

6<sup>th</sup> December 2006**ACCUMULATE**

Price	Target Price
<b>Rs318</b>	<b>Rs407</b>
<b>Sensex</b>	<b>13,938</b>

**Price Performance**

(%)	1M	3M	6M	12M
Absolute	(10.7)	(8.7)	0.5	5.9
Rel. to Sensex	(16.2)	(25.5)	(42)	(52.2)

Source: Capitaline

**Stock Details**

Sector	Engines
Reuters	GRVC.BO
Bloomberg	GRV@IN
Equity Capital	Rs488mn
Face Value	Rs10
52 Week H/L	Rs465/196
Market Cap	Rs15.5bn
Daily Avg Vol. (No of shares)	124224
Daily Avg Turnover (US\$)	\$1mn

**Shareholding Pattern (%)**

(30th Sept.'06)	
Promoters	50.0
FII/NRI	3.4
Institutions	32.6
Private Corp.	2.2
Public	11.7

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**Greaves Cotton Ltd**Con-call  
Update**Committed to growth**

We arranged the conference call of Greaves Cotton Ltd. with Mr. P. Sachdev, MD & CEO to take us through the strategy adopted by the company after Piaggio's announcement of setting up its own diesel engines plant in India. The management appeared in complete control of the situation and banked on robust untapped opportunities like exports, increasing share of its infrastructure equipment business and ramp of other OEMs as the key growth drivers. This would be on the backdrop of continued relationship with Piaggio, which would continue to source engines from the company post commencement of its own plant, albeit growth would be missing. We have already mentioned in our previous report that the growth for coming 3 years would be intact but the uncertainties over the Piaggio's business would cast a shadow over the valuations. We believe that the company would gradually catch up in terms of valuation as their de-risking actions pan out and one see success being tasted. At Rs318, the stock is currently trading at 14.8x FY07E EPS of Rs21.5 and 10.9x FY08E EPS of Rs29.1. We maintain Accumulate with 12-month target of Rs407.

**Key takeaways from the Conference call**

- Piaggio's planned 200000 units diesel engines plant in India on track and would spend around Euro 65mn and would come up in early CY2010. Piaggio sources 90% of its current requirement from Greaves (around 125000units) and forms 28-30% of Greaves overall revenues for FY06.
- Post commencement of the plant in 2010, the management is confident and also assured by Piaggio that the sourcing from Greaves would still continue given the strong cost-quality proposition offered by the company. The de-risking step adopted by Piaggio would result in flattish to marginal growth in the Piaggio's business to Greaves post 2010. **The logic** - currently Piaggio has sales of 1.3-1.4 lac units and 87-90% is supplied by Greaves; ie 1.25 lac units. This is expected to grow in range of 22-30% CAGR for next 3 years. Thus Piaggio's requirement would be 2.5-3 lac units by 2010. Since, it is building up capacity of 2lac, it will need to still outsource 50000-100000 units. The opportunity at that time would be 20-22% of twin cylinder quadricycles engines and 78-80% of single cylinder 3wheeler engines.
- Apart from Piaggio, Greaves has 22 OEMs including M&M, Atul Auto and Scooters India. M&M and Scooters India has shown strong growth during the year.
- Company would start supplying twin cylinder engines for quadricycles of Piaggio and is also in talks with several OEMs, which are contemplating entry into fast growing quadricycles market.
- The company has positioned itself as an independent engine manufacturer and believes that the model is sustainable, despite companies setting up of captive engine manufacturing facility.
- The company manufactured around 200000 single cylinder engines in FY06 and would achieve over 250000units in FY07 and around 300000 units in FY08.
- The planned capex of Rs1500mn for FY07 is on track and the company intends to hike capacity in the engines division by 100000units in next 18 months. We had specific concern regarding the possibility of capex being curtailed and the company has addressed the same with no change in plans.
- The company is betting on exports being a large untapped opportunity that would fill the growth vacuum created by flattish growth in Piaggio's business. We believe that company would utilize the next 3 years to aggressively venture into the international markets and construct a strong base, which would help them for a robust take-off in the international market.

- The company intends to change the business mix aggressively in favour of the infrastructure equipment business. The management is looking at 30% of revenues from the infrastructure business in FY10 and Piaggio's share dropping to 23-24% by that time. That would imply growth of over 50% in the infrastructure business for next 4 years.
- The company still maintains its vision of reaching turnover of Rs30bn by FY11, CAGR of 27% over next 5 years on back of robust economic environment and continued thrust on R&D and launching of new products and entering new markets.

#### **Valuations will catch up**

**The stock has been battered down from Rs420 to Rs295 after the news of Piaggio's setting up its own engines plant came in. We believe that the uncertainties over the issue and future course of action will loom large on the stock performance. However, given the confident outlook and strategy set by the management, we expect the stock to regain some ground and slowly catch up in valuations as their planned strategies take some shape and they taste some success.**

**We completely believe in the capabilities of the management and are confident of strong growth to be achieved in coming 3-4 years. The management appeared to be committed to growth, with or without Piaggio's growth.**

**At Rs318, the stock is trading at 14.8x FY07E EPS of Rs21.5 and 10.9x FY08E EPS of Rs29.1. Thus, we firmly believe that there is very limited downside on the stock. We maintain our estimates and also our rating as Accumulate with a target of Rs407.**

## Profit &amp; Loss

	Rs mn			
	FY05	FY06	FY07E	FY08E
Net Sales	6,523	9,396	11,843	15,077
Growth (%)		44.1%	26.0%	27.3%
Raw Material	4,365	6,592	8,290	10,554
% to sales	66.9%	70.2%	70.0%	70.0%
Staff cost	519	522	579	694
% to sales	8.0%	5.6%	4.9%	4.6%
S/G Admin	293	421	533	633
% to sales	4.5%	4.5%	4.5%	4.2%
Other expenses	406	536	722	890
% to sales	6.2%	5.7%	6.1%	5.9%
EBITDA	940	1,325	1,719	2,306
% of Sales	14.4%	14.1%	14.5%	15.3%
Depreciation & Amort.	114	132	175	215
EBIT	827	1,193	1,544	2,091
% of Sales	12.7%	12.7%	13.0%	13.9%
Other Income	82	80	90	100
Interest	115	79	70	70
EO Items	223	127	-	-
PBT	1,016	1,321	1,564	2,121
Tax	392	458	516	700
ETR	38.6%	34.7%	33.0%	33.0%
PAT	624	863	1,048	1,421
Adjusted PAT	484	768	1,048	1,421
Growth (%)		58.5%	36.5%	35.6%

## Cash Flow Statement

	Rs mn			
	FY05	FY06E	FY07E	FY08E
PBT	1,016	1,321	1,564	2,121
Depreciation	114	132	175	215
Other Income	(25)	19	2	(100)
Interest (paid)	115	79	70	70
EO items	(128)	(52)	-	-
Others	(93)	(141)	-	-
Change in working capital	80	(283)	(277)	(551)
Tax Paid	(81)	(134)	(235)	(212)
CFO	998	941	1300	1543
Capex	(68)	(397)	(1,350)	(650)
(Inc)/Dec in Inv	0	(414)	400	-
Other Income	40	142	90	100
CFI	(28)	(670)	(860)	(550)
Equity Issue	100	219	-	-
Net Borrowings	(489)	(239)	-	-
Dividend Paid	(202)	(480)	(390)	(501)
Interest Paid	(160)	(98)	(70)	(70)
CFF	(751)	(597)	(460)	(571)
Incr/(decr) in cash	219	(326)	(20)	422
Cash beginning	443	662	335	315
Cash ending	662	335	315	737

## Balance Sheet

	Rs mn			
	FY05	FY06E	FY07E	FY08E
Equity Capital	456	488	488	488
Adv for warrants	24	-	-	-
Reserves	996	1,673	2,219	2,972
Networth	1,476	2,161	2,708	3,460
Total Debt	787	550	550	550
Deferred Tax Liabilities	(393)	(43)	239	726
Total Capital Employed	1,870	2,668	3,496	4,737
Gross Block	1,847	2,209	3,573	4,323
Less Depreciation	948	1,063	1,238	1,453
Net Fixed Assets	899	1,146	2,335	2,870
CWIP	151	164	150	50
Investments	390	894	494	494
Inventory	665	880	1,248	1,680
Debtors	625	920	1,460	1,983
Cash and Bank	662	335	315	737
Loans & Advances	542	576	947	1,206
Total Curr. Assets	2,494	2,710	3,971	5,605
Current Liabilities	1,689	1,949	2,953	3,614
Provisions	375	298	501	668
Total Curr. Liabi. & Prov.	2,064	2,246	3,454	4,283
Net Current Assets	430	464	517	1,323
Total Assets	1,870	2,668	3,496	4,737

## Ratios

	FY05	FY06E	FY07E	FY08E
EBITDA %	14.4%	14.1%	14.5%	15.3%
EBIT%	12.7%	12.7%	13.0%	13.9%
NPM %	7.4%	8.2%	8.8%	9.4%
ROCE (avg) %	36.5%	44.0%	47.4%	52.1%
Adj. ROE %	37.2%	42.2%	43.0%	46.1%
Adj. EPS	10.6	15.7	21.5	29.1
Reported EPS	13.6	17.4	21.5	29.1
Book Value	31.2	44.2	55.4	70.9
DPS	7.0	7.0	9.0	12.0
Payout %	70.1%	48.1%	47.1%	48.3%
Debtors days	43	40	45	48
Creditors days	95	76	91	88
Total Debt: Equity (avg)	0.8	0.4	0.2	0.2
Asset Turnover (adj)	2.8	3.8	4.0	4.1
PE (x)	23.4	18.3	14.8	10.9
Cash PE (x)	19.8	15.8	12.7	9.5
P/BV (x)	10.2	7.2	5.7	4.5
EV/Sales (x)	2.3	1.7	1.3	1.0
EV/EBITDA (x)	14.3	11.2	8.7	6.4
Dividend Yield %	2.2%	2.2%	2.8%	3.8%

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