NIRMAL BANG
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Institutional Equities

NESCO

30 January 2018

Initiating Coverage

Reuters: NSEN.NS; Bloomberg: NSE IN

Step In Before It Is Too Late

We initiate coverage on NESCO with a Buy rating and a target price of Rs794 based on FY20E SOTP (sum of the parts) valuation, implying an upside of 30% from the CMP. Our optimism on NESCO is supported by: 1) Strategy focused on increasing rentable area supported by the expected increase in lease rentals. 2) Healthy balance sheet with a net cash balance. 3) Strong cash flow with positive FCFF. 4) Earnings expected to grow sharply post restructuring.

Strategy focused on commercial area, exhibition and convention centre: NESCO management's strategy is focused on: 1) Developing the entire land bank of 70 acres (usable 58 acres) in Goregaon, Mumbai, into a commercial complex and an exhibition centre with total rentable area of approximately 9.5mn sqft over the next 20 years. 2) Entry into hotels and food catering business verticals. 3) Strict financial discipline with capex for the proposed expansion to be funded through internal accruals.

Long-term plan to build and lease 5mn sqft of commercial space: NESCO IT Park has total leasable area of 1.02mn sqft as of FY17-end. Following the ongoing restructuring, leasable area will come down to 0.67mn sqft by FY19E. Post restructuring, leasable area of NESCO IT Park is expected to touch 1.87mn sqft by FY21E and 2.87mn sqft by FY24E. Over a 20-year period, the leasable area is expected to increase to 5mn sqft. NESCO has an attractive client base which includes companies like MSCI, KPMG and HSBC. Approximately, 45% of revenues are generated from leasing of commercial space.

Bombay exhibition centre leasable area to be expanded to 4.5mn sqft in next 20 years: Bombay Exhibition Centre (BEC) contributed 42% to total revenues in FY17. It has total leasable area of 0.64mn sqft which is expected to increase with the addition of 0.45mn sqft of convention centre (Phase1-FY23E).Along with the upcoming expansion plan, it benefits from client stickiness which also acts as a cushion during an economic downturn. Over the next 20 years, the total space is expected to be expanded to 4.5mn sqft.

Healthy balance sheet with net cash position: NESCO has maintained strong financial discipline with the capex for expansion being funded from internal accruals. As of FY17-end, the company had cash plus investment balance of Rs4.9bn on a balance sheet size of Rs10.3bn. We expect the company to maintain financial discipline which adds to our comfort.

Consistently positive free cash flows: Free cash flows have been in the range of Rs22mn-Rs641mn over FY10-FY17 and we expect the positive cash flow trend to continue.

Muted earnings growth at 6% CAGR (FY17-FY20E) because of restructuring: We expect subdued earnings growth over FY17-FY20E because of restructuring undertaken by the company. After the first phase of restructuring, we expect the earnings to register a 35% CAGR over FY21E-FY23E.

We recommend Buy rating with a target price of Rs794: Our target price of Rs794 is based on FY20E SOTP based valuation. Our valuation is driven by the restructuring of NESCO IT Park, increase in rentable space of BEC and the expected rise in rental rates. Our optimism is supported by a healthy balance sheet, consistently positive free cash flow and the management's growth-oriented focus with expansion of flagship business over the next 20 years. NESCO stock currently trades at Rs613, which is at a discount of 22% to our target price. We have assigned Buy rating to the stock.

Conservative valuation does not include proposed 5.5mn sqft in leasable area: In our SOTP based valuation, we have considered only 3.96mn sqft of leasable area for NESCO IT Park and Bombay Exhibition Centre. Over a 20-year horizon, the management plans to utilise 4.5mn sqft of leasable area for Bombay Exhibition Centre and 5mn sqft of leasable area for NESCO IT Park.

Risks: Delay in execution of expansion plan and any unexpected rise in the vacancy rate.

Y/E March (Rsmn)	FY15	FY16	FY17	FY18E	FY19E	FY20E
Revenues	1,944	2,635	3,114	3,666	3,846	4,085
YoY (%)	*20.7*	*35.5*	*18.2*	*17.7*	*4.9*	*6.2*
EBITDA	1,380	1,885	2,146	2,586	2,719	2,895
EBITDA (%)	*71.0*	*71.5*	*68.9*	*70.5*	*70.7*	*70.9*
PAT	1,116	1,442	1,700	2,040	2,057	2,053
YoY (%)	*37.8*	*29.2*	*17.9*	*20.0*	*0.9*	*(0.2)*
EPS (Rs)	15.8	20.5	24.1	29.0	29.2	29.1
RoE (%)	*20.7*	*21.2*	*20.0*	*19.7*	*16.8*	*14.6*
EV/EBITDA (x)	31.3	22.9	20.1	16.7	15.9	14.9
P/E (x)	38.7	29.9	25.4	21.2	21.0	21.0

Source: Company, Nirmal Bang Institutional Equities Research

BUY

Sector: Real Estate

CMP: Rs613

Target Price: Rs794

Upside: 30%

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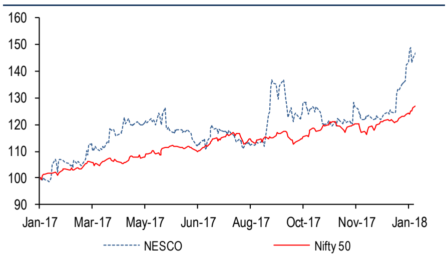
Key Data

Current Shares O/S (mn)	70.5
Mkt Cap (Rsbn/US$mn)	42.9/672.9
52 Wk H / L (Rs)	650/410
Daily Vol. (3M NSE Avg.)	93,370

Share holding (%)	3QFY18	2QFY18	1QFY18
Promoter	68.2	68.2	68.2
DII	-	-	-
General Public	31.8	31.8	31.8

One Year Indexed Stock Performance



Price Performance (%)

	1 M	6 M	1 Yr
NESCO	15.5	21.9	43.9
Nifty Index	5.0	10.4	28.1

Source: Bloomberg

Investment rationale

We initiate coverage on NESCO with a Buy rating and a target price of Rs794 based on FY20E SOTP based valuation. Declining vacancy rate in the commercial real estate sector, restructuring of NESCO IT Park, increase in rentable area of BEC, strong balance sheet and healthy cash flow are some primary drivers of our optimism on NESCO. Hospitality (food catering) and Bombay Exhibition Centre will drive revenues over the short run whereas NESCO IT Park will support growth over a longer horizon. Although there has been a decent run-up in the stock price over the past one year, we consider the valuation to be attractive, given the growth potential that the company offers.

Management strategy driven by expansion of commercial space and exhibition centre

NESCO's strategy is focused on utilizing the entire land bank (70 acres; usable 58 acres) in Goregaon to develop commercial office space and exhibition centre with rentable area of 9.5mnsqt in the next 20 years. In the short to medium term the company expect: 1. Post restructuring, the leasable area of NESCO's IT Park to increase to 2.87 mn sq ft by FY24E. 2. Expansion of leasable area of Bombay Exhibition Centre to 1.09mn sqft from the current 0.64mn sq ft in FY23E. 3 Post completion of restructuring in commercial and exhibition centre, the management's focus will be on executing the construction of hotel and auditorium (part of Phase1).

Further, NESCO plans to enter organization of events for existing/new clients. These events will be conducted on days when the Bombay Exhibition Centre is unoccupied.

Restructuring of NESCO IT Park

NESCO IT Park has a total of three fully occupied buildings as of FY17-end. NESCO IT Park will undergo restructuring where Building 1 (0.175mn sqft) and Building 2 (0.175mnsqft) will be demolished. The area of Building 1 will be utilised for Bombay Exhibition Centre and Building 2 will be reconstructed with a leasable area of 1mn sq ft. Building 4, with a total leasable area of 1.2mn sqft, is under construction and should be fully operational by FY21E.

Hospitality (food catering) segment expected to post 86% CAGR over FY17-FY20E

NESCO has commissioned two food courts and started food services with some national and international brands. A kitchen facility measuring 24,000sqft is operational. The facility has capacity to make 15,000 meals per shift. Currently, the facility operates at 1.5x shifts per day with a lower capacity utilisation and has the potential to run at least three shifts per day with better capacity utilisation.

Bombay Exhibition Centre – client stickiness

Around 80% of clients of Bombay Exhibition Centre (BEC) are repetitive in nature. Despite the number of exhibitions declining from 156 in FY16 to 109 in FY17, revenues grew 19% YoY which highlights the fact that the existing organisers' contribution to revenues was higher in FY17. Currently, BEC operates at 35% of its capacity and we believe that 40% can be achieved post FY19E.

To remain debt-free despite undertaking heavy capex

NESCO reported net debt-to-equity ratio of (0.57) in FY17, indicating that the company has net cash. We believe that capital expenditure over FY18E-FY20E could be to the tune of Rs7,963mn which would be met through internal accruals and sale of investments. NESCO has liquid investments of Rs4,818mn as of FY17-end, which acts as a cushion for undertaking capital expenditure and making dividend payment.

Conservative valuation (does not include valuation of 23 acres of land); recommend Buy with a target price of Rs794

We recommend Buy rating to NESCO with a target price Rs794 based on FY20E SOTP valuation.. We have divided the valuation into two phases: 1) Current phase, and 2) Future phase. In each phase, we have individually valued every segment namely: 1) NESCO IT Park, 2) Bombay Exhibition Centre, 3) Hospitality segment (food catering), and 4) Indabrator.

We believe the management's focus on expansion of NESCO IT Park and Bombay Exhibition Centre will be long-term growth drivers of the stock. Factors like client stickiness at Bombay Exhibition Centre, strong and reputed client base in the commercial office space and likely increase in capacity utilisation in hospitality segment will provide additional support to the current valuation.

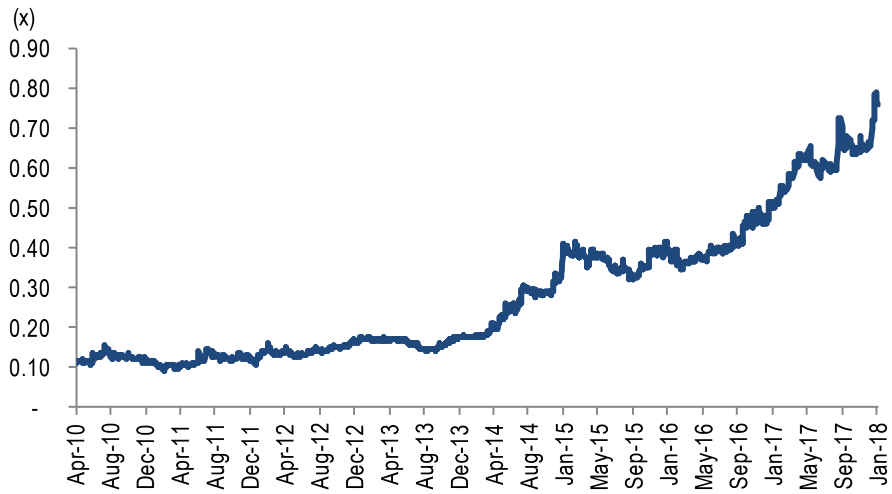
Further, in our valuation, we have included only 4mn sqft of leasable area expected to be operational by FY23E and have ignored the value of 23 acres of land which is likely to be developed into additional leasable area of 5.5mn sqft in the next 20 years. The valuation of NESCO does not look stretched given the growth potential the company offers and therefore we have assigned Buy rating to it with a target price of Rs794.

Risks:

1) **Delay in incurring planned capital expenditure.**

2) **Unexpected increase in the vacancy rate.**

Exhibit 1: Price/forward NAV



Source: Nirmal Bang Institutional Equities Research

NESCO stock currently trades at 3.1x FY20E P/BV and 0.8x FY20E P/NAV. Given the expected increase in total leasable area, and the likely increase in rent because of declining vacancy rate, we believe the stock will get re-rated. Although historically the stock has traded between 0.09x-0.79x P/NAV, we expect it to trade at 3.1xFY20E P/BV and 1x FY20E P/NAV.

SOTP Based Valuation

We initiate coverage on NESCO with a Buy rating and a target price of Rs794 based on FY20E SOTP based valuation method. We have divided our valuation into two phases - the current phase includes ongoing projects of the company and expansion in the near future and the future phase includes projects that the company plans to undertake in the long run. Within these two phases we have valued each segment of NESCO, namely NESCO IT Park, Bombay Exhibition Centre, hospitality (food catering) and Indabrator, arriving at a target price of Rs794.

Exhibit 2: Valuation based on FY20E SOTP

Segments (Rsmn)	Current phase	Future phase	Total
NESCO IT Park	19,361	4,876	24,237
Bombay Exhibition Centre	16,411	11,346	27,757
Hospitality	823	-	823
Indabrator	669	-	669
Sub-total	**37,263**	**16,222**	**53,486**
Cash plus Investments (FY20E)	-	-	2,473
Total value	**-**	**-**	**55,959**
Total number of shares (mn)	-	-	70
Value per share (Rs)	**-**	**-**	**794**

Source: Nirmal Bang Institutional Equities Research

Firstly, we shall discuss the assumptions undertaken in the current phase and then we shall move forward to valuation of the future phase. In the current phase, we shall be looking at relevant assumptions of different segments starting from NESCO IT Park.

Current Phase

Assumptions regarding NESCO IT Park

- We have considered a lease area of 0.97mn sqft for FY18E, 0.67mn sqft for FY19E and FY20E and 1.87mn sqft for FY21E-FY23E.
- Occupancy of Building 1 in FY18E is only for nine months as the building will be demolished and the area will be utilised for Bombay Exhibition Centre. Occupancy rate for Building 2 is 100% in FY18E and nil over FY19E-FY23E as the building will be demolished and a new building with a higher FSI will be constructed, the valuation of which is reflected in the future phase. Building 3 remains 100% occupied and Building 4 is available for lease from FY21E and is expected to achieve occupancy rate of 30%/60%/100% in FY21E/FY22E/FY23E, respectively.
- We have assumed a lease rate of Rs105sqft/month (net of maintenance cost) and inflation of 5% per annum for a hike in rentals.
- We have multiplied the leasable area with the occupancy rate to get the rented area. We have then multiplied the rented area with the lease rate to arrive at revenues.
- We have then subtracted depreciation to arrive at EBIT and then subtracted income-tax @30%.
- We have then added back depreciation and subtracted capital expenditure to arrive at segment-wise cash flows.
- We have assumed a capital expenditure of Rs5,800mn for Building 4. NESCO has already incurred Rs2,567mn of capex and we expect the balance Rs3,233mn to be incurred over FY18E-FY20E.
- NESCO is a debt-free company and we have considered cost of equity of 16% to arrive at the present value of future cash flows. (Refer Exhibit 11)
- To arrive at the terminal value, we have assumed long-term growth rate of 5% per annum which is the same as the inflation rate. The rental yields in the recent past have been in the range of 7.5%-8.0% per annum. based on which we have assumed a conservative capitalisation rate of 9% per annum. We have computed the terminal value at FY23E.
- After discounting future cash flows of NESCO IT Park, we have arrived at a valuation of Rs19,361mn.

Exhibit 3: Current phase - NESCO IT Park

NESCO IT Park	FY18E	FY19E	FY20E	FY21E	FY22E	FY23E
Lease area (sqft)	0.97	0.67	0.67	1.87	1.87	1.87
Building 1	0.13	-	-	-	-	-
Building 2	0.17	-	-	-	-	-
Building 3	0.67	0.67	0.67	0.67	0.67	0.67
Building 4	-	-	-	1.20	1.20	1.20
Occupancy rate (%)						
Building 1	100	0	0	0	0	0
Building 2	100	0	0	0	0	0
Building 3	100	100	100	100	100	100
Building 4	0	0	0	30	60	100
Leasable area*occupancy rate	0.97	0.67	0.67	1.03	1.39	1.87
Lease rate (Rs/sqft)	105	110	116	122	128	134
Inflation-sale (%)	*5*	*5*	*5*	*5*	*5*	*5*
Number of months	12	12	12	12	12	12
Revenues	**1,217**	**886**	**931**	**1,502**	**2,129**	**3,007**
Inflation-cost (%)	*5*	*5*	*5*	*5*	*5*	*5*
Maintenance Rs/sqft/month	-	-	-	-	-	-
Maintenance cost (Rsmn)	-	-	-	-	-	-
Depreciation (Rsmn)**	22	22	22	173	173	173
EBIT	**1,196**	**865**	**909**	**1,329**	**1,956**	**2,834**
Income-tax (%)	*30*	*30*	*30*	*30*	*30*	*30*
Income-tax (Rsmn)	359	259	273	399	587	850
Profit after tax	837	605	636	931	1,369	1,984
Add : Non-cash expenses	22	22	22	173	173	173
Operating cash flow	**859**	**627**	**658**	**1,104**	**1,542**	**2,157**
Capital expenditure						
Cost of land (Rsmn)	-	-	-	-	-	-
Cost of construction (Rsmn)	833	1,200	1,200	-	-	-
Total capital expenditure	**833**	**1,200**	**1,200**	**-**	**-**	**-**
Projected cash flow	26	(573)	(542)	1,104	1,542	2,157
Discount rate (%)	-	-	*16*	*16*	*16*	*16*
Period (years)	-	-	-	1	2	3
Discount factor	-	-	-	0.86	0.74	0.64
DCF	-	-	-	950	1,144	1,377
PVOFCF*	-	-	**3,471**	-	-	-
Terminal value	-	-	**15,890**	-	-	-
Value of NESCO IT Park (FY20E)	-	-	**19,361**	-	-	-

**PVOCF – Present value of future cash flows*

***Depreciation – Based on 0.67mnsqft*

Source: Nirmal Bang Institutional Equities Research

Assumptions- Bombay Exhibition Centre

- With an addition of 0.14mn sqft in FY18E, the total leasable area in FY18E-21E will be 0.64mn sqft.
- The occupancy rates are 35% for FY18E and 40% for FY19E-FY21E.
- We have considered a lease rate of Rs24sqft/day with an inflation of 5% per annum for hike in rentals.
- We have multiplied the leasable area to the occupancy rate to get the rented area. The rented area is then multiplied to the lease rate to arrive at revenues.
- Maintenance costs have been assumed at 15% of revenues.
- We have subtracted the maintenance costs and depreciation to arrive at EBIT.
- Income-tax rate is assumed @ 30%.
- We have arrived at operating cash flow after adding depreciation to profit after tax.

- We have assumed nil capital expenditure in this segment till FY21E.
- NESCO is a debt-free company and we have considered cost of equity of 16% to arrive at the current value of future cash flows. (Refer Exhibit 11)
- To arrive at the terminal value we have assumed long-term growth rate of 5% per annum, which is the same as the inflation rate. The rental yields in the recent past have been in the range of 7.5%-8.0% per annum based on which we have assumed a conservative capitalisation rate of 9% per annum. We have computed the terminal value based on FY21E financials.
- After discounting future cash flows of Bombay Exhibition Centre we have arrived at a valuation of Rs16,411mn.

Exhibit 4: Current phase -Bombay Exhibition Centre

Bombay Exhibition Centre	FY18E	FY19E	FY20E	FY21E
Lease (mnsqft)	0.64	0.64	0.64	0.64
Occupancy rate (%)	*35*	*40*	*40*	*40*
Total number of days	365	365	365	365
Occupied days	128	146	146	146
Leasable area	0.64	0.64	0.64	0.64
Lease rate (Rs/sqft/day)	24	25	26	27
Inflation rate (%)	*5*	*5*	*5*	*5*
Revenues (Rsmn)	**1,929**	**2,315**	**2,431**	**2,552**
Manitenance as a % of revenues	*15*	*15*	*15*	*15*
Maintenance costs (Rsmn)	289	347	365	383
Less: Depreciation) (Rsmn)	5	5	5	5
EBIT	**1,635**	**1,963**	**2,061**	**2,165**
Income-tax rate (%)	*30*	*30*	*30*	*30*
Income-tax (Rsmn)	490	589	618	649
PAT	1,144	1,374	1,443	1,515
Plus: Depreciation	5	5	5	5
Operating cash flow	**1,149**	**1,379**	**1,448**	**1,520**
Capital expenditure				
Cost of land (Rsmn)	-	-	-	-
Cost of construction (Rsmn)	-	-	-	-
Total capital expenditure	-	-	-	-
Projected cash flow	1,149	1,379	1,448	1,520
Discount rate (%)	-	-	-	*16*
Period (years)	-	-	-	1
Discount factor	-	-	-	0.86
DCF	-	-	-	1,309
PVOFCF*	-	-	**1,309**	-
Terminal value	-	-	**15,102**	-
Value of BEC (FY20E)**	-	-	**16,411**	-

*** Bombay Exhibition Centre*

**PVOCF – Present value of future cash flows*

Source: Nirmal Bang Institutional Equities Research

Assumptions – hospitality segment (food catering)

- We expect 56% revenue CAGR over FY17-FY22E. We believe the company will be able to increase the number of shifts from 1.5x to 3x per day. The company has the ability to make 15,000 meals per shift (currently operating at a lower capacity).
- We have assumed PAT margin of 15%. We have added depreciation to PAT in order to arrive at operating cash flow.
- The company has already incurred a capital expenditure of Rs1,500mn in FY17 and we have assumed that it will not incur any capex going forward.
- NESCO is a debt-free company and we have considered cost of equity of 16% to arrive at the present value of future cash flows. (Refer Exhibit 11).
- To arrive at the terminal value we have assumed long-term growth rate of 5% per annum, which is the same as the inflation rate. We have assumed capitalisation rate of 9% per annum (refer Exhibit 10). We have computed the terminal value at FY22E.
- After discounting future cash flows of hospitality segment we have arrived at a valuation of Rs823mn.

Exhibit 5: Current phase - Hospitality segment

Hospitality segment	FY18E	FY19E	FY20E	FY21E	FY22E
Revenues	**180**	**306**	**367**	**441**	**529**
PAT margin (%)	*15*	*15*	*15*	*15*	*15*
PAT	**27**	**46**	**55**	**66**	**79**
Add:Depreciation	3	3	3	3	3
Operational cash flow	**30**	**49**	**58**	**69**	**82**
Capital expenditure					
Cost of land (Rsmn)	-	-	-	-	-
Cost of construction (Rsmn)	-	-	-	-	-
Total capital expenditure	-	-	-	-	-
Projected cash flow	30	49	58	69	82
Discount rate (%)	-	-	-	*16*	*16*
Period (years)	-	-	-	1	2
Discount factor	-	-	-	0.86	0.74
DCF	-	-	-	59	61
PVOCF*	-	-	**120**	-	-
Terminal value	-	-	**703**	-	-
Valuation of hospitality segment (FY20E)	-	-	**823**	-	-

**PVOCF – Present Value of Future Cash Flows*

Source: Nirmal Bang Institutional Equities Research

Assumptions – Indabrator segment

- We have assumed flat revenues for FY18E and FY19E and a growth of about 5% over FY20E-FY22E.
- We have assumed PAT margin at 10%.
- We added depreciation to PAT to arrive at operating cash flow.
- We have assumed nil capital expenditure going forward.
- NESCO is a debt-free company and we have considered cost of equity of 16% to arrive at current value of future cash flow (refer Exhibit 11).
- To arrive at terminal value we have assumed long-term growth rate of 5% per annum, which is the same as the inflation rate. We have assumed capitalisation rate of 9% per annum (refer Exhibit 10). We have computed the terminal value at FY22E.
- After discounting future cash flows of Indabrator, we have arrived at a valuation of Rs669mn.

Exhibit 6: Current Phase – Indabrator segment

Indabrator segment	FY18E	FY19E	FY20E	FY21E	FY22E
Revenues (Rsmn)	339	339	356	374	392
PAT margin (%)	*10*	*10*	*10*	*10*	*10*
PAT (Rsmn)	34	34	36	37	39
Add: Depreciation	27	27	27	27	27
Operating cash flow	61	61	62	64	66
Capital expenditure					
Cost of land (Rsmn)	-	-	-	-	-
Cost of construction (Rsmn)	-	-	-	-	-
Total capital expenditure	-	-	-	-	-
Projected cash flow	61	61	62	64	66
Discount rate (%)	-	-	-	*16*	*16*
Period (years)	-	-	-	1	2
Discount factor	-	-	-	0.86	0.74
DCF	-	-	-	55	49
PVOCF*	-	-	**104**	-	-
Terminal value	-	-	**565**	-	-
Valuation of Indabrator (FY20E)	-	-	**669**	-	-

**PVOCF – Present value of future cash flows*

Source: Nirmal Bang Institutional Equities Research

Future Phase

Assumptions - NESCO IT Park

- Building 2 will have a leasable area of 1mn sqft and we expect revenues to flow in from FY24E.
- Occupancy rate for FY24E/FY25E/FY26E will be 40/80/100%, respectively.
- We have considered a lease rate of Rs141sqft/month (net of maintenance costs) for FY24E and assumed 5% per annum hike in rentals.
- We have multiplied the leasable area with the occupancy rate to get the rented area. Lease rate is multiplied with the rented area to arrive at revenues.
- We have subtracted depreciation from revenues to get EBIT and have considered income-tax at the rate of 30%.
- We have added back depreciation to PAT in order to arrive at operating cash flow.
- We have assumed capital expenditure of Rs4,800mn for Building 2, spread over FY20E-FY23E.
- NESCO is a debt-free company and we have considered cost of equity of 16% to arrive at the present value of future cash flow (refer Exhibit 11).
- To arrive at the terminal value we have assumed long-term growth rate of 5% per annum, which is the same as the inflation rate. Rental yields in the recent past have been in the range of 7.5%-8.0% per annum based on which we have assumed a conservative capitalisation rate of 9% per annum. We have computed the terminal value at FY26E.
- After discounting future cash flow of NESCO IT Park we have arrived at a valuation of Rs4,876mn.

Exhibit 7: Future phase - NESCO IT Park

NESCO IT Park	20E	21E	22E	23E	24E	25E	26E
Lease area (sqft)	-	-	-	-	1.00	1.00	1.00
Building 1	-	-	-	-	-	-	-
Building 2	-	-	-	-	1.00	1.00	1.00
Building 3	-	-	-	-	-	-	-
Building 4	-	-	-	-	-	-	-
Occupancy rate (%)							
Building 1	-	-	-	-	-	-	-
Building 2	-	-	-	-	40	80	100
Building 3	-	-	-	-	-	-	-
Building 4	-	-	-	-	-	-	-
Leasable area*occupancy rate	-	-	-	-	0.40	0.80	1.00
Lease rate (Rs/sqft)	116	122	128	134	141	148	155
Inflation-sale (%)	*5*	*5*	*5*	*5*	*5*	*5*	*5*
Number of months	12	12	12	12	12	12	12
Revenues	**-**	**-**	**-**	**-**	**675**	**1,418**	**1,862**
Inflation-cost (%)	*5*	*5*	*5*	*5*	*5*	*5*	*5*
Maintenance Rs/sqft/month	-	-	-	-	-	-	-
Maintenance costs (Rsmn)	-	-	-	-	-	-	-
Depreciation (Rsmn)	-	-	-	-	94	94	94
EBIT	**-**	**-**	**-**	**-**	**581**	**1,324**	**1,768**
Income-tax (%)	*30*	*30*	*30*	*30*	*30*	*30*	*30*
Income-tax (Rsmn)	-	-	-	-	174	397	530
Profit after tax	-	-	-	-	407	927	1,237
Add : Non-cash expenses	-	-	-	-	94	94	94
Operating cash flow	**-**	**-**	**-**	**-**	**501**	**1,021**	**1,331**
Capital expenditure							
Cost of land (Rsmn)	-	-	-	-	-	-	-
Cost of construction (Rsmn)	1,200	1,200	1,200	1,200		-	-
Total capital expenditure	**1,200**	**1,200**	**1,200**	**1,200**	**-**	**-**	**-**
Projected cash flow	(1,200)	(1,200)	(1,200)	(1,200)	501	1,021	1,331
Discount rate (%)	*16*	*16*	*16*	*16*	*16*	*16*	*16*
Period (years)	-	1	2	3	4	5	6
Discount factor	-	0.86	0.74	0.64	0.55	0.47	0.41
DCF	-	(1,033)	(890)	(766)	276	484	543
PVOFCF*	**(1,388)**	-	-	-	-	-	-
Terminal value	**6,264**	-	-	-	-	-	-
Valuation of NESCO IT Park (FY20E)	**4,876**	-	-	-	-	-	-

**PVOCF – Present Value of Future Cash Flows*

Source: Nirmal Bang Institutional Equities Research

Assumptions - Bombay Exhibition Centre: Convention centre (Phase 1)

- Convention centre is expected to have an additional leasable area of 0.45mn sqft and start generating revenues from FY23E.
- We expect occupancy rate of 40% over FY23E-FY26E. .
- We have considered lease rate at Rs30sqft/day for FY23E and assumed 5% per annum hike in rent.
- We have multiplied the leasable area with the occupancy rate to get the rented area. We have then multiplied the rented area with the lease rate to arrive at revenues.
- We have considered maintenance costs at 15% of revenues.
- We have subtracted depreciation and maintenance to arrive at EBIT.
- Income-tax rate is assumed at 30%.

- We have added back depreciation to PAT in order to arrive at operating cash flow.
- We have assumed capital expenditure of Rs2,000mn spread over FY19E-FY22E.
- NESCO is a debt-free company and we have considered cost of equity of 16% to arrive at the present value of future cash flows (refer Exhibit 11).
- To arrive at the terminal value, we have assumed long-term growth rate of 5% per annum, which is the same as the inflation rate. Rental yields in the recent past have been in the range of 7.5%-8.0% per annum based on which we have assumed a conservative capitalisation rate of 9% per annum. We have computed the terminal value at FY26E.
- After discounting future cash flows of Bombay Exhibition Centre (convention centre-phase1), we have arrived at a valuation of Rs8,281mn.

Exhibit 8: Bombay Exhibition Centre- Future phase

Bombay Exhibition Centre	FY19E	FY20E	FY21E	FY22E	FY23E	FY24E	FY25E	FY26E
Lease (mn sqft)	-	-	-	-	0.45	0.45	0.45	0.45
Occupancy rate (%)	-	-	-	-	*40*	*40*	*40*	*40*
Total number of days	-	-	-	-	365	365	365	365
Occupied days	-	-	-	-	146	146	146	146
Leasable area	-	-	-	-	0.45	0.45	0.45	0.45
Lease rate (Rs/sqft/day)	-	-	-	-	30	32	33	35
Inflation rate (%)	-	-	-	-	*5*	*5*	*5*	*5*
Revenues (Rsmn)	-	-	-	-	1,979	2,078	2,181	2,291
Maintenance as a % of revenues	-	-	-	-	15	15	15	15
Maintenance costs (Rsmn)	-	-	-	-	297	312	327	344
Less: Depreciation (Rsmn)	-	-	-	-	33	33	33	33
EBIT	-	-	-	-	1,649	1,733	1,821	1,914
Income-tax rate (%)	-	-	-	-	*30%*	*30%*	*30%*	*30%*
Income-tax (Rsmn)	-	-	-	-	495	520	546	574
PAT	-	-	-	-	1,154	1,213	1,275	1,340
Plus:Depreciation	-	-	-	-	33	33	33	33
Operating cash flow	-	-	-	-	1,187	1,246	1,308	1,373
Capital expenditure								
Cost of land (Rsmn)	-	-	-	-	-	-	-	-
Cost of construction (Rs mn)	500	500	500	500	-	-	-	-
Total capital expenditure	500	500	500	500	-	-	-	-
Projected cash flow	(500)	(500)	(500)	(500)	1,187	1,246	1,308	1,373
Discount rate (%)	*16*	*16*	*16*	*16*	*16*	*16*	*16*	*16*
Period (years)	-	-	1	2	3	4	5	6
Discount factor	-	-	0.86	0.74	0.64	0.55	0.47	0.41
DCF	-	-	(431)	(371)	758	685	619	560
PVOFCF*	-	**1,822**	-	-	-	-	-	-
Terminal value	-	**6,459**	-	-	-	-	-	-
Value of BEC (FY 20E)**	-	**8,281**	-	-	-	-	-	-

*** Bombay Exhibition Centre*

**PVOCF – Present Value of Future Cash Flows*

Source: Nirmal Bang Institutional Equities Research

Hotel segment valuation (Phase 1)

The company plans to build a hotel with 450 rooms which is expected to be operational by FY23E. To arrive at enterprise value of the hotel, we have considered the average EV/room multiple of comparable companies (not pure play comparables) and multiplying it by 450 rooms.

Assumptions - Bombay Exhibition Centre: Hotel (Phase 1)

Exhibit 9: Comparable Hotels EV/Room

Particulars	Number of rooms	EV/room
Byke Hospitality	733	10.18
Viceroy Hotels	473	11.56
Asian Hotels North	507	30.67
Indian Hotels	16675	11.75
Leela Hotels	2688	19.83
Oriental Hotels	666	17.66
Average	-	16.94

Source: Company, Nirmal Bang Institutional Equities Research

- We have assumed that the hotel will have around 450 rooms and will be operational by FY23E.
- We have multiplied the number of rooms to the average EV/room (refer Exhibit 9) of comparable companies to arrive at the enterprise value of hotel segment as of FY23E and then discounted it using cost of equity of 16% (refer Exhibit 11).
- We have considered capital expenditure of Rs4,500mn over FY19E-FY22E and subtracted it from the enterprise value to arrive at hotel segment's valuation of Rs3,066mn.

Key assumptions for NAV calculation

Our key assumptions for the purpose of calculation of NAV are given below:

- Assumed an inflation rate of 5% p.a. for rental increase.
- We have assumed a 5% p.a. increase in maintenance costs.
- We have considered a tax rate of 30%.
- Cash flows have been discounted using WACC of 16%.

Exhibit 10: Key assumptions

Discount rate	16%
Rate of inflation - Lease rate	5%
Rate of inflation - Maintenance cost	5%
Tax rate	30%
Cap rate – NESCO IT Park and BEC	9%
Cap rate – Hospitality and Indabrator	9%

Source: Nirmal Bang Institutional Equities Research

Exhibit 11: WACC calculation

The calculation of discount rate is given below:

Pre-tax cost of debt	**-**
Tax rate	30%
Cost of debt	0%
Risk-free rate	7%
Beta	0.75
Market premium	12%
Cost of equity	16%
WACC	**16%**
Debt	-
Equity	100%

Source: Nirmal Bang Institutional Equities Research

Key reasons for optimism

- Hospitality segment drives revenues in the short run, but commercial segment delivers over a long horizon
- EBITDA margin to remain above 70%.
- PAT margin at 50%, despite a decline in other income.
- One of the few players in real estate sector with a strong balance sheet.
- Healthy cash flow from operations throughout.
- RoE remains >14%, despite expansion plan and restructuring of the company.
- Stock trading at comfortable valuation.

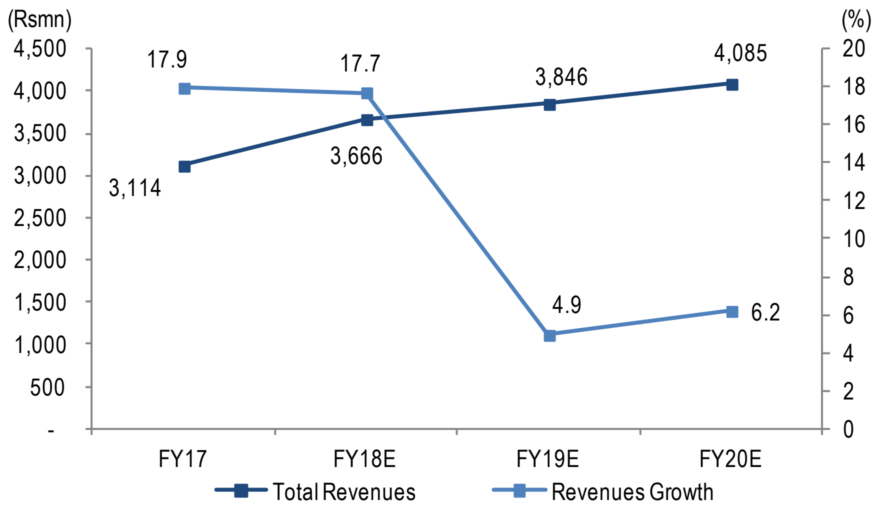
Hospitality segment drives revenues in the short run, but commercial segment delivers over a long horizon

We expect revenues to post 9% CAGR over FY17-FY20E. Revenues are derived from four segments namely: NESCO IT Part, Bombay Exhibition Centre, Hospitality and Indabrator. Revenue from NESCO IT Park is expected to decline at 13% CAGR over FY17-FY20E on account of ongoing restructuring. Bombay Exhibition Centre is likely to post revenue growth of 22% CAGR over FY17-FY20E supported by client stickiness. Revenue of Hospitality (food catering) segment is expected to grow at 86% CAGR over FY17-FY20E on account of increase in capacity utilisation. Revenues from Indabrator segment are expected to remain flat over FY17-FY20E.

Restructuring of NESCO IT Park includes: 1) Building 1 (approx 0.175mnsqft) to be demolished and the area to be utilised for Bombay Exhibition Centre, and so we have not considered lease rentals of Building 1 post FY18E. 2) Building 2 (approx. 0.175mnsqft) will be demolished and a new building will be constructed, the revenues of which shall start flowing post FY24E.

Lower revenue growth is countered by: 1) Increase in occupancy rate of Bombay Exhibition Centre from 35% in FY18E to 40% over FY19E and FY20E. 2) Increase in revenues from hospitality segment, considering the fact that the company will be able to increase the number of shifts per day from 1.5x to 3.0x. Hospitality segment can serve about 15,000 meals per shift (currently the capacity is under-utilised). The chart below shows our revenues estimates for FY17-FY20E:

Exhibit 12: Total revenues



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 13: Segmental revenues

Revenues	FY17	FY18E	FY19E	FY20E
NESCO IT Park	1,419	1,217	886	931
Growth (%)	*14*	*(14)*	*(27)*	*5*
Bombay Exhibition Centre	1,328	1,929	2,315	2,431
Growth (%)	*19*	*45*	*20*	*5*
Hospitality	57	180	306	367
Growth (%)	*155*	*217*	*70*	*20*
Indabrator	339	339	339	356
Growth (%)	*21*	*-*	*-*	*5*
Total revenues	**3,114**	**3,666**	**3,846**	**4,085**
Growth (%)	18	18	5	6

Source: Company, Nirmal Bang Institutional Equities Research

We have given the revenues expected from individual segments below.

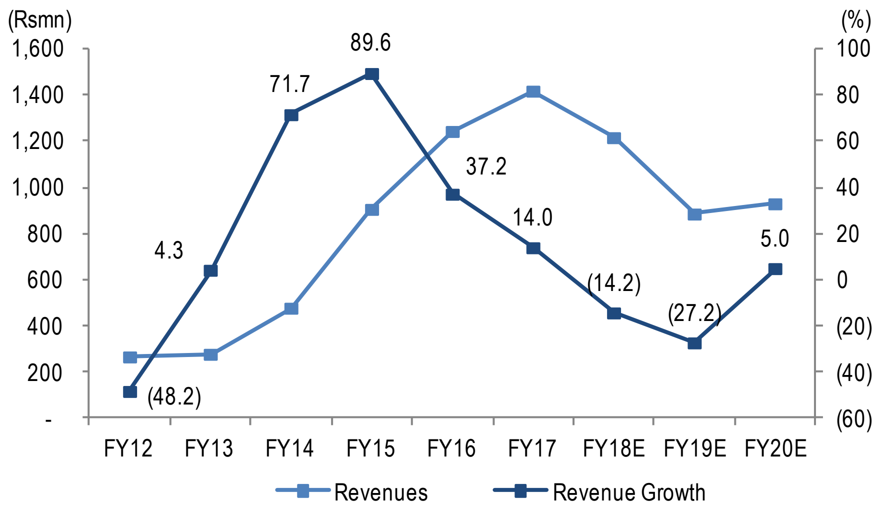
NESCO IT Park

NESCO IT Park contributes about 45% to total revenues. NESCO IT Park has a total of four buildings. Building 1 (appox. 0.175mn sqft) will be demolished and the area utilised for Bombay Exhibition Centre. Building 2 (approx. 0.175mn sqft) will be demolished and another building will be constructed, the revenues of which shall flow post FY24E. Building 4, is under construction and will contribute to revenues post FY21E (leasable area of 1.2mn sqft). Building 3, with area of 0.67mn sqft, will remain operational throughout.

Historically, the revenues of NESCO IT Park have posted 40% CAGR over FY12-FY17. The reasons attributable for higher growth are: 1) Lower base on account of slowdown in the economies of Europe, US and India which adversely hit the demand for IT space. 2) NESCO completed Building 3 in FY12 and started finalising licencing arrangements in FY13. 3) Building 1, 2 and 3 achieved full occupancy in FY15.

Going forward, we expect the segment to post 13% CAGR decline over FY17-FY20E on account of demolition of Buildings 1 and 2. Over a longer horizon, we expect revenues from NESCO IT Park to post 20% CAGR over FY18E-FY23E, primarily driven by addition of Building 4 in FY21E and it reaching 100% occupancy by FY23E.

Exhibit 14: Revenues of NESCO IT Park



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 15: Major clients of NESCO IT Park

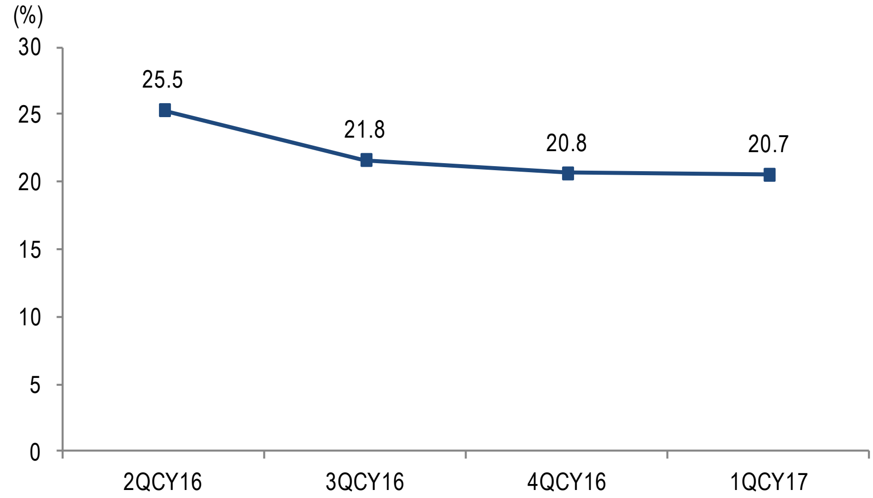
NESCO IT Park – Tenant Profile			
TCS	HSBC	MSCI	KPMG
Ericsson	PwC	Endurance	HERE
BlackRock	Aegon	Intelenet	Integreon

Source: Company

Vacancy rates show a declining trend in Malad/Goregaon region

In Exhibit 16, we see that vacancy rate has declined in Malad/Goregaon from 26% in 2QCY16 to 21% in 1QCY17. We have taken a conservative approach in our estimates and expect Building 4 to achieve full occupancy over a three-year period (FY21E-FY23E).

Exhibit 16: Malad/Goregaon vacancy rate (Grade A – commercial offices)



Source: cushman&wakefield

Historical vacancy rates in Mumbai Metropolitan Region or MMR

Vacancy rate in Malad/Goregaon, Andheri-Kurla, SBD (Secondary Business District) and Vashi witnessed a decline from 2QCY16 levels whereas in areas like CBD (Central Business District), Thane-Belapur and Worli there was an increase in vacancy rate.

Exhibit 17: Commercial offices vacancy rates – Grade A

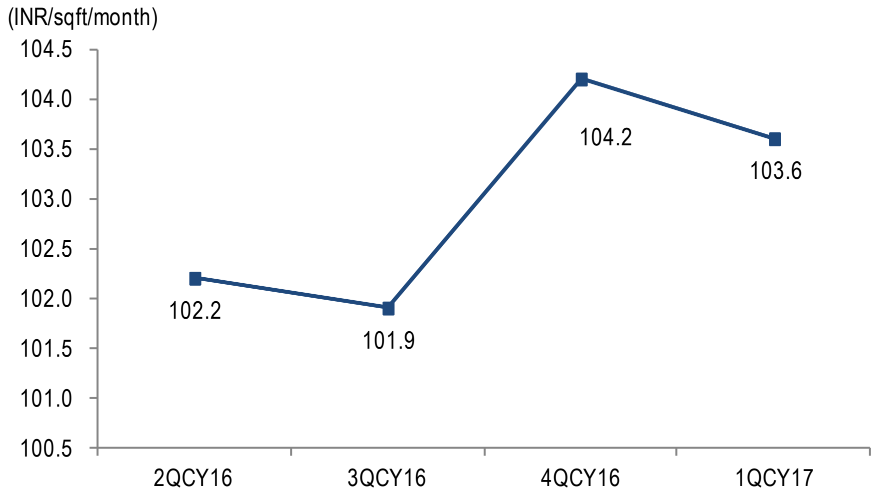
Commercial Offices Vacancy Rates – Grade A				
(%)	**2QCY16**	**3QCY16**	**4QCY16**	**1QCY17**
CBD	7	7	9	9
SBD	25	24	21	21
Worli	14	25	25	24
Lower Parel	13	12	13	13
Andheri-Kurla	20	19	19	19
Powai	4	4	4	4
Malad/Goregaon	26	22	21	21
Vashi	9	7	7	7
Thane-Belaur Road	10	20	19	19
Thane	21	20	20	20
Average	**16**	**19**	**18**	**18**

Source: Cushman & Wakefield

Decline in vacancy rate supported by increase in average asking rent

Average asking rent in case of Malad/Goregaon commercial offices increased from Rs102 (sqft/month) in 2QCY16 to Rs104 (sqft/month) in 1QCY17. We believe that if the vacancy rate continues to fall, there could be a further increase in lease rate which supports our assumption of lease rate increasing at 5% p.a. (inflation rate).

Exhibit 18: Average asking rent (INR/sqft/month) – Malad/Goregaon



Source: Cushman & Wakefield

Average asking rent in Mumbai Metropolitan Region or MMR

Areas like Malad/Goregaon, Thane and Vashi witnessed an increase in average rental rates from 2QCY16 onwards, while areas like Worli and Powai registered a decline in average asking rent.

Exhibit 19: Average Asking Rent – Commercial offices Grade A

Average asking rent – Commercial offices Grade A				
Region/Average Asking Rent	**2QCY16**	**3QCY16**	**4QCY16**	**1QCY17**
CBD	221	223	223	225
SBD	278	276	280	262
Worli	233	223	225	224
Lower Parel	176	177	176	176
Andheri-Kurla	118	118	118	118
Powai	109	108	108	108
Malad/Goregaon	102	102	104	104
Vashi	82	83	83	83
Thane-Belapur Road	45	45	45	45
Thane	56	56	58	58

Source: Cushman & Wakefield

Bombay Exhibition Centre

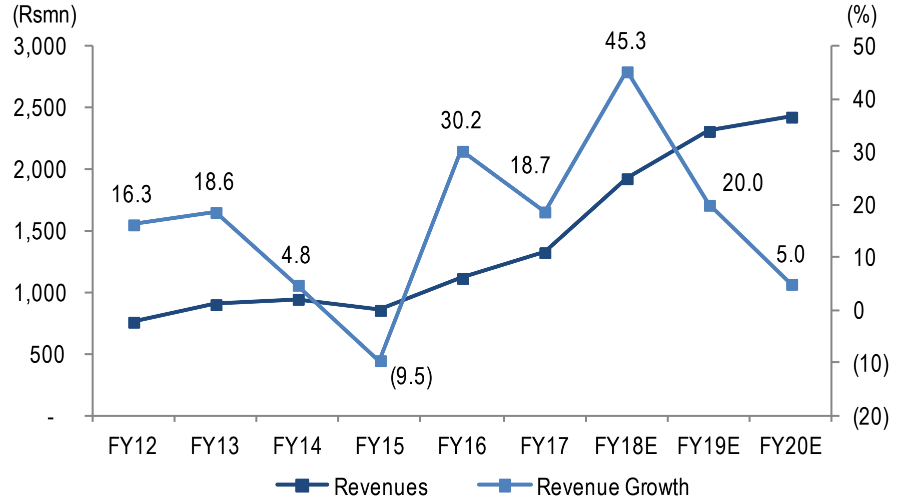
Bombay Exhibition Centre (BEC) contributes about 42% to total revenues of NESCO. Bombay Exhibition Centre held about 109 exhibitions in FY17 with 27 new organisers. The total leasable area of BEC in FY17 was 0.5mn sqft. With an addition of 0.14mn sqft in FY18E, the total rentable area for BEC goes to 0.64mn sqft.

Historically, revenues of Bombay Exhibition Centre have shown a consistent upmove and posted 12% CAGR over FY12-FY17. Going forward, we expect the revenues from BEC segment to post 22% CAGR over FY17-FY20E.

The primary drivers of growth are: 1) Increase in lease rate (Rs24sqft/day) at 5% p.a. (inflation rate) over FY18E-FY20E. 2) Increase in occupancy rate from 35% in FY18E to 40% in FY19E and FY20E. 3) Client stickiness. We want to highlight the fact that the number of exhibitions in FY17 have come down to 109 from 156 exhibitions in FY16. Despite a decline in the number of exhibitions, the increased contribution from existing clients led to revenue growth of 19% in FY17. We expect further growth post FY23E with an addition of 0.45mn sqft from convention centre (Phase1).

Under Phase 1 of expansion plan, the company plans to build a hotel with 450 keys. Revenues from the hotel segment are expected to flow in post FY23E.

Exhibit 20: Revenues of Bombay Exhibition Centre



Source: Company, Nirmal Bang Institutional Equities Research

The major clients of Bombay Exhibition Centre are given in the table below.

Exhibit 21: Major clients of bombay exhibition centre

Overseas organisers	National organisers
UBM/CMP	All India Plastic Manufacturers' Association
Reeds	Clothing Manufacturers' Association of India
Montgomery	Gems and Jewelry Export Promotion Council
IIR	Indian Electrical and Electronics Manufacturers' Association
Messe Dusseldorf	All India Photography Trade and Industry Association
Messe Frankfurt	Jasubhai Media Pvt. Ltd.
Koeln Messe	Confederation of Indian Industry (CII)
Messe Nurnberg	Federation of Indian Chambers of Commerce and Industry (FICCI)
Messe Hannover	Asian Business Exhibitions and Conferences (ABEC)

Source: Company

Competitor

Bombay Exhibition Centre is the largest exhibition centre in Mumbai with a leasable area of 0.64mn sqft (potential leasable area of 4.5mn sqft). The only competitor is CIDCO with 0.32mn sqft of leasable area, split into Exhibition Centre- 0.23mn sqft, Business Centre- 0.08mn sqft and the remaining into maintenance and administrative office.

As highlighted by the management, 80% of the clients are repetitive which provides a cushion in terms of risk from competitors. Existing organisers have not only kept the segment revenues stable, but also contributed to incremental revenues.

Exhibit 22: Bombay Exhibition Centre vs CIDCO

Particulars	Area (mnsqft)	Location
Bombay Exhibition Centre	0.64mn sqft- Current, 4.5mn sqft - potential	Goregaon
CIDCO	0.32mn sqft	Vashi

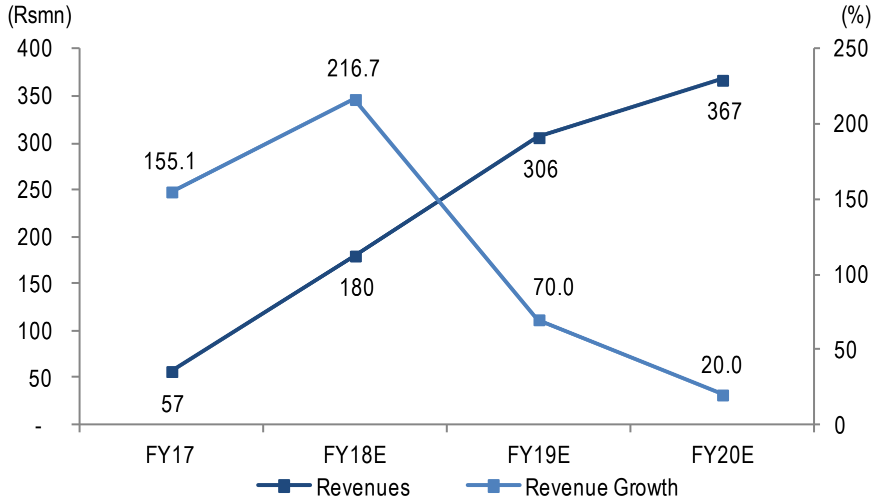
Source: Company, Nirmal Bang Institutional Equities Research

Hospitality/food catering segment (subsidiary)

The hospitality segment contributed about 2% to total revenues in FY17 and has potential to touch 10% by FY20E. The company recently commissioned two food courts and set up a kitchen facility of about 24,000sqft. Various national and international food brands are also available within the NESCO complex.

We expect 86% CAGR for hospitality segment over FY17-FY20E. We believe hospitality segment will be able to achieve such astonishing growth on account of: 1) Increase in the number of shifts per day from 1.5x to 3.0x. 2) Increase in the number of meals per shift (capacity of 15,000 meals per shift is currently under-utilised and is expected to increase).

Exhibit 23: Revenues - Hospitality segment



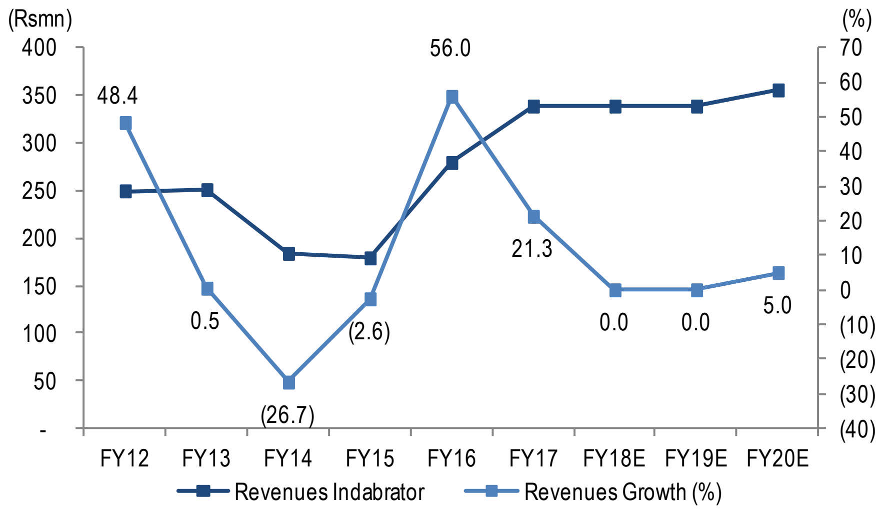
Source: Company, Nirmal Bang Institutional Equities Research

Indabrator segment

Indabrator segment accounts for 11% of total revenues. There are three manufacturing units located in Gujarat. The segment caters to automobile, railway, forging and foundry industry. Historically, the revenues have posted a moderate 6% CAGR over FY12-FY17. In FY14 and FY15, the segment witnessed a decline on account of various projects getting cancelled or delayed because of slowdown in demand from automobile and other sectors.

Going forward, we have considered flat revenues over FY18E-FY19E and a marginal growth of 5% in FY20E. We have a neutral view on this segment because: 1) Indabrator segment has posted 2% CAGR over FY09-FY17. 2) 60% of the segment's revenues are derived from automobile and railway sectors. The company has witnessed a major decline in revenues historically because of slowdown in sectors like automobile. The segment has concentration risk and is one of the primary reasons for our flattish revenue outlook.

Exhibit 24: Indabrator segment's revenues

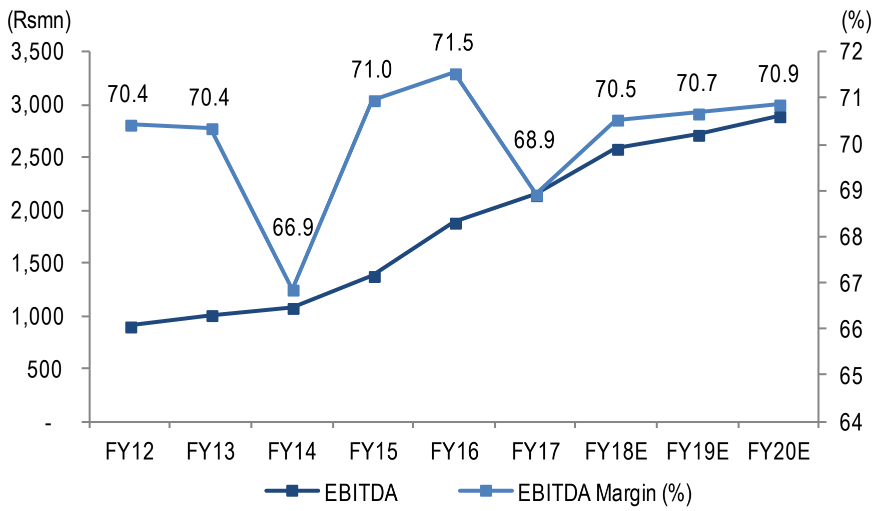


Source: Company, Nirmal Bang Institutional Equities Research

EBITDA margin to remain above 70%

Historically, EBITDA margin has been in the range of 67%-72% over FY12-FY17. We expect EBITDA margin to remain above70% over FY18E-FY20E. We have assumed cost increase in proportion to incremental revenues, keeping EBITDA margin constant.

Exhibit 25: EBITDA margin

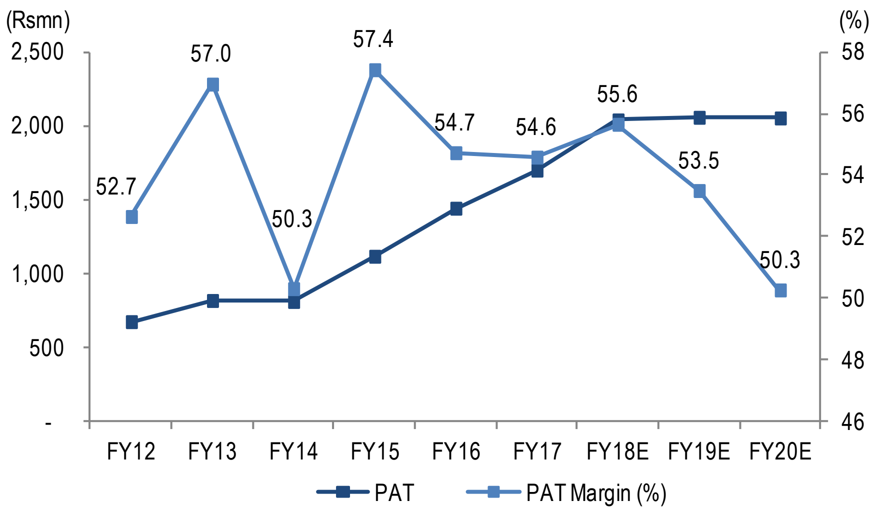


Source: Company, Nirmal Bang Institutional Equities Research

PAT margin at 50% despite a decline in other income

Historically, PAT margin has been in the range of 50%-57% over FY12-FY17. We expect PAT margin to decline from 55% in FY17 to 50% in FY20E. We have assumed a decline in PAT margin on account of lower other income. In order to incur capital expenditure for Building 4 (NESCO IT Park) and Phase 1 (hotel, convention centre and auditorium), operating cash flow will not be sufficient and sale of investments to the tune of Rs3,250mn will be required in FY19E and FY20E. Lower investments will translate into lower other income, thereby leading to a drop in PAT margin.

Exhibit 26: PAT margin

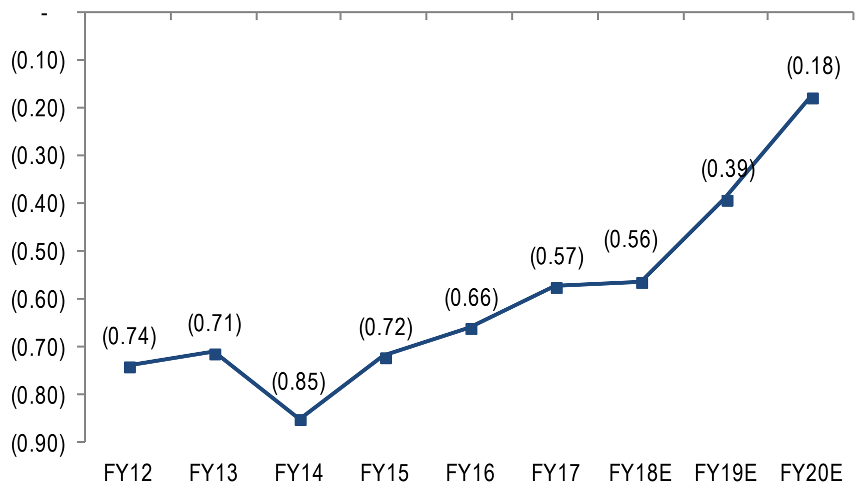


Source: Company, Nirmal Bang Institutional Equities Research

One of the few players in real estate sector with a clean balance sheet

Net debt-to-equity ratio of NESCO has been in the range of (0.85)-(0.57) over FY12-FY17. The company has zero debt since FY12 and plans to remain debt-free going forward. NESCO may sell some investments in FY19 and FY20 for making capital expenditure on Building 4 and Phase 1 (auditorium, hotel and convention centre). Sale of investments will increase the net debt-to-equity ratio to (0.18) in FY20E.

Exhibit 27: Net debt-to-equity ratio*



**Net debt = (Short+long-term debt) – (cash+short-term investments)*

Source: Company, Nirmal Bang Institutional Equities Research

Net debt-to-equity ratios of comparable companies

Though not pure play comparables, we have highlighted the net debt-to-equity ratio of major real estate players in Exhibit 28. Average net debt-to-equity ratio of realty players was 1.04 in FY17 vs. (0.57) of NESCO.

Exhibit 28: Net debt-to-equity ratio – real estate

Net debt-to-equity ratios of various players	FY12	FY13	FY14	FY15	FY16	FY17
DLF	0.85	0.82	0.66	0.74	0.81	0.91
Godrej Properties	1.06	1.05	0.85	1.35	1.74	1.95
Oberoi Realty	(0.35)	(0.26)	(0.11)	0.13	0.01	0.05
Prestige Estate	0.61	0.62	0.71	0.75	1.03	1.12
Sunteck Realty	0.68	0.97	0.86	0.63	0.67	0.42
Sobha	0.08	0.62	0.58	0.78	0.82	0.78
Phoenix Mills	0.72	0.88	1.31	1.43	1.59	1.33
Indiabulls Realty	0.25	0.62	0.38	0.77	1.53	1.75
Average	**0.49**	**0.66**	**0.66**	**0.82**	**1.03**	**1.04**
NESCO	**(0.72)**	**(0.71)**	**(0.84)**	**(0.71)**	**(0.65)**	**(0.57)**

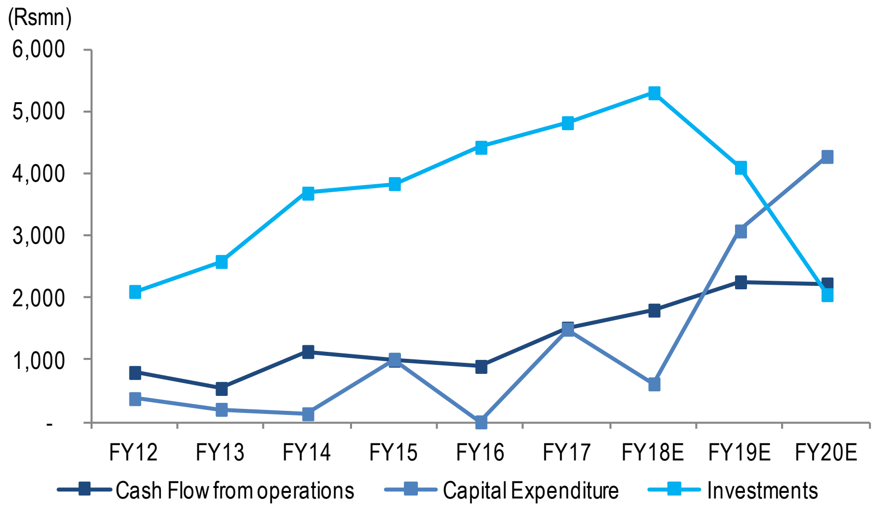
**Net debt = (Short+long-term debt) – (cash+short-term investments)*

Source: Bloomberg, Nirmal Bang Institutional Equities Research

Healthy cash flow from operations

NESCO had positive cash flow from operations over FY12-FY17 and we believe it will continue going forward. Historically, the company (except in FY15) had cash flow from operations that exceeded its capital expenditure requirement which makes us more confident that it will be able to execute the expansion plan (Building 4 and Phase1) with ease. Though the company's operating cash flows will not suffice for its aggressive expansion plan for FY19E and FY20E, it has investments worth Rs4,818mn which act as a support for its growth-oriented strategy.

Exhibit 29: Cash flow

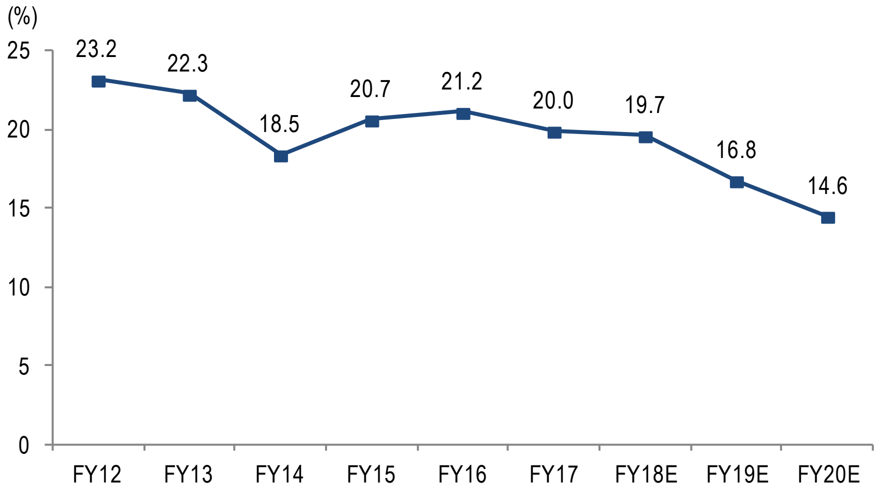


Source: Company, Nirmal Bang Institutional Equities Research

RoE remains >14%, despite expansion plan and restructuring of the company

NESCO has delivered RoE (Return on Equity) in the range of 18%-23% over FY12-FY17. We expect RoE to decline to 15% in FY20E on account of:1) Decline in other income (discussed earlier), 2) Likely decline in asset turnover from 0.30 in FY17 to 0.26 in FY20E. Asset turnover will decline because of expansion plan and restructuring undertaken by the company.

Exhibit 30: Return on equity



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 31: DuPont analysis

DuPont analysis	FY12	FY13	FY14	FY15	FY16	FY17	FY18E	FY19E	FY20E
EBIT margin (%)	*68%*	*66%*	*60%*	*68%*	*69%*	*66%*	*69%*	*69%*	*69%*
PAT/EBT	0.63	0.62	0.59	0.59	0.60	0.60	0.61	0.63	0.67
EBT/EBIT	1.23	1.39	1.42	1.43	1.32	1.37	1.34	1.24	1.09
Asset turnover	0.34	0.32	0.29	0.29	0.31	0.30	0.31	0.28	0.26
Leverage	1.31	1.22	1.28	1.25	1.23	1.21	1.14	1.13	1.12
RoE (%)	***23%***	***22%***	***18%***	***21%***	***21%***	***20%***	***20%***	***17%***	***15%***

Source: Company, Nirmal Bang Institutional Equities Research

Management strategy

NESCO's management to continue focus on two major segments: NESCO IT Park and Bombay Exhibition Centre (flagship businesses). The company plans to enter into event management business where it will be the organiser. The management believes that events could be conducted on days when the exhibition centre is unoccupied, thereby not sacrificing revenues from the exhibition centre.

We have already discussed about Phase 1 expansion, completing construction of Building 4 (FY21E) and Building 2 (FY24E). Now we shall consider a long-time horizon where the management's strategy will focus on executing Phase 2, 3 and 4.

> Phase2 and 4 includes construction and completion of exhibition hall.

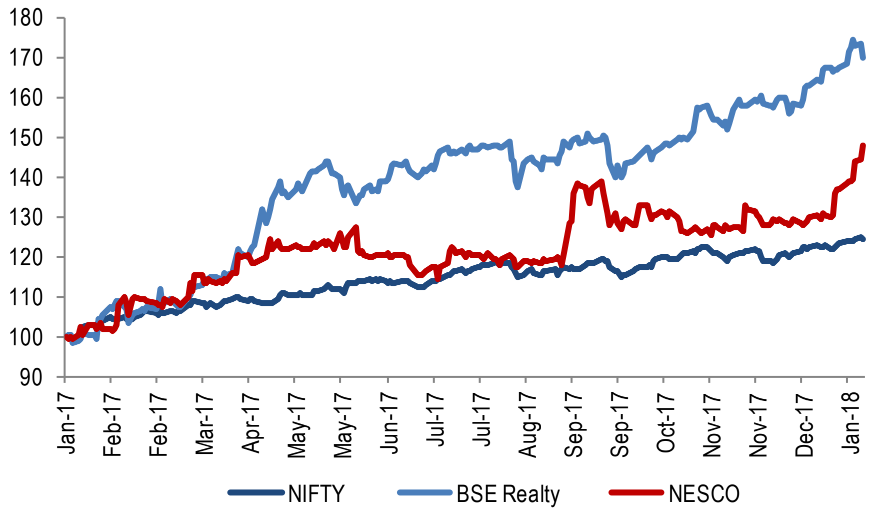
> Phase 3 includes construction and completion of food court, gaming arena, hotels and utilities centre.

NESCO has 70 acres of land parcel (58 acres leasable) located in Goregaon, Mumbai. Of the total 58 acres, 25 acres of land with a FSI of 4 is available for Bombay Exhibition Centre and 33 acres of land with a FSI of 3 will be available for NESCO IT Park. NESCO does not plan to sell any part of the land and at some time in future and may even consider buying additional land.

NESCO stock has outperformed Nifty in the past one year

NESCO stock has outperformed Nifty, but underperformed BSE Realty Index. BSE Realty Index includes pure residential companies and a combination of residential and commercial/retail real estate companies. NESCO gets categorised into pure commercial real estate company which has no pure-play comparable. We have highlighted in our initiating coverage report on the real estate sector that valuation of realty companies look stretched and had given our bearish outlook on the sector. However, NESCO stock has underperformed as compared to BSE Realty Index which gives us comfort in terms of reasonableness of valuation.

Exhibit 32: NESCO stock outperformed Nifty over the past one year



Source: Nirmal Bang Institutional Equities Research

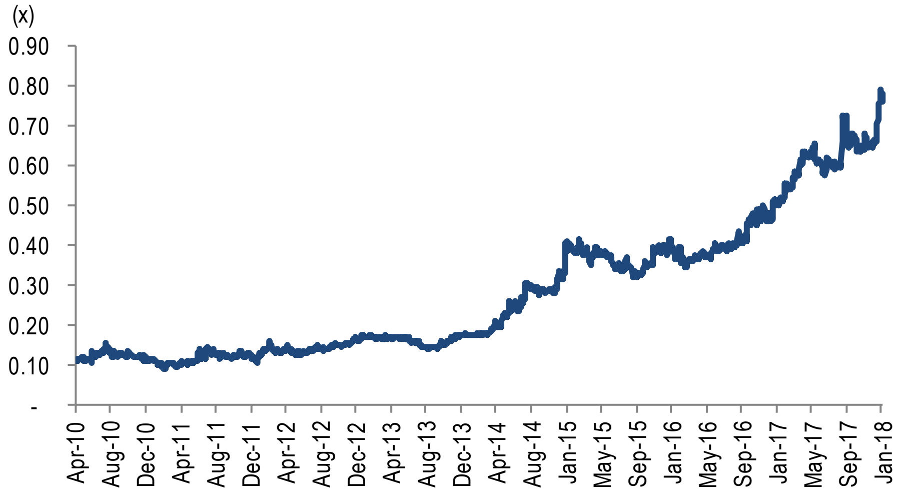
Stock trades at attractive valuation - we expect the outperformance to continue

NESCO stock currently trades at 3.1x FY20E P/BV and 0.8x FY20E P/NAV, which is justified considering our bullish overhang. Historically, the stock has traded between 0.09x-0.79x FY20E P/NAV.

Given the growth strategy of NESCO, we expect the outperformance to continue. Our optimism is driven by: 1) Attractive valuation. 2) Post completion of restructuring, addition of leasable area (1.2mn sqft) from Building 4 (FY21E). 3) Strong balance sheet with net cash balance 4) Positive free cash flow. 5) Increase in occupancy rate of Bombay Exhibition Centre.6) In addition to the above mentioned factors, the company also plans to construct a convention centre, auditorium and hotel which will be a part of Phase 1 of its future expansion plan. NESCO also plans to reconstruct Building 2 with higher FSI.

In our SOTP valuation we have considered only 3.96mn sqft of leasable area for NESCO IT Park and Bombay Exhibition Centre. Over a 20-year horizon, the management plans to utilise 4.5mn sqft of leasable area for Bombay Exhibition Centre and 5mn sqft of leasable area for NESCO IT Park.

Exhibit 33: Price/forward NAV



Source: Company, Nirmal Bang Institutional Equities Research

Company background

Established in April 1939 as New Standard Engineering Company, NESCO is known as a tool manufacturer as it introduced in India world class processes and designs for the manufacture of a number of engineering products. Equipment such as forging hammers and presses, blow room lines and high production cards for the textile industry, and sucker rod pumps for onshore oil recovery were some of the main product lines.

In order to reflect on the various new avenues that the company was entering into, the promoters of New Standard Engineering Company decided to change the name to NESCO. This reflected the company's transformation from a pure-play engineering company to that of a diversified one whose diversification entailed it to be a player in the services segment.

The company originally operated from Byculla, Mumbai, and set up two more plants at Parel and Santacruz. In 1959, it consolidated all these three operations and moved to a 70-acre estate on the Western Express Highway at Goregaon in Mumbai.

In 1986, the company diversified into realty business by developing and providing customised built-up space for multinational companies and leading corporates at Goregaon.

In 1992, the company set up an exhibition centre - known as Bombay Exhibition Centre - at its complex on the Western Express Highway at Goregaon.

The company currently operates in four segments namely: 1) NESCO IT Park, 2) Bombay Exhibition Centre, 3) Hospitality segment, and 4) Indabrator.

Exhibit 34: Key shareholders

Promoter and promoter group	68.18%
Mutual funds	-
Franklin India Smaller Companies Fund	3.98%
Foreign portfolio investors	2.04%
Foreign institutions/banks	0.04%
Non-institutions	-
Others	23.36%
Investor Education and Protection Fund	1.05%
Authority Ministry of Corporate Affairs	
Catamaran Advisors LLP	1.35%

Source: Bse india

Key Management Profile:

1) Sumant J Patel (Chairman)

Sumant J Patel is the executive chairman of NESCO. He graduated from university of Pennsylvania in 1959. Sumant J Patel played a key role in purchasing approximately 65 acres of land in Goregaon and centralizing all business units at Goregaon, Mumbai. He had taken the responsibility of transforming NESCO from a pure engineering company into a diversified one with the establishment of Bombay exhibition centre and NESCO IT Park. Some of the other key responsibilities held were: President, All India Manufacturers Organisation; Member, Engineering Export Promotion Council etc.

Financials

Exhibit 35: Income statement

Y/E March (Rsmn)	FY16	FY17	FY18E	FY19E	FY20E
Net sales	**2,635**	**3,114**	**3,666**	**3,846**	**4,085**
Growth YoY (%)	*35.5*	*18.2*	*17.7*	*4.9*	*6.2*
COGS	146	179	205	215	228
Operating Costs	405	560	569	592	621
Other expenses	**198**	**230**	**306**	**321**	**341**
EBITDA	**1,885**	**2,146**	**2,586**	**2,719**	**2,895**
EBITDA growth (%)	***36.6***	***13.8***	***20.5***	***5.1***	***6.5***
EBITDA margin (%)	***71.5***	***68.9***	***70.5***	***70.7***	***70.9***
Depreciation	67	81	75	75	75
EBIT	**1,818**	**2,065**	**2,511**	**2,644**	**2,820**
EBIT (%)	***69.0***	***66.3***	***68.5***	***68.7***	***69.0***
Interest expense	40	50	50	50	50
Other income	329	430	473	366	183
Earnings before tax	**2,108**	**2,445**	**2,934**	**2,959**	**2,953**
Tax- total	666	745	894	902	900
Rate of tax (%)	*31.6*	*30.5*	*30.5*	*30.5*	*30.5*
Net profit	**1,442**	**1,700**	**2,040**	**2,057**	**2,053**
% growth	*29.2*	*17.9*	*20.0*	*0.9*	*(0.2)*
EPS (FD)	20	24	29	29	29
% growth	*29.2*	*17.9*	*20.0*	*0.9*	*(0.2)*
Net DPS	3.00	-	2.28	2.30	2.30
Net Payout ratio (%)	*14.7*	*0.0*	*7.9*	*7.9*	*7.9*

Source: Company, Nirmal Bang Institutional Equities Research, Note: Based on Igaap

Exhibit 36: Cash flow

Y/E March (Rsmn)	FY16	FY17	FY18E	FY19E	FY20E
Profit after Tax	1,442	1,700	2,040	2,058	2,053
Depreciation	67	81	75	75	75
Finanace costs	40	50	50	50	50
Other Income	(329)	(430)	-	-	-
Working capital changes	(324)	109	(364)	73	43
Operating Cash Flow	**895**	**1,511**	**1,801**	**2,256**	**2,221**
Capital Expenditure	(2)	(1,493)	(613)	(3,075)	(4,275)
Net Cash After Capex	**894**	**17**	**1,187**	**(819)**	**(2,054)**
Other income/(expense)	(252)	34	(482)	1,200	2,050
Proceeds/Repayment of borrowings	-	-	-	-	-
Finance costs	(40)	(50)	(50)	(50)	(50)
Dividend & dividend distribution tax	(251)	-	(188)	(190)	(190)
Cash flow from Financing	**(291)**	**(50)**	**(239)**	**(240)**	**(240)**
Total Cash Generation	**18**	**(8)**	**469**	**141**	**(243)**
Opening Cash Balance	48	65	57	526	666
Closing Cash & Bank Balance	**65**	**57**	**526**	**666**	**423**

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 37: Balance sheet

Y/E March (Rsmn)	FY16	FY17	FY18E	FY19E	FY20E
Share capital	141	141	141	141	141
Reserves and surplus	6,672	8,370	10,222	12,090	13,953
Net worth	**6,813**	**8,511**	**10,363**	**12,231**	**14,094**
Loans	-	-	-	-	-
Other Financial Liabilities	687	721	194	141	148
Provisions	140	128	128	128	128
Deferred Tax Liability	163	273	273	273	273
Other Non- Current Liability	108	77	-	-	-
Total capital employed	**7,911**	**9,709**	**10,957**	**12,772**	**14,643**
Property, Plant and Equipment	3,082	4,500	5,039	8,039	12,240
Investments	-	-	-	-	-
Loans	22	28	28	28	28
Other Non-Current Assets	447	499	499	499	499
Total Non-Current Assets	**3,552**	**5,027**	**5,565**	**8,566**	**12,766**
Trade Payables	94	229	262	275	292
Other Financial Liabilities	400	392	638	766	804
Other current liabilities	-	-	-	-	-
Provisions (Current)	2	3	3	3	3
Total Current Liabiities	**495**	**624**	**903**	**1,044**	**1,099**
Inventories	110	134	152	159	169
Investments	4,422	4,818	5,300	4,100	2,050
Trade receivables	146	121	143	150	159
Cash and Bank Balance	65	57	526	666	423
Current Tax Assets (Net)	0	0	0	0	0
Other Current Assets	**110**	**175**	**175**	**175**	**175**
Total Current Assets	**4,854**	**5,305**	**6,295**	**5,250**	**2,976**
Net Current Assets	**4,358**	**4,681**	**5,392**	**4,206**	**1,877**
Total Capital Employed	**7,911**	**9,709**	**10,957**	**12,772**	**14,643**

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 38: Key ratios

Y/E March	FY16	FY17	FY18E	FY19E	FY20E
Profitability and return ratios					
EBITDA margin (%)	71.5	68.9	70.5	70.7	70.9
EBIT margin (%)	69.0	66.3	68.5	68.7	69.0
Net profit margin (%)	54.7	54.6	55.6	53.5	50.3
RoE (%)	21.2	20.0	19.7	16.8	14.6
RoCE (%)	23.0	21.3	22.9	20.7	19.3
Working capital & liquidity ratios					
Recievables (days)	20	14	14	14	14
Inventory (days)	311	271	271	271	271
Payables (days)	233	467	467	467	467
Current ratio (x)	9.8	8.5	7.0	5.0	2.7
Valuation ratios					
EV/sales (x)	16.4	13.8	11.8	11.2	10.6
EV/EBITDA (x)	22.9	20.1	16.7	15.9	14.9
P/E (x)	29.9	25.4	21.2	21.0	21.0
P/BV (x)	6.3	5.1	4.2	3.5	3.1

Source: Company, Nirmal Bang Institutional Equities Research

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