

August 26, 2020

GST rate cut proposed for 2-W segment...

Media reports say that the government is considering reducing GST rate on 2-W, recognising that vehicles are neither 'luxury' nor 'sin' goods and, hence, should not attract a high GST rate. It is said that the GST Fitment Committee has been asked for its recommendations in this regard, with the decision to then be ratified by GST Council.

Long standing industry demand

The 2-Ws currently (along with rest of the auto industry) are taxed at 28%. It has been a long standing demand of the industry to at least temporarily reduce the rate to 18% to counteract a rise in vehicle acquisition costs over the previous 18 months via introduction of various safety features (including ABS/CBS), implementation of BS-VI norms and increase in registration fees and road tax by some states. It is contended that a reduction in upfront price to be paid by consumers would boost sentiments and spur demand. During the present post-Covid environment of reduced incomes and consequent propensity to spend, any reduction in upfront acquisition costs could provide further fillip to ongoing steady improvement in demand (auto industry retail volumes back to ~70% of pre-Covid levels in recent days).

Our View

Our interaction with leading 2-W companies suggests the decision could lead to lowering of prices at the consumer level provided the cut is implemented for the entire 2-W ecosystem (i.e. including components and materials) and not just the final product produced by OEMs. Lowering of tax on final product without a corresponding reduction in components used to manufacture it (i.e. inverted duty structure) would not really benefit end consumers. If the change is made applicable for the entire 2-W value chain, however, there would be a reduction in final prices by ~8% (on *ceteris paribus* basis, reduced rate assumed to be 18%). However, there is a case wherein the benefit may not be extended to premium motorcycles (e.g. >150 cc) and prices for those products would remain unchanged. Our present target prices for 2-W OEM coverage universe i.e. Hero MotoCorp (HMCL), Bajaj Auto (BAL), Eicher Motors (EML) adequately reflects our outlook on demand, operational parameters. Hence, we leave them unchanged. Post stock price run up since our last updates, HMCL has been downgraded from BUY to **HOLD** while we maintain **HOLD** on BAL, EML.

Exhibit 1: Abridged key financials at 2-W OEMs (₹ crore)

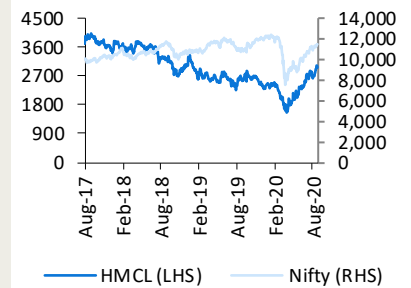
	FY19	FY20	FY21E	FY22E
HMCL				
Net Sales	33,650.5	28,836.1	28,215.0	33,829.9
Adjusted Net Profit	3,384.6	3,202.6	2,357.2	3,231.1
EPS (₹)	169.5	181.9	118.0	161.8
P/E	18.3	17.0	26.3	19.2
BAL				
Net Sales	30,250.0	29,918.6	25,004.4	30,461.2
Net Profit	4,675.1	5,100.0	3,962.0	5,022.0
EPS (₹)	161.6	176.2	136.9	173.5
P/E	19.2	17.6	22.6	17.9
EML				
Net Sales	9,797.1	9,153.6	8,561.5	10,677.4
Net Profit	2,202.8	1,827.5	1,269.6	1,942.5
EPS (₹)	80.8	67.0	46.6	71.3
P/E	27.8	33.6	48.3	31.6

Source: Company, ICICI Direct Research

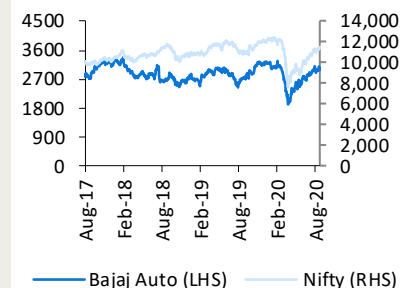
Rating matrix

Company	CMP (₹)	TP (₹)	Rating	Upside (%)
HMCL	3,100	3,235	Hold	4%
BAL	3,100	3,210	Hold	4%
EML	2,250	2,470	Hold	10%

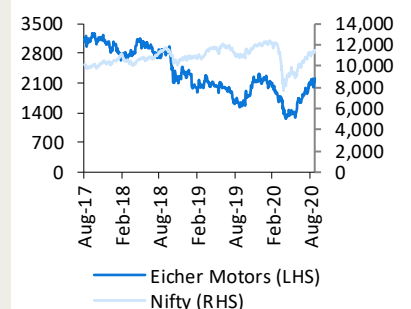
Price Chart – HMCL



Price Chart - BAL



Price Chart - EML



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Financial Summary – HMCL (CMP ₹ 3,100; Mcap ₹ 61,907 crore)

Exhibit 2: Profit and loss statement				
	₹ crore			
(Year-end March)	FY19	FY20	FY21E	FY22E
Total operating Income	33,650.5	28,836.1	28,215.0	33,829.9
Growth (%)	4.4	-14.3	-2.2	19.9
Raw Material Expenses	23,317.7	19,697.4	20,063.5	24,022.3
Employee Expenses	1,730.2	1,841.7	1,725.9	1,839.6
Other expenses	3,672.5	3,339.0	3,200.5	3,563.9
Total Operating Expenditure	28,720.5	24,878.1	24,989.9	29,425.7
EBITDA	4930.1	3958.0	3225.1	4404.1
Growth (%)	-6.0	-19.7	-18.5	36.6
Depreciation	602.0	818.0	775.9	845.7
Interest	8.6	22.0	24.8	26.0
Other Income	691.3	778.3	724.4	787.3
PBT	5010.4	3896.3	3148.8	4319.7
Total Tax	1,625.9	940.4	791.7	1,088.6
PAT	3384.6	3633.3	2357.2	3231.1
Growth (%)	-8.5	7.3	-35.1	37.1
Normalised PAT (₹)	3,384.6	3,202.6	2,357.2	3,231.1
EPS (₹)	169.5	181.9	118.0	161.8
Normalised EPS (₹)	169.5	160.4	118.0	161.8

Source: Company, ICICI Direct Research

Exhibit 3: Cash flow statement				
	₹ crore			
(Year-end March)	FY19	FY20	FY21E	FY22E
Profit after Tax	3,384.6	3,633.3	2,357.2	3,231.1
Add: Depreciation	602.0	818.0	775.9	845.7
(Inc)/dec in Current Assets	-1,696.4	1,459.9	81.4	-650.9
Inc/(dec) in CL and Provisions	-213.0	-182.6	-357.2	714.5
CF from operating activities	2077.2	5728.5	2857.2	4140.5
(Inc)/dec in Investments	2,107.5	-1,846.7	-700.0	-990.0
(Inc)/dec in Fixed Assets	-789.5	-2,115.9	-600.0	-1,200.0
Others	-1,103.7	543.5	-300.0	-300.0
CF from investing activities	214.3	-3419.2	-1600.0	-2490.0
Inc/(dec) in loan funds	0.0	150.0	0.0	0.0
Dividend paid & dividend tax	-2,084.9	-2,156.8	-1,198.2	-1,597.6
Inc/(dec) in Sec. premium & Others	-8.6	-22.0	-24.8	-26.0
CF from financing activities	-2304.9	-2226.0	-1223.0	-1623.6
Net Cash flow	-4.8	105.3	59.0	52.9
Opening Cash	141.3	136.5	241.9	300.9
Closing Cash	136.5	241.9	300.9	353.8

Source: Company, ICICI Direct Research

Exhibit 4: Balance Sheet				
	₹ crore			
(Year-end March)	FY19	FY20	FY21E	FY22E
Liabilities				
Equity Capital	39.9	39.9	39.9	39.9
Reserve and Surplus	12,817.2	14,096.5	15,255.5	16,889.0
Total Shareholders funds	12857.1	14136.4	15295.4	16928.9
Total Debt	0.0	150.0	150.0	150.0
Deferred Tax Liability	536.5	392.8	392.8	392.8
Others	117.2	122.4	122.4	122.4
Total Liabilities	13510.8	14801.6	15960.6	17594.1
Assets				
Gross Block	7,998.8	10,316.2	10,896.2	11,946.2
Less: Acc Depreciation	3,521.3	4,339.2	5,115.1	5,960.9
Net Block	4477.5	5977.0	5781.0	5985.3
Capital WIP	360.7	160.3	180.3	330.3
Total Fixed Assets	4,838.2	6,137.2	5,961.3	6,315.5
Investments	5,968.6	8,222.7	9,222.7	10,512.7
Inventory	1,072.4	1,092.0	927.6	1,112.2
Debtors	2,821.6	1,603.1	1,700.6	2,039.1
Loans and Advances	25.0	22.4	21.5	25.8
Cash	136.5	241.9	300.9	353.8
Total Current Assets	4,948.6	3,594.1	3,571.7	4,275.5
Creditors	3,355.3	3,030.5	2,705.5	3,244.0
Provisions	59.0	146.6	130.8	156.9
Total Current Liabilities	4,130.4	3,947.7	3,590.5	4,305.0
Net Current Assets	818.3	-353.7	-18.8	-29.5
Application of Funds	13510.8	14801.6	15960.6	17594.1

Source: Company, ICICI Direct Research

Exhibit 5: Key ratios				
(Year-end March)	FY19	FY20	FY21E	FY22E
Per share data (₹)				
EPS	169.5	181.9	118.0	161.8
Cash EPS	199.6	222.9	156.9	204.1
BV	643.8	707.9	765.9	847.7
DPS	87.0	90.0	60.0	80.0
Cash Per Share	227.0	324.8	362.8	415.0
Operating Ratios (%)				
EBITDA Margin	14.6	13.7	11.4	13.0
PBT / Net sales	12.9	10.9	8.7	10.5
PAT Margin	10.1	12.6	8.4	9.6
Inventory days	11.6	13.8	12.0	12.0
Debtor days	30.6	20.3	22.0	22.0
Creditor days	36.4	38.4	35.0	35.0
Return Ratios (%)				
RoE	26.3	22.7	15.4	19.1
RoCE	32.0	21.2	15.3	20.2
RoIC	59.9	39.9	29.7	40.5
Valuation Ratios (x)				
P/E	18.3	19.3	26.3	19.2
EV / EBITDA	11.6	14.0	17.0	12.2
Market Cap / Sales	1.8	2.1	2.2	1.8
Price to Book Value	4.8	4.4	4.0	3.7
Solvency Ratios				
Current Ratio	1.3	1.0	1.1	1.1
Quick Ratio	1.0	0.7	0.8	0.8

Source: Company, ICICI Direct Research

Financial Summary – BAL (CMP ₹ 3,100; Mcap ₹ 89,705 crore)

Exhibit 6: Profit and loss statement				
	₹ crore			
(Year-end March)	FY19	FY20	FY21E	FY22E
Total operating Income	30250.0	29918.6	25004.4	30461.2
Growth (%)	14.1	-1.1	-16.4	21.8
Raw Material Expenses	21,824.4	21,008.3	17,432.0	21,182.5
Employee Expenses	1,255.4	1,389.2	1,366.1	1,408.7
Other expenses	2,218.3	2,454.9	2,138.2	2,542.5
Total Operating Expenditure	25,268.0	24,822.4	20,912.6	25,103.2
EBITDA	4982.0	5096.2	4091.7	5358.1
Growth (%)	-14.3	2.3	-19.7	30.9
Depreciation	265.7	246.4	262.5	289.4
Interest	4.5	3.2	1.7	0.9
Other Income	1,649.3	1,733.6	1,445.1	1,646.0
PBT	6,361.1	6,580.2	5,272.6	6,713.9
Total Tax	2,028.0	1,480.2	1,310.5	1,691.9
PAT	4675.1	5100.0	3962.0	5022.0
Growth (%)	14.9	9.1	-22.3	26.8
EPS (₹)	161.6	176.2	136.9	173.5

Source: Company, ICICI Direct Research

Exhibit 7: Cash flow statement				
	₹ crore			
(Year-end March)	FY19	FY20	FY21E	FY22E
Profit after Tax	4,675.1	5,100.0	3,962.0	5,022.0
Add: Depreciation	265.7	246.4	262.5	289.4
(Inc)/dec in Current Assets	-1,871.0	1,054.4	372.2	-684.6
(Inc)/dec in CL and Provisions	557.4	-569.6	-482.2	627.5
CF from operating activities	3836.7	5783.6	4079.3	5338.5
(Inc)/dec in Investments	-3,172.1	973.7	-2,000.0	-2,650.0
(Inc)/dec in Fixed Assets	-142.9	-193.7	-215.0	-215.0
Others	1,619.0	-217.9	-95.0	-95.0
CF from investing activities	-1695.9	562.1	-2310.0	-2960.0
Inc/(dec) in loan funds	3.8	1.1	-20.0	-20.0
Dividend paid & dividend tax	-2,083.5	-4,166.9	-1,736.2	-2,315.0
Inc/(dec) in Sec. premium	0.0	0.0	0.0	0.0
CF from financing activities	-1999.8	-6956.5	-1772.0	-2349.8
Net Cash flow	141.0	-610.8	-2.7	28.7
Opening Cash	777.8	918.8	308.0	305.4
Closing Cash	918.8	308.0	305.4	334.1

Source: Company, ICICI Direct Research

Exhibit 8: Balance Sheet				
	₹ crore			
(Year-end March)	FY19	FY20	FY21E	FY22E
Liabilities				
Equity Capital	289.4	289.4	289.4	289.4
Reserve and Surplus	21,490.5	19,636.1	21,847.9	24,540.9
Total Shareholders funds	21779.9	19925.5	22137.3	24830.3
Total Debt	124.5	125.6	105.6	85.6
Deferred Tax Liability	542.7	346.4	346.4	346.4
Other non-current liabilities	1.1	0.8	0.8	0.8
Total Liabilities	22506.7	20520.1	22721.9	25404.9
Assets				
Gross Block	4,266.0	4,090.9	4,317.5	4,517.5
Less: Acc Depreciation	2,521.8	2,435.0	2,697.6	2,986.9
Net Block	1,744.2	1,655.9	1,619.9	1,530.5
Capital WIP	11.5	46.5	20.0	20.0
Total Fixed Assets	1755.7	1702.5	1639.9	1550.5
Investments	19,159.4	18,196.3	20,246.3	22,946.3
Inventory	961.5	1,063.5	822.1	1,001.5
Debtors	2,559.7	1,725.1	1,712.6	2,086.4
Loans and Advances	6.3	6.1	5.1	6.2
Other current assets	1035.8	714.3	597.0	727.3
Cash	918.8	308.0	305.4	334.1
Total Current Assets	5,482.2	3,817.0	3,442.1	4,155.4
Creditors	3,786.7	3,199.7	2,740.2	3,338.2
Provisions	140.6	158.0	135.3	164.8
Other current liabilities	575.4	347.3	290.3	353.6
Total Current Liabilities	4,873.7	4,253.3	3,734.1	4,445.0
Net Current Assets	608.5	-436.3	-291.9	-289.5
Deferred Tax asset	0.0	0.0	0.0	0.0
Application of Funds	22506.7	20520.1	22721.9	25404.9

Source: Company, ICICI Direct Research

Exhibit 9: Key ratios				
(Year-end March)	FY19	FY20	FY21E	FY22E
Per share data (₹)				
EPS	161.6	176.2	136.9	173.5
Cash EPS	170.7	184.8	146.0	183.5
BV	752.7	688.6	765.0	858.1
DPS	60.0	120.0	60.0	80.0
Cash Per Share	31.8	10.6	10.6	11.5
Operating Ratios (%)				
EBITDA Margin	16.5	17.0	16.4	17.6
PBT / Net sales	15.6	16.2	15.3	16.6
PAT Margin	15.5	17.0	15.8	16.5
Inventory days	11.6	13.0	12.0	12.0
Debtor days	30.9	21.0	25.0	25.0
Creditor days	45.7	39.0	40.0	40.0
Return Ratios (%)				
RoE	21.0	23.8	23.3	26.6
RoCE	19.9	25.6	17.9	20.2
RoIC	155.8	180.1	133.2	179.2
Valuation Ratios (x)				
Core P/E	20.7	17.6	22.6	17.9
EV / EBITDA	14.2	14.2	17.2	12.7
EV / Net Sales	2.3	2.4	2.8	2.2
Market Cap / Sales	3.0	3.0	3.6	2.9
Price to Book Value	4.1	4.5	4.1	3.6
Solvency Ratios				
Current Ratio	1.0	0.9	1.0	1.0
Quick Ratio	0.8	0.7	0.7	0.7

Source: Company, ICICI Direct Research

Financial Summary – EML (CMP ₹ 2,250; Mcap ₹ 61,335 crore)

Exhibit 10: Profit and loss statement				
	₹ crore			
(Year-end March)	FY19	FY20	FY21E	FY22E
Total operating Income	9,797.1	9,153.6	8,561.5	10,677.4
Growth (%)	9.3	-6.6	-6.5	24.7
Raw Material Expenses	4,845.7	4,770.9	4,942.5	6,113.0
Employee Expenses	702.4	795.8	687.9	722.4
Other Expenses	1,134.1	1,181.5	1,038.8	1,213.6
Total Operating Expenditure	6,893.9	6,973.3	6,848.6	8,260.9
EBITDA	2903.1	2180.3	1712.9	2416.5
Growth (%)	3.4	-24.9	-21.4	41.1
Depreciation	300.3	381.5	407.8	427.1
Interest	7.3	18.9	13.4	11.9
Other Income	443.4	543.3	503.4	548.2
PBT	3,038.9	2,323.2	1,795.1	2,525.8
Others	0.0	0.0	0.0	0.0
Total Tax	1,077.0	527.4	453.2	636.5
PAT	2202.8	1827.5	1269.6	1942.5
Growth (%)	12.4	-17.0	-30.5	53.0
EPS (₹)	80.8	67.0	46.6	71.3

Source: Company, ICICI Direct Research

Exhibit 11: Cash flow statement				
	₹ crore			
(Year-end March)	FY19	FY20	FY21E	FY22E
Profit after Tax	2,202.8	1,827.5	1,269.6	1,942.5
Add: Depreciation	300.3	381.5	407.8	427.1
(Inc)/dec in Current Assets	-286.6	64.7	124.2	-194.6
Inc/(dec) in CL and Provisions	-218.5	-75.7	-140.8	412.8
CF from operating activities	1554.6	1654.8	1157.3	2039.5
(Inc)/dec in Investments	838.0	-878.1	-800.0	-1,500.0
(Inc)/dec in Fixed Assets	-789.7	-746.9	-500.0	-500.0
Others	428.6	658.6	433.7	568.6
CF from investing activities	476.9	-966.4	-866.3	-1431.4
Issue/(Buy back) of Equity	0.0	0.0	0.0	0.0
Inc/(dec) in loan funds	35.9	62.2	-50.0	-50.0
Dividend paid & dividend tax	-410.3	-410.3	-272.6	-340.8
Others	96.1	-355.1	0.0	0.0
CF from financing activities	-278.2	-703.1	-322.6	-390.8
Net Cash flow	1,753.2	-14.7	-31.5	217.3
Opening Cash	1,212.0	2,965.2	2,950.5	2,918.9
Closing Cash	2965.2	2950.5	2918.9	3136.3

Source: Company, ICICI Direct Research

Exhibit 12: Balance Sheet				
	₹ crore			
(Year-end March)	FY19	FY20	FY21E	FY22E
Liabilities				
Equity Capital	27.3	27.3	27.3	27.3
Reserve and Surplus	8,891.4	9,953.6	10,950.6	12,552.3
Total Shareholders funds	8918.7	9980.9	10977.8	12579.6
Total Debt	186.8	249.0	199.0	149.0
Deferred Tax Liability	273.9	252.2	235.8	294.1
Others	120.8	156.6	151.7	169.3
Total Liabilities	9500.1	10638.6	11564.4	13192.0
Assets				
Gross Block	2,785.2	3,669.7	4,231.8	4,731.8
Less: Acc Depreciation	910.6	1,292.2	1,698.8	2,125.9
Net Block	1874.6	2377.5	2533.0	2605.9
Capital WIP	449.7	312.2	250.0	250.0
Total Fixed Assets	2,324.4	2,689.7	2,783.0	2,855.9
Investments	4,922.5	5,748.8	6,598.8	8,148.8
Inventory	633.4	572.4	469.1	585.1
Debtors	90.3	86.8	82.1	102.4
Others	252.5	252.4	236.1	294.4
Cash	2965.2	2950.5	2918.9	3136.3
Total Current Assets	3,941.4	3,862.0	3,706.2	4,118.1
Creditors	1,234.1	1,027.7	938.2	1,170.1
Provisions	33.0	33.9	31.0	38.6
Others	619.6	749.4	701.0	874.2
Total Current Liabilities	1,886.7	1,811.0	1,670.2	2,082.9
Net Current Assets	2054.7	2051.0	2036.1	2035.2
Other Non current asset	198.5	149.2	147.6	153.2
Application of Funds	9500.1	10638.6	11564.4	13192.0

Source: Company, ICICI Direct Research

Exhibit 13: Key ratios				
(Year-end March)	FY19	FY20	FY21E	FY22E
Per share data (₹)				
EPS	80.8	67.0	46.6	71.3
Cash EPS	91.8	81.0	61.5	86.9
BV	327.2	366.1	402.7	461.5
DPS	12.5	12.5	10.0	12.5
Cash Per Share	218.0	249.7	277.9	340.9
Operating Ratios (%)				
EBITDA Margin	29.6	23.8	20.0	22.6
PBT / Net sales	26.6	19.7	15.2	18.6
PAT Margin	22.6	20.0	14.8	18.2
Inventory days	23.6	22.8	20.0	20.0
Debtor days	3.4	3.5	3.5	3.5
Creditor days	46.0	41.0	40.0	40.0
Return Ratios (%)				
RoE	24.8	18.3	11.6	15.4
RoCE	27.8	17.2	11.4	15.3
RoIC	80.8	46.7	32.3	49.1
Valuation Ratios (x)				
P/E	27.7	33.6	48.3	31.6
EV / EBITDA	19.1	25.1	31.5	21.6
EV / Net Sales	5.7	6.0	6.3	4.9
Market Cap / Sales	6.3	6.7	7.2	5.7
Price to Book Value	6.9	6.1	5.6	4.9
Solvency Ratios				
Debt/E equity	0.0	0.0	0.0	0.0
Current Ratio	0.6	0.7	0.6	0.6
Quick Ratio	0.2	0.3	0.3	0.3

Source: Company, ICICI Direct Research

RATING RATIONALE

ICICI Direct endeavours to provide objective opinions and recommendations. ICICI Direct assigns ratings to its stocks according to their notional target price vs. current market price and then categorises them as Buy, Hold, Reduce and Sell. The performance horizon is two years unless specified and the notional target price is defined as the analysts' valuation for a stock

Buy: >15%;

Hold: -5% to 15%;

Reduce: -5% to -15%;

Sell: <-15%



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