

KNR Constructions Ltd

BUY

CMP Rs197

Target Rs266

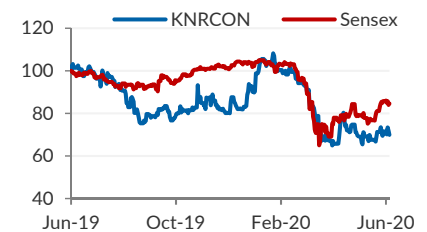
Upside 35%

HIGHLIGHTS	<ul style="list-style-type: none"> ✓ KNR Constructions (KNR) reported decent set of numbers during Q4 FY20 with standalone revenue de-grew by mere ~6% despite COVID related execution shutdown during 10 days of Mar' 20. ✓ Its operating margin remained robust at 21.7% (up 161bps yoy) backed by improved contribution from high-margin irrigation projects. However, higher interest and tax outgo led to a 29% decline in adjusted net profit. ✓ At the end of Mar'20, KNR's order book stood healthy at ~Rs.52 bn (excluding 1 HAM projects estimated to have EPC value of Rs.6.4 bn and two Irrigation projects worth ~Rs.20 bn), ✓ During the quarter, KNR received the appointed date for its Somwarpet HAM project (4 projects out of 5 HAM projects received AD). During FY20, KNR booked ~Rs.610 mn of arbitration award, ✓ The Working Capital has increased due to rise in receivables during the quarter. The Debtors increased to 78 days at end of Q4 FY20 from its normalized levels of ~50 days. ✓ Labor availability during April to June has been at 30-40% on an average. The Company expects situation to drastically improve from July 2020.
Our View	<ul style="list-style-type: none"> ✓ Despite strong order book position, we expect revenues to be under pressure in FY21 as loss of execution during Apr'20 and existing shortage of labor would impact execution. ✓ Operating margin is likely to come under pressure during H1 FY21 due to sluggish execution while fixed costs continue. ✓ Order book remains strong currently and focus on two major segments of roads and irrigation to help get new orders. The proceeds from BOT - toll asset sale (expected in next few months) would enhance bidding capacity.
Valuation	<ul style="list-style-type: none"> ✓ Considering the COVID impact on topline and margins, we cut our estimates for FY21 and FY22. However, we believe, the Company is well placed to speed up execution as COVID related impact settles. ✓ Continued focus on asset monetization and comfortable balance sheet position provide comfort. We maintain our BUY rating on the stock for revised target of Rs.266 (Based on SOTP valuation).
Risk to our call	<ul style="list-style-type: none"> ✓ Slower than expected ramp up in execution.

Stock data (as on June 12, 2020)

Sensex:	33,781
52 Week h/l (Rs)	312 / 171
Market cap (Rs/USD mn)	27,681 / 365
Outstanding Shares	141
6m Avg t/o (Rs mn):	59
Div yield (%):	0.3
Bloomberg code:	KNRC IN
NSE code:	KNRCON

Stock performance



	1M	3M	1Y
Absolute return	6.7%	-16.1%	-31.4%

Shareholding pattern (As of Mar'20 end)

Promoter	55.2%
FII+DII	34.5%
Others	10.3%

Δ in earnings estimates

	FY20	FY21e	FY22e
EPS (New)	16.0	11.4	18.5
EPS (Old)	16.6	18.3	20.5
% change	(3.5)	(37.5)	(9.6)

Exhibit 1: Result table (Standalone)

Y/e 31 Mar (Rs m)	Q4 FY20	Q4 FY19	yoy(%)	Q3 FY20	qoq (%)
Revenue	6,756	7,157	(5.6)	5,579	21.1
Operating Profit	1,469	1,441	1.9	1,244	18.1
OPM (%)	21.7	20.1	161 bps	22.3	-55 bps
Other Income	73	151	(51.9)	70	4.4
Depreciation	(538)	(478)	12.4	(517)	4.0
Interest	(145)	(75)	93.0	(142)	2.1
Exceptional item	-	(25)	NA	(67)	NA
PBT	860	1,014	(15.2)	588	46.2
Tax	(187)	(92)	103.2	(186)	0.7
Reported PAT	672	922	(27.0)	402	67.2
Adjusted PAT	672	947	(29.0)	469	43.3

Source: Company, YES Sec - Research

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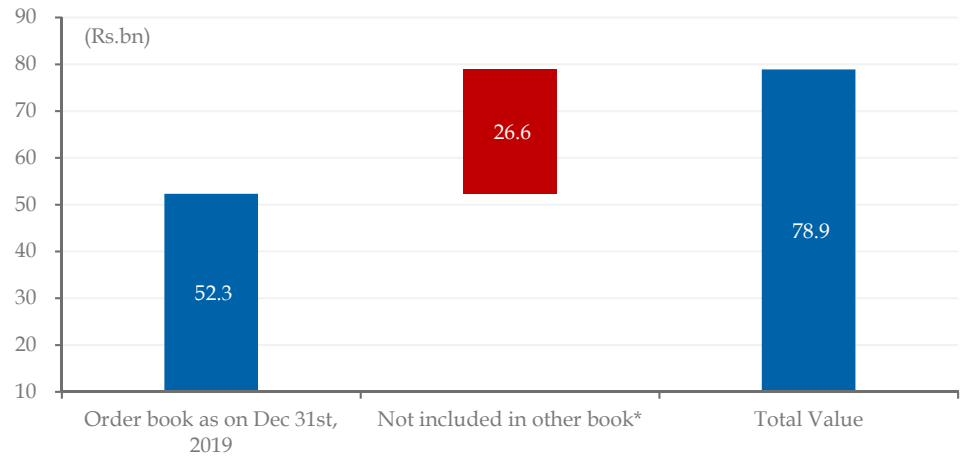
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CONCALL HIGHLIGHTS

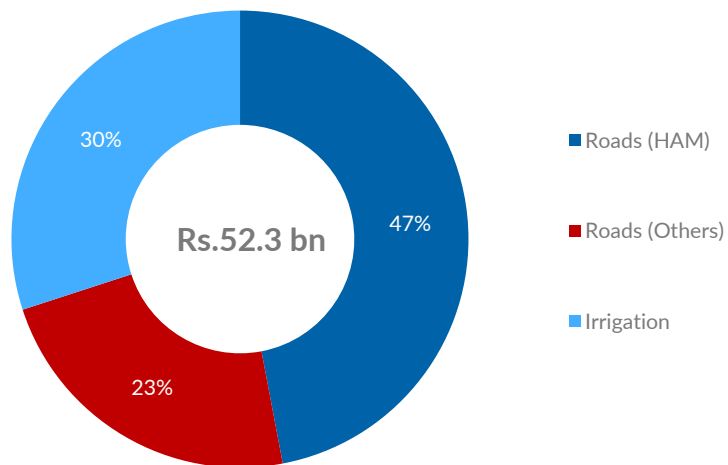
- ✓ With COVID-19 impacting the labor availability and raw material' supply chain, KNR is currently executing the projects with the efficiency level of ~55-60%. The management expects execution during H1 FY21 to remain subdued with likely rebound in H2 FY21.
- ✓ Out of its Portfolio of 5 HAM Projects, a) KNR Srirangam has achieved 37.4% physical progress, b) KNR Tirumala achieved 54.4%, c) KNR Shankampet achieved 43.7% and d) KNR Somwarpeth achieved 6.9% progress. In the 5th HAM project namely KNR Palani, the company has submitted financial closure document to NHAI on 22nd May'20 and expects to achieve Appointed date over next couple of months.
- ✓ Order book at the end of FY20 stood at Rs.52.3bn (excludes one HAM project having estimated EPC value of Rs.6.4bn and two irrigation projects worth ~Rs,20bn).
- ✓ The management expects NHAI to award ~4,000 km of road projects during FY21 (better than ~3,200 km awarded in FY20). Out of the current bidding pipeline, the company has identified 4-5 HAM projects (worth ~Rs.70 bn) mainly located in Telangana, Andhra and Telangana regions. The management is targeting ~Rs.30 bn of inflows during FY21 (mainly from road segment).
- ✓ KNR along with its JV partners has received 2 irrigation projects worth ~Rs.23bn from Irrigation & CAD Department, Govt. of Telangana on 17th May'20. As per the management, the projects have better margin profile as compared to roads and other type of irrigation projects. Going forward, the company is not targeting any major projects from irrigation segment.
- ✓ The company has arbitration claims (worth ~Rs.5.5bn) which are under process at different levels. During FY20, the company has booked Rs.610mn of arbitration award.
- ✓ For the KNR Walayar BOT project, the company has signed SPA with Cube Highways and Infrastructure III Pte. Ltd for sale of its 100% stake for an enterprise value of Rs.5.3bn. The company has received approvals from lenders and in-principal approval from NHAI. The management expects whole process to complete over next two-three months.
- ✓ With MoRTH considering the release of retention money to provide liquidity to the contractors, KNR is expecting some inflows from the same (total retention money: ~Rs.1.5bn).
- ✓ The company has not opted for moratorium considering its comfortable liquidity position (debt: Rs.2.3bn including promoter loan of Rs.1.8bn; D/E:0.1x).
- ✓ Till 31st Mar'20, the company has infused ~Rs.2bn towards equity investment in various projects. Equity requirement towards existing projects during FY21 is estimated to be ~Rs.1.5bn.
- ✓ The management has guided for minimal capex (Rs.500mn) during FY21.
- ✓ With available MAT credit of ~Rs.350mn, the management has guided for ~25% effective tax rate for FY21 (under old tax regime). However, the company would opt for new tax regime in FY22.

Exhibit 2: Robust order book provides revenue visibility over next couple of years



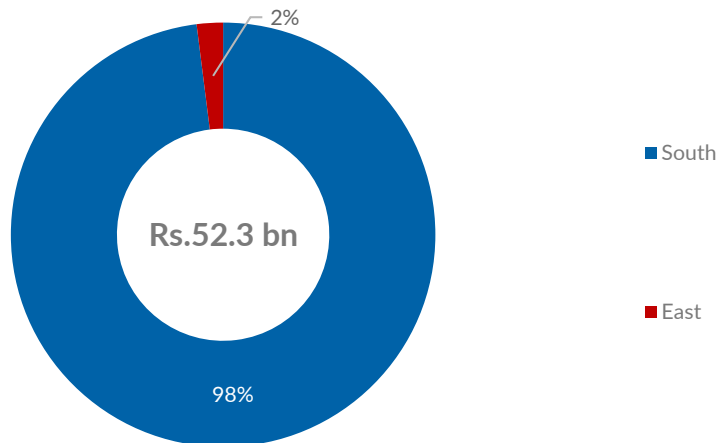
Source: Company, YES Sec - Research; * Estimated EPC value of Oddanchatram - Madathukulam HAM and Kaleshwaram Irrigation Projects

Exhibit 3: Roads segment contribute 70% to the overall order book*



Source: Company, YES Sec - Research; *Excludes estimated EPC value of Oddanchatram - Madathukulam HAM and Kaleshwaram Irrigation Projects

Exhibit 4: Major player in Southern India with 98% order book concentration



Source: Company, YES Sec - Research; *Excludes estimated EPC value of Oddanchatram - Madathukulam HAM and Kaleshwaram Irrigation Projects

Exhibit 5: Financial Summary (Standalone)

Y/e 31 Mar (Rs m)	FY19	FY20	FY21E	FY22E
Revenues	21,373	22,442	21,320	26,650
yoy growth (%)	10.6	5.0	(5.0)	25.0
Operating profit	4,270	4,871	3,997	5,273
OPM (%)	20.0	21.7	18.7	19.8
Reported PAT	2,633	2,252	1,607	2,605
Adjusted PAT	2,658	2,360	1,607	2,605
yoy growth (%)	(2.3)	(11.2)	(31.9)	62.1
EPS (Rs)	18.72	16.0	11.4	18.5
P/E (x)	10.5	12.3	17.2	10.6
EV/EBITDA (x)	7.0	6.1	7.1	4.5
Debt/Equity (x)	0.2	0.1	0.1	0.1
RoE (%)	20.5	14.8	9.5	13.7

Source: Company, YES Sec - Research

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