
Initiating Coverage: VA Tech Wabag

October 2010

Initiating Coverage

Issue Price

Rs. 1,310

Target

Rs. 1,954

Genuinely Potable Idea

VA Tech Wabag (VTW), an India based MNC player in the water treatment industry, has market presence in India, the Middle East, North Africa, Central and Eastern Europe, China and South East Asia. We believe, VTW is an attractive play on the water infrastructure spend in India and other emerging markets. Given the low per-capita availability of water in these markets, there have been massive investments planned in these regions catalysed by funding agencies like World Bank etc.. We believe VTW is rightly poised with Wabag's strong brand, advanced technology and excellent track record along with its local presence in growing markets to tap this opportunity. Initiate coverage with **Buy**.

Investment rationale

- Unique speciality EPC play vis-à-vis ubiquitous civil EPC
- Special focus on emerging markets
- Strong backlog of Rs. 28bn, robust order pipeline and resilient demand in emerging markets to drive doubling of revenues over FY10-13E
- Margin profile on improving trend owing to rising O&M revenues and cost rationalisation – EBITDA margins improved from 3% in FY08 to 9% in FY10. We expect it to further improve by 100bps over FY10-12E
- Strong and well incentivized leadership team

Attractively priced for long term growth

At an issue price of Rs. 1310, VTW is available at a valuation of 11x FY12E earnings (ex-cash), which seems very attractive given its robust growth prospects and high core RoCEs. We have valued VTW's operations at 18x FY12E earnings (ex-cash) and 1x cash (post money) to arrive at **target price of Rs. 1,954** implying an upside of 49%. We believe VTW is a compelling growth story (revenues and earnings CAGR of 24% and 45% respectively over FY10-13E) with no comparable peers in the listed space. **Recommend buy up till Rs. 1,800.**

Key risks

Execution delays could lead to liquidated damages; VTW derives around 65% of its annual sales in H2 – this seasonality could fail q-o-q test by market; Probable liability of disallowed tax benefits under sec 80-IA retrospectively worth Rs. 340mn; margin pressure in case of sharp rise in competition; order book concentration risk

Financial summary (Consolidated)

Year	Revenues (Rs. mn)	EBITDA (Rs. mn)	Adj PAT (Rs. mn)	EPS (Rs.)	P/E(x)	EV/EBITDA(x)
FY10	12,237	1,113	478	50.7	25.8	9.4
FY11E	14,754	1,313	704	67.1	19.5	8.5
FY12E	18,029	1,821	1,075	102.4	12.8	5.8

Date	Oct 8, 2010
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Issue details

Issue close date	Oct 8, 2010
Fresh issue (sh. mn)	0.95
Offer for sale (sh. mn)	2.65
Offer size	Rs. 4.73bn
Issue Price	Rs. 1,310
Face value	Rs. 5
Market Cap	Rs. 13.7bn

Objects of fresh issue

Working capital funding	Rs. 645mn
Capex - corporate office	Rs. 347mn
Global IT system	Rs. 111mn
Others	Rs. 87mn

Shareholding (%)

	Pre-issue	Post-issue
Promoters	34%	31%
Institutions	59%	46%
Others	7%	23%

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Company Overview

Issue Price

Rs. 1,310

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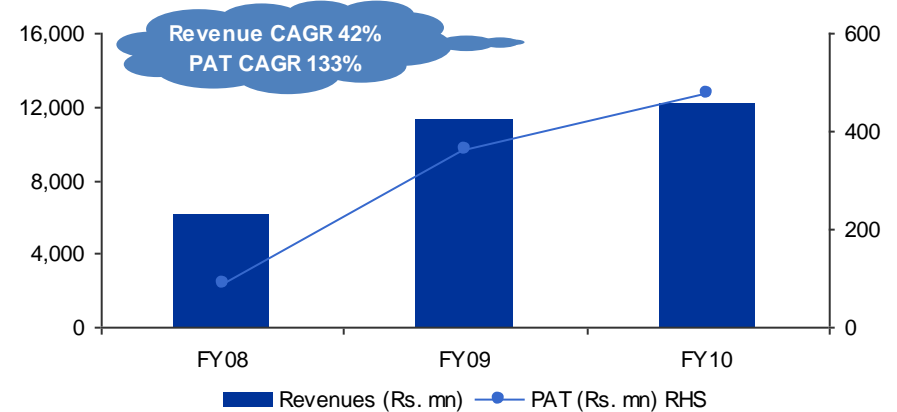
Rs. 1,954

Company background

VTW, a India based multinational player in water treatment industry is head quartered in Chennai, India. It provides a range of EPC and O&M solutions for sewage treatment, processed and drinking water treatment, effluents treatment, sludge treatment, desalination and reuse for institutional clients like municipal corporations and companies in the infrastructure sector such as power, steel and oil and gas. As on July 31, 2010, it has executed 113 projects and is currently executing 81 projects

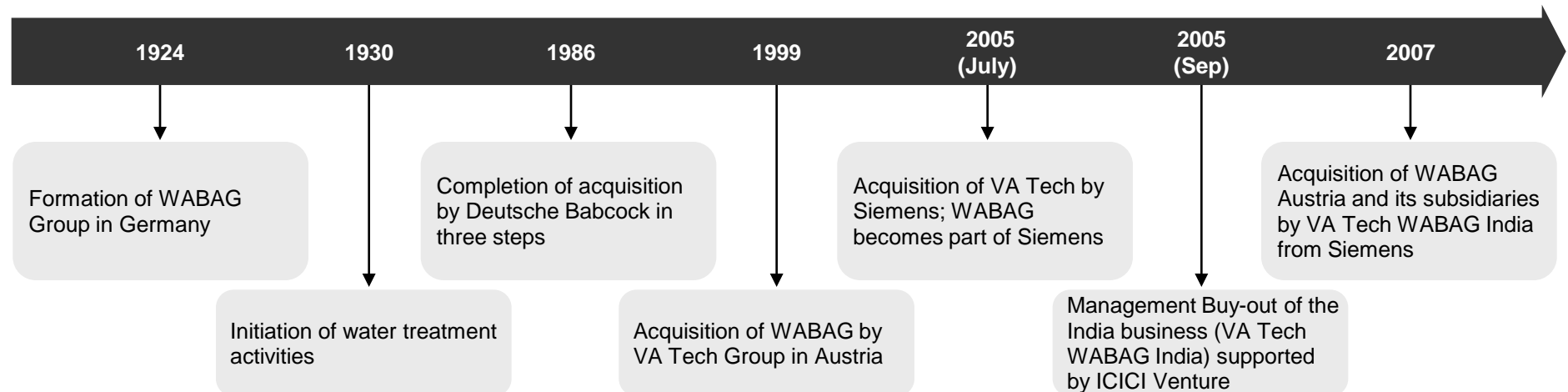
VTW has R&D centres located in Chennai, India and at Vienna and Winterthur in Austria and Switzerland respectively. Wabag Austria and Wabag Wassertechnik own 157 patents, which include both process and product patents. Wabag Austria has also applied for 51 patents that are pending. VTW has a workforce of approximately 1,469 including 757 qualified engineers. In India it employs around 754 employees including 588 qualified engineers

Financial performance FY08-10



Source: Company DRHP

Company history and evolution



Company Overview (Cont'd)

Issue Price

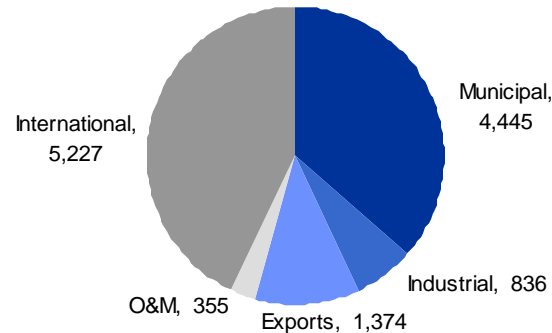
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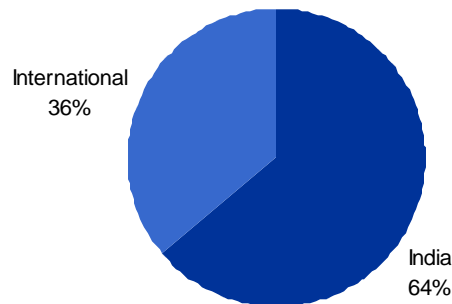
Business Mix

Sales Mix FY10 (Rs. mn)



Source: Spark Research

Order book (~Rs. 28bn) Mix FY10



Source: Spark Research

India	Municipal	<ul style="list-style-type: none"> This segment handles drinking water and wastewater treatment for municipal corporations and wastewater treatment for industrial clients
	Industrial	<ul style="list-style-type: none"> This segment caters to the 'pure' water needs of industries such as Power, Steel, Refineries, Petrochemicals, Fertilizers, SEZs, etc. While industrial clients are tech-savvy and the barriers to entry are high, this segment has had low margins due to the high incidence of levy of penalties and LDs by PSU clients
	Exports	<ul style="list-style-type: none"> Caters to both municipal and industrial clients in overseas markets Key target markets are South East Asia and the Middle East. SE Asia has tremendous potential for industrials treatment, while in the Middle East, desalination and municipal sewage treatment are important Margins are moderately higher than domestic projects
	O&M	<ul style="list-style-type: none"> O&M contracts provide steady stream of cash flow with higher margins compared to other SBUs As customer focus shifts to minimization of total life cycle costs, customers are bundling O&M contracts with EPC contracts for new plants and this represents significant opportunity for the Company In our view, there is also an opportunity for business from O&M contracts coming up for renewal in India and overseas markets
International Subsidiaries		<ul style="list-style-type: none"> The International business organization relies on a very large installed base of complex reference plants in Central and East Europe, Near and Middle East, China and North Africa It has a number of subsidiaries, offices and establishments in many countries in these regions enabling the acquisition of large and complex projects and contracts

Company Overview (Cont'd)

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Services Offering

VTW performs complete design of treatment plants starting from the preparation of the basic engineering plan to the detailed blueprints on hydraulics, layout, process calculations and electrical & mechanical equipment

The civil construction work is subcontracted to select contractors and civil engineering. WABAG extensively supervises the operations of subcontractors through appropriate quality control and assurance systems

Commissioning involves a step-by-step procedure encompassing examination of equipment procured and their integration into a fully functioning system. The objective is to ensure that all specifications and guarantees relating to output are met

WABAG provides customized O&M services based on client requirements.

It also undertakes projects on a BOOT/TOOT/ DBO/O&M basis based

O&M is a high margin business



A qualified internal team designs the equipment needed for the plant and provides the layout to pre-selected manufacturers

VTW has developed a global procurement platform to drive cost efficiencies

The mechanical, electrical, instrumentation and piping erection works are subcontracted to erection contractors and carried out under VTW's supervision

WABAG provides training to the client's personnel in terms of understanding, managing and operating the plant. This ensures that the plant functions smoothly after commissioning. WABAG also continues to support the user on process-related issues, equipment breakdown problems, etc.

WABAG is primarily a turnkey contractor for water and wastewater treatment plants. It executes water treatment projects on a turnkey basis. Its principal expertise lies in selection of appropriate technology, design, engineering and project execution while the civil works and manufacturing of equipment are outsourced

Market segments

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<p>Drinking Water Treatment</p>	<ul style="list-style-type: none"> Besides conventional surface water- drinking water treatment plants, WABAG provides innovative and state-of-the-art solutions for potable water generation from non-conventional sources like sea and brackish water Highest installed capacity of highly efficient and space saving plate type clarifier for clarification process in drinking water treatment plants 228 treatment plants have been installed since 1995
<p>Municipal Wastewater Treatment</p>	<ul style="list-style-type: none"> Offers end-to-end services in the field of municipal wastewater treatment including operation and maintenance of sewage treatment plants Has experience and expertise across a large number of aerobic as well as anaerobic biological technologies for wastewater treatment 370 installed plants since 1995 guarantee the environmentally compatible disposal of wastewater
<p>Desalination</p>	<ul style="list-style-type: none"> One of the foremost companies in the world offering a complete range of sea and brackish water desalination technologies Has more than 20 years experience in the field of desalination and has designed, installed and successfully commissioned more than 100 plants producing desalinated water
<p>Recycling</p>	<ul style="list-style-type: none"> With increased pressures on the world's water resources, the reuse of wastewater has become very important WABAG offers tailor-made solutions for recycle and reuse of wastewater Uses Reverse Osmosis, Ultra filtration, Micro filtration, Membrane Bio Reactors for water recycling Operates a unique direct potable water reuse plant in Windhoek Goreangab, Namibia with a capacity of 21,000 m³ per day
<p>Industrial and Process Water Treatment</p>	<ul style="list-style-type: none"> Offers the entire range of demineralization and condensate polishing processes and has some of the world's largest demineralization plants to its credit 208 plants installed since 1995, supplying 3.3mn m³ of water daily
<p>Industrial Wastewater Purification</p>	<ul style="list-style-type: none"> Provides total water management solutions across a wide spectrum of effluents like refinery waste, titanium leachate etc Since 1995, WABAG has completed 118 plants for various industrial unit

Investment Rationale

Unique speciality EPC play vis-à-vis ubiquitous civil EPC

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VA Tech Wabag is a niche technology based play on water infrastructure spend in India and other emerging markets. We argue that VTW is different from typical civil EPC players owing to niche technology, and designing & engineering capabilities required in a water treatment plant/ Waste water treatment plant (WWTP)/ Desalination plant.

Designing and engineering requirements

- Our research on the water sector suggests that around 25% of overall WTP/WWTP/ Desalination project execution involves highly engineered equipments and high end activities such as designing, engineering and preparing of blue prints of processes
- This is unlike other EPC projects where the key requirement is civil and erection

Niche Technology

- Water projects are technically complex and requires customised solutions rather than standard solutions required in typical civil EPC
- VTW is proactively pursuing R&D to offer latest and competitive solutions for customised clients requirement. It has R & D centres located in Chennai, India and at Vienna and Winterthur in Austria and Switzerland respectively. It has also established International Engineering Centre at Pune in India
- Wabag owns 157 patents which include both process and product patents. Wabag Austria has also applied for 51 patents that are pending. (refer annexure)

VTW's in-house technology and low cost Indian base gives competitive edge over peers

- No royalty payment
- Lesser overheads as compared to foreign peers

Skill sets

- Owing to the complexity involved, water turnkey solutions require qualified engineering staff.
- VTW has around 1,469 employees which includes 757 qualified engineers (i.e 52%).

VTW won a Rs. 5bn project with Kerala Water Authority despite being L2. They offered more suitable solution (lamella clarifiers) which required lesser land space and higher efficiency

Competitive advantage

- In India, VTW competes with pure EPC players having tie-ups with foreign technology players. As VTW owns many product/process technologies and not dependent on other technology players, it is well placed to bid for projects at very competitive rates

Our research suggests that in case of Chennai desalination project, Nammeli, VTW's bid was 17% lower than L2 and 70% lower than H1

Special focus on emerging markets which is witnessing strong growth

Issue Price

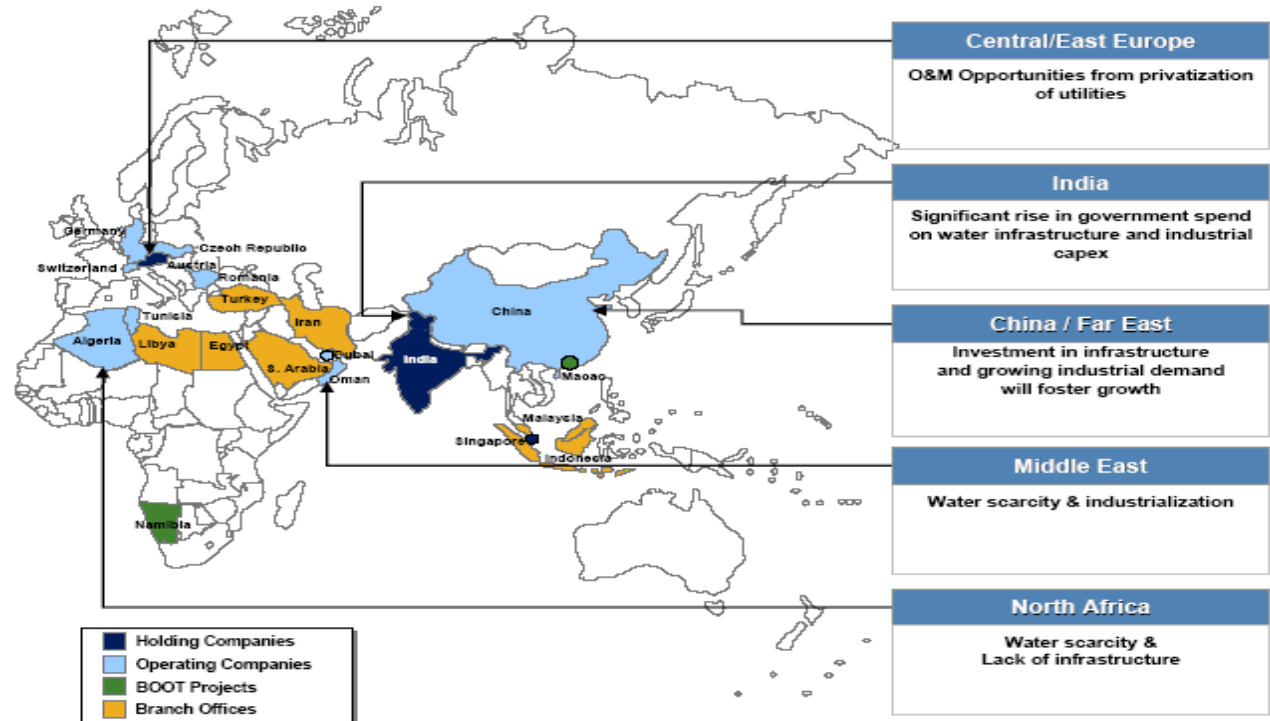
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Market (USD mn)	2007	2010E	2013E	CAGR
Saudi Arabia	2,455	3,832	5,981	16%
Romania	507	771	1,173	15%
Algeria	933	1,346	1,942	13%
India	2,531	3,556	4,996	12%
Oman	343	482	677	12%
Egypt	1352	1,849	2,529	11%
China	32,662	44,670	61,091	11%
Libya	835	1,111	1,479	10%
Spain	5,045	6,715	8,938	10%
Iran	1,203	1,558	2,018	9%
UAE	1,908	2,471	3,200	9%
Turkey	1,949	2,455	3,093	8%
Mexico	2,591	3,264	4,112	8%
Hungary	762	960	1,209	8%
Taiwan	2,078	2,546	3,119	7%
Total	57,154	77,585	105,556	11%

WABAG enjoys significant presence in most of the fast growing water and waste water treatment markets across the globe



Source: Global water intelligence 2008

We estimate emerging markets including India forms around 80% of VTW's revenues. VTW has been expanding its operations across emerging markets over the period to leverage the international Wabag brand and its reference lists to tap the high growth expected in these markets. It has recently set up full fledged subsidiary companies in China, Turkey and Egypt with local management. Local presence in these geographies is enabling it to understand client requirements better

Key beneficiary of the massive investments likely to happen in India

Issue Price

Rs. 1,310

Target

Rs. 1,954

Huge deficiency in safe water supply and sanitation facilities

- India with 16% of the population has only 4% of the available fresh water
- The per capita water supply in Indian cities is only 146 litres per day as compared to availability of more than 500 litres per capita per day in developed countries like the US
- Water demand in India is expected to rise from 552BCM in 2000 to 1093BCM by 2025
- Only, 21% of Indian population have access to piped drinking water and 28% to the improved sanitation facilities
- Waste water treatment is a massive opportunity as only 27% of waste water gets treated before disposal which is increasingly causing severe pollution

Huge funds allocated for Urban water infrastructure (Eleventh plan)

Funds Requirement - Urban Basic Services		Proposed Flow of Funds	
Sub-sector	(Rs. bn)	Source of Funding	(Rs. bn)
Urban water supply	537	Central Sector Outlay	700
Urban sewage and treatment	532	State Sector Outlay	350
Urban drainage	202	Institutional Funding	100
Solid Waste Management	22	External Agencies	100
Others	0.18	FDI and Private Sector	42
Total	1,292		1,292

Source: Ministry of Urban Development

As per Central pollution control board report, the per capita per day water supply increased to 187 litres in Dec 2009. Still there is an urgent need to atleast double the water supply to 360litres per capita per day to the 257mn people in class I/II cities (as on Dec 2009)

This would mean an opportunity of Rs. 447bn in WTP/ Desalination (44K MLD additional capacity at a cost of Rs. 10mn per MLD)

- Stringent Industrial norms driving industry players to treat waste water before disposal. Recycling of waste water for household usages is picking up sharply given shortage of fresh water in the country
- This % increased to 35% as on Dec 2009 as per Central Pollution control board report – Still long way to go. Increasing this % to 50% would entail an investment of Rs. 86bn on WWTP over next 2 years (assuming current waste water generation)

The proportion of waste water treated is at alarmingly low levels

Particulars	Class I cities	Class II towns	Total
Population (mm)	187	38	225
Water Supply (MLD)	29782	3035	32817
Water Supply (LPCD)	160	81	146
Wastewater Generated (MLD)	23826	2428	26054
Wastewater Generated (LPCD)	127	65	116
Wastewater Treated (%)	29%	4%	27%
Wastewater Untreated (%)	71%	96%	73%

Source: The Eleventh 5 yr plan documents

At the India Business Forum in Singapore, Water Resources Ministry Secretary Umesh Narayan Panjari highlighted investment opportunities in the Indian water sector, where \$50 billion investment is expected between 2007-2012,

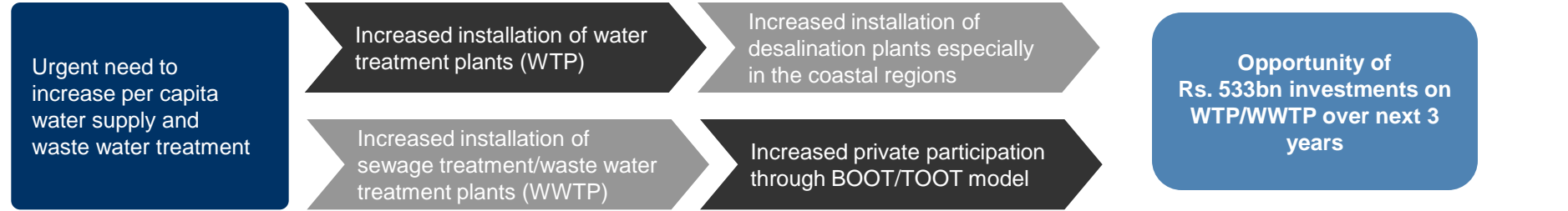
Key beneficiary of the massive investments likely to happen in India (Cont'd)

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(Addition capacity of ~44,000 MLD WTP @ Investment of Rs. 10mn per MLD; Additional capacity of ~6,000 MLD WWTP capacity of @ investment of Rs. 15mn per MLD)

Key Catalysts

- Increased funding from Int. agencies like World bank, Asian Dev. Bank (ADB) and Japan Bank for International Cooperation
- Renewed focus of Govt – Introduction of National water mission;
- JNNURM
- Regulatory norms driving compulsory sewage treatment for Industries

- VTW has proven its execution capabilities in large EPC contracts such as the construction of a 455 MLD WTP at Panjrapur; demineralization plant and condensate polishing at the refinery in Panipat and currently executing 100MLD desalination plant in Chennai
- We believe VTW is rightly poised with its advanced technology and execution capabilities to tap this Indian opportunity

Recently announced projects/plans

Region	Rs. mn	Particulars	Stage
Orissa	9,450	9 sewage plants proposed under Orissa Integrated Sanitation Improvement Project	Preliminary survey done
Goa	1,610	2 plants - 10MLD and 25MLD proposed	Bidding stage
Maharashtra	25,000	500MLD - 3 desalination plants proposed by MMRDA	Under Prel. Survey
Maharashtra	15,000	150MLD water recycle plant proposed by MCGM	Bidding stage
TN	30,000	Drinking water projects across state	Planning stage
Kerela	8,500	Sewage treatment projects	Planning stage
Punjab	44,000	Revamp of water supply and sewage system in 131 cities	Planning stage
Other states	50,000	Various WTP/WWTP projects	
Total	183,560		

Source: Projects Today, Spark Research

Strong order backlog of Rs. 28bn, robust order pipeline and resilient demand in emerging markets to drive doubling of revenues over FY10-13E

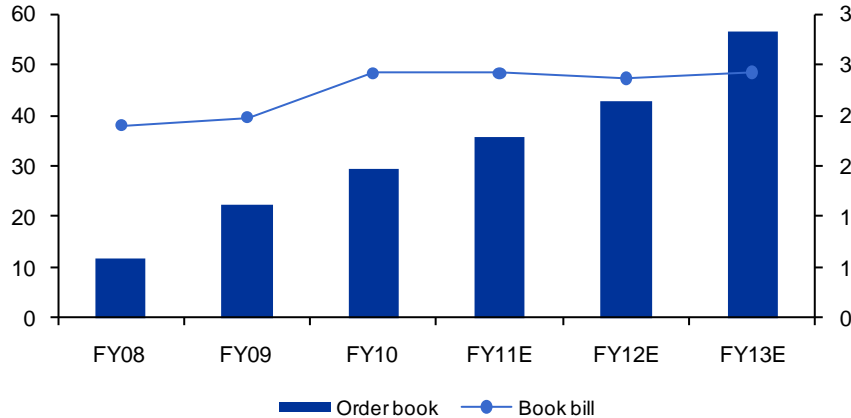
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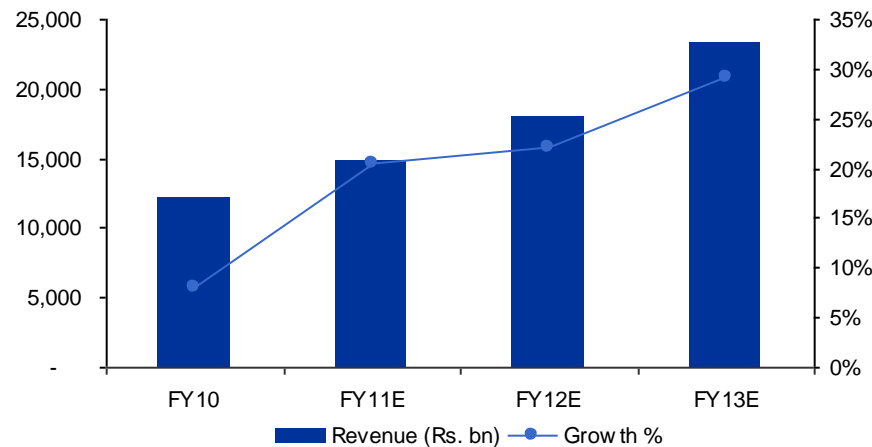
Rs. 1,954

Rising backlog with current book-bill of 2.4x



Source: Company DRHP, Spark Research

Revenues likely to double over FY10-13E



Source: Company DRHP, Spark Research

- We expect VTW revenues to double over FY10-13E on the back of strong order backlog, order pipeline and robust inflows expected from the emerging markets
- Current order book of Rs. 28bn has an execution cycle of around 2 years
- Based on industry sources, we believe that VTW has a strong order pipeline of Rs. 7.5bn in India and ~Rs. 5bn in overseas – This gives a strong support to our order inflows expectation in FY11E
- The recently bagged Chennai desalination plant order (Rs. 10bn) has opened up many opportunities for VTW in India and MEA

List of key on-going projects

Name of Project	Client	(In Rs. mn)	Completion Dt.
Indian			
Water system for thermal power plant, Vizag	An Indian steel plant	1,344	November-10
Water system package for 2x500 MW power plant at Durgapur	Damodar Valley Corporation	1,345	July 2010 (applied for ext)
54.6 MLD sewage treatment plant and allied works at Keshorpur	Delhi Jal Board	1,875	November-10
100 MLD sea water reverse osmosis desalination plant, chennai	Chennai Metro Water Supply & Sewerage Board	10,330	EPC - January 2012
50 MGD water treatment plant Dwarka	Delhi Jal Board	1,490	January-10
Overseas (Eur mn)			
Teheran WWTP	Tehran Sewerage Company, Iran	40	June-11
Benghazi 2&3	Housing and Infra Board, Libya	15	March-13
Zansur Pumping Stations	Housing and Infra Board, Libya	16	August-12

Source: Company DRHP

Margin profile on improving trend owing to rising O&M revenues, turnaround in Industrial business and cost rationalisation

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Rising share of O&M sales

- Increased emphasis on high margin O&M business; We estimate that around 25% of current order book comprises of O&M.

Cost Rationalisation

- It has started executing good proportion of international project with Indian manpower
- Global procurement policy and low cost sourcing model with data and vendor sharing across geographies; Integration synergies in the areas of engineering and procurement
- Shifting R&D to India – opened R&D centres in Pune and Chennai

Turnaround of Industrial biz

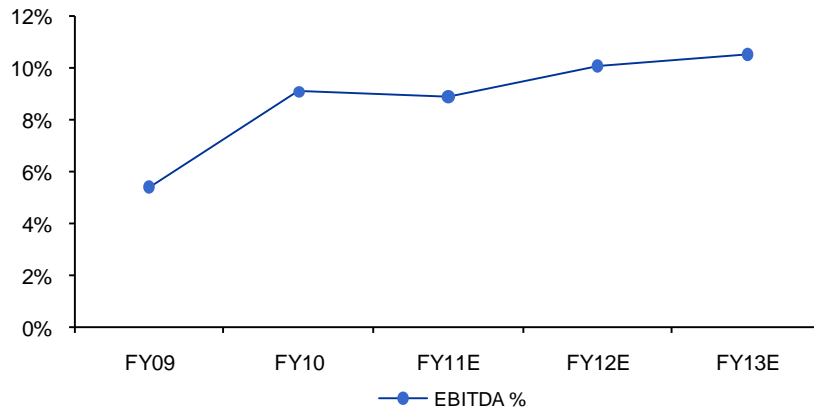
- Earlier Industrial projects were executed without price escalation which entailed losses when commodity rose sharply; Now, it is strategically bidding for orders only with price escalation clause; At present, around 65% of overall orders contain price escalation clause

Increased indigenization

- Utilising its engineering capabilities to reduce imports. It is designing the required components and getting it fabricated by Indian vendors;
- Outsourcing designing work related to overseas projects to India

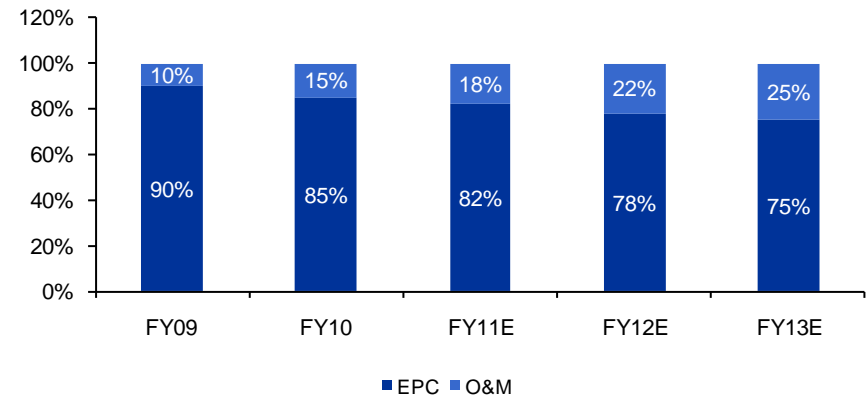
We expect EBITDA margin expansion from 5.4% to 10% over FY09 – FY12E

We expect the rising trend in EBITDA margin to continue



Source: Company DRHP, Spark Research

Rising share of high margin O&M revenues to raise margins



Source: Spark Research

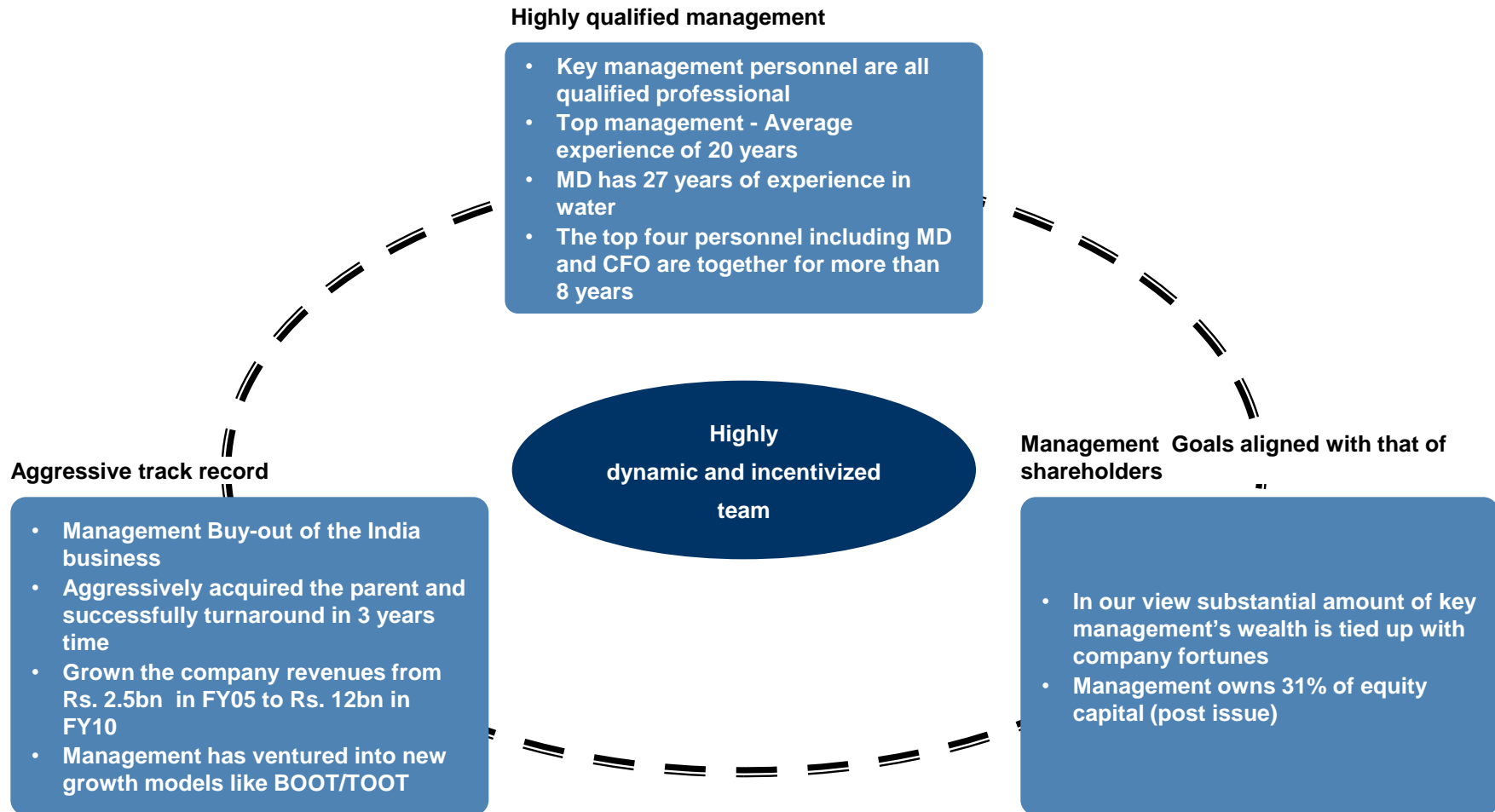
Strong and well incentivized management

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VA Tech Wabag

Buy

Wabag's strong brand recall, advanced technology and reference list along with resilient business model provides strong competitive advantage

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Strong Brand Wabag

- More than 80 years old Wabag brand in water management globally
- It helps VTW to penetrate new markets, pre-qualify for bids
- Expand services in new areas such as BOOT and TOOT
- VTW bids as European player in international markets

Advanced Technology and strong reference list

- Wabag Austria and Wabag Wassertechnik own 157 patents which include both process and product patents. Wabag Austria has also applied for 51 patents that are pending
- Provides customized solutions for total water management employing advanced technologies
- Wabag has a project reference list of more than 2,250 projects over the last three decades

Resilient Model

- Outsourcing – civil works, construction and erection works are outsourced to third party contractors (around 30% of project)
- Asset light model – Gross block is just 10% of Total Assets
- Fungible manpower – capability to execute around 25% of an overseas project with Indian manpower

Expanded operations to 19 countries

Key focus on engineering and designing

Negative working capital in overseas and modest working capital in India

Negligible capex requirement

Sales increased 5x from Rs. 2.5bn in FY05 to Rs. 12.2bn in FY10

High core ROCE in the range of 25-30%

VTW is the only water player in India which has advance technical capabilities and is not dependent on foreign players. This gives it an edge over the construction players having tie-ups with foreign firms. VTW offers water solution of international quality at competitive rates as it doesn't require to incur exorbitant overheads on managing foreign teams in India

Valuation

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We expect VTW's revenues and EPS to grow by CAGR 24% and 45% respectively over FY10-13E. We believe VTW would command a premium valuation owing to its high growth prospects (revenues to double over FY10-13E), high core capital efficiencies, strong brand recall; execution track record; and lack of any other listed pure-play water player.

In our view, the best way to value VTW is the earnings multiplier approach given the strong earnings visibility. We believe that DCF valuations are inappropriate in VTW's case as it operates in a cyclical industry, currently witnessing strong growth. The BG charges which are reported under financial items are quite significant which makes EV/EBITDA valuation criteria less suitable, particularly given depreciation charges are not substantial.

SOTP - Valuation	
Particulars	FY12E
PAT excl-cash (Rs. mn)	980
Target multiple (x)	18
Core business valuation (Rs. mn)	17641
Free Cash as on FY10 (Rs. mn)	1617
Cash proceeds from IPO (Rs. mn)	1250
Total cash value (Rs. mn)	2867
Overall Target Valuation (Rs. mn)	20508
Fully diluted shares (post issue) (nos. mn)	10.5
Target Price (Rs.)	1954
Upside over Issue price of Rs. 1310	49%

We have valued VTW based on SOTP methodology applying an earnings multiple of 18x on its core (ex-cash) FY12E earnings of Rs. 980mn and 1x free cash of Rs. 2.8bn (post-issue) resulting in a target price of Rs. 1,954. This implies an upside of 49% over the issue price of Rs. 1310. We recommend investors to Buy VTW up till the price of Rs. 1,800.

We believe VTW stock should command premium to second tier EPC players like IVRCL and discount to technology driven engineering companies like Thermax.

Our target multiple of 18x implies a premium of 30-35% to second tier construction players, given the former's niche engineering capabilities, in-house technology, management pedigree; better capital efficiencies and secular growth opportunities across India and other emerging markets

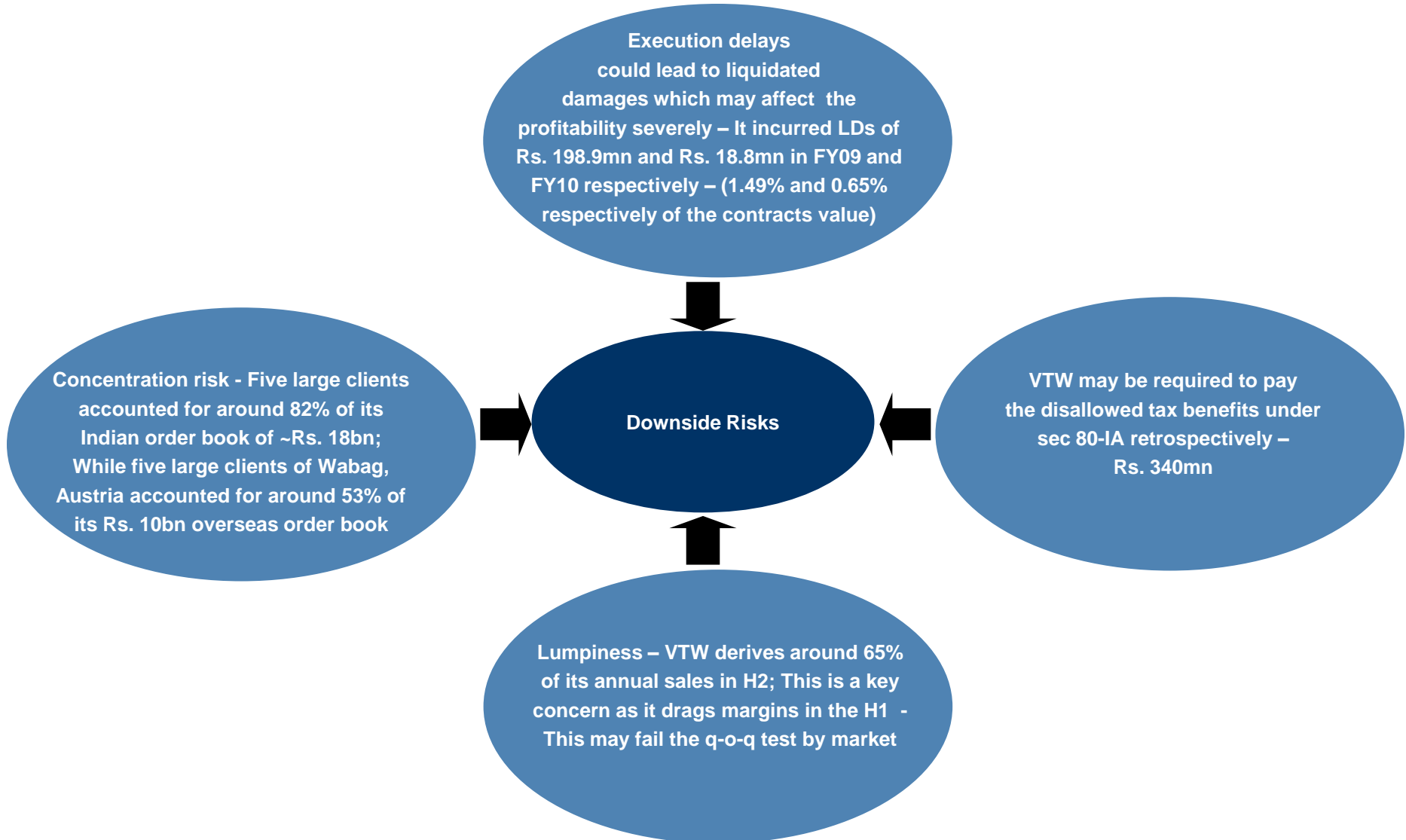
Key Risks

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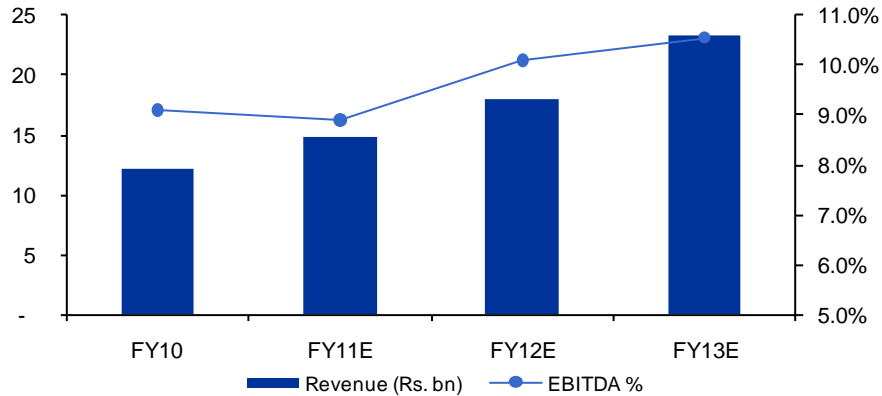
Rs. 1,954



Financial Analysis

Issue Price Rs. 1,310 Target Rs. 1,954

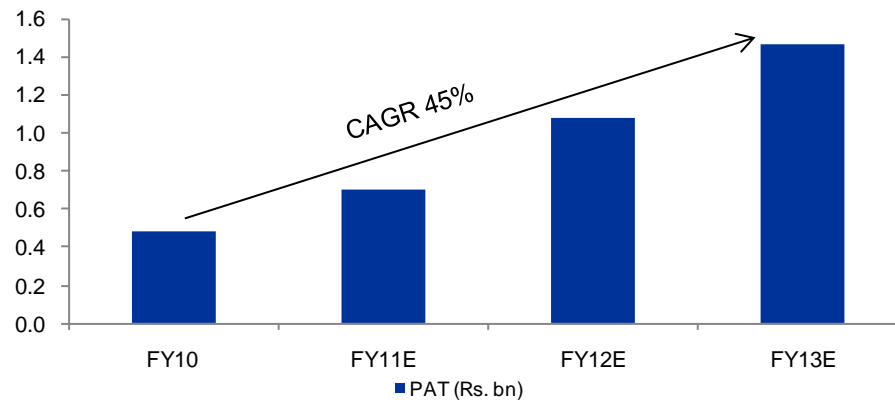
Revenues likely to double over FY10-13E; Margins on uptrend



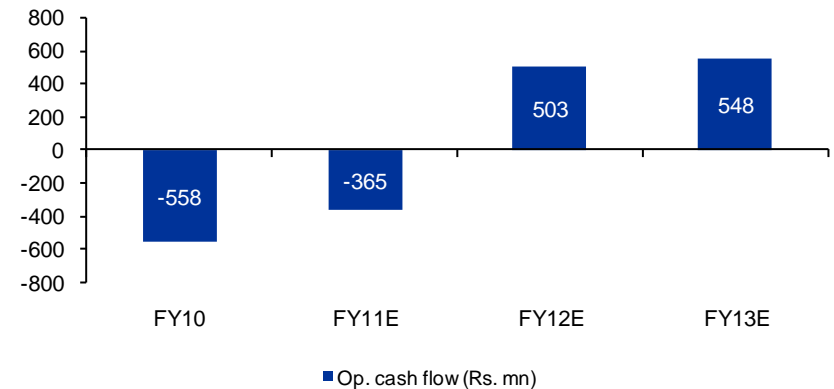
- Revenues are likely to grow at CAGR of 24% over FY10-13E owing execution of large on-going orders like Chennai desalination projects
- Margins are on an uptrend. We expect the benefits of cost rationalisation and increased outsourcing to get offset by higher commodity prices in FY11 before regaining momentum in FY12
- Apparently, VTW's RoEs are in the range of 12-16% due to large cash on the balance sheet – cash was around 84% and 55% of the networth as on FY09 and FY10 respectively. **The core RoEs are in the range of 23%-27%**
- VTW is making negative operating cash currently owing to investments in working capital. VTW is deliberately investing in working capital in overseas countries specifically where it incurs high BG charges due to lack of banking line

Source: Company DRHP, Spark Research

Sturdy PAT growth driven in top line momentum and better margins



Operating cash flows to turn positive in FY12



Source: Company DRHP, Spark Research

Source: Company DRHP, Spark Research

Financial Summary

Issue Price

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Abridged Financial Statements				
Rs. mn	FY09	FY10	FY11E	FY12E
Profit & Loss				
Revenues	11,333	12,237	14,754	18,029
EBITDA	614	1,113	1,313	1,821
Depreciation	84	139	138	127
EBIT	530	974	1,175	1,694
Other Income/Exp	203	69	105	130
Interest	354	299	325	361
PBT	379	744	955	1,463
Net Profit	422	494	704	1,075
Adjusted Net Profit	363	478	704	1,075
Balance Sheet				
Shareholders Equity	3,729	4,008	5,962	7,037
Total debt	459	391	391	391
Total Netw orth & Liabilities	4,189	4,399	6,353	7,428
Net fixed assets	241	239	165	246
CWIP	1	58	268	278
Investments	147	134	141	148
Current assets	10,812	10,174	13,287	16,113
Current liabilities	7,356	6,548	7,894	9,646
Net current assets	3,457	3,627	5,393	6,467
Total Assets	4,189	4,399	6,353	7,428
Cash Flows				
Cash flow s from Operations	(577)	(558)	(365)	503
Cash flow s from Investing	98	350	(215)	10
Cash flow s from Financing	(86)	(54)	1,250	-
Cash Generated	(564)	(262)	670	512
Opening Cash	3,606	3,145	2,185	2,856
Closing Cash	3,145	2,185	2,856	3,368

Key metrics				
	FY09	FY10	FY11E	FY12E
Growth ratios (%)				
Sales	85.5%	8.0%	20.6%	22.2%
EBITDA	248.9%	81.1%	18.0%	38.7%
Adj. Net Profit	310.9%	31.9%	47.1%	52.7%
Margin ratios (%)				
EBITDA	5.4%	9.1%	8.9%	10.1%
EBIT	4.7%	8.0%	8.0%	9.4%
Adj. Net Profit	3.2%	3.9%	4.8%	6.0%
Performance ratios				
ROIC (%)*	28.6	23.3	25.0	28.4
RoE (%)	10.6	12.4	14.1	16.5
RoCE (%)	17.2	14.8	17.4	19.3
Sales / Total Assets (x)	2.9	2.8	2.7	2.6
Fixed Assets Turnover (x)	26.6	26.7	26.9	28.4
Financial stability ratios				
Total Debt to Equity (x)	0.12	0.10	0.07	0.06
Inventory & Debtor days	202.6	200.0	218.0	218.0
Creditor days	236.9	195.3	195.3	195.3
Valuation metrics				
Issue Price (Rs.)	1,310			
Market Cap (Rs.mn)	13,748	13,748	13,748	13,748
Fully Diluted Shares (mn)	10.5	10.5	10.5	10.5
Adjusted EPS (Rs.)	38.2	50.7	67.1	102.4
P/E (x)	34.3	25.8	19.5	12.8
EV (Rs.mn)	9,621	10,434	11,144	10,625
EV to Sales (x)	0.8	0.9	0.8	0.6
EV/ EBITDA (x)	15.7	9.4	8.5	5.8
P/B	3.69	3.43	2.31	1.95

*Operating profit (after tax) divided by operating capital employed

Industry Analysis

Worldwide thirst for water is unquenchable – Rising demand with fixed supply amidst inadequate infrastructure is likely to widen water deficit

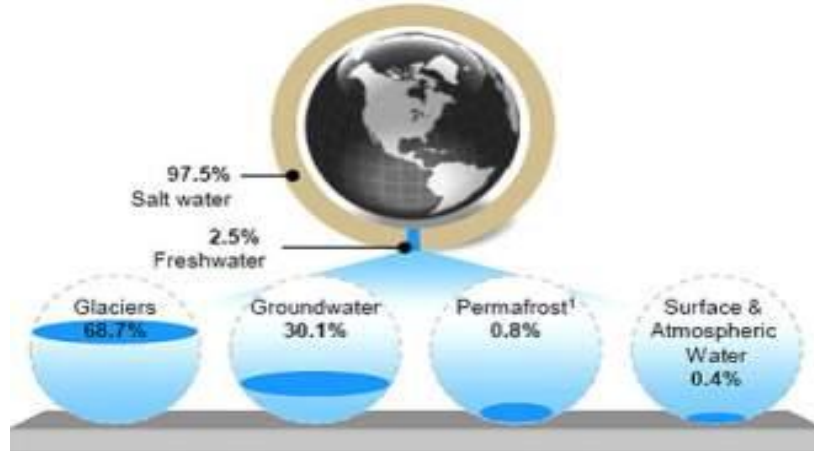
Issue Price

Rs. 1,310

Target

Rs. 1,954

Global fresh water reserves is just 2.5% of the overall availability



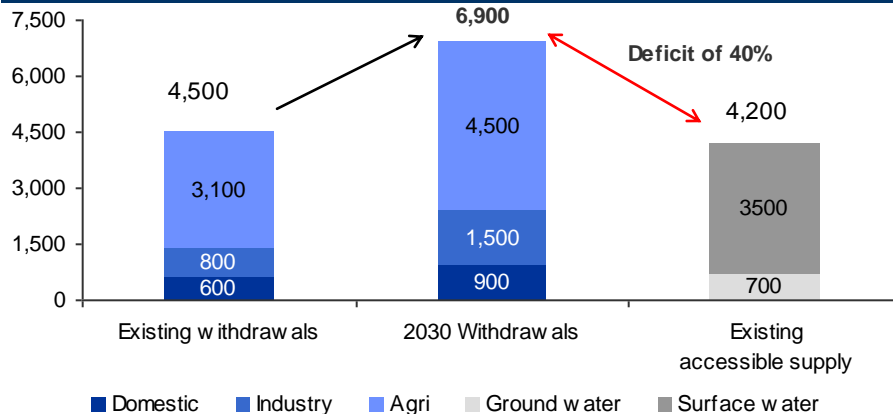
Source: World Water Development Report 2

Constrained water supply and poor infra structure

- Freshwater supply is relatively fixed – 2.5% of overall availability
- Climate change - Melting glaciers are likely to increase flood risk during the rainy season, and drought during dry-season
- Increasing pollution of the water reserves reduces fresh water supply
- Accessible freshwater resources are distributed unequally around the world, and subject to varying patterns of usage and discharge
- In 2008, over 2.6bn people were living without access to improved sanitation facilities, and nearly 900 million people were not receiving their drinking-water from improved water sources
- Only 58% of the world's population have access to piped water; Only 36% of the global population is connected to a sewer network

Source: Spark Capital Research

Demand-Supply deficit to grow to 40% if proper investments are not made in water infrastructure



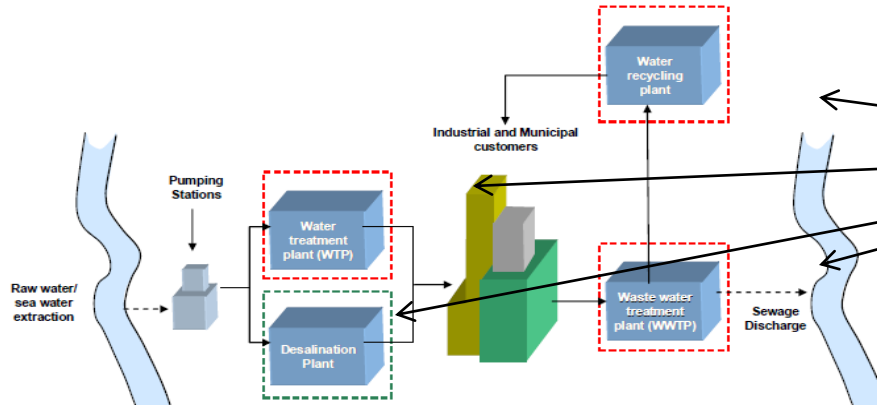
Source: Mckinsey - Charting Our Water Future

Rising population, increased urbanisation and industrialisation driving water demand

- Population growth - World's population is growing by about 80mn people a year implying increased freshwater demand of about 64bn cubic metres a year
- Urbanisation - urban population is expected to double by 2030 in Africa and Asia; with towns and cities of the developing world making up for close to 81% of the total urban population
- Higher living standards are causing greater consumption of water per capita
- Increased industrialisation in developing nations is likely to drive demand for water

Source: Spark Capital Research

Water cycle - overview



VA Tech Wabag is present across the value chain in the water treatment and waste water treatment segments

Source: World Water Development Report 2

Water Treatment/ Waste water treatment opportunity

Municipal

Drinking Water Treatment

Waste Water Treatment

Desalination

Demand Drivers

- Rising population
- Fixed water resources
- Existing low availability of consumable water
- Govt. Initiatives to improve water infra
- Rising standard of living

Industrial

Process Water Treatment

Waste water treatment

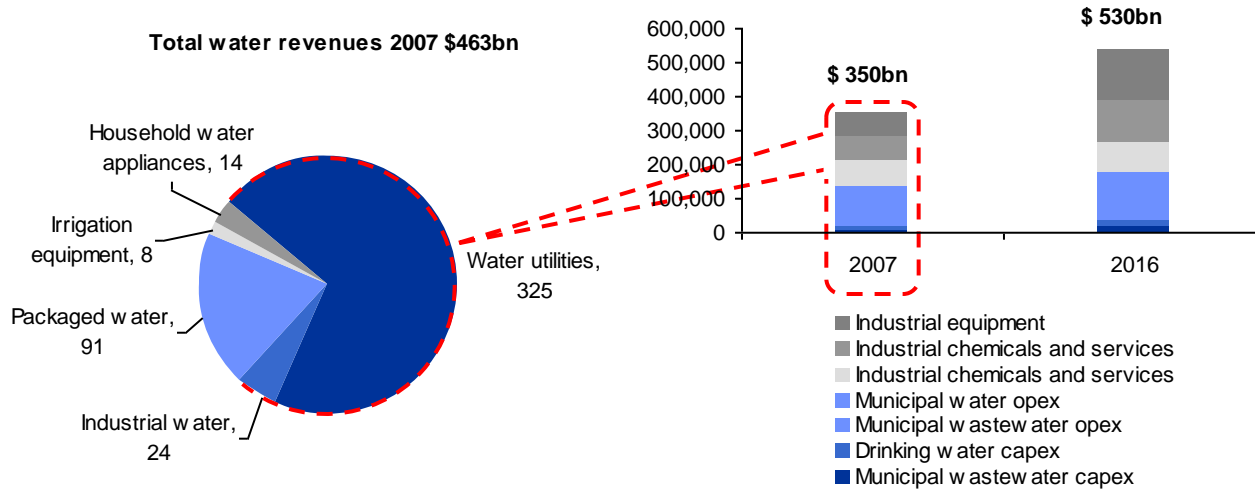
Demand Drivers

- Water is an important production factor for industries like power, food and beverages, pulp and paper, pharmaceuticals, refineries etc.
- Stringent norms related to disposal of waste water

Annual market opportunity of USD 530bn by 2016; Emerging markets to lead the growth path

Issue Price	Rs. 1,310	Target	Rs. 1,954
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Water utilities and Industrial segments of water to grow @5% CAGR to USD 530bn by 2016



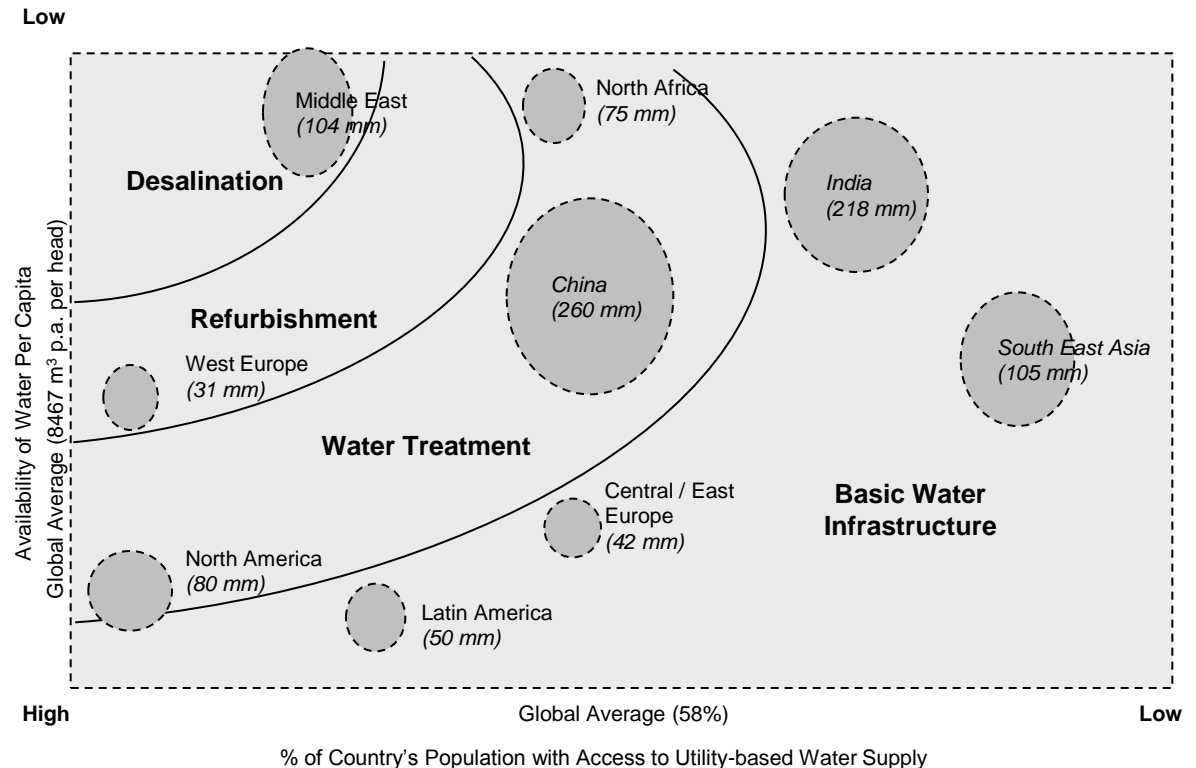
Source: Global Water Markets 2008

- Developing nations require huge investments to bridge the gaps and reduce the deficit
- Developed nations need to refurbish, maintain and upgrade their existing run down infrastructure and meet the stringent environmental regulations
- The world business council for sustainable development estimates the total cost of replacing ageing water supply and sanitation infrastructure in industrial countries may be as high as USD 200 billion p.a.

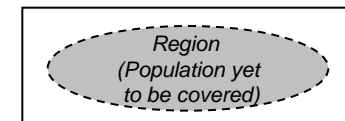
While the overall growth in global markets is likely to be ~5%, VTW is present in the below mentioned 15 fastest growing markets

Country		Saudi Arabia	Romania	Algeria	India	Oman	Egypt	China	Libya	Spain	Iran	UAE	Turkey	Mexico	Hungary	Taiwan
Mkt Size (\$ Mn)	2007	2,455	507	933	2,531	343	1,352	32,662	835	5,045	1,203	1,908	1,949	2,591	762	2,078
	2016	9,103	1,839	2,704	6,870	921	3,490	80,714	1,959	11,606	2,638	4,113	3,910	5,142	1,469	3,876
CAGR	(%)	16%	15%	13%	12%	12%	11%	11%	10%	10%	9%	9%	8%	8%	8%	7%

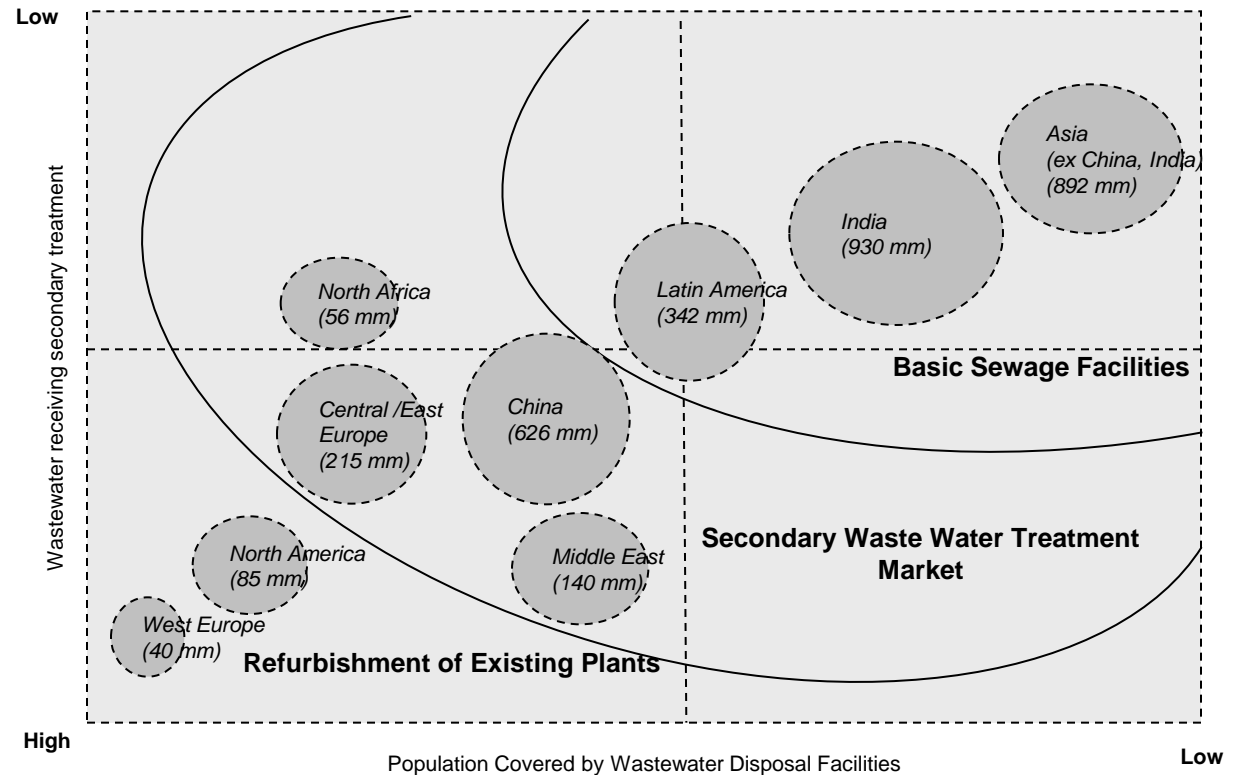
- The biggest markets for water are countries with low per capita availability of water and a strong government commitment to universal water access
- Markets in South East Asia present an opportunity to water treatment companies in terms of municipal projects to provide universal utility water access economically
- Water deficient markets like the Middle East and North Africa will soon need to deploy desalination and water re-use technologies to provide adequate water to their citizens
- In China, growth is expected to come from a rapid growth in population and an increased standard of living
- Markets in Europe require mainly refurbishment of existing facilities and capacity expansion for a moderately growing population



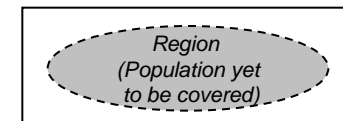
Source: Global Water Intelligence 2008



- Most countries of the developing world have enabled limited access to wastewater disposal facilities to their citizens
- An increase in GDP per capita in these countries, combined with urbanization and an improved standard of living will lead to ramp-up of wastewater treatment infrastructure in countries like China, India and SE Asia



Source: Global Water Intelligence 2008



Indian water management market poised for strong growth

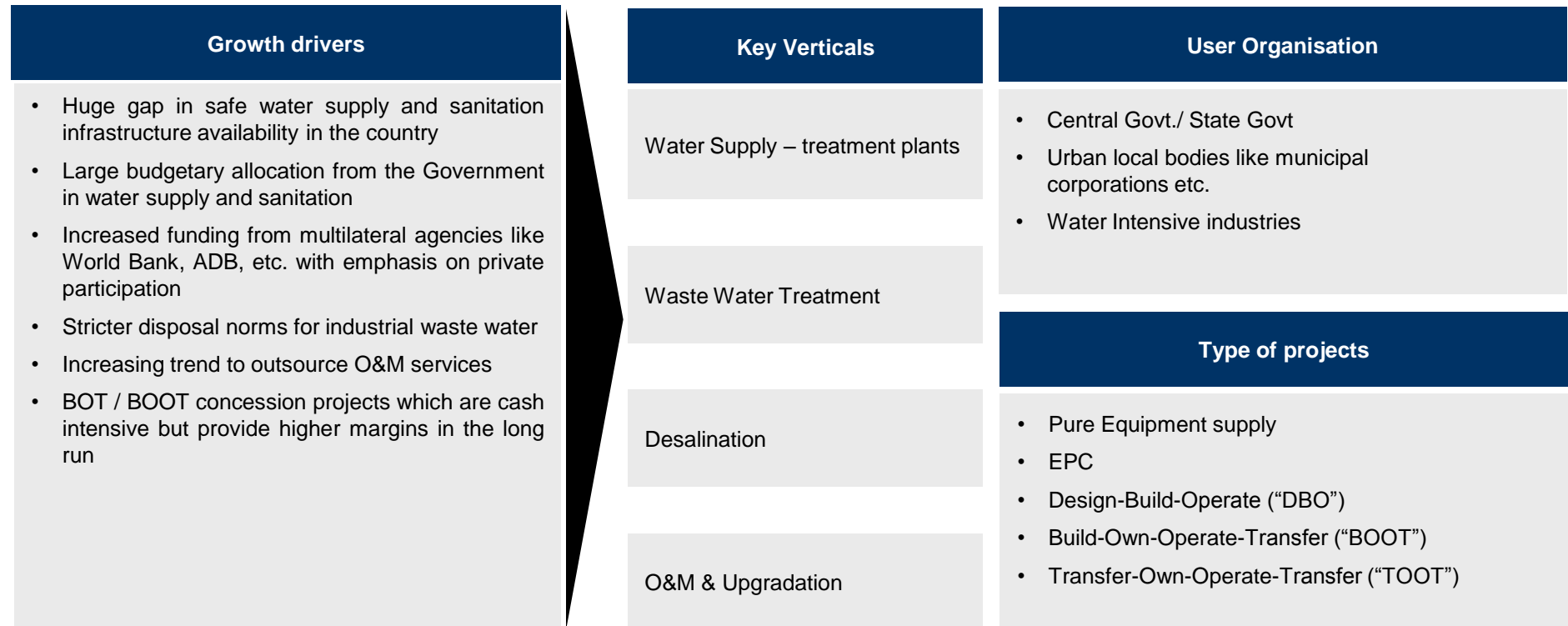
Issue Price

Rs. 1,310

Target

Rs. 1,954

We believe water management players have an enormous opportunity in India owing to rising demand for domestic and Industrial water, lack of sufficient water infrastructure, Govt renewed focus evidenced by large funds allocated to water and sanitation. This would entail growth of 12-15% per annum in the current estimated WT/WWT market of Rs. 146bn (USD 3175mn). At present the agriculture sector dominates water use owing to its importance in the Indian economy, but with higher level of development, more water will be demanded for domestic and industrial purposes.



Indian water management market poised for strong growth (Cont'd)

Issue Price

Rs. 1,310

Target

Rs. 1,954

Huge deficiency in safe water supply and sanitation facilities

- India with 16% of the population has only 4% of the available fresh water
- In India, per capita fresh water availability has dropped from 4000 m³/year in 1962 to 1647 m³/year in 2007
- Water demand in India is expected to rise from 552BCM in 2000 to 1093BCM by 2025
- Only, 21% of Indian population have access to piped drinking water and 28% to the improved sanitation facilities
- Waste water treatment is a massive opportunity as only 27% of waste water gets treated before disposal which is increasingly causing severe pollution. Further, waste treatment plant can be used to generate potable water

Large Govt. funds allocated to water and sanitation

- Govt has been increasingly focusing on water and sanitation evidenced by larger funds allocated to this segment under the current five year plan as compared to previous plan
- Govt is targeting 100% water supply and sanitation to the urban population by the end of Eleventh Plan. This would entail a **cash outlay of Rs. 1292bn**
- Under JNNURM, 463 projects requiring an **investment of ~Rs. 500bn** were sanctioned. Around 76% of these projects aim at improving urban water supply and sanitation
- Govt. has allowed 100% FDI in the infra sector, including water treatment systems. This is a strong incentive for global players to test Indian waters

The proportion of waste water treated is at alarmingly low levels

Particulars	Class I cities	Class II towns	Total
Population (mm)	187	38	225
Water Supply (MLD)	29782	3035	32817
Water Supply (LPCD)	160	81	146
Wastewater Generated (MLD)	23826	2428	26054
Wastewater Generated (LPCD)	127	65	116
Wastewater Treated (%)	29%	4%	27%
Wastewater Untreated (%)	71%	96%	73%

Source: The Eleventh 5 yr plan documents

Huge funds allocated for Urban water infrastructure

Funds Requirement - Urban Basic Services		Proposed Flow of Funds	
Sub-sector	(Rs. bn)	Source of Funding	(Rs. bn)
Urban water supply	537	Central Sector Outlay	700
Urban sewage and treatment	532	State Sector Outlay	350
Urban drainage	202	Institutional Funding	100
Solid Waste Management	22	External Agencies	100
Others	0.18	FDI and Private Sector	42
Total	1,292		1,292

Source: Ministry of Urban Development

At the India Business Forum in Singapore, Water Resources Ministry Secretary Umesh Narayan Panjari highlighted investment opportunities in the Indian water sector, where \$50 billion investment is expected between 2007-2012,

Competitive Landscape

Issue Price

Rs. 1,310

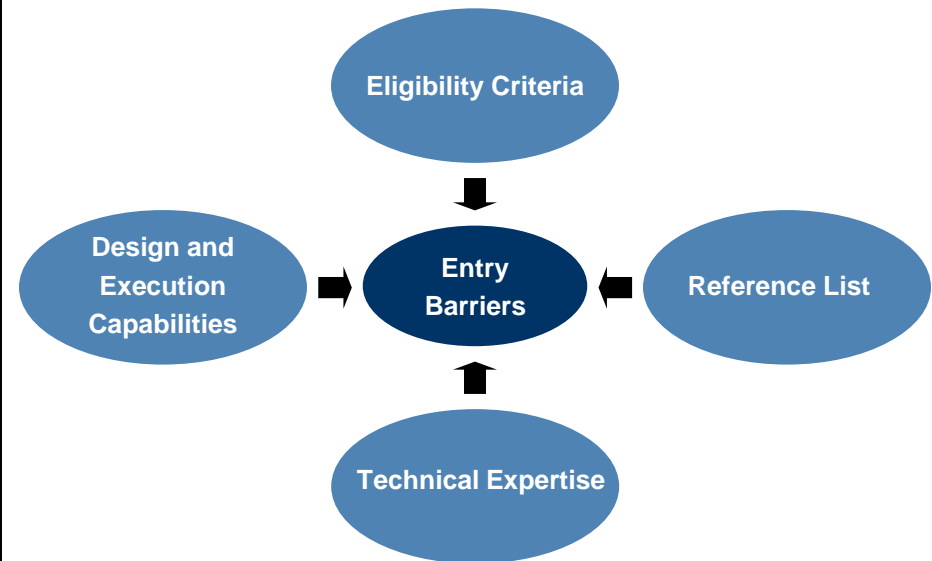
Target

Rs. 1,954

Water treatment is a regional business – locally oriented, and driven by local regulations, local water supply, local demand and local contracts. Players’ knowledge of local regulations and environment is very important. Therefore currently the water industry is highly fragmented industry with very few global players. But as the industry moves towards larger and more complex projects, the industry gets more organized. The global players with the dual advantage of global brand/technological competence and a local setup gain prominence and a larger share of the total industry pie. A global brand and technology base coupled with the local cost can make companies desirable bidders for a project. VTW scores well both on the global brand/technology and the local set-up in various geographies

Peer Group	
Global market	
Global	Suez Environment Veolia Environment
US	American Water Company
North Africa, MEA and Asia	Singaporean companies - Hyflux Japanese companies - Marubeni ; Spanish companies - Befesa, Aqualia, Cadagua, FCC, ACS
Indian market	
Municipal	Hindustan Dorr Oliver Limited Larsen & Toubro Limited
	IVRCL
Industrial	Thermax Ion Exchange Engineers India Gammon India Nagarjuna Const.

Source: Company DRHP



Most of the Indian players possess strong execution capabilities in the area of civil construction and erection but lack water expertise. They tie-up with foreign water technology players like Veolia and, Befesa etc. VTW is the only Indian water player which has capabilities across the value chain equipped with the brand and Technology of Wabag, Austria and low cost Indian set-up

Annexure

Technology and R&D capabilities

Issue Price

Rs. 1,310

Target

Rs. 1,954

- Provides customized solutions for total water management employing technologies from its constantly improved portfolio
- Has the ability to convert R&D into proprietary technologies with proven commercial applications and economic returns
- Works closely with customers to develop customized, cost-effective and practical solutions
- Participates in setting industry standards for wastewater treatment in many industries Z

Wide ranging products & technologies

Biological Treatment	Sludge Treatment	Anaerobic Digestion	Coagulation	Flocculation	Demineralization
Disinfection	Filtration	Sedimentation	Reverse Osmosis	Thermal Desalination	Screening & Separation
Ion Exchange	Ozone Treatment	UV Treatment	Membrane Treatment	Electro Dialysis	Water Stabilization

Patents for several innovative technologies

Fluidized Bed Biology	Biofiltration	Activated Sludge Processes	Anaerobic Biological Processes	Membrane Bioreactor
FLUOPUR®	BIOPUR	Hybrid™, SBR	EKJ™, UASB, an-OPUR™, EGSB	MARAPUR®, Megamodul™
Membrane Filtration	Denitrification	Oxidation Processes	Thermal Desalination	Sludge Digestion and Disintegration
RO, MF, UF, NF	BIODENE®, ENR®	ADOX®, BIOZONE®	MED, TVC, MVC, MSF	BIOZONE-AD®

Operating Structure and Business Overview

Issue Price

Rs. 1,310

Target

Rs. 1,954

VA Tech WABAG India

HQ: Chennai, India

India - Municipal SBU

India - Industrial SBU

India - O&M SBU

India - International SBU

SE Asia Operations

Singapore
Singapore

Sultanate of
Oman

China
Beijing

WABAG Austria

HQ: Vienna

European Operations

North African Operations

Middle East Operations

Eastern Europe

WABAG
Czech Rep.
Bmo

Romania
Bucharest

WABAG
Algeria
Algiers

Libya
Tripoli

Saudi Arabia
Riyadh

Iran
Tehran

Central Europe

Turkey
Ankara

WABAG
Tunisia
Tunis

Egypt
Cairo

Far East Operations

Western Europe

WABAG
Switzerland
Winterthur

Germany

Namibia
O&M⁽¹⁾
Windhoek

Macao
O&M⁽²⁾
Macao

China
Beijing



(1) O&M project for drinking water plant – JV with Veolia and Berlin Wasser Int

(2) O&M project for Macao sewage treatment – 20% held by local partner

Rating Interpretation	
BUY	More than 100% absolute return over a maximum of three years
OUTPERFORM	We expect the stock to outperform peers/ relevant sector index but is not a Buy
UNDERPERFORM	We expect the stock to underperform peers/ relevant sector index but is not a Sell
SELL	More than 25% downside to the stock price

Analyst Certification

The Research Analyst(s) who prepared the research report hereby certify that the views expressed in this research report accurately reflect the analyst(s) personal views about the subject companies and their securities. The Research Analyst(s) also certify that the Analyst(s) have not been, are not, and will not be receiving direct or indirect compensation for expressing the specific recommendation(s) or view(s) in this report.

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