SINCE 1986
DALAL STREET INVESTMENT JOURNAL
DEMOCRATIZING WEALTH CREATION

THINK DIFFERENT PROFIT MORE

UPSTREAM PICK

Company Name	:	**Sobha Ltd.**
BSE Code	:	**532784**
Time Duration	:	**2 year**
CMP	:	**₹554 (as on 01 March, 2018)**
Target Price	:	**₹795**

The Upstream Pick for the month of March is Sobha Ltd. It is a real estate company headquartered in Bangalore and has presence in 26 cities across 13 states in India. So far, the company has completed 406 projects in the real estate and contracts segments with developed area of 86.73 mn sq. ft. Under the real estate segment, its residential projects include luxury and super luxury apartments, villas, row houses and aspirational homes. Under the contracts segment, it provides end-to-end solutions from conceptualisation to its completion.

Luxury housing is the fastest growing segment in residential housing. During the past five years, the number of people in the high income group has almost tripled. The purchase of luxury housing is inelastic towards loan interest rates and people buy it despite higher prices. The demand for such luxury and super luxury housing is maximum in metros like Mumbai, Bangalore, Hyderabad, Kolkata and Gurgaon. The 'Smart City' mission will also boost the demand for luxury housing. We see this scrip as an Upstream Pick as the company belongs to real estate sector having certain headwinds. It has high debt component and the working capital cycle was undergoing a tough phase. All the regulations like demonetisation, GST and RERA impacted the demand for its products, especially the luxury housing segment. However, the company has overcome these obstacles and the business has been stabilised now.

New launches to drive topline

As per the management, post the implementation of GST and RERA, the momentum of the company's sales in terms of volumes has been stabilised. In 9MFY17, its sale volume was 2.28 mn sq. ft., which improved to 2.61 mn sq. ft. in 9MFY18. The company is planning to launch up to three projects in every quarter from now on. In this December quarter, the company launched two new projects, one each in Bangalore and Thissur, having total saleable area of 0.98 mn sq. ft. The Bangalore project will be jointly developed, with the company having 61.8% share in the revenue while the Thrissur project is an independent one and the company will earn the entire revenue. In the upcoming quarters, the company is planning to launch 5-7 new projects in Bangalore, Chennai, Mysore and Cochin. It is also planning to venture into new geographies like Ahmedabad and Hyderabad. With such new launches, we expect the pace of growth in volumes will increase going forward.

Foray into Affordable Housing

The affordable housing theme is gaining momentum in recent times with the government taking new initiatives to support it. Sobha Ltd too is buoyant about affordable housing and has planned to launch a project in Bangalore. The project would be 2 BHK flat system having approximately 1,800 apartments. As the project is under the process of getting approvals, the company is planning to launch it in H1FY19. With the PMAS and 'Housing for All' initiatives of the government, the momentum is expected to pick up in the affordable housing segment. If Sobha Ltd's initial project in affordable housing gets successful, the company will benefit and can grow in this segment going forward.

Strong Order Book in Contracts segment

As on December 31, 2017, the built-up area of the contractual projects was 7.17 mn sq. ft. The contractual order book of the company at present is ~Rs 1470 crore, which is 2x the TTM revenue from the contractual segment. Such strong order book has given revenue visibility for the next 2-2.5 years. The area under development of these contractual projects is ~7.17 mn sq. ft. spread over seven cities.

Impact of RERA

Under the RERA, factors such as transparency in dealings, mandatory timelines, risk-free mechanism to protect financial interests of the buyers have imbibed confidence amongst buyers to make investments in real estate. High net worth individuals have started investing again in real estate and we expect the demand for luxury housing to increase further and sustain in the long run.

Improving business performance

The total collections during 9MFY18 was up by 12% YoY, leading the company to generate positive cash flows over the past 10 quarters. The company's debt has gradually increased quarter-by-quarter in FY18 as investments have increased for bagging new opportunities and starting new projects. Its average cost of borrowing too has improved from 10.9% in 9MFY17 to 9.7% in 9MFY18. In FY18, the collections have improved as compared to the previous quarters. The products having sales value of more than Rs 2 crore have robust demand leading to higher realisations. The customer base of the company is also strong with 82% of the customers below 50 years of age and 80% of the customers are salaried professionals.

Financial Performance

Over the years, the company's topline has been growing in lower double digit. In FY17, the revenue grew by 14.1% YoY despite the demonetisation phase seen in Q3FY17. The EBITDA margin stood low at 18.8% as compared to the levels of 25-27% in the previous years due to higher operating expenses. The PAT margin declined to 6.4% in FY17 as against 9-10% in the previous years. The receivable days in FY16 were 40.9 days, which improved to 36.3 days in FY17. Despite operating in the realty sector which is highly debt-ridden, the company has maintained decent debt-equity ratio of 0.8x. Over the years, the company has been paying dividend consistently. In FY17 it paid 25% dividend to its shareholders.

Some revival is seen in 9MFY18. The topline in 9MFY18 grew by 14.3% YoY to Rs 1881.6 cr. The operating profit increased by 22.5% YoY as other income rose by 18.6% YoY. The PAT has jumped by 33.5% YoY to Rs 134 cr from Rs 100.4 cr in the corresponding period last year.

Valuation

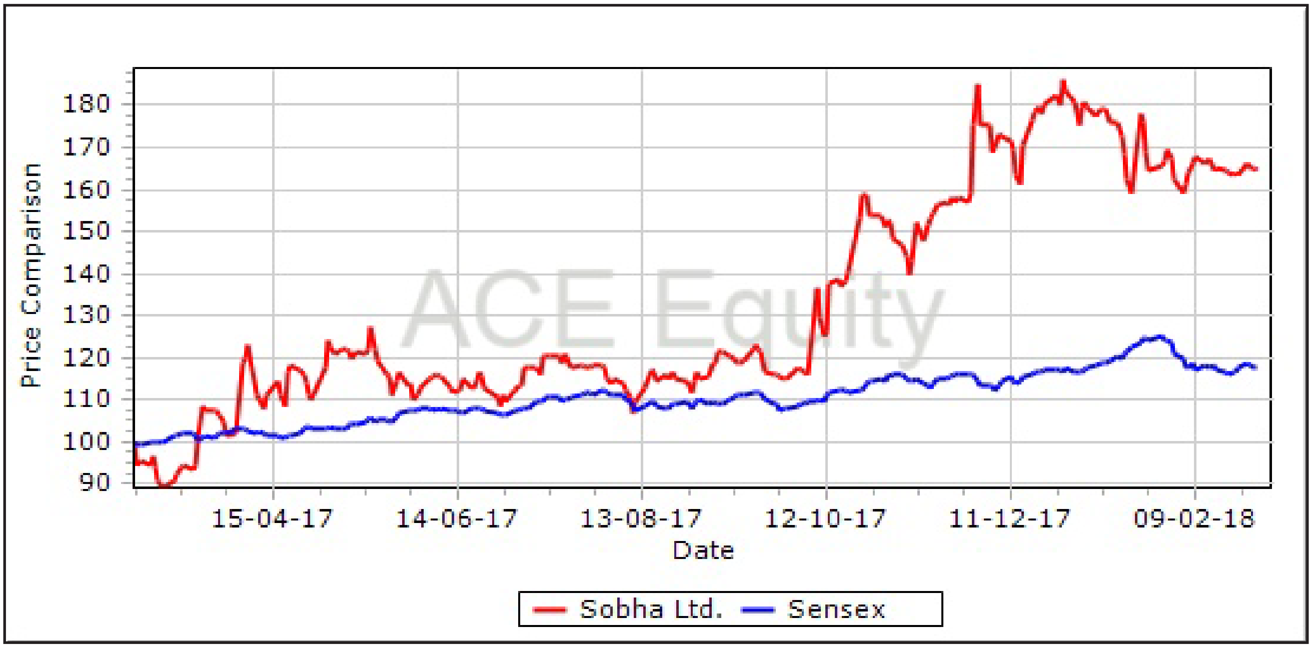
The company is trading at TTM P/E of 26.7x with TTM EPS of Rs 20.9. The bookings and collections are improving and the order book is strong. The company's cash flow position is stable and, thus, the increasing debt level will not prove risky for the company. The growing demand for luxury housing will augur well for the company. We see potential upside of 44% with a target price of Rs 795 over a period of two years. We urge investors to **BUY** the scrip and accumulate on dips.

Inc/Exp Statement(Consolidated) (Rs in Crore)

Description	201703	201603	201503	201403	201303
Net Sales	2229.06	1943.20	2440.56	2173.43	1864.54
Total Income	2267.67	1977.48	2455.48	2183.76	1870.06
Total Expenditure	1809.32	1500.27	1823.26	1570.84	1316.29
PBIDT	458.34	477.21	632.22	612.92	553.77
PAT	147.83	135.04	243.94	233.69	217.06
Dividend %	25.00	20.00	70.00	70.00	70.00
Adj. EPS(Rs)	16.69	14.08	24.27	23.97	22.15

Quarter On Quarter (Consolidated) (Rs in Crore)

Particulars	201712	201709	Q on Q Var%	201612	Y on Y Var%
Net Sales	691.90	646.60	7.01	545.00	26.95
Total Expenditure	554.40	521.80	6.25	448.60	23.58
PBIDT (Excl OI)	137.50	124.80	10.18	96.40	42.63
PAT	53.40	50.30	6.16	32.60	63.80
PBIDTM% (Excl OI)	19.87	19.30	2.95	17.69	12.32
PBIDTM%	21.10	21.03	0.33	19.41	8.71
PATM%	7.72	7.78	-0.77	5.98	29.10
Adj. EPS(Rs)	5.63	5.22	7.85	4.09	37.65


180
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Price Comparison
15-04-17
14-06-17
13-08-17
12-10-17
11-12-17
09-02-18
Date
ACE Equity
Sobha Ltd.
Sensex