



## Punj Lloyd Limited

### Investor/ Analyst Conference Call Transcript For Q2FY2012 Results

November 8, 2011

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**Moderator:** Ladies and Gentleman, Good day and Welcome to the Punj Lloyd Q2 and H1 FY2012 Earnings Conference Call. As a reminder for the duration of this conference, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions at the end of today's presentation. Should you need assistance during this conference call, please signal an operator by pressing \* and then 0 on your touch tone telephone. Please note that this conference is being recorded. At this time, I would like to hand the conference over to Ms. Sameera Kedar from CDR India. Thank you and over to you.

**Sameera Kedar:** Welcome everybody to the Punj Lloyd Q2 and H1 FY12 Earnings Conference Call. I trust you all have received the Quarterly results and Investor Communique. To recap on the company's financials for Q2FY12, consolidated revenues stood at ₹ 2,460 core, increase by 24% YOY, EBITDA at ₹ 270 crore increase by 45% YOY, and PAT at ₹ 29 crore increase by 43% YOY. The value of the order backlog as on date is ₹ 26,690 crore. Before we begin, I would like to mention that some statements made during this call may be forward looking in nature and a disclaimer to this effect has been sent to you with the conference call invitation. Also I would like to emphasize that while this call is open to invitees; it may not be broadcasted or reproduced in any form or manner. I would now like to hand over to Mr. Anil Jain, Head - Investor Relations, to introduce the management. Over to you Mr. Jain.

**Anil Jain:** Good afternoon everyone. On behalf of Punj Lloyd, we welcome you all to the 2<sup>nd</sup> Quarter Earnings conference call, post release of quarterly financial results yesterday. With me the entire management of Punj Lloyd is here. Let me introduce all the management team members, who are available for this call. Mr. Atul Punj, Chairman, Mr. Luv Chhabra, Director (Corporate Affairs), Mr. P K Gupta, Whole Time Director, Mr. Atul Jain, President & Joint CEO (Middle East, Africa & CIS), Mr. Ravindra Kansal, President & Joint CEO (Middle East, Africa & CIS), Mr. Pradeep Tandon, President & CEO – Building & Infrastructure (Middle East & Africa) & Mr. Raju Kaul, Group CFO &. We now invite investors to raise queries and begin the Q&A session.

**Moderator:** We have the first question from the line of Pritesh Chheda from Emkay Global.

**Pritesh Chheda:** We have seen margins getting stabilized around 8% from last two to three quarters. Further, on the debt side, there has been continuous addition. What is the debt outlook, going forward?

**Luv Chhabra:** The composition of the debt is largely working capital in nature, which is dependent on the project cycle. There has been an increase in our debt owing to, significant delays by a number of clients in India, particularly the Government owned companies, in releasing payments and we hope that the situation will normalize over the next three to six months. Our total debt levels will come down when the revenue significantly increases with robust profits, which will reduce the debt.

**Pritesh Chheda:** What is the outlook on the margins in the new orders worth ₹ 10,286 crores, which have been won in H1? How they are placed compared to the existing margin?

**Luv Chhabra:** We don't give any specific guidance, but our outlook is that it will be around the current level.

**Pritesh Chheda:** Lastly on the FX side, whether there is any FX impact in the current quarter and if you could also tell us, what has been the FX impact in the same quarter last year?

**Luv Chhabra:** Raju you can give the details, but my understanding is that on the balance sheet side, there is a benefit of approximately ₹ 60 crore, which has been included in Reserves and Surplus.

**Pritesh Chheda:** What is the impact on the P&L side?

**Raju Kaul:** On the P&L side, I don't have the exact numbers in hand now. However, we can provide you this information subsequent to the concall.

**Pritesh Chheda:** In the current order backlog, what is the amount of Libya's order backlog in terms of value?

**Raju Kaul:** ₹ 3,899 crores, on account of Building & Infrastructure.

**Pritesh Chheda:** Are there any developments on any of the Auditor's qualifications?

**Luv Chhabra:** There are two significant qualifications, one on Libya. Mr. Punj will provide his views in brief as to how the Libyan situation will evolve. The other major qualification is on ONGC Heera project. We have already mentioned in the last two quarterly concalls that it will take about two to two & half years to finally conclude this matter. However, the process of arbitration has already commenced.

**Pritesh Chheda:** No developments from last quarter to the current quarter?

**Luv Chhabra:** Yes, hearings have taken place and we have submitted our claims to the arbitrators. Now ONGC will submit their rebuttal and then we will be given time to submit our rejoinder to ONGC's rebuttal. Then hearings will take place again. Possibly the experts would also be invited for giving their views on the claims. This entire process is expected to be carrying on for about two to two and half years.

**Raju Kaul:** It may be also worth mentioning here that the quantum of the auditor's qualification in respect of Heera has come down by ₹ 62 crore in the second quarter on account of expiry of advance payment bank guarantee.

**Moderator:** The next question is from the line of Naveen Jain from JM Financial.

**Naveen Jain:** It appears from the balance sheet that in the first half we have done a Capex of around ₹ 400 crore, what is this Capex meant for and secondly what is the total Capex planned for the full year?

**Atul Punj:** Our Capex spends is linked with the projects that we win. We are not building up the Capex in anticipation of orders. So, whenever we win a project, we check first the availability of existing equipment and if not available, we analyse the option between taking it on rent vs. buying of equipment. This is largely the guiding factor of any Capex decision. The Capex spend numbers move based on the project wins in different business verticals.

**Naveen Jain:** What is the outlook for the Capex for the full year, as we have seen spend of almost ₹ 400 crore in the first half.

**Luv Chhabra:** First half year capex is below ₹ 400 crore and it will really depend on the nature of contracts and the geographies where these projects are won. As Mr. Punj explained, if it is economical and cheaper to hire equipment in these geographies or there is availability of adequate internal equipment, those equipment will be utilized and if neither of these options exist, only then we will go in for purchasing of equipment.

**Naveen Jain:** Generally we do not basically focus too much on the standalone results. Consolidated results are primarily looked at. But the margins in the standalone results have dropped quite a bit. Should we consider it as a sign of Indian businesses not doing well or lower or falling margins, Is it a correct interpretation, sir?

**Luv Chhabra:** I don't know from where you have gathered these numbers. In the published results, the EBITDA margin have gone up compared to last quarter. But your other observation about Indian businesses is possibly correct. We are witnessing an acute competitiveness in certain sectors in India. There is a very high level of competitive intensity particularly on the road sector or some of the other

infrastructure sectors. This is also evident from the fact that there are 14-15 bidders for even very large projects in the range of USD 750 million or a billion dollars. Even, on the oil and gas sector, we are seeing an increased level of competitiveness. Therefore, our focus will continue to be in the larger international markets, where we believe the margins are more robust and where we have not seen a drop in our EBITDA margins.

**Naveen Jain:** When I am talking about EBITDA margin, I am not considering other income; probably the one you are talking about is inclusive of other income which was about ₹ 112 crore in this quarter on the standalone basis. So I also wanted to understand what is this ₹ 112 crore other income. Is it largely Forex gain?

**Anil Jain:** Logically, Forex gains should be considered part of operating income only. If we look at the international operation of the businesses, it cannot really be called an other ancillary income. The rightful approach would be to take it into account in the business revenue and then to calculate EBITDA margins to arrive at a real conclusion.

**Naveen Jain:** Does it mean that volatility in the foreign exchange is basically part of your core business itself?

**Luv Chhabra:** Basically, it's a translation risk depending upon the geography and the currency movement in those geographies. In some quarters, the forex loss/gain will come down and in some quarters it will go up and this will keep on changing on quarter to quarter basis. We are operating in 20 countries. In case of standalone balance sheet, the businesses in the Middle East and Libya have been considered, as we are operating in these countries through branch offices of Punj Lloyd, India.

**Naveen Jain:** You have invested approximately ₹ 15 crore in Punj Lloyd Infrastructure Ltd., an infra holding company. Which are these projects and which other SPV's you will be investing in, going forward?

**Luv Chhabra:** Punj Lloyd Infrastructure currently has two projects; one is road project - Khagaria Purnea which is on an annuity basis and the other one is 5 MW Solar power project in Rajasthan. Both these projects will be developed through special SPVs, and the money flows in from Punj Lloyd infrastructure into the equity of these SPVs.

**Moderator:** The next question from the line of Srinivas Rao from HDFC Mutual Fund.

**Srinivas Rao:** Can you tell us are we going to have higher margins in the new orders compared to the existing margin that have been reported?

**Luv Chhabra:** We have already answered this question earlier. We don't give specific guidance on orders and the specific margins. We expect the margins to be in line with what the margins are on our existing projects.

**Srinivas Rao:** We are in the impression that currently the margins are getting lower in the new businesses. The margins that have been reported is in the range of 9.5 to 10%, so I am just trying to understand whether you are taking new orders at these levels or lower levels?

**Atul Punj:** If you look at our bidding strategy in the recent past, we have not been successful in winning projects in the highway sectors and the reason for this is that we are not compromising on the margins to win projects. We are looking to maintain consistency of the margins across all verticals in the group. I think you have seen that we have been exercising lot of restraints and we do not want to just win orders for the sake of winning it. The geographic spread of our recent wins will demonstrate to you as to how we have strategized to de-risk ourselves by having diverse deals to choose from in order to maintain a minimum level of expected margin.

**Srinivas Rao:** Earlier your margin seems to be in the range of 9.5 to 10%. Given the current competitive environment, will it not be fair to assume that, these kind of margins are not sustainable?

**Atul Punj:** I don't think that would be a fair assessment.

**Srinivas Rao:** Whether there is any one time income in the second quarter, which has been included in the other income of ₹ 67 crore?

**Raju Kaul:** Other income comprises of FX gains, Interest income, some liabilities write back, which is part and parcel of every quarter. Therefore, there is nothing like one time income in the other income.

**Srinivas Rao:** What will be the current utilization of the equipment?

**Raju Kaul:** Of all our equipment?

**Srinivas Rao:** Yes if you can give us the sense in terms of the overall utilization rate. How it is moving for you? PI also tell us specifically about offshore assets.

**Luv Chhabra:** There is a variety of equipment in our portfolio. Some equipment is used in a project only a few times during the duration of a project, but these are equipment which are very difficult or almost impossible to get on hire eg take the case of some very heavy duty cranes which are used to install heavy pressure vessels in a refinery project, such equipment would probably be used for couple of times in a two year project. So it depends on the nature and type of equipment. About offshore assets, I think Mr. Gupta can give you a clear indication.

**P. K. Gupta:** Right now our equipment is fully utilized, We are doing lots of pipeline projects which is equipment intensive. In a typical pipeline project, the utilisation rate is around 70% to 80% level and as far as offshore assets are concerned, we are now utilizing all our assets.

**Raju Kaul:** In fact in this second quarter, we have paid around ₹ 70 crore towards hire charges for hiring of equipment.

**Anil Jain:** If we are getting you correctly, you seem to be more interested in knowing about the current utilization status of offshore assets?

**Srinivas Rao:** Yes I was just trying to understand the utilisation of offshore equipment as well as overall.

**Luv Chhabra:** With the large order backlog this equipment is pretty well utilized.

**Moderator:** The next question is from the line of Indrajeet from Macquarie Capital Advisors.

**Indrajeet:** Historically you have taken lot of road projects in tie up with GMR where we used to hold a minority stake till the time of construction. GMR has off-late won very big ticket size contract so is it a possibility that you will enter into some kind of agreement with them to take the EPC contracts for those road projects? If you could comment on what kind of competitive intensity you are seeing for orders in India both on the civil construction side and also what kind of pipeline you are seeing from ONGC or the other oil companies in India and what kind of competitive pressures are also there?

**Atul Punj:** Well on the first question on GMR, we are in dialogue with GMR for doing some of the construction work, but all will depend upon whether the price is acceptable or not to both the sides. Thus, it's a 50-50 chance whether we will take up or not. But the discussions are going on. The second question was about competitiveness. In India this is rising as Mr. Chhabra mentioned few moments ago. We are currently operating in 20 geographies. We feel a lot more comfortable than if we were only in an India specific operation. The third point about oil and gas, the process side is running a bit slow, but ONGC on the offshore side has about almost ₹ 8,000 crore worth of orders, which are going to be decided in the next six months and we are well-positioned hopefully for a significant part of that. Competitive pressures on the offshore side are there but obviously less than the highway side. So overall I think we are in a comfortable place, simply because of our global diversification and the equipment & the assets that we have particularly on the offshore side.

**Indrajeet:** If you look at Middle East, there have been a lot of talk about Capex on the process side and the petrochemical side and at some point of time, Punj Lloyd was also interested in partnership with some of these very large global companies looking at these very big ticket size orders, are those strategies still on the table, are you still looking at those kind of multibillion dollar kind of contracts or those kind of orders are available at the first place itself that's one and the second is just a kind of question on the financial side. If by any chance we need to take some kind of write off or, would there be any kind of trigger on some of the financial covenants on the debt side because our debt equity is already 1:1. What's the kind of plan B in case if there is some write-off on some of those auditor's qualifications?

**Atul Punj:** On the petrochemical projects of large sizes there are projects that are going on in places like Qatar and Saudi Arabia. We are participating in some of those tenders and would continue to do so. We are now qualified for a number of bids in Iraq, which is a major opportunity country for us. The large petrochemical business will come, but there are billions of dollars which are being invested now in social infrastructure in the Middle East region..... an interesting position for us particularly in view of the recent political development in the region. So there would be a greater increase of infra projects, whereas the petrochemical projects are normally linked with the commodities cycle, which influences the client decision to kick start the project.

**Luv Chhabra:** Regarding your second question, we should analyse the situations from our two large projects on which we have qualification. The first one is Heera. We have explained this before that while our qualification is for approximately ₹ 243 crore, our claims on ONGC are over ₹ 1,300 crore. We are confident that we will recover through the process of arbitration or even if it's necessary subsequently through Courts, much more than what has been provided in the qualification. Therefore, we don't believe that there is any requirement of any kind of provisioning here. The second big one is Libya; you must understand that this is not a situation created by us. It's a situation of political and civil unrest and hopefully things are expected to stabilize or normalize over the next few months. We have remained in that country well after the political unrest started and we continued working on the projects and we have also invoked force majeure because of the political unrest. So I don't believe that there is any requirement of any provision on any of these contracts. In our view, after restoration of normalcy, that country will move ahead and start rebuilding, commencing with the oil and gas projects and then moving on to the infrastructure projects. We expect to see some movement on revival of our projects over the next few months.

**Atul Punj:** Let me just add a bit on the Libya situation. You have to understand that the National Transition Council had to give an undertaking to the United Nation that they would honor all commitments entered prior to this chaos breaking out. So this is a commitment by the Transition Council to the United Nations. We have already been having dialogues with some of our clients and there is no write-off really that we are expecting to take in Libya at all. So it was a deferment of revenues and of course profits along with it and as Mr. Chhabra also mentioned oil and gas will come back then the infra will come back.

**Indrajeet:** No, I think your point about some of these claims from your side could actually turnout to be of favor in the due course, my question is just from a financial point of view, whether our debt agreement carries any of those typical financial covenants like debt equity etc. Even if, there is something for a short term, there could be an issue on that front? Though you say in the next two years or so you might recover funds from the ONGC, but in the short term that might trigger of a kind of dilution or substantially higher interest rates?

**Raju Kaul:** No it will not, as the financial covenants are generally there in terms of DSCR & Interest Coverage and not for debt equity.

**Moderator:** The next question is from the line of Mukul from Goldman Sachs.

**Mukul:** In your Q2 results, there is a reclassification of about ₹ 63 crore in Q1FY11 from other operating income to other income, can you tell us the reason for this reclassification and the heads which have changed?

**Raju kaul:** This time the auditors have felt that this other income should be actually shown below the line, and that's why this reclassification. As far as we are concerned, this is very much part of the other operating income for us.

**Mukul:** Which part is related to us?

**Raju Kaul:** Interest, some liabilities write back and something on account of Forex gain or loss.

**Moderator:** The next question from the line of Parikshit Kandpal from Karvy.

**Parikshit Kandpal:** I just wanted to know the update on your Bihar EPC water treatment project, which you were doing? What was the earlier time lines and have you completed this project? And is there any cost overrun on this project?

**Atul Punj:** There is no cost overrun on this project. The project is moving ahead. I think we will deliver by the end of this calendar year about 100 sites and it's pretty much moving on track.

**Luv Chhabra:** 100 sites are in addition to what we have already delivered. The total project is about 855 sites and out of which, between 170 and 200 is expected to be completed by the end of this financial year and the balance will get completed towards next year when the entire project is supposed to be completed.

**Parikshit Kandpal:** So there was no time overrun on this project?

**Atul Punj:** No.

**P.K. Gupta:** It also depends on at what frequency the sites are handed over to us and we are here to complete about 100 sites in every two months.

**Parikshit Kandpal:** For projects like Ramprastha have you completely exited this real estate project or the project is still going on?

**Luv Chhabra:** There is no progress on that. We have mentioned it before that we are going through process of arbitration to get our money back from Ramprastha and it is expected that we would arrive at a fruitful conclusion by the end of this financial year.

**Parikshit Kandpal:** Any progress on this listing of this international subsidiary?



**Luv Chhabra:** Are we listing?

**Parikshit Kandpal:** There was talk about Sembawang getting listed.

**Luv Chhabra:** Did we make such a disclosure at any point of time?

**Parikshit Kandpal:** No, not you. I am saying there have been talks in the market about listing of Sembawang.

**Luv Chhabra:** You are asking us to comment on some speculative news. How can you expect the company to comment on that?

**Moderator:** The next question is from the line of Nitin Arora from Angel Broking.

**Nitin Arora:** Can you please tell me the reason for the high tax rate during the quarter?

**Raju Kaul:** It's not a high tax rate, as it looks like. There are overseas subsidiaries and whatever profits they are earning, cannot be set off against any losses of the main holding company in India, to arrive at a consolidated taxable income. Therefore, tax outgo does not have kind of correlation with consolidated PBT.

**Nitin Arora:** But if you look at historically, even in second quarter FY11 the tax rate was much lower even though we were operating in other geographies as well. So is it something which is happened in last few quarters or normal course?

**Luv Chhabra:** We have a subsidiary Sembawang in Singapore which has made profits and there the tax is around 18%. Similarly in Malaysia, we have a subsidiary which has made profits. They have paid 20% tax, which we can't set off against the marginal losses of one or two subsidiaries in other countries. So obviously on the consolidated PBT figure, there cannot be any single tax percentage which can be applied.

**Nitin Arora:** If you look at the past few quarters, our non-operating income has been around ₹ 3 crore; is this majorly foreign exchange income or it comprises of something else in the current quarter?

**Raju Kaul :** You have other things like we mentioned earlier. We have some liability write-back, some interest component and some dividend components. I don't have the exact figure right now.

**Nitin Arora:** Can you just break up the foreign exchange income from this ₹ 67-68 crore?

**Luv Chhabra:** We don't have this readily available now. Raju can give you those details subsequently.

**Moderator:** As there are no further questions, I would now like to hand the floor over to Mr. Atul Punj for closing comments.

**Atul Punj:** Thanks everybody for coming on the call. I think we are really doing what we do think best at this time to pick up more business. One of our major projects now is to address the interest component and debt components, so hopefully in the next few quarters we should start to see some positive impact of that effort as well. The Quality of our order book is strong. We are seeing clients are well-funded. There are no projects that are on hold and once again I think the global diversity is now beginning to pay off in view of the competitive intensity that we are seeing in India and we hope that this strategy will carry on and we look forward to delivering similar results in the next few quarters. Thank you very much.

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