

**HOLD**

TP: Rs 630 | ▼ 3%

**KEC INTERNATIONAL**

| Capital Goods

| 04 August 2023

## Healthy inflows, margin improvement ahead

- **Good Q1 with 28% YoY topline growth and 70bps EBITDA margin gains to 5.8%; management sees “improving trajectory of profitability”**
- **Order intake at Rs 45bn; guidance reiterated for FY24 order inflow growth (+15% YoY), revenue (Rs 200bn) and EBITDA margin (~7%)**
- **Improved confidence on margins leads us to raise FY24/FY25 EPS 9%/6%; on rollover, our TP rises to Rs 630 (vs. Rs 550) – retain HOLD**

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**Q1 strong on healthy inflows:** KECI reported 28% YoY revenue growth to Rs 42.4bn for Q1FY24, a gross margin of 24.7% and EBITDA margin of 5.8% (+70bps YoY on lower employee costs). The company pointed to a shift in margin profile as revenues from the US business and subsidiary SAE Towers have been ramping up. Order intake stood at Rs 45bn and KECI closed the quarter with a Rs 350bn order book split equally between transmission and distribution (T&D) and other orders. The company recently won T&D orders worth Rs 10.7bn in India, Africa and the Americas.

**Guidance maintained:** Management retained its FY24 revenue guidance of Rs 200bn backed by order inflow expectations of Rs 250bn. KECI’s current addressable order pipeline totals Rs 1tn, with the share of the T&D and civil segments at 30-40% each. EBITDA margin is guided to recover from the trough of H2FY23 as legacy orders get executed in H1FY24. KECI reiterated its guidance of a ~100bps YoY rise in margin by H1 and a further 100bps improvement in H2. Net working capital cycle is guided to improve to ~110 days (vs. 126 days in Q1), with a long-term target of <100 days.

**T&D and civil projects to drive FY24:** Management expects growth in the civil business (mainly data centres, water, residential, commercial projects) and power T&D business to fuel orders in FY24. It also anticipates rail orders in the international markets of Bangladesh and Nepal. The international order book currently consists entirely of T&D projects.

**Interest cost jumps:** Interest cost increased 59% YoY to Rs 1.6bn and the company expects this to remain high in coming quarters given the RBI’s 250bps policy rate hike over the last 12 months. Debt stood at Rs 57.1bn at the end of Q1 (vs. Rs 50bn in FY23) and is expected to remain around the same level for FY24.

**Maintain HOLD:** Management has reiterated confidence in margin improvement which leads us to raise our FY24/FY25 EPS forecasts by 9%/6%. We continue to value the stock at a target P/E of 15x, a 15% discount to the 5Y average, and roll valuations forward to Jun’25E for a revised TP of Rs 630 (vs. Rs 500). The stock has run up 45% in FY24 YTD and carries little upside, leading us to retain HOLD.

## Key changes

Target	Rating
▲	◀ ▶

Ticker/Price	KECI IN/Rs 646
Market cap	US\$ 2.0bn
Free float	47%
3M ADV	US\$ 7.2mn
52wk high/low	Rs 699/Rs 387
Promoter/FPI/DII	52%/13%/26%

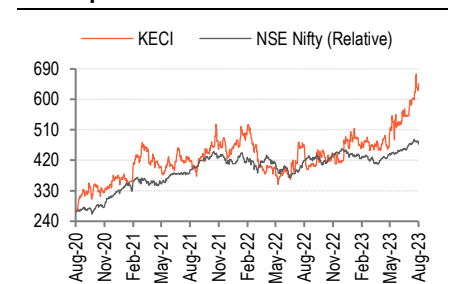
Source: NSE | Price as of 3 Aug 2023

## Key financials

Y/E 31 Mar	FY23A	FY24E	FY25E
Total revenue (Rs mn)	1,72,817	2,02,357	2,36,340
EBITDA (Rs mn)	8,297	14,423	19,543
Adj. net profit (Rs mn)	1,760	6,153	10,049
Adj. EPS (Rs)	6.8	23.9	39.1
Consensus EPS (Rs)	6.8	22.2	37.2
Adj. ROAE (%)	4.8	15.3	21.3
Adj. P/E (x)	94.4	27.0	16.5
EV/EBITDA (x)	16.6	9.4	7.3
Adj. EPS growth (%)	(53.2)	249.5	63.3

Source: Company, Bloomberg, BOBCAPS Research

## Stock performance



Source: NSE

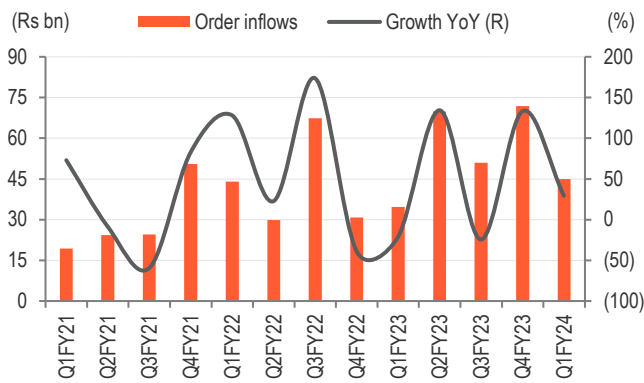


**Fig 1 – Quarterly performance**

Particulars (Rs mn)	Q1FY24	Q1FY23	YoY (%)	Q4FY23	QoQ (%)
Revenue	42,436	33,181	27.9	55,250	(23.2)
EBITDA	2,444	1,684	45.1	2,835	(13.8)
EBITDA margin (%)	5.8	5.1	70bps	5.1	60bps
Depreciation	418	393		415	
Interest	1,587	1,000		1,616	
Other Income	28	80		55	
PBT	467	371	25.8	859	(45.6)
Tax	44	61		137	
Adjusted PAT	423	310	36.5	722	(41.4)
Exceptional item	0	0		0	
Reported PAT	423	310	36.5	722	(41.4)
Adj. PAT margin (%)	1.0	0.9	10bps	1.3	(30bps)
EPS (Rs)	1.6	1.2		2.8	

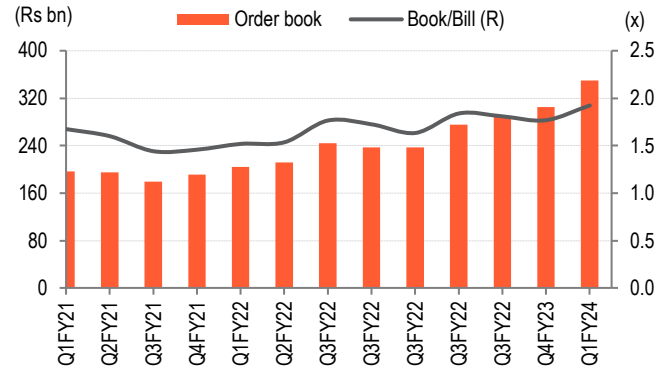
Source: Company, BOBCAPS Research

**Fig 2 – Order inflows**



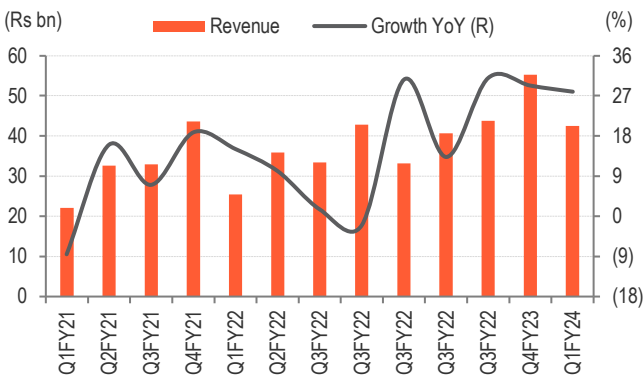
Source: Company, BOBCAPS Research

**Fig 3 – Order backlog**



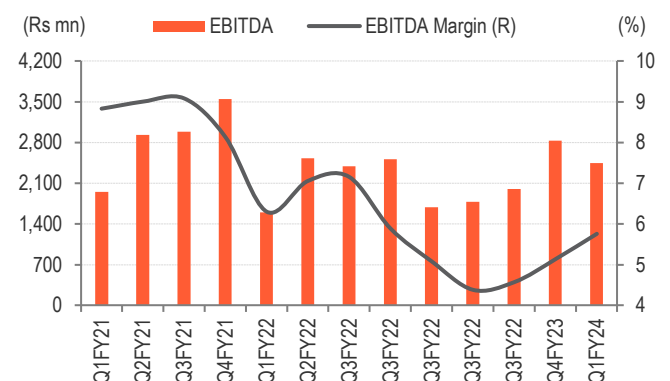
Source: Company, BOBCAPS Research

**Fig 4 – Revenue growth trend**

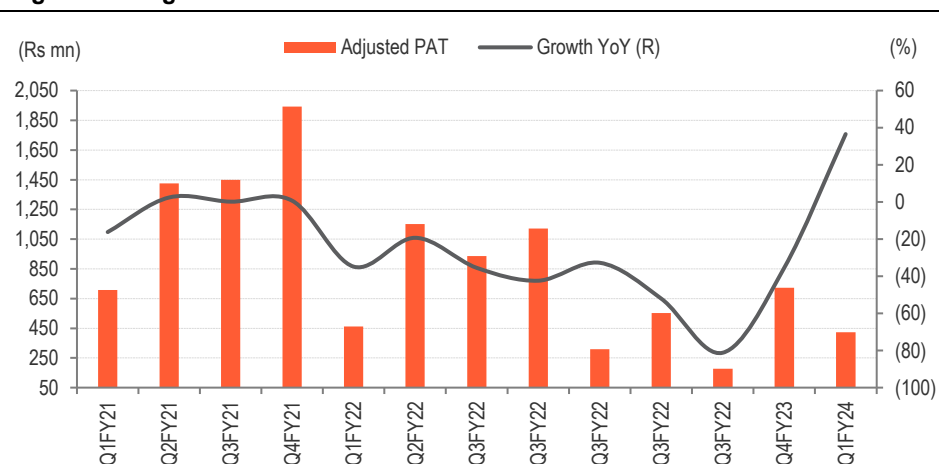


Source: Company, BOBCAPS Research

**Fig 5 – EBITDA trend**



Source: Company, BOBCAPS Research

**Fig 6 – Profit growth trend**

Source: Company, BOBCAPS Research

## Earnings call highlights

- Demand:** KECI is seeing unprecedented developments in the data centre segment and currently has four such projects under its purview. The company plans to expand further in this segment going forward. This apart, it is receiving enquiries from the residential and commercial sectors apart from continued momentum in the metals and mining sector. Additionally, the FMCG space has seen a rise in customer interest, which may be attributable to the rural pickup in the country.
- Order intake:** KECI garnered Rs 45bn in orders during Q1FY24 and expects inflows of Rs 250bn for FY24, including Rs 80bn in the civil segment.
- Margin:** Management is bullish on margins and also expects the revenue mix to improve.
- Renewables:** In the T&D segment, KECI is seeing traction in Gujarat and Rajasthan, where new renewable capacities are coming up. The company also has a 600MW solar project in Karnataka. It plans to undertake more orders in the solar segment, but maintains a no-module-risk policy to shield itself from volatility in the modules business globally.
- Competition:** Competition varies by the size of orders tendered. Smaller orders such as transmission lines typically have as many as 8-9 players in the fray. On the other hand, bigger orders for substations, especially for gas insulated substations (GIS), have competition limited to 3-4 players.
- International business:** KECI's order book in the international market is strong with a robust pipeline. The annual revenue rate is close to Rs 10bn in the Middle East region (including Dubai). Within SAARC, Nepal has started putting out several tenders, and management expects these to be bid out during 2023.
- Dubai plant:** With a 40,000t capacity, the company's Dubai plant has annual revenue potential of Rs 4bn-5bn, assuming realisations at Rs 100,000/t. Margins in this subsidiary are close to double-digits now due to benefits from the fall in steel prices.

- **Debt and working capital:** Debt stood at Rs 57.1bn at the end of Jun'23, up from Rs 50bn at the end of March. Management does not anticipate a further increase in debt to achieve its Rs 200bn revenue target. On the working capital side, it expects the cycle of 126 days during the quarter to reduce to 110 days in coming quarters.

## Valuation methodology

A burgeoning order book (Rs 350bn as at end-Q1FY24) and structural industry tailwinds bode well for KECI. Management has reiterated confidence in improving the company's operating margin, working capital and debt levels, which leads us to raise our FY24/FY25 EPS forecasts by 9%/6%.

We continue to value the stock at a target P/E of 15x, a 15% discount to the five-year average, and roll valuations forward to Jun'25E for a revised TP of Rs 630 (vs. Rs 500). The stock has run up 45% in FY24 YTD and 20% since our **last update** of 15 June, leading us to retain HOLD.

**Fig 7 – Revised estimates**

Particulars (Rs mn)	New		Old		Change (%)	
	FY24E	FY25E	FY24E	FY25E	FY24E	FY25E
Sales	2,02,357	2,36,340	2,02,357	2,36,340	0.0	0.0
EBITDA	14,423	19,543	13,747	18,742	4.9	4.3
PAT	6,153	10,049	5,647	9,450	9.0	6.3
EPS	23.9	39.1	22.0	36.8	9.0	6.3
EBITDA margin (%)	7.1	8.3	6.8	7.9	30bps	30bps

Source: Company, BOBCAPS Research

## Key risks

- Above-anticipated margin recovery is a key upside risk to our estimates.
- Weakness in margins and elevated working capital are key downside risks.

## Sector recommendation snapshot

Company	Ticker	Market Cap (US\$ bn)	Price (Rs)	Target (Rs)	Rating
ABB India	ABB IN	11.3	4,373	3,700	HOLD
AIA Engineering	AIAE IN	3.9	3,418	4,000	BUY
Cummins India	KKC IN	6.3	1,881	2,000	BUY
Hitachi Energy	POWERIND IN	2.2	4,276	4,400	HOLD
KEC International	KECI IN	2.0	646	630	HOLD
Larsen & Toubro	LT IN	44.4	2,598	3,000	BUY
Siemens India	SIEM IN	16.4	3,795	3,700	HOLD
Thermax	TMX IN	3.7	2,530	2,600	HOLD

Source: BOBCAPS Research, NSE | Price as of 3 Aug 2023

## Financials

### Income Statement

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23A	FY24E	FY25E
<b>Total revenue</b>	<b>1,31,142</b>	<b>1,37,423</b>	<b>1,72,817</b>	<b>2,02,357</b>	<b>2,36,340</b>
EBITDA	11,412	9,035	8,297	14,423	19,543
Depreciation	1,525	1,579	1,615	1,679	1,747
EBIT	9,887	7,456	6,682	12,744	17,796
Net interest inc./(exp.)	2,627	3,160	5,386	4,857	4,727
Other inc./(exp.)	299	134	313	338	365
Exceptional items	0	0	0	0	0
EBT	7,559	4,431	1,610	8,225	13,435
Income taxes	2,032	674	(151)	2,073	3,386
Extraordinary items	0	436	0	0	0
Min. int./Inc. from assoc.	0	0	0	0	0
<b>Reported net profit</b>	<b>5,527</b>	<b>3,321</b>	<b>1,760</b>	<b>6,153</b>	<b>10,049</b>
Adjustments	0	436	0	0	0
<b>Adjusted net profit</b>	<b>5,527</b>	<b>3,757</b>	<b>1,760</b>	<b>6,153</b>	<b>10,049</b>

### Balance Sheet

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23A	FY24E	FY25E
Accounts payables	62,777	68,473	83,883	94,248	1,10,076
Other current liabilities	23,850	27,490	30,937	38,808	45,326
Provisions	0	0	0	0	0
Debt funds	19,565	30,646	33,834	25,500	17,500
Other liabilities	691	580	318	372	435
Equity capital	514	514	514	514	514
Reserves & surplus	33,083	35,685	37,200	42,196	51,088
Shareholders' fund	33,597	36,199	37,714	42,710	51,602
<b>Total liab. and equities</b>	<b>1,40,479</b>	<b>1,63,389</b>	<b>1,86,686</b>	<b>2,01,638</b>	<b>2,24,939</b>
Cash and cash eq.	2,492	2,619	3,442	2,506	3,907
Accounts receivables	53,858	51,061	68,961	74,290	82,881
Inventories	8,422	10,665	11,372	14,414	16,835
Other current assets	54,064	72,524	74,482	79,544	87,722
Investments	0	0	0	0	0
Net fixed assets	13,975	15,377	15,828	16,149	16,402
CWIP	179	25	115	115	115
Intangible assets	0	0	0	0	0
Deferred tax assets, net	0	0	0	0	0
Other assets	7,491	11,119	12,487	14,622	17,077
<b>Total assets</b>	<b>1,40,480</b>	<b>1,63,389</b>	<b>1,86,686</b>	<b>2,01,638</b>	<b>2,24,939</b>

### Cash Flows

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23A	FY24E	FY25E
<b>Cash flow from operations</b>	<b>8,445</b>	<b>(2,837)</b>	<b>6,067</b>	<b>12,635</b>	<b>14,951</b>
Capital expenditures	(1,801)	(1,986)	(1,626)	(2,000)	(2,000)
Change in investments	878	(116)	126	0	0
Other investing cash flows	(351)	55	147	(2,080)	(2,393)
<b>Cash flow from investing</b>	<b>(1,274)</b>	<b>(2,047)</b>	<b>(1,352)</b>	<b>(4,080)</b>	<b>(4,393)</b>
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	(564)	8,709	2,365	(8,334)	(8,000)
Interest expenses	0	0	0	0	0
Dividends paid	0	0	0	0	0
Other financing cash flows	(6,075)	(3,750)	(6,373)	(1,157)	(1,157)
<b>Cash flow from financing</b>	<b>(6,639)</b>	<b>4,959</b>	<b>(4,008)</b>	<b>(9,491)</b>	<b>(9,157)</b>
<b>Chg in cash &amp; cash eq.</b>	<b>533</b>	<b>75</b>	<b>707</b>	<b>(936)</b>	<b>1,401</b>
<b>Closing cash &amp; cash eq.</b>	<b>2,492</b>	<b>2,619</b>	<b>3,442</b>	<b>2,506</b>	<b>3,907</b>

### Per Share

Y/E 31 Mar (Rs)	FY21A	FY22A	FY23A	FY24E	FY25E
Reported EPS	21.5	12.9	6.8	23.9	39.1
Adjusted EPS	21.5	14.6	6.8	23.9	39.1
Dividend per share	4.0	4.0	3.0	4.5	4.5
Book value per share	130.7	140.8	146.7	166.1	200.7

### Valuations Ratios

Y/E 31 Mar (x)	FY21A	FY22A	FY23A	FY24E	FY25E
EV/Sales	1.1	1.1	0.8	0.7	0.6
EV/EBITDA	12.8	16.5	16.6	9.4	7.3
Adjusted P/E	30.1	44.2	94.4	27.0	16.5
P/BV	4.9	4.6	4.4	3.9	3.2

### DuPont Analysis

Y/E 31 Mar (%)	FY21A	FY22A	FY23A	FY24E	FY25E
Tax burden (Net profit/PBT)	73.1	84.8	109.3	74.8	74.8
Interest burden (PBT/EBIT)	76.5	59.4	24.1	64.5	75.5
EBIT margin (EBIT/Revenue)	7.5	5.4	3.9	6.3	7.5
Asset turnover (Rev./Avg TA)	93.4	84.1	92.6	100.4	105.1
Leverage (Avg TA/Avg Equity)	4.6	4.7	5.1	5.0	4.8
<b>Adjusted ROAE</b>	<b>18.0</b>	<b>10.8</b>	<b>4.8</b>	<b>15.3</b>	<b>21.3</b>

### Ratio Analysis

Y/E 31 Mar	FY21A	FY22A	FY23A	FY24E	FY25E
<b>YoY growth (%)</b>					
Revenue	9.6	4.8	25.8	17.1	16.8
EBITDA	(7.5)	(20.8)	(8.2)	73.8	35.5
Adjusted EPS	(2.3)	(32.0)	(53.2)	249.5	63.3
<b>Profitability &amp; Return ratios (%)</b>					
EBITDA margin	8.7	6.6	4.8	7.1	8.3
EBIT margin	7.5	5.4	3.9	6.3	7.5
Adjusted profit margin	4.2	2.7	1.0	3.0	4.3
Adjusted ROAE	18.0	10.8	4.8	15.3	21.3
ROCE	26.3	17.6	15.0	27.4	32.6
<b>Working capital days (days)</b>					
Receivables	150	136	146	134	128
Inventory	23	28	24	26	26
Payables	175	182	170	170	170
<b>Ratios (x)</b>					
Gross asset turnover	5.3	5.0	5.8	6.4	7.0
Current ratio	1.2	1.1	1.1	1.1	1.1
Net interest coverage ratio	3.8	2.4	1.2	2.6	3.8
<b>Adjusted debt/equity</b>	<b>0.1</b>	<b>0.2</b>	<b>0.2</b>	<b>0.1</b>	<b>0.1</b>

Source: Company, BOBCAPS Research | Note: TA = Total Assets

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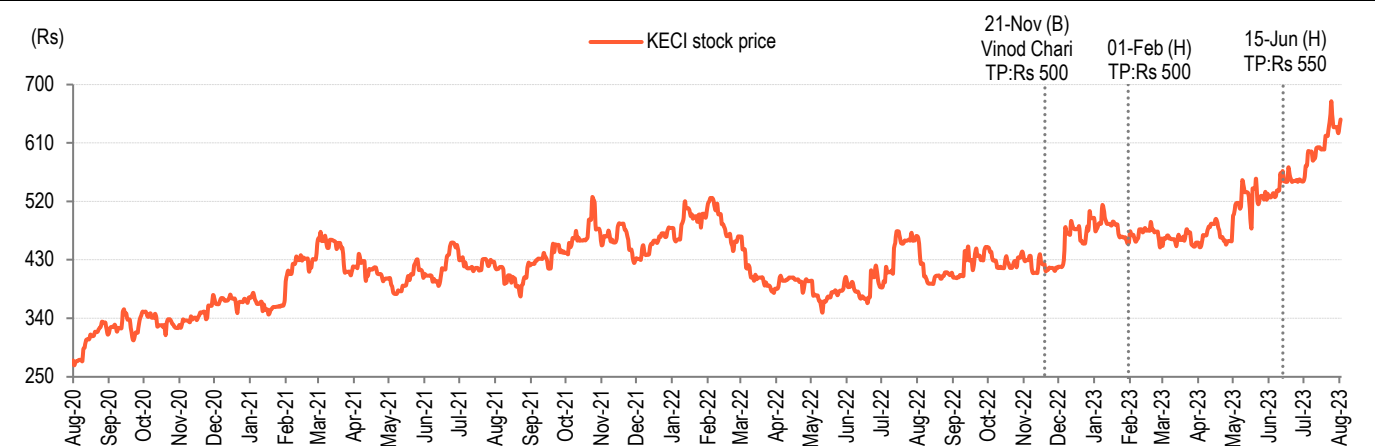
**HOLD** – Expected return from -6% to +15%

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**Note:** Recommendation structure changed with effect from 21 June 2021

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B – Buy, H – Hold, S – Sell, A – Add, R – Reduce

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