

HOLD
 TP: Rs 700 | ▲ 6%

KECI INTERNATIONAL

| Capital Goods

| 31 January 2024

Pipeline robust, margin improvement delayed

- Strong Q3 led by T&D and civil businesses, though rail revenue was subdued due to increasing competition
- Order book robust at Rs 380bn, including L1 pipeline of Rs 80bn; inflows could fall shy of Rs 250bn guided for FY24
- FY24/FY25 EPS estimates cut 18%/6% while TP rises to Rs 700 (vs. Rs 670) on rollover – retain HOLD

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Strong quarter: KECI posted a strong Q3FY24 with topline growth of 14% YoY and gross/EBITDA margin expansion of 110bps/160bps YoY to 20.7%/6.1%. Growth was led by the transmission and distribution (T&D: record Rs 220bn order book) and civil businesses (strategic FMCG and hospitality orders). The oil & gas and cables segments also fared well, with new international opportunities and product launches. On the other hand, rail business was subdued due to rising competition among tier-II/III EPC contractors and a change in client mix from public sector railway entities to zonal railway boards. Working capital improved by 10 days YoY to 129 days for Q3.

Resilient order book: KECI’s order book stood Rs 380bn at end-Q3, which includes an L1 (lowest bidder) pipeline of Rs 80bn. Order intake for the quarter and 9MFY24 was at Rs 38.5bn and Rs 128.5bn respectively. Management retained FY24 revenue guidance of Rs 200bn but believes KECI could fall slightly short of the initial order flow guidance of Rs 250bn.

T&D prospects bright, new challenges in rail: The T&D business has seen a pickup in ordering activities along with more projects and is looking at a domestic pipeline of Rs 250bn. The company expects a large HVDC order shortly. However, the shift in clientele from rail PSUs to zonal railways is likely to adversely impact margins and working capital.

Interest cost to decline: KECI’s net debt decreased by Rs 3bn QoQ to Rs 60bn as at end-Q3. Management expects a further reduction in Q4FY24 as margins and working capital improve. Additional debt of Rs 4bn in subsidiary SAE Towers is also guided to come down going forward.

Maintain HOLD: As new challenges emerge from a changing client mix, we expect margin improvement to be pushed back to FY25. Consequently, we cut our FY24/FY25 EPS estimates by 18%/6% while keeping FY26 broadly unchanged. We continue to value the stock at a P/E multiple of 15x, a 15% discount to the 5Y average, and roll valuations forward to Dec’25E for a revised TP of Rs 700 (vs. Rs 670). Our TP offers just 6.5% upside – HOLD.

Key changes

Target	Rating
▲	◀ ▶

Ticker/Price	KECI IN/Rs 658
Market cap	US\$ 2.1bn
Free float	47%
3M ADV	US\$ 3.5mn
52wk high/low	Rs 748/Rs 436
Promoter/FPI/DII	52%/13%/26%

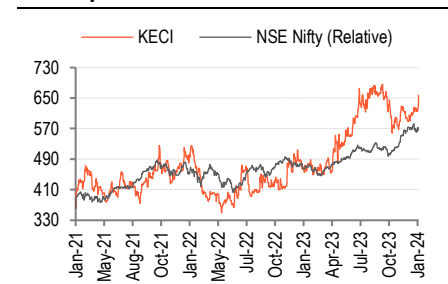
Source: NSE | Price as of 31 Jan 2024

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	13,411	18,598
Adj. net profit (Rs mn)	1,760	4,306	8,767
Adj. EPS (Rs)	6.8	16.7	34.1
Consensus EPS (Rs)	6.8	22.2	37.2
Adj. ROAE (%)	4.8	11.0	19.6
Adj. P/E (x)	96.1	39.3	19.3
EV/EBITDA (x)	17.0	10.3	7.8
Adj. EPS growth (%)	(53.2)	144.6	103.6

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE

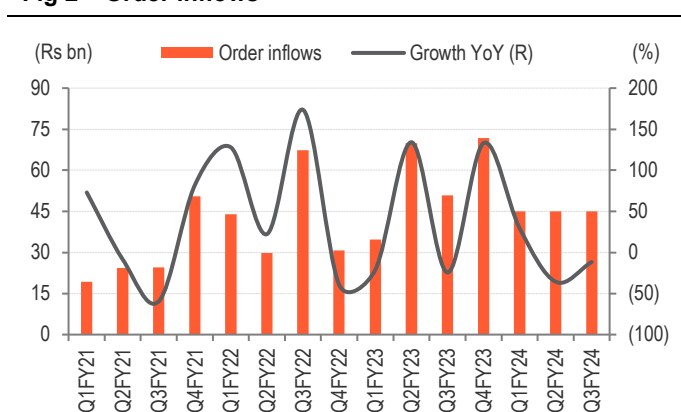


Fig 1 – Quarterly performance

Particulars (Rs mn)	Q3FY24	Q3FY23	YoY (%)	Q2FY23	QoQ (%)	9MFY24	9MFY23	YoY (%)
Revenue	50,067	43,746	14.4	44,990	11.3	1,37,493	1,17,567	16.9
EBITDA	3,079	1,999	54.0	2,743	12.2	8,266	5,463	51.3
EBITDA Margin (%)	6.1	4.6	160bps	6.1	10bps	6.0	4.6	140bps
Depreciation	488	408		465		1,371	1,200	
Interest	1,644	1,493		1,778		5,009	3,770	
Other Income	260	17		158		446	258	
PBT	1,207	114	956.2	658	83.5	2,332	751	210.5
Tax	239	(62)		100		382	(288)	
Adjusted PAT	969	176	450.4	558	73.5	1,950	1,039	87.8
Exceptional item	0	0		0		0	0	
Reported PAT	969	176	450.4	558	73.5	1,950	1,039	87.8
Adj. PAT Margin (%)	1.9	0.4	150bps	1.2	70bps	1.4	0.9	50bps
EPS (Rs)	3.8	0.7		2.2		7.6	4.0	

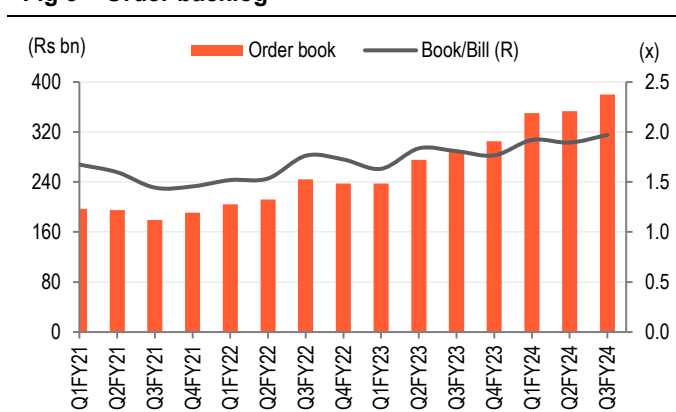
Source: Company, BOBCAPS Research

Fig 2 – Order inflows



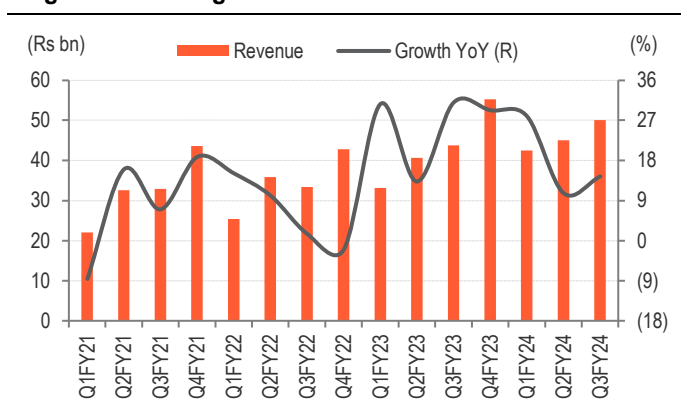
Source: Company, BOBCAPS Research

Fig 3 – Order backlog



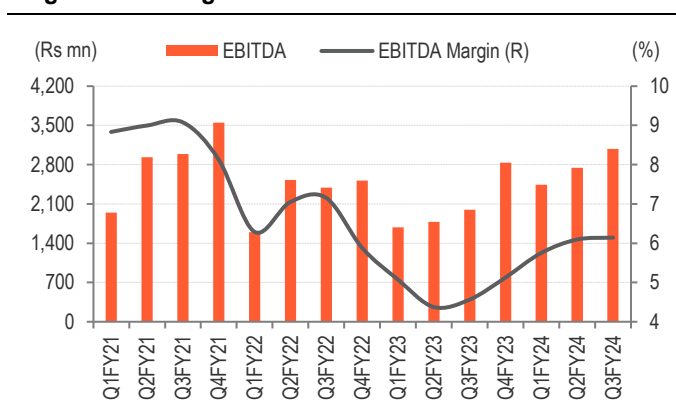
Source: Company, BOBCAPS Research

Fig 4 – Revenue growth



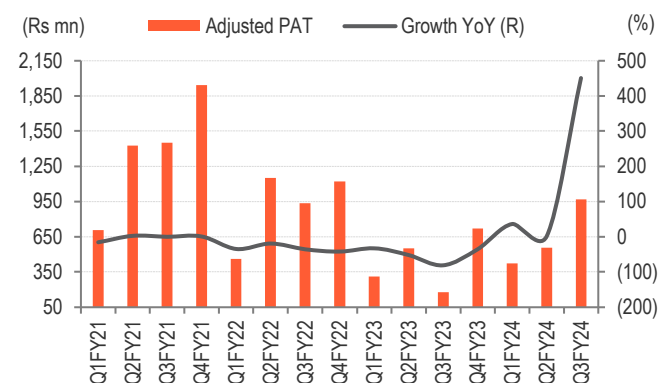
Source: Company, BOBCAPS Research

Fig 5 – EBITDA growth



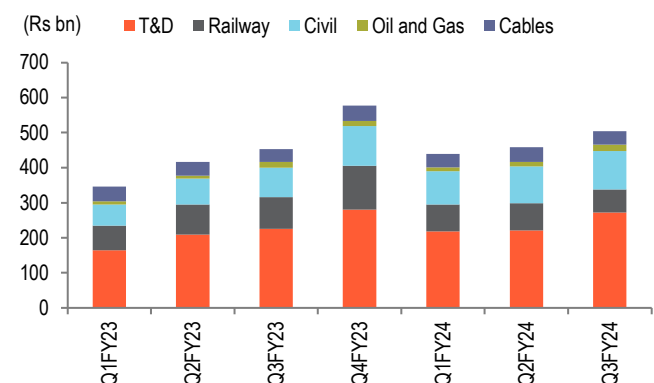
Source: Company, BOBCAPS Research

Fig 6 – Profit growth



Source: Company, BOBCAPS Research

Fig 7 – Revenue breakup



Source: Company, BOBCAPS Research

Earnings call takeaways

Business highlights

- Revenue:** KECI posted a strong revenue and margin performance during Q3FY24, and management believes growth could have been even higher but for supply chain issues, longer turnaround times along global shipping routes and higher freight costs. Growth is being driven by the civil, T&D and products supply businesses, and the company indicated that it remains watchful of its margin profile and working capital requirement while taking on new orders.
- Margins:** Management expects to close FY24 with a 20-30bps shortfall in EBITDA margin against the 7% previously guided. The company's margin profile is currently augmented by the lucrative Middle East and Brazil markets. Among its segments, cables has the best margin profile with close to double-digit margins in the T&D segment. Margins in the civil business are good but have room to improve.
- Legacy orders:** Management expects legacy orders to be executed by Q1FY24, after which it aspires to achieve double-digit margins in the T&D business.
- International market:** KECI indicated that it is witnessing multiple inquiries for supply in North America and Latin America, with large inquiries coming from Chile and Columbia as well. Africa has been a challenging market, though a few tenders have come up in the last couple of quarters. Saudi Arabia, the UAE and Oman are relatively lower competition markets given higher prequalification requirements and restrictions.
- Middle East:** KECI is expanding its Dubai tower capacity from 50,000tpa to 60,000tpa at an incremental debottlenecking cost of Rs 100mn, given strong Middle East demand. The current order book from the Middle East stands at Rs 65bn. The company's UAE subsidiary generates a topline of Rs 15bn p.a. with EBITDA margin in the range of 9-10%.
- Balance sheet:** Working capital cycle improved QoQ and YoY to 129 days for the quarter, and the company intends to end FY24 at ~110 days. Debt reduced by Rs 3bn QoQ to Rs 60bn, and management expects to close FY24 at Rs 50bn-52bn, similar to FY23 levels.

- **SAE Towers:** SAE Towers currently has Rs 4bn of debt at an average cost of borrowing of 12% p.a., which management believes will reduce going forward. The subsidiary is profitable on a pre-tax basis.

T&D

- **Orders:** The T&D segment (~60% of order book) saw strong execution in India and overseas, particularly in the Middle East, and management indicated that the current economic climate has led to one of the best years for the T&D sector. KECI saw YTD order intake of Rs 75bn in the segment, a bulk of which was from Power Grid with an execution timeline of 15 months.

The company is getting repeat orders from state utilities and reasonable orders in the UAE as it has strategically expanded its exposure in the Middle East. It is also seeing a consistent increase in tendering activities in the Middle East, besides recently garnering its largest power supply order from the US. The power supply business currently has a Rs 25bn order book.

- **Semiconductors:** Global demand for aluminium semiconductors has increased sharply for use in renewable energy and transmission lines. KECI is expanding its Baroda plant to manufacture aluminium semiconductors at an outlay of Rs 600mn, which is due to become operational in a few quarters. Post expansion, the company will be able to manufacture AL59 and ACSR conductors as well.
- **Pipeline:** Management sees substantial opportunities in the domestic market to the tune of ~Rs 250bn, including in the states of Gujarat, Rajasthan and Madhya Pradesh where several tenders have been floated. These are expected to be awarded in a few quarters, apart from a large potential HVDC project. TBCB projects by Power Grid and 30-35 upcoming tenders in the renewable energy sector for transmission lines are other visible opportunities. KECI sees strong sustainable growth in the T&D segment.

Civil business

- **Performance:** The civil business delivered robust project execution, with a YTD order intake of Rs 25bn and order book of Rs 110bn. KECI is the L1 bidder for many projects in the metals and mining, residential and commercial buildings, and water sectors. It has also received an order to develop a hybrid real estate structure from a real estate developer. Management expects to grow handsomely to the tune of 25-30% in the civil segment in FY25.
- **Order inflows:** YTD FY24 order intake came in below management estimates for this segment. Given the overenthusiastic demand in the T&D sector, KECI turned more stringent on threshold limits in its civil and railways segments.
- **Impact of elections:** The company expects slower tender announcements from Mar'24 as elections approach. During the month of elections, public projects which require ground support from government officials may be affected, though private and smaller projects will continue as usual. Post elections, new tenders are unlikely to be opened or awarded for a few months.

Valuation methodology

As new challenges emerge from a changing client mix in the rail segment, we expect margin improvement to be pushed back to FY25. Consequently, we cut our FY24/FY25 EPS estimates by 18%/6% while keeping FY26 broadly unchanged. We continue to value the stock at a P/E multiple of 15x, a 15% discount to the five-year average, and roll valuations forward to Dec'25E for a revised TP of Rs 700 (vs. Rs 670). Our TP offers just 6.5% upside – maintain HOLD.

Fig 8 – Revised estimates

Particulars (Rs mn)	New			Old			Change (%)		
	FY24E	FY25E	FY26E	FY24E	FY25E	FY26E	FY24E	FY25E	FY26E
Sales	2,02,357	2,36,340	2,76,515	2,02,357	2,36,340	2,76,515	0.0	0.0	0.0
EBITDA	13,411	18,598	24,044	14,423	19,543	24,044	(7.0)	(4.8)	0.0
PAT	4,306	8,767	12,308	5,244	9,342	12,164	(17.9)	(6.2)	1.2
EPS	16.7	34.1	47.9	20.4	36.3	47.3	(17.9)	(6.2)	1.2
EBITDA Margin (%)	6.6	7.9	8.7	7.1	8.3	8.7	(50bps)	(40bps)	0bps

Source: Company, BOBCAPS Research

Key risks

- Above-anticipated margin recovery is a key upside risk to our estimates.
- International geopolitical instability, increased freight hurdles, 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	12.0	4,672	4,700	HOLD
Hitachi Energy	POWERIND IN	3.1	5,930	4,200	SELL
KEC International	KECI IN	2.1	658	700	HOLD
Larsen & Toubro	LT IN	59.5	3,480	4,200	BUY
Siemens India	SIEM IN	17.9	4,140	4,600	BUY
Thermax	TMX IN	4.6	3,181	3,000	HOLD

Source: BOBCAPS Research, NSE | Price as of 31 Jan 2024

Glossary

Glossary of Abbreviations			
AL59	Aluminium-Magnesium-Silica Rods	TBCB	Tariff-Based Competitive Bidding
ACSR	Aluminium Conductor Steel Reinforced	L1	Lowest Bidder
HVDC	High Voltage Direct Current		

Financials

Income Statement

Y/E 31 Mar (Rs mn)	FY22A	FY23A	FY24E	FY25E	FY26E
Total revenue	1,37,423	1,72,817	2,02,357	2,36,340	2,76,515
EBITDA	9,035	8,297	13,411	18,598	24,044
Depreciation	1,579	1,615	1,712	1,780	1,851
EBIT	7,456	6,682	11,700	16,818	22,193
Net interest inc./(exp.)	3,160	5,386	6,475	5,672	6,360
Other inc./(exp.)	134	313	532	575	621
Exceptional items	0	0	0	0	1
EBT	4,431	1,610	5,757	11,720	16,454
Income taxes	674	(151)	1,451	2,954	4,146
Extraordinary items	436	0	0	0	0
Min. int./Inc. from assoc.	0	0	0	0	0
Reported net profit	3,321	1,760	4,306	8,767	12,308
Adjustments	436	0	0	0	0
Adjusted net profit	3,757	1,760	4,306	8,767	12,308

Balance Sheet

Y/E 31 Mar (Rs mn)	FY22A	FY23A	FY24E	FY25E	FY26E
Accounts payables	68,473	83,883	94,248	1,10,076	1,28,788
Other current liabilities	27,490	30,937	38,808	45,326	53,030
Provisions	0	0	0	0	1
Debt funds	30,646	33,834	25,500	17,500	17,500
Other liabilities	580	318	372	435	508
Equity capital	514	514	514	514	514
Reserves & surplus	35,685	37,200	40,349	47,959	59,110
Shareholders' fund	36,199	37,714	40,863	48,473	59,624
Total liab. and equities	1,63,389	1,86,686	1,99,792	2,21,810	2,59,452
Cash and cash eq.	2,619	3,442	691	843	3,571
Accounts receivables	51,061	68,961	74,290	82,881	96,970
Inventories	10,665	11,372	14,414	16,835	19,697
Other current assets	72,524	74,482	79,544	87,722	1,02,634
Investments	0	0	0	0	0
Net fixed assets	15,377	15,828	16,116	16,336	16,485
CWIP	25	115	115	115	115
Intangible assets	0	0	0	0	0
Deferred tax assets, net	0	0	0	0	0
Other assets	11,119	12,487	14,622	17,077	19,980
Total assets	1,63,389	1,86,686	1,99,792	2,21,810	2,59,451

Cash Flows

Y/E 31 Mar (Rs mn)	FY22A	FY23A	FY24E	FY25E	FY26E
Cash flow from operations	(2,837)	6,067	10,820	13,702	8,713
Capital expenditures	(1,986)	(1,626)	(2,000)	(2,000)	(2,000)
Change in investments	(116)	126	0	0	0
Other investing cash flows	55	147	(2,080)	(2,393)	(2,829)
Cash flow from investing	(2,047)	(1,352)	(4,080)	(4,393)	(4,829)
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	8,709	2,365	(8,334)	(8,000)	0
Interest expenses	0	0	0	0	0
Dividends paid	0	0	0	0	0
Other financing cash flows	(3,750)	(6,373)	(1,157)	(1,157)	(1,157)
Cash flow from financing	4,959	(4,008)	(9,491)	(9,157)	(1,157)
Chg in cash & cash eq.	75	707	(2,750)	152	2,727
Closing cash & cash eq.	2,619	3,442	691	843	3,571

Per Share

Y/E 31 Mar (Rs)	FY22A	FY23A	FY24E	FY25E	FY26E
Reported EPS	12.9	6.8	16.7	34.1	47.9
Adjusted EPS	14.6	6.8	16.7	34.1	47.9
Dividend per share	4.0	3.0	4.5	4.5	4.5
Book value per share	140.8	146.7	158.9	188.5	231.9

Valuations Ratios

Y/E 31 Mar (x)	FY22A	FY23A	FY24E	FY25E	FY26E
EV/Sales	1.1	0.8	0.7	0.6	0.6
EV/EBITDA	16.8	17.0	10.3	7.8	6.3
Adjusted P/E	45.0	96.1	39.3	19.3	13.7
P/BV	4.7	4.5	4.1	3.5	2.8

DuPont Analysis

Y/E 31 Mar (%)	FY22A	FY23A	FY24E	FY25E	FY26E
Tax burden (Net profit/PBT)	84.8	109.3	74.8	74.8	74.8
Interest burden (PBT/EBIT)	59.4	24.1	49.2	69.7	74.1
EBIT margin (EBIT/Revenue)	5.4	3.9	5.8	7.1	8.0
Asset turnover (Rev./Avg TA)	84.1	92.6	101.3	106.6	106.6
Leverage (Avg TA/Avg Equity)	4.7	5.1	5.1	5.0	4.8
Adjusted ROAE	10.8	4.8	11.0	19.6	22.8

Ratio Analysis

Y/E 31 Mar	FY22A	FY23A	FY24E	FY25E	FY26E
YoY growth (%)					
Revenue	4.8	25.8	17.1	16.8	17.0
EBITDA	(20.8)	(8.2)	61.6	38.7	29.3
Adjusted EPS	(32.0)	(53.2)	144.6	103.6	40.4
Profitability & Return ratios (%)					
EBITDA margin	6.6	4.8	6.6	7.9	8.7
EBIT margin	5.4	3.9	5.8	7.1	8.0
Adjusted profit margin	2.7	1.0	2.1	3.7	4.5
Adjusted ROAE	10.8	4.8	11.0	19.6	22.8
ROCE	17.6	15.0	26.2	32.7	35.4
Working capital days (days)					
Receivables	136	146	134	128	128
Inventory	28	24	26	26	26
Payables	182	170	170	170	170
Ratios (x)					
Gross asset turnover	5.0	5.8	6.4	7.0	7.7
Current ratio	1.1	1.1	1.1	1.1	1.1
Net interest coverage ratio	2.4	1.2	1.8	3.0	3.5
Adjusted debt/equity	0.2	0.2	0.1	0.1	0.1

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

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BUY – Expected return >+15%

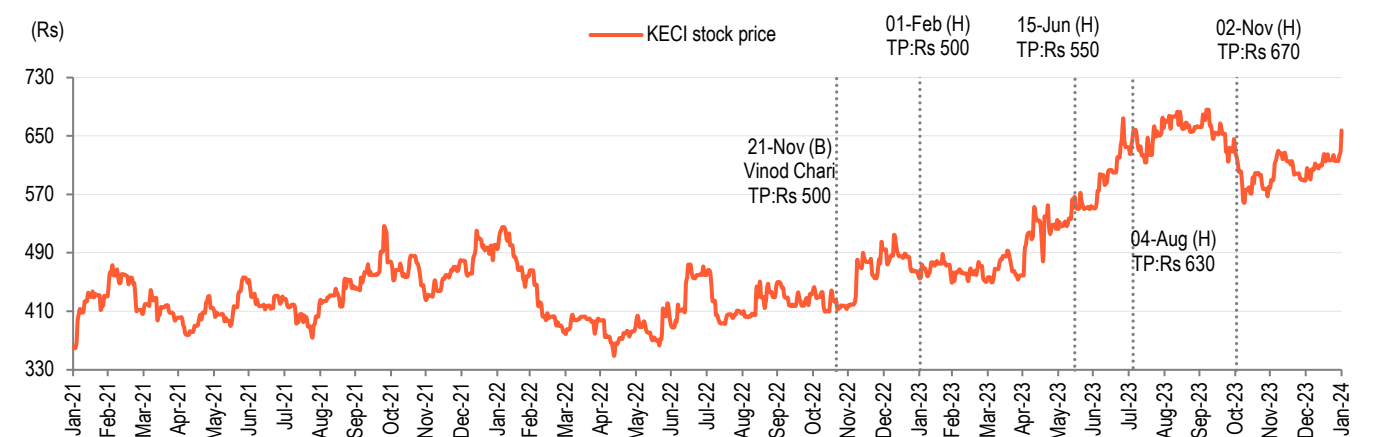
HOLD – Expected return from -6% to +15%

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

Our recommendation scale does not factor in short-term stock price volatility related to market fluctuations. Thus, our recommendations may not always be strictly in line with the recommendation scale as shown above.

Ratings and Target Price (3-year history): KEC INTERNATIONAL (KECI IN)



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

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