March 30, 2020

Escorts Limited: Long-term rating placed on watch with developing implications; short term rating reaffirmed

Summary of Rated Instrument

Instrument*	Rated Amount (Rs. crore)	Rating Action
Fund-based - Working Capital Facilities	339.0	[ICRA]AA- &; Rating placed on watch with developing implications; [ICRA]A1+ Reaffirmed
Non-fund Based - Working Capital Facilities	341.0	[ICRA]A1+ Reaffirmed
Unallocated	270.0	[ICRA]AA- &; Rating placed on watch with developing implications; [ICRA]A1+ Reaffirmed
Total	**950.0**	
Commercial Paper	200.0	[ICRA]A1+ Reaffirmed

Material Event

The board of directors of Escorts Limited (Escorts) in their meeting held on March 20, 2020, provided in-principle approval for the following:

- Kubota Corporation, a leading global tractor and machinery manufacturer from Japan, would invest in Escorts Limited through a preferential issue of 12,257,688 equity shares for a total investment of Rs. 1,041.9 crore (representing a premium of 48.21% over the last traded price as of March 19, 2020). Simultaneously, an equivalent amount of shares held by Escorts Benefit and Welfare Trust (treasury shares with Escorts Limited being the ultimate beneficiary), would be cancelled, subject to necessary approvals and completion of the preferential allotment to Kubota Corporation. Kubota Corporation would consequently hold 10% of the equity stake in Escorts (post the capital reduction exercise). There will be no secondary stake sale by promoters in the transaction, and the operating control would continue with the Nanda family; Kubota would have right to nominate two non-executive board members.
- Furthermore, as part of the collaboration, Escorts also agreed to acquire a 40% stake in Kubota Agricultural Machinery Private Limited (marketing and sales company of Kubota Corporation in India) at a consideration of Rs. 90 crore. The existing 60:40 joint venture between Kubota Corporation and Escorts named Escorts Kubota India Pvt. Ltd. (manufacturing entity) will continue as planned earlier.

The transaction is expected to be completed in H1 FY2021, post receipt of the requisite stakeholder and regulatory approvals.

Impact of the Material Event

The long-term rating has been placed on watch as the aforesaid development is likely to have a positive impact on the credit profile of Escorts, the extent of which would be ascertained over a period of time, given the nascent stage of developments and lack of complete information. Escorts and Kubota Corporation have collaborated for establishing Escorts as a leading player in the Indian tractor market, while also establishing a hub for product development, manufacturing and sourcing for global markets (leveraging on the existing channel of Kubota Corporation). The equity participation by Kubota Corporation, a leading global agricultural machinery manufacturer, is likely to aid in strengthening Escorts' product development capabilities and help the latter enrich its product profile over the medium term. The funds infused via the preferential allotment are likely to further support Escorts in strengthening its business profile by supporting its capacity and network expansion plans over the medium term. Accordingly, the development is a credit positive in ICRA's view.

On account of the ongoing lockout across the country (a result of the Covid-19 pandemic), however, the near-term demand outlook remains uncertain. Even as sales in the near-term would be adversely impacted by the outbreak, the strong liquidity position of Escorts, as characterised by negative net debt position and substantial undrawn credit lines, provides comfort and financial flexibility. The receipt of funds post the conclusion of the preferential issue, is also likely to further strengthen the company's liquidity profile.

ICRA would continue to monitor the developments related to the preferential issue, and take appropriate rating action, post analysing the impact of the same on Escorts' credit profile.

The previous detailed rating rationale is available on the following link: Click here

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About ICRA Limited:

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