



3R MATRIX

	+	=	-
Right Sector (RS)	✓	✗	✗
Right Quality (RQ)	✓	✗	✗
Right Valuation (RV)	✓	✗	✗

+ Positive = Neutral - Negative

What has changed in 3R MATRIX

	Old		New
RS	✗	↔	✓
RQ	✗	↔	✓
RV	✗	↔	✓

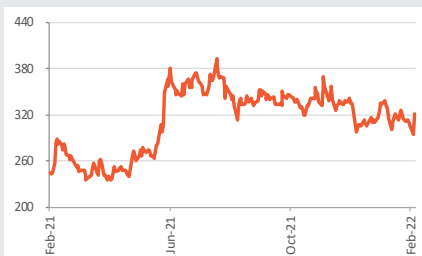
Company details

Market cap:	Rs. 2,002 cr
52-week high/low:	Rs. 404 / 229
NSE volume: (No of shares)	7.7 lakh
BSE code:	533269
NSE code:	WABAG
Free float: (No of shares)	4.9 cr

Shareholding (%)

Promoters	21.7
FII	18.0
DII	3.6
Others	56.64

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-4.8	-12.9	-5.5	31.6
Relative to Sensex	0.6	-9.5	-9.4	19.4

Sharekhan Research, Bloomberg

Va Tech Wabag Ltd

Strong performance; order prospects bright

Capital Goods

Sharekhan code: WABAG

Reco/View: Buy



CMP: Rs. 322

Price Target: Rs. 435



Upgrade



Maintain



Downgrade

Summary

- Q2FY2022 revenue was below estimate, while OPM surprised positively, leading to strong beat on net earnings. Net Debt reduces 37% q-o-q.
- Order inflows trebled y-o-y for 9MFY2022. Order book at Rs. 10,067 crore is 3.3x its TTM revenue, providing healthy revenue visibility.
- Domestic and overseas order pipeline remained buoyant. The company would focus on technological projects which would provide better margins and higher cashflows.
- We maintain a Buy on Va Tech Wabag with unchanged PT of Rs. 435, considering strong order book and healthy balance sheet.

Va Tech Wabag reported lower-than-expected consolidated revenue at Rs. 745.5 crore, down 6.3% y-o-y, owing to dip in overseas revenues (down 17.9% y-o-y at Rs. 230 crore) while revenues from India remained almost flat y-o-y at Rs. 510 crore. Consolidated operating profit margin (OPM) at 10.2% (+141 bps y-o-y) was higher than our estimate of 8.5% which was led by better project mix. Consolidated net profit growth grew by 5.7% at Rs. 44.2 crore which was much higher than our estimate. The order inflows for 9MFY2022 remained strong rising by 3x y-o-y at Rs. 2,832 crore aided by strong order booking in India (up 4.8x y-o-y). Consequently, order book remained strong at Rs. 10,067 crore, 3.3x TTM consolidated revenues. The company expects order momentum to continue over the next fiscal with its focus on winning international orders and works related to engineering & component supply. The same would lead to an improvement in margins in FY2023. In domestic markets, it is optimistic on strong order intake from schemes such as AMRUT, smart cities mission, Jal Jeevan Mission, etc.

Key positives

- OPM rose 141bps y-o-y and 195bps q-o-q led by better project mix.
- Order intake from India was up 4.8x y-o-y for 9MFY2022 at Rs. 2174 crore.
- Net debt reduced 37% q-o-q to Rs. 145 crore.

Key negatives

- Overseas revenues declined by 18% y-o-y at Rs. 230 crore.
- Overseas order inflow declined by 43% y-o-y at Rs. 166 crore.

Management Commentary

- The company would be focusing on technological projects which has higher margins and cash flows.
- The total receivables from two generation companies is Rs. 330 crore (majorly retention money) and Rs. 69 crore related to Techpro which is under NCLT. By end of H1FY2023, it will come down substantially.
- The company won \$100mn order in Dubai related to engineering and procurement to 545 million litres per day reverse osmosis plant. The desalination plant is expected to commission by March 2024.

Revision in estimates – We have retained our earnings estimates.

Our Call

Valuation – Maintain Buy with an unchanged PT of Rs. 435: Va Tech Wabag is on a strong earnings growth trajectory going ahead with concerns of high leverage, led by increasing working capital now behind it. A well-funded strong order book provides comfort on execution and collections going ahead. Further, the government's focus is expected to remain on water-related investments, providing healthy order intake tailwinds for the company going ahead. At the CMP, the stock trades at P/E of 9x its FY2024E earnings, which we believe is attractive considering its strong net earnings growth outlook and strengthened balance sheet. Hence, we maintain a Buy with an unchanged PT of Rs. 435.

Key Risks

- Decline in domestic capex and impact on gross margin due to rise in commodity costs.
- Problems in execution could impact earnings growth.

Valuation (Consolidated)

Particulars	FY21	FY22E	FY23E	FY24E
Revenue from Operations	2,834	3,235	3,677	4,132
Operating Profit Margin (%)	7.7	8.4	8.7	9.0
RPAT	100	135	177	214
AEPS (Rs.)	16.1	21.8	28.4	34.4
P/E (x)	20.0	14.8	11.3	9.4
Price/ Book (x)	1.4	1.3	1.2	1.0
EV/EBITDA (x)	9.0	7.5	6.5	5.6
RoCE (%)	10.9	13.0	14.3	15.1
RoE (%)	7.8	9.2	10.8	11.7

Source: Company; Sharekhan estimates

Better-than-expected OPM leads to strong beat on net earnings

Va Tech Wabag reported 6.3% y-o-y decline in consolidated net revenues at Rs. 745.5 crore for Q3FY2022 which was lower than our estimate. The overseas revenues were down 17.9% y-o-y at Rs. 230 crore, while revenues from India remained almost flat y-o-y at Rs. 510 crore. Consolidated OPM at 10.2% (+141bps y-o-y, up 195 bps q-o-q) was much higher than our estimate of 8.5%. Higher OPM was driven by improvement in execution and project mix. Hence, operating profit grew by 8.6% y-o-y to Rs. 76.2 crore (higher than our estimate). Healthy operational performance led to a 5.7% y-o-y rise (+68% q-o-q) in consolidated net profit at Rs. 44 crore which was higher than our estimate.

Strong order inflows to sustain growth

The company remains bullish on order inflows for FY2023. Total order inflows during 9MFY2022 rose 3x y-o-y at Rs. 2832 crore, led by 4.8x y-o-y rise in India order book and 1.3x in overseas. Order backlog at Q3FY2022 end stands at Rs. 10,067 crore, 3.3x its TTM revenue, providing healthy revenue visibility. The company is seeing good traction in the Middle East, Africa, and India. Water security is the most important factor in ESG and sustainability ratings are expected to lead to healthy order inflows both domestically and internationally. Industrial water treatment has been growing at not less than 15% per annum, which is expected to gain traction going ahead. We expect strong execution to continue going ahead along with healthy order inflows.

Q3FY2022 Concall Highlights

- ♦ **9M performance:** Consolidated revenues grew 14% y-o-y at Rs. 2087 crore for 9MFY2022. On standalone basis, revenues grew by 30% y-o-y at Rs. 1,490 crore. Consolidated EBITDA stood at Rs. 175 crore, up 23% y-o-y and standalone EBITDA stood at Rs. 129 crores, up 21% y-o-y. Consolidated PAT stood at Rs. 86 crore, up 35% y-o-y while standalone PAT stood at Rs. 60 crores, up 50% y-o-y. Core EBITDA stood at 10% Vs 9.5% in Q3FY2021. Core RoCE has grown to 24.1% vs 20.5% in Q3FY2021. The working capital position remained under control. The net debt improved by 35% q-o-q at Rs. 145 crores.
- ♦ **Recent order wins:** The company won \$100-mn order in Dubai related to engineering and procurement to 545mn litres per day Reverse Osmosis plant. The desalination plant is expected to commission by March 2024.
- ♦ **Order status:** The Saudi Arabia 120 MLD sewage plant for Jubail city is at final stages for completion. It is expected to commission by H1FY2023. The 300MLD new Jeddah airport in Saudi Arabia is in progress with a delivery of equipment. The Amour Gas project in Russia, detailed engineering is underway.
- ♦ **Outlook:** The ordering momentum is expected continue over the next fiscal. The company continues to focus on expanding its global reach in water treatment plants. The company's focus on engineering and supply of components especially in international arena has helped margins despite commodity inflation. Margins are sustainable and can improve in FY2023. Spends on cleaning rivers would be significantly higher than done over the last decade. The company would be focusing on technological projects which has higher margins and cash flows.
- ♦ **Receivables:** The total receivables from two generation companies is Rs. 330 crore (majorly retention money) and Rs. 69 crore related to Techpro which is under NCLT. By end of H1FY2023, it will come down substantially.

Results (Consolidated)

	Rs cr				
Particulars	Q3FY2022	Q3FY2021	Y-o-Y %	Q2FY2022	Q-o-Q %
Revenues	745.5	796.0	-6.3%	684.0	9.0%
EBITDA	76.2	70.2	8.6%	56.6	34.7%
Depreciation	2.3	3.0	-22.8%	2.6	-10.4%
Interest	22.3	22.9	-2.6%	22.2	0.5%
Other Income	5.5	3.6	51.2%	3.0	81.4%
PBT	57.1	47.9	19.1%	34.8	63.9%
Total Tax	10.9	12.0	-9.4%	9.3	17.8%
PAT before minority interest	46.2	35.9	28.7%	25.6	80.6%
Associate Income/Minority Interest	-2.0	5.9	-	0.7	-
Adjusted PAT	44.2	41.8	5.7%	26.2	68.4%
EPS (Rs.)	7.1	6.7	5.7%	4.2	68.4%
Margins			BPS		BPS
EBITDA Margin	10.2%	8.8%	141	8.3%	195
PAT Margin	5.9%	5.2%	68	3.8%	209
Tax Rate	19.1%	25.1%	-602	26.6%	-747

Source: Company; Sharekhan Research

Outlook and Valuation

■ Sector view – Investments by Governments and Private Sectors will play a vital role in water

Waste-water technology is primarily used by municipal authorities to treat waste-water in various Indian cities. Rising urban population in major Indian cities has created demand for waste-water treatment facilities to balance the population with the availability of fresh water. In the coming years, desalination is expected to be a prominent technology in Indian cities for water filtration due to the rising scarcity of fresh water. The global water treatment industry has undergone a sea change over the past decade. This is owing to rising awareness about water scarcity, innovations in water treatment technologies, and investments by governments and private sectors in this segment. The global water and wastewater treatment market is estimated to reach size of \$211 billion by 2025 at a CAGR of 6.5% over 2019-2025. India water and wastewater treatment (WWT) technology market is partially consolidated, with major players accounting for a moderate share of the market. Key players in the market include Veolia, Suez, Thermax Limited, VA Tech Wabag Limited, and DuPont. Increasing demand for water-treatment facilities across the world will have a positive impact on the market's growth in the coming years.

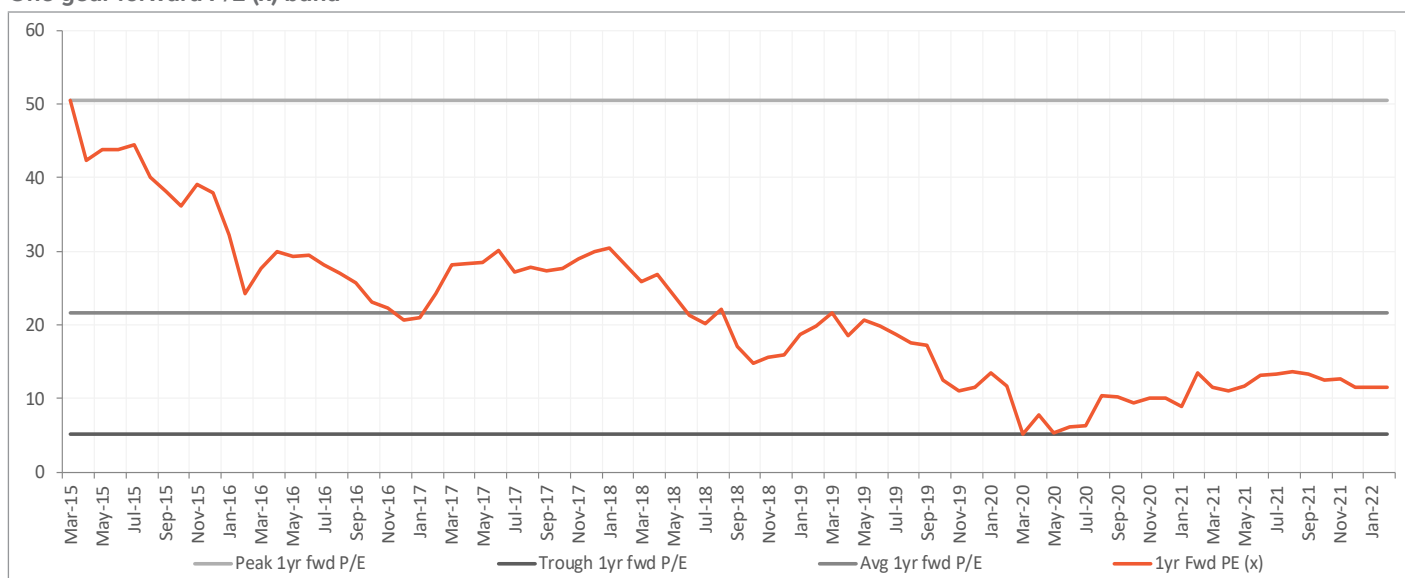
■ Company outlook – Creating Enduring Value

The company has a strong order book of Rs. 10,067 crore (3.3x TTM consolidated revenue, largely executable with financial closure of HAM projects) funded by the Centre, multilateral agencies, or sovereign entities, which provide comfort on cash collections and execution. The company generated Rs. 380 crore of net operating cash flows over FY2020-FY2021 and managed to curtail the rising working capital requirement, which strengthened the balance sheet. Further, the company generated free cash flows of Rs. 300 crore during FY2020-FY2021, which is also aided by its asset-light model. We expect the company to generate over Rs. 300 crore of free cash flows over FY2022-FY2023, led by strong operating cash flow generation, tighter control on working capital and lower capex requirements. The company is well placed to receive continuous flow of orders having a strong project execution track record and marquee clients, led by its asset-light business model and strengthened balance sheet profile.

■ Valuation – Maintain Buy with unchanged PT of Rs. 435

Va Tech Wabag is on a strong earnings growth trajectory going ahead with concerns of high leverage, led by increasing working capital now behind it. A well-funded strong order book provides comfort on execution and collections going ahead. Further, the government's focus is expected to remain on water-related investments, providing healthy order intake tailwinds for the company going ahead. At the CMP, the stock trades at P/E of 9x its FY2024E earnings, which we believe is attractive considering its strong net earnings growth outlook and strengthened balance sheet. Hence, we maintain a Buy with an unchanged PT of Rs. 435.

One-year forward P/E (x) band



Source: Sharekhan Research

About company

Va Tech Wabag is known for its innovative and successful solutions in the water engineering sector around the globe. The company is a systems specialist and full-service provider focusing on the planning, installation, and operations of drinking and wastewater plants for local government and industry in growth markets of Asia, North Africa, Middle East, and Central and Eastern Europe. The company represents a leading multinational player with a workforce of over 1,600 and has companies and offices in more than 20 countries.

Investment theme

Va Tech Wabag has unique technological knowhow, based on innovative, patented technologies and long-term experience. For over 95 years, the company has been facilitating access to clean and safe water to over 500 million people. With decades of rich experience, over 6,000 projects across multiple sectors and state-of-the-art plants in over 20 countries, Wabag is a globally respected organisation. The company is on a strong earnings growth trajectory going ahead, with concerns of high leverage led by increasing working capital now behind it. The company's well-funded strong order book provides comfort on execution and collections going ahead. Further, the government's focus is expected to remain on water-related investments, providing healthy order intake tailwinds for the company going ahead.

Key Risks

- ♦ Slowdown in economic activity might impact order intake visibility and delay in execution of existing order book might impact revenue booking.
- ♦ Hike in interest rate might impact profitability as the company has a stretched working capital situation.

Additional Data

Key management personnel

Malay Mukherjee	Chairman (Non-Executive Independent Director)
Rajiv Mittal	Managing Director & Group CEO
Pankaj Sachdeva	Chief Executive Officer
Sandeep Kumar Agrawal	Chief Financial Officer
R Swaminathan	Company Secretary & Compliance Officer

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Mittal Rajiv Devaraj	15.61
2	Jhunjhunwala Rekha Rakesh	8.04
3	Varadarajan Subramanian	3.51
4	Government Pension Fund – Global	3.22
5	Norges Bank	3.21
6	KBI Global Investors	2.75
7	Saraf Shivnarayan J	2.57
8	SBI Funds Management Pvt Ltd	2.54
9	Massachusetts Institute of Technology	2.52
10	Basera Home Finance	2.41

Source: Bloomberg

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Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and deteriorating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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