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Stock details

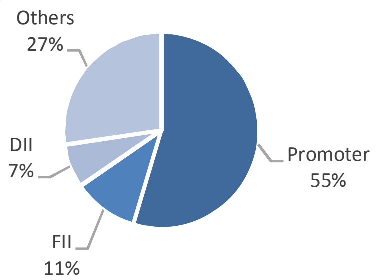
BSE code	:	505714
NSE code	:	GABRIEL
Market cap (Rs mn)	:	14,185
Free float (%)	:	45.4
52 wk Hi/Lo (Rs)	:	102/75
Avg daily volume (mn)	:	0.4
Shares (o/s) (mn)	:	144

Summary table

(Rs mn)	FY16	FY17E	FY18E
Sales	14,382	16,207	18,636
Growth (%)	(0.4)	12.7	15.0
EBITDA	1,275	1,451	1,769
EBITDA margin (%)	8.9	9.0	9.5
PBT	955	1,148	1,483
Net profit	752	861	1,112
EPS (Rs)	5.2	6.0	7.7
Growth (%)	25.3	14.4	29.2
CEPS (Rs)	7.5	8.5	10.4
BV (Rs/share)	26.4	30.7	36.6
Dividend/share (Rs)	1.2	1.4	1.6
ROE (%)	21.5	21.1	23.0
ROCE (%)	26.3	27.0	29.7
Net cash (debt)	253	770	1,413
NW Capital (Days)	28	25	24
P/E (x)	18.7	16.4	12.8
P/BV (x)	3.7	3.2	2.7
EV/Sales (x)	1.0	0.8	0.7
EV/EBITDA (x)	10.8	9.2	7.2

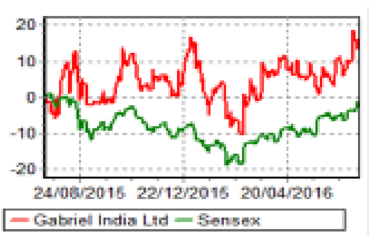
Source: Company, Kotak Securities - Private Client Research

Shareholding pattern



Source: Capitaline

One-year performance (Rel to Sensex)



Source: Capitaline

Gabriel India Ltd (Gabriel)

PRICE: RS.99 — **RECOMMENDATION: BUY**

TARGET PRICE: RS.124 — **FY18E PE: 12.8X**

Gabriel is the flagship company of ANAND Group. Gabriel was set up in 1961 in collaboration with Maremont Corporation (now Gabriel Ride Control Products of Arvin Meritor Inc, USA). The company provides wide range of ride control products, including shock absorbers, struts and front forks to the automotive segment. With 83% revenues coming from OEM's, Gabriel will be a key beneficiary of demand revival in the auto sector. Focus on aftermarket and export will further add to the growth. EBITDA margin improvement will likely continue over FY17/ FY18E. We thereby expect robust earnings CAGR growth of 21% over FY16-FY18E. Debt-free balance sheet, strong free cash flow and healthy return ratios provides high comfort. We initiate coverage on Gabriel with a BUY rating and price target of Rs124.

Key investment argument

- **Expect cyclical recovery for two-wheeler segment over FY16-FY18**. Gabriel generates close to 60% of revenues from the two wheeler segment. Given the significant exposure, revival in two wheeler demand holds significance for Gabriel. We expect the two wheeler volume growth in FY17/FY18 to grow in double digits as compared to mid-single digit CAGR witnessed in the past four years. Forecast of good monsoon, seventh pay commission payout, pent-up demand and expected improvement in macro-economic situation are the key demand growth drivers for the two wheeler industry, in our view. Expected recovery coupled with higher share of business from faster growing clients will likely translate into healthy double-digit revenue growth from the two wheeler segment.

- **Passenger car segment to grow at a healthy pace.** 30% of Gabriel's revenues comes from selling products to OEM in the passenger vehicle segment. Post an elongated phase of sluggish demand since FY12, the passenger vehicle industry did show some revival with 7% volume growth in FY16 (highest in the past 5 years). Backed by expectation of normal monsoon, seventh pay commission impact, likely pick-up in the economy and huge pent-up demand in the system, we expect recovery to gain further strength in FY17 and FY18. With improved growth prospects for the passenger vehicle industry, we expect Gabriel to report healthy 13% CAGR growth in revenues from the passenger vehicle segment.

- **Company to focus on aftermarket segment.** Gabriel India has a strong brand equity in the aftermarket segment and has a ~30% market share in that segment (organized and unorganized combined). Unorganized market accounts for ~40% of the aftermarket sales. Between FY10-FY16, share of aftermarket revenues in the overall revenue mix increased from ~8.5% in FY10 to 13% in FY16. Company will continue to focus on increasing aftermarket revenue share in the overall mix through further strengthening of brand, enhancing distribution network and introduction of new products. Company considers aftermarket to be a major driver for future growth.

- **Diversified business model**. Unlike certain auto ancillary companies that have high dependence on single vertical/client, Gabriel generates revenues across all auto segments and diverse set of clients. Gabriel generates ~60% of the revenues from the two wheeler segment, ~30% from passenger car segment and ~10% from the commercial vehicle segment. In terms of channel mix - the company is working on increasing its exposure from non-OEM's. Share of revenues from OEM's has come down from 90% in FY10 to 83% in FY16. Apart from this, the revenues are scattered across various clients and no single client accounts for more than 15% of Gabriel's revenues. Gabriel's diversified business model provides cushion to the company's revenues and profitability during underperformance by a segment/channel/clientele.

- **Debt free company with strong free cash flows.** From a high of Rs1.57bn in FY09, gross debt as of end FY16 stood at a mere Rs109mn. With cash of Rs362mn, the company is net debt free. With expected healthy earnings growth, no significant capex and efficient working capital management, we expect free cash flows for the company to remain strong over FY17/FY18. We expect free cash flow generation of Rs1.68bn over FY17/FY18 for the company.

Valuation

We expect Gabriel's earnings to grow at a healthy CAGR of 21% over FY16-FY18E, better than last five years (FY11-FY16) CAGR of 10%. Gabriel's balance sheet has improved substantially in the past few years and we foresee further strengthening with strong free cash flow and no major capex.

At the CMP of Rs99, the stock trades at a PE of 12.8x and P/CEPS of 9.5x based on FY18E EPS of Rs7.7 and CEPS of Rs10.4. We value the company at a PE of 16x on FY18 estimated EPS of Rs7.7 and arrive at a target price of Rs124. We initiate coverage on Gabriel India Limited with **BUY** rating and price target of Rs124.

Key Risks

- **Slowdown in automobile growth** - 83% of Gabriel's revenues come from its products fitted in new vehicles. We are expecting demand recovery in the automotive sector in FY17 and pick-up in growth in FY18. Delay in demand pick-up will impact Gabriel's revenues and profitability.

- **Growth to be limited from existing business segment** - Gabriel has various group companies that supply various auto ancillary product to the OEM's. There is low probability of Gabriel adding new business segments, thereby limiting growth to that extent.

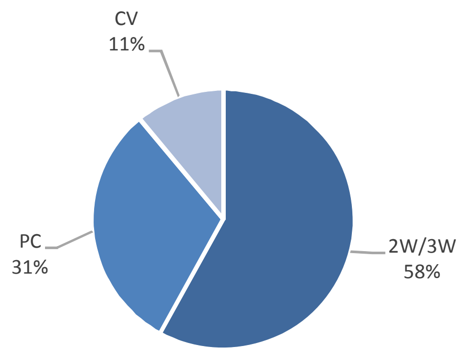
Company Background

Gabriel was set up in 1961 in collaboration with Maremont Corporation (now Gabriel Ride Control Products of Arvin Meritor Inc, USA) to manufacture shock absorbers. Gabriel has been the pioneer of Ride Control Products in India.

Gabriel is a well-recognized and respected ride control brand in India. Gabriel's brand in India and overseas is synonymous with shock absorbers. Company sells its products to OEM's and also in the replacement market. Gabriel has seven manufacturing facilities in India which are located in close proximity to OEMs.

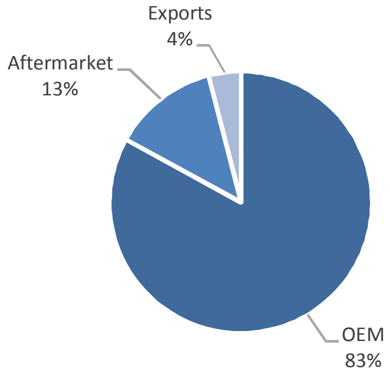
Gabriel supplies front forks, hydraulic shock absorbers and gas shock absorbers to the two wheeler segment, McPherson struts and shock absorbers to the passenger vehicle segment and cabin/seat dampers to the commercial vehicle segment.

Gabriel - FY16 revenue mix by segment



Source: Company

Gabriel - FY16 revenue mix by channel



Source: Company

Gabriel Manufacturing Facilities

Location	Commenced Poduction	Products Manufactured	Segment served	Major
Ambad (Nashik)	1990	Shock absorbers and Front forks	2W/3W	Bajaj, Yamaha, Piaggio M&M, HMSI Mahindra GenZe (USA)
Hosur (Karnataka)	1997	Shock absorbers and Front forks	2W/3W	TVS, Suzuki, HMSI, Yamaha, Royal Enfield
Parwanoo (HP)	2007	Shock absorbers Front forks and Struts	2W/3W, Passenger Cars, Commercial Vehicles	TVSM, Tata Motors and M&M Aftermarket
Chakan (Pune)	1997	Shock absorbers and Struts	Passenger Cars, Commercial Vehicles and Railways	Tata Motors, Renault, General Motors, M&M, Volkswagen, Toyota, Bajaj Piaggio and Railways
Khandsa (Gurgaon)	2008	Shock absorbers / Struts	Passenger cars	Maruti, Honda Cars and Tata Motors
Dewas (MP)	1992	Shock absorbers	Commercial vehicles	Tata Motors, M&M, Ashok Leyland Bharat Benz, VECV, Force, Man Trucks, AMW, Wheels India, Ride Control LLC (US)
Sanand (Gujarat)	2010	Shock Absorbers and Struts	2W/3W, Passenger Cars	Tata Motors and HMSI
Malur (Karnataka) Satellite Plant	2013	Shock absorbers	2W/3W	HMSI
Aurangabad Satellite Plant	2014	Shock absorbers	2W/3W	Bajaj Auto

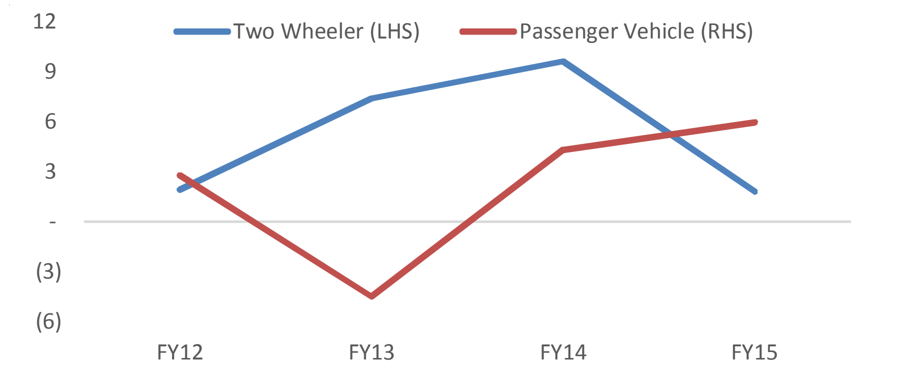
Source: Company

Investment Arguments

Gabriel to be a key beneficiary of auto sector demand revival

With 83% revenues coming from OEM's, Gabriel will be a key beneficiary of demand revival in the auto sector. In the past four years, the two wheeler and the passenger car segments grew at a sluggish pace. Over the next two years, we expect both, the two wheeler and the passenger car segment, to witness a healthy double-digit growth. Of the OEM revenues, 90% (72% of overall revenues) comes from the two wheeler and passenger car segment and expected revival in these segments augurs well for Gabriel.

Sluggish production growth for the 2W/PV segment (%)



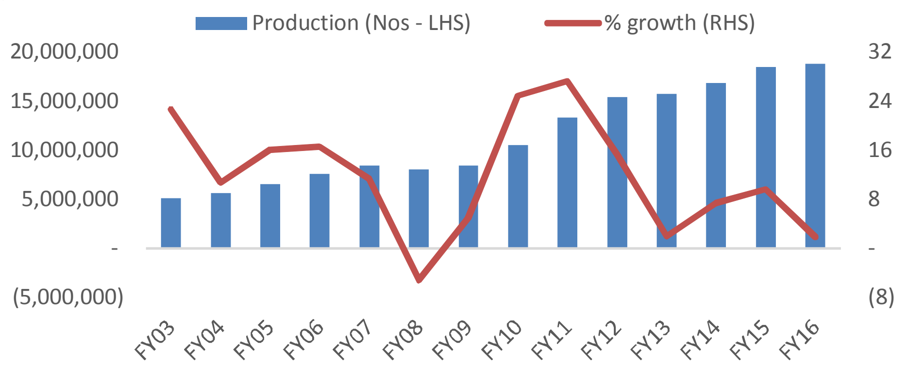
Source: SIAM, Kotak Securities - Private Client Research

Expect cyclical recovery for two-wheeler segment over FY16-FY18

Gabriel generates close to ~60% of revenues from the two/three wheeler segments. Fall in two wheeler segment revenues in FY16 led to share of the two wheeler segment coming down to 58%, from 63% in FY15. Given, significant exposure to two wheeler segment, revival in two wheeler demand holds significance for Gabriel.

Two wheeler production in the country grew at a CAGR of 5% between FY12-FY16, lower than longer term average CAGR of 14% achieved between FY02-FY12. Since FY03, this has been the longest slowdown period for the two wheeler industry. Slowdown in the economic growth since FY12 dampened demand sentiments for two wheelers. High base and challenging economic situation led to two wheeler production growth declining from 15% in FY12 to 2% in FY13. Back-to-back poor monsoons worsened demand sentiments further. Accordingly, two wheeler demand remained subdued in the past four years.

2W Production and growth - current slowdown is the longest since FY03



Source: SIAM, Kotak Securities - Private Client Research

However, situation is set to improve over the next two years and we expect the two wheeler volume in FY17/FY18 to witness double digit growth as compared to CAGR of mid-single digit witnessed in the past four years. Forecast of good monsoon, seventh pay commission payout, pent-up demand and expected improvement in macro-economic situation are the key demand growth drivers for the two wheeler industry, in our view.

Good monsoon forecast comes as a major relief

IMD has predicted that India will receive normal to above-normal monsoons this year. While good monsoon is always important for rural consumption growth, the significance has increased this year post two consecutive poor monsoons. Weak monsoon in the past two years coupled with other factors that include slow increase in MSP, dented the two wheeler demand and the same translated into mere 2% CAGR growth for motorcycles/mopeds over FY13-FY16. We note that the slowdown in rural areas has bottomed out and expect recovery from FY17 onwards. We view good monsoons, outflow from seventh pay commission and higher spend by the government (as indicated in the budget speech) to lead recovery in rural consumption.

Seventh pay commission to stimulate growth

Strong growth in consumption post sixth pay commission payouts have led to high hopes of seventh pay commission boosting consumption in FY17. The 7th Central Pay commission (CPC) has recommended a ~23.5% hike in salary levels of central government employees.

Strong growth in consumption post sixth pay commission implementation can be attributed to higher revision in pay scale and high arrear payment as sixth CPC was implemented with a lag. Further, during the same time, excise duties were reduced and interest rates were also low. All this factors translated into 22% CAGR growth in domestic 2W volumes over FY09-FY12. Though the recommended hike is lower than ~35% hike implemented by the 6th pay commission and there might not be any significant arrear payout (as implementation is expected in FY17 itself), we believe that seventh pay commission will likely stimulate consumption demand - though the extent may not be similar to sixth pay commission. We opine that convergence of seventh pay commission payout with good monsoon and weak base gels well for healthy pick-up in two wheeler demand.

Higher share of business with faster growing clients

In the 2W segment, Munjal Showa and Endurance are key competitors of Gabriel. Both of Gabriel's key competitors enjoys an inherent advantage of strong relationship with the top two wheeler manufacturer in India. For HMC, Munjal Showa is the only source for shock absorbers and thereby Gabriel does not get any business from the country's largest manufacturer. In case with Bajaj Auto, Endurance is the largest supplier and Gabriel's share of business is capped at 20%.

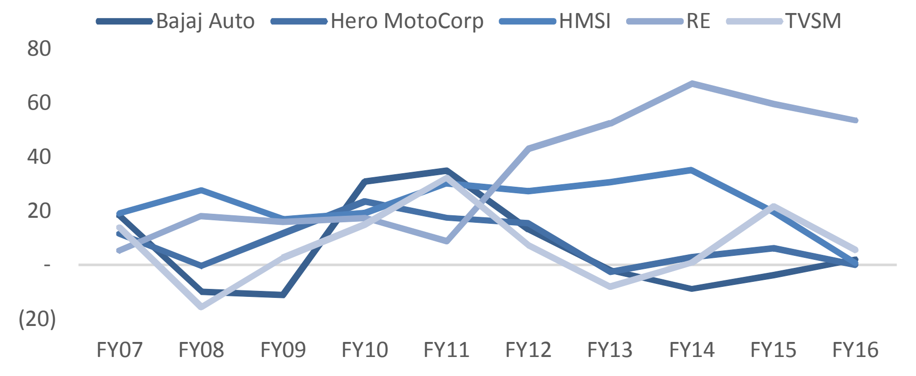
However, Gabriel derives significant business from other two wheeler players. Honda Scooters and Motorcycle India (HMSI) is the second largest and fastest growing two wheeler maker in India. With no business generation from HMC and limited business from Bajaj Auto, strong relationship with HMSI is of utmost importance for Gabriel India for sustaining strong market share in the domestic two wheeler segment. With HMSI, Gabriel has strong presence in the scooter segment. Along with Munjal Showa, Gabriel has been supplying suspension products to HMSI's Manesar and Tapukara plant. Gabriel was then selected as an approved vendor, along with Endurance, for HMSI's third plant near Bengaluru. Recently, HMSI started production at its fourth plant in Gujarat (scooters only) and Gabriel was selected as a vendor, along with Endurance.

Gabriel gets high share of business from TVS Motors, by supplying suspension products across all segments (Scooter/Motorcycle/Moped/Three wheeler). Gabriel also garners high share of business from Yamaha India, Suzuki Motorcycles and Royal Enfield. Gabriel's overall market share with OEM's is ~25%.

In recent times, Gabriel has added new clients/products like Vespa Aprilia, Mahindra Peugeot, Suzuki Gixxer, Suzuki scooter and new platforms from Royal Enfield.

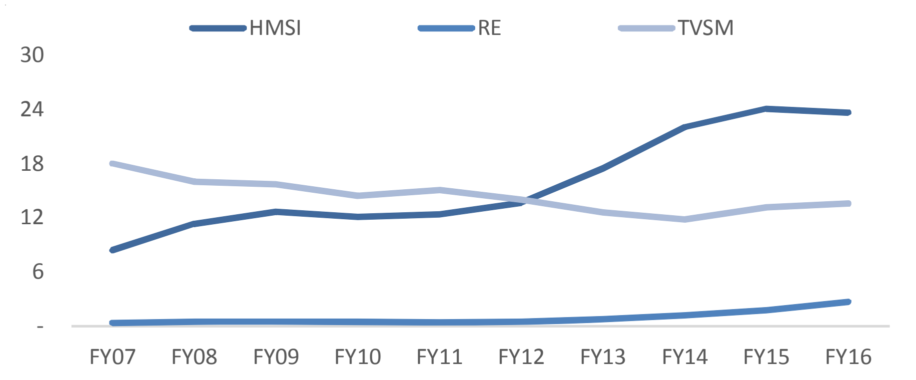
TVS Motors, Honda Motorcycle and Scooters India and Royal Enfield are Gabriel's top revenue contributor within the two wheeler segment. Most of these OEM's has been outperforming the industry growth for the past few years. Going ahead, we expect these players to continue outperforming the industry growth. In 1QFY17, key clients like HMSI/TVSM/Royal Enfield witnessed two wheeler YoY production growth of 27%/22%/40% respectively.

2W OEM's growth trend - Gabriel's key clients are growing at a strong pace (%)



Source: SIAM

2W OEM's market share trend - Gabriel's key clients are gaining market share (%)



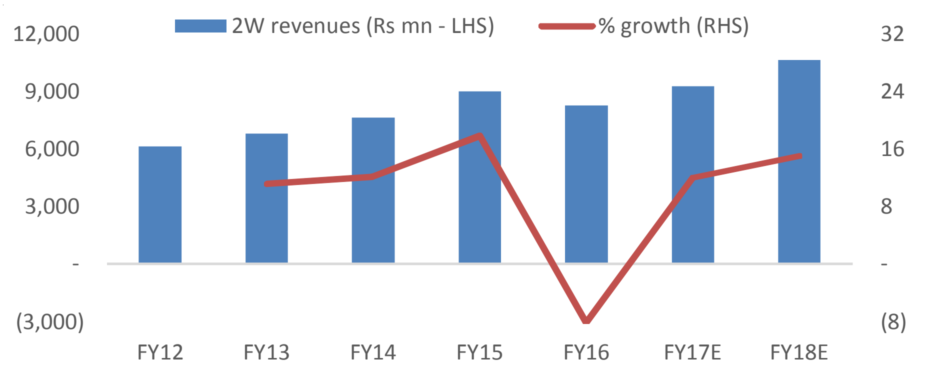
Source: SIAM

On the back of additional scooter capacity and new products, HMSI has set 18% volume growth target for FY17. Led by continued strong demand for scooters, we expect HMSI to continue gaining market share in the domestic two wheeler segment. Over the past few years, Gabriel have been gaining business traction with HMSI and hence it bodes well for Gabriel's growth prospects.

For TVSM, the top priority has been gaining market share. With strong scooter portfolio, new launches in the motorcycle industry and expected growth revival in moped sales, we expect TVSM to grow better than the industry. Royal Enfield (RE) continues to attract waiting period for its products. Capacity addition in CY16/CY17 will lead to higher sales growth for RE.

Gabriel's 2W/3W segment revenues are expected to grow at a healthy pace over FY16-FY18. Pick-up in two wheeler demand and expected strong growth from Gabriel's client are the key revenue growth drivers for Gabriel. Share of 2W business in the overall revenues declined from 63% in FY15 to 58% in FY16. Going ahead, we expect the share to broadly remain stable as we anticipate growth across all business verticals.

Gabriel - Revenue growth from two wheeler segment

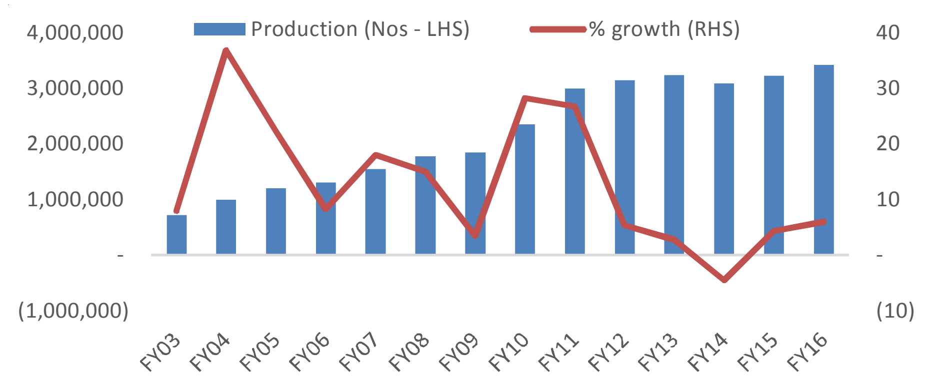


Source: Company, Kotak Securities - Private Client Research

Passenger car segment to grow at a healthy pace

Production of passenger vehicles in the country slowed down to 3% (CAGR) between FY11-FY16 as compared with 13% production CAGR over FY03-FY11 and long term CAGR of ~11%. Passenger car production in the country increased 4x between FY03 and FY11, increasing the base substantially. Higher base, coupled with slowdown in the economy, significantly slowed down passenger car demand. Demand for cars in the country is still subdued and is largely driven by new launches.

Passenger Vehicle Production and growth - five years of sluggish growth



Source: SIAM, Kotak Securities - Private Client Research

In FY16, the industry did show some revival with 7% volume growth (highest in the past 5 years) and we expect the recovery to gain further strength in FY17 and FY18. Factors such as expectation of normal monsoon, seventh pay commission impact and pick-up in the economy will likely translate into strong growth for the domestic passenger vehicle industry. Given tepid growth in the past five years, we expect robust pent-up demand to come into play upon revival of demand sentiments. We thereby expect healthy recovery in passenger car demand over the next few years.

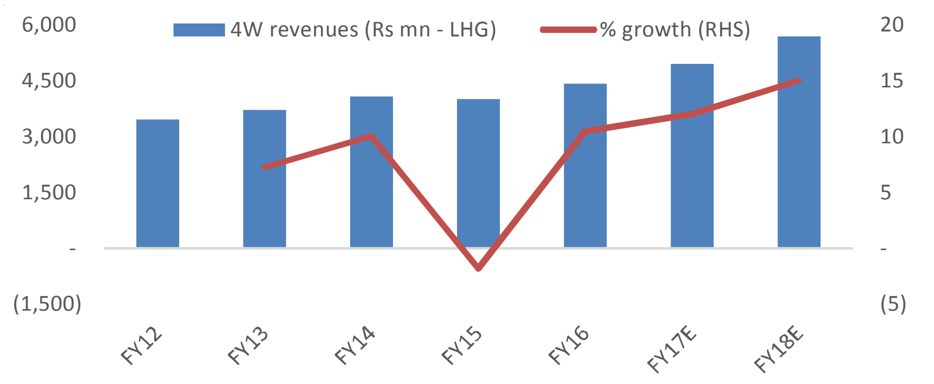
Gabriel growing amidst stiff competition

In the passenger vehicle segment, Gabriel faces stiff competition from various global and domestic suppliers of suspension products like Tenneco India, Mando India (JV with Anand Group), Magneti Marelli, and Munjal Showa. After Tenneco India (~35-40% market share), Gabriel, with ~25% market share, is the second largest OEM supplier of suspension products in the passenger vehicle segment. In the past four years (FY12-FY16), Gabriel's revenues from the passenger car segment grew at a CAGR of 6% as against 2% CAGR growth in car production.

Gabriel supplies to various models across various OEM's. Gabriel's key clientele in the passenger vehicle segment includes Maruti Suzuki, Mahindra and Mahindra, Tata Motors, Volkswagen, Toyota and General Motors. Gabriel is the second largest vendor for shock absorbers to Maruti Suzuki with ~25-30% share of business. Gabriel supplies to Hyundai through Mando, making them a tier II supplier to Hyundai. In recent quarters, the company have added key models like S-Cross, Viatara Brezza and KUV100 to its portfolio.

With improved growth prospects for the passenger vehicle industry, we expect Gabriel to report healthy 13% CAGR growth in revenues from the passenger vehicle segment.

Gabriel - Revenue growth from passenger vehicle segment

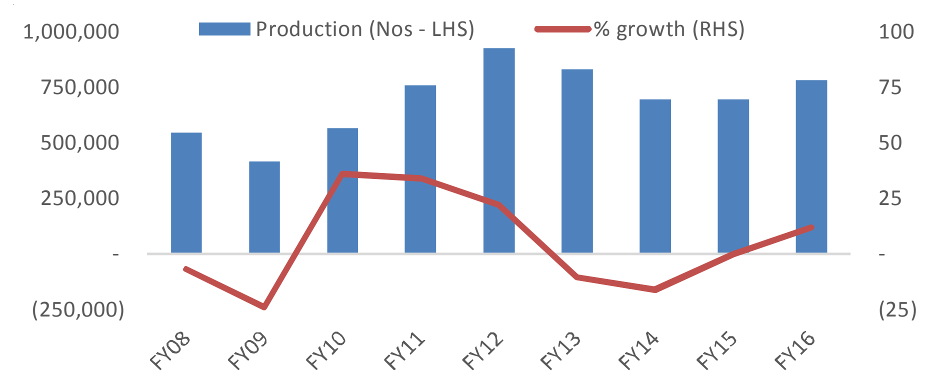


Source: Company, Kotak Securities - Private Client Research

Growth momentum in commercial vehicle segment to continue

Gabriel supplies cabin dampers, seat dampers and suspension shock absorbers to the commercial vehicle (CV) segment. Company's client consists of all the key players in the CV segment. Gabriel enjoys leadership position in the served segments. Apart from the CV segment, Gabriel also supplies to Indian Railways - though the share in the overall revenues is very small. Company is working on new shock absorbers for Indian Railways.

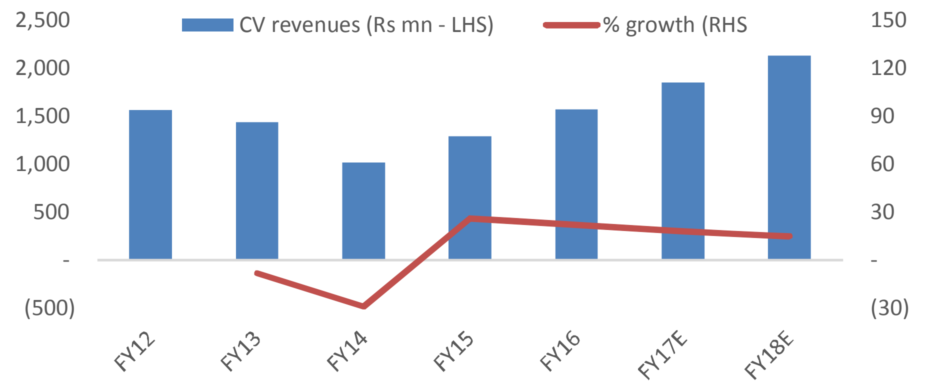
Commercial Vehicle Production and growth - in an upcycle



Source: SIAM

In FY16, Gabriel's revenue from the CV and railway segment was Rs1.6bn and accounted for ~11% of the overall revenues. In the past few months, Gabriel has received new orders from Mahindra Jeeto, Tata Xenon and Daimler Buses. We expect recovery in overall CV segment to continue, leading to healthy revenue growth for the company in the CV segment.

Gabriel - Revenue growth from commercial vehicle segment



Source: Company, Kotak Securities - Private Client Research

Company to focus on aftermarket segment

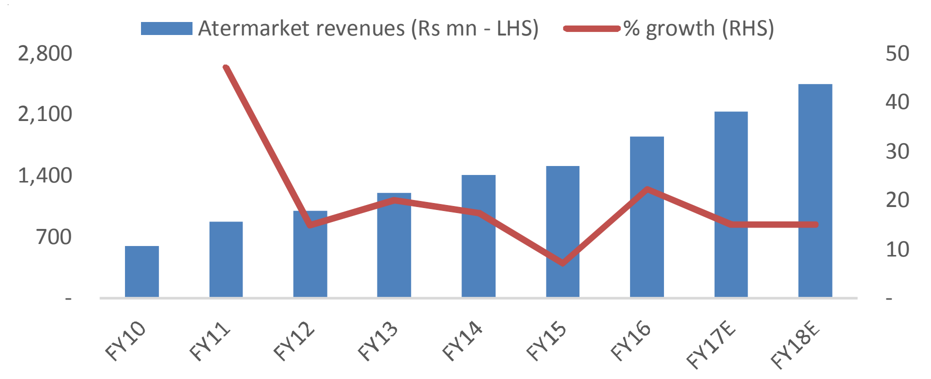
Gabriel India has a strong brand equity in the aftermarket segment. Both two wheeler segment and passenger car segment, account for significant portion of aftermarket revenues for the company. Gabriel has ~30% market share in the aftermarket segment (organized and unorganized combined). Within the organized market, Gabriel enjoys ~45% market share (includes OEM spare sales). Unorganized market accounts for ~40% of the aftermarket sales. As compared with the passenger car segment, the unorganized market is big in the two wheeler segment. Unorganized market has higher presence in rural areas as compared to its urban counterparts.

In the aftermarket segment, Gabriel is present through 375 dealers and 6,000 retailers. Gabriel has long standing relationships with 50% of its dealers (association ranging between 10-40 years). However, only 25% of the company's retailers market about 75% of its aftermarket products.

In order to improve revenues, the company has been launching new products and improving its engagement with the distribution network. Apart from its traditional products, Gabriel added new products like radiator coolants, suspension bush kits, front fork oils, gas springs and wheel rims. Gabriel has strengthened its brand and retailer connect through the execution of Elite Retailer programme across various regions in FY15/FY16. In the first phase, 500 premier retailers have been selected for this programme and the plan is to reach another 1,500 by 2018.

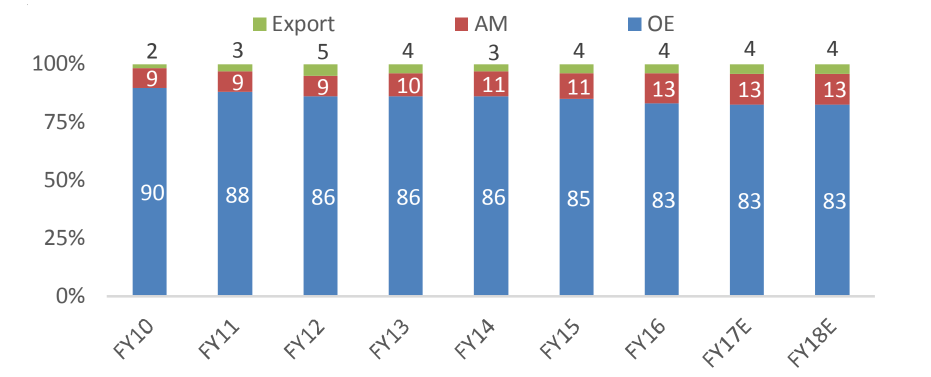
Gabriel earns ~83% of its revenues from OEM's. In order to lower its dependence on OE revenues, the company has been focusing on improving its aftermarket revenues and so far has been successful to an extent. Between FY10-FY16, share of aftermarket revenues in the overall revenue mix increased from ~8.5% in FY10 to 13% in FY16. Company will continue to focus on increasing aftermarket revenue share in the overall mix through further strengthening of brand, enhancing distribution network and introduction of new products. Company considers aftermarket to be a major driver for future growth.

Gabriel - Aftermarket revenue growing at a robust pace



Source: Company,Kotak Securities - Private Client Research

Gabriel - Rising aftermarket share in the revenue mix



Source: Company, Kotak Securities - Private Client Research

Exports is currently a small pie of the overall revenues

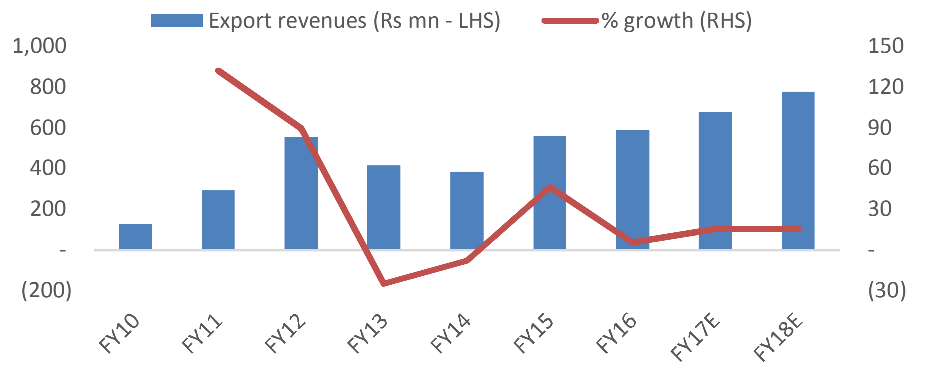
For Gabriel, exports accounts for a mere 4% of revenues. In the past six years, share of export revenues in the overall mix doubled from ~2% in FY10 to 4% in FY16.

Over the next three years, company is aiming for 10% revenues coming from exports. In the past couple of years, the company have made efforts to gain more traction in exports. However, unlike the domestic business, conversion into orders takes a longer time.

Company exports its products to six continents and has presence in US, Italy, Japan, Iran, and Colombia by supplying both to OEM's and aftermarket. Gabriel has also set up a dedicated team to focus on exports to South Asian, ASEAN, Middle East and Latin America.

Gabriel won export order from Mahindra GenZe USA and Isuzu. Company started supplying to Mahindra GenZe USA in FY16 and will see ramp-up in FY17. Export order from Isuzu will start getting executed in FY17. We thereby expect healthy export revenue growth in FY17.

Gabriel - Exports still a small pie of revenue



Source: Company, Kotak Securities - Private Client Research

Diversified business model

Due to cyclical nature of auto industry, OEM dependent auto ancillary companies are exposed to high business uncertainty. Thereby, diversifying business model is of utmost importance to sustain cyclical downturns. Unlike certain auto ancillary companies that are dependent on single vertical, Gabriel generates revenues across all auto segments. Gabriel's diversified business model provides cushion to the company's revenues and profitability during underperformance by a segment/channel/clientele. Gabriel generates ~60% of the revenues from the two wheeler segment, ~30% from passenger car segment and ~10% from the commercial vehicle segment. In terms of channel mix - the company is working on increasing its exposure from non-OEM's. Share of revenues from OEM's has come down from 90% in FY10 to 83% in FY16. On the other hand, revenues share from aftermarket/exports increased from 9%/ 2% in FY10 to 13%/4% respectively in FY16. Apart from this, the revenues are scattered across various clients. No single client accounts for more than 15% of Gabriel's revenues. Gabriel's top 4-5 customers individually contribute 10-15% of the revenues.

Accordingly the company's revenues do not face a major risk in an event of slowdown in demand from a particular segment/channel/clientele.

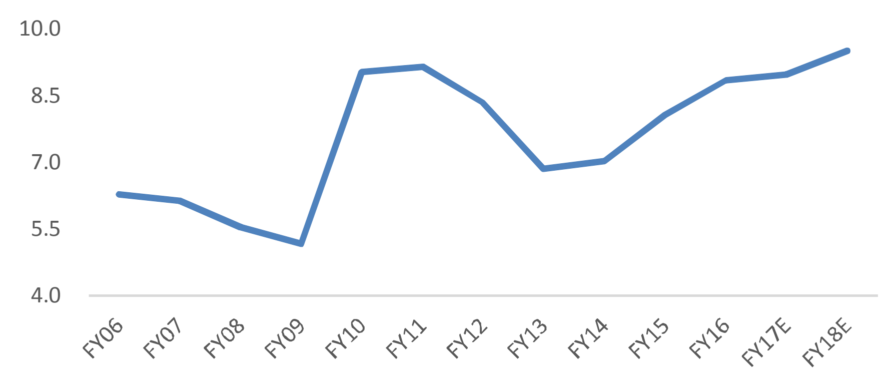
Amongst all the segments within the automobile segment, the two wheeler business is the least volatile. Higher revenue dependence on the two wheeler segment lowers volatility in company's revenue.

Operating margins to witness gradual improvement

Gabriel's EBITDA margins have improved for the past three consecutive years. From 6.9% in FY13, EBITDA margins improved to 8.9% in FY16. We expect operating margins to see further improvement. In FY16, operating margin expansion came primarily on account of fall in commodity prices and cost control measures. With OEM's, the company has a pass-through clause, but the same happens with a lag of 1-2 quarters. In a falling commodity prices scenario, the company benefits to an extent. Apart from this, the company can keep a part of the raw material cost benefit in the aftermarket segment. However, as commodity prices firms up, we expect the raw material cost (as a % of sales) to increase for company. Thereby in FY17, operating leverage benefit from higher capacity utilization is likely to get offset by slight increase in input cost. We thereby factor in a marginal 10bps improvement in EBITDA margin in FY17. For FY18, we expect operating margins to improve by 50bps on the back of positive impact of higher capacity utilization.

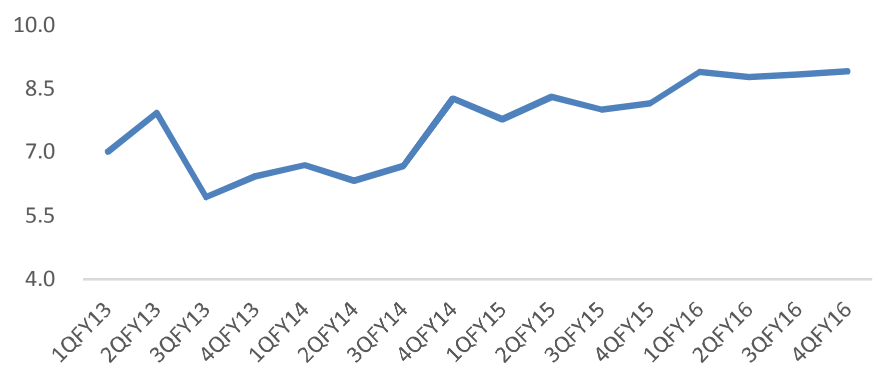
In FY17, capex on capacity will be limited to small brownfield expansion. Company will not be investing in new greenfield project in FY17. Current capacity utilization is 60-70% and we expect it to increase to 80-85% by FY18. Operating margins will benefit from increased capacity utilization. With expected double digit revenue growth, higher capacity utilization will translate into margin improvement. Further, higher focus on non-OEM revenues will positively contribute to operating margins.

Gabriel - EBITDA margin - steady improvement (%)



Source: Company, Kotak Securities - Private Client Research

Gabriel - Quarterly EBITDA margin - inching upwards (%)



Source: Company, Kotak Securities - Private Client Research

KONI tie-up to fill gap in product portfolio

In FY15, Gabriel signed a technical license agreement with KONI BV of the Netherlands for delivering products in the commercial vehicles space in order to sustain its leadership in this segment. KONI develops, manufactures and markets high performance shock absorbers for all types of cars and commercial vehicles.

As part of the agreement, KONI will provide technology that will allow Gabriel to manufacture innovative damper products for the original equipment and aftermarkets in India as well as Bangladesh, Sri Lanka, Nepal and Bhutan. The licensing agreement with KONI BV is for design, development and manufacturing of high-end shock absorbers for buses, trucks and earth moving equipment.

The tie-up with KONI is not expected to contribute significantly to Gabriel's revenue as this is a niche segment with low volumes and the tie-up is largely to fill product portfolio gap. Gabriel has received small order from Volvo Eicher Commercial Vehicle (VECV) and is expecting few more orders.

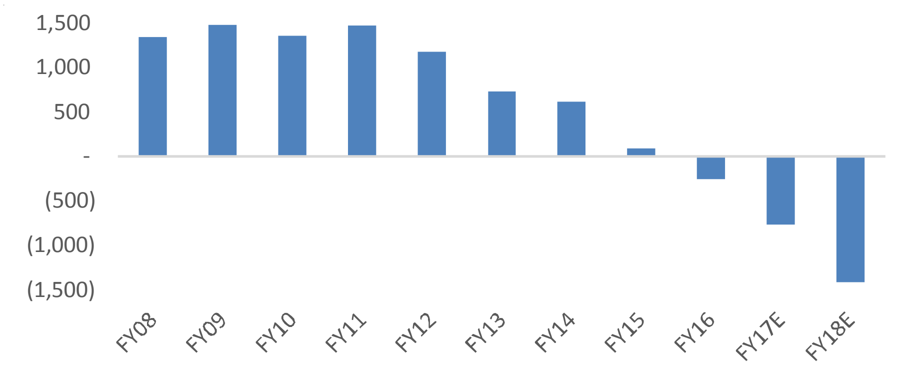
Strong balance sheet will provide cushion during cyclical downturn

Auto industry is cyclical and so are the performances of various OE dependent auto ancillaries. During slowdown, many auto ancillary company witness sharp drop in profitability and a weak balance sheet only added to the woes. Strong balance sheet provides cushion during downturns to Gabriel which has significantly strengthened its balance sheet in the past five years and over the next two years, we expect further strengthening.

Significant reduction in debt

In the past six years, Gabriel's debt has come down significantly. From a high of Rs1.57bn in FY09, gross debt as of end FY15 stood at a mere Rs133mn. In FY16, debt came down further to Rs109mn and that includes public fixed deposits and finance lease obligations. Gabriel has stopped acceptance of public fixed deposits from November 2015 and is now in the process of re-paying these FD's as per maturities. Outstanding public fixed deposits have come down from Rs101mn in end FY15 to Rs59mn by end FY16.

Gabriel - From high net debt to net cash (Rs mn)

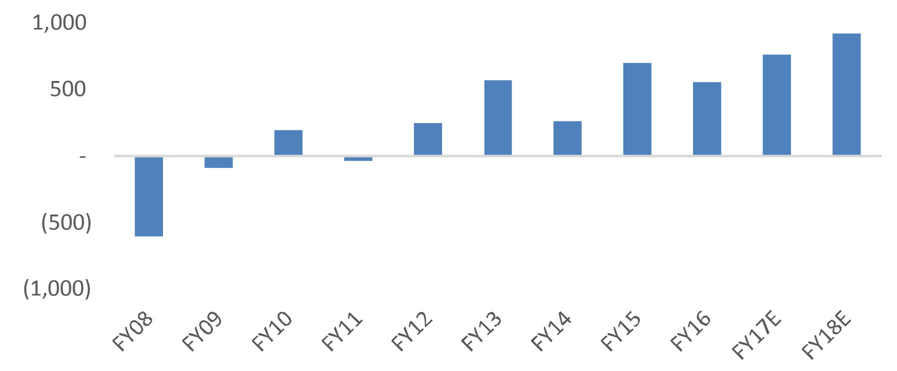


Source: Company,Kotak Securities - Private Client Research

Free cash flow generation

Gabriel has been generating healthy free cash flows for the past five consecutive years. With expected healthy earnings growth, no significant capex and efficient working capital management, we expect free cash flows for the company to remain strong over FY17/FY18. We expect free cash flow generation of Rs1.68bn over FY17/FY18 for the company.

Gabriel - Strong free cash flow provides comfort (Rs mn)

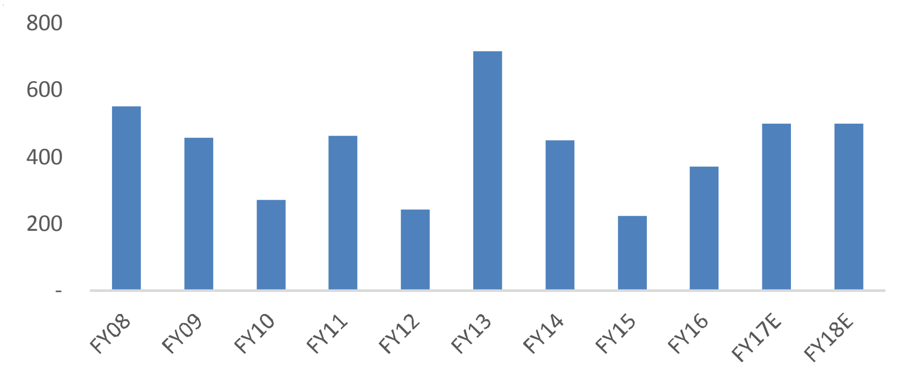


Source: Company, Kotak Securities - Private Client Research

Sufficient capacity does not demand any major capex in FY17

Gabriel's current capacity utilization is between 60-70%. Over the next couple of years, we estimate 14% revenue growth. We believe that the current capacity will be sufficient for FY17/FY18 growth. Management has guided for Rs450-500mn capex in FY17 and the same would be towards annual maintenance capex, R&D activities and small brownfield expansions. Company has ruled out any greenfield capex in FY17.

Gabriel - No significant capex planned (Rs mn)



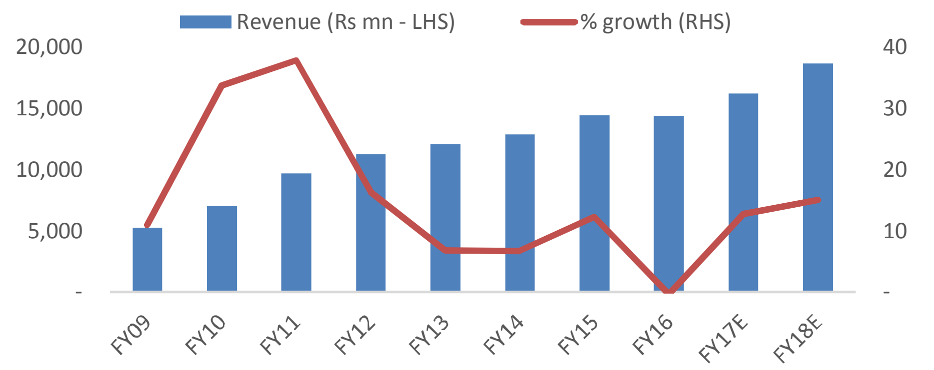
Source: Company, Kotak Securities - Private Client Research

Financial Outlook

Revenue growth to be healthy over FY16-FY18E

Gabriel's revenues are expected to grow at CAGR of 14% from Rs14.4bn in FY16 to Rs18.6bn in FY18. Demand recovery in the two wheeler/ passenger vehicle segment coupled with continued growth in the commercial vehicle segment will drive revenue growth for the company in FY17/FY18. Forecast of good monsoon, seventh pay commission payout, pent-up demand and expected improvement in macro-economic situation are the key demand growth drivers for the two wheeler/passenger vehicle industry. Replacement demand is expected to continue growing at a healthy pace.

Gabriel's revenue growth



Source: Company, Kotak Securities - Private Client Research

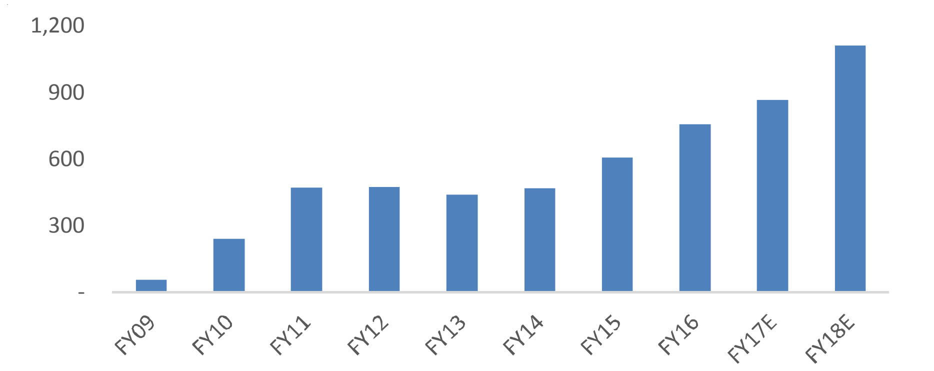
EBITDA margin to see further improvement

For the past three years (FY14-FY16), Gabriel EBITDA margin has been consistently moving north. Going ahead, we expect this trend of EBITDA margin improvement to continue. With expected growth in revenue, capacity utilization will increase, translating into operating leverage benefit. From 6.9% in FY13, EBITDA margin in FY16 stood at 8.8%. We assume EBITDA margin to improve further to 9.5% in FY18.

Adjusted PAT to grow at 22% CAGR over FY16-FY18E

Led by 14% CAGR revenue growth and EBITDA margin expansion, we expect Gabriel's adjusted PAT to grow by 21% CAGR from Rs0.76bn in FY16 to Rs1.1bn in FY18E. Adjusted PAT expectation of 21% CAGR over FY16-FY18E is much higher than the past five years (FY11-FY16) adjusted PAT CAGR growth of 10%.

Gabriel's Adjusted PAT (Rs mn)



Source: Company, Kotak Securities - Private Client Research

Improving return ratios

Robust earnings growth over FY16-FY18E will translate into improved return ratios. Gabriel's ROE increased from a low of 18% in FY13 to 21.5% in FY16 and we expect it to improve further to 23% in FY18.

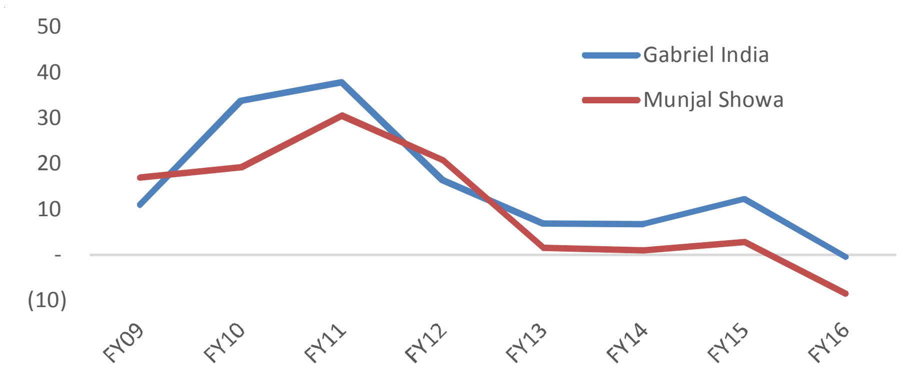
VALUATION

We expect Gabriel's earnings to grow at a healthy CAGR of 21% over FY16-FY18E, better than last five years (FY11-FY16) CAGR earnings growth of 10%. Gabriel's balance sheet has improved substantially in the past few years and we foresee further strengthening with strong free cash flow and no major capex.

At the CMP of Rs99, the stock trades at a PE of 12.8x and P/CEPS of 9.5x based on FY18E EPS of Rs7.7 and CEPS of Rs10.4.

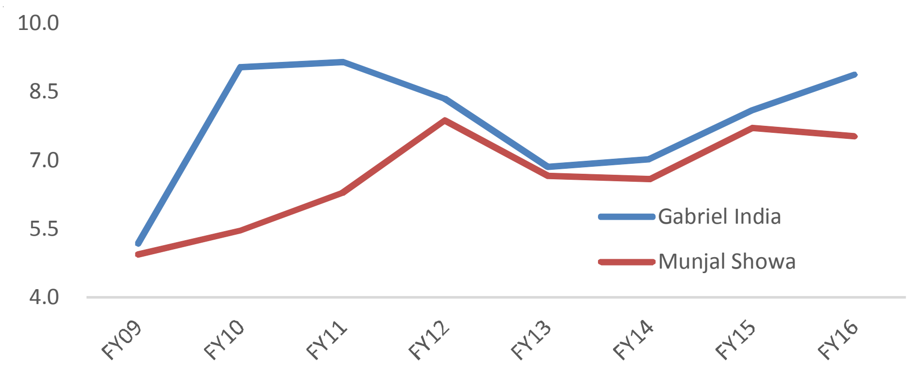
Gabriel trades at a premium to its nearest listed competitor - Munjal Showa. On FY16 earnings (12 trailing month), Gabriel trades at a PE of 18.8x as compared with Munjal Showa's PE multiple of 12x. We believe that the PE multiple premium to Gabriel India is justified on following grounds - 1/. Diversified client base - For Gabriel India, no single client accounts for more than 15% of revenues as against more than 70% revenue contribution coming from Hero MotoCorp for Munjal Showa. 2/. Faster growing clients - Gabriel's key clients like HMSI, TVSM and Eicher Motors are likely to outperform Hero MotoCorp in terms of volume growth 3/. Gabriel's financial performance (revenue/PAT growth, EBITDA margin expansion) has been ahead of Munjal Showa in the past few years and we expect the trend to continue.

Revenue growth (%) - Gabriel outperforming Munjal Showa



Source: Companies, Kotak Securities - Private Client Research

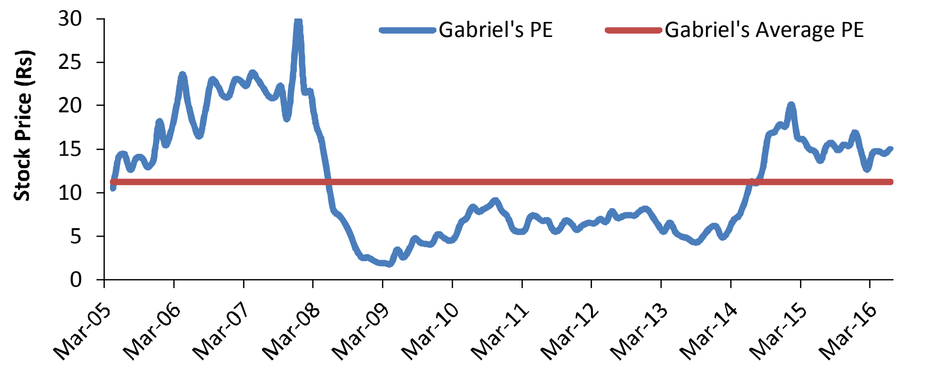
Gabriel's EBITDA margin are superior to Munjal Showa (%)



Source: Companies, Kotak Securities - Private Client Research

Gabriel's PE in the past two years has been re-rated from 11x (past 10 year average one year forward PE) to ~15x (past 2 year average one year forward PE) on the back of healthy earnings growth, increasing operating margin, company turning net debt free, strong free cash generation and improving return ratios. We expect healthy earnings growth and operating margin expansion trend to sustain, further strengthening of balance sheet and return ratios to improve further. Additionally, we also expect Gabriel's key business segment like two wheeler and passenger vehicle to witness recovery over FY16-FY18E. We accordingly assign a premium valuation and value the company at a PE of 16x on FY18 estimated EPS of Rs7.7 and arrive at a target price of Rs124. We initiate coverage on Gabriel India Limited with BUY rating and price target of Rs124.

Gabriel - Forward PE Chart



Source: Bloomberg, Kotak Securities - Private Client Research

Risk and Concerns

Slowdown in automobile growth

Gabriel's 83% revenues come from its products fitted in new vehicles. We are expecting demand recovery in the automotive sector in FY17 and pick-up in growth in FY18. Delay in demand pick-up will impact Gabriel's revenues and profitability.

Unlikely to foray in new business segments

Gabriel has various group companies that supply various auto ancillary product to the OEM's. There is low probability of Gabriel adding new business segments, thereby limiting growth to that extent.

Financials

Profit and Loss Statement

(Rs mn)	FY15	FY16	FY17E	FY18E
Revenues	**14,441**	**14,382**	**16,207**	**18,636**
% change YoY	12.2	(0.4)	12.7	15.0
EBITDA	**1,168**	**1,275**	**1,451**	**1,769**
% change YoY	29.2	9.2	13.8	21.9
Depreciation	311	332	355	385
EBIT	**856**	**944**	**1,097**	**1,384**
% change YoY	35.2	10.2	16.2	26.2
Interest cost	55	25	12	8
Other Income	40	42	69	108
Extraordinary income/(exp)	(6)	(6)	(6)	-
Profit before tax	**835**	**955**	**1,148**	**1,483**
% change YoY	49.8	14.3	20.2	29.2
Tax	235	203	287	371
as % of PBT	28.2	21.2	25.0	25.0
Profit after tax	**600**	**752**	**861**	**1,112**
% change YoY	40.9	25.3	14.4	29.2
Shares outstanding (mn)	144	144	144	144
EPS (reported) (Rs)	4.2	5.2	6.0	7.7
CEPS (Rs)	6.3	7.5	8.5	10.4
DPS (Rs)	1.1	1.2	1.4	1.6

Source: Company, Kotak Securities - Private Client Research

Balance sheet

(Rs mn)	FY15	FY16	FY17E	FY18E
Cash and cash equivalents	39	362	859	1,493
Accounts receivable	1,748	1,924	1,865	2,042
Inventories	1,121	1,107	1,294	1,484
Loans and advances	535	526	557	589
Others	37	50	50	50
Current assets	3,480	3,970	4,625	5,658
LT investments	0	0	0	0
Net fixed assets	2,708	2,746	2,892	3,007
Total assets	**6,188**	**6,716**	**7,517**	**8,665**
Payables	1,907	1,781	1,954	2,195
Others	381	468	438	465
Current liabilities	2,288	2,249	2,392	2,660
Provisions	408	454	515	570
Debt	133	109	89	80
Other liabilities	105	104	104	104
Equity	144	144	144	144
Reserves	3,111	3,656	4,273	5,107
Total liabilities	**6,188**	**6,716**	**7,517**	**8,665**
BVPS (Rs)	23	26	31	37

Source: Company, Kotak Securities - Private Client Research

Cash Flow Statement (Rs mn)

(Rs mn)	FY15	FY16	FY17E	FY18E
EBIT	856	944	1,097	1,384
Depreciation	311	332	355	385
Change in working capital	(5)	(288)	45	(126)
Chg in other net current asset	22	130	(0)	49
Operating cash flow	1,185	1,117	1,496	1,693
Interest	(55)	(25)	(12)	(8)
Tax	(226)	(203)	(287)	(371)
Other Income	40	42	69	108
EO income	(6)	(6)	(6)	-
Others	(16)			
CF from operations	**923**	**925**	**1,260**	**1,421**
Capex	(222)	(371)	(500)	(500)
(Inc)/dec in investments	-	-	-	-
CF from investments	**(222)**	**(371)**	**(500)**	**(500)**
Proceeds from equities	-	-	-	-
Increase/(decrease) in debt	(527)	(24)	(20)	(9)
Proceeds from share premium	-	-	-	-
Dividends	(181)	(207)	(243)	(278)
CF from financing	**(708)**	**(231)**	**(264)**	**(287)**
Net change in CF	(8)	324	496	634
Opening cash	47	39	362	859
Closing cash	39	362	859	1,493

Source: Company, Kotak Securities - Private Client Research

Ratio Analysis

	FY15	FY16	FY17E	FY18E
EBITDA margin (%)	8.1	8.9	9.0	9.5
PAT margin (%)	4.2	5.2	5.3	6.0
Inventory days	29	28	27	27
Debtor days	39	47	42	40
Creditor days	44	47	44	43
Debt-Equity	0.0	0.0	0.0	0.0
ROCE (%)	25.3	26.3	27.0	29.7
ROE (%)	19.9	21.5	21.1	23.0
Price/Sales (P/S)	1.0	1.0	0.9	0.8
Price/Book (P/B)	4.4	3.7	3.2	2.7
Price/Earnings (P/E)	23.4	18.7	16.4	12.8

Source: Company, Kotak Securities - Private Client Research

RATING SCALE

Definitions of ratings

BUY	–	We expect the stock to deliver more than 12% returns over the next 9 months
ACCUMULATE	–	We expect the stock to deliver 5% - 12% returns over the next 9 months
REDUCE	–	We expect the stock to deliver 0% - 5% returns over the next 9 months
SELL	–	We expect the stock to deliver negative returns over the next 9 months
NR	–	**Not Rated.** Kotak Securities is not assigning any rating or price target to the stock. The report has been prepared for information purposes only.
RS	–	**Rating Suspended.** Kotak Securities has suspended the investment rating and price target for this stock, either because there is not a sufficient fundamental basis for determining, or there are legal, regulatory or policy constraints around publishing, an investment rating or target. The previous investment rating and price target, if any, are no longer in effect for this stock and should not be relied upon.
NA	–	**Not Available or Not Applicable.** The information is not available for display or is not applicable
NM	–	**Not Meaningful.** The information is not meaningful and is therefore excluded.
NOTE	–	Our target prices are with a 9-month perspective. Returns stated in the rating scale are our internal benchmark.

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