

Nesco Limited

| | |
|-----------------------|--------------|
| STOCK INFO. | BLOOMBERG |
| BSE Sensex: 20,445.04 | NSE IN |
| S&P CNX: 6,143.40 | REUTERS CODE |
| | NSSEN.BO |

| Y/E MARCH | 2009 | 2010E | 2011E | 2012E |
|-----------------|------|-------|-------|-------|
| Net Sales (₹cr) | 95 | 120 | 140 | 190 |
| EBITDA (₹cr) | 50 | 82 | 104 | 152 |
| RPAT (₹cr) | 32 | 56 | 66 | 93 |
| BV/Share | 74 | 112 | 153 | 219 |
| Adj.EPS (₹) | 23 | 40 | 47 | 66 |
| EPS Growth (%) | -16 | 73 | 18 | 40 |
| P/E (x) | 25.7 | 14.8 | 12.5 | 8.9 |
| P/BV (x) | 8.0 | 5.3 | 3.9 | 2.7 |
| EV/EBITDA (x) | 17 | 10 | 8 | 5 |
| EV/ Sales (x) | 9 | 7 | 6 | 4 |
| RoE (%) | 34 | 41 | 34 | 34 |
| RoCE (%) | 31 | 38 | 33 | 34 |

KEY FINANCIALS

| | |
|-----------------------------|------|
| Shares Outstanding (₹cr) | 1.41 |
| Market Cap. (₹b) | 8.3 |
| Market Cap. (US\$ m) | 185 |
| Past 3 yrs Sales Growth (%) | 20 |
| Past 3 yrs NP Growth (%) | 46 |

STOCK DATA

| | |
|---------------------------------------|----------|
| 52-W High/Low Range (₹) | 777/330 |
| Major Shareholders (as of March 2010) | |
| Promoter | 62.0 |
| Non Promoter Corp Holding | 4.7 |
| Public & Others | 33.3 |
| Average Daily Turnover(6 months) | |
| Volume | 13841 |
| Value (₹cr) | 0.90 |
| 1/6/12 Month Abs. Performance (%) | -3/-9/32 |
| 1/6/12 Month Rel. Performance (%) | 12/16/19 |

1 October 2010

Buy

Initiating Coverage

₹585

We are initiating coverage on Nesco Limited (NESCO) with a BUY rating and 12 month price target of ₹750.

INVESTMENT ARGUMENTS

- Monopolistic business opportunity in the exhibition space
- Additional revenue stream from new IT park to start from FY12
- Strong earnings growth

Monopolistic Business opportunity/High Entry Barrier in Exhibition Space

The global trade exhibition business is a multibillion dollar market in which India presently has just a 0.7% stake. Bombay Exhibition Centre (BEC) is the largest exhibition centre in Mumbai, which is part of the 70-acre land bank on Western Express Highway at Goregaon, near Mumbai airport and has become a permanent venue for conventions, exhibitions and trade fairs in India. Bombay Exhibition Centre (BEC) is the only place in Mumbai where large scale exhibitions can be held.

Revenue from IT Park continues to grow rapidly

Nesco is developing an IT park, for the purpose of leasing and we expect this development to act as a major growth driver. The total area under construction will be 35 lacs. sq. ft. The first phase (IT Park 3) will have the built up area of ~ 8 lacs. sq ft.

Earnings to grow at a CAGR of 29% over FY10-12

We model Nesco's net profit to increase at a CAGR of 29% from ₹56 crs. to ₹93crs. over FY10-12, driven by rentals of new IT park, and increased revenue from Bombay Exhibition Centre. We estimate Nesco's EBITDA margins to move from 69% in FY 10 to 80% in FY12.

Valuation and View

Between FY10 & FY12, we expect Revenues and Net profit would grow at 26% and 29% CAGR respectively. We expect the EPS of ₹47 in FY11 & ₹ 66 in FY12. We are bullish on the growth story of Nesco Ltd. and initiate coverage with price target of ₹750 an upside of ~27%.

Terminal Valuation - NAV

To justify the valuation of Nesco's land, we enquired about the land prices in area where Nesco is situated. Per acre cost in the area comes in the range of ₹500 mn. This makes Nesco's land valuation at ₹35 bn, while the market capitalization of the company is just ₹8.3 bn.

CONCERNS:**Delay in Construction of IT Park:**

In last 1 year, the construction of IT Park has been delayed by 9-10 months due to delay in approval from various regulatory authorities. Any further delay may affect the timely completion of the IT park and thus delay the revenue accrual to the company

Oversupply in commercial Real Estate in Mumbai suburbs:

There is some oversupply of Real Estate in Mumbai's suburbs and is unlikely to change in the short term. Under these circumstances, rental rates are unlikely to show consistently upward trends, and could be flat for long periods.

Discount to NAV:

Since Nesco has no intention to monetize its assets by selling the land bank, it will continue to trade at discount to the NAV.

BUSINESS VERTICALS**BEC: Business Exhibition Centre**

Bombay Exhibition Centre (BEC) is the largest exhibition centre in Mumbai. It is part of the 70-acre land bank at Western Express Highway at Goregaon, near Mumbai airport and has become a permanent venue for conventions, exhibitions and trade fairs in India. Nesco has also modernized and upgraded the 4 convention and exhibition center halls covering an area of over 450,000 sq ft.

NESCO Realty

Nesco Realty provides built up spaces for multinational companies and corporates on lease. Currently, Nesco has provided 4.5 lacs sq ft to various companies. Nesco is developing an IT park, for the purpose of leasing and we expect this development to act as a major growth driver. The total area under construction will be 35lac. sq ft. The first phase (IT Park 3) will have the built up area of ~ 8lac. sq ft, which is expected to be complete by the end of FY11.

Nesco Engineering

Based at Karamsad and Vishnoli in Gujarat, engineering division manufactures forging hammers and presses, blow room lines and high production cards for textile industry, and sucker rod pumps for onshore oil recovery. Their major customers are Indian Railways, Ordnance Factories and Forging Plants.

KEY GROWTH DRIVERS**Marquee client base and high entry barrier**

Global exhibition companies like United Business Media (UBM), Reed Exhibitions, and Messe Frankfurt - all Nesco clients - enable face-to face interaction between global companies and their potential customers in India. When either of them wants to organize an exhibition in Mumbai - which is India's business capital - they have to go to BEC. There is no alternative. The exhibit below, taken from UBM's site, shows that of the 14 exhibitions booked by the company in India for 2010, eleven are to be held at Bombay Exhibition Centre. This gives the company the ability to earn supernormal profits in the long run.

Expansion of Exhibition Space

Nesco Ltd has decided to expand the area covered by exhibition space from existing 4.5 lacs sq ft to 1 mn. sq ft, after the completion of IT Park 3.

We like management's decision to grow the business without taking significant debt and without any need for equity dilution. Given the high cash generation, the gradual build-harvest-build approach makes sense.

Locational Advantage

To compete with Nesco in the exhibition business, one would need:

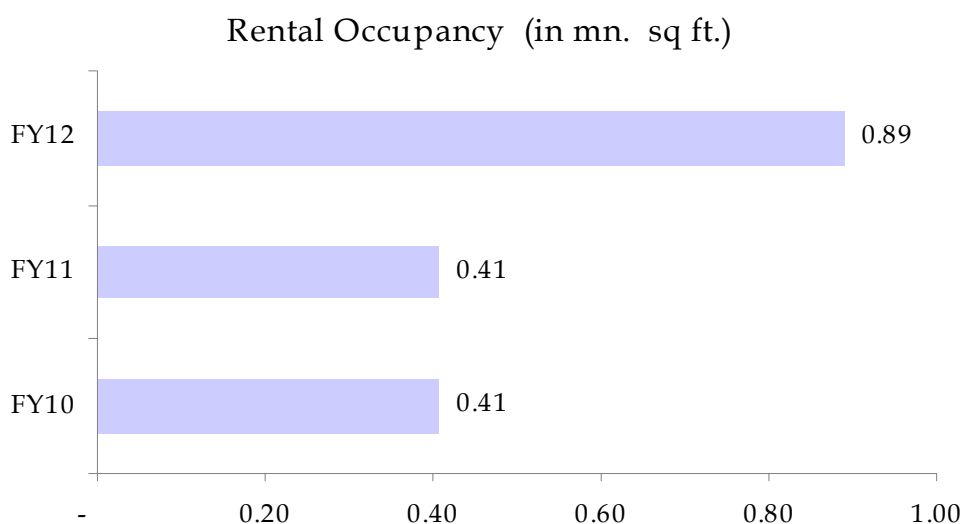
1. Large flat space which is scarce in Mumbai;
2. Proximity to a national highway;
3. Proximity to airport; and
4. Zero (or very little) land cost.

Meeting all four conditions will be very tough for potential competitors.

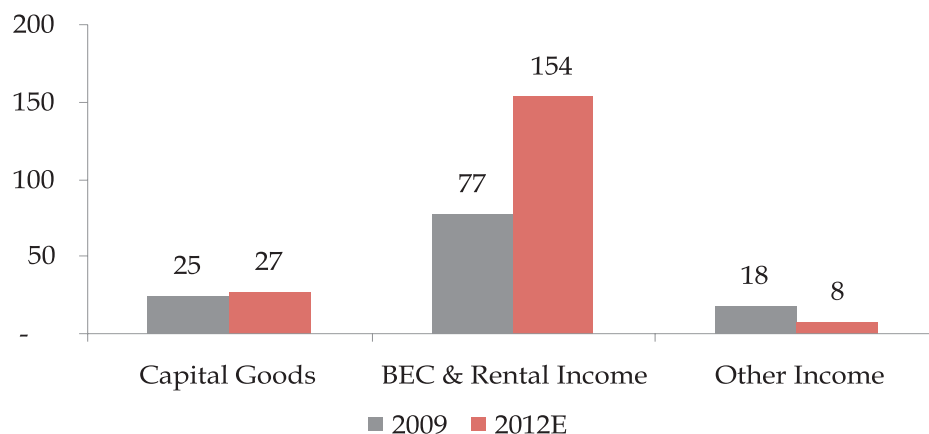
Revenue from IT Park continues to grow rapidly

Construction of IT Park 3, (proposed built up area of ~8 lacs sq. ft.) is being worked upon by Larsen & Toubro and is being funded totally out of Nesco's own resources. For FY 12, we expect the additional annual revenue of Rs.48 crores from IT Park 3.

For Nesco, the 70-acre parcel of land over which BEC and the commercial buildings stand is essentially free in the sense that it was bought several decades ago at a very low price. Accordingly, no lease rents or interest expense is charged to the income statement for the use of this land.



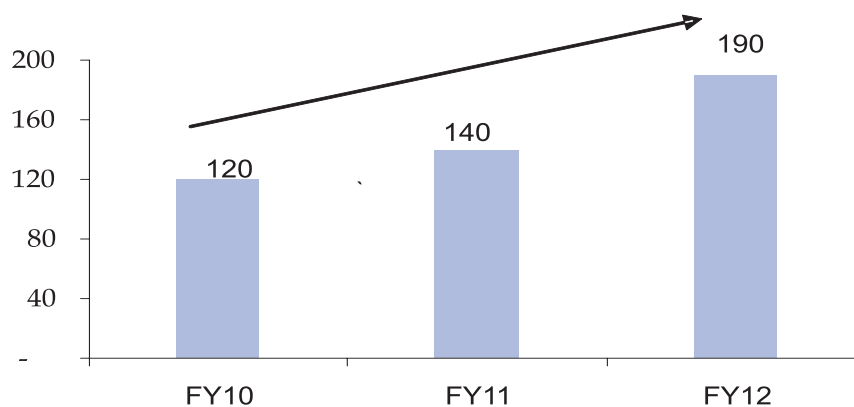
BEC & Rental Income to grow Rapidly



Source: Company/MOSL

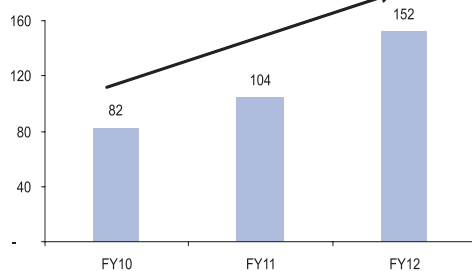
Earnings to grow at a CAGR of 26% over FY10-12

FY10-FY12 REVENUE CAGR OF 26%

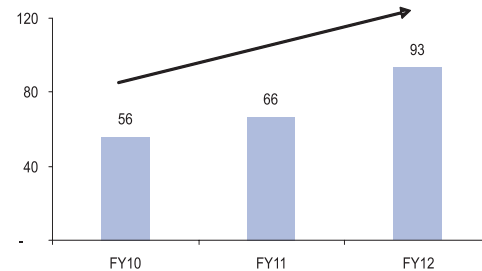


Source: Company/MOSL

FY10-FY12 EBITDA CAGR OF 36%



FY10-FY12 PAT CAGR OF 29%



Source: Company/MOSL

Nesco Ltd.- Financial & Valuation

INCOME STATEMENT (₹CRORE)

| Y/E MARCH | 2008A | 2009A | 2010A | 2011E | 2012E |
|-----------------------|------------|-------------|------------|------------|------------|
| Net Sales | 105 | 95 | 120 | 140 | 190 |
| <i>Change (%)</i> | | <i>-10%</i> | <i>27%</i> | <i>17%</i> | <i>36%</i> |
| Mfg & Estd expenses | 23 | 24 | 19 | 16 | 17 |
| Admin, S&G | 25 | 21 | 19 | 20 | 21 |
| EBITDA | 57 | 50 | 82 | 104 | 152 |
| <i>% of Net Sales</i> | <i>54%</i> | <i>53%</i> | <i>69%</i> | <i>74%</i> | <i>80%</i> |
| Interest Cost | 1 | 2 | 1 | - | - |
| Depreciation | 2 | 2 | 2 | 5 | 12 |
| PBT | 54 | 46 | 79 | 99 | 140 |
| Tax | 16 | 14 | 23 | 33 | 47 |
| <i>Rate (%)</i> | <i>30%</i> | <i>30%</i> | <i>29%</i> | <i>33%</i> | <i>33%</i> |
| Reported PAT | 38 | 32 | 56 | 66 | 93 |
| <i>% of Net Sales</i> | <i>36%</i> | <i>34%</i> | <i>47%</i> | <i>47%</i> | <i>49%</i> |

BALANCE SHEET (₹CRORE)

| Y/E MARCH | 2008A | 2009A | 2010A | 2011E | 2012E |
|----------------------------------|-------------|-------------|-------------|-------------|--------------|
| Share Capital | 7 | 7 | 7 | 14 | 14 |
| Reserves | 72 | 104 | 158 | 216 | 308 |
| Net Worth | 79 | 111 | 165 | 230 | 322 |
| Loans | - | 17 | - | - | - |
| Deffered Tax Liability | 2 | 1 | 1 | 1 | 1 |
| Capital Employed | 81 | 129 | 166 | 231 | 323 |
| Gross Fixed Assets | 57 | 62 | 57 | 259 | 259 |
| Less: Depreciation | 28 | 30 | 27 | 32 | 44 |
| Net Fixed Assets | 29 | 32 | 30 | 228 | 216 |
| Capital WIP | 4 | 3 | 33 | - | 240 |
| Investments | 94 | 111 | 134 | 80 | - |
| Curr. Assets | 51 | 87 | 95 | 98 | 116 |
| Inventory | 5 | 5 | 3 | 3 | 3 |
| Debtors | 7 | 10 | 14 | 7 | 8 |
| Cash & Bank Balance | 10 | 13 | 2 | 20 | 22 |
| Miscellaneous Expenditure | 2 | 1 | - | - | - |
| Loans & Advances | 27 | 58 | 75 | 68 | 83 |
| Current Liab. & Prov. | 97 | 105 | 126 | 173 | 247 |
| Creditors | 10 | 7 | 7 | 7 | 7 |
| Advance received | 5 | 20 | 24 | 37 | 40 |
| Security Deposit | 5 | 20 | 14 | 15 | 39 |
| Provisions | 5 | 52 | 75 | 108 | 154 |
| Other Liabilities | 72 | 6 | 6 | 6 | 7 |
| Net Current Assets | (46) | (16) | (31) | (78) | (131) |
| Application of Funds | 81 | 128 | 166 | 230 | 322 |

RATIOS

| Y/E MARCH | 2008A | 2009A | 2010A | 2011E | 2012E |
|--------------------------|-----------|-------------|------------|------------|------------|
| Adjusted EPS | 27 | 23 | 40 | 47 | 66 |
| <i>Growth (%)</i> | | <i>-16%</i> | <i>73%</i> | <i>18%</i> | <i>40%</i> |
| Cash EPS | 28 | 24 | 41 | 50 | 75 |
| Book Value | 51 | 74 | 112 | 153 | 219 |
| DPS | 0.6 | 0.6 | 1.5 | 2 | 4 |
| Payout (incl. Div. Tax.) | 2% | 3% | 4% | 4% | 6% |
| Depreciation (₹cr) | 2 | 2 | 2 | 5 | 12 |
| Depreciation per share | 1 | 2 | 2 | 3 | 8 |
| Valuation (x) | | | | | |
| P/E | 21.7 | 25.7 | 14.8 | 12.5 | 8.9 |
| Cash P/E | 20.8 | 24.2 | 14.3 | 11.7 | 7.9 |
| EV/EBITDA | 15 | 17 | 10 | 8 | 5 |
| EV/Sales | 8 | 9 | 7 | 6 | 4 |
| Price/Book Value | 11.6 | 8.0 | 5.3 | 3.9 | 2.7 |
| Dividend Yield (%) | 2% | 3% | 4% | 4% | 6% |
| Return Ratios (%) | | | | | |
| RoE | 49% | 34% | 41% | 34% | 34% |
| RoCE | 48% | 31% | 38% | 33% | 34% |

CASH FLOW STATEMENT (₹CRORE)

| Y/E MARCH | 2008A | 2009A | 2010E | 2011E | 2012E |
|-------------------------------------|-------------|-------------|-------------|--------------|--------------|
| PBT before EO Items | 55 | 46 | 79 | 99 | 140 |
| Add : Depreciation | 2 | 2 | 2 | 5 | 12 |
| Interest & Investment Inc | (7) | (7) | (11) | (12) | (4) |
| Others | (3) | 3 | (3) | 1 | 1 |
| Op. profit before WC changes | 47 | 45 | 67 | 93 | 149 |
| (Inc)/Dec in WC | 29 | (26) | 4 | 61 | 59 |
| CF from Operations | 77 | 18 | 71 | 154 | 206 |
| Taxes Paid/ E.O. Items | (19) | (1) | (25) | (31) | (47) |
| Net Cash from Operations | 58 | 17 | 46 | 123 | 159 |
| (Inc)/Dec in FA | (2) | (5) | (25) | (170) | (240) |
| (Pur)/Sale of Investments | (58) | (17) | (23) | 54 | 80 |
| Interest & Investment Income | 8 | 7 | 11 | 12 | 4 |
| CF from Investments | (52) | (15) | (37) | (104) | (156) |
| (Inc)/Dec in Networth | | | | | |
| (Inc)/Dec in Debt | 0 | 17 | (17) | 0 | 0 |
| Less : Interest Paid | (1) | (16) | (1) | 0 | 0 |
| Dividend Paid | (1) | (1) | (1) | (1) | (1) |
| CF from Fin. Activity | (2) | (0) | (19) | (1) | (1) |
| Inc/Dec of Cash | 4 | 2 | (10) | 18 | 2 |
| Add: Beginning Balance | 6 | 10 | 12 | 2 | 20 |
| Closing Balance | 10 | 12 | 2 | 20 | 22 |

PEER COMPARISON:

| PEER COMPARISON (FY10) | NIRLON LTD (*) | NESCO LTD |
|------------------------|----------------|-------------|
| | FY10 | FY10 |
| Sales (₹cr) | 56.2 | 120 |
| 3 yr growth (%) | 188 | 20 |
| M. Cap (₹bn) | 3.95 | 8.24 |
| Adj. Profit (₹cr) | -18.3 | 56 |
| 3 yr growth (%) | -14.9 | 46 |
| P/E (x) | N.A. | 14.8 |
| EV/EBITDA (x) | 41.5 | 10 |
| D/E (x) | 4.2 | N.A. |
| ROE (%) | NA | 41 |

(*) Does not have exhibition and capital goods business vertical

Period: Year-ended March 2010

Source- Capitaline/MOSL



For more copies or other information, contact

Institutional: Navin Agarwal. **Retail:** Manish Shah

Phone: (91-22) 39825500 Fax: (91-22) 22885038. E-mail: reports@motilaloswal.com

Motilal Oswal Securities Ltd, 3rd Floor, Hoechst House, Nariman Point, Mumbai 400 021

This report is for the personal information of the authorized recipient and does not constitute to be any investment, legal or taxation advice to you. Motilal Oswal Securities Limited (*hereinafter referred as MOSL*) is not soliciting any action based upon it. This report is not for public distribution and has been furnished to you solely for your information and should not be reproduced or redistributed to any other person in any form.

The report is based upon information that we consider reliable, but we do not represent that it is accurate or complete, and it should not be relied upon such. MOSL or any of its affiliates or employees shall not be in any way responsible for any loss or damage that may arise to any person from any inadvertent error in the information contained in this report. MOSL or any of its affiliates or employees do not provide, at any time, any express or implied warranty of any kind, regarding any matter pertaining to this report, including without limitation the implied warranties of merchantability, fitness for a particular purpose, and non-infringement. The recipients of this report should rely on their own investigations.

MOSL and/or its affiliates and/or employees may have interests/ positions, financial or otherwise in the securities mentioned in this report. To enhance transparency, MOSL has incorporated a Disclosure of Interest Statement in this document. This should, however, not be treated as endorsement of the views expressed in the report.

Disclosure of Interest Statement

1. Analyst ownership of the stock
2. Group/Directors ownership of the stock
3. Broking relationship with company covered
4. Investment Banking relationship with company covered

Nesco Ltd.

No
Yes
No
No

This information is subject to change without any prior notice. MOSL reserves the right to make modifications and alternations to this statement as may be required from time to time. Nevertheless, MOSL is committed to providing independent and transparent recommendations to its clients, and would be happy to provide information in response to specific client queries.