INDIA

Punj Lloyd

5 February 2007

PUNJ IN		Outperform
Stock price as of 01 Feb 07	Rs	1,019.40
12-month target	Rs	1,315.00
Upside/downside	%	+29.0
Valuation	Rs	1,315.00
- EV/EBITDA		
GICS sector		capital goods
Market cap	Rs m	53,263
30-day avg turnover	US$ m	9.78
Market cap	US$m	1,210
Number shares on issue	m	52.25

Investment fundamentals

Year end 31 Mar		2006A	2007E	2008E	2009E
Total revenue	m	16,846	50,001	73,257	89,816
EBITDA	m	1,909	3,333	6,118	8,361
EBITDA growth	%	-9.6	74.6	83.6	36.7
Recurring profit	m	814	2,029	3,682	5,445
Reported profit	m	555	1,554	2,574	3,808
Adjusted profit	m	538	1,539	2,574	3,808
EPS rep	Rs	17.34	29.76	49.29	72.92
EPS adj	Rs	18.56	29.48	49.29	72.92
EPS adj growth	%	513.7	58.8	67.2	48.0
PE adj	x	54.9	34.6	20.7	14.0
ROA	%	6.6	8.1	11.2	12.0
ROE	%	6.6	12.9	18.4	22.3
EV/EBITDA	x	30.6	17.5	9.5	7.0
Net debt/equity	%	39.6	42.8	81.1	84.4
Price/book	x	4.7	4.2	3.5	2.8

PUNJ IN rel SENSEX performance, & rec history

Source: Datastream, Macquarie Research, February 2007
(all figures in INR unless noted)

Analyst

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Stellar growth ahead

Event

- We initiate coverage on Punj Lloyd (PL) with an Outperform rating and 12-month target price of Rs1,315. Our target price is derived from the average of mid-sized peer EV/EBITDA multiple of 10.5x on FY09E. PL is on the cusp of explosive growth driven by strong order inflows and a huge expansion in capability set.

Impact

- **Graduating to the big league.** PL is consolidating its position as the second largest E&C player in India. The widening gap in revenues with respect to other mid-sized players is only a small part of the story. More importantly, it is increasing the capability gap. The Rs13bn offshore platform contract from ONGC is a case in point where it broke L&T's virtual monopoly in the sector.
- **Fastest growth driven by huge order inflows.** PL has fully exploited the capex upsurge in the core areas of competence – pipeline and petrochemical projects in overseas markets and the uptick in domestic infrastructure spend. Book-to-bill ratio of 3.7x as at end 3QFY07, driven by order intake of Rs125bn over FY06-07 is expected to translate into 61% revenue CAGR over FY06–09E.
- **Profits expected to double in two years.** Decline in depreciation and interest costs as the proportion of revenues should drive an expansion in net margins, driving 94% CAGR in profits over FY06–09E. Increasing asset utilization efficiency should drive an improvement in profitability ratios.
- **Acquisition triggers new growth avenues.** Recently acquired SembCorp E&C has significant EPC experience in a large number of high growth sectors like upstream oil & gas, SEZs and airports where PL did not have a presence. This should result in significant expansion in the addressable market for PL.
- **Geographic diversification reduces risk.** PL has the most diversified order book when compared to domestic E&C peers. Overseas projects account for more than one-third of its order book. This makes the order book resilient to vagaries of the capex cycle in a particular geography.

Price catalyst

- 12-month price target: Rs1,315.00 based on a EV/EBITDA methodology.
- Catalyst: Strong revenue growth driven by recent wins and continued order inflows from new sectors

Action and recommendation

- The stock trades at PER of 20.7x on FY08E earnings – a significant discount to L&T trading at an adjusted PER of 28.7x and a slight premium to mid-sized peers at 18.4x. We expect significant acceleration in growth as revenues from recent big ticket wins kick in. We recommend Outperform with a price target of Rs1,315, offering 29% upside from current levels.

Company profile

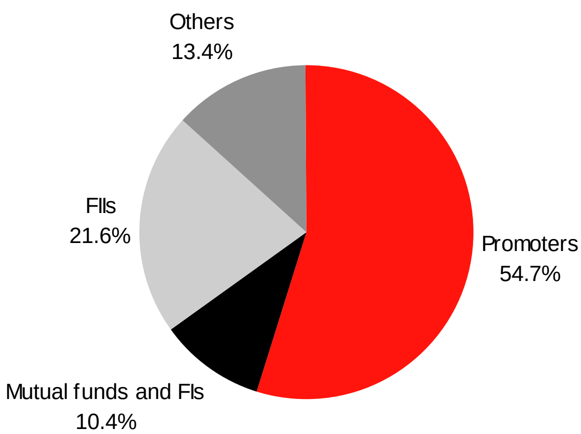
Punj Lloyd (PL) is a Delhi-based engineering construction company. Its main lines of business are offshore and onsite pipelines, oil & gas terminals, process facilities for the oil & gas industry and civil infrastructure construction. The company executes projects mainly in the Middle East, the Caspian Sea, South-East Asia and South Asia. It is gradually increasing its geographic presence and has recently won large orders in Africa.

It was incorporated in 1988 as Punj Lloyd Engineering Private Ltd. It was formed through the transfer of Punj Sons Pvt Ltd's engineering and general construction division, a part of the Punj group of companies, which has been operational since 1954. The name was subsequently changed to Punj Lloyd and the company first went public in 1992. The company was subsequently delisted and again went public in December 2005. Atul Punj is the current chairman & managing director. The promoter group holds a 54.67% stake in the company.

The company is focussed on the energy industry, undertaking projects for Indian and international energy majors across diverse geographies. It has significant expertise in pipeline construction; this segment contributed around half of FY06 consolidated revenues and 37% of the current order book.

To augment its engineering & project management skills and transform itself into a complete EPC player, the company recently acquired Singapore based SembCorp and its UK based subsidiary Simon Carves. SembCorp has significant E&C capabilities ranging from master planning to detailed engineering design to project & construction management across a wide variety of segments including speciality buildings, industrial parks, airports, jetties, mass rapid transport systems and tunnelling. Simon-Carves has significant EPC capabilities in petrochemical and refinery plants.

Fig 1 Shareholding pattern



Source: Company data, Macquarie Research, January 2007

Stellar growth ahead

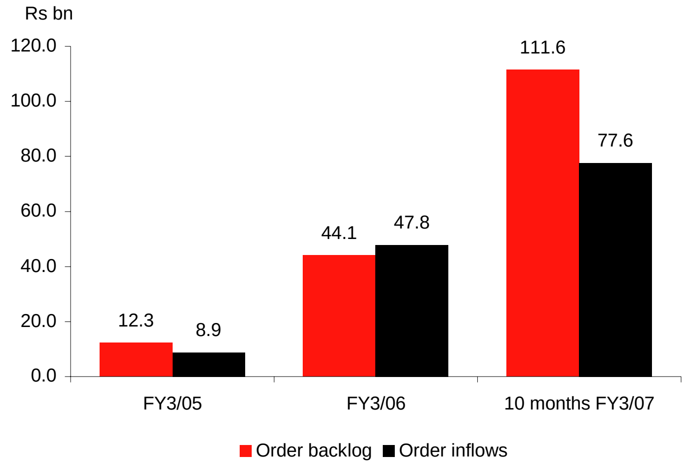
We initiate coverage on Punj Lloyd (PL) with an Outperform rating and 12-month target price of Rs1,315. Our target price is derived from an EV/EBITDA of 10.5x on FY09E. The target multiple is in line with adjusted EV/EBITDA multiples of mid-sized peers on FY08 and a 12.5% discount to industry leader, L&T.

PL is on the cusp of explosive growth, driven by a strong order book position and huge expansion in capability set. The company's growth outlook appears much brighter than those of its peers. We expect PL to enter the big league and pull ahead of mid-sized peers both in size and competencies. Also, lower dependence on domestic order inflows makes the growth momentum more robust. However, we would wait for more evidence of consistent execution at a higher scale before according a valuation premium to account for the superior growth.

Expect industry leading growth as order inflows are on a roll

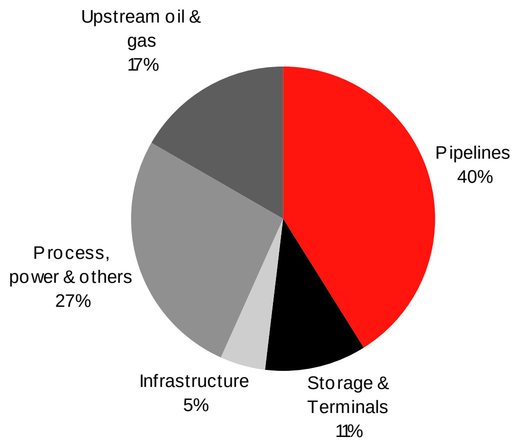
Punj Lloyd's order book has swelled over the last seven quarters. Order inflows worth Rs47bn in FY06 and Rs77.6bn in FY07 to date have resulted in a seven-fold increase in order book from Rs12.2bn at the beginning of FY06 to Rs102bn currently. This translates into 4.2x trailing twelve months revenues as at end 3QFY07.

Fig 2 Order inflows and backlog position



Source: Company data, Macquarie Research, January 2007

Fig 3 Order inflows by sector in FY07



Source: Company data, Macquarie Research, January 2007

PL has enjoyed huge order inflows in FY07 on account of:

- Buoyancy in sectors of traditional strength like pipelines and terminals. These sectors have contributed about a half of order inflows during FY07. Expansion into newer geographies like Africa has helped the order intake momentum. During the year, the company has won large pipeline orders worth Rs13.3bn from the Libyan national oil company.
- Entry into new sectors like upstream oil & gas. Helped by SembCorp's significant expertise and prequalification, the company has broken L&T's virtual monopoly in domestic orders in this sector.
- Focus on bidding for large projects. The average size of projects won during FY07 amounts to US$100m as compared to US$30m prior to FY07. The company intends to further increase the average size to US$200m.

The strong order book position and relatively shorter execution cycle of major orders as compared to infrastructure projects should translate into industry leading growth over the next couple of years. **We expect 61% CAGR in revenues over FY06-09E**.

Graduating to the big league

Punj Lloyd intends to become a large global E&C player and has set a target of becoming one of top five global EPC companies in the next five years. The target might be too steep to be realistic but it does underline PL's strategic intent. Together with SembCorp, Punj Lloyd has the widest range of EPC capabilities across sectors among Indian peers. It is increasing the capability gap vis-à-vis mid-cap peers and fast catching up with industry leader, L&T.

Fig 4 Order book and capability comparision of Indian E&C companies

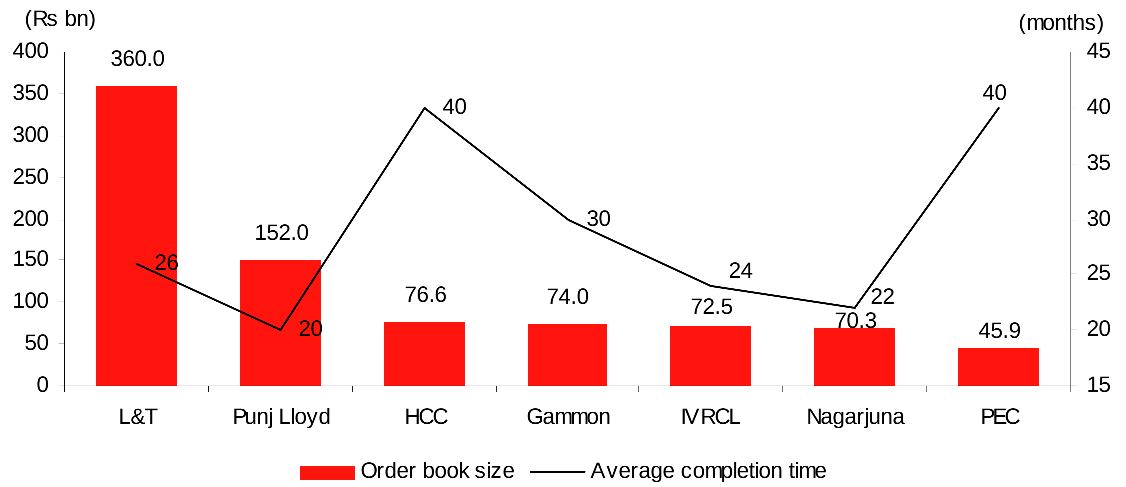
	Capabilities									
Company	Upstream oil & gas	Process plants	Pipelines & terminals	SEZs	MRTS	Airports	Thermal power	Hydropower	Civil	International orders
Punj Lloyd	x	x	x	x	x	x	x		x	x
L&T	x	x	x	x	x	x	x	x	x	x
HCC			x		x		x	x	x	
Gammon			x				x	x	x	x
PEC								x	x	
IVRCL									x	
Nagarjuna									x	x

Source: Macquarie Research, January 2007

The recent US$290m EPC contract from ONGC for an offshore platform is an example of PL's growing stature as a complete E&C player. Prior to this win, L&T had a virtual monopoly on ONGC's offshore platform contracts – it was the only domestic player present in this segment. With this win, the company has broken into a large, high-margin segment with few domestic competitors.

Though FY06 revenues for PL are comparable to that of mid-sized peers, it enjoys a much larger order book position. Also the execution cycle is much shorter as projects in the company's main area of operation – pipelines, tankages and process plants – have a completion time of 15-24 months as compared to 24-30 months for infrastructure projects. This should result in the company pulling way ahead of mid-cap peers over the next couple of years with the revenue gap in line with capability difference.

Fig 5 Order book position and average execution time



Punj Lloyd order book is inclusive of its 100% owned sub Sembawang E&C.
HCC's order book excludes the Rs19bn Sawalkote hydropower project.

Source: Company data, Macquarie Research, January 2007

Geographical diversification reduces leverage to domestic capex cycle

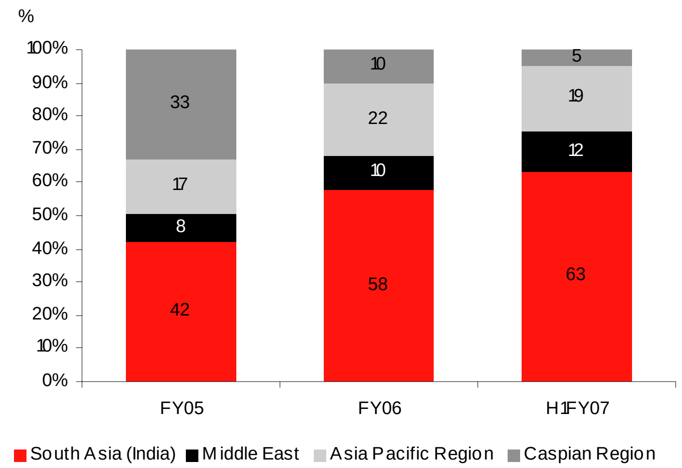
Punj Lloyd has the widest geographical footprint amongst Indian E&C companies. Overseas contracts make a significant contribution to PL's revenues and order inflows. International projects accounted for:

- ~40% of revenues during last two fiscal years – FY05 and FY06
- 41% to order inflows in FY07
- 37% of the current order book

This is by far the largest exposure to overseas markets for an Indian E&C player and is almost double that of next most diversified player, L&T where international projects account for ~20% of the revenues and order inflows.

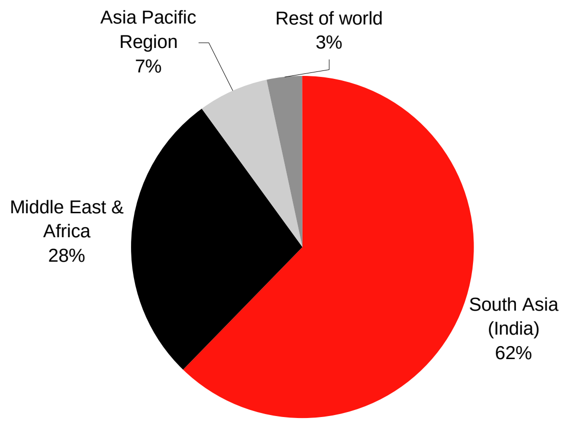
It has built significant local presence in the oil producing regions of Middle East, Caspian Sea and South East Asia. Recent large order wins in Libya would consolidate its position in Africa. Acquisition of SembCorp E&C would further strengthen its local presence in Southeast Asia and increase PL's coverage to new geographies like China, Iran and the UK.

Fig 6 Geographical break-up of revenues



Source: Company data, Macquarie Research, January 2007

Fig 7 Current order book composition by region



Source: Company data, Macquarie Research, January 2007

Wider geographical coverage not only expands the exploitable opportunity set but also decreases the leverage to domestic investment cycle. Any delay in fresh project awards by domestic agencies can be compensated by international order inflows, thereby reducing volatility in order intake. Also, a wider choice of projects allows more headroom in bidding for projects with better profitability.

Order inflow momentum to sustain as addressable market increases

To augment its engineering & project management skills and transform itself into a complete EPC player, PL acquired Singapore based SembCorp E&C (since renamed Sembawang E&C) and its UK based subsidiary Simon Carves for a consideration of Rs1173m.

Sembawang E&C together with its subsidiaries have significant capabilities ranging from master planning to detailed engineering design to project & construction management across a wide variety of segments including:

- Upstream oil & gas
- Petrochemical and refinery process plants
- Speciality buildings, industrial parks and SEZs
- Airports, jetties and seaports
- Mass rapid transport systems

Before this acquisition, PL's main competency lay in pipelines & storage construction for oil & gas sector and civil and infrastructure sectors. This acquisition significantly broadens the spectrum of capabilities for the company. Order inflows over the last two years have been driven by the traditional strongholds of the company. We expect the newer sectors to drive order flow momentum over the medium term. The recent large ONGC contract is a case in point. These sectors are expected to commit fresh investments of Rs2,340bn over the next three years in the domestic market.

Fig 8 New domestic opportunities addressable over next three years

Sector	Investments (Rs bn)	% addressable	Order flows (Rs bn)
ONGC capex	400	40	160
Reliance petrochemical and E&P	200	40	80
Others	250	40	100
Ports	400	50	200
Airports	90	50	45
Urban Infrastructure	750	60	450
SEZs and speciality buildings	250	80	200
Total	**2340**	**360**	**1235**

Source: Macquarie Research, January 2007

PL can exploit the newly acquired capabilities in the overseas markets as well. For example, Simon-Carves has been selected as the EPC contractor for GBP154m ethanol plant in the UK. Simon-Carves can now farm out a part of construction to PL rather than outsourcing the entire job as was the case earlier.

Enhanced capabilities would also help **Dayim Punj Lloyd Engineering** – the 49% owned JV with Prince Khalid Bin Bandar Bin Sultan of Saudi Arabia – corner a bigger chunk of the US$33bn investment proposed for the King Abdullah City near Jeddah. Sembawang's skills in speciality buildings, sewerage systems and MRTs would be especially useful. In addition to this mega project, the prince would help the JV identify opportunities in the oil & gas, petrochemical and urban infrastructure sectors as well.

Focus on large projects increases scalability

The company has increased focus on increasing the average ticket size of individual orders. The company had an average ticket size of US$30m prior to the current fiscal year. FY07 orders have an average ticket size of US$100m. Large orders have accounted for 87% of the total inflows in FY07. The company intends to increase the average contract size to US$200m. Increase in size of individual projects reduces scalability issues as management resources required per dollar of revenue decreases.

Fig 9 Pre-dominance of large ticket orders in FY07 inflows

Project	Cost (Rs bn)	Location	Agency	Award date
Heera Redevelopment project	13.0	Mumbai	ONGC	Jan-07
Hydrocracker unit	8.6	Haldia	IOCL	Nov-06
500 MW Chabbra Thermal power plant	8.2	Rajasthan	State PSU	Aug-06
Doha urban pipeline relocation project	8.0	Doha, Qatar	Qatar Petroleum	Nov-06
Tripoli to Melita gas pipeline	6.9	Tripoli, Libya	Sirte Oil Co	Aug-06
El Khoms Tripoli gas pipeline	6.5	Tripoli, Libya	Sirte Oil Co	Aug-06
Pipeline & electrical lines	3.6	Kazakhstan	Agip KCO Kazakhstan	Jun-06
Naphtha cracker storage facilities	3.5	Panipat	IOCL	Sep-06
Offsites and utilities for Yemen LNG	3.2	Yemen	Yemgas	Aug-06
Lalsot to Kota Road in Rajasthan	3.0	Rajasthan	RIDCOR	Jun-06
Hydrogen generation unit	3.0	Haldia	IOCL	Nov-06
Total large projects	**67.5**		**as % of total inflows**	**87.0**

Source: Company data, Macquarie Research, January 2007

Financials

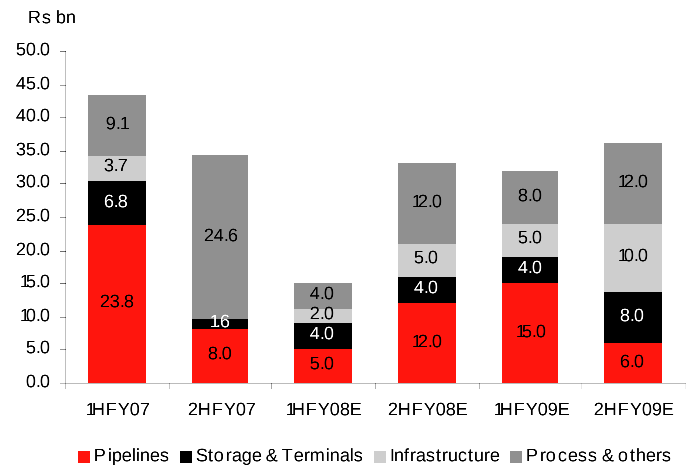
We estimate revenue CAGR of 61% over FY06–09

PL has witnessed huge order inflows of Rs125bn over the last seven quarters, driven by an uptick in oil & gas investments both in the domestic and global markets. The company has a strong order book position of Rs102bn which translates into 4.2x trailing twelve months revenues as at end 3QFY07.

We have assumed an order inflow of Rs116bn over FY08-09 in our model. There exist upsides to our inflow assumptions as we expect the order intake momentum to remain strong over FY08-09 driven by:

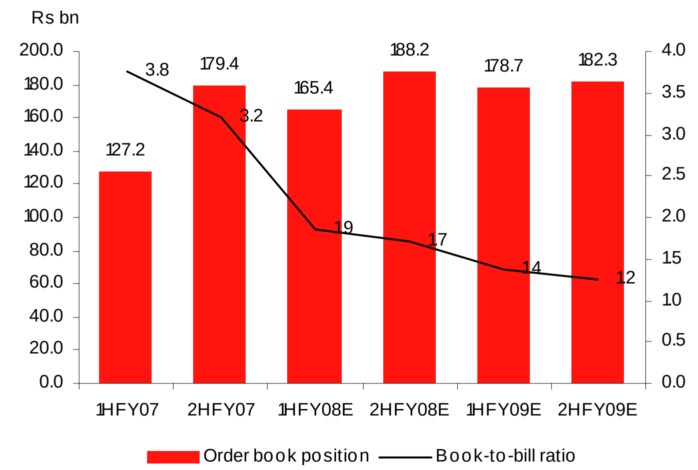
- Continued upturn in the domestic capex cycle
- Strong outlook for oil & gas investments in Middle East and Africa
- Expansion of addressable market for PL as skill sets increase

Fig 10 Order intake over FY07-09E



Source: Company data, Macquarie Research, January 2007

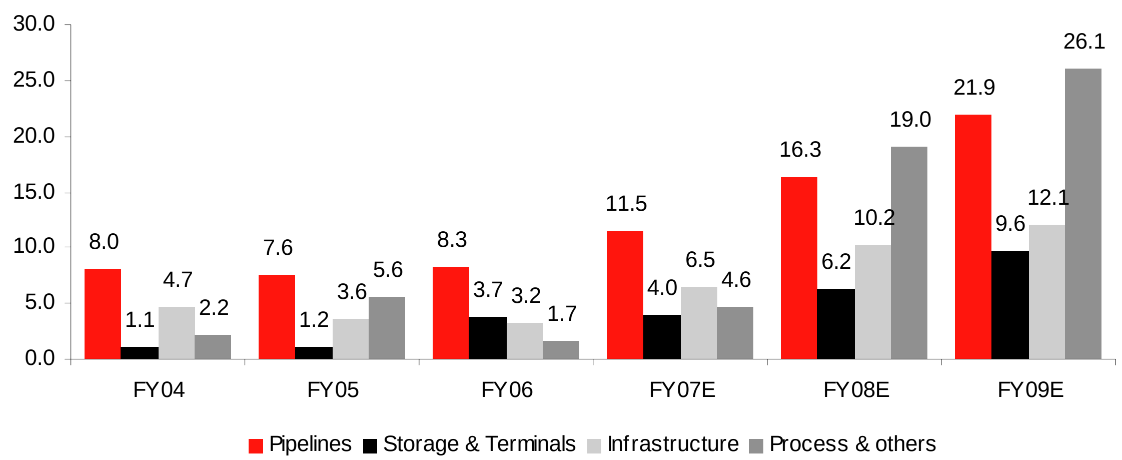
Fig 11 Order book position



Source: Company data, Macquarie Research, January 2007

Driven by strong current order book position, continued robustness in order inflows and shorter execution cycle of 15-20 months in the largest segment of pipeline and oil & gas sector, we expect revenue CAGR (excluding Sembawang E&C revenues) of 61% over FY06-09E.

Fig 12 Revenues by segment

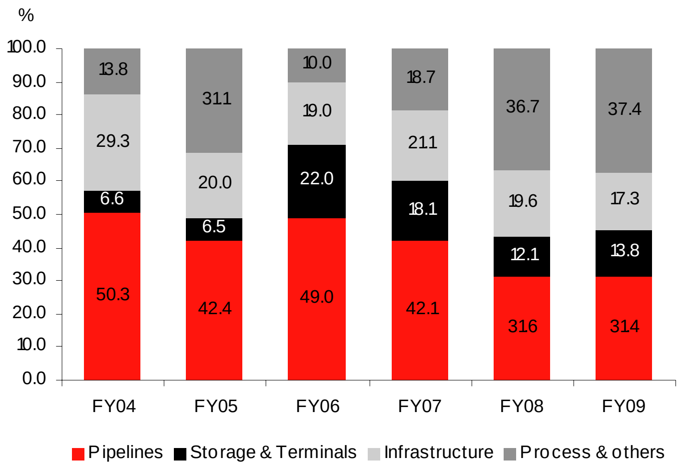


Source: Company data, Macquarie Research, January 2007

EBITDA growth to track revenue growth

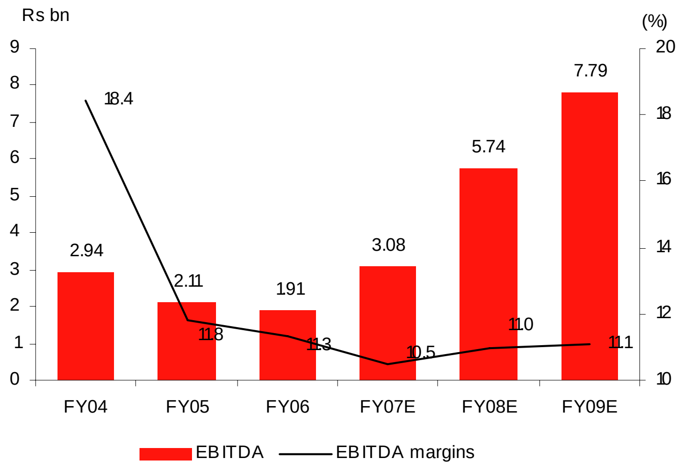
We estimate EBITDA margins (excluding Sembawang E&C) to remain stable at FY06 levels. With order inflows driven by pipeline and process plant projects and PL's continued focus on these sectors, we expect revenues from the relatively low margin infrastructure and civil projects to remain below 20% over FY07E-09E. Increasing complexity and ticket size of projects in the core segments are likely to drive an increase in margins. However, expansion into new geographies and segments could potentially put pressure on margins. Hence, we estimate margins to stay stable in the forecast period. Consequently, EBITDA CAGR during FY06-09E at 59.8% should track revenue growth over the period.

Fig 13 Revenue mix



Source: Company data, Macquarie Research, January 2007

Fig 14 EBITDA margins



Source: Company data, Macquarie Research, January 2007

Sembawang E&C profit contribution a while away

PL acquired Sembawang E&C (SEC) in June 2006 for expanding its competency set rather than adding to the bottom line. SEC has a large revenue base but very low profitability as it farms out actual construction contracts and only does the engineering and construction management in-house. Profitability was also hit by the fact that the company was in sell-off mode for a couple of years prior to the acquisition. CY05 revenues at Rs32.2bn were much higher than that of PL but the company had virtually no profits.

We expect margins to improve going forward as the PL streamline operations, progressively shifts engineering and design functions from high cost geographies like Singapore and the UK and bids for projects with better margins. However, this would take a while as the major proportion of revenues in the next couple of years would be driven by the existing Rs41bn low-margin order book. In addition, changes in order intake profile would take some time. This would also have an impact on revenue growth as well with the company potentially eschewing some low-margin projects.

Fig 15 Sembawang E&C revenues and EBITDA

	FY07E (10 months)	FY08E	FY09E
Revenues (Rs m)	20672	20963	19552
Revenue growth (%)		1.4	-6.7
EBITDA	250	374	568
EBITDA margins (%)	1.2	1.8	2.9

Source: Macquarie Research, January 2007

Net profit growth should lead revenue growth

Net margins (excluding Sembawang E&C) should expand by 210 bp over FY06-09E as interest and depreciation costs decline as proportion of revenues. Depreciation costs as proportion of revenues have been high in the past on account of low asset utilization. We expect this proportion to come down as asset efficiency increases going forward. Repayment of high interest rate bearing debt after recent capital raising would bring down interest costs. Consequently, we estimate net profits CAGR of 94% over FY06-09E driven by 210 bp expansion in net margins.

Fig 16 Consolidated profit & loss account

(Rs m)	FY05	FY06	FY07E	FY08E	FY09E
Revenues	**17,900**	**16,846**	**50,001**	**73,257**	**89,816**
Contract revenues ex SEC	17,035	15,982	28,714	51,694	69,665
Other operational revenues	584	564	200	200	200
Internet Services	281	301	415	399	399
Sembawang			20,672	20,963	19,552
Expenses	15,788	14,937	46,668	67,139	81,455
EBITDA	**2,112**	**1,909**	**3,333**	**6,118**	**8,361**
EBITDA excl SEC	2,112	1,909	3,083	5,744	7,793
Sembawang EBITDA			250	374	568
Depreciation & amortization	887	604	1,063	1,489	1,729
EBIT	1,225	1,306	2,270	4,629	6,632
Other Income	374	303	719	400	400
Interest	1,333	794	960	1,347	1,587
PBT	**265**	**814**	**2,029**	**3,682**	**5,445**
Tax	194	291	493	1,105	1,634
PAT	71	523	1,536	2,578	3,812
Share of associates profits	3	8	0	0	0
Minority profits	-2	-7	-3	4	4
Net profit	**76**	**538**	**1,539**	**2,574**	**3,808**
Interest on debt	66	15	15	0	0
Other extraordinary and non-recurring	864	2	0	0	0
Reported profit	**1,006**	**555**	**1,554**	**2,574**	**3,808**
EPS (Rs)	**3.0**	**10.3**	**29.5**	**49.3**	**72.9**
Margins (%)					
Overall EBITDA margins (%)	11.8	11.3	6.7	8.4	9.3
EBITDA excl SEC	11.8	11.3	10.5	11.0	11.1
SEC EBITDA			1.2	1.8	2.9
PBT margin	1.5	4.8	4.1	5.0	6.1
PAT margin	0.4	3.2	3.1	3.5	4.2
Tax rate	73.1	35.8	24.3	30.0	30.0
Growth (%)					
Revenues	12.3	-5.9	196.8	46.5	22.6
PL Revenues		-5.9	74.1	78.3	34.4
Overall EBITDA	-28.1	-9.6	74.6	83.6	36.7
PL EBITDA	-28.1	-9.6	61.5	86.3	35.7
SEC EBITDA				49.5	51.7
PAT	-92.8	604.7	186.2	67.2	48.0

Source: Company data, Macquarie Research, January 2007

Return ratios should improve as asset efficiency increases

Low asset utilization rates have had a dampening effect on the return ratios in the past. Slower order inflows in the past couple of years resulted in lower order book size as compared to the asset base created by the company. This impacted the turnover and return ratios. Strong order inflows over FY06-07 have corrected that situation and should drive efficiency in asset utilization.

Fig 17 Consolidated balance sheet

(Rs m)	FY05	FY06	FY07E	FY08E	FY09E
Sources of funds					
Shareholders' funds	**5,102**	**11,215**	**12,710**	**15,224**	**18,972**
Share Capital	252	522	522	522	522
Reserves & Surplus	4,850	10,693	12,188	14,702	18,450
Share premium account	2,539	7,977	7,977	7,977	7,977
Other reserves	2,310	2,716	4,210	6,725	10,473
Minority Interest	17	9	9	9	9
Total loan Funds	**7,187**	**5,550**	**12,112**	**19,112**	**22,612**
FCCB			5,563	5,563	5,563
Deferred tax liability	618	607	607	607	607
Total funds employed	**12,924**	**17,381**	**25,438**	**34,952**	**42,200**
Application of funds					
Gross block	7,413	9,070	14,570	17,070	19,570
Less: Depreciation	2,762	3,280	4,343	5,831	7,560
Net Block	4,651	5,790	10,227	11,238	12,010
Capital - Work In Progress	481	1,230	1,230	1,230	1,230
Net Fixed Assets	**5,133**	**7,020**	**11,457**	**12,469**	**13,240**
Preoperative Expenditure	98	156	156	156	156
Investments	259	416	1,916	1,916	1,916
Current Assets	**11,288**	**15,464**	**19,775**	**34,574**	**45,974**
Inventory	5,510	8,043	9,833	17,704	23,858
Debtors	3,364	4,024	5,900	9,914	13,360
Cash & bank balances	432	1,106	1,110	1,191	1,022
Other Current Assets	54	111	100	100	100
Loans & Advances	1,928	2,179	2,832	5,665	7,635
Current liabilities & provisions	**3,855**	**5,676**	**7,867**	**14,163**	**19,086**
Net Current Assets	**7,433**	**9,788**	**11,908**	**20,411**	**26,888**
Total funds applied	**12,924**	**17,381**	**25,438**	**34,952**	**42,200**
Balance sheet ratios					
Debt:Equity	1.4	0.5	1.0	1.3	1.2
Fixed Asset Turnover	3.8	2.9	2.8	4.6	5.8
Operating Cycle (days)	142.8	188.1	137.3	135.7	135.5
Inventory days	112.4	174.3	125.0	125.0	125.0
Debtor days	68.6	87.2	75.0	70.0	70.0
Loans & advance days	39.3	47.2	36.0	40.0	40.0
Current liabilities days	78.6	123.0	100.0	100.0	100.0
Return ratios					
EBIT/asset employed	8.5	6.9	8.8	12.5	13.7
ROE	2.2	6.6	12.9	18.4	22.3

Source: Company data, Macquarie Research, January 2007

Valuations

We have arrived at our 12-month price target of Rs1315 based on an EV/EBITDA multiple of 10.5x on FY09E EBITDA. The target multiple is in line with adjusted EV/EBITDA multiples of mid-sized peers on FY08 and a 12.5% discount to industry leader, L&T.

Fig 18 Peer Valuations

					EV / EBITDA (x)		Adj EV /EBITDA (x)		PER (x)		Adj PER (x)	
Company	**Ticker**	**Price (Rs)**	**Rating**	**Target (Rs)**	**FY07E**	**FY08E**	**FY07E**	**FY08E**	**FY07E**	**FY08E**	**FY07E**	**FY08E**
Larsen & Toubro	**LT IN**	**1600**	**UP**	**1252**	**32.6**	**25.3**	**25.4**	**19.7**	**45.5**	**37.4**	**34.9**	**28.7**
IVRCL	IVRC IN	427	OP	480	26.5	17.0	13.7	8.8	41.5	25.9	21.9	13.6
Nagarjuna Const	NJCC IN	215	OP	205	17.7	13.1	14.9	11.1	26.3	19.3	22.0	16.1
Hindustan Const	HCC IN	143	UP	111	19.7	15.1	18.4	14.1	44.8	32.7	41.1	30.0
Patel Engineering	PEC IN	464	OP	500	17.3	12.6	12.9	9.3	26.3	19.2	19.2	14.0
Average ex L&T					**20.3**	**14.5**	**15.0**	**10.8**	**34.7**	**24.2**	**26.0**	**18.4**
Punj Lloyd	PUNJ IN	1019	OP	1315	19.4	10.6	19.4	10.6	34.2	20.7	34.2	20.7

Prices as on February 1, 2007
UP : Underperform; OP : Outperform
Adjusted EV / EBITDA and PER calculated by stripping out subsidiary, BOT and real estate valuations

Source: Macquarie Research, January 2007

PL is on the cusp of explosive growth driven by strong order book position and huge expansion in capability set. Growth outlook for the company is much brighter as compared to peers. We expect the company to enter the big league and pull ahead of mid-sized peers both in size and competencies. Also, lower dependence on domestic order inflows makes the growth momentum more robust. However, we would wait for more evidence of consistent execution at a higher scale before according a valuation premium to account for superior growth.

Fig 19 Valuation summary

	(Rs m)
FY09E EBITDA	8,361
EV/EBITDA (x)	10.5
EV/EBITDA (x)	87,790
Debt as at end FY08E	19,112
Equity value	68,678
No. of shares (m)	52.2
Price (Rs)	**1315**

Source: Macquarie Research, January 2007

At our 12-month target price of Rs1,315, the stock would trade at a PER of 18.0x on FY09E.

Fig 20 PL's valuation metrics at our target price

	FY06	**FY07E**	**FY08E**	**FY09E**
EBITDA (Rs m)	1909	3333	6118	8361
PAT (Rs m)	523	1536	2578	3812
EPS (Rs m)	10.30	29.48	49.29	72.92
EV/EBITDA (x)	46.0	26.3	14.3	10.5
PER (x)	127.7	44.6	26.7	18.0

Source: Macquarie Research, January 2007

Key risks

Slower-than-expected ramp-up in road projects

PL has a large exposure to NHAI road projects in the states of Assam and Rajasthan with projects won before FY06 in these geographies totalling Rs21.2bn. Implementation was tardy in these projects due to right-of-way issues and as result revenue booking from these projects were low during 1HFY07. The management has indicated that these issues have since been resolved and we expect revenues from these projects to ramp up.

Slower-than-expected ramp up in these projects can impinge on performance over the next couple of quarters. However, the proportion of these orders in the total order book has reduced considerably as the company has won large orders in the oil & gas sector. Hence, leverage of these projects on revenue growth has also reduced. Also, increased emphasis by the planning authorities to complete the awarded projects rather than awarding new projects should help resolve any residual right-of-way issues.

Legacy issues in the balance sheet

Debtors on the balance sheet include an amount of Rs378m due from Spie Capag-Petrofac (SCPIL). PL had executed a pipeline project for SCPIL in Georgia. The company had raised variation orders of Rs1.49bn against SPCIL. SPCIL had raised counterclaims of Rs477m and served a notice to the company for terminating the contract. The company has initiated arbitration proceedings against the notice. The auditors have reserved an opinion on the outcome of the dispute.

The company had executed projects for IOCL on back-to-back subcontract from Petrofac International Limited (PIL). IOCL has withheld payment to PIL, which in turn has withheld payment of Rs297.7m to PL. The company has initiated arbitration proceedings against PIL. The company has taken a credit for interest on the outstanding amount of Rs14.6m in FY06 and Rs65.7m during FY05. The credit of interest is not in accordance with AS-9 on revenue recognition. The auditors have qualified the balance sheet with respect to these matters.

In addition to these qualifications, amounts withheld by customers and disputed by the company aggregating Rs766.3m are also included as part of debtors. As a result of these disputes, amounts totaling Rs1442m out of total debtors of Rs4,024m as per FY06 balance sheet are under arbitration proceedings. Any adverse rulings in these cases could result in write-off charges going forward. However, these charges would not have an impact on future cash flows or recurring profits.

Business segments

PL has four main construction divisions: 1) oil & gas pipelines, 2) Storage tanks & terminals, 3) process plants, and 4) infrastructure and civil works. The company has made an entry into the upstream oil & gas sector with a recent large contract win from ONGC. The company also has a small broadband business.

Pipelines are the largest segment, accounting for around half of FY06 revenues and 37% of 1HFY07 order backlog. Driven by strong order inflows from the road sector during FY05 and FY06, infrastructure & civil works has the second largest share in the order book at 30%. With right-of-way issue resolved for projects in the segment, we expect a pick-up in segment revenues from 2HFY07 onwards.

To augment its engineering & project management skills and transform itself into a complete EPC player, the company acquired Singapore based SembCorp E&C (since renamed Sembawang E&C) and its UK based subsidiary Simon Carves in June 2006.

Sembawang E&C has significant capabilities ranging from master planning to detailed engineering design to project & construction management across a wide variety of segments including speciality buildings, industrial parks, airports, jetties, mass rapid transport systems and tunnelling. Simon-Carves has significant EPC capabilities in petrochemical and refinery plants. This acquisition would result in significant expansion in addressable market for the company and help maintain the strong order intake momentum.

Pipelines – Best-in-class capabilities

PL has extensive execution experience in pipeline construction, having laid around 7,730km of cross-country pipelines in various regions across the world. It has capabilities to execute EPC projects in difficult terrains and adverse climatic conditions. It is one of the few companies anywhere in the world with expertise in laying large-diameter gas pipelines and operational experience in shallow water and swampy terrain.

Given the capital intensity of the business, the company has increased focus on larger length and larger diameter pipelines. Margins in this segment are significantly higher on account of the lower competition and the company's extensive experience in executing such projects.

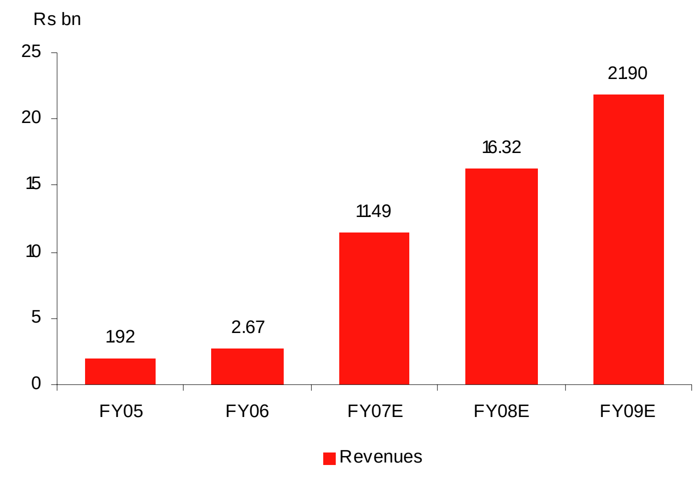
Fig 21 Major pipeline orders intake in FY07 – focusing on larger projects

Project Name	Cost	Location	Agency
Doha urban pipeline relocation project	8037	Doha, Qatar	Qatar Petroleum
Tripoli to Melita gas pipeline	6854	Tripoli, Libya	Sirte Oil Co
El Khoms Tripoli gas pipeline	6486	Tripoli, Libya	Sirte Oil Co
Pipeline from onshore facility	3573	Kazakhstan	Agip KCO - Agip Kazakhstan
Offsites and utilities for Yemen LNG project	3218	Yemen	Yemen LNG Co Ltd
Dabhol-Panvel pipeline	1642	Maharashtra	GAIL
Dahej Uran pipeline project	1383	Gujarat	GAIL

Source: Company data, Macquarie Research, January 2007

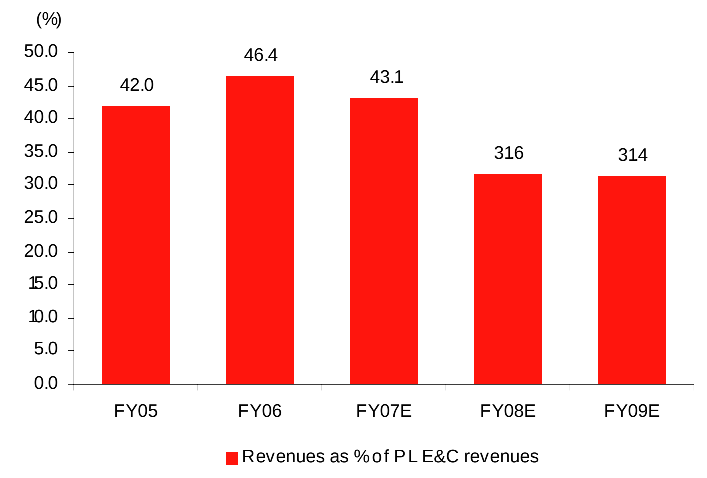
Pipelines are the largest segment, contributing around half of FY06 revenues. We expect pipelines to remain the most important segment for the company accounting for around two-fifths of revenues over the next couple of years. The segment contributed 41% to FY07 order inflows and 37% to 1HFY07 order backlog.

Fig 22 Pipeline revenues



Source: Company data, Macquarie Research, January 2007

Fig 23 Contribution to P&L overall E&C revenues



Source: Company data, Macquarie Research, January 2007

Storage tanks & terminals

In addition to best-in-class capabilities in pipeline laying, the company significant expertise in construction of storage & terminals. This enables it to offer a complete oil & gas transportation solution to clients. PL has constructed tankage and terminals with cumulative storage capacity of 6m cubic metres. The company has expertise to execute EPC contracts for various types of tanks and terminals used in the hydrocarbon sector, including cryogenic tanks for LNG and floating-roof storage tanks. The segment contributed to 22% to FY06. We expect this proportion to go down progressively as revenues from other segments grow faster. However, the segment would remain a key component of PL's capability in oil & gas sector.

Fig 24 Storage tank & terminals won during FY07

Project Name	Cost (Rs m)	Location	Agency
Naphtha cracker project storage facilities	3497	Panipat	IOCL
Dabhol LNG Terminal in JV with Whessoe UK	2093	Maharashtra	Ratnagiri Gas & Power
Bulk Liquid storage terminal	1638	Singapore	Horizon Terminal Ltd, UAE
Bulk Liquid storage	1170	Singapore	Helios Terminal Corporation

Source: Company data, Macquarie Research, January 2007

Process and power plants – thermal capacity addition plans augur well

EPC and turnkey execution capabilities in construction of process plants complete PL's expertise in oil & gas sector. The company has experience in executing contracts in a wide variety of application including gas compressor & process facilities, specialized process facilities for refineries like sulphur recovery, crude distillation, hydrocrackers and vacuum distillation units. The company can undertake the entire gamut of activities like fabrication of steel structures, erection of heavy equipment, piping, instrumentation, insulation and fireproofing services and civil works required for construction of process plants.

The company also has significant capabilities in thermal power plant construction. In this segment, it undertakes balance-of-work type of contracts where it can execute the entire construction contract except boilers and turbines. Contracts for new thermal power capacity totalling 40,000 MW are expected to be awarded over the next three years. Consequently, we expect robust order inflows from this segment.

The company has won large ticket size projects from this segment in FY07. The Rajasthan thermal power plant contract would help build pre-qualifications for much larger projects on the anvil.

Fig 25 Big ticket process and power plant contract wins in FY07

Project Name	Cost (Rs m)	Location	Agency
Hydrocracker unit (1.7 mmtpa)	8640	Haldia	IOCL
Hydrogen generation unit (70,000 tpa)	2990	Haldia	IOCL
2X250 MW Chabbra thermal plant	8230	Rajasthan	Vidyut Utpadan Nigam Ltd

Source: Company data, Macquarie Research, January 2007

Infrastructure – revenues should pick up as implementation ramps up

Infrastructure projects had the second largest share of the end-1HFY07 order book contributing 30% of the total order backlog. Highway projects in the state of Assam and Rajasthan accounted for bulk of the infrastructure order book. In addition to rich execution experience in NHAI road projects, it has also executed projects for the Delhi metro system. Sembawang's wide range of expertise in infrastructure and speciality building projects should help expand PL's span of activities in this sector.

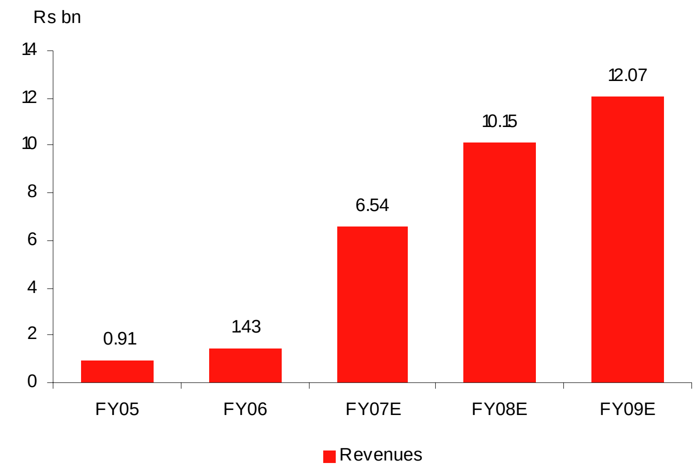
Fig 26 Major ongoing infrastructure projects

Project Name	Cost (Rs m)	Location	Agency
Assam road projects			
Guwahati-Nalbari NH-31 (AS-4)	1950	Assam	NHAI
Guwahati-Nalbari NH-31 (AS-5)	1750	Assam	NHAI
Nalbari-Bijni NH-31 (AS-8)	1420	Assam	NHAI
Nalbari-Bijni NH-31 (AS-9)	2000	Assam	NHAI
Lanka-Daboka NH-54 (AS-16)	2150	Assam	NHAI
Rajasthan road projects			
Kota-Chittorgarh (RJ-8) NH-76	4464	Rajasthan	NHAI
Hanumangarh to Ratangarh	2711	Rajasthan	RIDCOR
Ratangarh to Kishangarh	2275	Rajasthan	RIDCOR
Baran to Jhalawar	950	Rajasthan	RIDCOR
Lalsot to Kota Road in Rajasthan (LJ-1)	3020	Rajasthan	RIDCOR
Building structure for Medicity	860	Delhi	Global Health Pvt Ltd
Elevated via-duct in JV with Persys	710	Delhi	DMRC

Source: Company data, Macquarie Research, January 2007

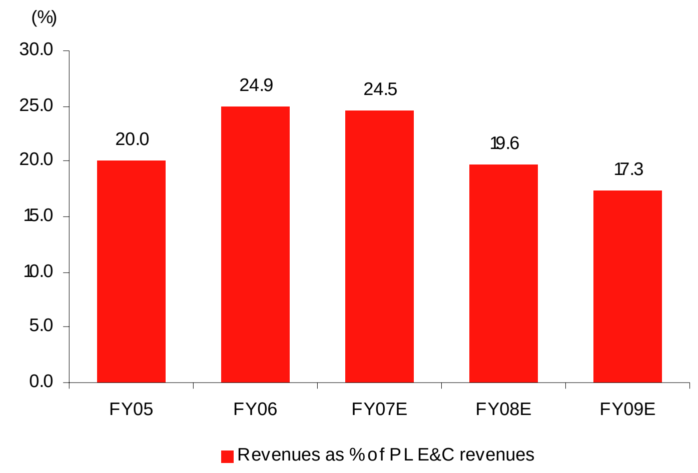
Revenues from the sector were sluggish during 1HFY07 due to right-of-way issues in the Assam and Rajasthan highway projects. The management has indicated that these issues have been resolved and implementation should ramp-up in quarters ahead. We expect the company to concentrate on implementation in this sector and hence, order inflows are likely to remain sedate over the next three-four quarters before picking up. As a result, contribution of infrastructure revenues to total revenues is expected to decline over the next couple of years.

Fig 27 Infrastructure revenues



Source: Company data, Macquarie Research, January 2007

Fig 28 Contribution to P&L overall E&C revenue



Source: Company data, Macquarie Research, January 2007

Broadband services

The company has a small broadband division and owns around 15,000 km of optical fibre network near the National Capital Region. The division provides internet bandwidth, data centre and managed network solutions to both corporate and household sectors. The division is not performing well – it made losses of Rs74m on revenues of Rs310m in FY06. Performance has improved in FY07 – revenues have grown 39% YoY to Rs216m and losses have reduced to Rs29m during the 1HFY07. The company is exploring opportunities to hive-off this business.

Punj Lloyd (PUNJ IN, Outperform, Target price: Rs1,315.00)

Quarterly Results		3Q/07A	4Q/07E	1Q/08E	2Q/08E
Revenue	**m**	**14,333**	**15,771**	**18,618**	**18,621**
Gross Profit	**m**	**3,647**	**4,034**	**4,374**	**4,389**
Cost of Goods Sold	m	10,686	11,736	14,244	14,232
EBITDA	**m**	**831**	**1,203**	**1,528**	**1,528**
Depreciation	m	296	330	350	365
Amortisation of Goodwill	m	0	0	0	0
Other Amortisation	m	0	0	0	0
EBIT	**m**	**535**	**873**	**1,178**	**1,164**
Net Interest Income	m	-279	-299	-314	-329
Associates	m	0	0	0	0
Exceptionals	m	0	0	0	0
Forex Gains / Losses	m	0	0	0	0
Other Pre-Tax Income	m	298	100	100	100
Pre-Tax Profit	**m**	**554**	**673**	**964**	**934**
Tax Expense	m	-80	-202	-289	-280
Net Profit	**m**	**474**	**471**	**675**	**654**
Minority Interests	m	6	-1	-1	-1
Reported Earnings	**m**	**483**	**474**	**674**	**653**
Adjusted Earnings	**m**	**479**	**470**	**674**	**653**
EPS (rep)		9.25	9.08	12.90	12.51
EPS (adj)		9.18	9.01	12.90	12.51
EPS Growth yoy (adj)	%	72.2	249.9	159.4	97.9
EBITDA Margin	%	5.8	7.6	8.2	8.2
EBIT Margin	%	3.7	5.5	6.3	6.2
Earnings Split	%	31.1	30.6	26.2	25.4
Revenue Growth	%	240.3	274.5	131.2	57.2
EBIT Growth	%	63.8	167.4	267.3	114.7

Profit & Loss		2006A	2007E	2008E	2009E
Revenue	**m**	**16,846**	**50,001**	**73,257**	**89,816**
Gross Profit	**m**	**5,979**	**12,813**	**17,593**	**20,076**
Cost of Goods Sold	m	10,867	37,188	55,664	69,740
EBITDA	**m**	**1,909**	**3,333**	**6,118**	**8,361**
Depreciation	m	604	1,063	1,489	1,729
Amortisation of Goodwill	m	0	0	0	0
Other Amortisation	m	0	0	0	0
EBIT	**m**	**1,306**	**2,270**	**4,629**	**6,632**
Net Interest Income	m	-794	-960	-1,347	-1,587
Associates	m	0	0	0	0
Exceptionals	m	0	0	0	0
Forex Gains / Losses	m	0	0	0	0
Other Pre-Tax Income	m	303	719	400	400
Pre-Tax Profit	**m**	**814**	**2,029**	**3,682**	**5,445**
Tax Expense	m	-291	-493	-1,105	-1,634
Net Profit	**m**	**523**	**1,536**	**2,578**	**3,812**
Minority Interests	m	15	4	-4	-4
Reported Earnings	**m**	**555**	**1,554**	**2,574**	**3,808**
Adjusted Earnings	**m**	**538**	**1,539**	**2,574**	**3,808**
EPS (rep)		17.34	29.76	49.29	72.92
EPS (adj)		18.56	29.48	49.29	72.92
EPS Growth (adj)	%	513.7	58.8	67.2	48.0
PE (rep)	x	58.8	34.3	20.7	14.0
PE (adj)	x	54.9	34.6	20.7	14.0
Total DPS		0.00	0.00	0.00	0.00
Total Div Yield	%	0.0	0.0	0.0	0.0
Weighted Average Shares	m	32	52	52	52
Period End Shares	m	52	52	52	52

Profit and Loss Ratios		2006A	2007E	2008E	2009E
Revenue Growth	%	-5.9	196.8	46.5	22.6
EBITDA Growth	%	-9.6	74.6	83.6	36.7
EBIT Growth	%	6.6	73.9	103.9	43.3
Gross Profit Margin	%	35.5	25.6	24.0	22.4
EBITDA Margin	%	11.3	6.7	8.4	9.3
EBIT Margin	%	7.8	4.5	6.3	7.4
Net Profit Margin	%	3.1	3.1	3.5	4.2
Payout Ratio	%	0.0	0.0	0.0	0.0
EV/EBITDA	x	30.6	17.5	9.5	7.0
EV/EBIT	x	44.7	25.7	12.6	8.8
Balance Sheet Ratios					
ROE	%	6.6	12.9	18.4	22.3
ROA	%	6.6	8.1	11.2	12.0
ROIC	%	7.1	11.0	17.8	16.8
Net Debt/Equity	%	39.6	42.8	81.1	84.4
Interest Cover	x	1.6	2.4	3.4	4.2
Price/Book	x	4.7	4.2	3.5	2.8
Book Value per Share		214.8	243.4	291.5	363.3

Cashflow Analysis		2006A	2007E	2008E	2009E
EBITDA	**m**	**1,909**	**3,333**	**6,118**	**8,361**
Tax Paid	m	-291	-493	-1,105	-1,634
Chgs in Working Cap	m	-1,681	-2,117	-8,421	-6,647
Net Interest Paid	m	-794	-960	-1,347	-1,587
Other	m	303	719	400	400
Operating Cashflow	**m**	**-554**	**482**	**-4,355**	**-1,106**
Acquisitions	m	-157	-1,500	0	0
Capex	m	-2,491	-5,500	-2,500	-2,500
Asset Sales	m	0	0	0	0
Other	m	-128	18	-4	-4
Investing Cashflow	**m**	**-2,775**	**-6,982**	**-2,504**	**-2,504**
Dividend (Ordinary)	m	-60	-60	-60	-60
Equity Raised	m	5,701	0	0	0
Debt Movements	m	-1,637	6,563	7,000	3,500
Other	m	0	0	0	0
Financing Cashflow	**m**	**4,004**	**6,503**	**6,940**	**3,440**
Net Chg in Cash/Debt	**m**	**674**	**3**	**82**	**-170**

Balance Sheet		2006A	2007E	2008E	2009E
Cash	m	1,106	1,110	1,191	1,022
Receivables	m	4,024	5,900	9,914	13,360
Inventories	m	8,043	9,833	17,704	23,858
Investments	m	2,595	4,748	7,581	9,550
Fixed Assets	m	7,020	11,457	12,469	13,240
Intangibles	m	0	0	0	0
Other Assets	m	268	257	257	257
Total Assets	**m**	**23,056**	**33,305**	**49,115**	**61,286**
Payables	m	5,387	7,348	13,230	17,829
Short Term Debt	m	0	0	0	0
Long Term Debt	m	5,550	6,550	13,550	17,050
Provisions	m	288	518	933	1,257
Other Liabilities	m	607	6,169	6,169	6,169
Total Liabilities	**m**	**11,832**	**20,585**	**33,881**	**42,305**
Shareholders' Funds	m	11,215	12,710	15,224	18,972
Minority Interests	m	9	9	9	9
Other	m	0	0	0	0
Total S/H Equity	**m**	**11,225**	**12,719**	**15,233**	**18,981**
Total Liab & S/H Funds	**m**	**23,056**	**33,305**	**49,115**	**61,286**

All figures in INR unless noted.
Source: Macquarie Research, February 2007

Important disclosures:

Recommendation definitions

Macquarie Australia/New Zealand
Outperform – return >5% in excess of benchmark return (>2.5% in excess for listed property trusts)
Neutral – return within 5% of benchmark return (within 2.5% for listed property trusts)
Underperform – return >5% below benchmark return (>2.5% below for listed property trusts)

Macquarie Asia
Outperform – expected return >+10%
Neutral – expected return from -10% to +10%
Underperform – expected return <-10%

Macquarie First South Securities (South Africa)
Outperform – return > 5% in excess of benchmark return
Neutral – return within 5% of benchmark return
Underperform – return >5% below benchmark return

Recommendations – 12 months

Note: Quant recommendations may differ from Fundamental Analyst recommendations

Recommendation proportions

	AU/NZ	Asia	RSA
Outperform	43.12%	58.91%	42.20%
Neutral	44.98%	22.92%	46.80%
Underperform	11.90%	18.17%	11.00%

For quarter ending 31 December 2006

Volatility index definition*

This is calculated from the volatility of historic price movements.

Very high–highest risk – Stock should be expected to move up or down 60–100% in a year – investors should be aware this stock is highly speculative.

High – stock should be expected to move up or down at least 40–60% in a year – investors should be aware this stock could be speculative.

Medium – stock should be expected to move up or down at least 30–40% in a year.

Low–medium – stock should be expected to move up or down at least 25–30% in a year.

Low – stock should be expected to move up or down at least 15–25% in a year.
* Applicable to Australian/NZ stocks only

Financial definitions

All "Adjusted" data items have had the following adjustments made:
Added back: goodwill amortisation, provision for catastrophe reserves, IFRS derivatives & hedging, IFRS impairments & IFRS interest expense
Excluded: non recurring items, asset revals, property revals, appraisal value uplift, preference dividends & minority interests

EPS = adjusted net profit / efpowa*
ROA = adjusted ebit / average total assets
ROA Banks/Insurance = adjusted net profit /average total assets
ROE = adjusted net profit / average shareholders funds
Gross cashflow = adjusted net profit + depreciation
*equivalent fully paid ordinary weighted average number of shares

All Reported numbers for Australian/NZ listed stocks are modelled under IFRS (International Financial Reporting Standards).

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