Sector: Industrial Machinery | RESULT REVIEW Q1FY22 | Declared On: 10 Aug 2021

Kirloskar Pneumatic Co. Limited

RECOMMENDATION SNAPSHOT					
*CMP	Initiation Price	Target	Potential Upside	Recommendation	MCap (Rs bn)
Rs356	Rs134	Rs475	33%	BUY	22.8

as on 18th Aug, 2021

About the Company:

Kirloskar Pneumatic Company Limited (KPCL) was founded in 1958 by Shantanurao Laxmanrao Kirloskar and is headquartered in Pune. KPCL is a well-diversified product company which serves some of the major and critical sectors (which help drive the economy of a country) like oil & gas, steel, cement, food & beverages, railways, defence, marine etc. The products offered by the company include air compressors, air conditioning and refrigeration systems, process gas systems, vapour absorption systems and industrial gear boxes. The company has its state-of-the-art manufacturing facilities at Hadapsar, Saswad and Nasik. The company is powered with highly qualified and trained service personnel who cater to clients across India. There are around 650 permanent employees on the rolls of company. Some of the customers with whom KPCL deals include Aurobindo, Gadre, Colourtex, Venkys, IOL, Hemani group, Dhanuka, Bharat Petroleum, Flex Foods Limited, Delmonte, DCM Shriram, John energy, Aditya Birla group, S.A Exports etc.

Result: Quick Glance

- The company has reported net sales of Rs1,689mn as compared to Rs804mn in the same quarter last year, growth of 110.2%
- The Ebitda margins for the quarter under review stood at 9.9% as compared to (-1.0%) in the corresponding quarter last year
- The net profit came in at Rs71mn as against a loss of Rs57mn in the same quarter last year
- EPS for the quarter under review stood at Rs1.10 as compared to Rs(-0.88) in the corresponding quarter last year

Conference Call Highlights:

- Despite the supply chain disruption and 2nd wave of Covid-19 affecting the company's operations, KPCL has reported good set of numbers which translates into 110.2% growth in revenue when compared to the corresponding period of the previous year (which was largely affected by nationwide lockdown).
- The Q1 results were impacted as it was challenging for the company with around 150 employees getting infected and a collapse in the supply chain, as well as ban of use of oxygen which stalled the fabrication business.
- The **compression business** now accounts for over 95% of the company's revenue and remains as only reporting segment; all other activities have been grouped under other non-reportable segments. The company has supplied 150 compressors packages in Q1FY22 to air separation plants for supply of oxygen through the PSA route. Around 200 were supplied in July as well. As per the management, this would be a component of business going forward as these would have benchmark minimum requirement across hospitals. This business would grow gradually with a particular level maintained. The company would have higher market share on larger capacity packages with almost leadership position. This should be a Rs1,500-2,000mn business for the company. In the gas generation and refrigeration space, the order intake was strong, the delayed packages are anticipated to be shipped out in Q2/ Q3FY22.The **Air compressor** segment grew the fastest in Q1FY22. It was contributing around 15-18% to the revenues last year, while is expected to be ~25% of the total sales this year. The company indicated that the transmission segment is being refocused for demand of gears and compressors, screw compressors. The **road railer** was impacted due to shut-down in Delhi for almost 2.5 months, but July was a strong comeback. The refrigeration compressors and systems business was muted during the quarter as projects were not taken up, but this is expected to be completed by Q3/Q4FY22. The cold chain ice plant compressor sales picked up as it was locally used for vaccine storage and is anticipated to pick up strongly going forward. The **vapour absorption chillers** demand also increased as the Pharma companies are doing well and going forward the growth should continue. Screw and reciprocating compressors for oxygen contributed to Q1 and should continue in Q2 as well. **CNG compressor** demand is increasing with the scaling up across CGD. The processed gas system is the larger part of the business where the company has seen record sales of CNG packages to the CGD companies; KPCL expects the business to grow further due to the 9th and 10th round of CGD bidding, while the industry expects another 8000 CNG stations to come up in next 8-10 years in an anticipation to cover about 70% of the Indian population, while bringing in a business of approximately Rs60bn to the industry. Market for CNG, CGD etc. is growing in India. Finally, as we see the economy moving from solid, to liquid to gas, there will be ample of opportunities for the industry as well as the company as a whole.
- The company has been known as a Project based company (45% from project business currently; trend of 60% in the past). However, during the quarter under review, the product sales has taken the lead which has translated into higher Ebitda margins (as the RM price increase can be passed on to customers which is not possible in project business). Going forward as the project business would get back, there could be some impact on the margins seen.
- Order booking during the first quarter was encouraging particularly in CNG compressors and Compressors for generation of Oxygen and the company intends to continue to supply these products in subsequent quarters as well. KPCL has already arranged for sufficient inventory and resources for this purpose even though some supply chain disruptions are still being experienced. The current **order book** is over Rs10bn (Rs6.80bn in the comparative period). This has 45% from gas business and 20-25% from both air compression and refrigeration respectively. The order book is more private oriented than Government based.
- Many customers buy products from KPCL due to the best-in-class aftersales backup which is an important add-on to boost the sales for company.

Please Turn Over

Kirloskar Pneumatic Co. Limited

Conference Call Highlights (contd.):

- The notable development during the quarter was the development and delivery of compressor system for methanol to coal project, through the Niti Aayog route and is expected to scale up in the next few quarters. The white spaces that the company is focusing on are the opportunity from the daughters station, hydro boosters which should pick up from Q4FY22 or Q1FY23. This is a 4000 compressor opportunity over the next 8 years in India alone. The other focus areas would be the Diaphragm compressors and biogas compressors.
- The company has off late been focusing on screw air compressors where their market share is low. The process and R&D to develop newer products is a continuous process and some new products with better efficiencies are anticipated to be launched going forward. The company is constantly working towards new product developments which is via their own R&D and design as well as manufacturing teams. Over the next 2-4 years, some new products are anticipated to hit the market once they are scaled up.
- The company had taken loan of Rs400mn in Q1FY21 as a provisioning for any Covid related set back, and so the finance cost is higher. The net cash as on 01st July, 2021 stands at Rs2,200mn. The company has chalked capex plan of Rs500mn of which Rs200mn has been done so far. On an average, it should have a runrate of Rs300-400mn per annum. The Ebitda margins of the past have been 15-16%, while the compression segment is around 18-19%; so as the turnover goes up the margins will also improve with the fixed costs getting amortized. The company has issued 79,500 equity shares under ESOPs. The exports remained muted during the quarter but the enquiries were strong which are yet to be finalized. One can expect execution from Q4 or early next year. Overall, the vision of the Management is to make it ~10% of the overall revenues.

Financials:

Performance (Q1FY22)							
Q1FY22 Result (Rs mn)	**June-21**	**June-20**	**y-o-y**	**Mar-21**	**q-o-q**	**FY21**	**FY22E**
Total Revenue	1689	804	-	4151	(59.3%)	8233	9509
EBITDA	167	(8)	-	722	(76.8%)	1130	1331
Other Income	31	23	33.9%	22	41.3%	101	107
Interest	7	1	-	9	(25.8%)	17	21
Depreciation	93	95	(1.7%)	93	0.1%	376	382
Exceptional Items	-	0	-	-	-	-	-
Tax	28	(24)	-	138	(80.1%)	200	259
Net Profit	**71**	**(57)**	-	**503**	**(85.9%)**	**638**	**777**

Outlook and Recommendations:

There was impact of the pandemic seen on the performance of the company. Q1FY21 had lower cases but complete lockdowns; while Q1FY22 had partial lockdowns but the case load was higher for the company to deal with. Inspite of these hindrances the company has clocked decent numbers. There has been encouraging growth seen across the segments with Air compressors being the lead which grew faster than anticipated and should also increase in share to the overall revenues going forward. KPCL is in position to manufacture some of the best in class products while providing superior solutions for the Make in India campaign. The company has an order book of Rs10bn which gives it the comfort in uncertain times. With India moving towards being a gas-based economy, (evident through the different opportunities chalked by the company); KPCL will definitely have an edge for this Rs60bn opportunity over the next 7-8 years in the CNG space as well in the replacement market. Considering the recent developments, strong industry tailwinds, healthy financials of the company, robust orderbook, new products to be launched (in pipeline) and strong management vision, we are very positive on the company with a long-term vision. The company maintains its aspiration of being a Rs20bn revenue company over the next 3 years and the efforts are being seen in this direction and thus we continue to maintain our target price of Rs475.

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