Emkay Research

Patel Engineering

Q1FY09 results

Result Update

16th July 2008

BUY

Price	Target Price
Rs343	Rs514

Sensex – 12,676

Price Performance

(%)	1M	3M	6M	12M
Absolute	(10)	(37)	(65)	(26)
Rel. to Sensex	8	(22)	(44)	(10)

Source: Bloomberg

Stock Details

Sector	Construction
Reuters	PENG.BO
Bloomberg	PEC@IN
Equity Capital (Rs mn)	60
Face Value (Rs)	1
No of shares o/s (mn)	60
52 Week H/L (Rs)	1,070/286
Market Cap (Rs bn /USD mn)	20/463
Daily Avg Vol (No of shares)	122778
Daily Avg Turnover (US$ mn)	1.4

Shareholding Pattern (%)

	31/3/08	31/12//07	30/9/07
Promoters	52.3	54.0	54.1
FII/NRI	11.3	11.9	10.9
Institutions	11.0	10.6	10.8
Private Corp.	1.9	1.7	0.9
Public	23.6	21.8	23.3

Source: Capitaline

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Patel Engineering Ltd. (Patel) announced its Q1FY09 results which were ahead of our estimates. Key highlights of the results were:

- The consolidated revenues for the quarter stood at Rs5.58 billion, up 34.5% over corresponding period last year. This was marginally ahead of our estimates. On the standalone basis, the company has reported revenues of Rs3.9 billion up 20% y-o-y. The growth in revenue was mainly on account of increased contribution from the overseas business and integrated JVs where the revenue almost doubled compared to last year.

- EBITDA margin was impressive at 14.1% on the consolidated basis an improvement of 300 bps over Q1FY08. The company has now reported very good margins for two quarters in a row, as the contribution from overseas operations have returned better profitability margins. Our estimates for FY09 full year is at 13% against 14.2% achieved in FY08. We believe that if the margins scenario continues over next quarter, we may revise our margin estimates upwards.

- PAT grew 29.4% to Rs349.9 million. The growth in PAT was slower on account of higher depreciation (growing at 70% over last year) and high interest cost (over 3x last year). However the higher depreciation and interest cost was in line with the expectations

- The company has continued to take benefit under Sec 80 IA, resulting in an effective tax rate of just 11.9% for the quarter. However, in our estimates we have built in tax at a rate of 33%.

Results in brief

Income Statement	Standalone			Consolidated		
Y/E,Mar (Rs. mn)	Q1FY08	Q1FY09	Y-o-Y Gr.(%)	Q1FY08	Q1FY09	Y-o-Y Gr.(%)
Net Sales	**3301**	**3962**	**20%**	**4153**	**5584**	**34%**
Expenses	2943	3396	15%	3690	4798	30%
Construction expenses	2690	3117	16%	3360	4328	29%
% of sales	*81*	*79*		*81*	*78*	
Other expenses	253	278	10%	330	470	42%
% of sales	*8*	*7*		*8*	*8*	
EBIDTA	**358**	**567**	**58%**	**462**	**786**	**70%**
EBIDTA %	***10.9***	***14.3***	***340 bps***	***11.1***	***14.1***	***300 bps***
Depreciation	66	91	38%	98	167	70%
EBIT	**292**	**475**	**63%**	**364**	**619**	**70%**
EBIT %	***8.9***	***12.0***	***310 bps***	***8.8***	***11.1***	***230 bps***
Interest	27	145	435%	50	176	253%
Other income	35	23	-35%	36	24	-34%
PBT	**300.1**	**352.9**	**18%**	**350.1**	**466.6**	**33%**
Total Tax	36.5	42.0	15%	61.1	85.5	40%
Effective tax rate (%)	*12.2*	*11.9*		*17.5*	*18.3*	
APAT (Before MI)	**263.6**	**310.9**	**18%**	**289.0**	**381.1**	**32%**
Net Margin (%)	*7.9*	*7.8*	-10 bps	*6.9*	*6.8*	-10 bps
Minority Interest	0.0	0.0		*18.6*	*31.2*	
APAT	***263.6***	***310.9***	**18%**	**270.4**	**349.9**	**29%**
E/O items	0.0	0.0		0.0	0.0	
Reported PAT	**263.6**	**310.9**	**18%**	**270.4**	**349.9**	**29%**
FDEPS	**4.4**	**5.2**	**18%**	**4.5**	**5.9**	**29%**

Outlook

The company has started FY09 on a firm note. The company has also maintained its core strength in the hydro-power segment with 59% of the strong order backlog of Rs60 billion coming from this segment. The company has restructured their US operation which is now returning good profitability numbers. This apart the company has forayed into newer geographical location of Algeria and is looking to expand its operations further in African continent. The company has also set an ambitious plan for its real estate business. The land bank of over 1000 acres which was historically acquired at a very low cost has been transferred to its real estate subsidiary and the company plans to develop it over next 10 years. We believe that the company's strong presence in the hydel power segment will drive the contracting business and also expect the real estate business to be value accretive in the long term.

Valuation & View

The stock currently trades at 11.0x FY09E EPS of Rs18.6 and 7.9x FY10E EPS of Rs25.8 (adjusting for the value from non-contracting business and value from contracting business through subsidiaries and JVs). We value the company on the SOTP basis valuing the core construction business at Rs378 per share, BOT road projects at Rs4 per share, and real estate projects at Rs134 per share. We thus arrive at our 12 month target price of Rs514 per share, which represents an upside potential of 50%. We maintain our 'BUY' rating.

Valuation

Segment	Basis	Multiple (x)	Value (Rs Mn)	Value per share (Rs)	Remarks
Construction business (Standalone)	FY10E, PE (x)	15.0	20012	335	Leader in high margin hydro power segment, RoIC among the best at 23% warrants a multiple of 15.0x.
Projects under Integrated JVs & Subsidiaries	FY10E, PE (x)	12.0	2410	40	Valued at a discount to Indian business because of lower margins
BOT projects (Annuity based)					
Karnataka-AP Border	NPV		108	2	Projects under construction. Both projects expected to be operational over next two years. Discounted FCFE @ 11%
Islam Nagar-Kadtal	NPV		90	2	
Real Estate division					
Phase-1	NPV	50% Disc	6023	101	NPV based on development over next 7 years of 120 acres of land under development, WACC -15%
Other land bank	P/BV	1.0	2000	34	Historically acquired land bank of 880 acres, valued at indicated cost
Total Fair value			**30642**	**514**	

For our bear case valuations, we take a discount of 20% to our target multiple. Thus contracting business on bear case is valued at Rs301 per share giving a target price of Rs438.

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