Management
Discussion & Analysis

Global Economy:

The global economy strengthened during the second half of 2013-14 and is expected to improve further in 2014-15, with much of the impetus being generated from advanced economies. Emerging economies faced several challenges, especially the ones with higher inflationary pressures and wider current account deficits. Some of them have tightened macroeconomic policies to shore-up confidence and strengthen their commitment to policy objectives.

Looking ahead, the global growth is projected to increase from 3.6 percent in 2013-14 to 3.9 percent in 2014-15. In advanced economies, growth is expected to increase to about 2.25 percent in 2014-15, an improvement of about 1 percentage point. Key drivers comprise reduction in fiscal tightening and highly accommodative monetary conditions. Growth will be strongest in the United States at about 2.7 percent amongst advance economies. Growth is projected to be positive but varied in the European region: stronger in the core, but weaker in other countries, especially with high debt levels. Across developing economies, growth is projected to pick up gradually from about 5 percent in 2013-14. Growth will be helped by stronger external demand from advanced economies.

Source: World Economic Outlook

Indian Economy:

The Indian economy is likely to grow by 5.6 percent in 2014-15. Economic growth is likely to be contributed majorly by the industrial sector, which is estimated to grow by 4.1 percent. Within the industrial sector, the manufacturing and construction sub-sectors are expected to grow at 3.3 percent and 5.6 percent, respectively. The last fiscal witnessed significant currency volatility, concerns on current account deficit and budget deficit, stalled projects and policy log-jam. Policy measures taken by RBI have helped reduce the volatility. Curb on gold imports dramatically cut down the current account deficit and helped the rupee strengthen. Despite RBI measures on the interest rates, CPI still remains at 8.6 percent, which was primarily fuelled by food and agri products; hence agri output remains a key focus area of the government.

1. Escorts Agri Machinery

The Indian tractors market witnessed robust growth in the fiscal gone by with demand from both agricultural and non-agricultural usage.

The key factor boosting tractor demand comprised strong rural liquidity, which in turn was a result of record production in 2011-12, healthy realisations for 2012-13 crop and collective buying of wheat by the government and private traders. The Minimum Selling Prices (MSPs) increased between 5-20 percent for various Rabi crops.

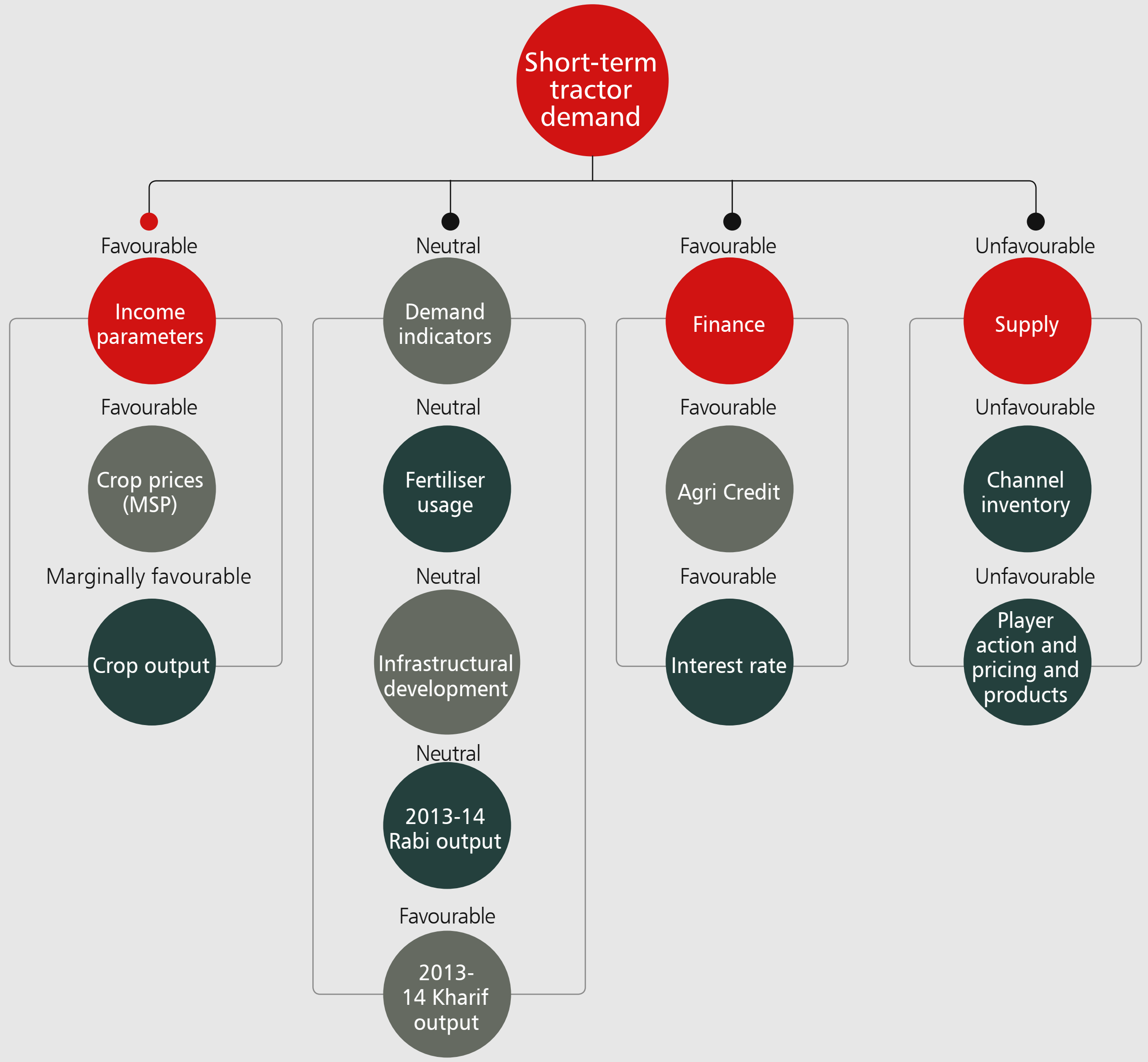
Improved credit environment, continuance of replacement demand and increased usage of tractors for non-agricultural purposes (for haulage in construction and infrastructure projects) were some of the other factors that contributed to improving tractor demand.

With increasing employment avenues like infrastructure projects and rural employment schemes, availability of labour for agricultural activities continued to decline, which is prompting farmers with medium-sized land holdings to either rent or purchase tractors.

Industry Outlook

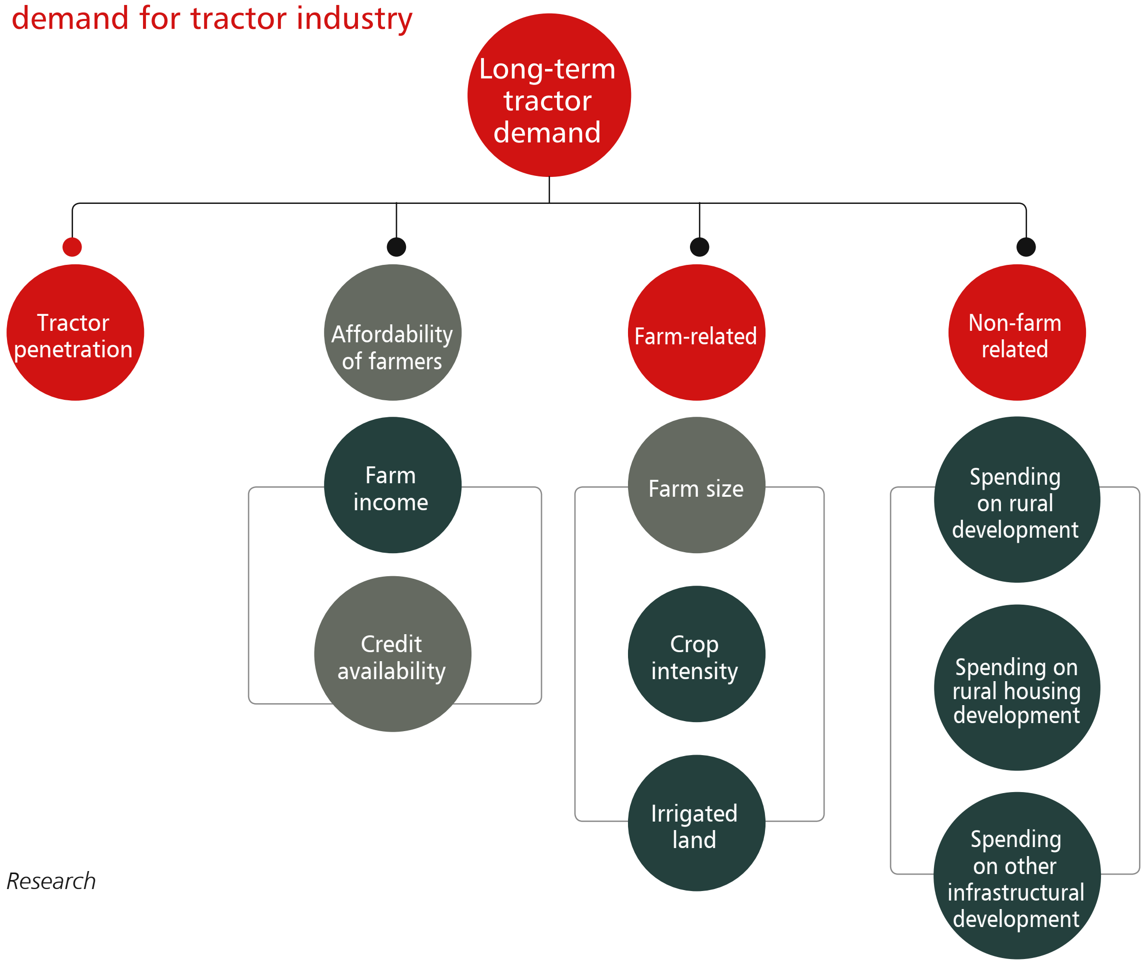
Demand for tractors is mainly driven by the farmer's ability to purchase a tractor and is affected both, directly and indirectly by a number of factors.

Short term demand for tractor industry



Note: Factors analysed while assessing tractor demand for 2013-14 are classified as favourable, neutral and unfavourable.
Source: CRISIL Research

Long term demand for tractor industry



Source: CRISIL Research

Key measures taken by the government in the agri sector allows 100% FDI under the automatic route in storage and warehousing, including cold storages, allocation of USD 145.8 billion which is around 8 percent of the GDP for agriculture credit and a total proposed outlay of USD 4.31 billion from the Ministry of Agriculture is expected to provide the much needed boost for the sector.

Going forward, agriculture export is likely to cross USD 45 billion, whereas agricultural credit is expected to exceed the target of ₹ 7 lakh cr. Such indicators help portray the huge potential of this sector which is crucial given the size and the future growth of the country.

The year under review witnessed robust growth in tractor volumes, led by the central region, followed by western, northern and southern regions. Going forward, the industry is expected to maintain a CAGR growth of 8-9 percent over the next five years. With the long-term industry drivers intact and the economy turning a corner, one can expect the sector to perform up to its potential over the coming years.

We expect domestic tractor sales to grow by 5-7 percent in 2014-15. The growth in farm incomes is expected to moderate to 3-5 percent from a 15 percent CAGR recorded over the last two years. Although farm mechanisation has shown an increasing trend in the country, there are wide ranging disparities in the progress of mechanisation across states. The northern states of Punjab, Haryana and Uttar Pradesh have already achieved high levels of mechanisation as compared with western and southern states of the country viz., Gujarat, Maharashtra, Rajasthan and certain areas of Tamil Nadu and Andhra Pradesh. Uptake in infrastructure development will have a positive impact on tractor sales.

With respect to monsoons for the current year, the Indian Meteorological Department (IMD) forecast states that the southwest monsoon will be below normal at 95 percent of the long period average.

Opportunities and Threats

Your company will focus on several new markets in the European region, Latin America and South Africa and provide the best of technology at an affordable price. Your company will further expand its current presence in ASEAN countries, Africa and pockets of Europe. The European markets in focus are Germany, the UK, France, Turkey, Italy and Spain.

The tractor industry is dominated by three major players. The entry of MNCs has further intensified competition. Your company is well-poised to capture the scenario through technology tie-ups and better product upgrades.

Product Launches

International launch of Tractors at AGRITECHNICA Hannover

Farmtrac Europeline product range will cater to the high HP segment, i.e. upto 110 HP. The USP of the product range comprises the fact that it comes with world-class components at a competitive price.

Farmtrac Heritage product range will cater to sub 80 HP segment. The USP of this range will be its classic finish, which is simple yet highly efficient. The Heritage series will emerge as a great choice for small farms wherein the use of a large, sophisticated tractor cannot be justified.

Glamour & Sophistication to the "World of Tractors"

Ferrari™ Orchard Tractor – a revolutionary new machine and a technology wonder, for the high value orchard farmers comprises:

- All four equal-sized wheels
- Oscillating chassis system
- All-time 4 wheel-drive
- Front-engine mounting for super-low turning radius and an ideal weight distribution

Powertrac Diesel-Saver Plus Euro

- With European style, comfort and safety for long working spans and additional income
- The new Diesel-Saver Plus Euro series enhances power of the current engines by about 10 percent and at the same time, reduces their fuel consumption by 10 percent

The New Farmtrac 'Executive' Series

- Tractors that are designed in consultation with a leading European engineering company
- The new Farmtrac Executive series tractors come with new style, improved operator ergonomics and a host of world-class features
- Greater traction is witnessed for these products and currently, supplies are gearing up to meet the demand. The complete potential of these and other new products is expected to come through in the near future.

2. Escorts Construction Equipment

Last fiscal, the industry underwent tough challenges. As per ICEMA (Indian Construction Equipment Manufacturers Association), there had been a dip of 13.8 percent year-on-year basis in sales of construction and material handling equipment.

Given that the domestic economy is passing through a rough phase, a moderate turnaround is expected on the back of some policy developments which have transpired over the last few months. The importance of infrastructure for sustained economic development is well recognised. With improving macro environment and a stable government at the centre, a faster turnaround is widely anticipated. Increased investment in different infrastructure sectors is expected to create significant demand for construction equipment across the value chain during the 12th Five Year Plan period. Industry estimates that construction equipment demand would go up to around 100,000 units during 2014. The market value of equipment is expected to be a mammoth USD 6.5 billion during 2014, with the earthmoving sector expected to command a value of USD 3.7 billion.

Projects are lined up for infrastructure development especially in sectors like metro, roads, power, steel and logistics, which will create a huge demand for construction equipment in the country.

At Escorts Construction Equipment division, we are working on product rationalisation and lean manufacturing. With this approach in mind we have embraced the following initiatives:

A. Reduced our breakeven point by a fair margin mainly through fixed cost rationalisation

B. Other business transformation initiatives

- Rationalised product platform
- Restructuring of sales and marketing operations
- Better raw material efficiency through vendor rationalisation

We will continue to shift towards a better product mix, leaner manufacturing/sales setup and better management of fixed costs.

Product Launches

In the construction equipment division, your Company has launched various models to suit customer needs. It has introduced new variants of its Pick-n-Carry cranes and safe cranes – the TRX series. These models will cater to the rising market demand for high-end cranes.

Backhoe Loader offering has been strengthened:

The new DigMax II series backhoe loaders are highly fuel efficient, more productive and exceptionally reliable machines packed with host of new exciting features like:

- Equipment monitoring system
- FM & USB Infotainment system
- Outrigger alarm
- Spacious all weather cabin
- Higher productivity, lower fuel consumption and powerful hydraulic system
- Improved aesthetics and new soothing machine color

These machines were well-received in the market over the last nine months and now supplies are being ramped-up to meet demand.

3. Escorts Railway Products

Your company is one of the key suppliers to the Indian Railways for products including Brake Systems, Couplers, Shock Absorbers, etc with a focus on safety, comfort and the environment. With this wide product range and in-house R&D capabilities, your company is well-poised to capture the immense opportunity presented by Indian Railways.

The railways sector has a potential to grow at a phenomenal rate in the years ahead. With focus on freight corridors, high capacity rolling stock, last mile rail linkages, high speed trains and port connectivity, the opportunities in this sector are in abundance.

Currently, the Indian Railways is on its way to becoming one of the best such networks in the world. Your company is now focusing on technology upgradation to ride this wave of growth.

Currently, your company is developing products for new generation rolling stock as a decline for the old generation

rolling stocks is witnessed. The Escorts Air Brake System for BMBS has been performing well in the field and the commercial benefits for which will commence post approval in mid-2014.

4. Escorts Auto Products

The Indian automobile industry continues to witness weak demand across vehicle segments on account of slowdown in economic activity and the consequent weakness in consumer sentiment. Commercial and passenger vehicles have witnessed a sharp decline over the past 18 months. However, two-wheeler sales have marginally picked up over the last few months driven by rural demand and growth in scooters.

The passenger vehicles segment witnessed the third consecutive year of muted demand. However, new launches have received good response, reflecting huge pent-up demand.

Commercial vehicle segment continued its steep decline with 16 percent overall decline in production as compared with the previous year. Tata Motors, which dominates the CV segment (both M&HCV and LCV) and is one of EAP's key customers, alone witnessed 21 percent production de-growth.

Outlook

Demand is expected to remain weak in the near term, particularly for CVs, given uncertain macro-economic environment. Over the long-term, easing macro headwinds in terms of lower interest rates and higher economic growth will emerge as the key drivers for volume growth and profitability.

With more product launches lined up, volume recovery is expected across segments. However, the benefit of the same would differ from player to player depending on their product lifecycle and competitive intensity. While an immediate upturn in the auto industry is not expected, industrial activity and infrastructure spending are expected to pick-up gradually, thereby leading to improvement in commercial vehicle demand.

Escorts Auto Products (EAP) top-3 OEM customers have been witnessing production de-growth in the range of 15-25 percent for over a year. In view of the pressure on OEM segment sales, the business undertook the following initiatives to reduce the adverse impact on profitability:

Greater focus on domestic as well as global aftermarkets: EAP increased its reach both in the domestic and global aftermarkets, expanded its merchant exports to Sri Lanka, Bangladesh, Nepal, Egypt, Indonesia and Dubai as well as entered into many of these markets through direct dealers.

New product development: New product variants were developed during the last 18 months. The focus was primarily on high margin exports and aftermarket segments. These new products accounted for nearly 10 percent of sales during this 18 month period. Also, speedy product development for OEM customers helped in arresting the sales decline to some extent.

Cost reduction efforts: Key fixed/semi variable expenses such as power and fuel cost and administration expenses have reduced YoY despite more than 30 percent increase in fuel prices.

Overall Risks and Concerns

The long-term prospects of the Indian tractor and construction industry are highly dependent on Government policies. Historically, a large number of equipment are sold on credit, despite an increase in the non-performing assets (NPAs) for financial institutions over the last few years, which has led to tightening of credit norms. There has also been a sharp increase in cash purchases over the last few years, indicating an increase in disposable incomes. Most of the equipment financing done by banks comes under priority sector lending, a direct-lending mechanism of the Government of India.

Monsoons

Normal monsoons are critical for the agriculture industry. The Indian met department is predicting below normal monsoon in the current fiscal. Tractor sales, to some extent, run the risk of a demand drop in case of significant variations in the monsoons.

Raw material cost

Raw material cost represents the largest expense head of the industry with alloy steel and pig iron (primary components), accounting for 75-80 percent of the total raw material cost.

Over the past three years, the prices of iron, alloy steel and rubber have been volatile. Any slight variation will affect profitability.

Fuel price

With the price of crude oil rising significantly over the past few months, the price of automotive fuel is likely to face upward pressures. Also, during the last fiscal, the government has announced partial deregulation of diesel prices. This has impacted cost of ownership and may have an impact on your Company's products as well.

Investor Relations

With the growing interest from investors both in India as well as abroad, your Company maintains an active engagement with the investor community through ongoing investor management meetings with shareholders and investors.

During the year under report, your Company has actively participated in a number of domestic as well as international investor meets organised by reputed international banks and financial services companies. Your Company also periodically conducted analyst meets and plant visits to communicate details of performance, important developments and exchange information.

Other strategic initiatives

Your Company implemented various strategic IT initiatives in transforming the business. Some of the major IT achievements are illustrated below:

Oracle R12 ERP has fully stabilised and is providing rich dividends to the Company. It has helped in standardising the group-wide operating processes and implementation of desired checks and balances with transparency and efficiency. The single instance ERP implementation has laid a strong foundation for consolidation of finance function including accounts, taxation and commercial billing across the Escorts Group. There is significant reduction in monthly financial closure time and the group-wide finance consolidation is done through the ERP system without any manual intervention. Another key highlight of this project is the successful implementation of the Warehouse Management Software. This has automated the entire warehouse operations while seamlessly integrating with the Oracle ERP, bringing significant operational efficiencies and is rated as one of the best WMS implementations in the country.

Disaster Recovery

To ensure business continuity, a Disaster Recovery (DR) System has been established for Oracle R12 ERP in a different seismic zone at the WIPRO data centre in Pune. Data from our primary data centre in Faridabad is replicated to the DR data centre at Pune to ensure business continuity in case of any natural/ manmade disaster.

Business Intelligence

In order to get deeper insights into its business activities, your Company implemented Business Intelligence software, which creates intelligent dashboards based on related data taken from multiple sources like ERP, legacy applications etc. This is a transformational project for your Company as all critical information is displayed as dashboards and departments can view their data in multiple ways and do meaningful analysis and comparisons easily.

Data Loss Prevention

In order to protect its business critical data including product designs, business plans, future business strategies etc., your Company initiated a major information security project called Data Loss Prevention (DLP) to prevent leakage of important data. This project is being implemented group-wide for all users, gateways and email solution on the cloud. This project has helped in establishing a framework for classifying and handling Escorts information based on its level of sensitivity, value and criticality to the Company.

Development in Industrial Relations

In continuation to our endeavours to maintain sustainable

Industrial Relations in the organisation, Long Term Settlement 2013-16 has been signed between the management and the union in September 2013. As part of LTS 2013, MOST has been implemented pan-Escorts resulting in an increase in productivity along with good work practices. Harmonious industrial relations are being maintained without any loss of man hours and production.

Training and Development

Your company has organised various in-house and external training workshops for workmen. There were around 510 training programmes with 10,205 training man-days; during the last 18 months, several initiatives are being undertaken for employee training across all business verticals.

Capital Expenditure

Your Company has carefully planned capital expenditure for the medium-term with primary focus on design, productivity improvement and cost reduction.

In addition, investments are also planned for modernisation of the existing manufacturing facilities and improving flexibility across all the plants, imparting a strong competitive advantage to your Company towards introducing a larger number of tractor models over the coming years.

Cost Savings

Your Company has continuously identified areas where costs can be reduced. Employees across all levels of the enterprise are involved in this initiative, wherein each team has targets to achieve in cost savings.

We have embraced several initiatives on building lean supplier base to benchmark ourselves against the best. We are confident of seeing positive results in this domain. Our efforts towards reducing fixed costs have kept pace in the year gone by and tangible results are expected to be visible in this financial year.

Financial performance with respect to operational performance

The financial statements have been prepared in compliance with the requirements of the Companies Act, 1956 and Generally Accepted Accounting Principles (GAAP) in India. The Company has provided segment reporting on a consolidated basis as per standard AS 17 on segment reporting. This information appears along with the consolidated accounts.

Operational Performance

The Company's revenues increased by 6.2 percent from ₹5,922.7 cr in 18-months ended March 2013 to ₹6,291.5 cr in 18-months ended March 2014. Tractor volumes were up 9 percent to 1,00,833 in the18-months ended March 2014 as against 92,543 in 18-months ended March 2013. Construction volumes at 4,789 in the 18-month ended March 2014 as that of 7,307 in 18-months ended March 2013.

Earnings before Interest, Taxes, Depreciation and Amortisation (EBITDA) were up 31.7 percent at ₹381.2 cr in 18-months ended March 2014 as against ₹289.5 cr in 18-months ended March 2013.

Profit Before Tax (PBT) was up by 81% to ₹272.4 cr in the 18-months ended March 2014, as compared with ₹150.4 cr in the 18-months ended March 2013 and Profit After Tax (PAT) at ₹245 cr as against ₹135 cr in the 18-months ended March 2013.

Segment Performance:

The Escorts Agri Machinery division revenues were up by 13.5% to ₹5,123.3 cr in 18-months ended March 2014 from ₹4,513.5 cr in 18-months ended March 2013. The EBIT for the division stood at ₹496.4 cr in 18-months ended March 2014 against ₹370.75 cr in 18-months ended March 2013.

The Escorts Auto Products Division revenues stood at ₹210.58 cr in 18-months ended March 2014 from ₹225 cr in 18-months ended March 2013. The EBIT stood at ₹(29.6) cr against ₹(16.4) cr last year.

The Escorts Railway Products Division registered sales of ₹255.78 cr in 18-months ended March 2014 against ₹222.05 cr in 18M ended March 2013. The EBIT stood at ₹14.56 cr against ₹8.42 cr last year.

The Escorts Construction Equipment Division revenue during 18-months ended March 2014 stood at ₹763.2 cr as against ₹1,044.9 cr in 18-months ended March 2013 down due to slowdown in industry demand.

Note: *"The 'forward-looking statements' part of the Management Discussion & Analysis on economic indicators is based on our best estimate of the current environment. This may be subject to change based on external macro-economic factors out of our control, including but not limited to raw material availability and prices, cyclical demand and pricing in the Company's principal markets, changes in Government regulations, tax and economic policies."*

For and on behalf of the Board

Sd/-

Place: Faridabad — **RAJAN NANDA**

Date: 28th May, 2014 — *Chairman & Managing Director*