

KNR Constructions

BUY

Doesn't stop surprising

We maintain BUY on KNR with SOTP-based TP of Rs 378/sh (valuing core EPC business 18x FY21EPS at Rs 319/sh, Subsidiaries Rs 60/sh). KNR delivered yet another robust quarter with Revenue/EBIDTA/APAT beat of 10/20/35% respectively.

HIGHLIGHTS OF THE QUARTER

- **Robust execution in seasonally weak monsoon quarter:** KNR 2QFY20 revenue grew 31/18% YoY/QoQ in a seasonally weak monsoon quarter vs most peers de-growing QoQ. New irrigation orders of Rs 17bn won in 1HFY20 contributed Rs 490mn to revenue. KNR booked Rs 232mn net arbitration claims in Rev and Rs 181mn in EBIDTA. Adjusted Rev/EBIDTA/APAT stood at Rs 5.2/1.1/0.6bn.
- **Order backlog robust at Rs 66.8bn (2.6x FY20 rev):** During 1HFY20 KNR bagged new orders worth Rs 18bn vs Rs 30bn guidance for FY20. KNR is targeting Rs 10-15bn of new NHAI EPC/HAM projects for 2HFY20E. Net executable order book as of 1HFY20 is Rs 51.4bn.
- **About 23% of order book yet to move into execution:** KNR has not included Rs 15.4bn of HAM orders in the backlog. KNR Chidambaram HAM project got mutually

terminated with NHAI. KNR wrote off Rs 40mn on same during 2QFY20. KSHIP and Palani HAM projects are awaiting Appointed Date (AD). KSHIP has 60% 3H land status, AD expected by Dec-19. Palani HAM concession agreement yet to signed as 3H land status is 65%.

- **Balance sheet is strong, net D/E 0.2x, NWC days at 42:** KNR balance sheet is robust with NWC days at 42. Gross debt is Rs 3.1bn of which promoter debt is Rs 2.1bn. Net D/E is 0.2x (ex promoter is 0.1x). KNR has invested its share of Rs 1.7bn equity in 3HAM projects.

STANCE

KNR delivered yet again another robust quarterly performance. Kerala/Muzaffarpur BOT collection per day stood at Rs 1.8/2.2mn vs. Rs 1.9/2.7mn QoQ. KNR is in advance stage of selling Kerala BOT. For 3 HAM projects Rs 1.7bn investment, KNR expects to receive Rs 3.3bn over the next 4yrs. Strong balance sheet, periodic BOT/HAM equity churn and robust execution capability reinforces our positive stance on KNR. We maintain BUY. Key risks (1) Slowdown in government ordering (2) Higher crude and cement prices (3) Increase in interest rates and (4) Further liquidity tightening in the financial sector.

Financial Summary (Standalone)

Y/E March (Rs mn)	2QFY20	2QFY19	YoY (%)	1QFY20	QoQ (%)	FY18	FY19	FY20E	FY21E
Net Sales	5,230	4,163	25.6	4,646	12.6	19,317	21,373	25,534	30,909
EBITDA	1,077	832	29.4	900	19.6	3,862	4,270	4,797	5,503
APAT	560	353	58.4	477	17.3	1,622	1,733	1,983	2,491
Diluted EPS (Rs)	4.0	2.5	58.4	3.4	17.3	11.5	12.3	14.1	17.7
P/E (x)						21.2	19.9	17.4	13.8
EV / EBITDA (x)						9.4	8.7	7.5	6.2
RoE (%)						15.8	13.5	12.9	13.9

Source: Company, HDFC sec Inst Research

INDUSTRY	INFRASTRUCTURE
CMP (as on 15 Nov 2019)	Rs 245
Target Price	Rs 378
Nifty	11,895
Sensex	40,357

KEY STOCK DATA

Bloomberg	KNRC IN
No. of Shares (mn)	141
MCap (Rs bn) / (\$ mn)	34/476
6m avg traded value (Rs mn)	30

STOCK PERFORMANCE (%)

52 Week high / low	Rs 303/181		
	3M	6M	12M
Absolute (%)	1.8	4.9	28.6
Relative (%)	(6.4)	(3.8)	14.1

SHAREHOLDING PATTERN (%)

	Jun-19	Sep-19
Promoters	55.17	55.17
FIs & Local MFs	30.17	30.66
FPIs	3.15	2.83
Public & Others	11.51	11.34
Pledged Shares	-	-

Source : BSE

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Revenue: Rs 5.4bn. Adjusting for Rs 232mn of net revenue booked from one project where arbitration award came in KNRs favour, Revenues stood at Rs 5,230mn (9.3% beat)

EBITDA: Rs 1,258mn. Adjusting for Rs 181mn of arbitration claim, EBITDA stood at Rs 1,077mn (20% beat)

RPAT came in at Rs 700mn. Adjusting for the exceptional Rs 40mn write off on account of Chidambaram project termination and Rs 181mn on arbitration claim profit, APAT was Rs 560mn (35% beat)

We have revised our FY20/21E EBITDA estimate to factor better margins in irrigation projects. Higher depreciation and lower other income results in muted APAT impact

Standalone Quarterly Financial

Particulars (Rs mn)	2QFY20	2QFY19	YoY (%)	1QFY20	QoQ (%)	1HFY20	1HFY19	YoY (%)
Net Sales	5,462	4,163	31.2	4,646	17.6	10,108	9,726	3.9
Material Expenses	(3,157)	(2,630)	20.0	(3,053)	3.4	(6,210)	(6,215)	(0.1)
Employee Expenses	(363)	(249)	45.7	(271)	33.7	(634)	(445)	42.6
Other Operating Expenses	(684)	(452)	51.4	(421)	62.5	(1,106)	(1,136)	(2.7)
EBITDA	1,258	832	51.2	900	39.7	2,158	1,931	11.8
Interest Cost	(98)	(74)	31.9	(90)	8.1	(188)	(146)	28.8
Depreciation	(475)	(393)	20.9	(389)	22.3	(864)	(753)	14.7
Other Income (Incl. EO Items)	215	88	144.3	168	28.2	383	266	44.1
PBT	900	453	98.7	589	52.8	1,489	1,297	14.8
Tax	(200)	(3)	7,454.2	(112)	78.7	(311)	(107)	191.0
RPAT	700	450	55.5	477	46.7	1,178	1,191	(1.1)
E/o (adj for tax)	(140)	(97)	44.9	-	-	(140)	(207)	(32.1)
APAT	560	353	58.4	477	17.3	1,037	984	5.5

Source: Company, HDFC sec Inst Research

Margin Analysis

	2QFY20	2QFY19	YoY (bps)	1QFY20	QoQ (bps)	1HFY20	1HFY19	YoY (bps)
Material Expenses % Net Sales	57.8	63.2	(537)	65.7	(792)	61.4	63.9	(246)
Emp Expenses % Net Sales	6.6	6.0	66	5.8	80	6.3	4.6	170
Other Ope Exp % Net Sales	12.5	10.9	167	9.1	346	10.9	11.7	(74)
EBITDA Margin (%)	23.0	20.0	304	19.4	365	21.4	19.9	150
Tax Rate (%)	22.2	0.6	2,159	19.0	322	20.9	8.2	1,266
APAT Margin (%)	10.3	8.5	176	10.3	(2)	11.7	12.2	(59)

Source: Company, HDFC sec Inst Research

Change in Estimates

	FY20E New	FY20E Old	% Change	FY21E New	FY21E Old	% Change
Revenues (Rs mn)	25,534	25,534	-	30,909	30,909	-
EBITDA (Rs mn)	4,797	4,325	10.9	5,503	5,163	6.6
Margin (%)	18.8	16.9	185bps	17.8	16.7	110bps
APAT (Rs mn)	1,983	1,987	(0.2)	2,491	2,462	1.2

Source: Company, HDFC sec Inst Research

We expect steady inflows to keep the order book at comfortable levels

FY19-21E Revenue CAGR of 20.3%

Tax rate to increase as projects with tax exemption achieve completion

The reported PAT includes impact of MAT credit. We have adjusted this to full marginal tax rate to arrive at normalized PAT

KNR to generate strong FCF over FY20-21E

Key Assumptions And Estimates

STANDALONE (Rs mn)	FY19	FY20E	FY21E	Comments
Closing order book	59,006	63,472	67,563	We expect steady inflows to keep the order book at comfortable levels
Order book growth (%)	(6.4)	7.6	6.4	
New order booking	17,306	30,000	35,000	KNR has guided for conservative Rs 30bn inflows for FY20E. Has already announced Rs 18bn of projects in 1HFY20
Book to bill ratio	2.8	2.5	2.2	
Total Revenue	21,373	25,534	30,909	FY19-21E Revenue CAGR of 20.3%
Growth (%)	10.6	19.5	21.0	
EBIDTA	4,270	4,797	5,503	EBIDTA FY19-21E CAGR of 13.5% as EBIDTA margins contract
EBIDTA margin (%)	20.0	18.8	17.8	High share of irrigation revenue driving margins for FY20E
Depreciation	1,681	1,697	1,892	Expected to remain stable
Financial Charges	291	439	411	Borrowing cost to remain at comfortable levels as debt may peak at current levels of Rs 3.2bn +- Rs 1bn
PBT	2,906	3,169	3,718	
PBT margin (%)	13.6	12.4	12.0	
Tax	273.3	633.7	1,003.8	
Tax rate (%)	9.4	20.0	27.0	Tax rate to increase as projects with tax exemption achieve completion. KNR has MAT credit of Rs 660mn which shall be utilized till FY21E. KNR may migrate to new tax regime from FY22E
RPAT	2,633	2,535	2,714	Muted RPAT CAGR
Net margin (%)	12.3	9.9	8.8	
Extraordinary	(899.5)	(551.9)	(223.1)	We have adjusted for full tax of 33%
Adjusted PAT	1,733	1,983	2,491	19.9% APAT CAGR driven by lower adjustment for full tax rate of 33% as tax provision in books increase
Gross Block Turnover	2.3	2.3	2.5	Improvement on account of new orders inflow
Debtor days	40	45	48	To remain stable
CFO - a	2,475	3,401	3,065	Higher revenue growth, robust client advance to result in higher positive cash flow from operations
CFI - b	(2,860)	(1,965)	(583)	Investments in Gross block and HAM projects
FCF - a+b	(384)	1,436	2,482	KNR to generate strong FCF over FY20-21E
CFF - c	72	(49)	(1,045)	
Total change in cash - a+b+c	(313)	1,387	1,436	

Source: HDFC sec Inst Research

We value standalone EPC business at Rs 319/sh (18x Mar 21E EPS)

Kerala BOT at Rs 28/share (at 1x P/BV of equity invested)

Muzaffarpur Barauni BOT at Rs 5/share (at 1x P/BV of equity invested)

Real estate at Rs 5/share (at 1x P/BV of amount invested)

HAM Projects investment at 21/share

Our SOTP target price is Rs 378/share

Outlook And Valuation

Maintain BUY with Target Price Of Rs 378/sh

Valuation methodology

- We have valued KNR's EPC business at 18x Mar-21E EPS. Our rationale behind this is (1) Strong Sep-19 order backlog of ~Rs 66.8bn (2.6x FY20 revenue), (2) Robust balance sheet net D/E of (0.0x) by FY21E-end in addition to BOT monetization plans, (3) Superior earnings quality vs. similar-sized peers makes a case for valuation premium and (4) Reduced Equity commitment post deal with Cube Highways.
- KNR's promoter's share of debt is Rs 2,080mn of the standalone debt of Rs 3,160mn. Adjusted for promoters' loans standalone net D/E is 0.1x. This gives us comfort on gearing. Apart from that, improvement in the working capital cycle (driven by 10% mobilisation advances on NHA road EPC orders) will keep debt under check.

- Investments in the road sector will continue to drive stock performance. KNR, with its strong execution skills, is likely to benefit from the pick-up in order activity.
- We value the (1) Standalone EPC business at Rs 319/share (18x Mar-21 EPS), (2) Kerala BOT at Rs 28/share (at 1x P/BV of equity invested), (3) Muzaffarpur Barauni BOT at Rs 5/share (at 1x P/BV of equity invested), (4) Real estate at Rs 5/share (at 1x P/BV of amount invested) and (5) HAM Projects investment at 21/share (Mar-20E NPV of expected receipts from Cube Highways and 1x P/BV(x) for equity in KSHIP HAM). We arrive at SOTP of Rs 378/sh.

SOTP Valuation

Particulars	Segments	Value (Rs mn)	Value per share (Rs)	Rationale
KNR Standalone	Core construction business	44,837	319	At 18x Mar-21E EPS
Kerala BOT Project	Roads Toll	3,974	28	At 1x P/BV(x) of invested equity
Land Cost		694	5	At 1x P/BV(x) of invested equity
Muzaffarpur Barauni BOT	Roads Toll	718	5	At book value in balance sheet
HAM Projects investment	Roads BOT	3,000	21	Mar-20E NPV of expected receipts from Cube Highways and 1x P/BV(x) for equity in KSHIP HAM
		53,224	378	

Source: HDFC sec Inst Research

We summarize the valuations of the core EPC operations of our coverage universe and excluding the value of the asset portfolio, land and any other investment

Peer Set Comparison: Core EPC

COMPANY	MCap (Rs bn)	CMP (Rs)	RECO	TP (Rs)	Adj. EPS (Rs/sh)			P/E (x)			EV/EBITDA (x)			ROE (%)		
					FY19E	FY20E	FY21E	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E
Ahluwalia Contracts	19.2	286	BUY	388	17.5	18.3	25.0	15.6	15.0	10.9	7.8	7.4	5.2	17.3	16.9	17.2
Ashoka EPC	26.9	96	BUY	220	11.5	10.5	12.4	2.1	2.3	2.0	2.8	2.5	2.2	15.5	12.6	13.2
Dilip Buildcon	54.4	398	BUY	717	55.6	50.0	50.5	5.1	5.7	5.6	4.5	4.0	3.8	26.9	19.3	16.4
IRB EPC	25.3	72	BUY	172	14.8	15.7	19.4	-1.6	-1.5	-1.2	1.0	0.5	0.4	18.7	16.5	17.0
ITD Cementation*	9.6	56	BUY	78	4.8	5.9	6.5	11.7	9.6	8.6	4.4	4.0	3.6	8.0	9.4	9.5
JKIL	10.8	158	BUY	258	23.4	27.5	32.3	6.8	5.7	4.9	3.9	3.3	2.9	11.1	11.9	12.7
KNR Constructions	34.5	245	BUY	378	12.3	14.1	17.7	15.0	13.1	10.5	6.7	6.0	4.8	13.5	13.0	13.7
NCC	33.0	55	BUY	127	10.4	5.9	7.9	4.5	8.0	5.9	3.2	4.4	3.4	13.8	7.2	8.9
PNC Infratech	48.2	188	BUY	340	9.1	12.4	15.9	14.7	10.8	8.4	8.1	4.9	4.7	11.9	15.3	15.4
Sadbhav Engineering	21.2	123	BUY	269	10.9	10.3	14.2	6.0	6.4	4.6	6.2	4.2	3.9	9.2	8.1	10.1
PSP Projects	19.0	529	NEU	590	25.1	33.1	39.4	21.1	16.0	13.4	11.5	9.8	8.1	26.8	28.3	26.9
JMC Projects	18.0	107	BUY	175	641.4	7.3	10.0	0.2	14.7	10.7	15.6	11.2	10.4	10.8	12.9	12.1
HG Infra	15.8	242	BUY	441	19.0	29.6	33.2	10.5	6.8	6.0	5.5	4.2	3.6	20.6	25.6	22.7
Average								9.2	8.9	7.0	6.2	5.1	4.3	15.2	14.8	15.1

Source: Company, HDFC sec Inst Research *ITD Cementation FY19E/FY20E should be read as 15MFY19E/FY20E

Income Statement(Standalone)

Year ending March (Rs mn)	FY17	FY18	FY19	FY20E	FY21E
Net Revenues	15,411	19,317	21,373	25,534	30,909
Growth (%)	70.7	25.3	10.6	19.5	21.0
Material Expenses	12,281	14,353	13,881	16,980	20,956
Employee Expenses	552	721	929	1,136	1,267
Other Operating Expenses	281	381	2,293	2,681	3,245
EBIDTA	2,296	3,862	4,270	4,797	5,503
EBIDTA (%)	14.9	20.0	20.0	18.8	17.8
EBIDTA Growth (%)	50.1	68.2	10.6	12.4	14.7
Depreciation	639	1,341	1,681	1,697	1,892
EBIT	1,657	2,521	2,589	3,101	3,612
Other Income (Incl. EO Items)	194	393	608	507	517
Interest	219	231	291	439	411
PBT	1,632	2,683	2,906	3,169	3,718
Tax	60	(38)	273	634	1,004
RPAT	1,573	2,721	2,633	2,535	2,714
EO items (net of tax)	(194)	(1,099)	(899)	(552)	(223)
APAT	1,378	1,622	1,733	1,983	2,491
APAT Growth (%)	(4.6)	17.7	6.9	14.4	25.6
EPS	9.8	11.5	12.3	14.1	17.7
EPS Growth (%)	(4.6)	17.7	6.9	14.4	25.6

Source: Company, HDFC sec Inst Research

Balance Sheet (Standalone)

As at March (Rs mn)	FY17	FY18	FY19	FY20E	FY21E
SOURCES OF FUNDS					
Share Capital	281	281	281	281	281
Reserves	8,674	11,298	13,862	16,312	18,942
Total Shareholders Funds	8,955	11,579	14,143	16,594	19,223
Long Term Debt	1,441	2,203	2,472	2,946	2,396
Short Term Debt	-	-	169	169	169
Total Debt	1,441	2,203	2,641	3,116	2,566
Deferred Taxes	(815)	(1,408)	(1,739)	(1,739)	(1,739)
Other Non Current Liabilities	314	284	181	181	181
TOTAL SOURCES OF FUNDS	9,894	12,658	15,226	18,151	20,230
APPLICATION OF FUNDS					
Net Block	2,576	3,315	3,710	3,514	2,622
CWIP	15	-	-	-	-
Investments, LT Loans & Advances	5,297	5,619	6,447	7,419	7,519
Other Non Current Assets	1,466	1,563	2,003	2,140	2,505
Total Non-current Assets	9,354	10,496	12,160	13,073	12,646
Inventories	574	712	951	1,008	1,268
Debtors	1,640	2,320	2,344	3,156	4,073
Cash & Equivalents	649	438	130	1,517	2,953
ST Loans & Advances, Others	3,147	4,282	5,378	6,392	8,099
Total Current Assets	6,009	7,752	8,803	12,072	16,394
Creditors	1,344	2,102	2,236	2,449	3,218
Other Current Liabilities & Provns	4,125	3,488	3,502	4,546	5,593
Total Current Liabilities	5,469	5,590	5,738	6,995	8,810
Net Current Assets	540	2,162	3,066	5,078	7,584
Misc Expenses & Others	-	-	-	-	-
TOTAL APPLICATION OF FUNDS	9,894	12,658	15,226	18,151	20,230

Source: Company, HDFC sec Inst Research

Cash Flow (Standalone)

Year ending March (Rs mn)	FY17	FY18	FY19	FY20E	FY21E
PBT	1,632	2,682	2,906	3,169	3,718
Non-operating & EO items	20	(119)	(347)	(507)	(517)
Interest expenses	219	231	291	439	411
Depreciation	639	1,341	1,681	1,697	1,892
Working Capital Change	730	(2,330)	(1,506)	(763)	(1,435)
Tax paid	(75)	(237)	(550)	(634)	(1,004)
OPERATING CASH FLOW (a)	3,165	1,567	2,475	3,401	3,065
Capex	(1,383)	(2,009)	(2,034)	(1,500)	(1,000)
Free cash flow (FCF)	1,782	(442)	441	1,901	2,065
Investments	(1,836)	(259)	(826)	(972)	(100)
Other non operating income	-	-	-	507	517
INVESTING CASH FLOW (b)	(3,219)	(2,268)	(2,860)	(1,965)	(583)
Share capital Issuance	-	-	169	-	-
Debt Issuance	273	763	268	474	(550)
Interest expenses	(220)	(189)	(298)	(439)	(411)
Dividend	-	(85)	(68)	(84)	(84)
Others	-	-	-	-	-
FINANCING CASH FLOW (c)	53	489	72	(49)	(1,045)
NET CASH FLOW (a+b+c)	(1)	(212)	(313)	1,387	1,436
Opening cash balance	650	649	438	130	1,517
Closing Cash & Equivalents	649	438	130	1,517	2,953

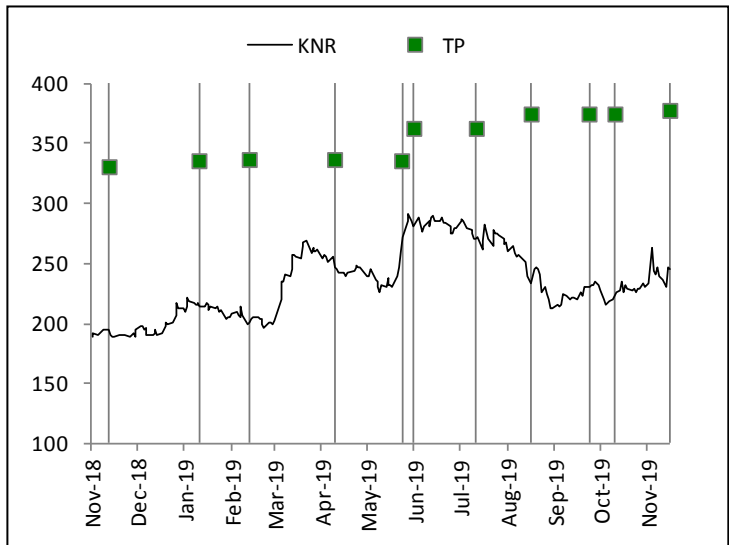
Source: Company, HDFC sec Inst Research

Key Ratios (Standalone)

	FY17	FY18	FY19	FY20E	FY21E
PROFITABILITY (%)					
GPM	20.3	25.7	35.1	33.5	32.2
EBITDA Margin	14.9	20.0	20.0	18.8	17.8
EBIT Margin	10.8	13.0	12.1	12.1	11.7
APAT Margin	8.9	8.4	8.1	7.8	8.1
RoE	16.9	15.8	13.5	12.9	13.9
Core RoCE	40.4	38.7	27.1	27.7	27.8
RoCE	16.1	14.7	13.1	12.9	13.8
EFFICIENCY					
Tax Rate (%)	3.7	(1.4)	9.4	20.0	27.0
Asset Turnover (x)	2.4	2.4	2.1	2.2	2.4
Inventory (days)	14	13	16	14	15
Debtors (days)	39	44	40	45	48
Payables (days)	32	40	38	35	38
Cash Conversion Cycle (days)	21	18	18	25	25
Other Current Assets (days)	75	81	92	91	96
Other Current Liab (days)	98	66	60	65	66
Net Working Capital Cycle (Days)	(3)	33	50	51	55
Debt/EBITDA (x)	0.6	0.6	0.6	0.6	0.5
Net D/E	0.09	0.2	0.2	0.1	(0.0)
Interest Coverage	7.6	10.9	8.9	7.1	8.8
PER SHARE DATA					
EPS (Rs/sh)	9.8	11.5	12.3	14.1	17.7
CEPS (Rs/sh)	14.3	21.1	24.3	26.2	31.2
DPS (Rs/sh)	0.0	0.5	0.4	0.5	0.5
BV (Rs/sh)	64	82	101	118	137
VALUATION					
P/E	25.0	21.2	19.9	17.4	13.8
P/BV	3.8	3.0	2.4	2.1	1.8
EV/EBITDA	15.4	9.4	8.7	7.5	6.2
OCF/EV (%)	0.1	0.0	0.1	0.1	0.1
FCF/EV (%)	5.1	(1.2)	1.2	5.3	6.1
FCFE/Market Cap (%)	5.3	0.4	1.2	5.6	3.2
Dividend Yield (%)	0.0	0.2	0.2	0.2	0.2

Source: Company, HDFC sec Inst Research

RECOMMENDATION HISTORY



Date	CMP	Reco	Target
12-Nov-18	194	BUY	331
10-Jan-19	217	BUY	336
13-Feb-19	200	BUY	337
9-Apr-19	247	BUY	337
23-May-19	247	BUY	336
1-Jun-19	280	BUY	363
11-Jul-19	271	BUY	363
17-Aug-19	233	BUY	375
22-Sep-19	231	BUY	375
10-Oct-19	224	BUY	375
16-Nov-19	245	BUY	378

Rating Definitions

BUY : Where the stock is expected to deliver more than 10% returns over the next 12 month period

NEUTRAL : Where the stock is expected to deliver (-)10% to 10% returns over the next 12 month period

SELL : Where the stock is expected to deliver less than (-)10% returns over the next 12 month period

Disclosure:

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