

IRB Infrastructure reported **+14% YoY growth in topline** (Rs8.45bn) and **+18% YoY growth in Operating Profit** (Rs3.8bn), in-line with our and consensus estimates. The numbers however, were better than our and street expectation at the **PAT level (Rs1.21bn, +10% YoY)**, mainly due to lower than expected interest expense (FX losses being capitalized and **refinancing of debt for Bharuch-Surat project**). While the EPC division reported robust execution (+18% YoY), traffic growth at all major projects remained muted. Overall, there were no major surprises, and the results were along expected lines.

IRB Infrastructure's stock has **fallen ~20% in the last one week**, on the back of allegations of its subsidiaries investing monies into a private firm, Purti Power and Sugar Ltd, promoted by Mr. Nitin Gadkari, member of the main opposition party at the center (BJP). IRB's management has clarified that the money invested in Purti Power, was **invested by Mr. Dattatray Mhaiskar**, member of the promoter group, **in his personal capacity**. The company has also denied allegations of being granted any undue favors, and that all the projects it won, were awarded through transparent bidding process. The Ministry of Corporate Affairs (**MCA**) and **IT department have initiated an investigation** into this matter.

While it is extremely difficult to deduce what the results of the investigation will be, we note that this is **not the first time that the company has come into news for a non-business reason**. An analysis of its stock price reveals, that **over the last two years**, the stock has witnessed a **sharp fall seven times** – with just one of those falls being for “pure business reason” (*for details, see inside*).

With the results of the polygraph test conducted on the MD in May-2012, still awaited, this revelation comes as a major blow to the company. We believe that in the current situation, the **risk-reward profile for the stock looks extremely unfavorable**. While there are very few positive triggers that can boost the stock price over the next six months, the negative events, and the probability of their occurrence is much higher. We see a **maximum +20% upside** from current levels **with a low probability** of occurrence and a **potential -40% downside**, with a relatively **high probability** of occurrence (*details inside*).

In wake of the unfavorable risk-reward profile, and the recent non-business developments, we believe the company can no longer be valued, just by aggregating the DCF value of its projects. A discount needs to be applied to the fundamental value, to reflect the concerns and overhang of the non-business developments, and their potential impact on the stock price.

We apply a **50% discount to the fair value** of the stock (arrived at valuing individual projects using DCF and EPC division at 3.5x FY14E EV/EBITDA), to arrive at a **price target of Rs109**, representing **10% downside** from current levels. We recommend investors to cut their losses at current levels, in view of the potential downside, if the recent developments take a negative turn for the company. We recommend **NEUTRAL**.

NEUTRAL

IRB IN | CMP RS 120

TARGET RS 109 (-10%)

Company Data

O/S SHARES (MN) :	332
MARKET CAP (RSBN) :	40
MARKET CAP (USDBN) :	0.7
52 - WK HI/LO (RS) :	210 / 100
LIQUIDITY 3M (USDMN) :	10.4
FACE VALUE (RS) :	10

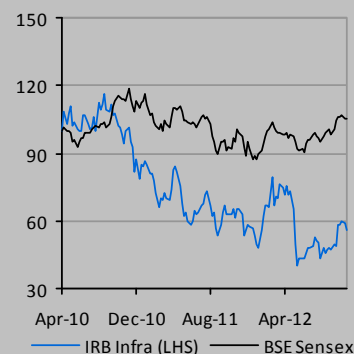
Share Holding Pattern, %

PROMOTERS :	54.3
FII / NRI :	18.5
FI / MF :	4.7
NON PROMOTER CORP. HOLDINGS :	5.1
PUBLIC & OTHERS :	18.4

Price Performance, %

	1mth	3mth	1yr
ABS	-21.2	-4.6	-29.2
REL TO BSE	-19.4	-12.1	-32.7

Price Vs. Sensex (Rebased values)



Source: PhillipCapital India Research

Other Key Ratios

Rs mn	FY12	FY13E	FY14E
Net Sales	31,307	37,152	43,055
Ebidta	13,735	15,720	20,788
Net Profit	4,960	5,128	5,410
EPS, Rs	14.9	15.4	16.3
PER, X	8.0	7.8	7.4
EV/EBIDTA, x	6.9	6.6	5.9
EV/Net Sales, x	3.0	2.8	2.9
ROE, %	18.8	15.5	13.5

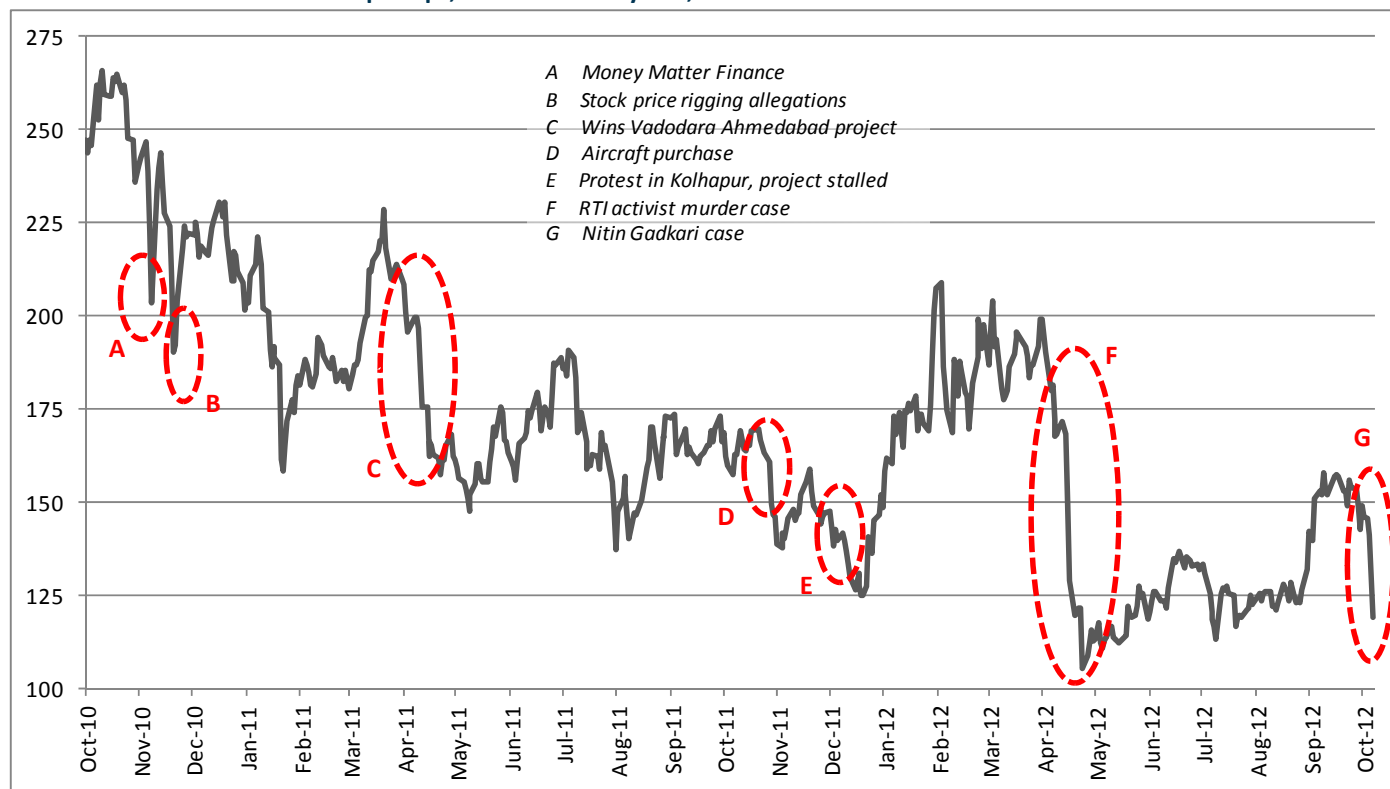
Source: PhillipCapital India Research Est.

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Eventful last two years

Over the last two years, IRB's stock price has fallen by over 50%. An analysis of the stock price movement over this period reveals, that there were **seven company specific reasons**, for which the stock registered a sharp fall. The interesting part is that **only one** of those seven was a **"pure business reason"** (*Vadodara Ahmedabad project win*) and the rest were related to the promoter group or their activities outside the IRB business.

IRB Stock Price – most of the sharp drops, in the last two years, have been for 'non-business' reasons



Source: Bloomberg, PhillipCapital India Research

- **Nov-2010:** IRB was "allegedly" linked with Money Matters Finance – the prime accused in a loan syndication fraud case being investigated. The management later clarified that none of its loans were syndicated through the accused company. **Matter closed for all practical purpose.**
- **Dec-2010:** The company was "reportedly" named, along with two other companies (Ruchi Soya and KS Oil), in stock price rigging activity being probed by SEBI. The management denied all charges, and having received any official communication from the regulator. **Matter closed for all practical purpose.**
- **Apr-2011:** IRB won the prestigious Vadodara-Ahmedabad project, although with a highly aggressive bid. The company offered to pay a premium of Rs3.09bn per annum to NHAI – 63% higher than the second highest bidder. Financial closure for the project achieved. **Yet to commence operation.**
- **Nov-2011:** IRB's subsidiary Modern Road Makers Pvt Ltd (MRM) purchased an aircraft in FY11, which was perceived, by the investor community, as irrational spending. The management clarified that it was done in order to aid its business, which was now expanding beyond Maharashtra and Gujarat.
- **Dec-2011:** Local residents in Kolhapur started protest against the imposition of toll on the interior road network, being developed by IRB – citing bad quality and incomplete work. The state government then formed a three member committee to investigate and submit its report. Report is awaited. **Tolling yet to commence.**
- **May-2012:** The MD of the company, Mr. V.D.Mhaiskar and two other company officials were asked by the CBI to undergo a polygraph test, regarding the murder

investigation of an RTI activist, Satish Shetty in Jan-2010. **Polygraph test concluded, but result not yet disclosed by the CBI.**

- **Oct-2012:** Indian Against Corruption (IAC) activist accuses the main opposition party member, Mr. Nitin Gadkari, of granting undue favors to various companies during his tenure (1995-99) as PWD minister in Maharashtra, in return for monies invested by them in his firm Purti Power and Sugar Ltd. Records show that Mr. Dattaray Mhaisakar, belonging to the promoter group of the company, invested Rs1.65bn into the firm. The management claims the said amount was invested by Mr. Mhaiskar in his personal capacity. Ministry of Corporate Affairs (MCA) and IT department have taken up investigation of the case.

What Now ?

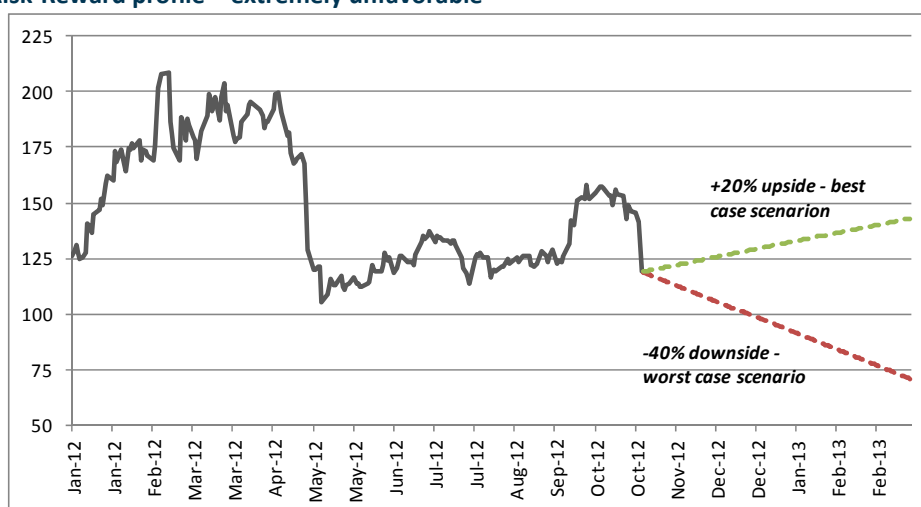
The current situation seems very difficult for the company to get out of. While most of its projects are performing along expected lines, we believe the overhang of the recent development (RTI Murder investigation and alleged links with Purti Power and Sugar Ltd) will continue for the next few months.

We have analyzed the various triggers (positive and negative) for IRB's stock, keeping other things constant. We realize that there are very few positive events that have a high probability of occurrence. On the other hand, there exist, multiple potential negative events that could have a significant impact on the stock price. Overall, the risk-reward snapshot looks highly unfavorable for the stock.

IRB Infrastructure – Possible stock price triggers from current level

Event	Probability of occurrence	Likely Impact	Comments
Positive			
New project win with good IRR	Highly Unlikely	5-10%	Highly unlikely given the competition intensity and all lucrative projects on western and southern belt bid out; Impact depends on the size of the project
Higher than expected traffic growth	Unlikely	2-5%	Unlikely given the current state of economy
100bps Interest rate cut in FY13	Unlikely	4-5%	Can have a huge impact but more than 50bps cut in FY13 looks unlikely
EPC margins improve	Highly Unlikely	2-3%	Unlikely to improve from current levels of 30%
MD clears polygraph test	NA	NA	Clearing polygraph test will not mean COMPLETE ACQUITAL - hence the impact expected to be limited
Cleared of Gadkari allegations	NA	NA	Since the company has admitted to have invested Rs1.65bn (although through promoter's personal capacity), the overhang of possibility of a business wrong-doing will remain
Negative			
MD fails polygraph test	NA	NA	Can have a HUGE impact - although the results of polygraph tests are not admissible in court, this will give CBI base to form a case against the MD, and investigate further
New project win with low IRR	Highly likely	10-15%	Impact can be very HIGH (depending on project size), as seen with the Vadodara-Ahmedabad project
Traffic growth declines	Likely	2-5%	Looks more likely, given the current state of economy
EPC Margins decline	Likely	2-3%	The only way the margins could go from the current 30% levels is South
Foray into external EPC work	Unlikely	5-10%	Lack of new BOT projects with decent IRRs, can force the company to go BACK to external contracts to maintain topline growth for EPC division; this will however be highly negative as the company will not be able to make EPC margins, in-line with those it makes for its captive projects
Further delay in commencement of tolling at Kolhapur, Ahmedabad project	Likely	4-5%	No word as yet from the Maharashtra government or NHAI on the status of the projects; while the Vadodara project might commence in next three months, tolling on Kolhapur project might be delayed further

Source: PhillipCapital India Research

Risk-Reward profile – extremely unfavorable


We note that large part of the 40% downside is on the back of the two recent non-business developments.

Source: Bloomberg, PhillipCapital India Research

In the wake of the unfavorable risk-reward profile, we have revised our recommendation on IRB to **NEUTRAL**. While the fundamental value of the business remains intact, we believe the stock can no longer be valued by valuing its different SPVs alone, and a discount needs to be applied for the non-business related issues, that will continue creating an overhang on the stock for next few months.

SOTP Valuation

DCF Valuation	Project Cost (Rs mn)	Length (kms)	Equity Value (Rs mn)	Per share (Rs)
Operational BOT Projects				
NKT	368	60	446	1.3
MKMM	180	33	380	1.1
Thane Bhiwandi	1,040	23	2,368	7.1
Pune-Nashik	737	30	1,580	4.8
Pune-Solapur	630	26	824	2.5
Kharpada	320	15	173	0.5
Thane-GHB	2,469	15	1,542	4.6
Mumbai-Pune	13,017	95	9,502	28.6
Bharuch-Surat	14,700	65	5,248	15.8
Surat-Dahisar*	25,372	239	1,157	3.5
MVR	3,076	68	1,756	5.3
Total Value	61,909	601	24,977	75.1
Under construction projects				
Kolhapur	4,300	50	1,521	4.6
Talegaon -Amravati	8,880	67	3,376	10.2
Jaipur - Deoli	17,330	149	7,619	22.9
Amritsar - Pathankot	14,453	102	3,713	11.2
Tumkur - Chitradurga	11,420	114	2,949	8.9
Vadodara - Ahmedabad	48,800	196	(3,226)	(9.7)
Total Value	105,183	678	15,953	48.0
E&C Business				
FY14E EBITDA			7,507	
Assumed EV/EBITDA			3.5	
Value to IRB			26,275	79.1
Others (Net Cash)			4,805	14.5
DCF SoTP Fair Value			72,010	217.0
Discount to fair value		50%		
Price Target			36,005	109.0

Source: PhillipCapital India Research

We apply a 50% discount to our fair value of IRB's business valuation, which gives a price target of Rs109, representing 10% downside from current levels. We recommend **NEUTRAL**.

QUARTERLY PERFORMANCE

Particulars (Rs mn)	2QFY12	3QFY12	4QFY12	1QFY13	2QFY13
Total income	7,358.8	7,454.8	8,480.0	9,797.8	8,453.3
yoy growth (%)	50.1	11.5	10.6	22.3	14.9
qoq growth (%)	(8.2)	1.3	13.8	15.5	(13.7)
Expenditure					
Direct Expenses	3,634.8	3,471.8	3,901.7	4,974.2	4,032.3
% of sales	49.4	46.6	46.0	50.8	47.7
Employee cost	313.3	362.2	419.5	357.9	365.1
% of sales	4.3	4.9	4.9	3.7	4.3
Admin expense	195.9	203.9	350.2	210.9	248.5
% of sales	2.7	2.7	4.1	2.2	2.9
TOTAL EXPENDITURE	4,144.0	4,037.9	4,671.4	5,543.0	4,645.9
% of net sales	56.3	54.2	55.1	56.6	55.0
EBITDA	3,214.9	3,416.9	3,808.7	4,254.8	3,807.5
yoy growth (%)	36.0	16.4	21.0	29.2	18.4
qoq growth (%)	(2.4)	6.3	11.5	11.7	(10.5)
EBITDA Margin (%)	43.7%	45.8%	44.9%	43.4%	45.0%
Other income	300.7	337.6	331.8	324.7	331.0
Interest	1,411.5	1,419.6	1,499.6	1,540.2	1,480.0
Depreciation	628.5	723.7	1,015.6	1,086.0	1,106.8
PBT	1,475.6	1,611.1	1,625.3	1,953.4	1,551.7
yoy growth (%)	22.1	(2.2)	16.9	8.5	5.2
qoq growth (%)	(18.0)	9.2	0.9	20.2	(20.6)
Tax	366.9	290.7	451.8	556.8	365.1
Tax rate	25%	18%	28%	29%	24%
PAT	1,108.7	1,320.4	1,173.5	1,396.6	1,186.7
yoy growth (%)	8.9	(2.9)	11.3	2.9	7.0
qoq growth (%)	(18.3)	19.1	(11.1)	19.0	(15.0)
Minority Interest	8.1	6.4	(30.0)	(21.8)	(23.0)
Net profit	1,100.6	1,313.9	1,203.5	1,418.4	1,209.7
yoy growth (%)	11.1	(1.2)	17.1	5.7	9.9
qoq growth (%)	(18.0)	19.4	(8.4)	17.9	(14.7)
Adjusted PAT	1,100.6	1,313.9	1,203.5	1,418.4	1,209.7
EPS	3.31	3.95	3.62	4.27	3.64

Interest expenses declined on qoq basis, mainly due to:

- FX losses being capitalized (P&L impact ~Rs40mn)
- Refinancing of loan for Bharuch-Surat project by IFCL. The new interest rate on the entire loan stands at 10.75%, as compared to 12% earlier

Source: Company, PhillipCapital India Research

SEGMENTAL BREAK-UP

	2QFY12	3QFY12	4QFY12	1QFY13	2QFY13
Revenue break-up (Rs mn)					
BOT segment	2,385	2,535	2,566	2,618	2,569
EPC segment	5,275	5,258	6,246	7,505	6,215
EBITDA break-up (Rs mn)					
BOT segment	2,116	2,285	2,271	2,319	2,266
EPC segment	1,399	1,469	1,865	2,260	1,873
EBITDA Margins (%)					
BOT segment	88.8	90.2	88.5	88.6	88.2
EPC segment	26.5	27.9	29.9	30.1	30.1

Source: Company, PhillipCapital India Research

Surat-Dahisar received **8.94% hike in tariff** this quarter – implying almost zero growth in traffic due to diversion in traffic from Thane

Tumkur-Chitradurga received **7% hike in tariff** last quarter – implying a decline in traffic, primarily due to mining ban in the region

Bharuch-Surat received **7.5% hike in tariff**

TOLL COLLECTION - PROJECT WISE BREAK-UP

Rs mn	2QFY13	2QFY12	1QFY13	YoY	QoQ
Surat - Dahisar	1,025	939	1,064	9%	-4%
Mumbai - Pune	1,039	997	1,035	4%	0%
Tumkur - Chitradurga	395	387	413	2%	-4%
Bharuch - Surat	397	347	381	14%	4%
Others	411	381	435	8%	-6%
Total	3,267	3,051	3,328	7%	-2%

Source: Company, PhillipCapital India Research

EPC REVENUE - PROJECT WISE BREAK-UP

Rs mn	2QFY13	2QFY12	1QFY13	YoY	QoQ
Surat-Dahisar	-	3,144	-	-	-
Kolhapur	-	380	-	-	-
Amritsar-Pathankot	2,064	437	1,697	373%	22%
Jaipur-Deoli	1,646	724	3,259	127%	-50%
Talegaon-Amravati	803	164	1,263	389%	-36%
Tumkur-Chitradurga	1,295	141	994	818%	30%
Others	100	99	96	1%	4%
Total	5,908	5,089	7,308	16%	-19%

Source: Company, PhillipCapital India Research

We have made minor changes to our estimates, to account for delay in commissioning of Kolhapur and Ahmedabad projects – both of which are expected to commence tolling by Dec-2012, as per the management.

REVISION OF ESTIMATES

	Old		New		Change	
	FY13E	FY14E	FY13E	FY14E	FY13E	FY14E
Revenue	38,979	44,109	37,152	43,055	-5%	-2%
EBITDA	16,023	20,882	15,720	20,788	-2%	0%
PAT	5,171	5,675	5,128	5,410	-1%	-5%

Source: PhillipCapital India Research

FINANCIALS

Income Statement

Y/E Mar, Rs mn	FY11	FY12	FY13E	FY14E
Net sales	24,381	31,307	37,152	43,055
Growth, %	43	28	19	16
Total income	24,381	31,307	37,152	43,055
Operating expenses	-13,442	-17,572	-21,432	-22,267
EBITDA (Core)	10,939	13,735	15,720	20,788
Growth, %	36.9	25.6	14.5	32.2
Margin, %	44.9	43.9	42.3	48.3
Depreciation	-2,254	-2,970	-4,084	-5,626
EBIT	8,685	10,765	11,636	15,162
Growth, %	40.7	23.9	8.1	30.3
Margin, %	35.6	34.4	31.3	35.2
Interest paid	-3,572	-5,505	-5,655	-8,297
Pre-tax profit	5,758	6,512	7,137	7,833
Tax provided	-1,117	-1,552	-2,089	-2,528
Profit after tax	4,641	4,960	5,048	5,304
Net Profit	4,523	4,960	5,128	5,410
Growth, %	17.4	9.6	3.4	5.5
Net Profit (adjusted)	4,523	4,960	5,128	5,410
Unadj. shares (m)	332	332	332	332
Wtd avg shares (m)	332	332	332	332

Balance Sheet

Y/E Mar, Rs mn	FY11	FY12	FY13E	FY14E
Cash & bank	12,000	18,208	14,805	17,454
Debtors	397	141	611	708
Inventory	1,638	1,624	2,036	2,359
Loans & advances	6,349	7,780	9,670	11,206
Other current assets	0	693	693	693
Total current assets	20,384	28,446	27,814	32,420
Investments	551	139	1,419	1,419
Gross fixed assets	41,317	66,189	66,189	113,564
Less: Depreciation	-7,695	-10,647	-14,731	-20,356
Add: Capital WIP	25,085	24,452	45,034	25,093
Net fixed assets	58,706	79,995	96,493	118,301
Total assets	79,641	108,580	125,727	152,140
Current liabilities	7,941	6,138	7,401	7,552
Total current liabilities	7,941	6,138	7,401	7,552
Non-current liabilities	46,487	72,753	79,571	101,375
Total liabilities	54,428	78,891	86,972	108,927
Paid-up capital	3,324	3,324	3,324	3,324
Reserves & surplus	21,002	25,243	34,389	38,954
Shareholders' equity	25,212	29,689	38,755	43,214
Total equity & liabilities	79,641	108,580	125,727	152,140

Cash Flow

Y/E Mar, Rs mn	FY11	FY12	FY13E	FY14E
Pre-tax profit	5,758	6,512	7,137	7,833
Depreciation	2,254	2,970	4,084	5,626
Chg in working capital	1,115	-3,657	-1,508	-1,806
Total tax paid	-1,153	-1,525	-2,089	-2,528
Cash flow from operating activities	7,975	4,300	7,623	9,124
Capital expenditure	-17,484	-24,258	-20,582	-27,434
Chg in investments	-100	411	-1,280	0
Cash flow from investing activities	-17,584	-23,847	-21,862	-27,434
Free cash flow	-9,609	-19,547	-14,239	-18,310
Equity raised/(repaid)	176	356	5,218	421
Debt raised/(repaid)	17,103	26,238	6,818	21,804
Dividend (incl. tax)	-583	-583	-1,200	-1,266
Other financing activities	-189	-483	0	0
Cash flow from financing activities	16,506	25,755	10,836	20,959
Net chg in cash	6,897	6,208	-3,403	2,649

Valuation Ratios & Per Share Data

	FY11	FY12	FY13E	FY14E
EPS, Rs	13.6	14.9	15.4	16.3
BVPS, Rs	73.2	85.9	113.5	127.2
DPS, Rs	1.5	1.5	3.1	3.3
Return on assets (%)	10.3	9.0	7.4	7.6
Return on equity (%)	20.2	18.8	15.5	13.5
Return on Invested capital (%)	13.4	11.4	8.8	9.0
RoIC/Cost of capital (x)	2.0	1.5	1.3	1.2
RoIC - Cost of capital (%)	6.6	4.0	1.8	1.7
Return on capital employed (%)	11.3	9.7	7.8	8.1
Cost of capital (%)	6.8	7.4	7.1	7.4
RoCE - Cost of capital (%)	4.5	2.3	0.8	0.7
Asset turnover (x)	0.5	0.4	0.4	0.4
Sales/Total assets (x)	0.4	0.3	0.3	0.3
Receivable days	5.9	1.6	6.0	6.0
Inventory days	24.5	18.9	20.0	20.0
Payable days	131.5	122.3	121.8	119.7
Current ratio (x)	2.6	4.6	3.8	4.3
Quick ratio (x)	2.4	4.4	3.5	4.0
Interest cover (x)	2.4	2.0	2.1	1.8
Dividend cover (x)	9.1	9.9	5.0	5.0
PER (x)	8.8	8.0	7.8	7.4
Price/Book (x)	1.6	1.4	1.1	0.9
EV/Net sales (x)	3.0	3.0	2.8	2.9
EV/EBITDA (x)	6.8	6.9	6.6	5.9
EV/EBIT (x)	8.5	8.7	9.0	8.1
EV/NOPLAT (x)	7.5	7.7	7.7	6.8
EV/CE	1.0	0.9	0.9	0.9

Source: Company, PhillipCapital India Research Estimates

Recommendation History

Recommendation	Target, Rs	CMP, Rs	Date
Neutral	109	120	31 Oct 2012
Under Review	Under Review	113	30 July 2012
Under Review	Under Review	121	11 May 2012
Neutral	215	199	19 Apr 2012

Management

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Research

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Banking, NBFCs

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Consumer, Media, Telecom

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Cement

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Economics

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Ankur Sharma	(9122) 6667 9759
Jishar Thoombath	(9122) 6667 9986

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Dhawal Doshi	(9122) 6667 9769
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Infrastructure

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Oil&Gas, Fertiliser

Gauri Anand	(9122) 6667 9943
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Retail, Real Estate

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Mid-caps

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