February 12, 2019

Rating matrix

Rating	:	Hold
Target	:	₹ 295
Target Period	:	12 months
Potential Upside	:	7%

What's Changed?

Target	Changed from ₹ 300 to ₹ 295
EPS FY20E	Changed from ₹ to ₹
EPS FY21E	Introduced at ₹
Rating	Unchanged

Quarterly Performance

	Q3FY19	Q3FY18	YoY (%)	Q2FY19	QoQ (%)
Revenue	661.9	864.7	(23.5)	752.0	(12.0)
EBITDA	49.3	77.7	(36.5)	62.8	(21.5)
EBITDA (%)	7.4	9.0	-153 bps	8.4	-90 bps
APAT	15.4	30.1	(48.9)	35.8	(57.2)

Key Financials

₹ Crore	FY18	FY19E	FY20E	FY21E
Revenue	3,457	3,350	4,207	5,312
EBITDA	292	261	332	429
EBITDA (%)	8.4	7.8	7.9	8.1
Net Profit	144	113	155	217
EPS (₹)	24.1	17.9	25.5	36.7

Valuation summary

	FY18	FY19E	FY20E	FY21E
P/E	11.4	15.4	10.8	7.5
Target P/E	12.3	16.5	11.6	8.0
EV / EBITDA	6.3	7.0	5.9	4.3
P/BV	1.3	1.2	1.1	0.9
RoNW (%)	12.3	8.1	10.3	13.4
RoCE (%)	22.0	16.6	19.5	23.0

Stock data

Particular	Amount
Market Capitalization (₹ Crore)	1,493
Total Debt (FY19E) (₹ Crore)	545
Cash and Investments (FY19E) (₹ Crore)	360
EV (FY19E) (₹ Crore)	1,313
52 week H/L (₹)	579 / 244
Equity capital (₹ crore)	10.9
Face value	₹ 2

Price performance (%)

	1M	3M	6M	12M
VA Tech	(12.8)	(7.3)	(26.7)	(52.1)
L&T	(9.0)	(8.9)	(1.4)	(6.2)
Thermax	(6.9)	1.4	(1.0)	(9.6)

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VA Tech Wabag (VATWAB)

₹ 275

Weak Q3, receivables a continued concern...

- VA Tech Wabag (Wabag) reported dismal Q3FY19 numbers
- Wabag's revenues fell 23.5% YoY to ₹ 661.9 crore. Lower topline was due to muted execution in both domestic (down 2.3% YoY) & overseas segment (down 23.4%YoY). Overseas segment contributed ~66% whereas domestic segment contributed ~33% to the topline
- Absolute EBITDA declined 36.5% YoY to ₹ 49.3 crore. EBIDTA margins came in at 7.4% vs. 9% YoY. Lower margins were mostly on account of provisioning of doubtful debts in 'other expenses' in addition to forex (translation) loss during the quarter
- Wabag's finance cost increased 32% YoY on account of higher interest cost for working capital. Accordingly, Wabag's net profit declined 48.9% YoY to ₹ 15.4 crore

Healthy inflows in 9MFY19, strong guidance for Q4FY19

Wabag witnessed order inflows of ₹ 3566 crore in 9MFY19. Key orders won include SWTP in Saudi Arabia (₹ 933 crore), desalination order in Tunisia (₹ 596 crore), STP order in Doha (₹ 555 crore), etc. The management continues to guide for strong order inflow of ₹ 5300-5700 crore for the full year FY19E. This is on the back of orders expected from large projects like the desalination and sewage treatment plants in Chennai, Mumbai (₹ 11000 crore) and Delhi (₹ 1500 crore). Wabag has already been declared L1 for the Mumbai project and expects at least one order worth ₹ 4000 crore in the next six to nine months. The order backlog is now at ₹ 9061 crore (including framework order of ₹ 700 crore).

Namami Gange order wins to accelerate growth

Under the Namami Gange action plan, Wabag has already won ₹ 147 crore WWTP, ₹ 253 crore sewage and related projects. With decision-making expected to improve in the next few months, Wabag is now expecting large orders 'integrated city management projects' up to ₹ 5000 crore for cities of Kanpur, Allahabad, Patna and Kolkata. Wabag has already been declared L1 bidder for Kolkata project (₹ 550-600 crore). It is also expecting to bag the Patna order in Q4FY19. As these large projects are likely to follow the hybrid model, Wabag may also raise up to ₹ 400 crore for meeting equity contribution criteria. All such projects are likely to be centrally funded to the tune of 40%. The rest 60% is to be funded via debt and equity. Of the 60%, 26% equity to be held by the key technology partner with a three year lock-in and 15 years O&M contract.

Receivables a continued concern; maintain HOLD

Net working capital days for Wabag have deteriorated from 98 days in FY18 to 122 days in H1FY19. Receivables of ~₹ 550 crore from Genco projects are also getting delayed due to various reasons. However, the management is expecting ₹ 150 crore in Q4FY19E. A further delay in their receipt can significantly strain the balance sheet (as interest outgo continues but interest is not paid on receivables). On the positive side, Wabag is witnessing significant order opportunities from overseas markets from geographies like South East Asia, Latin America, Middle East regions and Sub-Saharan regions. Thus, we expect order backlog to grow at 23.9% CAGR in FY18-21E. With strong execution capabilities, we expect revenue, EBITDA and PAT CAGR of 15.4%, 13.7% and 15.1%, respectively. We value the company at 8x FY21E earnings to arrive at a target price of ₹ 295. We maintain HOLD rating on the stock.

Variance analysis

	Q3FY19	Q3FY19E	Q3FY18	YoY (%)	Q2FY19	QoQ (%)	Comments
Revenue	661.9	999.2	864.7	-23.5	752.0	(12.0)	Key overseas projects nearing completion resulting in lower YoY sales
Cost of sales & Services	505.0		682.3	(26.0)	595.7	(15.2)	
Employees Remunaration & Benefits	71.0	63.0	66.9	6.2	63.6	11.7	
Other Expenses & Forex loss/(gain)	34.3	43.0	35.1	(2.3)	29.3	17.1	
Total operating expenses	612.6	910.3	787.0	(22.2)	689.2	(11.1)	
EBITDA	49.3	88.9	77.7	(36.5)	62.8	(21.5)	
EBITDA Margin (%)	7.4	8.9	9.0	-153 bps	8.4	-90 bps	Forex loss arising from translation
Depreciation	4.1	5.3	4.3	(4.8)	4.2	(1.4)	
Finance charges	18.8	18.8	14.2	32.0	17.7	6.3	
PBT	26.9	65.4	60.0	(55.1)	41.4	(35.0)	
Tax	14.9	21.9	24.8		14.1	5.3	
PAT	12.1	43.5	35.1	(65.7)	27.3	(55.8)	
Minority Interest	-3.3	9.5	5.8		-7.3	(55.0)	
Share of profit in associate	0.0	0.4	0.7		1.2		
Adjusted PAT	15.4	34.4	30.1	(48.9)	35.8	(57.2)	
Key Metrics	9MFY19						
India revenue	221.6		226.8	(2.3)	269.5	(17.8)	
RoW revenue	496		648	(23.4)	515	(3.7)	

Source: Company, ICICI Direct Research

Change in estimates

	FY18		FY19E			FY20E		FY21E
(₹ Crore)	Actual	Old	New	% Change	Old	New	% Change	Introduced
Revenue	3,457.3	4,041.3	3,350.1	(17.1)	4,697.7	4,207.1	(10.4)	5,311.6
EBITDA	291.8	338.7	260.7	(23.0)	398.5	331.6	(16.8)	429.3
EBITDA Margin (%)	8.4	8.4	7.8	-62 bps	8.5	7.9	-62 bps	8.1
PAT	131.5	151.9	97.6	(35.7)	180.7	139.2	(22.9)	200.7
EPS (₹)	24.1	27.8	17.9	(35.8)	33.0	25.5	(22.8)	36.7

Source: Company, ICICI Direct Research

Assumptions

	Actual	Actual		Estimated	
	FY17	FY18	FY19E	FY20E	FY21E
Order Intake	3,620	3,193	5,600	5,700	5,800
Order Backlog	8,194	7,743	9,651	13,151	14,744
EBITDA margin (%)	9.2	8.4	7.8	7.9	8.1

Source: Company, ICICI Direct Research

Company Analysis

VA Tech Wabag - Leading global water treatment player

VA Tech Wabag (Wabag) is a leading MNC in the water treatment space (water desalination, sewage water treatment, waste water treatment, etc), with a global presence. The company operates on an asset light-EPC led model in water treatment projects across municipal & industrial segments. It focuses on design & engineering while outsourcing civil construction & erection jobs. Wabag has executed over 2,250 projects till date and has a market share of ~14% in the Indian market. The company garners a higher EBITDA margin of ~13-14% across its India business, 8-9% across the India international business and 5-6% across the Europe segment taking overall EBITDA margin to 8-10%.

Exhibit 1: Order book composition

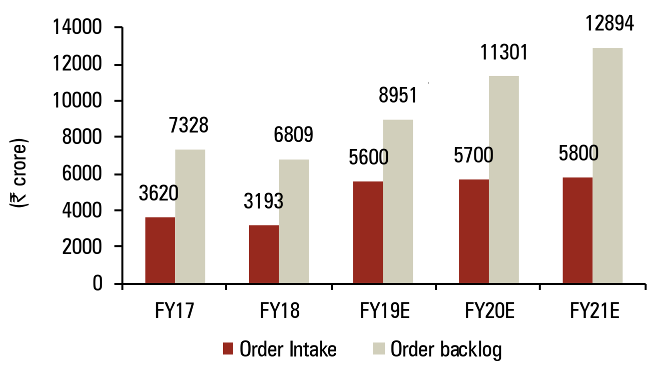
(₹ Crore)	EPC		O&M		Total
	Municipal	Industrial	Municipal	Industrial	
Wabag India	3096	1366	1293	141	5896
Wabag Overseas	2002	317	98	49	2465
Framework Contracts					700
Total	5097	1682	1391	190	9061

Source: Company, ICICI Direct Research

Engineering excellence and asset light business model

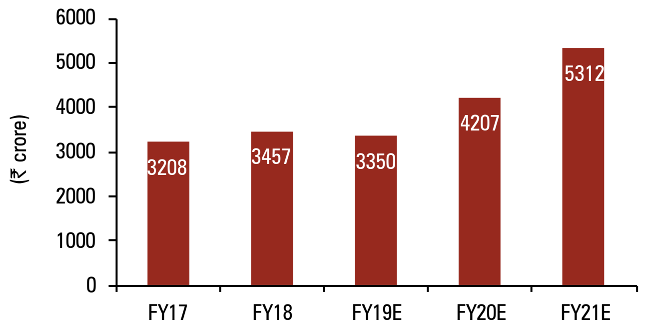
VA Tech Wabag (Wabag) operates on an asset light EPC model, thereby manifesting a lean balance sheet. With growing concern on access to clean water and urgent measures to solve the issue of depleting water resources, the investment in water treatment is likely to increase manifold globally. Accordingly, Wabag is expected to benefit significantly by leveraging its strong domestic presence and rising global footprint. The company's strong book-to-bill ratio of ~3.5x provides revenue visibility for over two years.

Exhibit 2: Annual trend – Order intake and backlog



Source: Company, ICICI Direct Research

Exhibit 3: Revenue growth to be driven by strong order intake …

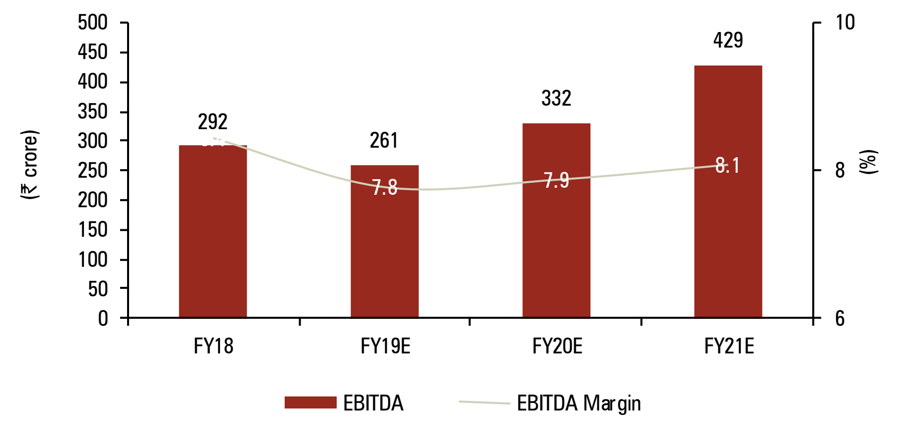


Source: Company, ICICI Direct Research

Stable EBITDA margin over next two years…

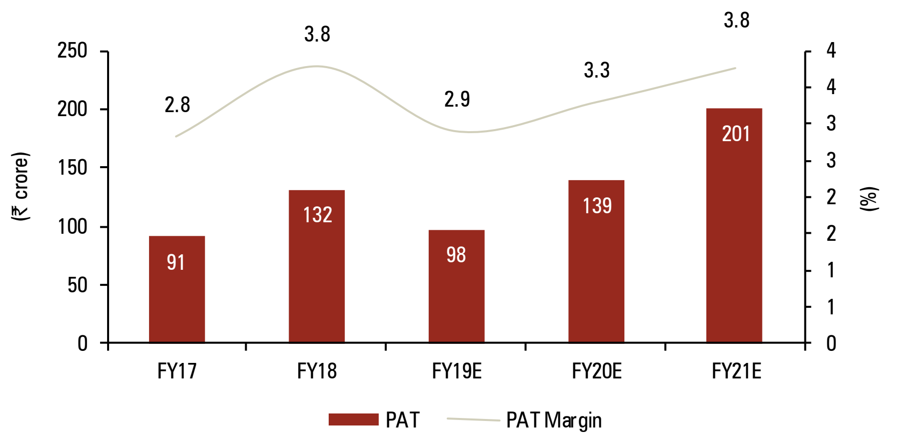
Wabag has earned EBITDA margins of 8.4% in FY18. Going ahead, margins are likely to improve on the back of shifting of its operations base from high cost countries to low cost local markets. Also, Wabag's focus on large-sized projects is likely to help the company in earning superior margins. Accordingly, we expect EBITDA margins to improve to 8.1% in FY20E. Broadly, we expect stable EBITDA margins over the next two years.

Exhibit 4: EBITDA and EBITDA margin trend



Source: Company, ICICI Direct Research

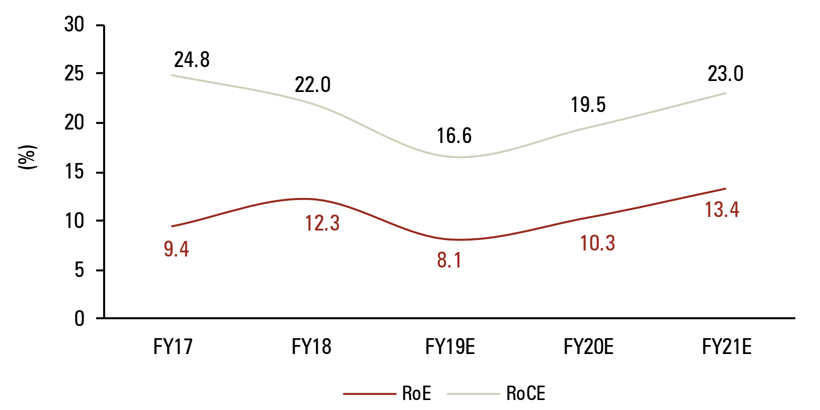
Exhibit 5: PAT trend



Source: Company, ICICI Direct Research

Return ratios likely to remain stable over FY18-21E

Exhibit 6: RoE and RoCE



Source: Company, ICICI Direct Research

Outlook and valuation

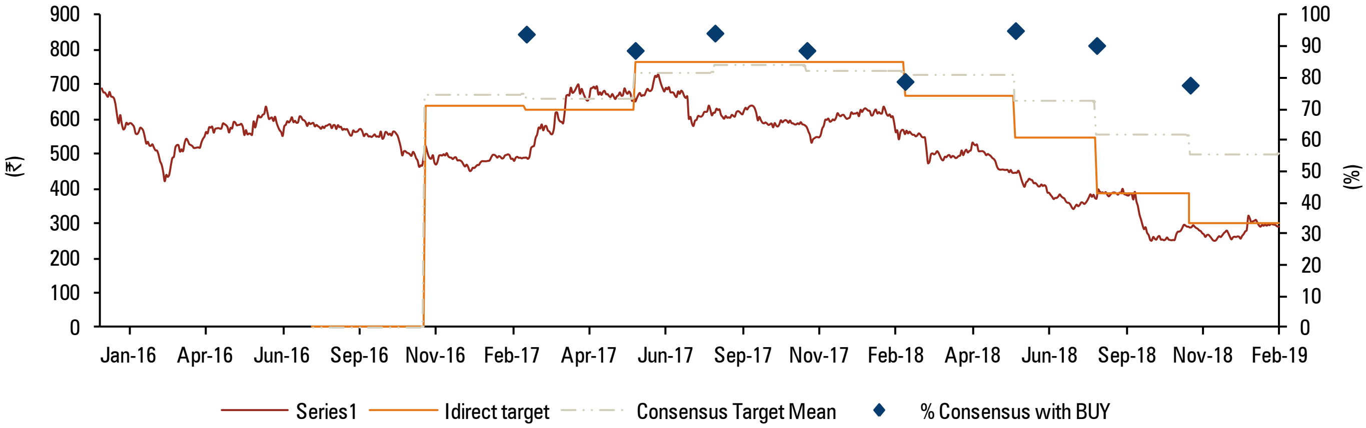
Strong management pedigree and execution capabilities

Wabag has a strong management team in place. The company continuously conducts an enterprise-wide exercise that results in reengineering of processes, realignment of strengths and reorganisation of business verticals. Since 2007, the company operated through four strategic business units (SBUs) comprising municipal business group (MBG), industrial water group (IWG), operations business group (OBG) and desalination business group (DBG) earlier known as international business group (IBG).

As part of organisational realignment, Wabag fine-tuned its business strategy and created four clusters — India, Europe, Middle East & Africa (MEA) and LatAm. This cluster approach tries to strike a balance between centralisation and decentralisation leading to enhanced capacity, better collaboration, greater competitiveness and increased competency

Net working capital days for Wabag have deteriorated from 98 days in FY18 to 122 days in H1FY19. Receivables of ~₹ 550 crore from Genco projects are also getting delayed due to various reasons. However, the management is expecting ₹ 150 crore in Q4FY19E. A further delay in its receipt can significantly strain the balance sheet (as interest outgo continues but interest is not paid on receivables). On the positive side, Wabag is witnessing significant order opportunities from overseas markets from geographies like South East Asia, Latin America, Middle East regions and Sub-Saharan regions. Thus, we expect order backlog to grow at 23.9% CAGR in FY18-21E. With strong execution capabilities, we expect revenue, EBITDA and PAT CAGR of 15.4%, 13.7% and 15.1%, respectively. We value the company at 8x FY21E earnings to arrive at a target price of ₹ 295. We maintain **HOLD** rating on the stock.

Recommendation history vs. consensus



Source: Bloomberg, Company, ICICI Direct Research, Initiated coverage on December 17, 2014

Key events

Date	Event
Oct-18	WABAG secures INR 1,000 crore worth order in the Middle East (EPC order worth for Jubail and Yanbu)
Nov-18	Wabag deliveers first and the largest sewage treatment project implemented under the "Namami Gange" mission
Nov-18	WABAG secures INR 600 crore order in Tunisia
Jan-19	WABAG secures Desalination Order from Mangalore Refinery
Feb-19	Kovser.

Source: Company, ICICI Direct Research

Top 10 Shareholders

Rank	Name	Latest Filing Date	% O/S	Position (m)	Change (m)
1	Mittal (Rajiv)	31-12-2018	17.76%	9.71M	0
2	SBI Funds Management Pvt. Ltd.	31-12-2018	4.96%	2.71M	-0.67M
3	Sumitomo Corp	31-12-2018	4.49%	2.46M	0
4	UTI Asset Management Co. Ltd.	31-12-2018	4.18%	2.29M	+0.41M
5	Varadarajan (S)	31-12-2018	4.00%	2.19M	0
6	Old Bridge Capital Management Pvt Ltd	31-12-2018	3.08%	1.69M	+0.16M
7	Sengupta (Amit)	31-12-2018	2.94%	1.61M	-0.07M
8	Saraf (Shiv Narayan)	31-12-2018	2.93%	1.60M	0
9	IDFC Asset Management Company Private Limited	30-09-2018	2.35%	1.28M	-1.94M
10	KBI Global Investors Ltd	31-12-2018	2.19%	1.20M	+0.00M

Source: Reuters, ICICI Direct Research

Shareholding Pattern

(in %)	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18
Promoter	24.7	24.7	24.7	24.7	24.7
FII	25.8	24.7	21.3	20.8	20.5
DII	22.5	20.1	23.5	12.9	9.1
Others	27.0	30.5	30.5	41.6	45.7

Recent Activity

Investor name			Investor name		
Investor name	Value	Shares	Investor name	Value	Shares
Norges Bank Investment Management (NBIM)	+3.40M	+0.91M	IDFC Asset Management Company Private Limited	-7.86M	-1.94M
UTI Asset Management Co. Ltd.	+1.53M	+0.41M	Amundi Hong Kong Limited	-6.57M	-1.94M
BNP Paribas Asset Management France SAS	+0.87M	+0.23M	SBI Funds Management Pvt. Ltd.	-2.49M	-0.67M
Old Bridge Capital Management Pvt Ltd	+0.58M	+0.16M	Aditya Birla Sun Life AMC Limited	-2.25M	-0.60M
KBI Global Investors Ltd	+0.02M	+0.00M	BNP Paribas Asset Management Asia Limited	-2.57M	-0.47M

Source: Reuters, ICICI Direct Research

Financial summary

Profit and loss statement				₹ Crore
(Year-end March)	FY18	FY19E	FY20E	FY21E
Total operating Income	3,457.3	3,350.1	4,207.1	5,311.6
Growth (%)	*7.8*	*(3.1)*	*25.6*	*26.3*
Cost of sales	2,733.0	2,646.6	3,311.0	4,169.6
Decrease in inventory	0.6	0.6	0.8	1.0
Employees Remunaration	263.7	271.4	349.2	440.9
Other expenses	168.2	170.9	214.6	270.9
Total Operating Expenditure	3,165.5	3,089.4	3,875.5	4,882.3
EBITDA	291.8	260.7	331.6	429.3
Growth (%)	*(1.6)*	*(10.6)*	*27.2*	*29.5*
Depreciation	17.8	21.0	25.0	29.0
Interest	57.7	70.0	72.8	74.9
Other Income	5.7	3.0	5.0	8.0
PBT	221.9	172.7	238.8	333.4
Total Tax	77.4	59.6	83.6	116.7
PAT	144.5	113.1	155.2	216.7
Growth (%)	*(8.7)*	*(21.7)*	*37.2*	*39.6*
Share of profit in associate	2.6	4.5	6.0	6.0
Adjusted PAT	131.5	97.6	139.2	200.7
EPS (₹)	24.1	17.9	25.5	36.7

Source: Company, ICICI Direct Research

Cash flow statement				₹ Crore
(Year-end March)	FY18	FY19E	FY20E	FY21E
Profit before Tax	221.9	172.7	238.8	333.4
Add: Depreciation	17.8	21.0	25.0	29.0
(Inc)/dec in Current Assets	(425.4)	54.2	(685.2)	(658.9)
Inc/(dec) in CL and Provisions	41.3	(108.2)	440.8	575.8
Others	(25.4)	7.4	(15.8)	(49.8)
CF from operating activities	(169.7)	147.1	3.6	229.5
(Inc)/dec in Investments	(8.4)	0.0	0.0	0.0
(Inc)/dec in Fixed Assets	(8.0)	(37.0)	(40.0)	(36.0)
Others	0.0	0.0	0.0	0.0
CF from investing activities	(16.4)	(37.0)	(40.0)	(36.0)
Issue/(Buy back) of Equity	0.0	0.0	0.0	0.0
Inc/(dec) in loan funds	168.2	67.6	15.0	16.0
Dividend paid & dividend tax	(21.9)	(21.9)	(24.6)	(27.3)
Inc/(dec) in Sec. premium	0.0	0.0	0.0	0.0
Others	(57.7)	(70.0)	(72.8)	(74.9)
CF from financing activities	88.7	(24.2)	(82.4)	(86.2)
Net Cash flow	(91.8)	88.9	(113.8)	115.3
Opening Cash	363.1	271.3	360.2	246.4
Closing Cash	271.3	360.2	246.4	361.7

Source: Company, ICICI Direct Research

Balance sheet				₹ Crore
(Year-end March)	FY18	FY19E	FY20E	FY21E
Liabilities				
Equity Capital	10.9	10.9	10.9	10.9
Reserve and Surplus	1,128.7	1,273.4	1,405.0	1,579.4
Total Shareholders funds	1,139.6	1,284.3	1,416.0	1,590.4
Total Debt	477.3	544.9	559.9	575.9
Deferred Tax Liability	12.9	12.9	12.9	12.9
Others LT liabilities	68.8	117.6	119.7	121.8
Long term provision	13.9	20.0	20.0	20.0
Minority interest	33.8	33.8	33.8	33.8
Total Liabilities	1,394	1,606	1,738	1,931
Assets				
Gross Block	216.3	238.3	273.3	308.3
Less: Acc Depreciation	51.7	72.7	97.7	126.7
Net Block	164.6	165.6	175.6	181.6
Capital WIP	0.0	15.0	20.0	21.0
Total Fixed Assets	172.4	253.8	268.8	275.8
Deferred Tax asset	102.9	102.9	102.9	102.9
Investments	15.0	15.0	15.0	15.0
Inventory	38.2	37.8	47.3	59.6
Debtors	2,456.1	2,233.4	2,804.7	3,319.7
Loans and Advances	34.8	34.4	43.0	54.2
Other Current Assets	305.4	335.0	420.7	531.2
Cash	222.7	311.6	197.8	313.1
Bank Balance	48.6	48.6	48.6	48.6
Total Current Assets	3,105.9	3,000.8	3,562.2	4,326.3
Creditors	1,617.6	1,470.3	1,839.4	2,316.4
Provisions	55.4	53.6	67.3	85.0
Total Current Liabilities	2,422.4	2,326.9	2,780.6	3,370.2
Net Current Assets	683.5	673.9	781.6	956.1
Others Assets	420.3	560.0	570.0	580.0
Application of Funds	1,394	1,606	1,738	1,931

Source: Company, ICICI Direct Research

Key ratios				
(Year-end March)	FY18	FY19E	FY20E	FY21E
Per share data (₹)				
EPS	24.1	17.9	25.5	36.7
Cash EPS	27.3	21.7	30.0	42.0
BV	208.5	234.9	259.0	290.9
DPS	4.0	4.0	4.5	5.0
Cash Per Share	40.7	57.0	36.2	57.3
Operating Ratios (%)				
EBITDA Margin	8.4	7.8	7.9	8.1
PAT Margin	4.2	3.4	3.7	4.1
Inventory days	5.1	5.2	5.2	5.2
Debtor days	241.8	243.3	243.3	228.1
Creditor days	201.5	202.8	202.8	202.8
Return Ratios (%)				
RoE	12.3	8.1	10.3	13.4
RoCE	22.0	16.6	19.5	23.0
Valuation Ratios (x)				
P/E	11.4	15.4	10.8	7.5
EV / EBITDA	6.0	6.7	5.6	4.1
EV / Net Sales	0.5	0.5	0.4	0.3
Market Cap / Sales	0.4	0.4	0.4	0.3
Price to adjusted Book Value	1.3	1.2	1.1	0.9
Solvency Ratios				
Debt/EBITDA	1.6	2.1	1.7	1.3
Debt / Equity	0.4	0.4	0.4	0.4
Current Ratio	1.3	1.3	1.3	1.3
Debt servicing coverage ratio	3.6	2.7	3.3	4.1

Source: Company, ICICI Direct Research

ICICI Direct coverage universe (Capital Goods)

		CMP			M Cap	EPS (₹)			P/E (x)			RoCE (%)			RoE (%)	
		(₹)	TP(₹)	Rating	(₹ Cr)	FY18	FY19E	FY20E	FY18	FY19E	FY20E	FY18	FY19E	FY20E	FY18	FY19E
1	L&T (LARTOU)	1244	1,655	Buy	172586	38.8	52.1	57.3	33.9	25.2	22.9	10.6	12.2	12.9	11.0	13.3
2	Bhel (BHEL)	62	60	Hold	22762	3.3	2.5	3.9	18.2	24.3	15.6	5.6	4.8	6.5	2.5	2.8
3	AIA Engineering (AIAENG)	1655	1,890	Buy	15610	47.0	51.3	63.0	35.5	32.5	26.5	18.4	19.2	21.3	14.7	14.2
4	Thermax (THERMA)	1060	1,265	Buy	12631	20.0	24.0	37.3	53.0	44.1	28.4	15.3	16.6	21.0	9.9	11.1
5	KEC International (KECIN)	250	265	Hold	6428	17.9	19.0	23.0	13.6	12.8	10.6	24.9	25.0	25.7	23.1	20.1
6	Kalpataru Power(KALPOW)	349	430	Buy	5356	21.0	25.6	30.0	17.4	14.2	12.2	17.0	17.4	17.8	11.6	12.0
7	Greaves Cotton (GREAVE)	124	140	Buy	3028	8.3	7.5	8.8	16.9	18.6	15.9	18.0	12.6	13.4	21.1	18.0
8	Elgi Equipment (ELGEQU)	247	310	Buy	3914	6.1	6.3	9.1	38.8	38.0	26.3	14.3	13.9	17.9	14.1	13.3
9	ABB India (ABB)	1247	1,460	Buy	30939	19.8	23.5	27.8	64.6	54.5	46.1	23.2	24.9	24.5	11.6	12.5
10	Bharat Electronics (BHAELE)	77	110	Buy	26803	5.7	7.3	7.3	14.8	11.6	11.6	24.9	28.1	25.6	18.0	20.0
11	Engineers India (ENGIND)	114	110	Hold	7413	6.0	5.9	6.9	17.9	18.1	15.4	23.2	21.7	23.7	16.7	16.3
12	VaTech Wabag (VATWAB)	278	295	Hold	1493	16.9	16.7	24.1	7.0	5.3	6.3	20.7	24.8	22.0	10.1	9.4
13	Cochin Shipyard (COCSHI)	350	520	Buy	5,891	29.2	33.6	31.6	13.4	11.6	12.3	13.4	13.9	12.0	12.2	13.1
14	SKF (SKFIND)	1941	2,050	Hold	10810	57.6	66.4	75.0	33.5	29.1	25.7	23.7	24.5	24.2	16.1	16.3
15	Timken India (TIMIND)	553	660	Buy	4487	13.5	16.7	20.1	41.8	33.7	28.1	18.9	14.2	15.8	13.1	10.1
16	NRB Bearing (NRBBEA)	189	215	Buy	2084	9.4	10.4	12.0	19.9	17.8	15.5	26.7	24.8	24.3	24.0	22.8
17	Grindwell Norton (GRINOR)	511	625	Buy	5868	13.5	16.0	18.1	39.2	33.1	29.3	22.2	24.3	24.8	15.1	16.3

Source: Company, ICICI Direct Research

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