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Q4FY20 result review and
reco change

Capital Goods

Target price: Rs260

Earnings revision

(%)	FY21E	FY22E
Sales	↑ 10.7	↑ 8.5
EBITDA	↑ 26.4	↑ 17.7
EPS	↑ 41.2	↑ 26.1

Target price revision

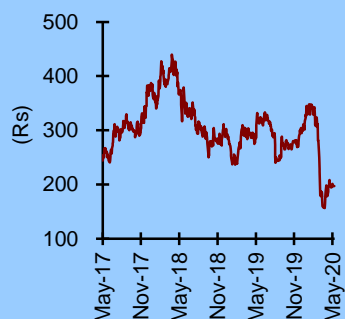
Rs260 from Rs199

Shareholding pattern

	Sep '19	Dec '19	Mar '20
Promoters	51.6	51.6	51.7
Institutional investors	34.7	35.4	36.1
MFs and other	23.8	23.5	22.9
F s/Banks	0.1	0.1	0.0
Insurance	3.2	3.6	3.8
FIs	7.6	8.2	9.4
Others	13.7	13.0	12.2

Source: NSE

Price chart



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INDIA

ICICI Securities

KEC International

BUY

Upgrade from HOLD

Rs197

Healthy margins, strong order prospects

Led by 39% growth in revenues from overseas subsidiary SAE Towers and 36% growth under railways, KEC reported better than expected execution in Q4FY20 at Rs36.7bn. Lockdown-related headwinds are likely to hit H1FY21E execution while migrant labour exodus will increase costs. However, reduction in commodity prices is likely to offset the higher labour costs and thereby limit any major impact on overall margins. Order prospects continue to be strong in SAARC region, Middle East and the domestic market despite an unfavourable environment. Factoring-in the better than expected execution and margins in Q4FY20, we raise FY21E/FY22E earnings by 41% and 26% respectively. Upgrade to BUY (from *Hold*) with a revised target price of Rs260 (previously: Rs199).

- **Strong execution under SAE Towers (SAE) and railways limits major drop in revenues:** SAE witnessed 39% revenue growth to Rs4.4bn due to bunching up of previous orders. Railways segment also witnessed strong growth of 36% YoY to Rs8.6bn in Q4FY20. SAE revenues are likely to reduce in FY21E due to currency devaluation and weak orderbook while business from railways remains promising in H2FY21E.
- **Working capital stress to ease out and support cashflows:** Due to lockdown, there have been slippages in collection to the tune of ~Rs3bn in March, which has been liquidated in April. Focus continues to be on reduction in working capital and, with overall reduction in exposure towards Saudi Arabia, we believe cashflows are likely to improve going forward.
- **Healthy order prospects in both domestic and overseas markets:** Around 35 schemes have recently been tendered by PGCIL (25 in transmission, 12 in substations) worth Rs200bn-250bn, which are expected to be finalised by June/July. Selective activity from other SEBs and TCB is likely to add up to an opportunity of ~Rs350bn-400bn from the domestic market in FY21E. There are prospects of bidding for a total of ~Rs50bn from Oman, UAE and Saudi Arabia and ~Rs60bn from Nepal and Bangladesh.
- **Debt reduction and borrowing mix led to improvement in interest cost:** KEC's net debt as at Q4FY20-end stood at Rs19bn (Rs1.5bn lower than Q2FY20-end). Shift in international borrowing mix (from 40% to 55%) led to decrease in interest cost to 1.8% in Q4FY20 vs 2.2% in Q4FY19. For FY21, the management expects further improvement of 25-30bps in interest cost as percentage of sales, from 2.6% in FY20.
- **Upgrade to BUY on strong execution and healthy order prospects:** Factoring-in the strong order prospects and better than expected margins, we raise our FY21E/FY22E earnings by 41%/26%. Upgrade the stock to **BUY** (from *Hold*) with a revised target price of Rs260 (Rs199 previously).

Market Cap	Rs50.6bn/US\$670mn
Reuters/Bloomberg	KECL BO/KECI IN
Shares Outstanding (mn)	257.1
52-week Range (Rs)	358/154
Free Float (%)	48.3
FII (%)	9.4
Daily Volume (US\$'000)	1,488
Absolute Return 3m (%)	(37.8)
Absolute Return 12m (%)	(41.9)
Sensex Return 3m (%)	(15.3)
Sensex Return 12m (%)	(18.4)

Year to March	FY19	FY20	FY21E	FY22E
Revenue (Rs mn)	1,10,005	1,19,654	1,25,297	1,35,227
Adjusted NI (Rs mn)	4,864	5,655	5,555	6,068
DEPS (Rs)	18.9	22.0	21.6	23.6
% Chg YoY	6.1	16.3	(1.8)	9.2
P/E (x)	10.3	8.9	9.0	8.3
CEPS (Rs)	23.5	27.7	27.4	29.4
EV/E (x)	5.6	5.6	5.5	5.0
Dividend Yield	1.4	1.7	1.8	1.8
RoCE (%)	16.4	16.0	14.4	14.3
RoE (%)	20.0	20.2	17.0	16.1

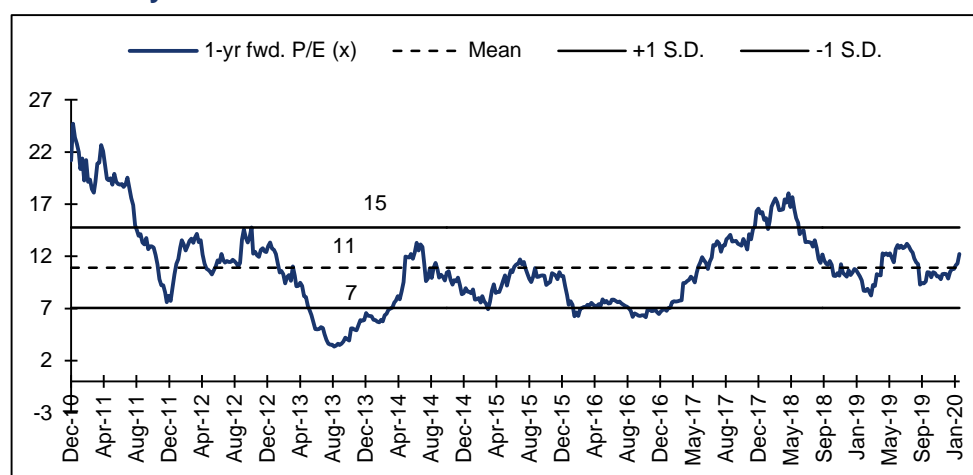
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Valuation and outlook

The stock is currently trading at 9x FY21E earnings. We believe, the company's healthy orderbook, stable traction from railways and focus on debt reduction will support an earnings CAGR of 3.6% during FY20-FY22E. However, given the challenges in working capital, execution and order intake due to Covid-19, we marginally cut our target valuation multiple to 12x from 13x 1-year forward earnings.

KEC is better placed vs peers and the competitive intensity from unorganised sector is likely to reduce due to Covid-19 slowdown. Given the company's focus on cashflow improvement and earnings growth, we upgrade the stock to **BUY** (from **Hold**) with the target price raised to Rs260 (previously: Rs199).

Chart 1: 1-year forward P/E chart



Source: Bloomberg, I-Sec research

Table 1: Earnings revision (consolidated)

(Rs mn)

Rs mn	FY21E			FY22E		
	Earlier	Revised	YoY (%)	Earlier	Revised	YoY (%)
Revenue	1,13,226	1,25,297	10.7	1,24,655	1,35,227	8.5
EBIDTA	9,603	12,134	26.4	11,135	13,110	17.7
PAT	3,934	5,555	41.2	4,812	6,068	26.1

Source: Company data, I-Sec research

Concall highlights

- Lost revenues to the tune of Rs5bn-6bn due to Covid-19 are expected to move Q1FY21.
- 85% of the total sites are currently active.
- Management expects migrant labour exodus to increase the proportion of local labour, high productivity, and increase mechanisation at project sites.
- Company is L1 in Rs40bn worth orders, of which Rs20bn are in international T&D (Rs9bn from the Middle East).
- Management expects T&D contribution to be higher in FY21 vs FY20 given Rs350bn-400bn domestic T&D pipeline for FY21
- KECI has placed 30-35 TBCB bids (25 in transmission, 12 in substations) for PGCIL tenders worth Rs200-250bn (mostly in Rajasthan) and expects to book these projects by July-end.
- Management does not expect cancellation of tenders except for some private industrial orders, which may be deferred.
- Prospects are better in SAARC region this year as compared to last year. Rs60bn of regional tenders are expected to be quoted. Increased activity is expected in Bangladesh and Nepal in the region, Mozambique, Tanzania, and Ivory Coast in Africa.
- Company has bid for a large portion in Rs50bn worth of orders tendered recently in Oman, UAE and Saudi Arabia.
- Company has won two orders worth a total of Rs5bn from Sterlite in SAE and does not see revenue growth in SAE in FY21 due to low activity and Brazil currency devaluation.
- In civil segment, the management expects Rs15bn revenues in FY21.
- In railways segment, the management is hopeful of 35-40% growth in FY21 given: 1) strong orderbook of Rs60bn, and 2) expectations of strong order intake in FY21 (Rs90bn-100bn worth tenders expected in June and some orders from metros)
- Rs3bn-4bn could not be collected in March due to Covid-19 and was collected in April (Rs1bn received from Saudi Arabia since March). Company has increased its working capital limit and is supporting small vendors, which led to reduction in payables in Q4FY19.
- Company will be reconsidering its FY21 capex plans. It expects outlay of Rs1bn from Rs2.2bn earlier. Capex will be towards increasing mechanisation in railways, civil and T&D segments.
- Shift in international borrowing mix (from 40% to 55%) led to decrease in interest cost as percentage of sales to 1.8% in Q4FY20 vs 2.2% in Q4FY19. For FY21, the management expects further improvement of 25-30bps in interest cost from 2.6% in FY20
- Staff costs increased during the quarter as the company had to employ permanent staff at SAE Towers.

Table 2: Financial highlights

(Rs mn)

	Q4FY19	Q4FY20	YoY(%)	Q3FY20	QoQ(%)	I-Sec est.	Var (%)	FY19	FY20	YoY(%)
Net Sales	38,412	36,710	(4.4)	30,731	19.5	34,387	6.8	1,10,005	1,19,654	8.8
EBITDA	3,990	3,707	(7.1)	3,185	16.4	3,152	17.6	11,499	12,344	7.3
Margin	10.4	10.1	-30bps	10.4	-27bps	9.2	93bps	10.5	10.3	
Depreciation	261	392	50.3	367	6.7	302	29.8	1,171	1,472	25.7
Finance Cost	846	652	(22.9)	811	(19.5)	916	(28.8)	3,119	3,080	(1.2)
Other Income	63	27	(56.9)	21	33.2	36	(24.8)	226	111	(50.9)
Extraordinary income	-	-		-		-		-	-	
PBT	2,948	2,691	(8.7)	2,028	32.7	1,970	36.6	7,435	7,903	6.3
Tax	1,009	762	(24.5)	579	31.6	525	45.0	2,571	2,247	(12.6)
Tax rate (%)	34.2	28.3	-590bps	28.5	-23bps	26.7		34.6	28.4	
Reported PAT	1,939	1,929	(0.5)	1,449	33.1	1,445	33.5	4,864	5,655	16.3
Adjusted PAT	1,939	1,929	(0.5)	1,449	33.1	1,445	33.5	4,864	5,655	16.3
Margin(%)	5.0	5.3	20bps	4.7	54bps	4.2	105bps	4.4	4.7	
EPS	7.5	7.5		5.6		5.6		18.9	22.0	
Order intake	25,540	15,110	(40.8)	60,540	(75.0)			1,40,840	1,13,310	(19.5)
Orderbook	2,03,070	2,05,030	1.0	2,20,110	(6.9)			2,03,070	2,05,030	1.0

Source: Company data, I-Sec research

Table 3: Segmental revenue breakup

(Rs mn)	Q4FY19	Q4FY20	YoY(%)	Q3FY20	QoQ(%)	I-Sec est	Var (%)	FY19	FY20	YoY(%)
T&D (excl. SAE)	24,340	20,180	(17.1)	17,030	18.5	20,993	(3.9)	63,390	66,370	4.7
T&D - SAE	3,190	4,440	39.2	4,320	2.8	3,285	35.2	9,670	15,370	58.9
T&D	27,530	24,620	(10.6)	21,350	15.3	24,278	1.4	73,060	81,740	11.9
Cables	3,490	2,170	(37.8)	2,490	(12.9)	3,037	(28.5)	11,830	9,780	(17.3)
Railways	6,330	8,610	36.0	6,010	43.3	6,106	41.0	19,180	25,520	33.1
Civil	1,630	1,720	5.5	870	97.7	948	81.4	4,980	3,760	(24.5)
Solar	320	320	-	420	(23.8)	418	(23.4)	3,410	1,270	(62.8)
Total	39,300	37,440	(4.7)	31,140	20.2	34,787	7.6	1,12,460	1,22,070	8.5

Source: Company data, I-Sec research

Table 4: Segmental assumptions

Rs mn	FY16	FY17	FY18	FY19	FY20	FY21E	FY22E
Revenues	87,103	87,540	1,00,900	1,10,010	1,19,650	1,25,297	1,35,227
Power T&D (excl SAE)	-	-	67,890	63,380	66,360	63,042	69,346
Power T&D (SAE)	-	-	10,250	9,670	15,390	13,851	13,851
Power T&D	72,120	70,310	78,140	73,050	81,750	76,893	83,197
Cables	11,180	10,540	10,090	11,830	9,790	8,811	9,692
Railway	2,100	4,460	8,440	19,180	25,510	25,510	27,551
Water /civil	1,030	860	2,680	4,980	3,760	13,327	13,993
Solar	930	1,590	2,880	3,420	1,260	756	794
Growth YoY (%)	2.8	0.5	15.3	9.0	8.8	4.7	7.9
Power T&D (excl SAE)				(6.6)	4.7	(5.0)	10.0
Power T&D (SAE)				(5.7)	59.2	(10.0)	-
Power T&D	(1.0)	(2.5)	11.1	(6.5)	11.9	(5.9)	8.2
Cables	23.3	(5.7)	(4.3)	17.2	(17.2)	(10.0)	10.0
Railway	57.9	112.4	89.2	127.3	33.0	-	8.0
Water /civil	(27.0)	(16.5)	211.6	85.8	(24.5)	254.4	5.0
Solar	933.3	71.0	81.1	18.8	(63.2)	(40.0)	5.0
Order Inflow	87,140	1,23,580	1,50,980	1,40,840	1,13,310	1,14,216	1,22,766
Power TD	71,047	92,685	96,627	87,321	44,191	57,448	60,321
Cables	9,583	9,886	10,569	9,859	9,065	9,065	9,971
Railway	5,384	14,830	39,255	30,985	31,727	33,313	36,644
Water	1,126	6,179	4,529	2,817	27,194	13,597	14,957
Growth YoY (%)							
Power TD	5.9	41.8	22.2	(6.7)	(19.5)	0.8	7.5
Cables	4.1	30.5	4.3	(9.6)	(49.4)	30.0	5.0
Railway	(16.8)	3.2	6.9	(6.7)	(8.1)	-	10.0
Water	118.2	175.4	164.7	(21.1)	2.4	5.0	10.0

Source: Company data, I-Sec research

Financial summary

Table 5: Profit & loss statement

(Rs mn, year ending March 31)

	FY19	FY20	FY21E	FY22E
Total Income	1,10,005	1,19,654	1,25,297	1,35,227
Operating Expenses	98,506	1,07,310	1,13,163	1,22,117
EBITDA	11,499	12,344	12,134	13,110
% margins	10.5	10.3	9.7	9.7
Depreciation & Amortisation	1,171	1,472	1,487	1,502
EBIT	10,328	10,872	10,648	11,608
Gross Interest	3,119	3,080	3,132	3,381
Other Income	226	111	200	200
PBT before exceptionals	7,435	7,903	7,715	8,428
Add:				
Extraordinaries/Exceptionals	-	-	-	-
Add: Share in associates	-	-	-	-
PBT	7,435	7,903	7,715	8,428
Less: Taxes	2,571	2,248	2,160	2,360
Less: Minority Interests	-	-	-	-
Net Income (Reported)	4,864	5,655	5,555	6,068
Adjusted Net Income	4,864	5,655	5,555	6,068

Source: Company data, I-Sec research

Table 6: Balance sheet

(Rs mn, year ending March 31)

	FY19	FY20	FY21E	FY22E
Assets				
Total Current Assets	1,04,915	1,12,731	1,22,809	1,34,272
of which cash & cash eqv.	2,762	1,637	4,022	5,235
Total Current Liabilities & Provisions	74,129	77,969	79,715	85,973
Net Current Assets	30,786	34,762	43,093	48,299
Investments	132	225	225	225
Other Non-Current Assets	2,037	2,226	2,226	2,226
Net Fixed Assets	9,860	10,662	7,020	7,019
Goodwill	-	1,470	1,470	1,470
Total Assets	42,816	49,345	54,034	59,238
Liabilities				
Borrowings	16,968	20,618	20,618	20,618
Deferred Tax Liability	1,497	751	788	828
Minority Interest	-	-	-	-
Equity Share Capital	514	514	514	514
Face Value per share (Rs)	2.00	2.00	2.00	2.00
Reserves & Surplus	23,837	27,462	32,114	37,278
Net Worth	24,351	27,976	32,628	37,793
Total Liabilities	42,816	49,345	54,034	59,238

Source: Company data, I-Sec research

Table 7: Cashflow statement

(Rs mn, year ending March 31)

	FY19	FY20	FY21E	FY22E
Operating Cashflow	6,980	5,975	11,431	12,407
Working Capital				
Changes	(4,993)	(5,101)	(5,945)	(3,993)
Capital Commitments	(318)	(1,085)	(1,030)	(1,500)
Free Cashflow	1,669	(210)	4,456	6,914
Cashflow from Investing Activities	261	(93)	-	-
Issue of Share Capital	-	-	-	-
Buyback of shares	-	-	-	-
Inc (Dec) in Borrowings	574	3,650	-	-
Interest paid	(3,119)	(3,080)	(3,132)	(3,381)
Dividend paid	(238)	(718)	(839)	(1,057)
Extraordinary Items/Others	1,302	(674)	1,902	(1,263)
Chg. in Cash & Bank balance	449	(1,125)	2,386	1,213

Source: Company data, I-Sec research

Table 8: Key ratios

(Year ending March 31)

	FY19	FY20	FY21E	FY22E
Per Share Data (in Rs.)				
Diluted adjusted EPS	18.9	22.0	21.6	23.6
Recurring Cash EPS	23.5	27.7	27.4	29.4
Dividend per share (DPS)	2.7	3.4	3.5	3.5
Book Value per share (BV)	94.7	108.8	126.9	147.0
Growth Ratios (%)				
Operating Income	9.0	8.8	4.7	7.9
EBITDA	14.3	7.3	(1.7)	8.0
Recurring Net Income	6.1	16.3	(1.8)	9.2
Diluted adjusted EPS	6.1	16.3	(1.8)	9.2
Diluted Recurring CEPS	6.3	18.1	(1.2)	7.5
Valuation Ratios				
P/E	10.3	8.9	9.0	8.3
P/CEPS	8.3	7.0	7.1	6.6
P/BV	2.1	1.8	1.5	1.3
EV / EBITDA	5.6	5.6	5.5	5.0
EV / Operating Income	0.6	0.6	0.5	0.5
EV / Op. FCF (pre-capex)	32.3	78.8	12.1	7.8
Operating Ratios				
Raw Material/Sales (%)	49.2	46.7	47.0	46.5
SG&A/Sales (%)	8.8	10.1	10.1	10.1
Other Income / PBT (%)	3.0	1.4	2.6	2.4
Effective Tax Rate (%)	34.6	28.4	28.0	28.0
NWC / Total Assets (%)	65.5	67.1	72.3	72.7
Inventory Turnover (days)	21.3	23.7	24.0	26.0
Receivables (days)	161.8	165.5	170.0	170.0
Payables (days)	159.3	152.7	150.0	150.0
Debt/Equity (x)	0.7	0.7	0.6	0.5
Profitability Ratios (%)				
Recurring Net Income				
Margins	4.4	4.7	4.4	4.5
RoCE	16.4	16.0	14.4	14.3
RoNW	20.0	20.2	17.0	16.1
Dividend Payout Ratio	14.3	15.5	16.2	14.8
Dividend Yield	1.4	1.7	1.8	1.8
EBITDA Margins	10.5	10.3	9.7	9.7

Source: Company data, I-Sec research

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