

# Eicher Motors

15 June 2020

Reuters: EICH.NS; Bloomberg: EIM IN

## Product / Network focus can be growth enabler in challenging times

Eicher Motors reported 4QFY20 standalone PAT at Rs3.46bn, down by ~28% YoY mainly on account of lower EBITDA margin and higher depreciation, partially offset by lower tax rate. PAT was ~23% below our estimate. Effective tax rate for the quarter was 29.2%. Revenue stood at Rs21.8bn, down 12.8% YoY due to a 17% decline in volume. ASP improved by 6.0% YoY as 2/3<sup>rd</sup> of the volume for the quarter comprised BS-VI models. EBITDA margin for the quarter stood at 23.1%, down 470bps YoY and 210bps QoQ on account of negative operating leverage, change in mix towards BS-VI models (relatively lower margins) and higher ESOP expenses. Volatility in forex and one-off provision for the recall of 650 Twins and Himalayan in US and Europe (to fix brake calliper) had an impact of Rs500mn (shown as an exceptional item). In April, RE took a price increase of Rs3,000 (at customer level; pass-through to RE will be lower) to pass on some of BS-VI costs. The company opened 100 studio stores during the quarter, taking its total count to ~600 stores. It intends to keep expanding the studio format as it sees potential in the rural and semi urban markets, which are currently doing well as they are less impacted by Covid-19. Since the easing of the lockdown, RE is seeing strong initial customer interest and its order book has reached pre-covid level. It offered consumer schemes for limited 10-12 days in May which ended in June and hasn't seen a decline in demand even since. However, the management stated that it will be difficult to predict the volume trajectory as the supply ramp up has been slower and it is operating at ~40% capacity utilization currently. All BS-IV inventories were sold off well ahead of time. Current channel inventory remains very low. RE's new platform launch has been delayed to 2QFY21 and has lined up practically a new product each quarter for the next 2-3 years, which will be in its current mid-segment category. Consolidated PAT declined by 44.2% YoY mainly due to its share of loss from VECV at Rs140.1mn. VECV revenue declined by 35% YoY to Rs2.1bn and its EBITDA margin declined by 670bps YoY to 1.8% due to negative operating leverage. We believe that RE's focus on network expansion and improving product accessibility can be a long-term growth enabler, especially in a challenging environment. Margins are likely to be affected in the medium term due to limited BS-VI pass-through and negative operating leverage. We expect volume, revenue and PAT to grow at a CAGR of 5.1%, 13.6% and 15.8%, respectively over FY20-22E. We expect margin to recover in FY22. We maintain BUY with a reduced target price of Rs19,377. Our target price is based on SOTP, valuing it at ~21 times Mar 2022 consolidated EPS.

**Focus on network expansion & improving accessibility are long term positives:** RE has over 600 studio stores in tier 2 & 3 towns and plans to expand it further. Studio stores have low cost operating model and have lower breakeven point. Expected recovery in the rural economy will support demand from studio stores. We expect this to boost the spares and services revenue as well. The company is also focusing on improving accessibility by way of strip down variants, new color options and has a long new launch pipeline, thereby giving customers more choices.

**Exports momentum to continue:** 650 Twins has been very well received internationally. Given the opportunity size, EML is looking to expand the distribution reach internationally which will continue to drive the volume momentum depending on the revival in export markets.

**Margins likely to be under pressure in the medium term:** On blended basis, RE has almost passed on the entire BS-VI cost so as to maintain absolute gross margin per vehicle. Thus, margins are likely to take a hit in the medium term due to limited future price hikes and negative operating leverage owing to challenging demand environment.

Y/E March (Rsmn)	4QFY19	3QFY20	4QFY20	YoY (%)	QoQ (%)	FY19	FY20	YoY (%)
Net sales	24,996	23,635	21,795	(12.8)	(7.8)	97,945	90,775	(7.3)
COGS	13,382	12,926	12,310	(8.0)	(4.8)	50,628	49,858	(1.5)
% of sales	53.5	54.7	56.5	2.9	1.8	51.7	54.9	3.2
Gross margin %	46.5	45.3	43.5	(300bps)	(180bps)	48.3	45.1	(320bps)
Employee costs	1,645	1,776	2,051	24.7	15.5	6,795	7,651	12.6
% of sales	6.6	7.5	9.4	2.8	1.9	6.9	8.4	1.5
Other expenses	3,027	2,981	2,402	(20.7)	(19.4)	11,078	10,728	(3.2)
% of sales	12.1	12.6	11.0	(1.1)	(1.6)	11.3	11.8	0.5
EBITDA	6,942	5,952	5,033	(27.5)	(15.5)	29,444	22,538	(23.5)
EBITDA margin %	27.8	25.2	23.1	(470bps)	(210bps)	30.1	24.8	(520bps)
Depreciation	808	942	1,079	33.6	14.5	2,989	3,779	26.4
Interest expenses	8	27	25	208.8	(9.2)	30	109	263.2
Other income	1,422	1,358	1,462	2.8	7.6	5,080	6,153	21.1
Exceptional items	-	-	500	-	-	175	500	-
PBT	7,549	6,341	4,891	(35.2)	(22.9)	31,330	24,303	(22.4)
Tax	2,744	1,452	1,429	(47.9)	(1.6)	10,785	5,265	(51.2)
Effective tax rate %	36.4	22.9	29.2	-	-	34.4	21.7	-
Reported PAT	4,804	4,889	3,462	(27.9)	(29.2)	20,544	19,038	(7.3)
Adj PAT	4,804	4,889	3,962	(17.5)	(19.0)	20,720	19,538	(5.7)
Adj PAT margin %	19.2	20.7	18.2	(100bps)	(250bps)	21.0	21.0	-
EPS	176.2	179.1	145.1	(17.7)	(19.0)	760.1	716.0	(5.8)

Source: Company, Nirmal Bang Institutional Equities Research

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## BUY

Sector: Automobiles

CMP: Rs16,825

Target Price: Rs19,377

Upside: 15%

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## Key Data

Current Shares O/S (mn)	27.3
Mkt Cap (Rsbn/US\$bn)	460.3/6.1
52 Wk H / L (Rs)	23,450/12,450
Daily Vol. (3M NSE Avg.)	260,520

## Price Performance (%)

	1 M	6 M	1 Yr
Eicher Motors	20.1	(23.5)	(14.7)
Nifty Index	9.2	(17.5)	(15.7)

Source: Bloomberg

**Exhibit 1: Key financials - Standalone**

Y/E March (Rsmn)	FY18	FY19	FY20	FY21E	FY22E
RE volume (units)	820,493	826,098	697,582	592,945	770,828
YoY growth (%)	23.1	0.7	(15.6)	(15.0)	30.0
Net sales	89,575	97,945	90,775	87,347	117,169
YoY growth (%)	27.3	9.3	(7.3)	(3.8)	34.1
EBITDA	28,532	29,444	22,538	20,134	29,585
EBITDA margin (%)	31.9	30.1	24.8	23.1	25.3
Adjusted PAT	20,249	20,720	19,538	17,512	25,534
EPS	742.8	760.1	715.7	641.5	935.3
YoY change (%)	29.6	2.3	(5.8)	(10.4)	45.8
RoCE (%)	52.9	42.2	28.9	23.4	28.1
RoE (%)	37.7	29.1	23.6	18.1	21.6
P/E (x)	22.7	22.1	23.5	26.2	18.0
EV/Sales (x)	4.6	4.1	4.3	4.4	3.1
EV/EBITDA (x)	14.3	13.6	17.4	18.8	12.0

Source: Company, Nirmal Bang Institutional Equities Research

**Exhibit 2: SOTP valuation**

(Rs)	March 2022E
Royal Enfield's EPS (Rs/share)	903.5
P/E (x)	21
<b>Royal Enfield- standalone</b>	<b>18,973</b>
<b>EICHER MOTORS' STAKE IN VECV</b>	
EPS @ 54.4% stake (Rs/share)	40.4
P/E (x)	10
<b>VECV's share</b>	<b>404</b>
<b>Total</b>	<b>19,377</b>

Source: Nirmal Bang Institutional Equities Research

**Exhibit 3: Change in our estimates**

Y/E March (Rsmn)	New estimate		Old estimate		Change (%)	
	FY21E	FY22E	FY21E	FY22E	FY21E	FY22E
Volume	592,945	770,828	744,314	818,746	(20.3)	(5.9)
Net sales	87,347	117,169	107,197	125,054	(18.5)	(6.3)
EBITDA	20,134	29,585	26,317	31,326	(23.5)	(5.6)
EBITDA margin (%)	23.1	25.3	24.6	25.1	(150bps)	20bps
PAT	17,512	25,534	22,190	26,763	(21.1)	(4.6)

Source: Company, Nirmal Bang Institutional Equities Research

**Exhibit 4: Deviation of our estimates from actual performance in 4QFY20**

(Rsmn)	Actual	Our estimate	Deviation
	4QFY20	4QFY20	(%)
Net sales	21,795	22,028	(1.1)
EBITDA	5,033	5,221	(3.6)
EBITDA (%)	23.1	23.7	(60bps)
Adj PAT	3,962	4,517	(12.3)

Source: Nirmal Bang Institutional Equities Research

## Key takeaways from post-result conference call

**Covid-19 update:** RE closed its plants from 23<sup>rd</sup> March. The company supported dealers by advancing all dealer payments and all outstanding claims while dealer incentives were paid off. The company offered extended free service to customers. The company has pledged Rs500mn for providing food, sanitization etc amid the Covid-19 outbreak. The company resumed operations from 6<sup>th</sup> May onwards and is ramping up production in a phased manner. Current capacity utilization stands at ~40%. ~90% of its retail network is now operational and as the lockdown is easing out, RE is seeing strong initial customer interest and confidence.

**Outlook on RE** – As per the management, since the easing out of lockdown, RE is seeing strong initial customer interest. RE's bookings have reached pre-covid level. Northern and central India is back on track whereas western India is lagging behind in terms of demand. Demand hasn't seen a decline even after the expiry of consumer schemes offered for limited 10-12 days in May and ended in June. Thus, overall demand remains reasonably good. However, the management stated that it would be difficult to forecast volume as it is facing supply side challenges which might take some time to pick up. **VECV** - CV industry witnessed volume decline of 40% in FY20. Industry was already facing slowdown due to weak economy, axle load norm changes, driver availability issues etc. Expectation of pre-buying demand before BS-VI transition did not materialize. Covid-19 pandemic has further worsened the situation and the management expects slower recovery at the industry level.

**Margin:** EBITDA margin declined by 470bps YoY and 210bps QoQ on account of negative operating leverage, change in mix towards BS-VI models (which have relatively lower margins) and higher ESOP expenses. Volatility in forex and one-off provision towards recall of 650 Twins and Himalayan in US and Europe (for fixing brake caliper) also affected margins (impact of Rs500mn shown as an exceptional item). Employee expense for the quarter was higher even though the employee count reduced mainly due to ESOP related expenses. The effect of reduction in headcount will be reflected from 1QFY21. RE will try to maintain absolute gross margin per vehicle under BS-VI, as it has passed on majority of BS-VI costs. This will affect margins in the medium term. In April, RE took a price increase of Rs3,000 (at customer level)

**BS-VI: RE** – RE was among the first companies to completely sell all its BS-IV inventory well ahead of timeline, which helped it in seamless transition to BS-VI. About 2/3<sup>rd</sup> of the retail sales during the quarter comprised BS-VI models. BS-VI products have been very well received with great customer feedback. **VECV** – During the quarter, the entire range of products from 4.9T to 59T were moved to new BS-VI platform in time and BS-IV inventory was managed optimally. The management believes that VECV is distinctively positioned to offer comprehensive BS-VI platforms that enhance customers' productivity, efficiency and profitability, thus giving VECV an edge in the industry.

**Inventory: RE** – All BS-IV inventory was sold off well ahead of time. Current channel inventory remains very low. RE is currently witnessing supply side challenges and expects gradual ramp up in production. Order book has reached pre-covid level but it is currently operating at ~40% capacity due to supply constraints.

**Studio stores:** Over 100 studio stores were added during the quarter, taking total studio store count to ~600 as on March end. The management stated that it is seeing good traction in sales from studio stores as these stores are outside city area where the covid-19 situation is much better. RE intends to continue the studio store expansion as operating cost of these stores is 1/10<sup>th</sup> of a normal store. These stores will create better accessibility and will be a growth enabler even during slowdown.

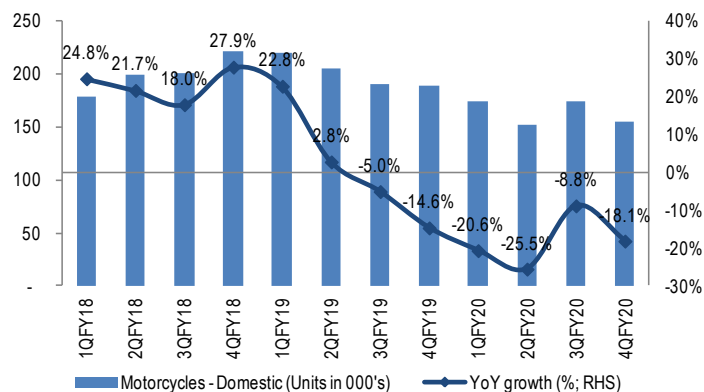
**Exports:** RE had the best ever export performance with ~89% increase in FY20. During the year, it added 35 exclusive stores in the international market, taking its exclusive store count to 77 stores spread across 21 countries. It opened new stores in its existing markets like Thailand and Brazil and entered new markets like Korea, Italy and Belgium.

**New/Upcoming launches: RE** – 1<sup>st</sup> launch from the new platform has been delayed due to Covid-19. The launch now will be in 2QFY21. The management stated that practically there will be a new launch every quarter going forward for the next 3 years. Though the management refrained from sharing any product details, it stated that even though it aspires to be a global player, future products will be relevant to the domestic market as well. It intends to remain in its current midsize category as it believes that motorcycle riders in India are upgrading to the midsize category and shifting towards motorcycles that are beyond just pure commuting.

**Capex:** All the major expansion related capex has been completed in FY20. For FY21, majority of the capex will be on the new platform and product development side. Thus, FY21 capex is expected to be similar to FY20. The management indicated that capex will reduce by about 25% from FY22 onwards.

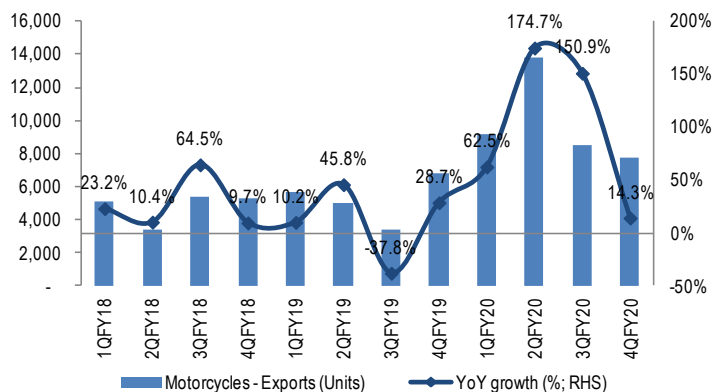
## Story in Charts

**Exhibit 5: RE - Motorcycle – Domestic volume trend**



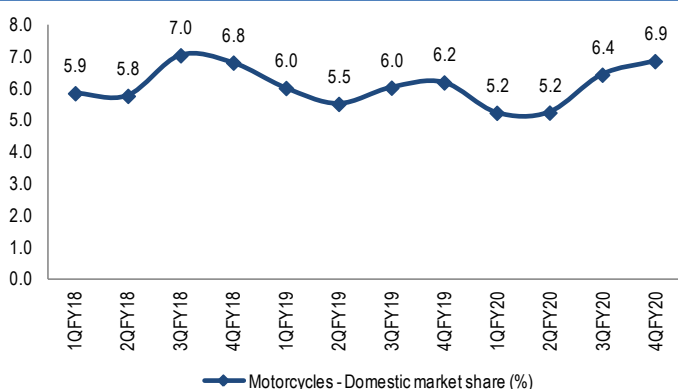
Source: Company, Nirmal Bang Institutional Equities Research

**Exhibit 6: RE - Motorcycle – Exports volume trend**



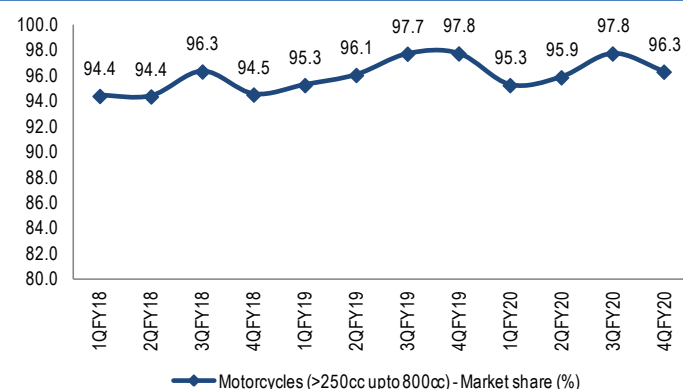
Source: Company, Nirmal Bang Institutional Equities Research

**Exhibit 7: Motorcycles – Domestic market share (%)**



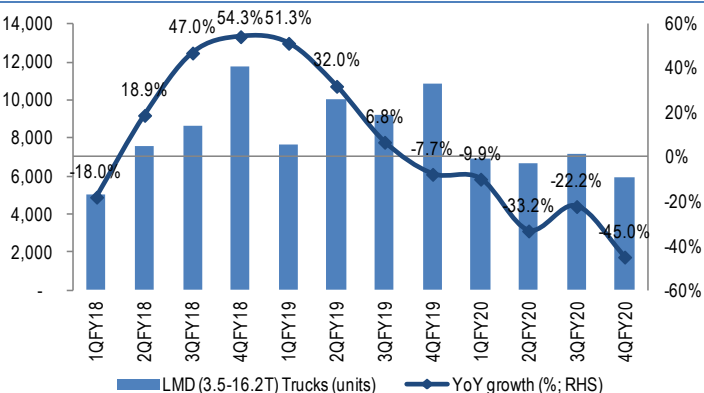
Source: Company, Nirmal Bang Institutional Equities Research

**Exhibit 8: RE-Domestic motorcycle (>250-800cc) market share**



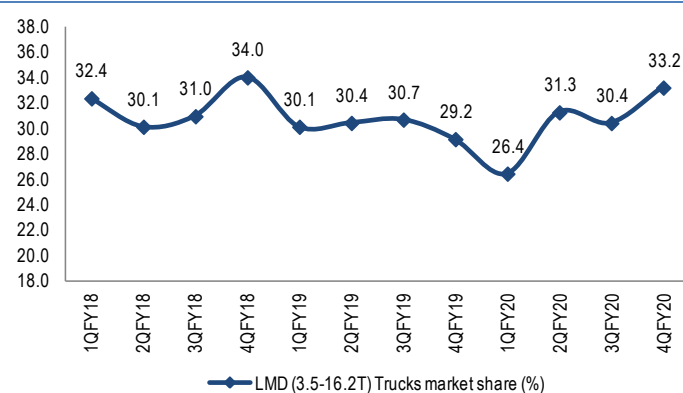
Source: CRISIL, Nirmal Bang Institutional Equities Research

**Exhibit 9: VECV: LMD – Domestic volume trend**

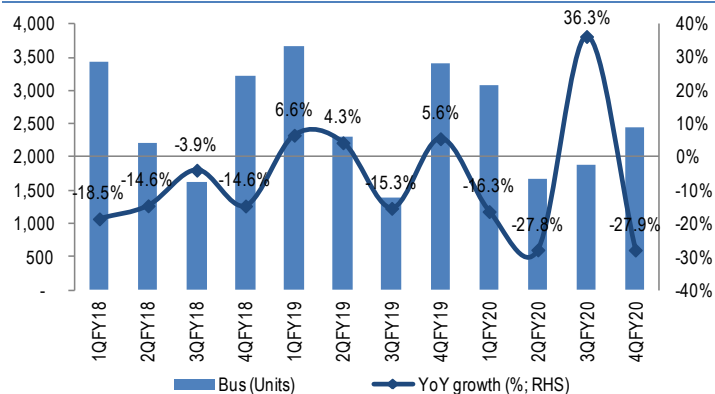


Source: CRISIL, Nirmal Bang Institutional Equities Research

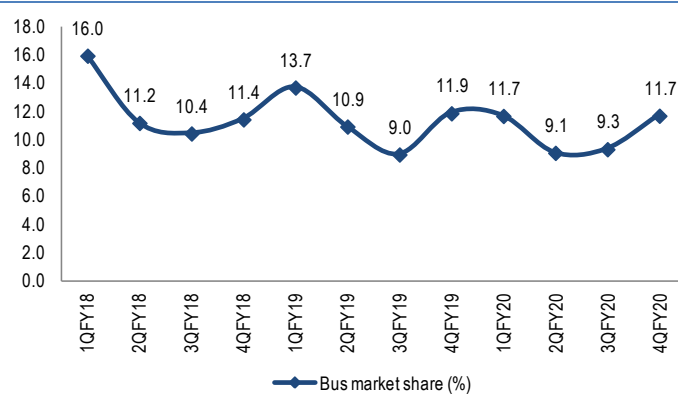
**Exhibit 10: VECV: LMD – Domestic market share (%)**



Source: CRISIL, Nirmal Bang Institutional Equities Research

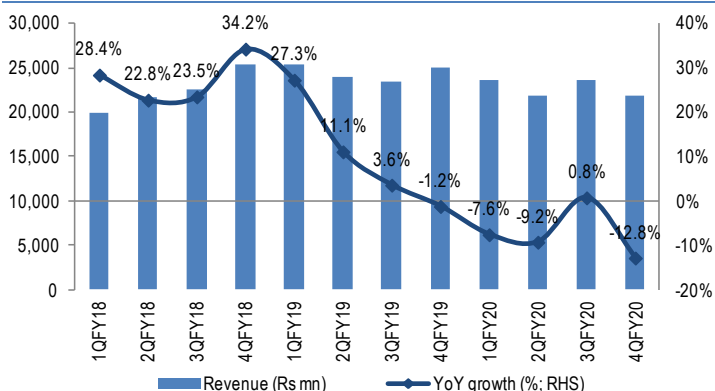
**Exhibit 11: VECV: Bus – Domestic volume trend**


Source: Company, Nirmal Bang Institutional Equities Research

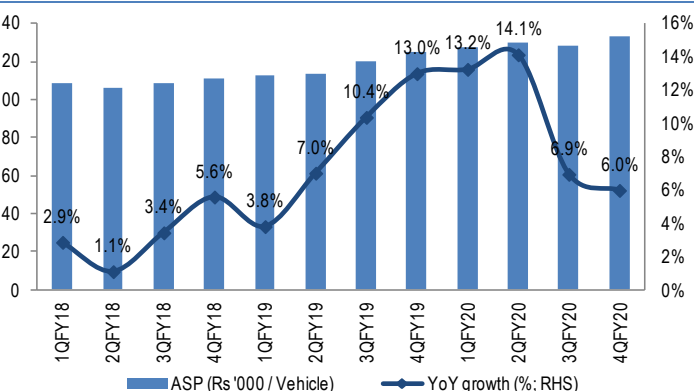
**Exhibit 12: VECV: Bus – Domestic market share (%)**


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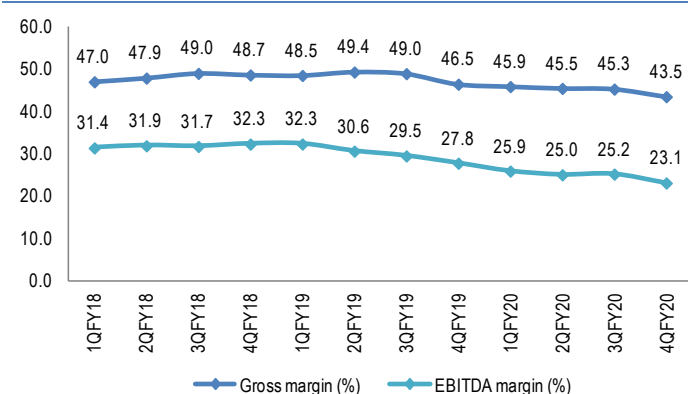
Source: CRISIL, Nirmal Bang Institutional Equities Research

**Exhibit 13: Revenue & YoY growth (%)**


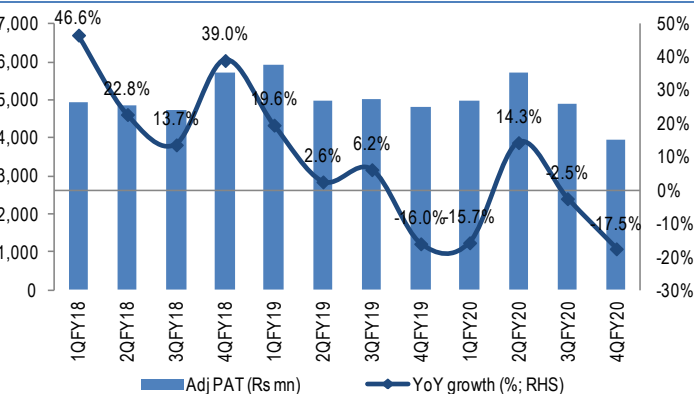
Source: Company, Nirmal Bang Institutional Equities Research

**Exhibit 14: Avg selling price (ASP) & YoY growth (%)**


Source: Company, Nirmal Bang Institutional Equities Research

**Exhibit 15: Gross margin & EBITDA margin trend**


Source: Company, Nirmal Bang Institutional Equities Research

**Exhibit 16: Adj PAT & YoY growth (%)**


Source: Company, Nirmal Bang Institutional Equities Research

**Exhibit 17: One-year forward P/E chart**



Source: Bloomberg, Nirmal Bang Institutional Equities Research



## Financials (Consolidated)

### Exhibit 18: Income statement

Y/E March (Rsmn)	FY18	FY19	FY20	FY21E	FY22E
<b>Net Sales</b>	<b>89,649</b>	<b>97,971</b>	<b>91,536</b>	<b>87,996</b>	<b>117,818</b>
<b>% Growth</b>	<b>27.5</b>	<b>9.3</b>	<b>(6.6)</b>	<b>(3.9)</b>	<b>33.9</b>
Raw material	46,435	50,574	49,959	48,303	64,560
Staff costs	5,737	7,024	7,958	7,425	9,608
Other expenses	9,402	11,341	11,815	13,016	15,122
Total expenses	61,573	68,940	69,732	68,743	89,290
<b>EBITDA</b>	<b>28,076</b>	<b>29,031</b>	<b>21,804</b>	<b>19,252</b>	<b>28,528</b>
<b>% Growth</b>	<b>29.1</b>	<b>3.4</b>	<b>(24.9)</b>	<b>(11.7)</b>	<b>48.2</b>
<b>EBITDA margin (%)</b>	<b>31.3</b>	<b>29.6</b>	<b>23.8</b>	<b>21.9</b>	<b>24.2</b>
Other income	2,801	4,434	5,433	6,682	8,219
Interest costs	53	73	189	217	250
Depreciation	2,233	3,003	3,815	4,346	4,998
Profit before tax (before x/o)	28,591	30,389	23,232	21,371	31,499
Exceptional items	2,201	175	500	0	0
Share of profit/(loss) of JV	2,561	2,584	317	472	1,303
Tax	9,359	10,770	5,275	5,343	7,875
<b>Adj PAT</b>	<b>21,792</b>	<b>22,203</b>	<b>18,274</b>	<b>16,500</b>	<b>24,927</b>
<b>% Growth</b>	<b>30.7</b>	<b>1.9</b>	<b>(17.7)</b>	<b>(9.7)</b>	<b>51.1</b>
<b>Adj PAT margin (%)</b>	<b>24.3</b>	<b>22.7</b>	<b>20.0</b>	<b>18.8</b>	<b>21.2</b>
EPS (Rs)	799.4	814.5	669.4	604.4	913.1
<b>% Growth</b>	<b>30.2</b>	<b>1.9</b>	<b>(17.8)</b>	<b>(9.7)</b>	<b>51.1</b>
DPS (Rs)	110.0	125.0	125.0	100.0	125.0
Payout (incl. div. tax) (%)	16.6	18.5	22.5	20.0	16.5

Source: Company, Nirmal Bang Institutional Equities Research

### Exhibit 20: Balance sheet

Y/E March (Rsmn)	FY18	FY19	FY20	FY21E	FY22E
Share capital	273	273	273	273	273
Reserves	70,028	88,914	99,536	112,744	133,556
Net worth	70,301	89,187	99,809	113,017	133,829
Total debt	1,508	1,868	2,490	2,490	2,490
Net deferred tax liability	1,421	2,739	2,522	2,522	2,522
<b>Capital employed</b>	<b>73,230</b>	<b>93,794</b>	<b>104,821</b>	<b>118,029</b>	<b>138,840</b>
Gross block	21,443	27,673	36,518	42,518	47,518
Depreciation	6,426	8,927	12,743	17,089	22,087
Net block	15,017	18,746	23,775	25,429	25,431
Capital work-in-progress	3,332	4,497	3,122	3,122	3,122
Investments	55,808	49,225	57,488	67,488	77,488
Inventories	3,946	6,334	5,724	5,512	7,385
Debtors	680	903	868	835	1,119
Cash	12,120	29,653	29,506	31,084	43,259
Loans & advances	7	13	1	26	51
Other current assets	4,311	4,497	4,014	4,514	5,014
Total current assets	21,064	41,400	40,113	41,971	56,829
Creditors	11,719	12,341	10,277	9,896	13,260
Other current liabilities & provisions	10,274	7,734	9,400	10,085	10,770
Total current liabilities	21,992	20,075	19,676	19,981	24,030
Net current assets	(928)	21,325	20,436	21,990	32,800
<b>Application of funds</b>	<b>73,230</b>	<b>93,794</b>	<b>104,821</b>	<b>118,029</b>	<b>138,840</b>

Source: Company, Nirmal Bang Institutional Equities Research

### Exhibit 19: Cash flow

Y/E March (Rsmn)	FY18	FY19	FY20	FY21E	FY22E
OP/(loss) before tax	25,843	26,028	17,988	14,906	23,530
Depreciation & amortization	2,233	3,003	3,815	4,346	4,998
Other income	2,801	4,434	5,433	6,682	8,219
(Inc.)/dec. in working capital	5,133	(4,720)	742	24	1,366
Direct taxes paid	(8,716)	(9,452)	(5,492)	(5,343)	(7,875)
Other/extra-ordinary Items	1,233	3,378	(3,220)	472	1,303
<b>Cash flow from operations (after E/O)</b>	<b>28,527</b>	<b>22,670</b>	<b>19,266</b>	<b>21,087</b>	<b>31,541</b>
Capital expenditure (-)	(8,117)	(7,897)	(7,469)	(6,000)	(5,000)
<b>Net cash after capex</b>	<b>20,411</b>	<b>14,773</b>	<b>11,797</b>	<b>15,087</b>	<b>26,541</b>
Other investing activities	(5,937)	6,583	(8,262)	(10,000)	(10,000)
Dividends paid (-)	(3,616)	(4,109)	(4,115)	(3,292)	(4,115)
Inc./(dec.) in total borrowings	1,011	286	434	(217)	(250)
Others	1	-	0	-	-
<b>Cash from financial activities</b>	<b>(2,604)</b>	<b>(3,824)</b>	<b>(3,681)</b>	<b>(3,510)</b>	<b>(4,365)</b>
Opening cash balance	251	12,120	29,653	29,506	31,084
Closing cash balance	12,120	29,653	29,506	31,084	43,259
Change in cash balance	11,869	17,533	(147)	1,578	12,176

Source: Company, Nirmal Bang Institutional Equities Research

### Exhibit 21: Key ratios

Y/E March	FY18	FY19	FY20	FY21E	FY22E
<b>Per share (Rs)</b>					
EPS	799.4	814.5	669.4	604.4	913.1
EPS Growth (%)	30.2	1.9	(17.8)	(9.7)	51.1
Cash EPS	706.7	823.4	779.2	746.3	1,048.4
Book value per share	2,578.9	3,271.7	3,656.0	4,139.8	4,902.1
DPS	110.0	125.0	125.0	100.0	125.0
Payout (incl. div. tax) %	16.6	18.5	22.5	20.0	16.5
<b>Valuation (x)</b>					
P/E	21.0	20.7	25.2	27.9	18.4
Cash P/E	23.8	20.5	21.6	22.6	16.1
EV/EBITDA	14.0	13.2	17.2	18.9	12.0
EV/Sales	4.4	3.9	4.1	4.2	2.9
P/BV	6.5	5.1	4.6	4.1	3.4
Dividend yield (%)	0.7	0.7	0.7	0.6	0.7
<b>Return ratios (%)</b>					
RoCE	39.1	32.5	22.3	18.3	22.9
RoE	31.0	24.9	18.3	14.6	18.6
<b>Profitability ratios (%)</b>					
EBITDA margin	31.3	29.6	23.8	21.9	24.2
PAT margin	24.3	22.7	20.0	18.8	21.2
<b>Turnover ratios</b>					
Debtors (days)	3	3	3	3	3
Inventory (days)	16	24	23	23	23
Creditors (days)	48	46	41	41	41
Asset turnover (x)	1.2	1.0	0.9	0.7	0.8
<b>Leverage Ratio</b>					
Debt/equity (x)	0.0	0.0	0.0	0.0	0.0

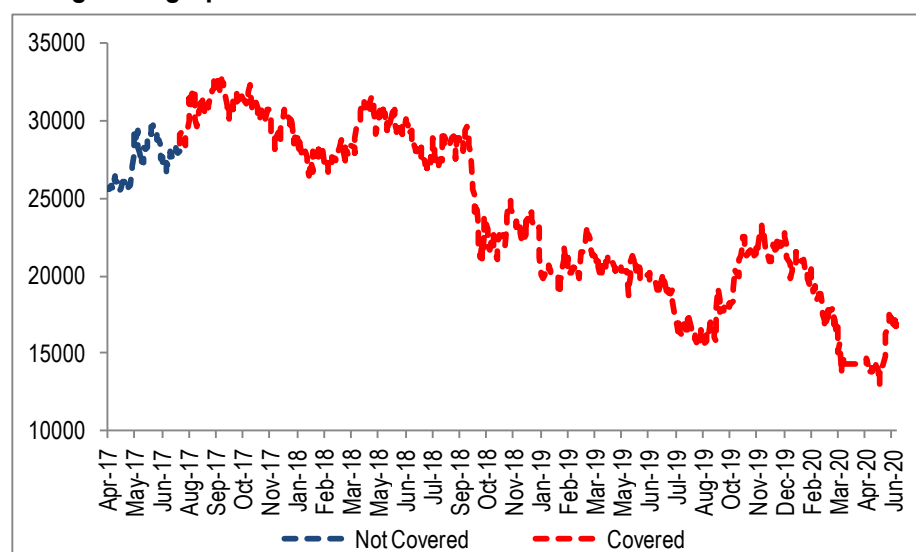
Source: Company, Nirmal Bang Institutional Equities Research

## Rating track

Date	Rating	Market price (Rs)	Target price (Rs)
18 July 2017	Buy	28,059	32,566
10 August 2017	Accumulate	31,440	33,462
15 November 2017	Buy	30,090	35,375
8 February 2018	Buy	28,010	36,271
10 May 2018	Buy	30,316	36,529
10 August 2018	Buy	27,439	36,529
13 November 2018	Buy	21,934	29,402
1 August 2019*	Under Review	16,240	N.A
9 October 2019	Buy	18,212	21,127
11 November 2019	Buy	21,640	24,843
07 February 2020	Buy	20,530	23,896
30 March 2020	Buy	14,360	20,372
15 June 2020	Buy	16,825	19,377

\* Coverage shifted to Anish Rankawat wef 1 August 2019

## Rating track graph





## DISCLOSURES

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### Stock Ratings Absolute Returns

BUY > 15%

ACCUMULATE -5% to 15%

SELL < -5%

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