



**HDFC securities**

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20

**Fundamental Research Analyst**

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PCG DESK

Industry	CMP	Recommendation	Add on dips to	Sequential Targets	Time Horizon
Industrial Machinery	Rs. 160	Buy at CMP and add on declines	Rs. 145-160	Rs. 185-208	4 Quarters

HDFC Scrip Code	GRELTD
BSE Code	501455
NSE Code	GREAVESCOT
Bloomberg	GRV IN
CMP as on 14 Jul 2017	160
Equity Capital (Rs Cr)	48.84
Face Value (Rs)	2
Equity O/S (Cr)	24.42
Market Cap (Rs Cr)	3,907
Book Value (Rs)	38
Avg. 52 Week Volumes	398338
52 Week High	178
52 Week Low	115

Incorporated in 1859, Greaves Cotton Limited is one of India's leading and well-diversified engineering companies with core competencies in diesel/ petrol engines, farm equipment, gensets and Pumpsets. The Company sustains its leadership through 11 manufacturing units which produce world class products backed by comprehensive marketing and service / parts network. Further, company exports to Middle East, Africa and South East Asia region.

The engine business accounted for 55-60% of total sales, farm segment accounted for 12-13%, genset and others accounted for 10-12% and the balance from aftermarket sales.

Previously also we have recommended. But looking at the current price and expected earnings we reinitiate Greaves Cotton a BUY at CMP of Rs. 160 and add on decline of Rs. 145 for the targets of Rs. 185 and Rs. 208 for the time Frame of over the next 4 Quarters.

Shareholding Pattern (%)	
Promoters	51.0
Institutions	33.5
Non Institutions	15.5

PCG Risk Rating*	Yellow
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\* Refer Rating explanation

## Investment Rational:

**Sustainable Growth:** Despite Average Monsoon of last 3 years Greaves Cotton has managed to sustain its revenues, profitability and cash flows. With expectations of good monsoon and robust economic growth ahead, we believe Greaves Cotton is all set to move to higher level of growth trajectory.

**Diversifying into new areas:** Greaves Cotton has diversified itself into new business segments such as aftermarket business and farm equipment business for more growth opportunities and also insulating the core auto engine business, in case of any slowdown. Company is also trying to grow its space region wise by adding newer geographies and customers internationally. We see this as the positive step of the company towards its bright future.

**Aftermarket Sales** (Also known as the spare-parts business): The company has strong pan India sales and distribution network (3000 Service outlets along with 1200 dealers) through which it is leveraging its infrastructure and gets into multi brand outlets. Apart from its own products this outlet sells spare parts of other companies. The addressable market is about Rs 1400 Cr. This is also a high margin business, we see immense opportunities in this segment going forward.

**Strong Balance Sheet:** Consistent earning has made company a debt free company. Operating cash flow has grown at 19% over last 5 years. Company has reported average RoE of 18% over the same period. Pay Out ratio of Greaves Cotton is excellent - average 45-50%, making the dividend yield of around ~3.4%. We expect the company to perform at robust pace going further also and keep on rewarding its shares holders with healthy return on equity and dividends.

**Challenges overdone:** In the last year Greaves Cotton has faced many changes like Demonetization and implementation of BS IV. However the effect of demonetization has faded away and company has also under gone price hike of 8-10% on overall basis for reducing effect of BS IV implementation.

***Technology partnership with US based Pinnacle Engines:***

Company has always been trying to develop its horizon in other market also and recently in June 2017, Greaves Cotton and US-based Pinnacle Engines Inc. announced technology partnership for the launch of a revolutionary Opposed Piston Petrol/CNG lean burn BS VI - compliant engine for 3-wheelers in India. As per the agreement, Pinnacle will grant license to Greaves Cotton for manufacturing and selling 3-wheel Pinnacle Engines and 2 Wheel (110 CC) Pinnacle Engines.

This move is seen as an important milestone for Greaves to establish itself as a leading fuel agnostic powertrain solutions & services company. This also allows Greaves access to export markets with large 3-wheeler population.

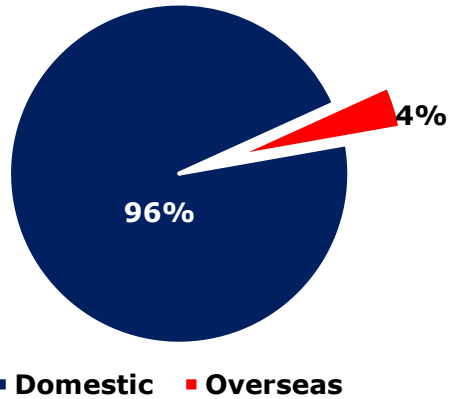
### **Valuation:**

Previously, we had recommended Greaves Cotton as a BUY in the range of Rs 136-125 with the targets of Rs 155 and Rs 170.

[https://www.hdfcsec.com/uat.hsl.research.pdf/HSL%20PCG%20Greaves%20Cotton%20May16\\_20160524130457.pdf](https://www.hdfcsec.com/uat.hsl.research.pdf/HSL%20PCG%20Greaves%20Cotton%20May16_20160524130457.pdf)

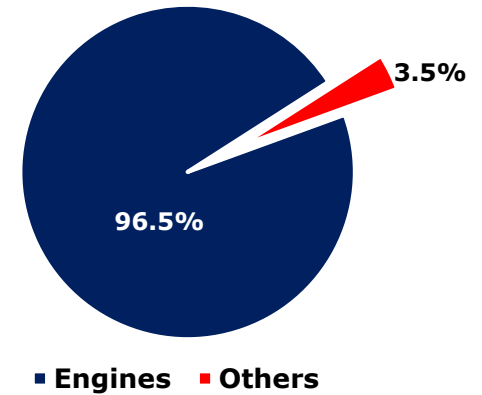
Good monsoon, positive macro environment, company's diversification strategy etc. are the key positives triggers for the company. We expect Topline to post CAGR of 12% and Bottom line at 13% CAGR for the period of FY17-19E. Margin is estimated to jump 210 bps till FY19E from 14.7% of FY17P. Return ratio is also estimated to remain at the robust level of around 25-28%. Currently stock is trading at 16.9x on FY19E earnings. We recommend Greaves Cotton a BUY at CMP of Rs. 160 and add on decline of Rs. 145 for the targets of Rs. 185 and Rs. 208 for the time Frame of over the next 4 Quarters.

**Revenue Contribution**



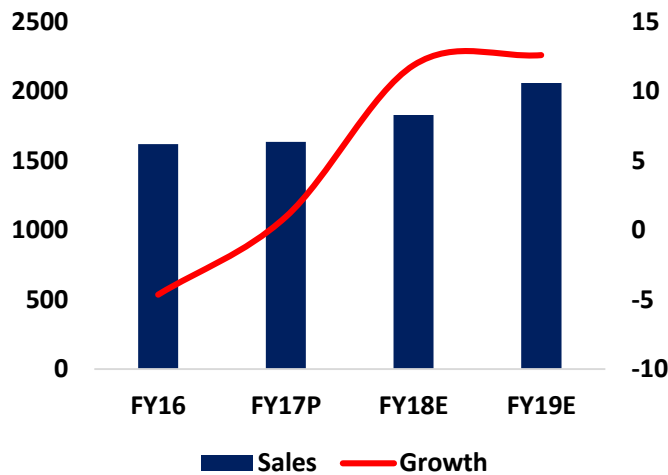
Source: Company, HDFC sec Research

**Revenue Contribution Segmentwise**



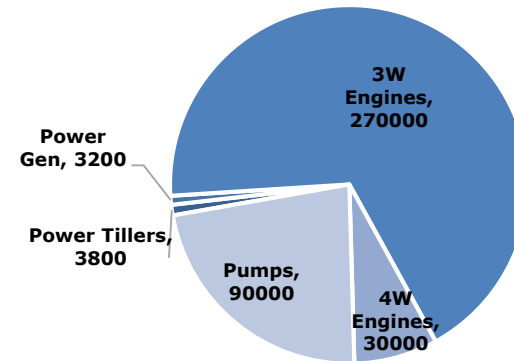
Source: Company, HDFC sec Research

**Revenues Trajectory**



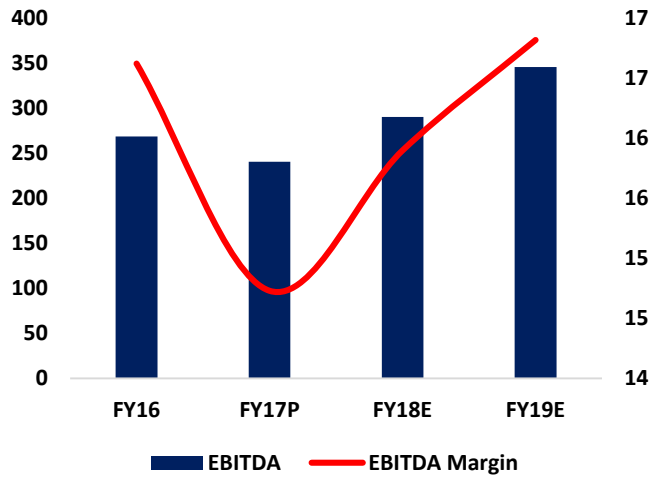
Source: Company, HDFC sec Research

**FY17 Volume Break-up**



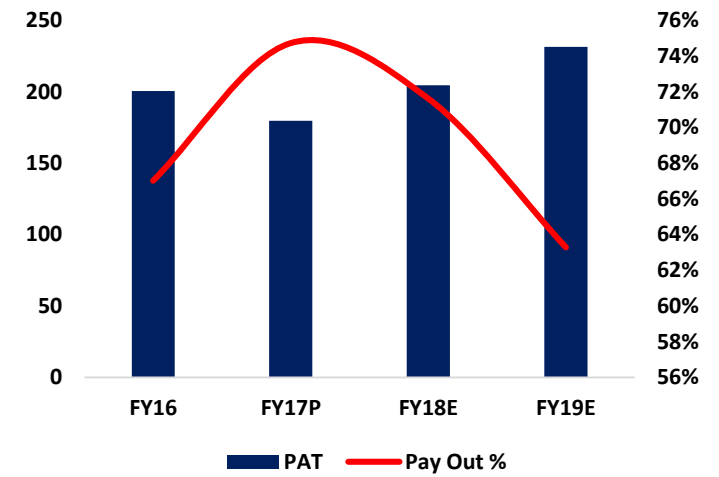
Source: Company, HDFC sec Research

## After market Sales to aid higher Margin



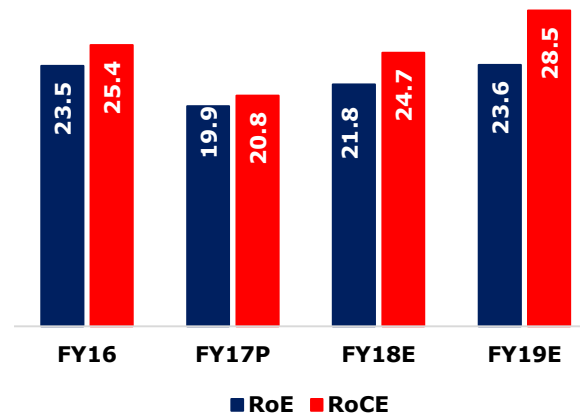
Source: Company, HDFC sec Research

## PAT and Pay Out Ratio



Source: Company, HDFC sec Research

## Robust return ratios



Source: Company, HDFC sec Research

**Income Statement (Consolidated)**

(Rs Cr)	FY15	FY16	FY17P	FY18E	FY19E
<b>Net Revenue</b>	<b>1697.7</b>	<b>1618.9</b>	<b>1634.4</b>	<b>1828.4</b>	<b>2058.8</b>
<b>Growth (%)</b>	<b>-2.2</b>	<b>-4.6</b>	<b>1.0</b>	<b>11.9</b>	<b>12.6</b>
Operating Expenses	1498.6	1349.7	1393.7	1537.7	1712.5
<b>EBITDA</b>	<b>199.1</b>	<b>269.1</b>	<b>240.8</b>	<b>290.7</b>	<b>346.3</b>
<b>Growth (%)</b>	<b>6.1</b>	<b>35.2</b>	<b>-10.5</b>	<b>20.8</b>	<b>19.1</b>
<b>EBITDA Margin (%)</b>	<b>11.7</b>	<b>16.6</b>	<b>14.7</b>	<b>15.9</b>	<b>16.8</b>
Depreciation	47.7	45.7	46.9	52.0	58.3
EBIT	151.4	223.4	193.9	238.7	288.0
Net Operating Income	-38.1	70.8	56.5	60.0	50.0
Interest	2.4	1.0	0.8	0.0	0.0
<b>PBT</b>	<b>111.0</b>	<b>293.2</b>	<b>249.5</b>	<b>298.7</b>	<b>338.0</b>
Tax	27.3	92.7	69.8	94.1	106.5
<b>RPAT</b>	<b>83.6</b>	<b>200.4</b>	<b>179.8</b>	<b>204.6</b>	<b>231.5</b>
<b>Growth (%)</b>	<b>-32.2</b>	<b>139.6</b>	<b>-10.3</b>	<b>13.8</b>	<b>13.1</b>
EPS	3.4	8.2	7.4	8.4	9.5

Source: Company, HDFC sec Research

Note: Financials for FY16 onwards are based on Ind-AS and hence FY15 numbers are not strictly comparable.

**Balance Sheet (Consolidated)**

(Rs Cr)	FY15	FY16	FY17P	FY18E	FY19E
<b>SOURCE OF FUNDS</b>					
Share Capital	49	49	49	49	49
Reserves	774	842	876	908	965
<b>Shareholders' Funds</b>	<b>823</b>	<b>891</b>	<b>925</b>	<b>957</b>	<b>1014</b>
Total Debt	0	0	0	0	0
Net Deferred Taxes	13	8	10	11	11
Long Term Provisions & Others	14	19	17	20	15
<b>Total Source of Funds</b>	<b>850</b>	<b>918</b>	<b>953</b>	<b>988</b>	<b>1040</b>
<b>APPLICATION OF FUNDS</b>					
Net Block	335	312	303	351	373
Long Term Loans & Advances	33	12	17	17	17
Non-Current Investments	0	255	272	270	270
Deferred Tax Asset(Net)	0	19	19	19	19
<b>Total Non Current Assets</b>	<b>367.6</b>	<b>598.8</b>	<b>610.4</b>	<b>656.5</b>	<b>678.1</b>
Investment	293	106	139	115	101
Inventories	106	108	129	143	161
Trade Receivables	231	201	270	276	327
Cash & Equivalent	36	8	10	30	19
Other Current Assets	91	160	84	88	93
<b>Total Current Assets</b>	<b>757</b>	<b>582</b>	<b>633</b>	<b>652</b>	<b>701</b>
Trade Payables	146	32	31	33	38
Other Current Liab & Provisions	128	228	260	286	301
<b>Total Current Liabilities</b>	<b>274.3</b>	<b>259.5</b>	<b>290.8</b>	<b>320</b>	<b>339</b>
Net Current Assets	<b>482.5</b>	<b>323.0</b>	<b>342.2</b>	332	362
<b>Total Application of Funds</b>	<b>850.0</b>	<b>917.8</b>	<b>952.6</b>	<b>988</b>	<b>1040</b>

Source: Company, HDFC sec Research

**Cash Flow Statement (Consolidated)**

(Rs Cr)	FY15	FY16	FY17P	FY18E	FY19E
Reported PBT	111.0	293.2	249.5	298.7	338.0
Non-operating & EO items	-47.7	-34.5	-47.4	-60.0	-50.0
Interest Expenses	2.4	1.0	0.8	0.0	0.0
Depreciation	47.7	45.7	46.9	52.0	58.3
Working Capital Change	-43.0	151.9	-20.5	33.7	-46.4
Tax Paid	-27.3	-92.7	-69.8	-94.1	-106.5
<b>OPERATING CASH FLOW ( a )</b>	<b>42.9</b>	<b>364.5</b>	<b>159.6</b>	<b>230.3</b>	<b>193.5</b>
Capex	8.6	-23.0	-37.9	-100.0	-80.0
Free Cash Flow	51.5	341.5	121.7	130.3	113.5
Investments	0.0	-255.5	-16.5	1.9	0.0
Non-operating income	24.9	45.5	56.5	60.0	50.0
<b>INVESTING CASH FLOW ( b )</b>	<b>33.5</b>	<b>-233.0</b>	<b>2.2</b>	<b>-38.1</b>	<b>-30.0</b>
Debt Issuance / (Repaid)	0.0	0.0	0.0	0.0	0.0
Interest Expenses	-2.4	-1.0	-0.8	0.0	0.0
FCFE	49.1	340.5	120.9	130.3	113.5
Share Capital Issuance	0.0	0.0	0.0	0.0	0.0
Dividend	-72.5	-158.5	-158.5	-172.9	-174.4
<b>FINANCING CASH FLOW ( c )</b>	<b>-74.9</b>	<b>-159.5</b>	<b>-159.3</b>	<b>-172.9</b>	<b>-174.4</b>
<b>NET CASH FLOW (a+b+c)</b>	<b>1.6</b>	<b>-27.9</b>	<b>2.4</b>	<b>19.4</b>	<b>-10.9</b>
Closing Cash	35.8	7.8	10.2	29.6	19.1

Source: Company, HDFC sec Research

**Key Ratios**

Key Ratios (%)	FY15	FY16	FY17P	FY18E	FY19E
EBITDA Margin	11.7	16.6	14.7	15.9	16.8
EBIT Margin	8.9	13.8	11.9	13.1	14.0
PAT Margin	4.9	12.4	11.0	11.2	11.2
RoE	10.2	23.5	19.9	21.8	23.6
RoCE	17.7	25.4	20.8	24.7	28.5
Net D/E	0.0	0.0	0.0	0.0	0.0
<b>PER SHARE DATA</b>					
EPS	3.4	8.2	7.4	8.4	9.5
CEPS	5.4	10.1	9.3	10.5	11.9
BV	33.5	36.3	37.7	39.0	41.4
Dividend	2.5	5.5	5.5	6.0	6.0
<b>Turnover Ratios (days)</b>					
Debtor days	59.9	48.7	52.6	54.5	53.4
Inventory days	29.0	24.2	26.5	27.2	26.9
Creditors days	57.0	32.7	11.5	10.5	10.4
Working capital days	31.9	40.2	67.6	71.1	70.0
<b>VALUATION</b>					
P/E	46.7	19.5	21.7	19.1	16.9
P/BV	4.8	4.4	4.2	4.1	3.9
EV/EBITDA	19.5	14.4	16.1	13.4	11.2
EV / Revenues	2.3	2.4	2.4	2.1	1.9
Dividend Yield (%)	1.6	3.4	3.4	3.8	3.8

Source: Company, HDFC sec Research



**Rating Chart**

R E T U R N	HIGH			
	MEDIUM			
	LOW			
		LOW	MEDIUM	HIGH
		RISK		

**Ratings Explanation:**

RATING	Risk - Return	BEAR CASE	BASE CASE	BULL CASE
BLUE	LOW RISK - LOW RETURN STOCKS	IF RISKS MANIFEST PRICE CAN FALL 20% OR MORE	IF RISKS MANIFEST PRICE CAN FALL 15% & IF INVESTMENT RATIONALE FRUCTFIES PRICE CAN RISE BY 15%	IF INVESTMENT RATIONALE FRUCTFIES PRICE CAN RISE BY 20% OR MORE
YELLOW	MEDIUM RISK - HIGH RETURN STOCKS	IF RISKS MANIFEST PRICE CAN FALL 35% OR MORE	IF RISKS MANIFEST PRICE CAN FALL 20% & IF INVESTMENT RATIONALE FRUCTFIES PRICE CAN RISE BY 30%	IF INVESTMENT RATIONALE FRUCTFIES PRICE CAN RISE BY 35% OR MORE
RED	HIGH RISK - HIGH RETURN STOCKS	IF RISKS MANIFEST PRICE CAN FALL 50% OR MORE	IF RISKS MANIFEST PRICE CAN FALL 30% & IF INVESTMENT RATIONALE FRUCTFIES PRICE CAN RISE BY 30%	IF INVESTMENT RATIONALE FRUCTFIES PRICE CAN RISE BY 50% OR MORE



**Rating Definition:**

Buy: Stock is expected to gain by 10% or more in the next 1 Year.

Sell: Stock is expected to decline by 10% or more in the next 1 Year.

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