

VA Tech Wabag

Performance Highlights

Quarterly highlights - Standalone

Y/E March (₹ cr)	3QFY16	3QFY15	2QFY16	% chg (yoy)	% chg (qoq)
Net sales	371	293	325	26.6	14.4
EBITDA	37	33	34	11.7	6.4
Reported PAT	21	18	24	17.0	(13.4)

Source: Company, Angel Research;

VaTech Wabag (Wabag) reported a 26.6% yoy increase in sales to ₹371cr in 3QFY2016, reflecting strong execution across its AP Genco project. The EBITDA for the quarter grew 11.7% yoy to ₹37cr. The EBITDA margin declined 132bp yoy to 9.9%, owing to a sharp increase in other expenses to ₹22cr (vs ₹5cr in 3QFY2015). In-line with the EBITDA margin, the PAT margin declined from 6.0% in the corresponding quarter of the previous year to 5.6% in 3QFY2016.

International revenues declined 20.8% yoy to ₹258cr, on account of (1) Euro depreciation, (2) some of the projects being at early stages of execution and not contributing to revenues (inclusive of Nepal based projects), and (3) lower revenue from Al Gubrah project (nearing completion). A poor operating performance coupled with higher interest expenses (at ₹5.5cr) led to international business losses.

The order book as of 3QFY2016-end stood at ₹7,952cr, reflecting Order book / last twelve month (LTM) sales ratio of 3.1x.

Valuation: The stock trades at FY2017E/2018E P/E multiple of 26.1x/20.7x, which continues to be at the higher end of the historical band. On considering the 25% correction in the stock price in the last 3 months period, valuations in our view still do not factor in the muted order inflow environment, modest earnings growth, and stretched working capital cycle. We assign a 20.0x P/E multiple to our FY2017E EPS of ₹25 to arrive at a price target of ₹492. Given the limited upside potential, **we recommend a Neutral rating on the stock.**

Key financials (Standalone)

Y/E March (₹ cr)	FY13	FY14	FY15	FY16E	FY17E
Net Sales	1,619	2,239	2,435	2,722	3,336
% chg	12.1	38.3	8.8	11.8	22.5
Net Profit	90	114	112	107	135
% chg	22.5	25.5	(2.9)	(3.8)	26.2
EBITDA (%)	9.6	8.4	8.6	7.9	8.1
EPS (₹)	34	42	20	20	25
P/E (x)	15.1	12.1	25.2	26.1	20.7
P/BV (x)	1.9	1.6	3.1	2.7	2.4
RoE (%)	12.6	14.6	12.6	11.1	12.4
RoCE (%)	20.1	20.6	22.0	19.5	21.3
EV/Sales (x)	0.7	0.5	1.1	0.9	0.8
EV/EBITDA (x)	7.4	6.1	12.6	11.8	9.3

Source: Company, Angel Research; CMP as of March 18, 2016

NEUTRAL

CMP	₹509
Target Price	-

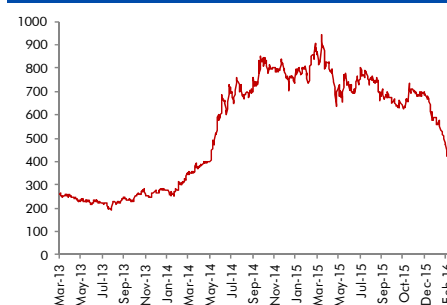
Investment Period	-
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Stock Info	
Sector	Capital Goods
Market Cap (₹ cr)	2,771
Net debt (₹ cr)	(131)
Beta	1.1
52 Week High / Low	957/409
Avg. Daily Volume	141,944
Face Value (₹)	2
BSE Sensex	24,953
Nifty	7,604
Reuters Code	VATE.BO
Bloomberg Code	VATW@IN

Shareholding Pattern (%)	
Promoters	29.0
MF / Banks / Indian Fls	25.0
FII / NRIs / OCBs	27.4
Indian Public / Others	18.7

Abs. (%)	3m	1yr	3yr
Sensex	(3.0)	(44.2)	145.0
Wabag	(25.8)	(12.4)	34.3

3-Year Daily Price Chart



Source: Company, Angel Research

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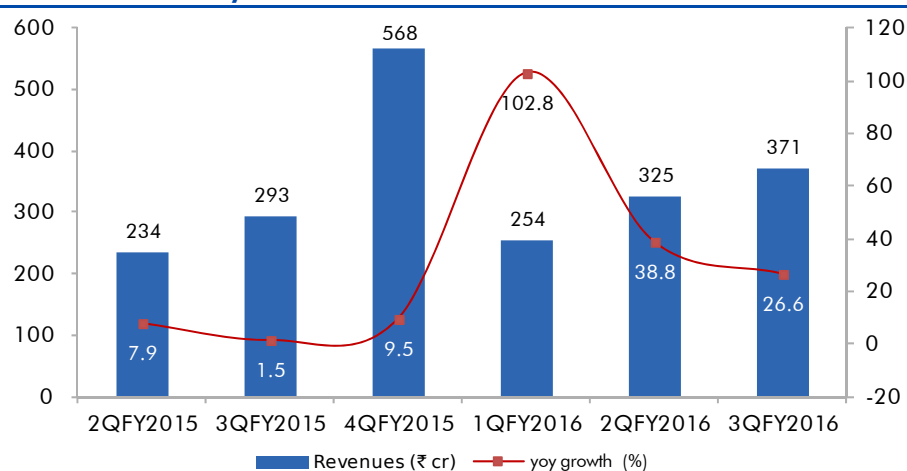
Exhibit 1: Quarterly Performance (Standalone)

Particulars (₹ cr)	3QFY16	2QFY16	% chg (qoq)	3QFY15	% chg (yoy)	9mFY16	9mFY15	% chg
Net Sales	371	325	14.4	293	26.6	950	652	45.6
Total Expenditure	335	290	15.4	261	28.4	852	591	44.1
Cost of materials consumed	311	251	23.7	234	32.7	766	536	42.9
Change in Inventories	(22)	11	(298.7)	4	(722.3)	(38)	(46)	(16.2)
Employee benefits Expense	23	21	9.9	18	29.1	70	61	14.9
Other Expenses	22	7	231.3	5	368.3	54	40	35.9
EBITDA	37	34	6.4	33	11.7	98	61	59.7
<i>EBIDTA %</i>	9.9	10.6		11.2		10.3	9.4	
Depreciation	3	3	(3.3)	3	(9.5)	9	4	119.3
EBIT	34	31	7.4	30	14.0	89	57	55.4
Interest and Financial Charges	5	3	38.1	2	<i>nmf</i>	9	5	71.6
Other Income & forex (gain)/loss	2	8	(80.0)	(1)	(327.0)	13	6	113.3
PBT before Exceptional Items	31	36	(15.6)	27	15.6	93	58	60.0
Exceptional Items	0	0	<i>nmf</i>	0	<i>nmf</i>	0	0	<i>nmf</i>
PBT after Exceptional Items	31	36	(15.6)	27	15.6	93	58	60.0
Tax	10	13	(20.0)	9	12.9	31	19	61.7
<i>% of PBT</i>	32.7	34.5	(5.1)	33.5	(2.4)	33.9	33.5	1.1
Net Profit/ (Loss) after taxes	21	24	(13.4)	18	17.0	61	38	59.1
<i>PAT %</i>	5.6	7.4	(24.3)	6.0	(7.5)	6.4	5.9	9.3
Dil. EPS (after extra-ord. Items)	3.79	4.38	(13.5)	3.26	16.3	11.23	7.10	58.2

Source: Company, Angel Research; Note: *nmf*- Not meaningful

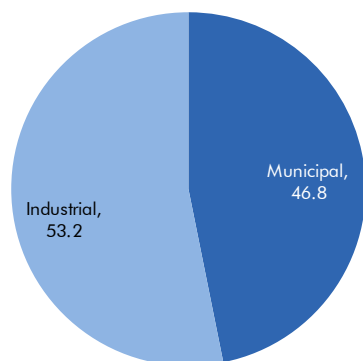
Revenues grow 26.6% yoy

VaTech Wabag reported a 26.6% yoy increase in sales to ₹371cr in 3QFY2016. Revenue growth was mainly on account of strong execution seen across the AP Genco project (has contributed ₹280cr to the top-line for 9MFY2016).

Exhibit 2: Quarterly revenue trend


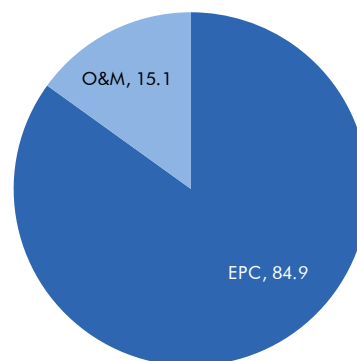
Source: Company, Angel Research

Exhibit 3: Business-wise 9MFY2016 Revenue split



Source: Company, Angel Research

Exhibit 4: Vertical-wise 9MFY2016 Revenue split

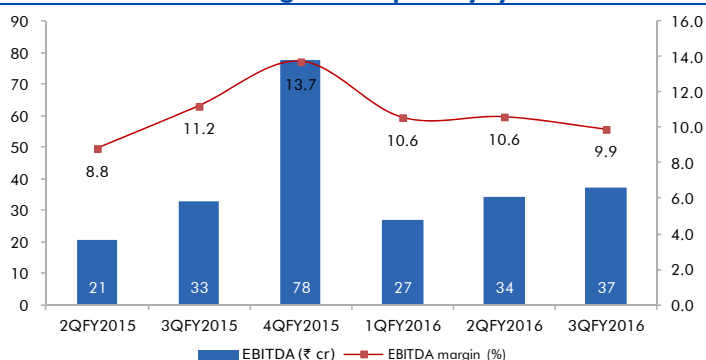


Source: Company, Angel Research

EBITDA margin declines yoy

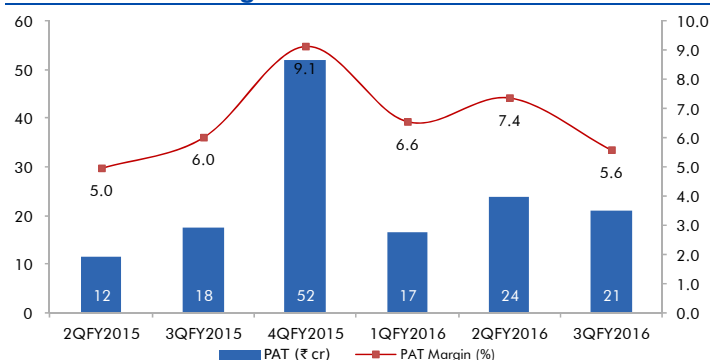
Wabag reported an 11.7% yoy increase in EBITDA to ₹37cr while the EBITDA margin declined 132bp yoy to 9.9%, in 3QFY2016. The compression in the EBITDA margin is owing to a sharp increase in other expenses to ₹22cr (vs ₹5cr in 3QFY2015). Such increase in other expenses is attributable to higher doubtful debts provisioning of ₹12cr, which is in-line with the company's internal policy of ageing debtors.

Exhibit 5: EBITDA margins compress yoy



Source: Company, Angel Research

Exhibit 6: PAT margins also decline...



Source: Company, Angel Research

PAT margin down yoy

In-line with the EBITDA margin, the PAT margin declined from 6.0% in 3QFY2015 to 5.6% in 3QFY2016. This is in spite of a 9.5% decline in yoy depreciation expenses (to ₹3cr) and a lower tax rate (at 32.7%).

Update on subsidiaries' performance

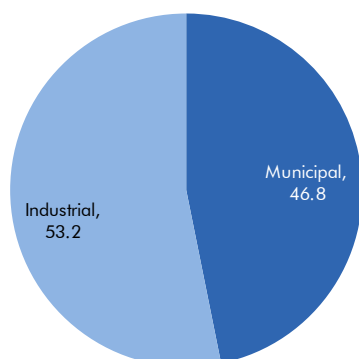
The company's International subsidiaries' revenues declined 20.8% on a yoy basis to ₹258cr which is attributable to (1) Euro depreciation (over 10%), and (2) some of the projects being at early stages of execution and not contributing to revenues (inclusive of Nepal based projects), and (3) lower revenue booking from Al Gubrah project (is nearing completion).

A poor operating performance coupled with higher interest expenses (at ₹5.5cr) led to international business losses. Surge in yoy interest expenses is on account of Ujams BOOT project, Namibia.

₹276cr of Order Inflows in 3QFY2016

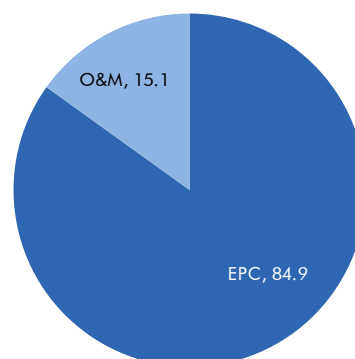
Wabag reported ₹276cr of order wins in 3QFY2016, which is down 59% yoy. Wabag reported a key order win from Sanliurfa WWTP, Turkey. The Management attributed client side delays on project finalization in domestic markets as the key reason for decline in yoy order inflows. For 9MFY2016 Wabag reported ~130% yoy increase in order inflows to ₹3,356cr.

Exhibit 7: Business-wise 9MFY2016 Order Inflows split



Source: Company, Angel Research

Exhibit 8: Vertical-wise 9MFY2016 Order Inflows split



Source: Company, Angel Research

Order book as of 3QFY2016-end stood at ₹7,952cr, reflecting Order book / last twelve month (LTM) sales ratio of 3.1x.

Management Guidance & Concall Updates

For FY2016, the company's Management maintained its order inflow guidance of ₹3,500-3,700cr (up 18-24% yoy). Considering Wabag having won ₹680cr of Polghawella Water Supply scheme in Sri Lanka in 4QFY2016, and with ₹3,356cr of order inflows for 9MFY2016, we believe that the company has a fair chance to attain its order inflow guidance for FY2016.

Wabag's Management has given a revenue guidance of ₹2,800-3,000cr (up 15-24%) for FY2016.

The Management highlighted that it expects to maintain FY2016 EBITDA margins on the lines of ~8.7%, as reported in FY2015. This in our view is a challenging task, given that Wabag will have to report 12.6% margin in 4QFY2016 vs 5.9% reported in 9MFY2016.

Investment arguments

Strong market positioning: Wabag in our view has a strong portfolio of offerings in the water treatment/ waste water/ desalination space. Unlike most of the domestic EPC players, Wabag has a differentiated business model, given its in-house technology. Strong technological know-how, coupled with large talent positions it to successfully execute complex water projects.

Asset-light business model drives RoEs: Wabag pursues an asset-light business model. Its strategy of keeping core areas of work in-house and outsourcing the non-critical, low-value work helps it maintain high RoEs. Also, it takes on large volume projects, thereby enabling it to generate high RoEs.

India & Emerging markets hold huge opportunity: India has low per capita water supply vis-a-vis developed nations, indicating huge growth potential for the company's business. Also, with rising stringency in norms for waste water treatment, scope for Wabag is huge, given that ~30% of industrial waste water is not treated. Wabag has made strong in-roads in emerging markets like Philippines, China, Saudi Arabia, Egypt, Spain and Turkey.

Risks & Concerns

- Delays in revival of international business could impact our margin assumptions.
- Any significant loss of market share could be a risk to our assumptions.
- Execution delays in the domestic markets could be a risk to our assumptions.

Valuation

The stock trades at FY2017E/2018E P/E multiple of 26.1x/20.7x, which continues to be at the higher end of the historical band. On considering the 25% correction in the stock price in the last 3 months period, valuations in our view still do not factor in the muted order inflow environment, modest earnings growth, and stretched working capital cycle. We assign a 20.0x P/E multiple to our FY2017E EPS of ₹25 to arrive at a price target of ₹492. **Given the limited upside potential, we recommend Neutral rating on the stock.**

Company background

VA Tech Wabag is a multinational player in the water treatment industry with presence across India, Middle East, North Africa, Central and Eastern Europe, China and South East Asia. Wabag offers an entire range of solutions including conceptualisation, design, engineering, procurement, supply, installation, construction and O&M (operational and maintenance) services. The company also provides range of EPC and O&M solutions for sewage treatment, processed & drinking water treatment, effluents treatment, sludge treatment, desalination and reuse for institutional clients like municipal corporations and companies in the infrastructure sector.

Profit and Loss Statement (Standalone)

Y/E March (₹ cr)	FY13	FY14	FY15	FY16E	FY17E
Net Sales	1,619	2,239	2,435	2,722	3,336
% Chg	12.1	38.3	8.8	11.8	22.5
Total Expenditure	1,464	2,050	2,226	2,506	3,066
Cost of sales & services	1,165	1,689	1,848	2,067	2,550
Changes in inventory	10	9	(15)	11	8
Employee benefits Expense	209	222	278	304	366
Other Expenses	80	130	115	123	142
EBITDA	155	189	209	216	270
% Chg	19.1	21.7	11.1	3.3	24.6
EBIDTA %	9.6	8.4	8.6	7.9	8.1
Depreciation	11	15	11	20	26
EBIT	144	173	199	197	243
% Chg	18.5	20.5	14.4	(1.0)	23.8
Interest and Financial Charges	22	25	39	45	50
Other Income	13	13	8	7	7
EBT & exceptional items	135	161	167	159	200
Exceptional Items	0	5	0	0	0
EBT	135	166	167	159	200
Tax Expenses	46	53	57	53	67
% of PBT	33.7	32.6	33.9	33.3	33.3
EAT before share of Profit in asso.	90	114	110	106	134
Share of profit in Associate	1	1	2	2	2
PAT before Minority Interest	90	114	112	107	135
Minority Interest	0	1	2	2	2
PAT	90	113	110	106	134
% Chg	22.5	25.5	(2.9)	(3.8)	26.2
PAT %	5.6	5.1	4.5	3.9	4.0
Diluted EPS	33.8	42.1	20.2	19.5	24.6
% Chg	21.2	24.8	(52.1)	(3.5)	26.2

Balance Sheet (Standalone)

Y/E March (₹ cr)	FY13	FY14	FY15	FY16E	FY17E
Sources of Funds					
Equity Capital	5	5	11	11	11
Reserves & Surplus	710	836	892	998	1,131
Networth	715	841	903	1,009	1,142
Total Debt	82	158	181	207	227
Minority Interest & Share appl. pending allot.	2	3	5	6	8
Other Long-term Liabilities & Prov.	112	182	242	255	275
Total Liabilities	912	1,185	1,331	1,477	1,652
Application of Funds					
Gross Block	107	175	252	277	302
Accumulated Depreciation	56	56	61	81	107
Net Block	51	119	191	197	195
Capital WIP & Intan. Assets under Develop.	48	69	1	0	0
Investments	3	23	38	38	38
Current Assets					
Inventories	41	35	47	60	73
Sundry Debtors	1,109	1,387	1,481	1,700	2,102
Cash and Bank Balance	287	370	311	414	469
Loans & Advances	116	100	116	125	129
Other Current Asset	225	320	361	370	375
Current Liabilities	979	1,251	1,237	1,454	1,764
Net Current Assets	798	962	1,078	1,215	1,384
Other Assets	11	11	23	28	35
Total Assets	912	1,185	1,331	1,477	1,652

Cash Flow Statement

Y/E March (₹ cr)	FY13	FY14	FY15	FY16E	FY17E
Profit before tax	135	161	167	159	200
Depreciation & Other Non-cash Charges	89	85	135	80	72
Change in Working Capital	(115)	(84)	(257)	(34)	(114)
Interest & Financial Charges	7	7	15	16	17
Direct taxes paid	(34)	(57)	(55)	(53)	(67)
Cash Flow from Operations	82	112	6	168	109
(Inc)/ Dec in Fixed Assets	(41)	(103)	(28)	(24)	(25)
(Inc)/ Dec in Investments & Oth. Adj.	1	5	(39)	0	0
Cash Flow from Investing	(40)	(97)	(68)	(24)	(25)
Issue/ (Buy Back) of Equity	3	1	20	0	0
Inc./ (Dec.) in Borrowings	(43)	76	22	27	20
Dividend Paid (Incl. Tax)	(19)	(22)	(25)	(25)	(31)
Interest Expenses & Oth. Adj.	(7)	(8)	(15)	(16)	(17)
Cash Flow from Financing	(65)	48	2	(14)	(29)
Inc./ (Dec.) in Cash & forex translation	(21)	86	(91)	130	55
Opening Cash balances	265	244	330	240	369
Closing Cash balances	244	330	240	369	424

Ratio Analysis (x)

Y/E March	FY13	FY14	FY15	FY16E	FY17E
Valuation Ratio (x)					
Adj. P/E (on FDEPS)	15.1	12.1	25.2	26.1	20.7
Adj. P/CEPS	13.3	10.5	22.8	22.0	17.2
Dividend yield (%)	1.2	1.4	0.8	0.8	1.0
EV/Sales	0.7	0.5	1.1	0.9	0.8
EV/EBITDA	7.4	6.1	12.6	11.8	9.3
EV / Total Assets	1.3	1.0	2.0	1.7	1.5
Per Share Data (₹)					
Adj. EPS (fully diluted)	33.8	42.1	20.2	19.5	24.6
Cash EPS	38.1	48.3	22.3	23.1	29.5
DPS	6.0	7.0	4.0	3.9	4.9
Book Value	269	316	166	186	210
Returns (%)					
RoCE (Pre-tax)	20.1	20.6	22.0	19.5	21.3
Angel RoIC (Pre-tax)	14.1	13.3	12.0	10.3	11.7
RoE	12.6	14.6	12.6	11.1	12.4
Turnover ratios (x)					
Asset Turnover (Gross Block) (x)	0.6	0.5	0.5	0.5	0.5
Inventory / Sales (days)	9	6	7	8	8
Receivables (days)	250	226	222	228	230
Payables (days)	221	204	185	195	193
WC (days)	39	28	44	41	45
Leverage Ratios (x)					
D/E ratio (x)	0.1	0.2	0.2	0.2	0.2

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Disclosure of Interest Statement

VA Tech Wabag

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%)