

Tractor business holds company in good stead...

Escorts reported a robust Q4FY20 performance despite 20% YoY fall in tractor volumes. Normalised EBITDA margins for the quarter were healthy at 12.1%, primarily tracking a better product mix, benign commodity prices and other cost efficiencies. Total operating income for Q4FY20 came in at ₹ 1,381 crore, down 15.4% YoY. Within its segments, gross revenue from agri equipment machinery (EAM) was at ₹ 1,058 crore; primarily tracking beat on ASPs. Tractor ASP for the quarter was at ₹ 5.26 lakh/unit. EBITDA in Q4FY20 was at ₹ 194.4 crore with corresponding PAT at ₹ 140.4 crore.

Tractor: Steady state market share, rural slate to limit decline

The tractor industry has been at the forefront of farm mechanisation in India with total tractor sales pegged at 7.1 lakh units in FY20. Escorts is a prominent tractor player domestically with market share as of FY20 pegged at 11.6%, 130 bps in FY16-20. Given the rural centric tractor demand that is relatively less impacted by Covid-19, the domestic tractor industry is expected to outperform the rest of the automobile industry in FY20. The tractor industry is also likely to benefit from upbeat farm sentiments primarily tracking healthy Rabi crop production, robust procurement of food grains by central government agencies, expectation of normal monsoon 2020. Hence, going forward, for the industry and Escorts, we build in 5% volume de-growth in FY20 and 10% YoY growth thereafter in FY22, implying sales volume CAGR of 2.2% in FY20-22E.

CE segment recovery some time away, Railways well placed

Tractor forms bulk of sales (77% of sales in FY20) with construction equipment comprising ~15% and railways constituting the rest at ~8% of sales. By virtue of construction equipment sales (cranes, backhoe loaders, compactors) linked to infrastructure spend, the management feels a recovery in this segment is still some time away with volume growth for the segment pegged at -10% for FY21E (over and above 27% volume de-growth in FY20). In the railways segment, the order book is healthy at over ₹ 500 crore. The management indicated at 15% YoY growth in the segment for FY21E. Building in all segmental revenues, overall revenue at Escorts is expected to de-grow 3.5% in FY21 and see a recovery thereafter by growing 14% YoY in FY22, with sales CAGR pegged at 4.9% in FY20-22E. EBITDA margin in aforesaid period is pegged at ~12-12.5%.

Valuation & Outlook

Escorts has a healthy B/S with ~₹ 1000 crore of cash on books as of FY20 and ~₹ 1000 due to be received from Kubota in near term (FY21E). However, we await clarity on cash utilisation before upgrading the stock. Hence, we maintain **HOLD** on the stock valuing Escorts at ₹ 860, using SOTP method, assigning 15x multiple to core FY22E EPS of ₹ 50.3 and ascribing 25% holding company discount to its treasury shares in books.



Particulars

Particular	Amount
Market Capitalization (₹ C crore)	9,800.0
Total Debt (FY20P) (₹ C crore)	6.6
Cash & Investments (FY20P) (₹ C crore)	956.6
EV (₹ C crore)	8,850.0
52 week H/L (₹)	914 / 423
Equity capital (₹ crore)	122.6
Face value	₹ 10

Key Highlights

- Normalised EBITDA margin for the quarter at 12.1% with tractor ASPs inching up to ₹ 5.26 lakh/unit
- With tractor forming bulk of sales at Escorts and tractor being a rural centric product, volume declines for Escorts to be limited to 5% in FY21E
- EBITDA margins healthy at ~12% with 80 bps improvement envisaged over FY20-22E
- Maintain HOLD with revised target price of ₹ 860 valuing base business at 15x FY22E EPS and applying 25% holding company discount to treasury shares in company's books

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Key Financial Summary

				FY21E	FY22E	CAGR (FY20-22E)
Net Sales	4,995.1	6,196.4	5,761.0	5,556.7	6,333.8	4.9%
EBITDA	557.2	733.3	675.8	637.3	791.4	8.2%
EBITDA Margins (%)	11.2	11.8	11.7	11.5	12.5	
Net Profit	344.8	484.9	485.6	500.1	616.3	12.7%
EPS (₹)	28.1	39.6	39.6	40.8	50.3	
P/E	28.4	20.2	20.2	19.6	15.9	
RoNW (%)	13.8	15.6	14.2	10.1	11.1	
RoCE (%)	21.0	21.7	18.9	13.3	14.2	

Exhibit 1: Variance Analysis

₹ crore	Q4FY20	Q4FY20E	Q4FY19	YoY (Chg %)	Q3FY20	QoQ (Chg %)	Comments
Total Operating Income	1,380.7	1,338.7	1,631.7	-15.4	1,633.4	-15.5	Topline came in ahead of our estimates tracking beat on ASPs in tractor division
Raw Material Expenses	763.4	823.3	993.2	-23.1	998.8	-23.6	
(Inc)/Dec in Stock in Trade and WIP	0.0	0.0	37.3		0.0		RM to sales came in lower primarily on account of better product mix (higher hp tractors), benign commodity prices as well as other cost efficiencies
Purchase of Traded Goods	95.8	73.6	92.2	3.9	92.8	3.2	
Employee Expenses	129.5	120.5	118.0	9.7	132.9	-2.6	
Other Expenditure	197.5	174.0	201.2	-1.8	196.7	0.4	
EBITDA	194.4	147.3	189.8	2.4	212.3	-8.4	Normalised margins for the quarter came in 200 bps lower than reported margins at 12.1%
EBITDA Margin (%)	14.1	11.0	11.6	245 bps	13.0	109 bps	
Interest	2.8	3.7	7.5	-62.1	2.9	-2.4	
Depreciation	27.8	25.9	21.8	27.3	26.7	4.1	
Total Tax	51.2	41.1	56.5	-9.4	56.4	-9.2	Tax rate for the quarter came in at 26.7%
PAT	140.4	95.9	121.3	15.7	153.1	-8.3	PAT came in higher tracking higher reported margins and beat on tractor ASPs
Key Metrics (₹ crore)							
Tractor Segment revenue	1,058	1,014	1,231	-14.0	1,292	-18.0	Tractor ASP for the quarter came in at ₹ 5.26 lakh/unit vs. ₹ 5.14 lakh/unit in Q3FY20
Construction Equipment	210	211	293	-28.3	217	-3.0	
Railway Equipment revenue	108	114	104	4.3	124	-13.2	Other segmental revenues came in line with our estimates

Source: Company, ICICI Direct Research

Exhibit 2: Change in estimates

₹ Crore)	FY21E			FY22E			Comments
	Old	New	% Change	Old	New	% Change	
Revenue	6,275.8	5,556.7	-11.5	6,946.5	6,333.8	-8.8	Downward revise our sales estimates tracking loss of tractor sales in Q1FY21E. Revenues CAGR over FY20-22E pegged at 0.7%
EBITDA	720.6	637.3	-11.6	835.5	791.4	-5.3	
EBITDA Margin (%)	11.5	11.5	-	12.0	12.5	50 bps	Better product mix and cost efficiencies to drive margin improvement, going forward
PAT	557.0	500.1	-10.2	660.9	616.3	-6.7	
EPS (₹)	45.4	40.8	-10.2	53.9	50	-6.7	Downward revision in sales estimates leads to decline in PAT estimates, going forward

Source: Company, ICICI Direct Research

Exhibit 3: Assumptions

	Current					Earlier		Comments
	FY18	FY19	FY20P	FY21E	FY22E	FY21E	FY22E	
Tractor volumes (no's)	80,417	96,412	86,018	81,717	89,869	94,350	100,955	Covid-19 has led to downward revision in our forward estimates. We now build in 5% decline in tractor volumes for FY21E and growth of 10% YoY thereafter in FY22E. Tractor sales volume CAGR in FY20-22E is pegged at 2.2%
Average ASP (₹)	492,166	492,053	515,890	522,069	534,254	512,004	522,296	Better product mix to leads to increase in ASPs

Source: Company, ICICI Direct Research

Conference call highlights

Tractor segment

- The company has resumed operations at its facilities in Faridabad and is currently operating on a single shift basis with utilisation levels of ~20%. Escorts expects to reach ~ 50-60% utilisation levels by mid-June 2020 and normalised level thereafter from July 2020 onwards
- Escorts has sufficient channel inventory to sustain retail sales up to June 2020
- The company expects tractor segment to witness healthy recovery post Covid-19 led disruption with encouraging initial signs on the rural front. Rural farm sentiments are upbeat tracking robust Rabi production, expectation of normal monsoon 2020 and record food-grain procurement by FCI
- Escorts have opened up ~65% of its dealership (total dealer count pegged at 1,000+) pan India
- Escorts expect 40-50% of tractor volumes lost for the industry in March end-April period (~70,000-80,000 units) to be recovered as sales in June-October 2020 period
- March 2020 ending market share for Escorts in the tractor segment was at 11.6% (down 20 bps YoY) and is of no major concern and should be looked as more of a timing mismatch
- Subsidy sales accounted for ~11-12% of total tractor volumes in FY19. In FY20, state specific issues led to meaningful decline in volumes. The company expects subsidy led sales to exceed FY19 figures in absolute numbers with company looking forward to supply meaningfully under the requisite schemes, going forward
- On the financing front, the company dealership network is comfortably placed. Wherever necessary, the company is helping dealers to overcome the liquidity crunch. On the demand side, financing operations by leading banks/ NBFCs have commenced and are currently operating at ~60% utilisation levels. On the tractor side, NBFCs constitute bulk of financing at ~66% followed by banks at ~34%

Construction Equipment segment

- On the construction equipment front, recovery is anticipated from H2FY21 onwards with full year volume guidance of de-growth to the tune of 10% YoY. Positive surprise could, however, come from greater infrastructure spend by the government of India

RED segment

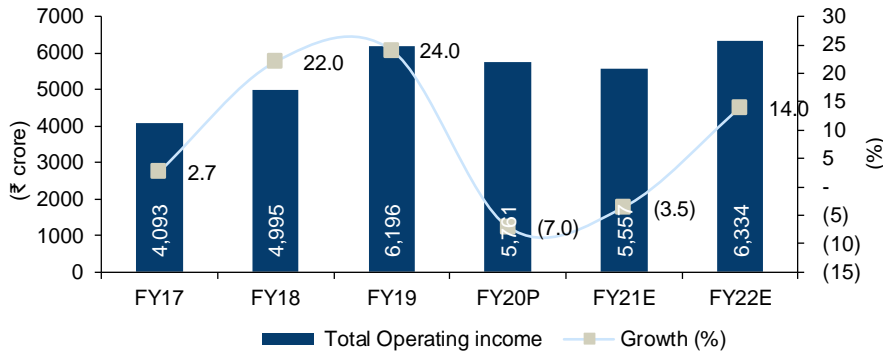
- In the railway segment the present order book is pegged at ~₹ 500 crore with FY21E revenues in this segment expected to grow at ~15% YoY. The company has also been approved for supplying certain components for locomotives procured by Indian railways the opportunity size of which is pegged at ~₹ 800 crore with foreign companies currently supplying the same

Others

- On the Kubota JV front, the company expects to start commercial production with a lag from Q2FY21 onwards. The company intends to develop and produce premium tractors under this JV with broader thought process to also look at other farm machinery equipment's in due course of time
- On the Kubota preferential allotment front, the company has attained shareholders' approval with other regulatory approvals awaited. It expects final transaction to be executed by June-July 2020
- The company plans to incur a capex of ₹ 200-250 crore in FY21

Financial story in charts

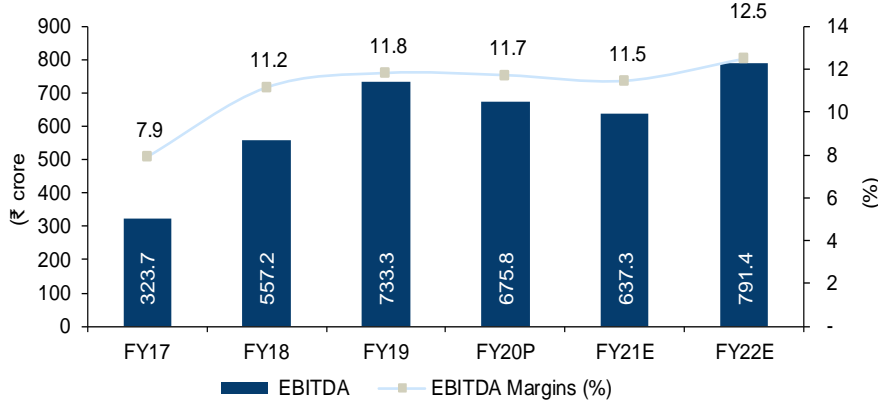
Exhibit 4: Topline trend



We expect sales to grow at a CAGR of 4.9% over FY20E-22E with tractor volumes growing at ~2.2% CAGR in this period

Source: Company, ICICI Direct Research

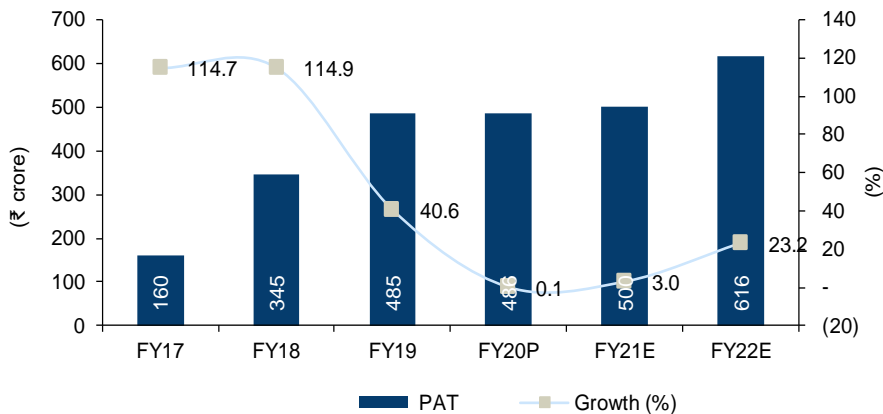
Exhibit 5: EBITDA margin trend



Margins are seen consolidating around 11.5-12.5% range over FY20E-22E

Source: Company, ICICI Direct Research

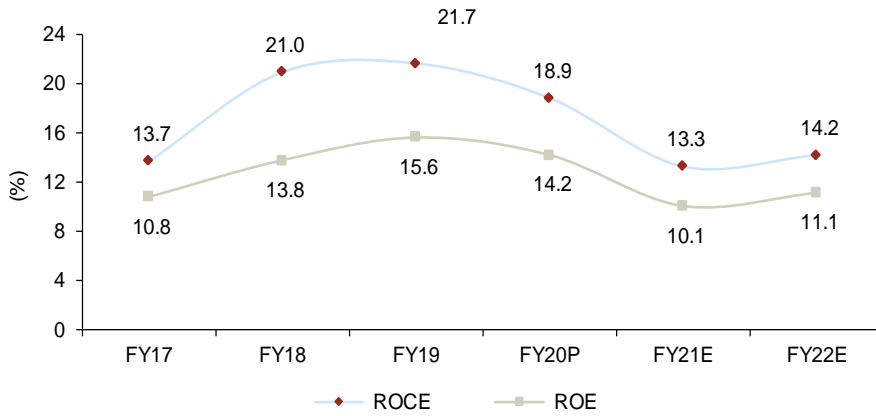
Exhibit 6: Profitability trend



PAT expected to grow at 12.7% CAGR over FY20E-22E to ₹ 616 crore in FY22E

Source: Company, ICICI Direct Research

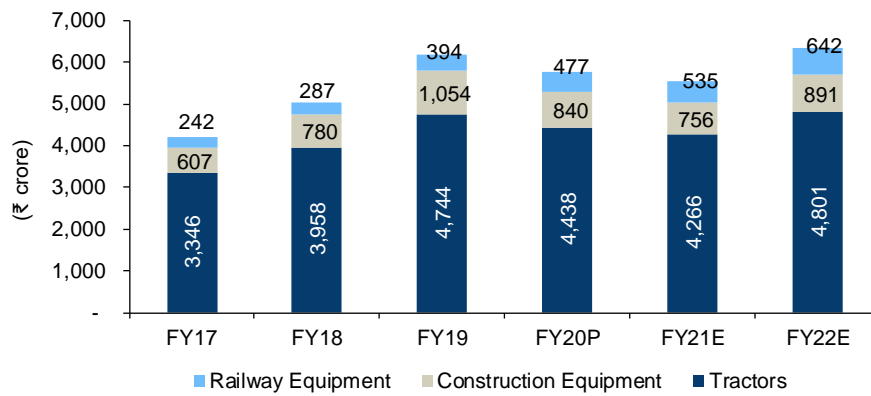
Exhibit 7: Return ratios



Escorts expected to continue to clock stable healthy return ratios

Source: Company, ICICI Direct Research

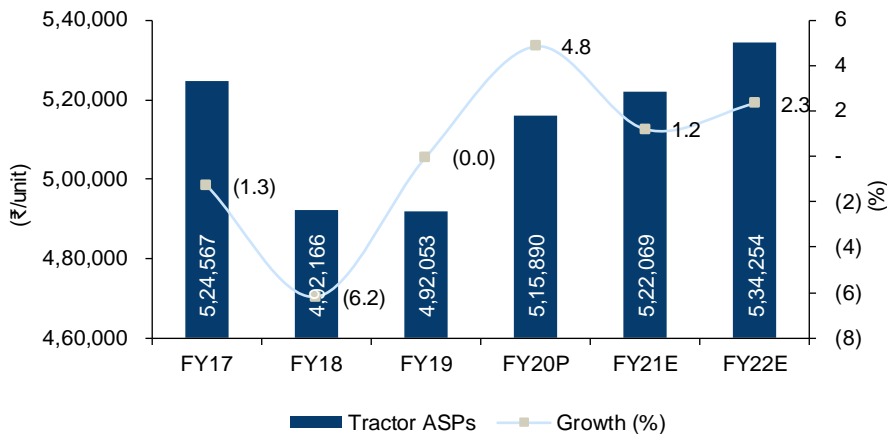
Exhibit 8: Segment mix



Tractors continue to dominate total sales with their share in total sales pie at ~77% as of FY20. Construction equipment constitute ~15% of sales while railways segment constitute the rest at ~8%

Source: Company, ICICI Direct Research

Exhibit 9: Trend in tractor ASPs



Tractor ASPs are seen inching upwards on the back of industry phenomenon of product mix change in favour of higher hp segment

Source: Company, ICICI Direct Research

Exhibit 10: Valuation Summary

	Sales	Growth	EPS	Growth	PE	EV/EBITDA	RoNW	RoCE
	(₹ cr)	(%)	(₹)	(%)	(x)	(x)	(%)	(%)
FY18	4995	22.0	28.1	114.9	28.4	16.2	13.8	21.0
FY19	6196	24.0	39.6	40.6	20.2	12.9	15.6	21.7
FY20P	5761	-7.0	39.6	0.1	20.2	13.1	14.2	18.9
FY21E	5557	(3.5)	40.8	3.0	19.6	12.3	10.1	13.3
FY22E	6334	14.0	50.3	23.2	15.9	9.9	11.1	14.2

Source: Bloomberg, ICICI Direct Research

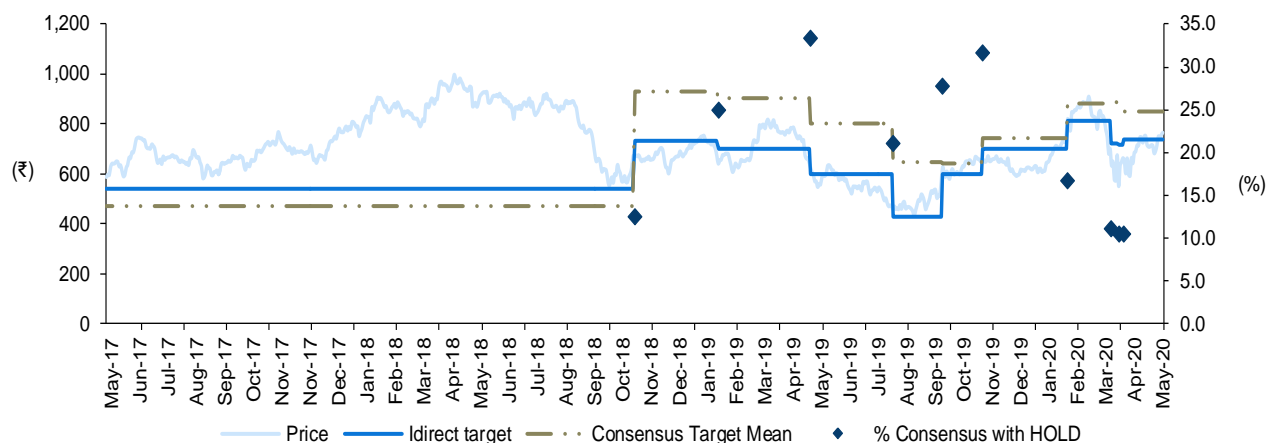
(Note - Per share data is adjusted for treasury shares on company's books.)

Exhibit 11: SOTP valuation matrix

Particulars	Amount (₹)
FY22E EPS (₹/share, A)	50
P/E Multiple (x, B)	15.0
Value of Base Business (C =A*B)	754
No of Treasury Shares (crore)	2.1
Current Market Price (₹/share)	800
Value of Investments (₹ crore)	1,716
Holding company discount (%)	25
Revised value of Investments (₹ crore)	1,287
Contribution per share (₹/share, D)	105
Target Price (C +D)	860

Source: ICICI Direct Research

Exhibit 12: Recommendation history vs. consensus



Source: Bloomberg, ICICI Direct Research

Exhibit 13: Top 10 shareholders

Rank	Name	Latest Filing Date	% O/S	Position (m)	Change (m)
1	SUTANU BEHURIA TRUTE	30-06-2019	27.49	33.70M	0
2	HARPARSHAD & COMPANY	30-06-2019	8.75	10.73M	0
3	Jhunjhunwala Rakesh	30-06-2019	8.16	10.00M	0
4	UTI ASSET MANAGEMENT	31-03-2020	3.24	3.97M	+0.15M
5	BLACKROCK	19-09-2019	2.84	3.49M	+3.49M
6	T ROWE PRICE GROUP I	31-03-2020	2.44	2.99M	+0.00M
7	DIMENSIONAL FUND ADV	31-03-2020	1.72	2.11M	-0.07M
8	TATA ASSET MANAGEMEN	31-03-2020	1.55	1.90M	+0.08M
9	MATTHEWS INTL CAPITA	31-12-2019	1.51	1.85M	+0.20M
10	BIG APPLE CLOTHING P	30-06-2019	1.45	1.77M	0

Source: Bloomberg, ICICI Direct Research

Exhibit 14: Shareholding pattern

(in %)	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20
Promoter	40.1	40.2	40.3	40.3	40.3
FII	24.6	20.4	21.8	20.4	19.3
DII	3.3	5.5	4.8	6.5	10.0
Others	32.0	33.8	33.2	32.8	30.5

Source: Company, ICICI Direct Research

Financial Summary

Exhibit 15: Profit and loss statement				
	₹ crore			
(Year-end March)	FY19	FY20P	FY21E	FY22E
Total operating Income	6,196.4	5,761.0	5,556.7	6,333.8
Growth (%)	24.0	-7.0	-3.5	14.0
Raw Material Expenses	4,040.3	3,449.3	3,334.0	3,800.3
Employee Expenses	471.7	510.3	501.9	532.6
Other expenses	750.7	755.2	722.3	797.9
Total Operating Expenditure	5,463.1	5,085.1	4,919.5	5,542.4
EBITDA	733.3	675.8	637.3	791.4
Growth (%)	44.1	-7.8	-5.7	24.2
Depreciation	85.4	104.6	118.8	140.1
Interest	18.5	15.5	1.0	1.0
Other Income	80.8	92.3	146.1	140.0
PBT	722.4	638.9	663.6	790.3
Total Tax	237.5	153.3	167.2	199.2
PAT	484.9	485.6	500.1	616.3
Growth (%)	40.6	0.1	3.0	23.2
EPS (₹)	39.6	39.6	40.8	50.3

Source: Company, ICICI Direct Research

Exhibit 16: Cash flow statement				
	₹ crore			
(Year-end March)	FY19	FY20P	FY21E	FY22E
Profit after Tax	484.9	485.6	500.1	616.3
Add: Depreciation	85.4	104.6	118.8	140.1
(Inc)/dec in Current Assets	-769.0	190.7	101.8	-525.5
Inc/(dec) in CL and Provisions	-49.9	112.4	-306.6	266.8
CF from operating activities	-248.7	893.1	414.1	497.7
(Inc)/dec in Investments	93.8	-247.2	-1,000.0	0.0
(Inc)/dec in Fixed Assets	-147.3	-210.4	-297.0	-300.0
Others	0.0	0.0	0.0	0.0
(Inc)/dec in Deferred Tax Asset	0.0	0.0	0.0	0.0
CF from investing activities	-80.9	-497.5	-1409.0	-396.8
Issue/(Buy back) of Equity	0.0	0.0	0.0	0.0
Inc/(dec) in loan funds	258.9	-280.1	0.0	0.0
Dividend paid & dividend tax	-36.8	-36.8	-42.9	-49.0
Inc/(dec) in Sec. premium	0.0	0.0	1,029.8	0.0
Others	26.7	8.4	0.0	0.0
CF from financing activities	248.9	-308.5	986.9	-49.0
Net Cash flow	-80.7	87.1	-8.0	51.9
Opening Cash	311.9	231.1	318.3	310.3
Closing Cash	231.1	318.3	310.3	362.2

Source: Company, ICICI Direct Research

Exhibit 17: Balance Sheet				
	₹ crore			
(Year-end March)	FY19	FY20P	FY21E	FY22E
Liabilities				
Equity Capital	122.6	122.6	122.6	122.6
Reserve and Surplus	2,900.3	3,357.5	4,844.6	5,411.8
ESOP	0.0	0.0	0.0	0.0
Total Shareholders funds	3022.9	3480.1	4967.1	5534.4
Total Debt	286.7	6.6	6.6	6.6
Other non-current Liabilities	63.7	83.7	83.7	83.7
Long-term Provisions	24.5	30.1	30.1	30.1
Total Liabilities	3397.7	3600.5	5087.5	5654.8
Assets				
Gross Block	2,501.6	2,645.8	2,995.8	3,315.8
Less: Acc Depreciation	924.7	1,012.7	1,115.7	1,238.7
Net Block	1,577.0	1,633.0	1,880.1	2,077.1
Capital WIP	53.1	104.4	54.4	29.4
Total Fixed Assets	1630.1	1737.4	1934.5	2106.5
Net Intangible Asset	53.8	52.3	33.4	21.3
Investments	862.0	1,172.8	2,300.5	2,350.5
Inventory	821.9	822.2	700.2	1,035.1
Debtors	932.0	756.5	761.2	867.6
Loans and Advances	20.0	37.7	29.1	59.7
Other Current Assets	298.9	265.8	289.9	343.5
Cash	231.1	318.3	310.3	362.2
Total Current Assets	2,303.9	2,200.4	2,090.6	2,668.1
Creditors	1,212.5	1,264.0	1,065.7	1,214.7
Provisions & Other Curr.Liab	386.8	447.7	339.4	457.2
Total Current Liabilities	1,599.3	1,711.7	1,405.1	1,671.9
Net Current Assets	704.6	488.7	685.5	996.2
Deferred Tax Asset	-52.9	-30.3	-30.3	-30.3
Other non-current assets	117.7	119.0	103.3	150.1
Application of Funds	3397.7	3600.5	5087.5	5654.8

Source: Company, ICICI Direct Research

Exhibit 18: Key ratios				
(Year-end March)	FY19	FY20P	FY21E	FY22E
Per share data (₹)				
EPS	39.6	39.6	40.8	50.3
Cash EPS	46.5	48.1	50.5	61.7
BV	246.6	283.9	405.2	451.5
DPS	2.5	2.5	3.5	4.0
Cash Per Share	75.4	82.6	91.0	101.0
Operating Ratios				
EBITDA Margin (%)	11.8	11.7	11.5	12.5
PAT Margin (%)	7.8	8.4	9.0	9.7
Inventory days	48.4	52.1	46.0	59.6
Debtor days	54.9	47.9	50.0	50.0
Creditor days	71.4	80.1	70.0	70.0
Return Ratios (%)				
RoE	15.6	14.2	10.1	11.1
RoCE	21.7	18.9	13.3	14.2
RoIC	23.2	21.5	16.5	17.3
Valuation Ratios (x)				
P/E	20.2	20.2	19.6	15.9
EV / EBITDA	12.9	13.1	12.3	9.9
EV / Net Sales	1.5	1.5	1.4	1.2
Market Cap / Sales	1.6	1.7	1.8	1.5
Price to Book Value	3.2	2.8	2.0	1.8
Solvency Ratios				
Debt/EBITDA	0.4	0.0	0.0	0.0
Debt/E equity	0.1	0.0	0.0	0.0
Current Ratio	1.6	1.4	1.5	1.7
Quick Ratio	0.9	0.8	0.9	1.0

Source: Company, ICICI Direct Research

Exhibit 19: ICICI Direct Research coverage universe (Auto & Auto Ancillary)

Sector / Company	CMP	TP	Rating	MCap	EPS (₹)			P/E (x)			EV/EBITDA (x)			RoCE (%)			RoE (%)		
	(₹)	(₹)		(₹ Cr)	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E
Apollo Tyre (APOTYR)	90	90	Hold	5,148	8.0	3.7	7.0	11.3	24.5	12.8	5.8	5.3	4.5	4.7	4.1	5.7	4.4	1.9	3.8
Ashok Leyland (ASHLEY)	48	55	Buy	14,050	1.2	1.7	3.2	41.3	28.3	14.9	12.2	10.6	7.2	6.0	7.0	11.9	4.7	5.7	10.4
Bajaj Auto (BAAUTO)	2,550	2,500	Buy	73,789	163.9	146.4	158.6	15.6	17.4	16.1	11.4	12.2	10.6	20.5	22.6	22.5	21.2	17.4	17.2
Bharat Forge (BHAFOR)	275	320	Hold	12,803	10.8	7.0	12.7	25.4	39.1	21.7	13.3	15.3	11.4	8.4	6.3	9.4	9.4	5.7	9.8
Eicher Motors (EICMOT)	14,000	16,870	Hold	38,164	737.9	687.6	838.2	19.0	20.4	16.7	14.5	14.6	11.5	22.9	19.6	20.5	19.1	15.6	16.4
Escorts (ESCORT)	800	860	Hold	9,806	39.6	40.8	50.3	20.2	19.6	15.9	13.1	12.3	9.9	18.9	13.3	14.2	14.2	10.1	11.1
Exide Industries (EXIIND)	150	160	Buy	12,750	9.4	7.6	9.4	15.9	19.7	15.9	8.8	10.0	8.3	16.4	12.8	14.7	12.9	9.6	11.1
Hero Moto (HERHON)	2,150	2,500	Buy	42,936	175.3	118.3	156.4	12.3	18.2	13.7	9.5	11.3	8.6	26.4	20.2	24.6	21.6	15.7	19.1
M&M (MAHMAH)	400	415	Buy	49,728	33.8	15.8	23.5	11.9	25.4	17.0	8.3	12.7	9.2	11.7	6.3	8.9	9.6	5.0	7.1
Maruti Suzuki (MARUTI)	5,000	4,650	Reduce	1,51,040	187.1	138.4	194.4	26.7	36.1	25.7	15.9	18.8	13.3	7.4	4.8	7.9	11.7	8.2	10.6
Minda Industries (MININD)	260	300	Buy	6,817	7.0	7.6	11.8	37.0	34.1	22.0	12.0	10.8	8.6	11.3	11.8	15.0	11.5	11.6	15.4
Tata Motors (TATMOT)	83	85	Hold	30,337	-9.1	-2.4	9.1	NM	NM	9.1	4.1	4.1	3.3	4.6	5.7	8.5	0.0	2.6	9.3

Source: Reuters, ICICI Direct Research

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Buy: >15%

Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



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