

7 February 2020

KEC International

Sturdy order-book; maintaining a Buy

The strong order book and better execution in T&D and Railways drove KEC's ~16% y/y revenue growth. After sluggish order inflows in H1 FY20, Q3 FY20 saw strong, 37% y/y, order inflow growth. With a ₹220bn order book and more than ₹25bn in L1, management maintained 15-16% revenue growth in FY20. Margins are expected to hold at present levels (~10.4%). We have rolled forward our estimates to FY22 and maintain a Buy rating, with a revised TP of ₹423 (13x the mean PER on FY22e earnings).

Strong order inflow growth in non-T&D. The Railways and the civil segments saw strong order inflows, leading to 68% y/y growth in orders. In Railways, traction was seen in track-laying, signalling, OHE and station building. Management said its Railways business would touch ₹25bn in FY20 driven by the sturdy ~₹70bn order backlog. Management expects its civil business to touch ₹40bn in the next 3-4 years.

T&D expected to be led by SEBs. With soft tendering by PGCIL, orders from SEBs and the Green Energy Corridor (GEC) are expected. Management said that states like Tamil Nadu, Rajasthan, Gujarat, West Bengal and Odisha would drive T&D capex. With the recent delay in awarding of GEC orders, fast-track tendering is expected in the next 2-3 weeks. International T&D will continue strong with traction from the Middle East, Africa and the Far East.

Outlook. Though sales growth is expected to be strong, margins are expected to hold at current levels. The company expects order inflows of ₹140bn in FY20 and a similar figure in FY21. Despite the strong order book and L1 for ₹25bn, we expect revenue and PAT CAGRs over FY19-22 of respectively 10% and 13%. We maintain a Buy with a revised TP of ₹423. **Risks:** Slowdown in ordering and pace of execution.

Key financials (YE Dec)	FY18	FY19	FY20e	FY21e	FY22e
Sales (₹ m)	1,00,526	1,10,005	1,26,126	1,40,222	1,53,522
Net profit (₹ m)	4,583	4,864	6,271	7,466	8,362
EPS (₹)	17.8	18.9	24.4	29.0	32.5
PE (x)	21.9	15.8	13.9	11.7	10.4
EV / EBITDA (x)	11.3	7.9	8.0	7.2	6.6
PBV (x)	5.0	3.2	3.0	2.4	2.1
RoE (%)	25.6	21.9	23.3	22.9	21.4
RoCE (%)	24.4	26.1	25.0	24.2	24.0
Dividend yield (%)	0.6	0.9	1.1	1.3	1.4
Net debt / equity (x)	0.7	0.6	0.6	0.6	0.5

Source: Company, Anand Rathi Research

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Rating: **Buy**

Target Price: ₹423

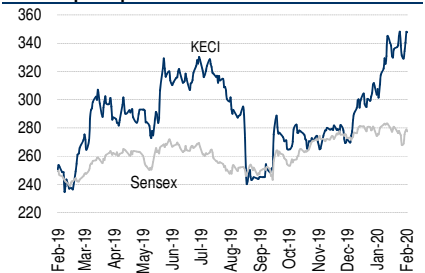
Share Price: ₹339

Key data	KECI IN / KECL.NS
52-week high / low	₹358 / 230
Sensex / Nifty	41142 / 12098
3-m average volume	\$1.5m
Market cap	₹89bn / \$1251.4m
Shares outstanding	257m

Shareholding pattern (%)	Dec'19	Sep'18	Jun'19
Promoters	51.6	51.6	51.4
- of which, Pledged	-	-	-
Free float	48.4	48.4	48.6
- Foreign institutions	7.6	7.6	6.7
- Domestic institutions	27.8	27.0	26.3
- Public	13.0	13.8	15.6

Estimates revision (%)	FY20e	FY21e
Sales	0.4	-5.1
EBITDA	1.0	-3.4
PAT	11.9	11.7

Relative price performance



Source: Bloomberg

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Quick Glance – Financials and Valuations (consolidated)

Fig 1 – Income statement (₹ m)

Year-end: Mar	FY18	FY19	FY20e	FY21e	FY22e
T&D order book	1,72,980	2,03,070	2,18,425	2,37,502	2,64,548
Net revenues	1,00,526	1,10,005	1,26,126	1,40,222	1,53,522
Growth (%)	17.1	9.4	14.7	11.2	9.5
Material cost	72,670	81,230	90,180	99,971	1,09,454
Employee & Other expense	17,800	17,276	22,621	25,274	27,710
EBITDA	10,057	11,499	13,325	14,977	16,359
EBITDA margins (%)	10.0	10.5	10.6	10.7	10.7
- Depreciation	1,097	1,171	1,309	1,471	1,634
Other income	207	226	230	253	279
Interest expenses	2,294	3,119	3,536	3,389	3,389
PBT	6,873	7,435	8,710	10,370	11,615
Effective tax rate (%)	33.3	34.6	28.0	28.0	28.0
+ Associates / (Minorities)	-	-	-	-	-
Net Income	4,583	4,864	6,271	7,466	8,362
Adjusted income	4,583	4,864	6,271	7,466	8,362
WANS	257	257	257	257	257
FDEPS (₹ / sh)	17.8	18.9	24.4	29.0	32.5
EPS growth (%)	50.4	6.1	28.9	19.1	12.0

Fig 3 – Cash-flow statement (₹ m)

Year-end: Mar	FY18	FY19	FY20e	FY21e	FY22e
PBT	6,873	7,435	8,710	10,370	11,615
+ Non-cash items	3,184	4,064	4,615	4,607	4,744
Oper. prof. before WC	10,057	11,499	13,325	14,977	16,359
- Incr. / (decr.) in WC	737	6,555	7,642	6,280	6,588
Others incl. taxes	2,392	2,346	2,625	2,904	3,252
Operating cash-flow	7,138	2,653	3,058	5,793	6,519
- Capex (tang. + intang.)	1,452	1,048	2,500	2,500	2,500
Free cash-flow	5,686	1,604	558	3,293	4,019
Acquisitions	-	-	-	-	-
- Div.(incl. buyback & taxes)	743	843	1,129	1,344	1,505
+ Equity raised	-	-	-	-	-
+ Debt raised	-3,688	574	7,089	-2,558	1,000
- Fin investments	911	261	-13	-15	-16
- Misc. (CFI + CFF)	111	626	4,227	3,665	3,643
Net cash-flow	233	449	2,304	-4,259	-112

Source: Company, Anand Rathi Research

Fig 5 – Price movement



Source: Bloomberg

Fig 2 – Balance sheet (₹ m)

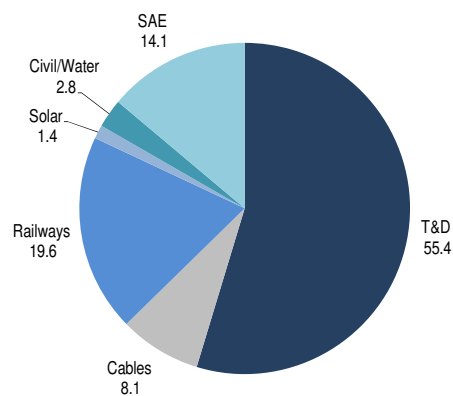
Year-end: Mar	FY18	FY19	FY20e	FY21e	FY22e
Share capital	514	514	514	514	514
Net worth	19,975	24,351	29,493	35,616	42,473
Debt	16,394	16,968	24,058	21,500	22,500
Minority interest	-	-	-	-	-
DTL / (Assets)	1,272	1,497	1,310	1,310	1,310
Capital employed	37,641	42,816	54,861	58,426	66,283
Net tangible assets	8,288	8,666	11,051	12,080	12,946
Net intangible assets	915	1,121	-	-	-
Goodwill	1,920	2,037	2,037	2,037	2,037
CWIP (tang. & intang.)	781	73	-	-	-
Investments (strategic)	-	-	-	-	-
Investments (financial)	393	132	145	160	176
Current assets (ex cash)	90,781	1,02,154	1,18,913	1,32,965	1,46,440
Cash	2,313	2,762	5,066	807	695
Current liabilities	67,749	74,129	82,352	89,623	96,011
Working capital	23,032	28,025	36,562	43,342	50,429
Capital deployed	37,641	42,816	54,862	58,426	66,283
Contingent liabilities	11,220	11,814	-	-	-

Fig 4 – Ratio analysis

Year-end: Mar	FY18	FY19	FY20e	FY21e	FY22e
P/E (x)	21.9	15.8	13.9	11.7	10.4
EV / EBITDA (x)	11.3	7.9	8.0	7.2	6.6
EV / Sales (x)	1.1	0.8	0.8	0.8	0.7
P/B (x)	5.0	3.2	3.0	2.4	2.1
RoE (%)	25.6	21.9	23.3	22.9	21.4
RoCE (%) - after tax	24.4	26.1	25.0	24.2	24.0
RoIC (%) - after tax	18.7	19.4	20.5	19.1	18.1
DPS (₹ / sh)	2.4	2.7	3.7	4.4	4.9
Dividend yield (%)	0.6	0.9	1.1	1.3	1.4
Dividend payout (%) – incl. DDT	16.2	17.3	18.0	18.0	18.0
Net debt / equity (x)	0.7	0.6	0.6	0.6	0.5
Receivables (days)	183	272	275	277	279
Inventory (days)	23	21	21	21	21
Payables (days)	188	178	168	162	157
CFO : PAT %	155.7	54.5	48.8	77.6	78.0

Source: Company, Anand Rathi Research

Fig 6 – Q3 FY20 revenue break-up



Source: Company

Result Highlights

Fig 7 – Segment-wise results (consolidated)

₹ m	Q3 FY20	Q3 FY19	% Y/Y	9MFY20	9M FY19	% Y/Y
T&D	17,030	15,630	9	46,190	39,050	18
SAE	4,320	1,950	122	10,930	6,480	69
Cables	2,490	3,100	(20)	7,610	8,340	(9)
Railways	6,010	5,510	9	16,910	12,850	31
Solar	420	160	163	950	3,090	(69)
Civil / Water	870	1,100	(21)	2,040	3,350	(39)
Intersegmental	(410)	(980)		(1,690)	(1,563)	8
Total	30,730	26,470	16	82,940	71,597	16

Source: Company

Fig 8 – Order book

₹ m	FY18				FY19				FY20			Y/Y (%)
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	
Transmission - Total	1,10,962	1,16,308	1,25,180	1,22,816	1,27,519	1,40,945	1,50,322	1,40,118	1,33,112	1,15,744	1,06,753	(29)
- SAE	12,179	21,020	17,148	19,028	18,373	20,135	20,592	20,307	13,311	10,417	13,427	(35)
Cables	2,706	2,803	3,430	3,460	2,547	4,027	4,118	4,061	3,803	3,617	4,182	2
Solar+Smart Infra	4,060	2,803	3,430	1,730	364	2,014	618	2,031	1,902	1,809	2,421	292
Railways	13,532	14,013	36,011	41,515	47,297	50,338	47,362	52,798	47,540	52,447	68,454	45
Civil/Water	4,060	4,204	3,430	3,460	4,184	4,027	4,118	4,061	3,803	7,234	24,872	504
Total	1,35,320	1,40,130	1,71,480	1,72,980	1,81,910	2,01,350	2,05,920	2,03,070	1,90,160	1,80,850	2,20,110	7

Source: Company

Fig 9 – Order intake

₹ m	FY18				FY19				FY20			Y/Y (%)
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	
Transmission - Total	22,320	24,231	25,769	24,307	13,932	36,039	24,041	13,308	6,579	2,836	25,347.4	5.4
SAE	1,395	9,524	1,511	2,668	330	6,809	4,391	1,146	1,450	810	882	-79.9
Cables	3,348	2,974	2,718	1,529	2,034	4,312	2,878	635	3,680	1,442	2,832	-1.6
Railways	-	1,149	25,632	12,474	9,288	8,162	3,304	10,231	-	18,830	12,594	281.2
Solar	-	575	(236)		110	1,873	323	511	-	100		
Civil/Water	2,232	642	1,647	9	2,116	1,453	1,043	2,430	892	3,251	19,818	1800.8
Total	27,900	29,570	55,530	38,319	27,480	51,840	36,000	25,540	11,151	26,459	60,592	68.3

Source: Company

Fig 10 – Cost structure

₹ m	FY17				FY18				FY19				FY20			% Y/Y
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	
Sales	17,487	20,742	19,123	28,492	18,568	21,322	24,049	36,642	21,047	24,085	26,466	38,412	24,125	28,088	30,731	16.1
Material cost	8,208	10,223	8,426	14,790	8,262	10,331	11,720	21,134	10,123	12,063	12,585	19,326	11,157	13,903	14,388	14.3
Employee cost	1,735	1,872	1,857	1,864	1,913	1,946	1,916	2,208	2,034	2,068	2,111	2,109	2,217	2,747	3,014	42.8
Erection and sub-contracting charges	3,899	4,410	4,593	4,941	4,347	4,486	5,663	6,774	5,145	5,095	6,418	10,481	5,717	5,538	7,035	9.6
Other expenses	2,151	2,384	2,429	3,886	2,282	2,400	2,310	2,827	1,584	2,327	2,539	2,505	2,520	2,962	3,110	22.5
% of sales																
Material cost	46.9	49.3	44.1	51.9	44.5	48.5	48.7	57.7	48.1	50.1	47.6	50.3	46.2	49	47	
Employee cost	9.9	9.0	9.7	6.5	10.3	9.1	8.0	6.0	9.7	8.6	8.0	5.5	9.2	10	10	
Erection and sub-contracting charges	22.3	21.3	24.0	17.3	23.4	21.0	23.5	18.5	24.4	21.2	24.2	27.3	23.7	20	23	
Other expenses	12.3	11.5	12.7	13.6	12.3	11.3	9.6	7.7	7.5	9.7	9.6	6.5	10.4	11	10	
EBITDA margins (%)	8.6	8.9	9.5	10.6	9.5	10.1	10.2	10.1	10.3	10.5	10.6	10.4	10.4	10.5	10.4	

Source: Company

Concall highlights

Financial

- Forex gain in Q4 FY20: ₹250m;

Because of the amount received from Saudi Arabia (₹6.9bn), the company announced interim dividend of 170% of the face value, at ₹3.40 a share. Total outflow: ₹1,055m (including the dividend-distribution tax.)

- Loans are now taken in foreign currency to act as a natural hedge for cashflow from the higher international business. Interest cost has come down to the guided-to level of 2.7%, from 3.2%

T&D (Domestic)

- PGCIL ordering has been under pressure. A pick-up in ordering looks challenging due to the new TBCB norms and other new norms. PGCIL ordering needs to be replaced for new strong ordering growth.
- The extended monsoon and delay in delivery of substation equipment led to flattish revenue.
- Major traction is seen from SEBs such as Tamil Nadu, West Bengal, Odisha, Rajasthan, Telangana and Gujarat
- The private sector has been muted. Expect some ordering in the next 10-15 days. There has been some delay in these awards due to the CERC petition.

T&D (International)

- T&D growth of 21% mainly came from International and SAE.
- Middle East, Africa, Malaysia and Mexico are coming out with various EPC tenders.
- SAE: Good execution in 9M FY20. Order inflows have been weak. Signed a couple of deals for EPC. However, a few delays are there. The company is L1 in a few deals. Not much growth is seen for next year.
- No overdue position of Saudi.

Railways and Civil

- Double-digit margins are expected in Railways.
- Bidding pipeline for conventional Railways is huge. Now, KEC is also bidding for metro-rail track-laying and signalling.
- No issue in railway tendering is seen; however, some slippages are seen. ₹400bn has been allocated in the Budget for station re-development.
- Management firmly said it is not going in for any development model.
- Civil business saw less-than-expected revenue growth because of headwinds such as muted industrial capex and challenges in real estate. However, some improvement has now been seen.
- Execution of Delhi (₹20bn) and Kochi metro-rail has started. However, such revenue will start coming from Q4 FY20. Management is very bullish on this segment. At present, it has four civil orders for

the metro. It is looking at ₹40bn in next 3-4 years.

- Civil business mainly consists of B&F (commercial, residential [not much focused]), metro-rail, etc. Competition has reduced in this space. However, not much in Industrials due to weak demand. Thus, management is looking at other sectors (such as Oil & Gas and Defence).

Cables

The impact of commodity prices (metals, copper) impacted revenue. Also, floods at the Baroda plant hurt revenue. However, margin improvement is seen. Margins are better than last year.

Guidance

- L1: ₹25bn, mainly from the T&D business. (SAE and international)
- Maintained FY20 guidance: sales 14-15%, OI ₹140bn, margins 10-10.5%
- FY20 net debt: ₹24bn. For Q4, slightly less is expected (-1bn) due to good collections.

Valuation

With its strong order book and healthy L1 position, KEC has sound revenue assurance. With increasing traction from the Railways and its civil business, prospects are promising. However, the pace of execution would be a key point to watch. We expect earnings to record a 13% CAGR over FY19-22. Hence, we maintain our Buy rating, with a TP of ₹423 (13x the mean PER on FY22e earnings).

Fig 11 – Change in estimates

₹ m)	Old		Revised		% Change	
	FY20e	FY21e	FY20e	FY21e	FY20e	FY21e
Revenue	125,598	1,47,675	1,26,126	1,40,222	0.4	-5.1
EBITDA	13,188	15,506	13,325	14,977	1.0	-3.4
EPS (₹)	21.8	26.0	24.4	29.0	11.9	11.7

Source: Anand Rathi Research

Fig 12 – One-year-forward PER



Source: Company, Anand Rathi Research

Key risks

- Slowdown in orders awarded.
- Slower pace of execution.

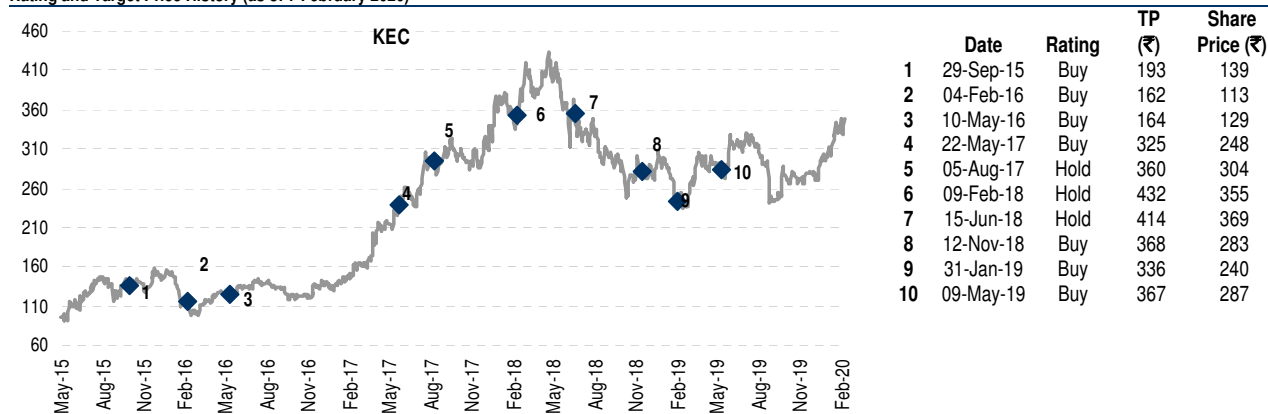
Appendix

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