

Escorts

Strengthening the core

We initiate on Escorts with a BUY as the domestic tractor OEM will benefit from the equity investment by Japan's leading tractor major Kubota. The partnership will provide new growth avenues for Escorts across product segments (including mechanised equipment) as well as geographies (new export markets as well as manufacturing base for Kubota's international operations). Further, the government is rolling out structural reforms in the agricultural segment, which will enhance farm incomes. These initiatives will promote mechanisation of agriculture.

- Strategic investment by Kubota...**: Escorts has deepened the existing relationship with Kubota as the Japanese partner is investing Rs 10.4bn for a 10% equity stake in Escorts. The Japanese major will have a right to nominate two non-executive board members on the Board.
- ...to provide new growth opportunities across products and geographies:** We believe that Escorts will strengthen its tractor product portfolio, which will drive market share gains (~12% currently) particularly in the southern region, where the north based OEM has been traditionally weak. The arrangement will also enable Escorts to be a part of Kubota's international supply chain and the Indian manufacturing unit could be used as a hub for the Japanese partners' global operations. Escorts will benefit from Kubota's expertise in mechanized equipment - the farm machinery segment is nascent in India, with annual sales of Rs 70bn (\$925mn). As the Indian farming practices mature, this segment is expected to benefit. We believe that Escorts will be well equipped to gain from this shift.
- Agri reforms:** The government has rolled out several structural reforms to improve farm incomes such as amending the stringent Essential Commodities Act and allowing inter state trade in agriculture. These initiatives will benefit the agri chain as it will improve price discovery for the produce, thus enhancing farm incomes. Further, the forecast of normal rainfall by the IMD will be supportive of agri incomes in the current year.
- Initiate with a BUY:** We set a target price of Rs 950 at 15x FY22E EPS. We value the stock at a 15% premium to the last five year average trading multiple. We believe the equity infusion by Kubota will strengthen the balance sheet and will provide multiple growth avenues for Escorts – both in India as well as internationally. **Key risks:** Any delay in implementation of reforms by the government, delays in fund infusion by Kubota/material changes in the arrangement between the two partners.

Financial Summary (Standalone)

YE Mar (Rs mn)	FY18	FY19	FY20	FY21E	FY22E
Net Sales	49,951	61,964	57,610	53,907	62,033
EBITDA	5,572	7,333	6,758	6,092	7,369
APAT	3,493	4,764	4,925	5,049	6,375
APAT Growth (%)	76.0	36.4	3.4	2.5	26.3
Adj. EPS (Rs)	39.3	53.6	55.4	49.9	63.1
Adj. EPS Growth (%)	68.9	36.4	3.4	(9.9)	26.4
P/E (x)	21.3	15.6	15.1	16.7	13.2
RoE (%)	15.4	17.1	15.1	12.0	12.2

Source: Company, HSIE Research

BUY

CMP (as on 19 May 2020)	Rs 835
Target Price	Rs 950
NIFTY	8,879

KEY CHANGES	OLD	NEW
Rating	-	BUY
Price Target	-	Rs 950
EPS %	FY21E	FY22E
	-	-

KEY STOCK DATA

Bloomberg code	ESC IN
No. of Shares (mn)	89
MCap (Rs bn) / (\$ mn)	74/980
6m avg traded value (Rs mn)	2,361
52 Week high / low	Rs 915/423

STOCK PERFORMANCE (%)

	3M	6M	12M
Absolute (%)	(8.2)	26.1	49.2
Relative (%)	18.7	51.5	69.6

SHAREHOLDING PATTERN (%)

	Dec-19	Mar-20
Promoters	40.3	40.3
FIs & Local MFs	6.5	10.0
FPIs	20.4	19.3
Public & Others	32.8	30.5
Pledged Shares	0.0	0.0

Source : BSE

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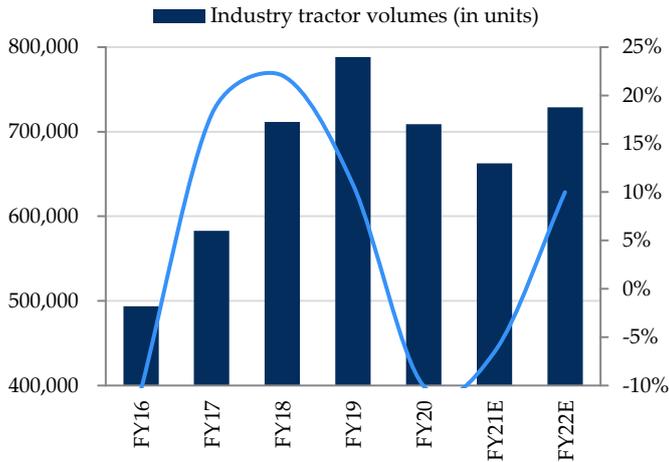
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Escorts: Initiating Coverage

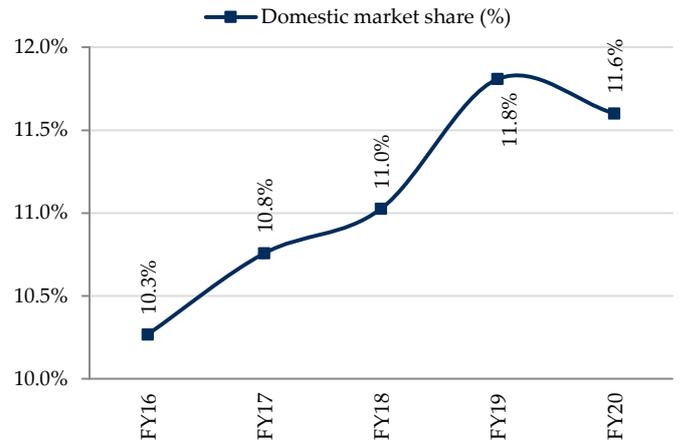
Focus charts

We expect the Indian tractor industry to witness a recovery from Sep-20 onwards



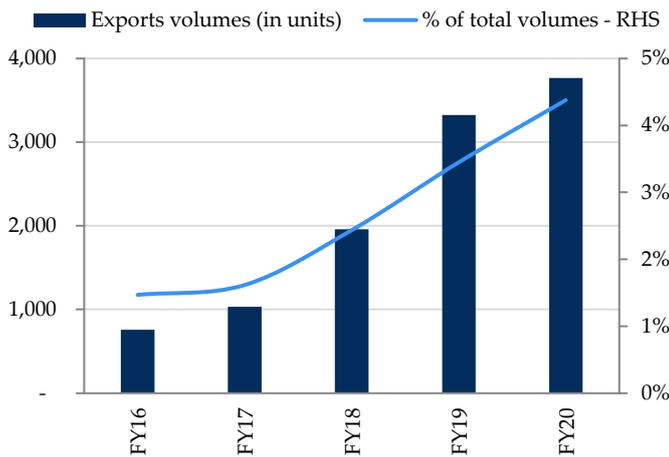
Source: TMA, Company, HSIE Research

Escorts has gained 150bps in market share in the domestic tractor market



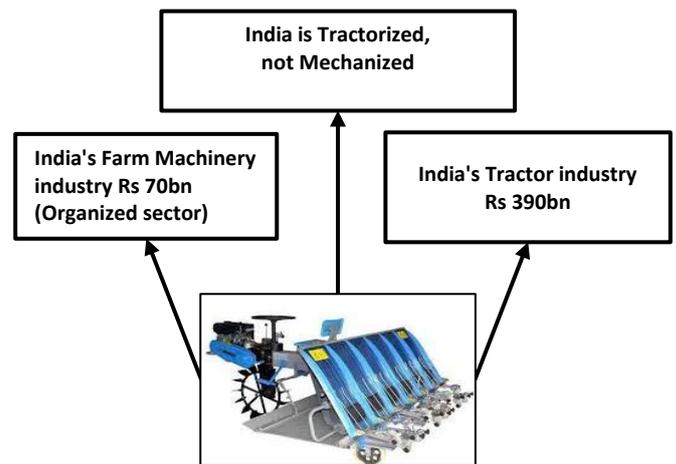
Source: TMA, Company, HSIE Research

Kubota tie up to expand export opportunities for Escorts



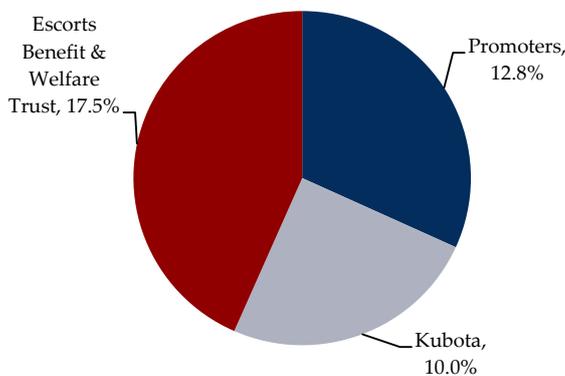
Source: TMA, Company, HSIE Research

Kubota will provide access to the mechanized segment for Escorts



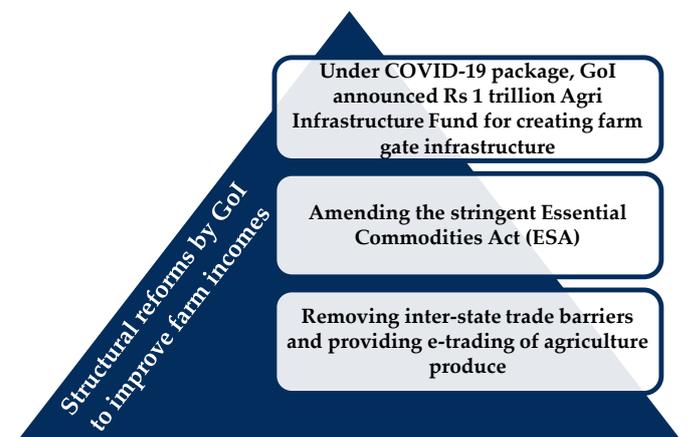
Source: Industry, HSIE Research

Strategic shareholding pattern post Kubota's investment



Source: Company, HSIE Research

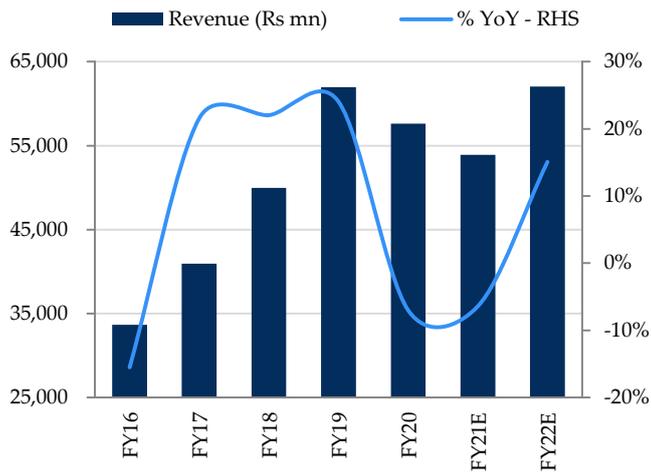
Government reforms for Agri economy



Source: GoI, HSIE Research

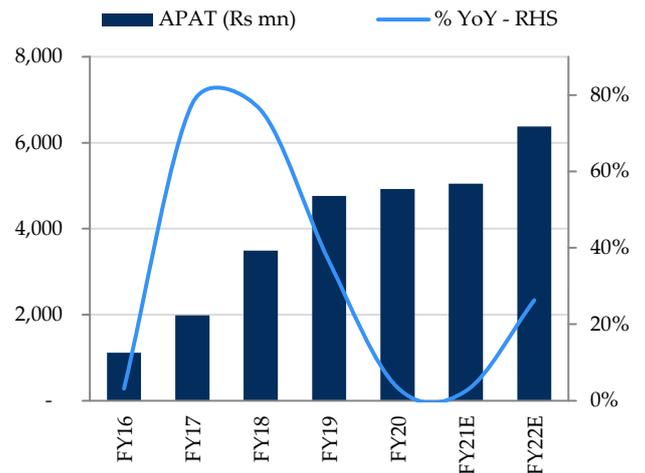
Escorts: Initiating Coverage

Net Revenue



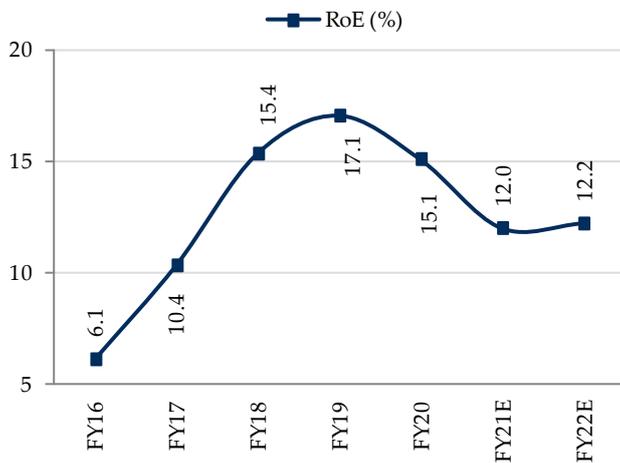
Source: Company, HSIE Research

Adjusted Net Profit



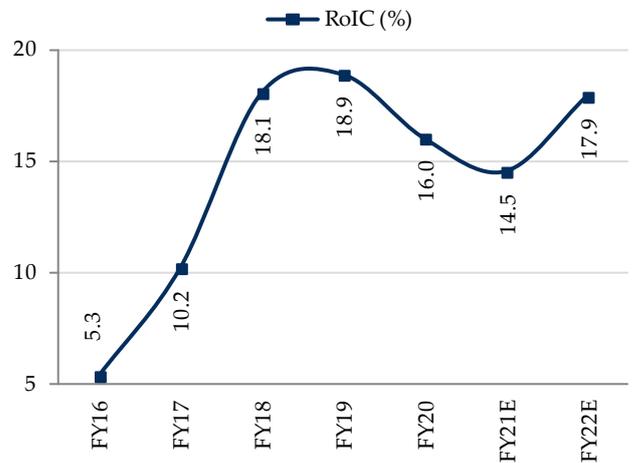
Source: Company, HSIE Research

RoE (%)



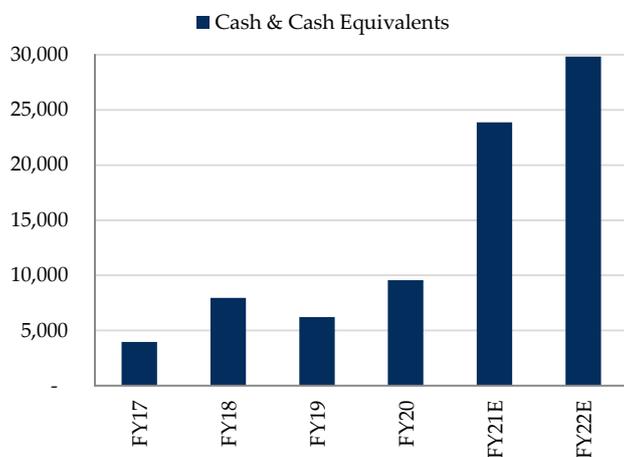
Source: Company, HSIE Research

RoIC (%)



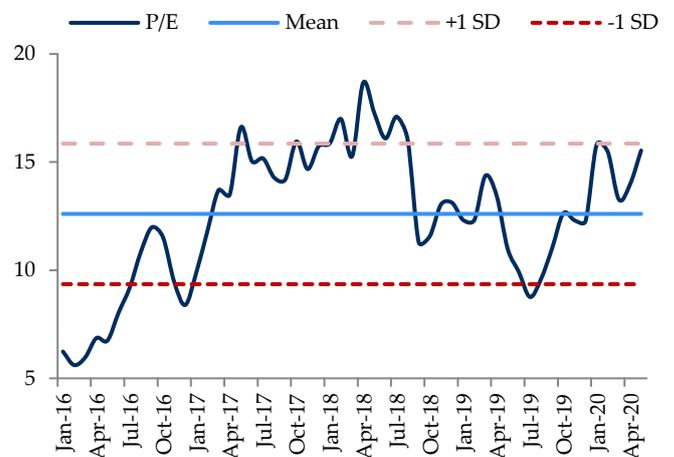
Source: Company, HSIE Research

Cash levels to increase post Kubota's Rs 10.4bn fund infusion



Source: Company, HSIE Research

Escorts rolling forward P/E multiple band chart (x)



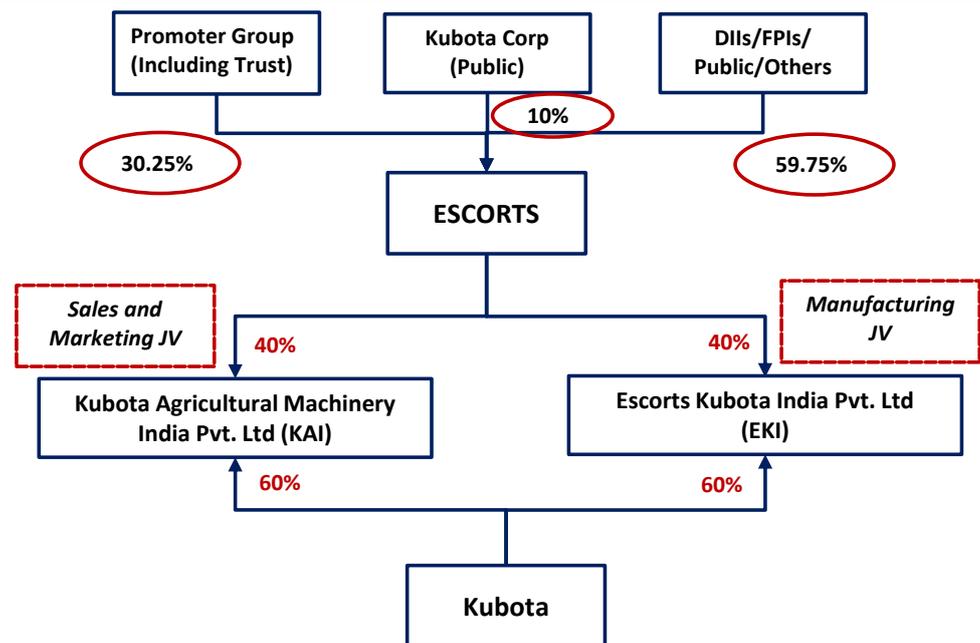
Source: Bloomberg, Company, HSIE Research

Kubota's Strategic Investment to drive new opportunities

- In Mar-20**, Escorts furthered deepened the existing relationship with Kubota through a strategic investment by Kubota in the company. Kubota will pick-up 10% stake in Escorts, with an equity fund infusion of Rs 10.4bn. Simultaneously, Escorts will acquire 40% stake in one of Kubota's Indian subsidiary, Kubota Agri Machinery India Pvt Ltd. (KAI) for Rs 0.9bn, in an all cash deal. KAI is the marketing and sales venture of Kubota in India.
- The Kubota Escorts manufacturing JV (formed in FY19) will continue to operate as planned. With these collaboration initiatives, Escorts will be a dedicated partner of Kubota for the Indian markets.

With access to product technology from Kubota and joint Research and Development efforts, Escorts will target to increase its market share in the Indian markets

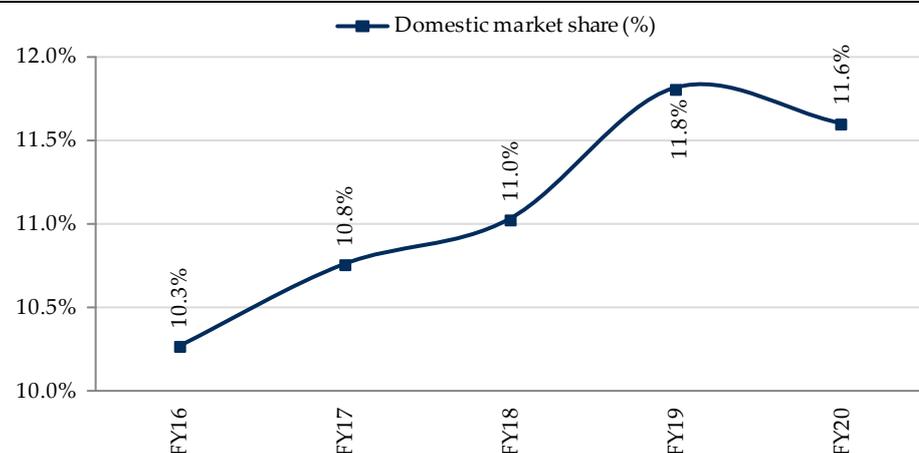
Escorts – Kubota partnership: Resulting Relevant Equity Structure



Source: Company, HSIE Research

- Escorts will target market share gains:** The collaboration with Kubota will enable the companies to integrate product technology, sales & distribution strengths alongside component sourcing and advanced supply chain development. With access to product technology from Kubota and joint Research and Development efforts, Escorts will target to increase its market share in the Indian markets.

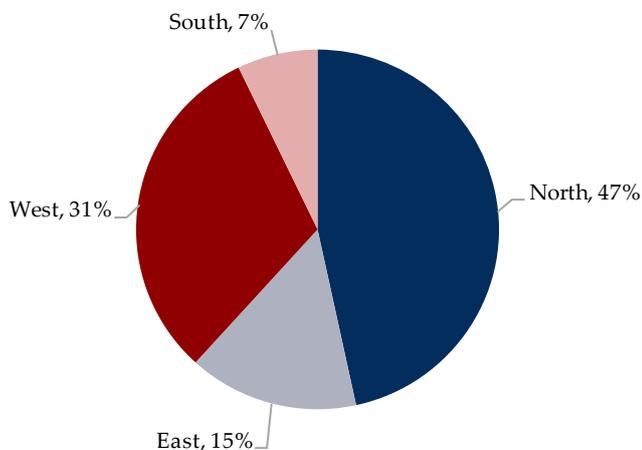
Escorts' domestic market share



Source: TMA, Company, HSIE Research

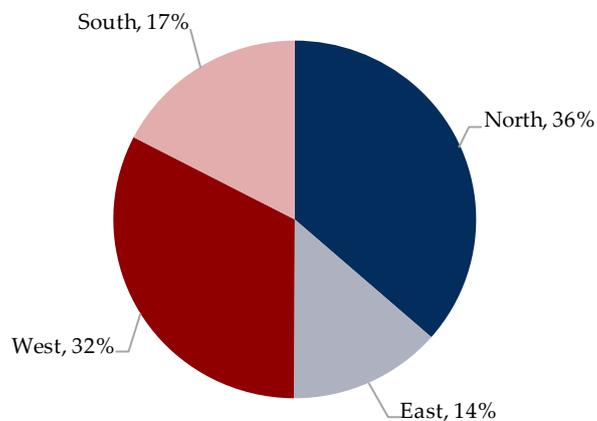
- While Escorts has a market share of ~12% in the Indian tractor market, the OEM has been traditionally weak in the southern market, which is primarily a paddy belt. As the north based company improves its product range further post the tie up, it will attempt to make inroads in the south.

Escorts' FY20 geographical mix



Source: TMA, Company, HSIE Research

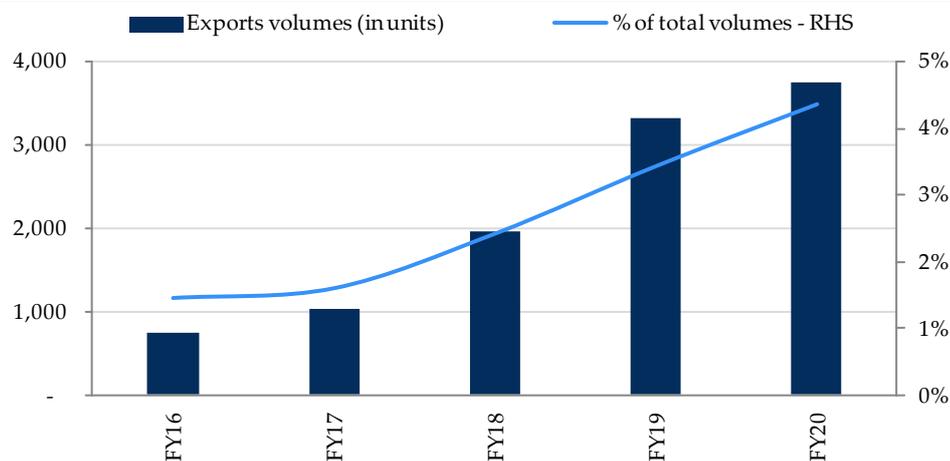
Industry's FY20 geographical mix



Source: TMA, Company, HSIE Research

- The arrangement will also enable Escorts to be a part of Kubota's international supply chain and the Indian manufacturing unit could be used as a hub for low cost supplies to the Japanese partners global operations. This will provide new export opportunities for Escorts. Currently, export volumes are nominal at under 5,000 units p.a. Overseas shipments can be a medium-term opportunity in our view.

Escorts' exports

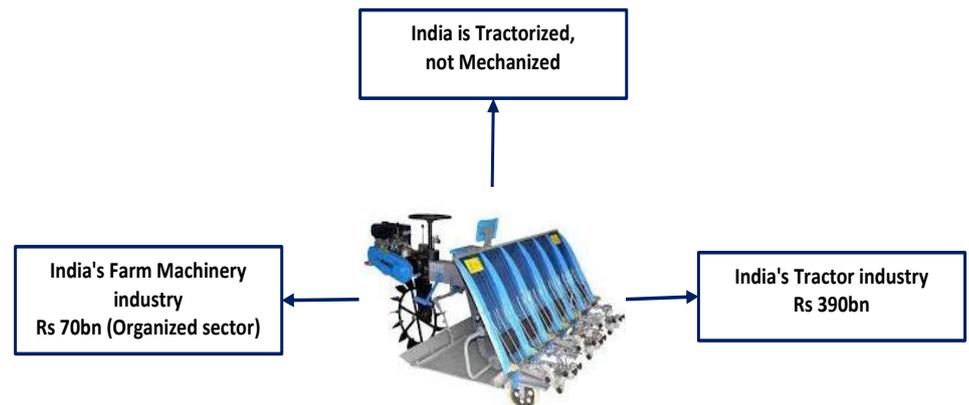


Source: Company, HSIE Research

Escorts will benefit from Kubota's expertise in mechanized equipments such as harvesters, rice trans planters, etc.

- To benefit from mechanization trends:** Escorts will benefit from Kubota's expertise in mechanized equipments such as harvesters, rice trans planters, etc. Currently, while the tractor industry sales are ~Rs 400bn (\$5.3bn), the farm machinery segment is yet nascent, with annual sales at Rs 70bn (\$925mn). As the Indian farming practices mature, Escorts will be well equipped to benefit from this shift aided by the collaboration with Kubota. The steady stream of reforms including reforms in the APMC act, allowing cross state agri trade, etc. will encourage investments in this segment. Further, any reforms around land leasing/contract farming practices will bring in the required economies of scale for the usage of these machines.

India tractor and mechanization trends



Source: Industry, HSIE Research

The capital reduction will be undertaken from the shares currently held by Escorts Benefit and Welfare Trust.

Kubota's investment will constitute 9.1% stake on a pre-capital reduction or 10% on a post-capital reduction basis.

- Transaction details:** In Mar-20, Escorts announced that Kubota will infuse Rs 10.4bn at Rs 850/sh for a 10% stake in the company. The transaction will be done through a preferential issue of 12.2mn equity shares. The entire deal is expected to be completed by 1HFY21, subject to regulatory approvals.

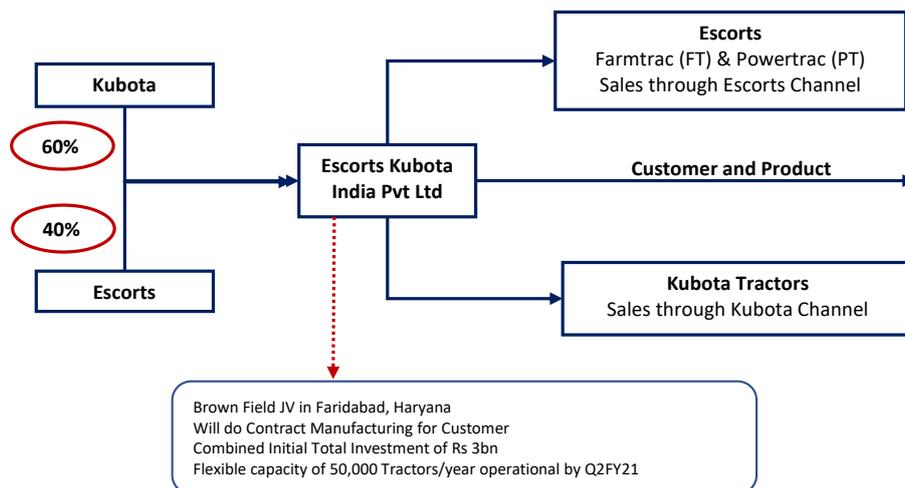
Shareholding pattern of Escorts (%)	As of Mar-20	Post the deal	Comments
Promoter Group Trust*	40.3	30.3	
Kubota Corp	-	10.0	Preferential issue
DIIs/FIIs/Public/Others	57.2	57.2	No change
Non-Promoter/Non-Public	2.5	2.5	No change
Total	100.0	100.0	

*Escorts Benefit and Welfare Trust, currently holds 27.49% of Equity after cancellation same will hold 17.49% of Equity

Source: Company, HSIE Research

- In FY19, Escorts had collaborated with Kubota Corporation for the joint manufacturing of high-end value-oriented utility tractors for domestic and export geographies. Under this 60:40 JV, Escorts Kubota India Pvt Ltd, a manufacturing facility was setup in Faridabad. The manufacturing line has an initial capacity of 50,000 tractors, thereby increasing overall annual capacity to 150,000 tractors for Escorts. The JV will facilitate each other's product platforms as well as focus on technology and process excellence integration.

The existing 60:40 JV between Kubota and Escorts - Escorts Kubota India Pvt. Ltd. ('EKI') will continue to operate as planned earlier



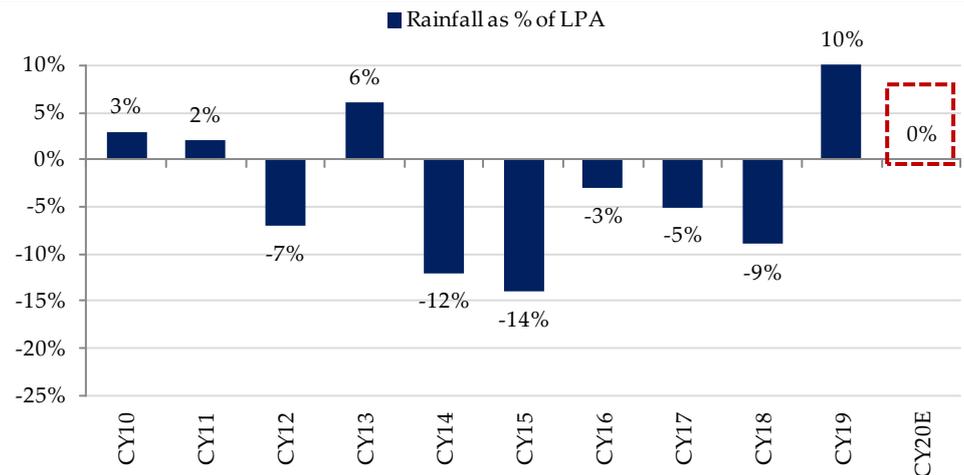
The manufacturing line set up by Escorts and Kubota has an initial capacity of 50,000 tractors, thereby increasing overall annual capacity to 150,000 tractors for Escorts

Source: Company, HSIE Research

Agri segment to benefit from supportive farm policies as well as the monsoons

- Agri economy to benefit from normal monsoons:** The agri economy benefitted from normal rainfall in FY20 (rains were at 110% of LPA). Further, initial forecasts in FY21 suggest that monsoons will be normal as well - in its first long-range forecast for Southwest Monsoon 2020, the India Meteorological Department (IMD) has predicted a normal season with rainfall at 100% of the Long Period Average (LPA). Good rainfalls likely for two consecutive years will be beneficial for agri production.

Annual rainfall as % of LPA

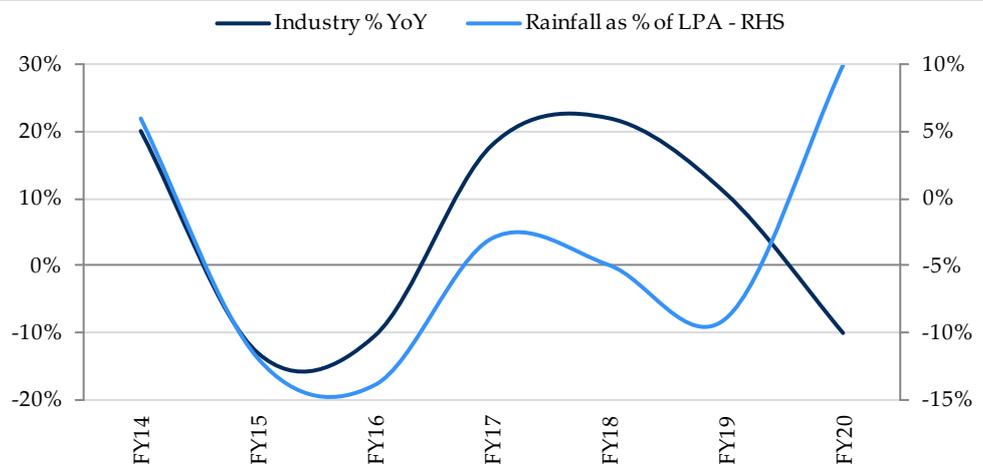


Initial forecasts in FY21 suggest that monsoons will be normal. Agri production will benefit in the current year with good rainfalls likely for two consecutive years

Source: GoI, HSIE Research

- While rainfall trends are closely correlated with tractor sales, FY20 volumes were impacted by the production disruptions in 4Q – a seasonally strong quarter. As monsoons are expected to be normal in FY21E as well, we expect that tractor sales will be relatively less impacted by the COVID led disruption - sustained agri production and favorable government policies will cushion demand for the same.

Tractor Sales and Monsoons are correlated



Source: Industry, GoI, HSIE Research

- The government has rolled out several structural reforms to improve farm incomes as part of relief measures. These initiatives will benefit the agri chain as it will provide better price discovery for the produce, thus enhancing farm incomes.
 - Under the COVID-19 package, the government has announced setting up a Rs 1 lakh crore (Rs 1 trillion) Agri Infrastructure Fund for creating farm gate infrastructure including setting up of cold chains and post harvest infrastructure.
 - Amending the stringent Essential Commodities Act (ESA) to remove cereals, edible oil, oil seeds, pulses, onions and potato from its purview.
 - A new law will be framed to provide farmers the option to choose the market where they want to sell their produce by removing inter-state trade barriers and providing e-trading of agriculture produce. The agricultural marketing policy changes being made to facilitate direct sale to aggregators will aid farm incomes.
 - These initiatives are over and above the regular annual support provided to the rural economy.

Under the COVID-19 package, the government has announced setting up a Rs 1 lakh crore (Rs 1 trillion) Agri Infrastructure Fund

Rural Benefits from Government of India

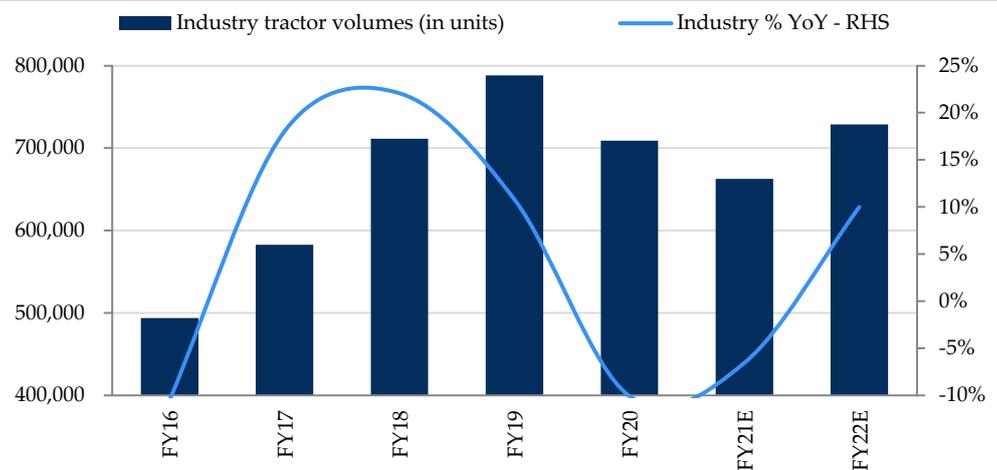
Rs bn	2018-2019 A	2019-2020 RE	2020-2021 BE
Pradhan Mantri Kisan Samman Nidhi (PM-Kisan)	12	544	750
Mahatma Gandhi National Rural Employment Guarantee Program	618	710	615
Pradhan Mantri Awas Yojna (PMAY)	254	253	275
Interest Subsidy for Short Term Credit to Farmers	115	179	212
Pradhan Mantri Gram Sadak Yojna	154	141	195
Crop Insurance Scheme	119	136	157
Pradhan Mantri Krishi Sinchai Yojna	81	79	111
Swachh Bharat Mission (Gramin)	129	83	100
Deen Dayal Upadhyaya Gram Jyoti Yojna	32	37	11
Pradhan Mantri Kisan Sampada	6	9	11
	1,522	2,171	2,437

Source: GoI, HSIE Research

Industry demand outlook

- Escorts' management indicated that 40-50% of the pent-up demand is expected to come back in Jun-Oct20. This demand was lost in the months of Mar-Apr20 due to the nationwide lockdown and the OEM is witnessing higher enquiries. This could lead to improved sales from 2QFY20.
- A strong Rabi harvest, procurement by state governments at remunerative prices, healthy water levels and prediction of normal monsoon this year will drive a gradual recovery.
- We expect industry demand to decline by 7% in FY21. While 1Q will be weak, we expect an improvement in sales from 2QFY21 onwards, while sales in FY22E are expected to grow in double digits.

Tractor industry volumes



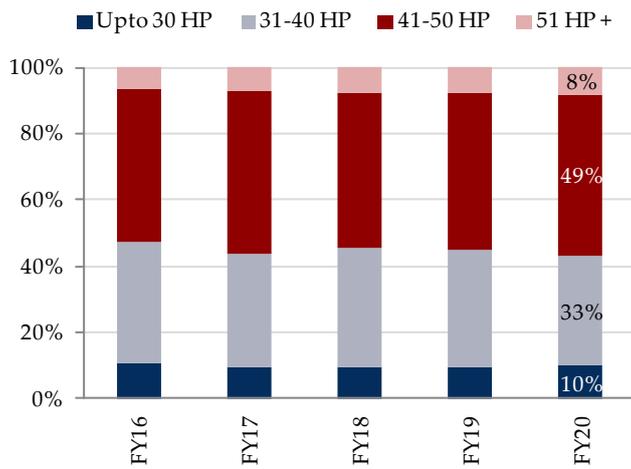
We expect industry demand to decline by 7% in FY21 followed by a double digit recovery in FY22E

Source: TMA, HSIE Research

Escorts: Initiating Coverage

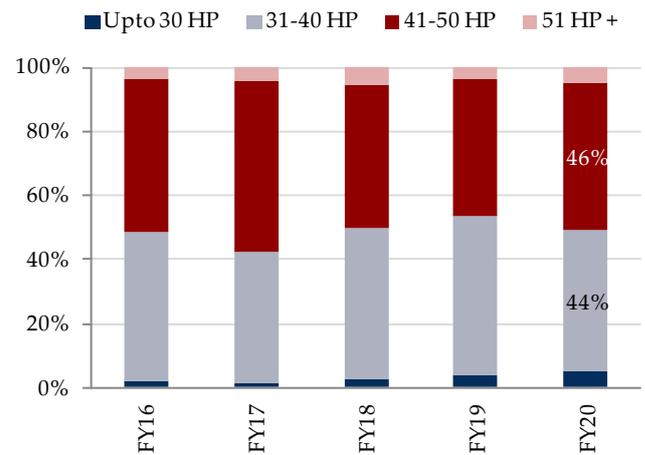
Escorts: Market share and product mix charts

Industry's Product mix (%)



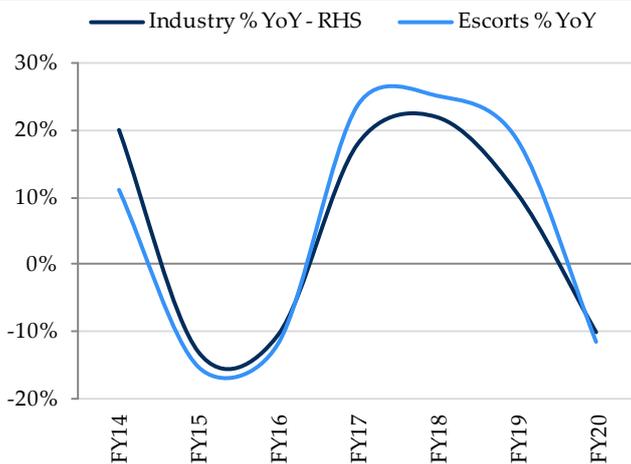
Source: TMA, Company, HSIE Research

Escorts' Product mix (%)



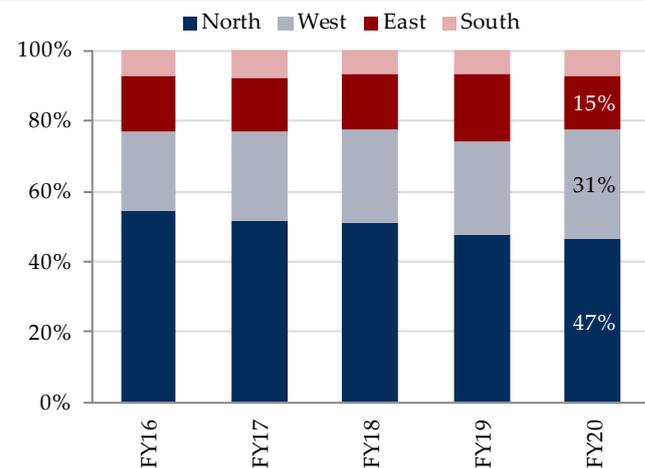
Source: TMA, Company, HSIE Research

Domestic Industry vs. Escorts' % growth YoY



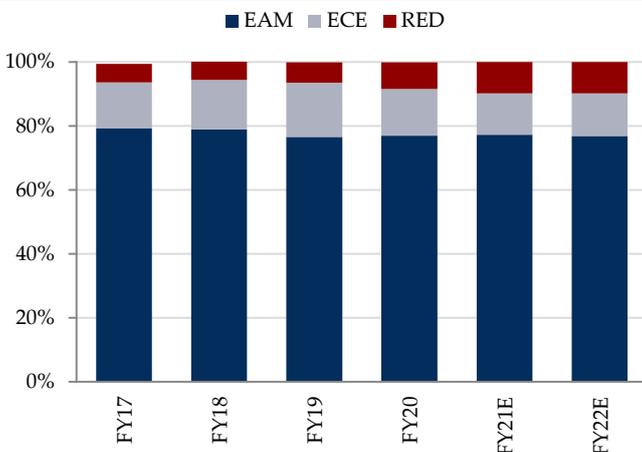
Source: TMA, Company, HSIE Research

Escorts' Geographical mix (%)



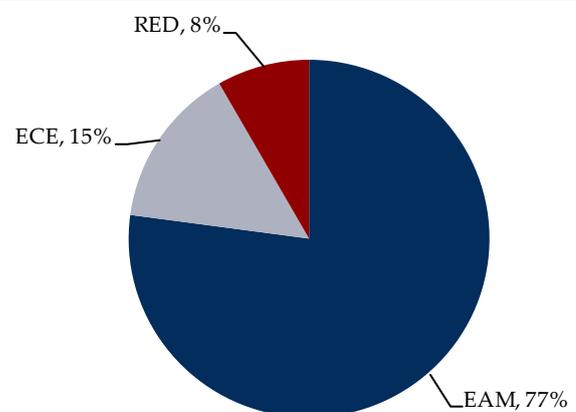
Source: TMA, Company, HSIE Research

Escorts Segmental Revenue (%)



Source: Company, HSIE Research

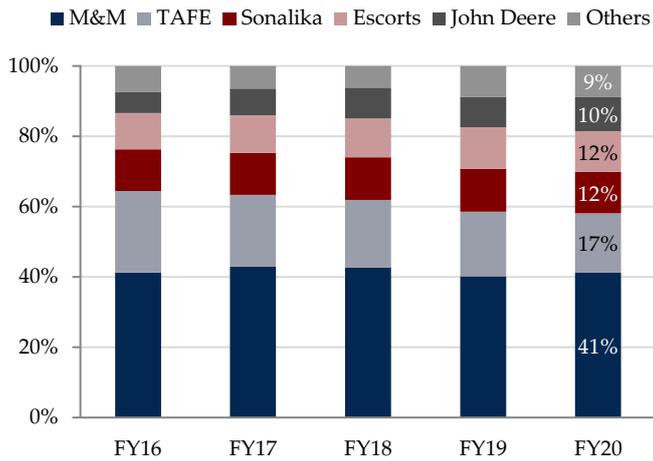
FY20 Segmental Revenue (%)



Source: TMA, Company, HSIE Research

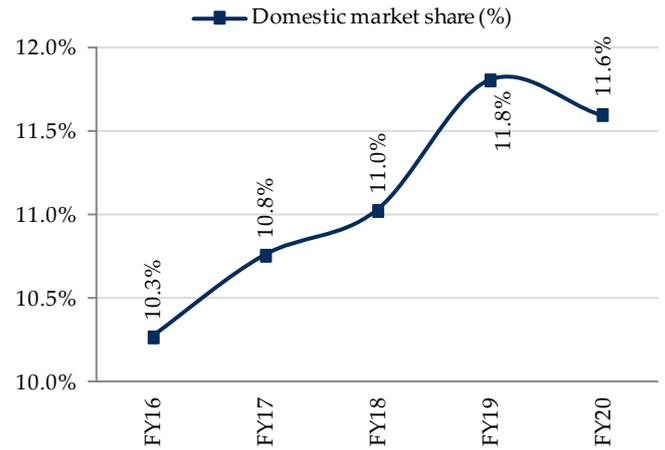
Escorts: Initiating Coverage

Tractor Market Share of OEMs



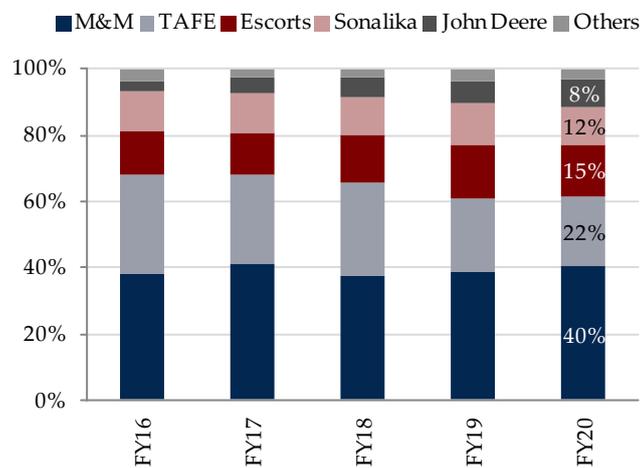
Source: TMA, Company, HSIE Research

Escorts' Market Share



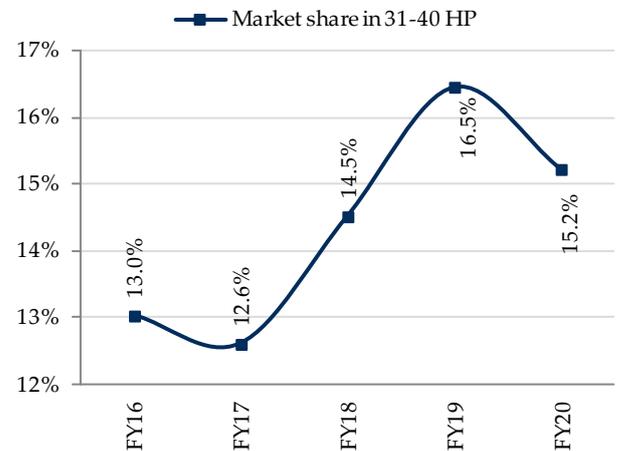
Source: TMA, Company, HSIE Research

31-40 HP Tractor Market Share (%)



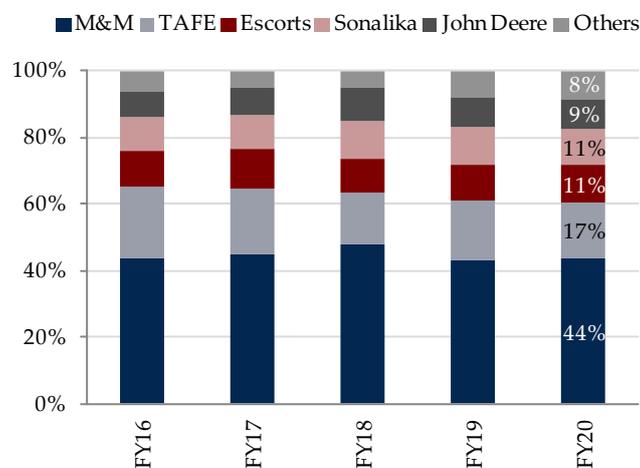
Source: TMA, Company, HSIE Research

Escorts' Market Share in 31-40 HP



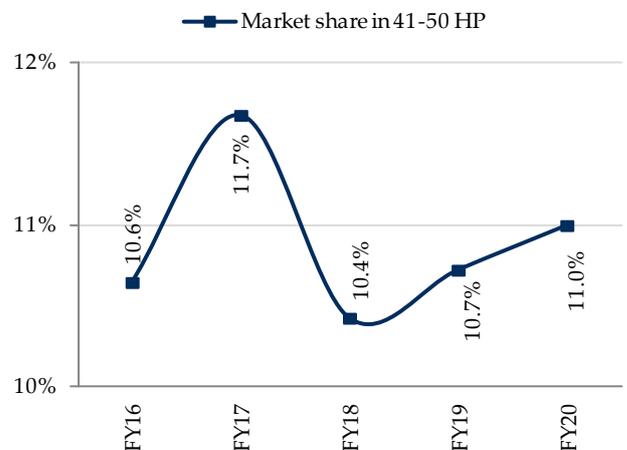
Source: TMA, Company, HSIE Research

41-50 HP Tractor Market Share (%)



Source: TMA, Company, HSIE Research

Escorts' Market Share in 41-50 HP

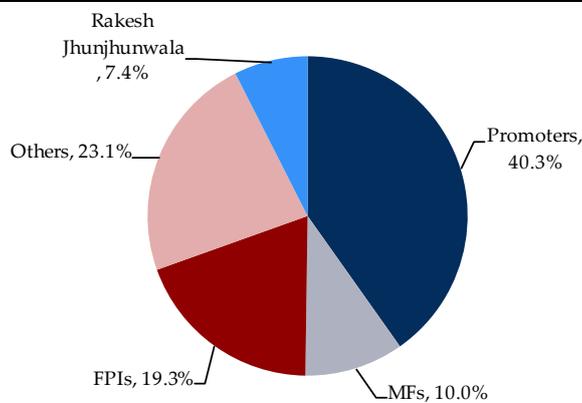


Source: TMA, Company, HSIE Research

Target Price, Valuation and Risks

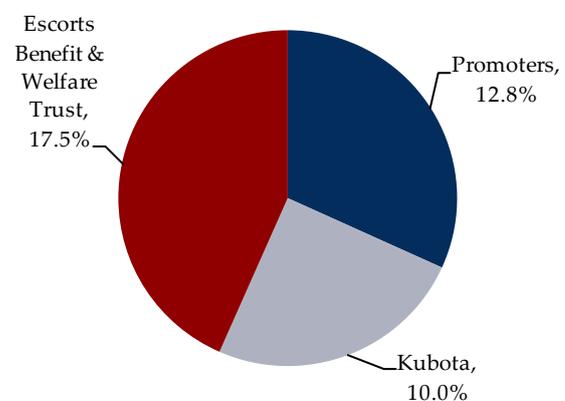
- We set a Mar 21 based target Price of Rs.950 for Escorts based on 15x PE multiple. We value the stock at a 15% premium to the last five year average trading multiple. We believe the equity infusion by Kubota will strengthen the balance sheet and will provide multiple growth avenues for Escorts – both in India as well as internationally.
- **Key Risks:** Any retraction of reforms by the government, delays in fund infusion by Kubota/material changes in the arrangement between the two partners.
- **Shareholding pattern:** Escorts has marquee investors including Mr. Rakesh Jhunjhunwala (7%), foreign investors (19%) and domestic MFs (10%). Post the fund infusion by Kubota (10%), the treasury shares will reduce to 17.5% (from 27.5% currently).

Current shareholding pattern



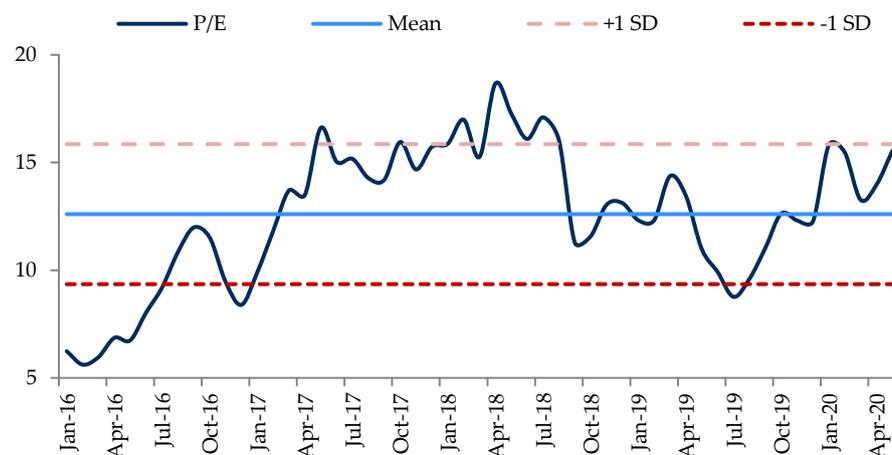
Source: Company, HSIE Research

Strategic shareholding pattern post Kubota's investment



Source: Company, HSIE Research

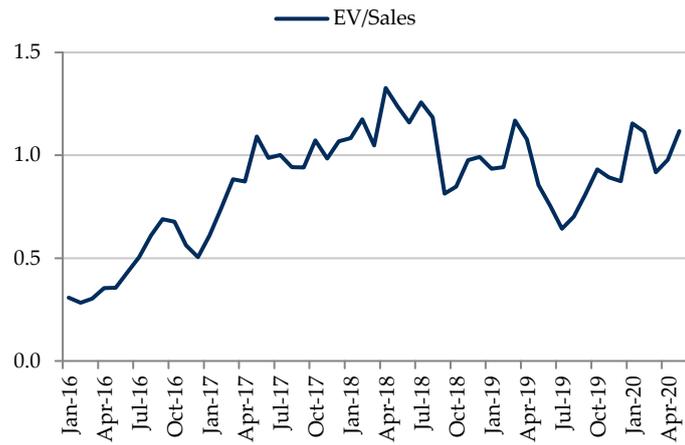
1 year rolling forward P/E band chart



Source: Bloomberg, Company, HSIE Research

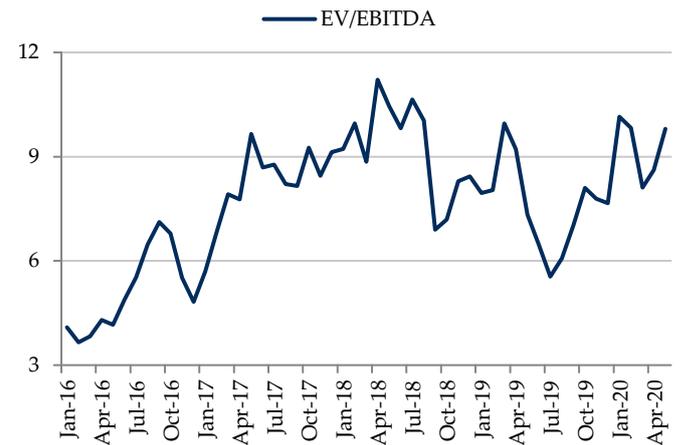
Escorts: Initiating Coverage

1 year rolling forward EV/Sales



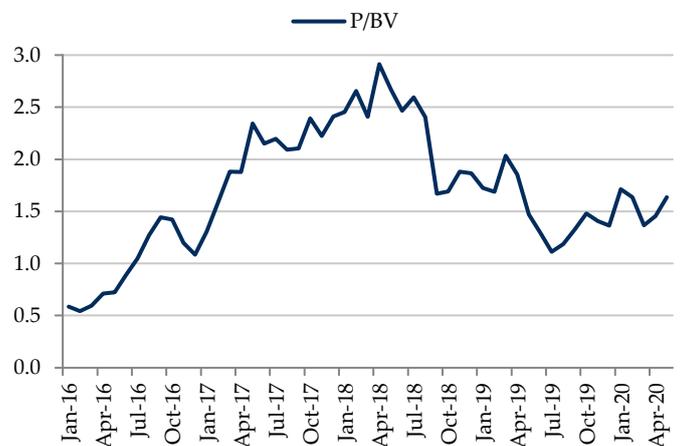
Source: Bloomberg, Company, HSIE Research

1 year rolling forward EV/EBITDA



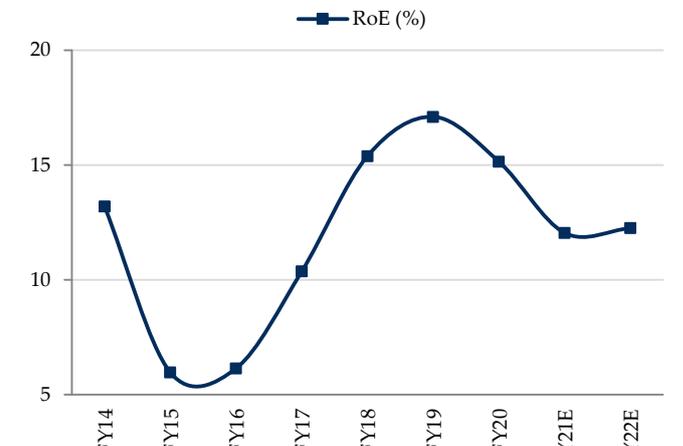
Source: Bloomberg, Company, HSIE Research

1 year rolling forward Price/Book Value



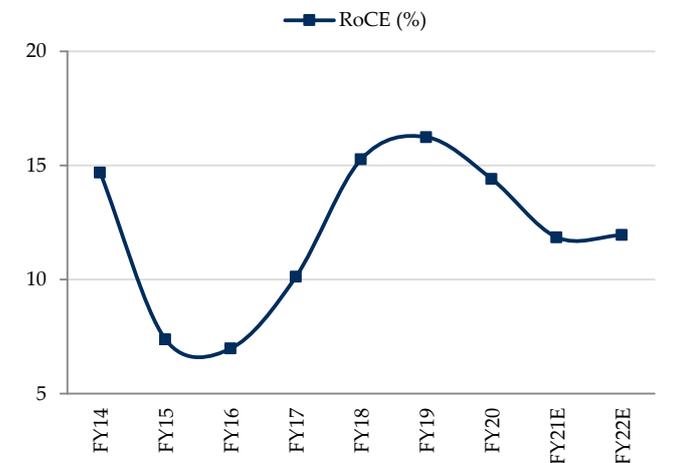
Source: Bloomberg, Company, HSIE Research

RoE (%)



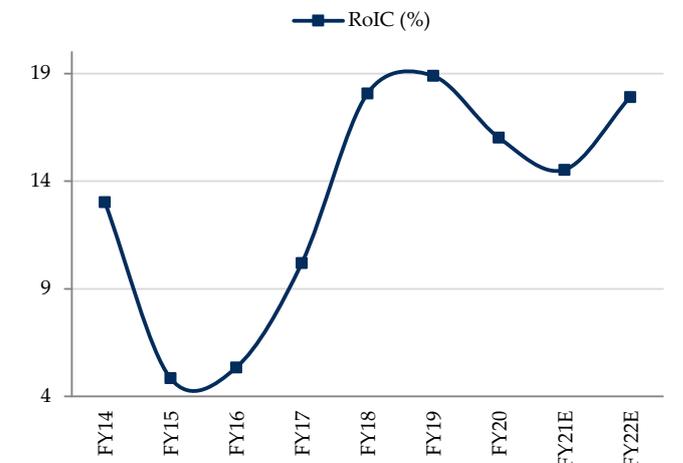
Source: Company, HSIE Research

RoCE (%)



Source: Company, HSIE Research

RoIC (%)



Source: Company, HSIE Research

Key Assumptions

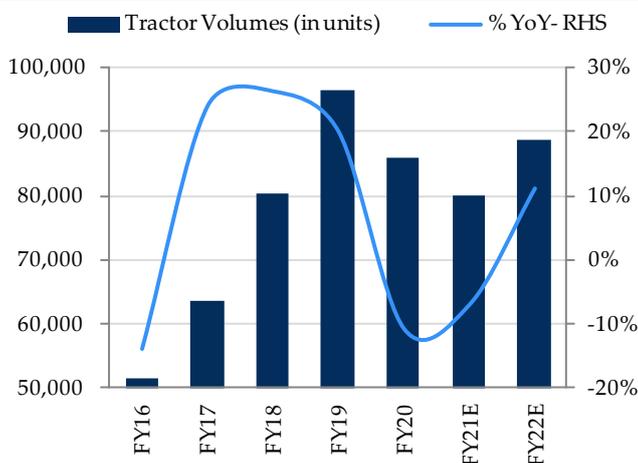
- We expect the Agri Machinery segment volumes to decline by 7% in FY21E owing to the COVID situation. However, we expect Agri machinery to make a sharp recovery in FY22E (+11% growth in volumes) led by pent up demand as well as supportive government policies.
- Construction Equipment volumes are expected to decline by 15% in FY21E owing to weak macroeconomic situation. We expect CE volumes to recover in FY22E (+14% YoY).
- We expect the railway division revenues to grow ~12% CAGR over FY20-22E driven by the sustained capex program of the Indian Railways as well as new product development by Escorts.

Volume Assumption

	FY17	FY18	FY19	FY20	FY21E	FY22E
Agri machinery						
Volumes (in units)	63,730	80,405	96,412	86,017	79,958	88,788
% YoY	24%	26%	20%	-11%	-7%	11%
Revenue (Rs mn)	33,460	39,579	47,440	44,376	41,663	47,702
% YoY	22%	18%	20%	-6%	-6%	14%
Construction Equipment						
Volumes (in units)	3,315	4,486	5,544	4,042	3,436	3,917
% YoY	30%	35%	24%	-27%	-15%	14%
Revenue (Rs mn)	6,068	7,803	10,541	8,398	6,995	8,294
% YoY	22%	29%	35%	-20%	-17%	19%
Railway division						
Revenue (Rs mn)	2,425	2,866	3,941	4,772	5,249	6,037
% YoY	6%	18%	37%	21%	10%	15%
Net Revenue						
	40,932	49,951	61,964	57,610	53,907	62,033
% YoY	22%	22%	24%	-7%	-6%	15%
Avg realisation (Rs)						
	610,509	588,416	607,748	639,686	646,417	669,141
% YoY	-2%	-4%	3%	5%	1%	4%

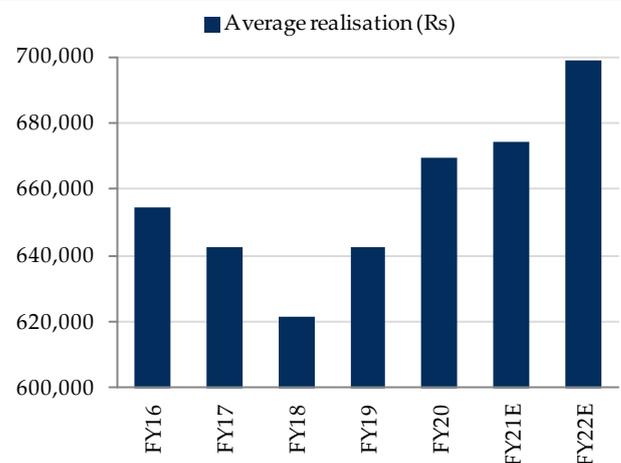
Source: Company, HSIE Research

Escorts' Tractor volumes



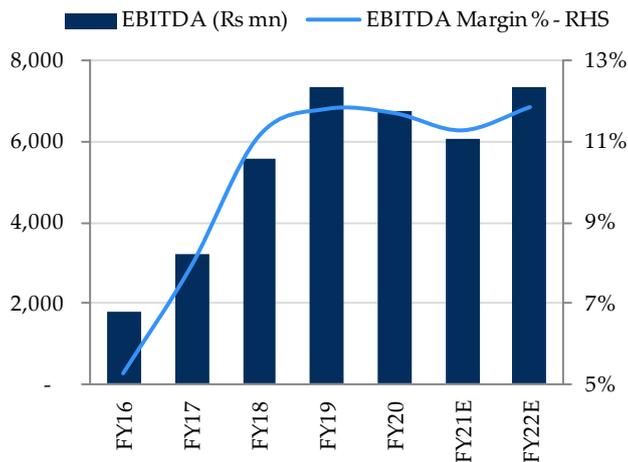
Source: Company, HSIE Research

Escorts' blended realization



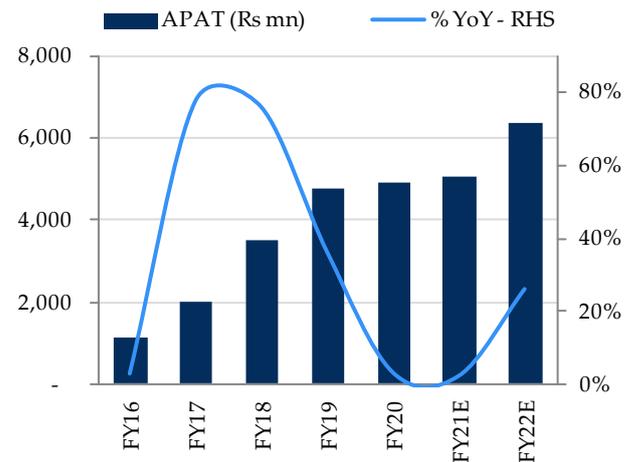
Source: Company, HSIE Research

Escorts' EBITDA margin



Source: Company, HSIE Research

Escorts' Adjusted Net Profit



Source: Company, HSIE Research

Peer set comparison

	Mcap (Rs bn)	CMP (Rs/sh)	Reco	TP	Adj EPS (Rs/sh)			P/E (x)			RoE (%)			EV/EBITDA (x)		
					FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E
Ashok Leyland	127	43	REDUCE	46	1.2	1.0	3.5	35.6	43.1	12.3	4.2	3.4	11.4	10.5	11.8	5.9
Bajaj Auto	726	2,510	ADD	2,695	162.6	138.0	158.4	15.4	18.2	15.8	20.4	15.7	16.6	10.6	12.6	10.4
Eicher	353	12,967	REDUCE	13,800	645.0	542.3	677.2	20.1	23.9	19.1	18.2	13.5	15.0	13.1	15.3	12.1
Escorts Ltd.	74	835	BUY	950	55.4	49.9	63.1	15.1	16.7	13.2	15.1	12.0	12.2	9.6	10.0	7.4
Hero Motocorp	414	2,074	BUY	2,210	151.9	112.3	138.1	13.7	18.5	15.0	22.0	14.8	17.1	9.0	11.9	9.3
Mahindra	457	384	ADD	410	31.3	24.1	31.9	12.2	15.9	12.0	10.2	7.3	9.1	6.5	8.1	6.0
Maruti Suzuki	1,453	4,812	BUY	5,810	187.1	146.0	252.4	25.7	33.0	19.1	11.7	8.5	13.6	14.4	18.8	10.7

Source: HSIE Research

International companies

	P/E (x)			RoE (%)		
	CY20	CY21	CY22	CY20	CY21	CY22
John Deer	21.9	15.3	12.6	NA	22.2	21.3
AGCO	19.8	11.7	10.0	7.2	12.3	12.8
Kubota	13.1	11.7	10.8	9.2	9.6	9.7

Source: Bloomberg consensus

4QFY20 Earnings snapshot:

- Escorts' tractor volumes for the quarter fell ~20% YoY and QoQ. However, the average realization was up ~6% YoY and QoQ.
- The revenues declined by ~15% YoY and QoQ. This was due to 14/28% YoY decline in construction equipment/agri machinery revenues.
- EBITDA margin at 14.1% came in as a surprise (+245/110bps YoY/QoQ). This was due to improved gross margins (+660/460 bps YoY/QoQ) led by higher finished good inventory (+200bps impact), lower raw material prices and improvement in product mix (higher mix of Farmtrac tractors).
- Net profit at Rs 1.4bn was up 15% YoY owing to higher other income (+60% YoY).

Quarterly Financial Snapshot

Particulars (Rs mn)	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20	4QFY20	QoQ (%)	YoY (%)
Volumes (in units)	24,494	21,039	25,743	25,136	21,051	19,750	25,109	20,108	(19.9)	(20.0)
Net ASP (Rs/veh)	617,004	664,651	642,917	649,133	675,963	670,309	650,540	686,632	5.5	5.8
Net sales (incl OOI)	15,113	13,984	16,551	16,317	14,230	13,239	16,334	13,807	(15.5)	(15.4)
Material Expenses	10,219	9,448	11,512	11,227	9,817	8,871	10,916	8,592	(21.3)	(23.5)
Employee Expenses	1,211	1,130	1,196	1,180	1,226	1,253	1,329	1,295	(2.6)	9.7
Other Expenses	1,828	1,830	1,837	2,012	1,763	1,847	1,967	1,975	0.4	(1.8)
Total Expenditure	13,257	12,409	14,546	14,419	12,806	11,972	14,212	11,862	(16.5)	(17.7)
EBITDA	1,856	1,575	2,005	1,898	1,424	1,267	2,123	1,944	(8.4)	2.5
Depreciation	206	215	215	218	241	260	267	278	4.1	27.3
EBIT	1,650	1,360	1,790	1,680	1,183	1,007	1,856	1,667	(10.2)	(0.8)
Other Income	170	221	244	173	167	211	267	278	3.9	60.1
Interest Cost	29	39	43	75	59	39	29	28	(2.4)	(62.0)
PBT	1,791	1,543	1,991	1,778	1,291	1,179	2,094	1,916	(8.5)	7.7
Tax	595	516	699	565	417	41	564	512	(9.2)	(9.3)
PAT	1,196	1,026	1,292	1,214	875	1,138	1,531	1,404	(8.3)	15.7
EO Items (Adj For Tax)	-	-	-	-	-	-	-	-	-	-
APAT	1,196	1,026	1,292	1,214	875	1,138	1,531	1,404	(8.3)	15.7
Adj EPS	9.8	8.4	10.5	9.9	7.1	9.3	12.5	11.5	(8.3)	15.7

As % of sales	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20	4QFY20	QoQ (bps)	YoY (bps)
Material Expenses	67.6	67.6	69.6	68.8	69.0	67.0	66.8	62.2	(459)	(657)
Employee Expenses	8.0	8.1	7.2	7.2	8.6	9.5	8.1	9.4	124	214
Other Operating Expenses	12.1	13.1	11.1	12.3	12.4	14.0	12.0	14.3	227	198
Total Expenditure	87.7	88.7	87.9	88.4	90.0	90.4	87.0	85.9	(109)	(245)
EBITDA	12.3	11.3	12.1	11.6	10.0	9.6	13.0	14.1	109	245
Depreciation	1.4	1.5	1.3	1.3	1.7	2.0	1.6	2.0	38	67
EBIT	10.9	9.7	10.8	10.3	8.3	7.6	11.4	12.1	71	178
Other Income	1.1	1.6	1.5	1.1	1.2	1.6	1.6	2.0	37	95
Interest Cost	0.2	0.3	0.3	0.5	0.4	0.3	0.2	0.2	3	(25)
PBT	11.9	11.0	12.0	10.9	9.1	8.9	12.8	13.9	106	298
Tax	3.9	3.7	4.2	3.5	2.9	0.3	3.5	3.7	26	25
PAT	7.9	7.3	7.8	7.4	6.1	8.6	9.4	10.2	80	273
Tax as % of PBT	33.2	33.5	35.1	31.8	32.3	3.5	26.9	26.7	(19)	(504)

Source: Company, HSIE Research

Segmental Revenue (Rs mn)	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20	4QFY20	QoQ (%)	YoY (%)
Agri machinery products	11,772	10,433	12,926	12,309	10,920	9,956	12,915	10,584	(18.0)	(14.0)
Construction equipment	2,460	2,491	2,660	2,930	2,122	2,010	2,166	2,100	(3.0)	(28.3)
Railway equipment	881	1,059	966	1,035	1,181	1,267	1,244	1,080	(13.2)	4.3

Segmental Revenue Mix (%)	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20	4QFY20	QoQ (bps)	YoY (bps)
Agri machinery products	78	75	78	75	77	75	79	77	(241)	122
Construction equipment	16	18	16	18	15	15	13	15	195	(275)
Railway equipment	6	8	6	6	8	10	8	8	20	148

EBIT %	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20	4QFY20	QoQ (bps)	YoY (bps)
Agri machinery products	14.2	14.7	14.3	13.1	10.9	10.3	14.5	15.8	135	270
Construction equipment	2.4	0.7	3.5	7.1	2.5	2.7	4.8	4.3	(56)	(280)
Railway equipment	25.3	20.0	20.0	15.1	20.0	19.1	18.4	14.0	(440)	(111)

Source: Company, HSIE Research

4QFY20 Conference call takeaways:

■ Tractor segment:

- Management's commentary on this segment was positive owing to a good Rabi harvest, agri procurement by state governments, healthy water levels and prediction of normal monsoon this year.
- Management indicated that 40-50% of the pent-up demand can come back in Jun-Oct'20. This demand was lost in the months of Mar-Apr20 due to the nationwide lockdown and is now coming back in forms of enquiries. This could lead to positive growth from 2QFY20.
- Escorts could gain market share due to favourable geographical mix as the North zone is likely to outperform due to a healthy Rabi output.
- Subsidy led tractor demand is expected to support sales in FY21. Subsidy based sales are likely to jump to FY19 level of 70-80k, which fell significantly in FY20 (due to deferral of purchases by state governments).
- Domestic tractor industry volumes were down by 9% YoY in 4QFY20.

■ Construction Equipment segment:

- Construction equipment volumes for Escorts declined by 32% YoY to 986 units in 4QFY20.
- Industry declined by 24%, led by fall of 25% in Backhoe loaders, 17% in Compactors and 27% in Cranes.
- Company's market share stood at 40% in Cranes, 9.1% in Compactors and 1.3% in Backhoe Loaders.
- Escorts EBIT margin declined to 4.3% in 4QFY20 (-280 bps YoY) due to negative operating leverage.
- The margins in this segment have improved over the years owing to improving product mix and reduction in fixed cost (breakeven point has been reduced by 30% to ~700 units per quarter).
- The management expects the volumes in this segment to decline by 10% YoY in FY21.

■ Railway segment:

- In FY20, revenue grew by 21% YoY (4% YoY in 4QFY20) due to introduction of new products and healthy order-book.
- Escorts has an order book of Rs 5bn (which was Rs 4.5 bn earlier) as of March 31, 2020. These orders are from existing as well as new products and will be executed in 12-15 months.
- The management expects the railways division to grow by 15% YoY in FY21.
- The co has no payment issues with the government.
- An approval for the prototype of Microprocessor Controlled Braking System (MCBS) has been received. This will be commercialised in FY22 on the back of successful trial runs in FY21. Management highlighted that only two MNC players are currently supplying this component and the market size is around Rs 7-8 bn.

■ Dealerships:

- Management highlighted that 65% of dealerships have opened for sale. The situation on ground is improving every passing day.
- ~90% of dealerships have started the workshops.
- The banks have provided moratorium on the working capital loans.
- Dealer network has crossed 1,000 outlets with an addition of 32 dealers in 4QFY20.

■ Supply chain:

- The situation with suppliers is improving gradually.
- The co procures more than 3,000 parts from different suppliers located across India. The co is helping these suppliers in getting necessary approvals to restart production.
- The co has commenced tractor production on May 12th on a single-shift basis (20% utilization level) and the company expects to reach 50-60% utilization levels by mid-June and normal levels by first week of July.
- Currently, the system inventory is at a high level, which will support retail sales until June.

■ Other highlights:

- The co has reduced its earlier capex guidance to Rs 2bn (from earlier planned spend of ~Rs 2.5bn).
- Co's presence remains strong in North, Central and East regions (60-70% of sales). In South markets it has gained market share by 100-120bps.
- 66% of the total financing is done by NBFCs, 33% by private banks and the balance 1% done by PSUs. 40% of the customers have availed moratorium.

Financials

Standalone Income Statement

(Rs mn)	FY15	FY16	FY17	FY18	FY19	FY20P	FY21E	FY22E
Net Revenues	39,858	33,668	40,932	49,951	61,964	57,610	53,907	62,033
<i>Growth (%)</i>	(36.6)	(15.5)	21.6	22.0	24.0	(7.0)	(6.4)	15.1
Material Expenses	28,480	23,351	27,924	33,681	42,407	38,196	36,010	41,221
Employee Expenses	4,318	3,993	3,902	4,311	4,717	5,103	4,852	5,360
Other Operating Expenses	5,487	4,556	5,869	6,387	7,507	7,552	6,954	8,083
Total Expenses	38,285	31,900	37,694	44,379	54,631	50,851	47,816	54,663
EBITDA	1,573	1,767	3,237	5,572	7,333	6,758	6,092	7,369
<i>EBITDA Margin (%)</i>	3.9	5.2	7.9	11.2	11.8	11.7	11.3	11.9
<i>EBITDA Growth (%)</i>	(58.7)	12.3	83.2	72.1	31.6	(7.8)	(9.9)	21.0
Depreciation	661	575	631	725	854	1,046	1,032	1,094
EBIT	912	1,192	2,607	4,847	6,479	5,713	5,060	6,275
Other Income (Including EO Items)	341	435	472	527	918	830	1,675	2,134
Interest	571	495	311	286	185	155	91	21
PBT	682	1,132	2,768	5,088	7,212	6,388	6,644	8,388
Tax (Incl Deferred)	(65)	125	756	1,641	2,375	1,533	1,594	2,013
RPAT	747	1,007	2,012	3,447	4,837	4,855	5,049	6,375
EO (Loss) / Profit (Net Of Tax)	(306)	(123)	38	(68)	109	(92)	-	-
APAT	1,082	1,116	1,984	3,493	4,764	4,925	5,049	6,375
<i>APAT Growth (%)</i>	(55.2)	3.1	77.8	76.0	36.4	3.4	2.5	26.3
Adjusted EPS (Rs)*	12.7	13.1	23.3	39.3	53.6	55.4	49.9	63.1
<i>EPS Growth (%)</i>	(55.2)	3.1	77.8	68.9	36.4	3.4	(9.9)	26.4

Source: Company, HSIE Research *EPS adjusted for treasury shares

Standalone Balance Sheet

(Rs mn)	FY15	FY16	FY17	FY18	FY19	FY20P	FY21E	FY22E
SOURCES OF FUNDS								
Share Capital - Equity	1,226	1,226	1,226	1,226	1,226	1,226	1,226	1,226
Reserves	16,737	17,151	18,686	24,255	29,003	33,575	47,807	53,839
Total Shareholders Funds	17,963	18,377	19,912	25,481	30,229	34,801	49,033	55,065
Long Term Debt	1,057	875	563	137	2	-	-	-
Short Term Debt	3,027	2,202	1,590	-	2,692	66	105	198
Total Debt	4,084	3,077	2,153	137	2,694	66	105	198
Net Deferred Taxes	(478)	(409)	(470)	197	529	303	308	343
Other Non-current Liabilities & Provns	1,481	556	492	388	526	835	918	1,010
TOTAL SOURCES OF FUNDS	23,050	21,600	22,086	26,203	33,977	36,004	50,364	56,616
APPLICATION OF FUNDS								
Net Block	15,830	15,354	15,544	15,578	16,074	16,651	16,993	17,388
CWIP	555	582	347	641	765	1,245	876	630
Investments	3,800	4,348	4,420	4,327	4,886	5,509	5,509	5,509
Other Non-current Assets	227	313	175	1,005	1,166	1,326	1,459	1,605
Total Non-current Assets	20,412	20,597	20,487	21,550	22,891	24,731	24,837	25,132
Cash & Equivalents	2,398	2,542	3,972	7,968	6,212	9,568	23,864	29,830
Inventories	4,159	3,970	4,295	5,411	8,219	8,222	8,418	8,668
Debtors	3,971	3,901	4,580	6,000	9,320	7,565	7,680	8,328
Other Current Assets	2,453	1,264	1,328	1,767	3,328	3,034	3,338	3,671
Total Current Assets	12,981	11,677	14,175	21,145	27,079	28,389	43,300	50,497
Creditors	7,006	7,377	8,938	12,255	12,125	12,639	12,849	13,596
Other Current Liabilities & Provns	3,337	3,297	3,638	4,237	3,868	4,476	4,924	5,416
Total Current Liabilities	10,343	10,674	12,575	16,492	15,993	17,116	17,773	19,013
Net Current Assets	2,638	1,003	1,599	4,653	11,086	11,273	25,527	31,484
TOTAL APPLICATION OF FUNDS	23,050	21,600	22,086	26,203	33,977	36,004	50,364	56,616

Source: Company, HSIE Research

Standalone Cash Flow

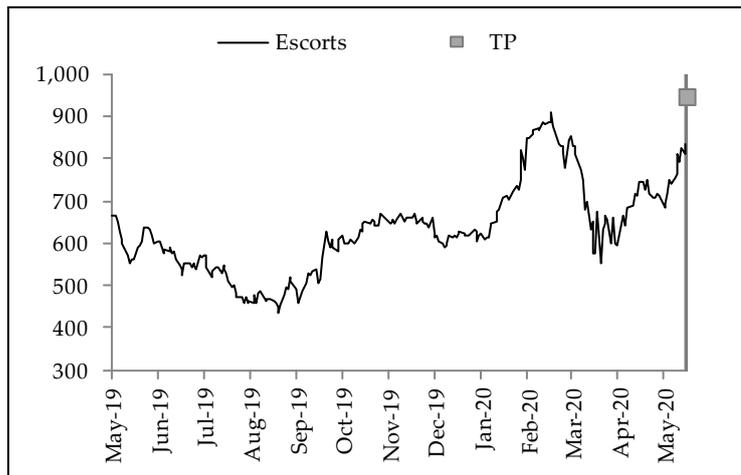
(Rs mn)	FY15	FY16	FY17	FY18	FY19	FY20P	FY21E	FY22E
Reported PBT	682	1,132	2,768	5,088	7,212	6,388	6,644	8,388
Non-operating & EO Items	(341)	(435)	(472)	(527)	(918)	(830)	(1,675)	(2,134)
Interest Expenses	571	495	311	286	185	155	91	21
Depreciation	661	575	631	725	854	1,046	1,032	1,094
Working Capital Change	(442)	1,779	834	942	(8,189)	3,169	43	9
Tax Paid	(340)	(56)	(818)	(974)	(2,044)	(1,759)	(1,589)	(1,978)
OPERATING CASH FLOW (a)	792	3,490	3,253	5,541	(2,900)	8,168	4,545	5,400
Capex	(244)	(127)	(585)	(1,053)	(1,474)	(2,102)	(1,006)	(1,243)
Free Cash Flow (FCF)	547	3,363	2,668	4,488	(4,374)	6,066	3,539	4,157
Investments	(55)	(1,559)	2	(839)	(583)	(475)	(49)	(54)
Non-operating Income	341	435	472	527	918	830	1,675	2,134
INVESTING CASH FLOW (b)	42	(1,250)	(112)	(1,366)	(1,139)	(1,747)	620	837
Debt Issuance/(Repaid)	580	(1,008)	(924)	(2,016)	2,557	(2,628)	39	93
Interest Expenses	(571)	(495)	(311)	(286)	(185)	(155)	(91)	(21)
FCFE	556	1,860	1,433	2,186	(2,001)	3,284	3,487	4,229
Share Capital Issuance	(974)	(469)	(322)	2,338	180	(14)	9,489	0
Dividend	(124)	(124)	(155)	(215)	(269)	(269)	(306)	(343)
FINANCING CASH FLOW (c)	(1,089)	(2,096)	(1,712)	(179)	2,283	(3,066)	9,131	(271)
NET CASH FLOW (a+b+c)	(255)	144	1,430	3,996	(1,756)	3,356	14,296	5,966
Closing Cash & Equivalents	2,398	2,542	3,972	7,968	6,211	9,567	23,864	29,830

Key Ratios

	FY15	FY16	FY17	FY18	FY19	FY20P	FY21E	FY22E
PROFITABILITY (%)								
GPM	28.5	30.6	31.8	32.6	31.6	33.7	33.2	33.6
EBITDA Margin	3.9	5.2	7.9	11.2	11.8	11.7	11.3	11.9
EBIT Margin	2.3	3.5	6.4	9.7	10.5	9.9	9.4	10.1
APAT Margin	2.7	3.3	4.8	7.0	7.7	8.5	9.4	10.3
RoE	6.0	6.1	10.4	15.4	17.1	15.1	12.0	12.2
RoIC (or Core RoCE)	4.8	5.3	10.2	18.1	18.9	16.0	14.5	17.9
RoCE	7.4	7.0	10.1	15.3	16.2	14.4	11.9	11.9
EFFICIENCY								
Tax Rate (%)	(9.5)	11.0	27.3	32.3	32.9	24.0	24.0	24.0
Fixed Asset Turnover (x)	2.5	2.2	2.6	3.2	3.9	3.5	3.2	3.6
Inventory (days)	38.1	43.0	38.3	39.5	48.4	52.1	57.0	51.0
Debtors (days)	36.4	42.3	40.8	43.8	54.9	47.9	52.0	49.0
Other Current Assets (days)	22.5	13.7	11.8	12.9	19.6	19.2	22.6	21.6
Payables (days)	64.2	80.0	79.7	89.5	71.4	80.1	87.0	80.0
Other Current Liab & Provsns (days)	30.6	35.7	32.4	31.0	22.8	28.4	33.3	31.9
Cash Conversion Cycle (days)	2.2	(16.7)	(21.2)	(24.2)	28.7	10.8	11.3	9.7
Debt/EBITDA (x)	1.1	0.3	(0.6)	(1.4)	(0.5)	(1.4)	(3.9)	(4.0)
Net D/E (x)	0.1	0.0	(0.1)	(0.3)	(0.1)	(0.3)	(0.5)	(0.5)
Interest Coverage (x)	1.6	2.4	8.4	17.0	35.1	37.0	55.6	298.8
PER SHARE DATA (Rs)								
Adj. no of shares (in mn; adjusted for treasury)	85	85	85	89	89	89	101	101
Adj. EPS	12.7	13.1	23.3	39.3	53.6	55.4	49.9	63.1
Adj. CEPS	16.5	18.6	31.0	46.9	64.0	66.4	60.1	74.0
Dividend	1.2	1.2	1.5	2.0	2.5	2.5	2.5	2.8
Adj. Book Value	211	215	233	287	340	392	485	545
VALUATION								
P/E (x)	65.8	63.8	35.9	21.3	15.6	15.1	16.7	13.2
P/BV (x)	4.0	3.9	3.6	2.9	2.5	2.1	1.7	1.5
EV/EBITDA (x)	46.4	40.6	21.4	11.9	9.6	9.6	10.0	7.4
EV/Revenues (x)	1.8	2.1	1.7	1.3	1.1	1.1	1.1	0.9
OCF/EV (%)	1.1	4.9	4.7	8.3	(4.1)	12.6	7.5	9.9
FCF/EV (%)	0.8	4.7	3.8	6.8	(6.2)	9.4	5.8	7.6
FCFE/Mkt Cap (%)	0.5	1.8	1.4	2.1	(2.0)	3.2	3.4	4.1
Dividend Yield (%)	0.1	0.1	0.2	0.2	0.3	0.3	0.3	0.3

Source: Company, HSIE Research

RECOMMENDATION HISTORY



Date	CMP	Reco	Target
19-May-20	835	BUY	950

Rating Criteria

- BUY: >+15% return potential
 ADD: +5% to +15% return potential
 REDUCE: -10% to +5% return potential
 SELL: >10% Downside return potential

Disclosure:

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