



India

**Neutral** (previously Overweight)**Highlighted Companies****Dilip Buildcon Ltd****ADD, TP Rs400, Rs217 close**

DBL has a strong order book or OB (2.7x TTM sales) and 80% of the OB is expected to be under the construction phase in FY24F. DBL trades at an attractive valuation of 4.1x FY23F EV/EBITDA, at a 42% discount to its five-year average.

**Summary Valuation Metrics**

P/E (x)	Mar23-F	Mar24-F
Dilip Buildcon Ltd	7.27	6.23
P/BV (x)	Mar23-F	Mar24-F
Dilip Buildcon Ltd	0.95	0.83
Dividend Yield	Mar23-F	Mar24-F
Dilip Buildcon Ltd	0.55%	0.55%

# Construction

## 3QFY23F results preview

- We expect steady engineering, procurement, and construction (EPC) sales in 3QFY23F, driven by robust order book.
- Dilip Buildcon (DBL) trades at a 42% discount while PNC Infra (PNC) and NCC trade at close to their respective five-year avg. EV/EBITDA. KNR Constructions (KNR) trades at a 22% premium to its five-year avg. EV/EBITDA.
- After a sharp run-up in stock prices in the last three months (up 18% on an avg.), we believe that only DBL has a significant near-term upside (TP Rs400). Therefore, we downgrade the sector to Neutral (from Overweight earlier).

### 3QFY23F results expectations

Since Mar 2020, the order inflow has picked up (Rs1,224bn over FY21-2QFY23), resulting in average OB/sales at 2.8x (Sep 2022). The companies in our coverage must fund 24% of their latest order book or OB (like in Mar 2019). We expect steady EPC sales in 3QFY23F driven by a strong order book and a high proportion of projects under construction. For toll-based assets, we forecast a ~5% qoq rise in revenue.

### Execution can rerate DBL; PNC, NCC and KNR trade at fair valuations

Dilip Buildcon (DBL) trades at a 42% discount while PNC Infra (PNC) and NCC trade at close to their respective five-year average EV/EBITDA. We believe strong EPC sales growth in FY23F-24F can rerate the valuation multiple of DBL. KNR Constructions (KNR) trades at a 22% premium to its five-year average EV/EBITDA. DBL and NCC have the highest target EPC segment enterprise value as a proportion of target equity valuation. Rerating of EV/EBITDA multiple and/or a strong financial performance can have the highest impact on DBL and NCC. Consolidated net debt/market capitalization is high for DBL. Thus, an expansion in the enterprise value or EV of DBL can have a substantial impact on its share price.

### Post sharp run-up, we feel only DBL has significant near-term upside

During the last three months, CMP of stocks in our coverage universe rose by 18% on an average (IRB Infra rose by 47%, NCC by 25%, PNC Infra by 10%, KNR by 14% and IRB InvIT by 12%). We believe the near-term upside is limited in these stocks. Only Dilip Buildcon or DBL remained flattish over the last three months. We have used EV/EBITDA multiple for valuation of the EPC segment, discounted cash flow for operational road assets and 1x capex for under-construction road assets. Our target valuations are (a) DBL (TP: Rs400), valuing its EPC business at 5x FY24F EV/EBITDA (25% discount to five-year median), (b) PNC Infra (TP: Rs316), valuing its EPC business at 6x EV/EBITDA (close to five-year median), (c) IRB Infra (TP: Rs293), valuing its EPC segment at 4x EV/EBITDA, (d) NCC (TP: Rs80), valuing its EPC segment at 5.5x EV/EBITDA (15% discount to five-year median), and (e) KNR (TP: Rs261), valuing its EPC segment at 7.5x EV/EBITDA (11% premium to five-year median). Difficulties in financial closure of new Hybrid Annuity Model (HAM) projects and a slowdown in project execution are key downside risks for the sector.

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**Figure 1: 3QFY23F estimates for companies in our coverage universe**

(Rs m)	Revenue	yoy %	qoq %	EBITDA	yoy %	qoq %	Adj. PAT	yoy %	qoq %
IRB Infra	15,738	23	23	6,599	(11)	9	945	(31)	89
IRB InvIT	2,141	(38)	7	1,713	(39)	8	827	374	12
Dilip Buildcon	25,932	18	15	3,112	4,846	19	684	-	216
PNC Infra	15,976	5	2	2,077	2	0	1,285	7	(2)
NCC	33,350	23	11	3,335	14	16	1,481	33	22
KNR Construction	8,429	10	3	1,602	1	2	1,481	15	20

SOURCE: INCRED RESEARCH, COMPANY REPORTS

## 3QFY23F results preview

**Figure 2: 3QFY23F estimates for companies under our coverage**

Company	3QFY23F	3QFY22	yoy %	2QFY23	qoq %	Comments
<b>IRB Infra (Consolidated)</b>						
Sales (Rs m)	15,738	12,791	23.0	12,840	22.6	We estimate 11% yoy rise in EPC sales. We estimate 10% qoq rise in BOT Sales driven by traffic.
EBITDA (Rs m)	6,599	7,384	(10.6)	6,061	8.9	
EBITDA margin %	41.9	57.7		47.2		
Adj. PAT (Rs m)	945	1,374	(31.2)	500		
<b>IRB InvIT (Consolidated)</b>						
Sales (Rs m)	2,141	3,466	(38.2)	1,994	7.4	We expect 38% yoy decline in sales as 2 projects which contributed 53% to FY22 EBITDA have been handed over to the awarding authority post Mar 2022.
EBITDA (Rs m)	1,713	2,809	(39.0)	1,591	7.7	
EBITDA margin %	80.0	81.0		79.8		
Adj. PAT (Rs m)	827	174	374.0	735	12.4	
<b>Dilip Buildcon (Standalone)</b>						
Sales (Rs m)	25,932	21,976	18.0	22,619	14.6	We expect 18% yoy rise in sales and 12% EBITDA margin. This is slightly higher than 11.6% EBITDA margin in 2QFY23 but below historical margins of 16-17%.
EBITDA (Rs m)	3,112	63	4,845.8	2,613	19.1	
EBITDA margin %	12.0	0.3		11.6		
Adj. PAT (Rs m)	684	(1,560)		216		
<b>PNC Infra (Standalone)</b>						
Sales (Rs m)	15,976	15,220	5.0	15,611	2.3	We expect just 5% yoy sales growth and 13% EBITDA margin, similar to historic level.
EBITDA (Rs m)	2,077	2,045	1.6	2,070	0.3	
EBITDA margin %	13.0	13.4		13.3		
Adj. PAT (Rs m)	1,285	1,200	7.1	1,311	(1.9)	
<b>NCC (Standalone)</b>						
Sales (Rs m)	33,350	27,039	23.3	30,037	11.0	We expect 23% yoy rise in sales and steady EBITDA margin of 10%, similar to historic level.
EBITDA (Rs m)	3,335	2,928	13.9	2,886	15.5	
EBITDA margin %	10.0	10.8		9.6		
Adj. PAT (Rs m)	1,481	1,110	33.5	1,216	21.8	
<b>KNR Constructions (Standalone)</b>						
Sales (Rs m)	8,429	7,663	10.0	8,155	3.4	We expect 10% yoy sales growth and strong 19% EBITDA margin.
EBITDA (Rs m)	1,602	1,589	0.8	1,569	2.1	
EBITDA margin %	19.0	20.7		19.2		
Adj. PAT (Rs m)	911	794	14.8	757	20.4	

SOURCE: INCRED RESEARCH ESTIMATES, COMPANY REPORTS

### Strong order flow of FY21-22 continues in YTD FY23 ▶

After a strong order flow in FY18-19, net order flow plummeted in FY20 to Rs39bn (90% yoy decline) for EPC companies in our coverage, partly due to order cancellations in FY20 for NCC (Rs132bn) and IRB Infra (Rs35bn). Adjusted for cancellations, FY20 order inflow was at Rs211bn (50% yoy decline).

For EPC companies in our coverage, sales grew 36% yoy in FY19 due to strong order book (OB)-to-sales ratio in FY18 (average 3.6x) and healthy order flow in FY19. In FY20, sales declined 5% yoy as the order flow dried up. OB-to-sales ratio declined to just 2.2x in FY20. Since Mar 2020, order flow has picked up (Rs1,224bn in FY21-YTD FY23). Thus, average OB-to-sales ratio for companies under our coverage was 2.8x (latest). This augurs well for sales growth in FY24F.

**Figure 3: Order flow over FY19 to YTD FY23 for EPC companies in our coverage**

(Rs bn)	Order inflow				
	FY19	FY20	FY21	FY22	YTD FY23
Dilip Buildcon	64	69	175	72	56
NCC	207	(64)	186	99	71
PNC Infra	80	12	79	92	78
IRB Infra	6	(12)	68	73	60
KNR Constructions	38	35	48	52	15
<b>Total</b>	<b>396</b>	<b>39</b>	<b>557</b>	<b>388</b>	<b>280</b>

SOURCE: INCRED RESEARCH, COMPANY REPORTS

**Figure 4: OB-to-sales and sales growth of EPC companies in our coverage universe**

	Order book/ Sales (x)						yoy Sales growth (%)				
	FY18	FY19	FY20	FY21	FY22	Latest	FY19	FY20	FY21	FY22	1HFY23
Dilip Buildcon	3.1	2.3	2.1	3.0	2.8	2.7	18	(2)	3	(2)	14
NCC	4.3	3.4	3.2	5.2	4.0	3.4	60	(32)	(12)	39	47
PNC Infra	4.1	4.0	1.8	2.4	2.4	2.9	71	55	3	26	18
IRB Infra	3.9	2.4	0.9	2.0	2.7	2.5	19	11	(25)	13	(14)
KNR Constructions	1.2	1.9	2.4	2.6	2.8	2.5	11	5	20	22	14
<b>Total</b>	<b>3.5</b>	<b>2.9</b>	<b>2.2</b>	<b>3.3</b>	<b>2.9</b>	<b>2.8</b>	<b>36</b>	<b>(5)</b>	<b>(5)</b>	<b>18</b>	<b>17</b>

SOURCE: INCRED RESEARCH, COMPANY REPORTS

### 23% of latest OB has to be funded by private road developers, similar to FY19 (24%) ▶

Around 20% of latest OB of companies in our coverage comprise hybrid annuity model (HAM) projects. The concessionaire bears 60% of the project cost of HAM projects and the project-awarding authority bears the remaining 40%.

12% of latest OBs comprise build-operate-transfer (BOT) projects which the concessionaire has to fund entirely. As a result, the companies in our coverage have to fund 23% of latest OB.

**Figure 5: Percentage of OBs to be funded by companies in our coverage universe**

(Rs bn)	Order book - FY19		Order book - Latest	
	Total	% to be funded by company	Total	% to be funded by company
Dilip Buildcon	212	30	263	24
NCC	412	-	400	-
PNC Infra	122	34	193	33
IRB Infra	111	85	88	97
KNR Constructions	40	40	88	29
<b>Total</b>	<b>897</b>	<b>24</b>	<b>1,032</b>	<b>23</b>

SOURCE: INCRED RESEARCH, COMPANY REPORTS

### Divergent FY24F EV/EBITDA valuations – stock-picking is key ▶

PNC Infra and NCC trade close to their respective five-year average EV/EBITDA. KNR Constructions trades at a 22% premium to its five-year EV/EBITDA. We believe the premium is justified as its OB/sales ratio (2.5x) is a tad higher than the historical level. We believe the near-term upside in these three stocks will be limited. DBL trades at a 42% discount to its five-year average EV/EBITDA. We believe the strong EPC sales growth in FY23F-24F can re-rate its valuation multiple close to historical level.

**Figure 6: Valuations of main third-party construction companies**

	EV/ EBITDA (x) for EPC segment			Premium (%) of current FY24F multiple vs.	
	5-year average	Mar 17-19	Current FY24F	5-year average	Mar 17-19
Dilip Buildcon	6.6	7.6	3.8	(42)	(50)
NCC	6.5	6.7	6.0	(8)	(10)
PNC Infra	6.1	8.2	5.6	(8)	(32)
KNR Constructions	6.4	6.8	7.8	22	15
<b>Average</b>	<b>6.4</b>	<b>7.3</b>	<b>5.8</b>	<b>(9)</b>	<b>(21)</b>

SOURCE: INCRED RESEARCH, COMPANY REPORTS

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