RESULT REVIEW

BOBCAPS
TRUST | INNOVATION | EXCELLENCE

BUY
TP: Rs 860 | ⮝ 16%

KEC INTERNATIONAL | Capital Goods | 08 May 2024

Good quarter, T&D to pull topline and margins; upgrade to BUY

- **Strong quarter with highest quarterly revenues of Rs 61.6bn, +11.6% YoY; management guides for 15% revenue growth in FY25**
- **EBITDA margin for Q4 at 6.3%, management expects 7.5% margin in FY25 with exit margin of 9%; order inflows guided at Rs 250bn for FY25**
- **We maintain our EPS estimates and value the stock at 18x FY26E EPS (16x earlier) and arrive at a revised TP of Rs 860; upgrade to BUY**

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Healthy quarter: KEC achieved its highest-ever revenues in Q4FY24 with a topline of Rs 61.6bn, 11.6% growth YoY, and FY24 revenue grew 15.2% YoY to Rs 199.1bn. EBITDA margin expanded 120bps to 6.3% in Q4FY24 and 130bps to 6.1% in FY24. Adjusted PAT stood at Rs 1.5bn for Q4 and Rs 3.5bn for FY24. The strong performance was supported by robust execution, strong traction in the Transmission & Distribution (T&D) business, and healthy international performance.

Strong order pipeline: Order book stood at Rs 370bn at the end of FY24 with order inflows of Rs 181bn during FY24. The largest contributors to inflows were Indian T&D business, international T&D business, followed by civil business. Management expects to clock inflows of Rs 250bn in FY25. Management sees an opportunity size of Rs 700bn in the domestic T&D market and Rs 400bn in the international T&D market.

T&D prospects bright, India in focus: The T&D business has seen a pickup in ordering activities along with more projects and is looking at a potential domestic pipeline of Rs 700bn. The company expects the international business to continue its strong performance with healthy performance in SAE Towers as well. On the domestic front, KEC is very optimistic on the tendering pipeline in the Indian T&D sector with projects across thermal and renewable power projects coming into play. KEC expects to capitalise on the country's move towards clean and green energy by securing orders in the transmission space.

Order outlook bright, margins to follow suit; upgrade to BUY: KEC has a strong presence in the T&D sector, and with the government pushing both thermal and renewable energy projects, management believes KEC will benefit. Additionally, margins improved during the quarter and year, and management expects further improvement over the next two years. We largely maintain our FY25E/FY26E EPS, and increase our target P/E to 18x from 16x, in line with the stock's 5Y average P/E. Consequently, we arrive at a higher target price of Rs 860 (from Rs 700), and upgrade to BUY from HOLD.

Key changes

Target	Rating
▲	▲

Ticker/Price	KECI IN/Rs 740
Market cap	US$ 2.3bn
Free float	47%
3M ADV	US$ 8.1mn
52wk high/low	Rs 839/Rs 444
Promoter/FPI/DII	52%/13%/26%

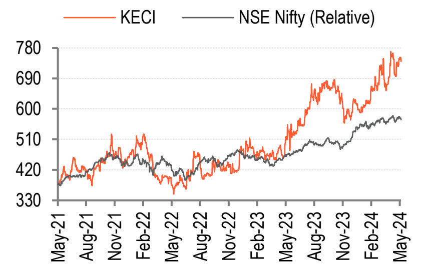
Source: NSE | Price as of 7 May 2024

Key financials

Y/E 31 Mar	FY24P	FY25E	FY26E
Total revenue (Rs mn)	1,99,142	2,29,056	2,67,686
EBITDA (Rs mn)	12,146	18,082	24,123
Adj. net profit (Rs mn)	3,468	8,704	12,329
Adj. EPS (Rs)	13.5	33.9	48.0
Consensus EPS (Rs)	13.5	35.0	43.3
Adj. ROAE (%)	8.8	19.5	22.8
Adj. P/E (x)	54.9	21.9	15.4
EV/EBITDA (x)	13.2	8.5	7.4
Adj. EPS growth (%)	97.0	151.0	41.7

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

Stock performance



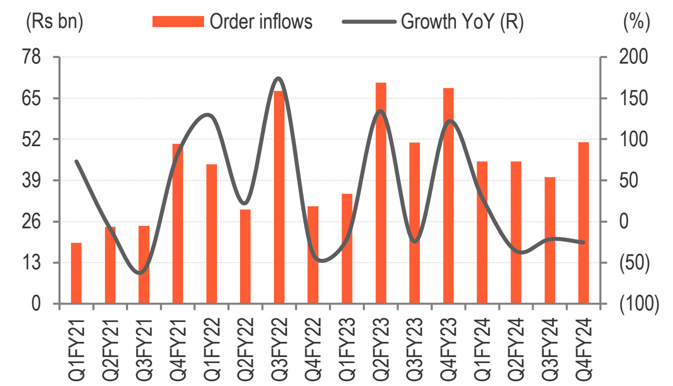
Source: NSE

Fig 1 – Quarterly performance

Particulars (Rs mn)	Q4FY24	Q4FY23	YoY (%)	Q3FY24	QoQ (%)	FY24	FY23	YoY (%)
Revenue	61,648	55,250	11.6	50,067	23.1	1,99,142	1,72,817	15.2
EBITDA	3,880	2,835	36.9	3,079	26.0	12,146	8,297	46.4
EBITDAM (%)	**6.3**	**5.1**	**120bps**	**6.1**	**10bps**	**6.1**	**4.8**	**130bps**
Depreciation	483	415		488		1,854	1,615	
Interest	1,543	1,616		1,644		6,551	5,386	
Other Income	78	55		260		524	313	
PBT	1,933	859	125.1	1,207	60.1	4,265	1,610	164.9
Tax	415	137		239		797	(151)	
Adjusted PAT	1,518	722	110.2	969	56.7	3,468	1,760	97.0
Exceptional item	0	0		0		0	0	
Reported PAT	1,518	722	110.2	969	56.7	3,468	1,760	97.0
Adj. PATM (%)	**2.5**	**1.3**	**120bps**	**1.9**	**50bps**	**1.7**	**1.0**	**70bps**
EPS (Rs)	5.9	2.8		3.8		13.5	6.8	

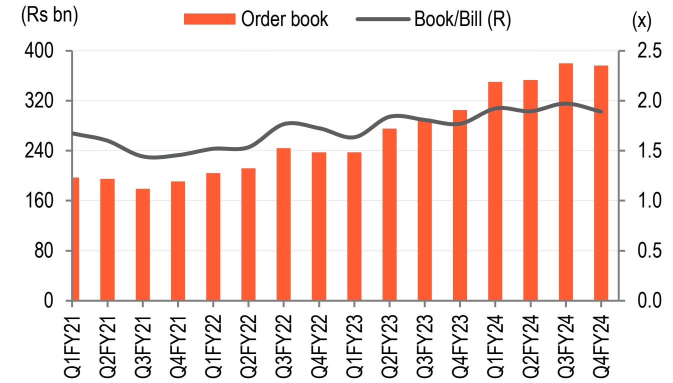
Source: Company, BOBCAPS Research

Fig 2 – Order inflows



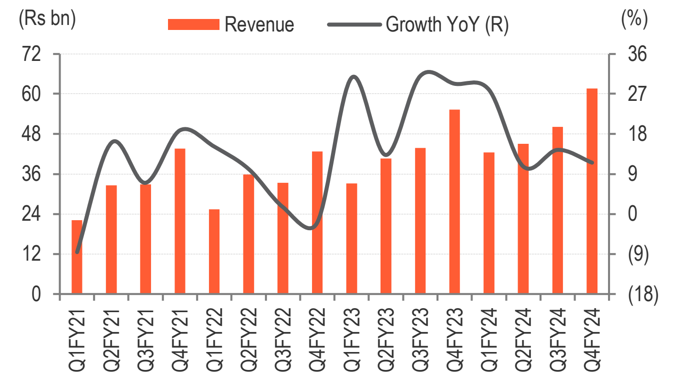
Source: Company, BOBCAPS Research

Fig 3 – Order backlog



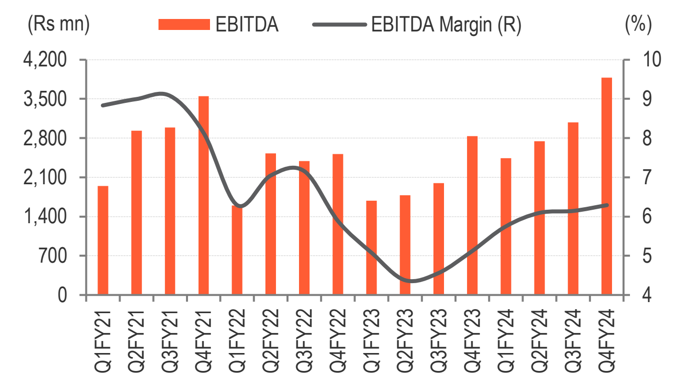
Source: Company, BOBCAPS Research

Fig 4 – Revenue growth



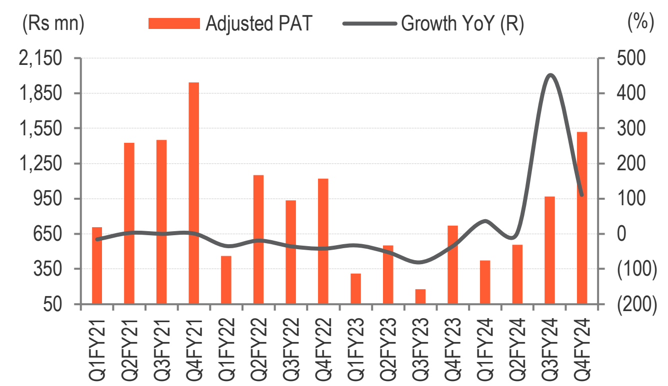
Source: Company, BOBCAPS Research

Fig 5 – EBITDA growth



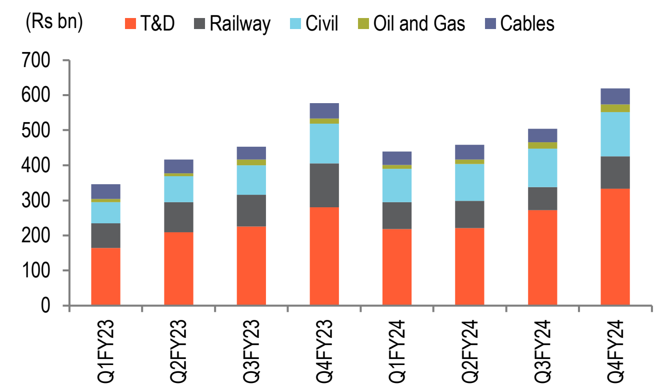
Source: Company, BOBCAPS Research

Fig 6 – Profit growth



Source: Company, BOBCAPS Research

Fig 7 – Revenue breakdown



Source: Company, BOBCAPS Research

Earnings call highlights

Business highlights

- **Profitability:** KEC ended the year with a 6.1% EBITDA margin, slightly lower than management's expectation of 6.5-7%. This was largely due to two reasons. Firstly, it witnessed the deferment of some margin-accretive revenues of Rs 4bn-5bn due to issues common to the industry and some impact of the ongoing crisis on the Red Sea route, causing a reduction of 25-30bps. Secondly, the railways segment has continued to witness execution delays, causing lower realisations within the segment. KEC took provisions here during Q4FY24, which further impacted margins.
- **Margin outlook:** Going forward, management expects margins to come back up and meet its earlier guidance. For FY25, it expects a 7.5% EBITDA margin, with exit margin for FY25 hovering around 9-10%. Going into FY26, margin of 9% can be expected, though market dynamics may move this number slightly. Management expects non-T&D margins to be slightly lower than T&D margins.
- **Oil & gas:** The segment showed healthy revenue growth with topline of Rs 6.3bn for FY24. KEC has entered into the international market with an order in Africa. It continues to focus on pre-qualification criteria to expand its addressable market here.
- **Solar:** Solar business continues to perform well, and KEC executed its largest order here in Karnataka during FY24. It has received another order to set up solar projects for an auto ancillary company. Management expects renewable energy EPC projects to be significant contributors in the future.
- **Cables:** The Cables segment achieved the highest revenue of Rs 1.65bn during FY24, and received orders from various sectors.
- **Capex:** KEC is expanding its Vadodara factory by adding a conductor line, with a capital expenditure of Rs 600mn, which is expected to be commissioned in Q3FY25. This line can generate a revenue of Rs 6bn on an annual basis.

- **Debt and working capital management:** KEC ended FY24 with a net debt of Rs 51bn. For KEC, Q1 and Q2 of any financial year typically see an increase in debt, with reductions in Q3 and Q4. Management expects debt to hover in the Rs 50bn-60bn range. Additionally, management expects collections to further improve in FY25, and have a consequent impact on revenue, interest costs and working capital cycle. The working capital cycle stood at 112 days for FY24, and management expects this to go below 100 days in a few quarters. As collections improve, refinancing and interest costs will have a positive impact too.

- **Impact of foreign exchange:** KEC had a minimal forex impact during the year, largely due to low foreign exposure. The company achieved this through hedging and borrowing in foreign currencies to manage costs.

- **Order inflows:** KEC recorded an order intake (OI) of Rs 181bn for FY24. Key contributors during the year were T&D India, T&D international, followed by the civil segment. The order intake was below management expectations of Rs 250bn, largely as KEC could not take a few L1 orders where price and cost issues arose, which would have otherwise bumped OI to Rs 220bn-230bn. Also, management was very selective in railways orders, leading to lower inflows there. Management continues to guide for a Rs 250bn OI for FY25.

- **Order book:** Order book currently stands at Rs 370bn, which provides revenue visibility for 6-8 quarters.

- **Afghanistan collections:** KEC collected another Rs 1.1bn in Afghanistan during the first week of April and expects collections to be realised in the coming quarters. The company has collected Rs 4.2bn till date.

T&D

- **Segment performance:** The T&D segment performance excelled with a topline of Rs 104.6bn for FY24, led by robust execution. Within the segment, the international business continues to perform well, with Indian business growing well too. The order book for T&D remains robust at over Rs 210bn. KEC won multiple orders in the Indian business from PWGR, state utilities and some private players.

- **Profitability:** Management expects the T&D business to clock double-digit margin by the end of FY25, furthering its margin expectations of 9% exit margin in FY25. The risk to this double-digit margin is fairly low, given that KEC has hedged its metals exposure in aluminum, zinc and copper and does not expect any significant delays in execution.

- **Indian T&D business:** Indian business picked up in FY24, and with the government push for renewable and thermal power capacity expansions, the T&D sector has seen, and will continue to see, strong growth. Within India, orders worth Rs 5bn and above have seen slightly lower competition, which has boded well for KEC. Competitors in this segment are more focused on private players, which has reduced competitive intensity for KEC.

- **Indian power sector:** Three major factors have contributed to the positive outlook in the Indian T&D sector. (1) The government is now focusing on adding thermal capacities, leading to increase in demand of transmission systems. (2) Transmission systems for renewable projects are now being bid out after approvals of solar and wind power projects are received by power generators, which was earlier being bid out once such projects were being commissioned. (3) Power demand in India is rising, leading to increased demand for transmission systems to cater to such demand. Also, new renewable packages are coming up within India, and high voltage direct current (HVDC) lines are expected to be bid out soon.

- **Segment outlook:** Management remains positive on the international business, and expects it to grow going forward. Indian business is expected to grow 40-45% for FY25, LEC is the L1 bidder for many projects in India currently.
- **Opportunity size:** Management expects a ~Rs 700bn opportunity in Indian T&D business, with Rs 250bn worth of tendering opportunities currently, and ~Rs 400bn in the international business for FY25.
- **SAE Towers:** SAE clocked a topline of Rs 14.5bn, 9% growth YoY for FY24. KEC is in active discussions with Brazil's government for supply of towers and hardware. SAE has a debt of US$ 15mn, with interest cost of 11%. Interest rates in Brazil have come down, along with management's expectations of rating upgrades for Brazil. These two factors should lead to lower finance costs for SAE.
- **International business:** International business has been growing over the last 2 years, and is expected to rise going forward. During the year, KEC won multiple orders in the Middle East, especially Saudi Arabia and UAE. KEC's debottlenecking programme in this region is going well, and with capacity expansions of ~20% performance should further improve. Demand for tower supply orders is also rising in the Middle East and Americas. Additionally, HVDC line tendering has been announced in the UAE and Saudi Arabia, which will improve business.

Civil

- **Segment performance:** Civil business did well too, with a topline of Rs 43.7bn, 32% growth YoY in FY24. Order intake here stood at Rs 42bn, as the company received multiple orders from companies in FMCG, metals & mining, cement, residential & commercial buildings and data centre sectors. KEC has also expanded its customer base in this segment.
- **Outlook:** During FY24, KEC did not receive as many water project orders, as was witnessed in FY23. Going forward, residential, industrial, private capex are expected to push topline here. Additionally, as the new government comes into effect, KEC expects better project execution as labour scarcity issues subside.

Railways

- **Quarter performance:** Margins were impacted in the railway segment, due to delays in execution. Management has been very selective in taking orders within the segment in terms of margin profile, customer profile and working capital conditions, which led to a lower order intake here.
- **Segment outlook:** Management expects a revenue de-growth of 15-20% within this segment, largely due to lower order execution, and expects revenue to rise only by Q4FY25.
- **Sector dynamics:** The rail PSUs witnessed management changes during the quarter, which led to delays in decision making, and consequently, order execution.

Going forward, as the new government comes into power, management expects a change in the spending pattern within the railways sector, with more focus on infrastructure-related spending. With this, it expects an improved performance in FY26 with a better margin profile.

Valuation methodology

KEC has a strong presence in the T&D sector, and with government pushing both thermal and renewable energy projects, management expects KEC to benefit. Margins improved during the quarter and the year, and management expects further improvement over the next two years. We largely maintain our FY25E/FY26E EPS, and increase our target P/E to 18x from 16x, in line with the stock's 5Y average P/E. Consequently, we arrive at a revised target price of Rs 860 (from Rs 700), and upgrade to BUY from HOLD.

Fig 8 – Revised Estimates

Particulars (Rs mn)	New		Old		Change (%)	
	FY25E	FY26E	FY25E	FY26E	FY25E	FY26E
Sales	2,29,056	2,67,686	2,36,340	2,76,515	(3.1)	(3.2)
EBITDA	18,082	24,123	18,598	24,044	(2.8)	0.3
PAT	8,704	12,329	8,767	12,308	(0.7)	0.2
EPS	33.9	48.0	34.1	47.9	(0.7)	0.2
EBITDAM (%)	7.9	9.0	7.9	8.7	0bps	30bps

Source: Company, BOBCAPS Research

Key risks

Key downside risk to our estimates are:

- international geopolitical instability,
- increased freight hurdles,
- weakness in margins, and
- elevated working capital requirements.

Sector recommendation snapshot

Company	Ticker	Market Cap (US$ bn)	Price (Rs)	Target (Rs)	Rating
AIA Engineering	AIAE IN	4.4	3,805	4,000	HOLD
Hitachi Energy	POWERIND IN	4.6	8,889	4,200	SELL
KEC International	KECI IN	2.3	740	860	BUY
Larsen & Toubro	LT IN	58.6	3,428	4,200	BUY

Source: BOBCAPS Research, NSE | Price as of 7 May 2024

Financials

Income Statement

Y/E 31 Mar (Rs mn)	FY22A	FY23A	FY24P	FY25E	FY26E
Total revenue	**1,37,423**	**1,72,817**	**1,99,142**	**2,29,056**	**2,67,686**
EBITDA	9,035	8,297	12,146	18,082	24,123
Depreciation	1,579	1,615	1,854	1,928	2,005
EBIT	7,456	6,682	10,292	16,154	22,118
Net interest inc./(exp.)	3,160	5,386	6,551	5,268	6,291
Other inc./(exp.)	134	313	524	566	611
Exceptional items	0	0	0	0	1
EBT	4,431	1,610	4,265	11,452	16,439
Income taxes	674	(151)	797	2,749	4,110
Extraordinary items	436	0	0	0	0
Min. int./Inc. from assoc.	0	0	0	0	0
Reported net profit	**3,321**	**1,760**	**3,468**	**8,704**	**12,329**
Adjustments	436	0	0	0	0
Adjusted net profit	**3,757**	**1,760**	**3,468**	**8,704**	**12,329**

Balance Sheet

Y/E 31 Mar (Rs mn)	FY22A	FY23A	FY24P	FY25E	FY26E
Accounts payables	68,473	83,883	92,070	1,06,684	1,24,676
Other current liabilities	27,490	30,937	17,188	43,929	51,337
Provisions	0	0	0	0	1
Debt funds	30,646	33,834	39,850	17,500	17,500
Other liabilities	580	318	250	287	336
Equity capital	514	514	514	514	514
Reserves & surplus	35,685	37,200	40,443	47,990	59,162
Shareholders' fund	36,199	37,714	40,957	48,504	59,676
Total liab. and equities	**1,63,389**	**1,86,686**	**1,90,315**	**2,16,903**	**2,53,526**
Cash and cash eq.	2,619	3,442	2,733	5,058	8,738
Accounts receivables	51,061	68,961	41,366	80,326	93,874
Inventories	10,665	11,372	12,133	16,316	19,068
Other current assets	72,524	74,482	1,05,346	84,545	98,803
Investments	0	0	0	0	0
Net fixed assets	15,377	15,828	16,283	16,355	16,350
CWIP	25	115	139	139	139
Intangible assets	0	0	0	0	0
Deferred tax assets, net	0	0	0	0	0
Other assets	11,119	12,487	12,314	14,164	16,553
Total assets	**1,63,389**	**1,86,686**	**1,90,315**	**2,16,904**	**2,53,525**

Cash Flows

Y/E 31 Mar (Rs mn)	FY22A	FY23A	FY24P	FY25E	FY26E
Cash flow from operations	**(2,837)**	**6,067**	**3,111**	**29,644**	**9,177**
Capital expenditures	(1,986)	(1,626)	(2,336)	(2,000)	(2,000)
Change in investments	(116)	126	0	0	0
Other investing cash flows	55	147	105	(1,812)	(2,340)
Cash flow from investing	**(2,047)**	**(1,352)**	**(2,231)**	**(3,812)**	**(4,340)**
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	8,709	2,365	(675)	(22,350)	0
Interest expenses	0	0	0	0	0
Dividends paid	0	0	0	0	0
Other financing cash flows	(3,750)	(6,373)	(772)	(1,157)	(1,157)
Cash flow from financing	**4,959**	**(4,008)**	**(1,447)**	**(23,507)**	**(1,157)**
Chg in cash & cash eq.	**75**	**707**	**(566)**	**2,325**	**3,680**
Closing cash & cash eq.	**2,619**	**3,442**	**2,733**	**5,058**	**8,738**

Per Share

Y/E 31 Mar (Rs)	FY22A	FY23A	FY24P	FY25E	FY26E
Reported EPS	12.9	6.8	13.5	33.9	48.0
Adjusted EPS	14.6	6.8	13.5	33.9	48.0
Dividend per share	4.0	3.0	4.0	4.5	4.5
Book value per share	140.8	146.7	159.3	188.7	232.1

Valuations Ratios

Y/E 31 Mar (x)	FY22A	FY23A	FY24P	FY25E	FY26E
EV/Sales	1.3	0.9	0.8	0.7	0.7
EV/EBITDA	19.2	19.6	13.2	8.5	7.4
Adjusted P/E	50.7	108.1	54.9	21.9	15.4
P/BV	5.3	5.0	4.6	3.9	3.2

DuPont Analysis

Y/E 31 Mar (%)	FY22A	FY23A	FY24P	FY25E	FY26E
Tax burden (Net profit/PBT)	84.8	109.3	81.3	76.0	75.0
Interest burden (PBT/EBIT)	59.4	24.1	41.4	70.9	74.3
EBIT margin (EBIT/Revenue)	5.4	3.9	5.2	7.1	8.3
Asset turnover (Rev./Avg TA)	84.1	92.6	104.6	105.6	105.6
Leverage (Avg TA/Avg Equity)	4.7	5.1	4.8	4.8	4.7
Adjusted ROAE	10.8	4.8	8.8	19.5	22.8

Ratio Analysis

Y/E 31 Mar	FY22A	FY23A	FY24P	FY25E	FY26E
YoY growth (%)					
Revenue	4.8	25.8	15.2	15.0	16.9
EBITDA	(20.8)	(8.2)	46.4	48.9	33.4
Adjusted EPS	(32.0)	(53.2)	97.0	151.0	41.7
Profitability & Return ratios (%)					
EBITDA margin	6.6	4.8	6.1	7.9	9.0
EBIT margin	5.4	3.9	5.2	7.1	8.3
Adjusted profit margin	2.7	1.0	1.7	3.8	4.6
Adjusted ROAE	10.8	4.8	8.8	19.5	22.8
ROCE	17.6	15.0	22.8	31.5	35.4
Working capital days (days)					
Receivables	136	146	76	128	128
Inventory	28	24	22	26	26
Payables	182	170	170	170	170
Ratios (x)					
Gross asset turnover	5.0	5.8	6.2	6.7	7.4
Current ratio	1.1	1.1	1.1	1.1	1.2
Net interest coverage ratio	2.4	1.2	1.6	3.1	3.5
Adjusted debt/equity	0.2	0.2	0.2	0.1	0.0

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

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Recommendation scale: Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

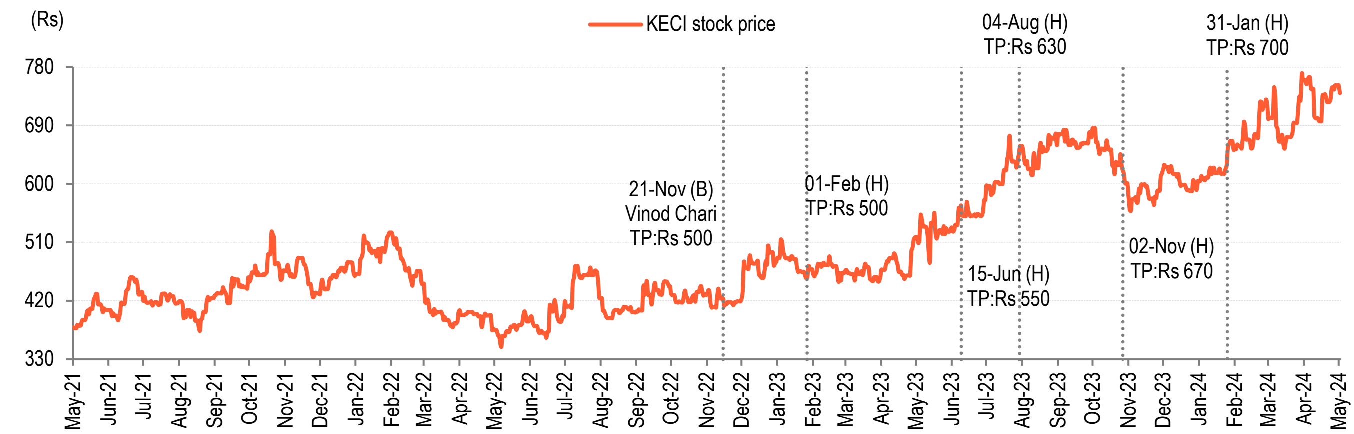
HOLD – Expected return from -6% to +15%

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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