

FIG  
Real Estate  
Equity – India

## Unitech Ltd (UT IN)

### Underweight (V)

Target price (INR)	20.00
Share price (INR)	21.55
Forecast dividend yield (%)	0.6
Potential return (%)	-6.6

Note: Potential return equals the percentage difference between the current share price and the target price, plus the forecast dividend yield

Performance	1M	3M	12M
Absolute (%)	-24.7	-32.0	-40.2
Relative <sup>A</sup> (%)	-20.9	-24.4	-32.8

Index<sup>A</sup> BOMBAY SE IDX

RIC UNTE.BO  
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Market cap (USDm)	1,047
Market cap (INRm)	56,341
Enterprise value (INRm)	74,625
Free float (%)	25

Note: (V) = volatile (please see disclosure appendix)

16 May 2012

**Ashutosh Narkar\***

Analyst  
HSBC Securities and Capital Market  
(India) Private Limited  
+91 22 22681474  
ashutoshnarkar@hsbc.co.in

**Chirag Gupta\***

Associate  
Bangalore

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This report must be read with the disclosures and the analyst certifications in the Disclosure appendix, and with the Disclaimer, which forms part of it

UW (V): From bad to worse

- ▶ **4Q earnings were c97-98% below HSBCe and consensus as execution and EBITDA margin disappoint once again**
- ▶ **A lack of new launches hurt contracted sales (-17% q-o-q); we cut our earnings forecasts by 12-15% in FY13-14**
- ▶ **We retain our UW(V) with a revised TP of INR20 (from INR25); we think any re-rating would need more visibility on execution and new launches**

**4Q earnings surprise.** Unitech's reported earnings of INR23m (-98% y-o-y) were 98% below HSBCe and 97% below consensus. The weak performance was driven by: 1) slower execution as sales of INR7.16bn (-32% y-o-y) were 23% below HSBCe; 2) an extraordinarily low EBITDA margin of c5% (HSBCe of 28%) primarily as all its fringe businesses (25% of sales) reported either a loss or sub-10% margins, while the real estate business reported a low 17% margin owing to cost escalations; and 3) a higher tax rate (c94%).

**Contracted sales were let down by the limited new project launches.** Q4 contracted sales at INR7.8bn (1.8m sq ft @ INR4,352psf) were 34% below HSBCe. Average realisation on contracted sales was down by 22%. A key reason for lower-than-expected contracted sales was the limited new launches of 0.6mn sq ft (-85% y-o-y and -47% q-o-q) during Q4.

**We cut FY13-14e earnings by 18-20%.** We expect Unitech's execution to remain under pressure as the backlog of slow execution and new launches during FY12 will exert pressure on further execution scale-up during FY13-14. Consequently, we lower our sales volumes expectation by 10-15% and earnings by 18-20% over FY13-14e.

**Retain UW (V) with a revised TP of INR20 (INR25 earlier).** Our revised target price reflects lower visibility on Unitech's execution scale-up and recent earnings cut. This leads us to increase our target NAV discount from 53% (1 std deviation below mean) earlier to 60% (12% below 1std deviation). At a 60% NAV discount, we value Unitech at the bottom end of the peer trading range (25-60%). A combination of weak earnings, a deteriorating business environment and lack of share price catalysts suggests to us that Unitech may continue to trade at a lower valuation multiple.

Figure 1: Unitech valuation snapshot

(INR m)	Sales	EBITDA margin (%)	PAT	EPS (INR)	EPS growth (%)	ROE	PB
FY11a	31,870	29.0	5,676	2.17	-14.3	5.2	0.5
FY12a	24,466	16.4	2,484	0.95	-56.4	2.1	0.5
FY13e	34,273	31.0	4,928	1.88	98.4	4.1	0.5
FY14e	41,444	26.7	6,177	2.35	25.3	4.9	0.4

Source: Company data, HSBC estimates

## Financials & valuation

### Financial statements

Year to	03/2011a	03/2012e	03/2013e	03/2014e
<b>Profit &amp; loss summary (INRm)</b>				
Revenue	31,870	24,466	34,273	41,444
EBITDA	9,238	4,019	8,658	11,051
Depreciation & amortisation	-319	-434	-744	-881
Operating profit/EBIT	8,919	3,585	7,914	10,170
Net interest	-1,455	-1,229	-2,145	-2,145
PBT	8,483	4,397	7,728	9,517
HSBC PBT	8,483	4,397	7,728	9,517
Taxation	-2,704	-1,835	-2,550	-3,141
Net profit	5,676	2,484	4,928	6,177
HSBC net profit	5,676	2,484	4,928	6,177
<b>Cash flow summary (INRm)</b>				
Cash flow from operations	-1,419	17,338	-5,451	-410
Capex	-2,105	-1,270	259	533
FCF enterprise	-1,375	19,345	-1,088	3,761
Cash flow from investment	-3,507	-1,259	259	533
Dividends	-262	-328	-393	-459
Change in net debt	-2,241	-20,061	3,012	-1,146
FCF equity	-2,830	18,116	-3,233	1,616
<b>Balance sheet summary (INRm)</b>				
Tangible fixed assets	34,728	35,569	36,054	36,401
Current assets	230,241	225,002	234,907	243,908
Cash & others	4,509	21,090	18,079	19,225
Total assets	297,634	293,226	303,616	312,964
Gross debt	58,480	55,000	55,000	55,000
Net debt	53,971	33,910	36,921	35,775
Shareholders' funds	115,836	118,334	123,262	129,438
Invested capital	261,662	241,021	254,422	262,625

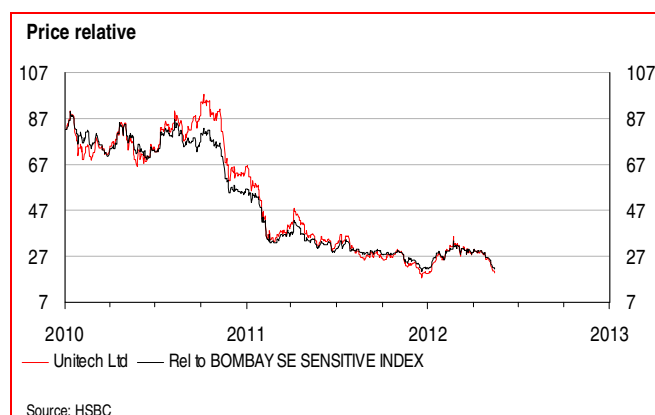
### Ratio, growth and per share analysis

Year to	03/2011a	03/2012e	03/2013e	03/2014e
<b>Y-o-y % change</b>				
Revenue	8.7	-23.2	40.1	20.9
EBITDA	-13.8	-56.5	115.4	27.6
EBIT	-14.0	-59.8	120.7	28.5
PBT	-6.2	-48.2	75.8	23.2
HSBC EPS	-14.3	-56.4	98.4	25.3
<b>Ratios (%)</b>				
Revenue/IC (x)	0.1	0.1	0.1	0.2
ROIC	2.5	0.8	2.1	2.6
ROE	5.2	2.1	4.1	4.9
ROA	2.4	1.1	2.2	2.5
EBITDA margin	29.0	16.4	25.3	26.7
Operating profit margin	28.0	14.7	23.1	24.5
EBITDA/net interest (x)	6.4	3.3	4.0	5.2
Net debt/equity	46.4	28.5	29.8	27.5
Net debt/EBITDA (x)	5.8	8.4	4.3	3.2
CF from operations/net debt		51.1		
<b>Per share data (INR)</b>				
EPS reported (fully diluted)	2.17	0.95	1.88	2.35
HSBC EPS (fully diluted)	2.17	0.95	1.88	2.35
DPS	0.10	0.13	0.15	0.17
NAV	44.27	45.11	46.99	49.34
NAV (adjusted)	0.00	0.00	0.00	0.00

### Valuation data

Year to	03/2011a	03/2012e	03/2013e	03/2014e
Premium/ (discount) to NAV	0.5	0.5	0.5	0.4
Premium/ (discount) to NAV (adj)				
PE*	9.9	22.8	11.5	9.2
FCF yield (%)	-7.0	44.5	-7.9	4.0
Dividend yield (%)	0.5	0.6	0.7	0.8

Note: \* = Based on HSBC EPS (fully diluted)



Note: price at close of 16 May 2012

## Unitech earnings update

Figure 2: Unitech quarterly earnings table

(INRm)	Q4 FY11	Q1FY12	Q2FY12	Q3FY12	Q4FY12	y-o-y	q-o-q
<b>Net sales</b>	<b>10,542</b>	<b>5,958</b>	<b>6,261</b>	<b>5,139</b>	<b>7,161</b>	<b>-32.1%</b>	<b>39.3%</b>
Total expenditure	(8,857)	(4,761)	(4,880)	(4,066)	(6,772)	-23.5%	66.5%
EBITDA	1,685	1,197	1,381	1,073	389	-76.9%	-63.7%
Depreciation/ amortisation	(67)	(84)	(85)	(93)	(172)	156.0%	83.9%
<b>EBIT</b>	<b>1,618</b>	<b>1,114</b>	<b>1,297</b>	<b>980</b>	<b>217</b>	<b>-86.6%</b>	<b>-77.8%</b>
Interest	(335)	(337)	(338)	(271)	(252)	-24.9%	-6.9%
Other income	415	714	403	334	544	31.0%	62.7%
Exceptional	(19)	1	3	(8)	(4)	-80.3%	-54.3%
<b>Profit before tax</b>	<b>1,680</b>	<b>1,490</b>	<b>1,364</b>	<b>1,035</b>	<b>506</b>	<b>-69.9%</b>	<b>-51.2%</b>
Tax	(566)	(468)	(424)	(468)	(475)	-16.1%	1.4%
Net profit after tax	1,114	1,022	941	567	31	-97.2%	-94.6%
Minority interest	(89)	(39)	(16)	(15)	(8)	-90.7%	-45.0%
<b>Adjusted net profit after tax</b>	<b>1,025</b>	<b>983</b>	<b>925</b>	<b>552</b>	<b>23</b>	<b>-97.8%</b>	<b>-95.9%</b>
EBITDA margin	16.0%	20.1%	22.1%	20.9%	5.4%	-10.6%	-15.4%
PAT margin	9.7%	16.5%	14.8%	10.7%	0.3%	-9.4%	-10.4%
Tax rate	33.7%	31.4%	31.0%	45.2%	93.9%	60.2%	48.7%
<b>Segment revenue</b>							
--Real estate	9,084	5,039	5,055	4,076	5,402	-40.5%	32.5%
--Construction	77	0	2	60	-	-100.0%	-100.0%
--Consultancy	263	176	155	195	336	27.7%	72.3%
--Hospitality	38	48	30	96	74	96.0%	-23.2%
--Electrical	629	259	503	278	969	54.1%	249.0%
--Others	452	436	516	435	381	-15.9%	-12.5%
Total	10,542	5,958	6,261	5,139	7,161	-32.1%	39.3%
<b>Segment EBIT margin</b>							
--Real estate	17.2%	26.1%	30.2%	27.0%	17.1%	-0.1%	-3.2%
--Construction	94.9%	-1200.0%	-156.5%	61.4%	NA	NA	218.0%
--Consultancy	100.0%	100.0%	100.0%	100.0%	100.0%	0.0%	0.0%
--Hospitality	-49.9%	17.1%	-35.8%	-5.2%	-49.3%	0.6%	30.6%
--Electrical	4.1%	11.0%	7.1%	15.9%	2.9%	-1.2%	8.8%
--Others	9.4%	12.8%	14.0%	14.0%	7.1%	-2.3%	0.1%
Total	18.4%	26.5%	28.4%	27.9%	17.1%	-1.3%	-0.5%

Source: Company data

Figure 3: Quarterly operational data trend

Area sold (mn sq ft)	Q2 FY11	Q3 FY11	Q4 FY11	Q1 FY12	Q2 FY12	Q3 FY12	Q4 FY12
Residential	1.44	1.76	1.80	1.66	1.56	1.44	1.68
Commercial	0.54	0.44	0.17	0.24	0.24	0.25	0.11
<b>Total</b>	<b>1.98</b>	<b>2.20</b>	<b>1.97</b>	<b>1.90</b>	<b>1.80</b>	<b>1.69</b>	<b>1.79</b>
<b>Pricing (INR psf)</b>							
Residential	4,757	4,557	4,341	4,360	5,385	4,729	3,863
Commercial	6,093	5,318	6,585	12,293	9,500	10,400	11,818
<b>Total</b>	<b>5,121</b>	<b>4,709</b>	<b>4,954</b>	<b>5,368</b>	<b>5,933</b>	<b>5,568</b>	<b>4,352</b>
<b>Cont value (INR m)</b>							
Residential	6,850	8,020	8,310	7,250	8,400	6810	6,490
Commercial	3,290	2,340	1,450	2,950	2,280	2600	1,300
<b>Total</b>	<b>10,140</b>	<b>10,360</b>	<b>9,760</b>	<b>10,200</b>	<b>10,680</b>	<b>9,410</b>	<b>7,790</b>

Source: Company data

Figure 4: Geography-wise volume trend

New launches (mn sq ft)	Q1 FY11	Q2 FY11	Q3 FY11	Q4 FY11	Q1 FY12	Q2 FY12	Q3 FY12	Q4 FY12
Mumbai	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Gurgaon	1.5	0.6	0.5	1.4	0.3	1.2	0.6	0.1
Noida + G Noida	0.8	0.4	0.8	0.2	0.5	0.6	0.0	0.5
Chennai	0.2	0.9	0.0	0.3	1.4	0.4	0.0	0.0
Kolkata	0.2	0.0	0.0	1.1	0.0	0.0	0.0	0.0
Others	0.1	0.0	0.4	1.3	1.0	0.6	0.6	0.1
<b>Total</b>	<b>2.8</b>	<b>1.8</b>	<b>1.6</b>	<b>4.3</b>	<b>3.2</b>	<b>2.8</b>	<b>1.2</b>	<b>0.6</b>
Area sold (M sq ft)	Q1 FY11	Q2 FY11	Q3 FY11	Q4 FY11	Q1 FY12	Q2 FY12	Q3 FY12	Q4 FY12
Mumbai	-	-	-	-	-	-	-	0.0
Gurgaon	1.4	1.2	1.0	0.8	0.5	0.9	0.7	0.3
Noida +G Noida	0.7	0.4	0.5	0.3	0.2	0.1	0.4	1.0
Chennai	0.4	0.1	0.2	0.3	0.6	0.4	0.1	0.1
Kolkata	0.3	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Others	0.2	0.1	0.3	0.4	0.5	0.3	0.3	0.3
<b>Total</b>	<b>3.0</b>	<b>2.0</b>	<b>2.2</b>	<b>2.0</b>	<b>1.9</b>	<b>1.8</b>	<b>1.7</b>	<b>1.8</b>
Cumulative area sold	Q1 FY11	Q2 FY11	Q3 FY11	Q4 FY11	Q1 FY12	Q2 FY12	Q3 FY12	Q4 FY12
Mumbai	86%	86%	86%	86%	86%	86%	86%	86%
Gurgaon	86%	92%	97%	93%	94%	92%	94%	94%
Noida +G Noida	50%	52%	53%	55%	54%	52%	56%	64%
Chennai	86%	68%	75%	77%	68%	70%	73%	74%
Kolkata	32%	40%	48%	39%	43%	47%	51%	55%
Others	43%	47%	50%	45%	46%	46%	45%	49%
<b>Total</b>	<b>67%</b>	<b>70%</b>	<b>73%</b>	<b>70%</b>	<b>69%</b>	<b>69%</b>	<b>71%</b>	<b>74%</b>

Source: Company data

## Cut earnings by 18-20% over FY13-14e

A combination of lower volume estimates (10-15% change over FY13-14) and weak EBITDA margins has led us to cut our earnings forecasts by 18% in FY13 and 20% in FY14. Our revised forecasts are 8-10% below consensus over FY13-14.

Figure 5 : Unitech earnings estimate changes (INRm)

	FY13e	FY14e
Sales – revised	34,273	41,444
Change	-9.1%	-9.4%
EBITDA – revised	25.3%	26.7%
Change	-0.8%	-0.6%
HSBC PAT – revised	4,928	6,177
Change	-17.8%	-19.7%
HSBC PAT relative to consensus	-8.3%	-10.2%
Sales volumes (mn sq ft)	9.5	11.0
Change	-9.5%	-15.4%

Source: HSBC estimates

## Valuation and risks

### Investment summary

A spate of weak quarterly results (five quarters in a row) has lowered visibility on core operating performance. We believe the operating margin structure on Unitech's development projects is far lower than warranted, despite consistent selling price inflation in the market. This, coupled with potential pressure on new sales volumes in a weak operating environment and a delayed execution cycle (12-18 months across project categories), exerts pressure on earnings and valuation. We expect Unitech to report a modest c3% earnings CAGR over FY11-14. We look forward to seeing management's focus on the core real estate business improving after the 2G spectrum issue court trials are over. This, in our view, could act as a share price catalyst over the next 12-18 months.

### Retain UW (V) with a revised target price of INR20 (INR25 earlier)

We lower our target price to INR20 (INR25 earlier), which is primarily driven our revised lower earnings forecasts and our increased NAV discount. We now value Unitech at a 60% discount (53% discount before) to its FY13e net asset value (NAV) of INR51. At a 60% NAV discount, Unitech is valued at the high end of the NAV discount range of 20-60% for its peer group. We do not include the value of its telecom business in our target valuation, as we foresee limited visibility on the monetisation of Unitech's stake in the business. A combination of weak earnings, a deteriorating business environment and the lack of share price catalysts suggests that Unitech may continue to trade at a lower valuation multiple.

Figure 6: Unitech valuation table

	New		Old
	INR bn	Per share (INR)	per share (INR)
Projects NAV	166	63	69
UCP	9	4	4
Amusement park	4	2	2
Hospitality/ Facility management/ Industrial parks	5	2	2
Transmission towers/construction/others	2	1	1
<b>Gross NAV</b>	<b>187</b>	<b>72</b>	<b>77</b>
Less: Net debt	(37)	(14)	(19)
Less: O/S land and statutory payments	(18)	(7)	(7)
Net asset value (real estate)	132	51	52
<b>Net asset value (Unitech group)</b>	<b>132</b>	<b>51</b>	<b>52</b>
<b>Less: NAV discount</b>	<b>(79)</b>	<b>(30)</b>	<b>(27)</b>
Target value	53	20	25

Source: HSBC estimates

### Ratings rationale

Under our research model, for stocks with a volatility indicator, the Neutral band is 10ppts above and below the hurdle rate for India stocks of 11%. Our new INR20 target price for Unitech (previously INR25) implies a potential return of -6.6% (including a forecast dividend yield of 0.6%), below the Neutral band; therefore, we retain our Underweight(V) rating. Potential return equals the percentage difference between the current share price and the target price, including the forecast dividend yield when indicated.

### Risks to our investment view

- ▶ The key upside risk is better-than-estimated execution improving its cash flow cycle.
- ▶ The key downside risk is the 2G spectrum allocation issue becoming protracted, which will likely distract management's focus.

# Disclosure appendix

## Analyst Certification

The following analyst(s), economist(s), and/or strategist(s) who is(are) primarily responsible for this report, certifies(y) that the opinion(s) on the subject security(ies) or issuer(s) and/or any other views or forecasts expressed herein accurately reflect their personal view(s) and that no part of their compensation was, is or will be directly or indirectly related to the specific recommendation(s) or views contained in this research report: Ashutosh Narkar

## Important disclosures

### Stock ratings and basis for financial analysis

HSBC believes that investors utilise various disciplines and investment horizons when making investment decisions, which depend largely on individual circumstances such as the investor's existing holdings, risk tolerance and other considerations. Given these differences, HSBC has two principal aims in its equity research: 1) to identify long-term investment opportunities based on particular themes or ideas that may affect the future earnings or cash flows of companies on a 12 month time horizon; and 2) from time to time to identify short-term investment opportunities that are derived from fundamental, quantitative, technical or event-driven techniques on a 0-3 month time horizon and which may differ from our long-term investment rating. HSBC has assigned ratings for its long-term investment opportunities as described below.

This report addresses only the long-term investment opportunities of the companies referred to in the report. As and when HSBC publishes a short-term trading idea the stocks to which these relate are identified on the website at [www.hsbcnet.com/research](http://www.hsbcnet.com/research). Details of these short-term investment opportunities can be found under the Reports section of this website.

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## Rating definitions for long-term investment opportunities

### Stock ratings

HSBC assigns ratings to its stocks in this sector on the following basis:

For each stock we set a required rate of return calculated from the cost of equity for that stock's domestic or, as appropriate, regional market established by our strategy team. The price target for a stock represents the value the analyst expects the stock to reach over our performance horizon. The performance horizon is 12 months. For a stock to be classified as Overweight, the potential return, which equals the percentage difference between the current share price and the target price, including the forecast dividend yield when indicated, must exceed the required return by at least 5 percentage points over the next 12 months (or 10 percentage points for a stock classified as Volatile\*). For a stock to be classified as Underweight, the stock must be expected to underperform its required return by at least 5 percentage points over the next 12 months (or 10 percentage points for a stock classified as Volatile\*). Stocks between these bands are classified as Neutral.

Our ratings are re-calibrated against these bands at the time of any 'material change' (initiation of coverage, change of volatility status or change in price target). Notwithstanding this, and although ratings are subject to ongoing management review, expected returns will be permitted to move outside the bands as a result of normal share price fluctuations without necessarily triggering a rating change.

\*A stock will be classified as volatile if its historical volatility has exceeded 40%, if the stock has been listed for less than 12 months (unless it is in an industry or sector where volatility is low) or if the analyst expects significant volatility. However, stocks which we do not consider volatile may in fact also behave in such a way. Historical volatility is defined as the past month's average of the daily 365-day moving average volatilities. In order to avoid misleadingly frequent changes in rating, however, volatility has to move 2.5 percentage points past the 40% benchmark in either direction for a stock's status to change.

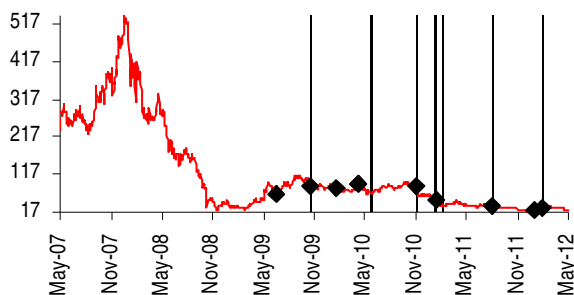
## Rating distribution for long-term investment opportunities

As of 16 May 2012, the distribution of all ratings published is as follows:

<b>Overweight (Buy)</b>	48%	(26% of these provided with Investment Banking Services)
<b>Neutral (Hold)</b>	38%	(25% of these provided with Investment Banking Services)
<b>Underweight (Sell)</b>	14%	(16% of these provided with Investment Banking Services)

## Share price and rating changes for long-term investment opportunities

Unitech Ltd (UNTE.BO) Share Price performance INR Vs HSBC rating history



Source: HSBC

Recommendation & price target history

From	To	Date
Underweight (V)	Neutral (V)	02 November 2009
Neutral (V)	Overweight (V)	01 June 2010
Overweight (V)	Neutral (V)	15 November 2010
Neutral (V)	Underweight (V)	24 January 2011
Underweight (V)	Overweight (V)	15 February 2011
Overweight (V)	Neutral (V)	15 August 2011
Neutral (V)	Underweight (V)	15 February 2012
Target Price	Value	Date
Price 1	65.00	29 June 2009
Price 2	85.00	02 November 2009
Price 3	83.00	01 February 2010
Price 4	91.00	19 April 2010
Price 5	94.00	22 April 2010
Price 6	87.00	15 November 2010
Price 7	50.00	24 January 2011
Price 8	31.00	15 August 2011
Price 9	24.00	15 January 2012
Price 10	25.00	15 February 2012

Source: HSBC

## HSBC & Analyst disclosures

### Disclosure checklist

Company	Ticker	Recent price	Price Date	Disclosure
UNITECH LTD	UNTE.BO	19.95	15-May-2012	4

Source: HSBC

- 1 HSBC\* has managed or co-managed a public offering of securities for this company within the past 12 months.
- 2 HSBC expects to receive or intends to seek compensation for investment banking services from this company in the next 3 months.
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**Issuer of report**

**HSBC Securities and Capital Markets (India) Private Limited**

Registered Office

52/60 Mahatma Gandhi Road

Fort, Mumbai 400 001, India

Telephone: +91 22 2267 4921

Fax: +91 22 2263 1983

Website: [www.research.hsbc.com](http://www.research.hsbc.com)

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