

**HOLD**

TP: Rs 500 | ▼ 3%

**KECI INTERNATIONAL**

| Capital Goods

| 04 May 2023

### Standalone margin remains weak

- Q4 revenue/PAT ahead of estimates at Rs 55bn/Rs 722mn; revenue growth guidance of 15%+ for FY24 on strong order inflow
- SAE Brazil now EBITDA positive but falling standalone margin a worry; full-year margin guidance at ~7%
- FY24/FY25 EPS estimates upped 4%/1%; TP unchanged at Rs 500 on rollover – maintain HOLD

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**Strong topline:** KECI's Q4FY23 topline at Rs 55.3bn (+29% YoY/+26% QoQ) was 14% ahead of our expectations led by strong growth in both the T&D and non-T&D businesses. Order traction continued for the T&D and civil segments. Consolidated EBITDA margin expanded sequentially while the standalone margin fell further. Adj. PAT stood at Rs 722mn (-36% YoY), ahead of our estimate of Rs 578mn. KECI aims to lower interest cost by 50bps in FY24 from 3.1% in FY23.

**Standalone margin slips further:** The company in Q4 posted its second quarter of sequential margin expansion following steady deterioration in the recent past. Consolidated EBITDA margin at 5.1% rose 60bps QoQ but dipped 80bps YoY. The standalone margin continued to slip further, clocking in at 4.1% (-310bps YoY, -50bps QoQ), as delayed clearances for some legacy orders weighed on profitability. With SAE Brazil turning EBITDA-positive in Q4 and newer order flows at higher rates, management expects a pronounced margin recovery in FY24.

**Healthy guidance:** Management has guided for revenue growth in excess of 15% for FY24 anchored by strong order inflows of Rs 240bn. EBITDA margin is guided to recover from the trough of H2FY23. Management sees a ~100bps increase in margin by H1FY24, exiting FY24 at ~7%. Net working capital days are expected to improve to ~110 days, closer to KECI's long-term target of <100 days. Order inflow traction is expected to persist on the back of industry tailwinds.

**Headwinds yet to abate; maintain HOLD:** A burgeoning order book of Rs 300bn+ and structural industry tailwinds bode well for KECI. However, margin recovery, debt and working capital management remain concerns. Additionally, pending recoveries from the Middle East pose a risk. We raise our FY24/FY25 EPS estimates by 4%/1% to bake in the Q4FY23 performance and roll valuations over to Mar'25E, which keeps our TP unchanged at Rs 500. We continue to value the stock at a 14x P/E multiple – a 20% discount to the five-year average – and maintain HOLD.

### Key changes

| Target | Rating |
|--------|--------|
| ◀ ▶    | ◀ ▶    |

|                  |                |
|------------------|----------------|
| Ticker/Price     | KECI IN/Rs 514 |
| Market cap       | US\$ 1.6bn     |
| Free float       | 47%            |
| 3M ADV           | US\$ 1.9mn     |
| 52wk high/low    | Rs 526/Rs 346  |
| Promoter/FPI/DII | 52%/13%/26%    |

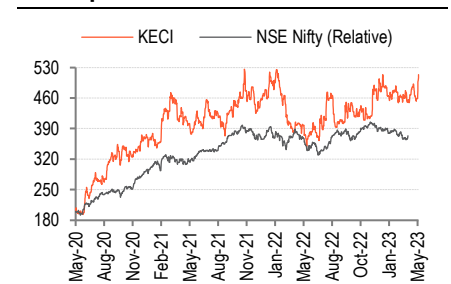
Source: NSE | Price as of 4 May 2023

### Key financials

| Y/E 31 Mar              | FY23P   | FY24E   | FY25E   |
|-------------------------|---------|---------|---------|
| Total revenue (Rs mn)   | 172,817 | 202,357 | 236,340 |
| EBITDA (Rs mn)          | 8,297   | 13,747  | 18,742  |
| Adj. net profit (Rs mn) | 1,760   | 5,647   | 9,450   |
| Adj. EPS (Rs)           | 6.8     | 22.0    | 36.8    |
| Consensus EPS (Rs)      | 6.8     | 25.5    | 37.7    |
| Adj. ROAE (%)           | 4.8     | 14.1    | 20.4    |
| Adj. P/E (x)            | 75.1    | 23.4    | 14.0    |
| EV/EBITDA (x)           | 12.6    | 7.4     | 5.8     |
| Adj. EPS growth (%)     | (53.2)  | 220.8   | 67.4    |

Source: Company, Bloomberg, BOBCAPS Research | P – Provisional

### Stock performance



Source: NSE



**Fig 1 – Quarterly performance**

| Particulars (Rs mn)        | Q4FY23     | Q4FY22     | YoY (%)         | Q3FY23     | QoQ (%)      | FY23       | FY22       | YoY (%)         |
|----------------------------|------------|------------|-----------------|------------|--------------|------------|------------|-----------------|
| Revenue                    | 55,250     | 42,748     | 29.2            | 43,746     | 26.3         | 172,817    | 137,423    | 25.8            |
| EBITDA                     | 2,835      | 2,517      | 12.6            | 1,999      | 41.8         | 8,297      | 9,035      | (8.2)           |
| <b>EBITDA Margin (%)</b>   | <b>5.1</b> | <b>5.9</b> | <b>(80bps)</b>  | <b>4.6</b> | <b>60bps</b> | <b>4.8</b> | <b>6.6</b> | <b>(180bps)</b> |
| Depreciation               | 415        | 419        | -               | 408        | -            | 1,615      | 1,579      | -               |
| Interest                   | 1,616      | 954        | -               | 1,493      | -            | 5,386      | 3,160      | -               |
| Other Income               | 55         | 34         | -               | 17         | -            | 313        | 134        | -               |
| PBT                        | 859        | 1,178      | (27.1)          | 114        | 651.4        | 1,610      | 4,431      | (63.7)          |
| Tax                        | 137        | 58         | -               | (62)       | -            | (151)      | 762        | -               |
| Adjusted PAT               | 722        | 1,120      | (35.6)          | 176        | 310.2        | 1,761      | 3,669      | (52.0)          |
| Exceptional item           | 0          | 0          | -               | 0          | -            | 0          | 348        | -               |
| Reported PAT               | 722        | 1,120      | (35.6)          | 176        | 310.2        | 1,761      | 3,321      | (47.0)          |
| <b>Adj. PAT Margin (%)</b> | <b>1.3</b> | <b>2.6</b> | <b>(130bps)</b> | <b>0.4</b> | <b>90bps</b> | <b>1.0</b> | <b>2.7</b> | <b>(170bps)</b> |
| EPS (Rs)                   | 2.8        | 4.4        | -               | 0.7        | -            | 6.8        | 14.3       | -               |

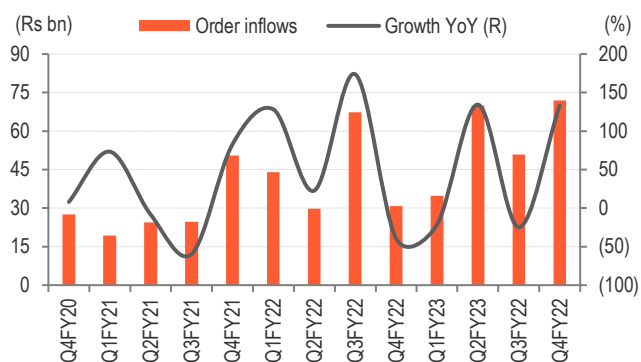
Source: BOBCAPS Research, Company

**Fig 2 – Actual vs. Estimates**

| Particulars | Actual | Estimates | Variance (%) |
|-------------|--------|-----------|--------------|
| Revenue     | 55,250 | 48,359    | 14.2         |
| EBITDA      | 2,835  | 2,515     | 12.7         |
| EBITDAM (%) | 5.1    | 5.2       | (10bps)      |
| Adj. PAT    | 722    | 578       | 24.9         |

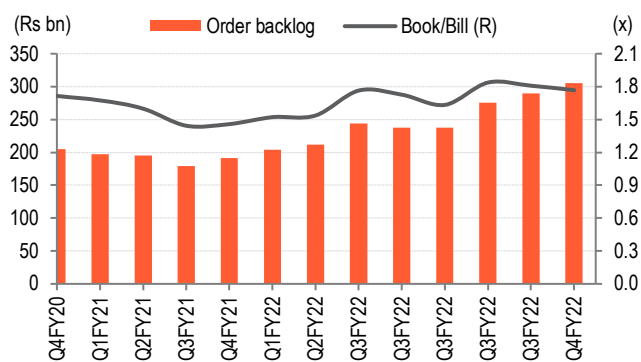
Source: Company, BOBCAPS Research

**Fig 3 – Order inflows**



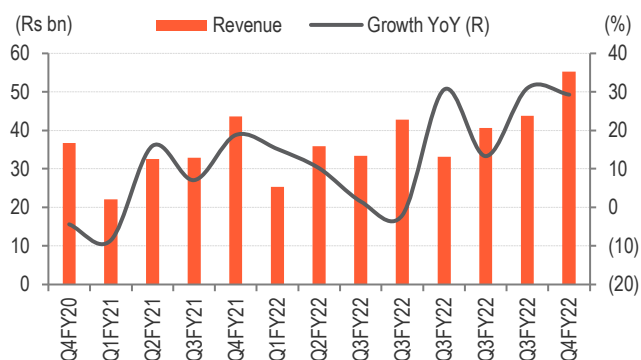
Source: Company, BOBCAPS Research

**Fig 4 – Order backlog**



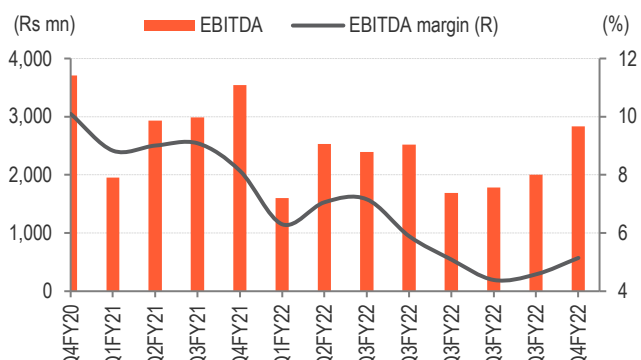
Source: Company, BOBCAPS Research

**Fig 5 – Revenue trend**

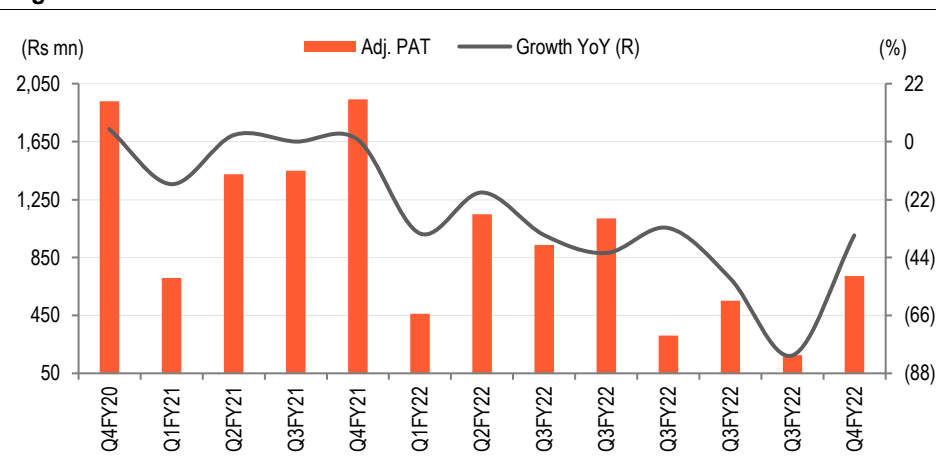


Source: Company, BOBCAPS Research

**Fig 6 – EBITDA trend**



Source: Company, BOBCAPS Research

**Fig 7 – Profit trend**

Source: Company, BOBCAPS Research

## Earnings call takeaways

- Revenue:** Q4FY23 saw peak revenues for KECI, mostly volume-driven. The company expects growth in excess of 15% for FY24 given its current Rs 305bn order book and its lowest bidder (L1) status for additional orders worth Rs 40bn.
- Margins:** EBITDA margin for FY23 hovered around 5%, which KECI expects will rise by 50bps each in Q1 and Q2 of FY24. H2 is guided at 8%, bringing the full-year margin to ~7%. The transmission & distribution (T&D) business has been a drag with segmental margins in the low single digits, but management expects a revival in Q1. Non-T&D projects earn an ~8% operating margin and cables have lower EBITDA but high ROCE margins. Per management, the new order intake carries margins in the range of 8-10%.
- Orders and Demand:** Management expects ~Rs 250bn of order intake in FY24. T&D orders are likely to flow in for wind energy projects, located mainly in Gujarat where several solar and hybrid projects are coming up. Various tariff-based competitive bidding (TBCB) schemes are also under bidding. Data centres, large buildings, and *Vande Bharat* infrastructure modification are other areas of potential demand.

In the international business, Saudi Arabia and the UAE have a good pipeline from a one-year perspective. The company believes that the plethora of current orders has reduced the competitive intensity as well.

- Afghanistan receivables:** KECI has received Rs 500mn of Afghanistan dues, and the balance Rs 1.5bn is expected in May. Upon receipt, gross and net receivables of Rs 4bn and Rs 2.5bn respectively will be outstanding, which the company expects to recover by FY24-end.
- Working capital and Debt:** KECI aspires to reach 100 days of working capital. Interest cost in FY23 was at 3.1% of sales and the company expects to bring this down by 50bps in FY24. Given its growth target of 15% in FY25, further debt reduction is unlikely. However, the impact of debt reduction achieved during Q4FY23 will be visible in lower interest costs from Q1 onwards.

## Valuation methodology

A burgeoning order book of Rs 300bn+ and structural industry tailwinds bode well for KECI. However, margin recovery, debt and working capital management remain concerns. Additionally, pending recoveries from the Middle East pose a risk.

We raise our FY24/FY25 EPS estimates by 4%/1% to bake in the Q4FY23 performance and roll valuations over to Mar'25E, which keeps our TP unchanged at Rs 500. We continue to value the stock at a 14x P/E multiple – a 20% discount to the five-year average – and maintain HOLD.

**Fig 8 – Revised estimates**

| Particulars (Rs mn) | New     |         | Old     |         | Change (%) |         |
|---------------------|---------|---------|---------|---------|------------|---------|
|                     | FY24E   | FY25E   | FY24E   | FY25E   | FY24E      | FY24E   |
| Sales               | 202,357 | 236,340 | 197,516 | 233,275 | 2.5        | 1.3     |
| EBITDA              | 13,747  | 18,742  | 13,302  | 18,554  | 3.3        | 1.0     |
| PAT                 | 5,647   | 9,450   | 5,450   | 9,409   | 3.6        | 0.4     |
| EPS (Rs)            | 22.0    | 36.8    | 21.2    | 36.6    | 3.6        | 0.4     |
| EBITDA Margin (%)   | 6.8     | 7.9     | 6.7     | 8.0     | 10bps      | (10bps) |

Source: Company, BOBCAPS Research

## Key risks

- Above-anticipated margin recovery is a key upside risk to our estimates.
- Weakness in standalone margins, a debt-heavy balance sheet 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      | 9.4                  | 3,645      | 3,220       | HOLD   |
| AIA Engineering   | AIAE IN     | 3.2                  | 2,801      | 3,300       | BUY    |
| Cummins India     | KKC IN      | 5.4                  | 1,607      | 1,600       | HOLD   |
| Hitachi Energy    | POWERIND IN | 1.8                  | 3,466      | 3,500       | BUY    |
| KEC International | KECI IN     | 1.6                  | 514        | 500         | HOLD   |
| Larsen & Toubro   | LT IN       | 40.5                 | 2,357      | 2,440       | BUY    |
| Siemens India     | SIEM IN     | 15.6                 | 3,578      | 3,800       | BUY    |
| Thermax           | TMX IN      | 3.4                  | 2,345      | 2,200       | HOLD   |

Source: BOBCAPS Research, NSE | Price as of 4 May 2023

## Financials

### Income Statement

| Y/E 31 Mar (Rs mn)         | FY21A          | FY22A          | FY23P          | FY24E          | FY25E          |
|----------------------------|----------------|----------------|----------------|----------------|----------------|
| <b>Total revenue</b>       | <b>131,142</b> | <b>137,423</b> | <b>172,817</b> | <b>202,357</b> | <b>236,340</b> |
| EBITDA                     | 11,412         | 9,035          | 8,297          | 13,747         | 18,742         |
| Depreciation               | 1,525          | 1,579          | 1,615          | 1,679          | 1,747          |
| EBIT                       | 9,887          | 7,456          | 6,682          | 12,068         | 16,996         |
| 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          | 7,549          | 12,634         |
| Income taxes               | 2,032          | 674            | (151)          | 1,902          | 3,184          |
| 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>5,647</b>   | <b>9,450</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>5,647</b>   | <b>9,450</b>   |

### Balance Sheet

| Y/E 31 Mar (Rs mn)              | FY21A          | FY22A          | FY23P          | FY24E          | FY25E          |
|---------------------------------|----------------|----------------|----------------|----------------|----------------|
| Accounts payables               | 62,777         | 68,473         | 83,883         | 94,248         | 110,076        |
| 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         | 41,690         | 49,983         |
| Shareholders' fund              | 33,597         | 36,199         | 37,714         | 42,204         | 50,498         |
| <b>Total liab. and equities</b> | <b>140,479</b> | <b>163,389</b> | <b>186,686</b> | <b>201,133</b> | <b>223,834</b> |
| Cash and cash eq.               | 2,492          | 2,619          | 3,442          | 2,000          | 2,802          |
| 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>140,480</b> | <b>163,389</b> | <b>186,686</b> | <b>201,133</b> | <b>223,834</b> |

### Cash Flows

| Y/E 31 Mar (Rs mn)                 | FY21A          | FY22A          | FY23P          | FY24E          | FY25E          |
|------------------------------------|----------------|----------------|----------------|----------------|----------------|
| <b>Cash flow from operations</b>   | <b>8,445</b>   | <b>(2,837)</b> | <b>6,067</b>   | <b>12,129</b>  | <b>14,352</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>(1,442)</b> | <b>802</b>     |
| <b>Closing cash &amp; cash eq.</b> | <b>2,492</b>   | <b>2,619</b>   | <b>3,442</b>   | <b>2,000</b>   | <b>2,802</b>   |

### Per Share

| Y/E 31 Mar (Rs)      | FY21A | FY22A | FY23P | FY24E | FY25E |
|----------------------|-------|-------|-------|-------|-------|
| Reported EPS         | 21.5  | 12.9  | 6.8   | 22.0  | 36.8  |
| Adjusted EPS         | 21.5  | 14.6  | 6.8   | 22.0  | 36.8  |
| Dividend per share   | 4.0   | 4.0   | 3.0   | 4.5   | 4.5   |
| Book value per share | 130.7 | 140.8 | 146.7 | 164.2 | 196.4 |

### Valuations Ratios

| Y/E 31 Mar (x) | FY21A | FY22A | FY23P | FY24E | FY25E |
|----------------|-------|-------|-------|-------|-------|
| EV/Sales       | 0.9   | 0.8   | 0.6   | 0.5   | 0.5   |
| EV/EBITDA      | 9.8   | 12.7  | 12.6  | 7.4   | 5.8   |
| Adjusted P/E   | 23.9  | 35.2  | 75.1  | 23.4  | 14.0  |
| P/BV           | 3.9   | 3.7   | 3.5   | 3.1   | 2.6   |

### DuPont Analysis

| Y/E 31 Mar (%)               | FY21A | FY22A | FY23P | 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  | 62.6  | 74.3  |
| EBIT margin (EBIT/Revenue)   | 7.5   | 5.4   | 3.9   | 6.0   | 7.2   |
| Asset turnover (Rev./Avg TA) | 93.4  | 84.1  | 92.6  | 100.6 | 105.6 |
| Leverage (Avg TA/Avg Equity) | 4.6   | 4.7   | 5.1   | 5.0   | 4.8   |
| Adjusted ROAE                | 18.0  | 10.8  | 4.8   | 14.1  | 20.4  |

### Ratio Analysis

| Y/E 31 Mar                                   | FY21A | FY22A  | FY23P  | FY24E | FY25E |
|----------------------------------------------|-------|--------|--------|-------|-------|
| <b>YoY growth (%)</b>                        |       |        |        |       |       |
| Revenue                                      | 9.6   | 4.8    | 25.8   | 17.1  | 16.8  |
| EBITDA                                       | (7.5) | (20.8) | (8.2)  | 65.7  | 36.3  |
| Adjusted EPS                                 | (2.3) | (32.0) | (53.2) | 220.8 | 67.4  |
| <b>Profitability &amp; Return ratios (%)</b> |       |        |        |       |       |
| EBITDA margin                                | 8.7   | 6.6    | 4.8    | 6.8   | 7.9   |
| EBIT margin                                  | 7.5   | 5.4    | 3.9    | 6.0   | 7.2   |
| Adjusted profit margin                       | 4.2   | 2.7    | 1.0    | 2.8   | 4.0   |
| Adjusted ROAE                                | 18.0  | 10.8   | 4.8    | 14.1  | 20.4  |
| ROCE                                         | 26.3  | 17.6   | 15.0   | 26.2  | 31.8  |
| <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    | 2.5   | 3.6   |
| Adjusted debt/equity                         | 0.1   | 0.2    | 0.2    | 0.1   | 0.1   |

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

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SEBI Research Analyst Registration No: **INH000000040 valid till 03 February 2025**

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**BUY** – Expected return >+15%

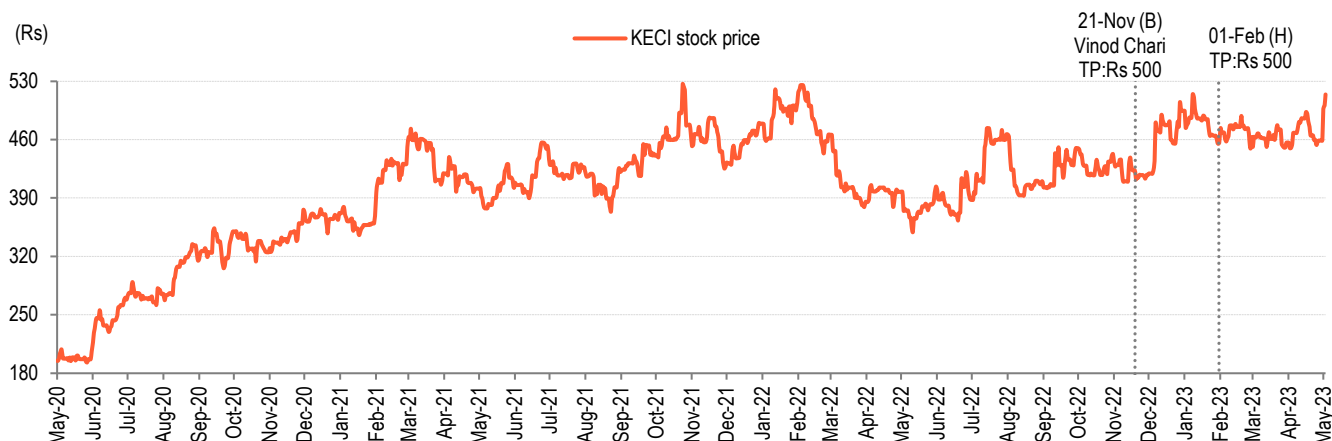
**HOLD** – Expected return from -6% to +15%

**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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