

SELL

TP: Rs 1,150 | ▼ 14%

ESCORTS

| Auto Components

| 02 February 2021

Management cautious on margins; maintain SELL

Escorts (ESC) reported Q3FY21 revenue at Rs 20bn (+24% YoY) and above-estimated operating margins at 18%. Management cautioned that its near-term margin performance was at risk due to the sharp rise in input costs and the return of fixed costs as operations normalise. Being a player dominant in North India, higher growth in South and West India led to 140bps market share loss for ESC in Q3. Management believes most pent-up demand has been exhausted as inventories have largely normalised during the last two months. Maintain SELL.

Mayur Milak | Nishant Chowhan, CFA

research@bobcaps.in

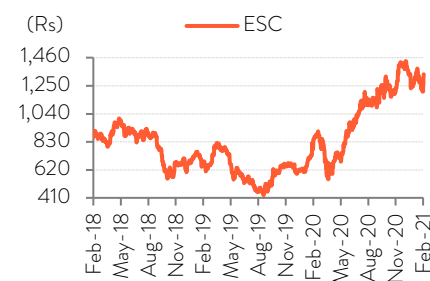
Low-cost inventories boost margins: ESC's Q3 revenue of Rs 20.2bn (+24% YoY) was marginally below our estimate as ASP dipped 2% YoY (flattish ASP expected). Operating margin surprised positively, expanding 500bps YoY to 18% (~300bps above our estimate), owing to above-expected gross margins which we believe could be a function of lower cost raw material inventories and better operating leverage. Given the steep rise in input prices, we expect margins to be under pressure in the near term. Adj. PAT grew 83% YoY to Rs 2.8bn.

Ticker/Price	ESC IN/Rs 1,334
Market cap	US\$ 2.2bn
Shares o/s	123mn
3M ADV	US\$ 32.9mn
52wk high/low	Rs 1,453/Rs 526
Promoter/FPI/DII	40%/20%/10%

Source: NSE

Near-term profitability at risk: Management stated that it would be difficult to take another significant price increase after close to the 2% hike taken in Nov'20. The spike in input cost thus puts near-term margin guidance at risk. ESC expects gross margins to correct over 300bps in the next quarter. Also, channel inventories are nearing normal levels as production ran ahead of retail sales over the last two months.

STOCK PERFORMANCE



Source: NSE

Maintain SELL: We expect ESC to clock a revenue/PAT CAGR of 4%/8% over FY21-FY23. Despite the recent stock price correction, valuations appear to be pricing in most of the positives. We continue to value the stock at 17x Mar'23E EPS and maintain our TP at Rs 1,150. SELL.

KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue (Rs mn)	62,620	58,101	64,382	69,485	75,139
EBITDA (Rs mn)	7,226	6,624	10,111	9,511	10,210
Adj. net profit (Rs mn)	4,789	4,825	7,689	7,370	8,315
Adj. EPS (Rs)	39.1	39.4	62.7	60.1	67.8
Adj. EPS growth (%)	38.0	0.8	59.3	(4.2)	12.8
Adj. ROAE (%)	17.9	15.5	19.9	16.1	15.5
Adj. P/E (x)	34.1	33.9	21.3	22.2	19.7
EV/EBITDA (x)	22.3	24.3	15.9	17.0	15.8

Source: Company, BOBCAPS Research

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FIG 1 – QUARTERLY PERFORMANCE

(Rs mn)	Q3FY21	Q3FY20	YoY (%)	Q2FY21	QoQ (%)	9MFY21	9MFY20	YoY (%)
Volume (nos)	31,562	25,109	25.7	24,441	29.1	74,153	65,910	12.5
Avg. Realisation per Vehicle (Rs)	639,196	650,541	(1.7)	670,881	(4.7)	636,355	664,584	(4.2)
Net Revenues	20,174	16,334	23.5	16,397	23.0	47,188	43,803	7.7
Total Income (A)	20,174	16,334	23.5	16,397	23.0	47,188	43,803	7.7
Operating Expenses:								
Raw materials consumed	13,245	10,916	21.3	10,422	27.1	30,795	29,604	4.0
Employee Expenses	1,358	1,329	2.2	1,256	8.2	3,876	3,808	1.8
Other Expenses	1,930	1,967	(1.8)	1,710	12.9	4,671	5,577	(16.2)
Total Expenditure (B)	16,534	14,212	16.3	13,388	23.5	39,342	38,989	0.9
EBITDA (A-B)	3,641	2,123	71.5	3,009	21.0	7,846	4,814	63.0
Other Income	472	267	76.7	376	25.7	1,146	645	77.8
Depreciation	315	267	18.0	274	15.0	853	768	11.0
EBIT	3,798	2,123	78.9	3,111	22.1	8,139	4,691	73.5
Finance Costs	33	29	12.4	32	1.9	84	126	(33.4)
PBT before excep items	3,765	2,094	79.8	3,079	22.3	8,055	4,565	76.5
Exceptional items	-	-	-	-	-	-	(92)	(100.0)
PBT after excep items	3,765	2,094	79.8	3,079	22.3	8,055	4,657	73.0
Tax expense	959	564	70.1	779	23.0	2,028	1,021	98.6
Reported PAT	2,807	1,531	83.4	2,300	22.0	6,028	3,636	65.8
Adjusted PAT	2,807	1,531	83.4	2,300	22.0	6,028	3,544	70.1
EPS (Rs)	22.9	12.5	83.4	18.8	22.0	49.2	28.9	70.1

Source: Company, BOBCAPS Research

FIG 2 – KEY PARAMETERS

(%)	Q3FY21	Q3FY20	YoY (bps)	Q2FY21	QoQ (bps)	9MFY21	9MFY20	YoY (bps)
Gross margin	34.3	33.2	118	36.4	(209)	34.7	32.4	232
EBITDA margin	18.0	13.0	505	18.4	(31)	16.6	11.0	564
EBIT margin	18.8	13.0	583	19.0	(15)	17.2	10.7	654
PBT margin	18.7	12.8	584	18.8	(11)	17.1	10.4	665
Tax rate	25.5	26.9	(145)	25.3	16	25.2	21.9	325
Adj PAT margin	13.9	9.4	454	14.0	(11)	12.8	8.1	468

Source: Company, BOBCAPS Research

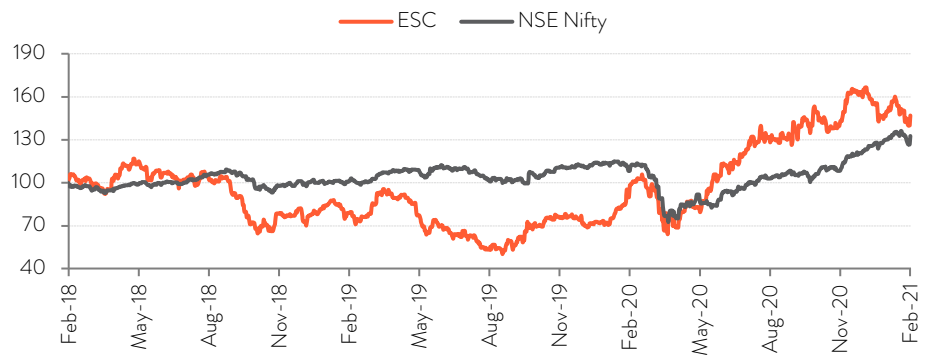
Earnings call highlights

- Last quarter, two-thirds of the tractors sold by ESC were in the >40hp category (62% in Q1FY21), leading to better ASPs. In Q3FY21, the >40hp tractor share reduced, leading to a ~5% QoQ decline in ASP.
- ESC took a price increase of ~2% in mid-November but RM cost inflation is guided to rise by 5% over Q3-Q4FY21.
- Inventory has normalised post festive season from very low levels at the start of the season but still remains below the pre-Covid range. Management expects inventory to remain at current levels.
- Retail demand remains healthy but management believes the pent-up demand has been catered too and new demand will be led by macro factors.
- Discounts are currently lower than normal.
- The company is confident of increasing its export sales run-rate from the current ~500 units/month on the back of its ability to fully meet domestic demand.
- Pent-up demand for commercial tractors (~25% of total tractor sales) has not yet been completely met, per management, and should drive growth in coming quarters. However, as commercial tractors are generally lower HP offerings, this may adversely affect the product mix.

Valuation methodology

We expect ESC to clock a revenue/PAT CAGR of 4%/8% over FY21-FY23. Despite the recent stock price correction, valuations at 20x FY23 EPS appear to be pricing in most of the positives. We continue to value the stock at 17x Mar'23E EPS and maintain our TP at Rs 1,150. Retain SELL.

FIG 3 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

- Above-anticipated volume growth
- Stronger margins in the construction equipment business

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue	62,620	58,101	64,382	69,485	75,139
EBITDA	7,226	6,624	10,111	9,511	10,210
Depreciation	872	1,072	1,143	1,206	1,290
EBIT	7,345	6,528	10,409	9,982	11,247
Net interest income/(expenses)	(195)	(172)	(130)	(130)	(130)
Other income/(expenses)	992	976	1,442	1,677	2,327
Exceptional items	(131)	(103)	0	0	0
EBT	7,019	6,252	10,279	9,852	11,117
Income taxes	2,371	1,535	2,590	2,483	2,801
Extraordinary items	(10)	(5)	0	0	0
Min. int./Inc. from associates	0	0	0	0	0
Reported net profit	4,658	4,722	7,689	7,370	8,315
Adjustments	131	103	0	0	0
Adjusted net profit	4,789	4,825	7,689	7,370	8,315

Balance Sheet

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Accounts payables	11,055	12,929	13,352	14,133	14,710
Other current liabilities	4,156	3,403	3,234	2,685	2,179
Provisions	1,201	1,563	1,256	1,256	1,256
Debt funds	2,810	192	192	192	192
Other liabilities	540	535	535	535	535
Equity capital	1,226	1,226	1,226	1,226	1,226
Reserves & surplus	25,509	29,948	37,507	44,509	52,518
Shareholders' fund	26,735	31,174	38,733	45,735	53,744
Total liabilities and equities	46,497	49,796	57,303	64,536	72,616
Cash and cash eq.	2,433	3,249	1,828	3,125	2,506
Accounts receivables	9,311	7,319	9,701	9,518	10,087
Inventories	8,574	8,834	9,701	9,138	9,470
Other current assets	3,206	3,199	4,016	4,105	4,193
Investments	4,908	7,974	12,974	18,974	25,974
Net fixed assets	16,472	17,024	16,881	17,674	18,384
CWIP	800	1,247	1,200	1,000	1,000
Intangible assets	0	0	0	0	0
Deferred tax assets, net	(517)	(307)	(307)	(307)	(307)
Other assets	1,366	1,310	1,310	1,310	1,310
Total assets	46,553	49,847	57,303	64,536	72,616

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Net income + Depreciation	5,661	5,898	8,832	8,576	9,606
Interest expenses	(195)	(172)	(130)	(130)	(130)
Non-cash adjustments	(992)	(976)	(1,442)	(1,677)	(2,327)
Changes in working capital	(7,856)	3,274	(4,119)	889	(918)
Other operating cash flows	(70)	(158)	0	0	0
Cash flow from operations	(3,452)	7,865	3,142	7,658	6,230
Capital expenditures	(1,609)	(2,071)	(953)	(1,800)	(2,000)
Change in investments	583	(3,066)	(5,000)	(6,000)	(7,000)
Other investing cash flows	992	976	1,442	1,677	2,327
Cash flow from investing	(34)	(4,161)	(4,512)	(6,123)	(6,673)
Equities issued/Others	(30)	(8)	0	0	0
Debt raised/repaid	2,299	(2,618)	0	0	0
Interest expenses	(195)	(172)	(130)	(130)	(130)
Dividends paid	(239)	(260)	(123)	(368)	(306)
Other financing cash flows	461	(170)	(7)	0	0
Cash flow from financing	2,296	(3,228)	(260)	(498)	(436)
Changes in cash and cash eq.	(1,191)	477	(1,630)	1,037	(879)
Closing cash and cash eq.	2,433	3,249	1,828	3,125	2,506

Per Share

Y/E 31 Mar (Rs)	FY19A	FY20A	FY21E	FY22E	FY23E
Reported EPS	39.1	39.4	62.7	60.1	67.8
Adjusted EPS	39.1	39.4	62.7	60.1	67.8
Dividend per share	1.9	1.7	1.0	3.0	2.5
Book value per share	218.1	254.3	316.0	373.1	438.4

Valuations Ratios

Y/E 31 Mar (x)	FY19A	FY20A	FY21E	FY22E	FY23E
EV/Sales	2.6	2.8	2.5	2.3	2.1
EV/EBITDA	22.3	24.3	15.9	17.0	15.8
Adjusted P/E	34.1	33.9	21.3	22.2	19.7
P/BV	6.1	5.2	4.2	3.6	3.0

DuPont Analysis

Y/E 31 Mar (%)	FY19A	FY20A	FY21E	FY22E	FY23E
Tax burden (Net profit/PBT)	68.2	77.2	74.8	74.8	74.8
Interest burden (PBT/EBIT)	95.6	95.8	98.8	98.7	98.8
EBIT margin (EBIT/Revenue)	11.7	11.2	16.2	14.4	15.0
Asset turnover (Revenue/Avg TA)	235.4	187.1	180.3	161.7	148.9
Leverage (Avg TA/Avg Equity)	1.1	1.1	1.0	1.0	1.0
Adjusted ROAE	19.6	16.7	22.0	17.4	16.7

Source: Company, BOBCAPS Research | Note: TA = Total Assets

Ratio Analysis

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
YoY growth (%)					
Revenue	23.8	(7.2)	10.8	7.9	8.1
EBITDA	32.2	(8.3)	52.6	(5.9)	7.3
Adjusted EPS	38.0	0.8	59.3	(4.2)	12.8
Profitability & Return ratios (%)					
EBITDA margin	11.5	11.4	15.7	13.7	13.6
EBIT margin	11.7	11.2	16.2	14.4	15.0
Adjusted profit margin	7.6	8.3	11.9	10.6	11.1
Adjusted ROAE	17.9	15.5	19.9	16.1	15.5
ROCE	18.3	15.9	21.8	17.4	16.7
Working capital days (days)					
Receivables	44	52	48	50	48
Inventory	41	55	53	49	45
Payables	93	114	112	107	104
Ratios (x)					
Gross asset turnover	0.4	0.5	0.4	0.4	0.4
Current ratio	1.4	1.3	1.4	1.4	1.4
Net interest coverage ratio	(37.6)	(37.9)	(80.1)	(76.8)	(86.5)
Adjusted debt/equity	0.1	0.0	0.0	0.0	0.0

Source: Company, BOBCAPS Research

Disclaimer

Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

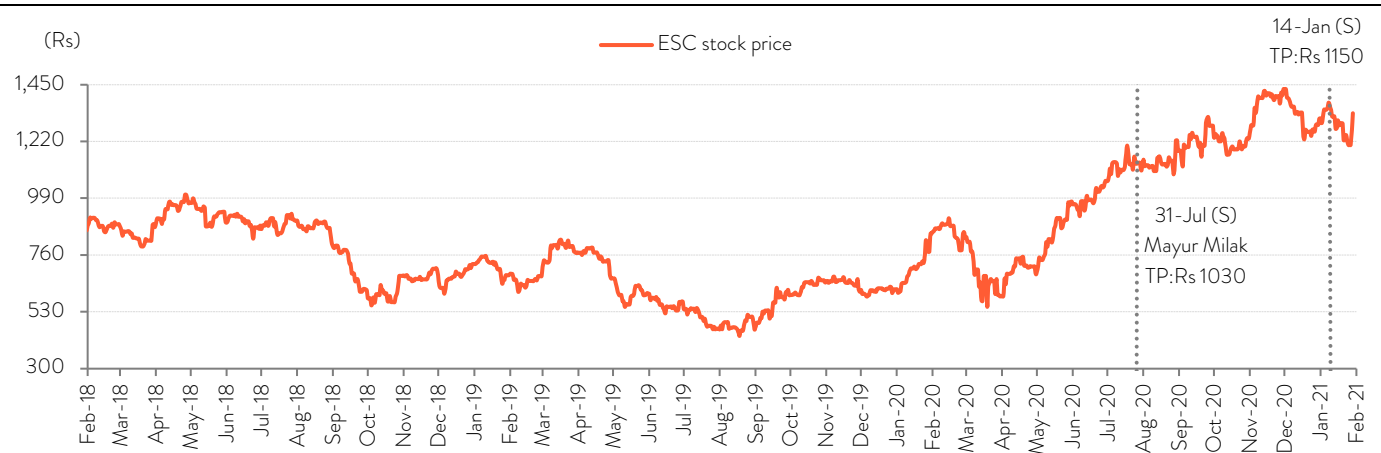
ADD – Expected return from >+5% to +15%

REDUCE – Expected return from -5% to +5%

SELL – Expected return <-5%

Note: Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

RATINGS AND TARGET PRICE (3-YEAR HISTORY): ESCORTS (ESC IN)



B – Buy, A – Add, R – Reduce, S – Sell

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