

Tax rate booster supports muted volume trajectory...

Eicher Motors reported a muted Q2FY20 performance. Consolidated sales for Q2FY20 were at ₹ 2,192 crore (down 9.0% YoY). ASPs for Royal Enfield (RE) in Q2FY20 were at ₹ 1.30 lakh/unit, up 2% QoQ while sales volumes were at 1.66 lakh units, down 20.7% YoY. EBITDA came in at ₹ 541 crore with corresponding EBITDA margins at 24.7%, down 110 bps QoQ. Consequent consolidated PAT was at ₹ 573 crore, up 4.4% YoY. Higher PAT was supported by lower effective tax rate, which was at 4.7% for the quarter against the usual run rate of 33%+.

October volumes promising, growth still mirage in FY19-21E

EML has been battling sharp 2-W volume challenges domestically over the last several quarters. RE volumes remained flattish YoY at 8.3 lakh units in FY19, with H1FY20 volumes falling 20%+ YoY to ~3.5 lakh units. EML, however, managed to post positive YoY dispatches in October 2019, after a gap of almost 11 months (double digit volume decline). It was largely led by encouraging response received for the company to its 650 cc twins in the international market. We expect the positive momentum to continue over the rest of FY20E & FY21E. However, this will be unable to compensate for the decline seen in H1FY20 with EML expected to post a volume decline of ~7% YoY in FY20E to 7.7 lakh units, well short of its production guidance of 9.5 lakh units. Given speed-breaker in terms of substantial price hike due to BS-VI transition in April 2020, we expect sales volume at RE to revive steadily by 6.4% YoY to 8.2 lakh units in FY21E (-1% volume CAGR over FY19-21E).

Excess system capacity, slowdown take toll on VE-CV

The domestic M&HCV segment has been the most impacted during the ongoing auto downturn, with Q2FY20 being particularly difficult. With the industry suffering from the perfect storm of structural (overcapacity caused by revised axle load norms, shorter turnaround times under GST) and cyclical (slowing economic activity, NBFC-led liquidity crunch) issues, a meaningful recovery appears to be far in the distance. We anticipate EML's CV JV i.e. VECV will remain a pain point, with expected volume CAGR of negative 5.8% in FY19-21E and upcoming BS-VI transition along with steep price discounts seen magnifying impact on profitability.

Valuation & Outlook

EML is receiving an encouraging response to its studio format stores (~500 as of October 2019 end) in semi-urban areas. This coupled with momentum seen in export markets is expected to lift RE sales volume, going forward. Building in positives, we expect sales, PAT to grow 11.1%, 11.7%, CAGR, respectively, in FY19-21E. We value EML at ₹ 22,215 on SOTP basis, valuing RE business at 22x P/E and VE-CV business at 14x P/E on FY21E numbers.



Particulars

Particular	₹ crore
Market Capitalization	59,154.2
Total Debt (FY19)	186.8
Cash & Investments (FY19)	5,943.8
EV (FY19) (₹ crore)	53,397.2
52 week H/L (₹)	25300 / 15197
Equity capital	₹ 27.3 Crore
Face value	₹ 10

Key Highlights

- RE volumes for the quarter i.e. Q2FY20 were down 20.7% YoY. The mix, however, improved in favour of high cc segment bikes, thereby improving ASPs by 2% QoQ
- Margins came in at a new recent low of 24.7%, down 110 bps QoQ tracking limited savings in raw material as well as other expenses
- Customer response to BS-VI transition as well as further ramp up of studio format stores - key monitorable
- Maintain HOLD with revised target price of ₹ 22,215 using SOTP valuation methodology

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Key Financial Summary

Key Financials	FY17	FY18	FY19	FY20E	FY21E	CAGR (FY19-21E)
Net Sales	7,033.4	8,965.0	9,797.1	10,244.2	12,086.5	11.1%
EBITDA	2,174.0	2,807.6	2,903.1	2,682.5	3,267.0	6.1%
EBITDA Margins (%)	30.9	31.3	29.6	26.2	27.0	
Net Profit	1,667.1	1,959.7	2,202.8	2,312.3	2,746.2	11.7%
EPS (₹)	612.7	718.9	808.1	848.2	1,007.4	
P/E	35.4	30.2	26.9	25.6	21.5	
RoNW (%)	31.8	29.9	24.8	21.5	21.1	
RoCE(%)	40.6	39.1	32.5	25.7	26.5	

Source: ICICI Direct Research, Company

Exhibit 1: Variance Analysis

	Q2FY20	Q2FY20E	Q2FY19	YoY (%)	Q1FY20	QoQ (%)	Comments
Total Operating Income	2192	2113	2408	-9.0	2382	-8.0	Topline ahead of our estimates tracking beat on ASPs due to better product mix
Raw Material Expenses	1122	1088	1164	-3.6	1231	-8.9	
Purchase of traded goods	63	42	55	14.0	46	36.0	RM costs came in higher as the company did not realise any meaningful cost saving on account of benign commodity prices
Employee Expenses	186	189	176	5.7	212	-12.1	
Other expenses	280	262	284	-1.2	279	0.5	Other expenses came in higher than our estimates at 12.8% of sales
EBITDA	541	532	729	-25.8	614	-11.9	
EBITDA Margin (%)	24.7	25.2	30.3	-559 bps	25.8	-110 bps	Margins came in lower tracking higher RM costs as well as higher other expenses
Other Income	145	127	94	54.4	120	20.5	
Depreciation	90	80	72	24.5	88	2.5	
Interest	4	1	2	148.3	5	-5.4	
Total Tax	28	135	260	-89.3	212	-86.9	Tax rate for the quarter came in 4.7% of PBT
PAT	573	453	549	4.4	452	26.8	Lower effective tax rate and higher other income led to a strong beat on net profitability
Key Metrics							
Royal Enfield ASP(₹)	129,884.9	125,939.2	113,807.6	14.1	127,211.3	2.1	ASPs came in higher tracking a better product mix with higher share of 650 cc twins led by export sales
VECV ASP (₹ lakhs)	17.6	15.5	15.8	11.6	17.1	3.0	

Source: Company, ICICI Direct Research

Exhibit 2: Change in estimates

(₹ Crore)	FY20E			FY21E			Comments
	Old	New	% Change	Old	New	% Change	
Revenue	10,665	10,163	-4.7	12,146	12,003	-1.2	We broadly maintain our topline estimates for FY20E & FY21E amid a better product mix (increasing share of 650 cc twins) and lower volume estimates
EBITDA	2,954	2,683	-9.2	3,246	3,267	0.6	Lower FY20E estimates tracking muted H1FY20 performance
EBITDA Margin (%)	27.7	26.4	-131 bps	26.7	27.2	49 bps	while upgraded forward estimates as operating leverage benefits return once volume recovers in FY21E
PAT	2,503	2,312	-7.6	2,808	2,746	-2.2	
EPS (₹)	917	848	-7.6	1,029	1,007	-2.2	Lower sales & margins estimates lead to 8% decline in PAT estimates for FY20E. Broadly maintain FY21E numbers

Source: Company, ICICI Direct Research

Exhibit 3: Assumptions

	Current		Earlier		Comments		
	FY18	FY19	FY20E	FY21E			
Royal Enfield volumes	820,121	826,098	768,687	817,533	822,364	844,020	We lower our sales volume estimates of RE, tracking muted performance in YTD FY20. We estimates sales volume will decline 7% in FY20E and then recover by 6.4% in FY21E. FY19-21E CAGR at -1%
Royal Enfield ASP/unit (₹)	111,785	117,603	131,778	146,814	129,250	143,908	Increasing share of 650 cc twins to better the blended realisations over FY19-21E
VECV volumes	66,233	72,860	61,633	64,651	72,113	73,781	Lower volume estimates tracking muted performance in H1FY20 and muted demand prospects domestically

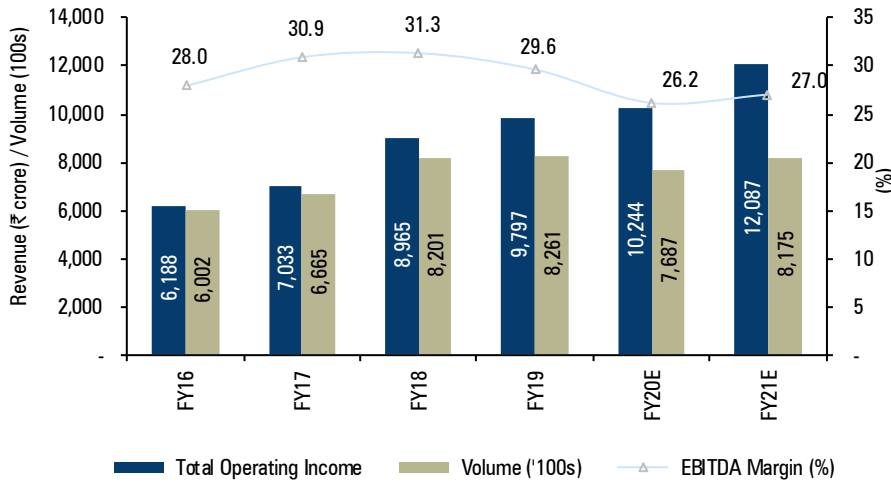
Source: Company, ICICI Direct Research

Conference Call Highlights

- The company added four large sized retail stores during the quarter, taking its total dealership count to 932 (large size format) as of September 2019 end
- EML also added 500 retail stores in the studio format and is currently selling about eight to 10 motorcycles/month from these new format stores. These stores are already operating at their breakeven levels (10 motorcycle sales/month). The company intends to further add 200-300 such stores by March end 2020
- Financing penetration in the case of RE has increased from 53% previously to ~59% as of September 2019 end
- EML is receiving a robust response to its 650 cc twins as well as the new Himalayan range
- In the festive season RE witnessed robust demand with volumes up to healthy double digits. Current inventory of RE is at <3 weeks with some stores in Delhi and Mumbai running out of stock at the end of festive season
- The company has maintained its EBITDA margin guidance of 25-28% over the medium to long term
- EML expects its spares revenue to grow double digit, going forward, and has maintained a capex guidance of ₹ 700 crore for FY20E
- The company is ready with BS-VI technology both for its RE brand as well as VECV product portfolio
- VECV net sales for the quarter were at ₹ 2004 crore, down 32% YoY. EBITDA was at ₹ 105 crore with corresponding EBITDA margins at 5.2%. PAT was at ₹ 15 crore, down 90% YoY. On the CV front, the demand situation remains challenging

Financial story in charts

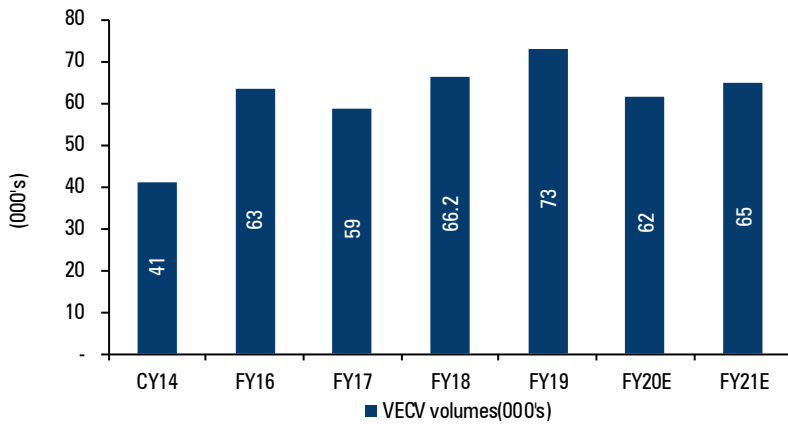
Exhibit 4: Royal Enfield growth trajectory



We expect sales to grow at a CAGR of 11.1% over FY19-21E on the back of -1% CAGR volume growth during this period and increase in ASPs primarily necessitated by regulatory cost push as well as encouraging response to 650 cc twins

Source: Company, ICICI Direct Research

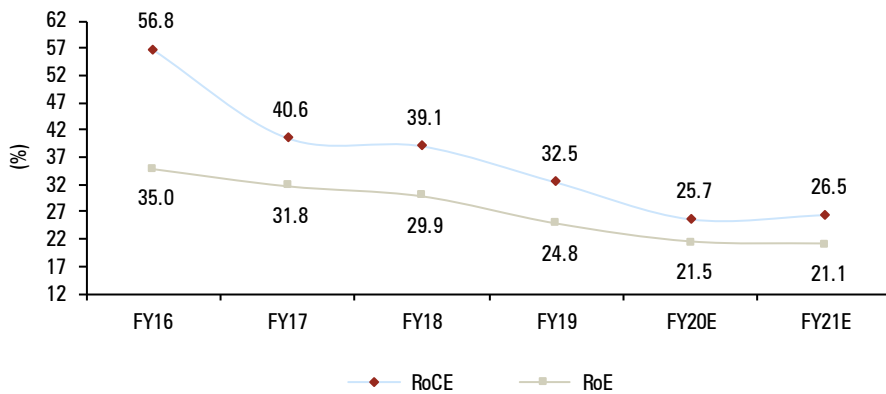
Exhibit 5: VECV volumes



We factor in negative 6% volume CAGR at VECV in FY19-21E

Source: Company, ICICI Direct Research

Exhibit 6: Return ratio profile



Eicher Motors expected to continue to clock healthy return ratios; albeit with a downward bias

Source: Company, ICICI Direct Research

Exhibit 7: SOTP valuation

	FY21E	Remarks
Two-wheeler business-Royal Enfield		
EPS (₹)	986	
Target PE multiple(x)	22.0	Valued RE business at 22x P/E, in tandem with its long period averages
Per share value (₹)	21,704	
Target market cap (₹ crore)	59,164	
CV business-VECV`		
PAT	183	
Target PE multiple(x)	14.0	Lowered the P/E multiple factoring in limited growth prospects over FY19-21E
Target market cap (₹ crore)	2,566	
Contribution towards EML	0.54	EML has 54.4% stake in VECV
Target market cap towards EML (₹ crore)	1,396	
Per share value-VECV Eicher (₹)	500	
Total target market cap (₹ crore)	60,560	
Per share value (₹)	22,215	

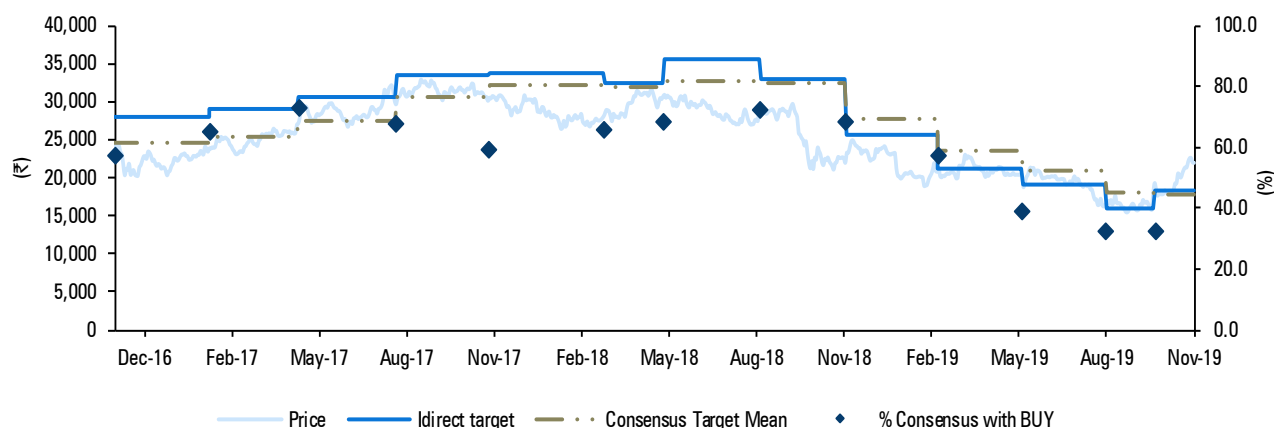
Source: Bloomberg, ICICI Direct Research

Exhibit 8: Valuation Summary

	Net Sales	Growth	EPS	Growth	PE	EV/EBITDA	RoNW	RoCE
	(₹ cr)	(%)	(₹)	(%)	(x)	(x)	(%)	(%)
FY17	7,033.4	N.A.	613	30.5	35.4	25.7	31.8	40.6
FY18	8,965.0	27.46	719	17.3	30.2	19.7	29.9	39.1
FY19	9,797.1	9.28	808	12.4	26.9	19.3	24.8	32.5
FY20E	10,244.2	4.6	848	5.0	25.6	20.4	21.5	25.7
FY21E	12,086.5	18.0	1,007	18.8	21.5	16.0	21.1	26.5

Source: Bloomberg, ICICI Direct Research

Exhibit 9: Recommendation history vs. consensus



Source: Reuters, ICICI Direct Research

Exhibit 10: Top 10 shareholders

Rank	Name	Latest Filing Date	% O/S	Position (m)	Change (m)
1	Simran Siddhartha Tara Benefit Trust	30-Jun-19	44.1	12.0	0.00
2	Brinda Lal Trust	30-Jun-19	1.8	0.5	0.00
3	The Vanguard Group, Inc.	30-Sep-19	1.7	0.5	-0.01
4	GIC Private Limited	30-Jun-19	1.6	0.4	0.07
5	Capital Research Global Investors	30-Sep-19	1.6	0.4	-0.52
6	BlackRock Institutional Trust Company, N.A.	30-Sep-19	1.5	0.4	0.00
7	Vontobel Asset Management, Inc.	30-Sep-19	1.4	0.4	0.00
8	UTI Asset Management Co. Ltd.	30-Sep-19	1.2	0.3	0.02
9	Lal (Simran)	30-Jun-19	1.2	0.3	0.00
10	Lal (Tara)	30-Jun-19	1.2	0.3	0.00

Source: Reuters, ICICI Direct Research

Exhibit 11: Recent activity

Buys			Sells		
Investor name	Value	Shares	Investor name	Value	Shares
ICICI Prudential Asset Management Co. Ltd.	+23.32M	+0.09M	Capital Research Global Investors	-131.78M	-0.52M
GIC Private Limited	+18.40M	+0.07M	Artisan Partners Limited Partnership	-22.66M	-0.09M
SBI Funds Management Pvt. Ltd.	+11.34M	+0.05M	Sands Capital Management, LLC	-14.18M	-0.06M
UTI Asset Management Co. Ltd.	+4.62M	+0.02M	Kotak Mahindra Asset Management Company Ltd.	-7.30M	-0.03M
Mellon Investments Corporation	+3.08M	+0.01M	Fidelity Management & Research Company	-7.39M	-0.02M

Source: Reuters, ICICI Direct Research

Exhibit 12: Shareholding pattern

(in %)	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19
Promoter	49.4	49.3	49.3	49.3	49.3
FII	31.5	30.8	32.5	33.2	31.9
DII	5.6	6.2	4.6	4.7	7.2
Others	13.6	13.7	13.6	12.8	11.6

Source: Company, ICICI Direct Research

Financial Summary

Exhibit 13: Profit and loss statement				
	₹ crore			
(Year-end March)	FY18	FY19	FY20E	FY21E
Total operating Income	8,965.0	9,797.1	10,244.2	12,086.5
Growth (%)	-42.9	9.3	4.6	18.0
Raw Material Expenses	4,481.7	4,845.7	5,286.6	6,290.1
Employee Expenses	573.7	702.4	777.0	823.2
Other Expenses	940.2	1,134.1	1,219.8	1,346.2
Total Operating Expenditure	6,157.3	6,893.9	7,561.7	8,819.5
EBITDA	2807.6	2903.1	2682.5	3267.0
Growth (%)	14.7	3.4	-7.6	21.8
Depreciation	223.3	300.3	360.2	386.8
Interest	5.3	7.3	10.7	7.6
Other Income	280.1	443.4	566.0	679.9
PBT	2,859.1	3,038.9	2,877.7	3,552.5
Others	0.0	0.0	0.0	0.0
Total Tax	935.9	1,077.0	644.8	905.9
PAT	1959.7	2202.8	2312.3	2746.2
Growth (%)	53.4	12.4	5.0	18.8
EPS (₹)	718.9	808.1	848.2	1007.4

Source: Company, ICICI Direct Research

Exhibit 14: Cash flow statement				
	₹ crore			
(Year-end March)	FY18	FY19	FY20E	FY21E
Profit after Tax	1,959.7	2,202.8	2,312.3	2,746.2
Add: Depreciation	223.3	300.3	360.2	386.8
(Inc)/dec in Current Assets	-217.4	-286.6	-129.8	-198.9
Inc/(dec) in CL and Provisions	696.5	-218.5	58.0	349.7
CF from operating activities	2662.1	1998.0	2600.6	3283.8
(Inc)/dec in Investments	-575.3	838.0	-1,400.0	-2,200.0
(Inc)/dec in Fixed Assets	-738.6	-789.7	-700.0	-500.0
Others	147.4	-14.8	13.9	57.3
CF from investing activities	-1166.5	33.5	-2086.1	-2642.7
Issue/(Buy back) of Equity	0.0	0.0	0.0	0.0
Inc/(dec) in loan funds	39.0	35.9	-25.0	-100.0
Dividend paid & dividend tax	-361.0	-410.3	-459.5	-492.3
Others	13.3	96.1	0.0	0.0
CF from financing activities	-308.7	-278.2	-484.5	-592.3
Net Cash flow	1,186.9	1,753.2	30.0	48.8
Opening Cash	25.1	1,212.0	2,965.2	2,995.2
Closing Cash	1212.0	2965.2	2995.2	3044.0

Source: Company, ICICI Direct Research

Exhibit 15: Balance Sheet				
	₹ crore			
(Year-end March)	FY18	FY19	FY20E	FY21E
Liabilities				
Equity Capital	27.3	27.3	27.3	27.3
Reserve and Surplus	7,002.8	8,891.4	10,744.2	12,998.1
Total Shareholders funds	7030.1	8918.7	10771.5	13025.4
Total Debt	150.8	186.8	161.8	61.8
Deferred Tax Liability	142.1	273.9	286.4	337.9
Others	94.1	120.8	123.4	134.3
Total Liabilities	7417.0	9500.1	11343.0	13559.3
Assets				
Gross Block	2,112.1	2,785.2	3,685.0	4,185.0
Less: Acc Depreciation	610.3	910.6	1,269.2	1,655.9
Net Block	1501.7	1874.6	2415.8	2529.0
Capital WIP	333.2	449.7	250.0	250.0
Total Fixed Assets	1,834.9	2,324.4	2,665.8	2,779.0
Investments	5,580.8	4,922.5	6,322.5	8,522.5
Inventory	394.6	633.4	701.7	827.8
Debtors	68.0	90.3	140.3	165.6
Others	227.0	252.5	264.0	311.5
Cash	1212.0	2965.2	2995.2	3044.0
Total Current Assets	1,901.6	3,941.4	4,101.2	4,348.9
Creditors	1,171.9	1,234.1	1,263.0	1,490.1
Provisions	38.0	33.0	33.8	39.8
Others	895.3	619.6	647.9	764.4
Total Current Liabilities	2,105.2	1,886.7	1,944.7	2,294.4
Net Current Assets	-203.6	2054.7	2156.6	2054.5
Other Non current asset	204.9	198.5	199.8	204.9
Application of Funds	7417.0	9500.1	11343.0	13559.3

Source: Company, ICICI Direct Research

Exhibit 16: Key ratios				
(Year-end March)	FY18	FY19	FY20E	FY21E
Per share data (₹)				
EPS	718.9	808.1	848.2	1,007.4
Cash EPS	800.8	918.2	980.4	1,149.3
BV	2,578.9	3,271.7	3,951.4	4,778.2
DPS	110.0	125.0	140.0	150.0
Cash Per Share	83.0	92.1	96.4	113.7
Operating Ratios (%)				
EBITDA Margin	31.3	29.6	26.2	27.0
PBT / Net sales	28.8	26.6	22.7	23.8
PAT Margin	23.4	22.6	22.6	22.7
Inventory days	16.1	23.6	25.0	25.0
Debtor days	2.8	3.4	5.0	5.0
Creditor days	47.7	46.0	45.0	45.0
Return Ratios (%)				
RoE	29.9	24.8	21.5	21.1
RoCE	39.1	32.5	25.7	26.5
RoIC	367.4	203.5	121.8	149.4
Valuation Ratios (x)				
P/E	28.1	26.7	25.6	21.5
EV / EBITDA	19.7	19.3	20.4	16.0
EV / Net Sales	6.2	5.7	5.3	4.3
Market Cap / Sales	6.6	6.0	5.8	4.9
Price to Book Value	8.4	6.6	5.5	4.5
Solvency Ratios				
Debt/Equity	0.0	0.0	0.0	0.0
Current Ratio	0.5	0.6	0.7	0.7
Quick Ratio	0.2	0.2	0.3	0.3

Source: Company, ICICI Direct Research

Exhibit 17: ICICI Direct Research coverage universe (Auto & Auto Ancillary)

Sector / Company	CMP		Rating	M Cap (₹ Cr)	EPS (₹)			P/E (x)			EV/EBITDA (x)			RoCE (%)			RoE (%)		
	(₹)	TP(₹)			FY19	FY20E	FY21E	FY19	FY20E	FY21E	FY19	FY20E	FY21E	FY19	FY20E	FY21E	FY19	FY20E	FY21E
Apollo Tyre (APOTYR)	165	180	Hold	9447	11.9	10.3	12.0	13.9	16.0	13.7	7.5	7.5	6.3	8.0	5.8	6.7	8.3	5.7	6.3
Ashok Leyland (ASHLEY)	77	75	Hold	22471	6.8	5.8	6.2	11.3	13.1	12.4	5.8	6.3	5.8	26.9	22.7	22.2	24.3	18.8	18.1
Bajaj Auto (BAAUTO)	3246	3300	Hold	93916	161.6	175.0	189.0	19.6	18.1	16.7	14.9	13.9	11.9	21.0	19.5	25.9	19.9	20.6	19.8
Bharat Forge (BHAFOR)	427	515	Buy	19864	22.2	23.5	24.9	19.2	18.1	17.1	11.5	11.5	10.8	17.9	16.0	16.3	19.1	17.6	16.9
Eicher Motors (EICMOT)	21700	22215	Hold	59154	808.1	848.2	1007.4	26.9	25.6	21.5	19.3	20.4	16.0	32.5	25.7	26.5	24.8	21.5	21.1
Exide Industries (EXIIND)	187	230	Buy	16150	9.9	11.2	12.7	18.8	16.6	14.6	11.2	9.8	8.5	18.4	18.8	19.2	12.9	14.3	14.6
Hero Moto (HERHON)	2700	3110	Buy	53919	169.5	195.0	182.9	15.9	13.8	14.8	10.0	10.5	9.7	37.1	30.1	29.8	26.3	23.9	23.0
M&M (MAHMAH)	580	660	Buy	72106	38.6	46.4	32.0	15.0	12.5	18.1	10.4	10.1	10.4	17.3	15.3	12.3	14.1	12.2	9.6
Maruti Suzuki (MARUTI)	7396	6420	Reduce	223418	248.3	212.7	257.9	29.8	34.8	28.7	17.1	21.7	17.6	16.3	9.4	11.5	16.3	12.9	14.3
Tata Motors (TATMOT)	169	175	Hold	54330	-84.6	-2.3	8.9	-2.0	-73.8	18.9	4.0	4.0	3.5	5.4	7.7	8.9	7.1	0.0	10.8

Source: Reuters, ICICI Direct Research

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Buy: >15%

Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



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