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Date: 18/05/2020
Company: Escorts Ltd.
Industry: Commercial Vehicle

Result Snapshot

Amt. in Rs. Crs.	Q4FY20	Q3FY20	Q-o-Q(%)	Q4FY19	Y-o-Y(%)
Revenue	1385.7	1650.2	-16.0%	1649.1	-16.0%
Other Income	30.3	27.9		19.6	
Total Income	1416.0	1678.2	-15.6%	1668.7	-15.1%
EBITDA	182.1	213.0	-14.5%	184.9	-1.5%
EBIDTA (%)	13.1%	12.9%		11.2%	
EBIT	153.7	185.7	-17.2%	162.4	-5.4%
Profit/Loss in Association	-1.5	1.1		-1.4	
PBT	179.2	211.1	-15.1%	172.8	3.7%
PAT	127.7	154.8	-17.5%	116.4	9.7%
PAT%	9.2%	9.4%		7.1%	

Result / Con-call Highlights:

1) Result Update:

Escorts reported revenue of Rs. 1,385 cr in Q4 FY20, down 16% Y-o-Y basis mainly on account of nationwide lock down as significant number of sales materialize during the Navratra festival. The company reported EBITDA of Rs. 182 cr with EBITDA margins at 13.1% in Q4 FY20. EBITDA margins expanded by 190 bps on Y-o-Y basis due to one off gain and softening of commodity prices. PAT came in at Rs. 127 cr up from Rs. 116 cr reported in corresponding quarter last year. The company also declared a final dividend of Rs. 2.5 per share during the quarter.

2) Business Update:

The Standalone business depicts company's main business of farming and construction equipment. Escort's consolidated numbers which include 6 subsidiaries, 1 associate and 3 JVs are all investments done by the company which comprise of interest in the agriculture machinery and construction equipment segment. For a better understanding of the business, all the numbers given below are on standalone basis.

Standalone (Rs. Cr)	Q4 FY20	Q3 FY20	Q-o-Q	Q4 FY19	Y-o-Y
Revenue	1380.7	1633.4	-15.5%	1631.7	-15.4%
Other Income	27.8	26.7		17.3	
Total Income	1408.5	1660.2	-15.2%	1649.0	-14.6%
EBITDA	194.4	212.3	-8.4%	189.8	2.5%
EBITDA %	14.1%	13.0%		11.6%	
EBIT	166.7	185.6	-10.2%	168.0	-0.8%
PBT	191.6	209.4	-8.5%	177.8	7.7%
PAT	140.4	153.1	-8.3%	121.4	15.7%
PAT %	10.2%	9.4%		7.4%	

Result / Con-call Highlights: (Continued)

EAM (Escorts Agri Machinery) – EAM segment contributes around 77% of Q4 FY20 standalone revenue. Segmental revenue stood at Rs. 1,058 cr with EBIT Margins of 15.8%, up by 270 bps as compared to 13.1% in the corresponding period last year due to softening commodity prices and one off operational benefit. An expansion in margin of around 200 bps came from inventory related cost absorption due to the lockdown.

Domestic Sales for EAM segment stood at 19,122 units which were down 20.7% Y-o-Y basis and down 21.1% on Q-o-Q basis whereas; export sales for EAM segment stood at 986 units up 3.8% on Y-o-Y basis. As significant number of sales happens during the Navratra festival, the company generally keeps 3x inventory compared to the normal inventory levels. Due to the nationwide lockdown, the anticipated sales could not be executed and Escort's domestic tractor volume de-grew by 11.9% in FY20 compared to the industry de-growth of 10% in FY20. We believe that the repercussion for Escort was higher than the industry mainly due to the company's focus on North and Central region where the industry de-grew by 19% compared to its growth of 3% registered in South and West region in FY20.

The built up in inventory during the last quarter has helped the company survive the lockdown period. The present inventory would help the company sustain until June end. As the company restarted their production facility on 12th May 2020, it is currently running at 20% utilization levels. Management has guided to reach ~50% utilization level by mid-June and return to normalcy by July thereby not affecting their sales.

We believe volumes will again pick up Q3 onwards based on good reservoir levels across India and healthy growth in Rabi crop sowing. Moreover, the management is more worried about the supply side issue rather than the demand side problems. On the supply side, there are about 300 suppliers that help built a tractor. Any delay in their production due to the extended lockdown would further delay Escorts normalcy plans. On the demand side, management has already guided that they are seeing 50% of their normal May demand with only 65% of their dealership operational. At this juncture, supply side issues are still manageable compared to demand side issues which generally take years to recover.

ECE (Escorts Construction Equipment) – ECE segment contributes around 15% of Q4 FY20 standalone revenue. The construction equipment industry has witnessed a slowdown in FY20 while showing some signs of revival in January 2020. However, due to the lockdown we believe this segment will remain subdued showing no growth. Even if the lockdown is lifted, monsoon season would set in thereby delaying most of the projects. A key demand driver for ECE segment would be pick-up of road construction sector. As Escorts is a small player in the construction equipment industry, we believe it would be difficult to gain market share given the presence of established players.

RED (Railway Equipment Division) – RED segment contributes around 7% of the Q4 FY20 standalone revenue. Escort's order book in RED segment stood at Rs. 400 cr in Q4 FY20 executable in 12 – 15 months. The company does not face any receivable problem and has good traction in demand. We believe this segment would continue to do well but margins may come under pressure as the introduction of new products may have a higher import content in the short term.

3) Outlook:

Domestic tractor industry is a cyclical industry going through the recovery phase of the industry cycle. Good reservoir levels along with healthy signs of Rabi crop sowing are an ideal arrangement for pick up in tractor sales and we expect Escorts to be the biggest beneficiary of the same. At CMP of Rs. 810 Escorts trades at 21x FY20 earnings of Rs 471.7 cr. Also, the impact of Covid-19 on sparsely populated agrarian industry is significantly constrained at the same time a good crop and unhampered consumption of the produce shall aid rural economy and keep the agriculture ancillary business like Escorts fueled. At current valuation, with the current capital market situation we expect intermediate corrections in the stock to around 17x trailing valuations; we assign an **Accumulate** rating to the stock and recommend to buy on dips below Rs. 693.

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