

15 February 2018

Techno Electric and Engineering

Stagnant order book; lowering to a Sell

At its present level of sales and margins, Techno Electric is likely to consolidate in FY19. Orders are expected to grow modestly in FY18 and FY19. The company is focusing on adding new revenue streams and assets to regularise or improve sales and earnings. We believe that it has good long-term prospects due to its strong balance sheet, but is likely to be under pressure in the next two years due to constrained growth. Valuations are rich; hence, we lower our rating to a Sell.

Standalone financials: revenue declined 17% y/y. The company focused on strengthening its balance sheet, closing old projects and repaying debt. Consolidated debt came down from ₹3bn in FY17 to ₹1.1bn. The company indicated a consolidation phase in FY18. The margin, at ~18.2% (up ~200bps y/y), seems a result of the favourable mix. Backed by healthy operating profit and aided by higher other income (dividend income from subsidiaries), earnings grew 7% y/y.

Sales likely to grow modestly in the next two years. Moderate growth in orders in FY18 and FY19 is likely to reflect in sales growth in those years. Transmission capex in the north-eastern region is expected to revive in FY19. The company is bullish on emission norm change capex in power generation and expects strong inflows for flue-gas-desulphurisation-related orders. We have factored in ~20% y/y growth in orders in the next two years. This should result in healthy, ~15%, growth in FY20. Margins are expected to hold at present levels

Valuation: On a sum-of-parts valuation (17x PE of FY20e core construction EPS, wind assets at ~₹45m/MW and DCF for BOOT/BOM assets), our target price works out to ₹348. At the CMP, the target price implies ~5% downside. **Risk.** Any more-than-anticipated orders is the key risk to our call.

Key financials (YE Mar)	FY15	FY16	FY17	FY18e	FY19e
Sales (₹ m)	10,328	12,363	12,479	13,510	15,073
Net profit (₹ m)	1,071	1,455	1,483	1,582	1,741
EPS (₹)	9.4	12.9	13.2	14.0	15.5
PE (x)	25.0	31.1	27.4	25.7	23.4
EV / EBITDA (x)	17.6	21.0	18.0	16.3	14.7
PBV (x)	3.7	5.3	4.2	3.7	3.3
RoE (%)	15.3	18.5	16.3	15.4	15.0
RoCE (%)	18.5	24.0	23.1	21.5	21.1
Dividend yield (%)	1.0	0.3	0.8	0.8	0.8
Net debt / equity (x)	0.2	-0.3	-0.4	-0.4	-0.5

Source: Company, Anand Rathi Research

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Rating: **Sell**

Target Price: ₹348

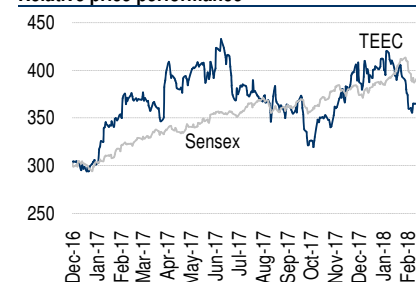
Share Price: ₹361

Key data	TEEC IN / TEEC.BO
52-week high / low	₹439 / 312
Sensex / Nifty	34156 / 10501
3-m average volume	\$1m
Market cap	₹41bn / \$647m
Shares outstanding	113m

Shareholding pattern (%)	Dec-17	Sep-17	Jun-17
Promoters	58.0	58.0	58.0
- of which, Pledged	-	-	-
Free float	42.0	42.0	42.0
- Foreign institutions	9.3	9.3	7.9
- Domestic institutions	16.5	16.5	17.7
- Public	16.2	16.2	16.4

Estimates revision (%)	FY18e	FY19e
Sales	-15.9	-18.1
EBITDA	-10.3	-14.0
EPS	-17.6	-19.4

Relative price performance



Source: Bloomberg

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Quick Glance – Financials and Valuations

Fig 1 – Income statement (₹ m)

Year-end: Mar	FY16	FY17	FY18e	FY19e	FY20e
Order book	26,000	26,000	27,369	29,783	33,022
Net revenues	10,328	12,363	12,479	13,510	15,073
Growth (%)	49.9	19.7	0.9	8.3	11.6
Material cost	7,816	9,325	9,459	10,258	11,559
Employee & other exp.	926	1,017	970	1,046	1,149
EBITDA	1,586	2,022	2,049	2,206	2,365
EBITDA margins (%)	15.4	16.4	16.4	16.3	15.7
- Depreciation	136	131	30	30	30
Other income	280	417	365	360	446
Interest expenses	208	159	102	102	102
PBT	1,522	2,149	2,281	2,434	2,679
Effective tax rate (%)	29.6	32.3	35.0	35.0	35.0
+ Associates / (minorities)	-	-	-	-	-
Net Income	1,071	1,455	1,483	1,582	1,741
Adjusted income	1,071	1,455	1,483	1,582	1,741
WANS	114	113	113	113	113
FDEPS (₹ / sh)	9.4	12.9	13.2	14.0	15.5
EPS growth (%)	26.5	37.4	1.9	6.7	10.1

Fig 3 – Cash-flow statement (₹ m)

Year-end: Mar	FY16	FY17	FY18e	FY19e	FY20e
PBT	1,522	2,149	2,281	2,434	2,679
+ Non-cash items	63	-105	467	462	548
Oper. prof. before WC	1,585	2,043	2,748	2,897	3,227
- Incr. / (decr.) in WC	-188	1,120	-580	-228	-241
Others incl. taxes	-511	-866	-798	-852	-938
Operating cash-flow	886	2,298	1,370	1,817	2,048
- Capex (tang. + intang.)	-87	1,872	-65	-113	-110
Free cash-flow	799	4,170	1,305	1,704	1,937
Acquisitions	-	-	-	-	-
- Div. (incl. buyback & taxes)	329	103	342	340	339
+ Equity raised	-	-	-	-	-
+ Debt raised	-42	-1,715	-	-	-
- Fin investments	262	2,209	-15	-15	-15
- Misc. (CFI + CFF)	-124	-311	-20	400	462
Net cash-flow	290	453	998	979	1,151

Source: Company, Anand Rathi Research

Fig 5 – Price movement


Source: Bloomberg

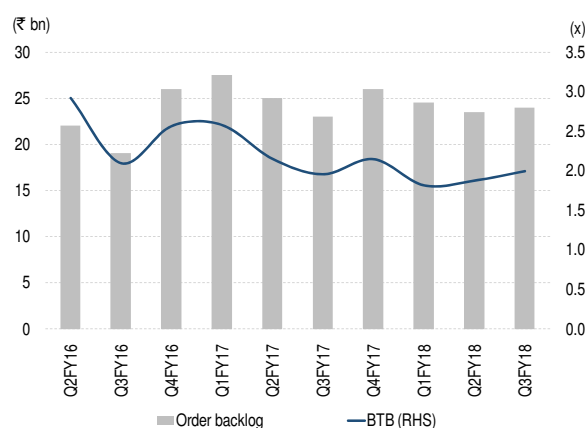
Fig 2 – Balance sheet (₹ m)

Year-end: Mar	FY16	FY17	FY18e	FY19e	FY20e
Share capital	114	228	228	228	228
Net worth	7,177	8,519	9,660	10,899	12,298
Total debt	1,715	-	-	-	-
Minority interest	-	-	-	-	-
DTL / (assets)	758	794	794	794	794
Capital employed	9,650	9,314	10,454	11,694	13,093
Net tangible assets	1,870	103	139	224	305
Net Intangible assets	5	3	2	1	-1
Goodwill	-	-	-	-	-
CWIP (tang. & intang.)	1	-	-	-	-
Investments (strategic)	4,478	4,940	4,940	4,940	4,940
Investments (financial)	132	1,894	1,894	1,894	1,894
Current assets (ex cash)	5,604	5,398	5,632	6,140	6,836
Cash	484	936	1,935	2,913	4,064
Current liabilities	2,924	3,962	4,088	4,417	4,947
Working capital	2,679	1,436	1,544	1,722	1,890
Capital deployed	9,650	9,314	10,454	11,694	13,093
Contingent liabilities	-	-	-	-	-

Fig 4 – Ratio analysis

Year-end: Mar	FY16	FY17	FY18e	FY19e	FY20e
P/E (x)	25.0	31.1	27.4	25.7	23.4
EV / EBITDA (x)	17.6	21.0	18.0	16.3	14.7
EV / sales (x)	2.7	3.4	3.0	2.7	2.3
P/B (x)	3.7	5.3	4.2	3.7	3.3
RoE (%)	15.3	18.5	16.3	15.4	15.0
RoCE (%) - after tax	18.5	24.0	23.1	21.5	21.1
RoIC (%) - after tax	26.8	48.8	75.1	65.3	63.7
DPS (₹ / sh)	2.3	1.0	3.0	3.0	3.0
Dividend yield (%)	1.0	0.3	0.8	0.8	0.8
Dividend payout (%) - incl. DDT	24.1	7.8	23.1	21.6	19.7
Net debt / equity (x)	0.2	-0.3	-0.4	-0.4	-0.5
Receivables (days)	161	143	148	149	149
Inventory (days)	13	0	0	0	0
Payables (days)	97	99	97	97	98
CFO:PAT%	82.7	158.0	92.4	114.8	117.6

Source: Company, Anand Rathi Research

Fig 6 – Stagnant order book


Source: Company

Result Highlights

Fig 7 – Consolidated financials (₹ m)

Quarterly results (YE: Mar)	Q3 FY17	Q3 FY18	% Y/Y	9M FY17	9M FY18	% Y/Y
Sales	3,563	3,015	-15.4	9,948	9,680	-2.7
EBITDA	754	736	-2.4	2,581	2,520	-2.4
EBITDA margin (%)	21.2	24.4		25.9	26.0	
Interest	80	39	-51.2	298	185	-38.0
Depreciation	133	106	-20.4	398	318	-20.2
Other income	49	17	-64.6	188	240	28.0
PBT	590	608	3.1	2,073	2,258	8.9
Tax	185	170	-8.0	470	522	11.2
PAT	409	434	6.3	1,595	1,725	8.2

Source: Company

Fig 8 – Standalone financials (₹ m)

Quarterly results (YE: Mar)	Q3 FY17	Q3 FY18	% Y/Y	9M FY17	9M FY18	% Y/Y
Sales	3,311	2,756	-16.8	8,790	8,452	-3.8
EBITDA	536	502	-6.3	1,514	1,385	-8.5
EBITDA margin (%)	16.2	18.2		17.2	16.4	
Interest	31	20	-34.8	124	72	-42.3
Depreciation	40	6	-84.0	121	20	-83.5
Other income	4	12	235.3	139	120	-13.6
PBT	467	487	4.2	1,408	1,414	0.4
Tax	158	152	-3.6	384	477	24.3
Tax rate	33.8	31.3	-	27.2	33.7	-
PAT	312	335	7.1	1,027	937	-8.8

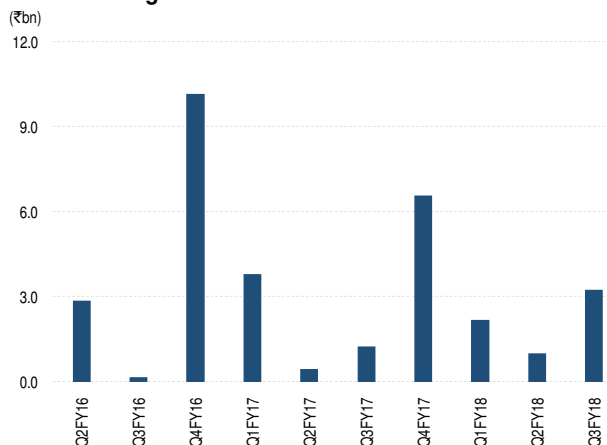
Source: Company

Fig 9 – Segment-wise highlights

	Standalone						Consolidated					
	Q3 FY17	Q3 FY18	% Y/Y	9M FY17	9M FY18	% Y/Y	Q3 FY17	Q3 FY18	% Y/Y	9M FY17	9M FY18	% Y/Y
Segment-wise revenues (₹ m)												
EPC	3,258	2,756	-15.4	8,538	8,452	-1.0	3,258	2,756	-15.4	8,538	8,452	-1.0
Energy	53	-		252	-		304	259	-14.9	1,410	1,228	-12.9
Corporate	4	12	235.3	139	120	-13.6	49	17	-64.6	188	240	28.0
Total	3,315	2,769	-16.5	8,929	8,572	-4.0	3,611	3,032	-16.0	10,136	9,920	-2.1
Segment-wise margins (%)												
EPC	15.1	18.0		15.0	16.2		15.1	18.0		15.0	16.2	
Energy	13.5			46.1			42.8	52.1		64.0	69.8	
Corporate	100.0	100.0	-	100.0	100.0	-	99.8	99.4		93.5	100.0	
Blended	15.1	18.3		17.2	17.3		18.6	21.3		23.3	24.8	

Source: Company

Fig 10 – FY18 inflows targeted at ~₹14bn



Source: Company, Anand Rathi Research

Results / Concall Highlights

- According to management, Q3 results were stable, both in EPC and wind-power, and have consolidated as expected. The company focus is to strengthen its balance sheet, close old projects and repay debt. Consolidated debt came down to ₹1.1bn, from ₹3bn in FY17. A further repayment of ₹200m is scheduled for Feb, which would bring down debt to ₹900m. The company expects zero debt (standalone) by end-FY18. Consolidated zero debt will be attained by end-H1 FY19.

Revenue

- EPC segment: The Company is focusing on consolidation of accounts, closing ongoing projects and collection retention money. It aims to triple the business.
- Unexpected heavy rains in Tamil Nadu led to flattish revenue in wind-power in Q2. The results are expected to be better or, in the worst case, on similar lines. Besides, the regulatory order on tariff revision has been implemented, keeping revenue at the same level. The company expects profitability to be better due to less outflow of interest cost (on debt reduction). It expects a better situation of grid availability in Tamil Nadu in FY19.
- Revenue was down 15%, mainly due to the impact of the GST.

Cost and Margins

- Material cost came down from 72% a year ago to 66%, a temporary phenomenon and due to a favourable sales-mix. Therefore, this savings will be diluted in coming quarters. The company expects to maintain a 15% margin in EPC.

Order book

- The company sees good opportunities in East Africa. It expects a \$100m business in FY19 from there.
- Its order book stands at ₹24bn.
- The company has booked orders of about ₹12bn in the last nine months and is expecting orders for the year to be around ₹14bn-15bn. It is L1 for orders of ₹3bn. It expects ~₹25bn orders in FY19 (₹10bn – utilities, ₹6bn – FGD, ₹6bn – Africa orders, ₹2.5bn – industry).

Segment-wise overview

- The FGD business did not grow in Q3 FY18 as expected. However, with the waning impact of the GST, it expects this segment to grow well from Q1 FY19. It aims at ~₹60bn-70bn in the FGD segment in coming years.
- Its industry segment is seeing a pick-up in enquiries and it sees order inflows by end-Q1 FY19. It expects growth to recover in H2 FY19.
- The REC market has turned around in the last three months. Trading here in Q3 FY18 is around 6.5m units, up from 0.5m in Q2 FY18. The company expects the backlog to be liquidated by end-FY18.

Other points

- Cash and cash equivalents are ₹3.7bn.
- Projects in Haryana and with Kalpataru are successfully in operation

with no major challenges.

- Trade receivables were healthy. The company is focusing on maintaining healthy working-capital along with growth.
- In India, winds are strong in the second quarter (Jul-Sep). Therefore, the company saw higher margins in Q2 (22.8%) than in Q3 (14.4%).
- It has received a \$32m order from Afghanistan. No capex will be required for export orders and will be carried out in association with partners (with Kalpataru for the Uganda project). These projects have been funded by EXIM, ADB, AFDB, etc.
- The tariff rate for Simran is ₹3.12. Average realisation came at ₹4.41.
- Apart from the company's investment in the JV with Kalpataru in the North-east (₹750m–800m), no other capex is expected in FY18.

NTPC tenders

- Lot 1A – 15 GW opportunity in FGD (the techno-commercial bid has already been submitted).
- Lot 1B – 10 GW opportunity (bidding will open by mid/end-Mar).
- NTPC Khargaon – 660 x 2GW (bidding should be complete by end-Feb).
- There are seven packages in each of them (Lots 1A and 1B). Each EPC operator cannot bid for more than three each. Eight operators are in the bidding.

Valuation

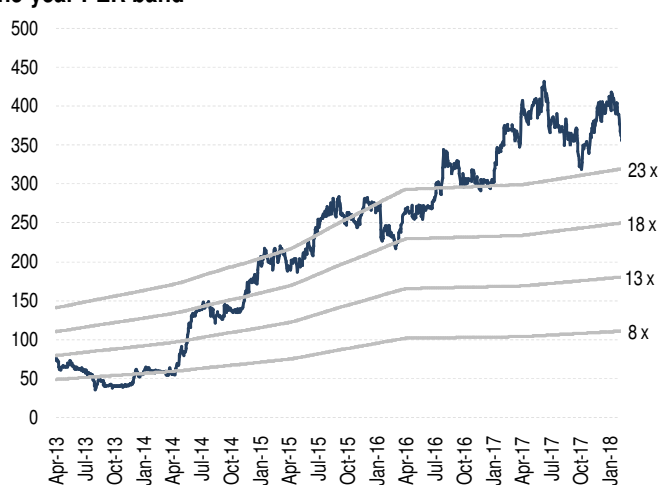
We value the company at 17x FY20e core EPC EPS of ₹15.3, wind capacity at an EV of ₹45m/MW and the three transmission assets on a DCF basis. Based on a sum-of-parts valuation, our target works out to ₹348.

Fig 11 – Sum-of-parts valuation

Valuation	Method	₹/ sh
EPC (construction)	17x FY20 EPS	259
BOOT / BOOM	DCF	9
Wind power	As per last transaction value	52
Add: Net Cash at SPVs		28
Target price (₹)		348

Source: Anand Rathi Research

Fig 12 – One-year PER band



Source: Bloomberg, Anand Rathi Research

Risks

- Any more-than-expected order inflows and better-than-anticipated pace of execution are key risks to our call.

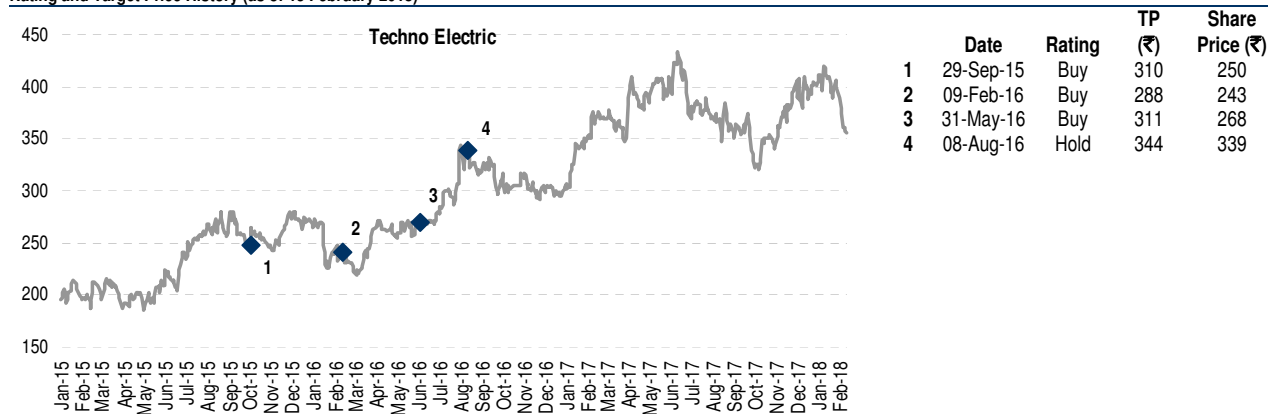
Appendix

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