



Industry	Automobiles
Bloomberg	ESC IN
BSE CODE	500495

## Margin expansion to be seen in FY21

<b>RATING</b>	<b>HOLD</b>
<b>CMP</b>	<b>648</b>
<b>Price Target</b>	<b>690</b>
<b>Potential Upside</b>	<b>6%</b>

<b>Rating Change</b>	
<b>Estimate Change</b>	
<b>Target Change</b>	

## Stock Info

52wk Range H/L	834/423
Mkt Capital (Rs Cr)	7947
Free float (%)	60%
Avg. Vol 1M (,000)	3733
No. of Shares (Cr.)	12
Promoters Pledged %	0%

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## 2QFY20 Result Update

- ❑ ESCORTS reported a decline in sales by 5.3% YoY to Rs.1324 crores (vs our estimates of Rs. 1395 crores) in 2QFY20.
- ❑ Agri Machinery segments revenue de-grew by 5%YoY to Rs.1231 crores on account of 6% YoY decline in volumes. Tractor sales for the quarter stood at 19750 units. However, realization grew by 2%YoY. EBIT margin declined by 60bps QoQ to 10.3%.
- ❑ The domestic market share in the agri-machinery segment stands at 11.2% in 2QFY20.
- ❑ Construction equipment segments revenue also de-grew by 19% YoY to Rs.201 crores largely on account of 29% YoY lower volumes. However, realizations grew by 14% YoY. EBIT margin for construction equipment segment went up by 195 bps YoY to 2.7%.
- ❑ The railways business revenue grew by 20%YoY to Rs.127 crores on the back of strong order book execution. The EBIT margin stood at 19.1% in 2QFY20.
- ❑ On the railway business, the company has an order book of around Rs.500 crores and it will be executed over the next 12-15 months
- ❑ Gross margin improved by 213 bps QoQ to 33.1% on account of softening commodity prices and price hikes in construction equipment segment. However, EBITDA margin declined by 29 bps QoQ to 9.7% due to change in product mix and higher fixed cost.
- ❑ PAT grew by 2%YoY to Rs.105 crores (vs our estimates of Rs.104 crores). PAT margin improved by 175 bps QoQ to 7.9% led by lower interest and tax expenses.
- ❑ Exceptional item during the quarter was Rs 9.22 crores on account of final settlement of old product liability.
- ❑ Dealer inventory level in the agri-machinery segment stands at less than 4 weeks.
- ❑ Tax rate is expected to be in the range of 23-24% for FY20.

## View and Valuation

The demand sentiment has improved in last couple of months and 2HFY20 is expected to be better on the back of better monsoon and subsidy-based sales and increased sales of new products in 21-30HP category. Exports will continue to grow at 25-30% for next 2 years with increased presence in new markets. Going ahead 100-120 bps margin expansion can be seen in FY21 based on better operating leverage, increasing premium product sales in construction equipment and improving localisation in high margin railway business. Factoring the improvement in demand scenario, better margins in FY21 and reduction in borrowings we increase our FY21 EPS estimates by 4%. We value ESCORTS at 14x FY21e EPS to arrive at target price of Rs.690 and recommend HOLD.

## Key Risks to our rating and target

- ❑ Slowdown in tractor industry
- ❑ Sharp increase in commodity prices

Fig in Rs Cr

KEY FINANCIAL/VALUATIONS	FY17	FY18	FY19	FY20E	FY21E
Net Sales	4145	5059	6262	6311	6922
EBITDA	309	554	725	664	830
EBIT	246	480	637	561	725
PAT	131	347	477	466	605
EPS (Rs)	13	28	39	40	49
EPS growth (%)	59	115	40	1	23
ROE (%)	9.9	15.6	18.1	17.9	18.4
ROCE (%)	15.5	21.7	24.2	21.0	22.3
BV	132	181	218	223	268
P/B (X)	4.1	4.9	3.0	2.9	2.4
P/E (x)	41.2	31.3	16.3	16.2	13.2

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## 2QFY20 Results

PAT in line with expectation

Financials	Fig in Rs Cr									
	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	YoY %	QoQ%	FY18	FY19	YoY %
Net Sales	1,398	1,655	1,632	1,423	1,324	-5%	-7%	5,059	6,262	24%
Other Income	22	24	17	17	21	-5%	26%	65	92	41%
Total Income	1,420	1,679	1,649	1,440	1,345	-5%	-7%	5,125	6,354	24%
COGS	944	1,151	1,123	982	885	-6%	-10%	3,397	4,277	26%
Staff Cost	113	120	118	123	125	11%	2%	442	485	10%
Other Exp.	184	184	201	176	185	0%	5%	666	776	16%
Expenditure	1,241	1,455	1,442	1,281	1,195	-4%	-7%	4,506	5,537	23%
EBITDA	157	200	190	142	129	-18%	-10%	554	725	31%
Depreciation	21	22	22	24	28	30%	16%	73	87	19%
EBIT	136	179	168	118	101	-26%	-15%	480	637	33%
Interest	4	4	7	6	4	0%	-34%	29	20	-34%
PBT	154	199	178	129	118	-24%	-9%	516	710	38%
Excpt. Item	-	(11)	-	-	9	0%	0%	7	(6)	0%
Tax	52	70	56	42	4	-92%	-90%	162	237	46%
PAT	103	140	121	88	105	2%	20%	347	477	38%

## Concall Highlights

### ➤ Tractor Industry :-

- The industry is expected to see single digit growth in FY20 while FY21 is expected to have a better growth momentum. In Q2FY20, domestic industry was down by 10% YoY to 1.68 lakh units.
- The overall sentiment improved after October led by festive season and good rainfall across various parts of the country. However, lower construction activities along with lower subsidy sales will continue to impact the industry.
- The management expects the growth momentum to continue going ahead based on good rainfall, improved reservoir level and better subsidy sales for next 2 years.
- The overall subsidy sales at the industry level is expected to be around 5-10% going ahead.
- Industry in Q2FY20 in North and central region de-grew by 1.8% YoY, whereas industry de-grew by 18.2% YoY in South and west region.

### ➤ Agri Machinery Business :-

- The domestic market share in the agri-machinery segment stands at 11.2% in 2QFY20. It was 10.5% in 1QFY20.
- North and Central India saw better retail sales in October. Western regions like Maharashtra also saw some recovery on account of good rainfall.
- H2FY20 is expected to grow led by festive season demand, Rabi sowing, higher subsidy sales from Telangana, Assam, Maharashtra and Gujarat going ahead.
- Tractor exports growth guidance is expected to be at 35-40% for FY21.
- Farmtrac and Powertrac ratio stood at 59:41 in 2QFY20 as against 62:38 in 1QFY20. The management expects it to be at 60:40 in FY20.
- The emission norms changes for tractors from 1st Oct 2020 is only for more than 50hp tractors and the price increase from this is expected to be 15-16%.
- The company is building capacity with the Kubota JV and it is expected to commence by mid of FY21.
- The non tractor based (spare parts and implements) contributes 9% to the total revenue. The company is focusing on increasing its product portfolio in farm implements.
- Dealer inventory level stands at less than 4 weeks.

➤ **Construction Equipment Business:-**

- The management expects to see high single digit growth on a long term basis in this segment.
- The construction equipment segment continues to see slowdown on account of financing issues, slowdown in construction activities and delayed payments for ongoing infra projects.
- The served industry including backhoe loaders pick up and carry cranes and compactors degrew by 30.1% YoY in 2QFY20.
- The total volumes, traded and manufacturing products were correspondingly down by 29% to 945 units in 2QFY20. However there has been marginal improvement in market share.
- The company made new launches in the compactors segment during the quarter.
- The management expects the margins to be around 4% for FY20 and 5-7% for the next 2-3 years.

➤ **Railway Business:-**

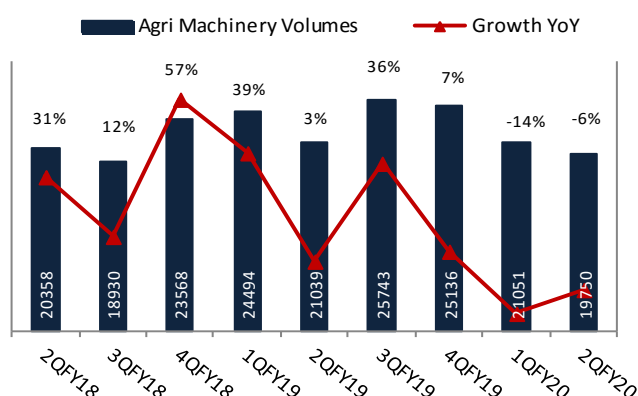
- The management expects to post 15-20% growth in railways business in FY20.
- Order book during the quarter is around Rs.500 crores and will be executed in the next 12-15 months.
- The management executed 42% of the total order from new products having higher import content and lower margins. In 1QFY20 it executed 30% of the order.
- Margins are expected to be maintained at the current level going ahead. Currently it stands at 19.1% in 2QFY20.

➤ **Other Highlights:-**

- Production level in 2QFY20 was down by 19%.
- The company added 45 new dealers and the total dealerships are at 950+. The management is focusing on expansion of dealerships going ahead.
- The company benefited by 1% on commodity cost which impacted the gross margin positively.
- Exceptional item during the quarter was Rs 9.22 crs on account of final settlement of old product liability.
- Total debt stood at Rs 209 crs in 2QFY20. It was Rs. 273 crs in FY19.
- Tax rate is expected to be in the range of 23-24% for FY20 and it will be 25% hoing ahead from FY21.
- Average debtor days are expected to be 35-40 days going ahead.

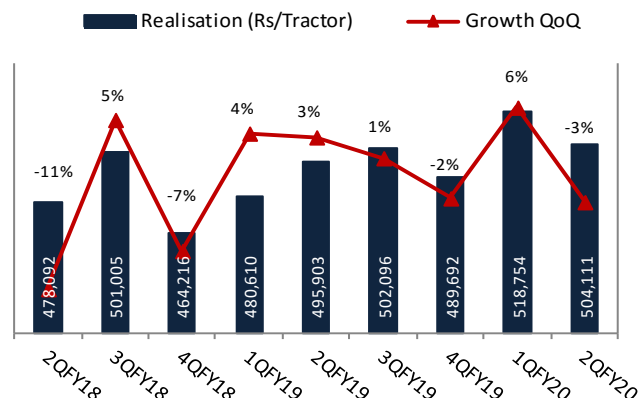
## Exhibit: Escorts Agri-Machinery Volume Trend

Volume growth declined by 6% YoY due to slowdown in demand sentiments across various markets



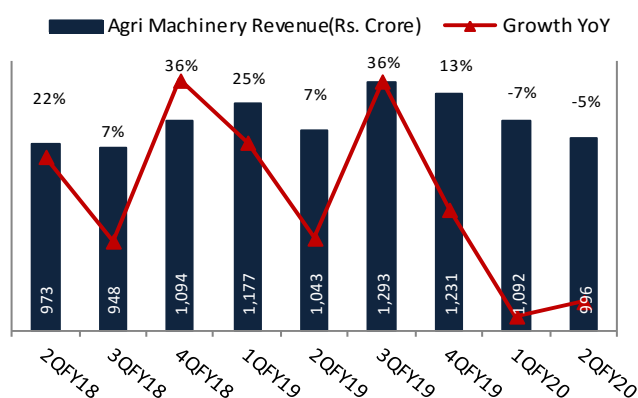
## Exhibit: Escorts Agri-Machinery Realisation Trend

Realization declined by 3% QoQ on the back of change in product mix towards lower HP segment



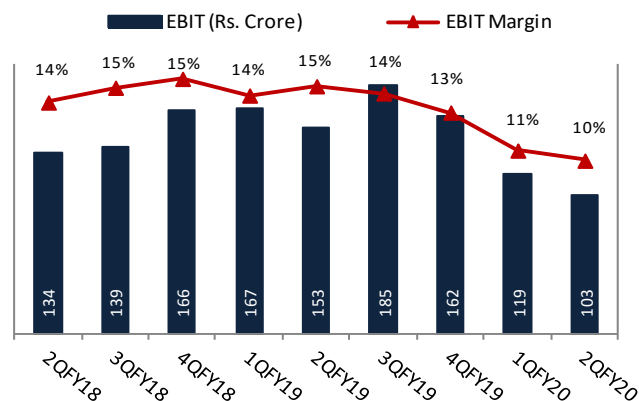
## Exhibit: Escorts Agri-Machinery Revenue Trend

Revenue growth declined due to lower sales in the domestic market



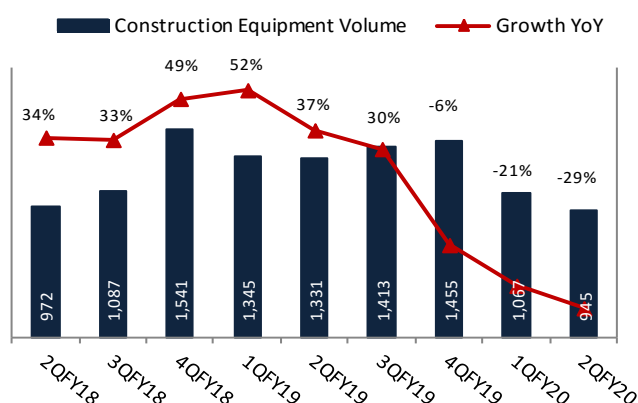
## Exhibit: Escorts Agri-Machinery EBIT & EBIT Margin

Margins declined due to lower volumes and unfavourable product mix



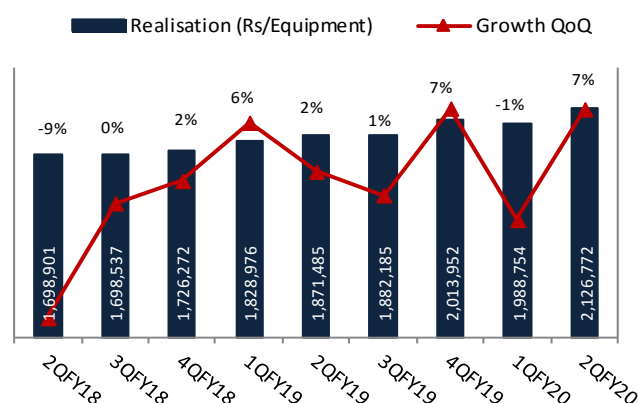
## Exhibit: Escorts Construction Equipment Volume Trend

Construction equipment volumes declined by 29%YoY due to liquidity crisis and pending payments on infra projects



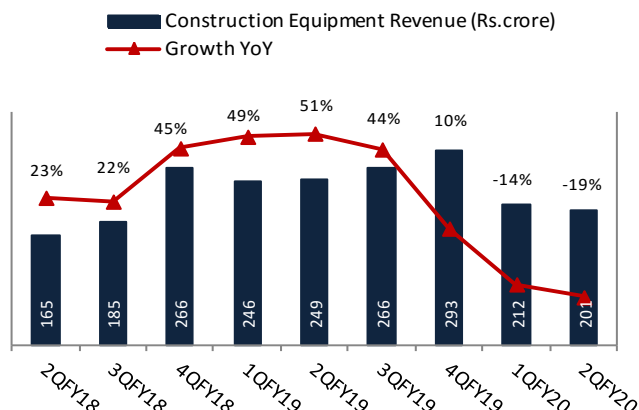
## Exhibit: Escorts Construction Equipment Realisation

Shift in product mix towards lower realisation products led to 7% QoQ decrease



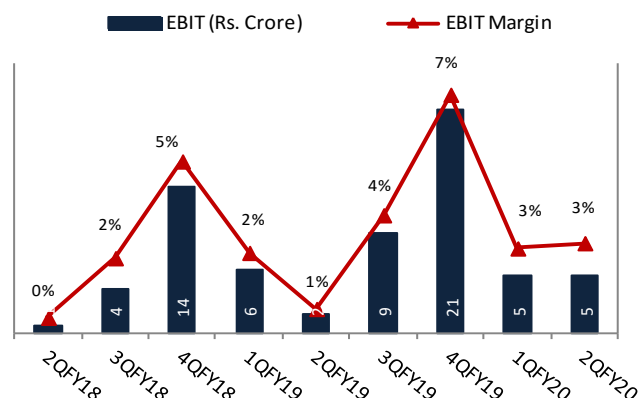
## Exhibit: Escorts Construction Equipment (ECE) Revenue

Revenue de-grew by 19%YoY due to slowdown in construction activities



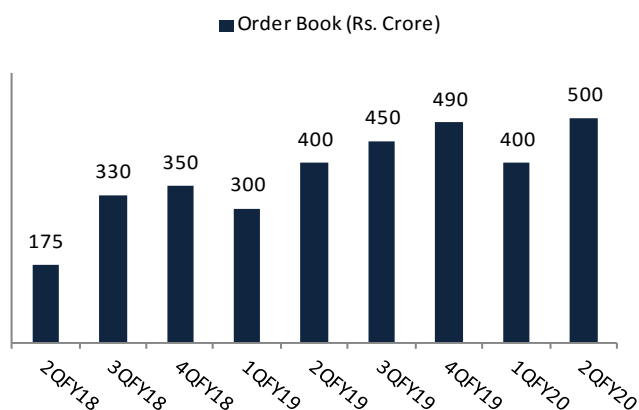
## Exhibit: ECE EBIT Margin

Margins improved marginally on the back of better product mix



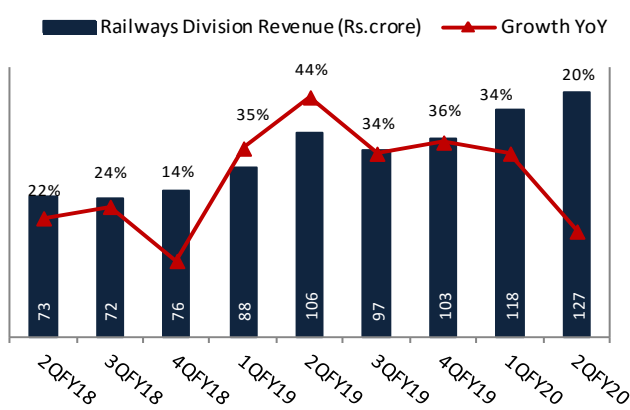
## Exhibit: Escorts Railway Division Order Book

The company's order book stands at Rs.500 crores which will get executed over a period of 12-15 months



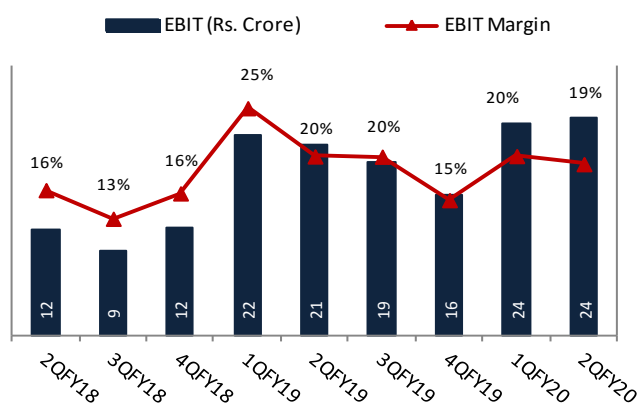
## Exhibit: Escorts Railway Division Revenue Trend

Higher revenue on account of higher order execution during the quarter



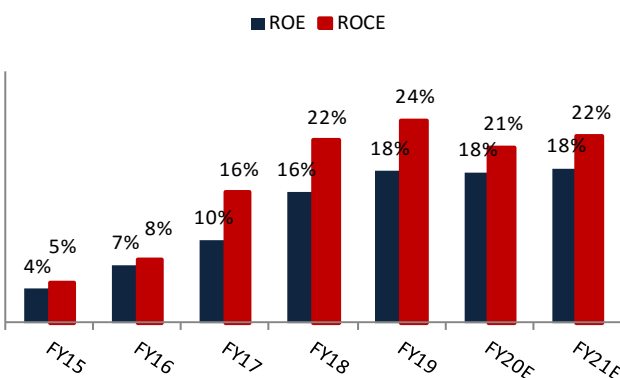
## Exhibit: Escorts Railway Division EBIT and EBIT Margin

Margins remained at 19% level due to introduction of higher margin products



## Exhibit: RoE and RoCE Trend

Increase in profitability will lead to expansion in return ratios going ahead



## Financial Details

### Balance Sheet

Fig in Rs Cr

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
Share Capital	119	119	123	123	123	123	123	123
Reserves	1,746	1,711	1,344	1,498	2,093	2,551	2,606	3,165
Networth	1,866	1,831	1,466	1,621	2,215	2,673	2,729	3,287
Debt	352	411	315	218	15	273	202	151
Other Non Cur Liab	191	163	57	51	60	107	107	110
Total Capital Employed	2,011	1,937	1,556	1,680	2,230	2,677	2,729	3,287
Net Fixed Assets (incl CWIP)	1,692	1,651	1,597	1,592	1,630	1,704	1,891	2,056
Non Cur Investments	368	367	30	38	50	2	2	2
Other Non Cur Asst	94	96	118	109	141	232	232	232
Non Curr Assets	2,154	2,115	1,746	1,739	1,820	1,938	2,125	2,290
Inventory	587	453	433	450	566	857	830	910
Debtors	372	414	375	456	592	931	865	948
Cash & Bank	271	251	253	244	317	243	241	389
Other Curr Assets	10	13	103	103	151	300	302	332
Curr Assets	1,488	1,388	1,189	1,445	2,144	2,756	2,612	3,108
Creditors	870	738	751	910	1,234	1,249	1,297	1,422
Provisions (both)	82	89	133	132	133	120	121	133
Other Curr Liab	263	256	89	118	125	132	133	146
Curr Liabilities	1,215	1,083	1,103	1,308	1,684	1,649	1,700	1,849
Net Curr Assets	273	305	86	138	460	1,107	912	1,258
Total Assets	3,642	3,503	2,944	3,199	3,973	4,708	4,737	5,398

### Income Statement

Fig in Rs Cr

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
Revenue from Operation	6,292	3,986	3,367	4,093	4,995	6,196	6,245	6,849
Change (%)	62	(37)	(16)	22	22	24	1	10
Other Income	81	61	56	43	59	81	76	88
<b>EBITDA</b>	<b>381</b>	<b>161</b>	<b>177</b>	<b>324</b>	<b>557</b>	<b>733</b>	<b>676</b>	<b>840</b>
Change (%)	109	(58)	10	83	72	32	(8)	24
<b>Margin (%)</b>	<b>6.1</b>	<b>4.0</b>	<b>5.3</b>	<b>7.9</b>	<b>11.2</b>	<b>11.8</b>	<b>10.8</b>	<b>12.3</b>
Depr & Amor.	83	66	57	63	72	85	103	105
EBIT	298	95	119	261	485	648	572	734
Int. & other fin. Cost	111	57	50	31	29	18	21	15
<b>EBT</b>	<b>269</b>	<b>99</b>	<b>126</b>	<b>273</b>	<b>516</b>	<b>710</b>	<b>627</b>	<b>807</b>
Exp Item	(4)	31	12	(44)	7	(11)	-	-
Tax	28	(6)	12	76	164	238	138	203
Minority Int & P/L share of Ass.	-	-	-	-	-	-	-	-
<b>Reported PAT</b>	<b>245</b>	<b>75</b>	<b>101</b>	<b>160</b>	<b>345</b>	<b>484</b>	<b>489</b>	<b>604</b>
<b>Adjusted PAT</b>	<b>245</b>	<b>75</b>	<b>101</b>	<b>160</b>	<b>345</b>	<b>484</b>	<b>489</b>	<b>604</b>
Change (%)	252	(69)	35	59	115	40	1	23
Margin(%)	3.9	1.9	3.0	3.9	6.9	7.8	7.8	8.8

## Financial Details

### Key Ratios

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
ROE	13.1%	4.1%	6.9%	9.9%	15.6%	18.1%	17.9%	18.4%
ROCE	15%	5%	8%	16%	22%	24%	21%	22%
Asset Turnover	1.79	1.17	1.17	1.30	1.27	1.33	1.33	1.28
Debtor Days	21	37	40	40	43	54	50	50
Inv Days	33	40	46	40	41	50	48	48
Payable Days	49	66	80	80	89	73	75	75
Int Coverage	3	2	2	8	16	33	-	-
P/E	6	20	17	41	31	16	16	13
Price / Book Value	1	1	1	4	5	3	3	2
EV/EBITDA	3	8	12	22	20	11	12	10
FCF/Share	38	5	21	30	47	(7)	85	78

### Cash Flow Statement

Fig in Rs Cr

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
PBT	275	70	73	190	509	716	623	809
(inc)/Dec in Working Capital	3	(119)	37	55	(18)	(745)	142	(41)
Non Cash Op Exp	86	69	61	65	73	87	103	105
Int Paid (+)	93	50	54	36	22	12	21	15
Tax Paid	(62)	(21)	7	(44)	(102)	(217)	(157)	(204)
others	(71)	(45)	(20)	2	(15)	(68)	14	-
CF from Op. Activities	324	5	212	304	471	(234)	746	685
(inc)/Dec in FA & CWIP	(125)	(55)	(49)	(66)	(105)	(147)	(290)	(270)
Free Cashflow	200	(50)	164	238	367	(381)	456	415
(Pur)/Sale of Inv	1	(0)	(3)	(161)	(311)	129	51	(155)
others	54	30	7	73	34	42	-	-
CF from Inv. Activities	(70)	(26)	(45)	(155)	(374)	(17)	(239)	(425)
inc/(dec) in NW	-	0	-	-	-	-	-	-
inc/(dec) in Debt	(115)	59	(132)	(103)	(213)	231	(71)	(50)
Int. Paid	(94)	(50)	(46)	(29)	(22)	(14)	(21)	(15)
Div Paid (inc tax)	(25)	(6)	(13)	(13)	(16)	(29)	(36)	(46)
others	5	(1)	(1)	31	250	3	-	-
CF from Fin. Activities	(230)	1	(191)	(113)	(1)	191	(128)	(112)
Inc(Dec) in Cash	24	(19)	(24)	36	96	(61)	379	148
Add: Opening Balance	145	271	56	33	69	154	243	241
Closing Balance	170	251	32	69	165	93	604	371

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Registration Details of Group entities: G. Raj & Company Consultants Ltd (G RAJ)-BSE Broker INZ260010731; NSDL DP: IN-DP-NSDL-371-2014 || Narnolia Commerze Limited (Formerly Microsec Commerze Ltd.)-MCX/NCDEX Commodities Broker: INZ000051636 || NarnoliaVelox Advisory Ltd.- SEBI Registered PMS: INP000005109 || Eastwind Capital Advisors Pvt Ltd. (EASTWIND)-SEBI Registered Investment Adviser: INA300005439 || Narnolia Insurance Brokers Limited (Formerly Microsec Insurance Brokers Ltd.)-IRDA Licensed Direct Insurance Broker (Life & Non-Life) Certificate No. 134, License No. DB046/02 || Narnolia Securities Ltd. (NSL)-AMFI Registered Mutual Fund distributor: ARN 20558, PFRDA NPS POP: 27092018 || Narnolia Capital Advisors Pvt. Ltd. - RBI Registered NBFC:B.05.02568.

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