Narnolia™

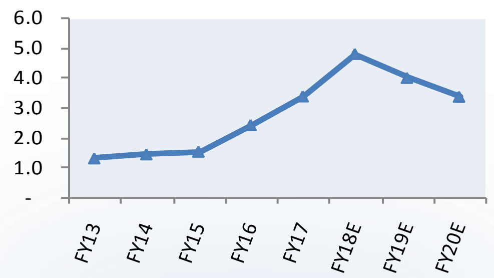
KEC
NEUTRAL
07-Feb-18

Bloomberg -	KECI IN
INDUSTRY -	Industrial
BSE Code -	532714
NSE Code -	KEC
NIFTY -	10498

Company Data

CMP	347
Target Price	**361**
Previous Target Price	290
Upside	**4%**
52wk Range H/L	395/152
Mkt Capital (Rs Cr)	8,943
Av. Volume (,000)	86

Tarding at 3.4x BVPS of FY20

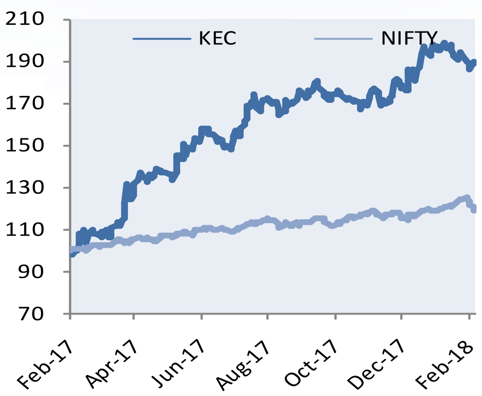


Shareholding patterns %

	3QFY18	2QFY18	1QFY18
Promoters	50.1	50.9	50.9
FII	10.3	10.3	7.2
DII	20.4	20.8	23.6
Public	19.2	17.9	18.3
Total	**100.0**	**100.0**	**100.0**

Stock Performance %

	1Mn	3Mn	1Yr
Absolute	(10.3)	11.9	125.7
Rel.to Nifty	(9.0)	10.1	105.3



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Key Highlights of the Report:

☑ KEC reported Q3FY18 earning numbers largely in line with our estimate. Top line was up by 25% YoY to Rs.2405 Cr (vs our estimate of Rs.2476 Cr) backed by strong execution across the segment.

☑ Order Inflow during the quarter manifold by 2x on account of robust International T&D orders. KEC has secured couple of big T&D orders from SAARC countries for construction of 132 kv D/C and 500 KV HVDC transmission line in Bangladesh and Afghanistan respectively.

☑ We estimate Revenue/Earning will grow by 11%/20% CAGR over FY17-20 backed by multifold revenue growth in railway and Civil segment.

☑ **KEC is in sweet spot to capitalize rising demand across the segment but considering the expensive valuation we are "NEUTRAL" on the stock with target price Rs.361 (3.5x FY20 book value).**

Financials/Valu	FY16	FY17	FY18E	FY19E	FY20E
Net Sales	8,710	8,755	9,376	11,084	12,133
EBITDA	692	818	923	1,087	1,196
EBIT	561	688	793	953	1,063
PAT	148	305	369	473	531
EPS (Rs)	6	12	14	18	21
EPS growth (%)	-8%	106%	21%	28%	12%
ROE (%)	11%	19%	20%	21%	20%
ROCE (%)	30%	29%	34%	36%	35%
BV	1,290	1,586	1,868	2,239	2,656
P/B (X)	2.4	3.4	4.8	4.0	3.4
P/E(X)	21.2	17.6	24.2	18.9	16.9

Recent Orders Win :-

✓ During the quarter KEC has secured large power T&D orders from SAARC countries for construction of 132 kv D/C and 500 KV HVDC transmission line in Bangladesh and Afghanistan respectively.

✓ SAE has secured EPC order worth of Rs.878 Cr and tower supply order of Rs.460 Cr during the quarter. Management has envisaged huge opportunities in power T&D projects in Brazil and KEC will continue to explore the market.

✓ On 19th Dec 2017 KEC has won one big from Indian Railways for electrification. Currently KEC is L1 in Orders worth Rs.4000 Cr and major orders are from Railways.

✓ During the quarter company has secured couple of Cable supply order worth Rs.227 Cr and one project to construct Auto and Tyre plant worth Rs.78 Cr.

Quarterly Performance

Financials	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	YoY %	QoQ%	FY16	FY17	YoY %
Sales	1,882	2,849	1,857	2,132	2,405	**28%**	**13%**	**8,708**	**8,755**	**1%**
Other Operating Income	30	-	-	-	-			192	-	**-100%**
Net Sales	**1,912**	**2,849**	**1,857**	**2,132**	**2,405**	**26%**	**13%**	**8,516**	**8,755**	**3%**
Other Income	7	11	10	6	12	76%	115%	10	29	**181%**
COGS	**843**	**1,479**	**826**	**1,033**	**1,172**	**39%**	**13%**	**4,148**	**4,165**	**0%**
Employee Expenses	186	186	191	195	192	3%	-2%	642	733	14%
Erection & Sub.	459	494	435	449	566	23%	26%	2,072	1,784	-14%
Other Expenses	243	389	228	240	231	-5%	-4%	975	1,085	11%
Total Expenditure	**1,730**	**2,548**	**1,680**	**1,916**	**2,161**	25%	13%	**7,837**	**7,937**	1%
EBITDA	**182**	**301**	**176**	**216**	**244**	**34%**	**13%**	**679**	**818**	**20%**
EBITDA M%	**9.5**	**10.6**	**9.5**	**10.1**	**10.2**			**8.0**	**9.3**	
Depreciation	30	41	27	28	27	-9%	-3%	88	130	**48%**
EBIT	**152**	**260**	**149**	**188**	**217**	**43%**	**15%**	**592**	**688**	**16%**
Intreset	58	64	63	57	61	4%	6%	277	254	**-9%**
Exceptional Item	-	-	-	-	-			-	-	
PBT	**101**	**208**	**96**	**136**	**169**	**68%**	**24%**	**325**	**463**	**43%**
Tax	38	63	33	47	57	49%	21%	133	159	19%
PAT	**63**	**146**	**63**	**89**	**112**	**79%**	**25%**	**192**	**294**	**54%**

Q3FY18 Result:- In line with our Expectation

- ✓ KEC reported Q3FY18 earning numbers largely in line with our estimate. Top line was up by 25% YoY to Rs.2405 Cr (vs our estimate of Rs.2476 Cr) backed by strong execution across the
- ✓ Revenue from Cabel business was impacted due to higher GST rate. But GST committee has cut down the rate and management expects recovery in business. Solar business was impacted due to GST.
- ✓ EBITDA margin was flat YoY to 9.5% on adjusted basis. EBITDA was higher by 34% YoY to Rs.244 Cr on back of strong revenue growth.
- ✓ Interest cost as % of sales remained under control at 2.5% which is in line with our estimate. However, Debt has gone up due to delay in payment. Payment from one of the T&D project should have been received in Q3FY18 but will be come in January. Debt level will be normalizing by the year end.
- ✓ KEC posted strong PAT growth of 78% YoY to Rs.112 Cr ahead of our estimate of Rs.98 Cr.

Segment Revenue	4QFY16	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	YoY%	QoQ%
Transmission	1,915	1,184	1,529	1,273	2,043	1,334	1,709	1,532	**20%**	**-10%**
Transmission SAE	266	255	261	227	259	151	248	319	**41%**	**29%**
Cables	326	245	228	278	303	220	239	272	**-2%**	**14%**
Railway	50	70	66	105	206	158	119	208	**98%**	**75%**
Civil/Water	37	18	19	20	28	15	40	87	**335%**	**118%**
Telecom	-	-	-	-	-	-	-	-		
Solar	52	14	26	59	60	21	44	34	**-42%**	**-23%**
Total	**2,646**	**1,786**	**2,129**	**1,962**	**2,899**	**1,899**	**2,399**	**2,452**	**25%**	**2%**

Detailed Order book

Order Book	4QFY16	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	YoY%	QoQ%
Transmission	1,507	1,469	1,851	1,947	2,395	2,093	1,833	3,443	77%	88%
SAE	1,134	1,769	1,510	1,342	1,263	1,218	2,102	1,715	28%	-18%
Cables	472	104	216	224	126	271	280	343	53%	22%
Railways	567	936	1,186	1,342	1,516	1,353	1,401	3,601	168%	157%
Civil/Water	189	208	216	112	126	406	420	343	207%	-18%
Solar	38	52	216	112	505	406	280	343	207%	22%
Total	**9,449**	**10,403**	**10,785**	**11,186**	**12,631**	**13,532**	**14,013**	**17,148**	**53%**	**22%**

Order Inflow manifold by 2x backed by robust International T&D business

- ✓ Order Inflow during the quarter manifold by 2x on account of robust International T&D orders. KEC has secured couple of big T&D orders from SAARC countries for construction of 132 kv D/C and 500 KV HVDC transmission line in Bangladesh and Afghanistan respectively.
- ✓ SAE has secured new EPC order worth of Rs.878 Cr and tower supply order of Rs.460 Cr during the quarter. Management has envisaged huge opportunities in power T&D projects in Brazil and KEC will continue to explore the market.
- ✓ Current Order stands at Rs.17148 Cr which is 1.8x of TTM revenue along with Rs. 4000 Cr of orders in L1 position. 70% of L1 orders are from India and major of this from railway segment.

Order Inflow during the quarter grew by 105% YoY led by International T&D.

Order Inflow	4QFY16	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	YoY%	QoQ%
Transmission	1,507	1,469	1,851	1,947	2,395	2,093	1,833	3,443	77%	88%
SAE	206	678	211	61	657	140	562	1,055	1643%	88%
Cables	138	198	336	244	212	335	325	611	151%	88%
Railways	12	424	584	460	15	-	59	111	-76%	88%
Civil/Water	-	-	-	-	-	223	148	278		88%
Solar	38	57	121	5	445	-	30	56	976%	88%
Total	**1,877**	**2,825**	**3,103**	**2,706**	**3,724**	**2,790**	**2,957**	**5,553**	105%	88%

Concall Highlights:

- ✓ Expect double digit revenue growth in FY19.
- ✓ Rs.2500 Cr of order in SAE order book will start converting into revenue from November 2018 onwards.
- ✓ Growth in order inflow from Brazil will be much higher compared to current growth going ahead.
- ✓ Management is eyeing on International market for railway business.
- ✓ Expect railway segment top line will be Rs.1500-1600 Cr in FY19.
- ✓ Currently debt level has gone up due to delay in payment from Saudi and one of T&D project in north east. But debt will be come down to March 2017 level.
- ✓ Currently, 49% of Domestic T&D order book is from PGCIL. Southern SEBs will continue to lead order momentum.
- ✓ Expect 50 bps improvements in EBITDA margin in FY19.
- ✓ 70% of L1 orders are from Indian market and major orders are from railway business.
- ✓ FY18 revenue growth will be 10-15%
- ✓ Interest as % of sales will continue to be in range of 2.5-2.7%.
- ✓ Competitive intensity in railway has come down from road developers as the mega project of Bharatmala ids coming up.
- ✓ Rs.1000 Cr of receivables is pending from Saudi.

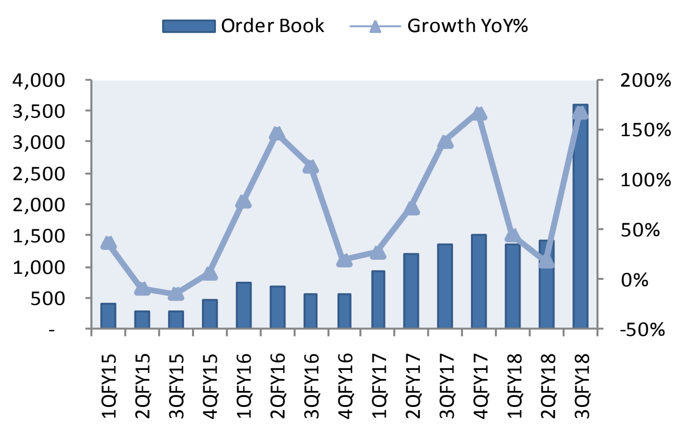
Investment Rational:

- ✓ **Railway and Civil business a key revenue growth driver:-** Company has continuously diversified its business into Railway, Solar and Civil to leverage its strong execution capabilities and we expect that the railway and civil will be the new growth drivers for the company along with strong hold in T&D business. Railway Ministry's increased focused on electrification of railway line ensures the healthy order inflow. Currently, KEC stand L1 in Rs.4000 Cr of orders, out of this major orders are from railway segment. Management is also eyeing railway electrification projects in international market and currently doing couple of projects. Management is also planning to extend its offering in civil business to residential buildings projects, affordable housing and civil work for defense.

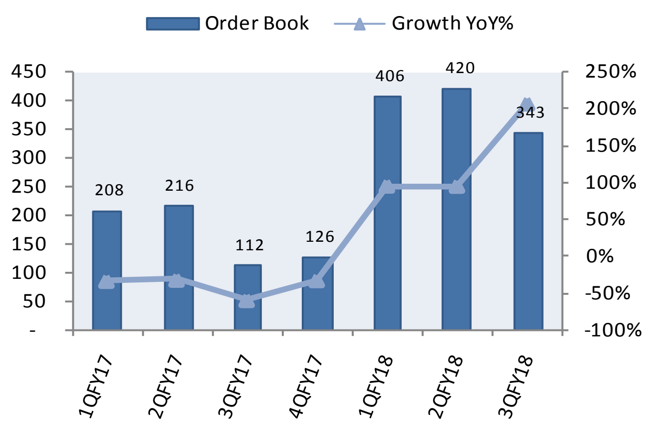
- ✓ **Strong Order Pipeline:-** Brazil will be the next big market for the power T&D projects as the Brazilian government has a capex plan of USD 4Bn for improving transmission networks. SAE, wholly owned subsidiary of the company is well placed to garb the opportunity. Rs.2500 Cr of orders in SAE order book will start converting into revenue from next year. With crude price stabilizing around USD 70 per barrel, we expect good ordering from Middle East and African region. Order inflow in domestic T&D market continue to dominate by some of the southern SEBs like Tamil Nadu, Karnataka and AP but we expect north east region will catch up speedily. Some of the Northern SEBs like UP and Bihar is in talk with PGCIL to carry out transmission projects in JV. Overall from domestic T&D market we continue to expect healthy ordering momentum. During the quarter KEC has won couple of big projects from SAARC countries and management expect that the big opportunities is coming up.

- ✓ **Improving EBITDA Margin:-** From last couple of years EBITDA margin continually improving on sequential basis from 5% to 9.5% in last quarter backed by turnaround in SAE, Railway and Cable business. EBITDA margin of SAE business improved significantly from 4-5% to 10-10.5%. KEC is heavily investing in railway and civil segment in order to cater the rising demand. Thus, the margin of these two key segments is blow T&D business margin but we expect the margin will catch up as the revenue increase. We estimate that the revenue from railway and Civil segment will be double by the next year and margin will inching up to 10.5-11%. We expect EBITDA will be improve by 50 bps in FY19 on account of higher EBITDA from railway and civil segment.

Revenue from railway segment will double based on robust order book



Strong Order book Growth of Civil business



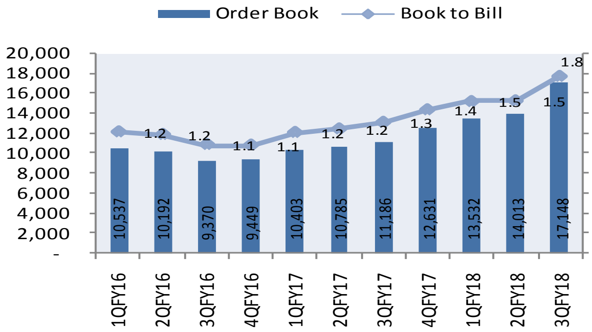
View and Valuation :-

KEC International has come up with yet another robust set of numbers. Strong execution across the segment led to healthy sales growth of 25% YoY. EBITDA margin was also improved by 60 bps YoY backed by strong revenue growth. Company has witnessed spurt in order inflow during the quarter, which will auger well for the revenue growth going ahead.

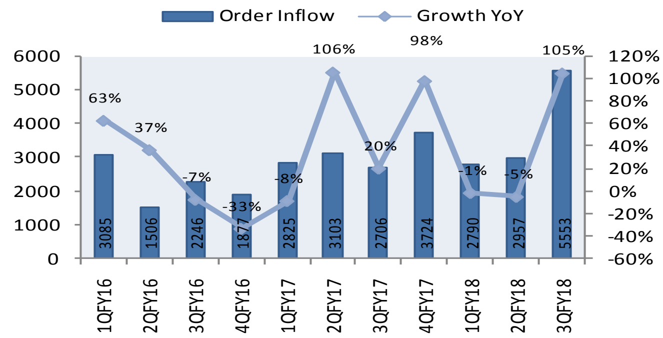
Company has continuously diversified its business into Railway, Solar and Civil to leverage its strong execution capabilities and we expect that the railway and civil will be the new growth drivers for the company along with strong hold in T&D business. Railway Ministry's increased focused on electrification of railway line ensures the healthy order inflow. Currently, KEC stand L1 in Rs.4000 Cr of orders, out of this major orders are from railway segment. Management is also eyeing railway electrification projects in international market and currently doing couple of projects. Management is also planning to extend its offering in civil business to residential buildings projects, affordable housing and civil work for defense. Brazil will be the next big market for the power T&D projects as the Brazilian government has a capex plan of 4 Bn USD for improving transmission network. SAE, wholly owned subsidiary of the company is well placed to garb the opportunity. With crude price stabilizing around USD 70 per barrel, we expect good ordering from Middle East and African region.

KEC is heavily investing in railway and civil segment in order to cater the rising demand. Thus, the margin of these two key segments is blow T&D business margin but we expect the margin will catch up as the revenue increase. We estimate that the revenue from railway and Civil segment will be double by the next year coupled with improvement in margin. Management has also guided for the 50 bps improvement in margin level in FY19. We expect revenue will grow by 11% CAGR over FY17-20 with strong operating margin of 9.9%. **KEC is in sweet spot to capitalize rising demand across the segment but considering the expensive valuation we are "NEUTRAL" on the stock with target price Rs.361 (3.5x FY20 book value).**

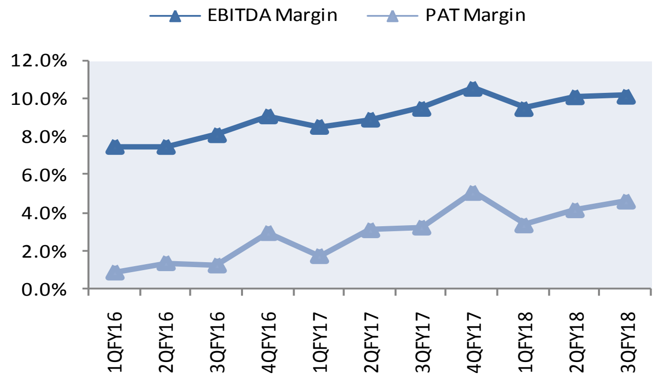
Order Book and Book to bill trend



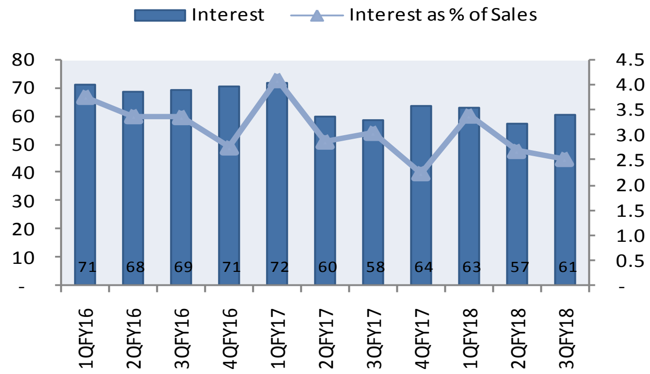
Strong Oder Inflow growth led by International T&D business



Improving Margin Trend



Interest as % of sales will remain at 2.5-2.7%



Financials Snap Shot

Income Statement

Rs in Crores

Y/E March	FY17	FY18E	FY19E	FY20E
Revenue from Operation	8,755	9,376	11,084	12,133
Change (%)	*1%*	*7%*	*18%*	*9%*
EBITDA	**818**	**923**	**1,087**	**1,196**
Change (%)	*18%*	*13%*	*18%*	*10%*
Margin (%)	9.3%	9.8%	9.8%	9.9%
Depr & Amor.	130	130	134	133
EBIT	***688***	***793***	***953***	***1,063***
Int. & other fin. Cost	254	246	254	275
Other Income	*29*	*29*	*29*	*29*
EBT	**463**	**576**	**728**	**817**
Exp Item	-	-	-	-
Tax	**159**	**207**	**255**	**286**
Minority Int & P/L share of Ass.	-	-	-	-
Reported PAT	**305**	**369**	**473**	**531**
Adjusted PAT	*305*	*369*	*473*	*531*
Change (%)	**106%**	**21%**	**28%**	**12%**
Margin(%)	*3%*	*4%*	*4%*	*4%*

Key Ratios

Y/E March	FY17	FY18E	FY19E	FY20E
ROE	19%	20%	21%	20%
ROCE	29%	34%	36%	35%
Asset Turnover	1.0	1.1	1.1	1.1
Debtor Days	175	165	160	165
Inventory Days	16	18	18	18
Payable Days	132	125	120	120
Interest Coverage	2.71	3.22	3.75	3.86
P/E	18	24	19	17
Price / Book Value	3.4	4.8	4.0	3.4
EV/EBITDA	*7*	*10.1*	*8.5*	*7.6*
FCF per Share	62	7	14	16
Dividend Yield	-	0.7%	1.0%	1.1%

Balance Sheet

Rs in Crores

Y/E March	FY17	FY18E	FY19E	FY20E
Share Capital	*51*	*51*	*51*	*51*
Reserves	1,535	1,817	2,188	2,604
Networth	*1,586*	*1,868*	*2,239*	*2,656*
Debt	*1,998*	*1,990*	*2,021*	*2,221*
Other Non Current Liab	*182*	*182*	*182*	*182*
Total Capital Employed	*2,352*	*2,358*	*2,661*	*3,077*
Net Fixed Assets (incl CWIP)	**922**	**996**	**983**	**969**
Non Current Investments	-	-	-	-
Other Non Current Assets	*262*	*262*	*262*	*262*
Non Current Assets	1,184	1,259	1,245	1,232
Inventory	**395**	**462**	**547**	**598**
Debtors	4,200	*4,238*	*4,859*	*5,485*
Cash & Bank	176	98	132	326
Other Current Assets	1,951	*2,090*	*2,471*	*2,704*
Current Assets	6,722	6,889	8,008	9,114
Creditors	2,198	3,211	3,644	3,989
Provisions	**70**	**75**	**88**	**97**
Other Current Liabilities	*1,552*	*1,406*	*1,663*	*1,820*
Curr Liabilities	*3,820*	*4,692*	*5,395*	*5,906*
Net Current Assets	*2,902*	*2,197*	*2,613*	*3,208*
Total Assets	*8,728*	*8,905*	*10,010*	*11,137*

Cash Flow Statement

Rs in Crores

Y/E March	FY17	FY18E	FY19E	FY20E
PBT	305	565	717	806
(inc)/Dec in Working Capital	703	(341)	(382)	(401)
Non Cash Op Exp	130	130	134	133
Int Paid (+)	254	246	254	275
Tax Paid	104	207	255	286
others	**215**	**-**	**-**	**-**
CF from Op. Activities	*1,662*	*393*	*468*	*527*
(inc)/Dec in FA & CWIP	*(67)*	*(205)*	*(120)*	*(120)*
Free Cashflow	1,595	188	348	407
(Pur)/Sale of Inv	-	64	-	(34)
others	**(24)**	**-**	**-**	**-**
CF from Inv. Activities	(183)	(140)	(120)	(154)
inc/(dec) in NW	-	-	-	-
inc/(dec) in Debt	(1,122)	(8)	31	200
Int. Paid	**(256)**	**(246)**	**(254)**	**(275)**
Div Paid (inc tax)	(1)	(80)	(102)	(115)
others	-	-	-	-
CF from Fin. Activities	(1,379)	(334)	(325)	(190)
Inc(Dec) in Cash	**100**	**(81)**	**23**	**184**
Add: Opening Balance	75	208	130	164
Closing Balance	*176*	*127*	*153*	*348*

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