



BL Kashyap & Sons

Emerging Star

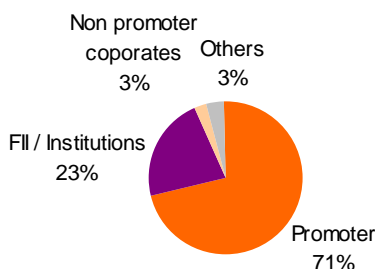
On a concrete footing

Buy; CMP: Rs2,189

Company details

Price target:	Rs2,850
Market cap:	Rs2,249 cr
52-week high/low:	Rs2340/989
NSE volume: (No of shares)	7,560
BSE code:	532719
NSE code:	BLKASHYAP
Sharekhan code:	BLKASHYAP
Free float: (No of shares)	0.3 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	34.6	29.6	92.7	114.6
Relative to Sensex	21.2	14.1	63.3	77.8

Key points

- ♦ **Poised to ride construction boom:** With its proven execution skills, reasonably large-scale of operations and an established customer base, BL Kashyap & Sons (BLK) is well poised to ride the construction boom in the fast-growing industrial, residential, commercial and retail segments.
- ♦ **Relatively low risk strategy:** Unlike most of its peers, BLK's strategy revolves around providing contractual construction services to private sector clients and it has consciously avoided exposure to long duration infrastructure projects that are prone to delays and are much more capital intensive. Thus, it does not require regular infusion of funds through debt or equity dilution.
- ♦ **To sustain growth momentum:** Despite its strategy to stay away from the big-ticket infrastructure projects, BLK has shown a healthy CAGR of 72.6% in its stand-alone revenues to Rs808 crore over the past three years. What's more, the strong order backlog of Rs2,100 crore (2.6x FY2007 revenues) provides a robust revenue growth outlook for the coming years. We expect the stand-alone revenues to grow at a CAGR of 48.8% over FY2007-10.
- ♦ **Value in real estate subsidiary:** BLK has forayed into real estate development through its subsidiary SSP, which undertakes joint development projects with the existing owners of land. Currently, it is executing six projects with saleable area of 13.2lsf (SSP's share of around 8.5lsf) and also has rights for around 150-acre land in Bikaner, Rajasthan. We have valued SSP at Rs580 crore.
- ♦ **Upside of 30% from current levels:** BLK's stand-alone earnings are estimated to grow at a CAGR of over 48% over FY2007-10. More importantly, given the company's limited exposure to highly capital intensive infrastructure projects, there is limited risk of equity dilution. At the current market price the stock trades at attractive valuations of 12.8x FY2009E and 9.3x FY2010E earnings (after adjusting for the value of its subsidiary: Rs554 per share). We recommend a Buy call on BLK with a price target of Rs2,850.

Company background

BLK is promoted by the Delhi-based Kashyap family that has been involved in the construction business for the past three decades.

Key financials (stand-alone)	FY2006	FY2007	FY2008E	FY2009E	FY2010E
Net sales (Rs crore)	465.5	808.1	1397.5	1982.5	2665.0
Net profit (Rs crore)	28.2	55.6	93.0	131.8	180.9
No of shares (crore)	1.0	1.0	1.0	1.0	1.0
EPS (Rs)	27.5	54.1	90.6	128.3	176.1
% y-o-y change	-	96.7	67.5	41.7	37.2
PER (x)	80.0	40.7	24.3	17.1	12.5
Price/BV (x)	9.3	7.6	5.9	4.4	3.3
EV/EBIDTA(x)	46.6	24.1	13.8	9.5	6.7
Dividend yield (%)	1.36	1.59	1.82	2.05	2.27
RoCE (%)	30.7	27.5	33.9	34.4	34.9
RoNW (%)	21.7	20.6	27.4	29.5	30.3

BLK has presence in various segments of the construction business like industrial, residential, commercial and retail projects.

In addition to its core business of undertaking civil construction work, the company offers other related services such as designing, furnishing and interiors.

The company has two major subsidiaries:

- ♦ **BLK Lifestyle Ltd (BLKL):** It is a wholly owned subsidiary involved in manufacturing of various fit-outs and furnishings that are utilised in residential and commercial projects. It has manufacturing facilities in Pune, Bangalore and Baddi (Himachal Pradesh) to produce various kinds of fit-outs. Though the company is expected to significantly scale up its revenues to around Rs25 crore in FY2008 (up from just Rs1.8 crore in FY2007), we have not considered BLKL's revenues in our estimates, as the same would still form an insignificant part of BLK's overall revenues in the coming years.
- ♦ **Soul Space Projects Pvt Ltd (SSP):** It is involved in real estate development through a model that minimises risk. The company does not purchase land but undertakes joint development projects in alliance with owners of the land on a sharing basis. BLK holds 97.9% stake in SSP.

Investment arguments

Huge opportunity for proven players

With almost three decades of experience in the construction business, the ability to manage over 40 projects in a single year and an established clients base of leading private sector players for projects across segments, BLK is comfortably placed to exploit the huge opportunity in the construction business in India. What's more, the company is cash rich with around Rs175 crore of cash and liquid investments on its books as in March 2007. The cash would be more than enough to fund its capital requirements to scale up its operations in order to effectively tap the huge opportunity in the sector.

Established client base

Segment	Some of the existing clients
Industrial	Biocon, Escorts, Yamaha, Maruti, Hindustan Times, Suzuki, Hero Honda and SmithKline among others
Housing/Residential	Mantri Builders, DLF, Acme, Uppal Housing and others
Commercial	Logica, Motorola, Perot Systems, Adobe Systems, Polyplex, Bhilwara group and others
Hotels	Indian Hotels, Radisson, Hyatt and EIH among others
Hospitals	Escorts, Fortis and Jaipur Golden

The size of the opportunity is huge in the various segments that BLK is focused on:

Housing/residential

- ♦ Cushman & Wakefield have noted that there is scope for 400 township projects over the next five years spread across 30 to 35 cities, each having a population of more than 0.5 million. It has estimated the total project value dedicated to low and middle income housing in the next seven years at US\$40 billion.
- ♦ According to CRIS INFAC's "Housing annual review", the residential sector is expected to grow at compounded annual growth rate (CAGR) of 18.4% over the next five years to Rs4.03 trillion.

Commercial

- ♦ According to CRIS INFAC, the space required for the information technology (IT) and IT enabled service (ITES) sectors alone is expected to increase at a CAGR of 23% over the next five years.

Estimated growth in expenditure			(Rs crore)
Segment	2005	2010P	% CAGR
Housing	172,000	400,000	18.4
Commercial*	3,800	10,500	22.5
Retail	35,000	109,500	25.6

* For IT and ITES sector alone

In addition to this, the aggressive expansion projects lined up by corporates and the impending development of special economic zones would only add to the existing opportunity for the construction companies.

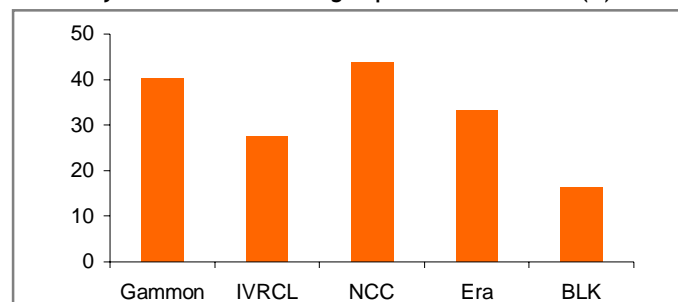
De-risked business model

BLK has remained focused on providing contractual construction services to private sector clients and expanding its operation to various regions in the country. This is contrary to the model adopted by most other construction companies that have aggressively forayed into government sponsored big-ticket infrastructure projects. Consequently, BLK has not been exposed to risks associated with the infrastructure projects, such as delays in execution (due to issues like delay in obtaining approvals, acquiring land etc) and the need for huge infusion of capital (projects are awarded based on the net worth criterion; the build-own-transfer [BOT] projects involve huge capital investments initially with cash flows spread over a number of years).

The business model to focus on the shorter duration projects (residential, commercial, retail or industrial) from largely private sector clients has enabled BLK to considerably limit its capital requirements (both in terms

of working capital and the initial capital expenditure in BOT projects) resulting in strong cash inflows and return ratios. For instance, BLK's working capital-to-sales ratio is around 10-15% as compared with 25-45% for most of its peers (such as Gammon India, Nagarjuna Construction, IVRC, Era Construction and Hindustan Construction) that are involved in infrastructure projects. Moreover, the visibility in execution of these projects of shorter duration is much better with limited scope for litigations.

Relatively much lower working capital-to-sales ratio (%)

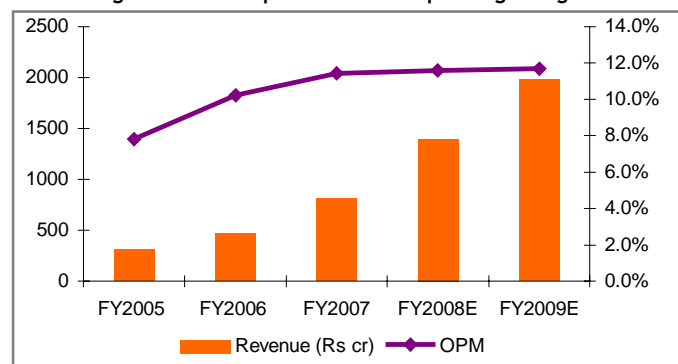


Source: Sharekhan Research

Healthy order backlog provides growth visibility

BLK has an order backlog of Rs2,100 crore that is executable over the next 18-24 months. In addition to this, the company has a strong pipeline of orders and expects to bag orders worth Rs400-500 crore in every quarter during the current fiscal. This provides a strong revenue growth visibility for the coming years. We expect its stand-alone revenues to grow at a CAGR of 48.8% over the three-year period FY2007-10.

Revenue growth accompanied with improving margins



Source: Sharekhan Research

In terms of profitability also, the company has shown a significant improvement in its operating profit margin over the past three years. The company believes that the margin is sustainable at the current levels and could improve marginally in the coming years.

Value to be unlocked in the real estate subsidiary

BLK has forayed into real estate development through its subsidiary SSP, which undertakes joint development projects with the existing owners of land. Currently, it is executing six projects with saleable area of 13.2 lakh sq ft (lsf; SSP's share of around 8.5lsf). Apart from this, the company has rights to develop 300 acre of land in Bikaner, Rajasthan with SSP's share estimated at around 150 acre. We have valued the subsidiary at Rs580 crore (or Rs554 per share for BLK's stake of 97.9% in SSP). Going forward, we believe that BLK could unlock value in its subsidiary through placement of part of the latter's equity to strategic investors.

Value of SSP

	Amount (Rs cr)
SSP's share of projects under execution	206
Value of Bikaner land	375
Total value of subsidiary	581
Value/share for BLK's stake (Rs)	554

Investment concerns

Intensified competitive scenario

The huge opportunity in the construction sector has attracted to India many globally leading construction companies, which are either directly setting up offices or forming joint ventures with existing construction or real estate companies. This would not only result in increasing competition for the contractual construction projects but put pressure on the cost side due to wage inflation. The industry is already witnessing a shortage of skilled and experienced manpower.

Valuation

BLK's stand-alone earnings are estimated to grow at a CAGR of over 48% over the three-year period FY2007-10. Given its business model (no exposure to capital intensive infrastructure projects, hence strong cash inflows), there is limited risk of equity dilution and the growth in its earnings would get fully reflected in its earnings per share. At the current market price the stock trades at attractive valuations of 12.8x FY2009 and 9.3x FY2010 estimated earnings (after adjusting for the value of its subsidiary Rs554 per share). We recommend a Buy call on BLK with a price target of Rs2,850 (15x FY2010 estimated earnings discounted backwards by one year plus the value of its real estate subsidiary).

Financials

Profit & loss account (stand-alone)						Balance sheet					
Rs (cr)						Rs (cr)					
Particulars	FY06	FY07	FY08E	FY09E	FY10E	Particulars	FY06	FY07	FY08E	FY09E	FY10E
Net sales	465.5	808.1	1397.5	1982.5	2665.0	Share capital	10.3	10.3	10.3	10.3	10.3
Total expenditure	417.9	715.9	1235.4	1750.5	2347.9	Reserves and surplus	233.9	285.2	373.5	499.9	674.8
EBITDA	47.6	92.2	162.1	232.0	317.1	Net worth	244.2	295.5	383.7	510.1	685.0
Other income	3.3	8.0	12.8	15.3	22.0	Total debt	19.5	93.2	167.7	237.9	319.8
Interest	4.1	5.0	16.8	21.4	28.8	Deferred tax liabilities	1.6	2.0	2.4	2.9	3.5
Depreciation	4.3	9.9	15.0	23.1	32.1	Capital employed	265.3	390.7	553.8	750.9	1008.3
PBT	42.6	85.3	143.1	202.8	278.3	Net fixed assets	42.8	70.0	120.0	166.9	214.9
Tax	14.3	29.7	50.1	71.0	97.4	Investments	140.5	145.4	160.0	176.0	193.6
PAT	28.2	55.6	93.0	131.8	180.9	Net current assets	75.6	170.6	269.6	403.8	595.6
						Msc exp not w/off	6.4	4.7	4.3	4.3	4.3
						Capital deployed	265.3	390.7	553.9	751.0	1008.3

Key ratios

Particulars	FY06	FY07	FY08E	FY09E	FY10E
OPM (%)	10.2	11.4	11.6	11.7	11.9
NPM (%)	6.1	6.9	6.7	6.6	6.8
RoCE (%)	30.7	27.5	33.9	34.4	34.9
RoNW (%)	21.7	20.6	27.4	29.5	30.3

Valuation

Particulars	FY06	FY07	FY08E	FY09E	FY10E
EPS (Rs)	27.5	54.1	90.6	128.3	176.1
P/E	80.0	40.7	24.3	17.1	12.5
Book value	237.7	287.7	373.6	496.6	666.9
Price/BV	9.3	7.6	5.9	4.4	3.3
EV/Sales	4.8	2.7	1.6	1.1	0.8
Market cap/Sales	4.9	2.8	1.6	1.1	0.8
EV/EBIDTA	46.6	24.1	13.8	9.5	6.7
Dividend yield (%)	1.4	1.6	1.8	2.0	2.3

The author doesn't hold any investment in any of the companies mentioned in the article.

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