CHART C: Industry's sales of two-wheelers, segment-wise

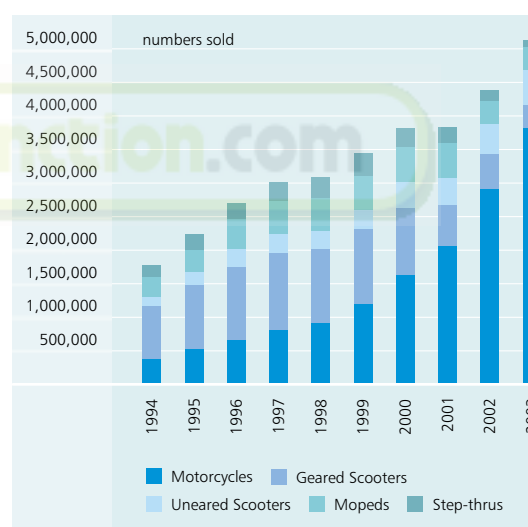


TABLE 2: Growth in Bajaj Auto's market share for motorcycles (in numbers)

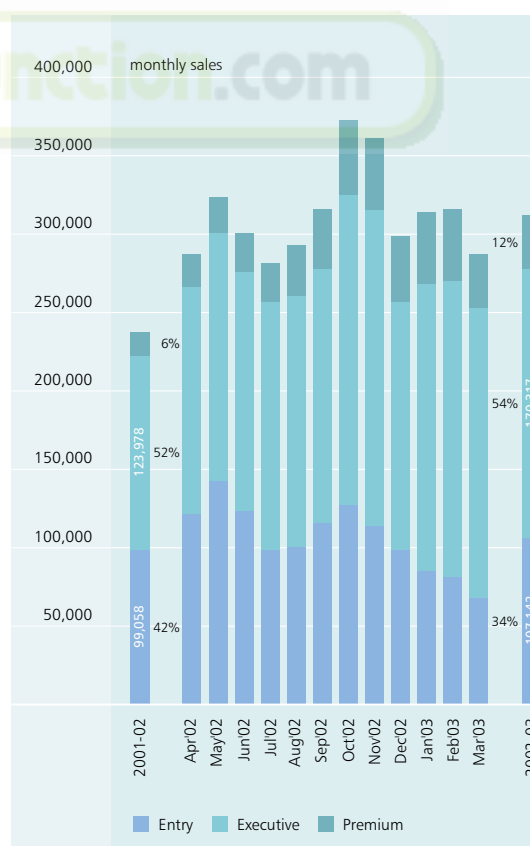
Year ended 31 March	Market	BAL	Growth of the Market	Growth of BAL's sales	BAL's market share
1994	380,558	42,080	25.2%	21.4%	11.1%
1995	528,043	75,087	38.8%	78.4%	14.2%
1996	660,672	89,675	25.1%	19.4%	13.6%
1997	802,266	129,263	21.4%	44.1%	16.1%
1998	913,956	136,017	13.9%	5.2%	14.9%
1999	1,176,779	200,183	28.8%	47.2%	17.0%
2000	1,612,895	255,176	37.1%	27.5%	15.8%
2001	2,033,196	422,016	26.1%	65.4%	20.8%
2002	2,861,375	656,018	40.7%	55.4%	22.9%
2003	3,757,125	868,138	31.3%	32.3%	23.1%

Having shown that Bajaj Auto has been steadily gaining market share for motorcycles, it is necessary to go into greater details of this important segment. In last year's Annual Report, we had segregated the market in four broad segments. Except for some changes at the margin, categorisation for motorcycles more or less remains the same:

- **Entry level — models priced between Rs.27,000 and Rs.37,000.** We are firmly placed in this category with the entire family of Boxers (AT, CT and AR), as well as our new 100 cc BYK model introduced in December 2002.
- **Executive category — models priced between Rs.38,000 and Rs.45,000.** These are models with Japanese and European standards of engineering, styling, manufacturing and riding comfort. We have the "Hoodibabaa" Caliber 115, and we propose to launch the World-Bike, developed in India with Kawasaki for the global market.
- **Premium category — models priced above Rs.45,000.** We have the Pulsar 150, Pulsar 150 ES, the Pulsar 180 and, in the super-premium, the Eliminator.

It is necessary to focus on these three segments individually and see how these sub-markets have moved in the last year. Chart D shows the trends.

CHART D: Monthly sales of motorcycles segment-entry level, executive, premium



As Chart D shows, in 2001-02, the industry's average sales in the entry level segment was a bit over 99,000 per month, and accounted for 42 per cent of the number of motorcycles sold. Despite an 8 per cent growth in the volume of sales in 2002-03, the overall market share of this segment dropped to 34 per cent.

No doubt, poor monsoons of 2002 and lower farm incomes played a role in declining sales in this segment, especially since November 2002. Nevertheless, even in the best case scenario, it is unlikely that the market share of the entry-level category will exceed 40 per cent. That would still make it a market ranging between 1.4 million and 1.5 million motorcycles. However, we at Bajaj Auto believe that it will be an increasingly competitive market, especially at the upper end of this segment. As the clear leader accounting for 42 per cent of this market, how do we propose to fight competition and further increase our share?

In 2002-03, we sold 502,144 Boxers (ATs, CTs and ARs). It is the largest selling brand in the entry-level category, and the second largest selling two-wheeler brand in the country. In addition, in the four month period from December 2002 to March 2003, we succeeded in selling 32,815 BYKs. Together, these models accounted for 62 per cent of the volume of Bajaj Auto's motorcycle sales.

We don't propose to gain market share in this segment by needlessly triggering debilitating price wars. Instead, we are going to further cut manufacturing costs, work on scale economies, improve efficiencies, and pass on the resultant price benefits to our entry-level consumers. In addition, starting with the BYKs, Bajaj Auto will introduce a new range of variants in this segment —

motorcycles with adequate power, high fuel efficiency and high reliability.

Let's now move on to the very top end of motorcycles — the premium category. In 2002-03, almost 425,000 motorcycles were sold in this segment. With our Pulsar 150, 150 ES and 180, Bajaj Auto sold 183,743 vehicles in this segment, and accounted for 43 per cent of the market share. We are comfortably placed here as the clear market leader.

We propose to introduce an upgraded version of the Pulsar in the second quarter of 2003-04. This machine is designed to set new benchmarks in engine performance, fuel economy, handling, braking and ergonomics. With the Pulsar range we aim to increase the market size of this premium segment and also further increase our share.

That brings us to the huge middle — the executive segment. As Chart D shows, this market has grown by a staggering 37 per cent from an average sales of 124,000 units per month in 2001-02 to well over 170,000 units per month in 2002-03. Today, this market accounts for over 54 per cent of the volume of motorcycle sales. And, three factors — higher disposable urban incomes for progressively younger people, the desire to ride smartly styled, well performing, fuel efficient bikes, and extremely attractive retail finance schemes — have made this a very large, attractive and robustly growing segment.

In 2002-03, the executive segment accounted for the overall sales of 2.04 million motorcycles. Bajaj Auto accounts for 7 per cent of the total sales in this market, and we clearly need to substantially ramp up our presence in this segment. The new Caliber 115 (popularised as "Hoodibabaa") was

launched in March 2003. In its first month, it notched sales in excess of 25,000. Although it is too early to tell, we expect this model to make inroads in this market throughout 2003-04. In addition, we will be introducing the 125 cc World-Bike jointly designed with Kawasaki. This will be further supplemented by another model designed in-house, slated for a launch towards the end of 2003-04. With these three products, Bajaj Auto will operate at three distinct price points in the executive segment, which should allow the company to increase its presence in this category.

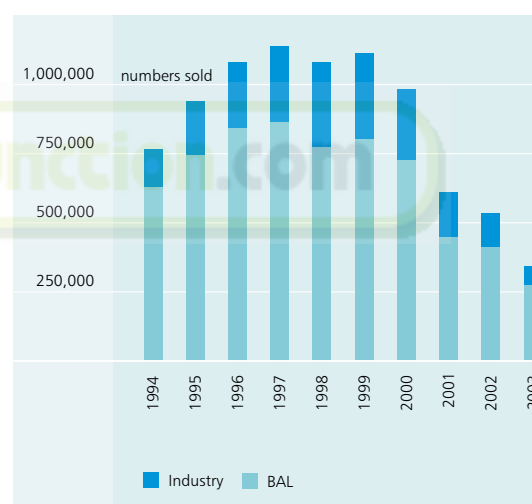
The philosophy that we have been following is in three parts. The first was, "Do what's Do-able". That led to the development, production and marketing of the Boxer models, which eventually resulted in our being the market leader in the entry level category. The second part was, "Do what's Unexpected". That led to the top-of-the-line Pulsar, and our quest to capture the high-end market with international quality. Now the stage is set to "Do what's Necessary" — to focus on populating the executive segment and gaining market share in this major category.

Geared Scooters

As Chart E shows, the geared scooter market continues to slump. In 2002-03, overall industry's sale of geared scooters fell to under 336,000 units — a decline of 37 per cent over the previous year. Bajaj Auto's sales fell by 34 per cent to 268,656 units. In last year's Management Discussion and Analysis, we had projected average monthly sales of 31,000 for 2002-03. We fell short by almost 28 per cent. The fact of the matter is becoming evident. Simply put, barring some pockets in North India, there is no appetite for the traditional geared

scooter. It would be all too easy to claim that, having hit the depth of 336,000 units, the market has finally bottomed out. Only the future will show whether this is true. The only thing that one can say with certainty is that if we were to produce a well priced model that is stylish, gives great fuel economy, riding comfort and reliability, Bajaj Auto would be able to grow this market once again. At present, we have begun working on new scooter projects that incorporate such attributes. Two models incorporating an entirely new approach to scooters will be unveiled at the Auto Expo in January 2004. It will then be seen how these do at the market place.

CHART E: Geared scooter sales continue to fall



Three-wheelers

After years of moderate growth, the three-wheeler industry has shown a 23 per cent growth over the previous year. Bajaj Auto has, more or less, grown in line with the industry by selling over 193,000 three-wheelers in 2002-03 — a growth of 21 per cent over the previous year. Our overall market share stands at 68.5 per cent, compared to almost 70 per cent in 2001-02.