Investors' Delight: Greaves Cotton Ltd. (GCL) – "BUY"

"Robust play in auto-ancillary and farm equipment space with attractive valuations"

Investment Summary

Date	23rd October, 2013
Industry	Auto – Ancillary: Engines
CMP	Rs. 59.8
Target Price	Rs. 87
Upside	47%
Beta vs Sensex	0.66
BSE/NSE Code	501455/GREAVESCOT
Bloomberg Code	GRV IN
52 Week High	Rs. 86.95 (4TH Feb, 2013)
52 Week Low	Rs. 54.15 (8th Aug, 2013)
Face Value	Rs. 10
Share Capital	Rs. 834.3 mn
Networth	Rs. 7,380 mn
Market Capitalization	Rs. 14,530 mn
Book Value	Rs. 30.5
Shareholding Pattern (%)	As on June 2013
Promoters	51.56
Bodies Corporate	2.79
Public and Others	45.65

The Company is engaged in the business of manufacturing Engines (Automotive applications, industrial applications, Auxiliary Power applications, Farm applications), Infrastructure Equipment (Road making, Concreting) and other products – traded (Light agricultural equipment, Traded construction equipment and other adjacent products). GCL topline has witnessed a CAGR of 13% over the period FY03-FY13 and an impressive PAT CAGR of 53 percent over the same period. FY13 revenue stood at Rs. 1,873 crores with an EBITDA margin of 12.9 percent. FY13 PAT was Rs. 138 crore resulting into a PAT margin of 7.4 percent.

GCL has about 35 per cent market share in the supply of engines to auto rickshaws and over 80 per cent share in engines for three-wheel cargo carriers. The company also supplies engines to four-wheel mini-trucks. Its key clientele include Piaggio, Atul Auto, Tata Motors and Mahindra and Mahindra. These segments typically, tend to be less cyclical in comparison with the medium and heavy CVs. For example, in 2012-13 even as the medium and heavy CV sales dipped 23 per cent, three-wheelers managed to eke out almost 5 per cent growth. Similarly, volumes in the light CV segment (of which mini-trucks form a part) grew by a robust 14 per cent. Going forward, these segments should continue to do well. GCL's three-wheeler clients are either expanding capacities or product lines. Atul Auto is doubling its production capacity to 48,000 units. GCL is supplying CNG engines for Piaggio's newly-launched Ape City. It has also added TVS to its client base. Greaves Automotive Engines Business will supply G435 engines for TVS King DS which is now on road in Kerala.

Besides, opening up of permits for autorickshaws in Delhi and Hyderabad recently is a positive for the company. Mini-trucks are increasingly being preferred, thanks to advantages such as greater cabin comfort, higher mileage/fuel efficiency and low maintenance costs.

While GCL currently has a ten-year contract (beginning 2011) to supply engines to the Ace Zip from Tata Motors, it will also supply for an upcoming CNG-powered mini-truck. With Mahindra and Mahindra also manufacturing small CVs, such as the Gio and Maxximo, given its existing relationship for supply of three-wheeler engines, GCL stands a good chance of winning a similar contract from them. Even as minor segments such as industrial engines, gensets (auxiliary power) and infrastructure equipment continue to struggle, the demand for farm equipment perked up, thanks to the good monsoons.

With due consideration to factors like a) leading diesel engine manufacturer with annual production of over half million engines, b) market leader in last mile automotive application and Pumpsets for farm application, c) farm equipment segment presenting bright prospects, d) strong reach and brand with good capabilities in diesel engine technology, e) consistently achieved high return ratios – ROCE and ROE, e) debt free status and f) consistent cashflow from operations, GCL deserves a premium. At CMP, the stock trades at a PE multiple of 10x FY13 EPS.

We recommend a "BUY" and value the Company based on its historic PE multiple of 13x at FY14 consensus estimated EPS of Rs. 6.7 with a target price of Rs. 87 with investors having 9-12 months horizon.

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