Sharekhan by BNP PARIBAS

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Stock Update

Plant visit update

Greaves Cotton Ltd

Diversification is the kingpin

Automobiles	Sharekhan code: GREAVESCOT
Reco/View: Buy ↔	CMP: Rs. 155
	Price Target: Rs. 183 ↔

↑ Upgrade ↔ Maintain ↓ Downgrade

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		↔	

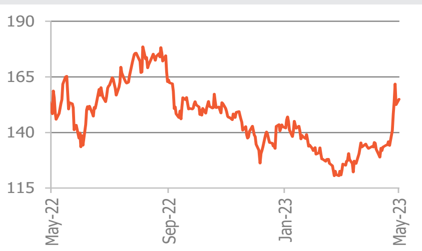
Company details

Market cap:	Rs. 3,584 cr
52-week high/low:	Rs. 184 /118
NSE volume: (No of shares)	11.7 lakh
BSE code:	501455
NSE code:	GREAVESCOT
Free float: (No of shares)	10.2 cr

Shareholding (%)

Promoters	55.7
FII	4.5
DII	4.3
Others	35.4

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	15.7	13.0	-1.4	18.3
Relative to Sensex	12.1	10.4	-3.3	0.5

Sharekhan Research, Bloomberg

Summary

- We retain our Buy rating on Greaves Cotton Limited with an unchanged TP of Rs. 183 on recovery in e-mobility business, traction in retail business, and acquisition of margin-accretive Excel's business.
- The company aims to play on multiple price points in the E2W business and is expected to launch NXG in the E2W space in FY2024.
- The acquisition of Excel Controlinkage Pvt. Ltd. would further diversify its revenue stream along with new customer additions.
- The stock trades at a P/E multiple of 19.9x and EV/EBITDA multiple of 9.6x its FY2025E.

For Q4FY2023, Greaves Cotton Limited (GCL) reported revenue and APAT above estimates, while EBITDA margin was below estimates on account of higher-than-expected revenue growth, else EBITDA was close to estimate. Lower-than-expected EBITDA margin can be attributed to higher-than-expected revenue growth and gross margin contraction. Q4FY2023 performance was largely driven by sharp improvement in the e-mobility business on a sequential basis, given the e-mobility business was impacted in Q3FY2023 to change battery-related norms. Revenue increased by 61% q-o-q to Rs. 827 (vs. estimate of Rs. 727 crore) on account of a 20.7% q-o-q increase in revenue from the engine business and a 171% q-o-q increase in revenue from the e-mobility business. The sharp jump in revenue from the e-mobility business was due to recovery in volumes as the production was impacted in Q3FY2023 because of regulatory issues. EBITDA surged sharply from Rs. 3.1 crore in Q3FY2023 to Rs. 49 crore (against estimate of Rs. 52.6 crore) in Q4FY2023, while EBITDA margin improved from 0.6% in Q3FY2023 to 5.9% in Q4FY2023. With this operating performance and a 33.3% q-o-q increase in other income, APAT came at Rs. 39.2 crore (against our estimate of Rs. 35.3 crore) in comparison to adjusted loss of Rs. 5 crore in Q3FY2023. We believe GCL's diversification strategy is reaping the benefit as it broadened growth prospects in both B2B and B2C spaces. The stock is trading at a P/E multiple of 15.7x and EV/EBITDA multiple of 6.5x its FY2025E. We maintain our Buy rating on the stock with an unchanged price target (PT) of Rs. 183.

Key positives

- E-mobility volumes have recovered from 14,140 units in Q3FY2023 to 38,954 units in Q4FY2023.
- The e-mobility segment registered breakeven at the operating level and recorded EBITDA margin at around 1% in Q4FY2023 compared to negative EBITDA margin (-2%) in Q3FY2023.
- Despite flat revenue, the retail segment registered 280-bps q-o-q improvement in EBITDA margin to 20.7%.

Key negatives

- Gross margin contracted by 510 bps q-o-q to 25.6%, which restricted EBITDA margin expansion.
- EBIT margin in the engine business contracted by 30 bps q-o-q to 12.6%.

Management Commentary

- B2C business is now contributing 66% to its revenue and the company continues to focus on its growth in the B2B business and enhancing the potential of its B2C business as per its diversification strategy.
- EV business has the potential to deliver EBITDA margin like that of the IC business on volume ramp- up, led by operating leverage benefit.
- Ampere would launch its electric scooter, NXG, in FY2024 and aims to play at multiple price points in the EV space.
- Greaves has completed a 60% stake purchase in Excel Controlinkage, effective from May 8, 2023.

Our Call

Valuation – Maintain Buy rating with an unchanged PT of Rs. 183: With recovery in the e-mobility business, GCL has reported strong topline performance in Q4FY2023. Hence, APAT came above our estimates. Further, management is strategically looking to expand both in the B2B and B2C businesses and is looking to play on multiple price points in the E2W space, as the company is expected to expand its E2W portfolio. We expect the financial performance of the e-mobility business to strengthen going forward, driven by increasing contribution of high-speed E2Ws, increasing retail penetration, and new launches. While the company has been focussing on the new-age business for sustainable growth, it has been equally looking for sustainable growth in its engineering segment, where it has been catering to the automobile engine and industrial engine segment. Along with the EV business, consolidation of high-margin Excel's business would drive its overall profitability and customer profile in the engineering division. We retain our Buy rating on GCL with an unchanged PT of Rs. 183 on recovery in the e-mobility business, traction in the retail business, and acquisition of margin-accretive Excel's business.

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) Rs cr

Particulars	FY21	FY22	FY23P	FY24E	FY25E
Revenues	1,500.4	1,709.7	2,699.5	3,081.7	3,448.2
Growth (%)	-21.5	13.9	57.9	14.2	11.9
EBIDTA	79.7	27.2	133.4	231.1	284.5
OPM (%)	5.3	1.6	4.9	7.5	8.3
Net Profit	15.7	(33.0)	90.5	146.7	180.6
Growth (%)	-87.4	-310.4	-374.4	62.0	23.2
EPS	0.7	(1.4)	3.9	6.3	7.8
P/E	229.0	(108.8)	39.7	24.5	19.9
P/BV	4.6	4.8	2.3	2.1	1.9
EV/EBIDTA	41.6	123.7	22.0	12.3	9.6
ROE (%)	2.0	-4.4	5.7	8.6	9.7
ROCE (%)	2.7	-2.0	6.1	9.1	10.2

Source: Company; Sharekhan estimates

E-mobility business: Returned to the growth path

- GCL is expected to launch one new product, NXG, (high speed) in the electric scooter segment in FY2024E.
- The company has yet to receive FAME 2 subsidy from the government. At the end of FY2023, the total unreceivable FAME 2 subsidy stands at Rs. 350 crore.
- The e-mobility business recovered sharply on a sequential basis, as volumes increased from 14,140 units in Q3FY2023 to 38,954 units in Q4FY2023, which resulted in a sharp jump in revenue from Rs. 142 crore in Q3FY2023 to Rs. 383 crore in Q4FY2023.
- While volume and revenue performance has improved, profitability has not enhanced in the same manner due to increased fixed costs because of addition of headcounts and delay in passing on of increased cost to customers pertaining to implementation of new norms.
- The e-mobility segment reported an EBITDA margin of 1% in Q4FY2023 against -2% in Q3FY2023 and 2% in Q2FY2023.
- With implementation of the new regulatory norms, the company has increased prices by Rs. 4,000/units in December 2022 and further increased prices for Magnus in April 2023.
- Volume trend in the EV space has been strong – both in retail as well as wholesales segment.
- Going forward, management intends to grow in line with the industry and assumes EBITDA margin in the EV business would reach to IC's EBITDA margin level in the coming years, led by operating leverage on volume ramp-up.
- Further, management is looking for aggressive growth in the E3W space. The company is strategically looking to play on various price points in the EV space to expand its market share.

Engine business: A structural play

- In Q4FY2023, automotive engine volumes increased by 9.9% q-o-q to 20,147 units. Volumes in the non-auto segment increased by 58.2% q-o-q to 13,579 units.
- With improved volumes, revenue increased by 20.7% q-o-q to Rs. 401 crore, though EBIT margin contracted by 30 bps q-o-q to 12.6%.

Retail segment: Asset-light and profitable business model

- With an aim to continue to capture its presence in the aftermarket segment and secure recurring revenue, the company has been focusing on the multi-brand retail segment, which offers components as well as services to retail consumers.
- The retail segment contributed 20% to its revenue in FY2023.
- On a q-o-q basis, while revenue remains flat at Rs. 140 crore, EBITDA margin expanded by 280 bps q-o-q to 20.7%.
- Management continues to share an optimistic outlook for the retail segment.

Acquired 60% stake in Excel Controlinkage

- GCL has completed the 60% stake acquisition in Excel Controlinkage, effective from May 8 , 2023.
- Excel has been enjoying a strong order book and has been delivering robust operating margin due to its exposure in the export market and aftermarket other than domestic OEMs.
- Excel generates 40% of its revenue from export markets.
- On proforma basis , consolidated revenue would be Rs. 880 crore in Q4FY2023 compared to Rs. 827 crore on adding the performance of Excel. While the company has been focussing on the new-age business for sustainable growth, it has been equally looking for sustainable growth in its engineering segment, where it has been catering to automobile engine and industrial engine segments.
- Excel delivered EBITDA margin at 29% in FY2022 compared to GCL's peak margin at 14.9% in FY2017. We attribute selective and judicious order bookings, exposure to export markets, technology-added products, and better customer mix for Excel's superior EBITDA margin.

Others

- The company has been strategically focussing on the BtoC business and now BtoC business contributes 66% to the total revenue.
- Net cash stands at Rs. 1,162 crore and the company intends to invest cash on further capex and investments going forward.

Results (Consolidated) Rs cr

Particulars	Q4FY23	Q4FY22	YoY%	Q3FY23	QoQ%
Revenues	826.9	620.8	33.2	513.5	61.0
Total operating costs	778.0	580.2	34.1	510.4	52.4
EBITDA	49.0	40.7	20.4	3.1	1,469.2
Depreciation	15.2	15.0	1.5	13.1	15.7
Interest	1.2	2.2	(47.0)	2.4	(51.5)
Other income	23.8	9.6	146.5	17.8	33.3
PBT	56.4	33.2	70.0	5.4	938.1
Tax	15.4	8.8	74.3	8.9	72.7
Adjusted PAT	39.2	23.0	70.8	(5.0)	NA
Reported PAT	27.2	16.7	62.9	(5.7)	NA
Adjusted EPS	1.69	1.0	70.8	(0.22)	NA

Source: Company, Sharekhan Research

Key ratios (Consolidated)

Particulars	Q4FY23	Q4FY22	YoY (bps)	Q3FY23	QoQ (bps)
Gross margin (%)	25.6	26.3	-70	30.7	-510
EBIDTA margin (%)	5.9	6.5	61	0.6	530
Net profit margin (%)	4.7	3.7	213	(1.0)	570
Effective tax rate (%)	27	26.6	106	-	-

Source: Company, Sharekhan Research

Outlook and Valuation

Sector View – Demand picking up

The business outlook for the automotive segment 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

GCL is expected to benefit from its improvement in business, driven by a robust recovery in the non-auto business and electric mobility but a slower-paced recovery in 3W. 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 GCL 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

With recovery in the e-mobility business, GCL has reported strong topline performance in Q4FY2023. Hence, APAT came above our estimates. Further, management is strategically looking to expand both in the B2B and B2C businesses and is looking to play on multiple price points in the E2W space, as the company is expected to expand its E2W portfolio. We expect the financial performance of the e-mobility business to strengthen going forward, driven by increasing contribution of high-speed E2Ws, increasing retail penetration, and new launches. While the company has been focussing on the new-age business for sustainable growth, it has been equally looking for sustainable growth in its engineering segment, where it has been catering to the automobile engine and industrial engine segment. Along with the EV business, consolidation of high-margin Excel's business would drive its overall profitability and customer profile in the engineering division. We retain our Buy rating on GCL with an unchanged PT of Rs. 183 on recovery in the e-mobility business, traction in the retail business, and acquisition of margin-accretive Excel's business.

Peer Comparison

Companies	CMP (Rs/ Share)	P/E (x)			EV/EBITDA (x)			ROCE (%)		
		FY22	FY23E	FY24E	FY22	FY23E	FY24E	FY22	FY23E	FY24E
Greaves Cotton	155		39.7	24.5	123.7	22.0	12.3	-2.0	6.1	9.1
Alicon Castalloy	772	51.5	22.3	12.9	10.8	7.2	5.2	8.1	13.0	17.8
Gabriel India	172	27.6	18.9	13.5	15.8	10.7	7.8	12.1	15.6	18.8

Source: Company; Sharekhan Research

Change in estimates

Particulars	Earlier		New		% change	
	FY24E	FY25E	FY24E	FY25E	FY24E	FY25E
Revenue	2700	3106	3,082	3,448	14.1%	11.0%
EBITDA	237	286	231	284	-2.5%	-0.5%
EBITDA margin	8.8%	9.2%	7.5%	8.3%		
PAT	144	178	147	181	1.8%	1.5%
EPS	6.2	7.7	6.3	7.8	1.8%	1.5%

Source: Company; Sharekhan Research

About the company

GCL 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 three categories – engines , aftermarket, and e-mobility .

Investment theme

GCL 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 GCL has displayed a strong quarterly revenue run-rate, which underpins 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

Top shareholders

Sr. No.	Holder Name	Holding (%)
1	Karun Carpets Pvt Ltd	55.7
2	Life Insurance Corp of India	1.6
3	New India Assurance Co Ltd/The	1.5
4	Matthews International Capital Management LLC	1.0
5	Aditya Birla Sun Life Asset Management Co Ltd	0.9
6	Dimensional Fund Advisors LP	0.2
7	BlackRock Inc	0.2
8	State Street Corp	0.04
9	Teachers Insurance & Annuity Association of America	0.04

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

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