HCC

30 April 2012

Reuters: HCNS.BO; Bloomberg: HCC IN

4QFY12 Result Update

Balance Sheet Strain, Slower Project Execution

HCC reported a net loss for 4QFY12, for the third consecutive quarter, at Rs542mn, which was above our/Bloomberg consensus estimates of a loss of Rs154mn and Rs183mn, respectively, following a decline in net sales, subdued performance at the operating level and surge in interest costs. We believe project execution would continue to be slow because of higher debt, increased working capital requirement and lack of order inflow, which will impact future growth and profitability. However, the likely approval to the CDR (corporate debt restructuring) package will ease the financial strain and the company may improve its performance going ahead. We maintain our Sell rating on HCC with a revised target price of Rs16 (from Rs17 earlier).

Change in earnings estimates: We have cut our earnings estimates for FY13 and introduced FY14 estimates. We cut net sales estimate by 14% for FY13E to factor in lower-than-expected revenue traction and expect 6.5% YoY growth in FY14E. We have tweaked our EBITDA margin from 12.5% to 11.2% for FY13E and expect 11.6% for FY14E because of negative operating leverage in the wake of slower growth. Subsequently, we expect a net loss of Rs540mn for FY13E (from net profit estimate of Rs47mn earlier) and a net profit of Rs317mn for FY14E.

Strain on the bottom-line continues: Net sales fell 3.9% to Rs11.56bn because of sluggish project execution run-rate in the wake of higher leverage. EBITDA tumbled by 47% to Rs881mn (34% lower than our estimate) and EBITDA margin got squeezed by 630bps to 7.6% (lowest in the past six years) due to decline in revenue and also some of the projects not crossing the threshold limit for booking revenue, but were included in costs. Interest costs increased 67% YoY to Rs1.5bn due to higher debt burden and rising interest rates (currently, average interest rate at 12.5%) as well as the change in accounting methodology, which disallows net out of interest receipts for computing interest costs. Other income rose 100% YoY to Rs269mn, driven by interest income. Decline in revenue, lower performance at the operating level and high interest costs led the company to report a net loss of Rs542mn for the quarter.

Valuation: HCC's balance sheet would continue to be under strain because of higher debt level, thereby restraining the growth of its core business, and the company would report a net loss even in FY13. Meanwhile, the likely nod to its CDR package will ease short-term cash flow, thereby improving project execution. However, we believe HCC would take some time to come out of its problems. Following the earnings downgrade, we have revised our TP from Rs17 to Rs16 and retained our Sell rating on HCC.

SELL

Sector: Infrastructure

CMP: Rs20

Target Price: Rs16

Downside: 20%

Amit Srivastava
amit.srivastava@nirmalbang.com
+91-22-3926 8116

Nitin Arora
nitin.arora@nirmalbang.com
+91-22-3926 8169

Key Data

Current Shares O/S (mn)	606.6
Mkt Cap (Rsbn/US$mn)	12.3/233.8
52 Wk H / L (Rs)	36/16
Daily Vol. (3M NSE Avg.)	5,502,332

Price Performance (%)

	1 M	6 M	1 Yr
HCC	(21.2)	(31.0)	(42.6)
Nifty Index	(1.6)	(2.2)	(9.4)

Source: Bloomberg

Y/E March (Rsmn)	4QFY11	3QFY12	4QFY12	YoY (%)	QoQ (%)	FY11	FY12	YoY (%)
Net sales	12,026	9,476	11,559	*(3.9)*	*22.0*	40,932	39,915	*(2.5)*
Consumption of raw materials	3,309	2,775	2,722	*(17.7)*	*(1.9)*	12,217	10,897	*(10.8)*
Construction expenses	5,270	4,260	6,557	*24.4*	*53.9*	16,749	18,761	*12.0*
Employee costs	1,188	1,092	1,019	*(14.3)*	*(6.7)*	4,676	4,393	*(6.1)*
Other expenditure	592	228	381	*(35.7)*	*66.9*	1,892	1,435	*(24.1)*
Total expenses	10,359	8,356	10,678	*3.1*	*27.8*	35,534	35,485	*(0.1)*
EBITDA	1,667	1,120	881	*(47.1)*	*(21.3)*	5,398	4,429	*(17.9)*
EBITDAM (%)	*13.9*	*11.8*	*7.6*	-	-	*13.2*	*11.1*	-
Other income	134	154	269	*100.1*	*74.1*	145	1,102	*660.6*
Interest costs	903	1,043	1,509	*67.2*	*44.7*	2,899	5,431	*87.4*
Depreciation	440	412	402	*(8.5)*	*(2.5)*	1,527	1,621	*6.2*
PBT	459	(181)	(762)	*(266.0)*	*320.5*	1,117	(1,522)	*(236.3)*
Tax	228	(609)	(210)	*(192.3)*	*(65.4)*	406.7	(962.3)	*(336.6)*
APAT	231	427	(551)	*(338.8)*	*(229.0)*	710	(559)	*(178.8)*
RPAT (Incl. exceptional item)	231	(1,304)	(542)	*(334.6)*	*(58.5)*	710	(2,222)	*(413.1)*

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 1: Financial summary

Y/E March (Rsmn)	FY10	FY11	FY12E	FY13E	FY14E
Net sales	36,442	40,932	39,915	41,662	44,381
EBITDA	4,429	5,398	4,429	4,667	5,127
Adj. net profit	815	710	(559)	(540)	317
Adj. EPS	0.9	1.2	(3.7)	(0.9)	0.5
EPS growth (%)	*(58.6)*	*36.8*	*(413.1)*	*NA*	*NA*
EBITDAM (%)	*12.2*	*13.2*	*11.1*	*11.2*	*11.6*
NPM (%)	*2.2*	*1.7*	*(1.4)*	*(1.3)*	*0.69*
PER (X)	12.3	17.9	(5.7)	(23.6)	40.2
P/BV (x)	0.4	0.8	1.0	1.0	1.0
Price/sales (x)	0.2	0.3	0.3	0.3	0.3
RoCE (%)	*11.6*	*11.6*	*8.0*	*8.0*	*9.1*
RoE (%)	*4.1*	*4.7*	*NA*	*NA*	*2.5*

Source: Company, Nirmal Bang Institutional Equities Research

Key highlights

- The company's final debt restructuring proposal is under consideration by a consortium of five banks and it expects to get the approval in the next 30-35 days. The total amount under the CDR package is Rs33bn and the company has asked for a two-year moratorium and an eight-year period for repayment of debt. We believe the approval to the CDR package would be a big relief for the company.

- The company's order book stood at Rs153bn (3.7x FY12 revenue), which excludes the L1 contract worth Rs17.1bn. In FY12, the company secured orders worth Rs18.9bn, declined 45% YoY. Major orders won by the company include Tehri pumped storage project in Uttaranchal, Limbdi branch canal project in Gujarat and Bogibeeel bridge superstructure project in Assam. The management expects closing order book position of Rs170bn in FY13E, which implies order inflow of Rs61bn during the year. We have factored in flat closing order book for FY13E.

- In FY12, standalone debt increased 24% YoY to Rs43bn (working capital loan of Rs10bn and term loan of Rs33bn). Average interest cost of debt was 12.5%. The company was able to realise claims worth Rs2.03bn and received an arbitration award worth Rs2.56 bn. The company laid more stress on settling the claims to reduce debt.

- The company expects BOT projects to contribute revenue worth Rs2bn in FY13E and Rs3.0-3.5bn in FY14E.

- For FY12, the Lavasa project reported revenue of Rs753mn, down 86% YoY, and reported a loss of Rs1.37bn as against a profit of Rs1.11bn in FY11. The company launched pre-sales for its second town Mugaon which was sold out in fortnight of launch and 95% of its first town Dasve is already sold out. The management intends to go for a capex of Rs8bn in FY13, which would be funded by banks (banks have agreed to lend additional funds worth Rs6bn) and inflow through new sales, which would bring the growth back on track. The total debt of Lavasa stood at Rs22bn. Interest payment span exceeded by 90 days on a sum of Rs7.5bn, while the rest of the debt is being serviced in a time-bound manner.

- Karl Steiner reported order book of Rs82.8bn (2xFY12 revenue) and order inflow for the year stood at Rs65.87bn.

Exhibit 2: Change in earnings estimates

	FY13E		
Rsmn	Earlier estimates	New estimates	*Change (%)*
Net sales	48,404	41,662	*(14)*
EBITDA	6,075	4,667	*(23)*
Adj. PAT	47	(540)	*NA*

Source: Company, Nirmal Bang Institutional Equities Research

Ratings track

Date	Rating	Market price (Rs)	Target price (Rs)
26 September 2011	Hold	29	33
17 October 2011	Hold	27	31
24 October 2011	Sell	27	26
18 November 2011	Hold	23	26
12 January 2012	Hold	20	22
23 January 2012	Sell	21	17
10 April 2012	Sell	25	17

Disclaimer

Stock Ratings Absolute Returns

BUY > 15%

HOLD 0-15%

SELL < 0%

This report is published by Nirmal Bang's Institutional Equities Research desk. Nirmal Bang has other business units with independent research teams separated by Chinese walls, and therefore may, at times, have different or contrary views on stocks and markets. This report is for the personal information of the authorised recipient and is not for public distribution. This should not be reproduced or redistributed to any other person or in any form. This report is for the general information for the clients of Nirmal Bang Equities Pvt. Ltd., a division of Nirmal Bang, and should not be construed as an offer or solicitation of an offer to buy/sell any securities.

We have exercised due diligence in checking the correctness and authenticity of the information contained herein, so far as it relates to current and historical information, but do not guarantee its accuracy or completeness. The opinions expressed are our current opinions as of the date appearing in the material and may be subject to change from time to time without notice.

Nirmal Bang or any persons connected with it do not accept any liability arising from the use of this document or the information contained therein. The recipients of this material should rely on their own judgment and take their own professional advice before acting on this information. Nirmal Bang or any of its connected persons including its directors or subsidiaries or associates or employees or agents shall not be in any way responsible for any loss or damage that may arise to any person/s from any inadvertent error in the information contained, views and opinions expressed in this publication.

Team Details:

Name		Email Id	Direct Line
Rahul Arora	CEO	rahul.arora@nirmalbang.com	+91 22 3926 8098 / 99
Hemindra Hazari	Head of Research	hemindra.hazari@nirmalbang.com	+91 22 3926 8017 / 18
Sales and Dealing:			
Neha Grover	AVP Sales	neha.grover@nirmalbang.com	+91 22 3926 8093
Ravi Jagtiani	Dealing Desk	ravi.jagtiani@nirmalbang.com	+91 22 3926 8230, +91 22 6636 8832
Sudhindar Rao	Dealing Desk	sudhindar.rao@nirmalbang.com	+91 22 3926 8229
Pradeep Kasat	Dealing Desk	pradeep.kasat@nirmalbang.com	+91 22 3926 8102/8103, +91 22 6636 8831
Michael Pillai	Dealing Desk	michael.pillai@nirmalbang.com	+91 22 3926 8100/8101, +91 22 6636 8830

Nirmal Bang Equities Pvt. Ltd.

Correspondence Address
B-2, 301/302, Marathon Innova,
Nr. Peninsula Corporate Park
Lower Parel (W), Mumbai-400013.
Board No. : 91 22 3926 8000/1
Fax. : 022 3926 8010