Kirloskar Oil Engines Ltd

Industry	CMP	Recommendation	Add on dips to	Sequential Targets	Time Horizon
Engineering / Capital Goods	Rs. 378.10	Buy at CMP and add on declines	Rs. 338 - 346	Rs. 430 - 474	2-3 quarters

HDFCSec Scrip Code	KIRENGEQNR
BSE Code	533293
NSE Code	KIRLOSENG
Bloomberg	KOEL IN
CMP Mar 03, 2017	Rs. 378.10
Equity Capital (Rs cr)	28.9
Face Value (Rs)	2.0
Equity Share O/S (cr)	14.46
Market Cap (Rs crs)	5467.9
Book Value (Rs)	99.6
Avg. 52 Wk Volumes	9996
52 Week High	379.9
52 Week Low	205.0

Shareholding Pattern % (Dec 31, 2016)	
Promoters	59.3
Institutions	22.3
Non Institutions	18.4
Total	100.0

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Kirloskar Oil Engines Limited (KOEL) has been one of the pioneers of the 'Make in India' concept since independence. KOEL, a part of the Kirloskar Group offers engineering products and solutions across the globe and has offices in Dubai, South Africa, and Kenya. It has manufacturing units in Pune, Kagal, Nashik (all in Maharashtra), and Rajkot (Gujarat). KOEL caters to the agriculture, power generation, and industrial and construction machinery sectors.

Investment Rationale:

- Rising acceptance of newly introduced higher kVA Diesel Gensets - typically the 750, 910 and 1010 kVA gensets.
- Increasing demand for higher HP power tillers being a cheap near-replacement for tractors.
- Increasing road constructions and infrastructural spending in the country raising the demand for industrial engines.
- High spends on R&D (2.8% of sales in FY16) ensures bringing innovative product offerings at competitive prices
- Recent focus on American markets may result in derisking dependence on Indian markets for gensets business.
- Large engine business could get a push through marine engines (exposure to commercial/defence ships) – orders for which are under execution in FY17-FY18.
- Financial parameters are healthy – debt equity ratio, working capital, return ratios, book value, cash per share.

Concerns:

- Fall in peak power deficit and Govt's initiatives to push power generation could hamper demand for gensets.
- Focus on shifting to solar and electric pumpsets shown by Govt may adversely impact sales of diesel pumpsets.
- Vagaries of Indian monsoon and wavering rural incomes may impact the diesel pumpset and power tiller markets.
- Dependency on economic growth / infrastructure spending.
- Local competition and competition from China.
- KOEL's exports has fallen by 32% Y-o-Y basis as per 9MFY17 numbers.

View and Valuation:

KOEL's topline has been flat for previous five fiscals on account of lower offtake in genset market both domestic as well as international except for the years in which the offtake under the large engines business jumped due to the orders received from NPCIL. KOEL is endowed with well-balanced management team which has been pro-active on all fronts to develop and capture any opportunity available in the market. This is evident from the working of 9MFY17 – currently helped by growth in the Industrial engines business, Agriculture business and Large Engines business segment.

We feel investors could buy the stock at the CMP and add on dips between Rs.338 and Rs.346 for sequential targets of Rs.430 and Rs.474 (24.5x and 27x FY19E EPS) over 2-3 quarters. At the CMP of Rs. 378.10 the stock trades at 21.5x FY19E EPS.

Financial Summary

Particulars (Rs cr)	Standalone					Standalone				
	Q3FY17	Q3FY16	YoY (%)	Q2FY17	QoQ (%)	FY15	FY16	FY17E	FY18E	FY19E
Net Sales	628.19	593.43	5.9%	650.13	-3.4%	2507.1	2454.7	2643.7	2909.5	3221.2
EBITDA	57.9	59.91	-3.4%	73.97	-21.7%	248.6	239.7	290.8	337.5	389.8
APAT	28.07	29.34	-4.3%	42.58	-34.1%	143.1	140.5	175.7	213.9	253.9
Diluted EPS (Rs)	1.94	2.54	-23.5%	2.94	-34.1%	9.9	9.7	12.1	14.8	17.6
P/E (x)						38.2	38.9	31.1	25.6	21.5
RONW						11.0%	10.1%	11.8%	13.4%	14.6%

(Source: Company, HDFC sec)

Company Profile:

KOEL, one of the flagship companies of the Kirloskar group, manufactures and services diesel engines (primarily in the range of 2.5 to 800 HP) and diesel generator sets (primarily in the range of 2 to 1010 kVA). Further, the company also produces large diesel engines in the range of 2400HP to 11000 HP. The company also manufactures diesel, petrol, and kerosene-based pump sets. The Company's engineering capabilities are backed by a strong R&D centre which works towards bringing innovative product offerings to the customer at competitive prices. It has manufacturing units in Pune, Kagal, Nashik (all in Maharashtra), and Rajkot (Gujarat). KOEL caters to the agriculture, power generation, and industrial and construction machinery sectors. The company generates 77% of its revenue from the engines business and approximately 22% from its genset business. In FY16 the company has accomplished the following which indicates better growth prospects for the company in near future:

- Launched complete range of 2.1kW, 3kW and 4kW petrol sets to offer the widest range of portable gensets for household and commercial applications.
- Added 36 new models to its product portfolio under the crop irrigation segment.
- Achieved the break-through order for Marine engines – export to Bangladesh.
- Understanding with Biocube for manufacturing, sale and service of biocube systems in India.

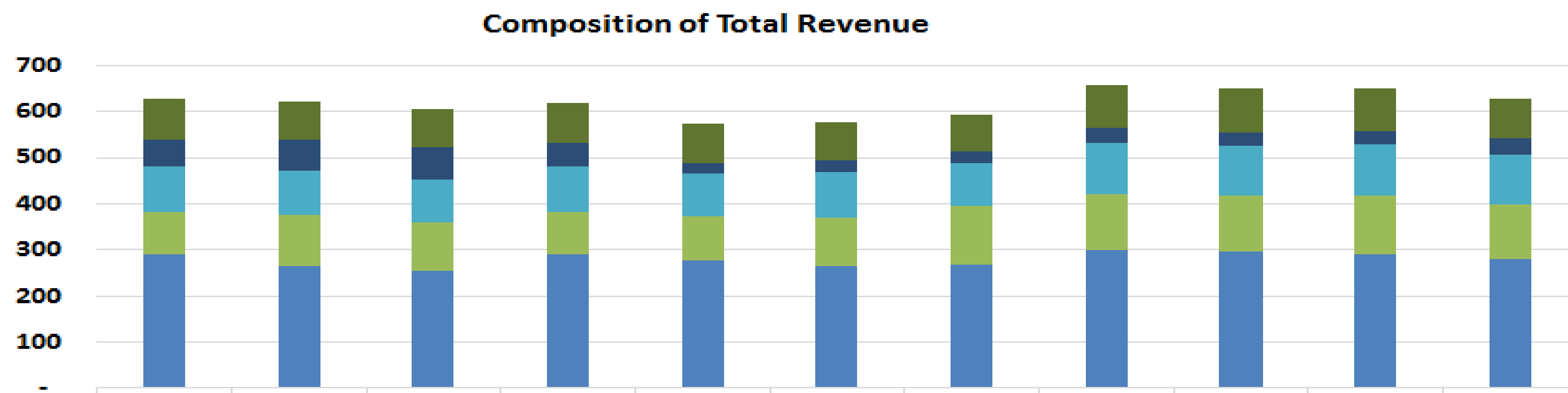
Business Overview:

The business operations of KOEL can be segmented into 5 operational segments which are: Power Generation, Agricultural and Allied Business, Industrial Engines Business, Large Engines Business and Customer Support:

Kirloskar Oil Engines Limited

Power Generation Business	Agriculture and Allied Business	Industrial Engines Business	Large Engines Business	Customer Support
Lower kVA GenSets	Crop Irrigation Business		Stationary power plants (base load / critical standby - AMF or black start)	
High kVA GenSets	Farm Mechanization Business		Marine main propulsion engines and auxiliary generating sets	

The segmental revenues of the company in the past have been as follows:



	Q1FY15	Q2FY15	Q3FY15	Q4FY15	Q1FY16	Q2FY16	Q3FY16	Q4FY16	Q1FY17	Q2FY17	Q3FY17
Customer Service	92	85	82	85	88	83	80	92	98	92	87
Large Engines Business	55	67	69	52	22	25	25	32	26	28	33
Industrial Segment	99	95	93	97	91	98	92	113	111	114	111
Agricultural Business	92	113	105	94	98	106	129	119	121	126	118
Power Generation Business	291	263	255	289	276	265	267	300	295	290	279

1. **Power Generation Business:**
KOEL specialises in the manufacture of both air-cooled and liquid-cooled diesel engines and generating sets across a wide range of power output from 2 kVA to 3000 kVA. It also offers engines operating on alternative fuels such as bio-diesel, natural gas, biogas and straight vegetable oil (SVO). The "Kirloskar Green Genset" (KOEL's generating brand) is the market leader with 30% quantity market share and 22.5% value market share. It is the most preferred brand among customers in the power generation and telecom industry in India. With a total revamp of the supply chain system and related processes over the last two years, the Company is now geared to deliver Gensets within 7 days to their customers. KOEL views its power generation business to be serving the following separate classes of customers:

   - <u>Individual and Standalone Requirements:</u>
     Here the company aims to provide gensets that support the households and business having low power requirements. The gensets range between 2kVA and 30kVA since the company here aims at providing comprehensive support for micro needs. Company's "KOEL Chota Chilli" brand of gensets are sold to this segments powering loads like ACs and pumps in times of extended power outages.

   - <u>Commercial and Bulk Requirements:</u>
     Here the company aims to provide gensets that support the OEMs and distributed users like banks and similar institutions. The gensets range between 15kVA and 250kVA. "KOEL Green" is the genset brand of the company under which the company has achieved over 2 million installations across

different operating conditions. Said range of gensets are CPCB emission norms compliant and also include remote monitoring system feature which adds to the easy maintenance of the genset.

- Large Power Requirement:
  KOEL provides turnkey power backup solutions for businesses from large manufacturing setups to large commercial establishments or critical power requirement and address their acute requirements like variable loading, synchronized generators, exhaust piping for continuous, efficient, economic and reliable power. The company has commissioned more than 30000 HHP generators having best-in-class fuel economy and best-in-class block loading. The generators ranging in this sub-segment include 160 kVA to 1010 kVA gensets.

In the power generation business the company has witnessed a Q-o-Q de-growth of 3.8% in Q3FY17 since the demonatisation has had direct impact on company's lower kVA gensets. Further, Q3 is has always been a weak quarter for the power generation business segment of the company. The same is also consistent with company's Y-o-Y numbers which have grown by 4.5% in this segment. The company's YTD sales in this segment have grown roughly by 7% which is more so due to the picking up of sales in the higher kVA segment of the company. The HHP segment which consists of the gensets ranging between 202kVA to 1010kVA has grown in this year alone by about 32%.

The company's HHP gensets have been the primary driver for growth in this segment for the company. Although the peak power deficit is on a steep decline in the country as a whole which affects adversely to the sompany's lower kVA demand, the demand for higher kVA segment of the company tends to remain high from the the real estate, from the metro railways and typically from the IT industry. The company expects its sales in the lower kVA segment which de-grew in the third quarter to recover by the H1FY18 and also expects the demand in its high kVA segment to sustain. The company has received about 300 enquiries for its 750kVA gensets and 150 enquiries for 910 kVA and 1010 kVA which goes on to support the view that there is good growth prospects in the said sub-segment for the company. The overall performance of this segment of the company is expected to improve taking into consideration:

- the seasonality witnessed in company's power generation business segment;
- the one-off adverse impact of demonetization on its lower kVA gensets sales; and
- its increasing acceptance and demand for HHP gensets.

2. Agriculture and Allied Businesses:

In agricultural sector, Kirloskar fulfils the motive power needs of customers globally; essentially farmers, who require products in the range of 3 hp to 130 hp. The companies agricultural business segment is further divided into two sub-segments which are as follows:

- Crop Irrigation:
  KOEL manufactures diesel pumpsets and agri engines powering more than 25 applications across five sectors. Kirloskar pumpsets have been finding applications in India, Egypt, Africa, and Latin and Central America. KOEL is the one of the most preferred brand amongst farmers because of its reliable performance and fuel efficiency. The rural electrification drive has led to shift in demand from conventional diesel engine pumpsets to electrical and solar powered water pumpsets. The business has more than 550 distributors and over 17,000 retailers in FY16 as compared to 500 distributors and 10000 retailers in FY15. The entire supply chain has been revamped to a pull based system, where inventory levels remain dynamic, thus reducing the risk of inventory pile up. With a wide range of products like conventional diesel engine pumpsets, light weight pumpsets and petrol kerosene pumpsets, the business gained market share by 1 %, as compared to the previous fiscal and more importantly managed to sustain the business despite an industry

decline for diesel engines and pumpsets. The company under the same sub-segment has introduced a trading model in the states of UP and Maharashtra selling electric hand-pumps to hedge the risk of low diesel pumpsets sales on account of increasing rural electrification. The elaborate service channel with Kirloskar Krishi Seva Kendra takes care of the quick field service requirements.

- Farm Mechanization:
  For a distinct identity, Kirloskar launched its new brand 'Kirloskar Mechanization Works' in FY15. This is its first farm mechanization product, power tillers (Mega T15). Fragmented land holdings of several farmers in the small and marginal categories have created challenges regarding the collective ownership of tractors costing Rs.250,000 to Rs.800,000 each. This opens up vast opportunities for the domestic power-tiller segment, as a power tiller costs Rs.125,000 to Rs.150,000, but can perform all requisite agricultural operations done by a tractor. In FY16 the company launched three new variants of Mega T to suit the market needs. The business has created a channel of about 140 exclusive dealers as against 77 in FY15 (almost doubling) for focussed delivery and service.

The company's agriculture and allied business segment was hit worse due to the demonetization. Under this segment the revenues de-grew by 6% Q-o-Q and 9% Y-o-Y in Q3FY17. The other factor resulting in lower revenues from this segment is the introduction of direct benefit transfer scheme over purchase of power tillers by the government without being equipped to execute same. This is proving to be a hindrance in the otherwise fast-growing power tiller business of the company. Even after such fall in revenues for the said quarter the YTD revenues from this segment have increased by 9.6% Y-o-Y. This is purely due to the growing distribution network of the company in its crop irrigation business and the wide and rising acceptance of a cheaper near-replacement of tractors i.e. power tillers. Also favourable monsoon has added to the revenue growth of the company this fiscal.

The effects of demonetization are expected to wear off by the end of this fiscal and the agriculture and allied business segment of the company is expected to return to its growing trend by H1FY18. The Q3 numbers which indicate this segment to be under-performing is temporary and we expect this segment to thicken company's topline taking into consideration

- the growing market for power tillers;
- solving of the long-standing DBT issue;
- company's foray in the electric pumpset business;
- possibility of a favourable monsoon and increasing efforts of government to improve rural income.

3. Industrial Engines Business:

KOEL's activities in this segment are moulded completely according to the motive power needs of customers who require products from 20 hp to 800 hp in the Industrial Engine space globally. KOEL manufactures a variety of quality diesel engines powering more than 85 Industrial Engine applications across seven sectors which include Earth-Moving, Fluid-Handling, Construction equipment, Marine Applications, Mining applications, Off-shore applications and Material Handling. KOEL's share of Indian construction market lies close to 55%. KOEL through its industrial segment also serves the tractor market by providing requisite power diesel engines.

In the quarter ended i.e. Q3FY17, the company's revenues have de-grown by 2.7% Q-o-Q and grown substantially by 20.7% Y-o-Y. On a YTD basis the revenues have grown by 19.6%. This growth in the revenue is due to the increase in the infrastructural expenditure on government's side. The demand for off-highway construction equipment is expected to grow at a CAGR of 12.3% and the same is to benefit KOEL it being a major producer of engines for these equipments. Further, on the back of a favourable monsoon the tractors off-take so an upmove. However, the same was muted in the Q3 due to the negative fruits of demonetization.

The effects of demonetization are to be viewed as short term in nature and same shall reverse in the coming quarters. The off-highway construction equipment is expected to grow at a CAGR of 13% and the tractor industry is to show a CAGR of 8-9% over the term of 3 years. This is the fastest growing segment for the company which is expected to boost company's revenues on account of:

- the growing infrastructural spending,
- the growth of off take in the off-highway construction equipment; and
- the expectation of a favorable monsoon.

4. Large Engines Business:

The Large Engines business group (LEBG) manufactures and markets diesel engines in the range of 2400 hp to 11000 hp catering to DG sets from 1.7 MW to 7.1 MW for stationary power plants. These engines are manufactured in Nashik. LEBG also manufactures marine propulsion engines and auxillary DG Sets under license from Daihatsu Diesel Mfg Co Ltd, Japan in the range 800 hp to 3500 hp. The sub-segments under this segment are:

➢ <u>Stationery Power Plants</u>:
KOEL specialises in providing stationary power plants up to 30 MW capacity, incorporating modular sets in the range 1.7 MW to 7.1 MW. Around 125 DG sets supplied so far in India for base load generation / standby power application, run on furnace oil / high speed diesel. These diesel generating sets provide power to industries such as textiles, pharmaceuticals, packaging, petrochemicals and refineries, cement, steel, and auto component manufacturing. KOEL undertakes complete turnkey projects for the execution of power plants, from design, engineering, manufacturing, assembly, testing up to erection and commissioning at site. KOEL LEBG is a vendor for various organisations such as Nuclear Power Corporation of India Ltd., (NPCIL), Bharat Heavy Electricals Ltd. (BHEL) and consultants like Engineers India Ltd. (EIL), MECON, DCPL, PDIL, Bechtel, Fichtner, etc.

➢ <u>Marine main propulsion engines and auxiliary generating sets</u>:
KOEL has been in the business of main propulsion engines since over three decades. The Marine Engines manufactured under the Kirloskar-Daihatsu brand are fully compliant with IMO TIER II requirements. The engines are approved by major classification societies like ABS, LRS, KR, BV, GL, DNV, NK & CCS. LEBG has a network of service and spare parts offices all along the Indian coast line for most responsive product support.

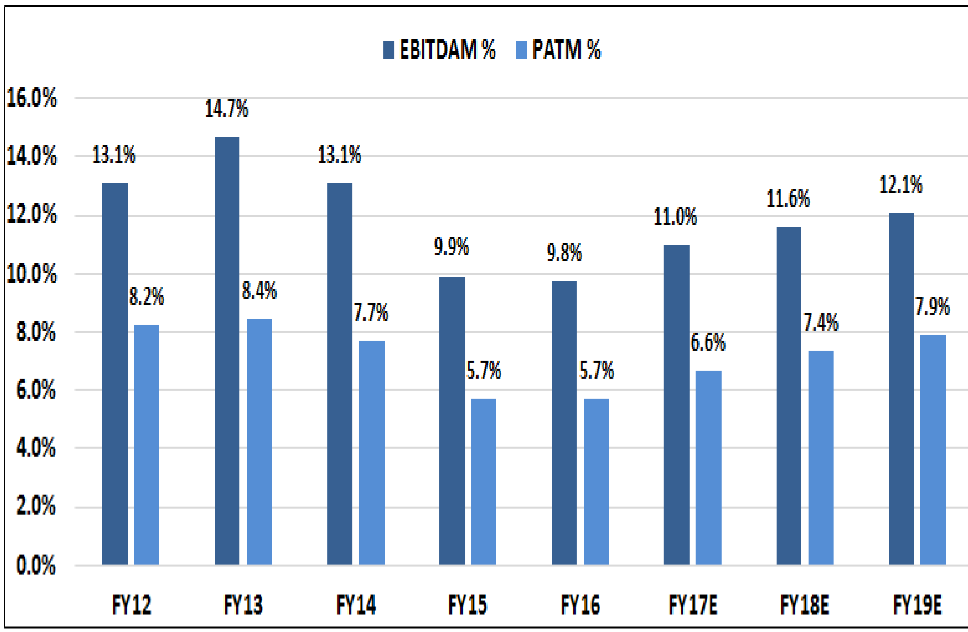
KOEL's focus under the large engines business had in the past been on the navy segment for the propulsion engines business and orders from NPCIL. In fact its revenue stream had thickened drastically in the FY15 due to the orders received and executed from NPCIL. However, the company has now shifted its focus on defense and marine. KOEL has received some orders from the defense and railway sector. It has also received its first order for fishing boats.

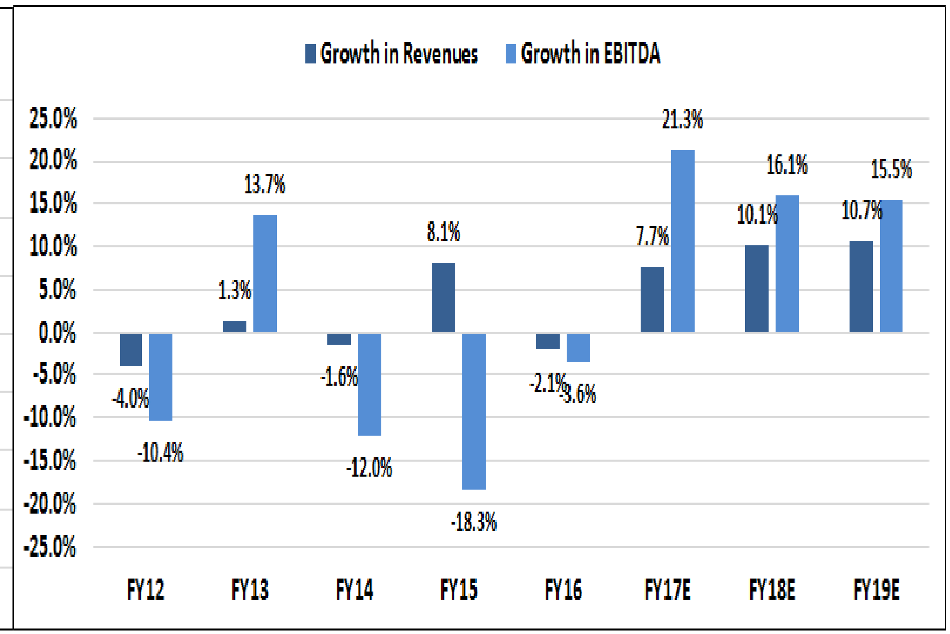
We believe that the growth of large engines business has some dependence on how well the company is fetching the orders from NPCIL. These orders from NPCIL have dried up on account of non-commissioning of the previously executed orders by company. KOEL expects orders from NPCIL to flow in with the commissioning of the already completed projects by end of this fiscal.

We expect that once the orders from NPCIL which have reduced as such in the previous 2 years should pick up in FY18 and FY19. Further, the orders from the defense sectors which have already been received by KOEL have been delayed by 6 to 8 months in their execution. These orders are expected to be executed and a revenue stream of approx. Rs.100 crs is expected from these orders. Further there has been a hike in the allocation for the defense sector in the budget of about 10% which is expected to positively impact company's revenue under this stream. Taking into account all of above we expect company to make better growth in this segment over the coming quarters.

5. **Customer Support Business:**
This division sells spares and offers servicing. Kirloskar has more than 450 service outlets and more than 5000 trained technicians serving the genset segment and 400 in the agriculture pump-set segment to service the products sold. Customer support depends largely on the operating cycle of products sold. Hence, customer support business segment majorly depends on how well the power generation, agricultural and industrial segment performs. Further it also depends on the growth in the IIP of the country.

With reasonable growth in the industrial segment and the power generation segment, the company expects customer support business to grow on same lines. The customer support business has remained constant at about 16-17% of the total of other segmental sales. In view of same the same is expected to continue over the coming quarters and the sales witness a growth in lines with the growth witnessed in other segments of the company.





(Source: Company, HDFC sec)

Investment Rationale:

Rising acceptance of higher kVA gensets:
The company has recently launched its higher kVA gensets ranging between 750kVA and 1010kVA. These gensets as typically serve the back-up power requirements in the industrial sector and commercial hubs like malls, multiplexes etc.are in great demand. KOEL's higher kVA gensets enjoy the tag of being cost-effective and compact in nature which increases its desirability. The company is bullish in this sub-segment as there's still enough room for growth in the near future. The enquiries have been high for these gensets and hence indicate better prospects for future

Introduction of Tillers - Successful Mega T:
Two years back company added power tillers to its product portfolio and the same have been successful to attract smaller farmers holding fragmented agriculture land where the use of tractors is not feasible. The cost of these power tillers and its efficacy in performing the similar operations that a 5 times costlier tractor would perform have led to surge in its demand. The company has not only met this demand but has also capitalized on the opportunity to introduce two new variants of Mega T – power tillers to further strengthen its hold over this segment.

Increasing infrastructural and road construction activity:
There has been an increase in the infrastructural expenditure on government's side over previous 2 years. The demand for off-highway construction equipment has improved and is expected to grow at a CAGR of 12.3%. Further, on the back of a favourable monsoon the tractors off-take is on an upmove. This all goes to benefit KOEL as it is a major producer of engines for these equipments.

Increased spending on R&D:
Company's expenditure on R&D has increased Y-o-Y and the same is at approx. 2.8% of the revenues for FY16. This is one of the prime reasons company has been able to diversify its business into all these segments reducing the dependency on power generation business over the years. This expenditure made by company on its research helps it to not only maintain its current market share but also grow the same by adding new products to its product portfolio.

Attempt to make a mark in US:
US is the biggest market for genset business and the same was untouched by KOEL until 2015. KOEL has been stating that it aims at doubling contribution of export to total revenues by 2020 and has therefore moved to US as a market option for its power gensets. KOEL has a wholly owned subsidiary in US through which it has started selling its products in the US markets and aims to grow its share in that market with time. This wholly owned subsidiary of KOEL will also focus on expansion in Latin American market as well as FMUL fire pump OEM business. For FY16, the Sales Revenue of this wholly owned subsidiary was US$ 502,402 (~ 3.34 Crores) with a Profit from operations of US$19,931 (~0.13 Crores)and Net Profit after Tax of US$16,941 (~0.11 Crores).If it is able to convert this opportunity into success it shall be able to improve its standings on the export turnover front.

Order for Marine Industry under the Large Engines Business:
The company has received orders for propulsion engines in the marine industry for commercial and navy ships. These orders are under execution and shall be executed by FY18 and have a good potential to generate revenues and grow the LEBG segment of the company. The first export order for supply 12 numbers of 250 kVA and 6 numbers of 87.5 kVA Marine DG sets, to be used for six ships, was received from Western Marine Shipyard, Bangladesh, in FY17. These sets will be delivered in FY17 / FY18.

Sound Fundamentals:

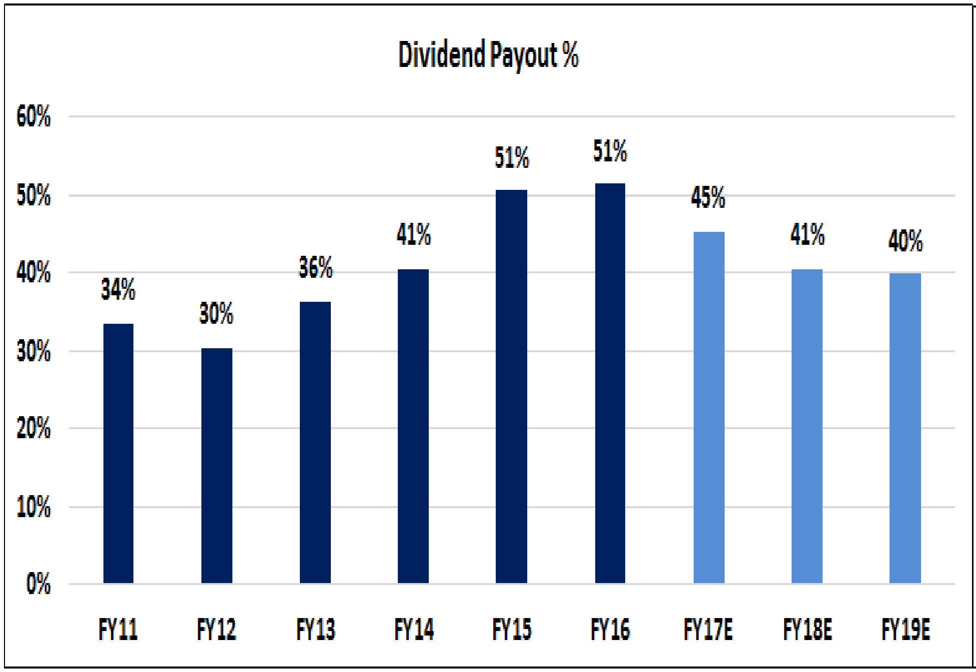
Despite challenging macro-environment on account of weak monsoon for FY15 and FY16 and weak industrial environment clubbed with a falling peak power deficit number, KOEL has done well in maintaining its market share and maintaining its turnover. The company enjoys the tag of a debt free company and has a balance sheet with zero debt burden. Taking into the consideration of recent management discussion, company has no intention to add further term debt in near future.

The company enjoys a payable days of 49 days and realizes its receivables in about 23 days. Having inventory days of 30 it has a cash conversion cycle of 4 days which is extremely good as an operational factor of efficiency. Company has high liquidity, Cash and Cash equivalent is almost 42% of balance sheet. The company has cash per share number of Rs.76 per share (FY19) indicating its cash abundance.

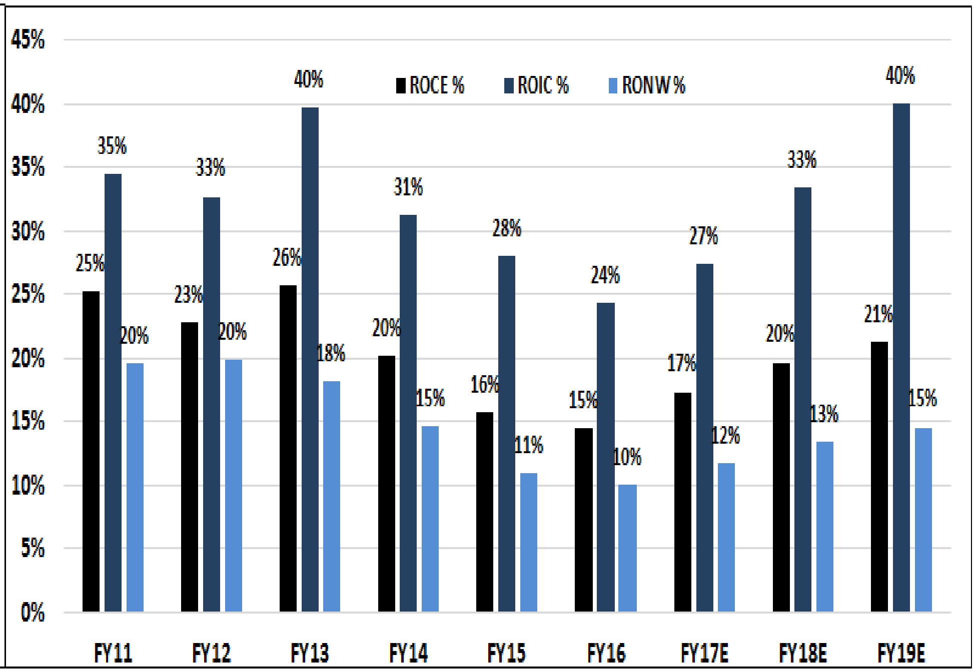
Further, company follows a very conservative accounting approach while charging depreciation where it has charged on an average depreciation at a rate of 16-18% of its net block which is higher than that provided by most Indian companies. This results in the cash EPS number of the company being almost double for FY16 at around Rs.17.43 against the basic EPS of Rs. 9.72. Hence a valuation based on its cash EPS would be more attractive than the one based on its basic EPS.

Apart from this, company is very good on dividend payments (interim and final payouts and payout ratios to its share holders) paying Rs.5 per share each year and maintaining ~50% payout. We expect 32%% and 26% dividend payout for FY18E and FY19E, respectively.

Dividend Per Share



Return Ratio-%



(Source: Company, HDFC sec)

Introduction of GST could benefit KOEL in power gensets segment which is competitive and consists of a number of unorganized players.
On introduction of GST there is a high probability that the unorganized players in lower kVA segment start losing out and that would mean organized segment stand to gain. KOEL being leader in the market could gain from introduction of GST as it would get increasingly difficult for unorganized players maintain competitiveness in the market.

Risk and Concerns:

Reduction in Peak Power Deficit:
The peak power deficit is one of the determinants determining the demand for diesel gensets, which is the major source of KOEL's revenue. Peak Power deficit has been reducing on a year on year basis since 2014. The government in July 2016 announced and projected that India by the end of FY17 will be a peak power surplus state. However, the provisional numbers issued by Ministry of Power state that India faced a Peak Power Deficit of 1.6% upto December 2016 as against the surplus projected by the government for the year of 3.1%. Although, the surplus as aimed for by the government was not achieved, the peak power deficit is on a downtrend which may affect the genset sales by KOEL in the country at least in its lower kVA segment.

Solar and Electric Pumpsets:
Diesel pumpsets sold by KOEL under its brand VARSHA as a part of its crop irrigation sub-segment have higher running cost as compared to the solar and electric pumpsets. Increasing incentives for solar equipments in the budget and fast rate of electrification of rural villages coupled with increasing rural incomes may push the agricultural sector to replace the old diesel pumpsets with more cost effective solar and electric pumpsets. Although KOEL has entered into the electric pumpset market by way of a trading model in the states of UP and Maharashtra, the revenue generated till date is miniscule and hence would require serious efforts and costs to be incurred till it establishes itself as a player in this market. Further, company has in the past informed that it is designing a hybrid model for a Solar-Diesel pumpset. However, there has been no update on its launch.

Uncertain Monsoon:
The inherent uncertainty of monsoon affects company's business on two fronts, viz. its agricultural business and its tractor engine segment under the industrial segment. Favourable monsoon leaves more disposable income in the hands of the rural agrarian community which in turn increases the demand under the above named segments of the company.

Increasing Steel Prices:
The steel prices have been on an uptrend of late. Steel is the prime raw material in the business in which KOEL is engaged. Total raw material cost hovers somewhere around 62% for the company, which goes to show that abnormal increase in this cost may put pressure on the margins. One of the major reasons for decreasing margins for previous 2 years has been the increasing raw materials cost. It should further be noted that the company is reluctant to pass on the increasing price effect to its customers in its persistence to maintain its market share. Hence, if the steel prices continue to rise the company's margins may be adversely affected consequently.

Dependency on Economic growth and Infrastructural Spending:
The company's 3 major segments majorly depend on how well the economy is performing and the level of infrastructural spending induced by the Govt authorities. If the economic growth or this infrastructural spending is subdued on any account it may adversely impact company's revenues. This, although not being very probable, may occur in events such as one witnessed in the December quarter i.e. demonetization.

Declining Exports:

Although company aims at doubling the contribution of exports to its total revenues by 2020, there has been a considerable decline in the export turnover of the company on account of weak global scenario. The 9MFY17 exports stand at Rs. 119 cr as against Rs. 176 cr in the previous year for the same period.

Exposure to FOREX:

Approximately 9% of company's sales are on account of exports that it makes. This leaves company exposed to the forex fluctuations. Appreciation of rupee against other currencies may lead to a decline in the company's topline from exports.

View and Valuation:

KOEL's topline has been flat for previous five fiscals on account of lower offtake in genset market both domestic as well as international except for the years in which the offtake under the large engines business jumped due to the orders received from NPCIL. KOEL is endowed with well-balanced management team which has been pro-active on all fronts to develop and capture any opportunity available in the market. This is evident from the working of 9MFY17 – currently helped by growth in the Industrial engines business, Agriculture business and Large Engines business segment.

We feel investors could buy the stock at the CMP and add on dips between Rs.338 and Rs.346 for sequential targets of Rs.430 and Rs.474 (24.5x and 27x FY19E EPS) over 2-3 quarters. At the CMP of Rs. 378.10 the stock trades at 21.5x FY19E EPS.

Quarterly Financials- Standalone

Rs in Cr	Q3FY17	Q3FY16	YoY (%)	Q2FY17	QoQ (%)	FY16	FY15	YoY (%)
Net Sales	628.19	593.43	5.9%	650.13	-3.4%	2419.01	2473.3	-2.2%
Other Operating Income	12.67	13.34	-5.0%	13.15	-3.7%	35.68	33.81	5.5%
Total Income from Operation	640.86	606.77	5.6%	663.28	-3.4%	2454.69	2507.11	-2.1%
Raw Material Consumed	407.24	382.99	6.3%	416.65	-2.3%	1543.05	1625.7	-5.1%
Employee Expenses	52.28	50.87	2.8%	50.66	3.2%	185.55	188.4	-1.5%
Other Expenses	123.44	113	9.2%	122	1.2%	486.36	444.41	9.4%
Total Expenditure	582.96	546.86	6.6%	589.31	-1.1%	2214.96	2258.51	-1.9%
EBITDA	57.9	59.91	-3.4%	73.97	-21.7%	239.73	248.6	-3.6%
Depreciation	27.56	27.02	2.0%	27.4	0.6%	111.5	101.9	9.4%
EBIT	30.34	32.89	-7.8%	46.57	-34.9%	128.23	146.7	-12.6%
Interest	0.84	2.17	-61.3%	0.72	16.7%	0.06	0.2	-70.0%
Other Income	17.6	7.64	130.4%	17.89	-1.6%	73.97	58.93	25.5%
Profit before Tax	47.1	38.36	22.8%	63.74	-26.1%	202.14	205.43	-1.6%
Tax Expenses	19.03	9.02	111.0%	21.16	-10.1%	36.13	62.29	-42.0%
Reported Profit After Tax	28.07	29.34	-4.3%	42.58	-34.1%	166.01	143.14	16.0%

Extra-ordinary Items	0	0	0.0%	0	0.0%	-25.48	0	0.0%
Adjusted Profit After Extra-ordinary item	28.07	29.34	-4.3%	42.58	-34.1%	140.53	143.14	-1.8%
EPS (Adj) (Unit Curr.)	1.94	2.54	-23.5%	2.94	-34.1%	9.72	9.9	-1.8%

(Source: Company, HDFC sec)

Financials – Standalone

Income Statement

Particulars, Rs in	FY14	FY15	FY16	FY17E	FY18E	FY19E
Net sales	**2287.0**	**2473.3**	**2419.0**	**2597.0**	**2885.7**	**3206.3**
Other Operat Rev	33.0	33.8	35.7	38.9	43.2	48.0
Net Rev from Ops	2320.0	2507.1	2454.7	2635.9	2928.9	3254.3
Cost of Mat Cons	1443.5	1625.7	1543.1	1660.3	1833.0	2029.4
Employee Exp	162.6	188.4	185.6	190.3	194.9	206.2
Other Expenses	409.5	444.4	486.4	502.3	544.1	595.9
Total Expenses	2015.6	2258.5	2215.0	2352.9	2572.0	2831.4
EBITDA	**304.4**	**248.6**	**239.7**	**283.0**	**357.0**	**422.8**
Depreciation	98.3	101.9	111.5	111.8	104.4	104.5
EBIT	206.1	146.7	128.2	171.2	252.6	318.3
Interest	0.4	0.2	0.1	0.0	0.0	0.0
Other Income	37.8	58.9	74.0	79.3	81.5	85.4
Profit before Tax	243.4	205.4	202.1	250.5	334.0	403.6
Tax Expenses	65.0	62.3	36.1	82.7	100.6	116.7
PAT	178.5	143.1	166.0	167.8	233.4	286.9
Extraordinar Item	0.0	0.0	-25.5	0.0	0.0	0.0
Net Profit	**178.5**	**143.1**	**140.5**	**167.8**	**233.4**	**286.9**
EPS [in Rupees]	**12.3**	**9.9**	**9.7**	**12.1**	**14.8**	**17.6**

Cash Flow Statement

Particulars, Rs in Cr	FY14	FY15	FY16	FY17E	FY18E	FY19E
EBT	**243.4**	**205.4**	**176.7**	**258.4**	**314.5**	**370.6**
Depriciation	98.2	101.8	111.4	111.8	104.4	104.5
Interest /Dividend paid	0.4	0.2	0.1	0.0	0.0	0.0
Other Adjustment	-36.2	-62.5	-79.8	-39.2	-23.4	-13.6
(Inc)/Dec in Work Cap	130.1	172.3	-69.6	-66.1	-19.7	-32.3
Tax Paid	-97.9	-77.9	-44.9	-80.0	-87.9	-100.0
CF from Operating	**338.0**	**339.3**	**93.8**	**184.8**	**288.0**	**329.3**
Capital expenditure	-66.9	-66.4	-76.5	-82.0	-85.0	-105.0
Sale of fixed assets	2.0	1.5	0.4	0.5	0.5	0.5
Change in Investments	-190.0	-239.6	156.5	-10.1	-[illegible]	-158.1
Others	30.6	22.4	1.9	25.0	27.5	30.3
CF from Investing	**-224.3**	**-282.1**	**82.2**	**-70.4**	**-[illegible]**	**-232.3**
Inc/(Dec) in Share capital	0.0	0.0	0.0	0.0	0.0	0.0
Inc/(Dec) in Debt	0.0	0.0	0.0	0.0	0.0	0.0
Dividend and Interest Paid	-84.5	-84.3	-166.9	-87.0	-87.0	-87.0
CF from Financing	**-84.5**	**-84.3**	**-179.6**	**-87.0**	**-87.0**	**-87.0**
Net Cash Flow	**29.2**	**-27.2**	**-3.6**	**27.4**	**7.4**	**10.0**
Opening Balance	**23.2**	**52.4**	**25.3**	**34.4**	**61.8**	**69.2**
Closing Balance	**52.4**	**25.3**	**34.4**	**61.8**	**69.2**	**79.1**

(Source: Company, HDFC sec)

Balance Sheet

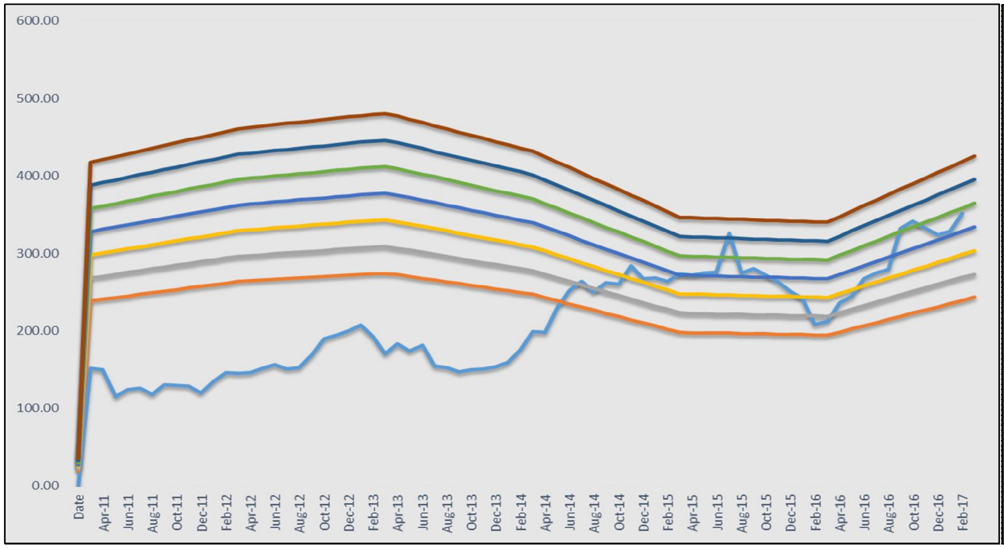
Particulars, Rs in Cr	FY14	FY15	FY16	FY17E	FY18E	FY19E
LIABLITIES						
Share Capital	28.9	28.9	28.9	28.9	28.9	28.9
Reserves and Surplus	1238.3	1312.5	1410.8	1507.0	1634.1	1786.7
Shareholders' Funds:	**1267.2**	**1341.4**	**1439.8**	**1535.9**	**1663.0**	**1815.6**
DTL	30.3	28.9	17.7	9.6	8.7	14.0
Other L T Liabilities	13.1	16.8	17.9	9.6	8.7	14.0
Long Term Provisions	24.6	24.5	22.9	12.7	11.6	18.7
Non-Current Liabilities:	**68.0**	**70.2**	**58.5**	**31.9**	**28.9**	**46.7**
Trade Payables	312.4	337.6	331.5	354.9	390.6	432.4
Other Current Liabilities	101.5	65.9	95.3	69.0	81.4	90.1
Short Term Provisions	101.8	117.3	33.4	69.0	70.5	78.1
Current Liabilities:	**515.8**	**520.8**	**460.2**	**492.9**	**542.5**	**600.6**
Total	***1851.0***	***1932.4***	***1958.5***	***2060.7***	***2234.4***	***2462.9***
ASSETS:						
Fixed Assets:	**585.0**	**534.9**	**506.2**	**476.5**	**457.0**	**457.5**
Non-Current Investments	10.0	5.3	3.6	3.6	3.6	3.6
L T Loans and Advances	95.7	108.4	103.3	110.0	108.2	108.4
Other Non-Current Invts	29.0	32.0	12.2	20.8	32.5	32.5
Non-Current Assets:	**719.7**	**680.5**	**625.3**	**610.9**	**601.4**	**602.0**
Current Investments	597.7	871.1	783.1	778.7	885.3	1012.9
Inventories	166.8	171.6	202.9	218.1	244.1	279.3
Trade Receivables	177.4	52.6	152.2	181.1	199.3	220.6
Cash and Bank Balances	52.4	25.3	39.5	61.8	69.2	79.1
S T Loans and Advances	101.7	100.2	118.2	123.6	124.5	142.4
Other Current Assets	35.3	31.1	37.3	86.5	110.7	126.6
Current Assets:	**1131.3**	**1251.9**	**1333.2**	**1449.8**	**1633.0**	**1861.0**
Total	***1851.0***	***1932.4***	***1958.5***	***2060.7***	***2234.4***	***2462.9***

Ratios

Particulars	FY14	FY15	FY16	FY17E	FY18E	FY19E
No of Equity Shares-cr	14.5	14.5	14.5	14.5	14.5	14.5
Entreprise Value-cr	5415.4	5442.6	5428.3	5406.0	5398.7	5388.7
EPS	12.3	9.9	9.7	12.1	14.8	17.6
Cash EPS	19.1	16.9	17.4	19.9	22.0	24.8
Book Value (Rs.)	87.6	92.8	99.6	106.2	115.0	125.6
PE(x)	30.6	38.2	38.9	31.1	25.6	21.5
P/BV (x)	4.3	4.1	3.8	3.6	3.3	3.0
Mcap/Sales(x)	2.4	2.2	2.2	2.1	1.9	1.7
EV/EBITDA	17.8	21.9	22.6	18.6	16.0	13.8
EBITDAM (%)	13.1%	9.9%	9.8%	11.0%	11.6%	12.1%
EBITM (%)	8.9%	5.9%	5.2%	6.8%	8.0%	8.9%
PATM (%)	7.7%	5.7%	5.7%	6.6%	7.4%	7.9%
ROCE (%)	20.1%	15.8%	14.5%	17.4%	19.7%	21.3%
ROIC (%)	31.2%	28.0%	24.3%	27.4%	33.4%	40.0%
RONW (%)	14.7%	11.0%	10.1%	11.8%	13.4%	14.6%
Current Ratio	2.2	2.4	2.9	3.0	3.0	3.1
Quick Ratio	1.9	2.1	2.5	2.5	2.6	2.6
Debt-Equity	0.0	0.0	0.0	0.0	0.0	0.0

(Source: Company, HDFC sec)

One Year forward P/E Chart:



One Year Price Chart

(Source: Company, HDFC sec)

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