

**Debt reduction factored in**

HCC's standalone revenue declined 5.3% YoY to ₹9.3bn in Q1FY18 (18.8% below estimates) due to slower execution in J&K. Excluding claims of ₹800 mn (₹770 mn in Q1FY17), core revenue declined 6.1% YoY to ₹8.5 bn. EBITDA margin expanded 70 bps YoY to 18.3% (239 bps above estimates) due to higher EBITDA margin of 40% vs. 26% on claims recovery. Excluding claims, core EBITDA margin declined 63bps YoY to 16.2%. PAT grew 33.5% YoY to ₹145mn (47.8% above estimates). We maintain 'Accumulate' as sharp surge in stock price in last one year have factored in drastic debt reduction due to arbitration cash flow and ₹8.3 bn debt to equity conversion due to S4A.

**Outlook and Valuation**

HCC could reduce its debt by ₹2.5-3.0 bn post FY17 despite arbitration cash flow of ₹6.9 bn due to encashment of ₹1.8 bn bank guarantee by IRCON and adjustment of ₹1.2 bn by NHPC. It expects further ₹1.5 bn adjustment against arbitration cash flow in remaining FY18. Accordingly, now we considered ₹15 bn (earlier ₹20 bn) / ₹15 bn debt reduction in FY18E/ FY19E due to receipt of arbitration claim money. We have considered 40% (earlier 50%) success for ₹43 bn (as on FY17) claims which are under arbitration and outcome is likely to come by FY19E as per new Arbitration Act. Our FY18E/ FY19E revenue ₹48.5 bn/ ₹63.3 bn (up 15.5%/ 30.5% YoY) includes ₹6.4 bn (earlier ₹10.7 bn) / ₹10.7 bn claims awards and 15%/ 25% YoY growth on core revenue. We have considered 35% EBITDA margin on claims award and 13% on core EBITDA margin in FY18E/ FY19E.

Interest cost will see significant decline in FY18E/ FY19E to ₹5.5 bn/ ₹3.2 bn vs. ₹7.7 bn due to ₹30 bn debt reduction during FY18-19E. Therefore, Adj. PAT is expected to jump 3.4/ 8.0-fold in FY18E/ FY19E to ₹2.4 bn/ ₹5.7 bn vs. ₹713 mn. We valued construction business based on FY19E core EV/ EBITDA as it does not contain any claims and which is sustainable. However, due to limited upside potential, we maintain 'Accumulate' with an SOTP-based target price of ₹43.4 (Exhibit 1).

**Q1FY18 Result (₹ Mn)**

Particulars	Q1FY18	Q1FY17	YoY (%)	Q4FY17	QoQ (%)
<b>Total revenue</b>	<b>9,307</b>	<b>9,825</b>	<b>(5.3)</b>	<b>13,583</b>	<b>(31.5)</b>
Operating expenditure	7,607	8,099	(6.1)	11,342	(32.9)
<b>EBITDA</b>	<b>1,700</b>	<b>1,726</b>	<b>(1.5)</b>	<b>2,241</b>	<b>(24.1)</b>
Depreciation	288	328	(12.0)	283	1.8
<b>Operating profit</b>	<b>1,412</b>	<b>1,398</b>	<b>1.0</b>	<b>1,958</b>	<b>(27.9)</b>
Other income	605	594	1.8	706	(14.4)
<b>EBIT</b>	<b>2,016</b>	<b>1,992</b>	<b>1.2</b>	<b>2,664</b>	<b>(24.3)</b>
Interest	1,821	1,797	1.4	2,080	(12.4)
Exceptional items	-	-	-	(212)	-
<b>EBT</b>	<b>195</b>	<b>195</b>	<b>(0.3)</b>	<b>372</b>	<b>(47.6)</b>
Income Tax	50	87	(42.7)	163	(69.4)
<b>Net income</b>	<b>145</b>	<b>109</b>	<b>33.5</b>	<b>209</b>	<b>(30.6)</b>
Adjustments	-	-	-	119	-
<b>Adj. Net income</b>	<b>145</b>	<b>109</b>	<b>33.5</b>	<b>328</b>	<b>(55.8)</b>
			bps		bps
EBITDA Margin (ex. O.I.)	18.3	17.6	70	16.5	177
EBITDA Margin (in. O.I.)	24.8	23.6	115	21.7	307
NPM (%)	1.5	1.0	42	2.3	(83)
Tax/PBT (%)	25.5	44.3	(1,885)	43.7	(1,824)
Const. Cost/Rev. (%)	67.1	69.4	(233)	73.2	(617)

CMP	₹ 40
Target / Upside	₹ 43/9%
BSE Sensex	32,238
NSE Nifty	10,014

**Script Details**

Equity / FV	₹ 1,015mn/₹ 1/-
Market Cap	₹ 40bn
	USD 632mn
52-week High/Low	₹ 48/21
Avg. Volume (no)	5,542,025
NSE Symbol	HCC
Bloomberg Code	HCC IN

**Shareholding Pattern Jun'17(%)**

Promoter	27.8
MF/Banks/FIs	9.3
FIIIs	12.2
Public/Others	50.7

**Valuation (x)**

	FY17	FY18E	FY19E
P/E	56.4	16.8	7.0
EV/EBITDA	11.4	9.8	5.7
ROE (%)	3.2	8.5	17.7
ROCE (%)	12.8	14.0	21.9

**Estimates (₹ mn)**

	FY17	FY18E	FY19E
Net Sales	41,959	48,468	63,272
EBITDA	7,536	7,718	10,589
PAT	713	2,398	5,730
EPS	0.7	2.4	5.6

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### Robust order book enhances revenue visibility

HCC bagged fresh orders worth ₹10.1 bn (up 536.5% YoY) in Q1FY18. HCC's order book stands at ₹203.6bn (5.6x FY17 core revenue). Moreover, it is L1 for orders worth ₹28 bn. Thus, we believe HCC's current order book (₹203.6bn) and fresh inflows of ₹53.8bn/ ₹53.8bn in FY18E and FY19E, will not only enhance its revenue visibility but also drive revenue growth.

### Update on Lavasa

The Joint Lenders' Forum achieved the required majority on 13 July, 2017 for financial restructuring on Lavasa. If post successful restructuring, HCC can derive some equity value for Lavasa then it would act as positive for HCC stock price. Currently, we have not assigned any value for Lavasa.

### Exhibit 1: SOTP Valuation

Component	Valuation Method	₹/sh	%
Standalone cons business	7x FY19E core EV/EBITDA	36.4	83.8
Road BOTs	0.7xBV	3.5	8.1
Steiner AG	1xBV	3.5	8.1
<b>Total</b>		<b>43.4</b>	<b>100.0</b>
CMP		39.7	
Potential upside		9.5%	

Source: Company, DART

## Downside risk to our valuation

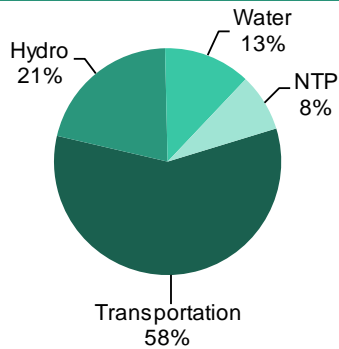
**Delay in arbitration cash receipt:** If there is more delay in getting money for arbitration awards vs. our estimates and lower than 40% success for claims under arbitration, then HCC's stretched working capital could have a negative impact on the company's revenue and profitability.

**Execution Delays:** Project delays due to hindrance at the client's end or other regulatory bottlenecks could adversely affect HCC's revenue and profitability.

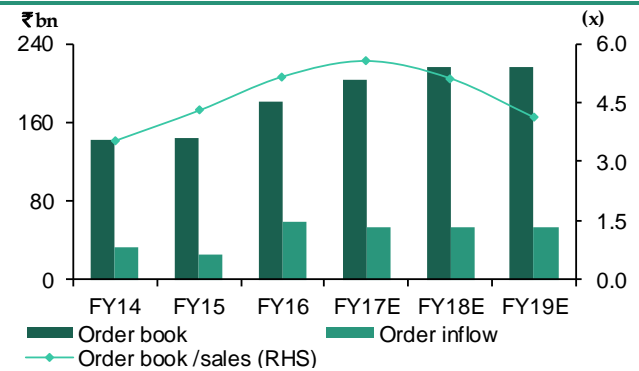
**Exhibit 2: Q1FY18 Performance (Standalone)**

Y/E Mar (₹ mn)	Q1FY18	Q1FY17	YoY (%)	Q4FY17	QoQ (%)	FY17	FY16	YoY (%)
<b>Revenue</b>	<b>9,307</b>	<b>9,825</b>	<b>(5.3)</b>	<b>13,583</b>	<b>(31.5)</b>	<b>41,959</b>	<b>41,909</b>	<b>0.1</b>
Consumption of materials	3,023	2,194	37.8	2,794	8.2	8,690	10,012	(13.2)
Staff cost	1,038	947	9.6	1,113	(6.7)	3,968	3,832	3.5
Construction expenses	3,218	4,623	(30.4)	7,153	(55.0)	20,577	18,643	10.4
Other expenses	327	335	(2.2)	283	15.8	1,188	1,338	(11.2)
Total expenditure	7,607	8,099	(6.1)	11,342	(32.9)	34,423	33,825	1.8
<b>EBITDA</b>	<b>1,700</b>	<b>1,726</b>	<b>(1.5)</b>	<b>2,241</b>	<b>(24.1)</b>	<b>7,536</b>	<b>8,084</b>	<b>(6.8)</b>
Depreciation	288	328	(12.0)	283	1.8	1,253	1,525	(17.8)
<b>Operating profit</b>	<b>1,412</b>	<b>1,398</b>	<b>1.0</b>	<b>1,958</b>	<b>(27.9)</b>	<b>6,283</b>	<b>6,559</b>	<b>(4.2)</b>
Other income	605	594	1.8	706	(14.4)	2,622	2,142	22.4
<b>EBIT</b>	<b>2,016</b>	<b>1,992</b>	<b>1.2</b>	<b>2,664</b>	<b>(24.3)</b>	<b>8,905</b>	<b>8,702</b>	<b>2.3</b>
Interest	1,821	1,797	1.4	2,080	(12.4)	7,724	7,017	10.1
Exceptional items	0	0	-	(212)	-	(212)	(280)	-
<b>EBT</b>	<b>195</b>	<b>195</b>	<b>(0.3)</b>	<b>372</b>	<b>(47.6)</b>	<b>970</b>	<b>1,404</b>	<b>(31.0)</b>
Provision for current tax	50	87	(42.7)	163	(69.4)	209	277	(24.7)
<b>Net income</b>	<b>145</b>	<b>109</b>	<b>33.5</b>	<b>209</b>	<b>(30.6)</b>	<b>594</b>	<b>948</b>	<b>(37.3)</b>
Adjustments	-	-	-	119	-	119	130	(8.2)
<b>Adjusted net income</b>	<b>145</b>	<b>109</b>	<b>33.5</b>	<b>328</b>	<b>(55.8)</b>	<b>713</b>	<b>1,078</b>	<b>(33.8)</b>
<b>EPS (₹)</b>	<b>0.1</b>	<b>0.1</b>	<b>33.5</b>	<b>0.3</b>	<b>(55.8)</b>	<b>0.7</b>	<b>1.1</b>	<b>(33.8)</b>
			bps		bps			bps
EBIDTA Margin (excl. O.I.)	18.3	17.6	70	16.5	177	18.0	19.3	(133)
EBIDTA Margin (incl. O.I.)	24.8	23.6	115	21.7	307	24.2	24.4	(19)
NPM (%)	1.5	1.0	42	2.3	(83)	1.6	2.4	(85)
Tax/PBT (%)	25.5	44.3	(1,885)	43.7	(1,824)	38.7	8.3	3,041
Construction cost/sales (%)	67.1	69.4	(233)	73.2	(617)	69.8	68.4	138

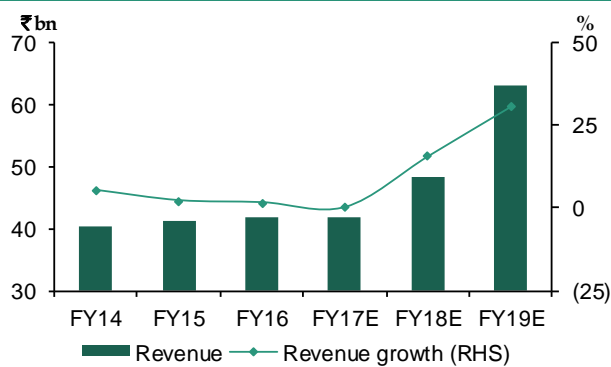
Source: Company, DART

**Exhibit 3: Order book (₹204bn) break-up**


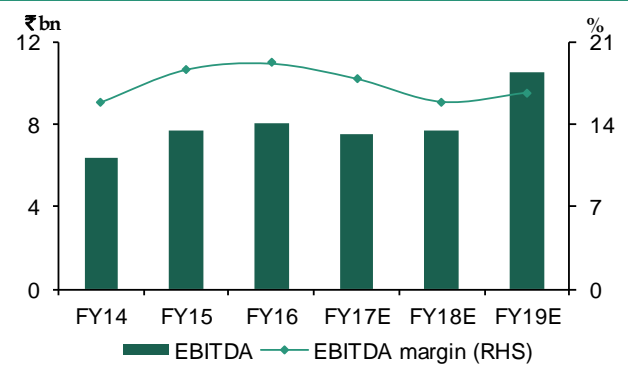
Source: Company, DART

**Exhibit 4: Order book trend**


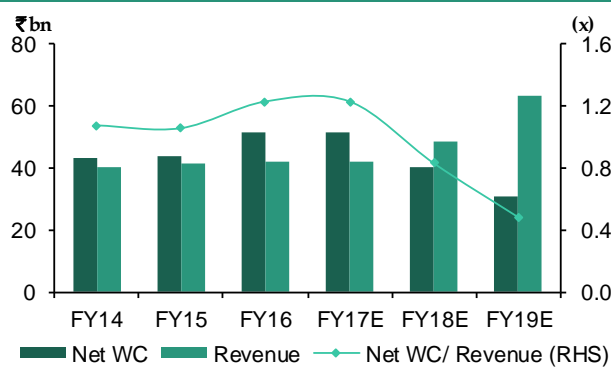
Source: Company, DART

**Exhibit 5: Revenue CAGR of 22.8% over FY17-19E**


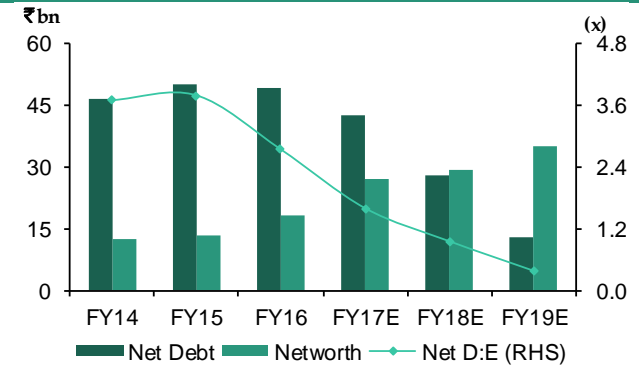
Source: Company, DART

**Exhibit 6: EBITDA Margin trend**


Source: Company, DART

**Exhibit 7: Ease in working capital**


Source: Company, DART

**Exhibit 8: Deleveraging balance sheet**


Source: Company, DART

### Income Statement (Standalone)

Particulars (₹ mn)	Mar16	Mar17	Mar18E	Mar19E
<b>Revenue</b>	<b>41,909</b>	<b>41,959</b>	<b>48,468</b>	<b>63,272</b>
Growth (%)	1.6	0.1	15.5	30.5
Total Expenditure	33,825	34,423	40,750	52,683
Consumption of materials	10,012	8,690	11,545	14,854
Construction Exp	18,643	20,577	23,580	31,509
Staff Cost	3,832	3,968	4,365	4,801
Other Expenses	1,338	1,188	1,260	1,519
Other Income	2,142	2,622	2,648	2,675
<b>EBIDTA (Excl. OI)</b>	<b>8,084</b>	<b>7,536</b>	<b>7,718</b>	<b>10,589</b>
Growth (%)	4.5	(6.8)	2.4	37.2
<b>EBIDTA (Incl. OI)</b>	<b>10,226</b>	<b>10,158</b>	<b>10,366</b>	<b>13,264</b>
Depreciation	1,525	1,253	1,264	1,363
<b>EBIT</b>	<b>8,702</b>	<b>8,905</b>	<b>9,103</b>	<b>11,901</b>
Interest	7,017	7,724	5,470	3,220
Exceptional items	(280)	(212)	0	0
Profit Before Tax	1,404	970	3,633	8,681
Tax	457	376	1,235	2,951
Net Profit	948	594	2,398	5,730
Adjustments	130	119	0	0
<b>Adj. Net Profit</b>	<b>1,078</b>	<b>713</b>	<b>2,398</b>	<b>5,730</b>
Growth (%)	32.0	(33.8)	236.0	139.0

### Balance Sheet (Standalone)

Particulars (₹ mn)	Mar16	Mar17	Mar18E	Mar19E
<b>Sources of Funds</b>				
Equity Capital	779	1,011	1,015	1,015
Reserves	17,254	25,889	28,480	34,209
<b>Net Worth</b>	<b>18,033</b>	<b>26,900</b>	<b>29,495</b>	<b>35,224</b>
Long Term Loans	29,853	32,481	20,820	10,820
Short Term Loans	20,496	11,486	8,147	3,147
<b>Loan Funds</b>	<b>50,350</b>	<b>43,967</b>	<b>28,967</b>	<b>13,967</b>
Deferred Tax Liability	65	232	304	478
<b>Total Capital Employed</b>	<b>68,448</b>	<b>71,099</b>	<b>58,767</b>	<b>49,669</b>
<b>Applications of Funds</b>				
Gross Block	20,043	19,899	22,221	23,221
Less: Accumulated Depreciation	13,158	13,944	15,208	16,571
<b>Net Block</b>	<b>6,885</b>	<b>5,955</b>	<b>7,013</b>	<b>6,650</b>
Capital Work in Progress	17	1,872	50	50
Investments	7,771	7,964	8,164	8,364
<b>Current Assets, Loans &amp; Advances</b>				
Inventories	1,735	2,333	2,774	3,677
Sundry Debtors	26,652	35,156	32,904	38,373
Cash and Bank Balance	954	1,196	1,106	1,057
Loans and Advances	51,656	51,851	39,023	30,623
Other Current Assets	4,469	5,714	6,934	8,668
<b>sub total</b>	<b>85,465</b>	<b>96,250</b>	<b>82,741</b>	<b>82,398</b>
<b>Less: Current Liabilities &amp; Provisions</b>				
Current Liabilities	30,132	39,411	37,511	46,032
Provisions	1,558	1,530	1,690	1,760
<b>sub total</b>	<b>31,690</b>	<b>40,941</b>	<b>39,201</b>	<b>47,792</b>
<b>Net Current Assets</b>	<b>53,775</b>	<b>55,309</b>	<b>43,540</b>	<b>34,606</b>
<b>Total Assets</b>	<b>68,448</b>	<b>71,099</b>	<b>58,767</b>	<b>49,669</b>

E – Estimates

### Cash Flow (Standalone)

Particulars (₹ mn)	Mar16	Mar17	Mar18E	Mar19E
<b>Profit before tax</b>	<b>1,404</b>	<b>970</b>	<b>3,633</b>	<b>8,680</b>
Depreciation	1,525	1,253	1,264	1,363
Finance cost	7,017	7,724	5,470	3,220
Other income	(1,995)	(2,205)	(2,648)	(2,675)
Others	463	193	0	0
Direct taxes paid	(52)	(185)	(1,163)	(2,777)
Change in Working Capital	(4,969)	(1,355)	11,678	8,885
<b>(A) CF from Operations</b>	<b>3,394</b>	<b>6,395</b>	<b>18,234</b>	<b>16,696</b>
Capex	(479)	(1,956)	(500)	(1,000)
<b>Free Cash Flow to Firm</b>	<b>2,915</b>	<b>4,439</b>	<b>17,734</b>	<b>15,696</b>
Inc./ (Dec.) in Investments	868	168	(200)	(200)
Others	38	3	2,648	2,675
<b>(B) CF from Investments</b>	<b>427</b>	<b>(1,785)</b>	<b>1,948</b>	<b>1,475</b>
Issue of Equity/ Preference	4,000	8,086	198	0
Inc./ (Dec.) in Debt	(690)	(6,762)	(15,000)	(15,000)
Interest exp net	(7,108)	(5,692)	(5,470)	(3,220)
Dividend Paid (Incl. Tax)	(1)	(2)	0	0
Other	(88)	3	0	0
<b>(C) CF from Financing</b>	<b>(3,887)</b>	<b>(4,368)</b>	<b>(20,272)</b>	<b>(18,220)</b>
Net Change in Cash	(67)	242	(90)	(50)
Opening Cash balances	1,020	954	1,196	1,106
Closing Cash balances	954	1,196	1,106	1,057

### Important Ratios

Particulars	Mar16	Mar17	Mar18E	Mar19E
<b>(A) Measures of Performance (%)</b>				
EBIDTA Margin (excl. O.I.)	19.3	18.0	15.9	16.7
EBIDTA Margin (incl. O.I.)	24.4	24.2	21.4	21.0
EBIT Margin	20.8	21.2	18.8	18.8
Interest/EBIT	80.6	86.7	60.1	27.1
Tax/PBT	32.5	38.7	34.0	34.0
Net Profit Margin	2.6	1.7	4.9	9.1
<b>(B) As Percentage of Net Sales</b>				
Raw Material	23.9	20.7	23.8	23.5
Construction Expenses	44.5	49.0	48.7	49.8
Employee Expenses	9.1	9.5	9.0	7.6
Other Expenses	3.2	2.8	2.6	2.4
<b>(C) Measures of Financial Status</b>				
Debt / Equity (x)	2.8	1.6	1.0	0.4
Interest Coverage (x)	1.5	1.3	1.9	4.1
Average Cost Of Debt (%)	13.8	16.4	15.0	15.0
Debtors Period (days)	232	306	248	221
Closing stock (days)	15	20	21	21
Working Capital (days)	459	312	459	259
Fixed Assets Turnover (x)	2.1	2.1	2.2	2.7
<b>(D) Measures of Investment</b>				
Diluted EPS (₹)	1.1	0.7	2.4	5.6
CEPS (₹)	2.4	1.8	3.6	7.0
DPS (₹)	0.0	0.0	0.0	0.0
Book Value (₹)	17.8	26.6	29.2	34.9
RoANW (%)	6.9	3.2	8.5	17.7
RoACE (%)	13.1	12.8	14.0	21.9
RoAIC (%)	15.2	14.6	16.3	24.0
<b>(E) Valuation Ratios</b>				
CMP (₹)	40	40	40	40
P/E (x)	37.4	56.4	16.8	7.0
Market Cap. (₹ Mn)	30,895	40,074	40,263	40,263
MCap/ Sales (x)	0.7	1.0	0.8	0.6
EV (₹ Mn)	80,761	86,158	75,579	60,648
EV/Sales (x)	1.9	2.1	1.6	1.0
EV/EBDITA (x)	10.0	11.4	9.8	5.7
P/BV (x)	2.2	1.5	1.4	1.1
FCFE Yield (%)	(12.4)	(20.1)	(6.8)	(6.3)
Dividend Yield (%)	0.0	0.0	0.0	0.0

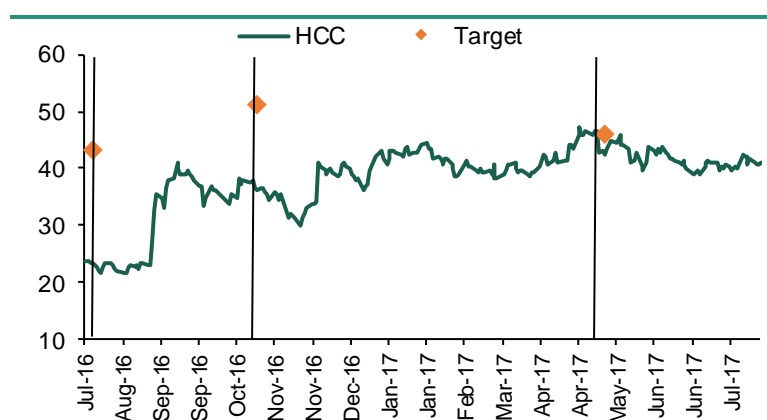
E – Estimates

## DART RATING MATRIX

Total Return Expectation (12 Months)

<b>Buy</b>	<b>&gt; 20%</b>
<b>Accumulate</b>	<b>10 to 20%</b>
<b>Reduce</b>	<b>0 to 10%</b>
<b>Sell</b>	<b>&lt; 0%</b>

## Rating and Target Price History



Month	Rating	TP (₹)	CMP (₹)
Jul'16	Buy	43	23
Oct'16	Buy	51	36
May'17	Accumulate	46	43

## DART Team

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**Analyst(s) Certification**

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