Narnolia
Advance Strategy · Simple Solutions

EICHERMOT

NEUTRAL

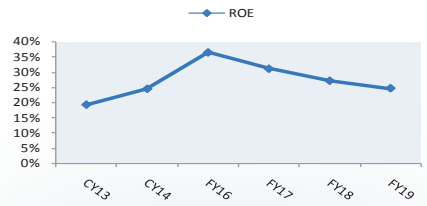
23-Jun-17

INDUSTRY -	AUTOMOBILE
BSE Code -	505200
NSE Code -	EICHERMOT
NIFTY -	9630

Company Data

CMP	27652
Target Price	**28009**
Previous Target Price	28009
Upside	**1%**
52wk Range H/L	29983/18006
Mkt Capital (Rs Cr)	75,277
Av. Volume (,000)	10

RoE on declining trend

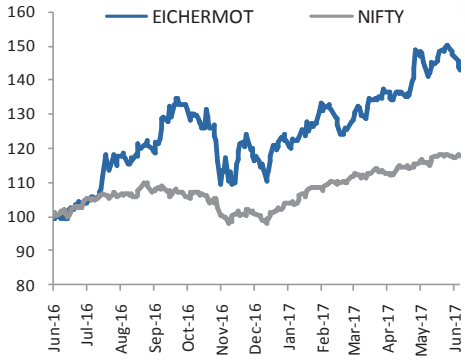


Shareholding patterns %

	4QFY17	3QFY17	2QFY17
Promoters	50.6	50.6	50.6
Public	49.4	49.4	49.4
Total	100.0	100.0	100.0

Stock Performance %

	1Mn	3Mn	1Yr
Absolute	0.2	12.7	48.2
Rel.to Nifty	(2.4)	6.0	31.3



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Key Highlights of the Report:

- ☑ Slow down in demand for two wheelers has resulted in reduction in waiting period to 2 months from 3 months and it will sharply reduce going ahead as the new facility comes in FY19.
- ☑ We expect sluggish growth for commercial vehicles in FY18 because of price increase due to BS-IV transition, Monsoon and GST implementation.
- ☑ Eicher Motors volumes has grown at 42% CAGR over last 5 years well ahead of industry growth.
- ☑ Currently the stock is trading at 8.8x FY19E P/B. Going ahead lower PAT growth compared to previous years gives us limited cushion on the valuation front. Hence we change our rating from 'Hold' to 'Neutral' with the target price of Rs.28009.

Financials/Valu	CY14	FY16	FY17	FY18E	FY19E
Net Sales	8,738	6,173	7,033	7,819	8,799
EBITDA	1,115	1,690	2,174	2,375	2,704
EBIT	895	1,553	2,020	2,205	2,410
PAT	615	1,338	1,667	1,832	2,021
EPS (Rs)	227	493	613	673	743
EPS growth (%)	56%	117%	24%	10%	10%
ROE (%)	24%	37%	31%	27%	24%
ROCE (%)	36%	43%	38%	32%	28%
BV	928	1,345	1,964	2,517	3,140
P/B (X)	16	14	13	11	9
P/E (x)	66	39	41	41	37

RECENT DEVELOPMENT: Commencement of Vallam Vadagal plant

- ✓ Earlier the company was facing capacity constraints because of huge demand for its classic models. But the management of the company took right decision to increase the capacity in phased manner and in-line with the demand.
- ✓ The Vallam Vadagal facility is likely to commence production from August 2017 and with this expansion total capacity for two wheelers will reach to 825000 units per annum in FY18.
- ✓ The company has target to take the production capacity to 900000 units per annum by FY2018-19. Eicher Motors has planned Rs.800 crore of capex in this regard in FY19.
- ✓ Besides that the company is also working on developing refreshed versions of popular models from its two technical centres situated in Chennai and UK. Significant part of capex will be spent on developing these models

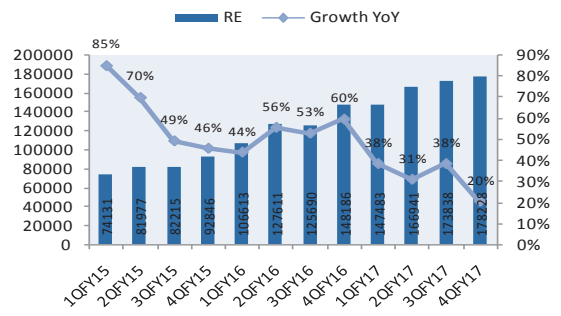
Quarterly Performance

Financials	4QFY16	1QFY17	2QFY17	3QFY17	4QFY17	YoY %	QoQ%	FY16	FY17	YoY %
Total Volumes ('000)	148	147	167	174	178	**20%**	**3%**	601	666	**11%**
Realization(Rs./ bike)	104258.2	105503.7	105121	105544.2	105935.1	**2%**	**0%**	102954	105526	**2%**
Net Sales	1,532	1,556	1,755	1,835	1,888	**23%**	**3%**	6,173	7,033	**14%**
Other Income	45	47	66	59	55	**22%**	**-7%**	178	227	**28%**
COGS	833	831	912	969	993	**19%**	**2%**	3,435	3,704	**8%**
Employee Cost	77	91	100	106	106	**37%**	**0%**	350	402	**15%**
Other Expenses	175	164	201	183	205	**17%**	**12%**	699	753	**8%**
EBITDA	447	470	542	577	585	**31%**	**1%**	1,690	2,174	**29%**
Depreciation	37	39	36	36	43	**16%**	**21%**	137	154	**13%**
Interest	1	1	1	1	1	**91%**	**14%**	2	4	**68%**
PBT	454	477	572	599	596	**31%**	**-1%**	1,729	2,244	**30%**
Tax	144	147	184	200	189	**31%**	**-6%**	539	720	**34%**
PAT	343	376	413	418	459	**34%**	**10%**	1,338	1,667	**25%**

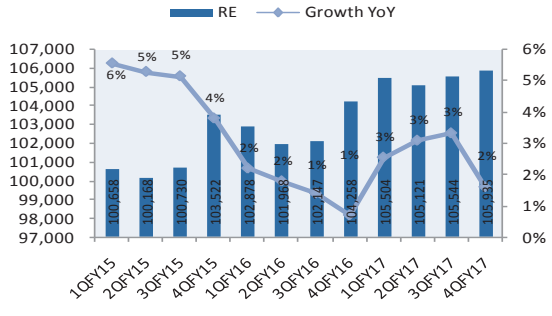
Strong growth momentum maintained

- ✓ Net sales grew by 23%YoY to Rs.1888 crore which was in-line with our estimates (Rs.1915 crore). Volumes grew by 21%YoY and realization have also grown by 2%YoY.
- ✓ Higher sales of Classic 350 motorcycles led to this volume growth. These motorcycles have 2 months of waiting period in the domestic market. Export volumes have seen sharp increase of 41%YoY during the quarter. On the commercial vehicle front VECV reported volume growth of 20%YoY in 4QFY17. The growth was supported by higher sales of Medium and Heavy Commercial vehicles on the back of BS-IV transition.
- ✓ Reported EBITDA grew by 30.9%YoY to Rs.585 crore. Lower advertising and promotion expenses helped company to post 31% of EBITDA margin.
- ✓ Depreciation and Amortization expenses remain higher in the quarter due to operationalization of valam vadagal facility.
- ✓ PAT stood Rs.459 crore at a growth of 34%YoY due to higher other income.

Royal Enfield volume trend



Royal Enfield realization trend

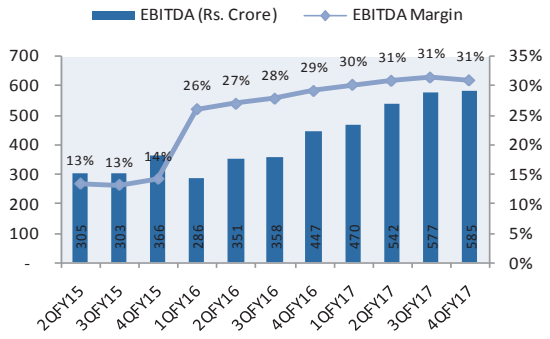


Higher operating leverage leads to further margin expansion

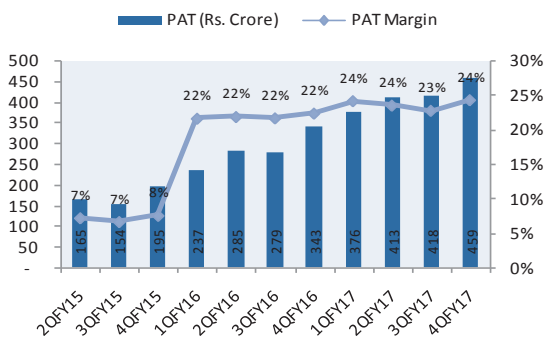
Margin %	4QFY16	1QFY17	2QFY17	3QFY17	4QFY17	YoY(+/-)	QoQ(+/-)	FY16	FY17	YoY(+/-)
Gross Margin	46%	47%	48%	47%	47%	**1.81%**	**0.00**	44%	47%	**0.03**
EBITDA Margin	29%	30%	31%	31%	31%	**1.81%**	**0.00**	27%	31%	**0.04**
PAT Margin	22%	24%	24%	23%	24%	**1.94%**	**0.02**	22%	24%	**0.02**

- ✓ Gross Margin improved by 180 bps YoY to 47.4% on the back of lower commodity prices and higher realization during the quarter.
- ✓ The company has been taking the advantage of high operating leverage based on the higher volumes which led the EBITDA margin to 31% during the quarter up by 180 bps YoY.
- ✓ PAT margin increased by 190 bps owning to minimal finance cost and higher other income in the 4QFY17.

EBITDA and EBITDA Margin trend



PAT and PAT Margin trend



Concall Highlights:

- ✓ The company has robust order book for classic 350 models
- ✓ Valam vadagal facility will start from August 2017 and the total capcity will reach to 825000 units p.a.
- ✓ Capex Rs.800 crore
- ✓ Waiting period of 2 months for classic 350.
- ✓ Exports: RE sales is higher in developed markets than developing market. (UK, Germany, Italy and France has on around 40-60 dealers in each countries)
- ✓ The company has 1 store in Bangkok, 1 in Jakarta and 4 in Columbia.
- ✓ 22 new exclusive stores will be added in the international market.
- ✓ Currently the company has 675 dealers and the company does not have any plans for expanding through sub-dealers.
- ✓ The outlook for commercial vehcles can be subdued going ahead.
- ✓ Management expects that the rollout of GST on July 1 and it will benefit the consumers tax wise and so may incentivize them to buy more trucks.
- ✓ The company will come out with refresh versions of existing Royal Enfield models the current fiscal.
- ✓ Spare parts stands 5-6 percent of total revenue.
- ✓ On the BS-III inventory, the management has stated that the company has left with very minimal BS-III stocks which can be sold to export markets.

Investment Arguments:

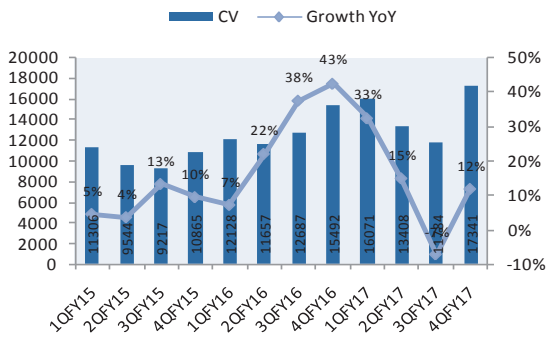
- ✓ **Focus to keep RE as a Premium brand-** Eicher Motors is catering niche segment in the Indian motorcycles market. In order to make it a global premium brand the management has complete focused approach to expand through exclusive dealers and stores. The company does not have any plan to expand through sub dealers strategy generally used by other two wheeler manufacturers.

- ✓ **Margins to come under pressure due to New Plants-** Considering the 2 months waiting period the company increased the capacity from 720000 units to 825000 units per annum looking at the demand scenario. We expect that there could be some pressure on margins once the new plant gets operational and new plant will take atleast 5 months to ramp up production.

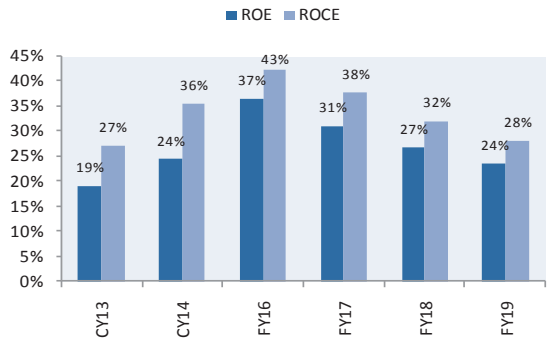
- ✓ **Expanding footprints in export markets-** RE has expanded its footprint in the exports by opening up stores in the various export markets like; Latin America, indonesia, bangkok and Madrid. The investments are becoming fruitful in terms of higher volumes from exports. The company has already more than 150 RE stores in UK, Germany, Italy and France. However considering the potential in the developing economies Royal Enfield has started looking for the big opportunity in the fast growing Brazilian market.

- ✓ **Commercial Vehicles industry to be sluggish in FY18-** Currently the CV segment is going through the pain of BS-IV transition from BS-III. Implementation of GST will free up the idle capacity and it will reduce the demand for commercial vehicles for couple of quarters. Infrastructure and Mining segment also slows down for the first half due to Monsoon. So we expect overall growth to be muted in FY18.

VECV volume trend



Declining trend in ROE and ROCE



View & Valuation

Eicher Motors is well placed in the domestic two wheeler industry. RE volumes have grown at a 42% CAGR over last 5 years. But we expect that the demand has been slowing down as the waiting period has come down to 2 months from 3 months and it will sharply reduce going ahead as the new facility comes in FY19. UM Renegade could be potential threat for the company in the cruiser segment as it has started gaining market share in that category. In the commercial vehicle space VECV has positioned itself as a third strong player after Tata Motors and Ashok Leyland. We expect demand to be sluggish in this segment in FY18 because of price increase due to BS-IV transition, Monsoon and GST implementation. Higher depreciation due to capacity addition in FY18 and FY19 will also add pressure to the margins. Currently the stock is trading at 8.8x FY19E P/B. Going ahead lower PAT growth compared to previous years gives us limited cushion on the valuation front. Hence we change our rating from 'Hold' to 'Neutral' with the target price of Rs.28009.

Financials Snap Shot

Income Statement

Rs in Crores

Y/E March	FY16	FY17E	FY18E	FY19E
Revenue from Operation	6,173	7,033	7,819	8,799
Change (%)	*-29%*	*14%*	*8%*	*12%*
Other Operating Income				
EBITDA	*1,690*	*2,174*	*2,375*	*2,704*
Change (%)	52%	29%	9%	14%
Margin (%)	**27%**	**31%**	**30%**	**31%**
Dep & Amortization	*137*	*154*	*169*	*294*
EBIT	1,553	2,020	2,205	2,410
Interest & other finance cost	*2*	*4*	*4*	*4*
Other Income	178	227	273	351
EBT	1,729	2,244	2,475	2,757
Exceptional Item				
Tax	539	720	785	875
Minority Int & P/L share of Ass.	148	143	143	143
Reported PAT	*1,338*	*1,667*	*1,833*	*2,026*
Adjusted PAT	**1,338**	**1,667**	**1,833**	**2,026**
Change (%)	*117%*	*25%*	*10%*	*11%*
Margin(%)	22%	24%	23%	23%

Key Ratios

Y/E March	FY16	FY17E	FY18E	FY19E
ROE	37%	31%	27%	24%
ROCE	43%	38%	32%	28%
Asset Turnover	1.2	1.0	0.9	0.8
Debtor Days	1.9	2.6	2.6	2.6
Inventory Days	18.2	17.4	17.4	17.4
Payable Days	42.8	43.2	43.2	43.2
Interest Coverage	733	567	571	649
P/E	38.9	40.7	40.0	36.2
Price / Book Value	14.2	12.7	10.7	8.6
EV/EBITDA	*30.8*	*31.2*	*30.8*	*27.1*
FCF per Share	217.7	6.2	18.4	20.8
Dividend Yield	0.5%	0.4%	0.4%	0.4%

Assumptions

Y/E March	FY16	FY17E	FY18E	FY19E
Volume ('000)	6,00,946	6,66,490	7,38,122	8,22,423
Volume Growth	99%	11%	11%	11%
Realization(Rs./vehicle)	1,02,954	1,05,526	1,05,935	1,06,994
Realization Growth	3%	2%	0%	1%
Capex(Rs crore)	977	223	800	500

Balance Sheet

Rs in Crores

Y/E March	FY16	FY17E	FY18E	FY19E
Share Capital	27	27	27	27
Reserves	3,626	5,318	6,824	8,524
Networth	**3,653**	**5,345**	**6,852**	**8,551**
Debt	*22.57*	*44.4*	*44.4*	*44.4*
Other Non Current Liab	81	144	148	153
Total Capital Employed	*3,653*	*5,345*	*6,852*	*8,551*
Net Fixed Assets (incl CWIP)	*884*	*1,242*	*1,883*	*2,100*
Non Current Investments	*2,801*	*4,104*	*4,800*	*6,078*
Other Non Current Assets	*141*	*232*	*232*	*232*
Non Current Assets	**3,890**	**5,610**	**6,947**	**8,442**
Inventory	308	336	373	420
Debtors	*33*	*50*	*56*	*63*
Cash & Bank	49	25	58	65
Other Current Assets	**63**	**77**	**86**	**97**
Current Assets	1,049	*1,381*	*1,745*	*2,252*
Creditors	723	833	926	1,042
Provisions	26	*33*	*36*	*41*
Other Current Liabilities	350	430	478	538
Curr Liabilities	1,182	1,457	1,602	1,782
Net Current Assets	**(134)**	**(76)**	**143**	**470**
Total Assets	*4,939*	*6,991*	*8,692*	*10,694*

Cash Flow Statement

Rs in Crores

Y/E March	FY16	FY17E	FY18E	FY19E
PBT	2,099	2,244	2,473	2,749
(inc)/Dec in Working Capital	2,460	2,587	2,789	3,191
Non Cash Op Exp	452	154	169	294
Interest Paid (+)	9	4	4	4
Tax Paid	(634)	(720)	(785)	(872)
others				
CF from Op. Activities	**2,282**	**2,404**	**2,101**	**2,439**
(inc)/Dec in FA & CWIP	*(1,070)*	*(512)*	*(810)*	*(510)*
Free Cashflow	*1,212*	*1,891*	*1,291*	*1,929*
(Pur)/Sale of Investment	207	(301)	(231)	(314)
others	(869)	(1,303)	(696)	(1,278)
CF from Inv. Activities	**(1,481)**	**(2,116)**	**(1,738)**	**(2,102)**
inc/(dec) in NW	1,137	1,692	1,505	1,694
inc/(dec) in Debt	28	22	-	-
Interest Paid	(9)	(4)	(4)	(4)
Dividend Paid (inc tax)	**(586)**	**(327)**	**(327)**	**(327)**
others	5	-	-	-
CF from Fin. Activities	(563)	(307)	(330)	(330)
Inc(Dec) in Cash	238	(19)	33	7
Add: Opening Balance	**353**	**36**	**17**	**50**
Closing Balance	591	17	50	57