Q2FY10 RESULT UPDATE

CONSTRUCTION

Punj Lloyd

SELL

Price	Rs 260
Target Price	**% Downside**
Rs 240	12%↓

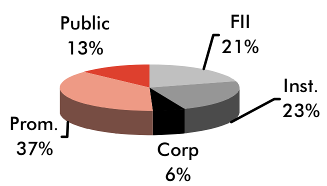
Market Capitalisation	
Rs26,445mn	(US$1,858mn)
52 wk range H/L (Rs)	299/67
Shares o/s (mn)	**Daily vol (mn shares)**
331.78	7.05
Reuters	**Bloomberg**
PUJL.BO	PUNJ IN

Performance (%)

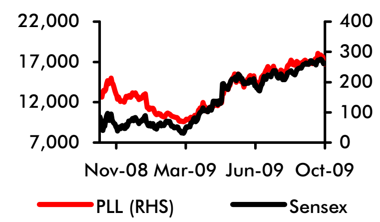
	1M	3M	12M	YTD
Absolute	0.5	3.7	73.4	77.2
Sensex	(0.2)	(5.2)	(10.2)	1.7

Source: Bloomberg

Shareholding pattern



Price performance



Source: Capitaline

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AMBIT Acumen at work

Write-off blues cloud upsides

- Simon Carves Rs1040mn (13.5mn Gbp) write off during Q2FY10 raises questions on margins stability and profit guidance. Partial recovery of claims seems possible.
- Margins surprise for H1FY10 impacted by cost overruns, further 16mn Gbp of liquidated damages claims by Ensus UK could dampen stock performance
- We recommend 'SELL' on the stock with a Rs240 target price, robust order book doesn't warrant a multiple re-rating at this juncture

The following are the key takeaways of Q2FY10 performance

- PLL Q2FY10 performance was below our and consensus expectations.
- Profitability again marred by cost overruns, one more quarter of pain possible until the entire Simon Carves project gets commissioned.
- Slow moving Libya orders dampen execution, revenue growth expected to pick up in H2FY10.

Stock to under-perform on the back of write off-blues

We recommend 'SELL' on the stock with a SOTP-based target price of Rs240 (PLL valued at Rs223 based on 12xFY11E earnings (earlier 14x) in line with mid-tier construction companies forward multiple, Pipavav Shipyard at Rs17 (20% discount to market cap for Punj Lloyd stake)). PLL robust order book doesn't warrant a multiple re-rating and we believe that project execution and order book quality may surprise negatively.

Key Risks

(a)Margins surprise as seen during H1FY10 excluding Simon Carves b) Favorable negotiation terms with Ensus UK for cost overrun recovery c) Currency risk

Exhibit 1: Key Financials - consolidated entity

YE March (Rs mn)	FY08	FY09E	FY10E	FY11E
Operating income	77,529	119,120	127,781	161,338
EBITDA	6,923	3,093	9,389	14,393
Net profit	3,583	(2,377)	2,901	6,025
EPS (Rs)	10.6	(8.3)	8.8	18.2
RoE (%)	16.1	(9.7)	9.8	16.2
RoCE (%)	14.8	2.5	11.1	16.0
P/E (x)	24.6	-31.2	29.7	14.3

Source: Company, Ambit Capital Research Estimates **adjusted for Rs2070mn SABIC write - off*

Q2FY10 Performance

1) PLL reported revenue of Rs 28716mn against our expectation of Rs 32313mn a variation of (11%), while EBIDTA and PAT numbers where 28% and 63% below estimates. The main reason behind the gross underperformance was Rs 1040mn cost overuns in Simon Carves - Wilton Teeside - Ensus UK Plant (13.5mn GBP). The plant is expected to be commissioned by Dec-09. There is a potential of a 16mn Gbp further write off in case Ensus UK seeks liquidated dama ges claims. We have written off this amount Rs1240mn in our FY10E numbers.

Exhibit 2 : Performance Q2FY10

Rs mn	Q2FY10 Estimate	Q2FY10 Actual	% Variation
Sales	32313	28717	(11.1)
EBIDTA	2957	2120	(28.3)
Net Profit	1451	528	(63.6)

Source: Ambit Capital research

2) The company is currently negotiating with Ensus UK to get into a Product sharing agreement and expects to reach a conclusive decision, the modality being worked out is - for the next 2 years Punj Lloyd will get paybacks for the 13.5mn GBP (Rs1040mn) write down taken this quarter. Punj Lloyd expects to get 5mn GBP minimum to 22mn GBP maximum (in case plant runs at 100%). Though the recovery of entire 13.5mn GBP looks remote.

3) Excluding this write off company would have reported Rs3160mn EBIDTA and Rs1260mn PAT. With this cost overun Simon Carves legacy order book comes to an end. The last contract with Gulf Flour has been taken over by Punj lloyd now.

4) Current order book is Rs268bn. Company expects to win some new projects in middle -east in near term also ONGC bids for B-193 are expected to open.

Key positive triggers in near term

- Macro-enviroment in Middle-East is improving and this had resulted in robust order awards during the last Quarters , Notably the larger ones are $24bn order announced in July-09 . Abu Dhabi is planning to award $10bn awards by the end of the year. Upstream projects which had become non-viable due to lower crude prices are being revived again about 40projects. Oct-09 was the Ramzan month so order awards were muted , going forward in H2FY10 more robust ordering activity is expected. This augers well for Punj Lloyd as Mid-stream and Downstream orders are derivatives of Upstream orders and 80% of order book for Punj is from International Segment.
- Some of the projects where the company would have recieved LOI but were deferred, would come up for awards again. Notably we believe that these would be in Infra, Hydrocarbons and Renewable Energy segment .
- With these triggers in place we believe that order book traction would continue as the business model is de-risked Geographically and Segmentally.

Key financials - Consolidated

Exhibit 3: Balance Sheet

Year to March (Rs mn)	FY08	FY09	FY10E	FY11E
Cash & equivalents	6,898	8,122	4,044	4,471
Debtors	20,901	26,686	42,010	53,043
Inventory	20,592	36,686	38,509	48,622
Loans & advances	7,429	11,461	10,903	13,766
Investments	5,458	6,609	6,609	6,609
Fixed assets	16,233	21,727	22,633	24,020
Other assets	(915)	(1,482)	(848)	(848)
Total assets	76,596	109,809	123,859	149,683
Current liabilities & provisions	32,869	48,952	53,231	67,216
Debt	16,326	35,592	35,900	42,000
Minority Interest	222	420	420	420
Total liabilities	49,417	84,964	89,551	109,636
Shareholders' equity	607	607	663	663
Reserves & surpluses	26,572	24,238	33,646	39,384
Total networth	27,179	24,845	34,309	40,047
Net working capital	9,875	9,828	12,311	10,024
Net debt (cash)	9,428	27,470	31,856	37,529
Total liabilities & equities	76,596	109,809	123,859	149,683

Exhibit 4: Income Statement

Year to March (Rs mn)	FY08	FY09	FY10E	FY11E
Operating income	77,529	119,120	127,781	161,338
% growth	51.2%	53.6%	7.3%	26.3%
Operating expenditure	70,606	116,028	118,391	146,944
EBITDA	6,923	3,093	9,389	14,393
% growth	68.7%	-55.3%	203.6%	53.3%
Depreciation	1,462.3	1,770.7	2,094.6	2,112.6
EBIT	5,461	1,322	7,295	12,281
Interest expenditure	1,806	2,208	3,345	4,006
Non-operational income	1,182	899	250	450
PBT	4,836	13	4,199	8,725
Tax	1,235	2,260	1,302	2,705
Minority/profit assc.	18.3	(130.3)	4.0	5.0
PAT / Net profit	3,583	(2,377)	2,901	6,025
% growth	81.8%	-166.3%	-222.1%	107.7%

*adjusted for Rs2070mn SABIC write - off

Source: Company, Ambit Capital Research Estimates

Key financials - Consolidated

Exhibit 5: Cash Flow Statement

Year to March (Rs mn)	FY08	FY09	FY10E	FY11E
EBIT	5,461	1,322	7,295	12,281
Other income (expenditure)	811	745	250	450
Depreciation	1,462	1,771	2,095	2,113
Interest	1,806	2,208	3,345	4,006
Tax	1,235	2,260	1,302	2,705
Others	1,032			
Net working capital	9,875	9,828	12,311	10,024
Cash flow from operating activities	(5,183)	(10,458)	(7,319)	(1,891)
Capital expenditure	3,139	6,543	3,000	3,500
Others	449	629	0	0
Investments	3,759	1,151	0	0
Cash flow from investing activities	(7,348)	(8,323)	(3,000)	(3,500)
Incr (decr) in borrowings	(242)	19,900	(326)	6,100
Issuance of equity	11,046	0	6,702	0
Net dividends	142	(105)	136	282
Others	(1,261)			
Cash flow from financing activities	9,402	20,005	6,240	5,818
Net change in cash	(3,129)	1,224	(4,078)	427
Closing cash balance	6,898	8,122	4,044	4,471

Exhibit 6: Ratio Analysis

Year to March (%)	FY08	FY09	FY10E	FY11E
EBITDA margin (%)	8.9	2.6	7.3	8.9
EBIT margin	7.0	1.1	5.7	7.6
PAT Margin (%)	4.6	(2.0)	2.3	3.7
Return on capital employed	14.8	2.5	11.1	16.0
Return on equity	16.1	(9.7)	9.8	16.2
Current ratio (x)	1.7	1.7	1.8	1.8

Exhibit 7: Valuation Parameters

Year to March (%)	FY08	FY09	FY10E	FY11E
EPS (Rs)	10.6	(8.3)	8.8	18.2
Diluted EPS (Rs)	10.6	(8.3)	8.8	18.2
Book value per share (Rs)	89.6	81.9	113.1	132.0
P/E (x)	24.6	(31.2)	29.7	14.3
P/BV (x)	2.9	3.2	2.3	2.0
EV/EBITDA (x)	16.2	36.2	11.9	7.8
EV/Sales (x)	1.3	0.8	0.8	0.7

**adjusted for Rs2070mn SABIC write - off*

Source: Company, Ambit Capital Research Estimates

Explanation of Investment Rating

Investment Rating	Expected return (over 12-Month period from date of initial rating)
Buy	>15%
Hold	5% to 15%
Sell	<5%

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