

INDIA

Market Cap
Rs.17522.75mn

EQUITY RESEARCH

Capital Goods & Engineering

C.M.P. Rs 95.00
(As on Dec. 18, 2009)

December 18, 2009

HOLD
Target Price Rs.105.00



Praj Industries Ltd

- The company`s principal activity is to manufacture turnkey plants and equipment for fermentation and distillation systems, worldwide.
- Praj Industries has received an order for downstream processing equipment from Range Fuels, USA, of approximately Rs 200 million.
- Praj Industries Ltd. has set up an energy agri solutions group. This facility would concentrate on non-food crops such as sweet sorghum, safflower and a variety of grasses.
- The company will focus on renewable fuels, specifically fuel-ethanol, in the years to come. It has tied up with the Research Institute of India to conduct joint research in producing ethanol from biomass.
- Praj, a leading company, in biofuel technology and plants, and Novozyrnes, the leading enzyme provider to the biofuel industry, has decided to collaborate on advanced biofuels.
- Net sales and PAT of the Company are expected to grow at a CAGR of 8% & 4% over FY08 to FY11E.

One-year comparative graph with BSE



PRAJ IND.LTD

BSE SENSEX

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Key Financials	FY08(A)	FY09(A)	FY10(E)	FY11(E)	Key Data	
Net sales (Rs.mn)	7016.30	7743.70	7976.01	8773.61	Face Value	Rs 2.00
EBITDA (Rs.mn)	1799.40	1693.70	1913.84	2179.36	52WK High/low	123.00 / 45.00
Margin %	25.65%	21.87%	23.99%	24.84%	Shares outstanding	184.45mn
PAT (Rs.mn)	1535.40	1297.60	1480.65	1689.50	2Wk Avg. volume	1572639
Margin %	21.88%	16.76%	18.56%	19.26%	BSE Code	522205

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Peer Group Comparison

Name of the Company	52 wk High / Low(Rs)	C.M.P(Rs.)*	E.P.S(Rs.)	P/E(x)
PRAJ INDUSTRIES LTD	123.00/45.00	95.00	7.58	12.53
BHEL	2550.00/1250.00	2310.80	70.81	32.63
L&T	1800.00/557.00	1646.55	79.94	20.60
BEML	1220.00/310.00	999.00	59.95	16.66

*As on 18/12/09

Company Updates

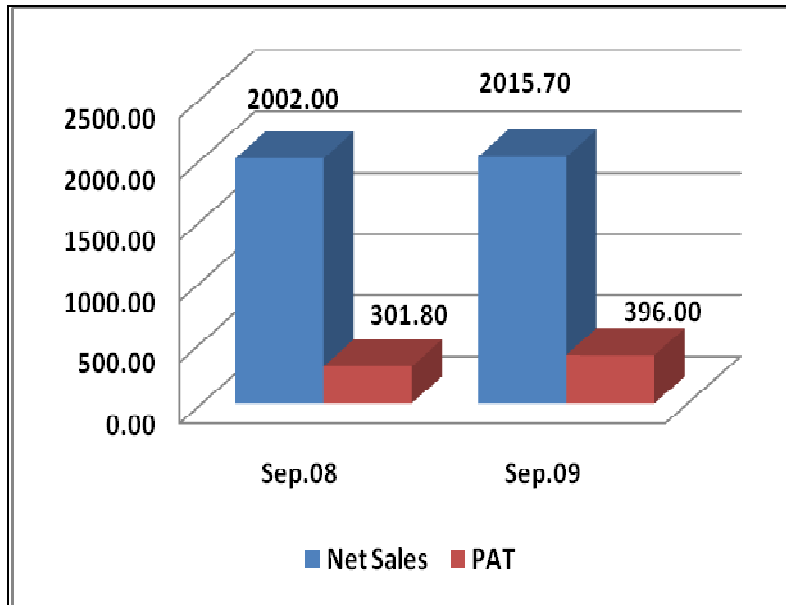
• Q2 FY10 Results Update

Praj Industries reported a phenomenal rise in standalone net profit for the quarter ended Sep 2009. During the quarter, the profit of the company rose 31.21% to Rs 396.00 million from Rs 301.80 million in the same quarter last year. Net sales for the quarter rose 0.68% to Rs 2015.70 million, while total income for the quarter rose 2.75% to Rs 2113.90 million compared with the prior year period. It posted earnings of Rs 2.15 a share during the quarter, registering 30.50% growth over prior year period.

Quarterly Results - Standalone (Rs in mn)			
As at	Sep - 09	Sep - 08	%Change
Net Sales	2015.70	2002.00	0.68
Net Profit	396.00	301.80	31.21
Basic EPS	2.15	1.65	30.50

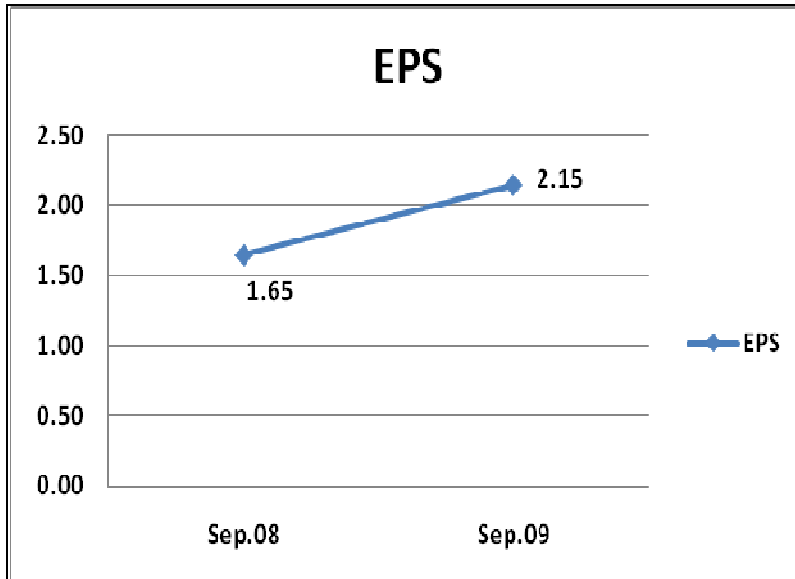
Net Sales & Net Profit Growth

Net sales for the quarter rose 0.68% to Rs 2015.70 million from Rs 2002.00 million in the same quarter last year and the profit of the company rose 31.21% to Rs 396.00 million from Rs 301.80 million in the same quarter last year.



EPS Growth

During the quarter, the company posted an EPS of Rs 2.15, registering a rise of 30.50% from Rs 1.65 in the same quarter previous year.



- **Praj, Novozymes join hands for advanced biofuels**

Praj, a leading company, in biofuel technology and plants, and Novozymes, the leading enzyme provider to the biofuel industry, has decided to collaborate on advanced biofuels. Together, Praj and Novozymes will optimize the enzymatic hydrolysis processes and the use of enzymes in the production of advanced biofuel. The two companies have worked together for several years within conventional biofuel.

- **Praj Industries bags Rs 200 mn order**

Praj Industries has received an order for downstream processing equipment from Range Fuels, USA, of approximately Rs 200 million. The company's principal activity is to manufacture turnkey plants and equipment for fermentation and distillation systems, worldwide.

- **Praj Industries sets up Energy Agri Solutions Facility**

Praj Industries Ltd. has set up an energy agri solutions group. This facility would concentrate on non-food crops such as sweet sorghum, safflower and a variety of grasses. It has been cultivating safflower in Maharashtra and Karnataka, and had achieved good production. The company was looking at commercial production in India and Africa.

- **Praj Industries develops cellulosic ethanol technology**

Praj Industries, the globally leading biofuels technology and solutions company has announced a breakthrough in cellulosic biomass to ethanol technology at Pilot Scale at its R&D center called Praj Matrix, the innovation centre near Pune. The first phase of the scaled up program for non-food biofuels and industrial biotech processes has now been achieved with this breakthrough wherein the pilot plant has successfully demonstrated production of ethanol from corn cob and sugarcane bagasse under varying operating conditions. This follows proven bench scale process development for which Praj has already filed for patents.

- **ICRA withdraws A1+ rating**

Credit rating agency, ICRA has withdrawn the A1+ rating assigned to the Rs 120 million short term debt (including commercial paper) programme of Praj Industries as there is no amount outstanding against the rated instrument.

- **CRISIL upgrades its rating to 'AA/Stable'**

CRISIL has upgraded its rating on Praj Industries Ltd's (PIL's) long-term bank facilities to 'AA/Stable' from 'AA-/Stable'. The upgrade reflects CRISIL's belief that PIL will maintain its financial risk profile at the current improved level over the medium term on the back of its strong market position, rising demand, and good operational efficiencies. PIL has a strong financial risk profile marked by high profitability and strong liquidity. As on March 31, 2009, the company had a low gearing and a relatively large net worth of Rs.4.2 billion. PIL's debt protection measures, too, are strong.

Furthermore, the company has large surpluses, Rs.3.2 billion as on March 31, 2009, in the form of cash and bank balances and marketable securities. The rating on PIL's short-term facility has been reaffirmed at 'P1+'.

- **MOU with Ardent Energy Group (AEG)**

Praj Industries Limited has signed an Memorandum of Understanding (MOU) with Ardent Energy Group (AEG) for providing consultancy in the cultivation energy crop for bio-fuels.



Company Profile

Praj Industries was established in 1984 and is headquartered in Pune, India for providing solutions to the distillery industry. Currently, the company is engaged in engineering and manufacture of alcohol plants, fuel ethanol plants, brewery plants, wastewater systems and fermentation systems. It has technical collaborations with Dab Brav Consult GmbH, Germany and Vogellbusch GmbH, Austria. The company is currently operating in Asia, Africa and South America. Its R&D centre, Matrix, has developed several patented technologies for the company.

The alcohol plants of the company deliver industrial, potable and fuel grade ethanol. They produce alcohol from various raw materials like sugar, starch and multiple feedstocks. The company manufactures flexible plants wherein the same equipment can deliver different grades of spirits for different applications. The company has a market share of 60% in ethanol plant and equipment manufacture.

The company also provides turnkey solutions, technical support and engineering services to the brewery industry for activities from malt reception to packaging. It manufactures mash vessels, wort boilers, fermentation systems, filtration systems, yeast drying systems, heat recovery systems and cleaning in place (CIP) systems for breweries. The company is also engaged in the engineering and manufacture of wastewater treatment plants and fuel-ethanol plants.

Future Plans

The company will focus on renewable fuels, specifically fuel-ethanol, in the years to come. It has tied up with the Research Institute of India to conduct joint research in producing ethanol from biomass. The company is also in the process of upgrading its manufacturing systems by deploying ERP solutions.

The company also has a vision of expanding in the biofuels technology arena. For biodiesel projects, the company will offer in-house developed turnkey solutions including technology, engineering, plant & equipment and project management services.



Financials

Results Update

12 Months ended Profit and Loss Account (Standalone)

Value(Rs. in million)	FY08	FY09	FY10E	FY11E
Description	12m	12m	12m	12m
Net Sales	7016.30	7743.70	7976.01	8773.61
Other Income	386.80	216.90	390.42	468.50
Total Income	7403.10	7960.60	8366.43	9242.12
Expenditure	-5603.70	-6266.90	-6452.59	-7062.76
Operating Profit	1799.40	1693.70	1913.84	2179.36
Interest	-0.30	-3.90	-6.05	-6.65
Gross Profit	1799.10	1689.80	1907.79	2172.71
Depreciation	-55.30	-81.70	-102.13	-112.34
Profit before Tax	1743.80	1608.10	1805.67	2060.37
Tax	-208.40	-310.50	-325.02	-370.87
Profit after Tax	1535.40	1297.60	1480.65	1689.50
Equity Capital	366.30	366.90	368.90	368.90
Reserves	3142.00	4067.70	5548.35	7237.85
Face Value (Rs)	2.00	2.00	2.00	2.00
Total No. of Shares	183.15	183.45	184.45	184.45
EPS (Rs)	8.38	7.07	8.03	9.16



Quarterly Ended Profit and Loss Account (Standalone)

Value(Rs. in million)	31-Mar-09	30-Jun-09	30-Sep-09	31-Dec-09E
Description	3m	3m	3m	3m
Net Sales	2093.10	1264.20	2015.70	2136.64
Other Income	42.60	116.10	98.20	108.46
Total Income	2135.70	1380.30	2113.90	2245.10
Expenditure	-1704.80	-1047.10	-1606.70	-1705.04
Operating Profit	430.90	333.20	507.20	540.06
Interest	-3.10	-1.90	-1.40	-1.44
Gross Profit	427.80	331.30	505.80	538.62
Depreciation	-23.10	-24.00	-25.60	-26.88
Profit before Tax	404.70	307.30	480.20	511.74
Tax	-130.00	-54.00	-84.20	-92.11
Profit after Tax	274.70	253.30	396.00	419.63
Equity Capital	366.90	367.00	368.90	368.90
Face Value (Rs)	2.00	2.00	2.00	2.00
Total No. of Shares	183.45	183.50	184.45	184.45
EPS (Rs)	1.50	1.38	2.15	2.28

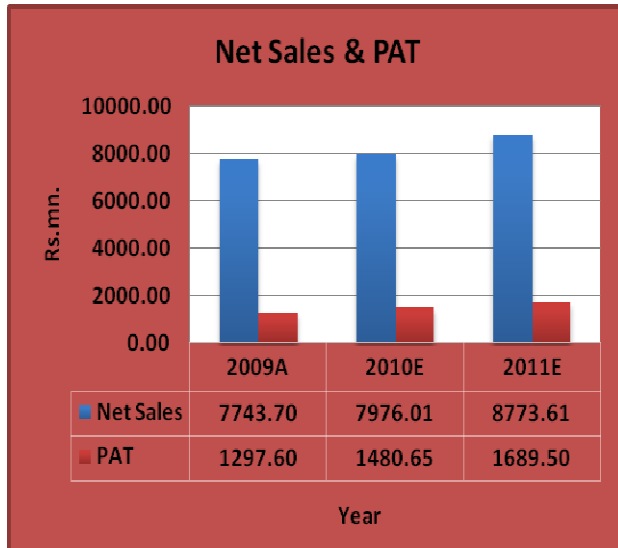
Key Ratios

Particulars	2008(A)	2009(A)	2010(E)	2011(E)
EBITDA Margin (%)	25.65%	21.87%	23.99%	24.84%
PAT Margin (%)	21.88%	16.76%	18.56%	19.26%
P/E (x)	11.33	13.43	11.83	10.37
ROE (%)	43.76%	29.26%	25.02%	22.21%
ROCE (%)	49.71%	35.34%	29.94%	26.68%
EV/EBITDA (x)	9.67	10.29	9.16	8.04
Debt-Equity Ratio	0.00	0.03	0.02	0.02
Book value (Rs)	19.16	24.17	32.08	41.24
P/BV (x)	4.96	3.93	2.96	2.30

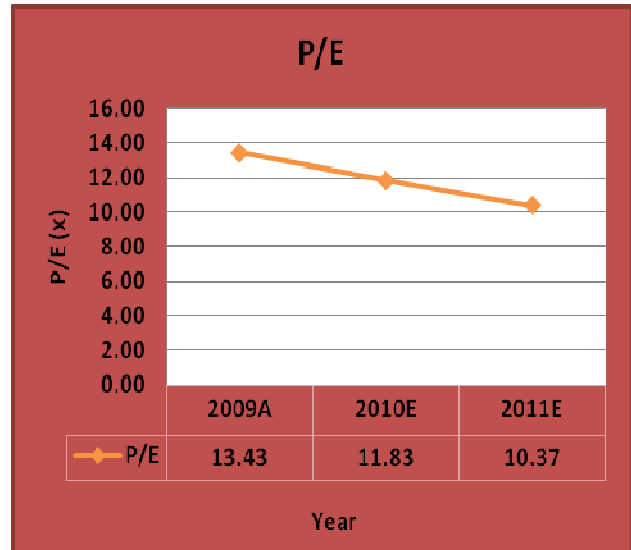
A-Actual E-Expected

Charts

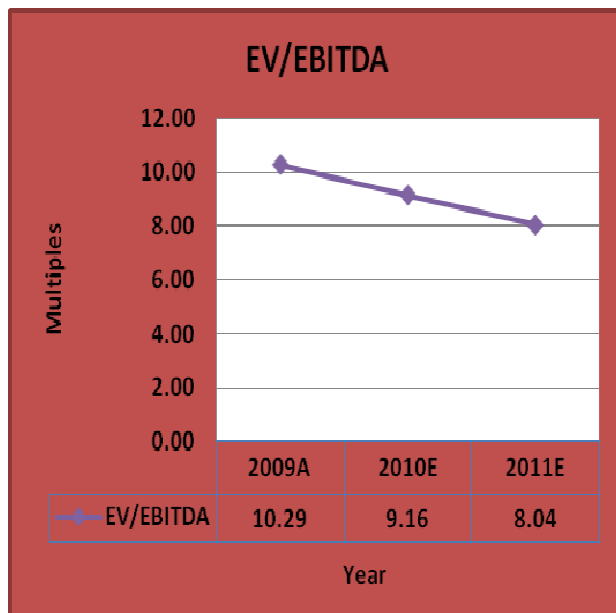
A) Net Sales & PAT Chart



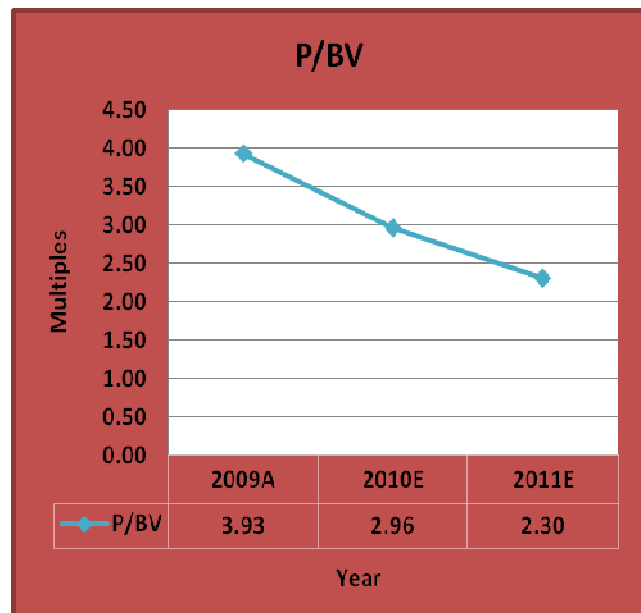
B) P/E Chart



C) EV/EBITDA Chart



d) P/BV Chart

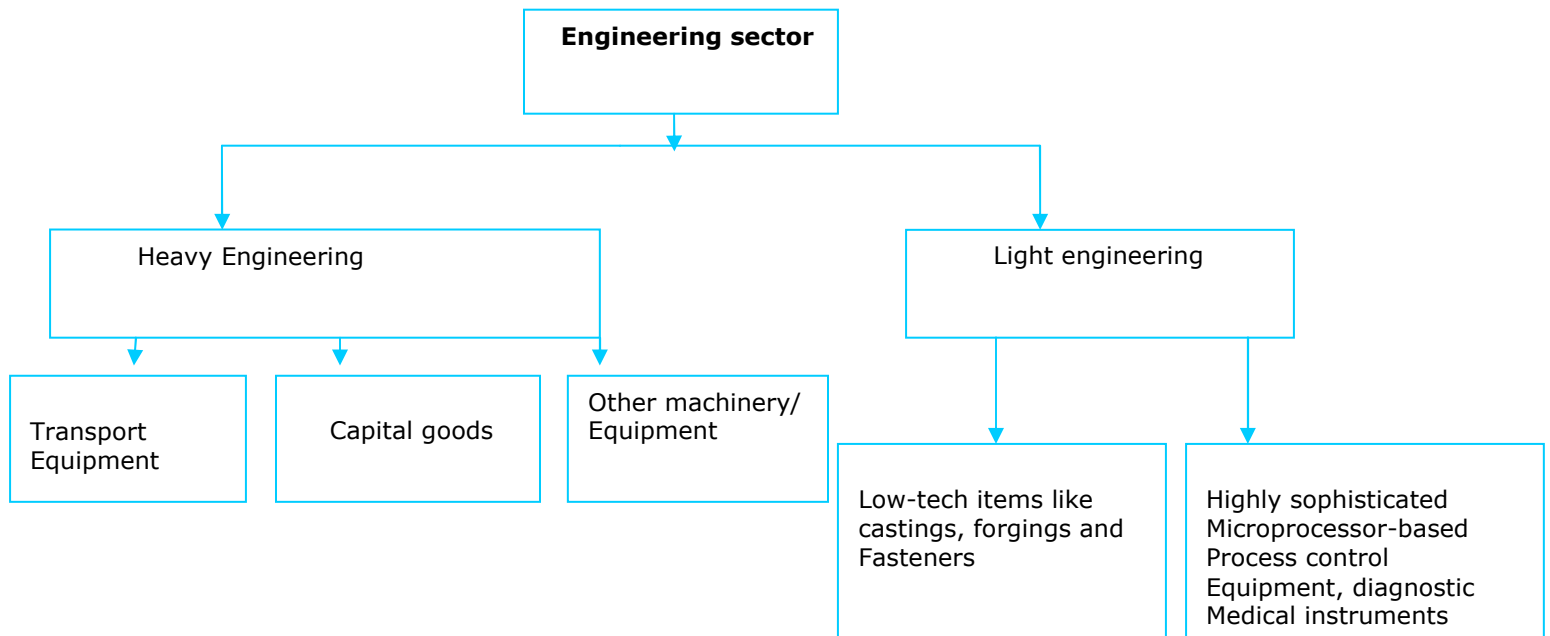


Valuation

- At the market price of Rs.95.00, the stock trades at 11.83x and 10.37x for the earnings of FY10E and FY11E respectively.
- Price to Book Value of the stock is expected to be at 2.96x and 2.30x respectively for FY10E and FY11E.
- Earning per share (EPS) of the Company for the earnings of FY10E and FY11E is seen at Rs.8.03 and Rs.9.16 respectively for equity share of Rs.10.00 each.
- Operating Profit of the Company is expected to grow at a CAGR of 7% over FY08 to FY11E.
- Praj Industries has received an order for downstream processing equipment from Range Fuels, USA, of approximately Rs 200 million.
- The company will focus on renewable fuels, specifically fuel-ethanol, in the years to come. It has tied up with the Research Institute of India to conduct joint research in producing ethanol from biomass.
- Praj, a leading company, in biofuel technology and plants, and Novozyrnes, the leading enzyme provider to the biofuel industry, has decided to collaborate on advanced biofuels.
- The order book on hand currently stands at Rs.800 crores, to be executed in next 12 months. Out of Rs.800 crores orders, a little over 50% are overseas orders. While there has been a little stagnancy in order book off late, yet we believe it is on a strong wicket considering the overall business scenario worldwide.
- We recommend 'HOLD' in this particular scrip with a target price of Rs.105.00.

Industry overview

Engineering Sector: Market & Opportunities



India's engineering industry is highly competitive with a number of players in each segment. The engineering sector has been growing, driven by growth in end user industries and the new projects being taken up in the power, railways, infrastructure development, and private sector investments fields amongst others. The industry attracted FDI inflows of US\$ 1,196.7 million from August 1991-July 2006

India's exports of engineering goods are valued at US\$ 27 billion during 2006-07 which represents a 6 per cent growth over the exports for 2005-06 (US\$ 20 billion). The engineering sector accounted for 14 per cent of the country's total exports. It is also noteworthy that 40 per cent of India's engineering export is from the small and medium enterprises (SME) sector. According to Engineering Exports Promotion Council (EEPC), engineering exports could touch US\$ 30 billion by 2008-09. In such a scenario, India, driven by the engineering sector, will emerge as a key global manufacturing hub.

Industry demand is driven by investments in core sectors

The demand from this sector depends largely on GDP growth, which in turn is a function of expenditure in core segments like power, railways, and infrastructure development, private sector investments, and the speed at which projects are implemented. The power sector is the largest contributor to the revenues of engineering companies. Engineering majors like Bharat Heavy Electricals Limited (BHEL) and ABB Limited derive a significant chunk of their revenues (69 per cent and 60 per cent, respectively) through the supply of equipment to the power sector.

Infrastructure is another key area of operation. Larsen & Toubro Limited, for example, garners around 35 per cent of its sales from infrastructure activities like engineering, design and construction of industrial projects, social and physical projects like housing, hospitals, information technology (IT) parks, expressways, bridges, ports, and water/effluent treatment projects. The industrial segment contributes to around 30 per cent of the total revenues of the engineering sector. While India's engineering industry has capabilities in manufacturing the range of machinery required by the different user sectors, the rapid rise in demand has led to a large part of the machinery requirements being met through imports. This indicates the size of opportunity for investment in the engineering and capital goods sector in India. The engineering industry has attracted FDI inflows of US\$ 1,196.73 million from August 1991-July 2006.

Indian Engineering goods are gaining acceptance in overseas markets

India's exports of engineering goods are valued at US\$ 27 billion during 2006-07 which represents a 36 per cent growth over the exports for 2005-06 US\$ 20 billion). The engineering sector accounted for 14 per cent of the country's total exports. It is also noteworthy that 40 per cent of India's engineering export is from the small and medium enterprises (SME) sector. A key driver for increased engineering exports is the trend towards shifting of global manufacturing bases to countries like India that offer lower costs and good engineering talent. This trend is expected to continue and boost exports of engineering goods from India over the next 5 years. According to Engineering Exports Promotion Council (EEPC), engineering exports could touch US\$ 30 billion by 2008-09. In such a scenario, India, driven by the engineering sector, will emerge as a key global manufacturing hub.

The nature of Indian engineering exports is also changing with time. India is fast moving from exporting low value goods to developing countries to more sophisticated goods targeted at developed countries. Capital goods account for 27 per cent of total engineering exports. Exports to European Union countries and North America accounted for 19 per cent and 17 per cent respectively, of total engineering exports in 2005-06. Engineering goods worth US\$ 3.34 billion were exported to USA alone in April – Feb 2006-07.



Growing Demand

Capacity creation and transformation in sectors such as infrastructure, power, mining, oil & gas, refinery, steel, automotive, consumer durables are driving growth in the engineering industry. The framework below captures some of the key factors that are contributing to domestic and international demand for engineering goods from India. Restructuring of the state electricity boards in different states, growth of private sector players and focus on capacity creation have driven growth in the power sector.

Conclusion

The Engineering sector's future outlook is promising. Drivers like power projects, other infrastructure development activities, industrial growth and favorable policy regulations will drive growth in manufacturing. The Indian engineering industry has been witnessing significant level of capability enhancement over the years. As export markets open up, this will help India develop a strong presence in global engineering exports. Power sector contributes the largest to the engineering companies' revenues. Major players in this sector like ABB and BHEL derive 60 per cent and 69 per cent of their revenues from supplying equipments to the power sector. Going forward, with the Government clearing the blueprint for adding 100,000 MW in the tenth (2002-07) and eleventh (2007-12) a five-year plan, the potential is high for the engineering majors. Emerging trends such as outsourcing of engineering services can provide new opportunities for quantum growth. Engineering and design services such as new product designing, product improvement, maintenance and designing manufacturing systems are increasingly getting outsourced to countries like India and China. India's engineering sector has significant potential for future growth, in manufacturing as well as services.

With development in associated sectors like automotive, one of the largest evolving markets for engineering and industrial goods, and a well developed technical human resources pool, India is poised to make significant strides in all segments of engineering.

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