

Stock Update

Mixed quarter, outlook remains strong

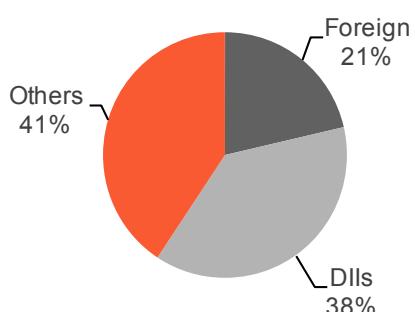
Larsen & Toubro

Reco: Buy | CMP: Rs1,355

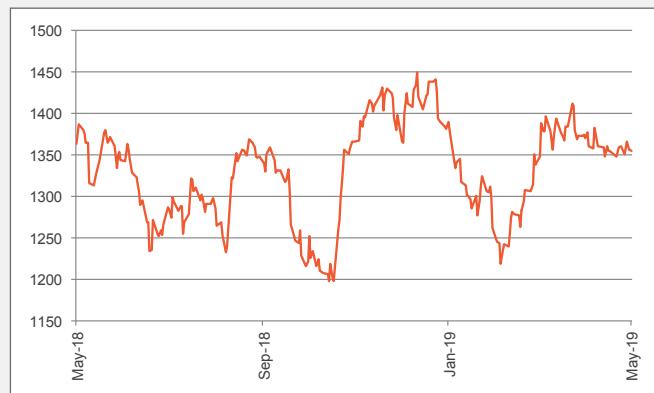
Company details

Price target:	Rs1,655
Market cap:	Rs190,105 cr
52-week high/low:	Rs1459/1183
NSE volume: (No of shares)	2.0 lakh
BSE code:	500510
NSE code:	LT
Sharekhan code:	LT
Free float: (No of shares)	140.3 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-1.4	7.5	-0.9	-0.1
Relative to Sensex	2.3	4.5	-7.4	-7.3

Key points

- **Execution remains strong:** In Q4FY2019, consolidated net sales of Larsen & Toubro (L&T) were in-line with our estimates, driven by healthy execution and strong order backlog during the quarter. Net sales grew by 10.5% y-o-y to Rs. 44,934 crore, driven by strong execution in the project business along with robust performance in the service business. Revenue was mainly driven by strong growth in domestic sales, led by infra, realty, hydrocarbons and services businesses. Operating profit margin (OPM) declined by 85 BPS y-o-y to 12.5%, owing to weak margins in the infra segment leading to 3.4% y-o-y growth in operating profit to Rs. 5,599 crore. Higher other income of Rs. 621 crore (up 50.5% y-o-y due to higher treasury earnings) led to 7.9% growth in net profit to Rs. 3,418 crore.
- **Strong order inflow results in healthy order backlog:** During Q4FY2019, order inflow was strong and better than expectation. Order inflow for the quarter came in at Rs. 56,538 crore (up 14% y-o-y), beating the company's guidance of 12% y-o-y growth, of which Rs. 17,680 crore constituted international order, which doubled from last year, largely contributed by hydrocarbons in Q4FY2019. Domestic order inflow came in lower for the quarter at Rs. 38,858 crore (down -5% y-o-y mainly driven by state government orders). Thus, order backlog grew by 12% y-o-y to Rs. 2,93,427 crore at the end of Q4FY2019, which provides revenue visibility of 2.1 years on TTM basis.
- **Outlook: Expect order momentum to sustain amidst general elections and post stable government:** Bidding pipeline for L&T is expected to be around Rs. 9 lakh crore-10 lakh crore (almost 50% to be from the infra segment, 25% from hydrocarbons and balance from other segments). L&T expects to win Rs. 1.8 lakh crore-2 lakh crore from this bidding pipeline. The mix is expected to remain 25% for international and 75% for domestic orders. Although general elections can hamper order inflows from the public sector space during H1FY2020 for the industry, L&T would be targeting big ticket-size projects having multilateral funding and key international geographies (Middle East, North and East Africa Bangladesh and Far East countries). Consequently, we believe L&T would be able to achieve its inflow guidance

of 10-12% y-o-y for FY2020. Post FY2020, management sees strong traction in order inflows from domestic markets, considering a stable government.

- ♦ **Maintain Buy with unchanged PT of Rs. 1,655:** Management reiterates its order inflow and topline guidance of 10-12%/12-15%, respectively, with stable margin on a consolidated level.

However, there is scope of margin improvement through better operating margin in the infra segment (FY2019 net profit was affected due to Rs 300 crore provisioning in the infra segment). Based on continued strong growth momentum in subsidiaries and improved outlook on standalone basis, we maintain our Buy rating with an unchanged price target (PT) of Rs. 1,655.

Results (Consolidated)

Particulars	Q4FY19	Q4FY18	YoY %	Q3FY19	Rs cr QoQ %
Net Sales	44,934	40,678	10.5%	35,709	25.8%
Total Expenditure	39,335	35,266	11.5%	31,697	24.1%
Operating profits	5,599	5,413	3.4%	4,012	39.6%
Other Income	621	413	50.5%	591	5.2%
Interest	507	420	20.6%	535	-5.2%
Depreciation	475	492	-3.6%	449	5.7%
PBT	5,239	4,913	6.6%	3,619	44.8%
Exceptional item	-	-		-	
PBT	5,239	4,913	6.6%	3,619	44.8%
Tax	1,323	1,458	-9.3%	1,200	10.2%
PAT	3,418	3,167	7.9%	2,042	67.4%
Adj. PAT	3,418	3,167	7.9%	2,042	67.4%
EPS (Rs.)	24.4	22.6	7.8%	14.6	67.3%
Margins (%)			BPS		BPS
OPM	12.5	13.3	(85)	11.2	123
PATM	7.6	7.8	(18)	5.7	189
Tax Rate	25.2	29.7	(443)	33.2	(792)

Valuations (Consolidated)

Particulars	FY17	FY18	FY19	FY20E	FY21E	Rs cr
Net sales	109,312	119,683	141,007	157,928		173,721
Growth (%)	8.1	9.5	17.8	12.0		10.0
OPM (%)	10.1	11.4	11.6	11.6		11.6
Adj Net profit	5,920	7,247	8,610	10,263		11,557
EPS (Rs.)	42.2	52.5	63.4	73.2		83.9
Growth (%)	43.0	24.3	20.8	15.5		14.6
PER	32.1	25.8	21.4	18.5		16.2
P/B	3.8	3.4	3.1	2.7		2.4
EV/EBIDTA	21.5	18.3	14.6	12.9		11.5
ROCE (%)	6.2	7.8	9.0	10.0		10.8
RONW (%)	12.8	13.9	15.1	15.5		15.7

SOTP valuation

Particulars	Remarks	Value (Rs cr)	Per share
L&T's core business (standalone)	At 23x FY2020 estimates	147,048	1,049
Subsidiaries			
L&T Infotech (LTI)	Based on our target price	28,597	204
L&T Finance Holdings (L&TFH)	Based on our target price	17,000	121
L&T Technology Services Ltd (LTTS)	25% holding discount to Mcap	13,358	95
Development projects (including IDPL)	At 0.8x Book Value	12,450	89
Hydrocarbon subsidiary	At 0.8x Book Value	6,500	46
Other subsidiaries	At 0.8x Book Value	6,142	44
Associates & Other	At 0.8x Book Value	954	7
Total subsidiary valuation		85,002	606
Fair value		232,050	1,655

Segmental Performance

Particulars	Q4FY19	Q4FY18	YoY/BPS	Comment
Infra	27,094	24,349	11.3%	Strong growth on robust order book, margins reflect stage of execution, job mix and cost provisions arising from execution headwinds in some transportation infra projects
PBIT margin (%)	11.4	12.7	(125)	
Power	934	1,507	-38.0%	Revenue decline reflects low order book. Profits of MHPS and other JV companies are consolidated at PAT level under equity method. Retrofitting of old plants with emission-control equipment (FGD and SCR) provides new business opportunity.
Heavy Engineering	899	512	75.7%	Demand for oil and gas and nuclear power equipment drives revenue growth. International markets showing strong traction in the refineries space; has driven growth in inflows (78%) and order book (61%) in FY2019. Global competence, technology differentiation, proven track record and cost efficiencies yield strong margins.
Defence Engineering	1,108	953	16.3%	Execution of tracked gun order contributing to revenue. Margin variation due to stage of execution, job mix and operational efficiency. Ordering delays restrict the potential of the segment.
PBIT margin (%)	15.4	9.2	618	
E&A	1,716	1,643	4.4%	Revenue growth driven by product businesses (ESP and MPS) across industrials, buildings, agriculture and rural electrification sub-sectors. Margins enhanced by operational efficiencies and profitable sales mix.
Hydrocarbons	4,324	3,559	21.5%	Significant growth in order Inflows (76%) and order book (49%) contributed by domestic and international wins. Stable oil prices leading to build-up of healthy prospect pipeline. Improved margins and superior ROIC obtained through efficient execution and working capital management.
IT & Tech	3,827	3,152	21.4%	LTI revenue growth led by BFS, CPG, retail and pharma and high-tech, media and entertainment verticals. LTTS revenue growth led by transportation, telecom and hi-tech and process industry. Margin improvement aided by currency gains and operational efficiencies.
Financials	3,182	2,722	16.9%	Revenue growth due to growth in retail book. Increasing NIMs, higher fee income and improving asset quality boost profit.
PBIT margin (%)	23.6	15.0	855	
Developmental projects	1,083	1,217	-11.0%	Revenue largely contributed by the power development business. Hyderabad Metro: Partial CoD of 30 km in November 2017, 16 km in September 2018 and 9 km in March 2019. Total of 55 km. Margin profile still emerging.
Others	1,413	1,635	-13.6%	Revenue & Margin growth largely contributed by the realty business.
PBIT margin (%)	11.0	42.0		

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