

DILIP BUILDCON

ENGINEERING

BUY

Target Price: Rs 385

On the right track

We spent 2 days with the top management of Dilip Buildcon (DBL) during the investor day and site visit to understand its unique business model and medium-term strategy.

Key takeaways: (1) As guided in Q3 call, on-track to monetize BOT/HAM projects by end Q1FY18; (2) reduction in working capital driven by lower no. of project sites and increase in share of in-house BOT as well as mining revenue; (3) strong order backlog at Rs 164 bn gives visibility to FY17-19 revenue CAGR of ~20% and management reiterated restricting capex to only maintenance at Rs 1 bn pa.; (4) management reiterated FY18 revenue guidance of ~Rs 60 bn (~20% YoY) and slight increase in EBITDA margin driven by higher-margin mining business.

CMP : Rs 348
Potential Upside : 11%

MARKET DATA

No. of Shares : 137 mn
Free Float : 24%
Market Cap : Rs 48 bn
52-week High / Low : Rs 365 / Rs 179
Avg. Daily vol. (1mth) : 220,708 shares
Bloomberg Code : DBL IB Equity
Promoters Holding : 76%
FII / DII : 15% / 3%

Clear strategy for BOT assets: Equity commitment of Rs 9 bn with Rs 2.5 bn pa over FY17-19. Management highlighted that change in the mix of road awards towards Hybrid Annuity (HAM) vs. EPC earlier is driving it to take HAM projects. However, it has a clear strategy of churning the existing assets as well as selling the HAM assets on commissioning.

On track to lower inventory/ working capital cycle: During FY18, sites under execution would halve to ~25, which will bring inventory level down. Further, the mining segment would constitute ~15% of FY18E revenue. NWC in mining is ~30 days vs. NWC of the company at 155 days as of Dec'16.

Focusing on sweating assets to be debt free over next 3 years: Unlike other EPC players, DBL owns a large fleet of equipment worth ~Rs 2.5 bn. Management believes that the current fleet can generate peak revenue of ~Rs 80 bn vs. ~Rs 50 bn currently. Hence, it plans to limit its capex to just maintenance at Rs 1 bn vs. ~Rs 4 bn pa over FY14-17.

Introduce FY19 estimates and raise TP; maintain BUY: We maintain FY17/18EPS at Rs 20/ Rs 28. We introduce our FY19 EPS at Rs 34. Our revised TP stands at Rs 385 (10x FY19E EPS + 1x book value of BOT assets) vs Rs 325 earlier.

Financial summary (Standalone)

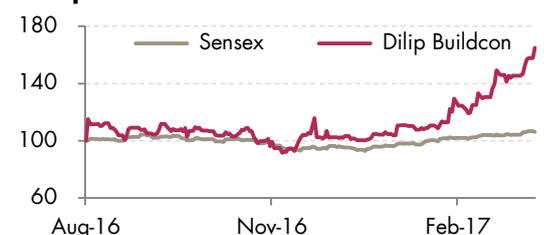
Y/E March	FY16	FY17E	FY18E	FY19E
Sales (Rs mn)	40,176	49,924	62,082	68,162
EBITDA (Rs mn)	7,992	9,606	11,325	12,419
Adj PAT (Rs mn)	2,199	2,760	3,845	4,642
EPS (Rs)	18.8	20.2	28.1	34.0
Change YOY (%)	50.8	7.5	39.3	20.7
P/E (x)	17.1	15.0	10.7	8.9
RoE (%)	22.3	19.0	19.3	19.2
EV/E (x)	8.9	7.2	6.0	5.4

Source: Company, Axis Capital

Key drivers (Rs bn)

	FY17E	FY18E	FY19E
Order inflow	85	85	102
Order backlog	143	165	199
Revenue growth	22.5%	24.4%	9.8%
Margin	19.2%	18.2%	18.2%

Price performance



Bidding selectively on strong visibility: Strong order book at ~Rs 164 bn (>3x TTM sales) lends comfort to the management to bid selectively. This coupled with rise in share of high-margin mining segment (>20% margin) lends visibility to EBITDA margin sustaining at 18%-20% in FY18.

Unique business model

Excellent execution track record: DBL has displayed excellent, quicker execution of projects across business segments and geographies. It has completed 58 EPC projects and 12 BOT projects till date. Of these, 47 (~70% of value) projects were completed ~150 days (average) ahead of the scheduled ~700 days (average).

Large, modern equipment bank worth ~Rs 25 bn and minimal sub-contracting ensure better control over execution and timely EPC services

- ◆ DBL owns a modern fleet of ~7,300 equipment, which includes high-end automated construction equipment such as stone crushers (for quarrying), bitumen and concrete plants, pavers, motor graders, excavators, tippers, etc.
- ◆ Homogenous machinery fleet e.g. bulk of excavators and motor graders are of CAT and pavers are from Writgen (Germany) etc. Homogenous fleet is easier to maintain and, maximizes efficiency

Exhibit 1: Vogele road paver on Guna-Biaora project



Source: Company, Axis Capital

Exhibit 2: Road rollers (Volvo and HAMM) at work



Source: Company, Axis Capital

Project selection: Bigger team (vs. peers) and more intense due diligence of projects before bidding for them (examining each hurdle thoroughly). Smaller project size (average size of Rs 2.5 bn) with large number of sites (65) lowers execution risk.

Robust systems and processes lend scalability to business

- ◆ 15+ functional heads for material procurement, project monitoring, equipment management, etc. based out of head office and delegated to take decisions. KRA of project manager (PM) at site is only to ensure road laying and getting work vetted by independent engineers appointed by client in stark contrast to peers where PM fire-fights a host of issues
- ◆ Strong operating systems and controls to monitor execution, e.g. its entire fleet has GPS devices, which help remote project monitoring and equipment utilization

Why DBL's inventory level is so high?

- ◆ DBL does negligible subcontracting vs. peers who sub-contract 20-40% of their projects and hence inventory is on sub-contractors' books
- ◆ DBL usually crushes aggregates (~25% of raw material) in the first 6-8 months of the project to be executed in 2-2.5 years
- ◆ DBL works on larger number of sites (~65) vs. 10-15 for peers and needs to maintain minimum level of inventory at every site

Exhibit 3: Quarry at the main site of Guna-Biaora project



Source: Company, Axis Capital

Exhibit 4: Inventory of aggregate at the main site



Source: Company, Axis Capital

Diversification into mining to reduce dependence on road: DBL has won ~Rs 32.5 bn of mining contracts during H1FY17. These contracts are principally for overburden removal from Coal India's subsidiaries. Execution risks are lower, as DBL does not need to acquire land or procure raw material or seek environment clearances for quarries. These are primarily deploying equipment and ferrying overburden to the nearest dump yard.

DBL expects revenue from mining at ~Rs 7-8 bn in FY18 and EBITDA margin of > 20%. The company has invested ~Rs 2bn towards procurement of equipment. Mining segment has zero inventories, and the company can raise bills every fortnight, resulting in NWC of 45-60 days vs. road segment at >135 days.

Mining segment order book of Rs 32.5 bn gives revenue visibility of ~Rs 7-8 bn pa over the next 3-5 years. Note: The company will depreciate the assets over 5 years towards the mining division. RoIC for mining is at ~50% vs. 20-25% for roads.

Clear strategy for BOT assets: Management highlighted that change in the mix of road awards towards Hybrid Annuity (HAM) vs. EPC earlier is driving the company to take HAM projects. However, it has a clear strategy of churning the existing assets as well as selling the BOT/HAM assets on commissioning.

DBL has 12 operational BOT projects with an overall equity investment of Rs 4.3 bn and debt of Rs 10.5 bn. These assets have generated revenue of Rs 2.37 bn (Rs 2.07 bn annuity + Rs 300 mn toll) in FY16. Company is targeting monetization of these operational BOT assets.

In addition, DBL has 7 under-construction BOT assets (1 Toll, 3 Hybrid Annuity and 4 Toll + Annuity), which would require equity investment of ~Rs 9 bn (over next 3 years, Rs 2.5 bn each in FY17/18), debt of ~Rs 25 bn and would be getting government grant of ~Rs 14 bn. Company has a clear strategy of monetizing these assets too once they are operational.

Exhibit 5: Raigarh dam project



Source: Company, Axis Capital

Exhibit 6: Raigarh dam project



Source: Company, Axis Capital

Profit & loss (Rs mn)

Y/E March	FY16	FY17E	FY18E	FY19E
Net sales	40,176	49,924	62,082	68,162
Other operating income	677	120	150	150
Total operating income	40,853	50,044	62,232	68,312
Cost of goods sold	(30,170)	(37,193)	(46,872)	(51,462)
Gross profit	10,683	12,851	15,360	16,850
<i>Gross margin (%)</i>	<i>26.6</i>	<i>25.7</i>	<i>24.7</i>	<i>24.7</i>
Total operating expenses	(2,691)	(3,245)	(4,035)	(4,431)
EBITDA	7,992	9,606	11,325	12,419
<i>EBITDA margin (%)</i>	<i>19.9</i>	<i>19.2</i>	<i>18.2</i>	<i>18.2</i>
Depreciation	(1,835)	(2,117)	(2,367)	(2,517)
EBIT	6,158	7,488	8,957	9,902
Net interest	(3,805)	(4,157)	(4,000)	(3,890)
Other income	154	162	170	178
Profit before tax	2,507	3,493	5,127	6,190
Total taxation	(308)	(734)	(1,282)	(1,547)
<i>Tax rate (%)</i>	<i>12.3</i>	<i>21.0</i>	<i>25.0</i>	<i>25.0</i>
Profit after tax	2,199	2,760	3,845	4,642
Minorities	-	-	-	-
Profit/ Loss associate co(s)	-	-	-	-
Adjusted net profit	2,199	2,760	3,845	4,642
<i>Adj. PAT margin (%)</i>	<i>5.5</i>	<i>5.5</i>	<i>6.2</i>	<i>6.8</i>
Net non-recurring items	-	-	-	-
Reported net profit	2,199	2,760	3,845	4,642

Balance sheet (Rs mn)

Y/E March	FY16	FY17E	FY18E	FY19E
Paid-up capital	1,171	1,367	1,367	1,367
Reserves & surplus	9,791	16,666	20,512	25,154
Net worth	10,962	18,034	21,879	26,521
Borrowing	25,138	24,138	23,138	22,138
Other non-current liabilities	965	965	965	965
Total liabilities	37,066	43,137	45,982	49,625
Gross fixed assets	19,424	22,924	24,424	25,924
Less: Depreciation	(5,220)	(7,337)	(9,704)	(12,222)
Net fixed assets	14,204	15,587	14,719	13,702
Add: Capital WIP	-	-	-	-
Total fixed assets	14,204	15,587	14,719	13,702
Total Investment	3,785	6,285	9,285	12,285
Inventory	15,803	19,833	22,962	25,211
Debtors	11,919	11,626	12,756	14,006
Cash & bank	1,476	2,938	2,639	2,405
Loans & advances	5,565	7,523	8,504	9,337
Current liabilities	16,267	21,337	25,734	28,254
Net current assets	19,077	21,266	21,979	23,638
Other non-current assets	-	-	-	-
Total assets	37,066	43,137	45,982	49,625

Source: Company, Axis Capital

Cash flow (Rs mn)

Y/E March	FY16	FY17E	FY18E	FY19E
Profit before tax	2,507	3,493	5,127	6,190
Depreciation & Amortisation	1,835	2,117	2,367	2,517
<i>Chg in working capital</i>	<i>(4,778)</i>	<i>(727)</i>	<i>(1,011)</i>	<i>(1,894)</i>
Cash flow from operations	3,060	8,306	9,202	9,156
<i>Capital expenditure</i>	<i>(4,126)</i>	<i>(3,500)</i>	<i>(1,500)</i>	<i>(1,500)</i>
Cash flow from investing	(7,463)	(10,157)	(8,500)	(8,390)
<i>Equity raised/ (repaid)</i>	<i>-</i>	<i>4,312</i>	<i>-</i>	<i>-</i>
<i>Debt raised/ (repaid)</i>	<i>3,269</i>	<i>(1,000)</i>	<i>(1,000)</i>	<i>(1,000)</i>
<i>Dividend paid</i>	<i>-</i>	<i>-</i>	<i>-</i>	<i>-</i>
Cash flow from financing	3,269	3,312	(1,000)	(1,000)
Net chg in cash	(1,134)	1,461	(298)	(234)

Key ratios

Y/E March	FY16	FY17E	FY18E	FY19E
OPERATIONAL				
FDEPS (Rs)	18.8	20.2	28.1	34.0
CEPS (Rs)	34.4	35.7	45.4	52.4
DPS (Rs)	-	-	-	-
Dividend payout ratio (%)	-	-	-	-
GROWTH				
Net sales (%)	56.0	24.3	24.4	9.8
EBITDA (%)	41.3	20.2	17.9	9.7
Adj net profit (%)	50.8	25.5	39.3	20.7
FDEPS (%)	50.8	7.5	39.3	20.7
PERFORMANCE				
RoE (%)	22.3	19.0	19.3	19.2
RoCE (%)	18.5	19.1	20.5	21.1
EFFICIENCY				
Asset turnover (x)	1.3	1.4	1.5	1.5
Sales/ total assets (x)	0.8	0.8	0.9	0.9
Working capital/ sales (x)	0.4	0.4	0.3	0.3
Receivable days	108.3	85.0	75.0	75.0
Inventory days	175.5	179.0	164.6	164.6
Payable days	177.8	190.1	182.4	182.5
FINANCIAL STABILITY				
Total debt/ equity (x)	2.6	1.7	1.2	0.9
Net debt/ equity (x)	2.4	1.5	1.0	0.8
Current ratio (x)	2.2	2.0	1.9	1.8
Interest cover (x)	1.6	1.8	2.2	2.5
VALUATION				
PE (x)	17.1	15.0	10.7	8.9
EV/ EBITDA (x)	8.9	7.2	6.0	5.4
EV/ Net sales (x)	1.8	1.4	1.1	1.0
PB (x)	3.7	2.6	2.2	1.8
Dividend yield (%)	-	-	-	-
Free cash flow yield (%)	-	0.1	0.2	0.2

Source: Company, Axis Capital

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HOLD	Between 10% and -10%
SELL	Less than -10%

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