



ENAM Securities
India Research

CMP: Rs 240
Target Price: Rs 305
Potential Upside: 27%
Absolute Rating: **BUY**

Sobha Developers Ltd

Relative to sector: **Outperformer**

Chirag Negandhi

ED & Deputy Head of Research
Email: chirag.negandhi@enam.com
Tel: 9122 6754 7618

Nitin Idnani

Sr VP - Realty
Email: nitin.idnani@enam.com
Tel: 9122 6754 7655

Kunal Lakhan

Asst VP - Realty
Email: kunal.lakhan@enam.com

Relative Performance



Source: Bloomberg, ENAM Research

Stock data

No. of shares : 98 mn
Market cap : Rs 23.5 bn
52 week high/low : Rs 404/ Rs 185
Avg. daily vol. (6mth) : 283,600 shares
Bloomberg code : SOBHA IB
Reuters code : SOBH.BO

Shareholding (%)

	Mar-11	QoQ chg
Promoters	60.6	0.0
FIs	30.2	0.6
MFs / UTI	4.0	(0.7)
Banks / FIs	0.6	0.0
Others	4.6	0.2

Financial Summary

Y/E Mar	Sales (Rs mn)	PAT (Rs mn)	P/E (x)	RoE (%)	RoCE (%)	Valuation	(Rs)
2010	11,299	1,341	-	9.4	7.5	Target Price (Rs)	305
2011	14,739	1,813	13.0	10.0	9.3	Upside (%)	27
2012E	17,155	2,338	10.1	11.7	12.0		
2013E	18,718	2,668	8.8	11.9	13.6		

Source: Company, ENAM estimates

ANNUAL REPORT 2010-11: KEY TAKEAWAYS

Key balance sheet highlights: Strong sales + Improved working capital cycle → repayment of debt

- Sobha registered robust sales of ~2.78 msf (↑ 33% YoY) @ an avg. realization of Rs 4,082/ sq. ft (↑ 40% YoY) in FY11.
- Working cap. cycle improved, with collections of ~Rs 5.5 bn & reduction in inventory (↓ from 22 months to 11 months) & debtors (↓ from 90 to 60 days) → net CFO of ~Rs 4 bn (↑ 22% YoY).
- Bulk of the operating cash flow was utilized towards reduction of debt by ~Rs 2.3 bn (net) to Rs 12.4 bn in FY11 (net D/E of 0.66x as compared to 0.82x at the end of FY10).

Key profit & loss highlights: Higher realization offset increase in input costs → operating margins sustain

- Construction cost was up ~18% from 1,800/ sq. ft at the beginning of the year to ~Rs 2,100/ sq. ft. (contractual segment is unaffected as it operates on a cost +15% margin).
- However, higher contribution from real estate operations (~67% to the revenue in FY11 vs. 59% in FY10), improved overall realizations (OPM of real estate: ~35%; OPM of contractual proj: ~15%), thus partially offsetting the impact of cost inflation on margins.
- While, reduction in debt has led to ~19% decline in interest costs to Rs 1.8 bn (~Rs 1.4 bn capitalized), higher tax outlay on a/c of lower contribution from 80IB projects capped net margins.

Valuation & Outlook

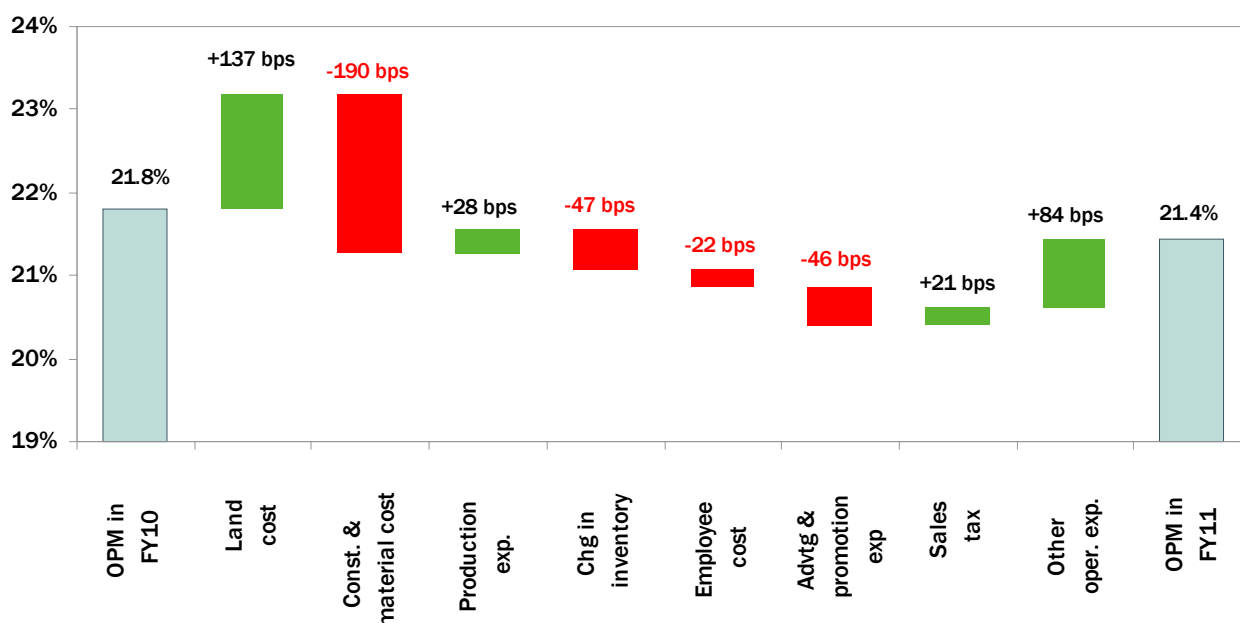
With only ~3 msf of existing inventory, new launches (in Gurgaon and B'lore) are critical for Sobha to meet its FY12E sales guidance of ~3.3-3.5 msf. The co. has received approvals for its Sobha International City, Gurgaon as well as Sobha City, Bangalore (plans to launch both by end June/ early July). Contractual business is picking up pace with company confident of clocking ~Rs 5 bn of revenues in FY12E. At CMP of Rs 240, we maintain our **BUY** rating with a **TP of Rs 305** – an upside of 27%.

Consolidated Profit & Loss Account

(Rs mn)	FY11	FY10	% Chg	Key comments
Income from operations	14,771.2	11,332.6	30.3%	
Property Development	9,852.2	6,730.2	46.4%	Completed ~4.12 msf of projects and added ~2.55 msf to execution
Sale of land and dev. rights	1,539.6	1,916.7	-19.7%	Sale of mainly 4 land parcels (1 in Pune, 1 in Chennai & 2 in Bangalore)
Contractual activity	2,452.1	1,702.9	44.0%	Completed ~2.2 msf of contracts in FY11
Manufacturing	927.3	982.8	-5.6%	
Less: Excise duty	32.4	33.9	-4.6%	
Income from operations (net)	14,738.8	11,298.7	30.4%	
Cost of Sales	8,632.2	6,536.7	32.1%	
Land cost	1,791.3	1,527.9	17.2%	
Construction cost	5,467.7	3,848.6	42.1%	Higher on a/c of increase in construction activity as well as cost of materials and its procurement
Raw material	700.7	665.9	5.2%	Higher mainly on a/c of rise in cost of raw materials and logistic cost
Production expense	237.2	213.2	11.3%	
Decrease/ (incr.) in inventories	435.5	281.1	54.9%	Mainly driven by higher sale of under construction projects as compared to ready/ completed projects
Personnel expenses	1,035.2	768.3	34.7%	Higher due to an increase in the employee strength from 1,852 in FY10 to 2,224 in FY11 and avg. annual salary increment of ~10%.
Operating and other expenses	1,910.5	1,530.5	24.8%	
EBITDA	3,160.9	2,463.3	28.3%	
EBITDA Margin (%)	21.4%	21.8%	-36 bps	Higher input cost offset by revenue booking from higher realization projects
Depreciation/ amortization	277.7	323.1	-14.0%	
EBIT	2,883.2	2,140.2	34.7%	
EBIT Margin (%)	19.6%	18.9%	62 bps	
Interest expenses	443.5	520.8	-14.8%	Net debt reduced by ~Rs 1.8 bn. Avg cost of debt remains steady at 12.9%. During FY11 ~Rs 1.37 bn of interest was capitalized.
Other Income	74.5	38.6	93.2%	Higher mainly due to receipt from the sale of scrap
Profit before tax	2,514.2	1,657.9	51.6%	
Tax	668.6	274.8	143.3%	
Effective tax rate	26.6%	16.6%	1002 bps	Increase in tax rate due to lower contribution of revenue from project which enjoy 80IB benefits
Profit after tax	1,845.6	1,383.1	33.4%	
Minority Interest	32.9	42.2	-21.9%	
Share of (profit)/ loss of asso.	(0.2)	0.0	-	
Net Profit	1,812.9	1,341.0	35.2%	
Net Margin	12.3%	11.9%	43 bps	

Source: Company, ENAM Research

Operating margin drivers in FY11



Source: Company; ENAM Research

Construction contracts

(Rs mn)	FY11	FY10
Contract revenue recognized as on Mar 31, 2011 for contracts in progress	9,640.6	7,268.8
Contract cost incurred till date for contracts in progress	13,772.7	12,363.1
Customer advances O/S for contracts in progress as on Mar 31, 2011	2,106.3	1,257.9
Amount due from customers for contracts in progress as on Mar 31, 2011	128.2	232.0

Source: Company

Other key highlights

- ❑ Delays in planned launches at Gurgaon, Chennai & Mysore have led to slippage in Sobha's sales volumes to ~2.78 msf for FY11 (as against its 3 msf guidance) @ an avg. realization of Rs 4,082/ psf (up 40% YoY).
- ❑ The company has completed ~6.32 msf of projects in FY11, which includes 4.12 msf of real estate projects.
- ❑ Of the ongoing projects of 6.99 msf (Sobha's share: 5.98 msf), Sobha has sold 3.21 msf from which Rs 9.3 bn (includes Rs 1.14 bn from the completed projs.) is to be received, leaving 3.04 msf (incl. 0.27 msf of completed projs.) to be sold with an expected realization of ~Rs 14.7 bn. Considering Rs 12.2 bn of costs to be incurred, net cash of Rs 11.8 bn is expected over ~2 years.
- ❑ Sobha plans to launch ~11 msf of projects in phases, of which ~3.3 msf in B'lore and ~5.8 msf in Gurgaon are the key ones.
- ❑ The company currently has 7.4 msf of ongoing contractual projects with unbilled value of ~Rs 5.6 bn.
- ❑ Sobha has a strong contractual pipeline with forthcoming projects of ~4.05 msf (worth Rs 3.07 bn) – to start over the coming quarters.

Consolidated Balance Sheet

(Rs mn)	FY11	FY10	% Chg	Comments
Sources of funds				
Shareholders' funds	18,507.8	17,038.0	8.6%	
Share capital	980.6	980.6	0.0%	
Reserves and surplus	17,527.2	16,057.3	9.2%	Includes debenture redemption reserve of ~Rs 162.3 mn towards redemption of Rs 750 mn worth of NCDs.
Minority Interest	324.0	291.1	11.3%	
Loan funds	12,418.4	14,740.4	-15.8%	Mainly led by ~Rs 2.4 bn reduction in term loans and redemption of ~Rs 250 mn worth of NCDs. Cash credit from banks increased by Rs 553 mn.
Secured loans	12,334.9	14,465.9	-14.7%	
Unsecured loans	83.5	274.5	-69.6%	
Total	31,250.2	32,069.4	-2.6%	
Application of funds				
Fixed assets	2,040.8	2,061.1	-1.0%	
Gross block	3,147.7	2,942.1	7.0%	
Less: Accu. Depr./ amort.	1,774.9	1,513.0	17.3%	
Net block	1,372.8	1,429.1	-3.9%	
CWIP incl. capital advances	668.0	632.0	5.7%	
Investments	37.1	27.0	37.6%	
Deferred tax asset (net)	73.8	51.5	43.2%	Arising on a/c of timing difference in relation to depreciation and expenditure disallowed under the Income Tax Act
Current assets, loans and advances	36,807.5	36,459.2	1.0%	
Inventories	10,684.6	11,101.4	-3.8%	Mainly driven by higher sale of under-construction projects (decline in work in progress by ~Rs 658 mn) as compared to ready/ completed projects (increase in stock in trade by ~Rs 216 mn). Inventory declined from 22 months to 11 months of inventory
Sundry debtors	4,251.6	4,429.9	-4.0%	Debtor days in FY11 declined to ~60 days from 90 days in FY10. ~Rs 804 mn worth of debtors are outstanding for more than 6 months
Cash and bank balances	288.5	825.7	-65.1%	Cash was lower on a/c of reduction of gross debt by Rs 2.3 bn, payments towards land acquisition of Rs 1 bn and payment towards dividend of Rs 287 mn.
Loans and advances	21,582.9	20,102.3	7.4%	Mainly driven by payments made towards acquisition of land (~Rs 1 bn) and deposits (Rs 200 mn)
Less: Current liabilities and prov.	7,708.9	6,529.4	18.1%	
Current liabilities	6,765.7	5,984.3	13.1%	
Customer advances	1,818.7	2,041.7	-10.9%	The company received ~Rs 5.5 bn of customer advances in FY11, bulk of which was booked as revenue indicating sales in FY11 were driven by existing projects and also most of the new launches crossed the revenue recognition threshold
Sundry creditors	1,042.8	869.1	20.0%	
Other current liabilities	3,904.2	3,073.5	27.0%	
Provisions	943.3	545.1	73.1%	Higher mainly on a/c of increase in the provision for taxes to ~Rs 527 mn (~Rs 192 mn in FY10)
Net current assets	29,098.5	29,929.8	-2.8%	
Total	31,250.2	32,069.4	-2.6%	

Source: Company, ENAM Research

Consolidated Cash Flow Statement

(Rs mn)	FY11	FY10
Cash flow from operating activities		
Profit before tax	2,514.2	1,657.9
Adjustments for-		
- Depreciation/ amortization	277.7	323.1
- (Profit)/ loss on sale of fixed assets	(3.1)	(3.9)
- Dividend income	0.0	(0.4)
- Interest income	(15.7)	(7.9)
- Interest expense	364.8	460.1
Operating profit before working capital changes	3,138.0	2,429.0
Movements in working capital-		
- (Increase)/ decrease in inventories	832.9	544.3
- (Increase)/ decrease in debtors	178.3	(746.7)
- (Increase)/ decrease in loans and advances	(559.3)	519.1
- Increase/ (decrease) in current liabilities and provisions	801.6	737.4
- Cash (used in)/ generated from operations	4,391.5	3,483.0
- Direct taxed paid (net)	(356.4)	(161.8)
- Net cash generated from operating activities	4,035.1	3,321.2
Cash flow from investing activities		
Purchase of fixed assets	(229.8)	(139.4)
Proceeds from sale of fixed assets	5.4	6.9
Purchase of investments	0.0	(650.0)
Purchase of equity investments	(10.0)	0.0
Sale of investments	0.0	650.0
Interest received	15.7	8.1
Dividends received	0.0	0.4
Net cash from investing activities	(218.6)	(124.1)
Cash flow from financing activities		
Refund of share application money	0.0	(474.7)
Proceeds from issue of shares	0.0	5,094.0
Proceeds from secured loans	4,274.6	1,838.0
Repayment of secured loans	(6,408.3)	(6,407.2)
Proceeds from unsecured loans	9.0	0.0
Repayment of unsecured loans	(200.0)	0.0
Interest paid (gross)	(1,741.9)	(2,470.0)
Dividends paid	(245.5)	(72.4)
Tax on dividend paid	(41.7)	(93.4)
Net cash from financing activities	(4,353.7)	(2,585.7)
Net Increase/ (decrease) In cash	(537.2)	611.5
Cash at beginning of the year	825.7	214.2
Cash at end of the year	288.5	825.7

Source: Company

Abridged Cash Flow Statement for FY11

(Rs mn)	FY11
Cash Inflow	
Total collections	14,416
Sale of land	1,544
New loans taken	4,284
Interest income	16
Proceeds from sale of fixed assets	5
Total cash Inflow	20,264
Cash outflow	
Total expenditure incurred	(8,290)
Payment towards land	(559)
Dividends paid (incl. dividend tax)	(287)
Interest paid	(1,742)
Repayment of loan	(6,608)
Purchase of fixed assets	(230)
Purchase of equity investments	(10)
Taxes paid	(356)
Other operating overheads	(2,718)
Total cash outflow	(20,801)
Change In cash	(537)
Opening cash	826
Closing cash	288

Source: Company; ENAM Research

Other key highlights

- ❑ Sobha repaid ~Rs 6.6 bn of loans and took ~Rs 4.3 bn of new loans in FY11 (net reduction of Rs 2.3 bn). The cost of debt continues to be at ~13%.
- ❑ Sobha has debt repayment of ~Rs 5.5 bn in FY12E, which will be met by sanctioned but un-disbursed loans against various projects.
- ❑ Besides the un-disbursed loan sanctions of Rs 4.15 bn, Sobha has received offer letter for a fresh sanction of ~Rs 2.2 bn with ~Rs 3.3 bn worth of new sanctions under discussion.

Details of secured loans and collaterals offered

Details of securities offered	Secured Debt (Rs mn)			Collateral Asset Value (Rs mn)		Security Provision (x)
	FY11	FY10	% Chg	FY11	FY10	
Debentures						
Secured by equitable mortgage of certain lands of the Group	750.0	1,000.0	-25.0%	-	-	-
Term loans						
Secured by equitable mortgage of land & bldg, receivables, lease rights, and hypothecation of plant & machinery and inventory (specific projects).	8,386.2 ^	10,768.6 ^	-22.1%	3,492.8	3,405.0	1.5 - 2x
Other loans						
From banks						
- Cash credit and other facilities						
- Secured by hypothecation of receivables (specific projects), equitable mortgage of land & bldg (specific projs.), fixed deposit, lease rights & hypothecation of stock of bldg materials.	3,167.7	2,615.0	21.1%	14,734.4 *	4,387.7	1.5 - 2x
From others						
- Vehicle/ equipment loan						
- Secured by specific assets/ vehicles	28.3	82.3	-65.6%	-	-	
Total	12,332.2	14,465.9	-14.7%	18,227.2	7,792.7	

Source: Company, Enam Research; Note: * Includes collateral for loans to the tune of ~Rs 4.5-5 bn which have been sanctioned but not disbursed; ^ Out of the total term loans, ~Rs 3.3 bn of term loans were not required to provide any security.

Redeemable NCDs

Particulars	Description	Int. rate (%)	Redemption Date	Redemption Amount (Rs mn)
As on Mar 31, 2011				
LIC	25 certificates of Rs 10 mn each	12.00%	11-Jun-11	250.0
LIC	25 certificates of Rs 10 mn each	12.00%	11-Sep-11	250.0
LIC	25 certificates of Rs 10 mn each	12.00%	11-Dec-11	250.0

Source: Company

Contingent liabilities not provided for

(Rs mn)	FY11	FY10
Guarantees and counter guarantees given by the company	1,193.4	677.1
Claims against the Company; not acknowledged as debts*	846.7	0.0
Income tax matters in dispute	209.6	226.9
Sales tax matters in dispute	125.1	60.5
Service tax matters in dispute	1,078.1	939.6
Total	3,452.9	1,904.1

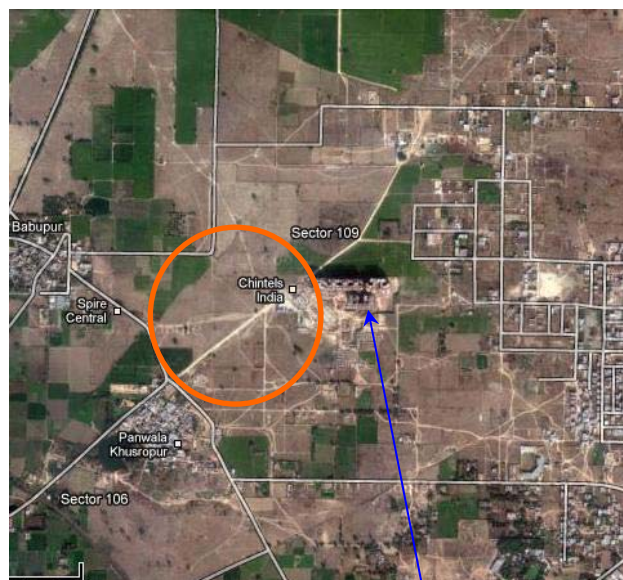
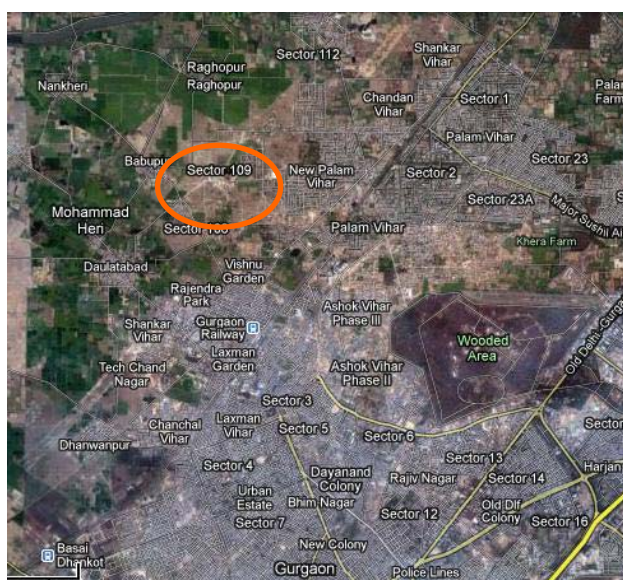
Source: Company; Note: * During the year, a customer has initiated arbitration proceedings against the Company for Rs 846.7 mn for breach of contractual obligation (dissatisfied with the quality of construction). The company has already completed and handed over the asset (a commercial complex with a retail mall) to the client and is yet to receive ~Rs 600-700 mn from the client (included in the receivables). Sobha has filed a statement of objection and counter claim for non-payment claiming payments of Rs 1 bn (which includes ~Rs 300-400 mn of accrued interest).

Top 10 shareholders as on March 31, 2011

Name of Shareholder	Category	No. of Shares	(%)
Ms. Sobha Menon	Promoter	41,348,421	42.2
Mr. P.N.C. Menon	Promoter	12,488,522	12.7
Mr. P.N.C. Menon & Ms. Sobha Menon (Jointly)	Promoter	5,494,407	5.6
Aranda Investments (Mauritius) PTE Ltd	FII	3,851,407	3.9
Emerging Markets Growth Funds INC	FII	3,594,606	3.7
Morgan Stanley Mauritius Co. Ltd.	FII	3,089,942	3.2
PCA India Equity Open Ltd.	FII	2,827,016	2.9
Merrill Lynch Capital Markets Espana S.A. S.V.	FII	2,264,634	2.3
Capital International Emerging Markets Fund	FII	1,723,609	1.8
Comgest Growth Plc A/C Comgest Growth India	FII	1,300,000	1.3
Total		77,982,564	79.5

Source: Company

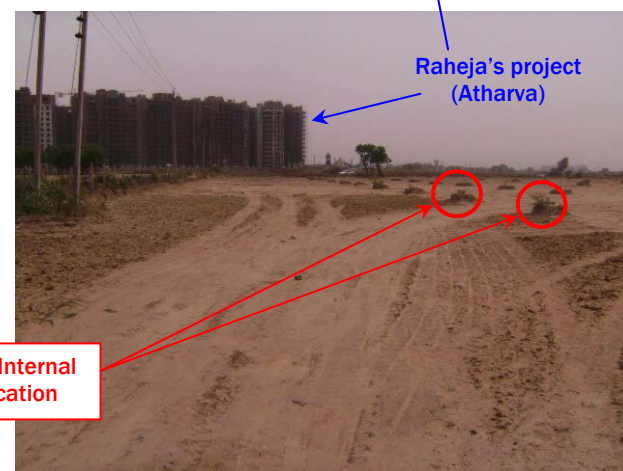
Sobha International city, Gurgaon, Sector 109 (Location map)



Sobha International city (Site pictures)



Phase I: Internal demarcation



Raheja's project (Atharva)

Source: ENAM Research

This document is provided for assistance only and is not intended to be and must not alone be taken as the basis for an investment decision. Nothing in this document should be construed as investment or financial advice, and nothing in this document should be construed as an advice to buy or sell or solicitation to buy or sell the securities of companies referred to in this document. The intent of this document is not in recommendatory nature

Each recipient of this document should make such investigations as it deems necessary to arrive at an independent evaluation of an investment in the securities of companies referred to in this document (including the merits and risks involved), and should consult its own advisors to determine the merits and risks of such an investment. The investment discussed or views expressed may not be suitable for all investors

Enam Securities Private Limited has not independently verified all the information given in this document. Accordingly, no representation or warranty, express or implied, is made as to the accuracy, completeness or fairness of the information and opinions contained in this document

The Disclosures of Interest Statement incorporated in this document is provided solely to enhance the transparency and should not be treated as endorsement of the views expressed in the report. This information is subject to change without any prior notice. The Company reserves the right to make modifications and alternations to this statement as may be required from time to time without any prior approval

Enam securities Private Limited, its affiliates, their directors and the employees may from time to time, effect or have effected an own account transaction in, or deal as principal or agent in or for the securities mentioned in this document. They may perform or seek to perform investment banking or other services for, or solicit investment banking or other business from, any company referred to in this report. Each of these entities functions as a separate, distinct and independent of each other. The recipient should take this into account before interpreting the document

This report has been prepared on the basis of information, which is already available in publicly accessible media or developed through analysis of ENAM Securities Private Limited. The views expressed are those of analyst and the Company may or may not subscribe to all the views expressed therein

This document is being supplied to you solely for your information and may not be reproduced, redistributed or passed on, directly or indirectly, to any other person or published, copied, in whole or in part, for any purpose. Neither this document nor any copy of it may be taken or transmitted into the United State (to U.S. Persons), Canada, or Japan or distributed, directly or indirectly, in the United States or Canada or distributed or redistributed in Japan or to any resident thereof. The distribution of this document in other jurisdictions may be restricted by law, and persons into whose possession this document comes should inform themselves about, and observe, any such restrictions

Neither the Firm, not its directors, employees, agents or representatives shall be liable for any damages whether direct or indirect, incidental, special or consequential including lost revenue or lost profits that may arise from or in connection with the use of the information.

Copyright in this document vests exclusively with ENAM Securities Private Limited.