

**HOLD**

TP: Rs 3,543 | ▲ 5%

**EICHER MOTORS**

| Auto Components

| 21 November 2022

**Volume gains encouraging; ASP revival key**

- Q2 revenue up 5% QoQ to Rs 33bn backed by 11% volume growth (MoM run-rate of 60k units), partly offset by 7% fall in ASP
- Gross margin dipped 119bps QoQ due to higher raw material cost at 58.5% of sales
- We assume coverage with HOLD and an SOTP-based TP of Rs 3,543, valuing the core business at 28x FY24E EPS

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**Volumes pick up:** EIM's Q2FY23 revenue grew 5% QoQ to Rs 33.4bn backed up 11% volume gains, partly offset by a 7% sequential fall in average selling price (ASP) which remains under pressure. With a MoM run-rate of 60k+ units, the volume revival over the past four months has been encouraging. Gross margin dipped 119bps QoQ owing to inflated raw material cost at 58.5% of sales (57.3% in Q1FY22). EBITDA was flat QoQ at Rs 8bn, but EBITDA margin fell 60bps to 23.7% due to lower operating efficiencies in Q2FY23. Adj. PAT increased 11% QoQ to Rs 6.4bn owing to a lower tax rate of 20% against the average of 24%.

**Margins on improving trajectory:** EIM's operations have suffered from the non-availability of semiconductor chips and raw material cost inflation. However, with both these constraints easing, we expect margins to improve. During the chip shortage, EIM had to rely on resellers which piled on pricing pressure. This is likely to recede as chip availability improves. The company launched new models including 'Hunter 350' and 'Super Meteor 650' that boosted Q2 volumes (by +50k units). With better synergies from higher utilisation, we expect operating leverage to improve, further boosting margins.

**No major capex plans:** Management does not have aggressive capex plans for Hunter 350 as the components required for variants 'Hunter Metro' are sourced from 'Hunter Retro', for which the company has already invested Rs 10mn-12mn. Thus, no major incremental capex is on the cards.

**HOLD, TP Rs 3,543:** We expect EIM to clock a revenue, EBITDA and PAT CAGR of 23%, 33% and 35% respectively over FY22-FY25. Our FY24-FY25 earnings forecasts are ~5% below consensus due to lower volume assumptions and our EBITDA margins are 100bps below at ~26%. Our margin forecast represents ~600bps expansion by FY25 to bake in new high-end variants, export volumes and operating efficiencies. However, we believe current valuations of ~28x FY24E EPS capture the positives. We value EIM at 28x FY24E EPS (in line with its long-term average) and assign Rs 175/sh (average consensus value) to its VECV business, translating to a TP of Rs 3,543 – assume coverage with HOLD.

**Key changes**

| Target | Rating |
|--------|--------|
| ▲      | ◀ ▶    |

|                  |                   |
|------------------|-------------------|
| Ticker/Price     | EIM IN/Rs 3,390   |
| Market cap       | US\$ 11.3bn       |
| Free float       | 51%               |
| 3M ADV           | US\$ 35.0mn       |
| 52wk high/low    | Rs 3,890/Rs 2,160 |
| Promoter/FPI/DII | 49%/30%/9%        |

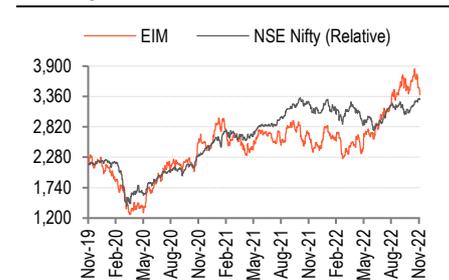
Source: NSE | Price as of 18 Nov 2022

**Key financials**

| Y/E 31 Mar              | FY22A   | FY23E   | FY24E   |
|-------------------------|---------|---------|---------|
| Total revenue (Rs mn)   | 101,229 | 144,350 | 165,600 |
| EBITDA (Rs mn)          | 21,136  | 35,338  | 42,641  |
| Adj. net profit (Rs mn) | 15,772  | 26,433  | 32,709  |
| Adj. EPS (Rs)           | 58.1    | 97.3    | 120.3   |
| Consensus EPS (Rs)      | 58.1    | 102.1   | 127.2   |
| Adj. ROAE (%)           | 14.6    | 20.7    | 21.3    |
| Adj. P/E (x)            | 58.3    | 34.9    | 28.2    |
| EV/EBITDA (x)           | 41.1    | 25.0    | 21.4    |
| Adj. EPS growth (%)     | 19.3    | 67.3    | 23.7    |

Source: Company, Bloomberg, BOBCAPS Research

**Stock performance**



Source: NSE



## Earnings call highlights

- **Royal Enfield:** EIM launched the Hunter 350 in Q2FY23, rolling out 50k+ units. Management indicated that the order book is healthy and growing. The vehicle pertains to a new segment of customers. Per management, first-time buyers typically comprise ~13% of the customer mix, but this has climbed to 18.2% following the Hunter launch.

The Hunter 350 has two categories: Retro (priced at Rs 0.15mn) and Metro (priced at Rs 0.17mn). Demand for the Metro is much higher than that for Retro. The company indicated that it has not seen any cannibalisation after the launch of Hunter 350, but this could be attributed to the festive season-led buoyancy across products. Pricing has been hiked by Rs 3k for Hunter from Nov'22, and EIM has refreshed its plants to tap demand. It also launched the Super Meteor 650 recently.

- **Margins:** Management is expecting commodity prices to soften in the medium term. Additionally, the company had to earlier rely on resellers during the semiconductor shortage phase, leading to an increase in product prices/logistic costs. With chip availability improving, pricing pressures are likely to recede.
- **Commercial vehicles:** Sales of heavy-duty trucks and buses grew in Q2, but management does not expect volumes to reach the FY19 peak. However, management expects to see a new peak in light and medium-duty trucks in FY23. Customers are focusing on productivity, lower costs and technology, spurring demand for new trucks.
- **Production and Capacity:** EIM indicated that there are no capacity constraints and that the semiconductor situation has also improved.
- **Capex:** The company has no major capital expenditure plans. Capex for Hunter 350 will be limited as the components required for the Metro are sourced from the Retro, for which the company has already invested Rs 10mn-12mn.

**Fig 1 – Quarterly Result (Standalone)**

| (Rs mn)                      | Q2FY23        | Q2FY22        | YoY (%)      | Q1FY23        | QoQ (%)      | H1FY23        | H1FY22        | YoY (%)      |
|------------------------------|---------------|---------------|--------------|---------------|--------------|---------------|---------------|--------------|
| Volume                       | 207,564       | 123,427       | 68.2         | 187,205       | 10.9         | 394,769       | 247,067       | 59.8         |
| Avg. Realization per Vehicle | 163,670       | 176,777       | (7.4)        | 173,496       | (5.7)        | 168,330       | 165,530       | 1.7          |
| Net Revenues                 | 33,972        | 21,819        | 55.7         | 32,479        | 4.6          | 66,451        | 40,897        | 62.5         |
| <b>Total Income (A)</b>      | <b>33,972</b> | <b>21,819</b> | <b>55.7</b>  | <b>32,479</b> | <b>4.6</b>   | <b>66,451</b> | <b>40,897</b> | <b>62.5</b>  |
| <b>Operating Expenses:</b>   |               |               |              |               |              |               |               |              |
| Raw materials consumed       | 19,874        | 12,880        | 54.3         | 18,614        | 6.8          | 38,488        | 24,213        | 59.0         |
| Employee Expenses            | 2,277         | 1,629         | 39.7         | 2,323         | (2.0)        | 4,600         | 3,753         | 22.6         |
| Other Expenses               | 3,786         | 2,883         | 31.3         | 3,660         | 3.5          | 7,446         | 5,159         | 44.3         |
| <b>Total Expenditure (B)</b> | <b>25,936</b> | <b>17,392</b> | <b>49.1</b>  | <b>24,597</b> | <b>5.4</b>   | <b>50,534</b> | <b>33,126</b> | <b>52.6</b>  |
| <b>EBITDA (A-B)</b>          | <b>8,036</b>  | <b>4,427</b>  | <b>81.5</b>  | <b>7,882</b>  | <b>1.9</b>   | <b>15,918</b> | <b>7,772</b>  | <b>104.8</b> |
| Other Income                 | 1,534         | 1,123         | 36.6         | 928           | 65.3         | 2,462         | 2,462         | 0.0          |
| Depreciation                 | 1,251         | 1,082         | 15.6         | 1,142         | 9.5          | 2,393         | 2,187         | 9.4          |
| EBIT                         | 8,319         | 4,468         | 86.2         | 7,668         | 8.5          | 15,987        | 8,047         | 98.7         |
| Finance Costs                | 34            | 16            | 119.9        | 25            | 36.7         | 59            | 35            | 72.2         |
| PBT after excep items        | 8,285         | 4,452         | 86.1         | 7,643         | 8.4          | 15,928        | 8,013         | 98.8         |
| Tax expense                  | 1,865         | 1,018         | 83.2         | 1,841         | 1.3          | 3,707         | 1,907         | 94.4         |
| Reported PAT                 | 6,419         | 3,434         | 87.0         | 5,802         | 10.6         | 12,221        | 6,106         | 100.2        |
| <b>Adjusted PAT</b>          | <b>6,419</b>  | <b>3,434</b>  | <b>87.0</b>  | <b>5,802</b>  | <b>10.6</b>  | <b>12,221</b> | <b>6,106</b>  | <b>100.2</b> |
| Adj EPS (Rs)                 | 23.5          | 12.6          | 87.0         | 21.2          | 10.6         | 44.7          | 22.3          | 100.2        |
| <b>Key ratios (%)</b>        |               |               | <b>(bps)</b> |               | <b>(bps)</b> |               |               | <b>(bps)</b> |
| Gross Margin (%)             | 41.5          | 41.0          | 53           | 42.7          | (119)        | 42.1          | 40.8          | 129          |
| EBITDA Margin (%)            | 23.7          | 20.3          | 337          | 24.3          | (61)         | 24.0          | 19.0          | 495          |
| EBIT Margin (%)              | 24.5          | 20.5          | 401          | 23.6          | 88           | 24.1          | 19.7          | 438          |
| PBT Margin (%)               | 24.4          | 20.4          | 398          | 23.5          | 86           | 24.0          | 19.6          | 438          |
| Tax Rate (%)                 | 22.5          | 22.9          | (36)         | 24.1          | (158)        | 23.3          | 23.8          | (53)         |
| Adj PAT Margin (%)           | 18.9          | 15.7          | 316          | 17.9          | 103          | 18.4          | 14.9          | 346          |

## Valuation methodology

We expect EIM to clock a revenue, EBITDA and PAT CAGR of 23%, 33% and 35% respectively over FY22-FY25. Our FY24-FY25 earnings forecasts are ~5% below consensus due to lower volume assumptions and our EBITDA margins are 100bps below at ~26%. Our margin forecast represents ~600bps expansion by FY25 to bake in new high-end variants, export volumes and operating efficiencies.

However, we believe current valuations of 28x FY24E EPS capture the positives. We value EIM at 28x FY24E EPS (in line with its long-term average) and assign Rs 175/sh (average consensus value) to its VECV business, translating to a TP of Rs 3,543 – assume coverage with HOLD.

**Fig 2 – Key assumptions**

| (Rs mn)           | FY23E   | FY24E   | FY25E     |
|-------------------|---------|---------|-----------|
| Volume            | 888,000 | 967,200 | 1,033,200 |
| Revenue           | 144,350 | 165,600 | 186,678   |
| EBITDA            | 35,338  | 42,641  | 49,770    |
| EBITDA margin (%) | 24.5    | 26      | 27        |
| Adj. PAT          | 26,533  | 32,818  | 38,783    |
| EPS (Rs)          | 97      | 120     | 142       |

Source: Company, BOBCAPS Research

**Fig 3 – Valuation summary**

| Business            | Value (Rs/sh) | Comments        |
|---------------------|---------------|-----------------|
| Standalone business | 3,368         | 28x FY24E EPS   |
| VECV business       | 175           | Consensus value |
| <b>Total</b>        | <b>3,573</b>  |                 |

Source: BOBCAPS Research

## Key risks

Key upside risks to our estimates are:

- stronger-than-expected response to new model launches, and
- robust export revenue building up average selling price

Key downside risks:

- raw material cost remaining inflated/higher than estimates.

## Financials

### Income Statement

| Y/E 31 Mar (Rs mn)         | FY21A         | FY22A          | FY23E          | FY24E          | FY25E          |
|----------------------------|---------------|----------------|----------------|----------------|----------------|
| <b>Total revenue</b>       | <b>86,190</b> | <b>101,229</b> | <b>144,350</b> | <b>165,600</b> | <b>186,678</b> |
| EBITDA                     | 17,865        | 21,136         | 35,338         | 42,641         | 49,770         |
| Depreciation               | 4,460         | 4,455          | 4,900          | 5,273          | 5,813          |
| EBIT                       | 17,925        | 21,223         | 35,597         | 43,607         | 51,497         |
| Net interest inc./(exp.)   | (92)          | (103)          | (126)          | (139)          | (129)          |
| Other inc./(exp.)          | 4,520         | 4,543          | 5,160          | 6,239          | 7,540          |
| Exceptional items          | 0             | 0              | 0              | 0              | 0              |
| EBT                        | 17,833        | 21,121         | 35,471         | 43,468         | 51,368         |
| Income taxes               | 4,536         | 5,259          | 8,939          | 10,650         | 12,585         |
| Extraordinary items        | 0             | 0              | 0              | 0              | 0              |
| Min. int./Inc. from assoc. | 311           | (91)           | (100)          | 0              | 0              |
| <b>Reported net profit</b> | <b>13,608</b> | <b>15,772</b>  | <b>26,433</b>  | <b>32,709</b>  | <b>38,662</b>  |
| Adjustments                | 0             | 0              | 0              | 0              | 0              |
| <b>Adjusted net profit</b> | <b>13,608</b> | <b>15,772</b>  | <b>26,433</b>  | <b>32,709</b>  | <b>38,662</b>  |

### Balance Sheet

| Y/E 31 Mar (Rs mn)              | FY21A          | FY22A          | FY23E          | FY24E          | FY25E          |
|---------------------------------|----------------|----------------|----------------|----------------|----------------|
| Accounts payables               | 15,174         | 19,498         | 24,070         | 25,958         | 29,262         |
| Other current liabilities       | 8,216          | 8,911          | 6,314          | 8,633          | 9,563          |
| Provisions                      | 1,123          | 4,202          | 4,500          | 4,756          | 4,986          |
| Debt funds                      | 0              | 60             | 80             | 90             | 110            |
| Other liabilities               | 2,475          | 0              | 0              | 0              | 0              |
| Equity capital                  | 273            | 273            | 273            | 273            | 273            |
| Reserves & surplus              | 96,777         | 107,673        | 127,613        | 153,612        | 185,574        |
| Shareholders' fund              | 97,050         | 107,945        | 127,886        | 153,884        | 185,847        |
| <b>Total liab. and equities</b> | <b>124,038</b> | <b>140,617</b> | <b>162,850</b> | <b>193,321</b> | <b>229,768</b> |
| Cash and cash eq.               | 57,988         | 26,986         | 30,396         | 34,820         | 41,499         |
| Accounts receivables            | 2,562          | 4,929          | 5,413          | 6,210          | 7,000          |
| Inventories                     | 7,691          | 8,984          | 11,548         | 12,420         | 14,001         |
| Other current assets            | 8,474          | 13,400         | 15,012         | 16,560         | 18,668         |
| Investments                     | 20,448         | 59,500         | 69,500         | 91,500         | 116,500        |
| Net fixed assets                | 24,234         | 27,715         | 30,815         | 31,542         | 31,730         |
| CWIP                            | 3,102          | 1,334          | 2,500          | 2,750          | 2,975          |
| Intangible assets               | 0              | 0              | 0              | 0              | 0              |
| Deferred tax assets, net        | (2,210)        | (2,229)        | (2,335)        | (2,480)        | (2,604)        |
| Other assets                    | 1,750          | 0              | 0              | 0              | 0              |
| <b>Total assets</b>             | <b>124,038</b> | <b>140,618</b> | <b>162,850</b> | <b>193,321</b> | <b>229,768</b> |

### Cash Flows

| Y/E 31 Mar (Rs mn)                 | FY21A         | FY22A           | FY23E           | FY24E           | FY25E           |
|------------------------------------|---------------|-----------------|-----------------|-----------------|-----------------|
| <b>Cash flow from operations</b>   | <b>10,102</b> | <b>14,551</b>   | <b>23,659</b>   | <b>32,850</b>   | <b>36,790</b>   |
| Capital expenditures               | (4,987)       | (6,169)         | (9,166)         | (6,250)         | (6,225)         |
| Change in investments              | 18,808        | (39,052)        | (10,000)        | (22,000)        | (25,000)        |
| Other investing cash flows         | 4,520         | 4,543           | 5,160           | 6,239           | 7,540           |
| <b>Cash flow from investing</b>    | <b>18,342</b> | <b>(40,678)</b> | <b>(14,006)</b> | <b>(22,011)</b> | <b>(23,685)</b> |
| Equities issued/Others             | 660           | 161             | (161)           | 0               | 0               |
| Debt raised/repaid                 | 0             | 60              | 20              | 10              | 20              |
| Interest expenses                  | (92)          | (103)           | (126)           | (139)           | (129)           |
| Dividends paid                     | 0             | (4,647)         | (6,820)         | (6,820)         | (6,820)         |
| Other financing cash flows         | (310)         | 18              | 106             | 146             | 124             |
| <b>Cash flow from financing</b>    | <b>258</b>    | <b>(4,511)</b>  | <b>(6,980)</b>  | <b>(6,803)</b>  | <b>(6,805)</b>  |
| <b>Chg in cash &amp; cash eq.</b>  | <b>28,702</b> | <b>(30,638)</b> | <b>2,672</b>    | <b>4,036</b>    | <b>6,300</b>    |
| <b>Closing cash &amp; cash eq.</b> | <b>57,988</b> | <b>26,986</b>   | <b>30,396</b>   | <b>34,820</b>   | <b>41,499</b>   |

### Per Share

| Y/E 31 Mar (Rs)      | FY21A | FY22A | FY23E | FY24E | FY25E |
|----------------------|-------|-------|-------|-------|-------|
| Reported EPS         | 48.7  | 58.1  | 97.3  | 120.3 | 142.2 |
| Adjusted EPS         | 48.7  | 58.1  | 97.3  | 120.3 | 142.2 |
| Dividend per share   | 0.0   | 17.0  | 25.0  | 25.0  | 25.0  |
| Book value per share | 355.8 | 395.7 | 468.8 | 564.1 | 681.3 |

### Valuations Ratios

| Y/E 31 Mar (x) | FY21A | FY22A | FY23E | FY24E | FY25E |
|----------------|-------|-------|-------|-------|-------|
| EV/Sales       | 10.3  | 8.6   | 6.1   | 5.5   | 4.8   |
| EV/EBITDA      | 49.7  | 41.1  | 25.0  | 21.4  | 17.9  |
| Adjusted P/E   | 69.6  | 58.3  | 34.9  | 28.2  | 23.8  |
| P/BV           | 9.5   | 8.6   | 7.2   | 6.0   | 5.0   |

### DuPont Analysis

| Y/E 31 Mar (%)               | FY21A       | FY22A       | FY23E       | FY24E       | FY25E       |
|------------------------------|-------------|-------------|-------------|-------------|-------------|
| Tax burden (Net profit/PBT)  | 74.6        | 75.1        | 74.8        | 75.5        | 75.5        |
| Interest burden (PBT/EBIT)   | 99.5        | 99.5        | 99.6        | 99.7        | 99.7        |
| EBIT margin (EBIT/Revenue)   | 20.8        | 21.0        | 24.7        | 26.3        | 27.6        |
| Asset turnover (Rev./Avg TA) | 93.7        | 97.6        | 122.3       | 117.5       | 109.8       |
| Leverage (Avg TA/Avg Equity) | 1.0         | 1.0         | 1.0         | 1.0         | 1.0         |
| <b>Adjusted ROAE</b>         | <b>14.8</b> | <b>15.5</b> | <b>22.5</b> | <b>23.3</b> | <b>22.8</b> |

### Ratio Analysis

| Y/E 31 Mar                                   | FY21A      | FY22A      | FY23E      | FY24E      | FY25E      |
|--|------------|------------|------------|------------|------------|
| <b>YoY growth (%)</b>                        |            |            |            |            |            |
| Revenue                                      | (5.1)      | 17.4       | 42.6       | 14.7       | 12.7       |
| EBITDA                                       | (18.9)     | 18.3       | 67.2       | 20.7       | 16.7       |
| Adjusted EPS                                 | (30.2)     | 19.3       | 67.3       | 23.7       | 18.2       |
| <b>Profitability &amp; Return ratios (%)</b> |            |            |            |            |            |
| EBITDA margin                                | 20.7       | 20.9       | 24.5       | 25.7       | 26.7       |
| EBIT margin                                  | 20.8       | 21.0       | 24.7       | 26.3       | 27.6       |
| Adjusted profit margin                       | 15.8       | 15.6       | 18.3       | 19.8       | 20.7       |
| Adjusted ROAE                                | 14.0       | 14.6       | 20.7       | 21.3       | 20.8       |
| ROCE   | 14.5       | 15.4       | 22.6       | 23.4       | 22.9       |
| <b>Working capital days (days)</b>           |            |            |            |            |            |
| Receivables                                  | 8          | 14         | 13         | 13         | 13         |
| Inventory                                    | 27         | 30         | 26         | 26         | 26         |
| Payables                                     | 91         | 106        | 96         | 97         | 95         |
| <b>Ratios (x)</b>                            |            |            |            |            |            |
| Gross asset turnover                         | 0.5        | 0.5        | 0.4        | 0.4        | 0.4        |
| Current ratio                                | 3.1        | 1.7        | 1.8        | 1.8        | 1.9        |
| Net interest coverage ratio                  | 194.8      | 207.1      | 282.5      | 313.7      | 399.2      |
| <b>Adjusted debt/equity</b>                  | <b>0.0</b> | <b>0.0</b> | <b>0.0</b> | <b>0.0</b> | <b>0.0</b> |

Source: Company, BOBCAPS Research | Note: TA = Total Assets

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### Recommendation scale: Recommendations and Absolute returns (%) over 12 months

**BUY** – Expected return >+15%

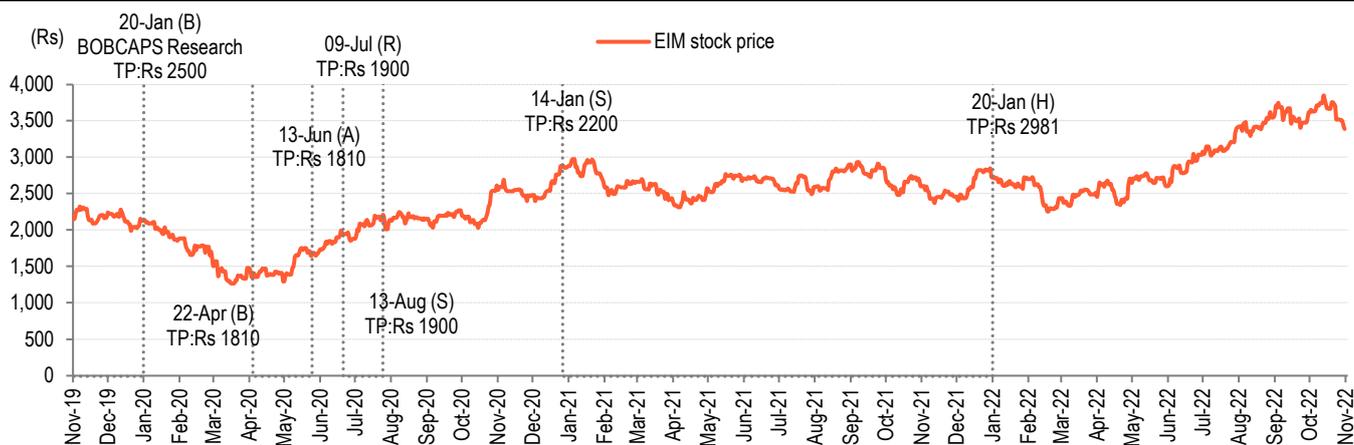
**HOLD** – Expected return from -6% to +15%

**SELL** – Expected return <-6%

**Note:** Recommendation structure changed with effect from 21 June 2021

Our recommendation scale does not factor in short-term stock price volatility related to market fluctuations. Thus, our recommendations may not always be strictly in line with the recommendation scale as shown above.

### Ratings and Target Price (3-year history): EICHER MOTORS (EIM IN)



B – Buy, H – Hold, S – Sell, A – Add, R – Reduce

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