Stock Note (CMP: Rs 154.5) **July 01, 2009**

Company Background & its Business Structure

Incorporated in 1998, IRB Infrastructure Developers Ltd. (IRBD) is an infrastructure development & construction company in India with significant experience in the roads & highways sector. Its infrastructure development business involves the construction, development and operation of infrastructure projects. IRBD currently has 10 operational BOT (Build, Operate & Transfer) projects in its portfolio, while 2 BOT projects are in the construction phase. Its construction business complements the infrastructure development business & involves engineering, procurement & construction work (EPC) for construction projects and operations and maintenance on a contractual basis. IRBD has moved up the value chain & recently ventured into the field of real estate development.

IRBD came out with an IPO of Rs. 9.44 bn in February 2008 with an objective to invest in its subsidiaries & for pre-payment & repayment of its existing loans. Most of the work in both in the infrastructure development business and construction business is won on a competitive bidding basis. IRBD's clients are usually Government entities (National Highways Authority of India, Maharashtra State Road Development Corporation, etc.) that award project specific contracts to bidders based on certain eligibility requirements. These eligibility requirements generally include project experience, engineering capabilities & financial strength. IRBD may enter into project-specific joint ventures with other companies to meet these requirements or to further enhance its credentials. In the Surat-Dahisar project (awarded to IRB in April 2008), IRB has entered into an agreement with Deutsche Bank as a financial partner, which has a 10% equity stake in the project.

IRBD is the holding company of the IRB Group. The company was formed to fund the capital requirements of the IRB Group's initiatives in the infrastructure and construction sectors. Its business operations are conducted through its various subsidiaries. The following is the existing group structure showing the subsidiaries through which the construction & real estate work is executed:

Subsidiaries of IRBD	Business / Project of Subsidiary	% Holding of IRBD
Infrastructure Development & Construction business		
Ideal Road Builders Pvt. Ltd. (IRBPL)	BOT projects (Thane Bhiwandi bypass BOT & Kaman Paygaon BOT). Bhiwandi Wada BOT & Khambhatki Ghat concession period over.	100
Modern Road Makers Pvt. Ltd.	Engineering & Construction Arm	100
Aryan Toll Road Pvt. Ltd.	Pune - Solapur BOT (29.81 km – NH9)	100
ATR Infrastructure Pvt. Ltd.	Pune - Nasik BOT (29.81 km – NH 50)	100
Mhaiskar Infrastructure Pvt. Ltd.	Mumbai - Pune BOT (206 km – MPEW & NH4)	100 (74% held by IRBD & 26% by IRBPL)
Thane Ghodbunder Toll Road Pvt. Ltd.	Thane Ghodbunder Toll Road BOT (14.9 km)	100 (74% held by IRBD & 26% by IRBPL)
IDAA Infrastructure Pvt. Ltd.	Bharuch - Surat BOT (65 km – NH8)	100 (53.29% held by IRBD, 10.81% by ATRPL, 23.75% held by ATR Infra & 12.05% held by IRBPL)
NKT Road & Toll Pvt. Ltd.	Ahmednagar - Karmala - Tembhurni Road (60 km)	100 (53.33% held by IRBD & 46.67% by IRBPL)
IRB Infrastructure Pvt. Ltd.	Bridge over Patalganga River – Kharpada BOT (1.4 km)	100 (80.15% held by IRBD & 19.85% held by IRBPL)
MMK Toll Road Pvt. Ltd.	Mohol - Kurul - Kamati - Mandrup Road (33 km – SH 149)	100 (100% held by IRBPL)
IRB Surat Dahisar Tollway Pvt. Ltd.	Surat-Dahisar Road – 239 km NH-8	90 (10% held by Deutsche Bank)
IRB Kolhapur Integrated Road Development Company	Integrated Road Development in the city of Kolhapur	100 (80% IRB, 10% MRMPL & 10% ATR Infra)
In Real Estate Business		
Aryan Infrastructure Investments Pvt. Ltd.	Land Bank Adjoining the MPEW	66

(Source: Company)

Investment Rationale:

Strong track record in infrastructure development & construction projects in the roads / highways sector

IRBD has years of experience in the infrastructure development and construction business. It has been involved in the construction or operation and maintenance of more than 1,200 km of highways and roads in India. This gives IRBD an advantage over its competitors when bidding for new large BOT projects and enables it to capitalize on the opportunities available in this growing sector. Its experience in roads & highway development projects enables it to effectively evaluate new projects. IRBD's portfolio of projects includes prestigious projects like the Mumbai - Pune Expressway (MPEW) & NH 4 (National Highway 4) BOT project that was awarded to it in March 2004 as well as the BOT project for the Bharuch to Surat section of the NH 8, which was awarded to it in July 2006.

Well placed to exploit the opportunity in the road BOT projects

IRBD is a pioneer in the road BOT business and is one the largest road BOT operators in the country with over 12 BOT projects under its belt (772 km of length), with 10 operational BOT projects, & 2 under-construction BOT projects (Surat - Dahisar project & Kolhapur). The company holds a market share of 7.56% in Golden Quadrilateral & reportedly ~ 20% share in BOT contracts awarded in the last 12-18 months. IRBD has strong execution & management skills in the BOT arena of road development with the company completing a majority of its projects on or before time.

For the road sector, the total amount of new work initiated is difficult to estimate. However, a look at the central government's highway development programme and state road programmes suggest a massive pick-up in new order inflows for construction players. In FY09, the number of road projects awarded reduced significantly due to changes in the model concession agreement, lower corporate confidence & tight liquidity situation.

There are a few players who can successfully execute long gestation BOT projects. IRBD, with its successful track record & strong project management and execution skills is well placed to exploit & capture growth opportunities in the road BOT projects. The company expects to add orders covering ~500 km in the Golden Quadrilateral project as it has been pre-qualified for (or applied for) ~Rs. 280 bn worth of contracts, which will be up for bidding in the next few months. The table below gives an overview of upcoming opportunities for IRBD:

(Rs. In Million)

Name of Client	Request for Proposal Stage (RFP)	Request for Qualification Stage (RFQ)
NHAI Projects – Phase III	56,138	62,968
NHAI Projects – Phase V	33,504	56,746
NHAI Projects – OMT Basis	2,614	5,520
GSRDC Projects	-	13,524
Government of Rajasthan Projects	-	5,000
MSRDC Projects	2,310	-
Maharashtra PWD Projects	13,644	8,109
MIDC Projects	1,500	-
Total	**1,30,501**	**1,51,867**

(Source: Company)

Integrated execution capabilities with in-house construction, toll collection & management capabilities

The EPC activities for IRBD's funded construction projects as well as for BOT projects are all completed within the IRB Group. Similarly, operation and maintenance activities (O&M) related to its BOT projects, including toll collection, are also executed within the IRB Group. This enables IRBD to not only reduce its dependence on third party sub-contractors & exercise greater control over the quality and timely execution of the construction and operation and maintenance works but also enables it to capture the entire economic value chain in such projects. IRBD has 20 years of experience in Toll Business, which includes the agency toll collections & approx. 13 years of experience since the time the first BOT project (Thane - Bhiwandi) was awarded to the company. The toll business currently accounts for 44.5% of IRBD's total revenues. Toll revenues have increased from Rs. 1.89 bn in FY06 to Rs. 4.54 bn in FY09. The company has strong locational advantage in serving the fast growing and strong economic centres of India viz, Maharashtra & Gujarat. IRBD owns a large fleet of sophisticated construction equipment and this enables it to be less dependent on third parties and to efficiently manage its equipment assets. This form of backward integration provides IRBD with a competitive advantage over other infrastructure development and construction companies that generally need to outsource portions of their operations to external contractors.

Moreover, the integrated execution capabilities enable IRBD to better evaluate potential funded construction or BOT projects. IRBD has successfully completed various challenging engineering construction projects, such as the four laning of the Mumbai - Pune stretch of NH 4, the construction of an 890 metre tunnel on the Khambatki Ghat near Satara, & the construction of a bridge over Kasheli Creek on the Thane Bhiwandi bypass road.

Economically beneficial arrangements with respect to certain BOT projects

Under the concession agreements relating to the Pune - Solapur road BOT project and the Pune - Nashik road BOT project, the Ministry of Shipping, Road Transport & Highways (MoSRTH) has undertaken that the Government of India will not construct & operate either on a BOT basis or otherwise a competing project facility, either toll free or otherwise, during the concession period; except where the fee charged for vehicles using such facility is in excess of 133% of the fee being charged for the vehicles using the roads under IRBD's concession agreements with the MoSRTH.

In addition, under the concession agreement for the BOT project relating to the Bharuch to Surat section of NH 8, the NHAI has undertaken that no expressway or toll road (other than a bypass) between the Bharuch to Surat section of NH 8 shall be opened to traffic before the expiry of eight years from the date of the commencement of the concession period. In addition, in the event that an additional tollway is constructed following such eight year period, then NHAI shall ensure that the per kilometre fee to be levied on any vehicle or class of vehicles using such additional tollway shall not be less than an amount which is 133% of the per kilometre fee levied & collected from similar vehicles or class of vehicles using the NH 8 section covered under IRBD's BOT project.

With respect to the arrangements described above, IRBD enjoys economically beneficial rights to certain important sections of these National Highways and other important roads and highways in Western India. In addition to the above arrangements, with respect to the Mumbai - Pune Expressway and NH 4 project, since the project covers both the Mumbai - Pune Expressway and the NH 4 corridors, the company does not expect to face competition from other competing road or highway in this route.

Moving up the value chain – Real Estate Developer

IRBD has ventured in the real estate business through its 66% subsidiary Aryan Infrastructure Investments Pvt Ltd (AIIPL). IRBD plans to setup an integrated township alongside the Mumbai-Pune expressway. The proposed township would be spread over 1,400-1,450 acres. Of this, around 60% would be residential and the rest will be developed for commercial activities. The company has a land bank of 1,250 acres and has proposed to acquire the balance 150-200 acres in the next 6-8 months for its proposed township. The total cost of 1,250 acres acquired amounts to Rs. 1.9 bn. This has been funded through internal accruals. With influx of major IT companies in and around the main city of Pune, we believe that the Real Estate venture could be a major growth driver for the company going forward. However, the entire development is expected to complete over the next 8 to 10 years. This would be in partnership with a developer. No revenue is expected to flow for the next 2 to 3 years. With the current downturn in the real estate cycle, the company has decided to go slow on this project. Also, if the company decides to sell the land bank acquired, it could still be profitable as it could fetch Rs. 40-45 lacs per acre (almost three times the cost of acquisition, which was Rs. 15 lacs per acre).

Healthy Order Backlog involving large projects like Surat-Dahisar, Surat-Bharuch & Kolhapur

IRB group's current order book stands at Rs. 59 bn, which has increased from Rs. 23.25 bn as on December 31, 2007. This is mainly on account of two projects awarded in FY09 viz; Surat-Dahisar (awarded in April 2008) & Kolhapur project (Awarded in March 2008).

Surat –Dahisar project

Surat-Dahisar project involves the six laning of the existing four-lane Surat - Dahisar section of NH 8 for a total length of 240 kms. IRBD has entered into an agreement with Deutsche Bank as a financial partner, which has an equity stake of 10% in this project. The total cost of this project is estimated at Rs. 23 bn (revised construction cost), which would be funded through a mix of internal accruals & borrowings (70:30 Debt-Equity). The original construction cost was Rs. 28.4 bn, which has been revised downwards due to decrease in the prices of bitumen & steel. The concession period is for 12 years including the construction period of 30 months (from Feb 2009). The project involves the construction of 25 flyovers over various junctions. However, the company would have to pay the effective share of 38% to NHAI of the toll revenue for the initial year of the concession period with an increase of 1% revenue share in each succeeding year during the course of the concession period. The toll collections have already started from February 2009 onwards. The average gross collections amount to Rs. 8.5-9 mn per day, which is lower than the company's estimates of Rs.10-15 mn per day. This is on account of sharp decline in the port traffic due to slowdown in the exports & imports witnessed over the past few months. Despite the lower toll collections, the project IRR could remain the same due to fall in the project cost by about Rs. 5.4 bn.

Surat-Bharuch project

The financial closure of Surat-Bharuch project was achieved in December 2006. The project involves expansion & improvement of Bharuch-Surat section of NH 8 in Gujarat on a BOT basis. IRBD is required to expand specific sections of NH 8 into a six-lane highway & to make improvement to the existing four-lane highway. The total cost of the project is Rs. 14 bn (including an upfront fee to NHAI of Rs. 5 bn), which has been funded through a mix of borrowings & internal accruals (Debt-Equity 85:15). The construction activity already commenced on January 2007 & work so far has progressed as per schedule. EPC work of Rs. 1 bn is still remaining to be completed, while the O&M contract is worth Rs. 5 bn. The tolling is likely to commence in July 2009 & the company expects the average toll collection to be Rs. 4-5 mn per day. The agreement involves the increase in toll rates linked to WPI index.

Kolhapur project

In March 2008, the Maharashtra State Road Development Corporation (MSRDC) awarded the maintenance & operating contract to IRBD to develop & maintain all major roads in Kolhapur city. It is for the first time in the history of India's road sector that a single operator has been appointed such project. The project will cover the upgradation of all major roads in Kolhapur into four-lane with all related infrastructure like footpaths. The total length of the road under upgradation is 49.5 km. After upgradation, IRBD would own & operate these roads for 30 years. The total cost of the upgradation project is estimated at Rs 4 bn (including negative grant of Rs. 0.27 bn to MSRDC), which is expected to be financed through a mix of debt (70%) & equity (30%). O&M cost over 30 years is around Rs. 650 crores. MSRDSC's traffic data shows that around 45,000 vehicles enter and exit city through nine entry/exit points in a single day. The company expects to recover its investments through toll collection rights at the peripheral entry points of the city's municipal limits (9 entry points). In addition to the concession period, IRBD has been allotted commercial plot admeasuring 30,000 square meters by the municipal corporation. The lease period for this land is 99 years. Thus, this is the only BOT project wherein the company has got land development right. The construction activity has commenced from January 2009 & will take 2-2.5 years to be completed. The company expects an average toll collection of Rs. 1-1.1 mn per day from this project.

The strong order book provides visibility to the future revenue and earnings of the company. This fiscal, IRBD expects to receive new projects worth Rs. 40-50 bn. This would further strengthen the current order backlog. The break up of the current order book is given below as follows:

Order Book Composition	Rs. in Million
BOT projects in O&M Phase	25,774
Funded Projects	2,742
EPC in ongoing BOT projects	30,462
Total	**58,978**

Other recently awarded projects (in June 2009) not included in order book

i) **Goa-Karnataka Highway project:** Recently, IRBD has been awarded the four-laning of the 65-km long National Highway-4a Goa-Karnataka border starting from Panjim. The contract has been awarded on a 30-year design-build-operate and transfer basis to IRBD, which will implement it through a special purpose vehicle. NHAI will be chipping in with Rs 1.86 bn by way of viability gap funding for this Rs. 8 bn project. The project is expected to be completed by 2011.

ii) **Highway project in Punjab:** IRBD has emerged as the lowest bidder to four-lane a 102-km stretch of the Pathankot-Amritsar section of National Highway-15, on a BOT basis. The project is on Grant basis with concession period of 20 years and estimated cost of the project is Rs. 12 bn. The Company has sought a grant of Rs. 1.26 bn for the project from NHAI. The construction period is 910 days.

iii) **Highway project in Rajasthan:** IRBD has emerged as the lowest Bidder for the highway project to be built between Jaipur to Deoli section of NH12 (a 146 km stretch) in Rajasthan under NHDP Phase III on BOT Basis. The project is on Grant basis with concession period of 25 years & estimated cost of the project is Rs. 15 bn. IRBD has sought a grant of Rs. 3.06 bn for the Project from NHAI.

iv) **Highway project in Maharashtra**: IRBD has emerged as the lowest Bidder for the highway project, which involves four lanning of Talegaon - Amravati section of NH 6 (167-km stretch) under NHDP Phase III on BOT Basis. The project is on Grant basis with concession period of 22 years & estimated cost of the project is Rs 8 bn. IRBD has sought a grant of Rs 2.16 bn for the Project from NHAI.

These projects are expected to further improve the revenue visibility of IRBD. In respect of (ii), (iii) & (iv) above, IRBD could be awarded the projects shortly. We expect the company to bag even more road BOT projects in the coming months.

Consolidated Net Sales & PAT to rise 83.1% & 60.1% respectively, however Margins to remain under pressure

We expect IRBD's consolidated Net Sales & PAT to increased by 83.1% & 60.1% respectively in FY10. PAT growth expected is lower than in line with sales mainly due to higher depreciation & interest cost to be incurred in FY10. Consolidated EBITDA margins are expected to decline from 44.1% in FY09 to 43.2% in FY10, while the PAT margins are expected to decline form 17.7% in FY09 to 15.6% in FY10. This could be mainly due to higher contribution from the construction business (expected to contribute 60% to the total consolidated revenues), which offers lower margins as compared to the toll business.

Toll business:

Toll business is expected to grow by 66.3% to Rs. 7.55 bn in FY10 [FY09: Rs. 4.54 bn], which could mainly be driven by incremental toll collections from Surat-Dahisar & Surat-Bharuch projects. The estimations have been made after considering the average toll collections from Surat-Dahisar at Rs. 8.5-9 mn, which are well below the company's estimates of Rs. 10-15 mn per day. Any increase in the toll collections here could boost the total toll revenues further. The EBITDA margins under this business are expected to improve from 80.5% in FY09 to 83% in FY10 on the back of lower operation & maintenance expenses in FY10 as compared to FY09. In FY09 the EBITDA margins had declined to 80.5% from 91.5% in FY08, mainly due to higher operation & maintenance expenses during the fiscal. In Q4FY09, the company incurred higher periodical maintenance expenses, which were earlier expected to be incurred in FY10. However, we expect the PAT margins to decline marginally to 28.1% from 28.2% in FY09, due to higher interest & depreciation cost.

The table below gives an overview of toll collections over the last four quarters & for FY09:

Projects (Rs. In Mn)	Q4FY09	Q4FY08	Q3FY09	Q3FY08	Q2FY09	Q2FY08	Q1FY09	Q1FY08	FY09	FY08	VAR [%]
4 BOT Projects of IRBPL	144	157	137	131	143	117	163	124	587	529	11.0
Kharpada Bridge	17	19	16	18	17	17	20	21	70	75	-6.7
Nagar-Karmala-Tembhurni	27	28	27	27	29	27	31	28	114	110	3.6
Pune - Solapur	30	39	30	35	31	29	37	34	128	137	-6.6
Pune - Nashik	41	41	41	40	42	39	40	40	164	160	2.5
Mumbai - Pune	704	595	722	594	726	584	720	579	2872	2352	22.1
Thane - Ghodbunder	66	75	67	69	64	63	68	66	265	273	-2.9
MMK	16	16	15	16	17	16	18	13	66	61	8.2
Surat Dahisar (Gross)	336	0	0	0	0	0	0	0	336	0	-
Total Toll Collection	**1381**	**970**	**1055**	**930**	**1069**	**892**	**1097**	**905**	**4602**	**3697**	**24.5**

(Source: Company)

The 'Mumbai-Pune Expressway (MPEW) and NH4 highway' contributes around 28.1% to IRBD's total consolidated revenues & 62.4% to the toll revenues (in FY09). The agreement specifies 18% hike in the toll rates every three years in April. From the table it can be observed that toll collections from Mumbai-Pune increased 22.1% over FY08. This includes the effect of 18% increase in the toll rates from April 2008. However, sequentially the toll collections declined in Q3FY09 & Q4FY09, which indicates a slowdown in traffic growth. Kharpada bridge, Pune Solapur & Thane-Ghodbunder witnessed a decline in the toll collections over FY08 by 6.7%, 6.6% & 2.9% respectively. MMK witnessed a decent growth of 8.2% in FY09 over FY08. The 4 BOT projects of IRBD witnessed an increase of 11% in toll collections in FY09. However, the concession period of two projects viz; Bhiwandi Wada & Khambatki Ghat have ended from Q3FY09 & Q1FY10 respectively. These projects contributed around Rs. 147 mn (3.2%) to the total toll revenues in FY09. Hence, it is unlikely to have any significant impact on the toll collections from FY10 onwards. Toll collections from Surat-Dahisar amounted to Rs. 336 mn (collections started from Feb 20, 2009). However, this is the gross collection, including 38% revenue share of NHAI. However, the toll collections were lower (Rs. 8.5-9 mn per day) than what the company had estimated (10-15 mn per day).

Construction Business:

We expect the construction business to report net sales of Rs. 10.95 bn in FY10, an impressive growth of 93.1% over FY09 sales. The growth would mainly be led by EPC revenues from Surat-Dahisar project & from other EPC contracts under the existing BOT projects. However, EBITDA margins are expected to decline to 17.5% in FY10 from 17.9% in FY09 due to higher construction cost. Higher interest & depreciation could put pressure on PAT margins, which are expected to decline to 7.5% in FY10 from 8.6% in FY09. The EPS of this business is expected to grow by 67.6% from Rs. 1.5 in FY09 to Rs. 2.5 in FY10.

Industry Outlook:

BOT Projects

Build-Operate-Transfer ("BOT")

Under this type of PPP contract, the Government grants to a contractor a concession to finance, build, operate and maintain a facility for the concession period. During the concession period, the operator collects user fees and applies these to cover the costs of construction, debt servicing and operations. At the end of the concession period, the facility is transferred back to the public authority. BOT projects can be annuity-based or toll-based, as defined below:

BOT annuity-based projects:

Under this form, the concessionaire is responsible for constructing and maintaining the project facility. The GoI, usually through the NHAI in the case of highway projects, pays the concessionaire a semi-annual payment, or annuity. The concession contract is awarded to the bidder, which, among other criteria, quotes the lowest annuity amount. Under this approach, the amount of income collected by the concessionaire is not directly related to the usage level of the project. In the context of highway projects, the amount of income is not by direct reference to the number of vehicles using the highway. Instead, the risk that traffic, and consequently user fees, may be lower than expected is borne by the NHAI alone. However, the NHAI retains the right to charge users a toll at any stage of the project and it also retains all rights to property development, advertising at the project site and other revenue-generating activities.

BOT toll-based projects:

In order to reduce the dependence on its own funds and to promote private sector involvement in developing projects, the NHAI has awarded some highway projects on a toll basis. In this case, the concessionaire is responsible for constructing and maintaining the project as well as being allowed to collect revenues through tolls during the concession period. After the expiry of the concession period, the project is transferred back to the NHAI.

Engineering Procurement Construction/Lump-Sum Turnkey (“EPC/Turnkey”) Contracts

In this form of contract, contractors are required to quote a fixed sum for the execution of an entire project including design, engineering and execution in accordance with drawings, designs and specifications submitted by the contractor and approved by the customer. The contractor bears the risk of incorrect estimation of the amount of work, materials or time required for the job. Escalation clauses might exist in some cases to cover, at least partially, cost overruns.

Operations and Maintenance (“O&M”) Contracts

Typically an operations and maintenance contract is issued for operating and maintaining facilities. This could be in sectors such as water, highways, buildings & power. The contract specifies routine maintenance activities to be undertaken at a predetermined frequency as well as breakdown maintenance during the contract period. While the contractor is paid for the routine maintenance based on the quoted rates, which are largely a function of manpower, consumables and maintenance equipment to be deployed at the site, any breakdown maintenance is paid for on a cost plus basis.

Buoyant Outlook of Infrastructure Sector

With the sweet victory claimed by the UPA government in the recently held elections, the importance towards implementation of the promised reforms and focus towards infrastructure comes back into the limelight. One of the key factors that could drive India’s growth story is the concerted focus to be laid towards infrastructure and allied activities. The 11th and the 12th Plan would play a significant role in building India along with the ranks of the global economies. Public investment in the nation’s infrastructure has been insufficient to develop the foundation for long-term growth. The infrastructure sectors in India are expected to draw funds of about US$ 345 billion during the 11th Five Year Plan, which may offer investment opportunities.

Visible failures are evident in the lack of power and potable water in large parts of India, poor road conditions and cargo handling delays at ports and airports that are managed by government entities. A beginning has been made in the public sector, by setting targets for various infrastructure sectors to address the gaps in quantity and quality. The strategy for the 11th Plan entails strengthening and consolidating the infrastructure-related initiatives, such as Bharat Nirman for building rural infrastructure, and sectoral initiatives, such as the RGGVY, APDRP, Accelerated Irrigation Benefit Programme (AIBP), NHDP, National Maritime Development Programme (NMDP) and the JNNURM. The strategy for the Eleventh Plan also encourages private sector participation directly as well as through various forms of PPPs where desirable and feasible. The share of the private sector in infrastructure investment will have to rise substantially from about 20% anticipated in the Tenth Plan to around 30% in the Eleventh Plan.

Road Transportation

India has an extensive road network of 3.3 million kilometres, which is the second largest in the world. Though the roads in India carry about 65% of the freight and 80% of passenger traffic, the quality and extent of the roads is inadequate, making it a priority sector for development. Private sector participation is increasing and is usually through construction contracts, or BOT models for about 36% of total investment, based on competitive bidding or the lowest total government investment involved. Developers or owners as the case may be are permitted to collect tolls on roads that are part of the National Highway Development Plan, India’s largest road project till date.

During FY05-09, total road projects completed stood at 9,819 kms; of which projects completed during FY07-09 stood at just 4,575 kms. Also, new projects awarded during FY05-09 stood at 11,502 kms; of which projects awarded during FY07-09 stood at just 3,571 kms. The key reasons for delays in terms of project awards during FY07-09 were largely due to restructuring of NHAI, formation of 'PPP Advisory Committee', introduction of new Model Concession Agreement, etc. Apart from the above, there were issues in terms of land acquisition, shifting of utilities, execution challenges, etc which impacted project execution.

With the appointment of Mr. Kamal Nath as the Union Minister for Road Transport and Highways, the focus of the government towards infrastructure seems clear. Mr. Kamal Nath who has handled key portfolios like Commerce & Industry in the previous term had played a key role in pinning down new trade policies including the comprehensive Foreign Trade Policy. This time the portfolio has been changed, but the responsibility has increased substantially. The new minister would have to address to key grey areas related to infrastructure such as improving the road network, faster execution of the existing projects, arranging adequate capital facilities to fund these projects and finally solving the operational concerns related to road infrastructure along with the respective state governments.

The minister has publicly acknowledged that India's roads are a mess, which says that opening up the sector for massive investment and infrastructure spending as a key area for development. Noting that currently India builds just two kilometers of highway every day, the minister has set a target to increase this to 20 kilometers a day and has established a new financial body, the Roads Finance Corporation, to increase road construction through securitizing the required income. It could also look to list this venture to raise funds to meet the requirements. The new government has earmarked US$92 billion for road and highway construction with immediate effect until 2012, while the government is inviting bids for over 200 national highway projects covering over 13,000 kilometers of road at this moment. The Indian government intends to finance the construction of India's new roads and highways by raising financing from the overseas, including pension funds and long term investors, in addition to opening up the sector to foreign development and participation. Funding from India's road tax and fuel sales taxes, in addition to budgetary allocations would also assist the construction.

Toll Collections - A Profitable phenomenon

The stimulus packages from Indian Government have started working and that is already seen by Auto sales in Jan-Feb-March 2009. With increasing vehicles on the road, toll collection looks like a profitable phenomenon. Any new government will try to improve the road-network in India by laying more roads and having more expressways, Infrastructure is a must for Indian growth story. Company like IRBD, which is one of the largest players in toll based BOT road projects is well placed to capitalize on it.

Real Estate Update:

After booming in FY08, under-construction activity has slowed down significantly over the last one year, implying lower cash outflows towards projects. A drop in land acquisition and sluggish construction activity generally translates to a delay in new launches & deferral of planned projects. With the global financial meltdown destroying domestic real estate demand, developers found themselves stuck up in a debt dilemma, with their capital inflows having been dried up completely. However, with the RBI allowing them a one time re-structuring of debt along with the better performance of capital markets over the last three to four months has receded the risk of defaults. Large developers are being allowed to raise equity capital.

There has been some improvement witnessed in demand for affordable housing as a result of strategies like downsizing the apartment sizes & cut in the prices by 20-25%. Further, cleaning up the balance sheets, selling part of non-core land bank, monetization of non-core assets, and deferment of work on commercial projects have started yielding results. In the long run, the stable government & lower / stable interest rates could be some of the positives for the sector. However in the short term, we don't expect any significant turnaround due to oversupply. It could take a few more quarters for the demand situation for commercial & residential properties to improve drastically.

Risks & concerns

- In order to fund the recently awarded / to be awarded projects, IRBD might have to dilute its equity capital (by way of rights issue, preferential issue, etc) besides resorting to borrowings.
- Certain statutory and regulatory approvals, licensing, registration & application procedures are required to be applied / followed by IRBD. Government delays in obtaining approvals may affect IRBD's future growth prospects.
- There is a significant risk of decline in traffic growth due to slow down in economic growth. Also, the ability to raise the toll rate is limited beyond certain point due to resistance by users and interference of government authorities.
- IRBD's revenues are derived primarily from contracts awarded on a project-by-project basis. It is very difficult to predict whether & when a new project would be awarded due to lengthy & complex bidding & selection processes. This could result in substantial fluctuations in IRBD's operations and cash flows materially from period to period depending on the timing of contract awards.
- Any significant price escalation in the costs of and/or scarcity in availability of key equipments, basic materials may affect IRBD's performance
- IRBD faces stiff competition from the international engineering & construction companies or their regional operating entities as well as other Indian infrastructure developers & construction companies. IRBD's industry has been frequently subject to intense price competition. This competitive bidding process could affect the profit margins.
- Delays in completion of the current contracts or complying with contract schedules could have a material adverse effect on IRBD's cash flow position, revenues and earnings.
- IRBD's current operations are concentrated in two states of Maharashtra and Gujarat. Their strategy to expand their operations to other parts of India could pose additional risks like not gaining acceptance outside their current markets, obtaining necessary governmental and other approvals in time or at all.
- IRBD has recently forayed into real estate projects. It has limited experience in the real estate sector & no assurance can be given that it will be successful in the execution of real estate projects going forward. Also, at present, the real estate cycle is in the midst of downturn, which could delay IRBD's progress on this front.

- IRBD's interest rates on loans are linked to BPLR with annual reset clause. Any increase in the BPLR could increase its interest outflow & reduce its valuations, while a reduction in the interest rates could have a positive impact.
- IRBD is exposed to the risk of litigations from the Government agencies, other vendors, suppliers, land owners, etc. This could lead to a slowdown in the project execution & give rise to financial liabilities at times.

Competitive Profile:

IRBD is basically only into toll based BOT Road Projects. In the absence of any pure toll based peer, comparison becomes difficult. The build up of a mature portfolio of toll road assets generating stable and steady cash flows over the years gives the Company an edge over the infrastructure companies in somewhat similar line of business and poses as a high barrier to entry for new entrants. Being a fully integrated Company, carrying out operations of construction as well as O&M (operations and management), gives it better control on the costs and project time lines. One could compare IRBD with key Indian infrastructure developers & construction companies like L&T, Noida Toll Bridge, Gammon Infrastructure & GMR Infrastructure.

Results Update: (Consolidated)

Q4FY09: (Q-o-Q)

IRBD's consolidated Net Sales increased by 34.3% to Rs. 3.21 bn [Q4FY08: Rs. 2.39 bn]. The construction & BOT segments accounted for 61% & 39% respectively to the total Q4FY09 revenue. Lower traffic growth across the road projects & specifically on the Surat-Dahisar stretch, which commissioned in February suppressed the sales growth, which could have been much higher. EBITDA grew by only 18.7% on account of higher total expenditure as a % to net sales, which increased from 57.5% in Q3FY09 to 62.5% in Q4FY09. EBITDA margins declined from 42.5% in Q3FY09 to 37.5% in Q4FY09 due to contraction in the BOT segment margins from 85% in Q3FY09 to 70.9% in Q4FY09. This coupled with higher tax expense & minority interest in Q4FY09 (for 10% stake of Deutsche Bank) restricted the PAT growth to only 10.4%. PAT margins declined from 16% in Q3FY09 to 14% in Q4FY09.

FY09:

Consolidated Net Sales increased by 35.4% over FY08. Toll revenues grew by 22.9%, accounting for 44.5% to IRBD's total revenues. Construction business grew by 56.2%. Consolidated EBITDA grew by only 6.2%, while the margins declined from 56.2% in FY08 to 44.1% in FY09. This was on account of higher total expenditure as a % to sales, which increased from 43.8% in FY08 to 55.9% in FY09. However, marginal increase in depreciation by 12.6% & decline in the interest cost by 29.7% resulted in higher PAT growth of 54.4% in FY09 over FY08. Also the tax expenses declined by 5.5% over FY08 with the effective tax rate reducing from 24% to 17.6% due to higher profits from toll business, which are entitled to tax benefits under 80IA. PAT margins improved from 15.5% in FY08 to 17.7% in FY09.

Conclusion:

At the CMP of Rs. 154.5, IRBD trades at 29.2xFY09 & 18.2xFY10 EPS. The P/BV for FY09 & FY10E is at 2.9x & 2.5x respectively. The NPV per share under the toll business for FY10E comes to Rs. 86 assuming the traffic growth of 4% p.a & 6% p.a growth in the toll rates. However, this does not include the NPV from the Kolhapur business. The management expects it to be around Rs. 10. Adding this, the NPV sums up to Rs. 96. A study conducted by CII-NCAER shows that for every 1% increase in GDP, domestic passenger traffic increases by 1% & internationally road traffic increases by 1.3%. Assuming that Indian economy could grow atleast 6% going forward, the traffic growth should ideally be 6%. However, we have estimated the traffic growth on a conservative basis at 4%. The WACC has been taken at 10.6% for calculation of NPV (assuming the cost of equity at 13% & base case interest rate throughout the life of project at 10% with an estimated debt equity component of 4:1). The construction business is valued on PE basis & is expected to trade at 11xFY10E EPS, which comes to Rs. 27 per share. Hence summing up, the fair value of IRBD comes to Rs. 123 per share. However, the real estate business has not been taken into account for arriving at the fair value, since the development for the same is going to take around eight to ten years & there is uncertainly on when the revenue would start flowing. The table below gives an overview of fair value of IRBD arrived using the sum-of-the-parts method.

Business	Methodology	Assumption	Fair Value (Rs.)
Toll Business	DCF Basis	Toll & Traffic Growth taken 10%, WACC at 11%	96
Contruction Business	PE basis	Valued at 11xFY10E EPS	27
Total			**123**

We are positive on IRBDs integrated approach on the road BOTs and feel that the Company is well placed to capture the potential offered by road BOT projects in India. Going forward, the company expects to continue to receive orders for the toll based BOT projects rather than annuity based, where the margins are comparatively lower than in the toll business. The company has been pre-qualified for (or applied for) ~Rs. 280 worth of contracts, which will be up for bids in the next few months. In FY10, the company expects to receive new projects worth Rs. 40-50 bn.

Even though the fair value of IRBD comes to Rs. 123, which is much lower than the current market price, the stock could continue to command premium valuations on the anticipation of new projects likely to be awarded to the company, thus factoring in their potential benefits much earlier. IRBD has already obtained orders / L1 status worth Rs. 43 bn in the past one month. These could be compared with the major projects of IRBD like Mumbai-Pune, Thane-Ghodbunder, Surat-Dahisar, Surat-Bharuch & Kolhapur, which are worth Rs. 70 bn, taken into consideration for NPV purposes. The company could gain some more orders in the coming months & be a beneficiary of the Government's spend thrust (expected in the Union Budget). All these could lead to a significant appreciation in our estimated NPV from the current levels. Also, any uptick in the average traffic growth p.a. over and above our estimations of 4% could enhance our NPV estimations further.

Over the last three months, the stock has almost doubled. Even though we feel that it has more room for appreciation from current levels, the margin of safety is low. Hence, risk-averse investors could wait for an attractive entry point at around Rs. 120-130. However, short-term investors could buy the stock at current levels in anticipation of stock price reacting to the expected favourable budget announcements for sequential targets of Rs. 165 & Rs. 185 over the next two to three months.

Quarterly Financial Performance: (Consolidated)

(Rs. in Million)

Particulars	Q4FY09	Q3FY09	VAR [%]	Q2FY09	Q1FY09
Net Sales	**3211.0**	**2391.1**	**34.3**	**2016.1**	**2300.6**
Other Income	65.8	90.0	-26.9	81.7	58.5
Total Income	3276.8	2481.1	32.1	2097.8	2359.1
Total Expenditure	2006.2	1375.7	45.8	1031.2	1131.7
PBIDT	**1270.6**	**1105.4**	**14.9**	**1066.6**	**1227.4**
Interest	403.3	364.3	10.7	304.2	304.8
PBDT	867.3	741.1	17.0	762.4	922.6
Depreciation	330.9	286.2	15.6	271.5	255.3
Tax	100.9	72.5	39.2	78.8	125.6
Fringe Benefit Tax	0.0	0.0	0.0	0.0	0.0
Deferred Tax	0.0	0.0	0.0	0.0	0.0
Reported Profit After Tax	435.5	382.4	13.9	412.1	541.7
Minority Interest After NP	13.2	0.0	-	0.0	0.0
Net Profit after Min Int.	**422.3**	**382.4**	**10.4**	**412.1**	**541.7**
EPS	1.3	1.2	13.9	1.2	1.6
Equity	3323.6	3323.6	0.0	3323.6	3323.6
PBIDTM (%)	**37.5**	**42.5**	**-13.0**	**48.9**	**50.8**
PATM (%)	**14.0**	**16.0**	**-12.5**	**20.0**	**24.0**

(Source: Company)

Financial Estimations: (Consolidated)

Profit & Loss A/c

(Rs. Million)

YE March	FY07	FY08	FY09	FY10E
Net Sales	**3057**	**7327**	**9919**	**18157**
Other Income	194	520	296	350
Total Income	3251	7847	10215	18507
Total Operating Expenses	1403	3208	5545	10322
EBITDA	**1848**	**4639**	**4670**	**8185**
Interest	877	1958	1377	2880
Depreciation	526	1016	1144	1730
Profit Before Tax	445	1666	2150	3575
Tax (including FBT & DT)	148	400	378	629
PAT (before minority interest)	298	1266	1772	2946
Minority Interest	72.3	126.4	13.2	118.8
PAT (net of minority interest)	**226**	**1139**	**1759**	**2827**

(Source: Company, HDFC Sec Estimates)

Balance Sheet

(Rs. Million)

YE March	FY07	FY08	FY09	FY10E
Share Capital	2473	3324	3324	3324
Reserves & Surplus	1303	12883	14447	17080
Shareholders Funds	3775	16207	17771	20404
Minority Interest	1118	281.1	13.2	118.8
Secured Loans	22404	20110	24000	28800
Unsecured Loans	2776	103	0	0
Loan Funds	25180	20213	24000	28800
Deferred Tax Liability	0	26	0	0
Capital Employed	**30073**	**36727**	**41784**	**49322**
Gross Block	21193	22189	28189	41189
Less: Depreciation	2326	3340	4484	6214
Net Block	18868	18848	23704	34974
Capital Work in Progress	5552	8889	10000	2000
Investments	414	1985	550	550
Working Capital	5059	6989	7530	11798
Misc. Exp not w/off	181	16	0	0
Capital Deployed	**30073**	**36727**	**41784**	**49322**

(Source: Company, HDFC Sec Estimates)

Ratio Analysis

YE March	FY07	FY08E	FY09	FY10E
FD EPS (Rs.)	**0.7**	**3.4**	**5.3**	**8.5**
PE (x)	**227.7**	**45.1**	**29.2**	**18.2**
FD Book Value (Rs.)	11.4	48.8	53.5	61.4
P/BV (x)	13.6	3.2	2.9	2.5
EBIDTA (%)	54.1	56.2	44.1	43.2
PBT (%)	14.6	22.7	21.7	19.7
NPM (%)	7.4	15.5	17.7	15.6
ROCE (%)	4.4	9.9	8.4	13.1
RONW (%)	6.0	7.0	9.9	13.9
Debt-Equity	6.7	1.2	1.4	1.4
Mk. Cap. /Sales (x)	12.5	7.0	5.2	2.8
EV/EBITDA	36.4	15.6	16.2	9.6

(Source: Company, HDFC Sec Estimates)

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