

BUY

TP: Rs 1,350 | ▲ 16%

ESCORTS

| Auto Components

| 14 May 2021

Fundamentals in place; valuations attractive – upgrade to BUY

Escorts (ESC) reported Q4FY21 revenue of Rs 22bn (+60% YoY) with above-expected ASP. Near-term demand looks hazy due to the Covid wave, but we believe fundamental drivers are in place and expect a 6% volume CAGR for FY21-FY23. The construction equipment and rail businesses are also likely to provide steady support. We raise FY22-FY23 revenue/EPS by 7-8% each and move to a new Mar'22 TP of Rs 1,350 (vs. Rs 1,150), set at 15x P/E. After correcting 18% in three months, the stock is at an attractive 13x FY23E EPS – raise from SELL to BUY.

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Revenue beat but RM cost inflation hits margins: ESC's Q4 revenue of Rs 22bn (+60% YoY) was marginally above our estimate on better-than-expected ASP (+6% QoQ). Operating margin contracted 245bps QoQ to 15.6%, ~70bps short of our estimate owing to a below-expected gross margin. EBITDA/adj. PAT grew 77%/93% YoY to Rs 3.4bn/Rs 2.7bn.

Demand drivers in place: After 26% YoY growth in FY21, we expect the domestic tractor industry to post a 6% volume CAGR over FY21-FY23 off a high base. Growth will be aided by a rising rural economy and aggressive infrastructure spends. ESC's construction and railway businesses (together 20% of revenue) continued to witness steady growth and improving margins in Q4.

Valuations compelling; upgrade to BUY: We raise FY22/FY23 revenue estimates ~8% each on higher realisations (input cost passthrough) and strong growth in other verticals, with EBITDA margin now forecast at 13.6% (vs. 13.5%) on better construction equipment margins. This leads to a ~7% rise in our EPS estimates. We now model for a revenue/EBITDA/PAT CAGR of 7%/–1%/7% over FY21-FY23. We reset our target FY23E P/E from 17x to 15x given the moderate growth outlook but upgrade to BUY as the stock is trading at attractive valuations of 13x FY23E EPS post an ~18% correction since Feb'21.

Ticker/Price	ESC IN/Rs 1,164
Market cap	US\$ 1.9bn
Shares o/s	123mn
3M ADV	US\$ 19.5mn
52wk high/low	Rs 1,468/Rs 799
Promoter/FPI/DII	40%/20%/10%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20A	FY21P	FY22E	FY23E
Total revenue (Rs mn)	62,620	58,101	70,144	75,370	80,770
EBITDA (Rs mn)	7,226	6,624	11,268	10,221	10,960
Adj. net profit (Rs mn)	4,789	4,825	8,724	8,583	9,835
Adj. EPS (Rs)	48.8	49.2	79.1	77.8	89.2
Adj. EPS growth (%)	38.0	0.8	64.4	(1.6)	14.6
Adj. ROAE (%)	17.9	15.5	17.7	15.0	14.8
Adj. P/E (x)	23.8	23.6	14.7	15.0	13.1
EV/EBITDA (x)	19.4	21.2	12.4	12.6	12.3

Source: Company, BOBCAPS Research | P – Provisional

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FIG 1 – QUARTERLY PERFORMANCE

(Rs mn)	Q4FY21	Q4FY20	YoY (%)	Q3FY21	QoQ (%)	FY21	FY20	YoY (%)
Volume (nos)	32,588	20,108	62.1	31,562	3.3	106,741	86,018	24.1
Avg. Realisation per Vehicle (Rs)	678,326	686,632	(1.2)	639,196	6.1	649,169	669,738	(3.1)
Net Revenues	22,105	13,807	60.1	20,174	9.6	69,293	57,610	20.3
Total Income (A)	22,105	13,807	60.1	20,174	9.6	69,293	57,610	20.3
Operating Expenses:								
Raw materials consumed	15,142	8,592	76.2	13,245	14.3	45,937	38,196	20.3
Employee Expenses	1,470	1,295	13.5	1,358	8.2	5,346	5,103	4.7
Other Expenses	2,047	1,975	3.6	1,930	6.0	6,718	7,552	(11.0)
Total Expenditure (B)	18,658	11,862	57.3	16,534	12.8	58,000	50,851	14.1
EBITDA (A-B)	3,447	1,944	77.3	3,641	(5.3)	11,293	6,758	67.1
Other Income	399	278	43.8	472	(15.4)	1,546	923	67.5
Depreciation	304	278	9.6	315	(3.3)	1,157	1,046	10.7
EBIT	3,542	1,944	82.2	3,798	(6.7)	11,682	6,635	76.1
Finance Costs	26	28	(9.5)	33	(21.4)	110	155	(29.0)
PBT before excep items	3,516	1,916	83.5	3,765	(6.6)	11,572	6,481	78.6
Exceptional items	-	-	NA	-	NA	-	(92)	(100.0)
PBT after excep items	3,516	1,916	83.5	3,765	(6.6)	11,572	6,573	76.1
Tax expense	803	512	56.8	959	(16.3)	2,831	1,533	84.6
Reported PAT	2,713	1,404	93.3	2,807	(3.3)	8,741	5,040	73.4
Adjusted PAT	2,713	1,404	93.3	2,807	(3.3)	8,741	4,948	76.7
EPS (Rs)	20.1	11.5	75.8	20.8	(3.3)	65	40	60.7

Source: Company, BOBCAPS Research

FIG 2 – KEY PARAMETERS

(%)	Q4FY21	Q4FY20	YoY (bps)	Q3FY21	QoQ (bps)	FY21	FY20	YoY (bps)
Gross margin	31.5	37.8	(627)	34.3	(285)	33.7	33.7	1
EBITDA margin	15.6	14.1	151	18.0	(245)	16.3	11.7	457
EBIT margin	16.0	14.1	194	18.8	(280)	16.9	11.5	534
PBT margin	15.9	13.9	203	18.7	(276)	16.7	11.2	545
Tax rate	22.8	26.7	(389)	25.5	(263)	24.5	23.3	114
Adj PAT margin	12.3	10.2	211	13.9	(164)	12.6	8.6	403

Source: Company, BOBCAPS Research

Earnings call highlights

- Though macro factors supportive of tractor demand are in place, such as normal monsoon predictions, healthy farm income, financing and government support, near-term demand in H1FY22 is likely to be impacted by the rising Covid-19 infections in rural regions. ESC expects low-single-digit tractor sales growth in FY22, after a healthy 26% YoY increase in FY21.
- The company took a price increase of ~2% in mid-Nov'20 and another 3% hike in Apr'21. RM cost has risen by 8-10% in H2FY21 (over Sep'20 end).
- Dealer inventory has normalised following healthy Q4FY21 sales, though factory inventory has risen given a steady production rate but lower offtake in the retail channel (over two-thirds of dealers are shut due to Covid lockdowns). Management expects factory inventory to remain high until pent-up demand is released when the situation normalises.
- The company is confident of increasing its export sales run-rate from the current ~500 units/month as it is currently able to fully meet domestic demand.
- For FY22, ESC has guided for capex of Rs 3bn-3.5bn towards capacity expansion. Capacity is scheduled to reach 180-190k units per annum by Sep'21, including ~30k at the Kubota plant.

Valuation methodology

We raise our FY22/FY23 revenue estimates for ESC by ~8% each on higher realisations (input cost passthrough) and strong growth in other verticals. EBITDA margin is now forecast at 13.6% (vs. 13.5%) in light of better construction equipment margins (>7% vs. 2% earlier). This translates to a ~7% hike in our FY22/FY23 EPS estimates from Rs 60/Rs 68 to Rs 64/Rs 73. We now model for a revenue/EBITDA/PAT CAGR of 7%/ -1%/7% over FY21-FY23, with ROE and ROCE at ~16% each.

The company is holding 20% of outstanding equity share capital as treasury stocks. Since these shares are not eligible for dividend payout (per company policy), EPS ex-treasury stocks works out to Rs 78/Rs 89 for FY22/FY23.

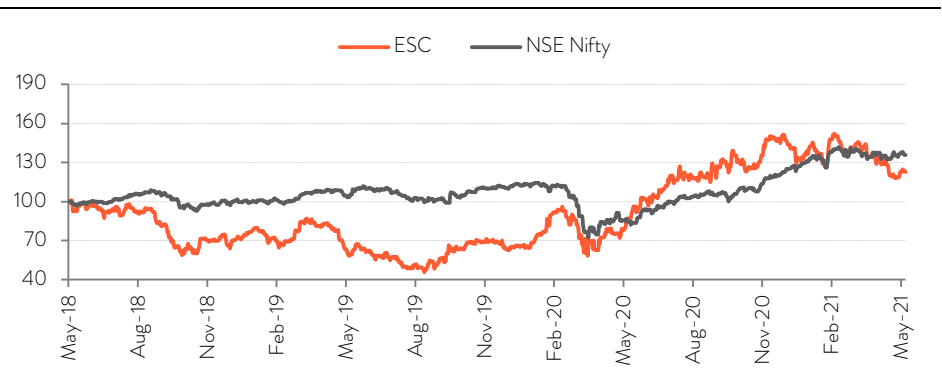
Given our moderate growth outlook over a strong FY21 base, we reset our target FY23E P/E from 17x to 15x, which is in line with the 10-year average multiple (ex-treasury stocks). Factoring in the estimate revision, our Mar'22 target price rises to Rs 1,350 (vs. Rs 1,150). ESC's stock price has corrected ~18% in the last three months and current valuations at 13x FY23E EPS look attractive – upgrade to BUY (from SELL).

FIG 3 – REVISED ESTIMATES

(Rs mn)	New		Old		Change (%)	
	FY22E	FY23E	FY22E	FY23E	FY22E	FY23E
Revenues	75,370	80,770	69,485	75,139	8.5	7.5
EBITDA	10,221	10,960	9,398	10,146	8.8	8.0
OPM (%)	13.6	13.6	13.5	13.5	4bps	7bps
Adj. PAT	8,583	9,835	7,328	8,313	17.1	18.3
EPS (Rs)	64	73	60	68	6.5	7.6

Source: BOBCAPS Research

FIG 4 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

Downside risks to our estimates are:

- below-estimated tractor growth,
- rise in commodity prices, and
- loss of market share.

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21P	FY22E	FY23E
Total revenue	62,620	58,101	70,144	75,370	80,770
EBITDA	7,226	6,624	11,268	10,221	10,960
Depreciation	872	1,072	1,183	1,284	1,400
EBIT	7,345	6,528	11,689	11,605	13,278
Net interest income/(expenses)	(195)	(172)	(133)	(130)	(130)
Other income/(expenses)	992	976	1,604	2,668	3,718
Exceptional items	(131)	(103)	0	0	0
EBT	7,019	6,252	11,555	11,475	13,148
Income taxes	2,371	1,535	2,832	2,892	3,313
Extraordinary items	(10)	(5)	0	0	0
Min. int./Inc. from associates	0	0	0	0	0
Reported net profit	4,658	4,722	8,724	8,583	9,835
Adjustments	131	103	0	0	0
Adjusted net profit	4,789	4,825	8,724	8,583	9,835

Balance Sheet

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21P	FY22E	FY23E
Accounts payables	11,055	12,929	11,954	13,217	14,463
Other current liabilities	4,156	3,403	3,980	4,352	3,044
Provisions	1,201	1,563	2,958	2,958	2,958
Debt funds	2,810	192	17	17	17
Other liabilities	540	535	837	837	837
Equity capital	1,226	1,226	1,348	1,348	1,348
Reserves & surplus	25,509	29,948	48,036	55,946	65,106
Shareholders' fund	26,735	31,174	49,385	57,294	66,454
Total liabilities and equities	46,497	49,796	69,131	78,675	87,774
Cash and cash eq.	2,433	3,249	13,809	2,237	1,007
Accounts receivables	9,311	7,319	6,576	7,847	8,409
Inventories	8,574	8,834	7,182	9,292	9,737
Other current assets	3,206	3,199	2,298	5,219	5,441
Investments	4,908	7,974	19,380	32,380	40,380
Net fixed assets	16,472	17,024	18,197	19,913	21,013
CWIP	800	1,247	412	500	500
Intangible assets	0	0	0	0	0
Deferred tax assets, net	(517)	(307)	(233)	(233)	(233)
Other assets	1,366	1,310	1,520	1,520	1,520
Total assets	46,553	49,847	69,140	78,675	87,774

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21P	FY22E	FY23E
Net income + Depreciation	5,661	5,898	9,906	9,868	11,234
Interest expenses	(195)	(172)	(133)	(130)	(130)
Non-cash adjustments	(992)	(976)	(1,604)	(2,668)	(3,718)
Changes in working capital	(7,856)	3,274	4,386	(4,669)	(1,290)
Other operating cash flows	(70)	(158)	0	0	0
Cash flow from operations	(3,452)	7,865	12,555	2,401	6,096
Capital expenditures	(1,609)	(2,071)	(1,521)	(3,088)	(2,500)
Change in investments	583	(3,066)	(11,407)	(13,000)	(8,000)
Other investing cash flows	992	976	1,604	2,668	3,718
Cash flow from investing	(34)	(4,161)	(11,324)	(13,420)	(6,782)
Equities issued/Others	(30)	(8)	123	0	0
Debt raised/repaid	2,299	(2,618)	(175)	0	0
Interest expenses	(195)	(172)	(133)	(130)	(130)
Dividends paid	(239)	(260)	(1,011)	(674)	(674)
Other financing cash flows	461	(170)	10,302	0	0
Cash flow from financing	2,296	(3,228)	9,105	(804)	(804)
Changes in cash and cash eq.	(1,191)	477	10,336	(11,823)	(1,490)
Closing cash and cash eq.	2,433	3,249	13,809	2,237	1,007

Per Share

Y/E 31 Mar (Rs)	FY19A	FY20A	FY21P	FY22E	FY23E
Reported EPS	48.8	49.2	79.1	77.8	89.2
Adjusted EPS	48.8	49.2	79.1	77.8	89.2
Dividend per share	1.9	1.7	7.5	5.0	5.0
Book value per share	218.1	254.3	366.3	424.9	492.9

Valuations Ratios

Y/E 31 Mar (x)	FY19A	FY20A	FY21P	FY22E	FY23E
EV/Sales	2.2	2.4	2.0	1.7	1.7
EV/EBITDA	19.4	21.2	12.4	12.6	12.3
Adjusted P/E	23.8	23.6	14.7	15.0	13.1
P/BV	5.3	4.6	3.2	2.7	2.4

DuPont Analysis

Y/E 31 Mar (%)	FY19A	FY20A	FY21P	FY22E	FY23E
Tax burden (Net profit/PBT)	68.2	77.2	75.5	74.8	74.8
Interest burden (PBT/EBIT)	95.6	95.8	98.9	98.9	99.0
EBIT margin (EBIT/Revenue)	11.7	11.2	16.7	15.4	16.4
Asset turnover (Revenue/Avg TA)	235.4	187.1	170.7	139.1	128.8
Leverage (Avg TA/Avg Equity)	1.1	1.1	1.0	1.0	1.0
Adjusted ROAE	19.6	16.7	21.7	16.1	15.9

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

Ratio Analysis

Y/E 31 Mar	FY19A	FY20A	FY21P	FY22E	FY23E
YoY growth (%)					
Revenue	23.8	(7.2)	20.7	7.5	7.2
EBITDA	32.2	(8.3)	70.1	(9.3)	7.2
Adjusted EPS	38.0	0.8	64.4	(1.6)	14.6
Profitability & Return ratios (%)					
EBITDA margin	11.5	11.4	16.1	13.6	13.6
EBIT margin	11.7	11.2	16.7	15.4	16.4
Adjusted profit margin	7.6	8.3	12.4	11.4	12.2
Adjusted ROAE	17.9	15.5	17.7	15.0	14.8
ROCE	18.3	15.9	21.5	16.0	15.8
Working capital days (days)					
Receivables	44	52	36	35	37
Inventory	41	55	42	40	43
Payables	93	114	98	88	91
Ratios (x)					
Gross asset turnover	0.4	0.5	0.4	0.4	0.4
Current ratio	1.4	1.3	1.6	1.2	1.2
Net interest coverage ratio	(37.6)	(37.9)	(87.6)	(89.3)	(102.1)
Adjusted debt/equity	0.1	0.0	0.0	0.0	0.0

Source: Company, BOBCAPS Research

Disclaimer

Recommendation scale: 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)

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



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

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