

India Construction Sector

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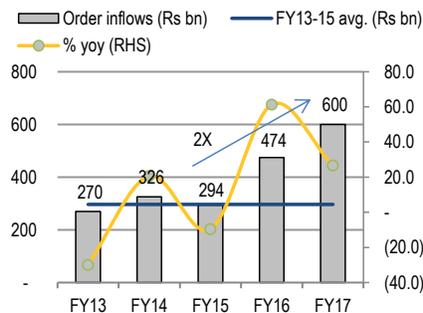
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INITIATION

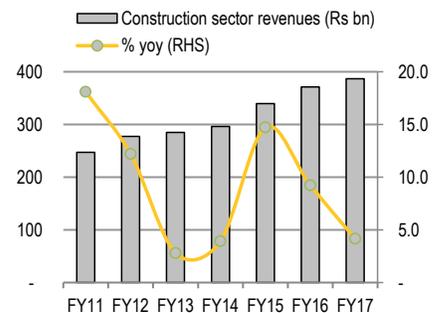
Play on infrastructure execution

Figure 1: Inflows up 2x vs FY15



Inflows of 11 construction companies.
Source: Company data

Figure 2: Revenues yet to pick up



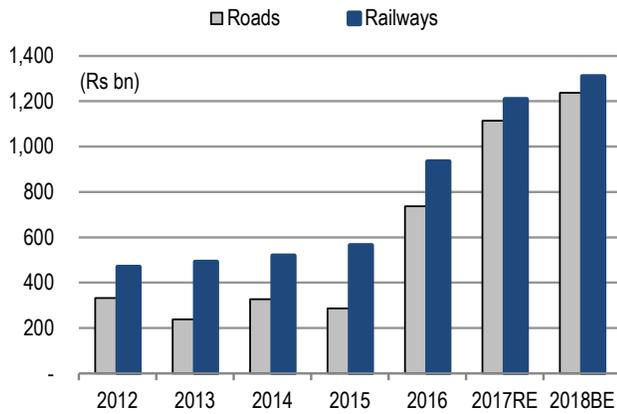
Source: Company data, Credit Suisse research

- Sector offers strong opportunity on government push.** Following up on our report in September 2016 ([Link](#)), we highlight that order inflows have continued to stack up (2x now vs the FY13-15 average). Macro tailwinds for a cyclical uptick are building up. Investment in infrastructure is growing (~10% CAGR, up ~40% from FY15-18E) after stagnating during FY12-15. The sector continues to offer strong opportunities in segments like roads, urban infrastructure (including metros) and institutional buildings. Core EPC returns remain strong (~20%), and most of the return dilution in the past cycle resulted from investments in infrastructure assets, real estate, etc. We expect a rise in activity to benefit L&T and Sadbhav as well.
- Execution catch-up and lower finance cost to buoy earnings.** Based on the aggregate of 12 listed construction companies, we highlight that while orders are up 2x, revenues are up only 25% (vs FY13-15), and thus, a lot of catch-up in execution is ahead of us, driving earnings from operating leverage. Fall in interest costs (as proportion) would buoy earnings further.
- Initiate with OUTPERFORM on Dilip Buildcon Ltd. (DBL) and J Kumar Infra Limited (JKIL).** We initiate on Dilip Buildcon Ltd. (DBL) with an OUTPERFORM rating (TP of Rs650 based on 18x full tax EPC earnings and 1x book for BOT investments) on (1) strong execution capabilities, (2) revenue visibility, and (3) 17% earnings CAGR. We initiate on J Kumar Infra (JKIL) with an OUTPERFORM rating (TP of Rs375 based on 18x FY19E earnings in line with peers) on (1) strong growth visibility, (2) 20% earnings CAGR over FY17-20E, (3) emergence as contractor for metros and sector/ geographical diversification. **Key risks** relate to (1) project concentration (particularly for JKIL), (2) sector concentration (urban infra in JKIL and roads in DBL), (3) management band width in family run firms, (4) delays in clearance for contracts (particularly hybrid contracts in DBL), and (5) rise in competition which will lower opportunity share and margins.

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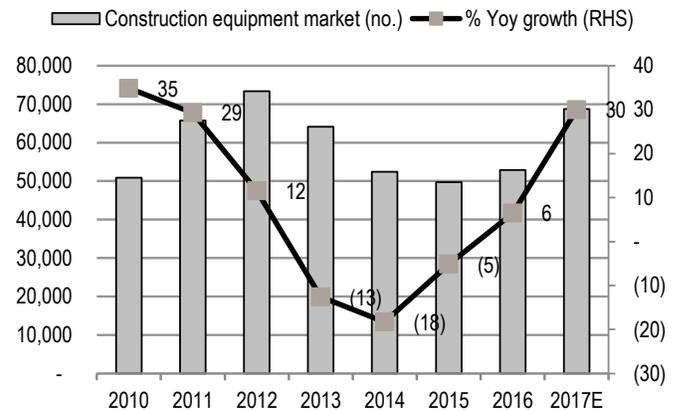
Focus charts and tables

Figure 3: Roads, rail capex up 3x over FY15-18E



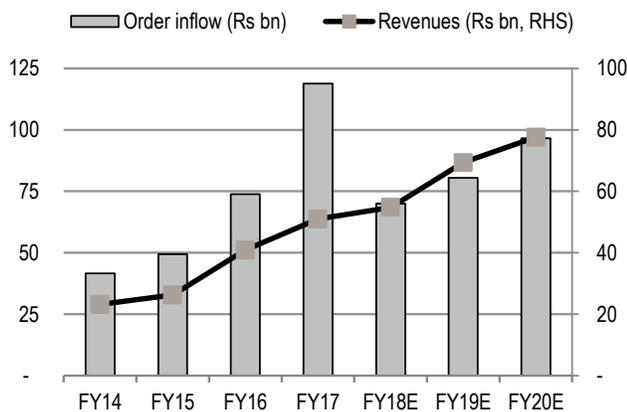
RE – Revised Estimate. BE – Budget estimate Source: Union Budgets, CS research

Figure 4: Construction equipment sales are rising



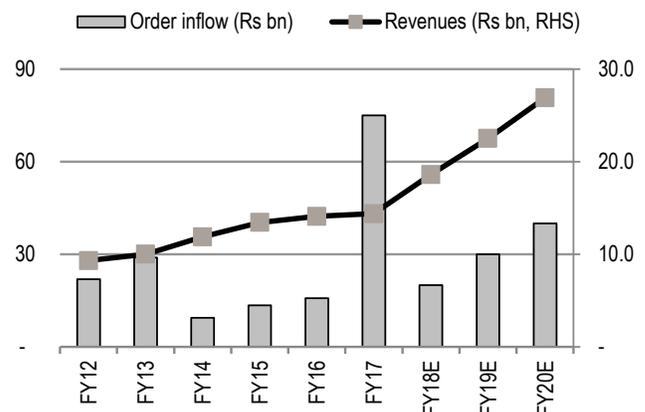
Source: Company data, Credit Suisse estimates

Figure 5: We expect DBL to post 15% revenue CAGR over FY17-20E



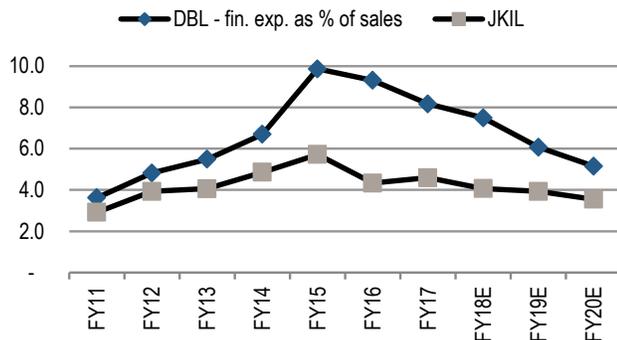
Source: Company data, Credit Suisse estimates

Figure 6: We expect JKIL to post 23% revenue CAGR over FY17-20E



Source: Company data, Credit Suisse estimates

Figure 7: Interest cost drag to reduce on bank debt repricing, replacement by market instruments



Source: Company data, Credit Suisse estimates

Figure 8: Valuation comparison

	CMP (Rs)	Mkt cap (Rs bn)	FY18 P/E (x)	FY19 P/E (x)	FY18E EV/EBITDA (x)	FY19E EV/EBITDA (x)
Ahluwalia*	320	21	19.8	15.5	11.0	9.3
Dilip Buildcon	439	60	19.0	12.6	8.3	6.9
Gayatri Projects*	160	28	20.3	14.2	14.8	11.8
HCC*	40	40	27.9	13.2	13.8	12.5
J. Kumar	294	22	16.6	14.6	7.6	6.7
KNR*	207	29	17.2	16.0	11.5	10.0
Simplex Infra*	508	25	20.7	15.2	7.7	6.9

* = Not covered. Source: Bloomberg estimates for not covered companies, Credit Suisse estimates for covered companies

Play on infrastructure execution

We highlight that the construction sector is recovering with investment in infrastructure sector growing (~10% CAGR, up ~40% between FY15 and FY18E) after stagnating between FY12 and FY15. A strong government push (specifically in roads and urban infrastructure), improving execution, lower interest cost in proportion to revenues should drive strong earnings growth for the companies. We initiate coverage on Dilip Buildcon Limited (DBL) and J Kumar Infra (JKIL) with an OUTPERFORM rating on the back of sectoral opportunity, strong medium-term earnings growth visibility and still reasonable valuations. Key risks relate to management bandwidth, the cyclical nature of the business, delay in approvals to work, and project/sector concentration risk.

Sector recovering; core returns strong, to get better

As a follow up to our report of September 2016, we present key construction sector trends (based on the aggregate of 12 listed companies). We highlight that (1) order inflows have almost doubled from FY13, even though this has mostly benefitted road focused players, (2) in spite of strong inflows, revenues have not seen as much benefit, with revenues up only 25% till FY17 from the FY13-15 average, (3) core business returns are strong and most of the dilution in returns result from unremunerative investments in infrastructure assets, real estate etc. (this proportion is reducing across companies on selldown, caution in incremental investments), and (4) working capital has remained high (a large proportion of EBITDA goes to service interest) and is trending down slowly. Associated interest cost is likely to come down in proportion to revenues (as execution improves and companies capture the benefit of a lower interest rate environment) driving strong earnings growth.

The sector has been a long-term underperformer, driven by its natural fragmentation, cyclicity and large non-core investments on the balance sheet. While the long-term issues of fragmentation may remain, the sector may still be positioned for significant cyclical upturn in earnings.

Initiate with OUTPERFORM on Dilip Buildcon (DBL) and J Kumar Infra (JKIL)

Initiate on DBL with an OUTPERFORM rating (TP of Rs650 based on 18x full tax EPC earnings and 1x book for BOT investments) on the back of (1) strong revenue visibility, (2) 17% earnings CAGR, and (3) focused execution and differentiated position. **Channel check from peers, equipment suppliers etc., seems very positive.**

Initiate on JKIL (TP of Rs375 based on 18x FY19E earnings in line with peers) with an OUTPERFORM rating on (1) strong growth visibility, (2) 20% earnings CAGR between FY17-20E, and (3) emergence as contractor for metros.

Key risks: project concentration, delays, band width

Key risks relate to: (1) project concentration (particularly for JKIL with Mumbai Metro contracts contributing about two-thirds of the backlog), (2) sector concentration (e.g. roads in DBL contribute about 80% of the backlog), (3) a lot of diversification vs the past track record is yet to pan out and can bring forth risks when those projects are actually executed (vs projects executed in MP for DBL and Mumbai flyovers/skywalk in case of JKIL), (4) management band width in family run firms can become a constraint to growth, (5) delays in clearance for contracts (particularly the recently won road hybrid contracts in DBL that are yet to get an appointed date), and (6) increase in competitive intensity which will lower opportunity share and margins.

Valuation summary

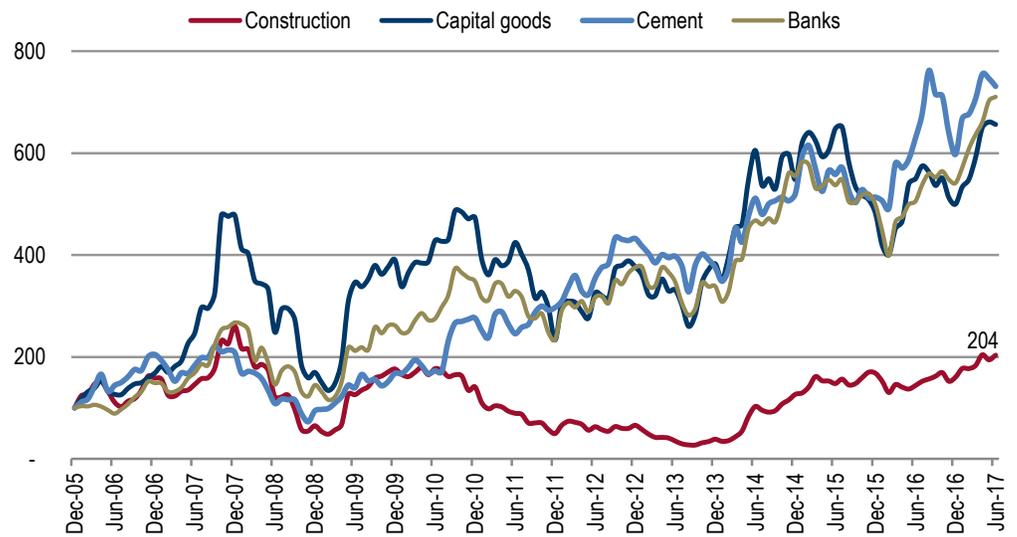
Figure 9: Valuation matrix of construction companies

	CMP (Rs)	ADTO (\$mn)	M-cap (Rs bn)	Sales (Rs bn)		EPS (Rs)		P/E (x)		EV/EBITDA (x)		P/B (x)		RoE (%)		12M perf (%)
				2018E	2019E	2018E	2019E	2018E	2019E	2018E	2019E	2018E	2019E	2018E	2019E	
Coverage companies																
Dilip Buildcon	439	1.7	60	55	69	23	35	19.0	12.6	8.3	6.9	2.8	2.3	15.8	20.0	NA
J. Kumar	294	1.4	22	19	22	18	20	16.6	14.6	7.6	6.7	1.5	1.4	9.3	9.7	31.5
Peer group																
Ahluwalia Contracts*	320	0.3	21	16	18	16	21	19.8	15.5	11.0	9.3	3.5	2.9	18.8	19.7	14.7
Gayatri Projects*	160	0.7	28	30	38	8	11	20.3	14.2	14.8	11.8	2.6	2.2	13.5	19.8	28.4
HCC*	40	5.1	40	47	54	1	3	27.9	13.2	13.8	12.5	1.4	1.3	5.5	8.7	95.6
KNR Constructions*	207	0.4	29	18	20	12	13	17.2	16.0	11.5	10.0	2.8	2.4	17.2	16.1	93.4
NBCC*	204	5.9	184	87	122	6	8	33.5	26.3	29.5	19.6	9.2	7.4	26.0	30.4	60.2
PNC Infratech*	143	1.3	37	27	36	2	5	87.5	30.2	9.2	7.6	2.3	2.1	(5.5)	(1.1)	28.0
Simplex Infra*	508	0.3	25	64	68	25	33	20.7	15.2	7.7	6.9	1.5	1.4	7.7	9.4	94.1

Note: * = Not covered.
Source: the BLOOMBERG PROFESSIONAL™ service for not covered companies, Credit Suisse estimates for covered companies.

Long laggard construction did catch up last year

Figure 10: Construction sector has lagged far behind in market cap growth in the last decade as compared to other sectors



Construction includes ten companies (NCC, Ahluwalia, IVRCL, Gammon, Simplex, HCC, KNR, MBL, J Kumar and Ashoka).
Source: Company data, Credit Suisse estimates

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Play on infrastructure execution

We highlight that the opportunity basket is growing as overall infrastructure spend in the country is starting to grow again after a long stagnation, driven by public sector investments in road and rail sectors, and potential for crowding in private investments at a later stage. We note positive tidings in construction equipment sales, favourable government policies on clearances and claim settlements as well as INVITS (Infrastructure investment Trusts) providing access to an additional pool of capital.

Expect activity to be driven by the public sector

We expect the public sector to drive capex/ordering momentum in FY17 as well. Focus will remain on roads, railways, power T&D and buildings sectors. While roads and railways will continue to be driven by the central government, in the case of power transmission & distribution (T&D), we expect State Electricity Boards (SEBs) to invest in T&D infrastructure once their balance sheets are repaired with the help of the UDAY (Ujjawal Discom Assurance Yojana) scheme. Housing/buildings segment will be driven by Public Sector Undertakings (PSUs) as well as state government/departments in addition to Smart City related ordering.

Indian Infra capex growing after a long hiatus

Total spending stagnated between FY12 and FY15 at about US\$100 bn after having doubled between FY07 and FY12. Growth has come back with FY17E capex likely at US\$124 bn, and this growth is primarily driven by higher spends in roads and railways.

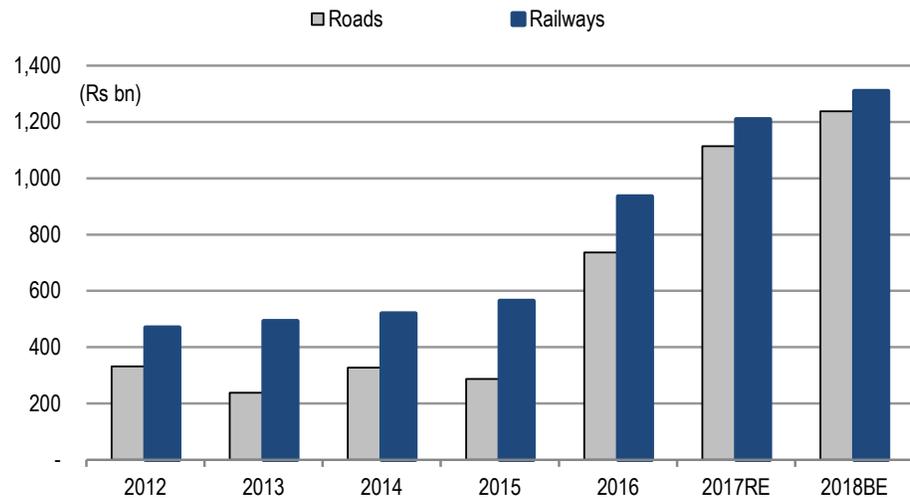
Private sector share remains ~20%, with the bulk of it coming from thermal power (last remnants of the past cycle), telecom and renewables. The aim to have half the spend from private (FY12-17) has not even come close, as the private sector retreated from roads and power and has not entered sectors such as railways as yet.

Figure 11: Capex is beginning to grow after being stagnant over FY12-15

US\$ bn	FY07	FY12	FY15	FY16E	FY17E	FY18E
Electricity	15.4	34.9	32.8	31.5	34.7	38.8
- Thermal, others			15.2	11.5	10.4	10.4
- Renewables			3.3	5.5	9.0	11.2
- Transmission			7.8	8.1	8.2	9.0
- Distribution			6.5	6.4	7.1	8.2
Roads & bridges	8.6	20.3	18.3	24.7	30.2	33.3
Telecommunications	8.1	17.2	11.9	14.2	13.4	13.4
Railways	5.8	10.8	10.6	16.1	18.6	21.4
Irrigation	6.8	10.9	11.1	11.5	12.3	13.5
Water supply & sanitation	3.4	5.4	6.8	6.3	6.7	7.3
Ports	1.2	2.0	1.8	1.7	1.6	1.8
Airports	0.4	1.6	1.0	0.9	0.9	0.9
Storage	0.3	0.8	0.5	0.4	0.4	0.4
Oil & gas pipelines	1.3	2.8	1.0	1.0	1.0	1.0
Total in US\$ bn	51.3	106.8	95.7	108.2	119.8	131.9

Source: Company data, Credit Suisse estimates

Figure 12: Public spending in roads and rail now almost at 3x the FY15 level

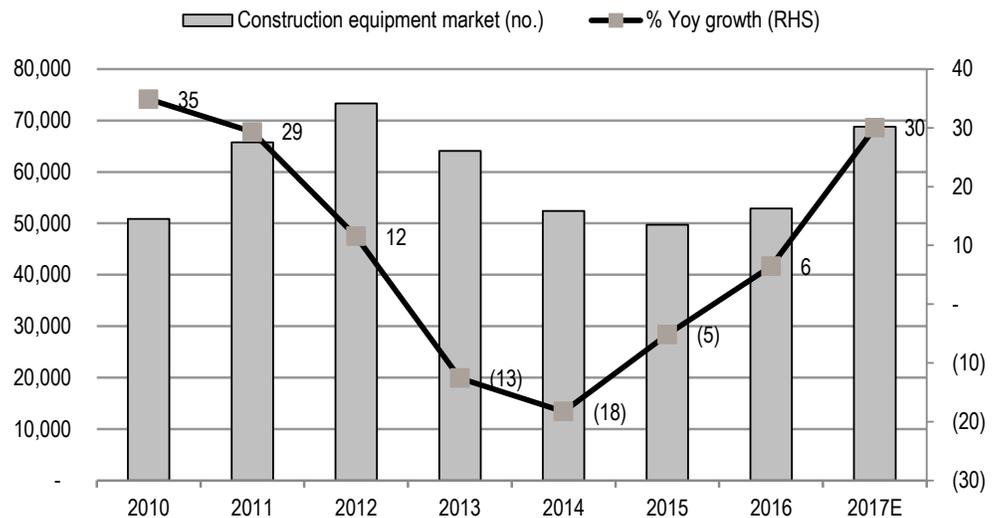


Source: Company data, Credit Suisse estimates

Construction equipment sector growth very strong after years of decline

We highlight that the construction equipment sector has started to grow again after declining for three years between FY12 and FY15. FY17 sales have been about 70,000 machines (US\$4 bn of sales) versus 55,000 in FY16. FY18 promises to have strong growth as well with the FY11/FY12 peak likely to be crossed in FY18. This is a strong signal that construction activity is reviving.

Figure 13: Construction equipment market grew ~30% in FY17E

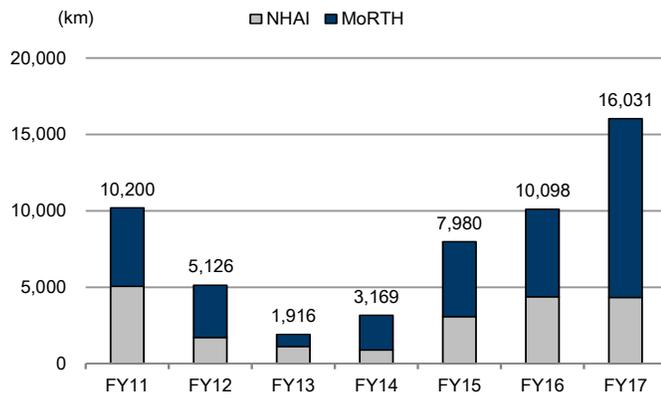


Source: ICEMA, Credit Suisse estimates

Road sector remains a strong opportunity: >5x from bottom

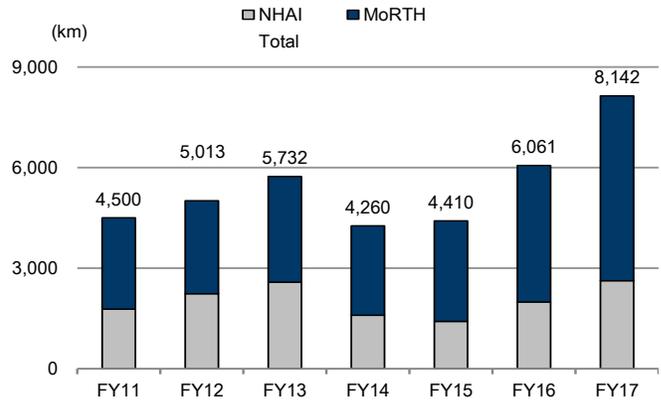
We highlight that ordering has become more than 4-5x from bottom and continues to remain strong. Execution is also picking up (measured in km completion) and that would support the sector.

Figure 14: Road awarding remains strong



FY12 data adjusted for project cancellations. Source: NHAI, Credit Suisse estimates

Figure 15: Construction has picked up as well



Source: Company data, Credit Suisse estimates

Urban Infrastructure: large opportunity unfolding

We highlight that urban infrastructure is emerging as a large opportunity with urban infrastructure improvement becoming a political showcase. Opportunities are arising in mass rapid transport (metros), roads and water supply. We highlight the opportunity in metros arising from various cities across the country. We believe that the rough annual size of this opportunity is in the range of about Rs300 bn p.a.

Figure 16: Post the success of the Delhi metro, projects are under way in most of the large cities

City	State	Population (mn)	Current status
Mumbai	MH	12.5	Few lines under development; more lines to be awarded
Delhi	DL	11.0	Phase I & II completed; Phase III under development; Phase IV approved
Bengaluru	KN	8.4	Couple of lines completed (in phases); remains under development
Hyderabad	TL	6.8	Under construction via private sector participation (L&T)
Ahmedabad	GJ	5.6	Phase I under development
Chennai	TN	4.7	Phase I in final stages of development; Phase II likely to get approved soon
Kolkata	WB	4.5	Old metro system under operation
Surat	GJ	4.5	Rs120 bn project approved; DPR under preparation
Pune	MH	3.1	Contracts award under progress
Jaipur	RJ	3.1	First phase commissioned; second phase under development
Lucknow	UP	2.8	First phase to be operational in near term; second phase under construction
Kanpur	UP	2.8	Project approved; contracts to be awarded
Nagpur	MH	2.4	Project under construction/Awards under way
Indore	MP	2.0	DPR approved
Thane	MH	1.8	Project announced by state government
Bhopal	MP	1.8	DPR approved
Visakhapatnam	AP	1.7	Approval sought from Central government
Varanasi	UP	1.2	Approved
Kochi	KL	0.6	Under development

Source: Company data, Credit Suisse estimates

Government proactive: aiding recovery

The government seems quite proactive in aiding the recovery of the sector with several steps like (1) easing out several project level clearances, (2) strong political focus on project progress, (3) policy for making time-bound claim payments and time-bound arbitration, (4) move to EPC contracts, particularly in sectors such as railways, where sub-scale projects are still the norm, and (4) establishing framework for INVITS that opens up a new and large pool of capital for the sector, helping to bring liquidity for clogged balance sheets.

Sector recovering; core returns strong, to get better

We highlight that the sector is on a recovery path with (1) improved order inflows, (2) likelihood of revenue growth acceleration on the back of improved inflows, and (3) lower finance costs.

We highlight that core EPC business returns are strong for most companies in spite of sector fragmentation. Most often these strong returns are diluted by investments in non-core businesses such as BOT infrastructure development, power and real estate, among others.

Sector order inflows almost double from bottom

We highlight that sector order inflows (sum of order inflows for eleven companies) has doubled to Rs600 bn in FY16 from Rs294 bn in FY15.

Figure 17: Order inflows have grown at 23% CAGR over FY13-16E

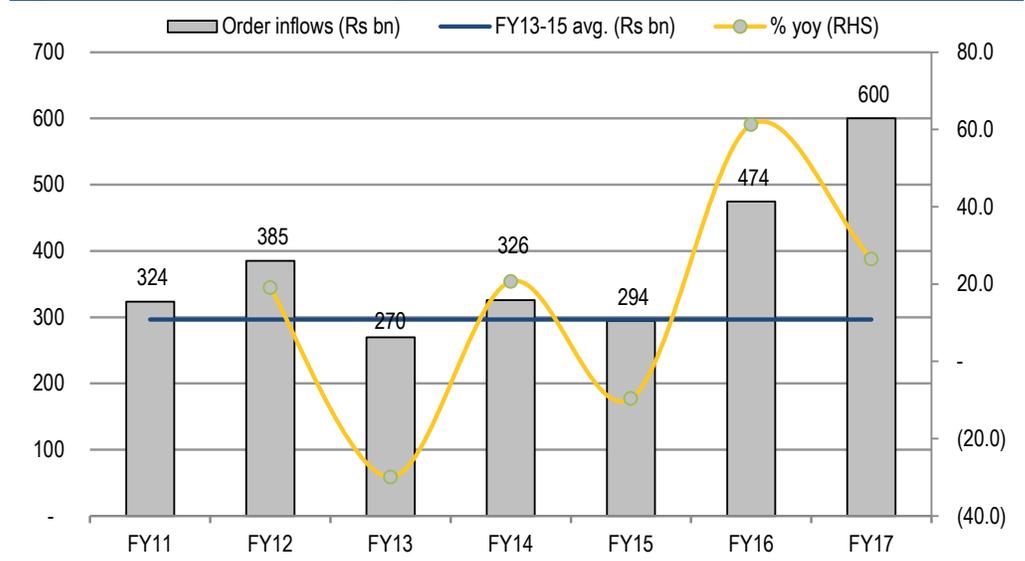
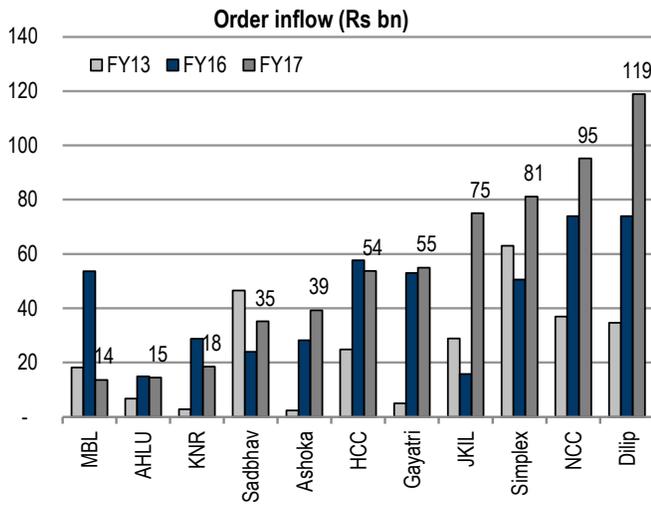
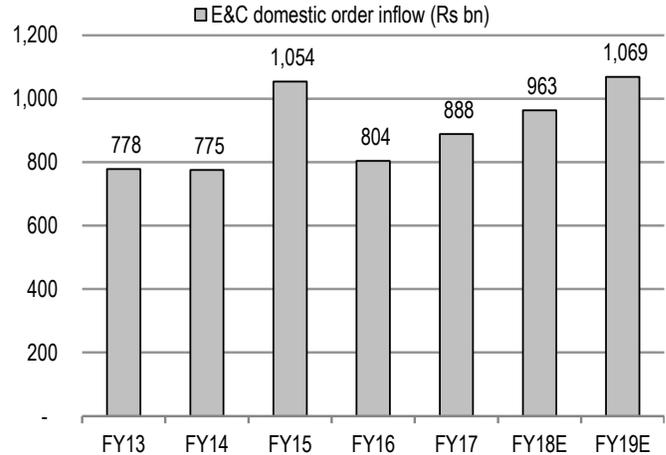


Figure 18: FY17 inflows strong for most companies



AHLU – Ahluwalia; JKIL – J Kumar. Source: Company, Credit Suisse research

Figure 19: L&T domestic EPC inflow stable



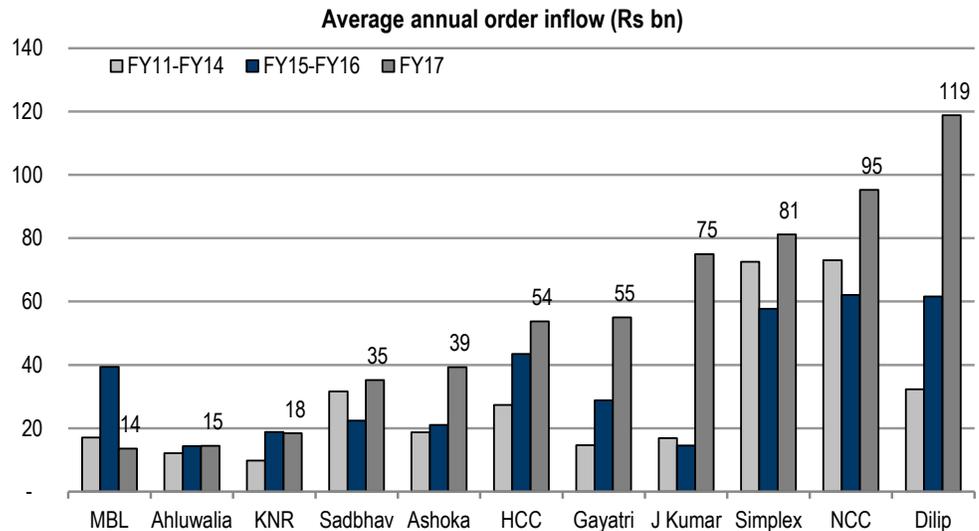
Source: Company data, Credit Suisse estimates

Momentum favourable for road focused contractors

We note that there is a distinct pick-up in order inflows of Ahluwalia Contracts, NBCC, KNR, JKIL and Gayatri Projects in the last two years as compared to their annual run-rate during FY11-14. A lot of these orders are concentrated in the roads and metro sectors.

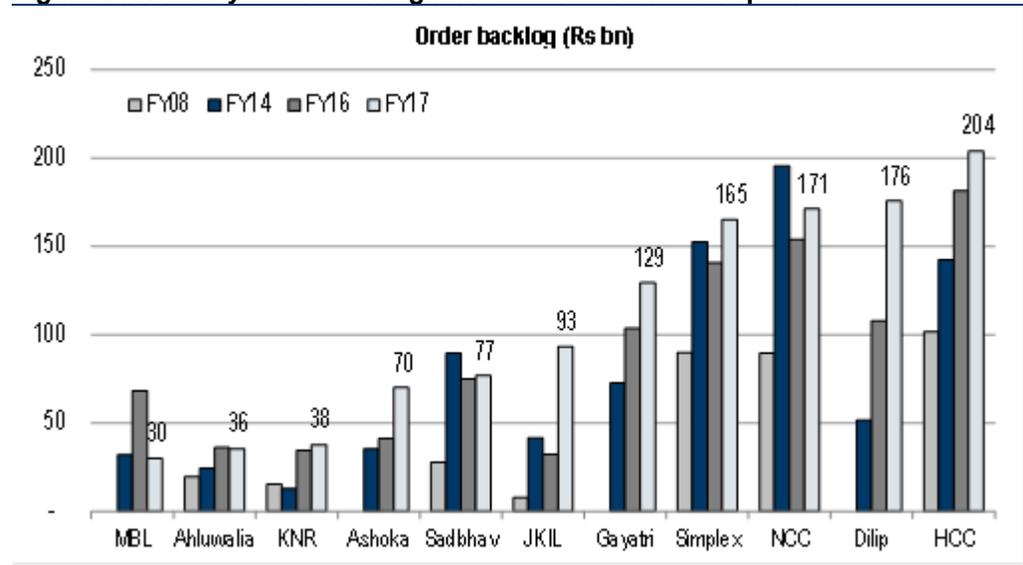
Even companies like NCC and Simplex Infra, where ordering momentum was weak in FY16 (slowdown in buildings segment), seem to be catching up now.

Figure 20: Sharp pick-up in inflows for road focused companies



Note: NCC numbers include parent company orders.
Source: Company data, Credit Suisse estimates for covered companies

Figure 21: Healthy order backlog for most of construction peers

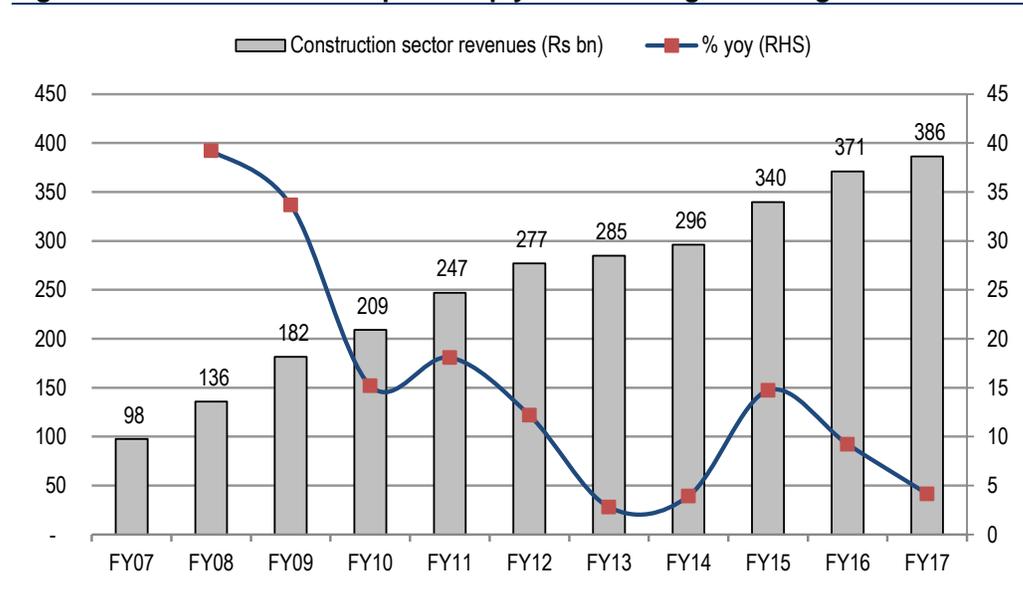


Note: NCC numbers include only domestic orders.
Source: Company data, Credit Suisse research

Revenue growth pick-up ahead of us

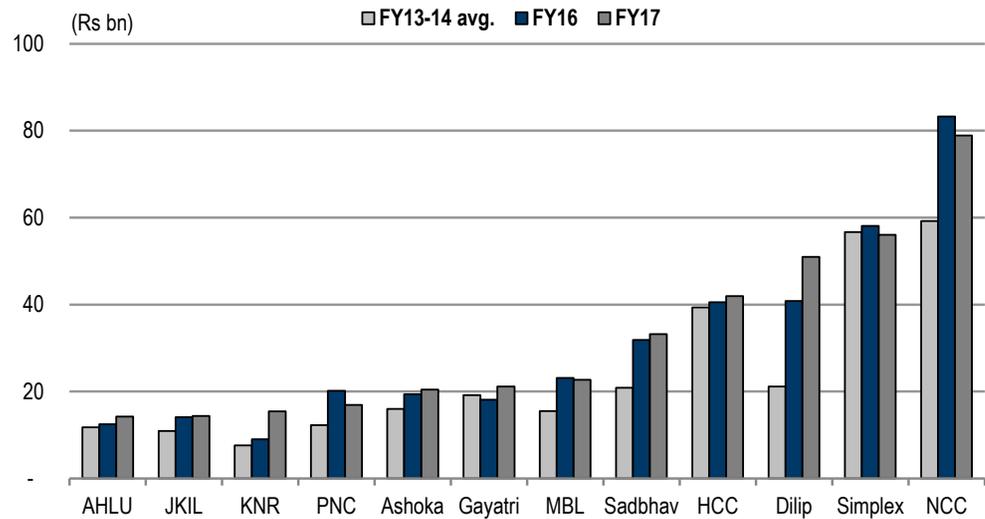
While order inflows have been strong for the sector, revenue growth has not yet gained as much momentum, implying that revenue growth momentum is ahead of us. While order inflows have doubled over FY15 to FY17 for the sample of companies that we have analysed, FY17 revenues are up only 25% as compared to FY13-FY15 average.

Figure 22: Execution has not picked up yet even though ordering has increased



Source: Companies, Credit Suisse research

Figure 23: Revenue growth yet to pick-up for most companies



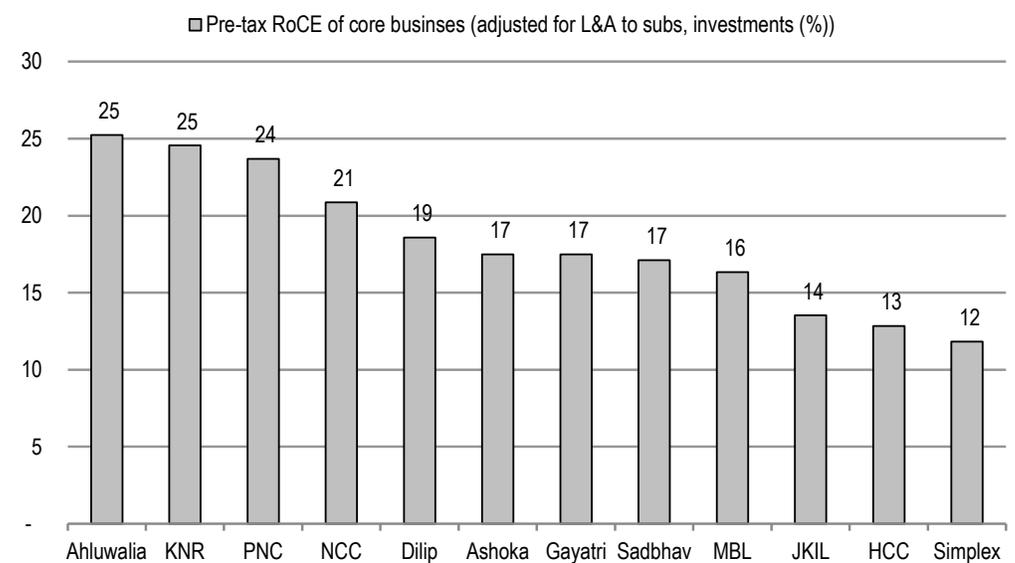
Source: Company data, Credit Suisse research

Adequate rewards for toil: diluted by non-core

We highlight that the returns ratios for the core business are reasonably strong despite sector fragmentation with reasonably high working capital across most companies.

Capital deployment in non-core business has led to dilution of returns for the consolidated entities and poor credit situations, including debt restructuring, in some companies. Several companies have more than 50% of their standalone capital deployment in real estate and BOT assets which are earning low returns for them.

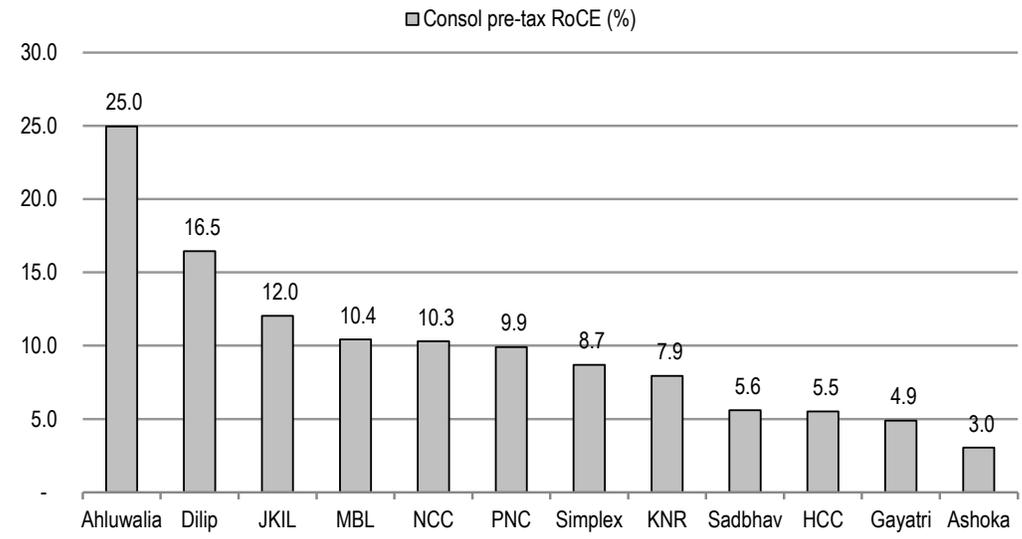
Figure 24: Pre-tax RoCE of construction business strong



RoCE calculation is pre-tax (FY16 data as FY17 balance sheets not yet available).
Source: Company data, Credit Suisse research

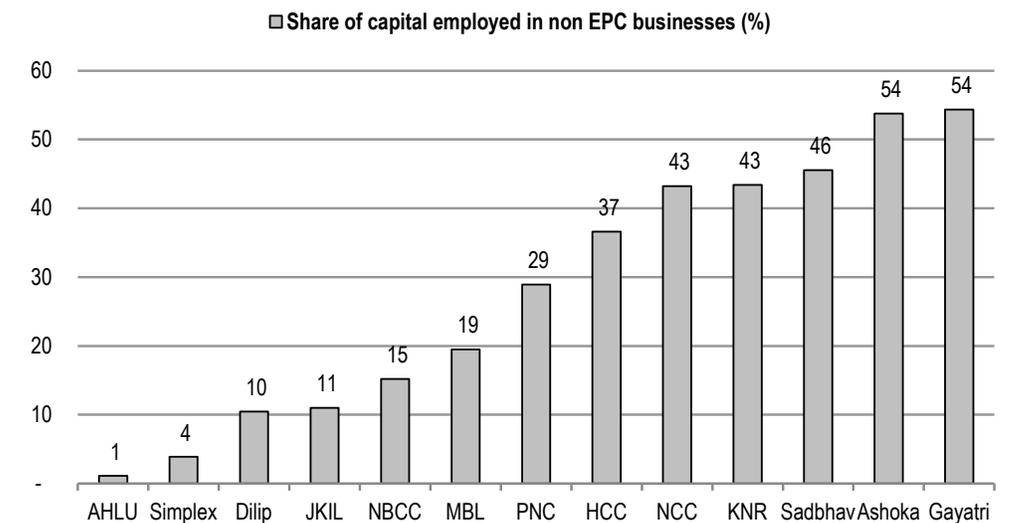
Returns dragged by non-core investments—much less for JKIL/DBL

Figure 25: Consolidated RoCE dragged by non-core investments



Source: Company data, Credit Suisse research

Figure 26: Share of capital employed (std. company) in non EPC businesses*



* Includes investments, L&A to subs, associates, related parties.

Source: Company data, Credit Suisse research. Based on FY16 data (as FY17 balance sheets are not yet available).

JKIL and DBL have no exposure to toll contracts/real estate

While working capital has continued to remain high, both DBL and JKIL have not had any exposure to real estate and power sector. DBL has exposure to road development contracts but almost all of this exposure is through annuity-based contracts, and thus, has not become a drag on financials. Many construction companies are beset with sub-optimal infrastructure development projects that have dragged the balance sheet.

Working capital still high but lower than FY16 levels

One of the key issues in the past cycle was a sharp rise in working capital for most construction companies, which led to high leverage and low returns. We note that companies seem to be trying to address this anomaly, and the FY17 working capital levels

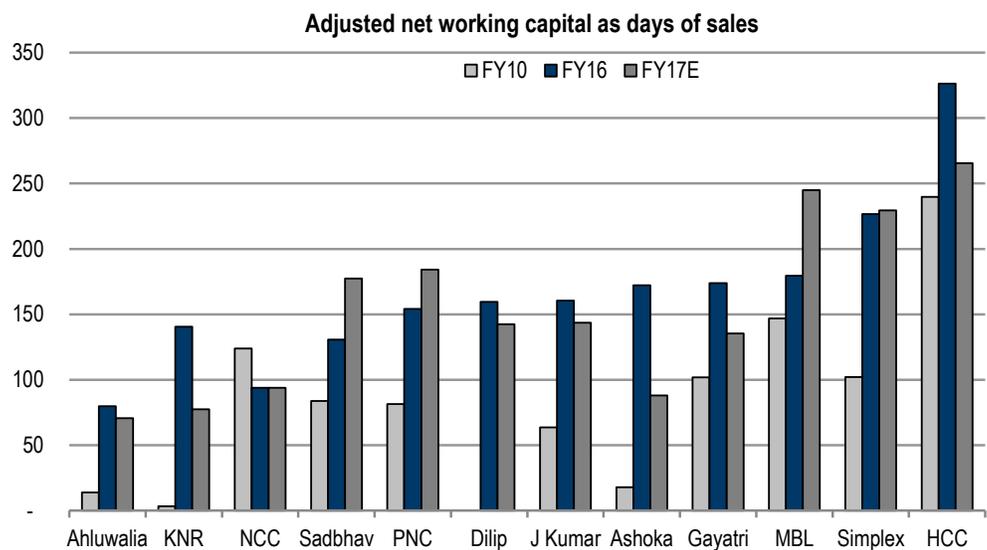
seem slightly better as compared to FY16's level for many companies. Debt levels of companies have also remained similar to FY16 as incremental support/investment in BOT assets was not there for most companies.

Among companies under our coverage, Dilip Buildcon (DBL) and J Kumar Infra Limited (JKIL) have moved to public sector projects, where bad debts are relatively lower as compared to the private sector projects.

In the case of DBL, while the company is continuing to invest in BOT assets since most of them are annuity-based projects, there is no exposure to traffic risk. As a result, DBL is only exposed to execution risk, which it has managed well.

JKIL has stayed away from committing capital in BOT projects, and hence, its balance sheet has remained light and leverage has remained below 1x in the last ten years.

Figure 27: Working capital has seen only modest improvement for some

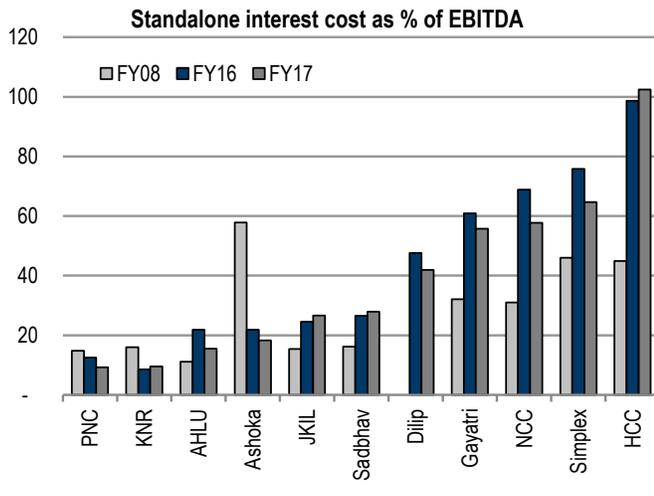


Note: Working capital adjusted for L&A to subs, related parties. FY17 net working capital is estimated as balance sheet data is not yet available (L&A to subs, associates, related parties).
 Source: Company data, Credit Suisse estimates.

Lower interest rates can buoy earnings further

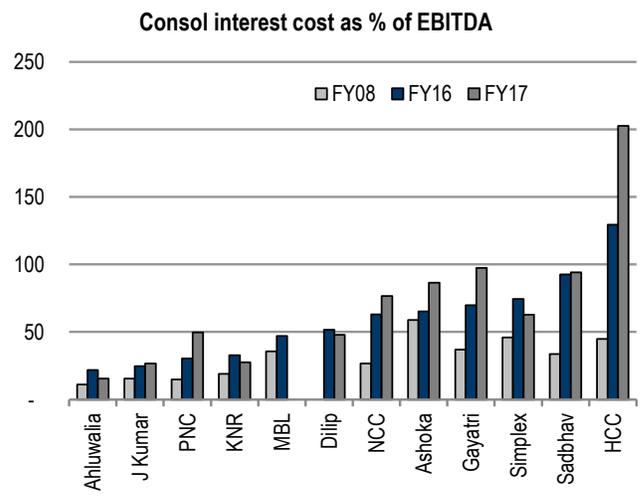
We highlight that construction companies have a very high proportion of their EBITDA being consumed by interest cost leaving limited fall through to the bottom line. Given this, the construction sector can be a substantial beneficiary of lower interest rates. Even though policy rates and G-sec yields have moderated in the last year, complete benefit will get transmitted to EPC companies when loans get repriced. Also, the companies are working towards replacing expensive bank debt by less expensive commercial paper.

Figure 28: Interest consumes half of EBITDA...



Source: Company data, Credit Suisse research

Figure 29: ...even more in consolidated accounts

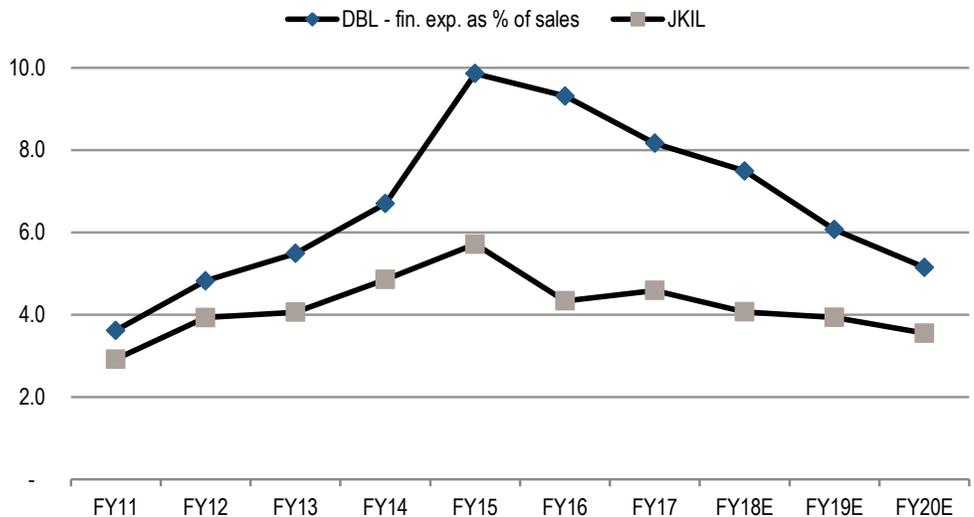


Source: Company data, Credit Suisse research

Interest cost to decline in proportion to revenues driving earnings

We highlight interest cost as % of sales for both DBL and JKIL. We envisage absolute interest cost to stay flat in DBL, driving a meaningfully stronger PBT growth (~28%) versus EBITDA growth of 13%. We expect JKIL's interest cost to rise in absolute terms but still contribute 100 bp to PBT margin over FY17-20E.

Figure 30: Financial expenses to moderate as % of sales over the next few years



Source: Company data, Credit Suisse estimates

Initiate with OUTPERFORM on DBL, JKIL

We initiate coverage on Dilip Buildcon Limited (DBL) and J Kumar Infra (JKIL) with OUTPERFORM ratings. We like DBL (TP of Rs650 based on 18x full tax EPC earnings and 1x book for BOT investments) for its (1) strong execution capabilities, (2) healthy revenue visibility, and (3) ~17% earnings CAGR over FY17-20E. We like JKIL (TP of Rs375 based on 18x FY19E earnings in line with peers) for its (1) strong growth visibility, (2) ~20% earnings CAGR between FY17 and FY20E, and (3) emergence as a contractor for metros.

Key risks relate to: (1) project concentration (particularly for JKIL), (2) sector concentration (urban infra in JKIL and roads in DBL), (3) management band width in family run firms, (4) delays in clearance for contracts (particularly hybrid contracts for DBL), and (5) increase in competitive intensity which will lower opportunity share and margins.

Key risks: project concentration, delays, band width

Key risks relate to (1) project concentration (particularly in JKIL with Mumbai Metro contracts contributing about two-thirds of the backlog), (2) sector concentration (e.g. roads in DBL contribute to about 80% of the backlog), (3) lot of diversification vs the last track record is yet to pan out and can bring forth risks when those projects are actually executed (vs projects executed in MP for DBL and Mumbai flyovers/skywalks in case of JKIL), (4) management band width in family-run firms can become a constraint to growth, (5) delays in clearance for contracts (particularly the recently won road hybrid contracts in DBL that are yet to get an appointed date), and (6) increase in competitive intensity which will lower opportunity share and margins.

Asset heavy model can impact profitability in down cycle

Both JKIL and DBL have chosen to adopt an asset heavy model with most of the work done in-house. This strategy can impact margins and profitability if ordering activity in the domestic market/specific focus segments moderates. In the case of JKIL, we believe that metro ordering in and around Mumbai should continue in the medium term. In the case of DBL, strong activity in the roads sector and efforts towards diversification by the company should help it address this risk.

Management band width can pose a constraint as companies grow further

Both companies have hands-on management, which has helped them achieve healthy growth over past years. However, as the companies grow further, management band width could pose a constraint. DBL has been trying to use technology to its advantage to address this issue. In the case of JKIL, project concentration has helped the promoter group manage the projects well.

Execution delays, competitive intensity and raw material price movement

EPC contracts are prone to delays on account of various internal and external factors. Both JKIL and DBL use their own equipment, which helps them in expediting the execution. Most projects under development have already received clearances, and are secured from financially strong and well-funded clients.

The companies need to continuously bid for new projects, and the rise in competitive intensity could impact the margin profile of new orders. JKIL has carved a niche for itself by focusing on metro projects, and can continue to operate with healthy margins unless competitive intensity becomes very severe (unlikely in the near term as most companies have healthy order backlogs). In DBL's case, NHAI and MORTH continue to award road contracts in large numbers, and hence, competitive intensity should remain benign in the medium term at least.

Sharp movement in raw material prices can have an impact on margins on EPC projects, where price variation clauses are not there. In the case of DBL, 40% of orders are secured from owned SPVs (special purpose vehicles) on a fixed-price basis. On these projects, the company has already built some cushion to offset any normal rise in raw material prices. Also, the recent movement in commodity prices has been range-bound with a negative bias, and hence, the possibility of a negative impact looks unlikely in the near term. JKIL's contracts have been secured from external clients with adequate price variation clauses.

Dilip Buildcon Ltd (DIBL.BO / DBL IN)

INITIATION

Rating	OUTPERFORM
Price (29-Jun-17, Rs)	438.20
Target price (Rs)	650.00
Upside/downside (%)	48.3
Mkt cap (Rs/US\$ mn)	59,933 / 926.96
Enterprise value (Rs mn)	83,948
Number of shares (mn)	136.77
Free float (%)	24.4
52-wk price range (Rs)	500-200
ADTO-6M (US\$ mn)	1.7

Target price is for 12 months.

[V] = Stock Considered Volatile (see Disclosure Appendix)

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Differentiated vertically integrated model

- Differentiated vertically integrated model.** DBL is a pan-India road (+80% of backlog)-focused EPC company, which undertakes all aspects of construction (including equipment ownership) by itself, without relying on subcontractors unlike most peers. Strong execution and an integrated model have helped the company grow (50% CAGR over FY11-17), earn higher margins and deliver projects ahead of schedule. The company has been able to move away from its dependence on Madhya Pradesh (its home state) and it is also diversifying from roads into early wins in contract mining. We initiate on DBL with OUTPERFORM and a target price of Rs650 (48% upside).
- ~17% earnings CAGR with strong return ratios.** We expect DBL to register 17% earnings CAGR in FY17-20 due to (1) execution of backlog worth Rs175 bn, and (2) PBT margin expansion with flattish EBITDA margin on falling interest costs. Its PBT CAGR is ~28% but part of it is negated by likely tax rate increases. DBL has enjoyed tax advantages on investments in machinery (expiring post FY18) and road development (80-IA). We factor in tax incentives on hybrid contracts to continue and build an average 20% effective tax rate over FY18-20E versus ~nil in FY17. We expect 16-20% ROE during FY17-20.
- BOT strategy: ready for churn.** DBL is working towards selling stake in its BOT portfolio (Rs6.5 bn deployed so far and is likely to invest over Rs8 bn over the next few years), which could reduce its equity commitment and help it churn capital, making the balance sheet more efficient. The company currently has 14 operational and ten under-construction projects. Majority of the projects are based on either annuity model or hybrid annuity model.
- Initiate with OUTPERFORM.** Our target price of Rs650 comprises Rs560 for the EPC business (18x FY19E earnings) and 1x book for BOT investment. The P/E multiple of 18x is based on (1) 17% earnings CAGR, (2) sector opportunity and (3) focused execution and differentiated position. Our channel check with peers and equipment suppliers yielded positive views. Risks include (1) delay in start of recent project wins, (2) less flexibility to deal with down cycles, and (3) promoter's family-driven management and its band width constraints.

Share price performance



The price relative chart measures performance against the S&P BSE SENSEX IDX which closed at 30,857.52 on 29/06/17. On 29/06/17 the spot exchange rate was Rs64.66/US\$1

Performance	1M	3M	12M
Absolute (%)	-0.9	24.9	
Relative (%)	0.1	20.7	

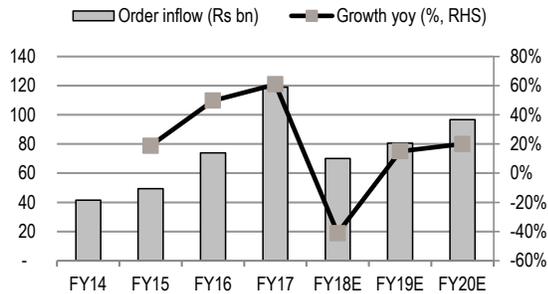
Financial and valuation metrics

Year	3/17A	3/18E	3/19E	3/20E
Revenue (Rs mn)	50,976.4	54,777.6	69,346.6	77,611.2
EBITDA (Rs mn)	9,922.8	10,124.1	12,816.8	14,344.2
EBIT (Rs mn)	7,648.9	7,472.4	10,023.2	11,418.9
Net profit (Rs mn)	3,609.8	3,154.2	4,758.7	5,780.5
EPS (CS adj.) (Rs)	26.39	23.06	34.79	42.26
Change from previous EPS (%)	n.a.	-	-	-
Consensus EPS (Rs)	n.a.	27.41	34.95	
EPS growth (%)	40.6	(12.6)	50.9	21.5
P/E (x)	16.6	19.0	12.6	10.4
Dividend yield (%)	31.2	31.2	31.2	31.2
EV/EBITDA (x)	8.5	8.3	6.9	5.9
P/B (x)	3.23	2.79	2.30	1.89
ROE (%)	24.5	15.8	20.0	20.0
Net debt/equity (%)	129.1	112.9	107.2	77.9

Source: Company data, Thomson Reuters, Credit Suisse estimates

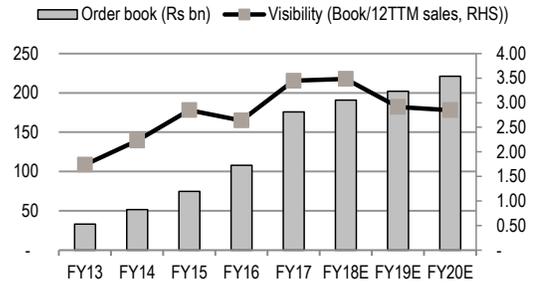
Focus charts

Figure 31: Strong inflows in FY17; expect a pick-up again from FY19 after moderating in FY18E...



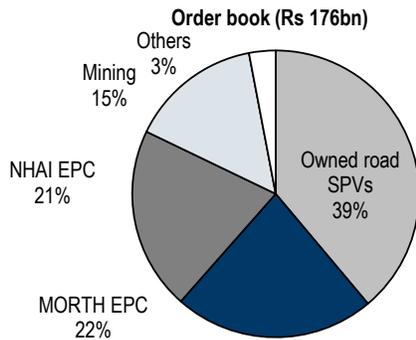
Source: Company data, Credit Suisse estimates

Figure 32: ...order backlog, however, remains healthy and provides strong visibility



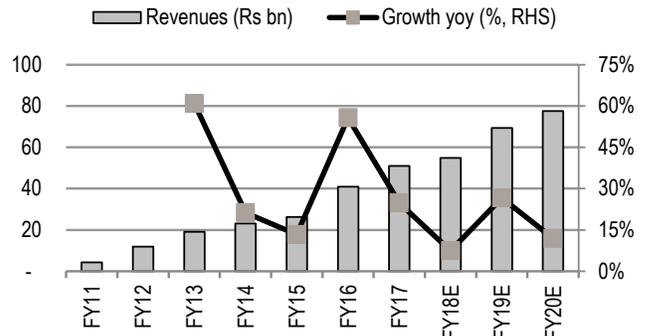
Source: Company data, Credit Suisse estimates

Figure 33: Owned SPVs, NHAI and MORTH account for over 80% of orders



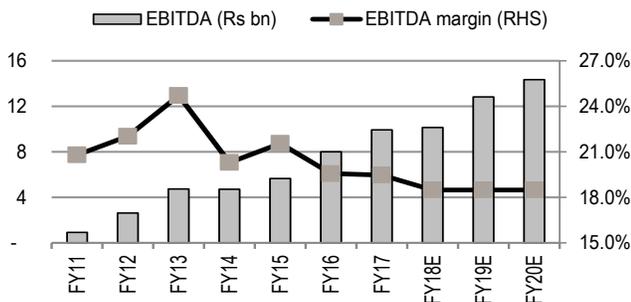
Source: Company data, Credit Suisse research

Figure 34: We estimate a revenue CAGR of 15% over FY17-20E



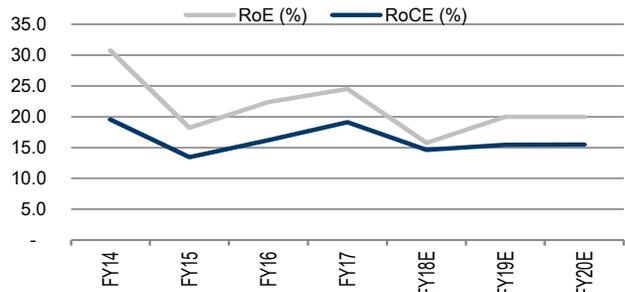
Source: Company data, Credit Suisse estimates

Figure 35: We build moderation into the EBITDA margin vs history



Source: Company data, Credit Suisse estimates

Figure 36: Return ratios are healthy



Source: Company data, Credit Suisse estimates

Figure 37: Our SOTP-based target price is Rs650

	Earnings/book	Multiple	Value	Value per share (Rs)	Valn methodology
Normalised PAT at 30% tax rate	4,164	18.0	74,949	560	P/E multiple
Investment in subsidiaries	12,757	1.0	12,757	90	P/B multiple
Total			87,705	650	

Source: Company data, Credit Suisse estimates

Dilip Buildcon Ltd (DIBL.BO / DBL IN)

Price (29 Jun 2017): **Rs438.20**; Rating: **OUTPERFORM**; Target Price: **Rs650.00**; Analyst: **Vaibhav Jain**

Income Statement (Rs mn)	03/17A	03/18E	03/19E	03/20E
Sales revenue	50,976	54,778	69,347	77,611
Cost of goods sold	38,954	42,398	53,674	60,071
EBITDA	9,923	10,124	12,817	14,344
EBIT	7,649	7,472	10,023	11,419
Net interest expense/(inc.)	4,162	4,104	4,208	3,996
Recurring PBT	3,601	3,505	5,948	7,507
Profit after tax	3,610	3,154	4,759	5,781
Reported net profit	3,610	3,154	4,759	5,781
Net profit (Credit Suisse)	3,610	3,154	4,759	5,781
Balance Sheet (Rs mn)	03/17A	03/18E	03/19E	03/20E
Cash & cash equivalents	1,137	2,751	1,064	1,333
Current receivables	10,165	9,312	11,095	11,642
Inventories	16,639	17,879	22,635	25,332
Other current assets	17,027	18,077	22,884	25,612
Current assets	44,968	48,019	57,679	63,919
Property, plant & equip.	16,785	16,133	15,340	14,414
Investments	4,695	8,749	12,757	13,620
Intangibles	40	40	40	40
Other non-current assets	0	0	0	0
Total assets	66,488	72,942	85,815	91,993
Current liabilities	22,144	23,607	29,886	33,448
Total liabilities	47,959	51,423	59,701	60,263
Shareholders' equity	18,529	21,519	26,114	31,730
Minority interests	0	0	0	0
Total liabilities & equity	66,488	72,942	85,815	91,993
Cash Flow (Rs mn)	03/17A	03/18E	03/19E	03/20E
EBIT	7,649	7,472	10,023	11,419
Net interest	4,162	4,104	4,208	3,996
Tax paid	9	(350)	(1,190)	(1,727)
Working capital	(2,848)	26	(5,068)	(2,409)
Other cash & non-cash items	2,274	2,652	2,794	2,925
Operating cash flow	11,245	13,904	10,768	14,204
Capex	(4,895)	(2,000)	(2,000)	(2,000)
Free cash flow to the firm	6,351	11,904	8,768	12,204
Investing cash flow	(6,692)	(6,054)	(6,007)	(2,864)
Equity raised	4,085	0	0	0
Dividends paid	(164)	(164)	(164)	(164)
Financing cash flow	(324)	(2,268)	(2,373)	(7,160)
Total cash flow	4,230	5,582	2,388	4,180
Adjustments	0	0	0	0
Net change in cash	4,230	5,582	2,388	4,180
Per share	03/17A	03/18E	03/19E	03/20E
Shares (wt'd avg.) (mn)	137	137	137	137
EPS (Credit Suisse) (Rs)	26.39	23.06	34.79	42.26
DPS (Rs)	136.77	136.77	136.77	136.77
Operating CFPS (Rs)	82.22	101.66	78.73	103.85
Earnings	03/17A	03/18E	03/19E	03/20E
Growth (%)				
Sales revenue	24.8	7.5	26.6	11.9
EBIT	24.2	(2.3)	34.1	13.9
EPS	40.6	(12.6)	50.9	21.5
Margins (%)				
EBITDA	19.5	18.5	18.5	18.5
EBIT	15.0	13.6	14.5	14.7
Valuation (x)	03/17A	03/18E	03/19E	03/20E
P/E	16.6	19.0	12.6	10.4
P/B	3.23	2.79	2.30	1.89
Dividend yield (%)	31.2	31.2	31.2	31.2
EV/sales	1.6	1.5	1.3	1.1
EV/EBITDA	8.5	8.3	6.9	5.9
EV/EBIT	11.0	11.3	8.8	7.4
ROE analysis (%)	03/17A	03/18E	03/19E	03/20E
ROE	24.5	15.8	20.0	20.0
ROIC	19.8	15.2	16.0	15.9
Credit ratios	03/17A	03/18E	03/19E	03/20E
Net debt/equity (%)	129.1	112.9	107.2	77.9
Net debt/EBITDA (x)	2.41	2.40	2.18	1.72

Source: Company data, Thomson Reuters, Credit Suisse estimates

Company Background

Dilip Buildcon is a construction company with focus on the road sector. The company provides EPC services and also develops assets on its balance sheet (BOT, HAM projects).

Blue/Grey Sky Scenario



Our Blue Sky Scenario (Rs) 750.00

Our blue sky scenario of Rs750 assumes higher-than-expected order inflows and execution will lead to higher-than-expected earnings.

Our Grey Sky Scenario (Rs) 410.00

Our grey sky scenario of Rs410 assumes lower-than-expected order inflows and execution will lead to lower-than-expected earnings.

Share price performance



The price relative chart measures performance against the S&P BSE SENSEX IDX which closed at 30,857.52 on 29-Jun-2017

On 29-Jun-2017 the spot exchange rate was Rs64.66/US\$1

Differentiated vertically integrated model

DBL is a pan-India road-focused (+80% of backlog) EPC company undertaking all aspects of construction (including equipment ownership), without relying on subcontractors, unlike most peers. Strong execution and an integrated model have helped the company grow (50% CAGR over FY11-17), earn higher margins and deliver projects ahead of schedule. The company has been able to move away from its dependence on Madhya Pradesh and is diversifying from roads with early wins in contract mining. The company has emerged as a strong player in hybrid contracts and is aiming to churn its existing investment in road development contracts. Strong margins, appropriate leverage and modest, well-managed investment in development contracts help the company earn strong ~20% ROE.

BOT/hybrid strategy: Ready for churn

The company has emerged as a large player in the hybrid annuity segment necessitating equity investments in six incremental projects of c.Rs8 bn. DBL has taken Shrem Infrastructure as a partner in one of the projects and can replicate this strategy in others to limit its direct equity investment in hybrid projects. DBL is also working towards selling a stake in its BOT portfolio (Rs6.5 bn deployed so far), which could counteract its equity commitment in six hybrid contracts, help it churn capital and make the balance sheet more efficient. The company currently has 14 operational and ten under-construction projects. The majority of these projects are based on either an annuity or hybrid annuity model.

~17% earnings CAGR with strong return ratios

We expect the company to register 17% earnings CAGR during FY17-20 due to (1) execution of backlog worth Rs175 bn, and (2) PBT margin expansion with flattish EBITDA margin on falling interest costs. We believe that the company will clock a 15% CAGR during FY17-20 and will have PBT CAGR of 28%. The higher PBT CAGR is driven by a lower proportion of interest and depreciation compared to revenues. We expect interest cost to stay flat as interest rates fall, based on (1) the lagged impact of a lower MCLR (marginal corporate lending rate) and (2) incremental possibilities of borrowing through cheaper instruments like commercial paper (working capital) and debentures (term loans). A part of this high pre-tax profit growth is negated by likely tax rate increases. The company has enjoyed tax advantages on investments in machinery (expiring post FY18) and road development (80-IA). We build tax incentives on hybrid contracts to continue and build an average 20% effective tax rate in FY18-20E versus ~nil in FY17. We expect 18% ROE during FY17-20. The company has low fixed asset turnover ratio of about 3x as well as working capital turnover ratio (2.4x); however, high margins and adequate leverage of about 1.3x ensure a reasonably strong RoE of ~18%.

Initiate with OUTPERFORM; TP of Rs650

Our target price of Rs650 is based on 18x FY19E earnings and 1x book for BOT investment. The P/E multiple of 18x is based on (1) 20% earnings CAGR, (2) sector opportunity and (3) focused execution and differentiated position. Our channel check on its peers, and equipment suppliers among others looked very positive.

Risks relate to (1) delay in the start of recent project wins—the company has about Rs50-60 bn of backlog that is yet to start construction (we note that Lucknow-Sultanpur has got the appointed date); (2) less flexibility to deal with downcycle—its integrated model would suffer in case ordering activity is lower in certain years as the company carries higher fixed manpower and equipment costs; (3) promoter's family-driven management and band width constraints—the company has grown exceptionally fast and unless it builds management band width, it may not be able to retain its edge in execution and (4) inability to build other verticals apart from roads as well as higher competition can limit the opportunity basket and affect margins as well.

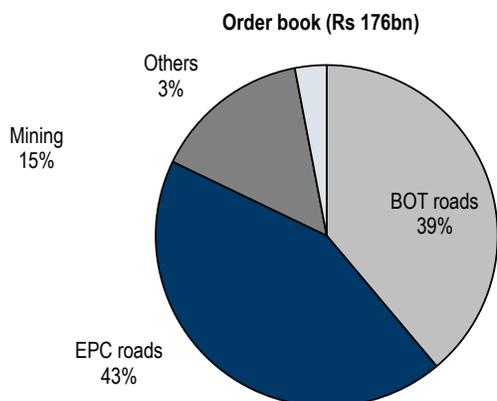
Pan-India, road-focused EPC company

DBL is one of the leading private sector road-focused EPC contractors in India. The company was founded by Mr Dilip Suryavanshi, a first generation entrepreneur, who entered into the construction business (buildings) in 1984 in the state of Madhya Pradesh. Over the years, DBL expanded its area of operations into roads, irrigation and mining. Currently, DBL has a pan-India presence with completed projects in the states of Madhya Pradesh (home state), Gujarat, Himachal Pradesh, Rajasthan and Maharashtra. The company is also working on projects in the states of Tamil Nadu, Punjab, Chhatisgarh, Jharkhand, Haryana, Telangana, Andhra Pradesh, Karnataka, Goa and Uttar Pradesh. In addition to its EPC business, DBL has developed a number of road projects on Build-Operate-Transfer (BOT) basis.

The company has chosen to adopt a vertically integrated model, which has helped it in delivering projects ahead of schedule and earn higher margins, even though it entailed higher investment in construction equipment, unlike its peers which subcontract part of the work.

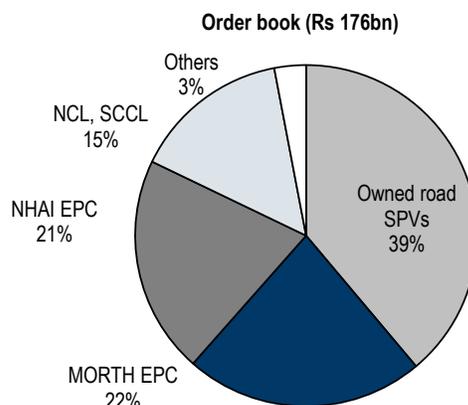
The current order backlog of the company has 80% dependence on the road sector. Of its total order book, 40% of orders have been secured from owned road special purpose vehicles (SPVs), which are developing road projects on toll/annuity basis. Another 43% of orders have been secured from the central government road agencies, i.e., NHAI and MORTH. The strong client profile, where funding and clearances issues are largely addressed, is a positive and implies a healthy order backlog, where execution timelines should not get impacted.

Figure 38: Order book is strong at Rs175 bn with roads accounting for +80% of orders



Source: Company data, Credit Suisse research

Figure 39: Owned projects and central government agencies account for 97% of order book



Source: Company data, Credit Suisse research

Mining segment: New business segment which can scale up

DBL has recently secured projects in the mining segment, where it has taken up Mine Development and Operation (MDO) and Over burden (OB) removal contracts from leading mining companies like Northern Coalfields, Singareni Collieries and DVC. Given the government's thrust on growing indigenous coal production (and reducing coal imports) and efforts to encourage captive mining, this business segment can scale up further in coming years. At end-FY17, the company had an order backlog of Rs26 bn from the mining segment.

Figure 40: DBL secured over Rs110 bn worth projects in the past eight months

Date	Client	Order type	Amount (Rs mn)	Description
Road EPC				
24-Apr-2017	AAI	EPC	1,250	Construction of parallel taxi track and associated civil works at Dabolim Airport
30-Mar-2017	NHAI	EPC	5,031	Four laning of Nalagampalli to AP/KN border (48km)
28-Mar-2017	MoRTH	EPC	2,925	Two laning of Kalamb to Wadki
28-Mar-2017	MoRTH	EPC	2,880	Two laning of Mantha Taluka border to Barshi
19-Nov-2016	MoRTH	EPC	1,980	Two laning of Rayachoti - Kadapa (NH 18)
7-Sep-2016	MoRTH	EPC	3,500	Two laning of Eeppurpalem - Ongole section of NH 216
1-Sep-2016	NHAI	EPC	6,131	Four laning of Chichra to Kharagpur
Road HAM				
30-Mar-2017	NHAI	HAM	9,865	Four laning of Mahagaon to Yavatmal section of NH 361 (Package II)
30-Mar-2017	NHAI	HAM	8,868	Four laning of Yavatmal to Wardha section of NH 361 (Package III)
30-Mar-2017	NHAI	HAM	9,057	Four laning of Wardha-Butibori section of NH 361 under NH(O)
18-Feb-2017	NHAI	HAM	7,744	Four laning of Tuljapur-Ausa section of NH 361
2-Nov-2016	NHAI	HAM	7,769	Four laning of Kalmath - Zarap
10-Sep-2016	NHAI	HAM	17,136	Four laning of Lucknow - Sultanpur
Mining projects				
24-Mar-2017	DVC	MDO	Not mentioned	Mining contract of Tubed block (130MT - 29 years - peak cap of 6MT) at R s837/MT
20-Jan-2017	Northern Coalfields	MDO	16,736	Excavation of OB and rehandling of mechanical systems at Nigahi coal mines
9-Sep-2016	Singareni Collieries	OB removal	9,736	1066 LBCM of OB including coal

OB – Over burden removal.

Source: Company data, Credit Suisse estimates

Hands-on promoters with civil engineering & management background

Mr Dilip Suryavanshi, Chairman and Managing Director

DBL was set up in 2006 by Mr Dilip Suryavanshi (Chairman and Managing Director), who has been in the construction business since 1984. He holds a bachelor's degree in civil engineering from the University of Jabalpur. He has over 33 years of experience in the business of construction. As CMD of the company, he liaises with various government departments and also overlooks processes including tendering, bidding and planning the projects.

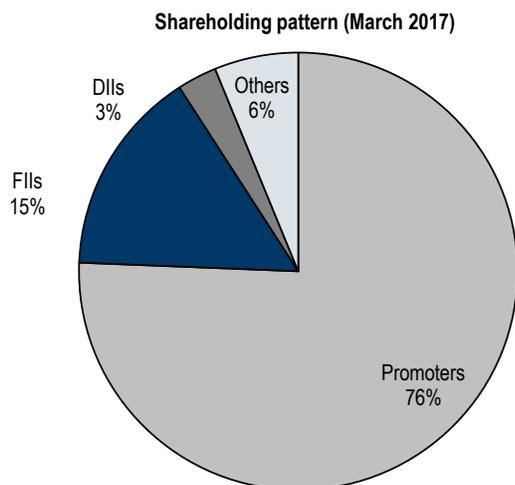
Mr Devendra Jain, Executive Director and CEO

Mr Devendra Jain is an Executive Director, and CEO of DBL. He holds a bachelor's degree in civil engineering from Vikram University, Ujjain. He has over 18 years of experience in the business of construction. He looks after project implementation along with the quality of work and ensures timely completion of the projects.

Mr Rohan Suryavanshi, Head – Strategy and Planning

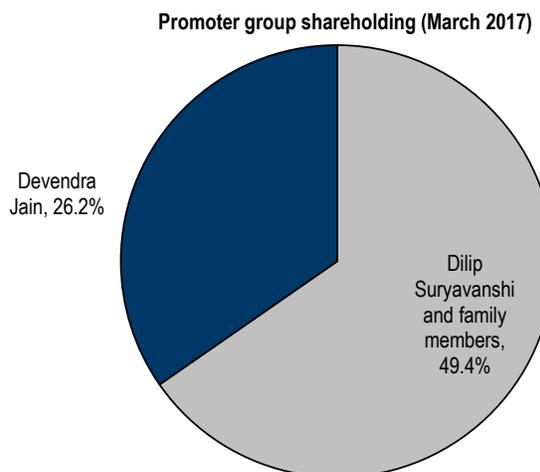
Mr Rohan Suryavanshi, 30 years, is the Head – Strategy and Planning. He handles the Investor Relations function as well for the company. He holds a bachelor's degree in commerce from the University of Pune and a master's degree in business administration from The Wharton School, University of Pennsylvania. He has a total work experience of three years. He is responsible for business strategy and planning, financial planning and streamlining existing business processes and implementing enterprise resource planning (ERP).

Figure 41: Promoters hold a 76% stake



Source: Company data, Credit Suisse research

Figure 42: Mr Suryavanshi has a 49% stake and Mr Jain holds 26%



Source: Company data, Credit Suisse estimates

Early completion bonus indicates strong execution capabilities

DBL has been executing projects ahead of schedule and had earned early completion bonus of Rs1.9 bn from 11 BOT projects and Rs286 mn from ten public sector funded EPC projects till March 2016. The company has also earned early completion bonuses in the recent past amounting to Rs758 mn.

Figure 43: Recently completed projects done 100-400 days ahead of schedule

Project	Order type	Order size (Rs mn)	Early completion (days)	Length (km)	Expected bonus (Rs mn)
Adoni to Madhavaram via Mantralayam Section	EPC	NA	102	55.2	49
Patan-Tendukheda-Rehli road	DBFOT	2,613	374	86.6	362
Jabalpur-Mandla-Chilpi section of NH12A	EPC	2,011	100	21.9	60
Jabalpur-Patan-Shahpura	EPC	900	190	38.8	27
Hata-Fatehpur-Rajpura-Darguwan	DBFOT	1,011	400	64.2	154
Mandla-Pindrai and Salimnabad-Vilayatkalani	EPC	1,908	185		57
Badnagar-Unhel and Sundarabad-Kachrod	EPC	1,620	150	95.1	49
Total					758

Note: These projects were completed over Feb-Mar 2017. DBFOT = Design, Build, Finance, Operate, Transfer
Source: Company data.

BOT projects: Focus on annuities, capital churn

DBL has been quite selective in taking BOT projects on its balance sheet given the traffic risk associated with the projects. In some cases, the company has opted for annuity based contracts, which offer a fixed revenue stream. In other cases, the company has taken up projects where revenue stream is a combination of annuity and toll based revenues, thus reducing exposure to traffic risk. Recently, the company secured six projects from NHAI, which were offered on the Hybrid Annuity model (HAM). Thus, the company has opted to take on project execution risk (which can be managed based on internal capabilities) as compared to traffic risk (which is dependent on external factors).

Currently, the company has 14 operational projects and ten under-construction projects. On operational assets, annual revenues are in excess of Rs2.5 bn on project cost of

~Rs19 bn. In terms of exposure on under-construction projects, only one project is on toll basis, which amounts to 8% of total project cost of under-construction projects.

Figure 44: BOT exposure tilted towards annuity/hybrid annuity projects (low exposure to traffic risk)

Project	Type	Project awarding agency	Annual annuity (Rs mn)	Concession period (yrs)	Project cost (Rs mn)	Length (km)
Operational projects						
Nadiad-Modasa	Annuity	R & BD GOG	349	14	2,081	108
Bankhlafatta-Dogawa	Annuity	MPRDC	198	15	1,158	65
Jaora-Piploda	Annuity	MPRDC	241	15	1,344	88
Mandsaur-Sitamau	Toll	MPRDC	-	25	349	44
Sardarpur-Badnawar	Annuity plus toll	MPRDC	94	15	977	43
Silwani-Sultanganj	Annuity plus toll	MPRDC	190	15	1,287	76
Sitamau-Suwasara	Annuity plus toll	MPRDC	74	15	604	35
Mundi-Sanawad	Annuity plus toll	MPRDC	166	15	1,410	68
Uchera-Nagod	Annuity plus toll	MPRDC	169	15	1,140	56
Ashoknagar-Vidisha	Annuity plus toll	MPRDC	101	15	847	36
Tikamgarh Jatara- Palera Nowgaon	Annuity plus toll	MPRDC	178	15	1,300	76
Betul Sami Junnardeo-Parasia	Annuity plus toll	MPRDC	310	15	3,216	124
Hata Fatehpur	Annuity plus toll	MPRDC	140	15	871	64
Patan-Tendukeda-Rehli	Annuity plus toll	MPRDC	353	15	2,250	87
Sub-total			2,563		18,835	970
Under-construction projects						
Guna - Biora	Toll	NHAI	Nil	26	7,150	94
Mundargi - Hadagali – Harapanahalli	Annuity	KRDC	355	10	1,571	54
Hassan - Ramanathapura - Periyapatna	Annuity	KRDC	526	10	2,204	74
Hirekerur – Ranibennur	Annuity	KRDC	392	10	1,742	58
Mahagaon to Yavatmal	HAM	NHAI	NA	17.5	9,865	80
Yavatmal to Wardha	HAM	NHAI	NA	17.5	8,868	65
Wardha-Butibori	HAM	NHAI	NA	17.5	9,057	59
Tuljapur-Ausa	HAM	NHAI	NA		7,744	67
Kalmath - Zarap	HAM	NHAI	NA		7,769	44
Lucknow - Sultanpur	HAM	NHAI	NA		17,136	123
Sub-total					73,106	
Total					91,941	

HAM – Hybrid Annuity Model. KRDC - Karnataka Road Development Corporation Ltd. MPRDC – Madhya Pradesh Road Development Corporation
Source: Company, Credit Suisse research

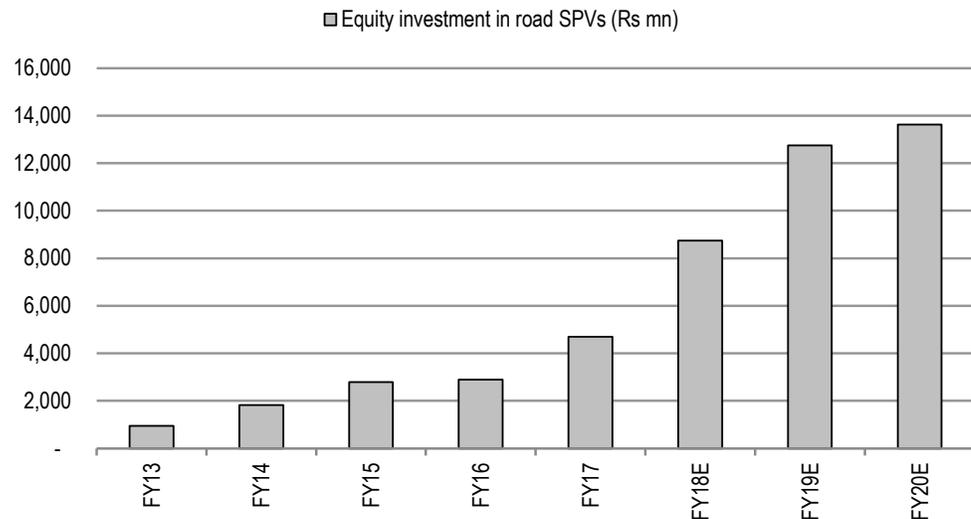
Exploring partnership model to limit equity commitment to BOT projects

In order to limit DBL's equity commitment to road assets, DBL is looking at selling a stake in its operational projects to a strategic partner. The proposed sale could be for a minority stake in the BOT portfolio. This sale will help release capital from operational projects, which can then be used for investment in new HAM projects, won recently by the company.

Apart from exploring the option of inducting a strategic partner in the entire portfolio, DBL has also entered into a project specific arrangement for Rs9 bn Tuljapur-Ausa HAM project, which was secured by the company in February 2017. DBL has entered into an agreement with Shrem Infra (Mumbai-based financial investor), which has agreed to buy a 49% equity stake in this project, and will buy the remaining 51% stake after completion at a pre-agreed IRR. Such an arrangement provides DBL the option to earn EPC margins on construction contracts, and at the same time, churn equity capital in a short period of time to invest in new projects.

In terms of our forecast, we assume that DBL will be funding the equity required for new projects, and do not build any stake sale/equity infusion from a strategic partner, except for factoring in the transaction with Shrem Infra.

Figure 45: We expect +Rs8 bn incremental equity investment in road SPVs by FY20E

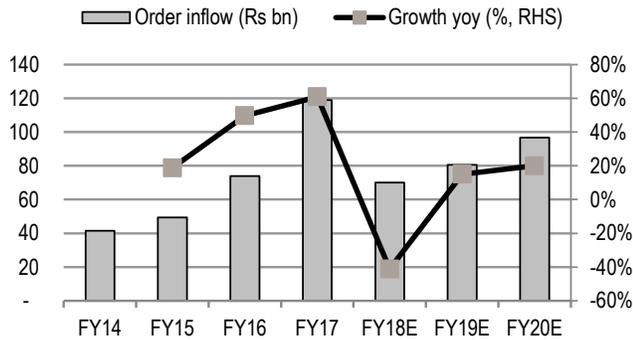


Source: Company data, Credit Suisse estimates

~17% earnings CAGR with strong return ratios

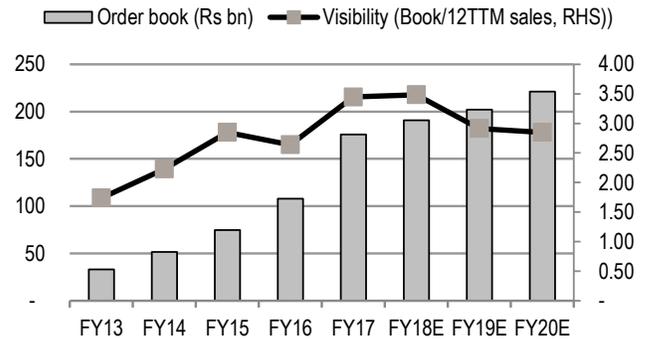
We expect the company to deliver 17% earnings CAGR over FY17-20E on (1) execution of backlog worth Rs175 bn, and (2) PBT margin expansion with flattish EBITDA margin on falling interest costs. We believe that the company will register 15% revenue CAGR during FY17-20; however, PBT CAGR is likely to be higher at ~28%. Higher PBT CAGR is driven by a lower proportion of interest and depreciation compared to revenues. We expect interest cost to stay flat as interest rate falls based on (1) lagged impact of a lower MCLR (marginal corporate lending rate) and (2) incremental possibilities of borrowing through cheaper instruments like commercial paper (working capital) and debentures (term loans). Part of this high pre-tax profit growth is negated by likely tax rate increases. The company has enjoyed tax advantages on investments in machinery (expiring post FY18) and road development (80-IA). We factor in tax incentives on hybrid contracts to continue and build an average 20% effective tax rate over FY18-20E versus ~nil in FY17. We expect 20% ROE during FY17-20. The company has low fixed asset turnover ratio of about 3x as well as working capital turnover ratio (2.4x); however, high margins and adequate leverage of about 1.3x ensure a reasonably strong ROE of ~18%.

Figure 46: Strong inflows in FY17; we build moderation going forward ...



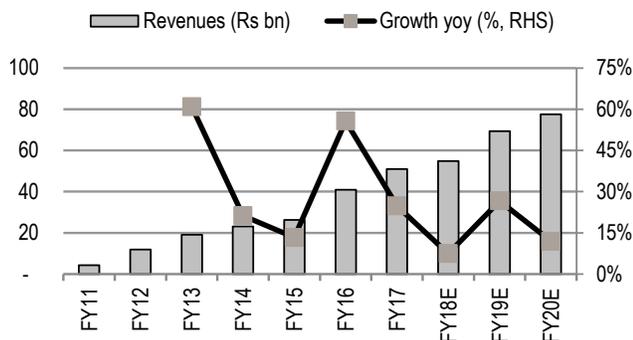
Source: Company data, Credit Suisse estimates

Figure 47: ...order backlog, however, remains healthy and provides strong visibility



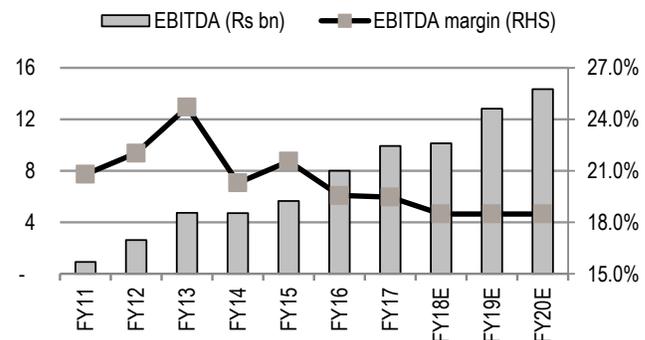
Source: Company data, Credit Suisse estimates

Figure 48: We estimate a revenue CAGR of 15% over FY17-20E



Source: Company data, Credit Suisse estimates

Figure 49: We build lower margins going forward

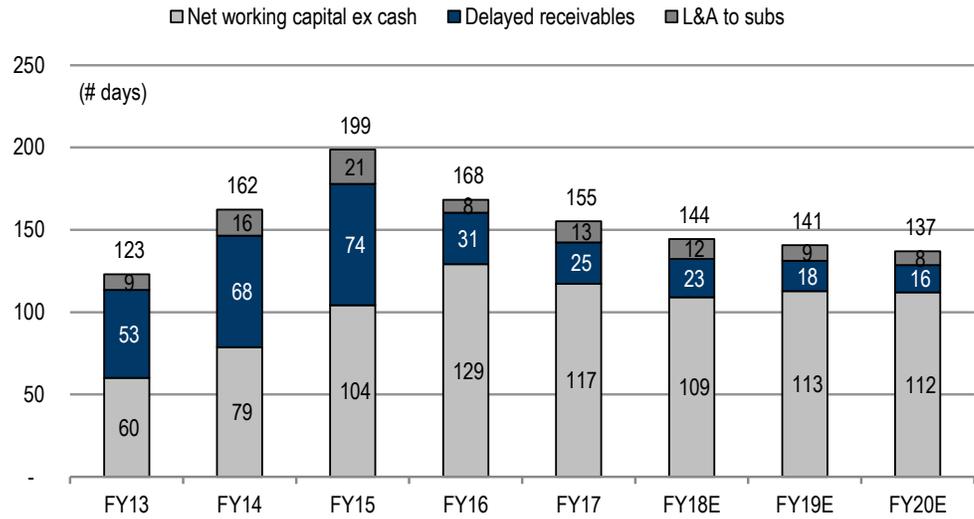


Source: Company data, Credit Suisse estimates

Operating working capital reasonable at 115 days

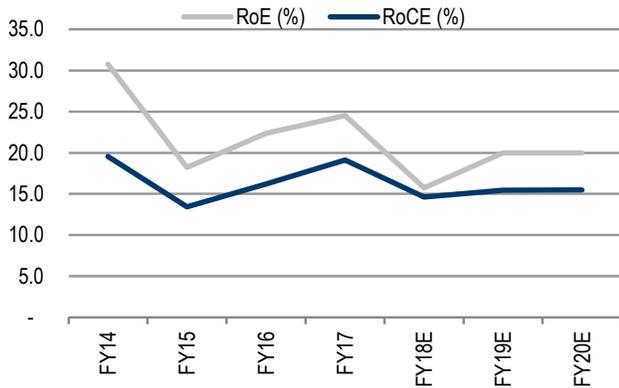
We look at the operating working capital of the company and segregate it into three parts. The first is the normal working capital. The second is delayed receivables from certain private sector clients, and the third is loans and advances to BOT subsidiaries. We note that working capital had risen during FY13 to FY15, as the company moved away from private sector projects to public sector projects with a higher share of projects awarded by central government entities. In terms of stuck receivables, there are two entities namely Essel Group and Topworth Infra which account for ~Rs3.5 bn of receivables. While management highlighted that there was a recovery of Rs1.8 bn in working capital in FY17 and there is expectation of further improvement, we model that these receivables may remain at the same level. On loans and advances to subsidiaries, the company funds part of its equity commitment to subsidiaries in the form of sub-debt. We model this to remain at a similar level in the coming years and assume that the incremental amount of funding in BOT subsidiaries will be in the form of equity investment.

Figure 50: We build a marginal improvement in core working capital (from 117 days in FY17 to 112 days in FY20E)



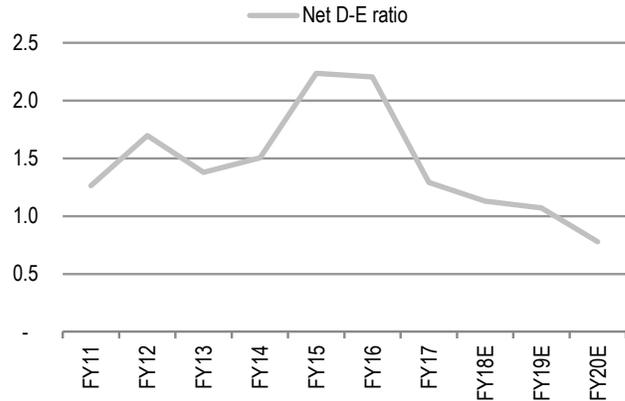
Source: Company data, Credit Suisse estimates

Figure 51: Return ratios are strong...



Source: Company data, Credit Suisse estimates

Figure 52: ...leverage is comfortable as well



Source: Company data, Credit Suisse estimates

Figure 53: Dilip Buildcon—key financials

(Rs mn)	FY11	FY12	FY13	FY14	FY15	FY16	FY17	FY18E	FY19E	FY20E
Profit and loss										
Net sales	4,343	11,872	19,107	23,158	26,241	40,853	50,976	54,778	69,347	77,611
Operational expenses	(3,440)	(9,257)	(14,387)	(18,458)	(20,586)	(32,861)	(41,054)	(44,653)	(56,530)	(63,267)
EBITDA	903	2,615	4,720	4,700	5,655	7,992	9,923	10,124	12,817	14,344
EBITDA margin	20.8	22.0	24.7	20.3	21.6	19.6	19.5	18.5	18.5	18.5
Other income	22	26	25	66	60	154	114	136	134	84
Financial costs	(157)	(572)	(1,048)	(1,551)	(2,587)	(3,805)	(4,162)	(4,104)	(4,208)	(3,996)
Depreciation	(182)	(429)	(709)	(788)	(1,179)	(1,835)	(2,274)	(2,652)	(2,794)	(2,925)
PBT	585	1,640	2,987	2,427	1,949	2,507	3,601	3,505	5,948	7,507
Total tax	(195)	(560)	(478)	(484)	(491)	(308)	9	(350)	(1,190)	(1,727)
Effective tax rate (%)	33.3	34.2	16.0	19.9	25.2	12.3	(0.2)	10.0	20.0	23.0
PAT	390	1,080	2,509	1,943	1,458	2,199	3,610	3,154	4,759	5,780
Balance sheet										
Net worth	1,035	2,855	5,352	7,284	8,730	10,925	18,529	21,519	26,114	31,730
Total debt	1,783	5,773	7,901	11,631	21,870	25,138	25,056	27,056	29,056	26,056
Deferred tax liabilities (net)	54	134	136	268	707	937	759	759	759	759
Total liabilities	2,873	8,762	13,389	19,182	31,307	37,000	44,344	49,334	55,929	58,545
Net fixed assets	2,272	5,334	5,476	6,391	11,890	14,204	16,825	16,173	15,380	14,454
Investments	65	587	952	1,830	2,789	2,898	4,695	8,749	12,757	13,620
Cash and bank balances	476	928	521	668	2,342	1,059	1,137	2,751	1,064	1,333
Net current assets ex-cash	60	1,913	6,440	10,293	14,285	18,839	21,687	21,661	26,728	29,138
Total assets	2,873	8,762	13,389	19,182	31,307	37,000	44,344	49,334	55,929	58,545
Cash flow statement										
CFO		229	(261)	429	1,232	3,285	7,198	9,936	6,693	10,292
CFI		(4,012)	(1,214)	(2,575)	(7,610)	(4,221)	(6,692)	(6,054)	(6,007)	(2,864)
CFF		3,407	1,070	2,167	7,640	(543)	(324)	(2,268)	(2,373)	(7,160)
Total cash flow		(376)	(406)	22	1,261	(1,479)	182	1,614	(1,687)	269

Source: Company data, Credit Suisse estimates

Figure 54: Cash flow from operations was strong in FY17 on improvement in working capital levels; we expect a healthy trend in coming years as well

(Rs mn)	FY12	FY13	FY14	FY15	FY16	FY17	FY18E	FY19E	FY20E
PBT	1,640	2,987	2,427	1,949	2,507	3,601	3,505	5,948	7,507
Depreciation	429	709	788	1,179	1,835	2,274	2,652	2,794	2,925
Interest expenses	572	1,048	1,551	2,587	3,805	4,162	4,104	4,208	3,996
Change in working capital	(1,852)	(4,527)	(3,853)	(3,993)	(4,553)	(2,848)	26	(5,068)	(2,409)
Taxes	(560)	(478)	(484)	(491)	(308)	9	(350)	(1,190)	(1,727)
CFO	229	(261)	429	1,232	3,285	7,198	9,936	6,693	10,292
CFO less interest expenses	(344)	(1,309)	(1,122)	(1,356)	(519)	3,035	5,832	2,485	6,297

Source: Company data, Credit Suisse estimates

Initiate with OUTPERFORM; TP of Rs650

Our target price of Rs650 is based on 18x FY19E earnings and 1x book for BOT investment. The P/E multiple of 18x is based on (1) 20% earnings CAGR; (2) sector opportunity; and (3) a focused execution and differentiated position. Channel checks on peers and equipment suppliers among others look very positive.

Risks relate to: (1) a delay in the start of recent project wins—the company has about Rs50-60 bn of backlog that is yet to start construction (we note that Lucknow-Sultanpur has received the appointed date); (2) less flexibility to deal with a downcycle—an integrated model would suffer in case the ordering activity is lower in certain years, as the company carries higher fixed manpower and equipment costs; (3) the promoter's family-driven management and its band width constraints—the company has grown exceptionally fast and unless it builds its management band width, it may not be able to retain its edge in execution; and (4) an inability to build other verticals apart from roads as well as higher competition could limit the opportunity basket and affect margins as well.

Figure 55: Our SOTP based target price is Rs650

(Rs mn)	Earnings/book	Multiple	Value	Value/share (Rs)	Valuation methodology
Normalised PAT*	4,164	18.0	74,949	560	P/E multiple
Inv. in subs (FY19E)	12,757	1.0	12,757	90	P/B multiple
Total			87,705	650	

* Assuming 30% tax rate.
Source: Company data, Credit Suisse estimates

Key risks

Asset-heavy model implies high fixed costs which is fine if activity remains strong

An asset-heavy model can create issues in periods of low ordering activity. DBL has chosen to keep an asset-heavy model with all work done in-house. In comparison, peers prefer to have a mix of owned equipment and hired equipment, as well as subcontracting some of the work. While this strategy has helped DBL deliver projects well ahead of schedule, it does expose the company to high fixed costs, which can impact margins if ordering activity moderates. Currently, the order backlog is strong and provides strong visibility of revenues in the next few years, and hence this risk is unlikely to play out in the near term. We also note that return ratios have not been impacted on account of this strategy and the company has been generating healthy ROEs.

Execution delays: An inherent risk in all EPC contracts

Execution delays remain the key risk in all large EPC contracts, and can emanate from a number of factors including external (client-side readiness, budget constraints, delay in clearances) and internal (delay in the mobilisation of equipment, slow execution). DBL has tried to address most of these factors by ensuring that projects are secured from large and reputed clients, which do not suffer from funding issues. Around 40% of orders are secured from owned road special purpose vehicles (SPVs). Another 45% of the current order book is secured from central government entities (NHAI, MoRTH), which are well funded. Both NHAI and MoRTH now award projects only after securing all clearances, thus ensuring that projects are not stuck on account of these issues. In terms of internal factors, adequate planning and IT-enabled monitoring of sites helped management in timely monitoring of project execution. The owned resource base also helps it in planning equipment use effectively. In addition, the company tries to follow a cluster approach, which helps in the efficient utilisation of equipment and management band width.

Raw material price risks

The raw material price risk is not significant in the case of EPC contracts as they have price variation clauses, which offset the movement in raw material prices. On contracts from owned SPVs, the price risk lies with the parent company, as these are awarded on a fixed-price basis. The parent company has built in contingencies to offset some increase in raw material prices. However, a sharp price increase can impact EPC business margins. We also note that commodity prices have been stable in the recent past, and hence we do not see any immediate risk from movement in raw material prices.

J Kumar Infra (JKIP.BO / JKIL IN)

Rating	OUTPERFORM
Price (29-Jun-17, Rs)	293.45
Target price (Rs)	375.00
Upside/downside (%)	27.8
Mkt cap (Rs/US\$ mn)	22,204 / 343.42
Enterprise value (Rs mn)	22,215
Number of shares (mn)	75.67
Free float (%)	56.1
52-wk price range (Rs)	314-115
ADTO-6M (US\$ mn)	1.4

Target price is for 12 months.

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INITIATION

Focused play on metro projects

- **Strong execution focus has provided a platform:** J Kumar (JKIL) is a Mumbai-based construction contractor and has excelled (a 30% CAGR from FY07-17) with a focus on Mumbai infrastructure projects and very strong execution. The company is leveraging on this platform to grow beyond Mumbai as well traditional roads, flyover and skywalks. We expect the company to deliver a 20% earnings CAGR between FY17 and 2020E on executing its large backlog.
- **Expanding opportunity basket ahead of time.** JKIL has recently established itself as a metro contractor (large wins in Mumbai/nearing completion of the Delhi Metro contract). It is attempting to diversify into other geographies and sectors (building/roads). It also has a large opportunity basket providing visibility beyond current projects from: (1) projects within Mumbai (Metro ordering, Trans-harbour link, etc.); (2) metros planned in other cities; (3) institutional buildings; and (4) an early foray in roads.
- **Well placed to take upcoming opportunity.** JKIL is a strong beneficiary of the government's focus on building infrastructure. It has low leverage and has had steady margins for the past five years. Given its high working capital, the company would benefit from lower interest rates.
- **OUTPERFORM on ~20% earnings CAGR.** We initiate coverage on JKIL with an OUTPERFORM rating and a target price of Rs375 based on 18x FY19E earnings in line with peers due to: (1) strong growth visibility from executing its backlog; (2) ~20% earnings CAGR over FY17-20E; and (3) a strong long-term opportunity in its key focus areas. **Key risks** include: (1) dependence on four or five large contracts for most of its revenues; (2) diversification from Mumbai-based projects is in early stages; (3) family-driven management with the second generation taking charge now; (4) high competitive intensity in the sector could impact opportunity share and margins; and (5) the escalation of charges of irregularities in contract execution by the Municipal Corp. of Greater Mumbai or any other client can be a risk.

Share price performance



The price relative chart measures performance against the S&P BSE SENSEX IDX which closed at 30,857.52 on 29/06/17. On 29/06/17 the spot exchange rate was Rs64.66/US\$1

Performance	1M	3M	12M
Absolute (%)	-1.8	12.8	31.1
Relative (%)	-0.9	8.7	15.7

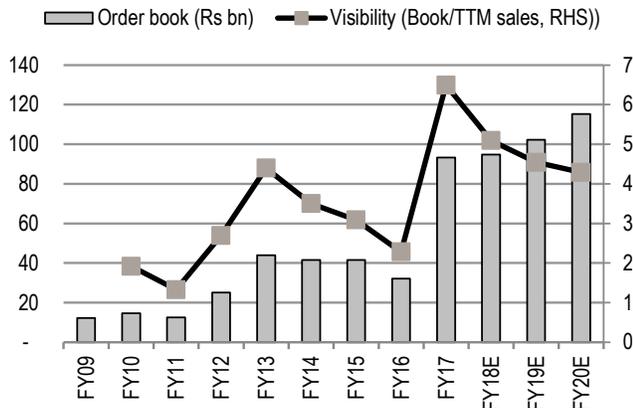
Financial and valuation metrics

Year	3/17A	3/18E	3/19E	3/20E
Revenue (Rs mn)	14,374.9	18,603.0	22,498.1	26,894.8
EBITDA (Rs mn)	2,476.2	3,162.5	3,712.2	4,303.2
EBIT (Rs mn)	1,920.0	2,474.7	2,893.2	3,409.1
Net profit (Rs mn)	1,055.0	1,343.3	1,518.8	1,800.2
EPS (CS adj.) (Rs)	13.94	17.75	20.07	23.79
Change from previous EPS (%)	n.a.	-	-	-
Consensus EPS (Rs)	n.a.	17.72	22.44	-
EPS growth (%)	2.3	27.3	13.1	18.5
P/E (x)	21.0	16.5	14.6	12.3
Dividend yield (%)	0.7	0.7	0.7	0.7
EV/EBITDA (x)	8.7	7.6	6.7	5.8
P/B (x)	1.60	1.48	1.35	1.23
ROE (%)	7.9	9.3	9.7	10.5
Net debt/equity (%)	Net cash	12.6	16.6	14.7

Source: Company data, Thomson Reuters, Credit Suisse estimates

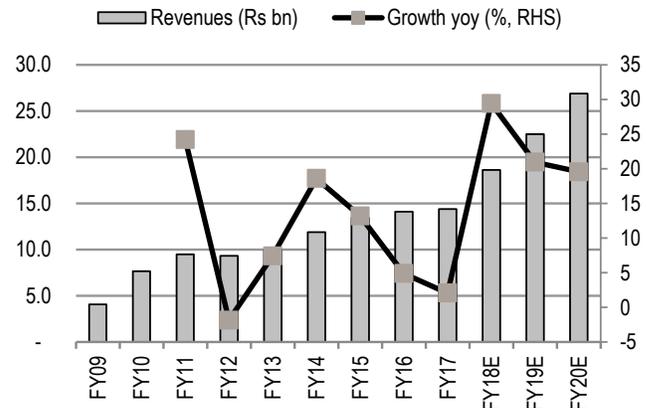
Focus charts

Figure 56: Order backlog of Rs93 bn (+6x FY17 sales) provides strong revenue visibility



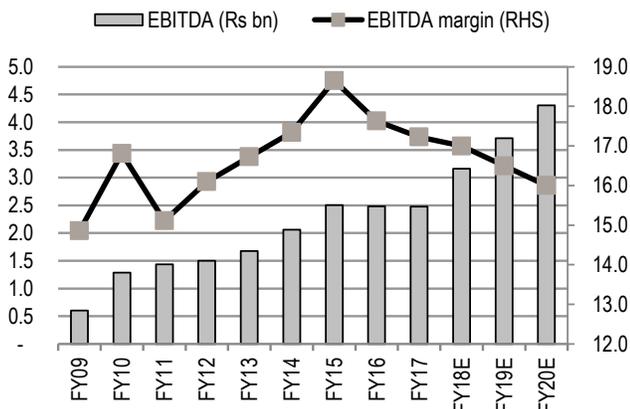
Source: Company data, Credit Suisse estimates

Figure 57: We expect a revenue CAGR of 23% over FY17-20E



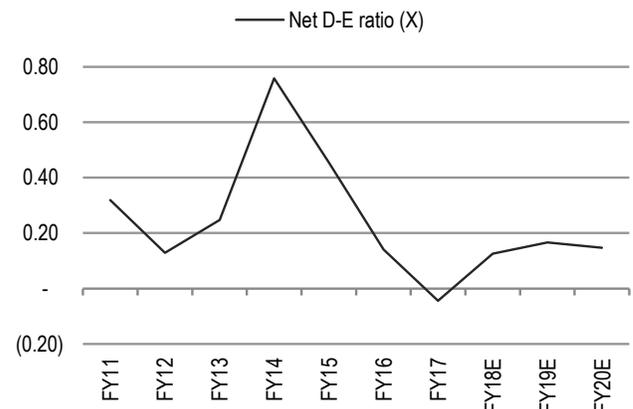
Source: Company data, Credit Suisse estimates

Figure 58: We build moderation into margins versus management guidance of maintenance



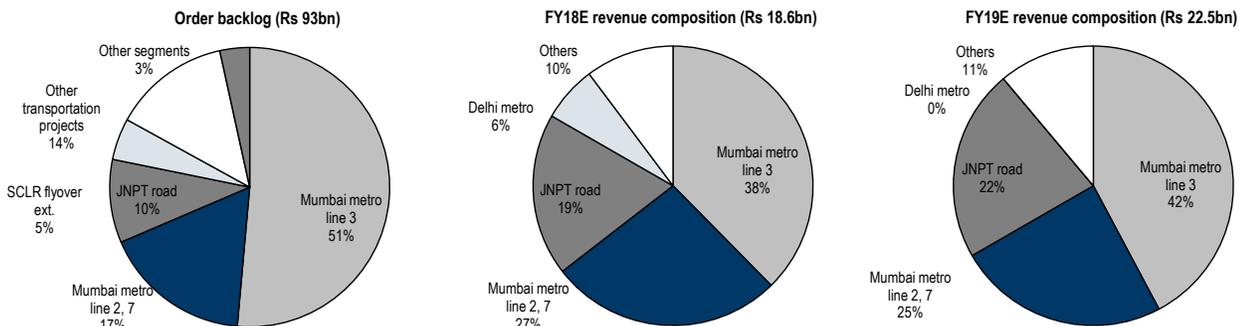
Source: Company data, Credit Suisse estimates

Figure 59: Leverage has remained under control throughout the company's history



Source: Company data, Credit Suisse estimates

Figure 60: Mumbai metro orders to account for the majority of revenues over the next two years



Source: Company data, Credit Suisse estimates

J Kumar Infra (JKIP.BO / JKIL IN)

Price (29 Jun 2017): **Rs293.45**; Rating: **OUTPERFORM**; Target Price: **Rs375.00**; Analyst: **Vaibhav Jain**

Income Statement (Rs mn)	03/17A	03/18E	03/19E	03/20E
Sales revenue	14,375	18,603	22,498	26,895
Cost of goods sold	9,812	12,836	15,524	18,557
EBITDA	2,476	3,163	3,712	4,303
EBIT	1,920	2,475	2,893	3,409
Net interest expense/(inc.)	659	757	885	955
Recurring PBT	1,548	2,005	2,267	2,687
Profit after tax	1,055	1,343	1,519	1,800
Reported net profit	1,055	1,343	1,519	1,800
Net profit (Credit Suisse)	1,055	1,343	1,519	1,800
Balance Sheet (Rs mn)	03/17A	03/18E	03/19E	03/20E
Cash & cash equivalents	4,984	4,177	3,847	4,424
Current receivables	5,233	5,581	6,299	5,379
Inventories	5,619	5,953	7,199	8,606
Other current assets	2,847	3,349	2,250	2,689
Current assets	18,684	19,060	19,596	21,099
Property, plant & equip.	5,113	6,926	7,107	7,213
Investments	3	3	3	3
Intangibles	0	0	0	0
Other non-current assets	2,683	3,131	3,637	4,209
Total assets	26,484	29,119	30,343	32,523
Current liabilities	8,039	7,813	7,199	7,262
Total liabilities	12,594	14,068	13,954	14,516
Shareholders' equity	13,890	15,052	16,389	18,008
Minority interests	0	0	0	0
Total liabilities & equity	26,484	29,119	30,343	32,523
Cash Flow (Rs mn)	03/17A	03/18E	03/19E	03/20E
EBIT	1,920	2,475	2,893	3,409
Net interest	659	757	885	955
Tax paid	(493)	(662)	(748)	(887)
Working capital	404	(1,856)	(1,987)	(1,435)
Other cash & non-cash items	556	688	819	894
Operating cash flow	3,047	1,401	1,862	2,936
Capex	(1,408)	(2,500)	(1,000)	(1,000)
Free cash flow to the firm	1,639	(1,099)	862	1,936
Investing cash flow	386	(2,500)	(1,000)	(1,000)
Equity raised	0	0	0	0
Dividends paid	0	0	0	0
Financing cash flow	830	1,700	500	500
Total cash flow	4,263	601	1,362	2,436
Adjustments	0	0	0	0
Net change in cash	4,263	601	1,362	2,436
Per share	03/17A	03/18E	03/19E	03/20E
Shares (wt'd avg.) (mn)	76	76	76	76
EPS (Credit Suisse) (Rs)	13.94	17.75	20.07	23.79
DPS (Rs)	2.00	2.00	2.00	2.00
Operating CFPS (Rs)	40.26	18.52	24.61	38.80
Earnings	03/17A	03/18E	03/19E	03/20E
Growth (%)				
Sales revenue	2.0	29.4	20.9	19.5
EBIT	(2.6)	28.9	16.9	17.8
EPS	2.3	27.3	13.1	18.5
Margins (%)				
EBITDA	17.2	17.0	16.5	16.0
EBIT	13.4	13.3	12.9	12.7
Valuation (x)	03/17A	03/18E	03/19E	03/20E
P/E	21.0	16.5	14.6	12.3
P/B	1.60	1.48	1.35	1.23
Dividend yield (%)	0.7	0.7	0.7	0.7
EV/sales	1.5	1.3	1.1	0.9
EV/EBITDA	8.7	7.6	6.7	5.8
EV/EBIT	11.2	9.7	8.6	7.3
ROE analysis (%)	03/17A	03/18E	03/19E	03/20E
ROE	7.9	9.3	9.7	10.5
ROIC	9.4	11.0	10.8	11.5
Credit ratios	03/17A	03/18E	03/19E	03/20E
Net debt/equity (%)	(4.4)	12.6	16.6	14.7
Net debt/EBITDA (x)	(0.25)	0.60	0.73	0.61

Source: Company data, Thomson Reuters, Credit Suisse estimates

Company Background
J Kumar Infra is a construction company which provides EPC services in roads, bridges and metro segments. J Kumar is working on large metro packages in Mumbai, which were won against large local and global competitors.

Blue/Grey Sky Scenario



Our Blue Sky Scenario (Rs)	430.00
Our blue sky scenario of Rs430 assumes higher-than-expected order inflows will lead to higher earnings, and higher target price.	

Our Grey Sky Scenario (Rs)	280.00
Our grey sky scenario of Rs280 assumes lower-than-expected order inflows will lead to lower earnings, and lower target price.	

Share price performance



The price relative chart measures performance against the S&P BSE SENSEX IDX which closed at 30,857.52 on 29-Jun-2017
On 29-Jun-2017 the spot exchange rate was Rs64.66/US\$1

Focused play on metro projects

Mumbai based contractor with 30% revenue CAGR over FY07-17; recent wins of Mumbai metro contracts likely to result in 20% PAT CAGR over FY17-20E

J Kumar is a Mumbai-based construction contractor and has excelled (a 30% CAGR over FY07-17) with a focus on Mumbai infrastructure projects and strong execution. The company is leveraging this platform to grow beyond Mumbai as well traditional roads, flyovers and skywalks. It recently won Mumbai Metro contracts and is likely to deliver ~20% earnings CAGR for FY17-20E on execution of its large backlog. We initiate with an OUTPERFORM rating and a target price of Rs375 based on strong earnings growth and opportunity visibility. Management bandwidth and project concentration are key risks.

Well placed with an expanding opportunity

Mumbai Metro expansion, trans harbour link and metro lines in other cities offer large EPC opportunities

The company has recently established itself as a metro contractor with: (1) large wins for the Mumbai Metro in terms of both underground and overground portions; (2) a win for the Ahmedabad metro for an elevated corridor; and (3) near completion of its Delhi Metro contract. JKIL has entered a JV with China Railway Third Group (CRTG) for its metro contracts and has many expat construction experts leading its projects. It is attempting to diversify into other geographies as well as sectors with recent wins in Uttar Pradesh for building and roads works from NHA in the Jawaharlal Nehru Port Terminal (JNPT) area. The company has a large opportunity basket providing visibility beyond current projects from: (1) projects within Mumbai (metro orders for additional lines, the Trans-harbour link, etc.); (2) metros planned in other cities; (3) institutional buildings; and (4) an early foray in roads. Thus, the company can be a strong beneficiary of the government's focus on building infrastructure.

Capital-intensive model, low-leverage diluting ROEs

The company has an order backlog of Rs93 bn based on large metro project wins recently relative to FY17 revenues of just Rs14.4 bn. Our due diligence from visiting sites and meeting the Mumbai Metro Rail Corp (the client for the underground packages) suggests strong execution with first girders already starting to be placed on elevated sections and digging for lowering tunnel boring machines for line-3 packages. JKIL has maintained steady margins of c.17% for the past few years. High margins are partly driven by its integrated model with high fixed assets (turnover ratio of 2.5x) and working capital (150 days of sales) deployment. Recent equity issuance and ensuing low leverage (zero net debt at end-FY17) resulted in RoE dilution to 10%. We expect the RoE to rise on stronger execution. The company has not made any investment in infrastructure development and thus not suffered from a cyclical downturn that has hurt many construction peers.

An OP on strong earnings, reasonable valuations

We expect JKIL's revenue and earnings to see a CAGR of 23% and 20% over FY17-20E on executing its strong order backlog. We initiate coverage with an OUTPERFORM rating and target price of Rs375 based on 18x FY19E earnings in line with peers on the back of: (1) strong growth visibility from executing its order backlog driving a 20% earnings CAGR for FY17-20E; (2) a strong long-term opportunity in its key focus areas; and (3) still reasonable valuations (14.6x FY19E P/E).

Key risks from project concentration and band width

Key risks include: (1) dependence on four or five large contracts for the bulk of its revenues (the Mumbai metro itself contributes about two-thirds of the current backlog and FY18-19E revenues); (2) diversification from Mumbai-based projects is in its early stages and may pose unforeseen risks in terms of execution and margin challenges; (3) family-driven management with the second generation taking charge now may limit bandwidth beyond a particular size; (4) high competitive intensity in the sector can impact opportunity share and margins and (5) escalation of issues with Municipal Corp of Greater Mumbai or any other client can be a risk.

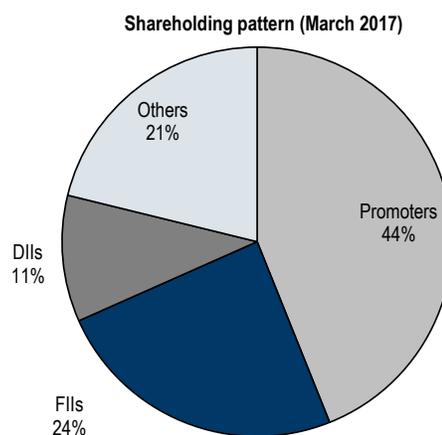
Mumbai niche; exploring more sectors/geographies

J Kumar is a niche play on metro projects' capex. The company, set up in 1980, focused on small roads and flyover projects in Maharashtra. Over the past few years, JKIL expanded its area of operations to metro projects and secured contracts from CIDCO (Navi Mumbai) and Delhi Metro. The most recent projects won by the company include two packages for the Mumbai metro line 3. We expect capex on metro projects to remain strong in the coming years, which should provide adequate growth opportunities for the company. The company has a strong order backlog with book to TTM sales at 6.5x. We expect the company to deliver a 23% revenue CAGR from FY17-20E and believe that the experience of Mumbai metro projects should enable the company to undertake large projects in coming years.

Promoters hold 44% in the company

JKIL was set up by Mr. Jagdishkumar Gupta (Executive Chairman) as a buildings construction firm in 1980. Over the years, the company expanded its area of business to include construction of roads, bridges and flyovers, earthen dams, airport buildings, housing and commercial complexes. While Mr Jagdishkumar Gupta oversees the company's strategy, his sons Mr Kamal Gupta (Managing Director) and Mr Nalin Gupta (Managing Director) handle business development and project execution. Mr. Kamal J. Gupta, 44 years, holds a bachelor's degree in civil engineering. He is associated with the company since 1996. Mr Nalin J. Gupta, 42 years, is a commerce graduate and a member of Indian Institution of Bridge Engineers. He is associated with the company since 1997. Both brothers follow a hands-on approach in managing project execution and have been able to grow the business at a strong pace over the past decade. They have also been successful in diversifying from flyover construction into metro projects, and also expanding area of operations from just Mumbai to now Delhi, Gujarat, Rajasthan and Uttar Pradesh.

Figure 61: Promoters own a 44% stake in the company



Source: Company data, Credit Suisse research

Large metro projects secured in past 12 months provide strong visibility

JKIL has secured ~Rs75 bn of projects in FY17 including Rs50 bn orders from Mumbai metro line 3 across two packages. Mumbai metro line 3 was divided into seven packages of civil works, which were awarded to a consortia led by JKIL (two packages), L&T (two packages), HCC (one), Tata Projects (one) and Soma Enterprises (one). Further, the company also secured over Rs13 bn of work related to the Mumbai metro line 2A project. These projects have provided strong visibility to JKIL's revenues, as the current order backlog is over 6x FY17 revenues.

Figure 62: Projects won by JKIL in the past few years including large metro orders

Date	Project	Client	Amount (Rs mn)
Nov-2016	Mumbai metro line 2A - viaduct and nine stations (from Dahisar to Kamraj Nagar near Malad)	DMRC*	6,809
Nov-2016	Mumbai metro line 2A - viaduct and eight stations (from Charkop to DN Nagar, Andheri)	DMRC*	7,041
Nov-2016	Santacruz Chembur link road extension work	MMRDA	4,492
Jul-2016	Mumbai metro line 3 contract (two packages)	MMRC	50,120
May-2016	Elevated viaduct and six stations on Mumbai metro line 7	MMRDA	3,602
May-2016	Administrative building in UP	UPRRN	2,599
May-2016	Various works including grade separator, reconstruction of Hancock bridges and vehicular bridge	MCGM	1,951
Feb-2016	Six lane bridge across Ulhas creek on Motagaon-Mankoli road	MMRDA	1,338
Oct-2015	Karalphata interchange	NHAI	3,866
Oct-2015	Gavanphata interchange	NHAI	3,504
Jul-2015	Various works including cement concrete road in western suburbs of Mumbai and flyovers in Thane	Various	2,806
May-2015	Various works including asphalt roads in western suburbs of Mumbai	MCGM, others	927
Apr-2015	Various works including flyovers, underpasses in Thane and road improvement works in Mumbai suburbs	MCGM	3,673
Feb-2015	Elevated viaduct from Vastral Gam to Apparel park in Ahmedabad	MEGA	2,781
Feb-2015	Pre-cast Arch bridges (3) in Navi Mumbai	CIDCO	753
Nov-2014	Various works including Thane Kalwa bridge, BKC-Eastern express highway elevated corridor and others	Various	2,938

* DMRC is acting as nodal authority for award of line 7 projects. UPRRN - Uttar Pradesh Rajkiya Nirman Nigam
 Source: Company data, Credit Suisse research

Metro projects: A long-term opportunity

While large cities the world over have seen investment in metro projects, India has seen the development of metro projects only in the past two decades. The first city to invest in metro projects was Delhi, where construction of the first phase started in 1998 and the first line was commissioned in 2002. Since then, a number of cities have commissioned metro projects including Mumbai, Bengaluru, Chennai and Jaipur. In addition, large metro projects are under development in various cities including Hyderabad, Ahmedabad, Lucknow, Nagpur, Pune and Kochi.

In August 2014, the central government approved a policy whereby it would provide assistance to cities with populations over 1 mn to develop metro rail projects. Key challenges faced in implementing metro projects relate to land acquisition and high fixed costs.

Figure 63: After Delhi metro's success, projects under way in most large cities

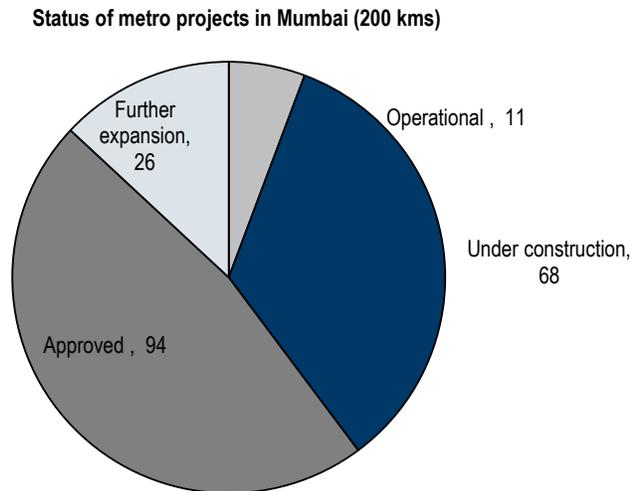
City	State	Population (mn)	Current status
Mumbai	MH	12.5	Few lines under development; more lines to be awarded
Delhi	DL	11.0	Phase I & II completed; Phase III under development; Phase IV approved
Bengaluru	KN	8.4	Couple of lines completed (in phases); remaining under development
Hyderabad	TL	6.8	Under construction via private sector participation (L&T)
Ahmedabad	GJ	5.6	Phase I under development
Chennai	TN	4.7	Phase I in final stages of development; Phase II likely to get approved soon
Kolkata	WB	4.5	Old metro system under operation
Surat	GJ	4.5	Rs120 bn project approved; DPR under preparation
Pune	MH	3.1	Contracts award under progress
Jaipur	RJ	3.1	First phase commissioned; second phase under development
Lucknow	UP	2.8	First phase to be operational in near term; second phase under construction
Kanpur	UP	2.8	Project approved; contracts to be awarded
Nagpur	MH	2.4	Project under construction/Awards under way
Indore	MP	2.0	DPR approved
Thane	MH	1.8	Project announced by state government
Bhopal	MP	1.8	DPR approved
Visakhapatnam	AP	1.7	Approval sought from Central government
Varanasi	UP	1.2	Approved
Kochi	KL	0.6	Under development

Source: Government of India, Credit Suisse research

Metro projects have seen support from all quarters including the public, government as well as judiciary. Recently, the Bombay High Court observed that metro projects provide a solution to traffic and pollution issues while hearing a petition against Mumbai metro line 3 project, filed by certain environmentalist groups. We expect that metro project development will rise further in the country, which should provide long-term growth opportunities for companies in the sector.

Mumbai metro projects

Figure 64: Another 94 km of metro work to be awarded in Mumbai; another 26 km expansion likely, which is under consideration



Source: MMRDA, Credit Suisse research

Figure 65: Rs400 bn worth of projects approved; another ~Rs100 bn proposed

Line	Project	Length (km)	Status	Project cost (Rs bn)	Developer/EPC contractor*
Line 1	Versova – Andheri – Ghatkopar	11.4	Operational	43.2	Reliance Infra led consortium
Line 2A	Dahisar (E) – D.N. Nagar	18.6	Under constn.	64.1	JKIL
Line 3	Colaba – BKC – SEEPZ	33.5	Under constn.	231.4	L&T, JKIL, Tata Proj., HCC, Soma
Line 7	Dahisar (E) – Andheri (E)	16.5	Under constn.	62.1	JKIL, NCC, Simplex
Line 2B	D.N. Nagar – Mankhurd	23.5	Approved	109.9	NA
Line 4	Wadala– Thane – Kasarvadavali	32.3	Approved	145.5	NA
Line 5	Thane – Bhiwandi – Kalyan	24.0	Approved	84.2	NA
Line 6	Lokhandwala – Jogeshwari – Kanjurmarg	14.5	Approved	66.7	NA
Line 9	Dahisar (E) to Mira-Bhayander	13.5	Proposed	NA	NA
Line 10	CSI Airport T-1 to Bandra (E)	NA	Proposed	NA	NA

* In case of line 3, only lead/Indian EPC contractors names mentioned here.
Source: MMRDA, company data, Credit Suisse research

Mumbai Trans Harbour Link: another large potential order

MMRDA is looking to develop the Mumbai Trans Harbour Link, which will connect Mumbai island city to Navi Mumbai. The project stretch will be a 21.8 km long road consisting of ~17 km of bridge across the sea and 5 km of road at the ground level. The project is estimated to cost Rs178 bn, and will be contracted out in three parcels, two including bridge construction and one on the road. JKIL (along with others bidders) has been shortlisted in the technical round for the land parcel.

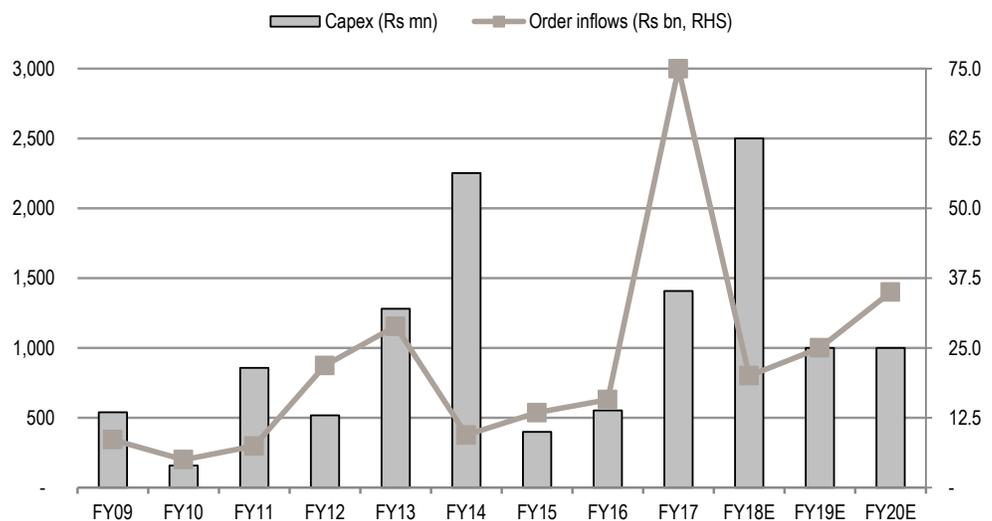
Capital intensive model, low leverage diluting ROEs

The company has a backlog of Rs93 bn based on large metro project wins recently relative to FY17 revenues of just Rs14.4 bn. Our due diligence in terms of visiting sites as well as meeting Mumbai Metro Rail Corporation (client for the underground packages) suggests strong execution with first girders already starting to get placed on elevated sections and digging on for lowering tunnel boring machines for line-3 packages. The company has maintained steady margins at about 17% in the last few years. High margins are partly driven by integrated model with high fixed (turnover ratio of 2.5x) and working capital (2.5x) deployment. The recent equity issuance and ensuing low leverage (zero net debt at FY17-end) has resulted in RoE dilution to 10%. We expect RoE to increase with stronger execution. The company has not made any investment in infrastructure development and thus has not suffered from the cyclical downturn that has hurt many construction peers.

Asset heavy model focused on select segment and states

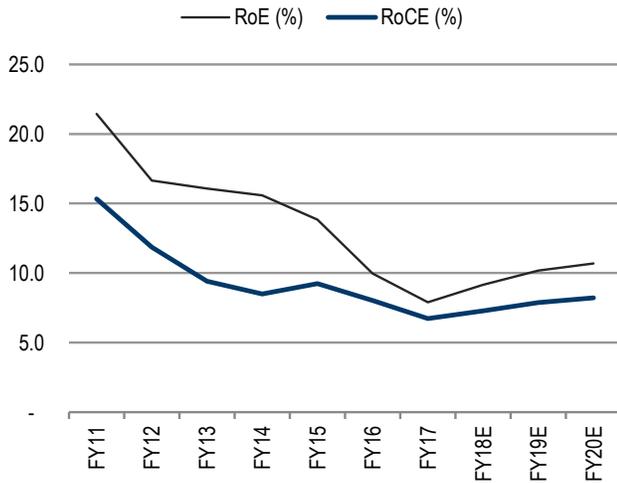
JKIL has adopted an asset heavy model for growth, preferring to own most of the equipment employed in the projects. This has helped the company exercise better control on execution timelines. The company has procured its equipment from leading players in the industry. Management prefers to secure projects in specific states (home state Maharashtra, Delhi, Rajasthan and Gujarat) as it believes that it is well placed to manage execution in these states. In our view, in addition to relationships with local authorities (which is critical in project execution in India), this also helps the company in managing its equipment and management band width efficiently.

Figure 66: Capex has usually picked up post securing large orders



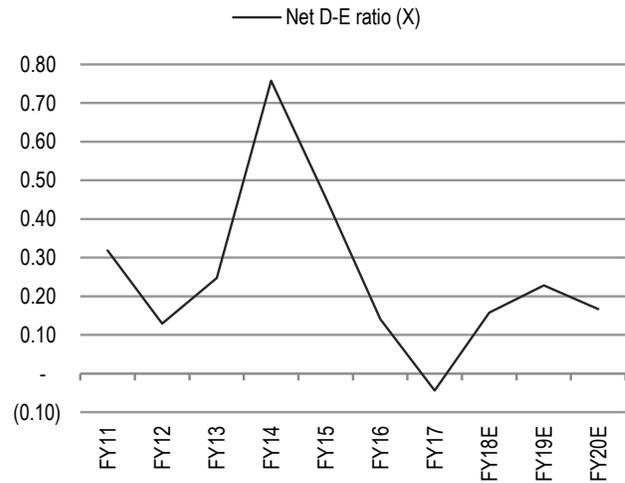
Source: Company data, Credit Suisse estimates

Figure 67: RoEs moderated in recent past post capital raise (Oct-15)



Source: Company data, Credit Suisse estimates

Figure 68: JKIL has maintained leverage at comfortable levels



Source: Company data, Credit Suisse estimates

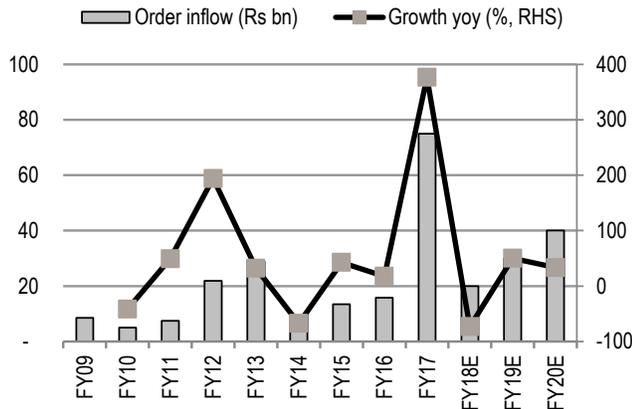
Initiate coverage with **OUTPERFORM** on strong earnings, reasonable valuations

We expect JKIL's revenue and earnings to register a CAGR of 23% and 20% over FY17-20E on the back of execution of its strong backlog. We initiate coverage on the company with an **OUTPERFORM** rating and TP of Rs375 based on 18x FY19E earnings in line with peers on the back of (1) strong growth visibility from execution of backlog driving 20% earnings CAGR between FY17 and FY20E, (2) strong long-term opportunity in its key focus areas and (3) still reasonable valuations (14.6x FY19E P/E).

Order inflows to moderate in FY18; expected to pick up again from FY19

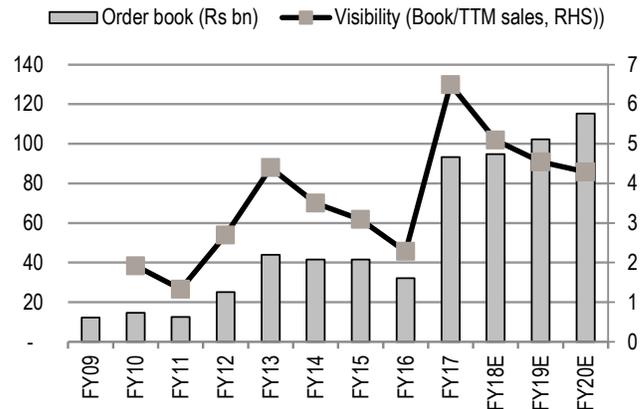
JKIL is currently focusing on the execution of Mumbai metro packages and will be selective in taking up small contracts (flyovers, bridges etc) in the near term. We expect order accretion to pick up again in FY19E as that will help the company build visibility on FY20E revenues. In the interim, the efficient execution of these projects should help the company report healthy growth in revenues.

Figure 69: Order inflows to moderate in FY18 after strong FY17 (large orders of Mumbai metro)



Source: Company data, Credit Suisse estimates

Figure 70: Book provides strong visibility

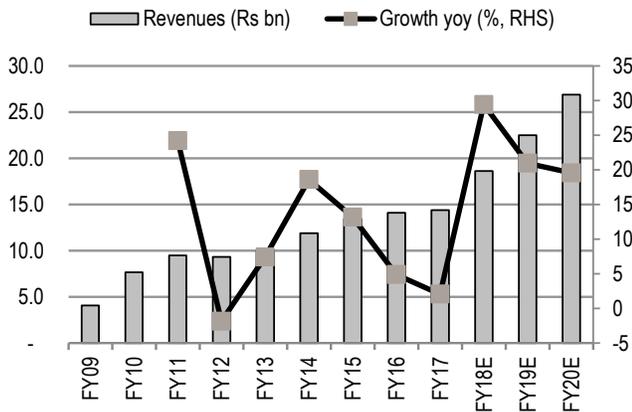


Source: Company data, Credit Suisse estimates

Revenue growth to pick up as execution scales up

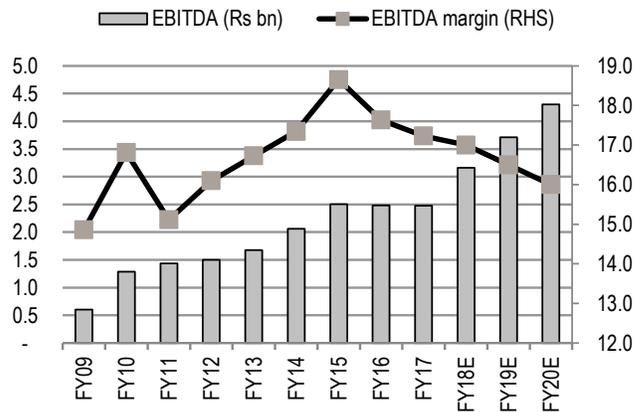
JKIL started work on Mumbai metro projects in 2H FY17. We expect execution to scale up in FY18, as the initial stages of work have been completed. Our site visit to the construction site as well as feedback from discussion with MMRDA suggests that work is picking up. On the margin front, we build some moderation in the future as a large size of work may throw up some unexpected challenges and costs.

Figure 71: Revenue growth likely to be strong on strong backlog



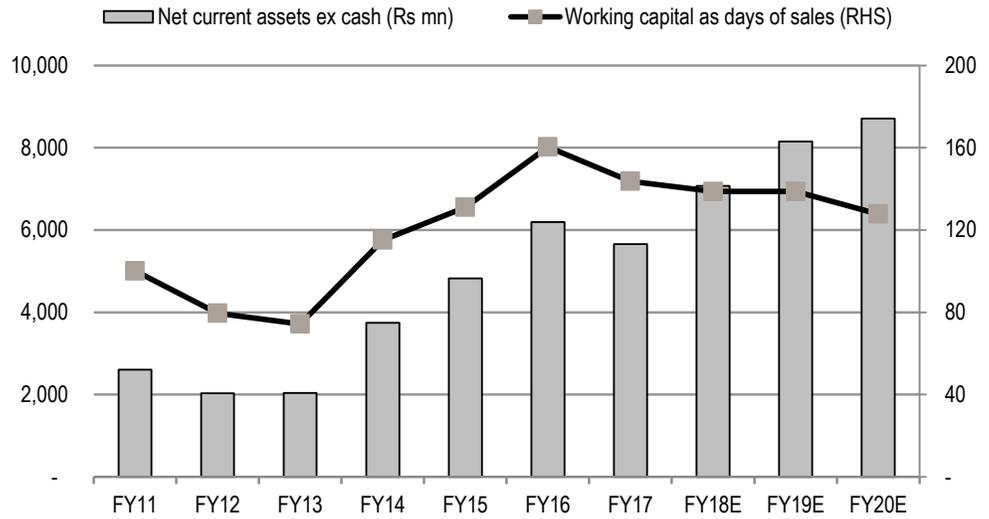
Source: Company data, Credit Suisse estimates

Figure 72: We build moderation in operating margin



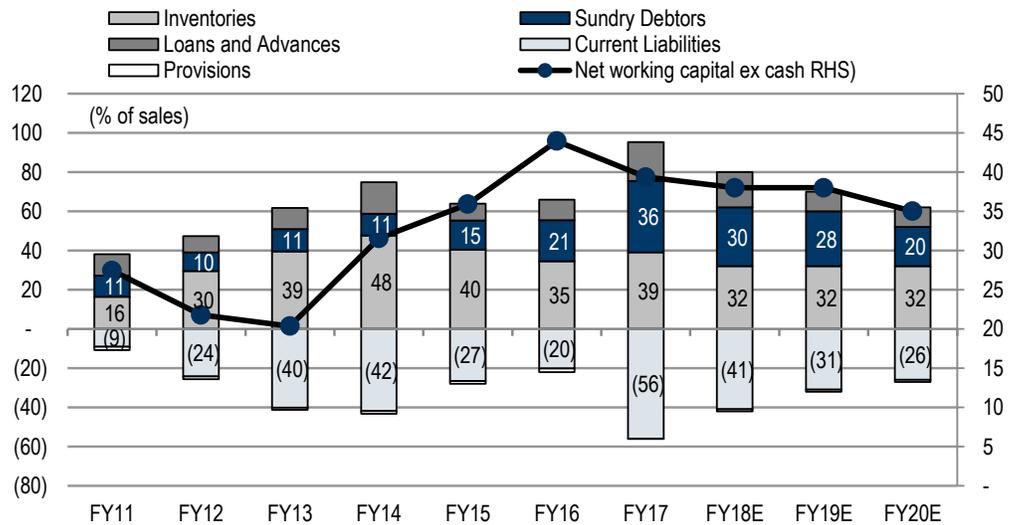
Source: Company data, Credit Suisse estimates

Figure 73: Working capital improved in FY17 as company received mobilisation advances for metro projects, even though debtors/inventories rose



Source: Company data, Credit Suisse estimates

Figure 74: Both current liabilities (mobilisation advances) and debtors likely to moderate in coming years—we build gradual improvement in working capital



Source: Company data, Credit Suisse estimates

Figure 75: We expect revenue/earnings CAGR of 23%/20% over FY17-20E

(Rs mn)	FY11	FY12	FY13	FY14	FY15	FY16	FY17	FY18E	FY19E	FY20E
P&L										
Net sales	9,492	9,316	10,007	11,868	13,432	14,086	14,375	18,603	22,498	26,895
Expenditure	(8,058)	(7,816)	(8,333)	(9,810)	(10,926)	(11,602)	(11,899)	(15,440)	(18,786)	(22,592)
EBITDA	1,434	1,500	1,674	2,058	2,506	2,484	2,476	3,163	3,712	4,303
EBITDA margin (%)	15.1	16.1	16.7	17.3	18.7	17.6	17.2	17.0	16.5	16.0
Other income	71	67	89	108	131	177	287	287	258	233
Interest expenses	(277)	(366)	(406)	(576)	(768)	(611)	(659)	(757)	(885)	(955)
Depreciation	(159)	(189)	(244)	(348)	(474)	(512)	(556)	(688)	(819)	(894)
PBT	1,070	1,012	1,112	1,242	1,395	1,538	1,548	2,005	2,267	2,687
Tax	(331)	(331)	(354)	(402)	(451)	(506)	(493)	(662)	(748)	(887)
PAT	739	681	757	840	944	1,032	1,055	1,343	1,519	1,800
Balance sheet										
Total shareholders' funds	3,782	4,390	5,034	5,753	7,891	12,833	13,890	15,052	16,389	18,008
Total debt	1,674	1,706	2,363	5,572	5,136	3,540	4,370	6,070	6,570	7,070
Deferred tax, other liabilities	40	51	53	77	145	169	184	184	184	184
Total liabilities	5,496	6,147	7,451	11,401	13,172	16,542	18,444	21,306	23,143	25,262
Net fixed assets	1,738	2,066	3,101	5,007	4,933	4,974	5,826	7,638	7,819	7,925
Investments	1	1	1	23	11	1,797	3	3	3	3
Cash and bank	468	1,139	1,119	1,212	1,548	1,736	4,984	4,177	3,847	4,424
Net current assets ex-cash	2,605	2,030	2,037	3,744	4,823	6,191	5,660	7,069	8,549	9,413
Other assets	683	912	1,193	1,414	1,856	1,844	1,971	2,418	2,925	3,496
Total assets	5,496	6,147	7,451	11,401	13,172	16,542	18,444	21,306	23,143	25,262
Cash flow statement										
CFO	(264)	1,583	1,119	(164)	664	799	2,674	932	1,236	2,214
CFI	(858)	(516)	(1,280)	(2,276)	(387)	(2,338)	386	(2,500)	(1,000)	(1,000)
CFF	826	(334)	251	2,632	166	1,907	171	943	(385)	(455)
Cash generated/(utilised)	(297)	733	91	192	443	368	3,231	(625)	(149)	759

Source: Company data, Credit Suisse estimates

Valuation

We rate the stock **OUTPERFORM** on 20% earnings CAGR. We initiate coverage on the company with an **OUTPERFORM** rating and a target price of Rs375 based on 18x FY19E earnings in line with peers on the back of (1) strong growth visibility from execution of backlog, (2) 20% earnings CAGR between FY17 and FY20 and (3) strong long-term opportunity in its key focus areas.

Key risks to our call include (1) dependence on four or five large contracts for the bulk of its revenues, (2) diversification from Mumbai-based projects is in early stages, (3) family-driven management with second generation taking charge now, (4) high competitive intensity in the sector could impact opportunity share and margins and (5) escalation of charges of irregularities in contract execution by Municipal Corp of Greater Mumbai or any other client can be a risk.

Figure 76: Sharp correction in Apr-Aug 2016 period in the wake of BMC issue as market feared impact on existing orders, inflows



Source: Company data, Credit Suisse estimates

Key risks: High project concentration

Project concentration risk on Mumbai Metro line 3 packages

JKIL is working on two packages of the Mumbai metro line 3, which account for ~50% of its total order backlog. If this project was to be impacted on account of any external issue, it could impact revenue and earnings growth for the company. We note that a part of the debt funding is secured from Japan International Cooperation Agency (JICA), which has provided debt funding for multiple infrastructure projects in the country including the Delhi metro and Dedicated Freight Corridor. On risks from opposition by environmental protection agencies, we note that recently the Bombay High Court made statements in support of metro projects, as it provides a practical solution to traffic and pollution issues. Further, both the central and state governments have provided complete support to the project. These factors make us believe that possibilities of delays in the project are less likely.

Concentrated exposure on Mumbai infrastructure contracts

JKIL has concentrated exposure on Mumbai (and adjoining areas) infrastructure projects, with about 80-90% of business in the last three years having been won in Mumbai itself. While this has helped keep up the execution pace given strong oversight, over a period of time the company would have to diversify to other cities and position itself as a broader urban infrastructure player.

Management band width limited with promoters running the company

JKIL continues to be a promoter-driven company with family members taking a hands-on approach in execution of the projects. While this is not a concern in the near to medium term, in our view, over the longer term, the company will need to shift to a more professional management driven approach.

Asset heavy model with most of the equipment owned themselves

JKIL has adopted an asset heavy model approach where it acquires most of the key equipment required in project execution. This helps the company deliver projects on time and within cost. At the same time, it does create a high fixed cost structure, which may not be desirable in a weak cycle scenario. In our view, since India is likely to continue its investment in metro projects, JKIL should be able to grow its business in the medium term and not get impacted due to lack of projects.

Blacklisting by Municipal Corp. of Greater Mumbai can sour business prospects

In March 2017, JKIL was one of the companies, which was blacklisted by the local municipal authority in Mumbai in relation to a road construction order, where BMC alleged that construction quality was not up to the mark. JKIL's management mentioned that BMC, in the past, has not accounted for a large portion of work, and that they continue to bid for projects awarded by other authorities in Mumbai and Maharashtra including MMRDA, MSRDC, MMRC. In our view, if other authorities were to take an adverse view based on MCGM's action, it could impact future business prospects. However, we also note that JKIL is working on large metro projects awarded by MMRC (line 3 orders worth Rs50 bn), and the possibility of any adverse action looks remote.

Appendix I

Owned equipment base provides greater control on execution

JKIL prefers to use its own equipment for execution. Over the years, the company has procured various equipment from leading equipment suppliers. The list below provides details of various construction equipment owned by the company.

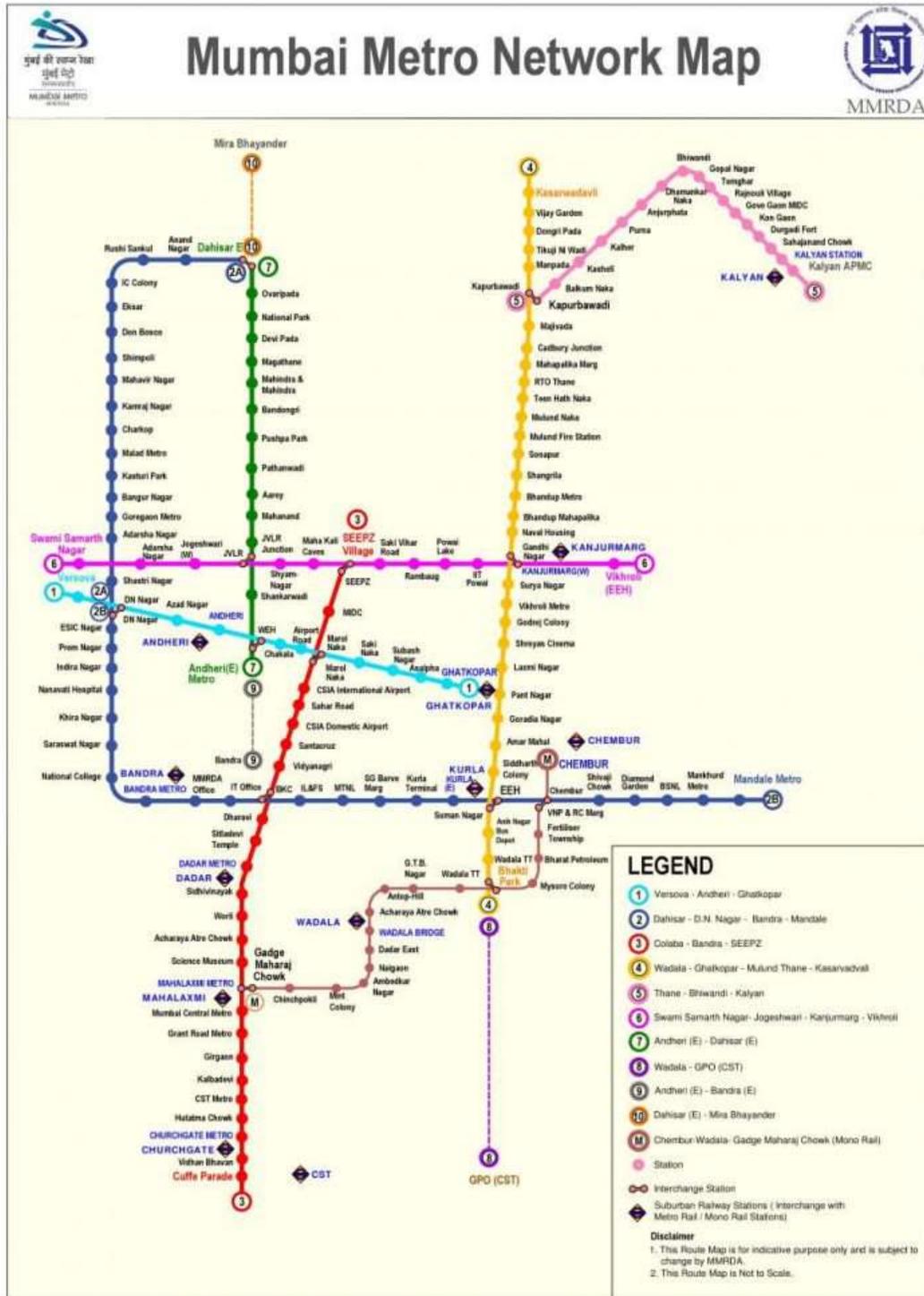
Figure 77: Equipment procured from leading equipment companies

Sr. No.	Type of equipment	No. of units	Kind & make
1	Tunnel Boring Machine	4	Terratec
2	Hydraulic Piling Rig	28	MAIT
3	Poclain/Excavators	19	Tata Hitachi/Komatsu
4	Dumper & Tripper	79	Tata/Ashok Leyland
5	JCB	52	JCB 3D/3DX/4DX
6	Concrete Batching Plant	19	Schwing Stetter
7	Transit Mixers	91	Greaves Cifa/ Schwing Stetter
8	Concrete Pump	18	Schwing Stetter/Putzmeister
9	Air Compressor	2	Atlas Copco
10	Rock Breaker	7	Atlas Copco/Fine 22X
11	Dozer	2	Komatsu/D-6-8-U
12	Vibratory Roller	15	Greaves Bomag
13	Soil Compactor	21	Greaves
14	Roller(static)	10	Kamal & Jessop
15	Gantry Cranes	33	Workshop made
16	Cranes	44	ACE/HYPPO/P&H 220
17	Generator	150	Kirloskar
18	Loader	6	Terex/Escort/JCB
19	Crusher Plant	3	Sandvik
20	Vibro Roller	15	Greaves
21	Boom Placer	5	Putzmeister / Schwing Sretter
22	Earth Compactor	13	Volvo/JCB/Greaves

Source: Company data

Appendix II: Mumbai Metro map

Figure 78: Mumbai Metro network map



Source: MMRDA, Credit Suisse research

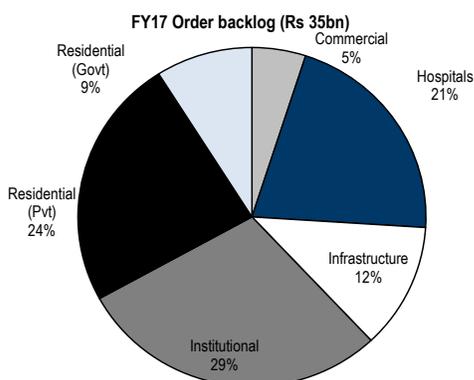
Appendix III: Profile of construction peers

Ahluwalia Contracts

(CMP: Rs327, Market cap: Rs22 bn, 6M ADTO US\$0.3 mn, NOT COVERED)

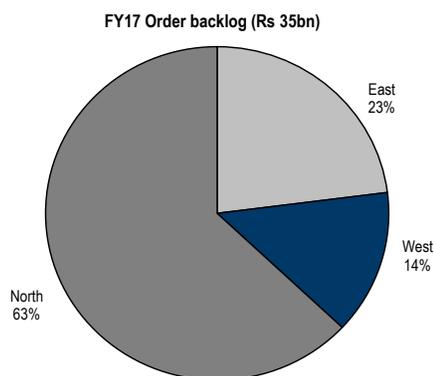
Ahluwalia Contracts (ACL) is an integrated buildings construction company with in-house expertise on design, structural works and electro-mechanical works. Over the past ten years, ACL has expanded its presence from the national capital region to other states as well. ACL has worked for clients such as DMRC, Tata Housing, ITC, Grand Hyatt etc. Over the years, the company has expanded its scope of operations from residential and commercial buildings to hotels, hospitals, institutional buildings and civil works for infrastructure projects (example, metros stations). The company has recovered from its losses in FY12/FY13 and revenues have grown to Rs14.3 bn in FY17 from a bottom in FY14 (though still below previous peak of Rs17 bn in FY11). However, momentum in inflows and backlog has been weak with company’s inflows and backlog being largely flat since end-FY15 at about Rs14 bn/Rs35 bn, respectively.

Figure 79: ACL—niche presence as buildings contractor



Source: Company data

Figure 80: North accounts for ~65% of order book



Source: Company data

Figure 81: Key financials (standalone)

Rs mn	FY14	FY15	FY16	FY17
Revenues	9,603	10,599	12,496	14,265
EBITDA	416	1,148	1,608	1,730
PAT	217	641	854	860
Net worth	2,262	3,377	4,221	5,081
Debt	2,386	1,731	1,419	900
Total liabilities	4,648	5,109	5,641	5,981
Net fixed assets	1,984	1,948	1,966	1,928
NWC, other assets	2,103	2,332	2,730	2,764
Cash	545	765	882	1,225
Investments	15	63	63	63
Total assets	4,648	5,109	5,641	5,981
EBITDA margin	4.3	10.8	12.9	12.1
EPS (Rs)	1.2	9.6	12.6	12.8
RoE (%)	3.5	22.7	22.2	18.5
RoCE (%)	(6.2)	5.5	11.0	11.8

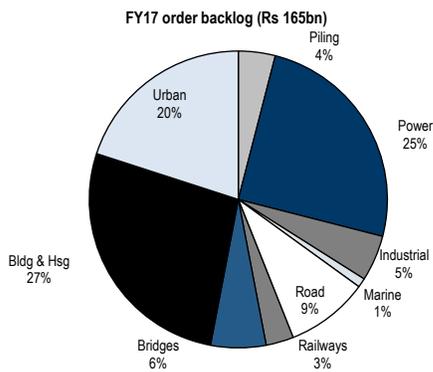
Source: Company data, Credit Suisse research

Simplex Infrastructures

(CMP: Rs506, Market cap: Rs25 bn, 6M ADTO US\$0.3 mn, NOT COVERED)

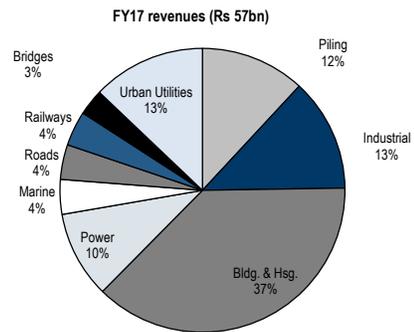
Simplex infrastructure is an old (almost 90 years) pan-India contractor spread across many sectors (buildings, power, industrial, metros and piling) along with modest international exposure (~12-14%). The company has limited presence in the roads vertical and is a pure-play contractor without any asset ownership. Over the last five years it has had flattish revenues with very narrow profitability (<2% net profit; <Rs1 bn PAT) because of high working capital driving interest costs higher. The company's working capital has increased to ~235 days of sales, for the last three years from an average of 110 days of sales between FY07 and FY12. There has been a recovery in profitability in FY17 on better margins. The company owns most of the equipment and thus its fixed asset turnover ratio is lower at about 2x at gross level and 4-5x at the net level. Given high working capital and fixed capital intensity, the company has high leverage of ~2x. The company has a sizeable private sector business contributing about 40% of its total order book.

Figure 82: Well diversified order book



Source: Company data

Figure 83: Buildings account for ~40% of sales



Source: Company data

Figure 84: Key financials

(Rs mn)	Standalone financials				Consolidated financials			
	FY14	FY15	FY16	FY17	FY14	FY15	FY16	FY17
Revenues	55,130	55,816	58,116	56,075	56,154	62,024	58,993	56,125
EBITDA	5,161	5,622	5,666	6,887	5,198	5,819	5,784	7,091
PAT	609	634	662	1,203	588	691	697	1,342
Net worth	13,978	14,422	15,388	15,303	14,339	14,817	15,879	15,324
Minority interests	-	-	-	-	104	61	88	(30)
Debt	29,296	32,253	32,637	32,816	29,306	33,688	32,637	32,816
Other liabilities	2,254	2,095	1,810	1,064	2,259	2,101	1,813	1,084
Total liabilities	45,528	48,770	49,835	49,183	46,008	50,668	50,417	49,194
Net fixed assets	12,169	11,208	11,673	11,845	13,002	12,472	11,804	11,937
NWC, other assets	31,212	35,858	36,495	35,670	30,709	36,395	36,714	35,795
Cash	807	227	142	329	938	334	265	509
Investments	1,341	1,476	1,525	1,339	1,359	1,466	1,633	952
Total assets	45,528	48,770	49,835	49,183	46,008	50,668	50,417	49,194
EBITDA margin	9.4	10.1	9.7	12.3	9.3	9.4	9.8	12.6
EPS (Rs)	12.3	12.8	13.3	24.2	11.8	13.9	14.0	27.0
RoE (%)	4.5	4.5	4.4	7.8	4.3	4.7	4.5	8.6
RoCE (%)	6.2	6.0	6.0	8.7	5.9	5.8	5.6	8.9

Source: Company data, Credit Suisse research

NCC Ltd.

(CMP: Rs90, Market cap: Rs50 bn, 6M ADTO US\$7 mn, NOT COVERED)

NCC has been in the EPC business since 1978, and has presence in buildings, roads, power (civil works), water, railways, irrigation, oil & gas, metals and mining. NCC has flattish revenues in the last three years (revenues declined 6% for the FY17 full year and 13% for the 4Q FY17) as FY15 execution was supported by execution of thermal power plant (its stake in the power plant has been sold to Semb Corp.). FY17 order inflows of Rs95 bn have been supported by Rs18.5 bn order from mining in a JV with BGR Energy group company. Total order backlog excluding this long-term order is about Rs152 bn which is lower than the order backlog at FY15 by 5-6% and flat over end-FY16 backlog. NCC Ltd. does not focus on the roads segment, one of the key segments that has driven growth in peers. Key segments for the company are buildings (42%), water supply (18%), irrigation (11%) and international business in Middle East (5%). The company has significantly scaled down its international business (not bidding incrementally) with backlog down by more than half from Rs22 bn at end-FY16 to Rs9.6 bn at end-FY17.

The company has sold most of the BoT roads and power portfolio and now has just two road projects (1) OB Infra annuity project and (2) Pondicherry-Tindivanam toll project with total exposure at Rs2 bn.

Debt has reduced from ~Rs25 bn at peak to Rs16 bn at end-FY17 implying a debt-equity of 0.5x. This has also reduced finance cost for the company to Rs4 bn in FY17 from Rs5.1 bn in FY16. Loans and advances to group companies have gone down to Rs5.6 bn from Rs11.2 bn at end-FY16. Equity investment in the group business is about Rs10.3 bn. Total exposure to real estate through loans and advances and equity is Rs12 bn, while about Rs4 bn is the exposure to infrastructure development contracts.

Figure 85: Key financials

(Rs mn)	Standalone financials				Consolidated financials			
	FY14	FY15	FY16	FY17	FY14	FY15	FY16	FY17
Revenues	61,173	82,969	83,252	78,921	74,632	95,129	95,835	90,006
EBITDA	4,049	6,493	7,374	6,852	7,570	9,997	10,614	6,697
PAT	43	1,133	2,473	2,616	(330)	554	1,548	1,119
Net worth	25,203	32,044	34,088	34,423	27,634	34,019	35,130	35,180
Minority interests	-	-	-	-	3,705	3,210	2,869	2,869
Debt	24,746	19,951	18,856	15,736	39,145	33,897	35,652	29,682
Other liabilities	125	142	0	0	120	138	0	(4)
Total liabilities	50,074	52,138	52,944	50,159	70,604	71,263	73,652	67,726
Net fixed assets	7,020	6,401	6,274	5,900	25,997	24,231	23,954	21,696
NWC, other assets	30,723	33,042	34,198	32,878	31,897	32,126	37,349	32,074
Cash	688	1,127	2,158	1,095	1,629	3,576	3,611	3,907
Investments	11,643	11,568	10,313	10,287	11,080	11,330	8,738	10,049
Total assets	50,074	52,138	52,944	50,159	70,604	71,263	73,652	67,726
EBITDA margin	6.6	7.8	8.9	8.7	10.1	10.5	11.1	7.4
EPS (Rs)	0.2	2.0	4.4	4.7	(1.0)	1.1	2.4	2.2
RoE (%)	0.1	3.4	7.2	7.3	(1.2)	1.8	4.5	3.2
RoCE (%)	6.5	9.9	12.5	11.7	6.1	8.1	8.6	6.7

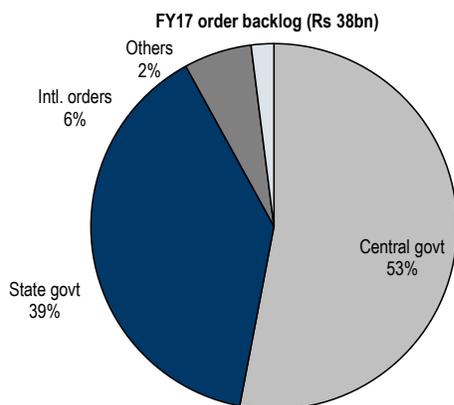
Source: Company data, Credit Suisse research

KNR Constructions

(CMP: Rs209, Market cap: Rs29 bn, 6M ADTO US\$0.4 mn, NOT COVERED)

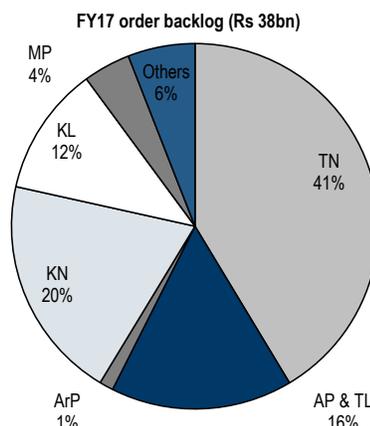
KNR Constructions is a South India-based road-focused contractor with ~90% of order backlog from the road sector. Most of the projects are secured from its public sector clients, with central government entities (NHAI, others) accounting for 53% of order backlog, and state government entities accounting for another 39%. In terms of geographical exposure, Tamil Nadu accounts for 40% of its total order backlog. Other southern states account for another 49% of its order book. The company also has a road development portfolio of two toll-based projects (Walayar and Muzaffarpur). The company has divested two of its annuity based projects that were owned in partnership with Patel Infrastructure to an Essel group company. KNR FY17 revenues came in at Rs15.4 bn (up 70% YoY) and PBT of Rs1.7 bn (up 35% YoY). Momentum on inflows and thus backlog has been gradual, with backlog up only 7-8% at end-FY17 over end-FY16.

Figure 86: Order book mainly from public sector



Source: Company data

Figure 87: Exposure largely in Southern states



Source: Company data

Figure 88: Key financials

Rs mn	Standalone financials				Consol financials			
	FY14	FY15	FY16	FY17	FY14	FY15	FY16	FY17
Revenues	8,348	8,761	9,026	15,410	8,950	9,312	9,951	16,795
EBITDA	1,258	1,262	1,554	2,296	1,314	1,268	1,742	2,639
PAT	600	709	1,589	1,681	590	677	1,245	1,016
Net worth	5,133	5,692	7,270	8,955	6,110	7,885	6,970	8,139
Minority interests.	-	-	-	-	559	560	807	646
Debt	908	963	1,168	1,303	4,260	7,683	7,454	6,662
Other liabilities	880	449	1,534	-	581	614	1,737	-
Total liabilities	6,921	7,105	9,971	10,257	11,510	16,741	16,968	15,447
Net fixed assets	2,640	2,269	2,468	2,622	8,575	13,432	12,631	2,657
NWC, other assets	3,768	4,363	6,908	6,701	2,106	2,637	3,718	11,807
Cash	112	157	161	246	573	436	450	338
Investments	400	315	434	688	256	236	168	645
Total assets	6,921	7,105	9,971	10,257	11,510	16,741	16,968	15,447
EBITDA margin	15.1	14.4	17.2	14.9	14.7	13.6	17.5	15.7
EPS (Rs)	21.3	25.2	56.5	59.8	21.0	24.1	44.3	36.1
RoE (%)	12.4	13.1	24.5	20.7	11.0	9.7	16.8	13.5
RoCE (%)	9.2	10.4	16.3	18.1	6.8	5.1	8.9	9.4

Source: Company data, Credit Suisse research

PNC Infratech

(CMP: Rs145, Market cap: Rs37 bn, 6M ADTO US\$1.3 mn, NOT COVERED)

PNC Infratech is an Uttar Pradesh-based, road-focused contracting company. It has taken up projects in Rajasthan, Haryana, Punjab, Bihar, Madhya Pradesh, Maharashtra, Karnataka and Tamil Nadu. On the asset development side, PNC has seven road projects awarded by NHAI, MPRDC, UPSHA and DSIIDC, and had invested Rs4.6 bn till March-2016. As on date, all the projects are operational and hence, there is no need for incremental equity investment in these BOT projects, per management. In FY17, revenues fell to Rs16.9 bn from Rs20 bn because of a delay in getting approval from NHAI for key contracts (on account of land acquisition delays). Several projects of the company are moving slowly, i.e., Nagina Kashipur, Varanasi Gorakhpur, Bhojpur-Buxar. The company has won four HAM projects worth Rs50 bn and projects worth about Rs41.5 bn have not been included in the order book as they are yet to achieve financial closure. The company

shared an order backlog of Rs54 bn, but effective backlog is Rs95 bn including the recently awarded HAM contracts.

Figure 89: Key financials

Rs mn	Standalone financials				Consol financials			
	FY14	FY15	FY16	FY17	FY14	FY15	FY16	FY17
Revenues	11,521	15,610	20,142	16,891	13,600	18,609	23,946	22,523
EBITDA	1,419	2,166	2,660	2,210	1,754	2,799	4,240	6,241
PAT	702	1,005	2,038	2,097	552	907	1,772	1,137
Net worth	6,290	7,184	13,623	15,722	7,097	8,711	13,097	14,610
Minority interests	-	-	-	-	1	1	1	0
Debt	2,747	3,530	117	1,473	10,250	16,924	16,035	17,946
Other liabilities	1,803	2,503	2,603	-	1,061	2,597	2,697	622
Total liabilities	10,839	13,218	16,343	17,195	18,409	28,232	31,829	33,179
Net fixed assets	1,544	2,175	2,144	3,557	12,415	21,655	22,899	24,126
NWC, other assets	4,786	6,596	8,585	8,607	3,788	5,229	7,208	7,560
Cash	999	212	971	355	1,156	411	1,066	466
Investments	3,510	4,235	4,644	4,676	1,051	938	656	1,027
Total assets	10,839	13,218	16,343	17,195	18,409	28,232	31,829	33,179
EBITDA margin	12.3	13.9	13.2	13.1	12.9	15.0	17.7	27.7
EPS (Rs)	17.6	25.2	39.7	40.9	13.9	22.8	34.5	22.2
RoE (%)	11.7	14.9	19.6	14.3	8.5	11.5	16.2	8.2
RoCE (%)	7.9	10.2	10.1	13.4	5.3	6.2	7.3	10.2

Source: Company data, Credit Suisse research

Gayatri Projects

(CMP: Rs162, Market cap: Rs29 bn, 6M ADTO US\$0.7 mn, NOT COVERED)

Gayatri Projects is an Andhra Pradesh-based construction company with exposure to roads and irrigation. The company also has a 13% stake in 1320 MW x 2 thermal power projects (option to up the stake to 30% as per agreement with Sembcorp.). The company has a stake in a road projects development portfolio, which is in the process of hiving off into a separate listed entity. Investment in both these ventures is about Rs13.4 bn (Rs6.4 bn in power and Rs7 bn in roads). Gayatri's FY17 revenues were up 17% to Rs21 bn and PAT of Rs0.9 bn (pre-exceptional basis). The company's order backlog is worth Rs130 bn, of which most of the projects have started execution after almost a year-long delay (Key projects are: four road projects around Varanasi, Eastern peripheral expressway, Navi Mumbai airport land preparation, Angul project in Odisha and Biharsharif project in Bihar). Roads constitute about 55% of the backlog while irrigation contributes about 26% of backlog. The company is a pan-India construction contractor and is not restricted to a specific geographical niche.

Figure 90: Key financials

(Rs mn)	Standalone financials				Consolidated financials			
	FY14	FY15	FY16	FY17	FY14	FY15	FY16	FY17
Revenues	18,125	16,011	18,122	21,154	15,940	15,008	16,204	22,765
EBITDA	2,697	2,076	2,595	3,246	3,309	3,417	4,086	2,945
PAT	476	221	586	897	(476)	(317)	12	(731)
Net worth	6,660	6,825	8,387	9,120	6,374	7,316	7,607	4,811
Minority interests	-	-	-	-	4,185	304	13	(915)
Debt	15,431	17,789	19,200	19,274	94,288	43,058	44,843	40,565
Other liabilities	6,500	5,329	231	232	11,490	6,382	195	232
Total liabilities	28,591	29,944	27,817	28,626	116,337	57,060	52,658	44,692
Net fixed assets	2,343	2,081	2,269	3,333	96,332	28,210	42,477	29,348
NWC, other assets	14,759	16,936	11,931	11,142	10,543	18,948	(206)	4,623
Cash	2,014	1,452	1,800	1,970	6,867	2,508	3,264	2,397
Investments	9,475	9,475	11,818	12,181	2,595	7,394	7,124	8,324
Total assets	28,591	29,944	27,817	28,626	116,337	57,060	52,658	44,692
EBITDA margin	14.9	13.0	14.9	15.3	20.8	22.8	25.2	12.9
EPS (Rs)	15.7	7.3	17.5	26.8	(15.8)	(10.5)	0.4	(20.8)
RoE (%)	7.4	3.3	7.7	10.3	(7.3)	(4.6)	0.2	(11.8)
RoCE (%)	5.1	3.9	5.9	7.7	5.0	3.4	3.7	2.6

Source: Company data, Credit Suisse research

HOLT® view

(Note: Credit Suisse HOLT is not a part of Equity Research)

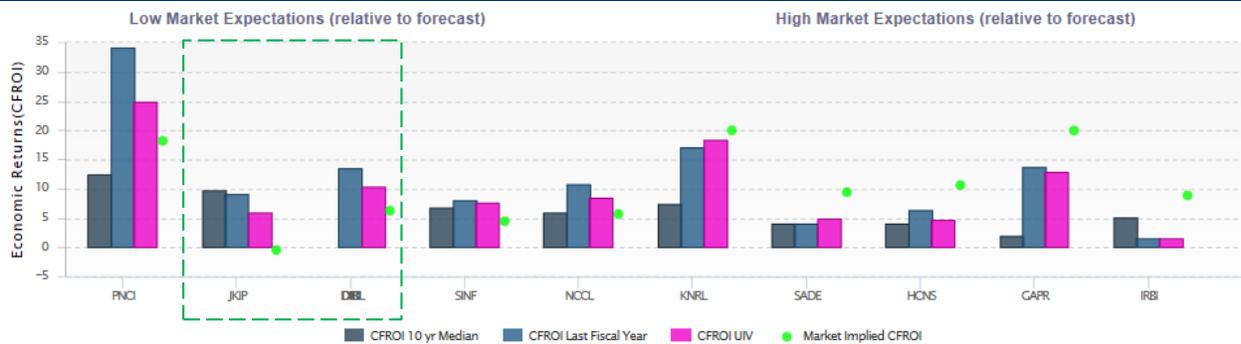
HOLT® view on Dilip Buildcon (DIBL) & J Kumar Infraprojects (JKIP)

HOLT is a value-based, return on capital framework proprietary to Credit Suisse. HOLT provides an objective view of over 20,000 companies in 65 countries using a methodology that examines accounting information, converts it to cash, and then values that cash, allowing investors to identify key drivers of value.

Benchmarking Dilip Buildcon & J Kumar Infraprojects with domestic peers

Benchmarking against domestic peers, both Dilip Buildcon and J Kumar Infraprojects have delivered higher-than-industry median CFROI® levels historically. That said, current market expectations appear conservative with investors pricing for further declines in CFROI relative to respective consensus forecasts and historical economic returns.

Figure 91: Implied market expectations are undemanding for both J Kumar & Dilip Buildcon



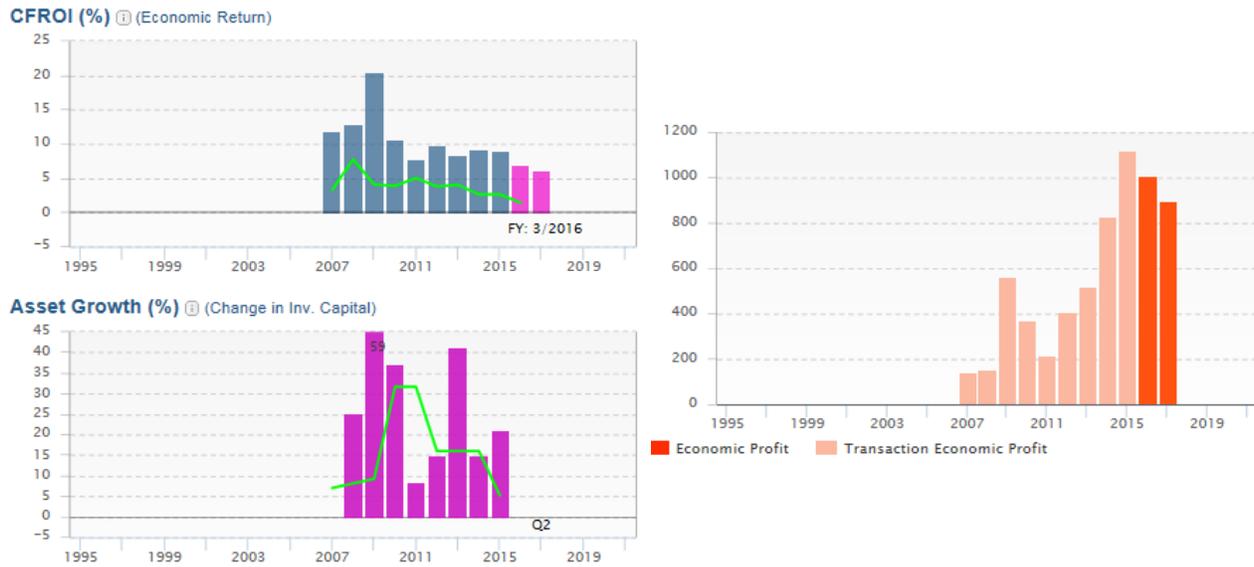
Source: Credit Suisse HOLT LensTM.

Gauging implied market expectations

Drilling down to individual companies, we note that J Kumar Infraprojects has delivered consistent improvements in economic profits (i.e. economic earnings of the firm in excess of the opportunity cost of using the assets or capital) over the past five years, a sign of strong wealth creation.

On Dilip Buildcon, the firm has consistently delivered double digit CFROI levels over the past five years. Supported by high operational quality, strong momentum and attractive valuation, the Best-in-Class name scores a near perfect 99 on the HOLT Scorecard.

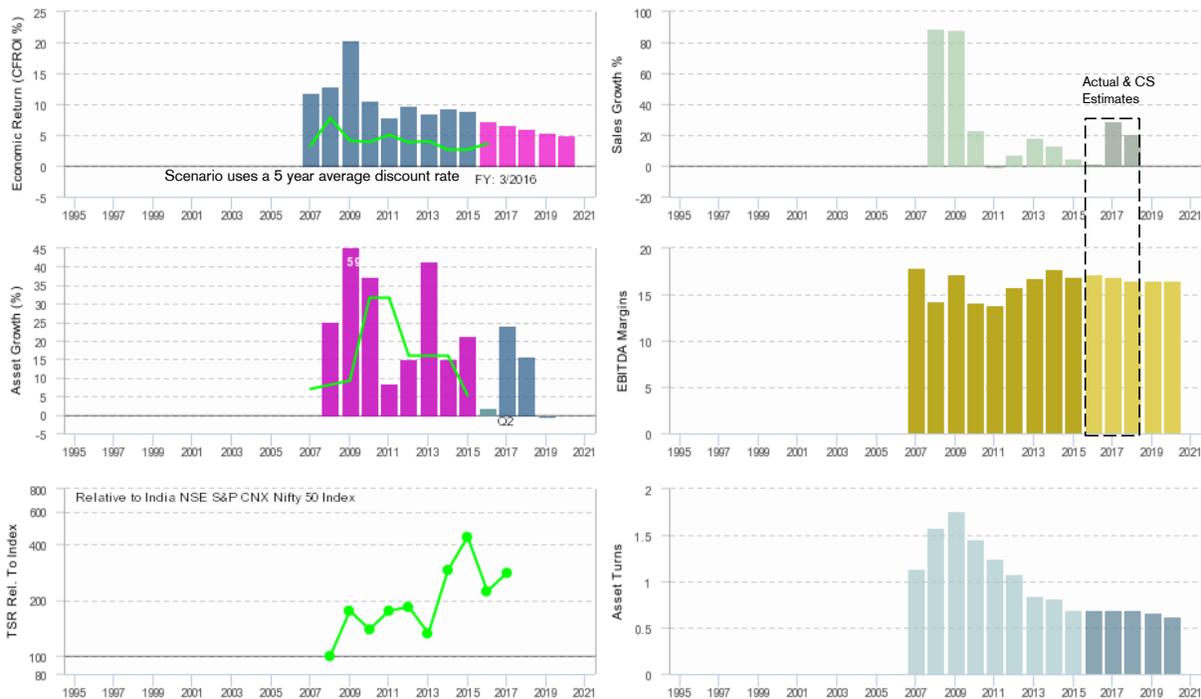
Figure 92: J Kumar Infra (JKIP)—delivering consistent improvement in economic profits over the past five years



Source: Credit Suisse HOLT LensTM.

We then run more refined analyses on both companies to gauge the current implied market expectations. On J Kumar, incorporating its latest results as well as CS revenue growth and EBITDA margin estimates through to FY19, the current share price implies for no growth thereafter. Implied CFROI would dip to historical lows over the same period. Expectations appear undemanding.

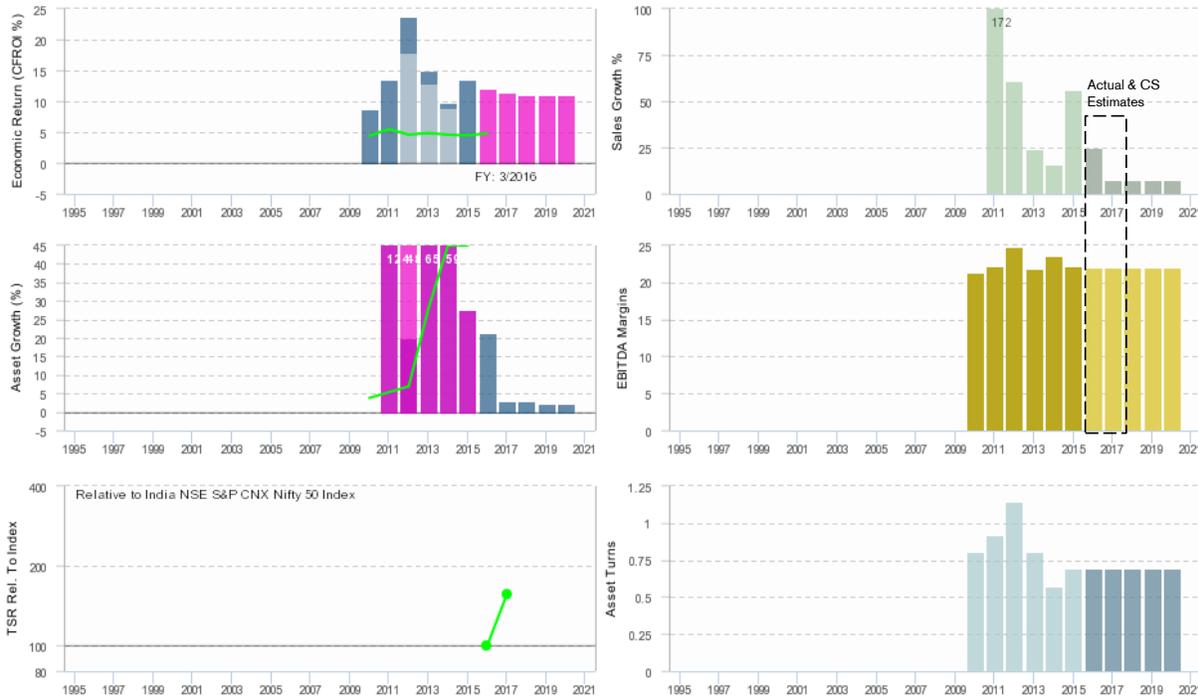
Figure 93: J Kumar Infraprojects (JKIP)—no growth priced beyond FY19



Source: Credit Suisse HOLT LensTM.

Moving to Dilip Buildcon, while top-line growth would be slower heading into FY18, the CS analyst is expecting growth (27%) to resume thereafter. Incorporating its latest results and CS sales estimates through to FY18, the current share price is implying just 7.5% top-line growth through to FY21, suggesting no recovery is priced in.

Figure 94: Dilip Buildcon (DIBL)—priced for 7.5% revenue growth into the medium term



Source: Credit Suisse HOLT LensTM.

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The HOLT methodology uses a proprietary performance measure known as Cash Flow Return on Investment (CFROI®). This is an approximation of the economic return, or an estimate of the average real internal rate of return, earned by a firm on the portfolio of projects that constitute its operating assets. A firm's CFROI can be directly compared against its real cost of capital (the investors' real discount rate) to see if the firm is creating economic wealth. By removing accounting and inflations distortions the CFROI allows for global comparability across sectors, regions and time, and is also a more comprehensive metric than the traditional ROIC and ROE.

Companies Mentioned (Price as of 29-Jun-2017)

- Ahluwalia (AHLU.BO, Rs321.05)
- Ashoka Buildcon (ABDL.BO, Rs185.25)
- Dilip Buildcon Ltd (DIBL.BO, Rs438.2, OUTPERFORM[V], TP Rs650.0)
- Gayatri Projects (GAPR.BO, Rs160.25)
- Hindustan Constr (HCNS.BO, Rs39.7)
- IVRCL Ltd (IVRC.BO, Rs4.3)
- J Kumar Infra (JKIP.BO, Rs293.45, OUTPERFORM, TP Rs375.0)
- KNRCL (KNRL.BO, Rs207.65)
- Larsen & Toubro (LART.BO, Rs1702.4)
- MBL (MBLI.BO, Rs27.15)
- NBCC (India) (NBCC.BO, Rs204.05)
- NCC Ltd (NCCL.BO, Rs89.0)
- PNC Infratech (PNCI.BO, Rs143.55)
- Punj Lloyd Ltd (PUJL.BO, Rs18.9)
- Sadbhav Engineering Ltd (SADE.BO, Rs307.25)
- Simplex Infrastructures Ltd (SINF.BO, Rs505.45)

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3-Year Price and Rating History for Larsen & Toubro (LART.BO)

LART.BO	Closing Price	Target Price	
Date	(Rs)	(Rs)	Rating
24-Jul-14	1662.90		NR
20-Nov-14	1642.20	1975.00	O *
10-Feb-15	1573.80	1900.00	
08-Jul-15	1804.30	2175.00	
23-Sep-15	1495.95	2000.00	
20-Oct-15	1572.95	1775.00	N
02-Nov-15	1388.40	1515.00	
11-Jan-16	1174.80	1475.00	O
01-Feb-16	1122.15	1425.00	
26-May-16	1472.60	1650.00	
21-Jul-16	1556.25	1825.00	
26-Sep-16	1468.70	1925.00	
23-Nov-16	1357.85	1900.00	
28-Nov-16	1356.15	1800.00	
20-Mar-17	1538.25	1850.00	
30-May-17	1766.85	2060.00	

* Asterisk signifies initiation or assumption of coverage.



3-Year Price and Rating History for Sadbhav Engineering Ltd (SADE.BO)

SADE.BO	Closing Price	Target Price	
Date	(Rs)	(Rs)	Rating
19-Jan-15	257.95	320.00	O *
04-Mar-15	336.50	385.00	
27-Nov-15	345.25	380.00	
09-Feb-16	299.45	350.00	
08-Jul-16	294.70	340.00	
26-Sep-16	283.55	375.00	
17-Feb-17	275.85	360.00	

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Neutral (N) : The stock's total return is expected to be in line with the relevant benchmark* over the next 12 months.

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Neutral/Hold*	40%	(60% banking clients)
Underperform/Sell*	14%	(54% banking clients)
Restricted	2%	

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Target Price and Rating

Valuation Methodology and Risks: (12 months) for Dilip Buildcon Ltd (DIBL.BO)

Method: We value Dilip Buildcon at Rs650 which includes Rs560/sh for EPC business (at 18x one-year forward earnings) and Rs90/sh for its build-operate-transfer (BOT) assets (at 1x forward book). Our OUTPERFORM rating is based on strong orders in the sector which will help growth in backlog and revenues supported by strong execution capabilities.

Risk: Key risks to our Rs650 target price and OUTPERFORM rating for Dilip Buildcon include: (1) delay in the start of recent project wins—the company has about Rs50-60 bn of backlog that is yet to start construction; (2) less flexibility to deal with downcycles—its integrated model would suffer in case ordering activity is lower in certain years as the company carries higher fixed manpower and equipment costs; (3) promoter's family-driven management and bandwidth constraints—the company has grown exceptionally fast and unless it builds

management band width, it may not be able to retain its edge in execution; and (4) inability to build other verticals apart from roads as well as higher competition can limit the opportunity basket and affect margins as well.

Target Price and Rating

Valuation Methodology and Risks: (12 months) for J Kumar Infra (JKIP.BO)

Method: We value J Kumar Infra's stock at 18x FY19E earnings in line with peers to get a target price of Rs375 due to: (1) strong growth visibility from executing its backlog; (2) ~20% earnings CAGR over FY17-20E; and (3) a strong long-term opportunity in its key focus areas. Our OUTPERFORM rating is based on orders of new metro projects in Mumbai and other large cities which will provide strong growth opportunities leading to strong revenue and earnings growth.

Risk: Key risks to our OUTPERFORM rating and target price of Rs375 for J Kumar Infra include: (1) dependence on four or five large contracts for most of its revenues; (2) diversification from Mumbai-based projects is in early stages; (3) family-driven management with the second generation taking charge now; (4) high competitive intensity in the sector could impact opportunity share and margins; and (5) the escalation of charges of irregularities in contract execution by the Municipal Corp. of Greater Mumbai or any other client could be a risk.

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