

Company Focus

30 October 2007 | 8 pages

Unitech (UNTE.BO)

 Target price change

Sell: Strong 2Q, Adds Landbank; but Upsides Priced In

- Strong quarter, but no surprises** — Unitech's consolidated 2QFY08 revenues and earnings recorded strong growth on a YoY and QoQ basis, largely in-line. This was largely on back of pre-sold volumes at higher price realizations early on. Higher other income - gains on sale of investments (Rs200m) and dividend (Rs120m) and lower tax provisions, also contributed toward this growth.
- Large addition to landbank** — The company added 1,750 acres of land in Visakhapatnam, a port city in Andhra Pradesh, for developing an integrated township with ~102m sq ft (~22% additional volumes) over a 10-year period. It continues to aggregate land in newer markets, which will be disclosed in due course once complete; hence presently not factored into our estimates.
- Thrust on asset monetization** — Having monetized part holding in 6 IT Parks early on to UCP the AIM Fund – Unitech is now exploring opportunities to list a business trust in Singapore for some of its IT Park assets (12% of asset portfolio), which are expected to commence leasing over the next 1-2 years; but given the evolving regulatory issues, timing remains uncertain.
- Raising target to Rs314** — This is based on a 15% premium on our increased NAV of Rs273 (vs. Rs215 based on Mar'07 earlier) as we roll forward to Mar'08 and factor in the landbank addition at Vishakhapatnam - adds ~Rs21 to NAV.
- Maintain Sell (3M)** – As stock trades at 37% premium significantly higher than our 15% premium and our increased TP; we believe upsides are priced in.

Sell/Medium Risk	3M
Price (30 Oct 07)	Rs374.40
Target price	Rs314.00
	from Rs247.50
Expected share price return	-16.1%
Expected dividend yield	0.1%
Expected total return	-16.1%
Market Cap	Rs607,792M
	US\$15,448M

Price Performance (RIC: UNTE.BO, BB: UT IN)



Statistical Abstract

Year to	Net Profit	Diluted EPS	EPS growth	P/E	P/B	ROE	Yield
31 Mar	(RsM)	(Rs)	(%)	(x)	(x)	(%)	(%)
2006A	841	0.52	152.0	nm	nm	36.9	0.0
2007A	13,058	8.04	na	46.5	30.5	115.9	0.1
2008E	16,374	10.09	25.4	37.1	16.9	58.6	0.1
2009E	27,542	16.97	68.2	22.1	9.6	55.7	0.1
2010E	41,908	25.82	52.2	14.5	5.8	50.0	0.1

Source: Powered by dataCentral

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¹Citigroup Global Markets India Private Limited

Fiscal year end 31-Mar	2006	2007	2008E	2009E	2010E
Valuation Ratios					
P/E adjusted (x)	nm	46.5	37.1	22.1	14.5
P/E reported (x)	nm	46.5	37.1	22.1	14.5
P/BV (x)	nm	30.5	16.9	9.6	5.8
Dividend yield (%)	0.0	0.1	0.1	0.1	0.1
Per Share Data (Rs)					
EPS adjusted	0.52	8.04	10.09	16.97	25.82
EPS reported	0.52	8.04	10.09	16.97	25.82
BVPS	1.60	12.29	22.11	38.83	64.39
NAVps ordinary	na	na	na	na	na
DPS	0.12	0.29	0.25	0.25	0.25
Profit & Loss (RsM)					
Net operating income (NOI)	2,427	19,565	29,435	46,495	69,064
G&A expenses	-1,077	0	-2,981	-3,459	-5,116
Other Operating items	-110	-66	-231	-289	-550
EBIT including associates	1,240	19,499	26,222	42,747	63,399
Non-oper./net int./except.	152	-1,567	-3,481	-3,956	-4,373
Pre-tax profit	1,392	17,933	22,741	38,791	59,025
Tax	-513	-4,864	-6,368	-11,249	-17,117
Extraord./Min. Int./Pref. Div.	-38	-11	0	0	0
Reported net income	841	13,058	16,374	27,542	41,908
Adjusted earnings	841	13,058	16,374	27,542	41,908
Adjusted EBIT	1,238	19,485	26,222	42,747	63,399
Adjusted EBITDA	1,350	19,565	26,454	43,036	63,949
Growth Rates (%)					
NOI	95.1	706.1	50.4	58.0	48.5
EBIT adjusted	211.5	nm	34.6	63.0	48.3
EPS adjusted	152.0	nm	25.4	68.2	52.2
Cash Flow (RsM)					
Operating cash flow	-2,165	-21,520	10,539	8,922	9,554
Depreciation/amortization	113	80	231	289	550
Net working capital	-2,180	-46,788	7,234	-19,634	-33,674
Investing cash flow	-3,127	-7,229	-5,608	-5,292	-6,852
Capital expenditure	-3,485	-2,826	-5,608	-5,292	-6,852
Acquisitions/disposals	0	0	0	0	0
Financing cash flow	6,474	35,077	104	1,962	2,020
Borrowings	6,686	29,356	510	2,368	2,426
Dividends paid	-188	-477	-406	-406	-406
Change in cash	1,182	6,328	5,035	5,592	4,722
Balance Sheet (RsM)					
Total assets	44,522	130,900	131,815	180,846	238,005
Cash & cash equivalent	3,899	10,227	15,262	20,854	25,576
Net fixed assets	4,887	8,148	12,904	17,907	23,939
Total liabilities	41,688	110,944	95,905	117,800	133,458
Total Debt	10,449	39,805	40,315	42,683	45,109
Shareholders' funds	2,834	19,956	35,910	63,045	104,548
Profitability/Solvency Ratios					
EBIT margin adjusted (%)	13.9	60.1	48.4	49.4	49.6
ROE adjusted (%)	36.9	115.9	58.6	55.7	50.0
ROA adjusted (%)	2.4	14.9	12.5	17.6	20.0
Net debt to equity (%)	231.1	148.2	69.8	34.6	18.7
Interest coverage (x)	2.9	6.5	6.1	8.6	11.6

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Key Points

Strong 2Q, but no surprises

Figure 1. Unitech Consolidated 2QFY08 and 1HFY08 Earnings Summary (Rs Millions)

	1QFY08	2QFY07	2QFY08	YoY	QoQ	1HFY07	1HFY08	YoY
Sales	8,656	4,306	10,135	135%	17%	7,348	18,843	156%
EBITDA	5,005	1,411	5,071	259%	1%	2,209	10,128	358%
EBITDA Mgn (%)	57.8%	32.8%	50.0%			30.1%	53.8%	
Interest	601	216	790	265%	31%	363	1,391	284%
Other Income	341	98	508	419%	49%	496	796	61%
Depreciation	32	17	30	78%	-5%	31	62	102%
PBT	4,714	1,275	4,759	273%	1%	2,312	9,472	310%
PAT	3,667	1,034	4,099	296%	12%	1,807	7,766	330%
PAT after Minority Int & Assoc	3,657	1,030	4,101	298%	12%	1,800	7,758	331%

Source: Company Reports, Citi Investment Research

Increasing our NAV estimate to Rs273 (vs. Rs215 earlier) as development volume increases to 561m sq ft

Landbank addition, increases NAV Estimate

We are increasing our NAV estimate for Unitech to Rs273 (compared to Rs215 earlier) factoring in the large land bank addition in Visakhapatnam and roll forward to Mar '08 (vs. Mar'07 earlier). Our revised NAV estimate is based on a development volume of 561m sq ft compared to ~471m sq ft earlier.

Large acquisition at Visakhapatnam

Unitech recently acquired 1,750 acres of land at Kapuluppada near Visakhapatnam, a port city, from Andhra Pradesh Industrial Infrastructure Corporation (APIIC) for development of 'Vizag Knowledge City'. As per the arrangement, Unitech will be required to pay a total of Rs.32.9bn over a 10-year period for the land parcel, which on an NPV basis (using discount rate of 14%) is an outflow of ~Rs.17bn as per our estimates. The Knowledge City will be an integrated eco-friendly township with environment friendly apartments, office space, hotels, shopping complexes and facilities for leisure tourism. The project will have a total saleable area of ~102m sq ft being a mix of villas, residential apartments, IT Parks, retail space, hotels and other utilities, which will be developed over a period of 10 years. We expect this project to add ~22% additional volumes and foresee it contributing ~Rs.21 per share to our NAV estimate.

Figure 2. Visakhapatnam Land Development Summary

	Acres
Villas	400
Apartments	600
IT Park	65
Hotels & Resorts	10
Retail	20
Golf Course	105
Schools, Hospitals, Roads	550
Total	1,750

Source: Company Reports, CIR

Exploring opportunities to sell more assets to sponsored Trusts/REITs – but timing uncertain, given the evolving regulatory issues

Thrust on monetizing assets, but timing still uncertain

With Unitech's initial success in monetizing part of its 6 IT parks early on to UCP, the AIM Fund – it is now exploring opportunities to sell more of its IT Park/IT SEZ assets in strategic locations such as Gurgaon, Noida, Kolkata, which are expected to commence leasing over the next 1-2 years to sponsored Trusts/REITs listed in Singapore. This, we believe, should provide Unitech with some benefit from the cap rate compression and boost cash flows. However, the timing of these structures materializing still remains uncertain given the evolving regulatory issues.

Management, plans to grow the telecom business; but probability of new players getting spectrum is remote

Other developments

- **Develop 28 hotels (~5000 rooms) across key cities** – Construction is already ongoing on 4 properties. Unitech could potentially look at early asset sales once the projects are close to getting operational.
- **Plans to scale up presence in telecoms** – Unitech has submitted an application to DoT for a Unified Access Service license in 22 circles. As per the management, this is in-line with its plans to grow the telecom business, apart from its existing telecom tower manufacturing for operators such as Hutch (now Vodafone). However, as per our telecom analyst - the ability for new players to get spectrum appears remote, given the shortage of spectrum. That said, should it be able to get any spectrum, we could see significant value being created from this business – but given the uncertainty, we have not built any upside from this into our estimates.

Unitech

Company description

Unitech is one of India's largest, most diversified real estate developers with an emerging pan-India presence. It enjoys leadership in markets of NCR and Kolkata. Its core strengths of land acquisition, reputation in building townships and relationships with governments and customers have enabled it to build a diversified portfolio. Unitech has a land bank of 12,511 acres with a total saleable area of ~593m sq ft spread over Chennai (19%), NCR (16%), Kolkata (16%) and Tier III cities (44%). Residential projects account for about 77% of the saleable area, commercial 5%, IT Parks 7% and retail 5%. In addition, it also has a small presence in power transmission, prefabricated construction, paving block and ready mix concrete. The promoter family holds a 75% stake in the company.

Investment strategy

We rate Unitech Sell/Medium Risk (3M) rating with a higher target price of Rs314 (vs. Rs247.5 earlier). Our increased target is based on a 15% premium to our revised NAV estimate of Rs273 per share. Recent efforts to monetize six of its IT parks by selling stakes to a REIT has provided it with healthy cash flows – and we expect more such structures going forward, but timing remains uncertain. Additionally, initiatives to reduce concentration in NCR and introduce new revenue streams from lease/management fees are positive. However, management's development plan of ~593mn sq ft is aggressive and does raise execution risks. We forecast an exponential growth in profitability from FY07-10E. With stock already trading at 37% premium significantly higher than our 15% premium, we believe valuations do not leave any margin for error from potential execution delays; upsides seem priced in, in our view.

Valuation

We increase our target price to Rs314 (vs. Rs247.5 earlier) based on a 15% premium to our increased NAV of Rs273 – due to large land-bank addition at Vishakapatnam (which translates to ~22% additional volumes) and roll forward to Mar'08E (vs. Mar'07 earlier). The 15% premium is based on high valuation

benchmarks for Tier-I developers and recognizing Unitech's - 1) competitive advantage of large diversified land bank, while peers are still aggregating land 2) dynamic business model with thrust on recycling capital faster; 3) strong brand positioning and proven track record. However, this is lower than the 25% premium we ascribe to DLF due to its - higher gearing towards commercial assets, ability to leverage on asset holding company for boosting cash flows and increased leasing income.

Figure 3. NAV Summary (Rs Millions)

Gross NAV of Residential	517,161
Gross NAV of Non-Residential	277,974
Gross Total NAV	795,134
Less: Amt outstanding for land	52,085
Less: Tax @ 28%	208,054
Less: Debt Outstanding	57,194
Less: Customer Advances	48,230
Add: Cash	13,927
Net NAV	443,498
No. of Shares Outstanding (Millions)	1623
NAV Per Share (Rupees)	273

Source: Citi Investment Research

Our NAV estimate of Rs273 is based on the following assumption: a) current market price levels to sustain with no price inflation; b) development volume of 561m sq ft (~32m sq ft recognized as revenue up to FY08) c) all projects undertaken will be completed largely as per schedule though, we expect risk of delays; d) average cost of capital of 14%; and e) tax rate of 28%. With stock already trading at a significant premium to NAV, above our estimate we believe upsides are priced in at current valuations.

Risks

We rate Unitech Medium Risk. Key reasons for Medium Risk rating are: 1) low-risk/high-return business model 2) pan-India land bank with initiatives to reduce weightage on NCR 3) relatively healthy cash flows. Main company-specific risks include: 1) Developments on monetization of retail and hotel assets similar to IT Parks, could result in healthy cash flows and should positively drive profitability and valuations 2) any developments providing higher visibility on execution of large SEZ projects not included in our NAV estimate is likely to create long-term value 3) Any interest rate reversals, would positively impact earnings growth assumption. If any of these risk factors plays out, Unitech's share price is likely to have difficulty attaining our target price.

Appendix A-1

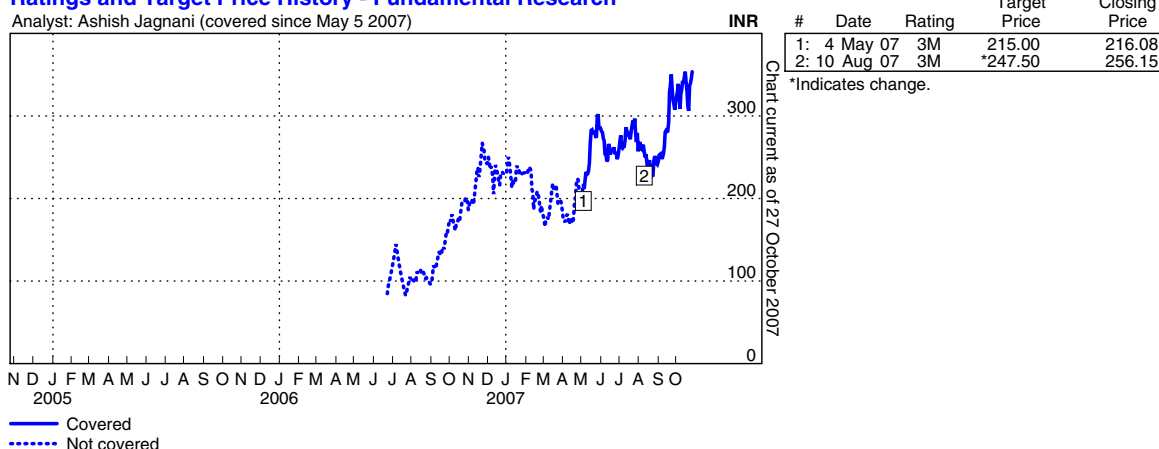
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Analyst: Ashish Jagnani (covered since May 5 2007)



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