

August 10, 2011

| | |
|---------------------------|----------------------|
| Reco | Previous Reco |
| Not Rated | NA |
| CMP | Target Price |
| Rs 79 | Not Rated |
| EPS change FY 12E/13E (%) | NA |
| Target Price change (%) | NA |
| Nifty | 5,073 |
| Sensex | 16,858 |

Price Performance

| (%) | 1M | 3M | 6M | 12M |
|---------------|------|------|------|------|
| Absolute | (27) | (39) | (19) | (58) |
| Rel. to Nifty | (20) | (34) | (17) | (55) |

Source: Bloomberg

Relative Price Chart



Source: Bloomberg

Stock Details

| | |
|-----------------------------|-------------|
| Sector | Automobiles |
| Bloomberg | ESC@IN |
| Equity Capital (Rs mn) | 1056 |
| Face Value(Rs) | 10 |
| No of shares o/s (mn) | 106 |
| 52 Week H/L | 246/78 |
| Market Cap (Rs bn/USD mn) | 8/184 |
| Daily Avg Volume (No of sh) | 1094665 |
| Daily Avg Turnover (US\$m) | 2.7 |

Shareholding Pattern (%)

| | Jun-11 | Mar-11 | Dec-10 |
|--------------|--------|--------|--------|
| Promoters | 26.8 | 26.8 | 26.8 |
| FII/NRI | 30.4 | 31.8 | 31.0 |
| Institutions | 15.9 | 15.9 | 16.8 |
| Private Corp | 5.7 | 5.3 | 6.1 |
| Public | 21.3 | 20.2 | 19.4 |

Source: Capitaline

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Regional disparity affects volumes, Not Rated

- Sharp drop in volumes 21%/20% YoY /QoQ results in EBITDA margins declining by 500/180 bps YoY/QoQ to ~4.6%. Margins are lowest in last 12 quarters (since Sep 2008)
- Volumes affected by regional disparity due higher growth in Southern markets, where Escorts is a weak player. North and Central region witnessed subdued demand
- Expect margins to bottom out with up tick in volumes and benefits of price hike and lower commodity prices (lag of ~1.5month)
- Stock looks attractive with P/BV of 0.7x, net DE of 0.1x on SY10 financials after adjusting for revaluation reserve. However, volumes and margins up tick will be the key trigger

Net Sales – Volumes decline 21%

Net sales at Rs 7.4bn declined strongly by ~9% YoY and ~18% QoQ. Key disappointment was ~21% YoY decline in tractor volumes as compared with ~20% YoY growth in M&M tractor sales. Average selling price at Rs 470,461 (up 13% YoY, 5% QoQ) offset the poor volumes performance in the tractor segment and supported standalone top line. Company benefited from price hike of ~Rs 16,000 per tractor taken during March 2011.

| Volumes Sold | Q3SY10 | Q4SY10 | Q1SY11 | Q2SY11 | Q3SY11 |
|--------------|--------|--------|--------|--------|--------|
| Tractors | 17,917 | 13,985 | 16,333 | 17,672 | 14,212 |
| % YoY | 39 | 15 | 20 | 21 | -21 |

Source: Company, Emkay research

EBIDTA at Rs 343mn– Weak farm equipment business impacts margins

EBIDTA margins nosedived to 4.6% at Rs 343mn (-500 bps YoY, -180 bps QoQ). This was the lowest ever margins recorded in the past 3 years due to sharp drop in volumes. RM to sales increased by 330 bps YoY and 50 bps QoQ to 71.3%. Staff cost declined ~2% YoY to Rs 844mn. Other expenses at Rs 937mn was also lower by ~2% YoY. Expect performance to improve going ahead as input costs have stabilized and benefits to accrue with a lag effect of 1-2 months.

APAT at Rs 122mn

APAT at Rs 122mn posted a strong decline of ~74% YoY and ~84% QoQ primarily led by weak operating performance. Interest costs at Rs 76mn were also higher as compared to Rs 62 mn in Q2 and Rs -3mn in Q3SY10.

Financial Snapshot

| YE- | Net | EBITDA | EPS | EPS | RoE | EV/ | EV/ | EV/ | EV/ | |
|------|--------|--------|-----|-------|-------|-------|-------|---------|--------|------|
| Mar | Sales | (Core) | (%) | APAT | (Rs) | % chg | (%) | P/E | EBITDA | P/BV |
| SY07 | 20,756 | 700 | 3.4 | -13 | (0.8) | - | (0.6) | (105.7) | 14.1 | 1.1 |
| SY08 | 19,923 | 663 | 3.3 | 14 | 1.3 | - | 1.0 | 62.1 | 15.3 | 1.0 |
| SY09 | 21,578 | 1,636 | 7.6 | 820 | 9.9 | 661.5 | 6.8 | 8.2 | 5.0 | 0.8 |
| SY10 | 27,457 | 1,868 | 6.8 | 1,282 | 13.4 | 36.0 | 13.2 | 6.0 | 4.9 | 0.7 |

Source: Company, Emkay Research

Quarterly Summary

| Rs mn | Q3SY10 | Q4SY10 | Q1SY11 | Q2SY11 | Q3SY11 | YoY (%) | QoQ (%) | YTDSY11 | YTDSY10 |
|-----------------------------|--------------|--------------|--------------|--------------|--------------|---------------|---------------|---------------|---------------|
| Revenue | 8,109 | 6,744 | 8,377 | 9,018 | 7,396 | (8.8) | (18.0) | 20,903 | 24,791 |
| Expenditure | 7,325 | 6,395 | 7,939 | 8,441 | 7,053 | (3.7) | (16.4) | 18,940 | 23,433 |
| as % of sales | 90.3 | 94.8 | 94.8 | 93.6 | 95.4 | | | 90.6 | 94.5 |
| Consumption of RM | 5,510 | 4,550 | 6,042 | 6,380 | 5,272 | (4.3) | (17.4) | 14,077 | 17,694 |
| as % of sales | 67.9 | 67.5 | 72.1 | 70.8 | 71.3 | 333 | 53 | 67.3 | 71.4 |
| Employee Cost | 861 | 628 | 801 | 864 | 844 | (2.0) | (2.3) | 2,264 | 2,508 |
| as % of sales | 10.6 | 9.3 | 9.6 | 9.6 | 11.4 | | | 10.8 | 10.1 |
| Other expenditure | 955 | 1,216 | 1,097 | 1,197 | 937 | (1.8) | (21.7) | 2,599 | 3,231 |
| as % of sales | 11.8 | 18.0 | 13.1 | 13.3 | 12.7 | | | 12.4 | 13.0 |
| EBITDA | 783 | 349 | 438 | 577 | 343 | (56.3) | (40.6) | 1,963 | 1,358 |
| Depreciation | 96 | 96 | 100 | 102 | 91 | (5.3) | (10.9) | 338 | 292 |
| EBIT | 688 | 253 | 339 | 476 | 252 | (63.3) | (47.0) | 1,624 | 1,066 |
| Other Income | - | 1 | - | - | - | | | - | - |
| Interest | (3) | 84 | 37 | 62 | 76 | | | 34 | 175 |
| PBT | 690 | 170 | 302 | 413 | 176 | (74.5) | (57.3) | 1,591 | 891 |
| Total Tax | 226 | 56 | 53 | (331) | 54 | (75.8) | (116.4) | 448 | (224) |
| Adjusted PAT | 465 | 113 | 249 | 745 | 122 | (73.8) | (83.7) | 1,143 | 1,115 |
| Extra ordinary items | (6) | 156 | 6 | (12) | 11 | | | (36) | 4 |
| Reported PAT | 458 | 269 | 255 | 732 | 132 | (71.2) | (81.9) | 1,106 | 1,119 |

| Margins (%) | | | | | | (bps) | (bps) | | |
|--------------------|------|------|------|--------|------|-------|--------|------|--------|
| EBIDTA | 9.7 | 5.2 | 5.2 | 6.4 | 4.6 | (503) | (177) | 9.4 | 5.5 |
| EBIT | 8.5 | 3.7 | 4.0 | 5.3 | 3.4 | (507) | (186) | 7.8 | 4.3 |
| EBT | 8.5 | 2.5 | 3.6 | 4.6 | 2.4 | (613) | (220) | 7.6 | 3.6 |
| PAT | 5.7 | 1.7 | 3.0 | 8.3 | 1.6 | (409) | (661) | 5.5 | 4.5 |
| Effective Tax rate | 32.7 | 33.2 | 17.5 | (80.2) | 30.9 | (174) | 11,118 | 28.2 | (25.2) |

Segmental performance- Tractor segment disappoints

Operating performance in tractor segment was impacted by higher input costs and poor volumes. Volumes were impacted due to lower off take from segments it is significantly exposed (>40 HP tractor segment contributing ~54% of FY11 volumes and Northern regions). EBIT margins declined 160 bps QoQ/580bps YoY to 5.3%. Auto ancillary division also continued to report losses at EBIT level (Rs -45mn). Management expects division to break even in the next 6 months. Railway equipment division reported EBIT margins at ~8.3%.

Wholly owned subsidiary Escorts Construction equipment limited (ECIL) reported ~39% increase in top line to Rs 5.8bn for YTD SY11. ECIL continues to maintain its leadership in pick and carry cranes and has recently introduced back hoe loaders in Earth Moving machinery segment.

| Segmental details (Rs mn) | Q3SY10 | Q4SY10 | Q1SY11 | Q2SY11 | Q3SY11 |
|---------------------------|---------|---------|---------|---------|---------|
| Farm Equipment | | | | | |
| Tractor (Units) | 17,917 | 13,985 | 16,333 | 17,672 | 14,212 |
| Net Sales (Rs mn) | 7,475 | 5,963 | 7,130 | 7,926 | 6,686 |
| Avg realisations | 417,228 | 426,381 | 436,540 | 448,530 | 470,461 |
| Results (Rs mn) | 832 | 430 | 481 | 549 | 357 |
| Margins % | 11.1 | 7.2 | 6.8 | 6.9 | 5.3 |
| Auto ancilliary | | | | | |
| Net Sales (Rs mn) | 281 | 276 | 250 | 378 | 306 |
| Results (Rs mn) | -71 | -45 | -55 | -17 | -45 |
| Margins % | -25.4 | -16.2 | -21.9 | -4.4 | -14.7 |
| Railway Equipment | | | | | |
| Net Sales (Rs mn) | 415 | 551 | 423 | 510 | 437 |
| Results (Rs mn) | 1 | 63 | 30 | 68 | 36 |
| Margins % | 0.3 | 11.5 | 7.0 | 13.2 | 8.3 |

Valuations and View

The stock has underperformed significantly due to continuous disappointment on margins. Margins in the quarter at 4.6% are the lowest in last 12 quarters (since Sep 2008). We expect performance to improve with up tick in volumes and benefit of price hikes/stable commodity costs with a lag of 1-2 months. Stock is currently trading at attractive (trailing) valuations of 0.7x P/BV and 0.1x net D/E based on SY10 financials adjusted for revaluation reserves. However, Volumes up tick and margin expansion are likely to be key trigger for stock performance in the immediate future.

Financials

Income Statement

| Y/E, Mar (Rs. mn) | SY07 | SY08 | SY09 | SY10 |
|--------------------------------|---------------|---------------|---------------|---------------|
| Net Sales | 20,756 | 19,923 | 21,578 | 27,457 |
| Growth (%) | 18.6 | (4.0) | 8.3 | 27.2 |
| Expenditure | 20,056 | 19,260 | 19,942 | 25,589 |
| Materials Consumed | 15,147 | 14,488 | 14,418 | 18,627 |
| Employee Cost | 2,040 | 2,026 | 2,344 | 2,960 |
| Other Exp | 2,869 | 2,746 | 3,181 | 4,002 |
| EBITDA | 700 | 663 | 1,636 | 1,868 |
| Growth (%) | 162.7 | (5.2) | 146.6 | 14.2 |
| EBITDA margin (%) | 3.4 | 3.3 | 7.6 | 6.8 |
| Depreciation | 450 | 429 | 378 | 385 |
| EBIT | 250 | 235 | 1,257 | 1,483 |
| EBIT margin (%) | 1.2 | 1.2 | 5.8 | 5.4 |
| Other Income | 474 | 716 | 599 | 918 |
| Interest expenses | 898 | 689 | 745 | 520 |
| PBT | -173 | 261 | 1,111 | 1,880 |
| Tax | -109 | 143 | 213 | 505 |
| Effective tax rate (%) | 62.8 | 54.6 | 19.2 | 26.8 |
| Reported PAT | -64 | 119 | 897 | 1,376 |
| Growth (%) | (133.9) | (284.3) | 655.9 | 53.3 |
| Net Margin (%) | (0.3) | 0.6 | 4.2 | 5.0 |
| (Profit)/loss from JV's/Ass/MI | - | - | - | - |
| Rep. PAT after MI | -64 | 119 | 897 | 1,376 |
| E/O items | -51 | 105 | 77 | 94 |
| Adjusted PAT | -13 | 14 | 820 | 1,282 |
| Growth (%) | (93.6) | (203.8) | 5,886.1 | 56.3 |

Cash Flow

| Y/E, Mar (Rs. mn) | SY07 | SY08 | SY09 | SY10 |
|------------------------------|--------------|----------------|----------------|----------------|
| PBT (Ex-Other income) | (648) | (454) | 512 | 963 |
| Depreciation | 450 | 429 | 378 | 385 |
| Interest Provided | 898 | 689 | 745 | 520 |
| Other Non-Cash items | 105 | 1,801 | (3,007) | 1,610 |
| Chg in working cap | (1,169) | (1,311) | 3,960 | (2,121) |
| Tax paid | 109 | (143) | (213) | (505) |
| Operating Cashflow | (255) | 1,011 | 2,375 | 852 |
| Capital expenditure | (279) | 200 | (6,363) | (443) |
| Free Cash Flow | (533) | 1,211 | (3,988) | 409 |
| Other income | 474 | 716 | 599 | 918 |
| Investments | (152) | (1,082) | 6,253 | (2,105) |
| Investing Cashflow | 322 | (367) | 6,852 | (1,188) |
| Equity Capital Raised | 115 | 70 | - | 116 |
| Loans Taken / (Repaid) | (648) | (885) | (1,718) | 333 |
| Interest Paid | (898) | (689) | (745) | (520) |
| Dividend paid (incl tax) | | | 91 | 162 |
| Income from investments | | | | |
| Others | 1,194 | 359 | 81 | 603 |
| Financing Cashflow | (237) | (1,145) | (2,292) | 694 |
| Net chg in cash | (448) | (300) | 572 | (85) |
| Opening cash position | 2,157 | 1,732 | 1,145 | 1,648 |
| Closing cash position | 1,709 | 1,432 | 1,717 | 1,563 |

* represents cash and cash equivalents for FY09 and FY10

Balance Sheet

| Y/E, Mar (Rs. Mn) | SY07 | SY08 | SY09 | SY10 |
|-------------------------------|---------------|---------------|---------------|---------------|
| Equity share capital | 837 | 907 | 907 | 1,023 |
| Reserves & surplus | 10,353 | 11,120 | 13,535 | 16,356 |
| Minority Interest | 11,190 | 12,027 | 14,442 | 17,378 |
| Net worth | | | | |
| Secured Loans | 4,945 | 4,226 | 2,538 | 2,838 |
| Unsecured Loans | 311 | 144 | 115 | 148 |
| Loan Funds | 5,256 | 4,371 | 2,653 | 2,986 |
| Net deferred tax liability | -902 | -475 | -278 | -51 |
| Total Liabilities | 15,543 | 15,922 | 16,816 | 20,313 |
| Gross Block | 14,370 | 14,159 | 20,598 | 20,955 |
| Less: Depreciation | 5,832 | 5,934 | 6,029 | 6,457 |
| Net block | 8,537 | 8,225 | 14,569 | 14,497 |
| Capital work in progress | 134 | 144 | 107 | 194 |
| Investment | 425 | 426 | 236 | 366 |
| Current Assets | 10,097 | 10,970 | 8,307 | 10,632 |
| Inventories | 1,607 | 2,044 | 1,995 | 2,965 |
| Sundry debtors | 4,602 | 5,182 | 3,292 | 3,326 |
| Cash & bank balance | 1,732 | 1,145 | 1,648 | 1,744 |
| Loans & advances | 2,156 | 2,599 | 1,373 | 2,597 |
| Other current assets | | | | |
| Current lia & Prov | 7,636 | 7,785 | 8,579 | 8,687 |
| Current liabilities | 6,067 | 6,553 | 7,267 | 7,310 |
| Provisions | 1,569 | 1,232 | 1,312 | 1,377 |
| Net current assets | 2,461 | 3,185 | -272 | 1,945 |
| Misc. exp | 159 | 110 | 54 | 20 |
| Total Assets | 11,717 | 12,090 | 14,694 | 17,021 |

Key Ratios

| Y/E, Mar | SY07 | SY08 | SY09 | SY10 |
|----------------------------|---------|------|--------|--------|
| Profitability (%) | | | | |
| EBITDA Margin | 3.4 | 3.3 | 7.6 | 6.8 |
| Net Margin | (0.3) | 0.6 | 4.2 | 5.0 |
| ROCE* | 5.6 | 8.7 | 16.5 | 18.3 |
| ROE* | (0.6) | 1.0 | 6.8 | 13.2 |
| RoIC* | 2.0 | 1.7 | 8.7 | 13.5 |
| Per Share Data (Rs) | | | | |
| EPS | (0.8) | 1.3 | 9.9 | 13.4 |
| CEPS | 4.6 | 6.0 | 14.1 | 17.2 |
| BVPS* | 75.4 | 79.9 | 98.2 | 117.2 |
| DPS | | | 1.0 | 1.5 |
| Valuations (x) | | | | |
| PER | (105.7) | 62.1 | 8.2 | 6.0 |
| P/CEPS | 17.7 | 13.5 | 5.8 | 4.7 |
| P/BV* | 1.1 | 1.0 | 0.8 | 0.7 |
| EV / Sales | 0.5 | 0.5 | 0.4 | 0.3 |
| EV / EBITDA | 14.1 | 15.3 | 5.0 | 4.9 |
| Dividend Yield (%) | - | - | 1.2 | 1.8 |
| Gearing Ratio (x) | | | | |
| Net Debt/ Equity* | 0.5 | 0.4 | 0.1 | 0.1 |
| Net Debt/EBIDTA | 5.0 | 4.9 | 0.6 | 0.7 |
| Working Cap Cycle (days) | 2.5 | 12.3 | (33.5) | (13.6) |

*calculated ex revaluation reserve

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