November 24, 2017 RE-INITIATING REPORT VOL-3, NO-23

KCP Limited

BUY

CMP: Rs. 121 **TARGET PRICE: Rs. 150** **TIME : 12 months**

We had initiated coverage on KCP Limited on September22, 2015 (Vol-1 No-5) at the price of Rs71 and target of Rs105. Post our coverage, the stock has breached our initial target of Rs105, revised to Rs150. Although the company has been a slow and compounding player, the conviction in the recommendation stands strong post analysis. We thereby re-initiate a BUY call on the stock at CMP of Rs and target of Rs150 over a horizon of 12 months.

About the company:

KCP Limited (KCP) is a diversified business group having presence in Cement, Heavy Engineering, Sugar, Power and IT. It operates its cement business through Macherla Cement Works and Mukthyala Cement Works having the combined capacity of 2.3mn tonnes, offering cement products such as ordinary Portland cement (OPC) and Portland pozzolana cement (PPC) under the brands KCP and Shreshtaa. The Power Segment consists of hydel, wind, waste heat based and thermal based plants at various locations which are primarily for captive consumption. The sugar business is through its joint venture Fives Cail KCP Ltd., which provides process equipments and plants for sugar, refining and bioethanol industries from cane and through its subsidiary, KCP Vietnam Industries Limited, which offers sugar, molasses and other products. The Company is engaged in the IT business through its associate, KCP Technologies Limited, a provider of offshore IT solutions.

INVESTMENT RATIONALE:

Business segments- the key triggers of growth going forward:

- Cement: For FY17, the company has registered record ever profits from the cement segment, in-spite of de-growth in realizations and demonetization blues. There was also improvement seen in the quantity of cement sold by about 15% over the previous year. With the brown field expansion (cement capacity would go up by 1.66million tons per annum (MTPA) to 3.52 MTPA and the clinker capacity by 1.51 MTPA to 3.06 MTPA) at Muktyalaunit likely to be completed by mid-2018-19, the volumes are expected to grow substantially. As indicated by the management, going forward, at the industry level, cement demand is expected to increase by 5-6% y-o-y in the near future on account of increased spends on roads and railways, push on affordable housing by central govt.
- Power: In the power segment, Hydel unit continues to disappoint with hardly any power generation. The performance of other power units viz. Wind, Thermal and Solar Plants is satisfactory.
- Engineering: The engineering unit continues to struggle due to combination of reasons like the recovery from cycle 'Vardah', delayed reflection of impact of reforms etc. It is still to take off awaiting pick up in the economic activity.
- Vietnam subsidiary for Sugar: the expansion from 6000 TCD of cane crushing to 8000 TCD, in the Vietnam subsidiary has been completed and on operations. The subsidiary has embarked on further expansion to 10,000 TCD which is expected to be on stream in about a year's time. Further, 30 MW Power Co-Generation plant was taken to production from March, 2017 to facilitate Son Hoa unit to operate at 8000 TCD rate and connected to national grid in 2017 to export the power and the Company is in the process of sourcing equipment to complete the expansion of Son Hoa sugar unit to 10,000 TCD for 2017-18 crushing season.
- Hospitality: With regards to the new projects in the hospitality space, the company has ventured into the Hospitality industry with a 128 room four star hotel project (Mercure Hyderabad KCP) by putting to beneficial use, the available land in a strategic location in Hyderabad. Being in operations, the occupancy rate is gradually picking up for the same and is expected to break even at operational levels.
- The Company undertook Ready Mix Concrete (RMC) business on experimental basis, by hiring the equipment temporarily, as the demand for the product is on the rise.

SNAPSHOT	
52 week H / L	Mcap (INR mn)
137/79	15,580
Face value: 1	
BSE Code	NSE CODE
590066	KCP

Annual Performance

(Rs mn)	FY15	FY16	FY17	FY18E
Sales (Net)	6,045	7,466	8,165	9,071
EBITDA	937	1,435	1,427	1,633
EBITDA (%)	15.5	19.2	17.5	18.0
Other Income	152	70	74	59
Interest	489	454	463	483
Depreciation	343	391	505	512
PBT	257	660	660	533
PAT	159	429	296	471
Equity	129	129	129	129
EPS (INR)	1.2	3.3	2.3	3.6

Quarterly Performance

Parameters (Rs mn)	Sep-16	Dec-16	Mar-17	Jun-17
Sales (Net)	2,038	2,024	2,290	2,368
EBITDA	371	407	352	519
EBITDA (%)	18	20	15	22
Other Income	12	7	19	22
Interest	120	117	108	104
Depreciation	130	127	131	120
PAT	86	102	90	232
Equity (Rs mn)	129	129	129	129

Ratio Analysis

Parameters (Rs mn)	FY15	FY16	FY17	FY18E
EV/EBITDA (x)	20.1	12.8	12.9	11.2
EV/Net Sales (x)	3.1	2.5	2.3	2.0
M Cap/Sales (x)	2.6	2.1	1.9	1.7
M Cap/EBITDA (x)	16.6	10.9	10.9	9.5
Debt/Equity (x)	1.2	1.0	1.0	0.9
ROCE (%)	10%	14%	13%	15%
Price/Book Value (x)	4.3	4.0	3.7	3.5
P/E (x)	133.2	50.5	53.3	33.1

Share Holding Pattern as on 30th September,2017

Parameters	No of Shares	%
Promoters	5,74,52,121	44.6
Institutions	78,06,894	6.1
Public	6,36,62,145	49.4
TOTAL	**12,89,21,160**	**100.0**

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Note: All the data is calculated as per Market Price on 24th November 2017

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INVESTMENT RATIONALE: (contd)

- The Company also has a brick unit in its cement unit at Muktyala. Considering the demand for traditional bricks, the unit has not made much progress. However, the unit is ready to meet the demand from upcoming capital of AP in Amaravati.

Financials:

When we had initiated coverage on the company, one of the key reasons was the expected value unlocking for the investors that could have happened if and when the company thinks of de-merging its businesses into independent entities. This process would help give accurate discounting for each of its business segments. This remains status quo for our recommendation till date. Further, the improving capacity utilizations led by the expansions and high operating leverage should lead to improvement in the operating margins going forward. For FY17, the company had reported sales growth of 9.1% at Rs8,183mn as against Rs7,498mn in the comparative year. The Ebidta margins were 18%. There was however a drop in the profits by 30.9% at Rs296mn as compared to Rs428mn in the last year.

Risk & Concern:

Although diversification insulates and reduces the dependency on a particular industry performance, it also has exposure to risks associated with each of the industries which could affect the overall performance of the company. However, as the company is equally aware of the same, timely and adequate steps are always taken to avoid the same.

Outlook and valuation:

With the government initiatives been taken across all the key industries for the overall economic boost, the company stands strong to benefit from the same. Also at the company level, there are various plans chalked by the company that should help it scale its business as well as reach across different industries. With the conviction remaining intact we re-initiate coverage on the stock with a target price of Rs150.

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