



Ref/EL/SEC/DISC//2016

Date: November 10, 2016

The Manager
Listing Department
National Stock Exchange of India Limited
5th Floor Exchange Plaza
Bandra Kurla Complex, Bandra East
Mumbai -400051

NSE Code: Escorts
BSE Code: 500495
DSE Code: 00012

Dear Sir

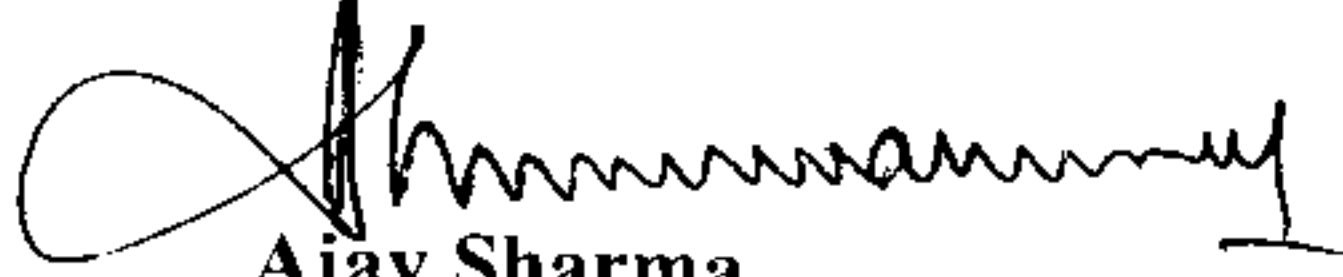
Sub: India Ratings Upgrades Escorts to 'IND A'/Stable

In compliance of the *Regulation 30 (6)* of the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015, we wish to inform you that M/s India Ratings & Research, a Fitch Group Company (Ind-RA) has upgraded and assigned the **Long term rating** to '**IND A**' from '**IND A-**'. A copy of letter dated November 10, 2016, released today by rating agency is annexed herewith for your reference and record.

This is for your information & record.

Thanking you,

Yours Faithfully
For **ESCORTS LIMITED**


Ajay Sharma
Group General Counsel
& Company Secretary

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Corporate Identification Number - L74899HR1944PLC039088

India Ratings Upgrades Escorts to 'IND A'/Stable

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By Chandan Sharma

NOV 2016

India Ratings and Research (Ind-Ra) has upgraded Escorts Limited's Long-Term Issuer Rating to 'IND A' from 'IND A-'. The Outlook is Stable. A full list of rating actions is at the end of this commentary.

KEY RATING DRIVERS

Revival in Volumes in FY17: Escorts' tractor volumes grew 21% yoy during 1HFY17 (1HFY16: negative 19.9%). Ind-Ra expects the growth trend to continue and to lead to an improvement in revenue and profitability and thus credit metrics in FY17. In 1HFY17, Escorts reported revenue of INR20.7bn (1HFY16: INR18bn) with EBITDA margins at 7.3% (4.7%) and net income at INR782m (INR450m).

Better-than-expected Credit Profile in FY16: Escorts' credit metrics was better than Ind-Ra's expectation in FY16, supported by a decline in overall debt levels to INR3.5bn in FY16 from INR4.8bn in FY15 (1HFY17: INR2.6bn) because of lower working capital and term debt requirements. Escorts reported net adjusted debt/EBITDA of 1.5x in FY16 (FY15: 2.4x) and gross interest coverage of 3.1x (2.8x). The improvement in metrics was despite a tractor volume decline of 13.9% in FY16 (FY15: negative 13.3%). Although any decline in volumes in future could affect the credit metrics negatively, the impact would be partly offset by the company's limited capex and short working cycle. Over FY12-FY16, net adjusted debt/EBITDA was below 2.5x while net interest coverage was above 2.9x.

Short Working Capital Cycle; Limited Capex: Escorts' working capital cycle in its main agri segment is short, keeping the overall cycle low. The company has sufficient capacity to fulfil its growth requirements in the medium term. With limited capex, Ind-Ra expects the cash flow from operations (CFO) as well as free cash flow to improve, aiding deleveraging. CFO was positive but volatile over FY12-FY16 due to varying working capital requirements. Free cash flow was also volatile during the same period owing to varying CFO. The company's use of the fund-based working capital was around 56% on an average over the 12 months ended September 2016.

Volatility in Tractor Volumes: The tractor industry volume growth has been volatile as the demand has a strong correlation with domestic agriculture sector output which depends upon monsoon and crop prices among other factors. The industry saw a volume decline of around 9% in FY16 (FY15: negative 10%). However, with normal monsoon this year, the industry volumes grew 17.4% yoy during 1HFY17. Industry volumes grew at a CAGR of 5% over FY07-FY16. The growth is likely to increase, driven by a gradual increase in farm mechanisation levels as well as an increase in the penetration of tractors, government impetus on increasing farm productivity and increased usage of tractor for non-farm activities. However, tractor volume growth would remain volatile depending on monsoons.

Focus on Key Segments to Augment Market Share: Escorts is the fourth-largest tractor manufacturer in India. Its market share marginally declined over FY13-FY16, driven by increasing competition as well as limited presence in the southern markets. In particular, the company has lost market share in the 41-50HP segment (FY16: 10.9%; FY15: 9.7%; FY13: 13.1%), which accounts for around 46% of the industry volumes. On an overall basis, the

company's domestic market share declined to 10.3% in FY16 from 11.6% in FY13. However, the company has launched specific products catering to haulage applications and to each of the industry sub-segment to capture market share. Escorts is also focussing on improving its product portfolio in the underpenetrated southern and western markets.

Cost Structure Initiatives; VRS Impact in Short Term: Escorts has initiated projects across its various segments to improve its cost structure by reducing material consumption and labour costs and improving supply chain efficiency. In FY16, it reported EBITDA losses of 15.1% (FY15: negative 20.6%; FY14: 12.4%) and 4.9% (3.3%, 2.7%) in its auto ancillary and construction equipment segments, respectively. However, the agri machinery and railway products segment reported EBITDA margins of 9.1% in FY16 (FY15: 8.1%; FY14: 10.3%) and 13% (11.4%; 7.7%). Ind-Ra's analysis indicates that Escorts' EBITDA margins are below the industry benchmarks, primarily due to high overhead and wage costs. However, the company has planned a reduction in wage costs through the voluntarily retirement scheme (VRS). Although this will impact the cash outflow in the near term, it will help improve the cost structure in the long term.

Divestment of Auto Business, One-offs: Escorts divested its loss-making auto division business in 1HFY17. The divestment is part of the company's long-term strategy to improve overall profitability. The divestment is likely to be cash neutral for the company as inflows from the sale will be used to pay off the liabilities associated with the auto division. Escorts has faced legacy issues in the past in terms of write-offs of inventory/assets/investments which have impacted its financial profile. The company can face such issues (write-offs/exceptional items) due to contingent liabilities or the divestment of auto business, in addition to the VRS related costs. However, Ind-Ra expects the cash flows of the company to be sufficient to absorb such losses/one-offs (up to a certain extent) without materially impacting the credit profile. However, a significant increase in one-offs could impact the credit profile negatively.

RATING SENSITIVITIES

Positive: Sustenance/ improvement in the market share along with an improvement in the revenue and profitability resulting in sustenance/improvement in the credit metrics could lead to a positive rating action.

Negative: A negative rating action could result from a decline in the revenue and profitability and/or debt-led capex leading to deterioration of the credit metrics with net adjusted debt/EBITDA being sustained over 2.5x.

COMPANY PROFILE

Escorts has an installed capacity of 100,000 tractors/year. It offers a wide range of tractors under two brands Famtrac and Powertrac. The company has presence in other segments such as construction equipment, auto and railway products. It has six plants in India - five in Faridabad and one in Haryana. It has a subsidiary in Poland with an installed capacity of 2,500 tractors/year. In FY16, the agri segment accounted for 79% of the revenue, construction equipment accounted for 12.7%, railway equipment accounted for 5.7% and auto ancillary accounted for 2.6%.

Escorts' ratings:

- Long Term Issuer Rating: upgraded to 'IND A' from 'IND A-'; Outlook Stable
- INR2,300m term loans (reduced from INR2,961.9m): upgraded to 'IND A'/Stable from 'IND A-'/Stable
- INR5,060m fund-based working capital limits: upgraded to 'IND A'/Stable from 'IND A-'/Stable and 'IND A1' from 'IND A2+'
- INR4,190m non-fund-based working capital limits (reduced from INR6,580m): upgraded to 'IND A'/Stable from 'IND A-'/Stable and 'IND A1' from 'IND A2+'

SOLICITATION DISCLOSURES

Additional information is available at www.indiaratings.co.in. The ratings above were solicited by, or on behalf of, the issuer, and therefore, India Ratings has been compensated for the provision of the ratings.

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Rating Outstanding

(As on 10/Nov/2016)

Long Term Issuer Rating	IND A / Stable	
Fund Based Working Capital Limit	IND A1	INR 5060 m
Fund Based Working Capital Limit	IND A / Stable	INR 5060 m
Non-Fund Based Working Capital Limit	IND A1	INR 4190 m
Non-Fund Based Working Capital Limit	IND A / Stable	INR 4190 m
Term loan	IND A / Stable	INR 2300 m

Applicable Criteria

Corporate Rating Methodology

Analyst Names

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