December 17, 2018 VISIT NOTE

Escorts Ltd.

Sensex: 36252 CMP: INR 664

SPA THE FINANCIAL ADVISORS

Automobile

We recently met CFO of Escorts Ltd. (EL), which is the fourth-largest player in the tractor segment in India (after Mahindra & Mahindra Ltd, Tractors and Farm Equipment Ltd. and Interactional Tractors Limited) with a market share of 11%. The Farm Equipment (EFE) division which contributes 79% to the top line, offers a wide range of tractors - 10-75HP - primarily under the Farmtrac, Powertrac and Steeltrac brands. Construction and material handling equipment (15% of revenue) and railway equipment (6% of revenue) are other businesses that company operates.

Expanding product portfolio and geographical presence to drive volumes in EFE business

Revamp of the product portfolio over the past three fiscals (75% of volume from products launched in last 3 years), healthy financing tie-ups (including a joint venture with De Lage Landen Financial Services India (DLL)), and an increasing dealer network have helped to gain market share in West India (9.5% in FY18 against 7.8% in FY16) and sustain the share in other geographies. We expect new product launches to serve local needs in opportunity markets such as West and South India along with improving dealer and financing penetration, will help to improve diversity in revenue and add to market share over the medium term. Furthermore, increasing focus on exports (3.7% of revenue) should help to sustain volume growth in near term.

Construction Equipment business at the cusp of the turnaround

The performance of the CE segment has improved in last couple of years. The division has been loss-making in the past due to high fixed costs and cyclical nature of the business. EBIT loss was 4-5% in the three fiscals through FY17, which has improved to 1.9% and 1.6% in FY18 and 1H FY19 respectively. The turnaround is led by a change in the product mix (increasing proportion of higher tonnage equipment) and cost rationalisation initiatives with vendor rationalisation and price renegotiation. Continued focus on cost reduction and positive operating leverageis expected to improve margin gradually to 5-6% over the medium term.

Railways to add to profitable growth

Revenue in the railways equipment business, the profitable product segment (TTM EBITM 13.9%), comprising of brakes, suspensions, couplers for Railway and India Railways, has also had a robust CAGR of 8% during the four fiscals through FY18. Margins can further improved with reducing import content of Raw Material.Substantial orders of over Rs 400 crore in 1HFY19, provide strong revenue visibility.

Cost cutting measures and operating leverage to expand margins

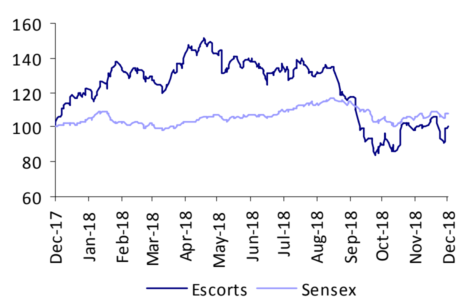
EBITDAM has consistently improved (11.8% in 1HFY19 against 6.9% in FY17) driven by the cost reduction initiatives, benefit of operating leverage and exit from the loss-making automotive component business. Additionally, there was an operating level breakeven in the CE segment in fiscal 2018.Further improvement in the margin to 1-2% is expected in FY20 driven by benefit of operating leverage, changing product mix, and cost reduction.

Outlook and valuation

Looking forward, we expect EFE/ECE volumes to grow at 14.6%/ 21.9% through FY18-20E. We expect EL's revenue/EBITDA/PAT to clock a growth of 15.6%/23.8%/24.8% through FY18-20E. EBITDA margin of EL is expected to expand from 11% in FY18 to 12.7% in FY20. At CMP of 664, the stock is trading at 15.3x its FY20 EPS. We recommend buy with a TP of INR 867 in 12-18 months, 20x its FY20 EPS.

Shareholding (%)	Sep-18
Promoters	40.07
FII's	22.42
DII's	6.09
Others	31.42

Relative Price Performance



Key Data	
BSE Code	500495
NSE Symbol	ESCORTS
Bloomberg Code	ESC IN
Reuters Code	ESCO.BO
Shares Outstanding (mn)	122
Face Value	10
Mcap (INR bn)	81.38
52 Week H/L	1019/543
2W Avg. Vol, BSE	195045
CMP	664
Beta	1.63

(INR mn)	FY17	FY18	FY19E	FY20E
Net Sales	41471	49951	59424	66775
Growth (%)	19.5%	20.4%	19.0%	12.4%
EBIDTAM (%)	6.7%	11.0%	11.8%	12.7%
Adj. PAT	1604	3447	4427	5366
Growth (%)	91.6%	114.9%	28.4%	21.2%
Adj. EPS (INR)	13.0	27.9	35.8	43.4
P/E (x)	40.9	23.8	18.6	15.3
EV/EBIDTA	20.1	14.0	11.2	9.3
EV/Sales	1.7	1.7	1.4	1.3
RoACE (%)	14.4%	23.3%	24.7%	25.4%
RoAE (%)	8.4%	15.2%	16.2%	17.0%

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Financials - Standalone

Income Statement

Y/E Mar (INR mn)	FY17	FY18	FY19E	FY20E
Net Sales	41471	49951	59424	66775
% Growth	*19.5%*	*20.4%*	*19.0%*	*12.4%*
RM Cost	27919	33578	40318	45292
% Growth	*19.6%*	*20.3%*	*20.1%*	*12.3%*
Employee Expenses	4390	4311	4682	4993
% Growth	*9.9%*	*-1.8%*	*8.6%*	*6.7%*
Oth Expense	6399	6546	7400	8029
% Growth	*-7.4%*	*41.7%*	*27.0%*	*11.1%*
Total Op Exp	38707	44435	52399	58315
EBIDTA (excl OI)	2764	5516	7024	8461
% Growth	*207.8%*	*99.6%*	*27.3%*	*20.4%*
EBITDA Margin %	*6.7%*	*11.0%*	*11.8%*	*12.7%*
Dep./Amortization	631	725	746	905
Other Income	743	650	650	650
EBIT	2876	5441	6929	8206
EBIT Margin %	*6.9%*	*10.9%*	*11.7%*	*12.3%*
Interest Expense	311	286	101	0
Exceptional Items	-382	-68	-220	-198
EBT	2183	5088	6608	8008
Tax Expenses	579	1641	2181	2643
PAT	1604	3447	4427	5366
% Growth	*91.6%*	*114.9%*	*28.4%*	*21.2%*
APAT Margin %	*3.9%*	*6.9%*	*7.5%*	*8.0%*

Balance Sheet

Y/E Mar (INR mn)	FY17	FY18	FY19E	FY20E
Share Capital	1227	1226	1226	1226
Reserves and Surplus	18685	24255	28019	32579
Total Networth	19912	25481	29244	33805
Long Term Debt	563	137	137	137
Short Term Debt	1590	0	0	0
Total Debt	2153	137	137	137
Net Deferred Tax Liability	(470)	197	201	205
Other Liabilities	492	388	422	449
Sources of Funds	**34661**	**42695**	**47540**	**54166**
Net Block	15544	15578	17832	19927
Investments	4420	4327	4327	4327
Current Assets	14175	21145	23538	27912
Current Liabilities	14166	16492	17536	19570
Net Current Assets	9	4653	6002	8342
Application of Funds	**34661**	**42695**	**47540**	**54166**

Key Ratios

Y/E Mar	FY17	FY18	FY19E	FY20E
Per Share Data (INR)				
Per Share Data (INR)				
Reported EPS	13.1	27.9	35.8	43.4
Adj. EPS	13.0	27.9	35.8	43.4
Growth (%)				
CEPS	18.2	33.7	41.8	50.7
DPS	1.2	2.0	5.4	6.5
BVPS	162.4	205.9	236.3	273.2
Return Ratios (%)				
RoACE	14.4%	23.3%	24.7%	25.4%
RoANW	8.4%	15.2%	16.2%	17.0%
Liquidity Ratios				
Net Debt/Equity	(0.0)	(0.1)	(0.2)	(0.2)
Interest Coverage Ratio	9.2	19.0	68.7	NA
Current Ratio	0.4	0.5	0.5	0.5
Quick Ratio	0.1	0.2	0.2	0.2
Efficiency Ratios				
Asset Turnover Ratio	1.2	1.3	1.3	1.3
Inventory Days	40	44	40	40
Debtor Days	40	44	39	39
Creditor Days	84	101	87	87
Valuation Ratios				
P/E (x)	40.9	23.8	18.6	15.3
P/BV (x)	3.3	3.2	2.8	2.4
P/CEPS (x)	29.3	19.7	15.9	13.1
Dividend Yield (%)	0.2	0.3	0.8	1.0
EV/Net Sales (x)	1.7	1.7	1.4	1.3
EV/EBIDTA (x)	20.1	14.0	11.2	9.3

Cash Flow

Y/E Mar (INR mn)	FY17	FY18	FY19E	FY20E
PBT	2,183	5,088	6,608	8,008
Add:Depreciation	631	725	746	905
Add: Interest paid	311	286	101	-
Change in Working Capital	222	(648)	104	350
Less: Taxes	(579)	(1,641)	(2,181)	(2,643)
Cash Flow from operations (a)	**2,025**	**3,159**	**4,728**	**5,970**
Change in Fixed Assets	(820)	(759)	(3,000)	(3,000)
Change in CWIP	(52)	(202)	(9)	(10)
Change in Investments	(1,714)	(3,067)	-	-
Others	1,042	294	499	535
Cash Flow from Investing (b)	**(1,545)**	**(3,735)**	**(2,511)**	**(2,474)**
Change in Equity	-	-	-	-
Debt Raised/(Repaid)	(312)	(426)	-	-
Dividend paid	(144)	(247)	(664)	(805)
Interest paid	(311)	(286)	(101)	-
Others	74	2,370	-	-
Cash Flow from Financing (c)	**(767)**	**(959)**	**(765)**	**(805)**
Net Change in Cash (a+b+c)	**(286)**	**(1,535)**	**1,452**	**2,690**
Opening Cash	2,496	2,284	3,119	4,571
Closing Cash	2,284	3,119	4,571	7,262

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