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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	■	↔	■

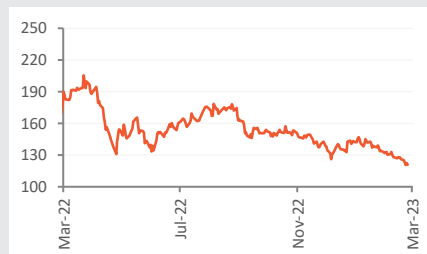
Company details

Market cap:	Rs. 2,798 cr
52-week high/low:	Rs. 211 / 119
NSE volume: (No of shares)	11.2 lakh
BSE code:	501455
NSE code:	GREAVESCOT
Free float: (No of shares)	10.3 cr

Shareholding (%)

Promoters	55.5
FII	4.1
DII	5.2
Others	35.2

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-13.0	-12.3	-30.5	-28.7
Relative to Sensex	-7.9	-4.3	-28.0	-32.5

Sharekhan Research, Bloomberg

Greaves Cotton Ltd
On multi-pronged growth path

Automobiles	Sharekhan code: GREAVESCOT	
Reco/View: Buy	↔	CMP: Rs. 121 Price Target: Rs. 183
↑ Upgrade	↔ Maintain	↓ Downgrade

Summary

- We reiterate a Buy rating on the Greaves Cotton Ltd (Greaves) on expectation of (1) sequential improvement in its performance in Q4, (2) fall in operating losses in EV business and (3) margin accretive acquisition of Excel's business.
- EV business is expected to revive from Q4FY23 onwards on expectation of recovery in production.
- Greaves is building a performance-based EV business, which can sail through even without subsidy support.
- Acquisition of high-margin Excel business would improve overall profitability and revenue mix. The stock trades at a P/E multiple of 15.7x and EV/EBITDA multiple of 6.5x its FY2025E estimates.

We visited Greaves Cotton's (Greaves) electric two-wheeler manufacturing plant at Ranipet (Chennai) and noted the following positives - (1) Plant has achieved manufacturing capacity of five lakh units in two shifts, which can be expanded to 10 lakh units (2) Except battery cell and semiconductors, the plant has been procuring most of the raw material from local markets and (4) The plant is close to supplier ecosystems and has already rolled out 125,000 units since inception. Over the period, the company undertook various steps to improve efficiency in the plants and that has resulted in sharp reduction in production lapses since Greaves acquires Ampere. Broadly, Greaves bifurcates its whole business in three key buckets - (1) Engineering segment: It comprises automotive as well as non-automotive engine businesses and Excel Control linkage would also be part of the engineering business after consolidation. Currently Engineering business contributes ~ 35% to the total revenues, (2) Electric mobility business: Here, Greaves manufactures and sells electric two wheelers and three wheelers, the electric mobility business is contributing ~ 40% of total revenues (3) Retail segment: Retail segment is an asset light franchise-based business model and contributes around 25% to the total revenues. The management has been optimistic on electric vehicle business and assumes that despite rise in competition it would continue to enjoy first mover advantage in electric two-wheeler segment. Similarly, its traditional business segment is expected to be boosted by acquisition of high margin Excel's business. We believe that GCL's diversification strategy is reaping the benefit as it broadened the growth prospects in both B2B and B2C space. The stock is trading at P/E multiple of 15.7x and EV/EBITDA multiple of 6.5x its FY2025E estimates. We maintain our Buy rating on the stock with an unchanged PT of Rs 183.

- Multi-brand strategy to cater to EV space:** We understand that Greaves is adequately equipped to develop wide range of products varying from mass-market products to premium products, however the company is launching products as per the established needs of the market. Currently it is catering to electric three wheeler segment with three well distinguished brands- (1) Zeal EX which has been priced at Rs 75,000 and caters to city speed or mass market segment youth centric product, (2) Magnus EX is priced at Rs 81,900 and is one of the most demanding name plate in domestic electric two wheeler segment and has been considered as family scooter, and (3) Greaves has introduced Primus with a price tag of Rs 110,000 to cater to high speed young family segment. Primus has been receiving healthy response in the market and is expected to be launch in the market soon. Further Greaves is expected to launch NXG and NXU brands in coming period.
- EV biz operating losses are reducing:** The management claims that it has been registering best in class gross margin in electric mobility business and operating performance would improve substantially once volumes would ramp up due to operating leverage benefit. While currently Greaves is catering to a large set of markets via limited brands but would continue to expand its product portfolio as demand improves in the segment. Currently EV penetration in India is around 5% and has large room to expand due to cost effective last-mile transport solution offerings. Besides electric two-wheelers, the company has been steadily building up its electric three-wheeler business in steps. In 9MFY23, the electric mobility segment reported an EBITDA margin at -3% compared to -10% in 9MFY22. The EBITDA loss in 9MFY23 is largely attributed to the muted performance in Q3FY23 due to change in regulatory norms.
- Excel to 'excel' in engineering segment:** While the company has been focussing on the new age business for a sustainable growth, it has been equally looking for a sustainable growth in its engineering segment where it has been catering to automobile engine and industrial engine segment. Further the company has been in process of completing the acquisition of Excel Control linkage. Operating performance of the engineering division would improve substantially as Excel deliver substantially higher margin than Greaves' overall EBITDA margin. Excel delivered EBITDA margins of 29% in FY22 as compared to Greaves' peak margin at 14.9% in FY17. We attribute selective and judicious order bookings, exposure to export markets, technology-added products and better customer mix for Excel's superior EBITDA margin.
- Retail division to cater to end-consumers:** Under retail segment, Greaves offers spare parts sales and services to its end customer. Greaves follows multi-brand franchise model in retail segment and hence it has been asset light business model. The retail segment helps Greaves in catering to the after sales segment and assures for a recurring revenue on an annuity. In general retail segment has potential to offer 20% EBITDA margin.

Our Call

Valuation – Maintain Buy rating with an unchanged PT of Rs. 183: After visiting Greaves' Ranipet plant and management interactions, we believe that Greaves is strategically building up new business (EVs & retail) for growth and continue to strengthen its legacy business via organic as well as organic route. While subdued performance in EV business has impacted its performance in Q3FY23 due to change in regulatory norms we understand that EV business would revive from Q4FY23 onwards. Further, the management is looking for a structural and sustainable growth in the EV business and indicated that it has been equipped to launch products in entry level to premium segment but gradually introducing products according to relevant demand scenario. Despite a muted Q3FY23, operating losses in the EV business came down on a rise in volumes and better product mix. This makes us to believe that operating performance would improve further on ramping up of volumes and operating leverage. Along with the EV business, a consolidation of high-margin Excel business would drive its overall profitability and customer profile in engineering division. We expect the financial performance of the e-mobility business to strengthen going forward, driven by increasing contribution of high-speed e-2Ws, increasing retail penetration, and new launches. We believe that GCL's diversification strategy is reaping the benefit as it has been broadening the growth prospects in both B2B and B2C space. The stock is trading at a P/E multiple of 15.7x and EV/EBITDA multiple of 6.5x its FY2025E estimates. We maintain our Buy rating on the stock with an unchanged PT of Rs 183.

Key Risks

The company's performance can be impacted adversely if commodity prices start to rise again in the near term. With larger players getting aggressive in the EV space, competition is expected to intensify, which may affect the company's profitability in the medium term.

Valuation (Consolidated)

Particulars	FY21	FY22	FY23E	FY24E	FY25E
Revenues	1,500	1,710	2,223	2,700	3,106
Growth (%)	-21.5	13.9	30.0	21.5	15.0
EBIDTA	80	27	144	237	286
OPM (%)	5.3	1.6	6.5	8.8	9.2
Net Profit	16	(32)	77	144	178
Growth (%)	-87.2	-	-	86.5	23.5
EPS	0.7	(1.5)	3.3	6.2	7.7
P/E	178.4	-	36.3	19.5	15.7
P/BV	4.5	4.7	2.1	2.1	2.0
EV/EBIDTA	32.4	94.7	13.3	8.0	6.5
ROE (%)	2.5	(5.9)	5.8	10.6	12.5
ROCE (%)	2.9	(2.9)	5.7	10.1	11.8

Source: Company; Sharekhan estimates

Excel's acquisition to be margin accretive

Greaves has decided to acquire Excel Control Linkage Private Limited (Excel). Excel is one of the largest players in mechanical and electronic motion control systems and manufactures push-pull cables, levers & sensors etc. In FY2022, Excel reported a turnover of Rs 167 cr. This acquisition would help Greaves to cater to the commercial vehicle segment. Initially, Greaves would acquire a 60% stake at an enterprise value of Rs 385 cr and the whole transition will be completed by August 2026. It would be acquiring 60% stake at 7.5x FY23 EV/EBITDA, the next 10% stake at 7x FY24EV/EBITDA, next 10% at 7x FY25EV/EBITDA and final 20% stake at 7x FY26EV/EBITDA. Greaves would also pay a one-time non-compete fee to the promoters of Excel. The acquisition would be margin accretive on consolidation as Excel delivers a higher margin than Greaves. Excel delivered an EBITDA margin at 29% in FY22 compared to GCL's peak EBITDA margin in the recent past at 14.9% in FY17.

Prepared to drive even without subsidies

The management believes that the government has offered FAME subsidy largely to motivate the customers to opt the electric vehicles. However, the management observes that customers who once uses electric vehicle does not shift again to ICs due to smooth usage and cost-effective transportation solutions. Further, the cost of the production is also expected to come down over the period due to volume ramp up, rise in localization and expected decline in imported battery cell costs. The EV segment is expected to grow dramatically once the local manufacturing of battery cell would begin in India on sharp reduction in costs. Hence, the company is preparing its business plan, which can be executed successfully without subsidies. Greaves has already submitted required documents to avail FAME subsidies and waiting for a disbursement from government. The total pending subsidy is around Rs 240 crore by December 2023. Currently EV penetration has reached to 5% in domestic two-wheeler segment and likely to reach to 30% by FY25.

Operating performance in electric mobility business is improving

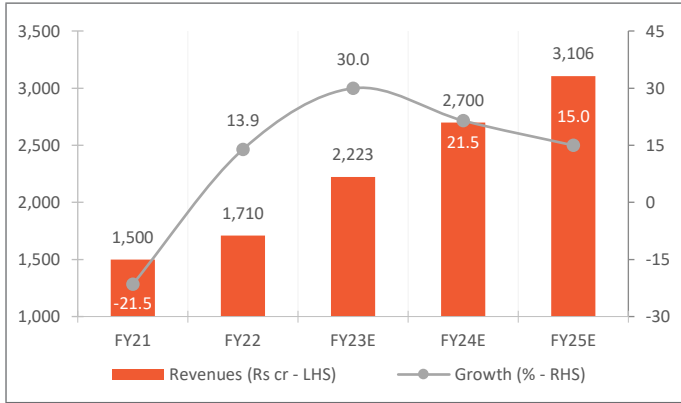
In 9MFY23, the electric mobility division has reported 106% growth in volumes to 76,660 units and reported 160% growth in revenue to Rs 741 crore. With a rise in volumes and improved product mix, the electric mobility division has reported improvement in operating performance, as operating losses come down sharply in 9MFY23. Overall EBITDA loss come down to Rs 20 crore with EBITDA margin stood at -3% compared to EBITDA loss of Rs 29 crore in 9MFY22 with EBITDA margin at -10%. We attributed the EBITDA loss in 9MFY23 to muted performance in Q3FY23 on regulatory challenges. The electric division has reported EBITDA loss of Rs 36 crore.

Electric mobility segment would do well in Q4FY23

The performance of electric mobility business was an aberration in Q3FY23 as it was a lack of clarity regarding the clauses of battery management related norms and hence it reduces production in Q3, while the retail demand was strong. However, the overall production has been normalized in Q4 and the management indicated that electric mobility segment would report a sequential improvement in its performance in Q4FY23, given it sold around 14,000 plus units in January 23 compared to 14140 units in Q3FY23.

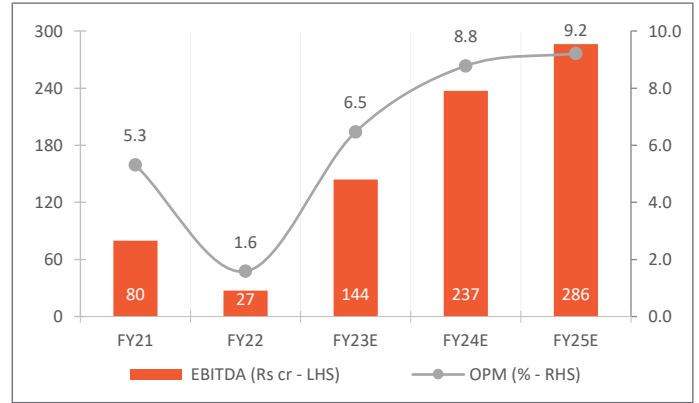
Financials in charts

Revenue and Growth Trend



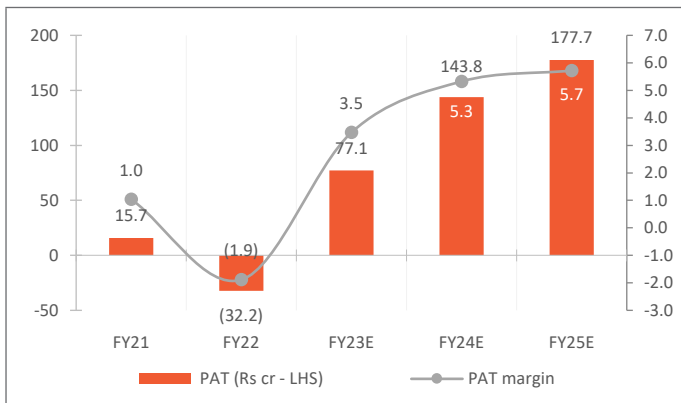
Source: Company, Sharekhan Research

EBITDA and OPM Trends



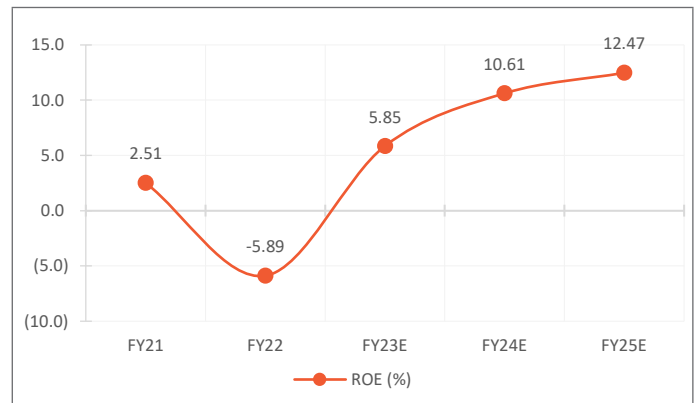
Source: Company, Sharekhan Research

PAT and PAT margin Trends



Source: Company, Sharekhan Research

ROE Trend



Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector View – Demand picking up

Business outlook for the automotive segments is expected to improve with the normalisation of economic activities. Automotive demand is witnessing strong recovery in the 2W and 4W segments, aided by pent-up demand and increased personal mobility transport. Rural and semi-urban markets remain buoyant on robust farm income this year. Recovery in export destinations is auguring well for the sector. In addition, the 3W industry is expected to gain demand as the economy is getting normalised. The opening of schools, educational institutions, corporates, and local/metro trains will be key catalysts for demand.

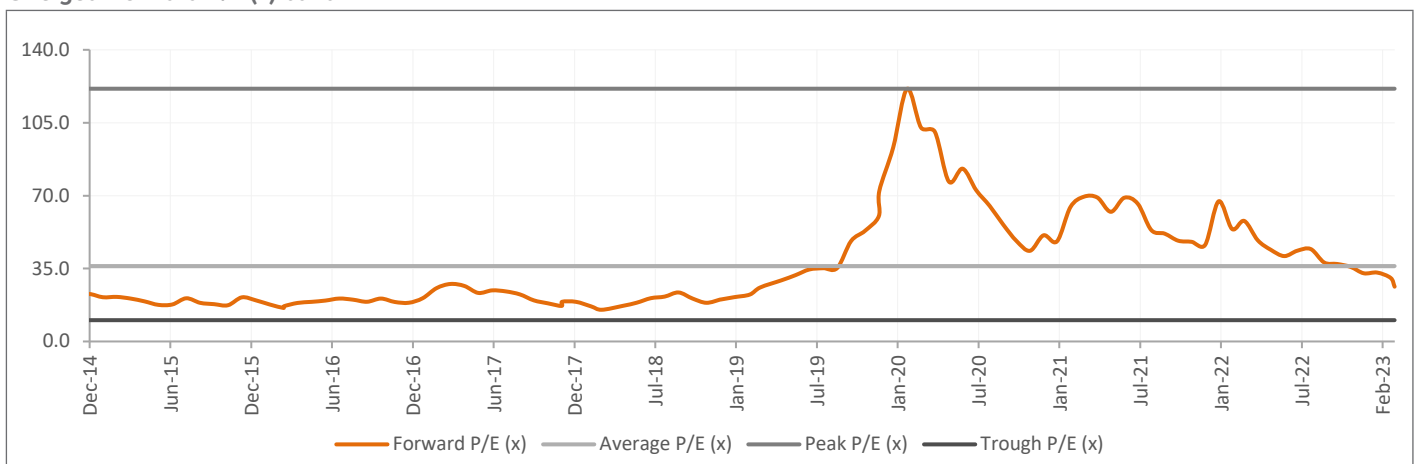
■ Company Outlook – Beneficiary of EV adoption in 2W and 3W segments

Greaves is expected to benefit from its improvement in business, driven by a robust recovery in non-auto business and electric mobility but a slower-paced recovery in 3Ws. We believe the company benefits from its re-focus strategy on automotive, non-automotive, e-mobility, retail, and finance businesses. In our view, the refocused strategy has played well for the company, as Greaves has displayed a strong quarterly revenue run-rate despite lacklustre sales in 3W engines. Greaves is well positioned to benefit from the government's push towards faster EV adoption, especially e-2Ws and e-3Ws, where the company has strong product lines. Given the improved new business outlook and expectations of improving 3W sales, we maintain our positive stance on the company.

■ Valuation – Maintain Buy rating with an unchanged PT of Rs. 183

After visiting Greaves' Ranipet plant and management interactions, we believe that Greaves is strategically building up new business (EVs & retail) for growth and continue to strengthen its legacy business via organic as well as organic route. While subdued performance in EV business has impacted its performance in Q3FY23 due to change in regulatory norms we understand that EV business would revive from Q4FY23 onwards. Further, the management is looking for a structural and sustainable growth in the EV business and indicated that it has been equipped to launch products in entry level to premium segment but gradually introducing products according to relevant demand scenario. Despite a muted Q3FY23, operating losses in the EV business came down on a rise in volumes and better product mix. This makes us to believe that operating performance would improve further on ramping up of volumes and operating leverage. Along with the EV business, a consolidation of high-margin Excel business would drive its overall profitability and customer profile in engineering division. We expect the financial performance of the e-mobility business to strengthen going forward, driven by increasing contribution of high-speed e-2Ws, increasing retail penetration, and new launches. We believe that GCL's diversification strategy is reaping the benefit as it has been broadening the growth prospects in both B2B and B2C space. The stock is trading at a P/E multiple of 15.7x and EV/EBITDA multiple of 6.5x its FY2025E estimates. We maintain our Buy rating on the stock with an unchanged PT of Rs 183.

One-year forward P/E (x) band



Source: Sharekhan Research

Peer Comparison

Companies	CMP (Rs/Share)	P/E (x)			EV/EBITDA (x)			ROCE (%)		
		FY22	FY23E	FY24E	FY22	FY23E	FY24E	FY22	FY23E	FY24E
Greaves Cotton	121		36.3	19.5		13.3	8.0		5.7	10.1
Alicon Castalloy	742	49.5	21.4	12.4	10.4	7.0	5.0	8.1	13.0	17.8
Gabriel India	148	23.7	15.2	11.6	13.5	9.1	6.6	12.1	15.6	18.8

Source: Company; Sharekhan Research

About company

Greaves is one of the leading suppliers of powertrain and related solutions to auto original equipment manufacturers (OEMs). The company has the lion's share in the 3W diesel segment. The company's products can be classified into four categories – engines (48% of sales), aftermarkets (21% of sales), e-mobility (31% of sales), and others (1% of sales). The other segment includes power gen sets, agri-equipment, and other application-based engines.

Investment theme

Greaves benefits from its re-focus strategy on automotive, non-automotive, e-mobility, retail, and finance businesses. Over the past few years, the company has transformed its businesses to expand its markets from 3W diesel engines to last-mile mobility, move beyond one product/application/fuel with a focus on clean tech, increase value to customers through B2C, expand products to solutions, and leverage the company's brand and penetration. The refocus strategy has played well for the company, as Greaves has displayed a strong quarterly revenue run-rate despite lacklustre sales in 3W engines in FY2021, which underpin our strong belief in the management. Given the improved new business outlook and expectations of improving 3W sales, we expect the company's revenue and profitability to remain firm in the medium term. Moreover, its strategic move towards investment in Ampere has a huge potential for businesses and a valuation multiple. The company is open to strategic and/or technical partners to strengthen its e-mobility business. Hence, we maintain our Buy rating on the stock.

Key Risks

- ♦ The company's performance can be impacted adversely if commodity prices again start to rise in the near term.
- ♦ Prolonged delay in the recovery of the 3W industry can materially impact our revenue projections.

Additional Data

Key management personnel

Karan Thapar	Chairman
Nagesh Basavanhalli	Executive Vice Chairman
Dr Arup Basu	Managing Director
Dalpat Jain	Group CFO

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	KARUN CARPETS PVT LTD	55.5
2	Life Insurance Corporation Of India	1.55
3	New India Assurance Co Ltd	1.54
4	L&T Mutual Fund Trustee Ltd	1.44
5	Matthews International Capital	0.99
6	Aditya Birla Sun Life Asset Management	0.97
7	Dimensional Fund Advisors LP	0.41
8	BlackRock Inc	0.16
9	Teachers Insurance & Annuity Ass of America	0.05
10	State Street Corp	0.04

Source: Bloomberg

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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 deteriorating 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

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