

RESULT UPDATE

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VASCON ENGINEERS LTD (VEL)

PRICE: RS.39
 TARGET PRICE: RS.57

RECOMMENDATION: BUY
 FY20E PE: 9.0x

Vascon Engineers (VEL) reported strong revenue growth in Q3FY18 due to high contribution from real estate business in the quarter. Net sales for the quarter grew at 84.8% yoy to Rs 935 mn with EBITDA turning positive at Rs.65mn and PAT going up to Rs.25 mn, which was inline with estimates. But the contribution from EPC segment was below our estimates at Rs 520 mn Vs estimates of Rs 571 mn as its new projects would contribute meaningfully from Q4FY18 onwards. VEL has external order backlog of Rs Rs 6.7 bn and internal order book of Rs 2.3 bn at the end of Q3FY18. VEL has added Rs 3.7 bn of new orders in 9MFY18 and is well placed in order worth Rs 1.6 bn which is at final stage of awarding. Further, it has strong bid pipeline of Rs 10 bn of new orders which is expected to be finalized in next 8-12 months. The company is expected to re-launch Windermere project in Pune by end of February 2018 and would launch affordable housing project at Katvi, Pune in April 2018. It also intends to launch four more real estate projects in FY19E which includes two projects in affordable housing space. Its subsidiary GMP is doing well after exiting services business. We have revised our estimates for EPC business in FY18E and FY19E assuming some shift in execution of large size project. We maintain our positive view on the company based on pickup in order book and traction in real estate business. We maintain Buy on VEL with revised SOTP based target price of Rs 57 (Vs Rs 60 earlier).

Summary table – Consolidated

(Rs mn)	FY18E	FY19E	FY20E
Revenue	5360	7066	9442
Growth (%)	9.4	31.8	33.6
EBITDA	419	761	1071
EBITDA margin (%)	7.8	10.8	11.3
PBT	173	569	931
PAT	134	423	688
EPS	0.8	2.6	4.3
EPS Growth (%)	594.5	215.0	62.6
CEPS (Rs)	2	4	5
Book value (Rs/share)	39	42	46
Dividend per share (Rs)	0	0	0
ROE (%)	2.0	6.2	9.3
ROCE (%)	2.7	6.5	9.7
Net cash (debt)	(1715)	(994)	(1113)
NW Capital (Days)	285	205	189
P/E (x)	46.2	14.7	9.0
P/BV (x)	1.0	0.9	0.8
EV/EBITDA (x)	19.5	9.8	7.1
EV/Sales (x)	1.5	1.1	0.8

Source: Company, Kotak Securities – Private Client Research

Standalone Result Table

Year to March (INR Mn.)	Q3FY18	Q3FY17	% Chg	Q2FY18	% Chg
Net Revenues	935	506	84.8	546	71.3
Raw Materials Cost	672	358	87.5	327	105.5
Gross Profit	263	148	78.3	219	20.2
Employee Expenses	130	78	67.3	111	16.9
Other Expenses	69	93	(25.8)	50	38.6
Operating Expenses	871	529	64.6	488	78.5
EBITDA	65	(23)	NA	58	10.8
EBITDA margin (%)	6.9	-4.5		10.7	
Depreciation	20	17	16.8	18	6.6
Other income	17	128	(86.4)	30	(42.8)
Net finance expense	38	67	(43.2)	55	(31.5)
Profit before tax	25	22	13.9	15	62.9
Provision for taxes	-	7	(100.0)	-	-
Reported net profit	25	15	64.0	15	62.9
As % of net revenues					
COGS	71.8	70.8		59.9	
Employee cost	13.9	15.4		20.4	
Other Expenses	7.4	18.4		9.1	
Operating expenses	93.1	104.5		89.3	
EBITDA	6.9	(4.5)		10.7	
Reported net profit	2.6	3.0		2.8	
Tax rate (% of PBT)	-	30.6		-	

Source: Company

Strong revenue growth led by higher real estate revenue

The standalone net sales for the quarter grew sharply by 84.8% yoy to Rs 935 mn as against estimates of Rs 684 mn due to high revenue recognition in real estate business at Rs 415 mn Vs Rs 44 mn on yoy. In EPC (external) segment, the revenue for the quarter grew by 12.4% yoy to Rs 520 mn Vs estimates of Rs 571 mn as its large size new projects did not contribute significantly. We expect the execution in the EPC segment to pick up from Q4FY18. Its subsidiary GMP is also doing well after exiting services business with Rs 1.18bn revenue in 9MFY18. EBITDA for the quarter turned positive to Rs 65 mn (Vs estimates of Rs 68 mn) with EBITDA

margins at 6.9% which was lower than our estimates on account of higher expenses in real estate segment due to increase marketing spend and higher employee expenses in the real estate segment. The company has added new employees for sales and marketing of real estate division. PAT for the quarter grew by 64% yoy to Rs 25 mn which was inline with our estimates. The tax rate for quarter was nil as company is setting off carry forward losses and expects to continue it in coming quarters.

Targets to grow its order book

VEL has external order backlog of Rs Rs 6.7 bn and internal order book of Rs 2.3 bn at the end of Q3FY18. VEL has added Rs 3.7 bn of new orders in 9MFY18 and is well placed in order worth Rs 1.6 bn which is at final stage of awarding. Further, it has strong bid pipeline of Rs 10 bn of new orders which is expected to be finalized in next 8-12 months. Based on the current pipeline of order VEL is expected to cross Rs 5 bn of order inflows in FY18 and targets to increase its order inflows further in next year. The company is at final stage of discussion with its banker SBI for higher bank guarantee limit and expect to get it soon. Besides this, it would be eligible to bid for government project directly as it would be able to meet prequalification criteria of 3 years of profitable track record. These would help VEL to enhance its order book further. Based on current gross block, VEL can execute Rs 10 bn of EPC work in a year.

Update real estate projects

VEL is focused on revamping its real estate business as it has sold Rs 1.4 bn of real estate projects in 9MFY18 as against Rs 600 mn in FY17. The company has witnessed robust response to its recent launches like Platinum square phase II and Forest Edge in Pune. Further, the company is expected to re-launch Windermere project in Pune by end of February 2018 and would also launch affordable housing project at Katvi, Pune in April 2018, depending upon approvals. It also intends to launch four more real estate projects in FY19E which includes two projects in affordable housing space.

Outlook and valuation

We maintain positive view on the company based on pickup in order book and traction in real estate business. We feel the company could be a good turnaround story in FY19E with focus on affordable housing in both its EPC and real estate segment. We have revised our estimates for EPC business in FY18E and FY19E assuming some shift in execution of large size project. Based on FY19E and FY20E consolidated EPS of Rs.2.6 and 4.3, the stock is trading at PE of 14.7x and 9.0x respectively. We have valued the company on sum of the parts (SOTP) based valuation. We maintain **BUY** on VEL with revised SOTP based target price of Rs 57 (Vs Rs 60 earlier).

We maintain **BUY** on Vascon Engineers Ltd with a price target of Rs.57

Valuation Table

Segment	Multiple	Per Share
EPC Business	8	27
Real Estate	1	27
GMP	9	13
Net Debt		10
Total Value		57

Source: Kotak Securities Private Client Research

Revision in consolidated earnings estimates

	Previous			Revised			% Change		
	FY18E	FY19E	FY20E	FY18E	FY19E	FY20E	FY18E	FY19E	FY20E
Revenue	5675	7643	9866	5360	7066	9442	-5.6	-7.5	-4.3
EBITDA margin (%)	7.7	10.8	11.4	7.8	10.8	11.3	7 bps	1 bps	-8 bps
APAT	149	468	729	134	423	688	-10.0	-9.6	-5.6
AEPS	0.9	2.9	4.5	0.8	2.6	4.3	-10.0	-9.6	-5.6

Source: Kotak Securities - Private Client Research

RATING SCALE

Definitions of ratings

BUY	– We expect the stock to deliver more than 12% returns over the next 12 months
ACCUMULATE	– We expect the stock to deliver 5% - 12% returns over the next 12 months
REDUCE	– We expect the stock to deliver 0% - 5% returns over the next 12 months
SELL	– We expect the stock to deliver negative returns over the next 12 months
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NA	– Not Available or Not Applicable. The information is not available for display or is not applicable
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NOTE	– Our target prices are with a 9-month perspective. Returns stated in the rating scale are our internal benchmark.

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