

Sobha

7 February 2019

Reuters: SOBH.NS; Bloomberg: SOBHA IN

Concern Over Rising Debt And Decline In Operational Cash Flow

Despite the strong growth in earnings of Sobha in 3QFY19, we are concerned over the sharp decline in cash flow after income tax and interest expenses by 20% QoQ and 65% YoY to Rs191mn. Consequently, net debt increased to Rs23,999mn, an increase of 7% QoQ. The weak cash flow is partially because of rising advertising, marketing and interest expenses following pricing pressure in a weak market. We also note that sales in 3QFY19 were muted compared to earlier quarters, despite being a festival season. We have retained our Sell rating on Sobha with a target price of Rs376.

Operating profit growth driven by rise in revenues: Revenues in 3QFY19 stood at Rs7,879mn, up 19.6% QoQ and 13.9% YoY. EBITDA margin was at 20.2%, a rise of 31bps YoY and a decline of 110bps QoQ. EBITDA rose 13.4% QoQ and 15.6% YoY. Other income at Rs198mn increased 13.1% QoQ and 133% YoY. Rise in other income supported earnings growth of 30.7% YoY and 13.7% QoQ to Rs698mn.

Sales volume declines 12% QoQ and 2.6% YoY which is surprising: Sobha reported sales volume of 0.91mn sqft in 3QFY19, representing a decline of 2.6% YoY and 12% QoQ, despite being a festival season.

Average realisation rises to Rs6,604/sqft: Sobha reported average realisation of Rs6,604/sqft, up 10.4% QoQ and flat on YoY basis. Sales value at Rs6,002mn declined 3% QoQ and 2% YoY on account of poor sales volume.

Rise in net debt is a cause for concern: Sobha reported net debt of Rs23,999mn in 3QFY19, higher than Rs23,652mn in 2QFY19 and Rs23,276 in 3QFY18. The rise in debt in a weak residential estate environment raises concerns.

Sharp decline in net operational cash flow after tax and interest costs: Net operating cash flow after tax and interest costs was Rs191mn in 3QFY19, a decline of 20% QoQ and 65% YoY. The decline in net operational cash flow was because of: 1) Rise in advertising and marketing expenses by 71.2% YoY and 32% QoQ to Rs 262mn in 3QFY19. 2) Interest expenses at Rs742mn rising 6% QoQ and 17% YoY in 3QFY19. 3) Higher cost of contractual business relative to cash inflow in the business.

Plans launch of 7.7mn sqft in the next three to four quarters: Sobha plans to launch 7.7mn sqft in the next three to four quarters. Launches are expected in the following cities: Bengaluru – 4.35mn sqft, Thrissur – 1.34mn sqft, GIFT City (Gujarat) – 0.47mn sqft, Coimbatore – 0.11mn sqft, Chennai – 0.92mn sqft, and Pune – 0.51mn sqft.

Retain Sell rating with a target price of Rs376: Rich valuation amid lack of pricing power and rising costs will exert pressure on the stock price. We have retained Sell rating on Sobha with a target price of Rs376.

SELL

Sector: Real Estate

CMP: Rs480

Target Price: Rs376

Downside: 22%

Amit Agarwal

 Research Analyst
 amit.agarwal@nirmalbang.com
 +91-22-6273 8033

Akash Mehta

 Research Associate
 akash.mehta@nirmalbang.com
 +91-22-6273 8062

Key Data

Current Shares O/S (mn)	94.8
Mkt Cap (Rsbn/US\$m)	45.6/636.9
52 Wk H / L (Rs)	590/380
Daily Vol. (3M NSE Avg.)	190,933

Price Performance (%)

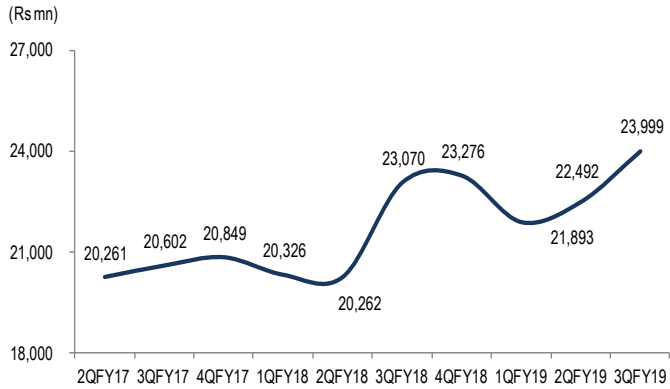
	1 M	6 M	1 Yr
Sobha	9.1	(0.8)	(11.9)
Nifty Index	3.1	(2.9)	5.4

Source: Bloomberg

Y/E March (Rsmn)	3QFY19	2QFY19	QoQ (%)	3QFY18	YoY (%)	3QFY19E	Var. (%)
Net sales	7,879	6,587	19.6	6,919	13.9	6,930	13.7
Cost of goods	(4,613)	(3,270)	41.1	(4,250)	8.5	(3,510)	31.4
Employee benefits expenses	(588)	(598)	(1.7)	(473)	24.3	(610)	(3.6)
Other expenses	(1,088)	(1,317)	(17.4)	(821)	32.5	(1,343)	(19.0)
EBITDA	1,590	1,402	13.4	1,375	15.6	1,467	8.4
EBITDAM (%)	20.2	21.3	-	19.9	-	21.2	-
Depreciation and amortisation	(161)	(154)	4.5	(137)	17.5	(162)	(0.6)
EBIT	1,429	1,248	14.5	1,238	15.4	1,305	9.5
EBITM (%)	18.1	18.9	-	17.9	-	18.8	-
Other income	198	175	13.1	85	132.9	175	13.1
Interest expenses	(531)	(532)	(0.2)	(498)	6.6	(543)	(2.2)
Extraordinary/exceptional items	-	-	-	-	-	-	-
Profit before tax	1,096	891	23.0	825	32.8	937	17.0
Tax expenses	(398)	(277)	-	(291)	-	(309)	-
Effective tax rate (%)	36.3	31.1	-	35.3	-	33.0	-
Reported net profit	698	614	13.7	534	30.7	628	11.1
NPM (%)	8.9	9.3	-	7.7	-	9.1	-

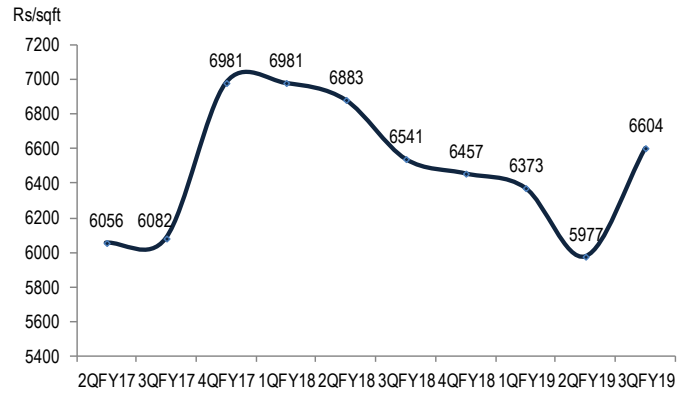
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 1: Net debt



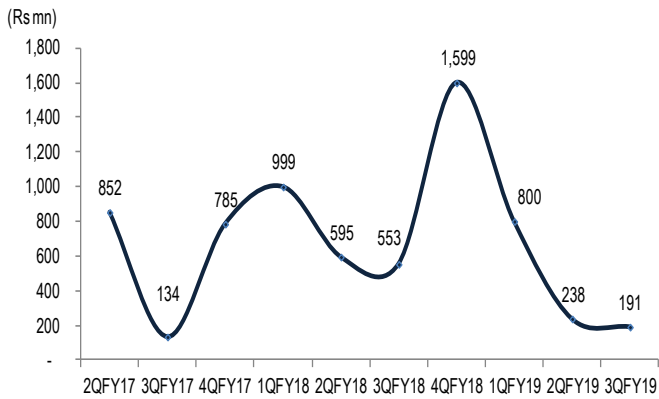
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 2: Average sale price



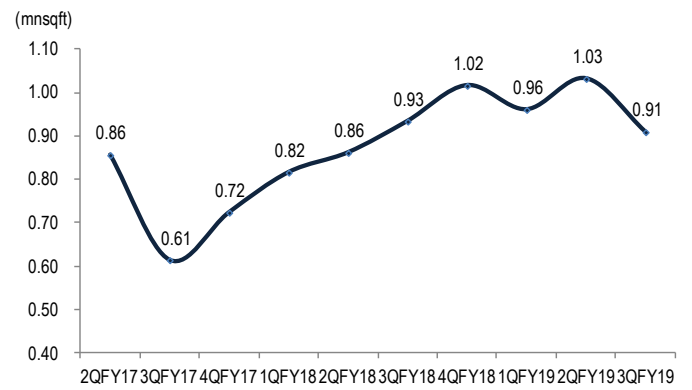
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 3: Net operating cash flow after interest costs and tax



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 4: Average sale volume



Source: Company, Nirmal Bang Institutional Equities Research

Consolidated financials

Exhibit 5: Income statement

Y/E March (Rsmn)	FY17	FY18	FY19E	FY20E	FY21E
Net sales	22,420	27,830	26,247	28,147	31,789
Growth YoY (%)	15.2	24.1	(5.7)	7.2	12.9
Operating costs	13,020	16,800	14,223	14,817	17,390
Staff expenses	1,779	1,985	2,084	2,188	2,298
Other expenses	3,294	3,848	4,040	4,242	4,454
EBITDA	4,327	5,197	5,899	6,899	7,648
EBITDA growth (%)	(3.0)	20.1	13.5	17.0	10.8
EBITDA margin (%)	19.3	18.7	22.5	24.5	24.1
Depreciation	638	544	544	544	544
EBIT	3,689	4,653	5,355	6,355	7,104
EBIT (%)	16.5	16.7	20.4	22.6	22.3
Net interest expenses	1,450	1,646	1,760	1,913	2,238
Other income	340	164	173	181	190
Earnings before tax	2,578	3,171	3,768	4,624	5,056
Tax- total	970	1,003	1,191	1,462	1,298
Rate of tax (%)	37.6	31.6	31.6	31.6	25.7
Net profit	1,608	2,169	2,576	3,162	3,758

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 7: Balance sheet

Y/E March (Rsmn)	FY17	FY18	FY19E	FY20E	FY21E
Share capital	963	948	948	948	948
Reserves and surplus	25,482	26,751	29,394	32,327	35,857
Net worth	26,445	27,699	30,342	33,275	36,806
Loans	22,219	23,313	27,313	29,813	34,313
Minority interest	-	-	-	-	-
Deferred tax liability	2,283	2,521	2,521	2,521	2,521
Total capital employed	50,948	53,533	60,176	65,609	73,640
Net fixed assets	5,952	6,103	5,559	5,015	4,471
Goodwill	-	-	-	-	-
Investments	-	1,125	1,125	1,125	1,125
Current assets loans & adv.	82,958	83,072	93,610	102,150	113,175
Inventories	50,960	48,349	54,036	60,326	68,828
Debtors	2,410	3,407	3,990	4,280	4,833
Cash and bank	1,659	1,353	1,852	1,166	258
Loans and advances	20,178	22,187	24,366	26,810	29,172
Current investments and others	7,751	7,775	9,366	9,567	10,084
Less: Current liab. & prov.	37,983	36,821	40,172	42,734	45,185
Current liabilities	37,278	36,045	38,339	40,630	43,245
Provisions	704	775	1,833	2,104	1,940
Net current assets	44,975	46,251	53,438	59,416	67,990
Miscellaneous	-	-	-	-	-
Deferred tax assets	21	54	54	54	54
Total capital employed	50,948	53,533	60,176	65,609	73,640

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 6: Cash flow

Y/E March (Rsmn)	FY17	FY18	FY19E	FY20E	FY21E
Profit after tax	1,608	2,169	2,576	3,162	3,758
Depreciation	638	544	544	544	544
Other income	(340)	(164)	(173)	(181)	(190)
Working capital changes	(1,598)	(1,581)	(6,690)	(6,663)	(9,483)
Operating cash flow	308	968	(3,742)	(3,139)	(5,370)
Capital expenditure	(410)	(695)	-	-	-
Investments	294	(1,125)	-	-	-
Cash flow from investments	(116)	(1,820)	-	-	-
Equity	(18)	(15)	-	-	-
Debt	417	1,093	4,000	2,500	4,500
Others	(157)	(304)	468	181	190
Dividends	(232)	(229)	(229)	(229)	(229)
Cash flow from financing	10	546	4,239	2,453	4,462
Total cash generation	202	(306)	497	(686)	(908)
Opening cash balance	1,457	1,659	1,355	1,852	1,166
Closing cash & bank balance	1,659	1,353	1,852	1,166	258

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 8: Key ratios

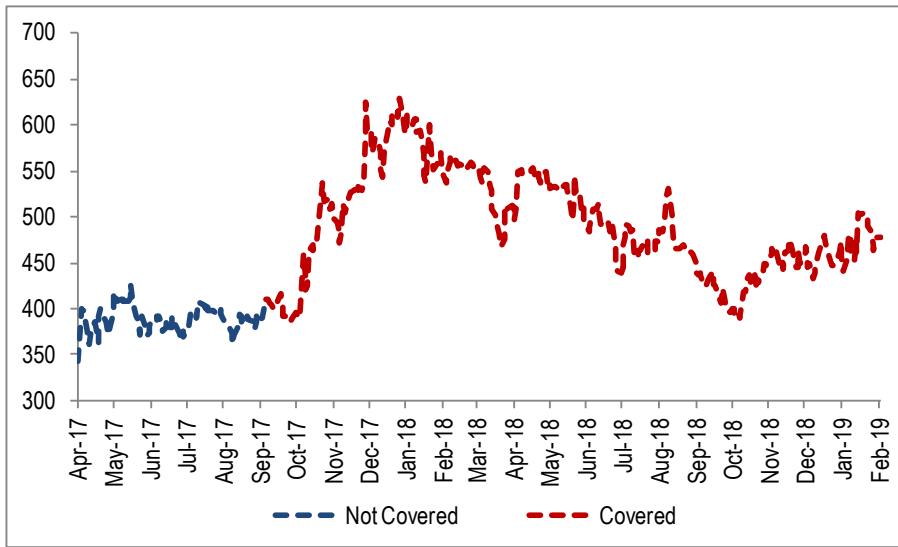
Y/E March (Rsmn)	FY17	FY18	FY19E	FY20E	FY21E
Profitability and return ratios					
EBITDA margin (%)	19.3	18.7	22.5	24.5	24.1
EBIT margin (%)	16.5	16.7	20.4	22.6	22.3
Net profit margin (%)	7.2	7.8	9.8	11.2	11.8
RoE(%)	6.1	7.8	8.5	9.5	10.2
RoCE (%)	8.5	9.7	9.8	10.5	10.4
Working capital & liquidity ratios					
Receivables (days)	39	45	55	56	55
Inventory (days)	830	634	751	782	790
Payables (days)	216	184	199	219	209
Current ratio (x)	2.2	2.3	2.3	2.4	2.5
Valuation ratios					
EV/sales (x)	2.9	2.4	2.7	2.6	2.5
EV/EBITDA (x)	15.3	13.0	12.0	10.8	10.4
P/E (x)	28.7	21.3	17.9	14.6	12.3
P/BV (x)	1.7	1.6	1.5	1.4	1.2

Source: Company, Nirmal Bang Institutional Equities Research

Rating track

Date	Rating	Market price (Rs)	Target price (Rs)
7 September 2017	Sell	401	295
14 November 2017	Sell	503	295
14 February 2018	Sell	561	363
22 May 2018	Sell	509	363
8 August 2018	Sell	496	363
13 November 2018	Sell	450	376
7 February 2019	Sell	480	376

Rating track graph



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Stock Ratings Absolute Returns

BUY > 15%

ACCUMULATE -5% to 15%

SELL < -5%

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Team Details:			
Name		Email Id	Direct Line
Rahul Arora	CEO	rahul.arora@nirmalbang.com	-
Girish Pai	Head of Research	girish.pai@nirmalbang.com	+91 22 6273 8017 / 18
Dealing			
Ravi Jagtiani	Dealing Desk	ravi.jagtiani@nirmalbang.com	+91 22 6273 8230, +91 22 6636 8833
Pradeep Kasat	Dealing Desk	pradeep.kasat@nirmalbang.com	+91 22 6273 8100/8101, +91 22 6636 8831
Michael Pillai	Dealing Desk	michael.pillai@nirmalbang.com	+91 22 6273 8102/8103, +91 22 6636 8830

Nirmal Bang Equities Pvt. Ltd.

Correspondence Address

B-2, 301/302, Marathon Innova,
 Nr. Peninsula Corporate Park,
 Lower Parel (W), Mumbai-400013.
 Board No. : 91 22 6273 8000/1; Fax. : 022 6273 8010