November 21, 2017

Escorts Limited

Summary of rated instruments

Instrument*	Rated Amount (in Rs. crore)	Rating Action
Term Loans	176.3 (reduced from 202.5)	Rating upgraded from [ICRA]A (positive) to [ICRA]A+ (positive)
Fund-based Facilities	434.0 (reduced from 478.0)	Rating upgraded from [ICRA]A (positive)/[ICRA]A1 to [ICRA]A+ (positive)/[ICRA]A1+
Non-fund Based Facilities	398.0 (reduced from 419.0)	Rating upgraded from [ICRA]A1 to [ICRA]A1+
Unallocated Limits	119.2 (enhanced from 28.0)	Rating upgraded from [ICRA]A (positive)/[ICRA]A1 to [ICRA]A+ (positive)/[ICRA]A1+
Total	**1127.5**	**-**
Commercial Paper	100.0	Rating upgraded from [ICRA]A1 to [ICRA]A1+

*Instrument details are provided in Annexure-1

Rating action

ICRA has upgraded the long term rating assigned to the bank facilities of Escorts Limited (Escorts) from [ICRA]A (pronounced ICRA A) to [ICRA]A+ (pronounced ICRA A plus) [1]. The outlook on the long term rating remains 'Positive'. ICRA has also upgraded the short term rating assigned to the bank facilities and Rs. 100.0 crore commercial paper programme of the company from [ICRA]A1 (pronounced ICRA A one) to [ICRA]A1+ (pronounced ICRA A one plus). The total rated amount of bank facilities is Rs. 1127.5 crore[2].

Rationale

The rating upgrade takes into account the sustained improvement in the operational performance of Escorts, demonstrated through a healthy volume growth in its key business divisions – agri machinery and construction equipment. While favourable farm sentiments on the back of improvement in farm cash flows and various government support programmes has supported double digit volume growth in the agri machinery division, the construction equipment division has also benefitted from a improved outlook for investments in roads and select infrastructure sector. A ramp up in volumes for the agri machinery division, coupled with the rationalisation of material costs on account of various VA-VE efforts undertaken, have aided significant improvement in the division's profitability metrics. Escorts continues to be a leading tractor manufacturer in the country, aided by an established dealer network, financing tie-ups, regular product launches/refreshes and targeted marketing efforts. In the backdrop of an expectation of a healthy demand outlook for tractors, the division's efforts to further expand its dealership network in the Southern and Western regions are likely to support volume growth over the medium term. Although the division derives modest volumes from exports, expansion in international markets has been a focus area identified by the management and provides opportunities for growth in the medium term.

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[1] *For complete rating scale and definitions, please refer to ICRA's website www.icra.in or other ICRA Rating Publications.*

[2] *100 lakh = 1 crore = 10 million*

Even as the agri machinery division remains the largest division, a robust growth in demand in the construction equipment industry has helped Escorts' construction equipment business to record a healthy growth in volumes and report profits at the PBIT level in Q2 FY2018. The division has benefitted to an extent from economies of scale as well as commonisation of engines for certain products across the agri machinery and the construction equipment divisions.

The ratings assigned continue to factor in the company's long operating history, strong brand franchise, along with its healthy financial risk profile, characterized by negligible debt and strong debt coverage indicators. Despite an annual capital expenditure plans of around ~Rs 100-120 crore towards product development, the company's expected healthy cash accruals are expected to help support its strong financial risk profile going forward. The impact of any inorganic growth steps undertaken by the company, on the credit profile of the company, would continue to be monitored. ICRA also takes note of the inherent cyclicality in both the tractor and construction equipment industry, which remain the company's key business segments.

The positive outlook on the long term rating reflects ICRA's expectation that the government's plans to increase farm incomes and various initiatives to promoter investments in infrastructure development bode well for the tractors and construction equipment segments, and would help the company report healthy revenue and earnings growth over the medium term. The healthy cash accruals are expected to help the company improve its financial risk profile further.

Key rating drivers

Credit strengths

- **Strong brand franchise, vast dealer network and established track record of the company in the agri machinery business –** Escorts is one of the leading tractor manufacturers in the country, aided by an established dealer network, healthy financing tie-ups, regular product launches/refreshes and targeted marketing efforts. The company has an installed capacity of 100,000 tractors/year; the agri machinery division offers a wide range of tractors, primarily under two brands - Farmtrac and Powertrac. Apart from these two brands, the company also sells a low HP tractor (10-15 HP) through a joint venture with Rajkot based Adico Group (under the Steeltrac brand). Over the past 18 months, the company's agri machinery division has recorded a healthy growth in revenues and profits, largely benefitting from an improved industry demand driven by favourable in farm sentiments.
- **Presence in multiple product segments - agri machinery, construction equipment and railway equipment –** Escorts has a presence across various product segments viz., tractors and agri machinery manufactured and marketed by Agri Machinery Division (EAM); Construction equipments such as cranes, compactors and back hoe loader under Construction Equipment Division (ECE) and equipments for railways (shock absorbers for railway coaches, centre buffer couplers and brake systems) under Railway Equipment Division. Although the EAM division contributes a majority of the revenues and profits, the company's presence in other businesses provides avenues for growth going forward.

- **Sustainable improvement in cost structure driven by cost rationalization initiatives across various divisions –** Escorts has been focused on improving profitability and has implemented various cost rationalization exercises over the past few years; raw material costs have been reduced across divisions through vendor consolidation, price renegotiation, product re-designing and other VA-VE efforts. The company's operating profitability in the current fiscal has been stronger than the corresponding previous with higher profitability of the agri machinery division, which has benefitted from economies of scale and savings on account of various cost reduction measures.

Credit weaknesses

- **Agri machinery and construction equipment divisions remains exposed to cyclicality –** The company's leading business divisions - agri machinery and construction equipment, remain inherently cyclical in nature. While the agri machinery division remains exposed to fluctuations in demand scenario with sensitivity to monsoons and farmer sentiments, the construction equipment business growth remains strongly correlated to level of economic activity in the country. The government of India (GOI) however remains committed towards rural development and agri-mechanization, while also focusing on improving the infrastructure the country with enhanced budget allocations. The continued focus of the government is likely to aid growth in industry volumes in both the industries over the long term and provides comfort.
- **Market presence of the agri machinery division in the Southern and Western regions continues to remain weak** – The agri machinery division's presence in the western and southern regions continues to remain weak, which has limited the company's market share gain prospects over the past few years. The division has identified various markets in the Western and Southern regions, where the division would be ramping up its management interaction efforts as well as dealership penetration with a view of gaining market share. Its ability to gain market share in these markets remains critical, given the high growth potential of these regions.
- **Limited market share in the highly competitive construction equipment sector** – The company's product range in the construction equipment segment (cranes, compactors and backhoe loaders) remains limits, thereby constraining the company's growth prospects in the construction equipment sector. While a healthy growth in volumes in the current fiscal has helped the division break even at a PBIT level in Q2 FY2018, the division's ability to increase its scale of operations for it to contribute in a meaningful manner to the company's profitability remains to be seen.

Analytical approach: For arriving at the ratings, ICRA has applied its rating methodologies as indicated below:

Links to applicable criteria:
Corporate Credit Rating Methodology
Rating Methodology for Tractor Industry

About the company:
Escorts Limited (Escorts) was incorporated as Escorts (Agents) Private Limited (EAPL) in Lahore in 1944. EAPL was converted into a Public Limited Company and renamed Escorts Limited (Escorts) in January 1960. The company started off by manufacturing tractors under the Escorts brand name in the 25-40 horsepower (HP) range. In 1969, the company promoted Escorts Tractors Limited (ETL) as a joint venture with Ford Motor Company (FMC), USA for the manufacture of Ford Series of tractors in the 40-50 HP range. Escorts acquired the entire equity stake of ETL in August 1995, thus making ETL its subsidiary (subsequently merged with agri machinery division).

Over the years, the company diversified into other products to emerge as a multi-business entity with interests in agri-machinery, automotive components, railway equipment, industrial and construction equipment, and telecom equipment and services. However, some of the non-core businesses viz., Telecom, Healthcare, Software and its stake in joint venture with Carraro were divested during mid 2000s.

At present, Escorts is engaged in three major segments viz., Agri Machinery Division (EAM) engaged in manufacturing of tractors and agri-machinery; Construction equipment Division (ECL) engaged in manufacturing and trading of construction equipment products and Railway equipment comprising of shock absorbers for railway coaches, centre buffer couplers and brake systems. In December 2016, the company had sold of the assets of the auto products, thereby leading to the closure of the division. The company has six manufacturing facilities in Faridabad (Haryana) and one manufacturing facility each in Rudrapur (Uttaranchal) and Poland.

Key Financial Indicators (Standalone)

Indicator	FY2016	FY2017
Operating Income (Rs. crore)	3,366.8	4,093.2
PAT (Rs. crore)	83.7	160.4
OBDITA/OI (%)	5.2%	7.9%
ROCE (%)	6.6%	12.2%
Total Debt/ TNW (times)	0.2	0.1
Total Debt/ OPBDIT (times)	2.0	0.8
Interest coverage (times)	3.6	10.4
NWC/ OI (%)	-3.2%	-5.0%

OI: Operating Income; PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation; ROCE: PBIT/Avg (Total Debt + Tangible Net-Worth + Deferred Tax Liability - Capital Work - in Progress);
NWC: Net Working Capital
Source: Company Results

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for last three years:

Table:

S. No.	Instrument	Current Rating (FY2018)			Chronology of Rating History for the past 3 years			
		Type	Amount Rated (Rs. crore)	Date & Rating	Date & Rating in FY2017		Date & Rating in FY2016	Date & Rating in FY2015
				November 2017	March 2017	October 2016	March 2016	November 2014
1	Term Loans	Long Term	176.3	[ICRA] A+ (Positive)	[ICRA] A (Positive)	[ICRA] A- (Stable)	[ICRA] A- (Stable)	[ICRA] BBB+ (Stable)
2	Fund-based Facilities	Long Term/ Short Term	434.0	[ICRA] A+ (Positive)/ [ICRA]A1+	[ICRA] A (Positive)/ [ICRA]A1	[ICRA] A- (Stable)/ [ICRA]A1	[ICRA] A- (Stable)/ [ICRA]A1	[ICRA] BBB + (Stable) / [ICRA]A2
3	Non-fund Based Facilities	Short Term	398.0	[ICRA]A1+	[ICRA] A1	[ICRA] A1	[ICRA] A1	[ICRA] A2
4	Unallocated Limits	Long Term/ Short Term	119.2	[ICRA] A+ (Positive)/ [ICRA]A1+	[ICRA] A (Positive)/ [ICRA]A1	[ICRA] A- (Stable)/ [ICRA]A1	[ICRA] A- (Stable)/ [ICRA]A1	[ICRA] BBB + (Stable) / [ICRA]A2
5	Commercial Paper	Short Term	100.0	[ICRA]A1+	[ICRA] A1	[ICRA] A1	[ICRA] A1	-

Complexity level of the rated instrument:
ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website www.icra.in

Annexure-1
Instrument Details

Instrument	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
Term Loan -1	May 2013	-	July 2018	26.3	[ICRA]A+ (Positive)
Term Loan - 2	August 2015	-	September 2023	150.0	[ICRA]A+ (Positive)
Fund-based Facilities	-	-	-	434.0	[ICRA]A+ (Positive)/ICRA]A1+
Non-fund Based Facilities	-	-	-	389.0	[ICRA]A1+
Unallocated Limits	-	-	-	119.2	[ICRA]A+ (Positive)/[ICRA]A1+
Commercial Paper	Yet to be placed	-	-	100.0	[ICRA]A1+

Source: Escorts Limited

Contact Details

Analyst Contacts

Subrata Ray
+91 22 2433 1086
subrata@icraindia.com

Anupama Arora
+91 124 4545 303
anupama@icraindia.com

Rohan Kanwar Gupta
+91 124 4545 808
rohan.kanwar@icraindia.com

Relationship Contact

L. Shivakumar
+91 22 2433 1046
shivakumar@icraindia.com

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Registered Office
ICRA Limited
1105, Kailash Building, 11th Floor, 26, Kasturba Gandhi Marg, New Delhi 110001
Tel: +91-11-23357940-50, Fax: +91-11-23357014

Corporate Office
Mr. Vivek Mathur
Mobile: +**91 9871221122**
Email: vivek@icraindia.com

Building No. 8, 2nd Floor, Tower A, DLF Cyber City, Phase II, Gurgaon 122002
Ph: +91-124-4545310 (D), 4545300 / 4545800 (B) Fax; +91- 124-4050424

<table>
<tr><td>Mumbai
Mr. L. Shivakumar
Mobile: +91 9821086490
Email: shivakumar@icraindia.com

3rd Floor, Electric Mansion
Appasaheb Marathe Marg, Prabhadevi
Mumbai—400025,
Board : +91-22-61796300; Fax: +91-22-24331390</td><td>Kolkata
Mr. Jayanta Roy
Mobile: +91 9903394664
Email: jayanta@icraindia.com

A-10 & 11, 3rd Floor, FMC Fortuna
234/3A, A.J.C. Bose Road
Kolkata—700020
Tel +91-33-22876617/8839 22800008/22831411,
Fax +91-33-22870728</td></tr>
<tr><td>Chennai
Mr. Jayanta Chatterjee
Mobile: +91 9845022459
Email: jayantac@icraindia.com

5th Floor, Karumuttu Centre
634 Anna Salai, Nandanam
Chennai—600035
Tel: +91-44-45964300; Fax: +91-44 24343663</td><td>Bangalore
Mr. Jayanta Chatterjee
Mobile: +91 9845022459
Email: jayantac@icraindia.com

'The Millenia'
Tower B, Unit No. 1004,10th Floor, Level 2 12-14, 1 & 2,
Murphy Road, Bangalore 560 008
Tel: +91-80-43326400; Fax: +91-80-43326409</td></tr>
<tr><td>Ahmedabad
Mr. L. Shivakumar
Mobile: +91 9821086490
Email: shivakumar@icraindia.com

907 & 908 Sakar -II, Ellisbridge,
Ahmedabad- 380006
Tel: +91-79-26585049, 26585494, 26584924; Fax:
+91-79-25569231</td><td>Pune
Mr. L. Shivakumar
Mobile: +91 9821086490
Email: shivakumar@icraindia.com

5A, 5th Floor, Symphony, S.No. 210, CTS 3202, Range
Hills Road, Shivajinagar,Pune-411 020
Tel: + 91-20- 6606 9999; Fax: +91-20-25561231</td></tr>
<tr><td>Hyderabad
Mr. Jayanta Chatterjee
Mobile: +91 9845022459
Email: jayantac@icraindia.com

4th Floor, Shobhan, 6-3-927/A&B. Somajiguda, Raj
Bhavan Road, Hyderabad—500083
Tel:- +91-40-40676500</td><td></td></tr>
</table>