ANANDRATHI

India I Equities

Industrial Consumables

Company Update

Change in Estimates ☑ Target ☑ Reco ☐

26 August 2021

KSB

Strong levers ahead, attractive valuations; maintaining a Buy

Rating: **Buy**
Target Price: Rs.1,411
Share Price: Rs.1,175

Strong opportunities exist for KSB in the next 2-5 years in FGD, nuclear power (NPCIL), O&G and exports. Such prospects would boost after-market and services (19% of its sales). Led by both pumps and valves, Q2 CY21 revenue was up 38% y/y. Cost savings and efficiencies, pricing and a favourable product-mix continue to benefit it, leading to a healthy 14.8% EBITDA margin in H1 CY21 (13.9% in CY20). With a strong H1 CY21, we have raised our estimates. Strong operations, execution abilities, sturdy margin expansion and attractive valuations keep us upbeat. We retain a Buy with a higher TP of Rs1,411 (28x CY22e earnings).

Strong Q2 CY21: Revenue grew 38% y/y to Rs3bn in Q2 CY21, driven by standard and engineered pumps performance. The EBITDA margin was a healthy 13%, better than in the past, due to cost-savings, price hikes and a favourable sales-mix (toward the distribution business). Other income was up 22% y/y; while interest/ depreciation rose 11%/9% y/y. PAT jumped 3.3x to Rs272m. Management guided double-digit revenue growth in CY21, but not regarding margins due to RM price uncertainty. Accordingly, we tweak our revenue/margin estimates.

Strong opportunities in FGD, nuclear, O&G. With capacity built up ahead of competition and pre-qualification in place, we expect opportunities in FGD, nuclear and O&G to be good. NPCIL announced 12 reactors (700MW each), a Rs3bn opportunity each, by 2031. FGD and the Atma Nirbhar vision are perceived as the largest opportunity. Stabilising crude-oil prices would lead to capex by oil producers. Agriculture, “smart” cities and waste-water management also throw up healthy prospects.

Valuations: A pick-up expected in order awards, its strong parent and execution ability augur well for the company. This, coupled with a brighter management outlook, enables us to raise our target multiple to 28x. We expect 19%/37% revenue/PAT CAGRs. The stock trades at attractive 29x/23x CY21e/CY22e P/Es. We retain our Buy, at a higher TP of Rs1,411; earlier Rs1,177. **Risk:** More-than-expected delay in order awards.

Key financials (YE Dec)	CY18	CY19	CY20	CY21e	CY22e
Sales (Rs m)	10,931	12,939	12,081	14,241	17,188
Net profit (Rs m)	716	918	938	1,427	1,753
EPS (Rs)	20.6	26.4	27.0	41.0	50.4
PE (x)	37.9	44.6	43.6	28.7	23.3
EV / EBITDA (x)	20.4	25.4	22.3	18.6	14.8
PBV (x)	3.6	4.9	4.6	4.1	3.6
RoE (%)	9.8	11.6	10.9	15.2	16.6
RoCE (%)	13.6	14.4	16.1	18.1	20.1
Dividend yield (%)	0.8	0.7	0.7	0.9	0.9
Net debt / equity (x)	-0.1	-0.3	-0.4	-0.3	-0.4

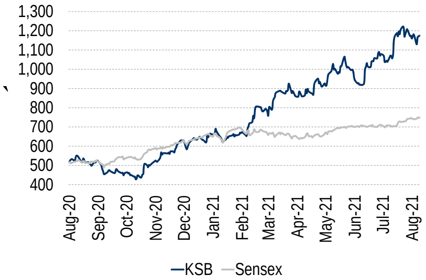
Source: Company, Anand Rathi Research

Key data	KSB IN / KSBP.BO
52-week high / low	Rs.1270 / 425
Sensex / Nifty	55949 / 16637
3-m average volume	$1.3m
Market cap	Rs.41bn / $550.7m
Shares outstanding	35m

Shareholding pattern (%)	Jun'21	Mar'21	Dec'20
Promoters	66.7	66.7	66.4
- of which, Pledged	-	-	-
Free float	33.3	33.3	33.6
- Foreign institutions	2.6	2.7	3.4
- Domestic institutions	11.6	11.7	11.6
- Public	19.2	18.9	18.6

Estimates revision (%)	CY21e	CY22e
Sales	8.4	8.4
EBITDA	6.5	6.8
EPS	6.8	7.0

Relative price performance



Source: Bloomberg

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Research Analyst

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Quick Glance – Financials and Valuations

Fig 1 – Income statement (Rs m)

Year-end: Dec	CY18	CY19	CY20	CY21e	CY22e
Net revenues (Rs m)	10,931	12,939	12,081	14,241	17,188
Growth (%)	*15.8*	*18.4*	*-6.6*	*17.9*	*20.7*
Material cost	5,651	6,983	6,206	7,476	9,075
Employee & Other expense	3,997	4,438	4,197	4,741	5,639
EBITDA	1,284	1,518	1,678	2,023	2,474
EBITDA margins (%)	*11.7*	*11.7*	*13.9*	*14.2*	*14.4*
Depreciation	397	457	418	435	458
Other income	200	216	291	306	321
Interest expenses	38	53	34	34	34
PBT	1,050	1,224	1,517	1,860	2,303
Effective tax rate (%)	*35.9*	*29.5*	*41.7*	*27.0*	*27.0*
+ Associates / (Minorities)	43	54	53	69	72
Net income	716	1,007	938	1,427	1,753
Adjusted income	716	918	938	1,427	1,753
WANS	35	35	35	35	35
FDEPS (Rs / sh)	20.6	26.4	27.0	41.0	50.4
EPS growth (%)	*1.0*	*28.1*	*2.2*	*52.1*	*22.9*

Fig 2 – Balance sheet (Rs m)

Year-end: Dec	CY18	CY19	CY20	CY21e	CY22e
Share capital	348	348	348	348	348
Net worth	7,578	8,288	8,906	9,916	11,249
Debt	434	600	600	600	600
Minority interest	-	-	-	-	-
DTL / (Assets)	-66	-16	-9	-9	-9
Capital employed	7,946	8,872	9,497	10,507	11,840
Net tangible assets	3,192	3,057	3,171	3,451	3,711
Net intangible assets	-	-	-	-	-
Goodwill	-	-	-	-	-
CWIP (tang. & intang.)	41	345	251	151	51
Investments (strategic)	-	-	-	-	-
Investments (financial)	598	644	662	662	662
Current asset (excl cash)	7,216	7,396	7,275	9,196	10,860
Cash	1,387	2,901	4,034	3,900	4,781
Current liabilities	4,488	5,471	5,896	6,853	8,225
Working capital	2,728	1,925	1,379	2,343	2,635
Capital deployed	7,946	8,872	9,497	10,507	11,840
Contingent liabilities	-	-	-	-	-

Fig 3 – Cash-flow statement (Rs m)

Year-end: Dec	CY18	CY19	CY20	CY21e	CY22e
PBT	1,050	1,351	1,517	1,860	2,303
+ Non-cash items	234	294	161	164	172
Oper. prof. before WC	1,284	1,645	1,678	2,023	2,474
- Incr. / (decr.) in WC	-225	688	516	-805	-292
Others incl. taxes	-359	-348	-625	-502	-622
Operating cash-flow	700	1,985	1,569	716	1,560
- Capex (tang. + intang.)	-526	-626	-438	-615	-618
Free cash-flow	174	1,360	1,131	101	942
Acquisitions	-	-	-	-	-
- Div. (incl. buyback & taxes)	242	323	296	348	348
+ Equity raised	-0	26	-24	-69	-72
+ Debt raised	308	166	-	-	-
- Fin investments	20	46	18	-	-
- Misc. (CFI + CFF)	-254	-332	-340	-182	-359
Net cash-flow	474	1,514	1,133	-134	881

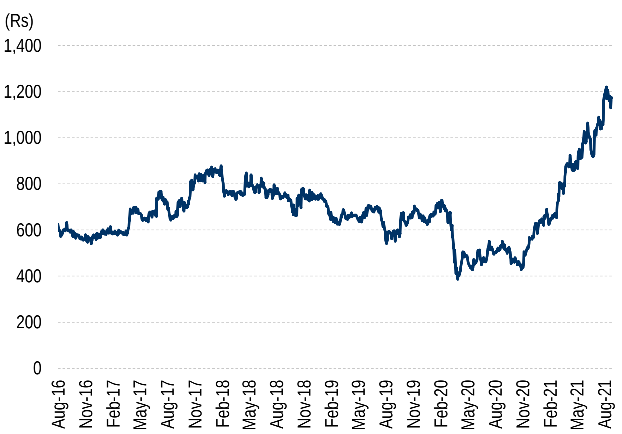
Source: Company, Anand Rathi Research

Fig 4 – Ratio analysis

Year-end: Dec	CY18	CY19	CY20	CY21e	CY22e
P/E (x)	37.9	44.6	43.6	28.7	23.3
EV / EBITDA (x)	20.4	25.4	22.3	18.6	14.8
EV / Sales (x)	2.4	3.0	3.1	2.6	2.1
P/B (x)	3.6	4.9	4.6	4.1	3.6
RoE (%)	9.8	11.6	10.9	15.2	16.6
RoCE (%) - after tax	13.6	14.4	16.1	18.1	20.1
RoIC (%) - after tax	11.1	14.8	16.4	23.7	25.7
DPS (Rs / sh)	6.0	8.0	8.5	10.0	10.0
Dividend yield (%)	0.8	0.7	0.7	0.9	0.9
Dividend payout (%) - incl. DDT	33.9	32.1	31.5	24.4	19.8
Net debt / equity (x)	-0.1	-0.3	-0.4	-0.3	-0.4
Receivables (days)	97	84	81	97	97
Inventory (days)	101	92	109	109	109
Payables (days)	82	77	92	92	93
CFO : PAT %	97.7	216.4	167.3	50.2	89.0

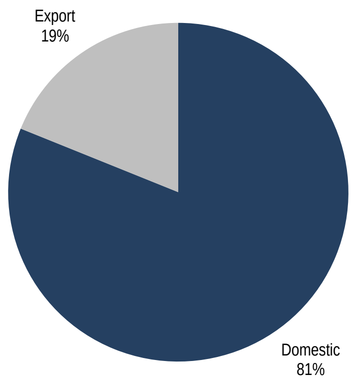
Source: Company, Anand Rathi Research

Fig 5 – Price movement



Source: Bloomberg

Fig 6 – Revenue, by region (H1 CY21)



Source: Company

Result Highlights

Fig 7 – Quarterly and annual trends

(Rs m)	Q2 CY21	Q2 CY20	Y/Y (%)	Q1 CY21	Q/Q (%)	H1 CY21	H1 CY20	Y/Y (%)
Net revenue	3,030	2,189	38.4	3,816	(20.6)	6,846	4,759	43.9
EBITDA	393	136	189.0	620	(36.6)	1,013	316	220.6
EBITDA margins (%)	*13.0*	*6.2*	*676bps*	*16.2*	*-328bps*	*14.8*	*6.6*	*816 bps*
Other income	84	69	21.7	72	16.7	156	197	(20.8)
Depreciation	108	99	9.1	108	-	216	198	9.1
Interest	10	9	11.1	9	11.1	19	17	11.8
Share of JV / Assoc.	12	6	100.0	19	(36.8)	31	12	158.3
Exceptional items	0	0		0		0	0	
Profit before tax	371	103	260.2	594	-38	965	310	211.3
Tax	99	21	371.4	155	(36.1)	254	119	113.4
PAT	272	82	231.7	439	(38.0)	711	191	272.3
Adj. PAT	272	82	231.7	439	(38.0)	711	191	272.3
Net margins (%)	9.0	3.7	*523bps*	11.5	*-253bps*	10.4	4.0	*637 bps*

Source: Company

Fig 8 – Cost analysis

(Rs m)	Q3 CY18	Q4 CY18	Q1 CY19	Q2 CY19	Q3 CY19	Q4 CY19	Q1 CY20	Q2 CY20	Q3 CY20	Q4 CY20	Q1 CY21	Q2 CY21
Sales	2,804	3,466	2,893	3,018	3,658	3,370	2,570	2,189	3,623	3,699	3,816	3,030
Raw material costs	1,449	1,939	1,552	1,608	2,082	1,741	1,308	1,253	1,942	1,703	1,891	1,569
Employee costs	394	400	417	455	439	468	475	450	477	460	520	503
Other expenses	640	648	606	634	750	684	607	350	595	783	785	565
% of sales												
Raw material costs	51.7	55.9	53.6	53.3	56.9	51.7	50.9	57.2	53.6	46.0	49.6	51.8
Employee costs	14.1	11.5	14.4	15.1	12.0	13.9	18.5	20.6	13.2	12.4	13.6	16.6
Other expenses	22.8	18.7	20.9	21.0	20.5	20.3	23.6	16.0	16.4	21.2	20.6	18.6
EBIDTA margins	11.4	13.8	11.0	10.6	10.6	14.2	7.0	6.2	16.8	20.4	16.2	13.0

Source: Company

Conference call highlights

- **Segment-wise contribution**: 1) Standard pumps 40-45%, 2) engineered pumps 30-35%, 3) distribution 15%, 4) exports 18-19%. However, in Q2 CY21, the distribution segment contribution went up, partially cushioning margins.
- **Exports** have increased 90% y/y to Rs1.3bn in H1 CY21. The share has moved up to 19.3% from 14.5% in H1 CY20 and 17.1% in CY20. 80-85% of exports have been done through the German parent.
- Management is positive on s**tandard pumps** mainly because of demand from buildings (commercial and residential), water & waste water treatment, agriculture (strong monsoon), sugar (the government's ethanol-blending programme) and steel, etc.
- On e**ngineered pumps**, the company is optimistic due to strong demand from nuclear pumps, FGD, oil & gas (due to the government's initiatives regarding a gas-based economy, greenfield and brownfield expansions by oil & gas companies in the next 3-4 years). The pipeline for API pumps for petrochemicals is also robust.
- **FGD** has been strong revenue driver because of restrictions on Chinese imports. Management expects another 180-190 pumps from FGD, which can be an opportunity of Rs1.5bn-2.5bn. While the project pipeline for FGD is expected to be strong for the next 2-3 years, it will also drive a strong after-market opportunity due to greater wear & tear.
- **The after-market segment** is one of the company's key focus areas. The company has been improving warehouse capability, increasing service centers across India to come closer to customer to shorten turnaround time.
- The **order book** is now Rs8bn (excl. Rs4.8bn from the Nuclear Power Corporation of India).
- **EBITDA margins:** The Q2 CY21 EBITDA margin would have been better if not affected by the steep rise in the commodity prices. Twice in the last six months the company hiked prices to pass on increases in commodity prices. However, management did not talk about margins as uncertainty reigns regarding commodity prices.
- **Competition** is very severe in India. However, KSB has operations across all the markets, which gives it an edge over peers. It is also looking at solar power as a new opportunity, where it will come out with highly differentiated products to tackle the competition. Other than government tenders, it will also be utilising its dealer network to control working capital.
- Ahead, management is positive and confident of **double-digit revenue growth** driven by a robust product basket.

Other key highlights

- At present, KSB has ~800 **dealers** of pumps, valves and systems in India and 150 a**uthorized centres**.
- The submersible pump capacity expansion at Sinnar is on track.
- Greater focus on the **digitisation** – to improve productivity and faster execution.
- From 2018 to 2020 KSB reduced its **carbon footprint** 36%, and aims to

reduce it by a further 50% by 2023, investing in several "green" initiatives at its factories and offices.

- **Capex** planned for CY21 is Rs850m.
- **Cash and cash balance** at end of Jun'21 was Rs3.4bn.

Fig 9 – Top-seven customers

Customer	Segment
NPCIL	Nuclear
HMEL Mittal Energy	Industry projects
ISGEC Heavy Engineering	Pumps and valves
Thermax	Valves
L&T Hydrocarbon Engineering	Industry projects
IOCL	Industry projects
BHEL	Control valves

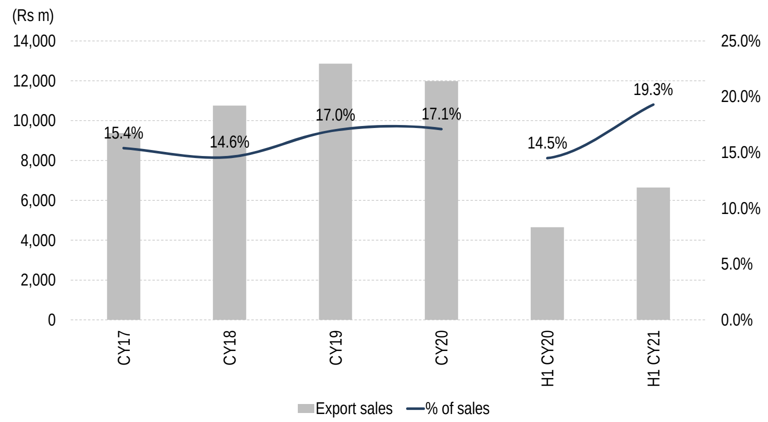
Source: Company

Fig 10 – Status on major investments of 2021

Investments	Amount (Rs m)	Remarks
Sinnar shed	249	Work in progress; expected completion by Dec'21. About 15% work completed as of date
Various machines for the nuclear project order - Mechanical seal testing / arrangement, nuclear localisation for RSR	138	- Mechanical seal testing arrangement PO realised, work completion by Dec'21 - Nuclear localisation for RSR, dynamic-balancing machine
3D-printing machine	88	Capex approved; ordering expected by Sep'21
Admin building and guest house at Shirwal plant	70	Shirwal office building and miscellaneous infra
Assembly, pre-testing & storage facility at TAPP for RSR 400/2	60	Contractor selection in progress, PO expected by Aug; Work completion by Dec'21
Mechanical seal localisation	59	Approval yet to be received
FGD lining-room extension	33	Currently on hold as government has extended timeline for environmental norms
Digitisation - RPA and various projects	32	MPC dossier - implementation and testing phase PO of RPA projects in the pilot phase Production booking software - CR approved, Digital info board - approved by committee
Other regular investments	122	BB2 and BB3 development, gamma development, group solar, central warehouse expansion, other regular investments
	850	

Source: Company

Fig 11 – Exports have jumped 90% y/y in H1 CY21



Source: Company

Valuation

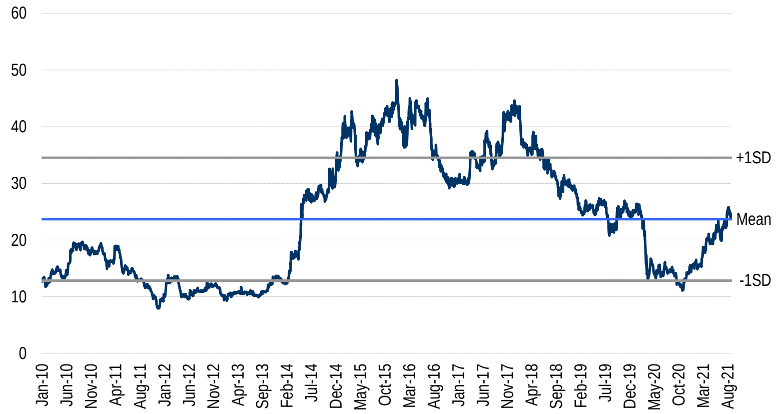
Expectations of a pick-up in awarding orders, its strong parent backing and execution ability augur well for the company. We expect 19% and 37% growth in respectively revenue and PAT over CY20-22. 14.2%/14.4% EBITDA margins are expected in CY21/CY22, backed by cost savings and efficiencies and a favourable product-mix. Based on this, we have raised our target multiple to 28x. The stock trades at attractive 29x and 23x CY21e and CY22e, respectively. Strong operations, execution capabilities, sturdy margin expansion and attractive valuations enable us to remain upbeat on it. We maintain our Buy, with a target price of Rs1,411, earlier Rs1,177.

Fig 12 – Change in estimates

	Old estimates		Revised estimates		% change	
(Rs m)	CY21	CY22	CY21	CY22	CY21	CY22
Revenue	13,132	15,857	14,241	17,188	*8.4*	*8.4*
EBITDA	1,899	2,317	2,023	2,474	*6.5*	*6.8*
EPS	38.4	47.1	41.0	50.4	*6.8*	*7.0*

Source: Company, Anand Rathi Research

Fig 13 – One-year-forward PE



Source: Bloomberg

Key risk

- Delay in booking orders due to postponements by the NPCIL.
- Deferred capex on higher-than-anticipated costs due to increase in commodity prices.
- Competition can eat into its market share in agriculture and residential pumps.
- Unable to pass on increases in commodity prices.

Appendix

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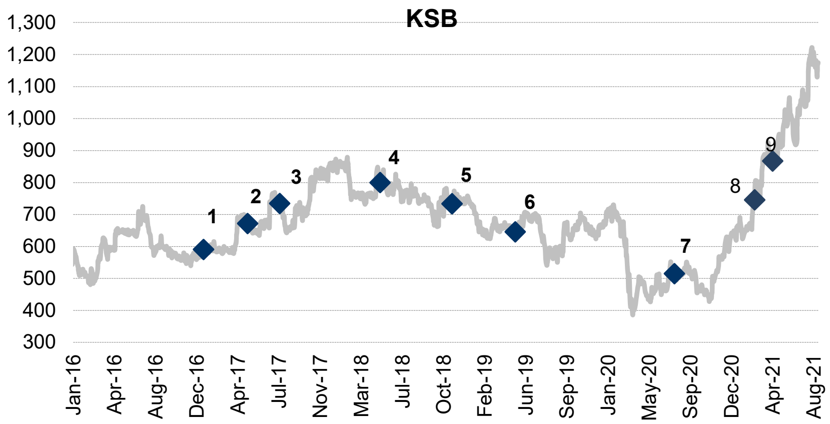

	Date	Rating	TP (Rs)	Share Price (Rs)
1	3-Feb-17	Sell	521	616
2	28-Apr-17	Sell	657	702
3	27-Jul-17	Sell	747	771
4	30-Apr-18	Sell	677	817
5	17-Nov-18	Sell	616	775
6	10-May-19	Sell	637	659
7	26-Jul-19	Sell	585	650
8	4-Mar-21	Buy	1008	785
9	4-May-21	Buy	1177	873

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