

In-line performance

■ Topline growth in line, margins suffer...

Greaves' Q3FY07 revenues, at Rs.3.25bn (36.6% Y-o-Y), were in line with our expectations of Rs.3.24bn. EBITDA margins for the quarter, however, suffered by 58bps to 14.7%, as against our expectation of 16% due to higher than expected increase in raw material costs & other expenses. EBITDA for the quarter was thus at Rs.478mn (31.4% Y-o-Y). PAT at Rs.339mn, was more than our expectation of Rs.301mn, due to MAT credit of Rs.60mn received which reduced tax outgo.

Upgrading our full year estimates

Based on nine-months numbers for FY07E, we are upgrading our revenue estimates by around 9% to Rs.12.58bn, mainly on account of higher growth in the infrastructure division, and by around 8.6% in PAT to Rs.1.1bn as against Rs.984mn earlier. We are maintaining our earnings estimates for FY08E and FY09E at Rs.1.3bn and Rs.1.65bn respectively.

Maintain Buy

The stock trades at 12x FY08E and 9.6x FY09E EPS; we expect a CAGR of 22.3% in revenue and 25% earnings CAGR over FY06-09E. Greaves compares favorably to peers comprising other engine manufacturers and major auto ancillaries, both on earnings growth and return ratios.

■ Estimates (Jun)

(Rs)	2005A	2006A	2007E	2008E	2009E
Net Income (Adjusted - mn)	621	851	1,069	1,310	1,654
EPS	13.60	17.42	21.89	26.83	33.87
EPS Change (YoY)	NM	28.1%	25.7%	22.5%	26.3%
Dividend / Share	7.00	7.00	9.50	9.50	12.00
Free Cash Flow / Share	16.01	12.17	(10.33)	16.32	17.28

Valuation (Jun)

	2005A	2006A	2007E	2008E	2009E
P/E	24.12x	18.83x	14.99x	12.23x	9.69x
Dividend Yield	2.13%	2.13%	2.90%	2.90%	3.66%
EV / EBITDA*	16.38x	11.91x	8.88x	7.23x	5.86x
Free Cash Flow Yield*	4.53%	3.69%	-3.13%	4.95%	5.24%

* For full definitions of *iQmethod*SM measures, see page 7.

Equity | India | Industrial Machinery
19 April 2007



Merrill Lynch

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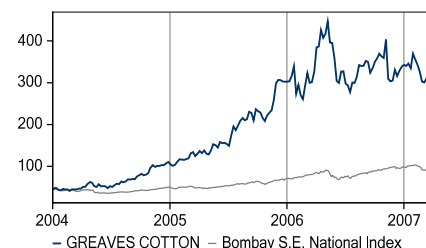
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■ Stock Data

Price	Rs328.10
Price Objective	Rs410.00
Date Established	18-Mar-2007
Investment Opinion	C-1-7
Volatility Risk	HIGH
52-Week Range	Rs236.10-Rs465.00
Mrkt Val / Shares Out (mn)	US\$381 / 48.8
Average Daily Volume	12,632
ML Symbol / Exchange	XGRVF / BSE
Bloomberg / Reuters	GRV IN / GRVL.BO
ROE (2007E)	44.8%
Net Dbt to Eqty (Dec-2006A)	9.9%
Est. 5-Yr EPS / DPS Growth	20.0% / 11.0%
Free Float	49.9%



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Refer to important disclosures on page 8 to 9. Analyst Certification on page 6. Price Objective Basis/Risk on page 6.

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*iQprofile*SM Greaves Cotton Ltd.

Key Income Statement Data (Jun)	2005A	2006A	2007E	2008E	2009E
(Rs Millions)					
Sales	6,604	8,415	12,687	15,289	18,848
Gross Profit	1,315	1,734	2,514	3,032	3,629
Sell General & Admin Expense	(293)	(328)	(629)	(717)	(772)
Operating Profit	908	1,273	1,724	2,066	2,572
Net Interest & Other Income	108	48	(169)	(81)	(66)
Associates	NA	NA	NA	NA	NA
Pretax Income	1,016	1,321	1,554	1,985	2,506
Tax (expense) / Benefit	(395)	(470)	(485)	(675)	(852)
Net Income (Adjusted)	621	851	1,069	1,310	1,654
Average Fully Diluted Shares Outstanding	46	49	49	49	49

Key Cash Flow Statement Data

Net Income (Reported)	621	851	1,069	1,310	1,654
Depreciation & Amortization	114	132	161	249	286
Change in Working Capital	80	(257)	(359)	(421)	(461)
Deferred Taxation Charge	308	350	19	79	100
Other Adjustments, Net	(124)	(137)	105	80	65
Cash Flow from Operations	998	939	995	1,297	1,644
Capital Expenditure	(267)	(345)	(1,500)	(500)	(800)
(Acquisition) / Disposal of Investments	0	(414)	800	0	0
Other Cash Inflow / (Outflow)	239	91	0	0	0
Cash Flow from Investing	(28)	(668)	(700)	(500)	(800)
Shares Issue / (Repurchase)	100	219	0	0	0
Cost of Dividends Paid	(202)	(480)	(534)	(534)	(674)
Cash Flow from Financing	(591)	(500)	(334)	(684)	(774)
Free Cash Flow	731	594	(505)	797	844
Net Debt	125	215	622	440	335
Change in Net Debt	(708)	87	408	(183)	(104)

Key Balance Sheet Data

Property, Plant & Equipment	1,050	1,310	2,648	2,834	3,250
Other Non-Current Assets	758	937	94	94	94
Trade Receivables	625	920	1,442	1,874	2,466
Cash & Equivalents	662	335	128	160	164
Other Current Assets	1,207	1,455	2,272	2,845	3,683
Total Assets	4,302	4,957	6,584	7,808	9,658
Long-Term Debt	595	480	680	530	430
Other Non-Current Liabilities	NA	NA	0	0	0
Short-Term Debt	191	70	70	70	70
Other Current Liabilities	2,064	2,246	3,227	3,812	4,782
Total Liabilities	2,850	2,796	3,977	4,411	5,282
Total Equity	1,452	2,161	2,607	3,396	4,375
Total Equity & Liabilities	4,302	4,957	6,584	7,807	9,657

*iQmethod*SM - Bus Performance*

Return On Capital Employed	24.0%	33.1%	39.1%	37.1%	38.3%
Return On Equity	48.2%	47.1%	44.8%	43.7%	42.6%
Operating Margin	13.9%	15.3%	13.7%	13.5%	13.7%
EBITDA Margin	15.5%	16.7%	14.9%	15.1%	15.2%

*iQmethod*SM - Quality of Earnings*

Cash Realization Ratio	1.6x	1.1x	0.9x	1.0x	1.0x
Asset Replacement Ratio	2.3x	2.6x	9.3x	2.0x	2.8x
Tax Rate (Reported)	38.9%	35.6%	31.2%	34.0%	34.0%
Net Debt-to-Equity Ratio	8.6%	9.9%	23.9%	12.9%	7.7%
Interest Cover	7.9x	16.0x	10.2x	25.5x	39.0x

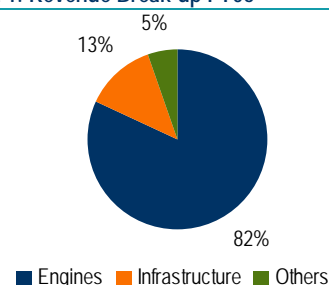
Key Metrics

* For full definitions of *iQmethod*SM measures, see page 7.

Company Description

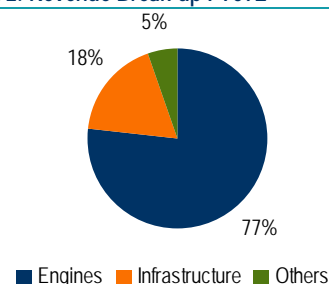
Greaves Cotton Ltd is one of India's leading and well-diversified engineering companies. It manufactures a wide range of auto and industrial products. Its core competencies are in diesel and petrol engines (about 80% of revenues), gensets, agro equipment and construction equipment. It is one of the major three-wheeler engine suppliers in the country.

Chart 1: Revenue Break-up FY06



Source: Merrill Lynch

Chart 2: Revenue Break-up FY09E



Source: Merrill Lynch

Stock Data

Price to Book Value

6.2x

Infrastructure zooms; engines follow

The infrastructure segment continued with its robust revenue growth of 61% (Y-o-Y basis) to Rs.600mn in Q3FY07. As expected, PBIT margins in this division improved by 200bps% (Y-o-Y basis), thus reporting growth of around 84% (Y-o-Y basis) in its PBIT to Rs.98mn. Engines, on the other hand, reported revenue growth of 31.6% (Y-o-Y basis) for the third quarter to Rs.2.55bn, in line with our expectations. However, PBIT margins of the division were down by nearly 133bps to 16%. PBIT for the quarter was Rs.409mn, Y-o-Y growth of 21.5%. Margins in the engine division are expected to suffer on account of increasing input costs and introduction of new products in the segment.

Financials

Table 1: Quarterly Results

Rs. in mn	3QFY07	3QFY06	% Y-o-Y	2QFY07	% Q-o-Q
Sales Turnover	3256.9	2384.7	36.6%	3233.3	0.7%
Total Exp. (a+ b +c +d)	2778.5	2020.5	37.5%	2759.1	0.7%
Raw Material Cost (a)	2303.4	1644.3	40.1%	2297.0	0.3%
Staff cost (b)	153.3	119.3	28.5%	177.5	-13.6%
Other Exp. (d)	321.8	256.9	25.3%	284.6	13.1%
Operating Profit	478.4	364.2	31.4%	474.2	0.9%
Interest	41.4	14.0	195.7%	51.4	-19.5%
Depreciation	42.0	36.4	15.4%	38.9	8.0%
PBT before other income	395.0	313.8	25.9%	383.9	2.9%
Other Income	26.0	8.4	209.5%	27.9	-6.8%
PBT	421.0	322.2	30.7%	411.8	2.2%
Tax - Provision	97.5	25.2	286.9%	113.6	-14.2%
Tax - Deferred	44.5	96.4	-53.8%		
Adjusted PAT	279.0	200.6	39.1%	298.2	-6.4%
Extraordinary income	60.0	36.8	63.0%	0.0	
Reported PAT	339.0	237.4	42.8%	298.2	13.7%

Source: Company, Merrill Lynch

Table 2: Segmental Break up

Rs.in mn	3QFY07	3QFY06	% Y-o-Y
Segmental Revenues			
Engines	2551.0	1938.5	31.6%
Infrastructure	600.6	372.5	61.2%
Segmental PBIT			
Engines	409.2	336.7	21.5%
Infrastructure	98.0	53.3	83.9%
EBITDA (%)			
Engines	16.0	17.4	
Infrastructure	16.3	14.3	

Source: Company, Merrill Lynch

Table 3: Revision of estimates for FY07E

Rs.in mn	Earlier	Revised	Revision
Engines	9264.1	9993.9	7.9%
Infrastructure	1820.0	2149.0	18.1%
Revenues	11525.6	12584.4	9.2%
EBITDA	1732.5	1782.7	2.9%
Adj. PAT	984.7	1069.4	8.6%
EPS (Rs.)	20.2	21.9	8.6%

Source: Merrill Lynch

Table 4: Earnings Statement

Rs. Mn	FY05	FY06	FY07E	FY08E	FY09E
Sales	6522.6	8334.5	12584.4	15258.5	18817.8
Raw Material Cost	4364.5	5669.7	8902.0	10681.0	13266.6
Labour cost	519.2	568.1	630.6	751.3	841.5
Other expenses	698.5	771.3	1269.1	1541.1	1881.8
Total operating expenses	5582.2	7009.1	10801.7	12973.4	15989.9
EBITDA	940.4	1325.4	1782.7	2285.2	2828.0
% Margins	14.4%	15.9%	14.2%	15.0%	15.0%
Depreciation	113.6	132.4	161.4	248.9	285.5
Gross Interest	114.8	79.4	169.4	81.0	66.0
Other Income	81.6	80.1	102.3	30.0	30.0
Recurring PBT	793.6	1193.7	1554.2	1985.3	2506.4
Add: Extra ordinaries	222.5	127.4	60.0	0.0	0.0
Less: Taxes	395.2	470.2	484.9	675.0	852.2
-Current Tax	87.4	120.6	466.3	595.6	751.9
-Deferred Tax	307.8	349.6	18.7	79.4	100.3
Net Income (Reported)	620.9	850.9	1129.3	1310.3	1654.2
Recurring Net income	398.4	723.5	1069.3	1310.3	1654.2

Source: Company, Merrill Lynch

Table 5: Balance Sheet

Rs. Mn	FY05	FY06	FY07E	FY08E	FY09E
Assets					
Total Current Assets	2493.8	2710.0	3968.4	5116.6	6586.8
Total Current Liabilities & Provisions	2063.8	2246.0	3250.8	3923.6	4905.1
Net Current Assets	430.0	464.0	717.6	1193.0	1681.7
Investments	390.1	894.3	94.3	94.3	94.3
Deferred tax assets	392.5	42.9	0.0	0.0	0.0
Net Fixed Assets	1050.2	1309.8	2640.4	2826.1	3250.4
Total Assets	2262.8	2711.0	3452.2	4113.4	5026.4
Liabilities					
Borrowings	786.6	549.9	649.9	499.9	399.9
Equity Share capital	456.4	488.4	488.4	488.4	488.4
Face value per share (Rs.)	10.0	10.0	10.0	10.0	10.0
Reserves & Surplus	1019.8	1672.7	2313.9	3125.1	4138.1
Less: Misc Exp.	0.0	0.0	0.0	0.0	0.0
Networth	1476.2	2161.1	2802.3	3613.5	4626.5
Total Liabilities	2262.8	2711.0	3452.2	4113.4	5026.4

Source: Company, Merrill Lynch

Table 6: Cash Flow Statement

Rs. Mn	FY05	FY06	FY07E	FY08E	FY09E
Net income	398.4	723.5	1069.3	1310.3	1654.2
Depreciation	113.6	132.4	161.4	248.9	285.5
Deferred Taxes	307.8	349.6	18.7	79.4	100.3
Cash Earnings	819.8	1205.5	1249.4	1638.6	2040.0
Minority Interest	0.0	0.0	0.0	0.0	0.0
Share of associate profit	0.0	0.0	0.0	0.0	0.0
Changes in working capital	79.6	(256.6)	(358.6)	(421.1)	(460.5)
Other adjustments, Net	98.2	(9.8)	164.6	67.7	52.7
Cash Flow from operations	997.6	939.1	1055.4	1285.2	1632.2
Capital expenditure	(266.9)	(344.7)	(1500.0)	(500.0)	(800.0)
Change in investments	239.2	(323.3)	800.0	0.0	0.0
Cash Flow from investing	(27.7)	(668.0)	(700.0)	(500.0)	(800.0)
Share issue/buyback	100.3	218.9	0.0	0.0	0.0
Dividends	(202.2)	(479.6)	(533.6)	(533.6)	(674.0)
Change in debt	(489.4)	(239.1)	200.0	(150.0)	(100.0)
Others	(159.9)	(97.6)	(169.4)	(81.0)	(66.0)
Cashflow from financing	(751.2)	(597.4)	(503.0)	(764.6)	(840.0)
Change in cash & cash equivalents	218.7	(326.3)	(147.6)	20.6	(7.8)
Free cash flow	730.7	594.4	(444.6)	785.2	832.2

Source: Company, Merrill Lynch

Table 7: Ratios

	FY05	FY06	FY07E	FY08E	FY09E
Raw Material/Sales	66.9%	68.0%	70.7%	70.7%	70.7%
Labour Cost/Sales	8.0%	6.8%	4.9%	4.4%	3.9%
Other exps/Sales	10.7%	9.3%	9.8%	10.1%	10.6%
Asset turnover ratio (x)	6.2	6.4	4.8	5.5	5.9
Net Profit Margin	6.1%	8.7%	9.2%	8.5%	8.7%
RoCE (%)	39.0%	51.2%	57.8%	55.2%	56.8%
Net debt/Equity (x)	0.3	0.4	0.9	0.4	0.3
RoE (%)	49.9%	48.1%	47.9%	42.1%	41.2%

Source: Company, Merrill Lynch

Price Objective Basis & Risk

Our price objective of Rs.410 is on the basis that company's multiples (15x FY07E) will likely sustain through FY08, and we have also used a DCF method, which gives us a value of Rs420/share.

The risks to achieving our price objective are a slowdown in the order book size in the infrastructure division and a reduction in Piaggio's revenue share.

Analyst Certification

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***iQmethod*SM Measures Definitions**

Business Performance	Numerator	Denominator
Return On Capital Employed	$\text{NOPAT} = (\text{EBIT} + \text{Interest Income}) * (1 - \text{Tax Rate}) + \text{Goodwill Amortization}$	Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill
Return On Equity	Net Income	Shareholders' Equity
Operating Margin	Operating Profit	Sales
Earnings Growth	Expected 5-Year CAGR From Latest Actual	N/A
Free Cash Flow	Cash Flow From Operations – Total Capex	N/A
Quality of Earnings		
Cash Realization Ratio	Cash Flow From Operations	Net Income
Asset Replacement Ratio	Capex	Depreciation
Tax Rate	Tax Charge	Pre-Tax Income
Net Debt-To-Equity Ratio	Net Debt = Total Debt, Less Cash & Equivalents	Total Equity
Interest Cover	EBIT	Interest Expense
Valuation Toolkit		
Price / Earnings Ratio	Current Share Price	Diluted Earnings Per Share (Basis As Specified)
Price / Book Value	Current Share Price	Shareholders' Equity / Current Basic Shares
Dividend Yield	Annualised Declared Cash Dividend	Current Share Price
Free Cash Flow Yield	Cash Flow From Operations – Total Capex	Market Cap. = Current Share Price * Current Basic Shares
Enterprise Value / Sales	$\text{EV} = \text{Current Share Price} * \text{Current Shares} + \text{Minority Equity} + \text{Net Debt} + \text{Sales Other LT Liabilities}$	
EV / EBITDA	Enterprise Value	Basic EBIT + Depreciation + Amortization

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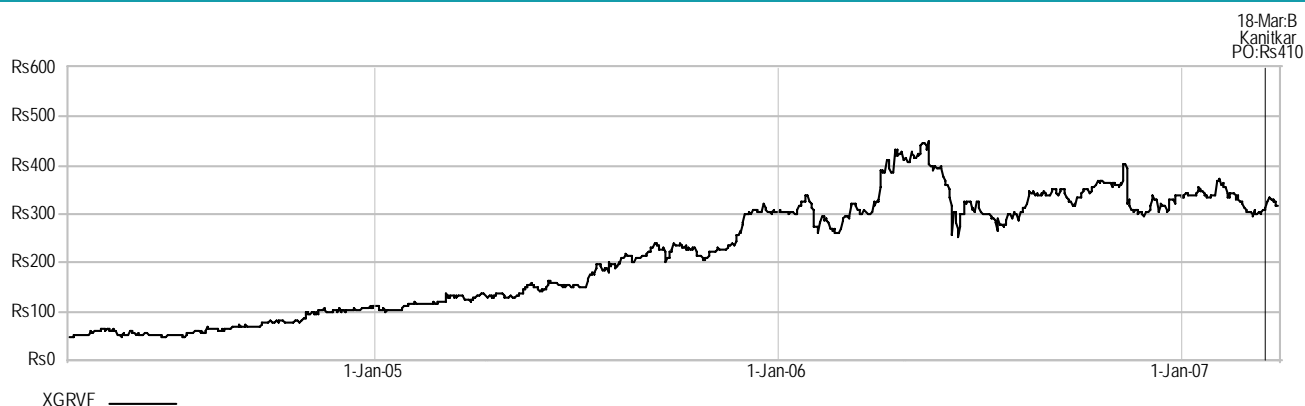
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Important Disclosures

XGRVF Price Chart



B : Buy, N : Neutral, S : Sell, PO : Price objective, NA : No longer valid

The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark Grey shading indicates the security is restricted with the opinion suspended. Light Grey shading indicates the security is under review with the opinion withdrawn. Chart current as of March 31, 2007 or such later date as indicated.

Investment Rating Distribution: Machinery/Diversified Manufacturing Group (as of 31 Mar 2007)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	32	62.75%	Buy	9	32.14%
Neutral	15	29.41%	Neutral	2	14.29%
Sell	4	7.84%	Sell	0	0.00%

Investment Rating Distribution: Global Group (as of 31 Mar 2007)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1562	45.16%	Buy	415	30.09%
Neutral	1615	46.69%	Neutral	446	30.65%
Sell	282	8.15%	Sell	49	19.76%

* Companies in respect of which MLPF&S or an affiliate has received compensation for investment banking services within the past 12 months.

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