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Company update and
earnings revision

Capital Goods

Target price Rs341

Earnings revision

(%)	FY20E	FY21E
Sales	0.0	↑ 0.0
EBITDA	0.0	↑ 4.9
EPS	0.0	↑ 8.6

Target price revision

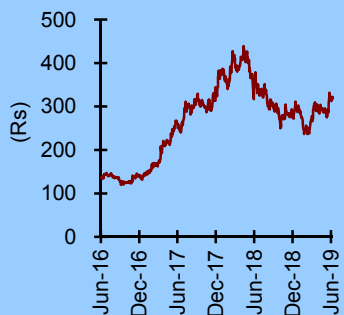
Rs341 from Rs314

Shareholding pattern

	Sep '18	Dec '18	Mar '19
Promoters	51.2	51.3	51.4
Institutional investors	30.7	31.5	31.1
MFs and other	18.9	21.6	22.5
F s/Banks	0.4	0.4	0.3
Insurance	1.7	1.7	1.7
FIs	9.8	7.8	6.6
Others	18.1	17.2	17.5

Source: NSE

Price chart



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INDIA

ICICI Securities

KEC International

ADD

Maintained

Rs322

Healthy growth to lift earnings

During KEC International (KEC) analyst meet, the management re-iterated their confidence on the overall growth prospects. Three projects that were stuck in Brazil due to environmental clearance issues have commenced execution, which will support growth of subsidiary SAE. On the domestic front, Railways and civil segments are expected to continue with their strong growth. Domestic T&D ordering is expected to get a fillip from ordering by key state electricity boards and green energy corridor opportunities. Overseas T&D demand from SAARC, South-East Asia and MENA continues to be healthy. We raise FY21E earnings by 8% and maintain ADD with a revised target price of Rs341 (previously Rs314).

- ▶ **T&D execution is poised to improve led by SAE:** Company is confident of recovery in T&D execution led by SAE with resolution of environmental clearance hurdles in three projects (in Brazil). Led by a healthy orderbook, overall growth traction in the overseas T&D segment is expected to improve and domestic order intake is poised to gain traction.
- ▶ **Strong growth under Railways and civil segments to continue:** KEC is gradually increasing its addressable pie under the Railways by targeting to enter signalling & telecommunication, metros, etc. Even under civil, the company is expanding towards airports, metros, etc. These two segments continue to promise high growth over the next two to three years.
- ▶ **Revival of domestic T&D orders led by SEB and GEC:** State electricity board (SEB) ordering had been weak during FY19, especially from some of the key SEBs like Karnataka and Tamil Nadu. These orders are expected to be revived in addition to traction from other states like Odisha, West Bengal, Gujarat and Uttar Pradesh. Green energy corridor order is also expected to gain traction. Overseas T&D ordering from MENA is expected to pick up, especially from the UAE, Saudi Arabia, etc. Bangladesh is flush with considerable multilateral funding, which should support order uptick.
- ▶ **Maintain ADD, raise earnings and target price on optimistic growth:** With a stable government in place, domestic order intake environment is optimistic while strong ordering from Railways and civil segments will continue. Overseas market growth prospects are healthy led by MENA, SAARC and South-East Asia. Working capital is expected to be high given better than expected collections in FY19 and large advances from projects in Bangladesh, etc. during Mar'19. We raise our earnings by 8% for FY21E. Maintain ADD with a revised target price of Rs341 implying 12x FY21E earnings (earlier target price: Rs314).

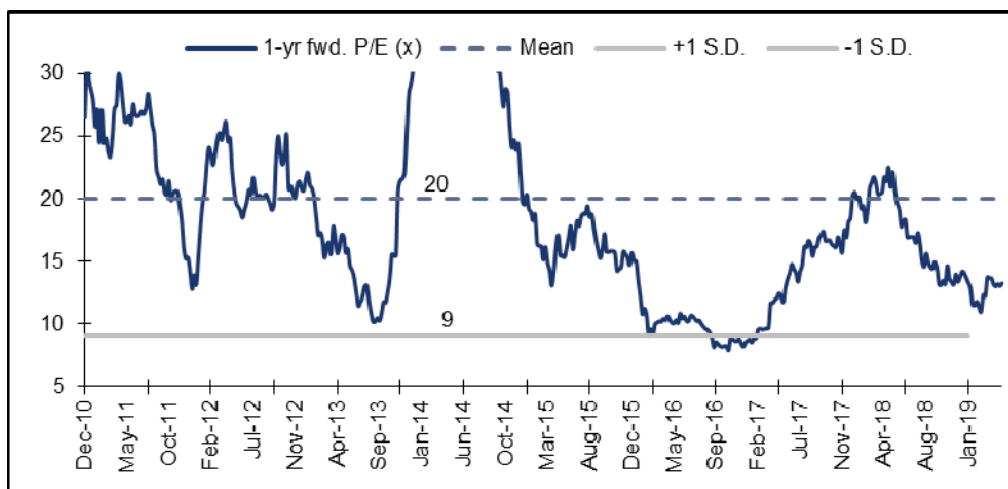
Market Cap	Rs83bn/US\$1.2bn	Year to March	FY18	FY19	FY20E	FY21E
Reuters/Bloomberg	KECL BO/KECI IN	Revenue (Rs mn)	1,00,910	1,10,005	1,29,070	1,47,183
Shares Outstanding (mn)	257.1	Adjusted NI (Rs mn)	4,583	4,864	6,172	7,303
52-week Range (Rs)	379/237	DEPS (Rs)	17.8	18.9	24.0	28.4
Free Float (%)	48.6	% Chg YoY	50.4	6.1	26.9	18.3
FII (%)	6.6	P/E (x)	18.1	17.1	13.5	11.4
Daily Volume (US\$'000)	1,871	CEPS (Rs)	22.1	23.5	28.6	33.1
Absolute Return 3m (%)	11.6	EV/E (x)	9.6	8.4	7.5	6.4
Absolute Return 12m (%)	(12.2)	Dividend Yield	0.7	0.7	1.1	1.1
Sensex Return 3m (%)	6.2	RoCE (%)	16.4	16.4	15.0	15.8
Sensex Return 12m (%)	12.7	RoE (%)	22.9	20.0	20.9	20.4

Please refer to important disclosures at the end of this report

Valuation and outlook

The stock is currently trading at 11.4x FY21E earnings. We maintain our valuation multiple due to working capital stress impacting RoE and cashflows. We believe that the current strong orderbook, prospects from Railways and healthy growth guidance of 15-20% in FY20E along with stable margins will support our estimate of 23% earnings CAGR over FY19-FY21E. Given benign valuation of 11.4x FY21E earnings and healthy earnings growth, we maintain ADD on the stock with a revised target price of Rs341 implying 12x FY21E earnings (earlier target price Rs314).

Chart 1: 1-year forward P/E chart



Source: Bloomberg, I-Sec research

Table 1: Earnings revision (consolidated)

(Rs mn)

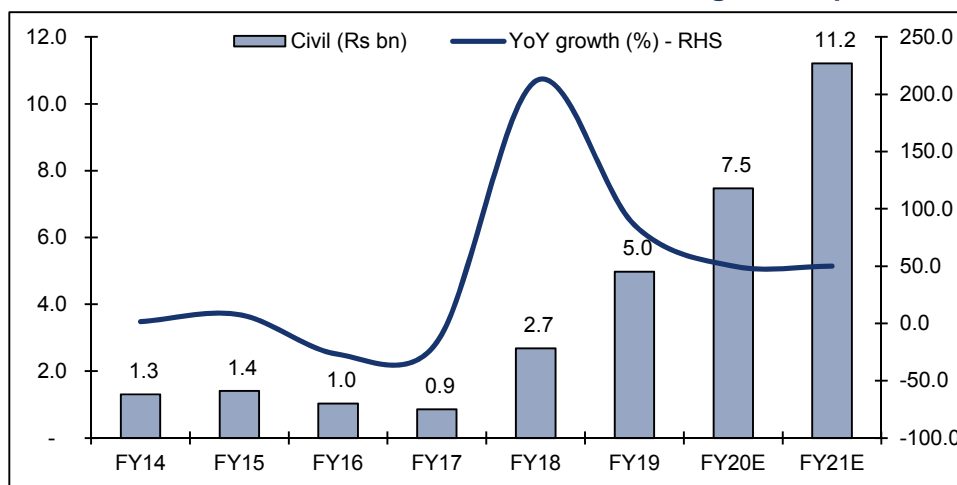
	FY20E			FY21E		
	Previous	Revised	YoY (%)	Previous	Revised	YoY (%)
Revenue	1,29,070	1,29,070	-	1,47,183	1,47,183	0.0
EBIDTA	12,887	12,887	-	14,938	15,674	4.9
PAT	5,665	5,665	-	6,724	7,303	8.6

Source: Company data, I-Sec research

Civil – A new growth engine

The management foresees strong growth from the civil vertical with focus towards infrastructure-related orders in the form of airport extension, government projects, terminal buildings, etc. KEC targets small to medium ticket size orders initially in the range of Rs1bn-3bn. In a medium to long term perspective, the company expect this segment to have substantial contribution to the overall revenues.

Chart 2: Increased revenue contribution from civil segment expected

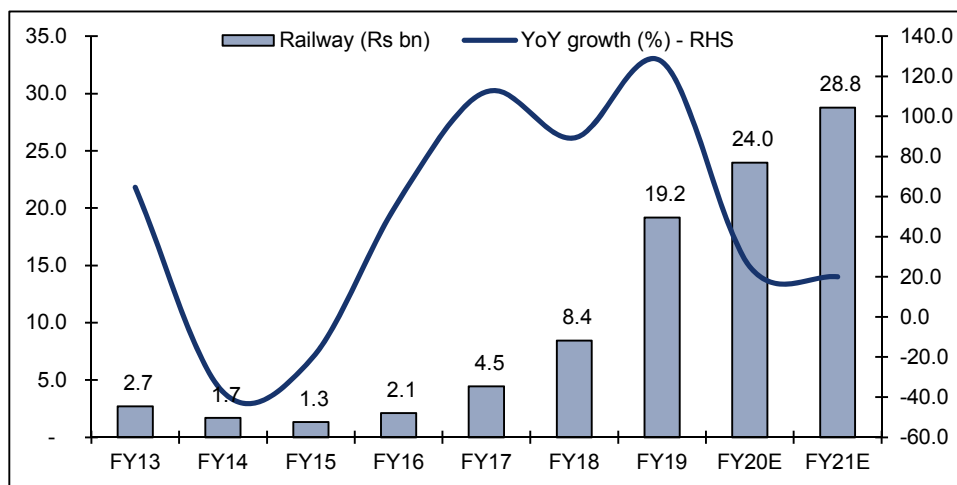


Source: Company Data, I-Sec research

Railways: Strong growth outlook

KEC plans to increase its overall scope of opportunity under the Railways segment by tapping into signalling and telecommunications, metro projects, etc. The company also has plans to enter into overseas geographies such as Bangladesh, Turkmenistan, Malaysia and Africa and bid for projects funded by the government of India. Given the current government’s thrust, the Railways segment is likely to witness strong growth over the next 2-3 years.

Chart 3: Growth to come from increased scope of work under railways

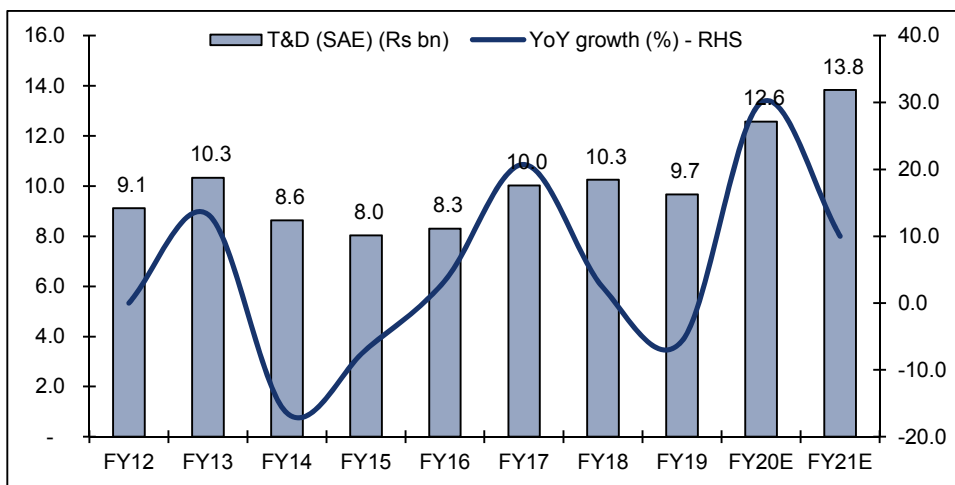


Source: Company Data, I-Sec research

SAE Towers: Growth to revive

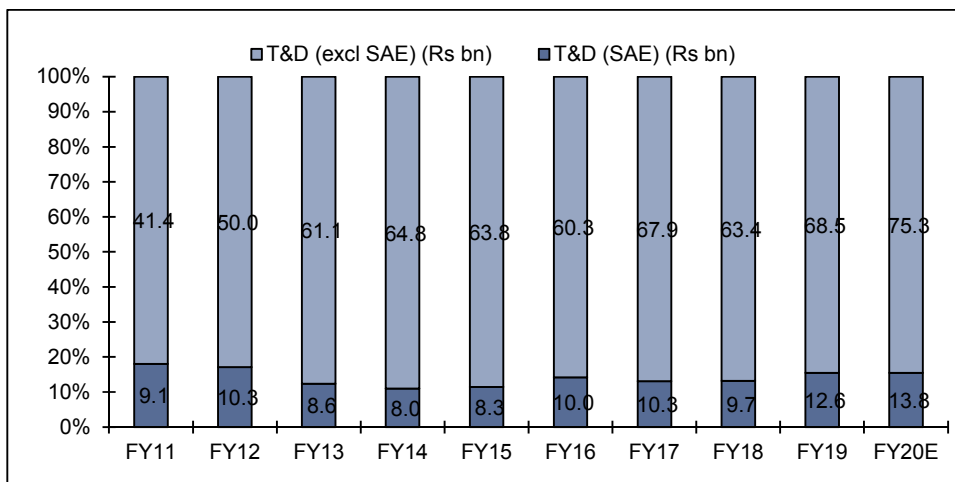
Due to certain environmental clearance hurdles, SAE Towers (100% subsidiary based out of Mexico) had witnessed revenue decline in FY19. Currently, most of these issues are sorted out and the management expects 30-35% growth in FY20E with 8-9% EBIDTA margin. SAE is L1 in one large project and this provides growth visibility for FY21E too.

Chart 4: SAE to revive on resolution of environmental clearance hurdles



Source: Company Data, I-Sec research

Chart 5: SAE revival to result in increased share in total T&D mix



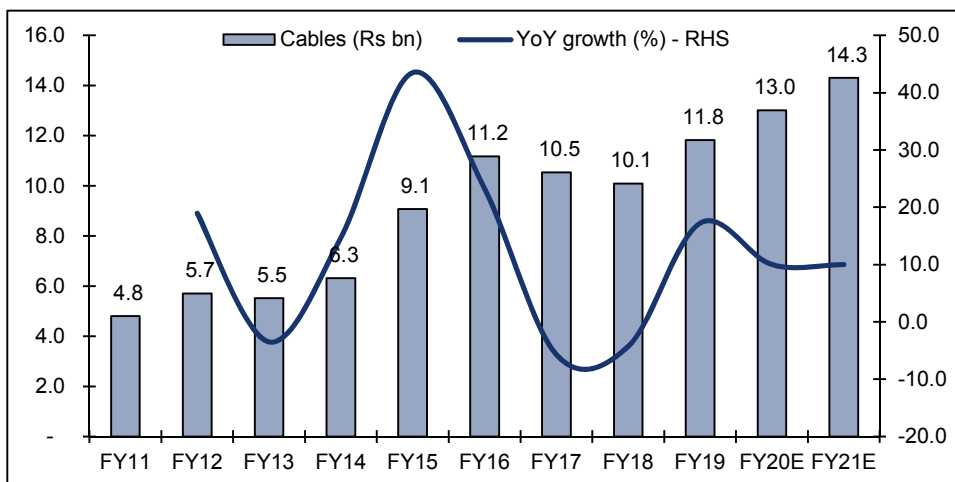
Company Data, I-Sec research

Source:

Cables – Focus on margin improvement

There is some ~1.5bn worth of captive consumption of cables by the Railways segment of the company. This has been capping the overall segmental margins since it is being shared by cables and the Railways division. ~30% of the cable sales are pertaining to EHV and the management expects stable growth with margins of 6-6.5% going forward.

Chart 6: Growth in cables to come from export market and EHV lines

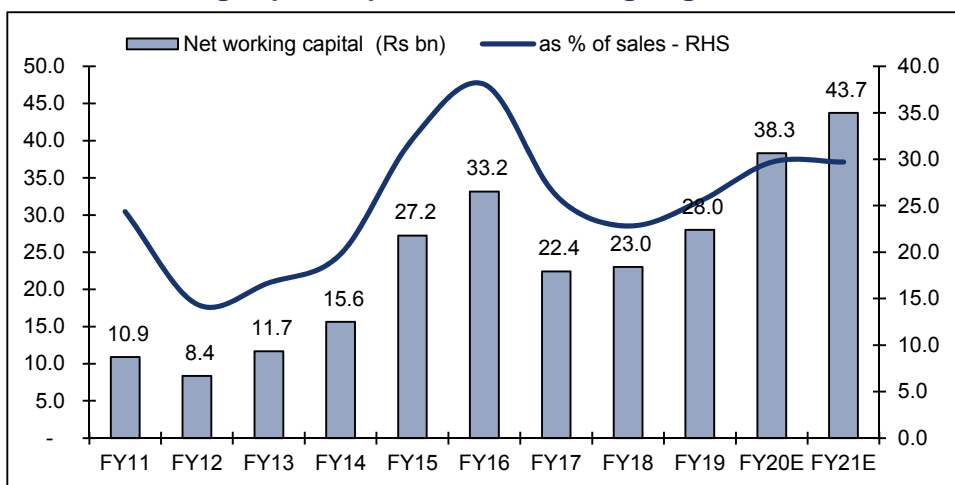


Source: Company Data, I-Sec research

Other key highlights

- Solar EPC currently contributed ~Rs3bn-4bn per annum. The company is looking at Middle East markets and will participate in large projects in Saudi Arabia along with a global partner.
- A major private sector project that was stalled is from Essel. Under this project, the company has executed works worth Rs5bn while Rs4.5bn is pending execution (it was stalled due to lack of financing at client-end). About Rs1.5bn of receivables is also pending from this project.
- Working capital reduced in Mar'19 due to receipt of large advances from Bangladesh and good improvement in collections. Hence, the management expects working capital to increase given the 15-20% revenue growth and targets for Rs24bn-25bn of debt (vs current debt of ~Rs30bn).

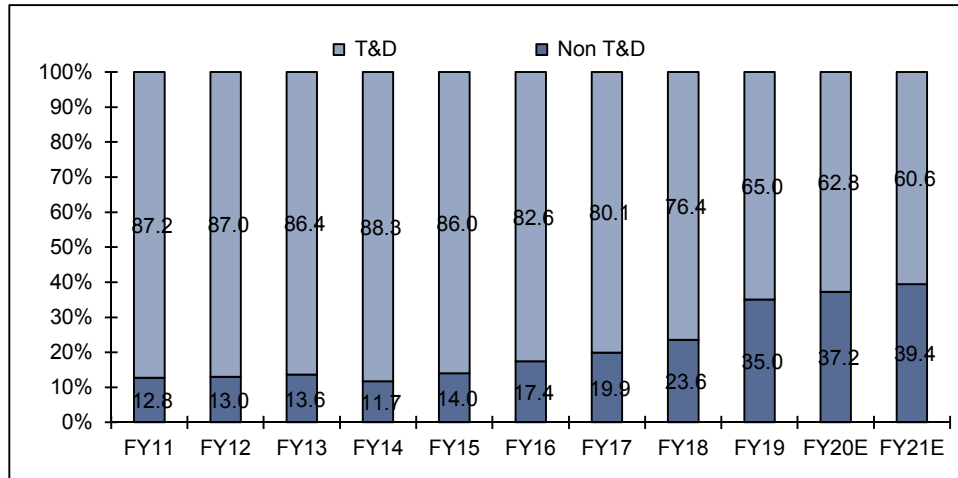
Chart 7: Working capital expected to increase going forward



Source: Company Data, I-Sec research

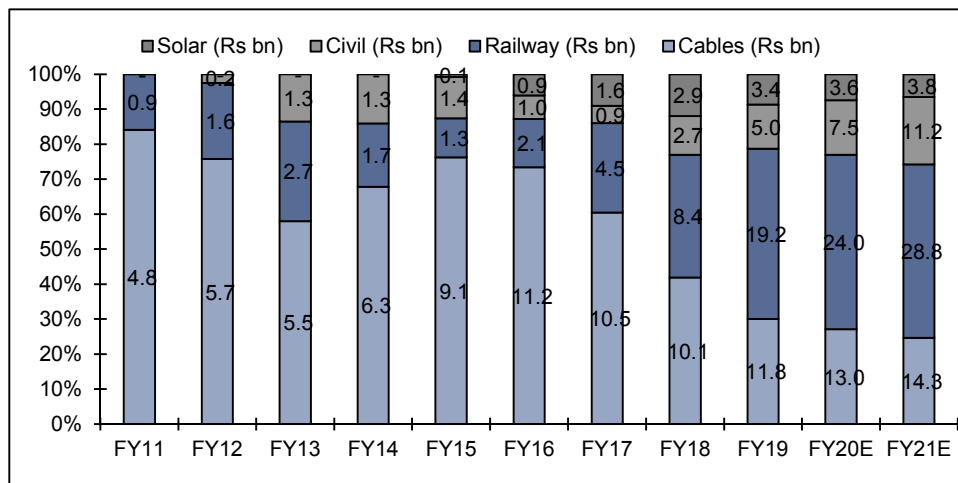
- Interest cost as a percentage of sales is expected to reduce to 2.5% in FY20E vs 2.6% in FY19.
- In the long term, KEC targets the non-T&D business contribution to stabilise at 40-45% of overall revenues.

Chart 8: Non-T&D mix to increase to stabilize at 40-45% of total revenues



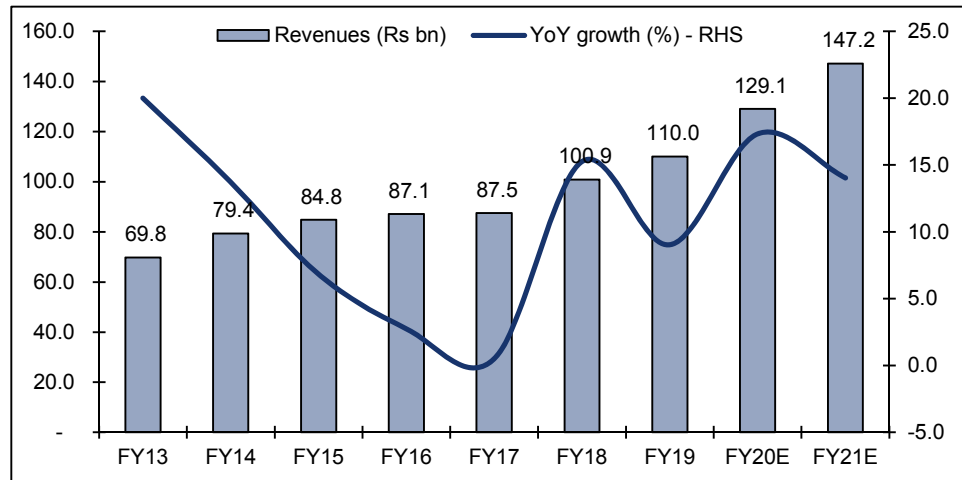
Source: Company Data, I-Sec research

Chart 9: Revenue share contribution in non-T&D segments



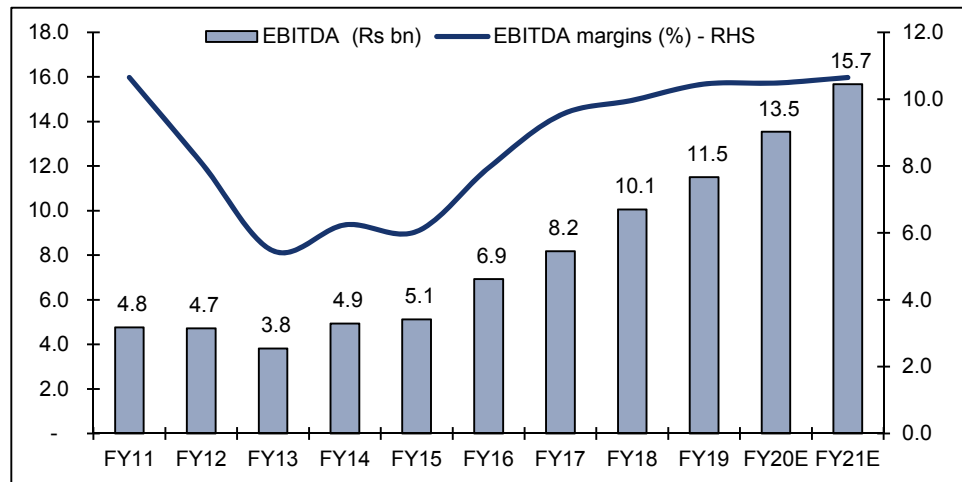
Source: Company Data, I-Sec research

Chart 10: Railways, civil and SAE revival to lead overall growth in revenues



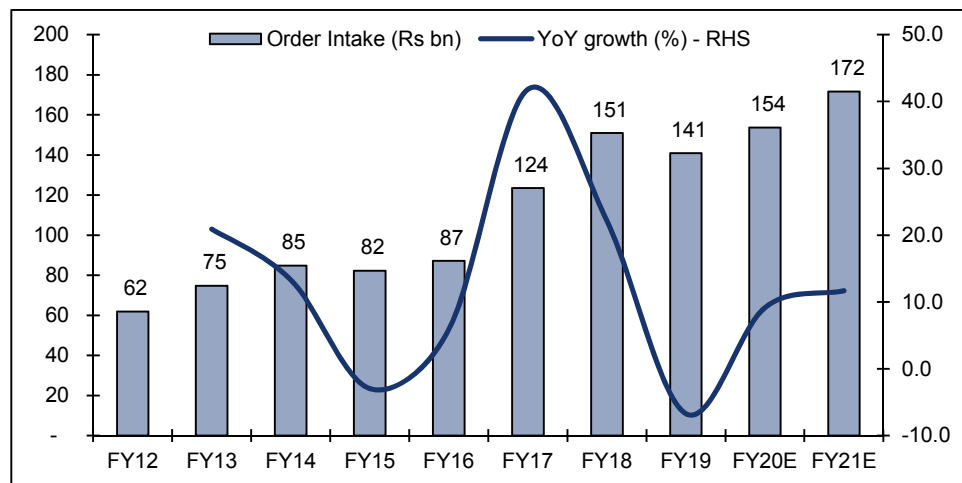
Source: Company Data, I-Sec research

Chart 11: Stable margins expected going forward



Source: Company Data, I-Sec research

Chart 12: Healthy order intake outlook



Source: Company Data, I-Sec research

Financial summary

Table 2: Profit & Loss statement

(Rs mn, year ending March 31)

	FY18	FY19	FY20E	FY21E
Total Income	1,00,910	1,10,005	1,29,070	1,47,183
Operating Expenses	90,853	98,506	1,15,538	1,31,510
EBITDA	10,057	11,499	13,533	15,674
% margins	10.0	10.5	10.5	10.6
Depreciation & Amortisation	1,097	1,171	1,183	1,195
EBIT	8,960	10,328	12,350	14,479
Gross Interest	2,294	3,119	3,227	3,680
Other Income	207	226	300	350
PBT before exceptionals	6,873	7,435	9,423	11,149
Add:				
Extraordinaries/Exceptionals	-	-	-	-
Add: Share in associates	-	-	-	-
PBT	6,873	7,435	9,423	11,149
Less: Taxes	2,290	2,571	3,251	3,847
Less: Minority Interests	-	-	-	-
Net Income (Reported)	4,583	4,864	6,172	7,303
Adjusted Net Income	4,583	4,864	6,172	7,303

Source: Company data, I-Sec research

Table 3: Balance sheet

(Rs mn, year ending March 31)

	FY18	FY19	FY20E	FY21E
Assets				
Total Current Assets	93,094	1,04,915	1,30,174	1,48,113
of which cash & cash eqv.	2,313	2,762	6,337	6,978
Total Current Liabilities & Provisions	67,749	74,129	85,511	97,421
Net Current Assets	25,345	30,786	44,664	50,692
Investments	393	132	132	132
Other Non-Current Assets	1,920	2,037	2,037	2,037
Net Fixed Assets	9,983	9,860	8,624	8,930
Goodwill	-	-	-	-
Total Assets	37,641	42,816	55,457	61,791
Liabilities				
Borrowings	16,394	16,968	24,411	24,411
Deferred Tax Liability	1,272	1,497	1,571	1,650
Minority Interest	-	-	-	-
Equity Share Capital	514	514	514	514
Face Value per share (Rs)	2.00	2.00	2.00	2.00
Reserves & Surplus	19,460	23,837	28,961	35,217
Net Worth	19,975	24,351	29,475	35,731
Total Liabilities	37,641	42,816	55,457	61,791

Source: Company data, I-Sec research

Table 4: Cashflow statement

(Rs mn, year ending March 31)

	FY18	FY19	FY20E	FY21E
Operating Cashflow	7,575	8,605	12,473	12,560
Working Capital Changes	(635)	(4,993)	(10,302)	(5,388)
Capital Commitments	(917)	(162)	(1,497)	(1,500)
Free Cashflow	6,023	3,450	674	5,672
Cashflow from Investing Activities	911	261	-	-
Issue of Share Capital	0	-	-	-
Buyback of shares	-	-	-	-
Inc (Dec) in Borrowings	(3,688)	574	7,443	-
Interest paid	(2,294)	(3,119)	(3,227)	(3,680)
Dividend paid	(209)	(238)	(718)	(718)
Extraordinary Items/Others	(510)	(480)	(329)	(329)
Chg. in Cash & Bank balance	234	448	3,843	945

Source: Company data, I-Sec research

Table 5: Key ratios

(Year ending March 31)

	FY18	FY19	FY20E	FY21E
Per Share Data (in Rs.)				
Diluted adjusted EPS	17.8	18.9	24.0	28.4
Recurring Cash EPS	22.1	23.5	28.6	33.1
Dividend per share (DPS)	2.4	2.4	3.5	3.5
Book Value per share (BV)	77.7	94.7	114.7	139.0
Growth Ratios (%)				
Operating Income	17.6	9.0	17.3	14.0
EBITDA	23.0	14.3	17.7	15.8
Recurring Net Income	50.4	6.1	26.9	18.3
Diluted adjusted EPS	50.4	6.1	26.9	18.3
Diluted Recurring CEPS	30.7	6.3	21.9	15.5
Valuation Ratios				
P/E	18.1	17.1	13.5	11.4
P/CEPS	14.6	13.8	11.3	9.8
P/BV	4.2	3.4	2.8	2.3
EV / EBITDA	9.6	8.4	7.5	6.4
EV / Operating Income	1.0	0.9	0.8	0.7
EV / Op. FCF (pre-capex)	13.9	26.9	46.5	14.0
Operating Ratios				
Raw Material/Sales (%)	50.9	49.2	50.7	51.3
SG&A/Sales (%)	10.0	8.7	8.3	8.0
Other Income / PBT (%)	3.0	3.0	3.2	3.1
Effective Tax Rate (%)	33.3	34.6	34.5	34.5
NWC / Total Assets (%)	61.2	65.5	69.1	70.7
Inventory Turnover (days)	22.7	21.3	26.0	26.0
Receivables (days)	182.3	161.8	170.0	170.0
Payables (days)	168.5	159.3	160.0	160.0
Debt/Equity (x)	0.8	0.7	0.8	0.7
Profitability Ratios (%)				
Recurring Net Income Margins	4.5	4.4	4.8	5.0
RoCE	16.4	16.4	15.0	15.8
RoNW	22.9	20.0	20.9	20.4
Dividend Payout Ratio	13.5	12.7	14.6	12.3
Dividend Yield	0.7	0.7	1.1	1.1
EBITDA Margins	10.0	10.5	10.5	10.6

Source: Company data, I-Sec research

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