Systematix

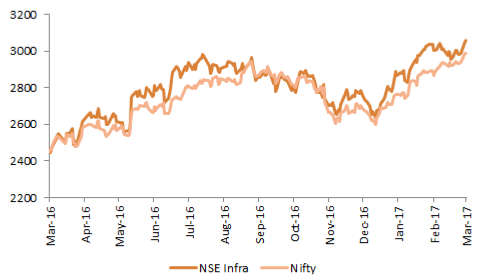
Institutional Equities

Indian Road Sector

27 March, 2017

SECTOR REPORT

NSE Infra vs Nifty



Source: Systematix Institutional Research

Not so slippery anymore; prefer well oiled and gripped companies

Road sector has been at the forefront of the proposed infra spend in the recent past given acute requirement and dynamic ministry leadership but has fallen short in delivery. The outlook is better given the tailwinds of low interest rates and improved regulatory environment (favourable exit policy, release of arbitration money, reimbursement of toll revenue loss of Rs9.2bn on demonetisation). We believe the segment will be encashed by select players with balance sheet & execution strength. We initiate coverage on Ashoka Buildcon, PNC Infratech, Sadbhav Engineering and Dilip Buildcon, given their superior management quality, limited gearing, healthy BOT portfolio with an average ~15-year residual life and a diversified EPC order book focused on irrigation/mining/airports/power distribution besides roads. While IRB Infrastructure is the largest player with 19 BOT assets, we would wait for a reduction of +3x leverage and clarity on InVIT. Ashoka Buildcon and PNC Infratech are our top picks.

Policy reforms showed positive results in FY16-17; expected to continue: Given the government's focus on infrastructure, the thrust continues on roads, with no dearth of funding. Numerous policy reforms undertaken by the new government scaled up project awarding 3.2x and construction 1.4x to 10,098km and 6,029km respectively in FY16, from the lows of FY14. In YTD-FY17, private sector participation gained momentum, with 55% of NHAI awards in PPP (40% HAM, 15% pure BOT) v/s 30% in FY16. Intervention by the road ministry to address the financing issue, release of 75% of arbitration award money and speeding up the arbitration process will improve liquidity with developers.

However a delay in approvals to provide higher compensation under the new land law, delayed the possession of 80% land, a key criterion to award road projects. This combined with cautious lending for HAM projects (only 10 of 27 projects financially closed so far) translated into 16% yoy growth in Apr-Feb'17 awards to 9,655 km far less than the annual target of 25,000km. Similarly construction has been ~22km/day in FY17e (12-17km/day in FY14-16) v/s a target of +40km/day which can possibly be achieved only by FY20e.

Improved environment to benefit select serious players: The expected improvement in investment climate led by easing land acquisition, moderate competition (four-six players) and better pricing (recent bids won above NHAI cost) will lead to bigger and serious players garnering lion's share of the upcoming opportunity. Certain emerging positive trends are:

- New programs such as Chardham Pariyojana (Rs120bn), conversion into national highways in Maharashtra (Rs300bn) and Mumbai- Nagpur expressway (Rs330bn) will provide an impetus for highways development besides NHDP.
- Monetisation of stakes in operational road BOT projects through InVITs/project/holdco sale will assist in deleveraging and free up equity for new investments. Select players such as ASBL, SADE and DBL with proven orderbook execution track record (15%+ revenue CAGR over FY10-17e), will be able to bag additional road EPC/HAM orders on freeing up of capital.
- Our interactions with PE investors, asset owners (both listed and private) suggest that there is ample appetite for good road assets with stable cash flows, long-term average 5-6% traffic growth, 9-10% yields and equity IRR of 15-16%. A scenario of lower interest rates, favourable exit policy and streamlined regulations will add to their confidence. NHAI plans to monetise 75 operational projects of 4,500km under TOT model to sovereign/pension funds for 25-30 years, in return for an upfront one-time fee. Within our coverage universe, ASBL and SADE are scouting to sell partial/full stakes in certain operational road projects/portfolio.

Stock selection paramount - prefer companies with strong balance sheet and longer residual asset life: Our analysis of stock returns of listed companies in road BOT/EPC space indicates that only six of the 19 companies have consistently delivered positive returns in three of the four time periods (1/3/5/7 years), while IRB Infra has delivered positive returns in 2/4 time periods. This implies investors have rewarded companies that focused on core road BOT segments and diversified EPC operations in fast-growing segments, in addition to roads. However, the one-year return is muted across companies vs three year as 1) unavailability of land, heavy monsoon delayed execution of FY16-awarded projects leading to cut in FY17e revenue guidance by few companies thus impacting earnings and 2) sluggish YTDFY17 order awarding impacted order inflows. Key monitorables in the near term will be 1) execution ramp-up of existing EPC order book in FY18, 2) GDP growth outlook, as road traffic is linked to economy and 3) NHAI/MoRTH tender pipeline.

Sector recommendations

	CMP (Rs)	TP (Rs)	Upside (%)	Reco.
Ashoka Buildcon	186	231	24%	Buy
PNC Infratech	114	140	23%	Buy
Dilip Buildcon	349	411	18%	Accumulate
Sadbhav Engineering	310	335	8%	Hold
KNR Construction	181	185	2%	Hold
IRB Infrastructure	235	NA	NA	Not Rated
MEP Infrastructure	51	NA	NA	Not Rated

Source: Systematix Institutional Research

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Coverage Universe Snapshot

Table 1: Comparative analysis of coverage companies

	Ashoka Buildcon*		Sadbhav Engineering #		PNC Infratech #		Dilip Buildcon #	
	FY18e	FY19e	FY18e	FY19e	FY18e	FY19e	FY18e	FY19e
Bloomberg Code	ASBL IN		SADE IN		PNCL IN		DBL IN	
Market Cap (Rs bn)	35		50		27		48	
CMP (Rs)	186		310		114		349	
TP (Rs)	231		335		140		411	
Upside (%)	24%		8%		23%		18%	
SOTP break up (Rs)								
EPC	160 (69%)		193 (58%)		115 (82%)		361 (91%)	
BOT	71 (31%)		141 (42%)		25 (18%)		36 (9%)	
PE (x)	27.5	23.3	28.8	24.8	16.5	14.9	17.3	13.3
Core P/E(x)	11.8	10.7	20.2	17.5	12.9	11.7	15.5	12.0
P/B (x)	1.7	1.6	3.0	2.7	1.7	1.5	2.4	2.0
EV/EBITDA (x)	9.8	9.0	15.3	13.3	10.1	8.3	6.7	5.9
ROE (%)	6.3	7.1	11.0	11.4	10.6	10.6	14.7	16.3
ROCE (%)	9.1	9.8	10.5	12.6	12.6	14.0	18.8	20.4
OPM (%)	24.0	22.8	10.8	10.8	13.2	13.5	19.0	19.0
NPM (%)	3.9	4.0	5.0	5.1	7.8	7.3	5.0	5.6
D/E (x)	2.1	1.9	0.5	0.4	0.1	0.1	1.2	1.1
Sales (Rs mn)	32,734	36,909	38,058	43,264	22,594	26,819	56,847	65,659
EBITDA (Rs mn	7,861	8,405	4,115	4,689	2,981	3,629	10,824	12,454
PAT (Rs mn)	1,264	1,492	1,909	2,211	1773	1962	2,822	3,655
EPS (Rs)	6.8	8.0	11.1	12.9	6.9	7.6	20.6	26.7
OCF (Rs mn)	3,592	3,177	5,302	1,197	2,184	2,973	3,032	3,324
FCF (Rs mn)	3,112	2,697	4,702	597	1684	2473	1,532	1,824
FCF post investment (Rs mn)	3,112	2,697	4,702	597	(2,066)	(1,277)	(1,015)	(226)
Interest coverage ratio (x)	1.4	1.6	2.4	3.3	9.5	8.4	1.9	2.2
WC Days (days)	52	42	174	153	105	88	147	144
Debtors(days)	50	50	135	125	85	90	95	92
Asset Turnover(x)	0.2	0.3	3.7	4.0	3.7	4.0	2.4	2.6
EPC Order book (Rs mn)	84,051	106,248	96,468	100,204	94,613	107,794	132,209	136,550
EPC Order book/sales (x)	3.5	3.9	2.5	2.3	4.2	4.0	2.3	2.1
BOT Revenue (Rs mn)	6,819	7,274	11,890	13,268	6,374	7,059	NA	NA
FCFE CAGR (Rs mn)	61% (FY24e-30e)		52% (SIPL : FY22e-27e)		44% (FY19e-23e)		-	

*Source: Systematix Institutional Research; Note: * consolidated, # standalone*

Policy reforms showed positive results in FY16-17; expected to continue

Widespread road network in India, but the path lacks quality

- Development of India's extensive road network of ~5.23mn km is of prime importance for growth, as ~70% of freight and 85% of passenger traffic moves by road.
- Estimates suggest that freight traffic is set for 8% CAGR over FY12-32e, while 15% CAGR is envisaged for passenger traffic over the same period.
- Thus, rapid expansion, strengthening of road network and augmenting quality are imperative to provide last mile accessibility, better connectivity to rural areas and inter-modal transport development.

Table 2: Break-up of road network in India

	FY16 - length (kms)	Importance	% of total	
			Length	Traffic
National highways	100,475	Primary arterial roads running through length and breadth of the country, connecting state capitals, ports and industrial areas	2%	40%
State highways	148,256	State roads carry medium-to-heavy traffic and add significantly to the development of rural economy and industrial growth of the country	3%	60%
Major district roads	348,850	Major district roads link main and rural roads	95%	
Other district roads and village roads	46,04,433	• Rural connectivity, which is vital to generate higher agricultural incomes and • Productive employment opportunities		
Total	**52,32,310**			

Source: MORTH, Systematix Institutional Research

Table 3: Quality-wise break-up of national highways (NHs)

Lanes	Quality	Share in NH	Length in km
Four lane/six lane/eight Lane	Above required standards	24%	24,114
Double lane	Just meets standards	53%	53,252
Single lane/intermediate lane	Intermediate standards	23%	23,109
Total length of NHs			**100,475**

Only 24% of roads of the total national highway network are above-standard quality, thus creating a huge opportunity for developers in highway improvement

Source: MORTH, Draft document 12th Five Year Plan

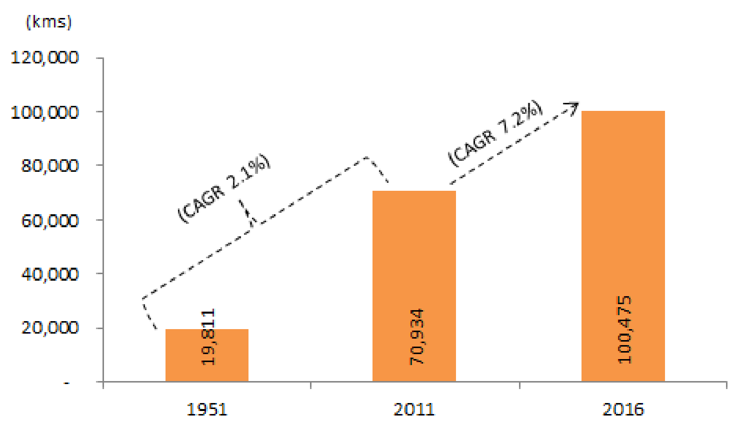
National highways – backbone of the country

As national highways constitute a significant part of the road network in India, NHAI initiated the largest and foremost infrastructure program - National Highway Development Programme (NHDP) in 1998. NHDP envisages widening, upgrading and rehabilitation of ~50,000km of highways in seven phases.

Phase I and II were launched in 1998 and were predominantly implemented under the EPC mode. From NHDP Phase III, private sector participation was encouraged, and awarding of road projects on public-private partnership gradually picked up from FY06 and soared during FY10-12, when all projects were tendered on either BOT toll or BOT annuity basis. Phase-wise details under NHDP are stated in annexure 1.

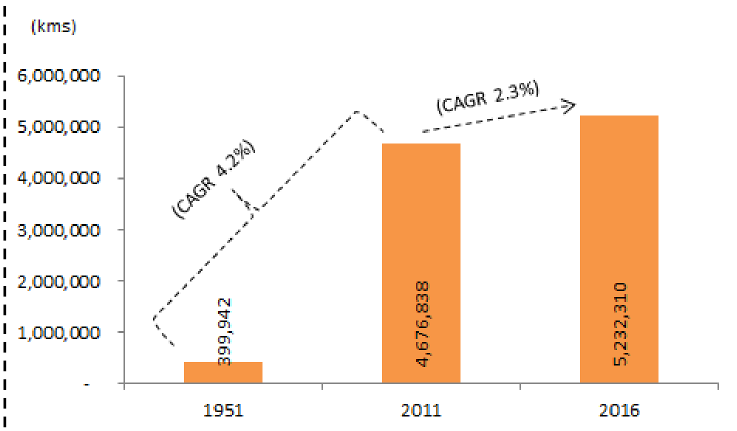
Widespread implementation of this program boosted 7.2% CAGR in national highways in the last five years v/s 2.1% over the last 60 years.

Chart 1: Strong 7.2% growth in NH network over last 5 years



Source: MORTH

Chart 2: Versus 2.3% CAGR in total road network



Source: MORTH

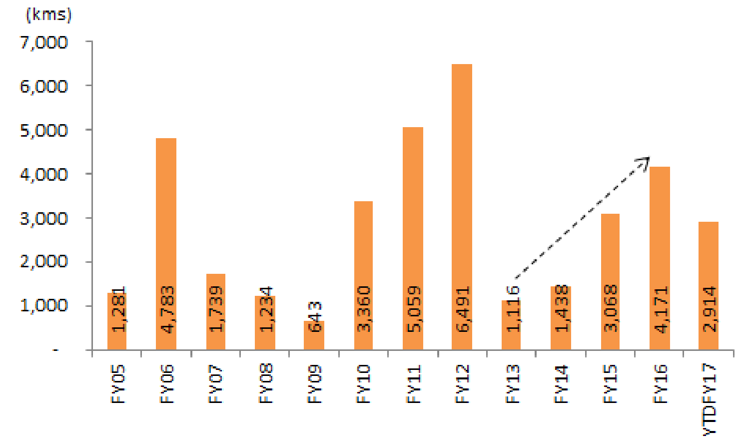
Bumpy ride for public-private partnership projects during FY06-16

Awarding of projects under NHDP picked up FY05 onwards. To reduce the strain on its finances and to enable effective utilisation of resources, the government encouraged private sector participation.

Use of standard bidding documents provided clarity, founded on a well-defined policy framework, which significantly enhanced the confidence of developers and financers and encouraged private sector investments.

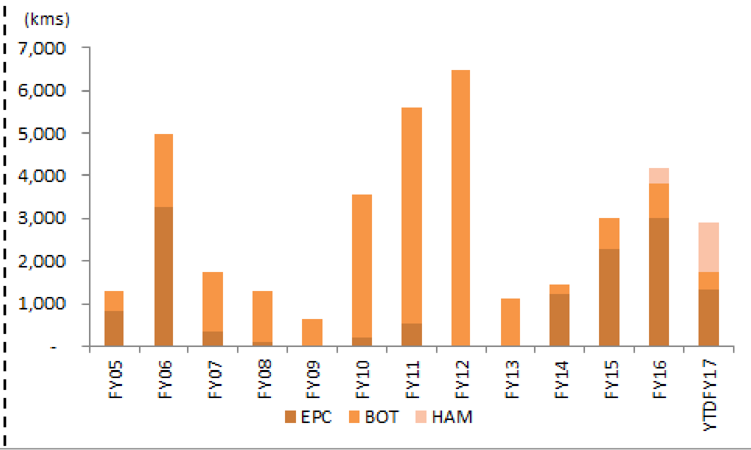
As per the government decision of April 2007, all new projects under various phases of NHDP were to be awarded on public-private partnership (PPP), first on built operate and transfer (BOT) toll basis, failing which to be taken up on BOT (annuity) basis. In the absence of any response from developers, the project would be taken up on EPC basis, with the approval of government.

Chart 3: NHAI awards catching up after FY13 plunge



Source: NHAI

Chart 4: NHAI awards break-up into EPC, BOT and HAM



Source: NHAI

Awarding of road projects soared 10x between FY09 and FY12. However, the next two years turned out to be very disappointing as the execution of projects awarded between FY09-12 did not take off for a variety of reasons listed below. At the same time, awarding of new projects plummeted as the high capital requirement for existing BOT projects resulted in developers falling into a debt trap.

What went wrong

Aggression in bidding: Within the infrastructure space, road sector was the only segment where orders were being finalised. This, along with tendering of projects under NHDP phase III and lucrative traffic expectation, led to intense competition and aggressive financial bidding by developers. Over estimation of traffic growth led to bidding for projects on premium/revenue share basis in most cases.

Undue delay in land acquisition and statutory clearances: To meet annual awarding targets, NHAI resorted to awarding of projects even without having adequate right-of-way and proper clearances. Inordinate delays in acquiring land, utility shifting and obtaining environment and forest clearances led to a failure in projects' takeoff (awarded in FY12) within the stipulated timeline, resulting in cost overruns.

Economic slowdown: Contrary to the expectation of gradual growth post 2012, economic growth slowed down. Since traffic growth is correlated to economic growth, estimates factored at the time of bidding did not fructify, leading to cash burns for projects. In addition, non-availability of aggregates/soil, ban on mining in some states, public agitation, arbitration/contractual disputes among others have caused delays in construction of highways across the country. The government has taken number of steps to minimise such delays in future.

Stressed balance sheet: Given the assumption of a growing economy and supportive capital markets to raise funds, developers garnered multiple projects at one time. However, the economic slowdown, delay in clearance and cost overruns along with premium payments to NHAI made projects unviable. This combined with a high working capital, due to claims on cost overruns, stressed balance sheets of developers.

Liquidity constraints: With stressed projects on the rise, banks became cautious to lend to infrastructure segment in general and roads in particular. A disbursement required 80% of the land for a project in possession and high equity commitment from developers, such as 30-40% v/s the norm of 25-30%, to account for lower traffic, higher construction risk and stressed balance sheets. New projects awarding plummeted as financial closure of these projects became difficult.

Remedial measures and policy interventions embarked to kick start projects

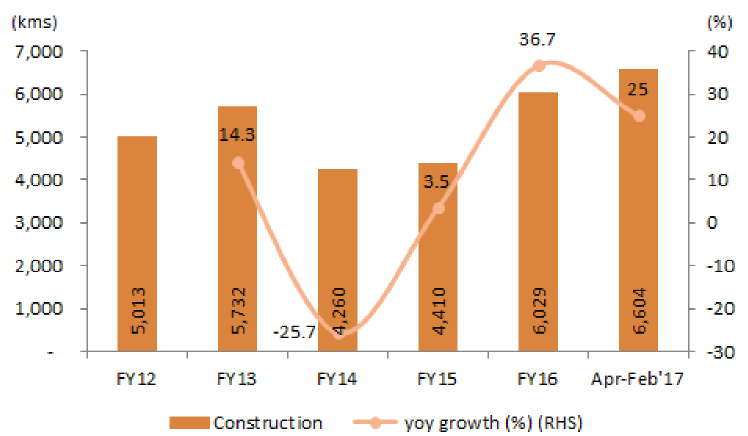
Taking cognizance of the above issues faced, the central government has taken several policy measures over FY14-16 to kick start construction of stranded projects as well as bring fresh investment for roads and highways sector. We believe premium deferment, awarding of projects through hybrid annuity model and release of 75% of arbitration payments have been effective announcements among those initiated.

Table 4: Initiatives to boost construction

Measures	Impact
1) Delinking environment and forest clearance for all linear projects. Delegation of power to regional officers to issue clearances and doing away with environmental clearance for length of 100km	Construction of the project could commence where there was no forest overlap
2) Delegation of power to a) NHAI's regional officers to hire equipments and labourers up to Rs10lakh per project, to demolish structures that fall within the right-of-way of a project and b) MoRTH's regional officers to ensure speedy utility shifting	Aided in making encumbrance-free land available more speedily to concessionaire/contractors
3) Extension of concession period in stranded BOT projects for delays, due to unavailability of land and clearances, which are not attributable to concessionaire	BOT toll: Extension of construction period without reducing the original tolling period and BOT annuity: Compensating annuities given for duration of the delay
4) One-time fund infusion by NHAI to revive and complete projects that have achieved 50% physical completion. NHAI would recover funds with first charge on toll receivables along with bank rate plus 2%	Likely to benefit three BOT (annuity) projects in West Bengal and Bihar, with a total infusion of Rs9bn. Another 12 BOT (toll) projects with fund requirement of Rs32bn could be revived with this measure. However, not seeing much traction, as lenders are not agreeable to NHAI's clause of first charge on receivables
5) Enhanced inter-ministerial co-ordination; Railways have prepared an online approval system for approval of ROB/RUB and standardised bridge design	In a year alone, more than 100 ROB/RUB designs have been approved by Railways, which earlier used to take five to six years
6) Harmonious substitution of concessionaire	NA
7) Fast track dispute resolution by forming a three-member committee to expedite claims by various developers	The committee has resolved 84 packages for a value of Rs175bn, settling these for an amount of Rs14bn till Mar'15

Source: Industry, Systematix Institutional Research

Chart 5: Construction bounces backs, 25% yoy growth in Apr-Feb'17



Source: MoRTH , NHAI

Table 5: Revival of stalled projects

Status	No of projects
Resolved	9
Terminated	3
Stalled	10

Source: Morth, NHAI

As seen from the chart no 5, measures undertaken gave a boost to construction in FY16, after a stagnant growth in FY14/15, and yielded results.

73 NH projects with an aggregate length of ~8,310km were languishing after award around two-and-half years back. These projects involved an estimated capital investment of ~Rs1,000bn that remained blocked. Due to MoRTH's interventions, that included taking up policy measures and rounds of one-to-one interaction with concessionaires and bankers, most of the languishing projects have been effectively

put on track. Of the 73 languishing projects mentioned above, issues remain to be resolved for only 10 projects.

Ease of financing: The government and RBI announced various initiatives to ease the financial stress arising from the slowdown in traffic and inability to access funds.

Premium deferment: While many developers offered a premium to win road projects in FY11 and FY12 to spruce up their order book, they were hit by lower-than-expected toll collection and huge finance cost, which resulted in a shortfall and inability to pay premium on operational projects. NHAI approved deferment of premium for the following 9 proposals with certain riders. The deferment shall be limited to the actual revenue shortfall after meeting the debt obligation and O&M expenditure. NHAI would be able to recover the deferred premium with interest in the latter period of concession.

Table 6: List of projects with deferment of premium payment since FY14

Stretch	Developer	Type	Project cost (Rs bn)
Godhra-GUJ/MP border	BSCPL	4 laning	8
Beawar-Pali-Pindwara	L&T	4 laning	26
Rohtak-Panipat	Sadbhav Infraprojects	4 laning	12
Hyderabad-Yadgiri	Sadbhav Infraprojects	4 laning	5
Samakhiyali-Gandihidham	L&T	6 laning	14
Ahmedabad –Vadodara	IRB Infra	6 laning	49
Tumkur-Chitradurga	IRB Infra	6 laning	11
Indore-Dewas	Gayatri- DLF	6 laning	8
Hosur-Krishangiri	Reliance Infra	6 laning	9
Belgaum- Dharwad	Ashoka Buildcon	6 laning	7
Dhankuni-Kharagpur	Ashoka Buildcon	6 laning	22

Source: NHAI

Classification of debt as secured: RBI has allowed classifying loans to toll road projects as “secured” to the extent assured by the authority. This would entail lower provisioning by banks and reduction in cost of debt to developers.

Addressing asset-liability mismatch: A long-term debt funding to match the concession period through the refinancing provision (5/25 structure) has been allowed, without classifying the exposure as "restructured".

Refinancing norms eased: RBI allowed banks to fix a fresh loan amortisation schedule for existing loans once during the lifetime of a project, after CoD, based on the reassessment of project cash flows, without treating the project loan as “restructured”.

Initiatives to boost awarding

- **Increase threshold for new project approval:** The cabinet has empowered MoRTH to decide the mode of awarding a project. In addition, MoRTH is also authorised to appraise projects up to Rs10bn under EPC and PPP mode, compared to Rs5bn earlier. This would lead to shorter turnaround time to award projects.
- **Segregation of civil and construction cost:** For speedy appraisal and award of projects, CCEA has approved segregation of civil construction cost from the cost for land acquisition, centages and pre-construction activities. Hence, a project with a construction cost up to Rs10bn can be appraised and approved by SFC headed by MoRTH, compared to CCEA approval earlier.
- **100% exit policy for developers to unlock capital for new projects:** CCEA has eased the exit policy for developers by allowing them to divest 100% equity after two years of completion of construction (CoD) for all BOT projects, irrespective of the year of award. This is a relaxation compared to the earlier policy where developers had to own at least 26% stake in projects awarded before 2009. The latest policy has allowed financial investors to fund completed projects, while developers can deploy the capital to complete languishing projects, bid for new highway projects or repay debt.

Table 7: Key stake sale transactions from January 2015

Acquiring company	Company/Project	Type	Offloading company	Stake	Deal value (Rs bn)
IDFC Alternatives	Reengus-Sikar Expressway,Rajasthan Shillong Bypass, Meghalaya	Projects	GR Infraprojects	100%	-
Cube highways and Infrastructure	Andhra Pradesh Expressway	Project	ILFS Transportation Network	100%	6.4
Abertis Infra	Farukhnagar-Jadcherla highway, Andhra Pradesh and Trichy Tollways project, Tamil Nadu	Projects	Macquarie Group	100%	10.0
Cube highways and Infrastructure	Western UP Tollway	Project	NCC Infra and Gayatri Projects	100%	5.75
IDFC Alternative IIF-2	Dewas- Bhopal Corridor	Project	Welspun Enterprises	37%	6.62
Cube Highway and Infrastructure	Madhucon Agra Jaipur Expressway (Mahua-Bharatpur toll asset)	Project	Madhucon Infra	100%	2.48
Brookfields Asset Management and Core Infrastructure	Gammon Infra 6 projects	Project	Gammon Infraprojects	-	-
Cube Highway and Infrastructure	Jaipur Mahua Tollway	Project	IJM Malaysia	Majority stake	-
IDFC Alternatives	Nirmal BOT	Project	HCC	100%	0.7
Canada Pension Plan Investment	L&T IDPL	Holdco	L&T	NA	21.2

Source: Industry

- **Step-up of government spending, EPC awards increase:** To address the issue of appetite loss from the private sector in bids for road BOT projects for various reasons cited above, NHAI stepped up awarding road projects on EPC basis. Chart no 4 shows awards on EPC basis made a comeback in FY14, after nil awarding in the previous two years. Since then, momentum has been maintained and NHAI awarded 3,017km on EPC basis in FY16. While the awarding target for FY17 has been set at 10,000km, it is expected that ~45-50% will be awarded on EPC basis. MoRTH targets to construct 15,000km of highways and NHAI's share would comprise of 8,000km.

- **Hybrid annuity model - a win-win for government and developers:** Given the inherent limitation of government finances to implement EPC projects, MoRTH adopted the hybrid annuity model (HAM) to encourage private sector participation through adequate incentives. As per the model, 40% of the project cost is provided by the government as 'construction support' to the private developer in five equal installments during the construction period and the balance 60% as annuity payments over the concession period along with interest on outstanding amount to the concessionaire. Concessionaire remains responsible for operation and maintenance (O&M) till the end of concession period and there is separate provision for O&M payments by the government to the concessionaire. Project costs are inflation indexed (through a price index multiple) and the toll is collected by the authority. With only 40% contribution for the project cost, the government can award more projects using the same budgetary resources.

Table 8: HAM mechanism

Bid parameter	Life cycle cost (NPV of the quoted bid project cost + NPV of O&M cost for the entire O&M period)
Returns for concessionaire	Amount financed by concessionaire to be recovered from the authority through bi-annual annuity payments along with interest payments (at bank rate +3%) on the reducing balance
O&M payments	Concessionaire responsible for O&M till end of concession period. O&M payments will be made bi-annually
Tenure	15 years
Toll collection	Responsibility of authority
Others	Project payments to be inflation linked

Source: MoRTH

Table 9: Comparison of different modes

	EPC	BOT Toll	BOT Annuity	HAM
Capital cost funding	100% authority	100% private developer	100% private developer	40% authority and 60% private developer
Construction risk	Private developer	Private developer	Private developer	Private developer
Revenue/toll collection risk	Authority	Private developer	Authority	Authority
O&M done by	Authority	Private developer	Private developer	Private developer
Awarding criteria	Lowest project cost	Highest premium quoted	Lowest annuity quoted	Lowest NPV
Financial closure	NA	To be achieved within 180 days of signing the concession agreement		To be achieved within 150 days of signing the concession agreement
Mobilisation advances	Interest bearing advances available	No mobilisation advance granted from authority during concession period. However, SPV can pay advances to the EPC arm during construction		Mobilisation advances can be availed from the authority up to 10% of bid project cost at bank rate compounded annually during construction period
Release of construction grant	NA	Construction grant, if any, can be disbursed in the proportionate form of term loan disbursement after infusion of 100% contribution from sponsors		To be released in five equal instalments, subject to the achievement of physical progress of 20%, 40%, 60%, 75% and 90% respectively
Delay in handover of ROW post appointed date (i.e. handover of 80% of land)	NA	Concessionaire is required to complete the work on all land for which RoW is granted at appointed date and can achieve PCoD after completion of such work. Final CoD will not be issued even though work is delayed due to reasons attributed by authority		If the remaining site is not provided within 180 days from the appointed date, it shall be removed from scope of work. Final CoD can be achieved after completing 100% work on the site available

Source: Systematix Institutional Research

What is in for developers?

- Capital commitment is reduced as the authority will fund 40% of the appraised cost, while the concessionaire will be required to fund 60% of the project cost (equity commitment of 12-16%).
- Participation in construction of road projects and insulation from traffic/toll collection risk.
- Annuities will also protect the developer from risks such as sudden withdrawal of collection rights by authorities, as seen in Maharashtra. Thus, the model has the potential to revive the road sector as the risk element of pricing based on traffic movement on roads will be taken over by the government.
- PCoD can be attained with the work done on available ROW and the unavailable part will be treated as change of scope.

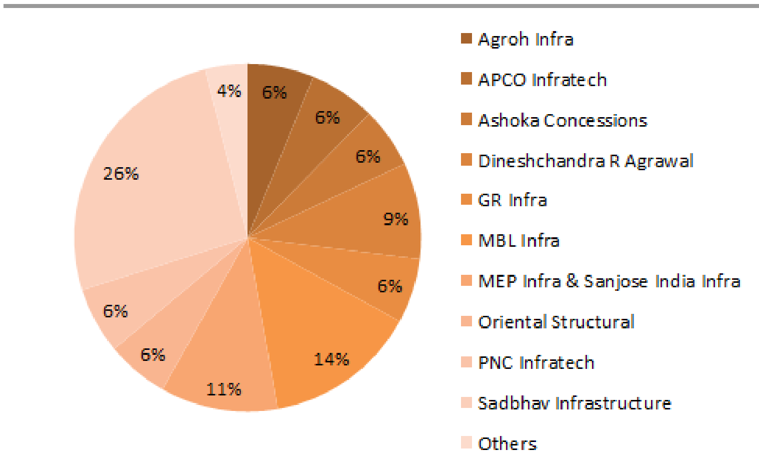
What is in for Authority/Government?

- Reduces upfront (over 2.5 years) capital commitment to 40%, when compared to 100% in a pure EPC project.
- Execution pace is also expected to improve due to stringent clauses for damages and encashment of performance as well as additional performance security in the event of delays by a concessionaire, compared to the conventional DBFOT model.

After a lukewarm response from just three to four bidders for each project during January-March 2016, NHAI made several amendments to the draft concession agreement, including a revised annuity payment schedule, which envisages payment of ~24.2% of the completion cost in the first five years versus 7.7% earlier. Thereafter, the number of bidders that placed bids from May 2016 for each project increased to 9-12, indicating heightened competitive intensity from regional players to increase their EPC order book.

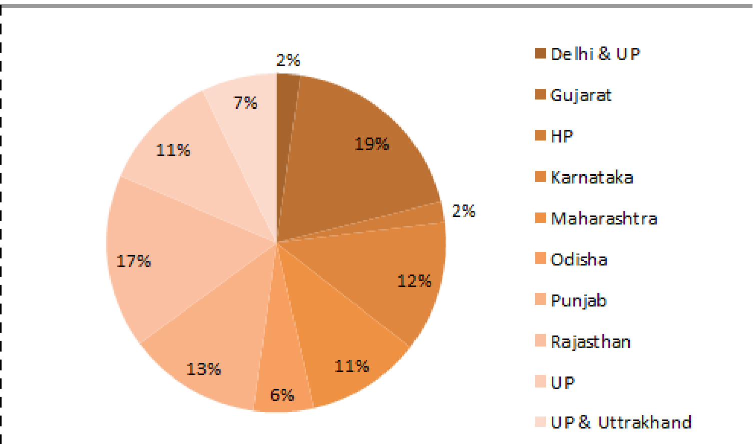
With only eleven projects achieving financial closure so far, it is evident that contractors with a healthy execution track record and strong balance sheet have managed to get loans, while others find it difficult. Thus competitive intensity has now come down with 4-5 serious players bidding for contracts.

Chart 6: Double-digit market share for Sadbhav, MBL and MEP Infra



Source: NHAI, Systematix Institutional Research

Chart 7: State wise awards of HAM projects



Source: NHAI, Systematix Institutional Research

Table 10: NHAI update - only 10 of 26 HAM projects awarded so far have achieved financial closure

	Concessionaire	FC done	Months since award	Stretch	Award date	Km	BPC (Rs mn)	State
1	APCO Infratech	No	13	Meerut – Bulandshahar	Jan-16	61	6,832	UP
2	APCO Infratech	No	13	Delhi - Meerut Expressway (PKG-2)	Jan-16	22	10,816	Delhi & UP
3	Welspun Enterprises	Yes	13	Delhi - Meerut Expressway (PKG-1)	Jan-16	9	7,014	Delhi & UP
4	MBL Infra	No	11	4 laning of Chultmalpur - Ganeshpur and Roorkee - Chutmalpur- Gagalheri	Mar-16	53	14,430	UP/Uttarakhand
5	MBL Infra	No	11	4 laning of Gagalgeri - Saharanpur – Yamunanagar	Mar-16	51	16,680	UP
6	MEP Infra & Sanjose India Infra	Yes	11	4 laning Ring Road / bypasses for Nagpur City (PKG-I)	Mar-16	34	5,460	Maharashtra
7	MEP Infra & Sanjose India Infra	Yes	11	4 laning Ring Road / bypasses for Nagpur City (PKG-II)	Mar-16	28	5,917	Maharashtra
8	Sadbhav Infrastructure	Yes	11	4 laning of Rampur - Kathgodam (I)	Mar-16	43	8,990	UP
9	Sadbhav Infrastructure	Yes	11	4 laning of Rampur - Kathgodam (II)	Mar-16	45	7,200	UP/Uttarakhand
10	Agroh Infra	Yes	10	4 laning of Kagavadar – Una	May-16	41	7,236	Gujarat
11	Eagle Infra	No	10	4 Lane Laddowal bypass	May-16	17	3,920	Punjab
12	MEP Infra & Sanjose India Infra	No	10	4 laning of Talaja – Mahuva	May-16	45	8,346	Gujarat
13	Sadbhav Infrastructure	Yes	10	4 laning of Bhavnagar – Talaja	May-16	48	9,982	Gujarat
14	Sadbhav Infrastructure	Yes	10	4 laning of Una – Kodinar	May-16	41	7,631	Gujarat
15	Dineshchandra R Agrawal	No	9	Salasar - Nagaur section of NH-65	Jun-16	120	6,372	Rajasthan
16	MEP Infra & Sanjose India Infra	No	9	4 laning of Mahuva to Kagavadar (III)	Jun-16	40	7,632	Gujarat
17	Agroh Infra	No	8	4 laning of Kodinar to Veraval section of NH-8E	Jul-16	42	8,300	Gujarat
18	PNC Infratech	Yes	8	4 laning / Two Laning with PS of Dausa - Lalsot - Kauthun section of NH-11A	Jul-16	83	6,887	Rajasthan
19	Ashoka Concessions	Yes	7	4/ 6 Laning of Kharar to Ludhiana section NH-95	Aug-16	76	13,883	Punjab
20	Chetak Enterprises	No	7	2 laning Shimla Bypass	Aug-16	27	15,832	HP
21	GR Infra	No	7	4 Laning from Phagwara to Rupnagar	Aug-16	81	11,696	Punjab
22	Sadbhav Infrastructure	No	6	2/4 laning of BRT Tiger Reserve Boundary to Bangalore section of NH-209	Sep-16	171	9,507	Karnataka
23	Oriental Structural	No	5	4 Laning of Binjhabahal – Telebani	Oct-16	78	10,090	Odisha
24	MBL Infra-Agroh Infra	No	4	4 laning of Tarsod - Fagne (package -IIB)	Nov-16	87	10,649	Maharashtra
25	Viswaraj Environmental	No	4	4 laning of Chikali- Tarsod	Nov-16	63	10,716	Maharashtra
26	Kalthia Engineering & Construction	No	3	2 Laning with PS of Gadu - Porbander	Dec-16	92	4172	Gujarat
	Termination							
	Gawar Infra	-		Samrala Chowk- Ludhiana	Apr-16		10,490	Punjab
	Overseas Infra	-		Kishangarh-Udaipur-Ahmedabad (Package VI)	Jun-16		-	Gujarat
	MBL Infra			6 laning of greenfield proposed Udaipur Bypass	Jun-16	24	7,260	Rajasthan

Source: NHAI, Systematix Institutional Research

Inability of a developer to invest equity or bring debt may lead to termination of additional projects compared to the above three projects.

Lenders' view

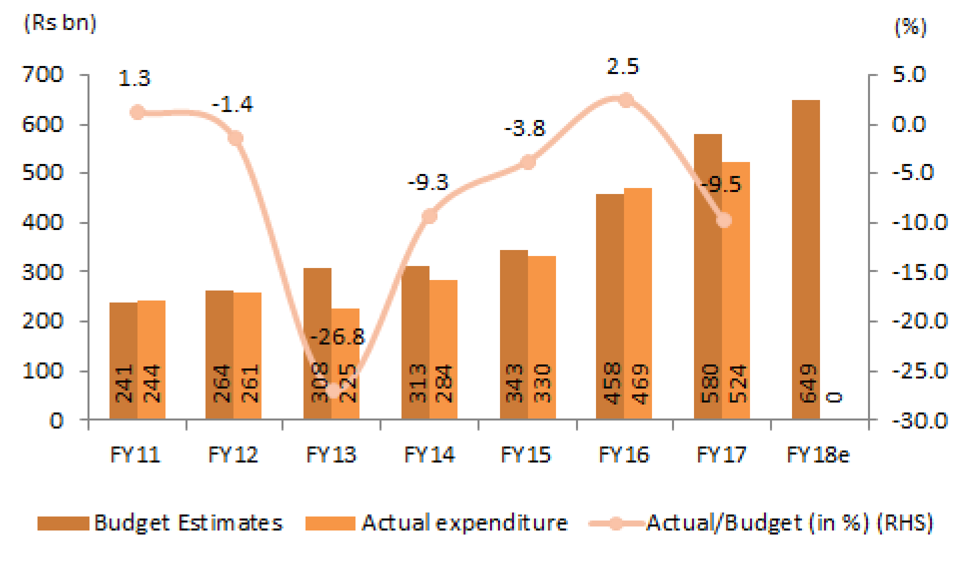
- Interest payable by NHAI on loans taken by developer is too low at bank rate +3%. Bankers suggest the SBI base rate +3%.
- Current rules stipulate lower compensation to lenders in the event of inability of a concessionaire to complete a project. Banks have suggested the termination charge should be 100% of the debt due.
- NHAI takes a timeline of 240 days to fulfill precedent conditions (land acquisition, right of way among others), while developers get just 150 days to achieve financial closure.

Our channel checks suggest that MoRTH may review the 150-day timeline for financial closure, given that it is a new model for lenders to comprehend.

Reforms backed by financing galore

High budgetary allocation: The central government stepped up allocation for roads and highways sector in its annual budget, to finance the shift in awarding towards EPC mode, due to poor participation from private parties under BOT mode. *While the allocation jumped 2.1x in FY16 to Rs550bn v/s Rs260bn in FY14, NHAI awards on EPC basis grew 2.4x to 3,017km in the same period.* The estimated total investment required by NHAI to execute different highway projects is Rs719bn (BE 2016-17).

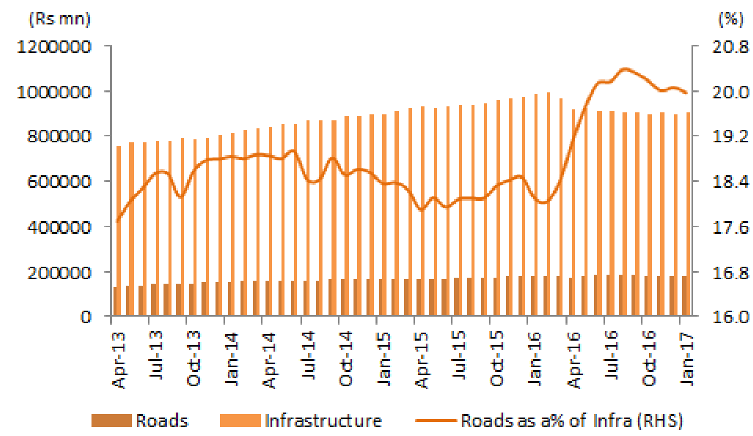
Chart 8: Stepping up budgetary resources



Source: GOI Budget

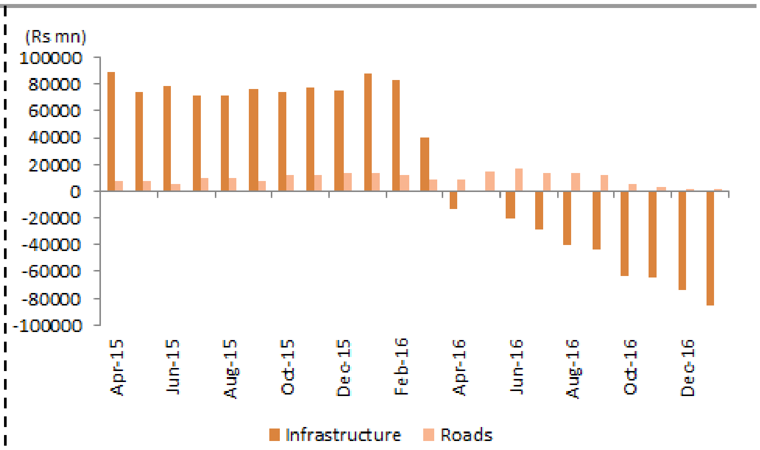
- While MoRTH has proposed Rs909bn budget estimate (BE) for 2017-18, the finance ministry allocated an outlay of only Rs649bn for roads sector in the budget.
- **NHAI bonds:** The government, in budget 2016-17, has allowed NHAI to raise funds up to Rs150bn via NHAI bonds.
- NHAI in FY17 raised Rs100bn through taxable bonds of EPFO for 25 years at 8.03% interest. It also raised an additional Rs119bn from investors availing capital gains exemption (as of Oct 31, 2016).
- **LIC** subscribed to 1st tranche of Rs85bn from NHAI for 30 years at an interest rate of 7.22%. In principle agreed to subscribe bonds worth Rs250bn.
- **Infrastructure debt fund:** Formulated in FY14, the infrastructure debt fund (IDF) is a step to ease banks' burden. During 2014-15, 20 projects received IDF funding of Rs18.8bn.

Chart 9: Roads attract ~20% of infrastructure bank credit



Source: RBI, Systematix Institutional Research

Chart 10: Incremental bank lending positive, albeit quantum lowers



Source: RBI, Systematix Institutional Research

Many construction/infra companies have raised funds via QIP/rights since FY14 to meet capex/working capital requirement and/or retire debt. A deleveraged balance sheet has aided in bidding for fresh contracts and has augmented their order book.

Table 11: QIP money raised by infra/construction companies since FY14

Date	Company	Amount (Rs mn)	Mode
Apr-14	ITNL	5,245	Rights
Jul-14	GMR Infra	14,768	QIP
Jul-14	J Kumar Infra	1,372	QIP
Aug-14	ITD Cementation	1,440	QIP
Sep-14	Gammon Infra	2,589	QIP
Sep-14	NCC	5,987	Rights
Oct-14	Sadbhav Engineering	2,500	QIP
Dec-14	MBL Infra	1,174	QIP
Jan-15	Supreme Infra India	1,000	QIP
Mar-15	IRB Infra	4,400	QIP
Mar-15	GMR Infra	14,018	Rights
Apr-15	HCC	4,000	QIP
Apr-15	Ashoka Buildcon	5,000	QIP
Apr-15	MEP Infra	3,240	IPO
May-15	PNC Infratech	4,884	IPO
Aug-15	Sadbhav Infraprojects	4,917	IPO
Oct-15	J Kumar Infra	4,093	QIP
Oct-15	ITNL	7,402	Rights
Jan-16	JMC Projects	1,500	Rights
	Total	**89,529**	

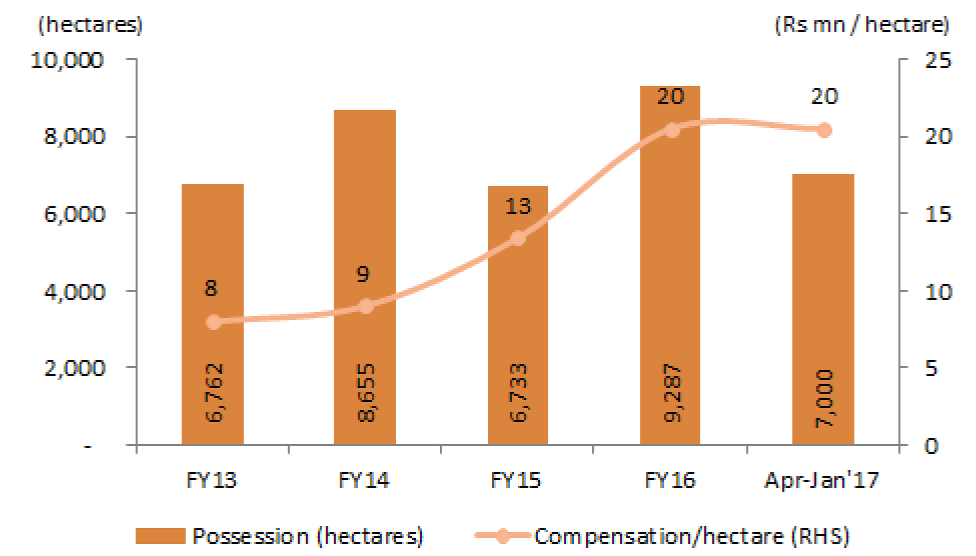
Source: Company, BSE

Land acquisition stepped up in FY16; compensation surpasses construction cost

For FY16, 9,287 hectares of land was acquired v/s 6,733 hectares in FY15, while the compensation paid has risen to Rs20/hectare in FY16, compared to Rs9/hectare in FY14. Reforms such as awarding projects only after 90% of the land is available and payment of compensation under a new land act have made it difficult to obtain the possession of land. Interactions with officials indicate that farmers/villagers are negotiating for a higher compensation, 4x new circle rates in rural areas and 2x new circle rates in urban areas, thereby making the process time consuming and delaying the actual possession of land.

Recently the Road Minister has indicated that many projects which have been sanctioned by the Ministry are currently facing land acquisition problems. It was also decided by the Ministry that appointed date would not be offered without 80% land acquisition. However owing to issues in land acquisition, road Ministry has now relaxed the criteria and decided that the appointed date can be granted after 50% of the land is acquired and the process for other land acquisition is in the process.

Chart 11: High compensation of Rs20mn/hectare paid since FY16



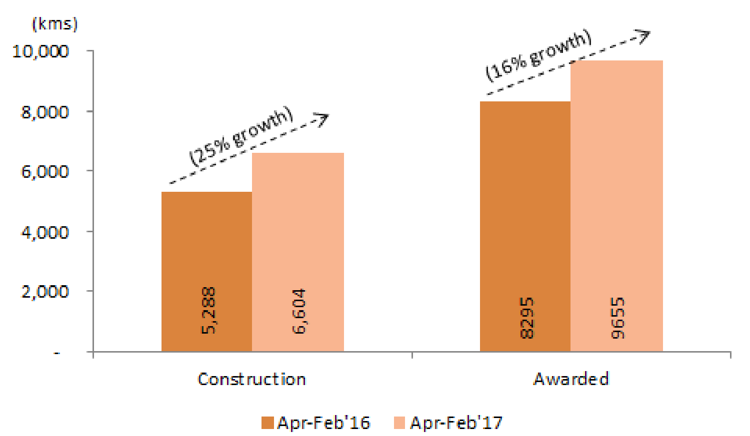
Source: MoRTH, NHAI

YTDFY17 awards and construction indicate stiff FY17 targets

Awarding of road projects has been at 9,655km during Apr-Feb'17, up 16% yoy. While growth has picked up in Feb'17, it is much lower than the target of 25,000km set at start of the year due to (a) delay in getting approval from Cabinet for payment of high compensation under new land acquisition act (b) Strict enforcement by the new Chairman for minimum 80% land rule for all projects (c) shortage of consultants to prepare DPRs and lastly inertia among bureaucrats to take strong decisions. We expect the awarding to surpass 10,098km achieved in FY16.

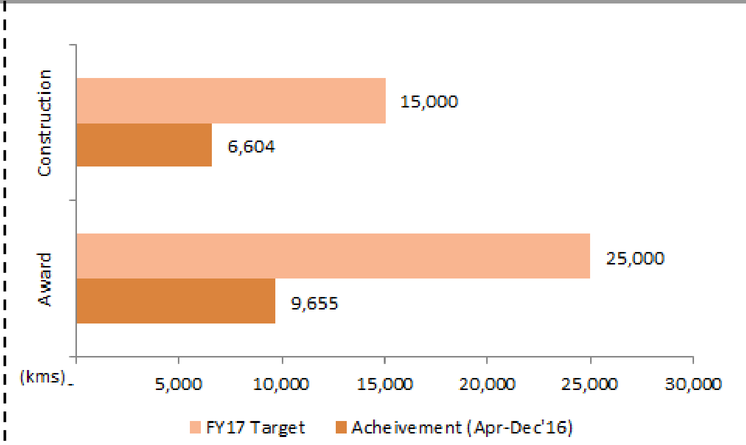
On the construction side, 6,604km were completed during Apr-Feb'17, up 25% yoy lower than target of 15,000km set at beginning of the year. The road ministry attributes the slowdown to issues on land acquisition, utility shifting, non-availability of Soil/Aggregates, poor performance of contractors, environment/ forest/wildlife clearance, ROB & RUB issue with railways, public agitation for additional facilities, arbitration/contractual disputes with contractors etc. MoRTH plans to ramp up road construction to 30km/day by March'17 from the 20km/day during Apr-Feb'17.

Chart 12: Construction picks pace, but awarding moderates



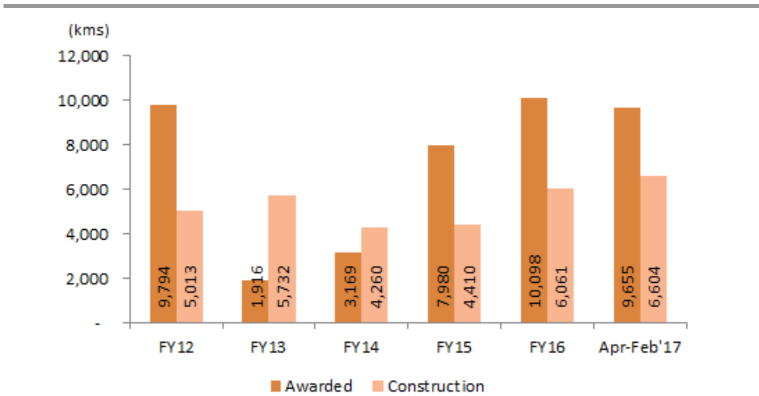
Source: MORTH & NHAI

Chart 13: Awarding at 39% & construction at 44% of target



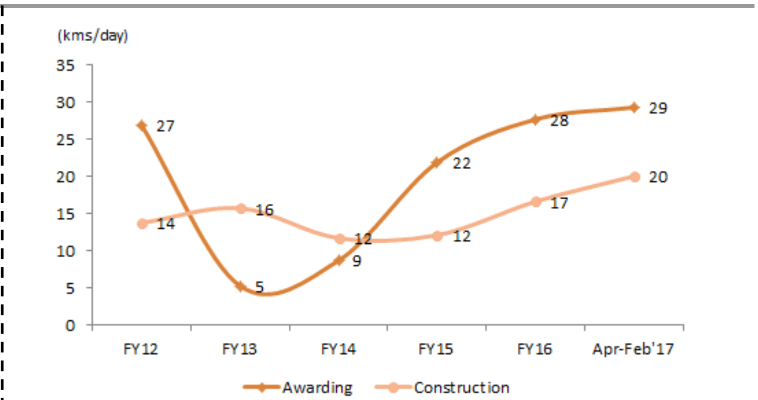
Source: MORTH & NHAI

Chart 14: Overall increase in awarding and construction



Source: MORTH & NHAI

Chart 15: Construction km/day increases to 20 in Apr-Feb'17



Source: MORTH & NHAI

Table 12: NHAI awards – mode-wise breakup

Type/ Mode	Apr-Jan'17				FY16				FY15			
	Km	% of total	Value (Rs bn)	No of projects	Km	% of total	Value (Rs bn)	No of projects	Km	% of total	Value (Rs bn)	No of projects
EPC	1,315	45%	220	28	3,038	70%	468	63	2,685	73%	148	35
HAM	1,177	40%	160	18	345	8%	83	9	-		-	-
BOT	422	14%	46	3	985	23%	132	7	1,051	27%	94	8
Total	**2,914**	**100%**	**426**	**36**	**4,368**	**100%**	**684**	**79**	**3,736**	**100%**	**242**	**43**

Source: NHAI

Competitive intensity heightens for EPC road projects

With favourable policy reforms and an increase in government spending, awarding picked from FY15 (as shown in chart no. 14), with 70-73% of bids being awarded on EPC mode. An analysis of NHAI awarding data in FY15 and FY16 indicates that the number of bidders increased significantly at 3-14 players for each bid. Large incumbent players such as GMR, IL&FS, HCC and NCC among others took a back seat due to debt-laden balance sheet, while established regional players with strong execution capabilities emerged to bid for EPC contracts. However, with a large number of players chasing bids to increase their order book, bids were aggressively low like ~20% below NHAI cost. L&T shifted its focus to EPC and emerged with the highest market share of 16-19% over FY15-16, while bidding aggressive in some cases. Regional players such as GR Infraprojects (Udaipur-based) and Dilip Buildcon (Bhopal-based) garnered a market share of 8-20% (as show in table no 13). Companies with unexecuted captive BOT order book such as Sadbhav Engineering (4-5% share), PNC Infratech (10% share) and Ashoka Buildcon (1% share) refrained from bidding aggressively. Their balance sheet strength and low working capital also gave the financial prowess to bid for larger new contracts.

Acceptance of HAM model led to a shift in awarding from EPC (45% in Apr-Feb'17 v/s 70% in FY16) during April-October 2016. Players such as L&T, Dilip Buildcon, Gayatri Projects and HG Infra continued to show more appetite for EPC projects. Within our coverage, while PNC Infratech won projects under HAM compared to EPC, Ashoka Buildcon won projects both under HAM and EPC.

Table 13: Emergence of new players in EPC segment

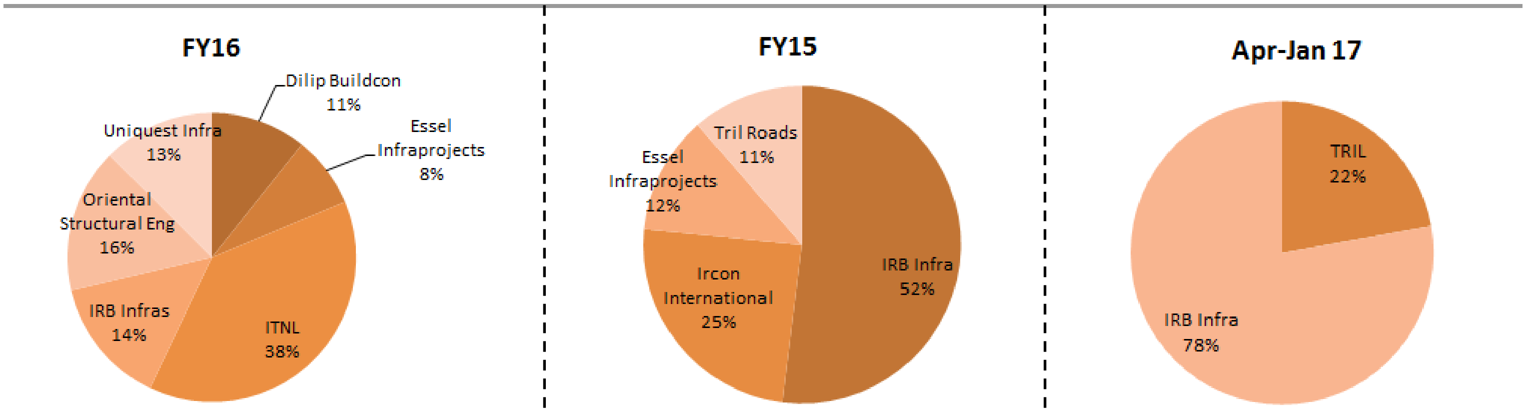
Companies	FY16		FY15		Apr-Jan'17	
	Km awarded	*%*	*Km awarded*	*%*	*Km awarded*	*%*
L&T	480	16	508	19	127	10
PNC Infratech	317	10	0	0	-	-
Gayatri Projects	279	9	55	2	153	12
GR Infra Projects	325	11	529	20	-	-
Punj Lloyd	201	7	0	0	-	
Dilip Buildcon	376	12	215	8	194	15
Jaiprakash Associates	156	5	0	0	-	-
KNR Construction	142	5	0	0	-	-
Sadbhav Engineering	133	4	130	5	-	-
PNC – SPSCPL	92	3	0	0	-	-
Ashoka Buildcon	43	1	0	0	57	4
H G Infra Engineering	75	2	52	2	129	10
Corsan Corviam Construction SA	72	2	293	11	-	-
Isolux Corsan India	45	1	0	0	-	-
BSCPL Infrastructure	45	1	0	0	143	11
Gawar Construction	37	1	7	0	22	2
J Kumar Infraprojects & J.M. Mhatre Infra	40	1	0	0	-	-
HCC	32	1	36	1	-	-
Gammon India	40	1	43	2	95	7
Others	110	4	486	18	379	29
Total	**3038**	**100**	**2,685**	**100**	**1,299**	**100**

Source: NHAI, Systematix Institutional Research

Selective bidders in BOT space

During FY15-16, the share of bids on BOT basis came down to 23-27% of total bids. While majority of the companies that won projects on BOT basis in the previous cycle (FY09-12) had limited balance sheet strength to bid for new projects on one side, companies with healthy financial appetite were grappling with lower traffic and high debt servicing cost on the other. Thus, the number of bidders for fresh bids came down drastically to four to five and many strategically chose to participate selectively and conservatively in new highway bids.

Chart 16: Competitive intensity lessens with old players grappling with tight balance sheet



Source: NHAI

Improved environment to benefit select serious players

Healthy NHAI bid pipeline – traction continues for Greenfield projects

Table 14: Phase-wise implementation of NHDP and status…

31st Jan 2017	Total Length (Km.)	Already 4/6Laned (Km.)	Under Implementation (Km.)	Contracts Under Implementation (No.)	Balance length for award (Km.)
GQ	5,846	5,846	0	0	-
NS – EW (Ph. I & II)	7,142	6,427	458	39	257
Port (Connectivity)	435	379	56	6	-
NHDP Phase III	11,809	6,835	3,227	81	1,747
NHDP Phase IV	13,203	2,054	4,654	64	6,495
NHDP Phase V	6,500	2,359	761	22	3,380
NHDP Phase VI	1,000	-	165	8	835
NHDP Phase VII	700	22	19	1	659
NHDP Total	46,635	23,922	9,340	221	13,373
Others (Ph.-I, Ph.-II & Misc.)	1,844	1,614	230	11	-
SARDP -NE	110	105	5	1	-
Total by NHAI	48,589	25,641	9,575	233	13,373
% of total		**53%**	**20%**		**28%**

Source: NHAI

Over 13,373km of projects are yet to be awarded under the National Highway Development Programme (NHDP). The government, in budget 2016, has indicated to convert 50,000km of state highways into national highways. These projects are expected to be awarded over the next two years. Currently, only 24% of the projects are above four/six and eight-lane. The increase in traffic, as estimated by National Transport Development Policy Committee (NTDPC), would necessitate the expansion of one and two-lane projects to four-lane and above. This indicates that ample opportunities are likely to come up in the sector over the longer run.

Table 15: Strong traffic growth estimation

	Traffic	
	Freight (bn tons/km)	Passenger (bn persons/km)
2011-12	1,385	9,329
2016-17	1,987	14,272
2021-22	2,949	35,043
2026-27	4,321	74,079
2031-32	6,559	1,63,109
CAGR FY12-32	8%	15%

Source: NTDPC

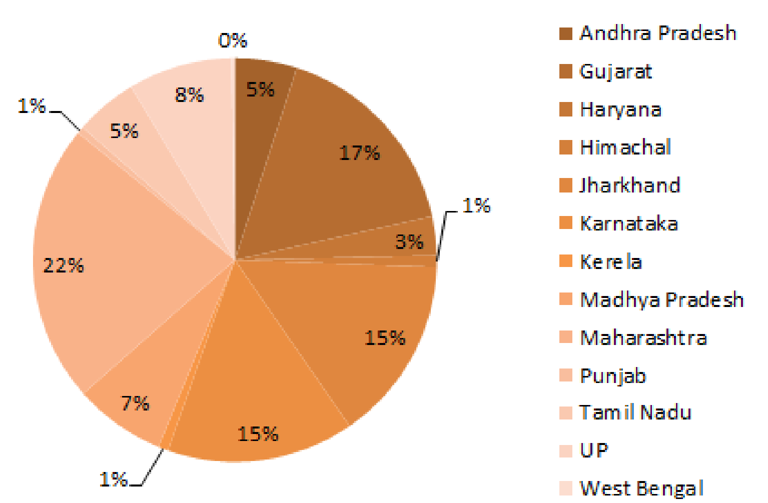
Table 16: NHAI Mar-May'17 bid pipeline: Projects of 1,420km amounting to Rs349bn

State	HAM		EPC		Toll		Total	
	Rs mn	km	Rs mn	km	Rs mn	km	Rs mn	km
Andhra Pradesh	28,232	116	4,652	110	-	-	32,883	226
Bihar	7,854	8	-	-	-	-	7,854	8
Gujarat	-	-	2,203	123	75,230	124	77,433	248
Haryana	-	-	-	-	-	-	-	-
Himachal Pradesh	24,859	21	-	-	-	-	24,859	21
Jammu & Kashmir			14,718	-	-	-	-	-
Karnataka	44,951	117	-	-	-	-	44,951	117
Kerala	12,886	29	-	-	-	-	12,886	29
Madhya Pradesh			8,884	108	-	-	8,884	108
Maharashtra	24,463	154	392	7	12,438	24	37,292	185
Myanmar			11,770	75	-	-	11,770	75
Punjab	-	-	7,923	12	-	-	7,923	12
Rajasthan	6,261	24	-	-	-	-	6,261	24
Tamil Nadu	19,335	98	4,049	80	-	-	23,384	178
UP	14,302	145	18,226	39	-	-	32,528	184
West Bengal	-	-	5,166	6	-	-	5,166	6
Total	**1,83,141**	**712**	**77,981**	**559**	**87,668**	**148**	**3,48,790**	**1,420**
as a %of total	**53%**	**50%**	**22%**	**39%**	**25%**	**10%**	**100%**	**100%**

Source: NHAI

NHAI has listed 27 road projects worth Rs349bn totaling to 1,420km that are expected to be awarded in March- May 2017. The focus continues to be on PPP basis. Within PPP, HAM continues to be the preferred mode (50% of listed projects in kms), followed by BOT toll mode (10% of the listed projects in kms). The share of government-funded EPC projects is lower at 39% in terms of kms. Value-wise, HAM projects comprise of 53%, followed by 25% for BOT and 22% for EPC projects. Based on the near-term PPP opportunity, we expect an equity investment requirement of Rs31-37bn.

Chart 17: NHAI bid pipeline – state wise



Source: Company, Systematix Institutional Research

Measure to revive liquidity in construction sector

a) Arbitration award payout

CCEA, in August 2016, issued a directive for payout of 75% of claims that were decided in favour of construction companies by the related government bodies. Construction companies can avail this sum against margin-free bank guarantee and use the amount to reduce their debt or invest in construction projects.

NHAI's website outlines following procedures for release of payout:

- Contractors/concessionaires would inform NHAI of the payout claim along with supporting documents. NHAI would verify and validate within five days and inform contractors/concessionaires about the bank guarantee to be furnished.
- In the second stage, the contractor/concessionaire would give acceptance of the payout + interest; furnish a one-year bank guarantee and arbitral award escrow account agreement.
- NHAI would verify the bank guarantee and disburse the amount within the next five days.

Based on the submission received by NHAI, IRB Infrastructure has received Rs2.7bn in December 2016. Following are the companies that have submitted documents and are expected to receive:

Table 17: 75% of the arbitration award payout

Company	Rs mn
HCC	9,777
ILFS Eng & Const	1,540
AFCONS Infrastructure	1,408
Oriental Structure Engineers - KMC (JV)	853
OSE Oriental Gammon (JV)	918
Gayatri - ECI (JV)	84
Others	2,692
Total	**17,272**

Source: NHAI

Within our coverage, Sadbhav Engineering and Ashoka Buildcon have submitted claims worth Rs7.5bn and Rs2bn respectively to NHAI, which are at various stages of arbitration.

As per recent statistics, a total of 123 cases for a claim amount of more than Rs250bn are pending before Arbitral Tribunals relating to highways sector.

b) Compensation for demonetization led toll revenue loss

- NHAI plans to compensate private BOT toll owners on loss of toll revenue due to demonetization; based on average daily collection in Oct'16, it is expected to reimburse Rs9.2bn and has moved Cabinet note in this regard.
- The card swiping machines (POS machines) have been installed at all lanes in toll plazas and 8-20% of the toll collection happens through the digital mode.
- Within our coverage universe, ASBL, SADE and PNCL faced temporary execution slowdown
    - EPC contracts led by shortage of material and labourers. However, companies proactively helped labourers to open bank accounts and arrange for payments in their accounts. The situation has improved by Dec'17 and construction revenue bounced back in 3QFY17.
    - Traffic declined between 2-5% on operational BOT assets in December'16 compared to October'16. Nevertheless, the management commentary post 3QFY17 results indicate average -7% yoy improvement in traffic growth since January'17.
- As per industry sources, there has been delay in reimbursement of cost from government sources and only partial reimbursement has happened. However, companies expect NHAI to replace the entire loss of toll revenue and not just the cost alone.
- Toll-based projects typically have monthly interest payment obligations and debt repayments on a monthly or quarterly basis. The delay is negative because the companies are servicing debt without revenue plus there is interest loss on delay in reimbursement.
- Long-term positives from demonetisation: While in the short term, headwinds will be faced by EPC companies and asset owners, the large amount of deposits with the banking system would enhance their capacity to lend. It is expected that interest rates would come down over the next few quarters, thus reducing the overall cost of capital in the longer term.

Consolidation of operational BOT projects – financial investors to benefit

Roads sector is relatively more mature in the infrastructure space, with over a decade's history of operational BOT projects. Our interactions with experts indicate that roads sector in the country offers standardised policies and procedures to attract global investors.

The current environment of lower interest rate and growing traffic is highly conducive for consolidation in BOT space. Further, the easing of exit policy by allowing assets owners to divest 100% stake two years after commencement of operations, compared to the earlier policy of retaining 26% stake till the end of concession period, will make it lucrative for investors to own controlling stakes in assets. The key stake sale transactions since January 2015 are listed in table No. 7

What owners/sellers get

The owners of road BOT assets in India range from pure play developers to EPC companies who diversified into asset development/ownership due to paucity of orders in other segments.

Table 18: Objective behind stake divestment in road assets

	Reasons entered for	What went wrong	Objective to exit
EPC companies	Non-core road BOT assets were won for EPC operations due to paucity in others EPC segments such as buildings, irrigation, industrial	• Economic downturn -lower traffic & high interest rates • High equity commitment • Inflated working capital cycle for core business • Forced into CDR	• Focus on asset divestment • Strengthening balance sheet by ploughing back capital into core EPC business
BOT developers	To ride on economic growth through asset ownership	• Investment in projects in sectors apart from roads (airports, power plants, MRTS) • Deteriorating macroeconomic environment impacted cash flow generation	• Deleverage balance sheet • Need to free up equity to invest in new projects

Source: Industry, Systematix Institutional Research

What is in for buyers

The appetite of buyers has improved for mature operational road assets as:

- It eliminates the construction risk
- Considerable traffic history provides a cushion against lower initial traffic
- Acquiring a controlling stake in operational projects combined with the strong parentage of acquirer has enabled a reset of interest at lower rate – 9% for annuity and 9-10% for toll projects

Table 19: Buyers Rationale

Buyers	Rationale	Players
Investors: Domestic PE funds, Venture capital firms Foreign pension funds, Sovereign funds, international infra funds	1) Invest in long duration projects with stable cash flows 2) Allows PE funds to deploy capital in infrastructure assets to provide returns to their investors 3) Allows pension/sovereign funds to buy revenue yielding assets 4) Refinancing debt at lower rate from infra debt funds that lend for longer duration.	IDFC Alternative, BIF Holdings, Brookfield AMC, Canada Pension Fund , Cube Highways and Infrastructure, Temasek Holdings, Abu Dhabi Investment Authority
BOT developers with strong balance sheet	1) Quick way to grow portfolio inorganically 2) Acquire missing link on continuous stretch	IRB Infrastructure Essel Infraprojects Sadbhav Infraprojects TRIL Roads

Source: Industry, Systematix Institutional Research

New investment options

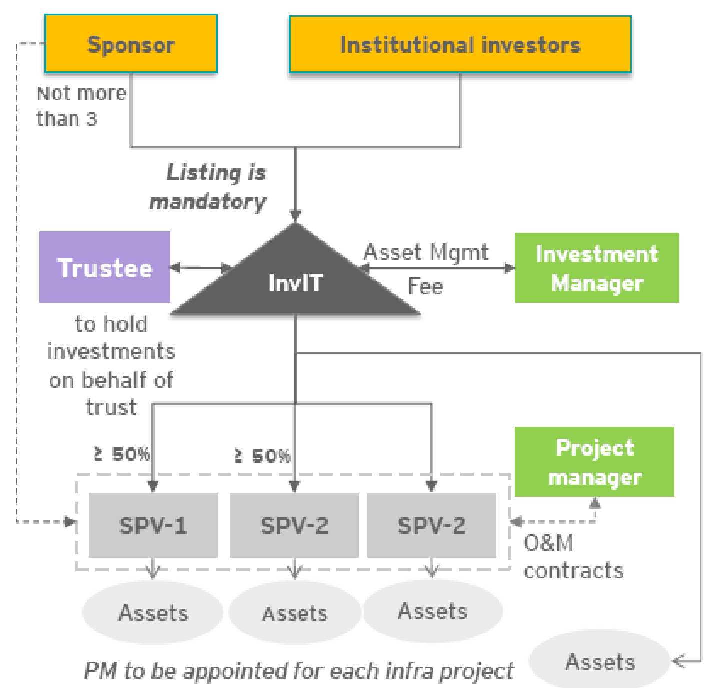
To tap the growing appetite of institutional/financial investors for Indian roads, two options are identified to free up domestic capital, both debt and equity. While InVIT involves divestment of road assets by private asset owners, the TOT model involves monetisation of public funded projects by NHAI.

A) Infrastructure Investment Trusts (InVIT)

In 2014, Sebi allowed Indian firms to launch infrastructure investment trusts to help cash-strapped developers get easier access to funds, while also creating a new investment avenue for institutions and high net worth individuals. The intent to allow InVITs in India for infra projects is to lower the domestic loan exposure to the sector and bring more foreign capital.

InVITs are trusts that manage income generating infrastructure assets, typically offering investors regular yields and a liquid method of investing in infrastructure projects. Developers can use the long-term funds raised to unlock value in completed projects or repay debt associated with them.

Chart 18: Framework



InvIT Structure	
Sponsor	Setup InvIT and appoint the trustee
	Hold minimum required percentage of total units of InvIT
Trustee	Hold InvIT's assets in the name of InvIT for the benefit of unit holders
	Ensure investment manager makes timely payment of dividend to unit holders
Investment Manager	Make investment decisions in relation to underlying assets
	Ensure assets have proper legal title and contracts entered are legal, valid and binding
Project Manager	Undertake operations and management of InvIT assets
	For under construction projects, ensure progress of developments, approval status and such other aspects

Source: Industry

Table 20: Indicative order of key cash inflows and outflows

Fund raising exercise	1.	InVIT raises proceeds from investors i.e. unit holders
	2.	InVIT pays consideration (cash) to sponsor for equity stake purchase in the project SPVs (sponsor to retain minimum 26% in InVIT)
	3.	InVIT to invest in NCDs in the underlying target assets to replace any existing debt (external and sub-debt)
Post the fund raising exercise	4.	Target assets upstream operating cash flows to InVIT in the form of debt service (Principal repayment + Interest(withholding tax just 5%)) and Dividends (dividend distribution tax NIL); SPVs are also required to distribute at least 90% of net distributable cash flow to InVIT (subject to Companies Act, 2013)
	5.	InVIT distributes at least 90% of its net distribution cash flows to unit holders

Source: ITNL PPT

Table 21: Companies that filed InVIT documents with SEBI

InVIT	No. of projects	kms	Target fund raising (Rs bn)
Reliance Infra	10	770	30
IRB Infra	6	3,635	43
ILFS Transportation Network	4	1,995	50

Source: Company

B) Toll Operate Transfer

The government has approved the monetisation of public funded, operational national highway (NH) projects that are generating toll revenue for at least two years after the start of operations through the Toll Operate Transfer (ToT) model.

The stretches of national highway already constructed by NHAI or a concessionaire will be bid out to the private sector investors (infrastructure developers, private equity, institutional investors like pension, wealth funds) against an upfront concession fee. The private party will operate and collect toll on the stretch during the concession period.

Key benefits of the model are: (a) efficient operation and maintenance of national highways, (b) checking pilferage of toll revenue and (c) securitisation of future toll revenue to create new road infrastructure.

Based on healthy annual revenue to attract domestic and international investors, NHAI had shortlisted 102 public funded national highways for monetisation.

Table 22: Selection criteria for projects under ToT

Annual revenue as a % of project cost	No of projects
> 10% of project cost	44
5-10% of project cost	24
< 5% of project cost	34
Total	**102**

Source: MoRTH

As of now, 75 operational NH projects have been identified for monetisation under the ToT model. The aggregate length of these projects is ~4,500km and their annual toll collection is ~Rs27bn. To assess the quality of these projects before they are bid out, NHAI has invited RFQ from technical consultants for ToT model. The ministry expects to raise Rs800-Rs1000bn initially from monetisation of public funded highway projects.

Capacity augmentation under ToT model:

As per the broad contours of ToT model, capacity augmentation should be undertaken once the average traffic in any year exceeds the target traffic. Two options are being considered:

a) The augmentation can be taken up by the authority under EPC contract and the additional revenue post augmentation can be shared in a fixed proportion between concessionaire and authority or

b) The concessionaire can take up augmentation. In which case, the land acquisition and approvals would be done by the authority. The concession period can be extended to account a fresh investment..

Operating and maintenance of the augmented road, however, is done by the concessionaire in both options.

New initiatives/programs to keep momentum on

1) High density Corridors

The government has approved a plan to construct expressways along high density corridors. Of the 9 corridors planned, the government has fast tracked three: Delhi-Meerut and Eastern peripheral which are at various states of construction and Vadodara-Mumbai expressway at bidding stage.

Table 23: Details on High Density Corridors

Stretch	km	NH	Status
Delhi - Meerut	66	24	1st phase comprising of improving 50kms from Delhi to Hapur in 3 phases; already awarded
Eastern Peripheral Expressway	135	11	Awarded into 6 packages on EPC mode with total aggregate cost of Rs44bn.
Western Peripheral expressway	135		Work in two phases: 52km Manesar –Palwal is ready; Work on 83km BOT Kundali- Manesar scheduled for completion by 31st Aug'2018
Vadodara – Mumbai Corridor	400	8	To be completed in 3 phases.
Bangalore – Chennai	334	4	Feasibility cum Preliminary Design report state
Delhi - Jaipur	261	8	NA
Delhi- Chandigarh	249	1 and 22	NA
Kolkata – Dhanbad	277	2	NA
Delhi – Agra	220	2	NA
Total	**2,077**		

Source: MoRTH

2) **Economic corridors:** Recently, NHAI had invited bids to prepare detailed project reports (DPR) for the development of 44 economic corridors totaling to 15,000km in phase 1. Overall, the government is planning to develop 35,000km of highways at an estimated cost of Rs3,000bn under the Economic Corridor Project for faster movement of freight.

3) **Bharatmala:** This has been envisaged as an umbrella program that will subsume unfinished parts of NHDP and also focus on new initiatives like development of border and international connectivity roads, coastal & port connectivity roads, national corridors efficiency improvements, economic corridors development and others.

4) **Char Dham Mahamarg Vikas Pariyojna:** The project aims to improve the connectivity to 'Char Dham' pilgrimage centres in the Himalayas, making the journey to these centres safer, faster and more convenient.

- The 'Char Dham' project includes developing 900km of national highways in Uttarakhand at a total cost of Rs120bn.
- Work for 17 projects worth Rs30bn have already been sanctioned and tendered.
- The entire length of highways will be two-laned, with paved shoulder and a minimum width of 10 metres.
- There will be tunnels, bypasses, bridges, subways and viaducts to prevent traffic bottlenecks.

5) **Setu Bharatam:**

This is a programme to make road travel safe by constructing ROB/under passes at all 208 level crossings in the country. The aim is to make national highways free of railway level crossings by 2019. In addition to this, ~1,500 old and depreciated bridges will also be improved by replacement/widening/strengthening in a phased manner at a cost of ~Rs30bn. MoRTH has already invited bids to appoint a consultancy to prepare a detailed project report for this.

6) **National Highways Interconnectivity Improvement Project:** This project will ensure a safe, fast and all-weather movement of traffic on national highways, mostly located in backward regions. The development of 1,120km of national highways in Karnataka, Odisha, Bihar, Rajasthan and West Bengal has been approved. Projects are already taken up for implementation and 429km have been completed. Civil works are expected to be completed by July 2019 and maintenance works by July 2024.

7) **LWE road connectivity projects at Rs117bn**

- CCEA has approved the road connectivity project for Left Wing Extremism (LWE) affected areas.
- Under the project, construction or upgradation of 5,411.81km of road and 126 bridges/cross drainage works will be taken at an estimated cost of Rs117bn.
- The project will be implemented as a vertical under the Pradhan Mantri Gram Sadak Yojana (PMGSY) to provide connectivity with necessary culverts and cross-drainage structures in 35 worst affected LWE districts, which constitute 90% of the total violence and 9 adjoining districts, critical from the security and communications point of view.
- The fund sharing pattern will be same as PMGSY — in the ratio of 60:40 between the Centre and all states, except for eight North Eastern and three Himalayan states (Jammu & Kashmir, Himachal Pradesh & Uttarakhand), for which it is 90:10.
- Finance Ministry will allocate Rs70bn to the Rural Development Ministry for this project during the period of implementation, 2016-17 to 2019-20.
- Roads taken up under the scheme would include other district roads (ODRs), village roads (VRs) and upgradation of existing major district roads (MDRs) that are critical from the security point of view.
- In Budget 2017, 2,000 km of coastal connectivity roads have been identified for construction and development to facilitate better connectivity of ports and remote villages.

Stock selection paramount - prefer companies with strong balance sheet and longer residual asset life

Our analysis of stock returns of listed companies in BOT roads and EPC space indicate that only six companies of 19 have consistently delivered positive returns in three of four time periods (1/3/5/7-year), while IRB Infra has delivered positive return in 2/4 time periods. This implies investors have rewarded companies that focused on their core road BOT segments and with diversified EPC operations in growing segments in addition to roads.

Table 24: +ve stock returns for >3 time periods for EPC & core BOT focused companies

INDEX	1Y	3Y	5Y	7Y
S&P BSE SENSEX INDEX	19.1	35.0	64.3	71.5
Nifty 50	21.0	39.7	66.3	76.9
Asset owners				
Larsen & Toubro	31.6	24.2	67.3	49.4
Sadbhav Engineering	15.1	224.8	93.2	136.7
IRB Infrastructure Developers	(0.8)	133.9	17.3	(9.1)
Ashoka Buildcon	(1.9)	162.2	185.0	69.2
IL&FS Transportation Network	41.4	(11.1)	(44.1)	(57.6)
Gammon Infrastructure Projects	(21.0)	(45.5)	(73.0)	(84.1)
Supreme Infrastructure India	22.5	(58.3)	(65.1)	(50.5)
GMR Infrastructure	41.1	(23.3)	(49.7)	(70.8)
GVK Power & Infrastructure	(11.7)	(38.6)	(68.6)	(85.7)
Lanco Infratech	(30.1)	(45.0)	(83.5)	(93.2)
Noida Toll Bridge	(50.3)	(50.0)	(45.8)	(64.6)
Sadbhav Infraprojects	8.3	(7.5)	(7.5)	(7.5)
JAIPRAKASH ASSOCIATES LTD	93.8	(70.9)	(82.7)	(90.3)
PNC Infratech	7.4	NA	NA	NA
Dilip Buildcon	NA	NA	NA	NA
MEP Infrastructure	20.4	NA	NA	NA
JMC Projects	8.1	185.0	73.5	37.3
Gayatri Projects	24.4	1,206.2	440.9	93.7
HCC	98.5	162.4	36.5	(45.2)

Source: Bloomberg

However, all companies delivered muted 1 year return vs 3 year return and v/s 1 year Nifty return of 21%, as 1) unavailability of land combined with heavy monsoon delayed execution of projects awarded in FY16 and 2) downward revision of FY17 revenue guidance by few companies will lower the estimated earnings. We initiate coverage on Ashoka Buildcon, PNC Infratech, Sadbhav Engineering and Dilip Buildcon, given their five-year average D/E ratio is well within the range of 0.8-2.2, healthy BOT portfolio with average residual life of 15 years and a diversified EPC order book with a focus on irrigation/mining/airports/power distribution apart from roads. While IRB Infra is the largest player with 22 BOT assets, we would wait for a reduction of 3.0x D/E, clarity on InVIT and pick-up in traffic growth on operational assets to match with Mumbai-Pune expressway that ends in August 2019. Ashoka Buildcon and PNC Infratech are our top picks. Key monitorables – 1) execution ramp-up of existing order book in FY18, 2) traffic growth post demonetisation and 3) NHAI awarding pipeline.

Annexure

Table 25: Status of arbitration awards

Company	Project	Amount awarded by AT	Total amount of award (principal + interest)	75% of amount payable by NHAI
		Rs mn	Rs mn	Rs mn
IL&FS Engineering and Construction	Dharamtul-Jagiroad	1,192	2,053	1,540
Oriental Structure Engineers - KMC (JV)	Allahabad bypass	17	26	20
Oriental Structure Engineers - KMC (JV)	Allahabad bypass	257	391	293
Oriental Structure Engineers - KMC (JV)	Allahabad bypass	637	694	521
Oriental Structure Engineers - KMC (JV)	Allahabad bypass	16	25	19
Oriental Structure Engineers	Jhansi bypass	NA	105	79
Oriental Structure Engineers	Jhansi bypass	NA	220	165
Oriental Structure Engineers	Jhansi bypass	NA	10	7
Oriental Structure Engineers	NH-25	NA	311	233
Oriental Structure Engineers	Mathura - Agra	NA	58	43
OSE Oriental Gammon (JV)	Four laning of NH-2 section	11	23	17
OSE Oriental Gammon (JV)	Four laning of NH-2 section	10	22	16
OSE Oriental Gammon (JV)	Four laning of NH-2 section	19	24	18
OSE Oriental Gammon (JV)	Four laning of NH-2 section	721	1,101	826
OSE Oriental Gammon (JV)	Four laning of NH-2 section	26	54	41
Ssangyong OSE Oriental (JV)	Four laning of NH-2 section	52	112	84
Ssangyong OSE Oriental (JV)	Four laning of NH-2 section	355	596	447
Gayatri - ECI (JV)	East-West corridor	38	53	39
Gayatri - ECI (JV)	East-West corridor	26	35	26
Gayatri - ECI (JV)	East-West corridor	21	26	19
AFCONS Infrastructure	Poornamallee-Kancheepuram	NA	199	149
AFCONS Infrastructure	Haveri-Hubli	NA	1232	924
AFCONS Infrastructure	Hyderabad-Bangalore	NA	447	335
Jog-Shirke (JV)	Bridge across Panvel creek	216	330	248
HCC Ltd	Kolaghat-Kharagpur	12	15	11
HCC Ltd	Kolaghat-Kharagpur	1	2	1
HCC Ltd	Kolaghat-Kharagpur	6	18	14
HCC Ltd	Kolaghat-Kharagpur	3	9	7
HCC Ltd	Kolaghat-Kharagpur	490	1,097	-
HCC Ltd	Lucknow-Muzaffarpur	1,352	2,754	2,065
HCC Ltd	Lucknow-Muzaffarpur	531	1,170	878
HCC Ltd	Lucknow-Muzaffarpur	374	670	502
HCC Ltd	Lucknow-Muzaffarpur	NA	175	131
HCC Ltd	Chennai bypass	NA	66	50
HCC Ltd	Chennai bypass	NA	2,766	2,075
HCC Ltd	Allahabad bypass	1354	1,827	1,370
HCC Ltd	Lucknow-Muzaffarpur	NA	138	104
HCC Ltd	Lucknow-Muzaffarpur	NA	433	325
HCC Ltd	Four laning of NH-76 section	314	693	520
HCC Ltd	Lucknow-Muzaffarpur	NA	1,521	1,141
HCC Ltd	Chadikhol-Paradip	700	777	583
Backborne Projects	Agra-Gwalior	NA	778	584
DS Toll Road	Dindigul bypass-Samayanallore	NA	1,067	800
NK Toll Road	Namakkal bypass	688	711	533
Total		**9,439**	**24,834**	**17,803**

Source: NHAI

COMPANIES SECTION

Ashoka Buildcon

27 March, 2017

On strong footing

INITIATING COVERAGE

Sector: Construction | **Rating: Buy**

CMP: Rs186 | **Target Price:Rs231**

Stock Info

Sensex/Nifty	29,332/ 9,086
Bloomberg	ASBL IN
Equity shares (mn)	187
52-wk High/Low	Rs200/ 111
Face value	Rs5
M-Cap	Rs35bn/ $0.5bn
3-m Avg volume	$0.5mn

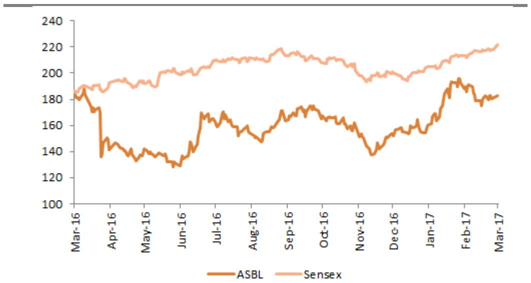
Financial Snapshot (Rs bn)

Y/E March	FY17e	FY18e	FY19e
Sales	28,730	32,734	36,909
EBITDA	8,024	7,861	8,405
PAT	1,183	1,264	1,492
EPS (Rs)	1.7	2.6	3.5
PE (x)	29.4	27.6	23.5
EV/EBITDA (x)	9.7	9.8	9.0
P/BV (x)	1.8	1.7	1.6
RoE (%)	6.2	6.3	7.1
RoCE (%)	9.9	9.1	9.8
Dividend yield (%)	0.9	0.9	1.1
Net gearing (x)	2.2	2.1	1.9

Shareholding pattern (%)

	Dec '16	Sep '16	Jun '16
Promoter	56.7	56.7	56.7
–Pledged	-	-	-
FII	7.7	8.4	8.1
DII	24.4	23.1	22.3
Others	11.2	11.8	12.9

Stock Performance (1-year)



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Ashoka Buildcon Ltd (ASBL) led by its integrated business model - strong in-house EPC, O&M capabilities and own construction equipment bank of Rs2.7bn, is involved in construction of roads and power distribution business with presence in Maharashtra, MP, Chattisgarh, WB, Bihar and TN. December'16-end EPC orderbook is at historical high of Rs62bn (3.4xTTM revenue) to be executed over 2.5-3 years. ASBL is L1 two orders (one HAM and one EPC).In addition, healthy NHAI bid pipeline of Rs250bn for 20 HAM projects in near term, provides comfort for 18% revenue CAGR over FY17-19e. Seven large-size operational BOT projects carved into Ashoka Concessions (ACL), ASBL and SBIM have 61%: 39% stake, with a residual age of 15+ years, can generate 7.0% CAGR in toll revenue over FY16-26e. Going ahead, as SBIM is looking for an exit; ASBL will invest equity of Rs2.5bn in two annuities, one HAM and city gas distribution projects from internal accruals. We initiate coverage on ASBL with a Buy and a SOTP-based target price of Rs231, valuing the EPC business at Rs157/share (15xFY19e), BOT projects at Rs71/share and Rs4/share for land.

Robust EPC order book, healthy bid pipeline to drive 18% EPC revenue CAGR over FY17-19e

December'2016-end EPC order book of Rs62bn (3.4x TTM revenue) comprises 44% from third party road EPC, 29% from captive road BOTs and 27% from power distribution EPC. While captive BOTs -- Chennai ORR and KSHIP are nearing completion, execution has picked up pace in two Karnataka annuity projects and most of the third party EPC projects barring Islampur bypass and Chaas project in Jharkhand (affected by land acquisition issues). ASBL along with a JV partner is L1 in one package of Lucknow- Balia expressway worth ~Rs18bn and solely in one HAM project worth Rs12bn. NHAI pipeline remains strong and ASBL will participate in 7-8 HAM projects out of 20 HAM projects worth Rs250bn (1,250km) that are expected to be tendered out in March'17. We estimate 30% order book CAGR over FY17-19e. ASBL has recently won a project in Ratnagiri for laying of city gas distribution pipeline involving total project cost of Rs1.5bn spread over five years. Based on average execution period of 2.5-3 years, we estimate 18% CAGR in standalone revenue over FY17-19e. The management has guided for 5-8% revenue growth for FY17e.

Lucrative BOT assets portfolio – offering stable cash flows and growth

Ashoka Concessions Ltd (ACL) is the holding company for seven large BOT projects, where ASBL and a private equity investor SBIM hold 61:39 stake. Four of the seven BOT projects are on NH6 (ACL 24% market share) and pass through industrialized areas of power, steel and mining thus offering good potential for movement of traffic. While toll collection dipped marginally by 2% yoy in 9MFY17 due to stoppage of toll collection led by demonetization, ASBL has claimed Rs300mn for loss of toll revenue. The management has indicated bounce back in overall traffic since January'17 for Dhankuni-Kharagpur toll project (~7-8% led by port traffic) in particular and 5-6% average traffic growth across projects in general. Given insignificant revenue contribution (residual age 12-20 months) from four ASBL-owned BOT projects, we expect the toll collection for ACL portfolio with a residual age of 15+ years to grow 7.0% CAGR over FY16-26e. Along with 150-300bps lower refinancing of three projects and savings on premium deferment, will drive 60% CAGR in FCFE over FY24e-30e.

Steady EPC EBITDA margin, healthy consolidated balance sheet

ASBL's led by its integrated business model, efficient execution and conservative bidding strategy for both road and power BOT projects has consistently delivered EBIDTA margins in range of 12.5-13.5% over FY10-16. Going ahead, we estimate consolidated EBITDA margin to trend downwards to 23% in FY18/19e (vs 25% for FY15-16) led by 1) concession period completion for four of ASBL margin accretive BOT toll projects 2) major maintenance expenditure for Durg and Jaora BOT projects and 3) EPC revenue mix comprising of power distribution(OPM 10.5-11%), third party road EPC (OPM 11-11.5%) and HAM (OPM-12.5%) will stabilize standalone EBIDTA margin at 12.0%.We expect ramp up in execution of new EPC orders and rising BOT toll/ annuity revenue to generate sufficient cash flows to meet the routine capex(Rs500mn) and equity required in CGD/annuity/HAM projects (Rs2.5bn). We expect consolidated D/E to reduce to 1.9x and ROE/ROCE to improve to 7.1%/9.8% in FY19e.

Investors are advised to refer through disclosures made at the end of the research report.

FINANCIALS (CONSOLIDATED)

Profit & Loss Statement

YE: Mar (Rs mn)	FY15	FY16	FY17e	FY18e	FY19e
Net revenues	23,197	26,724	28,730	32,734	36,909
Revenue growth (%)	29.2	15.2	7.5	13.9	12.8
- Op. expenses	18,467	18,710	20,705	24,873	28,504
EBIDTA	4,730	8,013	8,024	7,861	8,405
EBITDA margins (%)	20.4	30.0	27.9	24.0	22.8
- Interest expenses	2,721	4,478	4,187	4,193	3,955
- Depreciation	1,517	2,491	1,947	2,139	2,262
+ Other income	290	668	412	502	513
PBT	782	1,712	2,304	2,032	2,702
- Tax	796	973	1,497	813	1,081
Effective tax rate (%)	101.7	56.9	65.0	40.0	40.0
Adjusted PAT	(13)	739	806	1,219	1,621
+/- Extraordinary items	-	570	-	-	-
+/- Minority interest	(828)	(995)	(377)	(45)	129
Reported PAT	815	2,304	1,183	1,264	1,492
Adj. FDEPS (Rs/share)	(0.0)	1.6	1.7	2.6	3.5

Source: Company, Systematix Institutional Research

Balance Sheet

YE: Mar (Rs mn)	FY15	FY16	FY17e	FY18e	FY19e
Share capital	793	936	936	936	936
Reserves & Surplus	12,776	17,752	18,580	19,465	20,509
Networth	13,569	18,688	19,516	20,401	21,445
Minority interest	5,047	4,995	4,400	4,073	3,986
Total Debt	37,843	40,479	43,561	42,650	41,232
Def. tax liab. (net)	(99)	(221)	(221)	(221)	(221)
Capital employed	**56,360**	**63,941**	**67,256**	**66,902**	**66,442**
Net Fixed assets	125,712	125,831	130,083	129,565	128,997
Intg. assets under devp.	1,505	3,455	3,455	3,455	3,455
Investments	2,403	3,377	3,377	3,377	3,377
Net Working capital	(73,670)	(70,401)	(69,976)	(70,165)	(69,589)
Cash and bank balance	410	1,679	316	671	201
Capital deployed	**56,360**	**63,941**	**67,256**	**66,902**	**66,442**
Net debt	37,433	38,800	43,245	41,979	41,031
WC ex- LT liabilities (days)	65	78	73	52	42
Book value (Rs/sh)	86	100	104	109	115

Source: Company, Systematix Institutional Research

Cash Flow

YE: Mar (Rs mn)	FY15	FY16	FY17e	FY18e	FY19e
PAT	815	1,163	1,183	1,264	1,492
+ Non cash items	1,438	2,369	1,947	2,139	2,262
Cash profit	2,253	3,533	3,130	3,403	3,754
- Incr/(Decr) in WC	1,708	3,269	426	(189)	577
Operating cash flow	545	264	2,704	3,592	3,177
- Capex	7,190	4,410	4,962	480	480
Free cash flow	(6,645)	(4,146)	(2,258)	3,112	2,697
- Dividend	242	281	296	316	373
+ Equity raised	3	5,000	-	-	-
+ Debt raised	6,811	2,636	3,082	(911)	(1,418)
+ Minority Interest	402	(52)	(595)	(327)	(87)
- Investments	(444)	974	-	-	-
- Misc. items	1,309	914	1,296	1,203	(12)
Net cash flow	(535)	1,269	(1,363)	354	(470)
+ Opening cash	945	410	1,679	316	671
Closing cash	410	1,679	316	671	201

Source: Company, Systematix Institutional Research

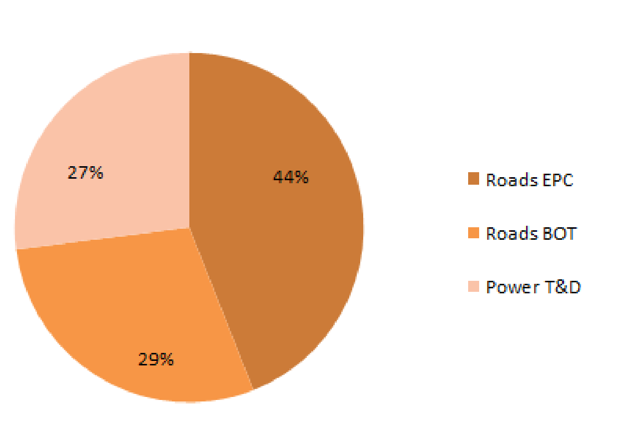
Ratios

YE: Mar	FY15	FY16	FY17e	FY18e	FY19e
P/E (x)	36.2	20.1	29.4	27.5	23.5
Core P/E - standalone (x)	13.0	12.8	12.7	12.1	11.0
P/B (x)	2.2	1.9	1.8	1.7	1.6
EV/EBITDA (x)	14.2	9.2	9.7	9.8	9.0
RoE (%)	6.3	10.7	6.2	6.3	7.1
RoCE (%)	6.8	10.0	9.9	9.1	9.8
Fixed Asset turnover (x)	0.3	0.2	0.2	0.2	0.3
Dividend yield (%)	0.8	0.8	0.9	0.9	1.1
Dividend payout (%)	29.7	24.1	25.0	25.0	25.0
Interest exp./Sales	11.7	16.8	14.6	12.8	10.7
Debtors (days)	57	50	51	50	50
Revenue growth (%)	29.2	15.2	7.5	13.9	12.8
PAT growth (%)	(28.3)	80.3	(31.7)	6.8	18.1
EBITDA growth (%)	19.9	69.4	0.1	(2.0)	6.9
EPS growth (%)	(28.3)	80.3	(31.7)	6.8	18.1
Net gearing (%)	2.8	2.1	2.2	2.1	1.9

Source: Company, Systematix Institutional Research

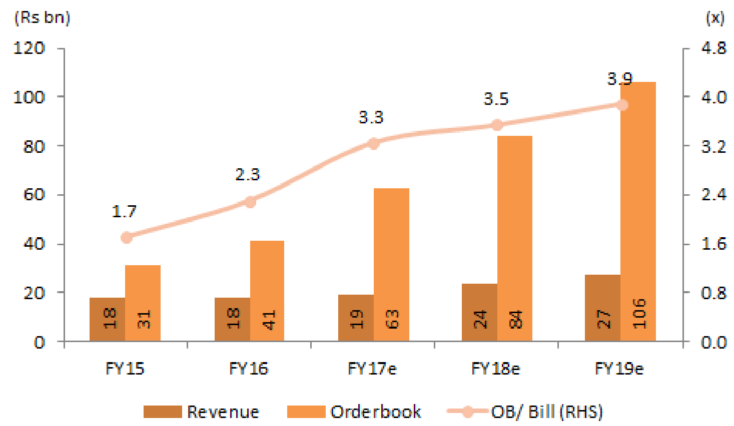
Charting the story

Chart 1: Diversified EPC order book at Rs62bn



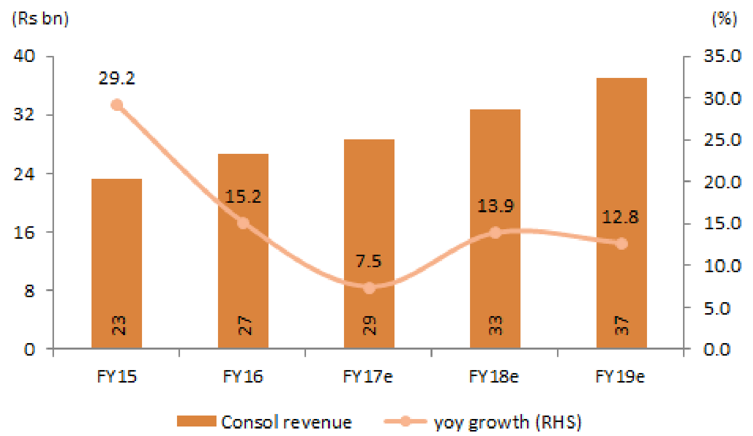
Source: Company

Chart 2: Robust Book-to-bill renders revenue visibility



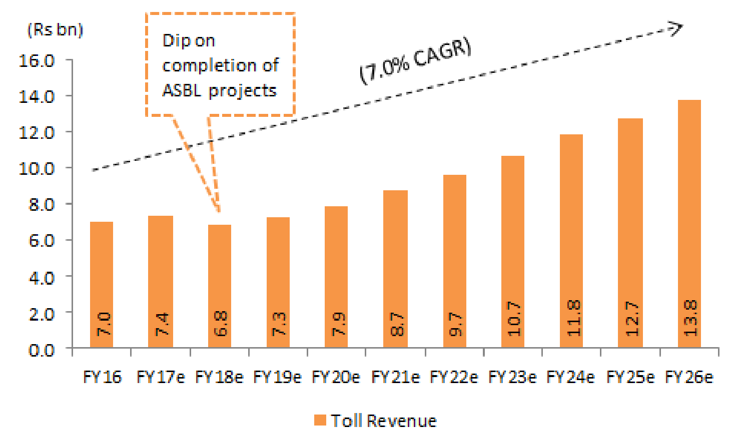
Source: Company, Systematix Institutional Research

Chart 3: Consolidated revenue to grow 13% CAGR over FY17-19e



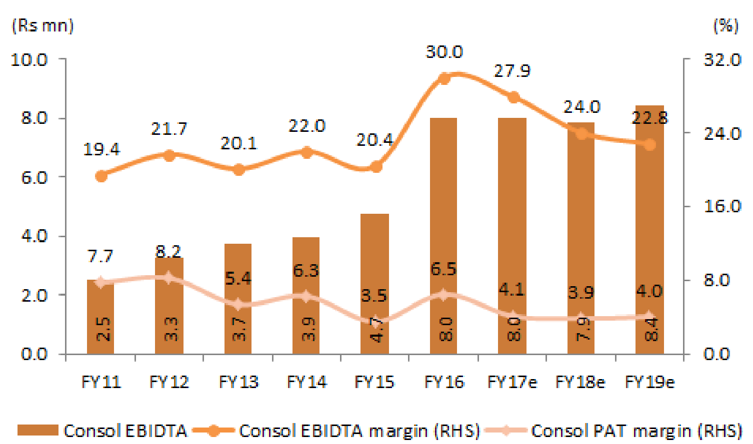
Source: Company, Systematix Institutional Research

Chart 4: Toll collection on rising trajectory barring FY18



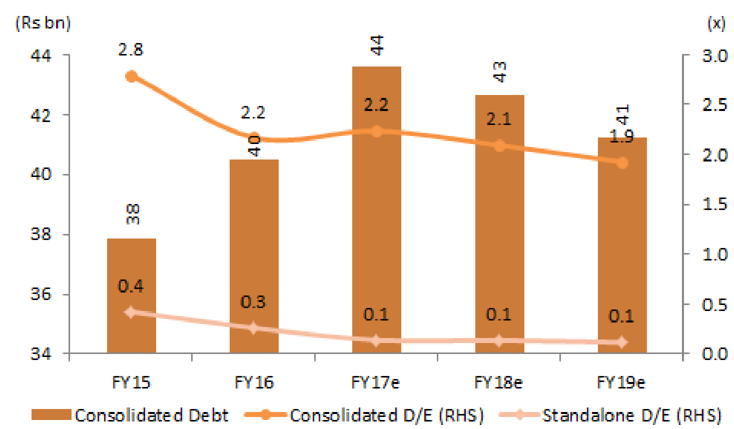
Source: Company, Systematix Institutional Research

Chart 5: Completion of ASBL road projects to impact consol OPM



Source: Company, Systematix Institutional Research

Chart 6: ... Consol D/E ratio to improve on cash flow generation

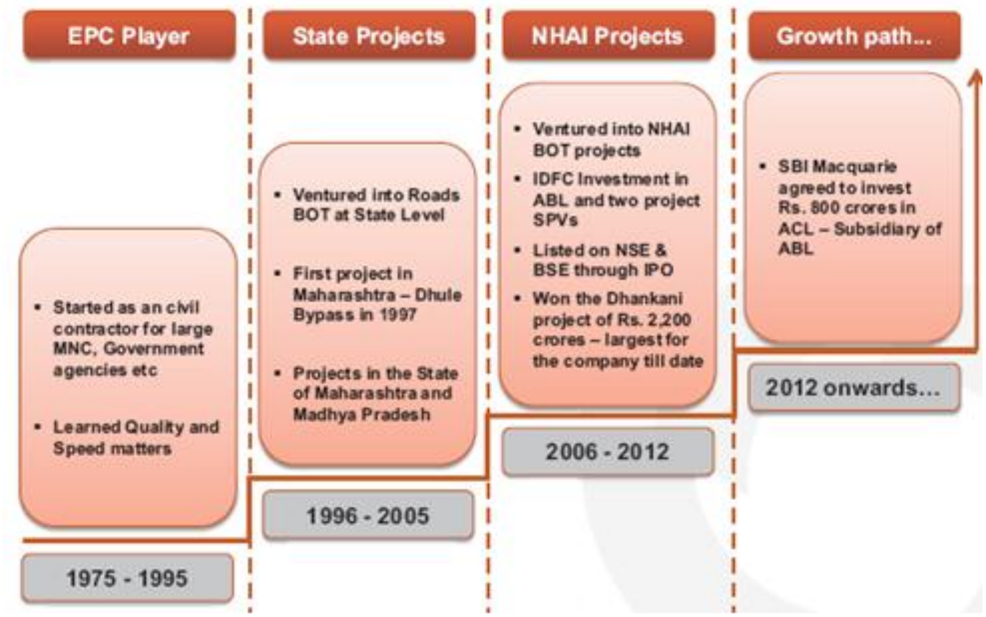


Source: Company, Systematix Institutional Research

Strong EPC order book at Rs62bn

ASBL is a construction company for road, highways and power distribution segments. Having constructed 7,000+ lane kms of roads (state and national highways), the company has a rich experience in undertaking EPC and BOT-based projects. From being a regional player confined to Maharashtra, ASBL has evolved and has a BOT portfolio of 4,140 lane kms (operational + under construction) spread across Madhya Pradesh, Odisha, Chhattisgarh, Maharashtra, Tamil Nadu, West Bengal and Karnataka. In the power distribution segment, the company is involved in modernising and setting up new lines.

Chart 7: Evolution of ASBL



Source: Company, Systematix Institutional Research

Backward integration to aid EPC activities

ASBL began manufacturing ready mix concretes (RMC) in year 2000 for in-house use by the EPC division and extended it to third party sales from 2002. The company has 14 RMC plants, with a total production capacity of 650 cubic metres per hour, 86 concrete transit trucks and 19 concrete pumps.

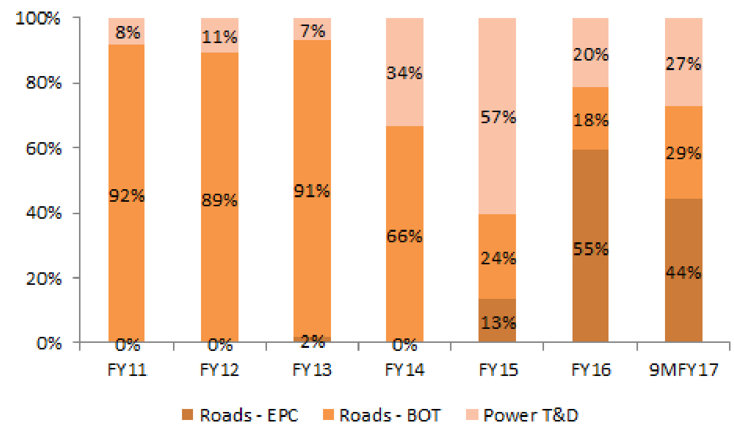
This division also sells and processes bitumen to a higher grade for use in road projects and supports the EPC division. A plant is set up in Pune to process bitumen, with a capacity of 60 metric tonnes per day.

De-risking EPC operations – exposure to road and power distribution

ASBL undertakes EPC projects from inception to completion stage, using state-of-the-art owned equipment fleet of Rs2.7bn and 15 in-house RMC facilities. This not only captures the entire value chain in-house, but also reduces the company's dependence on third party contractors/sub-contractors, ensures timely and adequate supply, better control on costs, timeline and quality of projects.

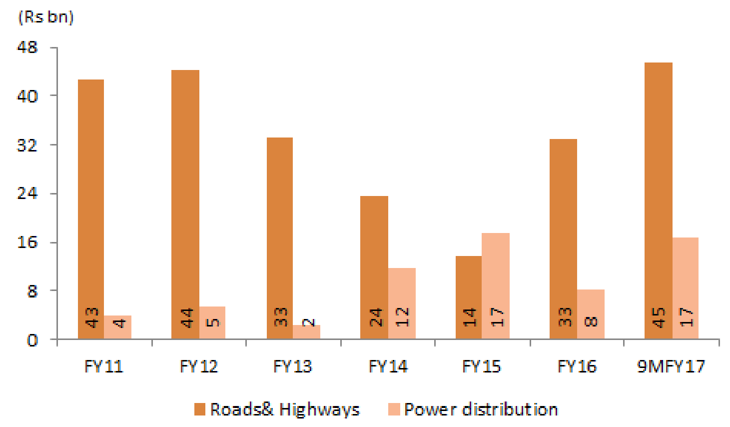
ASBL has refrained from bidding aggressively during times of intense competition in road EPC contracts and diverted its focus to power distribution contracts, as can be seen during FY14-15, thus ensuring a steady order book.

Chart 8: Healthy order book mix of roads and power segments



Source: Company, Systematix Institutional Research

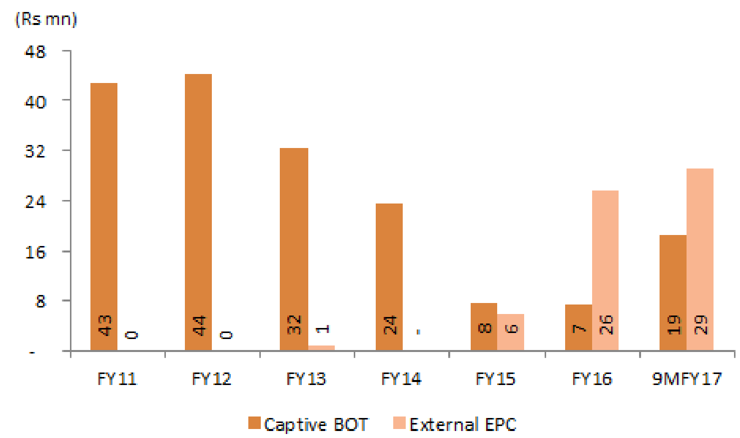
Chart 9: Roads share dominant, power distribution gains pace



Source: Company, Systematix Institutional Research

Core competency - road EPC: ASBL is involved in rehabilitation, upgradation, widening and strengthening of roads and highways for third party EPC and captive road BOT projects.

Chart 10: Shift towards third party road EPC from captive BOT



Source: Company, Systematix Institutional Research

Table 1: Major completed projects in past

Particulars	Rs mn
Phalodi - Pachpadra	1,560
Westerly Bypass	1,413
Chittorgarh Bypass	1,175
East Coast Road, TN	417

Source: Company

Power distribution gains pace: ASBL is involved in modernising and setting up new power distribution lines. Initially confined to Maharashtra, it expanded operations in Bihar, Tamil Nadu and Chhattisgarh. The division has till date executed 25+ power distribution works, with 19,000+ kms of distribution line network.

Table 2: Power T&D: Major projects completed/ ongoing

Particulars	(Rs mn)
Maharashtra Infrastructure Plan	
Phase 1 T8	2,659
Phase 2 T36	3,003
RAPDRP part B T01	1,812
Bihar - RGGVY Yojna	
Samastipur	1,692
Paschim Champaran	1,754
Munger	874
Tamil Nadu - RAPDRP Part B	
Chennai North	2,500
Chennai South	1,414

Source: Company

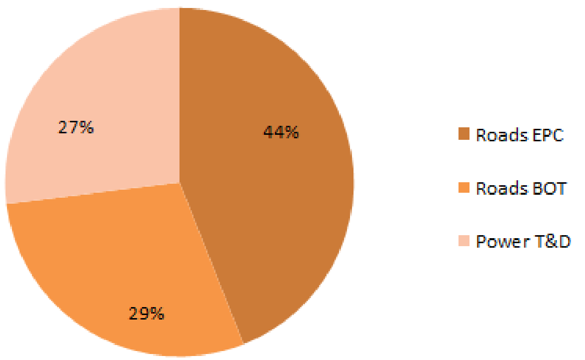
Foray into city gas distribution projects

ASBL, the sole bidder for the project, has recently bagged a city gas distribution (CGD) project in Ratnagiri, Maharashtra to supply gas to domestic and industrial users. The project involves building and operating a CGD network (laying distribution lines), with a 25-year exclusive licence period. An investment of Rs1.5bn will be required in the next five years, where the company will employ capital in 70:30 debt-equity ratio and targets equity IRR of 20%. ASBL will undertake EPC portion of the project. While the management is testing waters in CGD segment, it can bid for more projects in this segment, if the current one proves to be profitable and manageable.

Robust EPC order book at Rs62bn, healthy bid pipeline offers revenue visibility

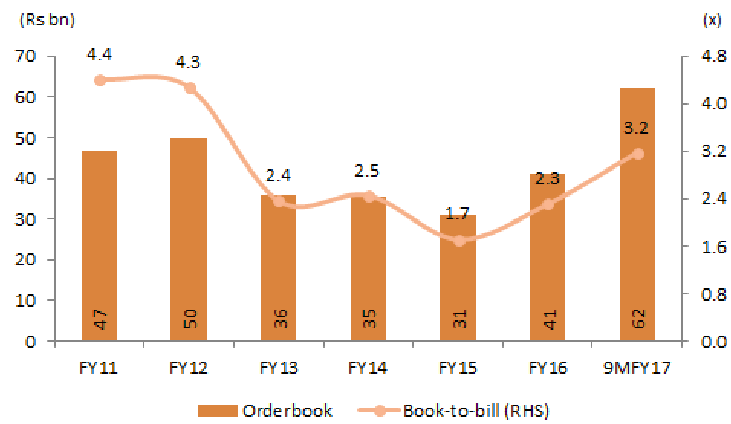
ASBL's order book has risen from Rs46.7bn in FY11 to Rs62bn in 9MFY17, with a book-to-bill ratio at 3.2x TTM sales. The order book is well spread across roads EPC, BOT and power distribution segment.

Chart 11: Diversified EPC order book at Rs62bn



Source: Company

Chart 12: 9MFY17 - book to bill highest in last 4 years



Source: Company

After witnessing initial hiccups pertaining to land acquisition, execution has picked up in third party EPC roads projects such as Eastern Peripheral expressway, Mumbai-JNPT projects, and two Jharkhand projects – Dumka, Govindpur while Islampur bypass and Chaas – Jharkhand are affected due to inadequate land availability. On BOT side, the Chennai ORR (by 1QFY18) and KSHIP (by Mar'17) are nearing completion, two Karnataka annuity projects (Bagewadi and Hungund) have recently commenced construction and the EPC portion (Rs12.7bn) of the newly-won HAM, Ludhiana-Kharar, is likely to commence construction in 1QFY18.

ASBL has recently won orders amounting to Rs1.8bn for rural electrification in Uttar Pradesh. Segment order book at Rs7.5bn comprises contracts largely from Bihar. Given better operational efficiency in Bihar v/s other states, the company has completed execution ahead of schedule in 2QFY17. In Dec'16, ASBL received letters of intent for rural electrification works worth Rs9.5bn in Sitamarhi, West Champaran, Munger, Patna and Sasaram districts from North and South Bihar Power Distribution Company, under the Deendayal Upadhyaya Gram Jyoti Yojana.

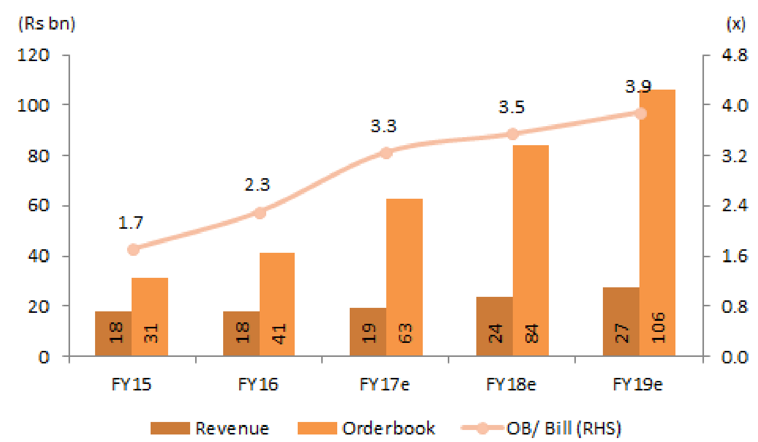
Table 3: Order book as of Dec 31, 2016 – Rs62bn

Project	Rs mn	% of total	Status
Roads – BOT	**17,793**	**29**	
Dhankuni	595	1	Nearing completion
Annuity BOT - Bagewadi	2,484	4	Ongoing since 3QFY17
Annuity BOT- Hungund	2,428	4	Ongoing since 3QFY17
HAM- Ludhiana	12,286	20	FC done, work to start in 1QFY18
Roads - EPC	**29,602**	**48**	
Eastern Peripheral Expressway	6,382	10	Ongoing; pick up pace in H2FY17
Mumbai- JNPT port	3,711	6	Ongoing ; pick up pace in H2FY17
Islampur bypass	2,759	4	Stuck for land acquisition
MoRTH – Badami	5,544	9	ongoing
MoRTH – Madhugiri	1,067	2	ongoing
Jharkhand - Dumka	1,928	3	Commenced construction after delay
Jharkhand- Govindpur	1,791	3	Commenced construction after delay
Jharkhand – Chaas	4,826	8	Stuck for land acquisition,
Others	4,585	7	NA
Power – T&D	**16,808**	**27**	
Maharashtra	862	1	ongoing
Bihar	12,661	20	ongoing
Tamil Nadu	886	1	ongoing
Uttar Pradesh	2,399	4	Recently won
Total Orderbook	**62,303**	**100**	

Source: Company, Systematix Institutional Research

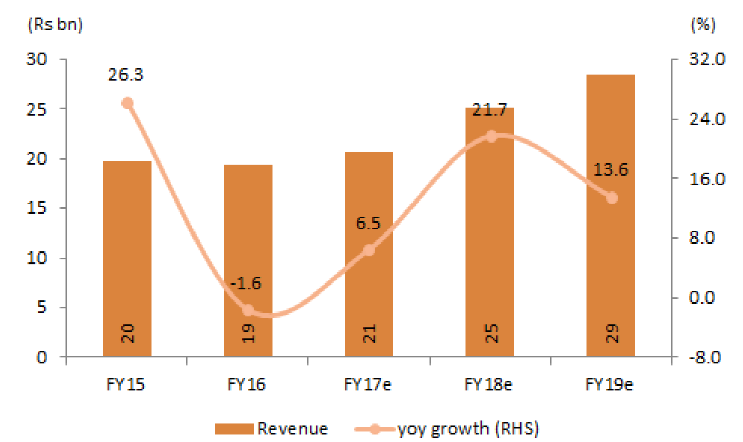
YTDFY17, ASBL has won projects worth Rs19.4bn v/s Rs28bn in FY16. ASBL along with a JV partner is L1 in one package of Lucknow- Balia expressway worth ~Rs18bn. ASBL has received LOA for 6 laning Ranastalam to Anandpuram HAM project worth Rs12bn. NHAI pipeline remains strong and ASBL will participate in 7-8 HAM projects out of 20 HAM projects worth Rs250bn (1,250km) that are expected to be tendered out in March'17. We estimate 30% order book CAGR over FY17-19e. Based on average execution period of 2.5-3 years, we estimate 18% CAGR in standalone revenue over FY17-19e. The management has guided for 5-8% revenue growth for FY17e.

Chart 13: Bid pipeline translates to robust EPC book-to-bill ratio



Source: Company, Systematix Institutional Research

Chart 14: Leading to 18% std. revenue CAGR over FY17-19e



Source: Company, Systematix Institutional Research

Lucrative BOT assets portfolio

Matured standalone portfolio

ASBL was awarded the first BOT project, Dhule bypass in Maharashtra in 1997. Since then, the company has on a standalone level undertaken 9 state BOT projects from Maharashtra and Madhya Pradesh. On completion of the concession period, five operational projects were successfully handed back to the government. The concession period of the remaining four operational projects would end latest by September 2018. In addition, ASBL won two BOT annuity projects in Karnataka, Bagewadi and Hungund, the funding for which was tied up recently. The company has invested Rs550mn in these projects till date and an outstanding equity commitment of Rs550mn (total Rs1.1bn) will be funded in FY18. The EPC arm has started mobilisation and expects to carry out construction of these projects.

Table 4: ASBL's standalone BOT assets portfolio

Particulars	Type	Client	ASBL stake	State	length (lane km)	Concession period ends	Residual age
Operational							
Indore - Edlabad	Toll	MPRDC	99.7%	MP	203	Feb-17	NA
Ahmednagar- Aurangabad	Toll	PWD	100.0%	Maharashtra	168	Dec-17	NA
Katni Road	Toll	PWD- MP	99.9%	MP	35	Feb-20	35 months
Wainganga Bridge	Toll	MoRTH	50.0%	MP	26	Feb-18	11 months

Source: Company, Systematix Institutional Research

Table 5: Under construction projects

Particulars	Type	State	Project cost (Rs mn)	Equity (Rs mn)	Grant (Rs mn)	Debt (Rs mn)	LOA date
Bagewadi-Saundati	Annuity	Karnataka	3,280	550	750	1,980	10th Dec 2015
Hungund-Muddebihal	Annuity	Karnataka	2,940	550	650	1,740	10th Dec 2015
Mudhol- Nepani (KSHIP)	Annuity	Karnataka	4,710	550	136	4,024	12th Dec 2014

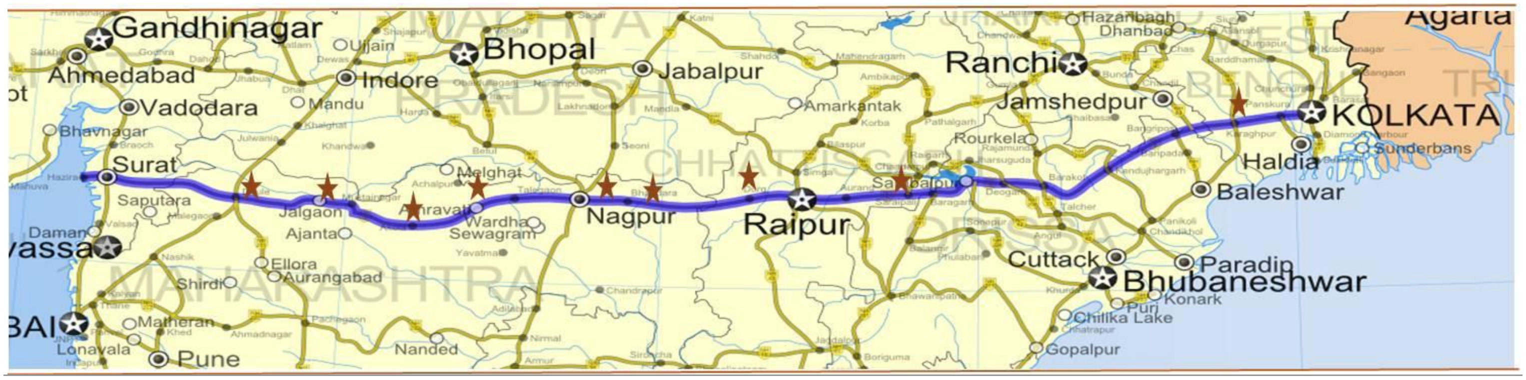
Source: Company, Systematix Institutional Research

ACL portfolio - established BOT assets; blend of stable cash flow and growth

ACL was formed in FY12 to house larger BOT projects (both NH and SH) under this subsidiary. ASBL holds 61% stake, while SBI Macquarie (SBIM) invested Rs8bn in several tranches for a 39% stake, thereby providing equity funding and technical qualification for large projects.

ACL has a portfolio of eight projects -- six operational and two under-construction, spread across 2,970 lane kms. The portfolio is a balanced mix of nascent and matured projects, offering steady revenue stream and growth potential. Given four of the seven projects are on NH6, ACL has 24% market share. NH6 connects six to seven key states across West and East India. The corridor passes through the industrialised areas consisting of power plants, steel plants, mining and minerals and engineering companies and also connects tourism centres. This offers good potential for the movement of commercial and passenger vehicles traffic.

Chart 15: Largest BOT Player on NH-6 with 1,739 Lane kms with over 24% PPP market share



Source: Company

ACL has recently executed a concession agreement with NHAI for 4/6 laning of Kharar-Ludhiana section of NH95 on HAM basis. Given no further equity infusion by SBIM, ASBL is likely to fund the Rs1.5bn equity required in the HAM project over the next two years. ACL plans to add ~Rs50bn of BOT and HAM projects to the portfolio within the next two to three years (equity requirement of Rs12-15bn). SBIM's stake would dilute on the addition of newer projects in ACL. The exit trigger for investors would likely occur in Jan-Feb 2018, on completion of 5-6 years. The management has indicated to get either a good replacement partner or will be buying their stake out in order to provide exit.

Table 6: ACL's BOT assets: lucrative portfolio with average residual life of 15 years

Project	Type	Stake	Client	Lane km	State	Project cost (Rs mn)	Equity (Rs mn)	Residual age (yrs)	Toll/ Annuity FY16
Operational									
Dhankuni- Kharagpur	Toll	100%	NHAI	841	West Bengal	22,000	4,592	10.4	2,442
Belgaum- Dharwad	Toll	100%	NHAI	454	Karnataka	6,940	1,850	24.4	696
Bhandara	Toll	51%	NHAI	377	Maharashtra	5,280	1,635	11.1	592
Durg	Toll	51%	NHAI	368	Chhattisgarh	6,310	2,205	11.8	734
Sambalpur Baragarh	Toll	100%	NHAI	408	Odisha	11,420	3,322	24.5	431
Jaora- Nayagaon	Toll	37%	MPRDC	340	Madhya Pradesh	8,650	3,106	16.9	1,638
Under construction									
Chennai ORR	Annuity	50%	Govt of TN	183	Tamil Nadu	14,400	1,630	17.4	NA
Ludhiana-Kharar	HAM	100%	NHAI	76	Punjab	13,880	NA	15.0	NA

Source: Company, Systematix Institutional Research

Steady traffic pick-up, WPI turnaround to augment toll revenue

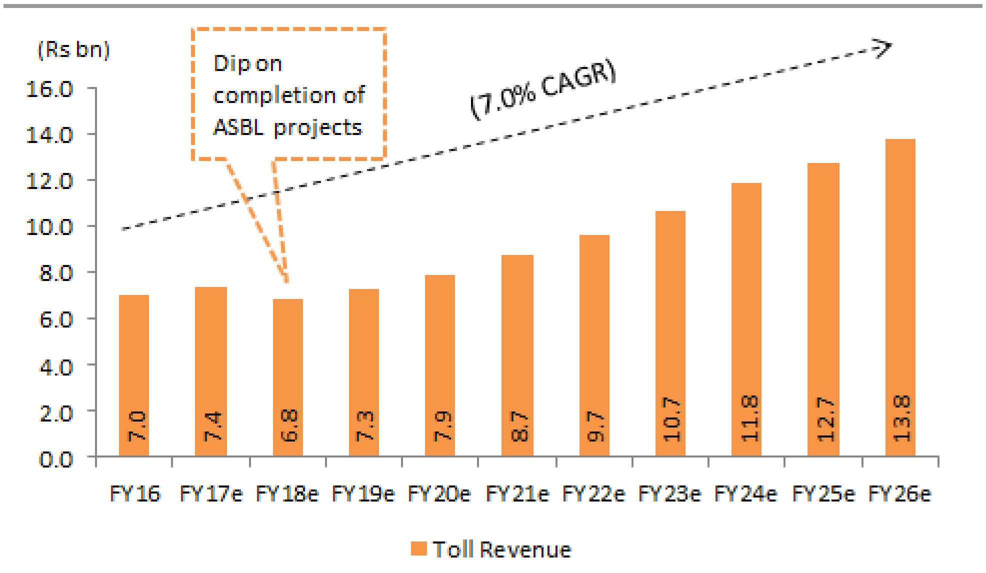
The revenue from toll collection for BOT assets (ASBL+ ACL) clocked 34% CAGR over FY13-16 to Rs6.9bn. Revenue boost was led by a) tolling at six lanes for Dhankuni-Kharagpur on CoD v/s four lanes while under construction, b) diversion of traffic on Jaora-Nayagaon on account of unavailability of parallel stretch and c) robust 70% CAGR in PNG project, led by strong traffic growth.

PNG Tollways in Mar'14 gave a termination notice to NHAI as non–payment of toll from locals as well as lack of state government support led to Rs1bn revenue loss. The consortium (ASBL and L&T) has claimed a total compensation of Rs17bn, including a debt of Rs12bn on account of termination, and received an instalment of Rs1bn from NHAI in August 2016. ASBL has written off Rs1.4bn on account of the equity investment.

While toll collection dipped marginally by 2% yoy in 9MFY17 due to stoppage of toll collection for 23 days led by demonetization, ASBL has claimed Rs300mn for loss of toll revenue. The management has indicated bounce back in overall traffic since January'17 for Dhankuni-Kharagpur toll project (~7-8% led by port traffic) in particular and in general 5-6% average traffic growth across other projects led by gradual improvement in economic activity.

Given insignificant revenue contribution (residual age 12-20 months) from four ASBL-owned BOT projects, we expect the toll collection for ACL portfolio with a residual age of 15+ years to grow 7.0% CAGR over FY16-26e. Along with 150-300bps lower refinancing of three projects and savings on premium deferment, will drive 60% CAGR in FCFE over FY24e-30e. ACL plans to add ~Rs50bn of BOT and HAM projects to the portfolio within the next two to three years (equity requirement of Rs12-15bn).

Chart 16: Long term toll collection revenue growth at 7.0% CAGR over FY16-26e



Source: Company, Systematix Institutional Research

Refinancing, premium deferment to boost FCFE

ACL has successfully refinanced few operational road projects lower by 150-170bps, resulting in savings in interest cost. Refinancing, in our view, can add 10-15% to a project's NPV. Any reduction in interest rates by RBI and subsequent pass-on of benefit by banks can lead to further savings in interest cost.

Table 7: Refinancing to reduce interest cost by 150-300bps

Project	Old interest rates (%)	New interest rates (%)	Reduction in last 2 years (bps)
Durg Chattishgarh	12.6%	9.62%	298
Bhandara Road	12.86%	10.35%	251
Jaora- Nayagaon	11.36%	9.80%	156

Source: Company

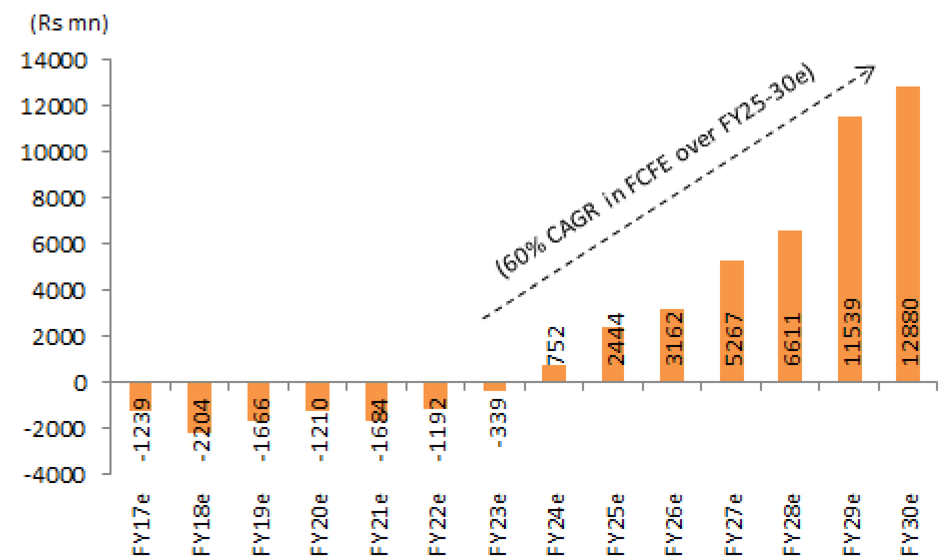
ACL's two projects, Dhankuni-Kharagpur and Belgaum-Dharwad, were considered for premium restructuring in FY14-15, as the projects witnessed low traffic volumes and incurred losses. Premium deferment can result in annual savings of Rs1.1-1.5bn and total savings of Rs7bn over FY16-20e.

Table 8: Reduction of cash outgo of Rs7bn over FY16-20e

Premium payable as contracted (Rs mn)	FY16	FY17	FY18	FY19	FY20
Belgaum- Dharwad	377	396	415	436	458
Dhankuni- Kharagpur	1,459	1,532	1,609	1,689	1,774
Total	**1,836**	**1,928**	**2,024**	**2,126**	**2,232**
Revised premium payable after deferment	**FY16**	**FY17e**	**FY18e**	**FY19e**	**FY20e**
Belgaum- Dharwad	13	19	216	53	360
Dhankuni- Kharagpur	149	389	645	937	276
Total	**162**	**408**	**861**	**990**	**636**
Savings due to deferment	1,674	1,520	1,164	1,136	1,596

Source: Company, Systematix Institutional Research

Chart 17: 60% CAGR in FCFE over FY24e-30e



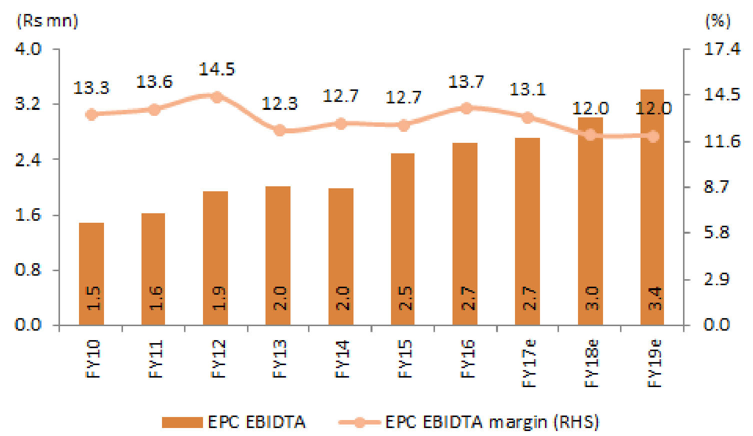
Source: Company, Systematix Institutional Research

We expect Dhankuni-Kharagpur, Durg-Chhattisgarh and Jaora-Nayagaon to generate positive FCFE led by the above refinancing and premium deferment. Projects such as Belgaum-Dharwad, Bhandara Road and Sambalpur-Baragarh are witnessing traffic below estimates, which will continue to weigh on FCFE till FY25. Successful refinancing of interest for Dhankuni and Sambalpur project by May'17 can lead to 100bps+ve improvement in interest cost to 9.7-9.8%. The management indicated a funding loss of Rs400mn in the Sambalpur-Baragarh project in FY17 (Rs1.2bn over last 2.5 years).

Steady EPC OPM, healthy consolidated balance sheet

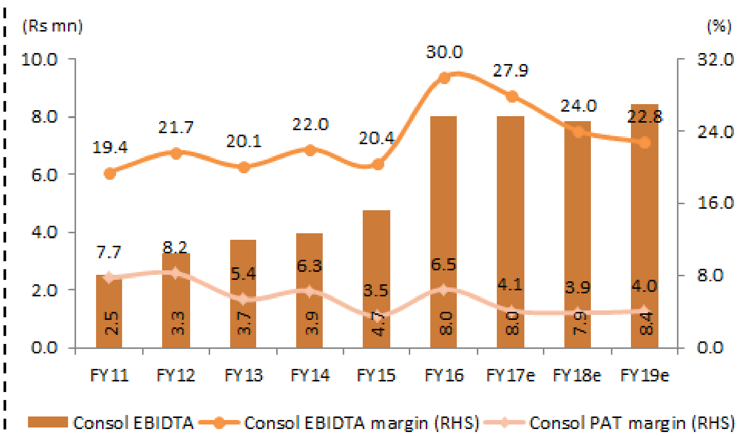
Margins for road EPC are ~12-13%, while that for power distribution is ~10.5-11%. ASBL has refrained from bidding aggressively for EPC projects, both in roads and power distribution segments. This combined with a backward integration of construction activities and execution of captive BOT road orders resulted in average blended EBITDA margin of 13% over FY10-16. For 1HFY17, EBITDA margin improved to 14.2%, led by OPM of 15.8% in 2QFY17. Completion of Bihar power distribution project six month ahead of schedule resulted in savings of Rs160mn (commodity gain + overheads), that augmented 2QFY17 EBITDA margin. As per the management, two more large distribution projects can see some upside, led by savings in cost.

Chart 18: EPC OPM to be at 12.0% led by stable revenue mix



Source: Company, Systematix Institutional Research

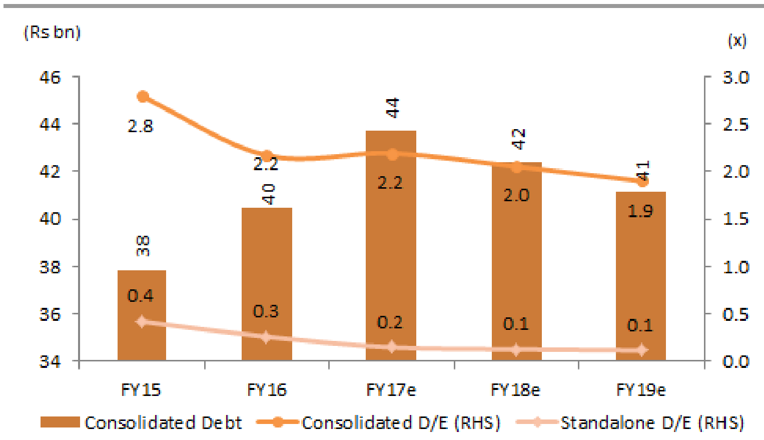
Chart 19: Consol. EBIDTA margin to trend downwards after FY17e



Source: Company, Systematix Institutional Research

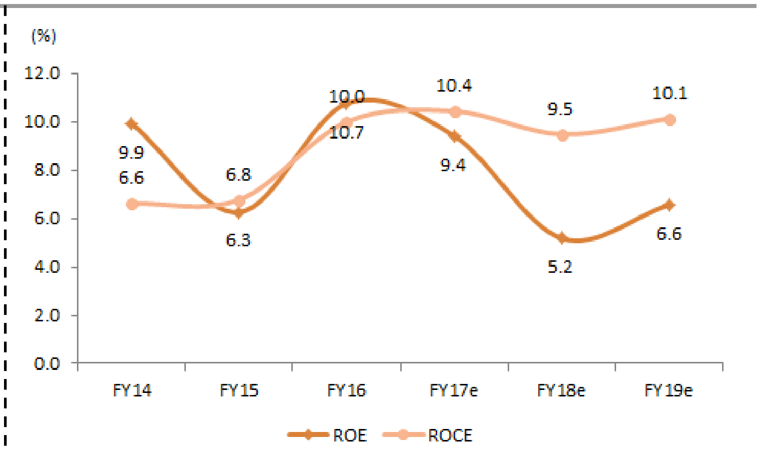
Going ahead, we estimate consolidated EBITDA margin to trend downwards to 23% in FY18/19e (vs 25% for FY15-16) led by 1) completion of concession period completion of four ASBL margin accretive BOT toll projects 2) expenditure for undertaking major maintenance of Durg and Jaora BOT projects and 3) EPC revenue mix comprising of power distribution(OPM 10.5-11%), third party road EPC (OPM 11-11.5%) and HAM (OPM-12.5%) will stabilize standalone EBITDA margin at 12.0%

Chart 20: Low capex, stable working capital to improve gearing



Source: Company, Systematix Institutional Research

Chart 21: Return ratios to improve FY19e onwards



Source: Company, Systematix Institutional Research

We expect ramp up in execution of new EPC orders and rising BOT toll/ annuity revenue to generate sufficient cash flows to meet the routine capex (Rs500mn) and equity required in CGD/annuity/HAM projects (Rs2.5bn). We expect the consolidated D/E to reduce to 1.9x and ROE/ROCE to improve to 7.1%/9.8% in FY19e.

Table 9: Standalone snapshot

(Rs mn)	FY15	FY16	FY17e	FY18e	FY19e
Sales	19,667	19,358	20,616	25,094	28,513
yoy growth (%)	26.3	(1.6)	6.5	21.7	13.6
EBITDA	2,498	2,652	2,709	3,015	3,419
yoy growth (%)	25.9	6.2	2.1	11.3	13.4
EBITDA margin (%)	13	14	13	12	12
Interest	590	558	406	472	485
Depreciation	553	648	514	606	655
PBT	1,938	2,238	2,202	2,439	2,793
Tax	517	644	506	659	838
Adj. PAT	1,422	1,689	1,695	1,780	1,955
yoy growth (%)	19.3	18.8	0.4	5.0	9.8
PAT margin (%)	7.2	8.7	8.2	7.1	6.9
EPS (Rs)	9.0	9.0	9.1	9.5	10.4
D/E (x)	0.4	0.3	0.1	0.1	0.1
Asset Turnover (x)	6.2	5.8	5.6	6.0	6.1
Working Capital (days)	38	146	133	143	137

Source: Company, Systematix Institutional Research

Key management team

Ashok Katariya (Chairman)

- A Civil Engineer with 42 years experience
- Responsible for the strategic direction of the company

Satish Parakh (Managing Director)

- A Civil Engineer with 33 years experience
- Associated with the Company since 1982. Responsible for overall management of the company.

Sanjay Londhe (CEO, Projects)

- A Civil Engineer working with the company for 26 years
- Heads Execution of Highway Projects

Ashish Katariya (Managing Director)

- A Civil Engineer and MBA with 15 years experience in the construction industry
- Heads Ashoka Concessions - responsible for execution and management of highway projects.

Paresh Mehta (CFO),

- He is a Chartered Accountant with 28 years of experience. He has been working with the company for last 15 years
- Heads Finance, Taxation and Accounting

Key risks

1) Inability to find a swap for SBI-Macquarie's investment by end-FY18 (Rs13bn liability versus current Rs39bn consolidated debt and 2x D/E).
2) Further delay in the commencement of EPC projects in order book, led by land acquisition hurdles, will risk execution and revenue estimates.
3) A slowdown in economic activity will entail lower-than-estimated traffic growth, impacting the toll collection and resultant free cash flows for BOT projects.
4) An adverse outcome on the ongoing scrutiny in the income tax raid issue.

Valuation and view

ASBL's integrated EPC operations, from inception to completion, combined with cautious bidding strategy has ensured a steady growth along with blended EBITDA margin of 12.5-13.5% over FY10-16. With limited impact of demonetisation on EPC execution coupled with a resolution of land related issues in most of the EPC projects barring , Islampur bypass and Jharkhand-Chaas, we expect a ramp-up in the execution of EPC order book of Rs62bn and estimate 18% EPC revenue CAGR over FY17-19e. Going ahead, as SBIM is looking for an exit; ASBL will invest equity of Rs2.5bn in two annuities, one HAM and city gas distribution projects from internal accruals.

We initiate coverage on ASBL with a Buy and a SOTP-based target price of Rs231, valuing the EPC business at Rs157/share (15xFY19e), BOT projects at Rs71/share and Rs4/share for land.

Table 10: SOTP Valuation Table

	Valuation basis	Multiple	Value (Rs mn)	Value / share (Rs)
EPC construction	P/E	15xFY19e PAT	29,324	157
ASBL's share in BOT projects	NPV	-	13,733	71
Land	P/BV	2x	708	4
Target Price				**231**

Road BOT projects	Stake	Value (Rs mn)	Basis	Value/ share (Rs)	P/BV (x)
Ahmednagar- Aurangabad	100.0	141	NPV @ 14% CoE	0.8	0.4
Katni Byepass	99.9	70	NPV @ 14% CoE	0.4	0.2
Wainganga River	50.0	59	NPV @ 14% CoE	0.3	0.4
KSHIIP	100.0	765	NPV @ 15% CoE	4.1	1.4
Jaora – Nayagaon	10.3	986	NPV @ 14% CoE	5.3	3.1
Others	100.0	185	NPV @ 14% CoE	1.0	1.0
Total ASBL BOT projects value (A)		**3,377**		**12.0**	
Bhandara	51%	772	NPV @ 14% CoE	4.1	0.5
Durg	51%	983	NPV @ 14% CoE	5.3	0.4
Jaora – Nayagaon	37%	3,543	NPV @ 14% CoE	18.9	3.1
Sambalpur- Baragarh	100%	791	NPV @ 14% CoE	4.2	0.2
Belgaum - Dharwad	100%	2,792	NPV @ 14% CoE	14.9	1.3
Dhankuni- Kharagpur	100%	7,766	NPV @ 14% CoE	41.5	1.7
Chennai ORR	50%	1,401	NPV @ 14% CoE	7.5	0.9
Total ACL BOT projects value (B)		**18,048**		**96.0**	**1.1**
ABL's share in ACL @ 61%		11,009		59.0	1.1
Total BOT Value		**13,733**		**71.0**	**1.1**

Source: Company, Systematix Institutional Research

PNC Infratech

27 March, 2017

On cusp of an upturn

INITIATING COVERAGE

Sector: Construction **Rating: Buy**

CMP: Rs114 **Target Price:Rs140**

Stock Info

Sensex/Nifty	29,332/ 9,086
Bloomberg	PNCL IN
Equity shares (mn)	257
52-wk High/Low	Rs135/ 98
Face value	Rs2
M-Cap	Rs29bn/ $0.4bn
3-m Avg volume	$0.8mn

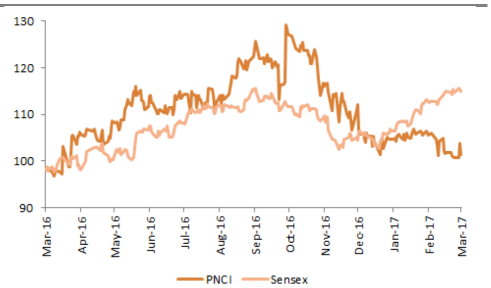
Financial Snapshot (Rs bn)

Y/E March	FY17e	FY18e	FY19e
Sales	18,163	22,594	26,819
EBITDA	2,363	2,981	3,629
PAT	1,962	1,773	1,962
EPS (Rs)	7.6	6.9	7.6
PE (x)	14.9	16.5	14.9
Core P/E (x)	11.7	12.9	11.7
EV/EBITDA (x)	12.1	10.3	8.9
P/BV (x)	1.8	1.7	1.5
RoE (%)	13.3	10.6	10.6
RoCE (%)	11.9	12.6	13.5
Dividend yield (%)	0.4	0.4	0.5
Net gearing (x)	(0.0)	0.1	0.2

Shareholding pattern (%)

	Dec '16	Sept'16	Jun '16
Promoter	56.1	56.1	56.1
–Pledged	-	-	-
FII	10.7	12.4	13.5
DII	18.3	15.6	14.8
Others	14.9	15.9	15.6

Stock Performance (1-year)



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UP based PNC Infratech Ltd (PNCL) involved in construction of roads, highways and airport runways segment has key strengths such as a) conservative bidding b) project selection within its stronghold region c) limited BOT exposure and backward integration into aggregates and equipments. This aided in maintaining a tight leash on costs, resulting in 12-13% EBITDA margin over FY11-17e. Besides the current orderbook of Rs58bn (2.9x FY16 sales) comprises 94% of road projects and is L1 in four roads projects worth Rs60bn resulting in orderbook/FY16 sales of 6.5x. While land acquisition issues delayed execution of four projects worth Rs30bn (51% of orderbook), with 60-70% land in possession now, PNCL expects to procure appointed date shortly. We estimate 22% revenue CAGR over FY17-19e, while factoring in 10% yoy de-growth in FY17 to factor in execution delay. PNCL's operational portfolio of seven BOT assets is fully funded and generates sufficient cash to comfortably service its debt. Led by ramp up in execution and healthy bid pipeline, we estimate 16% PBT CAGR, 18% orderbook CAGR and standalone D/E ratio to be at 0.1x over FY17-19e. We initiate coverage on PNCL with a Buy rating and a SOTP-based target price of Rs140/share, EPC value Rs115/share (15x FY19e EPS) and BOT value of Rs25/share.

Competent UP-based road EPC player with sizeable order book of Rs58bn

PNCL's core expertise in 1) undertaking detailed due diligence of EPC contracts to understand project related challenges, 2) selective bidding for contracts with continuous stretches or in close proximity in and around UP and 3) in-house stone crushing operations, captive mines and own equipments have enabled to deliver projects on/before schedule in roads and airports segment. The outstanding order book at Dec 2016-end is at Rs58bn (2.9x FY16 sales) spread across UP, Uttrakhand and Rajasthan, with top five orders contributing 74%. This includes Rs8.8bn Dausa- Lalsot-Kauthan HAM project, LOA received in Jan'17. PNCL is L1 in four contracts worth Rs60bn (one EPC, three HAM), resulting in current orderbook /sales ratio of 6.5x. Based on current orders and strong NHAI bid pipeline for HAM and EPC projects, we expect execution to pick up in FY18/19e. We thus estimate 22% revenue CAGR over FY17e-19e, while factoring in 10% yoy de-growth in FY17 to factor in delay in execution of four orders worth Rs30bn which were affected by inadequate land acquisition.

Well funded and self-sustaining BOT projects

PNCL diversified into asset ownership, from core EPC operations, in FY11-12 and owns the right to collect toll+annuity for a quality portfolio of seven projects spread across 826km in UP, MP and Delhi – four toll, two annuity and an OMT project. BOT portfolio is operational, fully funded with an equity infusion of Rs5.8bn towards its share. In spite of four of the seven projects commissioning operations in FY16, the toll revenue jumped 46% yoy to Rs3.8bn, led by a strong traffic growth in Gwalior-Bhind BOT and Kanpur-Ayodhya OMT. First annuity on Rae Bareilly-Jaunpur project which commenced operations in March 2016 was received in Dec'16. It expects to receive early completion bonus of Rs380mn by Mar'17. At an average traffic growth of 5-6% in FY18e, we expect the operational portfolio to generate EBITDA of Rs3.7bn in FY18e, making it self-sufficient to service a debt of Rs8.0bn (interest expense of Rs2.6bn). Going forward, we expect minimal risk arising for the parent to service BOT portfolio's debt.

Superior earnings quality, low leverage on balance sheet

PNCL's conservative bidding above NHAI's indicative costs, backward integration for in-house stone crushing, storage facilities for petroleum products, machinery components and cement has provided strong logistical support, thereby saving costs. This has resulted in consistent core EBITDA margin of 12-13% over last 10 years. Contracts in close proximity of UP and adjacent states has enabled higher sweating of own equipment for construction of roads and airport runways, resulting in superior asset turns of 5x-6x over FY11-16 vs 2x-3x for peers. Going ahead, in order to ramp up execution of existing and new orders (a) PNCL expects to incur capex of Rs2.0-2.5bn which in-turn will lower the asset turnover ratio to 3.6x-4.0x over FY17-19e and (b) average working capital cycle to remain at 100 days over FY17-19e (c) equity investments to go up on recent HAM project wins. However, we expect standalone /consol gearing to remain at 0.1x/1.1x over FY18e-19e.

FINANCIALS (STANDALONE)

Profit & Loss Statement

YE: Mar (Rs mn)	FY15	FY16	FY17e	FY18e	FY19e
Net revenues	15,610	20,142	18,163	22,594	26,819
Revenue growth (%)	36.3	29.0	(9.8)	24.4	18.7
- Op. expenses	13,444	17,482	15,800	19,613	23,190
EBIDTA	2,166	2,660	2,363	2,981	3,629
EBITDA margins (%)	13.9	13.2	13.0	13.2	13.5
- Interest expenses	462	332	155	243	350
- Depreciation	364	525	556	665	706
+ Other income	138	202	435	200	250
PBT	1,478	2,004	2,087	2,273	2,823
- Tax	475	386	125	500	861
Effective tax rate (%)	32.1	19.3	6.0	22.0	30.5
Adjusted PAT	1,004	1,618	1,962	1,773	1,962
+/- Extraordinary items	-	(810)	-	-	-
+/- Minority interest	-	-	-	-	-
Reported PAT	1,004	2,427	1,962	1,773	1,962
Adj. FDEPS (Rs/share)	5.0	6.3	7.6	6.9	7.6

Source: Company, Systematix Institutional Research

Balance Sheet

YE: Mar (Rs mn)	FY15	FY16	FY17e	FY18e	FY19e
Share capital	398	513	513	513	513
Reserves & Surplus	6,786	13,110	15,376	17,184	18,803
Networth	7,184	13,623	15,889	17,697	19,316
Minority interest	-	-	-	-	-
Total Debt	3,240	117	750	2,300	3,900
Def. tax liab. (net)	4	(30)	(30)	(30)	(30)
Capital employed	**10,429**	**13,710**	**16,609**	**19,967**	**23,186**
Net Fixed assets	2,174	2,144	3,169	3,004	2,798
Investments	4,235	4,644	5,747	9,497	13,247
- of which liquid	-	-	-	-	-
Net Working capital	3,807	5,952	6,370	6,624	6,319
Cash and bank balance	212	971	1,324	843	823
Capital deployed	**10,429**	**13,710**	**16,609**	**19,967**	**23,186**
Net debt	3,029	(853)	(574)	1,457	3,077
WC (days)	89	108	128	107	86
Book value (Rs/sh)	36	53	62	69	75

Source: Company, Systematix Institutional Research

Cash Flow

YE: Mar (Rs mn)	FY15	FY16	FY17e	FY18e	FY19e
PAT	1,004	1,618	1,962	1,773	1,962
+ Non cash items	340	491	556	665	706
Cash profit	1,344	2,109	2,518	2,438	2,668
- Incr/(Decr) in WC	1,052	2,144	418	254	(305)
Operating cash flow	292	(36)	2,100	2,184	2,973
- Capex	994	494	1,581	500	500
Free cash flow	(702)	(530)	519	1,684	2,473
- Dividend	93	161	154	154	185
+ Equity raised	-	4,057	-	-	-
+ Debt raised	758	(3,123)	633	1,550	1,600
- Investments	726	408	1,103	3,750	3,750
- Misc. items	25	(924)	(458)	(189)	158
Net cash flow	(788)	759	353	(481)	(20)
+ Opening cash	999	212	971	1,324	843
Closing cash	212	971	1,324	843	823

Source: Company, Systematix Institutional Research

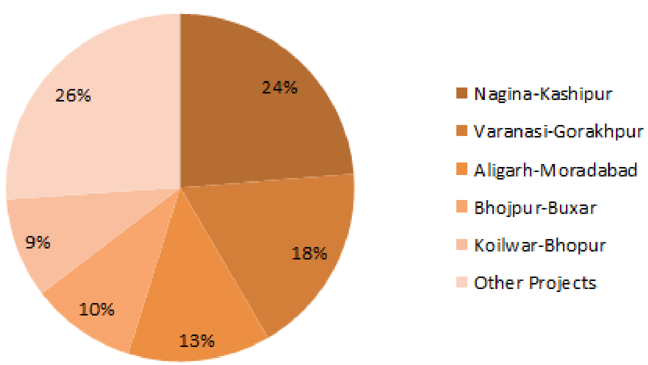
Ratios

YE: Mar	FY15	FY16	FY17e	FY18e	FY19e
P/E (x)	22.6	18.1	14.9	16.5	14.9
P/B (x)	3.2	2.1	1.8	1.7	1.5
EV/EBITDA (x)	11.9	10.7	12.1	10.3	8.9
RoE (%)	14.9	15.6	13.3	10.6	10.6
RoCE (%)	18.8	17.7	11.9	12.6	13.5
Fixed Asset turnover (x)	4.7	5.0	3.6	3.7	4.0
Dividend yield (%)	0.3	0.4	0.4	0.4	0.5
Dividend payout (%)	7.7	5.3	6.5	7.2	7.8
Interest exp./Sales	3.0	1.6	0.9	1.1	1.3
Debtors (days)	86	68	80	85	90
Revenue growth (%)	36.3	29.0	(9.8)	24.4	18.7
PAT growth (%)	49.9	61.2	21.3	(9.6)	10.7
EBITDA growth (%)	54.4	22.8	(11.1)	26.1	21.7
EPS growth (%)	49.9	87.7	(19.2)	(9.6)	10.7
Net gearing (%)	0.2	0.4	(0.1)	(0.0)	0.1

Source: Company, Systematix Institutional Research

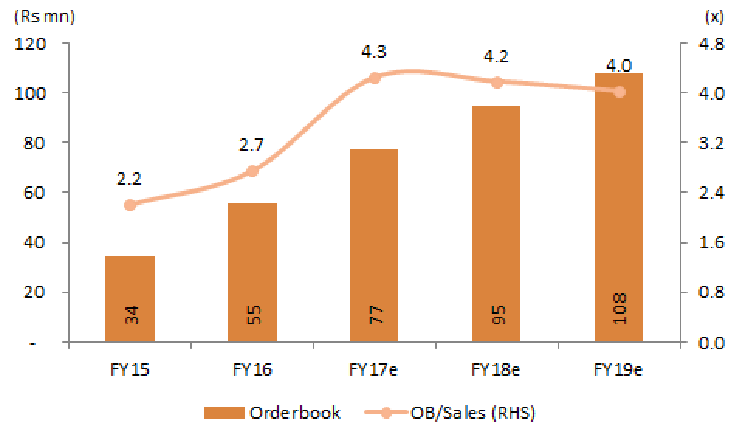
Charting the story

Chart 1: Top 5 roads projects contribute 74% of orderbook



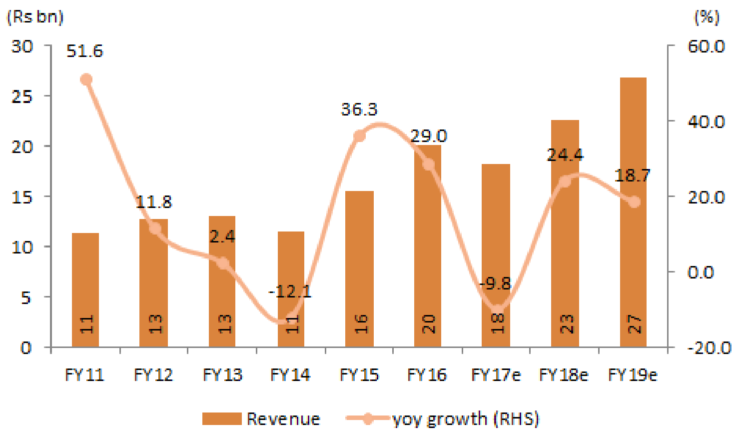
Source: Company

Chart 2: Healthy Order book to bill ratio provides revenue visibility



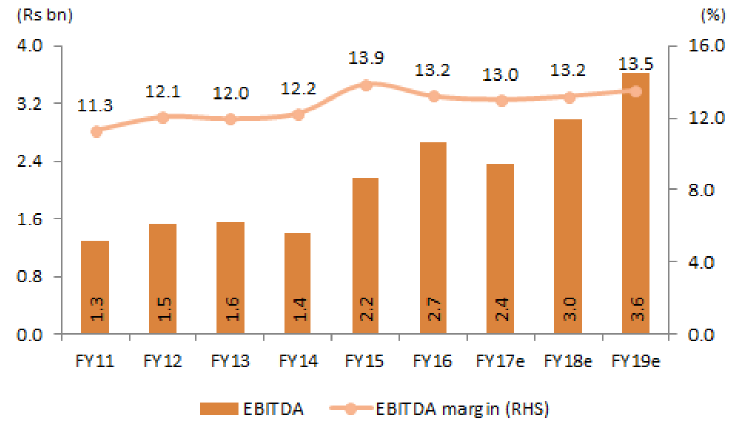
Source: Company

Chart 3: Revenue to grow at 21% CAGR over FY17-19e



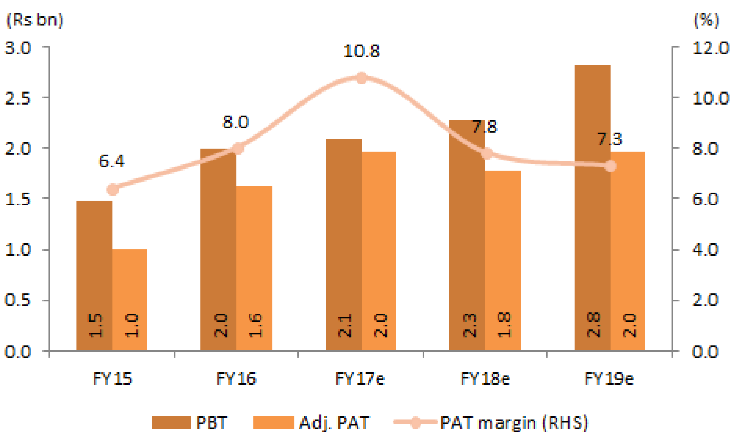
Source: Company, Systematix Institutional Research

Chart 4: EBITDA margin to stabilize at 13.2%



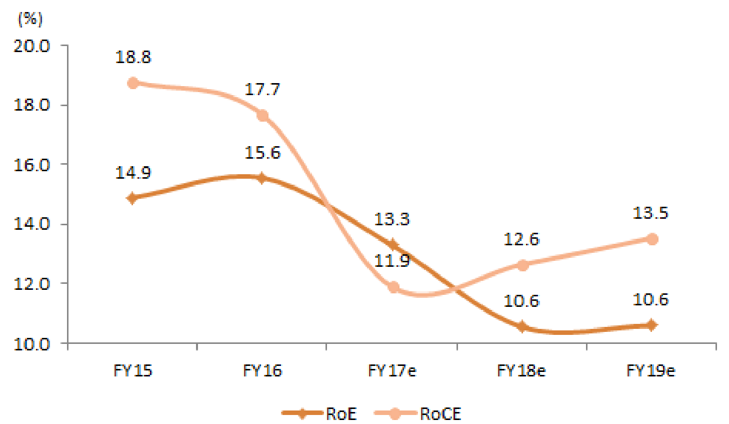
Source: Company, Systematix Institutional Research

Chart 5: OPM expansion, savings in interest to boost PAT margin…



Source: Company, Systematix Institutional Research

Chart 6: …and stable D/E ratio to improve RoCE



Source: Company, Systematix Institutional Research

Competent UP-based road EPC player, with sizeable order book of Rs58bn

Incorporated by Pradeep Kumar Jain in 1999, PNCL is an UP-based EPC player, with a proven track record in executing EPC projects in roads, highways and airport runways (its key focus segments) in a time bound manner. Over the years, the company has developed credible relationships with public sector clients such as NHAI, MPRDC, UPSHA, UPEIDA and PWD for roads and highways segment and with AAI, MES for airport runways. In addition, PNCL has developed an industrial zone at Narela, New Delhi and is involved in the construction of power transmission lines and railway track laying for the dedicated freight corridor. Since incorporation, PNCL has executed 59 EPC projects, primarily in UP and states such as MP, Rajasthan, Punjab and Haryana. The projects are bid after a detailed due diligence of contracts in advance to note the related challenges.

Table 1: Road projects executed in the past

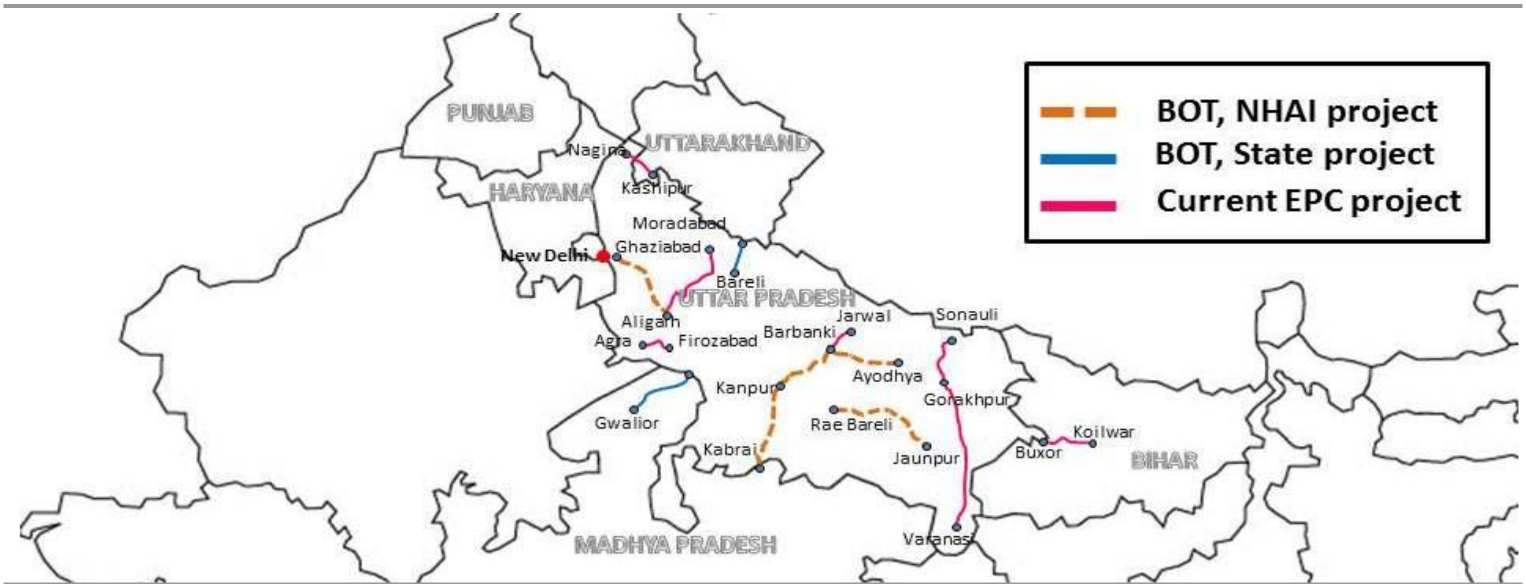
Etahwah bypass	NH2 , NHAI	UP	May 2008
Agra- Gwalior	NH3, NHAI	UP	Jan 2005
Sagar Beena Road	MPRSD	MP	Apr 2007
Various state highways in MP	MPSRS – II	MP	Jan 2011
Garhmukhteshwar to Moradabad	NHAI	UP	Oct 2012
Porsa-Mehgaon-Mau-Seonda	State highway, World Bank funded	UP	Jun 2008

Source: Company

Strong foothold within its region

PNCL follows a cluster-based approach for projects. In the past, it had selectively bid for projects in a continuous stretch pattern or in close proximity to each other to maintain a tight leash on execution.

Chart 7: Cluster based approach keeps costs under check



Source: Company

Experience in construction of airport runways

PNCL has developed an expertise in the construction of airport runway projects. The company had completed EPC of 19 airport runway projects spread across UP, West Bengal, Karnataka, Chattisgarh, Tamil Nadu, Uttranchal, MP, Assam and Maharashtra. The scope of work includes construction, extension, strengthening, resurfacing, widening, repairs, upgradation and maintenance and other activities in respect of airstrips and runways, as well as related infrastructure such as taxi tracks and aprons.

Table 2: Key projects completed in the past include

Particulars	State	Client	Completion date
Strengthening of main runway and other works at NSCBI Airport, Kolkata	West Bengal	NA	May-05
Upgradation of airstrips for operation of Boeing 737 type aircraft at Saifai Etawah Airport	Uttar Pradesh	NA	Feb-07
Resurfacing of runway, extension of existing runway and allied works AFS Jorhat	Assam	MES	Apr-14
Extension and strengthening of runway and construction of the new apron, isolation bay and associated works at Devi Ahilyabai Airport, Indore	Madhya Pradesh	AAI	Jun-09
Repairs, resurfacing, re-grading of shoulders of existing runway and area drainage works	Air Force Station Yelahanka, Bangalore	MES	Jan-05
Resurfacing of hard standing at Mehra Chowk at 402 Air Force Station Chakeri, Kanpur	402 Air Force Station Chakeri, Kanpur	MES	Mar-04

Source: Company

Backward integration aids timely execution

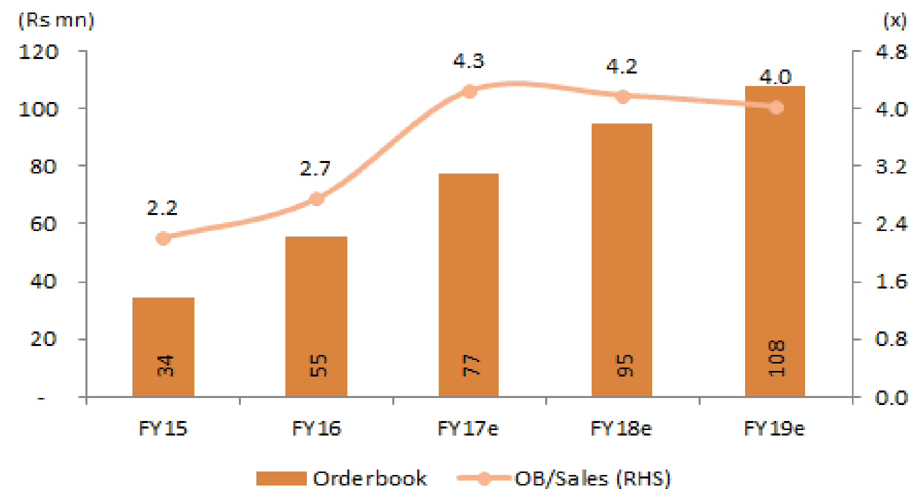
PNCL possesses captive mines for aggregates, carries out in-house stone crushing, which has enabled to meet 80% of stone aggregates' requirement from within for construction of roads and airport runway segment. In addition, ownership of state-of-the-art equipments such as bituminous hot mix plants, concrete batch plants among others ensures continuous availability of critical resources and facilitates savings in cost and timely/early completion. The company in 2003 received a bonus from NHAI for early completion of four-laning the Agra-Gwalior road project of NH3 in UP and commenced toll collection more than three months in advance, with an early completion of the Gwalior-Bhind BOT road project.

A dedicated procurement department, strong resource of 3,804 employees as on Mar 31, 2016, a logistics services team and storage facilities for petroleum products, machinery components and cement ensure uninterrupted work at sites.

Healthy EPC order book at Rs58bn (2.9x FY16 sales)

PNCL witnessed a steady increase in order book, 9% CAGR over FY12-16, to Rs55bn. Within road sector, the order book comprised of both third party EPC and captive BOT projects. At a time of high competitive intensity, the company refrained from bidding aggressively for EPC contracts to shore up the order book. Instead, it strategically bid for BOT projects in and around UP, and the EPC portion of these comprised a large part of its order book in FY13-15. The average order book/bill ratio during FY12-16 has been at 2.7x, thus providing steady revenue visibility. PNCL won seven EPC contracts – six road and an airport runway projects worth Rs39.7bn in FY16. Including the Dausa-Lalsot-Kauthan HAM project of Rs8.8bn (LOA received in Jan'17), YTDFY17 order inflows is at Rs13.7bn and the outstanding order book is at Rs58bn (2.9x FY16 sales). 94% of the order book is from roads segment and the top five orders comprise 75% of the order book. PNCL is also L1 in four projects worth Rs60bn – one EPC and three HAM projects. Considering these, the current orderbook/FY16 sales is at 6.5x.

Chart 8: Rising book/bill ratio provides strong revenue visibility



Source: Company, Systematix Institutional Research

Table 3: Key projects in order book

EPC projects	km	Rs mn	Lane, section	State	Client	Est. appointed date
Nagina-Kashipur	102	11,560	4 laning, NH-74	Uttarakhand/ UP	NHAI	End of Mar'17/early Apr'17
Varanasi- Ghorakhpur	76	8,690	4 laning,NH-29	Uttar Pradesh	NHAI	April'17
Aligarh- Mordabad	146	6,450	2 laning, NH-93	Uttar Pradesh	NHAI	Work in progress
Bhojpur-Buxar	47.9	4,770	4 laning, NH-84	Bihar	NHAI	April'17
Koliwar-Bhojpur	43.9		4 laning, NH-30&84	Bihar	NHAI	April'17
Other projects	-	12,690	-	-	-	Ongoing
Total order book		**48,700**				

Source: Company, Systematix Institutional Research

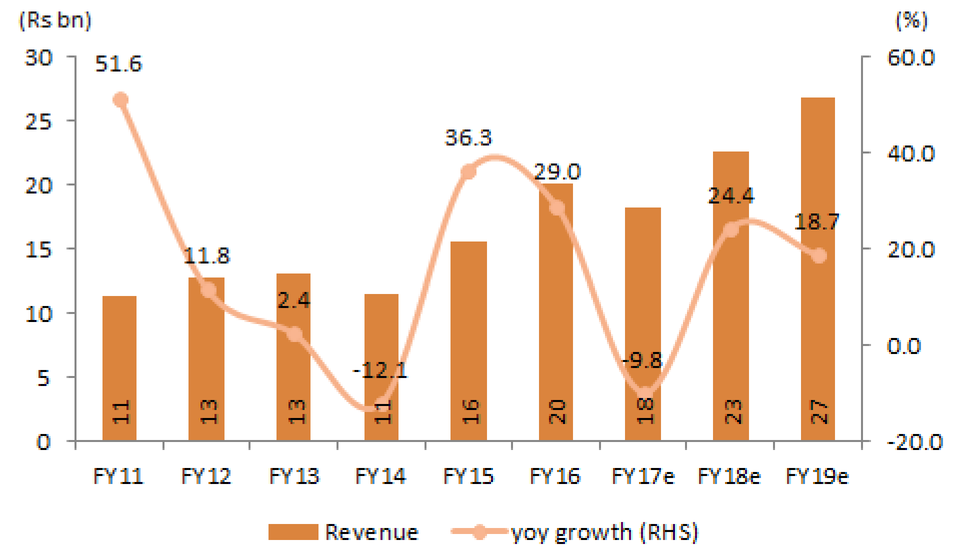
Table 4: Recently won projects not included in order book

Project	Type	Rs mn	State	Client	Status
4/2 laning Dausa-Lalsot-Kauthun	HAM	8,810	Rajasthan	NHAI	FC in progress, expects appointed date in 1st week of Apr'17
L1					
Lucknow - Balia	EPC	18,650	UP	UPEIDA	Yet to receive LOA, expects after UP election results
Chitradurga- Davanagere	HAM	14,340	Karnataka	NHAI	Yet to receive LOA, difference between L1 and L2 (Sadbhav) is 3%
Jhansi-Khajurao package 1	HAM	14,100	UP & MP	NHAI	Five firms participated , bids open on 23rd March'17
Jhansi-Khajurao package 1	HAM	13,100	UP & MP	NHAI	Six firms participated , bids open on 23rd March'17

Source: Company, Systematix Institutional Research

While NHAI bidding pipeline remains robust, PNCL has bid for two projects in UP and one project in Karnataka on EPC / HAM basis. Another five EPC projects with average ticket size of Rs4-5bn each has been bid for in Maharashtra. PNCL led by its established execution skills can capitalise on these opportunities and expects to win orders worth Rs40-50bn in FY18e. We estimate 18% CAGR in order book to Rs105.8bn over FY17e-19e.

Chart 9: Standalone EPC revenue expected to grow at 22% CAGR over FY17-19e



Source: Company, Systematix Institutional Research

Heavier than normal monsoon and temporary effect of unavailability of labor / raw materials led by demonetization impacted execution of ongoing orders in the orderbook leading to 6%/11% yoy decline in 9MFY17/3QFY17 revenue to Rs13.4/Rs4.6bn.

Besides, inspite of mobilizing the materials and equipments at site of four new projects namely Varanasi- Gorakhpur, Nagina- Kashipur, Bhojpur-Buxar and Koliwar – Bhojpur worth Rs30bn (61% of orderbook), availability of only ~50-60% of total required land has led to delay in procuring the appointed date. Thus, we expect FY17 revenue to decline by 9.8% yoy to Rs18bn. With 60-70% land in possession now, PNCL has indicated to take the appointed date for four projects by April'17. Since the sites are mobilized with material, labour and equipments, we expect execution to ramp up from FY18e and estimate 22% revenue CAGR over FY17-19e.

Well funded and self-sustaining BOT assets

PNCL diversified into asset ownership, from core EPC operations, in FY11-12 and owns the right-to-collect toll and annuity for a quality portfolio of seven projects spread across 826km. While state-wise BOT projects are restricted to Uttar Pradesh (83%) and Madhya Pradesh (13%), the clientele (awarding agency) is well diversified across NHAI, UPSHA, MPRDC and DSIIC.

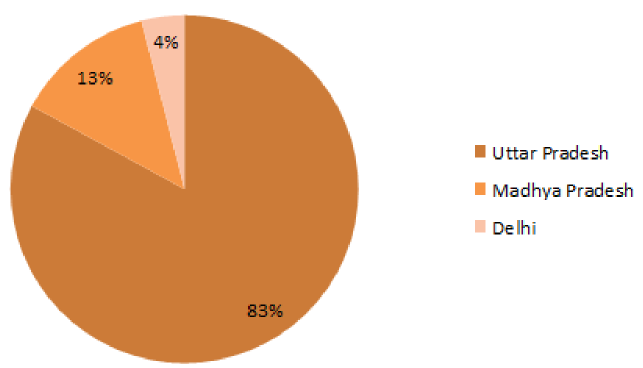
Table 5: Fully operational BOT portfolio

Particulars	Type	Client	PNC stake (%)	State	Project length (km)	lane	Status	CoD
Gwalior - Bhind	Toll	MPRDC	100%	Madhya Pradesh	108	2	Operational	Jan'13
Kanpur- Kabrai	Toll	NHAI	100%	Uttar Pradesh	123	2	Operational	May'15
Bareilly - Almora	Toll	UPSHA	100%	Uttar Pradesh	54	4	Operational	Oct'15
Narela Industrial Estate	Annuity	DSIIC	100%	Delhi	33	NA	Operational	Oct'13
Rae Bareily Jaunpur	Annuity	NHAI	100%	Uttar Pradesh	166.4	2	Operational	Feb'16
Kanpur Ayodhya	OMT	NHAI	100%	Uttar Pradesh	217	4	Operational	Aug'13
Ghaziabid - Aligarh	Toll	NHAI	35% (65%-SREI, Galfar)	Uttar Pradesh	125	4	Operational	Jun'15
Total					**826**			

Source: Company, Systematix Institutional Research

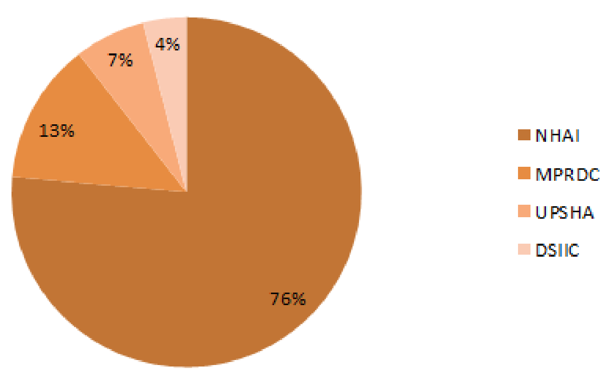
Classification of BOT assets

Chart 10: State-wise



Source: Company, Systematix Institutional Research

Chart 11: Client-wise



Source: Company, Systematix Institutional Research

PNCL is on schedule to achieve financial closure of the Dausa-Lalsot-Kauthun (4/2 laning with paved shoulders) by end of March'17 and expects to procure the appointed date in 1st week of April'17.

Well funded BOT projects

BOT portfolio is fully funded with an equity infusion of Rs4.6bn by PNCL towards its share. Rae Bareilly-Jaunpur commenced operations in March 2016, three months ahead of schedule, received 1st annuity in December 2016 and expects to receive early completion bonus of Rs.380mn in March'17.

Table 6: Completely funded BOT projects portfolio

Particulars	Type	TPC (Rs mn)	Equity (Rs mn)	Debt (Rs mn)	Grant (Rs mn)	PNC's stake (%)	PNC's Equity (Rs mn)	Concession Period (years)
Gwalior - Bhind	BOT	3,400	783	2,350	267	100%	783	14
Kanpur- Kabrai	BOT	4,590	675	2,680	1,230	100%	675	12
Bareilly - Almora	BOT	6,050	746	4,600	700	100%	746	25
Narela Industrial Estate	Annuity	1,750	350	1,400	-	100%	350	15
Rae Bareily -Jaunpur	Annuity	8,370	1,396	6,980	-	100%	1,396	17
Kanpur - Ayodhya	OMT	NA	0.1	NA	-	100%	0	9
Ghaziabid - Aligarh	BOT	20,190	1,940	15,140	3,110	35%	679*/1,181	24
Total		**44,350**	**5,890**	**33,150**	**5,310**		**5,811**	

Source: Company, Systematix Institutional Research ** PNC Share, # Warrant*

No funds required by parent on predictable cash flow generation

BOT projects are located in highly industrialised traffic corridor that cut across four districts and key cities of Agra and Lucknow. In spite of four of the seven projects commissioning operations in FY16, the toll revenue jumped 46% yoy to Rs3.8bn, led by a strong traffic growth in Gwalior-Bhind BOT and Kanpur-Ayodhya OMT. At an average traffic growth of 5-6% in FY18e, we estimate the operational portfolio to generate EBITDA of Rs3.7bn, making it self-sufficient to service a peak debt of Rs8.0bn (interest expense of Rs2.6bn in FY18e). Going forward, we expect minimal risk arising for the parent company to service the debt for BOT portfolio.

Table 7: Estimated revenue from BOT projects

Revenue (Rs mn)	CoD	FY15	FY16	FY17e	FY18e	FY19e	FY20e
Gwalior – Bhind	Toll	374	472	555	618	688	765
Kanpur- Kabrai	Toll	25	570	748	872	970	1080
Bareilly – Almora	Toll	87	165	384	423	467	514
Kanpur Ayodhya	OMT	1,972	2,383	2,627	2,897	3,193	3,521
Ghaziabid - Aligarh *	Toll	-	1,010	1,296	1,429	1,575	1,736
Total		**2,458**	**4,600**	**5,610**	**6,238**	**6,893**	**7,617**

Source: Company, Systematix Institutional Research; **assuming full CoD in FY17*

Table 8: Strong free cash flow from BOT assets prevents fund infusion from parent

FCFE (Rs mn)	PNC' stake	FY16	FY17e	FY18e	FY19e	FY20e
Gwalior – Bhind	100%	119	(83)	(6)	57	67
Kanpur- Kabrai	100%	(113)	41	96	271	384
Bareilly – Almora	100%	(60)	(553)	(502)	(351)	(254)
Kanpur Ayodhya	100%	4	817	934	1,042	1,141
Ghaziabad - Aligarh *	35%	(243)	(382)	(343)	(243)	(112)
Total		**(319)**	**(140)**	**178**	**776**	**1,227**

Source: Company, Systematix Institutional Research

Superior earnings quality, low leverage on balance sheet

PNCL has historically placed conservative bids for contracts above NHAI's indicative cost. Backward integration for in-house stone crushing, investment in storage facilities for petroleum products, machinery components and cement has provided strong logistical support, thereby saving costs. The company maintains a centralised workshop at Agra to keep part of the inventory of major equipments, which also has in-house facilities for repair and refurbishing. The centralised workshop enables to deploy equipments at a short notice in the event of contingencies at any of the project sites. It owns fleet of 1,726 equipments.

Table 9: Some of the key in-house equipments as on 31st March 2016

Type	No
Crusher plants	14
Hot Mix Plants	19
Soil compactors	65
Concrete mixers	41
Cranes	19
Excavators	35
Backhoe Loaders	56
Paver Finisher	41
Heavy duty vehicles	537

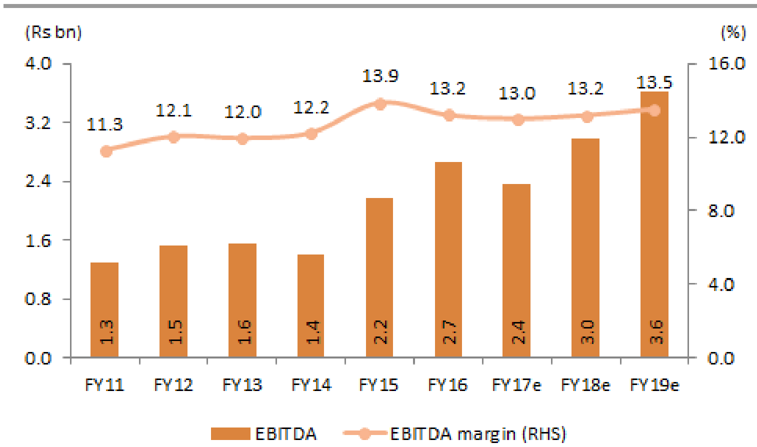
Source: Company

Besides, the core EBIDTA margins have been consistent in range if 12-13% over the last five to six years, which is superior among peers such as SADE. In FY15, EBITDA margin touched 13.9% on execution of captive BOT projects where margins are better due to added control on project costs. Close proximity of contracts in UP and adjacent states has enabled higher sweating of own equipment for construction of roads and airport runways, resulting in superior asset turns of 5x-6x over FY11-16 vs 2x-3x for peers.

PNCL expects EPC operating margins in the newly won HAM project: Chitradurga-Davanagere to be at 13-13.5%. Based on the current orderbook, we expect standalone OPM at 13.2% and PBT to grow at 14% CAGR over FY17e-19e.

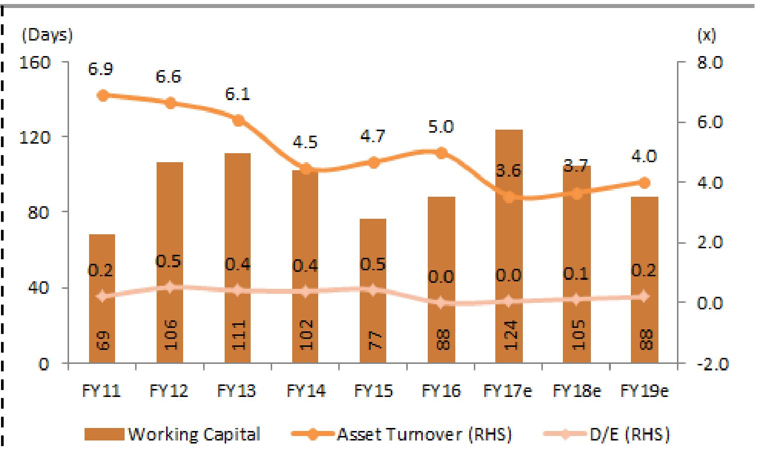
Going ahead, in order to ramp up execution of existing orderbook (a) PNCL expects to incur capex of Rs2.0-2.5bn which in-turn will moderate the asset turnover ratio to 3.6x-4.0x over FY17-19e and (b) average working capital cycle will be at 100 days. We expect standalone/consol gearing to remain at 0.1x/1.1x over FY18e-19e.

Chart 12: FY18e/19e OPM to trend higher to 13.2%



Source: Company, Systematix Institutional Research

Chart 13: Average working capital to be at 100 days, 0.1x net D/E



Source: Company, Systematix Institutional Research

Key management team

Pradeep Kumar Jain (Chairman & Managing Director)

- Over 37 years of experience in the construction, infrastructure sector and allied areas
- Responsible for overall administration and supervision of projects and liaison with agencies

Naveen Kumar Jain (Whole time Director)

- Over 28 years of experience in industries such as construction, cold storage, transportation, machineries and transport organization
- Responsible for supervision of administration, human resources, legal and logistics-related functions

Chakresh Kumar Jain (Managing Director)

- Over 27 years of experience in development of infrastructure sector, such as construction of highways, airports, rail over-bridges among others
- Responsible for overall finance, project management and administration

Yogesh Kumar Jain (Managing Director)

- Over 22 years of experience in planning, execution, supervision of work starting from pre-qualification and tendering up to completion and handing over of sites
- Responsible for technical supervision of projects up to completion stage of such projects

Chhotu Ram Sharma (Independent Director),

Subhash Chander Kalia (Independent Director)

Ashok Kumar Gupta (Independent Director)

Rakesh Kumar Gupta (Independent Director)

Deepika Mittal (Independent Director)

Key risks

1) Delay in finalisation of projects from NHAI/ state road development corporations can slow down the conversion of bid pipeline into order inflows.
2) Land acquisition hurdles.
3) Any impediment in the execution of current order book due to clients' liquidity crunch can hamper the revenue growth, stretch working capital cycle and increase leverage.

Valuation and view

PNCL has advanced from an UP state focused road projects company executing state EPC projects to NHAI-led EPC player with a presence across UP, Bihar and Punjab. NHAI orders now constitute more than 90% of the order book of Rs58bn. With the government's thrust on road development, bid pipeline from NHAI/MoRTH and NHIDCL remains strong for PNCL. Fund raising through an IPO in May 2015 aided in a debt-free balance sheet in CY14 and has strengthened its net worth to bid for large ticket size projects. Execution is yet to commence for four projects won in FY16, which coupled with a steady OPM of 13.2%, net gearing of 0.1, in our view, can drive 21%/14% revenue/PBT CAGR over FY17-19e.

We initiate coverage with a **Buy** rating. We value the EPC business at Rs110/share, 15x FY19e earnings and PNCL's share of BOT portfolio at Rs25/share (FCFE with CoE of 14%), and arrive at a SOTP-based target price of Rs135/share.

Table 10: SOTP Valuation table

	PNC's share	Valuation basis	Value (Rs mn)	PNC's share (Rs mn)	Value (Rs/share)	P/BV
(A)Standalone EPC		**15x FY19e earnings**	**28,302**	**28,302**	**115**	**-**
(B) BOT Assets						
a) Toll						
Gwalior-Bhind	100%	FCFE at CoE of 14%	1,106	1,106	4.3	1.4
Kanpur –Kabrai	100%	FCFE at CoE of 14%	1,601	1,601	6.2	2.4
Bareilly – Almora	100%	FCFE at CoE of 14%	851	851	3.3	1.1
Ghaziabad - Aligarh	35%	FCFE at CoE of 14%	1,929	675	2.6	1.0
b) Annuity						
Rae-Bareilly Jaunpur	100%	FCFE at CoE of 14%	823	823	3.2	0.6
Narela Industrial	100%	FCFE at CoE of 14%	519	519	2.0	1.5
c) OMT						
Kanpur Ayodhya	100%	FCFE at CoE of 14%	799	799	3.1	-
Total (B)					**25**	1.4
SOTP value					**140**	
CMP					114	
Upside (%)					22%	

Source: Company, Systematix Institutional Research

Dilip Buildcon

27 March, 2017

Excellence on the road

INITIATING COVERAGE

Sector: Construction	**Rating: Accumulate**
CMP: Rs349	**Target Price: Rs411**

Stock Info

Sensex/Nifty	29,332/ 9,086
Bloomberg	DBL IN
Equity shares (mn)	118
52-wk High/Low	Rs365/ 179
Face value	Rs10
M-Cap	Rs48bn/ $0.7bn
3-m Avg volume	$1.0mn

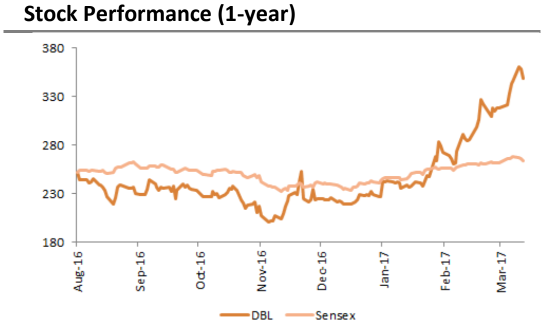
Financial Snapshot (Rs bn)

Y/E March	FY17e	FY18e	FY19e
Sales	49,432	56,847	65,659
EBITDA	9,412	10,824	12,454
PAT	2,706	2,822	3,655
EPS (Rs)	19.8	20.6	26.7
PE (x)	17.6	16.9	13.1
EV/EBITDA (x)	7.5	6.6	5.8
P/BV (x)	2.7	2.3	2.0
RoE (%)	18.8	14.7	16.3
RoCE (%)	18.3	18.8	20.4
Dividend yield (%)	0.1	0.1	0.2
Net gearing (x)	1.3	1.2	1.0

Shareholding pattern (%)

	Dec '16	Sept'16	Aug '16
Promoter	75.6	75.6	75.6
–Pledged	-	-	-
FII	14.8	12.3	6.7
DII	2.9	2.9	3.0
Others	6.7	9.2	14.7

Stock Performance (1-year)



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Madhya Pradesh-based Dilip Buildcon (DBL), one of the largest road EPC contractors, has executed 47 road projects across 5,612 lane kms and operates in 10+ states outside MP. Government orders comprise 96% of the order book of Rs131bn, compared to 21% in FY12. It integrated business model with large own equipment base of 8,500, in-house execution, central procurement and stringent project monitoring by skilled employee base helps to complete projects ahead of schedule thus saving fixed cost and earn bonus.DBL has thus reported industry leading EBIDTA margins of 19%-21%. On improvement in asset turnover to 2.6x (2.2x) and gearing to 1.1x (1.4x) in FY19e, we estimate 15%/16% CAGR in revenue/PAT over FY17-19e. We initiate coverage, with an Accumulate rating and SOTP-based target price of Rs411 (EPC value – Rs374, 14x FY19e EPS and Rs36 for BOT projects).

Fully integrated EPC operations with proven track record: Primarily a road contractor for private developers (79% revenue in FY12), DBL's rising pre-qualification has made it eligible to solely bid for large ticket size (Rs10bn+) government road projects. While government contracts contributed 88% to FY16 revenue, 84% of EPC revenue came from executing contracts for third parties. Since FY14, DBL forayed into irrigation, urban development and recently in mining EPC in a big way. Large in-house fleet of 8,500 construction equipment and vehicles from top suppliers and centralised procurement for all raw materials help it to make equipments/materials available on time, save leasing costs and reduce breakdown time and seamlessly execute projects. A strong workforce of 24,000 employees enables to form dedicated teams for each project jobs and daily monitoring of material/equipment movement and execution versus target set. Strong control over each task has improved efficiency and profitability, by executing most projects ahead of schedule.

Robust and diversified EPC order book, portfolio of 21 BOT projects provides visibility: Predominantly from an MP-centred order book, expansion of operations in 10+ states led 51% CAGR in order book over FY11-16. Dec-16-end order book is at Rs131bn (3.2x FY16 revenue), comprising of 89% orders from roads segment (75% EPC and 14% own BOT), 8% from mining segment (overburden removal), 2% each from urban development and irrigation. Government contracts are at 96%, while 85% of the order book is from states outside MP. DBL has submitted bids worth Rs12.4bn for government road projects where an outcome is expected by April 2017. With management's focus on execution of current order book, we expect 15% standalone revenue CAGR over FY17e-19e. Management has guided revenue of Rs50bn/Rs60bn/Rs70bn for FY17/18/19. DBL's portfolio consists of 21 BOT assets, 12 operational (invested Rs3.8bn, FY16 revenue Rs2.8bn) and 9 under-construction (three recently-won HAM projects).Over FY17-19 equity investment of Rs7bn is required in nine assets. DBL has signed a MoU with Shrem Infra for divesting 49% stake during construction in recently won Tuljapur-Ausa HAM project (TPC - Rs9.1bn).

Improvement in profitability and balance sheet on cards: DBL has consistently reported standalone EBITDA margins of 19%-21% during FY11-YTDFY17, highest compared to industry range of 10-15% on purchase of own equipment, in-house execution, centralized procurement and receipt of Rs2.2bn early completion bonus. During FY13-17e, DBL incurred massive capex of Rs18bn (Rs3.6bn in FY17e to purchase mining and road equipments) leading to a drop in asset turnover from 3.1x in FY13 to 2.2x in FY16. Besides, increase in operational sites to 50+ in FY16(23 in FY12) pushed up inventory to 141 days and debtor rose to 108 days on legacy private clients. FCF thus turned negative in-turn raising gearing to 2.3x. Recent IPO proceeds combined with peaking out of capex (upto Rs.2.0-3.0bn in FY18-19e), ongoing recovery from private clients (o/s Rs3.2bn) and likely reduction in sites to below 22 will improve gearing to 1.1x by FY19e. On lower interest expenses, while we expect 38% PBT CAGR over FY17-19e, PAT CAGR is estimated to be at 16%, due to phasing out of section 80 IA tax benefits in FY18/19.

Investors are advised to refer through disclosures made at the end of the research report.

FINANCIALS (STANDALONE)

Profit & Loss Statement

YE: Mar (Rs mn)	FY15	FY16	FY17e	FY18e	FY19e
Net revenues	26,241	40,853	49,432	56,847	65,659
Revenue growth (%)	13.3	55.7	21.0	15.0	15.5
- Op. expenses	20,586	32,861	40,020	46,024	53,205
EBIDTA	5,655	7,992	9,412	10,824	12,454
EBITDA margins (%)	21.6	19.6	19.0	19.0	19.0
- Interest expenses	2,587	3,805	4,402	4,385	4,433
- Depreciation	1,179	1,835	2,243	2,519	2,678
+ Other income	60	154	112	112	112
PBT	1,949	2,507	2,879	4,032	5,456
- Tax	491	308	173	1,209	1,800
Effective tax rate (%)	25.2	12.3	6.0	30.0	33.0
Adjusted PAT	1,458	2,199	2,706	2,822	3,655
+/- Extraordinary items	-	-	-	-	-
+/- Minority interest	-	-	-	-	-
+ PL of Associate Co.	-	-	-	-	-
Reported PAT	1,458	2,199	2,706	2,822	3,655
Adj. FDEPS (Rs/share)	24.6	18.8	19.8	20.6	26.7

Source: Company, Systematix Institutional Research

Balance Sheet

YE: Mar (Rs mn)	FY15	FY16	FY17e	FY18e	FY19e
Share capital	1,171	1,171	1,368	1,368	1,368
Reserves & Surplus	7,557	9,754	16,509	19,275	22,857
Networth	8,728	10,925	17,877	20,643	24,225
Minority interest	-	-	-	-	-
Total Debt	21,870	25,138	24,500	25,250	25,750
Def. tax liab. (net)	707	937	937	937	937
Capital employed	**31,305**	**37,000**	**43,313**	**46,829**	**50,911**
Net Fixed assets	11,890	14,204	15,579	14,559	13,381
Investments	2,789	2,898	5,648	8,195	10,245
- of which liquid	-	-	-	-	-
Net Working capital	14,285	18,839	20,586	22,895	25,904
Cash and bank balance	2,342	1,059	1,501	1,180	1,381
Capital deployed	**31,307**	**37,001**	**43,313**	**46,829**	**50,911**
Net debt	19,528	24,079	22,999	24,070	24,369
WC (days)	199	168	152	147	144
Book value (Rs/sh)	75	93	131	151	177

Source: Company, Systematix Institutional Research

Cash Flow

YE: Mar (Rs mn)	FY15	FY16	FY17e	FY18e	FY19e
PAT	1,458	2,199	2,706	2,822	3,655
+ Non cash items	1,619	2,064	2,243	2,519	2,678
Cash profit	3,077	4,263	4,949	5,341	6,333
- Incr/(Decr) in WC	5,687	4,554	1,746	2,309	3,009
Operating cash flow	(2,610)	(291)	3,203	3,032	3,324
- Capex	6,654	4,098	3,600	1,500	1,500
Free cash flow	(9,265)	(4,389)	(397)	1,532	1,824
- Dividend	7	4	54	56	73
+ Equity raised	(6)	2	4,300	-	-
+ Debt raised	11,933	3,269	(638)	750	500
+ MI	-	-	-	-	-
- Investments	959	109	2,750	2,547	2,050
- Misc. items	23	52	18	-	-
Net cash flow	1,673	(1,283)	442	(321)	201
+ Opening cash	669	2,342	1,059	1,501	1,180
Closing cash	2,342	1,059	1,501	1,180	1,381

Source: Company, Systematix Institutional Research

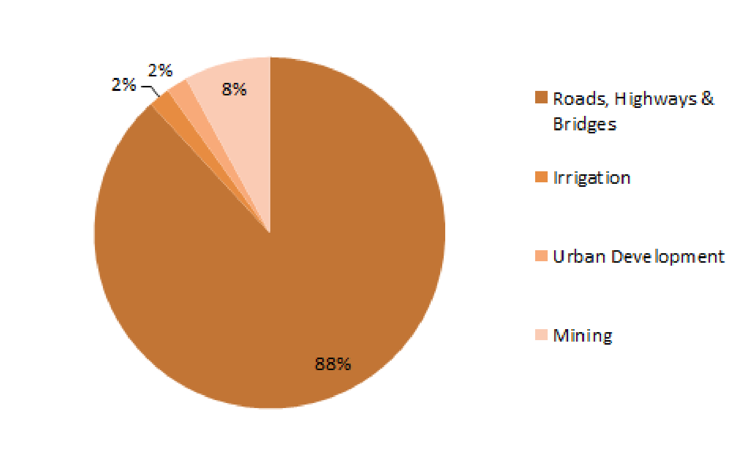
Ratios

YE: Mar	FY15	FY16	FY17e	FY18e	FY19e
P/E (x)	14.2	18.6	17.6	16.9	13.1
Core P/E (X)	12.7	16.7	15.8	15.1	11.7
P/B (x)	4.7	3.7	2.7	2.3	2.0
EV/EBITDA (x)	10.7	8.1	7.5	6.6	5.8
RoE (%)	18.2	22.4	18.8	14.7	16.3
RoCE (%)	18.7	18.5	18.3	18.8	20.4
Fixed Asset turnover (x)	2.2	2.4	2.3	2.4	2.6
Dividend yield (%)	0.0	0.0	0.1	0.1	0.2
Dividend payout (%)	0.5	0.2	2.0	2.0	2.0
Interest exp./Sales	9.9	9.3	8.9	7.7	6.8
Debtors (days)	176	108	98	95	92
Revenue growth (%)	13	56	21	15	16
PAT growth (%)	(25)	51	23	4	30
EBITDA growth (%)	20	41	18	15	15
EPS growth (%)	(55)	(24)	5	4	30
Net gearing (%)	2.2	2.2	1.3	1.2	1.0

Source: Company, Systematix Institutional Research

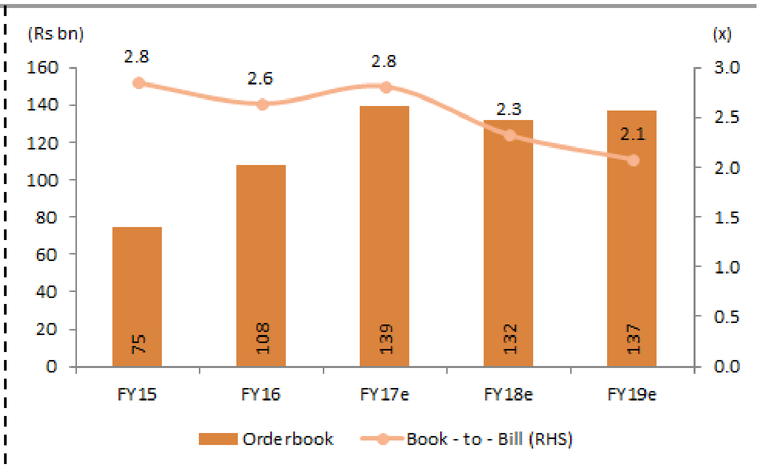
Charting the story

Chart 1: Order book – Rs131bn as of 9MFY17; roads dominate



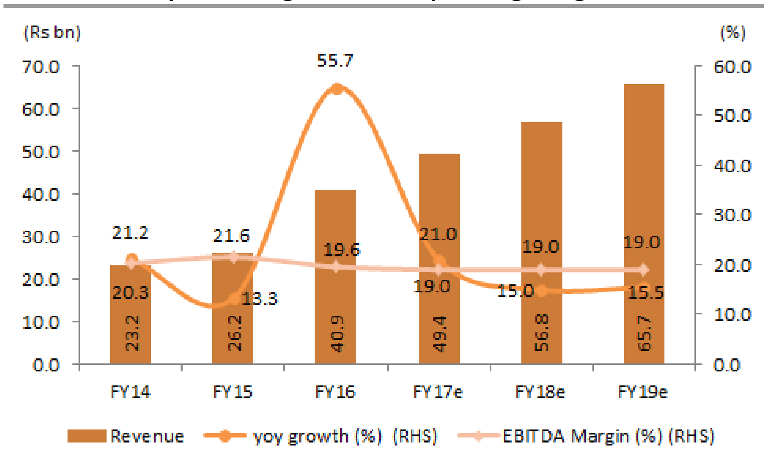
Source: Company

Chart 2: Robust book /bill at 2.8x provides revenue visibility



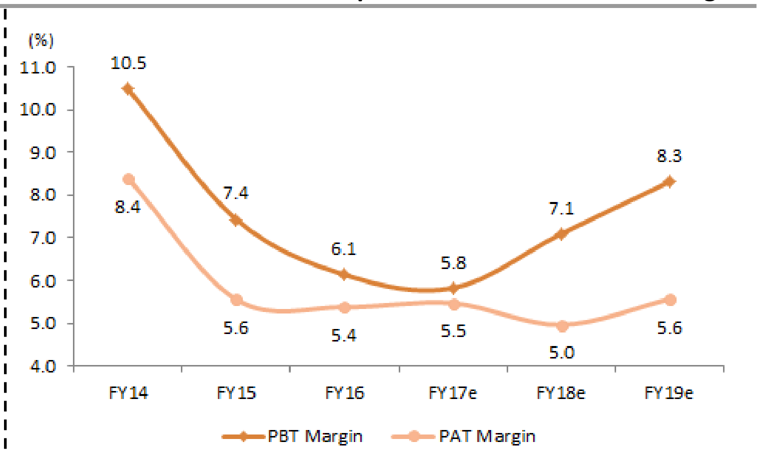
Source: Company

Chart 3: Steady revenue growth and operating margin



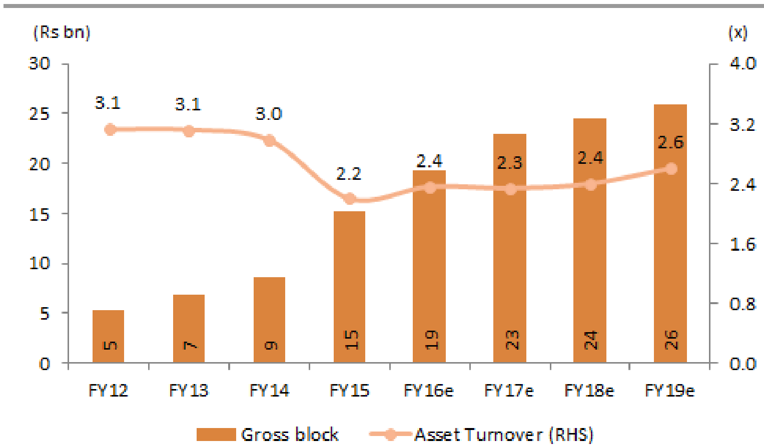
Source: Company, Systematix Institutional Research

Chart 4: Sec. 80 IA tax benefit phase-out to contain PAT margin



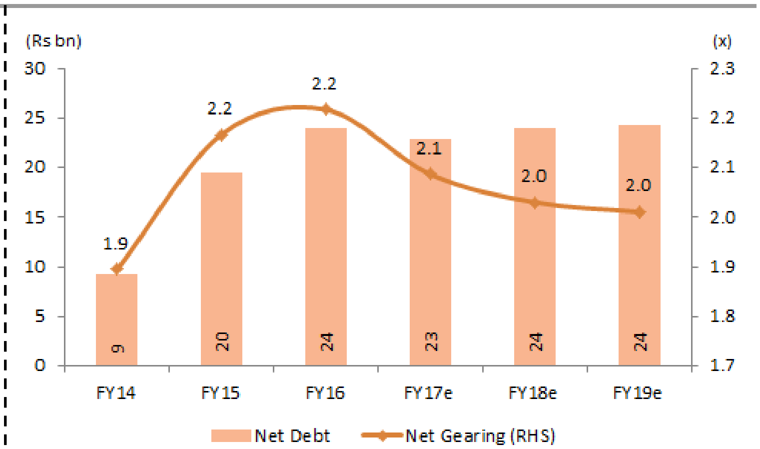
Source: Company, Systematix Institutional Research

Chart 5: Peaking-out of capex to improve asset turns



Source: Company, Systematix Institutional Research

Chart 6: Generation of +ve FCF to stabilise net gearing…



Source: Company, Systematix Institutional Research

Fully integrated road developer with proven track record

Incorporated in 2006, DBL is a leading road-focused EPC player, having executed 47 road projects across ~5,612 lane kms in MP, Gujarat, Himachal Pradesh, Rajasthan and Maharashtra. On the development side, DBL has 21 projects (12 operational – project cost Rs15.7bn and 9 under-construction) in its portfolio. Predominantly a contractor for private developers (FY12: 79% revenue from private), DBL's rising pre-qualification has made it eligible to bid solely for government road projects. In FY16, government contracts contributed 88% of total revenue and 84% of the EPC revenue came from executing contracts for third parties. Based on bidding criteria, DBL is pre-qualified to individually bid for EPC projects worth Rs12.5bn, HAM projects worth Rs28.5bn and BOT projects worth Rs25.6bn. Over the last three years, the company has forayed into irrigation and urban development, with a recent focus on mining segment in a big way. DBL's large in-house modern equipments' fleet comprising of 8,500 construction equipments and vehicles and own staff has aided in efficient execution of projects ahead of time.

Table 1: Business profile

	Roads & Highways (3rd party EPC+ own BOT)	Irrigation	Urban development	Mining
Scope of work	Design, construct and maintain roads and highways on an EPC basis for third party and captive BOT contracts awarded by subsidiary companies and joint ventures	Construction of dams, canals and tunnels, O&M	Redevelopment and re-densification of government housing, building residential units under affordable housing schemes, construction of district court, water supply schemes	Removal of over burden
9MFY17– revenue contribution – Rs33.5bn	90%	7%	1%	2%
9MFY17 order book at Rs131bn	89%	2.0%	2.0%	8.0%
Under execution	64 projects (8,422 lane kms) in 12 states	3 projects in MP	3 projects in MP	

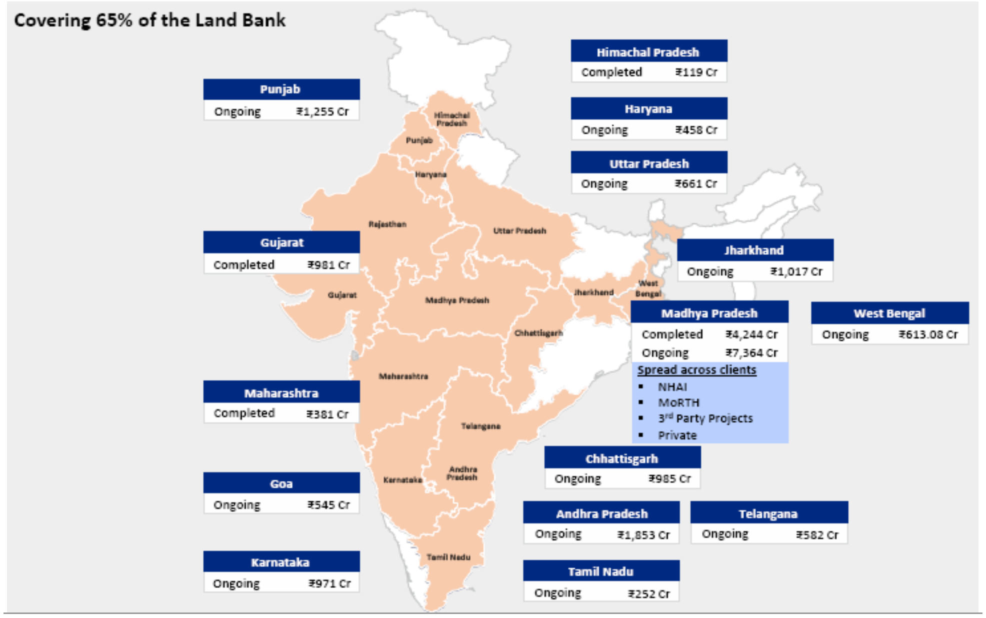
Source: Company, Systematix Institutional Research

Expansion of footprints in newer states, focus on project clustering

- Apart from the above five states, over FY12-17, DBL expanded road operations to newer states such as Andhra Pradesh, Karnataka, Tamil Nadu, Telangana, Punjab, Jharkhand, Chhattisgarh, Haryana, Goa and Uttar Pradesh.
- **EPC projects are selected after taking into consideration their proximity to clusters near existing projects and availability of land and other approvals.** Clustering strategy aids to leverage manpower, equipment and materials set-up at nearby work sites, thus saving transportation costs and investment in new equipments.
- The Guna-Biaora BOT road project in MP (under execution since September 2016) was bid keeping in mind its close proximity to Essel Infra's Gwalior-Shivpuri road BOT project, where DBL is undertaking EPC.
- Irrigation and urban development projects are in Madhya Pradesh, where a maximum number of projects are in progress.

  While DBL is executing projects with an average cost of Rs2.5bn across 65 sites, going forward the management plans to focus on 20-25 large ticket size government projects (average size Rs9-10bn) from Centre and states. Within states, DBL avoids bidding for projects in Odisha, Kerala and North East.

Chart 7: Geographical spread of operations



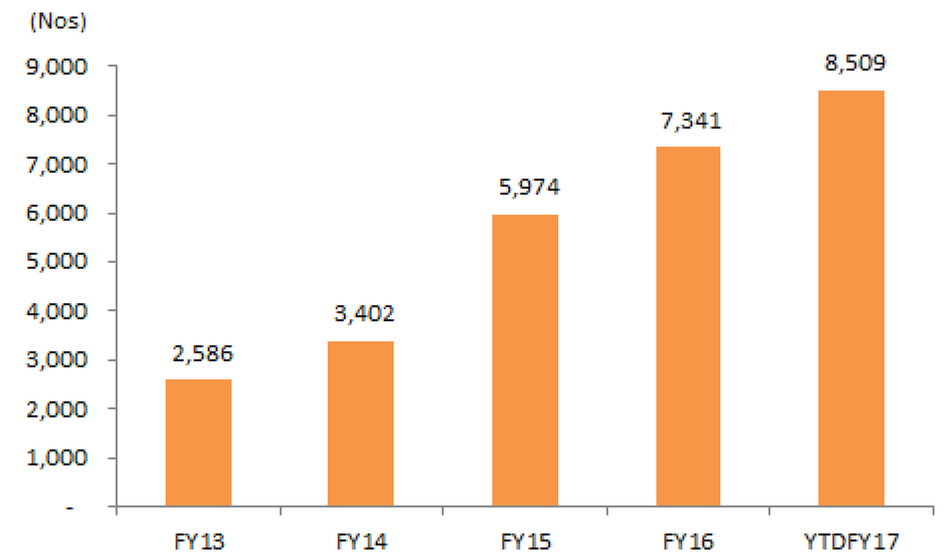
Source: Company

Large fleet of homogenous equipments, centralised procurement process saves costs and downtime

- DBL, over FY11-17, has built the largest equipment bank comprising of 8,500 construction equipments and vehicles (average age of 3.4 years) at a capex of ~Rs22bn to support the execution its growing road order book (procured mining equipment worth Rs2.5bn in FY17).
- Large owned homogenous equipments fleet of pavers, crushers, soil stabiliser, excavators, graders, dumpers among others procured from leading equipment suppliers such as Metso, Vogele, Writgen, Caterpillar, Ashok Leyland and Tata ensure availability of best equipments at competitive prices (avail 8-10% bulk discount).
- The central procurement workshop set up at Pithampur Logistic Park near Indore ensures better control and availability of critical spares and undertakes repair, maintenance and overhaul of its large fleet in-house. Management is confident of mending normal breakdown of equipments at any sites in India within 24 hours.
- In addition, DBL undertakes refurbishment of equipments beyond their standard life, to use them in the lower segment for three to four years. For example, dumpers are used for five years to transport bitumen and later are replaced with tankers on the same truck for a shorter distance of travel.
- For large-scale requirement of principal raw materials such as cement, bitumen and diesel across sites, DBL resorts to centralised procurement directly from the manufacturer. This aids in negotiating for a bulk discount of 6-10% versus market prices, thereby resulting in cost savings.
- A large fleet aids in quick mobilisation and to have complete control over execution, eliminate delay and cost overruns due to untimely breakdowns, thereby improving execution efficiency.

- The company procured a sand classifier CDE plant (cost of Rs15mn) to grind sand from rocks at the site, thus attaining full control on availability of sand and reduce freight transportation cost.
- Machinery deployed to a specific site is monitored by GPS at its head office in Bhopal to track the capacity utilisation, fuel consumption, idleness, cost effectiveness and other operational details.
- The management indicated tapering down of capex upto Rs2.0-3.0bn during FY18 and FY19 for maintenance of its fleet.

Chart 8: Steady increase in total equipments over FY13-FY17



Source: Company, Systematix Institutional Research

Robust employee base among construction peers ensures scalability

As of February 2017, the company has 24,967 personnel across various levels, with the largest being 17,234 technicians, drivers (~15,000), machine operators and other support staff, who are trained by OEMs, to operate the large fleet.

DBL's corporate HR team comprising of 236 personnel effectively deploys 24,967 employees at each team level, right from pre-bidding, designing, post-bidding, execution, monitoring and quality control (~800 employees continuously monitor projects at under-construction/post completion phase). The entire lifecycle of a project is divided into initial, peak and lean phase, over which the manpower is deployed.

Table 2: Large base of 24,967 employees

Top management	6
Senior management	13
DGM, AGM, Project Managers, Senior Managers, Functional Head	217
Engineers, Surveyor, Quantity Surveyor, Managers	1,456
Technicians, Drivers, Machine operators & other support staff	17,234
Other Admin Staff	6,041

Source: Company

Strong process – from inception, execution and to monitoring

DBL undertakes significant pre-bid activities such as site survey, checks land acquisition and EC/FC clearance status, prepares material requirement schedule, identifies aggregate sourcing sites and its proximity to ongoing projects. It follows a careful project selection criterion and has registered a strike rate of 33-36% over the last three years, due to a conservative bidding approach.

An exclusive arrangement with Infinite Civil Solutions, an Ahmedabad-based civil engineering firm with ~200 engineers, ensures project designing work for DBL. The company uses innovative techniques in project designing to save time and costs. In post-bid, the designing company visits site with a project manager to incorporate site specific requirements in the design.

On emerging as a successful bidder, DBL simultaneously mobilises crusher, batching plants and hot mix plants at the site and undertakes production of aggregates from boulders**. As 20% of total aggregates required for a project are kept ready on the site by appointed date, the inventory levels are high for DBL.**

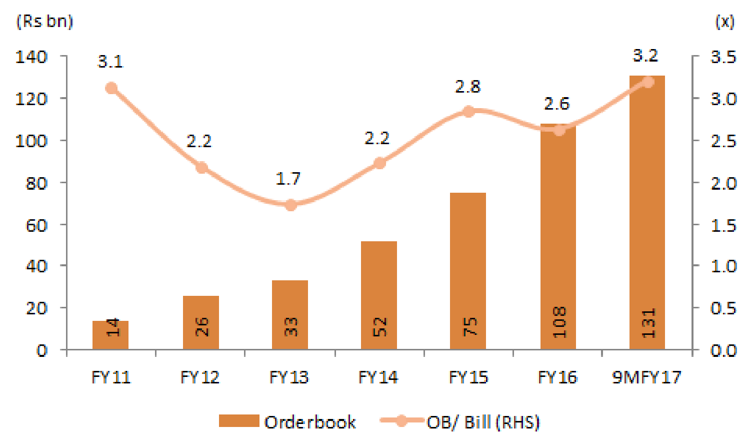
Daily monitoring at the micro level for consumption of raw materials and usage of equipments are undertaken and the project head submits daily progress on the earth work, sub base, GSB, WMM and other structural works to the head office at Bhopal. Any deviation from the target is monitored and measures are taken to immediately rectify the gap. To further undertake accurate monitoring across project sites, DBL is implementing SAP at a total cost of Rs200mn.

Thus, a fully backward integrated set-up, strong project management process, with a well defined task for large employees and equipment fleet, has aided DBL to not only have control on all aspects of project execution but also complete ~90% of a project ahead of schedule. This combined with a geographical diversification, while focusing on cluster-based projects, has resulted in a five-year revenue/PAT CAGR of 57%/41% over FY11-16.

Robust and diversified order book provides visibility

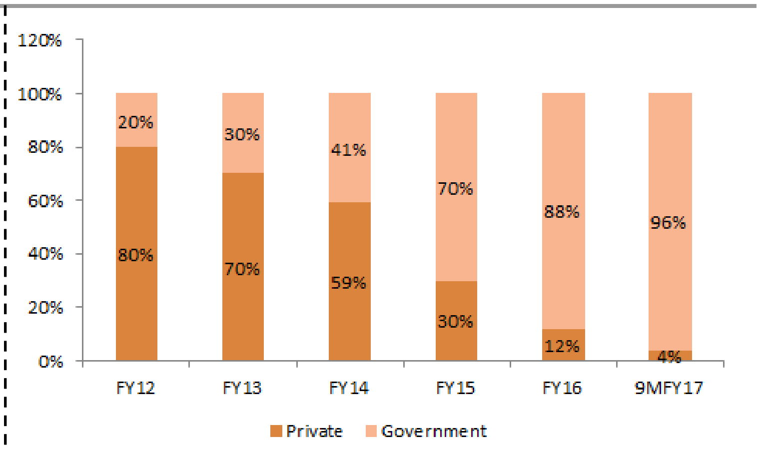
DBL's order book posted 57% CAGR over FY11-16, partly led by higher bidding for projects, on gradual improvement in its prequalification criteria for potential projects. Predominantly from being an MP-centered order book, the company expanded its operations in 10+ states and diversified into newer EPC sectors – irrigation, urban development and mining, while limiting exposure to private clients.

Chart 9: Robust book-to-bill at 3.3x



Source: Company, Systematix Institutional Research

Chart 10: Strategy to limit private sector revenue exposure



Source: Company, Systematix Institutional Research

The order book as of 9MFY17 is at Rs131bn (3.2x FY16 revenue), comprising of 85% orders from roads segment (71% EPC and 14% own BOT), 8% from mining segment, 6% from urban development and 2% from irrigation.

DBL has ventured into irrigation EPC and is undertaking smaller contracts for construction of dams, to build pre-qualification for being eligible for larger river interlinking projects in future. This segment will continue to remain a small part of the overall operations.

The focused strategy of bidding for government contracts, both Centre and states, has reduced the share of private developer orders to 4% in 9MFY17, compared to 80% in FY12. The share of government orders in current order book is at 96%. Geographical diversification led to 85% of the order book from states other than Madhya Pradesh. DBL is executing 54 projects across 11 states.

Break-up of 9MFY17 order book – Rs131bn

Chart 11: Roads dominate, mining picks up

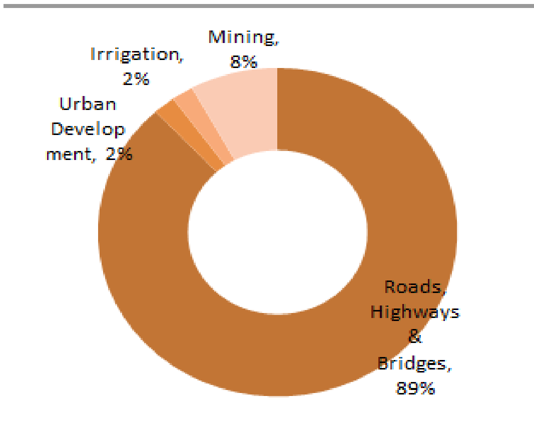


Chart 12: Government share dominant

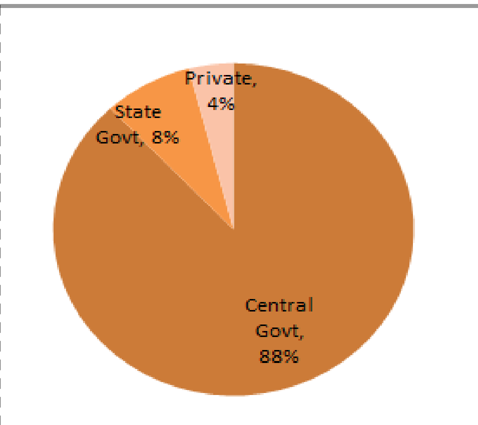
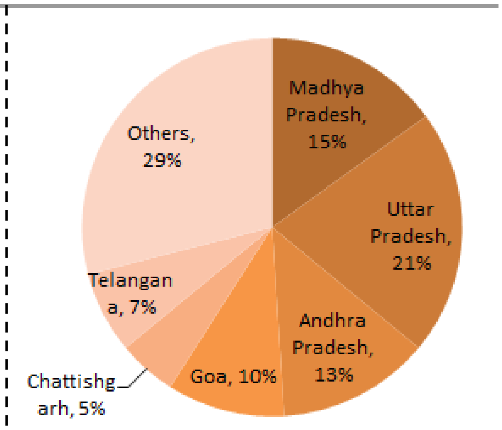


Chart 13: Diversified outside MP



Source: Company, Systematix Institutional Research

The order accretion for YTDFY17 is highest at Rs85bn, comprising Rs51bn from road orders (61%) and Rs34bn (39%) from mining EPC orders. With this the current unexecuted orderbook stands at Rs14.7bn. To build on its expertise of extracting boulders from quarries for road projects, DBL has forayed in a big way to undertake similar work of overburden removal for mining projects. With recent order wins, the share of mining projects has risen to 8% of the 9MFY17 order book. The management expects to generate revenue of Rs1.5/8bn from this segment in FY17/18.

Table 3: Recent mining orders wins

Mining	Rs bn	State	LoA date	Type of work
Northern Coalfields	16.7	MP	Jan-2017	excavation
Northern Coalfields	1.0	MP	Aug-2016	excavation
Singareni Collieries	9.7	AP	Sept-2016	excavation
Western Coalfields	1.5	Maharashtra	LOA not recd	Coal project
Western Coalfields	5.4	Maharashtra	LOA not recd	excavation
Total	**34.4**			

Source: Company

Table 4: Key projects in order book

Project name	Completion date	Project type	Contract price(Rs mn)	o/s order value (Rs mn)	Appointment date	Total single lane (km)	Total road length (km)
Vijayawada-Machilipatnam	Jan-18	Road	7,407	7,407	Jan-16	258	65
Mahulia-Baharagora	Feb-18	Road	6,741	6,741	Feb-18	286	72
Amritsar-Taran-taran-Harikesection	Sep-17	Road	5,580	4,797	Sep-15	184	46
Goa Zuari Cable-Stayed Bridge	Feb-19	Bridge	5,454	5,454	Feb-16	n/a	n/a
Mohanpuramajor multipurpose project	Mar-18	Irrigation	4,159	4,159	Mar-14	n/a	n/a

Source: Company

DBL is interested in bidding for upcoming metro projects in Indore and Bhopal (30km of Rs70bn each), tenders for which are expected in the next year. It will tie up with a foreign partner to qualify for these projects. DBL in consortium with Dhansar Engineering Company Private Limited (DECO) (90%:10%) is L1 at Rs837/MT in reverse auction for MDO tender conducted by DVC for Tubed cCoal block (with mineable reserves of 130 Million Metric Tonnesmn MTPA), located at Auranga Coalfields, District Latehar, Jharkhand. The expected life of the mine will be 29 years i.e. 2 years of construction period and 27 years of operation. The mineable reserves of the block are 130mn MT with the peak capacity of 6mn MTPA.

The company has submitted bids for government road projects worth Rs12.4bn (Rs.4.7bn HAM and Rs.7.2bn EPC), the outcome for which is expected by end-March 2017 and expects to win orders based on a strike rate of 33-36% for the last three years. DBL will submit additional bids worth Rs11bn in April 2017. The management expects to focus on execution of current order book, before adding new orders, and has guided for order accretion of Rs30bn in FY18 and revenue of Rs60bn/70bn for FY18/19. Based on healthy EPC order book, we expect 15% CAGR in standalone revenue over FY17e-19e.

Chart 14: Robust book /bill at 2.8x

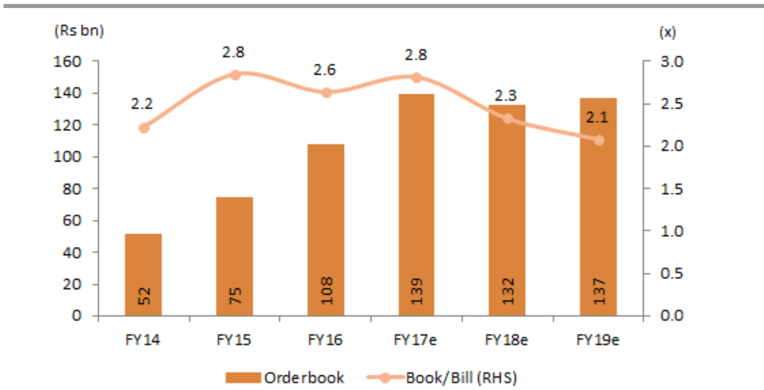
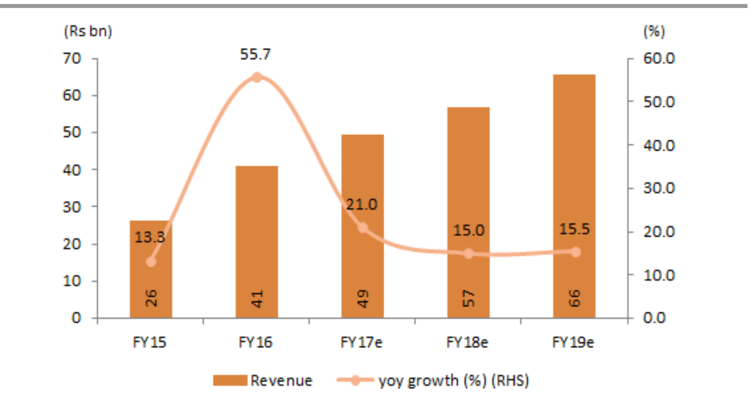


Chart 15: Provides 15% CAGR revenue visibility over FY17-19e



Source: Company, Systematix Institutional Research *Source: Company, Systematix Institutional Research*

Development portfolio of 21 BOT assets adds to revenue stream

DBL has built a portfolio of 21 BOT assets, comprising of 12 operational and 9 under implementation, spread across MP, UP, Maharashtra and Gujarat.

Table 5: Portfolio of 100% owned 12 operational assets

Project	Type	Total cost (Rs mn)	Length (km)	Awarding authority	Equity (Rs mn)	Annual annuity (Rs mn)	COD	Residual Life (yrs)
Betul Sarni Junnardeo-Parasia	Annuity + Toll	3,216	124	MPRDC	806	310	12-May-15	12.5
Nadiad-Modasa	Annuity	2,081	108	R&BD GoG	287	349	31-Dec-13	9.8
Mundi-Sanawad	Annuity + Toll	1,410	68	MPRDC	210	166	15-May-13	10.5
Jaora-Piploda	Annuity	1,344	88	MPRDC	200	241	9-May-14	11.8
Silwani-Sultanganj	Annuity + Toll	1,287	76	MPRDC	210	190	25-Mar-13	10.4
Bankhlafatta-Dogawa	Annuity	1,158	65	MPRDC	160	198	31-Mar-14	11.8
Uchera-Nagod	Annuity + Toll	1,140	56	MPRDC	320	169	15-May-14	11.2
Sardarpur-Badnawar	Annuity + Toll	977	43	MPRDC	100	94	9-Jun-12	10.2
Ashoknagar-Vidisha	Annuity + Toll	847	36	MPRDC	200	101	26-Jul-14	12.1
Sitamau-Suwasara	Annuity + Toll	604	35	MPRDC	78	74	28-Mar-13	10.6
Mandsaur-Sitamau	Toll	349	44	MPRDC	65	-	5-Feb-09	16.1
Tikamgarh (Dhajrai) Jatara-Palera Nowgaon	Annuity + Toll	1,300	76	MPRDC	260	178	26-May-15	12.9
Total		**15,713**	**819**		**2,895**			**Average 12 years**

Source: Company, Systematix Institutional Research

The company owns 100% stake and has invested Rs3.8bn till date in the 12 operational projects of 819km in the form of equity and sub-debt. In FY16, the portfolio generated total revenue of Rs2.8bn and PAT loss of Rs198mn. However, it is cash positive and given that majority of revenue comes in form of annuity; the risk to cash flow is low. Management is exploring options to monetise the portfolio and sell ~50% stake to financial investors to raise capital for funding newer projects.

Nine under-construction projects – foray into three hybrid annuity projects

DBL's 9 under-construction projects of 648km comprise of six projects of 425km, which are under various stages of construction (2 annuity + toll, 3 annuity and 1 toll) and three recently-won hybrid annuity projects of 223km.

During FY17, the company invested Rs2.5bn in these six under-construction projects. It has recently completed the construction of Hata-Fatehpur project (annuity + toll) 400 days ahead of schedule and is eligible to receive an early completion bonus of Rs154mn from MPRDC.

Table 6: Under construction asset portfolio of 9 projects

Project	Type	TPC (Rs mn)	Equity (Rs mn)	kms	Status
Hata Fatehpur	Annuity + Toll	1,011	271	64	Completed 400 days ahead of schedule; eligible for Rs154mn bonus
Guna Biora	Toll	9,010	2200	94	ongoing
Patan-Tendukeda- Rehli	Annuity + Toll	2,618	668	87	ongoing
Mundargi - Hadagali – Harapanahalli	Annuity	1,790	293	51	ongoing
Hassan - Ramanathapura - Periyapatna	Annuity	2,546	362	74	ongoing
Hirekerur – Ranibennur	Annuity	1,984	321	56	ongoing
Lucknow - Sultanpur	HAM	20,160	2846	123	FC done, two camp sites mobilized, to procure appointed date by March end
Kalmath to Zarap	HAM	9,140	-	44	FC under process
Tuljapur - Ausa	HAM	9,110	-	56	LOA received, signed MoU with Shrem Infraventure Pvt Ltd to invest 49% equity capital in SPV for this project, DBL to hold remaining 51%.

Total				**648**	

Source: Company, Systematix Institutional Research

We visited the site of Guna-Biaora road project recently, 100% owned by DBL. Given that the company attained an appointed date on Sept 7, 2017, significant progress is made on construction work, with four lanes of 38km (40% of total project) already complete.

Table 7: Project milestone schedule: Guna-Biaora BOT road project

Milestone	Timeline	Target v/s Achievement
I	15% progress of total project cost	6-Mar-17 (Rs1,352mn)
	180^{th} day from appointed date	Achieved on 15^{th} Dec'16
II	15% progress of total project cost	6-Dec-17 (Rs3,605mn)
	455^{th} day from appointed date	Achieved on 15^{th} Mar'17
III	70% progress of total project cost	19-Jun-18 (Rs6,309mn)
	650^{th} day from appointed date	In progress
IV	100% progress of total project cost	6-Mar-19 (Rs9,013mn)
	910^{th} day from appointed date	-

Source: Company, Systematix Institutional Research

DBL has achieved two milestones ahead of schedule and expects to complete the project by March 2018, a year ahead of estimated scheduled completion of Mar 6, 2019. The toll of ~Rs900mn collected during this one year will be booked as early completion bonus in the EPC arm.

The project is a part of erstwhile NH-3 and is the last leg on the road stretch which connects Delhi to Bhopal and further to Mumbai. Stretches prior to this are being developed by other contractors and once completed, the management expects a shift in Mumbai-based traffic to this route from NH-8, as it is shorter by 80km.

Financial closure and equity requirement

DBL has tied up for debt for the Lucknow-Sultanpur HAM project at a cost of ~9.5% and expects to receive appointed date by end of March 2016. The company has already invested Rs2bn and mobilised two camp sites with crushers, tippers and 1.5lakh tonne of material. It expects to receive 10% mobilisation advance of ~Rs2bn in May 2017, 60 days from the appointed date.

Financial closure of Kalmath-Zarap HAM project is in advanced stages and that for Tujlapur-Ausa is under progress.

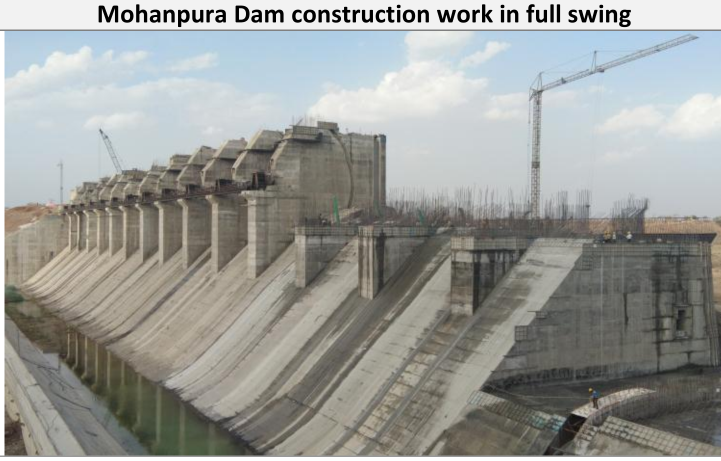
Over the next two years, the pending equity required to be invested by DBL in all 9 under-construction projects is at Rs4.6bn (Rs2.5bn in FY18 and Rs2bn in FY19), which will be funded through cash flows from operational projects and asset monetisation proceeds. The management has indicated that it is in talks with financial investors to divest 1) its partial stake in operational portfolio and 2) divestment of up to 49% in under-construction Lucknow-Sultanpur HAM project to free up capital.

Chart 16: Site Visit Snapshot

9 mtr long paver laying bitumen

Rollers plying for levelling of freshly laid bitumen

Mohanpura Dam construction work in full swing



Steel gates (fabricated inhouse)for releasing surplus water

Source: Company, Systematix Institutional Research

Improvement in profitability and balance sheet

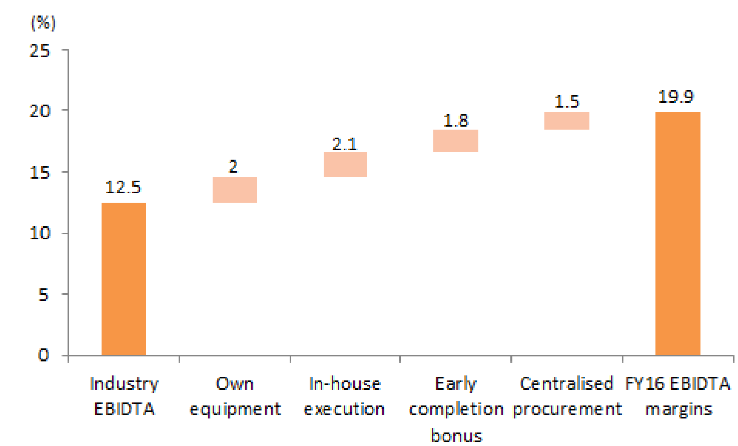
DBL's average standalone EBITDA margin over FY10-16 was at 21%, while for 9MFY17 at 19%. This is high compared to peers in the construction industry. Its business model, supported by robust in-house project execution and monitoring capabilities will aid in sustaining these, even as the business grows.

Procurement of own equipment from established suppliers, as against leasing from different operators helps to save costs (2-2.5% of revenue) and availing bulk discounts, reduces breakdown time, led by better regular maintenance.

Minimal subletting and carrying out each and every activity/job in-house by its massive and trained workforce saves DBL from sub-contracting work (saves 2.1% of revenue) compared to peers such as Sadbhav Engineering and KNR Construction. It also assists DBL to adhere to strict timelines and in turn complete projects ahead of time. The company has thus earned an early completion bonus of Rs2.2bn over FY12-16, comprising Rs1.9bn for 11 in-house BOT projects and Rs286mn for 10 government EPC projects. On an average, this translated into 1.5-2% of the revenue.

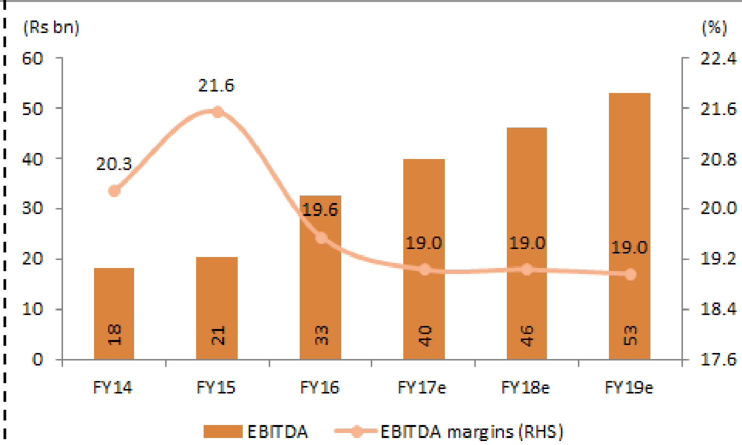
DBL also gains from bulk procurement of key raw materials such as cement, steel, bitumen, diesel, fuel oil, scaffolding, signboards, lubricants, tyres, batteries and spares for machinery at its central warehouse near Indore. Being a large-scale buyer, it is able to extract huge discount and also make available the material at projects' site within the lowest time.

Chart 17: Levers to support high EBITDA margin



Source: Company, Systematix Institutional Research

Chart 18: EBITDA margin to remain steady at 19%



Source: Company, Systematix Institutional Research

Historically, captive BOT projects comprised 7-17% of the order book during FY12-16. In spite of this, DBL was able to maintain high EBITDA margin from third party EPC contracts. Going forward, we expect EBITDA margin run rate of 19% to continue over FY17e-19e, in spite of third party EPC and HAM road projects.

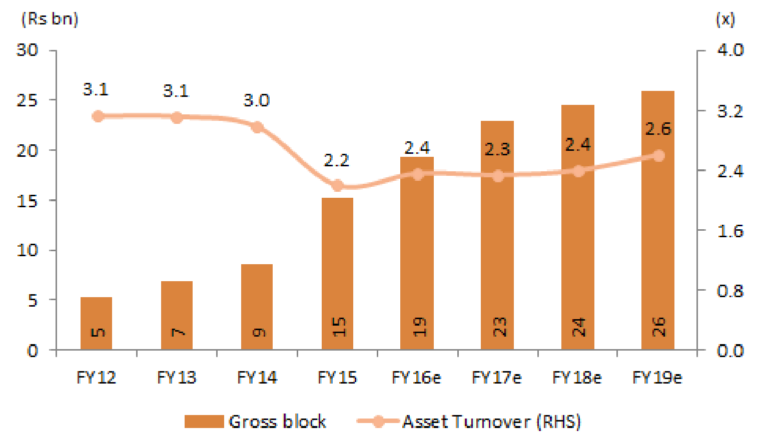
During FY13-17, the company incurred massive capex of Rs18bn (Rs3.6bn in FY17 to purchase mining and road equipments), resulting in a decline in asset turnover from 3.1x in FY13 to 2.2x in FY16. DBL has guided for routine maintenance capex of Rs1bn in FY18/19. With peaking-out of capex in FY17 and based on robust order book, we expect higher sweating of the gross block and the asset turns to improve to at least 2.6x in FY19e, considering a base case scenario of 15% revenue growth over FY17e-19e.

Gradual expansion to newer states led to an increase in operational sites to 56 in FY16, compared to 23 in FY12. DBL's practice of in-house crushing and stocking up large inventory of aggregates at sites resulted in an increase in inventory to 141 days in FY16 v/s 61 days in FY12. Going forward, with an increase in average ticket size of a project to Rs5bn+, compared to Rs2.5bn now, DBL envisages the number of sites to come down to 20. Thus, absolute inventory would remain the same and we expect inventory days to decline to 133 in FY19e.

In FY12, private players contributed 80% of the total revenue where DBL continued to execute work, in spite of irregularity and non-receipt of payment. While contribution from private players in total revenue came down to 12% in FY16, the corresponding debtor days increased from 84 in FY12 to 108 in FY16 on non-receipt of payments from two sticky customers, Essel Infra and Topsworth. DBL received Rs1bn from these two accounts during 9MFY17 (outstanding Rs4.3bn in FY16) and expects to receive Rs1.5bn in FY18 from current outstanding of Rs3.2bn. Thus, we expect the recovery of private debtors combined with rapid payments from government agencies to lower debtor days to 92 by FY19e.

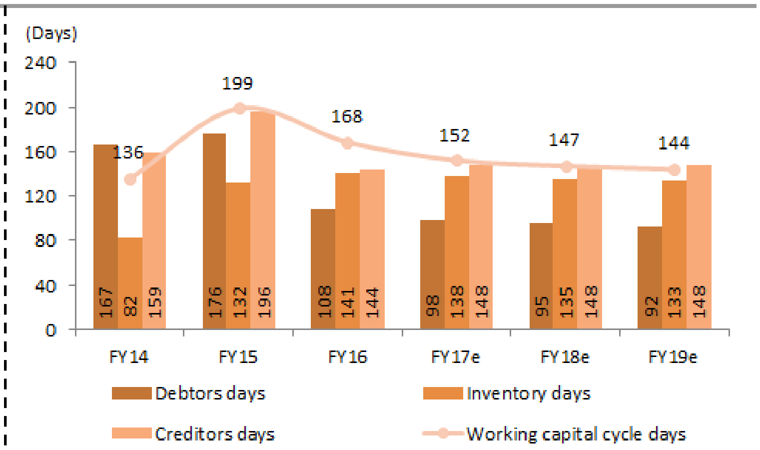
Overall, we expect the working capital cycle to come down to 147 days in FY19e, compared to 168 days in FY16.

Chart 19: Peaking-out of capex to improve asset turns



Source: Company, Systematix Institutional Research

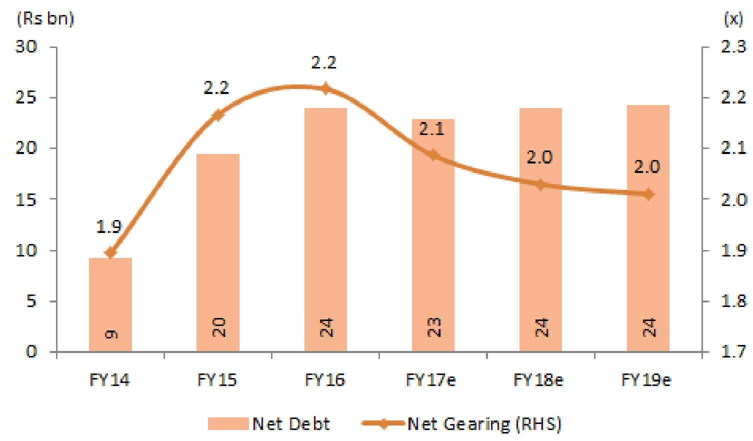
Chart 20: Working capital cycle to lower on improved efficiency



Source: Company, Systematix Institutional Research

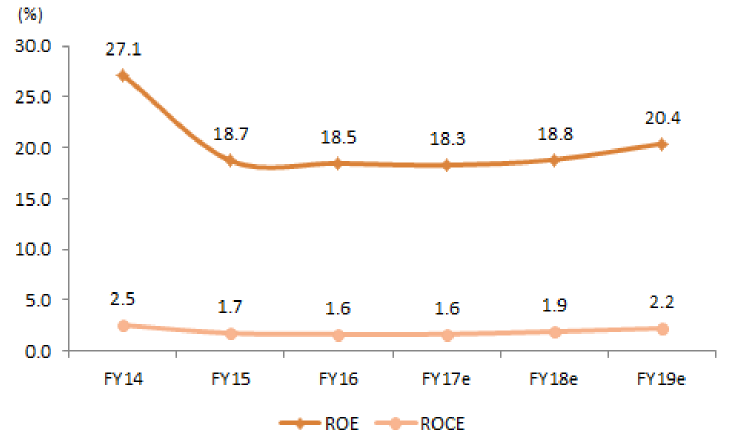
Rising working capital cycle combined with massive capex over FY12-16 resulted in negative FCF (Rs19bn), despite strong cash profit generation of Rs13bn. This in turn increased gearing to 2.3x in FY16, v/s 1.4x in FY14, and strained the balance sheet. Fund raising of Rs4.3bn via IPO has lowered the gearing for 9MFY17 to 1.3x. Current gross debt is at Rs24.5bn, comprising of Rs14bn of working capital loan and Rs10bn term loan. Going forward, we expect DBL to generate FCF of Rs2.7bn over FY17e-19e, given steady working capital and lower capex, thus improving the gearing to 1.1x in FY19e (still high compared to 0.5x for peers such as SADE).

Chart 21: Generation of +ve FCF to stabilise net gearing…



Source: Company, Systematix Institutional Research

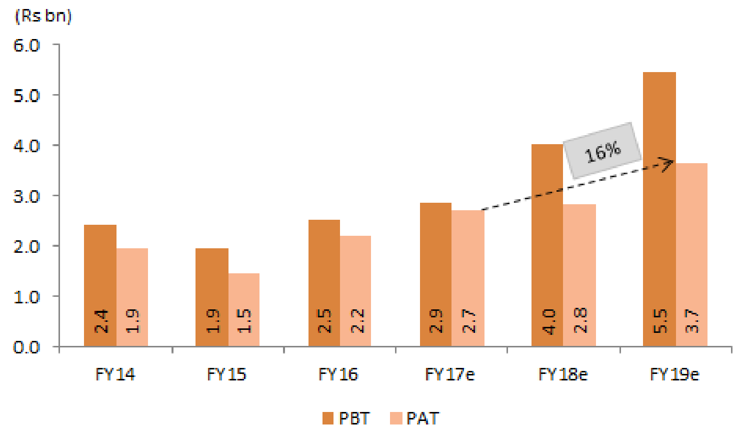
Chart 22: …Leading to RoCE improvement



Source: Company, Systematix Institutional Research

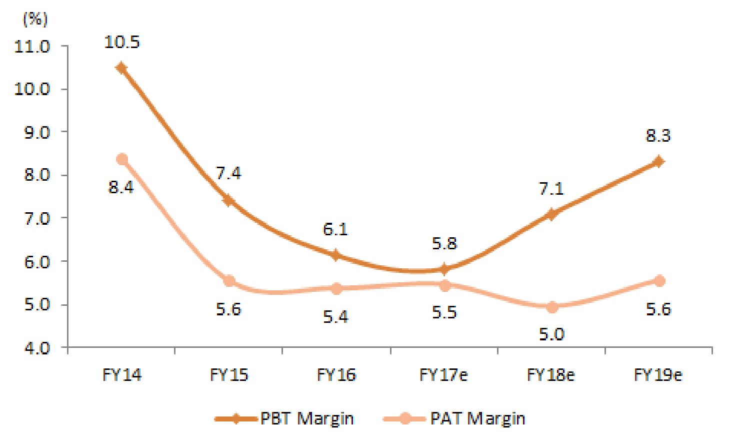
An improvement in net gearing will also lower interest expenses (fall to 36% of EBITDA, compared to 48% in FY16), thus driving 38% CAGR in PBT. While PBT margin is estimated to improve from 6.1% in FY16 to 8.3% in FY19e, we expect PAT margin to remain at 5.6%, due to phasing out of section 80 IA tax benefits in FY18/19.

Chart 23: 14% PAT CAGR over FY17e-19e



Source: Company, Systematix Institutional Research

Chart 24: Sec. 80 IA tax benefit phase-out to contain PAT marginz



Source: Company, Systematix Institutional Research

Key management team

Dilip Suryavanshi (Chairman and MD)

- A civil engineer with 32 years experience.
- He liaises with various departments of the government and also overlooks processes including tendering, bidding and planning projects.

Devendra Jain (CEO & Executive Director)

- A civil engineer, with over 17 years of experience in the business of construction.
- He looks after project implementation along with the quality of work and ensures timely completion of projects undertaken.

Seema Suryavanshi (Executive Director)

- She has over 17 years of experience in the business of construction.
- Actively participates in finance, investment and various company affairs as a coordinator between execution and administrative wing of the company.

Rohan Suryavanshi (Head – Strategy and Planning)

- He holds a bachelors degree in commerce from the University of Pune and a masters degree in business administration from The Wharton School, University of Pennsylvania.
- He is responsible for business strategy and planning, financial planning and streamlining existing business processes and implementing enterprise resource planning (ERP).

Karan Suryavanshi (Head – Business Development)

- He holds a bachelors degree in business administration from Symbiosis Centre for Management Studies.
- He has a total work experience of over Six years. He is responsible for planning, liasoning with the government, sales, marketing, business development, and management functions of our Company

Key risks

1) Backward integrated business model with equipment ownership and high employee base also entails high fixed costs. Inability to maintain a healthy order book can exert pressure on future profitability.
2) While DBL undertakes due diligence before bidding for a project, any delays in land acquisition clearance from an authority for EPC projects, will risk execution and revenue estimates.

Valuation and view

We expect DBL's healthy order book, large order pipeline and backward integrated business model to drive 15% revenue CAGR over FY17e-19e. We expect EBITDA margin to sustain at 19%, given a tight leash on project costs and early completion to generate bonus for ongoing projects. Peaking-out of capex and steady working capital along with recent fund raising will keep debt at current levels, resulting in gearing of 1.1x in FY19e. We expect PBT to grow at 35% CAGR over FY17e-19e and a PAT growth at 14% CAGR (phasing out of section 80 IA benefits to keep tax rate high).

We value the EPC business at 14x FY19e EPS, discount compared to industry average due to higher standalone FY19e gearing at 1.1x v/s 0.3-0.5x for peers. On the assets portfolio, we value operational assets at 1x P/BV, given annuity assets and investment of Rs2.5bn till date in under-construction assets at 0.5x P/BV. We initiate coverage with an **Accumulate** rating and a SOTP-based target price of Rs411 (EPC value Rs374, 14x FY19e EPS and Rs36 for BOT projects).

Table 8: SOTP valuation

	Valuation basis	Multiple	Value (Rs mn)	Value / share (Rs)
EPC construction	P/E	14xFY19e PAT	51,173	**374**
Investment in BOT assets				**36**
Operational	P/BV	1xFY17 BV	3755	27
Under construction	P/BV	0.5xFY17 BV	1222	9
Fair Price				**411**
CMP				349
Upside (%)				**18**

Source: Systematix Institutional Research

Sadbhav Engineering

27 March, 2017

Road specialist with unparalled execution track record

INITIATING COVERAGE	
Sector: Construction	Rating: Accumulate
CMP: Rs310	Target Price:Rs335

Stock Info

Sensex/Nifty	29,332/ 9,086
Bloomberg	SADE IN
Equity shares (mn)	172
52-wk High/Low	Rs325/ 220
Face value	Rs1
M-Cap	Rs53bn/ $0.8bn
3-m Avg volume	$0.4mn

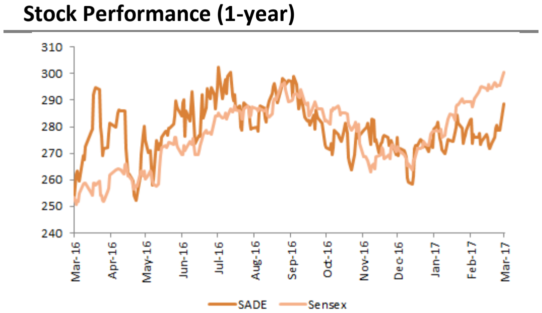
Financial Snapshot (Rs bn)

Y/E March	FY17e	FY18e	FY19e
Sales	32,848	38,058	43,264
EBITDA	3,550	4,115	4,689
PAT	1,633	1,909	2,211
EPS (Rs)	9.5	11.1	12.9
PE (x)	32.6	27.9	24.1
EV/EBITDA (x)	18.6	14.9	12.9
P/BV (x)	3.3	2.9	2.6
RoE (%)	10.5	11.0	11.4
RoCE (%)	9.1	10.5	12.6
Dividend yield (%)	0.2	0.2	0.2
Net gearing (x)	0.8	0.4	0.4

Shareholding pattern (%)

	Dec '16	Sep '16	Jun '16
Promoter	46.8	46.8	47.2
–Pledged	-	-	-
FII	16.9	17.6	16.1
DII	26.1	25.3	25.8
Others	10.2	10.3	10.9

Stock Performance (1-year)



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Sadbhav Engineering (SADE), among the top five construction companies, has an unparalleled track record to finish EPC projects ahead of time, led by strong in-house execution capabilities. Robust order book at Rs77bn (2.5x TTM sales) continues to be dominated with roads (63%) followed by mining (23%) and irrigation (14%). Diversification into road BOT assets through SINP, its 68% subsidiary, assures EPC business and aids in garnering upside from toll collection. The near term NHAI bid pipeline is strong with 27 projects of 1,420 km worth ~Rs350bn are expected to be tendered out in March-May'17. Six projects in mining while 17 projects (worth Rs75bn) in irrigation segment are up for bidding over next two quarters. SADE will infuse Rs1.6bn equity over next two years in five HAM projects while remaining SINP will invest remaining Rs3.0bn. We estimate 15%/16% revenue/PAT CAGR over FY17-19e, led by a strong order book growth and steady OPM at 10.8%. We initiate coverage with a Buy rating and SOTP-based target price of Rs335, valuing EPC business at Rs194 (15x FY19 earnings) and BOT assets at Rs141 (DCF).

Diversified order book, established pedigree to drive 15% revenue CAGR over 3 years

SADE's EPC order book of Rs77bn (2.5x TTM revenue) at 9MFY17-end, has compounded 19% since FY06, is welll-diversified in roads (63%), irrigation (14%) and mining (23%) segments across 11 states. Road segment dominates the orderbook with orders equally divided from external clients and captive BOT/HAM projects. Over-burden extraction in coal mining and construction & remodeling of canals in irrigation have given SADE the pre-qualification to bid for larger size contracts. Having worked with reputed clients such as NHAI, Sardar Sarovar Narmada Nigam, Coal India, GIPCL, L&T, HCC among others, SADE has clocked 27% revenue CAGR over FY06-16. Order pipeline of Rs350bn in roads EPC/HAM/BOT, ~Rs500bn in mining contracts and Rs97bn in irrigation is a positive. Given a proven execution track record and strong bid pipeline, we estimate 15% revenue CAGR over FY17-19e.

Increasing traffic and debt refinancing likely to improve BOT cash flows

SADE holds 68% stake in Sadbhav Infraprojects (SINP), the holding company for 12 BOT road assets(11 fully/partially operational, 1 under construction). On a like-to-like basis, 9MFY17 toll collection fell 5.9% yoy to Rs4.7bn. The management indicated 2-3% yoy traffic growth for January'17 and further improvement in February'17. Refinancing of eight projects (five completed and three in pipeline) can result in 100-150bps reduction in interest cost and cash outflow savings of Rs0.5-0.6bn. We expect with a residual life of ~16 years, increasing traffic along with debt refinancing on operational projects to generate 23% revenue CAGR in FY17-19e and healthy positive free cash flow of 52% over FY22e-27e. Over next two years, SADE will infuse Rs1.6bn equity in five HAM projects while SINP will invest remaining Rs3.0bn. SINP is exploring options to exit two operational road assets namely Bijapur-Hungund (equity value Rs3.5bn) and Dhule – Paleshnar(equity value Rs5.0bn) to unlock value and free up funds for investment in newer projects.

Steady operating margins; easing working capital cycle to improve ROCE

SADE has historically reported an average EBITDA margin of 10.7% over FY06-16, in spite of a change in sales mix from predominantly roads (70-75% in FY11-13) to a higher share of mining and irrigation, led by strong execution expertise and a tight leash on costs. The average working capital cycle increased from 78 days over FY09-12 to 138 over FY13-16, led by an increase in loans to SPVs in the form of sub-debt overall gearing increased only by 0.2x. With operational projects generating sufficient cash flows, Over FY17e-19e, we estimate steady EBITDA margin at 10.8%. In near term, stuck receivables in ongoing irrigation and mining projects, repayment of NHAI mobilisation advances (Rs1.1bn repaid, to pay Rs1.8bn in 4Q17) and financial support to SIPL will keep the gearing high at 0.8x in FY17e. We estimate that release of milestone based payment from NHAI and repayment of loan from SIPL can reduce net gearing to 0.3x in FY19e thus improving ROCE to 12.6% vs 9.1% in FY17e. We expect 16% CAGR in standalone PAT to Rs2.2bn in FY19e.

Investors are advised to refer through disclosures made at the end of the research report.

Financials (Standalone)

Profit & Loss Statement

YE: Mar (Rs mn)	FY15	FY16	FY17e	FY18e	FY19e
Net revenues	29,698	31,863	32,848	38,058	43,264
Revenue growth (%)	25.9	7.3	3.1	15.9	13.7
- Op. expenses	26,696	28,609	29,298	33,943	38,574
EBIDTA	3,002	3,254	3,550	4,115	4,689
EBITDA margins (%)	10.1	10.2	10.8	10.8	10.8
- Interest expenses	1,382	1,515	1,524	1,271	1,061
- Depreciation	817	849	1,035	1,108	1,172
+ Other income	655	905	659	711	701
PBT	1,459	1,794	1,650	2,447	3,158
- Tax	321	263	16	538	947
Effective tax rate (%)	22.0	22.6	1.0	22.0	30.0
Adjusted PAT	1,137	1,531	1,633	1,909	2,211
+/- Extraordinary items	-	(194)	-	-	-
+/- Minority interest	-	-	-	-	-
Reported PAT	1,137	1,337	1,633	1,909	2,211
Adj. FDEPS (Rs/share)	6.6	8.9	9.5	11.1	12.9

Source: Company, Systematix Institutional Research

Balance Sheet

YE: Mar (Rs mn)	FY15	FY16	FY17e	FY18e	FY19e
Share capital	172	172	172	172	172
Reserves & Surplus	13,349	14,543	16,176	18,085	20,296
Networth	13,521	14,715	16,348	18,257	20,467
Minority interest	-	-	-	-	-
Total Debt	10,763	10,588	13,250	8,800	7,800
Def. tax liab. (net)	244	231	231	231	231
Capital employed	**24,528**	**25,533**	**29,829**	**27,288**	**28,498**
Net Fixed assets	5,357	5,550	4,815	4,307	3,735
Investments	5,313	5,278	5,278	5,278	5,278
- of which liquid	-	-	-	-	-
Net Working capital	13,507	14,339	19,259	17,100	19,084
Cash and bank balance	351	366	477	603	401
Capital deployed	**24,528**	**25,533**	**29,829**	**27,288**	**28,498**
Net debt	10,412	10,221	12,773	8,197	7,399
WC (days)	166	164	214	164	161
Book value (Rs/sh)	79	86	95	106	119

Source: Company, Systematix Institutional Research

Cash Flow

YE: Mar (Rs mn)	FY15	FY16	FY17e	FY18e	FY19e
PAT	1,137	1,337	1,633	1,909	2,211
+ Non cash items	704	836	1,035	1,108	1,172
Cash profit	1,842	2,173	2,668	3,017	3,382
- Incr/(Decr) in WC	4,845	816	4,809	(2,285)	2,185
Operating cash flow	(3,004)	1,356	(2,141)	5,302	1,197
- Capex	1,248	1,042	300	600	600
Free cash flow	(4,252)	314	(2,441)	4,702	597
- Dividend	144	145	145	145	145
+ Equity raised	20	0	-	-	-
+ Debt raised	666	(176)	2,662	(4,450)	(1,000)
+ Minority Interest	-	-	-	-	-
- Investments	103	(35)	-	-	-
- Misc. items	(3,403)	13	(35)	(19)	(346)
Net cash flow	(410)	15	111	126	(201)
+ Opening cash	762	351	366	477	603
Closing cash	351	366	477	602	401

Source: Company, Systematix Institutional Research

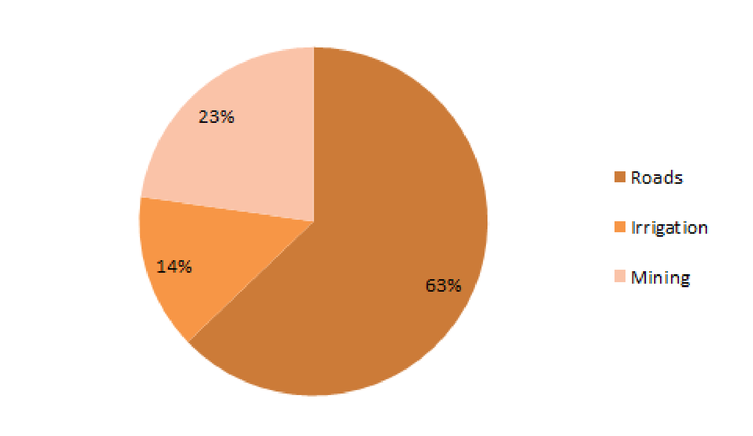
Ratios

YE: Mar	FY15	FY16	FY17e	FY18e	FY19e
P/E (x)	46.7	34.7	32.6	27.9	24.1
P/E core (x)	32.5	24.1	22.6	19.3	16.7
P/B (x)	3.9	3.6	3.3	2.9	2.6
EV/EBITDA (x)	21.2	19.5	18.6	14.9	12.9
RoE (%)	9.9	9.5	10.5	11.0	11.4
RoCE (%)	9.8	9.6	9.1	10.5	12.6
Fixed Asset turnover (x)	3.8	3.5	3.4	3.7	4.0
Dividend yield (%)	0.2	0.2	0.2	0.2	0.2
Dividend payout (%)	10.6	7.8	7.4	6.3	5.4
Interest exp./Sales	4.7	4.8	4.6	3.3	2.5
Debtors (days)	115	119	168	135	125
Revenue growth (%)	25.9	7.3	3.1	15.9	13.7
PAT growth (%)	(21.3)	34.6	6.7	16.9	15.8
EBITDA growth (%)	20.4	8.4	9.1	15.9	14.0
EPS growth (%)	(30.4)	34.6	6.7	16.9	15.8
Net gearing (%)	0.8	0.7	0.8	0.4	0.4

Source: Company, Systematix Institutional Research

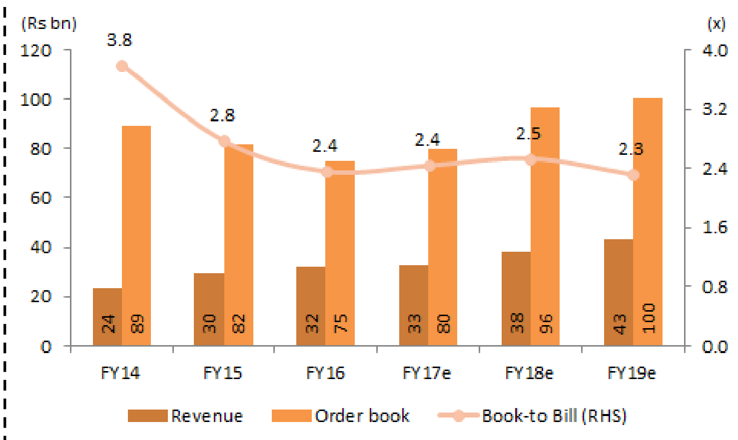
Charting the story

Chart 1: Diversified orderbook of Rs77bn



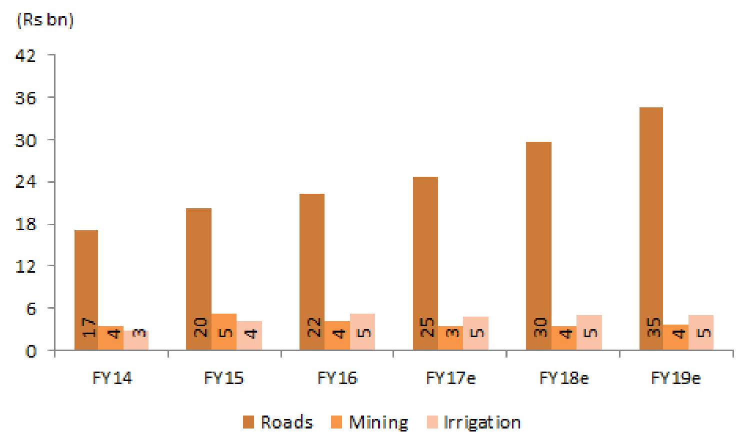
Source: Company

Chart 2: Healthy book/bill ratio, 15% revenue CAGR over FY17-19e



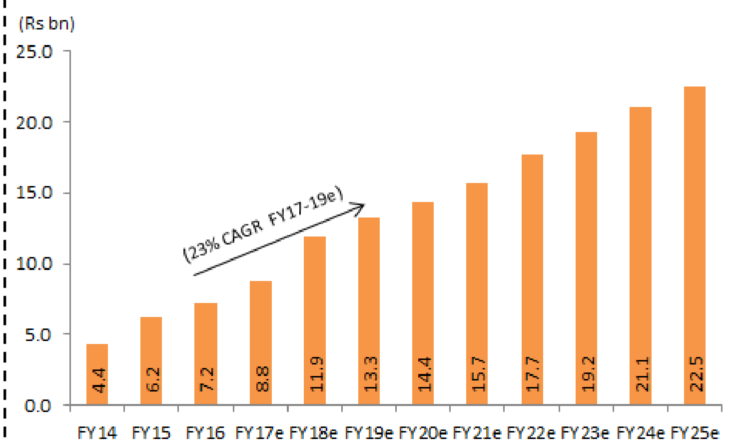
Source: Company, Systematix Institutional Research

Chart 3: Road segment to dominate in revenue mix



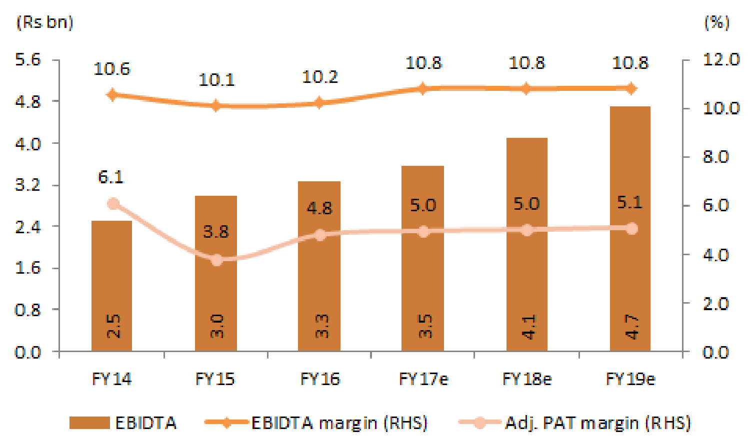
Source: Company, Systematix Institutional Research

Chart 4: SINP toll revenue to compound 26% CAGR over FY17-19e



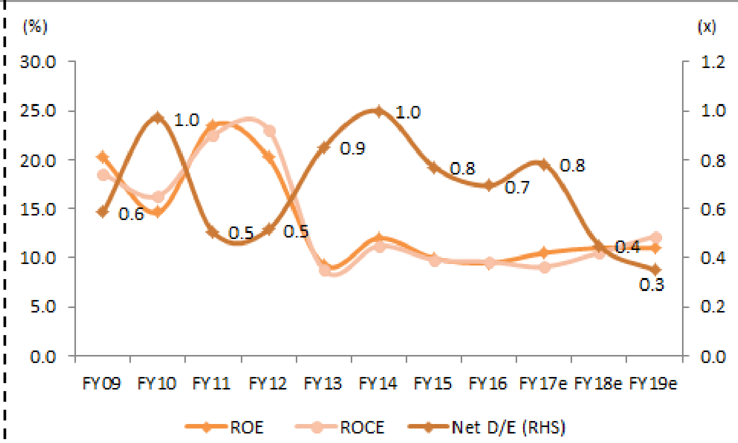
Source: Company, Systematix Institutional Research

Chart 5: EBITDA CAGR at 13% over FY17-19e



Source: Company, Systematix Institutional Research

Chart 6: Repayment of loans from SIPL to improve net D/E

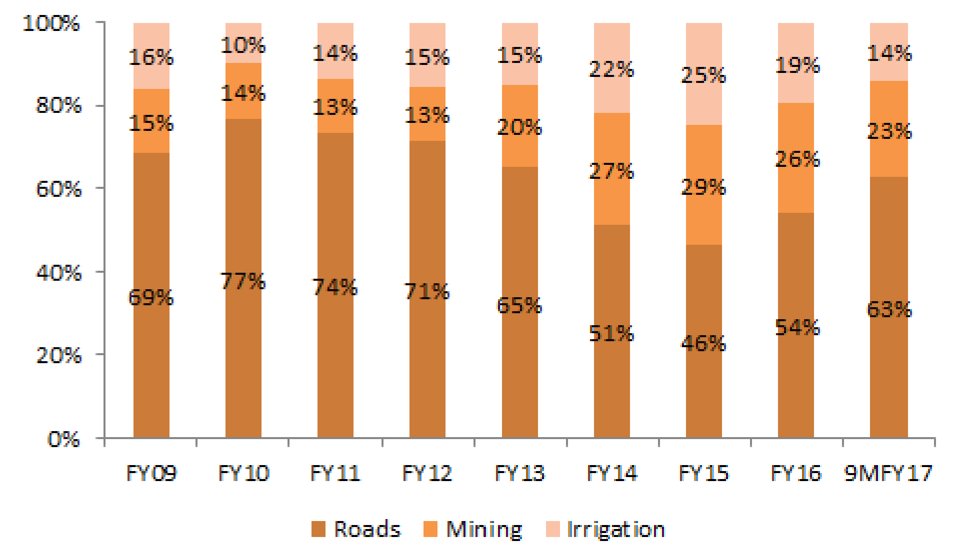


Source: Company, Systematix Institutional Research

Diversified order book, established pedigree to drive 15% revenue CAGR over 3 years

Founded in 1988, SADE is a well-established construction company, with a focus on roads and highways, irrigation and mining segment. It has successfully constructed more than 7,300 lane kms of roads and highways (both national and state), while 2,300 lane kms are under stages of construction. SADE's order book compounded 19% since 2006 to Rs74.8bn in FY16-end. While operations were diversified into mining and irrigation, road projects continue to dominate the order book. The company has worked with reputed clients such as NHAI, Sardar Sarovar Narmada Nigam, Coal India, GIPCL, L&T, HCC among others.

Chart 7: Orderbook: Share of mining & irrigation at 37% in 9MFY16 v/s 27% in FY11



Source: Company, Systematix Institutional Research

Transport EPC – among top 3 road players with proven track record

SADE undertakes rehabilitation, upgradation, widening and strengthening of roads & highways through cash contracts and development of BOT projects. Its strong in-house integrated execution capabilities, state-of-the-art equipments and sub-contracting of road EPC to reputed companies such as KNR Construction and HCC, in the past, has ensured completion of projects on time/ahead of schedule. SADE has also executed national and state highway contracts for reputed clients such as NHAI, KSHIP, DMRC, MSRDC and GSRDC. Besides, it had garnered an early completion bonus of Rs180mn for Dhule-Paleshnar and Rs915mn for Bijapur-Hungund road projects. The major projects completed in the past are:

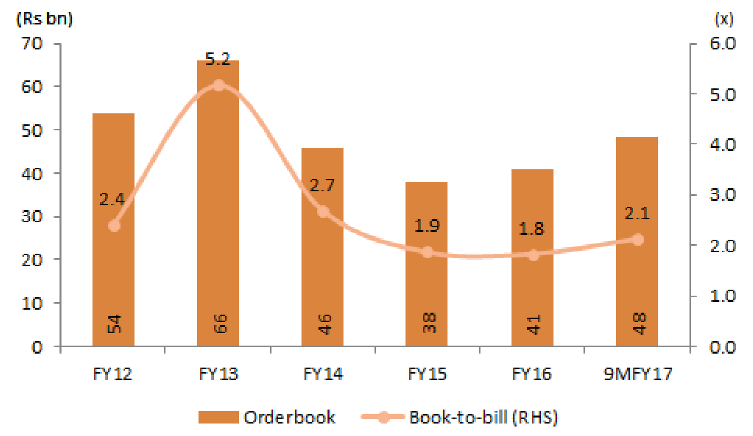
- Widening and strengthening of NH 15 (ADB funded) for 106kms
- Lalsotto Kota road project in Rajasthan for 183kms

Table 1: Major ongoing projects

Stretch	State	Km	Rs mn
Six lane Eastern Peripheral Expressway – Phase 1	Haryana & UP	21.0	7,920
Six lane Eastern Peripheral Expressway – Phase 2	UP	24.5	7,560
Four-laning of Yamunanagar - Saha - Barwala - Panchkula	Haryana	44.6	4,680
Four-laning of Yamunanagar - Saha - Barwala - Panchkula	Haryana	41.8	4,365
Four-laning of Ambala - Kaithal section of NH-65	Haryana	NA	NA
Delhi metro project	Delhi	NA	NA

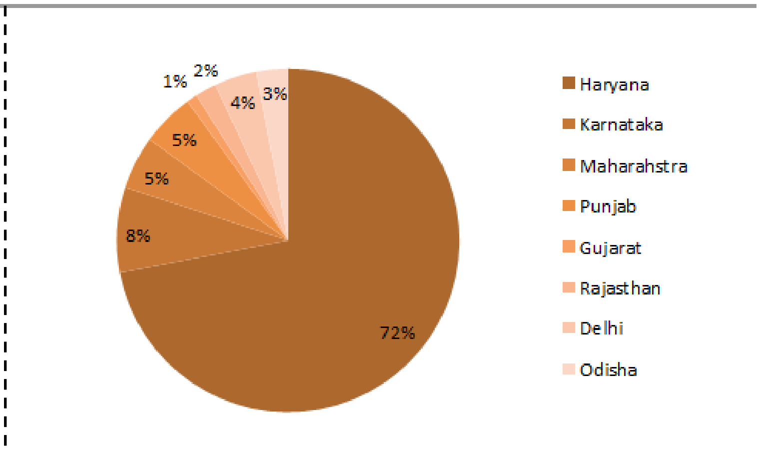
Source: Company

Chart 8: 9MFY17 Transport order book at Rs48bn, 2.1x TTM revenue



Source: Company

Chart 9: State-wise breakup: FY16 transport order book



Source: Company

With receipt of EPC contracts from four HAM projects of SINP, the transport orderbook for SADE is at 48bn. While the average execution period is 2-2.5 years, the orderbook is equally divided between third party EPC contracts and captive projects.

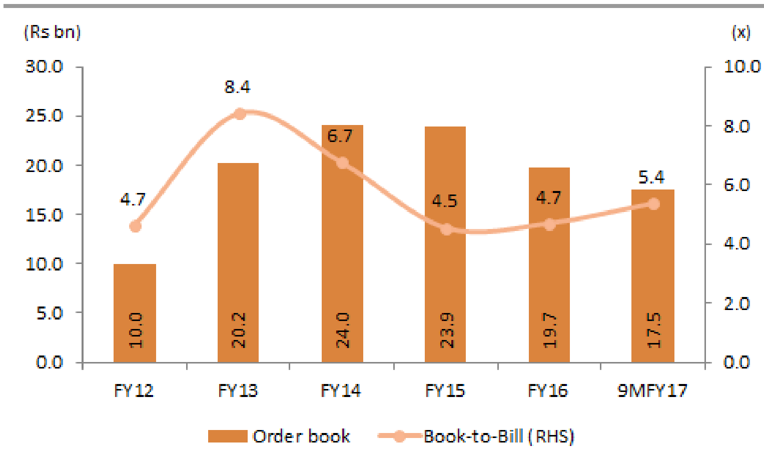
Strong road bid pipeline: For NHAI, the management highlighted that 21 EPC projects worth Rs124bn, 23 HAM projects worth Rs260bnand 2 BOT projects worth Rs28bn are in pipeline in near term.

Mining EPC – enormous opportunity

SADE undertakes extraction of over-burden, rock, coal, lignite and uranium ore for PSUs like GIPCL, GHCL, Bharat Coking Coal Ltd, Northern Mahanadi and Western Coalfield, UCIL among others. Over FY09-16, this segment contributed an average of 14% to the overall standalone revenue. Major completed projects include:

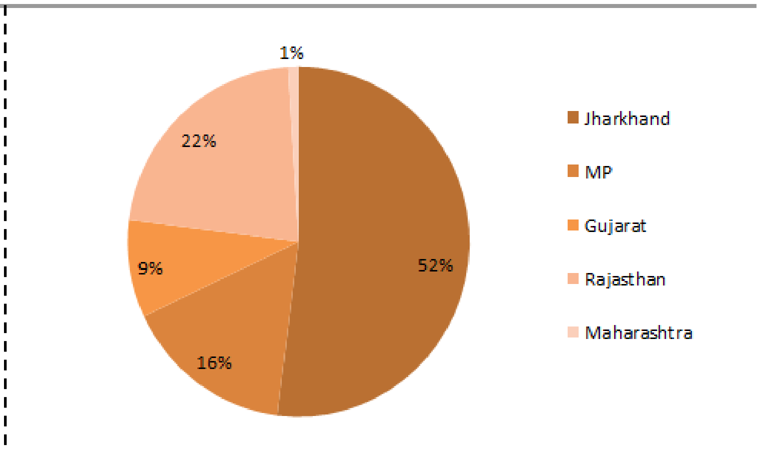
- Removal of over-burden at Khadia OCP
- Removal of all types of material at Junad OCM of Wani area
- Seven-year repeat contract from GIPCL for extraction of over-burden at Mangrol mines

Chart 10: Mining EPC order book at Rs17.5bn, 5.4x TTM revenue



Source: Company

Chart 11: State-wise break-up: FY16 order book



Source: Company

SADE is executing 19 projects, with an order book of Rs17.5bn. The major ongoing projects include:

- Excavation work at Pit B of Jalipa Lignite Mines Barmer, Rajasthan
- Excavation work at Mangrol lignite mines, Gujarat
- Removal of over-burden at Bharat Coking Coal, Dhanbad
- Basantimata-Dahibari patch of Dahibari colliery of C.V. area, Jharkhand
- Excavation of over-burden at specified places of Amlohri OCP of NCL, M.P
- Over-burden and extraction of Uranium ore Banduhurang mine, Jharkhand

For FY17, the management has guided revenue of Rs3.5-3.7bn (down ~14% yoy), based on commencement of execution in Badwar project of Rs4.4bn in 3QFY17 and stoppage of work at BCCL mines due to cenvat credit issue.

Eye on MDO contracts: Apart from small-term EPC contracts, SADE is exploring bids for long-term (20+ years) Mine Development and Operator (MDO) jointly with a technical partner, depending on bid requirements. Other two big ticket long-term projects which SADE envisages to bid are the Gare Palma-III for Chhattisgarh State Power Generation along with a JV partner and the Naini coal block from Singareni Collieries. In all, there are 9 projects in the pipeline, five of which are under MDO and remaining four are medium-term mining EPC contracts of four to five years each, where SADE will bid independently.

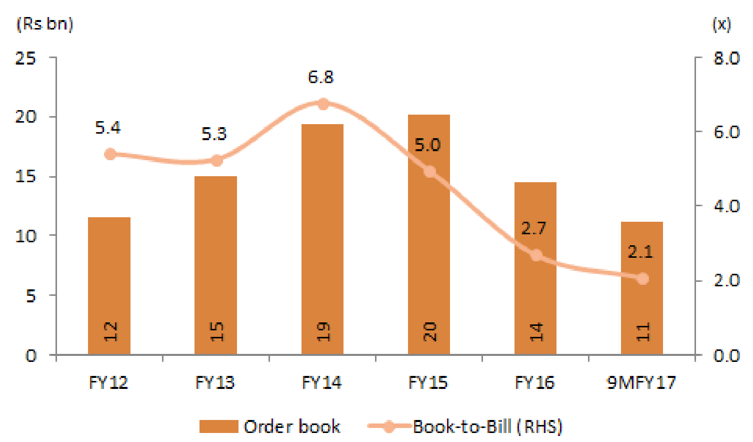
Irrigation EPC – bids selectively based on funding comfort

SADE, under the irrigation segment, engages in the construction of earthen dams, canals, siphons, remodeling and improvement of canals. Over FY09-16, this segment contributed an average 12% to the standalone revenue. Major projects completed include:

- Construction of NMC from 108 to 127 km for Sardar Sarovar Narmada Nigam (SSNNL)
- Canal siphon across river Watrak for SSNNL
- Construction canal earth work, structures, lining and service road to Kachchh Branch Canal

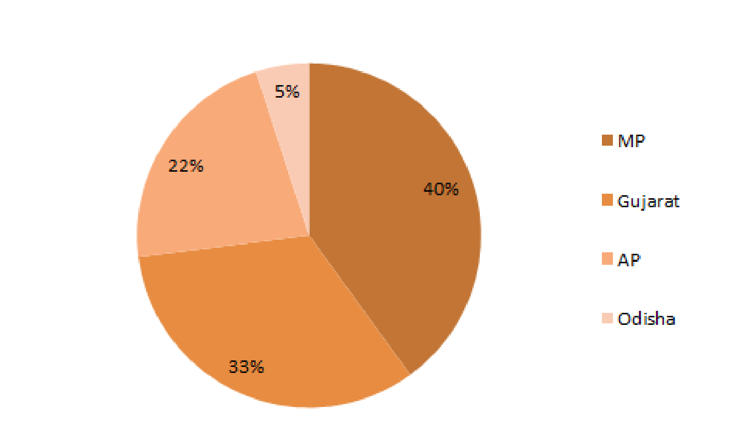
With irrigation projects being awarded by state governments, SADE is selective and bids only for projects that are funded either by the central government agencies or has other clear funding availability.

Chart 12: Irrigation OB at Rs11bn in 9MFY17, 2.1x TTM revenue



Source: Company

Chart 13: State-wise – FY16 order book break-up



Source: Company

Major ongoing projects include:

- Bhauti high level canal, MP
- Omkareshwar right bank lift canal, MP
- Kachchh branch canal Adipur, Gujarat
- HNSS main canal Anantapur district, Andhra Pradesh
- Radhanpur sub branch canal, Gujarat
- Gouravelly right side canal, Andhra Pradesh

Given that few of the above projects have seen a pick-up in execution in 9MFY17 v/s FY16, the management expects FY17 revenue at Rs7.5-8bn (up 40-50% yoy). On the working capital side, funds worth Rs1.5-1.6bn that were blocked over the last six to eight months in projects taken over from GKC JV, have started to flow back to SADE.

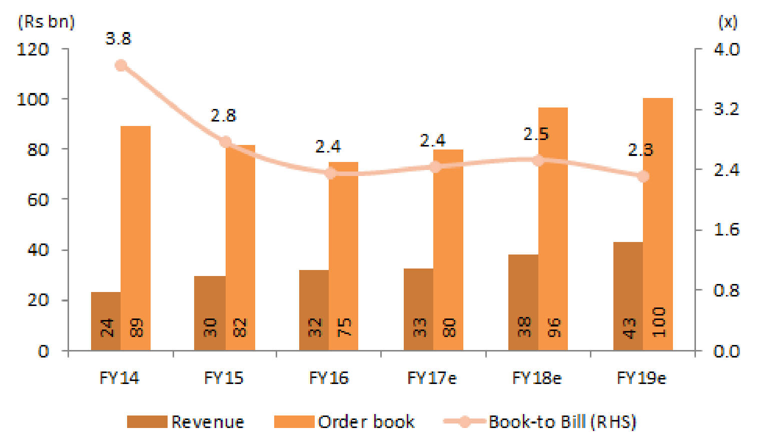
SADE has submitted a bid for Rs4.7bn to the irrigation department, Telangana. Price bid is also submitted for an irrigation project worth Rs22bn (Shrihind feeder irrigation project, Punjab) and tenders for 17 projects worth Rs75bn are to be floated in Gujarat/ MP by March'17.

15% CAGR in standalone revenues over FY17-19e

After 9.7% yoy de-growth in EPC revenue for 1HFY17 to Rs14bn due to heavy monsoon (revenue loss of Rs700mn in 2Q) and Cauvery water issue in Karnataka (revenue loss of Rs350mn) execution picked up in 3QFY17. All five major ongoing road EPC projects and irrigation project contributed materially to 15% yoy revenue growth to Rs8.6bn. The management expects four HAM projects to contribute Rs1.5bn to 4QFY17 revenue and guided for Rs38-40bn revenue for FY18. We estimate 3% yoy revenue growth in FY17e to factor the execution blip in 1HFY17. Order inflow guidance for FY17 remains at Rs50-70bn.

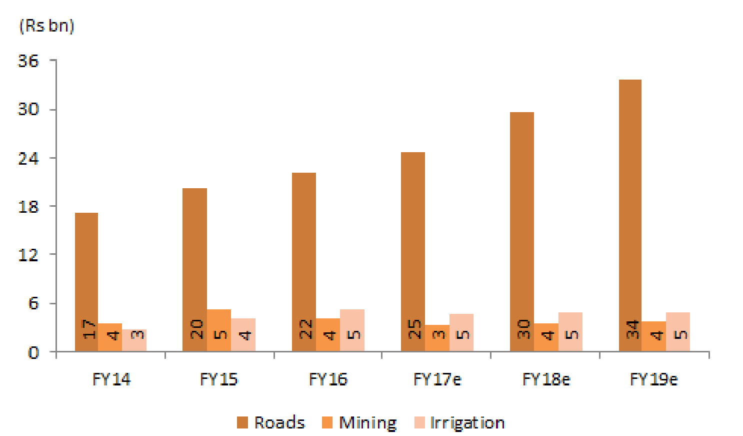
Based on a strong bid pipeline across all three EPC segments, we expect 12% order book CAGR over FY17-19e. Any order wins from MDO would provide further upside to our order book estimates. Given an average execution period of three years, we estimate standalone revenue to post 14% CAGR over FY17-19e.

Chart 14: Revenue CAGR of 15% over FY17-19e



Source: Company, Systematix Institutional Research

Chart 15: Road segment to dominate in revenue mix



Source: Company, Systematix Institutional Research

Increasing traffic and debt refinancing likely to improve BOT cash flows

SADE holds 68% stake in SINP (CMP Rs96, NR) which is the holding company for 12 BOT road assets. Within this, 10 projects are operational, one partially operational and one under construction. The portfolio is sizeable spanning 3,338km, with a total project cost of Rs108bn and is diversified across highly industrialised states. The average residual life is 16 years and with Mysore-Bellary likely to be operational in FY18, there would be no further equity required in these 12 projects.

Table 2: Established BOT portfolio

Particulars	Type	Client	SIPL stake (%)	Project length (kms)	Length (lane kms)	CoD	Residual years	Toll revision month
Operational Projects								
Ahmedabad Ring road	Toll	AUDA	100%	76	305.4	May-08	10.2	September
Aurangabad - Jalna	Toll	MSRDC	100%	66	263.2	Jul-09	12.8	Every 3 year
Nagpur- Seoni	Annuity	NHAI	100%	28	110.9	May-10	10.0	
Dhule - Paleshnar	Toll	NHAI	100%	89	355.2	Jan-12	10.1	April
Maharashtra Border^	User fee	Mah. Govt.	78%	22 CP	22 CP	Apr-12	16.8	April
Rohtak- Panipat	Toll	NHAI	100%	81	323.4	Jan-14	18.4	Every 3 year
Bijapur - Hungund	Toll	NHAI	77%	97	388.9	Apr-12	12.9	April
Hyderabad - Yadgiri	Toll	NHAI	100%	35	139.8	Dec-12	15.8	April
Shreenathji- Udaipur	Toll	NHAI	100%	79	317.2	Apr-16	12.9	April
Bhilwara - Rajasmand	Toll	NHAI	100%	87	349.0	Apr-16	27.9	April
Rohtak - Hissar	Toll	NHAI	100%	99	395.2	Jun-16	18.8	April
Total				**737**			**15 years**	
Under construction								
Mysore - Bellary	Annuity	Karnataka Govt.	100%*	193		Mar-17		

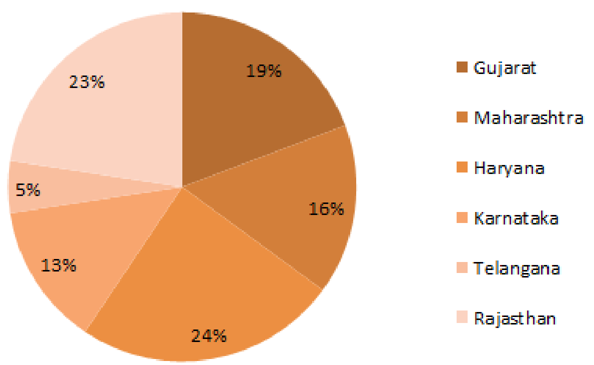
*Source: Company, Systematix Institutional Research ; ^partially operational, *proposed acquisition*

Given that the states are more stable economically and have a Net State Domestic Product growth rate that is higher than that of India, we expect a healthy flow of commercial traffic through these road assets.

Chart 16: Presence in high industrial growth states ensuring healthy traffic

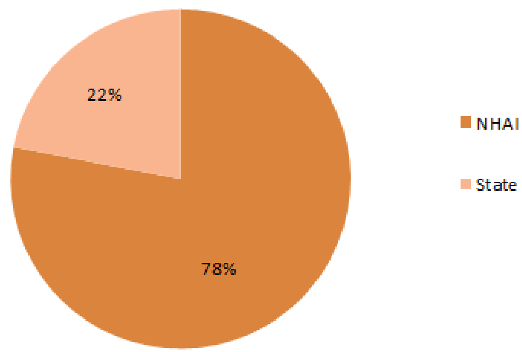
Source: Company

Chart 17: State-wise – lane kms of SINP portfolio



Source: Company

Chart 18: Total project cost Rs108bn – client-wise

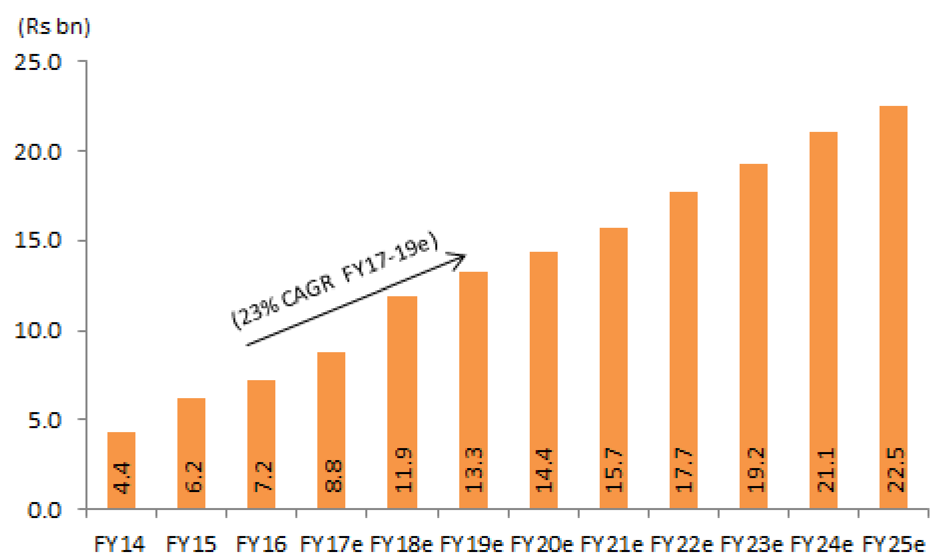


Source: Company

Effective toll collection and toll management systems reduce the leakages. In order to make functioning more efficient at toll plazas, SINP has implemented electronic tag collection (ETC) systems at Hyderabad-Yadgiri, Bijapur-Hungund and Rohtak-Panipat road projects.

Overall toll collection fell 5.4% in Dec'16 vs Oct'16 led by double digit fall in Dhule-Paleshnar, Bijapur-Hungund and Bhilwara–Rajasmand projects hit by demonetization. For 9MFY17 on like to like basis, toll collection on operational projects (excluding Shreenathji-Udaipur, Rajasmand-Bhilwara and Rohak-Hissar) de-grew by 5.9% yoy due to stoppage of toll collection for 23 days in November 2017. SINP has claimed compensation of Rs598mn on loss of toll revenue for all operational projects except MBCP and had received Rs145mn till Jan'17. For MBCP, claim compensation of Rs600mn would be by way of extension of concession period. Management has indicated that for January'17 traffic growth recovered by 2-3% yoy for operational BOT portfolio and has further picked up in February'17.

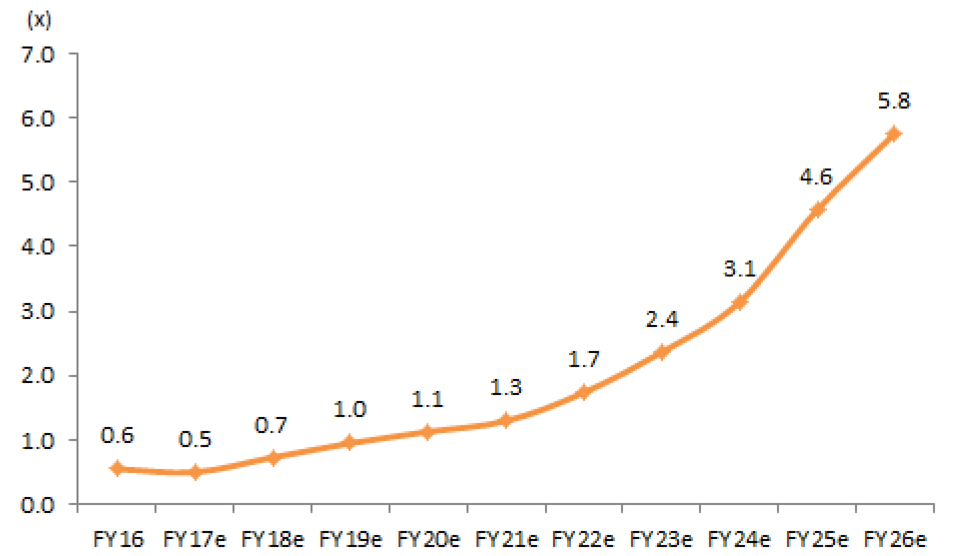
Chart 19: Toll revenue CAGR of 23% over FY17-19e



Source: Company, Systematix Institutional Research

We estimate 19% CAGR in toll revenue over FY17-19e, on commissioning of the Mysore-Bellary project in FY18 and a ramp-up in toll collection in SUTRL, BRTRL and RHTRL, which commenced operations in FY16-17.

Chart 20: Gradual increase in interest coverage ratio on refinancing of 5 road assets



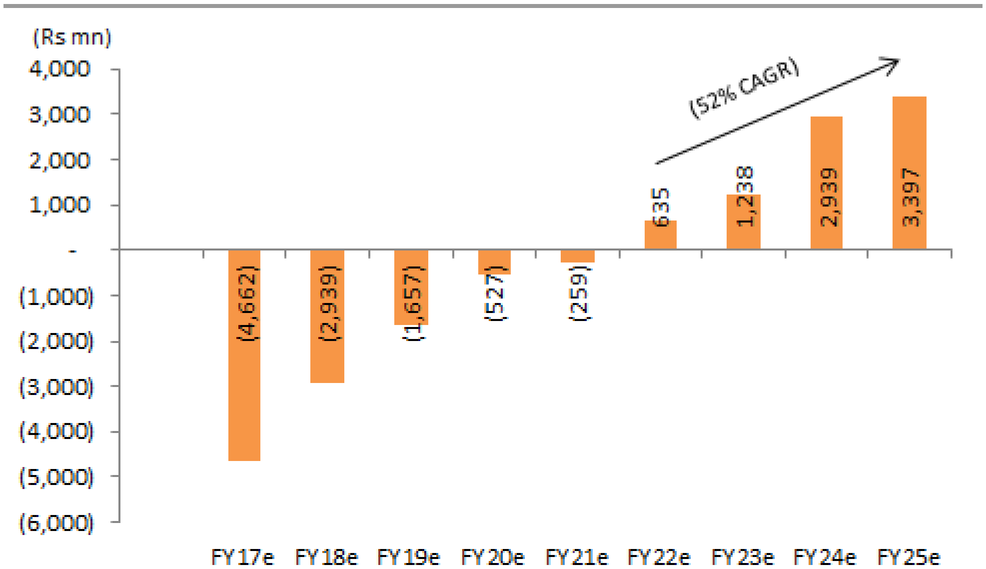
Source: Company, Systematix Institutional Research

SINP has refinanced five operational road projects and is looking to refinance three more projects, which can result in 100-150bps reduction in interest cost along with a cash outflow savings of Rs0.5-0.6bn in all eight projects.

Given a likely refinancing of Rohtak-Panipat, gradual pick-up in traffic in newly-commissioned road BOT assets and healthy toll revenue growth on operational projects, we expect the road portfolio to turn FCFE positive in FY22e and generate 52% CAGR over FY22e-27e.

The total equity investment required for five HAM projects is Rs4.6bn. SINP standalone will contribute Rs3.0bn from internal accruals (O&M income or PMC income during construction phase) while SADE will infuse Rs1.6bn over next two years.

Chart 21: 52% FCFE CAGR over FY22-27e



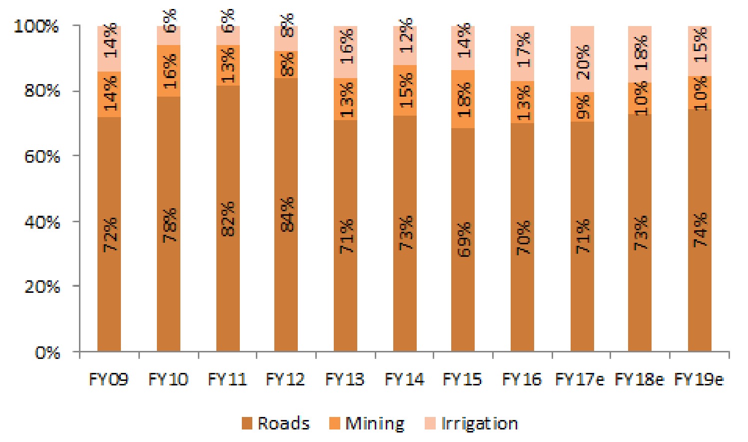
Source: Company, Systematix Institutional Research

SINP is exploring options to exit two of its operational road assets namely Bijapur-Hungund (equity value Rs1.6bn) and Dhule – Paleshnar(equity value Rs3.5bn) to unlock value and invest funds in newer projects mainly its five HAM projects.

Steady operating margins; easing working capital cycle to improve ROCE

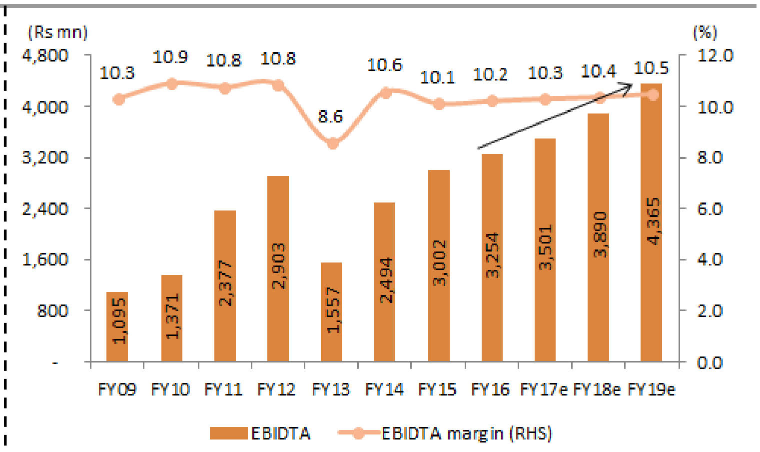
SADE has been able to maintain double digit EBITDA margin of 10-12% over FY06-12, as road segment, a key growth driver, contributed 70-75% to standalone revenue. Margins declined to 8.6% in FY13 on negative operating leverage due to early completion of old orders and time taken to ramp up execution on new orders. However, OPM bounced back to 10.3% in FY14-16. This expansion can be attributed to a higher revenue from mining orders (better margin at 18-20% compared to irrigation), combined with a pick-up in execution of road projects.

Chart 22: Rising share of roads to overall revenue



Source: Company, Systematix Institutional Research

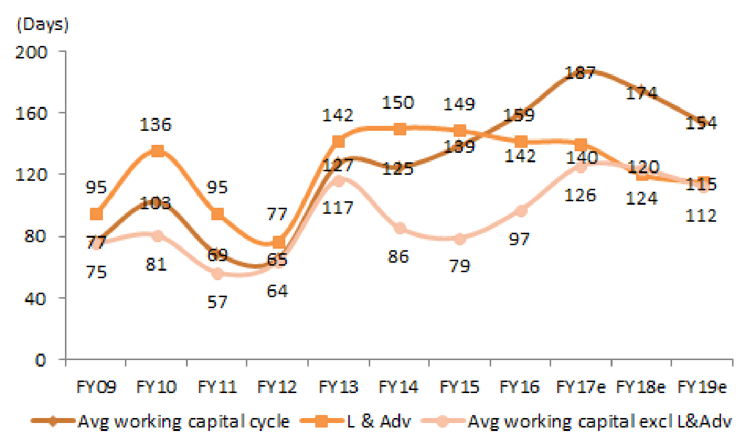
Chart 23: EBITDA CAGR at 12% over FY17e-19e



Source: Company, Systematix Institutional Research

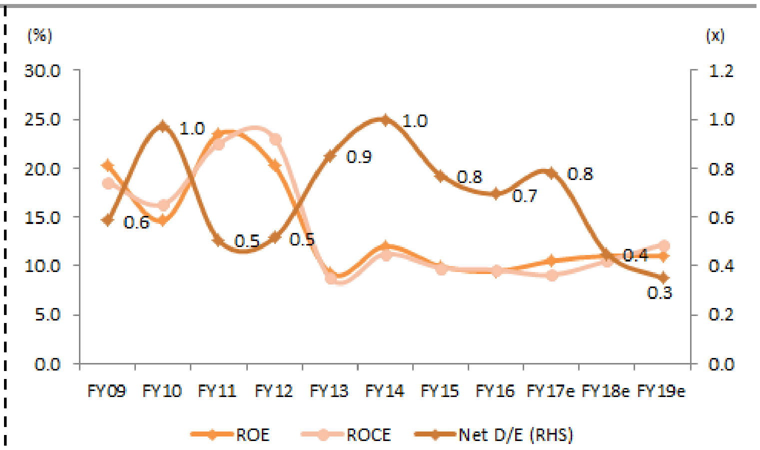
We estimate EBITDA margin to be at 10.8% over FY17-19e given 1) pick-up in execution of ongoing road EPC contracts in FY17 to offset higher irrigation revenue (low-margin) and 2) contribution from better-margin HAM contracts to transport revenue from FY18e onwards. The management expects EBITDA margin to be ~10.75-11% in FY17.

Chart 24: Working capital ex-L&Adv to stabilise in FY17-19e



Source: Company, Systematix Institutional Research

Chart 25: Repayment of loans from SIPL to improve net D/E



Source: Company, Systematix Institutional Research

The working capital cycle has increased from an average of 78 days over FY09-12 to 138 over FY13-16 led by 1) extension of loans & advances to SINP, which in turn invested as sub-debt in road SPVs, 2) Rs1.5-1.6bn blocked in GKC irrigation projects since December 2015 and 3) ~Rs1bn blocked in DMRC metro order.

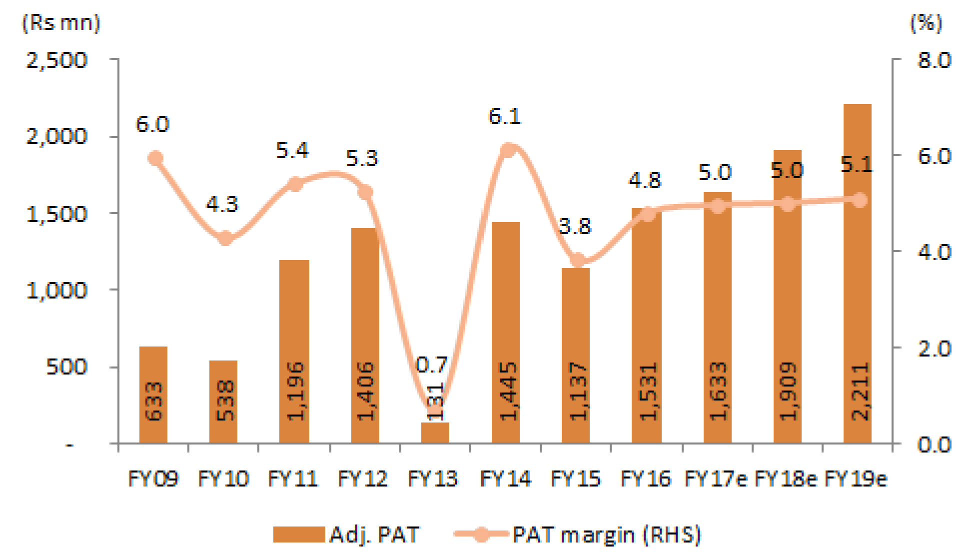
Given that operational road SPVs have started to generate positive cash flows, they have repaid the sub-debt to SIPL, which in turn has started to repay advances given by SADE (Rs500mn repaid between March 2016 and June 2016). SADE expects to recover at least Rs1bn in FY17 from irrigation projects taken over from GKC.

In near term, stuck receivables in ongoing irrigation and mining projects, repayment of NHAI mobilisation advances (Rs1.1bn repaid, to pay Rs1.8bn in 4Q17) and financial support to SIPL will keep the gearing high at 0.8x in FY17e.

We estimate that release of milestone based payment from NHAI and repayment of loan from SIPL should alleviate average working capital cycle from peak of 159 days and reduce net gearing to 0.3x in FY19e. Ease of working capital, lower capex requirement (incurred Rs700-750mn in FY16) and a gradual improvement in EBITDA margin can improve RoCE from 9.1% in FY17 to 12.2% in FY19e.

Based on the utilisation of commercial paper and bank loan mix, the average cost of debt has come down to 8.25-8.5%, compared to 10.25% earlier. Given an ease of working capital coupled with a lower cost of debt, we estimate interest expenses to reduce by 17% CAGR and PAT to improve by 14% CAGR to Rs2.2bn over FY17-19e.

Chart 26: PAT CAGR of 16% over FY17-19e



Source: Company, Systematix Institutional Research

Key management team

Vishnubhai Patel (Chairman Emeritus)

- He is promoter of Sadbhav Engineering and has 40 years of experience in construction business.
- Under his guidance the company has successfully completed various projects displaying high quality standards.

Shashin Patel (Chairman and Managing Director)

- A MBA with 17 years experience
- Associated with the Company since 2000. Responsible for overall management including strategic management decisions of the company.

Vasistha Patel (Whole time Director)

- A Civil Engineer working with 15+ years of experience in construction industry.
- Actively participates in bidding process and has track record for completing various road projects ahead of time.

Nitin Patel (Executive Director & CFO)

- A Chartered Accountant associated with the company since 1999 and participates in bidding process and execution of road projects.
- Overall functioning of the entire corporate affairs of the Company including liaising with banks and financial institutions for obtaining funds.

Vikram Patel (Whole time Director)

- He is associated with the Company since Septembet'2012.
- He has more than 22 years of experience in construction industry and activelt participates in execution of various road projects.

Key risks

1) Delay in awarding of projects can postpone the order inflows, leading to lower revenue compared to our estimate.
2) Lower-than-expected repayment of advances by SINP can result in elevated working capital cycle and resultant higher interest cost.

Valuation and view

SADE's premium valuation compared to peers can largely be attributed to its robust execution efficiency, stable margins, strong order book growth and low risk from operational BOT projects and nearing completion of under-construction projects.

We initiate coverage on SADE with a **Buy** rating and a SOTP-based target price of Rs324. We value the EPC business at Rs186/share, 15x FY19 earnings and its 69% stake in SINP BOT business at Rs139/share.

Table 3: SOTP Valuation Table

	Valuation basis	Multiple	Value (Rs mn)	Value / share (Rs)
Sadbhav Engineering				
A) EPC Construction	P/E	15x PE FY19e	33,158	194
B) Value of SADE stake @ 69% in SINP			30,292	
(-)20% holding co disc			6 058	
SADE share in SINP			24,234	141
Fair Value (A +B)				**335**
CMP				310
Upside (%)				**8**

Sadbhav Infraprojects (SINP) Road BOT projects

Project	Basis	Value (Rs mn)	Value/ share (Rs)
Ahmedabad Ring Road	NPV @ 14% CoE , FY19	3,971	11
Aurangabad- Jalna	NPV @ 14% CoE , FY19	2,748	8
Nagpur-Seoni	P/BV @ 1x	598	2
Dhule-Palasner	NPV @ 14% CoE , FY19	4,248	12
MBCP	NPV @ 14% CoE , FY19	7,220	20
Rohtak Panipat	NPV @ 14% CoE , FY19	1,299	4
Hyderabad-Yadgiri	NPV @ 14% CoE , FY19	3,210	9
Bijapur- Hungund	NPV @ 14% CoE , FY19	3,288	9
Shreenathji-Udaipur	NPV @ 14% CoE , FY19	7,313	21
Rajsamand-Bhilwara	NPV @ 14% CoE , FY19	5,147	15
Rohtak-Hissar	NPV @ 14% CoE , FY19	(248)	(1)
Mysore-Bellary Highway	NPV @ 14% CoE , FY19	494	1
5 HAM projects	P/BV @ 1x	4,614	13
Total SIPL value		**43,902**	**125**

Source: Systematix Institutional Research

KNR Constructions

27 March, 2017

Road specialist; posied for growth

COMPANY UPDATE

Sector: Construction **Rating: Hold**

CMP: Rs181 **Target Price: Rs185**

KNR Constructions Ltd (KNR), a pure road and highway EPC player, has demonstrated superior track record of on-time execution led by management's active involvement in bidding and project implementation. This along with prudent bidding strategy enabled KNR to win lucrative EPC road projects in the past involving complex strucures (low competition, better margins). A strong foothold in south India, large base of under-utilised construction equipments and strong FY16 orderbook of Rs35bn led 77% yoy growth in 9MFY17 revenue to Rs10.5bn with an OPM of 13% (mix of in-house and subcontracted orders).The 9MFY17 order accretion is at Rs18bn and the order book stands at Rs42.4bn (3.2x TTM sales). KNR expects to win order/s worth Rs10bn by Jun'17, has bid for two HAM projects of (Rs8-10bn) in Karnataka and for HAM and EPC projects in Maharashtra. Going forward, we expect moderate execution of current order book, led by delays in land acquisition and clearances. We expect KNR to record revenue/PBT CAGR of 14%/10% over FY17-19e led by an improvement in asset turnover to 2.1x (current 1.6x) and stable working capital. The RoCE will expand to 14.9% in FY19e vs 13.1% in FY16. We have a Hold rating with a SOTP-based target price of Rs185/share.

Stock Info

Sensex/Nifty	29,332/ 9,086
Bloomberg	KNRC IN
Equity shares (mn)	140.6
52-wk High/Low	Rs202/ 85
Face value	Rs2
M-Cap	Rs26bn/ $0.4bn
3-m Avg volume	$0.4mn

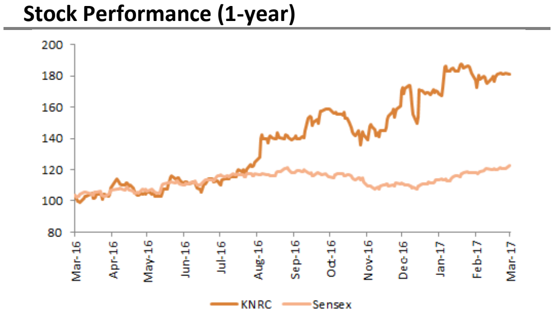
Financial Snapshot (Rs mn)

Y/E Mar	FY17e	FY18e	FY19e
Sales	13,790	15,782	17,975
EBITDA	1,930	2,207	2,508
PAT	1,285	1,421	1,426
EPS (Rs)	9.9	10.1	10.1
Core PE (x)	17.2	16.9	16.6
EV/EBITDA (x)	13.8	12.2	10.7
P/BV (x)	3.0	2.6	2.3
RoE (%)	17.7	15.5	13.5
RoCE (%)	14.8	14.4	14.9
Dividend yield (%)	1.0	1.1	1.1
Net gearing (x)	0.2	0.2	0.1

Shareholding pattern (%)

	Dec '16	Sept '16	Jun '16
Promoter	58.1	58.1	60.8
–Pledged	-	-	-
FII	4.4	5.0	4.0
DII	26.8	26.4	23.8
Others	10.6	10.5	11.4

Stock Performance (1-year)



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Large order book of Rs42bn provides strong growth visbility

KNRC's order accretion for 9MFY17 is at Rs18bn, with no new order wins in 3QFY17. The unexecuted order book is at Rs42.4bn (3.2x TTM revenue). While execution has commenced on the Pollachi-Coimbatore road project in January 2017, the appointed date on Hubli-Hospet is delayed by a month due to unavailability of land (75% available). Management expects to commence execution on the Hubli project by March 2017 to avail the section 80 IA benefit. This apart, ~80% of execution in large EPC projects, namely Madurai and Thiruvananthapuram bypass, would be completed by December 2017. To offset the slowdown in execution, KNRC expects to win order/s worth Rs10bn by June 2017. Incrementally, with new road projects coming up on HAM basis, KNRC has bid for two HAM projects of ~Rs8-10bn in Karnataka and plans to bid for two HAM and four to five EPC (Rs2.5-4bn) road projects in Maharashtra. As per management, HAM bidders are restricted to six.

Proven execution track record, limited BOT exposure

With over 20 years of experience in project execution, KNR has successfully executed 5,888 lane kms of road projects across 12 states in India. It is among the focused road EPC players where the management is closely involved in the business at every level – from selecting bids, mobilisation of equipments to choice of materials. This has translated into faster decision-making, timely completion of projects, sometimes even early and enabling KNR to avail the early completion bonus (Rs546mn in 2012 for Bijapur-Hungund). A disciplined bidding approach helped KNR to maintain consistence performance even at the time when the sector faced a downturn (FY12-14). Over FY08-15, KNR has taken only four BOT projects, 1 toll - under construction, two annuity projects (securitised) , 1 toll - operational, totaling to 778kms in the states of Telangana, Karnataka, Kerala and Bihar and plans to exit most of them.Going ahead it plans to maintain its focus on road EPC space given the mega opportunity.

Steady profitability, healthy balance sheet to expand return ratios

KNR's OPM in the range of 14-17% and PAT margin of 7-8% over FY11-16 has been the best in the industry in spite of a tough operating environment led by 1) minimal sub-contracting, 2) procuring aggregates from captive quarries and management's active involvement in the selection of major raw materials, 3) prudent bidding for projects, mainly in South India where KNR has a strong foothold and 4) availment of early completion bonus. Going forward, with sub-contracting of four orders (below the size of Rs5bn each) worth Rs9.8bn from the current order book, we estimate the blended EBITDA margin to be at 14.0% in FY18e/19e. With capex of Rs2.5bn on new order wins and increasing working capital cycle in FY17 and FY18, we expect free cash flow of Rs136mn over FY19e and improvement in ROCE to 14.9% in FY19 vs 13.1% in FY15. We expect 14%/10% Revenue/PBT CAGR over FY17-19e and improvement in asset turnover to 2.1x in FY19e vs 1.6x in FY16.

Investors are advised to refer through disclosures made at the end of the research report.

FINANCIALS (STANDALONE)

Profit & Loss Statement

YE: Mar (Rs mn)	FY15	FY16	FY17e	FY18e	FY19e
Net revenues	8,760	8,851	13,790	15,782	17,975
Revenue growth (%)	4.7	1.0	55.8	14.4	13.9
- Op. expenses	7,500	7,470	11,860	13,576	15,467
EBIDTA	1,260	1,381	1,930	2,207	2,508
EBITDA margins (%)	14.4	15.6	14.0	14.0	14.0
- Interest expenses	122	131	252	262	287
- Depreciation	540	425	595	679	725
+ Other income	126	413	485	405	405
PBT	723	1,237	1,569	1,671	1,902
- Tax	(7)	146	175	251	475
Effective tax rate (%)	(1.0)	11.8	12.0	15.0	25.0
Adjusted PAT	730	1,091	1,394	1,421	1,426
+/- Extraordinary items	-	(554)	109	-	-
+/- Minority interest	-	-	-	-	-
Reported PAT	730	1,645	1,285	1,421	1,426
Adj. FDEPS (Rs/share)	5.2	7.8	9.9	10.1	10.1

Source: Company, Systematix Institutional Research

Balance Sheet

YE: Mar (Rs mn)	FY15	FY16	FY17e	FY18e	FY19e
Share capital	281	281	281	281	281
Reserves & Surplus	5,411	6,988	8,214	9,567	10,926
Networth	5,692	7,270	8,495	9,848	11,207
Minority interest	-	-	-	-	-
Total Debt	963	1,222	1,656	1,717	1,707
Def. tax liab. (net)	(239)	(276)	(276)	(276)	(276)
Capital employed	**6,416**	**8,216**	**9,876**	**11,289**	**12,638**
Net Fixed assets	2,269	2,468	2,923	3,244	3,119
Investments	315	434	434	434	434
- of which liquid	87	79	79	79	79
Net Working capital	3,675	5,153	6,157	7,494	8,909
Cash and bank balance	157	162	362	117	175
Capital deployed	**6,416**	**8,216**	**9,876**	**11,289**	**12,638**
Net debt	806	1,060	1,294	1,600	1,532
WC (days)	127	182	150	158	167
Book value (Rs/sh)	202	258	302	350	398

Source: Company, Systematix Institutional Research

Cash Flow

YE: Mar (Rs mn)	FY15	FY16	FY17e	FY18e	FY19e
PAT	730	1,091	1,394	1,421	1,426
+ Non cash items	419	389	595	679	725
Cash profit	1,149	1,479	1,989	2,099	2,151
- Incr/(Decr) in WC	1,231	1,478	1,005	1,337	1,415
Operating cash flow	(81)	1	984	762	736
- Capex	169	624	1,050	1,000	600
Free cash flow	(250)	(623)	(66)	(238)	136
- Dividend	34	34	59	68	68
+ Equity raised	-	-	-	-	-
+ Debt raised	382	259	434	61	(10)
- Investments	(85)	119	(0)	-	-
- Misc. items	139	(522)	109	-	-
Net cash flow	44	5	201	(245)	58
+ Opening cash	112	156	161	362	117
Closing cash	156	161	362	117	175

Source: Company, Systematix Institutional Research

Ratios

YE: Mar	FY15	FY16	FY17e	FY18e	FY19e
Core P/E (x)	34.8	23.0	17.2	16.9	16.6
P/E (x)	34.8	23.3	18.3	17.9	17.8
P/B (x)	4.5	3.5	3.0	2.6	2.3
EV/EBITDA (x)	20.8	19.1	13.8	12.2	10.7
RoE (%)	13.5	16.8	17.7	15.5	13.5
RoCE (%)	12.0	13.1	14.8	14.4	14.9
Fixed Asset turnover (x)	1.6	1.5	2.1	2.1	2.1
Dividend yield (%)	0.6	0.6	1.0	1.1	1.1
Dividend payout (%)	3.9	1.7	3.8	4.0	3.9
Interest exp./Sales	1.4	1.5	1.8	1.7	1.6
Debtors (days)	74	50	60	65	70
Revenue growth (%)	4.7	1.0	55.8	14.4	13.9
PAT growth (%)	19.8	49.3	27.8	1.9	0.4
EBITDA growth (%)	(1.6)	9.6	39.8	14.3	13.7
EPS growth (%)	19.8	49.3	27.8	1.9	0.4

Source: Company, Systematix Institutional Research

IRB Infrastructure

27 March, 2017

Largest road BOT asset developer

NOT RATED

Sector: Construction	**Rating: NR**
CMP: Rs235	**Target Price: NA**

Stock Info

Sensex/Nifty	29,332/ 9,086
Bloomberg	IRB IN
Equity shares (mn)	257
52-wk High/Low	Rs266/ 177
Face value	Rs10
M-Cap	Rs82bn/ $1.3bn
3-m Avg volume	$6.3mn

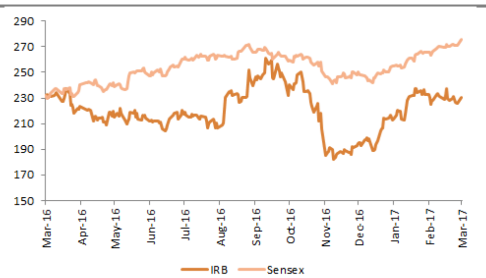
Financial Snapshot (Rs mn)

Y/E Mar	FY14	FY15	FY16
Sales	37,319	38,475	51,302
EBITDA	17,537	22,117	26,606
PAT	4,591	5,429	6,358
EPS (Rs)	13.8	15.4	18.1
PE (x)	16.9	15.1	12.9
EV/EBITDA (x)	9.9	8.7	8.1
P/BV (x)	2.2	1.9	1.7
RoE (%)	13.5	13.7	13.8
RoCE (%)	9.6	9.5	9.8
Dividend yield (%)	2.1	0.8	1.7
Net gearing (x)	2.7	2.5	2.8

Shareholding pattern (%)

	Dec '16	Sep '16	Jun '16
Promoter	57.4	57.4	57.4
–Pledged	-	-	-
FII	27.8	29.3	28.8
DII	7.7	6.6	7.1
Others	7.1	6.7	6.7

Stock Performance (1-year)



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IRB Infrastructure (IRB) is one of the largest pure-play toll operator, with a portfolio of 22 projects spread across 11,368 lane km, of which 68% is spread across Maharashtra, Gujarat and Rajasthan. IRB, through its integrated business model, undertakes execution of EPC order book of Rs96bn of its in-house BOT projects and O&M of operational BOT projects (order book of Rs17bn). Lower competitive intensity and selective projects under BOT toll mode places IRB in a sweet spot to win these projects. To deleverage existing balance sheet, having net D/E of 2.8x and free-up capital from operational projects, IRB has filed for InvIT with Sebi. It expects to raise Rs43bn through a primary issue of portfolio of six assets in addition to an offer-for-sale. The equity required for FY18 and FY19 for under-implementation and newer projects is at Rs18-19bn, which the company expects to meet from cash flow from operations and InvIT.

Largest BOT toll projects operator with integrated in-house operations

IRB's large portfolio of 22 BOT toll assets (14 operational, five under-construction and three recently-won) comprises of 11,368 lane km, with strong footprints in Gujarat, Maharashtra and Rajasthan. While operational projects reported 19% revenue CAGR over FY13-16, two large projects -- Mumbai-Pune (206km) and Surat-Dahisar (239km) contributed 50% to 3QFY17 toll revenue. With a residual concession period of less than five years for both latter projects, an increase in revenue trajectory from other large projects such as AV Expressway, Tumkur-Chitradurga and Bharuch-Surat becomes significant. Vertically integrated operations facilitate works related to the entire BOT value chain, from traffic studies, in-house construction and O&M of all operational BOT projects. EPC order book (excl. Rs17.4bn O&M) of Rs103bn (2.7x TTM revenue) comprises of five in-house under-construction projects and is heavily dependent on the addition of new assets for earnings growth, once the current portfolio becomes operational. The management has guided for 10-12% yoy growth in EPC revenue in FY18-19.

InvIT – new tool to monetise projects

IRB has filed an InvIT DRHP with Sebi and expects to raise ~Rs43bn via primary issuance apart from an offer-for-sale by sponsor companies through pooling six of its operational projects with a residual life of 5-21 years. As of Mar'16, the portfolio generated Rs10bn revenue (~80% commercial traffic) and invested Rs11bn equity. An estimated amount of Rs42bn from net proceeds will be invested in project SPVs by way of a debt issue, which in turn will prepay/partial repay Rs47bn external debt, unsecured loans & advances and Rs7bn sub-debt. The management values the portfolio at Rs80bn EV (9.6x FY16 EBITDA) and Rs30bn equity (2.7x invested equity). This factors 1) aggressive traffic assumptions of 6.5-7.1%+ over the life of assets (except Surat-Dahisar), along with 5.5% inflation linked toll hike and 2) extension of concession period for select projects (led by traffic shortfall).

Healthy financials, success of InvIT to aid in deleveraging

IRB's consolidated revenue posted 16% CAGR over FY11-16, led by 21% growth in BOT toll revenue on 2x increase in commissioning of assets. EBITDA clocked 20% CAGR over the same period, while a higher share of better OPM BOT projects in the revenue mix led to an increase in OPM to 51.9% in FY16 vs 44.6% in FY11. Operation of newer BOT projects led to an increase in net D/E to 2.8x in FY16, from 1.4x in FY11. Higher outgo of interest and depreciation expense on commissioning of these BOT projects led to 7% CAGR in adjusted PAT to Rs6.4bn over FY11-16. IRB won three new projects of ~330km in Rajasthan, thus meeting the FY17 target of 350-400km. The equity needed for FY18 and FY19 in under-implementation projects is at Rs18-19bn, including two recently-won projects in Rajasthan, which would be funded through cash flows generated from operational projects and success of InvIT.

FINANCIALS (CONSOLIDATED)

Profit & Loss Statement

YE: Mar (Rs mn)	FY12	FY13	FY14	FY15	FY16
Net revenues	31,330	36,872	37,319	38,475	51,302
Revenue growth (%)	28.5	17.7	1.2	3.1	33.3
- Op. expenses	17,637	20,540	19,782	16,358	24,696
EBIDTA	13,694	16,333	17,537	22,117	26,606
EBITDA margins (%)	43.7	44.3	47.0	57.5	51.9
- Interest expenses	5,464	6,153	7,562	9,312	10,633
- Depreciation	2,970	4,415	4,771	7,071	8,533
+ Other income	1,252	1,301	1,214	1,130	1,239
PBT	6,512	7,066	6,419	6,864	8,679
- Tax	1,552	1,530	1,823	1,441	2,316
Effective tax rate (%)	23.8	21.7	28.4	21.0	26.7
Adjusted PAT	4,960	5,536	4,596	5,424	6,363
+/- Extraordinary items	-	-	-	-	-
+/- Minority interest	0	(31)	5	(6)	4
Reported PAT	4,960	5,567	4,591	5,429	6,358
Adj. FDEPS (Rs/share)	14.9	16.7	13.8	15.4	18.1

Source: Company, Systematix Institutional Research

Balance Sheet

YE: Mar (Rs mn)	FY12	FY13	FY14	FY15	FY16
Share capital	3,324	3,324	3,324	3,515	3,515
Reserves & Surplus	25,243	29,232	32,283	40,094	44,758
Networth	28,566	32,556	35,607	43,609	48,272
Minority interest	1,123	1,092	356	351	355
Total Debt	70,722	87,761	110,841	125,762	149,807
Def. tax liab. (net)	259	259	224	194	156
Capital employed	**100,670**	**120,575**	**146,672**	**169,564**	**198,235**
Net Fixed assets	55,542	55,088	85,544	317,638	350,373
CWIP + Int assets u/dev	24,452	49,160	44,867	48,353	41,314
Investments	140	620	145	88	68
Net Working capital	2,328	2,089	1,567	(211,986)	(208,759)
Cash and bank balance	18,208	13,618	14,549	15,472	15,239
Capital deployed	**100,670**	**120,575**	**146,672**	**169,564**	**198,235**
Net debt	52,514	74,142	96,292	110,290	134,567
WC (days)	27	21	15	27	24
Book value (Rs/sh)	86	98	107	124	137

Source: Company, Systematix Institutional Research

Cash Flow

YE: Mar (Rs mn)	FY12	FY13	FY14	FY15	FY16
PAT	4,960	5,567	4,591	5,429	6,358
+ Non cash items	2,997	4,415	4,655	7,097	8,512
Cash profit	7,957	9,981	9,247	12,526	14,871
- Incr/(Decr) in WC	1,878	(239)	(522)	(213,554)	3,228
Operating cash flow	6,079	10,221	9,768	226,080	11,643
- Capex	24,269	28,669	30,934	242,651	34,229
Free cash flow	(18,190)	(18,448)	(21,166)	(16,571)	(22,586)
- Dividend	720	1,577	1,940	777	1,645
+ Equity raised	(0)	0	-	191	-
+ Debt raised	24,480	17,039	23,080	14,921	24,045
+ Minority interest	227	(31)	(736)	(6)	4
- Investments	(411)	481	(475)	(57)	(20)
- Misc. items	(0)	0	(400)	(3,159)	50
Net cash flow	6,208	(3,498)	113	974	(211)
+ Opening cash	12,000	18,208	14,710	14,823	15,798
Closing cash	18,208	13,618	14,549	15,472	15,239

Source: Company, Systematix Institutional Research

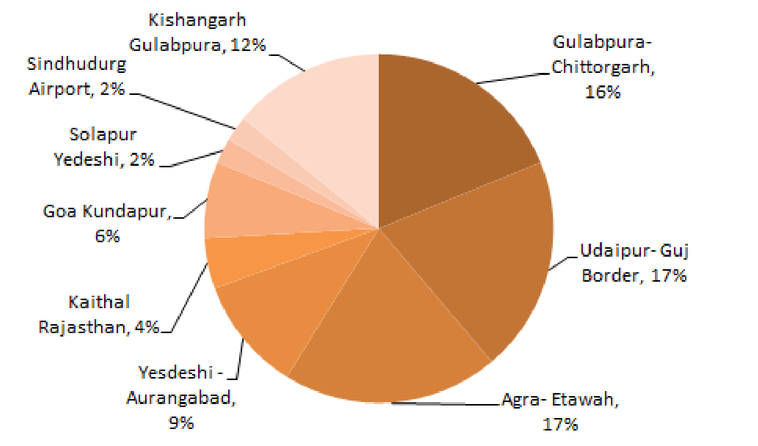
Ratios

YE: Mar	FY12	FY13	FY14	FY15	FY16
P/E (x)	15.7	14.0	16.9	15.1	12.9
P/B (x)	2.7	2.4	2.2	1.9	1.7
EV/EBITDA (x)	9.5	9.2	9.9	8.7	8.1
RoE (%)	18.8	18.2	13.5	13.7	13.8
RoCE (%)	12.6	10.9	9.6	9.5	9.8
Fixed Asset turnover (x)	0.6	0.5	0.4	0.2	0.1
Dividend yield (%)	0.8	1.7	2.1	0.8	1.7
Dividend payout (%)	12.1	24.0	36.1	12.3	22.1
Interest exp./Sales	17.4	16.7	20.3	24.2	20.7
Debtors (days)	2	1	1	0	7
Revenue growth (%)	28.5	17.7	1.2	3.1	33.3
PAT growth (%)	9.6	12.2	(17.5)	18.2	17.1
EBITDA growth (%)	25.8	19.3	7.4	26.1	20.3
EPS growth (%)	9.6	12.2	(17.5)	11.8	17.1
Net gearing (%)	1.8	2.2	2.7	2.5	2.8

Source: Company, Systematix Institutional Research

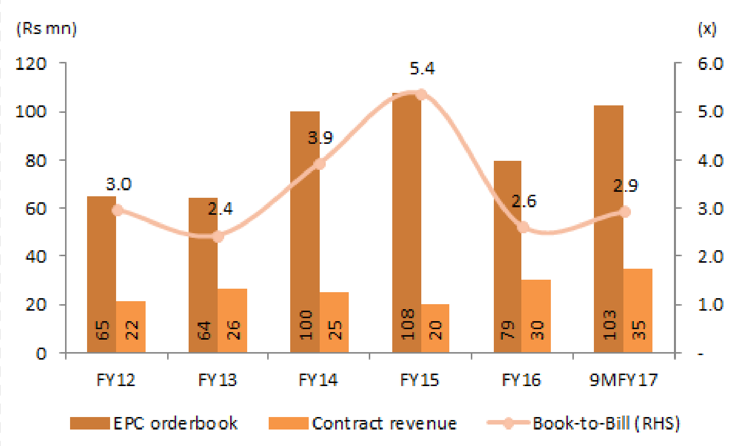
Charting the story

Chart 1: Order book break-up – Rs103bn (excl. O&M at Rs17.5bn)



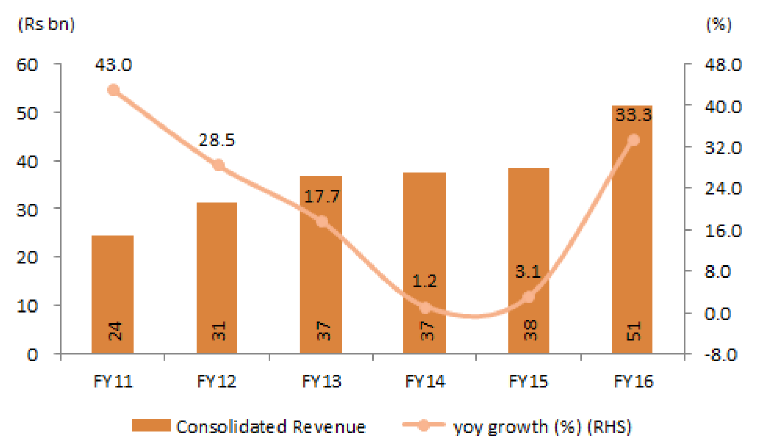
Source: Company, Systematix Institutional Research

Chart 2: Steady book-to-bill ratio at 2.9x



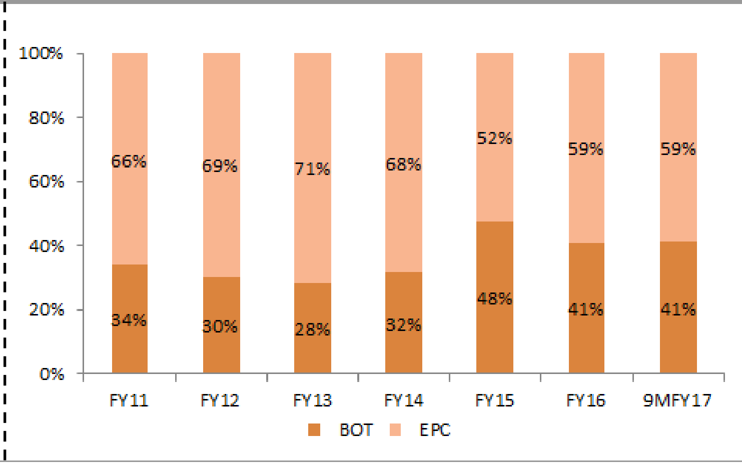
Source: Company, Systematix Institutional Research

Chart 3: Five-year revenue CAGR at 16%



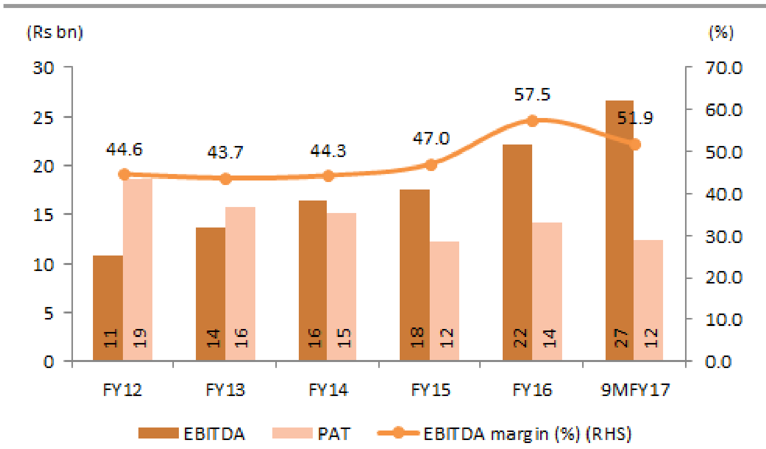
Source: Company, Systematix Institutional Research

Chart 4: Rising share of BOT toll in revenue mix



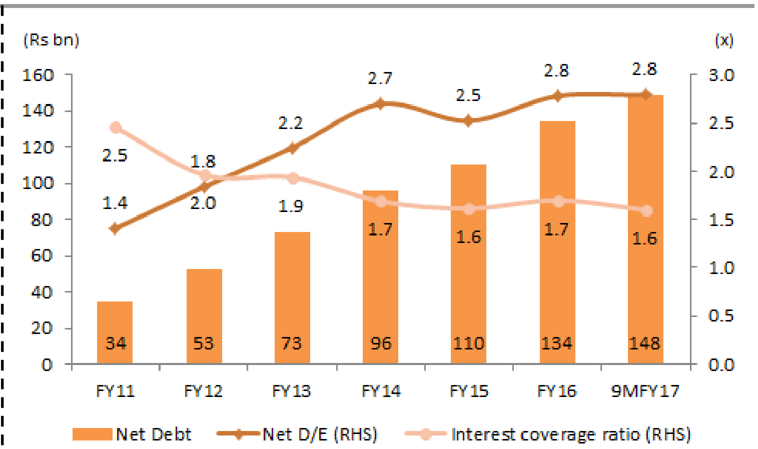
Source: Company, Systematix Institutional Research

Chart 5: EBITDA CAGR of 20% over FY11-16 on higher BOT revenue



Source: Company, Systematix Institutional Research

Chart 6: Net gearing on a rise due to new projects addition

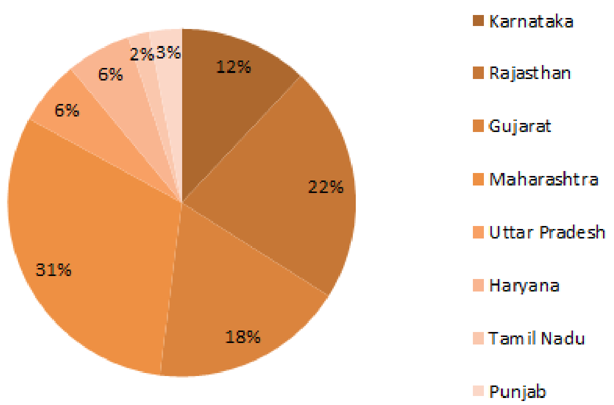


Source: Company, Systematix Institutional Research

Largest BOT toll road projects operator

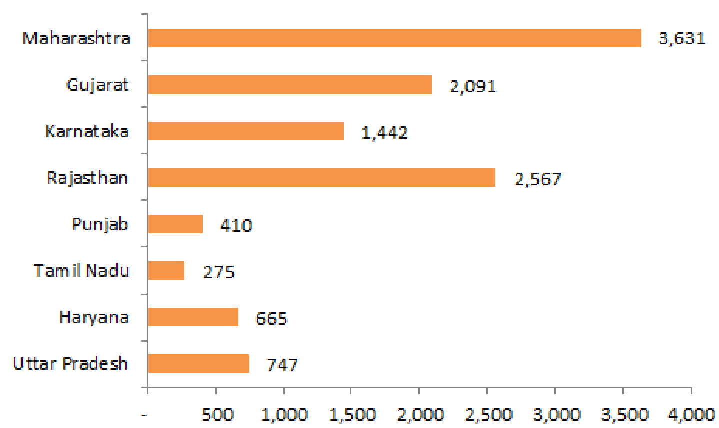
Incorporated in 1998, IRB is one of the largest build-operate-transfer (BOT) toll road operators in India, with a market share of 17.25% on the Golden Quadrilateral. Having executed the first-ever BOT project, Thane-Bhiwandi bypass in 1998, IRB now owns the largest BOT portfolio among peers, consisting of 22 BOT projects with 11,368 lane kms spread across India. The vertically integrated operation and efficient projects' execution capabilities aid in undertaking works related to the entire BOT value chain, from traffic studies, in-house construction and maintenance of all operational BOT projects. In spite of an upswing in awarding and substantial interest shown by players towards road EPC and HAM projects, IRB remained focused on BOT projects, where it has domain experience and expertise.

Chart 7: State-wise – BOT portfolio (%)



Source: Company, Systematix Institutional Research

Chart 8: Total lane kms – state-wise 11,828km



Source: Company, Systematix Institutional Research

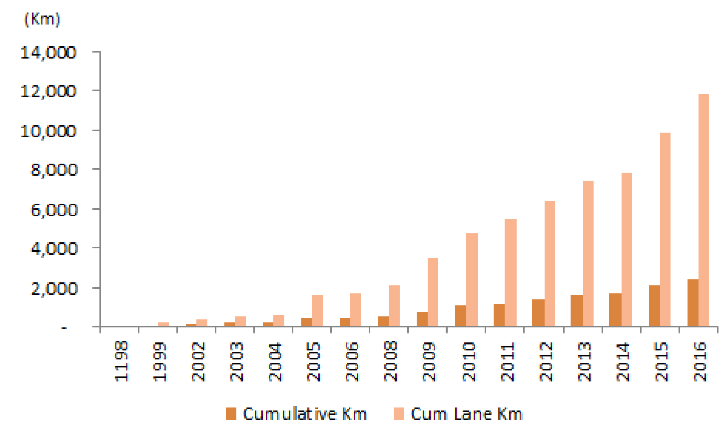
Of the 22 BOT projects in its portfolio, 14 are operational, five are under construction and the remaining three are won recently and under the process of financial closure.

Table 1: Healthy portfolio mix

	Lane km	No of projects
Under development	5,293	7
Operational	6,525	15
Total Portfolio	**11,828**	**22**

Source: Company, Systematix Institutional Research

Chart 9: Gradual projects addition increases to 2,448kms by FY16



Source: Company, Systematix Institutional Research

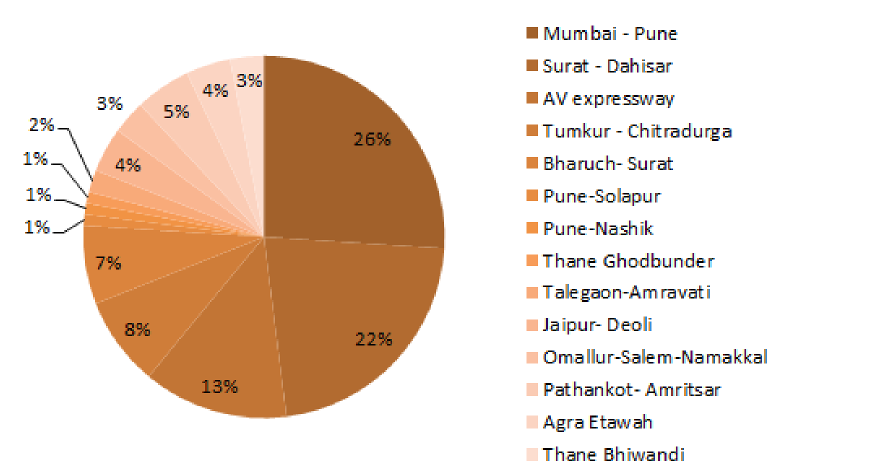
Table 2: BOT portfolio

Stretch	Length (km)	Client	Total Cost (Rs mn)	Residual yrs	Equity (Rs mn)	Grant (Rs mn)	Remarks
Operational							
Thane – Bhiwandi Bypass	24.0	PWD	1,040	0.6	312		-
Pune- Sholapur	26.0	MORTH	630	2.3	190		-
Pune –Nashik	29.8	MORTH	737	4.8	217		-
Mumbai – Pune	206.0	MSRDC	3,836	2.7	1,202		-
Thane – Ghodbunder	14.9	MSRDC	2,463	3.8	403		-
Bharuch – Surat	65.0	NHAI	9,655	5.0	1,981		-
Surat – Dahisar	239.0	NHAI	28,350	4.7	8,790		-
IRDP , Kolhapur	49.9	MSRDC	4,300	22.0	1,720		-
Pathankot - Amritsar	102.4	NHAI	14,453	13.6	3,955		-
Talegaon - Amravati	66.7	NHAI	8,800	15.1	1,992		-
Jaipur - Deoli	146.3	NHAI	17,330	18.6	4,281		-
Tumkur - Chitradurga	114.0	NHAI	11,420	20.6	3,426		-
Ahmedabad – Vadodara	196.0	NHAI	36,000	21.2	10,574		-
Omallur – Salem – Namakkal	68.6	NHAI	3,076	9.6	691		-
Under Construction							
Goa/Karnataka Border	190.0	NHAI	26,390	26.5	6,968	5,362	Scheduled CoD Aug'17
Solapur- Yedeshi	98.7	NHAI	14,920	27.5	3,933	1,890	Scheduled CoD Jul'17
Yedeshi – Aurangabad	189.1	NHAI	31,770	24.0	7,926	5,580	Scheduled CoD Dec'17
Kaithal- Rajasthan	166.3	NHAI	22,900	25.5	6,198	2,340	Scheduled CoD Jan'18
Agra- Etawah	124.5	NHAI	25,230	23.7	8,730		1st year premium Rs 810mn
Recently won							
Udaipur – Gujarat Border	113.8	NHAI	21,000	21.0			Premium commitment Rs1.6bn, 3 yrs after appointed date
Gulabpura-Chittorgarh bypass	124.9	NHAI	21,000	20.0			Premium commitment Rs2.3bn, 3 yrs after appointed date
Kishangarh – Gulabpura	90.0	NHAI	15,300	20.0			Premium commitment Rs1.9bn

Source: Company, Systematix Institutional Research

Historically, the Mumbai-Pune expressway project has been the primary driver of revenue for IRB; its contribution to toll revenue was as high as 62-64% in FY07-09. This came down to 33% of revenue in FY11, after commissioning of Bharuch-Surat and Surat-Dahisar projects. As shown below, Mumbai-Pune contributed 26% to the total 3QFY17 BOT toll revenue.

Chart 10: 3QFY17 project-wise BOT toll revenue break-up



Source: Company, Systematix Institutional Research

Table 3: BOT toll revenue growth

Particulars	FY12	FY13	FY14	FY15	FY16	9MFY17	3 yr CAGR FY13-16
Thane Bhiwandi Bypass	626	685	691	733	794	542	5.0
yoy growth (%)		9.4	0.9	6.1	8.3	1.3	
Pune-Solapur BOT	170	176	189	216	234	163	10.0
yoy growth (%)		3.5	7.4	14.3	8.3	3.5	
Pune-Nashik BOT	226	235	227	243	268	205	4.5
yoy growth (%)		4.0	-3.4	7.0	10.3	10.6	
Mumbai-Pune	3,977	4,162	4,376	5,673	6,331	4,986	15.0
yoy growth (%)		4.7	5.1	29.6	11.6	18.1	
Thane Ghodbunder	292	312	328	396	328	225	1.7
yoy growth (%)		6.8	5.1	20.7	-17.2	0.6	
Surat Dahisar	4,008	4,441	4,879	5,549	6,135	4,207	11.4
yoy growth (%)		10.8	9.9	13.7	10.6	-67.4	
Bharuch – Surat	1,429	1,612	1,666	1,857	1,936	1,336	6.3
yoy growth (%)		12.8	3.3	11.5	4.3	2.4	
IRDP , Kolhapur	0	0	25	41	23	0	NA
yoy growth (%)				64.0	-43.9	-100	
Talegaon-Amravati	0	0	264	461	472	346	NA
yoy growth (%)				74.6	2.4	9.4	
Jaipur- Deoli	0	0	343	1,015	1,206	812	NA
yoy growth (%)				195.9	18.8	(0.7)	
Omallur-Salem-Namakkal	0	292	613	756	749	544	36.9
yoy growth (%)			109.9	23.3	(0.9)	6.5	
Tumkur-Chitradurga	1,257	1,596	1,630	1,842	2,019	1,426	8.2
yoy growth (%)		27.0	2.1	13.0	9.6	3.4	
Pathankot- Amritsar	0	0	0	283	986	812	NA
yoy growth (%)		#DIV/0!	#DIV/0!	#DIV/0!	248.4	29.6	
Ahmedabad- Vadodara	0	291	1,219	1,566	2,187	2,392	95.9
yoy growth (%)		#DIV/0!	318.9	28.5	39.7	111.7	
Agra- Etawah	0	0	0	0	0	375	NA
yoy growth (%)		#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!	#DIV/0!	
KharpadaBridge	85	86	82	85	34	0	NA
yoy growth (%)		1.2	(4.7)	3.7	(60.0)	(100.0)	
Nagar -Karmala-Tembhurni	143	148	142	147	27	0	NA
yoy growth (%)		3.5	(4.1)	3.5	(81.6)	(100.0)	
Mohol-Mandrup-Kamtee	78	75	64	64	11	0	NA
yoy growth (%)		(3.8)	(14.7)	0.0	(82.8)	(100.0)	
Total	**12,291**	**14,111**	**16,738**	**20,927**	**23,740**	**18,371**	**18.9**
		14.8	18.6	25.0	13.4	55.2	
Like to Like comparable projects		**14,111**	**16,106**	**20,927**	**23,740**	**15,604**	**18.9**
yoy growth (%)			14.1	29.9	13.4	-1.4	

Source: Company, Systematix Institutional Research

Over FY13-16, BOT toll revenue for Mumbai-Pune project grew 15% over FY13-16 and the traction continued for 1HFY17, with 18% yoy growth led by strong passenger traffic. Commissioning of the NH8 Corridor in December 2015 led to an uptick in traffic. However, the shift of traffic from the AV expressway to the parallel toll free road led to PBT losses. While Tumkur-Chitradurga witnessed 8.2% revenue CAGR over FY13-16, weak mining cargo led to muted traffic growth of 3.4% yoy for 1HFY17. Strong monsoon too impacted growth at other stretches. Apart from Mumbai-Pune, projects operational within the last two years are yet to turn profitable. Commencement of operations in four of the five under-implementation projects, except Agra-Etawah, in FY18 will add to BOT revenue from FY18.

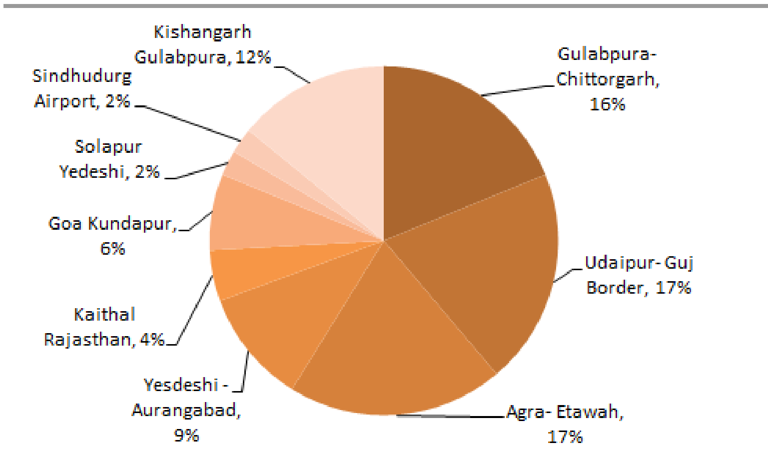
Newer projects strengthen footprints in Rajasthan

IRB recently won three BOT projects in Rajasthan totaling ~329km on the Kishangarh -Udaipur-Ahmedabad Highway (KUA) amounting to ~Rs57bn. The company has committed large premium payment of Rs3.9bn for the above two projects, assuming limited traffic risk on commissioning of DFC. However, the premium commitment on these projects starts from the fourth year of commissioning. The Agra-Etawah project, which commenced toll collection in August 2016, has also committed a premium of Rs810mn, in spite of a likelihood of traffic shifting to competing routes.

EPC order book contingent on new project wins

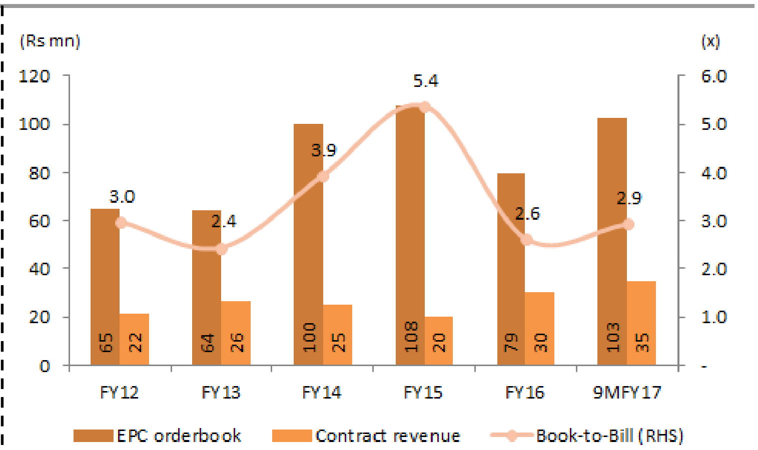
IRB's integrated business model has in-house capabilities of executing road projects from designing stage to construction. Its 100% subsidiary, Modern Road Makers Pvt Ltd (MRM), undertakes construction exclusively of in-house road BOT projects. Current EPC order book at Rs103bn (2.9x TTM revenue) excludes Rs17.5bn O&M on operational BOT projects.

Chart 11: Order book break-up – Rs103bn (excl. O&M at Rs17.5bn)



Source: Company, Systematix Institutional Research

Chart 12: Steady book-to-bill ratio at 2.9x



Source: Company, Systematix Institutional Research

While EPC order book at 2.9x provides revenue visibility, the newly-won projects contribute 35% to the order book which are undergoing financial closure and hence would start contributing to revenue from late FY18.

Compared to peers like ASBL, SADE and PNC Infra, IRB reports higher construction margins, which in our view can be unsustainable over the long run. This combined with an EPC focus only for in-house projects, makes the business heavily dependent on new assets addition for earnings growth, once the current portfolio becomes operational.

InvIT: Raising resources by assets' monetisation

IRB has floated an investment trust (InvIT) by pooling six of its operational projects and expects to raise Rs43bn by primary issuance apart from an offer-for-sale by sponsor group companies. The six assets include: 1) Surat-Dahisar, 2) Bharuch-Surat, 3) Tumkur-Chitradurga, 4) Omallur-Salem, 5) Talegaon-Amravati and 6) Jaipur-Deoli.

The portfolio is spread across 3,635 lane kms and is strong with (a) operational history of two to five years and an average residual life of 12 years (ranging between 5 to 21 years), (b) strong 9.4% traffic growth over FY14-16 and (c) revenue share of commercial traffic at 80% and (d) declining debt profile. As of March 2016, the portfolio of assets had a revenue of Rs10bn, debt of Rs47bn, sub-debt of Rs7bn and equity of Rs11bn.

Chart 13: Location of SPVs constituting the proposed InvIT

Source: Company, Systematix Institutional Research

The DRHP filed with Sebi mentions the likelihood of extension of concession for select projects due to traffic shortfall.

Table 4: Concession period extension due to traffic shortfall

Project	Extension
Surat- Dahisar	11 months
Jaipur- Deoli	2 years, 3 months
Talegaon- Amravati	4 years, 4months

Source: Company, Systematix Institutional Research

Features of InvIT

- The trust will acquire 100% of equity shares in each of the underlying five SPVs, except Omallur-Salem (where IRB holds 74%). Pursuant to the approval from NHAI, IRB also intends to acquire the rest 26% from other shareholders.
- As a consideration for acquisition of equity shares, the trust will issue units to the seller of each SPV, based on a mutually agreed price, and some of these units will also be available under the offer-for-sale.
- The trust has an option to retain oversubscription up to 25% of the issue size in accordance with InvIT regulations.
- By regulation, the sponsor has to hold 25% of the total post issue units, which will have a lock-in of three years. Any holding beyond 25% will have a lock-in of one year.

Regulatory framework

Recent budgets have cleared taxation issues, thus making the product investor friendly. Interest payout will have a pass-through mechanism, with 5-10% tax in the hands of foreign/resident investors. Dividend payout will have no taxation in the hands of the trust or unit holders.

Utilisation of proceeds

The trust proposes to invest Rs42bn from net proceeds in project SPVs by way of issue of debt. Project SPVs, in-turn intend to utilise the proceeds of such investment towards 1) partial repayment/prepayment of loans from their senior lenders (Rs37bn as of FY16), 2) prepayment in part or full of the subordinate debt provided to SPVs (Rs7bn as of FY16) and 3) prepayment in part or full of certain unsecured loans and advances (Rs10bn as of FY16).

Based on management estimates, the trust values the portfolio at Rs80bn EV (9.6x FY16 EBITDA) and Rs30bn equity (2.7x invested equity). This factors 1) aggressive traffic assumptions of 6.5-7.1%+ over the life of assets (except Surat-Dahisar) along with 5.5% inflation linked toll hike and 2) extension of concession period for select projects (led by traffic shortfall). Management indicates equity IRR of 12%.

Based on an average 5.5% traffic growth rate for residual years across all projects and a cost of equity of 14%, we estimate EV of ~Rs60bn for the trust's portfolio.

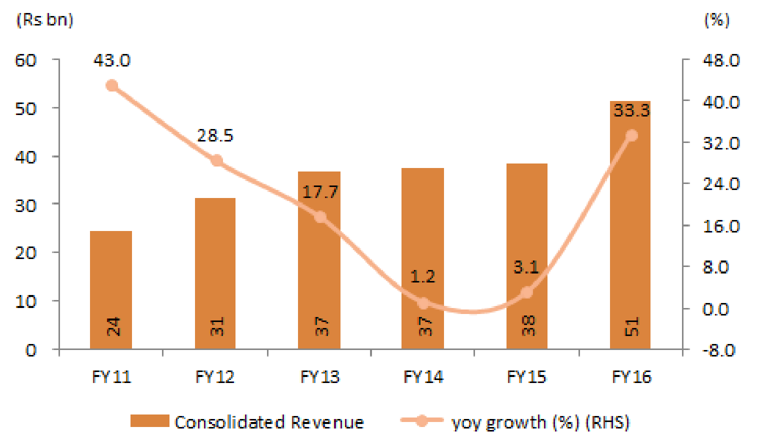
64% of FY16 revenue was contributed by two projects that have a residual life of five years -- Bharuch-Surat and Surat-Dahisar.

Key negatives for the portfolio are: 1) apart from repayment to senior lender, we believe the interest free sub-debt and unsecured loans & advances that SPVs avail at the moment will be replaced by interest-bearing debt from the trust, 2) concentration of 67% of residual revenue in two projects -- Tumkur-Chitradurga (41%) and Jaipur-Deoli (26%) and 3) large premium share with NHAI in Tumkur-Chitradurga project makes it highly sensitivity to traffic.

Healthy financials, success of InvIT to aid in deleveraging

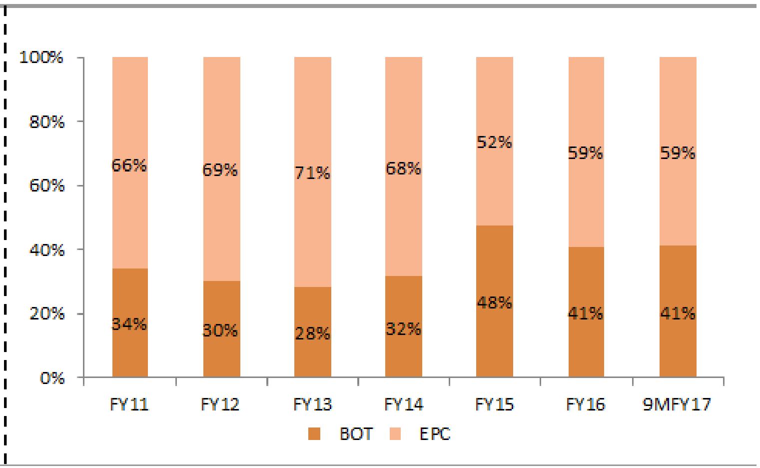
IRB's consolidated revenue clocked 16% CAGR over FY11-16, led by an increasing share of BOT toll revenue in total revenue mix, aided by more than 2x increase in cumulative operational lane km to 11,278km in FY16 v/s 5,452km in FY11.

Chart 14: Five-year revenue CAGR at 16%



Source: Company, Systematix Institutional Research

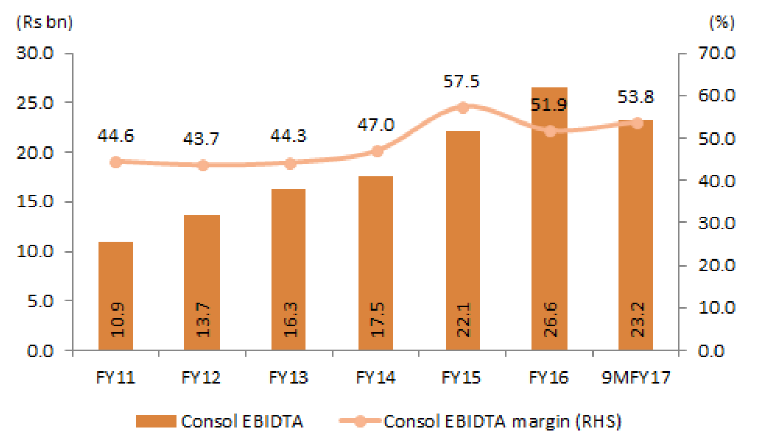
Chart 15: Rising share of BOT toll in revenue mix



Source: Company, Systematix Institutional Research

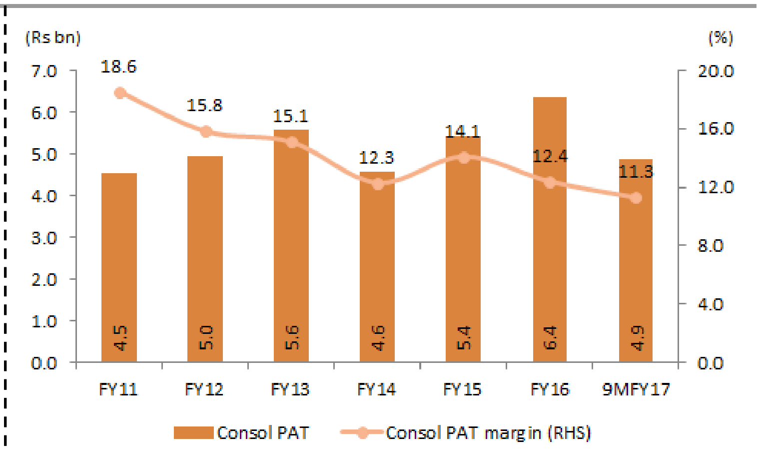
Consolidated EBITDA posted 19.6% CAGR over FY11-16 and EBITDA margin rose from 44.6% to 51.9% during the same period, led by 2x increase in commissioning of high-margin BOT projects; cumulative 2,355km in FY16 v/s 1,179km in FY11. A higher outgo of interest and depreciation expense on commissioning of these BOT projects led to 7% CAGR in adjusted PAT to Rs6.4bn over FY11-16.

Chart 16: EBITDA CAGR of 20% over FY11-16 on higher BOT revenue



Source: Company, Systematix Institutional Research

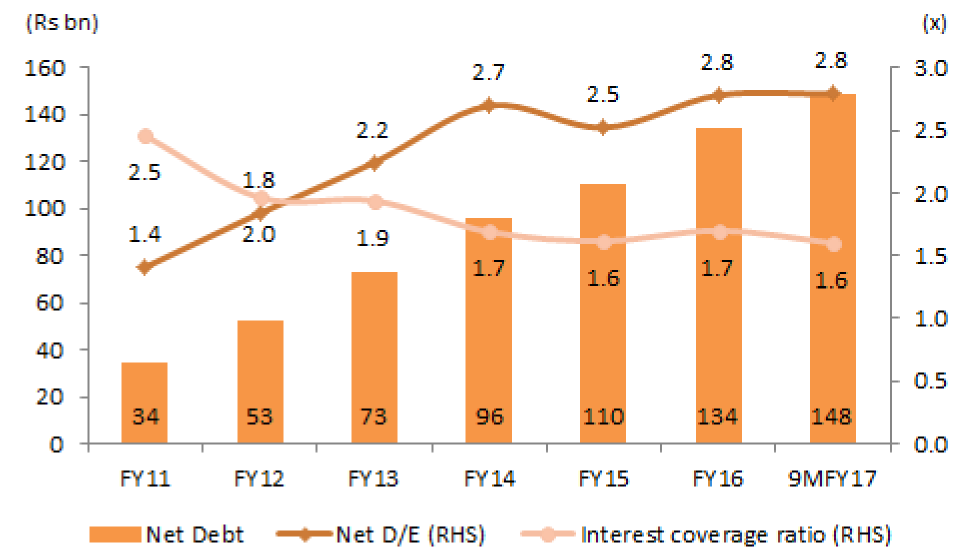
Chart 17: Int., depreciation led to 7% adj. PAT CAGR over FY11-16



Source: Company, Systematix Institutional Research

The average cost of debt is at 10.5-10.75% and the consolidated net D/E of 2.8x is likely to go up with new project wins. However, success of InvIT will aid in deleveraging and to free up capital to invest in new projects.

Chart 18: Net gearing on a rise due to new projects addition



Source: Company

Equity needed for under-development projects: The net equity requirement in under-construction projects is ~Rs18-19bn for FY18 and FY19.

Table 5: Equity requirement schedule (Rs mn)

Projects	FY18	FY19
Yedeshi- Aurangabad	1,900	-
Agra- Etawah	2,000	4,000
Kaithal - Rajasthan	1,200	-
Udaipur- Gujarat / Gulabpura – Chittorgarh	3,000	6,000
Total	**8,100**	**10,000**

Source: Company

Key risks

1) Delay in finalisation of projects from NHAI/ state road development corporations can slow down the conversion of bid pipeline into order inflows.

2) Successful listing of InvIT is needed to deleverage the balance sheet. Any delay in asset monetisation will add to the outstanding debt.

3) Any impediment in the execution of current order book, due to clients' liquidity crunch, can hamper the revenue growth, stretch working capital cycle and increase leverage.

MEP Infrastructure

27 March, 2017

Leading player in toll collection domain

NOT RATED	
Sector: Construction	**Rating: NA**
CMP: Rs51	**Target Price: NA**

Stock Info

Sensex/Nifty	29,332/ 9,086
Bloomberg	MIDL IN
Equity shares (mn)	163
52-wk High/Low	Rs50/34
Face value	Rs10
M-Cap	Rs8.0bn/$0.1bn
3-m Avg volume	$0.2mn

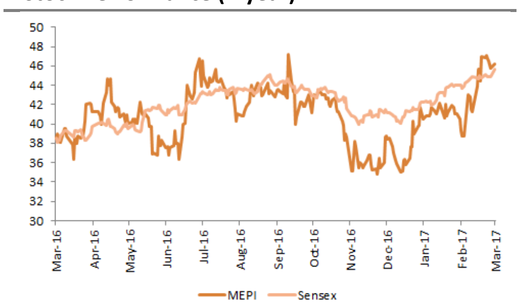
Financial Snapshot (Rs mn)

Y/E Mar	FY14	FY15	FY16
Sales	11,979	20,088	20,068
EBITDA	3,105	4,436	5,549
PAT	(1,279)	(1,153)	265
EPS (Rs)	(13.3)	(10.3)	1.6
PE (x)	(19.9)	(24.7)	156.5
EV/EBITDA (x)	11.5	8.5	56.6
P/BV (x)	(5.8)	(2.5)	0.8
RoE (%)	3.5	0.7	0.1
RoCE (%)	0.1	0.1	0.1
Dividend yield (%)	-	-	0.0
Net gearing (x)	(34.8)	(14.4)	28.9

Shareholding pattern (%)

	Dec '16	Sep '16	Jun '16
Promoter	69.5	69.5	69.5
–Pledged	-	-	-
FII	6.2	6.2	5.8
DII	8.9	8.9	8.9
Others	15.4	15.4	15.8

Stock Performance (1-year)



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MEP Infrastructure (MIDL), founded in 2002 by Dattatray Mahiskar, commenced operations with toll collection at five entry points to Mumbai. Over the years, MIDL has developed a leadership position in toll collection and has a portfolio 22 projects, comprising of 9 short-term, three long-term toll collection, three OMT and six HAM projects. The revenue from long-term projects increased to 67% in FY16 (39% in FY12), in line with the company's strategy to enhance revenue visibility and stability. Mumbai Entry Points project is the largest contributor to revenue (20% in FY16). An equity of Rs58bn will be invested by MIDL (Rs4bn) and its JV partner, Sanjose India (Rs1.8bn), over the next 2.5 years. MIDL is exploring InVITs options to deleverage a debt of Rs31bn, of which Rs25bn was raised to procure the Mumbai Entry Points project.

Leading player in business of toll collection

MIDL is among the few infrastructure companies with an expertise to undertake projects in road construction, maintenance and toll collection, both independently and collectively. Having commenced operations in December 2002, with toll collection at five entry points in Mumbai, MIDL added both short and long-term toll collection projects together with OMT projects over the last 13 years. With footprints in 12 states and a focus on asset-light business model, MIDL has successfully completed 106 projects covering 200 toll plazas and 1,230 lanes till FY16. It also has strong relationship with statutory and government authorities such as NHAI, MoRTH, MSRDC, RSRDC, RIDCOR, TNRDC among others. MIDL manages three long-term, 9 short-term and three OMT projects. The strategy is to balance short-term tolling contracts with long-term alternatives and OMT projects, enhancing revenue visibility and stability. Thus, the revenue share of long-term projects has increased to 67% in FY16, from 39% in FY12. The company has a workforce of 2,722 employees in tolling and maintenance activities.

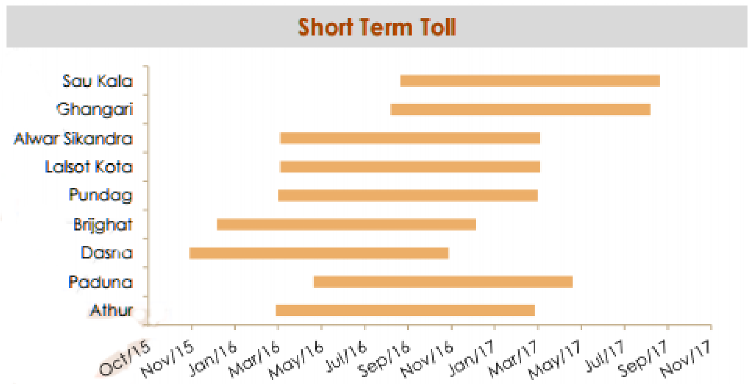
Foray into HAM to strengthen portfolio

MIDL in a JV with Sanjose India Infrastructure has won six HAM projects (four in Maharashtra and two in Gujarat) covering 1,060 lane kms. Total EPC work of Rs38bn for all six projects will be undertaken by MIDL with a mix of in-house execution and sub-contracting (mainly two Gujarat projects). MIDL has achieved financial closure of all six projects, with an average cost of debt at 11% and received appointed date of two Nagpur projects by Jan'17. Appointed date for two other Maharashtra projects and two Gujarat projects is expected by March'17 end. Total equity requirement in all six projects over next two-and-half years from the appointed date stands at Rs5.8bn. While MIDL has to invest Rs4bn for its share (Rs1.8bn already invested), Sanjose will invest Rs1.8bn. Management expects 12-14% EBITDA margin, net of outsourcing, due to savings in overheads led by a contiguous stretch of projects. MIDL is evaluating bids for fresh six to eight HAM projects and expects to bid by Mar'17. It is also eyeing opportunities in the recently-proposed toll-operate-transfer (ToT) model and will evaluate depending on the cluster tendered and kind of O&M requirement.

Steady revenue mix led by Mumbai Entry Points and HAM project

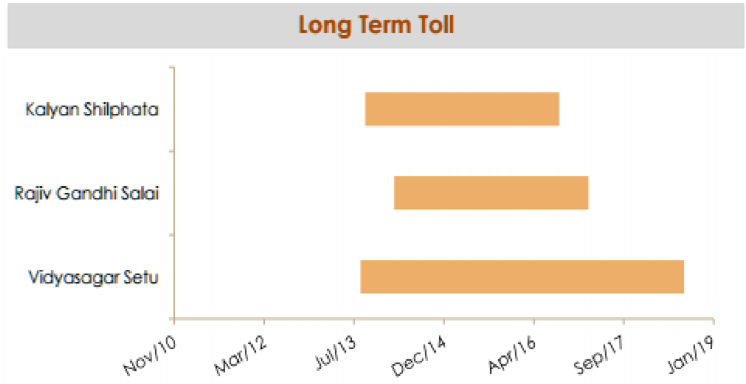
MIDL's revenue/EBITDA posted 17%/12% CAGR over FY12-16, led by a higher contribution from Mumbai Entry Points project (20% of FY16 revenue). The project was awarded to MIPL, MIDL's wholly-owned subsidiary, for an upfront fee of Rs21bn in 2010 for 16 years, which increased FY11 debt to Rs33bn. In FY16, MIDL generated a cash profit of Rs1.8bn and lowered its debt to Rs31bn. The Bandra-Worli sea link OMT project (three years completed in Feb'17) is up for rebidding and management is positive of re-winning it. Going forward, management expects revenue from HAM EPC projects to provide a steady revenue stream, compared to short-term tolling projects. MIDL has claimed Rs885mn due to a loss in toll revenue led by demonetisation. While it has recognised Rs498mn as other operating revenue, Rs387mn has been adjusted against depreciation and amortisation in terms of payment to authorities. To further reduce debt and bid for new HAM/OMT projects, MIDL is exploring options to raise funds through InVITs.

Chart 1: Seven of nine short-term tolling projects near completion



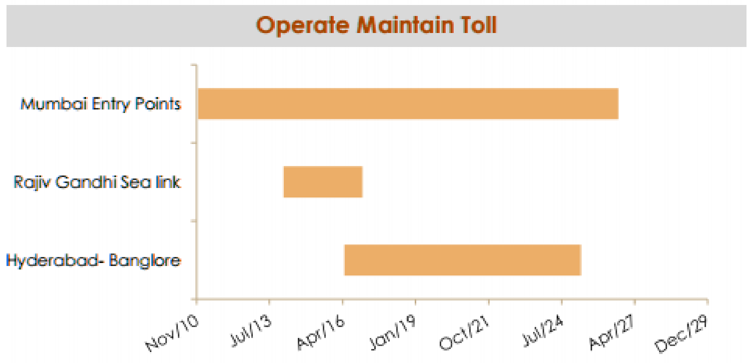
Source: Company

Chart 2: Higher residual life of long-term toll collection projects



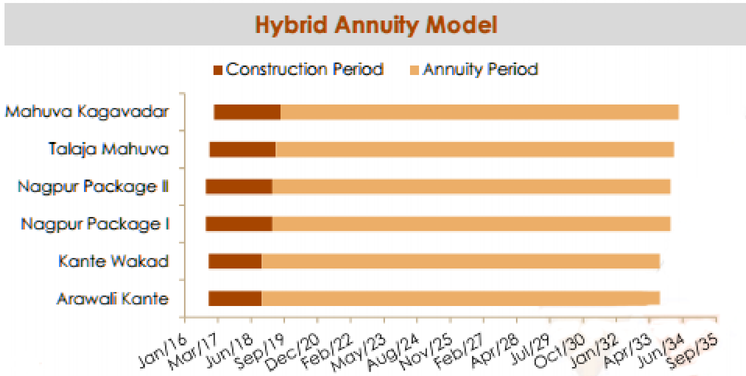
Source: Company

Chart 3: Mumbai Entry Points comprise 20% of revenue



Source: Company

Chart 4: HAM projects' EPC provide revenue visibility



Source: Company

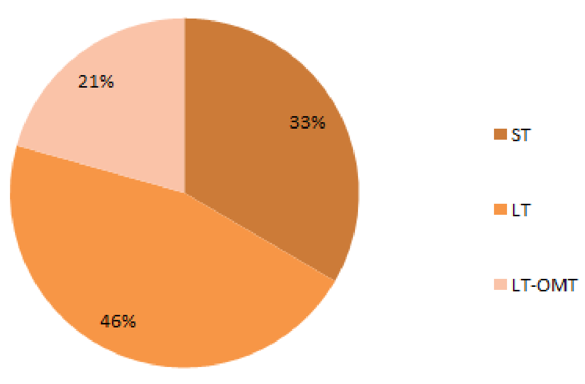
Table 1: 4-laning of six HAM projects won by MEPIDL–Sanjose India JV

Stretch	MEPIDL's stake	km	Lane km	Authority	State	BPC (Rs mn)	Const / Conc. period (yrs)	FC/ Appointed date	Terms of FC
Arawali- Kante	74%	40	156.9	MoRTH	Maharashtra	5930	5 / 15	FC done on 28th Jun'16	Debt: Rs2668mn, Avg cost of debt ~11%
Kante- Wakad	74%	51	203.6	MoRTH	Maharashtra	8263	2 / 15	FC done on 28th Jun'16	Debt: Rs3718 mn, Avg cost of debt ~11%
Nagpur -Package 1	74%	29	134.0	NHAI	Maharashtra	5310	2.5 / 15	Appointed date – 5th Jan'17; civil work underway	Debt: Rs2389mn, Avg cost of debt ~11%
Nagpur -Package 2	74%	28	112.1	NHAI	Maharashtra	6390	2.5 / 15	Appointed date – 20th Jan'17; civil work underway	Debt: Rs2876mn, Avg cost of debt ~ 11%
Talaja -Mahuva	60%	46.5	181.8	NHAI	Gujarat	6430	2.5 / 15	FC under process	NA
Mahuva - Kagavadar	60%	39.8	160.1	NHAI	Gujarat	6045	2.5 / 15	FC under process	NA

Source: Company

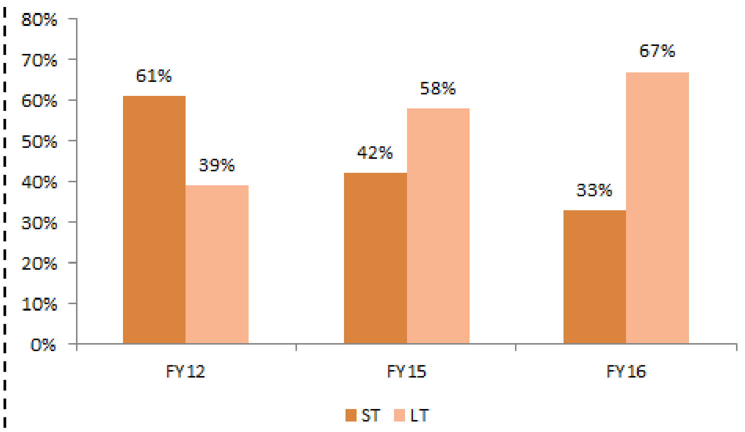
Charting the story

Chart 5: Revenue break-up



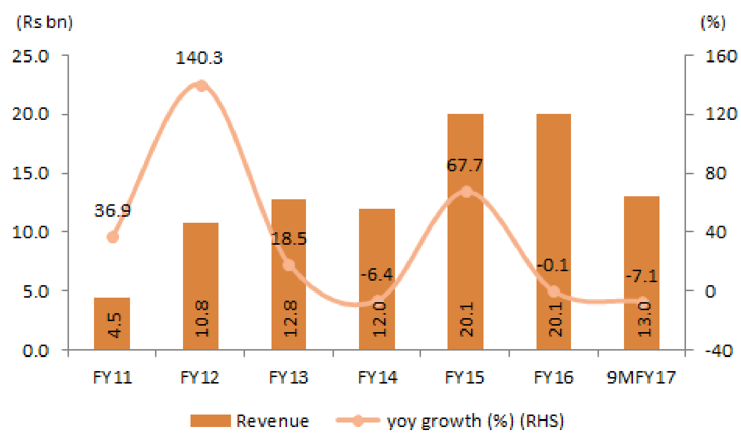
Source: Company, Systematix Institutional Research

Chart 6: Increasing focus on LT projects (Rs mn)



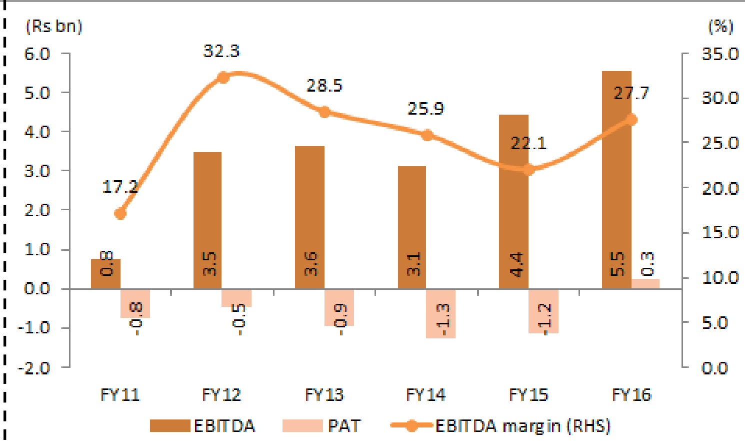
Source: Company, Systematix Institutional Research

Chart 7: 35% revenue CAGR over FY11-16



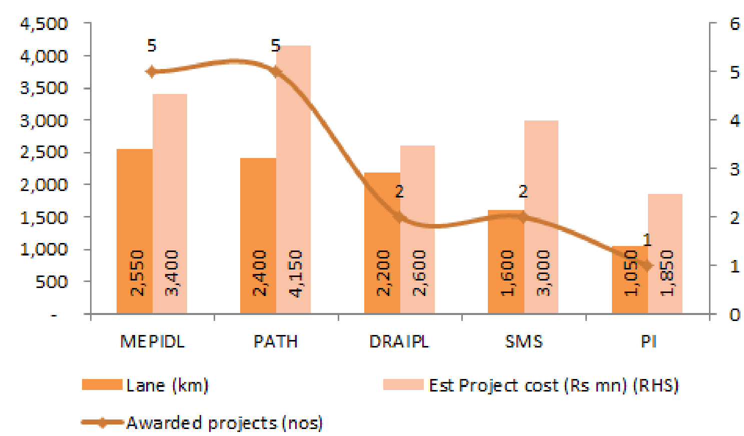
Source: Company, Systematix Institutional Research

Chart 8: Turnaround in profitability, PAT +ve for 1st time in FY16



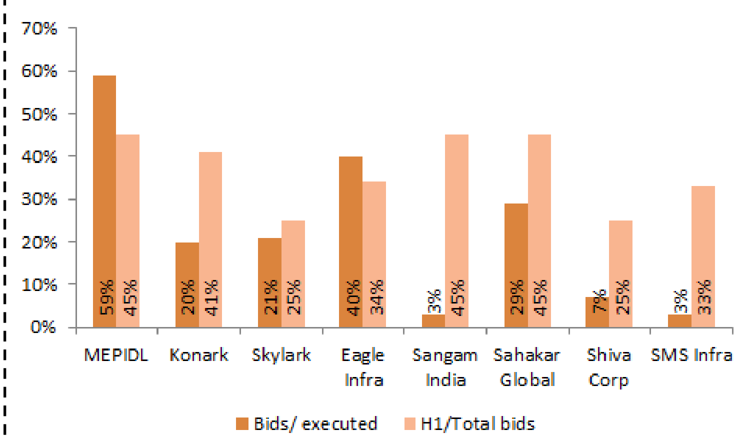
Source: Company, Systematix Institutional Research

Chart 9: Leading player in OMT



Source: Company, Systematix Institutional Research

Chart 10: Leading player in toll collection over FY12-15



Source: Company, Systematix Institutional Research

FINANCIALS (CONSOLIDATED)

Profit & Loss Statement

YE: Dec (Rs mn)	FY12	FY13	FY14	FY15	FY16
Net revenues	10,801	12,800	11,979	20,088	20,068
Revenue growth (%)	140	19	(6)	68	-
- Op. expenses	7,311	9,151	8,874	15,652	14,519
EBIDTA	3,490	3,649	3,105	4,436	5,549
EBITDA margins (%)	32	29	26	22	28
- Interest expenses	3,766	3,765	3,797	4,036	3,832
- Depreciation	947	990	1,303	1,799	1,706
+ Other income	565	220	433	325	407
PBT	(658)	(886)	(1,562)	(1,074)	418
- Tax	(126)	44	(236)	79	153
Effective tax rate (%)	19	(5)	15	(7)	37
Adjusted PAT	(532)	(930)	(1,326)	(1,153)	265
+/- Extraordinary items	-	-	(13)	-	-
+/- Minority interest	(54.0)	-	9.0	-	-
+ PL of Associate Co.	-	-	43.0	-	-
Reported PAT	(478)	(930)	(1,279)	(1,153)	265
Adj. FDEPS (Rs/share)	(5.3)	(9.3)	(13.3)	(10.3)	1.6

Balance Sheet

YE: Dec (Rs mn)	FY12	FY13	FY14	FY15	FY16
Share capital	1,000	1,000	1,000	1,115	1,626
Reserves & Surplus	(379)	(1,308)	(1,878)	(3,379)	(613)
Networth	621	(308)	(878)	(2,265)	1,013
Minority interest	453	453	-	-	-
Total Debt	31,503	30,890	32,201	33,886	30,755
Def. tax liab. (net)	(286)	(349)	(756)	(942)	(1,070)
Capital employed	**32,291**	**30,686**	**30,567**	**30,680**	**30,698**
Net Fixed assets	22,074	21,513	23,695	21,722	20,360
Investments	28	30	6	323	217
- of which liquid	-	-	-	-	-
Net Working capital	9,365	7,604	5,252	7,287	8,624
Cash and bank balance	824	1,539	1,623	1,348	1,499
Capital deployed	**32,291**	**30,686**	**30,576**	**30,680**	**30,700**
Net debt	30,679	29,351	30,579	32,538	29,256
WC (days)	461	340	482	252	418
Book value (Rs/sh)	11	1	(9)	(20)	6

Source: Company, Systematix Institutional Research

Cash Flow

YE: Dec (Rs mn)	FY12	FY13	FY14	FY15	FY16
PAT	(532)	(930)	(1,313)	(1,153)	265
+ Non cash items	702	927	896	1,613	1,578
Cash profit	170	(3)	(417)	460	1,843
- Incr/(Decr) in WC	482	(1,761)	(2,352)	2,035	1,337
Operating cash flow	(313)	1,759	1,935	(1,575)	506
- Capex	(470)	(561)	5,780	(249)	342
Free cash flow	157	2,320	(3,845)	(1,326)	165
- Dividend	-	-	-	-	-
+ Equity raised	888	-	-	115	511
+ Debt raised	(1,252)	(613)	1,311	1,685	(3,131)
+ MI	(54)	-	9	(9)	-
- Investments	(916)	2	(24)	316	(106)
- Misc. items	439	989	(2,584)	426	(2,501)
Net cash flow	216	716	83	(277)	151
+ Opening cash	608	824	1,539	1,623	1,348
Closing cash	824	1,539	1,622	1,345	1,499

Source: Company, Systematix Institutional Research

Ratios

YE: Dec	FY12	FY13	FY14	FY15	FY16
P/E (x)	(53.3)	(27.4)	(19.9)	(24.7)	156.5
P/B (x)	4.7	35.1	(5.8)	(2.5)	0.8
EV/EBITDA (x)	10.2	9.4	11.5	8.5	56.6
RoE (%)	(74)	(153)	349	73	7
RoCE (%)	8	8	6	8	12
Fixed Asset turnover (x)	0.3	0.4	0.2	0.3	0.3
Dividend yield (%)	-	-	-	-	-
Dividend payout (%)	-	-	-	-	12
Interest exp./Sales	35%	29%	32%	20%	19%
Debtors (days)	2	15	22	10	-
Revenue growth (%)	140	19	(6)	68	-
PAT growth (%)	(37)	95	38	(10)	(123)
EBITDA growth (%)	350	5	(15)	43	25
EPS growth (%)	1,317	(49)	(27)	24	(735)
Net gearing (%)	28.5	202.1	(34.8)	(14.2)	30.2

Source: Company, Systematix Institutional Research

TRIL Roads Private Ltd (TRPL)

27 March, 2017

Emerging developer for road BOTs

TRIL Roads Pvt Ltd (TRPL) is a wholly owned subsidiary of Tata Realty and Infrastructure Ltd. After announcement of various investor friendly policies by the Government, TRPL has been aggressive in building a road BOT portfolio both through brownfield and Greenfield route. It currently has four projects in its portfolio – two operational and two under construction. While the EPC work is sub-contracted, TRPL targets to yield equity IRR of 18% for Greenfield projects and in mid-teens for operational projects.

Table 1: Current project portfolio

Strech	km		CoD	State	Consortium	Status
Pune - Solapur Expressway	110	own	31st Jan 2015	Maharashtra	TRIL Roads & Autostrade IID	Operational
Durg Bypass	18	acquired	Acq in Jan'17	Chattishgarh	100% owned	Operational
Hospet - Chitradurga	120	own	Jun-18	Karnataka	100% owned	Under construction
6 laning Udaipur- Chittorgarh	95	own	Sep-16	Rajasthan	100% owned	Under construction
Salem Tollways	53	acquired	-	Tamil Nadu	Signed agreement with IVRCL in 2013 to acquire 3 (624 lane km approx) road projects in 2013 at EV of Rs22bn. Due to winding up petitions filed against IVRCL, the acquisition process is held up in court. It is expected that the acquisition would be completed in near term.	
Kumarapalayam Tollways	47	acquired	-	Tamil Nadu		
IVRCL Chengapally Tollways	55	acquired	-	Tamil Nadu & Kerela		

Source: Company, Systematix Institutional Research

- From 2200 lane km at present, the target is to increase to 5,000 lane km by FY19. TRPL endeavors to have portfolio of 11-13 projects with investment value of Rs100bn primarily with longer concession period. It is contemplating InVIT /IPO at a later date.
- TRPL participated in around 12 of 47 bids but were L2/L3/L4 in most projects. The management believes that HAM projects are profitable only for integrated EPC players.

Management views on the sector

- State roads: Inspite of opportunity size being huge (1.5-2.5 lakh km over 5-7 years) and funding not a concern, not many projects have fructified owing to lack of institutional mindset and political interference.
- Funding HAM/BOT projects: The model was introduced at the time when banks went into cleaning mode for already awarded infra loans. Hence extending fresh loans to HAM was a challenge. However, banks are willing to fund projects if sponsor and assets are good and bankable.
- Competition for BOT projects is restricted to 4-5 bidders vs 18-20 price bids earlier
- Abrupt **change of Chairman at NHAI** would not impact projects which are at advanced stage of awarding as the body has independent functioning mechanism. However, stability has set in, in terms of awarding of contracts with better interaction of team with the outgoing Chairman.

Table 1: Consolidated Financials for Tata Realty and Infrastructure (TRIL)

Rs mn	FY14	FY15	FY16
Total Income	2,168	1,480	7,049
EBITDA	1,409	706	3,878
PBT	687	(260)	(2,306)
Exceptional Items	-	-	(1,960)
PAT	(1,073)	(872)	(367)
Cash Flow from Operations	(1,619)	(1,422)	1,400
Debt To Equity	0.5	3.8	3.7
Current Ratio	1.1	0.3	0.4
ROCE (%)	10.2	1.5	4.2
RONW (%)	(12.4)	(11.2)	(4.3)
EBITDA Margin (%)	65.0	47.7	55.0
PAT Margin (%)	(49.5)	(58.9)	(5.2)

Source: Industry, Systematix Institutional Research

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IDFC Alternatives

27 March, 2017

Among top PE investor in roads segment

IDFC Alternatives under its Indian Infrastructure Fund (IIF) has bought controlling stakes in operational roads assets that enable them to have larger say in decision making and capital structure of the asset.

Table 1: IIF Current Portfolio

Stretch	km	Type	Acquired from	Year of Acq	% stake	State	Equity value (Rs mn)
Kadtal - Armur (Nirmal BOT annuity)	30	Toll	HCC	Dec-15	100%	Andhra Pradesh	640
Bhopal - Dewas	143	Toll	Welspun Enterprises	Dec-15	37%	Madhya Pradesh	NA
Tindivanam and Ulundurpet (Ulundurpet expressway)	734	Toll	GMR group	Feb-14	74%	Tamil Nadu	2200
Bangalore Elevated tollway	9	Toll	NCC and Soma Enterprise	Feb-16	68%	Andhra Pradesh	1500-200
Reengus-Sikar Expressway	44	Annuity	GR Infraprojects	Jan-17	100%	Rajasthan	NA
Shillong Bypass	47	Annuity	GR Infraprojects	Jan-17	100%	Meghalaya	NA
Gayatri Lalitpur Roadways	49	Annuity	Gayatri Projects (in talks to buy remaining stake)	-	49%	Uttar Pradesh	NA
Gayatri Jhansi Roadways	50	Annuity		-	49%	Uttar Pradesh	NA

Source: Company, Systematix Institutional Research

Key takeaways from on our interaction with Senior Official at IDFC Alternatives:

- **Acquisition strategy:** To scout for operating assets with residual life of 12-15 yrs which coincides with the life of their fund i.e 12 -15 yrs. Return parameter – should start generating yield from 2nd year and have equity IRR of 15-16%
- Traffic growth on operational road assets in their portfolio has seen healthy growth between 7%-14% over last 5 years.
- Strong parentage and longer term loan available from infra debt funds has aided in lowering interest rate on refinancing at time of acquisition of assets to as low as 9% for annuity and between 9-10% for toll projects.
- WPI linked toll increase has in some cases offset the benefit of higher traffic and favourable interest rates.
- Given the larger issue on ground is to develop integrity to avoid leakages in toll collection, IDFC Alternatives now looks to have 70-80 people on its payroll compared to 15-20 people earlier with balance outsourced.
- Compensation for loss of toll revenue on demonetisation- NHAI terms as political force majure and would compensate for O&M and interest expenses. However, sponsors want them to treat it as change in law and compensate 100% in cash or extend concession period at least by 45 days.
- On TOT model – NHAI now wants to do quality assessment of all 75 roads before tendering them under this model, which is estimated to take off by April-May'17.
- IDFC Alternatives recently (Jan'17) sold its 48.4% stake in Durg Bypass road project, Chattishgarh to TRIL for total equity value of Rs2.8bn (100% stake).

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