

Strong execution; healthy outlook...

KNR Constructions reported a better-than-expected performance during Q2FY21 with superior execution and margins leading to bottomline beat. Topline was up 10.1% YoY to ₹ 601.2 crore. Operating profit remained at an elevated level at 20.6% (down 239 bps YoY but up 80 bps on adjusted basis) backed by higher proportion of revenues from HAM and high margin irrigation projects. Reported PAT fell 28.9% YoY to ₹ 49.8 crore. We note that the company has booked net exceptional loss of ₹ 11.2 crore mainly on account of a) write-offs in Walayar project (sold to Cube Highways) and on another project terminated by NHAI and b) net of arbitration award. Adjusted for the same, PAT was at ₹ 61.1 crore (down 17.6% YoY).

Order book healthy; execution to ramp up ahead

The order book was robust at ₹ 8,555 crore at the end of Q2, translating to healthy ~3.7x order book to bill. The order book is mainly contributed by roads-HAM (31%), roads-EPC (24%) and irrigation (45%) segments. Additionally, the company has identified 10-15 bids, mainly in the roads segment and aims to bag ~₹ 2000-2,500 crore order inflows in the remaining period of FY21. This is likely to further strengthen its order book. On the execution front, KNR is currently operating at ~80% efficiency level and expects to achieve 100% by November 2020 end. The management guided for ~₹ 600 crore of revenues in Q3FY21 and another ₹ 700+ crore in Q4FY21. Operating margin is likely to sustain at 17-18% with better project mix.

Working capital improves; Telangana recovery likely soon

KNR witnessed an improvement in working capital days from 53 days as on March 31, 2020 to 44 days currently, aided by better collections. However, its exposure to the Telangana government's projects remains high at ₹ 740 crore. The management has indicated towards receipt of funds amounting to ~₹ 167 crore in October-November 2020 while expecting another ~₹ 400 crore by November 2020 end and balance in Q4FY21. Given the promising timeline, the working capital days is once again likely to normalise by FY21-end to its earlier level of ~40 days. KNR has already infused ~₹ 227 crore equity towards HAM projects and remaining equity commitment is ₹ 398 crore. It has guided for ₹ 240 crore further equity infusion towards HAM projects in FY21E with ₹ 108 crore, ₹ 50 crore infusion in FY22, FY23, respectively. Equity commitment is likely to be supported by internal cash generation and irrigation dues recovery and should not entail new debt at standalone levels.

Valuation & Outlook

Considering strong execution, best in class WC, monetisation of BOT/HAM assets, healthy balance sheet, strong return ratios, we maintain **BUY** on the stock with a revised SoTP TP of ₹ 310. We will closely monitor irrigation receivables recovery that will be key catalyst for stock performance.

Key Financial Summary

₹ crore	FY18	FY19	FY20	FY21E	FY22E	CAGR FY20-22E
Net Sales	1,931.7	2,137.3	2,244.2	2,398.7	2,792.2	11.5%
EBITDA	386.1	427.0	487.1	442.8	529.4	4.3%
EBITDA Margin (%)	20.0	20.0	21.7	18.5	19.0	
PAT	272.1	263.3	225.2	207.5	253.0	6.0%
EPS (₹)	19.4	18.7	16.0	14.8	18.0	
P/E (x)	13.3	13.7	16.0	17.4	14.3	
EV/EBITDA (x)	9.8	9.0	7.7	8.5	6.7	
RoNW (%)	23.5	18.6	13.9	11.4	12.2	
RoCE (%)	20.5	19.0	19.0	16.6	16.3	

Source: Company, ICICI Direct Research



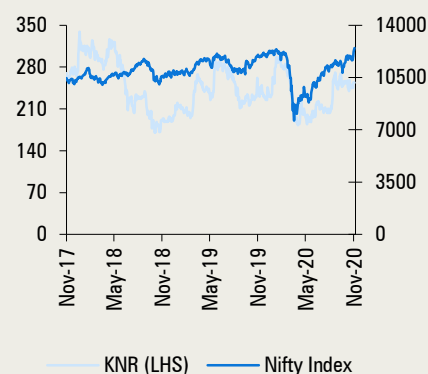
Particulars

Particular	Amount (₹ crore)
Market Capitalization	3,608.5
Total Debt (FY20)	214.1
Cash (FY20)	33.1
EV	3,789.6
52 week H/L (₹)	311/ 171
Equity capital	28.1
Face value	2.0

Key Highlights

- Total backlog at ~₹ 8555 crore, provides strong revenue visibility of 2.5-3 years
- Maintain BUY with target price of ₹ 310/share

Price Chart



Research Analyst

Bhupendra Tiwary, CFA
bhupendra.tiwary@icicisecurities.com

Lokesh Kashikar
lokesh.kashikar@icicisecurities.com

Exhibit 1: Variance analysis

Particulars	Q2FY21	Q2FY21E	Q2FY20	YoY (%)	Q1FY21	QoQ (%)	Comments
Total Operating Income	601.2	530.0	546.2	10.1	479.4	25.4	Strong execution led to topline beat
Other Income	7.6	10.0	25.6	-70.3	6.1	24.4	
Consumption of raw materials	190.5	172.1	172.1	10.7	189.9	0.3	
Employee benefit expenses	29.3	30.6	36.3	-19.4	27.8	5.4	
Other Expenses	53.9	54.7	68.4	-21.2	42.3	27.7	
EBITDA	124.0	100.5	125.8	-1.4	94.3	31.5	
EBITDA Margin(%)	20.6	19.0	23.0	-240 bps	19.7	95 bps	
Depreciation	35.2	45.0	47.5	-26.0	33.1	6.3	
Interest	15.8	10.0	9.8	61.8	10.2	54.6	
PBT	80.7	55.5	94.1	-14.2	57.1	41.2	
Taxes	19.6	14.0	20.0	-1.9	17.3	NM	
PAT	49.8	41.5	70.1	-28.9	39.8	25.3	

Source: Company, ICICI Direct Research

Exhibit 2: Change in estimates

(₹ Crore)	FY19	FY20	FY21E			FY22E			Comments
			Old	New	% Change	Old	New	% Change	
Revenue	2,137.3	2,244.2	2,002.9	2,398.7	19.8	2,511.6	2,792.2	11.2	Realign numbers after H1 performance
EBITDA	427.0	487.1	369.7	442.8	19.8	501.3	529.4	5.6	
EBITDA Margin (%)	20.0	21.7	18.5	18.5	0 bps	20.0	19.0	-100 bps	
PAT	263.3	225.2	140.5	207.5	47.7	234.2	253.0	8.0	
Diluted EPS (₹)	18.7	16.0	10.0	14.8	47.7	16.7	18.0	8.0	

Source: Company, ICICI Direct Research

Exhibit 3: Assumptions

EPC	FY19	FY20	Current	Current	Earlier	Earlier	Comments
			FY21E	FY22E	FY21E	FY22E	
Order Inflow	1,736	1,573	6,000	5,000	4,000	4,000	
Order Backlog	5,901	5,230	8,831	11,039	6,227	7,815	

Source: Company, ICICI Direct Research

Conference call Highlights

- NHAI Ordering & Construction:** Despite headwind faced by NHAI due to Covid-19 pandemic, the authority has awarded projects worth ~₹ 47,000 crore (1,330 km) during H1FY21. HAM contributed ~28% to the overall awarding. The management expects awarding activity to further strengthen in H2FY21 and is likely to surpass NHAI's target of 4,500 km for FY21. Additionally, construction activities are likely to pick up with workers returning to the project sites. Traffic movements in highways have also recovered sharply and are near pre-Covid levels
- Order book and inflows:** KNR's order book at the end of September 2020 was at ₹ 8,555 crore (order book to TTM bill: 3.7x), majorly contributed by roads-HAM (31%), roads-EPC (24%) and irrigation (45%) segments. In terms of order inflows, the company has secured orders worth ~₹ 3,190 in H1FY21. Given the robust pipeline, the company has identified 10-15 bids and aims to bag ~₹ 20-2,500 crore order inflows mainly from road- HAM segment in the remaining period of FY21
- Execution progress:** Project execution gathered pace during Q2FY21 with improved labour availability. Currently, the company is operating at ~80% efficiency levels and expects to achieve 100% by end-November 2020. With these, the management has guided for ~₹ 600 crore of revenues in Q3FY21 and another ₹ 700+ crore in Q4FY21. Operating margin is likely to sustain at 17-18% with better project mix
- HAM projects:** Execution is in full swing on four HAM projects whose appointed date (AD) has been received. The physical progress on these projects are: a) Trichy-Kallagam: 49.9%, b) Chittor-Mallavaram: 63.8%, c) Ramsanpalle-Mangloor: 55.9% and d) Magadi-Somwarpath: 13.9%. The management has guided to complete first three projects by May 2021. For the Palani HAM project, the company has secured AD on October 5, 2020
- Equity requirement:** Out of the total equity requirement of ₹ 624 crore, KNR has already infused ₹ 227 crore equity towards HAM projects till September 2020. The management has guided for ₹ 240 crore, ₹ 108 crore, ₹ 50 crore equity infusion towards HAM projects during H2FY21E, FY22E, FY23E, respectively
- Irrigation project:** Among its four major projects in the irrigation segments, a) Mallana Sagar (Megha Engineering): has achieved 60% physical progress; likely to get completed over next six to eight months, b) Venkatadri Reservoir bund (Navayuga Engineering) project: 30% physical progress; likely to get completed over next one year, and c) two packages of Kaleshwaram Project – expects to commence the work soon. However, the company has faced major delays in collection of dues mainly from Telangana and its total exposure is at ₹ 740 crore. The management expects to receive ~₹ 567 crore in November 2020 and balance during Q4FY21
- Walayar BOT project monetisation:** KNR, in January 2020, entered into a share purchase agreement with Cube Highways to sell its 100% entire equity stake in KNR Walayar BOT project at an enterprise value of ₹ 511.8 crore (implies equity value of ₹ 384.7 crore). The company completed sale on September 28, 2020 and received ₹ 308 crore (out of total equity value), which is utilised towards retiring promoter debt worth ₹ 210 crore, while the balance amount used for working capital requirement
- Debt:** KNR's standalone debt declined considerably to ₹ 64 crore at the end of September 2020 (vs. ₹ 230 crore at the end of FY20) largely backed by the repayment of borrowings with the receipt of funds from Walayar project

- **Capex:** The company incurred capex of ₹ 35 crore during H1FY21 and expects to incur another ~₹ 75 crore during H2FY21
- **Working capital:** Working capital days was at 44 days vs. 53 days in end-FY20 mainly aided by better collections
- **Tax rate:** The company has guided for full tax rate for FY21

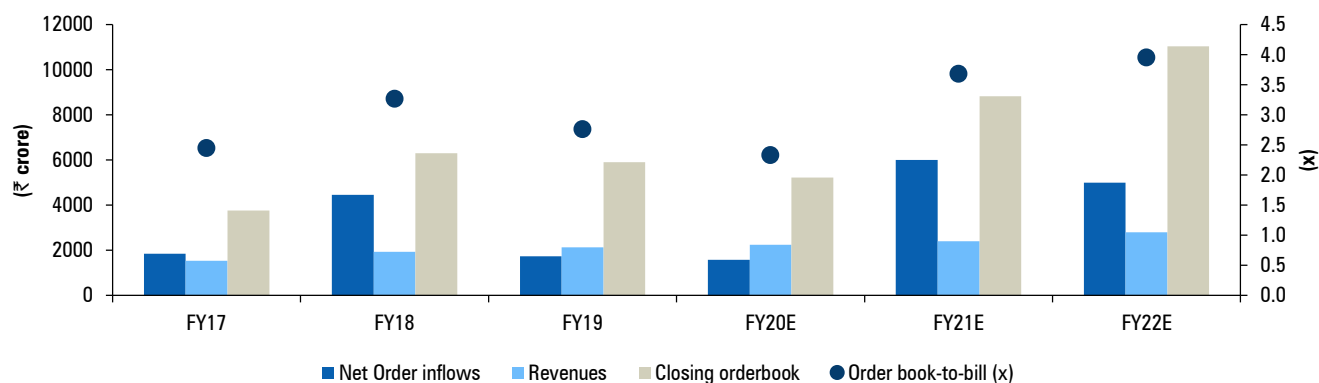
Company Analysis

Exhibit 4: Order book update

Key Projects	(₹ crore)
Elevated Highway along Avinashi Road in Coimbatore City (EPC)	1033
Magadi to Somwarpeth Project (KSHIP HAM)	771
Oddanchatram to Madathukulam Project (HAM)	640
Ramsanpalle to Mangloor Project (HAM)	461
Chittor to Mallavarm Project (HAM)	432
Trichy to Kallagam Project (HAM)	383
Top six projects	3720.0
Other Road projects	973.0
Irrigation projects	3861.5
Other projects	
Total	8554.5

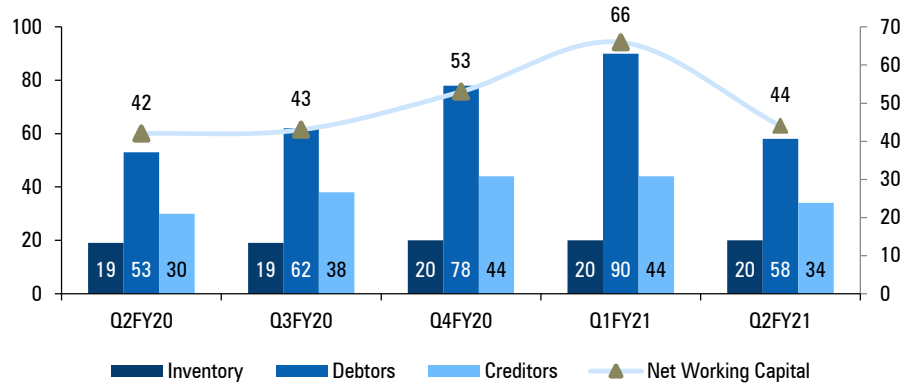
Source: Company, ICICI Direct Research

Exhibit 5: Strong order book position



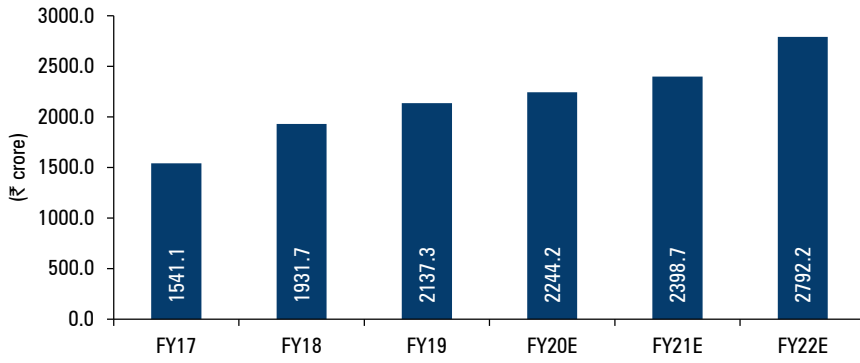
Source: Company, ICICI Direct Research

Exhibit 6: Net working capital days trend



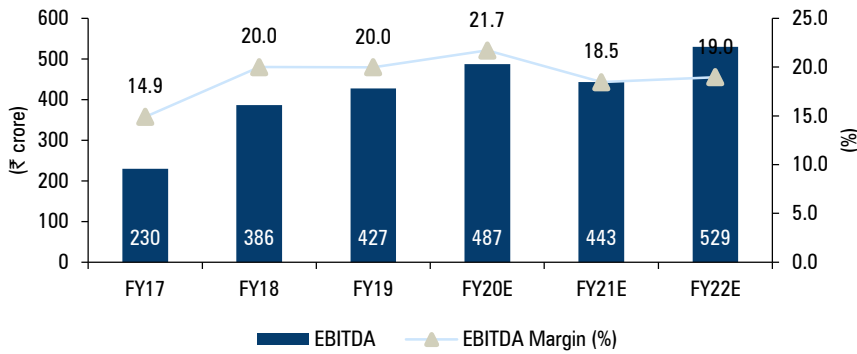
Source: Company, ICICI Direct Research

Exhibit 7: Revenue recovery better than anticipated



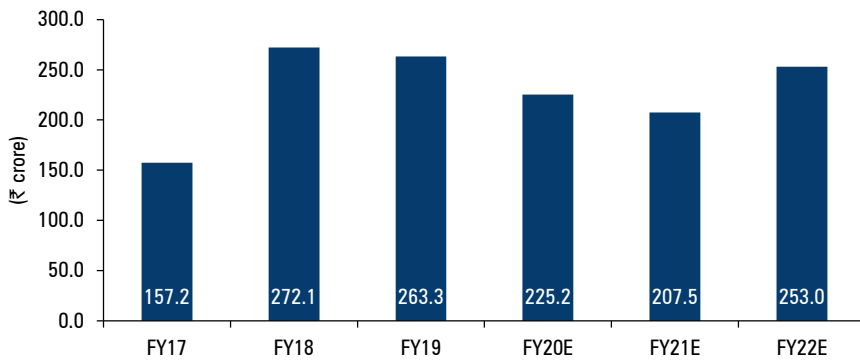
Source: Company, ICICI Direct Research

Exhibit 8: EBITDA & EBITDA margin trend



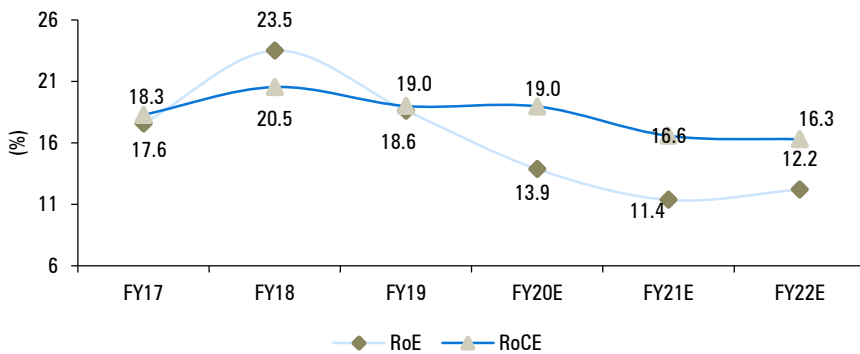
Source: Company, ICICI Direct Research

Exhibit 9: PAT trend



Source: Company, ICICI Direct Research

Exhibit 10: Return ratios trend



Source: Company, ICICI Direct Research

Valuation & Outlook

The company is a focused road based EPC player that enjoys a strong execution track record with the reputation of completing projects on time/ahead of the schedule. KNR also enjoys best in class WC cycle with very healthy balance sheet and strong return ratio. With virtual debt free position at standalone levels, equity commitment is likely to be supported by internal cash generation and irrigation dues recovery and should not entail new debt at standalone levels.

Hence, we maintain our **BUY** recommendation on the stock with an SoTP based revised target price of ₹ 310/share. We value its core EPC business at ₹ 286/share (7.5x FY22E EV/EBITDA).

Exhibit 11: SoTP valuation

	Value (₹ crore)	Per Share (₹)	Comment
EPC Business (A)	3995	284	7.5x FY22E EV/EBITDA
BOT toll Investment (B = C+D)	90	6	
Muzaffarpur tollway (D)	90	6	1x P/BV
HAM Projects Investment (E)	227	16	1x P/BV
Total Equity Investment (F=B+E)	317	23	
Less: Net Debt (G)	-35	-3	FY22E Net Debt
SoTP Value (A+F-G)	4347	309	
Rounded-off target price		310	

Source: Company, ICICI Direct Research

Financial summary

Exhibit 12: Profit and loss statement				
₹ crore				
(₹ Crore)	FY19	FY20	FY21E	FY22E
Net Sales	2,137.3	2,244.2	2,398.7	2,792.2
Other operating income	-	-	-	-
Total Revenues	2,137.3	2,244.2	2,398.7	2,792.2
Raw Material Expense	643.2	753.3	767.6	893.5
Other Construction Exp.	744.9	601.7	755.6	865.6
Employee benefit expenses	92.9	125.2	136.7	159.2
Other Expenses	229.3	277.0	296.0	344.6
Total Operating Exp	1,710.3	1,757.2	1,955.9	2,262.8
EBITDA	427.0	487.1	442.8	529.4
Other Income	63.4	56.6	61.7	67.2
Interest	29.1	47.4	37.5	32.0
Depreciation	168.1	191.8	170.4	226.3
PBT	290.6	304.4	296.5	338.2
Total Tax	27.3	68.5	88.9	85.2
Reported PAT	263.3	235.9	207.5	253.0
Adjusted PAT	263.3	235.9	207.5	253.0
EPS (Diluted)	18.7	16.0	14.8	18.0

Source: Company, ICICI Direct Research

Exhibit 13: Cash flow statement				
₹ crore				
₹ crore	FY19	FY20	FY21E	FY22E
Profit before Tax	290.6	304.4	296.5	338.2
Depreciation	168.1	191.8	170.4	226.3
Interest Paid	29.1	47.4	37.5	32.0
Cash Flow before WC changes	453.1	476.3	442.8	529.4
Net Increase in Current Assets	(168.5)	(350.5)	(42.4)	(256.5)
Net Increase in Current Liabilities	17.9	286.7	69.6	154.8
Net CF from Operating Activities	254.1	338.2	381.0	342.4
(Purchase)/Sale of Fixed Assets	(203.4)	(198.7)	(100.0)	(250.0)
Purchase of Investment	(108.3)	(70.2)	(283.7)	79.3
Interest Income	(4.5)	(56.6)	(61.7)	(67.2)
Net CF from Investing Activities	(285.4)	(212.3)	(322.1)	(103.5)
Proceeds from share capital	-	-	-	-
Interest Paid	29.1	47.4	37.5	32.0
Net CF from Financing Activities	7.2	(105.9)	(86.3)	(29.6)
Net Cash flow	(24.1)	20.1	(27.4)	209.3
Opening Cash/ Cash Equivalent	37.1	13.0	33.1	5.7
Closing Cash/ Cash Equivalent	13.0	33.1	5.7	215.0

Source: Company, ICICI Direct Research

Exhibit 14: Balance sheet				
₹ crore				
(₹ Crore)	FY19	FY20	FY21E	FY22E
Liabilities				
Share Capital	28.1	28.1	28.1	28.1
Reserves & Surplus	1,386.1	1,595.8	1,799.2	2,044.6
Networth	1,414.2	1,623.9	1,827.3	2,072.7
Secured Loan	33.6	33.7	109.5	179.5
Unsecured Loan	230.6	180.5	60.0	-
Total Debt	264.1	214.1	169.5	179.5
Deferred Tax Liability	-	-	-	-
Total Liabilities	1,696	1,856	2,015	2,273
Assets				
Gross Block	1,012.4	1,211.1	1,311.1	1,561.1
Net Block	371.1	377.9	307.5	331.2
Capital WIP	0.0	10.2	10.2	10.2
Non-current Investments	683.0	755.7	1,039.5	960.1
Current Assets				
Inventories	95.0	123.2	131.4	153.0
Sundry Debtors	234.4	476.1	460.0	535.5
Loans and Advances	9.1	6.9	7.1	7.6
Other Current Assets	533.9	635.2	678.9	790.2
Cash	13.0	33.1	5.7	215.0
Total Current Assets	872.3	1,241.4	1,277.4	1,486.3
Creditors	223.6	251.1	268.4	312.4
Provisions	11.8	17.3	18.5	21.6
Other Current Liabilities	338.4	593.7	644.0	749.7
Other Long Term Liabilities	13.3	11.6	12.4	14.4
Total Current Liabilities	573.8	862.2	930.9	1,083.7
Net Current Assets	331.1	433.2	373.1	638.6
Total Assets	1,696	1,856	2,015	2,273

Source: Company, ICICI Direct Research

Exhibit 15: Key ratios				
(Year-end March)	FY19	FY20	FY21E	FY22E
Per Share Data				
EPS (Fully Diluted)	18.7	16.0	14.8	18.0
Cash EPS	30.7	29.7	26.9	34.1
BV	100.6	115.5	130.0	147.4
Operating Ratios				
EBITDA / Net Sales	20.0	21.7	18.5	19.0
PAT / Net Sales	12.3	10.0	8.7	9.1
Inventory Days	16	20	20	20
Debtor Days	40	77	70	70
Creditor Days	38	41	41	41
Return Ratios				
RoE	18.6	13.9	11.4	12.2
RoCE	19.0	19.0	16.6	16.3
RoIC	26.5	28.6	29.1	28.5
Valuation Ratios				
EV / EBITDA	9.0	7.7	8.5	6.7
P/E	13.7	16.0	17.4	14.3
EV / Net Sales	1.8	1.7	1.6	1.3
Market Cap / Sales	1.7	1.6	1.5	1.3
Price to Book Value	2.6	2.2	2.0	1.7
Turnover Ratios				
Asset turnover	1.3	1.2	1.2	1.2
Gross Block Turnover	2.1	1.9	1.8	1.8
Solvency Ratios				
Debt / Equity	0.2	0.1	0.1	0.1
Current Ratio	1.5	1.4	1.4	1.4
Debt / EBITDA	0.6	0.4	0.4	0.3
Quick Ratio	1.4	1.3	1.2	1.2

Source: Company, ICICI Direct Research

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Sell: <-15%



Pankaj Pandey

Head – Research

pankaj.pandey@icicisecurities.com

**ICICI Direct Research Desk,
ICICI Securities Limited,
1st Floor, Akruiti Trade Centre,
Road No 7, MIDC,
Andheri (East)
Mumbai – 400 093
research@icicidirect.com**

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