

Subdued tractor outlook to weigh...

About the stock: Escorts is India's fourth largest tractor maker (11.3% FY21 market share) and also serves the domestic construction equipment, railways space.

- FY21 sales mix – tractors 82%, construction equipment 11%, railways 7%
- Past five year CAGR: 44.9%, 59.8% in EBITDA, PAT; cash positive b/s

Q1FY22 Results: The company posted a relatively healthy Q1FY22 performance.

- Total operating income declined 24.4% QoQ to ₹ 1,672 crore
- Margins dipped 164 bps sequentially to 14%
- Consequent PAT was lower by 34.3% QoQ to ₹ 175 crore

What should investors do? The share price of Escorts has grown >4x over last five years from ~₹ 270 levels in August 2016, vastly outperforming Nifty Auto Index.

- We retain **HOLD** rating given muted outlook for core tractor business

Target Price and Valuation: We value Escorts at revised SOTP-based TP of ₹ 1,325 (15x P/E on core FY23E EPS, 30% discount on treasury shares; earlier TP ₹ 1,140).

Key triggers for future price performance:

- Expect 11% tractor revenue CAGR over FY21-23E (7.5% volume CAGR), constrained by high installed base despite favourable macro tailwinds
- Construction equipment (CE), railways (RED) growth to be faster amid expected pick-up in economic activity and positive outlook for mining, construction, road building and general infra push by government
- Limited potential for incremental operating leverage gains in tractors along with lower contribution from tractors to keep margin prospects muted
- Optimum utilisation of surplus cash on b/s could be a large value driver

Alternate Stock Idea: In our auto OEM coverage we like M&M.

- Focused on prudent capital allocation, UV differentiation & EV proactiveness
- BUY with a target price of ₹ 1,000



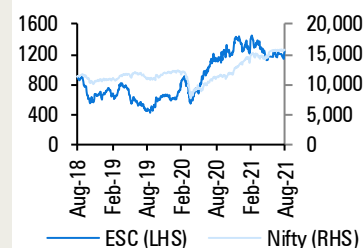
Particulars

Particular	₹ crore
Market Capitalization	15,016
Total Debt (FY21)	0
Cash & Investments (FY21)	2,968
EV	12,048
52 week H/L (₹)	1468 / 1078
Equity capital (₹crore)	122.6
Face value	₹ 10

Shareholding pattern

	Sep-20	Dec-20	Mar-21	Jun-21
Promoter	36.6	36.6	36.6	36.6
FII	21.6	23.8	26.0	21.3
DII	8.5	7.1	5.6	5.6
Other	33.3	32.5	31.9	36.5

Price Chart



Recent event & key risks

- Reported decent Q1FY22 results
- Key Risk:** (i) Earlier than expected market share gains, (ii) Inability to pass on commodity cost increase

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Key Financial Summary

Key Financials	FY19	FY20	FY21	5 year CAGR (FY16-21)	FY22E	FY23E	2 year CAGR (FY21-23E)
Net Sales	6,196.4	5,761.0	6,929.3	15.6%	7,949.9	8,926.3	13.5%
EBITDA	733.3	675.8	1,129.2	44.9%	1,035.7	1,205.1	3.3%
EBITDA Margins (%)	11.8	11.7	16.3		13.0	13.5	
Net Profit	484.9	485.6	873.3	59.8%	829.5	958.3	4.8%
EPS (₹)	39.6	39.6	71.2		67.7	78.2	
P/E	31.0	30.9	17.2		18.1	15.7	
RoNW (%)	15.6	14.2	16.2		13.6	13.8	
RoCE (%)	19.3	16.2	18.7		14.7	15.1	

Source: Company, ICICI Direct Research

Key takeaways of recent quarter & conference call highlights

Q1FY22 Results:

- Within segments, tractor revenues declined 18.8% QoQ to ₹ 1,411 crore (volumes down 20.4% to 25,935 units, ASPs up 2% to ₹ 5.44 lakh/unit)
- CE revenues declined 56.3% QoQ to ₹ 141 crore (volumes down 62% to 606 units) while RED revenues fell 18.5% QoQ to ₹ 119 crore. Present RED order book is at >₹ 300 crore
- Resilient margin performance was courtesy flattish gross margins on QoQ basis. Tractor EBIT margins declined 140 bps QoQ to 15.6% with capacity utilisation at ~90%

Q1FY22 Earnings Conference Call highlights

- The company maintained tractor industry growth outlook for FY22E at low to mid-single digit level. Macro factors (monsoon progress, crop production and procurement levels, etc) remain supportive but high installed base is viewed as a limiting factor for the industry
- CE industry growth in FY22E is expected in mid-teen territory while railways industry growth is expected in low double digit territory
- Escorts' tractor dealer count has increased to over 1,100. Total 60% of new dealers have been appointed in western and southern regions, where the company has a limited presence. It aims for ~15% overall market share in a few years vs. 11.3% as of FY21
- Cumulatively, raw material prices for tractors have risen by ~10-12% over the past year, of which the company has been able to recover ~7-8% via price hikes. It expects further ~200 bps QoQ cost increases in Q2FY22E, which would likely be passed on with a quarter's lag
- Frequent price hikes by tractor players is leading to delay in customer purchasing decisions/enquiry conversion. The same, however, is not thought to have meaningfully impacted volumes yet
- Average channel inventory level for tractor industry is at ~45-50 days, whereas the same for Escorts is placed at <30 days
- Spares, implements, etc, form ~8-10% of tractor division sales usually
- FY22E capex guidance stands at ₹ 300-325 crore

Peer comparison

Exhibit 1: ICICI Direct coverage universe (tractors)

Company	CMP	TP	Rating	Mcap	Total lakh volumes			EBITDA margin (%)			RoE (%)			RoCE (%)			P/E		
	₹	₹		₹ crore	FY21	FY22E	FY23E	FY21	FY22E	FY23E	FY21	FY22E	FY23E	FY21	FY22E	FY23E	FY21	FY22E	FY23E
Escorts (ESCORT)	1,225	1,325	Hold	15,016	1.1	1.2	1.2	16.3	13.0	13.5	16.2	13.6	13.8	18.7	14.7	15.1	17.2	18.1	15.7
M&M (MAHMAH)	759	1,000	Buy	94,377	3.5	3.8	4.0	14.4	11.8	13.0	2.7	9.6	11.1	9.5	8.2	10.5	330.1	25.4	20.1

Source: Company, ICICI Direct Research

Note – Volume data above is specific to tractor divisions for both companies

Exhibit 2: Variance Analysis

₹ crore	Q1FY22	Q4FY21E	Q1FY21	YoY (Chg %)	Q4FY21	QoQ (Chg %)	Comments
Total Operating Income	1,671.5	1,620.6	1,061.6	57.4	2,210.5	-24.4	Topline was ahead of estimates tracking beat on ASPs in the tractor as well as construction equipment space
Raw Material Expenses	1,027.7	1,045.3	641.1	60.3	1,391.4	-26.1	
Purchase of Traded Goods	113.4	103.7	71.7	58.1	122.8	-7.6	RM costs were contained at 68.3% of sales
Employee Expenses	137.1	124.8	126.2	8.7	147.0	-6.7	
Other Expenditure	160.1	162.1	103.1	55.3	204.7	-21.8	Other expenses for the quarter at 9.6% of sales
EBITDA	233.2	184.7	119.6	95.0	344.7	-32.4	
EBITDA Margin (%)	14.0	11.4	11.3	269 bps	15.6	-164 bps	EBITDA margins were ahead of estimates tracking better than anticipated gross margins
Interest	3.0	2.2	1.9	55.3	2.6	14.8	
Depreciation	31.4	32.4	26.4	18.8	30.4	3.0	Depreciation was on expected lines
Total Tax	60.9	47.9	28.9	110.6	80.3	-24.1	
PAT	174.8	145.0	90.7	92.6	266.1	-34.3	PAT was ahead of estimates tracking beat on margins
Key Metrics (₹ crore)							
Tractor Segment revenue	1,411	1,398	954	48.0	1,739	-18.8	Tractor segment revenues were marginally ahead of estimates with tractor ASPs for the quarter at ₹ 5.44 lakh/unit, up 2% QoQ
CE revenue	141	124	53	167.8	322	-56.3	
RED revenue	119	99	55	117.4	146	-18.5	Railway segment sales declined 18.5% QoQ

Source: Company, ICICI Direct Research

Exhibit 3: Change in estimates

₹ Crore)	FY22E			FY23E			Comments
	Old	New	% Change	Old	New	% Change	
Revenue	7,735.1	7,949.9	2.8	8,671.6	8,926.3	2.9	Broadly maintained revenue estimates. We expect sales to grow at a CAGR of 13.5% over FY21-23E
EBITDA	965.1	1,035.7	7.3	1,173.0	1,205.1	2.7	
EBITDA Margin (%)	12.5	13.0	50 bps	13.5	13.5	0 bps	Upgraded margin estimates for FY22E tracking robust performance in Q1FY22. Maintained FY23E estimates
PAT	760.4	829.5	9.1	942.8	958.3	1.6	
EPS (₹)	62.0	67.7	9.1	76.9	78.2	1.6	We expect PAT at the company to grow at a CAGR of 4.8% over FY21-23E, albeit on a high base

Source: ICICI Direct Research

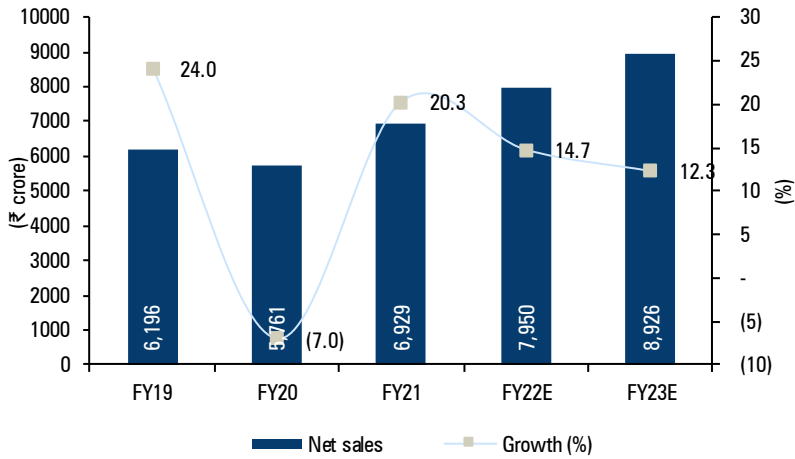
Exhibit 4: Assumptions

	Current				Earlier				Comments
	FY18	FY19	FY20	FY21	FY22E	FY23E	FY22E	FY23E	
Tractor volumes (units)	80,417	96,412	86,018	106,741	115,259	123,327	113,141	121,061	Marginally upgraded our estimates. We expect tractor sales volume to grow at a CAGR of 7.5% over FY21-23E
Average ASP (₹)	492,166	492,053	515,890	530,937	551,791	566,538	554,708	569,422	Broadly maintained ASP's estimates

Source: ICICI Direct Research

Financial story in charts

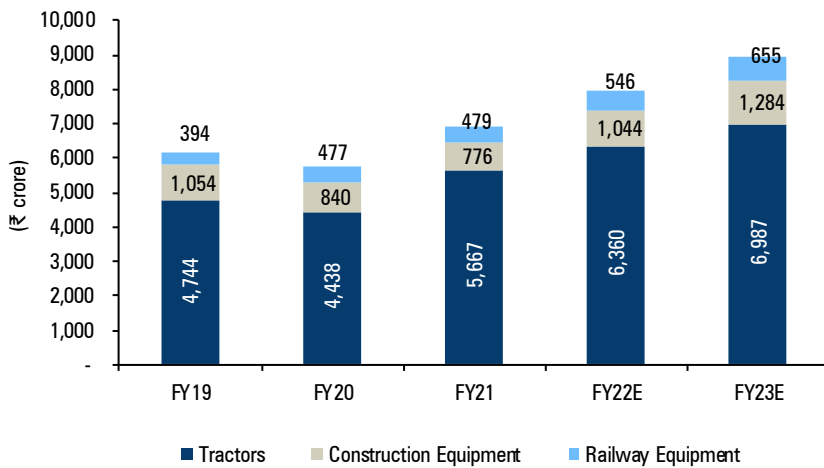
Exhibit 5: Trend in total operating income



We expect net sales to grow at 13.5% CAGR over FY21-23E

Source: Company, ICICI Direct Research

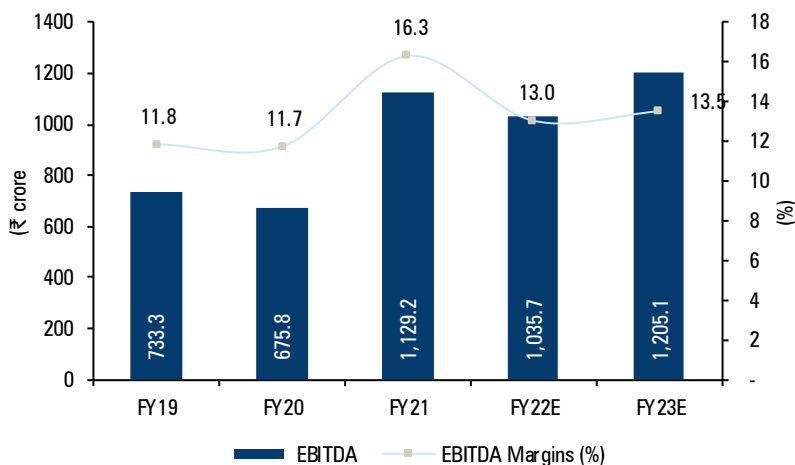
Exhibit 6: Trend in segment mix



Share of tractors within overall revenue mix is seen declining over the medium term amid muted 7.5% volume CAGR expectation. From a lower base, share of CE and RED is set to increase

Source: Company, ICICI Direct Research

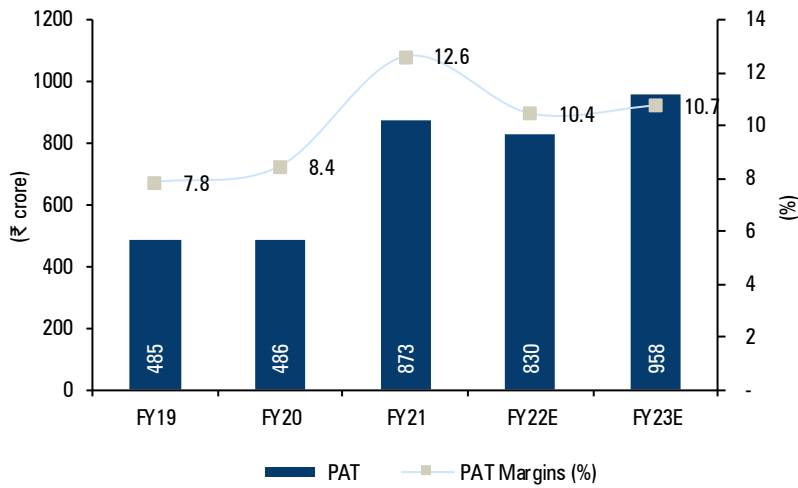
Exhibit 7: Trend in margins



Margins are seen declining to 13.5% by FY23E due to limited scope for further operating leverage gains and lower contribution from tractor segment, going forward

Source: Company, ICICI Direct Research

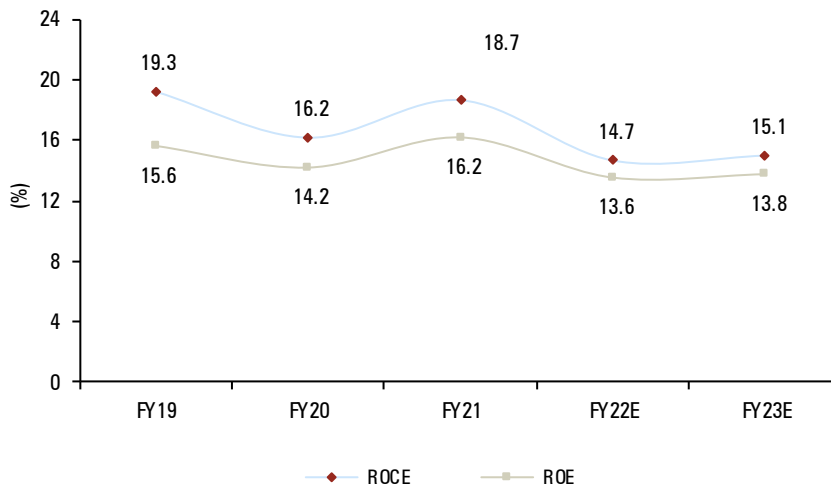
Exhibit 8: Trend in profitability



PAT is expected to grow at subdued 4.8% CAGR over FY21-23E

Source: Company, ICICI Direct Research

Exhibit 9: Trend in return ratios



Return ratios are seen stabilising around 14-15% mark by FY23E

Source: Company, ICICI Direct Research

Exhibit 10: Valuation summary

	Sales (₹ cr)	Growth (%)	EPS (₹)	Growth (%)	PE (x)	EV/EBITDA (x)	RoNW (%)	RoCE (%)
FY18	4995	22.0	28.1	114.9	43.6	25.6	13.8	18.7
FY19	6196	24.0	39.6	40.6	31.0	20.0	15.6	19.3
FY20	5761	-7.0	39.6	0.1	30.9	20.8	14.2	16.2
FY21	6929	20.3	71.2	79.9	17.2	10.7	16.2	18.7
FY22E	7950	14.7	67.7	-5.0	18.1	11.4	13.6	14.7
FY22E	8926	12.3	78.2	15.5	15.7	9.3	13.8	15.1

Source: Company, ICICI Direct Research

Financial Summary

Exhibit 11: Profit and loss statement					₹ crore
(Year-end March)	FY20	FY21	FY22E	FY23E	
Total operating Income	5,761.0	6,929.3	7,949.9	8,926.3	
Growth (%)	-7.0	20.3	14.7	12.3	
Raw Material Expenses	3,449.3	4,153.6	5,045.9	5,656.0	
Employee Expenses	510.3	534.6	570.7	602.0	
Other expenses	755.2	671.8	776.1	883.0	
Total Operating Expenditure	5,085.1	5,800.1	6,914.3	7,721.3	
EBITDA	675.8	1129.2	1035.7	1205.1	
Growth (%)	-7.8	67.1	-8.3	16.4	
Depreciation	104.6	115.7	130.5	154.3	
Interest	15.5	11.0	8.8	7.0	
Other Income	92.3	154.6	188.9	188.8	
PBT	638.9	1,157.1	1,085.3	1,232.5	
Total Tax	153.3	283.1	272.4	310.6	
Tax rate	24.0	24.5	25.1	25.2	
PAT	485.6	873.3	829.5	958.3	
Growth (%)	0.1	79.9	-5.0	15.5	
EPS (₹)	39.6	71.2	67.7	78.2	

Source: Company, ICICI Direct Research

Exhibit 12: Cash flow statement					₹ crore
(Year-end March)	FY20	FY21	FY22E	FY23E	
Profit after Tax	485.6	873.3	829.5	958.3	
Add: Depreciation	104.6	115.7	130.5	154.3	
(Inc)/dec in Current Assets	190.7	269.3	-448.7	-243.8	
Inc/(dec) in CL and Provisions	112.4	-55.7	185.6	215.7	
CF from operating activities	893.1	1202.7	696.9	1084.5	
(Inc)/dec in Investments	-247.2	-1,013.3	-200.0	-500.0	
(Inc)/dec in Fixed Assets	-210.4	-103.5	-310.0	-341.8	
Others	-39.9	-119.2	-33.5	-62.4	
CF from investing activities	-497.5	-1235.9	-543.5	-904.2	
Issue/(Buy back) of Equity	0.0	12.2	-12.2	0.0	
Inc/(dec) in loan funds	-280.1	-6.6	0.0	0.0	
Dividend paid & dividend tax	-36.8	-91.9	-91.9	-122.6	
Inc/(dec) in Sec. premium	0.0	1,029.8	0.0	0.0	
Others	8.4	88.1	0.0	0.0	
CF from financing activities	-308.5	1031.6	-104.2	-122.6	
Net Cash flow	87.1	998.3	49.3	57.7	
Opening Cash	231.1	318.3	1,316.6	1,365.9	
Closing Cash	318.3	1316.6	1365.9	1423.6	

Source: Company, ICICI Direct Research

Exhibit 13: Balance Sheet					₹ crore
(Year-end March)	FY20	FY21	FY22E	FY23E	
Liabilities					
Equity Capital	122.6	134.8	122.6	122.6	
Reserve and Surplus	3,357.5	5,256.8	5,994.4	6,830.1	
Total Shareholders funds	3480.1	5391.6	6117.0	6952.7	
Total Debt	6.6	0.0	0.0	0.0	
Other non-current Liabilities	83.7	106.7	109.2	111.7	
Long-term Provisions	30.1	49.0	67.8	86.6	
Total Liabilities	3600.5	5547.3	6293.9	7150.9	
Assets					
Gross Block	2,645.8	2,794.5	3,124.5	3,454.5	
Less: Acc Depreciation	1,012.7	1,109.6	1,220.8	1,351.9	
Net Block	1,633.0	1,684.9	1,903.6	2,102.6	
Capital WIP	104.4	41.2	16.2	16.2	
Total Fixed Assets	1737.4	1726.0	1919.8	2118.8	
Net Intangible Asset	52.3	51.5	37.1	25.6	
Investments	1,172.8	2,322.8	2,572.8	3,122.8	
Inventory	822.2	674.5	871.2	978.2	
Debtors	756.5	698.4	871.2	978.2	
Loans and Advances	37.7	32.8	48.0	42.7	
Other Current Assets	265.8	189.4	253.3	288.4	
Cash	318.3	1316.6	1365.9	1423.6	
Total Current Assets	2,200.4	2,911.6	3,409.6	3,711.2	
Creditors	1,264.0	1,187.1	1,306.8	1,467.3	
Provisions & Other Curr.Liab	447.7	468.9	534.8	589.9	
Total Current Liabilities	1,711.7	1,656.0	1,841.6	2,057.3	
Net Current Assets	488.7	1255.6	1568.0	1653.9	
Net Deferred Tax Asset	-30.3	-23.0	-23.0	-23.0	
Other non-current assets	119.0	154.5	159.3	193.0	
Application of Funds	3600.5	5547.3	6293.9	7150.9	

Source: Company, ICICI Direct Research

Exhibit 14: Key ratios				
(Year-end March)	FY20	FY21	FY22E	FY23E
Per share data (₹)				
EPS	39.6	71.2	67.7	78.2
Cash EPS	48.1	80.7	78.3	90.8
BV	283.9	439.8	499.0	567.2
DPS	2.5	7.5	7.5	10.0
Cash Per Share	78.0	242.1	262.5	308.0
Operating Ratios				
EBITDA Margin (%)	11.7	16.3	13.0	13.5
PAT Margin (%)	8.4	12.6	10.4	10.7
Inventory days	52.1	35.5	40.0	40.0
Debtor days	47.9	36.8	40.0	40.0
Creditor days	80.1	62.5	60.0	60.0
Return Ratios (%)				
RoE	14.2	16.2	13.6	13.8
RoCE	16.2	18.7	14.7	15.1
RoIC	23.3	42.1	31.1	33.0
Valuation Ratios (x)				
P/E	30.9	17.2	18.1	15.7
EV / EBITDA	20.8	10.7	11.4	9.3
EV / Net Sales	2.4	1.7	1.5	1.3
Market Cap / Sales	2.6	2.2	1.9	1.7
Price to Book Value	4.3	2.8	2.5	2.2
Solvency Ratios				
Debt/ EBITDA	0.0	0.0	0.0	0.0
Debt / Equity	0.0	0.0	0.0	0.0
Current Ratio	1.4	1.2	1.4	1.4
Quick Ratio	0.8	0.7	0.8	0.8

Source: Company, ICICI Direct Research

Exhibit 15: ICICI Direct coverage universe (Auto & Auto Ancillary)

Sector / Company	CMP	TP	Rating	M Cap	EPS (₹)			P/E (x)			EV/EBITDA (x)			RoCE (%)			RoE (%)		
	(₹)	(₹)		(₹ Cr)	FY21P	FY22E	FY23E	FY21P	FY22E	FY23E	FY21P	FY22E	FY23E	FY21P	FY22E	FY23E	FY21P	FY22E	FY23E
Apollo Tyre (APOTYR)	222	275	Buy	14,098	5.5	10.2	16.6	40.3	21.7	13.4	6.7	6.9	5.0	7.6	6.1	9.1	6.4	5.5	8.4
Ashok Leyland (ASHLEY)	134	150	Buy	39,223	-1.1	1.1	4.4	-125.4	121.6	30.5	78.8	32.1	15.8	-1.9	4.8	15.7	-4.4	4.5	16.5
Bajaj Auto (BAAUTO)	3,819	4,350	Hold	1,10,496	157.4	167.7	193.6	24.3	22.8	19.7	18.0	16.7	14.1	18.2	19.3	22.5	18.1	18.9	21.4
Balkrishna Ind. (BALIND)	2,497	2,250	Buy	48,271	59.8	68.2	80.5	41.8	36.6	31.0	27.3	23.5	19.9	19.3	20.4	21.6	19.2	19.0	19.4
Bharat Forge (BHAFOR)	778	875	Buy	36,221	-2.7	15.9	25.0	NM	49.1	31.1	44.7	24.0	17.1	2.2	8.0	12.1	3.3	12.3	16.9
Eicher Motors (EICMOT)	2,732	2,970	Hold	74,474	49.3	66.7	87.4	55.4	41.0	31.3	37.5	28.8	21.9	11.3	13.5	15.8	11.8	14.3	16.6
Escorts (ESCORT)	1,225	1,325	Hold	15,016	71.2	67.7	78.2	17.2	18.1	15.7	10.7	11.4	9.3	18.7	14.7	15.1	16.2	13.6	13.8
Hero Moto (HERHON)	2,820	3,440	Buy	56,315	148.4	170.8	196.5	19.0	16.5	14.4	12.0	10.2	8.7	20.8	23.1	24.5	19.5	20.7	21.7
M&M (MAHMAH)	760	1,000	Buy	94,483	2.3	29.9	37.8	337.6	25.4	20.1	14.0	14.8	11.8	9.5	8.2	10.5	2.7	9.6	11.1
Maruti Suzuki (MARUTI)	7,025	6,400	Reduce	2,12,211	140.0	153.1	228.5	50.2	45.9	30.7	31.6	26.4	18.0	4.3	5.9	9.5	8.2	8.5	11.7
Minda Industries (MININD)	735	725	Buy	19,985	7.6	10.9	19.1	96.7	67.5	38.4	28.7	24.0	17.0	9.1	10.6	16.7	10.4	14.2	19.6
Motherson (MOTSUM)	237	300	Buy	74,843	3.3	7.4	10.0	NM	31.9	23.7	16.5	10.0	8.0	6.7	16.2	20.5	8.8	16.7	19.7
Tata Motors (TATMOT)	300	375	Buy	1,14,870	-35.0	0.9	37.9	NM	348.4	7.9	5.2	5.0	3.2	6.3	7.9	14.8	-23.6	0.6	20.3

Source: Company, ICICI Direct Research

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Buy: >15%

Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



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