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CREDIT SUISSE

India Construction Sector

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SECTOR REVIEW

Buy in the correction

- **Structural concerns for construction companies are not over yet. While we continue to factor in conservative estimates, we believe that stock corrections are overdone and valuations appear very attractive, even as interest rates also seem to be peaking. We upgrade IVRCL and NCC to an OUTPERFORM, Gammon to a NEUTRAL and maintain our OUTPERFORM rating on Simplex.**
- **We continue to believe that Indian construction players' earnings will be impacted over FY09-10E, as their operating and financing environment continues to be difficult. We believe that most construction companies under our coverage might report disappointing results versus consensus estimates for most of FY09E. We factor in conservative estimates – our earnings are still 10-20% below consensus over FY09-10E.**
- **Even as we factor in our conservative estimates, we believe that with the stocks having fallen 56-80% from their peaks, the concerns are more than discounted in the stock prices. The core construction businesses are now valued at 7-9x FY10E EPS and most of the stocks are now trading at a significant discount to their fair values. Furthermore, interest rates now seem to be peaking, which provides potential for upside risk to our estimates.**
- **We upgrade IVRCL and NCC to an OUTPERFORM from Neutral and Underperform, respectively, given our 12-month SOTP-based target price reflects 41% potential upside for IVRCL and 24% potential upside for NCC from their current market prices. Gammon, on the other hand, is now trading at close to our target price; we therefore upgrade Gammon to a NEUTRAL from Underperform. We maintain our OUTPERFORM rating on Simplex. IVRCL and Simplex are our top picks due to their superior earnings growth, RoE and favourable order book mix.**

Figure 1: **Valuation summary of our coverage universe**

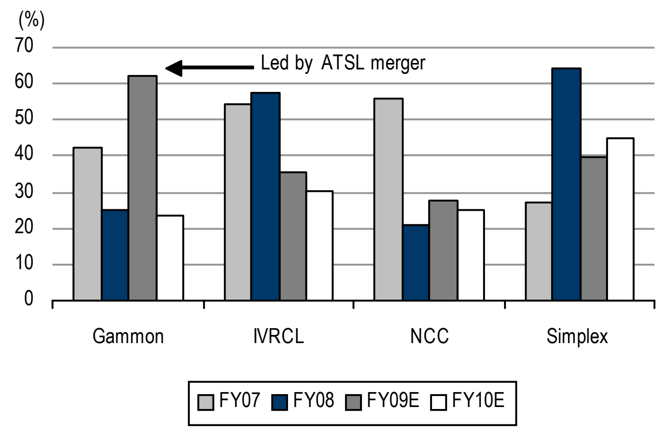
	CMP (Rs)	TP (Rs)	Pot. upside (%)	Rating	Market cap (US$ mn)	P/E (x)*		EV/EBITDA (x) *		ROE (%)		ROCE (%)		EPS (Rs)		EPS CAGR (%) (FY08-10E)
						FY09E	FY10E	FY09E	FY10E	FY09E	FY10E	FY09E	FY10E	FY09E	FY10E	
Gammon	166	174	5	N	317	6.6	6.3	6.4	4.9	10.8	10.1	9.8	9.2	12.4	13.0	9
IVRCL	250	352	41	O	734	9.6	7.2	7.3	6.3	12.6	14.6	10.9	11.6	16.1	21.3	22
NCC	116	145	24	O	585	9.7	8.6	6.4	6.3	10.5	10.8	10.6	10.8	7.5	8.4	8
Simplex	419	545	30	O	457	16.3	9.1	7.5	5.7	14.8	20.5	11.7	14.2	24.7	44.1	55

** Adjusted for BOT and real estate business valuations*

Source: Bloomberg, Company data, Credit Suisse estimates

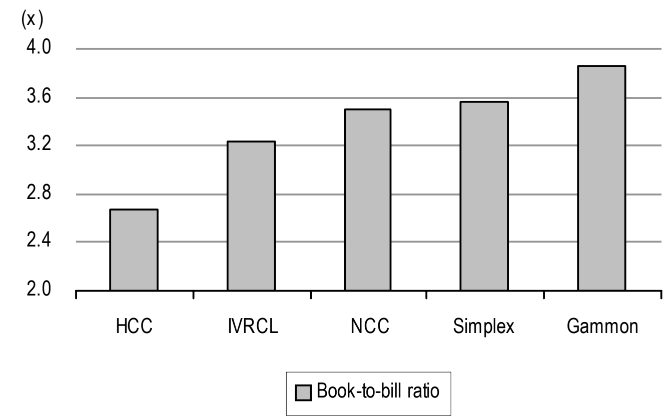
Focus charts

Figure 2: Sales growth to slow, led by execution delays …



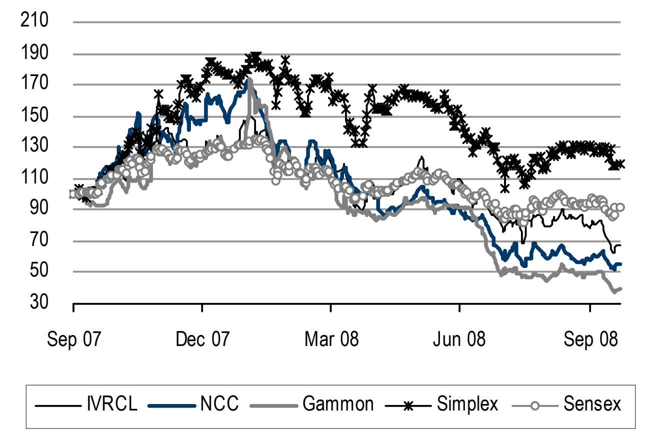
Source: Company data, Credit Suisse estimates

Figure 3: … even though revenue visibility is high



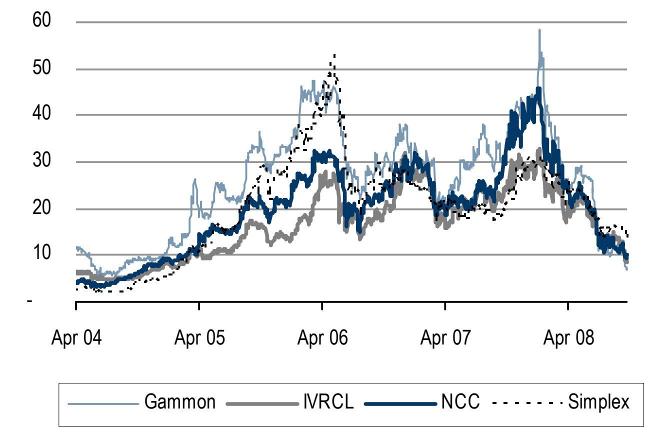
Source: Company data

Figure 4: Stocks have corrected 56-80% from their peaks



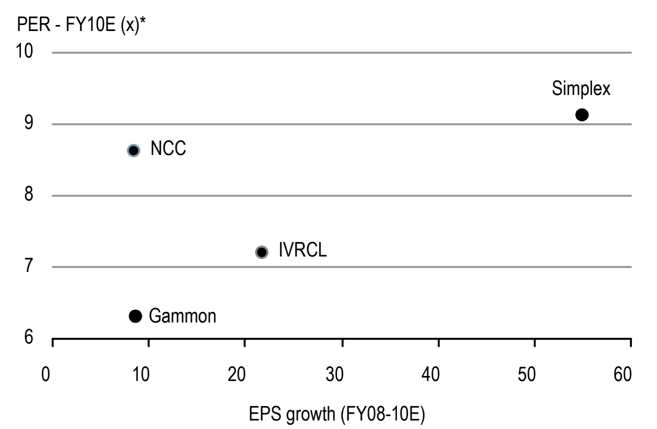
Note: Prices based to 100. Base date: Sept 1, 2007
Source: Bloomberg

Figure 5: One-year forward P/E multiples now attractive



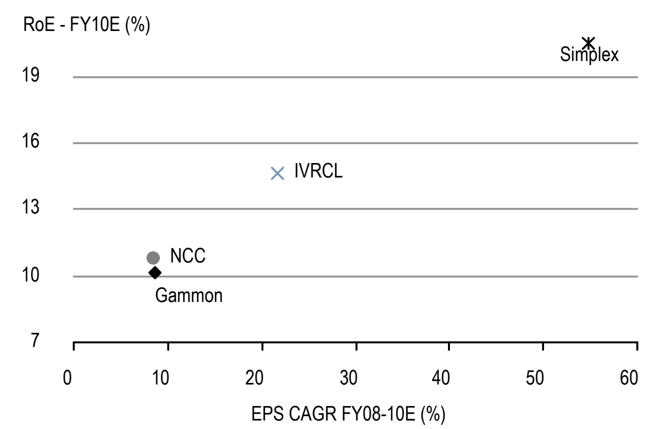
** Note: Adjusted for construction only business*
Source: Bloomberg, Company data, Credit Suisse estimates

Figure 6: Construction – EPS growth versus P/E



** Note: Adjusted for construction only business*
Source: Credit Suisse estimates

Figure 7: Prefer IVRCL & Simplex on EPS growth and ROE



Source: Credit Suisse estimates

Buy in the correction

Concerns not over yet; remain conservative on earnings

We continue to believe that Indian construction players' earnings will be impacted over FY09-10E due to the confluence of: 1) execution delays, 2) margin pressures from high commodity prices, 3) a slowdown in new order flow growth momentum led by imminent elections, delayed projects led by problems in achieving financial closures and a slowdown in government capex led by high inflation, 4) an increase in the cost of borrowings by ~300 bp over the past six months, and 5) rising working capital requirements putting further strain on the cash flows of company business models, which continue to be free cash flow negative.

Execution delays, margin pressures, interest costs and rising working capital needs are the biggest concerns

Led by these factors, we still believe that most construction companies under our coverage might report lower than consensus estimates over the next two to three quarters. Our earnings estimates are 10-20% below consensus estimates over FY09-10E.

Earnings to disappoint vs consensus estimates. Our estimates are 10-20% below consensus for FY09-10E

Stocks have over-reacted; valuations are attractive

Even as we factor in the impact of the above concerns, given that the stocks have fallen 56-80% from their peaks, we believe the concerns are more than discounted in the stock prices. The core construction business valuation is now at 7-9x FY10E EPS and most of the stocks are now trading at significant discounts to their fair values. Moreover, some of the concerns, such as inflation and interest rates, are showing signs of peaking and hence it appears that the worst might be behind them.

Stocks have corrected 56-80% from peaks. Core construction business trading at 7-9x FY10E EPS

Furthermore, steel companies for example have recently announced price cuts of ~5% on the price of steel (constitutes ~20% of sales for a construction company) during September 2008, and the prices are expected to correct further. Besides, according to our cement analyst, cement (~5% of sales) prices in India are likely to fall by ~5% during FY09E led by excess capacity. If commodity prices correct, it would provide a potential for upside risk to our estimates and valuations. We highlight here that valuations of real estate and BOT assets are highly sensitive to interest rates.

Inflation and interest rates seem to be peaking … steel and cement prices to correct … indicating that the worst might be in the past

Upgrade IVRCL and NCC to OUTPERFORM; Gammon to NEUTRAL

We have tweaked our earnings estimates for NCC by 1-4% and IVRCL by 3-5% over FY09-11E to factor in the sustained pressure on the working capital cycle, thereby increasing funding requirements and interest expenses. This would lead to ~2% and ~4% reduction in our target prices for NCC and IVRCL, respectively. For Gammon, we factor in the impact of outgoing interest expenses related to the debt raised for the Italian acquisitions (Sadelmi, Franco Tosi and Sofinter) in consolidated profits versus standalone profits earlier, as the company intends to pay these interest expenses through its overseas subsidiaries through loan support provided from the parent's balance sheet. However, our target price for Gammon remains unchanged. We maintain our estimates and target price for Simplex.

We upgrade IVRCL and NCC to an OUTPERFORM from Neutral and Underperform respectively, given our 12-month SOTP based target price reflects 41% potential upside for IVRCL and 24% potential upside for NCC. Gammon, on the other hand, is now trading at close to our target price; we therefore upgrade it to a NEUTRAL from Underperform. We maintain our OUTPERFORM rating on Simplex. IVRCL and Simplex are our top picks, as they offer: 1) maximum earnings growth over FY08-10E, 2) have relatively resilient business models led by their favourable order book mix, 3) the highest ROE among their peers and 4) attractive valuations.

Valuation snapshots

Figure 8: **Valuation snapshots – coverage universe**

	CMP	TP	Potential upside (%)	Rating	Market cap (US$ mn)	EPS (Rs)		P/E (x)*		EV/EBITDA (x)*		ROE (%)		ROCE (%)	
						FY09E	FY10E	FY09E	FY10E	FY09E	FY10E	FY09E	FY10E	FY09E	FY10E
Gammon India	166	174	5	N	317	12.4	13.0	6.6	6.3	6.4	4.9	10.8	10.1	9.8	9.2
IVRCL	250	352	41	O	734	16.1	21.3	9.6	7.2	7.3	6.3	12.6	14.6	10.9	11.6
NCC	116	145	24	O	585	7.5	8.4	9.7	8.6	6.4	6.3	10.5	10.8	10.6	10.8
Simplex	419	545	30	O	457	24.7	44.1	16.3	9.1	7.5	5.7	14.8	20.5	11.7	14.2

	Sales growth (%)		EBITDA growth (%)		Recurring PAT growth (%)		EPS growth (%)		EPS CAGR (%)	EBITDA margin (%)			Recurring PAT margin (%)		
	FY09E	FY10E	FY09E	FY10E	FY09E	FY10E	FY09E	FY10E	FY08-10E	FY08	FY09E	FY10E	FY08	FY09E	FY10E
Gammon India	62	23	62	22	49	4	13	4	9	9.1	9.1	9.0	4.1	3.7	3.2
IVRCL	35	30	31	37	13	33	11	33	22	9.8	9.5	10.0	5.2	4.3	4.4
NCC	28	25	19	28	5	12	5	12	8	10.4	9.7	9.9	4.7	3.9	3.5
Simplex	40	45	50	55	49	79	34	79	55	9.6	10.3	11.1	3.2	3.5	4.3

	Order inflow (Rs bn)		Order book (Rs bn)		Book-to-bill (x)	Shareholding (%)		Price performance – absolute (%)				Price performance – relative to Sensex (%)			
	FY09E	% growth	FY09E	% growth	FY09E	Non-promoter	FIIs	1M	3M	YTD	12M	1M	3M	YTD	12M
Gammon India	58	118	116	44	3.1	68.9	26.0	(26.6)	(39.6)	(71.1)	(58.7)	(22.2)	(36.0)	(40.3)	(44.6)
IVRCL	96	30	161	39	3.2	90.4	56.8	(22.2)	(27.5)	(54.8)	(39.3)	(17.8)	(23.9)	(24.0)	(25.2)
NCC	68	-11	137	21	3.1	77.5	31.4	(8.2)	(31.6)	(67.3)	(51.5)	(3.9)	(28.0)	(36.5)	(37.4)
Simplex	63	-6	114	27	2.9	50.6	16.3	(9.4)	(12.4)	(33.0)	8.9	(5.1)	(8.8)	(2.3)	(2.3)

	Debt/equity (gross)		Debt/equity (net)		P/B* (x)		EPS (FY09E)		EPS (FY10E)		% chg. in consensus EPS (FY09E)		% chg. in consensus EPS (FY10E)	
	FY09E	FY10E	FY09E	FY10E	FY09E	FY10E	CS	Consensus	CS	Consensus	3M	6M	3M	6M
Gammon India	1.0	0.8	0.9	0.7	0.7	0.6	12.4	13.9	13.0	16.7	(11.5)	(22.5)	(9.1)	(8.1)
IVRCL	0.8	1.0	0.7	0.9	1.1	1.0	16.1	19.3	21.3	25.8	(11.3)	(9.0)	(11.9)	(4.4)
NCC	0.7	1.0	0.6	1.0	1.0	0.9	7.5	8.1	8.4	10.7	(20.1)	(25.4)	(21.4)	(28.0)
Simplex	0.9	1.1	0.8	1.0	2.1	1.7	24.7	28.2	44.1	43.4	(8.5)	(6.2)	(15.0)	(12.1)

** Adjusted for BOT and real estate business valuations*

Source: Datastream, Bloomberg, Company data, Credit Suisse estimates

Concerns not over yet; remain conservative on earnings

We continue to believe that structural problems for construction companies are not over yet. We expect considerable execution delays for new and existing projects, a slowdown in the order book position, margin pressures and a slowdown in government orders on the back of upcoming elections and a deterioration in government finances, to impact the profitability of construction companies for the rest of FY09E (as is reflected in 1Q FY09). However, some of the problems, such as inflation, interest rates and commodity prices, are showing signs of peaking and hence it appears that the worst might be behind.

Execution delays still a key risk in our view; our numbers factor in a considerable slowdown in revenues …

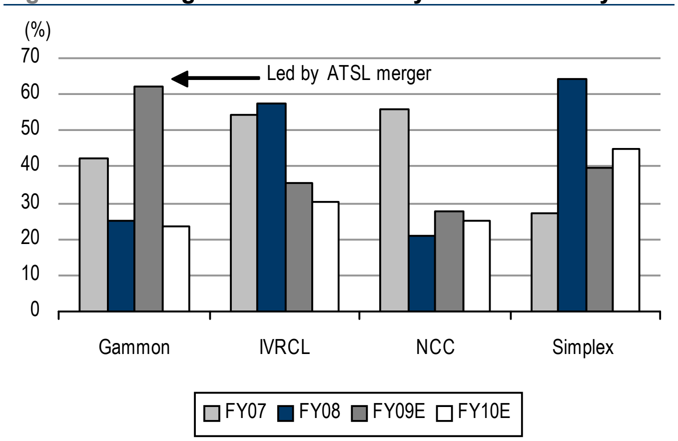
Projects to face execution delays led by several factors

We expect projects to face execution delays, led by a variety of reasons, such as: 1) problems with projects achieving financial closure, 2) project work being suspended for the delayed payments, 3) litigations relating to the fairness of the project awards, 4) arbitration relating to cost and time overruns, 5) projects getting postponed given the cost overruns led by high commodity prices and interest rates, 6) land acquisition problems and 7) delays in obtaining the necessary clearances.

We factor in execution delays in our sales estimates

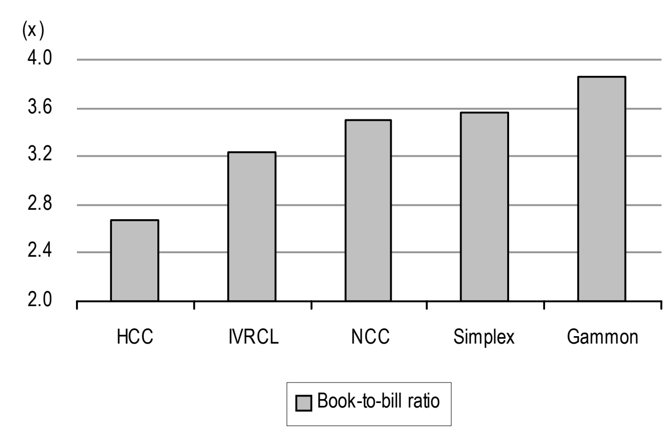
This would, in turn, lead to a slowdown in the award of new orders, as well as impact the potential of translating the existing order book into revenues. We have conservatively factored this into our estimates by: 1) slowing the new order flow momentum, 2) delaying the execution of projects by six to 12 months and 3) discarding the projects with limited visibility arising from litigations, suspensions, etc. Led by these factors, we believe that the construction companies' sales growth would witness a slowdown even as their current order books provide strong revenue visibility.

Figure 9: **Sales growth to slow led by execution delays …**



Source: Company data, Credit Suisse estimates

Figure 10: **… even as revenue visibility is high**



Source: Company data

We cite a few of the many examples of recently delayed projects:

- Projects, such as the Machilipatnam port, have been delayed as it is difficult to achieve financial closure for this project in the current high interest rate environment.
- Of the 60 national highway projects invited for the first round of bidding (RFQ stage) during YTD CY08, only four projects have moved to the second stage of bidding (RFP stage) and only one project has been awarded so far. Most of the other projects have been delayed, as the non short-listed bidders have contested the selection procedure.

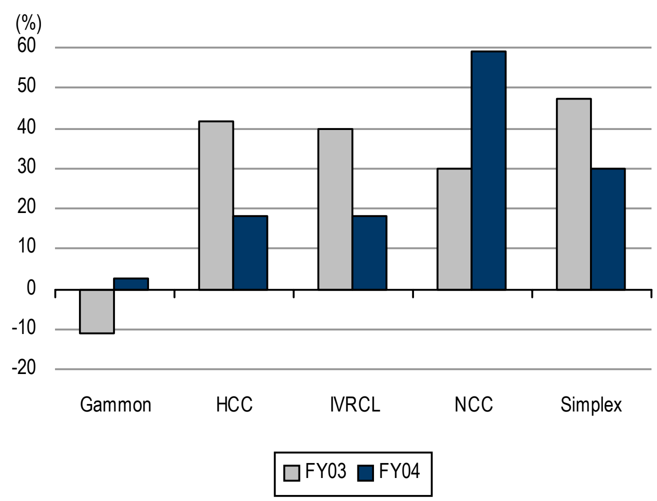
- The project to set up a Rs13 bn new container handling terminal at Ennore Port near Chennai is likely to be delayed, as DP World and PSA International, two of the world's top container terminal operators, are planning to approach the courts to challenge the short-listing procedure, given that they were not short-listed amongst the maximum six bidders permissible under the new model concession agreement.
- According to new eligibility criteria, infrastructure companies are prevented from participating in bids if they have already been shortlisted in eight projects in the past two months. Citing this, some companies may have to withdraw from national highway projects for which they have already been short listed.
- According to an article in the DNA on 19 September 2008, HCC (HCNS.BO, Rs88.2, Not rated) expects its projects to be delayed on account of the insurgency in Assam.
- Several highway projects have been delayed, as NHAI has been unable to acquire the requisite land for the projects.

… and also a considerable slowdown in new order flows growth

We expect a slowdown in the new order flows growth momentum for companies under our coverage led by:

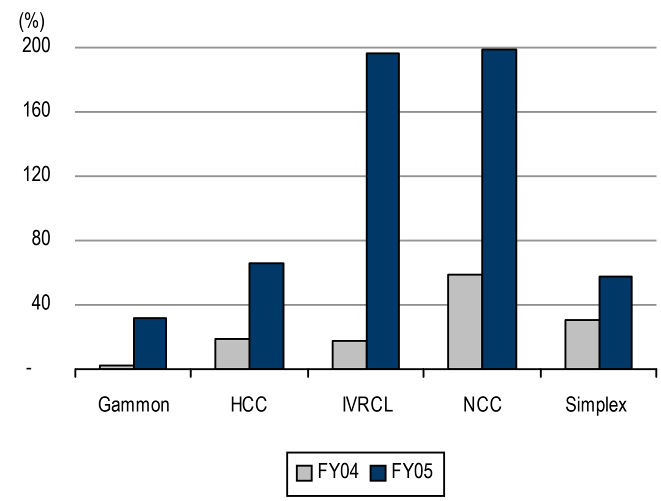
- **Imminent elections.** The India Election Commission's code of conduct mentions that from the time the elections are announced to the conclusion of the elections, the incumbent government cannot make any new promises, including spending on infrastructure developments. India is expected to hold general elections in May 2009 (but could be earlier), whereas the state-level elections are scheduled for CY08-09.

Figure 11: **Order inflow growth slows prior to elections …**



Source: Company data

Figure 12: **… though it spikes post-elections**



Source: Company data

- **Delays in achieving financial closures.** Led by the high cost of borrowing and the inability to access capital markets for fund raising; the costs of financing certain infrastructure projects have risen more than the returns expected to be earned from these projects, leading to problems in achieving financial closure and thereby delays.
- **Slowdown in government capex led by high inflation.** Led by high inflation, which puts a strain on government finances, we expect the government's ability to finance infrastructure projects over the next 12-18 months to be impacted, as resources are diverted towards inflation control. This may lead the government to curtail/defer infrastructure investments in the medium term.

Figure 13: **Expect slowdown in order inflow growth momentum over FY09-10E**

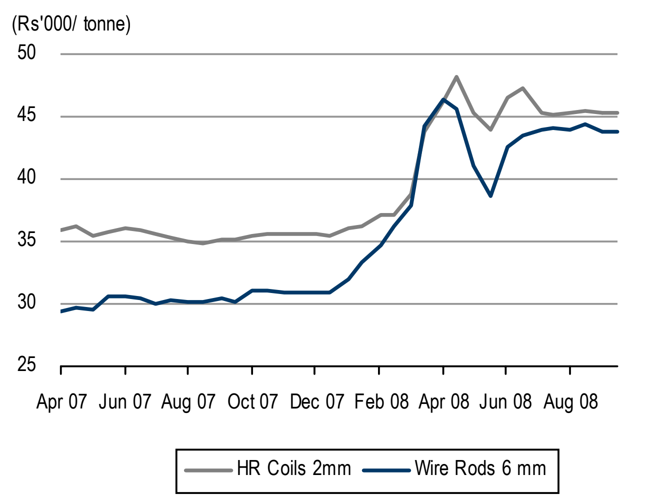
Company	FY08 (%)	FY09E (%)	FY10E (%)
Gammon	-15	118	6
IVRCL	64	30	9
NCC	61	-11	34
Simplex	163	-6	22

Source: Company data, Credit Suisse estimates

We factor in subdued margins for the rest of FY09E

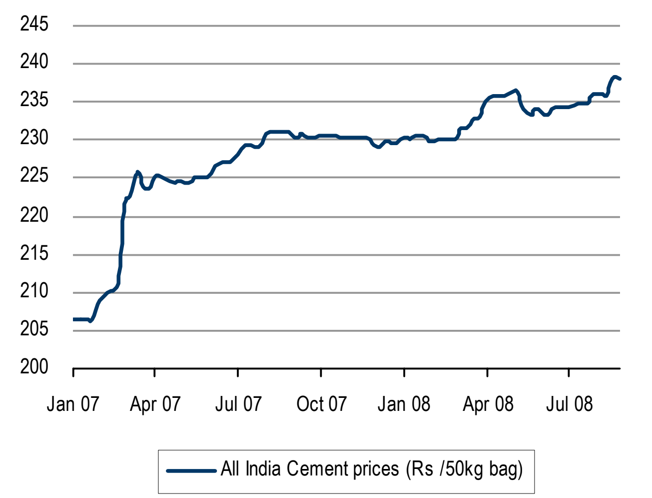
Led by the steep rise in the prices of key commodities, such as steel, cement bitumen and diesel, during YTD CY08, construction companies margins were impacted during 1Q FY09. Prices have continued to remain high (until recently, steel companies have announced a cut in steel prices by ~5%) and considering that most of the construction companies maintain around two months of inventories, we believe, it would impact the construction companies margins during most of FY09E; given that they had not anticipated such high commodity prices when bidding for contracts.

Figure 14: **Steel prices have risen sharply YTD CY08 …**



Source: Cris Infac

Figure 15: **… cement prices have also risen**

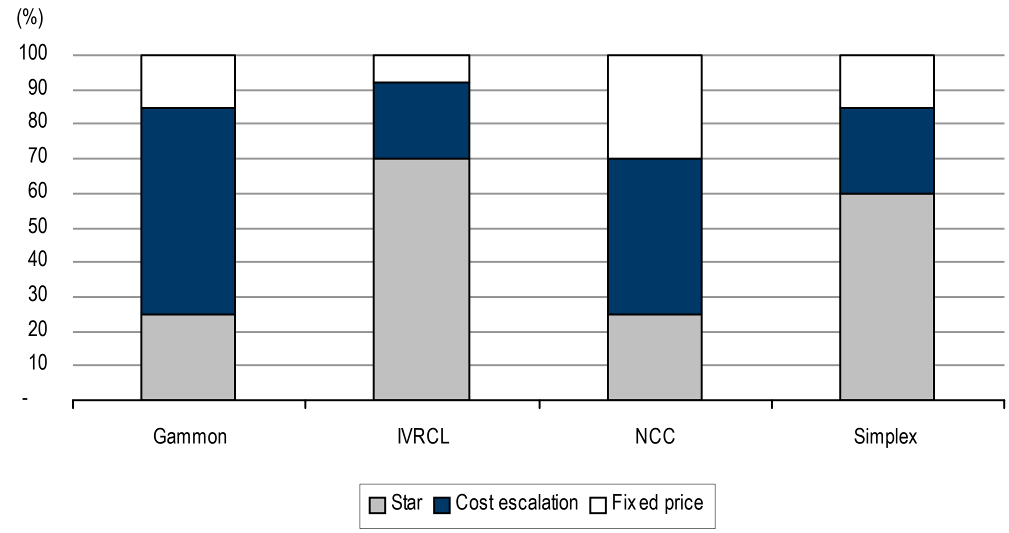


Source: CMA

Simplex & IVRCL have the most favourable order book mix

Led by this, we expect the FY09E EBITDA margins of most of the construction companies to come under pressure, with the impact being more severe in the case of players with a high proportion of fixed price and inflation index-linked (not all cost increases can be passed on) contracts in their order books, such as NCC and Gammon. However, Gammon's EBITDA margins would get a cushion during FY09E, led by the merger of relatively high margin ATSL with itself (merger effective April 2008), as discussed in our report *Near-term Concerns Galore,* dated 9 September 2008.

Figure 16: Order book mix – favourable for IVRCL and Simplex



Source: Company data

On the other hand, operating margins during FY09E for IVRCL and Simplex are expected to be the least impacted, given the high proportion of Star rated contracts (complete pass-through of raw material cost increases) in their order books.

Figure 17: EBITDA margins to come under pressure during FY09E (ex-Simplex)

Company	FY08 (%)	FY09E (%)	FY10E (%)	FY11E (%)
Gammon	9.1	9.1	9.0	9.2
IVRCL	9.8	9.5	10.0	10.2
NCC	10.4	9.7	9.9	10.5
Simplex	9.6	10.3	11.1	11.4

Source: Company data, Credit Suisse estimates

We also factor in higher borrowing costs that would considerably dampen profitability

The cost of borrowing for construction companies has risen by ~300 bp over the past six months to upwards of 12.5%. We have already factored in the cost of borrowing at ~13% for companies under our coverage during FY09E and ~12-12.5% over FY10-11E. According to our strategist, interest rates are unlikely to rise further. Our sensitivity analysis suggests a change of 3-7% on construction business earnings over FY09-11E for every 100 bp change in interest rates.

Our sensitivity suggests a change of 3-7% on construction EPS for 100 bp change in interest rates

Figure 18: Sensitivity of changes in interest rates by 100 bp – construction business EPS

	FY09E (%)	FY10E (%)	FY11E (%)
Gammon	4.3	6.7	6.5
IVRCL	3.9	4.2	4.3
NCC	4.0	5.6	4.7
Simplex	4.2	3.3	3.5

Source: Credit Suisse estimates

Given that most of the companies have raised equity financing during FY06-08, they would mostly fund their financing requirements through leverage over the next two years. The increased need for debt financing and high interest rates would put pressure on construction earnings. Led by this, we expect net interest expenses for companies under our coverage to increase more than proportionately to the growth of their operating profits.

We expect companies to fund all the financing requirements through debt over FY08-11E (ex promoter warrants at Simplex)

Figure 19: **Interest expenses expected to rise faster than EBIT (ex. Simplex)**

(%)	FY08	FY09E	FY10E	FY11E
Gammon				
EBIT growth	11.4	70.1	24.0	28.8
PBT growth	8.3	43.5	4.5	25.3
IVRCL				
EBIT growth	56.3	29.0	36.5	38.4
PBT growth	56.5	13.0	32.7	35.4
NCC				
EBIT growth	29.9	18.9	30.6	36.2
PBT growth	27.5	6.4	11.9	43.0
Simplex				
EBIT growth	67.1	50.4	65.3	33.8
PBT growth	85.8	59.3	78.7	36.2

Source: Company data, Credit Suisse estimates

Rising working capital requirements to insert further strain on cash flows …

Rising working capital cycle to further strain cash flows. Businesses are already free cash flow negative

Construction is a free cash flow negative business for all companies in our coverage, led by high working capital requirements leading to negative cash flows from operations. Also, these companies continuously incur capex towards equipment in order to service their growing order books. Besides, most construction companies have diversified into infrastructure and/or real estate development business, which require equity investments and support in terms of loans from the parent's balance sheet. We expect the working capital cycle/requirements to increase led by: 1) a rising debtor cycle, 2) a shortening of credit available from the vendors and 3) increased support to real estate/BOT subsidiaries. A rise in the working capital cycle would in turn increase the requirements for debt financing, inserting a strain on cash flows and profitability.

… however, companies in our universe are well funded

Given the free cash flow negative nature of the business, construction companies frequently have to access the equity markets for fund-raising in order to finance their expansion plans and to augment their net worth – one of the pre-qualifications for large projects. However, we note that most of the construction companies in our universe have raised equity funding over the past couple of years and are moderately leveraged.

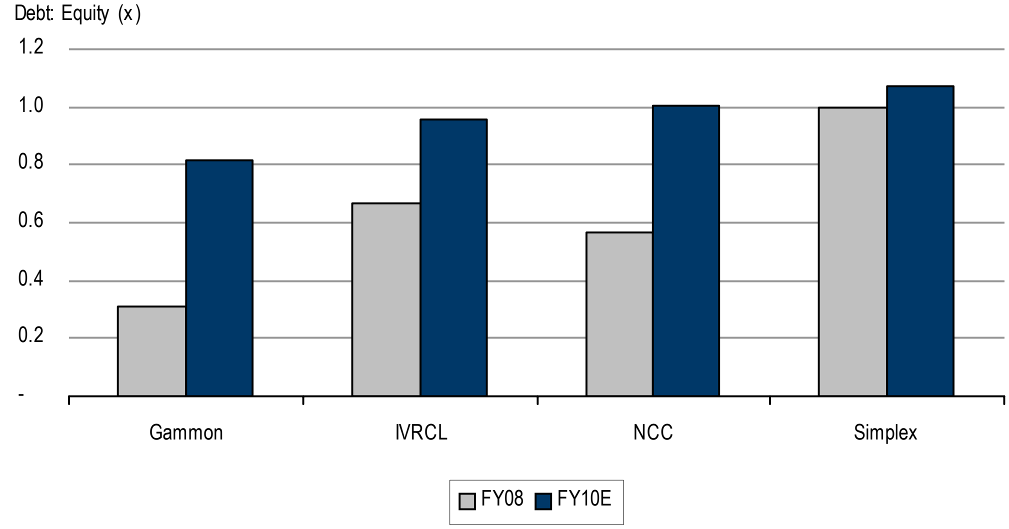
Figure 20: **Companies have raised equity funds over FY06-08**

	Period	Funds raised (Rs mn)
Gammon		**4,435**
GDR	FY06	4,435
IVRCL		**5,550**
QIP	FY07	5,550
NCC		**9,576**
GDR	FY06	5,476
QIP	FY08	4,100
Simplex		**7,139**
QIP	FY06	933
QIP	FY08	4,000
Promoter warrants	FY09E	2,206

Source: Company data, Credit Suisse estimates

Their FY08 debt-to-equity is at 0.3-1.0x and is likely to increase to 0.8-1.1x, assuming that all the financing requirements (post cash flow from operations) over FY08-10E would be funded through debt. Construction companies' can typically leverage their balance sheet to 2.5x their net worth and are therefore in a comfortable position to meet their financing requirements in order to service growth for the next two to three years.

Figure 21: **Companies are in comfortable position to raise leverage**



Source: Company data, Credit Suisse estimates

Construction is a high operating leverage business

Construction is a high operating leverage and fairly competitive business. We have factored in conservative estimates for: 1) new order flows, 2) sales led by execution delays 3) margin pressures from high commodity prices and 4) high interest rates. However, led by limited opportunities to expand margins and rising fixed costs from ongoing capex, and the rising cost of borrowings and funding needs, any disappointment in sales or expected margins could have a severe impact on profitability. Our sensitivity analysis suggests an impact of 10-15% on EPS led by a 5% disappointment in sales, and 15-20% from EBITDA margins disappointing by 100 bp.

Our sensitivity suggests an impact of 10-15% on construction EPS led by a 5% disappointment in sales, and 15-20% from EBITDA margins disappointing by 100 bp

Figure 22: **Impact on EPS from a 5% disappointment in sales**

(%)	FY09E	FY10E	FY11E
Gammon	-9.8	-11.5	-11.5
IVRCL	-11.8	-11.7	-11.6
NCC	-13.3	-14.9	-13.6
Simplex	-14.3	-11.9	-11.4

Source: Credit Suisse estimates

Figure 23: **Impact on EPS from 100 bp disappointment in EBITDA margin**

(%)	FY09E	FY10E	FY11E
Gammon	-17.6	-20.8	-20.6
IVRCL	-15.2	-14.9	-14.7
NCC	-17.0	-19.1	-16.8
Simplex	-19.1	-15.5	-14.6

Source: Credit Suisse estimates

Expect earnings 10-20% below consensus estimates

Led by these factors, we believe that most construction companies under our coverage would report disappointing results, compared to consensus estimates over the next two to three quarters. Our earnings estimates are 10-20% below consensus estimates over FY09-10E.

Figure 24: **EPS estimates – Credit Suisse versus Consensus**

	FY09E			FY10E		
Company	**CS (Rs)**	**Consensus (Rs)**	**% difference**	**CS (Rs)**	**Consensus (Rs)**	**% difference**
Gammon	12.4	13.9	-11	13.0	16.7	-22
IVRCL	16.1	19.3	-17	21.3	25.8	-17
NCC	7.5	8.1	-7	8.4	10.7	-21
Simplex	24.7	28.2	-13	44.1	43.4	2

Source: Bloomberg, Credit Suisse estimates

Commodity prices to soften near term; interest rates showing signs of peaking

Steel companies have announced a steel price cut of ~5% (constitutes ~20% of sales for a construction company) during September 2008, and the prices are expected to correct further. Besides, according to our cement analyst, cement (~5% of sales) prices in India are likely to fall by ~5% during FY09E led by excess capacity. If the prices of commodities correct, it would provide a potential for upside risk to our estimates.

If commodities prices correct, it would provide a potential for upside risk to our estimates

BOT/real estate project valuations have a high sensitivity to interest rates …

High interest rates have impacted the net present value of the BOT portfolios and real estate businesses of the construction companies. BOT/real estate valuations are highly sensitive to interest rates. On the one hand, rising interest expenses have increased project costs for projects under execution as these expenses are capitalised, while on the other, it increases the cost of discounting for these projects, leading to a fall in the net present values and the IRRs for the projects. However, this argument gets reversed in a falling interest rate scenario.

Besides, most of the infrastructure projects, such as toll roads, merchant power plants, airports and ports, have revenues linked to inflation. Therefore, the impact of the increase in interest rates is, to a great extent, passed on by higher revenues. Our sensitivity analysis suggests a change of 8-10% in the net present values of infrastructure BOT projects and ~5% for the real estate business for every 100 bp change in interest rates for companies in our coverage universe.

BOT assets are highly sensitive to interest rates…would benefit if interest rates were to fall

Figure 25: **Sensitivity of increase in interest rates by 100 bp – infrastructure assets' NPV**

Impact on account of	Annuity road (%)	Toll road (%)	Port (%)	Power plant (%)
Increase in interest expenses	-3.1	-4.0	-3.6	-3.3
Increase in cost of equity	-6.8	-8.8	-8.6	-8.6
Increase in inflation	n.a.	4.5	3.8	4.0
Net change	**-9.9**	**-8.3**	**-8.4**	**-7.9**

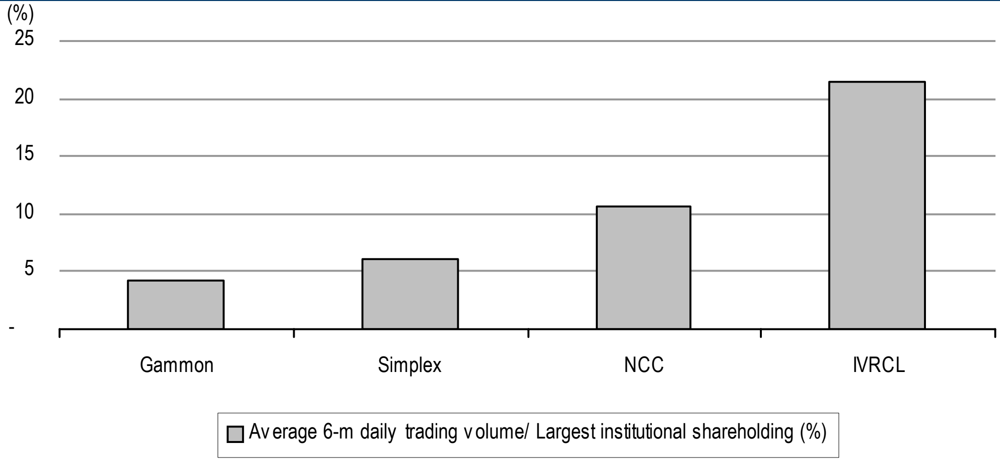
Source: Credit Suisse estimates

If the interest rates soften from the current levels, this would not only improve the valuations of these projects but would also aid in the projects achieving financial closure faster than expected as the viability of these projects would improve. However, we are not factoring in these upsides in our estimates currently.

Stock liquidity could be a key issue for certain stocks

Given the current market environment, we observe that a lack of adequate liquidity could be a key risk for the stock. We calculate the six-month average daily trading volume as a proportion to the largest institutional shareholding for companies under our coverage to ascertain stocks at maximum risk from this standpoint.

Figure 26: **IVRCL followed by NCC offers the maximum liquidity**

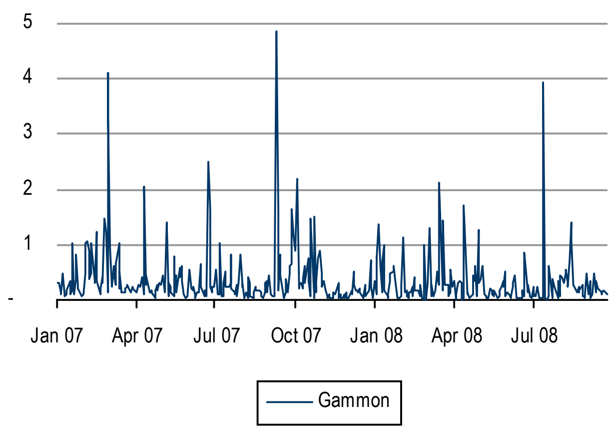


Source: Bloomberg, Company data

Simplex is the most thinly traded stock in our coverage

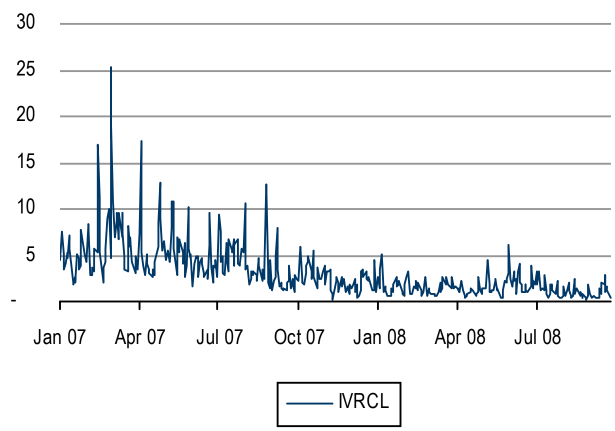
Liquidity for construction stocks has remained mostly weak. Daily trading volumes have fallen for most stocks under our coverage. IVRCL and NCC offer relatively better liquidity.

Figure 27: **Average daily trading volume – Gammon**



Source: Bloomberg

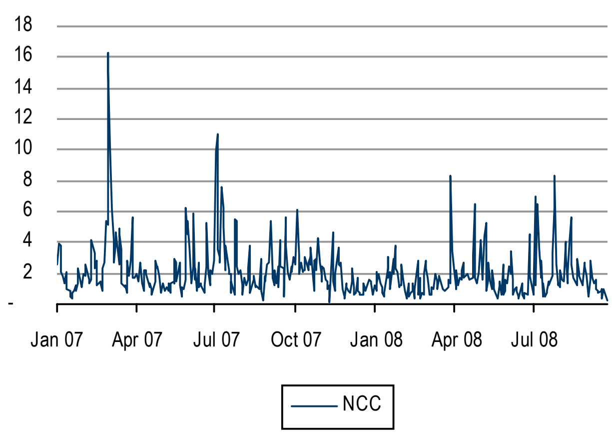
Figure 28: **Average daily trading volume – IVRCL**



Source: Bloomberg

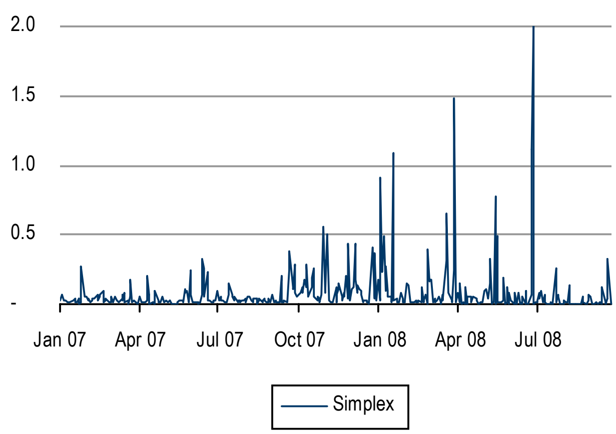
Simplex is the most thinly traded stock; while volumes for IVRCL have fallen significantly.

Figure 29: **Average daily trading volume – NCC**



Source: Bloomberg

Figure 30: **Average daily trading volume – Simplex**



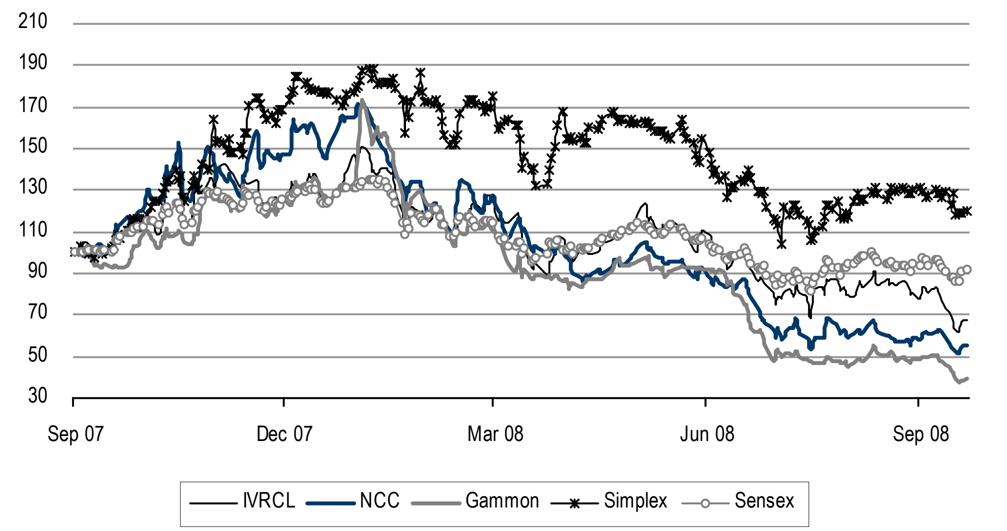
Source: Bloomberg

Stocks have over-reacted; valuations are now very attractive

Even as we factor in the impact of the above concerns, we believe that with the stocks having fallen 56-80% from their peaks, the concerns are more than discounted in the stock prices. Construction stocks under our coverage have underperformed versus the Sensex since April 2008 (excluding Simplex).

Stocks have corrected 56-80% from their peaks

Figure 31: Stocks have underperformed versus Sensex since April 2008 (ex-Simplex)



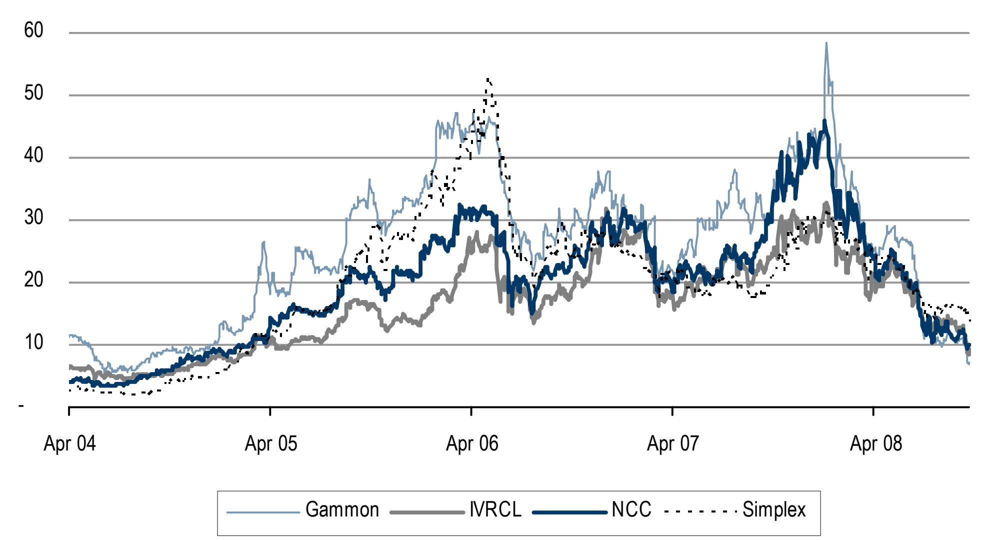
Note: Prices based to 100. Base date: 1 September 2007

Source: Bloomberg

The core construction business valuation is now at 7-9x FY10E EPS, considerably lower than their peak valuations earlier. Most of the stocks are now trading at a significant discount to their fair values.

Core construction business valuation at 7-9x FY10E EPS

Figure 32: Construction – one-year forward P/E



Note: Adjusted for construction only business

Source: Bloomberg, Company data, Credit Suisse estimates

Figure 33: **Construction sector – snapshot**

Company	CMP	TP	Potential upside (%)	Rating	Market cap (US$ mn)	EPS (Rs) FY09E	EPS (Rs) FY10E	EPS CAGR (%) FY08-10E
Gammon	166	174	5	N	317	12.4	13.0	9
IVRCL	250	352	41	O	734	16.1	21.3	22
NCC	116	145	24	O	585	7.5	8.4	8
Simplex	419	545	30	O	457	24.7	44.1	55

Source: Bloomberg, Company data, Credit Suisse estimates

Figure 34: **Stock valuations are now attractive**

Company	P/E (x) FY09E	P/E (x) FY10E	EV/EBITDA (x) FY09E	EV/EBITDA (x) FY10E	P/E (x)* FY09E	P/E (x)* FY10E	EV/EBITDA (x)* FY09E	EV/EBITDA (x)* FY10E
Gammon	13.4	12.8	9.2	7.2	6.6	6.3	6.4	4.9
IVRCL	15.6	11.7	10.0	8.3	9.6	7.2	7.3	6.3
NCC	15.5	13.8	8.7	8.2	9.7	8.6	6.4	6.3
Simplex	17.0	9.5	7.7	5.8	16.3	9.1	7.5	5.7

** Valuations adjusted for core construction business only (Ex-infrastructure BOT and real estate assets)*

Source: Company data, Credit Suisse estimates

Upgrade IVRCL and NCC to OUTPERFORM; Gammon to NEUTRAL

We have tweaked our earnings estimates for NCC by ~1-4% over FY09-11E to factor in the sustained pressure on the working capital cycle, thereby increasing the funding requirements and interest expenses. This would lead to ~2% reduction in our target price for the stock at Rs145 (Rs148 earlier).

Figure 35: **NCC – estimates change summary**

(Rs mn)	Earlier	Now	Change (%)
Sales			
FY09E	44,419	44,419	0.0
FY10E	55,641	55,641	0.0
FY11E	70,144	70,144	0.0
EBITDA			
FY09E	4,287	4,287	0.0
FY10E	5,493	5,493	0.0
FY11E	7,400	7,400	0.0
Recurring PAT			
FY09E	1,791	1,722	-3.9
FY10E	2,009	1,927	-4.1
FY11E	2,794	2,756	-1.3
EPS			
FY09E	7.8	7.5	-3.9
FY10E	8.8	8.4	-4.1
FY11E	12.2	12.0	-1.3

Source: Credit Suisse estimates

We had earlier estimated the interest expenses outgoings related to the debt raised for the Italian acquisitions (Sadelmi, Franco Tosi and Sofinter) from the standalone financials of Gammon India, given the company's recourse to these debts. However, the company intends to provide loans from the standalone balance sheet to the debt raising overseas subsidiaries to the extent of these interest expenses. The standalone profitability would therefore not be impacted on account of these interest expenses; however, they would be reflected in the company's consolidated profitability.

However, for valuation purposes, we continue to value Gammon's construction business net of the impact of Gammon's share of profits in Sadelmi, Franco Tosi and Sofinter, and the impact of interest expenses emanating from their acquisition debt; implying no change to our valuation.

Figure 36: **Calculation of Gammon's PAT used for the valuation of its construction business**

(Rs mn)	FY10E
Core construction PAT including ATSL	**1,482**
Add: Gammon's share of profits	**181**
– Sadelmi	64
– Franco Tosi	51
– Sofinter	66
PAT including share of profits from Italian acquisitions	**1,664**
Less: interest on acquisition debt	(523)
PAT used for valuation of construction business	**1,141**

Source: Company data, Credit Suisse estimates

We have tweaked our earnings estimates for IVRCL by 3-5% over FY09-11E to factor in the sustained pressure on the working capital cycle, thereby increasing the funding requirements and interest expenses. This would lead to ~4% reduction in our target price for the stock at Rs352 (Rs365 earlier).

Figure 37: IVRCL – estimates change summary

(Rs mn)	Old	New	% change
Sales			
FY09E	50,040	50,040	0.0
FY10E	65,192	65,192	0.0
FY11E	87,001	87,001	0.0
EBITDA			
FY09E	4,752	4,752	0.0
FY10E	6,487	6,487	0.0
FY11E	8,913	8,913	0.0
Recurring PAT			
FY09E	2,234	2,174	-2.7
FY10E	3,034	2,884	-5.0
FY11E	4,110	3,906	-5.0
EPS (Rs)			
FY09E	16.5	16.1	-2.7
FY10E	22.4	21.3	-5.0
FY11E	30.4	28.9	-5.0

Source: Company data, Credit Suisse estimates

We upgrade IVRCL and NCC to an OUTPERFORM from Neutral and Underperform, respectively, given our 12-month SOTP-based target price reflects 41% potential upside for IVRCL and 24% potential upside for NCC from their current market prices.

Figure 38: Upgrade IVRCL and NCC to OUTPERFORM; Gammon to NEUTRAL

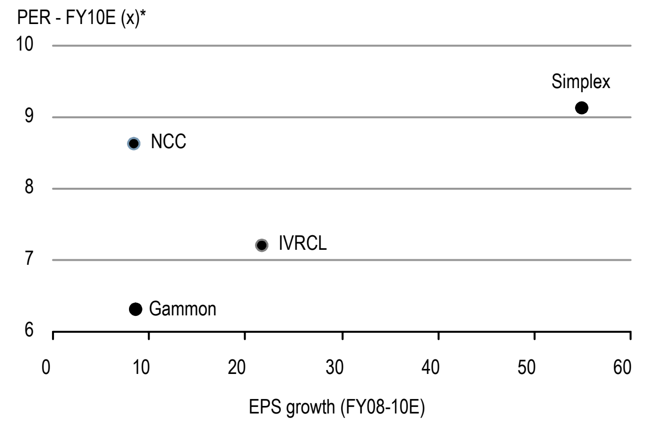
	CMP (Rs)	Earlier TP (Rs)	Revised TP (Rs)	Potential upside (%)	Earlier rating	Revised rating
Gammon India	166	174	174	5	U	N
IVRCL	250	365	352	41	N	O
NCC	116	148	145	24	U	O
Simplex	419	545	545	30	O	O

Source: Bloomberg, Credit Suisse estimates

Gammon, on the other hand is now trading at close to our target price; hence we upgrade Gammon to a NEUTRAL from Underperform. We maintain our OUTPERFORM on Simplex.

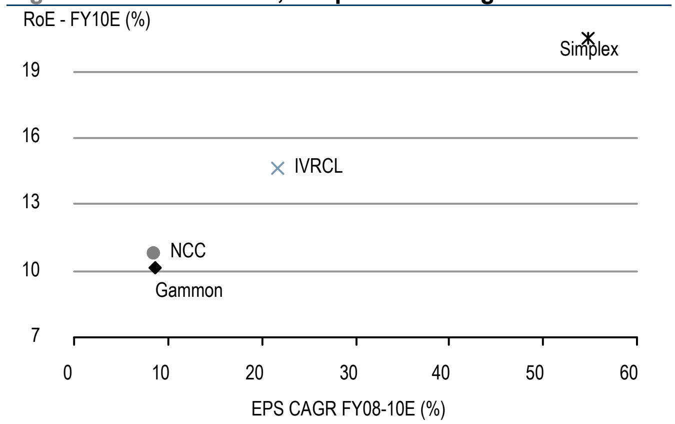
We recommend IVRCL and Simplex as our top picks, given these stocks offer: 1) relatively high earnings growth over FY08-10E, 2) resilient business models led by their favourable order book mix, 3) the highest ROE among its peers and 4) attractive valuations.

Figure 39: Construction – EPS growth vs P/E



Note: Adjusted for construction only business
Source: Company data, Credit Suisse estimates

Figure 40: Prefer IVRCL, Simplex on EPS growth and ROE



Source: Company data, Credit Suisse estimates

Key investment risks

Risk of change in government regulations

There is a risk that the government could change certain regulations for the construction sector. A case in point is the withdrawal of the 80-IA tax benefits for contractors in the Union Budget 2007. However, we believe the government is not likely to enact unfavourable regulations for the sector, given its importance to the economy – the construction sector contributes 7.3% of GDP.

Competition

Competition in the construction and infrastructure businesses has intensified. With the new model concession agreement favouring five to six bidders and project sizes increasing, this could lead to the entry of foreign players as well as large domestic players that are currently not related to the construction business.

Slowdown in government capex/economy

Inflationary pressures deteriorating government finances and political risk led by the imminent elections could lead to a significant slowdown in government capex/economy. Given that the government implements most of the infrastructure investments, it could slow down order inflows.

Shortage of manpower

A shortage of skilled manpower is a key threat to the industry as a whole. We have built in reasonable increases in employee costs for our coverage universe. However, we do not rule out the possibility of manpower shortages, leading to time and cost overruns for projects.

Pre-election ordering

We have factored in a slowdown in order inflow growth during FY09-10E. However, generally the incumbent government expedites the awarding of infrastructure projects prior to election announcements, as these are good election talking points. This would overturn our argument of a slowdown in revenues for these companies.

Valuation upside not captured in our assumptions

We have not yet factored in the value of IVRCL's stake in the oil and gas assets, resulting from the acquisition of Alkor Petroo, and the value of about 10 mn sq ft of saleable development at IVR Prime. Similarly, we have not ascribed any value to NCC's entitlement to develop land at the Machilipatnam port (6,200 acres, as per the company), its two airport BOT projects in Karnataka, the Gautami power project, real estate development upside from its landbank or the Jubilee Hills project, as we believe that these projects are in their very early stages.

Real estate valuations

We have used conservative assumptions in our estimates, based on the current situation of the real estate market in India. However, there is a possibility of the company realising much higher valuations for its properties or financial investors valuing the properties at a significant premium to our estimates.

Benefits under 80-IA being allowed

We have assumed no tax benefits under Section 80-IA deduction for companies under our coverage. Various construction companies have appealed to the authorities to challenge the reversal of the deduction and the interpretation of the amended section. The allowance of this benefit, or partial concessions, could increase our earnings estimates by about 12%.

Other risks

Political risk, traffic/revenue risk for BOT projects, the risk of equity dilution.

Financial summary

Gammon India

Figure 41: **Gammon – profit and loss summary (standalone financials)**

Year-end 31 Mar (Rs mn)	FY07	FY08	FY09E	FY10E	FY11E
Sales	**18,647**	**23,336**	**37,868**	**46,721**	**57,885**
– Core construction	*18,647*	*23,336*	*28,368*	*35,131*	*42,321*
– ATSL	-	-	*9,500*	*11,590*	*15,564*
Total operating expenses	(16,795)	(21,204)	(34,413)	(42,501)	(52,565)
EBITDA	**1,852**	**2,133**	**3,454**	**4,220**	**5,320**
– Core construction	*1,852*	*2,133*	*2,195*	*2,887*	*3,608*
– ATSL	*n.a.*	*n.a.*	*1,259*	*1,333*	*1,712*
Depreciation	(352)	(462)	(613)	(697)	(783)
EBIT	**1,500**	**1,671**	**2,841**	**3,523**	**4,537**
Net interest expenses	(117)	(173)	(692)	(1,277)	(1,723)
PBT	**1,383**	**1,498**	**2,149**	**2,246**	**2,814**
Total tax	(438)	(546)	(731)	(764)	(957)
Recurring PAT	**946**	**952**	**1,419**	**1,482**	**1,857**
– Core construction	*946*	*952*	*948*	*994*	*1,228*
– ATSL	*n.a.*	*n.a.*	*470*	*488*	*630*
Exceptional	(501)	(91)	308	-	-
Reported PAT	**445**	**861**	**1,727**	**1,482**	**1,857**

Source: Company data, Credit Suisse estimates

Figure 42: **Gammon – balance sheet summary (standalone financials)**

Year-end 31 Mar (Rs mn)	FY07	FY08	FY09E	FY10E	FY11E
Share capital	177	177	229	229	229
Reserves and surplus	11,326	12,110	13,736	15,131	16,880
Total net worth	**11,503**	**12,287**	**13,965**	**15,360**	**17,109**
Total loans	3,715	3,771	13,721	12,521	20,021
Deferred tax liability	379	372	372	372	372
Total liabilities and net worth	**15,597**	**16,429**	**28,057**	**28,252**	**37,501**
Gross block	8,962	10,268	14,249	16,729	19,689
CWIP	104	182	182	182	182
Net fixed assets	**7,015**	**7,915**	**10,702**	**12,485**	**14,662**
Investments	1,504	1,608	1,649	1,749	1,849
Inventories	5,290	7,050	11,522	12,525	16,628
Debtors	3,034	5,172	8,300	9,600	11,894
Cash and bank balances	960	381	756	909	1,097
Loans and advances	5,457	4,994	8,818	9,600	13,004
Other current assets	64	79	104	128	159
Total current assets	**14,804**	**17,675**	**29,500**	**32,762**	**42,782**
Current liabilities	6,571	9,043	11,522	15,941	18,319
Provisions	1,156	1,725	2,272	2,803	3,473
Total current liabilities and provisions	**7,727**	**10,768**	**13,794**	**18,744**	**21,792**
Net current assets	**7,078**	**6,907**	**15,706**	**14,019**	**20,990**
Total assets	**15,597**	**16,429**	**28,057**	**28,252**	**37,501**

Source: Company data, Credit Suisse estimates

Figure 43: **Gammon – cash flow statement (standalone financials)**

Year-end 31 Mar (Rs mn)	FY07	FY08	FY09E	FY10E	FY11E
PBT	1,383	1,498	2,149	2,246	2,814
Tax paid	(438)	(546)	(731)	(764)	(957)
Change in deferred tax liability	34	(8)	-	-	-
Add: depreciation	352	462	613	697	783
Change in working capital	**(1,083)**	**(408)**	**(8,424)**	**1,840**	**(6,784)**
Cash flow from operations	**249**	**999**	**(6,393)**	**4,020**	**(4,143)**
Extra-ordinary income/(expenses)	(501)	(91)	308	-	-
Capex	(4,270)	(1,362)	(3,401)	(2,480)	(2,960)
Change in investments	(343)	(103)	(41)	(100)	(100)
Others	-	-	-	-	-
Cash flow from investing activities	**(5,113)**	**(1,556)**	**(3,133)**	**(2,580)**	**(3,060)**
Change in debt	2,009	56	9,950	(1,200)	7,500
Change in equity	(0)	-	52	-	-
Change in reserves	2,523	(27)	(0)	-	0
Dividend and dividend tax	(50)	(51)	(101)	(87)	(109)
Cash flow from financing activities	**4,482**	**(22)**	**9,901**	**(1,287)**	**7,391**
Increase/(decrease) in cash	**(383)**	**(579)**	**375**	**153**	**188**
Opening cash and bank balance	1,343	960	381	756	909
Closing cash and bank balance	**960**	**381**	**756**	**909**	**1,097**

Source: Company data, Credit Suisse estimates

Figure 44: **Gammon – key ratios (standalone financials)**

Year-end 31 Mar (%)	FY07	FY08	FY09E	FY10E	FY11E
Sales growth	42	25	62	23	24
EBITDA growth	20	15	62	22	26
Recurring PAT growth	7	1	49	4	25
EPS growth	7	1	13	4	25
EBITDA margin	9.9	9.1	9.1	9.0	9.2
PBT margin	7.4	6.4	5.7	4.8	4.9
Recurring PAT margin	5.1	4.1	3.7	3.2	3.2
EPS (Rs)	10.9	11.0	12.4	13.0	16.2
DPS (Rs)	0.5	0.5	0.8	0.6	0.8
BV (Rs)	132.6	141.6	122.0	134.2	149.5
ROCE	9.4	7.9	9.8	9.2	9.6
ROE	9.4	8.0	10.8	10.1	11.4
Net debt/equity (x)	0.2	0.2	0.9	0.7	1.1
Gross debt/equity (x)	0.3	0.3	1.0	0.8	1.2

Source: Company data, Credit Suisse estimates

Figure 45: **Gammon – key valuation metrics (construction business) ***

(x)	FY07	FY08	FY09E	FY10E	FY11E
P/E	7.5	7.5	6.6	6.3	5.1
EV/EBITDA	5.2	4.7	6.4	4.9	5.3
P/B	0.6	0.6	0.7	0.6	0.5

** Adjusted for BOT and real estate business valuations*

Source: Company data, Credit Suisse estimates

Figure 46: Gammon India – sum-of-the-parts valuation

Parts	Rationale	Value (Rs mn)	Value (Rs/share)
Construction business		**10,271**	**90**
Construction business	9x FY10E EPS – 25% discount to its peers	10,271	90
Infrastructure business		**9,020**	**79**
Gammon infrastructure	DCF for Gammon India's 76.3% effective stake	9,020	79
Real Estate business		**151**	**1**
Gammon realty	At book value	151	1
Other investments		**464**	**4**
Sadbhav engineering	At 20% holding company discount to CMP	464	4
Total		**19,906**	**174**

Source: Company data, Credit Suisse estimates

IVRCL

Figure 47: **IVRCL – profit and loss summary (standalone financials)**

Year-end 31 Mar (Rs mn)	FY07	FY08	FY09E	FY10E	FY11E
Sales	**23,465**	**36,981**	**50,040**	**65,192**	**87,001**
Total operating expenses	(21,147)	(33,367)	(45,288)	(58,706)	(78,088)
EBITDA	**2,318**	**3,614**	**4,752**	**6,487**	**8,913**
Depreciation	(216)	(328)	(513)	(699)	(905)
EBIT	**2,102**	**3,286**	**4,239**	**5,788**	**8,008**
Net interest expenses	(241)	(373)	(946)	(1,419)	(2,090)
PBT	**1,861**	**2,913**	**3,293**	**4,369**	**5,918**
Total tax	(403)	(989)	(1,120)	(1,485)	(2,012)
Recurring PAT	**1,458**	**1,924**	**2,174**	**2,884**	**3,906**
Exceptional	(44)	181	-	-	-
Reported PAT	**1,415**	**2,105**	**2,174**	**2,884**	**3,906**

Source: Company data, Credit Suisse estimates

Figure 48: **IVRCL – balance sheet summary (standalone financials)**

Year-end 31 Mar (Rs mn)	FY07	FY08	FY09E	FY10E	FY11E
Share capital	259	267	271	271	271
Reserves and surplus	12,958	15,793	18,126	20,710	24,210
Total net worth	**13,217**	**16,060**	**18,396**	**20,980**	**24,480**
Total loans	5,561	10,678	14,130	20,130	27,380
Deferred tax liability	56	103	103	103	103
Total liabilities & net worth	**18,834**	**26,841**	**32,629**	**41,213**	**51,963**
Gross block	2,593	4,176	6,086	8,176	10,684
CWIP	506	541	541	541	541
Net fixed assets	**2,435**	**3,733**	**5,130**	**6,521**	**8,124**
Investments	**2,829**	**3,409**	**4,364**	**5,114**	**5,864**
Inventories	825	1,943	2,085	2,710	3,412
Debtors	6,332	6,585	11,379	14,825	19,545
Cash and bank balances	2,238	1,772	336	239	456
Loans and advances	7,071	7,806	10,508	13,690	18,270
Other current assets	6,367	10,725	11,516	14,646	19,069
Total current assets	**22,834**	**28,831**	**35,825**	**46,110**	**60,752**
Current liabilities	9,092	8,893	12,339	16,075	22,167
Provisions	172	238	350	456	609
Total current liabilities and provisions	**9,264**	**9,132**	**12,689**	**16,531**	**22,776**
Net current assets	**13,570**	**19,699**	**23,136**	**29,579**	**37,976**
Total assets	**18,834**	**26,841**	**32,629**	**41,213**	**51,963**

Source: Company data, Credit Suisse estimates

Figure 49: IVRCL – cash flow statement (standalone financials)

Year-end 31 Mar (Rs mn)	FY07	FY08	FY09E	FY10E	FY11E
PBT	1,861	2,913	3,293	4,369	5,918
Tax paid	(403)	(989)	(1,120)	(1,485)	(2,012)
Change in deferred tax liability	14	47	-	-	-
Add: depreciation	216	328	513	699	905
Change in working capital	**(6,316)**	**(6,596)**	**(4,872)**	**(6,540)**	**(8,180)**
Cash flow from operations	**(4,627)**	**(4,297)**	**(2,185)**	**(2,958)**	**(3,369)**
Extraordinary income/(expenses)	(44)	181	-	-	-
Capex	(1,277)	(1,626)	(1,910)	(2,090)	(2,508)
Change in investments	(64)	(580)	(955)	(750)	(750)
Others	-	-	-	-	-
Cash flow from investing activities	**(1,385)**	**(2,025)**	**(2,865)**	**(2,840)**	**(3,258)**
Change in debt	(1,225)	5,117	3,452	6,000	7,250
Change in equity	44	8	4	-	-
Change in reserves	7,140	949	385	-	-
Dividend and dividend tax	(152)	(219)	(226)	(300)	(406)
Cash flow from financing activities	**5,807**	**5,855**	**3,615**	**5,700**	**6,844**
Increase/(decrease) in cash	**(205)**	**(467)**	**(1,436)**	**(97)**	**217**
Opening cash and bank balance	2,444	2,238	1,772	336	239
Closing cash and bank balance	**2,238**	**1,772**	**336**	**239**	**456**

Source: Company data, Credit Suisse estimates

Figure 50: IVRCL – key ratios (standalone financials)

Year-end 31 Mar (%)	FY07	FY08	FY09E	FY10E	FY11E
Sales growth	54	58	35	30	33
EBITDA growth	73	56	31	37	37
Recurring PAT growth	57	32	13	33	35
EPS growth	29	28	11	33	35
EBITDA margin	9.9	9.8	9.5	10.0	10.2
PBT margin	7.9	7.9	6.6	6.7	6.8
Recurring PAT margin	6.2	5.2	4.3	4.4	4.5
EPS (Rs)	11.2	14.4	16.1	21.3	28.9
DPS (Rs)	1.0	1.4	1.4	1.9	2.6
BV (Rs)	101.9	120.3	136.0	155.1	181.0
ROCE	12.5	11.6	10.9	11.6	12.4
ROE	16.2	13.1	12.6	14.6	17.2
Net debt/equity (x)	0.2	0.6	0.7	0.9	1.1

Source: Company data, Credit Suisse estimates

Figure 51: IVRCL – key valuation metrics (construction business) *

(x)	FY07	FY08	FY09E	FY10E	FY11E
P/E	13.7	10.7	9.6	7.2	5.3
EV/EBITDA	10.0	8.1	7.3	6.3	5.4
P/B	1.5	1.3	1.1	1.0	0.9

** Adjusted for BOT and real estate business valuations*

Source: Company data, Credit Suisse estimates

Figure 52: **IVRCL – sum-of-the-parts valuation**

Parts	Rationale	Value (Rs mn)	Value (Rs/ share)
Construction business		**34,603**	**256**
IVRCL construction business	12x FY10E earnings - 35% discount to E&C majors	34,603	256
Real estate business		**7,951**	**59**
IVR Prime	30% discount to DCF for 62.3% stake; cost of equity - 16.4%	7,951	59
IVRCL Road Toll Holdings Ltd (BOT Road SPVs)		**2,160**	**16**
Jalandhar Amritsar Toll Road	DCF for 100% stake; cost of equity - 16.7%	471	3
Salem Toll Road	DCF for 100% stake; cost of equity - 16.7%	892	7
Kumarapalyam Toll Road	DCF for 100% stake; cost of equity - 16.7%	797	6
IVRCL Water Infrastructures Ltd (BOT Water SPV)		**1,338**	**10**
Chennai Water Desalination	DCF for 75% stake; cost of equity - 16%	1,338	10
Hindustan Dorr-Oliver Ltd.		**1,588**	**12**
Hindustan Dorr-Oliver	At 20% holding company discount to CMP for 53% stake	1,588	12
Total		**47,640**	**352**

Source: Company data, Credit Suisse estimates

Nagarjuna Construction (NCC)

Figure 53: **NCC – profit and loss summary (standalone financials)**

Year-end 31 Mar (Rs mn)	FY07	FY08	FY09E	FY10E	FY11E
Sales	**28,711**	**34,729**	**44,419**	**55,641**	**70,144**
Total operating expenses	(26,013)	(31,132)	(40,132)	(50,148)	(62,744)
EBITDA	**2,698**	**3,598**	**4,287**	**5,493**	**7,400**
Depreciation	(299)	(482)	(582)	(654)	(808)
EBIT	**2,399**	**3,116**	**3,704**	**4,839**	**6,592**
Net interest expenses	(475)	(664)	(1,096)	(1,919)	(2,416)
PBT	**1,923**	**2,452**	**2,608**	**2,919**	**4,176**
Total tax	(667)	(811)	(887)	(993)	(1,420)
Recurring PAT	**1,256**	**1,641**	**1,722**	**1,927**	**2,756**
Exceptional	(99)	(22)	-	-	-
Reported PAT	**1,157**	**1,619**	**1,722**	**1,927**	**2,756**

Source: Company data, Credit Suisse estimates

Figure 54: **NCC – balance sheet summary (standalone financials)**

Year-end 31 Mar (Rs mn)	FY07	FY08	FY09E	FY10E	FY11E
Share capital	417	458	458	458	458
Reserves and surplus	9,963	15,266	16,625	18,146	20,322
Total net worth	**10,380**	**15,724**	**17,083**	**18,604**	**20,780**
Total loans	6,370	8,938	11,188	18,688	25,688
Deferred tax liability	115	167	167	167	167
Total liabilities and net worth	**16,865**	**24,829**	**28,438**	**37,459**	**46,635**
Gross block	5,007	6,620	8,308	10,389	12,699
CWIP	186	143	143	143	143
Net fixed assets	**4,229**	**5,339**	**6,445**	**7,872**	**9,374**
Investments	**4,768**	**5,648**	**10,648**	**12,848**	**14,348**
Inventories	4,041	5,493	6,161	7,713	9,664
Debtors	5,817	8,677	9,371	11,738	14,798
Cash and bank balances	2,434	2,330	325	519	939
Loans and advances	8,579	14,923	13,104	16,692	21,043
Other current assets	93	61	78	98	123
Total current assets	**20,963**	**31,484**	**29,039**	**36,760**	**46,566**
Current liabilities	11,850	15,564	15,917	17,739	20,777
Provisions	1,244	2,078	1,777	2,281	2,876
Total current liabilities and provisions	**13,095**	**17,642**	**17,694**	**20,021**	**23,653**
Net current assets	**7,869**	**13,842**	**11,345**	**16,739**	**22,913**
Total assets	**16,865**	**24,829**	**28,438**	**37,459**	**46,635**

Source: Company data, Credit Suisse estimates

Figure 55: NCC – cash flow statement (standalone financials)

Year-end 31 Mar (Rs mn)	FY07	FY08	FY09E	FY10E	FY11E
PBT	1,923	2,452	2,608	2,919	4,176
Tax paid	(667)	(811)	(887)	(993)	(1,420)
Change in deferred tax liability	49	52	-	-	-
Add: depreciation	299	482	582	654	808
Change in working capital	**238**	**(6,077)**	**492**	**(5,200)**	**(5,754)**
Cash flow from operations	**1,842**	**(3,902)**	**2,796**	**(2,619)**	**(2,190)**
Extraordinary income/ (expenses)	(99)	(22)	-	-	-
Capex	(2,612)	(1,593)	(1,688)	(2,082)	(2,310)
Change in investments	(3,891)	(880)	(5,000)	(2,200)	(1,500)
Others	-	-	-	-	-
Cash flow from investing activities	**(6,602)**	**(2,495)**	**(6,688)**	**(4,282)**	**(3,810)**
Change in debt	4,590	2,569	2,250	7,500	7,000
Change in equity	210	41	-	-	-
Change in reserves	(129)	4,031	-	(0)	-
Dividend and dividend tax	(287)	(348)	(363)	(406)	(580)
Cash flow from financing activities	**4,384**	**6,293**	**1,887**	**7,094**	**6,420**
Increase/(decrease) in cash	**(375)**	**(104)**	**(2,004)**	**194**	**419**
Opening cash and bank balance	2,809	2,434	2,330	325	519
Closing cash and bank balance	**2,434**	**2,330**	**325**	**519**	**939**

Source: Company data, Credit Suisse estimates

Figure 56: NCC – key ratios (standalone financials)

Year-end 31 Mar (%)	FY07	FY08	FY09E	FY10E	FY11E
Sales growth	56	21	28	25	26
EBITDA growth	64	33	19	28	35
Recurring PAT growth	24	31	5	12	43
EPS growth	23	19	5	12	43
EBITDA margin	9.4	10.4	9.7	9.9	10.5
PBT margin	6.7	7.1	5.9	5.2	6.0
Recurring PAT margin	4.4	4.7	3.9	3.5	3.9
EPS (Rs)	6.0	7.2	7.5	8.4	12.0
DPS (Rs)	1.2	1.3	1.4	1.5	2.2
BV (Rs)	49.8	68.7	74.6	81.3	90.8
ROCE	11.9	11.5	10.6	10.8	11.1
ROE	12.7	12.6	10.5	10.8	14.0
Net debt/equity (x)	0.4	0.4	0.6	1.0	1.2

Source: Company data, Credit Suisse estimates

Figure 57: NCC – key valuation metrics (construction business) *

(x)	FY07	FY08	FY09E	FY10E	FY11E
P/E	12.1	10.1	9.7	8.6	6.0
EV/EBITDA	7.1	6.5	6.4	6.3	5.6
P/B	1.5	1.1	1.0	0.9	0.8

** Adjusted for BOT and real estate business valuations*

Source: Company data, Credit Suisse estimates

Figure 58: NCC – sum-of-the-parts valuation

Parts	Rationale/stake	Value (Rs mn)	Rs/share
Construction business (A)		**23,121**	**101**
NCC construction business	12x FY10E earnings - 35% discount to E&C majors	23,121	101
NCC Infrastructure Holdings Ltd (B)		**4,355**	**19**
Road Projects			
Brindavan Infrastructure	DCF- 33.3% stake; cost of equity - 14.9%	126	1
Orai-Bhognipur Infrastructure	DCF- 64% stake; cost of equity - 14.9%	1,004	4
Western UP Tollway	DCF- 30% stake; cost of equity - 16.7%	224	1
Bangalore Elevated Tollway	DCF - 33.5% stake; cost of equity - 16.7%	535	2
Pondicherry - Tindivanam Tollway	DCF- 49% stake; cost of equity - 16.7%	149	1
Power Projects			
Gautami Power	Book value of investment	413	2
Himachal Sorang Power	DCF- 90% stake; cost of equity - 16.7%	544	2
Himalayan Green Energy	DCF- 50% stake; cost of equity - 16.7%	747	3
Port Project			
Machalipatnam Port	DCF- 26% stake; cost of equity - 17.2%	612	3
Real Estate (C)		**5,637**	**25**
NCC urban infra. - land under development	30% discount to DCF- 80% stake; cost of equity - 16.4%	2,397	10
NCC urban Infra. - landbank	Book value of Investment	648	3
Tellapur - JV with Tishman & ICICI Venture	30% discount to DCF- 26% stake; cost of equity - 16.4%	1,832	8
Jubilee Hills Land Mark Projects	Book value of Investment	453	2
NCC-Vizag Urban Infrastructure Ltd	30% discount to DCF- 100% stake; cost of equity - 16.4%	308	1
Total (A+B+C)		**33,112**	**145**

Source: Company data, Credit Suisse estimates

Simplex Infrastructures

Figure 59: Simplex – profit and loss summary

Year-end 31 Mar (Rs mn)	FY07	FY08E	FY09E	FY10E	FY11E
Sales	**17,110**	**28,121**	**39,258**	**56,865**	**72,877**
Total operating expenses	(15,488)	(25,421)	(35,204)	(50,581)	(64,580)
EBITDA	**1,622**	**2,700**	**4,054**	**6,285**	**8,297**
Depreciation	(391)	(643)	(960)	(1,171)	(1,456)
EBIT	**1,231**	**2,057**	**3,094**	**5,114**	**6,840**
Net interest expenses	(537)	(768)	(1,041)	(1,444)	(1,844)
PBT	**693**	**1,289**	**2,053**	**3,669**	**4,997**
Total tax	(162)	(376)	(698)	(1,247)	(1,698)
Recurring PAT	**531**	**913**	**1,356**	**2,423**	**3,299**
Exceptional	6	(12)	-	-	-
Reported PAT	**537**	**901**	**1,356**	**2,423**	**3,299**

Source: Company data, Credit Suisse estimates

Figure 60: Simplex – balance sheet summary

Year-end 31 Mar (Rs mn)	FY07	FY08E	FY09E	FY10E	FY11E
Share capital	86	99	110	110	110
Reserves and surplus	2,673	7,432	10,688	12,728	15,506
Total net worth	**2,759**	**7,531**	**10,798**	**12,838**	**15,616**
Total loans	6,877	7,493	9,243	13,743	18,743
Deferred tax liability	181	371	521	788	1,151
Total liabilities and net worth	**9,816**	**15,396**	**20,562**	**27,369**	**35,510**
Gross block	4,305	7,567	10,727	14,192	18,172
CWIP	228	243	243	243	243
Net fixed assets	**3,619**	**6,537**	**8,737**	**11,031**	**13,554**
Investments	**53**	**99**	**99**	**99**	**99**
Inventories	2,852	4,741	5,420	7,934	10,474
Debtors	8,493	11,497	15,811	22,902	29,949
Cash and bank balances	425	1,232	977	279	315
Loans and advances	1,777	2,839	3,119	4,674	5,990
Other current assets	408	834	834	834	834
Total current assets	**13,955**	**21,143**	**26,161**	**36,622**	**47,563**
Current liabilities	7,729	12,267	14,238	20,098	25,341
Provisions	81	116	196	284	364
Total current liabilities and provisions	**7,810**	**12,383**	**14,434**	**20,383**	**25,705**
Net current assets	**6,145**	**8,760**	**11,727**	**16,240**	**21,858**
Total Assets	**9,816**	**15,396**	**20,562**	**27,369**	**35,511**

Source: Company data, Credit Suisse estimates

Figure 61: **Simplex – cash flow statement**

Year-end 31 Mar (Rs mn)	FY07	FY08E	FY09E	FY10E	FY11E
PBT	693	1,289	2,053	3,669	4,997
Tax paid	(162)	(376)	(698)	(1,247)	(1,698)
Change in deferred tax liability	58	191	149	267	363
Add: depreciation	391	643	960	1,171	1,456
Change in working capital	**(1,532)**	**(1,808)**	**(3,222)**	**(5,211)**	**(5,582)**
Cash flow from operations	**(551)**	**(62)**	**(756)**	**(1,351)**	**(463)**
Extraordinary income/(expenses)	6	(12)	-	-	-
Capex	(1,740)	(3,561)	(3,160)	(3,465)	(3,980)
Change in investments	(50)	(46)	-	-	-
Others	-	-	-	-	-
Cash flow from investing activities	**(1,784)**	**(3,619)**	**(3,160)**	**(3,465)**	**(3,980)**
Change in debt	2,425	617	1,750	4,500	5,000
Change in equity	-	13	11	-	-
Change in reserves	(30)	3,974	2,115	-	-
Dividend and dividend tax	(80)	(116)	(214)	(383)	(521)
Cash flow from financing activities	**2,315**	**4,488**	**3,661**	**4,117**	**4,479**
Increase/(decrease) in cash	**(20)**	**807**	**(255)**	**(698)**	**36**
Opening cash and bank balance	445	425	1,232	977	279
Closing cash and bank balance	**425**	**1,232**	**977**	**279**	**315**

Source: Company data, Credit Suisse estimates

Figure 62: **Simplex – key ratios**

Year-end 31 Mar (%)	FY07	FY08E	FY09E	FY10E	FY11E
Sales growth	27	64	40	45	28
EBITDA growth	39	66	50	55	32
Recurring PAT growth	45	72	49	79	36
EPS growth	46	49	34	79	36
EBITDA margin	9.5	9.6	10.3	11.1	11.4
PBT margin	4.1	4.6	5.2	6.5	6.9
Recurring PAT margin	3.1	3.2	3.5	4.3	4.5
EPS (Rs)	12.3	18.4	24.7	44.1	60.0
DPS (Rs)	1.6	2.0	3.3	6.0	8.1
BV (Rs)	64.1	151.6	196.4	233.6	284.1
ROCE	12.1	13.4	11.7	14.2	14.4
ROE	20.9	17.7	14.8	20.5	23.2
Net debt/equity (x)	2.3	0.8	0.8	1.0	1.2

Source: Company data, Credit Suisse estimates

Figure 63: **Simplex – key valuation metrics (construction business) ***

(x)	FY07	FY08E	FY09E	FY10E	FY11E
P/E	32.6	21.9	16.3	9.1	6.7
EV/EBITDA	14.7	9.7	7.5	5.7	4.9
P/B	6.3	2.7	2.1	1.7	1.4

** Adjusted for BOT and real estate business valuations*

Source: Company data, Credit Suisse estimates

Figure 64: **Simplex Infrastructures – sum-of-the parts valuation**

Parts	Rationale	Value (Rs/share)
Construction business	At 12x FY10E earnings – in line with its peers; 35% discount to E&C majors	529
Real estate business	30% discount to DCF for Simplex's stake; cost of equity – 16%	16
Total		**545**

Source: Company data, Credit Suisse estimates

Companies Mentioned *(Price as of 22 Sep 08)*
Gammon India Ltd (GAMM.BO, Rs166.15, NEUTRAL [V], TP Rs174.00)
Hindustan Construction Ltd (HCNS.BO, Rs89.75, NOT RATED)
IVRCL Infrastructures and Projects Ltd (IVRC.BO, Rs250.2, OUTPERFORM [V], TP Rs352)
Jaiprakash Associates Ltd. (JAIA.BO, Rs130.05, NOT RATED)
Nagarjuna Construction Company Ltd (NGCN.BO, Rs116.40, OUTPERFORM [V], TP Rs145.00)
Simplex Infrastructures Ltd (SINF.BO, Rs419.00, OUTPERFORM, TP Rs545.13)

Disclosure Appendix

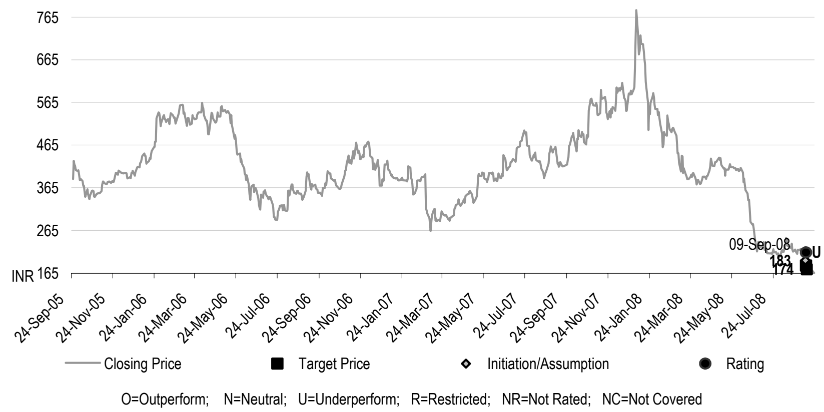
Important Global Disclosures

Amish Shah, CFA & Vinod Chari each certify, with respect to the companies or securities that he or she analyzes, that (1) the views expressed in this report accurately reflect his or her personal views about all of the subject companies and securities and (2) no part of his or her compensation was, is or will be directly or indirectly related to the specific recommendations or views expressed in this report.

See the Companies Mentioned section for full company names.

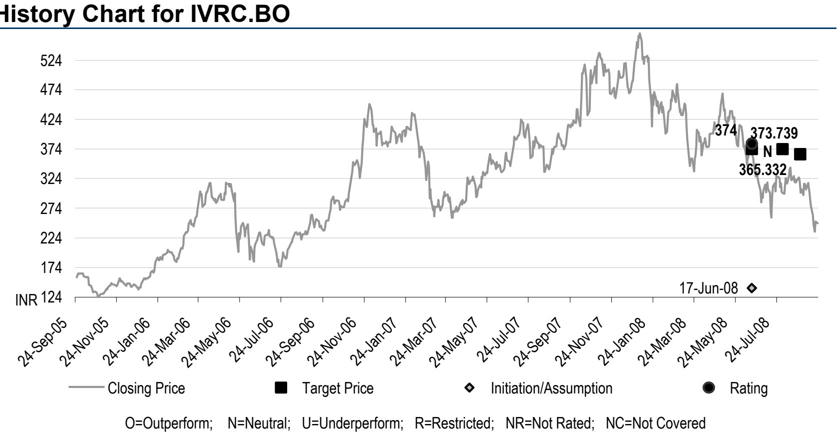
3-Year Price, Target Price and Rating Change History Chart for GAMM.BO

GAMM.BO Date	Closing Price (INR)	Target Price (INR)	Rating	Initiation/ Assumption
9-Sep-08				X
10-Sep-08	214	183	U	
11-Sep-08	212.3	174		



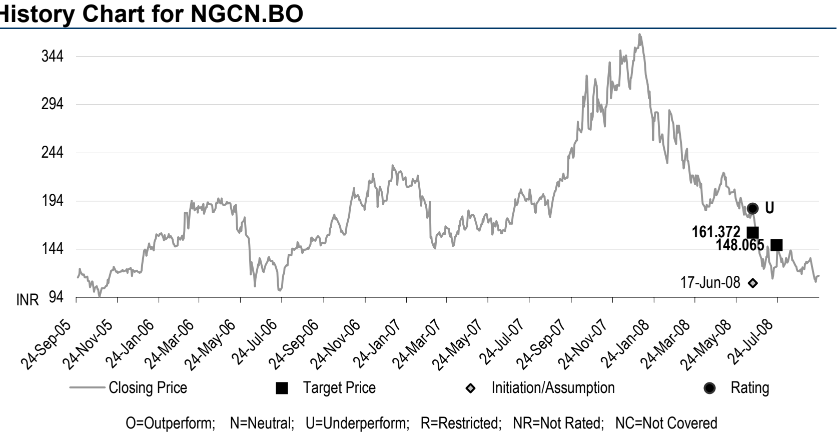
3-Year Price, Target Price and Rating Change History Chart for IVRC.BO

IVRC.BO Date	Closing Price (INR)	Target Price (INR)	Rating	Initiation/ Assumption
17-Jun-08	383.1	374	N	X
1-Aug-08	299.85	373.739		
27-Aug-08	315.7	365.332		



3-Year Price, Target Price and Rating Change History Chart for NGCN.BO

NGCN.BO Date	Closing Price (INR)	Target Price (INR)	Rating	Initiation/ Assumption
17-Jun-08	186	161.372	U	X
22-Jul-08	126.25	148.065		



3-Year Price, Target Price and Rating Change History Chart for SINF.BO

SINF.BO Date	Closing Price (INR)	Target Price (INR)	Rating	Initiation/ Assumption
17-Jun-08	485.95	557.213	O	X
1-Jul-08	419.85	545		

O=Outperform; N=Neutral; U=Underperform; R=Restricted; NR=Not Rated; NC=Not Covered

The analyst(s) responsible for preparing this research report received compensation that is based upon various factors including Credit Suisse's total revenues, a portion of which are generated by Credit Suisse's investment banking activities.

Analysts' stock ratings are defined as follows*:**

Outperform (O): The stock's total return is expected to exceed the industry average* by at least 10-15% (or more, depending on perceived risk) over the next 12 months.

Neutral (N): The stock's total return is expected to be in line with the industry average* (range of ±10%) over the next 12 months.

Underperform (U):** The stock's total return is expected to underperform the industry average* by 10-15% or more over the next 12 months.

**The industry average refers to the average total return of the relevant country or regional index (except with respect to Europe, where stock ratings are relative to the analyst's industry coverage universe).*

***In an effort to achieve a more balanced distribution of stock ratings, the Firm has requested that analysts maintain at least 15% of their rated coverage universe as Underperform. This guideline is subject to change depending on several factors, including general market conditions.*

****For Australian and New Zealand stocks a 7.5% threshold replaces the 10% level in all three rating definitions, with a required equity return overlay applied.*

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Analysts' coverage universe weightings are distinct from analysts' stock ratings and are based on the expected performance of an analyst's coverage universe* versus the relevant broad market benchmark:**

Overweight: Industry expected to outperform the relevant broad market benchmark over the next 12 months.

Market Weight: Industry expected to perform in-line with the relevant broad market benchmark over the next 12 months.

Underweight: Industry expected to underperform the relevant broad market benchmark over the next 12 months.

**An analyst's coverage universe consists of all companies covered by the analyst within the relevant sector.*

***The broad market benchmark is based on the expected return of the local market index (e.g., the S&P 500 in the U.S.) over the next 12 months.*

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	Global Ratings Distribution	
Outperform/Buy*	43%	(59% banking clients)
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Price Target: (12 months) for (GAMM.BO)

Method: Our price target of Rs174 is based on the sum-of-the-parts valuation methodology. We have valued the core construction business (including ATSL) at 9x FY10E earnings per share (EPS) - 25% discount to its peers given considerably low return ratios and earnings growth. We have used discounted cash flow (DCF)-equity method to value the BOT assets of GIPL for Gammon's effective 76.3% stake using cost of equity ranging from 14.9% to 16.7% depending on the nature of the asset, stage of completion and the risks involved. We have valued Gammon's real estate business at its book value of investments given the lack of disclosure of its land bank/ development plans in this space. We value Gammon's 5.6% stake in Sadbhav Engineering at 20% holding company discount to its current market price.

Risks: Potential risks to our Rs174 target price for Gammon India includes: Project execution risk, commodity prices, interest rates, foreign currency, traffic/ revenue risk for BOT projects, litigation/ arbitration proceedings, infrastructure/ real estate projects valuation, significant ramp-up at Franco Tosi/ Sadelmi/ Sofinter, allowance of benefits under Section 80-IA of Income Tax Act, 1961, cash flows from land litigation, manpower shortages, slowdown in economy/ government capex and potential equity dilution.

Price Target: (12 months) for (IVRC.BO)

Method: Our Rs352 target price for IVRCL Infrastructures and Projects (IVRCL) is based on sum-of-the parts. We have valued IVRCL's core construction business at a conservative 12x FY10E earnings, in line with its peers and at 35% discount to large E&C players. We have valued its infrastructure BOT projects based on DCF equity method and its real estate subsidiary, IVR Prime, at a 30% discount to its NAV. We have applied a 20% holding company discount to the market value of its ~53% stake in HDO.

Risks: Potential risks to our Rs352 target price for IVRCL Infrastructures and Projects include: project execution, commodity prices, interest rates, traffic/ revenue risk for BOT projects, manpower shortages, slowdown in economy/ government capex, real estate valuations, competition, allowance of benefits under Section 80-IA of Income Tax Act and potential equity dilution.

Price Target: (12 months) for (NGCN.BO)

Method: Our Rs145 target price for Nagarjuna Construction (NCC) is based on sum-of-the parts. We have valued NCC's core construction business at a conservative 12x FY10E earnings, in line with its peers and at 35% discount to large E&C players. We have valued its infrastructure BOT projects based on DCF equity method. We have valued the Gautami power project at the company's book value of the investment given the uncertainty of its fuel supply (natural gas). We have valued real estate projects for which development plans are in place at a 30% discount to NAV. We ascribe book value to NCC's land bank and to projects like Jubilee Hills, for which development plans are not yet complete.

Risks: Potential risks to our Rs145 target price for NCC include: project execution, commodity prices, interest rates, traffic/ revenue risk for BOT projects, manpower shortages, slowdown in economy/ government capex, real estate valuations, competition, allowance of benefits under Section 80-IA of Income Tax Act and potential equity dilution.

Price Target: (12 months) for (SINF.BO)

Method: Our Rs545 target price for Simplex Infrastructures is based on sum-of-the parts. We have valued Simplex's core construction business at a conservative 12x FY10E earnings, in line with its peers and at 35% discount to large E&C players. We have valued its real estate business at a 30% discount to NAV.

Risks: Potential risks to our Rs545 target price for Simplex Infrastructures include: foreign currency risk, project execution, commodity prices, interest rates, manpower shortages, slowdown in economy/ government capex, competition, allowance of benefits under Section 80-IA of Income Tax Act and potential equity dilution.

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