

Institutional Equity Research

H.G. Infra Engineering

Infrastructure | India

Initiating Coverage | March 19, 2018

CMP* (Rs)	301
Upside/ (Downside) (%)	25
Bloomberg Ticker	HGINFRA IN
Market Cap. (Rs bn)	19.6
Free Float (%)	26
Shares O/S (mn)	65

BUY 

Target Price: Rs375

Moving towards the Big League

H.G. Infra Engineering (HGI), a newly listed company, is primarily engaged in EPC, civil construction works and related infrastructure projects on item rate and lump sum basis. Roads & Highways segment – which is HGI’s key area of operation – forms a dominant portion of its total order book. While current order book of Rs50.6bn (4.8x FY17 revenue) provides robust growth visibility, HGI is expected to add big chunk of orders to its kitty, led by improvement in financial pre-qualification and enormous opportunity in Roads & Highway segment. Further, diversification into newer geographies and water segment is likely to propel HGI to sustain growth, in our view. **Expecting HGI’s revenue and earnings to clock 31% and 46% CAGR, respectively through FY17-FY20E, we initiate coverage on the stock BUY recommendation and one-year Target Price of Rs375.**

Huge Opportunity in Roads & Highway Segment Augurs Well

The visible development in Roads & Highways space along with likely further pick-up in projects awarding across the country and government’s increased allocation for the segment are likely to aid HGI to improve its order book further. Further, improvement in financial pre-qualification post the fund raising through IPO is expected to result in higher order book in coming quarters.

Impressive Order Book Growth Offers Visibility

HGI witnessed an exponential improvement in its order book to Rs40bn in FY17 from Rs11bn in FY15 (94% CAGR). Its current order book at Rs50.6bn (4.8x of FY17 revenue) including L1 of Rs13.5bn provides a healthy revenue visibility. We expect HGI to witness an order inflow of Rs25bn and Rs30bn for FY19E and FY20E, respectively. Considering fund-based limit of Rs4.3bn and non-fund based limit of Rs5.0bn, we believe it should not face any financial constraint to execute the current order book.

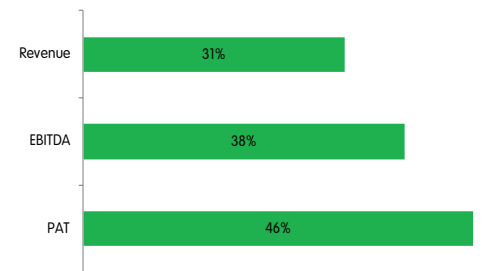
Diversification into New Geographies Bodes Well

In order to mitigate concentration risk and exploit the upcoming infrastructure opportunities in other geographies, HGI has been geographically diversifying for last couple of quarters. It currently operates in six states including Uttar Pradesh and it intends to selectively expand into other states, which is expected to aid HGI to sustain growth, going forward.

Promising Growth on the Cards; Initiate with BUY

HGI has been gaining a healthy traction for last two years on the backdrop of consistent order book addition and improving execution expertise. Further, with the improvement in financial pre-qualification post fund raising and enormous opportunity in its key vertical, we expect HGI’s revenue and earnings to clock 31% and 46% CAGR, respectively through FY17-FY20E. While HGI did not provide any listing gain to its subscribers, we believe current valuations at 17.3x / 12.9x EPS of FY19E / FY20E, respectively, look attractive considering less than 1x PEG ratio and strong return ratios. **Hence, we initiate our coverage on the stock with BUY recommendation and one-year Target Price of Rs375 (16x FY20 EPS).**

CAGR (FY17-20E)



Shareholding Pattern (%)	Dec'17	Post IPO
Promoter	100	74
Public	-	26

Key Financials (Rs mn)	FY17	FY18E	FY19E	FY20E
Sales	9,703	12,615	16,798	21,606
EBITDA	1,198	1,774	2,402	3,122
Net Profit	493	782	1,132	1,524
EPS (Rs)	7.6	12.0	17.4	23.4
DPS (Rs)	-	-	2.0	3.0
P/E (x)	39.8	25.1	17.3	12.9
P/B (x)	3.1	3.5	3.0	2.5
EV/EBITDA	6.2	11.8	8.7	6.8
RoE (%)	33.0	21.4	18.8	21.3
Divi. Yield (%)	-	-	0.7	1.0

Source: Company, RSec Research

Research Analyst: Binod Modi

Contact: 022 3320 1097

Email: binod.modi@relianceada.com

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Investment Rationale

Huge Opportunity in Roads & Highway Segment Augurs Well

The visible development in Roads & Highways space along with likely further pick-up in projects awarding across the country and government's increased allocation for the segment are likely to aid HGI to improve its order book further. Moreover, improvement in financial pre-qualification post the fund raising through IPO is expected to result in higher order book in coming quarters.

Notably, budgetary allocation for Roads & Highways increased at a robust 20.9% CAGR through FY09-FY19. In Union Budget 2018-19, the Government has allocated Rs1.21trln (US\$18.7bn) for the Road sector.

Exhibit 1: Outlays for Roads & Highways in Union Budgets

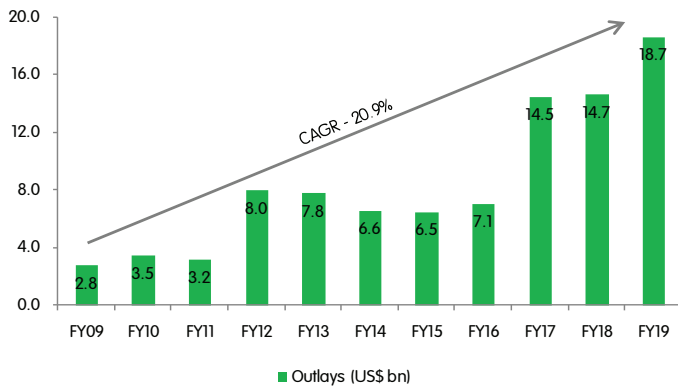
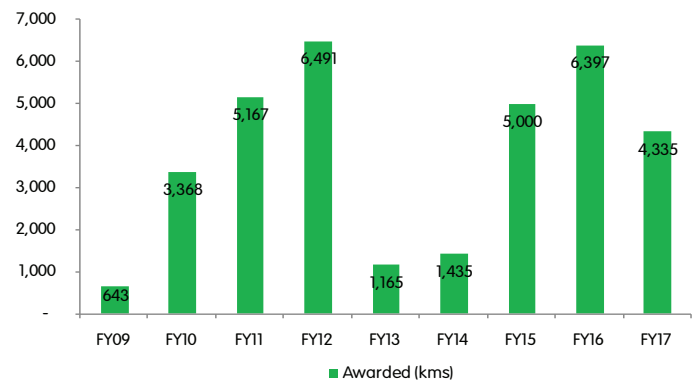


Exhibit 2: Projects Awarded by NHAI



Source: Industry; RSec Research

Impressive Order Book Growth Offers Visibility

Consistent improvement in execution expertise along with improvement in technical and financial pre-qualification criterion enabled HGI to grow its order book exponentially to Rs40bn in FY17 from Rs11bn in FY15 (94% CAGR). Its current order book at Rs50.6bn (4.8x of FY17 revenue) including LI of Rs13.5bn provides a healthy revenue visibility, in our view.

HGI is currently pre-qualified to bid for Roads & Highway projects of NHAI and Ministry of Road Transport & Highways worth up to Rs8bn on in own. We expect HGI to add orders worth Rs25bn and Rs30bn for FY19E and FY20E, respectively, as against the Management's guidance of Rs30bn and Rs40bn, respectively.

Notably, 44% of HGI's total order book is fixed price contracts and Rs1bn of orders book (2% of OB) comes from the JV. Further, HGI has recently secured a HAM project (part of LI) worth Rs5.6bn in Rajasthan. While HGI is still pursuing select HAM projects, it expects share of HAM projects in order book to contain within the range of 25%.

Considering fund-based limit of Rs4.3bn and non-fund based limit of Rs5.0bn, we believe it should not face any financial constraint to execute the current order book.

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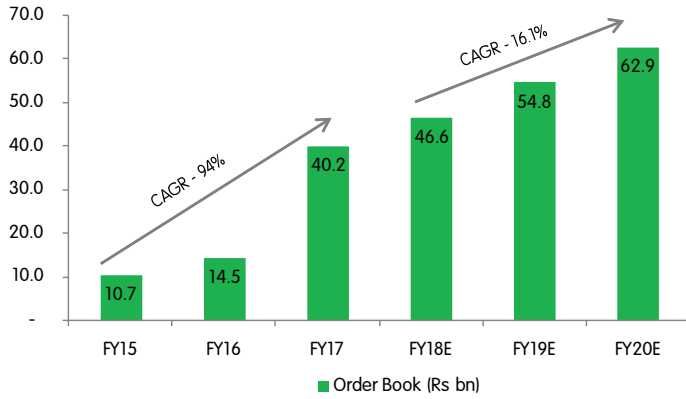
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Exhibit 3: Order Book Witnessed Robust Growth

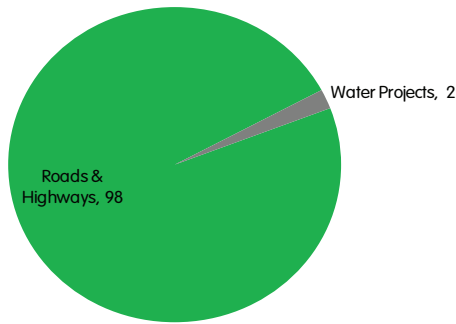


Source: Company; RSec Research

Exhibit 4: Top 5 Projects Under Execution

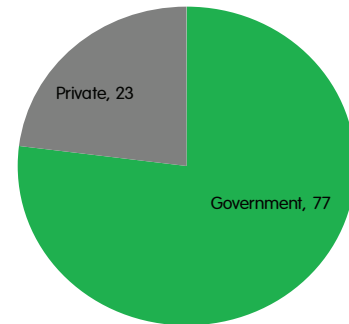
Projects	Appointed Date	Value (Rs bn)
Gulabpura- Chittorgarh Section-2	Nov-17	6.4
Chittorgarh- Udaipur Section of NH-76 Sec- 1	Jul-17	4.8
Nagpur-Katol- Warud State Highway	Jun-17	3.1
Nandurbar - Prakasha- Sahada-Khetia State Highway	Jun-17	3.0
Amaravati-Nandgaon-Morshi-warud-Pandhurna	Jun-17	2.9

Exhibit 5: Segmental Break-up of Order Book (%)



Source: Company; RSec Research

Exhibit 6: Clientele Break-up of Order Book (%)



Diversification into New Geographies Bodes Well

In order to mitigate the risk of excessive dependence on particular geography and exploit the upcoming infrastructure opportunities in other geographies, HGI has been geographically diversifying for last couple of quarters. It currently operates in six states including Uttar Pradesh and it intends to selectively expand its presence in other states.

It currently expects that a significant portion of its geographic expansion will be in states i.e. Gujarat, Punjab and Madhya Pradesh, where it has favourable geographic and climatic conditions. Through further diversification of geographical operations, HGI is expected to hedge against concentration and related risks.

Exhibit 7: A Snapshot of Statewise Order Book

States	Order Book (Rs bn)	% of OB
Rajasthan	26.7	52.8
Uttar Pradesh	0.5	1.1
Haryana	5.8	11.6
Uttarakhand	0.5	1.0
Maharashtra	16.6	32.7
Arunachal Pradesh	0.4	0.9
Total	50.6	100

Source: Company; RSec Research

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Foray into Water Segment Augurs Well

While HGI has proven its expertise in Roads & Highway segment by successfully executing various projects over the years, it has diversified into water pipeline segment and is currently undertaking 2 water supply projects on turnkey basis in Rajasthan. Renewed thrust of the Government on both the segments offers enormous opportunities for HGI. While the opportunities in Roads & Highways segments are already visible, we may see a robust ordering from irrigation, waterways and development of smart cities, going forward. Hence, any potential up-tick in order inflow from this segment is expected to aid HGI to witness a sustainable growth, in our view.

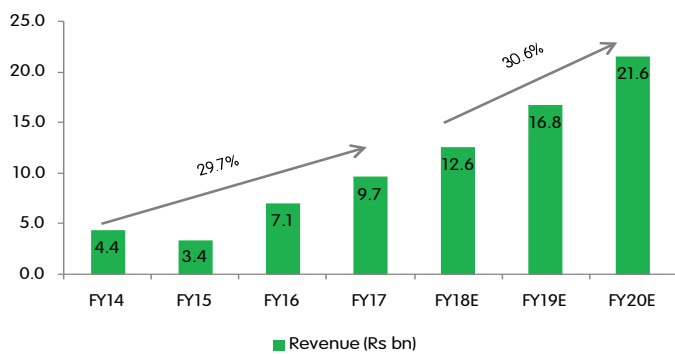
Robust Financial Performance & Financial Strength

An experienced management team, efficient working capital management, consistent addition of quality orders and prudent bidding strategy aided HGI to report robust numbers over the last 3 years. HGI's reported revenue and PAT clocked 30% and 42% CAGR, respectively over FY14-FY17. Further, light balance-sheet with efficient working capital management and asset-light business model enabled HGI to generate better-than-the-industry average return ratios in the range of 30-40% over last 3 years.

We believe that with the possible improvement in order book size with more geographies and segmental diversification and huge imminent opportunities in Roads & Highways and water pipeline projects, HGI is expected to report a consistent healthy growth, going forward. Revenue, EBITDA and PAT are expected to witness 31%, 39% and 46% CAGR, respectively through FY17-FY20E.

Notably, HGI's EBITDA margin significantly spiked in 1HFY18 due to new accounting standard, as revenue booking is done net off indirect taxes. Further, gradual shift from a prime sub-contractor to a lead contractor also aided margin expansion. We expect the same to remain in the range of 14-15% over the years.

Exhibit 8: Revenue Profile Over the Years



Source: Company; RSec Research

Exhibit 9: Net Profit and Margins Over the Years

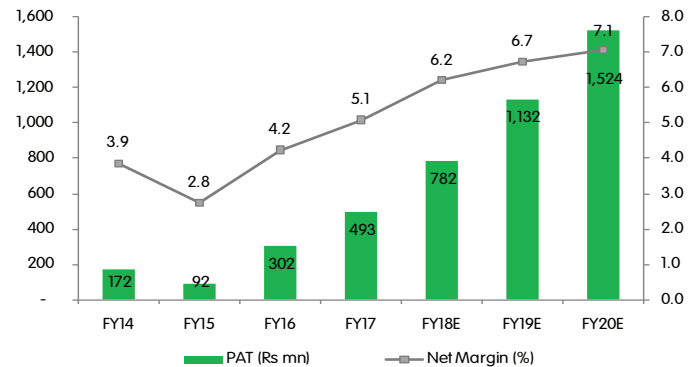
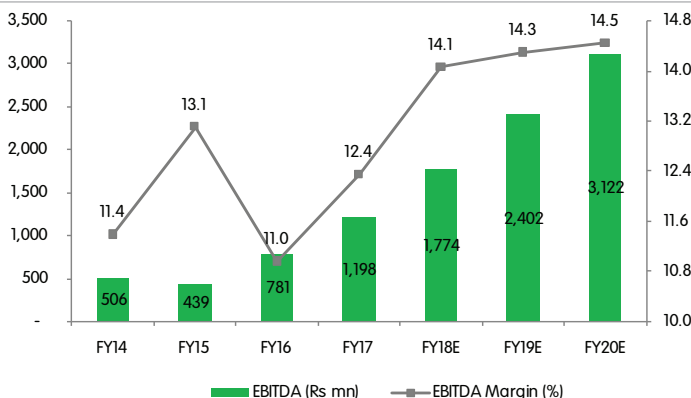
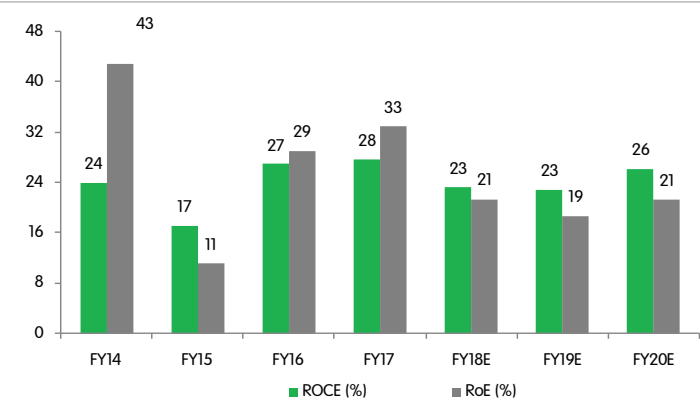


Exhibit 10: EBITDA and Margins Over the Years



Source: Company; RSec Research

Exhibit 11: Snapshot of Return Ratios



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Key Risks

- ▶ Higher dependence on road projects.
- ▶ Execution risk due to regulatory and social interferences.
- ▶ Cost overrun as 44% of total order book are fixed price contracts.
- ▶ Higher contingent liabilities (>200% of net worth).

Exhibit 12: Peers Comparison

	Revenue (Rs bn)		EBITDA Margin (%)		PAT (Rs bn)		PE (x)		RoE (%)	
	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E
KNR Construction	22.0	25.7	16.9	17.4	2.4	2.4	17.2	17.2	19.4	16.4
Dilip Buildcon	83.2	97.1	18.6	18.2	6.9	8	19.1	16.8	25.2	22.9
J Kumar Infra	23.4	28.0	16.2	16.4	1.7	2.4	13.1	9.7	11.2	13.6
JMC Projects	32.3	36.7	10.2	10.1	1.2	1.4	16.3	13.8	13.8	14.6
PNC Infra.	26.4	35.8	13.6	13.7	2.1	2.6	18.9	15.2	11.1	12.3
HG Infra	16.8	21.6	14.3	14.5	1.1	1.5	17.3	12.9	18.8	21.3

Source: Bloomberg, RSec Research

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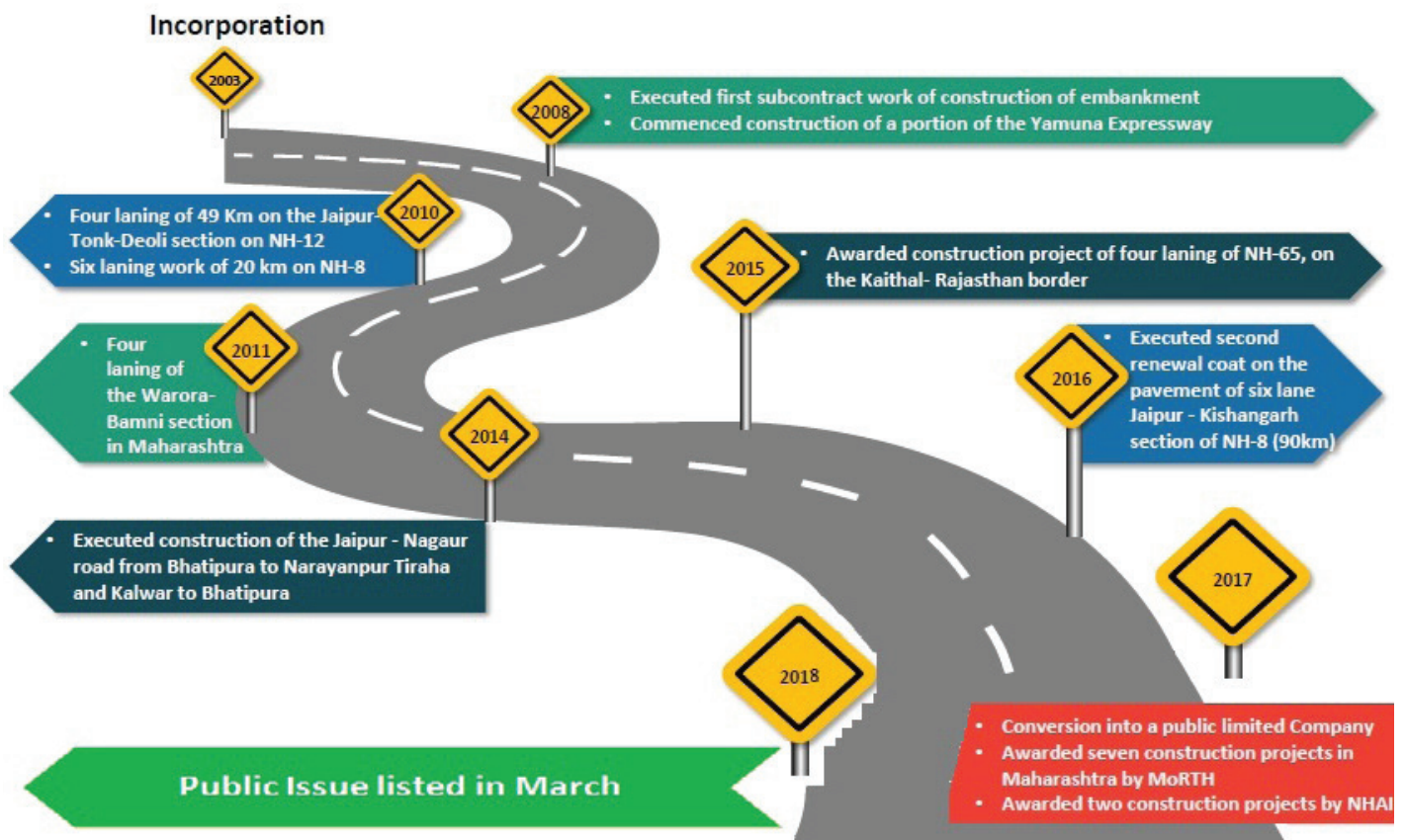
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Company Overview

The Company was incorporated on January 21, 2003 as HG Infra Engineering Pvt. Ltd. Pursuant to the conversion of it to a public limited company, its name was changed to HG Infra Engineering Ltd. (HGI) on June 8, 2017.

HGI is an infrastructure construction, development and management company with extensive experience in road projects including highways, bridges and flyovers. Its main business operations include: (i) providing Engineering, Procurement & Construction (EPC) services on a fixed-sum turnkey basis and; (ii) undertaking civil construction and related infrastructure projects on item rate and lump-sum basis, primarily in the road and highway sector. It has also forayed into executing water pipeline projects and is currently undertaking two water supply projects in Rajasthan on turnkey basis.

Exhibit 13: Company Milestones



Source: Company

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Profit & Loss Statement

Y/E Mar (Rs mn)	FY17	FY18E	FY19E	FY20E
Income	9,703	12,615	16,798	21,606
% yoy growth	36.2	30.0	33.2	28.6
Operating Expenses	8,505	10,841	14,396	18,484
EBIDTA	1,198	1,774	2,402	3,122
EBIDTA Margin (%)	12.4	14.1	14.3	14.5
Depreciation & Amortization	256	370	500	615
Finance Costs	193	261	281	286
Other Income	37	42	93	88
PBT before excep items	786	1,185	1,715	2,308
Extraordinary Items	-	-	-	-
PBT	786	1,185	1,715	2,308
Tax	294	403	583	785
% Tax	37.3	34.0	34.0	34.0
Net Profit- Reported	493	782	1,132	1,524
YoY Growth (%)	63.3	58.7	44.7	34.6
Net Profit Margin (%)	5.1	6.2	6.7	7.1

Balance Sheet

Y/E Mar (Rs mn)	FY17	FY18E	FY19E	FY20E
Sources of Funds				
Share Capital	180	652	652	652
Reserves & Surplus	1,579	4,889	5,865	7,154
Total Shareholder's funds	1,759	5,541	6,516	7,805
Borrowings	2,037	2,500	2,600	2,600
Non- Current Liabilities	303	402	529	691
Current Liabilities	1,282	1,761	3,264	4,261
Total Liabilities	5,380	10,203	12,909	15,358
Application of Funds				
Gross Fixed Assets	3,011	4,211	5,311	6,411
Less: Acc. Depreciation	967	1,337	1,837	2,453
Net Fixed Assets	2,044	2,874	3,474	3,958
CWIP	7	350	250	150
Deferred Tax Assets (Net)	20	22	22	22
NC Investments	4	5	505	1,005
Inventories	489	917	1,209	1,578
Sundry Debtors	1,132	1,529	2,015	2,630
Other Current Assets	596	1,834	2,216	2,630
Cash & Bank Balances	72	1,207	1,328	940
Loans & Advances	782	1,038	1,368	1,786
Total Current Assets	3,070	6,525	8,135	9,565
Other Non-Current Assets	235	428	524	658
Total Assets	5,380	10,203	12,909	15,358

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Cash Flow Statement

Y/E Mar (Rs mn)	FY17	FY18E	FY19E	FY20E
PBT	830	1,185	1,715	2,308
Depreciation	256	370	500	615
Net Change in Working Capital	(479)	(1,934)	46	(792)
Others	(4)	-	-	-
Interest	189	261	281	286
Tax Paid	(246)	(405)	(583)	(785)
Net Cash from Operating Activities	544	(523)	1,958	1,633
Capex	(1,151)	(1,543)	(1,000)	(1,000)
Sale / (Purchase) of Investments	(75)	-	-	-
Others	93	(1)	(500)	(500)
Net Cash used in Investing Activities	(1,134)	(1,544)	(1,500)	(1,500)
Borrowings (Net)	809	463	100	-
Issue of Share Cap.	-	3,360	-	-
Dividend Paid	-	-	(156)	(235)
Finance Cost	(189)	(261)	(281)	(286)
Others	-	(360)	-	-
Net Cash used in Financing Activities	620	3,203	(337)	(521)
Net Increase/ (Decrease) in Cash	31	1,135	121	(388)

Key Ratios

Y/E Mar	FY17	FY18E	FY19E	FY20E
Valuation Ratio (x)				
P/E	39.8	25.1	17.3	12.9
P/CEPS	26.2	17.0	12.0	9.2
P/BV	3.1	3.5	3.0	2.5
EV/EBIDTA	6.2	11.8	8.7	6.8
EV/Sales	0.8	1.7	1.2	1.0
Dividend Payout (%)	-	-	11.5	12.8
Dividend Yield (%)	-	-	0.7	1.0
Per Share Data (Rs)				
EPS (Basic)	7.6	12.0	17.4	23.4
EPS (Diluted)	7.6	12.0	17.4	23.4
CEPS	11.5	17.7	25.0	32.8
DPS	-	-	2.0	3.0
Book Value	98	85	100	120
Returns (%)				
RoCE	27.7	23.3	23.0	26.3
RoE	33.0	21.4	18.8	21.3
Turnover ratios (x)				
Asset Turnover (Gross block)	3.2	3.0	3.2	3.4
Inventory (days)	21	30	30	30
Receivables (days)	49	50	50	50
Payables (days)	27	27	28	28
WCC (days)	43	53	52	52

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Rating Guides

Rating	Expected absolute returns (%) over 12 months
BUY	>10%
HOLD	-5% to 10%
REDUCE	>-5%

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