Stock Update

Result Update

Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

KNR Constructions Ltd

Exploring new avenues for order wins

Infrastructure	Sharekhan code: KNRCON
Reco/View: Buy ↔	CMP: Rs. 242
	Price Target: Rs. 301 ↔

↑ Upgrade ↔ Maintain ↓ Downgrade

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 42.82

Updated Aug 08, 2023

Severe Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

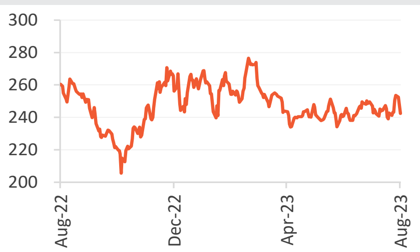
Company details

Market cap:	Rs. 6,819 cr
52-week high/low:	Rs. 281/203
NSE volume: (No of shares)	2.2 lakh
BSE code:	532942
NSE code:	KNRCON
Free float: (No of shares)	13.8 cr

Shareholding (%)

Promoters	51.1
FII	6.0
DII	33.7
Others	9.3

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-1.8	-1.6	-4.6	-6.9
Relative to Sensex	-0.2	-7.4	-11.5	-16.4

Sharekhan Research, Bloomberg

Summary

- Q1FY24 standalone numbers were broadly in-line driven by execution of HAM projects. Standalone net working capital cycle shrunk q-o-q, while it maintains net cash surplus position.
- Management retained a guidance of Rs. 4,000-crore in standalone revenues and Rs. 4000-5000 crore of order inflows for FY2024. OPM may get hit if irrigation payments are not received timely.
- Order book at 2.1x TTM including recent wins remains healthy. It continues to explore for projects in state highways, irrigation, urban infrastructure, railways and Metro Rail segments.
- We retain Buy on KNR with an unchanged PT of Rs. 301, considering healthy earnings growth outlook led by positive sector growth outlook.

KNR Constructions Limited (KNR) reported broadly in-line standalone performance for Q1FY2024. Standalone revenue growth of 4.4% y-o-y at Rs. 930 crore (5% lower than our estimate) was aided by HAM projects execution (45% revenue share). Standalone OPM at 18.6% (almost flat y-o-y) came in a tad below our estimate of 18.8%. Standalone operating profit marginally increased by 5% y-o-y at Rs. 173 crores. Further, lower depreciation (down 13% y-o-y) aided 9.3% y-o-y growth in standalone net profit at Rs. 110 crore. Including the three recent HAM project wins, its order book remains healthy at Rs. 8,045 crores (2.1x TTM standalone revenue). The company retained Rs. 4000 crore standalone revenue target for FY2024 and order inflow target of Rs. 4000-5000 crore. However, OPM may come in lower by 2-3% if irrigation payments gets stalled due to upcoming elections. Apart from roads, it is eyeing opportunities for projects in the Irrigation (Telangana, MP, Rajasthan), Pipeline (Rajasthan), tunnel (North East) and is under discussions with Patel Engineering, NCC and HW to diversify into other segments of infrastructure development.

Key positives

- Broadly in-line standalone performance driven by HAM project execution and stable OPMs y-o-y.
- Retained standalone revenue and order inflow guidance for FY2024. It is eyeing opportunities in Irrigation, Pipeline and Tunnel projects through JVs.

Key negatives

- Standalone OPM for FY2024 can negatively impacted if it is not able to received Irrigation payments on time due to state elections.
- Irrigation receivables stay high at Rs. 690 crore as funds receipt were offset by work done but not certified.

Management Commentary

- Company retained Rs. 4000 crore standalone revenue growth guidance for FY2024. However, OPMs may be lower by 2-3% than earlier guided if irrigation payments gets stalled due to upcoming elections. The order inflow target for FY2024 is maintained at Rs. 4000-5000 crore for FY2024.
- It has a visible pipeline of Rs. 49000 crore across segments. NHAI pipeline is Rs. 45000 crore of which it has selected Rs. 20,000-25,000 crore. It is looking at Irrigation projects of Rs. 45,000 crore. It is in discussion with Patel Engineering, NCC and HW to explore JV in Pipeline, tunnel projects etc.
- The company has infused Rs. 404 crore out of total equity requirement of Rs. 732.86 crore in existing five HAM projects. The equity requirement for newly bagged three HAM projects is Rs. 225 crore.

Revision in estimates – We have retained our net earnings estimates for FY2024-FY2025.

Our Call

Valuation – Retain Buy with an unchanged PT of Rs. 301: KNR is expected to benefit from the government's infrastructure spending, especially on roads and highways. However, in the near term, the company faces a highly competitive environment along with delays in opening up of bids. However, its order book remains healthy, providing revenue visibility over the next two years. Additionally, it is looking at other sectors, such as state highway projects, irrigation, urban infrastructure, railways and metros, which can provide growth. The company's de-leveraged balance sheet and contained outstanding receivables in irrigation provide comfort. We retain our Buy rating on the stock with an unchanged price target (PT) of Rs. 301, considering healthy earnings growth outlook led by positive sector growth outlook.

Key Risks

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

Valuation (Standalone) Rs cr

Particulars	FY22	FY23	FY24E	FY25E
Revenue	3,272.6	3,743.8	3,990.4	4,323.6
OPM (%)	20.7	19.3	18.6	18.5
Adjusted PAT	360.4	360.9	435.7	471.2
% YoY growth	41.1	0.1	20.7	8.1
Adjusted EPS (Rs.)	12.8	12.8	15.5	16.8
P/E (x)	18.9	18.9	15.6	14.5
P/B (x)	3.0	2.4	2.1	1.9
EV/EBITDA (x)	9.3	8.8	8.5	7.9
RoNW (%)	17.5	14.5	14.8	13.9
RoCE (%)	18.5	15.7	15.6	14.6

Source: Company; Sharekhan estimates

Broadly in-line performance

Standalone net revenues growth of 4.4% y-o-y (-20.9% q-o-q) at Rs. 930 crore which was 5% lower than our estimate. Standalone OPM at 18.6% (+11 bps y-o-y, +61 bps q-o-q) was in-line with our estimate of 18.8%. Standalone operating profit increased by 5% y-o-y (down 18.3% q-o-q) to Rs. 173 crore which was 6% lower than our estimate. Lower depreciation (down 13% y-o-y) and lower interest cost (down 28% y-o-y) partially offset by lower other income (down 22% y-o-y) leading to a 9% y-o-y growth in standalone PAT at Rs. 110 crore (down 14% y-o-y). The company's net working capital reduced by 5 days q-o-q to 62 days. Its order book stands at Rs. 8045 crore (2.1x TTM standalone revenues).

Key conference call takeaways

- **Guidance:** The company retained a Rs. 4,000 crore standalone revenue growth guidance for FY2024. However, OPMs may be lower by 2-3% than earlier guided if irrigation payments gets stalled due to upcoming elections. Order inflow target for FY2024 is maintained at Rs. 4000-5000 crore for FY2024.
- **Bid pipeline:** It has a visible pipeline of Rs. 49000 crore across segments. NHAI pipeline is Rs. 45000 crore of which it has selected Rs. 20,000-25,000 crore. It is looking at Irrigation projects of Rs. 45,000 crore. It is looking at irrigation bids in Telangana (Rs. 3500 crore), M.P. (Rs. 2900 crore) and Rajasthan (Rs. 2,000 crore). It has placed few bids in Tamil Nadu by NHAI which has not opened yet. It is looking at pipeline projects in Rajasthan and tunnel projects in North East. It is in discussion with Patel Engineering, NCC and HCW to explore JV in Pipeline, tunnel projects etc. It is also trying to enter into MSRDC projects like metros, urban infrastructure etc.
- **Q1FY2024 performance:** Standalone revenues increased by 4% y-o-y at Rs. 930 crore with HAM projects driving execution. Irrigation revenues stood at Rs. 200 crore, 45% revenue contribution was from HAM projects and 27% Road EPC. Standalone EBITDA grew 5% y-o-y at Rs. 173 crore with a margin of 18.6% while net profit was up 9% y-o-y at Rs. 110 crore. The consolidated revenue was almost flat y-o-y at Rs. 981 crore, EBITDA stood at Rs. 216 crore vs Rs. 211 crore in Q1FY2023 with OPM of 22% and net profit was Rs. 133 crore vs Rs. 91 crore in Q1FY2023. As on June, the order book stood at Rs. 6265 crore, while including the newly bagged three HAM projects, the order book stands at Rs. 8045 crore, providing a revenue visibility over the next two years.
- **Industry update:** NHAI awarding remained muted at 2,000 kms for Q1FY2024 while it targets to award 8500-9000 kms in FY2024 with expected pick-up in awarding from H2FY2024. NHAI looks at monetising two highway projects totalling Rs. 6000 crore through ToT route. It has set a target of monetising Rs. 45000 crore in FY2024. The toll collections from NHAI projects during April, May and June stood at Rs. 4,300 crore, Rs. 4,500 crore and Rs. 4,300 crore respectively.
- **Equity requirement:** The company has infused Rs. 404 crore out of total equity requirement of Rs. 732.86 crore in existing five HAM projects. The balance Rs. 330 crore will be infused as follows – Rs. 146 crore in FY2024, Rs. 161 crore in FY2025 and balance in FY2026. The equity requirement for newly bagged three HAM projects is Rs. 225 crore of which 50% would be infused in FY2025 and 25% each in FY2026 and FY2027.
- **Receivables:** The pending receivables (billed and unbilled) from Telangana government stands at Rs. 690 crore. It had received Rs. 180 crore from April onwards for package III irrigation project from Telangana. Total receivables is Rs. 880 crore of which Rs. 650 crore is HAM receivables.
- **Capex:** it incurred capex of Rs. 33 crore in Q1 and targets Rs. 100-120 crore for FY2024. FY2025 capex would depend on the order inflows during the current year.
- **Debt:** Standalone debt is nil and cash is Rs. 85 crores. Consolidated debt is Rs. 575 crore and cash Rs. 100 crore.

Results (Standalone) **Rs cr**

Particulars	Q1FY24	Q1FY23	Y-o-Y %	Q4FY23	Q-o-Q %
Net revenue	**929.6**	**890.6**	**4.4%**	**1175.6**	**-20.9%**
Other income	7.1	9.1	-22.1%	9.6	-26.0%
Total income	**936.7**	**899.7**	**4.1%**	**1185.2**	**-21.0%**
Total expenses	756.3	725.6	4.2%	963.6	-21.5%
Operating profit	**173.3**	**165.0**	**5.0%**	**211.9**	**-18.3%**
Depreciation	28.3	32.7	-13.3%	40.1	-29.2%
Interest	5.0	6.9	-27.5%	8.0	-37.0%
Exceptional items	0.0	0.0		0.0	
Profit Before Tax	**147.0**	**134.5**	**9.3%**	**173.5**	**-15.3%**
Taxes	36.7	33.6	9.2%	44.9	-18.2%
PAT	110.3	100.8	9.3%	128.6	-14.3%
Adjusted PAT	**110.3**	**100.8**	**9.3%**	**128.6**	**-14.3%**
EPS (Rs.)	3.9	3.6	9.3%	4.6	-14.3%
			BPS		**BPS**
OPM (%)	18.6%	18.5%	11	18.0%	61
NPM (%)	11.9%	11.3%	54	10.9%	92
Tax rate (%)	25.0%	25.0%	-3	25.9%	-89

Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector view - Roads to remain one of the key focus areas in the 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 after easing restrictions post COVID-19 led lockdowns. The industry expects strong order inflows and improved execution run-rate from Q3FY2021. Proactive payments from the NHAI have handled working capital issues of the companies.

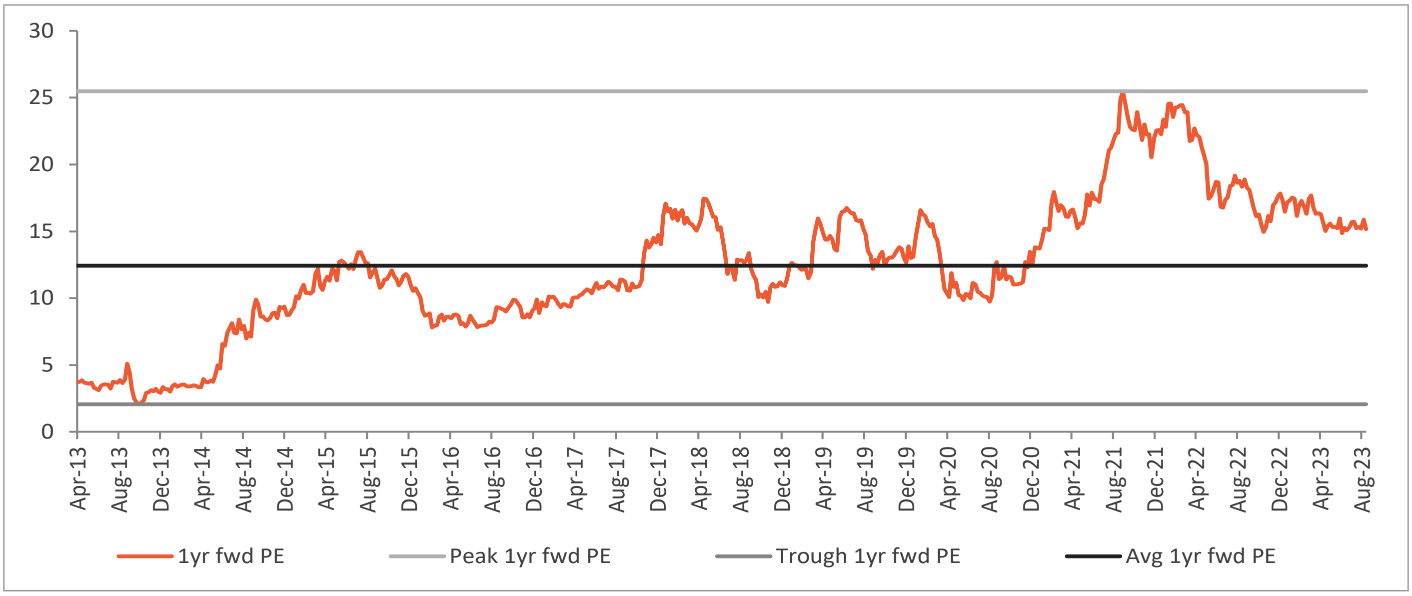
■ Company outlook - Well placed to gain from positive sector outlook

KNR is targeting Rs. 4,000-5,000 crore of order inflows for FY2024 due to cutthroat competition in NHAI bidding. However, it looks at other sectors, such as state highway projects, irrigation, urban infra, railways and metros, which can provide growth. The company targets to achieve Rs. 4,000 crore standalone revenue for FY2024 owing to a healthy order book. KNR remains prudent in bidding for projects in a highly competitive environment. The company has a healthy order backlog at almost 2.1x its TTM standalone revenue, providing healthy revenue visibility over the next two years. However, new project order wins going ahead would be a key monitorable. Its de-leverage balance sheet and contained irrigation receivables provide comfort.

■ Valuation - Retain Buy with an unchanged PT of Rs. 301

KNR is expected to benefit from the government's infrastructure spending, especially on roads and highways. However, in the near term, the company faces a highly competitive environment along with delays in opening up of bids. However, its order book remains healthy, providing revenue visibility over the next two years. Additionally, it is looking at other sectors, such as state highway projects, irrigation, urban infrastructure, railways and metros, which can provide growth. The company's de-leveraged balance sheet and contained outstanding receivables in irrigation provide comfort. We retain our Buy rating on the stock with an unchanged price target (PT) of Rs. 301, considering healthy earnings growth outlook led by positive sector growth outlook.

One-year forward P/E (x) band



Source: Sharekhan Research

Peer Comparison

Particulars	P/E (x)		EV/EBITDA (x)		P/BV (x)		RoE (%)	
	FY24E	FY25E	FY24E	FY25E	FY24E	FY25E	FY24E	FY25E
PNC Infratech	12.2	11.0	8.0	7.3	1.8	1.6	16.2	15.4
KNR Constructions	15.6	14.5	8.5	7.9	2.1	1.9	14.8	13.9

Source: Sharekhan Research, Standalone financials

About 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. To 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 requirements and 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 the Ministry of Road Transport.

Additional Data

Key management personnel

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

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Reddy Kamidi Narasimha	32.53
2	Reddy Kamidi Jalandhar	13.96
3	ICICI Prudential Asset Management	7.38
4	DSP Investment Managers Pvt. Ltd.	6.85
5	HDFC Asset Management Co. Ltd.	6.4
6	YASHODA KAMIDI	4.27
7	Reddy Mereddy Rajesh	4.27
8	UTI Asset Management Co. Ltd.	2.21
9	Franklin Resources Inc.	2
10	Invesco Asset Management India Pvt. Ltd.	1.91

Source: Bloomberg

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 detoriating 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

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