



VISIT NOTE

EICHER MOTORS

'Selling an experience'

India Equity Research | Automobiles



Our recent meeting with Mr. Siddhartha Lal, MD & CEO, Eicher Motors (EIM) reinforced our confidence about Royal Enfield's (RE) bright long-term prospects. What we liked the most was: (1) Unwavering focus on selling an 'experience' rather than selling a 'product'; (2) Decentralisation of decision making; (3) Strengthening of systems and processes (from product development to dealers) to gear up for next level of growth; and (4) Preparing the team for a mindset change amid limited order backlog. In exports, the aspiration is to create few India-like markets, where EIM can achieve leadership position.

- **Mindset change:** In past 5 years, the focus has been on sprucing up the backend in terms of manufacturing capacity, vendor capacity, products, etc. Going ahead, the team is being prepared to approach business with a new mindset with emphasis on frontend. Capacity ramp up will drastically reduce waiting period which has not been experienced by the team in last 5 years. There are successful businesses in India that have doubled volumes in a 'no-waitlist' scenario. The focus is on the entire ecosystem.
- **Exports:** Aspires to sell 10K bikes/month in few countries and establish dominance. A new model is likely to be launched in next 6-8 months, with major inputs from the new tech centre in the UK. EIM believes the new product will expand its product basket in export markets.
- **Institutionalising the process:** With scale, EIM has also been focusing on institutionalising the process across functions. For instance, a new product launch now takes ~3 years from inception stage, with the tooling ready ~18 months before the launch. Similarly, in R&D, earlier a single team carried out different functions simultaneously. Now each function is managed by separate teams.

Outlook and valuations: On firm footing; maintain 'BUY'

We estimate ~44% EPS CAGR over FY17-19 on strong demand for RE and margin improvement, which would benefit from scale and vendor consolidation. VECV is also focusing on profitable growth. At CMP, the stock trades at FY19E PER of 24.3x. Maintain 'BUY/SO' with TP of INR34,891 (30x core EPS (preferred band 25-35x), 17x VECV core EPS and INR2,576 cash per share).

Financials (Consolidated)		(INR mn)			
Year to March	FY16	FY17	FY18E	FY19E	
Revenues (INR mn)	61,735	70,334	94,198	127,881	
Adjusted profit (INR mn)	11,901	16,671	24,570	34,663	
Adjusted diluted EPS (INR)	438.2	613.8	904.6	1,276.2	
EPS growth (%)	64.0	69.5	47.4	41.1	
Diluted P/E (x)	70.7	50.5	34.2	24.3	
EV/EBITDA (x)	38.0	30.8	22.9	15.9	
ROAE (%)	32.8	37.1	38.6	39.3	

EDELWEISS 4D RATINGS

Absolute Rating	BUY
Rating Relative to Sector	Outperform
Risk Rating Relative to Sector	Medium
Sector Relative to Market	Underweight

MARKET DATA (R: EICH.BO, B: EIM IN)

CMP	: INR 30,980
Target Price	: INR 34,891
52-week range (INR)	: 33,484 / 19,530
Share in issue (mn)	: 27.2
M cap (INR bn/USD mn)	: 843 / 12,948
Avg. Daily Vol.BSE/NSE('000)	: 52.5

SHARE HOLDING PATTERN (%)

	Current	Q4FY17	Q3FY17
Promoters *	50.6	50.6	50.6
MF's, FI's & BK's	4.3	4.0	3.8
FII's	31.9	32.5	32.5
Others	13.2	12.9	13.0
* Promoters pledged shares (% of share in issue)	:	NIL	

PRICE PERFORMANCE (%)

	Stock	Nifty	EW Auto Index
1 month	1.9	2.0	4.3
3 months	14.1	3.5	1.6
12 months	27.3	12.4	7.3

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Royal Enfield (2W)

- Product development capabilities:** EIM has significantly beefed up its capabilities in past 3 years. Its tech centre in the UK has a cross-cultural team who are from various organisations. The expected new launch will have significant contribution from the UK tech centre. The new product will also be capable to meet specific customer requirements in export markets.
- Dealerships (2W):** There is strong focus on various aspects of dealerships – right from size to the background of the dealer to his income mix. The focus is to ensure that dealers consider each revenue stream – spares, services and accessories as critical sources of revenue rather than a push function. Also, EIM’s regional HR team plays an important role in career progression of employees at dealer level to ensure lower churn.
- Exports:** While the aspiration is to sell 10K bikes/month in few markets, the focus is to create brand pull. Hence, incrementally the preference is to set up dealerships rather than distributorship as it not only helps gauge pulse of consumer behaviour in a better manner but also helps wield control. The new product launch is expected to lend fillip to exports.

We also met CFO, Mr. Lalit Malik on August 31, 2017 (Click on [the link](#))

Chart 1: RE ramping up network across Tier I/II cities



Chart 2: RE exports gaining traction

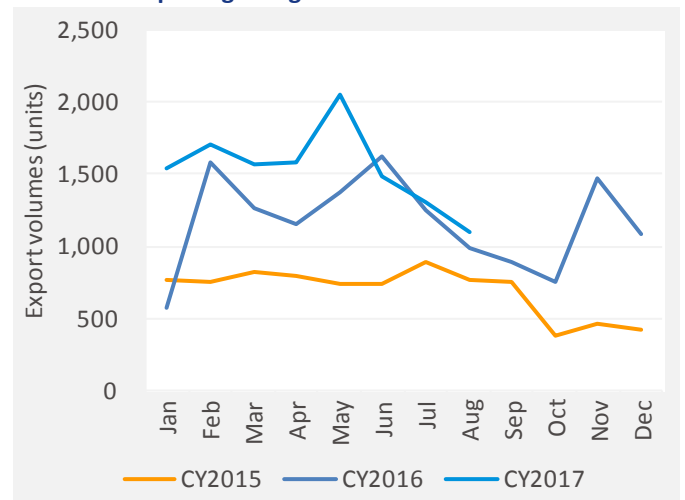


Table 1: Valuation snapshot

INR mn	FY19E	Target Multiple (x)	Target price
VECV (54.4% stake)	81	17.0	1,378
Standalone core EPS	1,031	30.0	30,936
Standalone cash per share			2,576
Value per share (INR)			34,891

Source: Edelweiss research

Table 2: Key assumptions

Volumes	FY16	FY17	FY18E	FY19E
Total CV	62,843	55,338	59,697	65,552
% YoY	23.4	10.1	7.9	9.8
MHCV	42,798	38,722	41,761	46,075
% YoY	22.9	13.1	7.8	10.3
LCV	18,546	15,453	16,657	18,070
% YoY	23.6	4.2	7.8	8.5
Volvo	1,499	1,163	1,279	1,407
% YoY	34.6	(3.0)	10.0	10.0
2-wh (RE)	601,000	666,490	841,162	1,112,407
% YoY	58.9	38.6	26.2	32.2

Source: Edelweiss research

Company Description

Incorporated in 1982, Eicher Motors (EIM) is the flagship company of the Eicher Group in India and a leading player in the Indian motorcycle and commercial vehicle (CV) segments. EIM manufactures and markets its motorcycle under the iconic brand name, 'Royal Enfield' and is market leader in the >250cc motorcycle segment with over 95% market share. EIM is a structural story on the premiumisation theme in motorcycles. The CV segment operates under a joint venture (JV) called VE Commercial Vehicles (VECV). We believe it is a strong candidate to break the duopoly of Tata Motors/Ashok Leyland in M&HCVs. Strong balance sheet, credible partner Volvo and management provide additional comfort.

Investment Theme

EIM (RE) remains key beneficiary of the shift in demand towards >250cc motorcycles given the ongoing premiumisation trend. Strong order book position, low penetration levels for premium motorcycles (3 per 1,000 males), network expansion across tier I/II cities and improving traction across export markets are likely to sustain the volume momentum. Operation leverage benefits are expected to drive robust ~280bps margin improvement over FY17-19E. We believe VECV is a strong candidate to break the duopoly of Tata Motors/Ashok Leyland in M&HCVs.

Key Risks

Capacity constraints for 2W: Slower pace of capacity addition will restrict EIM's ability to capitalise on the virtual monopolistic situation that it currently enjoys.

Excessive reliance on single model: Around 70% of 2W sales are currently accounted by its single model, Classic. We believe, it is pertinent for EIM to create an alternate successful model given the fast-changing consumer preferences.

Financial Statements

Key Assumptions

Year to March	FY16	FY17	FY18E	FY19E
Macro				
GDP(Y-o-Y %)	7.9	6.6	6.8	7.4
Inflation (Avg)	4.9	4.5	4.0	4.5
Repo rate (exit rate)	6.8	6.3	5.8	5.8
USD/INR (Avg)	65.5	67.1	65.0	66.0
Sector				
Motorcycle - dom. vol. (% YoY)	-	4.0	8.0	8.0
MHCV - domestic vol (% YoY)	30.0	1.0	8.0	8.0
Company				
Revenue assumptions				
Motorcycle - domestic volume (% YoY)	58.9	38.6	26.2	32.2
MHCV - domestic vol (% YoY)	27.0	7.5	7.8	9.8
LCV - dom. vol. (% YoY)	27.4	4.7	7.4	8.2
Average price (INR)				
Royal Enfield (INR)	107,651	109,217	110,310	112,295
Royal Enfield (% YoY)	6.0	1.5	1.0	1.8
VECV (INR)	872,260	863,537	949,891	978,387
VECV (% YoY)	8.2	(1.0)	10.0	3.0
Cost assumptions				
RM cost/vehicle	51,746	51,321	54,243	55,924
Employee cost/vehicle	5,275	5,574	5,744	5,098
EBITDA/vehicle	25,452	30,117	34,050	36,866
Financial assumptions				
Depreciation rate (%)	12.8	11.9	10.5	10.0
Tax rate (%)	31.2	32.1	30.0	30.0
Dividend payout (%)	26.4	23.1	17.3	17.3
B/S assumptions				
Net borrowings (INR mn)	(358)	218	(144)	-
Capex (INR mn)	(25,587)	5,036	8,000	5,000
Debtor days	18	2	2	2
Inventory days	51	32	29	28
Payable days	178	129	127	127
Cash conversion cycle	(110)	(95)	(96)	(97)

Income statement

(INR mn)

Year to March	FY16	FY17	FY18E	FY19E
Income from operations	61,735	70,334	94,198	127,881
Materials costs	34,351	37,045	48,865	65,876
Employee costs	3,502	4,024	5,174	6,005
Total SG&A expenses	6,985	7,526	9,485	12,573
Total operating expenses	44,839	48,594	63,524	84,454
EBITDA	16,896	21,740	30,674	43,427
Depreciation	1,366	1,538	2,196	2,592
EBIT	15,530	20,201	28,477	40,835
Add: Other income	1,780.9	2,273.3	4,332.75	5,582.83
Less: Interest Expense	21	36	27	27
Profit Before Tax	17,290	22,439	32,783	46,391
Less: Provision for Tax	5,389	7,203	9,835	13,917
Associate profit share	-	1,435	1,621	2,189
Reported Profit	11,901	16,671	24,570	34,663
Adjusted Profit	11,901	16,671	24,570	34,663
Shares o /s (mn)	27	27	27	27
Adjusted Basic EPS	438.2	613.8	904.6	1,276.2
Diluted shares o/s (mn)	27	27	27	27
Adjusted Diluted EPS	438.2	613.8	904.6	1,276.2
Adjusted Cash EPS	438.1	625.1	924.6	1,301.8
Dividend per share (DPS)	100.2	100.0	136.0	191.9
Dividend Payout Ratio(%)	26.4	23.1	17.3	17.3

Common size metrics

Year to March	FY16	FY17	FY18E	FY19E
Operating expenses	72.6	69.1	67.4	66.0
Materials costs	55.6	52.7	51.9	51.5
Staff costs	5.7	5.7	5.5	4.7
S G & A expenses	11.3	10.7	10.1	9.8
Depreciation	2.2	2.2	2.3	2.0
Interest Expense	-	0.1	-	-
EBITDA margins	27.4	30.9	32.6	34.0
Net Profit margins	19.3	23.7	26.1	27.1

Growth ratios (%)

Year to March	FY16	FY17	FY18E	FY19E
Revenues	(39.9)	34.0	33.9	35.8
EBITDA	28.8	51.4	41.1	41.6
PBT	48.1	52.7	46.1	41.5
Adjusted Profit	64.4	64.8	47.4	41.1
EPS	64.0	64.8	47.4	41.1

Automobiles

Balance sheet		(INR mn)			
As on 31st March	FY16	FY17	FY18E	FY19E	
Share capital	272	272	271	271	
Reserves & Surplus	36,259	53,179	73,491	102,148	
Shareholders' funds	36,531	53,451	73,762	102,419	
Short term borrowings	-	-	300	300	
Long term borrowings	226	444	-	-	
Total Borrowings	226	444	300	300	
Def. Tax Liability (net)	359	778	778	778	
Sources of funds	37,115	54,673	74,840	103,496	
Gross Block	10,708	12,951	20,951	25,951	
Net Block	7,942	8,728	14,531	16,939	
Capital work in progress	945	3,738	3,738	3,738	
Total Fixed Assets	8,886	12,466	18,269	20,677	
Cash and Equivalents	34,195	50,044	67,264	97,341	
Inventories	3,084	3,359	4,329	5,879	
Sundry Debtors	326	500	657	892	
Loans & Advances	2,830	3,535	5	6	
Other Current Assets	68	3	4,723	6,413	
Current Assets (ex cash)	6,309	7,397	9,713	13,191	
Trade payable	11,714	14,548	19,485	26,461	
Other Current Liab	561	686	922	1,251	
Total Current Liab	12,275	15,234	20,407	27,713	
Net Curr Assets-ex cash	(5,967)	(7,837)	(10,694)	(14,522)	
Uses of funds	37,115	54,673	74,840	103,496	
BVPS (INR)	1,345.0	1,968.0	2,715.8	3,770.9	

Free cash flow		(INR mn)			
Year to March	FY16	FY17	FY18E	FY19E	
Reported Profit	11,901	16,671	24,570	34,663	
Add: Depreciation	1,366	1,538	2,196	2,592	
Interest (Net of Tax)	15	24	19	19	
Others	1,349	(392)	(1,468)	(1,746)	
Less: Changes in WC	1,683	1,870	2,857	3,829	
Operating cash flow	14,631	17,841	25,317	35,527	
Less: Capex	(25,587)	5,036	8,000	5,000	
Free Cash Flow	40,218	12,805	17,317	30,527	

Cash flow metrics		FY16	FY17	FY18E	FY19E
Year to March					
Operating cash flow		14,631	17,841	25,317	35,527
Investing cash flow		(10,014)	(18,797)	(18,159)	(31,417)
Financing cash flow		(4,655)	(3,668)	(4,429)	(6,033)
Net cash Flow		(38)	(4,624)	2,729	(1,923)
Capex		25,587	(5,036)	(8,000)	(5,000)
Dividend paid		(3,138)	(3,851)	(4,257)	(6,006)

Profitability and efficiency ratios		FY16	FY17	FY18E	FY19E
Year to March					
ROAE (%)		32.8	37.1	38.6	39.3
ROACE (%)		47.2	49.6	51.3	52.5
Inventory Days		51	32	29	28
Debtors Days		18	2	2	2
Payable Days		178	129	127	127
Cash Conversion Cycle		(110)	(95)	(96)	(97)
Current Ratio		3.3	3.8	3.8	4.0
Gross Debt/EBITDA		-	-	-	-
Gross Debt/Equity		-	-	-	-
Adjusted Debt/Equity		-	-	5.6	5.5
Net Debt/Equity		(0.9)	(0.9)	-	-
Interest Coverage Ratio		732.6	567.5	-	-

Operating ratios		FY16	FY17	FY18E	FY19E
Year to March					
Total Asset Turnover		1.6	1.5	1.5	1.4
Fixed Asset Turnover		4.0	8.4	6.1	6.6
Equity Turnover		1.7	1.6	1.5	1.5

Valuation parameters		FY16	FY17	FY18E	FY19E
Year to March					
Adj. Diluted EPS (INR)		438.2	613.8	904.6	1,276.2
Y-o-Y growth (%)		64.0	64.8	47.4	41.1
Adjusted Cash EPS (INR)		438.1	625.1	924.6	1,301.8
Diluted P/E (x)		72.1	51.4	34.9	24.7
P/B (x)		23.5	16.0	11.6	8.4
EV / Sales (x)		13.1	11.3	8.2	5.8
EV/Sales adjusted for Volvo		7.2	6.8	5.5	4.2
EV / EBITDA (x)		48.8	37.2	25.8	17.5
EV/EBITDA adjusted for Volvo		38.0	30.8	22.9	15.9
Dividend Yield (%)		0.3	0.3	0.4	0.6

Peer comparison valuation

Name	Market cap (USD mn)	Diluted P/E (X)		EV / EBITDA (X)		P/B (X)	
		FY18E	FY19E	FY18E	FY19E	FY18E	FY19E
Eicher Motors	13,268	34.9	24.7	25.8	17.5	11.6	8.4
Bajaj Auto	13,587	19.7	17.7	14.3	12.2	4.6	4.1
Hero MotoCorp	11,684	20.5	17.6	13.4	11.3	6.8	6.0
Median	-	20.5	17.7	14.3	12.2	6.8	6.0
AVERAGE	-	25.0	20.0	17.8	13.7	7.7	6.1

Source: Edelweiss research

Additional Data

Directors Data

S Sandilya, Chairman	Non-Executive Independent Directors	Priya Brat	Non-Executive Independent Directors
M J Sibbaiah	Non-Executive Independent Directors	Prateek Jalan	Non-Executive Independent Directors
Siddhartha Lal, MD	Executive Director	R L Ravichandran, Whole Time Director	Executive Director

Auditors - Deloitte Haskins & Sells

**as per last annual report*

Holding – Top10

	Perc. Holding		Perc. Holding
The simran siddhar t	44.19	Capital group compan	3.98
Citigroup gbl mkts	2.01	Brinda lal trust	1.78
Blackrock	1.75	Vanguard group	1.7
Lal tara vikram	1.16	Lal simran vikram	1.16
Joshi rukmani	1.12	Lal siddhartha	1.08

**in last one year*

Bulk Deals

Data	Acquired / Seller	B/S	Qty Traded	Price
No Data Available				

**in last one year*

Insider Trades

Reporting Data	Acquired / Seller	B/S	Qty Traded
03 Apr 2017	KARVANSARAI TRAVEL & LIFESTYLE PVT. LTD.	Buy	15143.00
03 Apr 2017	EICHER GOODEARTH PVT. LTD.	Sell	15143.00
31 Mar 2017	KARVANSARAI TRAVEL & LIFESTYLE PVT. LTD.	Buy	15143.00
31 Mar 2017	EICHER GOODEARTH PVT. LTD.	Sell	15143.00
02 Feb 2017	THE SIMRAN SIDDHARTHA TARA BENEFIT TRUST	Buy	2479907.00

**in last one year*

Company	Absolute reco	Relative reco	Relative risk	Company	Absolute reco	Relative reco	Relative Risk
Amara Raja Batteries	BUY	None	None	Ashok Leyland	BUY	SO	H
Bajaj Auto	HOLD	SU	L	Ceat Ltd	BUY	SO	L
Eicher Motors	BUY	SO	M	Exide Industries	BUY	SP	L
Hero MotoCorp	HOLD	SU	H	Mahindra & Mahindra Ltd	BUY	SO	M
Maruti Suzuki India Ltd	BUY	SO	H	Minda Corporation	BUY	SO	M
Motherson Sumi Systems	HOLD	SU	H	Suprajit Engineering	BUY	SO	H
Tata Motors Ltd	HOLD	SP	H				

ABSOLUTE RATING

Ratings	Expected absolute returns over 12 months
Buy	More than 15%
Hold	Between 15% and - 5%
Reduce	Less than -5%

RELATIVE RETURNS RATING

Ratings	Criteria
Sector Outperformer (SO)	Stock return > 1.25 x Sector return
Sector Performer (SP)	Stock return > 0.75 x Sector return
	Stock return < 1.25 x Sector return
Sector Underperformer (SU)	Stock return < 0.75 x Sector return

Sector return is market cap weighted average return for the coverage universe within the sector

RELATIVE RISK RATING

Ratings	Criteria
Low (L)	Bottom 1/3rd percentile in the sector
Medium (M)	Middle 1/3rd percentile in the sector
High (H)	Top 1/3rd percentile in the sector

Risk ratings are based on Edelweiss risk model

SECTOR RATING

Ratings	Criteria
Overweight (OW)	Sector return > 1.25 x Nifty return
Equalweight (EW)	Sector return > 0.75 x Nifty return
	Sector return < 1.25 x Nifty return
Underweight (UW)	Sector return < 0.75 x Nifty return



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Coverage group(s) of stocks by primary analyst(s): Automobiles

Ashok Leyland, Amara Raja Batteries, Bajaj Auto, Ceat Ltd, Eicher Motors, Exide Industries, Hero MotoCorp, Minda Corporation, Mahindra & Mahindra Ltd, Maruti Suzuki India Ltd, Motherson Sumi Systems, Suprajit Engineering, Tata Motors Ltd

Recent Research

Date	Company	Title	Price (INR)	Recos
15-Sep-17	Suprajit Engineering	Tepid quarter, but long-term story intact; <i>Result Update</i>	281	Buy
15-Sep-17	Minda Corporation	Minda Furukawa springs a positive surprise; <i>Result Update</i>	132	Buy
04-Sep-17	Automobiles	Strong show across the board; <i>Routine Update</i>		

Distribution of Ratings / Market Cap

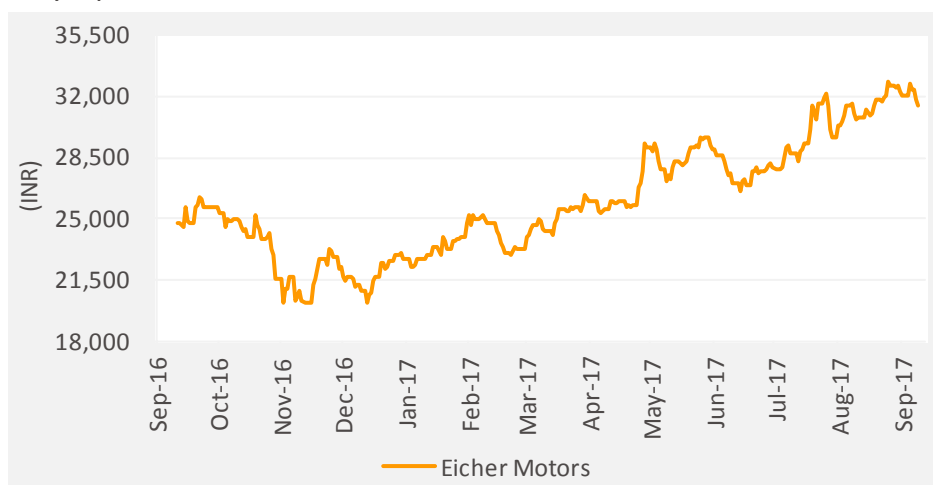
Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution*	161	67	11	240
* 1stocks under review				
	> 50bn	Between 10bn and 50 bn	< 10bn	
Market Cap (INR)	156	62	11	

Rating Interpretation

Rating	Expected to
Buy	appreciate more than 15% over a 12-month period
Hold	appreciate up to 15% over a 12-month period
Reduce	depreciate more than 5% over a 12-month period

One year price chart



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