

## Larsen & Toubro

### Performance Highlights

#### Quarterly highlights - Standalone

Y/E March (₹ cr)	4QFY16	3QFY16	4QFY15	% chg (yoy)	% chg (qoq)
Net sales	21,061	14,774	18,968	11.0	42.6
EBITDA	3,193	1,002	2,491	28.2	218.7
Adj. PAT	2,616	791	1,875	39.5	230.7

Source: Company, Angel Research

**Standalone numbers impress:** For 4QFY2016, Larsen & Toubro (L&T) reported an 11% yoy increase in the top-line to ₹21,061cr, which is slightly lower than our expectation. Revenue growth on a yoy basis reflects an 11.7%/ 33.3% increase in Infrastructure/ Power segment. EBITDA for the quarter came in higher than our expectation at ₹3,193cr. With some of the projects attaining revenue recognition threshold level, EBITDA margins expanded 203bp yoy to 15.2%. This is the first quarter after three successive quarters where the company reported yoy increase in its EBITDA margin. Further, the PAT at ₹2,539cr has come in ahead of our estimate. On adjusting for gains on divestment of stake in the Foundry business (₹48.5cr) and provision for impairment on the value of investment (₹135cr), Adjusted PAT stood at ₹2,616cr. Adj. PAT margin improved 254bps yoy to 12.4% in 4QFY2016.

Order inflows for consolidated entity in FY2016 declined 9.0% yoy to ₹43,334cr. The order backlog stands at ₹2,49,949cr, thereby giving revenue visibility for over the next 10 quarters.

**Hydro-carbon business reports minimal losses:** With completion of legacy projects in the international business, strong execution from ongoing projects helped the Hydro-carbon segment report 10.9% yoy increase in revenues to ₹2,479cr. For the quarter, the segment reported an EBIT level loss of ₹92cr vs a loss of ₹209cr in the corresponding quarter a year ago.

**Key positives:** More clarity on ongoing asset divestments, IDPL restructuring, completion of Hydro-carbon legacy projects; net WC cycle at 24% of sales.

**Key Negatives:** Miss on FY2016 order inflow guidance.

**Outlook and valuation:** L&T's diversified presence and an anticipated recovery in the capex cycle coupled with the company's strong balance sheet comfort us that it is well positioned to benefit from a revival in the award activity environment. With order backlog expected to grow, execution should pick-up gradually. We have valued the company using the sum-of-the-parts (SoTP) methodology to capture the value of all its businesses and investments. Ascribing separate values to its parent business (on a P/E basis) and investments in subsidiaries (using P/E, P/BV and M-cap basis), we arrive at FY2017E based target price of ₹1,700. We are of the view that L&T is a good proxy play for investors wanting to ride on the revival of the Indian infrastructure growth story. **Given the 15.3% upside potential in the stock from the current levels, we upgrade to BUY rating on the stock.**

#### Key financials (Standalone)

Y/E March (₹ cr)	FY13	FY14	FY15	FY16	FY17E	FY18E
Net Sales	51,611	56,599	57,017	59,780	67,665	77,249
% chg		9.7	0.7	4.8	13.2	14.2
Net Profit	4,385	5,493	5,056	4,191	5,380	6,685
% chg		25.3	(8.0)	(17.1)	28.4	24.3
EBITDA (%)	10.6	11.8	11.4	10.3	10.7	11.5
EPS (₹)	53	59	54	57	57	71
P/E (x)	27.9	25.0	27.3	26.1	25.7	20.7
P/BV (x)	3.2	3.0	2.7	2.5	2.4	2.2
RoE (%)	14.2	15.6	13.3	15.1	12.6	14.3
RoCE (%)	17.5	18.7	16.3	14.5	15.6	17.6
EV/Sales (x)	2.5	2.6	2.6	2.5	2.2	1.9
EV/EBITDA (x)	23.8	21.9	22.9	24.1	20.7	16.6

Source: Company, Angel Research; Note: CMP as of May 27, 2016

## BUY

CMP	₹1,475
Target Price	₹1,700

Investment Period	12 Months
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#### Stock Info

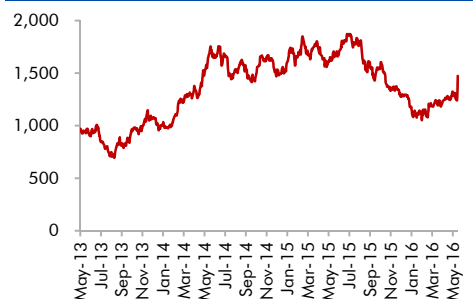
Sector	Infrastructure
Market Cap (₹ cr)	137,404
Net debt (₹ cr)	11,927
Beta	1.3
52 Week High / Low	1,887 / 1,017
Avg. Daily Volume	2,283,576
Face Value (₹)	2
BSE Sensex	26,654
Nifty	8,157
Reuters Code	LART.BO
Bloomberg Code	LT@IN

#### Shareholding Pattern (%)

Promoters	-
MF / Banks / Indian Fls	39.1
FII / NRIs / OCBs	16.6
Indian Public / Others	44.4

Abs. (%)	3m	1yr	3yr
Sensex	15.9	(4.1)	32.2
LT	36.6	(9.5)	52.0

#### 3-year price chart



Source: Company, Angel Research

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**Exhibit 1: Quarterly Performance (Standalone)**

Particulars (₹ cr)	4QFY16	3QFY16	% chg (qoq)	4QFY15	% chg (yoy)	FY16	FY15	% chg
<b>Net Sales</b>	<b>21,061</b>	<b>14,774</b>	<b>42.6</b>	<b>18,968</b>	<b>11.0</b>	<b>59,780</b>	<b>57,017</b>	<b>4.8</b>
<b>Total Expenditure</b>	<b>17,868</b>	<b>13,772</b>	<b>29.7</b>	<b>16,477</b>	<b>8.4</b>	<b>53,609</b>	<b>50,529</b>	<b>6.1</b>
Operating Expenses	16,213	11,819	37.2	14,799	9.6	46,629	44,380	5.1
Employee benefits Expense	1,037	1,200	(13.5)	1,022	1.5	4,480	4,162	7.6
Sales, Admin & Other Expenses	618	753	(18.0)	656	(5.9)	2,500	1,986	25.9
<b>EBITDA</b>	<b>3,193</b>	<b>1,002</b>	<b>218.7</b>	<b>2,491</b>	<b>28.2</b>	<b>6,171</b>	<b>6,488</b>	<b>(4.9)</b>
EBIDTA %	15.2	6.8		13.1		10.3	11.4	
Depreciation	255	244	4.1	246	3.5	999	1,008	(0.9)
EBIT	2,939	757	287.9	2,245	30.9	5,172	5,480	(5.6)
Interest and Financial Charges	397	381	4.2	335	18.7	1,449	1,420	2.1
Other Income	737	617	19.4	570	29.2	2,406	2,283	5.4
PBT before Exceptional Items	3,278	993	230.0	2,480	32.2	6,129	6,344	(3.4)
Exceptional Items	77	(92)		(186)		(560)	(357)	
PBT after Exceptional Items	3,201	1,085	195.0	2,666	20.1	6,689	6,701	(0.2)
Tax	662	202	227.2	605	9.3	1,378	1,645	(16.3)
% of PBT	20.7	18.6		22.7		20.6	24.5	
<b>PAT</b>	<b>2,539</b>	<b>883</b>	<b>187.6</b>	<b>2,061</b>	<b>23.2</b>	<b>5,311</b>	<b>5,056</b>	<b>5.0</b>
<b>Adj. PAT (for excep. Items)</b>	<b>2,616</b>	<b>791</b>	<b>230.7</b>	<b>1,875</b>	<b>39.5</b>	<b>4,751</b>	<b>4,699</b>	<b>1.1</b>
Adj. PAT %	12.4	5.4		9.9		7.9	8.2	
Dil. EPS	27.08	9.44	186.9	21.95	23.4	56.80	54.10	5.0

Source: Company, Angel Research

## Standalone business

### Revenues grew 11% yoy

For the quarter L&T reported an 11% yoy increase in the top-line to ₹21,061cr, which is slightly lower than our expectation. Revenue growth on a yoy basis reflects an 11.7% increase in the Infrastructure segment and a 33.3% increase in the Power segment. Revenue growth across the Infrastructure segment was owing to some of the projects awarded in 4QFY2015 reaching the threshold of revenue recognition. Within the Infra segment, the Transportation Infra, Heavy Civil and Waters businesses contributed to the revenue growth. Surge in Power segment revenue is on account of substantial progress seen across coal and gas based projects under execution. Lower opening order book and slow execution led to 2.2% and 6.1% yoy revenue de-growth across Metallurgical & Material Handling (MMH) and Electrical & Automation (E&A) segments, respectively.

For the full year FY2016, a strong 44.7% and 3.7% yoy increase in revenue booking across Power (10.7% of FY2016 revenue) and Infrastructure (69.8% of FY2016 revenue) segments led the company to report a 4.8% yoy increase in revenue to ₹59,780cr.

**Exhibit 2: Segment-wise Gross Revenue Split (Standalone)**

Particulars (₹ cr)	4QFY16	3QFY16	% chg (qoq)	4QFY15	% chg (yoy)	FY16	FY15	% chg
Infrastructure	15,949	9,785	63.0	14,278	11.7	42,175	40,652	3.7
Power	1,901	2,107	(9.8)	1,425	33.3	6,451	4,459	44.7
Metallurgical & Material Handling	905	678	33.4	925	(2.2)	2,756	3,303	(16.5)
Heavy Engineering	946	826	14.6	939	0.8	2,935	3,299	(11.0)
Electrical & Automation	1,236	1,085	13.9	1,316	(6.1)	4,228	4,129	2.4
Others	779	791	(1.5)	742	5.0	3,155	2,828	11.6
Less: Inter-segment Revenues	483	327	47.7	479	1.0	1,286	1,112	15.6
<b>Gross Segmental Revenues</b>	<b>21,232</b>	<b>14,944</b>	<b>42.1</b>	<b>19,146</b>	<b>10.9</b>	<b>60,415</b>	<b>57,558</b>	<b>5.0</b>

Source: Company, Angel Research

**Exhibit 3: Segment-wise Unadj. EBIT & EBIT Margins (Standalone)**

Particulars (₹ cr)	4QFY16	3QFY16	% chg (qoq)	4QFY15	% chg (yoy)	FY16	FY15	% chg
Infrastructure	2,757	833	230.9	1,958	40.8	5,037	4,443	13.4
EBIT Margin (%)	17.3	8.5		13.7		11.9	10.9	
Power	49	79	(37.7)	52	(4.7)	231	201	14.9
EBIT Margin (%)	2.6	3.8		3.6		3.6	4.5	
Metallurgical & Material Handling	82	(24)	nmf	61	34.9	42	239	(82.2)
EBIT Margin (%)	9.1	(3.6)		6.6		1.5	7.2	
Heavy Engineering	(10)	(17)	nmf	111	nmf	(75)	336	Nmf
EBIT Margin (%)	(1.0)	(2.1)		11.8		(2.5)	10.2	
Electrical & Automation	179	122	47.2	196	(8.9)	501	504	(0.6)
EBIT Margin (%)	14.5	11.2		14.9		11.8	12.2	
Others	103	136	(24.0)	100	3.4	556	653	(14.9)
EBIT Margin (%)	13.2	17.2		13.4		17.6	23.1	
<b>Segmental EBIT (unadj.)</b>	<b>3,160</b>	<b>1,129</b>	<b>180.0</b>	<b>2,477</b>	<b>27.6</b>	<b>6,293</b>	<b>6,377</b>	<b>(1.3)</b>

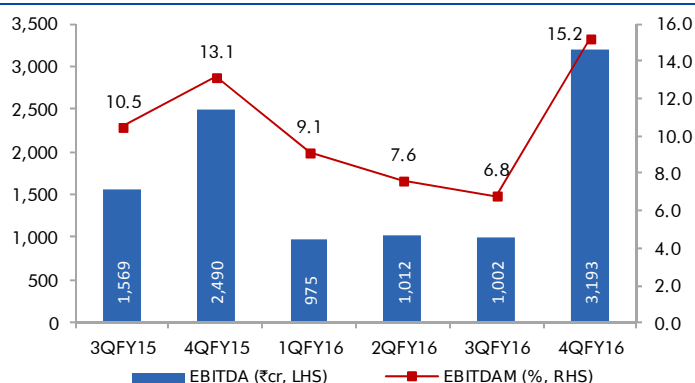
Source: Company, Angel Research; Note- nmf- Not Meaningful

**EBITDA margins expand yoy to 15.2%**

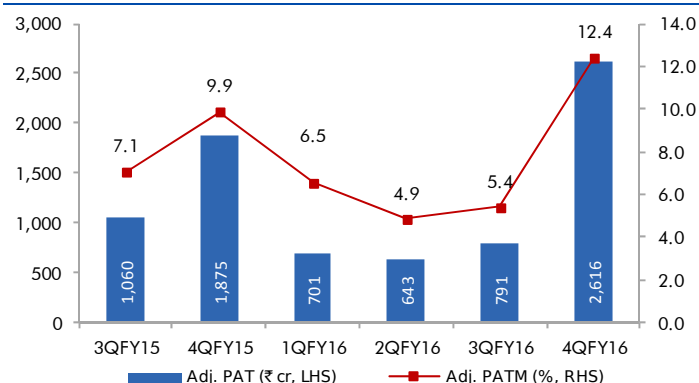
The company reported higher than expected EBITDA for the quarter at ₹3,193cr. With some additional projects attaining the threshold of revenue recognition, L&T reported a 203bp yoy EBITDA margin expansion to 15.2%. This is the first quarter after three successive quarters where L&T has been able to report a yoy increase in its EBITDA margin. Top-line growth coupled with (a) 5.9% yoy decrease in sales, administrative and other (SAO) expenses (to ₹618cr), and (b) just a 1.5% yoy increase in employee expenses (to ₹1,037cr) led to an expansion in the EBITDA margin on a yoy basis.

At the segment level, EBIT margins expanded on a yoy basis across the Infrastructure (up 357bp to 17.3%) and the MMH segment (up 249bp to 9.1%) while the Heavy Engineering segment reported negative margin on account of cost provisions and under recoveries.

For FY2016, higher operating, SAO, and employee expenses led to a 106bps yoy decline in the company's EBITDA margin to 10.3%. Barring the Infrastructure segment, all other segments reported yoy declines in their EBIT margins (Heavy Engineering reported negative margins).

**Exhibit 4: EBITDA margin expands to 15.2%**


Source: Company, Angel Research

**Exhibit 5: Adj. PAT margin expands yoy to 12.4%**


Source: Company, Angel Research

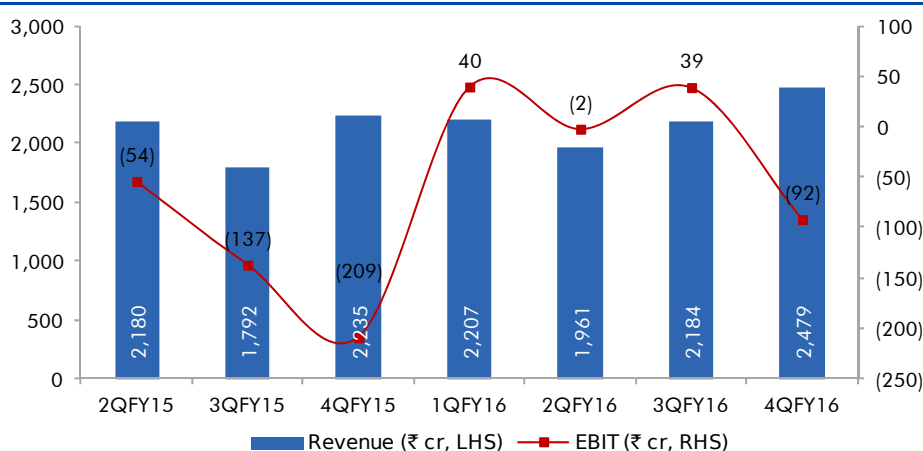
### Adj. PAT numbers report strong yoy growth

L&T reported a PAT of ₹2,539cr for the quarter, ahead of our estimate. On adjusting for gains on divestment of stake in the Foundry business (₹48.5cr) and provision for impairment on the value of investment (₹135cr), the Adjusted PAT stood at ₹2,616cr. The Adj. PAT margin improved from 9.9% a year ago to 12.4% in 4QFY2016. The 39.5% yoy increase in Adj. PAT for the quarter is on account of 28.2% increase in EBITDA, 29.2% increase in other income (to ₹737cr) and a lower tax rate.

For the full year FY2016, in-line with EBITDA margin, the Adj. PAT margin also compressed yoy from 8.2% in FY2015 to 7.9% in FY2016.

### Hydro-Carbon business comes out of Legacy projects

At the backdrop of stronger execution, the Hydro-carbon business reported a 10.9% yoy increase in revenue to ₹2,479cr.

**Exhibit 6: Hydro-carbon - Quarterly Revenues & EBIT**


Source: Company, Angel Research

The Hydro-carbon business reported ₹92cr of EBIT level losses for the quarter (vs ₹209cr loss in the corresponding period a year ago). The reduction in losses is owing to higher provisioning and completion of legacy projects in the Middle East.

For FY2016, the Hydro-carbons segment reported a 20% yoy increase in revenues to ₹8,787cr, reflecting strong execution (47% of the sales were from International subsidiaries).

Whereas, EBIT level loss margins declined from -18.1% in FY2015 to -0.2% in FY2016, owing to close-out costs in international projects and under recovery in fabrication yards.

### **IT & Technology Services business reports strong growth**

L&T's IT & Technology Services business reported an impressive 13.0% yoy increase in revenue for the quarter to ₹2,295cr. The top-line growth was driven by growth across sectors such as BFSI, autos, industrial products, and process engineering. On the operating front, the EBIT margin declined by 64bp yoy to 18.2%.

For FY2016, the segment reported an 18% yoy increase in revenue to ₹8,956cr. Similarly, higher manpower utilization and a weaker rupee helped the IT & Technology Services segment report EBIT margin expansion to 18.6% (in FY2016; vs 17.2% in FY2015).

## Consolidated Business Performance

### Revenue grew 18.3% yoy

L&T reported an 18.3% yoy and 28.4% qoq growth in its consolidated business' top-line to ₹33,157cr. Revenue growth on a yoy basis reflects (1) strong execution across Infrastructure segment (19% yoy revenue growth to ₹18,655cr), (2) projects under execution achieving substantial progress in the Power segment (51% yoy increase in revenue to ₹2,185cr), and (3) 23.4% yoy increase in Others segment (to ₹2,028cr). International revenues (~30% of 4QFY2016 revenues) reported a 23% yoy increase in revenues. Strong execution was seen across the Riyadh (40-45% of civil works completed) and Doha Metro projects (tunneling works completed, civil works related to stations would start soon).

For FY2016, revenues grew 11.6% yoy to ₹102,632cr, reflecting 12.3% and 47.4% increase in Infrastructure & Power segment revenues to ₹50,387cr and ₹7,011cr, respectively.

### Exhibit 7: Quarterly Performance (Consolidated)

Particulars (₹ cr)	4QFY16	3QFY16	% chg (qoq)	4QFY15	% chg (yoy)	FY16	FY15	% chg
<b>Net Sales</b>	<b>33,157</b>	<b>25,829</b>	<b>28.4</b>	<b>28,023</b>	<b>18.3</b>	<b>102,632</b>	<b>92,005</b>	<b>11.6</b>
<b>Total Expenditure</b>	<b>28,298</b>	<b>23,179</b>	<b>22.1</b>	<b>24,427</b>	<b>15.8</b>	<b>90,289</b>	<b>80,747</b>	<b>11.8</b>
Man. Cons. & Opex Exp. (MCO)	24,435	19,049	28.3	20,783	17.6	74,946	67,240	11.5
Employee benefits Expense	2,242	2,411	(7.0)	2,049	9.4	9,205	8,060	14.2
Sales, Admin & Other Expenses	1,620	1,719	(5.7)	1,595	1.6	6,138	5,446	12.7
<b>EBITDA</b>	<b>4,859</b>	<b>2,650</b>	<b>83.4</b>	<b>3,595</b>	<b>35.2</b>	<b>12,343</b>	<b>11,258</b>	<b>9.6</b>
EBIDTA %	14.7	10.3		12.8		12.0	12.2	
Depreciation	820	620	32.3	588	39.5	2,756	2,623	5.1
EBIT	4,039	2,030	98.9	3,007	34.3	9,587	8,635	11.0
Interest and Financial Charges	774	745	3.9	469	65.1	3,041	2,840	7.1
Other Income	218	452	(51.7)	290	(24.6)	1,183	1,075	10.1
PBT before Exceptional Items	3,483	1,737	100.5	2,828	23.2	7,729	6,870	12.5
Exceptional Items	(49)	0		(98)		(358)	(348)	
PBT after Exceptional Items	3,532	1,737	103.3	2,927	20.7	8,087	7,217	12.0
Tax	954	556	71.7	766	24.5	2,549	2,253	13.1
% of PBT	27.0	32.0		26.2		31.5	31.2	
<b>PAT before Minority Int.</b>	<b>2,578</b>	<b>1,182</b>	<b>118.2</b>	<b>2,161</b>	<b>19.3</b>	<b>5,538</b>	<b>4,964</b>	<b>11.6</b>
Extra-Ordinary Items	0	0		0		0	0	
Share in profit of Associates (net)	(2)	(2)		(2)		(3)	2	
Adj. of Minority Interests	(123)	(145)		(90)		(445)	(201)	
<b>PAT after Minority Interest</b>	<b>2,454</b>	<b>1,035</b>	<b>137.1</b>	<b>2,070</b>	<b>18.6</b>	<b>5,091</b>	<b>4,765</b>	<b>6.8</b>
<b>Adj. PAT (for excep. Items)</b>	<b>2,405</b>	<b>1,035</b>	<b>132.4</b>	<b>1,971</b>	<b>22.0</b>	<b>4,732</b>	<b>4,417</b>	<b>7.1</b>
Adj. PAT %	7.3	4.0		7.0		4.6	4.8	
Dil. EPS	26.17	11.07	136.4	22.05	18.7	54.44	50.98	6.8

Source: Company, Angel Research

### **EBITDA margins expand yoy to 14.7%**

The company reported an 182bp yoy expansion in the EBITDA margin for the quarter to 14.7%. The surge in margin was restricted owing to (1) 17.6% yoy increase in Man. Cons. & Opex Exp. (MCO) expenses to ₹24,435cr, and (2) 9.4% yoy increase in Employee expenses to ₹2,242cr. Surge in employee expenses is on account of manpower augmentation, impact of normal revisions witnessed in earlier quarter and higher staff mix from international operations. SAO expenses increased 1.6% yoy owing to higher provisions.

Further, if we look at segment-wise details, then the EBIT margin benefitted from a yoy expansion in segment margins across Infrastructure (322bp) and MMH (253bp) and narrowing of loss margins across Hydrocarbons business (-566bp).

Higher SGA expenses (mainly the provisioning) and staff costs (owing to hiring related to international business) led to marginal decline of 20bp yoy in EBITDA margins to 12.0% in FY2016.

### **Adj. PAT margins expands marginally to 7.3%**

L&T reported a PAT of ₹2,454cr for 4QFY2016. PAT margins of the company were at 7.4%, almost the same as in the previous year. Despite a yoy EBITDA margin expansion, a 24.6% decline in other income (to ₹218cr), 39.5% increase in depreciation expenses (to ₹820cr) and marginally higher tax rates (at 27.0% in 4QFY2016 vs 26.2% in 4QFY2015) led to an 18.6% yoy increase in PAT. On adjusting for exceptional items, the PAT of the company was at ₹2,405cr. The Adj. PAT margin was at 7.3% in 4QFY2016, slightly better than 7.0% in the corresponding quarter a year ago.

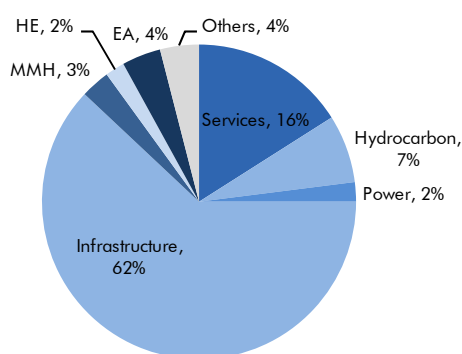
For the full year, effect of marginal decline in EBITDA margin was felt at the Adj. PAT margins level too which stood at 4.6%.

### Order inflow growth disappoints the street...

Consolidated order inflow for the quarter decreased 9.0% yoy to ₹43,334cr (on excluding Services business, order inflow reported 10.7% yoy decrease). A majority of 4QFY2016 order inflows were from Infra (contributed by Building & Factories, Power Transmission & Distribution and Transportation Infra), Hydro-Carbon and Electrical & Automation businesses. A third of the order wins during the quarter are from International markets.

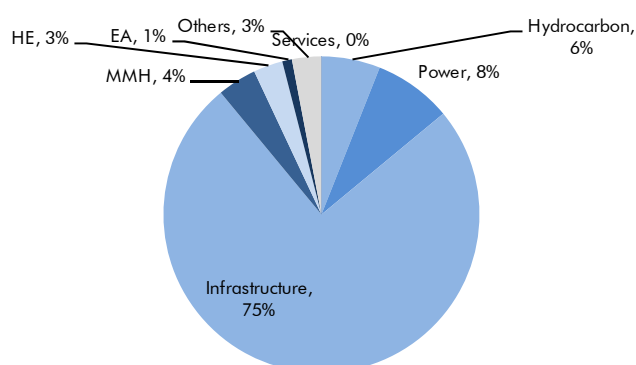
On the whole, order inflows for FY2016 missed the guidance as anticipated. Order Inflows for FY2016 declined 11.9% yoy to ₹136,858cr.

**Exhibit 8: 4QFY16 Order Inflows mix (consol.)**



Source: Company, Angel Research

**Exhibit 9: 4QFY16 Order Book mix (consol.)**



Source: Company, Angel Research

L&T's order book currently stands at ₹2,49,949cr, indicating a 7.4% yoy growth. As of 4QFY2016, L&T's order book is majorly dominated by Infra (75%), followed by Power (8%) and Hydro-carbon (6%) segments. International order book constitutes 28% of the total order book. The current order book gives revenue visibility for over the next 10 quarters.

The Management has given 15% order inflow guidance for FY2017E on the back of strong pipeline of projects coming-up for awarding. Some of the key highlights on the bid pipeline front include, (1) strong pipeline of projects across Roads & Highways (participated in bids worth ₹22,000cr), (2) Power (expect order wins to the tune of ₹10,000cr), (3) large ticket projects nearing the awarding stage in the Defense sector and (4) expect ₹17,000-18,000cr of projects to be awarded from the Dedicated Freight Corridor (DFC).



## Ongoing developments

L&T in order to transform itself into an asset light business is

1. Pursuing IDPL re-structuring; this is at advanced stages. With 13 of the 15 Road BOT projects operational (8 operational for >12 months) and 1 Transmission project operational, there exists a strong case of L&T pursuing Infrastructure Investment Trust (InvITs) route.
2. 1 (Nabha) of the 5 Power plants operational is at advanced stages of being sold.
3. Currently negotiating the sale of its General Insurance business.

All these asset divestment initiatives in our view should be looked upon positively. Given that all these businesses are capital intensive and consume higher capital, L&T's overall capital requirements would subside once the sale happens.

## Valuation

### We upgrade to BUY with target price of ₹1,700

We believe L&T has a better chance to beat its order inflow guidance and also attain its revenue growth guidance for FY2017 (in the range of 12-15%). Further, on considering FY2016 results for Hydro-carbon vertical, we expect improved performance to continue in FY2017. Improved performance from this should lead to consol. margin expansion. On the whole, L&T with its diverse business profile (E&C, Power, Alternate Energy, Roads & Highways, Defense, Metros, Urban Infra) is well positioned to benefit from revival in domestic infra capex cycle.

### Exhibit 10: Derivation of SOTP-based target price for L&T (FY2017E)

Business Segment	Methodology	Remarks	₹ cr	₹/share	% to TP
<b>L&amp;T- Parent</b>	P/E	15.0x FY2018E Earnings	<b>100,276</b>	<b>1,061</b>	<b>62.4</b>
<b>Infrastructure Subsidiaries</b>					
IDPL	P/BV	1.5x FY2017E BV	11,431	121	7.1
<b>Key Subsidiaries - Services</b>					
L&T InfoTech	P/E	15.0x FY2017E Earnings	27,127	287	16.9
L&T Finance	M-cap Basis	20% holding company discount	6,973	74	4.3
<b>Realty Space</b>					
L&T Realty (inc. Seawoods Realty)	P/BV	1.0x FY2017E BV	4,000	43	2.5
<b>Hydro-Carbons Business</b>					
Hydro-Carbons	P/BV	1.5x FY2017E BV	2,100	22	1.3
<b>Key Subsidiaries - Manufacturing</b>					
L&T Power-equipment JVs	P/BV	1.0x FY2017E BV	700	7	0.4
Other Associate Companies	P/BV	1.0x FY2017E BV	5,500	59	3.5
<b>International Business</b>					
International Subsidiaries	P/BV	1.5x FY2017E BV	2,400	26	1.5
<b>Grand Total</b>			<b>160,507</b>	<b>1,700</b>	<b>100</b>
<b>Upside</b>				<b>15.3%</b>	
<b>CMP</b>				<b>1,475</b>	

Source: Company, Angel Research

We have valued the company using sum-of-the-parts (SOTP) methodology to capture the value of all its businesses and investments. Ascribing separate values to its parent business on a P/E basis and investments in subsidiaries (using P/E, P/BV and M-cap basis), we arrive at a FY2017E target price of ₹1,700. At the current market price of ₹1,475, the standalone entity is trading at an implied P/E multiple of 11.7x (FY2018E), which is attractive. We are of the view that L&T is a proxy play for investors wanting to play on the revival in the Indian infrastructure growth story. **Given the 15.3% upside in the stock from the current levels, we upgrade our rating on the stock to BUY.**

## Investment arguments

- **Indian capex recovery is a matter of time:** Regular announcements on the policy front have eased the environment for capex revival. This along with ongoing rate cuts makes us believe that recovery is very much on cards. Considering that the awarding activity revival should further pick-up, we sense full-fledged recovery to be seen from 2HFY2017E onwards. Further we expect improvement in L&T's execution and margin expansion from FY2017E onwards.

Uptick in the domestic order inflow environment should lead to shift in order inflow mix more towards the domestic markets, going forward. On the back of shift in order book towards domestic markets, we expect uptick in execution. Accordingly, we have modeled a 13.7% top-line CAGR over FY2016-2018E.

Given that L&T is currently sitting on an order book which gives revenue visibility for over 10 quarters, this shift in order inflow mix should help the company in faster margin recovery. We expect EBITDA margins to expand from 10.3% in FY2016 to 11.5% in FY2018E.

- **Best stock to play the Indian infrastructure theme:** We are of the view that L&T is very well positioned to benefit from gradual recovery in the domestic capex cycle, given its diverse sectoral exposure, strong balance sheet and better cash flow generating potential in comparison to its peers, which are struggling with higher leverage, and strained cash flows.

## Company background

L&T, the largest Indian infrastructure conglomerate, is present across almost all the infrastructure segments and is at the forefront of the Indian infra growth story. Over the years, the company has diversified across various segments to encash the untapped infra opportunity, not only in India but in other geographies as well, and has an excellent track record of achieving the same. Currently, L&T manufactures and services its business in over 30 countries worldwide.

**Profit & loss statement (Standalone)**

Y/E March (₹ cr)	FY13	FY14	FY15	FY16	FY17E	FY18E
<b>Net Sales</b>	<b>51,611</b>	<b>56,599</b>	<b>57,017</b>	<b>59,780</b>	<b>67,665</b>	<b>77,249</b>
% Chg		9.7	0.7	4.8	13.2	14.2
Total Expenditure	46,138	49,932	50,530	53,609	60,459	68,404
RM & Contracting Expenses	40,205	43,346	44,397	46,629	52,610	59,636
Employee benefits Expense	3,861	4,662	4,151	4,480	5,075	5,794
Sales, Admin. & Other Exp.	2,072	1,923	1,982	2,500	2,774	2,974
<b>EBITDA</b>	<b>5,473</b>	<b>6,667</b>	<b>6,488</b>	<b>6,171</b>	<b>7,206</b>	<b>8,845</b>
% Chg		22	(3)	(5)	17	23
EBIDTA %	10.6	11.8	11.4	10.3	10.7	11.5
Depreciation	728	792	1,008	999	1,035	1,078
EBIT	4,745	5,875	5,480	5,172	6,171	7,767
% Chg		23.8	(6.7)	(5.6)	19.3	25.9
Interest and Financial Chrg.	955	1,076	1,419	1,449	1,508	1,531
Other Income	1,887	1,881	2,283	2,406	2,607	2,798
PBT	5,678	6,679	6,344	6,129	7,270	9,034
Exceptional Item	(176)	(589)	(357)	560	0	0
PBT after Exceptional Item	5,854	7,268	6,701	5,569	7,270	9,034
Tax Expenses	1,541	1,775	1,645	1,378	1,890	2,349
% of PBT	27.1	26.6	25.9	22.5	26.0	26.0
PAT before Extra-Ord. Items	4,313	5,493	5,056	4,191	5,380	6,685
Extra-Ordinary Item	(72)	0	0	0	0	0
<b>Rep. PAT</b>	<b>4,385</b>	<b>5,493</b>	<b>5,056</b>	<b>4,191</b>	<b>5,380</b>	<b>6,685</b>
% Chg		25.3	(8.0)	(17.1)	28.4	24.3
PAT %	8.5	9.7	8.9	7.0	8.0	8.7
Diluted EPS (after Extra-ord. Items)	53	59	54	57	57	71
% Chg		11.6	(8.3)	4.6	1.3	24.3

**Balance Sheet (Standalone)**

Y/E March (₹ cr)	FY13	FY14	FY15	FY16	FY17E	FY18E
<b>Sources of Funds</b>						
Equity Capital	123	185	186	186	186	186
Reserves Total	29,020	33,476	36,899	40,532	44,162	49,067
<b>Networth</b>	<b>29,143</b>	<b>33,662</b>	<b>37,085</b>	<b>40,718</b>	<b>44,348</b>	<b>49,253</b>
Total Debt	8,834	11,459	12,937	13,608	13,700	12,500
Other Long-term Liabilities	788	393	470	523	569	611
Deferred Tax Liability	242	410	363	203	203	203
<b>Total Liabilities</b>	<b>39,007</b>	<b>45,924</b>	<b>50,854</b>	<b>55,053</b>	<b>58,820</b>	<b>62,567</b>
<b>Application of Funds</b>						
Gross Block	11,855	11,397	12,604	13,461	14,511	15,631
Accumulated Depreciation	3,550	3,836	4,844	5,843	6,878	7,956
<b>Net Block</b>	<b>8,305</b>	<b>7,561</b>	<b>7,760</b>	<b>7,619</b>	<b>7,634</b>	<b>7,676</b>
Capital WIP	597	676	222	50	60	65
<b>Investments</b>	<b>16,103</b>	<b>19,215</b>	<b>23,053</b>	<b>24,569</b>	<b>25,359</b>	<b>27,439</b>
Current Assets	47,419	50,853	55,869	64,832	65,628	68,941
Inventories	2,064	1,983	2,208	1,888	2,275	2,355
Sundry Debtors	22,613	21,539	23,051	26,309	25,000	25,500
Cash and Bank Balance	1,456	1,783	1,516	1,681	1,797	2,349
Loans & Advances	9,413	10,067	10,533	13,237	14,279	15,450
Other Current Asset	11,873	15,481	18,562	21,717	22,277	23,287
Current Liabilities	33,417	32,381	36,050	42,017	39,860	41,553
<b>Net Current Assets</b>	<b>14,002</b>	<b>18,472</b>	<b>19,820</b>	<b>22,815</b>	<b>25,768</b>	<b>27,388</b>
<b>Total Assets</b>	<b>39,007</b>	<b>45,924</b>	<b>50,854</b>	<b>55,053</b>	<b>58,820</b>	<b>62,567</b>

**Cash Flow Statement (Standalone)**

Y/E March (₹ cr)	FY13	FY14	FY15	FY16	FY17E	FY18E
Profit before tax	5,678	6,679	6,344	6,129	7,270	9,034
Depreciation	728	792	1,008	999	1,035	1,078
Change in Working Capital	(3,703)	(5,029)	(1,579)	(3,730)	(3,748)	(1,986)
Net Interest & Financial Charges	422	581	909	929	973	996
Direct taxes paid	(1,653)	(1,977)	(1,645)	(1,378)	(1,890)	(2,349)
<b>Cash Flow from Operations</b>	<b>1,472</b>	<b>1,047</b>	<b>5,037</b>	<b>2,949</b>	<b>3,640</b>	<b>6,773</b>
(Inc)/ Dec in Fixed Assets	(1,000)	(962)	(1,655)	(1,030)	(1,040)	(1,115)
(Inc)/ Dec in Investments	1,657	(252)	(2,345)	508	528	(780)
<b>Cash Flow from Investing</b>	<b>657</b>	<b>(1,214)</b>	<b>(3,999)</b>	<b>(521)</b>	<b>(512)</b>	<b>(1,895)</b>
Issue/ (Buy Back) of Equity	163	144	0	0	0	0
Inc./ (Dec.) in Loans	(1,515)	2,612	1,478	672	92	(1,200)
Dividend Paid (Incl. Tax)	(1,115)	(1,227)	(1,375)	(1,485)	(1,595)	(1,595)
Interest Expenses	(850)	(1,025)	(1,419)	(1,449)	(1,508)	(1,531)
<b>Cash Flow from Financing</b>	<b>(3,316)</b>	<b>504</b>	<b>(1,316)</b>	<b>(2,262)</b>	<b>(3,012)</b>	<b>(4,326)</b>
Inc./ (Dec.) in Cash (inc. of Disc. Operat.)	(410)	337	(278)	165	116	552
<b>Opening Cash balances</b>	<b>1,906</b>	<b>1,496</b>	<b>1,794</b>	<b>1,516</b>	<b>1,681</b>	<b>1,797</b>
<b>Closing Cash balances</b>	<b>1,496</b>	<b>1,794</b>	<b>1,516</b>	<b>1,681</b>	<b>1,797</b>	<b>2,349</b>

**Key Ratios (Standalone)**

Y/E March	FY13	FY14	FY15	FY16	FY17E	FY18E
<b>Valuation Ratio (x)</b>						
P/E (on FDEPS)	27.9	25.0	27.3	26.1	25.7	20.7
P/CEPS	24.6	21.8	22.8	21.9	21.6	17.8
Dividend yield (%)	0.8	0.8	0.9	1.0	1.1	1.1
EV/Sales	2.5	2.6	2.6	2.5	2.2	1.9
EV/EBITDA	23.8	21.9	22.9	24.1	20.7	16.6
EV / Total Assets	3.3	3.2	2.9	2.7	2.5	2.4
<b>Per Share Data (₹)</b>						
EPS (fully diluted)	52.9	59.0	54.1	56.6	57.3	71.2
Cash EPS	59.9	67.5	64.6	67.2	68.3	82.7
DPS	12.0	12.3	13.3	14.4	15.4	15.4
Book Value	464	493	542	586	626	666
<b>Returns (%)</b>						
RoCE (Pre-tax)	17.5	18.7	16.3	14.5	15.6	17.6
Angel RoIC (Pre-tax)	17.5	17.2	15.5	13.9	15.1	17.1
RoE	14.2	15.6	13.3	15.1	12.6	14.3
<b>Turnover ratios (x)</b>						
Asset Turnover (Gross Block) (X)	4.4	4.9	4.8	4.6	4.8	5.1
Inventory / Sales (days)	15	13	13	13	11	11
Receivables (days)	160	142	143	151	138	119
Payables (days)	134	122	127	139	129	111
<b>Leverage Ratios (x)</b>						
D/E ratio (x)	0.3	0.3	0.3	0.3	0.3	0.3
Interest Coverage Ratio (x)	6.9	7.2	5.5	5.2	5.8	6.9

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### Disclosure of Interest Statement

	L&T
1. Analyst ownership of the stock	No
2. Angel and its Group companies ownership of the stock	No
3. Angel and its Group companies' Directors ownership of the stock	No
4. Broking relationship with company covered	No

*Note: We have not considered any Exposure below ₹1 lakh for Angel, its Group companies and Directors*

**Ratings (Based on expected returns over 12 months investment period):**

Buy (> 15%)

Accumulate (5% to 15%)  
Reduce (-5% to -15%)

Neutral (-5 to 5%)  
Sell (< -15)