Dreaming big

Marg, with its commitment to infrastructure development, has its fingers in a range of pies. With the slowdown, how will they turn out?

A commerce graduate, G.R.K. Reddy started his career in the mid-80s as a merchant banker, working for the then Mumbai-based Cholamandalam Investment and Finance Company (CIFCO) in south India. This was where he gained the expertise in corporate deal making, structuring financial products and achieving financial closures. "Having done this for many businessmen, I wanted to use the expertise to build my own empire," says Reddy, who quit his job to join the family-run construction business in 1994.

As an engineering, procurement and construction (EPC) contractor handling deep excavation works, construction of high-rise buildings, power sub-stations, high power (above 132 kV) transmission lines, marine infrastructure, industrial infrastructure and land development, Reddy believed that infrastructure and real estate verticals would drive second generation reforms in India, therein sowing the seeds of the Marg group. The group today has around Rs8,000 crore worth of projects in real estate, ranging from port, airport, SEZ, IT park and malls to commercial and residential complexes in and around Chennai.

Recognising the slowdown in this space, Reddy believes it is "more about the redefining of an economy. What we are doing is need-based and that will continue with small hiccups in between".

The flagship company of the group is Marg, a listed entity with a market cap of Rs90 crore against a net worth of Rs300 crore. On the bourse, while the stock is trading at Rs41 at a price to earnings of 1.3 times, the price to book value is only 0.33 times.

SANJAY BORADE

Reddy: building his own empire

Considering the slowdown and the way realty players have been hit, these numbers have failed to enthuse investment analysts who continue to visit Marg's facilities – SEZ, Karaikal port and other realty projects – to evaluate the extent of execution. They feel that Reddy is conservative and have refrained from preparing reports on the company because the market cap of Marg is below their threshold levels. Also, since the sector is out of favour, they have adopted a wait-and-watch approach, preparing a report at an appropriate time, which is after the first phase of the Karaikal port opens in March 2009.

For some time in June-July 2008, ICICI Securities was recommending the stock at Rs208 and Rs150 respectively, with a target price of Marg at Rs700. But now, they are revising the earnings and remaining tight-lipped about the future.

Meanwhile, several Chennai-based bankers are more upbeat. "One has only to look at Reddy's 14-year track record and the reputation that the group enjoys in Chennai. Unlike the competition, it has added value to each project. It has taken bridge loans and repaid them," says a source from the Indian Overseas Bank that sanctioned a Rs200-crore loan for the second phase of the Karaikal port and Rs100 crore for the SEZ project.

"One cannot look only at numbers on the balance sheet and market valuation of the flagship company in isolation as Marg's business model is such that they are developed under special purpose companies or vehicles, leading to a focused approach to each project. If these assets and land bank are considered, it adds strength," says the banker.

Some analysts feel that the group is relying too heavily on debt. While Marg's projects are excellent and work is happening at the project sites, Punit Chokani of Enam Securities says, "It needs to raise equity and increase liquidity."

Source: BSE, daily closing prices

The valuations will depend on when the real estate revenues flow in, or as Girish Solanki of Angel Broking, observes of the high debt-equity ratio, "The EBIDTA margins in the port business are expected to be strong. The Marg story on the big screen will unfold in the next five-six years."

If time will tell, others point out that ambitious plans require adequate funding, and that Marg's focus remains hazy. "The company missed a great chance to fund its projects during the boom times because management got too valuation-focused," says Ashish Kacholia, director, research, Lucky Securities. "It keeps getting diverted by new projects, such as Bijapur airport, which will eventually sap the management's time and energy and the company's capital. Companies need to be really focussed on getting their major projects off the ground. Marg still does not seem to get this," adds he.

While bankers and investment analysts may not always be right in spotting an early investment opportunity, Reddy's growth in the first decade (1994-2005) was slow, both in terms of resource mobilisation as well as establishing Marg as an infrastructure and realty developer. Marg in those 10 years, through an IPO at par (Rs10) raised just Rs1.60 crore in 1995 and after completing some residential apartments and an IT park in Chennai (leased to TCS) managed to touch a total income of Rs15.95 crore in 2004-05, making a net profit of Rs1.3 crore.

"The year 2006 was a turning point for us," recalls Reddy, who bagged the Karaikal port development concession from the government of Puducherry on a build-operate-transfer (BOT) basis with an annual cargo handling potential of over 30 million tonnes. The same year, Marg also mobilised FCCBs worth $12.5 million, and the following year, raised GDRs worth $15 million on the Luxembourg Stock Exchange. "As on date, all have been converted," says B.G. Menon, ED, infrastructure, at Marg.

In fact, it has been a no looking back' time (2005 to 2008) for Marg when it got into IT parks and other such ventures. While total income logged in a CAGR of 159.38 per cent, rising from Rs15.95 crore to Rs278.39 crore, the profits have moved at a faster clip. During this period, the CAGR in terms of operating profit (EBIDTA) has been at 169 per cent – from Rs4.66 crore to Rs91.84 crore. At net level the CAGR is 269 per cent, up from Rs1.33 crore to Rs67.44 crore.

Karaikal port project: the big one

The four segments

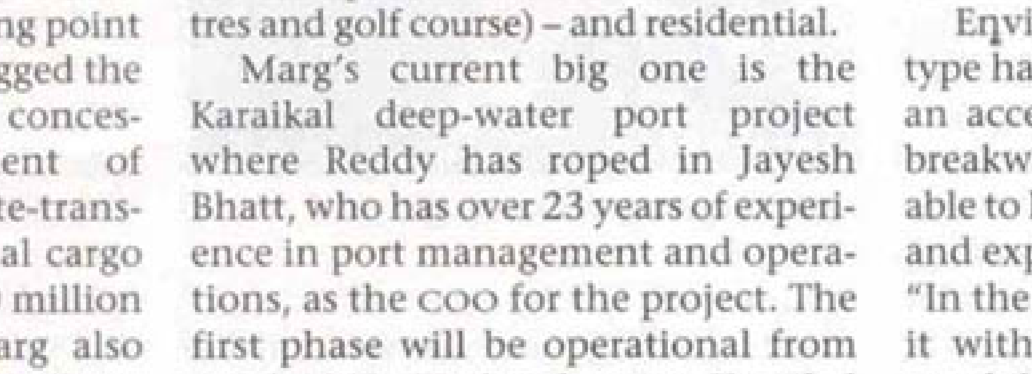
Basically, Marg has four business segments: infrastructure (ports, marine, fishing, harbour, dredgers and logistics solutions); industrial clusters (SEZs, industrial townships, port-based SEZs and desalination plants); real estate – commercial (malls, IT parks, service apartments, convention centres and golf course) – and residential.

Marg's current big one is the Karaikal deep-water port project where Reddy has roped in Jayesh Bhatt, who has over 23 years of experience in port management and operations, as the COO for the project. The first phase will be operational from April 2009. Under the SPV, Karaikal Port Pvt Ltd in the first phase, Reddy is erecting infrastructure in the port (which has a 12-metre draft) to handle 45,000 dwt vessels, consisting of two berths, one for coal, and the other, for general cargo with a total cargo capacity of 5.3 tpa, catering to the hinterland of central Tamil Nadu.

"This Rs416-crore first phase of the project is being financed by a debt to equity ratio of 2.6:1, the financial closure has taken place in November 2006," explains Menon, going by contributions coming from this project beginning from the year 2009-10. "The concession period is for 30 years, extendable by mutual consent for a further period of 20 years in two blocks of 10 years each."

Envisaged as a deep-water lagoon-type harbour, connected to the sea by an access channel and protected by breakwaters, the Karaikal port will be able to handle large volumes of import and export traffic, according to Bhatt. "In the next phase we plan to develop it with mechanised cargo handling capabilities with a cumulative capacity of up to 21 tpa. Phase-2 will be operational by 2011," he says.

While the Karaikal project looks good, portfolio managers remain watchful of the funding. Meanwhile, an ICICI Securities report on the company points out that one of its assets is a $13-million cutter suction dredger, with maximum dredging depth of 25 metres, which is being used to dredge this port, and later for contractual work on other ports through Marg's dredging subsidiary. The report also shows the logistical advantages of Karaikal *vis-à-vis* many key inland locations, such as



Coimbatore and Trichy.

Linked to this, Marg is developing the Rajakkamangalam (Tamil Nadu) fishing harbour, having made an investment of Rs45 crore for 40 acres of land. The harbour, which will have a mooring facility for 300 boats, is expected to be fully operational by October 2010 and will be equipped with waterfront facilities for safe landing and berthing of various categories of fishing craft, boat building and repair yards and ice plant and cold storage facilities for processing and preservation of fish. "These facilities are aimed at engaging the best practices to harvest the unexploited fishery potential to the level of 'Maximum Sustainable Yield', which will also enhance the food security and livelihoods of the people of Rajakkamangalam village," adds Bhatt. However, financial closure of the project is yet to happen.

Out of the other verticals in Marg, the Seekinkuppam SEZ (the site is connected to Chennai and Puducherry through the arterial east coast road) under its SPV – New Chennai Township Pvt Ltd – has commenced construction work on the project, called 'Swarnabhoomi'. Here, on 613 acres of land, the company is putting up a multi-services and light engineering complex. It plans to develop 26 million sq ft of saleable area, including 8 million sq ft plots, 9 million sq ft of residential space and 7 million sq ft of office space.

One of Marg's real estate projects

"Out of the total cost of Rs705 crore, a debt to the extent of Rs406 crore has been tied up," adds Menon, pointing out that out of the Rs183 crore of equity, Marg has already chipped in Rs78 crore, with the balance still to come. "It needs to quickly get equity investors into its real estate projects like Swarnabhoomi, else banks are unlikely to release their disbursements," cautions Kacholia.

According to a leading SEZ player, the competition in Chennai is hotting up, and with the slowdown, the demand is low. Menon, however, asserts that they are receiving enquiries from parties like the "Federal Mogul Corporation, a US-based $6.9-billion auto giant, which is entering Indian auto space through our SEZ."

Rental revenue

Marg has commercial real estate projects too under construction. The Riverside Mall is one. Located in Karapakkam, Old Mahabalipuram Road (OMR), south Chennai, on a 7.28-acre property, it will comprise shops, a multiplex and a business-class hotel, besides Oakwood Residence, offering 185 serviced apartments on a lease basis, and Anjali Square, jointly developed on a rental and sale basis, with Anjali Devi, Tamil and Telugu actress. Reddy already has three office buildings in Chennai, which fetch Marg an average monthly rental of Rs38 per sq ft, aggregating close to Rs10 crore per annum.

In the residential segment, Marg has two ongoing projects, Tapovan, consisting of villas, and Marg Ramlakshmi Enclave, where 96 residential apartments will come up. "We will be entering low-cost housing too," says Oscar Braganza, ED, real estate.

Being regarded as the latest feather in Reddy's cap is Marg's first airport project. In December 2008, the Karnataka government awarded Marg the contract for the development and operation of the greenfield airport at Bijapur on a BOT basis under the public-private partnership (PPP) model. The airport will come up on 727 acres of land in Burnapur village in Bijapur. Marg has won a 30-year deal to design, develop, operate and manage the airport, extendable subsequently by mutual consent in three-decade slots.

Reddy sees Bijapur, with its many heritage monuments, as a tourist gateway to North Karnataka – it receives roughly 7 lakh tourists annually. But there are other areas too – export, cargo and horticulture – that would benefit from an airport in the vicinity. The city is a hub of sorts for education, having 65 colleges, while businessmen will be able to stay connected to Pune, Hyderabad, Belgaum, Bangalore and Goa, says Reddy, who, in addition to the terminals, runways and control towers, is also developing access facilities and utilities necessary to serve the airport during the operational phase.

It is notable that GVK as well as GMR, who have been operating the busiest airports in the country, have stayed away from small airports. "They don't seem to be a viable business model. Our feasibility study shows that the revenues would be low," say sources at GVK.

The Marg group's diverse range of projects is expected to "be executed in the next five years and they will be self-sustaining projects," says Reddy, who hopes to make Marg into a Rs600-crore company next year and join the Rs2,000-crore league in the next five years. This can happen only if financial closure takes place in a time-bound manner – or else his dreams there may have a setback.

• LANCELOT JOSEPH