

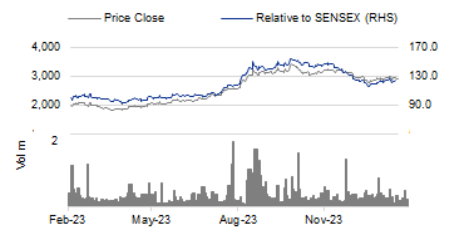
India

REDUCE (no change)

Consensus ratings*:	Buy 6	Hold 6	Sell 10
Current price:	Rs2,933		
Target price:	Rs2,071 ▲		
Previous target:	Rs2,019		
Up/downside:	-29.4%		
InCred Research / Consensus:	-34.6%		
Reuters:	ESCO.NS		
Bloomberg:	ESCORTS IN		
Market cap:	US\$3,906m		
	Rs324,058m		
Average daily turnover:	US\$14.8m		
	Rs1227.6m		
Current shares o/s:	111.8m		
Free float:	33.7%		
*Source: Bloomberg			

Key changes in this note

- Sales cut by 11-19% for FY24F-26F.
- EBITDA cut by around 10%.
- FY24F-26F EPS cut by around 6%.



Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	2.8	(6.8)	47.9
Relative (%)	2.7	(15.4)	25.9

Major shareholders	% held
Kubota Corporation	53.5
Nanda Family	12.8
HDFC Mutual Fund	1.6

Research Analyst(s)



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Escorts Kubota Ltd

Decline in tractor demand likely to prolong

- 3Q EPS grew 18% qoq to Rs24.8, a 4% beat to our estimate, aided by other income, while EBITDA in line. The railway segment's sales miss disappoints.
- Management confirms our fears of mid-teen sales drop in 4Q and uncertainty to prolong till general elections. We cut EBITDA/EPS by 10/6% for FY24F-26F.
- Stock trades at +1SD above five-year mean level. P/E and P/BV valuations are rich considering the start of tractor downcycle phenomenon. Retain REDUCE.

Railway division disappoints in 3QFY24

Escorts Kubota's 3QFY24 EBITDA rose by 19% qoq and 64% yoy to Rs3.1bn, in line with our/Bloomberg consensus estimates. The EBITDA margin improved by 60bp qoq to 13.5% due to lower other expenses, which helped overcome the 7% miss in net sales. The railway division's sales dip of 12% qoq led to sales miss. EBIT grew 22% qoq to Rs2.7bn, aided by tractors, while construction equipment and railway segments recorded a qoq dip. PAT grew 18% qoq and 49% yoy to Rs2.77bn, a 4% beat to our estimate.

Management conference-call highlights

Management gave tractor industry volume dip guidance of 6% for FY24F vs. a 3% drop witnessed in 9MFY24. The company has been able to outperform in tractor exports in 9MFY24, aided by Kubota. The TREM-4 norms for above 50HP tractors has led to a sharp collapse in the above 50HP tractor segment to just 2% of industry volume now vs. 7% earlier. However, the delay in the government's timeline to implement TREM-5 norms to Apr 2026 is a welcome relief. The company will focus on penetrating the western India tractor market to improve its market share.

Cut EBITDA by ~10% for FY24F-26F

The tractor industry is witnessing a typical cyclical downfall, as financiers' non-performing assets or NPAs, starting in Oct 2023, have spread to new states amid the rabi crop challenges. With general elections in May 2024, the peak tractor demand season may face challenges. We expect the mid-teen decline, as per management's guidance, in 4QFY24F to prevail for a few quarters into FY25F. We build a 10% tractor volume dip in FY25F, leading to a reduction of 10% in our EBITDA and 6% in EPS estimates for FY24F-26F.

Rich valuation undermines cyclical tractor demand risk; REDUCE

The weakness in tractor demand, we believe, is overlooked at the current rich valuation at +1SD above the mean level. We maintain our REDUCE rating on the stock with a higher target price of Rs2,071 (Rs2,019 earlier) valuing it at 18x one-year forward P/E, which is near the five-year mean level. Rainfall outlook and government policy on agriculture will be key upside risks.

Financial Summary

	Mar-22A	Mar-23A	Mar-24F	Mar-25F	Mar-26F
Revenue (Rsm)	71,527	83,450	89,221	95,092	111,189
Operating EBITDA (Rsm)	9,513	7,805	11,923	12,581	15,042
Net Profit (Rsm)	7,656	6,070	10,559	11,118	13,144
Core EPS (Rs)	68.5	60.8	94.4	99.4	117.6
Core EPS Growth	(12.4%)	(11.2%)	55.2%	5.3%	18.2%
FD Core P/E (x)	42.83	54.02	31.05	29.49	24.94
DPS (Rs)	7.0	7.0	13.0	15.0	17.0
Dividend Yield	0.28%	0.28%	0.44%	0.51%	0.58%
EV/EBITDA (x)	34.19	41.41	26.96	25.51	21.44
P/FCFE (x)	(11.79)	108.44	102.36	150.78	1,062.47
Net Gearing	(3.3%)	(5.6%)	(6.9%)	(6.8%)	(4.7%)
P/BV (x)	4.16	3.89	3.52	3.19	2.88
ROE	11.5%	8.3%	11.9%	11.3%	12.1%
% Change In Core EPS Estimates			(5.84%)	(5.66%)	(6.13%)
InCred Research/Consensus EPS (x)					

SOURCE: INCRED RESEARCH, COMPANY REPORTS

Decline in tractor demand likely to prolong

Management conference-call highlights▶

- **Agri machinery:** Management expects industry volume to decline by 6-8% next year due to the high base effect and a weak monsoon. In 3QFY24, agri machinery domestic industry volume fell by 4% yoy vs. Escorts Kubota's volume decline of 5.6%, and its market share stood at 10.5%. Industry export volume declined by 27% yoy vs. Escorts Kubota's exports volume decline of 25.7% yoy. USA and Europe markets remain under pressure, and this is likely to sustain. Exports through the Kubota channel stood at 47%+ of total export volume. Management believes that dealer consolidation will take place in the next one year, which will drive export volume.
- **Industry norms:** Implementation of the Tractor Emission Norms-4 or TREM-4 mainly impacted 40-50HP tractors and prior to implementation, the segment used to contribute 7% to the total volume vs. 2% post implementation. Escorts Kubota was able to pass on the elevated prices, led by the change in emission norms, to its customers.
- **Construction equipment:** Industry volume was up 31% vs. Escorts Kubota's volume growth of 49%. The long-term growth momentum is likely to continue led by the government's push to the infrastructure sector, but the near-term headwind is expected to delay project execution due to the forthcoming general elections in India. During the quarter, management took price hikes to offset higher input costs.
- **Railway equipment:** Total order book at the end of the quarter stood at Rs.9bn+, with the major orders being from Indian Railways. In the case of freight wagons, the company is ramping up its production due to high demand while in the passenger carrier segment, major traction comes from Vande Bharat trains. The company is in the process of developing and rolling out new products for the same.
- **Demographic strategy:** Management's current focus is the western and southern regions, primarily Gujarat and Maharashtra, as they contribute around 20-21% to its revenue. The company stated that industry in the southern region has shrunk over the last 18 months and now contributes only 15-16%.
- **Inventory level:** Currently, the inventory level is 35-37 days which, management believes, to be a healthy level, even for the upcoming Navratri festive season.
- **Finance business:** The company has incorporated a finance company last month and is hopeful of starting the financing business from the next financial year.

Figure 1: Results comparison

Y/E Mar (Rs m)	3QFY24	3QFY23	yoy % chg	2QFY24	qoq % chg	9MFY24	9MFY23	yoy % chg	Comments for the quarter
Revenue	23,204	22,637	2.5	20,462	13.4	66,943	61,620	8.6	7% below our estimate.
Raw material costs	16,092	16,871	(4.6)	13,846	16.2	46,190	45,055	2.5	
RM as % of revenue	69.4	74.5	(5.18)	67.7	168.5	69.0	73.1	(411.8)	65bp below our estimate.
EBITDA	3,127	1,903	64.3	2,633	18.8	9,031	5,447	65.8	In line with our estimate.
EBITDA margin (%)	13.5	8.4	506.7	12.9	60.9	13.5	8.8	465.1	98bp above our estimate.
Depreciation & amortization	415	376	10.5	407	2.0	1,224	1,104	10.8	-
EBIT	2,712	1,528	77.5	2,226	21.8	7,807	4,343	79.8	
Interest expenses	24	26	(9.8)	24	1.3	74	75	(1.6)	
Other income	1,035	913	13.3	950	8.9	2,930	2,043	43.4	15% higher than our estimate.
Pre-tax profit	3,723	2,414	54.2	3,152	18.1	10,663	6,310	69.0	5% above our estimate.
Tax	950	550	72.7	802	18.4	2,710	1,367	98.3	
Tax rate (%)	25.5	22.8	273	25.4	7	25.4	21.7	375.8	
Normalized net profit	2,773	1,864	48.7	2,350	18.0	7,953	4,944	60.9	4% above our estimate.
Exceptionals	-	-	-	-	nm	-	(728)	nm	
Reported net profit	2,773	1,864	48.7	2,350	18.0	7,953	4,216	88.6	
Normalized EPS (Rs)	24.8	20.6	20.2	21.0	18.0	90.5	56.3	60.9	
Tractor volume (nos.)	25,999	28,025	(7.2)	22,019	18.1	74,600	78,525	(5.0)	
Tractor realization (Rs)	6,37,848	6,09,452	4.7	6,33,194	0.7	6,59,437	6,05,999	8.8	4% below our estimate.

SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 2: Tractor division's EBIT margin declines

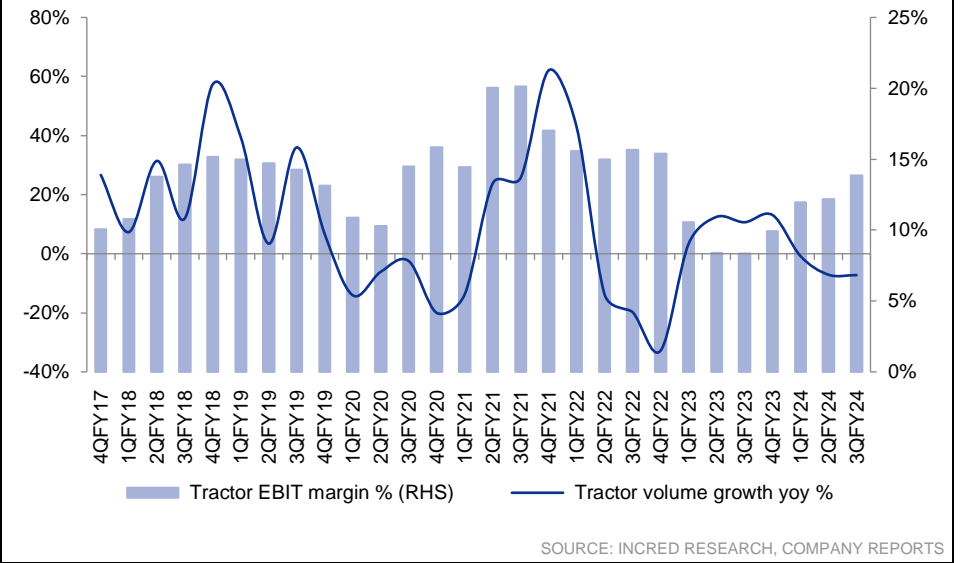


Figure 3: Railway division's sales down qoq from their peak

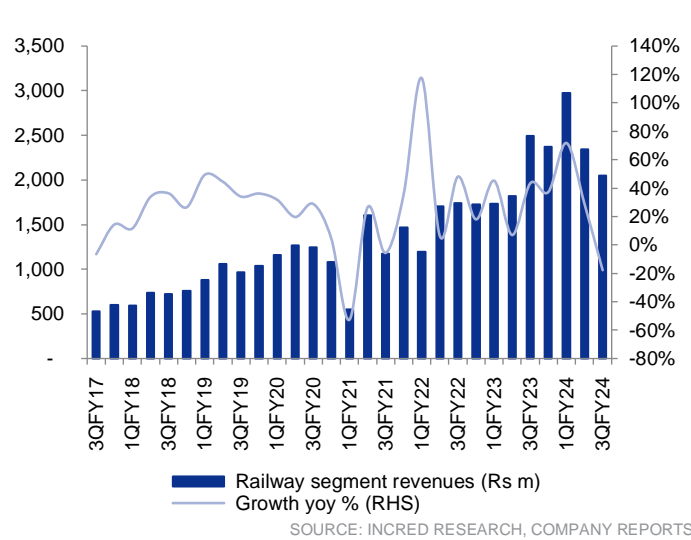


Figure 4: Segment-wise EBIT margin trend

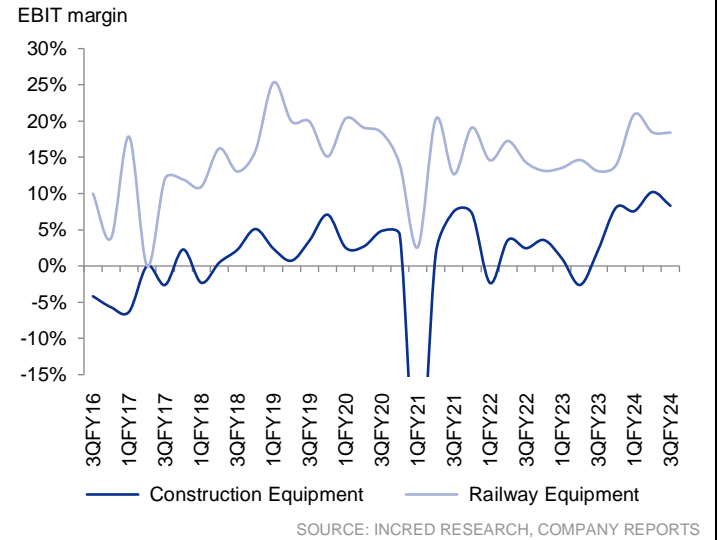


Figure 5: EBITDA margin trend

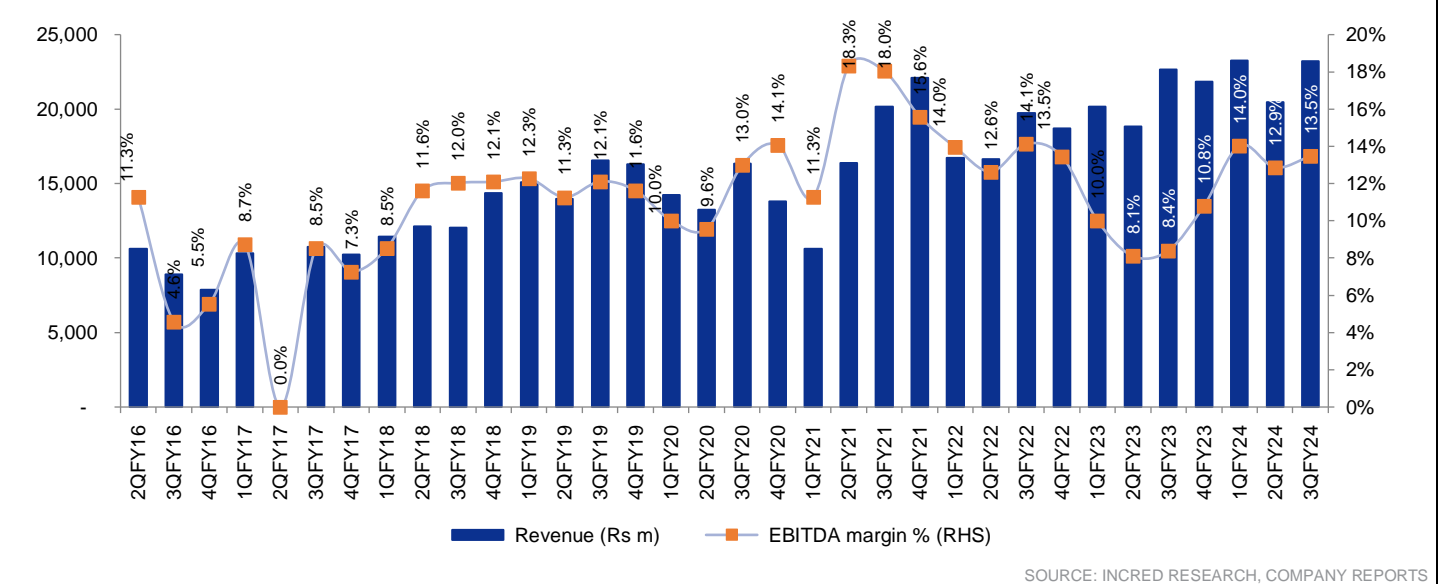
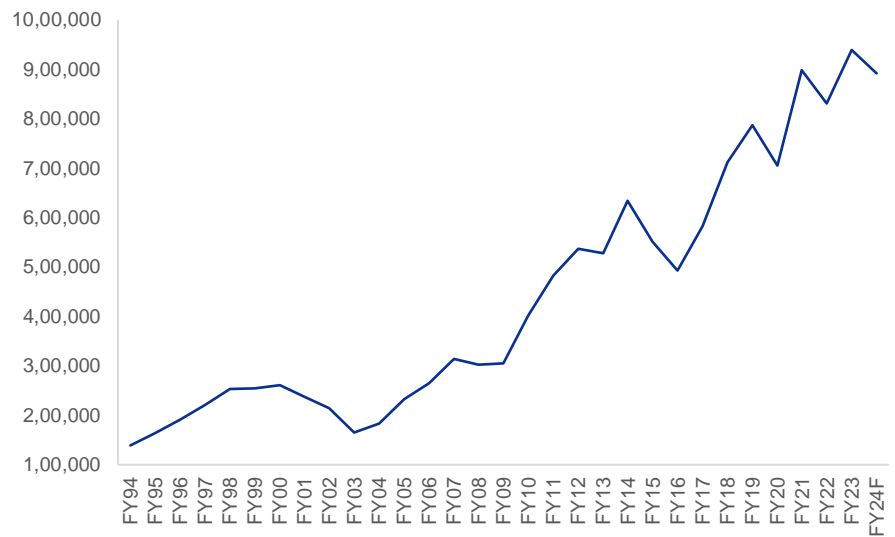


Figure 6: Tractor sales volume ready for cyclical plunge



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 7: Our revised earnings estimates

Rs m	FY24F		FY25F		FY26F	
	Old	New	Old	New	Old	New
Tractor volume (nos)	1,09,648	97,072	1,18,307	88,488	1,29,123	96,309
% change		-11.5%		-25.2%		-25.4%
Net sales	1,00,608	89,221	1,17,829	95,092	1,35,708	1,11,189
% change		-11.3%		-19.3%		-18.1%
EBITDA	13,266	11,923	13,977	12,581	16,781	15,042
% change		-10.1%		-10.0%		-10.4%
EBITDA margin	13.2%	13.4%	11.9%	13.2%	12.4%	13.5%
bp change		13		115		94
PAT	11,214	10,559	11,785	11,118	14,003	13,144
% change		-5.8%		-5.7%		-6.1%

SOURCE: THE TRACTOR AND MECHANIZATION ASSOCIATION (TMA), INCRED RESEARCH, COMPANY REPORTS

Figure 8: Key assumptions

Volume Assumptions	Mar-22A	Mar-23A	Mar-24F	Mar-25F	Mar-26F	
Tractor volume (units)	94,228	1,03,290	97,072	88,488	96,309	
Growth yoy %		-11.7%	9.6%	-6.0%	-8.8%	8.8%
Construction equipment volume (units)	4,117	4,620	6,838	8,547	10,256	
Growth yoy %		5.2%	12.2%	48.0%	25.0%	20.0%
Total revenue (Rs m)	71,527	83,450	89,221	95,092	1,11,189	
Growth yoy %		3.2%	16.7%	6.9%	6.6%	16.9%
EBITDA margin %		13.6%	9.4%	13.4%	13.2%	13.5%
Segment-wise assumptions						
Tractor Revenue (Rs m)	55,210	63,161	61,576	60,200	68,139	
EBIT margin %		15.5%	9.3%	13.1%	13.5%	14.0%
Construction equipment revenue (Rs m)	9,853	11,790	17,711	23,467	29,568	
EBIT margin %		2.4%	2.9%	8.5%	9.0%	9.0%
Railway equipment revenue (Rs m)	6,362	8,419	9,934	11,425	13,481	
EBIT margin %		14.8%	13.8%	19.0%	20.0%	19.0%

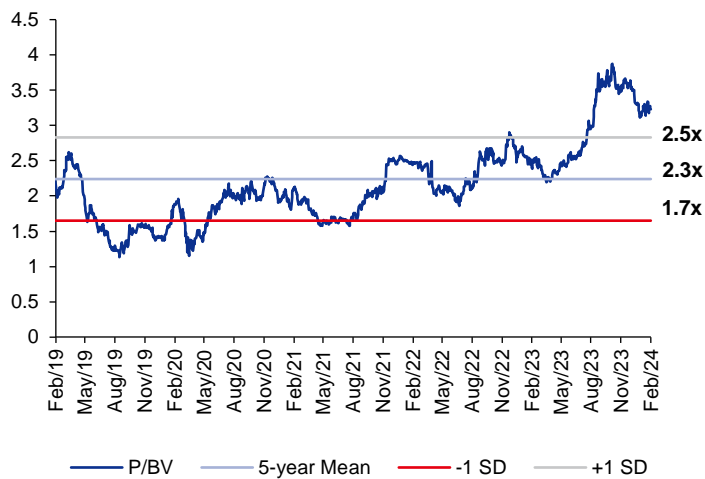
SOURCE: THE TRACTOR AND MECHANIZATION ASSOCIATION (TMA), INCRED RESEARCH, COMPANY REPORTS

Figure 9: Forward P/E is rich at +1 standard deviation



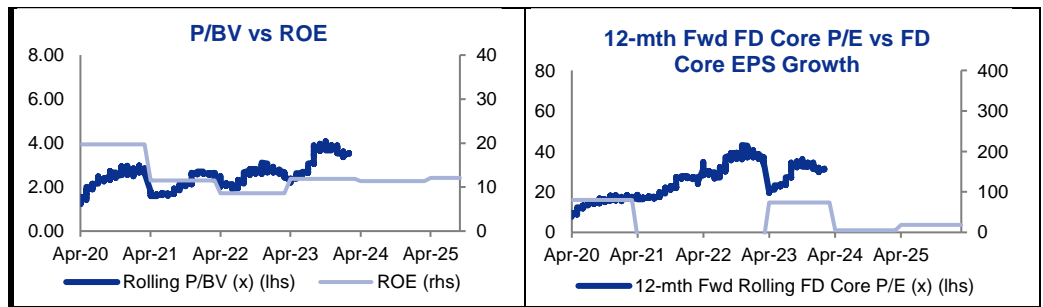
SOURCE: BLOOMBERG, INCRED RESEARCH, COMPANY REPORTS

Figure 10: Forward P/BV is super-rich at +2 standard deviation above the mean level



SOURCE: BLOOMBERG, INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS



Profit & Loss

(Rs mn)	Mar-22A	Mar-23A	Mar-24F	Mar-25F	Mar-26F
Total Net Revenues	71,527	83,450	89,221	95,092	111,189
Gross Profit	22,199	22,781	27,748	30,144	35,580
Operating EBITDA	9,513	7,805	11,923	12,581	15,042
Depreciation And Amortisation	(1,298)	(1,484)	(1,673)	(1,890)	(2,090)
Operating EBIT	8,216	6,321	10,250	10,690	12,952
Financial Income/(Expense)	(127)	(103)	(100)	(70)	(50)
Pretax Income/(Loss) from Assoc.					
Non-Operating Income/(Expense)	2,130	2,806	3,928	4,203	4,624
Profit Before Tax (pre-EI)	10,219	9,024	14,078	14,824	17,526
Exceptional Items		(972)			
Pre-tax Profit	10,219	8,052	14,078	14,824	17,526
Taxation	(2,563)	(1,982)	(3,520)	(3,706)	(4,381)
Exceptional Income - post-tax					
Profit After Tax	7,656	6,070	10,559	11,118	13,144
Minority Interests					
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	7,656	6,070	10,559	11,118	13,144
Recurring Net Profit	7,656	6,802	10,559	11,118	13,144
Fully Diluted Recurring Net Profit	7,656	6,802	10,559	11,118	13,144

Cash Flow

(Rs mn)	Mar-22A	Mar-23A	Mar-24F	Mar-25F	Mar-26F
EBITDA	9,513	7,805	11,923	12,581	15,042
Cash Flow from Invt. & Assoc.					
Change In Working Capital	(5,678)	(3,803)	1,071	367	(1,676)
(Incr)/Decr in Total Provisions	(620)	(392)	596	350	300
Other Non-Cash (Income)/Expense					
Other Operating Cashflow		(972)			
Net Interest (Paid)/Received	2,003	2,703	3,828	4,133	4,574
Tax Paid	(2,420)	(1,982)	(3,520)	(3,706)	(4,381)
Cashflow From Operations	2,799	3,360	13,899	13,725	13,859
Capex	(2,023)	(2,304)	(4,955)	(5,000)	(3,500)
Disposals Of FAs/subsidiaries					
Acq. Of Subsidiaries/investments					
Other Investing Cashflow	(28,596)	1,968	(5,741)	(6,550)	(10,050)
Cash Flow From Investing	(30,619)	(336)	(10,696)	(11,550)	(13,550)
Debt Raised/(repaid)					
Proceeds From Issue Of Shares	18,162				
Shares Repurchased					
Dividends Paid	(924)	(924)	(1,453)	(1,677)	(1,901)
Preferred Dividends					
Other Financing Cashflow					
Cash Flow From Financing	17,239	(924)	(1,453)	(1,677)	(1,901)
Total Cash Generated	(10,581)	2,100	1,750	498	(1,592)
Free Cashflow To Equity	(27,819)	3,024	3,203	2,175	309
Free Cashflow To Firm	(27,692)	3,127	3,303	2,245	359

SOURCE: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS...cont'd

Balance Sheet

(Rs mn)	Mar-22A	Mar-23A	Mar-24F	Mar-25F	Mar-26F
Total Cash And Equivalents	2,585	4,685	6,434	6,932	5,340
Total Debtors	8,276	12,076	11,000	11,203	12,185
Inventories	8,036	11,590	11,489	10,421	11,576
Total Other Current Assets	4,287	4,405	4,745	5,095	5,445
Total Current Assets	23,183	32,756	33,667	33,650	34,545
Fixed Assets	19,200	20,725	23,302	26,411	27,821
Total Investments	51,335	50,306	55,806	62,306	72,306
Intangible Assets					
Total Other Non-Current Assets					
Total Non-current Assets	70,534	71,030	79,107	88,717	100,127
Short-term Debt					
Current Portion of Long-Term Debt					
Total Creditors	8,777	12,329	12,222	11,724	12,185
Other Current Liabilities	4,388	4,300	4,800	5,300	5,800
Total Current Liabilities	13,165	16,628	17,022	17,023	17,985
Total Long-term Debt					
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities					
Total Non-current Liabilities					
Total Provisions	1,771	2,105	2,501	2,651	2,751
Total Liabilities	14,936	18,733	19,523	19,674	20,736
Shareholders Equity	78,782	84,348	93,252	102,693	113,937
Minority Interests					
Total Equity	78,782	84,348	93,252	102,693	113,937

Key Ratios

	Mar-22A	Mar-23A	Mar-24F	Mar-25F	Mar-26F
Revenue Growth	3.2%	16.7%	6.9%	6.6%	16.9%
Operating EBITDA Growth	(15.8%)	(18.0%)	52.8%	5.5%	19.6%
Operating EBITDA Margin	13.3%	9.4%	13.4%	13.2%	13.5%
Net Cash Per Share (Rs)	23.12	41.90	57.55	62.00	47.76
BVPS (Rs)	704.67	754.46	834.10	918.54	1,019.11
Gross Interest Cover	64.69	61.37	102.50	152.72	259.04
Effective Tax Rate	25.1%	24.6%	25.0%	25.0%	25.0%
Net Dividend Payout Ratio	12.1%	13.1%	13.8%	15.1%	14.5%
Accounts Receivables Days	38.93	44.51	47.20	42.61	38.39
Inventory Days	54.68	59.04	68.52	61.57	53.09
Accounts Payables Days	76.39	63.49	72.89	67.29	57.71
ROIC (%)	31.7%	18.5%	23.9%	23.9%	26.9%
ROCE (%)	12.3%	7.7%	11.5%	10.8%	11.9%
Return On Average Assets	9.4%	7.2%	9.8%	9.5%	10.3%

Key Drivers

	Mar-22A	Mar-23A	Mar-24F	Mar-25F	Mar-26F
ASP (% chg, main prod./serv.)	10.4%	4.4%	3.7%	7.2%	4.0%
Unit sales grth (% , main prod./serv.)	(11.7%)	9.6%	(6.0%)	(8.8%)	8.8%
ASP (% chg, 2ndary prod./serv.)	20.7%	6.6%	1.5%	6.0%	5.0%
Unit sales grth (% ,2ndary prod/serv)	5.2%	12.2%	48.0%	25.0%	20.0%

SOURCE: INCRED RESEARCH, COMPANY REPORTS

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