

25 July 2024

## ZF Commercial Vehicles

*Improving CV visibility, export orders ramping up; upgrading to a Buy*

Slightly lagging ARe of Rs1.42bn, ZF Commercial Vehicles' Q1 EBITDA slipped 2% y/y to Rs1.38bn on higher employee cost. India's CV sector is likely to grow at a healthy 7% CAGR (earlier 5%), led by infra/economic activity and the low base. Content for CVs, due to government regulations, would increase in stages on penetration of ESC, AEBS, ADAS and EVs with potential to more than double ahead. The ESC regulation (Rs20,000/vehicle) for all buses would be implemented from Sep'25. The overseas CV sector could fall in CY24, but export revenue would outstrip that of the industry due to sourcing by global group companies. The EBITDA margin would expand due to greater scale and localisation benefits. After the recent share price fall and on improving domestic CV/export growth visibility, we upgrade to a Buy at a higher TP of Rs18,400, 55x FY26e P/E (earlier Rs17,300, 50x FY26e P/E).

**EBITDA slightly below estimates.** Q1 standalone revenue fell 2% y/y to Rs9.4bn (ARe Rs9.5bn), broadly in line with estimates. Product sales fell 4% to Rs8.25bn, while services grew 11% to Rs1.04bn. The underlying CV (>6 tonnes) production fell slightly, 3% y/y, 4% q/q, to 98,007 units. EBITDA slipped 2% to Rs1.38bn, slightly below our Rs1.42bn estimate, on higher employee cost. The EBITDA margin was flat y/y at 14.7%. The gross margin rose 260bps y/y to 40.8%, aided by price hike (70bps) and a better mix (OEM/aftermarket). Employee cost grew 19% y/y to Rs1.36bn due to headcount increase for service exports. Overall, PAT slipped 1% y/y to Rs992m (ARe Rs1bn), broadly in line with estimates. The subsidiary's revenue/EBITDA/PAT were Rs74m/8m/2m.

**Valuation.** We expect 18%/25% revenue/PAT CAGRs over FY24-26. We raise our FY25e/26e EBITDA 2% each, factoring in higher domestic CV volumes. We upgrade to a Buy at a higher TP of Rs18,400, 55x FY26e P/E (earlier Rs17,300, 50x FY26e P/E). The multiple is raised on better domestic CV demand visibility, and is the median of historical forward P/E. **Key downside risks:** Less-than-expected growth in underlying segments and delay in new regulations for CVs.

Key financials (YE Mar)	FY22	FY23	FY24	FY25e	FY26e
Sales (Rs m)	25,434	34,446	37,837	43,463	52,784
Net profit (Rs m)	1,421	3,177	4,048	4,937	6,322
EPS (Rs)	74.9	167.5	213.4	260.3	333.3
P/E (x)	204.3	91.4	71.7	58.8	45.9
EV / EBITDA (x)	110.7	59.0	49.2	40.5	31.7
P/BV (x)	13.7	12.0	10.4	9.0	7.6
RoE (%)	5.2	10.5	11.7	12.3	13.4
RoCE (%)	7.3	14.5	16.0	16.7	18.2
Dividend yield (%)	0.1	0.1	0.1	0.1	0.2
Net debt / equity (x)	-0.5	-0.5	-0.5	-0.5	-0.5

Source: Company, Anand Rathi Research

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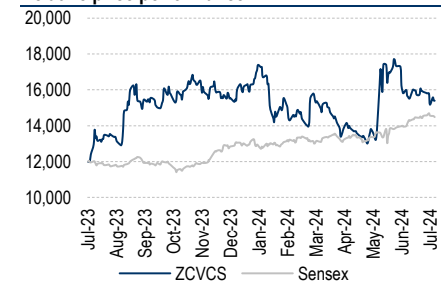
Rating: **Buy**  
Target Price: Rs.18,400  
Share Price: Rs.15,303

Key data	ZCVCS IN / WIL.BO
52-week high / low	Rs.18,250 / 11,684
Sensex / Nifty	80,040 / 24,406
3-m average volume	\$8m
Market cap	Rs.290bn / \$3,467.6m
Shares outstanding	19m

Shareholding pattern (%)	Jun'24	Mar'24	Dec'23
Promoters	67.5	75.0	75.0
- of which, Pledged	-	-	-
Free float	25.0	25.0	25.0
- Foreign institutions	3.7	2.2	2.0
- Domestic institutions	21.2	15.8	15.8
- Public	7.6	7.0	7.2

Estimates revision (%)	FY25e	FY26e
Sales	0.7	1.6
EBITDA	0.7	1.8
EPS	-3.3	-3.9

### Relative price performance



Source: Bloomberg

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## Quick Glance – Financials and Valuations

**Fig 1 – Income statement (Rs m)**

Year-end: Mar	FY22	FY23	FY24	FY25e	FY26e
Net revenues	25,434	34,446	37,837	43,463	52,784
Growth (%)	36.5	35.4	9.8	14.9	21.4
Raw material	16,433	21,971	23,211	26,566	32,341
Employee & other expenses	6,475	7,772	8,995	10,144	11,900
<b>EBITDA</b>	<b>2,525</b>	<b>4,703</b>	<b>5,631</b>	<b>6,753</b>	<b>8,544</b>
EBITDA margins (%)	9.9	13.7	14.9	15.5	16.2
- Depreciation	924	1,048	1,095	1,178	1,270
Other income	375	670	958	1,073	1,226
Interest expenses	19	57	50	50	50
PBT	1,957	4,269	5,444	6,598	8,449
Effective tax rates (%)	27	26	26	25	25
+ Associates / (Minorities)	-	-	-	-	-
Adjusted income	1,421	3,177	4,048	4,937	6,322
Extraordinary items	-	-	-	-	-
Net income	1,421	3,177	4,048	4,937	6,322
WANS	19	19	19	19	19
FDEPS (Rs)	74.9	167.5	213.4	260.3	333.3
Growth (%)	36.9	123.6	27.4	22.0	28.1

**Fig 2 – Balance sheet (Rs m)**

Year-end: Mar	FY22	FY23	FY24	FY25e	FY26e
Share capital	95	95	95	95	95
Net worth	21,141	24,091	27,887	32,429	38,245
Debt	-	-	-	-	-
Minority interest	-	-	-	-	-
DTL / (Assets)	-185	-220	-290	-296	-305
<b>Capital employed</b>	<b>20,956</b>	<b>23,871</b>	<b>27,597</b>	<b>32,132</b>	<b>37,940</b>
Net tangible assets	5,357	5,855	6,538	7,235	8,227
Goodwill	-	-	-	-	-
CWIP (tang. & intang.)	203	768	825	950	1,188
Investments (strategic)	10	10	177	177	177
Investments (financial)	3,981	1,001	233	4,410	8,410
Current assets (excl. cash)	9,941	10,656	12,713	14,603	17,735
Cash	6,691	11,687	12,918	12,115	11,180
Current liabilities	5,226	6,107	5,807	7,357	8,977
Working capital	4,715	4,549	6,906	7,246	8,758
<b>Capital deployed</b>	<b>20,956</b>	<b>23,871</b>	<b>27,597</b>	<b>32,132</b>	<b>37,940</b>

**Fig 3 – Cash-flow statement (Rs m)**

Year-end: Mar	FY22	FY23	FY24	FY25e	FY26e
PBT	1,957	4,269	5,464	6,598	8,449
+ Non-cash items	757	1,104	232	1,228	1,320
Oper. prof. before WC	2,714	5,373	5,696	7,826	9,769
- Incr. / (decr.) in WC	453	756	1,990	411	1,623
Others incl. taxes	879	1,629	1,778	1,667	2,135
Operating cash-flow	1,383	2,987	1,929	5,747	6,011
- Capex (tang. + intang.)	1,763	1,276	1,980	2,000	2,500
Free cash-flow	-381	1,712	-52	3,747	3,511
Acquisitions	-	-	-	-	-
- Div. (incl. taxes)	209	228	247	324	395
+ Equity raised / buyback	-	-	-	-	-
+ Debt raised	-	-	-	-	-
- Fin investments	178	1,816	-810	4,177	4,000
- Misc. (CFI + CFF)	(2,839)	(5,328)	(719)	50	50
Net cash-flow	2,071	4,996	1,231	-803	-934

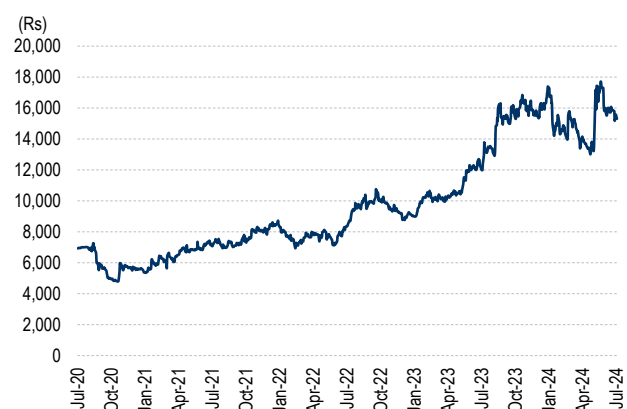
Source: Company, Anand Rathi Research

**Fig 4 – Ratio analysis**

Year-end: Mar	FY22	FY23	FY24	FY25e	FY26e
P/E (x)	204.3	91.4	71.7	58.8	45.9
EV / EBITDA (x)	110.7	59.0	49.2	40.5	31.7
EV / Sales (x)	11.0	8.1	7.3	6.3	5.1
P/B (x)	13.7	12.0	10.4	9.0	7.6
RoE (%)	5.2	10.5	11.7	12.3	13.4
RoCE (%) - after tax	7.3	14.5	16.0	16.7	18.2
RoIC (%) - after tax	14.9	28.7	30.4	31.4	35.6
DPS (Rs)	12.0	13.0	17.1	20.8	26.7
Dividend yield (%)	0.1	0.1	0.1	0.1	0.2
Dividend payout (%)	16.0	7.8	8.0	8.0	8.0
Net debt / equity (x)	-0.5	-0.5	-0.5	-0.5	-0.5
Receivables (days)	96	80	90	90	90
Inventory (days)	21	16	16	16	16
Payables (days)	51	38	36	36	36
CFO : PAT (%)	97	94	48	116	95

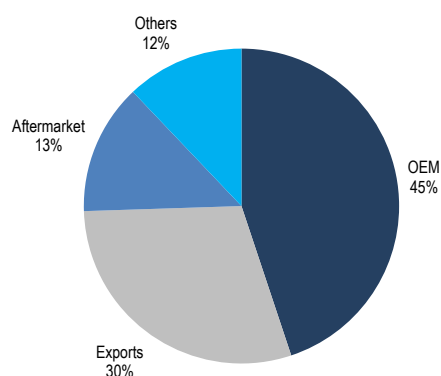
Source: Company, Anand Rathi Research

**Fig 5 – Price movement**



Source: Bloomberg

**Fig 6 – Revenue mix (Q1 FY25)**



Source: Company

## Quarterly financials

Fig 7 – Quarterly performance

(Rs m)	Q1 FY24	Q2 FY24	Q3 FY24	Q4 FY24	Q1 FY25	Y/Y (%)	Q/Q (%)	FY25e	FY24	Y/Y (%)
<b>Revenue</b>	<b>9,605</b>	<b>9,808</b>	<b>8,868</b>	<b>9,555</b>	<b>9,383</b>	<b>(2.3)</b>	<b>(1.8)</b>	<b>43,463</b>	<b>37,837</b>	<b>14.9</b>
<b>Expenditure</b>	<b>8,193</b>	<b>8,368</b>	<b>7,558</b>	<b>8,086</b>	<b>8,001</b>	<b>(2.3)</b>	<b>(1.1)</b>	<b>36,710</b>	<b>32,206</b>	<b>14.0</b>
as % of sales	85.3	85.3	85.2	84.6	85.3			84.5	85.1	
Consumption of RM	5,936	6,067	5,445	5,764	5,557	(6.4)	(3.6)	26,566	23,211	14.5
as % of sales	61.8	61.9	61.4	60.3	59.2			61.1	61.3	
Employee cost	1,145	1,162	1,158	1,175	1,363	19.0	15.9	5,343	4,640	15.2
as % of sales	11.9	11.8	13.1	12.3	14.5			12.3	12.3	
Other expenditure	1,113	1,140	955	1,147	1,082	(2.8)	(5.7)	4,801	4,355	10.2
as % of sales	11.6	11.6	10.8	12.0	11.5			11.0	11.5	
<b>EBITDA</b>	<b>1,412</b>	<b>1,440</b>	<b>1,310</b>	<b>1,469</b>	<b>1,382</b>	<b>(2.1)</b>	<b>(5.9)</b>	<b>6,753</b>	<b>5,631</b>	<b>19.9</b>
<b>EBITDA margins (%)</b>	<b>14.7</b>	<b>14.7</b>	<b>14.8</b>	<b>15.4</b>	<b>14.7</b>			<b>15.5</b>	<b>14.9</b>	
Depreciation	276	270	261	287	287	3.7	(0.0)	1,178	1,095	7.6
<b>EBIT</b>	<b>1,136</b>	<b>1,170</b>	<b>1,049</b>	<b>1,182</b>	<b>1,095</b>	<b>(3.6)</b>	<b>(7.4)</b>	<b>5,575</b>	<b>4,537</b>	<b>22.9</b>
Other income	214	242	302	200	255	19.2	27.6	1,073	958	12.0
Interest	13	13	14	10	18	33.4	82.0	50	50	-
<b>PBT</b>	<b>1,337</b>	<b>1,399</b>	<b>1,337</b>	<b>1,372</b>	<b>1,333</b>	<b>(0.3)</b>	<b>(2.9)</b>	<b>6,598</b>	<b>5,444</b>	<b>21.2</b>
Total tax	339	355	341	362	340	0.5	(5.8)	1,661	1,396	18.9
<b>Adj. PAT</b>	<b>998</b>	<b>1,043</b>	<b>996</b>	<b>1,011</b>	<b>992</b>	<b>(0.5)</b>	<b>(1.8)</b>	<b>4,937</b>	<b>4,048</b>	<b>22.0</b>
Extraordinary items (loss) / gain	-	-	-	-	-			-	-	
<b>Reported PAT</b>	<b>998</b>	<b>1,043</b>	<b>996</b>	<b>1,011</b>	<b>992</b>	<b>(0.5)</b>	<b>(1.8)</b>	<b>4,937</b>	<b>4,048</b>	<b>22.0</b>
<b>Adj. EPS (Rs)</b>	<b>52.6</b>	<b>55.0</b>	<b>52.5</b>	<b>53.3</b>	<b>52.3</b>	<b>(0.5)</b>	<b>(1.8)</b>	<b>260.3</b>	<b>213.4</b>	<b>22.0</b>
<b>Margins (%)</b>						<b>(bps)</b>	<b>(bps)</b>			<b>(bps)</b>
Gross	38.2	38.1	38.6	39.7	40.8	257	110	38.9	38.7	22
EBIDTA	14.7	14.7	14.8	15.4	14.7	3	-65	15.5	14.9	65
EBIT	11.8	11.9	11.8	12.4	11.7	-15	-70	12.8	12.0	84
PAT	10.4	10.6	11.2	10.6	10.6	19	-0	11.4	10.7	66
Effective tax rates	25.4	25.4	25.5	26.4	25.6	19	-80	25.2	25.6	(48)

Source: Company

## Earnings call takeaways

- Q1 FY25 CV (>6 tonnes) production slid 3% y/y to 98,007 vehicles. The shift in mix toward ILCV drove lower content per vehicle (tractor trailer share reduced by 13%). **The company maintains its FY25 outlook for single-digit domestic CV industry growth.**
- **OEM.** Q1 revenue fell 4% y/y to Rs4.3bn due to lower production and an adverse ILCV mix. Growth to improve, led by better CV demand and new products (lift axle control systems), deeper penetration of EV (e-compressors and electronic braking systems) and potential government mandates relating to advanced driver-assistance systems (advanced emergency braking and lane-departure warning).
- **Exports.** Q1 export sales dipped 6% y/y to Rs2.78bn due to delay in sea cargoes (lead time increased from six to eight to nine weeks) and slowdown for BMW (-12%). However, the company **maintains its 15-20% revenue growth outlook for FY25**, led by rising order-books in the bus segment in Europe and the electric trucks segment in the US, new projects related to clutch compressors and actuator assemblies for OEM customers. To clear some back orders, the company is adding another line in Oragadam. New product dual-cylinder high-end compressors to be launched from Aug'24. The new compressor line for Daimler would start in a couple of months.
- **Aftermarket.** Q1 revenue grew 4% y/y to Rs1.26bn. Growth drivers are increase in sale of door-control systems, and OEM-spares segment growing 46% due to greater consumption of BS6 and EV products (e-compressor kits and filters). Growth in coming quarters would be supported by deeper penetration of the torque-control system providing ADAS and driver-behaviour-monitoring systems to a leading corporate customer for its employees' transport.
- **Export of services.** Q1 revenue grew 11% y/y to Rs1bn, led by the rise in engineering and related support activities to global digital business.
- **Digital business.** Q1 saw 40% growth y/y. Two types of revenue streams: from selling hardware to OEMs and from subscriptions. Both amount to Rs800m a year. Ahead, major growth to come from the aftermarket and subscription revenues, while OEMs would like to have their own solutions.
- **Margins.** The gross margin rose, mainly due to price hikes (Rs70m). The company expects margins ahead to improve. Employee cost rose due to rise in headcount (120) in export services.
- **Domestic EV buses demand.** In Q1 FY24, demand was ~1,200+ compressors; in Q1 FY25, it dropped ~53% to 550 as these were produced based on tenders, government programs, etc.
- **The Oragadam plant** produces electric compressors, hydraulic ESC, double-diaphragm spring-break actuators and automatic slack-adjusters, etc. Key product launches in Q1 were electric compressors, AMTs, air-processing units, ECAS and ECU for domestic OEMs and actuator 4.0 for export.

## Valuation

**More content because of regulations and EVs.** Content to increase in stages, led by **regulations** regarding electronic-stability controls (Rs20,000/vehicle), advanced emergency-braking systems (Rs30,000), advanced driver-assistance systems (Rs10,000-80,000), disc-brake levers (Rs40,000-80,000) and telematics. Electric vehicles and trailer penetration would drive products such as electric compressors (Rs80,000), EBS (Rs60,000) and trailer ABS (Rs30,000).

**Exports** to be driven by market-share gains in CVs/PVs from group companies. The wider distribution network and retrofitment solutions would drive the **aftermarket**. **Service** revenue would increase, led by more software sales and R&D support to group companies.

**Better CV visibility.** India's CV sector is likely to see a healthy 7% CAGR over FY24-26. The overseas CV sector could fall in CY24, but export revenue would outstrip that of the industry due to sourcing by global group companies.

**View, Valuations.** We expect an 18% revenue CAGR over FY24-26, led by 18% export growth, 18% OEM growth and the aftermarket at 11%. We expect 18%/23% revenue/EBITDA CAGRs over FY24-26. We recommend a Buy at a TP of Rs18,400, 55x FY26e P/E.

**Fig 8 – Change in estimates**

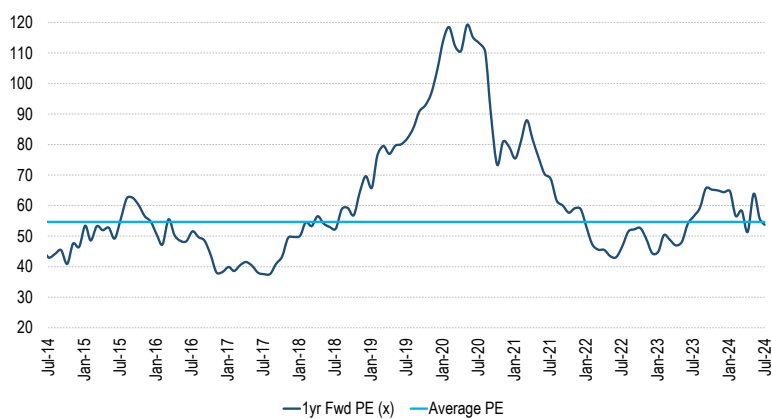
(Rs m)	Old		Revised		Change (%)	
	FY25e	FY26e	FY25e	FY26e	FY25	FY26
Revenue	43,165	51,950	43,463	52,784	0.7	1.6
EBITDA	6,707	8,396	6,753	8,544	0.7	1.8
% of revenue	15.5	16.2	15.5	16.2		
Adj. PAT	5,107	6,581	4,937	6,322	-3.3	-3.9
EPS (Rs)	269.2	347.0	260.3	333.3	-3.3	-3.9

Source: Anand Rathi Research

**Fig 9 – Key assumptions**

Segmental revenue (Rs m)	FY19	FY20	FY21	FY22	FY23	FY24	FY25e	FY26e	CAGR FY24-26 (%)
OEM	15,302	7,695	6,848	10,311	15,976	18,201	21,033	25,431	18
Y/Y change, %	11	-50	-11	51	55	14	16	21	
Exports	8,222	6,985	7,218	9,443	10,999	10,747	12,037	15,046	18
Y/Y change, %	6	-15	3	31	16	-2	12	25	
Aftermarket	2,983	2,599	2,598	3,340	4,291	4,785	5,264	5,895	11
Y/Y change, %	4	-13	-0	29	28	12	10	12	
Other operating income	2,035	2,016	1,971	2,340	3,180	4,104	5,130	6,412	25
Y/Y change, %	48	-1	-2	19	36	29	25	25	
<b>Revenues</b>	<b>28,541</b>	<b>19,296</b>	<b>18,635</b>	<b>25,434</b>	<b>34,446</b>	<b>37,837</b>	<b>43,463</b>	<b>52,784</b>	<b>18</b>
Y/Y change, %	11	-32	-3	36	35	10	15	21	

Source: Company, Anand Rathi Research

**Fig 10 – Valuation chart (1-year forward P/E) – Historical median is 55x**

Source: Bloomberg, Anand Rathi Research

### Downside risks

- Less-than-expected growth in underlying segments.
- Delay in new regulations for CVs.

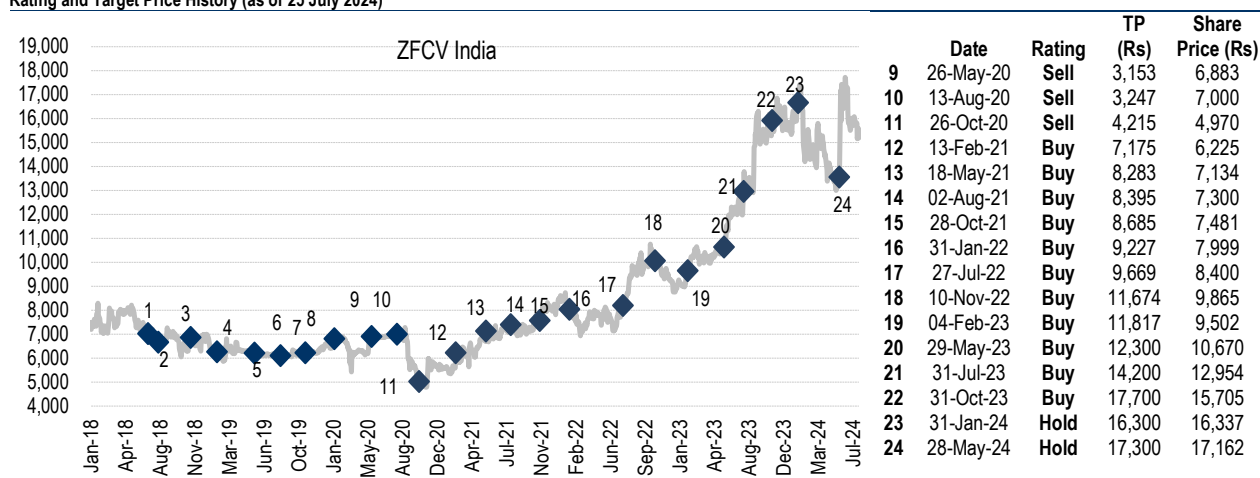
## Appendix

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#### Rating and Target Price History (as of 25 July 2024)



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	Buy	Hold	Sell
Large Caps (Top 100 companies)	>15%	0-15%	<0%
Mid Caps (101st-250th company)	>20%	0-20%	<0%
Small Caps (251st company onwards)	>25%	0-25%	<0%

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