



....em **POWER**ing the nation

A2Z: An Engineering Marvel

A2Z is engineering its way to success in the FMS, EPC and waste management solutions business. High growth strategy and government support makes the company's public offering quite attractive for investors with a long-term investment perspective

IPO of A2Z Maintenance & Engineering Services Ltd (A2Z) RECOMMENDATION: SUBSCRIBE

A2Z Maintenance & Engineering Services Ltd (A2Z) operates in facility management services (FMS) and engineering, procurement and construction (EPC) projects.

FMS includes engineering maintenance (mechanical, plumbing, electrical, HVAC, DG Set), energy-saving solutions, janitorial services, parking management, property lease management, telecommunication tower maintenance and security services to public and private sector clients.

Under EPC, the company provides services to the power transmission and distribution sector, with primary focus on the distribution segment. It is also diversifying into providing EPC services to power generation companies and companies in other sectors, including road and telecommunication.

A2Z has been operating the EPC business since fiscal 2006 and has historically focused on the power distribution sector. EPC services include the installation of distribution line infrastructure with capacities of up to 33 KV, the construction of substations of up to 33 KV and participation in system-strengthening projects and rural electrification projects.

In the power transmission sector, it has undertaken select EPC projects like the construction of extra high voltage (EHV) substations of up to 400 KV and EHV transmission lines of up to 765 KV. Its customers in EPC business are state power utilities and central public sector utilities such as PGCIL, NTPC and NHPC.

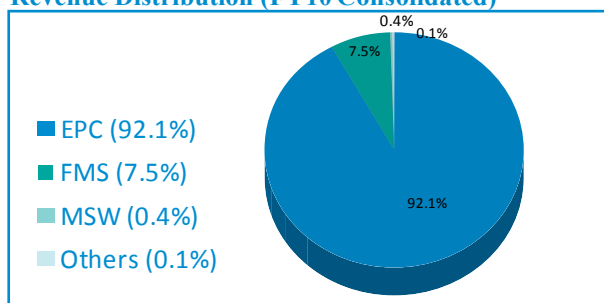
In addition to this, the company is diversifying its focus on to other businesses that include the following:

- Generating power from renewable energy sources
- Providing municipal solid waste management services (MSW)
- Developing information technology (IT) solutions for power utilities

The company's business operations are geographically spread across India.

The EPC segment revenue for FY10 was ₹1,123 crore comprising 91.6% of total revenue of the company. The Order Book for EPC business was ₹1,292 crore as on 31st Jul '10.

Revenue Distribution (FY10 Consolidated)



Source: RHP

INVESTMENT RATIONALE

Successful Execution Capability In Distribution EPC Business Is The Differentiator

A2Z derives over 90% of its revenue from the distribution EPC business. It has shown strong execution capabilities by successfully completing various distribution EPC contracts, wherein its competitors have failed. A2Z has been successful in managing and executing high working, capital intensive and difficult-to-implement ground-level distribution EPC contracts.

The direct implementation of projects instead of subcontracting has helped A2Z in completing projects on time and managing the working capital cycle. Apart from this, A2Z has also grown this business from ₹35 crore in FY06 to over ₹1,100 crore in FY10.

Integrated Approach To Municipal Solid Waste (MSW) Management To Drive Profitability

A2Z started the municipal solid waste business in the year 2008 and received initial success in its integrated approach to the MSW business. The integrated contract involves door-to-door collection, transportation to the disposal site, processing the waste and capturing various materials like plastic, metal, glass, etc for recycling; sand for manufacturing bricks; producing composites (organic fertilizer) for sale and Refuse Derived Fuel (RDF) to be used as fuel for power plants.

It started its first processing plant in Kanpur in October '10, which will capture the full benefit of the value chain of municipal solid waste. A2Z is further integrating the MSW business at Kanpur by setting up a 15 MW biomass power plant to utilize RDF as fuel for the same. Encouraged by its initial success in the municipal solid waste business, A2Z has adopted an aggressive growth

strategy and has already taken up 20 contracts in different cities to manage 5,565 tonnes of municipal waste per day. We feel that over the next two to three years, this business will grow manifold and will be the key value driver for the company.

Multi-fuel Biomass Power Plant Structure And Fuel Security Through Integration Will Make The Biomass Power Plant Highly Successful.

The basic problem of single fuel biomass power plant is low availability of fuel, availability in part of the year, rising cost of fuel, etc. By using multi-fuel plant structure (used for the first time in India), the company can run this power plant throughout the year. Further, by integrating the biomass power plant with municipal solid waste or rice processing mill, the company will secure fuel supply at lower costs.

The company is setting up various small biomass power plants of 10 MW to 15 MW capacities, aggregating to 285 MW. Of these, four power plants are expected to be commissioned by March '11, five by October '11 and one plant of 10 MW is expected to start in December '11. The successful implementation of these power plants will help A2Z to diversify its revenue base.

Upcoming Biomass Power Plants

Power Plant	State	Fuel	Commission Month	Project Cost	Amount Invested
3X15MW (45MW)	Punjab (BOOT, in sugar Mill)	Bagasse	March '11	246.03	49.72
15MW	UP, Kanpur	RDF from MSW business	March '11	85.00	16.36
5X15MW (75MW)	Rajasthan	Crop residue	October '11	400.00	0.27
10MW & Rice mill	Punjab	Husk from captive rice mill	December '11	102.33	1.80

Source: RHP

The Company Is Growing Its Business In High-growth Industries And Is Supported By The Government

Power distribution loss of over 30% - 40% is a big concern for India and the government is aggressively looking to bring down these losses. To achieve the same, the government is consistently coming up with policy measures like Restructured Accelerated Power Development and Reforms Programme (R-APDRP) to improve the situation. In solid waste management, the government has come up with various incentive schemes under programmes like National Urban Renewal Mission (NURM) to encourage private sector participants in waste management.

Likewise, the government has mandated all states to generate 5% - 10% of power from renewable sources of energy. Government support and enough opportunity in the target industry will keep the company's growth momentum intact.

Consolidated Financials

Profit And Loss (₹ in Crore)	FY08	FY09	FY10	4MFY11
Revenue	479.0	715.7	1219.3	415.6
Growth	165%	49%	70%	2%
Operating Profit	88.3	126.9	200.7	74.5
Operating Margin	18.4%	17.7%	16.5%	17.9%
Interest	12.5	38.8	49.3	19.4
Depreciation/Amortization	1.3	2.0	3.6	2.8
Other Income	2.3	8.2	6.0	2.5
Net Profit Before Tax	76.9	94.3	153.8	54.9
Tax	27.0	35.3	55.6	20.1
PAT	49.8	59.1	98.2	34.8
PAT Margin	10.4%	8.3%	8.1%	8.4%
Exceptional	0.0	0.0	0.0	-8.7
PAT	49.8	59.1	98.2	26.1
Minority Interest	0.0	0.0	0.4	0.0
Net profit	49.8	59.0	97.9	26.1
Balance Sheet (₹ in Crore)	FY08	FY09	FY10	4MFY11
Net Fixed Assets	12.2	21.8	54.8	91.3
Capital Work-in-progress (including capital advances)	0.0	13.6	84.6	55.1
Investments	0.0	0.0	0.0	0.0
Deferred Tax Assets (Net)	1.2	2.3	4.6	10.1
Current Assets, Loans And Advances	473.2	757.8	1209.1	1235.0
Current Liability And Provision	197.6	307.8	531.4	389.8
Net Current Assets	275.7	450.0	677.7	845.2
Misc Expenditure	0.0	0.0	6.8	17.0
Total Capital Deployed	289.0	487.7	828.5	1018.8
Loan Fund				
Secured Loans	124.7	244.3	404.8	569.9
Unsecured Loans	0.1	20.0	0.4	1.7
Total Loan Fund	124.9	264.3	405.2	571.6
Minority Interest	0.0	0.2	2.2	2.6
- Equity Shares	19.1	21.6	57.3	57.3
- Preference Shares	75.0	0.0	0.0	0.0
Reserves & Surplus	70.0	201.6	363.8	387.3
Total Fund Employed	289.0	487.7	828.5	1018.8
Ratios	FY08	FY09	FY10	4MFY11
EPS	23.02	27.28	17.08	18.22*
Book Value	75.84	103.12	73.49	77.59
Return On Equity	30.4%	26.5%	23.2%	23.5%*
Return On Capital Employed	21.6%	20.1%	17.8%	16.0%*
Debt Equity	0.76	1.18	0.96	1.29

Source: RHP *Annualized

RECOMMENDATION

A2Z is operating in an emerging and high-growth industry and has shown rapid growth capabilities in the past. Execution capability in the distribution EPC business, emerging opportunities in solid waste management and high growth planned in the renewable energy business, supported by government policy, will drive growth for A2Z.

At the upper band of ₹410, though the shares seem to be offered at a higher PE multiple of 24 on historic earnings of FY10, we feel the multiple on forward earnings will be attractive due to growth in all its businesses.

We recommend investors to subscribe to the company's initial public offering with a long-term perspective. The issue opens on 8th December '10 and closes on 10th December '10.



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