

# KNR CONSTRUCTION LTD.

## ACCUMULATE

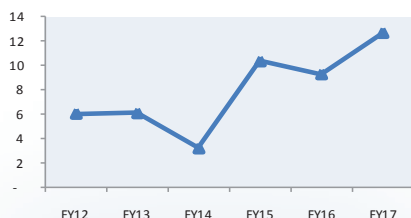
15-Nov-17

**INDUSTRY -** Eng. & Cons.  
**Bloomberg Code -** KNRC IN  
**BSE Code -** 532942  
**NSE Code -** KNRCON  
**NIFTY -** 10118

### Company Data

CMP	255
<b>Target Price</b>	<b>286</b>
Previous Target Price	230
<b>Upside</b>	<b>12%</b>
52wk Range H/L	290/132
Mkt Capital (Rs Cr)	3,598
Av. Volume (,000)	36

### P/E Multiple

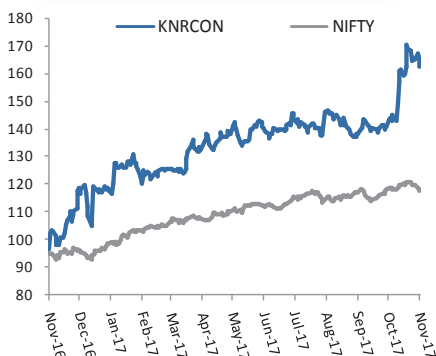


### Shareholding patterns %

	2QFY18	1QFY18	4QFY17
Promoters	57.4	57.4	58.0
Public	42.6	42.6	42.1
<b>Total</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>

### Stock Performance %

	1Mn	3Mn	1Yr
Absolute	19.7	16.0	77.5
Rel.to Nifty	20.8	13.8	58.8



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### Key Highlights of the Report:-

- ✓ KNRCON posted mix set of numbers in Q2FY18. Revenue was up by the 5% YoY while adj. EBITDA margin improved by 368 bps on account of lower subcontracting and higher margin on projects near completion.
- ✓ Management expect to win at least Rs.2500-3000 Cr of new orders (50-50% from EPC and HAM) in second half of FY18.
- ✓ Based on the KNRCON's strong execution capabilities we are confident that the revenue will grow by 15% CAGR over FY17 to FY19 with 12% CAGR earning growth in same period.
- ✓ EBITDA Margin will improve by 200 bps in FY18 on account of lower work through Subcontracting and higher margin on projects near completion.
- ✓ **We value KNRCON at 20x FY19 expected EPS and recommend "ACCUMULATE" with target price Rs.286.**

Financials/Value	FY15	FY16	FY17E	FY18E	FY19E
Net Sales	876	903	1,541	1,780	2,044
EBITDA	126	153	230	312	335
EBIT	72	111	166	217	245
PAT	73	161	158	208	201
EPS (Rs)	5	11	11	15	14
EPS growth (%)	20%	120%	-2%	32%	-3%
ROE (%)	13%	22%	18%	19%	15%
ROCE (%)	11%	13%	16%	17%	16%
BV per Share	40	52	64	78	93
P/B (X)	1.3	2.0	2.2	3.3	2.8
P/E (x)	10.3	9.3	12.6	17.2	17.9

### Recent Development

- ✓ On 21st September KNR-HES-ACPL JV has won EPC (Irrigation) order worth of Rs. 884.87 Cr for formation of Konda Pochamma Sagar for capacity of 15 TMC near Pamulaparthi in state of Telengana.
- ✓ KNR share will be Rs.442 Cr (assuming 50% stake in JV) and execution time line for the construction is 18 months.
- ✓ Small order intake of Rs.442 Cr will does not change revenue visibilities as we expect same amount of execution in Q2FY18 and book to bill at the end of Q2FY18 will be 1.96x of TTM.
- ✓ Earlier Management is reluctant to take HAM projects but considering the current market scenario, management is open to take HAM and expects Rs. 1000 Cr of orders in FY18 via HAM mode.
- ✓ Management expects to complete Thiruvananthapuram Bypass and Madurai -Ramanathapuram Section of NH-49 by January 2018 and April 2018 respectively.

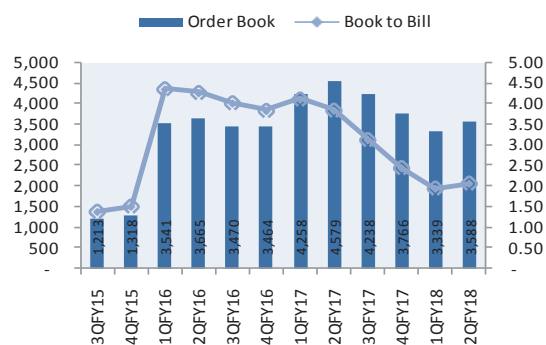
## Quarterly Performance

Financials	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	YoY %	QoQ%	FY16	FY17	YoY %
<b>Net Sales</b>	<b>373</b>	<b>382</b>	<b>482</b>	<b>481</b>	<b>393</b>	<b>5%</b>	<b>-18%</b>	<b>903</b>	<b>1,541</b>	<b>71%</b>
Other Income	13	10	1	12	3	-80%	-78%	32	30	-5%
<b>COGS</b>	<b>271</b>	<b>277</b>	<b>349</b>	<b>344</b>	<b>251</b>	<b>-7%</b>	<b>-27%</b>	<b>606</b>	<b>1,115</b>	<b>84%</b>
Employee Expenses	13	15	15	15	19	48%	30%	43	55	28%
Other Expenses	<b>33</b>	<b>32</b>	<b>47</b>	<b>37</b>	<b>40</b>	<b>22%</b>	<b>8%</b>	<b>100</b>	<b>142</b>	<b>41%</b>
<b>Total Expenditure</b>	<b>318</b>	<b>325</b>	<b>410</b>	<b>396</b>	<b>311</b>	<b>-2%</b>	<b>-22%</b>	<b>750</b>	<b>1,311</b>	<b>75%</b>
<b>EBITDA</b>	<b>56</b>	<b>58</b>	<b>72</b>	<b>85</b>	<b>82</b>	<b>47%</b>	<b>-2%</b>	<b>153</b>	<b>230</b>	<b>50%</b>
EBITDA M%	15%	15%	15%	18%	21%			17%	15%	
Depreciation	<b>15</b>	<b>17</b>	<b>19</b>	<b>24</b>	<b>24</b>	<b>61%</b>	<b>-3%</b>	<b>42</b>	<b>64</b>	<b>51%</b>
<b>EBIT</b>	<b>41</b>	<b>41</b>	<b>53</b>	<b>60</b>	<b>59</b>	<b>43%</b>	<b>-2%</b>	<b>111</b>	<b>166</b>	<b>50%</b>
Intreset	6	7	5	5	4	-23%	-18%	13	22	65%
Exceptional Item	-	<b>11</b>	-	-	-			-	<b>11</b>	
<b>PBT</b>	<b>49</b>	<b>45</b>	<b>48</b>	<b>67</b>	<b>57</b>	<b>17%</b>	<b>-15%</b>	<b>129</b>	<b>163</b>	<b>26%</b>
Tax	<b>5</b>	<b>3</b>	<b>(4)</b>	<b>(0)</b>	<b>(2)</b>	<b>-133%</b>	<b>345%</b>	<b>(32)</b>	<b>6</b>	<b>-119%</b>
<b>PAT</b>	<b>44</b>	<b>31</b>	<b>53</b>	<b>68</b>	<b>59</b>	<b>35%</b>	<b>-13%</b>	<b>161</b>	<b>158</b>	<b>-2%</b>
<b>PAT %</b>	<b>12%</b>	<b>8%</b>	<b>11%</b>	<b>14%</b>	<b>15%</b>			<b>18%</b>	<b>10%</b>	

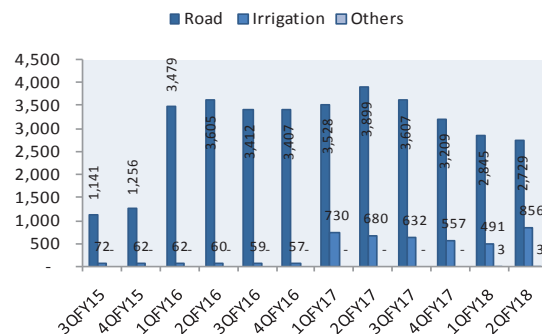
### Muted Revenue Growth on account of delay in necessary approval

- ✓ KNR posted mixed set of numbers in Q2FY18. Revenue was up by 5% YoY to Rs. 393 Cr compared to Rs. 373 Cr in last year. Muted revenue growth on account of delay in project related necessary approval.
- ✓ Revenue includes claim of Rs.16.81 Cr in Q2FY18. The two JV Company Patel –KNR and KNR-Patel has booked claim during the quarter. This directly contributes in operating margin.
- ✓ EBITDA during the quarter grew by 47.4% YoY to Rs. 82 Cr as against Rs. 56 Cr in same period last year on account of claim.
- ✓ During the quarter KNRCON received new order of Rs.884 Cr (51% KNR share). Tepid bidding and delay in new tenders due to GST, impacted awarding activity.
- ✓ Current order book stands at Rs.3588 Cr, revenue visibilities down to 2.1x from 4.1x of TTM revenue.

### Order Book and Book to Bill



### Order Book Break Up



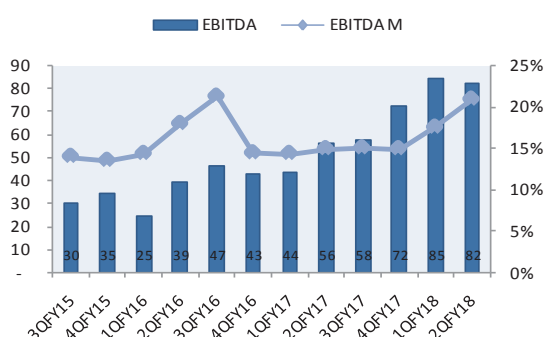
## Margin Matrix

Margin %	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	YoY(+/-)	QoQ(+/-)	FY16	FY17	YoY(+/-)
Gross Margin	79.2	78.9	79.8	78.9	71.5	(7.7)	(7.4)	69.1	78.3	9.2
EBITDA Margin	15.0	15.1	15.0	17.6	21.0	6.0	3.4	16.9	14.9	(2.0)
PAT Margin	11.7	8.0	11.0	14.1	15.0	3.3	0.9	17.8	10.2	(7.6)

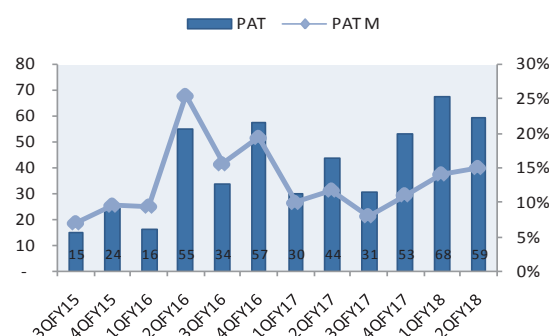
## Lower Subcontracting and higher margin on projects nearing completion led to margin improvement

- ✓ After adjusting claim EBITDA margin improved by 368 bps on account of lower Subcontracting and high margin on couple of projects which are near completion.
- ✓ EBITDA margin for the full year will be higher by 200 bps compared to FY17 based on lower work through Subcontracting. However margin in FY19 will be lower as the Hubli Hospet projects is lagging behind 8-9 months and margin is not good as other project has.
- ✓ PAT has improved by 330 bps on back of lower tax outgo and higher EBITDA. PAT was up by 35% YoY to Rs.59 Cr compared to Rs.44 Cr in same period last year.

### EBITDA (cr) and EBITDA margin trend



### PAT (cr) and PAT margin trend



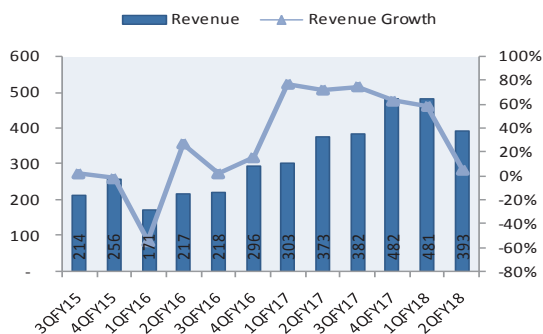
## Concall Highlights :-

- ✓ EBITDA is higher as the lower work through Subcontracting and high margin on couple of projects which are near completion.
- ✓ KNRCON has submitted bid for K-SHIP project in Karnataka and bid will open in a month time.
- ✓ Maintain Revenue guidance of Rs.1700-1800 Cr for FY18 and Rs.2000 Cr for FY19.
- ✓ EBITDA margin will be 16-17% in FY18.
- ✓ Management expects to receive projects related necessary approval on Hubli Hospet in a month time. Execution in pace will start from Q4FY18.
- ✓ EBITDA on Hubli Hospet is not as good as other projects have.
- ✓ Company is evaluating opportunity in River linking projects.
- ✓ Tax rate will be 10% in FY18 and 15% in FY19.
- ✓ Expect lower EBITDA margin in FY19 compared to FY18 as the revenue contribution from Hubli Hospet will increase.
- ✓ Management is targeting new orders worth of Rs.2500-3000 Cr in FY18, out of which Rs.1000-1500 Cr of orders through HAM and rest from Road EPC.

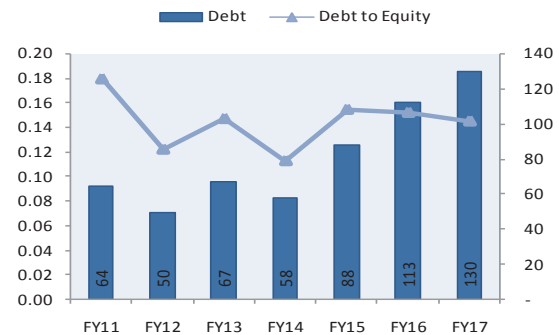
## Investment Argument :-

- ✓ **Order Inflow to pick up:-** Revenue visibility has come down to 2.1x of TTM revenue from 4.1x. Tepid bidding and delay in new tenders due to GST implementation lead to sluggish quarter in terms of new order inflow. But now Government's push in infra by announcing Rs.6.92lakh Cr of investment through Bharatmala project will open up huge scope of work. Earlier management was reluctant to take HAM projects but now management is ready to take up and expect to win at least Rs.2500-3000 Cr of new orders (50-50% from EPC and HAM) in second half of FY18. Management also planning to enter into new verticals likes elevated metros,Railways and River linking. This change in management's strategy will boost the order book growth going forward.
- ✓ **Strong Execution capabilities:-** Execution is key characteristic in infra companies. Superior execution capabilities have given extensive headroom for the growth. For the last 5 quarters KNRCON revenue has grown at an average of 70%. Currently management expect to complete couple of projects ahead of schedule time. Based on the KNRCON's strong execution capabilities we are confident that the revenue will grow by 15% CAGR over FY17 to FY19 with 12% CAGR earning growth in same period.
- ✓ **Healthy Debt to Equity:-** Strong execution capabilities and limited exposure to captive projects have kept KNRCON balance sheet light. Current debt to equity stands at 0.15x on standalone basis and 0.82x on consolidated basis. To grow higher in the competitive scenario management is eyeing on HAM model considering the government's extreme focus. Strong debt to equity position will allow company to leverage it and taking more projects to grow higher.

## Muted Revenue Growth on account of delay in necessary approval



## Strong Debt to Equity



## Outlook and Valuation:-

KNRCON is one of the fastest growing companies in Engineering, Procurement and Construction segment. Company undertakes EPC projects in Roads and Highways, Irrigation and Urban Water Infrastructure. KNRCON posted mix set of numbers in Q2FY18. Revenue was up by the 5% YoY while adj. EBITDA margin improved by 368 bps on account of lower subcontracting and higher margin on projects near completion. Revenue visibility continues to reduce from 4.1x to 2.1x of TTM revenue but we expect strong recovery in bidding activity in second half of FY18. Earlier management was reluctant to take HAM projects but now management is ready to take up and expect to win at least Rs.2500-3000 Cr of new orders (50-50% from EPC and HAM) in second half of FY18. This change in management's strategy will boost the order book growth going forward. Hubali Hospet EPC project in Karnataka is lagging behind 8-9 months but will receive the necessary approval in a month time period and we expect healthy execution from Q4FY18. Based on the KNRCON's strong execution capabilities we are confident that the revenue will grow by 15% CAGR over FY17 to FY19 with 12% CAGR earning growth in same period. **We value KNRCON at 20x FY19 expected EPS and recommend "ACCUMULATE" with target price Rs.286.**