

November 07, 2024

RESULT REPORT Q2 FY25 | Sector: Automobile

Escorts Kubota Ltd

Growth outlook improving

View – Recent stock correction yet not make risk reward favorable

Escorts Kubota (ESCORTS) 2QFY25 results were weak led by first quarter of amalgamation of EKI and KAM. While CE/railways business performance was in-line, lower than expected margins in FES led EBITDA margins at 10.8% (flat YoY/ -240bp QoQ). Margins expansion for the merged entity to likely be gradual given full benefits of localization etc. to only kick-in over 2-3 years. However, improved volume outlook on tractors, price hikes undertaken, and benign RM should help margins expansion QoQ. We believe, ESCORTS can surpass co guidance of mid-single digit industry volume growth for FY25E with sings of volume recovery in South/West markets (key markets for Kubota) to be supported by new launches in Escorts brand. While we remain constructive on growth opportunities for merged entity in tractor, implements, components sourcing and exports to synergize only over mid-term, near term margin recovery to be gradual. Co has indicated revision in MTPB targets, impacted by few factors such as delay in land acquisition for greenfield capacity, weak exports etc. We see EKL's market share remain range bound.

We believe, EKL is more vulnerable v/s peers as 1) it derives ~70% of its revenues from agri segment and 2) aggressive expansion by Sonalika, TAFE, John Deere, etc. necessitating tight balance between market share and margins. Despite recent correction, the valuations at 34.5x/29.5x FY26/27 EPS, do reflect positive synergies making risk reward yet not favorable. We believe, benefits arising out of Kubota JV to start reflecting meaningfully led by exports ramp-up (FY26) and localization (FY27). We cut FY26/27 EPS by ~13.8/10.6% each to factor in for weaker margin profile of merged entity. Maintain Neutral with revised TP of Rs3,693 (vs Rs3,918). We value co at 35x Mar'27 EPS (vs Mar'26) and build in revenue/EBITDA/PAT CAGR of 16.2%/14.8%/13% over FY24-27E.

Result Highlights – Merged entity margins lower then expected

- Revenues grew 0.5% YoY (-11.6% QoQ) at Rs24.7b as Agri/railways/construction equip (CE) revenues grew +5.3%/-9.9%/-13.7% YoY. FES ASP grew 5.6% YoY (+0.7% QoQ) at Rs720k/unit and vol. fell ~1% YoY (14.4% QoQ) at ~26k units.
- Gross margins came in at 30.8% (+70bp YoY/+90bp QoQ). However, this was offset by higher other expense at Rs2.9b (+4.6% QoQ) led EBITDA at Rs2.8b (flat YoY/-27.3% QoQ) with margins at 10.8% (flat YoY/ -240bp QoQ).
- Segmental EBIT margins – FES at 9.1% (-20bp YoY/-250bp QoQ), Railway at 15.2% (-320bp YoY/-520bp QoQ), CE at 9.3% (-60bp YoY/-100bp QoQ).
- Weak EBITDA margins offset by utilization of tax credits available with amalgamating cos led Adj.PAT to grow 53.2% YoY (+7.6% QoQ) at ~Rs3.3b

Exhibit 1: Actual vs estimates

Rs mn	Actual	Estimate		% variation		Remarks
		Yes Sec	Consensus	Yes Sec	Consensus	
Sales	24,762	21,734	22,089	13.9	12.1	Operationally better performance
EBITDA	2,676	2,738	2,952	-2.3	-9.4	
EBITDA margins %	10.8	12.6	13.4	-180bp	-260bp	
Adjusted PAT	3,267	2,454	2,630	33.2	24.2	

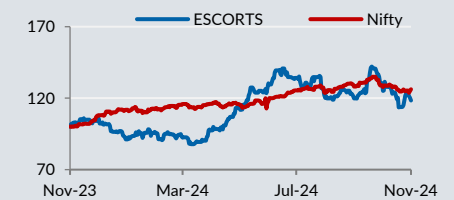
Source: Company, YES Sec

Reco	: NEUTRAL
CMP	: Rs 3,644
Target Price	: Rs 3,693
Return	: +1.3%

Stock data (as on Nov 7, 2024)

Nifty	24,199
52 Week h/l (Rs)	4,420 / 2,648
Market cap (Rs/USD mn)	4,12,582 / 4,893
Outstanding Shares (mn)	110
6m Avg t/o (Rs mn):	1,045
Div yield (%):	0.5
Bloomberg code:	ESCORTS IN
NSE code:	ESCORTS

Stock performance



	1M	3M	1Y
Absolute return	(5.3%)	(2.5%)	+16.6%

Shareholding pattern (As of Sep'24)

Promoter	68.0%
FII+DII	16.5%
Others	13.7%

Δ in stance

(1-Yr)	New	Old
Rating	NEUTRAL	NEUTRAL
Target Price	3,693	3,918

Δ in earnings estimates

	FY25E	FY26E
EPS (New)	91.6	105.5
EPS (Old)	108.5	122.5
% change	(15.6%)	(13.8%)

Financial Summary

Y/E Mar (Rs b)	FY25E	FY26E	FY27E
Sales	108.8	122.6	138.7
EBITDA	12.5	14.7	17.6
Adj. PAT	11.2	12.9	15.2
EPS (INR)	91.6	105.5	123.7
EPS Gr. (%)	(3.5)	15.1	17.2
BV/Sh. (INR)	834	932	1,049
RoE (%)	11.6	11.9	12.5
RoCE (%)	15.4	15.9	16.6
Payout (%)	7.6	6.6	5.7
P/E (x)	39.8	34.5	29.5
P/BV (x)	4.4	3.9	3.5
EV/EBITDA (x)	34.5	28.8	23.5
EV/Sales (x)	4.0	3.5	3.0

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Exhibit 2: Quarterly snapshot

Y/e Mar (Rs. mn)	Q2FY25	Q2FY24	YoY chg (%)	Q1FY25	QoQ chg	1HFY25	1HFY24	YoY chg (%)
Net Revenues	24,762	24,646	0.5	28,010	(11.6)	52,771	47,923	10.1
Raw Materials	17,139	17,232	(0.5)	19,639	(12.7)	36,778	33,484	9.8
% of Net Sales	69.2%	69.9%		70.1%		69.7%	69.9%	
Gross Margins %	30.8%	30.1%		29.9%		30.3%	30.1%	
Personnel	2,016	1,940	3.9	1,874	7.6	3,890	3,424	13.6
% of Net Sales	8.1%	7.9%		6.7%		7.4%	7.1%	
Manufacturing & Other Exp	2,932	2,807	4.4	2,802	4.6	5,734	5,079	12.9
% of Net Sales	11.8%	11.4%		10.0%		10.9%	10.6%	
Total Expenditure	22,086	21,979	0.5	24,315	(9.2)	46,401	41,987	10.5
EBITDA	2,676	2,667	0.3	3,694	(27.6)	6,370	5,937	7.3
EBITDA Margin (%)	10.8%	10.8%		13.2%		12.1%	12.4%	
Depreciation	636	582	9.3	615	3.4	1,251	984	27.2
EBIT	2,039	2,085	(2.2)	3,079	(33.8)	5,119	4,953	3.3
Interest Expenses	92	87	6.5	101	(9.1)	193	113	71.0
Non-operating income	1,153	936	23.1	1,025	12.5	2,178	1,882	15.7
Extraordinary Expenses	-	-		-		0	0	
PBT	3,100	2,935	5.6	4,003	(22.6)	7,103	6,721	5.7
Tax-Total	(167)	802	(120.8)	968	(117.3)	801	1,760	(54.5)
Tax Rate (%) - Total	-5.4%	27.3%		24.2%		11.3%	26.2%	
Reported PAT	3,267	2,133	53.2	3,035	7.6	6,302	4,961	27.0
Adj. PAT	3,267	2,133	53.2	3,035	7.6	6,302	4,961	27.0
PAT Margin	13.2%	8.7%		10.8%		11.9%	10.4%	

Source- Company, Yes Sec

KEY CON-CALL HIGHLIGHTS

Agriculture (FES) segment -

- **Domestic outlook** – expect domestic tractor industry to grow by mid-single digit for FY25E (vs flat growth in 1HFY25) led by better farm sentiments due to favorable monsoon and terms of trade.
 - Festive to festive growth was decent double digit. Have seen the best ever festive for industry and escorts due to concentration of festive in single month.
 - Current inventory levels are 35-37 days (sharp correction post festive).
 - Region wise – Ex of Bihar industry grew healthy in East led by subsidy in Chhattisgarh. West led by MH (while Guj is laggard) and South to pick up as the reservoir levels are back at 85-90%.
 - Expect higher than industry performance from Kubota with revival of volumes from South and West markets. EKL focus will be in both these markets as have put in place channel for MH and Gujarat and couple of states in South.
- **Exports sales through Kubota channel contributed ~20% in 2QFY25 (vs 21% in 1QFY25).** Exports continue to decline by ~21% YoY in 2Q and ~24.7% in 1HFY25.
 - Working in new products for Mexico and SE Asian (by FY26), Europe (by end this year).
 - For North America and South America will depend on greenfield project.
 - Overall expect exports momentum to start from 4Q and double-digit growth in FY26.
- **Margins drag due to merger and levers for improvement over mid term**
 - Amalgamated cos topline is ~Rs20b with nominal operating margin (breakeven) hence expect a margin drag of 1.5-2%.
 - RM cost is high in the merged entity as many products are imported while co will work on localization over 2-3 years.
 - Greenfield is important to drive localization – Have submitted EOI submitted to UP government for land parcel acquisition.
 - Synergy expected around manpower cost which is ~11% of sales will get rationalized.
 - Expect margins to be scaled back to 12-13% over 2-3 year (without railway business) and mid-teens for long term.
 - Seeing large growth from engines and the parts verticals ahead.
- **Channel expansion** – total dealer counts for the merged entity at ~1,550 as of Sep'24. Co indicated >1,200 (flat QoQ since 2 quarters) for Escorts while Kubota channel is ~300 dealers.
 - **Domestic tractor volume mix**
 - <40HP/>40HP – 34/66 (vs 34/66 QoQ and 41/49 YoY).
- **Expect to launch new product in Farmtrac in 41-50HP in Feb'25** in 2WD/4WD which will cover significant product gaps.
- **Revenue mix Post-Merger** - Tractor share of business (SOB) at ~83% (v/s 89% pre-merger) and Non tractor SOB is 17% (v/s 11%). Increase in non-tractor segment is led by addition of global sourcing vertical for Kubota.
- Capacity utilization at 73% in 2QFY25. Current capacity is ~170k and production of ~125-130k leaving out limited scope for further growth. Hence there is need for greenfield.

Escorts Kubota Ltd (ESCORTS)

- EKL's domestic market share at ~11.8% in 2QFY25 (vs ~11.2% in 1QFY25, ~11.8% in 2QFY24).
- Have setup 58,000 Sq. ft + facility for components exporting to Kubota Group.
- Agri implements to post healthy growth – Escorts was primarily focus on Rotavators with Kubota integration the product portfolio expanded to combined harvesters, rice transplanters, sprayers, super seeders which should support overall growth.

Construction equipment

- **Outlook** – Expect 2HFY25 volumes to better than 1HFY25. Expect pre buy ahead of BSI norms from Jan'25 which should support volumes.
 - Served industry volumes degrew ~2% YoY to 16,700 units
- In 2QFY25, BHL Industry up by 2.3% YoY, PnC Industry declined 17.7% YoY, compactors industry grew by 0.3% YoY, mini excavators declined 1.6% YOY. EKL's CE volume declined 18.4% YoY at 1,394 units.
- Capacity utilization at ~68% in 2QFY25 (vs ~55% in 1QFY25 and ~70% in 4QFY24).
- Margins levers are – operating leverage and volumes led by infra push where EKL play for ~50% of the market, Backhoe loaders – product is worked out for exports along with meeting BS5 emission, Crane – product portfolio is worked as per MTBP.
 - Will have benefit of NBFC in driving volumes in the retail segment (especially backhoe loaders).
- Expect CE margins to be at best early double don't expect uptick towards mid-teens.

Railways

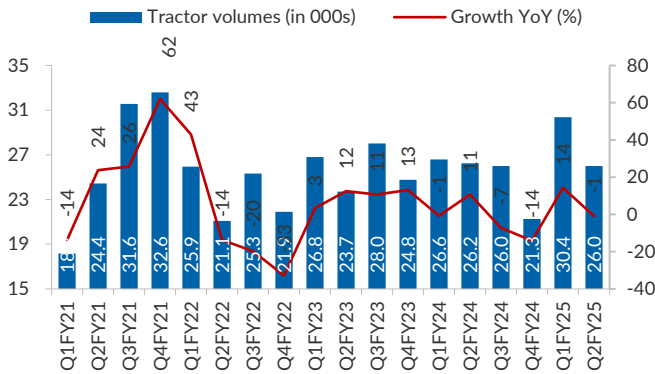
- Railway Equipment Division have >Rs11b of order book in 2QFY25 include BMBS orders for ~Rs3.82b supplies of which have temporarily been on hold by RDSO.

Financials

- Expect captive finance NBFC to be operational in FY25 itself as expect RBI approval is likely.
- EKL repaid the debt of Rs3.47b of merged entity EKI and KAM.
- Have taken price hike in 1QFY25 in anticipation of some spike in NR. Overall RM impact is not significant for 2QFY25.
- Higher manpower cost was led by higher contractual labor cost in anticipation of higher volumes ahead of festive.
- Tax rate – benefits of all the carry forwarded losses have been part of P&L. ETR expected at 22-23% for FY25.

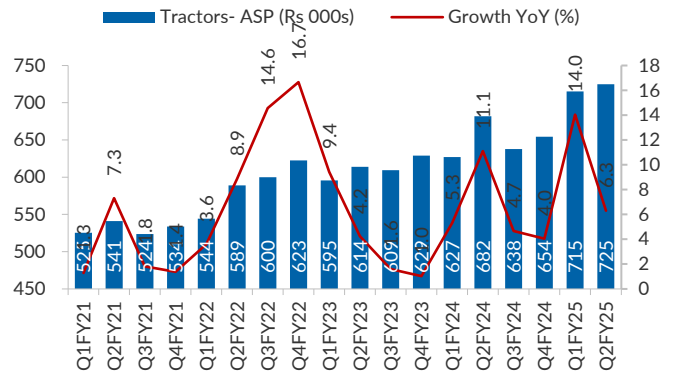
CHARTS

Exhibit 1: Tractor volume fell 0.9% YoY/-14.4% QoQ



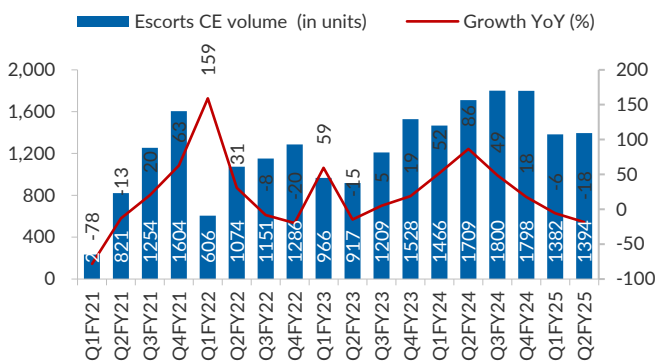
Source: Company, YES Sec

Exhibit 2: ASPs grew 6.3% YoY led by price hikes, mix



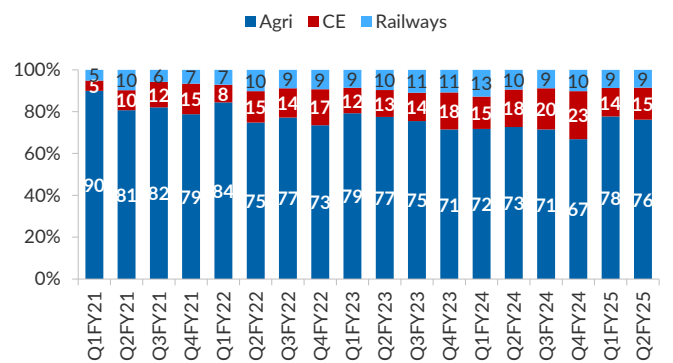
Source: Company, YES Sec

Exhibit 3: CE volumes fell 18.4% YoY/+0.9 QoQ



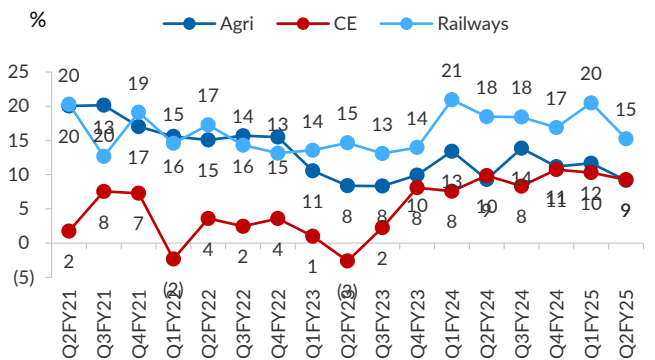
Source: Company, YES Sec

Exhibit 4: Segment wise revenue share trend



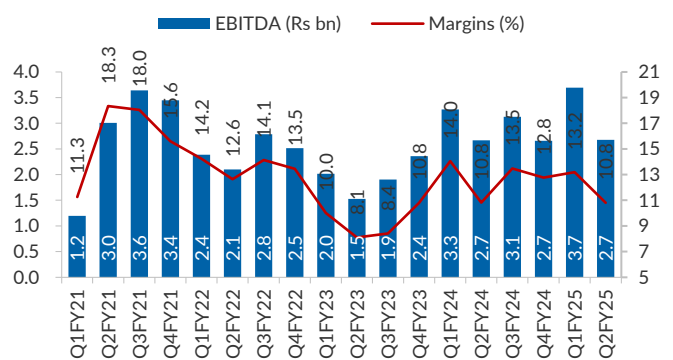
Source: Company, YES Sec

Exhibit 5: Trend in segmental margins



Source: Company, YES Sec

Exhibit 6: EBITDA margin contracted ~240bp QoQ



Source: Company, YES Sec

FINANCIALS

Exhibit 7: Balance Sheet

Y/E March	FY22	FY23	FY24	FY25E	FY26E	FY27E
Equity Share Capital	1,319	1,319	1,105	1,226	1,226	1,226
Total Reserves	74,680	80,548	90,658	101,011	113,079	127,372
Net Worth	75,999	81,867	91,763	102,237	114,305	128,598
Minority Interest	-38	-39	-39	-39	-39	-39
Deferred Liabilities	373	646	1,149	1,213	1,286	1,372
Total Loans	-	-	42.00	42.00	42.00	42.00
Capital Employed	76,334	82,475	92,915	103,452	115,594	129,973
Gross Block	29,973	31,687	32,666	33,713	34,835	36,034
Less: Accum. Deprn.	12,389	13,573	14,502	16,162	17,875	19,647
Net Fixed Assets	17,585	18,114	18,164	17,552	16,959	16,387
Capital WIP	878	1,137	1,515	1,414	1,594	1,804
Total Investments	49,184	48,465	52,746	55,383	58,152	61,060
Curr. Assets, Loans&Adv.	23,431	33,135	40,244	50,733	63,278	78,317
Inventory	8,466	12,177	12,181	15,163	17,073	19,233
Account Receivables	7,926	11,797	11,732	15,494	17,470	19,767
Cash and Bank Balance	2,718	4,719	11,790	14,627	22,195	31,469
Loans and Advances	4,320	4,442	4,542	5,450	6,540	7,848
Curr. Liability & Prov.	14,743	18,375	19,754	21,630	24,389	27,595
Account Payables	13,341	16,912	18,156	19,665	22,174	25,089
Provisions	1,402	1,463	1,599	1,965	2,215	2,506
Net Current Assets	8,687	14,760	20,490	29,104	38,888	50,722
Deferred Tax assets	-	-	-	-	-	-
Appl. of Funds	76,334	82,475	92,915	103,452	115,594	129,973

Source: Company, YES Sec

Exhibit 8: Income statement

Y/E March	FY22	FY23	FY24	FY25E	FY26E	FY27E
Total Income from Operations	72,827	84,287	88,496	108,755	122,629	138,748
Change (%)	3.8	15.7	5.0	22.9	12.8	13.1
Total Expenditure	62,872	76,512	76,829	96,232	107,895	121,106
% of Sales	86.3	90.8	86.8	88.5	88.0	87.3
EBITDA	9,954	7,775	11,667	12,523	14,734	17,642
Margin (%)	13.7	9.2	13.2	11.5	12.0	12.7
Depreciation	1,321	1,501	1,669	1,659	1,714	1,772
EBIT	8,634	6,275	9,998	10,864	13,020	15,870
Int. and Finance Charges	150	133	137	130	124	118
Other Income	1,738	2,809	3,986	4,105	4,229	4,356
PBT bef. EO Exp.	10,222	8,951	13,847	14,839	17,125	20,108
EO Items	-	(530.50)	-	-	-	-
PBT after EO Exp.	10,222	8,421	13,847	14,839	17,125	20,108
Current Tax	2,572	1,979	3,519	3,704	4,279	5,024
Deferred Tax	-	-	-	63.67	73.55	86.37
Tax Rate (%)	25.2	23.5	25.4	25.4	25.4	25.4
Less: Mionrity Interest	294	75	-164	-164	-164	-164
Reported PAT	7,356	6,367	10,491	11,235	12,936	15,161
Adjusted PAT	7,356	6,772	10,491	11,235	12,936	15,161
Change (%)	(15.6)	(7.9)	54.9	7.1	15.1	17.2
Margin (%)	10.1	8.0	11.9	10.3	10.5	10.9

Source: Company, YES Sec

Exhibit 9: Cash Flow Statement

Y/E March (Rs mn)	FY22	FY23	FY24	FY25E	FY26E	FY27E
OP/(Loss) before Tax	9,928	8,346	14,010	14,815	17,115	20,098
Depreciation	1,321	1,501	1,669	1,659	1,714	1,772
Interest & Finance Charges	790	1,513	2,081	130	124	118
Direct Taxes Paid	(2,547)	(1,864)	(2,340)	(3,704)	(4,279)	(5,024)
(Inc)/Dec in WC	(6,526)	(4,102)	512	(5,777)	(2,217)	(2,559)
CF from Operations	2,966	5,393	15,932	7,124	12,457	14,403
Others	(2,644)	(3,154)	(5,610)	-	-	-
CF from Operating incl EO	323	2,239	10,322	7,124	12,457	14,403
(inc)/dec in FA	(1,759)	(2,132)	(1,751)	(946)	(1,301)	(1,409)
Free Cash Flow	(1,436)	107	8,571	6,178	11,155	12,994
(Pur)/Sale of Investments	(28,434)	6,702	(1,363)	-	-	-
Others	11,625	(5,187)	(6,165)	(2,637)	(2,769)	(2,908)
CF from Investments	(18,567)	(618)	(9,279)	(3,584)	(4,071)	(4,317)
Issue of Shares	19,021	206	135	121	-	-
Inc/(Dec) in Debt	(78)	(71)	(84)	-	-	-
Interest Paid	(98)	(91)	(101)	(130)	(124)	(118)
Dividend Paid	(737)	(757)	(758)	(858)	(858)	(858)
Others	(8)	-	42	164	164	164
CF from Fin. Activity	18,099	(712)	(767)	(704)	(818)	(812)
Inc/Dec of Cash	(145)	909	276	2,837	7,568	9,274
Opening Balance	1,057	915	1,822	11,790	14,627	22,195
Closing Balance	912	1,825	2,098	14,627	22,195	31,469

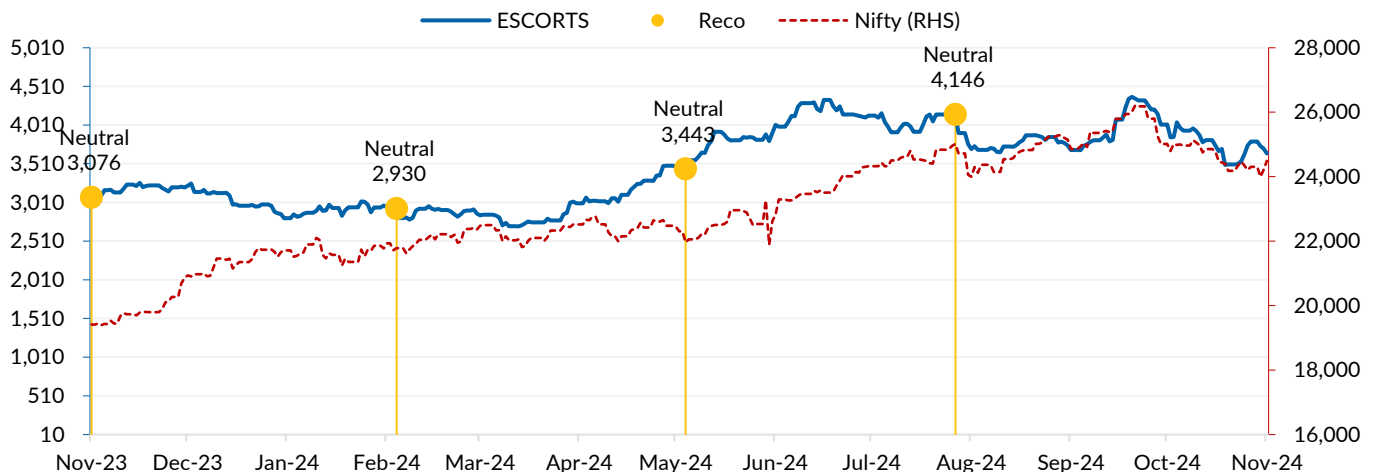
Source- Company, Yes Sec

Exhibit 10: Growth and Ratio matrix

Y/E March	FY22	FY23	FY24	FY25E	FY26E	FY27E
Basic (INR)						
EPS (ex treasury)	74.9	68.9	94.9	91.6	105.5	123.7
Cash EPS	88.3	84.2	110.0	105.2	119.5	138.1
BV/Share	773.6	833.3	830.4	833.9	932.3	1,048.9
DPS	7.0	7.0	7.0	7.0	7.0	7.0
Payout (%)	12.6	14.5	7.4	7.6	6.6	5.7
Valuation (x)						
P/E	48.7	52.9	38.4	39.8	34.5	29.5
Cash P/E	41.3	43.3	33.1	34.6	30.5	26.4
P/BV	4.7	4.4	4.4	4.4	3.9	3.5
EV/Sales	6.1	5.2	4.9	4.0	3.5	3.0
EV/EBITDA	44.6	56.8	37.3	34.5	28.8	23.5
Dividend Yield (%)	0.2	0.2	0.2	0.2	0.2	0.2
FCF per share	(10.9)	0.8	77.6	50.4	91.0	106.0
Return Ratios (%)						
RoE	11.7	8.6	12.1	11.6	11.9	12.5
RoCE	16.4	11.5	16.1	15.4	15.9	16.6
RoIC	32.2	18.6	27.1	27.5	29.6	34.2
Working Capital Ratios						
Asset Turnover (x)	1.0	1.0	1.0	1.1	1.1	1.1
Inventory (Days)	62.1	72.6	73.0	73.0	73.0	73.0
Debtor (Days)	39.7	51.1	48.4	52.0	52.0	52.0
Creditor (Days)	66.9	73.2	74.9	66.0	66.0	66.0
Working Cap. Turnover (Days)	29.9	43.5	35.9	48.6	49.7	50.6
Leverage Ratio (x)						
Current Ratio	1.6	1.8	2.0	2.3	2.6	2.8
Interest Cover Ratio	57.7	47.3	72.9	83.3	105.2	134.9
Debt/Equity	-	-	0.0	0.0	0.0	0.0

Source- Company, Yes Sec

Recommendation Tracker



Source - YES Sec

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Registration Nos.: CIN: U74992MH2013PLC240971 | SEBI Registration No.: NSE, BSE, MCX & NCDEX : INZ000185632 | Member Code: BSE - 6538, NSE - 14914, MCX - 56355 & NCDEX - 1289 | CDSL & NSDL: IN-DP-653-2021 | RESEARCH ANALYST: INH000002376 | INVESTMENT ADVISER: INA000007331 | Sponsor and Investment Manager to YSL Alternates Alpha Plus Fund (Cat III AIF) and YES Wealth Maximiser AIF (Cat III AIF) SEBI Registration No.: IN/AIF3/20- 21/0818 | AMFI ARN Code - 94338

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