

## Sector: Infrastructure

## Result Update

	Change
Reco: <b>Buy</b>	↔
CMP: <b>Rs. 49</b>	
Price Target: <b>Rs. 75</b>	↓

↑ Upgrade ↔ No change ↓ Downgrade

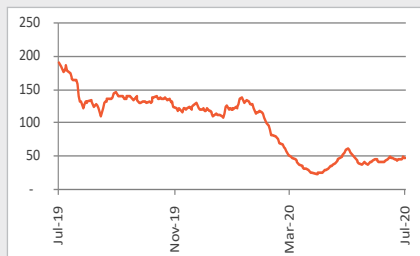
## Company details

Market cap:	Rs. 837 cr
52-week high/low:	Rs. 195/23
NSE volume: (No of shares)	2.4 lakh
BSE code:	532710
NSE code:	SADBHAV
Sharekhan code:	SADBHAV
Free float: (No of shares)	15.2 cr

## Shareholding (%)

Promoters	47
FII	11
DII	31
Others	12

## Price chart



## Price performance

(%)	1m	3m	6m	12m
Absolute	8.9	60.3	-61.0	-74.4
Relative to Sensex	-0.2	44.4	-48.5	-68.7

Sadbhav Engineering Limited (SEL) reported weak execution during Q4FY2020, led by issues related to Right of Way in some HAM projects and COVID-19 led lockdown during March 2020. Standalone revenue and operating profit dipped by 60% y-o-y, while it posted adjusted net loss (adjusting for Rs. 17 crore exceptional gain from transfer of assets to Indinfravit trust) of Rs. 8.8 crore for Q4FY2020. On the positive note, the company now has appointed dates for all its HAM projects and has applied for descope/delinking of projects where Right of Way is not available. Though H1FY2021 performance is likely to be affected by COVID-19 led lockdown, monsoons, and labour shortage, it expects to revert back to its quarterly run-rate of Rs. 800 crore to Rs. 900 crore from Q3FY2021. Further, considering normal conditions, it would be targeting Rs. 3,400 crore to Rs. 3,500 crore turnover during FY2022. SEL has also reduced its net standalone debt and net consolidated debt by Rs. 1,601 crore and Rs. 5,415 crore during Q4FY2020 with stake sale in eight operational assets to Indinfravit trust. Standalone net debt to equity reached almost at decadal low at 0.5x. SEL would be reducing its debt further with pending Rs. 340 crore (Rs. 267 crore from Ahmedabad Ring Road stake sale) from Indinfravit. SEL's order book stands at Rs. 8,372 crore (3.7x its FY2020 standalone revenue), while it expects to win Rs. 3,000 crore to Rs. 4,000 crore orders in the next three to four months. SEL expects merger of Sadbhav Infrastructure Projects Limited (SIPL) with SEL to be complete before March 2021. Overall, we expect the company to gradually return back to track with execution of projects at advanced stage and reduction in leverage. We have revised our FY2021 estimates downwards, factoring extended impact of COVID-19 on execution. We have also factored lower valuation of SIPL, which has led to reduction in our price target (PT) to Rs. 75. Considering attractive valuation and improving fundamentals, we have maintained our Buy rating on the stock.

## Key positives

- From Q3FY2021, SEL expects normal quarterly revenue run-rate with strong jump in FY2022.
- Received appointed dates for all HAM projects while applying for descope/delinking projects to expedite execution.

## Key negatives

- H1FY2021 to be affected by COVID-19 disruption, monsoons, and labour shortage.
- Increased receivables due to pending claims and unbilled revenue.

## Our Call

**Valuation –Maintain Buy with a revised PT of Rs. 75:** SEL has been affected by weak execution during 9MFY2020, which is expected to improve from Q3FY2021. However, it has been able to meaningfully deleverage its balance sheet and has been able to receive appointed dates for all its HAM projects. The company has started its focus on bidding and execution of projects, which should aid in healthy earnings growth in FY2022. Overall, we expect the company to gradually return back to track with the execution of projects at advanced stage and reduction in leverage. We have revised our FY2021 estimates downwards, factoring extended impact of COVID-19 on execution. We have also factored lower valuation of SIPL, which has led to reduction in our PT to Rs. 75. Considering attractive valuation and improving fundamentals, we have maintained our Buy rating on the stock.

## Key Risks

Further delay in execution of projects is a key risk to our call.

## Valuation (Standalone)

Particulars	FY19	FY20	FY21E	FY22E
Revenue	3,549.2	2,251.7	2,378.4	3,208.0
OPM (%)	12.1	12.4	10.9	11.9
Adjusted PAT	186.1	68.1	63.2	152.3
% YoY growth	(15.7)	(63.4)	(7.3)	141.1
Adjusted EPS (Rs.)	10.8	4.0	3.7	8.9
P/E (x)	4.5	12.3	13.3	5.5
P/B (x)	0.4	0.4	0.4	0.4
EV/EBITDA (x)	4.2	6.4	6.9	4.7
RoNW (%)	9.5	3.3	3.0	6.9
RoCE (%)	8.8	4.8	4.7	7.1

Source: Company; Sharekhan estimates

## Weak execution continues to impact net earnings

SEL's reported lower-than-expected execution during Q4FY2020 with standalone revenue declining by 60% y-o-y to Rs. 409 crore. The company's execution had been affected by non-availability of Right of Way in some HAM projects and COVID-19 led nationwide lockdown during the last 10 days of March 2020. However, the company surprised on the OPM front with stable operating margins y-o-y. Operating profit declined by 60% y-o-y to Rs. 50.4 crore, which was marginally lower than our estimate. Further, lower other income, higher interest, and higher depreciation expense led to loss before tax of almost Rs. 1 crore. The company booked Rs. 17 crore exceptional gain from the transfer of entire equity in eight projects transferred to Indinfravit trust leading to reported standalone profit of Rs. 8.2 crore. However, adjusting for the same, the company reported standalone net loss of Rs. 8.8 crore in Q4FY2020 versus Rs. 28 crore net profit in Q4FY2019.

## Revenue run-rate to get normalised from Q3FY2021

SEL expects Q1FY2021 to be washed out due to COVID-19 led lockdown and labour shortage. The company is currently doing Rs. 4.5 crore to Rs. 5 crore revenue per day with around 50-60% labour availability. Q2FY2021 is expected to be muted due to the monsoons, while labour availability is increasing. From September 2020, the company expects to achieve Rs. 10 crore revenue per day, factoring 80-90% labour availability. Hence, management expects that from Q3FY2021 the company should revert back to Rs. 800 crore to Rs. 900 crore quarterly revenue run-rate. The company has also received appointed dates for all its HAM projects and expects to complete six HAM projects during the current fiscal. The company expects to achieve Rs. 3,400 crore to Rs. 3,500 crore revenue in FY2022, considering the normal scenario.

## Key Conference Call Takeaways

- ♦ **Guidance:** The company is currently executing Rs. 4.5 crore to Rs. 5 crore per day revenue. It expects Q1FY2021 to be washed out due to COVID-19 led lockdown. Further, Q2FY2021 is expected to be affected by monsoon and labour shortage. It expects to achieve Rs. 800 crore to Rs. 900 crore quarterly run-rate from Q3FY2021. Further, it expects to achieve Rs. 3,400 crore to Rs. 3,500 crore revenue in FY2022.
- ♦ **Bidding pipeline:** As per the company, NHAI has invited bids for 24 EPC projects and 27 HAM projects worth Rs. 17,663 crore and Rs. 27,974 crore, respectively, to be submitted by August 2020 end. The company has submitted bids for 4 EPC projects worth Rs. 3,367 crore on July 7, 2020. The company is also interested in 3 metro projects for which bids are submitted by August 2020 end. It has also submitted bid for one project worth Rs. 470 crore on July 1, 2020.
- ♦ **Loss funding for Rohtak Panipat and Rohtak Hisar projects:** The company infused Rs. 75 crore to Rs. 77 crore as shortfall in the two Rohtak projects during FY2020. It expects loss funding of Rs. 50 crore to Rs. 60 crore in FY2021 and Rs. 90 crore to Rs. 100 crore in FY2022. The company has started arbitration process for Rohtak Panipat with NHAI. It has launched claim of Rs. 1,100 crore for which arbitration process is expected to get started in a month's time.
- ♦ **Ahmedabad Ring Road Project:** The company expects approval from AUDA by the end of this month. The approval from one of the lender is left. Equity value of the project is Rs. 267 crore as against equity invested of Rs. 104 crore. The said project is the ninth project stake sale to Indinfravit trust.
- ♦ **Order book:** The company has an order book of Rs. 8,372 crore. It has received appointed dates for all projects.
- ♦ **Equity investment:** Out of the total Rs. 1,013 crore equity requirement for nine HAM projects, Rs. 705 crore has been invested till date. Balance Rs. 308 crore equity is required to be infused. The company will be investing Rs. 195 crore to Rs. 200 crore equity in FY2021.

**Results (Standalone)**

	Rs cr				
Particulars	Q4FY2020	Q4FY2019	y-o-y%	Q3FY2020	q-o-q%
Net sales	408.9	1021.7	-60.0%	440.0	-71%
Total expenses	358.4	894.9	-59.9%	385.2	-6.9%
Operating profit	50.4	126.8	-60.2%	54.8	-8.0%
other income	4.1	5.5	-24.8%	7.6	-46.2%
Depreciation	26.0	23.1	12.2%	26.8	-3.0%
Interest	29.4	28.2	4.4%	23.1	27.5%
Exceptional items	17.0	0.8		0.0	
Profit Before Tax	16.2	81.6	-80.2%	12.6	28.0%
Taxes	8.0	52.7	-84.9%	1.0	726.0%
PAT	8.2	28.9	-71.7%	11.7	-29.8%
Adjusted PAT	-8.8	28.1	-	11.7	-
No of equity shares	17.2	17.2	0.0%	17.2	0.0%
EPS (Rs.)	-0.5	1.6	-	0.7	-
OPM (%)	12.3%	12.4%	-7 bps	12.5%	-13 bps
NPM (%)	-2.2%	2.8%	-	2.6%	-
Tax rate (%)	49.4%	64.6%	-1524 bps	7.7%	4171 bps

Source: Company; Sharekhan Research

## Outlook

**Expect strong bounce back in FY2022:** SEL expects Q1FY2021 to be washed out due to COVID-19 led lockdown and labour shortage. It is currently doing Rs. 4.5 crore to Rs. 5 crore revenue per day with around 50-60% labour availability. Q2FY2021 is expected to be muted owing to the monsoons, while labour availability is increasing. From September 2020, it expects to achieve Rs. 10 crore revenue per day, factoring 80-90% labour availability. Hence, it expects from Q3FY2021, the company should revert back to Rs. 800 crore to Rs. 900 crore quarterly revenue run-rate. The company has also received appointed dates for all its HAM projects and expects to complete six HAM projects during the current fiscal. The company expects to achieve Rs. 3,400 crore to Rs. 3,500 crore revenue in FY2022, considering the normal scenario.

## Valuation

**Maintain Buy with a revised PT of Rs. 75:** SEL has been affected by weak execution during 9MFY2020, which is expected to improve from Q3FY2021. However, it has been able to meaningfully deleverage its balance sheet and able to receive appointed dates for all its HAM projects. The company has started its focus on bidding and execution of projects, which should aid in healthy earnings growth in FY2022. Overall, we expect the company to gradually return back to track with the execution of projects at advance stage and reduction in leverage. We have revised our FY2021 estimates downwards, factoring extended impact of COVID-19 on execution. We have also factored lower valuation of SIPL, which has led to reduction in our PT to Rs. 75. Considering attractive valuation and improving fundamentals, we have maintained our Buy rating on the stock.

## Peer Comparison

Particulars	P/E (x)		EV/EBITDA (x)		P/BV (x)		RoE (%)	
	FY21E	FY22E	FY21E	FY22E	FY21E	FY22E	FY21E	FY22E
PNC Infratech	11.8	9.2	5.8	4.7	1.3	1.1	12.0	13.5
KNR Constructions	17.0	13.8	6.3	5.5	1.6	1.5	10.2	11.4
Sadbhav Engineering	13.3	5.5	6.9	4.7	0.4	0.4	3.0	6.9
Ashoka Buildcon*	12.6	15.8	3.6	2.4	4.9	3.9	-	34.8

Source: Sharekhan Research, Consolidated financials

## About company

SEL, incorporated in 1988, is engaged in 1) EPC business for transport, mining and irrigation sectors; and 2) development of roads and highways on a BOT basis through SIPL. SEL has a healthy order book of Rs. 8,726 crore (3.0x its TTM standalone revenue). The company has robust in-house integrated execution capabilities with qualified human resources and owned equipment. The company has been making profits since its inception in its standalone business and has paid regular dividends for the past 16 years.

## Investment theme

We expect SEL to benefit from improved order execution, enhanced order inflows (particularly from the transport segment), and resolution of working capital issues, resulting in a sturdier balance sheet. The company's recent stake sale is likely to significantly deleverage its balance sheet. The reverse merger of SIPL with SEL can lead to an asset-light business model with focus on core EPC and O&M execution. Further, expected improvement in outlook for the Indian roads sector and limited competitive intensity augur well for SEL as it is present in both the asset creation and EPC verticals.

## Key Risks

- ♦ Delay in receipt of appointed dates for HAM projects can lead to lower earnings.
- ♦ Inability to fructify asset sale deal with IndInfravit can limit its ability to bid for future projects.
- ♦ Weak macro-economic environment leading to lower traffic at toll projects affects valuation.

## Additional Data

### Key management personnel

Mr. Vishnubhai M Patel	Chairman Emeritus
Mr. Shashin V. Patel	Chairman and Managing Director
Mr. Nitin R Patel	CFO & Whole time Director
Mr. Tushar D Shah	Company Secretary & Compliance Officer

Source: Company Website

### Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	PATEL SHANTABEN VISHNUBHAI	28.07
2	PATEL SHANTABEN V	28.07
3	SADBHAV FINSTOCK PVT LTD	9.64
4	HDFC Asset Management Co Ltd	9.27
5	ICICI Prudential Life Insurance Co	6.97
6	SBI Funds Management Pvt Ltd	4.13
7	PATEL SHASHIN	3.64
8	Reliance Capital Trustee Co Ltd	3.5
9	Patel Vikramkumar R	2.7
10	Aditya Birla Sun Life Asset Manage	2.67

Source: Bloomberg

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# Sharekhan

by BNP PARIBAS

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