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L&T hopeful of a recovery in the second half

The management believes that the current fiscal will play out pretty much like the last, which saw a sudden pick-up in investment in the second half.

By **ANTO T. JOSEPH**, **May 18, 2021**
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S.N. Subrahmanyan, managing director and CEO, Larsen & Toubro

Image: By special arrangement

S.N. Subrahmanyan, managing director and CEO of Larsen & Toubro (L&T), didn't mince words as he wrapped up an hour-long virtual interaction with the media on May 14.

"Last year has been one of the toughest in the company's history," was his candid admission.

L&T is an informal but reliable barometer of India's infrastructure sector. The engineering and construction giant, which survived the first wave of the pandemic nearly unscathed, "despite a dismal first half", is now facing a litmus test with the second wave.

Subrahmanyan counted many unknowns for the year ahead—the surging pandemic, supply-chain disruption, increasing commodity prices, migration and disruption of workforce, and so on. "The company will need to calibrate its growth based on the basis of the operational environment and conditions resulting from this. Performance in the challenging 2020-21 reaffirms our strong position, stability in our performance, and our ability to deliver in line with our strategic priorities in spite of the fact that almost six months were lost. While the headwinds are there, we are still well-positioned to meet the expectations of the customers and increase the value of our shareholders," he said.

The management however doesn't read too much into the current slowdown driven by local lockdowns. It believes that the current financial year will play out pretty much the same as the last fiscal, which saw a sudden pick-up in investment in the second half. In the first quarter of the 2021-22, the central and state governments are preoccupied with the safety and healthcare of the people. But L&T expects a surge in investments from the need to consume funds allocated in the Union Budget to be eligible for an additional allocation. Like in the last fiscal, there is a bias towards the second half in the current fiscal as well. L&T hopes that things will improve from August onwards.

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The disruption in the availability of the workforce has been a critical issue. "In the first wave, many workers went to their villages. With a huge effort, we brought many of them back. We had 245,000 workers on our rolls in March 2020. Now, we have around 171,000 workers. It shows that some people have gone back. An intensified campaign is on at the work sites and labour camps to tell them to stay back, which is clearly a better option for them than the conditions back in their respective villages," said Subrahmanyan.

He is confident that the company would continue to build and execute on its commitments.

R. Shankar Raman, whole-time director and chief financial officer, said the company has been reporting consistent improvement quarter-on-quarter right from the dismal Q1 of

FY21. “Even though I realise that our business is not [a] quarter-on-quarter business being a project company, it is very important that we measure the progress that we made in the very challenging environment,” he said during the conference call.

In the March quarter, the company reported a rise of 3% in consolidated net profit year-on-year at ₹3,293 crore on the back of higher revenue from operations. It reported a 9% growth in consolidated revenues to ₹48,088 crore, showing a return to pre-Covid-19 levels.

“We are not hard-coding the numbers on guidance but are sharing our thinking… that we are looking forward to growth over 2020-21. Yes, it is based on an assumption that the second wave of Covid-19 will leave us with no further damage in a month or two,” said Raman.

For the company, the bleeding Hyderabad Metro Rail project continues to be awork in progress. It allocated about ₹1,000 crore last year and has to set aside another ₹2,000 crore this year for solving the vexing debt-equity problems. The debt was contracted based on700,000-800,000 people travelling every day, but it has fallen far short of the target, owing to the pandemic.

“At the current level or the projected improved level of ridership, the debt is not sustainable. We need to refinance the debt and push liability back, and convert a portion of the debt into equity or preferential equity. Third, we also need to get some additional equity investors. All these are works in progress,” the CFO told analysts during a separate conference call, adding that he doesn’t expect the metro project to suck in more money in 2021-22.

L&T was looking to exit from ₹18,000-crore Hyderabad Metro, the world’s largest metro rail project executed in the public-private-partnership model, as a part of its overall plans to move away from non-core businesses.

Apart from the metro project, the company doesn’t see any significant capital allocation to any of its other subsidiaries. “There is no need to allocate capital for our services businesses. They are generating adequate cash. Last time when we made a large allocation was for the Mindtree acquisition, and that has played out well. On the engineering and construction side, the requirement has been for working capital. We have to purchase strategic equipment whenever we win large projects and such, but the cost is amortised over a period of time. Hence, they won’t be a big drainer. For the financial services sector, we had allocated ₹2,000 crore last year to participate in the rights issue to maintain our shareholding. We don't expect any significant capital allocation in the next couple of years," said the CFO.

"We will also look at unlocking power development assets. We expect it to generate some cash flow as well," he said.

The order inflow for the January-March quarter stood at ₹50,651 crore, lower by 12% over the corresponding period of the previous year with deferment of contract awards, but L&T has thrown up a strong operating performance with a stronger balance sheet, according to stock analysts.

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"Balance sheet improvement was a huge positive as net debt-to-equity ratio (including minorities and adjusted for current investments) improved to 1x from 1.5x in 2019-20. This was driven by completion of the sale of the electrical and automation business (to Schneider Electric), working capital cycle improvement to 22.3% of sales from 23.7%. The last fiscal brought out the core strengths of the L&T's re-aligned business model as a pure EPC player, even though P&L was impacted," Nilesh Bhaiya and Pratik Singh, research analysts at Motilal Oswal, point out.

The consolidated order book of the group stood at ₹3,27,354 crore as of March 31, 2021, registering a growth of 8% over March 31, 2020, with order book/revenue ratio of 3.5x being the highest in many years.

The company received orders worth ₹1,75,497 crore at the group level during the year ended March 31, 2021, registering a decline of 6%. International orders stood at ₹47,951 crore during the year, down 27% of the total order inflow. The bulky high-speed rail order gave a big push to its domestic order book. In terms of clientele, central and state governments make up 9% and 31%, respectively, while PSUs hold another 42%. The private sector contributes the remaining 18%. This gives a clear picture of the infrastructure investment climate in the country.

Motilal Oswal said Covid 2.0 has brought on similar challenges as last year, but the construction activity has been ongoing unlike last year and hence, the impact should be lower than last time.

According to Aditya Bhartia and Veenit Pasad of Investec Capital Services (India), the L&T management expects order flows and revenues to grow at 13%-16% according to a 2021-22 estimate, despite lockdowns in several states. "Order pipeline is strong (around ₹9.1 lakh crore), and the management is not seeing the same level of execution challenges (labour availability, restrictions) it faced last year. It is also confident of sustaining margins at current levels. We feel that the company should be able to deliver at least the lower end of the guidance," they said in a research report.

Everyone hopes the company will get back on track by August.

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