

NCC Ltd.**₹ 47*****Decreasing Rates are of Interest !!!*****Buy**

January 20, 2012

Company Background

NCC is an Indian construction and infrastructure enterprise. Founded by Dr AVS Raju, it is based in Hyderabad. The company which was started as Nagarjuna Construction Company Limited - merely a construction company has now presence across a variety of infra segments. It changed its name a year ago to NCC Ltd to reflect its transition from a construction firm to an integrated infrastructure group.

NCC was ranked as the fastest growing construction company in the country by Construction World – NICMAR. The Company's business divisions are diversified across several infrastructure verticals & include - Building & Housing, Transportation, Electrical, Water & Environment, Irrigation, International, Power, Metals and Oil & Gas Division. The Property Division was established in 1996 followed by the Transportation Division in 1998. The Water, Electrical, Power, Irrigation, Metals, Oil & Gas Divisions were established subsequently. NCC Infrastructure Holdings Limited (NCC INFRA) is a wholly owned subsidiary of NCC Limited established for the development of Infrastructure Projects independently and through Government concessions. The Company had started its International operations by registering as a local company in the Sultanate of Oman in May of the year 2005- known as NCC International LLC.

NCC is the only construction company from India hailed as 'Best Under a Billion' in Asia Pacific and evolved from a mere contractor to a full-fledged & diversified infrastructure solutions provider. NCC's projects have been recognised as the "Outstanding Structure of the Year" by the Indian Concrete Institute.

Financial Performance

NCC posted below par results for the quarter ended on September 2011(Q2FY12). Sales declined 9.04% to ₹ 10.90 bn in Q2FY12 as against ₹ 12 bn during the previous quarter ended September 2010. As per management, muted revenue performance was because of the delays in the projects. The Uttar Pradesh road project did not move as per expectations on account of heavy rainfall. Few of the company's mining and other projects in Andhra Pradesh also faced delays on account of Telangana issue. The management has lowered its standalone revenue guidance to ₹ 56 bn vs. ₹ 59 bn guided earlier. On a consolidated basis, its Sales reported a nominal increase to ₹ 14.72 bn during the quarter as against ₹ 14.68 during the corresponding previous quarter.

NCC's EBITDA margin for the quarter reduced to 9.5%. The company continues to remain under pressure on the earnings front on account of subdued top-line growth and rising project costs. The company's debt level (₹ 26.01 bn) has remained flat, but the rise in interest rates has pushed up the overall interest burden. Interest cost during the quarter shot up to ₹ 709 mn – n increase of 89% yoy. Consequently, NCC's bottom line came in at ₹ 114 mn as against ₹ 460 mn during the corresponding previous quarter, registering a yoy decline of 75.2%. On a consolidated basis, NCC's net profit fell 53.8% to ₹ 294 mn.

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Info Codes

Reuters	NGCN.BO
Bloomberg	NJCC@IN
NSE	NCC
BSE	500294

Market Data

52 Wk Range (₹)	: 118 / 32
Shares in Issue (mn)	: 257
Mkt. Cap (₹ bn)	: 12.54
BSE 2 Wk Avg Vol	: 365000

Share Holding Pattern (%)

Promoters	: 19.52
DII's	: 12.51
FII's	: 44.11
Others	: 23.86

Investment Theme

Infrastructure Companies outperformed benchmark indices rising more than 20% in last couple of weeks. The major factor was the tapering of interest rates. RBI the central bank of India is expected to do away with the rate hikes & may reduce it to boost the liquidity. Further the government is being more and more forced to improve state of infrastructure in the country to boost the falling rate of economic growth. This would present the great opportunity to infrastructure player especially to those who have power, road & port in portfolio. NCC has experience in these verticals as well as currently executing such projects thus has advantage. Its share price has fallen more than 70% due to higher interest rates. We expect NCC to perform better as the interest cost comes down. thus recommend to buy this share.

The Good Raju from Hyderabad !!!

Investment Rationale

➔ Diversified order book

NCC's order book remains attractive. It is well diversified covering most of the key infrastructure verticals. NCC's order book stands at ₹ 166 bn (3.3x FY2011 revenue) as of Q2FY12, which is spread across nine verticals. NCC had a decent order inflow of ₹ 17.46 bn during the quarter, registering a growth of 15.6% yoy. Its subsidiary company, NCC Infra has five road projects with aggregate length of 200 kms, 720 MW of Hydro Electrical Projects and Re-development of A.P Bhavan (International Center) in its asset portfolio in different stages of development through concession route. Going ahead, we believe order inflow would be driven by EPC work of its own power plant and the road, building, water and electrical segments to gather momentum and add significantly to the order book as well.

➔ Power plant to boost order book

NCC acquired 55% stake in Nelcast Energy Corporation (NECL), which is developing 1320 MW (2X660 MW) power plant in Krishnapatnam. The ₹ 70 bn greenfield thermal power plan is being executed through a special purpose vehicle in a joint venture with Gayatri Projects, another Hyderabad-based infrastructure company. As per the company statement, The debt component of ₹ 53 bn is led by a consortium of Rural Electrification Corporation with ₹ 19 bn, Power Finance Corporation pitching in with ₹ 17 bn along with ICICI Bank and others. As a part of the project execution, NCC would get the mandate for ₹ 50 bn EPC contract for the power plant. Out of company's total equity requirement of ₹ 9.7 bn, it has already submitted ₹ 1.5 bn and remaining nearly ₹ 2 bn are expected to be submitted from internal accruals. All mandatory clearances for the project have been achieved. This is going to boost the order book of the company significantly.

➔ Macro factors improving

NCC has strong order book yet the company is highly undervalued. The reason being the high level of debt. The company management is considering some dilution of equity to raise funds for some of the ongoing projects. This could be either at the holding company or at the special purpose vehicle level. It has roped in a consultant to finalise fundraising options for NCC Infra- either bringing an initial public offer of NCC Infra or may go ahead with issuing of NCC Infra bonds. This could ease the pressure on the margin. Further the interest rates are tapering in the Indian economy. Going forward, as the inflation rate has fallen considerably; one can expect the RBI to take breather or may reduce the interest rates to boost the liquidity.

Key Financials

Year Ended 31 st	Mar 09	Mar 10	Mar 11
Revenue (₹ mn)	42214.3	48959.8	51771.1
Rev. growth (%)	19.99	15.98	5.74
EBITDA (₹ mn)	4260.3	5760.5	5619.3
Net profit (₹ mn)	1538.6	2326.2	1634.5
Shares outstanding (mn)	229.1	256.9	256.9
EPS (₹)	6.7	9.1	6.4
EPS growth (%)	(5.00)	34.85	(29.74)
P/E (x)	9.2	18.0	15.9
EV/ EBITDA	35.9	74.8	50.4
ROCE (%)	8.27	10.13	5.72

Sectoral overview

The infrastructure in India remains way below the global standards. Despite The past year or so has shown the classic cyclical nature of the industry. The infra stocks were trading at their peaks. The government of India had plans to put trillion of rupees to boost the sector. The crisis in European market coupled with higher inflation rates in the emerging markets had threatened the global economic recovery. The RBI had to raise the rates for 12 times consecutively to check the inflation. Despite this, inflation remained up & the stocks in the sector have tumbled by more than 50 –to 90%. order book growth rate had almost stalled as the corporate delayed their capex plans. However things seem to be hanging as the rates cycles has peaked up. we can expect better days for infrastructure players.

Andhra Pradesh - a power hub???

Andhra Pradesh has electricity demand of 12000 MW. The government has plans to have installed capacity of nearly 15000 MW in the near term which will further be doubled. The government plans to turn the state in the energy surplus one. Following this a number of power plants have been announced mainly in the coastal area of the state with some of them spending money on land acquisitions and other project start up expenses. However many of them have run up in the environmental related issues. It is really crucial for the government to address these issues if it wants to achieve its target. But it offers great opportunity for the power plant related infrastructure companies.

Financial Statements

Income Statement

(₹ mn)

Year end	Mar 09	Mar 10	% Chg	Mar 11	% Chg
Total Sales + Excise	41514.1	47778.2	15.09	50737.3	6.19
Other Income	700.2	1181.6	68.75	1033.8	(12.51)
Change in Stocks	1378.2	(407.5)	(129.57)	1137.3	(379.09)
Raw Material Con.	14892.6	18460.4	23.96	19458.2	5.41
Employee Exp.	1886.6	1841.3	(2.40)	2438.5	32.43
Indirect Taxes	1085.4	1393.2	28.36	1272.1	(8.69)
Other Exp.	21467.6	21096.9	(1.73)	24120.3	14.33
Operating Exp.	37954.0	43199.3	13.82	46151.8	6.83
Operating Profit	3560.1	4578.9	28.62	4585.5	0.14
Total Interest	1445.6	1743.9	20.64	2324.6	33.30
Gross Profit	2814.7	4016.6	42.70	3294.7	(17.97)
Net Dep.	533.0	526.8	(1.16)	686.7	30.35
Total Taxation	743.1	1163.6	56.59	973.5	(16.34)
Net Profit/Loss	1538.6	2326.2	51.19	1634.5	(29.74)

4 Years Balance Sheet

(₹ mn)

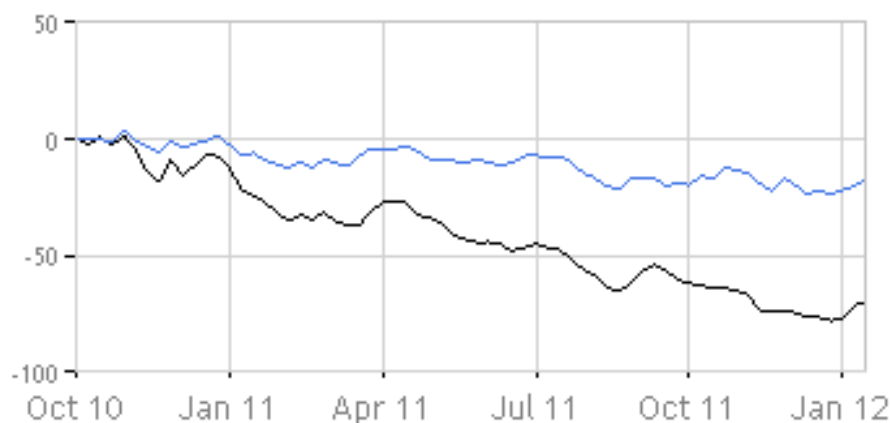
Balance Sheet as on 31 st	Mar 08	Mar 09	Mar 10	Mar 11
SOURCES OF FUNDS	24662.0	29294.3	37758.4	48627.6
Equity Share capital	457.7	457.7	513.2	513.2
Share Application Money	0.0	0.0	0.0	0.0
Preference Share Capital	0.0	0.0	0.0	0.0
Reserves & Surplus	15211.8	16397.7	21943.4	23273.7
Loan Funds	7242.5	8863.9	10499.2	13120.7
Unsecured Loans	1750.0	3575.0	4802.6	11720.0
USES OF FUNDS	24662.0	29294.3	37758.4	48627.6
Gross Block	6620.3	6232.8	7560.9	9230.5
Less : Revaluation Reserves	0.0	0.0	0.0	0.0
Less : Accumulated Depreciation	1423.6	1640.6	2022.9	2485.2
Net Block	5196.7	4592.2	5538.0	6745.3
Capital Work in Progress	142.6	281.2	434.2	469.4
Investments	6996.7	7762.5	9685.5	12219.8
Current Assets	28985.5	34918.4	43053.2	51782.8
Less : Current Liabilities	16659.5	18260.0	20952.5	22589.7
Total Net Current Assets	12326.0	16658.4	22100.7	29193.1
Misc. Expenses not written	0.0	0.0	0.0	0.0
NOTE				
Bk Val Unquoted Investments	6996.7	7762.5	9685.5	12219.8
Mkt Val. Quoted Investments	0.0	0.0	22.0	30.2
Contingent Liabilities	25702.4	44370.1	45684.1	52468.2
Dividend (%)	65	55	65	50

Quarterly Income Sheets

(₹ mn)

Quarter Ended	Dec 10	Mar 11	Jun 11	Sep 11
Net Sales	13355.00	14504.20	11415.40	10902.70
Cost Of Sales	12079.10	13195.00	10250.30	9870.90
Operating Profit	1275.90	1309.20	1165.10	1031.80
Recurring Income	23.00	56.40	20.80	22.40
Adjusted PBDIT	1298.90	1365.60	1185.90	1054.20
Financial Expenses	438.20	575.40	639.90	709.40
Depreciation	174.90	185.70	197.20	201.90
Other Write Offs	0.00	0.00	0.00	0.00
Adjusted PBT	685.80	604.50	348.80	142.90
Tax Charges	281.50	248.00	116.00	28.90
Adjusted PAT	404.30	356.50	232.80	114.00
Non Recurring Items	0.00	0.00	0.00	0.00
Other Non Cash Adjust	0.00	0.00	0.00	0.00
Net Profit	404.30	356.50	232.80	114.00

52 Week Index Relative Percentage Appreciation



NCC vs SENSEX

Risks Associated

➔ Cyclical nature of industry

The infrastructure projects are long term and capital intensive in nature. The ROCE in initial months of the projects is very tight and this can put the pressure on the overall company margins. Further projects face many hindrances during the execution phase which catapults the cost putting further pressure on the companies.

The sector itself is highly cyclical in nature. The economic cycle of inflation leads to fluctuation in interest rates. Currently Indian economy is facing the peak interest rates. This coupled with long project duration make it difficult to keep the margins in comfortable levels. Further competition has grown phenomenally leading to trade-off between order inflow & margin levels.

➔ Political issues

The key projects of NCC are in Andhra Pradesh where the Telangana issue has already affected the businesses. The issues has not yet resolved and thus would continue to affect routine business especially big infrastructure project which requires the movement of huge resources such as land, people & other natural resources.

In a Nutshell

NCC is an Indian construction and infrastructure enterprise. Founded by Dr AVS Raju, it is based in Hyderabad. The company which was started as Nagarjuna Construction Company Limited - merely a construction company has now presence across a variety of infra segments. The Company's business divisions are diversified into Building & Housing, Transportation, Electrical, Water & Environment, Irrigation, International, Power, Metals and Oil & Gas Division. Infrastructure companies had corrected more than 50 % in the last one year. The slowdown in order inflow and higher interest rates were the main reasons. However the companies have outperformed the benchmark indices rising more than 20% in last couple of weeks. The major factor was the tapering of interest rates. RBI the central bank of India is expected to done with the rate hikes & may reduce it to boost the liquidity. Further the government is being more and more forced to improve the state of infrastructure in the country to boost the falling rate of economic growth. This would present the great opportunity to infrastructure player especially to those who have power, road & port in tier portfolio. NCC having experience in these verticals as well as currently executing such projects thus has advantage. Its share price has fallen more than 70% due to higher interest rates burden. We expect the company to perform better as the interest cost comes down. Thus we recommend to buy this share.

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Rating Interpretation

Buy	: Expected to appreciate 20% or more over 12-months	Reduce	: Expected to depreciate up to 10% over 12-months
Accumulate	: Expected to appreciate 10% to 20% over 12-months	Sell	: Expected to depreciate 10% or more over 12-months
Trade Buy	: Expected to appreciate more than 10% over 45-days	Trade Sell	: Expected to depreciate more than 10% over 45-days

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