Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Stock Update

Result Update

# Eicher Motors Ltd

## Well poised to deliver profitable growth

| Automobiles | Sharekhan code: EICHERMOT |
|---|---|

| Reco/View: Buy | ↔ | CMP: Rs. 3,702 | Price Target: Rs. 4,260 | ↑ |
|---|---|---|---|---|

↑ Upgrade ↔ Maintain ↓ Downgrade


**Summary**

- We maintain our Buy rating on Eicher Motors Limited (EML) with a revised PT of Rs. 4,260, led by success of new launches, robust export opportunities, and focus on profitable growth path.
- Q2FY2023 performance was slightly above expectations, with PAT beating estimates by 3.2%. Revenue, EBITDA, and PAT grew by 56.4% y-o-y, 74.9% y-o-y, and 76% y-o-y, respectively, in Q2FY2023.
- Management's focus on refreshed and new launches in India and international markets, expanding export opportunities, and increasing addressable markets should boost 2W performance. Moreover, its CV business is expected to benefit from multi-year CV upcycle, widening product portfolio, and strong hold in niche segments.
- EML's consolidated earnings would report a robust 48.3% CAGR over FY2022-FY2024E, driven by a 28.7% domestic revenue CAGR, 32% export revenue CAGR, and a 410-bps increase in EBITDA margin from 21.1% in FY2022 to 25.2% in FY2024E. The stock trades at 27.4x P/E and 24x EV/EBITDA on its FY2024E estimates.


**Eicher Motors Limited's (EML) Q2FY2023 performance was slightly above expectations, with PAT beating estimates by 3.2%. Revenue, EBITDA, and PAT grew by 56.4% y-o-y, 74.9% y-o-y, and 76% y-o-y, respectively, in Q2FY2023. Consolidated EBITDA margin saw a decline of 110bps q-o-q to 23.3% in Q2, led by inferior product mix, partially supported by positive operating leverage and softening commodity prices. Management continues to focus on 250cc+ market segment and aims to lead and grow the global mid-sized motorcycle segment (250-750cc). The company has a strong pipeline of new products for the next five years, through upgrading products on existing platforms. We believe the company is well poised to recover strongly and put performance in top gear, driven by an increase in addressable market size and better operational performance in the company's two-wheeler (2W) division. Further, the company's commercial vehicle (CV) business is geared up to significantly improve its contribution to consolidated PBT, led by expected market share gains, increasing synergies with the JV partner (Volvo), and operating leverage benefits. As the economy and supply constraints are normalising, we expect premiumisation to surge again in the 2W segment and expect Royal Enfield to outperform in the premium bike segment. Given a strong business outlook and robust earnings CAGR of 48.3% during FY2022-FY2024E, we reiterate our Buy rating on the stock with a revised price target (PT) of Rs. 4,260.**

**Key positives**

- Q2FY23 performance was slightly above expectations, with PAT beating estimates by 3.2%. Revenue, EBITDA, and PAT grew by 56.4% y-o-y, 74.9% y-o-y, and 76% y-o-y, respectively, in Q2.
- Consolidated revenue increased by 56.4% y-o-y to Rs. 3,519 crore, led by 68.3% growth in Royal Enfield volume, partially offset by a 7.5% decline in average sales realisation.
- VE Commercial Vehicles' (VECV) share of profit increased by 349% y-o-y and 31% q-o-q to Rs. 44.1 crore in Q2 on account of recovery in CV sales and operating leverage benefits. During Q2FY2023, VECV's market share for Heavy Duty Trucks and Buses improved.

**Key negatives**

- Consolidated EBITDA margin saw a decline of 110bps q-o-q to 23.3% in Q2, led by inferior product mix, partially supported by positive operating leverage and softening commodity prices.

**Management Commentary**

- During Q2FY2023, the company's management is optimistic about demand recovery on account of pent-up demand, new launches, and easing chips supply constraints.
- The company has registered healthy growth during the festive season and expects the trend to continue in the quarter as well. The company is witnessing a strong uptick in volumes, led by Hunter 350. The company has also launched the Super Meteor 650 recently, which will make its 650cc portfolio stronger.
- Management continues to focus on 250cc+ market segment and aims to lead and grow the global mid-size motorcycle segment (250cc-750cc). The company has a strong pipeline of new products for the next five years, through upgrading products on existing platforms.

**Our Call**

**Valuation – Maintain Buy with a revised PT of Rs. 4,260:** EML is well poised to show strong recovery in its overall performance, driven by the increase in addressable market size and improvement in operational performance in the 2W division, while the CV division is expected to benefit from a multi-year CV upcycle. Given a strong business outlook and a robust earnings CAGR of 48.3% during FY2022-FY2024E, the valuation is yet to catch up with the expected recovery in performance, as the stock trades at a 15-20% discount to its historical average multiples, at 27.4x P/E and 24x EV/EBITDA on FY2024E estimates. We reiterate our Buy rating on the stock with a 12-month PT of Rs. 4,260 by valuing the business at 28x its rolling-forward December 2024E EPS.

**Key Risks**

Failure of new launches due to competition may result in Royal Enfield's market share loss and adversely impact our future projections. Moreover, if chips shortage aggravates against our expectations of easing out gradually, volume and performance estimates may be impacted.

**Valuation (Consolidated)** Rs cr

| Particulars | FY21 | FY22 | FY23E | FY24E | FY25E |
|---|---|---|---|---|---|
| Net Sales | 8,720 | 10,298 | 14,068 | 16,582 | 18,751 |
| Growth (%) | (3.9) | 18.1 | 36.6 | 17.9 | 13.1 |
| EBIDTA | 1,781 | 2,172 | 3,457 | 4,177 | 4,780 |
| OPM (%) | 20.4 | 21.1 | 24.6 | 25.2 | 25.5 |
| Adjusted PAT | 1,347 | 1,677 | 2,850 | 3,689 | 4,312 |
| Growth (%) | (30.4) | 24.5 | 70.0 | 29.5 | 16.9 |
| EPS (Rs ) | 49.3 | 61.4 | 104.4 | 135.1 | 158.0 |
| PE (x) | 75.0 | 60.3 | 35.5 | 27.4 | 23.4 |
| P/BV (x) | 8.8 | 8.0 | 6.7 | 5.5 | 4.5 |
| EV/EBIDTA (x) | 56.2 | 46.1 | 29.0 | 24.0 | 21.0 |
| RoNW (%) | 13.7 | 13.9 | 20.6 | 22.0 | 21.2 |
| RoCE (%) | 13.8 | 14.1 | 20.7 | 22.1 | 21.2 |

*Source: Company; Sharekhan estimates*

**3R MATRIX**

| | + | = | - |
|---|---|---|---|
| Right Sector (RS) | ✓ | | |
| Right Quality (RQ) | ✓ | | |
| Right Valuation (RV) | ✓ | | |

\+ Positive = Neutral – Negative

**What has changed in 3R MATRIX**

| | Old | | New |
|---|---|---|---|
| RS | | ↔ | |
| RQ | | ↔ | |
| RV | | ↔ | |

**ESG Disclosure Score** NEW

ESG RISK RATING 13.45

Updated Oct 08, 2022

Low Risk

| NEGL | LOW | MED | HIGH | SEVERE |
|---|---|---|---|---|
| 0-10 | 10-20 | 20-30 | 30-40 | 40+ |

*Source: Morningstar*

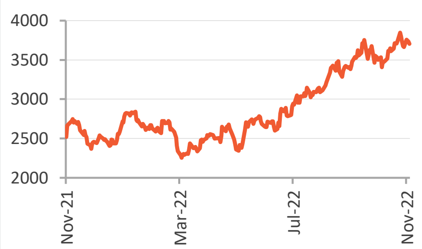
**Company details**

| | |
|---|---|
| Market cap: | Rs. 1,01,223 cr |
| 52-week high/low: | Rs. 3,886 / 2,110 |
| NSE volume: (No of shares) | 8.19 lakh |
| BSE code: | 505200 |
| NSE code: | EICHERMOT |
| Free float: (No of shares) | 13.9 cr |

**Shareholding (%)**

| | |
|---|---|
| Promoters | 49.2 |
| FII | 30.3 |
| DII | 10.1 |
| Others | 10.5 |

**Price chart**




**Price performance**

| (%) | 1m | 3m | 6m | 12m |
|---|---|---|---|---|
| Absolute | 5.8 | 17.7 | 48.9 | 46.8 |
| Relative to Sensex | 1.6 | 13.8 | 40.0 | 45.4 |

*Sharekhan Research, Bloomberg*

## Key takeaways from the conference call

- **Strong performance in Q2FY2023:** EML's Q2FY2023 performance was slightly above our expectations, with PAT beating estimates by 3.2%. Revenue, EBITDA, and PAT grew by 56.4% y-o-y, 74.9% y-o-y, and 76% y-o-y, respectively, in Q2. Consolidated revenue grew by 56.4% y-o-y to Rs. 3,519 crore, led by 68.3% growth in Royal Enfield's volumes, partially offset by a 7.5% decline in average sales realisation. Average sales realisation was lower due to increased share of Hunter 350, which is a lower-priced bike in Royal Enfield's product portfolio. Consolidated EBITDA margin saw a decline of 110bps q-o-q to 23.3% in Q2, led by inferior product mix, partially supported by positive operating leverage and softening commodity prices. While on a y-o-y basis, EBITDA margin improved by 250bps, aided by operating leverage benefits, cost reductions, and lower raw-material prices. The company's EBITDA and PAT increased by 74.9% y-o-y and 76% y-o-y to Rs. 822 crore and Rs. 657 crore, respectively. VECV's share of profit increased by 349% y-o-y and 31% q-o-q to Rs. 44.1 crore in Q2 on account of recovery in CV sales and operating leverage benefits. During Q2FY2023, VECV's market share for Heavy Duty Trucks and Buses improved.
- **Positive management outlook:** Management is optimistic about demand recovery because of pent-up demand, new launches, and easing chips supply constraints. The company has registered healthy growth during the festive season and expects the trend to continue in the next quarter as well. The company will continue to focus on the profitable growth path and expand its addressable market through new and refreshed launches.
- **Market share:** The company has increased its market share across its 2W and CV portfolio. Royal Enfield's market share has increased to 30.2% in H1FY2023 from 26% in H1FY2022. In the CV segment, the company has established a strong brand value in niche markets. During Q2FY2023, the company's market share increased in heavy duty trucks and buses.
- **Management's focus stays on Royal Enfield; Focus also remains on converting sales:** Management asserts that the brand value of Royal Enfield is intact despite the 35% decline in volumes in FY2022 from its peak levels in FY2019. The company highlighted that the aspirational value remains strong for the brand, with 48% top-of-mind awareness and 98% net sentiment. Management highlighted that there were more than 30 million searches for Royal Enfield in FY2022. Despite heavy traffic, conversions were below expectations. The company is working on improving its conversions from online channels.
- **New launches in the pipeline:** Management continues to focus on 250cc+ market segment and aims to lead and grow the global mid-size motorcycle segment (250-750cc). The company has a strong pipeline of new products for the next five years, through upgrading products on existing platforms. The company is witnessing a strong uptick in volumes, led by Hunter 350. The company has also launched the Super Meteor 650 recently, which will make its 650cc portfolio stronger. Royal Enfield is now preparing to launch a slew of new products, including variants in the coming years. It has recently launched Hunter 350. Management shared its plan to add two new variants on its J-series platform. The company also plans to add five new derivative models and two variants on the Twins platform. The company is also planning to add a new platform to its total offerings. Further, the company has no plans for the LS410 platform currently. The company expects to launch a new model in 1-2 years and aims to launch refreshed versions every quarter. The use of one platform helps it to rationalise cost and shorten the payback period.

**Results (Consolidated)** Rs cr

| Particulars | Q2FY23 | Q2FY22 | Y-o-Y % | Q1FY23 | Q-o-Q % |
|---|---|---|---|---|---|
| Revenue | 3,519 | 2,250 | 56.4 | 3,397 | 3.6 |
| Total Expenses | 2,698 | 1,780 | 51.6 | 2,566 | 5.1 |
| EBITDA | 821.6 | 469.9 | 74.9 | 831.1 | (1.1) |
| Other income | 149 | 109 | 36.8 | 49 | 205.4 |
| Depreciation | 127 | 109 | 16.2 | 116 | 9.4 |
| Interest | 7 | 3 | 124.8 | 5 | 35.2 |
| PBT | 836 | 466 | 79.4 | 758 | 10.3 |
| Tax | 223 | 103 | 117.7 | 181 | 23.1 |
| Reported PAT | 657 | 373 | 76.0 | 611 | 7.6 |
| Adjusted PAT | 656.9 | 373.2 | 76.0 | 610.7 | 7.6 |
| EPS (Rs) | 24.0 | 13.7 | 75.9 | 22.3 | 7.5 |

*Source: Company; Sharekhan Research*

**Key ratios (Consolidated)**

| Particulars | Q2FY23 | Q2FY22 | Y-o-Y (bps) | Q1FY23 | Q-o-Q (bps) |
|---|---|---|---|---|---|
| Gross margin (%) | 42.4 | 42.4 | 10 | 44.0 | (150) |
| EBIDTA margin (%) | 23.3 | 20.9 | 250 | 24.5 | (110) |
| EBIT margin (%) | 19.7 | 16.0 | 370 | 21.0 | (130) |
| Net profit margin (%) | 18.7 | 16.6 | 210 | 18.0 | 70 |
| Effective tax rate (%) | 2.7 | 2.2 | 50 | 2.4 | 30 |

*Source: Company; Sharekhan Research*

**Results (Standalone)** Rs cr

| Particulars | Q2FY23 | Q2FY22 | Y-o-Y % | Q1FY23 | Q-o-Q % |
|---|---|---|---|---|---|
| Revenue | 3,397 | 2,182 | 55.7 | 3,248 | 4.6 |
| Total Expenses | 2,594 | 1,739 | 49.1 | 2,460 | 5.4 |
| EBITDA | 803.6 | 442.7 | 81.5 | 788.2 | 2.0 |
| Other income | 153 | 112 | 36.6 | 93 | 65.3 |
| Depreciation | 125 | 108 | 15.6 | 114 | 9.5 |
| Interest | 3 | 2 | 119.9 | 3 | 36.7 |
| PBT | 829 | 445 | 86.1 | 764 | 8.4 |
| Adjusted PAT | 614.9 | 343.4 | 79.1 | 580.2 | 6.0 |
| EPS (Rs) | 22.5 | 12.6 | 79.0 | 21.2 | 5.9 |

*Source: Company; Sharekhan Research*

**Key ratios (Consolidated)**

| Particulars | Q2FY23 | Q2FY22 | Y-o-Y (bps) | Q1FY23 | Q-o-Q (bps) |
|---|---|---|---|---|---|
| Gross margin (%) | 41.5 | 41.0 | 50 | 42.7 | (120) |
| EBIDTA margin (%) | 23.7 | 20.3 | 340 | 24.3 | (60) |
| EBIT margin (%) | 20.0 | 15.3 | 460 | 20.8 | (80) |
| Net profit margin (%) | 18.1 | 15.7 | 240 | 17.9 | 20 |
| Effective tax rate (%) | 25.8 | 22.9 | 290 | 24.1 | 170 |

*Source: Company; Sharekhan Research*

**Volume Analysis (Standalone)** (Rs. per Vehicle)

| Particulars | Q2FY23 | Q2FY22 | Y-o-Y % | Q1FY23 | Q-o-Q % |
|---|---|---|---|---|---|
| Volume | 2,07,764 | 1,23,427 | 68.3 | 1,87,205 | 11.0 |
| Realization | 1,63,512 | 1,76,777 | (7.5) | 1,73,496 | (5.8) |
| RMC/Vehicle | 95,651 | 1,04,352 | (8.3) | 99,432 | (3.8) |
| Contribution/Vehicle | 67,861 | 72,425 | (6.3) | 74,065 | (8.4) |
| EBITDA/Vehicle | 38,680 | 35,865 | 7.9 | 42,104 | (8.1) |
| PAT/Vehicle | 29,594 | 27,819 | 6.4 | 30,991 | (4.5) |

*Source: Company; Sharekhan Research*

## Outlook and Valuation

### ■ Sector View – 2W demand set to recover in double digits after three years of slowdown

The 2W industry is well poised to register double-digit growth rates over the next few years and surpass FY2019 peak volumes by FY2025-FY2026. The 2W industry is core to India's business mobility and is the most affordable mode of personal commute. We expect normalcy in the economy to support growth in the 2W industry, driven by pent-up demand and improving income levels of potential customers. We expect growth to be driven by rural as well as urban markets. Rural and semi-urban markets are already showing signs of recovery, led by increased number of enquiries and footfalls at showrooms. We expect the return in urban demand to drive faster growth in scooters and premium bikes. Strong players in the premium motorcycle segments (>125cc bike segment) are expected to be key beneficiaries.

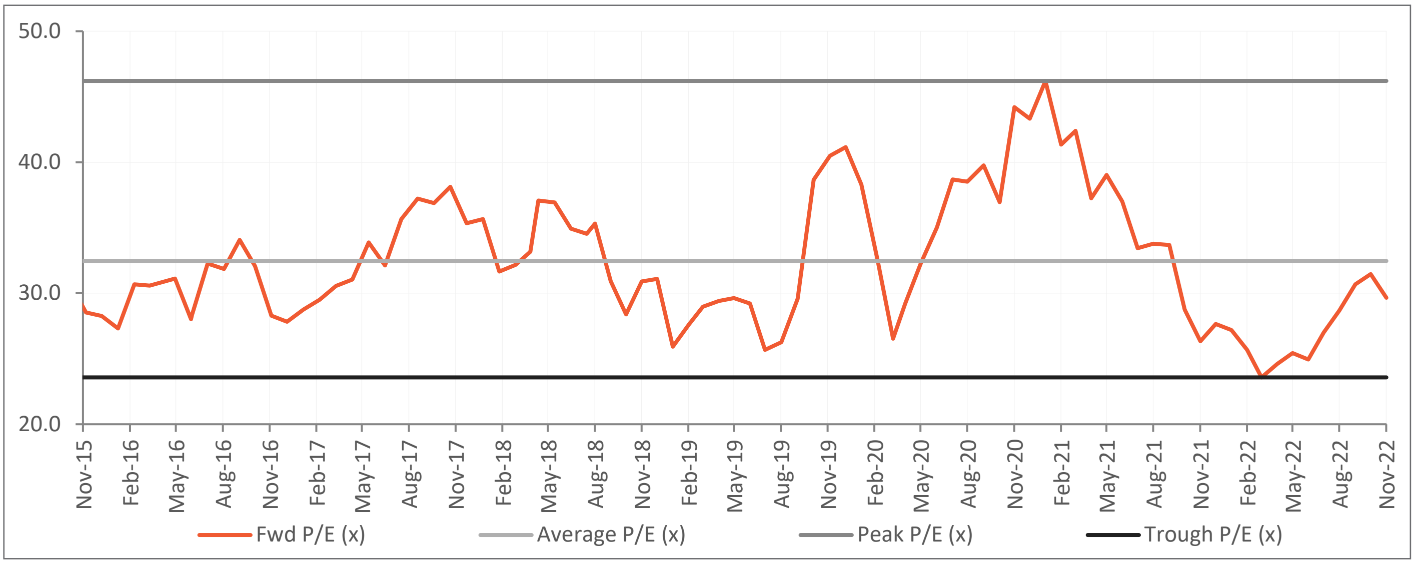
### ■ Company Outlook – Beneficiary of strong demand in the 2W and multi-year CV cycle

EML is well poised to recover strongly and put performance in top gear, driven by an increase in addressable market size and improvement in operational performance in the company's 2W division. Further, the company's CV business is geared up to significantly improve its contribution to consolidated PBT, led by expected market share gains, rising synergies with the JV partner (Volvo Group), and operating leverage benefits.

### ■ Valuation – Maintain Buy with a revised PT of Rs4,260:

Valuation - Maintain Buy with a revised PT of Rs. 4,260: EML is well poised to show strong recovery in its overall performance, driven by the increase in addressable market size and improvement in operational performance in the 2W division, while the CV division is expected to benefit from a multi-year CV upcycle. Given a strong business outlook and a robust earnings CAGR of 48.3% during FY2022-FY2024E, the valuation is yet to catch up with the expected recovery in performance, as the stock trades at a 15-20% discount to its historical average multiples, at 27.4x P/E and 24x EV/EBITDA on FY2024E estimates. We reiterate our Buy rating on the stock with a 12-month PT of Rs. 4,260 by valuing the business at 28x its rolling-forward December 2024E EPS.

**One-year forward P/E (x) band**




*Source: Company, Sharekhan Research*

**Peer Comparison**

| Particulars | CMP | P/E (x) | | | EV/EBITDA (x) | | | RoCE (%) | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Rs/Share | FY22 | FY23E | FY24E | FY22 | FY23E | FY24E | FY22 | FY23E | FY24E |
| Eicher Motors | 3,702 | 60.3 | 35.5 | 27.4 | 46.1 | 29.0 | 24.0 | 14.1 | 20.7 | 22.1 |
| Hero MotoCorp | 2,714 | 21.9 | 17.9 | 14.4 | 13.6 | 10.1 | 7.7 | 20.1 | 21.1 | 22.0 |
| Bajaj Auto | 3,723 | 22.9 | 19.6 | 16.6 | 16.0 | 13.1 | 10.6 | 21.2 | 21.7 | 23.7 |
| TVS Motor | 1,108 | 57.0 | 32.5 | 25.9 | 27.3 | 18.6 | 14.9 | 21.3 | 29.5 | 30.6 |

*Source: Company, Sharekhan estimates*

## About company

EML is the owner of the Royal Enfield brand and is a leading manufacturer in the premium motorcycle segment. In 2008, the company formed a JV with Volvo Group, VE Commercial Vehicles (VECV). Eicher holds a 54% stake and has transferred its CV businesses to the JV.

## Investment theme

EML is a brand-conscious company and invests significant time and money in building up the motorcycling community and promoting its brands through direct engagement with customers. The company is focusing on increasing its addressable market size and improve the operational performance of the company's 2W division through new launches and is working on a profitable growth model. Further, the company's CV business is geared up to significantly improve its contribution to consolidated PBT, led by expected market share gains, increasing synergies with the JV partner (Volvo Group), and operating leverage benefits. The company is also focused on improving its export business through brand recognition and widening addressable market. We remain positive on EML's growth prospects and recommend a Buy rating on the stock.

## Key Risks

- Failure of new launches due to competition may result in Royal Enfield's market share loss and affect our estimates.
- If semiconductor chip shortage aggravates against expectations of easing out gradually, volume and performance estimates may be impacted.

## Additional Data

**Key management personnel**

| | |
|---|---|
| Siddhartha Lal | Managing Director & CEO - Eicher Motors |
| B. Govindrajan | CEO - Royal Enfield & Wholetime Director - Eicher Motors |
| Yadvinder Singh Guleria | Chief Commercial Officer - Royal Enfield |
| Kaleeswaran Arunachalam | Chief Financial Officer - Eicher Motors |

*Source: Company Website*

**Top 10 shareholders**

| Sr. No. | Holder Name | Holding (%) |
|---|---|---|
| 1 | The Simran Siddhartha Tara Benefit Trust | 44.0 |
| 2 | SBI-ETF Nifty 50 | 2.0 |
| 3 | Amansa Holdings Private Limited | 1.8 |
| 4 | The Brinda Lal Trust | 1.8 |
| 5 | UTI Flexi Cap Fund | 1.3 |
| 6 | Government Pension Fund Global | 1.2 |
| 7 | Simran Lal | 1.2 |
| 8 | Tara Lal | 1.2 |
| 9 | Siddhartha Vikram Lal | 1.1 |
| 10 | Stichting Depositary Apg Emerging Markets Equity Pool | 1.1 |

*Source: Bloomberg*

## Understanding the Sharekhan 3R Matrix

| | |
|---|---|
| **Right Sector** | |
| Positive | Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies |
| Neutral | Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies |
| Negative | Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability. |
| **Right Quality** | |
| Positive | Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance. |
| Neutral | Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable |
| Negative | Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet |
| **Right Valuation** | |
| Positive | Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment. |
| Neutral | Trading at par to historical valuations and having limited scope of expansion in valuation multiples. |
| Negative | Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple. |

*Source: Sharekhan Research*

Sharekhan

by BNP PARIBAS

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