Fullerton Securities

Result Update

January 24, 2012

LARSEN & TOUBRO LTD — BUY

Larsen & Toubro Ltd (L&T) reported better than expected Q3FY12 top line and bottom line growth. The revenues grew 23.6% Y-o-Y to Rs 139.98bn indicating healthy execution. The net profit rose 18% Y-o-Y to Rs 9.91bn, nearly 12% higher than consensus estimates of Rs 8.80bn. Looking at the current macro environment, we believe it is a strong set of numbers.

Key Highlights:-

- The order inflow for the quarter was Rs. 171bn, which is 27% higher on Y-o-Y basis, a positive surprise. The nine month order book stood at Rs. 494bn. Major contributor to the order book was infrastructure sector (roads and B&F segments), which added 45%. Power contributed 21%, hydrocarbons contributed 14%, process contributed 11% and others contributed the balance 9%.
- The Engineering & Construction (E&C) division registered robust 25% revenue growth to Rs 124.65bn on Y-o-Y basis. The Electrical & Electronics (E&E) segment and the Machinery & Industrial Products (MIP) segment got negatively affected by the sectoral slowdown and reported muted ~ 6% revenue growth on Y-o-Y basis to Rs. 84.3bn and Rs. 72bn, respectively.
- The management has maintained order inflow guidance at 5%, which was revised down in the last quarter and maintained its revenue guidance for 20-25%
- The company reported an order backlog of Rs 1.46tn at end 9MFY12, which provides a revenue visibility for next 2-3 years.
- The revenue growth was aided by other income, which jumped 79%, from Rs 2.5bn to Rs 4.49bn, mainly driven by dividend from subsidiaries and treasury operations.

Based on a sum-of-the-parts valuation, the fair value for Larsen & Toubro Ltd works out to Rs 1,478

Recommendations	<= 1 year	1 - 2 yrs	2 - 5 yrs
Strong Buy			
Buy			
Hold			
Reduce			
Sell			

***Strong Buy –** Expected Returns > 20% p.a.*
***Buy –** Expected Returns from 10 to 20% p.a.*
***Hold –** Expected Returns from 0 % to 10% p.a.*
***Reduce –** Expected Returns from 0 % to 10% p.a. with possible downside risk*
***Sell –** Returns < 0 %*

STOCK DATA

BSE / NSE Code	500510 / LT
CMP Rs (23th Jan'12)	1,278
Market Cap (Rs mn)	780,866
52 Week High-low	1932.95 / 971

STOCK RETURN (%)

	30D	3M	6M	1Y
Larsen & Toubro	27%	-4%	-30%	-23%
Sensex	6%	0%	-11%	-12%
Nifty	7%	0%	-10%	-11%

The management has maintained order inflow guidance of 5% and maintained its revenue guidance of 20-25% for FY12

The current order backlog of Rs 1.46tn implies 3.3times revenues based on FY11 revenues

Financial Snapshot

Projections (Rs. Mn)	Q3FY11	Q3FY12	% chg	FY10A	FY11A	% chg	FY12E	FY13E
Net Revenue	113,217	139,986	*23.6%*	370,097	438,417	*18.5%*	524,846	599,839
Total Income	116,956	144,473	*23.5%*	391955	454189	*15.9%*	537967	617834
EBIDTA	15,204	17,918	*17.9%*	70,350	72,248	*2.7%*	77,401	86,103
EBIDTA %	13.4%	12.8%		19.0%	16.5%		14.7%	14.4%
PAT	8,405	9,916	*18.0%*	43,755	39,579	*-9.5%*	41,898	45,643
NPM %	7.4%	7.1%		11.8%	9.0%		8.0%	7.6%
EPS Rs	12.7	13.1	*3.2%*	70.8	63.2	*-10.8%*	68.6	74.8
BVPS Rs				304.1	358.8	*18.0%*	426.4	501.2
ROE %				23.3%	17.6%		16.1%	14.9%
PER x							17.9	16.4
P/B Ratio							2.9	2.4

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OTHER HIGHLIGHTS

The management has maintained its revenue guidance at 20-25% and order inflow guidance at 5%. The management still believes that ordering environment is challenging and stiff competition will continue going forward. This was reflected in the nine months order inflow, which was flat compared to last year. In Q3FY12, order inflows mainly came from infrastructure. Power sector witnessed sharp correction in the order inflow. As far as geographical breakup is concerned, domestic market dominated with 80% of the order inflow while foreign market contributed rest 20%, mainly Middle East.

More than 5000 employees added during the quarter

The management intends to incur Rs 15bn of CAPEX at the parent level this fiscal, out of which Rs. 10bn cash outlet has already happened in the first nine months. The company also intends to infuse equity of Rs 15-20bn in subsidiaries. On the Hyderabad Metro Rail Project, the company stated that the State Government is yet to handover the complete land and is likely to be delayed. The major part of the land, 100 acres of block is stuck in court case which is stumbling block. The company's IT subsidiary, **L&T Infotech** registered a top line growth of 34% to Rs 8.35bn, led by growth in BFSI segment. PAT grew by healthy 40% to Rs. 1.17bn, due to operating leverage, inspite of STPI tax benefit withdrawal in the current year. The company has total developmental projects of around 40 SPVs from diverse sectors such as roads, power, ports, metro rails and urban infrastructure space in excess of Rs. 750bn.

Developmental projects of around 40 SPVs in excess of Rs. 750bn

Key risks include further downside risks to order inflows and slower than expected execution. However, we believe that declining interest rate and pick up in investment cycle will benefit the stock. We expect L&T's revenues to grow at a CAGR of 17% over FY2011-13 to Rs 599.8bn by FY13 and estimate PAT to grow at a CAGR of 7.4% over the same period to Rs 45.6bn in FY13. Considering the current macroeconomic headwinds, lowered profitability for the company and further risks to FY12 order inflow guidance, we assign a P/E multiple of 14 for the standalone entity. **Based on a sum-of-the-parts valuation, the fair value for Larsen & Toubro Ltd works out to Rs 1,478.** We upgrade our recommendation from 'HOLD' to **'BUY'** due to correction in the stock price in the last quarter.

Hyderabad Metro Project orders to be delayed as 100 acres of land block is stuck in litigation

Financial Analysis and Projections

Particulars (Rs Mn)	FY09A	FY10A	FY11A	FY12E	FY13E
Net Revenue	339,081	370,097	438,417	524,846	599,839
Other Income	17,341	21,858	15,772	13,121	17,995
Total Income	356,422	391,955	454,189	537,967	617,834
Operating Expenditure	301,702	321,605	381,941	460,566	531,730
Depreciation	2,848	3,837	5,758	6,797	8,370
EBIT	51,872	66,514	66,490	70,605	77,734
EBIT Margin (%)	15.3%	18.0%	15.2%	13.5%	13.0%
Interest	4,777	6,377	7,475	8,070	9,610
Profit Before Tax	47,095	60,137	59,015	62,534	68,124
Less: Tax	12,278	16,382	19,436	20,636	22,481
Profit After Tax	34,817	43,755	39,579	41,898	45,643
PAT Margin (%)	10.3%	11.8%	9.0%	8.0%	7.6%
ROE (%)	27.1%	23.3%	17.6%	16.1%	14.9%
EPS (Rs)	57.7	70.8	63.2	68.6	74.8
BVPS (Rs)	212.7	304.1	358.8	426.4	501.2
Valuation Ratios (x)				**FY12E**	**FY13E**
P/E				17.9	16.4
P/B				2.9	2.4

SOTP Valuation

L&T Value	Methodology	Value
Standalone Entity	Standalone P/E multiple of 14 for FY13E	**1047**
Subsidiaries Value		**432**
L&T InfoTech	12x FY13E EPS	98
L&T Finance Holding	30% discount to EV	114
L&T IDPL	1.5x Equity Invested as on Q2FY12	129
Other Subsidiaries	1x FY11A BV	90
	Total Value	**1478**