28 November 2017

PSP Projects

Rating: **NR**

Share Price: ₹439

Strong growth momentum; WC-cycle prolongation an aberration

Q2, post-listing, is as inspiring as Q1, with the strong growth pace persisting for PSP. The working-capital-cycle elongation seems to be a GST-led aberration. As this is expected to correct shortly and as recently-bagged projects begin to contribute, we see the healthy growth momentum continuing. Also, the opportunity landscape in its area of expertise (institutional buildings) is bright and recent fund raising would help make the most of it. We do not have a rating on the stock but a long-term admiration for the company's sound fundamentals.

Impressive year-to-date inflows. Backed by its largest ever single order (the Surat Diamond Bourse valued (excl. GST at ~₹15.8bn), the company has secured orders of ~₹23bn for the year till now. As inflows are far in excess of revenues recognized, revenue assurance has jumped manifold (at 5x TTM sales). With revenue assurance secure, project execution is likely to gain centre-stage but select bidding isn't ruled out (management expects another ~₹4bn-5bn by the year end).

Working-capital cycle prolonged but expected to contract. Protraction in the cycle was largely due to an increase in receivables days (up from 49 at 31st Mar'17 to 86 at end-Q2). Management attributes this to GST-driven issues with billing and *adhoc* payments by some of the clients (probably, the held-back GST component).

Competition keener for smaller projects. Hyper-competition by smaller operators for orders of below ₹1.5bn is pricing out the company. For larger projects, competition is not as intense and rational bidding prevails.

Valuation. At the CMP, the stock trades at a PE of 29x TTM EPS of ~₹14.9. To justify such a high valuation, PSP would have to deliver ~30% earnings CAGR in the next two years. Backed by a strong order backlog and continued focus on project execution, the targeted growth seems achievable. **Risks.** Any failure to maintain prudence.

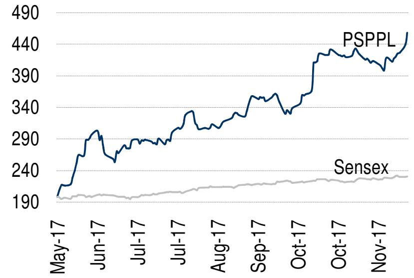
Key financials (YE Mar)	FY13	FY14	FY15	FY16	FY17
Sales (₹ m)	2,572	2,104	2,805	4,580	4,008
Net profit (₹ m)	123	101	141	249	413
EPS (₹)	4.3	3.5	4.9	8.7	14.3
Growth (%)	46.7	-17.8	39.6	77.4	65.7
PE (x)	103.2	125.5	89.9	50.7	30.6
EVEBITDA (x)	70.5	91.3	67.7	38.3	22.9
PBV (x)	59.4	45.4	33.7	23.9	14.7
RoE (%)	58.5	32.8	34.4	44.1	47.6
RoCE (%)	53.3	34.3	33.8	44.2	50.2
Net debt/equity (x)	-1.1	-1.5	-1.3	-1.1	-0.7

Source: Company Note: Standalone Financials

Key data	PSPPL IN / PSPP.BO
52-week high / low	₹469 / 189
Sensex / Nifty	33724 / 10400
3-m average volume	$0.7m
Market cap	₹16bn / $244m
Shares outstanding	36m

Shareholding pattern (%)	Sep'17	Jun'17	May'17
Promoters	72.0	72.0	72.0
- of which, Pledged	-	-	-
Free Float	28.0	28.0	28.0
- Foreign Institutions	1.2	1.1	2.5
- Domestic Institutions	10.5	13.6	13.8
- Public	16.3	13.4	11.7

Relative price performance



Source: Bloomberg

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Quick Glance – Financials and Valuations

Fig 1 – Income statement (₹ m) - Standalone

Year-end: Mar	FY13	FY14	FY15	FY16	FY17
Order Backlog	NA	4,472	4,877	3,381	7,292
Average order size	NA	244	198	192	351
Net revenues (₹ m)	2,572	2,104	2,805	4,580	4,008
Growth (%)	44.0	-18.2	33.3	63.3	-12.5
Direct costs	2,232	1,858	2,489	4,032	3,188
SG&A	121	79	92	155	161
EBITDA	220	167	224	393	658
EBITDA margins (%)	8.5	8.0	8.0	8.6	16.4
Depreciation	37	37	52	71	76
Other income	37	44	65	97	132
Interest Exp	38	20	25	34	75
PBT	182	154	213	386	639
Effective tax rate (%)	32.7	34.6	33.9	35.4	35.4
+ Associates/(Minorities)	-	-	-	-	-
Net Income	123	101	141	249	413
Adjusted income	123	101	141	249	413
Growth (%)	46.7	-17.8	39.6	77.4	65.7
FDEPS (₹/share)	4.3	3.5	4.9	8.7	14.3

Fig 2 – Balance sheet (₹ m) - Standalone

Year-end: Mar	FY13	FY14	FY15	FY16	FY17
Share capital	8	8	8	32	288
Net worth*	266	348	469	661	1,076
Total debt	150	260	334	452	677
Minority interest	-	-	-	-	-
DTL/(assets)	-2	-3	-5	-9	-11
Capital employed	**414**	**605**	**798**	**1,105**	**1,742**
Net tangible assets	185	185	332	519	513
Net intangible assets	-	-	0	3	5
Goodwill	-	-	-	-	-
CWIP (tang. & intang.)	-	-	2	-	-
Investments (strategic)	35	8	8	50	76
Investments (financial)	-	81	118	130	140
Current assets (ex cash)	342	401	550	513	1,158
Cash	446	684	848	1,064	1,250
Current liabilities	594	755	1,060	1,174	1,399
Working capital	-252	-354	-511	-661	-241
Capital deployed	**414**	**605**	**798**	**1,105**	**1,742**
Contingent liabilities	177	183	457	727	1,178

Fig 3 – Cash-flow statement (₹m) - Standalone

Year-end: Mar	FY13	FY14	FY15	FY16	FY17
PBT	182	154	213	386	639
+ Non-cash items	37	37	52	71	76
Oper. profit before WC chg	219	191	264	457	715
- Incr./(decr.) in WC	-120	-102	-157	-150	420
Others including taxes	59	53	72	137	226
Operating cash-flow	280	239	349	470	69
- Capex (tangible + Intangible)	42	37	201	258	71
Free cash-flow	238	202	148	212	-2
Acquisitions	-	-	-	-	-
- Dividend*	9	19	19	58	-
+ Equity raised	-	-	-	-	-
+ Debt raised	-110	109	72	115	222
- Fin Investments	32	54	37	53	36
- Misc. Items (CFI + CFF)	0	(0)	0	-	-2
Net cash-flow	87	238	164	216	186

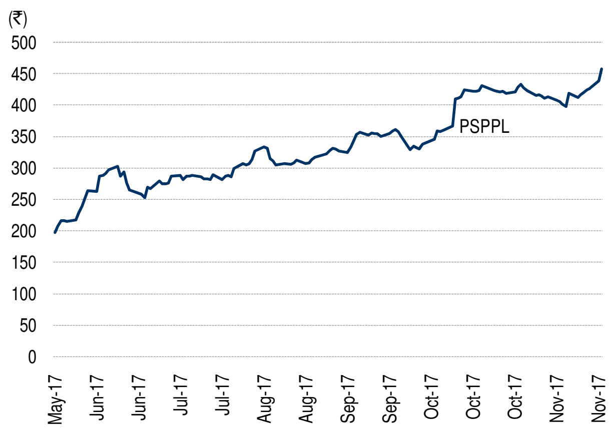
Source: Company

Fig 4 – Ratio analysis@ ₹439

Year-end: Mar	FY13	FY14	FY15	FY16	FY17
P/E (x)	103.2	125.5	89.9	50.7	30.6
EV/EBITDA (x)	70.5	91.3	67.7	38.3	22.9
EV/sales (x)	6.0	7.3	5.4	3.3	3.8
P/B (x)	59.4	45.4	33.7	23.9	14.7
RoE (%)	58.5	32.8	34.4	44.1	47.6
RoCE (%)	53.3	34.3	33.8	44.2	50.2
Sales/FA (x)	13.9	11.4	8.4	8.8	7.7
DPS (Rs per share)*	0.3	0.6	0.6	1.7	2.5
Dividend yield (%)*	0.1	0.1	0.1	0.4	0.6
Dividend payout (%) - Inc. DDT*	7.6	18.6	13.7	23.1	26.2
Net debt/equity (x)	-1.1	-1.5	-1.3	-1.1	-0.7
Receivables (days)	17	24	31	8	49
Inventory (days)	3	3	5	3	3
Payables (days)	50	69	82	55	63
CFO:PAT%	228.4	237.7	248.5	188.6	16.7

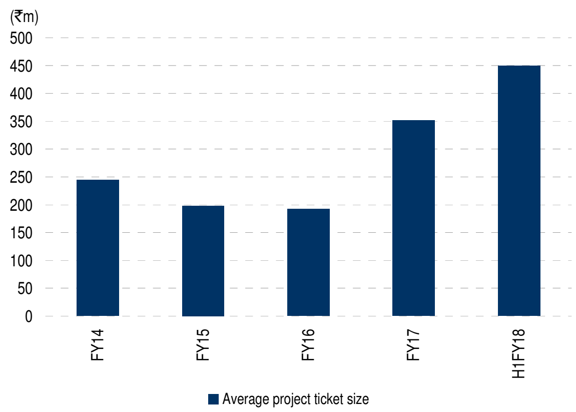
*Source: Company ; * Dividend for FY17 proposed after IPO; considered in ratio analysis*

Fig 5 – Price movement



Source: Bloomberg

Fig 6 – Average order ticket size on an uptrend**



*Source: Company ** Excludes recently bagged the Surat Diamond Bourse project of `15.8bn*

Operations update / Concall highlights

Financial performance

- A robust pace of execution in the quarter, at ~₹7.5bn of the opening order backlog (attributable to the standalone entity) helped the company report a strong ~80% y/y growth in revenue. The growth is equally impressive for H1 FY18, at ~80%, implying there was no drop in pace of execution in Q2.
- The margin contracted ~113bps y/y to ~13.4% but is still better than the long-term median (~8.5% for the last six years). The margin contraction seems a function of the revenue mix as well as the project mix.
- A healthy jump in revenue, combined with contained finance costs (at ~1.4% of sales vs. ~2.3% a year ago) and higher other income (due to the higher cash balance) helped earnings double y/y (up ~102%).

Fig 7 – Financial highlights

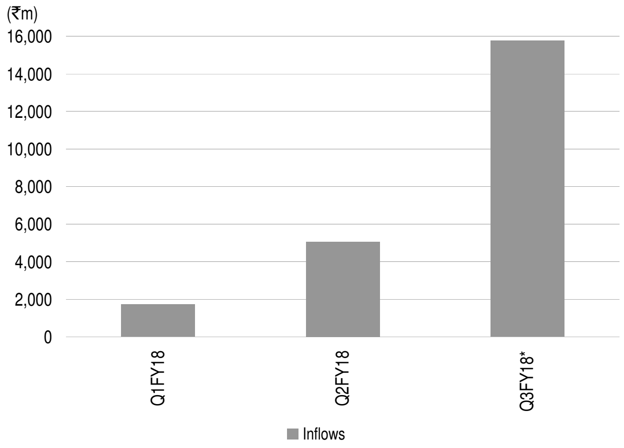
(YE: Mar) (₹ m)	Q2 FY17	Q2 FY18	% y/y	Q1 FY18	% q/q	H1 FY17	H1 FY18	% y/y
Sales	776	1,396	*79.7*	1,558	*(10.4)*	1,637	2,954	*80.4*
EBITDA	112	186	*65.7*	199	*(6.4)*	231	385	*67.0*
EBITDA margin (%)	*14.5*	*13.4*	*-113bps*	*12.8*	*58bps*	*14.1*	*13.1*	*-105bps*
Interest	18	20	*14.0*	14	*47.4*	33	34	*2.5*
Depreciation	18	23	*24.4*	18	*24.3*	35	41	*16.8*
Other income	23	52	*126.2*	41	*26.3*	50	93	*87.3*
PBT	99	195	*96.5*	208	*(6.1)*	212	403	*90.1*
Tax	37	69	*87.3*	72	*(5.3)*	75	141	*89.5*
Adjusted PAT	63	127	*101.8*	136	*(6.6)*	138	262	*90.4*

Source: Company

Order backlog / inflows

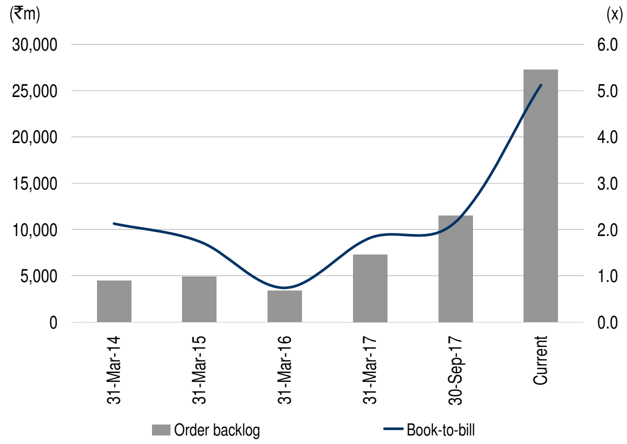
- Backed by strong inflows of ~₹5.1bn in Q2, H1 inflows have been a healthy ~₹6.8bn. Consequently, the order backlog at 30th Sep'17 was ~₹11.5bn.

Fig 8 – Year-to-date inflows of ~₹23bn



*Source: Company * Q3-to-date*

Fig 9 – Strong order backlog= strong revenue assurance



Source: Company

- Besides, subsequently, the company has secured its largest ever single order in the institutional buildings sub-segment. Valued at ~₹15.8bn (excl. GST), this institution order for the Surat Diamond Bourse is to be completed within 30 months. This takes the order backlog to ~₹27bn and implies a book-to-bill of 5x on reported TTM sales.
- With this healthy order backlog and work yet to stabilise at some of the new orders (especially on the Surat Diamond Bourse project), management intends to be very selective in bidding for projects. Nevertheless, it expects orders of another ~₹4bn-5bn in H2 FY18, based on the present bid pipeline and client comfort.
- In its Sep'17-end order backlog of ~₹11.5bn, government contracts account for ~13%. Management identify these as contracts with no pass through structure for any change in prices of any raw material.

The Surat Diamond Bourse project

- Management expects to incur capex of ~4-5% of the project value for the Surat Diamond Bourse project, but does not see any need to dip into its own cash-flows to fund this. As per management, mobilisation advances of 5% from the project would ideally suffice for a large part of the required capex. Besides capex for the Surat Diamond Bourse, management is also looking at another ~₹0.3bn-0.4bn of capex over the next 1.5 years. Over H1 FY18, it incurred capex of ~₹109m.
- Management expects excavation to take three months, then foundation 4-6 months. A need for shuttering material would then arise.
- Management does not see the Surat Diamond Bourse project to be a cash drag since it is an activity-linked monthly-payment scheme. It sees mobilisation advances of ~₹0.8bn (excl. GST) to help the first payment milestone and kick-start the payment cycle. At any time, it does not see more than ~₹0.6bn of exposure to the project. Mobilisation advances in this project are adjustable against the receipts; to be adjusted over the entire project value (5% to be deducted from every payment due).
- Management expects this project to turn revenue contributing by Jan/ Feb'18.
- Management has been given to understand that L2 in this project was ~₹0.3bn-0.35bn higher than its bid of ₹15.75bn.
- It believes its credentials from completing a 1.8m sq.ft. housing project in Gujarat ahead of scheduled helped it qualify for the project.
- On the client's ability to pay, management has been given to understand that the client (Association of Diamond Merchants) has already sold ~85-90% of the saleable area and collected ~₹6bn as first instalment. The rest of the payments are to be received on a milestone basis.

New opportunity / Competitive intensity

- Management sees hyper-competition in sub-₹1.5bn orders. Thus, it is being priced out by smaller operators. For larger projects, competition is not as intense and rational bidding by large operators continues.

- Gujarat remains the company's mainstay. Management intends to conservatively explore opportunities outside that state. For such opportunities, its focus would continue on segments in which it already operates. The idea is to gradually strengthen capabilities outside Gujarat.
- It expects bidding for IIT in Hyderabad by mid- to end-Dec'17.
- Based on its present credentials and balance sheet, the company is well placed to bid for any single project of ₹5bn.

Capex / cash flows

- During H1 FY18, the company incurred a capex of ~₹109m, funded from the issue proceeds. For the rest of the year, it expects to incur another ~₹0.3bn-0.4bn. This is besides the capex required for the Surat Diamond Bourse.
- Receivables have seen a meaningful increase in H1 FY18, from ~₹0.5bn on 31st Mar'17 (49 days) to ~₹1.3bn (86 days). Management attributes this to GST-driven issues, with billing and *adhoc* payments by clients in the mean time. Management expects the cycle to return to 40-45 days by Mar'18.
- Of the IPO proceeds of ~₹1.5bn, the company has utilized ~₹0.8bn (working capital ~₹0.55bn, capex ~₹109m and general purposes ~₹91m).

Valuation

At the CMP, the stock trades at PE of 29x TTM EPS of ~₹14.9. To justify such a high valuation, PSP would have to deliver ~30% earnings CAGR in the next two years. Backed by a strong order backlog and continued focus on project execution, the targeted growth seems achievable.

Risks. Any failure to maintain prudence.

Appendix

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