

# SPML Infra's inflection point

A remarkable contrarian play is the country's infrastructure sector.

This is why I am sticking my neck out.

In the past, whenever infrastructure companies worked for the government, there was always the possibility of a disputed delivery ('I asked for this, you gave me that'). Each time this transpired, the vendor and customer locked into arbitration for years (often resolution-less).

The result: No remuneration for much of the expenses incurred, a need to stay in business by addressing new contracts, the possibility of additional arbitration and borrowing working capital at high costs to plug the revenue gap.

The result is that most companies were defeated not by terrain challenges or projects complexity but by the interminable arbitration process that destroyed their balance sheets and pre-qualification credentials.

This message was not lost on the government. A modern India could not be built without an enabling environment that attracted the best contractors who could report a reasonable profit. It could also not expose the country to a scenario where Indian contractors



## MARKET MIND

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were driven out of business and most contracts were carved away by international firms.

The government addressed the nerve of the problem: Accelerated arbitration. It introduced the landmark S4A law, expected to create a win-win proposition

for customer, lender, community and country. The six ways in which S4A will transform sectoral realities comprise: Establish the integrity of contractors passing the stringent S4A test; directive to disburse 75 per cent of the awarded amount without contest against a bank guarantee (though this is yet to be accepted by state governments), inclusion of disputed receivables by banks in estimating the strength of the contractor, which could reduce borrowing costs; segregation of debt helping identify the quantum that was mobilised following arbitration delay; the decision to get banks to buy the company's equity at market price (turning lender into investor, with a vested interest in closing the arbitration) and enunciation of defined time-lines to conclude the arbitration.

The big implication: A combi-

nation of debt reduction on the one hand and increased net worth on the other, kick-starting a virtuous cycle for the beleaguered company. This in turn could strengthen credit rating and moderate funding costs. Best of all, this could strengthen the pre-qualification credentials of construction companies, resulting in larger contracts.

The one company I would put my money on is SPML Infra. It is principally a water infrastructure solutions provider (in addition to a presence in other infra segments). The company is among the top two in India's water infra space. Its interest cover was nominal in 2016-17; order book was ₹6,800 crore by mid-June 2017, with a 14 per cent Ebitda (earnings before interest, tax, depreciation and amortisation) hurdle rate margin.

The big story is if the company clears the stringent S4A, this could be its virtual reincarnation, where knowledge and competence finally begin to reflect in its profit and loss account, lower debt and market capitalisation. That is the inflection point I am willing to put my money on.

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