

SADBHAV ENGINEERING

Stellar performance

India Equity Research | Infrastructure - Construction



Sadbhav Engineering (SEL) posted strong Q4FY17 numbers with revenue at INR10.3bn jumping 20% YoY driven by execution in EPC projects won in FY16 gathering pace. While interest cost rose 21% YoY due to repayment of mobilisation advance to NHAI, lower tax rate led to adjusted PAT catapulting ~129% YoY to INR682mn. Traffic on BOT projects grew ~3% YoY post demonetisation impact. SEL's book-to-bill stands at ~2.3x. While execution of hybrid annuity (HAM) projects will boost FY18 top line, we believe order inflows remain key catalyst for earnings. Maintain 'BUY' with SOTP-based target price of INR388.

Execution on an upswing

Revenue, at INR10.3bn, jumped 20% YoY on strong execution of Eastern Peripheral Expressway and Yamunanagar Panchkula projects. Completion of existing EPC projects in the current year coupled with ramp up of work in HAM projects has led to management guiding for ~INR38bn plus revenue in FY18. While work on EPC projects is in full swing, HAM projects' execution will gather pace in H2FY18.

Traffic on BOT projects back to normal post demonetisation

Post demonetisation, traffic normalised-grew 3% YoY in Q4FY17 (in December 2016 had fallen 7-8% YoY). SEL has achieved financial closure for 5 HAM projects; while work has already commenced on 3 projects, the company expects to receive 'appointed date' for the balance two projects in Q2FY18. An additional 2 HAM projects are expected to achieve financial closure and start execution in H2FY18. We believe, winning 7 HAM projects balances SEL's BOT portfolio, which hitherto was skewed in favour toll projects.

Outlook and valuations: Attractive; maintain 'BUY'

Strong order book, robust BOT portfolio and best-in-class execution skills render SEL an attractive bet to benefit from upcoming opportunities in EPC and BOT segments. We remain sanguine about increasing revenue traction in the EPC arm and better cash flow generation in the BOT subsidiary. We maintain 'BUY' with SOTP-based target price of INR388 (INR161 from EPC business at 16x FY19E P/E and balance from DCF valuation of BOT projects).

Financials		(INR mn)						
Year to March	Q4FY17	Q4FY16	% change	Q3FY17	% change	FY17	FY18E	FY19E
Revenues	10,329	8,580	20.4	8,648	19.4	33,203	37,143	42,971
EBITDA	1,096	908	20.7	938	16.8	3,556	3,978	4,602
Adj. profit	682	298	128.6	524	30.1	1,878	1,685	1,721
Dilu.EPS (INR)	4.0	1.7	128.6	3.1	30.1	11.0	9.8	10.0
Dilu.P/E (x) *						7.9	8.8	8.6
EV/EBITDA (x) *						8.8	7.3	6.5
ROAE (%)						11.9	9.7	9.1

* for implied construction business

EDELWEISS RATINGS

Absolute Rating	BUY
Investment Characteristics	Growth

MARKET DATA (R: SADE.BO, B: SADE IN)

CMP	: INR 315
Target Price	: INR 388
52-week range (INR)	: 351 / 220
Share in issue (mn)	: 171.6
M cap (INR bn/USD mn)	: 54 / 837
Avg. Daily Vol. BSE/NSE ('000)	: 147.9

SHARE HOLDING PATTERN (%)

	Current	Q3FY17	Q2FY17
Promoters *	46.8	46.8	46.8
MF's, FI's & BKs	26.3	26.1	25.3
FII's	17.2	16.9	17.5
Others	9.8	10.2	10.4
* Promoters pledged shares (% of share in issue)	:	16.23	

PRICE PERFORMANCE (%)

	BSE Midcap Index	Stock	Stock over Index
1 month	(2.9)	(5.9)	(3.0)
3 months	6.0	13.4	7.3
12 months	26.6	13.8	(12.8)

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Concall highlights

- **Bid pipeline:** SEL has bid for 10 NHAI EPC contracts worth INR74bn, 5 EPC contracts from Government of Gujarat worth ~INR27bn, 3 MDO projects, 7 mining EPC jobs worth ~INR27bn and 5 irrigation projects worth ~INR13bn. The company is also pursuing opportunities in the Metro space. It is planning to bid for Metro projects in Mumbai, Pune, Nagpur, Ahmadabad and Gandhinagar.
- **FY18 guidance:** **Revenue** - INR38-39bn, of which HAM projects will contribute ~INR13-15bn, Road EPC – INR17bn; Mining – INR4.0-4.5bn and Irrigation – INR5bn. **Operating margin** - 11%. **Order intake** – INR60-70bn.
- **Order book:** SEL ended FY17 with order book of INR77bn. This does not include 2 HAM projects worth ~INR15.75bn.
- **FY17 order book break-up:** Transport projects account for 65% of order book (captive BOT projects 42%); irrigation and mining contribute 13% and 22%, respectively.
- **Debt:** As at Q4FY17 end, SEL's gross debt (standalone) stood at INR16.6bn. The company has repaid mobilisation advance worth INR1.7bn in Q4FY17 to NHAI, which led to debt build up and rise in interest expenses in Q4FY17. Interest costs will decline in Q1FY18 as SEL has already received mobilisation advance of INR1.3bn from HAM projects. In addition, as execution on projects which involve JV partners will get completed, additional working capital will be released.
- **Working capital cycle** deteriorated in FY17 on account of: a) repayment of high-cost mobilisation advance to NHAI; and b) higher working capital utilisation in certain projects. Going ahead, working capital cycle is expected to improve due to: a) receipt of INR5.3bn mobilisation advance on new HAM projects; b) reduction in JV work from GKC and DMRC which requires higher funding support; and c) lower working capital requirement in HAM projects compared to EPC projects.
- **Loans given by SEL to SIPL** have reduced to INR4.3bn (INR5.3bn, as at March 2016 end).
- **Tax rate:** Management has guided for tax rate of 20% in FY18 since most of the work which will be on EPC projects, which avail Sec 80 (IA) benefits. SEL expects full tax rate in FY19 as the proportion of HAM projects, which do not avail 80 (IA) benefits, will increase in the top line.
- **HAM projects:** The company has already started work on the Rampur Kathgodam Pkg 1, Una Kodinar and Bhavnagar Talaja projects. It expects to receive 'appointed date' for Rampur Kathgodam Pkg 2 and BRT Tiger reserve boundary project in Q2FY18. It has received LoI for Udaipur bypass and Waranga-Mahagaon (Pkg-I) projects. It expects to achieve financial closure and start work on these projects by Q3FY17.

Financial snapshot

(INR mn)

Year to March	Q4FY17	Q4FY16	% change	Q3FY17	% change	FY17	FY18E	FY19E
Net revenues	10,329	8,580	20.4	8,648	19.4	33,203	37,143	42,971
Direct costs	8,106	6,900	17.5	6,986	16.0	26,552	29,702	34,363
Staff costs	379	315	20.1	319	18.7	1,366	1,528	1,768
Other expenses	748	456	64.1	405	84.9	1,729	1,934	2,238
Total expenditure	9,233	7,672	20.3	7,710	19.7	29,647	33,165	38,369
EBITDA	1,096	908	20.7	938	16.8	3,556	3,978	4,602
Depreciation	243	335	(27.7)	250	(2.9)	1,000	1,082	1,170
EBIT	853	573	49.0	688	24.0	2,556	2,897	3,432
Other income	218	225	(3.1)	60	261.3	333	479	276
Interest	355	293	21.2	243	46.1	992	1,270	1,140
Add: Prior period items	-	141	NA	-	-	-	-	-
Add: Exceptional items		(91)	NA					
Profit before tax	716	555	29.0	505	41.6	1,897	2,106	2,569
Provision for taxes	33	205	(83.7)	(19)	(276.6)	18	421	848
Reported profit	682	349	95.4	524	30.1	1,878	1,685	1,721
Adjusted profit	682	298	128.6	524	30.1	1,878	1,685	1,721
Equity capital	172	172		172		172	172	172
Diluted shares (mn)	172	172		172		172	172	172
Adjusted Diluted EPS	4.0	1.7	128.6	3.1	30.1	11.0	9.8	10.0
as % of net revenues								
Direct costs	78.5	80.4		80.8		80.0	80.0	80.0
Other expenses	7.2	5.3		4.7		5.2	5.2	5.2
EBITDA	10.6	10.6		10.8		10.7	10.7	10.7
Reported profit	6.6	3.5		6.1		5.7	4.5	4.0
Tax rate	4.7	37.0		(3.7)		1.0	20.0	33.0

Company Description

Founded in 1988, SEL is an infrastructure development and construction company focusing on roads and highways, irrigation and mining operations. SEL's expertise includes rehabilitating, upgrading, widening and strengthening roads and highways, construction of earthen dams, etc. The company is reputed for completing projects ahead of schedule and excellent quality of projects.

Investment Theme

SEL's revenue has grown at one of the fastest rates in the last five years in the construction space. It has been able to achieve this feat on back of: (1) its focus on roads, which is one of the fastest growing segments in construction space; (2) ownership of road projects via BOT route, enabling greater control; and (3) consistently completing work ahead of schedule.

The company has raised INR 4 bn by divesting 22.22% stake in Sadbhav Infrastructure Projects, the holding company for its BOT assets to PE investors. This would take care of its equity requirements of the ongoing projects.

Key Risks

SEL has exposure to the road BOT space, which entails upfront investments with returns generally being back-ended. While the company is currently well funded, it needs to win large amount of BOT projects to maintain its current growth momentum. This is likely to stretch SIPL's balance sheet and may lead to equity dilution.

With the company focusing on PPP projects, it is exposed to risks associated with gaining right-of-way on land stretches, execution risk, 'force majeure' risk, etc. Also, the focus on toll projects exposes it to the unpredictability of traffic growth.

Financial Statements

Key Assumptions

Year to March	FY16	FY17	FY18E	FY19E
Macro				
GDP(Y-o-Y %)	7.2	6.5	7.1	7.7
Inflation (Avg)	4.9	4.8	5.0	5.2
Repo rate (exit rate)	6.8	6.3	6.3	6.3
USD/INR (Avg)	65.0	67.5	67.0	67.0
Company				
Order intake (INR bn)	25	35	63	73
Y-o-Y growth (%)	11.0	42.1	79.4	15.9
Book-to-bill ratio (x)	2.3	2.3	2.8	3.1
Order backlog (INR bn)	75	77	103	133
Order backlog growth (%)	(8.7)	2.6	33.7	29.3
Revenue growth (% yoy)	7	4	12	16
Raw Material (% net rev)	81.0	80.0	80.0	80.0
Employee (% of net rev)	3.9	4.1	4.1	4.1
Other admin (% net rev)	4.7	5.2	5.2	5.2
Avg. Interest rate (%)	7.4	6.9	6.9	6.9
Depreciation rate (%)	9.5	9.5	10.0	10.0
Tax rate (%)	28.4	1.0	20.0	33.0
Dividend per share	0.7	0.7	0.7	0.7
Inc. in invts (INR mn)	(248)	65	-	-
Capex (INR mn)	(881)	(1,060)	(760)	(1,010)
Debtor days	113	151	170	157
Inventory days	25	18	18	21
Other cur. assets days	63	54	53	50
Payable days	58	59	75	83
Other creditors days	60	43	29	27
Provisions days	12	-	-	-
Loans & adv (% net rev)	18.3	16.2	15.7	15.7
Incremental debt	766	(4,296)	2,050	(1,200)

Income statement

(INR mn)

Year to March	FY16	FY17	FY18E	FY19E
Income from operations	31,863	33,203	37,143	42,971
Direct costs	25,805	26,552	29,702	34,363
Employee costs	1,228	1,366	1,528	1,768
Other Expenses	1,482	1,729	1,934	2,238
Total operating expenses	28,515	29,647	33,165	38,369
EBITDA	3,348	3,556	3,978	4,602
Depreciation	971	1,000	1,082	1,170
EBIT	2,377	2,556	2,897	3,432
Add: Other income	318	333	479	276
Less: Interest Expense	855	992	1,270	1,140
Add: Prior period items	141	-	-	-
Add: Exceptional items	(194)	-	-	-
Profit Before Tax	1,787	1,897	2,106	2,569
Less: Provision for Tax	467	18	421	848
Prior Period(Net of Tax)	141	-	-	-
Reported profit	1,320	1,878	1,685	1,721
Exceptional Items	(194)	-	-	-
Adjusted profit	1,373	1,878	1,685	1,721
Shares o/s (mn)	172	172	172	172
Adjusted Basic EPS	8.0	11.0	9.8	10.0
Diluted shares o/s (mn)	172	172	172	172
Adjusted Diluted EPS	8.0	11.0	9.8	10.0
Adjusted Cash EPS	13.7	16.8	16.1	16.9
Dividend per share (DPS)	0.7	0.7	0.7	0.7
Dividend Payout Ratio (%)	10.9	7.7	8.6	8.4

Common size metrics

Year to March	FY16	FY17	FY18E	FY19E
Operating expenses	89.5	89.3	89.3	89.3
EBITDA margins	10.5	10.7	10.7	10.7
Adj. profit margins	4.3	5.7	4.5	4.0

Growth ratios (%)

Year to March	FY16	FY17	FY18E	FY19E
Revenues	7.3	4.2	11.9	15.7
EBITDA	11.5	6.2	11.9	15.7
PBT	20.5	6.2	11.0	21.9
Adjusted profit	23.4	36.8	(10.3)	2.1
EPS	23.4	36.8	(10.3)	2.1

Infrastructure - Construction

Balance sheet (INR mn)				
As on 31st March	FY16	FY17	FY18E	FY19E
Share capital	172	172	172	172
Reserves & Surplus	14,721	16,437	17,978	19,554
Shareholders' funds	14,892	16,609	18,149	19,726
Short term borrowings	7,275	13,441	12,641	13,641
Long term borrowings	4,932	3,062	1,812	2,012
Total Borrowings	12,207	16,503	14,453	15,653
Long Term Liabilities	32	98	98	98
Def. Tax Liability (net)	(90)	(477)	(477)	(477)
Sources of funds	27,041	32,734	32,225	35,001
Gross Block	9,293	10,343	11,093	12,093
Net Block	5,918	5,222	5,334	5,176
Intangible Assets	12	7	13	11
Total Fixed Assets	5,931	5,229	5,347	5,187
Non current investments	5,629	5,694	5,694	5,694
Cash and Equivalents	166	230	428	590
Inventories	1,406	1,234	1,697	2,258
Sundry Debtors	10,372	17,010	17,589	19,378
Loans & Advances	5,832	5,381	5,834	6,749
Other Current Assets	5,524	4,950	5,417	5,932
Current Assets (ex cash)	23,135	28,574	30,537	34,317
Trade payable	3,703	4,910	7,282	8,283
Other Current Liab	4,116	2,083	2,500	2,504
Total Current Liab	7,819	6,993	9,781	10,787
Net Curr Assets-ex cash	15,316	21,581	20,755	23,529
Uses of funds	27,041	32,734	32,225	35,001
BVPS (INR)	86.8	96.8	105.8	115.0

Free cash flow (INR mn)				
Year to March	FY16	FY17	FY18E	FY19E
Reported Profit	1,125	1,878	1,685	1,721
Add: Depreciation	971	1,000	1,082	1,170
Interest (Net of Tax)	632	982	1,016	764
Others	(764)	(1,604)	(1,637)	(1,385)
Less: Changes in WC	3,612	4,678	4,751	4,786
Operating cash flow	(1,647)	(2,421)	(2,606)	(2,516)
Less: Capex	(881)	(1,060)	(760)	(1,010)
Free Cash Flow	(767)	(1,361)	(1,846)	(1,506)

Cash flow metrics				
Year to March	FY16	FY17	FY18E	FY19E
Operating cash flow	(1,647)	(2,421)	(2,606)	(2,516)
Investing cash flow	1,108	3,399	1,408	5,246
Financing cash flow	672	(4,296)	2,050	(1,200)
Net cash Flow	132	(3,318)	852	1,530
Capex	881	1,060	760	1,010
Dividend paid	(145)	(145)	(145)	(145)

Profitability and efficiency ratios				
Year to March	FY16	FY17	FY18E	FY19E
ROAE (%)	9.7	11.9	9.7	9.1
ROACE (%)	10.4	9.6	10.3	10.9
Inventory Days	25	18	18	21
Debtors Days	113	151	170	157
Payable Days	115	101	103	109
Cash Conversion Cycle	23	67	85	69
Current Ratio	3.0	4.1	3.2	3.2
Gross Debt/EBITDA	3.6	4.6	3.6	3.4
Gross Debt/Equity	0.8	1.0	0.8	0.8
Adjusted Debt/Equity	0.8	1.0	0.8	0.8
Net Debt/Equity	0.8	1.0	0.8	0.8
Interest Coverage Ratio	2.8	2.6	2.3	3.0

Operating ratios				
Year to March	FY16	FY17	FY18E	FY19E
Total Asset Turnover	1.2	1.1	1.1	1.3
Fixed Asset Turnover	5.6	6.0	7.0	8.2
Equity Turnover	2.2	2.1	2.1	2.3

Valuation parameters				
Year to March	FY16	FY17	FY18E	FY19E
Adj. Diluted EPS (INR)	8.0	11.0	9.8	10.0
Y-o-Y growth (%)	23.4	36.8	(10.3)	2.1
Adjusted Cash EPS (INR)	13.7	16.8	16.1	16.9
Diluted P/E (x)*	10.8	7.9	8.8	8.6
P/B (x)	3.6	3.2	3.0	2.7
EV / Sales (x)*	0.8	0.9	0.8	0.7
EV / EBITDA (x)*	8.0	8.8	7.3	6.5
Dividend Yield (%)	0.2	0.2	0.2	0.2

* for implied construction business

Peer comparison valuation

Name	Market cap (USD mn)	Diluted P/E (X)		P/B (X)		ROAE (%)	
		FY18E	FY19E	FY18E	FY19E	FY18E	FY19E
Sadbhav Engineering	837	16.1	16.9	3.0	2.7	9.7	9.1
Ashoka Buildcon	580	25.4	19.9	2.0	1.9	2.2	5.1
Nagarjuna Construction Co	734	19.7	13.2	1.3	1.2	6.8	9.4
Simplex Infrastructures Ltd	323	26.3	13.9	1.2	1.1	4.8	8.5
Median	-	25.9	16.9	1.6	1.5	5.8	8.7
AVERAGE	-	25.8	19.9	1.9	1.8	5.9	8.0

Source: Edelweiss research

Additional Data

Directors Data

Mr. Vishnubhai M. Patel	Chairman and Managing Director	Mr. Shashin V. Patel	Joint Managing Director
Mr. Vikram R. Patel	Executive Director	Mr. Vasistha C. Patel	Executive Director
Mr. Nitin R. Patel	Executive Director & CFO	Mr. Vipul H. Patel	Executive Director
Mr. Sandip A. Sheth	Independent Non-Executive Director	Mr. Sandip V. Patel	Independent Non-Executive Director
Mr. Atul N. Ruparel	Independent Non-Executive Director	Mr. Mirat N. Bhadlawala	Independent Non-Executive Director
Mrs. Purvi S. Parikh	Independent Non-Executive Director	Mr. Arun S. Patel	Independent Non-Executive Director

Auditors - Surana Maloo & Co.

**as per last annual report*

Holding – Top 10

	Perc. Holding		Perc. Holding
Max New York Life Ins Co	6.32	HDFC Asset Management	5.58
Prudential ICICI Asset Management	5.51	SBI Fund Management	5.27
ICICI Prudential Life Insurance Company	5.03	Tata Asset Management	4.31
Nomura	3.62	DSP Blackrock Investment	2.91
Abu Dhabi Investment Authority	1.72	Government Pension Fund - Global	1.52

**as per last available data*

Bulk Deals

Data	Acquired / Seller	B/S	Qty Traded	Price
No Data Available				

**as per last available data*

Insider Trades

Reporting Data	Acquired / Seller	B/S	Qty Traded
30 Mar 2017	Truptiben Nileshbhai Patel	Buy	650000.00
30 Mar 2017	Bhavnaben Vikramkumar Patel	Buy	650000.00
30 Mar 2017	Rajshreeben Vishnubhai Patel	Sell	650000.00
30 Mar 2017	Rekhaben Vasisthakumar Patel	Buy	650000.00
30 Mar 2017	Shashin Vishnubhai Patel	Sell	650000.00

**as per last available data*

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Coverage group(s) of stocks by primary analyst(s): Infrastructure - Construction

Ahluwalia Contracts, Ashoka Buildcon, Hindustan Construction Co., J Kumar Infraprojects, KNR Constructions, NBCC, Nagarjuna Construction Co, PNC Infratech, Sadbhav Engineering, Simplex Infrastructures Ltd, Supreme Infrastructure

Recent Research

Date	Company	Title	Price (INR)	Recos
29-May-17	NBCC	Strong margins aid profitability; <i>Result Update</i>	195	Hold
26-May-17	PNC Infratech	Tough, but only temporary pain; <i>Result Update</i>	145	Buy
23-May-17	Nagarjuna Construction	Interest cost savings aid profitability; <i>Result Update</i>	95	Buy

Distribution of Ratings / Market Cap

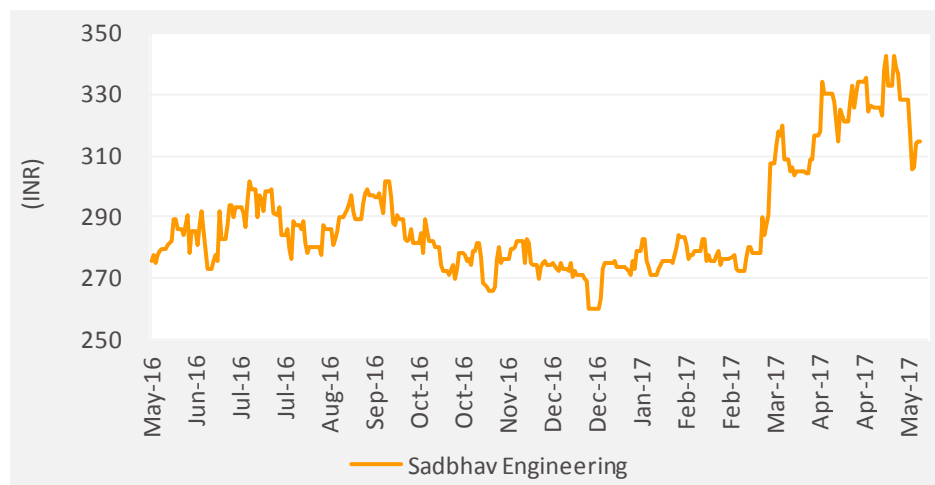
Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution*	161	67	11	240
* 1stocks under review				
	> 50bn	Between 10bn and 50 bn	< 10bn	
Market Cap (INR)	156	62	11	

Rating Interpretation

Rating	Expected to
Buy	appreciate more than 15% over a 12-month period
Hold	appreciate up to 15% over a 12-month period
Reduce	depreciate more than 5% over a 12-month period

One year price chart



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