MOTILAL OSWAL

22 October 2019

Update | Sector: Infrastructure

Sadbhav Engg.

BSE SENSEX	S&P CNX
38,964	11,588

Sadbhav TODAY FOR TOMORROW

Stock Info

Bloomberg	SADE IN
Equity Shares (m)	172
M.Cap.(INRb)/(USDb)	24.1 / 0.3
52-Week Range (INR)	274 / 105
1, 6, 12 Rel. Per (%)	-3/-41/-50
12M Avg Val (INR M)	51
Free float (%)	53.5
Bloomberg	SADE IN

Financials Snapshot (INR b)

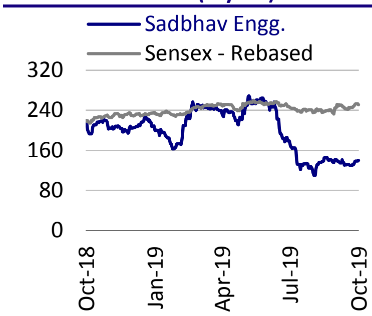
Y/E Mar	FY19	FY20E	FY21E
Net Sales	35.5	36.5	46.9
EBITDA	4.3	4.4	7.5
PAT	1.9	1.7	4.4
EPS (INR)	10.8	9.9	21.4
Gr. (%)	-15.7	-9.1	116.5
BV/Sh (INR)	118.5	127.5	215.9
RoE (%)	9.5	8.0	13.3
RoCE (%)	10.1	9.4	13.3
P/E (x)	12.8	14.1	6.5
P/BV (x)	1.2	1.1	0.6

Shareholding pattern (%)

As On	Sep-19	Jun-19	Sep-18
Promoter	46.6	46.6	46.5
DII	33.5	25.5	20.9
FII	12.7	13.4	16.5
Others	7.2	14.6	16.1

FII Includes depository receipts

Stock Performance (1-year)



CMP: INR140 TP: INR225(+60%) Buy

SIPL merger in favor of SADE's shareholders

To issue one equity share for every three equity shares of SIPL

- **SADE-SIPL merger ratio in favor of former's shareholders:** The Board of Directors of Sadbhav Engineering (SADE) has approved the merger of the company and its listed subsidiary Sadbhav Infrastructure Project Limited (SIPL). In consideration of the merger, SADE will issue one equity share for every three equity shares of SIPL. We note that the merger ratio of 3:1 (versus our expected ratio of 2.7:1 based on intrinsic valuation) is somewhat in favor of SADE's shareholders. As a result of the merger, the promoter stake in SADE will come down from 46.55% to 38.74%. The merger is likely to be completed in 6-9 months.
- **Merger was inevitable post sale of nine operational BOT assets in SIPL:** To recap, SADE had divested its stake in nine road assets at an EV of INR66.1b, resulting in a debt reduction of INR40.6b at the project level and realization of INR25.5b in lieu of equity invested. Of this, INR19b is expected to be cash consideration and the remaining INR6.5b in the form of the units of the InvIT, IndInfravit Trust, to the tune of a 10% stake. Post the asset sale, SIPL will have three operational assets and a portfolio of 11 HAM projects, thereby reducing the dependency on traffic growth. Anyway, the investor interest in the listed asset arm has been on a decline, as InvITs are better products compared to listed companies in the road assets business, given the removal of the dividend distribution tax on SPVs and the minimum construction risk.
- **Merged standalone to capture deleveraging benefits but also future equity funding risk to SPVs:** Prima facie, the merger appears value accretive to standalone SADE as the entire benefit of debt reduction in SIPL standalone gets captured in the new merged entity. Thus, the estimated merged SADE standalone FY21 PAT increases by 85% to INR4.4b from INR2.4b earlier. Over FY19-21, adj. PAT CAGR is estimated at 54.5% and adj. EPS CAGR at 40.3% as there is a dilution of 21% on share capital. However, we note that the future equity commitment in SPVs (both for loss making SPVs like Rohtak Panipat and Rohtak Hissar as well as equity commitment in HAM portfolio) now comes on SADE's balance sheet. Thus, if SADE bids for new projects on a HAM basis, it will have to use the balance sheet strength of merged SADE rather than SIPL earlier.
- **Increasing target price; maintaining Buy:** We have incorporated the merger of SIPL into SADE from FY21. Consequently, there is no change to our FY20 forecasts, but our FY21 EPS estimate increases by 53%. Our SOTP-based target price increases by 15% to INR225 (prior: INR195), of which 11% is attributed to lower dilution than our earlier estimate and the remaining 4% to re-rating of the combined standalone entity to similar multiple of FY21E 8x P/E of pre-merged SADE entity. The delay in merger may have a negative impact on our FY21 estimates. Maintain **Buy** on account of cheap valuations.

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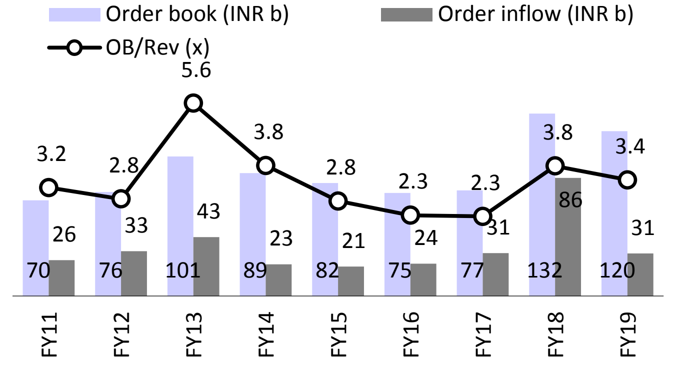
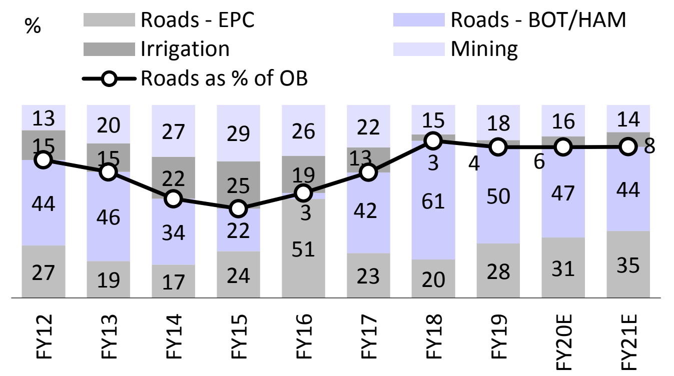
Story in charts

Exhibit 1: Order book trend



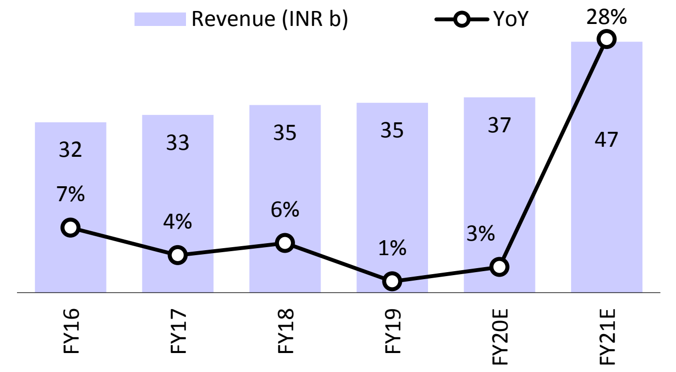
Source: MOFSL, Company

Exhibit 2: Higher share of road projects in OB augers well



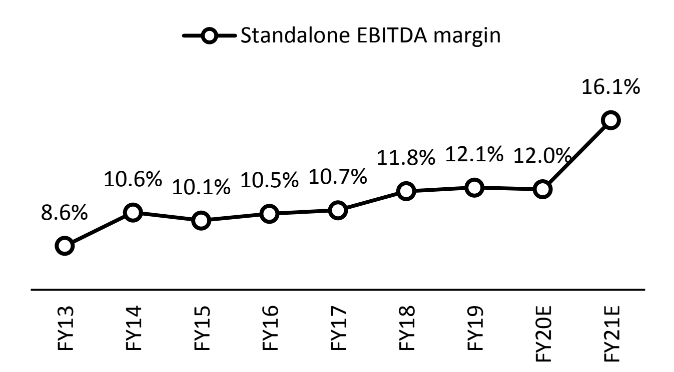
Source: MOFSL, Company

Exhibit 3: We forecast EPC revenue CAGR of 15% over FY19-21 for the merged standalone entity



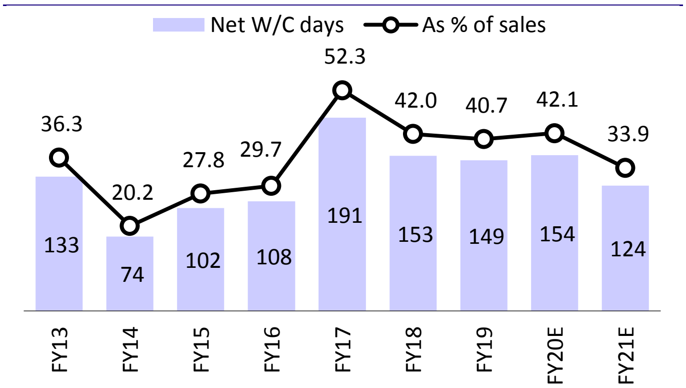
Source: MOFSL, Company

Exhibit 4: EBITDA margin trend for the merged standalone entity



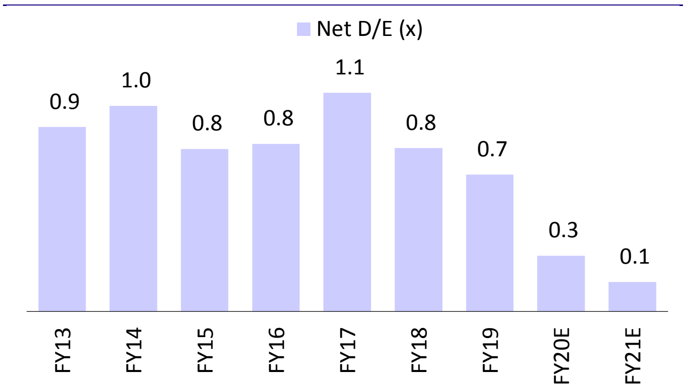
Source: MOFSL, Company

Exhibit 5: Net working capital cycle to improve post-merger



Source: MOFSL, Company

Exhibit 6: Net D/E to improve to 0.1x



Source: MOFSL, Company

Exhibit 7: We increase our FY21E PAT to INR4.4b as we factor in the merger of SADE and SIPL standalone; EPS increase is lower on account of dilution

Earnings Change	Old		New		Change	
INR m	FY20E	FY21E	FY20E	FY21E	FY20E	FY21E
Revenue	36,512	43,183	36,512	46,900	0%	9%
EBITDA	4,365	5,113	4,365	7,529	0%	47%
EBITDA margin	12.0%	11.8%	12.0%	16.1%	0.0%	4.2%
PAT	1,692	2,402	1,692	4,440	0%	85%
EPS	9.9	14.0	9.9	21.4	0%	53%

Source: MOFSL, Company

Exhibit 8: Our SOTP-based valuation stands at INR225/sh

Segment (INR m)	Equity Commitment	Equity invested (till FY19E)	Basis	Value (INR m)	Value/sh (INR)	as % of TP
Road BOTs – Operational						
Rohtak Panipat	2,427	2,427	NPV	-1,933	-9	-4%
Rohtak - Hissar	1,108	1,108	NPV	-2,483	-12	-5%
Maharashtra Checkpost	2,765	4,046	NPV	8,982	43	19%
Sub-total	**20,206**	**20,609**		**4,566**	**22**	**10%**
Road BOTs - Under implementation						
Rampur - Kathgodam Pkg 1	886	643	NPV	488	2	1%
Rampur - Kathgodam Pkg 2	788	461	NPV	392	2	1%
Bhavnagar Talaja	983	546	NPV	733	4	2%
Una Kodinar	748	285	NPV	436	2	1%
BRT Tiger Reserve - Bangalore	1,210	948	NPV	416	2	1%
Waranga - Mahagaon	1,285	488	NPV	-44	0	0%
Udaipur Bypass	1,069	648	NPV	231	1	0%
Jodhpur Ring Road - I	1,393	228	NPV	-443	-2	-1%
Bhimasar - Bhuj	1,382	56	NPV	-799	-4	-2%
Tumkur Shivamogga	1,210	1	NPV	-735	-4	-2%
Vadodara Kim Phase VI	1,685	6	NPV	-434	-2	-1%
Sub-total	**12,638**	**4,309**		**240**	**1**	**1%**
InvIT				6,500	31	14%
Road BOTs (Total)	**32,844**	**24,918**		**11,306**	**54**	**24%**

	Basis	Multiple (x)	Value (INR m)	Value/sh (INR)	as % of TP
SEL EPC	FY21E PE (x)	8.0	35,518	171	76%
Total Fair value (SEL)			**46,824**	**225**	**100%**

Source: Company, MOFSL

Financials and Valuations

Standalone - Income Statement					(INR m)
Y/E March	**FY17**	**FY18**	**FY19**	**FY20E**	**FY21E**
Total Income from Operations	**33,203**	**35,051**	**35,492**	**36,512**	**46,900**
Change (%)	4.2	5.6	1.3	2.9	28.5
EBITDA	**3,556**	**4,151**	**4,279**	**4,365**	**7,529**
Margin (%)	10.7	11.8	12.1	12.0	16.1
Depreciation	1,000	979	958	1,125	1,200
EBIT	**2,556**	**3,172**	**3,321**	**3,240**	**6,329**
Int. and Finance Charges	1,534	1,907	1,749	1,635	1,462
Other Income	875	897	1,003	657	1,067
PBT bef. EO Exp.	**1,897**	**2,163**	**2,575**	**2,262**	**5,933**
EO items	0	0	8		
PBT after EO Exp.	**1,897**	**2,163**	**2,583**	**2,262**	**5,933**
Total Tax	18	-44	714	569	1,493
Tax Rate (%)	1.0	-2.0	27.7	25.2	25.2
Reported PAT	**1,878**	**2,207**	**1,869**	**1,692**	**4,440**
Adjusted PAT	**1,878**	**2,207**	**1,861**	**1,692**	**4,440**
Change (%)	24.0	17.5	-15.7	-9.1	162.3
Margin (%)	5.7	6.3	5.2	4.6	9.5

Standalone - Balance Sheet					(INR m)
Y/E March	**FY17**	**FY18**	**FY19**	**FY20E**	**FY21E**
Equity Share Capital	172	172	172	172	208
Total Reserves	16,437	18,496	20,165	21,708	44,683
Net Worth	**16,609**	**18,668**	**20,337**	**21,879**	**44,891**
Total Loans	17,771	14,847	14,900	8,900	13,133
Deferred Tax Liabilities	-477	-994	-994	-994	-881
Capital Employed	**33,904**	**32,520**	**34,243**	**29,785**	**57,142**
Gross Block	6,759	7,282	8,174	8,874	9,591
Less: Accum. Deprn.	1,530	2,278	3,235	4,361	5,573
Net Fixed Assets	**5,229**	**5,004**	**4,939**	**4,514**	**4,018**
Capital WIP	0	23	33	33	33
Total Investments	**5,694**	**5,775**	**6,094**	**5,084**	**23,434**
Curr. Assets, Loans&Adv.	**28,804**	**31,910**	**33,918**	**31,204**	**42,723**
Inventory	1,234	1,643	1,792	1,843	2,180
Account Receivables	17,010	16,280	15,551	16,506	16,035
Cash and Bank Balance	230	127	1,469	3,022	6,713
Loans and Advances	10,331	13,860	15,107	9,833	17,795
Curr. Liability & Prov.	**5,823**	**10,192**	**10,741**	**11,048**	**13,066**
Account Payables	5,803	10,165	10,713	11,021	13,035
Provisions	20	27	27	27	31
Net Current Assets	**22,981**	**21,718**	**23,177**	**20,155**	**29,657**
Appl. of Funds	**33,904**	**32,520**	**34,243**	**29,785**	**57,142**

Financials and Valuations

Ratios

Y/E March	FY17	FY18	FY19	FY20E	FY21E
Basic (INR)					
EPS	**11.0**	**12.9**	**10.8**	**9.9**	**21.4**
Cash EPS	16.8	18.6	16.4	16.4	27.1
BV/Share	96.8	108.8	118.5	127.5	215.9
DPS	0.7	0.7	0.7	0.7	0.6
Payout (%)	7.7	7.0	8.0	8.9	3.4
Valuation (x)					
P/E	12.7	10.8	12.8	14.1	6.5
Cash P/E	8.3	7.5	8.5	8.5	5.1
P/BV	1.4	1.3	1.2	1.1	0.6
EV/Sales	1.2	1.1	1.1	0.8	0.8
EV/EBITDA	11.7	9.3	8.7	6.8	4.7
Dividend Yield (%)	0.5	0.5	0.5	0.5	0.4
FCF per share	-50.9	16.2	14.8	44.7	-1.8
Return Ratios (%)					
RoE	11.9	12.5	9.5	8.0	13.3
RoCE	8.9	9.6	10.1	9.4	13.3
RoIC	8.3	9.3	10.0	10.7	20.8
Working Capital Ratios					
Fixed Asset Turnover (x)	4.9	4.8	4.3	4.1	4.9
Asset Turnover (x)	1.0	1.1	1.0	1.2	0.8
Inventory (Days)	14	17	18	18	17
Debtor (Days)	187	170	160	165	125
Creditor (Days)	64	106	110	110	101
Leverage Ratio (x)					
Current Ratio	4.9	3.1	3.2	2.8	3.3
Interest Cover Ratio	1.7	1.7	1.9	2.0	4.3
Net Debt/Equity	1.1	0.8	0.7	0.3	0.1

Standalone - Cash Flow Statement **(INR m)**

Y/E March	FY17	FY18	FY19	FY20E	FY21E
OP/(Loss) before Tax	1,897	2,163	2,575	2,262	5,933
Depreciation	1,000	979	958	1,125	1,200
Interest & Finance Charges	992	1,167	1,749	1,635	1,462
Direct Taxes Paid	-18	44	-714	-569	-1,381
(Inc)/Dec in WC	-11,025	86	-117	4,576	-5,811
CF from Operations	**-7,154**	**4,439**	**4,451**	**9,029**	**1,404**
Others	-333	-157	-1,003	-657	-1,067
CF from Operating incl EO	**-7,487**	**4,281**	**3,448**	**8,371**	**337**
(Inc)/Dec in FA	-1,250	-1,500	-902	-700	-704
Free Cash Flow	**-8,737**	**2,781**	**2,546**	**7,671**	**-368**
(Pur)/Sale of Investments	6,474	218	-319	1,010	336
Others	333	157	1,003	657	1,067
CF from Investments	**5,557**	**-1,125**	**-218**	**967**	**698**
Issue of Shares	0	0	0	0	36
Inc/(Dec) in Debt	3,005	-1,851	53	-6,000	4,233
Interest Paid	-992	-1,167	-1,749	-1,635	-1,462
Dividend Paid	-221	-241	-150	-150	-150
Others	0	0	-42	0	0
CF from Fin. Activity	**1,792**	**-3,259**	**-1,888**	**-7,785**	**2,657**
Inc/Dec of Cash	**-137**	**-103**	**1,342**	**1,554**	**3,692**
Opening Balance	367	230	127	1,469	3,023
Closing Balance	**230**	**127**	**1,469**	**3,023**	**6,714**

NOTES

Explanation of Investment Rating	
Investment Rating	**Expected return (over 12-month)**
BUY	>=15%
SELL	< - 10%
NEUTRAL	< - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

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