Punj Lloyd Limited Q4 and FY13 Post Results Conference Call Transcript

May 13, 2013

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Moderator

Ladies and gentlemen, good day and welcome to Punj Lloyd's Q4 FY13 Earnings Conference Call. As a reminder for the duration of this conference, all participants' lines will be in the listen-only mode and there will be an opportunity for you to ask questions at the end of today's presentation. Should you need assistance during this conference call, please signal an operator by pressing "*" and then "0" on your touchtone telephone. Please note that this conference is being recorded. At this time, I would like to hand the conference over to Mr. Vinay Sood – Group Head, Investor Relations. Thank you and over to you sir.

Vinay Sood

Welcome to the Q4 and FY13 Earnings Conference Call. Joining us today on the call are members of our Senior Management Team, Mr. Atul Punj – Chairman, Mr. P. K Gupta – Director, Mr. P. N. Krishnan – Director, Designate F&A, Mr. Raju Kaul – President and CFO, Mr. Sanjay Goel – President and CEO, Punj Lloyd Engineering, Mr. Ravindra Kansal – President and CEO, ME & CIS, Mr. Atul Jain – President and CEO, ME & CIS.

I believe that you have received the Investor Communication and Results. Just to recap – Current order book stands at Rs. 22,499 crore. Consolidated revenue for Q4 stands at Rs. 3,307 crore, EBITDA at Rs. 276 crore, and PBT at Rs. 2 crore. The revenue for FY13 stands at Rs. 11,743 crore, EBITDA at Rs. 1,176 crore and PBT at Rs. 41 crore.

Before we begin, I would like to mention that some statements made during this call may be forward looking in nature and disclaimer to this effect has been sent to all with the conference call invitation.

I would also like to emphasize that while this call is open to all invitees, it may not be broadcasted or reproduced in any form or manner. We can now begin with the Q&A.

Moderator Thank you very much sir. Ladies and gentlemen, we will now begin the question and answer session. We have the first question from Ankit Babel of Subhkam Ventures.

Ankit Babel How frequently do you bill your contracts? For example, if you have a Rs. 100 crore project, with a 24 month execution cycle, how often do you bill it?

Atul Punj The bills are raised based on the terms of payment in each contract. They can be bills based on work done or on milestone basis.

Ankit Babel Your inventories in the books are very high to the tune of more than Rs. 6,500 crore. If you have a monthly billing cycle, how can the inventories be so high, that is almost 60% of your sales?

Raju Kaul One is billing based on time period and the other is milestone linked billing. It is a mix of both. Work in progress and available inventories are reflected in this figure. The figure of Rs. 6,000 crore plus is basically the billing which is yet to be done and which will happen over the next 1 or 2 months.

Ankit Babel We have been seeing high inventories in your balance sheet. Are there any projects that are stuck or certain projects which are getting executed but you are not getting it certified from clients so that you can bill them, is there some money stuck on that part as well?

Raju Kaul Yes. There is Libya and ONGC Heera where the OEC is on. These are also part of the WIP.

Ankit Babel During the quarter, there was Rs. 109 crore of other income and around Rs. 335 crore for the year. Could you give a broad break-up of the other income?

Raju Kaul Other Income for the full year consists of forex gain of Rs 240 crore, scrap sale of Rs. 12 crore, unspent liabilities and provisions written back of Rs 18 crore, gain in sale of investments of Rs 27 crore, profit on sale of fixed assets of Rs 6 crore, interest income of Rs 13 crore and others of Rs 19 crore.

Ankit Babel Is forex gain purely M to M or translation gain?

Raju Kaul It is a mix of both.

Ankit Babe What was the total Capex for FY13?

Raju Kaul Capex is Rs. 696 crore which includes around Rs. 275 crore on account of the development projects**.**

Ankit Babel What are your expectations for Capex for FY14?

Atul Punj Capex is linked to project wins. Based on projects that we win, we have to decide how much Capex we want to or do not want to incur. Hence, that is a moving target. We do not really have plans to build a factory this year which goes into production three years from now. The nature of the business is dependent on project to project wins.

Moderator Thank you. Our next question is from Rajesh Agarwal of Moneyore.

Rajesh Agarwal It has been mentioned that Rs. 89 crore has been written off in this year? Were there any write offs in this quarter?

Raju Kaul No.

Rajesh Agarwal What is the plan for debt and interest reduction?

Atul Punj We are currently in talks with some banks to do a debt swap so that we are able to reflect our borrowings more in the currencies in which revenue is being generated. We are looking at much lower rates of interest.

Rajesh Agarwal Is substantial reduction possible?

Atul Punj We are hoping for this.

Moderator Thank you very much. Our next question is from Kesvinder Suri of Span Capital.

Kesvinder Suri Could you just throw some light on the ground scenario in your key operating markets with respect to competitive intensity, orders and operational efficiencies?

Atul Punj We have diversified ourselves by being present in many geographies and this gives us a broader canvas to work on. This strategy has worked well for us especially since we have seen very little activity in India. But this strategy has inherent geographical risk. We saw that in Libya. That is actually our biggest exposure and it is now beginning to come back. For the upstream drilling business in Libya we now have the rig operating. We managed to get one rig out which is now operating in Gabon for Oil India. The one in Libya is now functioning and payments are coming through. The Oil & Gas projects currently, as we speak, are under re-negotiation in Tripoli. We hope to see some positive developments on that also within the next 60 days. Regarding the two infrastructure projects, we have received letters to restart work. So, we are re-mobilizing those projects. In the first 6 months of this year, we should start seeing some positive flows into the balance sheet from those projects. When you look at the petrochemicals space, some of the countries are being targeted by the South Koreans at a very aggressive pricing. We are not going in and dropping our prices just to win business. We want to make sure that we can execute them profitably and in a positive cash flow environment. That is true for places like Abu Dhabi but other places like Qatar and Saudi are fairly large markets where there is enough room for us to play. In South East Asia, you have the South Koreans in some countries and you do not have them in other countries. But they really seem to be the primary aggressive competition. In Africa, we are seeing that the Chinese pretty much with their subsidised finance are able to score wins, but we are well positioned on a couple of large projects there which hopefully should get locked up in the next 6 months. We are cutting our own path and are really being very choosy about which projects we are picking up so as not to get stuck in this competitive environment. Similarly, in India, we did not drop our prices and try to go aggressive on the BOT road projects in this massive rush for picking up BOT projects. We actually picked up none because we could not figure out the pricing that was prevalent. And now that things are moving upwards, we are re-looking at this space and hope we have some more prudent competition.

Kesvinder Suri Have you already bid or are you in preparation for bidding for BOTs in India in the near term?

Atul Punj Yes, we will be bidding now. We see that the competition has now moved more to the pure play EPC projects and thus in the BOT projects, the competition has reduced drastically. From 20 bidders there are around 4-5 bidders on the BOT projects and all are serious companies that can raise the financing for these projects. Most of the people who had rushed in are not able to raise finance because of the very aggressive bids that they had put in earlier.

Kesvinder Suri I will tackle the BOT part first. Would you be looking at fresh bids or would you be open to picking up certain distress work in progress or projects which are underway and you could get them at fairly good valuations?

Atul Punj Combination. Both are work in progress.

Kesvinder Suri These types of projects do entail a great degree of financing and since you are struggling with your debt how do you propose to tackle that situation? Would you look at forming a separate vertical and looking at equity funding into that?

Atul Punj Yes, each BOT project is a separate SPV anyway. We are open to look at how we can restructure that because for good projects there is enough money floating around. The projects that were very aggressively bid are the ones which are struggling to find the justification for their numbers. But we find that for good projects, where the construction risk is relatively low or is almost over; there is enough money available globally. So, we have to be prudent to pick & choose the kind of projects that we want to take. You said correctly that right now we are working for the banks, and we are not really working for any of us. That is one of the initiatives that we have launched on debt restructuring. We are swapping it with foreign currency debt to reflect our foreign currency earnings. We have a natural hedge in forex as well. We are taking advantage of that now and on top of that, we are looking at some assets' sale which will drop the debt down to more reasonable levels.

Kesvinder Suri Have you identified these non-core assets and what quantum could they fetch you over a 2 or 3 year horizon?

Atul Punj It is work in progress. I would not want to comment on that. Mandates have been given out. Strategic sales of some assets to a partner who has financial muscle can help us grow. We are not really looking at a pure play financial investor but for a strategic partner with deep pockets who can then assist us to grow going forward because at the current rates of bank finance and lack of alternate instruments, it is impossible to develop across the financial regime.

Kesvinder Suri You have been through the worst, are you approaching the light at the end of the tunnel kind of a situation or you still have some way to go? How do you term it?

Atul Punj We are pretty much done with all the bad news. Now, it is a function of recovering from all that bad news in a gradual manner. Libya would be a big help. The ONGC dispute that we are resolving through the outside expert committee nominated by ONGC is now coming to a close. There are a few developments happening. So, God willing, things should start playing out now in the next 3 to 6 months.

Kesvinder Suri If these things do pan out the way you hope over the next 1 or 2 quarters, where do you see Punj Lloyd three years down the line in terms of size or your vision or aspiration?

Atul Punj It is not fair to ask that question because, given the current environment, I do not think anybody's vision really can be converted to reality.

Kesvinder Suri We are going through a lot of uncertainty today in terms of regulatory as well as a lot of other factors. Where do you aspire to see the group?

Atul Punj We want to have about 90% of our business overseas up from 70% currently. We will be very choosy about the projects that we pick in India. We would only go for those that make sense. Essentially, we really have a nomadic business. We do not have a particular factory that we have founded into somebody's land. We are a construction EPC group and we go where we want to do business. We get our margins from the clients by delivering a good job to them. So, in that sense, in terms of work split, we are looking to increase internationally. Our defense business is expected to grow quite smartly and on the infrastructure development side, given the opportunities that are now emerging it can be a primary driver as well.

Moderator Thank you. Our next question is a follow up question from Rajesh Agarwal of Moneyore.

Rajesh Agarwal When are our mining operations in Indonesia going to start?

Atul Punj We are waiting for the last regulatory approval. It should start seeing the light of day hopefully in the next quarter.

Rajesh Agarwal Our order book has again started changing from Oil & Gas to Infra. The current order back log is 50% Infra and 50% other businesses. Do you feel margins will be under pressure or are the margins from the Infra orders which we have abroad in Sembawang better than Infra in India?

Atul Punj Yes, there are generally better margins for sure and the important thing is that we are able to execute them efficiently because the contracting regime is much fairer overseas than it is in India and we will see this trend continuing. The Infra space is probably going to be as large, if not larger than the Oil & Gas space. Oil & Gas is dependent on new finds, new field developments and in that direction there are a few that are taking place right now. The major bulk of the investment even in the oil producing GCC countries is now shifting from only Oil & Gas investments into a lot of social Infrastructure work and that is a direct reaction to the Arab springs where governments are now minded that they need to improve a lot of their people and that is really resulting in a lot of projects in the Infra space.

Rajesh Agarwal Will there be any major breakthrough in the Oil & Gas orders? How is the traction in that?

Atul Punj We picked up some nice offshore business recently. We are looking at some good opportunities. Iraq is looking good. There are a couple of projects there that are looking good. This is a lumpy business, it is not a consistent quarter-on-quarter business and that is the nature of the business.

Rajesh Agarwal Was there any major breakthrough in the Oil & Gas orders in African countries?

Atul Punj There are some projects which I do not want to disclose because competition tends to chase us quite quickly but we are definitely moving ahead.

Rajesh Agarwal What will be the EBITDA level margin in Infra abroad, like in the Middle East and other regions?

Atul Punj Infra would be about 12 – 13% on an EBITDA level, may be even 15%.

Rajesh Agarwal Can Infra orders in Libya begin shortly?

Atul Punj Two of them already are restarting right now. Out of balance four projects – one Oil & Gas project and three Infra projects are under negotiation.

Rajesh Agarwal Once Libya starts, can the cash flow be better?

Atul Punj From your mouth to God's ears.

Moderator Thank you very much. Our next question is from Amit Sinha of Macquarie Capital.

Amit Sinha Would you like to give any guidance in terms of revenue growth and margins for FY14?

Atul Punj We do not believe in giving forward guidance. The only guidance that we can give is that our order backlog is robust; a lot of the business that was stuck will come back online this year. This will show up in our balance sheet as well. Beyond that, I would not want to comment.

Amit Sinha Directionally, do you see margins improving?

Atul Punj Margins are going to improve from a few other factors that we are working on. The debt piece is the important one. The other is operational efficiencies. Both of which are getting a lot of our attention and it should get reflected in our numbers, shortly.

Amit Sinha BOT road projects have been quiet, since last one year. Do you see NHAI coming up with fresh bids?

Atul Punj We have a great chairman at NHAI now and if anybody has the ability to make changes, it is him. He seems to be on the right track. Hopefully, the Government will support him in his endeavors. They are all conscious that unless Infra moves, the country's GDP is going to continue slowing down. There is a direct intervention from the PMO now to get this sector moving back up again. What is really to be seen in the BOT projects is that how much finance banks will provide to BOT projects, given their recent experiences. This is the single biggest challenge. Unless the Government comes up with alternate financing instruments whether global or domestic, that would allow money to flow into the sector, it will remain challenging.

Amit Sinha There are issues in the already bid projects. Do you see them going for new projects before solving the old issues?

Atul Punj No, there are a lot of changes now in the way that they are pitching projects. There is some debate happening in the top level of the Government as we speak on making the terms a little more realistic. Our USP is that we did not get stuck into that herd mentality that everybody has seemed to have got stuck into by picking up BOT projects, which were unviable. We do not have anything in our portfolio that was actually given out maybe more than 3 years ago on the BOT side. We have won annuity projects but there is no traffic risk or right of way risk in those projects.

Amit Sinha In the last 9 months, you have reported a loss of around Rs 1.7 billion. So, was there a loss this quarter with respect to the Indonesian offshore platform?

Atul Punj No, that was pretty much written off as it happened. It was only a combination of regulatory issues that affected our performance. The laws changed in the country. So, our barge that was positioned to go into the country to do the work could not go in and that really resulted in a huge cost overrun over there. It was really a regulatory issue. A few others in the country also got impacted negatively.

Amit Sinha For this quarter, was there no loss?

Raju Kaul There was a marginal loss of around Rs. 10 crore.

P K Gupta It was basically on our power projects where extra claims have been put in. We have about $12-13 million of extra claims, out of which they have paid about $5 million. So, rest of it is under negotiations. We have not taken into account those extra claims and that is why loss was booked. However, when these extra claims are realized, which we expect in the coming quarters, we will be able to book it.

Amit Sinha What is the order inflow for this 4th quarter?

Raju Kaul For the year we have booked around Rs. 6,459 crore and for this quarter it is Rs 954 crore

Moderator Thank you very much. Our next question is from Prerna Jhavar from Emkay Global.

Prerna Jhavar What is the value of the orders that we expect to begin in Libya?

Raju Kaul Order backlog in Libya is Rs. 4,526 crore.

Prerna Jhavar Out of this, what should be the value that we are about to commence?

Atul Punj We are about to commence about half of that and the balance half is under renegotiation as we speak. There is a team sitting in Tripoli right now.

Moderator Thank you very much. We have a follow-up question from Kesvinder Suri of Span Capital Please go ahead.

Kesvinder Suri You just mentioned that the biggest challenge for the BOT sector is about banks willing to finance with regards to the recent experience. What are the other challenges you see to your business as it stands today?

Atul Punj The new tenders on the BOT side are really coming out where at least 80% of continuous right of way is available before the tenders are even floated. The NHAI has minded now of not giving right of way in bits and pieces. You cannot be hopping and taking all your equipment around in a two kilometer gap because of right of way acquisition issues. There is some serious rethink going on and it is the classic Indian mindset that we have to drop to the absolute bottom before we spring back up again. We are pretty much dropped there and now in an attempt to create an environment collectively with the private sector on how to come back. So, hopefully this year should be a change in the way that the BOT projects across the board are run in the country.

Kesvinder Suri What are the challenges for the other verticals?

Atul Punj The other verticals pretty much tick along. Not too many major investments happening in India which is why our focus is so much outside, where the international oil companies, each one is spending between $30 and $40 billion annually. So, we add up to nine companies in that category. They have significant quantum of work that one can expect to get and that is what we are doing.

Kesvinder Suri What does the defense opportunity looks like for you?

Atul Punj Our defense plant in Malandpur is now up and running. It is a very hi-tech, high precision large component fabrication machining facility. We are doing work for HAL, BHEL, and a bunch of highly precision-oriented components and as we move along, we will look to participate in some of the defense programs and see what packages we can get and work on an integration basis also. We have a couple of bids where trials have happened. We have shortlisted two companies. Let us see how that plays out. Nothing is done till it is done in that sector.

Moderator Thank you. Our next question is from Ronald Siyoni of ShareKhan.

Ronald Siyoni There was about Rs. 240 crore Forex gain during the year and about Rs. 70 crore was in Q3. How much was the gain in Q4-FY13?

Raju Kaul It was around Rs. 69 crore.

Ronald Siyoni On the margins front, in the last two years, this has been the lowest margin, based on increase in the other expenditure as well as raw material cost, any specific projects on which there were cost overruns?

Raju Kaul There was no specific reason. It is dependent on the revenue mix i.e. whether we are doing more of pure construction or EPC in a particular quarter. The value keeps changing between procurement and construction.

Ronald Siyoni Is it just because of a mix that the margins have been so low?

Raju Kaul Yes.

Ronald Siyoni Our execution was higher during the quarter, but employee cost was lower during the quarter, is there any particular reason behind lower employee expenditure?

Atul Punj We have done a lot of restructuring in terms of creating operational efficiencies and that is reflecting in lower numbers.

Ronald Siyoni Is there any particular reason for the tax write-back of Rs. 10.9 crore?

Raju Kaul Yes, in the last quarter, there were some adjustments in tax on account of full year. There was a slight write-back.

Ronald Siyoni Was this due to higher taxes payment during the previous quarter?

Raju Kaul This has been because of adjustment for previous three quarters.

Moderator Thank you. As there are no further questions from the participants, I would now like to hand the conference over to the management for closing comments.

Atul Punj Thank you all for attending the conference. We shall see better numbers going forward. We have got our heads down and trying to make sure that the efficiencies kick in. Hopefully, we will start seeing some positive news pretty soon.

Moderator Thank you very much sir. Ladies and Gentlemen, on behalf of Punj Lloyd, that concludes this conference call.