

Engineers India

BUY

CMP Rs73

Target Rs102

Upside 39%

Our View: When compared to GDP growth, the average energy multiplier for India has been at ~0.8x of GDP growth. Hence, assuming 5% CAGR demand for petroleum products, India is likely to face supply deficit situation by FY25. In addition, current refining capacity utilization stands at 100%+, which warrants significant capex, implying improving business prospects for ENGR over medium to long term. Hence, Govt. has set up a plan to nearly double its oil refining capacity in the next 5 years (refining capacity expansion of ~250MMTPA), so the cumulative capex is expected to be Rs7-8trn, implying a PMC opportunity size of ~Rs450-500bn for ENGR. Engineers India's core business is services based on strong technical knowhow which enables it to operate on negative working capital & negligible capex (Infinite core RoIC) leading to strong free cash flows. We cut FY22E/FY23E EPS by 11%/8% to factor in the subdued margin in LSTK segment & lower other income. Margins seems to have bottomed out in FY21 & expect its improving trend over FY22-FY23. Given debt-free balance sheet, market leadership, superlative avg. FCF yield of 14%, strong execution capability and inexpensive valuation (8.6x FY23 earnings, -1.5SD of long term average). Retain BUY with TP of Rs102.

Key highlights from Q3FY21 earnings call

FY22 order inflow guidance at Rs15-20bn: ENGR has two committed order from i) Indian Oil for Panipat refinery expansion, and ii) the other project for BPCL. The major project execution for these is targeted next year. So, phase 2 of these projects is targeted by middle of next year. The main project execution for Panipat refinery is expected to be in the range of Rs6bn and for BPCL – Rs2bn. Besides, ENGR is looking for new refinery at Kaveri basin from Indian Oil (Indian Oil has approved capex for this refinery and bidding process has been initiated with order expected this end of the year or beginning of next year). Moreover, company is looking for Mangalore refinery expansion project for which feasibility study has been done. One or more small project from Numaligarh could materialize by the end of quarter for revamp and quality upgrade of Numaligarh refinery. In addition, HEML cracker expansion from 1.2 to 1.5mmtpa; Cracker project is currently ongoing for 1.2 mmtpa and subsequent expansion is planned next year. Order inflow for FY22E is expected to be in the range of Rs15bn – Rs20bn.

Exhibit 1: Financial Summary

Y/e 31 Mar (Rs m)	FY19	FY20	FY21E	FY22E	FY23E
Revenues	24,443	32,031	28,351	32,190	36,529
yoy growth (%)	36.7	31.0	(11.5)	13.5	13.5
Operating profit	3,660	4,430	2,686	3,863	4,997
OPM (%)	15.0	13.8	9.5	12.0	13.7
Adjusted PAT	3,701	4,302	3,430	4,384	5,356
yoy growth (%)	(0.7)	16.3	(20.3)	27.8	22.2
EPS (Rs)	5.9	6.8	5.4	6.9	8.5
P/E (x)	12.5	10.7	13.4	10.5	8.6
Price/Book (x)	2.0	2.0	1.9	1.7	1.6
EV/EBITDA (x)	5.8	4.8	7.9	5.5	4.3
Net D/E (x)	(1.2)	(1.2)	(1.1)	(1.1)	(1.2)
Core RoIC (%)	16.3	18.7	14.3	17.1	19.4
RoE (%)	16.3	18.6	14.2	17.1	19.4

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- ✓ Margins of Turnkey segment (LSTK) likely to remain muted in near term: Currently, the company is executing two jobs - i) Rajasthan refinery project, and ii) HPCL VRMP project which are cost plus project with margins at competitive pricing. The company has provided certain provisions – Guarantee/warranty liabilities for these projects which resulted in lower margin. So, when these projects are completed, the provisions might be released leading to higher margins. With current orderbook, turnkey margin is expected to be in the range of 2-3%
- ✓ Update on RFPL: Commissioning of RFPL was targeted during Dec-2020. However, it got delayed due to equipment related problem in CPP plant executed by BHEL. Problem has been rectified now. Now, the targeted commissioning of project is in Feb-2021.
- ✓ Barmer Refinery: The total capex for Barmer refinery is estimated around Rs450-480bn. ENGR is currently executing two jobs - i) PMC: Rs11.8bn, and ii) OB job: Rs37bn. Overall progress for the project is at 20-25% on the capex with proportionate contracts with ENGR.
- ✓ Exports markets are still sluggish due to fall in crude oil prices. Mgmt. expects recovery in ordering activities in early FY22.
- ✓ Healthy cash balance of Rs25bn including customer advance Rs1-1.5bn as of Q3FY21
- ✓ Capex guidance: Capex for FY21/FY22 at Rs0.75bn/Rs1.5bn respectively.

Q3FY21 standalone results

- ✓ Sales declined by 6% yoy to Rs8.4bn (marginal miss vs our est.) as Consultancy/LSTK segment revenues were down by 2%/9% yoy respectively.
- ✓ Consultancy/LSTK segment sales mix was 43%/57% for Q3FY21
- ✓ EBITDA was down 12% yoy as LSTK segment margin declined from 3.0% to 1.4% while consultancy segment margin improved by 70bps yoy to 25.4%
- ✓ Other income was down 27% yoy.
- ✓ Adjusted PBT stood at Rs1.2bn, down 19% yoy (-23% vs our est.)

Exhibit 2: Quarterly results table (Standalone)

(Rs mn)	Q3FY21	Q3FY20	% yoy	Q2FY21	% qoq	Q3FY21 Yes Sec	vs. our est
Total sales	8,367	8,906	(6.0)	6,834	22.4	8,461	(1.1)
EBITDA	751	856	(12.3)	773	(2.8)	1,015	(26.1)
EBITDAM (%)	9.0	9.6	(63.6)	11.3	(233.2)	12.0	(302.8)
Depreciation	(51)	(56)	(9.0)	(60)	(14.6)	(62)	(17.9)
Interest	(4)	(4)	(7.4)	(5)	(13.1)	(5)	(19.3)
Other income	480	657	(27.0)	533	(9.9)	580	(17.3)
PBT	1,176	1,452	(19.1)	1,241	(5.3)	1,528	(23.1)
Tax	(294)	(366)	(19.8)	(314)	(6.5)	(385)	(23.8)
Adjusted PAT	882	1,086	(18.8)	927	(4.8)	1,143	(22.8)
Exceptional item	0	0		0		0	
Reported PAT	882	1,086	(18.8)	927	(4.8)	1,143	(22.8)
PATM (%)	10.5	12.2	(165.7)	13.6	(302.0)	13.5	(297.0)
EPS (Rs)	1.4	1.7	(18.8)	1.5	(4.8)	1.8	(22.8)

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