Dimensional Securities Pvt Ltd.

Date: 5th January, 2018
CMP: 14.6
Price Target: Rs. 22.8
Recommendation: BUY

Sunil Hitech Engineers Ltd..

Initiating Coverage

MARKET DATA	
NSE TICKER	SUNILHITEC
Networth FY17 (Rs in Crs)	519.7
P/BV Ratio (FY17E) (x)	1.2X
EPS (TTM)(Rs.)	1.0
Market Price (Rs.)	14.6
P/E Ratio (TTM) (x)	14.6X
52 Week High(Rs)	16.2
52 Week Low (Rs)	10.3
Market Capitalisation (Rs. Cr)	552.6

AVERAGE DAILY VOLUME (in lakhs)	
BSE	8.1
NSE	45.3

SHARE HOLDING PATTERN	
Promoter	35.3
FII	0.0
DII	0.0
Public	64.7
Total	100.0

RETURN (%)	3M	6M	12M
Sunil	15.9	10.4	13.3
Nifty	6.6	9.7	27.7

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Sunil Hitech Engineers Ltd. (SHEL) The Company pre-dominantly operated in power sector and over the years it has successfully diversified into infrastructure EPC.

We believe that SHEL is in a good position to benefit from the Government's infrastructure push over next 5-10 years given its strong presence across key infrastructure verticals, superior execution capabilities and comparatively healthy balance sheet.

Focus on fast growing road sector to foster second phase of growth

Owing to changing dynamics in power sector and deteriorating margins, SHEL forayed into road sector in FY15. The road sector has been a priority for NDA Government and it will continue to see huge investments going ahead. Sunil Hitech's current order book for road segment stands at Rs. 3,183 cr giving us strong revenue visibility for future. The management is also consciously focusing on HAM projects which is less risky and guarantees cash flows over 15 years. During current fiscal, SHEL won its biggest road project of Rs. 982 cr under HAM model. On the back of strong order book and project wins we expect Sunil's revenues from road EPC to grow at 33.5% CAGR over FY18-FY20

Focus on institutional buildings to aide faster growth and better margins

SHEL entered the buildings space for PWD and other Govt. departments and now the focus would be mainly into institutional buildings like IIM, IITs, AIIMs, etc. It is currently qualified for projects up to Rs. 500 cr from the Govt. The EPC work for institutional buildings is more profitable business with EBITDA Margins in the range of 11.5-12%. We expect SHEL's revenues from this division to grow at 12.7% CAGR over FY17-FY20.

Power EPC business to remain stable, but high margin O&M business to remain strong

Owing to Government's push to renewable energy the capacity addition for thermal power plants is slowing down leading to dip in company's order-book. Therefore expect revenues from Power EPC to remain more or less stable going ahead.

However we believe that the O&M business will continue to report strong growth due to robust order book and huge opportunities as many large plants are expected to be modernized over next 3-5 years.

Foray into many emerging businesses

In order to diversify its business presence and tap fast growing opportunities, Sunil Hitech has ventured into many emerging businesses like Water Treatment, Solid waste management, river inter-linking, etc. Though these are small in size currently but they have the potential to scale up significantly over next 5-7 year time frame.

Valuation & View:

The stock price of Sunil Hitech took a beating during October 2016 on the news of promoters selling their shares. Further, there is a sense of scepticism among the market participants after the Income Tax Dept. conducted raids at Sunil Hitech's office. We believe that this entire thing was blown out of proportion and Street reacted quite adversely to these news. In our view there is significant value in the stock and accordingly we are coming out with a BUY rating on it with a target price of Rs. 22.8, implying an upside of 57% from CMP of Rs. 14.6.

❖ About the Company:

Sunil Hitech Engineers Limited (SHEL) is Engineering, Procurement and Construction (EPC) Company with presence across Roads, Buildings, and Power sector. Besides EPC, company also carries out Operation and Maintenance of Power & Steel plants and manufacturing of steel products.

- EPC Projects: EPC Projects for Roads & Highways with Flyover & Bridges, Institutional Buildings, BOP & EPC assignments for power plants as well as providing comprehensive services in Civil Engineering, Architectural and Structural works.
- Operation & Maintenance: The service portfolio covers providing permanent solutions to Operation, Overhauling & Maintenance (renovation and modernization) of Power & Steel plants.
- Manufacturing: Manufacturing includes Heavy Engineering Fab Shop catering to Power, Infrastructure, Process & Chemical Industries.

FY17	Power EPC	O&M	Roads EPC	Buildings EPC	Manufacturing	Others
Revenue (in Rs. Cr)	855.2	508.6	481.6	472.3	149.1	73.8
% of Total Revenue	33.7%	20.0%	18.9%	18.5%	5.9%	2.9%

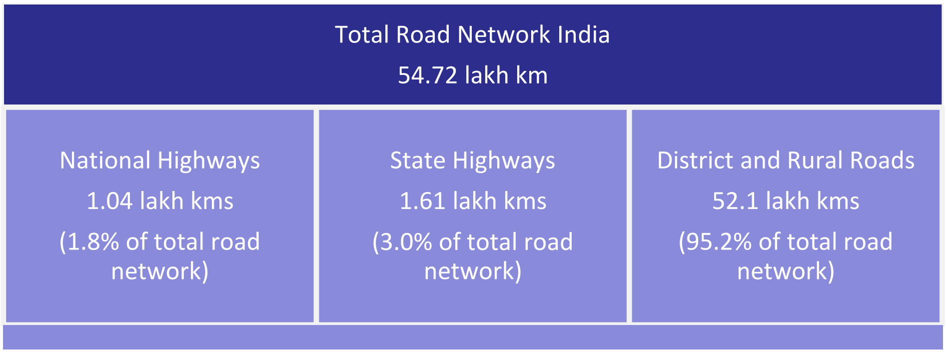
❖ Key thesis:

Focus on fast growing road sector to foster second phase of growth

Sunil Hitech pre-dominantly operated in power sector which formed ~60% of company's revenues till FY15. With change in market dynamics in power sector after Government's thrust on Renewable Energy and build up in competition, the order inflows and margins for power plants started deterioration. This led the management to take a conscious decision to move towards high margin and fast growing Road EPC segment.

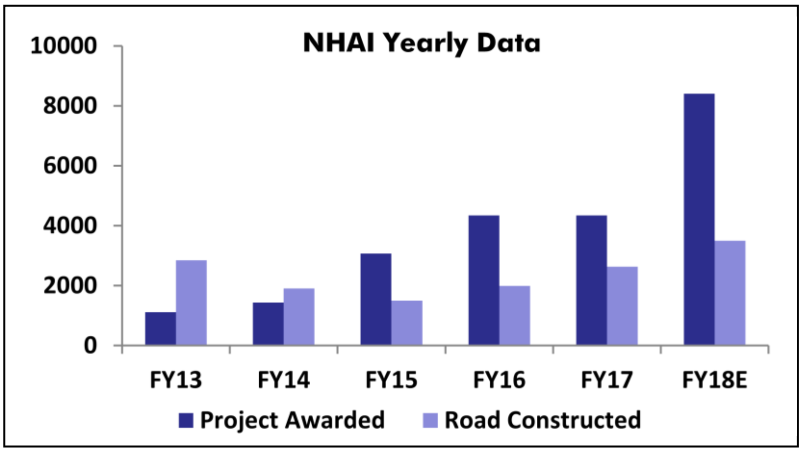
Sunil Hitech had been looking at road sector since FY12 but never really participated in bidding due to multiple headwinds present in the sector then like slow movement of projects, delay in financial closures, cost overruns and stressed balance sheet of BOT operators. SHEL timed its foray into road sector with perfection when the newly elected NDA Government came at the helm and turned the sector on its head by clearing the stuck projects and aggressively giving out new tenders. Since the company didn't have any legacy backlogs and financial stress, it was able to bid and win new projects. In a matter of 3 years, company was able to ramp up its order book from Rs. 494 cr in FY15 to Rs. 3183 cr by the end of FY17.

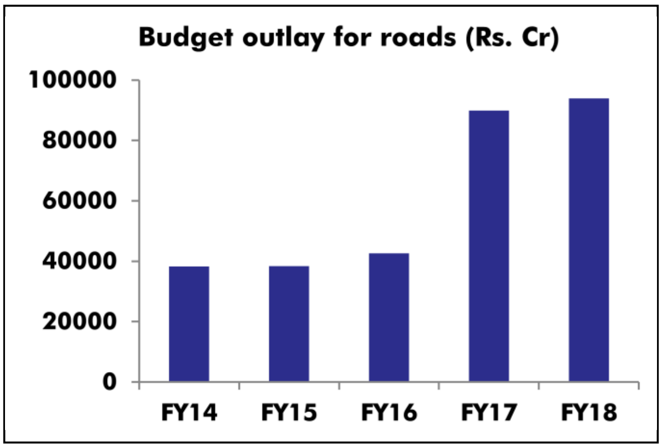
Road Industry in a sweet spot, looking good for multi-year growth



Though India's has one of the largest road networks in the world but when it comes to highways it lacks far behind. The National highways which carry 40% of country's traffic forms only 1.8% of total road network.

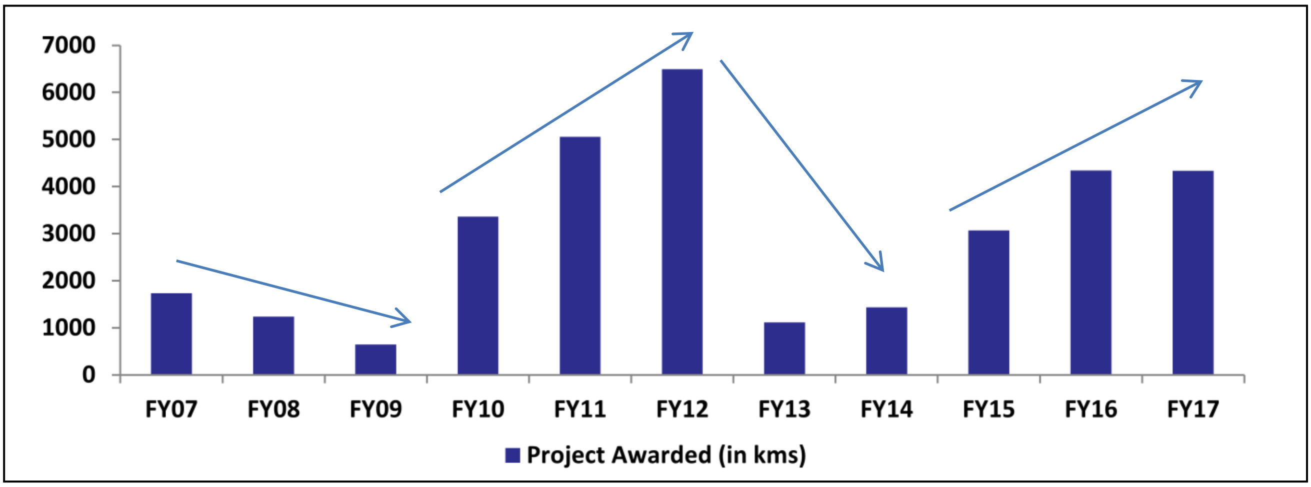
The road sector has been in a sweet spot since the arrival of new Government in 2014. The pace of project awards and project construction has improved considerably and it is only expected to get stronger given that the sector has been Government 's priority and has been receiving strong budgetary support





When viewed historically, the road sector has been cyclical in nature with spurt in growth for 3-4 years followed by cyclical downturn. There are many factors leading to such cyclicality in industry;

- Aggressive bidding during good times led to bulky order-book for pure play road operators. Most of these projects were awarded under BOT Model.
- The bids were also based on aggressive assumptions about future traffic growth, and in most cases the toll growth came in much lower than anticipated.
- This caused financial stress for BOT operators as lower revenues and consequentially lower profits were hardly able to cover debt repayments. This led to slow down in financial closure for new projects as banks were hesitating in lending to BOT projects.
- The impact was more pronounced between FY12-14 which saw India's GDP growing at slowest pace leading to lower traffic growth. This coupled with stretched balance sheets of incumbents and land acquisition problems led to slowdown in new project awards.



From 2014, in order to ensure more bidding and higher absorption of projects, the Govt. moved towards EPC model of awarding projects which caught interests of not only old players but also newer ones. The funding requirement under EPC model is significantly lower than BOT. The companies need only working capital loans which they repay on receiving milestone payments. A rough calculation is that if a company has Bank Guarantee of 300-500 cr, they can bid for projects worth ~Rs. 3500-4000 cr. The new Government carried on awarding projects under EPC model and they also started awarding projects under Hybrid-Annuity Model (HAM) which assures guaranteed cash flows to the operator irrespective of traffic growth. Besides this, they also eased down land acquisition norms and tendered projects only after NHAI acquires 95% of land which quickens the financial closure once the project is tendered.

Type	Description	Traffic Risk	Financing Required	Concession Period
BOT	The party builds the roads, carries out O&M and collects the toll over concession period.	Private Party	100% of project cost	20-25 years incl construction period
HAM	The party builds the roads, carries out O&M over concession period and collects fixed annuity from the Govt.	Government	60% of project cost, 40% is funded by the Govt.	15 years after completion of construction
EPC	The party only builds the road for the Govt. on contract basis.	Government	3-4% of project cost as working capital	No concession period

Growth drivers for road sector:

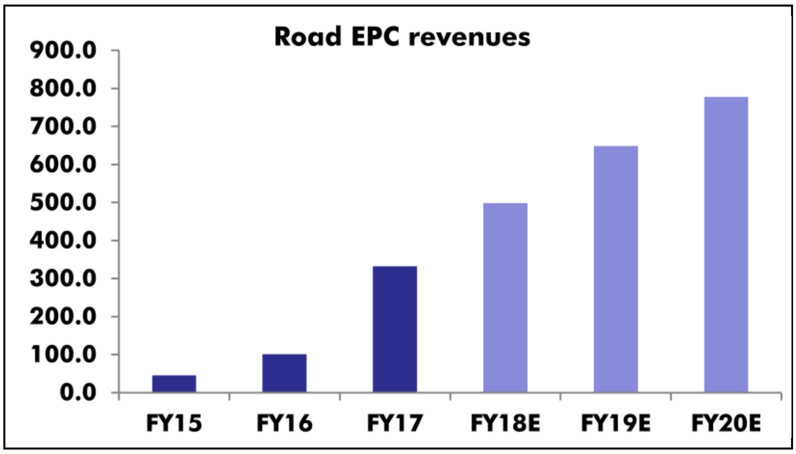
- Penetration of National Highways and State Highways still very low and their capacity needs to be in pace with the industrial growth.
- Consistent increase in passenger vehicles and freight traffic.
- Higher award of projects on EPC and HAM basis would lead to higher absorption rate.
- Government has announced project worth Rs. 1.45 lakh crore for constructing and upgrading roads in North Eastern part of the country and another Rs. 7 lakh crore for Bharat Mala project by 2022.

Strong revenue growth on the cards on the back of robust order-book and project wins

Sunil Hitech's order book for road segment stands at Rs. 3,183 cr giving us strong revenue visibility for future. And since it is company's focus area for next 5-8 years, they will continue to bid for more viable projects. SHEL is qualified for Road EPC projects from NHAI and MORTH for 2 lanes, 4 lanes & 6 lanes projects up to Rs. 1,200 cr and BOT & Annuity Projects up to Rs 1,500 cr.

The management is also consciously focusing on HAM projects which is less risky and guarantees free cash flows over 15 years. During current fiscal, SHEL won its biggest road project of Rs. 982 cr under HAM model. This gives us confidence for future such wins. The management has ambition to create 4-5 such HAM assets over next 5-6 years.

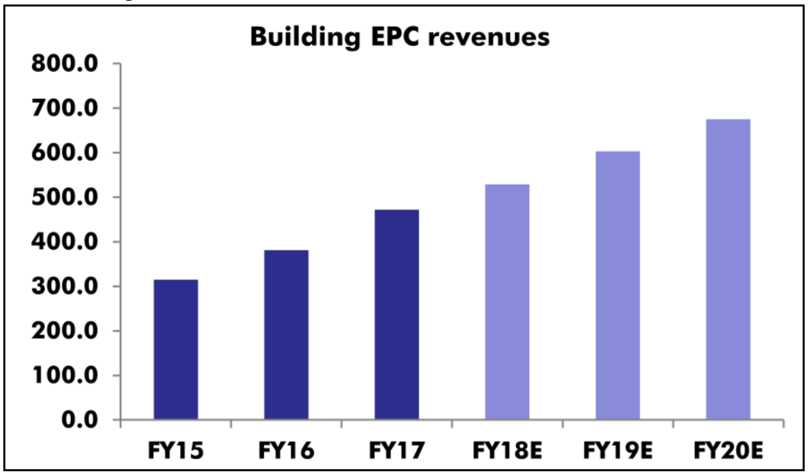
On the back of strong order book and project wins we expect Sunil's revenues from road EPC to grow at 32.8% CAGR over FY18-FY20.



Focus on institutional buildings to aide faster growth and better margins

SHEL entered the buildings space for PWD and other Govt. departments which includes construction work for Hospitals, National Institutions (like IIMs, AIIMs, etc.), Government Housing projects, industrial and commercial buildings, hostels, industrial sheds etc. It is currently qualified for projects up to Rs. 500 cr from the Govt. The EPC work for institutional buildings is more profitable business with EBITDA Margins in the range of 11.5-12%.

The construction industry which is at cyclical low will pick up traction from Govt spending and then going ahead from revival in private capex. The Govt. is expected to spend over Rs. 15000 cr for construction of IIMs, IITs, AIIIMs and other such institutions. For affordable housing alone, the Govt. is expected to spend Rs. 100,000 crore by FY20. We expect SHEL's revenues from this division to grow at 12.0% CAGR over FY17-FY20.

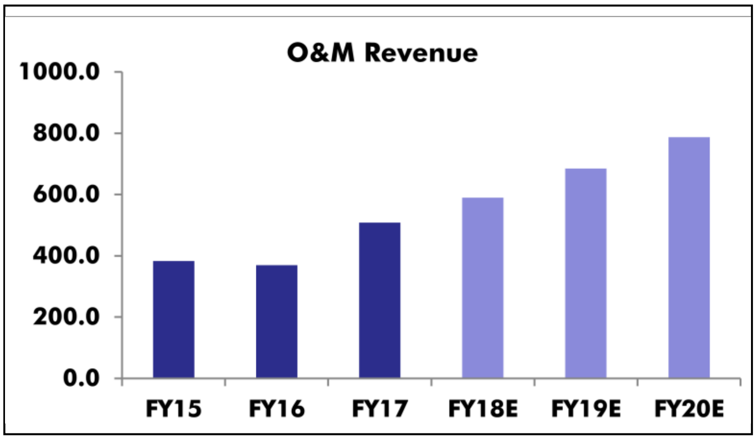


Power EPC business to remain stable, but high margin O&M business to remain strong

Under Power sector SHEL provides design, manufacturing, supply, erection, testing and commissioning of Balance of Plants (BOP) & EPC assignments for power plants. It specializes in setting up EPC / turnkey projects (up to 660 MW), which includes erecting boilers, Turbine Generators and auxiliaries, Transmission & Distribution projects etc. Until FY15, the Power sector contributed ~60% of company's revenues and order book. It benefitted significantly from rapid addition in thermal power plants between 2010 to 2014, which spearheaded its power revenues by 21.1% CAGR over FY10 to FY15.

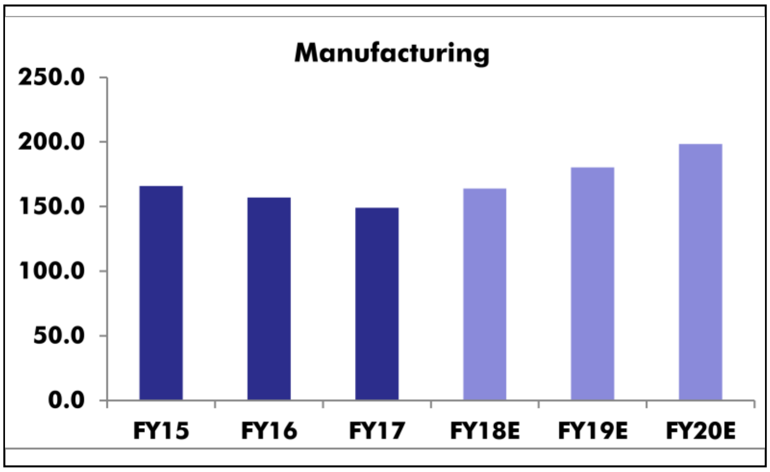
Since the capacity addition in thermal power plant is slowing down due to Government's push to renewable energy, company's order-book has also dipped slightly. Therefore expect revenues from Power EPC to remain more or less stable going ahead. We expect revenues from Power EPC to grow at 1.1% CAGR through FY17-FY20.

However we believe that the O&M business will continue to report strong growth due to robust order book and huge opportunities as many large plants are expected to be modernized over next 3-5 years. SHEL's O&M service portfolio covers the entire spectrum of operations and maintenance - boilers, turbine generators and auxiliaries; repair, modification and rehabilitation for utility boilers up to 800 MW; pressure plants, milling system, rotating parts and ducting; high pressure/low pressure piping works; renovation, modernisation and retrofitting of ESP; coal and ash handling plants. We expect the O&M revenues to grow at 16% CAGR over FY17-Y19 to Rs. 684.4 cr.



Manufacturing business to grow fast due to product diversification

Besides above, SHEL also manufactures parts and components for Power, Infrastructure, & Chemical Industries. It undertakes manufacturing of Super heater and re-heater coils, Economizer and LTSH coils, Water wall panels, High pressure parts bend, Technological structures for power and process industry, Tanks and vessels Piping, Boiler pressure parts tubes up to 660 MW, Collection and emitting electrodes of ESP. The manufacturing business is housed in company's subsidiary Seam Industries in which it holds 94% stake. The management soon expects to come out with an IPO for Seam Industries.



Foray into many emerging businesses

In order to diversify its business presence and tap fast growing opportunities, Sunil Hitech has ventured into many emerging businesses. Though these are small in size currently but they have the potential to scale up significantly over next 5-7 year time frame.

- Solid Waste Management: The Company is undertaking Solid Waste Management projects worth Rs. 220 crore at Patna (Bihar) in technology tie-up with Hitachi and Kolhapur (Maharashtra) with Ikos, France. The solid waste management industry has a huge potential to grow in India given the quantum of waste produced in India.
- Water Treatment: SHEL also offers tools and technology for water treatment, water purification, sea water desalination and effluent treatment.
- Under Seam Industries, company aims to diversify its product portfolio and manufacture railway over bridge and railway under bridge girders and soon they will start exploring opportunities in defence as well. .

Proven track record provides confidence for future success

SHEL has proven expertise in construction of National Highways, Institutional Buildings and executing large industrial civil work along with fabricating, erecting, testing and commissioning of bunkers, electrostatic precipitators, boilers and turbo generators sets in power plants.

- It has executed over 46GW worth of power projects since inception, which is one the highest by any private company.
- SHEL has also successfully executed its largest housing project worth Rs. 415 cr in Bihar by Bihar State Housing Board.
- It completed a road project in West Bengal worth Rs. 300 crore before schedule and was awarded bonus of Rs. 9.7 cr by the Govt. agency.

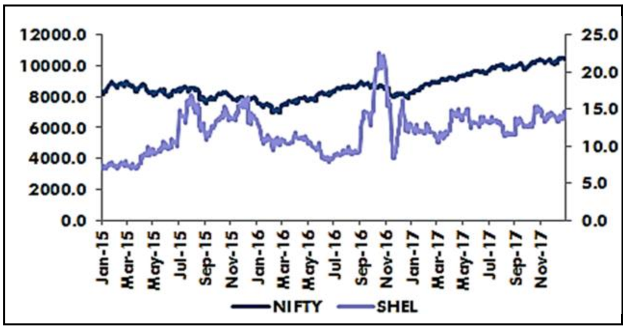
This gives us confidence on company's execution capabilities and future performance.

❖ Valuation & View:

The stock price of Sunil Hitech took a beating during October 2016 on the news of promoters selling their shares. Further, there is a sense of scepticism among the market participants after the Income Tax Dept. conducted raids at Sunil Hitech's office. We believe that this entire thing was blown out of proportion and Street reacted quite adversely to these news. In our view there is significant value in the stock and accordingly we are coming out with a BUY rating on it with a target price of Rs. 22.8, implying an upside of 57% from CMP of Rs. 14.6.

We are valuing Sunil Hitech at 1.3X FY20's BV of Rs. 17.1 given its superior return profile and adding the value of HAM project by arriving at its present value. Our valuation implies FY20 EV/EBITDA of

FY19 Book Value per share = Rs. 15.1	Multiple assigned= 1.3X	Value per share = Rs. 19.6
PV of HAM project as at FY19 = Rs. 171 cr (Ref. Annexure I)	Nos. of Shares= 53.6 cr	Value per share= Rs. 3.2
		Total Value per share= Rs. 22.8



Peer Comparison (FY17 data):

Company	Revenue	EBITDA	PAT	RoE	RoCE	TTM P/B	TTM EV/EBITDA
Sunil Hitech	2559.6	202.3	39.5	8.0%	14.9%	1.2X	5.4X
NCC	7982.1	677.1	225.5	6.7%	13.0%	2.0X	8.5X
Dilip Buildcon	5319.2	1159.6	357.7	27.0%	17.6%	4.5X	12.1X
HCC	4195.9	717.7	59.4	2.6%	12.5%	1.6X	11.2X

Risks & Concerns:

- Slowdown in Government spending on infrastructure.
- There has been aggressive bidding for road projects since many companies are vying at that space and could lead to deterioration of margins and returns, in case of HAM projects.

❖ Financials

Statement of Profit & Loss

Sunil Hitech Engineers Ltd.- Statement of Profit & Loss				
DESCRIPTION	**FY16**	**FY17**	**FY18E**	**FY19E**
Net Sales	2021.3	2559.6	2875.7	3280.7
EXPENDITURE :				
Raw Material Consumed	1122.5	1290.9	1459.1	1657.4
Project Costs	578.4	934.3	1046.8	1186.0
Employee Cost	70.7	54.0	58.4	61.9
Other Operating Expenses	43.8	78.0	86.1	95.7
EBITDA(Excl OI)	**205.9**	**202.3**	**225.4**	**279.7**
EBITDA Margin	***10.2%***	***7.9%***	***7.8%***	***8.5%***
Depreciation	36.8	38.2	43.4	48.8
EBIT	**169.2**	**164.1**	**182.0**	**230.9**
Other Income	14.2	13.3	13.4	13.4
Interest	98.4	110.9	128.4	131.4
PBT before exceptional item	85.0	66.5	67.0	112.9
Exceptional Item	0.0	0.0	0.0	0.0
PBT	**85.0**	**66.5**	**67.0**	**112.9**
Provision for Tax	29.1	25.9	22.8	38.4
Minority Interest	-2.4	-1.2	-1.3	-2.2
Profit After Tax	**53.4**	**39.5**	**42.9**	**72.3**
Earnings Per Share	**1.5**	**1.0**	**0.8**	**1.3**

Balance Sheet

Sunil Hitech Engineers Ltd.- Balance Sheet				
DESCRIPTION	**FY16**	**FY17**	**FY18E**	**FY19E**
Equity Share Capital	34.7	37.8	53.6	53.6
Total Reserves	432.0	481.8	536.5	756.5
Shareholder's Funds	**466.7**	**519.6**	**590.1**	**810.1**
Minority Interest	**17.5**	**18.7**	**17.4**	**15.2**
Total Borrowings	563.6	658.8	726.1	610.5
Other Long Term Liabilities	104.2	122.3	146.9	176.0
Total Non-Current Liabilities	**667.8**	**781.1**	**873.0**	**786.5**
Trade Payables	478.1	499.9	549.9	624.2
Other Current Liabilities	211.9	216.6	245.2	279.7
Total Current Liabilities	**690.0**	**716.5**	**795.1**	**904.0**
Total Liabilities	**1842.0**	**2036.0**	**2275.6**	**2515.7**
Fixed Assets	280.3	274.3	296.3	312.7
Other Non-Current Assets	106.6	93.1	101.3	111.2
Total Non-Current Assets	**386.9**	**367.3**	**397.6**	**423.9**
Inventories	254.1	302.8	343.7	382.3
Sundry Debtors	545.5	631.9	724.8	808.9
Cash and Bank	124.2	166.9	166.9	166.9
Other Current Assets	531.4	567.1	642.6	733.7
Total Current Assets	**1455.1**	**1668.7**	**1878.0**	**2091.8**
Total Assets	**1842.0**	**2036.0**	**2275.6**	**2515.7**

Cash Flow Statement

Sunil Hitech Engineers Ltd.- Cash Flow				
DESCRIPTION	**FY16**	**FY17**	**FY18E**	**FY19E**
PBT + Depreciation	112.0	113.6	110.4	161.7
Tax Paid	-22.6	-31.1	-22.8	-38.4
Changes in Working Capital	-89.8	-134.7	-121.5	-93.9
Cash Flow from Operations	**-0.4**	**-52.1**	**-33.9**	**29.4**
Cash Flow from Investing	**-28.7**	**-38.1**	**-75.6**	**-45.2**
Dividend Paid (Eq + Pref)	-3.6	-2.6	-2.6	-2.6
Proceeds from Equity	5.2	13.5	44.7	134.0
Free Cash Flow	-27.2	-27.1	-33.5	86.2
Debt (Repaid)/ Borrowed	**22.1**	**95.4**	**67.4**	**-115.6**
Opening Cash	100.5	98.5	166.9	166.9
Closing Cash	**122.6**	**166.8**	**166.9**	**166.9**

Ratio Analysis

Sunil Hitech Engineers Ltd.- Key Ratios				
DESCRIPTION	**FY16**	**FY17**	**FY18E**	**FY19E**
EBITM (%)	10.2	7.9	7.8	8.5
ROE (%)	12.7%	8.2%	8.0%	10.6%
ROCE (%)	17.5%	14.9%	14.6%	16.9%
Inventory Turnover(x)	4.1	4.3	4.0	4.1
Debtors Turnover(x)	7.2	8.0	7.3	7.4
Creditors Turnover(x)	3.7	4.6	4.6	4.6
Fixed Asset Turnover (x)	5.3	6.0	6.0	6.0
Receivable days	88	84	92	90
Inventory Days	51	46	50	49
Payable days	98	80	80	80
Total Debt/Equity(x)	1.2	1.3	1.2	0.8
Current Ratio(x)	2.1	2.3	2.4	2.3
Adjusted P/E Ratio	9.5	14.0	18.3	10.9
Price/ Book value	13.5	13.6	11.0	15.1

Annexure I: Details of HAM project

Sunil Hitech bagged a HAM project worth Rs. 982 cr during current fiscal year. The details are as follows:

Total Project Cost (incl O&M, inflation adjustment)	1,060 cr
Grant by NHAI (40% of Rs. 1,060 cr)	424 cr
Annuity to be received over 15 years (60% of Rs.1,060 cr)	636 cr
Financing:	
Grant from NHAI (as above)	424 cr
Debt	300cr
Equity	75 cr

- Company will receive grant of Rs. 424 cr (which is 40% of total project value) over 2.5 years from the date of financial closure. This will be like EPC revenue for the company.
- For the remaining 60% i.e. Rs. 636 cr, company will receive equal annuity of Rs. 42.4 cr over next 15 years (over FY22-FY36). Along with this company will also receive interest on WDV basis on the said Rs. 636 cr at 'Bank Rate plus 3%' which works out to 9.25%.
- Company will infuse equity of Rs. 75 cr and borrow another Rs. 300 cr at 9.75% for the project.

Year End (All figures in crore)	FY22	FY23	FY24	FY25	FY26	FY27	FY28	FY29	FY30	FY31	FY32	FY33	FY34	FY35	FY36
Inflows	42.4	84.8	127.2	169.6	212.0	254.4	296.8	339.2	381.6	424.0	466.4	508.8	551.2	593.6	636.0
Annuity from NHAI (60% of project Cost)	42.4	42.4	42.4	42.4	42.4	42.4	42.4	42.4	42.4	42.4	42.4	42.4	42.4	42.4	42.4
Interest from NHAI on 60% of project	54.9	51.0	47.1	43.1	39.2	35.3	31.4	27.5	23.5	19.6	15.7	11.8	7.8	3.9	0.0
O&M payment received	3.0	3.1	3.2	3.3	3.4	3.5	3.6	3.7	3.8	3.9	4.0	4.2	4.3	4.4	4.7
Total Revenue	**100.3**	**96.5**	**92.6**	**88.8**	**85.0**	**81.2**	**77.4**	**73.5**	**69.7**	**65.9**	**62.1**	**58.3**	**54.5**	**50.7**	**47.1**
Outflows															
Operational Cost															
O&M Expense	14.0	14.4	14.9	15.3	15.8	16.2	16.7	17.2	17.7	18.3	18.8	19.4	20.0	20.6	21.2
Total Expense	**14.0**	**14.4**	**14.9**	**15.3**	**15.8**	**16.2**	**16.7**	**17.2**	**17.7**	**18.3**	**18.8**	**19.4**	**20.0**	**20.6**	**21.2**
EBITDA	**86.3**	**82.1**	**77.8**	**73.5**	**69.2**	**64.9**	**60.6**	**56.3**	**52.0**	**47.7**	**43.3**	**38.9**	**34.6**	**30.2**	**25.9**
Interest @ 9.75%	29.3	27.7	25.6	23.2	20.5	17.1	14.3	11.2	7.6	4.4	2.1	0.0	0.0	0.0	0.0
Depreciation	27.7	27.7	27.7	27.7	27.7	27.7	27.7	27.7	27.7	27.7	27.7	27.7	27.7	27.7	27.7
Profit Before Tax	**29.4**	**26.7**	**24.5**	**22.6**	**21.0**	**20.1**	**18.6**	**17.5**	**16.7**	**15.6**	**13.5**	**11.2**	**6.9**	**2.5**	**-1.8**
Tax	10.0	9.1	8.3	7.7	7.2	6.8	6.3	5.9	5.7	5.3	4.6	3.8	2.3	0.8	0.0
Profit after tax	19.4	17.6	16.2	14.9	13.9	13.3	12.3	11.5	11.1	10.3	8.9	7.4	4.5	1.6	-1.8
Gross Cash accruals	**47.1**	**45.3**	**43.9**	**42.6**	**41.6**	**41.0**	**40.0**	**39.2**	**38.8**	**38.0**	**36.6**	**35.1**	**32.2**	**29.3**	**25.9**
Discount Rate @ 14%	0.9	0.8	0.7	0.6	0.5	0.5	0.4	0.4	0.3	0.3	0.2	0.2	0.2	0.2	0.1
Present Value of Cash Flows	41.3	34.9	29.6	25.2	21.6	18.7	16.0	13.8	11.9	10.3	8.7	7.3	5.9	4.7	3.6
PV as at end of FY22	253.3														
PV as at end of FY19	171.0														
Nos. of Shares	53.6														
Value per share	**3.2**														

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