Sharekhan
by BNP PARIBAS

Greaves Cotton

Weak quarter; challenging near term outlook

Sector: Automobiles
Result Update

	Change
Reco: **Hold**	↔
CMP: **Rs. 84**	
Price Target: **Rs. 95**	↔

↑ Upgrade ↔ No change ↓ Downgrade

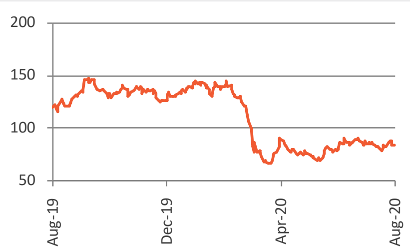
Company details

Market cap:	Rs. 1,940 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	-2.1	12.9	-41.2	-29.5
Relative to Sensex	-3.8	-13.8	-34.2	-31.2

Sharekhan Research, Bloomberg

Greaves Cotton (Greaves) posted higher than expected loss during Q1FY21. Revenue drop of 69% y-o-y was higher than anticipated driven by a lower offtake by OEM due to the lockdown on account of COVID-19. Gross margins dropped 420 bps y-o-y as the company was unable to pass on entire BS6 cost increases due to weak demand. The EBIDTA loss of Rs 22 cr was higher than expectations. The company reported a net loss of Rs 24.2 cr which is higher than our estimates of Rs 2.5 cr. We expect demand to remain weak in near term due to decline in 3W segment on account of COVID-19. People are reluctant to use 3W so as to ensure social distancing in COVID-19 times. While non-automotive segment volumes are picking up, it is not sufficient to offset decline in the automotive space. Negative operating leverage and inability to fully pass on BS6 cost increases due to weak demand would lead to a decline in margins. At CMP, the stock is trading at 15x FY22 earnings which is close to its long-term historical average of 16-17x. Hence, we retain our Hold rating on the stock.

Key positives

- Electric scooter subsidiary Ampere vehicles continued to gain market share in the organised space. Ampere market share improved to 24% as against 21% in FY20.
- Non-automotive segment (gensets, agriculture and after market) have witnessed an improvement in volumes from June 2020 levels.

Key negatives

- Greaves revenue decline of 69% was higher than anticipated. Lower OEM volume offtake on account of COVID-19 impacted the volumes.
- Gross margins dropped 420 bps y-o-y as the company was unable to pass on entire impact of the increase in cost on account of BS6.

Our Call

Earnings pressure to sustain in near term; retain Hold: Volumes are expected to remain under pressure in the near term due to weakness in the 3W automotive segment on account of COVID-19. Negative operating leverage due to a decline in volumes and the inability to fully pass on BS6 cost increases for the automotive segment would keep earnings under pressure in the near term.We have fine-tuned our earnings estimates for both FY21 and FY22 to factor in Greaves acquisition of Noida based electric 3W company Bestway Agencies. At CMP, the stock is trading at 15x FY22 earnings which is close to its long-term historical average of 16-17x. Hence, we retain our Hold rating on the stock with revised PT of Rs 95.

Key Risks

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

Valuation Rs cr

Particulars	FY18	FY19	FY20	FY21E	FY22E
Net sales (Rs cr)	1,792.1	2,015.3	1,911.0	1,783.9	2,069.7
Growth (%)	9.7	12.5	-5.2	-6.7	16.0
EBITDA (Rs cr)	255.3	272.2	210.1	180.8	233.7
OPM (%)	14.2	13.5	11.0	10.1	11.3
Adjusted PAT (Rs cr)	154.5	180.5	122.6	95.6	129.4
Growth (%)	-13.3	16.9	-32.1	-22.0	35.4
FD EPS (Rs)	6.3	7.5	5.4	4.1	5.6
P/E (x)	13.3	11.2	15.6	20.3	15.0
P/B (x)	2.1	2.1	2.8	3.0	3.2
EV/EBITDA (x)	5.9	5.8	8.0	9.5	7.7
RoE (%)	16.1	18.8	17.7	14.7	21.1
RoCE (%)	25.1	24.2	20.9	17.5	24.7

Source: Company; Sharekhan estimates

Posts higher than expected loss: Greaves Cotton Ltd (Greaves) reported a weaker than anticipated performance for the quarter. Revenues declined 69% y-o-y to Rs 147 cr(which was lower than our estimates of Rs 215 cr) impacted by lockdown on account of COVID-19. The company reported a loss of Rs 21.7 cr at the EBIDTA level as against our expectations of profit of Rs 8.5cr. Gross margins for the quarter declined 420 bps y-o-y to 27.8% as the company was unable to pass on cost increases on account of BS6 norms due to weak demand. Moreover, negative operating leverage due to a steep fall in topline impacted the operating performance.Greaves Cotton reported a loss of Rs 24 cr as against an estimated loss of Rs 2.5 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 account of COVID-19. In order to ensure social distancing, people are avoiding usage of 3W (particularly passenger segment) which would keep the sales subdued. Although other segments such as agriculture and aftermarket are recovering, it would not be sufficient to offset decline in the automotive segment. Overall, we expect Greaves revenues to decline 7% y-o-y in FY21. 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 jump and a weak demand scenario. Also, operating deleverage due to fall in the revenues is likely to sustain pressure on margins. We expect GCL margins to contract by 90 bps in FY2021.

Conference call highlights:

- **Demand outlook:** Greaves stated it is witnessing a recovery in farm, genset and aftermarket segment from July 2020 as compared to June as the economy is opening. However, the 3W passenger segment is yet to witness revival. To ensure social distancing, people are avoiding 3W resulting into weak demand for 3W passenger space. Greaves expects 3W passenger sales to remain under pressure.
- **BS6 pricing not fully passed:** Greaves stated it was not fully able to pass on BS6 pricing increases due to lower volume offtake due to COVID-19. Because of lower 3W demand particularly in the passenger segment, Greaves would be unable to pass on entire price increases in the near term.
- **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 yet to receive any approval from OEM's for Crest engines.
- **Ampere vehicles:** Greaves stated that Ampere is continuing to gain market share. Ampere reached market share of 24% in organized electric scooter in Q1FY21 as against 21% in FY20.
- **VRS in Ranipet plant:** Greaves has launched voluntary retirement scheme for employees at its Ranipet plant in order to control costs. Greaves plans to close down the manufacturing unit at Ranipet.
- **Debt:** In order to maintain sufficient liquidity during COVID-19, Greaves raised debt to the tune of about Rs 70 cr. Greaves has stated that it would repay the entire debt raised during Q1FY21 quarterby end of FY21.
- **Acquisiton:** Post Q1FY21, Greaves acquired 74% stake in Noida based electric 3W company Bestway Agencies for Rs 7 cr. Bestway agencies had revenues of Rs 35cr in FY20. Greaves plans to further enhance its electric vehicle offerings with acquisition of Bestway.
- **Subscription scheme for electric vehicles:** Greaves has launched an attractive subscription schemes for electric 2W which would enable it to boost sales.
- **Management change:** Greaves announced that Mr Nagesh Basavanhalli, Managing Director and Chief Executive Officer has resigned from executive responsibilities due to personal reasons. However, he would continue to work for the company and would be designated as Vice Chairman of the Board effective 14th August 2020 and hold office till the next AGM to be held for FY21.The Board has appointed Mr. Ajit Venkataraman as an Additional Director - Executive for the period of three years with effect from 14th August, 2020. Mr Ajit currently heads the automotive business and will take on the executive responsibilities from Mr Nagesh.

Results Rs cr

Particulars	Q1FY21	Q1FY20	YoY%	Q4FY20	QoQ%
Revenues	147.1	476.8	-69.2	359.6	-59.1
EBITDA	(21.7)	61.3	NA	30.6	NA
EBITDA margins (%)	(14.7)	12.8	NA	8.5	NA
Depreciation	11.8	12.3	-4.1	14.4	-18.4
Interest	2.3	0.6	264.5	1.1	115.2
Other income	2.2	7.4	-71.0	3.3	-35.6
PBT	(33.5)	55.8	NA	18.4	NA
Tax	(9.3)	17.6	NA	3.4	NA
Adjusted PAT	(24.2)	38.2	NA	15.1	NA
Reported PAT	(24.2)	38.2	NA	10.0	NA
Adjusted EPS	(0.50)	1.56	NA	0.31	NA

Source: Company; Sharekhan Research

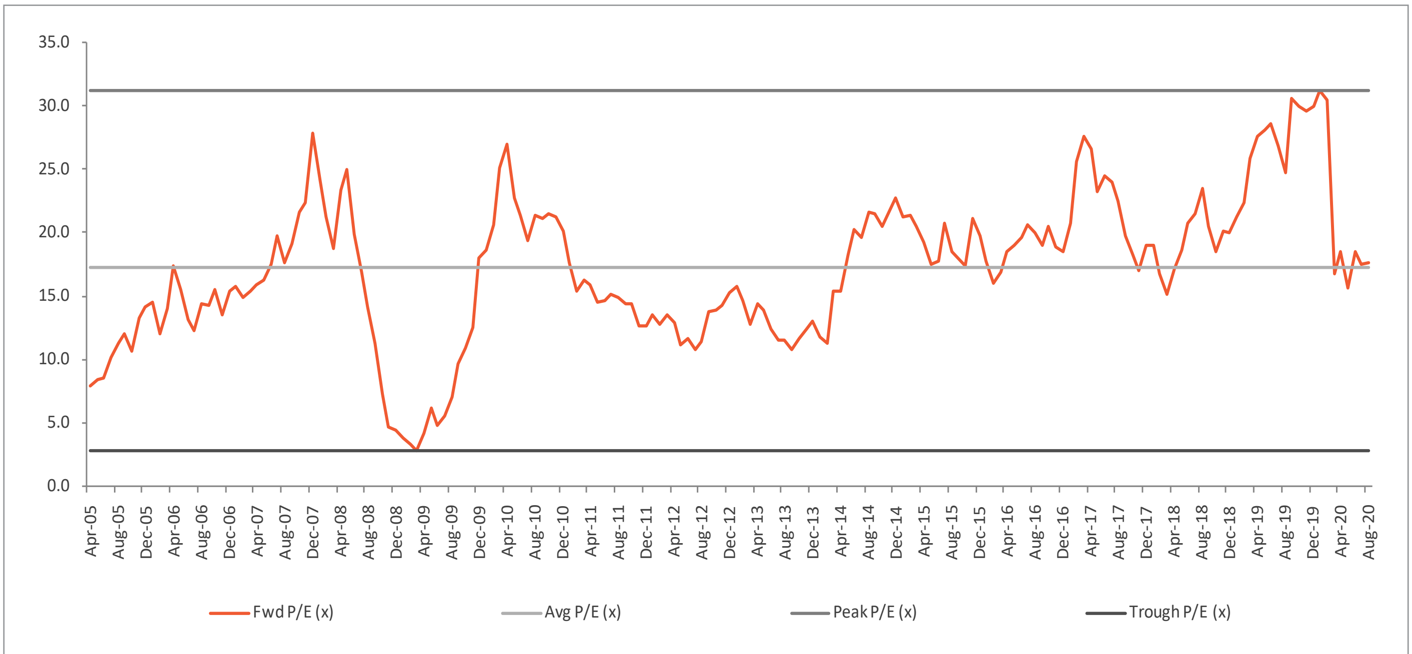
Outlook

Earnings pressure to sustain in near term: Volumes are expected to remain under pressure in the near term due to weakness in the 3W automotive segment on account of COVID-19. People are reluctant to use 3W so as to ensure social distancing in COVID-19 times. Negative operating leverage due to a decline in volumes and the inability to fully pass on BS6 cost increases for the automotive segment would keep earnings under pressure in near term.

Valuation

Fine-tuned estimates; Retain Hold: Greaves earnings are expected to decline in FY21 driven by a decline in the automotive segment and a drop in margins due to its inability to pass on cost increases due to BS6 norms. We have fine-tuned our earnings estimates for both FY21 and FY22 to factor in Greaves acquisition of Noida based electric 3W company Bestway Agencies. At CMP, the stock is trading at 15x FY22 earnings which is close to its long-term historical average of 16-17x. Hence, we retain Hold rating on the stock with revised PT of Rs 95.

One 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 3 wheeler 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. We expect demand to remain weak in near term due to decline in 3W segment on account of COVID-19. People are reluctant to use 3W so as to ensure social distancing in COVID-19 times. While non-automotive segment volumes are picking up, it is not sufficient to offset decline in the automotive space. Negative operating leverage and inability to fully pass on BS6 cost increases due to weak demand would lead to a decline in margins. At CMP, the stock is trading at 15x FY22 earnings which is close to its long-term historical average of 16-17x. Hence, we retain our Hold rating on the stock

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	Vice Chairman
Ajit Venkataraman	Additonal Director (Executive)
Amit Mittal	Chief Financial Officer

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 Tustee Ltd/India	1.78
10	VANTAGE EQUITY FUND	1.69

Source: Bloomberg

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