Company Focus

2 January 2008 | 16 pages

Hindustan Construction (HCNS.BO)

Downgrade to Sell Following Share Price Outperformance

Change in opinion ☑
Rating change ☑
Target price change ☑
Estimate change ☑

- **Target price Rs208** — We are downgrading the stock to Sell/Low Risk (3L) from Buy/Low Risk (1L) given downside to our new target price of Rs208 and its outperformance of the BSE Sensex of more than 50% in the past 3–6 months on the Lavasa Phase I launch.
- **Rollover of target multiple** — We are raising our target price to Rs208 from Rs130 as we: 1) Increase our target multiple to 17x (from 16x earlier) and roll forward our target multiple to September 2009 from March 2009 in line with its peers; and 2) take a more constructive view with our real estate valuations and increase the value of real estate projects to Rs116, from Rs39 earlier.
- **Early advantage lost** — HCC has lost its higher margins and larger size advantage over the past two years due to what we believe is poor project selection. Younger and more nimble companies, like Nagarjuna Construction and IVRCL, have not only caught up with HCC, but have also grown larger in terms of the profits generated from their core E&C businesses.
- **Margins expand, but no growth** — Despite significant margin expansion in 1HFY08 (respite on the BWSL losses) the company has not shown growth at the recurring PBT level because of high interest and depreciation costs.
- **Private equity will help set benchmark** — We believe it is critical that HCC Real Estate ropes in private equity for the Lavasa project. This would not only provide funds but would also help establish a reasonable valuation benchmark given the lack of information on the project to undertake a detailed valuation.

Sell/Low Risk	**3L**
from Buy/Low Risk	
Price (01 Jan 08)	Rs242.75
Target price	Rs208.00
from Rs130.00	
Expected share price return	-14.3%
Expected dividend yield	0.4%
Expected total return	**-14.0%**
Market Cap	Rs62,205M
	US$1,578M

Price Performance (RIC: HCNS.BO, BB: HCC IN)

Figure 1. HCC – Statistical Abstract

Year to	Net Profit	EPS	EPS Growth	P/E	Adj. P/E	EV / EBITDA	Adj EV/EBITDA	P / Book	ROE	DPS	Div. Yield
31-Mar	(Rsmn)	(Rs)	(%)	(x)	(x)	(x)	(x)	(x)	(%)	(Rs)	(%)
FY05A	661	2.88	66.8%	84.2	43.3	37.9	20.5	15.8	25.6%	0.60	0.2%
FY06A	858	3.13	8.6%	77.6	39.8	35.6	19.1	7.0	13.8%	0.70	0.3%
FY07A	751	2.74	-12.5%	88.6	45.5	35.1	21.0	6.9	8.4%	0.75	0.3%
FY08E	770	2.81	2.5%	86.5	44.4	22.9	14.1	6.3	8.2%	0.85	0.4%
FY09E	1,251	4.44	58.2%	54.7	28.1	18.5	11.4	5.2	11.3%	0.95	0.4%
FY10E	1,742	6.18	39.2%	39.3	20.2	15.2	9.5	4.7	13.4%	1.05	0.4%

Source: Company reports and Citi Investment Research estimates

See Appendix A-1 for Analyst Certification and important disclosures.

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Fiscal year end 31-Mar	2006	2007	2008E	2009E	2010E
Valuation Ratios					
P/E adjusted (x)	77.6	88.6	86.5	54.7	39.3
EV/EBITDA adjusted (x)	35.1	32.0	21.9	17.5	14.3
P/BV (x)	7.0	6.9	6.3	5.2	4.7
Dividend yield (%)	0.3	0.3	0.4	0.4	0.4
Per Share Data (Rs)					
EPS adjusted	3.13	2.74	2.81	4.44	6.18
EPS reported	4.55	2.89	3.86	4.44	6.18
BVPS	34.72	35.28	38.42	46.72	52.11
DPS	0.70	0.75	0.85	0.95	1.05
Profit & Loss (RsM)					
Net sales	19,870	23,576	30,515	37,399	45,627
Operating expenses	-18,567	-22,220	-28,194	-34,318	-41,708
EBIT	**1,303**	**1,356**	**2,321**	**3,081**	**3,918**
Net interest expense	-414	-620	-1,194	-1,319	-1,429
Non-operating/exceptionals	42	293	21	105	110
Pre-tax profit	**931**	**1,030**	**1,149**	**1,867**	**2,600**
Tax	-73	-279	-379	-616	-858
Extraord./Min.Int./Pref.div.	389	42	288	0	0
Reported net income	**1,247**	**793**	**1,058**	**1,251**	**1,742**
Adjusted earnings	858	751	770	1,251	1,742
Adjusted EBITDA	1,827	2,153	3,421	4,383	5,422
Growth Rates (%)					
Sales	33.6	18.7	29.4	22.6	22.0
EBIT adjusted	17.8	4.1	71.2	32.7	27.2
EBITDA adjusted	17.2	17.8	58.9	28.1	23.7
EPS adjusted	8.6	-12.5	2.5	58.2	39.2
Cash Flow (RsM)					
Operating cash flow	**-2,152**	**-4,951**	**172**	**99**	**1,722**
Depreciation/amortization	524	797	1,100	1,302	1,504
Net working capital	-3,877	-6,718	-1,985	-2,454	-1,524
Investing cash flow	**-1,504**	**-4,798**	**-2,830**	**-2,300**	**-2,600**
Capital expenditure	-2,139	-3,776	-2,500	-2,000	-2,500
Acquisitions/disposals	634	-1,022	-330	-300	-100
Financing cash flow	**12,842**	**1,882**	**1,346**	**2,127**	**977**
Borrowings	8,722	2,532	1,600	900	1,300
Dividends paid	-204	-225	-254	-292	-323
Change in cash	**9,186**	**-7,866**	**-1,311**	**-74**	**99**
Balance Sheet (RsM)					
Total assets	**30,327**	**34,323**	**38,886**	**44,652**	**50,249**
Cash & cash equivalent	10,061	2,194	883	809	909
Accounts receivable	28	5	6	8	9
Net fixed assets	5,995	8,974	10,374	11,072	12,069
Total liabilities	**21,429**	**25,282**	**29,041**	**32,330**	**36,506**
Accounts payable	5,910	6,796	8,433	10,294	12,559
Total Debt	12,978	15,511	17,111	18,011	19,311
Shareholders' funds	**8,898**	**9,041**	**9,845**	**12,323**	**13,743**
Profitability/Solvency Ratios (%)					
EBITDA margin adjusted	9.2	9.1	11.2	11.7	11.9
ROE adjusted	13.8	8.4	8.2	11.3	13.4
ROIC adjusted	14.0	6.5	8.4	9.3	10.4
Net debt to equity	32.8	147.3	164.8	139.6	133.9
Total debt to capital	59.3	63.2	63.5	59.4	58.4

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Downgrade to Sell

- We are downgrading HCC to Sell/Low Risk (3L) from Buy/Low Risk (1L) as the stock has outperformed the BSE Sensex by more than 50% in the last 3–6 months on the Lavasa Phase – I launch.
- Despite significant margin expansion in 1HFY08 (signs of respite on the BWSL losses) the company has not shown growth at the recurring PBT level because of high interest and depreciation costs.
- Over the past two years, despite its good reputation, high margins and its scale advantage over other mid-cap construction companies, HCC has lost its early advantage in the Indian E&C space. Younger, more nimble companies like Nagarjuna Construction and IVRCL have not only caught up with HCC, but have also grown larger in terms of the profits generated from the core E&C business. We are downgrading HCC to Sell given downside to our new target price of Rs208.

Figure 2. HCC v/s BSE Sensex Price Performance

Comparative Performance	3 Years	2 Years	1 Year	6 Month	3 Months
HCC	538%	88%	58%	89%	70%
BSE Sensex	207%	116%	47%	38%	17%
HCC v/s BSE Sensex	330%	-28%	11%	51%	53%

Source: DataCentral Citi Investment Research

Peer Comparison

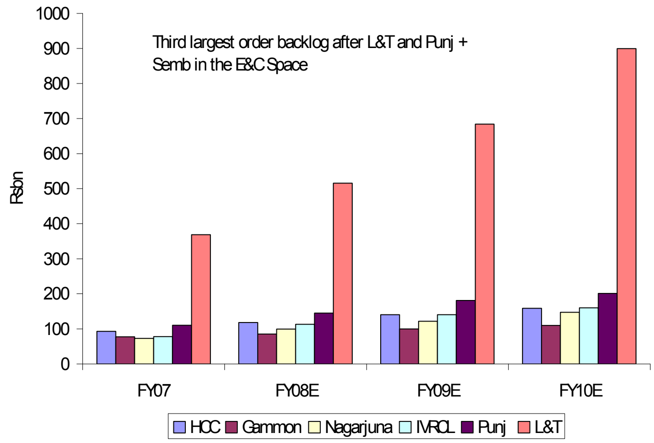
Figure 3. Indian E&C Valuation Comparables

		L&T	Punj Lloyd	HCC	Nagarjuna	Gammon	IVRCL
RIC Code		LART.BO	PUJL.BO	HCNS.BO	NJCN.BO	GAMM.BO	IVRC.BO
Recommendation		3L	1L	3L	1L	1L	1L
Price (Rs)		4145	566	240	358	601	543
Value of BOT/Real Estate/Subsidiary		527	33	118	56	257	190
Mkt Cap US$mn		28,636	3,607	1,500	1,821	1,272	1,717
EPS CAGR (FY07-10E)		41.0%	55.0%	31.2%	37.9%	32.7%	39.6%
P/E	FY08E	58.2	46.7	85.5	43.8	45.6	42.1
P/E	FY09E	41.6	30.1	54.0	27.4	32.1	27.2
P/E	FY10E	31.3	21.8	38.8	21.9	22.7	19.0
Adj. P/E	FY08E	50.8	44.0	43.4	36.9	26.1	27.4
Adj. P/E	FY09E	36.3	28.4	27.5	23.1	18.4	17.7
Adj. P/E	FY10E	27.3	20.5	19.7	18.4	13.0	12.4
EV/EBITDA	FY08E	41.8	22.7	22.7	24.7	24.5	22.4
EV/EBITDA	FY09E	29.7	16.2	18.4	17.7	18.3	14.1
EV/EBITDA	FY10E	22.3	12.2	15.1	14.8	13.6	10.1
Adj. EV/EBITDA	FY08E	36.5	21.5	13.9	21.2	14.7	15.4
Adj. EV/EBITDA	FY09E	26.0	15.3	11.3	15.2	11.0	9.2
Adj. EV/EBITDA	FY10E	19.5	11.5	9.3	12.8	8.2	6.5
RoE	FY08E	31.6%	21%	8%	15%	12%	12%
RoE	FY09E	33.7%	22%	11%	17%	15%	16%
RoE	FY10E	33.6%	24%	13%	17%	18%	20%

Note: Adj metrics are computed ex – value of BOT/Real Estate/Subsidiary and Priced as of January 1, 2007

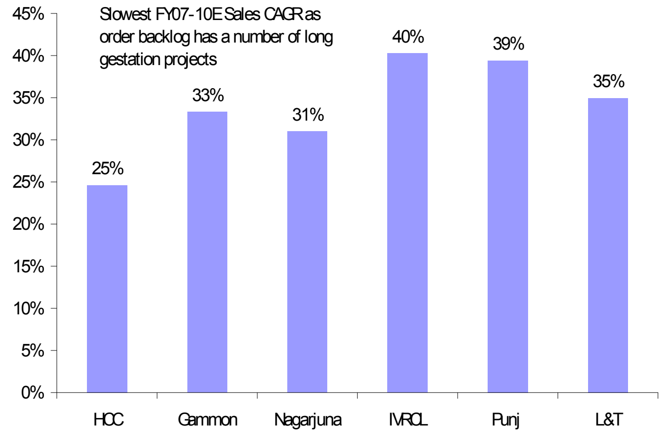
Source: Citi Investment Research estimates

Figure 4. Indian E&C – Order Backlog Comparison



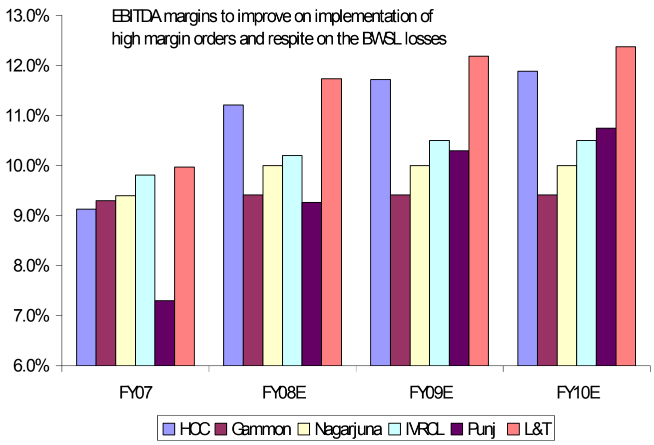
Source: Citi Investment Research estimates

Figure 5. Indian E&C Sale CAGR FY07-10E Comparison



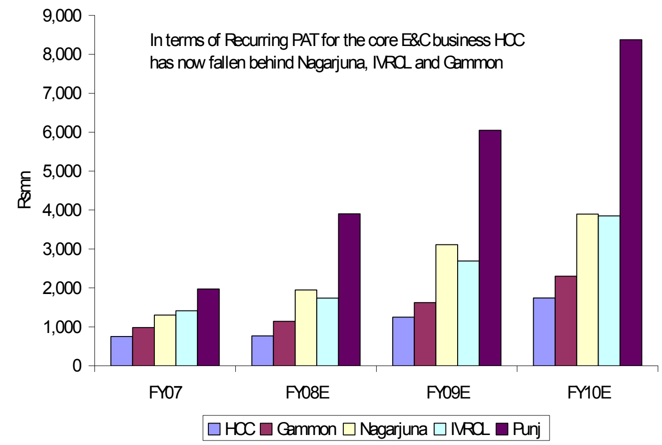
Source: Citi Investment Research estimates

Figure 6. Indian – E&C Order EBITDA Margin Comparison



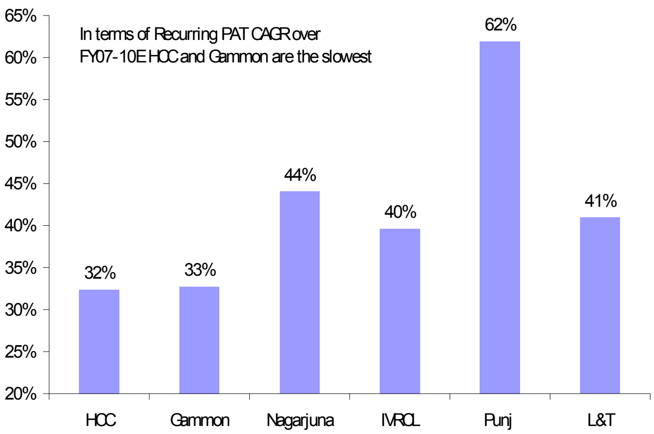
Source: Citi Investment Research estimates

Figure 7. Indian E&C – Recurring PAT Comparison



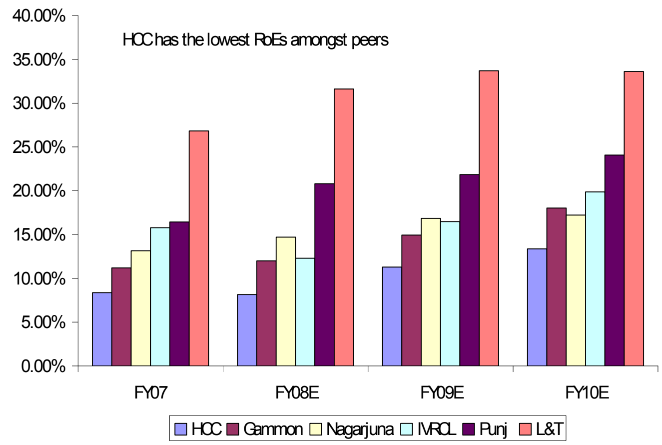
Source: Citi Investment Research estimates

Figure 8. Indian E&C – Recurring PAT CAGR FY07 - 10E Comparison



Source: Citi Investment Research estimates

Figure 9. Indian E&C – RoE Comparison



Source: Companies, Citi Investment Research estimates

Target price of Rs208

We are riasing our target price to Rs208 from Rs130 earlier as:

- We increase our target P/E multiple to 17x from 16x earlier and roll forward the same to September 2009 from March 2009, in line with peers like Gammon and IVRCL. We peg Nagarjuna at 19x as we believe it is structurally moving up the value chain with its entry into the metals and pipelines space.

- We take a more constructive view with our real estate valuations and increase the value of real estate projects to Rs116 from Rs39 earlier, based on the following figures:

  1. **Lavasa:** 12,500 acres of land at Rs3mn/acre vis-à-vis 9,100 acres at Rs2mn/acre earlier on launch of Lavasa Phase I

  2. **Vikhroli (West):** DCF of post tax rentals for 1.9mn sqft

  3. **Vikhroli (East) :** 1.6mn sqft of slum encroached land at Rs800/sqft

  4. **1500 acres of land:** For the other projects HCC is building its land bank across various cities in Maharashtra such as Mumbai, Pune, Nasik, Aurangabad and Navi Mumbai. HCC has contracted ~ 1500 acres of land across various cities which we value at acquisition cost of Rs2bn.

Figure 10. HCC – Sum of the Parts

Part	Remark	Value
Construction Business	**P/E of 17x Sep09E**	**90**
AP - 8 & Pune Paud BOT Projects	**P/Equity Investment of 1.2x**	**3**
Lavasa Project - 63% Stake	12,500 acres of land at Rs3mn/acre less Rs3.75bn of debt	78
Vikhroli (West) -100% Stake	DCF of post tax rentals for 1.9mn sqft @ Rs65/sqft	26
Vikhroli (East) - 100% Stake	1.6mn sqft @ Rs800/sqft	5
1500 acres of land	At acquisition cost of Rs2bn	7
Real Estate Value		**116**
Target Price		**208**

Source: Citi Investment Research estimates

Figure 11. HCC – Earnings Revision Table

	FY08E	FY09E	FY10E
Sales			
Old	30,200	37,099	44,609
New	30,515	37,399	45,627
% Chg	1%	1%	2%
EBITDA			
Old	2,806	4,196	5,130
New	3,421	4,383	5,422
% Chg	22%	4%	6%
EBITDA Margin %			
Old	9.3%	11.3%	11.5%
New	11.2%	11.7%	11.9%
% Chg	192bps	41bps	38bps
Recurring PAT			
Old	803	1,507	1,931
New	770	1,251	1,742
% Chg	-4%	-17%	-10%
FD EPS			
Old	2.93	5.50	7.04
New	2.81	4.44	6.18
% Chg	-4%	-19%	-12%

Source: Citi Investment Research estimates

Downward earnings revisions

We are reducing our earnings estimates by 4% to 19% over FY08E- FY10E as we factor in:

- Marginal changes to our sales estimates
- Higher EBITDA margins from FY08E as the Bandra Worli Sealink project draws to a close. The margin improvement that we had expected from 1QFY09E began in 1HFY08E as HCC is booking lower losses
- Our Recurring PAT numbers are lower on account of higher interest and depreciation costs
- Dilution on account of the recent issuance of 7.5mn preferential warrants convertible into shares at Rs202.50 in the next 18 months

We now expect HCC to grow EPS at a CAGR of 31% over FY07-10E, vis-à-vis 37% earlier, with RoE at 8 – 15%.

Figure 12. HCC – Key Assumptions

Year Dec31 (Rsmn)	FY05	FY06	FY07	FY08E	FY09E	FY10E	FY07-10E
Order Book e-o-y	53,810	96,720	93,120	118,450	140,657	158,595	19.4%
OB e-o-y/Turnover (x)	3.41	4.77	3.89	3.88	3.76	3.48	-
Sales	14,873	19,870	23,576	30,515	37,399	45,627	24.6%
EBITDA	1,559	1,827	2,153	3,421	4,383	5,422	36.1%
EBITDA Margins	10.5%	9.2%	9.1%	11.2%	11.7%	11.9%	
EBIT	1,106	1,303	1,356	2,321	3,081	3,918	42.4%
EBIT Margins %	7.4%	6.6%	5.8%	7.6%	8.2%	8.6%	
Tax Rate %	8.3%	7.8%	27.1%	33.0%	33.0%	33.0%	
Recurring PAT	661	858	751	770	1,251	1,742	32.4%
PAT Margins %	4.4%	4.3%	3.2%	2.5%	3.3%	3.8%	

Source: Company reports, Citi Investment Research estimates

EBITDA margin improvement not translating into growth

HCC's improving EBITDA margin in 1HFY08 have not translated into significant growth of recurring PAT. It could be argued that because of removal of Section 80 I (A) benefits, PAT numbers are not comparable on a YoY basis. However, with close observation, there is hardly any growth at the recurring PBT levels on account of both higher interest and depreciation costs.

We can trace back the incidence of high capital costs to the order wins of FY06, which included a number of large long gestation orders. This resulted in HCC investing heavily on equipment and leveraging over the past two years.

Exceptional items have largely driven the strong reported PAT growth.

Figure 13. HCC – 1HFY08 Results

Year End Mar31 (Rsmn)	1Q07	1Q08	% YoY	2Q07	2Q08	% YoY
Order Book Position	91,430	93,810	2.6%	98,190	96,020	-2.2%
Net Sales	**5,806**	**7,306**	**25.8%**	**4,257**	**5,487**	**28.9%**
Less: JV	(71)	(15)		(54)	0	
Income	**5,735**	**7,290**	**27.1%**	**4,202**	**5,487**	**30.6%**
EBITDA	**454**	**788**	**73.6%**	**394**	**601**	**52.6%**
EBITDA Margin	**7.9%**	**10.8%**		**9.4%**	**11.0%**	
Depreciation	(161)	(228)	40.9%	(186)	(226)	21.6%
EBIT	**292**	**560**	**91.7%**	**208**	**375**	**80.4%**
EBIT Margin	**5.1%**	**7.7%**		**4.9%**	**6.8%**	
Interest	(74)	(322)	334.1%	(158)	(342)	116.7%
Other Income	2	6	150.2%	10	6	-38.1%
Company' share of Profit/(Loss) in JVs	0	(3)		0	0	
PBT	**220**	**241**	**9.3%**	**60**	**39**	**-34.2%**
PBT Margin	**3.8%**	**3.3%**		**1.4%**	**0.7%**	
Total Tax	(16)	(89)	453.6%	(19)	(13)	-32.3%
Tax Rate	7.3%	37.0%		32.1%	33.0%	
Recurring PAT	**204**	**152**	**-25.7%**	**41**	**26**	**-35.1%**
Exceptional	7	315		1	100	
Capital Gains on Transfer of DR	60	0		0	0	
Tax Adjustment	(20)	(117)		0	(10)	
Reported PAT	**251**	**350**	**39.2%**	**42**	**116**	**178.9%**

Source: Company, Citi Investment Research

Respite in sight on the Bandra Worli Sealink (BWSL) project

HCC won the Bandra Worli Sealink project in 2001. This was supposed to reach completion in 30 months at a cost of Rs4bn. However, protests by environmentalists forced the client, Maharashtra State Road Development Corporation (MSRDC), to change the design and consultants, leading to cost escalations. The original project cost of Rs4.0bn escalated by Rs3.4bn. HCC has already booked losses to the tune of Rs2.5bn up to 1QFY08. The company expects to complete the project by March 2009.

Figure 14. Bandra Worli Sealink Project

Source: Company

Gradually shedding its BOT conservatism

- HCC has taken a conservative approach vis-à-vis companies such as L&T and Gammon in avoiding build-operate-transfer (BOT) projects. BOT projects are long gestation, capital-intensive projects. Whereas L&T and Gammon have gained valuable experience over the years by involving themselves in numerous BOT projects, HCC has preferred a “wait and watch” approach. If we analyze the next round of ordering in roads, ports, hydroelectric power and power transmission sectors, we see that the government is showing an increased preference for BOT projects as public funds are stretched. Securing a BOT project is advantageous to the cash contracts business of the BOT operator, as they typically contract the cash contract of the project to themselves.

- HCC took its first step in the BOT direction with the Pune Paud road project, which has a total cost of Rs300m (debt: Rs260m, equity: Rs40m). The company expects to make equity IRR of 15-16% on the project. In 1QFY07, HCC won its second BOT project - an annuity road project for the development of 30km four-lane highway between Kadtal and Armur in Andhra Pradesh. The project cost is Rs2.75bn (debt: Rs2.2bn, equity: Rs550mn), and the semi-annual annuity payments is Rs238mn to be paid over 18 years (36 semi annual instalments).

Lavasa project soft launched in October 2007

- The 12,500 acres/150mn sqft Lavasa project comprises of plotted land, apartments, retail outlets, hotels, IT and biotech parks, event centres, convention centres and recreational facilities.

- The company has signed MoUs with Accor Hotels who are setting up two hotels (150 and 250 rooms) under the Novotel and Grand Mercure brands. It also expects Starwood Hotels to set up a 250-room hotel with a convention centre and a 200-room resort. The ITC Fortune hotel is under construction. Test sales on the low-end apartment block initially yielded Rs1,800 – 1,900/sqft. The company expects that it will take about 10 years to populate the entire place, but Lavasa might be decently populated by 2012.

- Out of the 12,500 acres of land scheduled for purchase by HCC Real Estate, it has already acquired 9,100 acres (in terms of complete payment, title transfer and sale deeds). It plans to acquire a further 2,000 acres in the near future. Interestingly 7,800 acres have been mortgaged to banks for loans, which provides us a good amount of comfort.

- Up to September 2007, Rs7bn was invested in Phase I, made up of Rs2.5bn of equity and Rs4.5bn of debt. Phase I of the Lavasa project is likely to cost Rs12–13bn, which will be financed by Rs5.5bn of debt, 2.5bn of equity from promoters and Rs3bn of private equity money/pre sales. Post Phase I the project will move into a self financing mode.

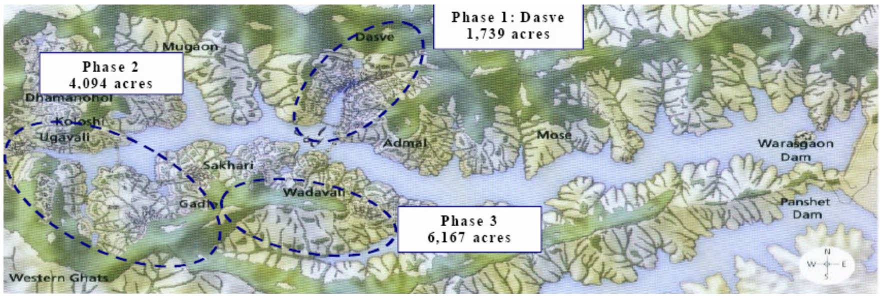
- The basic infrastructure for access to the property and ancillary infrastructure such as dams for water bodies and walkways are complete.

- The soft launch of the sale of plots, bungalows and apartments at Lavasa started on 22 October, 2007. It completed booking for 300 bungalows and apartments on offer in Phase I at values ranging from Rs1mn to Rs10mn (average realization of Rs2,900/sq ft). Total revenue from the sale of the units stands at Rs3.0bn and revenue booking for the project will start from 1QFY09.

- Lavasa has also signed various joint venture agreements with (1) Girls Day School Trust (GDST - An education trust in Europe managing 27 institutes, including Oxford University) to set up a university at Lavasa, (2) Apollo Hospitals (51% stake for Apollo and 49% for Lavasa) to set up a hospital and wellness centre with a 50-bed hospital on 200 acres to come up by October 2009, 3) Ecole Hotelier, Switzerland to run a hospitality and culinary school from June 2009 (first academic year).

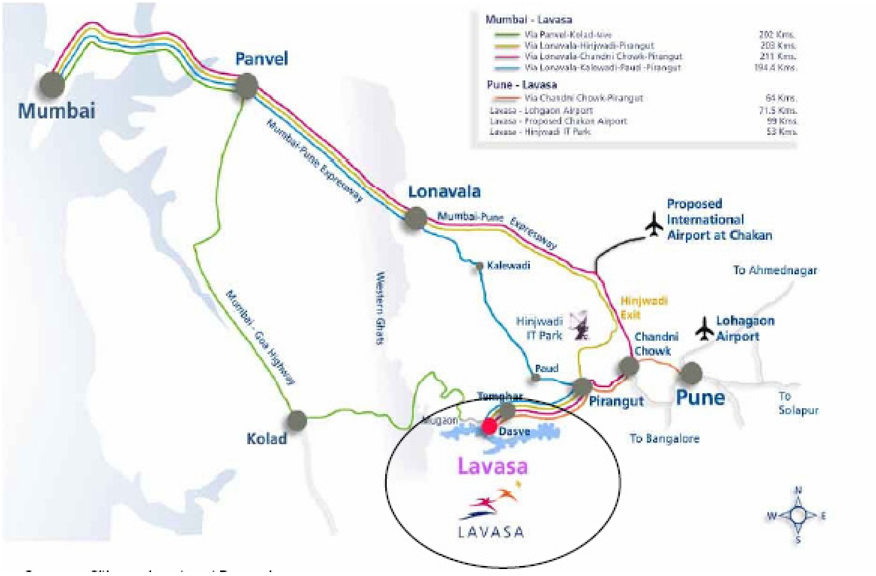
- *We believe it is critical that HCC Real Estate manages to rope in private equity players for the Lavasa project. This would not only provide funds but would also help establish a reasonable valuation benchmark given the lack of information on the project to undertake a detailed valuation exercise.*

Figure 15. Lavasa Development Plan



Source: Company

Figure 16. Lavasa Project



Source: Company

Figure 17. Lavasa – Dasve Site View

Source: Company

Figure 18. Lavasa Phase – I Artist's Impression - 1

Source: Company

Vikhroli (West) Project

- Construction work has begun on the Vikhroli (West) IT Park and the company expects rentals of Rs65–70/sqft/month for the project. Offices should be ready for fit out by Dec 2008, for occupation by Mar2009, and the company should start booking revenues from 4QFY09.

Figure 19. Vikhroli West IT Park – Under Development

Source: Company

Other real estate projects

- For the Vikhroli (East) SRS Projects the requisite consents of the slum dwellers is expected in 3-4 months
- For its other projects, HCC is building its land bank across various cities in Maharashtra, such as Mumbai, Pune, Nasik, Aurangabad and Navi Mumbai. HCC has already contracted nearly 1500 acres of land across various cities. To date, HCC has invested Rs2bn on land acquisition.

Figure 20. HCC – Real Estate Development

	Acres	mn sqft
Lavasa (UD)	12,500	150.0
Vikhroli West (UD)	11	1.9
Residential Project in Mumbai SRS (UD)	12	1.5
Vikhroli East SRS (UD)	15	1.6
Township in MMR	200	3.0
SEZ/ Township in Nashik	1,000	21.8
Township in Pune	300	6.5
Total	**14,038**	**186.3**

Source: Company, Citi Investment Research

Hindustan Construction

Company description

HCC is an 80-year-old construction company, of which the major shareholders own a 48% stake. It has cash contracting skills across power (thermal, hydel, nuclear), roads, bridges, dams, barrages, industrial, buildings, water supply, sanitation, ports, harbors and other marine works.

Investment strategy

We rate HCC Sell/Low Risk (1L), with a target price of Rs208 as:

- The stock has outperformed the BSE Sensex by more than 50% in the last 3–6 months on the Lavasa Phase I launch.
- Despite significant margin expansion in 1HFY08 (signs of respite on the BWSL losses) the company has not shown growth at the recurring PBT level because of high interest and depreciation costs.
- Over the past two years, despite its good reputation, high margins and its scale advantage over other mid-cap construction companies, HCC has lost its early advantage in the Indian E&C space. Younger, more nimble companies like Nagarjuna Construction and IVRCL have not only caught up with HCC, but have also grown larger in terms of the profits generated from the core E&C business. We downgrade HCC to Sell given downside to our new target price of Rs208.

Valuation

Our target price of Rs208 is composed of: construction (Rs90); Real estate projects (Rs116), and BOT projects (Rs3).

1) Our construction business value is based on a target P/E multiple of 17x September 2009, in line with peers like IVRCL and Gammon. We peg Nagarjuna at 19x as we believe the company is structurally moving up the value chain with its entry into the metals and pipelines space.

2) We value the real estate projects at Rs116. This consists of:

a) **Lavasa:** 12,500 acres of land at Rs3mn/acre vis-à-vis 9,100 acres at Rs2mn/acre earlier on launch of Lavasa Phase I

b) **Vikhroli (West):** DCF of post tax rentals for 1.9mn sqft

c) **Vikhroli (East):** 1.6mn sqft of slum encroached land at Rs800/sqft

d) **1,500 acres of land:** For its other projects, HCC is building its land bank across various cities in Maharashtra, such as Mumbai, Pune, Nasik, Aurangabad and Navi Mumbai. HCC has contracted ~1,500 acres of land across various cities that we value at the acquisition cost of Rs2bn.

3) Lastly, we value HCC's two BOT projects at P/Equity investment of 1.2x.

Risks

We rate HCC Low Risk, which differs from the Medium Risk rating assigned by our quantitative risk-rating system. This is as HCC has a beta of less than 1 and its order backlog of greater than Rs90bn implies sales coverage of 3.8x FY07 sales and provides what we believe is good earnings visibility in the medium term. Key upside risks are:

(1) Private equity investors taking a stake in Lavasa project at value higher than we impute

(2) Completion and sale of phase I of Lavasa Corporation ahead of schedule

(3) Markets imputing a higher valuation for the real estate investment on the sale of smaller tracts of land

(4) Faster-than-expected order execution

(5) Stronger-than-expected order inflow.

If any of these risk factors has a greater impact than we expect, HCC's share price may continue to exceed our target price.

Appendix A-1

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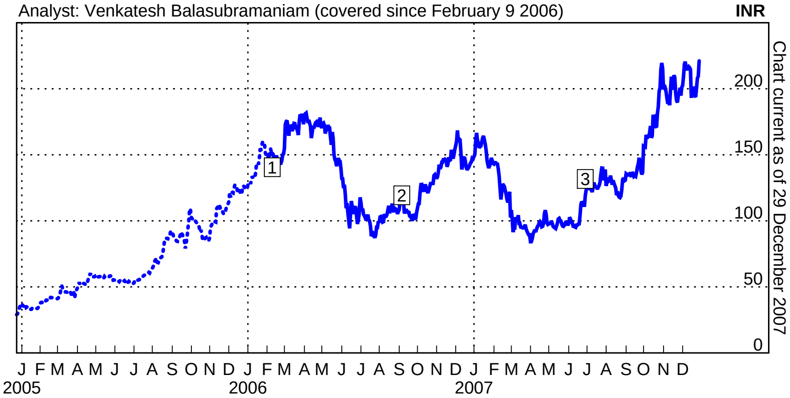
Hindustan Construction (HCNS.BO)

Ratings and Target Price History - Fundamental Research

Analyst: Venkatesh Balasubramaniam (covered since February 9 2006)



#	Date	Rating	Target Price	Closing Price
1:	9 Feb 06	3L	130.00	NA
2:	6 Sep 06	3L	*105.00	117.60
3:	28 Jun 07	*1L	*130.00	119.00

*Indicates change.

Covered
Not covered

Rating/target price changes above reflect Eastern Standard Time

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