19 January 2023

PSP Projects

Strong order accretion, execution ramp-up awaited

Rating: **NR**

Share Price: Rs.691

Strong order accretion but sluggish revenues, we believe, aptly characterise PSP's FY23. Management expects the recent soft execution to fade quickly and its new orders to begin making a real difference, starting Q4 FY23. In light of this, it appears that execution momentum will continue into FY24. We find the Q4 revenue projection to be ambitious, but it, if achieved, fulfilment would reinforce confidence in the company's execution abilities. The bright longer-term outlook continues otherwise, led by recent strong orders added, a sturdy prospects pipeline and a well-set balance sheet.

Strong accretion, sturdy assurance. With orders of ~Rs4.4bn in Q3 FY23, and of ~Rs13.4bn subsequently, ytd additions, at ~Rs33bn, have been strong. With this strong a ytd addition, the OB now (incl. post-Q3), at ~Rs64.2bn, is sturdy, and implies revenue assurance for over three years. The appetite for more stays, and the company looks to close this year with Rs38bn-40bn, and sustain the pace with another ~Rs30bn in FY24. For this, its eyes are already set on an immediate prospects pipeline of ~Rs45bn.

Uttar Pradesh healthcare orders, status update. The contribution rose from ~Rs0.75bn the quarter prior to ~Rs1.65bn, but was still sub-optimal for the potential it entails, and for management's internal estimate of ~Rs2.5bn for Q3. The issues (mostly approval-related) have been resolved, and management looks for it to contribute more meaningfully in coming quarters (~Rs1bn per month targeted in Q4 FY23). At end-Q3, the balance potential was ~Rs10.7bn.

Guidance; FY23 inflows raised, but revenue lowered. With ytd additions ahead of its earlier guidance (of ~Rs25bn), and L1 status in an order of ~Rs3.5bn, it now targets Rs38bn-40bn in FY23. Revenue guidance, though, was pruned from ~Rs22bn to ~Rs21bn, on the soft Q3. Management expects the pace of execution to turn optimal by Q4 FY23, and thus targets ~25% higher revenues in FY24. It sees orders of ~Rs30bn in FY24 to suffice for its growth aspirations.

Valuation. At the CMP, the stock trades at 17.7x TTM EPS of Rs39. We do not have a rating for the company. **Risk:** Failure to ramp-up execution.

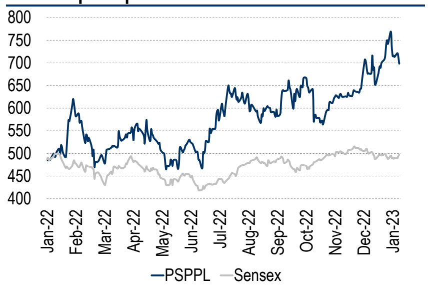
Key financials (YE Mar)	FY18	FY19	FY20	FY21	FY22
Sales (Rs m)	7,298	10,440	14,993	12,409	17,488
Net profit (Rs m)	644	902	1,293	835	1,624
EPS (Rs)	17.9	25.1	35.9	23.2	45.1
Growth (%)	23.8	40.2	43.2	-35.4	94.4
P/E (x)	25.1	18.3	9.0	20.0	12.0
EV / EBITDA (x)	13.8	9.8	5.4	11.3	7.2
P/BV (x)	5.3	4.5	2.5	3.1	2.8
RoE (%)	31.4	26.8	31.2	16.8	26.6
RoCE (%)	43.8	41.3	41.1	22.2	35.5
Net debt / equity (x)	-0.7	-0.5	-0.3	-0.3	-0.1

Source: Company

Key data	PSPPL IN / PSPP.BO
52-week high / low	Rs776 / 459
Sensex / Nifty	60858 / 18108
3-m average volume	$2.5m
Market cap	Rs25bn / $305.9m
Shares outstanding	36m

Shareholding pattern (%)	Dec'22	Sep'22	Jun'22
Promoters	67.5	70.4	70.4
- of which, Pledged	-	-	-
Free float	32.5	29.6	29.6
- Foreign institutions	2.3	2.0	1.9
- Domestic institutions	4.2	4.5	4.8
- Public	26.0	23.1	22.9

Relative price performance



Source: Bloomberg

Prem Khurana
Research Analyst
+9122 6626 6470
premkhurana@rathi.com

Quick Glance – Financials and Valuations (standalone)

Fig 1 – Income statement (Rs m)

Year-end: Mar	FY18	FY19	FY20	FY21	FY22
Order backlog	25,590	29,780	30,736	41,210	43,240
Order inflows	25,582	14,150	15,780	22,815	19,399
Net revenues	**7,298**	**10,440**	**14,993**	**12,409**	**17,488**
Growth (%)	*82.1*	*43.0*	*43.6*	*-17.2*	*40.9*
Direct costs	6,199	8,851	12,949	10,911	14,636
SG&A	87	99	134	150	286
EBITDA	**1,013**	**1,489**	**1,910**	**1,348**	**2,565**
EBITDA margins (%)	*13.9*	*14.3*	*12.7*	*10.9*	*14.7*
Depreciation	112	242	267	256	321
Other income	185	230	248	169	213
Interest expenses	87	92	146	147	264
PBT	999	1,385	1,744	1,114	2,193
Effective tax rate (%)	*35.6*	*34.9*	*25.9*	*25.0*	*25.9*
+ Associates / (Minorities)	-	-	-	-	-
Net income	644	902	1,293	808	1,624
Adjusted income	644	902	1,293	835	1,624
WANS	36	36	36	36	36
FDEPS (Rs / sh)	17.9	25.1	35.9	23.2	45.1

Fig 2 – Balance sheet (Rs m)

Year-end: Mar	FY18	FY19	FY20	FY21	FY22
Share capital	360	360	360	360	360
Net worth	3,027	3,714	4,571	5,380	6,847
Debt	216	263	748	810	997
Minority interest	-	-	-	-	-
DTL / (Assets)	-18	-49	-58	-92	-94
Capital employed	**3,225**	**3,928**	**5,262**	**6,098**	**7,750**
Net tangible assets	763	1,021	1,065	1,149	2,060
Net intangible assets	7	10	14	12	14
Goodwill	-	-	-	-	-
CWIP (tang. & intang.)	18	-	-	416	-
Investments (strategic)	44	44	44	8	7
Investments (financial)	151	-	-	-	-
Current assets (excl. cash)	2,604	3,964	6,444	5,938	8,540
Cash	2,232	2,217	1,967	2,288	1,952
Current liabilities	2,595	3,329	4,273	3,714	4,822
Working capital	9	635	2,171	2,224	3,717
Capital deployed	**3,225**	**3,928**	**5,262**	**6,098**	**7,750**
Contingent liabilities	2,577	3,401	4,045	3,674	4,877

Fig 3 – Cash-flow statement (Rs m)

Year-end: Mar	FY18	FY19	FY20	FY21	FY22
PBT + Net interest expense	901	1,247	1,643	1,092	2,245
+ Non-cash items	112	242	267	256	321
Oper. profit before WC chg.	1,013	1,489	1,910	1,348	2,565
- Incr. / (decr.) in WC	18	626	1,536	53	1,493
Others including taxes	355	483	452	279	569
Operating cash-flow	639	381	-78	1,017	503
- Capex (tang. + intangibles)	392	486	314	756	816
Free cash-flow	247	-105	-392	261	-313
Acquisitions	-	-	-	-	-
- Dividend (incl. buyback & taxes)	108	217	434	-	144
+ Equity raised	1,419	-	-	-	-
+ Debt raised	-464	16	477	27	185
- Fin. investments	-21	-151	-0	-36	-1
-Net interest expense + Misc.	(99)	(140)	(100)	4	64
Net cash-flow	1,214	-15	-250	320	-336

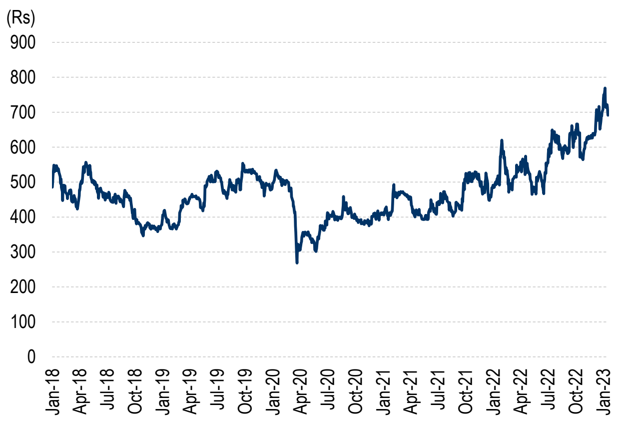
Source: Company

Fig 4 – Ratio analysis

Year-end: Mar	FY18	FY19	FY20	FY21	FY22
P/E (x)	25.1	18.3	9.0	20.0	12.0
EV / EBITDA (x)	13.8	9.8	5.4	11.3	7.2
EV / Sales (x)	1.9	1.4	0.7	1.2	1.1
P/B (x)	5.3	4.5	2.5	3.1	2.8
RoE (%)	31.4	26.8	31.2	16.8	26.6
RoCE (%)	43.8	41.3	41.1	22.2	35.5
Sales / FA (x)	9.3	10.1	13.9	7.9	8.4
DPS (Rs / sh)	2.5	5.0	10.0	-	4.0
Dividend yield (%)	0.6	1.1	3.1	-	0.7
Dividend payout (%) - incl. DDT	16.8	24.0	33.6	-	8.9
Net debt / equity (x)	-0.7	-0.5	-0.3	-0.3	-0.1
Receivables (days)	58	50	55	65	65
Inventory (days)	17	26	24	26	17
Payables (days)	61	55	53	75	54
CFO : PAT %	99.3	42.2	-6.1	121.7	31.0

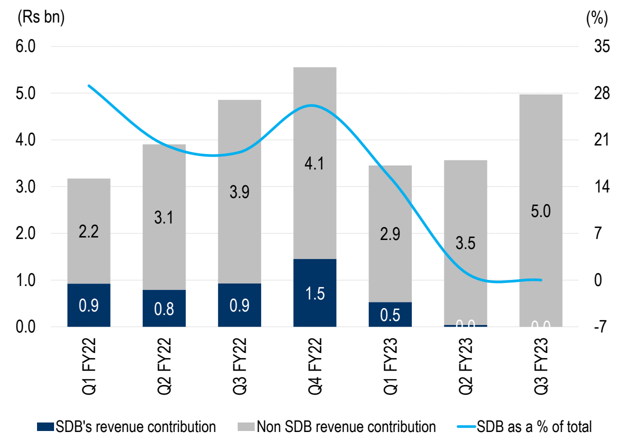
Source: Company

Fig 5 – Price movement



Source: Bloomberg

Fig 6 – Quarterly revenue trend



Source: Company

Result / concall highlights

Income statement

- **Softer execution continues.** A mere ~2% y/y higher revenue from operations (at ~Rs5bn) even on an expanded order backlog makes Q3 rather soft. This is the company's third straight quarter of soft revenue, mostly attributed to a slower-than-expected ramp-up at the recently added orders. Management sees this to change, expecting significantly better contribution from the newer orders from Q4 FY23. Sequentially, growth was strong (at ~39%), mostly owing to the monsoon-impacted pace of execution in Q2, and the gradually rising contribution from newer orders.
  - The Q3 contribution, ~Rs1.65bn (~Rs1.3bn more y/y), from the Uttar Pradesh healthcare orders was comfortably ahead of the ~Rs0.9bn recorded in the corresponding quarter last year from the then recently completed Surat Diamond Bourse. Despite this, the y/y revenue growth was muted, and could be attributed to slow progress at other orders.
  - Though the contribution from the Uttar Pradesh healthcare orders rose materially from ~Rs0.75bn in Q2, it fell short of management's own expectation of ~Rs2.5bn. Consequently, Q3 revenue from operations lagged internal estimates by ~Rs1bn.
  - For Q4, management pegged targeted revenue at ~Rs9bn. Of this, it expects the Uttar Pradesh healthcare orders to contribute ~Rs3bn, and the balance to come from the rest. The targeted revenue appears ambitious to us.
  - Q3 missing internal estimates by ~Rs1bn led to management pruning its FY23 revenue guidance to ~Rs21bn (from ~Rs22bn). Citing strong order additions in FY23, and more expected in FY24, management sees FY24 revenue at Rs26bn-27bn (~25% higher y/y).

Fig 7 – Financial highlights – Uttar Pradesh Healthcare orders, key contributor

(Rs m)	Q1 FY22	Q2 FY22	Q3 FY22	Q4 FY22	Q1 FY23	Q2 FY23	Q3 FY23	% Y/Y	% Q/Q
Sales	3,174	3,904	4,856	5,553	3,452	3,566	4,974	2.4	39.5
EBITDA	394	547	741	881	471	386	616	(16.8)	59.7
EBITDA margins (%)	*12.4*	*14.0*	*15.3*	*15.9*	*13.6*	*10.8*	*12.4*	*-286bps*	*157bps*
Interest	34	38	98	95	56	70	101	3.8	43.7
Depreciation	54	70	94	102	87	91	98	4.9	8.7
Other income	38	46	76	54	56	83	65	(14.8)	(22.2)
PBT	344	485	625	739	384	308	482	(23.0)	56.2
Tax	93	120	156	201	99	79	129	(17.7)	62.6
PAT	251	366	469	538	285	229	353	(24.8)	54.0
EPS (Rs)	7.0	10.2	13.0	14.9	7.9	6.4	9.8	(24.8)	54.0

Source: Company

- **Margin in line with guidance.** The Q3 FY23 margin compressed ~286bps y/y/, mostly on account of the high base. The margin, at ~12.4%, is healthy otherwise, and in line with management's guided-to 11-13%. Sequentially, the operating leverage helped the margin to expand ~157bps.
  - The y/y compression is owing to the higher proportion of the contribution from near-complete orders such as Shri Kashi

Vishwanath Dham and the Surat Diamond Bourse in the corresponding quarter last year. The near-complete status would have led to final cost adjustments, as well as execution of some high-value works.

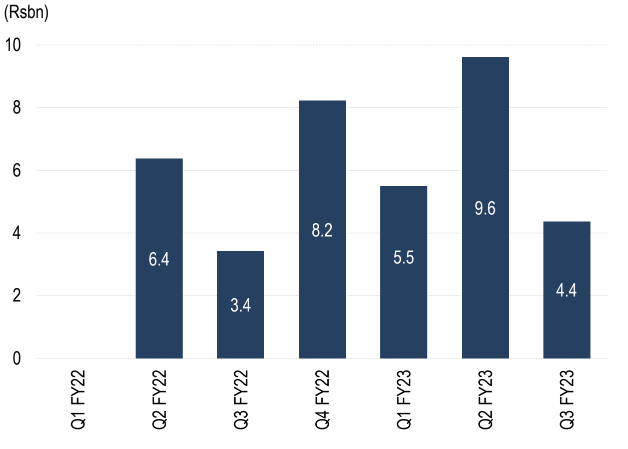
- Management yet again pegged the secular margin guidance at 11-13%.

- **Earnings, track operations.** Largely tracking movement in absolute operating profitability, net income was down ~25% y/y to ~Rs353m. Besides the lower operating profitability, the y/y drag was accentuated by reduced other income, higher depreciation, more finance costs and an elevated tax-rate. Sequentially, though, net income rose ~54% but lower other income and a higher effective tax rate confined growth.
  - Further capex required for newer projects led to more depreciation costs.
  - Finance costs were higher on greater mobilisation advances, increased utilisation of fund-based (for working capital needs) and nonfund-based limits (more bank guarantees on strong orders added).

Order backlog / inflows / scope

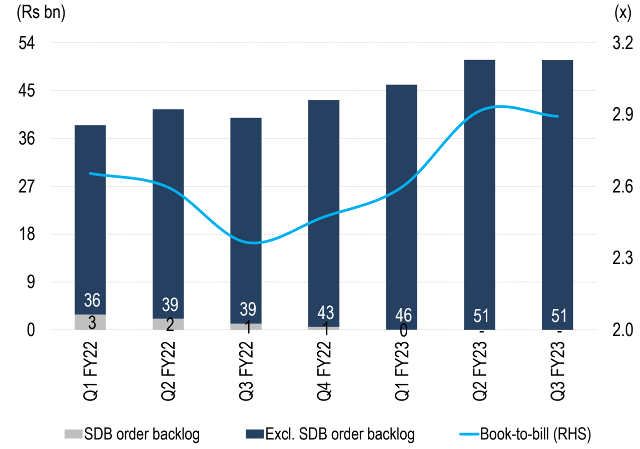
- Though the pace of execution has been relatively softer this fiscal, it has not deterred management from adding more to augment the assurance. With fresh orders of ~Rs4.4bn in Q3, 9M FY23 additions have been a healthy ~Rs19.5bn. And, with the recent (post-Q3) large order of ~Rs13.4bn from the Surat Municipal Corporation, the additions turn sturdier. Besides these, it holds L1 status in an order of ~Rs3.5bn.

Fig 8 – Q3 inflows: ~Rs4.4bn, 9M: ~Rs19.5bn, YTD: ~Rs33bn, FY23 target: Rs38bn-40bn



Source: Company

Fig 9 – End-Q3 OB: ~Rs51bn, incl. ~Rs7bn of stuck or slow moving orders

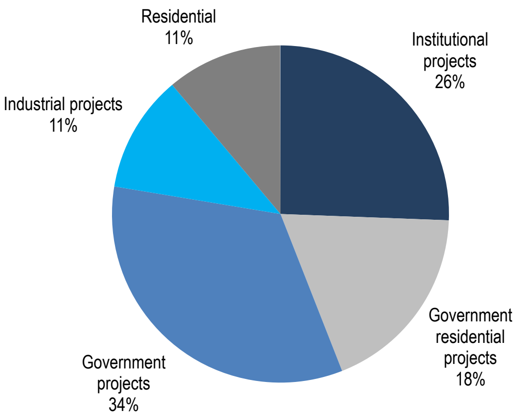


Source: Company Note: The chart denotes quarter-end or year-end figures

- Though ytd additions have been strong, Q3 additions slightly lagged the quarter's revenue. Consequently, the OB contracted ~Rs60m q/q to end Q3 FY23 at ~Rs50.8bn.
  - With only a minor q/q dip in the OB, and only slightly higher TTM revenues q/q, the book-to-bill was mostly unchanged at ~2.9x.
  - Including the post-Q3 order, the OB rises to ~Rs64.2bn, and the assurance turn sturdier (~3.7x TTM revenues). The L1 of ~Rs3.5bn, as and when firmed up, would further augment the OB and assurance.

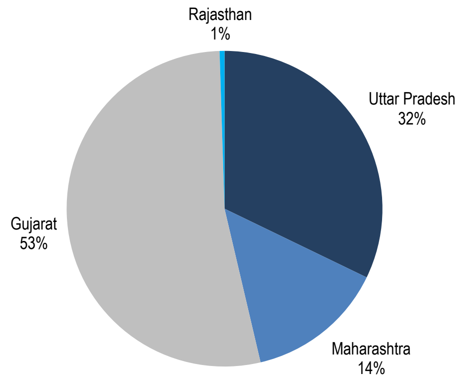
- However, both its public-sector housing projects in Maharashtra continue to be faced with execution challenges and, thus, have not been moving. The Bhiwandi project has been stuck by a delayed work-front (and, consequently, turning unviable against the quoted price), and progress at the Pandharpur order has suffered from delayed payments.

Fig 10 – Government OB, only slightly ahead of private



Source: Company Note: Break-up of the end-Q3 OB of ~Rs50.8bn

Fig 11 – Gujarat dominant, followed by Uttar Pradesh



Source: Company Note: Break-up of the end-Q3 OB of ~Rs50.8bn

- Adjusted for the above two orders (~Rs7bn combined), the OB (incl. the post-Q3 order but excl. L1) works out to ~Rs56.9bn, and the implied book-to-bill is ~3.2x TTM revenues. The assurance is good for the short to medium term.

- With strong, ~Rs33bn, orders already, management looks to close the year with total additions of Rs38bn-40bn. For this, it looks to its L1 status in an order of ~Rs3.5bn, and hopes to find success with a few more orders.
  - For FY24, management looks at more orders of ~Rs30bn. For this, it has its eyes on an immediate prospects pipeline of ~Rs45bn. These include ~Rs12bn for a gems & jewellery park in Mumbai, ~Rs12bn for the Central Vista project, ~Rs5bn for a private residential project in Delhi, ~Rs3.7bn for an IT park in Chennai, ~Rs3.3bn for the Dharoi Dam development and ~Rs3bn for an industrial project in Hazira (Gujarat).
  - The prospects pipeline is well diversified, with Gujarat accounting for ~30%; the balance ~70% are from regions other than Gujarat. Besides, private orders make up ~60% of the total, and the balance are public orders.

Balance sheet

- At end-Q3 FY23, the company had utilised ~Rs1.4bn of its working-capital limits; the term loan availed of was ~Rs0.5bn. This ~Rs1.9bn of gross debt compares to ~Rs1.6bn at end-Q2.
  - The rise in fund-based utilisation was mainly due to additional capex required for the newly bagged projects, and an increase in advances to suppliers and contractors.
- At 31st Dec'22, the company had access to fixed deposits of ~Rs3.16bn (down from ~Rs3.34bn at end-Q2). These comprised ~Rs0.60bn of unencumbered FDs (q/q down from ~Rs1.16bn), ~Rs2.53bn of FDs with liens (up from ~Rs1.99bn q/q) and ~Rs30m extended to clients as security deposits (down from ~Rs189m the quarter prior).

- Management pegs the Q3 FY22 cash-conversion cycle at 41 days. This is a sequential increase of 11 days due to more debtor days (79, up from 72 at end-Q2 FY23), and fewer creditor days (60, down from 71 at end-Q2 FY23). Inventory days, however, went down to 22 (from 29 at end-Q2 FY23).
  - Management highlights that, subsequent to the quarter, it has pruned its receivables by ~Rs1.3bn (from ~Rs4bn at end-Q3). This is likely to have normalised its cash-conversion cycle.
- Retention money, unbilled revenue and mobilisation advances rose q/q, on the greater scale of operations.
  - Retention receivables were pegged at ~Rs1.34bn (up from ~Rs1.2bn at end-Q2), unbilled revenues were ~Rs1.6bn (~Rs0.23bn higher q/q), and mobilisation advances were ~Rs1.69bn (from ~Rs1.41bn the quarter prior).
  - While the company has availed of mobilisation advances from most of the orders, it has potential to draw down mobilisation advances from its recently secured Surat Municipal Corporation project. However, these would be availed of keeping in mind the cash-flow situation.
- At end-Q3, fund-based and non-fund-based limits were pegged at ~Rs10.47bn. Of the total limits, the company had utilised ~Rs1.4bn of the fund-based limit at end-Q3 while non-fund-based utilisation was ~Rs7.18bn. Unutilised limits augur well for the targeted order additions and scale-up.

Guidance

- With ~Rs33bn of orders added already in FY23, L1 status in an order of ~Rs3.5bn and a healthy prospect pipeline, management looks to close this year with order additions of Rs38bn-40bn (against the earlier guidance of ~Rs25bn).
  - The strong prospects pipeline of ~Rs45bn, and as bidding for these is most likely in FY24, management looks to add orders of ~Rs30bn in FY24.
- Management says that it internally envisaged ~Rs1bn more revenue in Q3 FY23. With this miss, it lowered its FY23 revenue guidance to ~Rs21bn (from the earlier guided-to ~Rs22bn).
  - It expects the Uttar Pradesh healthcare orders to contribute ~Rs3bn in Q4 (against ~Rs1.65bn in Q3) in the total ask of ~Rs9bn.
  - For FY24, the company is aiming at ~25% y/y growth (Rs26bn-27bn), and expects the targeted new orders of ~Rs30bn in FY24 would suffice.
- On EBITDA margins, it retained its 11-13% guidance for FY22.
- Though it aims at a significant jump in scale of operations in Q4, it does not see its gross debt (~Rs1.9bn at end-Q3, up ~Rs0.3bn q/q) to rise in tandem. It sees advances extended to vendors for MEP supplies at Uttar Pradesh healthcare orders to help contain the working capital required.

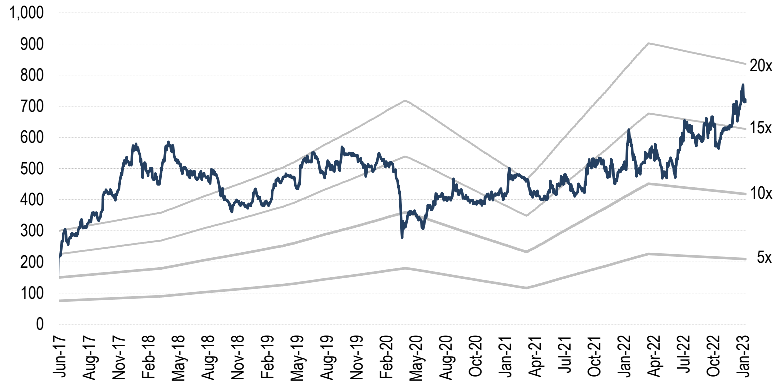
Project updates

- **The medical college and hospitals at seven locations in UP.** At this ~Rs14.9bn aggregate order, the company booked ~Rs1.7bn revenue in Q3 FY23 and ~Rs2.7bn in 9M FY23. Cumulative recognition is pegged at ~Rs4.2bn. Execution, however, was curbed by delays in certain approvals related to MEP from Project Management Consultants and a client, which compressed potential revenue by ~Rs1bn during Q3 FY23. With this behind, management looks to hit a monthly revenue run-rate of ~Rs1bn in Q4 FY23.
- **The Bhiwandi EWS housing project.** Secured in Q1 FY20, this long-delayed project entailed ~Rs6bn revenue potential. However, execution could not be taken up for want of work-front / approvals.
  - Significant delays have led to changes in cost estimates. Management was in touch with the client to seek approval for cost escalations or to terminate the project. If the company's terms are agreed with, it will continue with the project.
  - The Authority earlier served the company with a show-cause notice.
  - The company approached a court of law seeking a stay against the invoking of bank guarantees (of ~Rs67m) furnished to the client. The court declared a stay.
  - The case is in the advanced stage, and an arbitrator is likely be selected at the next hearing.
- **The Pandharpur affordable-housing project.** Delayed payments led to management halting work at the site. The balance executable potential on 31st Dec 22 was estimated at ~Rs1.3bn.
- **The Surat Municipal Corporation order.** The company was recently awarded (Jan'23) an order by the Surat Municipal Corp to construct twin towers that will house the administrative and other departments. The order is valued at ~Rs13.4bn.
  - At this project, the scope is to build two 27-storey buildings (0.22m sq.mtrs.) over the next 36 months. Most of the land is available currently.
  - Management expects execution to begin in the next 1 to 1.5 months. With this, management guided to Rs3bn-3.5bn revenues from this order in FY24 and near-equal revenue in the next two years.

Valuation

At the ruling price, the stock trades at 17.7x TTM EPS of Rs39. We do not have a rating on the company. Its well-managed balance sheet, proven execution abilities and healthy return ratios augur well. The recent soft growth, we believe, is temporary, and we see PSP to return to optimal growth sooner than later as the recent orders seem set to contribute better ahead. The healthy prospects pipeline suggests that growth beyond, too, is unlikely to be a challenge.

Fig 12 – PE band



Source: Bloomberg, Anand Rathi Research

Risks

- Failure to ramp-up the pace of execution.
- Failure to maintain prudence.

Appendix

Analyst Certification

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Ratings Guide (12 months)

	Buy	Hold	Sell
Large Caps (>US$1bn)	>15%	5-15%	<5%
Mid/Small Caps (<US$1bn)	>25%	5-25%	<5%

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ARSSBL registered address: Express Zone, A Wing, 9th Floor, Western Express Highway, Diagonally Opposite Oberoi Mall, Malad (E), Mumbai – 400097.
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