October 25, 2021

Escorts Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund-based – Working Capital Facilities	339.00	646.0	[ICRA]AA (Stable)/ [ICRA]A1+; Reaffirmed
Non-fund Based – Working Capital Facilities	356.00	281.0	[ICRA]A1+; Reaffirmed
Unallocated	255.00	23.0	[ICRA]AA (Stable)/ [ICRA]A1+; Reaffirmed
Total	**950.00**	**950.00**	

**Instrument details are provided in Annexure-1*

Rationale

The reaffirmation of the ratings factors in the continuation of Escorts' healthy operational performance, driven by robust volume and profitability expansion in its key business division of agri-machinery. Over the past few years, Escorts has been able to report a sustained healthy operational performance across business divisions, which has aided it in recording strong cash accruals. In FY2021, despite the adverse impact of the lockdowns following the spread of Covid-19, the company posted healthy topline growth of more than 20%. Revenues from its agri-machinery segment (EAM) and railway equipment division (RED) grew by27.7% and 0.4% YoY, respectively, while that from the construction equipment segment (ECE) declined by 7.6% YoY. Escorts benefitted from an overall improved scale of operations and saw a healthy improvement in operating profit margins (expansion of ~467 basis points in FY2021).

The EAM and ECE divisions are likely to record growth in revenues in the current fiscal on expectations of a continuation of healthy farm sentiments and strong infrastructure push by the government. The strong performance of the EAM division, in particular, will help Escorts offset any impact of a relatively weak performance of the ECE segment (impacted by the lockdown measures in Q1 FY2022) and the railway equipment division (order book inflow hit by the adverse impact of the pandemic on railways' operations)), while also helping it maintain healthy profitability and return indicators.

The ratings assigned continue to take into account the healthy financial risk profile of the company, characterised by robust capitalisation and coverage metrics (Debt/OPBDITA at 0.1 time and interest coverage at 84.5 times in FY2021). Strong cash and liquid investments of Rs. 2,826.3 crore and significant working capital buffer as on March 31, 2021 provide additional comfort.

ICRA notes the inherent cyclicality in both the EAM and ECE divisions, which remain the company's key business segments. However, the ratings assigned continue to take comfort from the company's established market share (11.3% market share in FY2021) and strong brand franchise in the EAM division, especially in the northern and central markets.

Escorts continues to be a leading tractor manufacturer in the country, aided by a well-entrenched dealer network, financing tie-ups, regular product launches/refreshes and targeted marketing efforts. While the company's market share in the southern and western markets in India is limited, its efforts to expand its dealership network in these regions are likely to support volume growth in these regions over the medium term. Even as the company's presence in the exports market remains relatively low, its collaboration with Kubota Corporation is expected to help it strengthen its business profile and ramp up exports over the medium term

Over the recent past, the company has been on the lookout for acquisitions to enhance its product profile, especially in the railway equipment division. As a part of its collaboration with Kubota Corporation, the company could also undertake significant investments in the agri-machinery/construction equipment segments to enhance its product profile. More clarity on the same is expected to emerge in the near future. The impact of any major investments/inorganic growth steps undertaken by the company on its credit profile would continue to be monitored.

The Stable outlook on the long-term rating reflects ICRA's opinion that Escorts would be able to report a moderate-to-healthy revenue and earnings growth over the medium term, benefitting from its established market position, collaboration with Kubota Corporation and the government's plans to increase agricultural income and promote infrastructure investment. The same is likely to help the company maintain a strong credit profile.

Key rating drivers and their description

Credit strengths

Leading tractor OEM in India with strong brand franchise, vast dealership network and established track record; collaboration with Kubota Corporation to aid exports ramp up – Escorts is one of the leading tractor manufacturers in the country (domestic market share of 11.3% in FY2021), aided by regular product launches/refreshes, an established dealership network, healthy financing tie-ups, and targeted marketing efforts. The company has an installed production capacity of 1,20,000 tractors/year and is in the midst of expanding its capacity. The EAM division offers a wide range of tractors, primarily under two brands, Farmtrac and Powertrac. Escorts also sells a low horsepower (HP) tractor (10-30 HP category) through a JV with the Rajkot-based Adico Group (under the Steeltrac brand). Over the past three fiscals, the company's EAM division has recorded healthy revenues and profits, benefitting from a healthy industry demand driven by favourable farm sentiments. The division recorded 20.7% YoY growth in revenues in FY2021 on the back of a good monsoon, stable crop prices, easy availability of finance, sufficient availability of water and healthy water reservoir levels.

Kubota Corporation, Japan, picked up stake in Escorts through a preferential share issue in 2020, and both the companies have two JVs in the Indian market. Given Escorts' limited presence in the exports market till date, its collaboration with Kubota Corporation, which is a well-established player in the global market, is likely to ramp up the company's exports. The collaboration is also likely to strengthen Escorts' product development capabilities and help it improve its product portfolio.

Presence in multiple product segments – Escorts has a presence across various product segments. These include agri-machinery equipment manufactured and marketed by its EAM division; construction equipment, such as cranes, compactors and back hoe loaders by its ECE division; and equipment for railways (shock absorbers for railway coaches, centre buffer couplers and brake systems) by its RED division. Although the EAM division drives majority of the company's revenues and profits, the company's presence in other businesses provides avenues for growth.

Strong financial risk profile characterised by negligible debt and superior liquidity profile – The financial risk profile of the company remains strong, characterised by a conservative capital structure and strong debt coverage indicators (TD/OPBITDA of 0.1 time and interest coverage of 84.5 times as on March 31, 2021). Additionally, the company continues to maintain healthy cash and bank balances (unencumbered cash and liquid investment reserve of ~Rs. 2,826.3 crore as on March 31, 2021), resulting in a superior liquidity profile. Escorts has been able to maintain healthy profitability and return indicators over the past few years. The operating margin improved to 16.1% in FY2021, benefitting from the economies of scale, favourable product mix and various cost efficiency measures. Going forward, while Escorts has capex plans towards capacity expansion, the same are likely to be largely funded through existing cash balances and future cash accruals, keeping the credit profile strong.

Credit challenges

EAM and ECE divisions exposed to cyclicality – The company's leading business divisions - EAM and ECE – are inherently cyclical in nature. While the EAM division remains exposed to the fluctuations in demand with sensitivity to monsoons and farmer sentiments, growth in the ECE division is strongly correlated to the level of economic activity in the country. The Government of India (GoI), however, remains committed to rural development and agri-mechanisation, while focusing on improving the infrastructure with enhanced budgetary allocations. While government focus is likely to aid growth in industry volumes across both divisions over the medium to long term, the company is likely to remain exposed to periods of downturn in demand in the key end-user industries. In FY2021, while there was a strong demand recovery in the EAM segment following the disruptions caused by the lockdowns, the performance of the ECE division was impacted to a certain extent.

Market presence of EAM division in southern and western India limited – Even as the company has strengthened its business position over the past few years, its market share in the western and southern regions remains limited, restricting the company from ramping up its market share at a pan-India level. The company has identified various markets in the western and southern regions, where the division has ramped up its management interaction efforts as well as dealership penetration to gain market share. Additionally, the management remains focussed on launching new application targeted products to plug any gaps in its product portfolio. Escorts' ability to gain market share in these regions is critical, given their high growth potential.

Limited market share in the highly competitive construction equipment sector – The company has a limited product range in the construction equipment segment (cranes, compactors and backhoe loaders), constraining growth prospects in the sector. While various cost-control measures over the past few fiscals have helped the division report profit at the PBIT level, its ability to increase its scale of operations for it to contribute in a meaningful manner to the company's profitability remains to be seen. In FY2021, the disruptions caused by the lockdowns impacted the division's performance. The division was adversely affected again in Q1 FY2022 due to the second wave of Covid-19. Escorts and the Tadano Group, Japan's biggest and the world's leading mobile crane manufacturer, entered into a JV to manufacture rough terrain cranes and truck mounted cranes. The JV is likely to help strengthen Escorts's market presence in the material handling equipment space over the medium to long-term.

Liquidity position: Superior

Escorts' liquidity is superior**,** with cash and liquid investments of Rs. 2,826.3 crore and significant working capital buffer as on March 31, 2021. The company is expected to incur capex of Rs. 300-325 crore in FY2022 and does not have any material long-term debt on its books. Going forward, Escorts is expected to meet its capex requirements and debt obligations over the near term from internal sources, and yet be left with sufficient cash surplus.

Rating sensitivities

Positive factors – The rating may be revised upwards if the company further strengthens its market share meaningfully in the domestic tractor and farm equipment segment, aided by product launches, market share traction in geographies where it has a relatively limited presence and technological support through the tie-up with Kubota Corporation. The company's ability to maintain comfortable profitability and credit metrics on a sustained basis will also be considered favourably.

Negative factors – The rating may be revised downwards if the company is not able to sustain the improvement in its operating profitability demonstrated over the past few years, leading to a significant deterioration in its return indicators and credit metrics. The adverse impact of any acquisition undertaken by the company on its financial risk profile could also exert downward pressure on the rating.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Tractor Manufacturers
Parent/Group Support	Not Applicable

Analytical Approach	Comments
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of Escorts Limited. As on March 31, 2021, the company had six subsidiaries, an associate company and four JVs, which are enlisted in Annexure-2.

About the company

Incorporated in 1944, Escorts Limited is a leading tractor and farm equipment OEM in India with an 11.3% market share in the domestic market (FY2021). The company generates business from its three key divisions — agri-machinery (EAM) engaged in manufacturing tractors (~82% of revenues in FY2021), construction equipment (ECE) involved in manufacturing and trading construction equipment products (~11%), and the railway equipment division (RED), which manufactures shock absorbers for railway coaches, centre buffer couplers and brake systems (~7%). The company has manufacturing facilities in Faridabad (Haryana), Rudrapur (Uttarakhand) and Poland.

The EAM segment manufactures and markets its tractors under the Farmtrac, Powertrac and Steeltrac brands and commands a strong presence in the northern and central regions, aided by strong brand recall and a well-entrenched dealership network. The company's product portfolio spans HP segments with healthy presence in the 31-50 HP category.

Escorts has entered into a collaboration with Kubota Corporation, wherein after establishing a manufacturing JV, the latter has acquired an equity stake in Escorts through a preferential issue.

The ECE segment manufactures as well as trades construction, material handling and earth moving equipment. The division's manufactured product range includes pick-and-carry cranes (PNC), compactors and back-hoe loaders, etc.

The company was promoted by Delhi NCR-based Nanda family. Mr. Nikhil Nanda is the current chairman and managing director of the company. The company's board comprises 12 members, of whom six are independent directors.

Escorts was incorporated as Escorts (Agents) Private Limited (EAPL) in Lahore in 1944. EAPL was converted into a public limited company and renamed as Escorts in January 1960. The company started off by manufacturing tractors under the Escorts brand in the 25-40 HP range. In 1969, the company promoted Escorts Tractors Limited (ETL) as a JV with Ford Motor Company (FMC), US, for manufacturing the Ford Series of tractors in the 40-50 HP range. Escorts acquired the entire equity stake of ETL in August 1995, making ETL its subsidiary (subsequently merged with the 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, construction equipment, and telecommunication equipment and services. However, some of its non-core businesses, such as telecommunications, healthcare, software and its JV stake with Carraro were divested during the mid-2000s. In December 2016, the company sold off its auto product assets, leading to the closure of the division.

Key financial indicators (audited)

Consolidated	FY2020	FY2021	Q1 FY2022
Operating Income (Rs. crore)	5,810.1	7,014.4	1,701.8
PAT (Rs. crore)	472.8	872.4	188.8
OPBDIT/OI (%)	11.4%	16.1%	13.9%
PAT/OI (%)	8.1%	12.4%	11.1%
Total Outside Liabilities/Tangible Net Worth (times)	0.6	0.4	NA
Total Debt/OPBDIT (times)	0.1	0.1	NA
Interest Coverage (times)	38.5	84.5	67.9

PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2022)				Chronology of Rating History for the past 3 years					
		Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating	Date & Rating in FY2021		Date & Rating in FY2020		Date & Rating in FY2019	
					Oct 25, 2021	Mar 31, 2021	Sep 17, 2020	Mar 30, 2020	Jul 19, 2019	Mar 28, 2019 Oct 4, 2018	Jul 19, 2018
1	Fund-based- Working Capital Facilities	Long Term/ Short Term	646.0	-	[ICRA]AA (stable)/ [ICRA]A1+	[ICRA]AA (stable)/ [ICRA]A1+	[ICRA]AA (stable)/ [ICRA]A1+	[ICRA]AA- &/ [ICRA]A1+	[ICRA]AA- (stable)/ [ICRA]A1+	[ICRA]AA- (stable)/ [ICRA]A1+	[ICRA]AA- (stable)/ [ICRA]A1+
2	Non-fund based- Working Capital Facilities	Short Term	281.0	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
3	Unallocated Limits	Long Term/ Short Term	23.0	-	[ICRA]AA (stable)/ [ICRA]A1+	[ICRA]AA (stable)/ [ICRA]A1+	[ICRA]AA (stable)/ [ICRA]A1+	[ICRA]AA- &/ [ICRA]A1+	[ICRA]AA- (stable)/ [ICRA]A1+	[ICRA]AA- (stable)/ [ICRA]A1+	-
4	Commercial Paper	Short Term	-	-	-	[ICRA]A1+ Withdrawn	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long Term/Short Term - Fund-based- Working Capital Facilities	Simple
Short Term - Non-fund based-Working Capital Facilities	Very Simple
Long Term/Short Term - Unallocated Limits	Not Applicable

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional, or legal aspects. Details on the complexity levels of the instruments, is available on ICRA's website: www.icra.in

Annexure-1: Instrument details

ISIN No/Banker Name	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (RS Crore)	Current Rating and Outlook
NA	Fund-based- Working Capital Facilities	-	-	-	646.0	[ICRA]AA (stable)/[ICRA]A1+
NA	Non-fund based- Working Capital Facilities	-	-	-	281.0	[ICRA]A1+
NA	Unallocated Limits	-	-	-	23.0	[ICRA]AA (stable)/[ICRA]A1+

Source: *Company*

Annexure-2: List of entities considered for consolidated analysis

Company Name	Escorts Ownership	Consolidation Approach
Escorts Finance Limited	69.42%	Full Consolidation
Escorts Securities Limited	51.26%	Full Consolidation
Escorts Benefit & Welfare Trust	100.00%	Full Consolidation
Escorts Benefit Trust	100.00%	Full Consolidation
Farmtrac Tractors Europe Spolka z.o.o	100.00%	Full Consolidation
Escorts Crop Solution Limited	100.00%	Full Consolidation
Adico Escorts Agri Equipment Private Limited	40.00%	Equity Method
Tadano Escorts India Private Limited	49.00%	Equity Method
Escorts Kubota India Private Limited	40.00%	Equity Method
Kubota Agricultural Machinery India Private Limited	40.00%	Equity Method
Escorts Consumer Credit Limited	29.40%	Equity Method

Source: *Annual report FY2021*

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