

RESULT UPDATE

MID CAP

Share Data

Reuters code	KROLBO
Bloomberg code	KKOEIN
Market cap. (US\$ mn)	560
6M avg. daily turnover (US\$ mn)	0.8
Issued shares (mn)	194
Target price (Rs)	150

Performance (%)	1M	3M	12M
Absolute	16	26	181
Relative	18	18	46

Valuation ratios

Yr to 31 Mar	FY10E	FY11E
EPS (Rs.)	9.0	8.8
+/- (%)	59.0	(1.9)
PER (x)	15.1	15.4
PBV (x)	2.4	2.1
Dividend/Yield (%)	0.7	0.7
EV/Sales (x)	1.4	1.2
EV/EBITDA (x)	8.4	8.4

Major shareholders (%)

Promoters	62
FII's	11
MF's	2
BFSI's	8
Public & Others	17

Financial highlights

(Rs mn)	2QFY10	2QFY09	YoY (%)	1HFY10	1HFY09	YoY (%)	FY09	YoY (%)	FY10E	YoY (%)	FY11E	YoY (%)
Net Sales	6,046	6,142	(1.6)	10,956	11,964	(8.4)	21,948	(0.8)	21,271	(3.1)	23,892	12.3
Expenses	5,001	5,419	(7.7)	9,110	10,557	(13.7)	19,161	(3.2)	17,820	(7.0)	20,448	14.7
EBITDA	1,045	723	44.6	1,846	1,408	31.2	2,787	20.2	3,452	23.8	3,444	(0.2)
Margin (%)	17	12	-	17	12	-	13	-	16	-	14	-
Other Income	94	78	20.6	150	95	57.2	133	(18.4)	237	78.7	278	17.1
Depreciation	232	185	25.4	430	378	13.6	804	83.9	857	6.5	915	6.8
Interest	41	262	(84.5)	70	338	(79.2)	376	123.3	158	(58.0)	184	16.3
PBT	866	353	145.5	1,496	786	90.3	1,740	(7.2)	2,674	53.7	2,623	(1.9)
Extra-ordinary Items	-	57	-	-	57	-	65	-	-	-	-	-
PBT after Extraordinary	866	410	-	1,496	843	90.3	1,805	-	2,674	-	2,623	-
Tax	244	136	79.2	446	275	62.4	647	(5.6)	936	44.8	918	(1.9)
Reported PAT	622	274	127.3	1,050	568	84.7	1,159	(2.6)	1,738	50.0	1,705	(1.9)
Adjusted Net Profit	622	217	187.1	1,050	511	27.9	1,094	(8.2)	1,738	59.0	1,705	(1.9)

Kirloskar Oil Engines

Maintain Outperformer

Price: Rs 135

BSE Index: 16,353

27 October 2009

2QFY10 Result – Margins improve

Kirloskar Oil Engines (KOEL) reported a drop in sales by 1.6% YoY in 2QFY10. Stationary Diesel Engine sales volumes have dropped by 1.5% YoY YTD FY10 (Source: DIPP). The other operating income of the sales jumped from Rs 221 mn in 2QFY09 to Rs 535 mn in 2QFY10, due to Rs 260 mn contribution of incentive on Kagal plant. In 1HFY10, Rs 1.5 bn of the total sales was from the small engine segment, Rs 6 bn from the medium engine segment and Rs 0.8 bn from the heavy engine segment. A reduction in material prices, steady sales prices in the last six months, stagnant employee costs, tax incentives and increased utilisation at the Kagal plant have enabled significant improvement in operating margins. Due to favourable movements on the exchange rate and LIBOR, the interest expenditure related to the ECB has dropped. Also, the interest expense in the comparable quarter last year included Rs 190 mn MTM increase on ECB. The debt held by KOEL stands at Rs 3 bn. The other income for 1HFY10 includes the dividend income from group companies. The company has launched its 525 kVA DG set, thereby entering Cummins's stronghold. For FY10, the capex budgeted is Rs 600 mn.

Increased competition is expected, especially in the lower kVA rating due to entry of cheaper new domestic options and Chinese manufacturers in the power generation segment. The company also expects a reduction in the power deficit from 12.5% in FY09 to negatively impact growth rate in generator set sales. With 50% and 25% of its sales coming from the power backup and industrial markets, the demand for KOEL's products are dependent on revival in construction and industrial activity.

We have revised earning estimate for FY10 upward by 20% to Rs 9 and for FY11 by 4% to Rs 8.8. At the current market price of Rs 135, adjusted for investments the stock is trading at 12x FY10E and 12x FY11E earnings. The favourable exchange rate and LIBOR may not sustain in FY11 for KOEL, likewise the drop in employee cost seen in FY10 may not hold once sales volumes starts increasing next year, and the 20% YoY YTD drop in material cost, in spite of an 8% drop in sales will be unsustainable. Factoring this, margins will likely drop from present levels, thereby slowing down earnings growth in FY11. Consequently upsides from present levels will be limited and will depend heavily on strong sales growth. We retain our Outperformer rating on the stock with a target price of Rs 150, which adjusted for 50% of market value of investments and related dividend income implies a P/E of 14 on FY11 earnings.

Segment analysis

(Rs mn)	1QFY10	1QFY09	YoY (%)	1HFY10	1HFY09	YoY (%)
Revenues						
Engines	5,719	5,823	(1.8)	10,364	11,307	(8.3)
Auto components	365	333	9.4	658	711	(7.5)
Other	–	26	–	–	45	–
Less: Inter segmental	38	41	(7.6)	66	99	(33.2)
Total	6,046	6,142	(1.6)	10,956	11,964	(8.4)
Results						
Engines	772	532	45.3	1362	1,048	30.0
Auto components	86	14	517.1	127	23	443.8
Other	–	11	–	–	23	–
Total	858.8	556.7	54.3	1,489	1,094	36.1
PBIT margins (%)						
Engines	13.5	9.1	–	13.1	9.3	–
Auto components	23.7	4.2	–	19.3	3.3	–
Other	–	–	–	–	–	–
Capital employed						
Engines	7,132	7,286	(2.1)	–	–	–
Auto components	–	527	–	–	–	–
Unallocated	6,950	5,621	23.7	–	–	–
Total	14,082	13,433	4.8	–	–	–

Income Statement

Yr end 31 Mar (Rs mn)	FY08	FY09	FY10E	FY11E
Net sales	22,117	21,948	21,271	23,892
<i>Growth (%)</i>	<i>14.1</i>	<i>(0.8)</i>	<i>(3.1)</i>	<i>12.3</i>
Operating expenses	(19,799)	(19,161)	(17,820)	(20,448)
Operating profit	2,318	2,787	3,452	3,444
EBITDA	2,318	2,787	3,452	3,444
<i>Growth (%)</i>	<i>6.4</i>	<i>20.2</i>	<i>23.8</i>	<i>(0.2)</i>
Depreciation	(438)	(804)	(857)	(915)
Other income	163	133	237	278
EBIT	2,043	2,116	2,832	2,807
Interest paid	(168)	(376)	(158)	(184)
Pre-tax profit	1,875	1,740	2,674	2,623
(before non-recurring)				
Non-recurring items	–	65	–	–
Pre-tax profit	1,875	1,805	2,674	2,623
(after non-recurring)				
Tax (current + deferred)	(685)	(647)	(936)	(918)
Net profit (before Minority Interest, Pref. Dividend, etc.)	1,190	1,159	1,738	1,705
Reported PAT	1,190	1,159	1,738	1,705
Adjusted net profit	1,190	1,094	1,738	1,705
<i>Growth (%)</i>	<i>(23.7)</i>	<i>(8.1)</i>	<i>59.0</i>	<i>(1.9)</i>

Balance Sheet

Yr end 31 Mar (Rs mn)	FY08	FY09	FY10E	FY11E
Cash & Marketable securities	616	791	1,074	2,088
Other current assets	6,845	6,029	5,887	6,613
Investments	4,763	4,719	4,697	4,697
Net fixed assets	7,105	6,730	6,391	6,295
Other non-current assets	227	285	–	–
Total assets	19,557	18,554	18,050	19,693
Current liabilities	6,453	4,861	4,212	4,731
Total debt	3,429	3,491	2,725	2,372
Other non-current liabilities	523	602	–	–
Total liabilities	10,405	8,954	6,938	7,103
Share capital	388	388	388	388
Reserves & surplus	8,764	9,211	10,724	12,202
Shareholders' funds	9,150	9,601	11,112	12,590
Total equity & liab.	19,557	18,554	18,050	19,693
Capital employed	13,104	13,693	13,838	14,962

Cash Flow Statement

Yr end 31 Mar (Rs mn)	FY08	FY09	FY10E	FY11E
Pre-tax profit	1,875	1,805	2,674	2,623
Depreciation	437	803	857	915
Change in working capital	437	(775)	(507)	(208)
Total tax paid	(553)	(626)	(1,253)	(918)
Cash flow from oper. (a)	2,197	1,207	1,771	2,412
Capital expenditure	(3,979)	(247)	(319)	(800)
Change in investments	411	45	21	
Others	(240)	(181)	(199)	(19)
Cash flow from inv. (b)	(3,809)	(383)	(496)	(819)
Free cash flow (a+b)	(1,612)	824	1,274	1,593
Equity raised/(repaid)	194	–	–	–
Debt raised/(repaid)	2,366	62	(765)	(354)
Dividend (incl. tax)	(452)	(227)	(228)	(225)
Others	(293)	(483)	–	–
Cash flow from fin. (c)	1,815	(649)	(993)	(579)
Net change in cash (a+b+c)	203	176	282	1,014

Key Ratios

Yr end 31 Mar (%)	FY08	FY09	FY10E	FY11E
Adjusted EPS (Rs)	6.1	5.6	9.0	8.8
Growth	(23.7)	(8.1)	59.0	(1.9)
Book NAV/share (Rs)	47.1	49.4	57.2	64.8
Dividend/share (Rs)	2.0	1.0	1.0	1.0
Dividend payout ratio	38.2	20.8	13.1	13.3
Tax	36.5	35.8	35.0	35.0
EBITDA margin	10.5	12.7	16.2	14.4
EBIT margin	9.2	9.6	13.3	11.7
RoCE	17.8	15.8	20.6	19.5
Net debt/Equity	30.7	28.1	14.9	2.3

Valuations

Yr end 31 Mar (x)	FY08	FY09	FY10E	FY11E
PER	22.1	24.0	15.1	15.4
PCE	16.1	13.9	10.1	10.0
Price/Book	2.9	2.7	2.4	2.1
Yield (%)	1.5	0.7	0.7	0.7
EV/Net sales	1.3	1.3	1.4	1.2
EV/EBITDA	12.5	10.4	8.4	8.4

Du Pont Analysis – ROE

Yr end 31 Mar (x)	FY08	FY09	FY10E	FY11E
Net margin (%)	5.4	5.0	8.2	7.1
Asset turnover	1.3	1.2	1.2	1.3
Leverage factor	2.0	2.0	1.8	1.6
Return on equity (%)	13.5	11.7	16.8	14.4

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