

Larsen & Toubro | BUY

Weak margins a dampener but remain positive on outlook

L&T's 2QFY24 PAT at INR 32.2bn beat estimate of INR 26.2bn (consensus: INR 28.3bn) led by higher revenue, gain of INR 5.1bn on TOD monetization and higher other income. P&M business EBITDA margin at 7.4% missed estimate of 8.2% due to pressure in legacy (pre-Covid) projects owing to time and cost overruns. Order inflows beat estimate and grew 72% YoY to INR 892bn with order backlog at INR 4.5tn (3.2x P&M revenue). NWC remained low at 16.7% of revenue (17% in June-23). While L&T lowering its FY24 margin guidance (8.5-9% from 9% earlier) was a dampener, we remain positive on the outlook for FY25 and FY26 led by strong order wins, supportive execution environment and a likely margin normalcy (9-10% historically for P&M). Strong EPS growth (25.3% CAGR over FY23-26E for P&M), lower asset intensity along with the recent buyback should drive ROE expansion. Maintain BUY with revised price target of INR 3380 with the P&M business valued at 25x Mar-26E EPS.

- Robust execution led by strong backlog; P&M margins miss estimate:** Consolidated revenue/EBITDA grew by 19%/15% YoY to INR 510bn/INR 56.3bn and beat estimate of INR 491bn/INR 53.7bn. Execution was particularly strong in Infra (+27% YoY) and Hydrocarbons (+29% YoY) segments. Core P&M business revenue/EBITDA grew by 24%/12.3% YoY to INR 349bn/INR 25.8bn with P&M margins at 7.4% (estimate: 8.2%, down 80bps YoY). P&M EBITDA missed estimate of INR 27.3bn due to continued pressure from low margin legacy projects in the infrastructure segment. The beat in the consolidated EBITDA was driven by gain of INR 5.1bn on TOD monetization in Hyderabad Metro.
- Order inflows remain robust; order prospects boosted by Hydrocarbons (HC):** Consolidated order inflows grew 72% YoY to INR 891bn with P&M inflows of INR 730bn (+96% YoY; estimate INR 682bn). Order backlog remains strong at INR 4.5tn (3.2x TTM revenue). Prospects pipeline for 2HFY24 order wins stands at INR 8.7tn (+39% YoY) with HC pipeline at INR 2.9tn (+2.6x YoY). Management specifically highlighted large prospects in the Middle East (Saudi Arabia, Qatar and UAE) in the HC space.
- Likely to exceed order intake and execution guidance; margin guidance lowered:** L&T expects to exceed its FY24 guidance of 10-12% growth in order inflow and 12-15% growth in revenue for the P&M business. We build-in 20% growth in P&M order inflow to INR 2.06tn (2HFY24E: INR 830bn, down 22% YoY) and 19.7% growth in execution in FY24. However, EBITDA margin guidance for the P&M business has been lowered to 8.5-9% range from 9% earlier due to likely delay in margin recognition from newer projects even as older legacy projects drag the margins.
- Expect 25.3% CAGR in P&M earnings over FY23-26E; supports valuations:** We expect EPS CAGR of 25.3% over FY23-26E for L&T's P&M business. Strong growth, reducing asset intensity (lower NWC & asset sales) and push from the recent buyback should drive ROE expansion to 18.5% by FY26 (12% in FY23). Valuations at 25.1x/20.8x FY25E/26E P&M business EPS remain well supported. Our revised SOTP-based price target of INR 3380 values the P&M business at 25x Mar-26E EPS. Maintain BUY.



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Recommendation and Price Target

Current Reco.	BUY
Previous Reco.	BUY
Current Price Target (12M)	3,380
Upside/(Downside)	15.4%
Previous Price Target	2,835
Change	19.2%

Key Data – LT IN

Current Market Price	INR2,929
Market cap (bn)	INR4,117.2/US\$49.5
Free Float	100%
Shares in issue (mn)	1,405.1
Diluted share (mn)	1,374.4
3-mon avg daily val (mn)	INR5,803.7/US\$69.7
52-week range	3,115/1,966
Sensex/Nifty	63,875/19,080
INR/US\$	83.3

Price Performance

%	1M	6M	12M
Absolute	-3.1	24.2	45.1
Relative*	-0.2	18.8	38.9

* To the BSE Sensex

Financial Summary

Y/E March	FY22A	FY23A	FY24E	FY25E	FY26E
Net Sales	1,565,212	1,833,407	2,147,060	2,469,669	2,813,927
Sales Growth	15.1%	17.1%	17.1%	15.0%	13.9%
EBITDA	182,173	207,533	248,442	291,201	336,341
EBITDA Margin	11.6%	11.3%	11.6%	11.8%	12.0%
Adjusted Net Profit	85,724	103,348	136,911	168,318	200,033
Diluted EPS (₹)	61.0	73.5	99.6	122.5	145.5
Diluted EPS Growth	21.3%	20.5%	35.5%	22.9%	18.8%
ROIC	5.8%	7.0%	8.6%	9.8%	11.0%
ROE	10.8%	12.0%	15.4%	17.8%	18.5%
P/E (x)	27.7	26.0	29.4	23.9	20.1
P/B (x)	2.9	3.0	4.6	4.0	3.5
EV/EBITDA (x)	17.1	15.8	18.9	15.8	13.4
Dividend Yield	1.3	1.3	1.2	1.1	1.3

Source: Company data, JM Financial. Note: Valuations as of 31/Oct/2023

JM Financial Research is also available on:
Bloomberg - JMFR <GO>,
Thomson Publisher & Reuters,
S&P Capital IQ, FactSet and Visible Alpha

Please see Appendix I at the end of this report for Important Disclosures and Disclaimers and Research Analyst Certification.

Exhibit 1. Consolidated Quarterly Results

INR mn	2QFY23	3QFY23	4QFY23	FY23	1QFY24	2QFY24	2QFY24E	Variance (%)	FY24E	FY25E	FY26E
Net sales	427,626	463,897	583,352	1,833,407	478,824	510,240	490,853	3.9%	2,147,060	2,469,669	2,813,927
EBIDTA	48,994	50,730	68,330	207,533	48,686	56,320	53,704	4.9%	248,442	291,201	336,341
EBIDTA Margin (%)	11.5	10.9	11.7	11.3	10.2	11.0	10.9		11.6	11.8	12.0
Other income	7,385	7,550	7,409	29,292	11,456	11,330	7,500	51.1%	40,250	40,250	41,713
Depreciation	8,602	8,252	8,535	35,023	8,305	9,099	8,450	7.7%	35,830	38,105	40,555
Interest	8,357	8,025	8,130	32,072	8,514	8,640	8,350	3.5%	34,187	29,212	27,412
PBT	39,421	42,004	59,074	169,730	43,324	49,911	44,404	12.4%	218,675	264,134	310,086
Tax	11,229	12,705	14,606	44,841	12,163	11,355	11,989	-5.3%	56,507	68,130	79,240
Effective tax rate (%)	28.5	30.2	24.7	26.4	28.1	22.8	27.0		25.8	25.8	25.6
PAT	28,192	29,299	44,467	124,889	31,161	38,556	32,415	18.9%	162,168	196,004	230,846
Minority interest	5,563	5,055	4,718	20,599	6,026	6,229	6,100	2.1%	24,657	28,086	31,313
Profit from associates	(339)	(75)	118	(943)	(205)	(101)	(150)	-33.0%	(600)	400	500
Consolidated PAT	22,290	24,169	39,868	103,348	24,930	32,226	26,165	23.2%	136,911	168,318	200,033
Extra-ordinary items	-	1,360	-	1,360	-	-	-		-	-	-
Reported PAT	22,290	25,529	39,868	104,708	24,930	32,226	26,165	23.2%	136,911	168,318	200,033
% change yoy											
Net sales	23.0	17.3	10.4	17.1	33.6	19.3	14.8		17.1	15.0	13.9
EBIDTA	22.6	12.0	4.8	13.9	23.0	15.0	9.6		19.7	17.2	15.5
Other income	38.8	32.1	43.7	29.2	64.9	53.4	1.6		37.4	-	3.6
Interest	7.2	(1.4)	15.3	2.6	12.6	3.4	(0.1)		6.6	(14.6)	(6.2)
Depreciation	18.0	12.7	10.9	18.8	(13.8)	5.8	(1.8)		2.3	6.3	6.4
PBT	30.6	18.1	6.2	17.8	47.8	26.6	12.6		28.8	20.8	17.4
Adj PAT	29.4	17.6	10.1	20.6	46.5	44.6	17.4		32.5	22.9	18.8
Reported PAT	22.5	24.2	10.1	20.8	46.5	44.6	17.4		30.8	22.9	18.8

Source: Company, JM Financial

Exhibit 2. P&M business performance

INR mn	2QFY23	3QFY23	4QFY23	FY23	1QFY24	2QFY24	FY24E	FY25E	FY26E
P&M Order inflows	372,670	457,380	611,030	1,721,900	503,550	730,380	2,064,246	2,326,999	2,629,832
YoY growth	23.7%	20.3%	0.0%	19.2%	79.3%	96.0%	19.9%	12.7%	13.0%
Revenue	281,160	314,250	433,450	1,250,047	327,180	349,090	1,495,803	1,746,188	2,001,818
YoY growth	23.6%	15.4%	8.3%	15.8%	47.9%	24.2%	19.7%	16.7%	14.6%
EBITDA	22,974	26,814	40,015	107,540	24,510	25,794	130,489	161,015	189,745
YoY growth	10.2%	16.2%	-2.3%	6.6%	34.8%	12.3%	21.3%	23.4%	17.8%
EBITDA Margin (%)	8.2	8.5	9.2	8.6	7.5	7.4	8.7	9.2	9.5
P&M PAT	13,630	17,750	26,480	67,760	14,380	15,470	86,095	110,651	133,423
P&M EPS	9.7	12.6	18.8	48.2	10.2	11.3	62.6	78.8	95.0
YoY growth	10.4%	21.1%	-3.4%	6.9%	45.3%	16.0%	29.9%	25.7%	20.6%

Source: Company, JM Financial

Exhibit 3. L&T segmental performance

INR mn	Revenue			EBITDA Margin	
	2QFY24	2QFY23	YoY	2QFY24	2QFY23
Infrastructure	246,130	193,700	27.1%	5.4	6.6
Power	7,400	9,000	-17.8%	8.2	3.2
Heavy Engineering	8,260	6,800	21.5%	18.0	16.4
IT & Technology services	111,820	101,510	10.2%	20.2	21.9
Defence Engineering	10,600	7,760	36.6%	12.5	20.4
Developmental projects	18,490	13,440	37.6%	38.7	5.2
Hydrocarbon	60,480	46,860	29.1%	9.7	9.7
L&T Finance Holdings	30,840	31,520	-2.2%	17.0	20.3
Others	16,220	17,047	-4.9%	20.0	15.6
Total	510,240	427,637	19.3%	11.0	11.5
- Domestic	291,260	272,907	6.7%		
- International	218,980	154,730	41.5%		

Source: Company, JM Financial

Exhibit 4. Order backlog and order inflow movement

INR mn	Order backlog			Order inflows		
	Sep-23	Sep-22	YoY	2QFY24	2QFY23	YoY
Infrastructure	3,019,918	2,687,520	12.4%	279,900	250,580	11.7%
Heavy Engineering	41,938	53,348	-21.4%	7,350	12,900	-43.0%
Defence & shipbuilding	235,516	142,342	65.5%	16,600	4,780	247.3%
Power	65,815	81,159	-18.9%	13,300	10,200	30.4%
Hydrocarbon	990,512	608,551	62.8%	388,110	74,210	423.0%
Services				161,150	146,470	10.0%
Others	153,641	150,890	1.8%	25,120	20,000	25.6%
Total	4,507,340	3,723,810	21.0%	891,530	519,140	71.7%
- Domestic	2,929,771	2,681,143	9.3%	294,660	346,000	-14.8%
- International	1,577,569	1,042,667	51.3%	596,870	173,140	244.7%

Source: Company, JM Financial

Exhibit 5. Group Balance sheet

INR bn	Mar-23	Sept-23	Incr/(Decr)
Equity & Reserves	893	784	(109)
Non-controlling interest	142	150	8
Borrowings	1,186	1,198	12
Financial Services	820	761	(59)
Development Projects	179	168	(11)
Others	187	269	82
Sources of Funds	2,221	2,132	(89)
Fixed Assets	164	176	12
Intangible Assets & Investment Property	293	283	(10)
Loans towards Financing Activities	738	724	(14)
Finance lease receivable	62	59	(3)
Net Non-Current Assets	180	190	10
Current Investments, Cash & Cash Equivalents	581	474	(107)
Net Current Assets	193	217	24
Assets held for sale (net)	10	10	-
Application of Funds	2,221	2,132	(89)

Source: Company, JM Financial

Exhibit 6. Share in Profit/ (Loss) of JVs/ Associates

INR bn	2QFY24	2QFY23
L&T Power JVs	(0.04)	0.01
L&T IDPL group	(0.0)	(0.32)
Others*	(0.14)	(0.03)
Total	(0.10)	(0.34)

Source: Company, JM Financial; *: mainly includes Hydrocarbon and Defence JVs

Exhibit 7. SoTP based price target of INR 3,380

Key subsidiaries (INR bn)	Valuation method	Value driver	Multiple (x)	Value	L&T's stake	L&T's value	INR/share
P&M business (A)	PEX FY26E PAT	133.4	25.0	3,340	100.0%	3,340	2,430
L&T Finance Holdings	Mcap*	330	0.8^	264	66.0%	174	127
LTIMindtree	Mcap*	1,497	0.8^	1,198	68.7%	823	598
LTTS	Mcap*	441	0.8^	353	73.8%	260	189
Total value of listed subsidiaries (B)						1,257	915
Infrastructure Development (C)	P/B (capital invested)	58	0.9	49	100.0%	49	36
Target price (A+B+C)						4,646	3,380

Source: Company, JM Financial; *: as on 31st October 2023; ^: @20% holding company discount

Key conference call takeaways

- **Guidance strengthened on inflows and execution; cut on margins:** L&T expects to surpass its FY24 order inflow guidance of 10-12% growth and revenue growth guidance of 12-15% led by strong 1HFY24 performance. Lowers P&M margin guidance from 9% to range of 8.5-9% for FY24E due to expected delay in certain newer orders hitting margin recognition threshold even as the older legacy (pre-Covid) orders continue to report lower margins. Orders adding up to about 60% of the order backlog are yet to cross margin recognition threshold. FY24E margin guidance is without any benefit of expected claims.
- **P&M margins weak** at 7.4% in 2QFY24 due to pressure in legacy (pre-Covid) projects owing to time and cost overruns. Such legacy projects are likely to be completed by 3Q/4QFY24E paving the way for better margins in FY25E.
- **Prospects pipeline strong** at INR 8.8tn (+39% YoY) for H2FY24E. It was mainly driven by Infrastructure (INR 5.06tn, +11% YoY) and Hydrocarbons (INR 2.9tn, up 2.6x YoY). L&T talked about mega sized hydrocarbon orders from Saudi Arabia and Qatar in the pipeline.
- **TOD monetization in Hyderabad metro:** L&T sold land worth INR 10.45bn and booked a gain of INR 5.12bn which boosted the overall profitability.
- **Hyderabad metro performance:** Average ridership improved to 462k/day in 2QFY24 (1QFY24: 422k/day) with peak ridership at 547k during 2QFY24. Cumulatively, L&T has received state support of INR 9bn till Oct-23. Balance support of INR 21bn is likely to be received over the next two years.

Financial Tables (Consolidated)

Income Statement		(INR mn)				
Y/E March	FY22A	FY23A	FY24E	FY25E	FY26E	
Net Sales	1,565,212	1,833,407	2,147,060	2,469,669	2,813,927	
Sales Growth	15.1%	17.1%	17.1%	15.0%	13.9%	
Other Operating Income	0	0	0	0	0	
Total Revenue	1,565,212	1,833,407	2,147,060	2,469,669	2,813,927	
Cost of Goods Sold	997,385	1,166,153	1,346,206	1,550,952	1,767,146	
Personnel Cost	297,335	372,141	416,798	458,478	504,326	
Other Expenses	88,319	87,580	135,613	169,038	206,115	
EBITDA	182,173	207,533	248,442	291,201	336,341	
EBITDA Margin	11.6%	11.3%	11.6%	11.8%	12.0%	
EBITDA Growth	16.6%	13.9%	19.7%	17.2%	15.5%	
Depn. & Amort.	29,480	35,023	35,830	38,105	40,555	
EBIT	152,694	172,510	212,612	253,096	295,786	
Other Income	22,671	29,292	40,250	40,250	41,713	
Finance Cost	31,257	32,072	34,187	29,212	27,412	
PBT before Excep. & Forex	144,107	169,730	218,675	264,134	310,086	
Excep. & Forex Inc./Loss(-)	0	0	0	0	0	
PBT	144,107	169,730	218,675	264,134	310,086	
Taxes	42,166	44,841	56,507	68,130	79,240	
Extraordinary Inc./Loss(-)	969	1,360	0	0	0	
Assoc. Profit/Min. Int.(-)	16,217	21,542	25,257	27,686	30,813	
Reported Net Profit	86,693	104,708	136,911	168,318	200,033	
Adjusted Net Profit	85,724	103,348	136,911	168,318	200,033	
Net Margin	5.5%	5.6%	6.4%	6.8%	7.1%	
Diluted Share Cap. (mn)	1,405	1,406	1,374	1,374	1,374	
Diluted EPS (₹)	61.0	73.5	99.6	122.5	145.5	
Diluted EPS Growth	21.3%	20.5%	35.5%	22.9%	18.8%	
Total Dividend + Tax	30,911	33,721	46,730	46,159	53,455	
Dividend Per Share (₹)	22.0	24.0	34.0	33.6	38.9	

Source: Company, JM Financial

Cash Flow Statement		(INR mn)				
Y/E March	FY22A	FY23A	FY24E	FY25E	FY26E	
Profit before Tax	145,077	171,090	218,675	264,134	310,086	
Depn. & Amort.	29,480	35,023	35,830	38,105	40,555	
Net Interest Exp. / Inc. (-)	31,257	32,072	34,187	29,212	27,412	
Inc (-) / Dec in WCAP.	-2,490	7,991	-61,314	-61,694	-66,462	
Others	0	0	0	0	0	
Taxes Paid	-39,211	-39,130	-51,507	-63,130	-74,240	
Operating Cash Flow	164,112	207,046	175,871	206,627	237,351	
Capex	-21,146	-52,225	-45,000	-45,000	-45,000	
Free Cash Flow	142,966	154,821	130,871	161,627	192,351	
Inc (-) / Dec in Investments	233	-51,949	-3,000	-5,000	-5,000	
Others	5,111	-23,994	-10,600	-9,600	-9,500	
Investing Cash Flow	-15,803	-128,168	-58,600	-59,600	-59,500	
Inc / Dec (-) in Capital	1	0	-99,999	0	0	
Dividend + Tax thereon	-30,911	-33,721	-46,730	-46,159	-53,455	
Inc / Dec (-) in Loans	-91,370	-49,548	-20,000	-20,000	-20,000	
Others	1,088	40,056	-24,187	-19,212	-17,412	
Financing Cash Flow	-121,193	-43,214	-190,915	-85,371	-90,867	
Inc / Dec (-) in Cash	27,117	35,664	-73,645	61,655	86,984	
Opening Cash Balance	162,415	189,532	225,196	151,551	213,207	
Closing Cash Balance	189,532	225,196	151,551	213,207	300,191	

Source: Company, JM Financial

Balance Sheet		(INR mn)				
Y/E March	FY22A	FY23A	FY24E	FY25E	FY26E	
Shareholders' Fund	824,077	893,259	883,441	1,005,601	1,152,179	
Share Capital	2,810	2,810	2,749	2,749	2,749	
Reserves & Surplus	821,267	890,449	880,692	1,002,852	1,149,430	
Preference Share Capital	0	0	0	0	0	
Minority Interest	129,661	142,413	167,070	195,155	226,468	
Total Loans	1,234,682	1,185,134	1,165,134	1,145,134	1,125,134	
Def. Tax Liab. / Assets (-)	-18,008	-33,544	-38,544	-43,544	-48,544	
Total - Equity & Liab.	2,170,412	2,187,262	2,177,101	2,302,346	2,455,237	
Net Fixed Assets	439,864	457,066	466,236	473,131	477,576	
Gross Fixed Assets	488,388	510,240	555,240	600,240	645,240	
Intangible Assets	74,770	77,987	77,987	77,987	77,987	
Less: Depn. & Amort.	134,997	160,652	196,482	234,587	275,142	
Capital WIP	11,703	29,491	29,491	29,491	29,491	
Investments	396,034	447,983	450,983	455,983	460,983	
Current Assets	2,317,731	2,336,438	2,539,872	2,832,133	3,165,829	
Inventories	59,433	68,288	77,282	88,085	99,571	
Sundry Debtors	522,165	526,864	711,765	818,712	932,836	
Cash & Bank Balances	189,532	225,196	151,551	213,207	300,191	
Loans & Advances	65,363	6,072	5,882	6,766	7,709	
Other Current Assets	1,481,237	1,510,019	1,593,391	1,705,364	1,825,522	
Current Liab. & Prov.	983,217	1,054,225	1,279,990	1,458,901	1,649,151	
Current Liabilities	511,442	497,841	676,221	770,740	871,249	
Provisions & Others	471,774	556,384	603,769	688,161	777,901	
Net Current Assets	1,334,515	1,282,213	1,259,883	1,373,232	1,516,678	
Total - Assets	2,170,412	2,187,262	2,177,101	2,302,346	2,455,237	

Source: Company, JM Financial

Dupont Analysis						
Y/E March	FY22A	FY23A	FY24E	FY25E	FY26E	
Net Margin	5.5%	5.6%	6.4%	6.8%	7.1%	
Asset Turnover (x)	0.7	0.8	1.0	1.1	1.2	
Leverage Factor (x)	2.8	2.5	2.5	2.4	2.2	
RoE	10.8%	12.0%	15.4%	17.8%	18.5%	

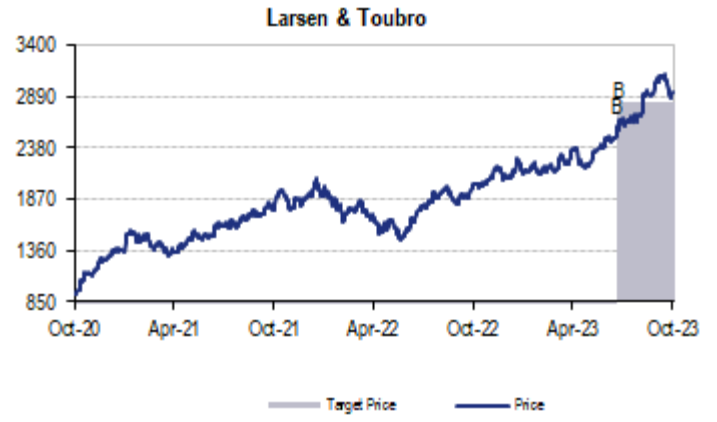
Key Ratios						
Y/E March	FY22A	FY23A	FY24E	FY25E	FY26E	
BV/Share (₹)	586.6	635.7	635.7	731.7	838.3	
ROIC	5.8%	7.0%	8.6%	9.8%	11.0%	
ROE	10.8%	12.0%	15.4%	17.8%	18.5%	
Net Debt/Equity (x)	0.9	0.7	0.7	0.6	0.4	
P/E (x)	27.7	26.0	29.4	23.9	20.1	
P/B (x)	2.9	3.0	4.6	4.0	3.5	
EV/EBITDA (x)	17.1	15.8	18.9	15.8	13.4	
EV/Sales (x)	2.0	1.8	2.2	1.9	1.6	
Debtor days	122	105	121	121	121	
Inventory days	14	14	13	13	13	
Creditor days	135	112	130	129	128	

Source: Company, JM Financial

History of Recommendation and Target Price

Date	Recommendation	Target Price	% Chg.
20-Jul-23	Buy	2,745	
26-Jul-23	Buy	2,835	3.3
1-Nov-23	Buy	3,380	19.2

Recommendation History



APPENDIX I

JM Financial Institutional Securities Limited

Corporate Identity Number: U67100MH2017PLC296081

Member of BSE Ltd. and National Stock Exchange of India Ltd.

SEBI Registration Nos.: Stock Broker - INZ000163434, Research Analyst - INH000000610

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Investment in securities market are subject to market risks. Read all the related documents carefully before investing.

Definition of ratings	
Rating	Meaning
Buy	Total expected returns of more than 10% for stocks with market capitalisation in excess of INR 200 billion and REITs* and more than 15% for all other stocks, over the next twelve months. Total expected return includes dividend yields.
Hold	Price expected to move in the range of 10% downside to 10% upside from the current market price for stocks with market capitalisation in excess of INR 200 billion and REITs* and in the range of 10% downside to 15% upside from the current market price for all other stocks, over the next twelve months.
Sell	Price expected to move downwards by more than 10% from the current market price over the next twelve months.

* REITs refers to Real Estate Investment Trusts.

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