

Sunil Hitech Engineers Ltd.

CMP: Rs. 205 P/E 10.3x FY08E

PRICE TARGET Rs 325 (12 Months)

Index Details

Sensex	14,868
Nifty	4,403
BSE SMLCAP	7,904

 Industry **POWER**

Scrip Details

Mkt Cap (Rs in Cr)	205.5
Book Value (Rs)	56.9
Eq Shares O/s (Cr)	1.0
Avg Vol	111,868
52 Week H/L	223 / 67
Dividend Yield (%)	0.6
Face Value (Rs)	10.0

BSE Code	532711
NSE Code	SUNILHITEC

Shareholding Pattern (30th June '07)

Shareholders	% holding
Promoters	65.1
Indian Institutions	0.0
FII's	1.4
Non Promoter Corporate	8.9
Public	24.6
Total	100

Sunil Hitech Engineers Ltd. Vs Sensex



Sunil Hitech Engineers Ltd. (SHEL) specializes in the niche segment of fabrication, erection and testing and commissioning of bunkers, electrostatic precipitator, boilers, and turbine generator sets in power plants. It is amongst the very few EPC companies that are focused in the ever-growing power sector for the last two decades.

Key Investment Highlights

Strong Industry Outlook

Power has gained greater importance in the last three years after a decade of lacklustre growth. The primary reason for this shift is due to increasing gap between power demand and supply and the Government impetus to achieve the ambitious target of providing "Power for All" by 2012. The increasing number of power projects scheduled to come on stream should augur well for the company going forward.

Expanding Presence...

SHEL has recently diversified its portfolio of services by venturing into the hydropower plants, setting up of transmission substations, steel structure erection and manufacturing of pressure parts. These services would further give a fillip to the company's growth.

Strong Order Book Position

SHEL has accumulated a sizeable order book over the few years. The company's present unexecuted order book stands at Rs 800 crore to be executed over approximately 3 year period. Further the company has bid for 7-8 contracts worth Rs 400 crore from which the orders are awaited.

Valuations

With the current boom in the power sector coupled with increasing government thrust on Power Infrastructure we expect SHEL's Revenues and PAT to grow at a CAGR of 55% and 115% respectively by FY09. At the CMP of Rs 205 the stock is trading at 10.3x its FY08e earnings of Rs 20 and at 6.2x its FY08e EV/EBIDTA. Considering the positive industry outlook, a robust order book coupled with SHEL expanding presence across various segments, **we recommend a BUY on the scrip with a price target of Rs 325, an upside of ~60% over a period of 12 months.**

Key Financials:

Y/E March, 2007 (Rs in Cr)	FY06	FY07	FY08E	FY09E
Net Revenues	132.7	144.8	235.0	350.0
EBIDTA	12.7	17.8	40.0	63.0
PAT	5.2	7.4	20.0	33.1
EPS (Rs)	5.2	7.4	20.0	*24.0
EPS Growth (%)	136.4	41.3	171.4	20.0
ROCE	22.4	17.8	27.8	28.0
RONW	16.6	13.7	28.8	25.7
P/E (x)	39.4	27.7	10.3	8.5
EV/EBIDTA (x)	15.7	13.2	6.2	5.1

*Note: Dilution of equity on account of warrants

□ Company Background

SHEL specializes in the niche segment of fabrication, erection and testing of power plant infrastructure

Sunil Hitech Engineers Ltd. specializes in the niche segment of fabrication, erection and testing and commissioning of bunkers, electrostatic precipitators, boilers, turbine generator sets in power plants. SHEL is also engaged in overhauling and maintenance post-installation. It is amongst the very few EPC companies that are focused in the ever-growing power sector for the last two decades. The company has recently forayed into setting up of transmission substation thereby emerging as a complete turnkey player, right from providing services for setting up a power station to its distribution infrastructure.

□ Business Overview

Power Projects

Under this segment SHEL undertakes turnkey projects having capacities ranging from 30MW to 500MW and has a clientele comprising both public & private sector power companies. Further, the company is eyeing captive projects between 5 MW to 60 MW, as the demand for captive power is set to grow by 1500 - 2000 MW annually due to capacity additions in cement, food processing, chemical industry and others.

With its foray into setting up of transmission substations, SHEL will emerge as a complete turnkey player from power generation to distribution

Transmission and Distribution

SHEL has recently forayed into setting up of transmission substations in the power distribution segment. Its services include design, supply, testing & commissioning of electric sub-stations and lines, with capacity ranging from 66 kv – 132kv - 220 kv etc.

With this venture, SHEL has emerged as a complete turnkey player, right from providing services for setting up a power station to its distribution.

□ Expanding Presence...

SHEL also offers products and services to Process & Piping Industries, Sugar Industries, Irrigation Projects, Raw Water Systems and structural steel works in steel plants. SHEL is also catering to steel and aluminium industry in areas of boilers, steel structures and other captive energy sources.

Steel Projects

SHEL has recently diversified its portfolio of services by venturing into the steel sector. The company is engaged in setting up and construction of super steel structures for this sector. Presently, it is doing structural works for setting up a sinter plants for Jindal Steel and Rashtriya Ispat Nigam Ltd.

SHEL has recently diversified its portfolio of services by venturing into the steel structure erection and hydropower plants

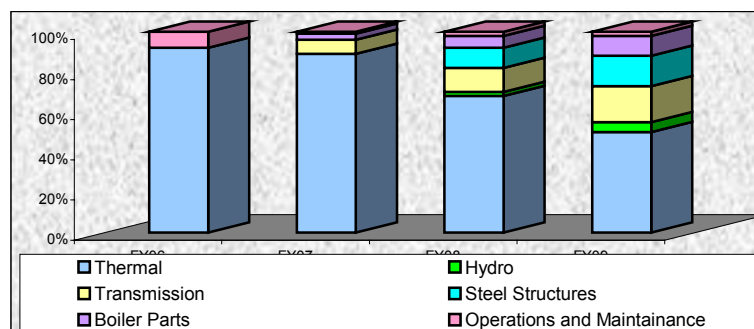
Hydro Power Plants

Though earlier the company had a presence only in thermal power plant segment, SHEL has also forayed into hydropower plants since March '07. Recently, SHEL has received an order from Dodson-Lindblom, USA (through its Indian subsidiary) for a hydropower project in Himachal Pradesh. The value of the order, which is slated to be completed by March '08, is estimated at Rs 45 crore.

□ Revenue Mix

The following chart depicts the SHEL's revenue stream through FY06 to FY09.

We expect contributions from Pressure Parts, Transmission Projects and Steel Structures to increase gradually through FY08 to FY09



SHEL's revenue comprises of five major components viz. Thermal Power Projects, Hydro Power Projects, Transmission Projects, Pressure Parts, Steel Structures and Operations and Maintenance (O&M). Though Thermal Power projects would continue to dominate the revenues through FY06 to FY09, we expect contributions from Pressure Parts, Transmission Projects and Steel Structures to increase gradually through FY09.

□ Backward Integration into Boiler Parts

As a backward integration of its core business of overhauling and maintenance of boiler, SHEL has commenced production of various pressure parts used by Power plants, Petrochemicals sector, Sugar Industry and Heavy Engineering Industry

In Nov'06 SHEL, through its subsidiary entered into the business of manufacturing of pressure parts used by Power plants, Petrochemicals sector, Sugar Industry and Heavy Engineering Industry. As a backward integration of its core business of overhauling and maintenance of boilers, SHEL has initiated production of various parts like Economizer coil, Reheater Coils, Raiser Tubes, J Bends, Super heater coil, header etc. The total project cost was approximately Rs 10 crore.

The plant has manufacturing and fabrication capacity of about Rs 100 crore in terms of revenues. SHEL consumes around Rs 15-17 crore of pressure parts in a year for overhauling & maintenance. Further, SHEL is also planning to increase its capacity to meet the growing demand. The current order book in this segment stands at Rs 25 crore, executable over a period of 12 months.

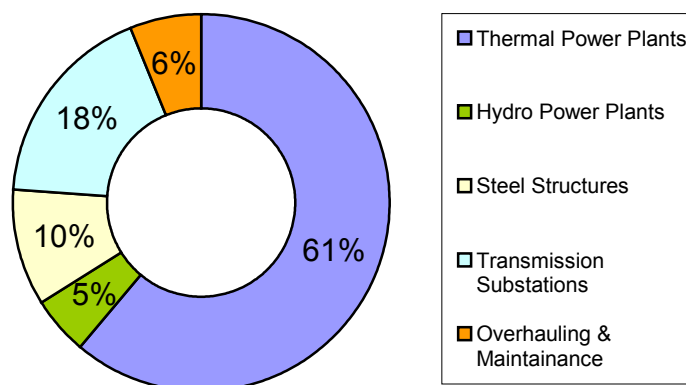
Apart from captive consumption of these parts SHEL also supplies to boiler manufacturers like Thermax and ISGEC John Thompson. There is a strong replacement demand from old power plants, which in turn will generate demand for the spare parts. SHEL will reap the benefits of backward integration through its subsidiary on account of cost effective inputs and reduction in lead-time.

Strong Order Book Position

SHEL has accumulated a sizeable order book over the few years. The company's present unexecuted order book stands at Rs 800 crore having an execution period of approximately 3 years.

SHEL has accumulated a sizeable order book of Rs 800 crore, which is 5.5x, its FY07 sales, having an execution period of approximately 3 years

Order Book Position



Thermal Power Plants

SHEL has the capabilities to cater both big and small power stations, ranging from 5 MW to 660 MW. With more capacities coming up in both the segments we expect SHEL to bag more orders under this segment. Presently the company is catering more to big power plants i.e. in the range of 250MW to 660MW. Recently, the company received an order of Rs 35 crore from NTPC for a 660MW Power Plant of which 50% has already been executed till date.

Some of the Major Thermal Power Projects Include			
Company Name	Nature of Contract	Contract Value	Tenure
MAHAGENCO	Supply, Fabrication & Erection of Structural Steel for the plant	152.45	2 years
Reliance Energy Ltd.	Structural Fabrication and Erection	37.00	1.5 Years

Hydro Power Projects

SHEL has also forayed into the Hydro Power Project space, bagging a Rs 45 crore contract from US-based Dodson Lindblom Hydro Power Private Limited. The contract has been awarded for providing consultancy services and does not include the cost of material. The value of the order, which is slated to be completed by March '08, is estimated at Rs 45 crore.

Transmission Projects

Some of the Major Transmission Projects Include			
Company Name	Nature of Contract	Contract Value	Tenure
MAHADISCOM	Design, testing, supply, transport, construction, erection, testing and commissioning of Substation	24.75	1 year
MAHADISCOM	Strengthening and renovation work of existing lines, erection of new lines & laying of underground cable	17.71	1 year

The tenure of execution for both projects will be 12 months from the date of work order. Both the projects have commenced by the end of October 2006.

Steel Structures

While SHEL has traditionally worked on power infrastructure projects, it is also making a foray into infrastructure development for the steel industry with some of the new contracts.

Some of the Major Steel Structure Projects Include			
Company Name	Nature of Contract	Contract Value	Tenure
RINL	Structural steel works	25.32	2 years
Punj Lloyd Ltd.	Structural steel works	16.34	1 Year
JSW Steel	Sinter Plant	12.95	1 Year
Tata Projects	Fabrication and erection of structural steel for its plant	5.35	6 Months

Overhauling & Maintenance

Apart from setting up of completely new power plants SHEL also has orders where it has to do the maintenance of old power plants. As almost 50% of the power plants in India are old, there is a huge demand from the maintenance side.

□ Sound Client Profile

SHEL's customer list includes the likes of NTPC, BHEL, JSW Steel, Sterlite, Jindal Steel & Power, Reliance Energy, L&T and major State Electricity Boards such as Maharashtra State Power Generation Company, Rajasthan Viduyt Utpadan Nigam, Madhya Pradesh State Electricity Board, Chattisgarh State Electricity Board, Tamil Nadu State Electricity Board, Ahmedabad Electricity Co Ltd etc.

It has also forged relationships with new players like Punj Lloyd and entered in JV with foreign EPC (Engineering, Procurement & Construction) contractors like SEPCO for undertaking power plant construction work.

SHEL's client mix includes 50% of SEBs, 30% Private Players and the remaining 20% from the Central Government. The top 5 customers of the company include Jindal Steel, MSEB, RINL, BHEL and NTPC.

SHEL's customer list includes NTPC, BHEL, JSW Steel, Sterlite, Jindal Steel, Reliance Energy, L&T and many State Electricity Boards

□ Industry Outlook

Power has gained greater importance in the last three years after a decade of lacklustre growth. The primary reason for this shift is an increase in the gap between power demand and supply, which is about 11% in 2006 as compared to 7% in 2005. The Government has set an ambitious target of providing “Power for All” during the X and XI Plan, which would require an additional capacity creation of nearly 100,000 MW by 2012 to achieve this goal. Further in the 2007-2008 Budget the government has continued with the policy of boosting the power sector with the announcement of 2 more Ultra Mega Power Projects (UMPP) and five other power projects. Thus the industry outlook remains fairly robust.

Thermal Power Projects

Currently, thermal power projects accounts for 65% of the total generating capacity. The XIth plan alone targets addition of around 78,577 MW of which 58,644 MW is expected to be contributed through thermal power projects.

Around 60% of SHEL’s revenues are contributed through projects undertaken under this space. SHEL being one of the leading EPC providers in this space is likely to be one of the biggest beneficiaries.

Hydro Power Projects

Hydroelectricity is clean energy and its generation is not linked to issues concerning fuel supply, especially the price volatility of imported fuels. Its share as compared to thermal power projects has gradually declined. Only about 17% of vast hydel potential of 150,000 MW has been tapped so far whereas countries like Norway, Canada, Brazil have all been utilizing more than 30% of their hydro potential. This opens up a vast room for investments in the hydro power projects in India over the coming years.

SHEL, which has recently forayed into the Hydro Power Project space by bagging Rs 45 crore contract from US-based Dodson Lindblom Hydro Power Private Limited for undertaking structural fabrication & erection works, is all set to explore the increasing opportunities arising under this space.

T&D projects

Presently per capita power consumption in India is at 606 kwh/year as against 1,212 kwh/yr for China and World average at 2,326 kwh/yr. Only 66% of India’s current generated capacity is being used due to inefficient Transmission and Distribution (T&D), hence there is a crying need for heavy investments in T&D by way of technological upgradation and optimization of transmission costs along with development of National Grid. This in turn will result in increasing demand for setting up of transmission substations.

SHEL has already forayed into setting up of transmission substations in the power distribution segment just before the IPO. For this purpose SHEL has invested Rs 70 crore for expansion of its facility in Nagpur. With this venture, SHEL has emerged as a complete turnkey player, right from providing services for setting up a power station to its distribution.

Structural Steel works

SHEL has already forayed into the structural steel sector by bagging two prestigious order in the last fiscal from RINL (Rashtriya Ispat Nigam Ltd) & Jindal Steel for various works like fabrication & erection of technological structures for the sinter plant. With the domestic steel players likely to be on an expansion mode over the next five years, SHEL expects fresh order inflows coming from this segment.

□ Strategically Positioned to Capture the Power Sector Boom

Few players engaged in the fabrication and erection works of the power plants

Newly bought machinery to result in significant savings to the tune of Rs 1.5 crore

Strong employee base of 900 employees

Gearing up to qualify for UMPP participation by acquiring machinery, certification and manpower

Plans to foray into niche areas like GIS technology for substations

- There are few players in the power industry who are engaged in the fabrication and erection works of the power plants. Of these, L&T and BHEL though present in this segment, only a small division is dedicated to this area. Other players include Petron Engineering, Simplex Infrastructure, Era Construction etc.
- SHEL has added civil machinery for its thermal and hydropower projects. These machines were earlier hired and SHEL had to pay high lease rentals for it. This will result in significant savings to the tune of Rs 1.5 crore in FY08E and will in turn boost margins.
- SHEL currently has a strong employee base of 900 employees generating Rs 0.16 crore per employee. With the company diversifying into newer segments it plans to increase the employee base to 1,100 employees by FY09. The business per employee is expected to increase to Rs 0.25 crore in FY09.
- The company is gearing itself to qualify for participation in UMPPs by acquiring the required machinery, certification and manpower. Recently SHEL has acquired heavy crawler cranes from Australia with a capacity of 300 MT for carrying out execution of UMPP. The company is also undergoing certification for 18001 OHSAS (Occupational Health & Safety) from DNV (Det Norske Veritas), Netherlands that will give a further boost for UMPP participation.
- Since SHEL already has a presence in the substation segment, it also plans to foray into Gas Insulated Substation (GIS) technologies. It has already identified suppliers in Japan for sourcing this technology. These substations are noiseless, smaller in size, nonflammable, have effective protection against atmospheric pollution and reduced maintenance costs as compared to conventional high-voltage substations. They are also effective in reducing the T&D losses significantly. Though NTPC and a few state electricity boards are using this technology, in India there are no manufacturers for Gas Insulated Substations.

□ Improving financial performance

SHEL posted impressive results for Q108, with a 51% and 133% jump in Revenue and PAT respectively

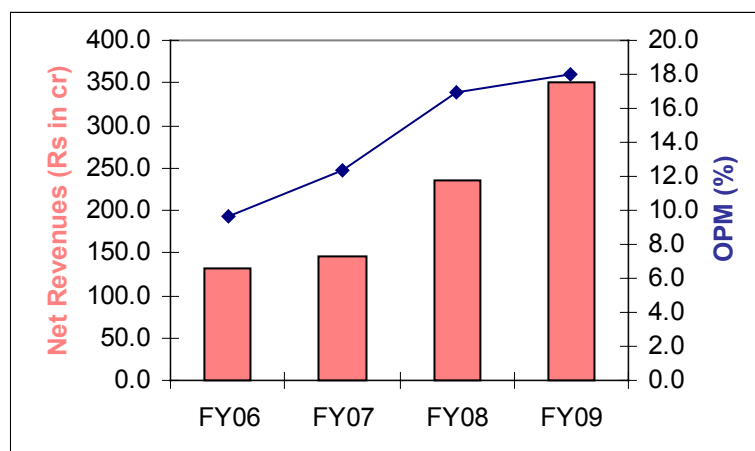
The company's net revenues for Q1FY08 jumped by 51% to Rs 45.4 crore from Rs 30.0 crore in Q1FY07. Its PAT for the quarter went up by 133% to Rs 3.4 crore from Rs 1.5 crore. EPS for the quarter was also up 133% at Rs 3.4 as against Rs 1.5 in Q1FY07. The operating margins were up 730 bps at 16.8% as against 9.5% in Q1FY07.

For FY07, net revenues were up 9% at Rs 144.8 crore. The company showed a growth of 41% in PAT, to Rs 7.4 crore from Rs 5.2 crore in FY06. The EPS jumped to Rs 7.4 for FY07 from Rs 5.2 in FY06. For FY07, the operating margins were up 270 bps from 9.6% to 12.3% while the net margins also showed an improvement of 120 bps from 3.9% to 5.1%.

□ Financial Outlook

We expect the company's net revenues to touch Rs 350 crore in FY09, which represents a CAGR of 55% and the net profit to touch Rs 33.1 crore at a CAGR of 115% over the next two years. Consequently, we expect the margins to improve from 9.6% in FY06 to 18% in FY09.

We expect SHEL to grow at a CAGR of 55% in revenues & 115% in PAT over the next two years



We expect the order inflow to remain robust for the next few years considering the positive industry outlook. Further the transmission & pressure parts segment which are currently in the nascent stage should drive the growth going forward.

□ Equity Dilution

The company is planning to issue 38 lakh warrants to promoters & non promoters at a price to be determined in accordance with the SEBI regulations aggregating approximately Rs 70 crore. Of the above warrants, promoters would be allotted 15 lakh warrants.

With the above issuance of equity expected in the near term, the total equity would increase from Rs 10.0 crore in FY07 to Rs 13.8 crore in FY09 which will dilute promoter's stake from the current 65% to 64%.

□ Key Concerns

- **Delay in execution**
Any delay in the project execution from either party may have a negative impact on the financials of the company.
- **Increasing Employee cost**
Being a labour intensive company involving both skilled employees (like engineers) and unskilled labours, SHEL is always exposed to the risk of increasing cost and availability of employees.

□ Peer Review

Parameters	SHEL	Simplex Infra	Petron Engg
Net Revenues – TTM	160.2	1926.9	244.5
Net Profit – TTM	9.6	61.8	9.6
OPM (%)	14.1	9.6	10.4
NPM (%)	6.0	3.2	3.9
CMP (10/08/07)	205.0	372.0	188.0
Market Capitalization	205.5	1592.2	141.8
Market Capitalization / Sales	1.3	0.8	0.6
Debt to Equity (x)	0.8	1.9	0.5
Debtors T/o (no of days)	98	128	81
EPS – TTM	9.6	14.4	12.7
PE – TTM	21.5	25.8	14.8
ROE (%)	16.6	17.6	16.1
ROCE (%)	22.4	24.5	22.7

SHEL has a clear upper edge over its peers considering that it enjoys better margins which would further be increased in the coming years considering its presence in the higher margin pressure parts segment

Though L&T and BHEL are present in erection & fabrication works segment, we have ignored them in the list of peers as only a small division is dedicated to this area. **We feel that SHEL has a clear upper edge over its peers considering that it enjoys better margins which would further be increased in the coming years as the company is likely to increase its presence in the pressure parts segment where the margins are on the higher side as compare to turnkey projects.**

□ Valuation & Recommendation

With the current boom in the power sector coupled with increasing government thrust on Power Infrastructure we expect SHEL's Revenues and PAT to grow at a CAGR of 55% and 115% respectively by FY09.

At the CMP of Rs 205 the stock is trading at 10.3x its FY08e earnings of Rs 20 and at 6.2x its FY08e EV/EBIDTA. Considering the positive industry outlook, a robust order book coupled with SHEL's expanding presence across various segments we recommend a BUY on the scrip with a price target of Rs 325 over a period of 12 months, an upside of about ~60% from the current levels.

Exhibit 01: Financials and Projections

Profit & Loss Statement				Key Ratios			
Y/E March, Fig in Rs. Cr	FY2007	FY2008e	FY2009e	Y/E March, Fig in Rs. Cr	FY2007	FY2008e	FY2009e
Net Sales	144.8	235.0	350.0	Per Share Data (Rs)			
% Chg	9.1	62.3	48.9	EPS	7.4	20.0	24.0
Total Expenditure	127.0	195.0	287.0	Cash EPS	11.7	27.0	30.5
% Chg	5.8	53.5	47.2	DPS	1.2	2.0	3.0
EBDITA	17.8	40.0	63.0	Book Value	56.9	81.8	126.8
EBDITA Margin %	16.8	17.0	18.0	Capital, Liquidity, Returns Ratio			
Other Income	1.6	2.0	3.5	Debt / Equity (x)	0.8	0.8	0.5
PBDIT	19.4	42.0	66.5	Current Ratio (x)	2.3	2.1	2.2
Depreciation	4.4	7.0	9.0	ROE (%)	13.7	28.8	25.7
Interest	3.3	5.0	8.0	ROCE (%)	17.8	27.8	28.0
PBT	11.5	30.0	49.5	Dividend Yield (%)	0.6	0.9	1.4
Tax Provisions	4.1	10.0	16.4	Valuation Ratio (x)			
Reported PAT	7.4	20.0	33.1	P/E	27.7	10.3	8.5
PAT Margin (%)	5.1	8.5	9.5	P/BV	3.6	2.5	1.6
				EV/ Sales	1.6	1.1	0.9
Raw Materials / Sales (%)	35.4	48.9	48.6	EV / EBDITA	13.2	6.2	5.1
Other Mfr. Exp / Sales (%)	47.5	27.9	27.1	Efficiency Ratio (x)			
Employee Exp / Sales (%)	4.8	6.2	6.3	Inventory (days)	63	50	54
Tax Rate (%)	36.0	33.3	33.1	Debtors (days)	98	93	89
				Creditors (days)	221	163	177

Balance Sheet				Cash Flow Statement			
Y/E March, Fig in Rs. Cr	FY2007	FY2008e	FY2009e	Y/E March, Fig in Rs. Cr	FY2007	FY2008e	FY2009e
Equity Capital	10.0	10.0	13.8	Profit After Tax	7.4	20.0	33.1
Reserves & Surplus	47.0	64.8	161.5	Depreciation & W/o	4.4	7.0	9.0
Warrants	0.0	7.2	0.0	Working Capital Changes	-22.8	-15.2	-28.8
Total Loans	44.4	68.0	85.0	Others	-0.1	0.0	-0.4
Deferred Tax Liability	0.2	0.1	0.0				
Total Liabilities	101.6	150.1	260.4	Operating Cash Flow	-11.1	11.8	12.9
				Capital Expenditure	-23.5	-29.4	-48.0
Gross Block	52.0	70.0	110.0	Change in Investment	1.3	-1.1	-20.0
Less: Acc. Depreciation	14.1	21.1	29.1	Cash Flow from Investing	-22.2	-30.5	-68.0
Net Block	37.9	48.9	80.9	Proceeds from equity issue	0.0	7.2	65.0
Capital Work in Progress	0.5	12.0	20.0	Inc/(Dec) in Debt	30.6	23.6	17.0
Investments	3.9	5.0	25.0	Dividend Paid	-1.4	-2.3	-4.7
Net Current Assets	58.5	83.5	134.5	Cash Flow from Financing	29.2	28.6	77.3
Misc. Expd not w/o	0.8	0.7	0.0				
Total Assets	101.6	150.1	260.4	Net Change in Cash	-4.1	9.8	22.2
				Opening Cash Balance	19.4	15.2	25.0
				Closing Cash Balance	15.2	25.0	47.2

Ventura Securities Limited

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