

Estimate change



TP change



Rating change



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Bloomberg	ESC IN
Equity Shares (m)	123
M.Cap.(INRb)/(USD\$b)	135.7 / 1.8
52-Week Range (INR)	1211 / 423
1, 6, 12 Rel. Per (%)	1/59/134
12M Avg Val (INR M)	2318

Financials & Valuations (INR b)

Y/E March	2020	2021E	2022E
Sales	58.1	61.8	70.1
EBITDA	6.6	8.3	9.3
EBITDA Margin (%)	9.6	11.7	11.5
Adj. PAT	4.8	6.3	7.2
EPS (INR)	54.0	62.4	71.6
EPS Gr. (%)	1.4	15.5	14.8
BV/Sh. (INR)	350.7	469.4	536.1
Ratios			
RoE (%)	16.6	16.0	14.2
RoCE (%)	21.4	21.2	18.8
Payout (%)	5.7	6.8	6.8
Valuations			
P/E (x)	20.5	17.8	15.5
P/BV (x)	3.2	2.4	2.1
EV/EBITDA (x)	14.4	11.4	9.7
Div. Yield (%)	0.2	0.3	0.3
FCF yield (%)	4.5	3.8	4.0

Shareholding pattern (%)

As On	Jun-20	Mar-20	Jun-19
Promoter	40.3	40.3	40.3
DII	10.0	10.0	5.5
FII	22.9	21.8	22.9
Others	26.9	28.0	31.3

FII Includes depository receipts

CMP: INR1,107 TP: INR 1,175 (+6%)
Neutral

Strong operating performance led by cost management

Outlook positive; Supply chain key bottleneck

- Escorts' (ESC) 1QFY21 results were above estimates due to lower other expenses. While demand outlook was strong, the tractor industry is currently facing supply-side constraints, which should ease by mid-Aug'20.
- We have upgraded our FY21/FY22E EPS estimates by ~9%/7%, but are maintaining **Neutral** rating as the positives seem to be fully priced in.

Better mix, lower other expenses/discounts support operating margins

- ESC's 1QFY21 revenues/EBITDA/PAT grew -25%/-16%/5% YoY to ~INR10.6b/INR1.2b/INR0.92b.
- Tractor volumes declined ~14% YoY. Net realizations improved ~1.3% YoY to INR525.4k (v/s est. INR518.5k) due to better mix (higher share of >40HP).
- EBITDA margins expanded ~130bp YoY (-280bp QoQ) to 11.3% (v/s est. ~8.9%). Margin improved due to lower commodity cost, improved product mix (>40hp tractors), lower discounts and other expenses (no marketing spends/lower G&A expenses by INR300-350m due to the 45-day lockdown).
- Tractor PBIT margins improved 355bp YoY (-140bp QoQ) to ~14.5%. PBIT margin of Railways' business declined 2.6% (-17.4pp YoY). Construction equipment had PBIT loss of INR168m due to 78% volume decline.

Highlights from management commentary

- Supply chain constraints:** Currently operating at 50-60% capacity (Jun'20 – 95%) due to supply constraints on fuel injection system from Bosch since end Jun'20. It expects to reach full capacity by mid-Aug'20.
- In FY21, it expects low single-digit growth for the tractor industry, implying ~10% growth for the rest of the year.
- Inventory is 3-3.5 weeks (incl. depots) v/s normal 6-7 weeks (2 weeks at depot and 4-5 weeks at dealer).
- Cost:** It has aggressive plans to cut fixed costs by 10-15% in FY21.
- Kubota JV production should start in 3QFY21.
- Railway business** was impacted due to (a) logistics issues impacting deliveries, and (b) railway units being shut. It is expected to grow in higher single digits and maintain margins.
- Construction equipment** volumes should recover in 2HFY21. Its break-even volumes are 230-250 machines/month and the target is to reduce it further.
- Capex:** INR2.25-2.5b in FY21 for new product development and capacity expansion (machining capacity of 50k).

Valuation and view

- We are upgrading our EPS estimates by 9%/7% for FY21/FY22E to reflect the improving outlook for tractor volumes, mix and cost savings. Our estimates are yet to factor in the benefits from its partnership with Kubota.
- Valuations at 17.8x/15.5x FY21/22E consol. EPS largely reflect the expected recovery. Maintain **Neutral** with TP of INR1,175 (~16x Jun'22E consol. EPS).

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Investors are advised to refer through important disclosures made at the last page of the Research Report.

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Standalone Quarterly Performance

(INR Million)

Y/E March	FY20				FY21				FY20	FY21E	FY21E 1QE
	1Q	2Q	3Q	4Q	1Q	2QE	3QE	4QE			
Net Sales	14,230	13,239	16,334	13,807	10,616	15,077	17,693	18,457	57,610	61,844	11,110
YoY Change (%)	-5.8	-5.3	-1.3	-15.4	-25.4	13.9	8.3	33.7	-7.0	7.4	(21.9)
Total Expenditure	12,805	11,972	14,212	11,862	9,420	13,006	15,238	15,863	50,851	53,526	10,121
EBITDA	1,424	1,267	2,123	1,944	1,196	2,071	2,456	2,595	6,759	8,318	989
Margins (%)	10.0	9.6	13.0	14.1	11.3	13.7	13.9	14.1	11.7	13.5	8.9
Depreciation	241	260	267	278	264	275	285	288	1,046	1,112	280
Interest	59	39	29	28	19	20	20	21	155	80	30
Other Income	167	211	267	278	298	300	320	272	923	1,190	210
PBT	1,292	1,087	2,094	1,916	1,211	2,076	2,471	2,558	6,389	8,316	889
Rate (%)	32.2	3.8	26.9	26.7	23.9	24.2	24.2	24.3	24.0	24.2	24.1
Adj PAT	875	1,135	1,531	1,404	922	1,575	1,874	1,936	4,798	6,306	674
YoY Change (%)	-26.8	10.5	15.2	15.7	5.3	38.8	22.4	37.9	1.4	31.4	-23.0

Key Performance Indicators

	FY20				FY20				FY20	FY21E	FY21E 1Q
	1Q	2Q	3Q	4Q	1Q	2QE	3QE	4QE			
Volumes ('000 units)	21,051	19,750	25,109	20,108	18,150	24,068	27,066	27,916	86,018	97,200	18,150
Change (%)	-14.1	-6.1	-2.5	-20.0	-13.8	21.9	7.8	38.8	-10.8	13.0	-13.8
Net Realn (INR '000/unit)	518.8	504.1	514.4	526.4	525.4	524.0	524.0	523.4	515.9	524.1	518.5
Change (%)	7.9	1.7	2.4	7.5	1.3	4.0	1.9	-0.6	4.8446	1.6	-0.1
Cost Break-up											
RM Cost (% of sales)	69.0	67.0	66.8	62.2	67.1	65.0	65.5	65.8	66.3	65.8	65.0
Staff Cost (% of sales)	8.6	9.5	8.1	9.4	11.9	9.1	8.3	8.0	8.9	9.0	10.8
Other Cost (% of sales)	12.4	14.0	12.0	14.3	9.7	12.2	12.4	12.2	13.1	11.8	15.3
Gross Margins (%)	31.0	33.0	33.2	37.8	32.9	35.0	34.5	34.2	40.1	34.3	35.0
EBITDA Margins (%)	10.0	9.6	13.0	14.1	11.3	13.7	13.9	14.1	11.7	13.5	8.9
EBIT Margins (%)	8.3	7.6	11.4	12.1	8.8	11.9	12.3	12.5	9.9	11.7	6.4
Revenue mix (%)											
Agri Machinery	76.7	75.2	79.1	76.7	89.8	83.7	80.2	79.2	77.0	82.4	84.7
Railway Equipments	8.3	9.6	7.6	7.8	5.2	9.7	8.8	8.4	8.3	8.3	9.6
Construction Equipments	14.9	15.2	13.3	15.2	4.9	6.7	11.0	11.3	14.6	9.0	5.7
Segmental PBIT Margin (%)											
Agri Machinery	10.9	10.3	14.5	15.8	14.5	10.6	9.8	11.3	13.0	11.3	10.8
Railway Equipments	20.0	19.1	18.4	14.0	2.6	8.2	6.0	7.8	18.0	6.8	6.1
Construction Equipments	2.5	2.7	4.8	4.3	-32.0	0.8	2.1	6.5	3.6	0.3	-5.5

E:MOFSL Estimates

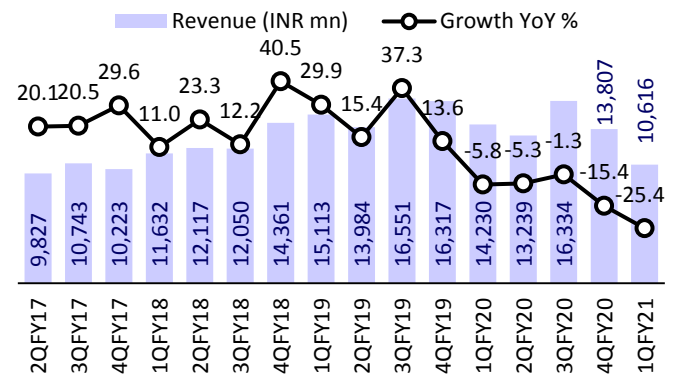


Management call highlights

Tractors

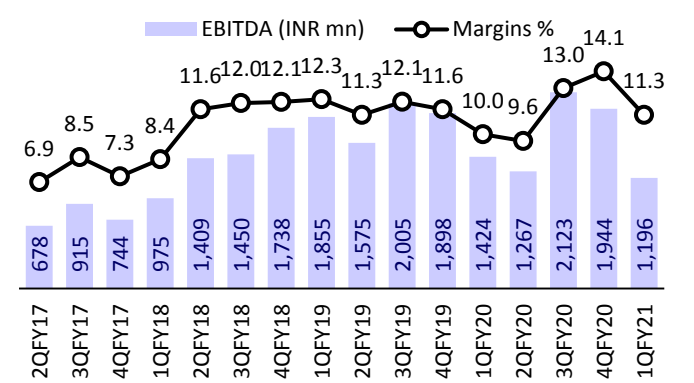
- **Supply Chain constraints** - Biggest challenge to ramp up production is supply chain for the entire industry. For FY21, supply side would determine market size/share. It has reached peak capacity in Jun'20. However, by end-Jun'20, the industry has started facing supply constraints on fuel injection system from Bosch. This is getting resolved and full capacity is expected by mid-Aug'20 (from 50-60% currently), though there would be some near-term uncertainties.
- **Growth Outlook:** For FY21, low single-digit growth for the tractor industry is implied (~10% growth for rest of the year).
- Geographically, it has positive growth, except in West Bengal and Chhattisgarh. Growth is skewed toward the South with 50% growth (v/s pan-India growth of 22%) and is expected to remain skewed for the next 3-4 months.
- This Kharif season crop sowing has been pre-poned; therefore, early harvest might start the season early.
- **Current Inventory** is ~3-3.5 weeks (incl. depots) v/s normal 6-7 weeks (2 weeks at depot and 4-5 weeks at dealer).
- **Operating performance** - Margin has improved due to lower commodity cost along with
 - Improved product mix (>40hp tractors), as share of 40HP+ tractors has increased to 62% in 1QFY21 (v/s 45-46% YoY) v/s 57-58% in 4QFY20,
 - Subdued discounts during the quarter, which is expected to remain subdued till the supply chain normalizes, and
 - Other expenses being lower by INR300-350m due to (a) no SG&A expenses in 45 days shutdown (had resulted in no cost on SG&A of INR300-350m, and (b) no marketing spends, both of which will normalize in the coming quarters.
- **Cost:** It has aggressive plans to cut fixed cost by 10-15% in FY21.
- **Kubota JV production** to start in 3QFY21 (end-Sep'20) for domestic requirement.
- **Exports:** Some delays are seen in aspiration of exports of 8-10k tractors by FY22E (v/s 3k in FY20), however, it should be achieved in the next 3 years.
- **Railway business** was impacted due to (a) logistics issues impacting deliveries, and (b) railway units being shut. Order book at INR4.8b would be executed over the next 12-15 months. For FY21, it expects Rail business to grow in higher single digits and maintain margins.
- **Construction equipment** volumes should recover in 2HFY21. Its break-even volumes are 230-250 machines/month and the target is to reduce it further.
- **Capex:** INR2.25-2.5b in FY21 for new product development and capacity expansion (machining capacity of 50k).

Exhibit 1: Revenue and revenue growth trend



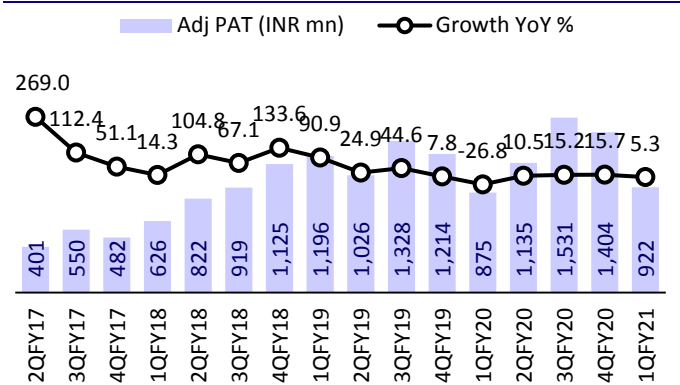
Source: MOFSL, Company

Exhibit 2: EBITDA and EBITDA margin trend



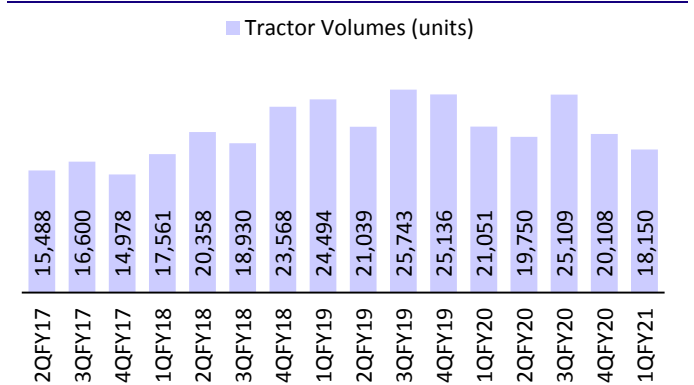
Source: MOFSL, Company

Exhibit 3: Adjusted PAT and growth trend



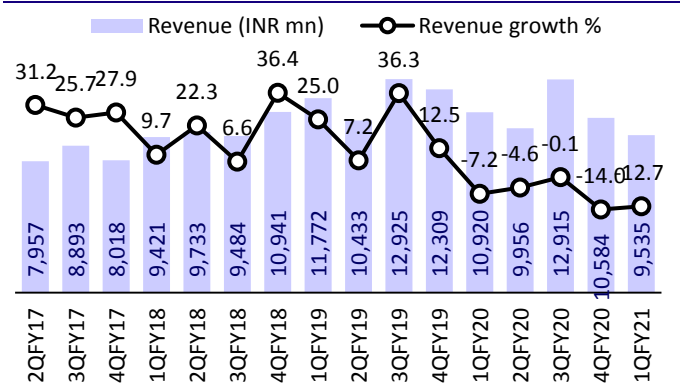
Source: MOFSL, Company

Exhibit 4: Trend in tractor volumes



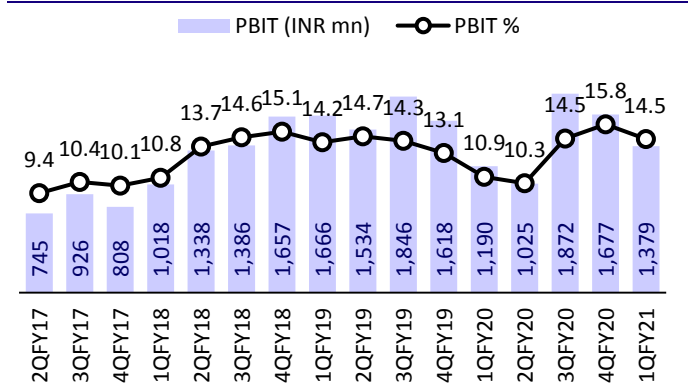
Source: MOFSL, Company

Exhibit 5: Tractor segment revenue and growth



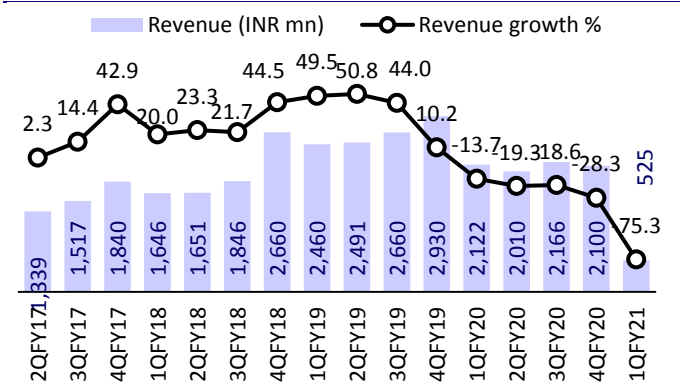
Source: MOFSL, Company

Exhibit 6: Tractor segment PBIT trend



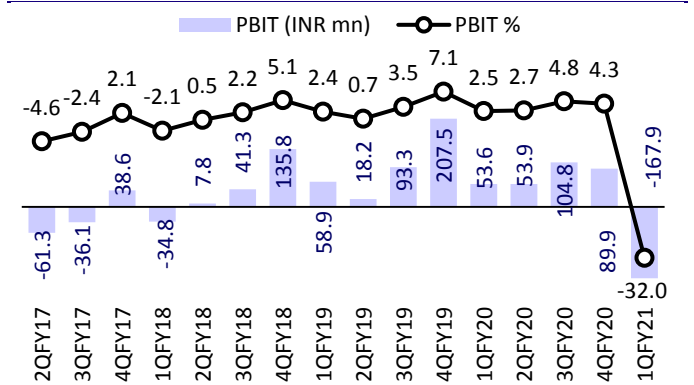
Source: MOFSL, Company

Exhibit 7: Construction equipment revenue and growth



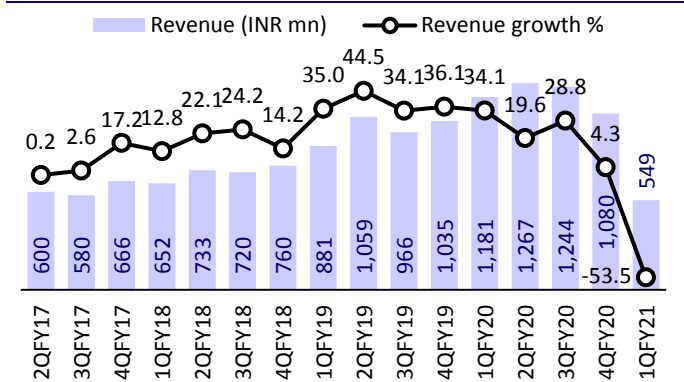
Source: MOFSL, Company

Exhibit 8: Construction equipment segment PBIT trend



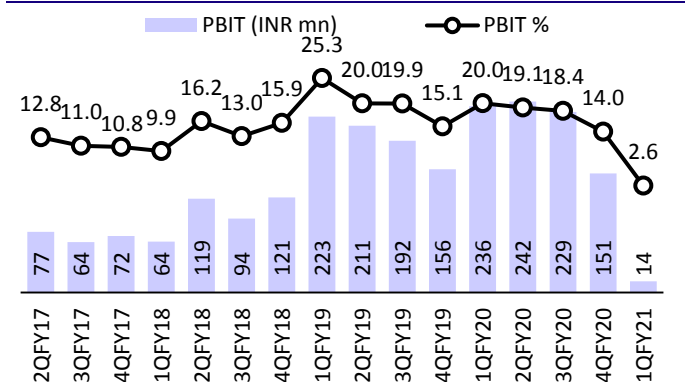
Source: MOFSL, Company

Exhibit 9: Railways' segment revenue and growth



Source: MOFSL, Company

Exhibit 10: Railways' segment PBIT trend



Source: MOFSL, Company

Valuation and view

Favorable farm economics to drive demand despite COVID-19 impact: Farm level sentiment is improving with (a) good improvement in farm level economics led by robust increase in yield and stable prices, (b) good cash flows from the Rabi season, (c) along with good reservoir level and positive outlook for monsoons, and (d) reasonable credit availability. As a result, demand for tractors has improved post relaxation of the lockdown. We expect tractor volume recovery to continue, resulting in Industry volumes growing 7-8% in FY21. We estimate tractor industry volumes to grow 9-10% CAGR over FY20-22E.

Market share gains in tractor business to continue: We expect ESC to garner market share backed by gains in ESC's opportunity market, coupled with gradual improvement in the company's competitive positioning in its traditional market due to plugging of product gaps. This coupled with the Kubota partnership will help to improve competitive positioning of ESC in the long run. We expect ESC to continue outperforming domestic tractor industry volumes with 11-12% CAGR over FY20-22E.

Kubota partnership strengthened with 10% equity stake in ESC: ESC's competitive positioning should improve further post deepening of its relationship with global major Kubota, making ESC a partner of choice for Kubota for its focused India foray. The recent partnership with Kubota (global player in Agri and construction equipment) would also help ESC to improve its competitive positioning in (a) small tractors (<30HP), (b) exploring export markets by leveraging Kubota's distribution network, (c) agri implement business, (d) component sourcing, and (e) construction equipment business (Kubota is global leader in small excavators). Through this partnership, ESC gains access to (a) global product knowhow (in tractors and implements), (b) global distribution network, and (c) global supply chain (by leveraging India cost base).

Healthy traction in railways business, construction equipment to recover from down-cycle: We expect the railway business to deliver ~15% CAGR over FY20-22E, benefitting from the ramp-up in new products, whereas construction equipment revenues are estimated to be flat over FY20-22E. ESC indicated benefits related to localization and cost savings in both segments to elevate the margin profile of both its businesses.

Tractor cycle recovery to result in EPS CAGR of 15% over FY20-22E: With market share expansion in the core tractor business and healthy traction in the railway businesses, we estimate revenues at ~10% CAGR over FY20-22E. We expect ESC margins to expand ~190bp (over FY20-22E) to ~13.3% in FY22E. Consequently, we expect EPS at 15% CAGR. Our estimates are not yet factoring in any contribution from the Kubota JV.

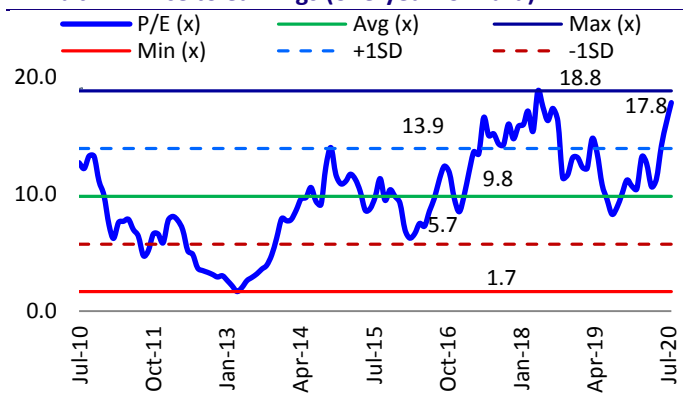
Valuation and view: We are upgrading our EPS estimates by 9%/7% for FY21/22E to reflect the improving outlook for tractor volumes, mix and cost savings. We are factoring in ~13%/10% tractor volume growth for ESC in FY21/22E. Strong balance sheet (net cash) coupled with scope to ramp up the railway and construction equipment business adds to the attractive business fundamentals of tractors. Kubota getting two board seats post acquiring 10% stake in the company should help in improving perception on ESC's corporate governance (none to highlight in the last 5 years). However, valuations at 17.8x/15.5x FY21/22E consol. EPS largely reflects the above mentioned positives and are trading at 25%/55% premium to 5/10 year average PE of 12.5/10x. Maintain **Neutral** with TP of INR1,175 (16x Jun-22 Consol. EPS).

Exhibit 11: Revised forecast (Consol.)

(INR M)	FY21E			FY22E		
	Rev	Old	Chg (%)	Rev	Old	Chg (%)
Net Sales	61,844	62,203	-0.6	70,074	68,366	2.5
EBITDA	8,318	7,775	7.0	9,320	8,888	4.9
EBITDA (%)	13.5	12.5	100bp	13.3	13.0	30bp
Adj. PAT	6,306	5,784	9.0	7,241	6,782	6.8
EPS (INR)	62.4	57.2	9.0	71.6	67.1	6.8

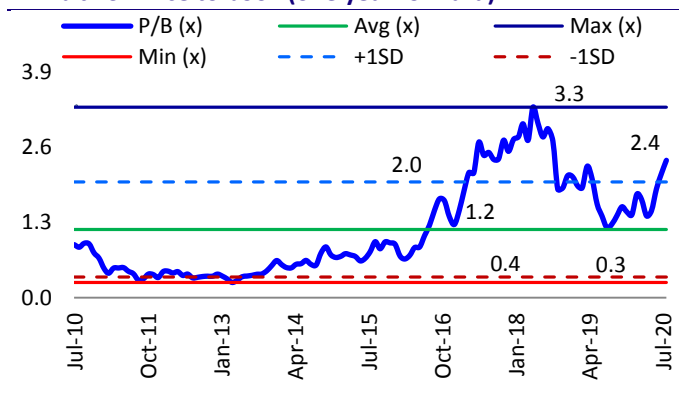
Source: MOFSL

Exhibit 12: Price to earnings (one year forward)



Source: MOFSL, Company

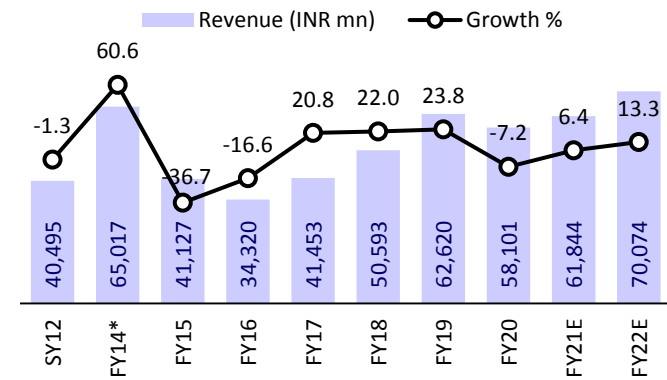
Exhibit 13: Price to book (one year forward)



Source: MOFSL, Company

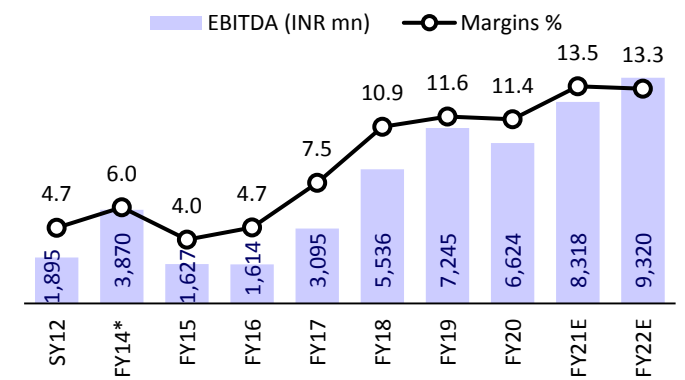
Story in charts

Exhibit 14: Revenue and revenue growth trend



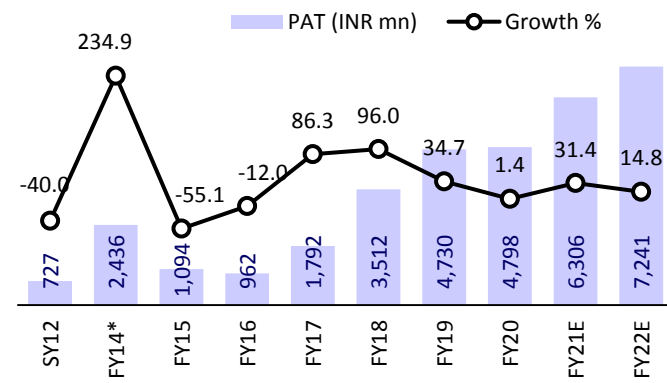
Source: MOFSL, Company

Exhibit 15: EBITDA and EBITDA margin trajectory



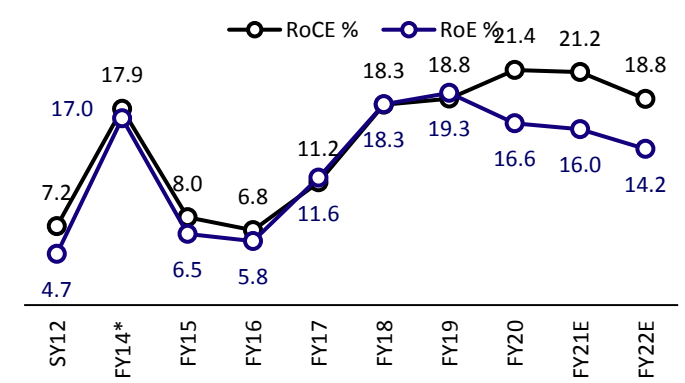
Source: MOFSL, Company

Exhibit 16: PAT and PAT growth trend



Source: MOFSL, Company

Exhibit 17: RoE and RoCE trend



Source: MOFSL, Company

Financials and Valuations

Consolidated - Income Statement

(INR Million)

Y/E March	FY16	FY17	FY18	FY19	FY20	FY21E	FY22E
Total Income from Operations	34,320	41,453	50,593	62,620	58,101	61,844	70,074
Change (%)	-16.6	20.8	22.0	23.8	-7.2	6.4	13.3
EBITDA	1,614	3,095	5,536	7,245	6,624	8,318	9,320
Margin (%)	4.7	7.5	10.9	11.6	11.4	13.5	13.3
Depreciation	581	634	732	872	1,072	1,112	1,268
EBIT	1,033	2,461	4,804	6,373	5,552	7,206	8,052
Int. and Finance Charges	511	322	295	195	172	80	60
Other Income	608	471	653	924	976	1,190	1,540
PBT bef. EO Exp.	1,130	2,610	5,162	7,102	6,356	8,316	9,532
EO Items	-306	-112	-68	56	-92	0	0
PBT after EO Exp.	824	2,498	5,094	7,157	6,263	8,316	9,532
Current Tax	123	773	1,625	2,371	1,535	2,010	2,291
Deferred Tax	0	0	0	0	0	0	0
Tax Rate (%)	14.9	30.9	31.9	33.1	24.5	24.2	24.0
Less: Mionrity Interest	0	11	4	20	0	0	0
Reported PAT	702	1,715	3,466	4,767	4,728	6,306	7,241
Adjusted PAT	962	1,792	3,512	4,730	4,798	6,306	7,241
Change (%)	-12.0	86.3	96.0	34.7	1.4	31.4	14.8
Margin (%)	2.8	4.3	6.9	7.6	8.3	10.2	10.3

Consolidated - Balance Sheet

(INR Million)

Y/E March	FY16	FY17	FY18	FY19	FY20	FY21E	FY22E
Equity Share Capital	1,226	1,226	1,226	1,226	1,226	1,226	1,226
Total Reserves	13,439	14,984	20,926	25,509	29,948	46,245	52,996
Net Worth	14,665	16,209	22,151	26,735	31,174	47,471	54,222
Minority Interest	19	17	-4	56	51	51	51
Deferred Liabilities	0	0	197	529	307	307	307
Total Loans	3,153	2,179	147	2,810	192	192	192
Capital Employed	17,836	18,406	22,492	30,130	31,724	48,021	54,772
Gross Block	25,050	24,600	24,960	26,213	28,040	31,275	33,734
Less: Accum. Deprn.	9,051	8,707	9,082	9,741	10,813	11,925	13,193
Net Fixed Assets	15,999	15,893	15,878	16,472	17,227	19,349	20,541
Capital WIP	216	266	657	800	1,044	309	350
Total Investments	398	2,123	5,490	4,908	7,974	8,974	8,974
Curr. Assets, Loans&Adv.	12,184	13,187	17,700	24,890	23,895	36,287	44,056
Inventory	4,326	4,503	5,657	8,574	8,834	6,461	7,321
Account Receivables	3,750	4,565	5,920	9,311	7,319	7,116	8,063
Cash and Bank Balance	2,530	2,441	3,173	2,433	3,249	17,316	22,200
Loans and Advances	1,578	1,679	2,949	4,572	4,494	5,393	6,472
Curr. Liability & Prov.	11,604	13,587	17,242	16,952	18,430	16,913	19,163
Account Payables	9,997	12,064	15,746	15,495	16,867	15,249	17,279
Provisions	1,606	1,522	1,495	1,458	1,563	1,663	1,885
Net Current Assets	580	-399	458	7,938	5,465	19,374	24,893
Deferred Tax assets	643	523	8	12	14	14	14
Misc Expenditure	0	0	0	0	0	0	0
Appl. of Funds	17,836	18,406	22,493	30,130	31,724	48,021	54,772

Financials and Valuations

Ratios

Y/E March	FY16	FY17	FY18	FY19	FY20	FY21E	FY22E
Basic (INR)							
EPS (ex treasury)	11.3	21.0	39.5	53.2	54.0	62.4	71.6
Cash EPS	18.1	28.5	47.8	63.0	66.0	73.3	84.1
BV/Share	172.0	190.1	249.2	300.8	350.7	469.4	536.1
DPS	1.2	1.0	1.5	1.8	1.8	2.9	3.3
Payout (%)	25.2	9.2	6.2	5.6	5.7	6.8	6.8
Valuation (x)							
P/E	98.1	52.7	28.0	20.8	20.5	17.8	15.5
Cash P/E	61.2	38.9	23.2	17.6	16.8	15.1	13.2
P/BV	6.4	5.8	4.4	3.7	3.2	2.4	2.1
EV/Sales	2.8	2.3	1.9	1.6	1.6	1.9	1.6
EV/EBITDA	58.9	30.4	17.2	13.6	14.4	11.4	9.7
Dividend Yield (%)	0.1	0.1	0.1	0.2	0.2	0.3	0.3
FCF per share	14.4	19.5	28.9	-31.6	50.2	42.1	44.3
Return Ratios (%)							
RoE	5.8	11.6	18.3	19.3	16.6	16.0	14.2
RoCE	6.8	11.2	18.3	18.8	21.4	21.2	18.8
RoIC	5.6	12.0	24.5	24.2	20.2	26.7	27.4
Working Capital Ratios							
Asset Turnover (x)	1.9	2.3	2.2	2.1	1.8	1.3	1.3
Inventory (Days)	66	58	61	73	84	58	58
Debtor (Days)	39	39	43	54	46	42	42
Creditor (Days)	106	106	114	90	106	90	90
Working Cap. Turnover (Days)	-21	-25	-20	32	14	12	14
Leverage Ratio (x)							
Current Ratio	1.0	1.0	1.0	1.5	1.3	2.1	2.3
Interest Cover Ratio	2	8	16	32.6	32.2	90.1	134.2
Net Debt/Equity	0.0	-0.1	-0.4	-0.1	-0.3	-0.5	-0.5

Consolidated - Cash Flow Statement

(INR Million)

Y/E March	FY16	FY17	FY18	FY19	FY20	FY21E	FY22E
OP/(Loss) before Tax	789	1,903	5,091	7,157	6,253	8,316	9,532
Depreciation	612	649	732	872	1,072	1,112	1,268
Interest & Finance Charges	145	11	-26	-301	0	80	60
Direct Taxes Paid	11	-437	-1,021	-2,166	-1,748	-2,010	-2,291
(Inc)/Dec in WC	605	548	-181	-7,449	3,272	158	-635
CF from Operations	2,161	2,674	4,596	-1,887	8,849	7,656	7,934
Others	132	365	5	-456	-877	0	0
CF from Operating incl EO	2,293	3,038	4,601	-2,343	7,972	7,656	7,934
(inc)/dec in FA	-532	-654	-1,059	-1,529	-1,822	-2,500	-2,500
Free Cash Flow	1,761	2,384	3,541	-3,873	6,150	5,156	5,434
(Pur)/Sale of Investments	-275	-1,196	-2,934	994	-2,390	-1,000	0
Others	376	304	252	362	0	0	0
CF from Investments	-432	-1,546	-3,742	-174	-4,212	-3,500	-2,500
Issue of Shares	0	0	2,501	28	0	10,419	0
Inc/(Dec) in Debt	-1,212	-1,031	-2,134	2,309	-2,644	0	0
Interest Paid	-463	-287	-216	-138	-100	-80	-60
Dividend Paid	-132	-128	-161	-289	-260	-428	-490
Others	-37	314	0	-3	4	0	0
CF from Fin. Activity	-1,844	-1,131	-10	1,906	-3,001	9,911	-550
Inc/Dec of Cash	17	361	849	-611	758	14,067	4,884
Opening Balance	2,514	2,530	2,441	1,541	931	3,249	17,316
Closing Balance	2,531	2,892	3,290	931	1,689	17,316	22,200

NOTES

Explanation of Investment Rating	
Investment Rating	Expected return (over 12-month)
BUY	>=15%
SELL	< - 10%
NEUTRAL	< - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

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