Engineered to succeed

Punj Lloyd's USP is its shift towards larger and more complex projects. Its valuation looks attractive, despite recovery on the price front

STOCK IDEA

PUNJ LLOYD is the second-largest engineering company in India and is present in the infrastructure and energy sectors. Like other stocks in the construction space, Punj Lloyd has seen a sharp correction in the past few weeks — from a level of Rs 1,000, the stock had come down to Rs 731.5 recently. Given the company's prospects, its valuation still looks attractive, despite some recovery on the price front. Moreover, due to its project profile, the impact of the tax proposals on infrastructure companies will have a minimal impact on the company's bottomline. This is because the company has a lower exposure to sectors such as roads and irrigation, where these sops were being contested.

FINANCIALS: Punj Lloyd recorded a turnover of Rs 3,423 crore for the nine months ended December '06 on a consolidated basis. Standalone turnover for the same period was Rs 1,441 crore. Net profit stood at Rs 107.5 crore and Rs 38.4 crore on s consolidated and standalone basis, respectively.

Punj Lloyd has a number of subsidiary companies, which operate in the countries where it is active. However, the bulk of the difference between its standalone and consolidated figures is on account of a single subsidiary Sembawang, which it acquired in '06. Sembawang has a large order backlog taken up at low margins — this will impact Punj Lloyd's margins for the next two years.

CONCERNS: One major concern for the company is low profit margins — its net profit margin for three quarters was only 3.1%. The company also seems to be inefficient at working capital management. Its current debt-equity ratio is 0.9:1. For funding growth and fresh capital expenditure, the company needs to raise additional capital. An enabling resolution to that effect was adopted recently. The company raised $125 million via a five-year foreign currency convertible bond (FCCB) last year — the conversion price is well above the current market price.

PROSPECTS: Punj Lloyd has executed projects in sectors such as roads, oil & gas pipelines and process plants. Its project profile sets it apart from other similar size construction companies like Gammon or Hindustan Construction. The company had a consolidated order backlog of Rs 14,357 crore at the end of '06 — about four times its consolidated nine-month sales. The last big order bagged by the company was a $290-million contract for building an offshore oil & gas production platform for ONGC. This makes Punj Lloyd the second Indian company with the capability to fabricate such equipment. In the recent past, it has also bagged some large orders in power, oil refining, pipelines and petrochemicals. Most of the new orders have been worth over Rs 500 crore.

VALUATIONS: Punj Lloyd's USP seems to be its changing work profile, i.e. opting for larger and more complex projects. These projects can offer better margins since there is a lot of competition in this segment. The company also has a higher geographical spread compared to its peers. Its P/E multiple on FY07 earnings is likely to be below 30, which is not steep if its topline grows at 30-40%.

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PUNJ LLOYD'S FINANCIALS

COUNTRY	PROJECT DETAILS	VALUE
India	Heera Redevelopment Project, ONGC	1,300
Thailand	Petrochem Plant	NA
Qatar	Gas Pipeline	804
India	Haldia Refinery Upgrade, IOC	1,163
Libya	Gas Pipeline	1,348
India	Power Plant, Rajasthan	823

SOURCE: COMPANY

COMPANY RESULTS	Q3	9M
Net Sales	1,433	3,423
Other Income	30	63
PBDIT	113	267
PBT	56	137
Net Profit	48	108
EPS (Rs)	9.25	20.68

(RS CRORE)

COMPARATIVE P/E*	
Gammon	27.8
Hindustan Construction	27.1
IVRCL	31.7
Nagarjuna Construction	20.9
Punj Lloyd	112.2

*Trailing Four-Quarter

SOURCE: ETIG