



3R MATRIX

	+	=	-
Right Sector (RS)	✓	■	■
Right Quality (RQ)	✓	■	■
Right Valuation (RV)	✓	■	■
	+ Positive	= Neutral	- Negative

What has changed in 3R MATRIX

	Old		New
RS	■	↔	■
RQ	■	↔	■
RV	■	↔	■

ESG Disclosure Score NEW

ESG RISK RATING	38.82			
Updated Jan 08, 2022				
High Risk				
NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

Company details

Market cap:	Rs. 8,683 cr
52-week high/low:	Rs. 344 / 189
NSE volume: (No of shares)	2.2 lakh
BSE code:	532942
NSE code:	KNRCON
Free float: (No of shares)	13.6 cr

Shareholding (%)

Promoters	51.5
FII	4.6
DII	34.0
Others	9.9

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-1.7	3.5	4.0	40.7
Relative to Sensex	3.4	7.1	-0.6	29.1

Sharekhan Research, Bloomberg

Infrastructure	Sharekhan code: KNRCON		
Reco/View: Buy	↔	CMP: Rs. 309	Price Target: Rs. 370 ↑
↑ Upgrade	↔ Maintain	↓ Downgrade	

Summary

- KNR Construction Limited (KNR) reported lower-than-expected execution for Q3FY2022; OPM surprised positively; Sale of stake in couple of projects boosts net earnings; Net working capital days reduced sequentially.
- Management expects FY2022 and FY2023 revenue at Rs. 3,100 crore and Rs. 3,500 crore, respectively. Management expects Rs. 2,000 crore-4,000 crore order inflows for Q4. FY2023 order intake conservatively pegged at Rs. 3,500 crore.
- Pending receivable reduced by Rs. 380 crore q-o-q. Standalone cash strong at Rs. 407 crore.
- We retain our Buy rating on KNR with a revised PT of Rs. 370, considering strong industry growth tailwinds.

KNR Constructions Limited (KNR) reported lower-than-expected standalone revenue at Rs. 766 crore for Q3FY2022 (up 11.7% y-o-y, affected by extended monsoon and COVID-19 third wave). Operating profit margin (OPM) stood at 20.7% (+103 bps y-o-y), higher than our estimate. Operating profit rose by 17.5% y-o-y at Rs. 159 crore although lower other income (down 71% y-o-y), which led to standalone adjusted net profit growth of 2.3% y-o-y at Rs. 79.4 crore (adjusted for Rs. 21 crore gain on transfer of 49% stake in couple of HAM projects to Cube Highways). The company achieved strong order inflows of Rs. 4,000 crore during 9MFY2022 and expects to bag another Rs. 2,000 crore-4,000 crore orders in Q4FY2022. The company conservatively pegged order intake for FY2023 at Rs. 3,500 crore. Management expects Rs. 3,100 crore and Rs. 3,500 crore standalone revenue for FY2022 and FY2023, respectively.

Key positives

- OPM at 20.7% was up 103 bps y-o-y, higher than our estimate.
- Net working capital fell q-o-q to 40 days in Q3FY2022 from 45 days in Q2FY2022.

Key negatives

- Sale of couple of HAM projects to Cube Highways to reduce debt by Rs. 1,185 crore at consolidated level.
- Execution was lower than expectation, affected by extended monsoons and COVID impact.

Management Commentary

- The company transferred 49% stake in two HAM projects to Cube Highways at an equity value of Rs. 338 crore versus Rs. 288 crore equity invested yielding 1.2x P/B.
- The company's order book at the end of December 2021 was Rs. 10,090 crore comprising 74% share of EPC and HAM and 26% irrigation. Third-party clients comprised 58% share.
- Standalone cash and cash equivalents stand at Rs. 407 crore and working capital at 40 days. Consolidated debt stood at Rs. 1,374 crore with consolidated net debt to equity at 0.4x.
- Pending receivables stand at Rs. 590 crore in Q3FY2022 versus Rs. 700 crore in Q2FY2022. The company received Rs. 380 crore in Q3FY2022.

Revision in estimates – We have fine tuned our estimates for FY2022-FY2024.

Our Call

Valuation – Retain Buy with a revised PT of Rs. 370: KNR is expected to witness improvement in execution with better operating margins going ahead. Order inflow outlook remains healthy with the government's Gati Shakti Programme emphasising on speeding up infrastructure construction in the country. The company's standalone and consolidated balance sheet continues to remain strong. The company's strong order book and healthy bidding pipeline provide comfort. We expect KNR to be one of the key beneficiaries in the roads sector, given the government's investment plans in the next five years. We retain our Buy recommendation with a revised price target (PT) of Rs. 370.

Key Risks

Delay in execution and a weak macroeconomic environment will lead to lull in new project awards.

Valuation (Standalone)

Particulars	Rs cr			
	FY21	FY22E	FY23E	FY24E
Revenue	2,702.6	3,074.0	3,621.0	4,286.5
OPM (%)	19.8	20.5	19.1	19.2
Adjusted PAT	255.4	336.4	410.5	503.5
% YoY growth	8.3	31.7	22.0	22.7
Adjusted EPS (Rs.)	9.1	12.0	14.6	17.9
P/E (x)	34.0	25.8	21.2	17.2
P/B (x)	4.5	3.9	3.3	2.8
EV/EBITDA (x)	15.3	13.0	11.8	9.9
RoNW (%)	14.5	16.6	17.2	17.8
RoCE (%)	15.3	17.4	17.9	18.4

Source: Company; Sharekhan estimates

Execution lower than estimate; OPM surprised positively

KNR reported 11.7% y-o-y rise (+1.4% q-o-q) in standalone net revenue at Rs. 766 crore, which was lower than our estimate. Lower execution was on account of extended monsoon and impact of COVID-19 third wave. OPM at 20.7% (+103 bps y-o-y, -144 bps q-o-q) was higher than our estimate. Hence, operating profit grew by 17.5% y-o-y (down 5.2% q-o-q) to Rs. 158.9 crore, which was marginally lower than our estimate. The company provided for Rs. 21 crore profit on transfer of 49% stake in two of its road assets to Cube Highways, which led to standalone net profit growth of Rs. 30% y-o-y at Rs. 101 crore. Adjusting for the same, adjusted net profit was up 2.3% y-o-y at Rs. 79 crore. The company's standalone net working capital days reduced to 40 days in Q3FY2022 versus 45 days in Q2FY2022. Order book stands strong at Rs. 10,774 crore, 3.4x TTM standalone revenue.

Management outlook positive

The company retained Rs. 3,100 crore revenue target for FY2022, while it expects Rs. 3,500 crore revenue for FY2023. The company received Rs. 4,000 crore order inflows during 9MFY2022, while it expects to bag another Rs. 2,000 crore-4,000 crore in Q4FY2022. The company has conservatively set order inflow target of Rs. 3,500 crore for FY2023. The company has submitted bids for three HAM and one EPC project having average ticket size of Rs. 1,000 crore-1,200 crore. The company may receive Rs. 10 crore claim for Patel KNR project and Rs. 9 crore early completion bonus, which may lead to higher OPM in Q4FY2022. The company's order book at the end of December 2021 was Rs. 10,090 crore, comprising 74% share of EPC and HAM and 26% irrigation. Third-party clients comprised 58% share.

Key conference call takeaways

- ◆ **Guidance:** The company retained Rs. 3,100 crore revenue target for FY2022. The company received Rs. 4,000 crore order inflows during 9MFY2022, while it expects to bag another Rs. 2,000 crore-4,000 crore in Q4FY2022. The company would target Rs. 3,500 crore for FY2023. The company has submitted bids for three HAM and one EPC project having average ticket size of Rs. 1,000 crore-1,200 crore. The company may receive Rs. 10 crore claim for Patel KNR project and Rs. 9 crore early completion bonus, which may lead to higher OPM in Q4FY2022. The company has conservatively set order inflow target of Rs. 3,500 crore for FY2023.
- ◆ **Budget infra push:** The government increased allocation towards MORTH to Rs. 1.9 lakh crore from Rs. 1.1 lakh crore. It would be developing 25,000 kms of highways and is undertaking five river linking projects.
- ◆ **Sector:** The government constructed 6,684 kms of highways during April 2021 to January 2022 as against 9,132 kms last year same period. Awards stood at 6,883 kms compared to 7,696 kms. Construction and awards were affected by COVID and extended monsoons.
- ◆ **HAM equity investment:** The company would be infusing Rs. 604 crore equity as follows – FY2022 - Rs. 132 crore, FY2023 - Rs. 252 crore, FY2024 - Rs. 132 crore, and FY2025 - Rs. 88 crore.
- ◆ **HAM divestment to Cube Highways:** The company transferred 49% stake in two HAM projects to Cube Highways at an equity value of Rs. 338 crore versus Rs. 288 crore equity invested yielding 1.2x P/B. It has received Rs. 245 crore in December 2021, while balance Rs. 93 crore would be received by June 2022. The transaction would lead to debt reduction of Rs. 1,185 crore.
- ◆ **Order book:** The company's order book at the end of December 2021 was Rs. 10,090 crore, comprising 74% share of EPC and HAM and 26% irrigation. Third-party clients comprised 58% share.
- ◆ **Debt and cash:** Standalone cash and cash equivalents stand at Rs. 407 crore and working capital stands at 40 days. Consolidated debt stood at Rs. 1.374 crore with consolidated net debt to equity at 0.4x.
- ◆ **Receivables:** Pending receivables stand at Rs. 590 crore in Q3FY2022 versus Rs. 700 crore in Q2FY2022. The company received Rs. 380 crore in Q3FY2022.
- ◆ **Capex:** The company incurred Rs. 130 crore capex in 9MFY2022. Capex for FY2022 and FY2023 is expected to be Rs. 180 crore and Rs. 150 crore-160 crore, respectively.
- ◆ **Other highlights:** Retention receivables stand at Rs. 157 crore, mobilisation advance at Rs. 120 crore, and unbilled revenue of Rs. 257 crore.

Financials (Standalone)

	Rs cr				
Result table	Q3FY2022	Q3FY2021	y-o-y%	Q2FY2022	q-o-q%
Net revenue	766.3	686.3	11.7%	755.6	1.4%
Other income	7.8	26.6	-70.5%	10.5	-25.7%
Total income	774.1	712.8	8.6%	766.1	1.0%
Total expenses	607.4	551.0	10.2%	588.0	3.3%
Operating profit	158.9	135.3	17.5%	167.5	-5.2%
Depreciation	35.8	37.3	-4.0%	32.0	12.1%
Interest	6.4	18.4	-65.5%	7.2	-11.7%
Exceptional items	21.4	0.0		0.0	
Profit Before Tax	146.0	106.1	37.6%	138.9	5.1%
Taxes	45.2	28.5	58.4%	43.7	3.5%
PAT	100.8	77.6	29.9%	95.2	5.8%
Adjusted PAT	79.4	77.6	2.3%	95.2	-16.7%
EPS (Rs.)	2.8	2.8	2.3%	3.4	-16.7%
			BPS		BPS
OPM (%)	20.7%	19.7%	103 bps	22.2%	-144 bps
NPM (%)	10.4%	11.3%	-95 bps	12.6%	-225 bps
Tax rate (%)	31.0%	26.9%	407 bps	31.4%	-47 bps

Source: Company; Sharekhan Research

Outlook and Valuation

■ Sector outlook – Roads to remain one of the key focus areas in government’s infrastructure spending

The government’s infrastructure investment is pegged at Rs. 111 lakh crore over FY2020-FY2025. The road sector is expected to witness Rs. 20 lakh crore investments during the same period. Huge investments and favourable government policies are expected to provide strong growth opportunities for players. The roads sector is recovering with near pre-COVID level manpower strength and availability of materials post easing of restrictions post COVID-19 led lockdowns. The industry is expected to see strong order inflows and improved execution run-rate from Q3FY2021. Working capital issues of the companies have been handled by proactive payments from the NHAI.

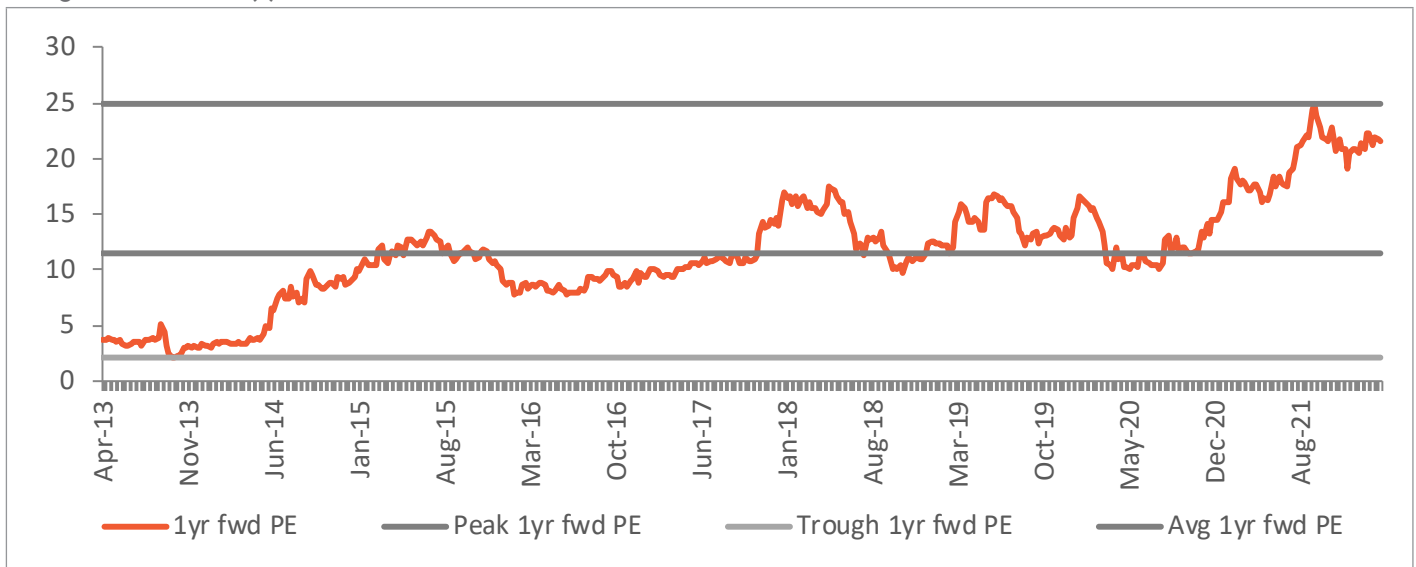
■ Company outlook – Strong order backlog provides comfort

The company is targeting Rs. 3,100 crore revenue for FY2022 and Rs. 3,500 crore for FY2023. Order inflow during 9MFY2022 remained healthy at Rs. 4,000 crore. Currently, it has four bids in roads with average ticket size of Rs. 1,000 crore-1,200 crore. The company targets to bag Rs. 2,000 crore-4000 crore order inflows in the balance fiscal year. The company has a strong order backlog at 4x its TTM standalone revenue, providing strong revenue visibility over the next two years. Standalone and consolidated balance sheet continues to remain strong. Conclusion of Cube Highways deal will further free up equity for future project infusions. A strong order book and healthy bidding pipeline provide comfort.

■ Valuation – Retain Buy with a revised PT of Rs. 370

KNR is expected to witness improvement in execution with better operating margins going ahead. Order inflow outlook remains healthy with the government’s Gati Shakti Programme emphasising on speeding up infrastructure construction in the country. The company’s standalone and consolidated balance sheet continues to remain strong. The company’s strong order book and healthy bidding pipeline provide comfort. We expect KNR to be one of the key beneficiaries in the roads sector, given the government’s investment plans in the next five years. We retain our Buy recommendation with a revised PT of Rs. 370.

One-year forward P/E (x) band



Source: Sharekhan Research

Peer Comparison

Particulars	P/E (x)		EV/EBITDA (x)		RoE (%)		RoE (%)	
	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E
PNC Infratech	12.1	10.7	6.8	6.2	1.7	1.5	15.6	15.2
KNR Constructions	21.2	17.2	11.8	9.9	3.3	2.8	17.2	17.8

Source: Sharekhan Research

About the company

Incorporated in 1995, KNR has over two decades of experience in project execution. The company is one of the leading companies providing engineering, procurement, and construction (EPC) services, majorly concentrated in the roads and highways segment. The company also has a minor presence in the irrigation and urban water infrastructure management segments. Till date, KNR has successfully executed more than 6,000 lane km of road projects across 12 states in India.

Investment theme

KNR is one of the best managed road construction companies with more than two decades of experience executing over 6,000 lane km road projects across 12 states in India. KNR has in-house construction capabilities, which ensure on-schedule project completion (history of receiving early completion bonuses). KNR entered into a complete stake sale agreement with Cube Highways for four of its hybrid annuity projects, which will aid in lower equity requirement along with booking of EPC work with the possibility of receiving an early completion bonus.

Key Risks

- ◆ Delay in project execution of hybrid annuity projects.
- ◆ Slowdown in the macro-economy leading to muted road project awards from NHAI and Ministry of Road Transport.

Additional Data

Key management personnel

Mr. K. Narasimha Reddy	Founder Promoter & Managing Director
Mr. K. Jalandhar Reddy	Promoter & Executive Director
Mr. M.V. Venkata Rao	Company Secretary & Compliance Officer

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Reddy Kamidi Narasimha	32.5
2	Reddy Kamidi Jalandhar	14.0
3	ICICI Prudential Asset Management	7.4
4	DSP Investment Managers Pvt. Ltd.	6.9
5	HDFC Asset Management Co. Ltd.	6.4
6	YASHODA KAMIDI	4.3
7	Reddy Mereddy Rajesh	4.3
8	UTI Asset Management Co. Ltd.	2.2
9	Franklin Resources Inc.	2.0
10	Invesco Asset Management India Pvt. Ltd.	1.9

Source: Bloomberg

Sharekhan Limited, its analyst or dependant(s) of the analyst might be holding or having a position in the companies mentioned in the article.

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and deteriorating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

Sharekhan

by BNP PARIBAS

Know more about our products and services

For Private Circulation only

Disclaimer: This document has been prepared by Sharekhan Ltd. (SHAREKHAN) and is intended for use only by the person or entity to which it is addressed to. This Document may contain confidential and/or privileged material and is not for any type of circulation and any review, retransmission, or any other use is strictly prohibited. This Document is subject to changes without prior notice. This document does not constitute an offer to sell or solicitation for the purchase or sale of any financial instrument or as an official confirmation of any transaction. Though disseminated to all customers who are due to receive the same, not all customers may receive this report at the same time. SHAREKHAN will not treat recipients as customers by virtue of their receiving this report.

The information contained herein is obtained from publicly available data or other sources believed to be reliable and SHAREKHAN has not independently verified the accuracy and completeness of the said data and hence it should not be relied upon as such. While we would endeavour to update the information herein on reasonable basis, SHAREKHAN, its subsidiaries and associated companies, their directors and employees ("SHAREKHAN and affiliates") are under no obligation to update or keep the information current. Also, there may be regulatory, compliance, or other reasons that may prevent SHAREKHAN and affiliates from doing so. This document is prepared for assistance only and is not intended to be and must not alone be taken as the basis for an investment decision. Recipients of this report should also be aware that past performance is not necessarily a guide to future performance and value of investments can go down as well. The user assumes the entire risk of any use made of this information. Each recipient of this document should make such investigations as it deems necessary to arrive at an independent evaluation of an investment in the securities of companies referred to in this document (including the merits and risks involved), and should consult its own advisors to determine the merits and risks of such an investment. The investment discussed or views expressed may not be suitable for all investors. We do not undertake to advise you as to any change of our views. Affiliates of Sharekhan may have issued other reports that are inconsistent with and reach different conclusions from the information presented in this report.

This report is not directed or intended for distribution to, or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject SHAREKHAN and affiliates to any registration or licensing requirement within such jurisdiction. The securities described herein may or may not be eligible for sale in all jurisdictions or to certain category of investors. Persons in whose possession this document may come are required to inform themselves of and to observe such restriction.

The analyst certifies that the analyst has not dealt or traded directly or indirectly in securities of the company and that all of the views expressed in this document accurately reflect his or her personal views about the subject company or companies and its or their securities and do not necessarily reflect those of SHAREKHAN. The analyst and SHAREKHAN further certifies that neither he or his relatives or Sharekhan associates has any direct or indirect financial interest nor have actual or beneficial ownership of 1% or more in the securities of the company at the end of the month immediately preceding the date of publication of the research report nor have any material conflict of interest nor has served as officer, director or employee or engaged in market making activity of the company. Further, the analyst has also not been a part of the team which has managed or co-managed the public offerings of the company and no part of the analyst's compensation was, is or will be, directly or indirectly related to specific recommendations or views expressed in this document. Sharekhan Limited or its associates or analysts have not received any compensation for investment banking, merchant banking, brokerage services or any compensation or other benefits from the subject company or from third party in the past twelve months in connection with the research report.

Either, SHAREKHAN or its affiliates or its directors or employees / representatives / clients or their relatives may have position(s), make market, act as principal or engage in transactions of purchase or sell of securities, from time to time or may be materially interested in any of the securities or related securities referred to in this report and they may have used the information set forth herein before publication. SHAREKHAN may from time to time solicit from, or perform investment banking, or other services for, any company mentioned herein. Without limiting any of the foregoing, in no event shall SHAREKHAN, any of its affiliates or any third party involved in, or related to, computing or compiling the information have any liability for any damages of any kind.

Compliance Officer: Mr. Joby John Meledan; Tel: 022-61150000; email id: compliance@sharekhan.com;

For any queries or grievances kindly email igc@sharekhan.com or contact: myaccount@sharekhan.com

Registered Office: Sharekhan Limited, 10th Floor, Beta Building, Lodha iThink Techno Campus, Off. JVLR, Opp. Kanjurmarg Railway Station, Kanjurmarg (East), Mumbai – 400042, Maharashtra. Tel: 022 - 61150000. Sharekhan Ltd.: SEBI Regn. Nos.: BSE / NSE / MSEI (CASH / F&O / CD) / MCX - Commodity: INZ000171337; DP: NSDL/CDSL-IN-DP-365-2018; PMS: INP000005786; Mutual Fund: ARN 20669; Research Analyst: INH000006183;

Disclaimer: Client should read the Risk Disclosure Document issued by SEBI & relevant exchanges and the T&C on www.sharekhan.com; Investment in securities market are subject to market risks, read all the related documents carefully before investing.