Stock Update

Challenging times to persist

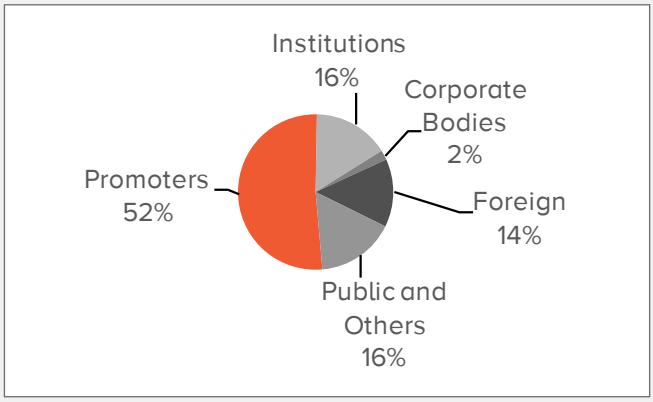
Greaves Cotton

Reco: Hold | CMP: Rs144

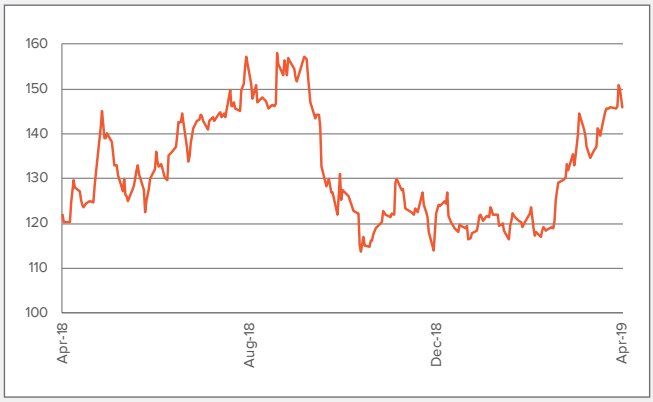
Company details

Price target:	Rs155
Market cap:	Rs3,517 cr
52-week high/low:	Rs165 / 111
NSE volume: (No of shares)	3.5 lakh
BSE code:	501455
NSE code:	GREAVESCOT
Sharekhan code:	GREAVESCOT
Free float: (No of shares)	11.8 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	9.0	24.6	18.2	25.2
Relative to Sensex	5.4	15.5	5.4	8.8

Key points

- **Traditional 3W engines business continues to remain under pressure; shift in favor of alternate fuel run engines and a likely steep increase due to BS6 emission norms to impact volumes:** Greaves cotton Limited (GCL) derives around 40% of its revenues from the 3wheeler diesel engines segment. The diesel engine segment demand has been under pressure in the recent past given the Government thrust to promote environment friendly fuel to curb pollution levels. Various OEM's have launched CNG powered vehicles even in the goods segment (earlier goods segment was fully diesel driven) which is leading to market share loss for the diesel powered vehicles. GCL 3W business in 9MFY2019 has been flat as against strong 19% growth for 3W industry. Also in the recent past, the Government has lifted the need for permits for alternate fuel (CNG and petrol) in 3W passenger category in which GCL supplies to only one OEM customer compared to 4-5 customers currently, which would lead to the underperformance of the GCL 3W business. Moreover, the upcoming BS 6 emission norms which would come into effect from 1st April 2020, would result in a 10-12% increase in the vehicle costs which would adversely impact the volumes. We expect GCL 3W volumes to be flat in FY2020 with a marginal drop expected in FY2021.

- **New business segments margin dilutive; steep increase in BS 6 costs cannot be fully passed; margins to decline:** GCL has consistently emphasized on diversifying its revenues streams to offset the slowdown in the 3W business. GCL forayed into the multi-brand aftermarket space (GCL sources products manufactured by others and sells it through its distribution network). In the 3w spares business. the company has widened its product offerings, which almost covers 85% of the products industry. Also, the company has recently entered the 2w spares business. In order to capitalize on the electric two wheelers opportunity, the company has acquired a majority stake in Ampere and plans to introduce new products. The multi-brand segment is a trading business while the electric scooter business is loss making due to lack of scale. Further, transition from BS4 to BS6 norms would entail an increase in the prices by steep

10-12% which cannot be fully passed onto the consumer. We expect GCL margins to drop from 14.2% in FY2018 to 13.3% in FY2021.

- **Outlook- Earnings growth to slow down sharply; expect 5% earnings CAGR between FY19-21:** GCL 3W business is expected to remain under pressure over the next two years driven by a shift towards gasoline/CNG engines. Further, GCL margins are likely to drop led by increased costs due to shift to BS6 norms and increased proportion of low margin multi-brand products and electric scooters. We expect earnings growth to decelerate to 5% CAGR over FY2019-2021 period.

- **Valuations- Introduce FY2021 estimates; Retain Hold with a revised PT of Rs 155:** We have broadly retained our earnings estimates for FY2020. We have introduced FY2021 estimates in this note. At the CMP the stock trades at 18.3/17.3x its FY20/FY21E estimates, which is closer to the higher end of historical average multiple, thus leaving a limited upside potential. We retain our Hold recommendation on the stock with a revised PT of Rs 155 as we rollover our valuation multiple on FY2021 earnings. (Earlier PT of Rs 134)

Valuations **Rs cr**

Particulars	FY17	FY18	FY19E*	FY20E*	FY21E*
Net sales (Rs cr)	1,634.3	1,792.1	2,074.2	2,240.1	2,464.1
Growth (%)	1.3	9.7	15.7	8.0	10.0
EBITDA (Rs cr)	243.4	255.3	280.0	302.4	327.7
OPM (%)	14.9	14.2	13.5	13.5	13.3
Adjusted PAT (Rs cr)	178.1	154.5	185.4	192.5	204.3
Growth (%)	3.0	-13.3	20.0	3.8	6.1
FD EPS (Rs)	7.3	6.3	7.7	7.9	8.3
P/E (x)	19.7	22.8	18.8	18.3	17.3
P/B (x)	3.8	3.7	3.5	3.4	3.3
EV/EBITDA (x)	12.7	11.7	10.8	10.0	9.1
RoE (%)	19.3	16.1	18.9	18.8	18.9
RoCE (%)	25.9	25.1	27.2	27.3	27.7

*includes Ampere numbers

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Compliance Officer: Mr. Joby John Meledan; Tel: 022-61150000; email id: compliance@sharekhan.com;

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