Power T&D

Capex boom underway, established players to make hay

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1 April, 2016

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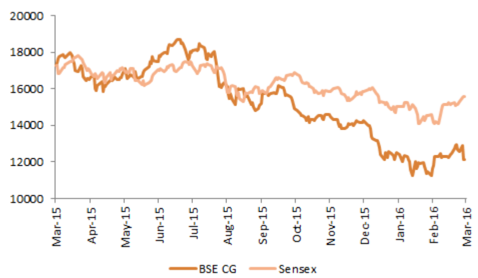
SECTOR REPORT

Industry	Power T&D

BSE Capital Goods v/s Sensex



Source: Systematix Institutional Research

Indian power transmission sector is undergoing the largest-ever capex cycle, as the historical lag in transmission capacity addition versus generation capacity and investments in transmitting power efficiently over longer distances are coming into play at the same time. During FY17e-22e, we expect cumulative investments of over Rs2.6tr to be made by PGCIL, SEBs and the private sector. This is higher than the cumulative actual investments in the past 10 years. We believe "UDAY scheme" will be a transformation for SEBs over the next two to three years, thus freeing their capital to invest in essential T&D lines. We believe a right tariff structure and attractive IRR is generating strong interest in projects based on the Tariff Based Competitive Bidding (TBCB), even from private sector players. Globally too transmission lines are getting a priority as the developing regions of Latin America, the Middle East and Africa are set to receive investments of US$127bn, US$61bn and US$135bn respectively over 2014-30 in the sector. We believe Indian transmission line EPC and tower manufacturing companies which derive 40-50% of their order book/revenue from international operations are likely to benefit from the global investment surge in the sector. Our top picks are Kalpataru Power (for maintaining the order book momentum in both domestic and international markets) and Techno Electric (continues to lead the market with industry-leading operating efficiency). We also have a Buy on Skipper (will continue to derive the benefits of low cost operations and locational advantage) and an Accumulate on KEC International (will maintain the leadership position, OPM improves but to remain below peers).

Established players with T&D as core competency in the spotlight

Under-investments in the transmission sector have led to idle generation capacities, regional power deficits, load shedding and power outages in the country. To address these issues, PGCIL is driving the capex momentum by spending Rs1.1tr in the 12th plan and Rs1.2tr in the 13th plan. SEBs have lagged in the new intra-state line investments, which we believe will be resolved on successful implementation of UDAY. Transmission lines are increasingly getting added at voltages of 765kV and HVDC -- target of 63% and 69% growth in 13th plan compared to 12th plan. Payment cycles and execution timelines are being made stringent by large utilities like PGCIL to ensure timely completion of these systemically vital projects. All these factors are leading to concentration of orders in value terms (60-70% of total value), with the top four to five players like KECI, L&T, KPTL and Tata Projects leading on the transmission line front and TEEC, BHEL, EMCO, CGL and prominent Korean and Chinese players on the substations front. Skipper dominates the tower supply space in PGCIL as well as private sector orders and is likely to be a major beneficiary.

TBCB and UDAY to deleverage SEBs balance sheet leading to new investments

We expect TBCB's booster role to continue for the cash-strapped utilities, which through global BOOT tenders for transmission lines have been attracting aggressive participation from PGCIL and private sector players. The UDAY scheme, initiated in November 2015, has got an encouraging response as 15 states have signed preliminary MoUs with the central government. These states cumulatively account for 80% of SEBs' losses. We believe UDAY's success lies in the faster issuance of bonds by states and milestone-based achievement on operational parameters like AT&C loss reduction and smart metering. We believe the above two initiatives will lead to SEBs' deleveraging, resulting in new order roll-out.

Opportunities galore for Indian players in international markets

The global transmission market is expected to witness an overall capex of US$1.8tr over 2014-30. Indian players have major operations in Latin America, the Middle East and Africa and these regions are expected to receive cumulative investments of US$323bn over 2014-30. In our view, the ability to win and execute over 30-40 projects in various countries across the globe cannot be developed overnight by newer players, and thus will give a first-mover advantage to KECI and KPTL. Skipper, with a presence in Latin America for the past two years, has created a brand impact in these markets and is expected to be a major tower supplier in the region.

Top picks

	CMP (Rs)	TP (Rs)	Upside (%)	Reco.
Kalpataru Power	205	281	37%	Buy
KEC International	122	138	13%	Accumulate
Techno Electric	535	640	20%	Buy
Skipper	134	182	36%	Buy

Source: Systematix Institutional Research

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Coverage universe snapshot

Table 1: Comparative analysis of coverage companies

	Kalpataru Power		KEC Intl		Techno Electric		Skipper	
	FY17e	FY18e	FY16e	FY17e	FY17e	FY18e	FY17e	FY18e
Bloomberg Code	KPP IN		KECI IN		TEEC IN		SKIPPER IN	
Market Cap (Rs bn)	32.2		30		30		14	
CMP (Rs)	205		120		535		134	
TP (Rs)	281		138		640		182	
Upside (%)	34%		15%		20%		36%	
PE (x)	13.6	11.1	12.2	10.6	22.0	17.7	13.4	11.0
P/B (x)	1.3	1.2	1.8	1.6	2.7	2.4	2.8	2.2
EV/EBITDA (x)	7.1	6.0	4.6	3.7	13.2	12.0	6.2	5.2
ROE (%)	9.9	11.1	15.9	15.9	13.0	14.3	22.9	22.2
ROCE (%)	11.1	12.4	18.2	18.3	10.7	11.5	28.4	28.1
OPM (%)	10.6	10.8	7.7	7.5	20.4	19.5	15.7	15.7
PBIT Margin (%)	8.7	9.1	6.7	6.6	15.5	15.2	14.1	14.3
NPM (%)	4.4	4.6	2.5	2.6	11.6	12.5	6.0	6.3
Net D/E (x)	0.15	0.1	1.1	0.8	0.2	(0.15)	0.6	0.4
Sales (Rs mn)	52,368	61,105	100,641	114,481	11,878	13,696	16,986	19,879
EBITDA (Rs mn)	5,525	6,569	7,749	8,529	2,418	2,673	2,667	3,121
PAT (Rs mn)	2,256	2,790	2,566	2,964	1,391	1,726	1,022	1,246
EPS (Rs)	15.0	18.5	10.0	11.5	24.4	30.2	10.0	12.2
OCF (Rs mn)	4,829	1,654	3,272	4,215	1,234	1,683	10.0	12.2
FCF (Rs mn)	4,329	1,154	2,472	3,415	984	1,433	315	366
Net worth (Rs mn)	24,287	26,855	17,260	19,927	11,204	12,700	4,983	6,230
Capital Employed (Rs mn)	36,216	40,006	40,493	43,672	16,138	17,228	9,508	11,239
Interest coverage ratio (x)	3.5	3.7	2.9	3.1	6.7	13.9	3.1	3.3
Working Capital Days	97	96	(15)	38	89	89	110	110
Debtors (days)	150	150	190	190	170	170	110	110
Asset Turnover Ratio (x)	11.1	14.5	8.1	9.3	1.6	2.0	4.4	5.2
Order book (Rs mn)	80,954	96,422	113,015	123,209	20,141	22,482	24,842	25,035
Order book/ sales (x)	1.5	1.6	1.1	1.1	1.7	1.6	1.5	1.2

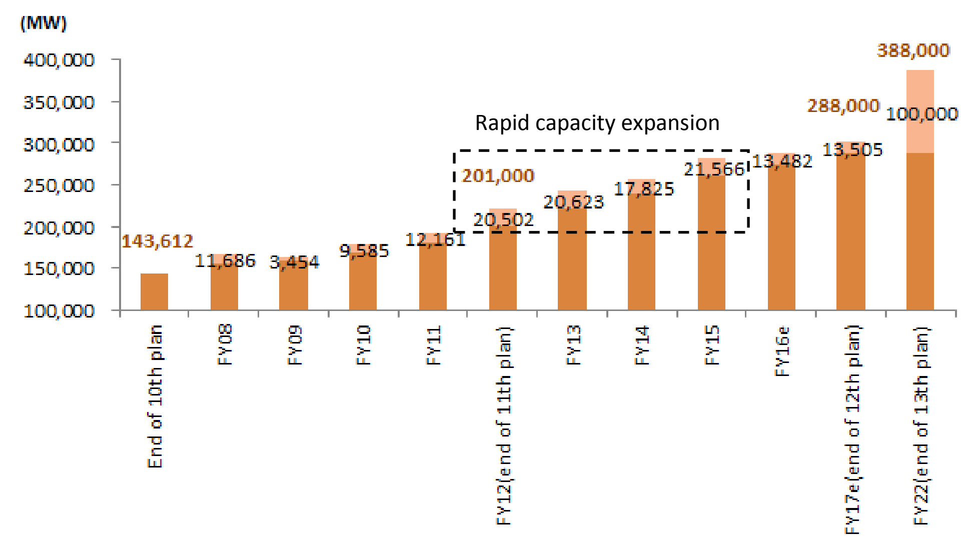
Source: Systematix Institutional Research

Power generation capacity addition in last 10 years

India achieved substantial progress in power capacity addition in the last 10 years. For decades, the Indian power sector was marred by under-achievement of the targeted capacity additions. Execution speed significantly improved in the 11th plan, when the country as a whole added 57,388MW against the targeted capacity addition of 78,700MW, a target achievement of 73%. The pace of execution improved even further in the 12th plan as the private sector, which started contributing from the 11th plan, is expected to account for as much as 53% of the capacity addition in the 12th plan. Target for the 12th plan capacity addition has been set at 88,537MW, of which ~78,000MW has already been achieved. As of January 2016, the installed capacity in India stood at 288,000MW, suggesting inevitable execution of the remaining ~10,000MW from the 12th plan in the next 13 months. From the end of the 7th plan, India added power generation capacity at a CAGR of 6.5% till date.

The central government has set an ambitious target of adding 100GW of solar power and 60GW of wind power by 2022 and is expecting an execution of 30,000MW in FY16 itself.

Chart 1: Power generation capacity addition gained pace since 11th plan



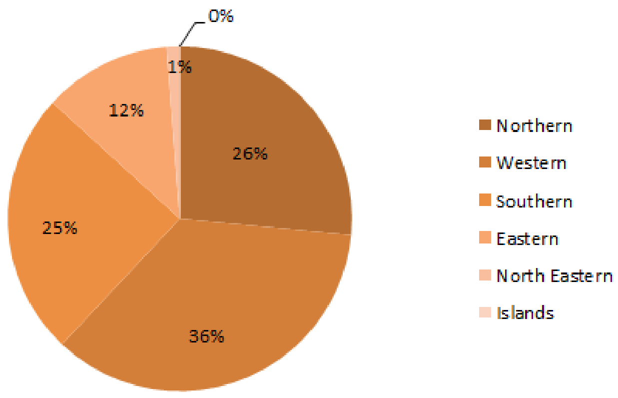
Source: Systematix Institutional Research

Western India contributes the highest proportion of installed capacity due to two UMPPs and a high number of private sector capacities in the region. The Northern region also contributes significant capacity due to a large number of pithead-based thermal power projects in the region.

Private sector accounts for over 40% of the total installed capacity of 288GW dominated by utilities like Tata Power, Reliance Power, Adani Power and JSW Energy. Among the central government-owned companies, NTPC continues with its rapid capacity expansion. Central sector accounts for 34%, while the remaining 26% is accounted by the state sector.

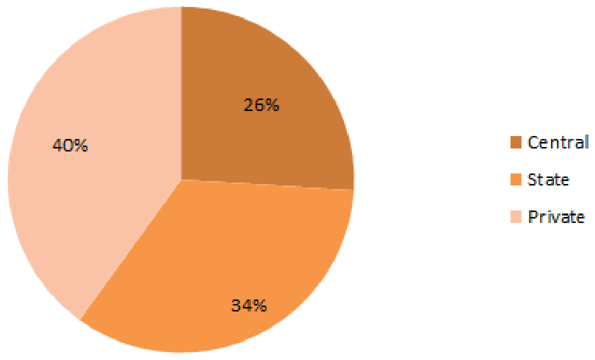
Installed capacity analysis – 288GW as of Feb 2016

Chart 2: Installed capacity – geography-wise



Source: Systematix Institutional Research

Chart 3: Installed capacity – sector-wise



Source: Systematix Institutional Research

With a current installed capacity of 288GW, India ranks among the top power producers in the world, while the per capita power consumption of 1,010 kilowatt-hour (kwh) in 2014-15 is much lower than the world average of ~2,980kwh. This is due to inadequate last mile transmission infrastructure and inefficient transmission and distribution, which causes power deficits in high demand areas, blackouts, load shedding in rural areas and high cost of power to industries.

Table 2: Transmission line capacity addition since 8th plan (ckms)

	At the end of 8th Plan	At the end of 9th Plan	At the end of 10th plan	At the end of 11th plan	As on 31 Jan 16	At the end of 12th plan	At the end of 13th plan
+500 kV HVDC	1,634	4,738	5,872	9,432	12,938	16,872	27,472
% growth		190%	24%	61%		79%	62.8%
765 kV	-	1,160	2,184	5,250	24,073	32,250	54,450
% growth			88%	140%		514%	68.8%
400 kV	36,142	49,378	75,722	106,819	145,249	144,819	174,819
% growth		37%	53%	41%		36%	20.7%
220 kV	79,600	96,993	114,629	135,980	155,722	170,980	NA
% growth		22%	18%	19%		26%	
Total	117,376	152,269	198,407	257,481	337,982	364,921	-
% growth		30%	30%	30%		42%	

Source: Systematix Institutional Research

Table 3: Substations capacity addition since 8th plan (MW/MVA)

	At the end of 8th Plan	At the end of 9th Plan	At the end of 10th plan	At the end of 11th plan	As on 31 Jan 16	At the end of 12th plan	At the end of 13th plan
+500 kV HVDC Converter/BTB Station	-	5,200	8,200	9,750	15,000	22,500	37,500
% growth	-	-	58%	19%	-	131%	67%
765 kV	-	-	-	25,000	135,000	174,000	253,000
% growth	-	-	-	-	-	596%	45%
400 kV	40,865	60,380	92,942	151,027	203,392	196,027	245,027
% growth		48%	54%	62%		30%	25%
220 kV	84,177	116,363	156,497	223,774	284,549	299,774	-
% growth		38%	34%	43%	-	34%	-
Total	125,042	181,943	257,639	409,551	637,941	692,309	535,528
% growth		46%	42%	59%	-	69%	

Source: Systematix Institutional Research

Since the beginning of 11th plan, the central government started focusing on extra high voltage 765kV transmission lines under the aegis of PGCIL. The segment grew rapidly since then posting a CAGR of 24% during FY2002-16 with mainly imported technology. Investments in the segment have been raised by a whopping 514% for the 12th plan and incremental 68.8% in the 13th plan, with a compulsory domestic manufacturing clause for various products like 765kV transformers, conductors, and Gas Insulated Switchgears (GIS).

The 400kV transmission lines have become mainstay of inter-state networks as the segment has clocked a CAGR of 8% during FY2002-16.

Inter-regional transmission capacity

By the end of 12th plan, it is expected that the National Grid's inter-regional power transfer capacity will be ~72,250MW. These transmission schemes include 765kV and 400kV transmission system strengthening in the Northern, Western, Southern, North Eastern regions and would facilitate transfer of power from the new hydro electric projects in Bhutan and the generation-linked projects in Chhattisgarh, Odisha among others. At February 2016-end, the inter-regional capacity had already touched 57,450mw, indicating a strong traction in PGCIL-led projects. The synchronous connection of Southern grid with rest of the nation has led to a reduction in the exchange rate of power from Rs6-7 per unit to Rs3-4 per unit. On certain days, an uniform price across the country was achieved, thus portraying that the congestion has been reduced to nil.

Since July 2014, with the commissioning of 765kV transmission lines of Wardha-Aurangabad, Aurangabad-Sholapur, Sholapur-Pune, Raichur- Kurnool and Kolhapur-Narendra, the transfer capacity to southern grid increased from 3,450MW to 5,900MW. This would be further enhanced to ~18,000MW in different phases on completion of the following transmission lines which are already under implementation with an investment of ~Rs380bn:

1) Angul-Srikakulam-Vemagiri 765kv d/c line along with realignment works at Vemagiri and system strengthening beyond Vemagiri -- Vemagiri-C'peta-Cuddapah 765kV d/c line
2) Wardha-Nizamabad-Hyderabad 765kV d/c line
3) Warora Pool-Warangal (New) 765kV d/c line
4) +800kV, 6,000MW Raigarh-Pugalur-North Trichur HVDC bipole link

Table 4: Strengthening of National Grid looks achievable (in MW)

Break-up	Capacity at the end of 10th Plan Actual	11th Plan addition Actual	Capacity at the end of 11th Plan Actual	12th Plan addition Target	12th Plan addition Expected	Expected at the end of 12th Plan	Cumulative 12th Plan addition (Up to Feb-16)	Capacity As on Date (Upto Feb-16)
	1	**2**	**3**	**4**	**4A**	**5(3+4A)**	**6**	**7=(3+6)**
ER - NR	3,430	8,700	12,130	5,800	5,800	17,930	3,700	15,830
ER - WR	1,790	2,600	4,390	8,400	8,400	12,790	8,400	12,790
ER - SR	3,130	500	3,630	-	-	3,630	-	3,630
ER – NER	1,260	-	1,260	1,600	1,600	2,860	1,600	2,860
Sub Total	**9,610**	**11,800**	**21,410**	**15,800**	**15,800**	**37,210**	**13,700**	**35,110**
WR - NR	2,120	2,100	4,220	10,200	12,700	16,920	8,700	12,920
WR - SR	1,720	(-)200*	1,520	6,400	6,400	7,920	6,400	7,920
Sub Total	**3,840**	**1,900**	**5,740**	**16,600**	**19,100**	**24,840**	**15,100**	**20,840**
NR - NER	-	-	-	6,000	6,000	6,000	1,500	1,500
132kV (Inter Regional)	600	-	600	-	-	-	-	600
Grand Total	**14,050**	**13,700**	**27,750**	**38,400**	**40,900**	**68,050****	**30,300**	**57,450****

Source: PGCIL, Systematix Institutional Research

Power deficit persists despite an increase in capacities

Table 5: Power demand and supply conditions in India over past five years

Years	Requirement (mu)	Availability (mu)	Surplus(+)/Deficits(-) (mu)	Surplus(+)/Deficits(-) (%)
2010-11	861,591	788,355	(73,236)	-8.5%
2011-12	937,199	857,886	(79,313)	-8.5%
2012-13	995,557	908,652	(86,905)	-8.7%
2013-14	1,002,257	959,829	(42,428)	-4.2%
2014-15	1,068,943	1,030,785	(38,158)	-3.6%
Apr 15 -Feb 16	1,017,954	995,980	(21,974)	-2.2%

Source: Systematix Institutional Research

Table 6: Region-wise power deficit - April to February 2016

Years	Requirement (mu)	Availability (mu)	Surplus(+)/Deficits(-) (mu)	Surplus(+)/Deficits(-) (%)
Northern	315,112	299,758	(15,354)	-4.9%
Western	316,123	315,323	(800)	-0.3%
Southern	259,942	255,710	(4,232)	-1.6%
Eastern	113,487	112,617	(870)	-0.8%
North Eastern	13,291	12,572	(719)	-5.4%
All India	1,017,955	995,980	(21,975)	-2.2%

Source: Systematix Institutional Research

Despite a rapid increase in power generation capacity from 2010 till date, a CAGR of 8.5%, the deficit in supply and demand of power continues. Power deficit was at a staggering 8.5% in FY10-11, which declined to 3.6% in FY15 -- part of the decline has been due to a slowdown in industries and agriculture in the past two years. During April 2015 to February 2016, the deficit fell to 2.2%, which is the lowest in the past five years.

Deficit also persists region-wise where the resource-rich states in Central and Northern parts of India continue to have excess power, while the metro cities, Southern and North Eastern states still face a huge shortage of power. The absence of an integrated National Grid had been the major cause of persisting deficits, which was partially solved in July 2014 when the Southern grid was integrated in the National Grid. Now, PGCIL is looking to expand the current power transfer capacity of 5,800mw to the Southern grid to 18,000MW by the end of 13th plan.

The creation of a green corridor to integrate all the upcoming renewable capacity is expected to solve the issue of peak deficit in metro cities.

Significant investment lined up to boost transmission infrastructure

Table 7: Plan-wise requirement of investments in the sector

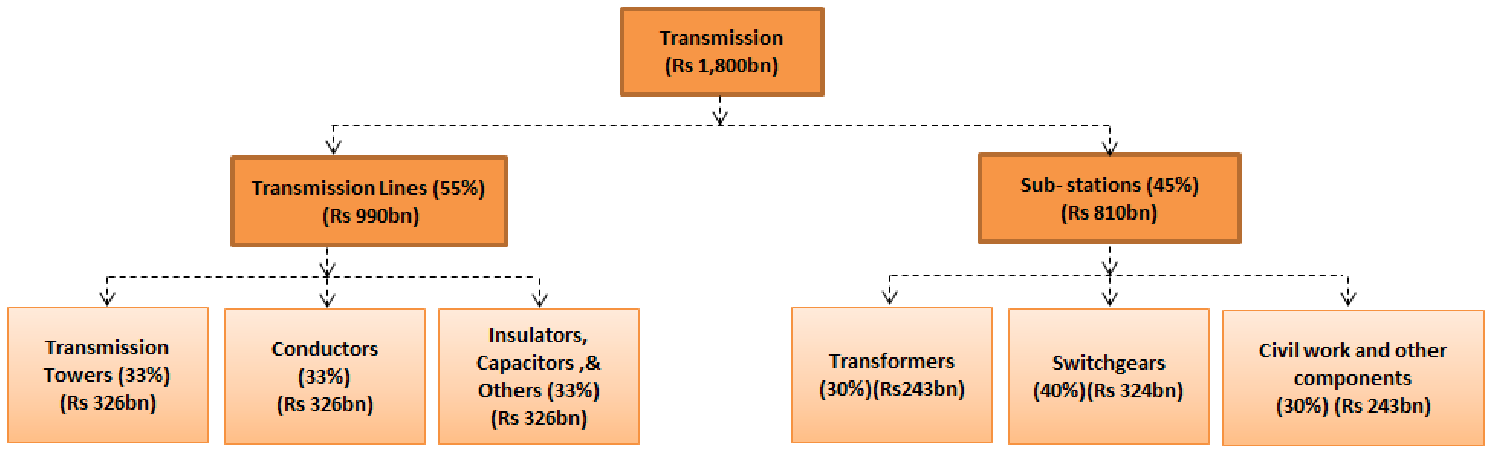
(Rs bn)	10th Five Year Plan	11th Five Year Plan	12th Five Year Plan (e)	13th Five Year Plan (e)
Generation	1,826	4,796	6,386	6,000
T&D	877	2,230	4,860	5,600
- Transmission	457	1,230	1,800	2,600
-Distribution	420	1,000	3,060	3,000
Investments in T&D as % of generation	48%	46%	76%	93%

Source: PGCIL, Systematix Institutional Research

As per the National Electricity Plan document published by the Central Electricity Authority in November 2012, the total fund requirement for the development of transmission system in the 12th and 13th plans is estimated to be Rs4lakh crore during both the plan period together, which will cover all the states/UTs.

As a rule of thumb, investments in transmission and distribution sector combined should be equivalent to the investments in generation sector. Historically, investments in T&D have lagged considerably in India leaving a big gap in the T&D network. Investments planned in T&D sector combined at the start of the 12th plan were almost 76% of the investments in generation. Actual capex on the transmission front has been in line with the targets as close to 75%, and 81% volume targets have already been achieved till February 2016 in transmission lines and substations respectively.

Chart 4: Investments in transmission sector – category-wise (12th plan)



Source: Systematix Institutional Research, Industry

PGCIL – the sector driver

Acting as a Central Transmission Utility (CTU) with the responsibility of creating the transmission network for the country, Powergrid Corp (PGCIL) has achieved remarkable progress. As of Dec 31, 2015, the transmission assets owned and operated by the company stood at 127,539ckm of extra high voltage (EHV) transmission lines and 205 number of EHVAC & High Voltage Direct Current (HVDC) sub-stations with 248,164mva transformation capacity. The company owns and operates over 90% of the inter-state network in the country. PGCIL is a pioneer in adapting state-of-the-art technologies like 765kv (now attempting 1,200kv), HVDC lines, FACT and STATCOM.

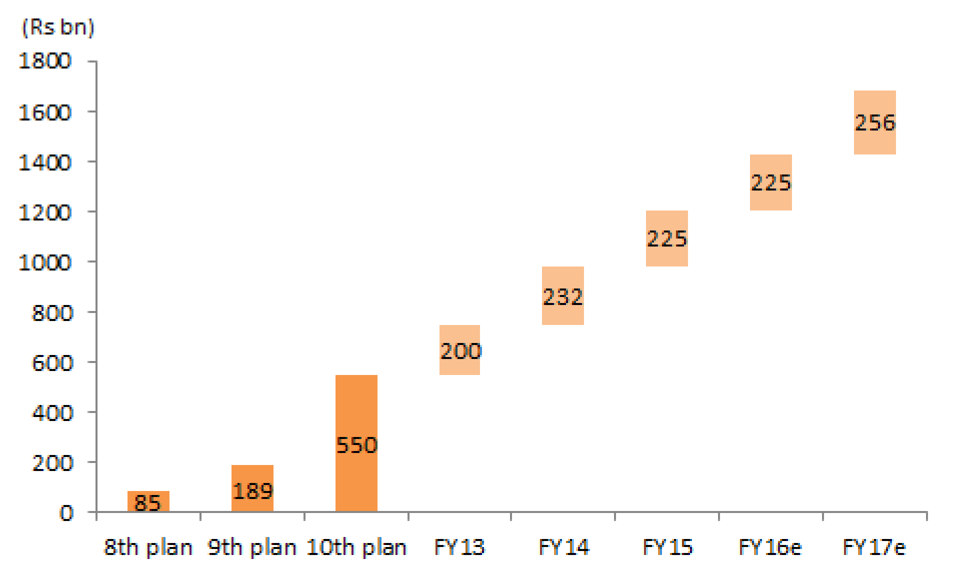
The company has taken the initiative and developed indigenously 1,200kv Ultra High Voltage (UHC) AC technology, the highest transmission voltage level in the world, in collaborative efforts with domestic manufacturers. On this front, PGCIL has successfully established the 1,200kv UHVC test station at Bina, including test-charge of 1,200 kv single and double circuit transmission lines as a pilot project.

Few significant projects currently under implementation by PGCIL are:

1) Construction of the 1,200kV upgradable transmission line from Wardha to Aurangabad (~350km length), to be with the introduction of higher voltage transmission systems like 765kV Double Circuit transmission lines, +800kV UHVDC and 1,200kV UHVAC transmission lines
2) Construction of UHVDC line -- +800kV, 6,000MW HVDC line from Biswanath Chariyali (Assam) to Agra (Uttar Pradesh) via Alipurduar (West Bengal) (~1,750km long), facilitating the transfer of bulk power from North Eastern region to the Northern region through the constricted "chicken neck area".
3) +800kV HVDC line between Champa (Western region) and Kurukshetra (Northern region) having a length of ~1,400km.

PGCIL expects to incur a capex of Rs1,100bn in the 12th plan, of which the company has already spent ~Rs788bn by Dec 31, 2015 and is on the path to incur the remaining capex of Rs312bn by FY17-end. For the 13th plan, it is expected to incur a capex of Rs 1,200bn.

Chart 5: PGCIL capex since the 8th plan



Source: Systematix Institutional Research

PGCIL has been entrusted the task to independently create capacities in the following two segments:

1) **North Eastern region**

The North East region suffers from chronic power deficit throughout the year as it severely lacks the transmission network to facilitate smooth flow of power from other regions. The central government is planning a 400kV ring system along with five new 400kV substations to provide a quantum boost to inter-state transmission system in North East, at an estimated cost of ~Rs350bn. This inter-connection shall facilitate enhanced exchange of power among states within the North East as well as other parts of the country. These schemes are planned to be commissioned progressively by 2019-20.

Additionally, a comprehensive scheme to strengthen the intra-state transmission and distribution system in all North East states, including Sikkim, comprising of ~8,000ckms of transmission & distribution lines and 234 transmission & distribution substations has been approved by the Centre at an estimated cost of ~Rs100bn. PGCIL has been nominated to execute all schemes. The scheme will cover the entire North East and make the intra-state system strong to cater to demand for the next 10 years. It is planned to be commissioned progressively over the next three to four years.

2) **Green Energy Corridor**

Keeping up with the target of adding 100GW of solar power and 75GW of wind power by 2022, the power ministry has appointed PGCIL as the nodal agency to ensure the setting up of transmission infrastructure required to evacuate power. PGCIL is implementing the “Green Energy Corridors” to facilitate the integration of large scale renewable generation in the states of Gujarat, Rajasthan and Tamil Nadu into the ISTS grid along with other control infrastructure. These corridors comprise of establishment of 765/400kV pooling substations and 765kV d/c and 400kv d/c lines comprising intra-regional and its strengthening. In the second phase, work on the Green corridors will be extended to Maharashtra, Andhra Pradesh and Madhya Pradesh.

Hiving off POSOCO into a separate company – a step in the right direction

The Centre has decided to set up the Power System Operation Corporation (POSOCO) as an independent government company. In the process, the institutional framework for an independent, secure and reliable power system operation entity at the national level has been put in place as mandated under the Electricity Act 2003. POSOCO operates the National Load Despatch Centre (NLDC) and the Regional Load Despatch Centres (RLDCs), which are also responsible for operating the vibrant electricity market in the country. POSOCO is also designated as the nodal agency for major reforms in the power sector such as the Renewable Energy Certificate (REC) Mechanism, transmission pricing, short term open access in transmission, Deviation Settlement Mechanism, Power System Development Fund (PSDF) and so on.

Central government schemes for distribution sector

A) Deen Dayal Upadhyaya Gram Jyoti Yojana

The Deendayal Upadhyaya Gram Jyoti Yojana (DDUGJY) envisages feeder separation, strengthening of sub-transmission and distribution system, including metering of distribution transformers/feeders/consumers and rural electrification, with a scheme cost of Rs430bn during the entire implementation period.

B) Integrated Power Development Scheme

The Integrated Power Development Scheme (IPDS) has the objective of:

1) Strengthening of sub-transmission and distribution network in the urban areas

2) Metering of distribution transformers/feeders/consumers in the urban areas

3) IT enablement of distribution sector and strengthening of distribution network

The scheme will help in the reduction of AT&C losses, establishment of IT enabled energy accounting/auditing system, improvement in billed energy based on metered consumption and improvement in collection efficiency. The estimated cost of the present scheme with components of strengthening the sub-transmission and distribution networks, including metering of consumers in the urban areas, is Rs326bn.

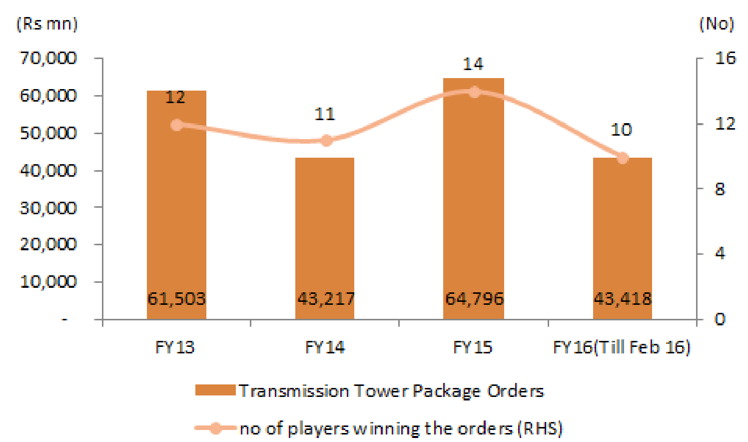
Market share of players in PGCIL orders from start of 12th plan

We analyse the composition and amount of orders from PGCIL since the beginning of the 12th plan period (FY13 onwards) only 12th plan period (FY13 onwards) only for transmission tower packages (EPC as well as only tower supply orders) and substations orders.

A) Transmission tower projects

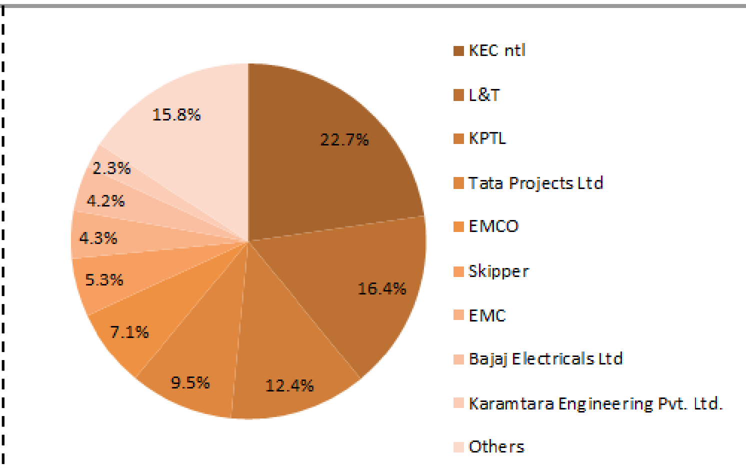
Since the beginning of 12th plan, PGCIL has placed orders worth Rs213bn out of the expected capex of Rs327bn of the 12th plan related to transmission tower packages and supply of towers. These orders exclude those for conductor, insulator and other civil parts.

Chart 6: Order inflows need to improve, competition declines



Source: Systematix Institutional Research

Chart 7: Top players by market share in 12th plan orders



Source: Systematix Institutional Research

The market for transmission tower EPC packages in the 12th plan is being dominated by top 9 players with the shares in descending order starting from KEC Intl, L&T, Kalpataru Power, Tata Projects, EMCO, Skipper (including JVs), EMC, Bajaj Electricals and Karamtara Engg. These top 9 players account for ~84.2% of the market. Among them, orders for Skipper and Karamtara are exclusively for supply of only transmission towers.

Chart 8: Market share movement of top players

	FY13	FY14	FY15	FY16(Till Feb 16)
Project orders				
Bajaj Electricals	3.7%	5.6%	6.4%	0.0%
EMCO	6.8%	14.3%	7.3%	0.0%
KPTL	11.9%	14.7%	11.8%	11.9%
KEC Intl	35.0%	20.0%	8.5%	29.2%
Tata Projects	0.0%	17.8%	19.2%	0.0%
EMC	0.0%	0.0%	4.1%	14.9%
L&T	15.7%	12.9%	17.7%	18.8%
Tower orders				
Skipper (incl JVs)	0.0%	1.0%	9.2%	11.4%
Karamtara	0.0%	0.0%	3.3%	6.2%

Source: PGCIL, Systematix

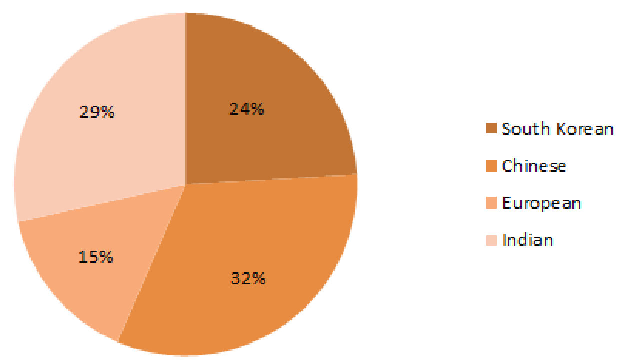
KEC International has been the most consistent player with leading market shares since the beginning of the 12th plan. L&T has also significantly ramped up the presence in the market, with consistently being the No. 2 player in the market. KPTL and Tata Projects continue to be the other two significant players in the market, especially in the 765kv market which is getting dominated by the top four players. Even though there have been more than 10 players every year winning orders from PGCIL, the composition of players year-on-year has been changing, indicating the emergence of non-serious ones in the market.

In tower supply orders, Skipper dominates the space being the largest player in the market. Order flows of only tower packages have been strong as Skipper and Karamtara both won significant orders since the beginning of FY15.

Substation EPC orders - dominated by Koreans & Chinese

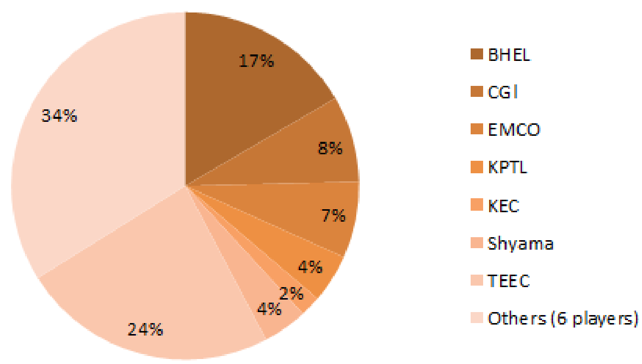
PGCIL has given out orders worth Rs131bn since the beginning of 12th plan in the substation EPC segment from voltage levels 220kV to 765kV. The total capex planned in the 12th plan for this segment is ~Rs243bn, which looking at the pipeline of orders from PGCIL certainly looks achievable. These orders exclude the supply of main components of a substation, namely transformers and switchgears, on which Rs567bn worth of capex has been planned in the 12th plan.

Chart 8: Substations - Korean & Chinese players dominate



Source: Systematix Institutional Research

Chart 9: TEEC leads among the Indian players



Source: Systematix Institutional Research

The market for substations has seen intense competition from the South Korean and Chinese players accounting for 24.1% and 32.4% market share respectively in the 12th plan orders. Hyosung Corp from South Korea is the single-largest player in the market with 24.1% share, while New Northeast Electric from China is the second-largest player with 17.3% market share. Both these players have been significantly importing from their home countries. With the domestic manufacturing clause by PGCIL coming into force, both these companies are setting up 765kV substation bay manufacturing facilities in India, indicating their long-term interest in India's transmission sector.

European players -- ABB, Siemens and Alstom T&D have strong competency in extra high voltage levels of 765kV and HVDC. As a group, European players account for only 15% of the market share in EPC business as their focus moved to Products Business in the past five years.

Indian players, almost 13 of them, have accounted for a combined market share of 28.5% in the EPC business in 12th plan orders. Techno Electric & Engineering (TEEC) dominates among the Indian players, especially in the extra high voltage levels of 765kV with a market share of 24% among Indian players. BHEL comes second on the ladder with 17% market share. TEEC is the only leading Indian player with strong capabilities in the EHV market to compete with international players.

TBCB – driver of orders in future

The Ministry of Power has initiated a scheme for development of Independent Transmission Projects (ITPs) through private sector participation for evacuation of power from the generating stations, transmission of power from pooling stations to other grid stations up to load centres and system strengthening in India under the tariff-based competitive bidding route of Electricity Act, 2003. For the development of ITPs, PFC Consulting Ltd (PFCCL) and REC Transmission Projects Company Ltd (RECTPL) have been appointed as the 'Bid Process Coordinator' by the Ministry of Power.

With a view to encourage participation of private sector in building the transmission capacity in India, the Centre had notified 14 power transmission schemes worth Rs339bn during 2014-15. Nine schemes worth Rs122.7bn were notified in July 2014 and further five transmission schemes worth Rs216.6bn were notified in February 2015. All these projects had been allocated to the Bid Process Coordinator (BPC) -- RECTPCL and PFCCL -- under the tariff-based competitive bidding (TBCB) route. The bid process is underway by both BPCs.

Progress in private sector participation in TBCB orders is expected to save the government's funds in the transmission sector and simultaneously provide the participants with fixed annuity return projects.

We list the two players -- Sterlite Technologies and PGCIL -- from private and public sector respectively for winning the largest number of orders in TBCB projects.

A) Sterlite Technologies

The company has a portfolio of eight projects in Build-Own-Operate-Maintain (BOOM) model of 6,000ckm transmission lines and three substations across 14 states. An estimated capital expenditure of US$1.5bn would be incurred on these projects. The company has fully commissioned two projects, while the remaining eight would be commissioned by FY20.

Table 9: Orders won under TBCB

	Project name	States covered	Technical details	Status	Cost of project (Rs mn)
1	Scheme for enabling import of NER/ER surplus by NR	Assam, Bihar & West Bengal	2 * 400 kV double circuit line of 450kms	Commissioned	1,187
2	Jabalpur Transmission	Chhattisgarh, Madhya Pradesh	1 * 765 kV single circuit 1 * 765 kV double circuit 610 kms line	Commissioned	1,400
3	Bhopal -Dhule	Madhya Pradesh, Maharashtra & Gujarat	4 * 765 kV single circuit 2 * 400 kV double circuit 2 sub stations, 990km line	Commissioned	2,000
4	Rajasthan Atomic Power	Rajasthan & Madhya Pradesh	1 * 400 kV double circuit 200kms line	Commissioned	400
5	Purulia & Kharagpur	West Bengal &Jharkhand	2 * 400 kV double circuit 270km line	Commissioning by May 16	600
6	NRSS 29	Punjab & Jammu & Kashmir	3 * 400 kV double circuit 1 substation, 440kms line	Commissioning by July 18	4,400
7	Maheshwaram project	Telangana	400 Kv double circuit transmission line 258kms line	Commissioning by June 18	550
8	Jharsugda to Raipur	Odhisa & Chattisgarh	765Kv double circuit Line 300kms line	Commissioning by FY19	1,400

Source: Systematix Institutional Research

B) Power Grid Corp

Powergrid Corporation (PGCIL) won the maximum number of 11 out of 20 TBCB projects awarded till Dec 2015, both in terms of number and value of projects. It has already commissioned 2 projects in the past one to two years. Contrary to the street's perception of PGCIL under cutting competitors with aggressive pricing, the PGCIL management is extremely optimistic on generating higher returns from TBCB, compared to traditional EPC business. With its vast experience in executing complex projects across different terrains, we believe PGCIL has become the most efficient player in the country, which will continue to boost its prospects in winning more TBCB orders.

Table 10: Prominent orders won under TBCB

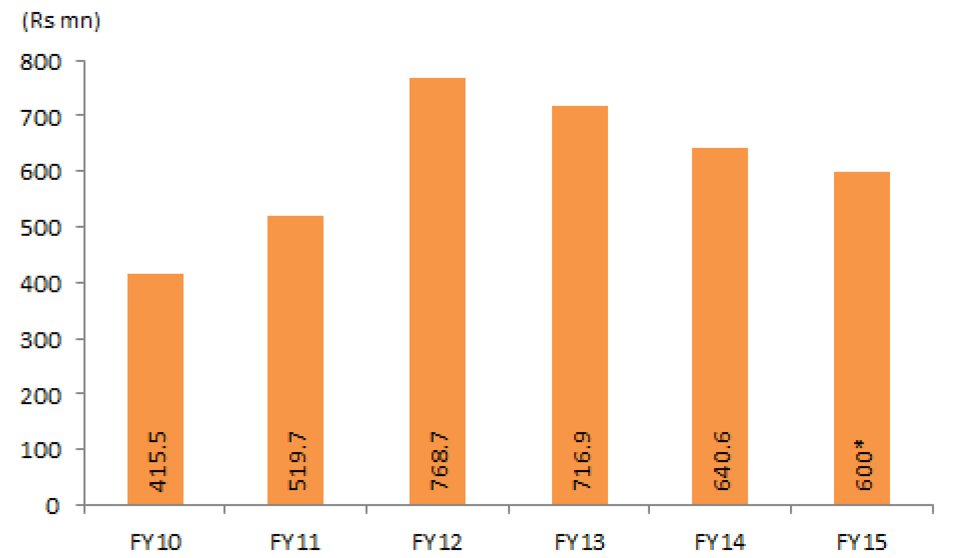
	Project name	States covered	Technical details	Status	Cost of project (Rs mn)
1	Nagarjunasagar	Telangana and Andhra Pradesh	400KV DC,150 km line	Commissioned	10,000
2	Vindhyachal-V	Madhya Pradesh	765 Kv DC ,382 km line	Commissioning in FY17-18	12,000
3	Gadarwara STPS (2X800 MW) of NTPC Part-A	Maharashtra, Madhya Pradesh	765KV D/C,250km line	Commissioning in FY17-18	10,250
			765KV S/C, 250 km line		
4	Gadarwara STPS (2X800 MW) of NTPC Part-B	Maharashtra, Madhya Pradesh	765KV D/C,468 km line	Commissioning in FY17-18	-
			1 AIS substation		
5	Vemagiri 2 transmission line	Andhra Pradesh	-	Commissioning in FY17-18	63,000

Source: Systematix Institutional Research

UDAY - potential game changer in the long term

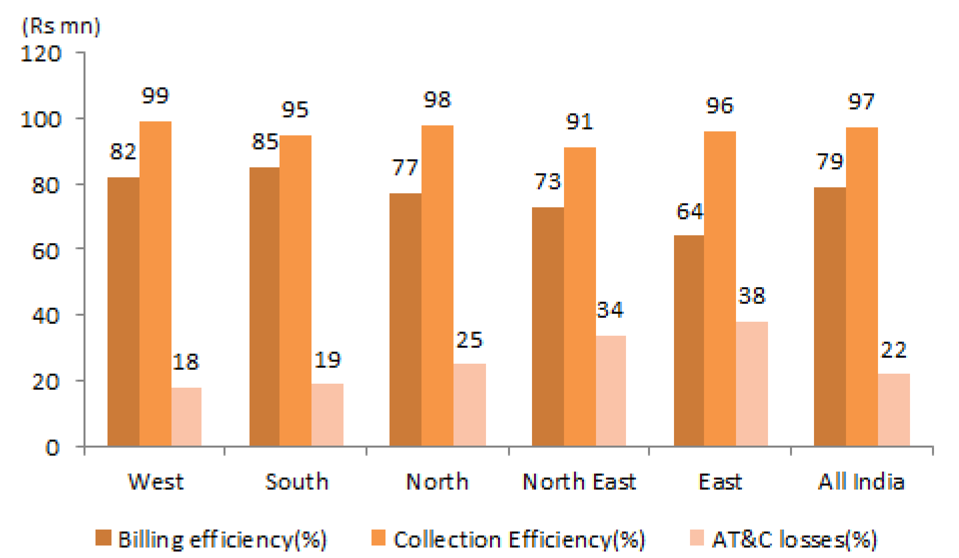
The weakest link in power value chain is distribution, wherein issues of under-reporting, theft and lack of collection efficiency have plagued the system for long. Discoms in the country have accumulated losses of ~Rs3.8tr and outstanding debt from the banking system of ~Rs4.3tr (as of March 2015), with interest rates up to 14-15%.

Chart 10: Combined losses for Discoms in the past 5 years



*Source: Audited State Accounts, *-projected accounts*

Chart 11: Lack of efficiency leads to distribution losses



Source: Systematix Institutional Research

Table 11: Top six states account for 60% of total debt of Discoms

States	Debt in Discoms (Rs bn)	AT&C losses (in %)
Rajasthan	850	27
Tamil Nadu	700	22
Haryana	345	22
UP	320	25
Madhya Pradesh	227	28
Andhra Pradesh	215	15

Source: Systematix Institutional Research

Under power minister Piyush Goyal, the ministry has launched a new scheme for revival of ailing discoms called Ujwal Discom Assurance Yojana (UDAY) in November 2015. UDAY focuses on transferring the debt of Discoms to states over two years followed by strict guidelines for following milestones on efficiency improvements. The scheme envisages turning all Discoms as profitable ventures by 2019 and reduction of AT&C losses to 15% by 2019.

Key features of UDAY

A) Financial parameters:

Debt of Discoms in the country are de facto borrowing of states, which is not counted in de jure borrowing. That means the debt is not considered in a state's FRBM limits but it remains as contingent liability on the state's balance sheet. Under the scheme, the states shall take over 75% of Discoms' debt outstanding as on Sept 30, 2015, 50% in FY16 and 25% in FY17. The outstanding principal of debt taken over will not be included in the fiscal deficit of states. However, interest has to be serviced within FRBM limits.

The respective states can then issue non-SLR bonds (SDL) with a maturity period of 10-15 years with a moratorium on principal up to five years, which could be of immense interest to the large domestic and foreign institutions. The government has proposed the idea of issuance of these bonds only after detailed discussions with all stake holders in the banking and financial services sector.

The 10-year bond will be priced at base rate plus 0.25% spread for non-SLR status on semi-annual compounding basis. Even though the yield is market-driven, there is a cap of 10 years. G-Sec + 50 + 25bps on these bonds, making them very attractive low cost issue from a state's point of view.

Currently, most discoms are paying interest rates of closer to 13-14%, which will be reduced to 9-9.5%, entailing a huge savings of 4-5% to the government. The banks will have to take a one-time hit on the loss of interest income but we believe it is a better alternative for banks than bearing the eventual default of Discoms' debt.

Residual Discoms' debt of 25% of the total to be converted into bonds to be offered in the market at a likely state bond rate +0.2%. If it is not converted into bonds, the banks can lend to Discoms at base rate + 0.1%.

In February 2016, Rajasthan issued Rs285bn bonds under UDAY meant for Discoms revival to 26 banks at an interest rate of 8.39%. The outstanding debt of Discoms as of Sept 30, 2015 stood at Rs805bn, of which 75% or Rs605bn would be taken over by the state, as envisaged in the scheme. This is lower than the 8.55% paid by the state to raise Rs10bn at the previous state government bond auction on Mar 8, 2015.

B) Operational parameters:

Under the scheme, financial restructuring will be followed by strict guidelines on achievement of operational parameters like reduction of AT&C losses, real-time monitoring of consumption patterns and reduction of theft.

Table 12: Monitoring of operational parameters

Activity	Benefit	End Date
Compulsory feeder and distribution transformers (DT) metering by states	Ability to track real time losses	Feeders- June 2016 DT- June 2017
Consumer indexing & GIS mapping of losses	Identification of loss making areas for corrective action	Sep 2018
Upgrade/change power transformers/meter	Reduce technical losses	Dec 2017
Smart metering	Reduction of theft	Dec 2019

Source: Ministry of Power

Additional benefits to states entering UDAY scheme

1) Financial incentives:

The states accepting the scheme and performing as per operational milestones will be given additional/priority funding through the Deen Dayal Yojana (DDUGJY), Integrated Power Development Scheme (IPDS), power priority funding through DDUGJY, IPDS, Power System Development Fund (PSDF) or other such schemes of MoP and MNRE.

2) Operational incentives:

The states will be supported through additional coal at notified prices in case the state shows higher capacity utilisation at its own power plants. The states will also be supplied power at lower cost from NTPC/other CPSUs.

Targeted outcome of UDAY scheme

1) Reduction of AT&C loss to 15% in 2018-19

2) Reduction in the gap between Average Revenue Realised (ARR) and Average Cost of Supply (ACS) to zero by 2018-19

3) Almost all Discoms to be profitable by 2017-18, 3-4 by 2018-19

Discoms financing in future – in case losses do not decline

Loss financing will only be as per the loss trajectory finalised by the ministry of power with Discoms and will be implemented only through Discoms' bonds backed by a state guarantee. For day-to-day operations, a working capital funding of 25% of Discoms previous year's revenue will be allowed.

Table 13: Structure of compensation in case of future losses

	FY16	FY17	FY18	FY19	FY20	FY21
Previous years DISCOM loss to be taken over by the state	0% of the loss of FY15	0% of the loss of FY16	5% of the loss of FY17	10% of the loss of FY18	25% of the loss of FY19	50% of the loss of FY20

Source: Ministry of Power, Systematix Institutional Research

Demand side management – bringing efficiency by use of higher rated products

Under the UDAY scheme, the focus is also on improving efficiency in existing load centres by implementation of various energy saving measures like LED bulbs, energy rated consumer durables, efficient pumps & motors in the agriculture and industrial sectors ,translating into potential savings of Rs650bn in the next five years.

Long-term impact on the Discoms – strengthening the balance sheet

The scheme has got encouraging response from states, with as many as 15 signing the preliminary MoU with the central government. The states which agreed to join the scheme are Andhra Pradesh, Rajasthan, Jharkhand, Madhya Pradesh, Uttarakhand, Himachal Pradesh, Punjab, Jammu & Kashmir, Haryana, Gujarat, Chhattisgarh, Uttar Pradesh, Bihar, Odisha and Maharashtra. All these states combined account for ~90% of Discoms' losses as of March 2015. There are 12 states and union territories in India which do not have a separate Discom and are still operating under the combined generation, transmission and distribution SEB structure. Identification of a Discom's loss under such a structure is difficult and the central government is working with these states to sort out the issue.

Likely winners and losers?

UDAY scheme assures the rise of vibrant and efficient Discoms through a permanent resolution of past and potential future issues of the sector. It empowers Discoms with the opportunity to break even in the next two to three years We believe post the break-even, the Discoms will have stronger balance sheets to take on next round of expansion of network which will coincide with development on multiple smart cities in India, creating new demand centers. Banking sector is likely to lose out on the interest income in the short term but we believe the implementation of this scheme will be good for the banking sector in the long term which would have otherwise suffered from NPAs in the Discom sector. On overall basis, the government is expecting savings of Rs1.8tr through financial structuring and operational efficiencies.

We believe the demand for new transmission network will arise from these new demand centres and potential order flow will start flowing from FY18 onwards. SEBs with lighter balance sheets by FY18 will be in a position to undertake the next wave of capex in the T&D sector.

World investment outlook on power transmission

Power transmission network is seeing rapid expansion across the developing and developed countries in order to connect renewable energy sources as well as modernizing/refurbishing of older networks. According to the 'World Energy Investment Outlook, 2015' the investment on the transmission & distribution sector during 2014-30, will be to the tune of US$6.8trillion. Asia, Latin America, and Africa are expected to be the drivers of this capex momentum as these countries will incrementally gain on per capita consumption, building inter-state grids, and electrifying their villages.

Table 14: Investment in T&D infrastructure by regions in the new policies scenario, 2014-2035

	Transmission				Distribution				
	Additions		Refurbishment	Total	Additions		Refurbishment	Total	Total T&D
(in $bn)	**New Demand**	**Renewables**			**New Demand**	**Renewables**			
OECD									
A) Americas	127	26	171	324	245	18	433	696	1,020
-USA	98	19	138	255	183	16	365	564	819
b) Europe	26	37	94	157	157	23	409	589	746
c) Asia Ocenia	15	9	40	64	119	11	219	349	413
- Japan	4	5	25	34	44	10	146	200	234
TOTAL OECD	**168**	**72**	**305**	**545**	**521**	**52**	**1,061**	**1,634**	**2,179**
Non - OECD									
d) Eastn Europe	50	3	73	126	124	1	176	301	427
- Russia	32	1	48	81	59	-	62	121	202
e) Asia	567	69	156	792	1,602	32	701	2,335	3,127
- China	392	49	107	548	746	20	403	1,169	1,717
- India	**78**	**14**	**28**	**120**	**333**	**9**	**208**	**550**	**670**
- South East Asia	73	2	13	88	394	1	61	456	544
Middle East	38	7	16	61	129	2	34	165	226
Africa	110	5	20	135	238	2	46	286	421
Latin America	89	7	31	127	214	2	92	308	435
- Brazil	63	6	20	89	136	2	48	186	275
Total Non - OCED	**854**	**91**	**296**	**1,241**	**2,307**	**39**	**1,049**	**3,395**	**4,636**
WORLD	**1,022**	**163**	**601**	**1,786**	**2,828**	**91**	**2,110**	**5,029**	**6,815**

Source: World Energy Investment Outlook, 2015, Systematix Institutional Research

COMPANIES SECTION

Kalpataru Power Transmission

1 April, 2016

Order inflow momentum to drive growth

INITIATING COVERAGE

Sector: Power T&D	**Rating: Buy**
CMP: Rs205	**Target price: Rs281**

Stock Info

Sensex/Nifty	25,342/ 7,738
Bloomberg	KPP IN
Equity shares (mn)	153.5
52-wk High/Low	Rs292/ 160
Face value	Rs2
M-Cap	Rs 32.2bn/ $480mn
3-m Avg volume	$0.4mn

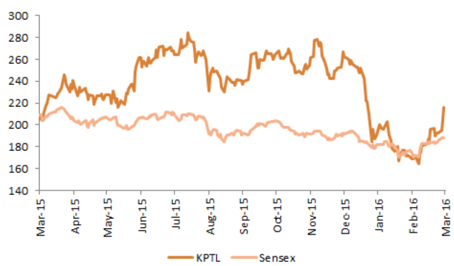
Financial Snapshot (Rs mn)

Y/E March	FY16e	FY17e	FY18e
Sales (Rs mn)	44,628	52,368	61,105
Net Profit (Rs mn)	1,769	2,256	2,790
EPS (Rs)	11.9	15.0	18.5
Growth (%)	9.8	26.8	23.2
PE (x)	17.3	13.6	11.1
EV/EBIDTA (x)	8.5	7.1	6.0
P/B (x)	1.4	1.3	1.2
RoE(%)	8.5	9.9	11.1
RoCE (%)	9.7	11.1	12.4
Dividend Yield (%)	0.1	0.1	0.1
Net Gearing (x)	0.3	0.2	0.1

Shareholding pattern (%)

	Dec '15	Sep '15	June '15
Promoter	59.4	59.3	59.3
–Pledged	26.9	18.8	20.7
FII	3.9	9.2	9.7
DII	23.1	21.9	21.3
Others	13.6	9.6	9.7

Stock Performance (1-year)



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Kalpataru Power Transmission Ltd (KPTL), with a presence across transmission, railways and construction segments, is likely to benefit from the ordering pickup on capex by railways, SEBs and few private players from power transmission side. The company has seen order inflows of ~Rs70bn (till Mar 23, 2016), which is more than the order inflows for FY14 and FY15 combined. We expect KPTL's order inflow to post a CAGR of 49% during FY15-18e, providing revenue visibility of >1.5x throughout the period. While JMC reported strong order flows, its road BOT projects continue to make operational losses. We are more positive on the standalone businesses of KPTL and JMC and cautious on the asset-heavy non-performing business of road BOT. We intiate coverage on KPTL with a Buy rating, based on SOTP valuation of Rs281, an upside of 37%.

Domestic ordering bounces back

The opening order backlog of Rs43.5bn in T&D segment has slowed down execution growth to negative zone during 9MFY16. Ironically, order inflows have been at ~Rs70bn YTD basis (Mar 23, 2016), taking the overall backlog to >Rs80bn, and providing >1.7x years of revenue visibility. Stronger opening order backlog for FY17 is expected to result in net revenue growth of 16% and 18% in FY17e and FY18e respectively. Order inflows have been mainly from SEBs and private sector, topping it by Rs7.8bn worth EPC order from its own BOT win (Bhutan). International orders have been well diversified across Africa, the Middle East, Saarc countries and few CIS countries, accounting for 40% of the backlog as of 9MFY16. KPTL is witnessing strong traction in Africa (present in at least eight countries), while the Middle East is still strong but is likely to witness a correction due to curtailment of government budgets. We expect KPTL to maintain margins of >10% in transmission orders, aided by low commodity prices and lesser competition at EHV level orders.

Infra EPC business turns around - strong order booking in JMC as well

Completion of legacy orders and improved execution have turned the infra EPC segment EBIT positive (9MFY16 margin of 2.3%) from heavy losses in the past three years. Order backlog is up ~30% to Rs11bn at 9MFY16-end as the company won multiple orders across Railways and pipelines segment. We expect the momentum in Railways orders to continue as KPTL is likely to benefit from ~Rs5tr of capex planned by the ministry of railways during FY15-20. We estimate infra segment to post 41% CAGR during FY15-18e and EBIT margin to trend towards 5% by FY18e. KPTL's subsidiary, JMC Projects has bagged orders worth Rs25bn in 9MFY16, taking its order backlog over Rs62bn and dominated by government buildings and infra projects.

Road BOOT still in losses, Transco BOOT performs in line

Toll collection in BOOT assets is still falling short by Rs8-9lakh/day from cash breakeven, needing equity funding of at least Rs600mn over the next one year. Transco BOOT, Satpura, will be operational by May 2016. Recently, KPTL won its third BOOT project worth Rs12bn, having in-built EPC of Rs7.8bn. KPTL is actively looking to monetise all the BOOT assets to strengthen the balance sheet. Under the Thane project, KPTL has sold off 30% inventory and 60% has been leased out. Indore project was launched for sale in Mar 2016, after initiating the construction work.

Valuation and view

We value the company on SOTP basis – KPTL standalone at a PE of 12x FY18e, Transco BOT at P/BV of 1.5x, real estate projects P/BV of 0.6x for Indore and 1x for Thane, JMC standalone at PE of 6x FY18e and road BOT at P/BV of 0.5x, arriving at a target price of Rs281, an upside of 34% from CMP of Rs205.

FINANCIALS (STANDALONE)

Profit & Loss Statement

YE: Mar (Rs mn)	FY14	FY15	FY16e	FY17e	FY18e
Net Revenues	40,552	44,223	44,628	52,368	61,105
% growth	21.6%	9.1%	0.9%	17.3%	16.7%
- Op. Expenses	36,690	39,955	39,987	46,843	54,536
EBITDA	3,863	4,268	4,641	5,525	6,569
EBIDTA Margin (%)	9.5	9.7	10.4	10.6	10.8
- Interest Expenses	1,460	1,409	1,494	1,593	1,782
- Depreciation	695	852	911	958	1,003
+Other Income	484	522	519	519	519
- Tax	727	873	937	1,188	1,463
Effective Tax Rate (%)	33%	35%	34%	34%	34%
PAT	1,464	1,656	1,819	2,305	2,840
+/- Extraordinary Items	73.9	(38.7)	-	-	-
+/- Minority Interest	-	-	(49.4)	(49.4)	(49.4)
Reported PAT	1,538	1,618	1,769	2,256	2,790
Adj. FDEPS (Rs/Share)	9.5	10.8	11.9	15.0	18.5
Adj. FDEPS growth (%)	6.3	13.1	9.8	26.8	23.2

Source: Company, Systematix Institutional Research

Balance Sheet

YE: Mar (Rs mn)	FY14	FY15	FY16e	FY17e	FY18e
Share Capital	307	307	307	307	307
Reserves & Surplus	19,235	20,401	21,947	23,980	26,548
Net Worth	19,542	20,708	22,254	24,287	26,855
Minority Interest	`	-	-	-	-
Total Debt	7,850	9,714	10,245	10,882	12,106
Other liabilities	1,040	1,046	1,046	1,046	1,046
Capital Employed	28,432	31,467	33,545	36,216	40,006
Net Fixed Assets	5,918	5,590	5,179	4,721	4,218
other assets	6,050	6,426	6,426	6,426	6,426
investments	3,834	3,935	3,935	3,935	3,935
Net Working Capital	11,983	14,763	15,534	13,919	16,058
Cash and Bank Balance	647	753	2,471	7,214	9,369
Capital Deployed	28,432	31,466	33,545	36,216	40,006
Net Debt	7,201	8,956	7,770	3,664	2,733
WC Days	108	122	127	97	96
Book Value (Rs/sh)	127.3	134.9	145.0	158.3	175.0

Source: Company, Systematix Institutional Research

Cash Flow

YE: Mar (Rs mn)	FY14	FY15	FY16e	FY17e	FY18e
PAT	1,538	1,618	1,769	2,256	2,790
+ Non Cash Items	695	852	911	958	1,003
Cash Profit	2,233	2,469	2,680	3,214	3,793
- Incr/(Decr) in WC	(2,082)	(2,780)	(771)	1,615	(2,139)
Operating Cash Flow	151	(311)	1,909	4,829	1,654
- Capex	(1,227)	(523)	(500)	(500)	(500)
Free Cash Flow	(1,076)	(834)	1,409	4,329	1,154
- Dividend	264	272	272	272	272
+ Equity Raised	(196)	(179)	49	49	49
+ Debt Raised	1,939	1,864	531	637	1,223
- Investments	(572)	(477)	-	-	-
+ other CL	246	6	-	-	-
Net Cash Flow	78	107	1,718	4,743	2,154
+ Opening Cash	569	647	753	2,471	7,214
Closing Cash	647	753	2,471	7,214	9,369

Source: Company, Systematix Institutional Research

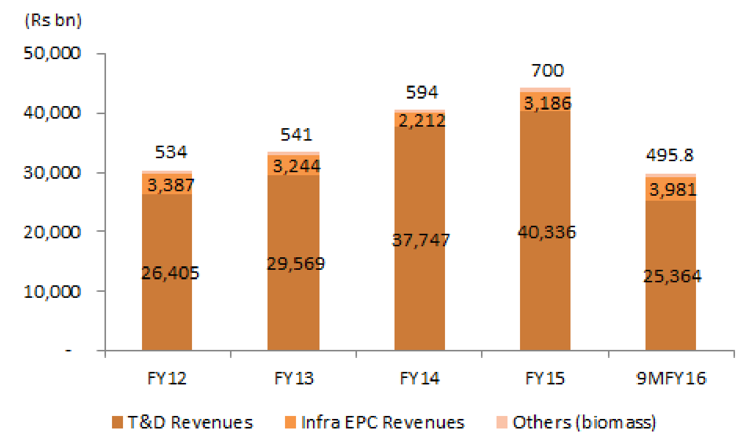
Ratios

YE: Mar	FY14	FY15	FY16e	FY17e	FY18e
P/E(x)	21.5	19.0	17.3	13.6	11.1
P/CEPS(x)	14.6	12.5	11.5	9.6	8.2
Mcap/Sales	0.8	0.7	0.7	0.6	0.5
EV/EBIDTA(x)	10.2	9.2	8.5	7.1	6.0
RoE(%)	7.7	8.2	8.5	9.9	11.1
RoCE(%)	10.1	9.7	9.7	11.1	12.4
Fixed Asset Turnover (x)	6.9	7.9	8.6	11.1	14.5
Dividend Yield (%)	1.6	0.7	0.7	0.7	0.7
Dividend Payout (%)	18.0	16.4	15.0	11.8	9.6
Debt/Equity(x)	0.4	0.5	0.5	0.4	0.5
Debtors (days)	152.3	153.6	155.0	150.0	150.0
Revenue Growth (%)	21.6	9.1	0.9	17.3	16.7
PAT Growth (%)	6.3	13.1	9.8	26.8	23.2
EBIDTA Growth (%)	19.9	10.5	8.8	19.0	18.9
EPS Growth (%)	6.3	13.1	9.8	26.8	23.2

Source: Company, Systematix Institutional Research

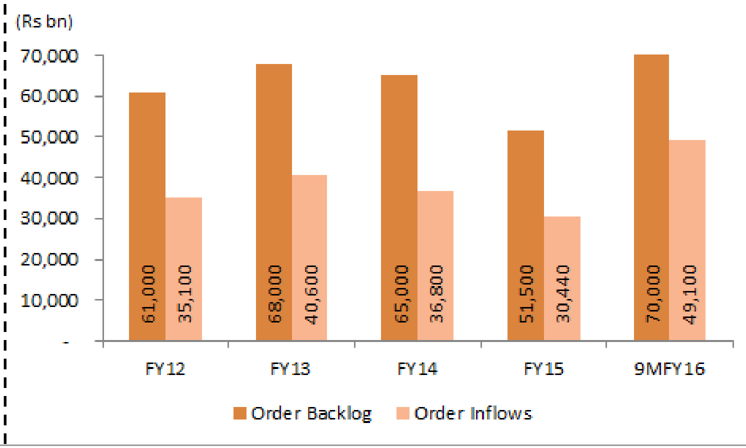
Charting the story

Chart 1: Revenue growth moderate on lower order book



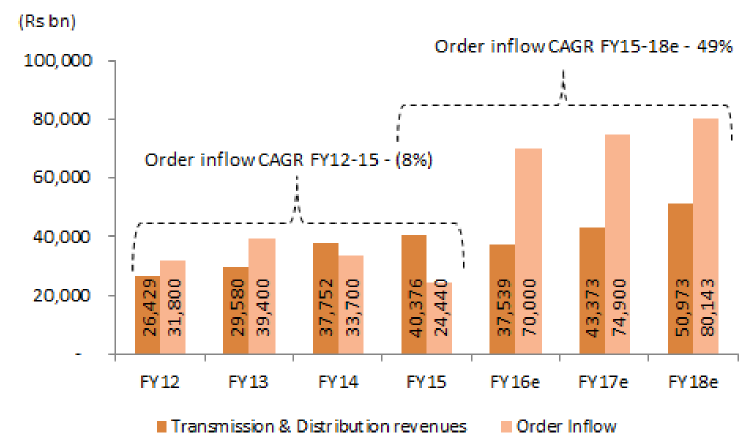
Source: Company, Systematix Institutional Research

Chart 2: Order booking stagnant during FY12-15



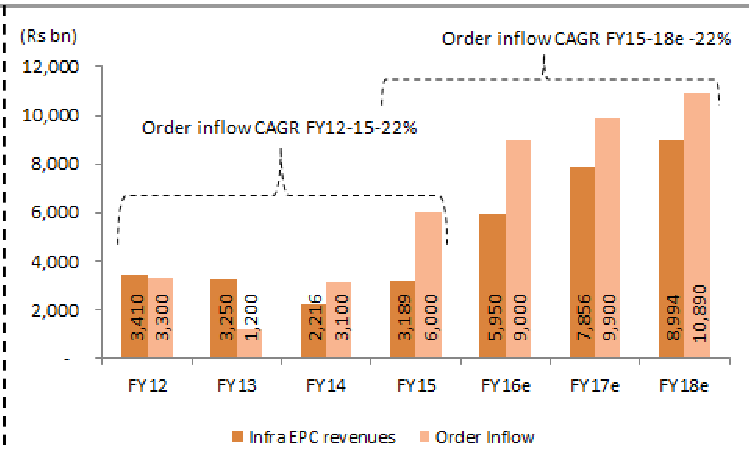
Source: Company, Systematix Institutional Research

Chart 3: T&D order inflow expected at 49% CAGR during FY15-18e



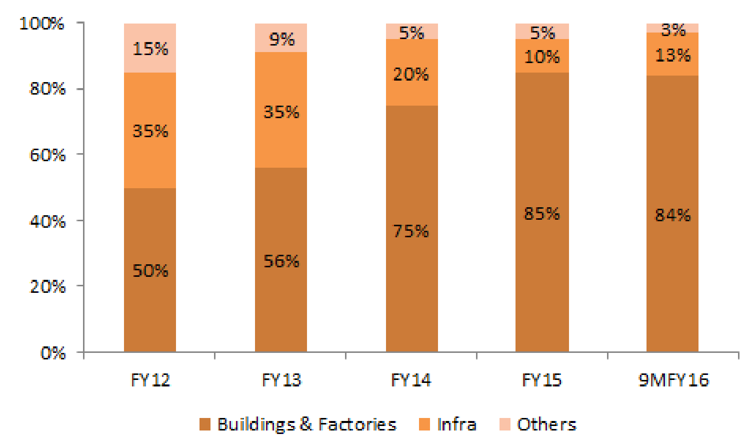
Source: Company, Systematix Institutional Research

Chart 4: Execution improves in infra EPC, order outlook positive



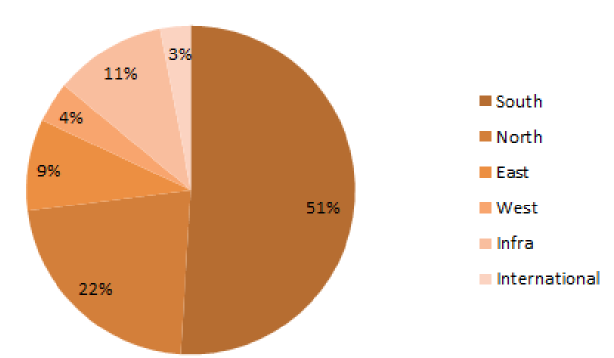
Source: Company, Systematix Institutional Research

Chart 5: Increasing proportion of B&F in JMC's order book



Source: Company, Systematix Institutional Research

Chart 6: Southern region remain dominant in JMC's portfolio



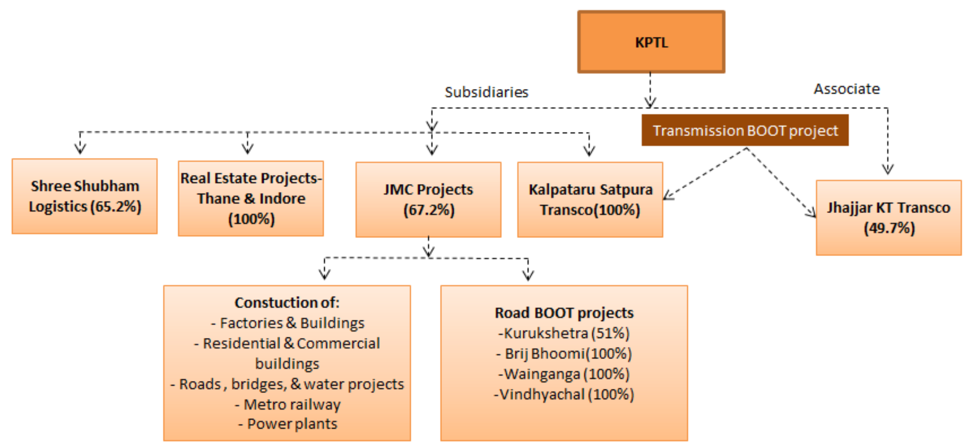
Source: Company, Systematix Institutional Research

Company background

Kalpataru Power Transmission Ltd (KPTL) is the flagship company of the Kalpataru group, with a presence in the setting up of transmission lines, EPC of infrastructure segments like oil/gas pipelines & railways and biomass energy (owns two small power plants). The company has tower manufacturing plants with a capacity of 180,00tpa located at Gujarat and Chattisgarh, with pre-qualifications up to 765kV for supply to all leading utilities and testing facilities up to 1200kV. Under the transmission segment, KPTL owns two BOOT projects -- an operational asset at Jhajjar and an under-construction asset at Satpura. Recently, the company won its third BOOT asset to connect the hydro power station located near Bhutan.

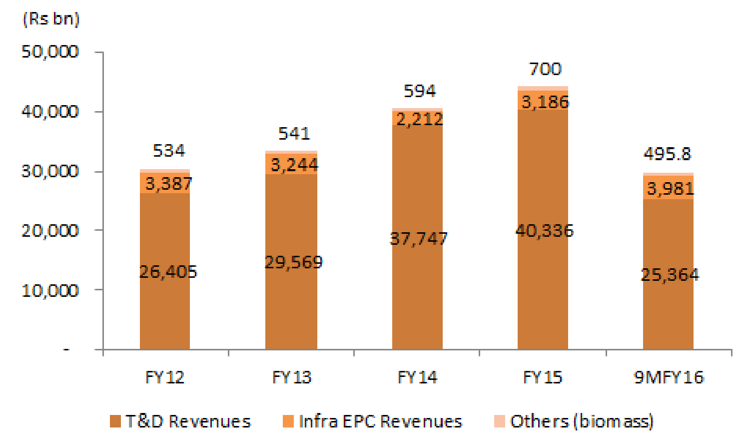
KPTL holds a 67% stake in JMC Projects (JMC); JMC is primarily engaged in the construction of industrial buildings, government buildings, residential and commercial complexes. Recently, JMC ventured into the infrastructure segment, with projects in roads and bridges. Under JMC, KPTL owns four toll collecting BOT assets -- three are already operational and the fourth is pending final COD.

Chart 7: Organisation setup



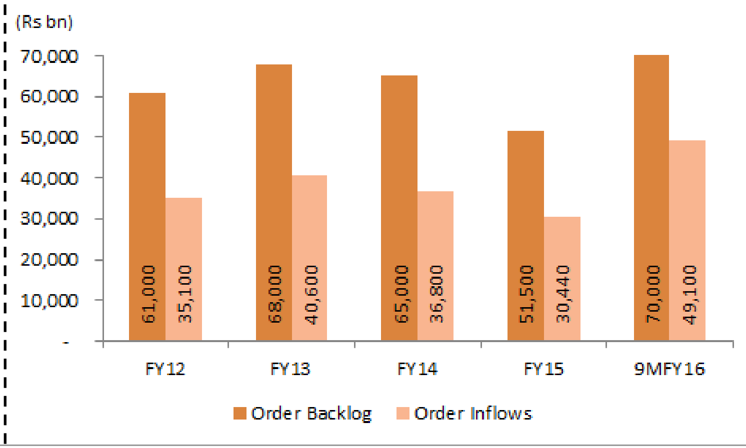
Source: Company, Systematix Institutional Research

Chart 8: Revenue growth moderate on lower order book



Source: Company, Systematix Institutional Research

Chart 9: Order booking stagnant during FY12-15



Source: Company, Systematix Institutional Research

A slowdown in the economy during the last five years affected KPTL's order booking as order inflows posted a CAGR of negative 4.6% during FY12-15. Net sales also got impacted as the sales growth came in at 13.4% CAGR during FY12-15 owing mainly to smaller base in FY12. EBITDA margin was under pressure as high competition, delays in execution and cost overruns, especially on the infra EPC side, kept margins below 10% (company's threshold for margins).

The opening order book in FY16 was only at Rs 51.5bn and the company's revenue actually de-grew 11% yoy on a 9M basis. The low commodity prices were not the main factor which led to a revenue decline during this period.

On the order booking front, 9MFY16 has been a different scenario as KPTL booked orders worth Rs 49bn during the period. Between Jan 1, 2016 to Mar 23, 2016, the company booked incremental orders worth Rs 26bn. Order booking has been driven by renewed ordering from certain SEBs, private operators, PGCIL and BOT related orders. The order flow also includes those from railways and pipeline segment; in fact the management is expecting a tendering pipeline of Rs25bn just in railways segment to be finalised in the next three to six months.

T&D Division – domestic ordering recovers, aided by SEBs and own BOT projects

Going international

As orders dried up in the domestic market in FY10-11, KPTL aggressively focused on the international markets for transmission projects. Now, the company is present across 40 countries, with a dominant share of orders from North Africa, CIS, Middle East and few East European countries. KPTL is benefiting from the planned capex of US$ 135bn and US$61bn to be incurred during 2014-30 in Africa and Middle East respectively (source: World Energy Investment Outlook, 2014). Funding for these orders are pre-arranged through large international financing institutions and multilateral agencies, thus virtually eliminating the risk of defaults or payment delays. The company has not faced any cancellation/delay in existing transmission projects in the Middle East, which is reeling under the impact of low crude oil prices. The management is confident that priority infra projects like power transmission would not witness budget cuts, unlike commercial real estate/hospitality projects.

Order book composition

With KPTL's concerted effort to garner international orders, the order book composition was 55% international and 45% domestic at FY15-end. Africa constituted the highest with 20% share, while the Middle East accounted for 15% of the total order backlog.

Few of the recent order wins in international markets are:

International:

- A turnkey transmission line project in Nepal worth ~Rs2.4bn from the Nepal Electricity Authority
- A turnkey transmission line project of ~Rs730mn in Abu Dhabi
- Construction of 380kV overhead transmission lines in Saudi Arabia worth ~Rs1.5bn. The project is implemented by Kalpataru IBN Omairah Idle Company Ltd, a joint venture between IBN Omairah Contracting Company and KPTL, where KPTL owns 65% equity stake

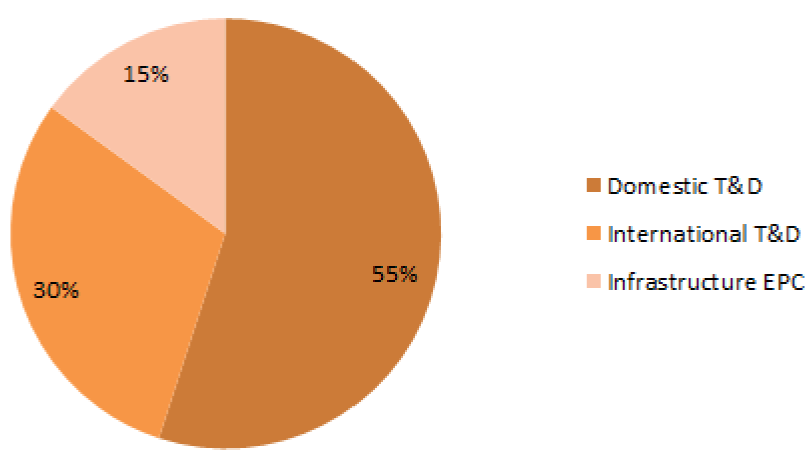
Impact of fixed priced contracts on margins

Of the current backlog of international orders, almost 30% are fixed priced in nature. As a practice, the company immediately gets into back-to-back forward contracts on the raw material front by booking commodities on various exchanges. Both aluminium and zinc can be hedged completely but the steel portion cannot be hedged perfectly. In the current scenario of low commodity prices, KPTL is likely to benefit on the margins front.

Order inflow in 9MFY16 – composition again changes towards domestic

Since the beginning of FY16, the Indian transmission market has been on a roll with PGCIL and SEBs spending close to Rs45-50bn each on transmission lines, well supported by private sector operators. Moreover, the EPC orders emanating from the recently-awarded BOOT projects to private operators have come in thick and fast in the current year.

Chart 10: Order inflows YTD Mar 23, 2016 - Rs75bn

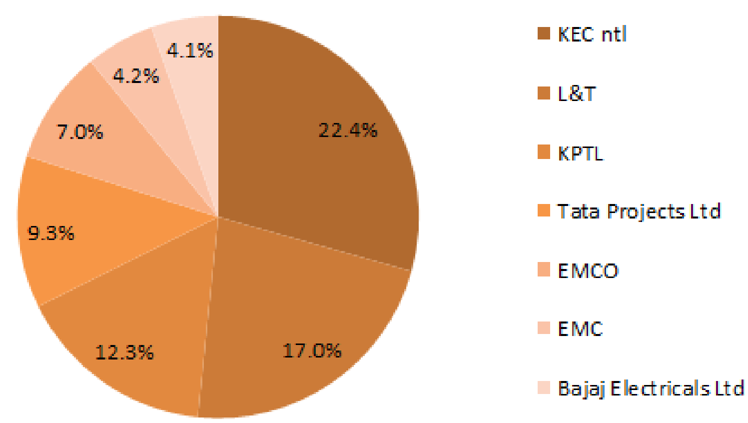


Source: Company, Systematix Institutional Research

Recent domestic order wins

- Establishment of transmission system strengthening for transfer of power from new hydro-electric power projects in Bhutan to India. The 400kV transmission line project to be constructed in West Bengal and Bihar worth ~Rs8.64bn has been awarded to the company's 100% subsidiary, Alipurduar Transmission Ltd. This is the third BOOM project to be executed by KPTL.
- A turnkey transmission line project of 765kV D/C Vemagiri-Chilakaluripeta of ~Rs7.8bn from Powergrid Southern Interconnector Transmission System Ltd (a wholly-owned subsidiary of PGCIL).
- Transmission line supply projects for Gadarwara-Warora transmission line project of ~Rs3,530mn from Powergrid Warora Transmission Ltd (a wholly-owned subsidiary of PGCIL).
- Transmission line supply project for an ultra mega solar park transmission system in Andhra Pradesh of ~Rs770mn from PGCIL.
- A substation project of ~Rs440mn from PGCIL.
- A transmission tower supply project worth ~Rs470mn from Power Grid Warora Transmission Ltd (a wholly-owned subsidiary of PGCIL).

Chart 11: Domestic market share – 12th plan orders

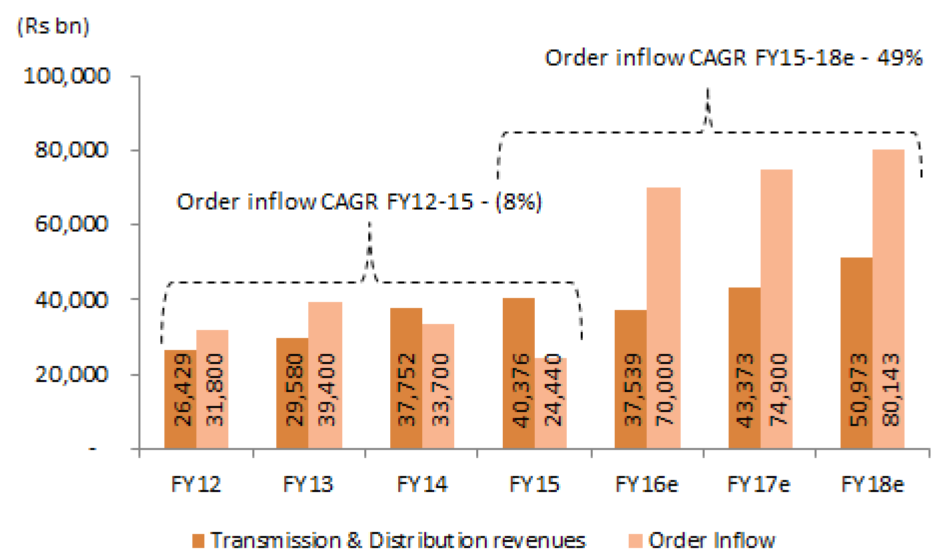


Source: Company, Systematix Institutional Research

We note for the 12th plan orders -- the period starting from April 2013 till date -- PGCIL has placed transmission line orders worth Rs215bn. According to our analysis, KPTL ranks third in terms of share of PGCIL orders after KEC International and L&T. As discussed in the sector report, the entry barriers at EHV level projects and strict working capital conditions by PGCIL has resulted in top four players accounting for >60% share of the orders. Lesser competition at the top end will ensure decent margins for all four players.

KPTL has made up for the lesser share in PGCIL orders by garnering its third BOOT project, which has an inbuilt EPC order worth Rs7.8bn.

Chart 12: T&D order inflow expected at 49% CAGR during FY15-18e



Source: Company, Systematix Institutional Research

We estimate the strong order flows in FY16 will result in robust revenue growth and EBITDA margin of >10% for the company's T&D segment. We expect the segment to post a CAGR of 8% over FY15-18e(CAGR of 17% over FY16-18e), while the growth in order booking is expected to be at 49% CAGR during the same period versus negative 8% CAGR in order inflows during FY12-15.

BOOT projects

1) Jhajjar KT Transco Pvt Ltd (Jhajjar KT)

Jhajjar KT is a joint venture with Techno Electric Engg Ltd, with KPTL holding 49.72% stake. The SPV operates with the objective of exclusive right and authority to construct, operate, maintain and transfer the 400kV/200kV transmission lines and substations (transmission system) in Haryana on design, build, finance, operate and transfer (DBFOT) basis and provide transmission services for a period of 25 years, with an option to extend the period for further 10 years mutually agreed, for which a transmission license has been granted by the Haryana Electricity Regulatory Commission (HERC) for transmission of electricity from the 2x660MW thermal power plant at Jhajjar.

2) Kalpataru Satpura Transco

The company won the project from the Madhya Pradesh State Electricity Board to build, own, operate and transfer 240kms, 400kV double circuit power transmission line between Satpura to Ashta, under the viability gap funding for a concession period of 25 years and a construction period of 15 months, with an optional extension of 10 years on annuity basis.

3) Alipurduar Transmission (WB-Bihar-Bhutan)

KPTL won its third BOOT project for evacuation of power from Bhutan to West Bengal and Bihar. The order's execution period is of three years and other T&C are yet to be finalised. We are not considering this project for valuation purpose as the terms and conditions of financial closure are yet to be finalised.

Table 1: Details of BOOT projects

(Rs mn)	Jhajjar KT Transco	Kalpataru Satpura Transco
Equity Investment	458	1,074
Debt	1,408	2,142
Total Cost for KPTL	1,866	3,215
Operational Since	Mar-12	Apr-15
Annual Revenue	540	380

Source: Company, Systematix Institutional Research

Infrastructure EPC Segment: Execution momentum improves

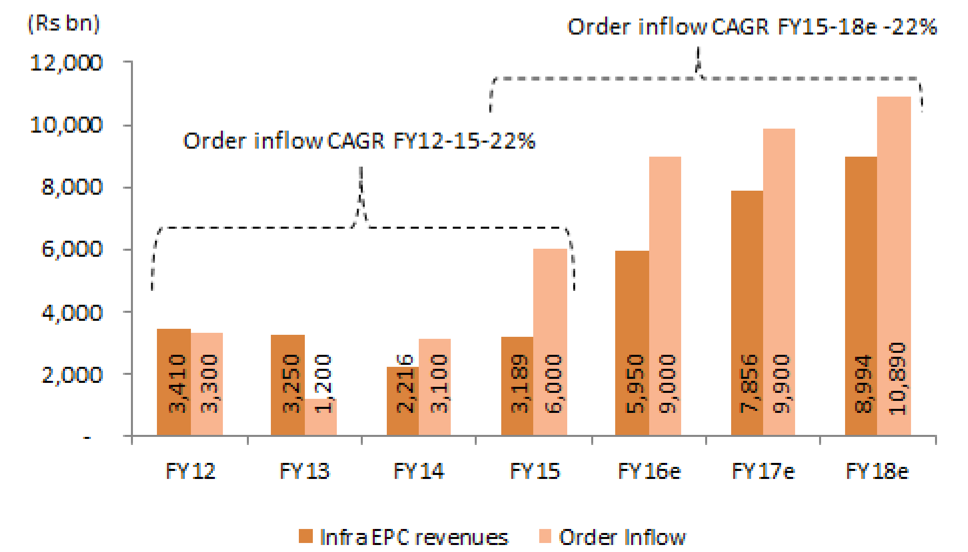
Under this segment, the company undertakes work for laying of cross country oil & gas pipelines and laying and electrification of railway tracks along with other civil works related to railways. The segment was reeling under losses due to delays in execution, escalation of costs and under utilisation of facilities.

With the new government targeting a capex of Rs5tr on modernisation, electrification and expansion of existing railway tracks, the sector presents huge opportunities for the company. Traction is already seen in the order backlog -- ~Rs12bn as of Feb 23, 2016 versus Rs6.5bn at FY14-end.

In the initial years, under the railway vertical, KPTL accepted various small-sized low margin projects just to get pre-qualifications and execution experience in various categories. Now, fully equipped with pre-qualifications, the company is looking to focus on orders above Rs2bn only with healthy margins. The order flow momentum is likely to be maintained at a CAGR of 22% for FY15-18e, similar to FY12-15 CAGR of 22%.

We expect better traction on the execution front as many stuck projects are moving now. Also, as the government has taken Railways' expansion and modernisation as a priority, we expect issues like ROW, delays in planning and other clearances to get solved. We estimate infrastructure EPC vertical to post a CAGR of 41% over FY15-18e, with EBIT margin trending towards 5% in the same period.

Chart 13: Execution improves, order outlook positive



Source: Company, Systematix Institutional Research

Real estate projects – Slow progress

KPTL is developing a commercial realty project in Thane (0.32mn sqft) and a residential project in Indore (0.42mn sqft) on company-owned land. It has invested close to Rs3.5bn in both the projects combined. Kalpataru Prime, the commercial project in Thane has been 30% sold and 60% leased as of now. The company aims to monetise the entire project going forward at the right opportunity. The lease rental per sqft on an average has been Rs48/sqft/month. Through the sale of 30% of the property, KPTL has received a cash inflow of Rs600mn. As on date, the total loans and advances to this project from the parent company are Rs1.8bn.

Indore project's construction work has been initiated at the plinth level. The project has been officially launched in March 2015. The project is a mix of residential and commercial use, with a total developable area of 0.42mn sqft

Table 2: Details of real estate venture

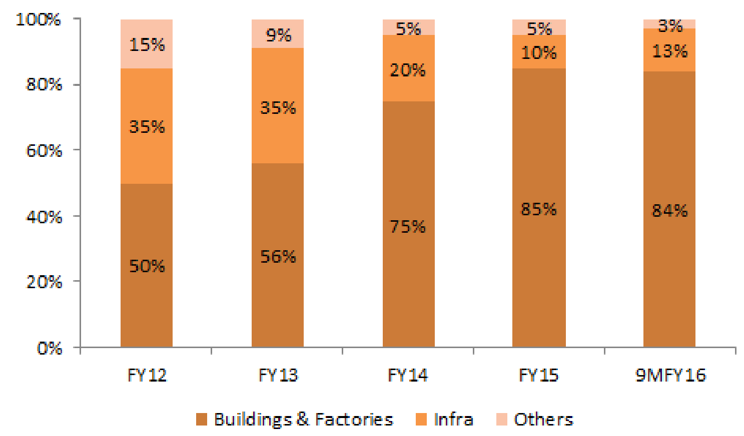
	Amber RE (Thane)	**Indore**
(Area in sqft)	0.32mn	0.42mn
Development Usage	Commercial	Residential and Commercial
Stage of development	Completed	Plinth work initiated
Commercial Status	30% sold,60% leased	Just launched. No sales reported yet
Equity Funding from KPTL (Rs mn)	1,936	1,989

Source: Company, Systematix Institutional Research

JMC Projects – Ordering picks up, margins set to improve

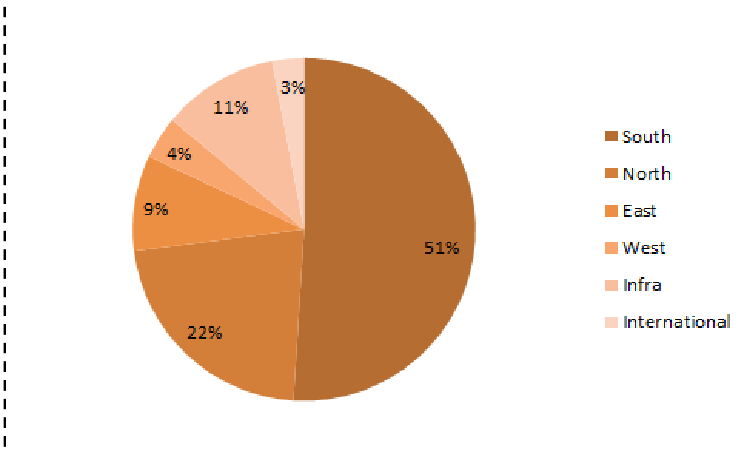
Through its 67.2% subsidiary, JMC Projects, KPTL is present in the construction of highways, bridges, flyovers, townships, tall buildings, hospitals, industrial units, power plants and so on. Of late, JMC has started expanding vistas by taking orders from international counterparts. With a strong workforce of 2,800+ professionals supported with technology and an inspiring work environment, the company's capabilities span the entire gamut of construction -- civil & structural, mechanical, electrical and fire-fighting engineering among others for all major industries and project types.

Chart 14: Increasing proportion of B&F in order book



Source: Company, Systematix Institutional Research

Chart 15: Southern region remain dominant in JMC's portfolio



Source: Company, Systematix Institutional Research

Over the last five years, JMC has built significant capabilities in buildings & factories segment, which comprises construction of commercial complexes, institutional buildings, IT parks, hospitals, R&D complexes, hotels, hostels and housing & residential buildings. The company avoids exposure to residential building complexes due to the current real estate market scenario -- has only Rs3bn from the residential segment as of now. JMC is also present in infra sector like construction of roads, bridges, metro railways and water in both domestic as well as international markets. JMC has bagged several orders from the government sector like Supreme Court building, President's convention centre and museum. The company is targeting more orders in this segment as the norm of high quality work discourages smaller contractors, thus improving the overall margins.

Table 3: Road BOOT projects: Operational losses continue

	Rohtak- Bawal (Kurukshetra)	Agra-Aligarh (Brij Bhoomi)	Nagpur-Wainganga (Wainganga)	Rewa MP-UP border (Vindhyachal)
Concession Period	28	15	18	30
Length in Kms	84	79	45	89
Company's stake in SPV	51%	100%	100%	100%
Equity Investment	1,224	500	1,200	1,900
Debt	4,029	1,600	3,300	5,000
Grant	-	500	-	-
Total Cost	5,253	2,650	4,500	6,900
Operational Since	3QFY15	4QFY15	4QFY15	FULL COD pending

Source: Company, Systematix Institutional Research

Funding of operational losses

JMC Projects owns four road BOOT toll collection projects across various parts of India. As of Feb 23, 2016, the company's daily toll collection from the four BOT projects put together was close to Rs52lakh/day, while the cash breakeven for the company is at Rs60lakh/day. Toll collection below estimates in Rohtak-Bawal, Agra-Aligarh and Nagpur-Wainganga projects and award of only partial COD for Rewa project have led to below-potential revenue collection for the company.

For 4QFY16, KPTL will infuse Rs300mn as equity in these projects to fund the operational losses from the four BOT projects, which will be supplemented with one more round of Rs300mn equity funding in FY17.

Other highlights

- JMC has raised Rs1.5bn through a rights issue in January 2016, the proceeds of which will be used to repay debt.
- Total debt on the balance sheet is Rs7.5bn, which is likely to reduce to Rs6bn immediately. But it is likely to rise again as the company needs to fund operational losses.
- JMC's management has decided to not opt for any road BOT projects going forward.
- Order book composition stands at 60% private and 40% public. L1 position at Rs10bn.
- Working capital cycle stands at -65 days.
- Cost of debt stands at 10.75% for EPC projects and 11.2% for BOOT projects.
- The company expects a recovery in commercial buildings sector along with good ordering in road EPC.
- JMC expects to improve the EBITDA margin to 9% over the next two years and is not aggressively pursuing the growth in revenues

Shree Shubham Logistics – running on low utilisation

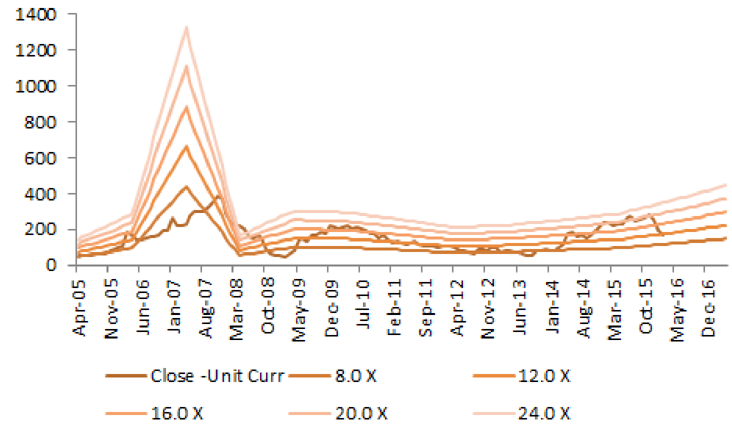
Shree Shubham Logistics decided to withdraw the DRHP before its scheduled IPO last year due to exit of senior management personnel and change of business strategy. KPTL owns 65% stake, the original promoters (Bafna family) own 10% and Tano private equity owns 25% of Shree Shubham. KPTL has invested Rs580mn in Shree Shubham in the form of equity and preferential shares, while Tano PE has invested Rs800mn in the company.

The company’s warehouse utilisations have fallen drastically to 40-45% in the states of Maharashtra and Madhya Pradesh as a result of severe decline in agri output in the last one year. Utilisations are still running high at 85-90% in the states of Gujarat and Rajasthan.

On 9MFY16 basis, the division has actually de-grown at 14% on a yoy basis, while net profit has turned into losses of Rs180mn as of Dec 31, 2015. We believe the prospects of improving utilisation in warehouses located in MP and Maharashtra are low in the immediate future as both places are still reeling under drought conditions. We do not expect the company to make profits before FY18.

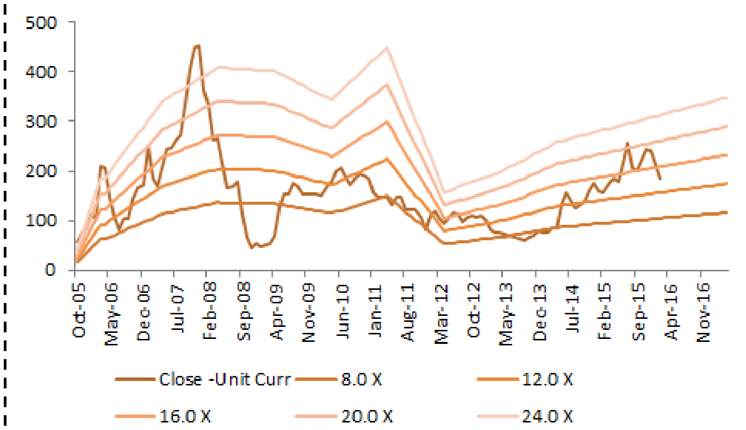
Valuation methodology

Chart 16: 1-year forward PE – KPTL



Source: Company, Systematix Institutional Research

Chart 17: 1-year forward PE - JMC Projects



Source: Company, Systematix Institutional Research

Table 4: SOTP Valuation for Kalpataru Power

	Equity Invested (expected on Mar 18)	Net Profits (FY18e)	Target P/E Multiple (FY18e)	Target P/BV Multiple (FY18e)	Valuation (Rs mn)	Valuation /share of KPTL	Remarks
1) Kalpataru Power - Standalone		2,840	12		34,075	222	50% discount to large EPC players like Ahulwalia, ITD owing to size, lower returns, and high D/E
2) KPTL Transmission Assets							
- Jhajjar	458			1.5	687	4.5	Asset operational since Mar 13, earning Rs 540mn annuity
- Satpura	1073.6			1.5	1,610	10.5	Asset operational since Apr 15, earning Rs 380mn annuity
3) Energylink (Indore Project	1989			0.6	1,193	7.8	Launched for sales in Mar 2016
4) Amber RE (Thane Project)	1936			1	1,936	12.6	30% sold,60% leased at Rs48/sqft/pm
Total	**KTPL+Investments Valuation**					**257.4**	
3) JMC Projects - Standalone		577	6		3,460	15	50% discount to large EPC players like Ahulwalia, ITD owing to size, lower returns, and high D/E
- Road BOOT Projects	6,100			0.5	3,050	13	Traffic below target .Expected to break-even by FY18e
Applying Holding Company Discount @ 25%.	**JMC Valuation**					21	
4) Shree Shubham Logistics	628.5			1.0	628.5	3	Turning into profitability looks farfetched now.
TOTAL						**281**	

Source: Company, Systematix Institutional Research

KEC International

1 April, 2016

Market leadership position, margins set to improve

INITIATING COVERAGE

Sector: Power T&D	Rating: Accumulate
CMP: Rs122	Target price: Rs138

Stock Info

Sensex/Nifty	27,337/ 7,716
Bloomberg	KECI IN
Equity shares (mn)	257.1
52-wk High/Low	Rs165/ 72
Face value	Rs2
M-Cap	R30 bn/ $455mn
3-m Avg volume	$0.6mn

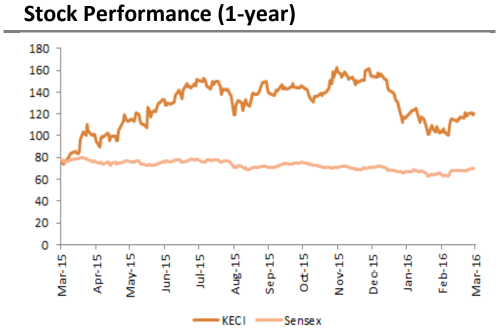
Financial Snapshot (Rs mn)

Y/E March	FY16e	FY17e	FY18e
Sales (Rs mn)	88,880	100,641	114,481
Net Profit (Rs mn)	1,828	2,566	2,964
EPS (Rs)	7.1	10.0	11.5
Growth (%)	157.2	40.4	15.5
PE (x)	17.2	12.2	10.6
EV/EBIDTA (x)	5.8	4.6	3.7
P/B (x)	2.1	1.8	1.6
RoE(%)	12.9	15.9	15.9
RoCE (%)	16.6	18.2	18.3
Dividend Yield (%)	0.8	0.8	0.8
Net Gearing (x)	1.4	1.1	0.8

Shareholding pattern (%)

	Dec '15	Sep '15	Jun '15
Promoter	50.5	50.5	50.4
–Pledged	-	-	-
FII	6.3	5.9	4.7
DII	25.8	26.0	25.1
Others	17.4	17.6	19.8

Stock Performance (1-year)



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KEC International Ltd (KECI), the leading player in power transmission sector, is extending the market share to 22.7% in orders from PGCIL and to ~25% in the orders from select SEBs. Higher spending by PGCIL/SEBs on >400kV/HVDC lines will restrict the competition, leading to margin improvement. SAE Towers is witnessing an improvement in demand in Latin American markets and is expected to be PBT positive in FY16. We expect railways and solar segments to be the drivers of incremental growth for the next three years, benefiting from the huge capex underway in the segments. Higher asset utilisation and improving margin profile will lead to a RoCE expansion to 18.3% in FY18e, from 13.8%% in FY15. We estimate the company to grow its net sales and net profit at a CAGR of 10.6% and 61% during FY15-18e. We initiate coverage on KECI with an Accumulate rating, valuing the stock at a PE of 12x FY18e and arrive at a target price of Rs138.

Extending the lead in transmission – margin profile too improves

KECI extended the market share in PGCIL orders in the 12th plan to 22.7% from ~15% in the 11^{th} plan as its integrated operations and excellent track record in project execution up to 765kV/HVDC levels has given an edge over peers. We expect KECI to post order inflow CAGR of 13% over FY15-18e, thus consistently providing over one-year visibility to the domestic T&D business. The JV in Saudi Arabia for transmission projects has not faced a slowdown in power T&D related capex in the Middle East as these projects continue to be of systemic importance for the region. SAE Towers, the tower manufacturing subsidiary in Latin America is reporting higher utilisations in Mexico and dispatch clearances in Brazil, resulting in the company turning PBT positive this year and adding substantially to its overall profitability. We expect KECI's transmission EPC vertical and SAE Towers to grow by 7% and 11% CAGR respectively in net sales during FY15-18e, on lower commodity prices.

Railways and solar – growth drivers of future

Cables vertical is expected to witness the continued strong demand from distribution & railway electrification-led capex by posting a CAGR of 15% during FY15-18e. We expect railways and solar segments to be the growth drivers for KECI in the next few years. Both the segments are expected to be a beneficiary of the large capex of Rs5trn and Rs6trn planned till 2020 and 2022 respectively. Pertinently, as KECI has the proven credentials and experience in executing small to medium-sized projects in both segments, the migration to larger orders above Rs2bn would provide the impetus to growth momentum reaching 31% and 296% in railways and solar (from a small base) respectively during FY15-18e. The water segment is facing headwinds as many projects are yet to materialise and some are being bid intensely by competitors.

Valuation and view

We expect KECI's strong volume growth in businesses such as cables, solar and railways to more than offset the headwinds suffered by transmission vertical and SAE Towers vertical due to fallen commodity prices. We expect the company's net sales to grow at a CAGR of 10.6% during the period FY15-18e. As the profitability normalises in the next two years, we expect the company's net profit to grow at a CAGR of 61% between FY15-18e. We assign the valuation of power EPC companies to KECI, valuing the stock at a PE of 12x on FY18e and recommend an Accumulate rating with a target price of Rs138, an upside of 13%.

FINANCIALS (CONSOLIDATED)

Profit & Loss Statement

YE: Mar (Rs mn)	FY14	FY15	FY16e	FY17e	FY18e
Net Revenues	79,018	84,678	88,880	100,641	114,481
% growth	13.2	7.2	5.0	13.2	13.8
- Op. Expenses	74,086	79,560	82,302	92,891	105,953
EBITDA	4,933	5,118	6,577	7,749	8,529
EBIDTA Margin (%)	6.2	6.0	7.4	7.7	7.5
- Interest Expenses	2,633	3,089	2,741	2,625	2,690
- Depreciation	705	881	902	959	1,011
+Other Income	138	112	112	112	112
- Tax	883	550	1,218	1,711	1,976
Effective Tax Rate (%)	57	44	40	40	40
Adj.PAT	849.2	710.7	1,828	2,566	2,964
+/- Extraordinary Items	(181.6)	891.3	-	-	-
+/- Minority Interest	-	-	-	-	-
Reported PAT	668	1,602	1,828	2,566	2,964
Adj. FDEPS (Rs/Share)	3.3	2.8	7.1	10.0	11.5
Adj. FDEPS growth (%)	30.2	(16.3)	157.2	40.4	15.5

Source: Company, Systematix Institutional Research

Balance Sheet

YE: Mar (Rs mn)	FY14	FY15	FY16e	FY17e	FY18e
Share Capital	514	514	514	514	514
Reserves & Surplus	11,402	12,784	14,436	16,746	19,413
Net Worth	11,916	13,298	14,951	17,260	19,927
Minority Interest	-	-	-	-	-
Total Debt	21,273	21,894	22,075	22,318	22,830
Other liabilities	932	915	915	915	915
Capital Employed	34,120	36,106	37,940	40,493	43,672
Net Fixed Assets	13,700	12,753	12,651	12,492	12,281
Investments	3,506	5,226	5,478	5,743	6,021
- of which liquid	-	-	-	-	-
Net Working Capital	15,474	16,064	18,993	19,247	19,006
Cash and Bank Balance	1,440	2,063	818	3,011	6,364
Capital Deployed	34,120	36,106	37,940	40,493	43,672
Net Debt	19,833	19,831	21,257	19,307	16,466
WC Days	(37)	(14)	(15)	(15)	38
Book Value (Rs/sh)	46	52	58	67	78

Source: Company, Systematix Institutional Research

Cash Flow

YE: Mar (Rs mn)	FY14	FY15	FY16e	FY17e	FY18e
PAT	849	711	1,828	2,566	2,964
+ Non Cash Items	705	881	902	959	1,011
Cash Profit	1,554	1,592	2,730	3,525	3,975
+ (Incr)/Decr in WC	(3,925)	(590)	(2,929)	(254)	240
Operating Cash Flow	(2,371)	1,002	(199)	3,272	4,215
+ Capex	(513)	230	(800)	(800)	(800)
Free Cash Flow	(2,884)	1,233	(999)	2,472	3,415
- Dividend	150	175	175	257	296
+ Equity Raised	(75)	(45)	-	-	-
+ Debt Raised	4,583	621	181	243	512
+Investments	(1,339)	(1,885)	(252)	(265)	(278)
+ other CL	(253)	874	-	-	-
Net Cash Flow	(116)	623	(1,245)	2,193	3,353
+ Opening Cash	1,556	1,440	2,063	818	3,011
Closing Cash	1,440	2,063	818	3,011	6,364

Source: Company, Systematix Institutional Research

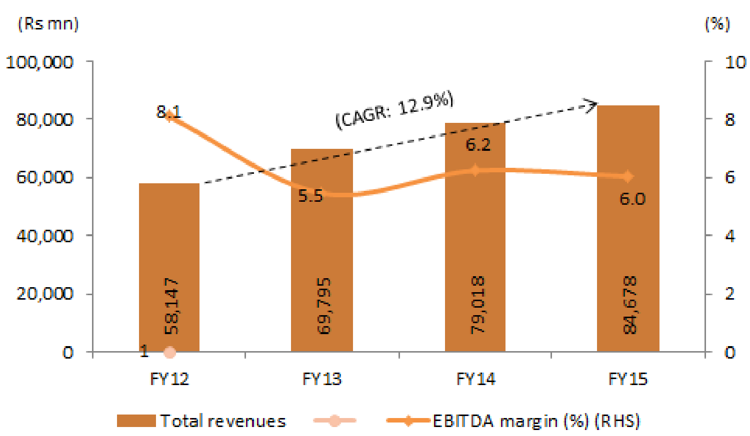
Ratios

YE: Mar	FY14	FY15	FY16e	FY17e	FY18e
P/E(x)	48.1	44.1	17.2	12.2	10.6
P/CEPS(x)	20.2	19.7	11.5	8.9	7.9
Mcap/Sales	0.4	0.4	0.4	0.3	0.3
EV/EBIDTA(x)	7.3	7.2	5.8	4.6	3.7
RoE (%)	5.7	12.7	12.9	15.9	15.9
RoCE (%)	16.4	13.8	16.6	18.2	18.3
Fixed Asset Turnover (x)	5.8	6.6	7.0	8.1	9.3
Dividend Yield (%)	2.7	1.0	0.8	0.8	0.8
Dividend Payout (%)	22.4	10.9	9.6	10.0	10.0
Debt/Equity(x)	1.8	1.6	1.5	1.3	1.1
Debtors (days)	186.8	171.8	190.0	190.0	190.0
Revenue Growth (%)	13.2	7.2	5.0	13.2	13.8
PAT Growth (%)	30.2	(16.3)	157.2	40.4	15.5
EBIDTA Growth (%)	29.3	3.8	28.5	17.8	10.1
EPS Growth (%)	30.2	(16.3)	157.2	40.4	15.5

Source: Company, Systematix Institutional Research

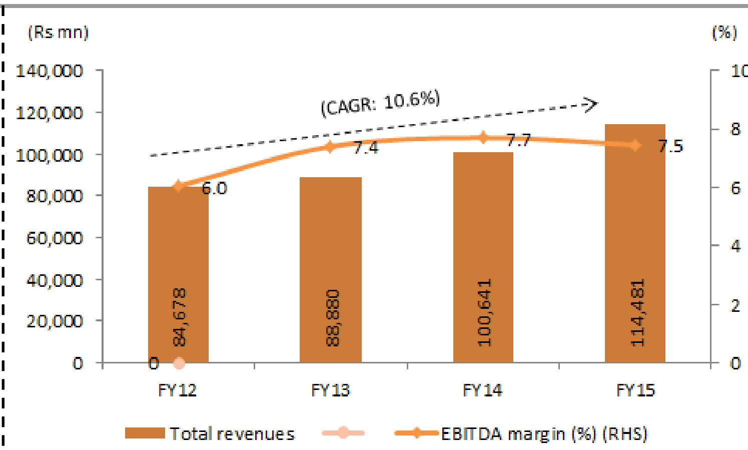
Charting the story

Chart 1: Margins were under pressure despite healthy revenue



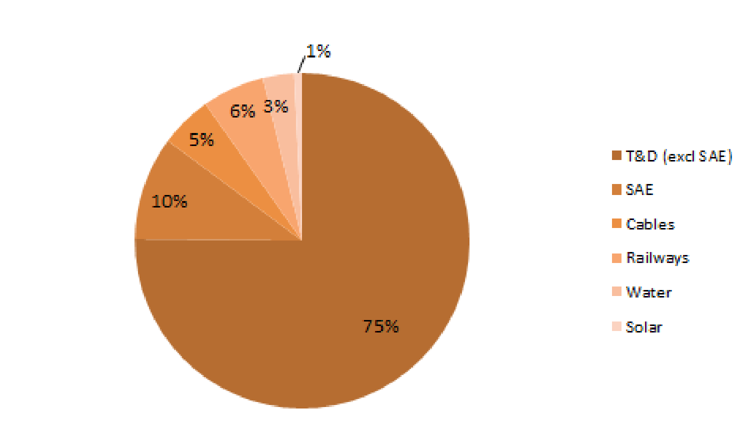
Source: Company, Systematix Institutional Research

Chart 2: Commodities impact revenue while improving margins



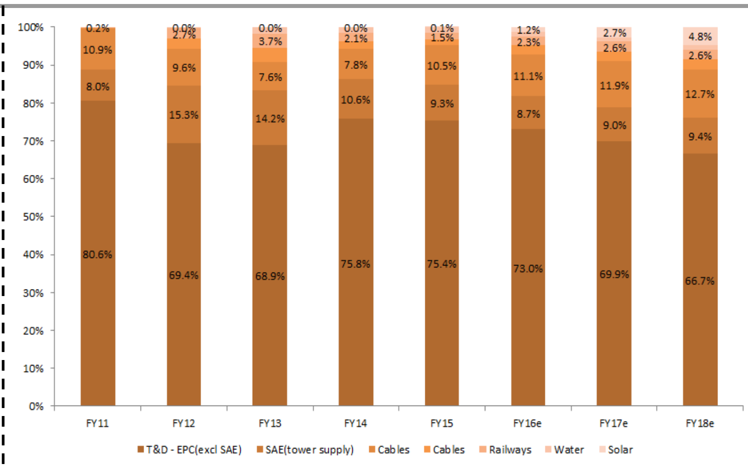
Source: Company, Systematix Institutional Research

Chart 3: Order backlog - segment-wise, Rs93.7bn, 9MFY16



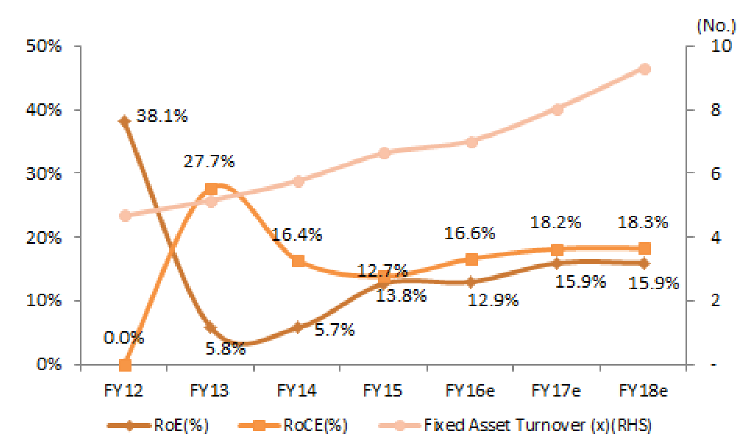
Source: Company, Systematix Institutional Research

Chart 4: Cables, Railways & Solar to be growth drivers



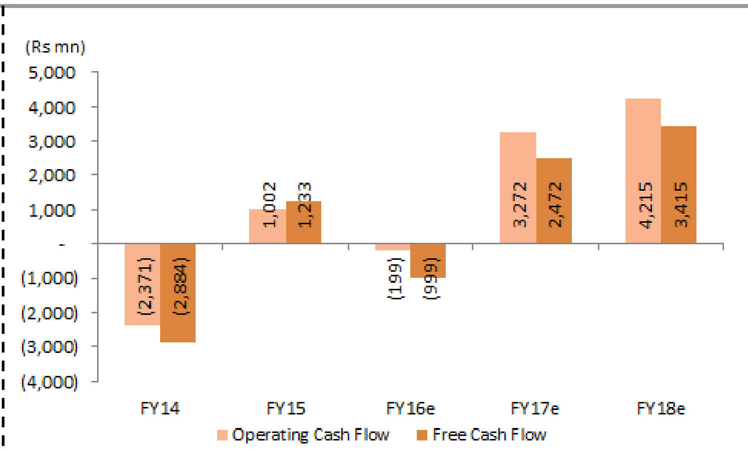
Source: Company, Systematix Institutional Research

Chart 5: Steady improvement in return ratios



Source: Company, Systematix Institutional Research

Chart 6: Savings in WC to improve cash flows



Source: Company Systematix Institutional Research

Company description

KEC International Ltd is the flagship company of the RPG group, acquired in 1952, and operating in five key verticals -- mainly as an EPC player in power transmission & distribution, railways, water and solar energy, and has a cable manufacturing facility. The company has an experience of over seven decades, executing projects in extreme climatic conditions and environments in more than 60 countries across the world.

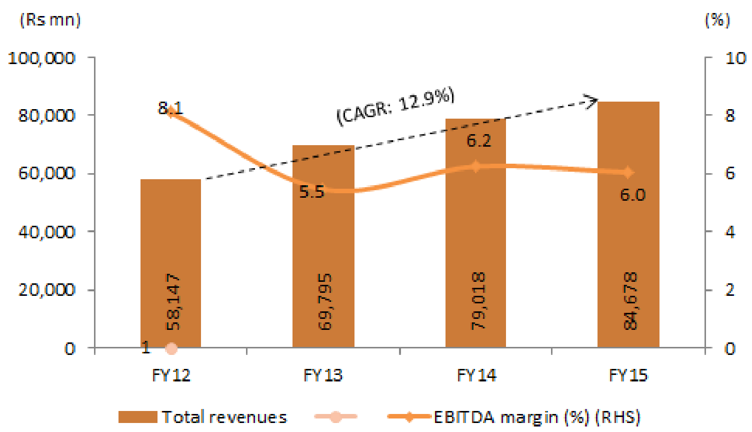
KECI has pre-qualifications with most leading transmission utilities across the world, with an ability to manufacture and supply power transmission lines up to 1,200kv and substations of up to 1,150kV. It has more than 5,000 employees deployed across the EPC vertical and four tower testing facilities (three in India, one in Brazil) and transmission-tower-manufacturing capacity (combined capacity of 311,200tpa) at five locations (three in India, two outside).

Organisation structure

The domestic business is a part of the standalone entity, while the international operations are run through country specific subsidiary/JV/associate companies. International tower supply business is handled by the 100% owned subsidiary, SAE Towers.

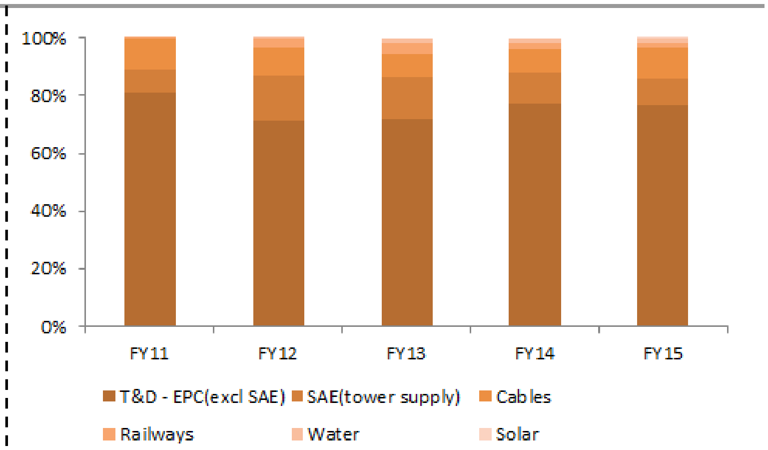
Financial overview

Chart 7: Lower margins despite healthy revenue growth



Source: Company, Systematix Institutional Research

Chart 8: Segmental break-up – T&D (domestic) dominates the pie



Source: Company, Systematix Institutional Research

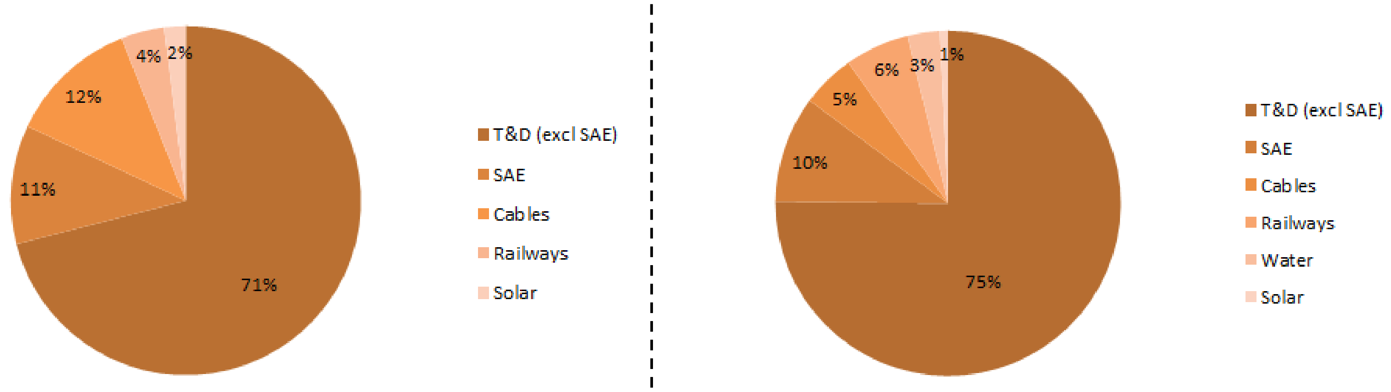
T&D (excluding SAE) continues to be the largest segment for the company, contributing to 77% of sales in FY15. KECI had acquired 100% stake in SAE Towers, headquartered in Houston, US in 2011 to gain a foothold in the American market. Since then, SAE Towers has posted a CAGR of 23% during FY11-15 to account for 9.5% of total revenue in FY15. The company's efforts in turning around the fortunes of SAE Towers are expected to be seen in FY16, with SAE most likely to post a net profit for the first time since acquisition.

Similarly, KECI entered the cables segment (HT/LT cables, EHV cables, control & instrumentation cables) in 2012, post which the division clocked a CAGR of 17% during FY12-15, accounting for 10.7% of net sales in FY15. One of the lagging segment for KECI has been water, which despite the huge potential, has grown to a revenue size of only Rs1.3bn in FY15, which is insignificant compared to the size of the company.

KECI executes railway signaling, track laying and other civil work for Indian Railways. The segment has posted a CAGR of negative 7% during FY12-15, to account for 1.6%

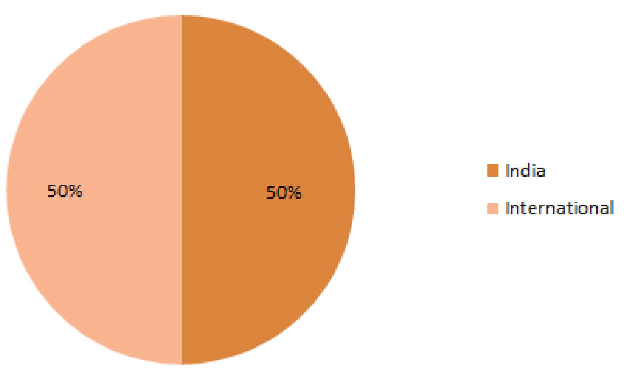
in FY15. Recently, Indian railways announced plans to invest Rs5tr till 2020 on modernisation, laying new tracks, doubling existing ones and electrification. The company expects railways segment to be one of the growth drivers in the next five to seven years. Recently, KECI also entered the fast-growing solar segment, with capabilities across EPC of medium-to-large size solar parks. The segment is seeing strong traction with orders worth Rs1.3bn in hand and at least Rs5bn of orders where the company is expecting high prospects of immediate order closure. Despite the lower margin profile, KECI would prefer solar EPC orders as the execution time is shorter with faster working capital cycle.

Chart 9: Order book – stronger inflows in FY15, comfortable order backlog of Rs93.7bn as of 9MFY16



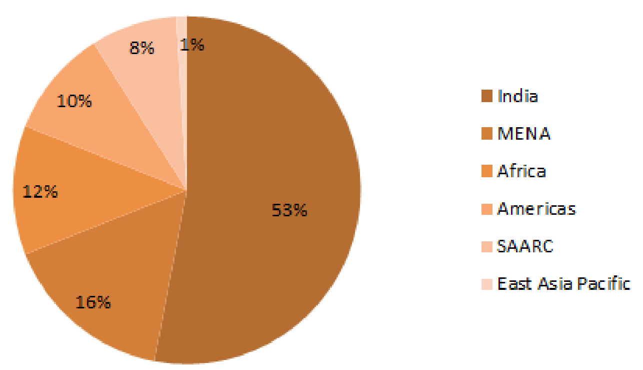
Source: Company, Systematix Institutional Research

Chart 10: Order inflow – region-wise



Source: Company, Systematix Institutional Research

Chart 11: Order backlog – region-wise



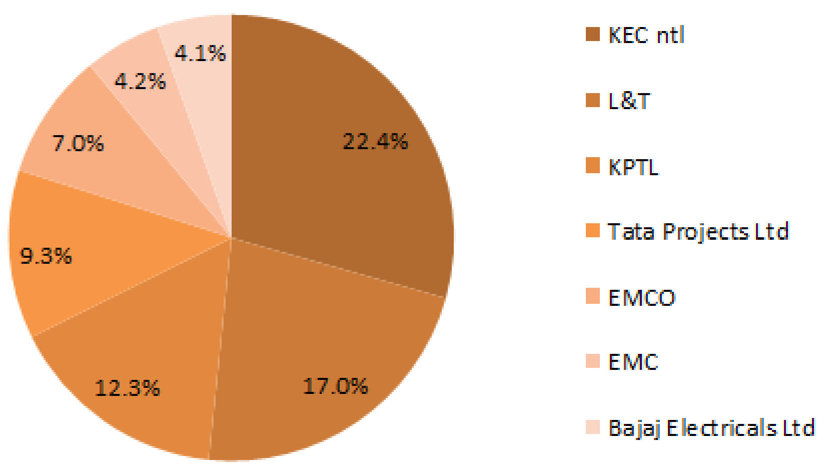
Source: Company, Systematix Institutional Research

Transmission EPC: Extending the lead

KECI is dominant in the power transmission and distribution (excluding SAE Towers) sector as an integrated player with strong execution capabilities. The company is capable of executing projects up to 1,200kV transmission lines on a turnkey basis. On the distribution side, KECI has the ability to execute EPC projects of High Voltage Electrical Switching and Distribution Substations, High Voltage Air Insulated Substations (AIS) up to 1,150kV and Gas Insulated Substations (GIS) up to 765kV as per various national and international standards. The company also undertakes installation of Optical Fibre Cable (OFC) networks, Optical Ground Wire (OPGW) stringing and HV/EHV cabling project works on a turnkey basis for the telecom sector.

KECI is the largest power transmission tower manufacturer in India, with an installed capacity of 211,200mt/annum, spread across three factories in India – Nagpur (Maharashtra), Jaipur (Rajasthan) and Jabalpur (Madhya Pradesh). Through SAE Towers, the wholly-owned subsidiary, the company has an annual production capacity of 100,000tpa spread over Mexico (35,000tpa) and Brazil (65,000tpa).

Chart 12: Leading market share in PGCIL orders for 12th plan



Source: PGCIL, Systematix Institutional Research

KECI has achieved the highest market share in transmission tower EPC orders (including only tower supply orders) placed during the 12th plan. It accounted for a market share of 22.7%, which is almost 6.3% higher than the nearest competitor, Larsen & Toubro. Increase in market share can be attributed to KECI's enhanced capability to execute projects across regions in the most cost effective manner. Also, the stringent norms laid by PGCIL in pre-qualification and timely project completion have limited the competition at >400kV levels. For projects above 400kV, the competition has narrowed down to top six to eight players only.

KECI prefers to work with select SEBs like Tamil Nadu, Karnataka, Gujarat, and Maharashtra. Orders from SEBs accounted for 15% of the company's total order inflow during 9MFY16 from the T&D segment. KECI continues to bid selectively for SEBs' projects which have financial backing from multilateral or bilateral agencies.

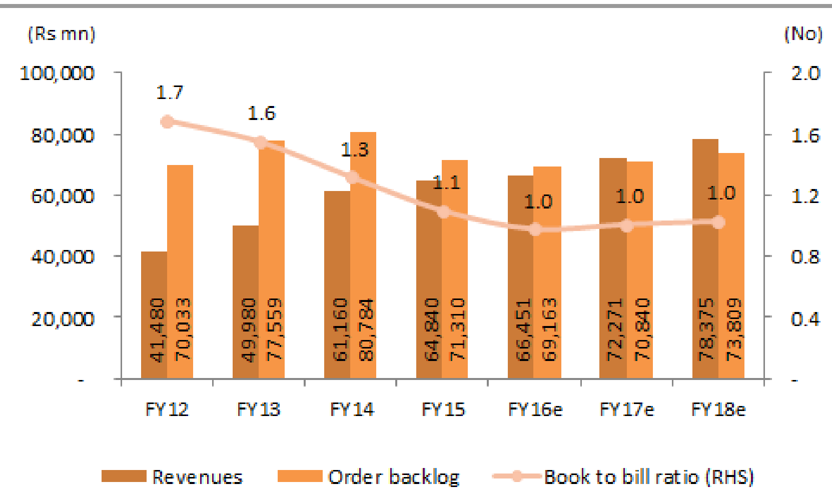
Table 1: Major order wins in FY16 – Domestic & International Businesses

March 17,2016
• Orders worth Rs 2.5 bn from PGCIL for construction of Transmission Lines in various parts of India • An order worth Rs 830mn from West Bengal State Electricity Transmission Company Limited for construction of Transmission Lines • Orders worth Rs 4.0 bn for construction of Transmission Line in Ghana, Africa.
January 01,2016
• -Orders of Rs 6.6 bn for construction of various Transmission Lines and Substations in Saudi Arabia.
October 07,2015
• -An order from Transmission Corporation of Telangana Limited for supply and construction of 400kV transmission line in Southern India.
July 10,2015
• Secured two orders of Rs. 1.26 bn from PGCIL for supply and construction of Transmission Lines in Northern India. • Secured an order of Rs. 3 bn for the construction of HVDC Transmission Line in Kenya. In addition secured orders of Rs. 81 crore for supply of lattice towers, monopoles & hardware in the Americas
June 09,2015
• Four orders of Rs. 3.7 bn from PGCIL for construction of Transmission Lines in the Northern, Southern, Eastern (Indo- Bangladesh) and Central Regions. • Secured orders of Rs. 1.1bn for underground cabling works in Saudi Arabia. In addition secured small orders totaling Rs. 400 mn in Africa, the Middle East and the Americas.

Source: PGCIL, Systematix Institutional Research

The Middle East & North Africa (MENA) region accounts for 15% of KECI's order backlog as of Dec 31, 2015. The management has not seen any reduction in the power transmission orders from the region, despite their annual budgets getting constrained from a fall in oil prices. We believe as power T&D sector is a part of the essential infrastructure in all these countries, the capex would not be curtailed immediately as has been the case with commercial and residential real estate sectors. If crude oil stays below US$40/barrel for over one to two years, then deep cuts are likely in the budgets of countries from MENA region. Currently, we factor only an elongation in the working capital cycle for orders corresponding to the MENA region.

Chart 13: Ordering to improve with better execution in India, if Middle East falters



Source: Company, Systematix Institutional Research

We expect capex of Rs2 tn in the transmission sector in the next five years, resulting in capex of Rs 800 bn on EPC transmission lines and substations during the same period. With expanding opportunities in both AIS and GIS substations, we expect the company to benefit incrementally from the substation orders. Volume growth in the traditional transmission EPC business is expected to be in the range of 12-15%, while in value terms, we expect order inflows at a CAGR of 14.6% during FY15-18e.

Entry into substations

KECI has developed the abilities to execute both AIS and GIS substations up to 765kv. The company has entered into an equipment sourcing partnership with the Chinese player 'Pianggio' for 765kv switchgears. KECI is still a small player in the substation space with a market share of less than 1% in the 12th plan orders.

Recent order wins

1) 765kv GIS substation in Thiruvalam, Tamil Nadu for PGCIL
2) A turnkey order for 400 kV GIS Substation in Bhutan from Bhutan Power Corporation Limited.
3) Combined orders for setting-up 33/11kV and 66/11 kV substations at areas near Nairobi, Kenya. The order value is Rs.1.67bn and project duration is 24 months.

As of Dec 31, 2015, substations accounted for 15% of the order backlog spread over both India and the Middle East combined. We expect substations segment to gradually grow across regions. Rather than the company becoming a dominant player in substations segment, we expect the segment to act more as complimentary to the company's offerings in transmission line orders.

KEC ventures into BOOT projects

KECI has bagged its first BOOT order of Rs2.5bn on PPP basis from the Rajasthan Rajya Vidyut Prasaran Nigam Ltd. The project is of 172km, which KECI plans to execute over the next 21 months. It has been bagged on VGF basis, with a debt:equity contribution of 70:30; KECI intends to restrict its equity contribution to Rs500mn. We have not taken this BOOT project under consideration while valuing the company as the final terms and conditions are yet to be finalised.

SAE turning profitable

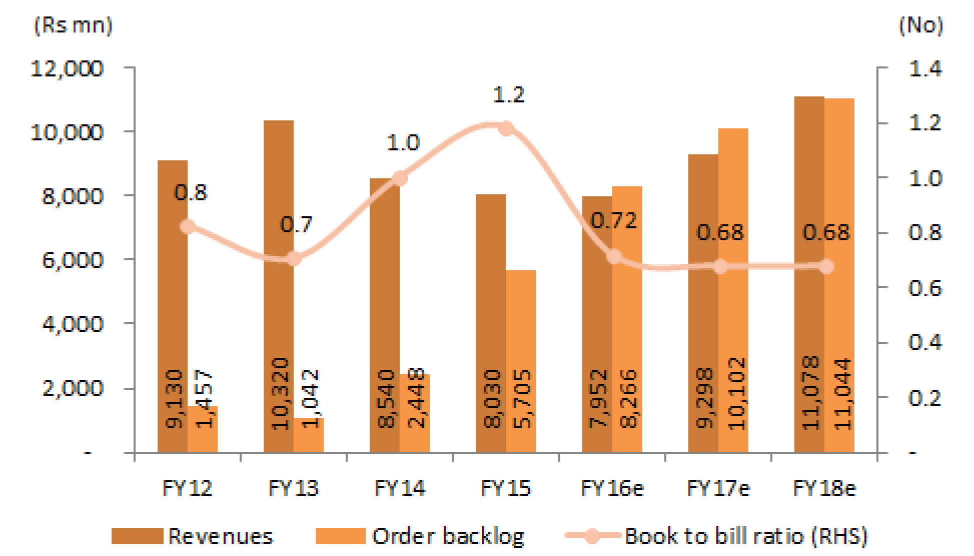
KECI acquired 100% stake in SAE Towers in September 2010 at an enterprise value of US$95mn. Currently, SAE is a 100% wholly-owned subsidiary of KECI. SAE is the leading manufacturer of lattice transmission towers in the Americas. It has a manufacturing capacity of 100,000tpa spread over two locations – Brazil (65,000 tpa) and Mexico (35,000 tpa).

SAE's acquisition strengthened KECI's global leadership in the power transmission space. This acquisition marked KECI's entry into the large markets of North and South America -- US, Canada, Mexico, Brazil and other neighbouring countries. Post this acquisition, Americas has become one of the largest markets for the company outside India.

Latin American transmission market is mostly operated by large private sector transmission line operators based out of North America or Europe. These operators plan long-term projects well in advance and are most of the time funded by multilateral agencies like the World Bank.

According to World Energy Investment Outlook,2014, the spend on power transmission lines during 2014-35 in the Latin American market is expected to be $127bn. We believe the Latin American market holds the long-term potential similar to India, wherein the sheer demand for power and size of the region will drive the power sector for the next decade.

Chart 14: Order inflows on upward trajectory – profitability improves



Source: Company, Systematix Institutional Research

Mexican operations were weighed down by lack of orders in FY15 while Brazil operations had suffered due to lack of clearances for dispatch of materials leading to inventory accumulation. Both these factors led to loss to the extent of Rs 580mn in FY15 vis-à-vis marginal profits in FY14. Over the 9MFY16, SAE received orders in Mexico reviving the operations. Also, Brazil operations are slowly getting dispatch approvals leading to disposal of inventory.

Higher utilisation of production facilities and disposal of inventory is expected to turn the company's PBT into positive territory this year.

Turnaround of SAE is vital for margins improvement as segmental profits will promptly enhance the company's overall profitability. By comparing KECI's peer (Skipper) margin profile in orders from Latin America of ~15-18%, we believe KECI has a huge scope for profitability improvement. For the next two years, the management expects likely operating margins of 5% levels for SAE Towers combined entity.

Cables: Power cables driving the segment

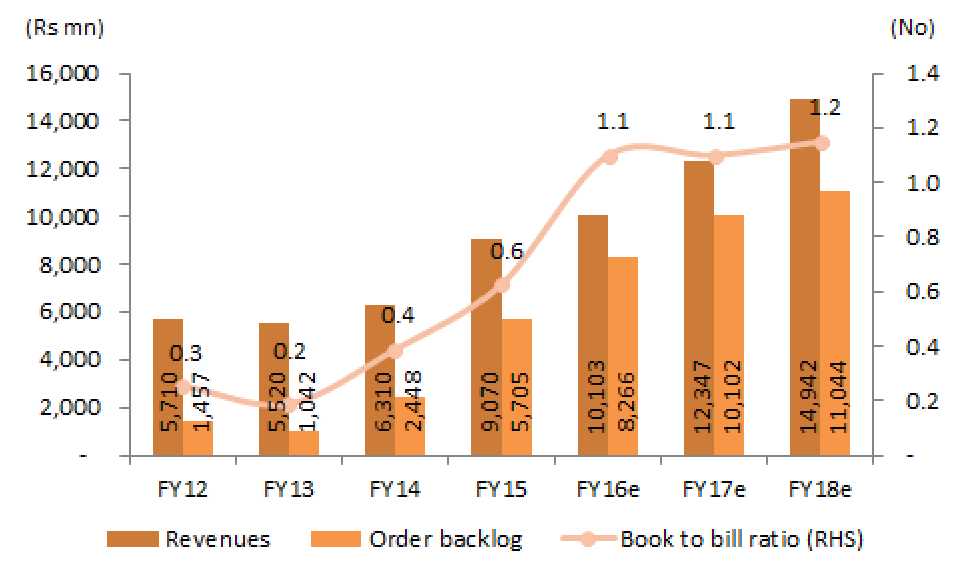
KECI entered the manufacturing of cables business through merger of RPG Cables with itself in 2010. Since then the company has built world class integrated factories in Mysore, Vadodara and Silvassa with a capacity to manufacture power cables - 36,000 km/year, optical fibre cables - 0.6mn fkm and copper telecom cables - 2mn ckm.

The company closed down the production of cables at its Thane factory from February 2013 and finally assets were disposed off in December 2014 for a net consideration of Rs1,346.4mn.

KECI's wide range of power cables (HT and EHV cables up to 220kv) and telecom cables have seen strong acceptance in the market as the segment has posted a CAGR of 16.7% during FY12-15, while the order backlog has clocked a CAGR of 57.6% during the same period.

The government's thrust on strengthening the sub-transmission and distribution systems and increasing the share of renewables is expected to result in increased demand for power cables. The demand is also expected to get a boost on account of the proposed smart cities and mass transportation projects where higher proportion of EHV and HT cables are majorly used. We expect the cables business to post a revenue CAGR of 15% during FY15-18e.

Chart 15: Traction in distribution and renewables driving growth for power cables



Source: Company, Systematix Institutional Research

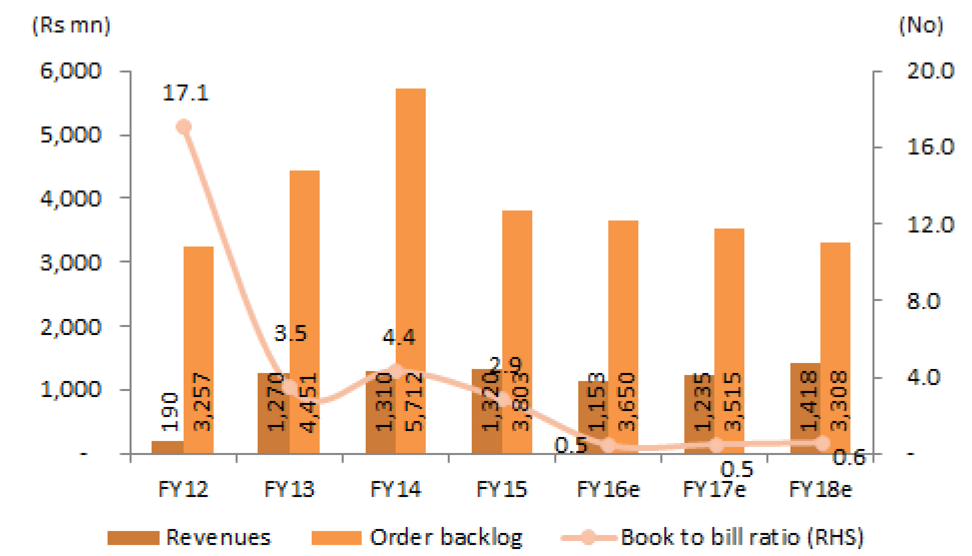
Water segment: lags despite the potential

KECI has established a strong presence in Water Resource Management (WRM) works like building canals, construction of dams and water system civil works related to thermal power projects. Also, under the Waste Water Treatment (WWT) services, the company undertakes sewage and industrial effluent treatment projects.

Despite the immense potential in the segment, KECI has been able to reach a turnover of only Rs1.3bn in FY15, as the slow growth in industrial sector and delay in finalisation of orders in river cleaning projects and water pipelines have restricted growth opportunities. Lack of quality orders has also led to huge competition in the sector, prompting the company to opt out of the ordering process since the past two years.

The water segment registered a CAGR of 91% during FY12-15, coming from a low base in FY12, and now accounts for 3% of the order backlog. Unless the segment receives massive impetus from projects like Ganga river cleaning or rapid industrial expansion, we believe the company's segmental business will grow at below potential CAGR of 9% during FY15-18e.

Chart 16: Order inflows below potential



Source: Company, Systematix Institutional Research

Railways and solar - next wave of growth

Over the past five decades, KECI has been working with Indian Railways in different capacities like:

- Civil infrastructure, including bridges, tunnels, platform, workshop modernisation and station building
- Earthwork, new track laying and rehabilitation of existing tracks
- Railway electrification and power systems, signaling and telecommunication network

The company has been involved in electrification of close to 20% of total tracks laid out in the country. KECI, through the participation in smaller tenders, has achieved pre-qualifications to bid for various parts of the dedicated freight corridor projects in consortium with partners.

Currently, the railways vertical accounted for 6% of the order backlog or Rs5.6bn worth of orders as of Dec 31, 2015. KECI has started to focus only on large size projects above Rs2bn. The company is executing more than 50 projects currently, varying from electrification to civil works.

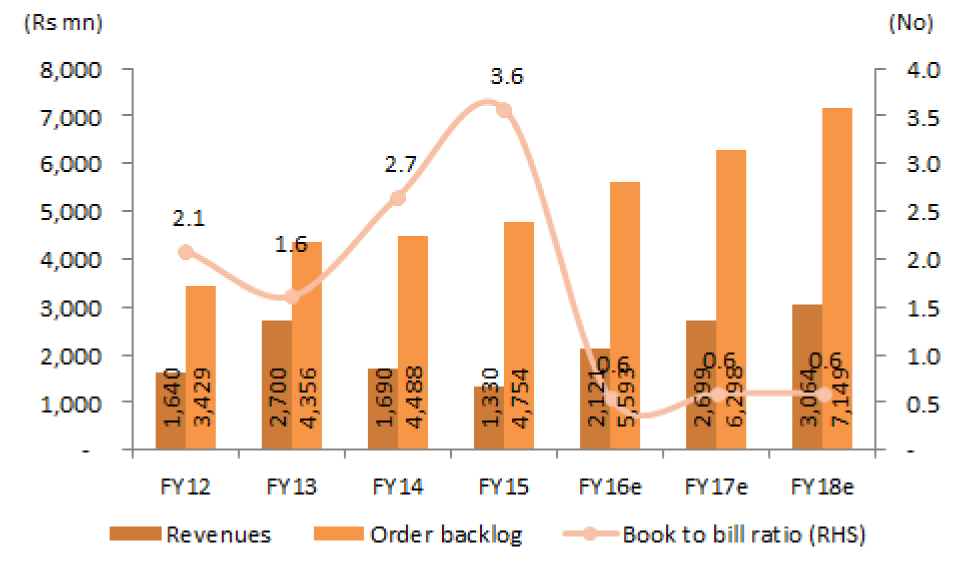
In FY15, cost overruns in few projects had exerted pressure on segmental profit margins. The existing order backlog has a better margin profile. Moreover, under railway minister Suresh Prabhu's leadership, Indian Railways is witnessing a new vibrancy and urgency in project completion.

Railway Budget 2016-17 – highlights

- Commissioning of 2,800kms of track in 2016-17; targets commissioning of broad gauge lines at over 7kms per day against an average of ~4.3kms per day in the last six years. Execution would increase to ~13kms per day in 2017-18 and 19kms per day in 2018-19.
- Under the Dedicated Freight Corridor, almost all contracts for civil engineering works to be awarded by Mar 31, 2016. It proposed to take up North-South, East-West & East Coast freight corridors through innovative financing, including PPP.
- Cabinet approval for JVs with state governments, 17 consented and 6 MoUs signed with state governments. 44 new partnership works covering ~5,300kms and valuing ~Rs927bn have been indicated in the Budget documents.
- Proposed to develop rail side logistics parks and warehousing in PPP mode, 10 goods sheds will be developed by the Transport Logistics Company of India (TRANSLOC) in 2016-17.

We expect KECI to be a beneficiary of capex of ~Rs5tr over FY15-20 by the Indian Railways. We expect the segment's order backlog and net sales to post a CAGR of 14% and 31% respectively over FY15-18e.

Chart 17: Beneficiary of investments for modernisation of railways



Source: Company, Systematix Institutional Research

Solar – rapid growth possible

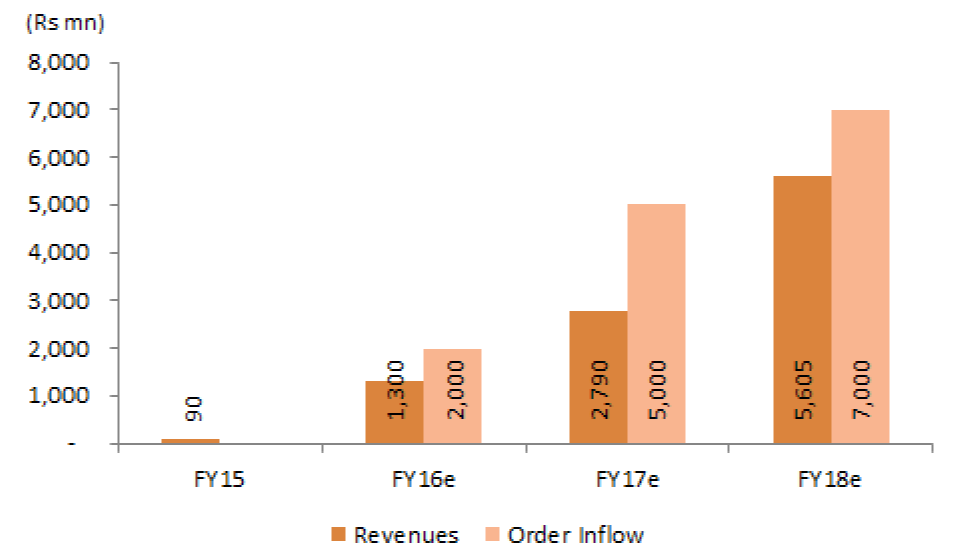
KECI has ventured into providing solar EPC services for large solar PV projects developed by private players and roof top PV solutions for industrial and commercial consumers.

The central government has raised India's solar power capacity target under the Jawaharlal Nehru National Solar Mission (JNNSM) by five times, reaching 100,000mw by 2022. The target will principally comprise of 40gw roof top and 60gw through large and medium scale grid connected solar power projects. The total investment in setting up 100gw will be ~Rs6,000bn.

The primary reason for KECI's entry into solar EPC market is the large number of orders available in the market and pertinently the faster execution cycle of 6-9 months. Solar EPC, being not a very complex job, is inherently a low margin job, with operating margin of ~5-8%. Despite the low margin profile, the faster turnaround time which leads to better asset turns, makes it a lucrative proposition for large EPC players like KECI.

We expect the company to grow rapidly in the solar EPC segment from Rs90mn in FY15 revenue to Rs5.6bn in FY18e, as the strong order flow and faster execution period will maintain the momentum.

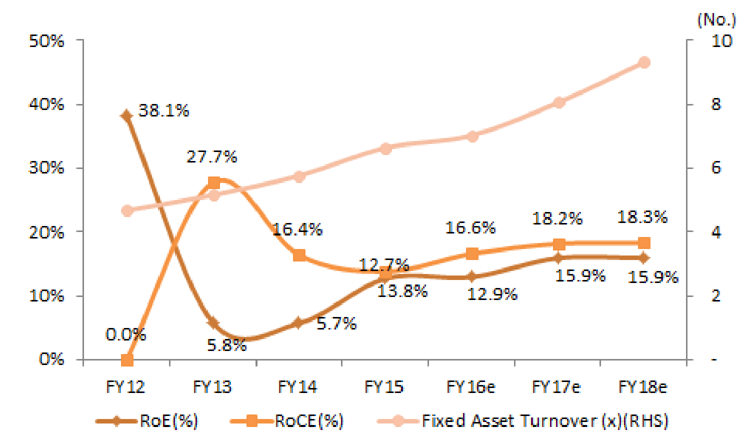
Chart 18: Multifold growth expected in Solar segment



Source: Company, Systematix Institutional Research

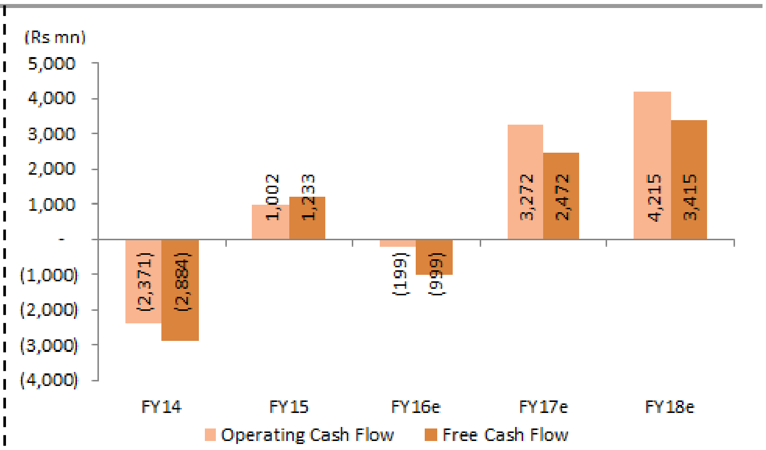
Improving working capital to strengthen cash flows and RoCE

Chart 19: Steady improvement in return ratios



Source: Company, Systematix Institutional Research

Chart 20: Savings in WC to improve cash flows

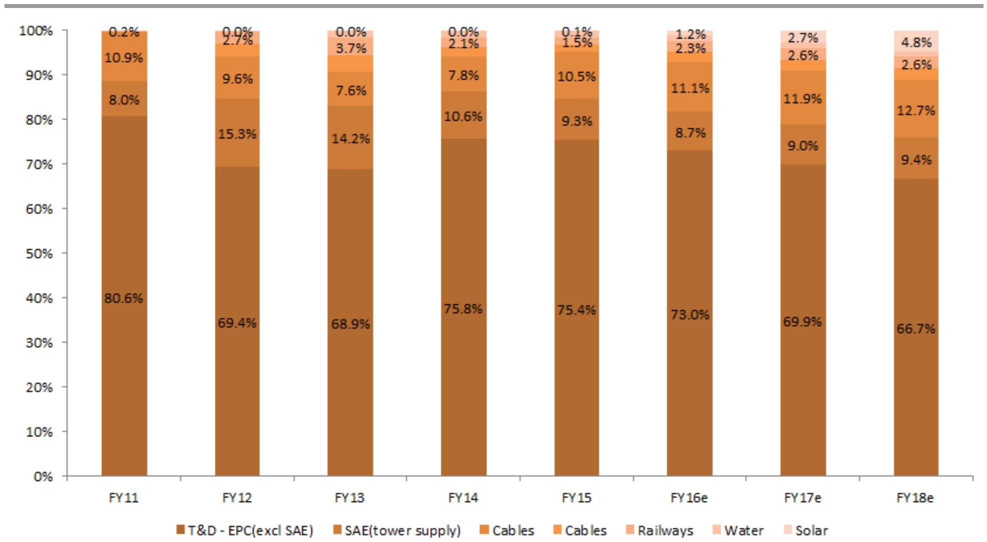


Source: Company, Systematix Institutional Research

KECI is expected to benefit on the back of a strong order backlog of Rs93bn and low commodity prices, leading to an improvement in EBITDA margin from 6% in FY15 to 7.5% in FY18e. Also, as the asset light businesses of cables, solar and railways are expected to be the growth drivers during FY16e-18e, the fixed asset turnover is expected to improve from 6.6x in FY15 to 9.3x in FY18e. Both these factors would lead to an improvement in RoE from 12.7% in FY15 to 15.9% in FY18e and RoCE from 13.8% in FY15 to 18.3% in FY18e respectively.

Higher operating profit generation and lesser investments in incremental working capital is expected to lead to a substantial improvement in operating and free cash flows for FY17 and FY18.

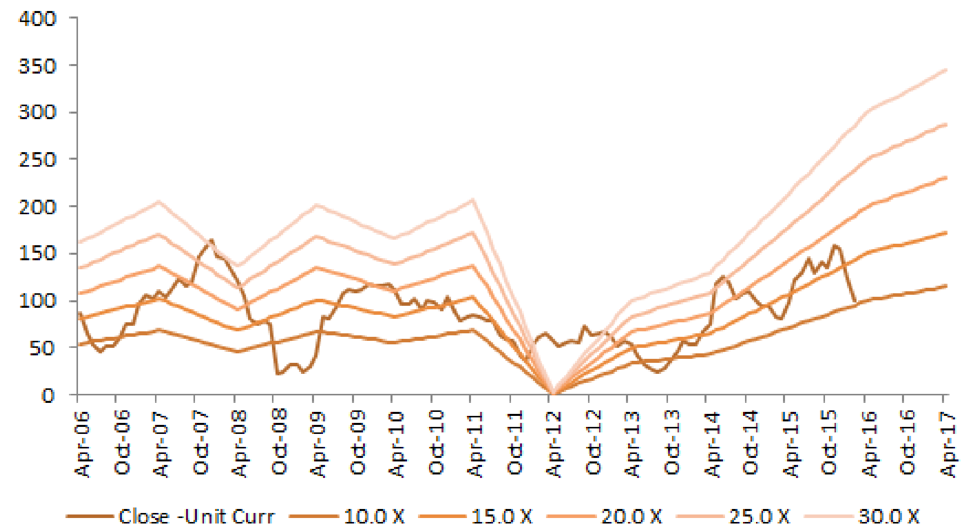
Chart 21: Cables, Railways & Solar to be growth drivers



Source: Company, Systematix Institutional Research

We expect KECI's strong volume growth in businesses such as cables, solar and railways to more than offset the headwinds witnessed by transmission vertical and SAE Towers vertical due to low commodity prices. We estimate the company's net sales to post a CAGR of 10.6% during FY15-18e. Benefits arising from operating leverage, improved execution in transmission projects and fixed priced contracts in international markets are expected to improve EBITDA margin to 7.5% in FY18e, from 6% in FY15. We factor a minor increase in debt levels from FY15 as the management has resorted to low cost short-term finance rather than accepting few of the high cost customer advances. KECI's net profit had hit a rough patch in FY15, falling to close to five-year low profitability. As profitability normalises in the next two years, we expect the company's net profit to post a CAGR of 61% during FY15-18e.

Chart 22: 1-year forward PE



Source: Capitaline, Systematix Institutional Research

We assign the valuation of EPC companies to KECI, valuing the stock at PE of 12x FY18e basis, and recommend an Accumulate rating with a target price of Rs138, an upside of 13%.

Techno Electric and Engg

1 April, 2016

Stellar show in EPC; BOOT projects – the way forward

INITIATING COVERAGE	
Sector: Power T&D	**Rating: Buy**
CMP: Rs535	**Target price: Rs640**

Stock Info

Sensex/Nifty	25,342/ 7,738
Bloomberg	TEEC IN
Equity shares (mn)	57.1
52-wk High/Low	Rs580/361
Face value	Rs2
M-Cap	Rs30bn/ $448mn
3-m Avg volume	$0.07mn

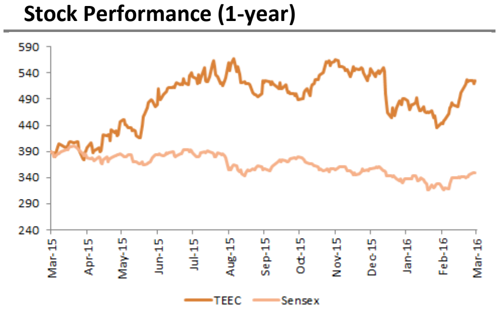
Financial Snapshot (Rs mn)

Y/E March	FY16e	FY17e	FY18e
Sales (Rs mn)	10,125	11,878	13,696
Net Profit (Rs mn)	1,115	1,379	1,714
EPS (Rs)	19.7	24.4	30.2
Growth (%)	31.0	23.4	24.1
PE (x)	27.1	22.0	17.7
EV/EBIDTA (x)	14.4	13.0	11.7
P/B (x)	3.0	2.7	2.4
RoE(%)	11.6	13.0	14.3
RoCE (%)	9.3	10.7	11.5
Dividend Yield (%)	1.0	1.0	1.0
Net Gearing (x)	0.2	0.1	-

Shareholding pattern (%)

	Dec '15	Sep '15	June '15
Promoter	58.0	58.0	58.0
–Pledged			
FII	11.9	8.6	6.7
DII	17.2	16.3	14.8
Others	12.9	17.1	20.5

Stock Performance (1-year)



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Techno Electric and Engineering Company Ltd (TEEC) has been at the forefront in executing complex EPC works for 400/765kv substations. TEEC has always adopted a prudent approach in selecting projects and have remarkable record in project execution which is reflected in high segment RoCE of >70%, industry leading margins of ~14% and strong cash flows. A shift towards ownership of annuity-based projects and wind assets was necessitated to deploy the strong cash flows of EPC business. The company's bet on wind assets has not worked as PLF and IRRs have fallen substantially, prompting it to decide on an exit from wind asset ownership. We believe the TBCB model of BOOT projects business will be a better IRR option (>15%) for the company and also provide a stable annuity income. We expect the company's consolidated net sales and net profit to post a CAGR of 20.3% and 26.1% respectively over FY15-18e. We initiate coverage on TEEC with a Buy rating and arrive at a SOTP-based target price of Rs640 (FY18e basis).

Prudent player in EPC – generates industry-leading margins and strong cash flow

TEEC generates industry-leading operating margin of ~14% and high operating cash flows based on the prudent practice of choosing orders selectively, focusing on complex extra high voltage jobs and scoring over competition on the execution front. PGCIL continues to be the largest client for the company (~47% of order book as of Dec 31, 2015). Certain SEBs like Bihar, Rajasthan and Andhra Pradesh also contribute substantially to the order book. TEEC prefers to work with limited set of clients as reflected in its top five clients accounting for almost 89% of the existing order backlog. It is actively participating in solar park EPC orders, which have an execution time of less than six months and faster payment cycle. Although these orders will come with lower margins, TEEC prefers the option of faster turnaround of working capital in these orders. During FY13-15, the company's EPC business posted a CAGR of 14%, while improving the operating margin from 11.1% in FY13 to 14% in FY15. Strong order backlog of Rs19.5bn and a healthy order pipeline gives the company visibility over the next two years. We expect the EPC business to register a CAGR of 24% during FY15-18e , with operating margin being maintained ~14%.

Asset ownership model – exit from wind business imminent, BOOT is way forward

TEEC's wind assets of ~162mw continue to suffer from power evacuation issues, resulting in IRRs declining to 10-11%. In the past one year, the company has been able to sell only 55mw, reflecting subdued market conditions. We expect the sale of remaining 162mw to fetch not more than Rs50/mw (~book value). Hence, we expect the company to deploy the resultant cash flows into the burgeoning market of BOOT projects with IRRs of ≥15%.

Valuation and view

We value the company using SOTP valuation, assigning a PE of 15x FY18e to the company's EPC business based on high growth, superior operating matrix and market leadership position in the substation segment. We value Transco assets at 1.5x P/BV and wind assets/cash at P/BV of 1x to arrive at a target price of Rs640, an upside of 20% from the current levels.

FINANCIALS (CONSOLIDATED)

Profit & Loss Statement

YE: Mar (Rs mn)	FY14	FY15	FY16e	FY17e	FY18e
Net Revenues	7,029	7,875	10,125	11,878	13,696
% growth	1.5	12.0	28.6	17.3	15.3
- Op. Expenses	5,159	5,858	7,946	9,459	11,023
EBITDA	1,870	2,017	2,179	2,418	2,673
EBIDTA Margin (%)	26.6	25.6	21.5	20.4	19.5
- Interest Expenses	454	431	397	358	192
- Depreciation	667	603	624	580	593
+Other Income	120	202	202	202	202
- Tax	38	186	245	303	376
Effective Tax Rate (%)	4	16	18	18	-
PAT	830.4	998.2	1,114.9	1,378.9	1,714.0
+/- Extraordinary Items	12.0	126.0	-	-	-
+/- Minority Interest	12.0	12.0	12.0	12.0	12.0
Reported PAT	806	860	1,127	1,391	1,726
Adj. FDEPS (Rs/Share)	14.1	15.1	19.7	24.4	30.2
Adj. FDEPS growth (%)	(27.7)	6.7	31.0	23.4	24.1

Source: Company, Systematix Institutional Research

Balance Sheet

YE: Mar (Rs mn)	FY14	FY15	FY16e	FY17e	FY18e
Share Capital	114	114	114	114	114
Reserves & Surplus	8,257	9,033	9,930	11,090	12,586
Net Worth	8,371	9,147	10,044	11,204	12,700
Minority Interest	193	199	199	199	199
Total Debt	6,077	5,649	4,967	4,543	4,138
Other liabilities	523	192	192	192	192
Capital Employed	15,163	15,187	15,402	16,138	17,228
Net Fixed Assets	10,729	10,248	7,573	7,243	6,900
Investments	681	747	747	747	747
- of which liquid	-				
Net Working Capital	3,272	3,946	4,486	5,223	5,860
Cash and Bank Balance	481	247	2,596	2,925	3,721
Capital Deployed	15,163	15,187	15,402	16,138	17,228
Net Debt	4,110	5,402	2,372	1,618	416
WC Days	31	85	89	89	89
Book Value (Rs/sh)	147	160	176	196	222

Source: Company, Systematix Institutional Research

Cash Flow

YE: Mar (Rs mn)	FY14	FY15	FY16e	FY17e	FY18e
PAT	806	860	1,127	1,391	1,726
+ Non Cash Items	667	603	624	580	593
Cash Profit	1,473	1,463	1,751	1,971	2,319
- Incr/(Decr) in WC	(629)	(674)	(540)	(737)	(636)
Operating Cash Flow	845	790	1,211	1,234	1,683
- Capex	(360)	(122)	2,050	(250)	(250)
Free Cash Flow	485	668	3,261	984	1,433
- Dividend	176	230	230	230	230
+ Equity Raised	41	147	-	-	-
+ Debt Raised	(200)	(427)	(682)	(424)	(405)
+Investments	(65)	(66)	-	-	-
+ other CL	(323)	(325)	-	-	-
Net Cash Flow	(237)	(234)	2,349	329	797
+ Opening Cash	718	481	247	2,596	2,925
Closing Cash	481	247	2,596	2,925	3,721

Source: Company, Systematix Institutional Research

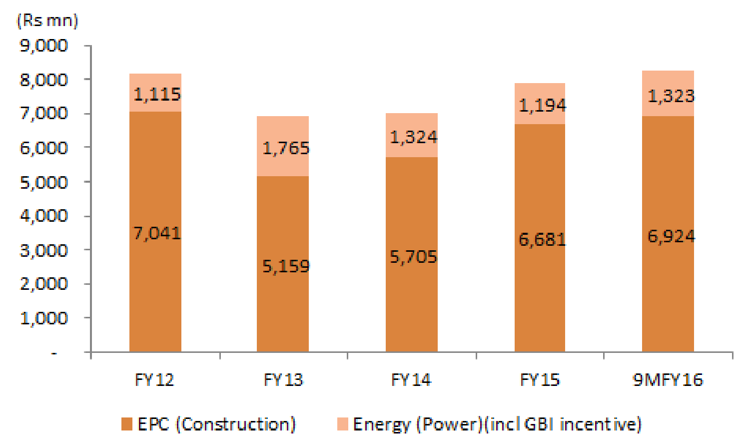
Ratios

YE: Mar	FY14	FY15	FY16e	FY17e	FY18e
P/E(x)	37.9	35.5	27.1	22.0	17.7
P/CEPS(x)	20.7	20.9	17.4	15.5	13.2
Mcap/Sales	4.3	3.9	3.0	2.6	2.2
EV/EBIDTA(x)	17.1	15.8	14.7	13.2	12.0
RoE(%)	10.2	10.0	11.6	13.0	14.3
RoCE(%)	8.3	8.7	9.3	10.7	11.5
Fixed Asset Turnover (x)	0.7	0.8	1.3	1.6	2.0
Dividend Yield (%)	2.7	1.0	1.0	1.0	1.0
Dividend Payout (%)	21.8	26.8	20.4	16.6	13.4
Debt/Equity(x)	0.7	0.6	0.5	0.4	0.3
Debtors (days)	107.8	169.0	170.0	170.0	170.0
Revenue Growth (%)	1.5	12.0	28.6	17.3	15.3
PAT Growth (%)	(27.7)	6.7	31.0	23.4	24.1
EBIDTA Growth (%)	(17.6)	7.9	8.0	11.0	10.5
EPS Growth (%)	(24.1)	(27.7)	6.7	31.0	23.4

Source: Company, Systematix Institutional Research

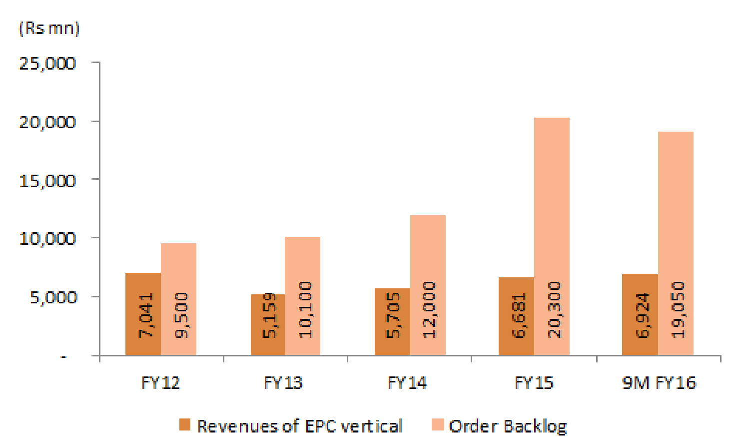
Charting the story

Chart 1: EPC segment posts consistent growth



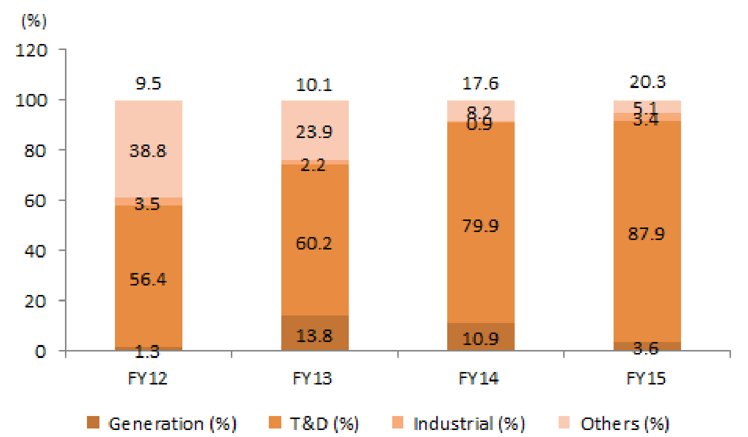
Source: Company, Systematix Institutional Research

Chart 2: Healthy order addition in the past two years



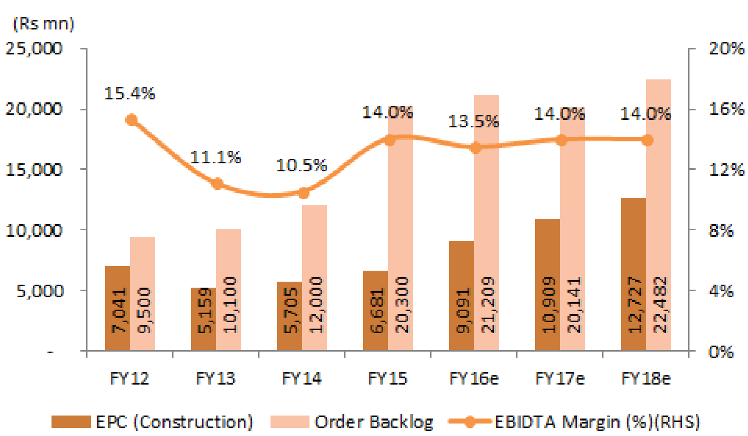
Source: Company, Systematix Institutional Research

Chart 3: Order book breakup – tilted towards T&D



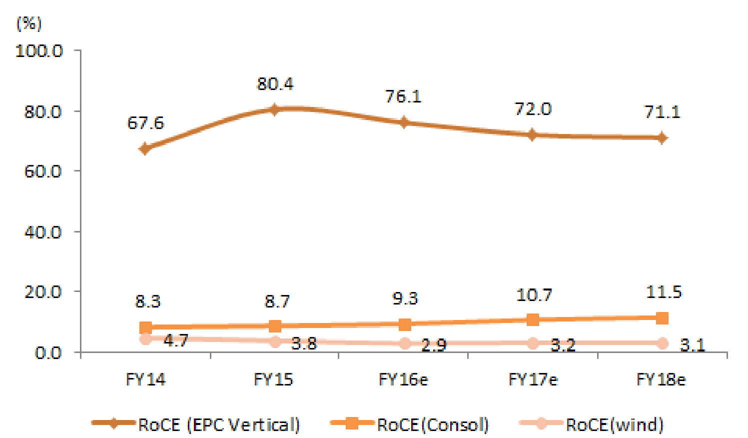
Source: Company, Systematix Institutional Research

Chart 4: Healthy order book to drive execution momentum



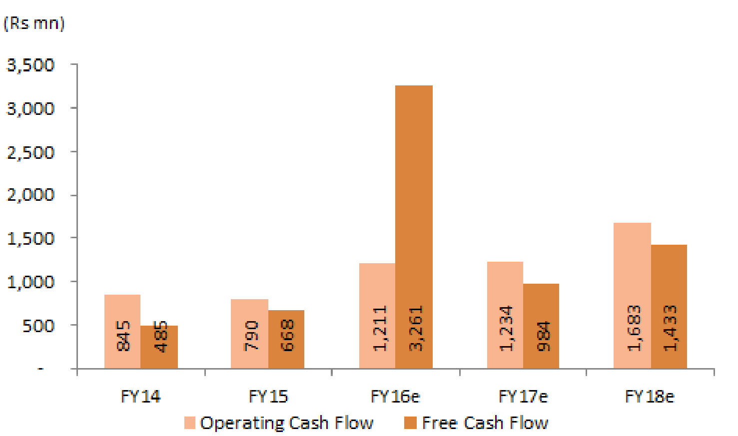
Source: Company, Systematix Institutional Research

Chart 5: Return ratios far superior to peers



Source: Company, Systematix Institutional Research

Chart 6: EPC business continues to generate strong cash flows



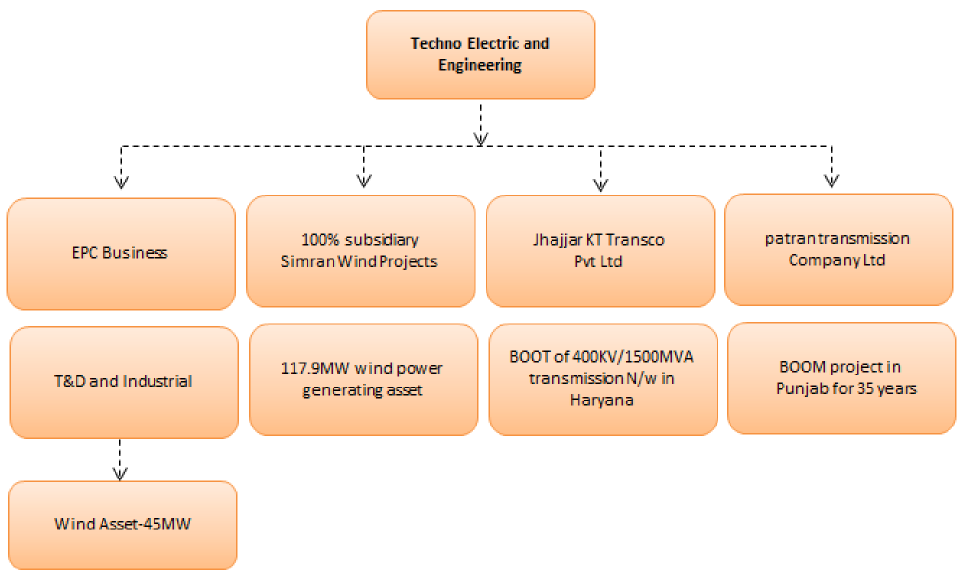
Source: Company, Systematix Institutional Research

Company overview

With over three decades of experience in EPC business, TEEC has an enviable position in the Indian power sector, with a presence across the entire power sector value chain -- generation, transmission and distribution. In generation, though the company has the capability to set up captive power plants up to 250mw, it is focusing only on specific areas like switchyards. In T&D, 765kv substation projects are its forte, besides distribution projects. Thus, we believe TEEC is favourably placed to tap opportunities across the entire power value chain. On the industrial front, through a tieup with Canmec Industriel (Canada), the company has a presence across fire fighting and fuel oil systems. TEEC ventured into BOOT business in 2010 and currently has two projects, with plans to add at least one BOOT project every year. It chooses projects with a higher proportion of substation EPC business to recover the equity investments through EPC job margins. BOOT projects with expected IRRs of 15% are also being bid due to the better investment option compared to expansion into unrelated space or paying out dividends.

With an aim to derive tax incentives, TEEC ventured into the wind business in 2009 by acquiring a plant of 45MW from Suzlon and added another 165MW in a brownfield expansion. However, power evacuation issues in Tamil Nadu have increased over the years, leading to PLFs declining below 20% and IRRs to 10-11%. Thus, the company decided to exit the business, sold 44.45mw in May 2015, and is on the lookout for a buyer for the remaining 163mw of wind assets.

Chart 7: TEEC's organization setup



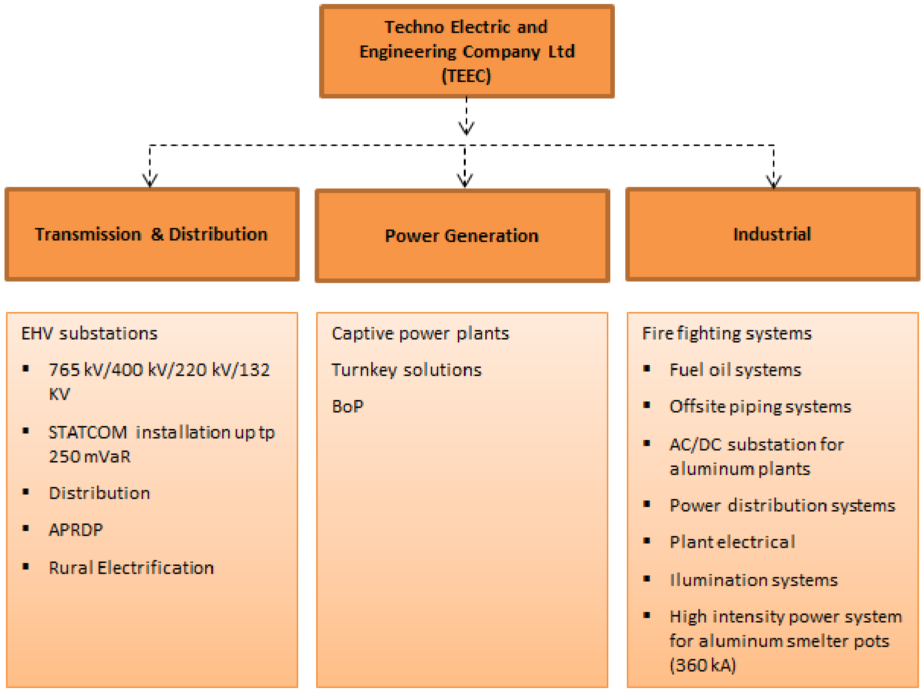
Source: Company, Systematix Institutional Research

Segmental analysis

A) EPC business

TEEC (established in 1963) entered the power transmission and distribution segment in 1980 and the power generation segment in 2009. The company is regarded for its expertise in the fields of heavy engineering and light construction across the country's power generation, transmission and distribution segments. TEEC has provided solutions to nearly half of India's installed thermal and inter-regional transmission providers and catered to customers like NTPC, PGCIL, BHEL among others.

Chart 8: TEEC's scope of work



Source: Company, Systematix Institutional Research

The company has executed more than 315 projects across India leading to FY14-15. It employs 382 professionals (including engineering and management graduates and post graduates) -- the core engineering team possesses a cumulative industry experience of more than 30 years as of March 31, 2015.

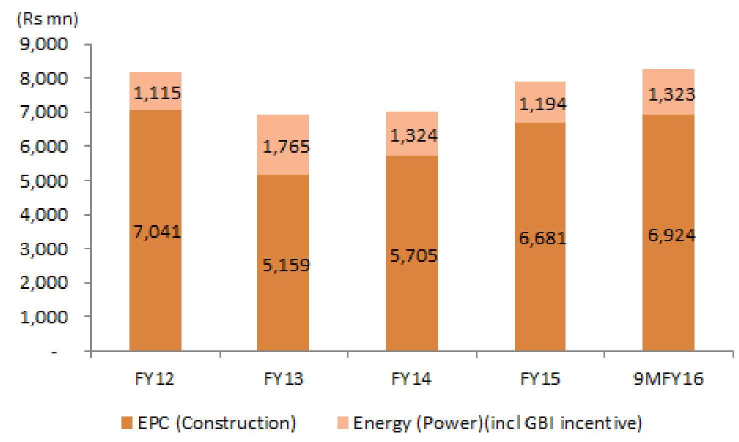
Competent team

TEEC's 135-member engineering team possesses an average industry experience of more than 25 years. The company's areas of competence comprise design, construction, project management, procurement, quality assurance, business development and marketing and financial management. TEEC has a track record of timely project completion, resulting in faster realisations with multiple instances of completing the projects before time. It has implemented zero-defect projects within the timeframe repeatedly.

Enduring relationships

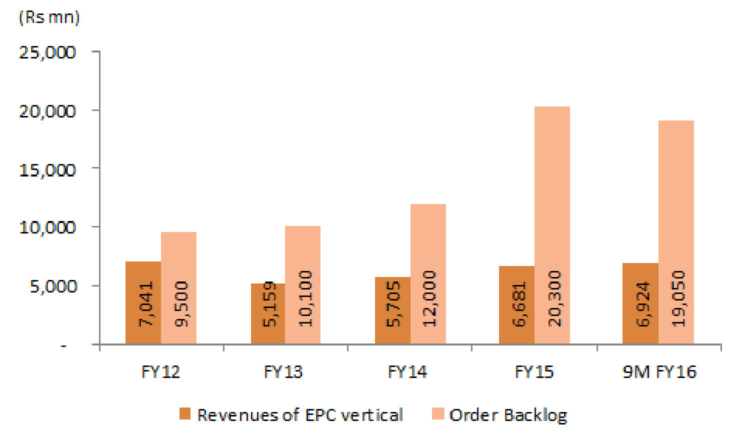
The company forged longstanding relationships with a family of 1,500 vendors, resulting in timely project completion.

Chart 9: EPC segment posts consistent growth



Source: Company, Systematix Institutional Research

Chart 10: Healthy order addition in the past two years



Source: Company, Systematix Institutional Research

Table 1: Order book breakup

Order book details	FY12	FY13	FY14	FY15
Generation (%)	1.3	13.8	10.9	3.6
T&D (%)	56.4	60.2	79.9	87.9
Industrial (%)	3.5	2.2	0.9	3.4
Others (%)	38.8	23.9	8.2	5.1
Order backlog (INR bn)	**9.5**	**10.1**	**17.6**	**20.3**

Source: Company, Systematix Institutional Research

TEEC played a vital role in India's power sector development due to working relationships with clients like NTPC, PGCIL, BHEL and oil refining PSUs. TEEC has also been a part of more than 50% of NTPC projects in various capacities and was associated with prestigious projects of other marquee clients.

Table 2: Tilted towards T&D – order backlog composition as of Dec 31, 2015

Name of the client	Amount (Rs mn)	% of total
PGCIL	8,900	46.72
North Bihar Power Distribution Ltd	2,825	14.83
NTPC	2,130	11.18
Rajasthan Rajya Vidyut Prasaran Nigam Ltd	1,545	8.11
Bihar State Power Transmission Ltd	1,510	7.93
Patran Transmission Co Ltd	780	4.09
APTRANSCO	505	2.65
Meja Urja Nigam	320	1.68
Others	535	2.81
Total	19,050	100

Source: Company, Systematix Institutional Research

For the past few years, the company's order book tilted more towards T&D projects, which constituted as much as 90% of the total order book. The shift has been due to cashing on the T&D orders traction on one hand and a slowdown in generation and industrial sectors on the other. PGCIL continues to be the largest client for TEEC (~47% of order book as of December 31, 2015). Certain SEBs like Bihar, Rajasthan and AP also contribute substantially to the order book.

Client concentration high at 89% for top 5 clients – a conscious effort

TEEC always had a selective approach to bid for orders, playing to its strength of choosing highly technical projects. The company repeatedly aims to leverage its strong competence in complex substation projects, which would enhance its scope of work and increase margins. TEEC bids for projects either funded by PGCIL or a multilateral/bilateral project of SEBs to mitigate the risk of delayed payment or risks arising from the cancellation of awarded projects.

As of Dec 31, 2015, top five clients accounted for 89% of the order backlog of Rs19.5bn. The ratio has been similar for the past three to four years, which indicates the company's preference to work with smaller set of clients. Pertinently, it also shows that clients have a greater comfort in working with TEEC by giving newer orders.

Leader in EHV space amongst Indian peers

Table 3: Share in PGCIL orders during 12th plan

Company	FY13	FY14	FY15	FY16	12th plan till date
Techno Electric	3.4%	9.5%	3.7%	10.6%	6.8%
Bharat Heavy Electricals Limited (BHEL)	0.0%	4.7%	6.2%	6.0%	4.7%
Crompton Greaves Ltd (CGL)	8.2%	4.2%	0.0%	0.0%	2.3%
Kalpataru Power Transmission Ltd (KPTL)	0.0%	1.1%	2.3%	1.1%	1.3%
KEC International Ltd	3.0%	0.0%	0.0%	0.0%	0.5%
Larsen & Toubro Limited	27.3%	0.0%	0.0%	0.0%	5.1%
European players(ABB, Alstom T&D,Siemens)	17.5%	16.1%	14.5%	13.4%	15.0%
Chinese players	29.8%	30.2%	36.5%	31.0%	32.4%
South Korean player-Hyosung	2.8%	33.6%	26.6%	28.5%	24.1%

Source: Company, Systematix Institutional Research

PGCIL is likely to incur its stated capex of Rs 450bn over FY16 and FY17 respectively. While the target for PGCIL for the 13th plan is Rs 1200bn to be spent over FY17-22.

North eastern corridor – location and technical advantage to TEEC

PGCIL has been entrusted with the task of building sub-transmission systems of 220/132kv over three years in the six states of North East India. The terrains are difficult and the award is likely to come to the player with highest quality. We believe TEEC has an edge in bagging orders from North East due to its strong technical competence in carrying out such jobs and aided by the proximity to location compared to other EPC players.

Green Energy Corridors: leveraging Statcom and EPC knowledge

Keeping up with the target of adding 100GW of solar power and 75GW of wind power by 2020, the power ministry has appointed PGCIL as the nodal agency to ensure the setting up of transmission infrastructure required to evacuate power. PGCIL is implementing the "Green Energy Corridors" to facilitate the integration of large scale renewable generation in the states of Gujarat, Rajasthan and Tamil Nadu into the ISTS grid along with other control infrastructure. These corridors comprise of establishment of 765/400kv pooling substations and 765kv d/c and 400kv d/c lines comprising intra-regional and its strengthening. In the second phase, work on the Green corridors will be extended to Maharashtra, Andhra Pradesh and Madhya Pradesh.

Exciting new opportunities

We believe exciting opportunities exist within the EPC space which can grow multifold within a few years. Among them, EPC of Statcom and Solar parks are the two verticals which are on the growth path and could be significant opportunities:

A) Statcom

Static Synchronous Compensator (Statcom) represents one of the most exciting opportunities in India's transmission space, mainly due to the government's ambitious target on renewable power capacity addition of close to 175gw till 2020. Renewable power being unstable needs a STATCOM to maintain the stable voltage even if the current fluctuates. Inefficient power management can result in high network losses, network overloading, unacceptable voltage levels, voltage inconsistency and even power outages. STATCOM systems offer rapid response to systemic malfunctions, ensures improved voltage and power system stabilisation, enhances reliability, real and reactive power flow control and increases power transfer limits.

The government plans to install 50 STATCOM of ~Rs80bn over a period of three to five years. TEEC emerged as the first service provider to win comprehensive Statcom orders aggregating Rs2.7bn at Solapur, Satna and Aurangabad jointly with the Chinese company, Rongxin. This successful order will serve as a formidable prequalification credential for TEEC to enjoy a head start towards acquiring more and larger orders going forward. L&T has emerged as a competitor for TEEC after winning STATCOM order at Kunta Substation in Andhra Pradesh from PGCIL.

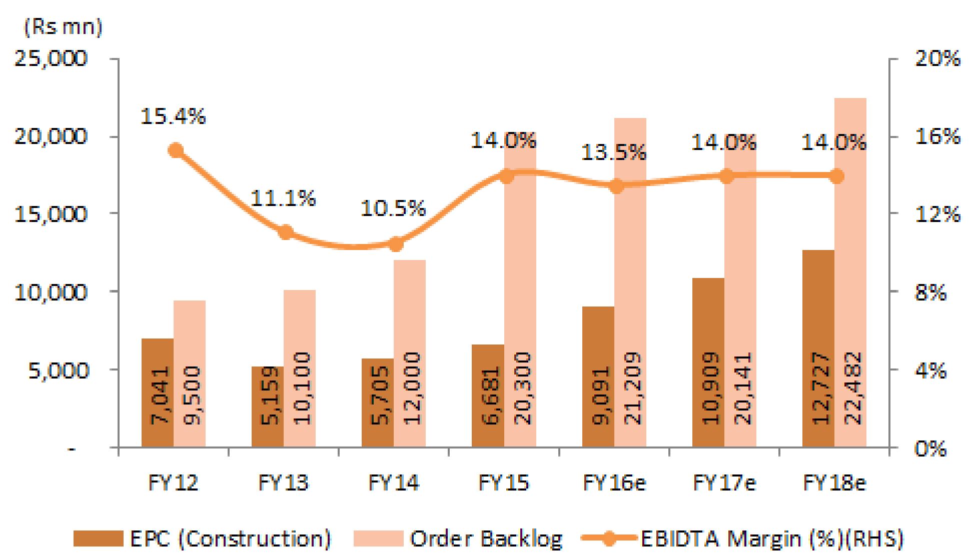
B) Solar parks

TEEC is also in the fray to execute EPC of solar projects. Though these projects would be below margin compared to its core substations EPC business, the amount of work order is more and the faster execution time of 6-9 months will lead to higher asset turnover, thus maintaining the return ratios. The company has bid for NTPC's first batch of 750mw solar park in Tanda. If successful, TEEC is likely to bag orders worth Rs7-8bn in 1QFY17e through solar business. NTPC is planning to bid out at least 10 such parks in the near term, thus presenting an enormous opportunity for the company.

Ministry of New and Renewable Energy (MNRE) is also targeting setting up of least 25 Solar Parks in different parts of the country with a target of over 20,000 MW installed capacity of solar power in a span of 5 years from 2014-15 to 2018-19.

TEEC would work with only top tier solar power developers with strong balance sheet and select projects with financial closure. Noting the aggression in capacity addition facilitated by various state governments and the Centre, the sector presents opportunities which can take TEEC's revenue to a different scale.

Chart 11: Execution momentum to continue, aided by healthy order booking



Source: Company, Systematix Institutional Research

Opening order backlog for FY16 was at Rs20.5bn, strongest in the past 5 years. Even though 9MFY16 order booking has been lower at Rs5.6bn, we believe award of orders in 4QFY16 from PGCIL/SEBs and from solar developers in 1QFY17 will shore up the order backlog. We expect company's EPC division to post revenue CAGR of 24% during FY15-18e. As the company continues to move up the value chain in EPC segment with more orders in 765kV and STATCOM sector, margins are expected to remain stable around 14% during FY15-18e despite increasing proportion of low margin solar business.

Foray into BOOT projects – steady revenue, better deployment of cash are the motives

TEEC ventured into BOOT segment to better utilise the cash flow generated from the EPC business. The aim was also to bid for projects where substations' EPC portion is substantially higher, thereby recovering the equity contribution from EPC business' margin. TEEC does not bid for projects with higher transmission line component or where the substations' EPC part does not involve complexity. The company bagged two projects in BOOT space in Haryana and Punjab respectively. As the government incrementally adapts to TBCB, TEEC expects to garner at least one project worth Rs2bn every year. Moreover, when the company is able to sell the wind energy assets, the resultant cash is expected to be deployed in BOOT projects after debt repayment. As of Dec 31, 2015, TEEC had Rs3bn cash and investments on book, providing a cushion for aggressive play in BOOT projects. It would not be a long-term investor in these projects as it expects to monetise the assets for a right price.

Table 4: Investments made in BOOT assets

	Jhajjar	Patran
Total cost of the project	4440	2,000
- Equity Contribution	760	500
- Debt	2,760	1,500
- VGF	920	-
TEEC's share	49%	100%
Tariff	Rs 540mn in first year; Fixed: 85%, Escalable: 15%	Rs 220mn in first year; Fixed: 97%, Escalable: 3%

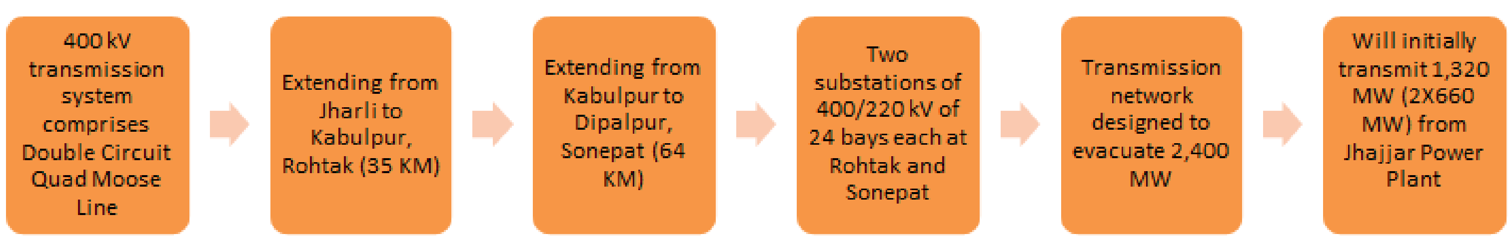
Source: Company, Systematix Institutional Research

1) **Jhajjar KT Transco**

TEEC emerged as the first successful network bidder in Jhajjar project awarded by Haryana in 2012 with a viable gap funding from the Centre. Kalpataru Power Transmission and Techno Electric formed a 51:49% (KPTL-TEEC) joint venture to design the transmission network to evacuate 2,400mw from the Jhajjar plant. The 400kv transmission system comprises of a double circuit quad moose line that extends from Jharli to Rohtak (35kms) and extends to Sonepat (64kms). It comprises of two substations of 400/200kv of 24 bays each at Rohtak and Sonepat.

The project will generate annual revenue of Rs540mn with the DBFOT arrangement spanning over 25 years (extendable by 10 years). The terminal value to be derived from this project is 60 months of revenue (following 25 years of concession period) in case the contract is not extended.

Chart 12: Jhajjar BOOT – first project to receive VGF

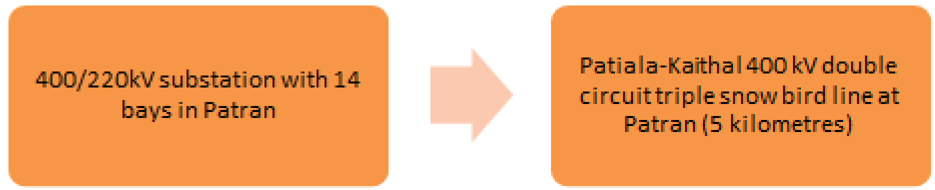


Source: Company, Systematix Institutional Research

2) Patran project

The Rs2bn project under BOOM transmission network possesses an evacuation capacity of 1,000MVA. The project was bagged from PFC Consulting Ltd and is likely to be completed by May 2016. The EPC opportunity for TEEC in the project is Rs1,750mn and the expected revenue to O&M agency (TEECL) is Rs200mn annually. Total revenue from this project is estimated at Rs10bn over the entire concession period of 35 years.

Chart 13: High content of EPC portion



Source: Company, Systematix Institutional Research

Wind business: Proving to be a drag on overall business

Table 5: Wind assets description

	Techno Electric	Simran Wind Project Ltd	
Capacity	45 MW	6 MW	111.90 MW
Date of Acquisition/Commissioning	During 2009-10	During 2009-10	March 31, 2011 - February 24, 2012
Location	Karnataka (12 MW) and Tamil Nadu (33 MW)	Karnataka	Tamil Nadu (111.90 MW)
No. of turbines	30 turbines at 3 wind farms	4 turbines at 2 wind farms	67 turbines at 2 wind farms
Capacity	30 turbines * 1.5 MW each	4 turbines * 1.5 MW each	48 turbines * 1.5 MW each 19 turbines * 2.1 MW each
PLF	18% - 26%	19% - 26%	19% - 26%
Tariff	INR 3.40 (Karnataka) and INR 3.39 (Tamil Nadu)	Preferential tariff – INR 3.40	APPC tariff – INR 2.63 (TN) for 111.90 MW
O&M	Free for first 5 years; 5% escalation from INR 1 mn/MW	Free for first 5 years; 5% escalation from INR 1 mn/MW	Free for first 4.5 years; 5% escalation from INR 1 mn/MW
CDM benefit	33 MW registered with UNFCC	-	111.9 MW registered with UNFCC
GBI benefit	-	-	111.9 MW registered with IREDA

Source: Company, Systematix Institutional Research

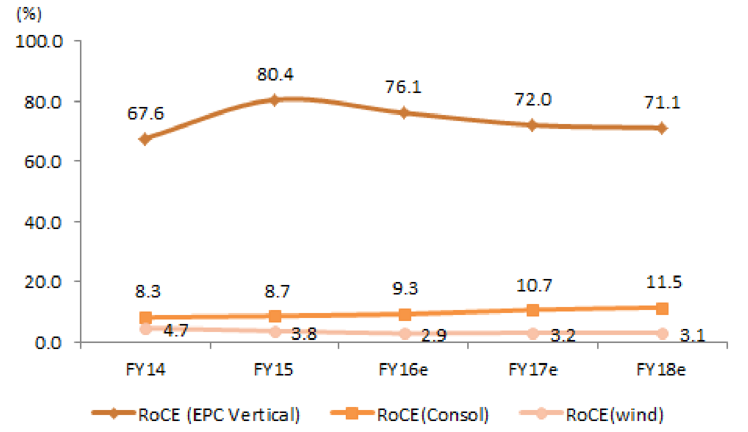
TEEC ventured into the wind business by purchasing 95mw wind assets from Suzlon on a slump sale basis in 2009 for Rs4.4bn. Subsequently, through a brownfield expansion, the company ramped up the portfolio of its wind energy assets by 112mw over the next four years, taking the total capacity to 207mw. The entire capacity is tied up with a long-term PPA with Tamil Nadu and Karnataka SEBs. Part of the capacity is tied up for benefits under generation-based incentives (GBI), renewable energy certificates (RE) and carbon credits. During 2012-13, the company was expecting to take the total wind capacity to 1,000mw.

However, within few years, TEEC started facing power evacuation issues, especially in Tamil Nadu, resulting in inefficient operations of wind mills. Hence, PLF fell to close to 20% and made the overall operation unviable and prompted the company to exit the wind power business completely. In the first round, TEEC sold wind assets of 44.45mw in Tamil Nadu in May 2015 for Rs2.15bn, almost recovering the investment made in building corresponding assets.

Also, the market for wind assets slowed down considerably, thus lowering the investors' risk appetite. TEEC expects a speedy resolution to the evacuation issue in Tamil Nadu which would lead to IRR expansion to a reasonable level of 15%. The company is expecting an EV of Rs8-9bn from the sale of balance wind assets, which we believe could be lower by 5-10%, considering the current market situation. Earlier, the company had guided for an asset sale of ~50mw in 4QFY16, which is more likely to be postponed to 1HFY17.

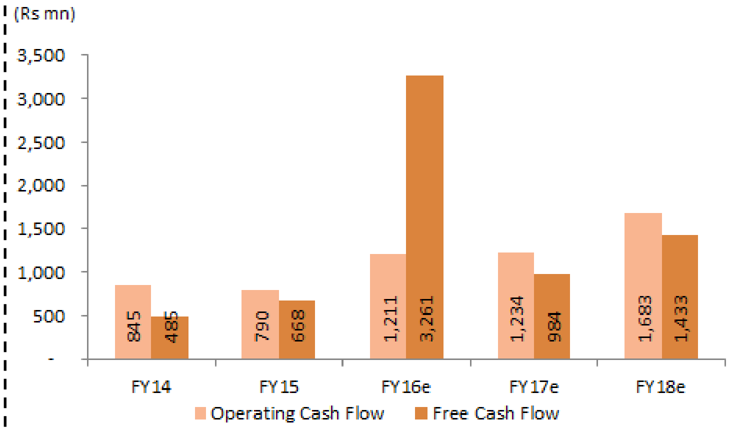
EPC business gets premium relative valuation

Chart 14: Return ratios far superior to peers



Source: Company, Systematix Institutional Research

Chart 15: EPC business continues to generate strong cash flows



Source: Company, Systematix Institutional Research

Wind energy business drags the overall RoCE for the company to single digits while actually EPC business has been making RoCE of over 70% consistently for last 4 years. We believe company's superior execution capabilities and working capital management for EPC business will continue to throw stronger free cash flows in between FY15-18e (FY16e cash flows is higher after accounting for sale of 45MW wind assets for Rs 2.15bn).

We value the company using SOTP valuation, assigning PE of 15x on FY18e basis to company's EPC business, valuing the Transco assets at 1.5x P/BV, and the wind assets/cash at P/BV of 1.0x to arrive at a target price of Rs640, an upside of 22% from the current levels.

Table 6: SOTP - based valuation

	Equity Invested/ Book Value	Net Profits (FY18e)	Target P/E Multiple (FY18e)	Target P/BV Multiple (FY18e)	Valuation (Rs mn)	Valuation/ share of TEEC	Remarks
1)Techno Electric (EPC business)		1,726	15		25,890	453	RoCE >70% to be maintained, revenue growth of 24% CAGR with 14% EBIDTA margin over FY15-18e
2)TEEC Transmission Assets							
- Jhajjar	376			1.5	564	9.9	Asset operational since Mar 13, earning Rs 540mn annuity
- Patran	500			1.5	750	13.1	Asset will be operational from May 16
3) Simaran Wind Energy	5,800			1	5,800	101.6	Market not conducive for sale of wind assets. Last transaction happened closer to book value
4) Cash & cash equivalent	3,563			1	3,563	62.4	
Total		**TEEC+ Transmission BOT + Wind Assets + Investments Valuation**			**640**		

Source: Company, Systematix Institutional Research

Skipper

1 April, 2016

Efficient operations result in industry-leading operating metrics

INITIATING COVERAGE

Sector: Power T&D	**Rating: Buy**
CMP: Rs134	**Target price: Rs182**

Stock Info

Sensex/Nifty	25,342/ 7,738
Bloomberg	SKIPPER IN
Equity shares (mn)	102.3
52-wk High/Low	220/ 116
Face value	10
M-Cap	Rs14bn/ $207mn
3-m Avg volume	$1.1mn

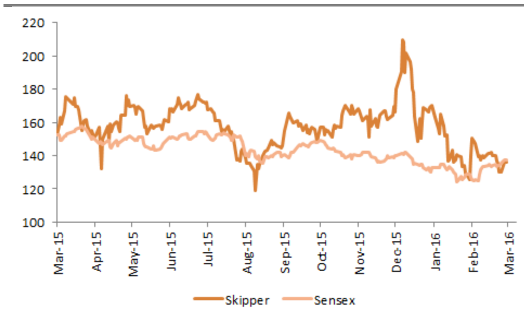
Financial Snapshot (Rs mn)

Y/E March	FY16e	FY17e	FY18e
Sales (Rs mn)	14,271	16,986	19,879
Net Profit (Rs mn)	923	1,022	1,246
EPS (Rs)	9.0	10.0	12.2
Growth (%)	3.5	10.8	21.9
PE (x)	14.9	13.4	11.0
EV/EBIDTA (x)	7.1	6.2	5.2
P/B (x)	3.5	2.8	2.2
RoE(%)	26.4	22.9	22.2
RoCE (%)	30.3	28.4	28.1
Dividend Yield (%)	0.1	0.1	0.1
Net Gearing (x)	0.8	0.6	0.4

Shareholding pattern (%)

	Dec '15	Sep '15	Jun '15
Promoter	72.4	72.4	72.4
–Pledged	-	-	-
FII	1.1	-	-
DII	0.0	-	-
Others	26.5	27.6	27.6

Stock Performance (1-year)



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Skipper Ltd, the flagship company of SK Bansal group from Kolkata, is a leading player in the power transmission towers segment since more than two decades. The company has an edge over peers as 1) the only leading player with an integrated rolling mill facility, 2) has a locational advantage of being situated near the supplier, resulting in low cost operations and industry-leading operating margins. Orders bagged in Latin American markets worth Rs12.5bn in FY14 and FY15 have provided impetus to the order backlog, raising the overall order backlog to healthy levels of Rs25bn (Mar 15). We expect the company's engineering products (towers) business to post a CAGR of 11% over FY15-18e while the CPVC products and fittings business is likely to grow at a CAGR of 42% over FY15-18e as the company continues to add capacity & distributor across regions. Skipper's asset light model is expected to strengthen the fixed asset turnover from 3.8x in FY15 to 5.2x by FY18e, aiding to maintain an RoCE of ~28% during FY16e-18e. Despite the strong volume in both verticals (transmission towers and PVC), we expect the lower commodity prices to limit growth in overall net sales and net profit to 14% and 12% CAGR respectively during FY15-18e. We initiate coverage on Skipper with a Buy rating and a target price of Rs182 (PE of 15x FY18e).

Booming transmission tower segment, diversified customer base to drive growth

We expect Skipper to be a beneficiary of the expected Rs2tr capex on transmission towers during FY16e-22e. Reduced dependence on PGCIL and increasing exposure to private operators/SEBs augur well for the company's growth prospects. Diversification into international markets with Rs12.5bn order wins in Latin America will help the company to establish credentials in the booming markets of Latin America and Africa. Increasing proportion of TBCB orders augurs well for the company as developers tend to prefer larger established players for tower supply. Despite the strong volume CAGR of 17.2% during FY15-18e, we expect Skipper's net sales in engineering products division to post a CAGR of 16% in the same period due to lower commodity prices. The business is also getting impacted as a result of Skipper exiting the ERW pipes manufacturing business.

PVC business – smaller base and strong sourcing relationships to aid growth

Skipper is planning to increase the installed capacity in PVC pipes segment to 100,000tpa, from the current 39,000tpa, using an asset light model. The company has tied up with Sekisui, Japan to source CPVC compound and with Wavin, Netherlands for fittings, thus giving it a technical advantage in a highly competitive space. The PVC pipes industry is expected to clock a CAGR of 15-18% during FY15-18e, and Skipper being a more aggressive player (growing from a lower base) is expected to post a CAGR of 42% during the same period.

Lower commodity prices to restrict profit growth but margins to sustain

The company's inherent advantage of low cost operations and higher fixed asset turnover are expected to maintain the operating profit and RoCE at healthier levels of 15-16% and 28-29% respectively during FY16e-18e. On the other hand, lower commodity prices will result in net sales and net profit growth of 14% and 12% during FY15-18e, thereby restricting the advantage of strong volume growth in both verticals. We believe the recent correction in stock price gives the right entry opportunity. We value the stock at three year average one year forward PE of 15x. We initiate coverage on Skipper with a Buy rating and a target price of Rs182 on FY18e basis.

FINANCIALS (STANDALONE)

Profit & Loss Statement

YE: Mar (Rs mn)	FY14	FY15	FY16e	FY17e	FY18e
Net Revenues	10,752	13,469	14,271	16,986	19,879
% growth	15.7%	25.3%	6.0%	19.0%	17.0%
- Op. Expenses	9,549	11,179	11,888	14,319	16,758
EBITDA	1,203	2,290	2,383	2,667	3,121
EBIDTA Margin (%)	11.2	17.0	16.7	15.7	15.7
- Interest Expenses	685	704	741	852	949 -
Depreciation	151	220	244	266	284
+ Other Income	-	-	-	-	-
- Tax	98	474	475	527	642
Effective Tax Rate (%)	17	31	34	34	34
Adj.PAT	269.1	891.8	922.7	1,022.1	1,246.3
+/- Extraordinary Items	(0.2)	(2.6)	-	-	-
+/- Minority Interest	-	-	-	-	-
Reported PAT	269	889	923	1,022	1,246
Adj. FDEPS (Rs/Share)	2.6	8.7	9.9	10.0	12.2
Adj. FDEPS growth (%)	37	231	3.5	10.8	21.9

Source: Company, Systematix Institutional Research

Balance Sheet

YE: Mar (Rs mn)	FY14	FY15	FY16e	FY17e	FY18e
Share Capital	102	102	102	102	102
Reserves & Surplus	2,209	2,936	3,859	4,881	6,127
Net Worth	2,312	3,039	3,961	4,983	6,230
Minority Interest	-	-	-	-	-
Total Debt	4,062	3,431	3,707	4,260	4,745
Other liabilities	227	265	265	265	265
Capital Employed	6,601	6,734	7,933	9,508	11,239
Net Fixed Assets	3,468	3,547	3,704	3,837	3,804
Investments	21	31	31	31	31
- of which liquid	-	-	-	-	-
Net Working Capital	2,849	2,596	3,606	4,179	5,093
Cash and Bank Balance	263	561	593	1,461	2,312
Capital Deployed	6,601	6,734	7,933	9,508	11,239
Net Debt	3,799	2,870	3,114	2,799	2,433
WC Days	119	107	110	110	110
Book Value (Rs/sh)	23	30	39	49	61

Source: Company, Systematix Institutional Research

Cash Flow

YE: Mar (Rs mn)	FY14	FY15	FY16e	FY17e	FY18e
PAT	269	889	923	1,022	1,246
+ Non Cash Items	151	220	244	266	284
Cash Profit	420	1,109	1,166	1,288	1,530
- Incr/(Decr) in WC	(50)	254	(1,010)	(573)	(914)
Operating Cash Flow	370	1,363	156	715	616
- Capex	(321)	(299)	(400)	(400)	(250)
Free Cash Flow	49	1,064	(244)	315	366
- Dividend	-	-	-	(10)	(10)
+ Equity Raised	(18)	(168)	-	10	10
+ Debt Raised	86	(631)	276	552	485
Investments	(12)	(10)	-	-	-
+ other CL	31	37	-	-	-
Net Cash Flow	134	293	32	867	851
+ Opening Cash	128	263	561	593	1,461
Closing Cash	263	561	593	1,461	2,312

Source: Company, Systematix Institutional Research

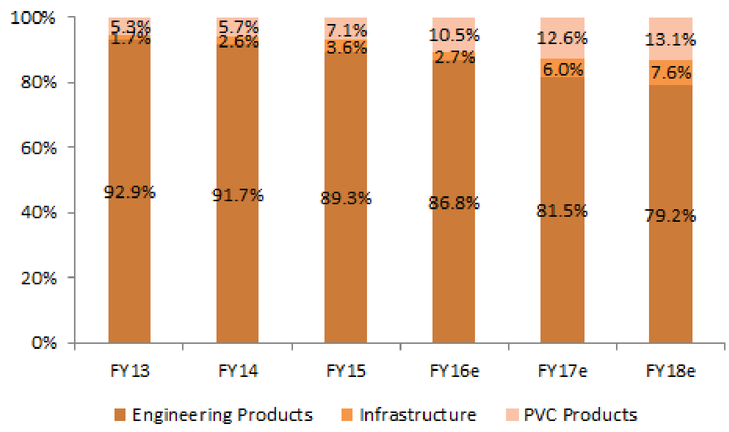
Ratios

YE: Mar	FY14	FY15	FY16e	FY17e	FY18e
P/E(x)	50.9	15.4	14.9	13.4	11.0
P/CEPS(x)	32.7	12.4	11.8	10.6	9.0
Mcap/Sales	1.3	1.0	1.0	0.8	0.7
EV/EBIDTA(x)	14.6	7.2	7.1	6.2	5.2
RoE(%)	12.3	33.4	26.4	22.9	22.2
RoCE(%)	17.0	32.2	30.3	28.4	28.1
Fixed Asset Turnover (x)	3.1	3.8	3.9	4.4	5.2
Divident Yield (%)	0.0	0.9	0.5	0.5	0.5
Dividend Payout (%)	-	15.0	15.0	15.0	15.0
Debt/Equity(x)	1.8	1.1	0.9	0.9	0.8
Debtors (days)	84.4	113.3	110.0	110.0	110.0
Revenue Growth (%)	15.7	25.3	6.0	19.0	17.0
PAT Growth (%)	43.8	232.1	3.2	10.8	21.9
EBIDTA Growth (%)	31.1	90.3	4.1	11.9	17.0
EPS Growth (%)	37.0	231.4	3.5	10.8	21.9

Source: Company, Systematix Institutional Research

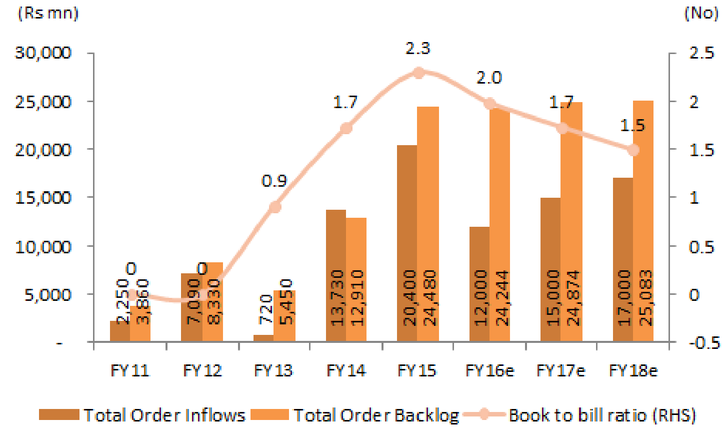
Charting the story

Chart 1: Towers will continue to be the mainstay of business



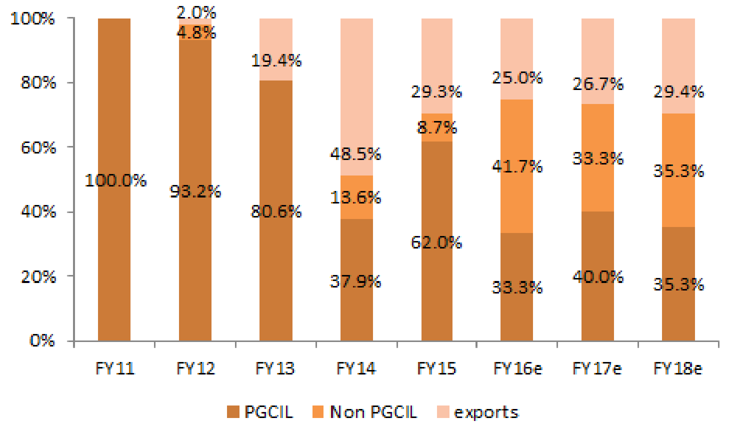
Source: Company, Systematix Institutional Research

Chart 2: Order volume growth strong, value getting impacted



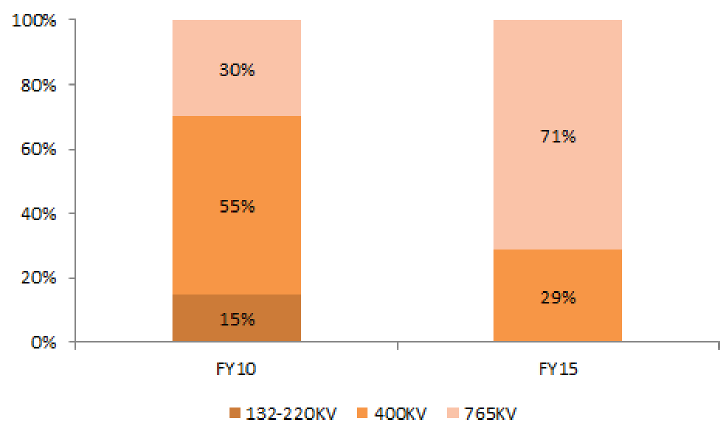
Source: Company, Systematix Institutional Research

Chart 3: Dependence on PGCIL for orders reduces



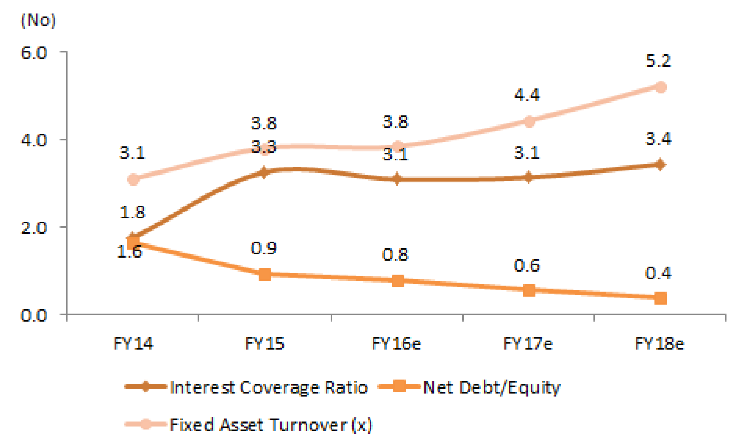
Source: Company, Systematix Institutional Research

Chart 4: Proportion of EHV towers increases



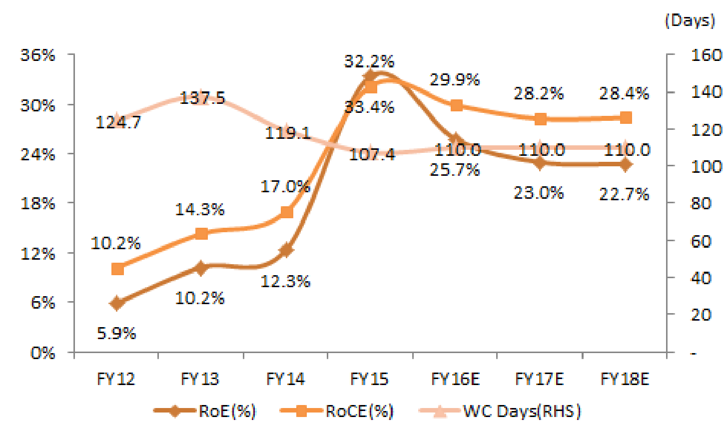
Source: Company, Systematix Institutional Research

Chart 5: D/E under control, asset turns improve



Source: Company, Systematix Institutional Research

Chart 6: Return ratios steadily move higher



Source: Company, Systematix Institutional Research

Company background

Skipper is a leading player with a core business of manufacturing power transmission towers, with an installed capacity of 175,000tpa near Kolkata. The company also manufactures towers for telecom, including monopoles and octagonal poles used in lighting of commercial areas. Skipper selectively takes EPC projects of laying power transmission lines. It ventured into the manufacturing of PVC pipes five years ago and has aggressively ramped up capacity to 41,000tpa. Skipper offers PVC and CPVC pipes along with fittings, which are entirely manufactured in-house. It is targeting to expand the transmission tower manufacturing facility by 15-20% every year, while the PVC pipes manufacturing capacity is expected to be ramped up to 100,000tpa by 2018.

Table 1: Manufacturing capacities location

	Engineering Products (tpa)	PVC Pipes & Fittings (tpa)
Uluberia – Kolkata	70,000	15,000
Unit 1 – Kolkata	69,000	
BCTL – Kolkata	36,000	
Ahmedabad		10,000
Guwahati		4,000
Sikandarabad, New Delhi		6,000
Hyderabad		6,000
Total	175,000	41,000

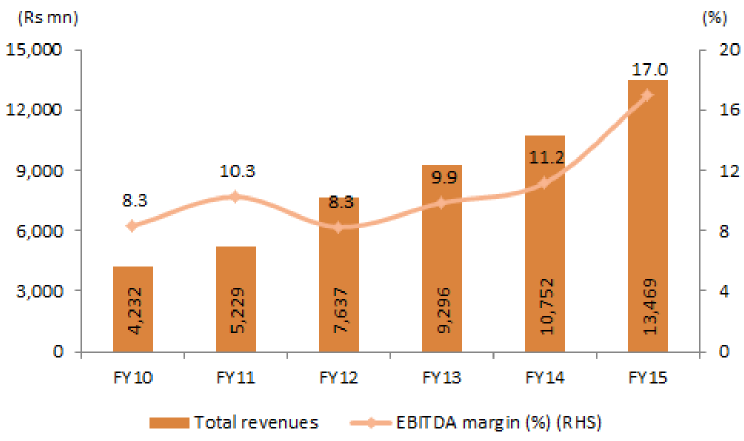
Source: Company, Systematix Institutional Research

Chart 7: Products profile

Source: Company, Systematix Institutional Research

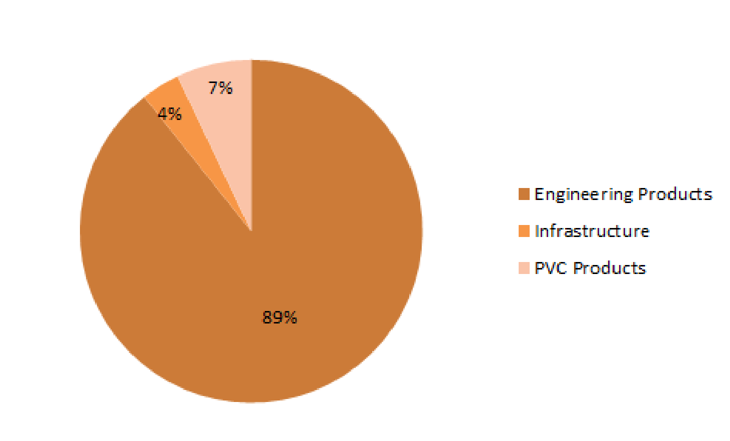
Business performance in the past 5 years

Chart 8: Consistent revenue growth with improving margins



Source: Company, Systematix Institutional Research

Chart 9: Revenue (FY15) - engineering products drives business



Source: Company, Systematix Institutional Research

Skipper posted revenue and net profit CAGR of 27% and 46% respectively during FY11-15. The company has the highest operating margin in peer group as the low cost operation and vertical integration increased margin from 8.3% in FY10 to 17% in FY15. Skipper also diversified, from being dependent on PGCIL for 100% of its order backlog in FY11, to derive as much as 38% of order backlog from exports and SEBs in FY15, and simultaneously grow the order book to Rs25bn in FY15, from Rs3.9bn in FY11.

Exports - led growth in order book

Skipper's order book posted a CAGR of 100% during FY13-15 as it received number of orders from PGCIL, SEBs and international clients. Pertinently, it reduced the dependence on PGCIL from 100% in 2011 to the extent of 62% in FY15. Over FY11-15, Skipper received few vital orders from select SEBs of Rs4bn. In FY14-15, the company received two large international orders worth Rs5.5bn and Rs4bn for the supply of EHV transmission towers to one of the largest transmission system operator in Latin America operating in Columbia, Peru, and Chile. Skipper won this order against international competition and without sacrificing the margins due to scale efficiency. The order is to be executed over 30 months and management stated that 50-55% of execution is complete.

Chart 10: Important orders won by Skipper

Order description

- Nellore Kurnul-365kms long 765kV transmission line executed by Tata Projects
- Completed supplies of 40,000mt to the prestigious ±800kV HVDC Bipole Biswanath Chariyali – Agra line, which was the first line to use ±800kV structures in India
- Multi-Circuit Towers (average tower weight more than 60mt) to Gaya-Kodarma T/L project

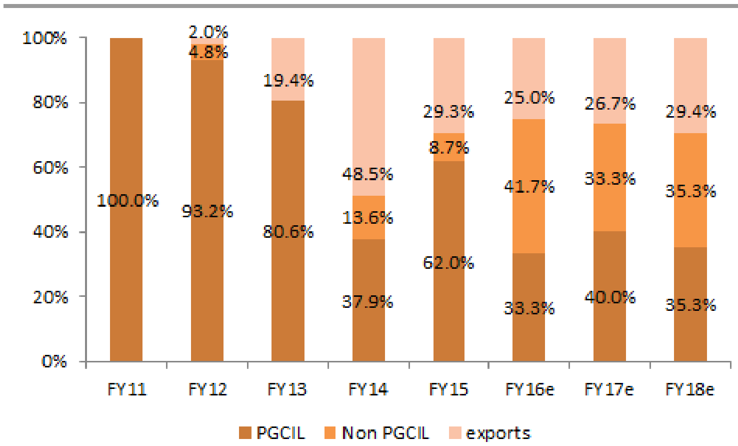
Source: Company, Systematix Institutional Research

Increasing proportion of 765kV orders: Limited competition enables higher margins

Over the last five years, the Indian transmission sector led by PGCIL, upgraded to 765kV voltage levels, in turn pushing all the vendors to upgrade their technological capabilities. Skipper has been at the forefront to adopt the 765kV technology (aided by the company's tie-up with Ramboll, Denmark for designing capabilities). Composition of Skipper's order backlog has changed drastically in favour of 765kV orders, accounting for 71% in FY15 from 30% in FY10. The 765kV transmission tower orders are an advantage for the company as the limited competition enables higher margins.

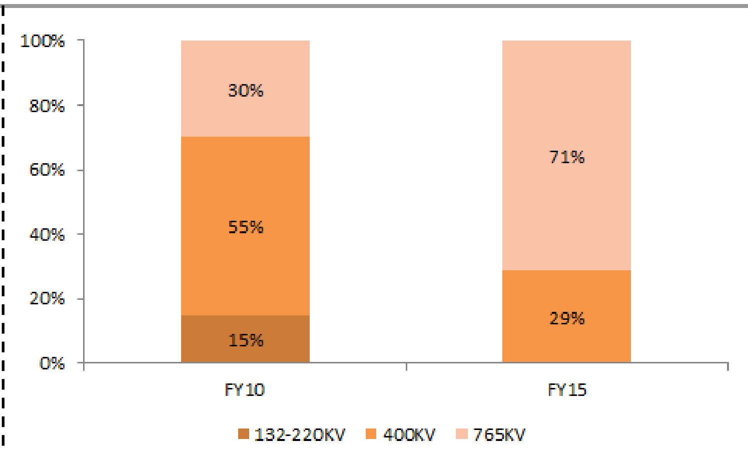
Order book composition:

Chart 11: Dependence on PGCIL reduces



Source: Company, Systematix Institutional Research

Chart 12: Proportion of EHV towers increases



Source: Company, Systematix Institutional Research

Large export order takes company into different league

Skipper made inroads into the Latin American markets (through a large export order), which is poised to witness investments of $380bn (incl North America) over FY14-30e. The Latin American market is mainly operated and controlled by private sector transmission system operators (TSOs) from North America and Europe. Plans for the development of power infrastructure are generally long term in nature and are taken up after the financial closure through large multilateral agencies/financial institutions. Skipper won the order from transmission sector operator, INSA, which is a dominant player in Latin America, especially in Columbia, Chile, and Peru.

Skipper won the order through a competitive bidding among 20 players. The company's low cost manufacturing advantage proved beneficial to win the order against Chinese, Korean and Russian competition. There is an inherent advantage in having the manufacturing facility in India as the galvanising operation comes under the 'Red colour' polluting norm and is not allowed to be operated in most developed nations, thereby limiting competition. As transmission projects have a life of more than 25 years, vendors are chosen carefully by utilities to ensure a high degree of stickiness.

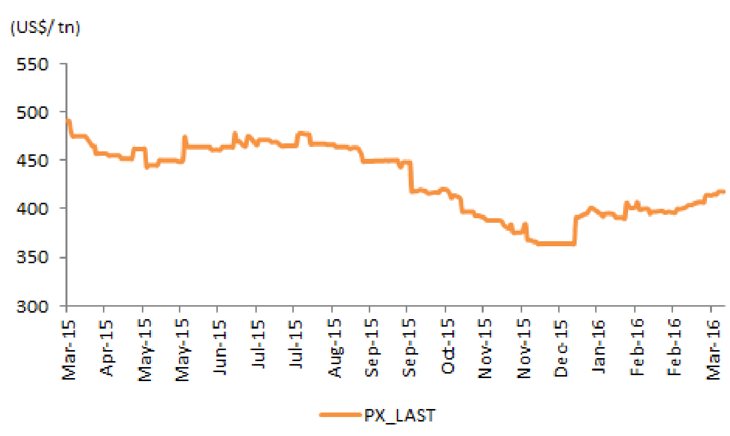
Skipper is also aggressively scouting for orders in the developing markets of Africa and it recently won an order for supply of transmission towers in Egypt for Rs1.7bn. We believe the exports market will play a significant part in the company's growth momentum during FY15-18e. We expect Skipper's order booking from exports market to remain steady ~Rs3-5bn, excluding the lumpy large orders.

Monopoles – tapping the nascent market

Monopoles are tubular structures which provide the ease of erection in areas where space is a constraint; saving up to 90% space compared to lattice towers. Skipper has a manufacturing capacity of 15,000mtpa under an existing setup in the current year for monopoles and plans to increase it to 40,000mtpa going forward to benefit from the 'first mover advantage'. Though the prices of monopoles are 60-70% higher compared to lattice towers, we believe as the usage of monopoles in India increases to the levels seen in Europe, prices would decline significantly and enable increased general use.

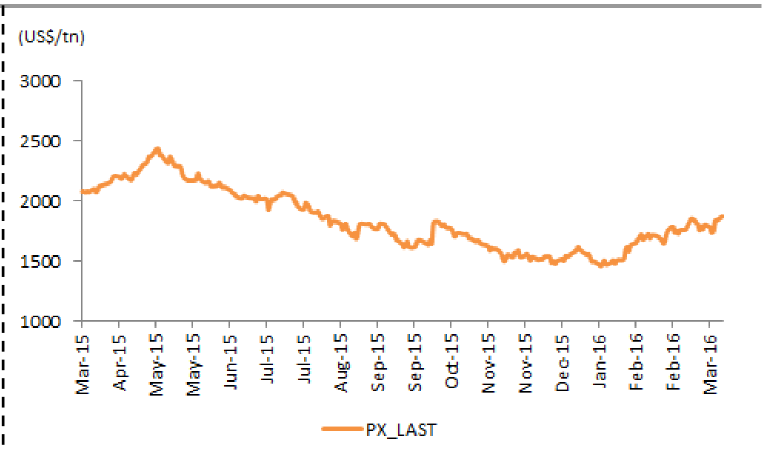
Impact of realisations on order book

Chart 13: US Midwest steel - index Futures



Source: Bloomberg, Systematix Institutional Research

Chart 14: LME Zinc – spot prices



Source: Bloomberg, Systematix Institutional Research

As steel and zinc account for ~63% and 9% of the selling price of tower, volatility in raw material prices tends to impact margins. In the domestic market, government utilities adopt a price variation clause in all orders and hence the company does not get impacted either way in the long term; short-term impact is a probability though. Export contracts are fixed priced and they tend to benefit the supplier in a falling commodity price scenario. Skipper won combined export orders worth Rs12bn in FY14 and FY15 which were fixed priced. The company always prefers to enter into 100% back-to-back forward contracts, thus hedging the entire currency risk and movement of zinc prices. Only steel as a raw material cannot be completely hedged due to the lack of perfect hedging options. As Skipper is set to execute at least 50% of the orders in the current year, the benefits from lower steel prices should accrue to the company.

However, the correction in commodity prices is expected to restrict its order flow growth in absolute terms. We incorporate zero increase in price realisation for transmission towers from now till FY18e-end. On volume terms, we expect the company to post a CAGR of 17.2% over FY15-18e and the order booking in value is expected to see a CAGR of only 16% during the same period.

Table 2: Order flow assumptions

(Rs mn)	FY11	FY12	FY13	FY14	FY15	FY16e	FY17e	FY18e	CAGR	Remarks
A) Order inflows										
- PGCIL	2,250	6,610	580	5,200	12,650	4,000	6,000	6,000	-22%	FY15 was an exceptional year in terms of order inflows from PGCIL. Minimum of Rs5bn worth of orders every year from FY16e-18e to maintain the growth momentum
- SEBs and Private	-	340	-	1,870	1,780	5,000	5,000	6,000	50%	Order inflows from SEBs/pvt sector is key to maintain the execution momentum
Total domestic order inflow	**2,250**	**6,950**	**580**	**7,070**	**14,430**	**9,000**	**11,000**	**12,000**	-6%	
% growth		208.9%	-91.7%	1119.0%	104.1%	-37.6%	22.2%	9.1%		
Export order inflow	**-**	**140**	**140**	**6,660**	**5,970**	**3,000**	**4,000**	**5,000**	-6%	Development of T&D in Latin America and Africa will drive the export order momentum. Regular order flow, rather than lumpy orders, should help maintain the pace of execution
% growth			0.0%	4657.1%	-10.4%	-49.7%	33.3%	25.0%		
Total order inflows	**2,250**	**7,090**	**720**	**13,730**	**20,400**	**12,000**	**15,000**	**17,000**	-6%	
% growth		215.1%	-89.8%	1806.9%	48.6%	-41.2%	25.0%	13.3%		
B) Order backlog										
Domestic order backlog	3,860	8,190	5,300	6,440	13,190					
% growth		112.2%	-35.3%	21.5%	104.8%					
Export order backlog	-	140	150	6,470	11,290					
			7.1%	4213.3%	74.5%					
Total order backlog	**3,860**	**8,330**	**5,450**	**12,910**	**24,480**	**24,228**	**24,842**	**25,035**	**1%**	Order backlog should stagnate at ~Rs25bn from FY16e-18e
% growth		115.8%	-34.6%	136.9%	89.6%	-1.0%	2.5%	0.8%		
Net revenue of engg products segment plus infra projects (ex engg product job work)	**-**	**-**	**5,964**	**7,502**	**10,670**	**12,252**	**14,386**	**16,807**		
				25.8%	42.2%	14.8%	17.4%	16.8%		
Book to bill ratio			0.91	1.72	2.29	2.00	1.70	**1.50**		The company needs to maintain the book-to-bill ratio at minimum 1.5x under every situation to sustain the growth momentum

Source: Company, Systematix Institutional Research

PVC pipes: Business to grow rapidly, margins below T&D business

The PVC pipes market in India is close to 1.7 million tpa, of which the organised sector contributes almost 60% share. The major players are Finolex Industries, Supreme Industries, Astral Polytechnic, Ashirwad Pipes and Prince Pipes.

Skipper entered the PVC pipes market five years ago, with an initial capacity of 12,000tpa in Uluberia plant and catering mainly to Eastern India. To aggressively expand to other parts of the country, the company adopted a strategy of adding capacity through an asset light model on leased premises. This reduces capex by ~50-60% as it invests only in machinery and operating expenses, thus saving a huge amount of capex by not investing in land. An asset light model will help in enhancing the return ratios and limit Skipper's over-exposure to any particular region. It has aggressive plans to increase the installed capacity to 100,000tpa by 2018 -- has already increased the capacity to 41,000tpa as of February 2016.

Table 3: Top players in PVC pipes segment

No.	Company	Installed capacity(tpa)	Plant locations(states)	Margins
1	Finolex Industries	250,000	MH, GJ	9.5%
2	Supreme Industries	150,000	MH,UP,WB,MP	12-13%
3	Astral Polytechnik	102,371	GJ,KN	11-12%
4	Ashirwad Pipes	108,000	KN	NA
5	Prince Pipes	90,000	MH,GJ,UT,,TN	NA
6	Skipper	41,000	WB, MH, Delhi, AP	10-11%

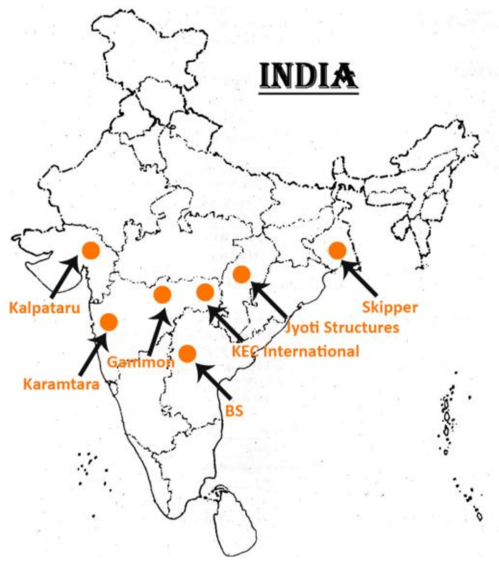
Source: Industry, Systematix Institutional Research

Skipper recently tied up with a Japanese firm, Sekisui, to source CPVC compounds to make CPVC pipes as the demand in the urban market (pipes for hot/cold water) is mainly shifting towards CPVC pipes. Skipper has also tied up with a Netherland-based firm, Wavin, to market advanced fittings of PVC pipes India.

We believe Skipper can grow at a rapid pace in this space -- growing from a smaller base and also driven by multi-locational capacities catering to multiple geographies. Competition has been intense in the industry as the slowdown in housing sector in the last two to three years resulted in margin pressure. Considering the size of business and investments being made into brand building, the operating margin is expected to be ~9-10% in the PVC vertical.

Plant location and vertical integration – is it a sustainable advantage?

Chart 15: Tower manufacturing plant locations



Source: Systematix Institutional Research

Table 4: Installed capacities of leading players

Company	Capacity (tpa)		
	FY13	FY14	FY15
KEC International	174,000	211,200	313,200
Kalpataru Power	180,000	180,000	180,000
Skipper	130,000	151,000	175,000
BS Ltd	240,000	240,000	240,000
Jyoti Structures	116,100	116,100	116,100
Gammon India	110,000	110,000	110,000
Karamtara Engg	108,000	108,000	108,000

Source: Industry, Systematix Institutional Research

Skipper is one of the leading manufacturers of power transmission towers, with a capability up to 1,200kV voltage levels -- highest voltage level in the country. The company has over two decades of experience in manufacturing transmission towers and is a pre-qualified bidder with PGCIL, SEBs and private transmission operators. Skipper's two plants are located within 60kms of Kolkata -- Uluberia and Jangalpur. It has also set up a 180,000tpa rolling mill in-house, which gives the flexibility to schedule manufacturing optimally, apart from the savings due to in-house manufacturing.

Table 5: Operating margin* profile of top players

Company	FY13	FY14	FY15
KEC Intl	5.5	6.2	6.0
Kalpataru Power	9.5	9.7	10.4
BS	12.5	13.1	15.0
Skipper	9.9	11.2	17.0

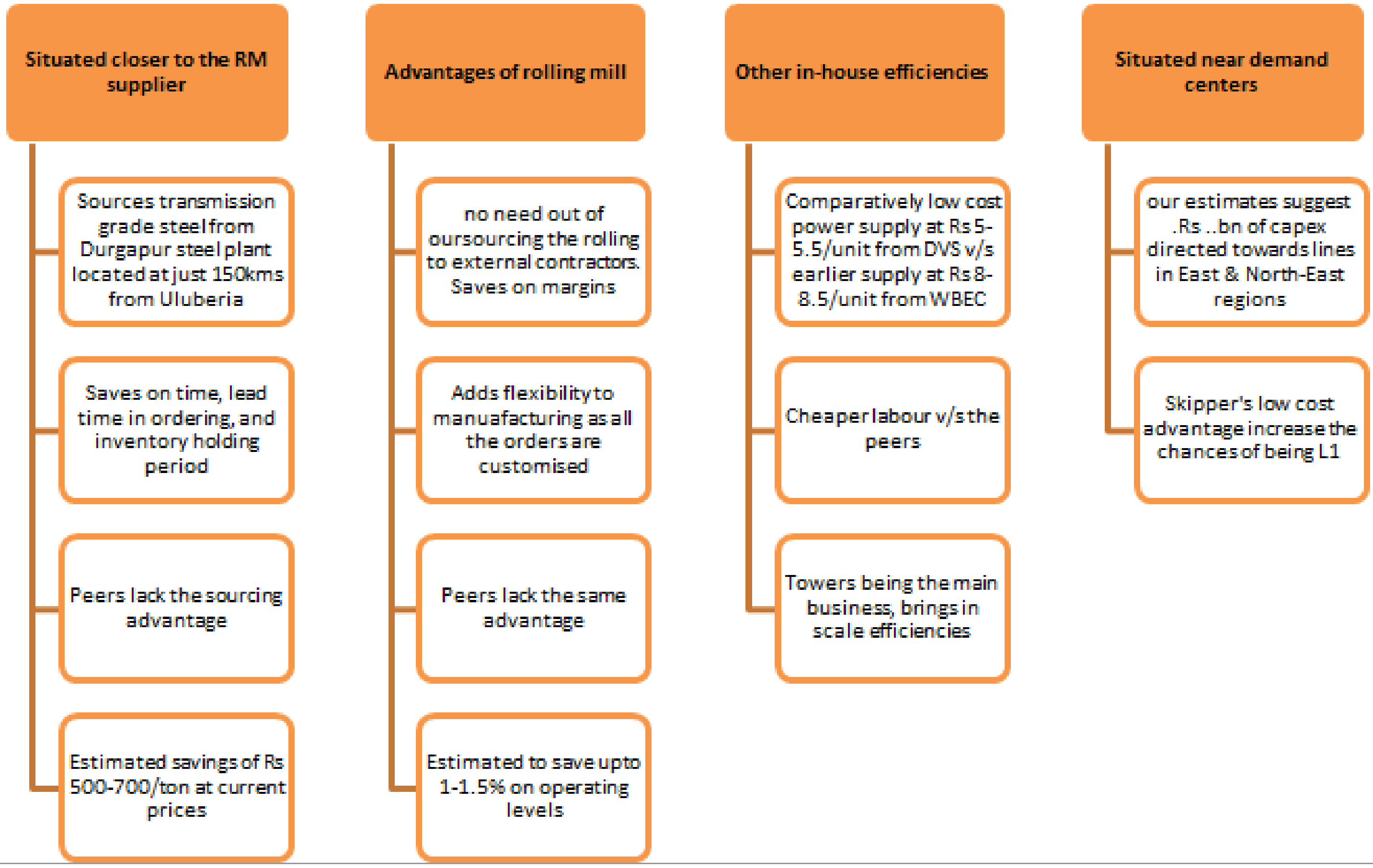
**-consol business, Source: Systematix Institutional Research*

Skipper's EBITDA margin was under pressure from FY11 to FY14 and remained ~9.3-10.6% on account of its low margins in ERW steel tubes and scaffoldings business. In FY14, the company restructured its ERW steel tubes business and leased its 50,000mtpa capacity to Tata Steel and earns job work charges on cost plus basis from it. Post restructuring of ERW steel tubes business, margins improved significantly to 16.9% in FY15, which was also aided by higher capacity utilisation and steep fall in raw material prices.

The company attributes the above-industry operating margin in tower division to the strategic plant location and vertical integration of the in-house rolling mill. Being the largest buyer of transmission grade steel from Durgapur steel plant gives it the advantage of economies of scale.

We analyse Skipper's operating margin sustainability versus peers in the transmission towers segment.

Chart 16: Parameters determining operating performance



Source: Company, Systematix Institutional Research

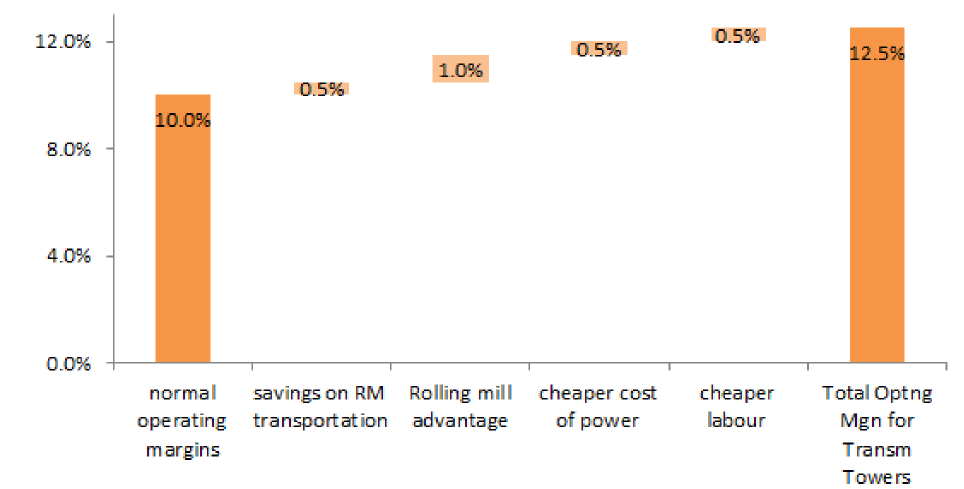
Skipper operates in an industry where most of the large organised players are predominantly EPC companies with revenues greater than it. Their in-house transmission tower production is mostly consumed internally and hence are not very aggressive in bidding for exclusive transmission tower orders. Among the top five EPC players in the industry, two players namely KEC International and Kalpataru Power consume transmission towers in their own EPC projects, while L&T and Tata Projects do not have any tower manufacturing facilities and hence place orders with manufacturers like Skipper. Transmission system operators (largest is PGCIL, a public sector entity and Adani and Sterlite, private operators) being utility players, outsource the entire tower manufacturing process either through tenders or private one-to-one negotiation.

Transmission tower manufacturers like BS Ltd, Gammon, Technocraft among others are not major players in PGCIL or SEB orders due to limitations in their pre-qualification criteria. We expect Skipper to retain the dominant player advantage in terms of supply of towers for high voltage lines for government utilities.

Galvanising – location becomes an advantage

Skipper also has in-house galvanising facilities at both plants. Galvanising facilities are considered 'Red' coloured (indicating very high level of pollution) and are banned in the developed world. They continue to operate in developing countries where pollution control norms are lax. We believe the possibility of galvanising operations getting banned in India is less going forward as the country is still at a developing stage and many industries depend on the activity.

Chart 17: Sustainable operating margin at 12.5% in T&D vertical

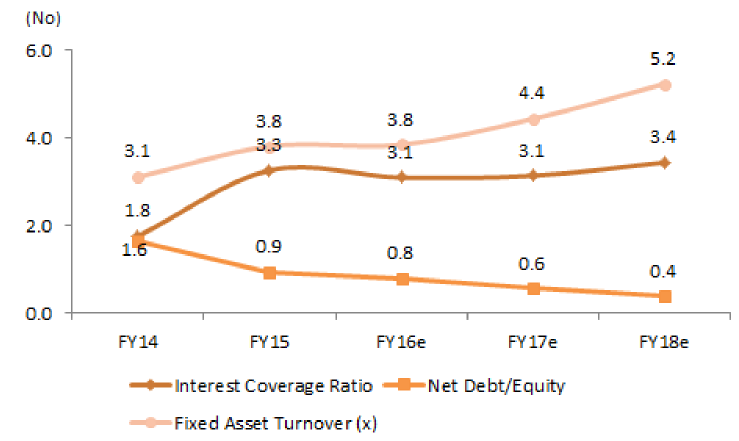


Source: Company, Systematix Institutional Research

We believe Skipper's location and rolling mill integration provide an edge over peers in terms of being the lowest cost producer. The low cost advantages are more effective in a high volume growth scenario causing higher asset turnovers, making it essential for the company to grow volumes at a minimum of 15-18% to keep utilisation effectively above 80%. We believe the company would be able to sustain the operating margins at 12.5%.

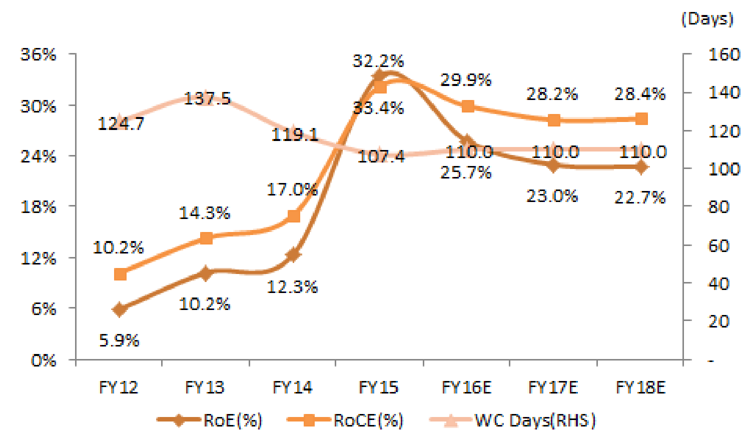
Improving asset turnover to maintain stronger return ratios

Chart 18: D/E under control, improving asset turns



Source: Company, Systematix Institutional Research

Chart 19: Return ratios steadily moving higher



Source: Company, Systematix Institutional Research

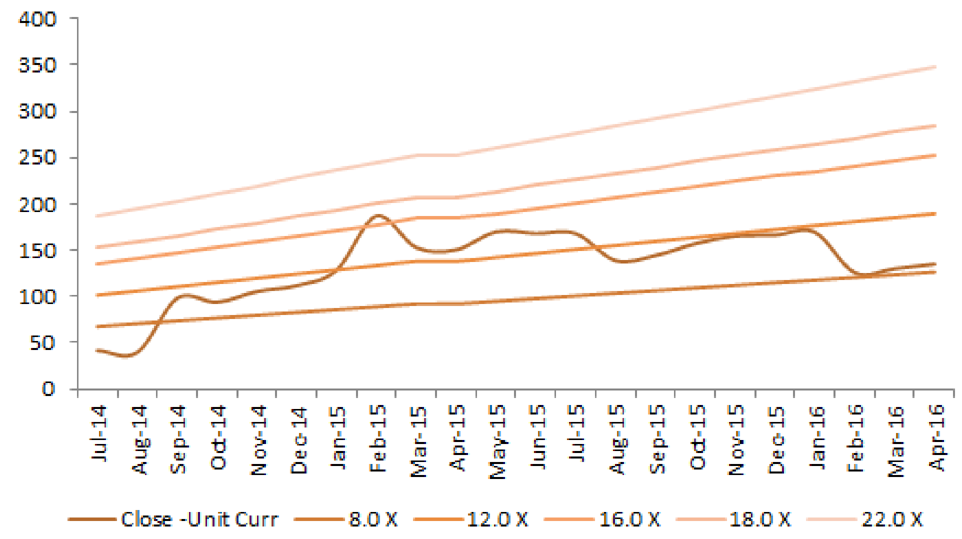
Skipper has a sufficient period of at least next three years for incremental capex in the transmission towers segment, thus limiting investments for purchase of land. Similarly, capacity building in PVC segment is planned to be carried out on a leased model. We believe the company's efforts to build an asset light model in both segments will result in increasing the asset turnover from 3.8x in FY15 to 5.2x in FY18e.

The long term debt repayment and maintenance capex are expected to negate each other and hence maintain the long term debt at the current level of Rs1.6-1.7bn for the next three years. Stronger operating cash flows would outpace the incremental requirement in short-term working capital, thus improving the debt-to-equity from 1.1x in FY15 to 0.7x in FY18e.

Even though RoE and RoCE are expected to decline from the FY15 level, we expect the company to post healthy RoE and RoCE of 22.7% and 28.4% respectively in FY18e.

Valuation: Correction in the stock price gives good entry point

Chart 20: 1 - year forward PE



Source: Capitaline, Systematix Institutional Research

Despite the strong volume momentum in both towers and PVC verticals, we expect the fallen commodity prices to restrain growth in the turnover of the company to CAGR of 13.8% during FY15-18e. As PVC business is inherently a lower margin business compared to towers, the operating margins are headed structurally downwards for the company. We expect EBIDTA margins to fall to 15.7% in FY18e from 17% in FY15. Net profits are expected to post a CAGR of 12% between FY15-18e. We value the company at ~3 years average one year forward PE of 15x to arrive at a target price of Rs182, an upside of 36% from the current level.

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