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20
YEARS

Initiating Coverage Eicher Motors Ltd.

28-December-2020





Industry	LTP	Recommendation	Base Case Fair Value	Bull Case Fair Value	Time Horizon
Automobile – 2W/CV	Rs 2437	Buy at LTP and add on dips to Rs 2155-2169 band	Rs 2751	Rs 2948	2 quarters

HDFC Scrip Code	EICMOT
BSE Code	505200
NSE Code	EICHERMOT
Bloomberg	EIM IN
CMP Dec 24, 2020 (Rs)	2436.8
Equity Capital (cr)	27.3
Face Value (Rs)	1
Eq. Share O/S (cr)	27.3
Market Cap (Rs cr)	66432.6
Book Value (Rs)	365.6
Avg.52 Wk Volume	650,000
52 Week High (Rs)	2715.0
52 Week Low (Rs)	1245.0

Share holding Pattern % (Sep, 2020)	
Promoters	49.25
Institutions	38.25
Non Institutions	12.50
Total	100.0

Fundamental Research Analyst

Atul Karwa

atul.karwa@hdfcsec.com

Our Take:

Eicher Motors Ltd. (EML) with a strong established brand ‘Royal Enfield’ has a strong product portfolio and a long operational track record. It has a loyal base of customers and is the market leader in the addressable segment (more than 95% market share in the over 250-cc sub-segment) of the Indian two-wheeler industry. The company had invested significantly in its motorcycle business over the past five years for setting up new manufacturing facilities and new product developments; the same were entirely funded through internal accruals. Its debt free and cash rich balance sheet provides adequate liquidity to meet its future capex requirement through internal accruals and available cash balances.

Although the company has had limited presence in the export market for its motorcycles business, the latest addition of 650cc ‘Twins’ to its portfolio (launched in H2FY19) has received a favourable response and has already started aiding in growing the export volumes as reflected in the 96% YoY growth in FY20, albeit on a low base. However, the increasing competition in the mid-size motorcycles segment as evident from recent launches as well as their partnerships with their Indian counterparts, could pose a threat to its sustained dominance over the medium to long term.

The commercial vehicle business has been able to largely maintain its market position in the industry amid industry headwinds on the back of continuous product launches/refreshes, expanding dealer network and targeted marketing efforts over the past few years. The Government’s thrust on infrastructure projects, coupled with the potential implementation of fleet modernisation or scrappage programme, will support demand.

Valuations & Recommendation:

Eicher Motor is a structural story on premiumisation theme in motorcycles. In the M&HCV space, it is well poised to break the duopoly of Tata Motors and Ashok Leyland. Strong execution track record coupled with superior balance sheet provides additional comfort. We expect 4.6% CAGR in revenues over FY20-FY22 driven by 6.2% CAGR growth in realisations. Volumes are expected to decline by 1.1% CAGR as the Covid pandemic would delay discretionary spending by consumers. PAT is expected to grow by 8.4% CAGR on back of demand revival in the CV business. New product launches, network expansion, strong orderbook and possibility of a pick-up in CV cycle all bode



well for EML. Investors can buy the stock at the LTP (31.0x FY22E EPS) and add further on declines to Rs 2155-2169 band (27.5x FY22E EPS) for a base fair value of Rs 2751 (35.0x FY22E EPS) and bull case fair value is Rs 2948 (37.5x FY22E EPS) over the next two quarters.

Financial Summary

(Rs cr)	Q2FY21	Q2FY20	YoY-%	Q1FY21	QoQ-%	FY19	FY20	FY21E	FY22E
Revenues	2133.6	2192.5	-2.7	818.2	160.8	9797.1	9153.6	8225.3	10013.0
EBITDA	471.1	541.4	-13.0	3.8	12328.8	2903.1	2180.4	1802.0	2468.8
APAT	343.3	517.9	-33.7	-55.2	LP	2220.3	1827.5	1463.8	2146.1
Diluted EPS (Rs)	12.6	19.0	-33.7	-2.0	LP	81.4	66.9	53.6	78.6
RoE (%)						24.7	18.3	13.2	16.7
P/E (x)						29.9	36.4	45.4	31.0
EV/EBITDA (x)						17.6	21.3	24.3	18.0

(Source: Company, HDFC sec)

Recent Triggers

Q2FY21 Financials

Eicher reported Q2FY21 consolidated revenues of Rs 2,134cr down 2.7% yoy. Volumes for RE (Royal Enfield) at ~150k units declined 10% YoY. However, the realisations grew ~8% yoy to Rs 141k, owing to better product mix and price hike taken in Sep-20. EBITDA margin at 22.8% was up sharply qoq, (-220bps yoy). PAT declined 36% yoy to Rs 361cr, owing to a lower tax rate in the base quarter. Consolidated PAT declined 34% yoy to Rs 343cr.

Commercial Vehicle JV volumes/revenue declined 28/13% yoy. Margin at 6.9% surprised positively due to higher realisation and cost savings. Loss reduced to Rs 7cr (vs a loss of Rs 120cr qoq).

RE Orderbook is at 125000 including 8000 for the recently launched Meteor.

VECV sales volumes rose 12.2% and 3.2% YoY in Oct 2020 and Nov 2020 respectively. RE sales volumes fell 7% YoY and rose 5.6% YoY in Oct 2020 and Nov 2020 respectively.



New product launch

The OEM has rolled out the 'Meteor 350cc' on a new platform along with personalisation options (MIY), which is expected to be a 'differentiator'. The new launch comes at a time when the competition is increasing – the Honda H'ness CB350 has just been launched. The newly launched Meteor has secured 8k bookings. As per management, the vehicle personalisation option (MIY) is a significant differentiator and has been well accepted by customers. RE plans to launch a revamped model on its new platform every quarter.

Increased demand penetration

Expansion of studio stores (133 opened in Q2, total ~770 stores) has led to demand penetration, especially in tier-II and III cities. Demand in urban cities is now picking up. Bookings in Oct-20 exceeded that of the previous year and currently stand at 125k units.

- While RE has a capacity of 10 lakh units, the OEM is facing constraints for specific models or due to bottlenecks from the vendor's side. The company produced 72k units in Oct-20.
- VECV volumes were down 28% in Q2 (sharply higher QoQ). The industry is witnessing signs of improvement, led by a ramp-up in constructions/mining activities.

Long term Triggers

Established leadership and niche brand positioning in over 250cc segment

EML's RE reported annual global sales of 69.6 lakh motorcycles in FY20 (against 82.4 lakh in FY19) and maintained its leadership position with more than 95% market share in the over 250-cc displacement sub-segment of motorcycles in India. The niche positioning along with aspirational and iconic status of the brand has helped it in garnering volumes and outperform the motorcycle industry over the past many years. As a result, the company's volumes grew at a CAGR of ~26% between FY2015 to FY2019; albeit on a low base. In the 125cc+ motorcycle segment in India its market share stood at 26.6%. Despite the increasing competition from domestic and international OEMs, EML is expected to maintain its stronghold in the target sub-segment over the medium term, backed by its strong brand and value proposition, established track record in the Indian market and after-sales service network. Furthermore, increasing export volumes, although marginal at present, are expected to increasingly support overall volume growth. Its total dealer touch points in international markets as on FY20 stood at 660 stores with presence across Thailand, Brazil, Argentina, France and UK.



CV JV was hit by slowdown in FY20



(Source: Company, HDFC sec)

Expanding product range and improving technical capability

Regular new launches and product variations underpins EML's technical prowess. With Himalayan (launched in 2016) and recent launches Continental GT 650 as well as Interceptor 650 (the 'twins' in FY2019), it has demonstrated its capability to build new models from the ground up, incorporating new engine as well as body structure. This has given the existing RE users a chance to upgrade and has resulted in an opportunity to ramp up its export volumes.



Royal Enfield range of motorcycles – traditional to urban aspiration

Bullet	Classic	Meteor 350	Himalayan	Continental GT 650	Interceptor 650
<ul style="list-style-type: none"> Longest production motorcycle Resolute, unchanged form Pride of the armed forces Iconic cues – thump, pinstripes, road presence 	<ul style="list-style-type: none"> Sense of distinctiveness Post-war styling Timeless design 	<ul style="list-style-type: none"> Easy cruiser with British aesthetic and timeless charm Comfortable riding position with easy handling ability High torque and smooth power delivery 	<ul style="list-style-type: none"> Purpose-built and adventure tourer Versatile for riding on- and off-road Fully ground-up with all-new engine Touring capabilities 	<ul style="list-style-type: none"> Authentic café racer Powered by modern Twin cylinder engine Perfect for high speed blasts on twisty backroads or as a stylish motorcycle for the city 	<ul style="list-style-type: none"> The quintessential roadster with commanding and comfortable riding position Powered by modern twin cylinder engine Fun and practical to ride in almost all terrains
<p>Traditional and Iconic ←</p>			<p>→ Urban, Lifestyle and now Adventure</p>		

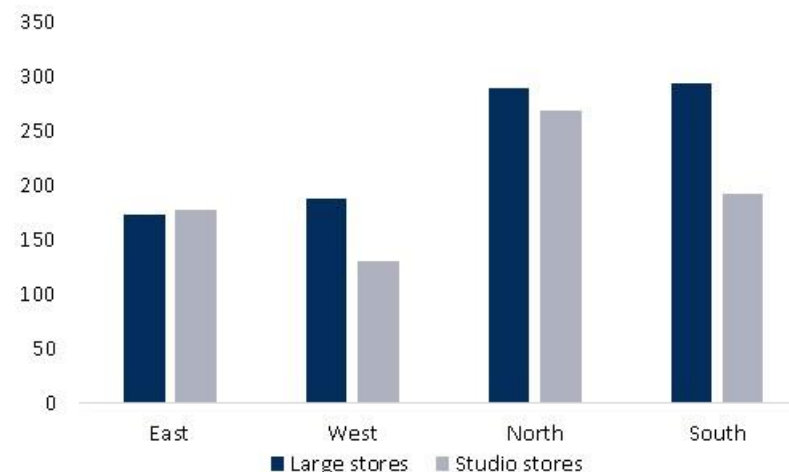
(Source: Company)

Enhancing domestic as well as global distribution network

Royal Enfield is rapidly expanding its presence in the domestic as well as global arena with its new differentiated range of evocative, accessible and truly global line of motorcycles. Its large format stores have grown from 527 in FY16 to 946 in Q2FY21. As the company

expands to capture the audience from Tier 2, 3 and 4 cities/towns, it has adopted a strategy to open studio stores. These studio stores typically measure ~500 sq.ft. (225 sqft of retail space and 275 sqft of workshop area) as compared to ~2000 sq.ft. for a large store. As of Q2FY21 the company had 771 studio and it had plans to expand studio stores to 1200 by end of FY21. The strategy of adding studio stores would give a wider reach to the company at a relatively lower costs and capture the growing demand of premium bikes in smaller cities/towns.

Expanding its pan-India network



(Source: Company, HDFC sec)

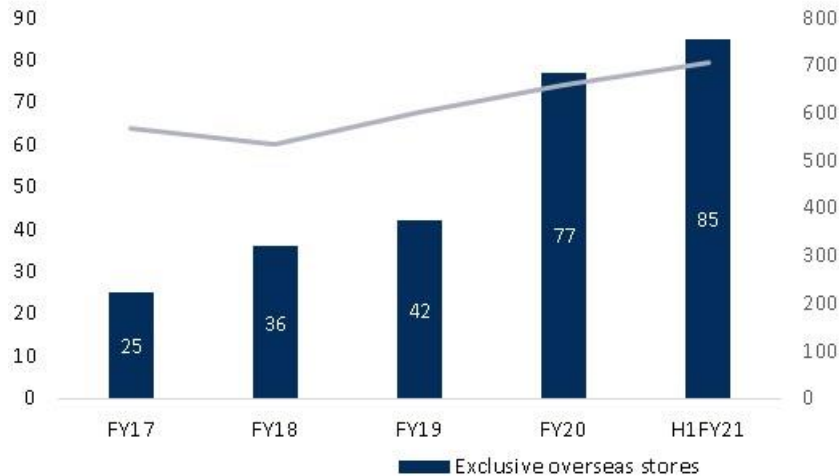
EML has been steadily working towards expanding its “Pure Motorcycling” experience across the globe and aims to lead and expand the mid-weight (250-750cc) motorcycle segment. It is working on strengthening its brand positioning by developing a world-class product portfolio, building a widespread distribution network, executing differentiated branding activities and setting up local operations. Sales volumes from overseas markets doubled from 19,721 in 2018-19 to 38,662 in 2019-20. Its exclusive stores have increased from 12 in FY16



to 85 in Q2FY21 with plans to increase to 100 stores by end of FY21. Royal Enfield now features among the Top 5 brands, in terms of volumes, in the middleweight segment in Thailand, Australia-New Zealand and South Korea.

RE's exports grew by ~100% in FY20 to ~39000 units (more than double of that in FY19) on the back of new 650 Twins. It is expected to grow further with new launches such as Meteor with international product quality.

Increasing overseas presence



(Source: Company, HDFC sec)

Growing trend of premium bike to benefit EML

India's premium motorcycles market witnessed a major turnaround with rapid increase in demand for premium motorcycles over the last few years. Rising number of high net worth Individuals coupled with an increasing number of premium motorcycle players focusing on setting up domestic production or assembly units in India are the major factors expected to drive the country's premium motorcycles market over the next five years.



The share of premium segment has increased over the years from ~15% in FY14 to ~22.7% in FY20. It reached a high of 23.7% in FY19 but the economic slowdown led to a drop of ~100bps in market share. EML with most of its portfolio coming under premium segment would be a key beneficiary of this trend.

Capitalizing the loyal base for branding and marketing

Royal Enfield has a strong fan following in India and the company is capitalizing its loyal base to improve its branding. Its motorcycles have a cult following and EML keeps organizing events to build a Royal Enfield community which makes owning the motorcycle a prestigious thing for the riders. Customers go on long adventurous trip with fellow Royal Enfield owners which inculcate a sense of belonging and pride among the motorcycle enthusiasts. Rider Mania is an annual event hosted by Brotherhood of Bulleteers Motorcycling Consortium (BOBMC) member clubs for Royal Enfield motorcycle owners attracted 8,000 enthusiasts from across the world in 2019.

The company also offers customization options and accessories to further nurture the spirit of motorcycle personalization. Motorcycle accessories are now firmly part of the customer proposition and every product is co-designed with the motorcycle itself and tested extensively in parallel. It has also launched its own apparel brand in order to provide a full range of apparel to its consumers for their lifestyle and riding needs.

Scrappage policy implementation could prop up demand for commercial vehicles

The government on July 26, 2019 had proposed amendments to motor vehicle norms to allow scrapping of vehicles older than 15 years in a bid to spur adoption of electrical vehicles and eliminating the fleet of old polluting commercial vehicles plying on the country's roads. The policy is awaiting final clearance from the Union Cabinet. EML which has a JV with Sweden's AB Volvo to manufacture light and medium duty trucks (4.9-15 tonnes), heavy duty trucks (16-55 tonnes) and buses (12-62 seats) is likely to benefit from the implementation of the policy. It is a market leader in light and medium duty truck segment with 29.5% market share.

VECV was the first company in the CV Industry to migrate to BS VI norms well before the mandated timeline as it was supplying Euro 6 compliant engines to Volvo. It has an edge over competitors in handling the challenges posed by the BS VI technology. It has launched Pro 2000 series range of light and medium duty trucks with many industry-first features. Volvo trucks are known for enhanced reliability, safety, comfort and efficiency.



The CV JV segment was witnessing strong growth till FY19. However, the slowdown of FY20 and the Covid pandemic has resulted in sharp de-growth in CV sales. However with the government focusing on improving infrastructure we expect CV sales to pick up going forward.

CV JV was hit by slowdown in FY20



(Source: Company, HDFC sec)

Strong financial risk profile

EML has a strong financial risk profile with debt of just ~Rs 150cr. It had liquid investment in mutual funds worth Rs 2512cr as of FY20. The company has sizeable cash and liquid investments vis-à-vis capex and working capital requirements. Despite the slowdown, return ratios continue to remain strong with RoE at 18.3% and RoCE at 22.6% in FY20. All its funding requirements have been met through internal accruals and are expected to be similarly funded, going forward. Healthy accruals from the business coupled with negligible debt obligations and a favourable working capital cycle, have led to a strong liquidity profile, despite large capex undertaken in the last few years.



What could go wrong

Entry of new players in the premium motorcycle segment

With the increasing trend of premiumisation of motorcycles in India, many global OEMs have been forging partnerships with local players to develop mid-size motorcycles (250-500cc). Some of the OEMs have already launched these locally developed models. While the domestic trend towards premiumisation offers significant scope of market expansion and remains an industry positive, rising competition and change in customer preferences towards alternative offerings remain a key risk. Large 2-wheeler OEM tie-ups with global players like Harley Davidson- Hero MotorCorp, TVS-BMW Bikes and Bajaj- Triumph is likely to increase the competition intensity in the premium 200+cc segment. Honda H'ness CB350 has also been launched recently.

High dependence on some models

The company's growth has been driven by the over 250-cc motorcycle sub-segment in the last few years. It has no presence in the high-volume (75-110 cc) sub-segments. Even in the over 250-cc sub-segment, its Classic 350 model accounts for ~70% of total volumes. Strong competition to its leading model could significantly hurt its volumes.

Deferment of discretionary spending

The transition to BS-VI emission norms (with effect from April 2020) has further increased the acquisition price for customers. Although EML's products are not targeted at a price-sensitive clientele, deferment of discretionary spending in the current pandemic situation could lead to muted off-take and may constrain profitability.

Geographical concentration

Although the products of EML are sold in 60 countries, exports accounted for only 5.6% of its total volumes and 7.9% of its revenues in FY20. Thus, the company remains exposed to geographical concentration risk. However, increased efforts to build a brand presence in South Asian and Latin American markets are likely to help in expanding its geographical footprint and diversifying its revenue concentration risk in the medium to long-term.

Sustained economic slowdown

EML has negligible presence in the mass and mid-market 2-wheeler segment. Its market share in overall Indian 2-wheeler industry has been declining from 6.4% in FY18 to 5.9% in FY20. A sustained slowdown in the economy could hamper the discretionary spending and can



also result in downtrading across consumer categories which can impact growth of premium motorcycles in short to medium term. Also there can be severe impact the sale of its commercial vehicles business which is cyclical in nature and highly sensitive to economic growth of the country. EML's share of profit from the JV contracted from Rs 258cr in FY19 to Rs 32cr in FY20.

Rising commodity costs could pressurize margins unless the company takes price hikes and/or saves costs by value reengineering.

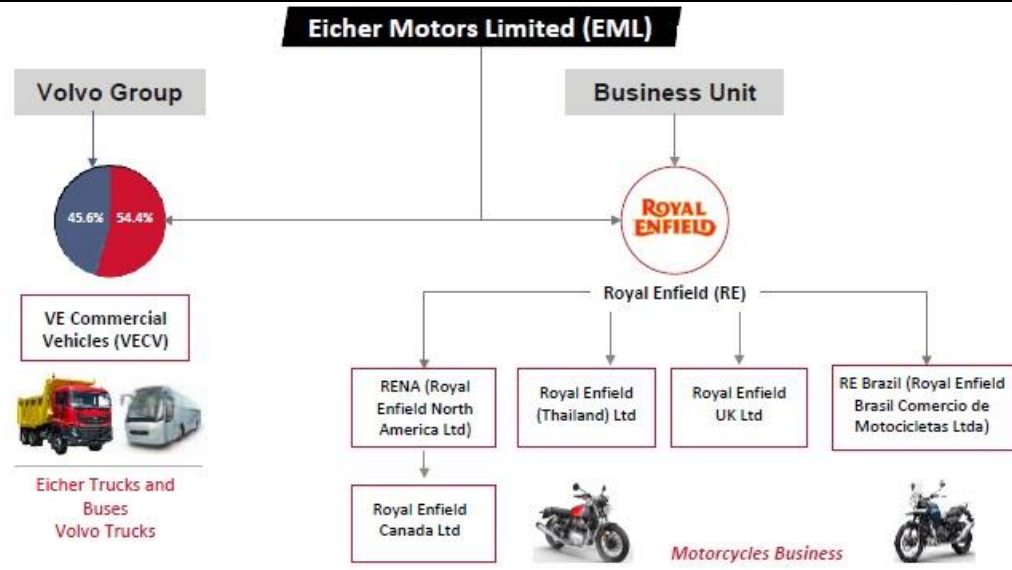
About the company

Eicher Motors Limited (EML) is the listed parent of Royal Enfield, the global leader in middleweight motorcycles. The world's oldest motorcycle brand in continuous production, Royal Enfield has made its distinctive motorcycles since 1901. Royal Enfield's motorcycle line-up includes the newly launched Interceptor 650 and the Continental GT 650, the Classic, Bullet and Thunderbird models in 350 and 500cc displacement and the purpose-built adventure tourer - Himalayan, powered by the new LS410 engine.

Royal Enfield operates through 18 company-operated stores and 850+ dealers in all major cities and towns in India, and exports to over 60 countries across the world including the USA, UK, several European and Latin American countries, as well as the Middle East and South-East Asia. Royal Enfield is fast becoming a very important player in the global mid-size motorcycle market and is working towards re-inventing this space with motorcycles that are evocative and engaging and great fun to ride.

In addition to motorcycles, EML (54.4%) has a joint venture with Sweden's AB Volvo (45.6%) - Volvo Eicher Commercial Vehicles Limited (VECV) – which has pioneered modernisation of commercial vehicles in India and other developing countries. VECV has a complete range of trucks and buses from 4.9-55 tonnes, and its integrated manufacturing plant in Pithampur, Madhya Pradesh is the global hub for medium duty five- and eight-litre engines for Volvo Group.

Company structure



(Source: Company, HDFC sec)

Financials

Income Statement

(Rs cr)	FY18	FY19	FY20	FY21E	FY22E
Net Revenues	8965.0	9797.1	9153.6	8225.3	10013.0
Growth (%)	27.5	9.3	-6.6	-10.1	21.7
Operating Expenses	6157.3	6894.0	6973.2	6423.4	7544.2
EBITDA	2807.6	2903.1	2180.4	1802.0	2468.8
Growth (%)	31.3	29.6	23.8	21.9	24.7
EBITDA Margin (%)	29.1	3.4	-24.9	-17.4	37.0
Depreciation	223.3	300.3	381.5	381.7	400.8
Other Income	60.1	425.9	543.3	529.8	601.5
EBIT	2644.4	3028.7	2342.1	1950.1	2669.5
Interest expenses	5.3	7.3	18.8	19.2	20.1
Exceptional item	2639.0	3021.4	2323.3	1930.9	2649.4
PBT	935.9	1077.0	527.5	440.2	601.4
Tax	1703.1	1944.3	1795.8	1490.6	2048.0
PAT	256.6	258.4	31.7	-26.8	98.1
Adj. PAT	2179.7	2220.3	1827.5	1463.8	2146.1
Growth (%)	27.2	1.9	-17.7	-19.9	46.6
EPS	80.0	81.4	66.9	53.6	78.6

Balance Sheet

As at March (Rs cr)	FY18	FY19	FY20	FY21E	FY22E
SOURCES OF FUNDS					
Share Capital - Equity	27.3	27.3	27.3	27.3	27.3
Reserves	7002.8	8891.4	9953.6	11092.0	12789.9
Total Shareholders Funds	7030.1	8918.7	9980.9	11119.3	12817.2
Total Debt	150.8	186.8	144.4	151.7	159.2
Net Deferred Taxes	142.1	273.9	252.2	254.7	257.2
TOTAL SOURCES OF FUNDS	7323.0	9379.4	10377.5	11525.7	13233.7
APPLICATION OF FUNDS					
Net Block	1501.7	1874.6	2377.5	2319.9	2529.3
CWIP	333.2	449.7	312.2	342.2	372.2
Investments	1764.3	1943.9	1892.1	1865.2	1930.2
Total Non-current Assets	3599.2	4268.2	4581.7	4527.3	4831.7
Cash & Equivalents	394.6	633.4	572.4	518.3	631.0
Inventories	68.0	84.3	86.8	112.7	137.2
Debtors	5028.6	5943.9	6807.3	8097.2	9643.4
Other Current Assets	431.9	457.0	401.6	431.8	464.7
Total Current Assets	5923.1	7118.6	7868.0	9160.0	10876.2
Creditors	1171.9	1234.1	1027.7	1036.6	1261.9
Other Current Liabilities & Provsns	1027.4	773.4	1044.6	1125.1	1212.4
Total Current Liabilities	2199.2	2007.5	2072.2	2161.7	2474.3
Net Current Assets	3723.8	5111.1	5795.8	6998.4	8401.9
TOTAL APPLICATION OF FUNDS	7323.0	9379.4	10377.5	11525.7	13233.7

Cash Flow Statement

(Rs cr)	FY18	FY19	FY20	FY21E	FY22E
Reported PBT	2,895.6	3,279.8	2,355.0	1,904.1	2,747.5
Non-operating & EO items	-60.1	-425.9	-543.3	-529.8	-601.5
Interest Expenses	5.3	7.3	18.8	19.2	20.1
Depreciation	223.3	300.3	381.5	381.7	400.8
Working Capital Change	513.3	-472.0	178.8	87.3	142.6
Tax Paid	-871.6	-945.2	-549.2	-437.7	-598.9
OPERATING CASH FLOW (a)	2,705.8	1,744.3	1,841.7	1,424.8	2,110.7
Capex	-811.7	-789.7	-746.9	-354.1	-640.2
Free Cash Flow	1,894.2	954.6	1,094.7	1,070.7	1,470.5
Investments	-18.5	-179.7	51.9	26.8	-65.0
Non-operating income	60.1	425.9	543.3	529.8	601.5
INVESTING CASH FLOW (b)	-770.1	-543.5	-151.8	202.5	-103.7
Debt Issuance / (Repaid)	106.4	35.9	-42.3	7.2	7.6
Interest Expenses	-5.3	-7.3	-18.8	-19.2	-20.1
FCFE	1,995.3	983.2	1,033.6	1,058.7	1,457.9
Share Capital Issuance	74.6	83.2	-368.0	0.0	0.0
Dividend	-349.3	-397.3	-397.3	-325.4	-448.2
FINANCING CASH FLOW (c)	-173.6	-285.5	-826.4	-337.4	-460.8
NET CASH FLOW (a+b+c)	1,762.2	915.3	863.4	1,289.9	1,546.2

Key Ratios

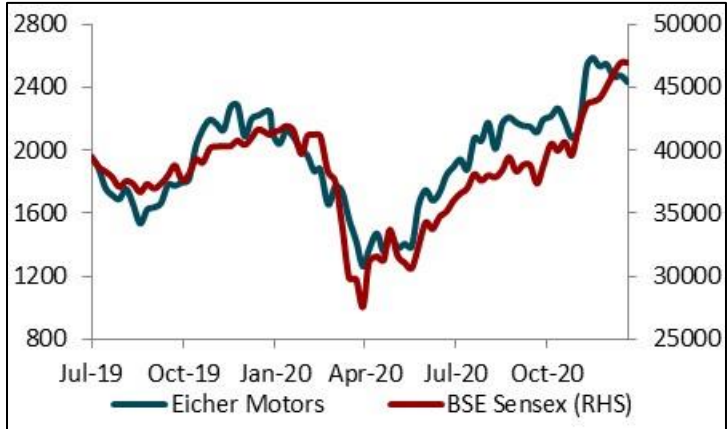
	FY18	FY19	FY20	FY21E	FY22E
Profitability (%)					
EBITDA (%)	31.3	29.6	23.8	21.9	24.7
EBIT (%)	28.8	26.6	19.7	17.3	20.7
APAT (%)	24.3	22.7	20.0	17.8	21.4
RoE (%)	35.2	27.8	19.3	13.9	17.9
RoCE (%)	28.9	23.5	18.3	13.7	16.7
Solvency Ratio					
Debt/EBITDA (x)	-1.7	-2.0	-3.1	-4.4	-3.8
Net D/E (x)	-0.7	-0.6	-0.7	-0.7	-0.7
PER SHARE DATA (Rs)					
EPS	80.0	81.4	66.9	53.6	78.6
CEPS	80.1	91.8	80.9	67.6	93.3
BV	257.9	327.2	365.6	407.3	469.5
Dividend	110.0	125.1	124.9	102.3	140.9
Turnover Ratios (days)					
Inventory	2.8	3.1	3.5	5.0	5.0
Debtor	16.1	23.6	22.8	23.0	23.0
Creditors	47.7	46.0	41.0	46.0	46.0
VALUATION (x)					
P/E	30.5	29.9	36.4	45.4	31.0
P/BV	9.4	7.4	6.7	6.0	5.2
EV/EBITDA	21.9	20.9	27.5	32.5	23.1
EV / Revenues	6.9	6.2	6.5	7.1	5.7
Dividend Yield (%)	4.5	5.1	5.1	4.2	5.8

(Source: Company, HDFC sec Research)

Eicher Motors Ltd.

598.71	685.65	685.65	685.65	203.88	118.92	118.92
(-2.11)	(-14.5)	(-7.74)	(-1.05)	(-1.05)	(-1.05)	(-1.05)
142.09	167.29	154.12	393.13	-62.95	-187.58	-42.38
(-35.1)	(-17.4)	(-7.84)	(-7.58)	(-11.88)	(-71.48)	(-15.88)

Price Chart





Disclosure:

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HDFC securities Limited, I Think Techno Campus, Building - B, "Alpha", Office Floor 8, Near Kanjurmarg Station, Opp. Crompton Greaves, Kanjurmarg (East), Mumbai 400 042 Phone: (022) 3075 3400 Fax: (022) 2496 5066 Compliance Officer: Binkle R. Oza Email: complianceofficer@hdfsec.com Phone: (022) 3045 3600

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