Action Construction Equipment Ltd I BUY I TP:630

When the loading beckons...

We initiate coverage on Action Construction Equipment (ACE), a thinly-covered stock, with a TP of Rs.630 (~42% upside). With a combination of all (economic) stars getting aligned and a high-competency, cost-competitive business portfolio, ACE is all ready to deliver value. Clear market leadership position in several segments of cranes, construction equipment, material handling and agricultural implements and a credible, proven de-cyclicalisation strategy through defence and exports set it clearly apart. Our deep dive into the sector, including chats with consultants, provides a clear glimpse of ACE's competitiveness and product acceptance. An unassailable balance sheet with surplus cash and low debt, in an otherwise capital-intensive sector, high asset turnover and return ratios are other visible icings on the cake.

- **Even a perfect storm passes, and it has –** ACE's businesses, unquestionably linked to the broader economy, is coming out of an extended downturn due to corporate overleveraging, burgeoning bank NPLs, a crippling Asset Quality Review, demonetization, GST, Covid and the Russia-Ukraine war. The massive fiscal outlays on government-driven capex, coupled with some private sector incentives such as PLI, a clear departure from the shaky private sector-driven misadventure of the 2000s, is creating a positive downstream impact on construction equipment. Owing to a diversified product portfolio and application base, ACE is in a vantage position to benefit from this - arguably more sustainable - capex cycle and overall economic upturn.
- **Strong market positioning and getting better –** ACE, a market leader in cranes for over two decades, is leveraging this strength to enter higher capacity-class cranes. The company has been able to become a prominent market player in the MHE segment as well, which jells well with lower capacity cranes used in logistics. In the CE segment, backhoe loaders - a large, cost-conscious and fragmented market - ACE has positioned itself as a cost competitive player. Moreover, ACE is delivering backhoe loaders to gain incremental share through increased cross selling with the cranes segment. Finally, the company is growing its revenue potential through regular capex and acquisitions.
- **Proven cycle-smoothing strategy & fortification of balance sheet -** To tackle the businesses' inherent cyclicity, ACE has been foraying into businesses that counterbalance its cycles, the key initiative being entering the Agri equipment segment which follows a different cycle as compared to CE. ACE has also dipped its toes into the export market through a high-profile, scalable order from Ghana. It has also begun supplying specialised equipment to the defence sector. We estimate defence and exports to cumulatively contribute ~18-20% of the revenue moving ahead. Additionally, ACE's low-debt status and ample liquidity buffers are a veritable bulwark against financial risk which this volatile sector is prone to.
- **Valuation & View- -** We initiate coverage on ACE with a TP of Rs 630 (30x FY25E EPS – 10% premium to its 6-year average 1-year forward PE). The premium valuation is justified given the strong revenue growth visibility, margin expansion of ~200bps over FY23-25E following foray into specialized high margin products. The move towards agricultural equipment, defence and exports should mitigate the cyclicity risk historically experienced. Our bull-case TP in a stronger up-cycle is at Rs763, whereas in an event of delayed execution and margin pressure, our bear case TP could be at Rs522. Thus, the risk-reward tradeoff remains favourable. Our estimates are ahead of consensus.

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Target Price			630	Key Data	
				Bloomberg Code	ACCE:IN
CMP*			443	Curr Shares O/S (mn)	119
				Diluted Shares O/S(mn)	119
Upside			42%	Mkt Cap (Rsbn)	52730
Price Performance (%)				52 Wk H / L (Rs)	455 / 175
	1M	**6M**	**1Yr**		
ACE	8.34	27.17	148		
Nifty	2.72	-0.18	15.75		

Source: Bloomberg, ACE Equity, MNCL Research

	Sep-22	Dec-22	Mar-23
Promoter	**66.76**	**66.76**	**66.76**
DIIs	**4.86**	**4.97**	**5.63**
FIIs	**4.56**	**3.44**	**3.54**
Others	**23.83**	**24.84**	**24.08**

Source: NSE

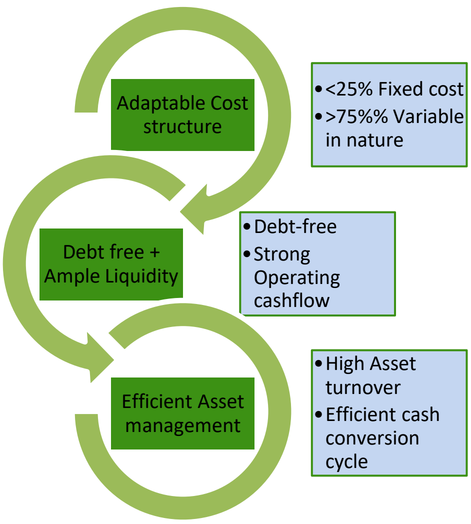
Why should you read this report?

•Why the construction equipment market in India is set for the next leg of growth

•Where is ACE positioned in the market

•Backhoe loader business a potential game changer for the company

•How the business accommodates cyclicity



Particulars FY25E (Rs mn)	MNCL estimates	Consensus estimates	Variance
Revenue	29,322	27,890	5%
EBITDA	3,323	3,012	10%
OPM (%)	11.3%	10.8%	50 Bps
PAT	2499	2296	9%
EPS (Rs)	21	19.20	

Source: MNCL research, Bloomberg

Y/E Mar (Rs mn)	Revenue	YoY (%)	EBITDA	EBITDA (%)	Adj PAT	YoY (%)	Adj EPS	RoE (%)	RoCE (%)	P/E (x)	EV/EBITDA (x)
FY21	12,270	-13.88%	1,193	9.73%	801.5	52.29%	7.1	16.59%	20.05%	21.9	14.8
FY22	16,303	6.12%	1,523	9.34%	1,059.1	32.13%	9.1	16.58%	20.56%	26.4	18.8
FY23E	22,240	32.87%	2,293	10.31%	1,657.8	56.53%	13.9	19.91%	25.10%	32.3	23.1
FY24E	26,530	36.41%	2,874	10.83%	2,150.4	29.71%	18.1	21.22%	26.22%	24.9	17.8
FY25E	29,322	19.29%	3,323	11.33%	2,498.9	16.21%	21.0	20.23%	25.11%	21.4	15.0

Source: Company, MNCL Research estimates, Consolidated Financials

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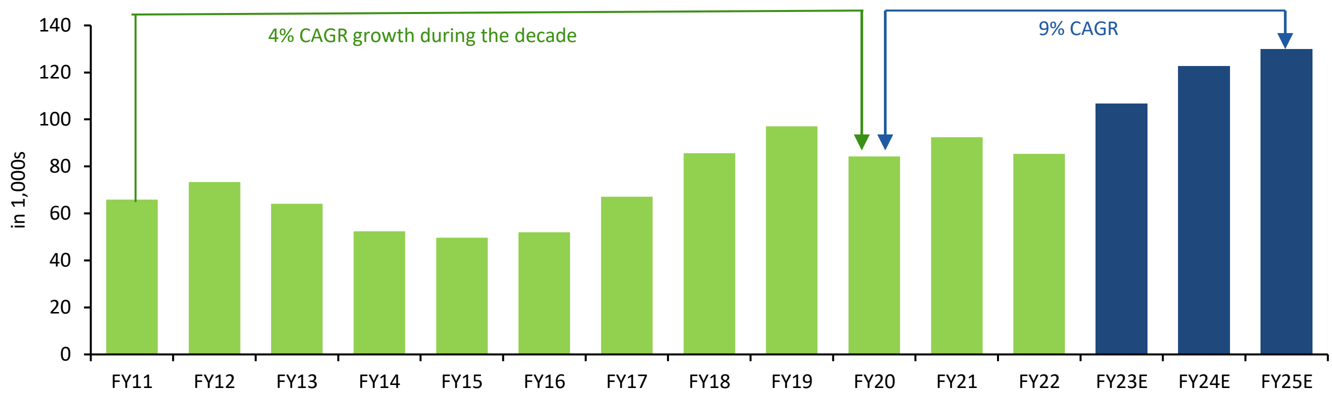
Investment Thesis in Charts

Exhibit 1: Construction Equipment sales industry to witness revival after a decadal lull backed by the massive fiscal outlay



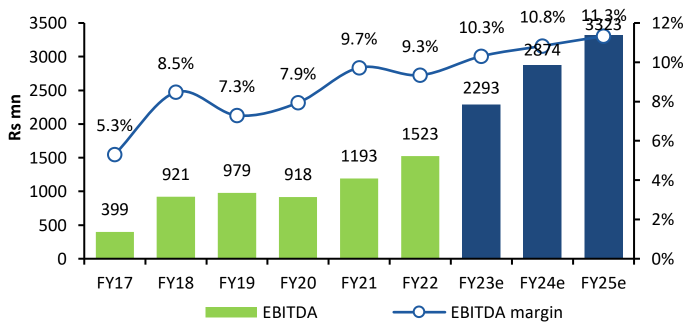
Source: ICEMA, MNCL Research

Exhibit 2: Accelerated revenue growth and profitability on the road ahead

Particulars (Rs mn)	FY20	FY21	FY22	FY23E	FY24E	FY25E
Revenue	11562	12270	16303	22240	26530	29322
EBITDA	918	1193	1523	2293	2874	3323
EBITDA Margin %	7.94%	9.73%	9.34%	10.31%	10.83%	11.33%
PAT	526	802	1059	1658	2150	2499
PAT Margin %	4.55%	6.53%	6.50%	7.45%	8.11%	8.52%
EPS (Rs)	4.58	7.06	9.10	13.92	18.06	20.98

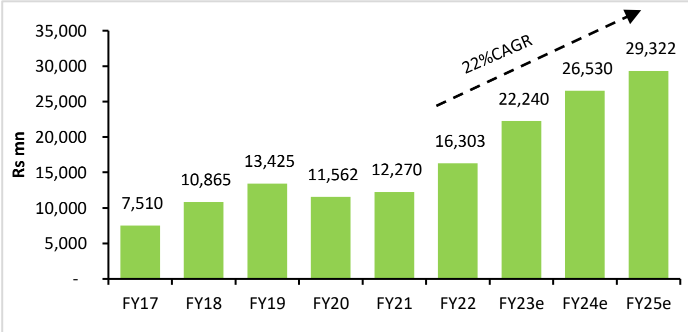
Source: Company, MNCL Research

Exhibit 3: OPM expansion aided by increased realization



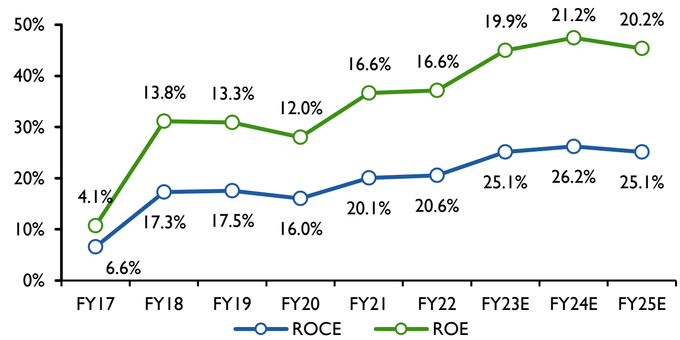
Source: Company, MNCL Research

Exhibit 4: Robust revenue growth expected to continue



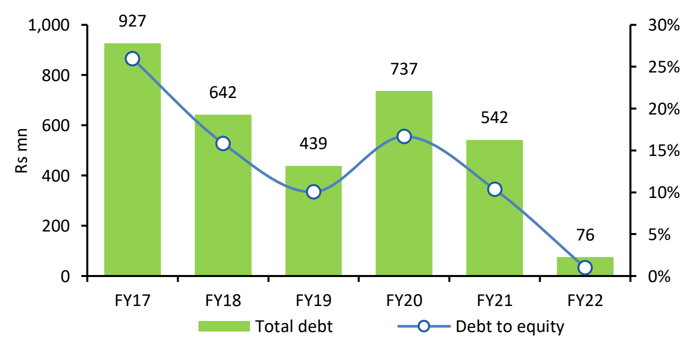
Source: Company, MNCL Research

Exhibit 5: Incremental return ratios higher owing to higher profitability



Source: Company, MNCL Research

Exhibit 6: : Debt free capital structure with adaptable cost structure acts as hedge to financial downturn



Source: Company, MNCL Research

Strong demand outlook

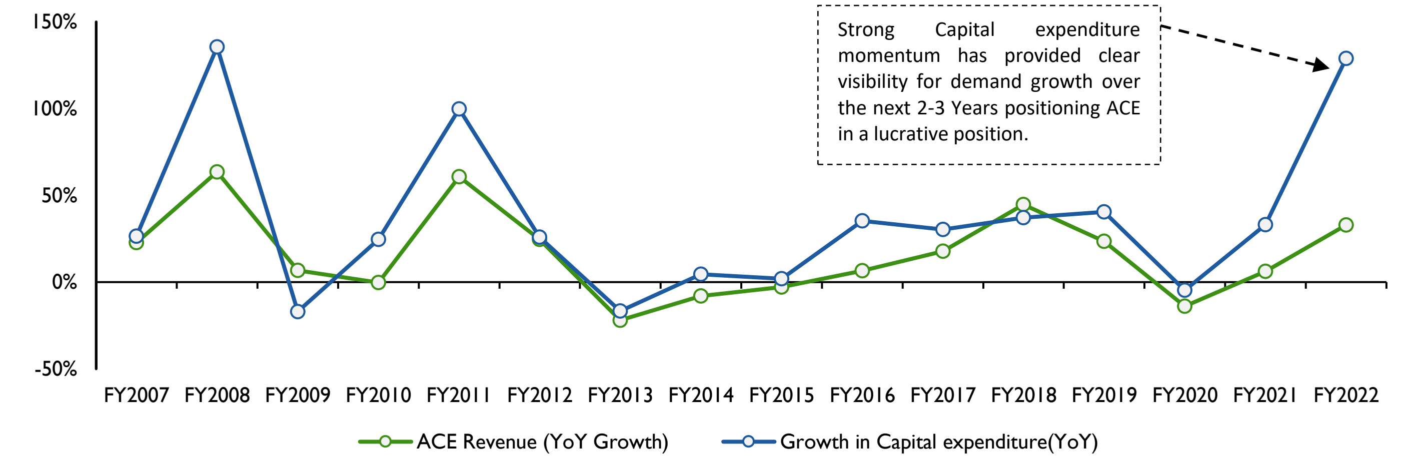
Drawing strength from the increased capital outlay

ACE is an established brand with over 27 years of industry presence and is the market leader in the domestic cranes market. It owns a well-diversified construction equipment product portfolio that finds application across various sectors. This variety of end users puts ACE at an advantageous position as these sectors enjoy the tailwinds created by an economic recovery and support through the government fiscal outlay.

India has begun its journey on a massive capex cycle, powered by the Government of India (GoI). Focusing on capital investment outlay, GOI has increased its capital investments for the third year in a row to Rs 10tn, in the budget FY2023-24. The government's capex commitments for the development of core sectors such as cement, metals, oil refining, power and transportation will have a domino effect on private sector companies as well, which has been amplified through PLI schemes.

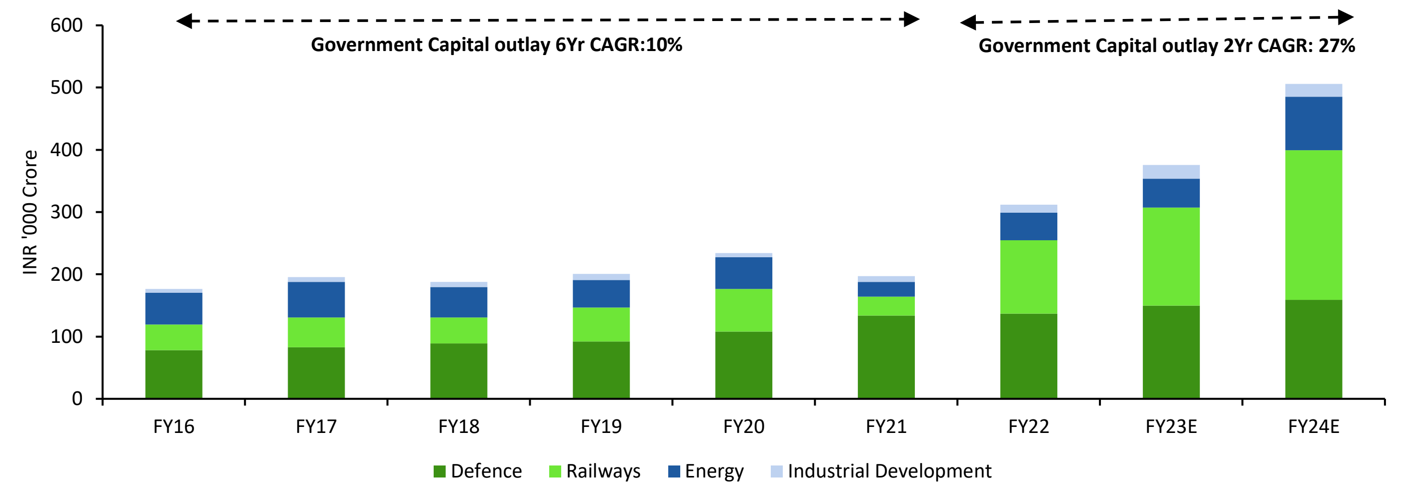
With increasing government outlays for infrastructure, execution of higher priced orders and revival in private capex, we expect a demand surge in the medium term for the construction equipment industry. We believe the construction equipment industry should witness a stable demand going forward which will arguably be more sustainable.

Exhibit 7: Revenue growth of ACE is interlinked to the capital expenditure growth in the country



Source: RBI, MNCL Research

Exhibit 8: Higher Government capital outlays driving growth at much faster pace in comparison to past decade



Source: RBI, Ministry of finance, MNCL Research

Private capex pickup supported by policy thrust

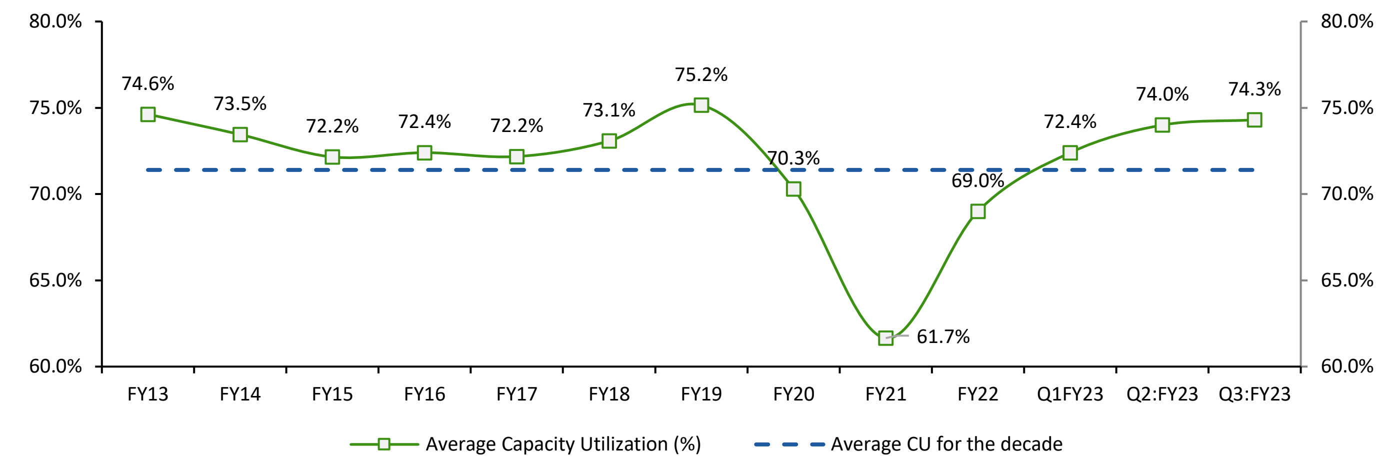
Construction equipment like cranes are not only used in infra development but >40% of the lower capacity cranes are used in manufacturing process, automation and logistics.

In our view the production linked incentives (PLI) schemes announced across 14 sectors with budgeted outlay of Rs 2 lakh Crore over the next 4-5 years will create a domino effect on private capex cycle and boost demand for construction equipment and related industries, as private capex picks up.

In addition to government incentives, *capacity utilization levels have been increasing every quarter in FY23 as India picks up its economic activities and reaches the pre-pandemic levels*. The capacity utilization (CU) in 9MFY23 was at ~74% which has been well above the average capacity utilization levels of 71.2% in the past decade. In addition to improvement in operating profiles due to healthy execution and steady demand post pandemic, the increased CU levels will be encouraging expansion and mechanization in the manufacturing sector. The increased production levels should also boost the demand for additional cranes and other material handling equipment used in inter and intra plant logistics.

Higher fiscal outlay coupled with manufacturing expansion and mechanization will enhance the demand for various construction equipment used in this value chain. Owing to its diversified product portfolio, ACE is placed in a very lucrative position to benefit from these tailwinds and cater to the upcoming demand in infrastructure and other industrial-use construction equipment.

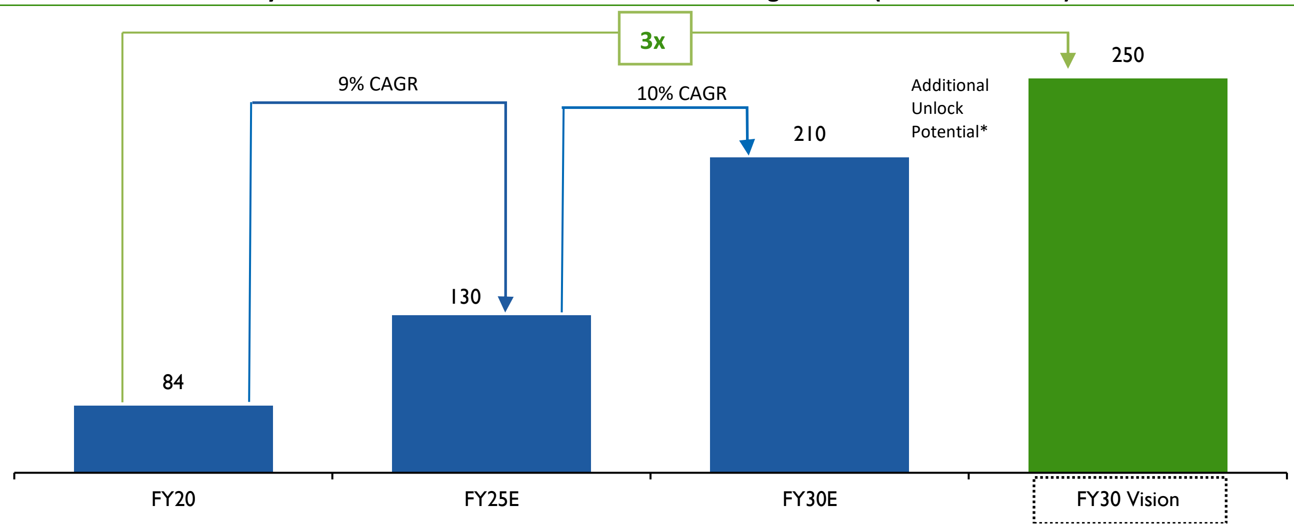
Exhibit 9: Capacity utilization inching to pre-pandemic levels and well above the average CU over the decade will promote private capex



RBI survey of over 700 participating manufacturing companies

Source: RBI, MNCL Research

Exhibit 10: Indian CE Industry: Accelerated demand outlook for the coming decade (Units sales 000's)



Source: ICEMA, Company, MNCL Research

Macroeconomics favouring demand outlook

The company's equipment is used in sectors like Infrastructure, Construction, Power Projects, Ports & Shipyards, Dams, Metro Rail, Roads, Mining, Steel Industry, Engineering Industry, Railways, Cement, Petroleum, Defence, Chemicals & Fertilizer Plants, Warehousing, Logistics, Building Construction, and many more. With such a diverse end-user base, the demand for products of ACE becomes interlinked with the growth of these varied end-users. In addition to dependence on overall expansion and profitability of these end user industries it is intrinsically linked to the infrastructure sector, and hence indirectly fluctuates with the fortunes of the Indian economy at large.

Tracing through the cycles starting early 2000s

In the last 27 years ACE has undergone many cycles. Starting from the early 2000 when the economy was booming. and the nominal GDP grew at a CAGR of ~13.5% during this period, ACE underwent robust revenue growth. But in 2008 owing to the Great Recession, when GDP growth fell during the period FY08-09, there was a corresponding dip in the revenue growth of the company, which later revived in the following year as growth picked up in FY11 & FY12. Since FY12, the economy had turned sluggish hitting lows around 4.5% in FY13 and FY14, which was correspondingly reflected in the business performance of the company with a decline of 21.9% and 7.9% in revenues, in the respective years.

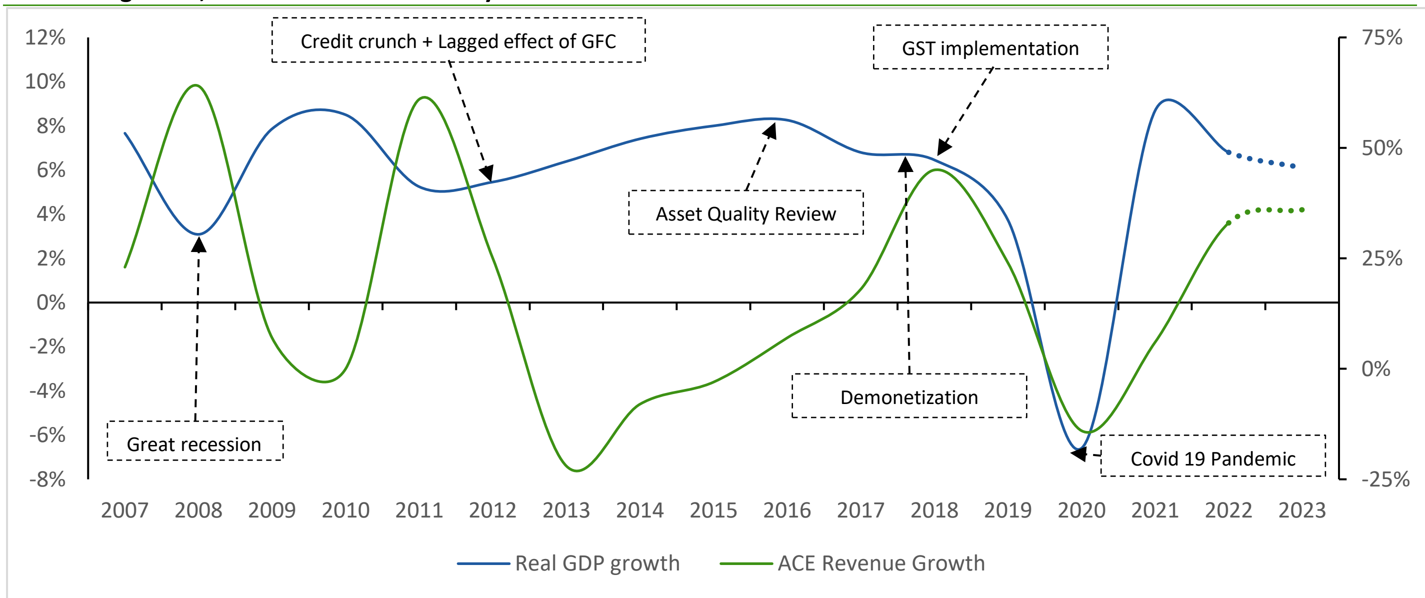
Owing to the pent-up demand and the downcycle persisting for almost a decade we believe the upcycle has just begun and this growth will sustain in the medium term with the growth-enhancing policies already in place and private capex cycle uptake

Resurgence of demand: The economy transitioned in FY15 and FY16 growing at real ~8%, which was reflected in the growth of ACE as the revenue started growing again in FY16 and the cycle saw a clear turnaround in FY17. For FY17, FY18 despite the demonetization and GST implementation the economy grew at a stable pace, but the repercussions of these events were seen in FY19 when the economy growth rate declined to 3.5%, reflecting in contraction of revenue growth rate for ACE as well. This upsurge in FY17 and FY18 was short lived after a decadal lull in the sector and was depressed again by exogenous policy shocks.

Pandemic and the after-effects: In FY2020 and FY2021 the world was hit by the pandemic and the economy weakened. The consequent effects were observed in the company sales as well. The economy started recovering in FY22, But in FY22 it was blighted by the Russia-Ukraine war, commodity inflation and other supply chain issues disrupting economic output. By FY23 all the sectors in the economy have inched up to the pre-pandemic levels and the Indian economy has stabilized.

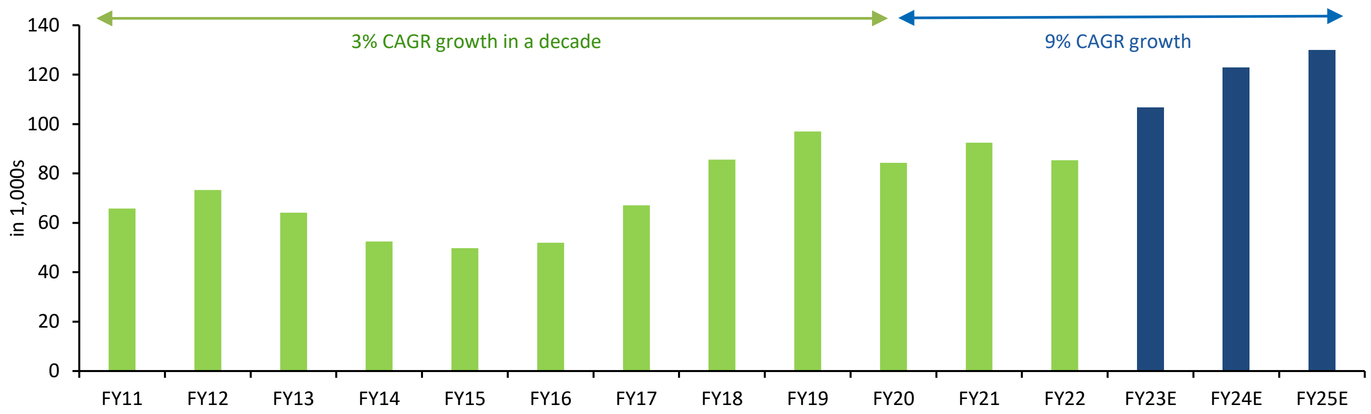
Our view: We believe, now that the perfect storm has passed, we are ready for a demand surge at much faster pace with the upcycle being more sustainable, owing to the high pent up demand. With the policies aiding growth already in place, we are still to witness the full throttle of the upcycle leading to a greater demand for proxies like CE industry.

Exhibit 11: Revenue growth of ace is interlinked with the economic growth of the country: With the positive outlook on Indian economic growth, ACE should be favored by macroeconomic factors



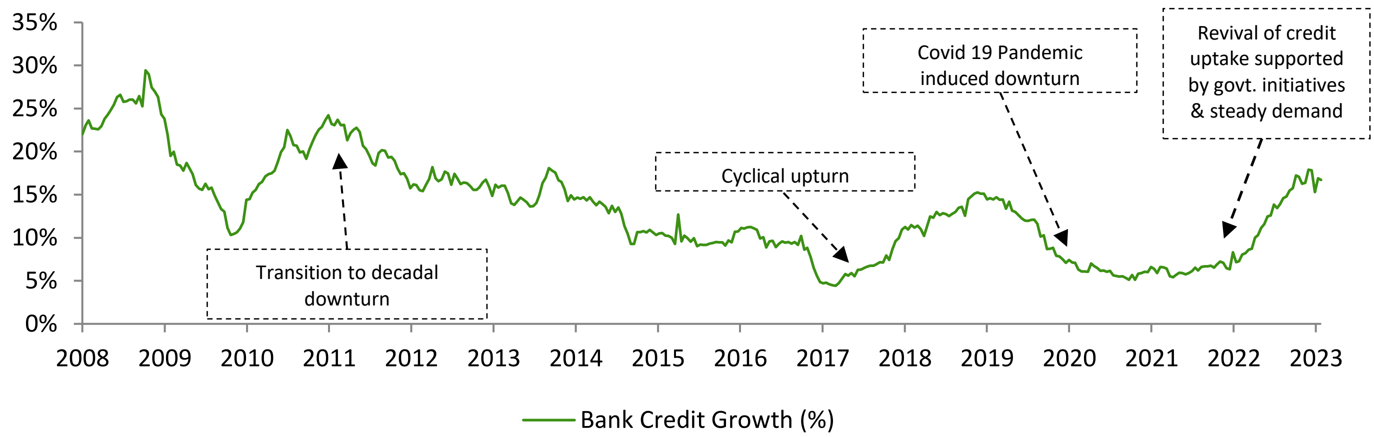
Source: RBI, MNCL Research

Exhibit 12: Construction Equipment sales CAGR in the country will outperform the decadal CAGR owing to favorable macroeconomic conditions



Source: ICEMA, MNCL Research

Exhibit 13: Construction equipment lull for the decade was mirrored by the bank credit growth over the decade: Clear downcycle since FY12



Source: RBI, MNCL Research

Exhibit 14: Sectoral growth driven by governmental support - Favorable policies in place

Sector	Capital outlay
Urban Infra	▪ The Centre has allocated RS 10,00,000 Crs capital investment, a steep increase of 33% for third year in a row. ▪ Investment of RS 75,000 Crs, for one hundred critical transport infrastructure projects, for last and first mile connectivity for ports, coal, steel, fertilizer, and food grains sectors. ▪ The government has allocated RS 160bn towards its Smart Cities Mission for FY24.
Railways	▪ Capital outlay of RS 2.4tn has been provided for the Railways. ▪ 400 new Vande Bharat trains to be developed in the next three years ▪ Construction of dedicated new line projects will be getting an allocation of RS 3185bn and National High Speed Rail Corporation Limited will be allocated RS 4018bn.
Manufacturing	▪ The Manufacturing sector of India has the potential to reach US$ 1 Tn by 2025. ▪ PLI in 14 sectors for achieving the vision of 'Atmanirbhar Bharat' with the potential to have additional production of RS 3tn during next 5 years.
Roads	▪ As per Budget 2023-24 Expansion of the National Highways network by 14,000 km in FY24, RS 200bn Cr to be mobilized through innovative ways of financing. ▪ The roads sector is likely to account for 18% capital expenditure over FY 2019-25 and Roads worth $200 Bn to be built in next 2 years. ▪ NHAI is coming up with 23 new highways including a network of expressways and economic corridors by March 2025.
Housing	▪ Outlay for PM Awas Yojana is being enhanced by 66% to over RS 790bn. ▪ Real estate sector in India is expected to reach a market size of US$ 1 trillion by 2030 and contribute 13% to the country's GDP by 2025.
Agriculture	▪ In the 2023-24 Union Budget, Ministry of Agriculture and Farmers' Welfare has been allocated RS 1.25tn. ▪ Indian tractor market stands at ~8,00,000 units and is anticipated to grow at a CAGR of 4.5% over the next five years owing to increase in demand for mechanization in agriculture & logistics industry.
Logistics	▪ 5 Multimodal Logistics Parks at four locations through PPP mode contracts to be awarded in FY24. ▪ The government had decided to set up as many as 35 Multi Modal Logistics Parks, at a total capital cost of Rs. 500bn. ▪ One hundred PM Gati Shakti Cargo Terminals for multimodal logistics facilities will be developed till 2025.
Airports	▪ India's aviation industry is expected to witness RS 350bn (US$ 4.99 Bn) investment in the coming years. ▪ The Indian Government is planning to invest US$ 1.83 Bn for development of airport infrastructure along with aviation navigation services by 2026
Ports	▪ The Ministry of Ports, Shipping and Waterways aims to complete projects worth RS 2tn in the next financial year under the Sagarmala Programme. ▪ Projects worth RS 133.08bn were awarded in the last three years on upgradation of the major ports.

Source: MNCL Research

Growing revenue potential - Leveraging Strong Product Portfolio

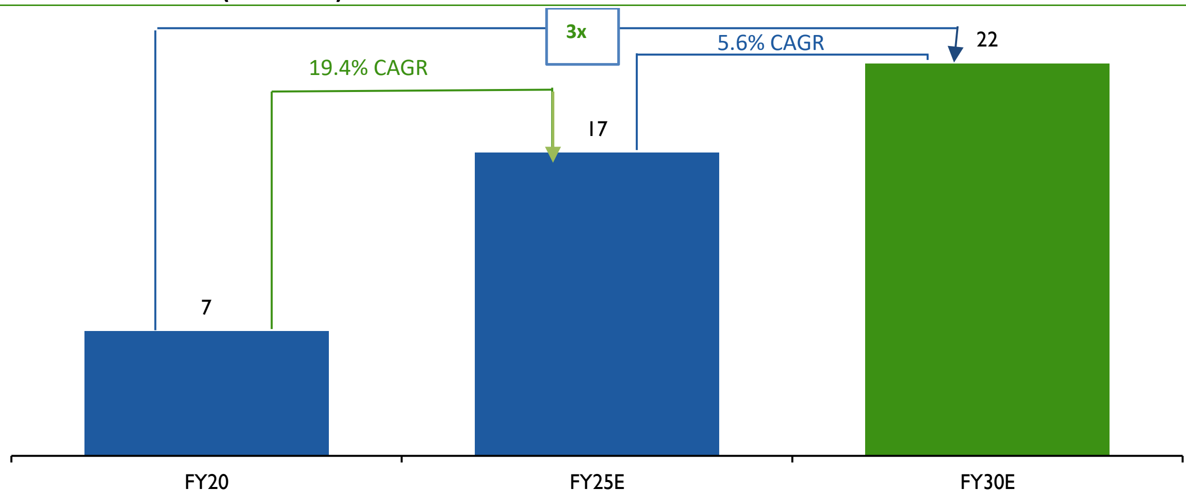
ACE offers a diversified product portfolio amongst cranes, material handling equipment, construction equipment & agricultural equipment segments. The company is an established player and has been the dominant manufacturer of cranes for more than two decades now. The company's versatility to satisfy a diverse range of sectors for wide application helps it to leverage its customer base to explore further cross-selling opportunities and gain market share. The continuous R&D for developing new products and advanced manufacturing process to improve quality while making the product more economical and cost effective has enabled the company to cement its market leadership position.

Market leadership in Cranes - Creating a legacy brand

ACE maintains market leadership in pick and carry crane, crawler cranes, self-erecting tower cranes and fixed tower cranes. It has been able to maintain this market leadership for more than two decades now by a continuously evolving manufacturing process, innovative products and an extensive after sale service network. Cranes as a segment contributes to ~68% of the total revenue.

The Indian crane market is estimated to grow at 20% CAGR between FY20 and FY25E owing to the infrastructural deficit in the country and the rising investments in infra development. Manufacturing sector target of USD 1 Trillion in the Indian economy by 2025 will be another major driver for cranes. Application in manufacturing processes combined with the upcoming industrial capex cycle should lead to an impressive growth in the segment.

Exhibit 15: Indian Crane market (Units'000) to witness accelerated demand over the next decade

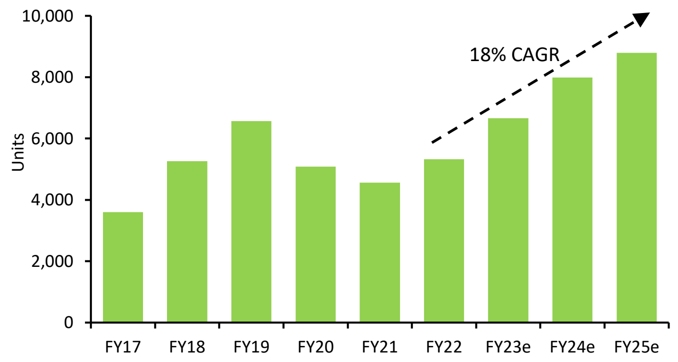


Source: Industry sources, MNCL Research

ACE is a dominant market player in mobile cranes and pick & carry cranes with >60% market share in the domestic market. The demand for these cranes has a strong correlation with industrial growth. They undertake a wide range of lifting jobs across infrastructure, mining, agricultural, industrial and urban renewal sectors. These cranes are widely used for intra- and inter-plant movement in the manufacturing sectors, to support a host of production activities. This diverse usage across the infra and production value chain makes the segment a prime beneficiary of industrial growth and infra development cycle that is set in motion.

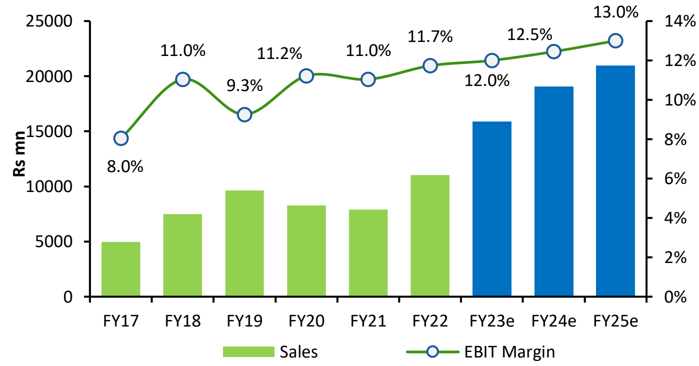
In tower cranes the company has more than~70% market share. With increasing necessity for vertical construction in the country, this segment will witness rising demand. The company faces competition from Chinese manufacturers in the segment, owing to the Chinese's price-competitive product offerings. But in recent developments, as the transportation costs have firmed up owing to volatility in global oil prices coupled with rising inflation in commodity prices and Chinese government raising interest rates, the Chinese tower crane manufacturers are compelled to increase prices of their products. Thus, easing up the competition in this area.

Exhibit 16: Robust volume growth in cranes- in line with industry growth



Source: Company, MNCL Research

Exhibit 17: Revenue (Rs Mn) and EBIT Margin (%) expansion backed by higher capacity utilization



Source: Company, MNCL Research

ACE has positioned itself in the market as one of the lowest-cost sellers. The customer-centric approach and focus on after sales service has made the company a partner of choice for corporates. ACE maintains an 80% customer retention in the cranes category and the majority of sales (~60%) are directly to the customer. Competitive pricing in its designated capacity class continues to make the company's cranes attractive for rental companies and minor hirers as well. ACE has a dedicated network of 55-70 dealers across the country which contribute to 40% of the crane sales.

Based on the end user, cranes sold by ACE can be divided into
~ 45% used in logistics and manufacturing
~45% in used in Infrastructural development
~20% in real-estate development.

In addition to the governmental and industrial capex, we expect significant replacement demand aiding growth in the medium term as the replacement cycle got delayed due to the unforeseen situations like the pandemic, leading to reduced wear and tear due to the minimal activity of machines during the time. We believe leveraging its brand name and high customer retention ACE Ltd. will be able to exploit this demand to drive sales and further increase market share.

The company is also trying to increase higher-tonnage market penetration which is currently dominated by the Chinese players. These cranes have higher realization as the base manufacturing capacity for all cranes is same and requires minimal incremental investments for production. ACE has already developed cranes of higher tonnage and will be incurring capex in FY24 for commencement of a separate facility for manufacturing cranes of more than 40 Tons.

Exhibit 18: Cranes product portfolio – Presence across segments

Source: Company, MNCL research

The company aims to grow organically by the introduction of new and innovative products. ACE has already introduced new age products like Nextgen Pick & Carry Cranes, 360 degrees slew with Pick N Carry Cranes and a portfolio of multi activity cranes that are ~60% lower in cost and have combined features of two or more types of cranes to capitalize and maintain its market leadership position in these segments. With similar intent the company has launched its first fully electric crane as well which is witnessing healthy demand uptake. ACE's focus on R&D gives it an edge to stay relevant and maintain its leadership position.

Exhibit 19: Continuous R&D led new age product offerings

Source: Company, MNCL research

Exhibit 20: Unenviable positioning in the Crane segment

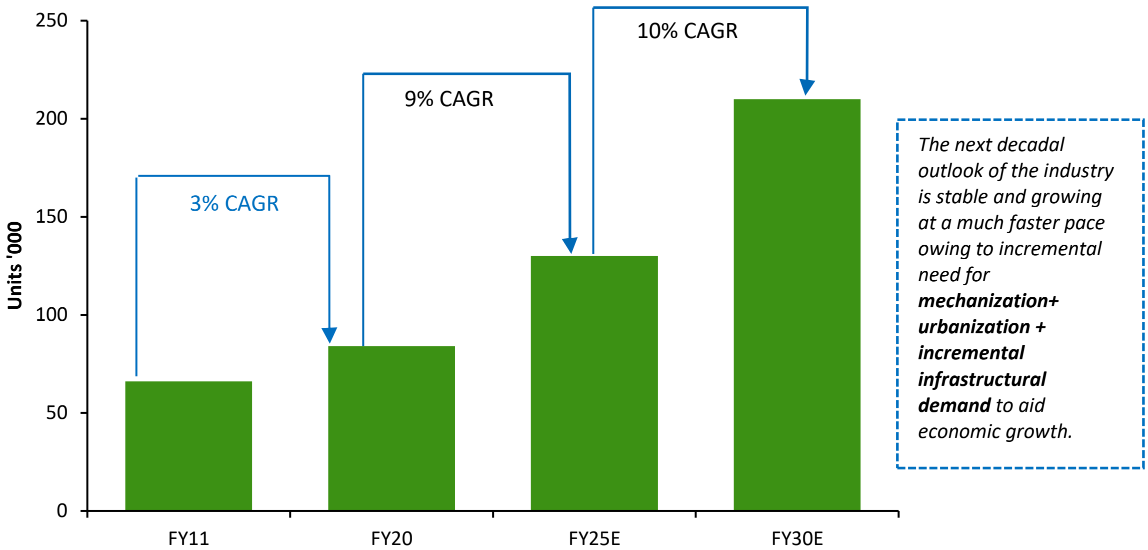
Crane category	Market position	Capacity Class	Application	Selling Price	Comments
Pick & Carry Cranes	Market leader (63% market share)	9 Tons - 30 Tons	Infrastructure, Construction, Manufacturing, Logistics	Rs 1.8-2mn	• Launch of 100% Electric variant developed by ACE is witnessing good demand as conglomerates like Reliance, L&T etc. witness policy shift towards decreasing carbon footprint
Crawler Cranes	Market Leader (up to 75 Tons)	25 Tons - 75 Tons	Infrastructure, Construction	Rs 11-16mn	• The company is developing higher tonnage cranes for strategic growth. (160 tons crane under development)
Truck Cranes	No. 3 position in India	25 Tons - 60 Tons	Infrastructure, Construction, Logistics	Rs 7.0 -10mn	• 70-80% of the demand in the category comes from general infrastructure construction and road projects, we expect growth at a faster pace led by incremental expenditure in road projects under PMGSY and various other schemes .
Fixed Tower Cranes	Market Leader (>63% market share)	5 Tons- 25 Tons (Lifting Heights: up to 300 meters)	Infrastructure, Construction (especially Real Estate)	RS 6.0-6.5 mn	• These cranes are predominantly used in real estate development, thus this category will greatly benefit from the PM Awas Yojana which has been allocated Rs. 79,000 crore in the Union Budget 2023-24
Self-Erecting Tower Cranes	Market Leader (75-80% market share)	24 meters to 36 meters heights	Infrastructure, Construction (especially Real Estate)	Rs ~2.1 mn	• These cranes are used in lifting, shifting, concreting and erection jobs at civil construction sites for low to medium height projects.
Lorry Loader Cranes	No. 2 position in India	6 Tons to 50 Tons	Infrastructure, Construction, Logistics	Rs~1.1 mn	• These cranes are majorly sold to the government of India for their application in defence.

Source: Company, MNCL research

Unlocking value in CE industry

Indian Construction Equipment market is expected to grow 3x in the next 10 years on account of the rising investments in infrastructure development. The growing population in India has resulted in increased residential and commercial construction activities leading to significant growth in the recent past, with the incremental infrastructural push by the government, we expect the CE industry to grow by 10-15% in FY24E. Backhoe loaders (BHL) form a significant part of the CE industry due to their relatively lower cost and multi-functionality.

Exhibit 21: Construction Equipment sales in the country- FY20-25E CE sales growth could be ~3X of the past decade owing to favorable macroeconomic conditions



Source: ICEMA, Company, MNCL Research

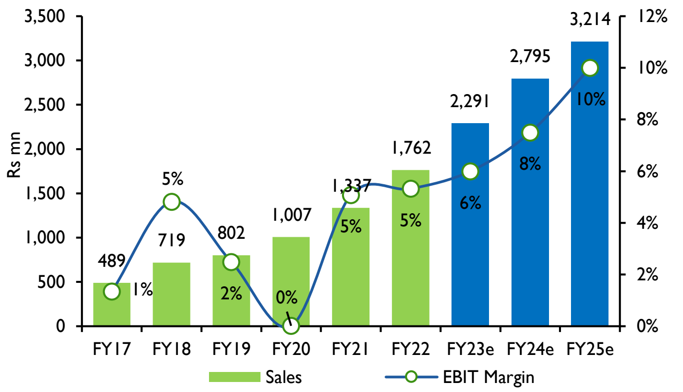
Backhoe loaders- enormous opportunity

India is the largest market for backhoe loaders which accounts for almost 50% of all construction equipment sales in unit terms. Backhoe loader is one of the key focus products for ACE due to significantly large addressable market size of Rs 90 Bn domestically. At present ACE has a very low market share (~2-3%) while JCB India is the market leader with ~70-80% market share, followed By Case New Holland Construction Equipment India which has a market share of ~7%.

ACE plans to capture this market by leveraging its brand name for cross selling with the existing customer base. Currently the cross selling between cranes and backhoe loaders is limited to the extent of 10-20%, but now with the product upgradation and resolution of previous supply chain issues, the company believes it will be able to increase its cross-selling potential to 50%. Additionally, ACE's backhoe loaders (BHL) are placed at a very competitive price point. Compared to its peers, ACE is currently compromising on margins to increase its market share.

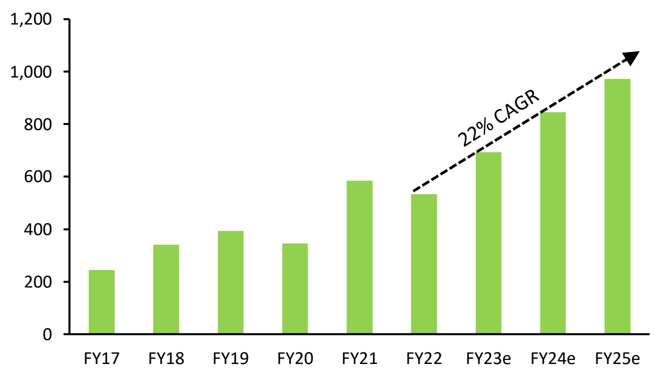
ACE has also introduced new models like Phantom 4x4 backhoe loader with Perkins engine to focus on European markets and tap into its export potential. Being positioned in a growing market, we believe ACE can leverage its existing sales & service network to grow at a market-beating rate of ~30-35% in the next 2-3 years by gaining incremental market share domestically as well as through export contributions.

Exhibit 22: Revenue from CE to increase and subsequent EBIT margin expansion (%)



Source: Company, MNCL Research

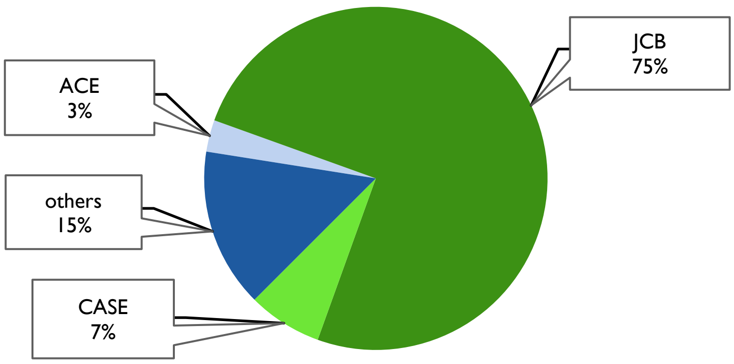
Exhibit 23: CE Units sold by ACE Ltd. to accelerate as the market size and share increase



Source: Company, MNCL Research

ACE should achieve incremental market share in this segment, supported by the high revenue growth outlook for BHLs and the cost-competitive positioning.

Exhibit 24: BHL - Domestic market share division for backhoe loaders- JCB dominates market



Source: Company, MNCL research

Exhibit 25: ACE is well-positioned to gain market share from the market leader

ACE V/S JCB		
Brand	**ACE**	**JCB**
Brand Value	ACE is market leader in the cranes segment and is focusing to leverage on brand value to increase cross selling	First mover advantage (starting in 1979). Reliable brand with high brand recall amongst customers for BHL
Price	Lowest cost producer amongst peers	JCB is 20-30% expensive as compared to ACE
Dealer network and after sales service	55-70 dealers across the country	60+ dealers across the country
Equipment Parts	Engines and transmission are outsourced	Fully backward integrated, uses inhouse engines and transmission system

Source: Company, MNCL research

Exhibit 26: Backhoe loaders- Positioning of ACE amongst peers- Lowest Cost producer

Company	Minimum value Range (RS)	Maximum value Range (RS)	Average price point (RS)
ACE Ltd.	17,00,000	33,00,000	25,00,000
CASE New Holland Construction Equipment	25,00,000	38,00,000	31,50,000
JCB India Pvt. Ltd.	29,00,000	38,00,000	33,50,000
Caterpillar India Pvt. Ltd.	34,00,000	44,00,000	39,00,000
Mahindra Construction Equipment	23,00,000	33,00,000	28,00,000
Tata Hitachi	29,00,000	2,51,00,000	1,40,00,000

Source: Industry, MNCL Research, Infrajunction

Exhibit 27: 74HP BHL market price comparison – ACE most efficient and economical

Brand	ESCORTS Digimax Super	ACE AX 124	TATA HITACHI Prime	MAHINDRA SX BSIV	JCB 3DX Plus
Power(hp)	74	74	74.3	74	74
Fuel Milage approx. (liter/hr)	6	5.5	5.5	4.5	5.5
Price RS Lakh	30	26.71	36	29.5	35.93

Source: MNCL research, Industry sources

Exhibit 28: 49HP BHL market price comparison – Lowest priced product closely followed by Mahindra

Brand	JCB 3DX	ACE AX 124 ECOMASTER	TATA HITACHI PRO	MAHINDRA SX SMART 50	JCB2DX
Power(hp)	49	49.5	47	49.2	49
Fuel Milage approx.. (liter/hr)	4.5	4.5	4	5	3.5
Price RS Lakh	33.78	25.43	33	25.7	20.19

Source: MNCL research, Industry sources

In both 49HP and 74HP BHL ACE is the most economical option available and has well positioned itself as the lowest cost producer.

Material Handling Equipment (MHE): Growing synergistically

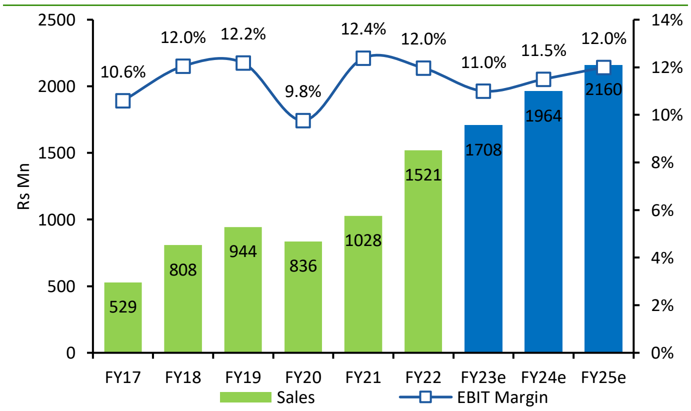
ACE entered the segment with forklifts and other warehousing equipment owing to the synergies of the segment with lower tonnage cranes used in internal logistics and manufacturing. Due to this ACE ltd was able to leverage its sales network to gain market share in the segment. *In this segment, 90% of sales are direct to customers where the company has a broad clientele ranging from Indian Army to Airport Authority of India, and FMCG companies like PepsiCo*. This segment helps ACE to build relations with the clients and leads to incremental wallet share of existing clients.

The domestic warehousing market is highly fragmented, resulting in higher average inventory holding, higher storage and handling losses, driven by lower level of mechanization. But lately, the sector has been attracting investments from government and international players, which is propelling the formalization of the sector. The demand for forklifts in MHE has seen particularly significant growth in the past few years due to strong growth in the sectors such as retail, e-commerce, manufacturing, warehousing and logistics. The Indian forklift market is expected to grow from 11234 units in 2019 to 30293 units in 2027, a CAGR of 13.2 % during the forecast period.

MHE sector is a highly competitive market. However, it is dominated by 4 players having almost equal market share - Toyota Material Handling India Pvt. Ltd., Voltas (Kion India), ACE Ltd. and Godrej. Apart from this, many forklift manufacturers are operating in India like Junghersich, Hyster, Yale, Clark, Doosan, Mitsubishi etc. ACE has been able to become the second largest manufacturer through its value proposition despite this high competition from MNC and local players. *ACE has positioned itself as one of the lowest price forklift providers in addition to being the only company to provide the heaviest weight lifting forklifts in the country*.

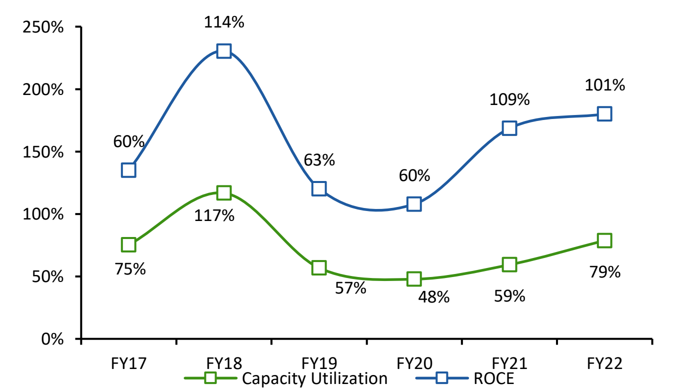
To gain incremental market share, ACE partnered with Doosan Corporation, a Fortune 500 company, which was one of the first foreign MHE brands to foray into India. It had its supremacy established globally through its technologically advanced and innovative products. Doosan brand is popular for its reliability and dependability, whereas ACE is the Indian brand grown with the core philosophy of offering 'reliable product at reasonable price and supported by prompt services'. ACE now represents Doosan premium MHE in India, besides its own range for the mass market. In Indian MHE market, 75-80% represents mass market and the remaining 20-25% is premium. The premium segment is mainly taken up by imported European and Japanese brands. But with this partnership, ACE has the potential to grow in the premium segment as well.

Exhibit 29: MHE unit – Revenue increase and subsequent EBIT margin expansion



Source: Company, MNCL Research

Exhibit 30: MHE unit has been a very lucrative segment and has led to incremental CU



Source: Company, MNCL Research

Growing revenue potential – Incremental Capex+ Acquisitions underway

ACE is increasing its revenue potential by strategically expanding, since the current capacity utilization has gone up to 75%. It is incurring a capex of Rs 300-400 mn, expanding current crane capacity by 40-50% with incremental revenue potential of Rs 7000—8000 mn. This incremental expansion will also lead to debottlenecking of the current facility in the other segments, thus providing additional space for manufacturing of material handling equipment of revenue potential ~Rs1000-1500 mn. This unit should become operational by Q2FY24E.

In FY24 the company has planned an additional capex of ~Rs 350mn for manufacturing cranes of higher tonnage, i. e. above 40 tons with revenue potential of Rs 3000-4000mn. The company is trying to enter this Chinese-dominated market and get a footing by leveraging its legacy brand name and established market leadership in the Indian crane market. This capacity will commence operations in FY25E.

Acquisitions- Growing Inorganically: In Q1FY23, ACE acquired two companies, one of which is a startup crane company operating in a very price-sensitive zone, and the second is a small company operating in pick and carry cranes having market share in rural markets. Both companies are crane manufacturing companies and have a capacity to generate Rs 100 to 150 mn of revenue. The motive for these acquisitions was to alleviate competition and maintain leadership in price-sensitive markets. The company has planned acquiring more companies which will enable ACE to integrate backward, supporting the company's margin profile and gain market share by acquiring the competition.

Exhibit 31: With limited incremental capex ACE can tremendously increase its revenue potential owing to high asset turnover

Source: Company, MNCL research

Broad comparison of key profitability metrics with comparable MNC players operating in India

The company's profit margins lag some of its peers because some of its products being priced at a discount, positioning itself at a very competitive cost. But the company will be able to expand margins over the medium term, aided by expectations of an increase in the scale of operations and benefits of operating leverage kicking in. This lag also provides headroom for growth as the brand gains incremental market share.

Exhibit 32: Peer comparison of revenue and profitability over the years

Financial performance	FY17	FY18	FY19	FY20	FY21	FY22
Sales (Rs Mn)						
Action Construction Equipment Ltd.	7,971	10,986	13,425	11,562	12,270	16,303
JCB India Ltd.	79,788	95,132	1,23,247	1,02,658	1,17,517	1,19,060
Caterpillar India Pvt Ltd.	42,380	62,409	88,358	59,089	46,000	80,335
Hyundai Construction Equipment India Pvt Ltd.	14,082	18,235	19,940	13,914	16,845	-
L&T Construction Equipment Ltd.	5,315	11,562	384	7,806	5,717	-
Komatsu India Pvt Limited	23,358	24,857	24,543	17,981	17,640	-
Operating Profit (Rs Mn)						
Action Construction Equipment Ltd.	399	921	979	918	1,193	1,523
JCB India Ltd.	11,415	14,073	18,405	18,098	21,572	17,314
Caterpillar India Pvt Ltd.	5,073	12,601	21,965	13,907	6,015	8,953
Hyundai Construction Equipment India Pvt Ltd.	1,228	1,167	760	-139	460	-
L&T Construction Equipment Ltd.	100	6,652	58	3,106	3,345	-
Komatsu India Pvt Limited	910	1,961	1,879	973	1,124	-
Operating Profit Margin (%)						
Action Construction Equipment Ltd.	5%	8%	7%	8%	10%	9%
JCB India Ltd.	14%	15%	15%	18%	18%	15%
Caterpillar India Pvt Ltd.	12%	20%	25%	24%	13%	11%
Hyundai Construction Equipment India Pvt Ltd.	9%	6%	4%	-1%	3%	-
L&T Construction Equipment Ltd.	2%	58%	15%	40%	59%	-
Komatsu India Pvt Limited	4%	8%	8%	5%	6%	-
Net Profit (Rs Mn)						
Action Construction Equipment Ltd.	145	526	562	526	802	1,059
JCB India Ltd.	6,592	8,416	10,790	11,747	14,338	11,379
Caterpillar India Pvt Ltd.	2,283	7,094	12,918	8,618	3,125	5,473
Hyundai Construction Equipment India Pvt Ltd.	730	639	262	-697	-9	-
L&T Construction Equipment Ltd.	-69	5,094	-8,342	2,399	3,818	-
Komatsu India Pvt Limited	26	1,152	1,985	134	402	-
Net Profit Margin (%)						
Action Construction Equipment Ltd.	2%	5%	4%	5%	7%	6%
JCB India Ltd.	8%	9%	9%	11%	12%	10%
Caterpillar India Pvt Ltd.	5%	11%	15%	15%	7%	7%
Hyundai Construction Equipment India Pvt Ltd.	5%	4%	1%	-5%	0%	-
L&T Construction Equipment Ltd.	-1%	44%	-2171%	31%	67%	-
Komatsu India Pvt Limited	0%	5%	8%	1%	2%	-

Source: Company, MNCL research

Countering Cyclicality by Evolving business model

ACE is dependent on the sales of Cranes and other construction equipment for majority of its earnings. The growth of construction equipment industry is interlinked with the growth of infrastructure sector and hence fluctuates with the fortunes of the Indian economy at large. A major portion of demand also comes from the requirement for intra-inter plant logistics, manufacturing process as well where the demand is again linked to the overall economy. In the last 27 years ACE has undergone many cycles and has evolved its business to sustain these cycles.

Exhibit 33: Cyclical timeline of events in the economy leading to a decadal lull in CE industry and consequent impact on ACE

FY2002-2007

Robust economic growth- The economy real GDP grew at a CAGR of 16%	During this period ACE grew at a robust CAGR of >60% owing to its low base and during this time became market leader in cranes

Great recession in 2008

The GDP growth rate declined to 3% in FY2008 with its effects persisting till 2010	During this time, ACE Ltd. revenue saw a corresponding dip in FY2009 and FY2010 when the growth became very restricted

Revival in 2011-12

The economic pace of growth became higher during this period coming from a low base due to GFC and overall economy reviving from the GFC	ACE saw a major bump up in sales during this period due to the sudden disruption in 2008-09. The company saw a revenue growth of 61% and 25% in FY11 & FY12 respectively.

Beginning of the decadal lull

Since FY12, economy had turned sluggish as the credit poilicies became stringent, GDP hit lows around 4.5% in FY13 and FY14.	This downturn was reflected in the business performance of the company with a decline of 21.9% and 7.9% in revenues in the respective years

Economic turn around in 2017

The economy transitioned in FY15 and FY16 growing at ~8% and 7% in FY17 with continuos momentum.	During FY15 & FY16 ACE saw a transitional phase coming out of the degrowth in the previous years and by FY17 the revenue registered a growth of 18%

The perfect storm

The economy had entered shortlived upcycle in FY17 which was repressed by external factors like- demonetization and GST Implementation. creating repurcussions in FY19 (Real GDP growth 3.5%) followed by economic downfall due to the pandemic in 2020	This upsurge in FY17 & FY18 was short lived and was suppressed again by external policy changes. But during this period ace started making changes in its business model and with higher asset turnovers the profitability increased

Where are we now?

During FY22, the ecocomy had started recovering from the pandemic, and the Govt increased its capital outlay by 33%. In FY23 the infrastructural push remained high aided by steady demand and increased profitability in private sector	During FY22 & FY23 the company revenues directly linked to the capital outlay increased at a similar rate. We expect this strong demand momentum to continue in the medium term

Source: MNCL Research

The company plans to counter the infrastructure sectoral multi-year cyclicality by evolving its business model and foraying into other businesses avenues that do not have overlapping cycles.

Our View: With the prolonged downcycle led by various external factors over the years the pent-up demand for the sector is high. The industry has gone through a perfect storm and transitioned to an upcycle. We believe that at this juncture, with the infra push by the government and the output gap in the economy created by the pandemic, followed by the Russia-Ukraine war and subsequent supply chain issues now behind us, this upcycle will be sustainable for the next 2-3 years, as all the growth drivers in place take effect.

However, cyclicity linked with the economy is intrinsic to the business. To counter this cyclicity, ACE is evolving its business model and foraying into other business avenues that are not directly interlinked.

Dampening the cyclicity

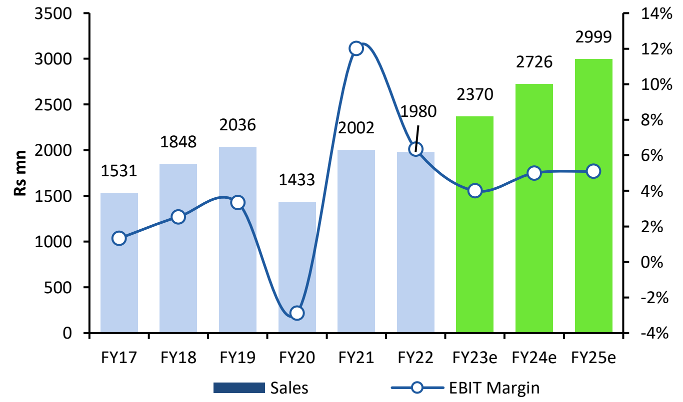
Agricultural equipment - easing the pain

The company manufactures a range of tractors, harvester combines and rotavators. Being a highly competitive industry, it is a mammoth task to gain market share in the segment. Currently this segment contributes 12% of the overall revenues (FY22). Further, ACE hold a minority market share in tractors but is positioned No.1 in South for its Harvester segment and has good tie ups with banks like Indusind bank, AU bank, Chola Bank, etc. to provide financing to the end users.

This sector is ancillary to the main business of cranes, construction equipment and material handling equipment, and not intended to be a standalone. It requires an entirely different sales and service network. However, presence in this segment provides a revenue stream that is not linked to the CE market, therefore helping in down cycles. The company's strategy is to maintain the contribution from the segment in the range of 10-15% as the revenue base increases and gradually penetrates 5-7% of the market.

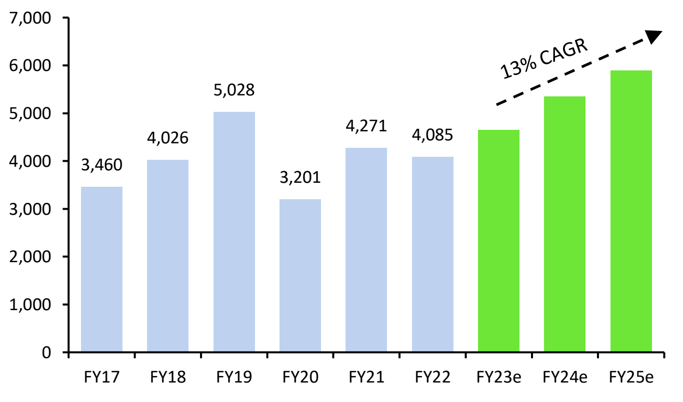
For sustainable growth in the segment, ACE plans on to enhance its international presence starting to focus on SAARC markets, viz. Myanmar, Iraq, Sudan, Tunisia, East Africa and Ethiopia etc. The company has subsequently launched Forma Range of tractors that are designed and engineered for the international markets. It is also trying to grow in the domestic market by introducing new and upgraded products like Orchard Special Tractor (26 HP, 4 WD) and Next-gen Light-weight Harvesters.

Exhibit 34: Focusing on stabilizing margins while increasing exports in agri-equipment



Source: Company, MNCL Research

Exhibit 35: Volume growth expected aided by export of agri equipment in African markets



Source: Company, MNCL Research

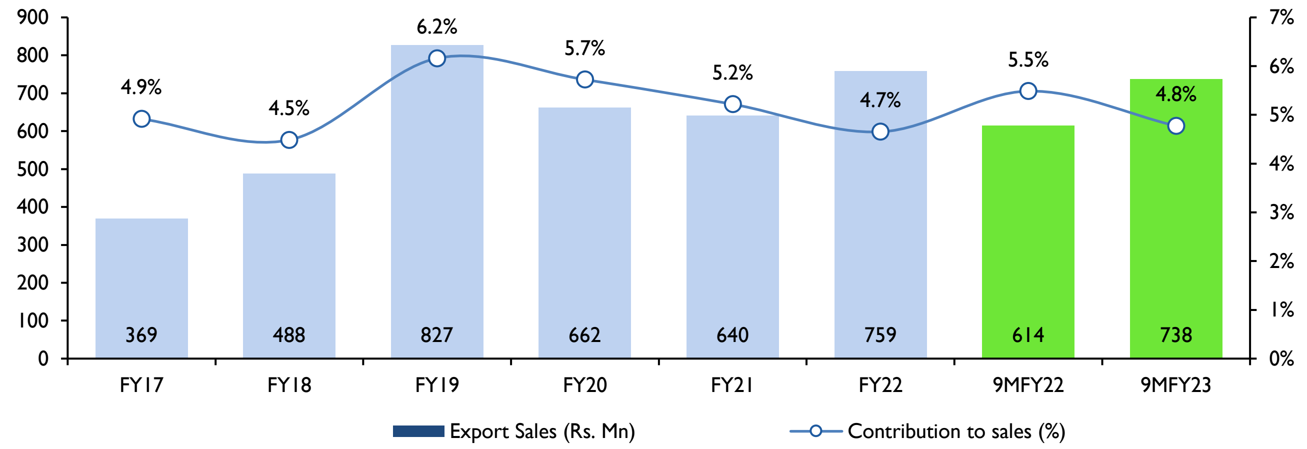
Exposure to exports

India is the 3rd largest CE market globally. With strong "make in India" agenda CE market is expected to be one of the champion exporting sectors for India

ACE exports to over 37 countries globally. However, until recently, exports have formed a very small part (2-3%) of revenues. But in Q4FY22, the company received an order from Government of Republic of Ghana for setting up a state-of-the-art assembly plant for manufacturing tractors and backhoe loaders for a total consideration of 24.98 Mn USD (approx. Rs 2bn). The said contract is secured through a credit agreement between the government of Ghana and the export import Bank of India. The project will be owned and operated by the Government of Ghana. The project involves designing, engineering, commissioning of assembly supply lines and supply of plant and machinery for the manufacturing in addition to transferring the technical know-how. The manufacturing unit will be installed with a capacity for production of 4500 tractors, 600 backhoes, 600 agricultural equipment implements and 300 tipping trailers annually. The contract also includes the supply of an initial pilot lot of tractors, backhoe and agriculture implements in CKD form for the assembly lines for manufacturing.

Subsequently, after commissioning of the plant, the prices of CKD kits shall be applicable as per the prevailing market rate at the time of supply. The company is expecting a realization of up to Rs.400mn crors in the current financial year and balance in FY24E. After setting up the new project, the company has the yearly potential to supply around RS. 1.5-4.0bn on a yearly basis by supplying CKDs and SKDs for machines which will be manufactured there. Further, on completion, the project will play a vital role in opening of export markets in Western African region for the company's products and augmenting the companies export efforts. Moving forward we expect ~10-15% contribution from exports.

Exhibit 36: Increasing overall share of exports - Ghana project to aid growth and visibility in African markets



Source: Company, MNCL Research

Exhibit 37: New range of products especially designed for international markets

Forma Range of Tractors

Backhoe Loader – Phantom 4x4

Source: Company, MNCL Research

- ACE intends to increase the contribution of exports in total revenues significantly over the next 2-3 years.
- ACE's products have been upgraded to new emission norms BS IV CEV, which is at par with European standards. This will help the company increase its sales and open up new opportunities in international markets.

Foray into defence

The Ministry of Defence, in Aug’20, introduced an import embargo on 101 items to push Aatmnirbhar Bharat (self-reliant India) and increase the indigenisation of defence production. This was then supplemented with an additional list of 108 items, all of which should be locally procured by 2025, in a phased manner. ACE has benefited from these policy changes as these new markets present ACE with the perfect opportunity for gain market share in the defence sector. The company has targeted the previously import-intensive products which are analogous to the company’s product portfolio and has won various defence orders over the past 2 years.

The company has been a supplier to Ministry of Defence for 482 nos. of 4x4 Multipurpose Tractors with special attachments for the Indian army (~50% of this order is already executed and the rest will be executed in FY24). The company is also the sole supplier for special purpose cranes for missile handling system. One of them is called MRSAL Medium Range Surface to AIR missile system which was imported into our country previously. ACE is also supplying specialised equipment to Tata Advance System, L&T Défense and DRDO

In the defence segment, the applicable products are new and ACE offering a wide product basket with larger application segment in addition to its knack for providing innovative and cost-effective solutions makes ACE a partner of choice for the Indian government as well as for larger private companies catering to the sector. In the next 2-3 years, we expect the contribution from defence to be 5-10%; it could be a margin-accretive business owing to customisation requirements.

With 5-10% of revenue coming from defence and another 10-15% from exports, the company will be able to generate some counter cyclicity in the business. The company is supported by strong financials and has built a business model that is adaptable enough to sustain the cyclicity of the business by hedging its financial risk.

Exhibit 38: Specialized Products for Defence sector in pipeline: Customized Cranes, Forklifts, Skid Steer Loaders, Multi Purpose Tractors, Tele handlers and special mobile equipment.

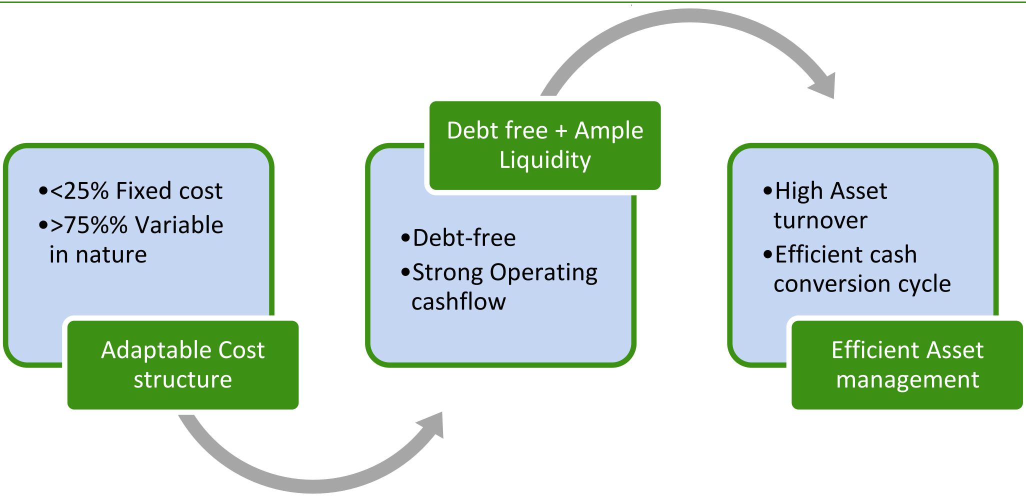
Source: Company, MNCL Research

Hedging Financial Risk

ACE has over the years oriented its financials to cushion cyclical impact, though it cannot be eliminated. *In a very capital-intensive space, ACE is one of the few players who have a debt-free or low-debt balance sheet. With ~80% expenses being variable in nature it can prudently adapt to the market scenario and protect its profitability. Further the high asset turnover limits the amount of capex required to grow the revenue potential of the company*.

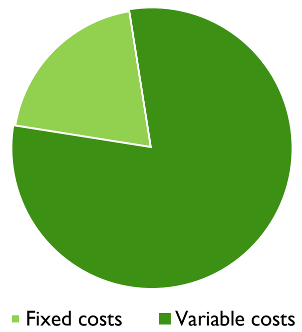
Most of the CE sales are funded by 3rd party banks and NBFCs the payment is done within ~30 days of product delivery. Dynamic inventory management and a comfortable credit period of 100-110 days enable ACE to meet its working capital requirements efficiently. Limited debt obligation, well-calibrated capex plans and ample liquidity buffers that ACE maintains make it capable of withstanding the economic cyclicity and managing financial risk.

Exhibit 39: How the company manages financial risk



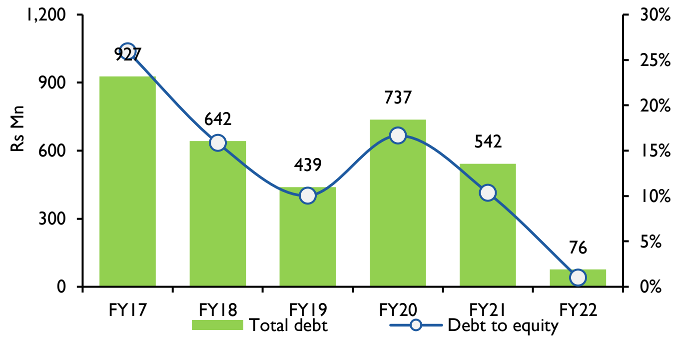
Source: MNCL research

Exhibit 40: Flexible cost structure shielding against downturn



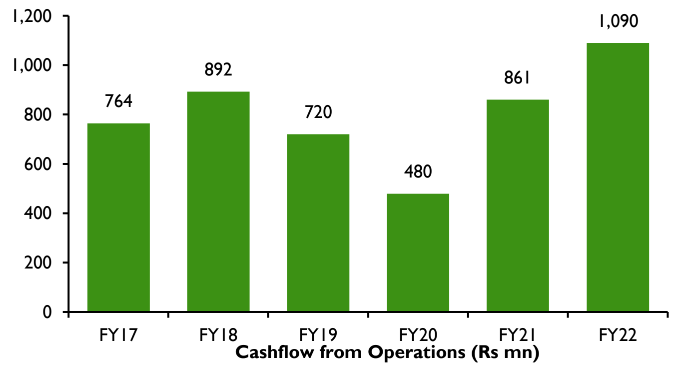
Source: Company, MNCL Research

Exhibit 41: Debt free capital structure



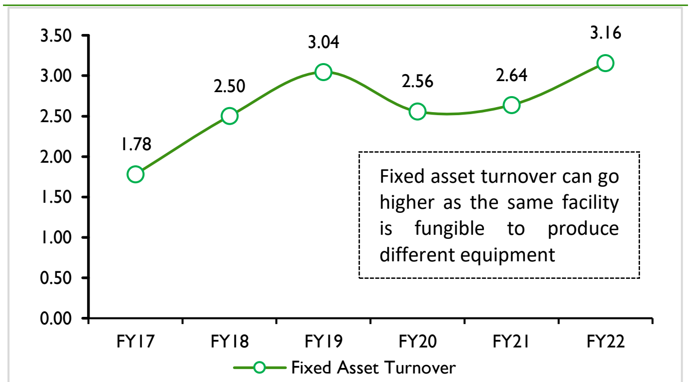
Source: Company, MNCL Research

Exhibit 42: Ability to generate high operating cashflows



Source: Company, MNCL Research

Exhibit 43: Limited capex can generate high revenue potential

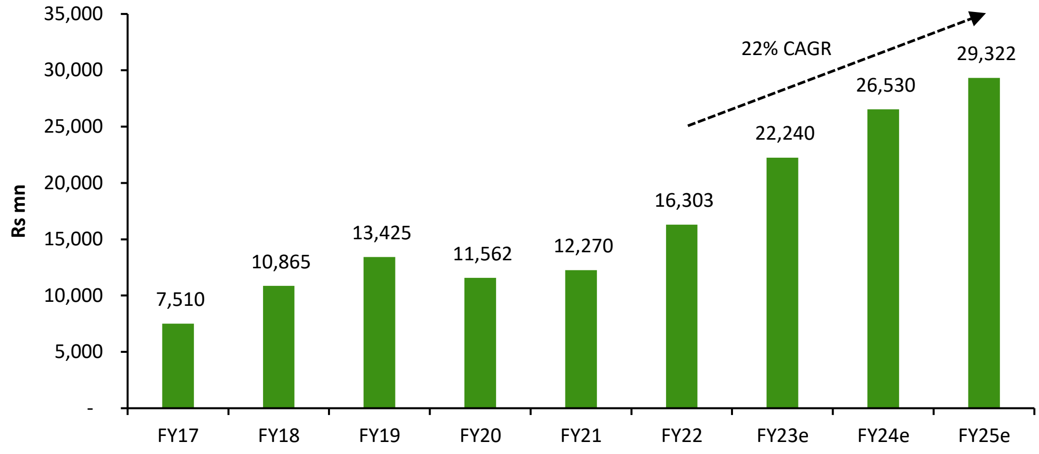


Source: Company, MNCL Research

Financial Analysis

Revenue growth is to be driven by robust volume demand in the cranes and construction equipment segment

Exhibit 44: Revenue to grow at a much faster pace

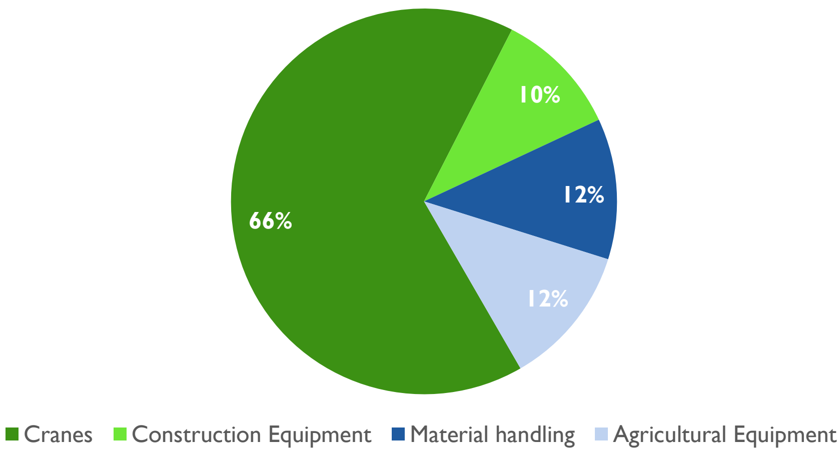


Source: MNCL Research Estimates

We expect the company to post revenue growth of 22% CAGR over FY22-25E. This is primarily predicated on volume growth as the construction equipment industry went through a decadal lull that has largely reversed and the massive public and private capex has begun.

We expect growth to be driven by incremental demand for cranes and gaining market share in the CE segment.

Exhibit 45: Revenue contribution pie should remain stable

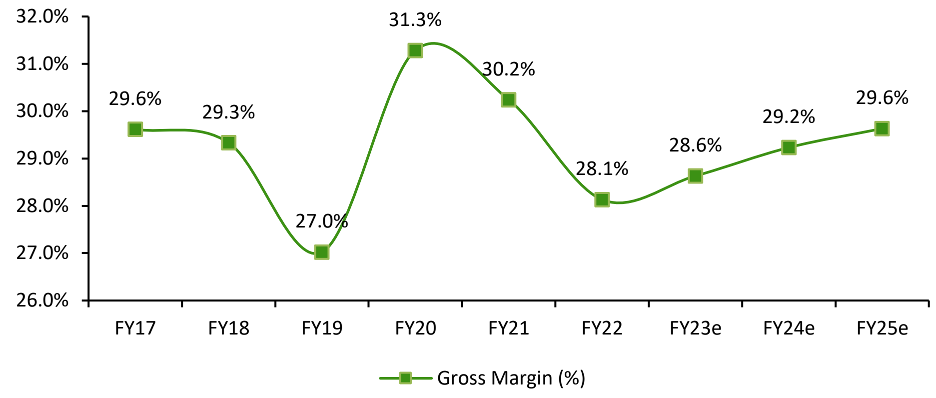


Source: MNCL Research Estimates

We expect the revenue contribution to largely remain on similar lines. However, the CE segment is expected to grow at a faster pace from FY23E-25E owing to the low base as the company focuses on gaining incremental market share. Cranes are expected to grow at a CAGR of 24% with the capacity utilization reaching higher levels.

Margins to grow as a contribution from Exclusive brands increases.

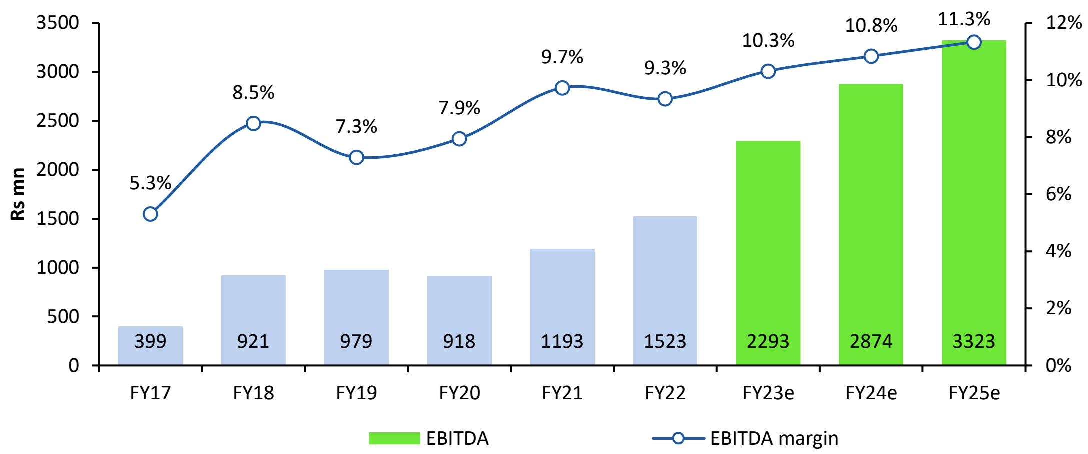
Exhibit 46: Gross margins, to sustain with policy changes



Source: MNCL Research Estimates

With the company changing its strategy for cranes and passing on the raw material costs to the customers taking advantage of its market leadership position, gross margins should stabilize moving forward.

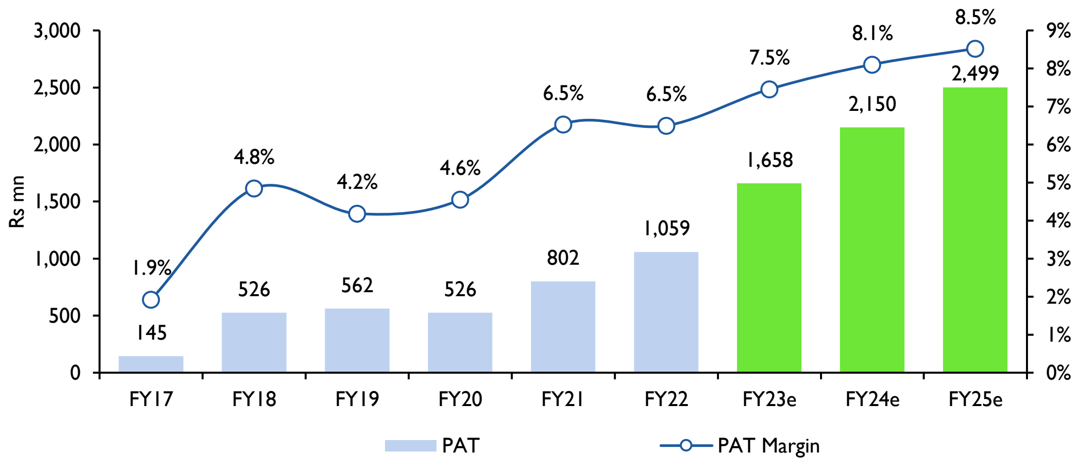
Exhibit 47: EBITDA and OPM growth to be at an accelerated pace



Source: MNCL Research Estimates

We expect ACE to post an EBITDA growth of 30% over FY22-25E, while margins will likely expand by close to 200bps YoY to 11.3%. This is likely driven by higher realization in the higher capacity crane class and incremental share from specialized equipment sales in exports and defence. Execution of high-priced orders increasing as the demand upsurge continues will further support the operating margin.

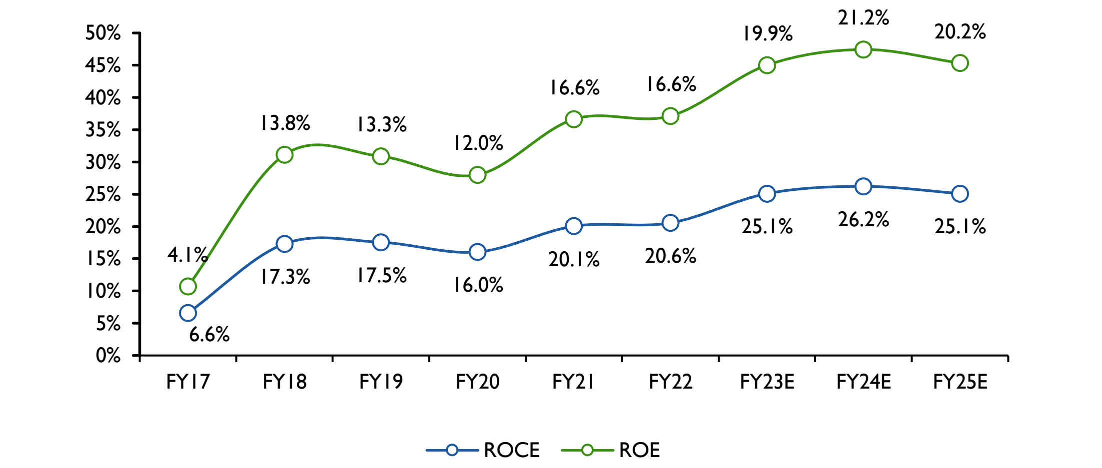
Exhibit 48: PAT growth to be at an increased pace as realization becomes higher



Source: MNCL Research Estimates

We expect the company to post a PAT growth of 33% over the same period, led by strong operating leverage and execution of higher-priced orders.

Exhibit 49: Incremental ROE & ROCE profile – Benefits of high asset turnover and flexible cost management kicking in



Source; MNCL Research Estimates

For the medium term we expect ROCE and ROE to sustain at higher levels owing to the higher asset turn as the demand surges and realizations rise.

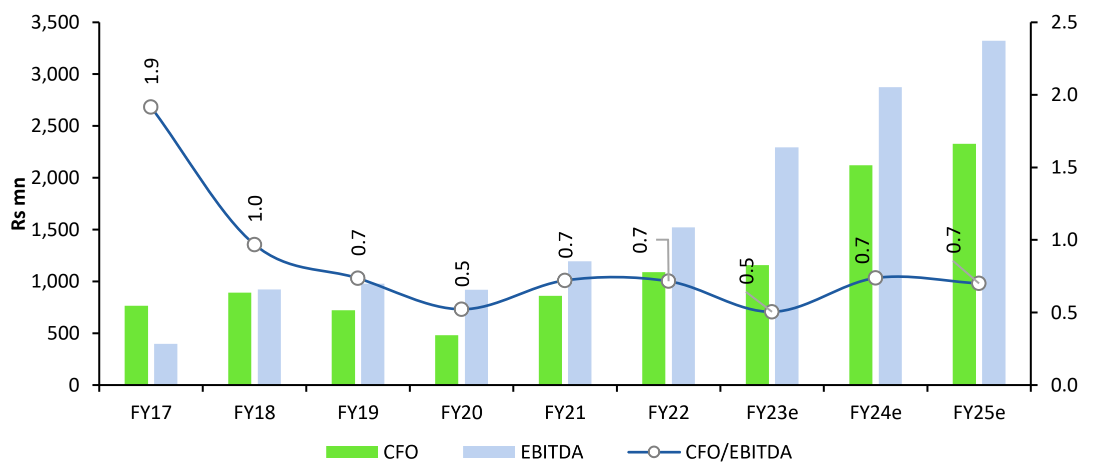
Exhibit 50: Efficiently managing the cash conversion cycle

Particulars	FY17	FY18	FY19	FY20	FY21	FY22
Receivable Days	50	57	39	46	67	42
Payable Days	102	112	101	144	138	111
Inventory Days	78	68	79	124	113	104
Cash Conversion Cycle	**27**	**13**	**17**	**26**	**43**	**35**

Source: Company, MNCL Research

The company increased its inventory days in FY20-22 on account of recurrent supply chain issues. ACE follows a dynamic inventory management approach and thus adapts very flexibly to the market situation. Being financed by 3rd party financiers, most of the payment is received within 30-45 days of product delivery. However, the company maintains a longer credit policy for its larger clients as a display of goodwill. On the supplier side the company gets a credit of ~90+ days. Overall, it does efficiently regulate its cash conversion cycle.

Exhibit 51: OCF to EBITDA- Ability to generate high cashflows



Source; MNCL Research Estimates

The company has been able to generate positive cashflows consistently over the years owing to high asset turnover and flexible cost management. Further the EBITDA to OCF conversion has been consistently above 50%, commendable for a capital goods company, and is expected to climb higher.

Exhibit 52: Segmental revenue & profitability to accelerate

Segment Revenue (Rs mn)	FY17	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E
Cranes	4,962	7,490	9,643	8,287	7,902	11,040	15,870	19,044	20,949
Construction equipment	489	719	802	1,007	1,337	1,762	2,291	2,795	3,214
Material handling equipment	529	808	944	836	1,028	1,521	1,708	1,964	2,160
Agriculture equipment	1,531	1,848	2,036	1,433	2,002	1,980	2,370	2,726	2,999

EBIT Margin (%)	FY17	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E
Cranes	8%	11%	9%	11%	11%	12%	12%	12%	13%
Construction equipment	1%	5%	2%	0%	5%	5%	6%	8%	10%
Material handling equipment	11%	12%	12%	10%	12%	12%	11%	12%	12%
Agriculture equipment	1%	3%	3%	-3%	12%	6%	4%	5%	5%

Source: Company, MNCL Research

Segmental revenue to be driven by better demand uptake. Margin expansion expected on account of higher capacity utilization and focus towards higher realization products.

Exhibit 53: Segmental ROCE(%)- All segments on incremental profitability trend

ROCE %	FY17	FY18	FY19	FY20	FY21	FY22
Cranes	11%	24%	26%	24%	20%	32%
Construction equipment	2%	6%	4%	0%	13%	18%
Material handling equipment	60%	114%	63%	60%	109%	101%
Agriculture equipment	-354%	-27%	-171%	-42%	89%	26%

Source: Company, MNCL Research

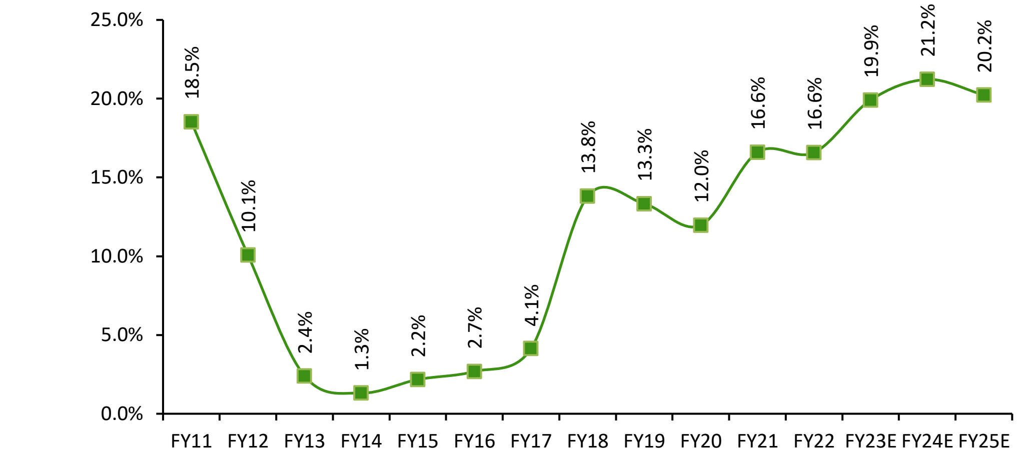
ACE has been able to turn its agri-equipment and CE segment profitable post the pandemic. These have previously been hurting the overall profitability of the business due to the incremental capital required to find a footing in the market. Owing to better demand and product positioning in the aforementioned segments, the company was able to break even and further turn the segments ROCE-accretive. We believe this incremental trend will further continue as ACE witnesses better uptake in the two segments.

Valuation – Transitioning Business cycle

ACE is the market leader in the cranes segment and has established itself as a key brand. With increasing government outlays for infrastructure, execution of higher priced orders and revival in private capex, we see a demand surge in the medium term for the construction equipment industry. We expect a stable demand going forward, as India embarks on its massive capex journey, turning in a multi-year upcycle for the construction equipment industry. Hence, the medium-term outlook remains bullish for the CE sector and ACE being a key beneficiary of these tailwinds would benefit from the demand momentum. We estimate FY22-FY25E EPS CAGR of 32%, with RoE of ~20% vs. ~14.5% RoE in the past 5 years. Average trailing PEs for last 6/10 years have been ~28x/~35x respectively.

We initiate coverage on ACE with TP at Rs 630 (30x FY25E EPS – 10% premium to its 6-year average 1 year forward PE). *The premium valuation is justified given the strong revenue growth visibility, margin expansion of ~200bps over FY23-25E following foray into specialized high margin products. The move towards construction equipment and defence space will mitigate the risk of cyclicality that the company has historically experienced*.

Exhibit 54: Return ratio improving on account of increased asset turnover and flexible cost management



Source: MNCL Research

Exhibit 55: 1-yr forward rolling PE

Source; MNCL research, Bloomberg

Currently the share price is below the 10 year average PE, making the risk-reward equation favourable for the company.

Exhibit 56: Risk Reward favorable! Our bull and bear case assessments

Scenario	FY25E EPS (RS)	PE (x)	Fair value (RS)	Upside (%)	Triggers	Our analysis
 Bull Case	*24*	*32 (x)*	*763*	*70%*	The demand surge continues with continued growth in private and public capital investments	Over the past 15 years the PAT margin has increased by 32% YoY on an average basis assuming the same growth momentum in FY25E, we estimate the EPS and given the robust growth it will lead to a premium valuation multiple
Base Case	*21*	*30*	*630*	*40%*		
 Bear case	*19*	*27*	*522*	*16%*	Macro-economic downturn, capital crunch, commodity inflation	Due to external factors if the future growth is subdued, with the current growth momentum and the investments already in place the company should grow by 7% on YoY basis. In case of this scenario we value the company at the 10 year forward PE (x) average of 27(x)

Source: MNCL Research estimates

Key Risks to our thesis

- **Exposed to cyclicality in end-user industries** – ACE is exposed to the underlying cyclicality of its end-user industries, primarily the CE industry, wherein growth is directly related to infrastructure investments, and more generally to domestic economic growth. Nevertheless, supported by the Government's focus on increasing infrastructure spending, construction activity is expected to see sustained recovery in the coming quarters, which will support volumes for the MCE industry, and in turn support ACE's revenues as well.
- **Pricing environment for key raw materials**: Steel is one of the primary inputs in the construction equipment business. With steel prices remaining at elevated levels, the ability to procure related steel products on timely basis and reasonable prices remains paramount to the profitability of the company. Any further increase in the price or delay in price normalization is a key risk to our earnings assumptions.
- **Ease of system credit availability:** A large part of the construction equipment business is driven by third-party financing due to the high upfront costs of the equipment. This is one of the reasons why almost all construction equipment manufacturers have tied up with financiers and regularly work with them to provide comfortable borrowing options for purchasers. Any system-wide liquidity hampering credit event or tightening of financing release, will impact the purchasing power of buyers, and in turn ACE's sales.
- **Competition from established foreign and domestic players**– The company faces stiff competition from established foreign and domestic players in the construction equipment and agri-equipment industries. In the construction equipment segment, it faces intense competition from JCB in the backhoe loader segment, Escorts, Volvo and Hitachi in the soil compactor segment, apart from Caterpillar and Case in the motor grader segment. The tractor segment is dominated by long-standing incumbents, such as Mahindra & Mahindra (M&M), Tractor & Farm Equipment Limited (TAFE) and Sonalika; and ACE faces significant competition from these players. Nevertheless, ACE has been focusing on improving its presence in these two segments by upgrading its product, strengthening its financial tie-ups and expanding its dealership network.

About The Company

Action Construction Equipment (ACE) Limited was established in 1995 by Mr. Vijay Agarwal, a technocrat, who has over 50 years of industry experience and is run by a team of experienced professionals. ACE is an established and reputed brand with a significant presence across diversified sectors like Construction, Infrastructure, Manufacturing, Logistics and Agriculture. The company has four verticals: Cranes, Material Handling, Construction Equipment and Agri-Equipment.

ACE Ltd is the world’s largest Pick & Carry cranes manufacturer with over 63% market share in the Mobile cranes segment in the country and a majority market share of more than 60% in Tower Cranes segment domestically. Additionally ACE also offers Crawler Cranes, Truck Mounted Cranes, Lorry Loaders, Backhoe Loaders/Loaders, Vibratory Rollers, Motor Graders, Forklifts, Tractors & Harvesters and other Construction Equipment.

ACE has 3 fabrication units, its production facilities are based in the Industrial townships in NCR, Haryana with a capacity to produce around 9,000 cranes, 1500 construction equipment, 1800 material handling equipment and 9,000 tractors annually. These facilities are engineered to be flexible in production and capacity. The fabrication, engine and transmission manufacturing lines are capable of manufacturing different products.

ACE is promoted by Mr. Vijay Agarwal, a first-generation entrepreneur with over 50 years of industry experience. Mr. Agarwal is supported by his son, Mr. Sorab Agarwal, who is responsible for overall marketing and new product initiatives. ACE has four manufacturing units with the mother plant at Palwal (Haryana), two fabrication units and an R&D centre in Faridabad (Haryana). The company went public in 2006 and is currently listed on both BSE and NSE with the promoters controlling 66.76% stake as on December 31, 2021.

Exhibit 57: Group Structure

Source: Company, MNCL Research

Exhibit 58: Segment summary

Segment Industry	Products	Market Size (RS bn)	Market share	Competition
Cranes	Pick & Carry, Crawler, Truck, Fixed Tower, Self-Erecting, Lorry Loader	15-20	60%	JCB, SANY, TIL India, Escorts, Kobelco, Liebherr, Schwing Stetter, etc.
Construction equipment	Backhoe Loaders, Vibratory Rollers, Motor Graders, Piling Rigs	80-90	2-3%	JCB, Case New Holland, CAT, Mahindra Construction Equipment, Tata Hitachi, Doosan Bobcat
Material handling equipment	Forklift Trucks, Warehousing Equipment	10	20-25%	Godrej, Toyota, Voltas (KION), Hyundai
Agriculture equipment	Tractor, Harvester Combines, Rotavator	-	-	Mahindra, Escorts, TAFE, New Holland, Sonalika

Source: MNCL research

Exhibit 59: Management Team

Name	Designation	About
Mr. Vijay Agarwal	Chairman & Managing Director	He is the promoter, Chairman & Managing Director of the company. Mr. Agarwal has over 50 years of industry experience in the field of material handling and heavy engineering industry to his credit. He has a degree in Mechanical Engineering & MBA from the Faculty of Management Studies (FMS), Delhi.
Mrs. Mona Agarwal	Whole Time Director	She is the Promoter and Whole-Time Director of the company. She has been associated with the company since its inception and is actively involved in the administrative and Human development, strategic transformations, business management and employee engagement processes.
Mr. Sorab Agarwal	Whole Time Director	Mr. Sorab Agarwal has a degree in Mechanical Engineering and is leading the Cranes and Equipment side of the business. Mr. Agarwal has been associated with the company for last 23 years. He has played a major role in setting up all India competent sales and services network.
Mr. Rajan Luthra	Chief Financial Officer	He has been associated with the company since 2010 and appointed as Chief Financial Officer with effect from July 31, 2014. He is a member of Institute of Company Secretary of India and Institute of Cost and Works Accountants of India. Prior to joining ACE, he was associated with Aryan Cargo Express Private Limited.
Mr. Ashok Anantharaman	COO- Agriculture	He is the Chief Operating Officer- Sales & Marketing (Tractor & AED Vertical) of the company since September 2, 2020. He holds a bachelor’s degree in Engineering from The Birla Institute of Technology and Science and PGDM from Indian Institute of Management, Bangalore. Prior to ACE, he was associated with CNH Industrial (India).
Mr. Chetan Kumar Gole	CEO - Forklifts	He has been associated with ACE since March 21, 2007. He has 30 years of experience in companies such as Elecon Engg. Ltd and Godrej & Boyce mfg. Co. Ltd. He holds a bachelor’s degree in Engineering from Sardar Patel University.
Mr. Mohammad Imteyaz Ahmed	Head Manufacturing (Tractor & AED Vertical)	He has 38 years in the Agricultural Equipment division with Escorts Limited and M/S Carraro India and led manufacturing verticals of assembly and testing of Tractors, Engines, Transmissions and Axles.
Mr. Manish Mathur	CEO – Cranes and Construction Equipment	He joined ACE in 1997 and under his leadership, ACE has been a dominant market leader in the crane segment.

Source: Company, MCNL Research

Corporate Governance

MNCL Research's AQCG Score

We analyze the company's accounting quality and corporate governance based on MNCL's proprietary AQCG score, which accounts for 14 different attributes in the accounting and corporate governance domain for at least 5 years and back tested on BSE 500 companies.

Quadrant 1: >=72% Quadrant 2: 65% - 71.9% Quadrant 3: 60% - 64.9% Quadrant 4: <60%

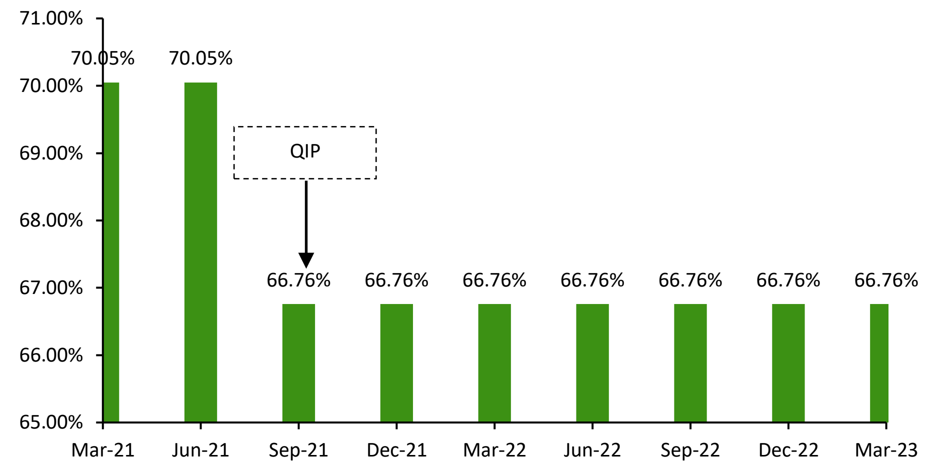
AQCG Score: 69% and 2nd quadrant

Interpretation of the score: A score of 69% signifies that ACE's financial reporting and governance policies are well in compliance with the widely accepted regulations, raising no red flags. A 2nd quadrant score signifies its above average positioning in corporate governance standards. The company misses a higher score due to the impact of pandemic on the business operations. We believe this score will improve over the next 2-3 years with the uptake in demand and good growth in EBITDA numbers.

Promoter group analysis

ACE is promoted by Mr. Vijay Agarwal, a first-generation entrepreneur with over 50 years of industry experience. Mr. Agarwal is supported by his son, Mr. Sorab Agarwal, who is responsible for overall marketing and new product initiatives. The company went public in 2006 and is currently listed on both BSE and NSE with the promoters controlling 66.76% . the promoter stake has gone down from 70% in FY21 due to QIP where the company raised ~Rs1.35bn via fresh issuance of 5.6mn shares at an issue price of Rs242/share (after a 5% discount on the floor price). Management raised this cash to deploy the fresh capital for funding 1) long-term growth of existing businesses, 2) organic or inorganic growth opportunities, 3) strategic acquisitions, and 4) long-term debt management.

Exhibit 60: Promoter holding in last two years



Source: MNCL Research

Related party transaction analysis

We believe that these transactions form part of usual operations and do not raise any red flags. The past 3-year details are as follows:

Exhibit 61: Related Party Transactions

Particulars (RS Mn)	FY20	FY21	FY22
Sales	15.05	42.14	21.55
Purchases	0.07	0.5	5.27
Rent received	0.05	0.085	0.11
Rent paid	-	-	0.24
Donation paid	1.82	1.42	1.6
Investment in equity	1.07	0	0.44

Source: MNCL research

Promoter compensation analysis

The promoter group draws a fixed salary. The past 3-year details are as follows-

Exhibit 62: Promoter remuneration

Name of Directors	Designation	FY20	FY21	FY22
Mr. Vijay Agarwal	Chairman & Managing Director	30.60	30.62	30.62
As % of PAT		5.8%	3.8%	2.9%
Mrs. Mona Agarwal	Whole Time Director	15.09	15.07	15.08
As % of PAT		2.9%	1.9%	1.4%
Mr. Sorab Agarwal	Whole Time Director	5.88	5.89	5.89
As % of PAT		1.1%	0.7%	0.6%
Mrs. Surbhi Garg	Whole Time Director	5.89	6.06	5.28
As % of PAT		1.1%	0.8%	0.5%

Source: MNCL research

Financials (Consolidated)

Income Statement

Y/E March (RS Mn.)	FY20	FY21	FY22	FY23E	FY24E	FY25E
Net Sales	**11,562**	**12,270**	**16,303**	**22,240**	**26,530**	**29322**
% growth	-14%	6%	33%	36%	19%	11%
Raw Materials	7,945	8,559	11,717	15,872	18,774	20,634
% of sales	69%	70%	72%	71%	71%	70%
Personnel	856	721	845	1,094	1,326	1,466
% of sales	7%	6%	5%	5%	5%	5%
Other Exp.	1,842	1,796	2,219	2,980	3,555	3,900
% of sales	16%	15%	14%	13%	13%	13%
EBITDA	**918**	**1,193**	**1,523**	**2,293**	**2,874**	**3,323**
EBITDA Margin (%)	8%	10%	9%	10%	11%	11%
Depreciation	130	139	153	161	172	179
EBIT	**788**	**1,054**	**1,370**	**2,132**	**2,702**	**3,144**
Interest Expenses	147	122	137	90	23	23
Other Income	40	153	150	168	188	211
PBT	**682**	**1,085**	**1,383**	**2,210**	**2,867**	**3,332**
Exceptionals	-	-	-	-	-	-
PBT after Exceptional	**682**	**1,085**	**1,383**	**2,210**	**2,867**	**3,332**
Tax-Total	156	283	324	553	717	833
Effective Tax Rate (%)	23%	26%	23%	25%	25%	25%
Reported PAT	**526**	**802**	**1,059**	**1,658**	**2,150**	**2,499**
PAT Margin	5%	7%	6%	7%	8%	9%
% Growth	-4%	54%	29%	53%	30%	16%

Source: MNCL Research Estimates, Numbers , *Reinstated Numbers

Balance Sheet

Y/E March (RS Mn.)	FY20	FY21	FY22	FY23E	FY24E	FY25E
SOURCES OF FUNDS						
Capital	227	227	238	238	238	238
Reserves & Surplus	4,198	5,008	7,305	8,868	10,923	13,303
Shareholders' Funds	4,425	5,235	7,544	9,106	11,161	13,541
Total debt	737	542	76	76	76	76
Def. tax liab	142	161	135	135	135	135
Total Liabilities	**9,512**	**10,551**	**12,823**	**15,697**	**18,780**	**21,888**
Gross Block	5,028	5,275	5,546	5,946	6,346	6,446
Accumulated Dep.	1,112	1,198	1,265	1,426	1,598	1,777
Capital WIP	182	125	243	243	243	243
Net Fixed Assets	**4,656**	**4,647**	**5,678**	**5,825**	**6,053**	**5,974**
Investments	280	64	688	688	688	688
Other non-current assets	130	97	65	65	65	65
Goodwill	-	-	-	-	-	-
Inventories	2,703	2,660	3,334	4,435	5,144	5,653
Sundry Debtors	1,473	2,246	1,887	2,620	2,907	3,213
Other Current Assets	479	357	643	707	776	852
Cash & Cash Equivalent	93	364	143	975	2,765	5,061
Loans and Advances	23	23	30	30	30	30
Total Current Assets	4,856	5,904	7,145	9,872	12,726	15,913
Trade Payables	3,205	3,305	3,610	4,783	5,658	6,218
Other Current Liabilities	231	380	418	460	506	557
Provisions	13	14	18	20	22	24
Total Current Liab. & Prov.	4,615	4,935	5,109	6,421	7,448	8,176
Net Current Assets	4,856	5,904	7,145	9,872	12,726	15,913
Total Assets	**9,512**	**10,551**	**12,823**	**15,697**	**18,780**	**21,888**

Source: MNCL Research Estimates

Key Ratios

Y/E March	FY20	FY21	FY22	FY23E	FY24E	FY25E
Growth ratios (%)						
Net sales	-14%	6%	33%	36%	19%	11%
EBITDA	-6%	30%	28%	51%	25%	16%
Adjusted Net Profit	-6%	52%	32%	57%	30%	16%
Margin Ratio (%)						
Gross Margin	31%	30%	28%	29%	29%	30%
EBITDA Margin	8%	10%	9%	10%	11%	11%
EBIT Margin	6%	9%	8%	10%	11%	11%
PBT Margins	5%	7%	6%	7%	8%	9%
PAT Margin	23%	26%	23%	25%	25%	25%
Return Ratio (%)						
ROCE	16%	20%	21%	25%	26%	25%
ROE	12%	17%	17%	20%	21%	20%
ROA	6%	8%	9%	12%	12%	12%
ROIC	12%	15%	16%	20%	24%	28%
Turnover Ratio days (days)						
Fixed Asset Turnover Ratio	2.6	2.6	3.2	3.9	4.5	4.9
Debtors Period	46	67	42	43	40	40
Creditors Period	144	138	111	110	110	110
Inventory Period	124	113	104	102	100	100
Net Working Capital Days	26	43	35	35	30	30
Solvency Ratio (%)						
Debt-equity (x)	0.4	0.4	0.3	0.2	0.1	0.2
Net debt- Equity	0.1	0.0	-0.0	-0.1	-0.2	-0.4
Interest Coverage ratio	5	9	10	24	118	138
Current Ratio	1	1	1	2	2	2
Per share (Rs)						
Basic EPS (reported)	4.6	7.1	9.1	13.9	18.1	21.0
CEPS	5.8	8.3	10.2	15.3	19.5	22.5
Book value	39.0	46.1	63.3	76.5	93.7	113.7
Valuation						
P/E	7.5	21.9	26.4	29.5	22.7	19.5
P/BV	0.9	3.3	3.8	5.4	4.4	3.6
EV/EBITDA	4.9	14.8	18.8	20.9	16.1	13.2
EV/Sales	0.4	1.4	1.8	2.2	1.7	1.5

Source: MNCL Research Estimates

Cash Flow

Y/E March (RS Mn.)	FY20	FY21	FY22	FY23E	FY24E	FY25E
Pre-tax profit	682	1,085	1,383	2,210	2,867	3,332
Net chg in working capital	(343)	(254)	(277)	(583)	(37)	(163)
Cash flow from operating activities (a)	**480**	**861**	**1,090**	**1,157**	**2,120**	**2,327**
Capital expenditure	(855)	(421)	(377)	(400)	(400)	(100)
Cash flow from investing activities (b)	**(196)**	**(162)**	**(2,018)**	**(112)**	**(212)**	**111**
Debt raised/(repaid)	(93)	(140)	(233)	-	-	-
Dividend (incl. tax)	(138)	-	(57)	(95)	(95)	(119)
Cash flow from financing activities (c)	**(334)**	**(404)**	**655**	**(125)**	**(118)**	**(142)**
Net chg in cash (a+b+c)	**146**	**698**	**(985)**	**950**	**1,813**	**2,319**

Source: MNCL Research Estimates

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