

INDUSTRY INFRASTRUCTURE

CMP (as on 31 May 2018) Rs 298

Target Price Rs 364

Nifty 10,736

Sensex 35,322

KEY STOCK DATA

Bloomberg KNRC IN

No. of Shares (mn) 141

MCap (Rs bn) / (\$ mn) 41/612

6m avg traded value (Rs mn) 78

STOCK PERFORMANCE (%)

52 Week high / low Rs 349/193

3M 6M 12M

Absolute (%) (4.8) 6.7 46.1

Relative (%) (8.1) 0.1 32.6

SHAREHOLDING PATTERN (%)

Promoters 55.38

FIs & Local MFs 28.08

FPIs 3.78

Public & Others 12.76

Source : BSE

Parikshit D Kandpal

parikshitd.kandpal@hdfcsec.com

+91-22-6171-7317

Kunal Bhandari

kunal.bhandari@hdfcsec.com

+91-22-6639-3035

A steady ship

KNRC continues to outperform its growth guidance and delivered strong 4QFY18 revenue at Rs 6.2bn which was 25.9% above estimates. Revenue for FY18 came in at Rs 19.3bn (+25.3% YoY). EBITDA margin for FY18 was 20.0% on account of cost reversals in several near completion projects. We estimate sustainable margins to be around 15-16% after considering contribution from HAM projects.

Order book is now at Rs 63.0bn including Rs 39.8bn EPC works of the 5 HAM projects it won in 4QFY18. KNRC is now focusing on completing financial closure. It has guided for ~25.0bn for inflows in FY19. Bidding will only be on the EPC front as KNR takes a breather from further HAM tenders.

KNRC has delivered industry beating return ratios in the past. We believe it is set on a steady growth path with strong growth visibility, minimal leverage, lean WC cycle, a prudent bidding strategy and a good corporate governance track record. We continue to maintain **BUY with SOTP of Rs 364/sh.**

Financial Summary (Standalone)

Year Ending March (Rs mn)	4QFY18	4QFY17	YoY (%)	3QFY18	QoQ (%)	FY17	FY18	FY19E	FY20E
Net Sales	6,244	4,821	29.5	4,332	44.1	15,411	19,317	23,200	27,572
EBITDA	1,207	722	67.1	984	22.7	2,296	3,861	3,622	4,307
APAT	797	524	52.0	658	21.1	1,432	1,917	1,617	1,944
Diluted EPS (Rs)	5.7	3.7	52.0	4.7	21.1	10.2	13.6	11.5	13.8
P/E (x)						30.0	22.4	26.5	22.1
EV / EBITDA (x)						19.1	11.6	12.1	10.1
RoE (%)						17.5	18.7	12.8	13.2

Source: Company, HDFC sec Inst Research

Highlights of the quarter

- **Funding options being explored:** 4 HAM projects are close to FC with a draft agreed with the bankers and 1 project has received LOA only recently. With ~Rs 4.4bn of Equity requirement over the next 2.5 years, KNRC is exploring options to get in a partner. Currently due diligence is ongoing and KNRC open to options like 50% equity infusion or a hive off post EPC (COD + 2years). Communication on this front is likely in a month.
- **Balance Sheet remains strong:** NWC remains comfortable at 42days (one of the best vs EPC peers). KNRC's gross debt is Rs 2.2bn, of which a large chunk is the promoter's loan at Rs 2.1bn. Both the Muzaffarpur and the Walayar BOT projects are each clocking ~Rs 1.6mn/ day collections. Monetization of assets will further free up capital. With planned capex of ~1.2bn not very significant we expect KNRC to generate healthy FCFF over FY19-20E.
- **Near-term outlook:** We expect KNR to clock a 19.5% revenue CAGR over FY18-20E as HAM projects will start contributing in 2HFY19E and expect it to continue to demonstrate high core return ratios >30%.

KNRC 4QFY18 net revenues were 25% above estimates at Rs 6.2bn (+29.5% YoY, +44.1% QoQ)

EBITDA at Rs 1.2bn (+67.1% YoY, +22.7% QoQ) was 24.8% above our estimates, with EBITDA margins expanding to 19.3%(+435bps YoY, -338bps QoQ)

APAT came at Rs 0.8bn (+52.0% YoY, +21.1% QoQ), 76.5% ahead of our estimates due to other income increasing to Rs 0.2bn (+1,768.5% YoY, 200% QoQ). Interest Costs increased to Rs 88mn (-26.2%YoY)

Standalone Quarterly Financial

Particulars (Rs mn)	4QFY18	4QFY17	YoY (%)	3QFY18	QoQ (%)	FY18	FY17	YoY (%)
Net Sales	6,244	4,821	29.5	4,332	44.1	19,317	15,411	25.3
Material Expenses	(4,121)	(3,486)	18.2	(2,782)	48.1	(12,854)	(11,145)	15.3
Employee Expenses	(200)	(146)	37.4	(181)	10.5	(721)	(552)	30.6
Other Operating Expenses	(716)	(468)	53.1	(385)	86.0	(1,880)	(1,417)	32.7
EBITDA	1,207	722	67.1	984	22.7	3,861	2,297	68.1
Interest Cost	(88)	(54)	62.3	(49)	79.6	(231)	(219)	5.5
Depreciation	(491)	(195)	152.0	(371)	32.3	(1,341)	(639)	109.9
Other Income (Incl. EO Items)	183	10	1,768.5	61	200.0	393	194	102.6
PBT	811	483	67.9	625	29.8	2,682	1,633	64.2
Tax	(14)	41	(133.8)	33	(142.4)	39	(60)	(165.0)
RPAT	797	524	52.0	658	21.1	2,721	1,573	73.0
E/o (adj for tax)	-	-	-	-	-	-	109	-
APAT	797	524	52.0	658	21.1	2,721	1,682	61.8

Source: Company, HDFC sec Inst Research

Margin Analysis

MARGIN ANALYSIS	4QFY18	4QFY17	YoY (bps)	3QFY18	QoQ (bps)	FY18	FY17	YoY (bps)
Material Expenses % Net Sales	66.0	72.3	(630)	64.2	178	66.5	72.3	(577)
Employee Expenses % Net Sales	3.2	3.0	18	4.2	(98)	3.7	3.6	15
Other Operating Expenses % Net Sales	11.5	9.7	177	8.9	258	9.7	9.2	54
EBITDA Margin (%)	19.3	15.0	435	22.7	(338)	20.0	14.9	508
Tax Rate (%)	1.7	(8.6)	1,029	(5.3)	701	(1.5)	3.7	(513)
APAT Margin (%)	12.8	10.9	189	15.2	(243)	14.1	10.2	388

Source: Company, HDFC sec Inst Research

We expect steady inflows to keep the order book at comfortable levels

FY18-20E revenue CAGR 26.0%

Tax rate to increase as projects with tax exemption achieve completion

The reported PAT includes impact of MAT credit. We have adjusted this to arrive at normalized PAT

KNR to generate strong FCF

Key Assumptions And Estimates

STANDALONE (Rs mn)	FY19E	FY20E	Comments
Closing order book	64,816	67,244	We expect steady inflows to keep the order book at comfortable levels
Order book growth (%)	2.9	3.7	
New order booking	25,000	30,000	
Book to bill ratio	2.8	2.4	Book to bill ratio to remain steady
Total Revenue	23,200	27,572	FY18-20E Revenue CAGR of 19.5%
Growth (%)	20.1	18.8	
EBIDTA	3,622	4,307	
EBIDTA margin (%)	15.6	15.6	Margins to decline from FY19E as KNRC has written back some excess provision in projects nearing completion during FY18
Depreciation	1,288	1,456	
Financial Charges	311	368	Borrowing cost to remain relatively stable as debt is not likely to expand significantly
PBT	2,311	2,777	
PBT margin (%)	10.0	10.1	
Tax	346.6	555.4	
Tax rate (%)	15.0	20.0	Tax rate to increase as projects with tax exemption achieve completion
RPAT	1,964	2,222	
Net margin (%)	8.5	8.1	Margins to remain muted
Extraordinary	(346.6)	(277.7)	To reflect MAT rate we taken additional provisioning. KNRC numbers will be reflected in RPAT
Adjusted PAT	1,617	1,944	
Gross Block Turnover	2.5	2.7	Improvement on account of new orders inflow
Debtor days	45	45	
CFO - a	3,768	3,224	Higher revenue growth, robust client advance to result in higher positive cash flow from operations
CFI - b	(2,473)	(2,406)	Investments in Gross block and HAM projects
FCF - a+b	1,295	818	KNR to generate strong FCF
CFF - c	(297)	(452)	
Total change in cash - a+b+c	998	366	

Source: HDFC sec Inst Research

We value standalone EPC business at Rs 303/share (10x one year forward EV/EBITDA)

Kerala BOT at Rs 28/share (at 1x P/BV of equity invested)

Muzaffarpur Barauni BOT at Rs 5/share (at 1x P/BV of equity invested)

Real estate at Rs 5/share (at 1x P/BV of amount invested)

HAM Projects investment at 23/share (at 1x book value of investments)

Our SOTP target price is Rs 364/share

Outlook and valuation

Maintain BUY – TP of Rs 364/sh

Valuation methodology

- We have valued KNRC's EPC business at 10x one year forward EV/EBITDA. Our rationale behind this is (1) Strong order backlog of ~Rs 63bn (3.3x FY18 revenue), (2) Robust balance sheet net D/E of 0.1x in addition to BOT monetization plans, (3) Superior earnings quality vs. similar-sized peers makes a case for valuation premium and (4) Tremendous opportunity in HAM projects in the Southern states in the near future.
- KNR's promoter's share of debt is Rs 2,110mn of the standalone debt of Rs 2,200mn. Adjusted for promoters' loans standalone is a net cash company. This gives us comfort on gearing. Apart from that, improvement in the working capital cycle (driven by 10% mobilisation advances on NHAI road EPC orders) will keep debt under check.
- Investments in the road sector will continue to drive stock performance. KNRC, with its strong execution skills, is likely to benefit from the pick-up in order activity.
- We value the (1) Standalone EPC business at Rs 303/share (10x Mar-20 EV/EBITDA), (2) Kerala BOT at Rs 28/share (at 1x P/BV of equity invested), (3) Muzaffarpur Barauni BOT at Rs 5/share (at 1x P/BV of equity invested), (4) Real estate at Rs 5/share (at 1x P/BV of amount invested) and (5) HAM Projects investment at 23/share (at 1x book value of investments).

SOTP Valuation

Particulars	Segments	Value (Rs mn)	Value per share (Rs)	Rationale
KNR Standalone	Core construction business	42,584	303	At 10x Mar-20 EV/EBITDA
Kerala BOT	Roads toll	3,974	28	At 0.8x P/BV(x) of invested equity
Muzaffarpur Barauni BOT	Roads toll	694	5	At 1x P/BV(x) of invested equity
Real Estate	Land on Book	718	5	At book value in balance sheet
HAM Projects investment	Roads BOT	3,200	23	Expected investment over next 3yrs at book value in balance sheet.
Total		47,252	364	

Source: HDFC sec Inst

Income Statement (Standalone)

Year ending March (Rs mn)	FY16	FY17	FY18	FY19E	FY20E
Net Revenues (post JV partner share)	9,025	15,411	19,317	23,200	27,572
Growth (%)	2.1	70.7	25.3	20.1	18.8
Material Expenses	6,805	12,281	12,854	17,935	21,451
Employee Expenses	431	552	721	879	1,048
Other Operating Expenses	260	281	1,880	764	827
EBIDTA	1,529	2,296	3,861	3,622	4,307
EBIDTA (%)	16.9	14.9	20.0	15.6	15.6
EBIDTA Growth (%)	13.8	50.1	68.2	(6.2)	18.9
Depreciation	423	639	1,341	1,288	1,456
EBIT	1,106	1,657	2,520	2,334	2,851
Other Income (Incl. EO Items)	317	194	393	288	294
Interest	132	219	231	311	368
PBT	1,291	1,632	2,682	2,311	2,777
Tax	(319)	60	- 39	347	555
RPAT	1,611	1,573	2,721	1,964	2,222
EO items (net of tax)	(165)	(141)	(805)	(347)	(278)
APAT	1,445	1,432	1,917	1,617	1,944
APAT Growth (%)	97.9	(0.9)	33.9	(15.6)	20.2
EPS	10.3	10.2	13.6	11.5	13.8
EPS Growth (%)	97.9	(0.9)	33.9	(15.6)	20.2

Source: Company, HDFC sec Inst Research

Balance Sheet (Standalone)

As at March (Rs mn)	FY16	FY17	FY18	FY19E	FY20E
SOURCES OF FUNDS					
Share Capital	281	281	281	281	281
Reserves	7,096	8,674	11,297	13,429	15,566
Total Shareholders Funds	7,377	8,955	11,578	13,710	15,847
Long Term Debt	1,125	1,303	2,118	2,299	2,299
Short Term Debt	-	-	82	-	-
Total Debt	1,125	1,303	2,200	2,299	2,299
Deferred Taxes	(374)	(432)	(1,408)	(432)	(432)
Other Non Current Liabilities	325	314	284	314	314
TOTAL SOURCES OF FUNDS	8,453	10,140	12,654	15,891	18,029
APPLICATION OF FUNDS					
Net Block	1,762	2,607	3,316	3,511	3,254
CWIP	59	15	0	15	15
Investments, LT Loans & Advances	3,363	4,663	5,100	6,363	7,863
Other Non Current Assets	1,663	1,850	1,561	1,973	2,109
Total Non-current Assets	6,848	9,135	9,977	11,862	13,241
Inventories	353	574	712	939	1,132
Debtors	1,294	1,640	2,320	2,860	3,407
Cash & Equivalents	161	246	439	1,438	1,803
ST Loans & Advances, Others	3,555	4,153	4,801	5,907	6,904
Total Current Assets	5,364	6,612	8,272	11,143	13,246
Creditors	1,038	1,344	2,102	2,536	3,022
Other Current Liabilities & Provns	2,721	4,263	3,493	4,578	5,438
Total Current Liabilities	3,759	5,607	5,595	7,114	8,459
Net Current Assets	1,605	1,005	2,677	4,029	4,786
TOTAL APPLICATION OF FUNDS	8,454	10,140	12,655	15,891	18,028

Source: Company, HDFC sec Inst Research

Cash Flow (Standalone)

Year ending March (Rs mn)	FY16	FY17	FY18P	FY19E	FY20E
PBT	1,291	1,632	2,682	2,311	2,777
Non-operating & EO items	(86)	20	(393)	(288)	(294)
Interest expenses	132	219	231	311	368
Depreciation	423	639	1,341	1,288	1,456
Working Capital Change	830	730	(2,197)	492	(528)
Tax paid	(56)	(75)	39	(347)	(555)
OPERATING CASH FLOW (a)	2,534	3,165	1,703	3,768	3,224
Capex	(595)	(1,383)	(2,035)	(1,498)	(1,200)
Free cash flow (FCF)	1,939	1,782	(332)	2,269	2,024
Investments	(1,944)	(1,750)	(437)	(1,263)	(1,500)
Other non operating income	-	-	393	288	294
INVESTING CASH FLOW (b)	(2,538)	(3,133)	(2,079)	(2,473)	(2,406)
Share capital Issuance	-	-	-	-	-
Debt Issuance	204	273	897	99	-
Interest expenses	(128)	(220)	(231)	(311)	(368)
Dividend	(68)	-	(97)	(84)	(84)
Others	-	-	-	-	-
FINANCING CASH FLOW (c)	9	53	569	(297)	(452)
NET CASH FLOW (a+b+c)	4	85	193	998	366
Opening cash balance	157	161	246	439	1,438
Closing Cash & Equivalents	161	246	439	1,438	1,803

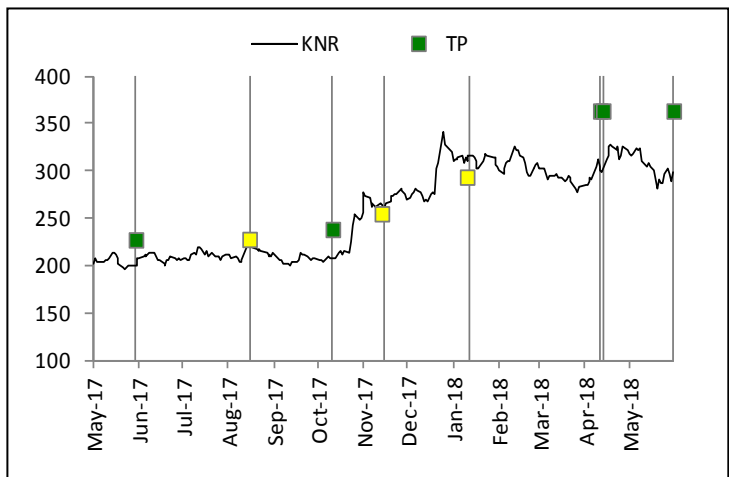
Source: Company, HDFC sec Inst Research

Key Ratios (Standalone)

	FY16	FY17	FY18	FY19E	FY20E
PROFITABILITY (%)					
GPM	24.6	20.3	33.5	22.7	22.2
EBITDA Margin	16.9	14.9	20.0	15.6	15.6
EBIT Margin	12.3	10.8	13.0	10.1	10.3
APAT Margin	16.0	9.3	9.9	7.0	7.1
RoE	22.1	17.5	18.7	12.8	13.2
Core RoCE	28.0	30.5	35.9	24.5	27.3
RoCE	19.0	16.2	17.0	11.8	12.4
EFFICIENCY					
Tax Rate (%)	(24.7)	3.7	(1.5)	15.0	20.0
Asset Turnover (x)	1.8	2.4	2.2	2.4	2.5
Inventory (days)	14	14	13	15	15
Debtors (days)	52	39	44	45	45
Payables (days)	42	32	40	40	40
Cash Conversion Cycle (days)	25	21	18	20	20
Other Current Assets (days)	144	98	91	93	91
Other Current Liab (days)	110	101	66	72	72
Net Working Capital Cycle (Days)	58	18	42	41	39
Debt/EBITDA (x)	0.7	0.6	0.6	0.6	0.5
Net D/E	0.13	0.12	0.2	0.1	0.0
Interest Coverage	8.4	7.6	10.9	7.5	7.8
PER SHARE DATA					
EPS (Rs/sh)	10.3	10.2	13.6	11.5	13.8
CEPS (Rs/sh)	13.3	14.7	23.2	20.7	24.2
DPS (Rs/sh)	0.4	0.0	0.6	0.5	0.5
BV (Rs/sh)	52	64	82	97	113
VALUATION					
P/E	29.7	30.0	22.4	26.5	22.1
P/BV	5.8	4.8	3.7	3.1	2.7
EV/EBITDA	28.7	19.1	11.6	12.1	10.1
OCF/EV (%)	5.8	0.1	0.0	0.1	0.1
FCF/EV (%)	4.4	4.1	(0.7)	5.2	4.7
FCFE/Market Cap (%)	4.7	4.3	0.8	4.8	3.9
Dividend Yield (%)	0.1	0.0	0.2	0.2	0.2

Source: Company, HDFC sec Inst Research

RECOMMENDATION HISTORY



Date	CMP	Reco	Target
30-May-17	202	BUY	228
17-Aug-17	221	NEU	228
11-Oct-17	209	BUY	239
15-Nov-17	255	NEU	255
12-Jan-18	314	NEU	293
12-Apr-18	300	BUY	364
14-Apr-18	298	BUY	364
31-May-18	298	BUY	364

Rating Definitions

BUY : Where the stock is expected to deliver more than 10% returns over the next 12 month period
NEUTRAL : Where the stock is expected to deliver (-)10% to 10% returns over the next 12 month period
SELL : Where the stock is expected to deliver less than (-)10% returns over the next 12 month period

INSTITUTIONAL RESEARCH
Disclosure:

We, **Parikshit Kandpal, MBA**, and **Kunal Bhandari, CA**, authors and the names subscribed to this report, hereby certify that all of the views expressed in this research report accurately reflect our views about the subject issuer(s) or securities. HSL has no material adverse disciplinary history as on the date of publication of this report. We also certify that no part of our compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report.

Research Analyst or his/her relative or HDFC Securities Ltd. **does not have** any financial interest in the subject company. Also Research Analyst or his relative or HDFC Securities Ltd. or its Associate may have beneficial ownership of 1% or more in the subject company at the end of the month immediately preceding the date of publication of the Research Report. Further Research Analyst or his relative or HDFC Securities Ltd. or its associate **does not have** any material conflict of interest.

Any holding in stock –No

HDFC Securities Limited (HSL) is a SEBI Registered Research Analyst having registration no. INH000002475.

Disclaimer:

This report has been prepared by HDFC Securities Ltd and is meant for sole use by the recipient and not for circulation. The information and opinions contained herein have been compiled or arrived at, based upon information obtained in good faith from sources believed to be reliable. Such information has not been independently verified and no guaranty, representation of warranty, express or implied, is made as to its accuracy, completeness or correctness. All such information and opinions are subject to change without notice. This document is for information purposes only. Descriptions of any company or companies or their securities mentioned herein are not intended to be complete and this document is not, and should not be construed as an offer or solicitation of an offer, to buy or sell any securities or other financial instruments. This report is not directed to, or intended for display, downloading, printing, reproducing or for distribution to or use by, any person or entity who is a citizen or resident or located in any locality, state, country or other jurisdiction where such distribution, publication, reproduction, availability or use would be contrary to law or regulation or what would subject HSL or its affiliates to any registration or licensing requirement within such jurisdiction.

If this report is inadvertently sent or has reached any individual in such country, especially, USA, the same may be ignored and brought to the attention of the sender. This document may not be reproduced, distributed or published for any purposes without prior written approval of HSL.

Foreign currencies denominated securities, wherever mentioned, are subject to exchange rate fluctuations, which could have an adverse effect on their value or price, or the income derived from them. In addition, investors in securities such as ADRs, the values of which are influenced by foreign currencies effectively assume currency risk.

It should not be considered to be taken as an offer to sell or a solicitation to buy any security. HSL may from time to time solicit from, or perform broking, or other services for, any company mentioned in this mail and/or its attachments.

HSL and its affiliated company(ies), their directors and employees may; (a) from time to time, have a long or short position in, and buy or sell the securities of the company(ies) mentioned herein or (b) be engaged in any other transaction involving such securities and earn brokerage or other compensation or act as a market maker in the financial instruments of the company(ies) discussed herein or act as an advisor or lender/borrower to such company(ies) or may have any other potential conflict of interests with respect to any recommendation and other related information and opinions.

HSL, its directors, analysts or employees do not take any responsibility, financial or otherwise, of the losses or the damages sustained due to the investments made or any action taken on basis of this report, including but not restricted to, fluctuation in the prices of shares and bonds, changes in the currency rates, diminution in the NAVs, reduction in the dividend or income, etc.

HSL and other group companies, its directors, associates, employees may have various positions in any of the stocks, securities and financial instruments dealt in the report, or may make sell or purchase or other deals in these securities from time to time or may deal in other securities of the companies / organizations described in this report.

HSL or its associates might have managed or co-managed public offering of securities for the subject company or might have been mandated by the subject company for any other assignment in the past twelve months.

HSL or its associates might have received any compensation from the companies mentioned in the report during the period preceding twelve months from the date of this report for services in respect of managing or co-managing public offerings, corporate finance, investment banking or merchant banking, brokerage services or other advisory service in a merger or specific transaction in the normal course of business.

HSL or its analysts did not receive any compensation or other benefits from the companies mentioned in the report or third party in connection with preparation of the research report. Accordingly, neither HSL nor Research Analysts have any material conflict of interest at the time of publication of this report. Compensation of our Research Analysts is not based on any specific merchant banking, investment banking or brokerage service transactions. HSL may have issued other reports that are inconsistent with and reach different conclusion from the information presented in this report.

Research entity has not been engaged in market making activity for the subject company. Research analyst has not served as an officer, director or employee of the subject company. We have not received any compensation/benefits from the subject company or third party in connection with the Research Report.

HDFC securities Limited, I Think Techno Campus, Building - B, "Alpha", Office Floor 8, Near Kanjurmarg Station, Opp. Crompton Greaves, Kanjurmarg (East), Mumbai 400 042 Phone: (022) 3075 3400 Fax: (022) 2496 5066

Compliance Officer: Binkle R. Oza Email: complianceofficer@hdfcsec.com Phone: (022) 3045 3600

HDFC Securities Limited, SEBI Reg. No.: NSE-INB/F/E 231109431, BSE-INB/F 011109437, AMFI Reg. No. ARN: 13549, PFRDA Reg. No. POP: 04102015, IRDA Corporate Agent License No.: HDF 2806925/HDF C000222657, SEBI Research Analyst Reg. No.: INH000002475, CIN - U67120MH2000PLC152193

Mutual Funds Investments are subject to market risk. Please read the offer and scheme related documents carefully before investing.

