

Escorts (ESCORT)

Rs 204

WHAT'S CHANGED...

PRICE TARGET Changed from Rs 193 to Rs 221
 EPS (SY10E) Changed from Rs 12.3 to Rs14.0
 EPS (SY11E) Changed from Rs 15 to Rs17.7
 RATING..... Unchanged

Financials zoom as agro revenue jumps...

Escorts reported its standalone Q3SY10 results that were marginally below our estimates. The topline improved 20% QoQ and 38.5% YoY to Rs 806.2 crore (I-direct estimate of Rs 837.4crore) on the back of higher tractor sales and improved realisations. Escorts maintained its margin sequentially incurring a slight drop of 12 bps to 9.66% on the back of a reduction in other expenses even in the face of rising input costs. The PBT performance was strong with 26.5% QoQ and 66.8% YoY growth at Rs 69 crore (I-direct estimate of Rs 68.8 crore) though the PAT was subdued in comparison, due to higher provisioning for taxes.

Highlights of the quarter

Escorts recorded tractor sales of 17,919 units as compared to 12,889 units over the same period last quarter. The company also launched a new 27 HP tractor variant in the Powertrac category. It also introduced a backhoe loader – DIGMAX in the construction equipment segment. However, the railway segment has witnessed shrinkage of 15.0% YoY and 20.0% QoQ while the auto ancillary segment has grown by a healthy 39.1% YoY. It has won an export order of Rs 185 crore consisting of 1,400 premium Farmtrac tractors (60% order value) and rest of other farm equipment.

Stable EBITDA margin, albeit rising input cost

The raw material cost increased from 67.0% of net sales in Q3SY09 to 72.0% in Q3SY10 with rising rubber and steel prices. However, other expenses have declined from 13.7% in Q3SY09 to 11.8% in Q3SY10 due to various cost rationalisation measures. This has aided the company to arrest the fall in EBITDA margin to only 12 bps.

Valuation

The stock is currently trading at Rs 204, 9.4x SY11E consolidated EPS of Rs 21.6. We value the standalone business at 10.5x SY11E EPS of Rs 17.7 to arrive at a valuation of Rs 186 per share while ECEL is valued at Rs 35 per share (9x SY11E EPS of Rs 3.9). Our SOTP target price of Rs 221 implies an 8% upside potential. Hence, we rate the stock as **ADD**.

Exhibit 1: Financial Performance (Standalone)

(Rs Crore)	Q3SY10	Q3SY10E	Q3SY09	Q2SY10	QoQ (Chg %)	YoY (Chg %)
Net Sales	806.2	837.4	582.0	671.7	20.0	38.5
EBITDA	78.3	83.3	63.3	66.1	18.5	23.8
EBITDA Margin (%)	9.7	9.9	10.8	9.8	-1.3	-10.9
Depreciation	9.6	10.5	11.9	12.4	-22.7	-19.7
Interest	-0.3	4.0	9.9	-0.9	NC	-102.8
Reported PAT	46.5	55.7	22.2	41.5	12.1	109.3
EPS (Rs)	4.9	5.9	2.4	4.7	4.8	101.3

SY~September year end

Source: Company, ICICIdirect.com Research

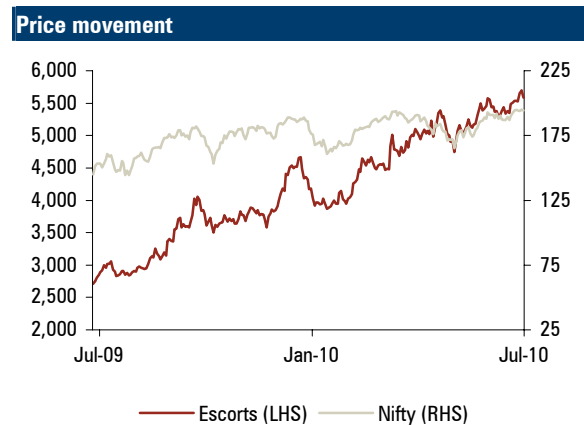
Rating matrix	
Rating	: Add
Target	: Rs 221
Target Period	: 12 months
Potential Upside	: 8%

Key Financials (Standalone)			
(Rs Crore)	SY09	SY10E	SY11E
Net Sales	2157.8	2805.7	3257.1
EBITDA	177.2	261.3	313.8
Net Profit	89.7	142.1	179.5
EPS	9.9	14.0	17.7

SY~September year end

Valuation summary			
	SY09	SY10E	SY11E
PE (x)	20.7	14.6	11.6
Target PE (x)	22.3	15.7	12.5
EV to EBITDA (x)	13.2	9.4	7.4
Price to book (x)	1.4	1.4	1.2
RoNW (%)	8.5	9.8	11.1
RoCE (%)	10.6	13.2	14.9

Stock data	
Market Capitalisation	Rs 1,927.9crore
Debt (FY09)	Rs264.2crore
Cash (FY09)	Rs164.8crore
EV	Rs2172crore
52 week H/L	212.3 / 60
Equity capital	Rs101.4crore
Face value	Rs 10
MF Holding (%)	15.90%
RI Holding (%)	17.80%



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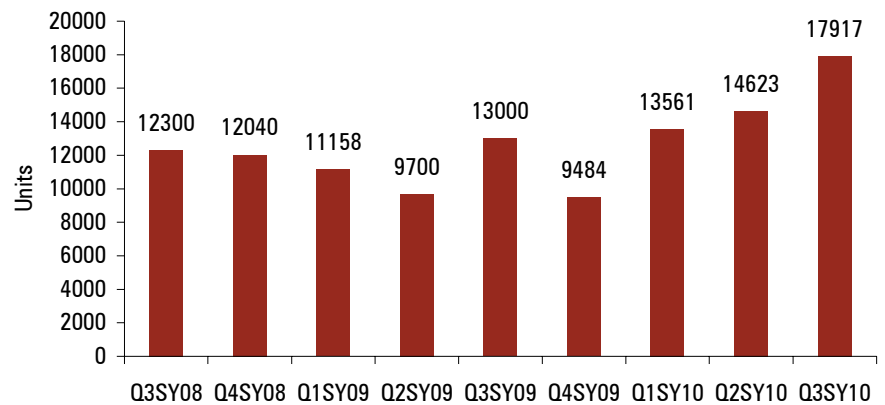
Scenario going ahead

The management has guided about expanding capacity in the agri machinery business in addition to continuous investment in development of new technology. The company plans to launch six to seven new products in the segment in the near future. Escorts has also tied up with implement and attachment manufactures to provide farming solutions across various stages of the cropping cycles as well as non-farm applications.

In Q3FY10, Escorts has bailed out one of its group companies Escorts Finance by issuing 7.1mn shares to a Hardship Committee formed to repay off the liabilities of fixed deposit holders of Escorts Finance Ltd thereby resulting in 7% equity dilution. Pursuant to the order passed by the high court, the company has issued two tranches of equity; issuing 500,000 shares and 6.6mn shares at a premium of INR 84/share on May 14, 2010, and at a premium of INR 166.15/per share on May 31, 2010, respectively.

Tractor volumes have seen a significant upward movement with the new product launches in the 41-50 HP segment Powertrac and Farmtrac variants

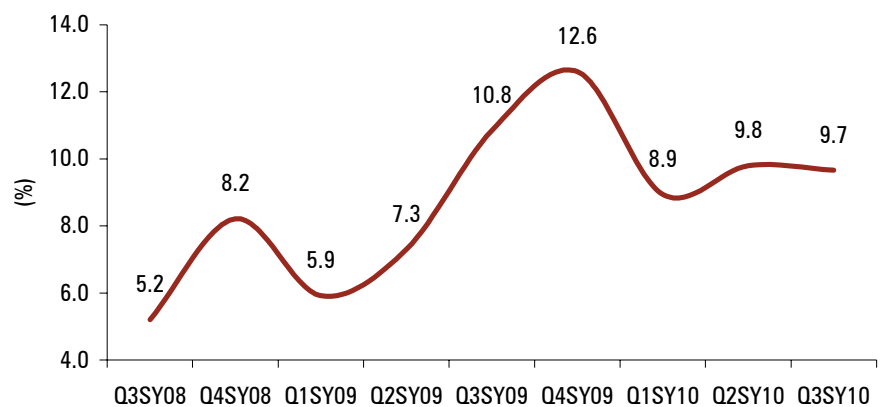
Exhibit 2: Tractor sales on an uptrend



Source: Company, ICICIdirect.com Research

Escorts has been able to maintain margins on a sequential basis even as higher input costs are causing a decline in profitability across the industry

Exhibit 3: Stable EBITDA margin



Source: Company, ICICIdirect.com Research

Outlook & Valuation

Outlook

Escorts has exhibited an encouraging trend during this quarter with tractor sales reaching 17,917 units, a 39% YoY growth. We expect the company to continue with its growth momentum and end the current year with total sales of 63,745 units on the back of strong monsoon led agricultural demand. The recent launch of Powertrac 429 in the 27 HP segment is expected to aid tractor segment sales. Also, the recent price hike in the tractor segment is expected to contribute positively to the margin. The auto ancillary segment is also expected to post a healthy growth in SY10 on the back of rising demand from OEMs.

Valuation

The stock is currently trading at Rs 204, 9.4x SY11E consolidated EPS of Rs 21.6. In light of the robust tractor sales in Q3SY10 and rising demand in the agriculture segment, we have upwardly revised our standalone EPS estimates for SY10E and SY11E by 7.7% and 10.5%, respectively. We have valued the standalone business at 10.5x SY11E fully diluted EPS of Rs 17.7 to arrive at a valuation of Rs 186 per share while ECEL has been valued at Rs 35 per share (9x SY11E EPS of Rs 3.9). Our target price of Rs 221 implies an 8% upside potential over the current market price. Hence, we rate the stock as **ADD**.

Exhibit 4: SOTP Valuation

Company	FY11E EPS (Rs)	Multiple	Value (Rs)
Escorts	17.7	10.5	186
ECEL	3.9	9	35
Total value (Rs)			221
CMP (Rs)			204.4
Potential upside (%)			7.9

Source: Company, ICICIdirect.com Research

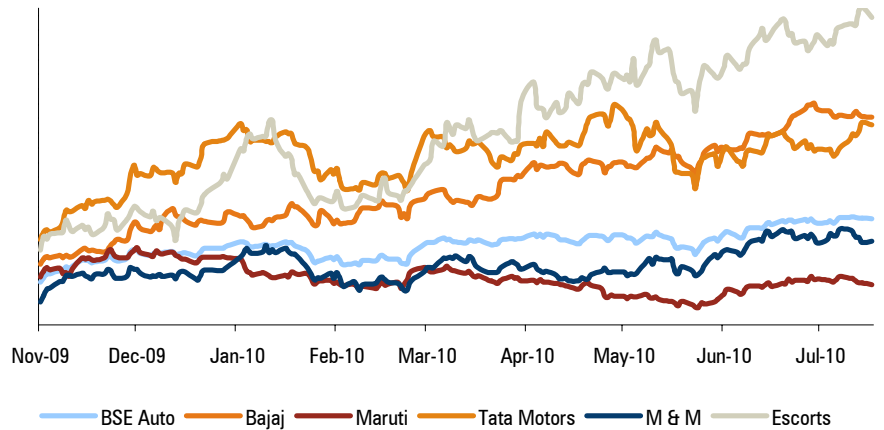
Exhibit 5: ICICIdirect.com Research coverage universe

Tata Motors					Sales (Rs cr)	EPS (Rs)	PE(x)	EV/E (x)*	RoNW (%)	RoCE (%)
Idirect Code	TELCO	CMP	825	FY09	25,354.1	13.4	61.7	55.9	6.9	7.1
		Target	877	FY10E	35,373.8	39.3	21.0	17.4	15.4	12.2
Mcap (Rs cr)	42432.3	% Upside	6.2	FY11E	38,958.3	51.7	16.0	15.2	16.6	11.0
				FY12E	45,870.6	57.1	14.5	13.7	16.1	11.1
Maruti Suzuki					Sales (Rs cr)	EPS (Rs)	PE(x)	EV/E (x)*	RoNW (%)	RoCE (%)
Idirect Code	MARUTI	CMP	1364	FY09	20,775.6	40.3	33.9	19.6	13.3	18.5
		Target	1614	FY10E	31,684.5	84.0	16.2	9.5	23.1	33.3
Mcap (Rs cr)	39423.9	% Upside	18.3	FY11E	34,957.7	94.0	14.5	8.7	21.0	28.9
				FY12E	37,714.7	101.8	13.4	7.9	18.8	26.4
M&M					Sales (Rs cr)	EPS (Rs)	PE(x)	EV/E (x)*	RoNW (%)	RoCE (%)
Idirect Code	MAHMAH	CMP	607	FY09	13,093.7	15.3	39.6	34.3	17.4	9.9
		Target	675	FY10E	18,602.1	36.9	15.9	12.2	31.9	25.8
Mcap (Rs cr)	33117.9	% Upside	11.2	FY11E	22,165.9	36.8	16.5	10.9	23.9	25.6
				FY12E	25,487.6	41.8	14.5	9.6	22.1	25.8
Bajaj Auto					Sales (Rs cr)	EPS (Rs)	PE(x)	EV/E (x)*	RoNW (%)	RoCE (%)
Idirect Code	BAAUTO	CMP	2,401	FY09	8,696.2	44.4	54.1	34.1	40.1	38.5
		Target	2,567	FY10E	11,810.6	115.4	18.2	14.1	72.4	68.1
Mcap (Rs cr)	34742.0	% Upside	6.9	FY11E	15,244.7	143.1	16.8	12.9	57.9	62.0
				FY12E	17,092.8	171.1	14.0	10.6	49.0	38.5
Escorts*					Sales (Rs cr)	EPS (Rs)	PE(x)	EV/E (x)*	RoNW (%)	RoCE (%)
Idirect Code	ESCORT	CMP	204	FY08	1,998.0	1.3	156.2	28.1	-1.6	7.0
		Target	221	FY09	2,162.8	9.9	20.7	13.2	8.5	10.6
Mcap (Rs cr)	1927.9	% Upside	7.9	FY10E	2,830.7	14.0	14.6	9.4	9.8	13.2
				FY11E	3,282.1	17.7	11.6	7.4	11.1	14.9
Apollo Tyres					Sales (Rs cr)	EPS (Rs)	PE(x)	EV/E (x)*	RoNW (%)	RoCE (%)
Idirect Code	APOTYR	CMP	63	FY09	4,070.4	2.1	30.1	10.8	7.8	14.6
		Target	85	FY10E	5,036.8	8.2	7.7	4.8	26.9	30.8
Mcap (Rs cr)	3099.6	% Upside	33.8	FY11E	5,875.8	8.1	7.9	4.5	21.3	24.1
				FY12E	6,376.1	8.4	7.6	4.4	18.5	21.2
Automotive Axle*					Sales (Rs cr)	EPS (Rs)	PE(x)	EV/E (x)*	RoNW (%)	RoCE (%)
Idirect Code	AUTAXL	CMP	469	FY08	751.9	39.6	11.8	6.5	37.7	40.4
		Target	525	FY09	267.2	3.6	131.6	22.6	3.1	6.3
Mcap (Rs cr)	708.4	% Upside	12.0	FY10E	539.9	24.8	18.9	9.7	19.8	24.7
				FY11E	641.3	29.8	15.7	7.7	20.1	26.9
Balkrishna Industries					Sales (Rs cr)	EPS (Rs)	PE(x)	EV/E (x)*	RoNW (%)	RoCE (%)
Idirect Code	BALIND	CMP	582	FY09	1,252.5	36.0	16.1	6.7	15.9	20.9
		Target	689	FY10E	1,394.4	107.9	5.4	7.1	37.0	28.6
Mcap (Rs cr)	1125.3	% Upside	18.4	FY11E	1,622.0	122.1	4.8	4.7	30.6	24.2
				FY12E	1,862.7	125.3	4.6	5.0	24.4	19.7
Bharat Forge					Sales (Rs cr)	EPS (Rs)	PE(x)	EV/E (x)*	RoNW (%)	RoCE (%)
Idirect Code	BHAFOR	CMP	336	FY09	2,057.6	4.3	77.8	20.1	6.5	11.8
		Target	352	FY10E	1,856.4	5.7	59.0	20.2	8.4	9.1
Mcap (Rs cr)	7490.5	% Upside	4.6	FY11E	2,521.3	9.5	35.4	14.2	11.5	11.9
				FY12E	3,070.1	12.8	26.2	12.4	12.5	12.6
JK Tyres					Sales (Rs cr)	EPS (Rs)	PE(x)	EV/E (x)*	RoNW (%)	RoCE (%)
Idirect Code	JKIND	CMP	168	FY09	4,934.1	4.6	36.1	6.3	3.5	12.5
		Target	211	FY10E	3,678.0	39.9	4.2	5.0	25.2	17.9
Mcap (Rs cr)	688.4	% Upside	25.9	FY11E	4,338.8	43.7	3.8	4.6	22.1	16.5
				FY12E	4834.9	52.8	3.2	4.1	21.6	16.7
Subros					Sales (Rs cr)	EPS (Rs)	PE(x)	EV/E (x)*	RoNW (%)	RoCE (%)
Idirect Code	SUBROS	CMP	48	FY09	694.4	2.2	21.9	6.1	7.6	12.2
		Target	61	FY10E	875.6	3.9	12.3	4.1	12.1	16.5
				FY11E	931.0	5.6	8.5	3.0	15.5	20.9
Mcap (Rs cr)	289.1	% Upside	25.9	FY12E	1,081.7	6.7	7.1	2.5	16.2	22.6

ICICIdirect.com Universe price movement vis-à-vis BSE Auto index

The chart compares the movement of OEM stocks in the ICICIdirect.com Universe with the BSE Auto index, thereby reflecting the degree of mimicking of the index

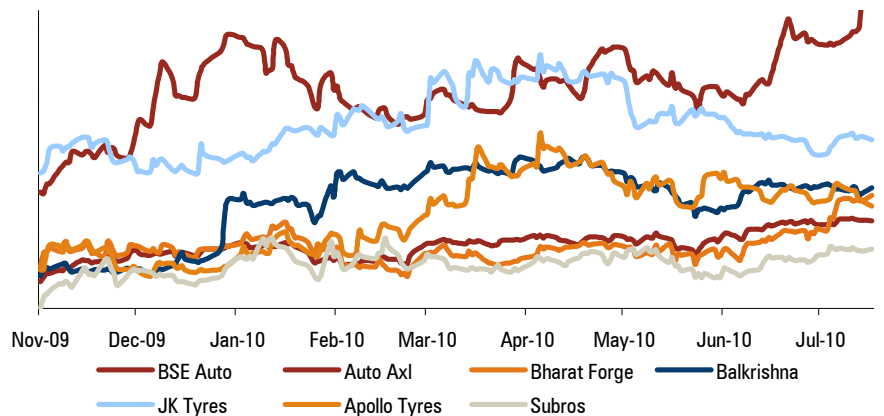
Since mid February 2010, Bajaj Auto, Tata Motors and Escorts have outperformed and Maruti Suzuki has underperformed in comparison to the index by being divergent on the upside and downside, respectively

Exhibit 6: OEM comparison with BSE Auto


Source: Company, ICICIdirect.com Research

The chart compares the movement of auto ancillary stocks in the ICICIdirect.com universe with the BSE Auto index

The volatile nature of smaller ancillary companies is reflected. These have met with numerous fluctuations with the exception of larger market capitalisation companies like Bharat Forge, which mimic the index greatly

Exhibit 7: Ancillaries comparison with BSE Auto


Source: Company, ICICIdirect.com Research

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