Sharekhan by BNP PARIBAS

KEC International

Decent performance despite challenges

Sector: Capital Goods
Result Update

	Change
Reco: **Buy**	↔
CMP: **Rs. 197**	
Price Target: **Rs. 240**	↑

↑ Upgrade ↔ No change ↓ Downgrade

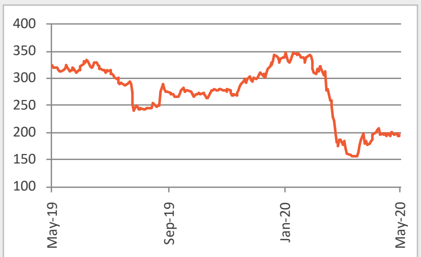
Company details

Market cap:	Rs. 5,057 cr
52-week high/low:	Rs. 358/155
NSE volume: (No of shares)	3.8 lakh
BSE code:	532714
NSE code:	KEC
Sharekhan code:	KEC
Free float: (No of shares)	12.4 cr

Shareholding (%)

Promoters	51.7
FII	8.7
DII	27.5
Others	12.2

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	7	-36	-29	-41
Relative to Sensex	6	-21	-8	-22

Sharekhan Research, Bloomberg

The revenues of KEC International Limited (KEC) came in lower by 4% y-o-y (marginally above estimates) impacted by COVID-19 led disruption leading to lower T&D business (revenue de-grew by 11% y-o-y). Management estimates Rs. 500 crore to Rs. 600 crore revenue loss due to COVID-19 led lockdown in March 2020. SAE revenues grew 39%y-o-y due to execution of three large orderswhich is expected to continue to contribute for next couple of quarters. The non-T&D (railways, civil and other businesses) grew by 9% y-o-y, wherein railways saw strong growth of 36% y-o-y. The civil segment saw a marginal growth due to muted industrial capex and challenges in the realty sector. Blended operating margins remained almost flat at 10.1% which along with lower interest cost and lower tax outgo resulted in flat net earnings growth y-o-y. The management refrained from giving any revenue and margin guidance for FY2021 due to the uncertainty in a COVID-19 led business environment. Order inflow from KEC remained weak during the quarter while order book stood at Rs. 20,503 crore (up 1% y-o-y). KEC has received orders worth Rs. 739 crore for YTDFY21 and has L1 position in orders worth Rs. 4000 crore.The company has bid for Rs. 14,000 crore worth projects (Power Grid tenders & Southern SEBs) over trailing two weeks. The outlook for KEC'sbusiness segments, viz. T&D international and non T&D comprising railways, civil and other businesses remains favorable. In the railways segment, order momentum has remained slow but is expected to pick up as railways get fully operational. Further, opportunities in the international T&D (Mena region and Africa) with a good chunk of tenders being floated provides further avenues for order inflow. We have fine-tuned our earnings estimates for FY2021-FY2022 and revised our valuation multiple given a healthy order backlog along with order inflow visibility in international T&D &non T&D business and KEC's ability to ramp-up execution (currently 85% of sites operational). We maintain a Buy rating on the stock with a revised PT of 240.

Key positives

- Strong growth in international T&D (SAE).
- KEC is L1 bidder for projects worth Rs. 4,000 crore, largely in T&D from the international market.
- Railways continue its strong execution (36% y-o-y)

Key negatives

- Domestic T&D revenues remained lower due to COVID-19 led shutdown and delay in delivery of some substation equipment
- Order booking remained lower y-o-y

Our Call

Maintain Buy with a revised PT of Rs. 240: The sector and the stock have seen significant correction and at CMP, the valuation is attractive at 8.3x one-year forward P/E. We believe, this provides an attractive investment proposition. We have fine-tuned our earnings estimates for FY2021-FY2022 and have revised our valuation multiples given a healthy order backlog along with order inflow visibility in international T&D &non T&D business as well as KEC's execution capabilities to bag orders in tough scenarios. We maintain a Buy rating on the stock with a revised PT of 240.

Key Risks

Slowdown in tendering activities, especially in T&D and railways.

Valuation (Consolidated) Rs cr

Particulars	FY19	FY20	FY21E	FY22E
Revenue	11,001	11,965	12,668	13,915
OPM (%)	10.5	10.3	9.8	10.0
Adjusted PAT	486	566	534	607
% YoY growth	5.7	16.3	(5.6)	13.7
Adjusted EPS (Rs.)	18.9	22.0	20.8	23.6
P/E (x)	10.4	8.9	9.5	8.3
P/B (x)	2.1	1.8	1.5	1.3
EV/EBITDA (x)	5.6	5.6	5.8	5.1
RoNW (%)	21.9	21.6	17.5	17.0
RoCE (%)	26.4	24.0	20.6	20.7

Source: Company; Sharekhan estimates

Revenues marginally ahead with inline OPM: Revenues of KEC International Limited (KEC) came lower by 4% y-o-y (marginally above estimates) impacted by COVID-19 led disruption leading to lower T&D business where revenue degrew by 11%. SAE revenues grew 39% y-o-y due to three large order executions. It will continue to contribute strongly for next couple of quarters. The non-T&D comprising railways, civil and other businesses grew by 9% y-o-y, wherein railways saw strong growth of 36% y-o-y growth, whereas the civil segment saw a marginal growth due to muted industrial capex and challenges in realty sector. Blended operating margins remained almost flat at 10.1% y-o-y largely led by lower raw material cost offset by higher employee cost. Stable operational performance along with lower interest cost and lower tax outgo resulted in flat net earnings growth. The company's has 85% of its projects operational now and expects execution to gain momentum going ahead. Although labour remains a challenge, the company is training the local labourers and working with them to suffice the labour shortage.

Order book remains healthy despite weak ordering: KEC's order backlog remains strong at Rs. 20,503 crore, providing a revenue visibility of 1.7x FY2020 revenue. Moreover, KEC stands as the lowest bidder for approximately Rs. 4000 crore worth of projects majorly in international T&D. Further, in the Green Energy Corridor, the tendering pipeline provides healthy order inflow visibility for KEC, but fructification of the same remains a key monitorable. Globally, KEC is witnessing traction in Middle East (UAE, OMAN and Saudi) despite falling crude and Africa where tenders are coming. Order inflows in these geographies are likely to gain momentum from FY2021. For SAE Towers, all three major EPC projects on its book are currently being executed and are expected to end in next couple of quarters. In the railways business vertical, the company has a strong order book and expects tendering to continue as economic activity starts and no tenders being shelved as of now.

Key conference call highlights

Guidance: The management didn't give any revenue and margin guidance due to the COVID-19 led uncertain business environment

Order backlog and L1 positions: The company's current order book stands at Rs.20,503 crore and L1 in orders worth Rs.4000 crore majorly in T&D. Further, in the Green Energy Corridor, the tendering pipeline provides a healthy order inflow visibility but fructification of the same remains a key monitorable. PGCIL has also floated tenders worth Rs 14000 crore through TBCB and the company has bid for the same. Further, the management expects tenders in domestic T&D is expected to be better than last year. In railways, the large tenders are expected to come out in June 2020 and no capex are being shelved from railways as of now.

T&D: PGCIL has floated tenders worth Rs 14000 crore and more are expected in the couple of weeks through the TBCB route . Internationally KEC is witnessing traction in Middle East despite lower crude prices majorly in OMAN, UAE and Saudi. Further SAARC and Africa is also witnessing good tendering activity. Order inflows in these geographies are likely to gain momentum from FY2021.

Railways: In the railways segment, KEC earlier has entered into new sub-segments such as railway over-bridges, metrocivil works and the Regional Rapid Transit System (RRTS), which is in line with the company's strategy to expand its presence in the Railways and civil segment. Order tendering remains healthy for the new segments and execution for the current orders are on track. Order book remains healthy in railways.

Civil: KEC has been focusing on diversification in sub-segments; secured orders in Metro. The company has healthy order book in civil segment and expects this segment to scale up in the next two three years on the same line as railways.

Saudi receivables: There are no overdues from Saudi Arabia as of now and the company has received Rs.100 crore in the quarter.

Borrowings: Average borrowing level has come down to ~Rs.2,600Cr for the full year against ~Rs.3,100 Cr in the last year.

Capex: Company is relooking at its capex plans and expected to do a capex of Rs 100 crore against earlier plans of Rs 200-250 crore.

Operation in factories and project sites: The KEC management stated that work has partially started in all its factories with social distancing norms' 85% of its projects are operational now. Management also mentioned that although labour remains a challenge but the company is training the local labours and working with them to suffice the labour shortage. Further cost incurred on retaining labours will be largely offset by lower raw-material prices.

Results (consolidated) Rs cr

Particulars	Q4FY20	Q4FY19	YoY %	Q3FY20	QoQ %
Net Sales	**3,671**	**3,841**	**-4%**	**3,073**	**19%**
Net raw material	1,647	1,933	-15%	1,439	14%
Erection and subcontracting charges	998	1,048	-5%	703	42%
Employee cost	307	211	45%	301	2%
Other Expenditure	349	251	39%	311	12%
Operating Profit	**371**	**399**	**-7%**	**319**	**16%**
OPM %	10.1%	10.4%		10.4%	
Other Income	3	6	-57%	2	33%
EBITDA	**373**	**405**	**-8%**	**321**	**16%**
EBITDAM %	10.2%	10.6%		10.4%	
Depreciation	39	26	50%	37	7%
Interest	65	85	-23%	81	-20%
PBT	269	295	-9%	203	33%
Tax Expenses :	76	101	-25%	58	32%
Tax rate %	28%	34%		29%	
Net Profit before exceptional items	**193**	**194**	**-1%**	**145**	**33%**
Exceptional items	-	-		-	
Net Profit after exceptional items	**193**	**199**	**-3%**	**145**	**33%**
NPM %	5.3	5.2		4.7	

Source: Company; Sharekhan Research

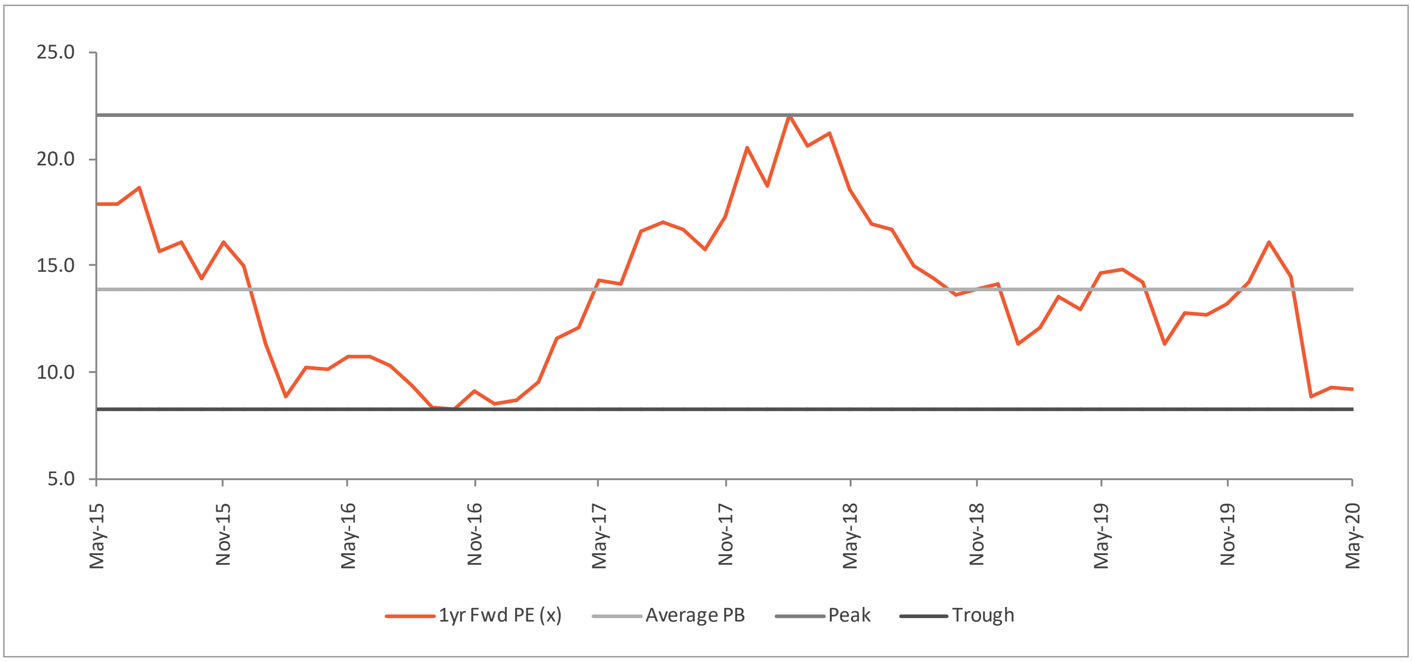
Outlook

FY2021 revenue growth to be in single digits due to COVID-19: In wake of COVID-19 led lockdown since mid-March 2020, the management didn't provide any guidance due to the uncertainties in the business otlook. KEC has received Rs. 739 crore order inflow during YTD 2021 and is L1 in Rs. 4,000 crore. Tender pipeline is expected to remain healthy in the domestic and international T&D. Further favorable raw material prices are expected to support margins.

Valuation

Maintain Buy with a revised PT of Rs. 240: The sector and the stock have seen significant correction and at CMP, the valuation is attractive at 8.3x one-year forward P/E. We believe, this provides an attractive investment proposition. We have fine-tuned our earnings estimates for FY2021-FY2022 and have revised our valuation multiples given a healthy order backlog along with order inflow visibility in international T&D &non T&D business as well as KEC's execution capabilities to bag orders in tough scenarios. We maintain a Buy rating on the stock with a revised PT of 240.

One-year forward P/E (x) band



Source: Sharekhan Research

About company

KEC International is a Global Power Transmission Infrastructure EPC major. The company is present in the power T&D, cables, railways, renewable (solar energy), smart Infra and civil construction businesses. Globally, the company has powered infrastructure development in more than 61 countries. KEC is a leader in power transmission EPC projects and has more than seven decades of experience. Over the years, it has grown through the organic as well as the inorganic route.

Investment theme

T&D spend in India is expected to be around Rs.2,300 billion over FY2018-FY2023E, up 28% over FY2012-FY2017. A large part of this spend is likely to come from state electricity boards. Additionally, ordering for the Green Energy Corridor is likely to provide ample opportunities in the domestic market. Moreover, expansion in regional transmission network in Africa, SAARC and CIS countries is likely to supplement domestic demand and present a large business opportunity. KEC has significantly scaled up the non-T&D segments (railways and civil segments) and margins in these segments have improved significantly. The opportunity size remains high in the non-T&D segment to provide enough opportunity to ramp up its total order outstanding for the business.KEC's order book remains strong, providing strong revenue visibility; and order inflow visibility remains healthy in international T&D and railways segments.

Key Risks

- Slower-than-expected execution of projects in domestic and international markets due to various reasons is expected to affect performance.
- Slowdown in tendering activities, especially in T&D, railways and overseas orders.

Additional Data

Key management personnel

Mr. Harsh Vardhan Goenka	Non-Executive - Non Independent Director-Chairperson
Mr. Vimal Kejriwal	Executive Director
Rajeev Aggarwal	Chief Financial Officer
Mr. Ajit Tekchand Vaswani	Non-Executive - Independent Director

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Swallow Associates Ltd	26.36
2	Summit Securities Ltd	10.86
3	HDFC Asset Management Co Ltd	9.25
4	Instant Holdings Ltd	8.49
5	Reliance Capital Trustee Co Ltd	3.56
6	Kotak Mahindra Asset Management Co	3.11
7	Aditya Birla Sun Life Asset Manage	3.10
8	IDFC Mutual Fund/India	2.37
9	STEL Holdings Ltd	1.95
10	LIC of India	1.70

Source: Bloomberg

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