



3R MATRIX

	+	=	-
Right Sector (RS)	✓	■	■
Right Quality (RQ)	✓	■	■
Right Valuation (RV)	✓	■	■

+ Positive = Neutral - Negative

What has changed in 3R MATRIX

	Old		New
RS	■	↔	■
RQ	■	↔	■
RV	■	↔	■

Reco/View

Reco: Buy	↔
CMP: Rs. 332	
Price Target: Rs. 400	↑

↑ Upgrade ↔ Maintain ↓ Downgrade

Company details

Market cap:	Rs. 9,348 cr
52-week high/low:	Rs. 335/114
NSE volume: (No of shares)	2.2 lakh
BSE code:	532942
NSE code:	KNRCON
Free float: (No of shares)	13.1 cr

Shareholding (%)

Promoters	53.3
FII	2.3
DII	34.4
Others	10.1

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	22.3	50.2	59.7	165.1
Relative to Sensex	13.6	39.4	44.3	117.1

Sharekhan Research, Bloomberg

Summary

- KNR's board approved asset sale at 1.1x P/B which forms 71% of consolidated debt. Asset sales to be completed by FY2022, thereby significantly deleveraging balance sheet and freeing up equity capital.
- Roads sector forms 27% of government's Rs. 6 lakh-crore national monetisation plan till FY2025. Asset divestment to help improving liquidity in sector & increase project tendering.
- FASTag collections indicate tolling reaching pre-COVID levels. Bank credit deployment to roads maintain double digit y-o-y growth since February 2021 to June 2021.
- We retain a Buy on the stock with a revised PT of Rs. 400 as we believe that a brighter industry outlook and strengthening balance sheet are strong growth levers.

KNR Constructions Limited (KNR) is expected to benefit from the government's continued focus on increasing investments in the road sector and significant deleveraging of its consolidated balance sheet, giving further headroom to improve its already strong order backlog. The company's board approved the sale of three assets (KNR Srirangam Infra, KNR Tirumala and KNR Shankarampet) for which the company had signed share purchase agreements with Cube Highways during 2019. The three assets are valued at 1.1x P/B at an equity value of Rs. 466 crore to be received by the company. The company had only drawn down 51% (Rs. 694 crore) of the total debt of the three projects which forms 71% of the total consolidated debt as on Q1FY2022 end while its standalone balance sheet has a net cash position of Rs. 47 crore. Hence, completion of transfer of these projects would significantly pare down KNR's consolidated balance sheet along with freeing up equity capital which will be utilized for its new HAM projects bagged till date and future hybrid annuity model (HAM) project wins. Further, road sector comprised 27% (Rs. 1.6 lakh crore) of the recently announced Rs. 6 lakh crore National Monetisation plan by the finance minister which will be monetised over four years till FY2025. The government has identified 104 national highways spanning 26,700 kms (~22% of the total national al highways estimated at 1,21,155 kms excluding private BOT projects) which will be monetized by FY2025 under the NMP plan. The asset divestment would reduce NHAI's leverage and increase project tendering in the sector, of which KNR, with a strong balance sheet, is expected to be one of the key beneficiaries. The roads sector saw project awards drop in July 2021 (by 28% y-o-y) after a healthy growth in June 2021 (which saw 12% y-o-y rise in awards at 1018 km). However, construction activities remained strong with road construction during FY2022 till July 2021 rising by 10% y-o-y to 2,927 km. Road project awards is expected to gather pace from as early as next month as per our interaction with industry players, while awarding pipeline for FY2022 remain robust. Further, FASTag issuances reached pre-COVID level in July 2021 (up 21.8% y-o-y and almost similar to March 2021) after a strong rebound in June 2021 (up 35.5% m-o-m and down 18% versus March 2021). Further, bank credit deployment in the roads sector has been rising in double-digits since February 2021 with June 2021 seeing a 28% y-o-y growth. The higher deployment of bank credit to the road sector highlights easing of funding requirements for the sector and would help improve execution of under-construction projects and financial closure of newly-bagged projects. The government's Rs. 111 lakh crore worth of investments envisaged over FY2020-FY2025 entails Rs. 20.3 lakh crore (18% share) investments in the road sector. The company already has a strong order backlog of Rs. 11,679 crore, translating to 4x TTM standalone revenues providing strong revenue visibility in the next two years. Overall, we expect KNR to benefit from a better outlook for the road sector and strengthening KNR's balance sheet. KNR currently trades at a P/E of 17x FY2024E standalone earnings with enough levers of earnings upgrade going ahead. Hence, we maintain our Buy rating on the stock with a revised PT of Rs. 400.

Our Call

Valuation –Retain Buy with a revised price target of Rs. 400: KNR has been able to ramp-up its execution over the past four quarters and also maintained a high OPM. The company had recently upped its revenue guidance for FY2022 if a potential third wave of COVID-19 does not pose challenges. The company's standalone and consolidated balance sheet remain strong. Completion of the Cube Highways deal will further free up equity for future project infusions. A strong order book and healthy bidding pipeline provide comfort. KNR is expected to be one of the key beneficiaries from the government's planned investments in the roads sector up to FY2025. Hence, we maintain our Buy rating on the stock with a revised PT of Rs. 400.

Key risk

Execution delays and a weak macroeconomic environment will lead leading to lull in new project awards.

Valuation (Standalone)

Particulars	Rs cr			
	FY21	FY22E	FY23E	FY24E
Revenue	2,702.6	3,311.9	3,823.9	4,465.0
OPM (%)	19.8	18.9	18.9	19.0
Adjusted PAT	255.4	388.4	462.6	557.1
% YoY growth	8.3	52.0	19.1	20.4
Adjusted EPS (Rs.)	9.1	13.8	16.5	19.8
P/E (x)	36.6	24.1	20.2	16.8
P/B (x)	4.9	4.1	3.4	2.8
EV/EBITDA (x)	16.5	14.1	12.2	10.4
RoNW (%)	14.5	18.9	18.8	18.8
RoCE (%)	15.3	19.6	19.4	19.4

Source: Company; Sharekhan estimates

Company's board approves divestment of three assets at 1.1x P/B: KNR's board approved the sale of three assets (KNR Srirangam Infra, KNR Tirumala and KNR Shankarampet) for which the company had signed share purchase agreements with Cube Highways during 2019. The three assets are valued at 1.1x P/B at an equity value of Rs. 466 crore to be received by the company. The company had only drawn down 51% (Rs. 694 crore) of the total debt of the three projects which forms 71% of the total consolidated debt as on Q1FY2022 end while its standalone balance sheet has a net cash position of Rs. 47 crore. Hence, completion of transfer of these projects would significantly pare down KNR's consolidated balance sheet along with freeing up equity capital which will be utilized for its new HAM projects bagged till date and future hybrid annuity model (HAM) project wins.

Asset sale details

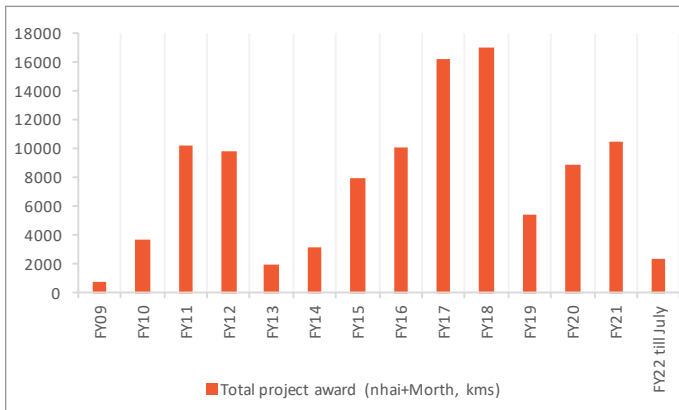
Particulars	Agreement Date	Total Equity (Rs cr)	Turnover (Rs cr)	Net Worth (Rs cr)	Consideration to be received (Rs cr)	P/B Multiple (x)	Expected date of sale completion
KNR Srirangam Infra	28-Jan-19	96	241	98	111	1.1	On or before 31st March 2022
KNR Tirumala Infra	11-Feb-19	143	425	177	218	1.2	On or before 31st Dec 2021
KNR Shankarampet Projects	16-Aug-19	104	368	139	137	1.0	On or before 31st March 2022
Total	-	344	1034	414	466	1.1	-

Source: Company; Sharekhan Research

Road project divestment form 27% of NMP plan: The finance ministry recently announced a Rs. 6 lakh crore National Monetisation Plan (NMP) that seeks to unlock value in infrastructure assets across sector including road, power and railways over four years till FY2025. Road assets worth Rs. 1.6 lakh crore or 27% of the total NMP would be flag bearer of the government's plan. The government has identified 104 national highways spanning 26,700 km (~22% of the total NHs estimated at 1,21,155 excluding private BOT projects) which will be monetized by FY2025 under the NMP. The road ministry would be monetizing the completed NH stretches through Toll Operate Transfer (TOT) and Infrastructure Investment Trust (InvIT) routes. The asset divestment would aid in bringing down the leverage of NHAI and aid in increasing project tendering for the sector.

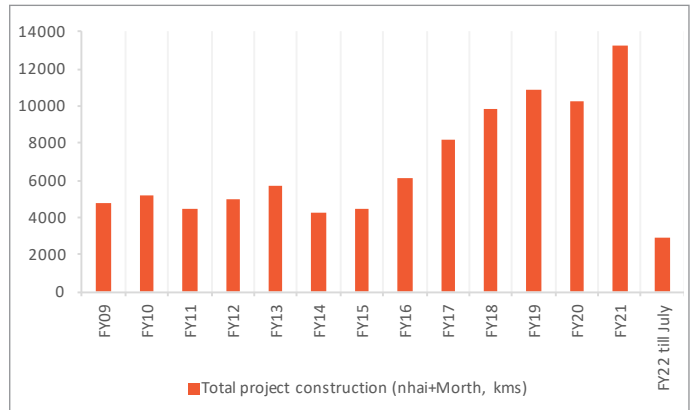
Project tolling reaches pre-COVID levels: The roads sector saw project awards drop in July 2021 (by 28% y-o-y) after a healthy growth in June 2021 (which saw 12% y-o-y rise in awards at 1018 km). However, construction activities remained strong with road construction during FY2022 till July 2021 rising by 10% y-o-y to 2,927 km. Road project awards is expected to gather pace from as early as next month as per our interaction with industry players, while awarding pipeline for FY2022 remain robust. Further, FASTag issuances reached pre-COVID level in July 2021 (up 21.8% y-o-y and almost similar to March 2021) after a strong rebound in June 2021 (up 35.5% m-o-m and down 18% versus March 2021). Further, bank credit deployment in the roads sector has been rising in double-digits since February 2021 with June 2021 seeing a 28% y-o-y growth. The higher deployment of bank credit to the road sector highlights easing of funding requirements for the sector and would help improve execution of under-construction projects and financial closure of newly-bagged projects.

Project Awards (MORTH+NHAI)



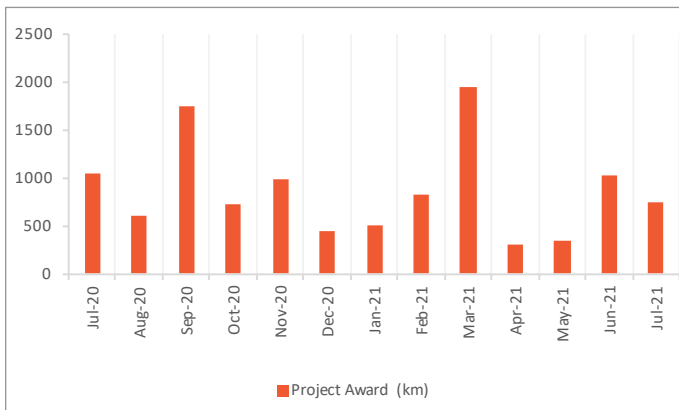
Industry; Sharekhan Research

Project Construction (MORTH+NHAI)



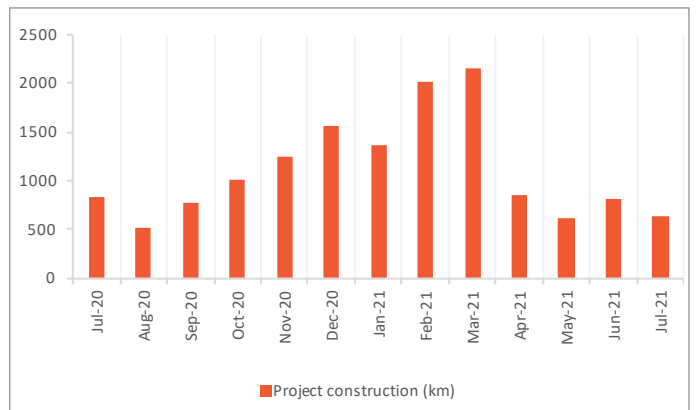
Industry; Sharekhan Research

Project Award Monthly trend



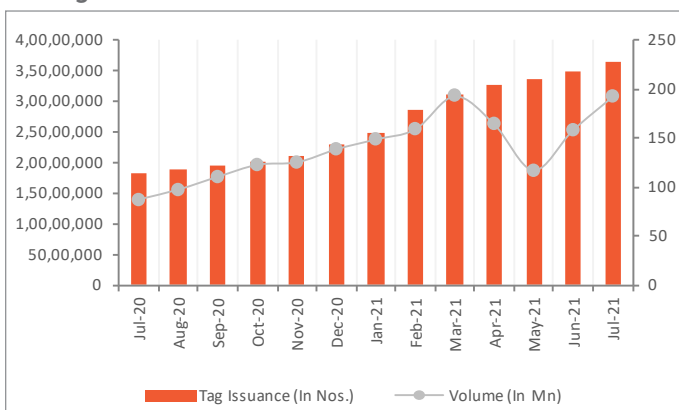
Industry; Sharekhan Research

Project Construction monthly trend



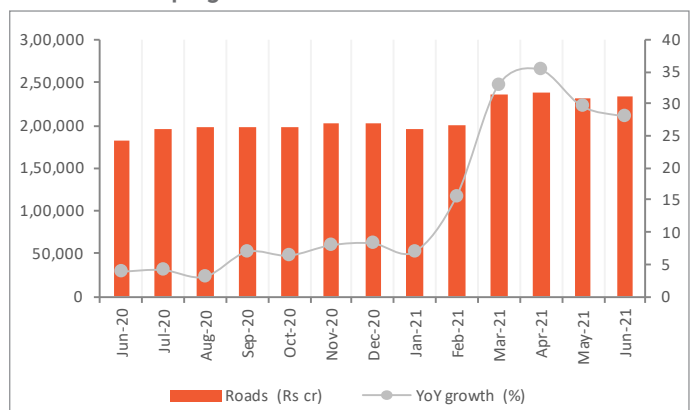
Industry; Sharekhan Research

FASTag trend



Industry; Sharekhan Research

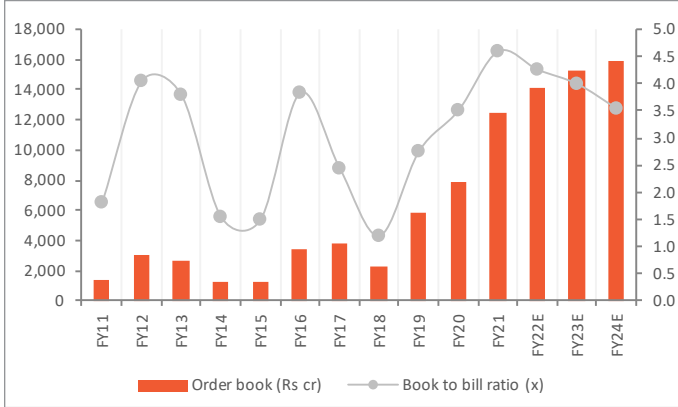
Bank credit deployment in Roads



Industry; Sharekhan Research

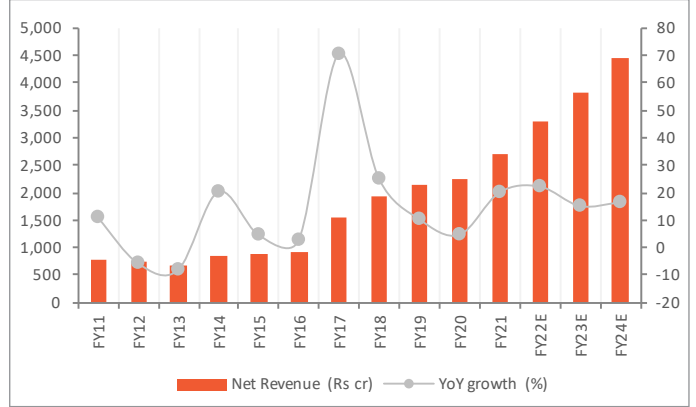
Financials in charts

Order Book trend



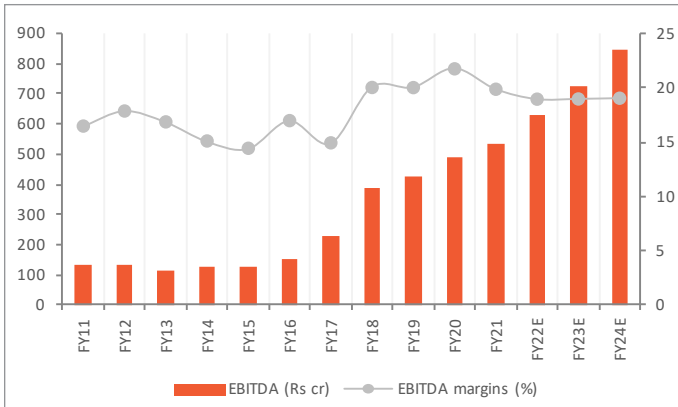
Source: Company, Sharekhan Research

Standalone Revenue trend



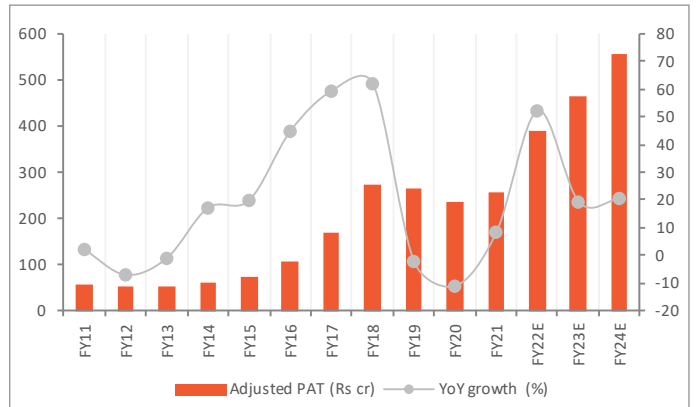
Source: Company, Sharekhan Research

Standalone EBITDA trend



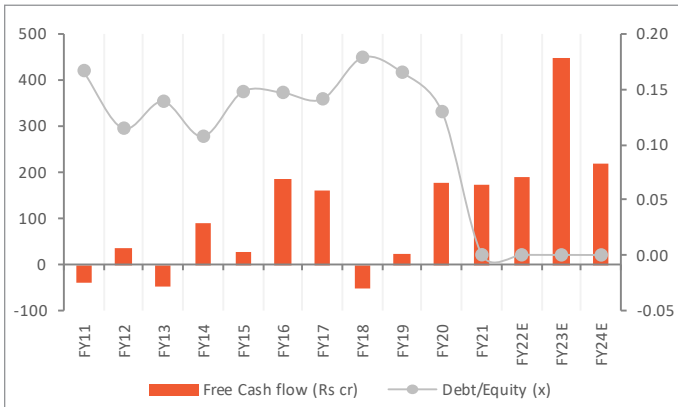
Source: Company, Sharekhan Research

Standalone PAT trend



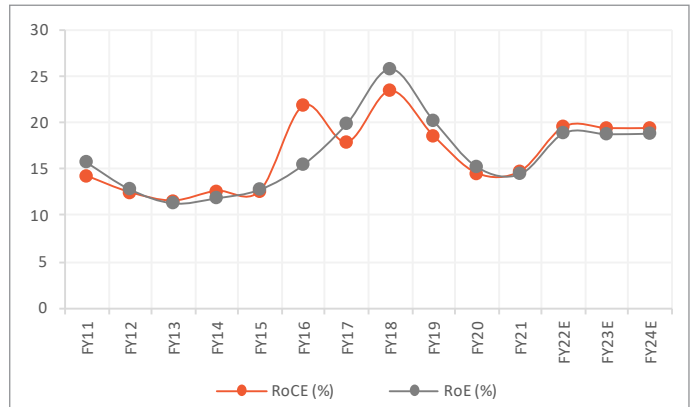
Source: Company, Sharekhan Research

Free Cash Flow and D/E trend



Source: Company, Sharekhan Research

ROCE/ROE trend



Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector View – Roads to remain one of key focus areas in government’s infrastructure spending

The government’s infrastructure investments are pegged at Rs. 111 lakh crore over FY2020 to FY2025. The roads sector is expected to witness Rs. 20 lakh crore investments during the same period. Huge investments and favourable government policies are expected to provide strong growth opportunities for industry players. The road sector is recovering with near pre-COVID level manpower strength and availability of materials post easing of lockdown restrictions. The industry is expected to see strong order inflows and an improvement in execution run-rate from Q3FY2021 onwards. Working capital issues of the companies have been handled by proactive payments from NHAI.

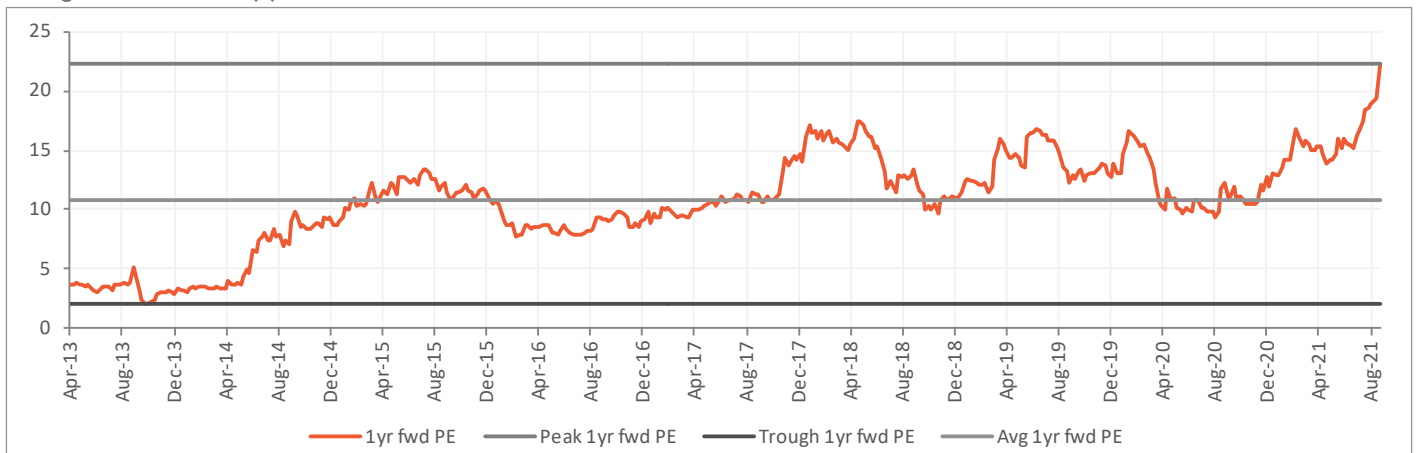
■ Company Outlook – Expect execution and order intake to improve

The management is eyeing revenues of over Rs. 3,400 crore in FY2022 assuming a third wave of COVID-19 does not pose challenges on execution. The operating margins are expected to continue at 17-18% range in the near future. Further, the management conservatively guided for order intake of Rs. 2000-3000 crore for FY2022. The company has a strong order backlog at 4x TTM standalone revenues providing strong revenue visibility over next two years. Standalone and consolidated balance sheet continue to remain strong. The conclusion of Cube Highways deal will further free up equity for future projects infusions. A strong order book and healthy bidding pipeline provide comfort.

■ Valuation – Retain Buy with a price target of Rs. 400

KNR has been able to ramp-up its execution over the past four quarters and also maintained a high OPM. The company had recently upped its revenue guidance for FY2022 if a potential third wave of COVID-19 does not pose challenges. The company’s standalone and consolidated balance sheet remain strong. Completion of the Cube Highways deal will further free up equity for future project infusions. A strong order book and healthy bidding pipeline provide comfort. KNR is expected to be one of the key beneficiaries from the government’s planned investments in the roads sector up to FY2025. Hence, we maintain our Buy rating on the stock with a revised PT of Rs. 400.

One-year forward P/E (x) band



Source: Sharekhan Research

Peer Comparison

Particulars	P/E (x)		EV/EBITDA (x)		P/BV (x)		RoE (%)	
	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E
PNC Infratech	15.0	13.2	8.4	7.5	2.1	1.8	15.0	14.7
KNR Constructions	20.2	16.8	12.2	10.4	3.4	2.8	18.8	18.8

Source: Sharekhan Research

About company

Incorporated in 1995, KNR has over two decades of experience in project execution. The company is one of the leading companies providing engineering, procurement and construction (EPC) services, majorly concentrated in the roads and highways segment. The company also has a minor presence in the irrigation and urban water infrastructure management segments. Till date, KNR has successfully executed more than 6,000 lane km of road projects across 12 states in India.

Investment theme

KNR is one of the best managed road construction companies with more than two decades of experience executing over 6,000 lane km road projects across 12 states in India. KNR has in-house construction capabilities, which ensure on-schedule project completion (history of receiving early completion bonuses). KNR entered into a complete stake sale agreement with Cube Highways for four of its hybrid annuity projects, which will aid in lower equity requirement along with booking of EPC work with possibility of receiving an early completion bonus.

Key Risks

- ◆ Delay in project execution of hybrid annuity projects.
- ◆ Slowdown in the macroeconomy leading to muted road project awards from NHAI and Ministry of Road Transport.

Additional Data

Key management personnel

Mr. K. Narasimha Reddy	Founder Promoter & Managing Director
Mr. K. Jalandhar Reddy	Promoter & Executive Director
Mr. M.V. Venkata Rao	Company Secretary & Compliance Officer

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Reddy Kamidi Narasimha	32.53
2	Reddy Kamidi Jalandhar	13.96
3	ICICI Prudential Asset Management	7.38
4	DSP Investment Managers Pvt Ltd	6.85
5	HDFC Asset Management Co Ltd	6.4
6	YASHODA KAMIDI	4.27
7	Reddy Mereddy Rajesh	4.27
8	UTI Asset Management Co Ltd	2.21
9	Franklin Resources Inc	2
10	Invesco Asset Management India Pvt	1.91

Source: Bloomberg (Old data)

Sharekhan Limited, its analyst or dependant(s) of the analyst might be holding or having a position in the companies mentioned in the article.