EKI Energy

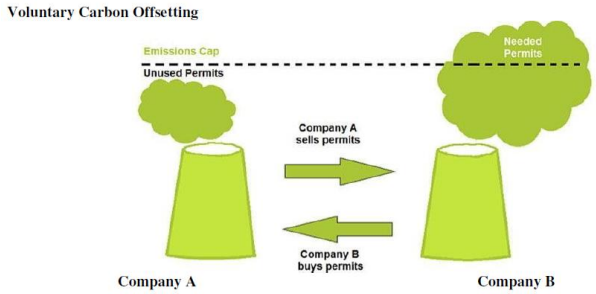
Company Overview

Incorporated in 2011, EKI Energy has been in the business of Climate Change Advisory Services, Carbon Credits Trading, Business Excellence Advisory and Electrical Safety Audits. The Company offers its services to various clients in the government and private sectors like power generation, waste management, clean development mechanism, airports and many more industries.

In 2011 the Company started the business of climate change advisory services involving consultancy for validation, registration, monitoring, verification, issuance and trading of eligible Carbon Credits Projects as from CDM (Clean Development Mechanism) /VCS (Verified Carbon Standard) Project. With the response from the market, the company further expanded it services in 2015 into carbon credits trading and also started various other services like Business Excellence Advisory Services & Training Services. With increasing awareness among the community with regards to the environment safety and energy conservation, the company has also entered in to Electrical Safety Audits.

Service Portfolio

1. ***Climate Change Advisory Services:*** Offers Carbon Neutrality services to various industries like - Bio-Methanation project, Renewable Power Project (Wind, Solar, Hydro, Geo Thermal), Waste Management - Landfill project, Compost formation project, Energy Efficiency Project, Cookstove Project, Water Purification Project. Provides end to end solution to achieve carbon neutrality.
   The business of climate change advisory services involves assistance for validation, registration, verification, issuance and trading of eligible Carbon Credits Projects as CDM (Clean Development Mechanism) /VCS (Verified Carbon Standard) Project. This process is done on the seller side to make their projects viable for carbon trading.
   Carbon offsetting means compensating for the carbon dioxide pollution one is making by preventing the same amount of pollution from happening somewhere else. Carbon offsetting is the way to compensate for the damage done by an individual or a company by reducing or absorbing emitting carbon dioxide through any activity. Once the organizations have decided to acquire carbon offsets for their carbon neutrality goals, next big hurdle is to select the right kind of carbon offset. The company conducts all the due diligence to ensure that client gets the right kind of offsets from the right project that suits their organization's interest and priorities.



   The Company studies the project requirements, credibility, quantum and profile of the buyer to offer the suitable credits at a competitive price, thereby making its margins. It has various projects registered with

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it holding carbon credits and once it finds a suitable buyer for its credits, the issuance fees for the said projects are paid to make them tradable. Apart from registered projects in its portfolio it may also look for sellers across the globe with requisite carbon credits.

2. ***Carbon Credits Trading:*** Carbon credit represents ownership of the equivalent of one metric ton of carbon dioxide that can be traded, sold or retired. If an organization is regulated under a cap-and-trade system (e.g., the California Cap and Trade Program) it likely has an allowance of credits it can use towards its cap. If the organization produces fewer tons of carbon emissions than it is allocated, the organization can trade, sell or hold the remaining carbon credits. When a credit is sold, the buyer is purchasing the seller's allowance of emissions. A credit becomes tradeable because of a very real reduction in emissions.
3. ***Business Excellence Advisory and Training Services:*** Provides end to end solutions for ISO standards implementation within an organization and even ensures proper maintenance of standards that are being implemented through a wide range of professional management training and consultancy programmes which aims to satisfy the clients' requirements and needs.
4. ***Electrical Safety Audits:*** An Electrical Safety Audit (ESA) is a systematic approach to evaluate potential hazards and to recommend suggestions for improvements. It is an important tool for identifying deterioration of standards, areas of risks or vulnerability, hazards and potential accidents in plants for determining actions to minimize hazards. Electrical Safety Audit is performed by enquiry, inspection, testing and verification.

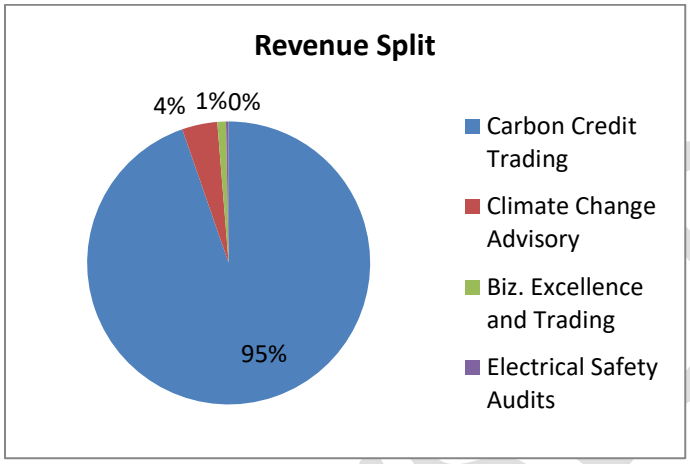
Clientele

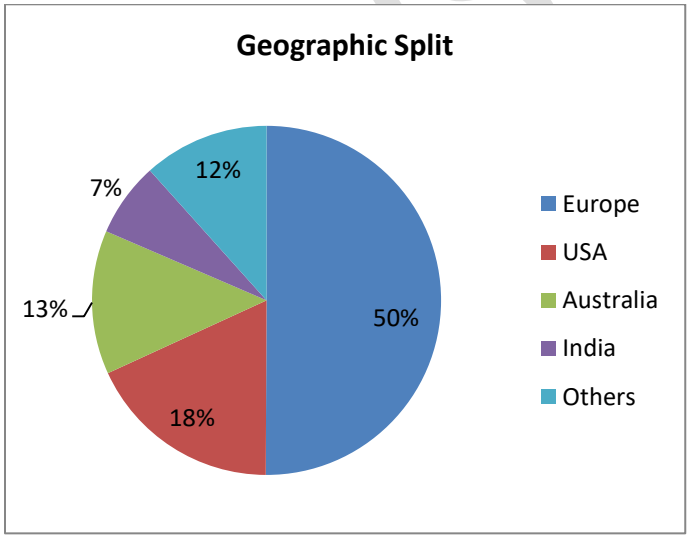
The Company has a broad client base in India and various countries like Australia, USA, Germany, Europe and many more. It has widespread reach in India and abroad including customers like:

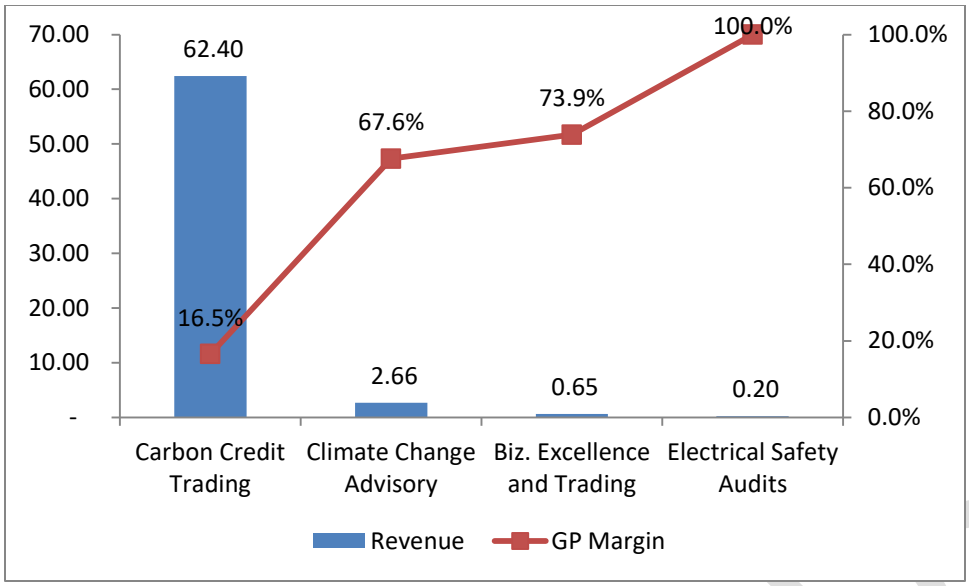
Financial Snapshot (04/04/21)

MARKET CAP (RS CR)	87,158
P/E	46.5x
P/FCF	92.6x
P/B	32.6x
EV/EBITDA	32.1x
ROCE	37.4%
ROE	32.7%
Debt/Equity	0.92x
DIV YIELD.(%)	4.01%
Working Capital Days	45.6

Revenue and Gross Margin Analysis (FY20 Sales of ₹65.9cr)







SWOT Analysis

Strengths

- First listed company in the world in the Carbon Credit trading and Carbon offsetting space
- Business is reasonably diversified between Carbon Credit trading and Climate Change advisory
    - Business is also reasonably diversified with no particular region contributing more than 50% of the revenue
- Has a strong clientele base both locally and internationally with repeat business
- Operates through a very low asset base which requires limited Capital Expenditure and hence also as an asset turnover of 9.18x
- The Company seems to have some degree of float as it doesn't hold any inventory and payables far exceed the receivables
    - Could have infinite returns to capital since no investment is required
- Asset Turnover is high enough to support super high ROE of 114%

Weaknesses

- Company has been forced into Carbon Credit trading despite the fact that Climate Advisory seems to be their main and preferred line of business
    - Carbon Credit trading brings in the bulk of revenues but gross margins are a measly 16%
    - The Advisory segment may take a long time to take off but till then the Company is more of a trading company than anything else
- Top five clients contributed to approximately 60.68% of the revenue from operations based on Restated Financial Statements for the period ended June 30, 2020 which signifies that diversification among clients is not the best
    - However considering the size of the Company it can be acceptable
- Management seems to be questionable due to practice of personal borrowing through the Company
- Company has extremely low Operating Leverage due to the source of Revenue coming from Trading

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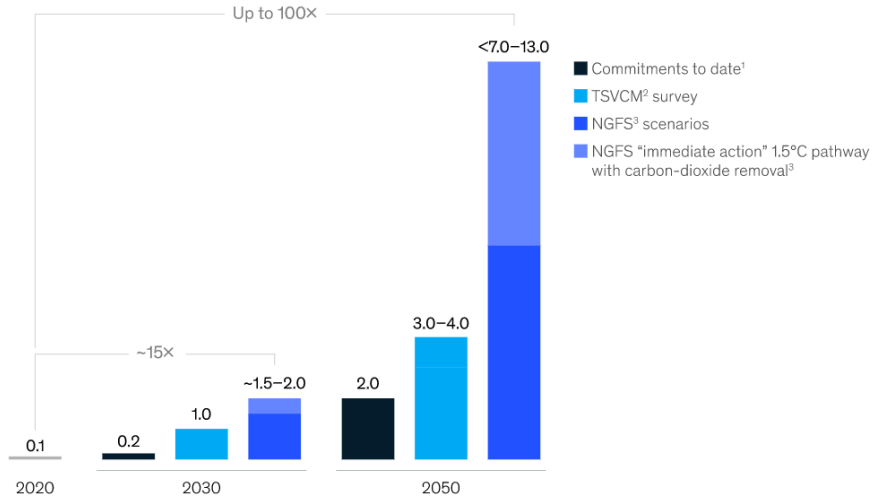
Opportunities

- Under the 2015 Paris Agreement, nearly 200 countries have endorsed the global goal of limiting the rise in average temperatures to 2.0 degrees Celsius above preindustrial levels, and ideally 1.5 degrees
    - More companies are aligning themselves with this agenda: in less than a year, the number of companies with net-zero pledges doubled, from 500 in 2019 to more than 1,000 in 2020
- Taskforce on Scaling Voluntary Carbon Markets (TSVCM), sponsored by the Institute of International Finance (IIF) with knowledge support from McKinsey, estimates that demand for carbon credits could increase by a factor of 15 or more by 2030 and by a factor of up to 100 by 2050
    - Overall, the market for carbon credits could be worth upward of $50 billion in 2030 and from approx. $0.6bn in 2019
- Voluntary markets are the driving force for the market as companies take it upon themselves to reduce their carbon footprint

Voluntary demand scenarios for carbon credits, gigatons per year



[1]These amounts reflect demand established by climate commitments of more than 700 large companies. They are lower bounds because they do not account for likely growth in commitments and do not represent all companies worldwide.
[2]TSVCM = Taskforce on Scaling Voluntary Carbon Markets. These amounts reflect demand based on a survey of subject-matter experts in the TSVCM.
[3]NGFS = Network for Greening the Financial System. These amounts reflect demand based on carbon-dioxide removal and sequestration requirements under the NGFS's 1.5°C and 2.0°C scenarios. Both amounts reflect an assumption that all carbon-dioxide removal and sequestration results from carbon credits purchased on the voluntary market (whereas some removal and sequestration will result from carbon credits purchased in compliance markets and some will result from efforts other than carbon-offsetting projects).
Source: NGFS; TSVCM; McKinsey analysis

Threats

- Carbon offset generation has been historically beset by scandals and whereas fraudsters sold same carbon credits twice and charged EU Value Added Tax (VAT) on both the buyer and seller leg
    - Some credits have turned out to represent emissions reductions that were questionable at best
- Carbon offset projects have heavily dependent on the aviation industry as clients
- In the past, oversupply of credits from ex-Soviet Bloc countries that far outstripped demand from Western Europe caused the prices of certain credits to crash
- Large consultants like Mitcon Consultancy & Engineering Services Limited, Ernst & Young, Deloitte Haskins & Sells LLP, Price Waterhouse Coopers, and Emergent Ventures India could create a very large barrier to the business scaling
- While the increase in demand for carbon credits is significant, analysis by McKinsey indicates that demand in 2030 could be matched by the potential annual supply of carbon credits: 8 to 12 $GtCO_2$ per year

- Pricing is an issue: When verifying the quality of new credits—an important step in maintaining the market's integrity—suppliers endure long lead times and when selling those credits, suppliers face unpredictable demand and can seldom fetch economical prices
    - Overall, the market is characterized by low liquidity, scarce financing, inadequate risk-management services, and limited data availability
- Carbon credits are essentially a commodity with larger than expected fluctuations and lack of transparency in pricing

*Porter's 5 Forces (Score: 3/10) – Carbon Credit Market**

Threat of new entrants – High

- Carbon credit trading can take place a through both public and private market with the largest exchange being EU ETS
- Low capital requirements and limited global regulation allows anyone to enter in as a broker or trade on their own
- Very low chance of building long term relationships for repeat business

Threat of substitutes – Medium

- Companies can always switch to a more sustainable method of functioning with reduced emissions
- Much of the profitable market is driven by Voluntary market which can always choose not to buy carbon credits
- Compliance markets may find it very difficult to shift to not purchasing credits or shifting away from carbon offsetting projects in the short-term

Bargaining power of Suppliers – Medium

- Carbon credits are rather generic in nature and trade as a commodity so sellers can always choose their clients
- The Company could increase the seller's dependence by providing added services through consultancy although this is not a necessity for the seller

Bargaining power of Buyers – High

- Product is very commodity-like and traded on exchanges as well which gives it no differentiation
- Difficult for the Company to build a relationship based business with the product available through other means as well and switching costs being relatively low
- Size of the order can vary and be small which gives the buyer flexibility to defer or adjust purchases
- Prices are not always transparent and buyers may not have complete information

Rivalry amongst competitors – Medium

- Despite being the first Indian company to enter into this business, the clientele mostly operates in the developed world where quite a few alternatives, including exchanges already exist
- Competitors can be trading/consultancy companies or exchanges
- Large potential in industry growth would allow enough space for competitors to grow and move into specialized offerings in the broader carbon credit/offset space
- Low barriers to exit allows companies to wind up easily in times when trading is not profitable

Management Review

EKI Energy is a family run business with Mr. Manish Kumar Dabkara acting as the Chairman & Managing Director. He has 12 years of experience within the field. The promoter has purchased a BMW and Mercedes car, for a combined value of ₹1cr, by borrowing through the Company which is a major red flag. Although this was done before the Company went public, the debt is still on the books of the Company.

Management Effectiveness

	Mar-18	Mar-19	Mar-20
ROE	28%	41%	73%
ROCE	26%	34%	84%
ROIC	15%	30%	87%

High return on capital is driven by high Asset Turnover of 9.18. This is mainly due to the nature of the business with low capital requirement and the Company managing to have negative working capital due to zero inventory and Payables exceeding Receivables.

Name (Position)	Remuneration (₹ cr.)	Remuneration as a % of N. Profit
Manish Kumar Dabkara (Managing Director)	1.21	27.86%
Naveen Sharma (Director)	0.17	3.86%
Sonali Sheikh (Director)	0.08	1.95%
Priyanka Dabkara (Director)	0.18	4.13%

Management takes home a large proportion of Net Profit at nearly 28%.

Overall management doesn't seem the most trustworthy with allocation of ₹1.2cr on luxury cars (out of a total Gross Block of ₹1.64cr), raising red flags. Additionally, the promoter group / directors taking away more than a third of the Company's Net Profit as salaries is very astounding.

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Valuation

	Mar-21	Mar-22	Mar-23	Mar-24	Mar-25	Mar-26	Mar-27	Mar-28	Mar-29	Mar-30	Terminal Value
EBITDA	5.7	7.8	10.6	14.3	19.1	25.0	32.2	40.3	48.6	55.2	
Capex	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
WC Investment	4.6	6.9	10.4	15.5	23.2	34.6	51.8	77.4	115.7	173.0	
FCFF	**10.3**	**14.7**	**21.0**	**29.8**	**42.3**	**59.7**	**84.0**	**117.7**	**164.3**	**228.2**	**1,486.8**
Discount Rate	16.35%	16.35%	16.35%	16.35%	16.35%	16.35%	16.35%	16.35%	16.35%	16.35%	
Year	1	2	3	4	5	6	7	8	9	10	
PV of CF	8.9	10.9	13.3	16.3	19.8	24.1	29.1	35.1	42.1	377.2	
Sum of PVFCF	**576.7**										
PV of Equity	**577.6**										
PV per share	**840.316**										

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