Introduction

Karda Constructions Limited (KCL), founded in 1994 and incorporated in 2007, is a real estate developer and a civil contractor. The 26-year-old company primarily conducts business in the city of Nashik in Maharashtra. Initially, KCL concentrated only on the affordable segment but now has become one of the leading real estate developers in Nashik (developments under the "Hari" brand name) with a diverse range of projects ranging from affordable to luxury. The Company is looking to ramp up on its commercial portfolio as well. KCL, in the last couple of years, has also entered the construction contracts space to further diversify its offerings and de-risk its business model.

Key Market Indicators	
Latest Date	14-Aug-2020
Latest Price (₹)	83.50
52 Week High (₹)	84.70
52 Week Low (₹)	18.00
Beta	0.60
Face Value (₹)	2.00
Industry P/E	21.13
Industry P/BV	1.03
TTM Period	202003
TTM EPS (₹)	1.57
TTM PE (x)	48.98
Price/BV (x)	4.57
EV/TTM EBIDTA (x)	18.79
EV/TTM Sales (x)	5.20
Dividend Yield (%)	0.00
MCap/TTM Sales (x)	4.14
Latest Book Value (₹)	16.78
Market Cap (₹ In Crores)	470.47
EV (₹ In Crores)	593.78
Latest no. of shares (In Crores)	6.15

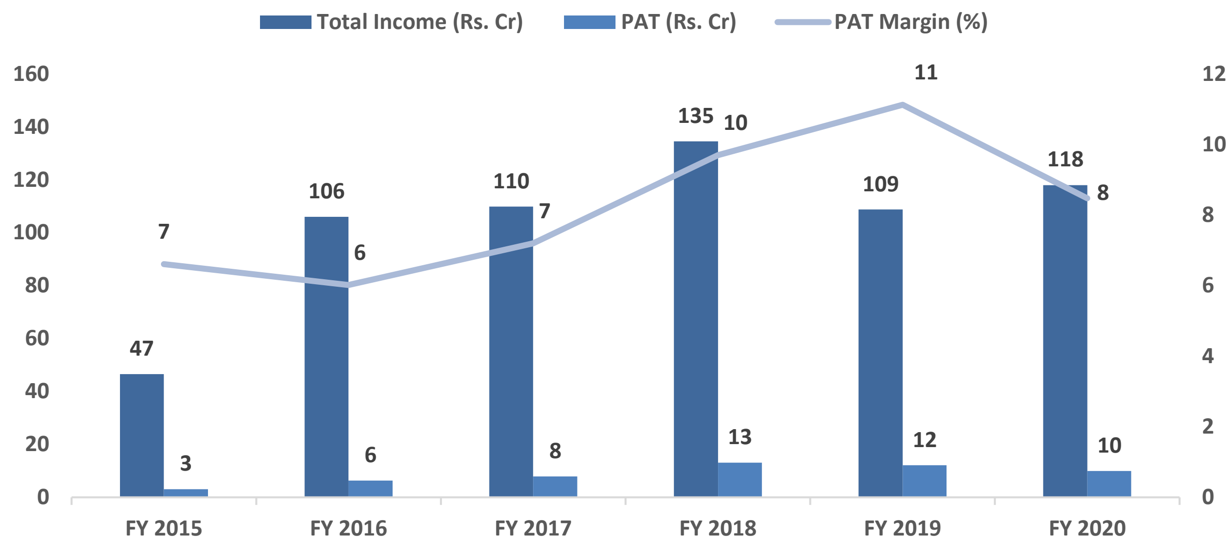
Source: Ace Equity

Share Holding Pattern as on June 2020	
Promoter (%)	65.16
FII (%)	0.28
Free Float (%)	34.84

Source: Ace Equity

Financial Performance

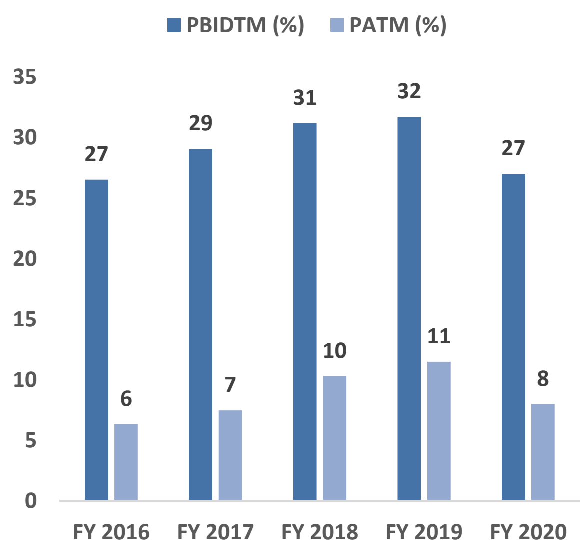
Exhibit 1: Key Financials

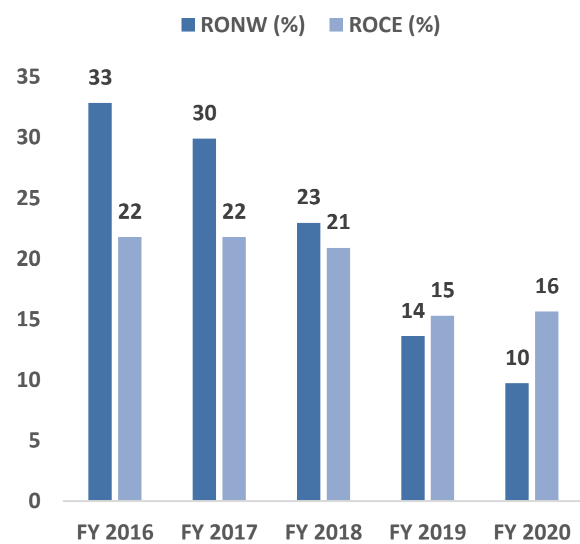


Source: Ace Equity

The total income for the company has growth at a 5-year CAGR of 20%. Margins have also seen a substantial improvement (up by 400 bps) over the past 4 years barring the most recent financial year.

Exhibit 2: Margins and Ratios





Source: Ace Equity

Key Points

Track-record

The Company, which was founded in 1994, has a track-record of over 25 years in the real estate sector with 65 projects (>31 lakh sqft delivered) till date.

Healthy Pipeline

KCL has multiple ongoing and planned projects in the pipeline with a total deliverable area of ~32 lakh sqft. Its diversified orderbook between residential and commercial is also a good strategy in terms of de-risking its operations. Given the projects in hand the company seems well placed to achieve 15% income CAGR for the next 3 years.

Margin Expansion

All the old projects of the company were on a sale model where they would purchase the land and then make sales. These projects were more capital intensive and hence the interest component would bring the net margins down but the new projects they will develop are on a revenue sharing (joint venture) model where they do not purchase the land by way of loan funds, leading to savings in interest which in turn will lead to net margin expansion.

More Joint Venture Deals on the Cards

The landlords in Nashik, due to a decrease in the outright sale model, have started to prefer the joint venture/development model. This opens up a lot of opportunities for the company as more land becomes developable than before.

Focus on Mid-Size Projects

The Company does not believe in developing projects which are of more than 300-400 units because the absorption of such units becomes difficult for a market like Nashik. The Company, having witnessed the low execution and sales traction of larger projects (built on 30-40 acres), believes in selling all their units by the time 80% of their project is complete. This allows the company to finish off a project in three years, unlock the capital invested, and redeploy it in the next project.

In-house Construction

The Company has focused on building its own projects and not sub-contracting them. This has also helped them in the civil construction business where they focus on building construction contracts since they already have expertise in the building construction space.

Diversified and Changing Development Mix

The Company has chosen to be a developer across the entire residential spectrum, from affordable to luxury. This allows the company to focus on a particular segment as per the current demand and not rely only on one segment. Up to FY'19, the Company's residential portfolio constituted almost 95-98%. Since the sales traction in the residential segment was not very strong in the last couple of years compared to the commercial segment, the company has going forward planned to take their commercial segment to 14% of their portfolio.

Advantage Nashik

Given that Nashik is the 4th most populous city in Maharashtra (population of 1.48 mn) and has the 3rd largest urban area in the state (with an area of 259 sq km) with a decadal population growth rate of 38% over 2001-2011, demand for residential, commercial, and civil construction is bound to be robust. The shift towards nuclear families is also a growth driver for cities such as Nashik.

Nashik's proximity to Mumbai and Pune also gives it an advantage. The road connectivity from Mumbai to Nashik is good and the travelling time has halved in the last couple of years (from 4-5 hours to 2 hours). The road connectivity to Pune is also being worked on with 60-70% of the work being completed. This has resulted in the travel time coming down from 6 hours to 4 hours and will further reduce to 2.5-3 hours once the road construction is completed. Railway connectivity from Mumbai has been good and the connectivity from Pune is being worked on with land acquisition for the railway being underway. With the airport made operational a year back, Nashik has received another boost in terms of connectivity. The city is connected with flights to New Delhi, Ahmedabad, Hyderabad, and Bengaluru.

The industry of Nashik is fairly diversified. In recent times, the IT sector has shown keen interest in setting up offices in the city. This augurs well for real estate demand as Nashik has plenty of talent and real estate (the two major expenses for IT companies) available at much cheaper rates than major metros. The SME IT companies already have an established presence in the city which gives the bigger companies an assurance of talent supply. The government setup in Nashik is large with the currency press, the government press (catering to the entire stationery needs of the Government of India), railway traction unit, artillery centre, and an air force unit. The

Company stated that members from the armed forces are one of their biggest clients as they are stationed in Nashik for a couple of years and buy a property during their stay as they like the city.

Nashik also has many industrial development zones setup by the Maharashtra Industrial Development Corporation (MIDC) for industrial companies. The presence of large corporates such as Crompton Greaves, Mahindra & Mahindra, GlaxoSmithKline, and Bosch also augurs well for Nashik's growth.

Nashik is also a hub for many of the nearby smaller towns/semi-rural areas such as Aurangabad, Manmad, Lasalgoan, and Dindori where people aspire to move to Nashik which provides a steady flow of potential clients for the company.

Nashik is also an agricultural hub where farmers are wealthy due to their preference for high yielding cash crops such as grapes, pomegranates, and onions. For example, a farmer having a farm of 5 acres with a cash crop will earn a net income of ~₹ 30-40 lakhs/year. Such farmers are known to buy properties in cash and do not need loans.

Nashik's civic infrastructure is also good. One of the reasons for this being that Nashik hosts the Kumbh Mela once every 13 years. During the Kumbh Mela, the Nashik Municipal Corporation gets a lot of funds and they go ahead and spend it on infrastructure. Water supply is also steady in Nashik along with good weather which adds to its appeal. In terms of affordability and cost of living as well, Nashik has many advantages compared to other metros.

Shift from Unorganised to Organised

Given the challenging economic conditions, real estate players from the unorganised space will find it difficult to navigate this environment and the organized players are well suited to gain market share. Customers moving away from unbranded players to branded ones is also a key trend which will aid established players.

Rise of Tier II and III Towns

Given the burgeoning population, the rise of tier II and III towns such as Nashik, Pune, Nagpur, Kolhapur, and Solapur is inevitable which will bring in robust demand for residential and commercial real estate in these cities.

Deleveraging

The Company has managed to deleverage its balance sheet over the years with the debt-to-equity ratio coming down from 5x in FY 2015 to 0.5x in FY 2020. At this rate if the company were to become debt-free in the next 2-3 years it would be better placed.

Diversified Business Profile

The civil construction book which constitutes 11% of revenue gives the company a diversified revenue source and de-risks its orderbook from being too reliant on the development business. The Company recently got its public works department (PWD) license and has received 3 contracts from the government of Goa (residential apartments and market complex/community centre) and a couple from the Maharashtra government for the construction of a bus stand and police housing. As demand for affordable housing grows, growth traction possibilities for the company will also be high. With work orders in hand worth ₹ 173 crores, (of which ₹ 33 crores was booked up to FY'20) this segment looks to grow at a slow and steady pace.

Changing Business Model

The Company has entered into a joint venture with Ashoka Buildcon Limited to develop a mall and premium/luxury residences in Nashik. This is a good strategy to de-risk the business model, take advantage of market opportunities, and gain market share. We have seen other major developers such as Godrej Properties Limited run successful joint venture projects.

Valuations and View

Exhibit 3: Valuations

Description	FY 2019	FY 2020	FY 2021E	FY 2022E	FY 2023E	FY 2024E
Total Income/Sales (₹ Cr)	108.74	118.00	131.00	193.00	243.00	267.00
PAT Margin (%)	11	8	11	26	31	35
PAT (₹ Cr)	12.10	10.00	14.00	51.00	75.00	94.00
No. of Shares (In Cr)	1.23	1.23	6.15*	6.15	6.15	6.15
EPS (₹)	9.84	8.13	2.28	8.29	12.20	15.28
Market Price/Share (₹)	193	129	32	100	122	153
P/E (x)	20	16	14	12	10	10

*Source: Ace Equity, Management guidance, Mangal Keshav Securities (*stock split from FV ₹ 10 to FV ₹ 2)*

As per management guidance if the company grows its topline at a CAGR of 23% over the next four years and margins expand on the back of a shift from a land purchase model to a joint development model, we arrive at an EPS of ₹ 15.28 for FY 2024. After applying a conservative multiple of 10x and a high discount rate of 10% we arrive at a present value of ₹ 105 for the company.

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