Constructions

Institutional Equity Research

Results Preview | July 15, 2019

Decent Quarter Expected despite Challenges

While a robust pick-up in order book over last three years has been aiding the construction companies to witness decent revenue growth for last couple of quarters despite several projects are stuck due to land availability issues, we believe their performance should continue to be decent in 1QFY20. However, higher YoY base and delay in obtaining Appointed Dates (ADs) for the HAM projects will have a cascading effect on overall growth. We believe likely deterioration in working capital cycle for several companies along with higher depreciation due to higher capex led by higher order book is expected to impact earnings growth. The companies under our coverage universe have witnessed an aggregate ~15% YoY growth in their order book mainly supported by healthy order awarding across segments. While the NHAI awarded road projects of 7,400kms (Rs1.2trln in value terms) in FY18, awarding activities slowed considerably in FY19, as the NHAI could award mere ~2,200kms in FY19 led by delay in land acquisition and funding constraints. Further, cumulative road projects awarded by the NHAI and the Ministry of Road Transport & Highways (MoRTH) declined to 5,543kms in FY19 vs. 24,452kms in FY18. The NHAI is likely to award >6,000kms highway projects in FY20 with a focus on awarding projects with adequate land availability for the benefits of all related stakeholders.

As the government emphasises on Rs100trln of investment in infrastructure segment over the next five years, there should not be any dearth of fresh orders for the construction companies in India. A humongous order awarding during the NDA 1.0 helped most companies to shore up their outstanding order book to almost 3-3.5x sales, which is the highest in recent history. Hence, even though the order inflows remain low in FY19, the companies will not worry much to generate growth and would rather focus on execution and convert some of these orders to revenue to drive growth. The companies under our coverage are likely to report an aggregate top-line growth of ~18% YoY and earnings growth of 12%. Notably, growth is expected to improve further in subsequent quarters with the recently awarded HAM projects coming to execution phase.

Revenue Growth to Remains Firm amid Labour & Water Crisis

Along with slowdown in order inflow led by election code of conduct, water shortage and labour crisis were the key concerns for the construction companies in 1QFY20, which have certainly impacted the pace of construction in several projects across the country. Despite that, we expect the construction companies under our coverage to report aggregate revenue growth of ~18% YoY mainly due to higher order book accumulated over the last four years. Aggregate order book of the companies under our coverage witnessed ~15% growth in FY19, as the quality companies continued to witness sizeable growth in their order book. We foresee revenue growth to witness further traction, going ahead with the recently awarded HAM projects coming to execution phase. Concerns over funding through state-owned banks due to capital crisis and land acquisition delay resulted in delay in projects awarding. However, for the quality projects and the companies maintaining healthy balance sheet and cash flow generation, funding should not be a big hurdle, in our view.

New Order Awarding to Pick-up Pace

Given likely expenditure of Rs100trln over the next five years, as envisaged by the government and likely pick-up in road awarding activities in the ensuing months, we expect the construction companies to witness sizeable order inflows here on. Notably, most construction companies have given increased guidance of order inflow for FY20, as several tenders are likely to be floated shortly. However, funding of annual Rs20trln infrastructure projects would be quite challenging for the government and hence PPP model is likely to be promoted again with upgraded version.

Top Sectoral Picks: NCC & Ahluwalia Contracts

While NCC is expected to report over ~24% YoY earnings growth led by sustained pick-up in execution in key projects and robust order book, Ahluwalia is expected to deliver an earnings growth of ~19% owing to commencement of execution from the key stalled projects. However, NCC's exposure to Andhra Pradesh (~Rs60bn) may result in moderate cut in earnings, which is already factored in the current market price.

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Exhibit 1: Quarterly Results Preview

Company	1QFY20E	1QFY19	% yoy chg.	4QFY19	% qoq	
KNR Construction						
Net Sales	6,100	5,564	9.6	7,157	(14.8)	Commencement of HAM projects to aid yoy revenue
EBITDA	1,007	1,099	(8.4)	1,441	(30.2)	
EBITDA margins (%)	16.5	19.7		20.1		Margins are considered as per the guidance of the Management
APAT	575	740	(22.3)	938	(38.8)	Lower margins to result in earnings de-growth
Net Margin (%)	9.4	13.3		13.1		
J Kumar Infra						
Net Sales	7,400	6,184	19.7	9,680	(23.6)	Consistent traction in metro projects execution to drive yoy growth
EBITDA	1,147	1,000	14.8	1,341	(14.4)	
EBITDA margins (%)	15.5	16.2		13.8		margins should improve qoq led by high margin contributing works
APAT	443	402	10.3	573	(22.6)	
Net Margin (%)	6.0	6.5		5.9		
Ahluwalia Contracts						
Net Sales	4,600	4,039	13.9	4,874	(5.6)	Execution ramp up from key projects viz- Delhi re-deveopment projects to aid revenue
EBITDA	598	526	13.8	567	5.5	
EBITDA margins (%)	13.0	13.0		11.6		Margin is expected to remain in guided range of management at 13%-13.5%
APAT	335	282	19.0	310	8.2	Healthy revenue to drive earnings growth
Net Margin (%)	7.3	7.0		6.4		

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Quarterly Results Preview

Company	1QFY20E	1QFY19	% yoy chg.	4QFY19	% qoq	
NCC						
Net Sales	27,800	23,596	17.8	33,889	(18.0)	Robust order book to drive strong YoY revenue growth
EBITDA	3,197	2,678	19.4	3,977	(19.6)	
EBITDA margins (%)	11.5	11.3		11.7		Margins is considered as per the guidance of management
APAT	1,285	1,037	24.0	1,820	(29.4)	Strong revenue booking to drive yearly earnings growth
Net Margin (%)	4.6	4.4		5.4		
NBCC						
Net Sales	19,500	16,335	19.4	23,776	(18.0)	Robust order book to drive YoY revenue growth despite slowdown in Delhi redevelopment projects
EBITDA	897	629	42.6	1,788	(49.8)	
EBITDA margins (%)	4.6	3.9		7.5		Better margins from PMC to drive YoY margins improvement
APAT	863	677	27.5	1,528	(43.5)	Healthy revenue and margins to resulted in decent yoy profit growth
Net Margin (%)	4.4	4.1		6.4		
HG Infra.						
Net Sales	5,350	4,502	18.8	5,800	(7.8)	Strong order book and sustained execution to drive revenue growth
EBITDA	803	671	19.6	932	(13.9)	
EBITDA margins (%)	15.0	14.9		16.1		Margins are expected to be under guidance range of the company
APAT	312	270	15.5	367	(15.1)	Strong revenue booking and healthy margins to result in YoY earnings growth
Net Margin (%)	5.8	6.0		6.3		

Source: Company, RSec Research

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Exhibit 2: Valuations table

	CMP*	Recommendation	Target Price	M.Cap	P/E (x)		EV/EBITDA (x)		RoE (%)	
	(Rs)		(Rs)	(Rs bn)	FY20E	FY21E	FY20E	FY21E	FY20E	FY21E
KNR Construction	261	BUY	315	37	16.5	14.0	9.8	7.4	14.6	14.9
J Kumar Infra.	146	BUY	260	11	5.5	4.6	2.8	2.2	11.5	12.4
Ahluwalia Contracts.	330	BUY	440	22	14.7	11.9	7.7	6.0	18.5	18.9
NCC Ltd	85	BUY	170	51	8.0	6.5	4.5	3.8	12.7	14.0
NBCC	54	HOLD	64	97	24.8	19.9	20.4	15.2	26.1	27.3
HG Infra	262	BUY	395	17	10.7	8.7	5.7	4.8	23.1	22.9

*Source: Company, RSec Research ; Note: *CMP as on July 15, 2019*

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Rating Guides

Rating	Expected absolute returns (%) over 12 months
BUY	>10%
HOLD	-5% to 10%
REDUCE	>-5%

NAVEEN KULKARNI

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