

## MBL Infrastructure and KNR Construction

### Beneficiaries of a pick-up in road capex - Company Visit Note

Road project awards gathered momentum in FY15 and have accelerated in FY16. MoRTH is targeting 10,000km to be awarded in FY16 vs. 8,000km in FY15 and 3,600km in FY14. NHAI's Chairman recently stated that they have awarded 2,500km in FY16TD i.e. ~50% of the target; with project value already more than that in FY15. With several projects on the anvil, ordering outlook for E&C contractors like KNR Construction (Rs38bn OB, Rs23bn BOT Portfolio) and MBL Infrastructure (Rs37bn OB, Rs10bn BOT Portfolio) appears bright. KNR has tripled its OB in 1H FY16, whereas MBL is expecting >100% growth in orders this year. KNR/MBL have outperformed the Sensex by 118%/44% in the past year, while also outperforming road asset owners (IRB, ITNL, Ashoka Buildcon), conglomerates (RELI, GMR, GVK) as well as E&C companies with more diversified order books (L&T, Sadbhav Engg).

- **Pick-up in road orders to drive revenue growth in FY17.** As per MBL, Rs500bn of road contracts are to be awarded by the Govt. in the next 6 months. Mgmt is confident of the Govt's reform efforts translating into a pick-up in road capex over the next 3-4 years. MBL's FY15 OB was up by 18% and mgmt expects >100% growth in inflows in FY16. KNR's OB has tripled between Mar and Aug 2015 – they have won ~1/3<sup>rd</sup> of NHAI's EPC contracts (by value) awarded until July (L&T leads the pack). KNR is aiming for more inflows in FY16 followed by a ~40% jump in execution in FY17.
- **Expecting stable margins on new orders.** MBL reported 11.5% EPC margin in FY15, while KNR's margin was higher at 14.4% with backward integration for raw material. MBL's mgmt expects margins of 11-14% on new EPC contracts, while KNR too aims to maintain its EPC margins at 13-14%.
- **Exposure to state projects impacts working capital for MBL.** KNR's OB has an almost equal mix of NHAI and state projects, while 79% of MBL's is state projects. Thus KNR's receivable cycle is shorter (~40 days) compared to MBL's (60-70 days). MBL also maintains a large inventory. With a 180 day working capital cycle, MBL's interest cost was ~50% of EBITDA and operating cash flow negative. Management wants to trim working capital by 50-60 days.
- **BOT portfolio expansion put on hold.** While BOT project awards by NHAI have picked up, MBL and KNR are not keen on expanding their portfolio. MBL expects its three under construction BOT roads to be operational by June'16 (6% of FY17 revenue based on consensus estimate), post which they may bid for more. KNR is targeting only EPC orders and may exit one of the two BOT projects upon completion which would contribute 8% of FY17 revenue based on consensus estimates.
- **Being low leverage, relatively asset light and with concentrated OB exposure to roads, KNR and MBL outperform peers.** KNR is trading at 22x FY17 P/E i.e. almost at the top of the range for EPC companies and road asset owners, with 43% earnings growth in FY17 based on consensus with net D/E of 0.8x. MBL is trading at a lower 12x FY17 P/E with 5% earnings growth in FY17 based on consensus with leverage at 1.6x.

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#### MBL IN, Not Covered

INR 244, October 6, 2015

#### Five-year share price chart



Source: Bloomberg.

#### One-year price performance - MBL

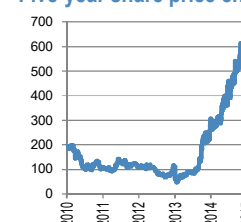
	1M	3M	12M
Absolute (%)	6	(15)	47
Relative (%)	(2)	(11)	44

Source: Bloomberg.

#### KNR IN, Not Covered

INR 598, October 6, 2015

#### Five-year share price chart



Source: Bloomberg.

#### One-year price performance - KNR

	1M	3M	12M
Absolute (%)	15	3	120
Relative (%)	7	7	118

Source: Bloomberg.

**MBL Infrastructures Ltd. (Reuters: MBLI.NS, Bloomberg: MBL IN), Historical financial data**

INR, year-end March	FY13	FY14	FY15
Sales	13,554	17,663	19,618
EBITDA	1,434	1,882	2,369
Net Income	566	770	816
EPS	16.2	22.0	22.1
BPS	113.6	133.9	158.2
Return on equity	15.2	17.8	14.5
Return on invested capital	9.7	9.9	9.2
PE ratio	15.1	11.1	11.1
Price-to-book ratio	2.1	1.8	1.5
EV/EBITDA	11.2	9.4	8.6
Dividend payout ratio	4.6	3.4	3.4
DPS	1.5	1.5	1.5

Source: Company Reports, Bloomberg. Price as on 6 October 2015.

**Company data - MBL**

52-wk range (INR)	150-329.5
Mkt cap. (INR B)	10.3
Mkt cap. (US\$ MM)	158.2
Shares O/S (MM)	41.50
Free float (%)	46%
Avg. daily value (US\$ MM)	0.19
Avg. daily volume (MM shr)	0.05
Sensex	27,036
Exchange rate (USDINR)	65.1
Year-end	March

Source: Bloomberg

**KNR Constructions Ltd. (Reuters: KNRL.NS, Bloomberg: KNRC IN), Historical financial data**

INR, year-end March	FY13	FY14	FY15
Sales	7,650	8,950	9,312
EBITDA	1,166	1,314	1,268
Net Income	491	605	698
EPS	17.5	21.5	24.8
BPS	165.0	217.4	280.6
Return on equity	11.1	11.3	10.0
Return on invested capital	4.5	5.1	4.1
PE ratio	34.3	27.8	24.1
Price-to-book ratio	3.6	2.8	2.1
EV/EBITDA	20.6	12.8	13.3
Dividend payout ratio	5.7	4.6	4.0
DPS	1.0	1.0	1.0

Source: Company reports. Price as on 6 October 2015.

**Company data - KNR**

52-wk range (INR)	260-625
Mkt cap. (INR B)	17.0
Mkt cap. (US\$ MM)	261.4
Shares O/S (MM)	28.1
Free float (%)	38%
Avg. daily value (US\$ MM)	0.26
Avg. daily volume (MM shr)	0.03
Sensex	27,036
Exchange rate (USDINR)	65.1
Year-end	March

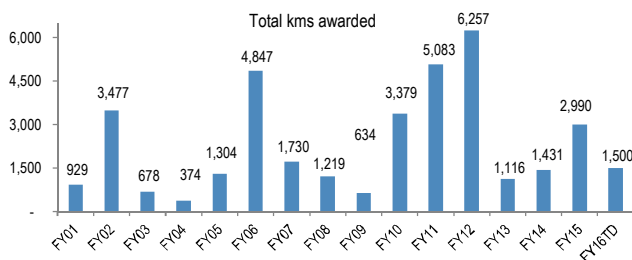
Source: Bloomberg.

## Road project ordering accelerates in FY16

Road project awards gathered momentum in FY15 (see Figures 1 and 2 below) and have accelerated in FY16. MoRTH ordered out ~8,000km in FY15 vs. 3,600km in FY14 including 3,000km by NHAI i.e. 2x of FY14. In total 10,000km are to be awarded in FY16 and there are an additional 15,000-20,000km worth of projects are on the anvil, providing opportunities for road E&C companies to grow their order book. In a recent interview (Economic Times) NHAI's Chairman stated that they have awarded 2,500km of projects to date i.e. ~50% of the target of 5,100km for FY16; project cost of stretches awarded until Jul'15 (Rs193bn) has surpassed the total project cost of 3,000km awarded in FY15 (Rs117bn).

**Figure 1: NHAI: Projects awarded by volumes**

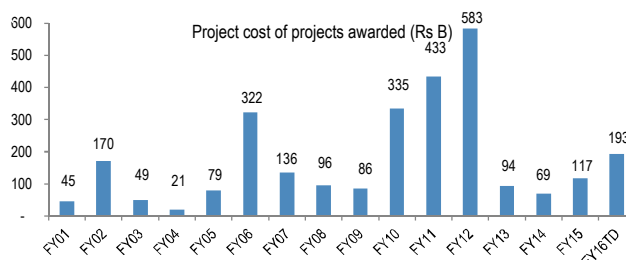
in kms, year end March



Source: NHAI, J.P.Morgan. FY16 data till July'15.

**Figure 2: NHAI: Project awarded by value**

In Rs billion, year end March



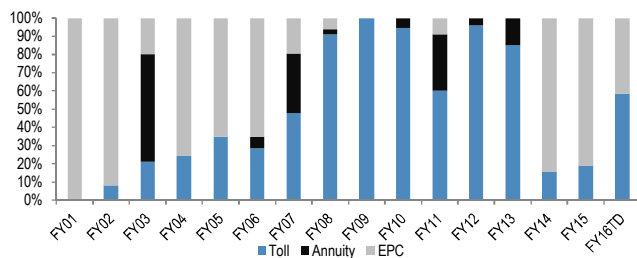
Source: NHAI, J.P.Morgan. FY16 data till July'15.

In FY15, the appetite for BOT projects was muted – 80% of road contracts by length and 75% by value were awarded through the EPC route (see Figures 3 and 4).

However, in FY16, from the data published by NHAI until July, of the 1,500km of road projects awarded with a project cost of Rs193bn, 870km (Rs130bn of project cost) were awarded under BOT Toll route and 630km (Rs64bn of project cost) via the EPC route.

**Figure 3: NHAI: Project mix (in kms)**

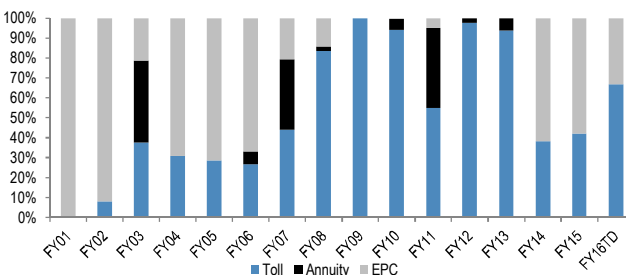
Year end March



Source: NHAI, J.P.Morgan. FY16 data till July'15.

**Figure 4: NHAI: Project mix (in Rs bn)**

Year end March



Source: NHAI, J.P.Morgan. FY16 data till July'15.

Order books of road contractors have grown in the past 18 months. See Table 1 below.

**Table 1: Order Book growth for E&C contractors with exposure to roads sector**

Rs. in million, year end March

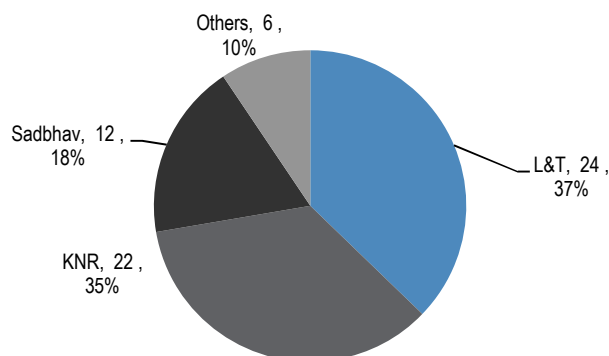
	FY11	FY12	FY13	FY14	FY15	1QFY16
KNR	14,434	30,420	26,291	12,960	13,181	35,409
MBL	10,699	25,222	29,919	32,049	37,708	37,241
Sadbhav	65,868	72,137	96,025	89,407	82,000	84,651
IL&FS	109,500	120,573	146,717	NA	119,038	157,908
IRB	117,412	85,150	84,322	113,480 <sup>(a)</sup>	126,310	121,160
Ashoka Buildcon	46,720	49,670	35,680	35,460	31,060	28,328
Gayatri Projects	83,006	98,300	80,360	72,735	59,680	69,100
J Kumar Infraprojects	12,662	25,125	36,610	31,409	30,240	43,119
Nagarjuna Construction	161,800	201,950	185,540	209,560	193,230	187,270
<b>Domestic Road Order Inflows reported</b>	<b>FY11</b>	<b>FY12</b>	<b>FY13</b>	<b>FY14</b>	<b>FY15</b>	<b>FY16TD</b>
L&T	14,500	53,700	26,850	24,090	65,110	36,740

Source: Company reports. Note: (a) As of June of the next financial year. (b) In August Gayatri Projects has won Rs33.2bn of new NHAI contracts.

In FY15 and FY16TD, L&T leads in market share of EPC road contracts won by value. In FY16TD, order wins so far have been more concentrated vs. FY15 (see Figures 5 and 6 below).

**Figure 5: Market share of EPC contracts awarded by NHAI in FY16TD (in value terms)**

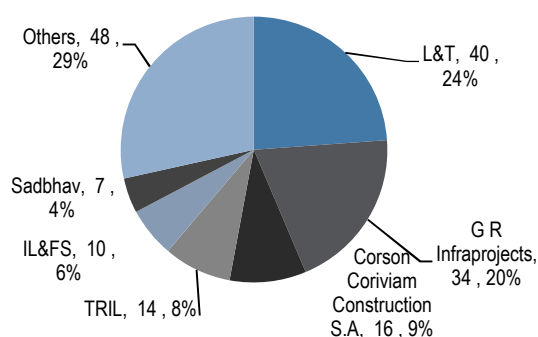
Rs. in billion



Source: NHAI, J.P. Morgan. FY16 data till July'15.

**Figure 6: Market share of EPC contract awarded by NHAI in FY15 (in value terms)**

%

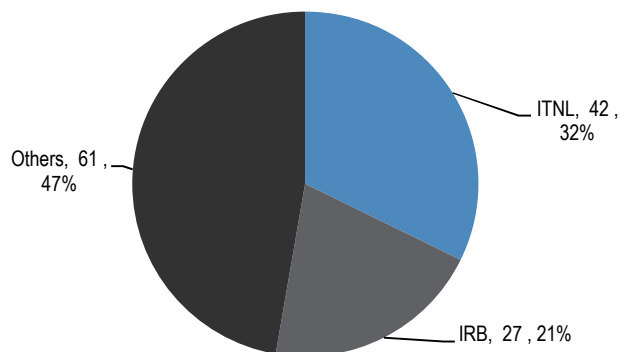


Source: NHAI, J.P. Morgan.

Amongst listed players, ITNL and IRB continue to bid for and win BOT projects. Other construction companies including L&T are predominantly bidding in the EPC space and has not won any BOT project in the past 18 months (see Figures 7 and 8 below).

**Figure 7: Market share of BOT contracts awarded by NHAI in FY16TD (in value terms)**

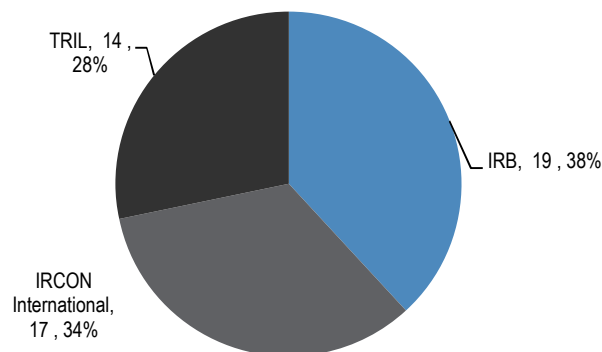
Rs. in billion



Source: NHAI, J.P. Morgan. FY16 data till July'15.

**Figure 8: Market share of BOT contract awarded by NHAI in FY15 (in value terms)**

%



Source: NHAI, J.P. Morgan.

## EPC contractors to benefit from ordering momentum - Key takeaways from meetings with KNR Construction and MBL Infrastructure

### Road ordering activity has picked up, revenue growth to follow suit in FY17

As per MBL management, ~Rs500bn of road contracts are expected to be awarded by NHAI and MoRTH in the next 6 months. Management is confident of the current Government's reform efforts translating into a pick-up in road capex over the next 3-4 years.

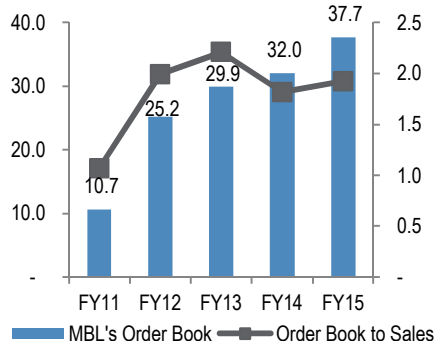
MBL's order book grew by 18% yoy in FY15 to Rs38bn. In FY16, MBL is expecting order inflow of Rs35bn vs. Rs16bn in FY15; Rs2bn or orders have been received in FY16TD. As per management, while they have been conservative in bidding for projects thus far, they expect to be L1 in a few projects in FY16 with the gap narrowing as compared to competitors.

With current OB/Sales at ~2x, the company has revenue visibility for at least 2 years. MBL has had revenue CAGR of 18% over the past four years. In case the company can double its inflows this year, we could see a spurt in revenue growth in FY17.

MBL has bids outstanding for Rs75bn worth of projects of which >70% is from the roads sector including NHAI, MoRTH and state projects (West Bengal, Uttarakhand, Madhya Pradesh and Bihar).

**Figure 9: MBL: Order Book growth**

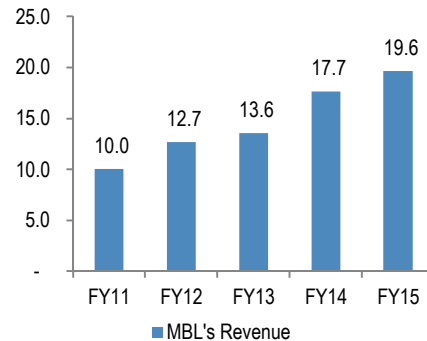
Rs. in billion, year end March



Source: Company reports.

**Figure 10: MBL: Revenue growth**

Rs. in billion, year end March



Source: Company reports.

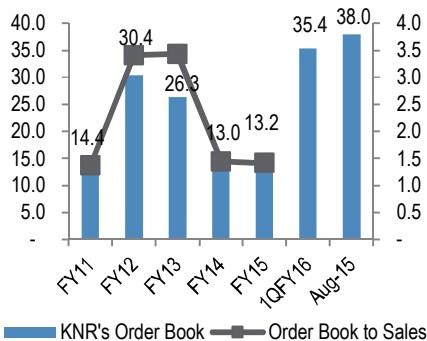
KNR has tripled its order book in the past 6 months, increasing from Rs13.2bn as of Mar'15 to Rs38bn in August with an inflow of Rs16bn of NHAI projects and Rs10bn of state projects (funded by multilateral agencies).

Of the FYTD NHAI awarded EPC contracts of Rs64bn, KNR has had a 35% market share (Rs22bn). The company is attempting at securing another Rs10bn worth of projects in FY16. In FY17, the company is targeting to at least equate orders to execution to keep the order book stable.

KNR has had standalone revenue CAGR of 3% over the past four years. With the OB tripling in FY16TD, management is expecting topline of Rs13bn in FY17 i.e. +40% compared to FY15. In FY16, management expects topline to be flat.

**Figure 11: KNR: Order Book growth**

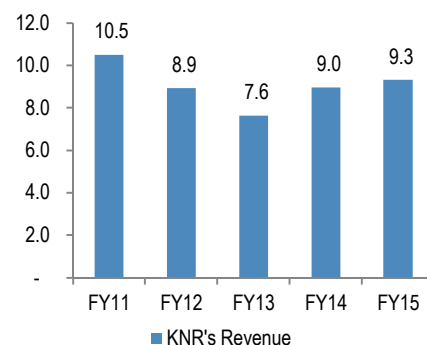
Rs. in billion, year end March



Source: Company reports.

**Figure 12: KNR: Revenue growth**

Rs. in billion, year end March



Source: Company reports.

As of June'16, 46% of KNR's OB comprised of NHAI projects and 43% state projects with ~88% of total projects in South India. For MBL, 79% of the OB comprised of state projects and only 6% from NHAI projects. MBL has a stronger presence in North and East India.

### Order book to be driven via the external contracts as BOT portfolio expansion put on hold

MBL expects its three under construction BOT projects (Rs4bn, 11% of order book) to be operational by June 2016, after which they will look to participate in bidding for more projects. Until then, the focus will be on securing more EPC contracts. The company wants to participate in road projects of both states (but funded by multilateral agencies) and NHAI with a ticket size of Rs2-10bn; however expects exposure to NHAI projects (only 6% of OB) to increase.

KNR is targeting only EPC contracts (of >Rs5bn ticket size since competition is lesser) and not looking at expanding its BOT portfolio at the moment. Only 1% of its OB is from captive BOT projects. Amongst state projects, KNR is also looking at those that are funded by multilateral agencies.

### Order inflow gains expected at stable margins

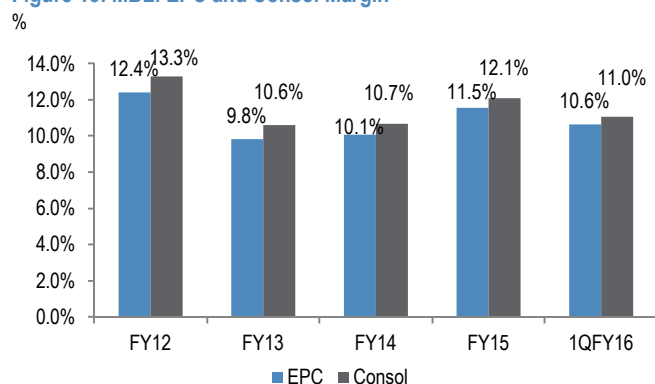
MBL reported 11.5% EPC margins in FY15 (+150bps yoy). MBL has improved its EPC margin over the past two years given its careful selection of projects, bidding for selective clients (projects with multilateral funding i.e. ADB, World Bank), its integrated business model (own equipment), raw material cost savings and working capital management. For its captive BOT contracts, they have benefited from a decrease in RM prices over the last two years given the orders are fixed price. In EPC contracts, the company does not bear the risk of RM price fluctuation; any escalation is passed on to the customers.

Management is expecting margins of 11-14% on new EPC contracts. While off late they have not won any contracts given their conservative bidding, they expect to be L1 in some projects soon with the bid gap narrowing as compared to competitors.

As per MBL, currently there are 6-7 bidders per projects. Overall there are 53 players vs. 147 about 2 years ago with 20 bidders per project.

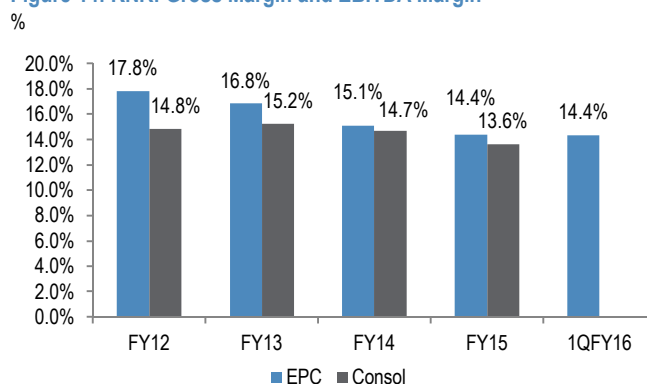
KNR's margin has been higher at 14%+ given their backward integration; KNR sources aggregates from its own mines, for road projects under execution enabling them to control costs. Also, KNR has a track record for in-time execution, enabling them to get bonus payments at times. KNR aims to maintain EPC margins at 13-14% on new contracts as well.

Figure 13: MBL: EPC and Consol Margin



Source: Company reports and J.P. Morgan.

Figure 14: KNR: Gross Margin and EBITDA Margin



Source: Company reports and J.P. Morgan.

## Expected BOT Portfolio Performance

MBL expects its three under construction BOT projects to be operational by June 2016, with a project IRR of 15%. Management expects topline contribution of Rs1.7bn in FY17 and Rs2.1bn in FY18 from its BOT portfolio vs. Rs0.2bn reported in FY15 (1% of consol revenue) from its one operational road project. Management expects these projects to make cash profits from day one and to recover equity in 6.5 years.

Table 2: MBL's Road Portfolio

	Operational		Under Construction		
	Seoni-Balaghat-Rajegaon	Waraseoni-Lalbarra	Seoni-Katangi	Garra-Waraseoni	Bikaner-Suratgarh
Length (kms)	114.0	18.3	75.6	46.9	172.4
State	Madhya Pradesh	Madhya Pradesh	Madhya Pradesh	Madhya Pradesh	Rajasthan
Concession Period (years)	15	15	30	15	16
Type	Toll	Toll + Annuity	Toll	Toll + Annuity	Toll
Expected CoD	Feb 2008	Aug 2015	June 2016	June 2016	June 2016
Project Cost (Rs mn)	1,082	569	2,116	1,368	6,201
Equity (Rs mn)	120	150	816	398	1,701
Debt (Rs mn)	500	419	1,300	970	4,500
Equity As on 31st March '15	120	150	511	398	900
Debt as on 31st March '15	281	485	806	0	2,373
% complete	100%	100%	93%	30%	42%

Source: Company reports.

Table 3: P&L of Seoni-Balaghat-Rajegaon road

Rs. in million, year end March

	FY12	FY13	FY14	FY15	1QFY16
Revenue	142	162	177	192	51
% yoy		14%	9%	8%	11%
% of consol revenue	1%	1%	1%	1%	1%
EBITDA	126	120	120	126	30
% Margin	88%	74%	68%	66%	59%
PAT	17	13	19	18	5
% of consol PAT	2%	2%	2%	2%	2%

Source: Company reports, J.P.Morgan.

KNR has two operational annuity projects with a 40% stake in each. Additionally, the company has two toll road projects under construction:



(1) **Muzaffarpur Barauni Tollway** – The Rs3.6bn project is expected to be complete by December but has been delayed by 1 year and has had a cost overrun. KNR wants to exit the project on CoD. Management estimates a project IRR of ~13%.

(2) **Walayar Tollways** – The Rs9bn project is expected to be completed this month itself despite; while partial tolling commenced in June, the current traffic is ~25% below target. Management estimates a project IRR of ~16%.

Both the projects are expected to Rs1.2bn in annual revenue i.e. 13% of FY15 topline and 8% of FY17 revenue based on consensus estimate.

Table 4: KNR's Road Portfolio

	Operational		Under Construction	
	Patel KNR Infrastructures	Patel KNR Heavy Infrastructures	KNR Walayar Tollways	KNR Muzaffarpur Barauni Tollway
Stake	40%	40%	100%	51%
Length (kms)	60	53	54	108
State	Karnataka	Telangana	Kerala	Bihar
Concession Period (years)	20	20	20	21
Type	Annuity	Annuity	Toll	Toll
Expected CoD	December 2009	June 2010	Nov 2015	Dec 2015
Project Cost (Rs mn)	4,420	5,920	9,005	3,597
Equity As on June '15	370	497	3,677	1,072
Debt as on June '15	3,341	4,847	4,598	2,346
% complete	100%	100%	96%	87%
Annual Revenue (Rs mn)	329	444	783	438

Source: Company reports, J.P.Morgan.

## Roads sector to continue to be the mainstay of the EPC OB

71% of MBL's OB and 98% of KNR's OB is exposed to the roads sector.

KNR's focus continues to be on the roads sector alone given limited orders available in irrigation.

15% of MBL's OB is comprised of housing and buildings and 4% is railways. MBL is planning to bid for Nagpur, Ahmedabad, Bangalore and Delhi metro projects. MBL is also trying to make inroads into the inland water transport segment by signing a JV Piacentini Costruzione, an Italian company engaged in the construction and civil engineering in maritime works. MBL has started bidding for port projects (Chennai, Mumbai and Mangalore) and will also bid for the Rs42bn inland waterway project of Allahabad to Haldia which will be completed over 6 years. However, >70% of MBL's outstanding bids are roads projects.

## Financials

Almost all of MBL's topline as of FY15 was composed of EPC revenues with only one operational BOT project. EPC revenues have grown at a CAGR of 16% over the past three years to Rs19.4bn, while the OB has grown at a CAGR of 14% to Rs38bn.

As of FY15 OB/Sales stood at 1.9x. If MBL wins 2x orders in FY16 as compared to FY15 (management expects Rs35bn vs. Rs16bn), we will see an uptick in EPC revenue growth FY17 onwards.

MBL has reported 10-12% EPC margins over the past four years, consolidated margins have been slightly higher with the BOT project.

Given the high interest expense of Rs1bn in FY15 (on Rs11bn of debt), PAT Margin was 4%, steady over the past three years.

Table 5: MBL: Summary P&L

Rs. in million, year-end March

	FY12	FY13	FY14	FY15
<b>Revenue from operations</b>	<b>12,653</b>	<b>13,554</b>	<b>17,663</b>	<b>19,618</b>
% yoy	26	7	30	11
EPC	12,511	13,392	17,486	19,426
% yoy		7	31	11
BOT	142	162	177	192
% yoy		14	9	8
Cost of materials consumed	9,590	9,542	13,762	15,169
<b>Gross Profit</b>	<b>3,062</b>	<b>4,012</b>	<b>3,901</b>	<b>4,449</b>
% Margin	24.2%	29.6%	22.1%	22.7%
Employee benefits expense	175	226	269	367
Other expenses	1,209	2,352	1,750	1,712
<b>EBITDA</b>	<b>1,679</b>	<b>1,434</b>	<b>1,882</b>	<b>2,369</b>
% Margin	13.3%	10.6%	10.7%	12.1%
EPC EB ITDA	1,553	1,314	1,761	2,243
% Margin	12.4%	9.8%	10.1%	11.5%
BOT EBITDA	126	120	120	126
% Margin	88.4%	74.1%	67.9%	65.6%
Depreciation and amortisation expenses	113	111	141	202
<b>EBIT</b>	<b>1,566</b>	<b>1,323</b>	<b>1,741</b>	<b>2,168</b>
Finance costs	531	577	753	1,011
Other income	22	16	42	31
<b>PBT</b>	<b>1,056</b>	<b>762</b>	<b>1,030</b>	<b>1,188</b>
Current tax	280	154	215	249
Tax for Earlier Year	-	3	-	55
Deferred tax	51	38	44	67
<b>Total Taxes</b>	<b>331</b>	<b>196</b>	<b>260</b>	<b>372</b>
% Rate	31.4%	25.7%	25.2%	31.3%
<b>PAT</b>	<b>725</b>	<b>566</b>	<b>770</b>	<b>816</b>
<b>EPS (Rs)</b>	<b>20.7</b>	<b>16.2</b>	<b>22.0</b>	<b>22.1</b>
Shares O/s	35.0	35.0	35.0	41.5

Source: Company reports and J.P. Morgan estimates.

Post the equity raise of Rs1.2bn in FY15, MBL's D/E stood at 1.7x.

However, the company is yet to incur Rs4.7bn of capex on the under construction road projects, implying additional debt of Rs3.6bn, hence the company's leverage will continue to increase until FY17.

Working capital days increased to ~180 days in FY15 with the sharp increase in inventory as well as debtor days. As per management, they increased the inventory given the low commodity prices. Management is targeting to reduce inventory by 50 – 60 days.

On the increased equity base, MBL generated 15% RoE in FY15 and 9% RoCE.

Table 6: MBL: Summary Balance Sheet

Rs. in million, year-end March

	FY12	FY13	FY14	FY15
Share capital	175	175	175	207
Reserves and surplus	3,296	3,801	4,510	6,358
Minority interest	-	0	320	0
<b>Non-Current Liabilities</b>				
Long-term borrowings	1,547	2,774	3,705	4,725
Deferred tax liabilities (Net)	259	298	342	409
Other long-term liabilities	262	428	393	787
Long-term provisions	8	9	10	13
<b>Current Liabilities</b>				
Short-term borrowings	2,873	3,669	4,016	5,900
Trade payables	218	976	1,801	2,288
Other current liabilities	1,000	1,016	1,345	1,183
Current Maturities	252	323	558	417
Short-term provisions	374	85	156	316
<b>Total</b>	<b>10,012</b>	<b>13,231</b>	<b>16,772</b>	<b>22,186</b>
Gross Fixed Assets	2,154	2,477	2,868	3,103
Net Tangible assets	1,112	1,368	1,663	1,743
Net Intangible assets	558	518	475	428
Intangible Assets under development	703	2,088	3,759	5,407
Non-current investments	1	196	196	237
Long-term loans and advances	27	5	13	17
Other non-current assets	132	58	149	589
<b>Current Assets</b>				
Inventories	4,488	4,912	5,589	8,105
Trade receivables	1,710	2,535	3,182	3,949
Cash and cash equivalents	685	766	682	760
Short-term loans and advances	517	723	983	876
Other current assets	79	62	80	73
<b>Total</b>	<b>10,012</b>	<b>13,231</b>	<b>16,772</b>	<b>22,186</b>
Total Debt	4,672	6,767	8,279	11,042
D/E	1.35	1.70	1.77	1.68
Net Debt	3,987	6,001	7,597	10,282
Net D/E	1.15	1.51	1.62	1.57
Current assets ex cash	6,795	8,231	9,834	13,004
Current liab ex debt	1,340	1,753	2,743	3,370
Working Capital	5,455	6,478	7,090	9,634
Days	157	174	147	179
Inventory Days	129	132	115	151
Debtor Days	49	68	66	73
L&A Days	15	19	20	16
Payable Days	6	26	37	43
BVPS (INR)	99	114	134	158
RoE (%)	23	15	18	15
RoCE (%)	14	10	10	9

Source: Company reports and J.P. Morgan estimates.

Given the sharp increase in inventory, operating cash flow declined further in FY15.

Additionally, the company is incurred capex on its BOT portfolio translating into negative FCF over the past four years.

MBL is yet to incur Rs4.7bn of capex with an equity investment of Rs1.1bn on its three under construction projects which get completed in FY17.

EPC revenues have grown at a CAGR of 5% over the past three years to Rs8.8bn, while the OB has declined by a CAGR of 24% to Rs13bn given the cancellation of GMR/GVK subcontracts in FY14.

With influx of new orders, OB is now Rs38bn, which implies 4.3x FY15 EPC revenue.

Management expects FY16 topline to be flat yoy with 1Q declining -28% yoy and 2Q also expected to be weak. Typically it takes 4-5 months to commence execution on new contracts hence management is expecting a pick-up in FY17 with a Rs13bn topline i.e. +40% compared to FY15.

KNR expects to maintain its EBITDA margin at 13-14%. KNR benefits from sourcing aggregates from its own mines.

With the commissioning of road projects in FY16, interest costs will increase FY17 onwards. Both the projects will have a combined debt of ~Rs7-8bn with a funding cost of ~12%.

Table 7: MBL: Summary Cash Flow

Rs. in million, year-end March

	FY12	FY13	FY14	FY15
Net income	725	566	770	816
Depreciation & Amortization	113	111	141	202
Change in working capital	(1,808)	(1,024)	(612)	(2,544)
Taxes	(331)	(196)	(260)	(372)
Net interest	(509)	(561)	(711)	(980)
<b>Cash flow from operations</b>	<b>(1,810)</b>	<b>(1,103)</b>	<b>(673)</b>	<b>(2,878)</b>
Capex	(677)	(1,708)	(2,062)	(1,883)
Investments	(1)	(196)	0	(41)
<b>Cash flow from investing</b>	<b>(677)</b>	<b>(1,904)</b>	<b>(2,062)</b>	<b>(1,924)</b>
Equity raised/(repaid)	0	0	0	1,126
Debt raised/(repaid)	1,854	2,095	1,513	2,763
Other	0	1,046	1,191	1,052
Dividends	(53)	(53)	(53)	(62)
<b>Cash flow from financing</b>	<b>2,873</b>	<b>3,088</b>	<b>2,651</b>	<b>4,879</b>
Beginning cash	299	685	766	682
Change in cash Flow	386	81	(83)	77
Ending cash	685	766	682	760

Source: Company reports and J.P. Morgan estimates.

Table 8: KNR: Summary P&L

Rs. in million, year-end March

	FY12	FY13	FY14	FY15
<b>Revenue from operations</b>	<b>8,922</b>	<b>7,650</b>	<b>8,950</b>	<b>9,312</b>
% yoy	(15)	(14)	17	4
<b>EPC</b>	<b>7,505</b>	<b>6,921</b>	<b>8,348</b>	<b>8,761</b>
% yoy	(5)	(8)	21	5
<b>BOT</b>	<b>1,417</b>	<b>729</b>	<b>602</b>	<b>551</b>
% yoy	(45)	(49)	(17)	(9)
Cost of materials consumed	7,067	6,010	7,075	7,233
<b>Gross Profit</b>	<b>1,855</b>	<b>1,640</b>	<b>1,876</b>	<b>2,079</b>
% Margin	20.8%	21.4%	21.0%	22.3%
Employee benefits expense	302	296	352	382
Other expenses	231	178	210	429
<b>EBITDA</b>	<b>1,323</b>	<b>1,166</b>	<b>1,314</b>	<b>1,268</b>
% Margin	14.8%	15.2%	14.7%	13.6%
EPC EBITDA	1,338	1,164	1,258	1,261
% Margin	17.8%	16.8%	15.1%	14.4%
Depreciation and amortisation expenses	556	560	586	552
<b>EBIT</b>	<b>767</b>	<b>607</b>	<b>728</b>	<b>716</b>
Finance costs	118	121	179	130
Other income	111	185	172	129
<b>PBT</b>	<b>760</b>	<b>671</b>	<b>721</b>	<b>715</b>
Current tax	288	201	147	118
Deferred tax	(20)	(43)	(82)	(121)
<b>Total Taxes</b>	<b>268</b>	<b>157</b>	<b>65</b>	<b>(3)</b>
% Rate	35.3%	23.5%	9.1%	-0.4%
<b>PAT</b>	<b>492</b>	<b>513</b>	<b>655</b>	<b>718</b>
Share of profit / (loss) from Associates	(42)	(23)	(51)	(20)
Prior year share of profit from Associates	18	-	-	-
Minority Interest	0	-	0	0
<b>PATAMI</b>	<b>468</b>	<b>491</b>	<b>605</b>	<b>698</b>
<b>EPS (Rs)</b>	<b>16.6</b>	<b>17.5</b>	<b>21.5</b>	<b>24.8</b>
<b>Shares Outstanding</b>	<b>28.1</b>	<b>28.1</b>	<b>28.1</b>	<b>28.1</b>

Source: Company reports and J.P. Morgan estimates.

**KNR's leverage at 1x D/E as of FY15 will not increase significantly with only Rs1-2bn of capex pending on its under construction BOT projects.**

**The company saw an increase in working capital days to 54 vs. 37 in FY14 with the increase in debtors. As per management, certain dues were collected two months later from the year end.**

**KNR generated 10% RoE and 4% RoCE in FY15.**

**Table 9: KNR: Summary Balance Sheet**

Rs. in million, year-end March

	FY12	FY13	FY14	FY15
Share capital	281	281	281	281
Reserves and surplus	3,897	4,356	5,829	7,604
Minority interest	11	534	559	560
<b>Non-Current Liabilities</b>				
Long-term borrowings	64	804	3,432	6,719
Deferred tax liabilities (Net)	8	-	-	-
Other long-term liabilities	828	1,311	695	843
Long-term provisions	11	11	11	17
<b>Current Liabilities</b>				
Short-term borrowings	465	636	501	880
Trade payables	1,082	1,130	781	754
Other current liabilities	1,001	1,083	1,892	2,058
Current Maturities	56	38	326	83
Short-term provisions	1,031	1,122	562	399
<b>Total</b>	<b>8,679</b>	<b>11,268</b>	<b>14,544</b>	<b>20,116</b>
Gross Fixed Assets	5,059	5,146	5,353	5,615
Net Tangible assets	3,212	2,961	2,722	2,349
Net Intangible assets	1	1	0	0
Intangible Assets under development	12	1,098	5,853	11,083
Non-current investments	330	307	256	236
Deferred Tax Assets (Net)	-	36	126	247
Long-term loans and advances	274	706	482	515
Other non-current assets	515	636	727	735
<b>Current Assets</b>				
Current Investments	-	182	-	-
Inventories	643	473	530	557
Trade receivables	883	1,159	755	1,101
Cash and cash equivalents	116	234	573	435
Short-term loans and advances	2,067	2,525	1,757	1,727
Other current assets	625	951	763	1,131
<b>Total</b>	<b>8,679</b>	<b>11,268</b>	<b>14,544</b>	<b>20,116</b>
Total Debt	586	1,478	4,260	7,683
D/E	0.14	0.32	0.70	0.97
Net Debt	470	1,062	3,687	7,247
Net D/E	0.11	0.23	0.60	0.92
Current assets ex cash	4,219	5,108	3,805	4,517
Current liab ex debt	3,058	3,297	2,909	3,128
Working Capital	1,161	1,811	896	1,388
Days	47	86	37	54
Inventory Days	26	23	22	22
Debtor Days	36	55	31	43
L&A Days	85	120	72	68
Payable Days	44	54	32	30
BVPS (INR)	149	165	217	281
RoE (%)	11.8	11.1	11.3	10.0
RoCE (%)	5.7	4.5	5.1	4.1

Source: Company reports and J.P. Morgan estimates.

Given the increase in debtors, operating cash flow declined further in FY15. As per management, Rs800mn of claims were received 2 months after the year end.

Additionally, the company has incurred capex on its BOT portfolio translating into negative FCF over the past four years.

KNR is yet to incur ~Rs1-2bn of capex in FY16 (including the cost overrun) on its two under construction projects (project cost of Rs12.6bn + Rs0.8bn cost overrun).

**Table 10: KNR: Summary Cash Flow**

Rs. in million, year-end March

	FY12	FY13	FY14	FY15
Net income	468	491	605	698
Depreciation & Amortization	556	560	586	552
Change in working capital	(17)	(650)	915	(493)
Taxes	(268)	(157)	(65)	3
Net interest	(7)	64	(7)	(1)
<b>Cash flow from operations</b>	<b>731</b>	<b>307</b>	<b>2,033</b>	<b>758</b>
Capex	(433)	(1,173)	(4,963)	(5,491)
Investments	23	23	51	20
<b>Cash flow from investing</b>	<b>(409)</b>	<b>(1,150)</b>	<b>(4,912)</b>	<b>(5,471)</b>
Equity raised/(repaid)	0	0	0	0
Debt raised/(repaid)	(162)	892	2,782	3,423
Other	0	97	464	1,181
Dividends	(28)	(28)	(28)	(28)
<b>Cash flow from financing</b>	<b>(663)</b>	<b>961</b>	<b>3,218</b>	<b>4,575</b>
Beginning cash	457	116	234	573
Change in cash Flow	(341)	118	339	(137)
Ending cash	116	234	573	435

Source: Company reports and J.P. Morgan estimates.

## Valuation & Stock Performance

Stocks with lower BOT exposure (and hence lower leverage) like KNR, J Kumar and MBL have outperformed asset owners i.e. IRB, ITNL and Ashoka Buildcon as well as the more diversified L&T and RELI.

**Table 11: Stock performance road asset owners and E&C companies**

%	1 month	3 months	6 months	1 year
KNR	15	3	38	120
MBL	6	(15)	(22)	47
Sadbhav	7	1	(14)	41
IL&FS	12	(31)	(50)	(41)
IRB	19	6	0	15
Ashoka Buildcon	(1)	(10)	(13)	25
J Kumar Infraprojects	10	5	12	155
RELI	10	(13)	(19)	(37)
L&T	3	(14)	(12)	10
GMR	23	(7)	(23)	(30)
GVK	8	(15)	(18)	(22)
Gayatri Projects	43	70	274	241
Nagarjuna Construction	36	(6)	(34)	107

Source: Bloomberg.

KNR is trading at 22x FY17 earnings i.e. almost at the top of the range for EPC road companies with an estimated 43% earnings growth in FY17 based on Bloomberg consensus with low leverage at 0.8x. The stock is up 120% in the past year, outperforming the Sensex.

MBL is trading at a lower 12x FY17 P/E with an estimated 5% earnings growth in FY15 based on Bloomberg consensus with leverage at 1.6x. The stock is up 47% in the past year, outperforming the Sensex.

**Table 12: Valuation Summary: Road asset owners and E&C contractors**

year end March

	BBG Ticker	CMP Rs	Mcap Rs bn	EPC OB		BOT Portfolio (kms)		P/E		EV/EBITDA		P/B		RoE		Net D/E
				Rs bn	% Roads	Operational	Under Implementation	FY16E	FY17E	FY16E	FY17E	FY16E	FY17E	FY16E	FY17E	FY15
KNR	KNRC IN	598	17	35	98%	113	162	31.0	21.7	16.2	9.1	2.0	1.8	5.4	9.2	0.8
MBL	MBL IN	244	10	37	71%	132	295	12.6	12.1	7.2	5.0	1.3	1.2	13.0	10.6	1.6
Sadbhav	SADE IN	303	52	85	52%	1,886 <sup>(a)</sup>	1,448 <sup>(a)</sup>	2,524.2	80.4	13.1	9.3	2.5	2.2	3.2	4.6	3.9
IL&FS	ILFT IN	100	32	158	93%	8,899 <sup>(a)</sup>	5,768 <sup>(a)</sup>	12.1	7.1	12.2	11.1	0.4	0.4	3.5	6.2	3.8
IRB	IRB IN	253	89	121	100%	6,101 <sup>(a)</sup>	3,935 <sup>(a)</sup>	14.7	12.8	8.4	7.6	1.8	1.6	12.9	13.2	2.6
Ashoka Buildcon	ASBL IN	166	31	28	44%	2,431 <sup>(a)</sup>	1,883 <sup>(a)</sup>	32.6	21.6	9.5	7.5	1.7	1.6	5.1	6.7	2.1
J Kumar																
Infraprojects	JKIL IN	794	26	43	NA	-	-	20.7	14.7	9.7	7.7	2.8	2.4	14.5	17.6	0.6
RELI	RELI IN	358	94	42	NA	519	451	5.0	4.3	11.0	9.8	0.3	0.3	5.7	7.4	0.8
L&T	LT IN	1,555	1,447	2,390	NA	5,619 <sup>(a)</sup>	2,177 <sup>(a)</sup>	27.0	20.7	17.6	14.6	3.2	2.9	12.5	14.5	1.7
Gayatri Projects	GAYP IN	579	21	69 <sup>(b)</sup>	44%	410	211	36.2	19.2	13.8	10.2	NA	NA	7.6	12.5	4.8
Nagarjuna																
Construction	NJCC IN	75	42	187	35%	291	-	24.3	16.7	7.0	6.4	1.2	1.0	4.6	6.5	0.6

Source: Company reports, Bloomberg. Price as on 6 October 2015. Note: (a): Lane kms. (b) In August Gayatri Projects has won Rs33.2bn of new NHAI contracts. (c) EPC OB is as of June 2015.

**Table 13: Revenue Growth and EBITDA Margin**

%, year end March

	Revenue growth		EBITDA Margin		
	FY16E	FY17E	FY15	FY16	FY17
KNR	4.6	48.7	13.6	15.6	18.6
MBL	17.9	20.9	12.1	12.2	14.6
Sadbhav	24.3	26.6	17.3	21.8	24.2
IL&FS	13.4	15.9	33.2	33.1	35.0
IRB	25.5	19.2	58.1	55.1	55.0
Ashoka Buildcon	15.6	17.4	20.4	27.5	28.5
J Kumar Infraprojects	21.3	25.8	18.7	18.4	18.3
RELI	13.6	13.0	18.3	18.2	18.7
L&T	13.4	19.8	12.4	12.9	13.3
GMR	4.6	15.1	25.6	35.5	36.1
GVK	22.0	57.4	38.2	44.4	45.9
Gayatri Projects	31.5	28.6	22.9	13.4	14.0
Nagarjuna Construction	(0.5)	10.1	10.5	9.5	9.7

Source: Bloomberg consensus estimates.

## MBL Infrastructure Ltd.: Summary historical financial

### Profit and loss statement

INR in millions, year-end March

	FY13	FY14	FY15
Revenue	13,554	17,663	19,618
% change Y/Y	7.1	30.3	11.1
Gross margin (%)	29.6	22.1	22.7
EBITDA	1,434	1,882	2,369
% change Y/Y	(14.6)	31.2	25.9
EBITDA margin (%)	10.6	10.7	12.1
EBIT	1,323	1,741	2,168
% change Y/Y	(15.5)	31.6	24.5
EBIT margin (%)	9.8	9.9	11.0
Net interest	561	711	980
Earnings before tax	762	1,030	1,188
% change Y/Y	(27.8)	35.1	15.4
Tax	196	260	372
as % of EBT	25.7	25.2	31.3
Net income (reported)	566	770	816
% change Y/Y	(21.9)	35.9	6.0
Shares O/S (MM)	35.0	35.0	41.5
EPS (INR)	16.2	22.0	22.1

Source: Company reports.

### Cash flow statement

INR in millions, year-end March

	FY13	FY14	FY15
Net income	566	770	816
Depreciation & Amortization	111	141	202
Change in working capital	(1,024)	(612)	(2,544)
Taxes	(196)	(260)	(372)
Net interest	(561)	(711)	(980)
<b>Cash flow from operations</b>	<b>(1,103)</b>	<b>(673)</b>	<b>(2,878)</b>
Capex	(1,708)	(2,062)	(1,883)
Investments	(196)	0	(41)
<b>Cash flow from investing</b>	<b>(1,904)</b>	<b>(2,062)</b>	<b>(1,924)</b>
Equity raised/(repaid)	0	0	1,126
Debt raised/(repaid)	2,095	1,513	2,763
Other	1,046	1,191	1,052
Dividends	(53)	(53)	(62)
<b>Cash flow from financing</b>	<b>3,088</b>	<b>2,651</b>	<b>4,879</b>
Beginning cash	685	766	682
Change in cash Flow	81	(83)	77
Ending cash	766	682	760
DPS (INR)	1.5	1.5	1.5

Source: Company reports.

### Balance sheet

INR in millions, year-end March

	FY13	FY14	FY15
Cash and cash equivalents	766	682	760
Inventories	4,912	5,589	8,105
Accounts receivable	2,535	3,182	3,949
Loans and advances	723	983	876
Others	62	80	73
<b>Total Current assets</b>	<b>8,997</b>	<b>10,516</b>	<b>13,764</b>
LT investments	196	196	237
Net fixed assets	1,886	2,138	2,171
CWIP	2,088	3,759	5,407
Other LT assets	63	162	606
<b>Total assets</b>	<b>13,231</b>	<b>16,772</b>	<b>22,186</b>
Total current liabilities	1,753	2,743	3,370
Total Debt	6,767	8,279	11,042
Other long term liabilities	735	745	1,208
Total liabilities	9,255	11,767	15,621
Minority Interest	0	320	0
Shareholders' equity	3,977	4,685	6,565

Source: Company reports.

### Ratio analysis

%, year-end March

	FY13	FY14	FY15
EBITDA margin	10.6	10.7	12.1
Net profit margin	4.2	4.4	4.2
Sales growth	7.1	30.3	11.1
Net profit growth	-21.9	35.9	6.0
Interest coverage (x)	2.49	2.50	2.34
Gross debt to equity	1.7	1.8	1.7
Net debt to equity	1.5	1.6	1.6
Sales/assets	102.4	105.3	88.4
ROCE	9.7	9.9	9.2
Assets/equity (x)	3.3	3.6	3.4
ROE	15.2	17.8	14.5
DPS (Rs)	1.5	1.5	1.5
Dividend payout ratio	4.6	3.4	3.4
BVPS (Rs)	113.6	133.9	158.2

Source: Company reports.



## KNR Constructions Ltd.: Summary historical financial

### Profit and loss statement

INR in millions, year-end March

	FY13	FY14	FY15
Revenue	7,650	8,950	9,312
% change Y/Y	(14.3)	17.0	4.0
Gross margin (%)	21.4	21.0	22.3
EBITDA	1,166	1,314	1,268
% change Y/Y	(11.8)	12.6	(3.5)
EBITDA margin (%)	15.2	14.7	13.6
EBIT	607	728	716
% change Y/Y	(20.9)	19.9	(1.6)
EBIT margin (%)	7.9	8.1	7.7
Net interest	(64)	7	1
Earnings before tax	671	721	715
% change Y/Y	(11.7)	7.5	(0.8)
Tax	157	65	(3)
as % of EBT	23.5	9.1	(0.4)
Net income (reported)	491	605	698
% change Y/Y	4.8	23.3	15.3
Shares O/S (MM)	28.1	28.1	28.1
EPS (INR)	17.5	21.5	24.8

Source: Company reports.

### Balance sheet

INR in millions, year-end March

	FY13	FY14	FY15
Cash and cash equivalents	234	573	435
Inventories	473	530	557
Accounts receivable	1,159	755	1,101
Loans and advances	2,525	1,757	1,727
Others	951	763	1,131
Total Current assets	5,342	4,378	4,952
LT investments	489	256	236
Net fixed assets	2,961	2,722	2,349
CWIP	1,098	5,853	11,083
Other LT assets	1,378	1,335	1,496
Total assets	11,268	14,544	20,116
Total current liabilities	3,297	2,909	3,128
Total Debt	1,478	4,260	7,683
Other long term liabilities	1,322	707	861
Total liabilities	6,097	7,875	11,672
Minority Interest	534	559	560
Shareholders' equity	4,637	6,110	7,885

Source: Company reports.

### Cash flow statement

INR in millions, year-end March

	FY13	FY14	FY15
Net income	491	605	698
Depreciation & Amortization	560	586	552
Change in working capital	(650)	915	(493)
Taxes	(157)	(65)	3
Net interest	64	(7)	(1)
<b>Cash flow from operations</b>	<b>307</b>	<b>2,033</b>	<b>758</b>
Capex	(1,173)	(4,963)	(5,491)
Investments	23	51	20
<b>Cash flow from investing</b>	<b>(1,150)</b>	<b>(4,912)</b>	<b>(5,471)</b>
Equity raised/(repaid)	0	0	0
Debt raised/(repaid)	892	2,782	3,423
Other	97	464	1,181
Dividends	(28)	(28)	(28)
<b>Cash flow from financing</b>	<b>961</b>	<b>3,218</b>	<b>4,575</b>
Beginning cash	116	234	573
Change in cash Flow	118	339	(137)
Ending cash	234	573	435
DPS (INR)	1.0	1.0	1.0

Source: Company reports.

### Ratio analysis

%, year-end March

	FY13	FY14	FY15
EBITDA margin	15.2	14.7	13.6
Net profit margin	6.4	6.8	7.5
Sales growth	-14.3	17.0	4.0
Net profit growth	4.8	23.3	15.3
Interest coverage (x)	9.7	7.3	9.7
Gross debt to equity	0.3	0.7	1.0
Net debt to equity	0.3	0.6	0.9
Sales/assets	67.9	61.5	46.3
ROCE	4.5	5.1	4.1
Assets/equity (x)	2.4	2.4	2.6
ROE	11.1	11.3	10.0
DPS (Rs)	1.0	1.0	1.0
Dividend payout ratio	5.7	4.6	4.0
BVPS (Rs)	165.0	217.4	280.6

Source: Company reports.

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