

BSE SENSEX	S&P CNX
40,302	11,941
Bloomberg	ESC IN
Equity Shares (m)	123
M.Cap.(INRb)/(USD\$b)	79.5 / 1.1
52-Week Range (INR)	834 / 423
1, 6, 12 Rel. Per (%)	1/-4/-19
12M Avg Val (INR M)	1562
Free float (%)	59.8

CMP: INR648

TP: INR700(+8%)

Neutral

In-line; recovery in festive season drives inventory reduction

- Operating leverage hurts margins:** Escorts' (ESC) revenue declined ~5% YoY to INR13.2b (our estimate: INR13.5b), led by lower volumes in Tractor (-6% YoY) and Construction Equipment (CE; -21% YoY) segments. Railway revenue grew ~20% YoY. Tractor realizations declined 2.8% QoQ (+1.7% YoY) to ~INR504k due to a weaker mix. EBITDA margin of 9.6% (our estimate: 9.8%) was impacted by operating leverage and an adverse mix in Tractor/Rail. PBT declined ~24% YoY, but lower tax drove PAT growth of ~10% YoY to INR1.1b (our estimate: INR1b). Tractor segment PBIT margin shrank ~440bp YoY (-60bp QoQ) to 10.3%.
- 1H performance:** ESC reported positive CFO of ~INR3b (v/s negative ~INR2.7b in 1HFY19), led by lower working capital. FCFE was at ~INR2b (v/s -INR3.4b in 1HFY19). Revenue/EBITDA/PAT declined ~6%/21.5%/9.5% YoY.
- Earnings call highlights:** (a) Industry volumes declined 10% YoY. ESC's strong markets declined by ~2% and opportunity markets (east, south and west) by ~18%. (b) Dealer inventory was at <4 weeks as of Oct'19 (below normal), whereas inventory with company stood at 2 weeks. (c) FY20 industry volumes are likely to decline in single digit (implied flat volumes for 2H). A full-fledged recovery might be seen from Mar'20 or May-Jun'20. (d) The recovery was good in the festive season (Navratras to Diwali), though lower on a YoY basis. Industry de-grew by 15% in Apr-Aug and 5% in Sep-Oct. Momentum is expected to continue in Nov'19. (e) It added 45 new dealers (to over 950 dealers) in 2Q. (f) Rail order book stood at ~INR5b, which will get executed over the next 12-15 months. (g) Margins in 2H are likely to be better than 1H with inventory correction now behind.
- Valuation view:** We upgrade our FY21E EPS by ~5% as we factor in higher tractor volumes in wake of good monsoon. The stock trades at 12.3x/10.8x FY20/21E EPS. Maintain **Neutral** with a TP of ~INR700 (~11x Sep'21 EPS).

Financials & Valuations (INR b)

Y/E Mar	2019	2020E	2021E
Net Sales	62.6	60.6	65.3
EBITDA	7.2	6.6	7.6
PAT	4.7	4.7	5.3
EPS (INR)	53.2	52.7	59.8
Gr. (%)	34.7	-1.0	13.4
BV/Sh (INR)	300.8	348.7	402.8
RoE (%)	19.3	16.2	15.9
RoCE (%)	18.8	20.8	21.4
P/E (x)	12.2	12.3	10.8
P/BV (x)	2.2	1.9	1.6

Estimate change



TP change



Rating change



Standalone Quarterly Performance

Y/E March	FY19				FY20				(INR Million)		
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	FY19	FY20E	FY20 2Q
Net Sales	15,113	13,984	16,551	16,317	14,230	13,239	16,125	16,992	62,620	60,584	13,523
YoY Change (%)	29.9	15.4	37.3	13.6	-5.8	-5.3	-2.6	4.1	23.8	-3.3	(3.3)
Total Expenditure	13,257	12,409	14,546	14,419	12,805	11,972	14,214	14,960	55,375	53,950	12,197
EBITDA	1,855	1,575	2,005	1,898	1,424	1,267	1,911	2,032	7,245	6,634	1,325
Margins (%)	12.3	11.3	12.1	11.6	10.0	9.6	11.9	12.0	11.6	11.0	9.8
Depreciation	206	215	215	218	241	260	265	270	872	1,036	245
Interest	29	39	43	75	59	39	40	43	195	180	60
Other Income	170	221	244	173	167	211	210	244	924	832	200
PBT before EO expense	1,791	1,543	1,991	1,778	1,292	1,179	1,816	1,963	7,102	6,250	1,220
Extra-Ord expense	0	0	-109	0	0	92	0	0	-56	0	0
PBT	1,791	1,543	1,100	1,778	1,292	1,087	1,816	1,963	7,157	6,250	1,220
Rate (%)	33.2	33.5	33.3	31.8	32.2	3.8	24.5	32.9	33.1	24.8	18.0
Adj PAT	1,196	1,026	1,328	1,214	875	1,135	1,371	1,299	4,730	4,683	1,001
YoY Change (%)	90.9	24.9	44.6	7.8	-26.8	10.5	3.2	7.0	34.7	-1.0	-2.5

E: MOFSL Estimates

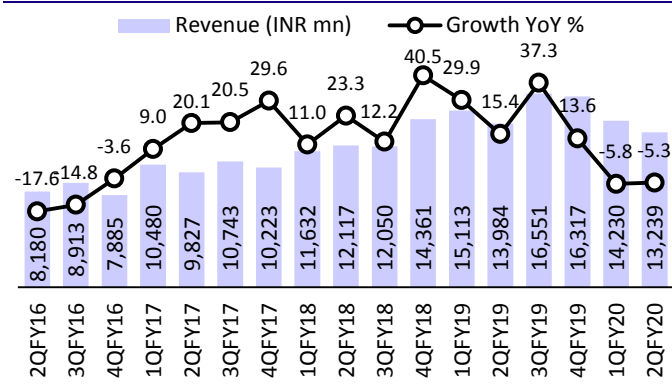
Jinesh Gandhi - Research analyst (Jinesh@MotilalOswal.com); +91 22 6129 1524

Aanshul Agarawal - Research analyst (Aanshul.Agarawal@MotilalOswal.com); +91 22 7193 4337

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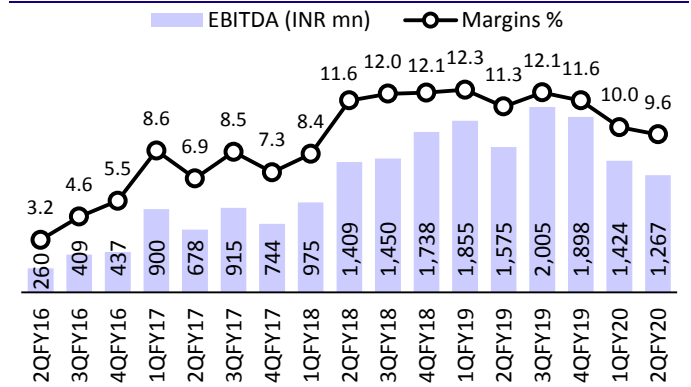
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Exhibit 1: Revenue and revenue growth trend



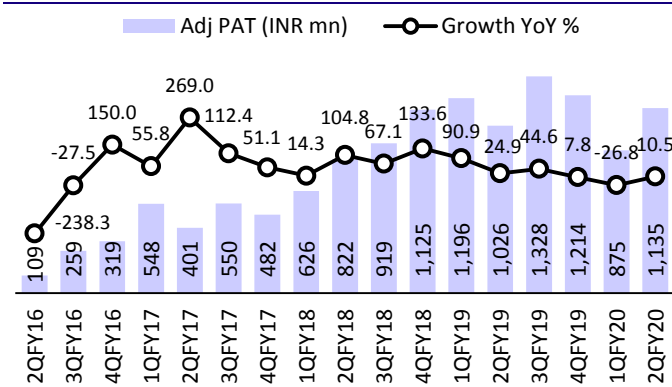
Source: MOFSL, Company

Exhibit 2: EBITDA and EBITDA margins trend



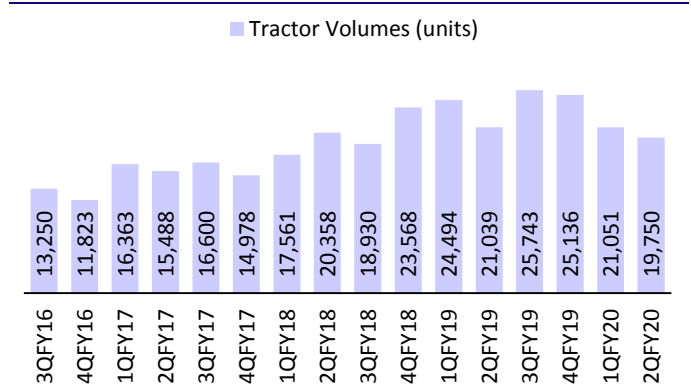
Source: MOFSL, Company

Exhibit 3: Adjusted PAT and growth trend



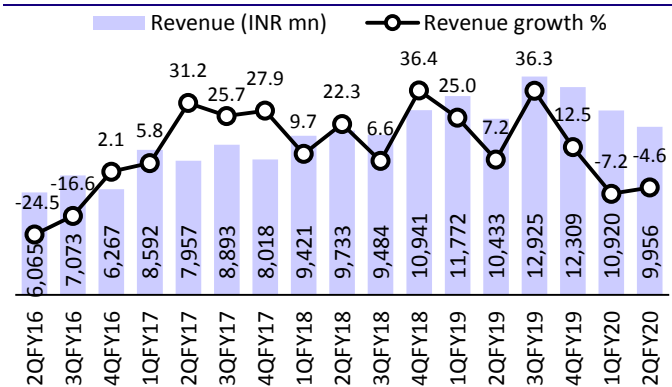
Source: MOFSL, Company

Exhibit 4: Trend in tractor volumes



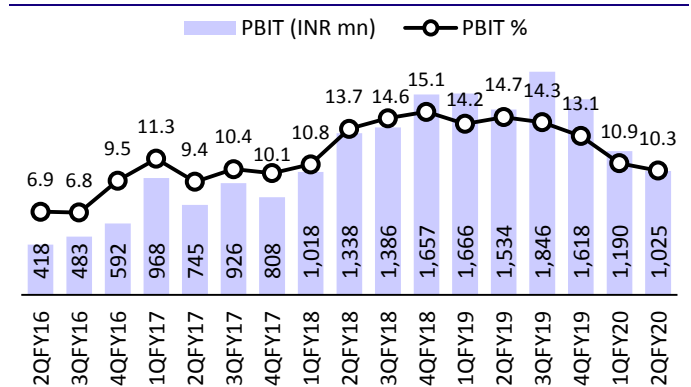
Source: MOFSL, Company

Exhibit 5: Tractor segment revenue and growth



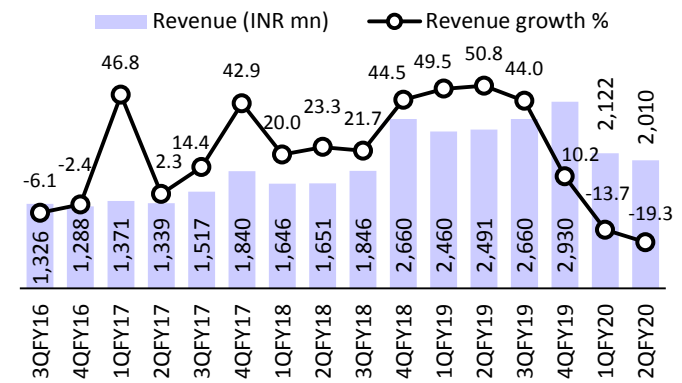
Source: MOFSL, Company

Exhibit 6: Tractor segment PBIT trend



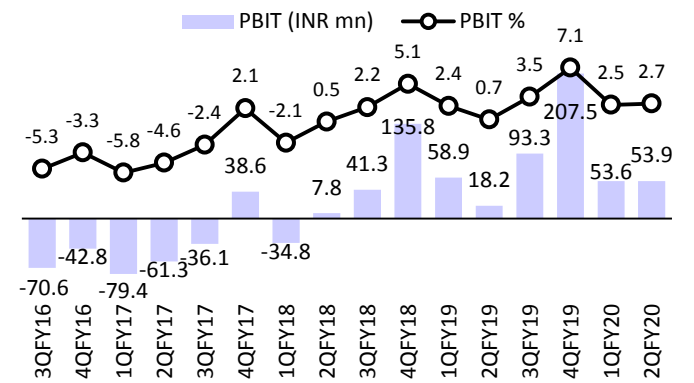
Source: MOFSL, Company

Exhibit 7: Construction equipment revenue and growth



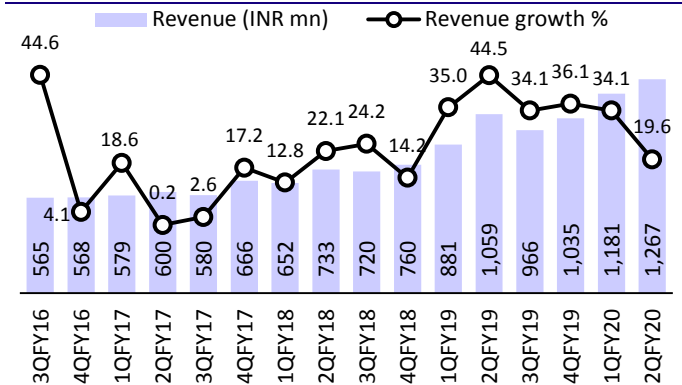
Source: MOFSL, Company

Exhibit 8: Construction equipment segment PBIT trend



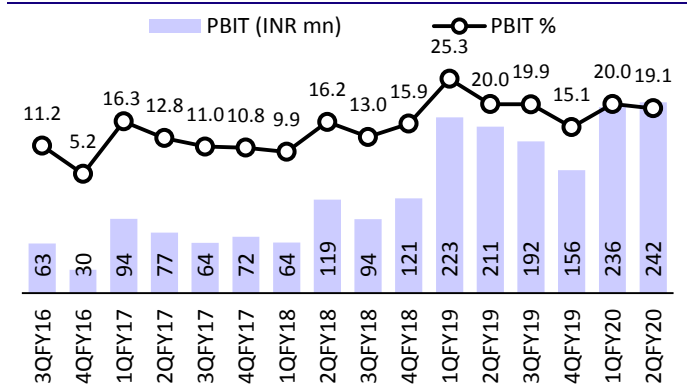
Source: MOFSL, Company

Exhibit 9: Railways segment revenue and growth



Source: MOFSL, Company

Exhibit 10: Railways segment PBIT trend



Source: MOFSL, Company

Valuation and view

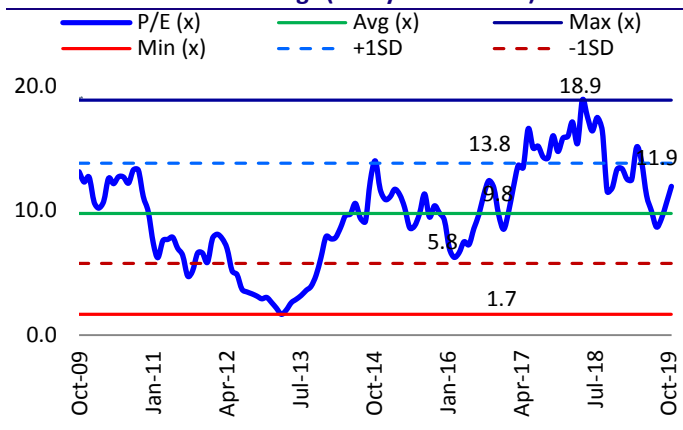
Market share gains in tractor business to continue: With good monsoon, industry volumes are likely to recover in FY21. We expect ESC to gain market share backed by gains in its opportunity market, coupled with a gradual improvement in the company’s competitive positioning in its traditional market due to plugging of product gaps. We expect ESC to continue outperforming the domestic tractor industry volume, with ~5% CAGR over FY19-22.

Healthy traction in construction equipment and railways business: We expect construction equipment revenues to decline at a compounded annual rate of ~3% over FY19-22 on a high base of FY19, whereas railway business CAGR is estimated at ~17%. ESC indicated benefits related to localization and cost savings to elevate the margin profile of both the businesses.

EPS trajectory over FY19-22: With market share expansion in the core tractor business and healthy traction in the CE and railway businesses, we estimate revenues CAGR of ~5% over FY19-22. We expect ESC’s margins to expand ~20bp (over FY19-22) to ~11.8%. Consequently, we expect EPS CAGR of 8%. Our estimates are not yet factoring in any contribution from the Kubota JV.

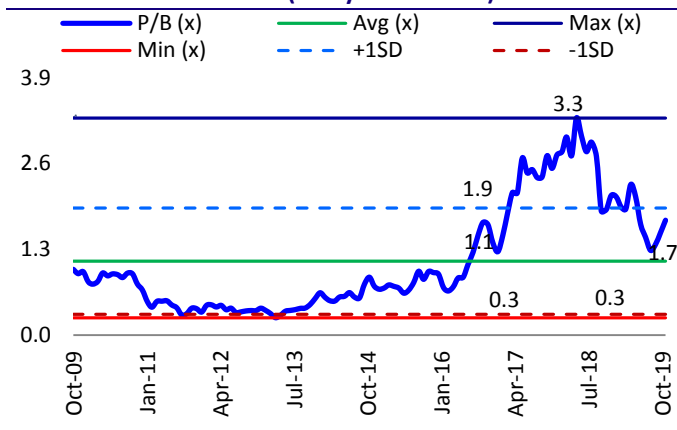
Valuation and view: We have upgraded our FY21E EPS by ~5% as we factor in higher tractor volumes in wake of good monsoon. The stock trades at 12.3x/10.8x FY20/21E EPS. Maintain **Neutral** with a TP of ~INR700 (~11x Sep-21 EPS, at ~10% premium to 10 year average PE of ~9.8x).

Exhibit 11: Price to earnings (one-year forward)



Source: MOFSL, Company

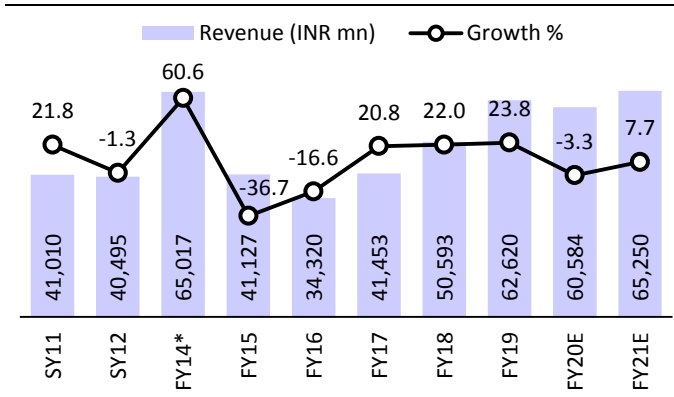
Exhibit 12: Price to book (one year forward)



Source: MOFSL, Company

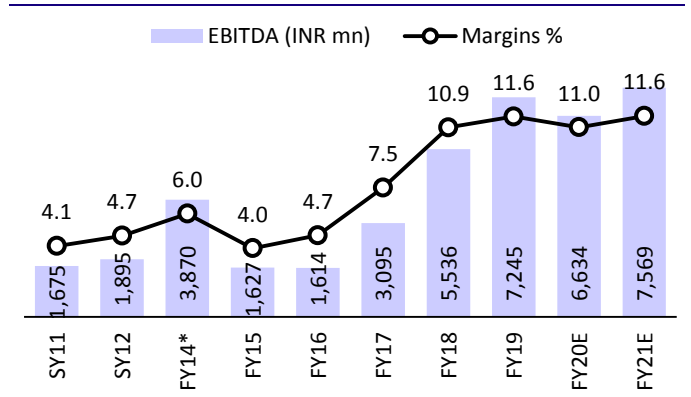
Story in charts

Exhibit 13: Revenue and revenue growth trend



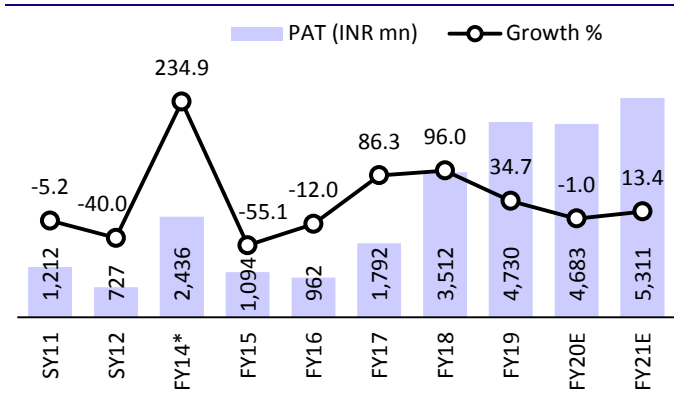
Source: MOFSL, Company

Exhibit 14: EBITDA and EBITDA margins trajectory



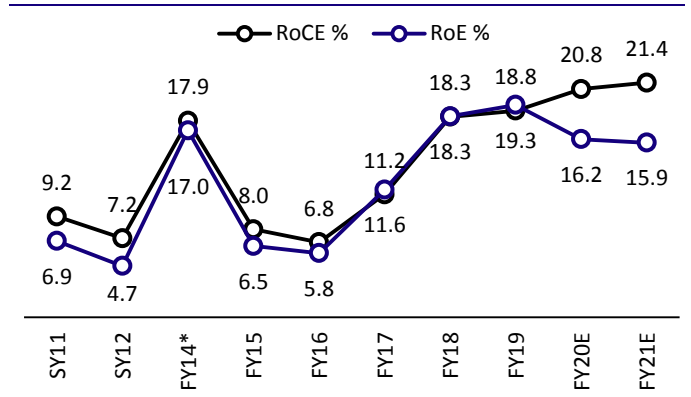
Source: MOFSL, Company

Exhibit 15: PAT and PAT growth trend



Source: MOFSL, Company

Exhibit 16: RoE and RoCE trend



Source: MOFSL, Company

Financials and Valuations

Consolidated - Income Statement

(INR M)

Y/E March	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
Total Income from Operations	41,127	34,320	41,453	50,593	62,620	60,584	65,250
Change (%)	-36.7	-16.6	20.8	22.0	23.8	-3.3	7.7
EBITDA	1,627	1,614	3,095	5,536	7,245	6,634	7,569
Margin (%)	4.0	4.7	7.5	10.9	11.6	11.0	11.6
Depreciation	686	581	634	732	872	1,036	1,105
EBIT	941	1,033	2,461	4,804	6,373	5,598	6,464
Int. and Finance Charges	583	511	322	295	195	180	250
Other Income	652	608	471	653	924	832	873
PBT bef. EO Exp.	1,011	1,130	2,610	5,162	7,102	6,250	7,087
EO Items	-306	-306	-112	-68	56	0	0
PBT after EO Exp.	704	824	2,498	5,094	7,157	6,250	7,087
Current Tax	136	123	773	1,625	2,371	1,547	1,757
Deferred Tax	-192	0	0	0	0	0	0
Tax Rate (%)	-7.9	14.9	30.9	31.9	33.1	24.8	24.8
Less: Minority Interest	-3	0	11	4	20	20	20
Reported PAT	763	702	1,715	3,466	4,767	4,683	5,311
Adjusted PAT	1,094	962	1,792	3,512	4,730	4,683	5,311
Change (%)	-55.1	-12.0	86.3	96.0	34.7	-1.0	13.4
Margin (%)	2.7	2.8	4.3	6.9	7.6	7.7	8.1

Consolidated - Balance Sheet

(INR M)

Y/E March	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
Equity Share Capital	1,193	1,226	1,226	1,226	1,226	1,226	1,226
Total Reserves	17,114	13,439	14,984	20,926	25,509	29,764	34,575
Net Worth	18,307	14,665	16,209	22,151	26,735	30,990	35,801
Minority Interest	147	19	17	-4	56	56	56
Deferred Liabilities	137	0	0	197	529	529	529
Total Loans	4,844	3,153	2,179	147	2,810	1,310	560
Capital Employed	23,434	17,836	18,406	22,492	30,130	32,885	36,946
Gross Block	24,425	25,050	24,600	24,960	26,213	29,771	32,687
Less: Accum. Deprn.	8,470	9,051	8,707	9,082	9,741	10,777	11,882
Net Fixed Assets	15,955	15,999	15,893	15,878	16,472	18,994	20,805
Capital WIP	557	216	266	657	800	242	326
Total Investments	3,726	398	2,123	5,490	4,908	5,508	5,608
Curr. Assets, Loans&Adv.	14,108	12,184	13,187	17,700	24,890	24,477	27,802
Inventory	4,528	4,326	4,503	5,657	8,574	6,561	7,077
Account Receivables	4,143	3,750	4,565	5,920	9,311	6,971	7,508
Cash and Bank Balance	2,514	2,530	2,441	3,173	2,433	5,459	6,634
Loans and Advances	2,923	1,578	1,679	2,949	4,572	5,487	6,584
Curr. Liability & Prov.	11,592	11,604	13,587	17,242	16,952	16,349	17,608
Account Payables	9,563	9,997	12,064	15,746	15,495	14,939	16,089
Provisions	2,030	1,606	1,522	1,495	1,458	1,410	1,519
Net Current Assets	2,515	580	-399	458	7,938	8,129	10,194
Deferred Tax assets	680	643	523	8	12	12	12
Misc Expenditure	0	0	0	0	0	0	0
Appl. of Funds	23,434	17,836	18,406	22,493	30,130	32,885	36,946

E: MOFSL Estimates

Financials and Valuations

Ratios

Y/E March	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
Basic (INR)							
EPS (ex treasury)	13.3	11.3	21.0	39.5	53.2	52.7	59.8
Cash EPS	21.7	18.1	28.5	47.8	63.0	64.3	72.2
BV/Share	223.3	172.0	190.1	249.2	300.8	348.7	402.8
DPS	1.2	1.2	1.5	2.0	2.5	3.0	3.5
Payout (%)	23.2	25.2	12.5	8.2	7.4	9.1	9.3
Valuation (x)							
P/E	48.6	57.5	30.9	16.4	12.2	12.3	10.8
Cash P/E	29.9	35.8	22.8	13.6	10.3	10.1	9.0
P/BV	2.9	3.8	3.4	2.6	2.2	1.9	1.6
EV/Sales	1.4	1.6	1.3	1.1	0.9	0.9	1.1
EV/EBITDA	35.4	34.6	17.8	9.9	8.0	8.1	6.8
Dividend Yield (%)	0.2	0.2	0.2	0.3	0.4	0.5	0.5
FCF per share	-5.4	14.4	19.5	28.9	-31.0	46.9	22.8
Return Ratios (%)							
RoE	6.5	5.8	11.6	18.3	19.3	16.2	15.9
RoCE	8.0	6.8	11.2	18.3	18.8	20.8	21.4
RoIC	6.1	5.6	12.0	24.5	24.2	19.3	21.1
Working Capital Ratios							
Asset Turnover (x)	1.8	1.9	2.3	2.2	2.1	1.8	1.8
Inventory (Days)	56	66	58	61	73	58	58
Debtor (Days)	36	39	39	43	54	42	42
Creditor (Days)	85	106	106	114	90	90	90
Working Cap. Turnover (Days)	0	-21	-25	-20	32	16	20
Leverage Ratio (x)							
Current Ratio	1.2	1.0	1.0	1.0	1.5	1.5	1.6
Interest Cover Ratio	2	2	8	16	32.6	31.1	25.9
Debt/Equity	0.3	0.2	0.1	0.0	0.1	0.0	0.0

Consolidated - Cash Flow Statement

(INR M)

Y/E March	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
OP/(Loss) before Tax	704	789	1,903	5,091	7,231	6,246	7,082
Depreciation	686	612	649	732	854	1,036	1,105
Interest & Finance Charges	11	145	11	-26	-230	180	250
Direct Taxes Paid	-209	11	-437	-1,021	-2,165	-1,547	-1,757
(Inc)/Dec in WC	-1,335	605	548	-181	-7,512	2,835	-891
CF from Operations	-141	2,161	2,674	4,596	-1,823	8,749	5,789
Others	43	132	365	5	-584	0	0
CF from Operating incl EO	-98	2,293	3,038	4,601	-2,407	8,749	5,789
(inc)/dec in FA	-552	-532	-654	-1,059	-1,391	-3,000	-3,000
Free Cash Flow	-650	1,761	2,384	3,541	-3,798	5,749	2,789
(Pur)/Sale of Investments	-2	-33	-1,196	-2,934	909	0	0
Others	446	134	304	252	346	-600	-100
CF from Investments	-109	-432	-1,546	-3,742	-136	-3,600	-3,100
Issue of Shares	0	0	0	0	0	0	0
Inc/(Dec) in Debt	592	-1,212	-1,031	-2,350	2,268	-1,500	-750
Interest Paid	-503	-463	-287	-216	129	-180	-250
Dividend Paid	-64	-132	-128	-161	-222	-424	-494
Others	-11	-37	314	2,716	-257	-20	-20
CF from Fin. Activity	13	-1,844	-1,131	-10	1,917	-2,123	-1,514
Inc/Dec of Cash	-193	17	361	849	-626	3,026	1,175
Opening Balance	2,707	2,514	2,530	2,441	3,173	2,433	5,459
Closing Balance	2,514	2,531	2,892	3,290	2,547	5,459	6,634

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

*In case the recommendation given by the Research Analyst is inconsistent with the investment rating legend for a continuous period of 30 days, the Research Analyst shall within following 30 days take appropriate measures to make the recommendation consistent with the investment rating legend.

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