

Reiterate Buy With 56% Upside Potential



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Buy With 56% Upside Potential; Export Initiatives To Pay Off

Post our interaction with management of Nagarjuna Construction (NJCC IN) we remain convinced of robust business outlook (FY06 revenue growth guidance of 62%YoY) and believe that the recent 41% correction in the stock represents an **opportunity to Buy** as the stock offers visibility of earnings with its book-to-bill ~3x.

FY06: Backlog +51%; PAT +85%YoY & New Initiatives Pay-off

NJCC reported in-line results: sales Rs18.5bn (+56%YoY) & PAT Rs1.04bn (+85% YoY). EBIDTA +83%YoY driven by 140bps margin expansion. Order backlog up 51% to Rs54.3bn (US\$1.2bn ~3x FY06 sales). Its initiatives in export markets are also likely to bear fruit, with **20% of FY07E order intake from exports**.

Sector-Leading Earnings Growth (60% CAGR over FY06-08E)

We est NJCC's earnings to grow at a CAGR of 60% over FY06-08 led by 50% sales CAGR driven by 3x book-to-bill & order inflow (22%) and, stable margins.

Tweaking Estimates & Cut PO By 10%

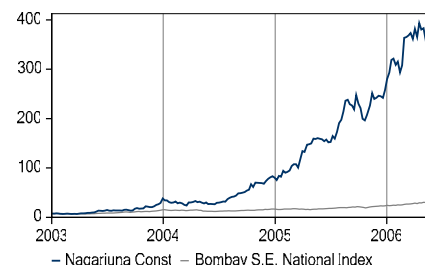
We have updated FY06 actual, FY07E & FY08E and introduce FY09E. We hike our FY08E by 1% despite 5% cut in FY07E due to higher interest rate/capex. However, we have cut our PO by 10% to factor in a) recent de-rating of Indian markets/mid-caps led us to cut target multiple for core business by 20% (to 13x) and b) higher interest rates (WACC) leading to fall in value of infra SPVs.

One Year Price Target - Rs400, +56%

Our PO of Rs400 (Rs450) is based on sum-of-the-parts. We have valued NJCC's core business at PE 13x FY08E – a 30% discount to majors & in line with its own FY07E multiples. **Risks:** Government capex, raw material costs, competition, denial of tax benefits, traffic/interest rate risk in Infra projects, & proj. execution.

Stock Data

Price (Common / GDR)	Rs257.15 / US\$5.65
Price Objective	Rs400.00 / US\$8.70
Date Established	19-Jun-2006 / 19-Jun-2006
Investment Opinion	C-1-7 / C-1-7
Volatility Risk	HIGH / HIGH
52-Week Range	Rs145.68-Rs404.45
Market Value (mn)	US\$578
Shares Outstanding (mn)	103.2 / 103.2
Average Daily Volume	245,232
ML Symbol / Exchange	NGRJF / BSE
ML Symbol / Exchange	XAKUF / LIN
Bloomberg / Reuters	NJCC IN / NGCN.BO
ROE (2007E)	18.1%
Net Dbt to Eqty (Mar-2006A)	-22.6%
Est. 5-Yr EPS / DPS Growth	25.0% / 25.0%
Free Float	73.0%



Estimates (Mar)

(Rs)	2005A	2006A	2007E	2008E	2009E
Net Income (Adjusted - mn)	570.22	1,039	1,781	2,661	3,511
EPS	7.20	10.07	17.25	25.77	34.00
EPS Change (YoY)	30.6%	39.7%	71.3%	49.4%	31.9%
Dividend / Share	1.20	1.60	2.60	3.20	3.80
Free Cash Flow / Share	(12.05)	(12.17)	(14.30)	(5.07)	(3.69)
GDR EPS (US\$)	0.165	0.226	0.376	0.562	0.742
GDR Dividend / Share (US\$)	0.027	0.036	0.057	0.070	0.083

Valuation (Mar)

	2005A	2006A	2007E	2008E	2009E
P/E	35.69x	25.55x	14.91x	9.98x	7.56x
Dividend Yield	0.467%	0.622%	1.01%	1.24%	1.48%
EV / EBITDA*	30.44x	16.83x	10.60x	7.27x	5.49x
Free Cash Flow Yield*	-3.61%	-4.73%	-5.56%	-1.97%	-1.43%

* For full definitions of *iQmethod*SM measures, see page 7.

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Refer to important disclosures on page 8 to 9. Analyst Certification on page 6. Price Objective Basis/Risk on page 6.

iQprofileSM Nagarjuna Construction Co.

Key Income Statement Data (Mar)

	2005A	2006A	2007E	2008E	2009E
(Rs Millions)					
Sales	11,885	18,505	28,999	41,547	53,611
Gross Profit	1,169	2,128	3,388	4,920	6,419
Sell General & Admin Expense	(262)	(487)	(783)	(1,124)	(1,394)
Operating Profit	798	1,459	2,387	3,512	4,689
Net Interest & Other Income	(98)	(197)	(161)	(227)	(354)
Associates	NA	NA	NA	NA	NA
Pretax Income	700	1,263	2,226	3,285	4,334
Tax (expense) / Benefit	(127)	(223)	(445)	(624)	(823)
Net Income (Adjusted)	570	1,039	1,781	2,661	3,511
Average Fully Diluted Shares Outstanding	80	103	103	103	103

Key Cash Flow Statement Data

Net Income (Reported)	573	1,039	1,781	2,661	3,511
Depreciation & Amortization	109	182	218	284	336
Change in Working Capital	(2,440)	(3,206)	(4,930)	(5,805)	(6,251)
Deferred Taxation Charge	24	0	0	0	0
Other Adjustments, Net	0	0	0	0	0
Cash Flow from Operations	(670)	(436)	(476)	76	419
Capital Expenditure	(287)	(820)	(1,000)	(600)	(800)
(Acquisition) / Disposal of Investments	(458)	(280)	(1,300)	(1,400)	(700)
Other Cash Inflow / (Outflow)	NA	NA	NA	NA	NA
Cash Flow from Investing	(745)	(1,100)	(2,300)	(2,000)	(1,500)
Shares Issue / (Repurchase)	45	47	0	0	0
Cost of Dividends Paid	(108)	(188)	(305)	(376)	(446)
Cash Flow from Financing	2,133	3,881	(352)	1,524	954
Free Cash Flow	(958)	(1,256)	(1,476)	(524)	(381)
Net Debt	1,276	(2,069)	1,060	3,359	4,886
Change in Net Debt	390	(3,345)	3,128	2,300	1,527

Key Balance Sheet Data

Property, Plant & Equipment	1,098	1,737	2,519	2,835	3,298
Other Non-Current Assets	NA	NA	NA	NA	NA
Trade Receivables	1,916	3,100	4,767	6,488	8,813
Cash & Equivalents	1,372	3,717	588	189	62
Other Current Assets	2,650	3,824	5,742	8,217	10,597
Total Assets	9,022	15,491	19,375	26,497	33,784
Long-Term Debt	2,648	1,648	1,648	3,548	4,948
Other Non-Current Liabilities	NA	NA	NA	NA	NA
Short-Term Debt	NA	NA	NA	NA	NA
Other Current Liabilities	305	305	305	305	305
Total Liabilities	5,735	6,284	8,740	13,576	17,799
Total Equity	3,213	9,133	10,561	12,846	15,911
Total Equity & Liabilities	8,947	15,417	19,301	26,422	33,710

iQmethodSM - Bus Performance*

Return On Capital Employed	15.2%	14.5%	16.8%	20.0%	20.4%
Return On Equity	23.6%	16.8%	18.1%	22.7%	24.4%
Operating Margin	6.7%	7.9%	8.2%	8.5%	8.7%
EBITDA Margin	7.6%	8.9%	9.0%	9.1%	9.4%

iQmethodSM - Quality of Earnings*

Cash Realization Ratio	-1.2x	-0.4x	-0.3x	0x	0.1x
Asset Replacement Ratio	2.6x	4.5x	4.6x	2.1x	2.4x
Tax Rate (Reported)	18.2%	17.7%	20.0%	19.0%	19.0%
Net Debt-to-Equity Ratio	39.7%	-22.6%	10.0%	26.1%	30.7%
Interest Cover	5.4x	6.7x	12.0x	13.3x	12.4x

Key Metrics

* For full definitions of iQmethodSM measures, see page 7.

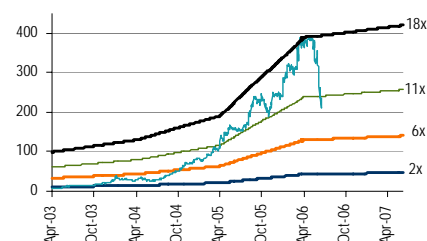
Company Description

Established in 1978 as a partnership by founder and chairman AVS Raju, NCC is engaged in civil construction work in the industrial structures, buildings, and housing sectors. It became a public limited company in 1990. NCC has moved across the domains in the engineering and construction space to capitalize on capex cycles in different subsectors.

Stock Data

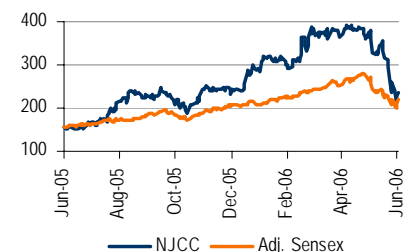
Shares / ADR	1.00
Price to Book Value	2.5x

Chart 1: PE Band



Source: Trends; ML Research

Chart 2: Stock Performance



Source: Trends

Table 1: Estimate Changes

Sales (Rsmn)	Old	New	% Change
FY07E	26,246	28,999	10.5%
FY08E	37,040	41,547	12.2%
FY09E	NA	53,611	NA
EBITDA (Rsmn)			
FY07E	2,434	2,605	7.0%
FY08E	3,565	3,796	6.5%
FY09E	NA	5,025	NA
Recurring PAT (Rsmn)			
FY07E	1,878.4	1,780.6	-5.2%
FY08E	2,645.3	2,660.7	0.6%
FY09E	NA	3,510.7	NA
EPS (Rs)			
FY07E	18.2	17.2	-5.2%
FY08E	25.6	25.8	0.6%
FY09E	NA	34.0	NA

Source: ML Research Estimates

Table 2: NCC Profit & Loss Statement

Year End Mar31 (Rsmn)	FY05	FY06A/E	FY07E	FY08E	FY09E
Gross Sales	11885	18505	28999	41547	53611
<i>Growth</i>	<i>57%</i>	<i>56%</i>	<i>57%</i>	<i>43%</i>	<i>29.0%</i>
(Inc)/Dec in Stock	165	1204	250	300	350
as % of gross sales	-1.4%	-6.5%	-0.9%	-0.7%	-0.7%
Raw Material	(5382)	(7585)	(12818)	(18281)	(23589)
as % of gross sales	45.3%	41.0%	44.2%	44.0%	44.0%
Construction Expense	(3905)	(7645)	(9309)	(13378)	(17156)
as % of gross sales	32.9%	41.3%	32.1%	32.2%	32.0%
Labour Cost	(1107)	(1778)	(2494)	(3531)	(4557)
as % of gross sales	9.3%	9.6%	8.6%	8.5%	8.5%
Staff Cost	(309)	(473)	(812)	(1122)	(1448)
as % of gross sales	2.6%	2.6%	2.8%	2.7%	2.7%
Others	(262)	(487)	(783)	(1124)	(1394)
as % of gross sales	2.2%	2.6%	2.7%	2.7%	2.6%
Total Expenditure	(10978)	(16864)	(26395)	(37751)	(48586)
EBITDA	907	1641	2605	3796	5025
EBITDA Margin (LHS)	7.6%	8.9%	9.0%	9.1%	9.4%
Depreciation	(109)	(182)	(218)	(284)	(336)
EBIT	798	1459	2387	3512	4689
EBIT Margin	6.7%	7.9%	8.2%	8.5%	8.7%
Interest	(147)	(217)	(199)	(265)	(379)
Other Income	49	20	38	37	24
PBT	700	1263	2226	3285	4334
PBT Margin	5.9%	6.8%	7.7%	7.9%	8.1%
Current Tax	(104)	(223)	(445)	(624)	(823)
Deferred Tax	(24)	0	0	0	0
Total Tax	(127)	(223)	(445)	(624)	(823)
Tax Rate	18%	18%	20%	19%	19%
Recurring PAT	573	1039	1781	2661	3511

Source: ML Research, Company

Table 3: NCC Balance Sheet

Year End Mar31 (Rsmn)	FY05	FY06A/E	FY07E	FY08E	FY09E
Share Capital	159	206	206	206	206
Reserves & Surplus	3054	8927	10355	12640	15704
Total Net worth	3221	9141	10570	12855	15919
Secured Loans	648	648	648	648	648
Unsecured Loans	2000	1000	1000	2900	4300
Total Loans	2648	1648	1648	3548	4948
DTL	66	66	66	66	66
TOTAL LIABILITIES & NET WORTH	5936	10856	12284	16469	20934
Gross Block	1665	2485	3485	4085	4885
Accumulated D&A	(576)	(758)	(976)	(1260)	(1596)
Net Block	1089	1727	2509	2825	3289
CWIP	9	9	9	9	9
Net Fixed Assets	1098	1737	2519	2835	3298
Investments	462	742	2042	3442	4142
Inventories	1523	2372	3717	5325	6872
Debtors	1916	3100	4767	6488	8813
Cash and bank balances	1372	3717	588	189	62
Loans and advances	2629	3802	5720	8196	10575
Other CA	21	21	21	21	21
Total CA	7462	13012	14814	20219	26343
CL	2781	4330	6786	9722	12545
Provisions	305	305	305	305	305
Total CL & Provisions	3087	4636	7091	10028	12851
NCA	4375	8377	7723	10192	13492
TOTAL ASSETS	5936	10856	12284	16469	20933

Source: ML Research Estimates

Table 4: NCC Cash flow statements

Year End Mar31 (Rsmn)	FY05	FY06A/E	FY07E	FY08E	FY09E
PBT	700	1263	2226	3285	4334
Tax Paid	(127)	(223)	(445)	(624)	(823)
Change in DTL	24	0	0	0	0
Add: D&A	109	182	218	284	336
Chg in Inventories	(504)	(848)	(1345)	(1608)	(1546)
Chg in Debtors	(1073)	(1184)	(1667)	(1721)	(2325)
Chg in Loans & Advances	(859)	(1174)	(1918)	(2475)	(2380)
Chg in other CA	(5)	0	0	0	0
Chg in CL	951	1549	2456	2936	2823
Chg in Provisions	114	0	0	0	0
<i>Change in Working Capital</i>	<i>(1376)</i>	<i>(1657)</i>	<i>(2474)</i>	<i>(2868)</i>	<i>(3428)</i>
Cash Flow from Operations	(670)	(436)	(476)	76	419
Capex	(287)	(820)	(1000)	(600)	(800)
Change in Investments/Assets	(458)	(280)	(1300)	(1400)	(700)
Others					
Cash Flow from Investing Activities	(747)	(1100)	(2300)	(2000)	(1500)
Change in Debt	1108	(1000)	0	1900	1400
Change in Equity	45	47	0	0	0

Table 4: NCC Cash flow statements

Year End Mar31 (Rsmn)	FY05	FY06A/E	FY07E	FY08E	FY09E
Change in Reserves	1089	5021	(47)	0	0
Dividend and Dividend Tax	(108)	(188)	(305)	(376)	(446)
Cash Flow from Financing Activities	2133	3881	(352)	1524	954
Increase/(Decrease) in Cash	715	2345	(3128)	(400)	(127)
Opening Cash and Bank Balance	657	1372	3717	588	189
Closing Cash and Bank Balance	1372	3717	588	189	62

Source: Company, ML Research Estimates

Table 5: NCC Valuation

Year End Mar31	FY05	FY06A/E	FY07E	FY08E	FY09E
Shares Price	237	237	237	237	237
Share Outstanding	79.5	103.2	103.2	103.2	103.2
Mkt Cap (Local)	18842	24469	24469	24469	24469
Mkt Cap (USD)	428	556	556	556	556
EPS	7.2	10.1	17.2	25.8	34.0
% growth	30.6%	39.7%	71.3%	49.4%	31.9%
CEPS	8.57	11.82	19.36	28.52	37.26
DPS	1.20	1.60	2.60	3.20	3.80
BV	40.5	88.5	102.4	124.5	154.2
P/E	32.9	23.5	13.7	9.2	7.0
P/CEPS	27.6	20.0	12.2	8.3	6.4
Yield	0.5%	0.7%	1.1%	1.4%	1.6%
P/BV	5.8	2.7	2.3	1.9	1.5
EV/EBITDA	22.2	13.7	9.8	7.3	5.8
EV/Sales	1.69	1.21	0.88	0.67	0.55
EV/OB	0.56	0.41	0.37	0.33	0.31
P/OB	0.52	0.45	0.35	0.29	0.26
RoCE	14.5%	14.4%	16.6%	19.9%	20.4%
RoE	24%	17%	18%	23%	24%

Source: ML Research Estimates

Table 6: NJCC- Sum Of The Parts

Parts	Rationale/stake	Value (Rs Mn)	Rs/share
NCC Construction business	13x FY08E PER - 30% discount to majors and in line with NCC's own multiples	37,250	361
Bangalore-Maddur Road SPV	DCF Value - 33% equity share	407	4
Meerut-Mu'nagar SPV	DCF Value - 30% equity share	452	4
Bagalore Elevated Tollway PVT LTd	DCF Value - 33.5% equity share	1,172	11
Orai-Bhognipur Infrastructure Ltd	DCF Value - 64%equity share	1,052	10
National Games Housing Complex project at Ranchi	DCF Value - 100% equity share	205	2
Andhra Pradesh Housing Board project in Vishakhapatnam	DCF Value - 89% equity share	227	2
Land Bank	4x Book Value; 20% discount to market	960	9
Gautami Power	Book value of Investment	226	2
Total		41,952	406

Source: ML Research Estimates

Price Objective Basis & Risk

Our PO of Rs400 is based on sum-of-the-parts. We have valued NJCC's core business at PE 13x FY08E – a 30% discount to majors & in line with its own FY07E multiples. Risks: Government capex, raw material costs, competition, potential denial of tax benefits (80IA), traffic/interest rate risk in Infra projects, & project execution.

Analyst Certification

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19 June 2006

iQmethodSM Measures Definitions

Business Performance	Numerator	Denominator
Return On Capital Employed	$\text{NOPAT} = (\text{EBIT} + \text{Interest Income}) * (1 - \text{Tax Rate}) + \text{Goodwill Amortization}$	Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill
Return On Equity	Net Income	Shareholders' Equity
Operating Margin	Operating Profit	Sales
Earnings Growth	Expected 5-Year CAGR From Latest Actual	N/A
Free Cash Flow	Cash Flow From Operations – Total Capex	N/A
Quality of Earnings		
Cash Realization Ratio	Cash Flow From Operations	Net Income
Asset Replacement Ratio	Capex	Depreciation
Tax Rate	Tax Charge	Pre-Tax Income
Net Debt-To-Equity Ratio	Net Debt = Total Debt, Less Cash & Equivalents	Total Equity
Interest Cover	EBIT	Interest Expense
Valuation Toolkit		
Price / Earnings Ratio	Current Share Price	Diluted Earnings Per Share (Basis As Specified)
Price / Book Value	Current Share Price	Shareholders' Equity / Current Basic Shares
Dividend Yield	Annualised Declared Cash Dividend	Current Share Price
Free Cash Flow Yield	Cash Flow From Operations – Total Capex	Market Cap. = Current Share Price * Current Basic Shares
Enterprise Value / Sales	$\text{EV} = \text{Current Share Price} * \text{Current Shares} + \text{Minority Equity} + \text{Net Debt} + \text{Sales} + \text{Other LT Liabilities}$	
EV / EBITDA	Enterprise Value	Basic EBIT + Depreciation + Amortization

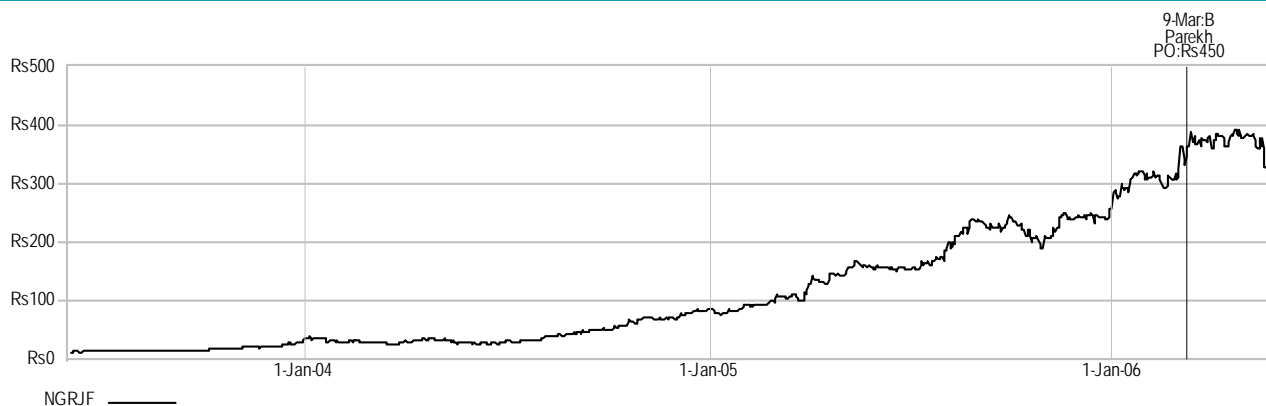
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Important Disclosures

NGRJF Price Chart



B : Buy, N : Neutral, S : Sell, PO : Price objective, NA : No longer valid

The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark Grey shading indicates the security is restricted with the opinion suspended. Light Grey shading indicates the security is under review with the opinion withdrawn. Chart current as of May 31, 2006 or such later date as indicated.

Investment Rating Distribution: Engineering & Construction Group (as of 31 Mar 2006)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	11	64.71%	Buy	4	36.36%
Neutral	6	35.29%	Neutral	1	16.67%
Sell	0	0.00%	Sell	0	0.00%

Investment Rating Distribution: Global Group (as of 31 Mar 2006)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1145	40.29%	Buy	393	34.32%
Neutral	1474	51.86%	Neutral	430	29.17%
Sell	223	7.85%	Sell	44	19.73%

* Companies in respect of which MLPF&S or an affiliate has received compensation for investment banking services within the past 12 months.

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