Emkay Research

Punj Lloyd

Update

Overhang Blues

3rd June 2008

BUY

Price	Target Price
Rs287	Rs414

Sensex –	**16,063**

The Q4FY2008 consolidated performance was overshadowed by the auditor's qualification. Company reported strong performance in Q4FY2008 registering (1) revenue growth of 38% yoy to Rs23.5 bn (2) 60 bps expansion in EBIDTA margins and (3) net profit growth of 35% yoy to Rs1.2 bn- in line with estimates. But, the auditor's qualification has sprung as negative surprise taking the sheen off Q4FY2008 performance. Considering the auditor's qualification and concerns on quality of order backlog, we have fine tuned our EBIDTA margin assumptions for FY2009E and FY2010E. Consequently, we have cut our net profit estimates by 8% and 10% to Rs4.9 bn and Rs6.0 bn for FY2009E and FY2010E respectively. We believe that, concerns on the quality of order backlog and likelihood of further provisioning and write-offs will remain overhang on the valuations. Consequently, we have cut our target multiples and valued the core EPC business at 20X FY2010E earnings. We have valued the core EPC business at Rs374/Share and New Business is valued at Rs40/Share. We maintain BUY rating with 18-month price target of Rs414, an upside of 44%.

Auditor's qualification has marred strong performance

Company has sprung yet another negative surprise in the Q4FY08 results- in form of Auditors Qualification. *'The auditors have qualified in their audit report for 31st March 2008 in respect of losses on a long term contract currently in progress, a project in UK undertaken by Simon Carves Ltd, a wholly owned subsidiary amounting to Rs3.0 bn'.* In response to above qualification- management has clarified that Rs0.7 bn is recoverable in said contract and negotiations for balance amount is currently under progress. Further, the company is of the view that cost increases is owing to changes in design and scope of work. Company is hopeful to break even in the above project and recover the said cost overruns from the clients.

We believe that, above events normally happens in EPC business- but the magnitude is quite alarming and disturbing (almost equivalent to FY08 consolidated net profit). Further, the cost overrun is associated with a legacy order under execution for last 24 months- which was not qualified earlier. Company has indicated that prudent measures have been taken w.r.t. above project and outstanding backlog- but one cannot rule out further occurrence of negative surprises in respect of above.

Price Performance

(%)	1M	3M	6M	12M
Absolute	(24)	(24)	(46)	30
Rel. to Sensex	(16)	(17)	(34)	18

Source: Bloomberg

Stock Details

Sector	Cap Goods
Reuters	PUJL.BO
Bloomberg	PUNJ@IN
Equity Capital (Rs mn)	607
Face Value (Rs)	2
52 Week H/L (Rs)	303
Market Cap (Rs bn)	589/214
Daily Avg Vol (No of shares)	87/2,054
Daily Avg Turnover (US$ mn)	2766768

Shareholding Pattern (%)

(31st March.'08)

Promoters	44.7
FII/NRI	25.5
Institutions	13.5
Private Corp.	6.0
Public	10.4

YE-Mar	Gross Sales	EBITDA (Core)	(%)	APAT	AEPS (Rs)	EV/ EBITDA	P/BV	Div Yld (%)	RoE (%)	P/E
FY2007	51,266	3,885	7.6	1,970	7.4	18.0	5.8	1.0	16.1	38.4
FY2008	77,529	7,086	9.1	3,584	11.1	12.0	2.8	1.5	15.7	25.8
FY2009E	105,720	9,715	9.2	4,910	15.2	9.3	2.5	1.5	14.1	18.7
FY2010E	133,282	12,234	9.2	6,051	18.7	7.4	2.1	1.5	15.0	15.2

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Punj Lloyd reported revenues of Rs23.5 bn in Q4FY2008- in line with estimates

Punj Lloyd reported a 38% yoy growth in revenues to Rs23.5 bn, in line with our estimates. We attribute strong performance to all round growth in key business verticals and strong growth in local and international business operations.

EBIDTA margins expanded by 60 bps and EBIDTA grew by 46% yoy- in line with estimates

EBIDTA grew by 46% yoy to Rs2.4 bn- in line with estimates. The current quarter results were not marred by write-offs or provisioning for ongoing projects- especially Sembawang legacy orders as visible in sequential quarter. The EBIDTA growth at 46% yoy was higher than the revenue growth – triggering a 60 bps expansion in EBIDTA margins from 10.0% in Q4FY2007 to 10.6% in Q4FY2008.

Net profit grew by 35% yoy during Q4FY2008, in line with estimates

The net profit stood at Rs1.2 bn in Q4FY2008, in line with estimates. We attribute this to (1) robust order booking and (2) strong EBIDTA margins. Despite a reversal of exchange gains of Rs218 mn of previous quarter (in accordance with AS-11), net profit growth was strong at 35% yoy. Adjusting for reversal of exchange gains - the growth would be much stronger and higher. The net profit margins are stable at 5.1% in the ongoing quarter. The earnings in the quarter stood at Rs3.9 versus Rs3.4 in same quarter last year.

FY2008 consolidated results were in line with estimates- net profit grew by 82% yoy to Rs3.6 bn

For FY2008- Punj Lloyd reported revenues of Rs77.5 bn and revenue growth of 51% yoy- in line with estimates. We attribute strong revenue growth to robust order booking. The EBIDTA growth at 89% yoy to Rs7.1 bn - in line with estimates. We have considered the Rs0.7 bn provisions in above calculations. The EBIDTA margins stood at 9.1% against 7.3%- 180 bps expansions and in line with estimates. The net profit stood at Rs3.6 bn an 82% yoy growth- in line with estimates.

Order backlog at Rs196 bn- signifies 2.5X FY2008 revenues

The consolidated order book stood at Rs196 bn in Q4FY2008 against Rs160 bn in Q3FY2008, growth of 22% qoq. We attribute rise in order backlog to sustained inflow of orders of Rs10.1 bn, Rs18.9 bn, Rs40.2 bn and Rs38.5 in Q1FY2008, Q2FY2008, Q3FY2008 and Q4FY2008 respectively. We believe that, Punj Lloyd has strong visibility in earnings at 2.5X FY2008 consolidated revenues. Sembawang contributes around Rs68 bn or 35% of current order backlog. The infrastructure vertical which is most susceptible to volatility in raw material prices contributes 35% of order backlog. The legacy orders are pegged at measly Rs7 bn- executable in next 9 months. Company has indicated that 90% of order backlog has price variation clause and 10% of order backlog is susceptible to volatile raw material prices.

We have fine tuned our EBIDTA margin assumptions- in lieu of possible cost overruns

Considering the auditor's qualification and concerns on quality of order backlog, we have fine tuned our EBIDTA margin assumptions for FY2009E and FY2010E. Instead of EBIDTA margin expansion of 70 bps in FY2008-10E period, we have considered stable margins in FY2008-10E period due to escalating raw material price scenario and probable provisioning on ongoing projects due to cost overruns. Our EBIDTA margin assumptions are fine tuned from 9.8% and 9.9% in FY2009E and FY2010E respectively to 9.2% for ensuing years. Consequently, the net profit is revised downwards from Rs5.3 bn to Rs 4.9 bn and Rs6.7 bn to Rs6.0 bn in FY2009E and FY2010E respectively. We have cut our net profit estimates by 8% and 10% for FY2009E and FY2010E respectively. We continue to maintain our revenue estimates at Rs105.2 bn and Rs133.2 bn for FY2009E and FY2010E respectively considering strong order book and robust business environment.

We maintain BUY rating, with revised price target of Rs414

We are very bullish on growth prospects of the company especially after the Singapore acquisition which adds strong product offering and expands addressable market. We believe that, PLL will reap handsome gains of the ensuing opportunity in energy and infrastructure segment the two strong pillars for growth by leveraging on its experience and skill sets.

However, concerns on the quality of order backlog and likelihood of further provisioning and write-offs will remain overhang on the valuations. Consequently, we have cut our target multiples and valued the core EPC business at 20X FY2010E earnings. We have valued the core EPC business at Rs374/Share and New Business is valued at Rs40/Share i.e. Ship Building Rs11/Share, Real Estate Rs17/Share and Medicity Rs12/Share. We maintain BUY rating with 18-month price target of Rs414, an upside of 44%.

Quarterly Results

In Rs Mn	Q4FY2008	Q4FY2007	yoy %	Q3FY2008	qoq %
Net Sales	23467.0	17035.5	37.8	21170.4	10.8
Expenditure	20981.1	15329.0	36.9	19446.3	7.9
Material Cost	7478.3	2989.3	150.2	7614.1	-1.8
% of Sales	36%	18%	-	36%	-
Contractor Charges	5966.0	5901.3	1.1	6746.9	-11.6
% of Sales	32%	35%	-	32%	-
Employee Expenses	2888.5	2018.7	43.1	2392.1	20.8
% of Sales	11%	12%	-	11%	-
Other Expenses	4648.3	4419.7	5.2	2693.2	72.6
% of Sales	13%	26%	-	13%	-
Operating Profit	2485.9	1706.5	45.7	1724.1	44.2
EBIDTA (%)	11%	10%	-	8%	-
Other Income	-183	163.6	-211.9	458.9	-139.9
Interest	325.5	257.8	26.3	284.3	14.5
Depreciation	409.1	329.2	24.3	365.2	12.0
PBT	1568.3	1283.1	22.2	1533.5	2.3
Tax	374.3	398.2	-6.0	308.3	21.4
PAT	1194.0	884.9	34.9	1225.2	-2.5
PAT (%)	5%	5%	-	6%	-
Extraordinary	0	0	-	-308.4	--
PAT (After Extraordinary)	1177.4	889.3	32.4	917.2	28.4
EPS	3.9	3.4	16.2	4.2	-6.6

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