

# Covid 19 corollaries

July 27, 2020

## On skid row

The construction equipment (CE) business, comprising backhoes, excavators, cranes, compactors and loaders, has run into greasy grounds.

With the Covid-19 pandemic and attendant lockdown bringing construction activity to a halt, and labourers trudging back to the presumed safety of their native place, CE sales volume has nosedived ~70% on-year in the first quarter, and utilisation has nearly halved. This follows a 20% volume decline in fiscal 2020.

The second half of the current fiscal could see more whirr and hum. However, volume could retract by a third on-year this fiscal, especially since public spending will be diverted towards healthcare and public welfare. That means lower investments in infrastructure and ergo, slack demand for CE.

Excavators (~23% of total sales), more expensive and niche, will see a sharper volume de-growth. Backhoe loaders (~45%) may be relatively less impacted owing to their lower cost and multi-functionality. Crane volume (~9%) is expected to dip with slowdown in the cement, power and auto sectors. Compactor volume (~4%) would compact as highway construction declines 10-13% on-year this fiscal.

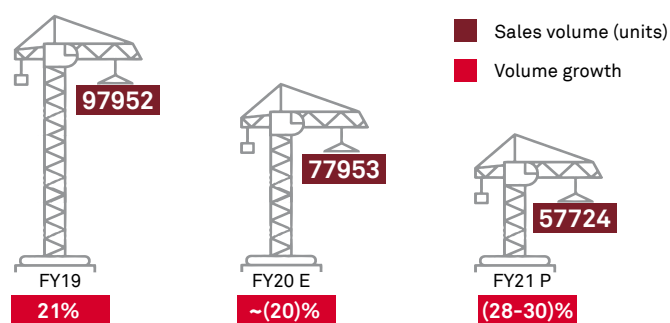
Operating margins, which fell 350-400 bps to 7-8% in fiscal 2020, could contract another 200-250 bps. A drop in utilisation would translate to higher fixed costs (25-30% of total costs), driving margins down. But a 6-7% decline in steel prices might offer some cushion.

The bright side is that the industry has low debt and healthy interest coverage, our analysis of companies accounting for close to 60% of CE sales in fiscal 2019 shows. They have low gearing between 0 and 1, and high financial flexibility because of multinational parentage.

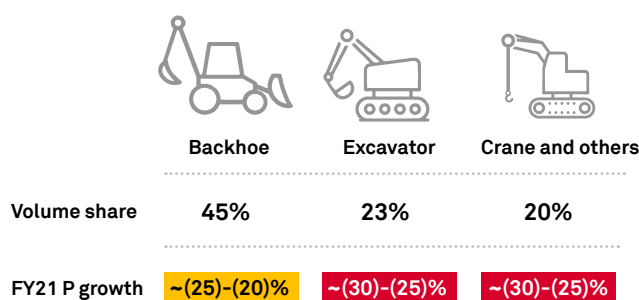
However, low utilisation remains the stick in the mud.

## Downhill drive

### CE volumes continue to fall



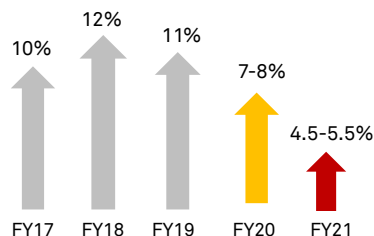
### Excavator, crane sales worse off than backhoes



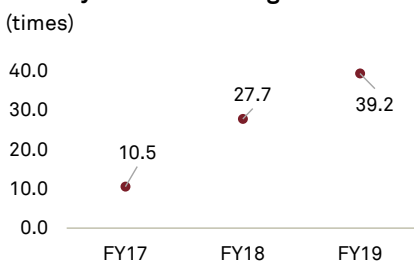
Note: P- Projected, E- Estimated, 'others' include: wheel loaders, motor grader, skid-steer loader, track-type loader, off-highway truck, pick and carry cranes, crushers and screeners, compactors and pavers; equipment accounting for ~89% volume share as of FY20; concrete equipment not included  
Source: CRISIL Research

## Margin in a slush, gearing lends traction

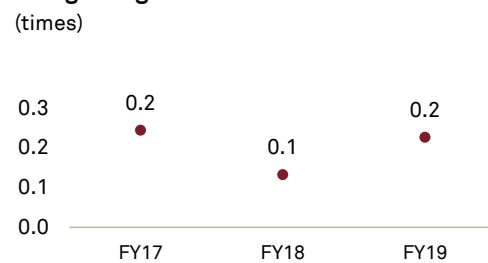
### Operating margins at a five-year low



### Healthy interest coverage ratio



### Low gearing



Note: P- Projected, E- Estimated; aggregate includes financials of JCB India, Tata Hitachi Construction Equipment, Escorts Ltd and ACE  
Source: CRISIL Research