MOTILAL OSWAL

15 February 2012

3QFY12 Results Update | Sector: Real Estate

Unitech

BSE SENSEX	S&P CNX
17,849	5,416

Bloomberg	UT IN
Equity Shares (m)	2,438.8
52-Week Range (INR)	49/17
1,6,12 Rel. Perf. (%)	11/-4/-16
M.Cap. (INR b)	73.2
M.Cap. (USD b)	1.5

CMP: INR30 **TP: INR42** **Buy**

Year End	Net Sales (INR m)	PAT (INR m)	EPS (INR)	EPS Gr. (%)	P/E (X)	P/BV (X)	RoE (%)	RoCE (%)	EV/ Sales (X)	EV/ EBITDA (X)
3/10A	29,313	6,751	2.8	-53.6	-	-	6.5	6.4	-	-
3/11A	31,871	5,677	2.2	-21.6	13.8	0.8	4.9	5.2	4.2	14.3
3/12E	23,646	3,351	1.3	-41.0	23.2	0.8	2.8	3.3	5.4	25.6
3/13E	29,290	4,348	1.7	29.7	17.9	0.7	3.5	3.9	4.2	17.7

- Unitech (UT) posted lower than estimated numbers for 3QFY12. EBITDA declined ~49% YoY to INR1.1b (v/s our estimate of INR1.6b). EBITDA margin was 21% v/s 32% in 3QFY11. Revenue was down ~22% YoY at INR5.1b (v/s our estimate of INR7b) while PAT declined ~50% YoY to INR552m.
- The Real Estate vertical contributed ~80% (INR4.1b) of the revenue. Real Estate revenue booking run-rate (INR4b-5b/quarter) has been disappointing over FY12, given that the average sales run-rate has been INR9b-10b/quarter over the last 8 quarters. The key reason behind this gap has been lower than targeted construction expenditure due to commitment towards debt servicing.
- EBITDA margin was impacted due to (1) additional MTM loss provisioning of ~INR330m towards dollar-linked foreign investment, and (2) margin contraction in real estate projects due to contribution from lower margin projects in Noida and cost escalation. EBIT margin in the Real Estate vertical was 27% v/s 30% in 2QFY12 and 45% in 3QFY11.
- Consolidated gross debt increased marginally to INR54.7b, while net debt stood at INR51.9b, implying net debt-equity of 0.43x. Increase in debt is due to currency impact on foreign loans.
- The stock trades at ~46% discount to our NAV estimate of INR56/share, and at 17.9x FY13E EPS of INR1.7 and 0.7x FY13E BV. Maintain **Buy**.

Quarterly Performance (INR Million)

	FY11				FY12				FY11	FY12E
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4QE		
Sales	**8,286**	**6,445**	**6,598**	**10,542**	**5,959**	**6,261**	**5,139**	**6,288**	**31,871**	**23,646**
Change (%)	60.9	26.5	-14.8	-6.9	-28.1	-2.9	-22.1	-40.4	8.7	-25.8
Total Expenditure	5,348	3,917	4,510	8,857	4,761	4,880	4,066	4,932	22,632	16,529
EBITDA	**2,938**	**2,528**	**2,088**	**1,685**	**1,198**	**1,381**	**1,073**	**1,356**	**9,239**	**5,008**
Change (%)	-6.8	-15.1	12.4	-38.2	-59.2	-45.4	-48.6	-19.5	-13.8	-45.8
As of % Sales	35.5	39.2	31.6	16.0	20.1	22.1	20.9	21.6	29.0	21.2
Depreciation	88	89	75	67	84	85	93	96	319	357
Interest	340	439	340	335	337	338	271	286	1,455	1,232
Other Income	150	304	181	415	714	403	334	334	1,050	1,785
PBT	**2,660**	**2,305**	**1,853**	**1,698**	**1,490**	**1,362**	**1,043**	**1,308**	**8,516**	**5,204**
Tax	834	564	740	566	468	424	468	357	2,704	1,717
Effective Tax Rate (%)	31.4	24.5	39.9	33.3	31.4	31.1	44.9	27.3	31.8	33.0
Adj PAT	**1,800**	**1,738**	**1,113**	**1,057**	**984**	**924**	**552**	**891**	**5,677**	**3,351**
Change (%)	52.8	-2.2	-36.7	-47.4	-45.4	-46.8	-50.4	-15.7	-15.9	-41.0

E: MOSL Estimates

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MTM loss provisioning continues to impact margins

UT witnessed a sharp decline in EBITDA margin from 32% in 3QFY11 to 22% in 3QFY12, led by:

- Cost escalation in ongoing projects
- Higher contribution from low margin Noida project, which started contributing to revenue from 4QFY11
- ~INR330m loss provisioning for dollar-linked foreign investment - UT invested ~INR2.3b in a derivative product called Yield Enhancement Certificate in FY10, and has already provisioned ~INR2b of MTM loss in 4QFY11-1QFY12, implying ~INR0.3b investment value as at 3QFY12, to be provisioned in forthcoming quarters. EBITDA margin adjusted for provisions stood at ~27%.

Understanding the actual impact on operating margin

Revenue (INR b)	5.1
EBITDA (INR b)	1.1
Margin (%)	**20.9**
Loss provision in Foreign investment (INR b)	0.3
EBITDA ex. loss provision (INR b)	1.4
Adjusted margin (%)	**27.3**

Source: Company/MOSL

Sales steady; average realization across locations declines

- The company sold 2msf (INR9.4b) in 3QFY12 v/s 1.8msf (INR10.7b) in 1QFY12. Total sales over 9MFY12 were IN30.3b v/s our estimate of ~INR40b. Residential projects accounted for 71% of sales, while Gurgaon projects accounted for 51% of sales. During the quarter, Noida projects witnessed an uptick in sales, with 0.4msf (INR2.3b) sold in 3Q v/s 0.1msf (INR1b) in 2Q.
- Average realization declined 10-33% QoQ across cities and by an average 19% QoQ. The management has attributed this to change in product mix; there has been no price reduction in ongoing projects.
- In 3QFY12, UT delivered 0.7msf of projects, taking total delivery over 9MFY12 to 2.9msf v/s 4.3msf in FY11. Total area under construction stood at 46msf, of which ~20msf (18.9msf in 2Q) is in delivery/finishing stage and structure work has been completed for another 9.4msf (8.8msf in 2Q).

Liquidity constraints haunt execution and revenue booking

- **Widening gap between sales and revenue recognition run-rate:** The Real Estate vertical has contributed almost 80% (INR4.1b) of the 3QFY12 revenue. Real Estate revenue booking run-rate (INR4b-5b/quarter) has been disappointing over FY12, given that the average sales run-rate over the last 8 quarters has been INR9b-10b/quarter.
- **Debt servicing requirements impacting planned construction expenditure:** The key reason for the increasing gap is lower than targeted construction expenditure due to commitment towards debt servicing. UT has scheduled repayments of ~INR10b during FY12, of which it has paid only INR3.8b over 9MFY12. It plans to re-finance the rest. However, the prevailing tight liquidity scenario and banks' apathy towards the realty sector have been delaying the re-financing process, leading to uncertainty over cash flow management in the backdrop of subdued demand for

real estate. At the beginning of FY12, UT had planned to increase its construction expenditure to INR4b-4.5b/quarter from INR3b/quarter (only INR2.5b in 3QFY12). However, higher commitment towards debt servicing has impacted the construction ramp-up plan. The company utilized ~INR10b of its INR20b-22b of operational cash flow towards debt repayment and interest expense over 9MFY12.

- **Cash flow snapshot for 3QFY12:** UT collected ~INR6.7b (v/s INR7b/8b in 1Q/2QFY12) from sales of ongoing projects, including rental income (~INR350/quarter). It utilized ~INR2.5b towards construction, ~INR0.8b for net debt reduction, ~INR1.6b for interest payment, and the rest for tax and operating expense.
- **Leverage up due to currency movement:** Consolidated gross debt increased marginally to INR54.7b, while net debt stood at INR51.9b, implying net debt-equity of 0.43x. The marginal increase in debt is due to currency impact on foreign loans.

Gross debt increased marginally QoQ

Debt repayment (INR b)	**2.8**
Fresh loan availed (INR b)	1.5
Loan at UCP (UT's stake) (INR b)	0.5
Net debt reduction (INR b)	**0.8**
Currency impact on foreign loan (INR b)	0.9
Net increase in debt (INR b)	**0.1**

Source: Company/MOSL

Cutting earnings estimates on slower construction outlook

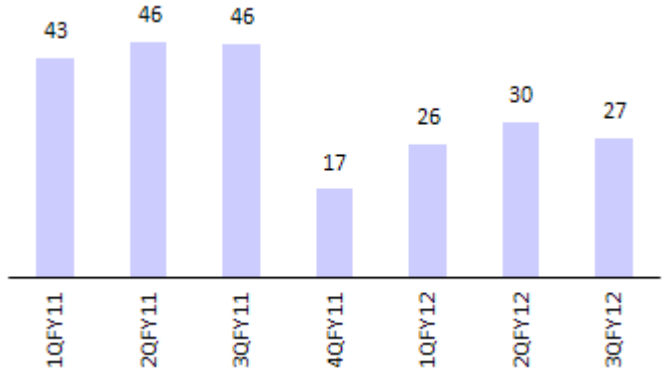
While the management has indicated that managing cash flow and execution ramp-up are the key areas of focus, we expect delays in re-financing to impact construction pace and revenue booking in FY12/1HFY13. We are downgrading our revenue estimates by 16% each and our PAT estimates by 27% and 20% for FY12 and FY13.

Valuation and view: Ability to manage liquidity, execution ramp-up the key

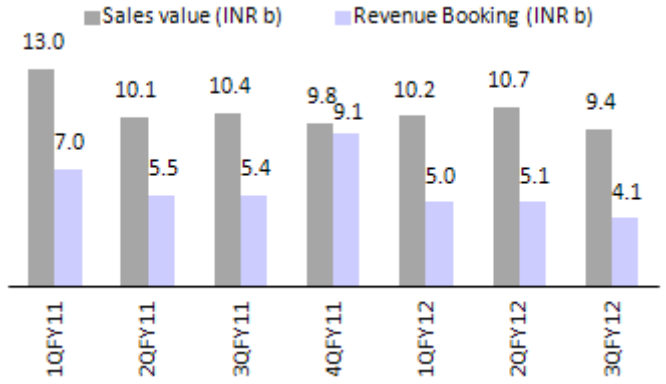
UT's steady launch volume and pre-sales value of ~INR130b over the last 11 quarters render meaningful cash flow visibility. However, slowdown in construction would delay the conversion of sales to cash flow and revenue booking. Despite a comfortable balance sheet with net debt-equity at ~0.43x, near-term repayment commitments and delays in re-financing have been eating away a significant portion of the operating cash flow, adversely impacting the construction ramp-up plan.

The stock trades at ~46% discount to our NAV estimate of INR56/share, and at 17.9x FY13E EPS of INR1.7 and 0.7x FY13E BV. The key catalysts for the stock would be (1) improvement in execution and cash flow through re-financing or asset sales, and (2) sales boost in ongoing projects. Maintain **Buy.**

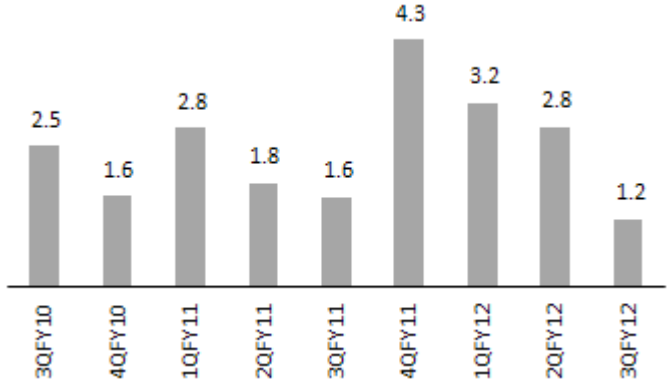
EBIT margin for real estate vertical declines QoQ (%)



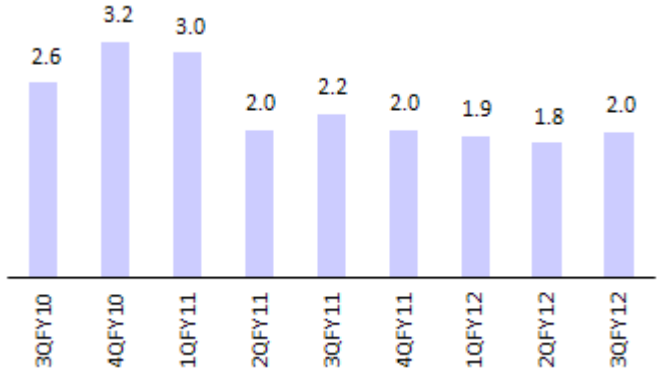
Gap between sales and revenue run-rate widening



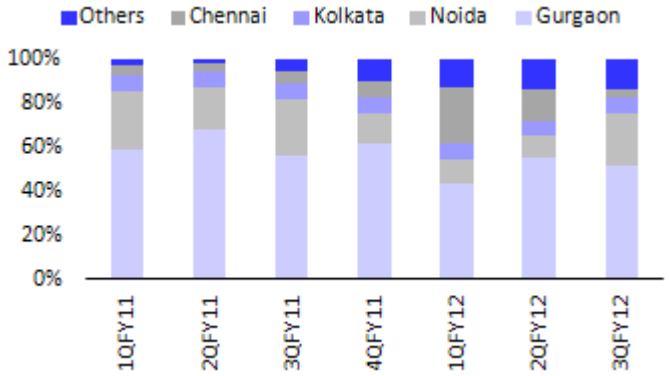
New launches decline, largely in Gurgaon and tier-II cities (msf)



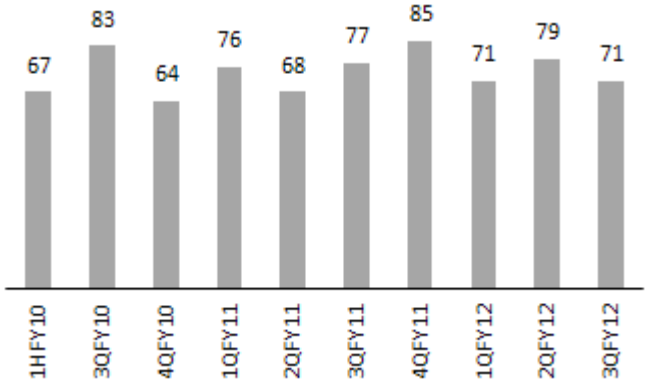
Sales volumes steady (msf) ...



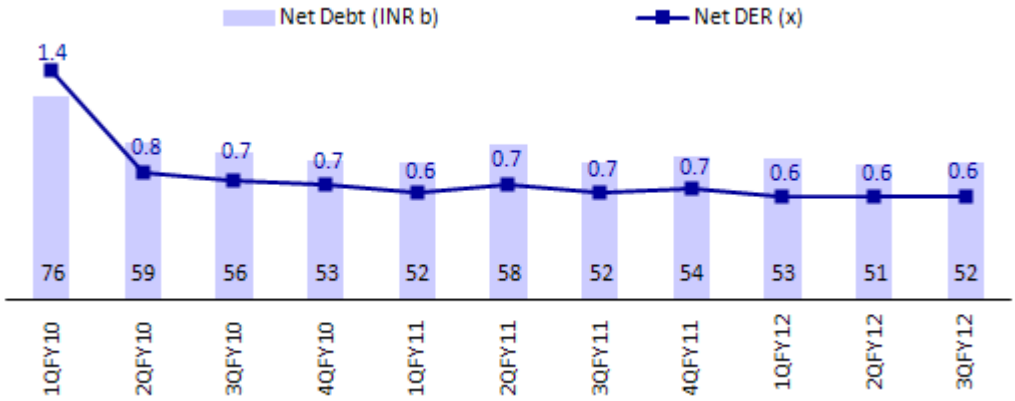
Gurgaon major sales contributor, contribution from Noida improves



Contribution from residential sales (%)



Net debt marginally up



Most locations witnessed QoQ de-growth in realization ('000INR/sf)

(INR '000)	1HFY10	3QFY10	4QFY10	1QFY11	2QFY11	3QFY11	4QFY11	1QFY12	2QFY12	3QFY12	QoQ (%)
Gurgaon	-	-	-	5.4	6.0	5.7	7.1	9.8	6.9	4.9	(29.2)
Noida	-	-	-	4.8	5.3	5.9	4.9	5.5	8.0	5.4	(32.7)
Kolkata	-	-	-	2.8	3.5	3.5	4.1	4.1	4.8	4.3	(9.7)
Chennai	-	-	-	1.7	2.7	2.3	2.1	4.6	3.8	2.7	(27.6)
Others	-	-	-	2.0	1.8	2.3	2.7	2.7	5.9	5.0	(15.0)
Total	**4.4**	**6.3**	**4.7**	**4.3**	**5.1**	**4.7**	**4.9**	**5.4**	**5.9**	**4.8**	**(19.2)**

Source: Company/MOSL

Unitech: an investment profile

Company description

Unitech is the second largest listed real estate developer in India by market capitalization. It was incorporated in February 1971 and converted to a public limited company in October 1985. In 1986, it launched its real estate development business with its first project in Gurgaon. Unitech Group also has a construction business, which undertakes civil construction and infrastructure projects.

Key investment arguments

- Improved revenue mix, accelerated new launches and focus on affordable housing segment
- Cashflow visibility from robust pre-sales
- Comfortable leverage

Key investment risks

- Negative news flow on the ongoing telecom 2G spectrum issue is a key overhang for the stock
- Headwind in re-financing, impacting construction
- Continuation of increasing debtors

Recent developments

- Consolidated gross debt increased marginally to INR54.7b, while net debt stood at INR51.9b, implying net debt-equity of 0.43x. Increase in debt is due to currency impact on foreign loans.
- The company sold 2msf (INR9.4b) in 3QFY12 v/s 1.8msf (INR10.7b) in 1QFY12. Total sales over 9MFY12 were IN30.3b v/s our estimate of ~INR40b.

Valuation and view

- The stock trades at ~46% discount to our NAV estimate of INR56/share, and at 17.9x FY13E EPS of INR1.7 and 0.7x FY13E BV.

Sector view

- RE sector has been a major underperformer over the last 12 months with multiple operational and nonoperational headwinds such as volume slowdown (due to declining affordability), monetary tightening, pilling liquidity pressure etc. However, with imminent rate cut cycle and increasing instances of regulatory pressure subsiding, we believe the outlook will improve going forward.

Comparative valuations

		Unitech	DLF	HDIL
P/E (x)	FY12E	23.2	29.1	5.7
	FY13E	17.9	24.8	3.5
P/BV (x)	FY12E	0.8	1.5	0.4
	FY13E	0.7	1.4	0.4
EV/Sales (x)	FY12E	5.4	6.3	3.7
	FY13E	4.2	5.5	2.0
EV/EBITDA (x)	FY12E	25.6	14.1	7.5
	FY13E	17.7	12.5	4.1

EPS: MOSL forecast v/s consensus (INR)

	Most Forecast	Consensus Forecast	Variation (%)
FY12	1.3	2.0	-35.5
FY13	1.7	2.5	-33.2

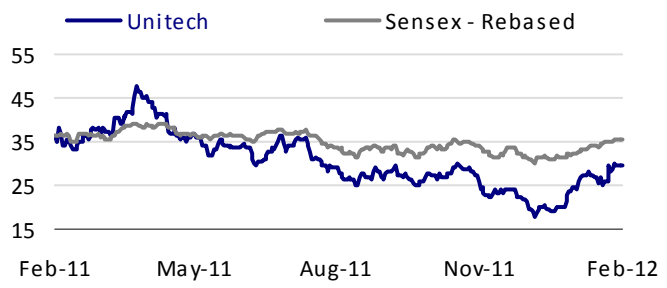
Target price and recommendation

Current Price (INR)	Target Price (INR)	Upside (%)	Reco.
30	42	40.0	Buy

Shareholding pattern (%)

	Dec-11	Sep-11	Dec-10
Promoter	48.6	48.6	48.6
Domestic Inst	2.3	2.5	1.9
Foreign	32.0	32.6	34.5
Others	17.2	16.4	15.0

Stock performance (1 year)



Financials and Valuation

Income Statement					(INR Million
Y/E March	2009	2010	2011	2012E	2013E
Net Sales	**28,945**	**29,313**	**31,871**	**23,646**	**29,290**
Change (%)	-29.7	1.3	8.7	-25.8	23.9
Construction Exper	11,891	17,608	21,339	15,444	18,370
Office & Site Est. E:	1,118	994	1,293	1,085	1,289
EBITDA	**15,935**	**10,712**	**9,239**	**5,008**	**6,958**
% of Net Sales	55.1	36.5	29.0	21.2	23.8
Depreciation	209	341	319	357	357
Interest	5,546	2,000	1,455	1,232	1,148
Other Income	4,212	585	1,050	1,785	1,065
PBT	**14,392**	**8,956**	**8,516**	**5,204**	**6,518**
Tax	2,424	2,169	2,704	1,717	2,024
Rate (%)	16.8	24.2	31.8	33.0	31.1
Reported PAT	**11,968**	**6,787**	**5,812**	**3,486**	**4,494**
Adjusted PAT	**9,689**	**6,751**	**5,677**	**3,351**	**4,348**
Change (%)	-41.7	-30.3	-15.9	-41.0	29.7

Balance Sheet					(INR Million)
Y/E March	2009	2010	2011	2012E	2013E
Share Capital	3,247	4,878	5,233	5,233	5,233
Reserves	48,448	99,173	110,604	113,657	117,706
Net Worth	**51,695**	**104,050**	**115,836**	**118,889**	**122,939**
Loans	90,558	60,078	58,507	53,507	50,832
Deffered Tax Liabi	14	46	56	76	96
Deferred Liab. for I	17,922	17,907	23,964	23,964	20,369
Capital Employed	**160,803**	**182,455**	**198,852**	**196,925**	**194,724**
Goodwill	11,673	15,264	16,540	16,540	16,540
Gross Fixed Assets	22,502	21,807	20,478	21,915	23,830
Less: Depreciation	1,003	1,344	1,539	1,896	2,254
Net Fixed Assets	**21,500**	**20,462**	**18,938**	**20,019**	**21,576**
Capital WIP	11,758	13,118	0	15,913	16,354
Investments	15,808	14,724	16,125	16,125	16,125
Curr. Assets	**202,189**	**220,098**	**254,232**	**267,430**	**282,494**
Projects in Progres	172,108	194,252	193,921	216,528	227,340
Debtors	9,310	12,670	21,474	23,130	24,250
Cash & Bank Balar	6,448	3,799	4,509	3,030	5,487
Loans & Advances	28,566	31,491	33,816	31,270	36,144
Curr. Liab. & Prov.	**22,846**	**101,211**	**122,773**	**139,102**	**158,365**
Creditors	22,549	99,870	121,248	137,576	156,839
Provisions	297	1,341	1,526	1,526	1,526
Net Curr. Assets	**179,342**	**118,887**	**131,459**	**128,328**	**124,129**
Appl. of Funds	**160,803**	**182,455**	**198,852**	**196,925**	**194,724**

E: MOSL Estimates

Ratios					
Y/E March	2009	2010	2011	2012E	2013E
Basic (INR)					
Adjusted EPS	**6.0**	**2.8**	**2.2**	**1.3**	**1.7**
Growth (%)	-41.7	-53.6	-21.6	-41.0	29.7
Cash EPS	7.5	2.9	2.3	1.5	1.9
Book Value	24.7	36.4	38.0	39.1	40.7
DPS	0.1	0.0	0.1	0.1	0.1
Payout (incl. Div. T:	1.4	0.0	4.5	7.5	5.8
Valuation (x)					
P/E			13.8	23.2	17.9
Cash P/E			12.8	20.3	16.0
EV/EBITDA			14.3	25.6	17.7
EV/Sales			4.2	5.4	4.2
Price/Book Value			0.8	0.8	0.7
Dividend Yield (%)			0.3	0.3	0.3
Profitability Ratios (%)					
RoE	18.7	6.5	4.9	2.8	3.5
RoCE	13.2	6.4	5.2	3.3	3.9
Leverage Ratio					
Debt/Equity (x)	1.8	0.6	0.5	0.5	0.4

Cash Flow Statement					(INR Million)
Y/E March	2009	2010	2011	2012E	2013E
PBT before EO Iter	**14,392**	**8,956**	**8,516**	**5,204**	**6,518**
Add : Depreciation	209	341	319	357	357
Interest	5,546	2,000	1,455	1,232	1,148
Less : Direct Taxes	2,424	2,169	2,704	1,717	2,024
(Inc)/Dec in WC	-12,549	-21,472	-11,861	1,651	6,655
CF from Operations	**-9,410**	**-12,344**	**1,737**	**6,558**	**12,473**
(Inc)/Dec in FA	-2,025	-664	-1,466	-1,561	-5,951
(Pur)/Sale of Inves	-1,643	-2,506	-2,678	0	0
CF from Invest.	**-3,669**	**-3,170**	**-4,144**	**-1,561**	**-5,951**
(Inc)/Dec in Net W	6,140	45,637	6,417	20	20
(Inc)/Dec in Debt	5,035	-30,480	-1,571	-5,000	-2,675
Less : Interest Paic	5,546	2,000	1,455	1,232	1,148
Dividend Pai	185	0	298	298	298
CF from Fin. Act.	**5,444**	**13,157**	**3,093**	**-6,511**	**-4,101**
Inc/Dec of Cash	**-7,634**	**-2,650**	**710**	**-1,480**	**2,457**
Add: Opening Bala	14,083	6,448	3,799	4,509	3,030
Closing Balance	**6,448**	**3,799**	**4,509**	**3,030**	**5,487**

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