RESEARCH REPORT

13th April 2021

ACTION CONSTRUCTION EQUIPMENT LTD

BSE : ACE | **Sector: CRANES,MHE & FARM EQUIPMENT** | **BSE: 532762**

View - BUY

CMP : Rs. 153

Target Price: Rs 240 (In next 12 to 18 mths)

Suggested Buying Range (Between Rs 150 to Rs 170)

BUSINESS BACKGROUND

Action Construction Equioment Ltd (ACCE) incorporated in 1995, manufactures material-handling and construction equipment. It has four segments: Cranes (65% of sales), material handling equipment (7%), construction equipment (7%), and agriculture equipment (21%).

ACCE is a leading manufacturer of mobile cranes (63% market share) and tower cranes (60%) in India. ACCE also caters to a large clientele base, (with over 15000 customers) which includes major Indian as well as international players such as Reliance, L&T, BSES, BHEL, Gammon, NCC, Gujarat Ambuja, IISCO, Simplex, Coal India, etc & its products are used in sectors like infrastructure, construction, roads, engineering, coal mines, chemical and fertilizer plants, power stations, ports, heavy project engineering, railways, cement, oil, defense etc.

INVESTMENT HIGHLIGHTS

Steady Financial Performance for FY20 & Q3FY21 –

ACE reported a steady set of FY20 numbers in a difficult year with net sales at Rs 1156 crs as compared to a revenue of Rs 1343 crs last year, with EBIDTA placed at Rs 92 crs from Rs 98 crs last year with the PAT placed at Rs 52 crs from Rs 56 crs. ACE declared a dividend of 26% for FY20.

For ACE for first 9 months of FY21 Revenue was Rs. 767 crs with EBIDTA at Rs 69.28 crs with the PAT at Rs 57 crs vs Rs 49 crs in the same period last year

ACE enjoys well diversified product basket with a strong clientele base –

ACE manufactures material-handling and construction equipment. It has four segments which include cranes (65% of sales), material handling equipment (7%), construction equipment (7%), and agriculture equipment (21%). ACE is a market leader in mobile cranes (63% market share) and tower cranes (60%) in India.

In fact ACE is amongst the few home-grown Indian companies, which, which today has one of the widest range of construction equipment in the industry. ACE is the only company to manufacture 12 Tons & 16 Tons Tower Cranes and the biggest Pick & Carry Crane in India which is of 25 Tons. ACE has always been a customer-centric player giving timely support and service to customers which has enabled it to build a strong customer base of over 15000 nos in the last 22 years with major clients added like Reliance, L & T. NCC, Dilip Buildcon, Adani, BHEL, JSW, Tatas etc.

KEY DATA

FACE VALUE Rs	2.00
DIVD YIELD %	0.32
52 WK HI/LOW	175/32
NSE CODE	ACE
BSE CODE	ACE
MARKET CAP	RS 1824 CRS

SHAREHOLDING PATTERN

PROMOTERS	-	73%
BANKS, MFs & DIIs	-	1%
FIIs	-	1%
PUBLIC	-	25%

KEY FUNDAMENTALS

YE	FY21	FY22	FY23
Rev Gr%	1	20	22
EBIDTA Gr%	30	30	22
PAT Gr%	43	40	33
EPS Gr%	43	40	33
EPS (Rs)	6.61	9.25	12.33
ROE %	17	20	22
ROCE %	11 0	13	15
P/E(x)		17	12

Long term Drivers for DHFL look good in view of the follow18

ACE enjoys a very strong R & D base for its entire product range –

ACE has a dedicated R&D center in Faridabad, where it conducts proto activities along with designing with a focus on 3 main objectives. These include

Value engineering where ACE can provide something better to the customer at the same cost.

Secondly using trouble shooting as an essential & continuous feedback from customers and always using this as a medium for further product improvement and enhancement.

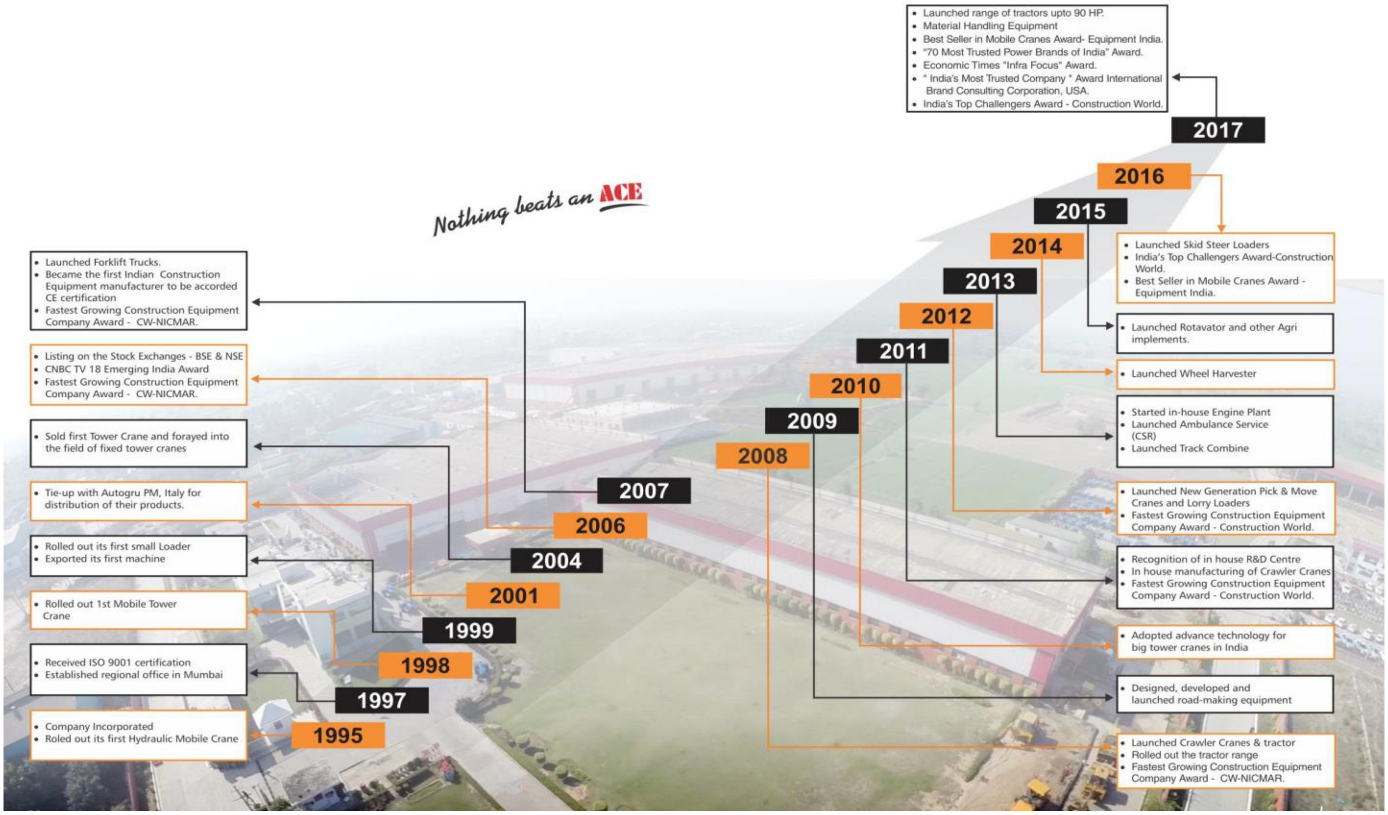
New product development which is the most critical component of ACE strategy which is the reason ACE has a wide range of equipment to suit needs of varied customers.

ACE's R&D team has also helped the company to meet and satisfy customer requirements as regards the output and performance of its products which is very important for the customer as they look out for the right specifications and right performance parameters

Based on these parameters the owning, operating cost, are determined and here the ACE management stands committed with respect to the output as compared to the owning cost or operation cost being equally good, if not better, than that most of its multinational peers.

This R & D based approach has enabled ACE to convert clients faster as Indian operating conditions and the usage tendency of the operators are much different than what is seen in other developed markets, and hence ACE strives to make its products more abuse-proof and designed to take extra load, extra work hours, and continuous duties, which is quite common in India.

ACE's Product Development Journey over the last 2 Decades –



Strong demand for mobile cranes continues (70% of FY21 sales) –

ACC has three key products in cranes: mobile/pick-and-carry cranes (55% of total sales), tower cranes (6%), and crawler cranes. According to the management mobile cranes demand will continue to be strong, aided by replacement demand. Here ACE is a market leader with a 65% market share where its capacity utilization is currently 75%

ACE is also a market leader in tower cranes with 60% share. The current capacity utilization is about 40%. While capacity utilisation in crawler cranes (25-70-tonne class) is around 20%. The management expects improvement in demand with a revival in the infra sector.

Growing Investments in infrastructure to boost sales going ahead –

ACE equipments are used in diverse segments like roads, ports, railways, mines, etc. With rapid development in economy, the government is allocating huge amount of budget towards infrastructure development.

As per the 12th Five year plan, the total investment of Rs 10,000 bn is expected to come in infrastructure segment due to which the construction equipment industry is expected to grow from to $5 bn by 2020 providing huge opportunity for ACE

Other BIG Infra Drivers for ACE will come from the following Govt initiatives like

Roads

Bharat Mala Phase-I – 35000 Kms
PMGSY (Pradhan mantri Gramin Sadak Yojna) – 57000 Kms.
Mumbai Trans harbour Link (MTHL)

Railways

Dedicated freight corridor
High Speed Rail Project (Ahmedabad – Mumbai)
Re-development of 600 Major Railway stations
3600 Kms. Of track removal

Airports

Increasing airport capacity by 5 times
Navi Mumbai Airport
50 locations for Reconstruction

Housing

PMAY (Pradhan Mantri Awas Yojna)
1.2 Crore houses by 2022
Sanctioning @ 3-5 Lacs houses per month

Ports
Sagar Mala – comprising of 400 projects

Metro Rail Delhi, Mumbai, Ahmadabad, Jaipur, Lucknow, Kolkatta & Bangalore

Urban : Infrastructure

City Roads, Bridges, Flyovers, Water, Sewage etc.

Already the increased focus of the government on developing infrastructure, railways, roads, etc, has translated into steady and strong demand for equipment across the infrastructure and construction value chain. As per the company's estimates, the Indian construction equipment industry is estimated to grow to $5 billion by FY25. While infrastructure spending is also expected to rise to 9% of GDP during the same timeline, upward of 7.2% was spent in FY20 indicating significant incremental addressable market demand for the near future.

ACE is perfectly poised to tap this huge growth ahead with underutilized manufacturing facilities across its three segments of cranes, material handling, construction equipment and agri equipment with utilisation levels currently at 50% across the board. With no further capital investment outlays envisaged by ACE incremental revenues are expected to translate to disproportionate bottomline growth for the company due to operating leverage at play. In addition, currently ACE also has adequate land area to expand its capacity further at a later stage going ahead.

ACE enjoys a Pan-India presence through a network of 83 sales and service locations, supported by 21 offices based at Delhi, Mumbai, Chennai, Kolkatta, Ahmedabad, Surat, Pune, Jaipur, Chandigarh, Ranchi, Raipur, Indore, Bhubaneshwar, Lucknow, Jamnagar, Hyderabad, Bangalore, Guwahati, Patna, Vizag & Kochi.

Going ahead the Construction Equipment segment holds big potential

ACE has an insignificant presence in construction equipment. Management expects highest growth in this segment over 3-4 years led by strong growth in road construction and improvement in market share due to leveraging its cranes-division sales network.

It indicated that its equipment prices are at a significant discount to its market leader, which provides a cushion for price hikes and improvement in margins. Currently, it is operating at 25 to 30% capacity

The current share of exports in the topline is at 6-7%. It is expected to grow to the 10-11% range in the next three years. A higher mix of export in revenue would assist ACE in beating the domestic cyclicality. Furthermore, we expect backhoe loader to play a pivotal role in achieving the targeted growth in CE segment

Agriculture equipment also is another big focus area for ACE going ahead –

ACCE has an insignificant presence in tractors, despite operating for 7-8 years. This is because of its limited presence (only in north India; Haryana, UP, Rajasthan) and challenges that it has faced in terms of its products.

Management highlighted that it has addressed these challenges and is now focusing on improving its market share by increasing its presence across India. ACE is also focusing on the exports markets, for which it has launched a 90HP product. Consequently, it sees strong growth in this segment (on a low base and on operating-leverage-led improvement in margins)

Growth drivers for the Agri Equipment Business

Higher MSP for key crops leading to higher income for farmers

Increasing rural wages makes alternative (tractors / agri-equipment) viable

Ease of credit availability enables farmers to buy tractors / agri-equipment

Mechanization helps in raising farm income by increasing productivity and limiting post-harvest losses

Also ACE is the third largest player in forklifts with 18% market share. Management expects this segment to be driven by strong demand due to increased logistics and warehousing activity

ACE is in a sweet spot as growth across all its product segments looks strong –

With the Infra and Agri sector expected to do well over the next 2-3 years we believe that most Infra and Agri equipment players across verticals like construction, infrastructure, material handling and Tractors are confident of a continued double digit growth. Also Tractor players are riding high on strong rural demand with tractor sales also expected to grow at a healthy pace in 2021 also.

ACE is looking becoming debt free by FY23–

ACE plans to become debt free by FY23 as it plans to use the cash flows generated to repay debts and keep a reasonable funds for meeting its working capital requirements

ACE enjoys a strong balance sheet with huge scalability potential going ahead –

ACE runs a strong business model covering multiple product segments across multi locations with a efficient working capital management while it continues to invest on a sustained basis largely from its internal accruals.

ACE has a total debt of Rs 74 crs as on FY20 and is expected to reduce this to Rs 30 crs by FY23 as compared to a tangible networth of Rs 478 crs as on FY21. We expect that going ahead overall bottomline growth in the next 3 years starting FY21 onwards should easily increase at a CAGR of 20-22% and with capex funded largely from internal cash flows. Hence going ahead we expect both the ROCE and ROE to improve to 15% and 22% by FY23

ACE last pursued capacity expansion in FY2011-12. With slowdown in the infra capex cycle; Cranes, CE and MH division plants have been running at sub-50% capacity utilization levels. Given the smaller base, and presence only in lower engine capacity tractors, the Agri-division (mainly led by tractors) has been operating at sub 50% capacity levels.

The Management has highlighted that it does not need to pursue any major capex atleast till another 2 years and with a revival on the cards, expected improvement in utilization levels, and with minimal requirement for incremental capital investments, we see ACE well positioned to scale its business quickly

Business Outlook & Stock Valuation –

On a rough cut basis, in FY21, Topline will see a steady rise wherein Topline is expected to touch Rs 1171 crs in FY19E which is expected to bounce back to Rs 1405 crs and Rs 1714 crs in FY22E and FY23E

On the bottomline level we expect the company to record a PAT of Rs 75 crs in FY21E. Thus on a conservative basis, ACE should record a EPS of Rs 6.61 for FY21E. For FY22E and FY23E our expectation is that earnings traction for ACE would continue to be strong wherein we expect a EPS of Rs 9.25 and Rs 12.33 respectively.

With the new government according top priority to the infrastructure sector, we believe the infrastructure sector is on the cusp of a turn-around. The government has already taken many steps (making funding easier for infrastructure sector, expediting approval process, debottlenecking the system, simplifying bureaucratic complexities, restoring confidence of the investors, etc) which will show visible improvement over next few quarters. ACE, being in the derived demand space, is ideally poised to benefit.

Also with ACE being practically debt free by FY23, we expect the ROE and ROCE to improve to around 22% and 15% by FY23. Looking at ACE's steady financial track record, strong product domain and dominant market share and strong promoters we expect the stock to get re rated in future.

ACE has already taken price hikes in November and January coupled with positive operating leverage should aid margins. In addition, the growth highlighted by the management will be achieved with an increase of less than 10% in fixed cost hence going ahead profitability is expected to improve significantly

Hence we believe that the ACE stock should be purchased at the current price for a price target of around Rs 240 over the next 12 to 18 months

FINANCIALS

For the Year Ended March RsCrs	FY19	FY20	FY21	FY22	FY23
Net Sales	1342.52	1156.23	1171.00	1405.20	1714.34
EBIDTA	97.77	91.55	119.28	154.57	188.58
EBIDTA %	7.28	7.92	10.19	11.00	11.00
Interest	11.52	14.65	13.00	10.00	5.00
Depreciation	11.75	13.01	13.94	16.00	18.00
Non Operational Other Income	9.70	4.15	10.00	10.00	12.00
Profit Before Tax	84.20	68.03	102.34	138.57	177.58
Profit After Tax	56.02	52.33	75.00	105.00	140.00
Diluted EPS (Rs)	4.78	4.61	6.61	9.25	12.33
Equity Capital	23.46	22.70	22.70	22.70	22.70
Reserves	389.91	388.96	455.96	551.96	681.96
Borrowings	44.00	74.12	80.00	40.00	30.00
GrossBlock	457.00	537.00	562.00	617.00	652.00
Investments	45.08	28.00	15.00	15.00	15.00

Source Company our Estimates

KEY CONCERNS

Any sharp rise in raw material costs can impact the Companys financials adversely.

Also slowdown due to covid and slow down in the economy could also impact the companys financials negatively

ACE business performance is highly sensitive to the economy and infrastructure outlook, which is cyclical in nature. A fall in the demand and / or prices would adversely impact the financial performance of the company

Agri business runs the risk of a demand drop in case of significant variation in monsoon

Disclaimer –