September 14, 2010

HDIL

Cash in; Eye on usage

Equity dilution could be an overhang in the near term: As per media reports, HDIL have successfully raised equity up to US $250mn through a QIP at a price of Rs268.18/share. This would lead to equity dilution of 10%. The amount would be utilised to part-finance the second phase of the airport project and for fresh land acquisitions. As of June 2010, the company had quite manageable net debt position of Rs3,533cr (0.47x) with unpaid land cost of Rs300cr, where majority of repayment obligation largely starts from FY2012. This is the third round of equity dilution since June 2009, which is quite surprising given the kind of successful new launches taken place over the last year and comfortable net debt position. We believe the stock price to remain range bound on account of the slowdown in Mumbai realty market, likely hike in FSI impacting TDR volumes and overhang of equity dilution at this level. However, faster execution of phase II of the airport project and winning of new NAV accretive SRA projects through QIP issuance will act as a positive share price catalyst. **We maintain Accumulate on HDIL.**

Hike in FSI seems priced in: The Maharashtra state government is likely to hike FSI from 1 to 1.33 in suburbs, which will affect TDR prices. We have already factored stable TDR prices of Rs2400/sq. ft. (i.e., 25% discount from the current level of Rs3,200/sq. ft.) and do not expect a major negative impact incrementally. Further, we have assumed 4.5mn sq. ft. of TDR sale (i.e., 30% drop in TDR sales from FY2010) in FY2011 to factor in the hike in FSI. A 10% decline in TDR price adversely impacts our NAV by mere 3%.

Slowdown in Mumbai realty may be a temporary phenomenon: The recent price rise of 10–15% has hurt volumes and pre-sales over the last three months. Further, medium-term supply concerns in Central Mumbai and likely hike in FSI in suburbs will keep realty prices range bound in the near term. However, we believe long-term demand in Mumbai realty market remains intact given robust wage growth and hiring activity. We believe developers such as HDIL will continue to enjoy successful new launches on account of being launched at a 10–20% discount rate to prevailing market prices.

Outlook and valuation: Smooth execution of the Rs200bn MIAL project, sustainable TDR prices and successful new launches provide strong visibility for HDIL. The stock has been laggard over the last six months and is currently trading at 33% discount to our one-year forward NAV. We maintain Accumulate on HDIL with a Target Price of Rs302 (25% discount to our one-year forward NAV).

Key Financials (Consolidated)

Y/E March (Rs cr)	FY2009	FY2010	FY2011E	FY2012E
Net Sales	**1,750**	**1,523**	**1,858**	**3,159**
% chg	*(26.9)*	*(13.0)*	*22.0*	*70.0*
Net Profit	**786**	**568**	**832**	**1,325**
% chg	*(44.3)*	*(27.8)*	*46.4*	*59.4*
EBITDA (%)	45.8	53.2	54.9	53.4
EPS (Rs)	**18.9**	**13.7**	**20.0**	**31.9**
P/E (x)	14.3	19.8	13.5	8.5
P/BV (x)	1.7	1.6	1.2	1.1
RoE (%)	19.5	9.9	10.3	13.5
RoCE (%)	10.4	7.5	8.4	12.3
EV/Sales (x)	7.7	8.3	6.3	3.7
EV/EBITDA (x)	16.7	15.6	11.5	6.9

Source: Company, Angel Research

ACCUMULATE

CMP	Rs271
Target Price	Rs302

Investment Period	12 Months

Stock Info	
Sector	Real Estate
Market Cap (Rs cr)	9,358
Beta	1.8
52 Week High / Low	411/202
Avg. Daily Volume	2,117,806
Face Value (Rs)	10
BSE Sensex	19,347
Nifty	5,796
Reuters Code	HDIL.BO
Bloomberg Code	HDIL@IN

Shareholding Pattern (%)	
Promoters	42.3
MF / Banks / Indian FIs	1.0
FII / NRIs / OCBs	45.7
Indian Public / Others	11.0

Abs. (%)	3m	1yr	3yr
Sensex	11.6	19.3	24.0
HDIL	15.1	(10.4)	(41.3)

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Investment arguments

High-margin slum redevelopment projects

Slum redevelopment (SRA) does not involve upfront investment in land compared to conventional real estate projects. Cost per sq. ft. in slum redevelopment projects is around Rs3,000/sq. ft. v/s Rs5,000–6,000/sq. ft. (including land cost) on freehold land due to high property prices in Mumbai. Slum redevelopment also has high entry barriers, as it requires expertise and experience to deal with government agencies and slum dwellers regularly until the completion of the project. In Mumbai, over 54% of the population lives in slum clusters situated in certain pockets of the city. A slum population of 7.5mn could translate into 1.5mn families, with an average household size of five. This could translate into SRA potential of 644mn sq. ft. and revenue potential of Rs2,000bn for redevelopers.

HDIL, the market leader in slum rehabilitation, is well poised to cash in on the immense opportunity in the SRS segment. The company has executed close to 10mn sq. ft. of SRS projects in the last 15 years and is more competitive than other developers in the fray. Thus, HDIL stands a good chance to win large SRA projects, such as Dharavi, where rehab families could be of similar size to MIAL.

Execution of the airport project on track

The first phase of HDIL's MIAL project to rehabilitate 28,000 families is on track and likely to be completed by September 2010, generating around 10mn sq. ft. of TDR. The company will also get 2mn sq. ft. of FSI for commercial development in the airport vicinity once the 28,000 families are rehabilitated. We expect HDIL to sell 4mn–5mn sq. ft. of TDR annually over the next five years on strong ongoing execution of the MIAL project, which will generate further 37mn sq. ft. of TDR over the next 5–6 years. The MIAL project contributes around 30% to our one-year forward NAV.

Rewarding new launches

In 1QFY2011, HDIL launched the first phase of *The Meadows*, Goregaon West. The company sold 0.75mn sq. ft. in just two days of the launch. HDIL has also launched the second phase of *Premier*, a 0.75mn sq. ft. residential project in Kurla.

HDIL has strategically deleveraged its business model by launching various projects through the conventional route since March 2009, thereby reducing its overdependence on the TDR market. The company has been able to pre-sell 75% of its residential projects (5.7mn sq. ft.) launched since FY2009, thereby providing Rs4,000cr of revenue visibility over FY2010–12E. HDIL has even managed to pre-lease 20% of its commercial launches at its Andheri (*Metropolis*) project for Rs140/sq. ft. The company's recent launches have been successful on account of being launched at a 10–20% discount rate to prevailing market prices. Management has indicated that it would adopt the same strategy for its forthcoming launches. In FY2011, HDIL plans to launch new projects of 5mn–6mn sq. ft., largely in Mumbai (including Siddharth Nagar, Goregaon; Ekta Nagar, Kandivali; and Pant Nagar, Ghatkopar).

Exhibit 1: Launching projects through the conventional route

Project	Location	Saleable area (mn sq ft)	Sold/leased (%)	Average sales rate (Rs/sq ft)
Residential				
Galaxy	Kurla (E)	0.48	> 90	4,500
Premier	Kurla (W)	1.00	> 95	5,700
Metropolis	Andheri (W)	0.65	> 95	9,000
Majestic	Bhandup	1.30	> 40	6,500
Residency Park	Virar	1.25	> 75	2,600
Harmony	Goregaon	0.04	> 95	8,451
Meadows -Phase I	Goregaon	1.00	>75	7,740
Commercial				
Premier	Kurla (W)	2.00		
Metropolis	Andheri (W)	1.02	20	Rs140/sq ft
HDIL Industrial Park	Virar	1.50	>90	
Harmony	Goregaon (W)	0.07	>75	
Total		10.30		

Source: Company, Angel Research

Outlook and valuation

HDIL is the largest listed slum rehabilitation developer in the most resilient market of Mumbai, which contributes a substantial 71% to our GNAV. Smooth execution of the Rs200bn MIAL project, sustainable TDR prices and successful new launches via the conventional method provide strong visibility for HDIL.

We maintain our TDR price assumption of Rs2,400/sq. ft. for the company's MIAL project. Further, HDIL seeks to deleverage its balance sheet on the back of the expected high revenue inflow from the MIAL project and the recent low-cost Rs1,375cr fresh NCD issue, which will reduce its net gearing to 0.21x in FY2012E from the current level of 0.47x. The stock is currently trading at 33% discount to our one-year forward NAV. **We maintain our Accumulate rating on the stock with a Target Price of Rs302, which is at 25% discount to our one-year forward NAV.**

Exhibit 2: Valuation summary

One-year forward NAV	(Rs per share)
MIAL (Airport FSI and TDR)	168
Residential	151
Commercial	105
Other SRS	103
Retail	35
Total	**561**
Less	
Net debt	(63)
Unpaid land cost and customer advances	(20)
Tax	(76)
NAV/share (Rs)	**402**
Target Price (Rs) 25% discount to NAV	**302**

Source: Company, Angel Research

Exhibit 3: Key assumptions

Particulars		FY2010	FY2011E	FY2012E
TDR sales (mn sq. ft.)		6.5	4.6	4.6
TDR price (Rs/ sq. ft.)		2,060	2,400	2,400
Pricing (% change)				
Residential		-	5.0	5.0
Commercial		-	(5)	5
Retail		-	(5)	5
Discount rate	15%			
Cap rate	11%			

Source: Angel Research

Profit & Loss Statement (Consolidated)

Y/E March (Rs cr)	FY2007	FY2008	FY2009	FY2010	FY2011E	FY2012E
Net Sales	1,214	2,395	1,750	1,523	1,858	3,159
Other operating income	-	-	-	-	-	-
Total operating income	1,214	2,395	1,750	1,523	1,858	3,159
% chg	*179.2*	*97.2*	*(26.9)*	*(13.0)*	*22.0*	*70.0*
Total Expenditure	(593)	(825)	(949)	(713)	(838)	(1,473)
Cost of construction	(513)	(633)	(299)	(141)	(277)	(955)
Other operating exp	(51)	(136)	(537)	(477)	(445)	(366)
Personnel	(8)	(12)	(22)	(29)	(34)	(45)
Administrative exps	(22)	(44)	(91)	(66)	(82)	(107)
EBITDA	621	1,570	802	810	1,020	1,686
% chg	*362.8*	*152.8*	*(48.9)*	*1.0*	*25.9*	*65.3*
(% of Net Sales)	*51.1*	*65.5*	*45.8*	*53.2*	*54.9*	*53.4*
Depreciation	(1)	(1)	(4)	(72)	(11)	(19)
EBIT	620	1,568	798	738	1,009	1,667
% chg	*364.4*	*152.9*	*(49.1)*	*(7.5)*	*36.7*	*65.2*
(% of Net Sales)	*51.1*	*65.5*	*45.6*	*48.4*	*54.3*	*52.8*
Interest & other chgs	(5)	(4)	(58)	(46)	(82)	(78)
Other Income	10	38	32	14	113	68
(% of PBT)	2	2	4	2	11	4
Recurring PBT	625	1,602	771	705	1,039	1,657
% chg		*156.3*	*(51.8)*	*(8.6)*	*47.4*	*59.4*
Extraordinary Exp/(Inc.)	-	-	-	-	-	-
PBT (reported)	625	1,602	771	705	1,039	1,657
Tax	(77)	(192)	(94)	(133)	(208)	(331)
(% of PBT)	*12.3*	*12.0*	*12.2*	*18.9*	*20.0*	*20.0*
PAT (reported)	548	1,410	677	572	832	1,325
Add: Associate's earnings	-	-	-	-	-	-
Less: Minority interest-MI	0	(0)	(1)	(0)	-	-
Prior period items	-	(0)	109	(6)	-	-
PAT after MI (reported)	548	1,410	786	567	832	1,325
ADJ. PAT	548	1,410	677	567	832	1,325
% chg	*367.2*	*157.3*	*(52.0)*	*(16.3)*	*46.8*	*59.4*
(% of Net Sales)	*45.1*	*58.9*	*38.7*	*37.2*	*44.8*	*42.0*
Basic EPS (Rs)	25.6	65.8	28.5	15.8	20.0	31.9
Fully Diluted EPS (Rs)	13.2	33.9	18.9	13.6	20.0	31.9
% chg	*367.2*	*157.3*	*(44.2)*	*(27.9)*	*46.8*	*59.4*

Balance Sheet (Consolidated)

Y/E March (Rs cr)	FY2007	FY2008	FY2009	FY2010	FY2011E	FY2012E
SOURCES OF FUNDS						
Equity Share Capital	180	214	275	359	415	415
Preference Capital	-	-	-	-	-	-
Reserves& Surplus	554	3,427	4,146	6,684	8,767	9,998
Shareholders' Funds	**734**	**3,642**	**4,422**	**7,043**	**9,182**	**10,413**
Minority Interest	-	0	0	0	0	0
Total Loans	376	3,113	4,143	4,102	3,702	3,702
Deferred Tax Liability	1	2	2	5	5	5
Total Liabilities	**1,111**	**6,756**	**8,568**	**11,150**	**12,889**	**14,120**
APPLICATION OF FUNDS						
Gross Block	27	58	65	194	442	658
Less: Acc. Depreciation	2	3	6	11	22	41
Net Block	**25**	**54**	**60**	**183**	**420**	**617**
Capital Work-in-Progress	0	5	15	22	22	22
Goodwill	2	9	48	259	259	259
Investments	**158**	**191**	**249**	**243**	**243**	**243**
Current Assets	1,782	7,241	8,865	11,319	13,855	15,137
Cash	6	351	75.5	792	1,381	1,510
Loans & Advances	141	1,311	1,708	1,565	1,800	1,980
Other	1,636	5,580	7,082	8,962	10,674	11,647
Current liabilities	859	748	669	876	1,909	2,158
Net Current Assets	**923**	**6,493**	**8,196**	**10,443**	**11,946**	**12,979**
Mis. Exp. not written off	2	2	-	-	-	-
Total Assets	1,111	6,756	8,568	11,150	12,889	14,120

Cash Flow Statement (Consolidated)

Y/E March (Rs cr)	FY2007	FY2008	FY2009	FY2010	FY2011E	FY2012E
Profit before tax	625	1,602	771	705	1,039	1,657
Depreciation & others	(2)	(46)	15	113	93	97
Change in Working Capital	(754)	(5,345)	(1,823)	(1,615)	(1,008)	(904)
Less: Other income	10	38	32	14	113	68
Direct taxes paid	(20)	(164)	(63)	(120)	(208)	(331)
Cash Flow from Operations	**(161)**	**(3,991)**	**(1,132)**	**(931)**	**(196)**	**451**
(Inc.)/ Dec. in Fixed Assets	(62)	(45)	(62)	(342)	(248)	(217)
(Inc)/ Dec. in Investments	-	(23)	(57)	0	-	-
Other	11	39	32	20	113	68
Cash Flow from Investing	**(50)**	**(29)**	**(88)**	**(322)**	**(135)**	**(149)**
Issue of Equity	(1)	1,712	-	2,078	1,403	-
Inc./(Dec.) in loans	179	2,737	1,031	(42)	(400)	-
Dividend Paid (Incl. Tax)	-	(49)	(75)	(0)	-	(95)
Others	(4)	(35)	(11)	(67)	(82)	(78)
Cash Flow from Financing	**174**	**4,365**	**944**	**1,970**	**921**	**(172)**
Inc./(Dec.) in Cash	(38)	346	(275)	716	589	129
Opening Cash balances	**44**	**6**	**351**	**75**	**792**	**1,381**
Closing Cash balances	**6**	**352**	**75**	**792**	**1,381**	**1,510**

Key Ratios

Y/E March	FY2007	FY2008	FY2009	FY2010	FY2011E	FY2012E
Valuation Ratio (x)						
P/E (on FDEPS)	20.5	8.0	14.3	19.8	13.5	8.5
P/CEPS	20.5	8.0	16.5	17.4	13.3	8.4
P/BV	7.9	1.6	1.7	1.6	1.2	1.1
Dividend yield (%)	0.2	1.8	-	-	0.7	0.7
EV/Sales	8.0	5.1	7.7	8.3	6.3	3.7
EV/EBITDA	15.7	7.7	16.7	15.6	11.5	6.9
EV / Total Assets	4.9	1.6	1.5	1.1	0.8	0.7
Per Share Data (Rs)						
EPS (Basic)	25.6	65.8	28.5	15.8	20.0	31.9
EPS (fully diluted)	13.2	33.9	18.9	13.7	20.0	31.9
Cash EPS	13.2	34.0	16.4	15.5	20.3	32.4
DPS	0.5	5.0	-	-	2.0	2.0
Book Value	34.3	169.9	160.5	169.5	221.0	250.7
DuPont Analysis						
EBIT margin	51.1	65.5	45.6	48.4	54.3	52.8
Tax retention ratio	0.9	0.9	0.9	0.8	0.8	0.8
Asset turnover (x)	1.9	0.6	0.2	0.2	0.2	0.3
ROIC (Post-tax)	85.9	36.8	9.4	6.4	7.4	11.1
Cost of Debt (Post Tax)	10.5	11.0	12.3	10.5	9.6	9.6
Leverage (x)	0.3	0.8	0.9	0.7	0.5	0.4
Operating ROE	109.3	57.3	6.8	3.3	6.3	11.6
Returns (%)						
ROCE (Pre-tax)	83.0	39.9	10.4	7.5	8.4	12.3
Angel ROIC (Pre-tax)	98.0	41.8	10.7	7.8	9.2	13.8
ROE	59.5	64.5	16.8	9.9	10.3	13.5
Turnover ratios (x)						
Asset Turnover (GB)	74	57	28	12	6	6
Inventory/Sales (days)	271	522	1,297	1,878	1,875	1,244
Receivables (days)	59	28	23	44	53	45
Payables (days)	180	104	128	179	258	220
Wkg. Cap. (ex-cash, days)	178	538	1,487	2,130	1,986	1,273
Solvency ratios (x)						
Net debt to equity	0.5	0.8	0.9	0.5	0.3	0.2
Net debt to EBITDA	0.6	1.9	15.4	9.9	4.0	1.7
Int. coverage (EBIT/Int)	10.1	10.2	0.4	0.5	1.1	2.9

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DISCLAIMER

Disclosure of Interest Statement	**HDIL**
1. Analyst ownership of the stock	No
2. Angel and its Group companies ownership of the stock	Yes
3. Angel and its Group companies' Directors ownership of the stock	No
4. Broking relationship with company covered	No

Note: We have not considered any Exposure below Rs 1 lakh for Angel, its Group companies and Directors.

Ratings (Returns):	*Buy (> 15%)*	*Accumulate (5% to 15%)*	*Neutral (-5 to 5%)*
	Reduce (-5% to 15%)	Sell (< -15%)	

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