

Nagarjuna Constructions

Q2FY11 update

11 November 2010

Buy

Target Price: Rs215

CMP: Rs155*

Upside: 39%

*as on 10 November 2010

Inline results; maintain Buy

Nagarjuna Constructions Company's (NCC) Q2 numbers were inline with our estimates. The results were better-than-expected despite good monsoons this year (construction activities slowdown during rains). Though order intake during Q2 was low at Rs15bn (vs our estimate of Rs28bn), the company seems on target for its target order intake of Rs100bn for FY11 (we have factored in Rs116bn). The management said execution has improved in Q3 till date and the company is on track to meet its FY11 standalone revenue guidance of Rs58bn (our estimate: Rs57bn). Though real estate sales were slightly lower, consolidated revenue of Rs73bn is not at major risk. We maintain our estimates and reiterate Buy with a target price of Rs215. (Upside of 39%).

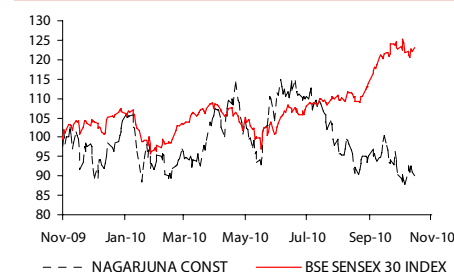
- **Q2 results inline:** NCC's Q2 numbers were inline with our expectation with revenue at Rs12bn, EBITDA at Rs1.2bn and adj PAT at Rs500mn.
- **Order-inflow guidance maintained:** The company bagged orders worth Rs14bn in Q2FY11 (Rs35bn in 1HFY11) and is on target to achieve its guided Rs100bn order-intake in FY11 (we factor Rs116bn).
- **BOT projects/Power project:** NCC's 3 road BOT projects would be operational within this year and decision on disputed power project of 1,320MW in Andhra Pradesh is awaited this month.
- **Reiterate Buy:** We maintain our estimates and reiterate Buy with a target price of Rs215 (upside of 39%). We predicate our view on its diversified order-book, strong execution record, low leverage of 0.8x v/s peers of >1X, and low investment needs for BOT projects.

Key Data

| | |
|--------------------------|------------|
| Bloomberg Code | NJCC IN |
| Reuters Code | NGCN.BO |
| Current Shares O/S (mn) | 256.6 |
| Diluted Shares O/S(mn) | 256.6 |
| Mkt Cap (Rsbn/USDmn) | 39.8/899.1 |
| 52 Wk H / L (Rs) | 198/132 |
| Daily Vol. (3M NSE Avg.) | 1,272,619 |
| Face Value (Rs) | 2 |

USD = Rs44.3

One Year Indexed Stock Performance



Price Performance (%)

| | 1M | 6M | 1Yr |
|-------|-----|--------|-------|
| NJCC | 3.0 | (10.1) | (9.6) |
| NIFTY | 2.9 | 22.1 | 24.2 |

Source: Bloomberg, Centrum Research
*as on 10 November 2010

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| Y/E March (Rsmn) (Standalone) | Q2FY11 | Q2FY10 | YoY (%) | Q1FY11 | QoQ (%) | Q2FY11E | Variance (%) |
|--------------------------------|---------------|---------------|-------------|---------------|-------------|---------------|---------------|
| Net sales | 12,013 | 10,670 | 12.6 | 10,865 | 10.6 | 12,361 | (2.8) |
| Consumption of RM | 9,817 | 8,871 | 10.7 | 8,959 | 9.6 | 10,277 | (4.5) |
| % of sales | 81.7 | 83.1 | (142) | 82.5 | (74) | 83.1 | (142.9) |
| Employee costs & SG&A | 963 | 711 | 35.5 | 848 | 13.5 | 840 | 14.6 |
| % of sales | 8.0 | 6.7 | 135 | 7.8 | 21 | 6.8 | 122.0 |
| EBITDA | 1,234 | 1,089 | 13.3 | 1,058 | 16.7 | 1,244 | (0.8) |
| EBITDA Margin (%) / bps | 10.3 | 10.2 | 7 | 9.7 | 54 | 10.1 | 20.8 |
| Dep and amortisation | 168 | 129 | 30.6 | 156 | 7.8 | 147 | 14.5 |
| Interest | 375 | 322 | 16.2 | 293 | 27.6 | 333 | 12.5 |
| EBT | 691 | 637 | 8.4 | 608 | 13.6 | 763 | (9.5) |
| Other income | 54 | 8 | 549.7 | 13 | 328.5 | 12 | 352.5 |
| PBT | 745 | 646 | 15.4 | 621 | 20.1 | 775 | (3.9) |
| Provision for tax | 285 | 206 | 38.2 | 207 | 38.0 | 264 | 8.2 |
| Effective Tax Rate %/bps | 38.3 | 32.0 | 632 | 33.3 | 498 | 34.0 | 429.3 |
| PAT (reported) | 460 | 439 | 4.7 | 414 | 11.1 | 512 | (10.2) |
| PAT (adjusted) | 500 | 439 | 13.8 | 414 | 20.8 | 512 | (2.4) |
| NPM (%) / bps | 4.2 | 4.1 | 4 | 3.8 | 35 | 4.1 | 195.3 |
| EPS (adjusted) | 1.95 | 1.85 | 5.3 | 1.61 | 20.8 | 2.0 | (2.4) |

Source: Company, Centrum Research

| Y/E Mar (Rsmn)* | Revenue | YoY (%) | EBITDA | EBITDA (%) | Adj PAT | YoY (%) | EPS (Rs) | RoE (%) | RoCE (%) | P/E (x) | EV/EBITDA (x) |
|-----------------|---------|---------|--------|------------|---------|---------|----------|---------|----------|---------|---------------|
| FY09 | 41,514 | 19.4 | 3,737 | 9.0 | 1,539 | (5.0) | 6.7 | 9.4 | 11.9 | 23.0 | 12.8 |
| FY10 | 47,778 | 15.1 | 4,834 | 10.1 | 1,998 | 29.9 | 7.8 | 11.8 | 12.9 | 19.9 | 11.4 |
| FY11E | 57,043 | 19.4 | 5,830 | 10.2 | 2,576 | 28.9 | 10.0 | 11.0 | 12.8 | 15.4 | 10.1 |
| FY12E | 69,503 | 21.8 | 7,171 | 10.3 | 3,102 | 20.4 | 12.1 | 12.1 | 13.6 | 12.8 | 8.9 |
| FY13E | 82,649 | 18.9 | 8,609 | 10.4 | 4,310 | 20.2 | 14.0 | 12.7 | 14.0 | 11.1 | 8.0 |

* Standalone; Source: Company, Centrum Research Estimates

Please refer to important disclosures/disclaimers in Appendix A

Key takeaways from the conference call

Management maintains guidance: The management maintains its FY11 standalone revenue guidance of Rs57.5bn and order-inflow guidance of Rs100bn (out of which Rs45bn has been bagged in FY11 till date; Rs35bn in H1FY11 and Rs10bn later).

Investment in BOT assets: Three road projects out of five will be operational in FY11 (2 in Dec 2010 and another in Jan 2011) and the additional investment on these projects is Rs250mn. The hydro-power project Himachal Sorang project will be operational by Dec 2011 and additional investment required is Rs250mn. Please note that two of company road projects are operational and the total investment in all infrastructure assets is Rs5bn till date.

Update on 1,320MW Sompeta Thermal Power plant: The Expert Committee in Ministry of Environment and Forests (MoEF) will deliver its report in November on whether the thermal power project at the Sompeta site can go ahead. However, the company has already started working on alternative with searching new sites since the report have a negative tone to it. As far as investment is concerned, the company has invested around Rs2bn (Rs1.2bn for performance guarantee and Rs830mn for land, survey, consultancy, etc). Company cited 2015 as the year to decide the fate of this guarantee amount Rs1.2bn since they have been given option to supply power from external source. Power supply agreement with Karnataka is for 400MW @ Rs3.89/unit.

Dubai Real Estate Project: The company spent further Rs250mn in that project this quarter.

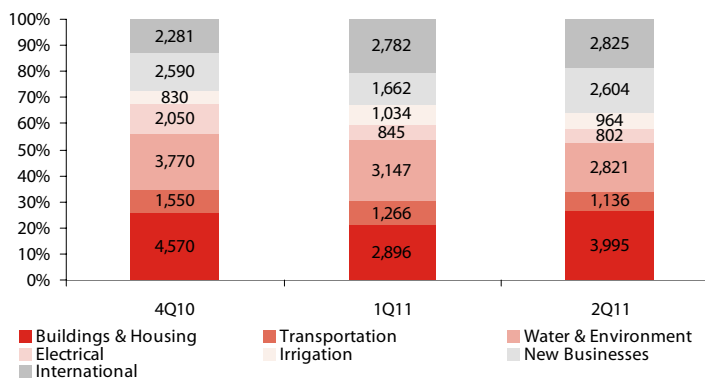
Rs100-150m liability emerged out of tax raids conducted in early Oct 2010: As a result of Income Tax raids conducted on NCC's offices (46 locations including corporate office), the tax officials has made company liable for tax of Rs100-Rs150mn which will be booked in FY11. The reason for this amount is not clearly indicated (the management says IT officials are still preparing for their case). The company has made a provision of Rs40m with regards to this in this quarter. In 2002, IT officials made a similar raid making company liable for Rs40-Rs50mn.

Road Project: The management expects Rs20bn order-inflow from road segment as bidding activity is expected to get hectic between Dec 2010 and June 2011.

Power segment update: Execution will pick-up substantially in 2HFY11 as KVK Nilachal project has received mobilization advance.

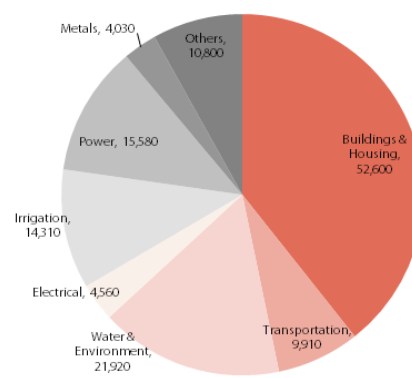
Andhra Pradesh Update: State has paid most of the bills. Current outstanding is Rs250-Rs300mn from irrigation side. NCC is working on a low-cost housing project worth Rs5bn. Andhra Pradesh made allocation of Rs150bn for irrigation out of which Rs70bn was paid to developers/contractors.

Exhibit 1: Order-Book Mix over last 3 quarters



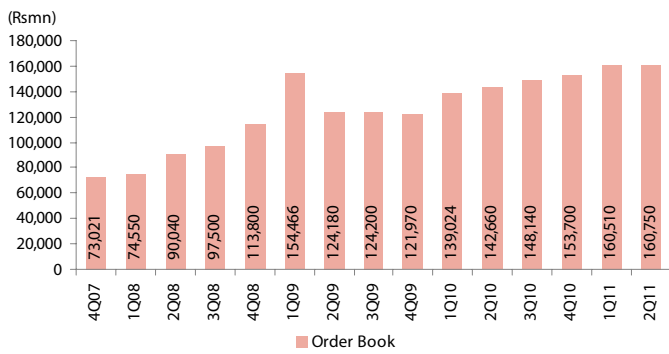
Source: Company, Centrum Research Estimates

Exhibit 2: Order-book as on Q2FY11



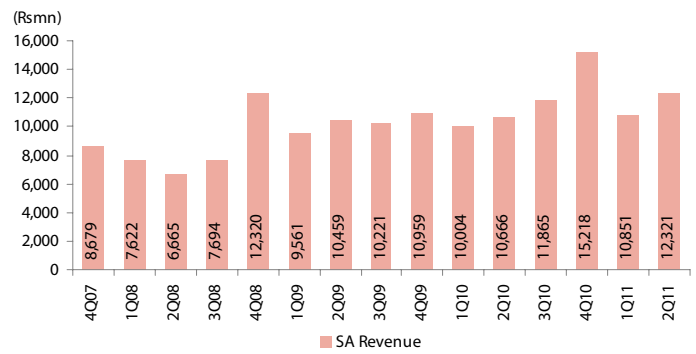
Source: Company, Centrum Research Estimates

Exhibit 3: Order-book trend over last 4 years



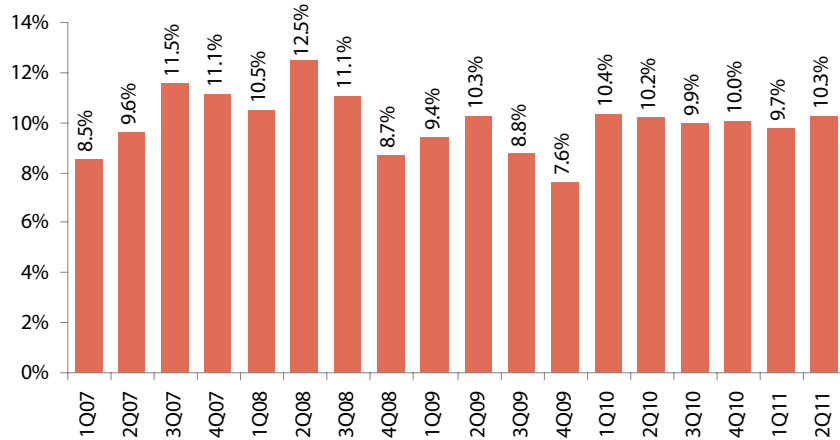
Source: Company, Centrum Research Estimates

Exhibit 4: Standalone revenue trend over last 4 years



Source: Company, Centrum Research Estimates

Exhibit 5: Standalone EBITDA Margins trend



Source: Company, Centrum Research Estimates

Financials (Standalone)

Exhibit 6: Income Statement

| Y/E March (Rsmn) | FY09 | FY10 | FY11E | FY12E | FY13E |
|--------------------------------|---------------|---------------|---------------|---------------|---------------|
| Revenues | 41,514 | 47,778 | 57,043 | 69,503 | 82,649 |
| <i>Growth in revenue</i> | 19.4 | 15.1 | 19.4 | 21.8 | 18.9 |
| Cost of Raw Material | 34,972 | 40,133 | 47,616 | 58,205 | 69,215 |
| <i>% of Revenue</i> | 84.2 | 84.0 | 83.5 | 83.7 | 83.7 |
| Employee cost | 1,885.9 | 1,841.3 | 2,356.8 | 2,643.0 | 3,060.6 |
| <i>% of Sales</i> | 4.5 | 3.9 | 4.1 | 3.8 | 3.7 |
| O&M expenses | 919.5 | 969.4 | 1,239.8 | 1,483.7 | 1,764.3 |
| <i>% of Sales</i> | 2.2 | 2.0 | 2.2 | 2.1 | 2.1 |
| EBITDA | 3,737 | 4,834 | 5,830 | 7,171 | 8,609 |
| <i>EBITDA Margin (%)</i> | 9.0 | 10.1 | 10.2 | 10.3 | 10.4 |
| Depreciation | 533 | 525 | 598 | 715 | 866 |
| PBIT | 3,204 | 4,309 | 5,233 | 6,456 | 7,743 |
| Interst expenses | 964 | 1,322 | 1,398 | 1,830 | 2,398 |
| PBIT from operations | 2,240 | 2,987 | 3,835 | 4,626 | 5,345 |
| Other non operating income | 42 | 48 | 61 | 73 | 87 |
| PBT before ext.od items | 2,282 | 3,035 | 3,896 | 4,699 | 5,433 |
| Extra-ordinary income/ (exp) | - | 495.6 | - | - | - |
| PBT | 2,282 | 3,530 | 3,896 | 4,699 | 5,433 |
| Provision for tax | 743 | 1,204 | 1,320 | 1,597 | 1,847 |
| <i>Effective tax rate (%)</i> | 32.6 | 34.1 | 33.9 | 34.0 | 34.0 |
| <i>Minority interest</i> | - | - | - | - | - |
| PAT | 1,539 | 2,326 | 2,576 | 3,102 | 3,586 |
| Adjustment for Ext.Od items | - | 328 | - | - | - |
| Adjusted PAT | 1,539 | 1,998 | 2,576 | 3,102 | 3,586 |
| <i>Growth in PAT (%)</i> | (5.0) | 29.9 | 28.9 | 20.4 | 15.6 |
| <i>PAT margin (%)</i> | 3.7 | 4.2 | 4.5 | 4.5 | 4.3 |

Source: Company, Centrum Research Estimates

Exhibit 7: Balance Sheet

| Y/E March (Rsmn) | FY09 | FY10 | FY11E | FY12E | FY13E |
|-------------------------------|---------------|---------------|---------------|---------------|---------------|
| Share Capital | 458 | 513 | 513 | 513 | 513 |
| Stock Options | - | - | - | - | - |
| Reserves | 16,398 | 21,943 | 23,935 | 26,332 | 29,221 |
| Shareholders' fund | 16,856 | 22,457 | 24,448 | 26,846 | 29,734 |
| Debt | 12,439 | 15,302 | 19,302 | 24,402 | 29,302 |
| Deferred Tax Liability | 188 | 255 | 255 | 255 | 255 |
| Minority Interest | - | - | - | - | - |
| Total Capital Employed | 29,482 | 38,013 | 44,005 | 51,502 | 59,290 |
| Gross Block | 6,233 | 7,561 | 8,790 | 10,141 | 11,628 |
| Accumulated dep. | 1,641 | 2,023 | 2,621 | 3,336 | 4,202 |
| Net Block | 4,592 | 5,538 | 6,169 | 6,806 | 7,426 |
| Capital WIP | 281 | 434 | 484 | 534 | 582 |
| Total Fixed Assets | 4,873 | 5,972 | 6,653 | 7,339 | 8,008 |
| Investments | 7,402 | 9,412 | 10,412 | 11,612 | 12,612 |
| Deferred Tax Asset | - | - | - | - | - |
| Inventories | 7,495 | 7,539 | 9,883 | 11,607 | 14,439 |
| Debtors | 10,260 | 12,995 | 15,423 | 18,878 | 21,700 |
| Cash & bank balances | 1,345 | 1,997 | 2,037 | 2,079 | 2,975 |
| Loans and Advances | 14,484 | 18,520 | 21,803 | 25,606 | 29,000 |
| Other Current Assets | 30 | 32 | 54 | 63 | 75 |
| Total current assets | 33,615 | 41,083 | 49,200 | 58,234 | 68,189 |
| Current lia & provisions | 16,408 | 18,453 | 22,260 | 25,682 | 29,518 |
| Net current assets | 17,206 | 22,629 | 26,940 | 32,552 | 38,671 |
| Total Assets | 29,482 | 38,013 | 44,005 | 51,502 | 59,291 |

Source: Company, Centrum Research Estimates

Exhibit 8: Cash flow

| Y/E March (Rsmn) | FY09 | FY10 | FY11E | FY12E | FY13E |
|-----------------------------------|----------------|----------------|----------------|----------------|----------------|
| CF from operating | | | | | |
| Profit before tax | 2,282 | 3,530 | 3,896 | 4,699 | 5,433 |
| Depreciation | 533 | 525 | 598 | 715 | 866 |
| Interest expenses | 964 | 1,322 | 1,398 | 1,830 | 2,398 |
| OP profit before WC change | 3,786 | 4,886 | 5,891 | 7,244 | 8,697 |
| Working capital adjustment | (3,955) | (3,345) | (4,270) | (5,569) | (5,224) |
| Gross cash from operations | (169) | 1,541 | 1,621 | 1,675 | 3,473 |
| Direct taxes paid | (1,319) | (1,302) | (1,320) | (1,597) | (1,847) |
| Cash from operations | (1,488) | 238 | 301 | 78 | 1,626 |
| CF from investing | | | | | |
| Capex | (75) | (1,628) | (1,278) | (1,402) | (1,535) |
| Investment | (1,107) | (2,148) | (1,000) | (1,200) | (1,000) |
| Others | 100 | 12 | - | - | - |
| Cash from investment | (1,082) | (3,763) | (2,278) | (2,602) | (2,535) |
| CF from financing | | | | | |
| Proceeds from sh cap & prem. | 0 | 3,580 | - | - | - |
| Borrowings/ (Repayments) | 3,501 | 2,863 | 4,000 | 5,100 | 4,900 |
| Interest paid | (1,567) | (1,972) | (1,398) | (1,830) | (2,398) |
| Dividend paid | (348) | (294) | (585) | (704) | (698) |
| Cash from financing | 1,586 | 4,177 | 2,018 | 2,566 | 1,804 |
| Net cash increase/ (dec) | (985) | 652 | 40 | 42 | 895 |

Source: Company, Centrum Research Estimates

Exhibit 9: Key Ratios

| Y/E March | FY09 | FY10 | FY11E | FY12E | FY13E |
|---------------------------------|-------|-------|-------|-------|-------|
| Margin Ratios (%) | | | | | |
| EBITDA Margin | 9.0 | 10.1 | 10.2 | 10.3 | 10.4 |
| PBIT Margin | 7.7 | 9.0 | 9.2 | 9.3 | 9.4 |
| PBT Margin | 5.4 | 6.3 | 6.7 | 6.7 | 6.5 |
| PAT Margin | 3.7 | 4.2 | 4.5 | 4.5 | 4.3 |
| Growth Ratios (%) | | | | | |
| Revenues | 19.4 | 15.1 | 19.4 | 21.8 | 18.9 |
| EBITDA | 2.5 | 29.4 | 20.6 | 23.0 | 20.1 |
| Net Profit | (5.0) | 29.9 | 28.9 | 20.4 | 15.6 |
| Return Ratios (%) | | | | | |
| ROCE | 11.9 | 12.9 | 12.8 | 13.6 | 14.0 |
| ROIC | 19.2 | 19.9 | 20.6 | 21.4 | 21.9 |
| ROE | 9.4 | 11.8 | 11.0 | 12.1 | 12.7 |
| Turnover Ratios | | | | | |
| Asset turnover ratio (x) | 1.4 | 1.3 | 1.3 | 1.3 | 1.4 |
| Working Capital Turnover (x) | 2.4 | 2.1 | 2.1 | 2.1 | 2.1 |
| Avg collection period (days) | 90.2 | 99.3 | 98.7 | 99.1 | 96.1 |
| Avg payment period (days) | 155.8 | 148.7 | 150.4 | 142.6 | 147.6 |
| Per share (Rs) | | | | | |
| Fully diluted EPS | 6.7 | 7.8 | 10.0 | 12.1 | 14.0 |
| CEPS | 9.1 | 9.8 | 12.4 | 14.9 | 17.4 |
| Book Value | 73.7 | 87.5 | 95.3 | 104.6 | 115.9 |
| Solvency ratios (%) | | | | | |
| Debt/ Equity | 0.7 | 0.7 | 0.8 | 0.9 | 1.0 |
| Interest coverage ratio | 3.9 | 3.7 | 4.2 | 3.9 | 3.6 |
| Valuation parameters (x) | | | | | |
| P/E | 23.0 | 19.9 | 15.4 | 12.8 | 11.1 |
| P/BV | 2.1 | 1.8 | 1.6 | 1.5 | 1.3 |
| EV/ EBITDA | 12.8 | 11.4 | 10.1 | 8.9 | 8.0 |
| EV/ Sales | 1.2 | 1.2 | 1.0 | 0.9 | 0.8 |
| M-Cap/ Sales | 0.9 | 0.8 | 0.7 | 0.6 | 0.5 |

Source: Company, Centrum Research Estimates

Appendix A

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