

November 03, 2023

RESULT REPORT Q2 FY24 | Sector: Automobile

Escorts Kubota Ltd

On a steady footing!

Valuation and View – New product launches in tractors to help MS

Escorts Kubota (EKL) 2QFY24 results were weak (EBITDA miss of ~13%) to our while in-line to street estimates. The key positives were, 1) better than expected gross margins at 32.3% (est 30.7%, +470bp YoY/ +210bp QoQ), 2) favorable mix in railway business (led by spares and exports) led to EBIT margins at 18.9% (+380bp YoY) and 3) CE business EBIT margins at 10.2% (highest, +12.8% YoY). The management indicated sustenance of margins (assuming stable RM and price hike of ~1.7% in 1HFY24) have further headroom for margins expansion. We think this would not be tough but challenging given low-mid single digit volume growth expected in FES and stabilizing product mix benefit in railway segment. However, we remain constructive on growth opportunities for merged entity in tractor, implements, components sourcing and exports.

We believe, EKL is more vulnerable v/s peers as i) it derives >70% of its revenues from FES segment and ii) aggressive expansion plans by Sonalika, TAFE, John Deere, etc. to keep tight balance between market share and margins priorities. The valuations at 26.9x/22.6x FY24/25 EPS do reflect upon positive synergies post Kubota integration. We believe, benefits arising out of Kubota JV to start reflecting meaningfully from FY25E. We raise FY24/25 EPS by 3-6% to factor in sharper than expected RM decline. We maintain Neutral on the stock with revised TP of Rs2,995 (earlier Rs2,897). We value co at 22x Mar-25 EPS (vs 10year LPA of 14.5x) and build in revenue/EBITDA/PAT CAGR of 9%/45%/40.5% over FY23-25E.

Result Highlights – Healthy growth in CE/railways helped earnings

- Revenues grew 8.6% YoY (-12.1% QoQ) at Rs20.5b (est Rs21.5b, cons Rs20.8b) as Agri/railways/construction equip (CE) revenues grew -4.2%/+28.8%/+71.9% YoY. Agri ASP grew ~3% YoY (+1% QoQ) at Rs633k/unit (est Rs639.6k/unit).
- Gross margins came in better at 32.3% (+470bp YoY/ +210bp QoQ, est 30.7%). However, this was offset by higher staff cost at Rs1.67b (est Rs1.42b, +12.8% QoQ) and other expense at Rs2.3b (+1.6% QoQ, est Rs2.1b) led to miss on EBITDA margins at 12.9% (+480bp YoY/ -110bp QoQ, est ~14%, cons 12.8%) with EBITDA at Rs2.6b (est Rs3b, cons Rs2.67b, +72.4% YoY/ -19.5% QoQ).
- Segmental EBIT margins – Agri at 12.2% (-120bp QoQ), Railway at 18.9% (-240bp QoQ), CE at 10.2% (+260bp QoQ).
- Led by weak operating performance, Adj.PAT declined ~17% QoQ (+66% YoY) at Rs2.3b (est Rs2.6b, cons Rs2.3b).
- 1HFY24 performance – Revenue/EBITDA/Adj.PAT grew 12%/66%/79%.

Exhibit 1: Actual vs estimates

Rs mn	Actual	Estimate		% variation		Remarks
		Yes Sec	Consensus	Yes Sec	Consensus	
Sales	20,462	21,452	20,853	-4.6	-1.9	EKL's results missed our estimates while in-line to street.
EBITDA	2,633	3,021	2,672	-12.9	-1.5	
EBITDA margins %	12.9	14.1	12.8	-120bp	10bp	
Adjusted PAT	2,347	2,679	2,289	-12.4	2.5	

Source: Company, YES Sec

Reco	: NEUTRAL
CMP	: Rs 3,076
Target Price	: Rs 2,995
Potential Return	: -2.6%

Stock data (as on Nov 02, 2023)

Nifty	19,230
52 Week h/l (Rs)	3440 / 1808
Market cap (Rs/USD mn)	331461 / 3987
Outstanding Shares (mn)	108
6m Avg t/o (Rs mn):	925
Div yield (%):	0.2
Bloomberg code:	ESCORTS IN
NSE code:	ESCORTS

Stock performance



	1M	3M	1Y
Absolute return	(4.1%)	17.6%	52.2%

Shareholding pattern (As of Sep'23)

Promoter	67.7%
FII+DII	16.0%
Others	14.4%

Δ in stance

(1-Yr)	New	Old
Rating	NEUTRAL	NEUTRAL
Target Price	2,995	2,897

Δ in earnings estimates

	FY24E	FY25E
EPS (New)	114.2	136.1
EPS (Old)	107.4	131.7
% change	+6.3%	+3.4%

Financial Summary

Y/E Mar (Rs b)	2023	2024E	2025E
Sales	84.3	94.0	100.0
EBITDA	7.8	13.4	16.3
Adj. PAT	6.8	11.2	13.4
EPS (INR)	68.9	114.2	136.1
EPS Gr. (%)	(7.9)	65.6	19.3
BV/Sh. (INR)	833.3	938.1	1,064.8
RoE (%)	8.6	12.9	13.6
RoCE (%)	11.5	17.4	18.3
Payout (%)	14.5	8.2	6.9
P/E (x)	44.6	26.9	22.6
P/BV (x)	3.7	3.3	2.9
EV/EBITDA (x)	47.9	27.3	21.9
EV/Sales (x)	4.4	3.9	3.6

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Exhibit 2: Quarterly snapshot

Y/e Mar (Rs. mn)	Q2FY24	Q2FY23	YoY chg (%)	Q1FY24	H1FY24	H1FY23	YoY chg (%)
Net Revenues	20,462	18,835	8.6	23,277	43,739	38,983	12.2
Raw Materials	13,846	13,638	1.5	16,252	30,098	28,184	6.8
% of Net Sales	67.7%	72.4%		69.8%	68.8%	72.3%	
Personnel	1,675	1,489	12.5	1,484	3,159	2,858	10.5
% of Net Sales	8.2%	7.9%		6.4%	7.2%	7.3%	
Manufacturing & Other Exp	2,309	2,182	5.8	2,272	4,581	4,399	4.1
% of Net Sales	11.3%	11.6%		9.8%	10.5%	11.3%	
Total Expenditure	17,829	17,308	3.0	20,008	37,837	35,441	6.8
EBITDA	2,633	1,527	72.4	3,269	5,902	3,543	66.6
EBITDA Margin (%)	12.9%	8.1%		14.0%	13.5%	9.1%	
Depreciation	410	365	12.3	402	811	729	11.4
EBIT	2,223	1,162	91.3	2,868	5,091	2,814	80.9
Interest Expenses	24	23	3.1	27	50	49	2.9
Non-operating income	950	776	22.5	945	1,895	1,130	67.7
Extraordinary Expenses	-	726.70		-	0	727	
PBT	3,150	1,188	165.1	3,786	6,936	3,169	118.9
Tax-Total	802	310	158.4	958	1,760	817	115.5
Tax Rate (%) – Total	25.5%	26.1%		25.3%	25.4%	25.8%	
Reported PAT	2,347	878	167.5	2,828	5,175	2,352	120.0
Adj. PAT	2,347	1,414	66.0	2,828	5,175	2,889	79.2
PAT Margin	11.5%	7.5%		12.1%	11.8%	7.4%	

Source- Company, Yes Sec

KEY CON-CALL HIGHLIGHTS

Agriculture (FES) segment -

- **Outlook - Expect tractor industry growth of plus minus 2% in FY24E.** Navratri festive retails were good but dipped at the fag end of the season. Believe Nov'23 to be positive, Dec flat (hence expect 3QFY24 growth to be ~2% YoY) and 4Q would be marginal positive (led by moderate base and general elections, stock building ahead of Navratri in April).
 - **Region wise** South and East have declined for festive, west mixed bag (MH declined while Guj grew) and Central/North markets have grown (while UP is flattish).
 - **Non-agriculture usage contribution is ~30-35% of overall sales (flat YoY).**
 - In 2QFY24, domestic tractor industry declined 5.8% YoY (-19.9% QoQ) to ~210k units with MS at 9.8% (9.6%). Agri capacity utilization at 85% in 2QFY24.
 - **Current inventory is ~4.5-5 weeks** at dealership level which is expected to come down to ~4 weeks by end of Nov'23.
 - **To set-up captive finance arm which should help market share gains.** This will be for KEL's tractor, farm implements and construction equipment segment.
 - **Expect new product launches** for both Farmtrac (targeting emerging applications in >50HP segment) and Powertrac with change in look and feel as well as features.
 - **Farm implements** – JV with Kubota will help scale this segment as it has strong presence in Harvester and transplanter applications. Kubota (sales co) current revenue is ~Rs3b v/s EKL's of Rs500-600m. Overall target is to reach ~Rs10b revenues.
 - **TREM 5 regulations cost impact would be ~Rs125k** for <50HP segment as it would leap-frog directly to TREM 3 to TREM 5. However, the same is expected to be delayed by ~18 months for implementation.
- **Exports** – EKL's exports at 1,551 declined YoY by 32.8% while grew QoQ by 14.4%. Exports sales through Kubota channel contributed 31% (v/s ~32% in 1Q).
 - **Outlook** - Markets in Europe due to macro challenges leading to decline in volumes. Also, there was some issue on production side (beginning of FY24). Expect FY24 volumes to be 15-20% lower YoY, FY25E to see 25-30% growth YoY. Expect significant growth from FY26E.
 - **Entry in to markets like US is delayed due to product requirements.** Expect US to be bigger market as part of MTBP and expect FY26E volumes to US shall improve.
- **Domestic tractor volume mix –**
 - Farmtrac/Powertrac at 44/56 (v/s 44/56 QoQ and 42/58 YoY).
 - <40HP/>40HP – 39/61 (flat YoY).
- **Channel expansion** – total dealer counts as of Sep'23 at 1,230 (v/s Jun'23 1,240+ and 1,200+ in 4QFY23). Will continue network expansion in opportunity markets.
- **Price hikes** - Had taken cumulative price hike of ~1.7% in 1HFY24 (~1% in 1Q and 0.7% in 2Q).
- **Amalgamation with Kubota Agri** – Expect order from NCLT to come through by 4QFY24.
- **Overall Capex** – FY24E to be Rs2-2.5b (actual cash outflow basis).

Construction equipment - Served industry volumes grew ~37.4% YoY (+14.8% QoQ) at 16.3k

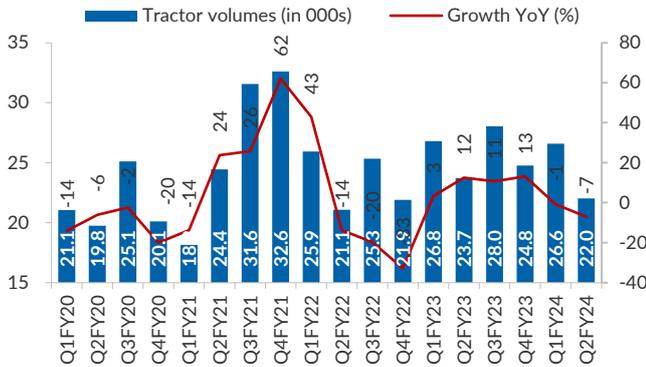
- **Outlook** – expect current growth momentum to continue in rest of FY24E.
- In 2QFY24, BHL Industry up by 27.8% Y-o-Y, PnC Industry up by 73.2% Y-o-Y, Compactors Industry grew by 63.5% Y-o-Y. EKL's CE volume grew 72% YoY (+14.9% QoQ) at 1,577 units.
- Construction equipment capacity utilization at 65% in 2QFY24.
- **Regulatory price hike indicative impact** - BS 3 BS 5 price hike impact at customer level at 8-9% and for products which will move from BS4 to BS 5 will be 4-4.5%.

Railways

- **Outlook** – Expect revenues to grow double digit as new product launches continue (like for Vande Bharat).
- **Margins outlook** – Current margins are backed by better product mix, higher spares sales and soft RM. Expect to maintain current level margins plus minus 100b-200bp.
- **New product development** - Have successfully completed field trials EMCVS. Share of new products to revenues would be >60% (v/s 70% in 1QFY24).
- **Order book** at Rs8.7b as of 2QFY24 (v/s Rs9.5b in 1QFY24, Rs10.5b in 4QFY23). The decline in OB is led by higher execution (leading to decline in outstanding orders). The pace of orders are normalizing to pre-covid levels.

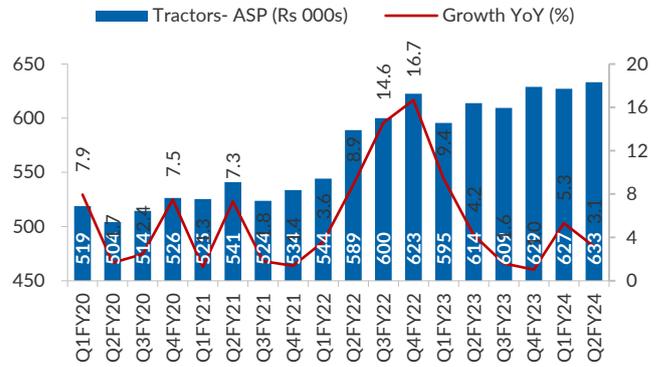
CHARTS

Exhibit 1: 2QFY24 tractor volume fell ~7% YoY



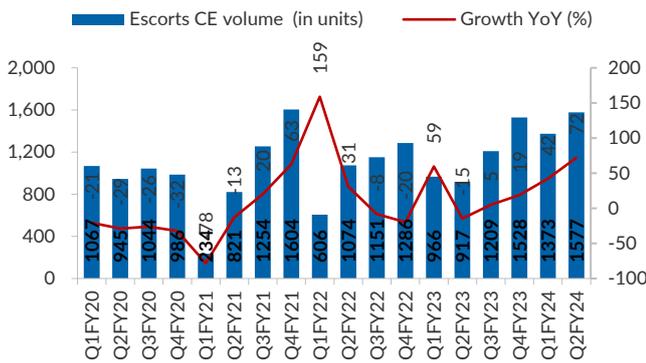
Source: Company, YES Sec

Exhibit 2: ...while ASPs grew ~3% YoY led by price hikes



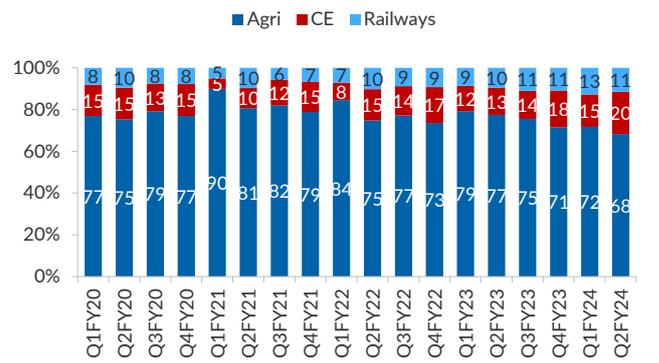
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Exhibit 3: CE volumes grew 72% YoY/ 15% QoQ



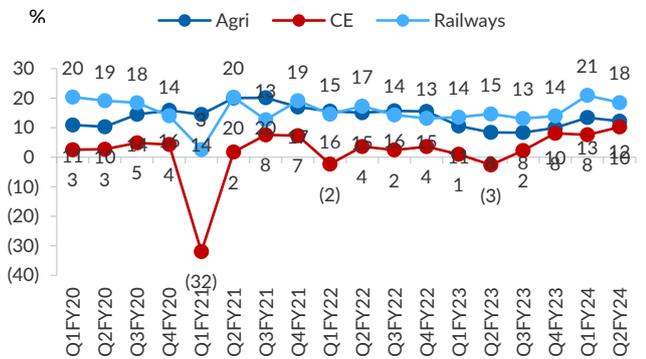
Source: Company, YES Sec

Exhibit 4: Segment wise revenue share trend



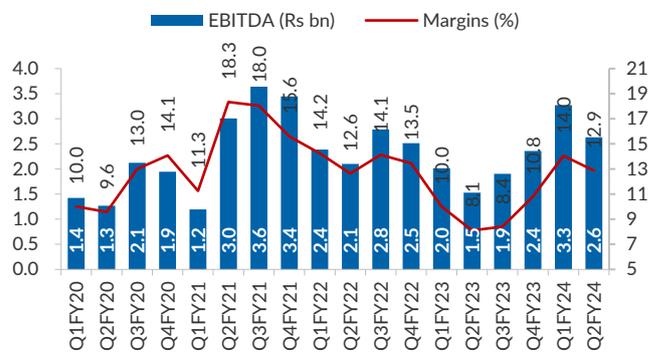
Source: Company, YES Sec

Exhibit 5: Trend in segmental margins



Source: Company, YES Sec

Exhibit 6: EBITDA margin contracted ~110bp QoQ



Source: Company, YES Sec

FINANCIALS

Exhibit 7: Balance Sheet

Y/E March (Rs mn)	FY20	FY21	FY22	FY23	FY24E	FY25E
Equity Share Capital	1,226	1,348	1,319	1,319	1,319	1,319
Total Reserves	29,948	48,913	74,680	80,548	90,837	103,283
Net Worth	31,174	50,261	75,999	81,867	92,157	104,602
Minority Interest	51	(9)	(38)	(39)	(39)	(39)
Deferred Liabilities	307	233	373	646	646	826
Total Loans	192	25	-	-	-	-
Capital Employed	31,724	50,511	76,334	82,475	92,764	105,389
Gross Block	28,253	28,652	29,973	31,687	33,520	35,481
Less: Accum. Deprn.	11,026	11,388	12,389	13,573	15,203	16,928
Net Fixed Assets	17,227	17,264	17,585	18,114	18,316	18,553
Capital WIP	1,044	647	878	1,137	1,222	1,300
Total Investments	7,974	20,079	49,184	48,465	50,888	53,433
Curr. Assets, Loans&Adv.	23,678	30,792	23,431	33,135	40,962	51,926
Inventory	8,834	7,182	8,466	12,177	11,708	12,100
Account Receivables	7,319	6,576	7,926	11,797	13,645	13,702
Cash and Bank Balance	3,249	13,218	2,718	4,719	10,279	19,728
Loans and Advances	4,277	3,817	4,320	4,442	5,331	6,397
Curr. Liability & Prov.	18,211	18,271	14,743	18,375	18,624	19,823
Account Payables	16,648	16,763	13,341	16,912	16,992	18,086
Provisions	1,563	1,508	1,402	1,463	1,632	1,737
Net Current Assets	5,467	12,521	8,687	14,760	22,338	32,103
Deferred Tax assets	12	-	-	-	-	-
Misc Expenditure	-	-	-	-	-	-
Appl. of Funds	31,724	50,511	76,334	82,475	92,764	105,389

Source: Company, YES Sec

Exhibit 8: Income statement

Y/E March (Rs mn)	FY20	FY21	FY22	FY23	FY24E	FY25E
Total Income from Operations	58,101	70,144	72,827	84,287	93,972	100,023
Change (%)	(7.2)	20.7	3.8	15.7	11.5	6
Total Expenditure	51,477	58,877	62,872	76,512	80,534	83,719
% of Sales	88.6	83.9	86.3	90.8	85.7	83.7
EBITDA	6,624	11,268	9,954	7,775	13,438	16,304
Margin (%)	11.4	16.1	13.7	9.2	14.3	16.3
Depreciation	1,072	1,183	1,321	1,501	1,630	1,725
EBIT	5,552	10,085	8,634	6,275	11,808	14,579
Int. and Finance Charges	172	133	150	133	126	120
Other Income	976	1,604	1,738	2,809	3,371	3,472
PBT bef. EO Exp.	6,356	11,555	10,222	8,951	15,053	17,931
EO Items	(92)	-	-	(531)	-	-
PBT after EO Exp.	6,263	11,555	10,222	8,421	15,053	17,931
Current Tax	1,535	2,832	2,572	1,979	3,763	4,302
Deferred Tax	-	-	-	-	-	179
Tax Rate (%)	24.5	24.5	25.2	23.5	25.0	25.0
Less: Mionrity Interest	11	7	294	75	75	75
Reported PAT	4,717	8,716	7,356	6,367	11,215	13,375
Adjusted PAT	4,787	8,716	7,356	6,772	11,215	13,375
Change (%)	1.2	82.1	(15.6)	(7.9)	65.6	19.3
Margin (%)	8.2	12.4	10.1	8.0	11.9	13.4

Source: Company, YES Sec

Exhibit 9: Cash Flow Statement

Y/E March (Rs mn)	FY20	FY21	FY22	FY23	FY24E	FY25E
OP/(Loss) before Tax	6,253	11,548	9,928	8,346	15,051	17,925
Depreciation	1,072	1,183	1,321	1,501	1,630	1,725
Interest & Finance Charges	300	699	790	1,513	126	120
Direct Taxes Paid	(1,748)	(2,527)	(2,547)	(1,864)	(3,763)	(4,302)
(Inc)/Dec in WC	3,272	2,722	(6,526)	(4,102)	(2,019)	(316)
CF from Operations	9,148	13,625	2,966	5,393	11,025	15,152
Others	(1,177)	(2,338)	(2,644)	(3,154)	-	0
CF from Operating incl EO	7,971	11,287	323	2,239	11,025	15,152
(inc)/dec in FA	(1,902)	(1,182)	(1,759)	(2,132)	(1,918)	(2,040)
Free Cash Flow	6,070	10,105	(1,436)	107	9,107	13,112
(Pur)/Sale of Investments	(2,699)	(10,568)	(28,434)	6,702	-	0
Others	388	(10,160)	11,625	(5,187)	(2,423)	(2,544)
CF from Investments	(4,212)	(21,910)	(18,567)	(618)	(4,341)	(4,584)
Issue of Shares	-	10,576	19,021	206	-	0
Inc/(Dec) in Debt	(82)	(60)	(78)	(71)	-	0
Interest Paid	(100)	(76)	(98)	(91)	(126)	(120)
Dividend Paid	(260)	(245)	(737)	(757)	(924)	(924)
Others	(2,563)	(161)	(8)	-	(75)	(75)
CF from Fin. Activity	(3,005)	10,033	18,099	(712)	(1,124)	(1,118)
Inc/Dec of Cash	754	(590)	(145)	909	5,560	9,449

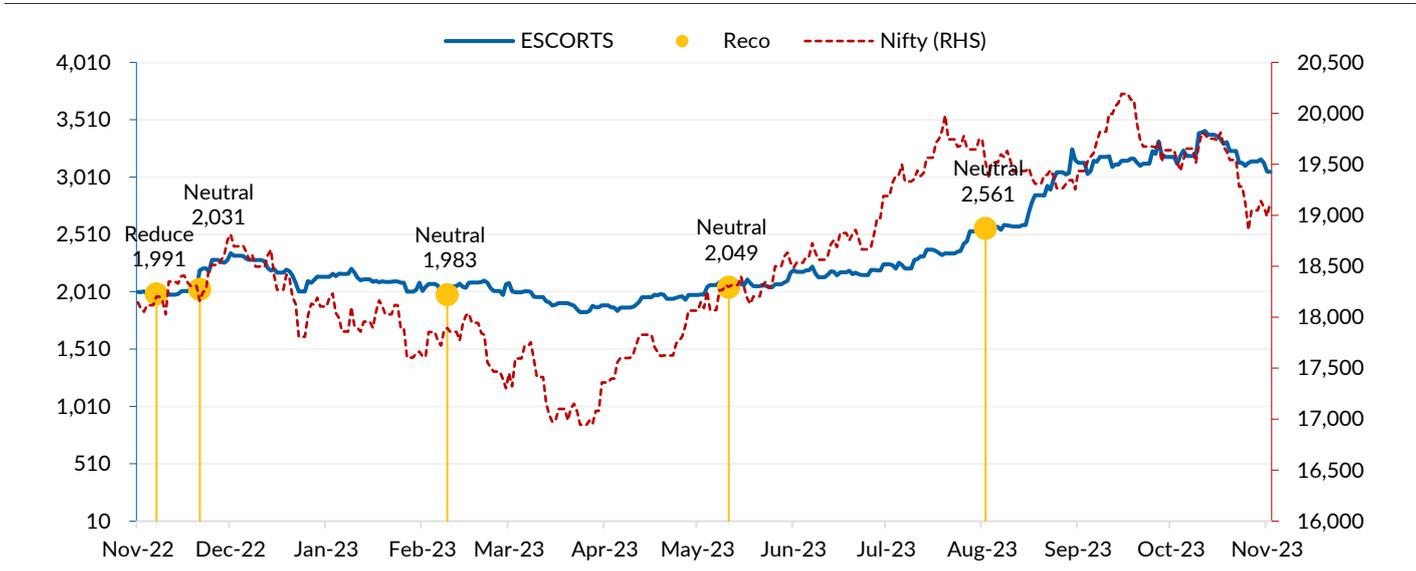
Source- Company, Yes Sec

Exhibit 10: Growth and Ratio matrix

Y/E March	FY20	FY21	FY22	FY23	FY24E	FY25E
Basic (INR)						
EPS	53.9	86.2	74.9	68.9	114.2	136.1
Cash EPS	65.9	97.9	88.3	84.2	130.8	153.7
BV/Share	350.7	497.0	773.6	833.3	938.1	1,064.8
DPS	2.5	7.5	7.0	7.0	7.0	7.0
Payout (%)	7.5	11.6	12.6	14.5	8.2	6.9
Valuation (x)						
P/E	57.1	35.7	41.1	44.6	26.9	22.6
Cash P/E	46.7	31.4	34.8	36.5	23.5	20.0
P/BV	8.8	6.2	4.0	3.7	3.3	2.9
EV/Sales	4.7	5.2	5.1	4.4	3.9	3.6
EV/EBITDA	40.8	32.3	37.6	47.9	27.3	21.9
Dividend Yield (%)	0.1	0.2	0.2	0.2	0.2	0.2
FCF per share	49.5	74.9	(10.9)	0.8	69.0	99.4
Return Ratios (%)						
RoE	16.5	21.4	11.7	8.6	12.9	13.6
RoCE	21.5	28.6	16.4	11.5	17.4	18.3
RoIC	20.1	42.3	32.2	18.6	30.3	35.7
Working Capital Ratios						
Asset Turnover (x)	1.8	1.4	1.0	1.0	1.0	0.9
Inventory (Days)	83.9	56.4	62.1	72.6	66.0	66
Debtor (Days)	46.0	34.2	39.7	51.1	53.0	50
Creditor (Days)	104.6	87.2	66.9	73.2	66.0	66
Working Cap. Turnover (Days)	13.9	(3.6)	29.9	43.5	46.8	45
Leverage Ratio (x)						
Current Ratio	1.3	1.7	1.6	1.8	2.2	2.6
Interest Cover Ratio	32.2	75.6	57.7	47.3	93.7	121.7
Debt/Equity	0.0	0.0	-	-	-	-

Source- Company, Yes Sec

Recommendation Tracker



Source - YES Sec

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