

Sector: Automobiles
Result Update

	Change
Reco: Hold	↔
CMP: Rs. 79	
Price Target: Rs. 90	↔

↑ Upgrade ↔ No change ↓ Downgrade

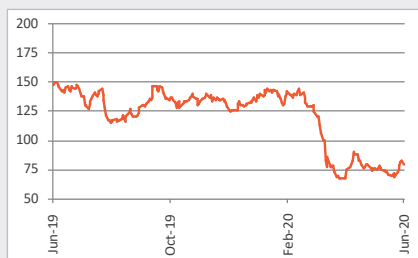
Company details

Market cap:	Rs. 1835 cr
52-week high/low:	Rs. 154/66
NSE volume: (No of shares)	2.6 lakh
BSE code:	501455
NSE code:	GREAVESCOT
Sharekhan code:	GREAVESCOT
Free float: (No of shares)	10.4 cr

Shareholding (%)

Promoters	54.8
FII	16.0
DII	10.6
Others	18.6

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	6.1	-34.1	-37.2	-47.1
Relative to Sensex	-2.8	-30.6	-22.1	-33.5

Sharekhan Research, Bloomberg

The Q4FY20 results of Greaves Cotton (Greaves) were lower than estimates across parameters. Earnings pressures are expected to sustain in near term as economic slowdown on account of COVID-19 would impact growth across segments. Moreover, negative operating leverage and pricing pressures from customers would impact margins. At CMP, the stock is trading at 14.4x FY22 earnings which is close to its long-term historical average of 16-17x. Hence, we retain our Hold rating on the stock with an unchanged PT of Rs 90.

Key positives

- ◆ Ampere vehicles (electric scooter business) was the only bright spot reporting a strong double-digit growth in Q4FY20 as compared to double-digit decline in other segments
- ◆ Tax rate during Q4FY20 was lower at 18.3% owing to deferred tax credit

Key negatives

- ◆ The topline of Greaves dropped sharply by 32% y-o-y in Q4FY20 and was below our estimates. While the automotive segment was impacted by transition from BS4 to BS6 emission norms, other businesses were impacted by lockdown due to COVID-19.
- ◆ Operating margins dipped sharply 480 bps y-o-y to 8.5% and were lower than estimates. Negative operating leverage due to a drop in topline and the inability to fully pass on cost increases related to the implementation of BS6 norms impacted the margins.

Our Call

Earnings pressure to sustain in near term; valuations close to historical average; retain Hold: Greaves volumes are expected to remain under pressure in the near term due to COVID-19 as well as steep cost increases due to transition from BS4 to BS6 emission norms. Negative operating leverage due to volume decline and the inability to fully pass on cost increases for the automotive segment would keep earnings under pressure in the near term. Q4FY20 results were below estimates across parameters. In order to factor volume and margin pressures in near term, we have cut our FY21 estimates by about 30%. We have reduced our FY22 estimates by 7%. The stock is trading at 14.4x FY22 earnings which is close to its long-term historical average of 16-17x. Hence, we retain our Hold rating on the stock with an unchanged PT of Rs 90.

Key Risks

Prolonged impact of coronavirus in India could impact the topline. Further, continued pricing pressures particularly from automotive OEM's can dent margins.

Valuation

Particulars	FY18	FY19	FY20E	FY21E	FY22E
Net sales (Rs cr)	1,792.1	2,015.3	1,911.0	1,759.0	2,032.0
Growth (%)	9.7	12.5	-5.2	-8.0	15.5
EBITDA (Rs cr)	255.3	272.2	210.1	175.0	229.8
OPM (%)	14.2	13.5	11.0	10.0	11.3
Adjusted PAT (Rs cr)	154.5	180.5	122.6	91.3	126.6
Growth (%)	-13.3	16.9	-32.1	-25.5	38.6
FD EPS (Rs)	6.3	7.5	5.4	4.0	5.5
P/E (x)	12.5	10.6	14.6	19.9	14.4
P/B (x)	2.0	2.0	2.6	2.8	3.0
EV/EBITDA (x)	5.5	5.4	7.5	9.2	7.3
RoE (%)	16.1	18.8	17.7	14.1	20.9
RoCE (%)	25.1	24.2	20.9	16.8	24.4

Source: Company; Sharekhan estimates

Results below estimates: Greaves Cotton Ltd (Greaves) Q4FY20 results were lower than estimates. The topline dropped 32% y-o-y to Rs 360 and was higher than our expectations of a drop of 8%. A steep fall in the automotive segment (about 35-40% of revenues) ahead of the transition from BS4 to BS6 emission norms & gensets and the pumpset segment due to lockdown on account of COVID-19 impacted the topline. Operating margins dipped sharply 480 bps y-o-y to 8.5% and were below our estimates of ~14%. Negative operating leverage due to a steep drop in the topline impacted the margins. Also, the company was unable to fully pass on price increases in the automotive segment (due to BS6 emission norm change) which accelerated a drop in the margins. Tracking the weak operating performance, Adjusted PAT dropped 70% y-o-y to Rs 15.1 cr and was below our estimates of Rs 43.5 cr. During the quarter, Greaves had exceptional charge of Rs 5 cr due to employee separation costs. Reported Net Profit stood at Rs 10 cr.

Volumes to decline in near term; margin pressures to sustain: The volumes of the 3W segment of Greaves (that comprises about half of its revenues) are expected to remain under pressure on the back of slowdown due to COVID-19. Further, huge cost increases on account of transition from BS4 to BS6 emission norms would keep the volumes under pressure. Also, owing to slowdown in the economy on account of COVID-19, other segments such as aftermarket and gensets are also likely to remain under pressure. Overall, we expect revenues to decline 8% y-o-y in FY2021. Further, Greaves stated that it would not be able to fully pass on cost increases on account of BS6 emission norms given the steep cost increases and a weak demand scenario. Moreover, operating deleverage due to fall in the revenues is likely to sustain pressure on margins. We expect GCL margins to contract by 100 bps in FY2021.

Conference call highlights:

- ◆ **Transition to BS6 norms:** The company stated that it has successfully transitioned from BS4 emission to BS6 emission norms. Automotive OEM customers have approved Greaves engine and are gradually inducting it onto their products and launching in the marketplace.
- ◆ **Pricing for BS6:** It did not reveal the quantum of price increases due to BS6 norms and stated that the pricing agreements with OEM's are getting finalised.
- ◆ **Ampere vehicles:** It also stated that Ampere electric scooters are gaining traction and the company has reached a 21% market share in e-scooter space. Ampere sold 18,536 units in FY20 registering growth of 30%. Ampere plans to launch "Magnus" high speed scooter in June 2020 which would further boost growth.
- ◆ **Captive financing arm:** The company has set up a captive financing arm. The financing arm is mainly aimed at boosting the Ampere electric scooter business.
- ◆ **Gensets:** The company will launch a new range of gensets (Genius series) in coming few months.
- ◆ **Profitability:** Greaves stated that profitability is likely to remain under pressure in the near term as it would not be able to fully pass on the price increases in the automotive segment related due to BS6 emission.
- ◆ **Aftermarket segment:** Greaves stated about 75-80% of the aftermarket dealers have comeback and the aftermarket business would ramp up faster than other segments.
- ◆ **Crest engines for CNG/Petrol:** Greaves stated that it is in talks with various OEM's for its "Crest" series of engines to be used in 3W petrol and CNG applications. As per Greaves, the engine delivers about 30% more fuel efficiency substantially improving the Total Cost of ownership. Greaves is set to receive any approval from OEM's for Crest engines.

Results

Particulars	Q4FY20	Q4FY19	YoY %	Q3FY20	Rs cr
					QoQ %
Revenues	359.6	528.1	-31.9	494.7	-27.3
EBITDA	30.6	70.0	-56.3	77.2	-60.4
EBITDA margins (%)	8.5	13.3	(480 bps)	15.6	(710 bps)
Depreciation	14.4	11.7	23.4	11.2	29.2
Interest	1.1	0.5	101.9	1.2	-14.6
Other income	3.3	8.6	-61.0	2.8	17.6
PBT	18.4	66.3	-72.2	67.6	-72.7
Tax	3.4	16.1	-79.0	18.3	-81.6
Adjusted PAT	15.1	50.3	-70.0	49.3	-69.5
Reported PAT	10.0	37.4	-73.2	54.1	-81.4
Adjusted EPS	0.31	2.06	-85.0	1.01	-69.5

Source: Company; Sharekhan Research

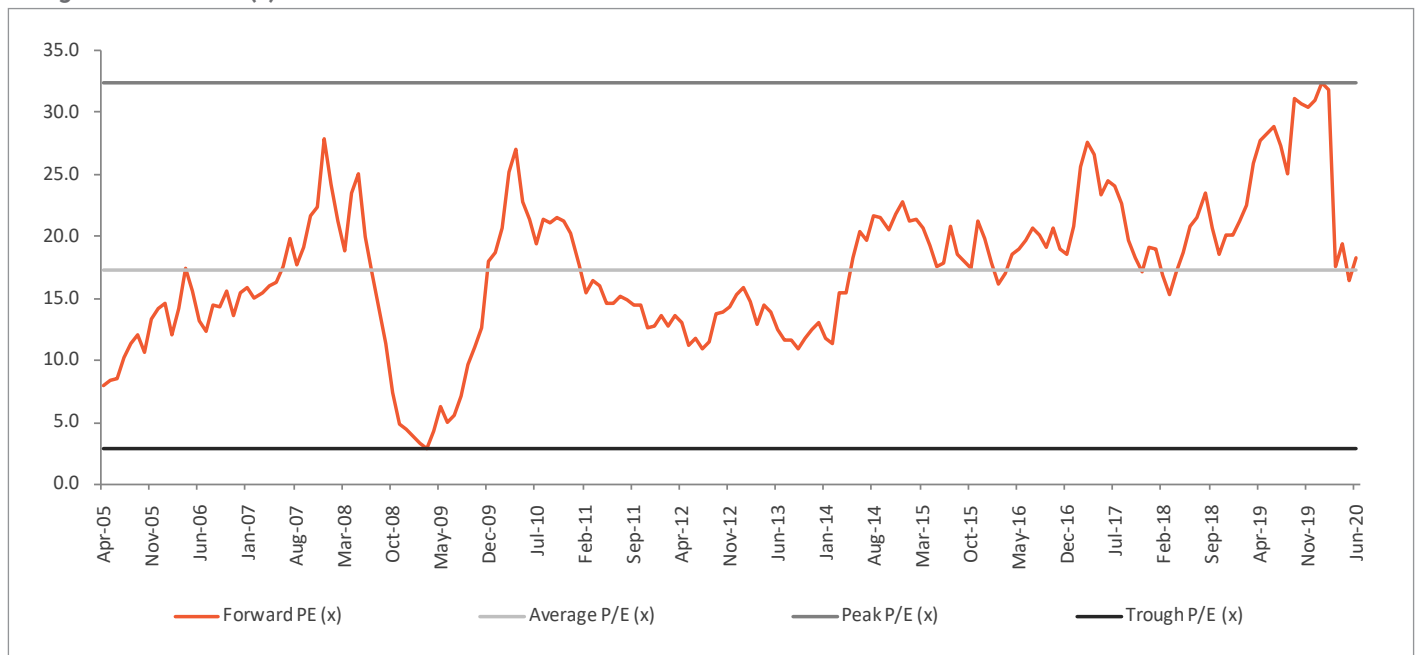
Outlook

Earnings pressure to sustain in near term: Volumes are expected to remain under pressure in the near term due to COVID-19 and steep cost increases due to the transition from BS4 to BS6 emission norms. Negative operating leverage due to a decline in volumes and the inability to fully pass on cost increases for the automotive segment would keep earnings under pressure in near term.

Valuation

Cut estimates; retain Hold rating: Q4FY20 results were below estimates across parameters. In order to factor volume and margin pressures in near term, we have cut our FY21 estimates by about 30%. We have reduced our FY22 estimates by 7%. The stock is trading at 14.4x FY22 earnings which is close to its long-term historical average of 16-17x. Hence, we retain Hold rating on the stock with an unchanged PT of Rs 90.

One year forward P/E (x) band



Source: Sharekhan Research

About company

Greaves Cotton Limited (Greaves) is one of the leading suppliers of power-train and related solutions to the auto OEM's. The company has a lion's share in the 3 wheeler diesel segment. Its products can be classified in to three categories – Engines (56% of sales), Aftermarkets (21% of sales) and others (23% of sales). The others segment includes power Gensets, Agri-equipment and electric scooter business.

Investment theme

GCL is the market leader in 3wheeler diesel engine business having a share of about 70% with all the major OEM's engaged for a long-term supply agreement. It is scaling up the multi- brand aftermarket business its strong distribution reach. Also, GCL has recently forayed into the fast growing electric 2W space and plans to scale up the business substantially. However, earnings are expected to remain under pressure in the near term as the automotive segment would be impacted by steep cost increase on account of BS6 emission norms. Also, COVID-19 is likely to impact other businesses in near term. Moreover, margins are expected to be under pressure due to negative operating leverage and pricing pressures in the automotive segment.

Key Risks

- ◆ Prolonged impact of coronavirus in India could impact topline.
- ◆ Also continued pricing pressures particularly from automotive OEM's can dent margins

Additional Data

Key management personnel

Karan Thapar	Chairman
Nagesh Basavanhalli	Managing Director & CEO
Amit Mittal	Chief Financial Officer
AtindraBasu	Company Secretary

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Dbh International Pvt Ltd	42.71
2	Capital Group Cos Inc/The	8.84
3	Karun Carpets Pvt Ltd	6.15
4	Bharat Starch Products Ltd	5.96
5	Smallcap World Fund Inc/Fund Paren	5.8
6	New India Assurance Co Ltd/The	2.81
7	Life Insurance Corp Of India	2.57
8	General Insurance Corp Of India	2.23
9	L&T Mutual Fund Trustee Ltd/India	1.78
10	Vantage Equity Fund	1.69

Source: Bloomberg

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