

## Welspun Gujarat (WELGUJ)

Rs 266

### WHAT'S CHANGED....

PRICE TARGET .....	Unchanged
EPS (FY11E) .....	Changed from Rs 28.6 to Rs 27.7
RATING.....	Changed from Add to Strong Buy

### Robust volume growth pipeline...

Welspun Gujarat's FY10 revenue grew ~28% to Rs 7350.3 crore while the PAT increased 186% YoY to Rs 610.4 crore (I-direct: Rs 589 crore) on the back of pipe sales volume growth of 17% and plate volumes growth of 151%. The US mill contributed ~1.15 lakh tonne to the pipe sales volume. The EBITDA margin expanded to 19.2% in Q4FY10 and 17.9% in FY10 with EBITDA/tonne of ~Rs 11000 on pipes and ~Rs 6000 on plates for FY10. The management remains upbeat about the improved outlook in the oil and gas space and expects strong volume growth in FY11E. We maintain our positive stance on the stock and target price of Rs 325.

#### ■ Strong sales volume maintained

Pipe sales volume rose ~20% QoQ and ~8% YoY to ~2.05 lakh tonne in Q4FY10 with commencement of deferred shipments from Q3FY10. External plate sales continued to surprise for the third straight quarter with sales volume of ~83000 tonne in Q4FY10. Plate external sales volumes are expected to dip, going forward, as most plate orders are executed. The management guided towards 10 lakh tonne of pipes and 6 lakh tonne of plates production in FY11E.

#### ■ Pipe capacity being augmented to 2.0 MT

The company is in the process of increasing its pipe manufacturing capacity to 2.0 million tonne (MT) by FY11E through the setting up of 2 lakh tonne HSAW (two mills of 1 lakh tonne each) and 3 lakh tonne of LSAW capacity. It expects to incur a capex of ~Rs 400 crore for the same.

### Valuation

At the CMP of Rs 266, the stock is trading at FY11E P/E of 9.6x and FY11E EV/EBITDA of 5.4x. With an improving scenario for pipe manufacturers, order inflow is expected to be strong, going forward, while revenue visibility would increase. We continue to value the stock at 6x FY11E EV/EBITDA and maintain our target price of Rs 325. We are assigning a **STRONG BUY** rating to the stock.

#### Exhibit 1: Performance Highlights

(Rs Crore)	Q4FY10	Q4FY10E	Q4FY09*	Q3FY10	YoY (Chg %)	QoQ (Chg %)
Net Sales	1597.4	1706.3	1831.8	1639.5	-12.8	-2.6
EBITDA	306.0	322.1	160.9	348.6	90.2	-12.2
EBITDA Margin (%)	19.2	18.9	8.8	21.3	+ 1040 bps	- 210 bps
Depreciation	52.0	52.3	34.4	51.1	51.0	1.7
Interest	28.2	50.0	50.1	42.8	-43.7	-34.1
Reported PAT	166.5	145.1	51.8	166.8	221.3	-0.2
Basic EPS (Rs)	8.1	7.1	2.8	8.9	193.3	-8.9

\* Standalone nos for Q4FY09

Source: Company, ICICIdirect.com Research

Rating matrix	
Rating	: Strong Buy
Target	: Rs 325
Target Period	: 12-15 months
Potential Upside	: 22%

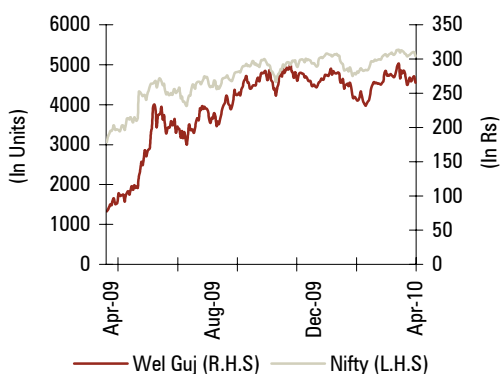
Annual performance				
(Rs Crore)*	FY08	FY09	FY10	FY11E
Net Sales	3994.5	5739.5	7350.2	6702.7
EBITDA	655.5	634.8	1318.6	1245.7
Net Profit	347.7	213.5	610.4	565.7

\* Not including MSK financials

Valuation summary				
	FY08	FY09	FY10	FY11E
PE (x)	13.8	23.8	8.9	9.6
Target PE (x)	16.8	29.1	10.9	11.7
EV/EBITDA (x)	9.4	10.3	5.5	5.4
P/BV (x)	3.0	3.2	2.1	1.8
RoNW (%)	30.7	13.7	29.4	20.0
RoCE (%)	20.5	12.5	23.7	19.0

Stock data	
Market Capitalisation	Rs 5443.1 Crore
Debt (FY10)	Rs 2547.6 Crore
Cash & Invst (FY10)	Rs 1702.8 Crore
EV	Rs 6287.9 Crore
52 week H/L	296/90
Equity capital	Rs 102.16 Crore
Face value	Rs 5
MF Holding (%)	15.8
FII Holding (%)	17.7

#### Price movement (Stock vs. Nifty)



#### Analyst's name

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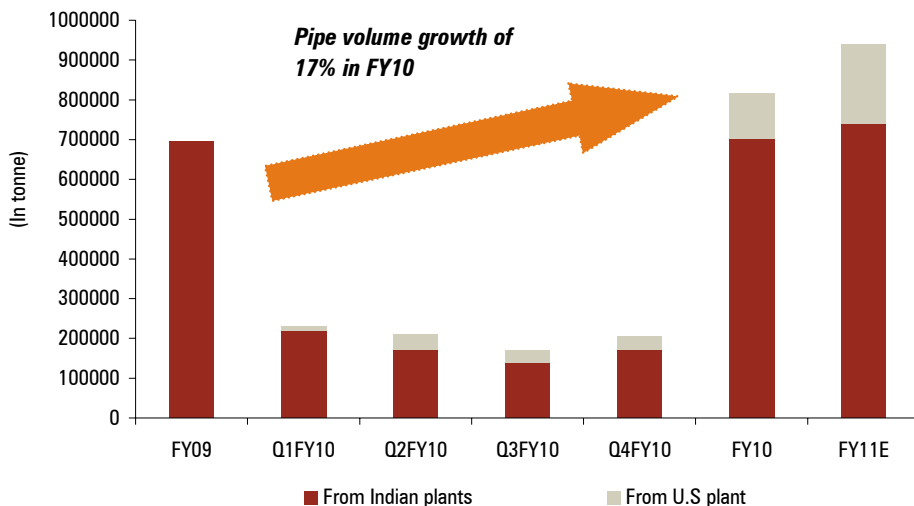
**Result Analysis**

The company reported outstanding numbers for Q4FY10 due to sustained pipe volumes contribution from the US mill resulting in higher overall sales volume, continuation of robust plate sales, lower overall expenses and lower interest expenses due to repayment of high interest cost debt of ~Rs 800 crore.

Sales volume of pipes increased 17% YoY to reach ~8.15 lakh tonne with the US mill contributing ~1.15 lakh tonne. We expect overall pipe sales of ~9.4 lakh tonne in FY11E against the management's target of 10 lakh tonne. The company maintained EBITDA/tonne of ~Rs 11,000/tonne in pipes in FY10

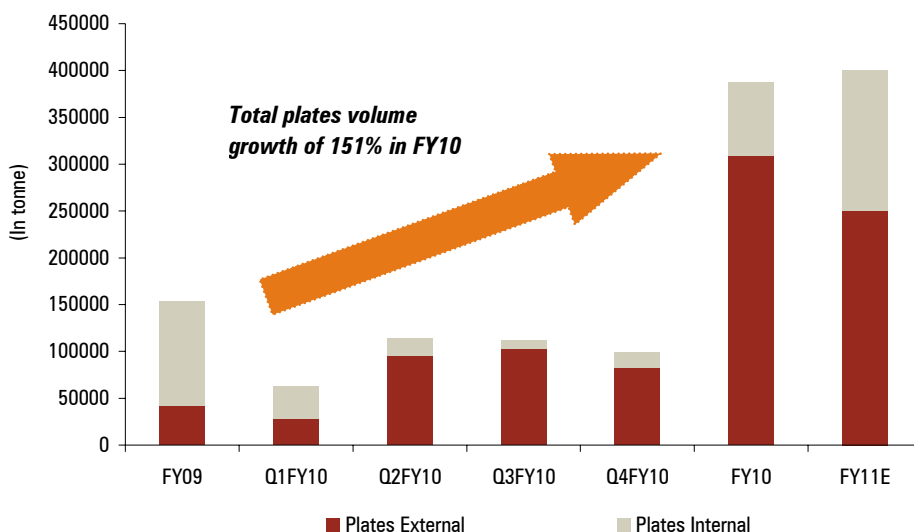
Sales volumes in plates continued to remain robust with external plate sales of ~83000 tonne in Q4FY10. External plate sales jumped 634% to ~3.1 lakh tonne in FY10. However, we expect lower external plate sales in FY11E as plate orders in hand are not substantial as of now. The company achieved an EBITDA/tonne of ~Rs 6000/tonne in plates in FY10

**Exhibit 2: Pipes sales volumes**



Source: Company, ICICIdirect.com Research

**Exhibit 3: Plates sales volumes**



Source: Company, ICICIdirect.com Research

#### Analyst meet and quarterly highlights

- The company's US plant has continued its stable performance and achieved sales volume of ~34,000 tonne of pipes in Q4FY10. Full year sales in the US plant were ~1.15 lakh tonne. The company expects its US plant to operate at 70-75% capacity utilisation in FY11E
- The company's consolidated order book stood at ~ Rs 6,400 crore with pipe orders to the tune of ~7.9 lakh tonnes. The order book is expected to increase in the next three to six months as major contracts for which the company has already bid are due to be allotted soon while ~0.5 MT of new orders are under advanced stage of allocation
- The company is making good progress with its expansion projects. The coil mill in Anjar has completed trial production and has been commissioned. The 3 lakh TPA LSAW mill at Anjar is targeted to be completed by FY11E. HSAW pipe mill expansion of 1 lakh TPA in Bangalore is being implemented according to schedule (expected by June 2010). Another 1 lakh TPA HSAW mobile plant in central India has been announced
- The company's consolidated gross debt stood at ~Rs 2,550 crore, whereas total cash in hand was ~ Rs 1,700 crore
- The company made an attractive EBITDA/tonne of ~Rs 11,200 on pipes and ~Rs 5,700 on plates during Q4FY10. It remained upbeat on maintaining an EBITDA/tonne on pipes and plates of ~Rs 11,000 and 6,000, respectively, on the current order book to be executed, going forward, in FY11E
- The outlook for the pipes industry has started to improve with the recovery having started in global markets and crude oil prices hovering around US\$80 per barrel leading to a revival of several shelved projects in the oil and gas space
- The company has bid for various international projects translating into order inflows of more than 2 MT of pipes. It expects to bag ~8 lakh tonne of orders in the next eight to 12 months
- The company expects to achieve pipe sales volume of more than a million tonne and plate production of more than 6 lakh tonne in FY11E
- The company expects a turnover of Rs 525 crore from its recently acquired infrastructure company, MSK Projects Ltd in FY11E

#### Issues & Concerns

- Cancellation of existing projects and postponement of new pipeline projects due to unexpected slowdown of global economy
- Unexpected fall in crude oil prices to below US\$60/barrel leading to cancellation of projects from oil and gas majors
- Increase in raw material costs affecting margins negatively
- Unexpected losses due to foreign exchange rates fluctuations
- Slow inflow of new orders affecting the target production

### Outlook & Earnings Revision

With the company's US subsidiary turning profitable in the first year of its operation and delivering higher-than-expected volumes (~1.15 lakh tonne), the earnings for the company have shown phenomenal growth in FY10. The outlook for the pipe industry has improved on the back of global economic revival and crude oil price recovery. We are revising our earnings estimate (EPS) for FY11E lower by ~3% for FY11E. This is on the back of a conservative volume assumption in the plates segment considering the fact that orders in the plates segment have been subdued. Also, revenue visibility remains at ~0.8x the target for FY11E based on current order book of ~7.9 lakh tonne.

### Exhibit 4: Revised financials

	FY11E*		
	Current	Previous	% Change
Net Sales	6702.7	7052.5	-5.0
EBITDA	1245.7	1306.4	-4.6
EBITDA Margin (%)	18.6	18.5	-40 bps
PAT	565.7	583.6	-3.1
EPS (Rs)	27.7	28.6	-3.2

\* Not including MSK financials

Source: Company, ICICIdirect.com Research

### Exhibit 5: EPS (Including MSK contribution)

FY11E	Rs Cr
Welspun PAT	565.7
Welspun EPS	27.7
MSK PAT	42.6
Welspun Stake (%)	79.3%
Addition to Welspun PAT	33.7
Welspun revised PAT	599.5
Welspun revised EPS	29.3
<b>EPS accretion (%)</b>	<b>6.0</b>

Source: Company, ICICIdirect.com Research

### Valuations

At the CMP of Rs 266, the stock is trading at FY11E PE of 9.6x and FY11E EV/EBITDA of 5.4x. With the improving scenario for pipe manufacturers, the order inflow is expected to be strong, going forward, and revenue visibility would increase. We continue to value the stock at 6x FY11E EV/EBITDA and maintain our target price of Rs 325. We are assigning a **STRONG BUY** rating to the stock.

### Exhibit 6: Valuation Table

	Sales (Rs)		EV/EBITDA				
	Crore)	EPS (Rs)	PE (x)	(x)	P/ BV (x)	RoNW (%)	RoCE (%)
<b>FY09</b>	5739.5	11.2	23.8	10.3	3.2	13.7	12.5
<b>FY10</b>	7350.2	29.9	8.9	5.5	2.1	29.4	23.7
<b>FY11E</b>	6702.7	27.7	9.6	5.4	1.8	20.0	19.0

Source: Company, ICICIdirect.com Research

## ICICIdirect.com coverage universe (Pipes)

<b>Jindal SAW</b>				<b>Sales(Rs Cr.)</b>	<b>EPS (Rs)</b>	<b>PE (x)</b>	<b>EV/EBITDA (x)</b>	<b>RoNW (%)</b>	<b>RoCE (%)</b>
<b>Idirect Code</b>	SAWPIP <b>CMP</b>	214.9	<b>CY08</b>	5009.1	13.1	16.4	9.8	15.4	15.6
	<b>Target</b>	228.0	<b>FY10*</b>	6791.6	26.7	8.0	4.7	19.1	21.6
<b>MCap</b>	5878.3 <b>Upside (%)</b>	6.1	<b>FY11E</b>	5814.4	19.3	11.1	5.7	12.4	14.2

\*FY10 represents 15 months data

<b>Maharashtra Seamless</b>				<b>Sales(Rs Cr.)</b>	<b>EPS (Rs)</b>	<b>PE (x)</b>	<b>EV/EBITDA (x)</b>	<b>RoNW (%)</b>	<b>RoCE (%)</b>
<b>Idirect Code</b>	MAHSEA <b>CMP</b>	393.2	<b>FY09</b>	2038.9	36.8	10.7	2.0	20.0	26.6
	<b>Target</b>	380.4	<b>FY10E</b>	1603.8	41.1	9.6	1.5	18.9	24.4
<b>MCap</b>	1386.7 <b>Upside (%)</b>	-3.3	<b>FY11E</b>	1774.8	46.2	8.5	1.3	17.6	22.8

<b>Man Industries</b>				<b>Sales(Rs Cr.)</b>	<b>EPS (Rs)</b>	<b>PE (x)</b>	<b>EV/EBITDA (x)</b>	<b>RoNW (%)</b>	<b>RoCE (%)</b>
<b>Idirect Code</b>	MANIN <b>CMP</b>	70.6	<b>FY09</b>	1883.4	3.8	18.4	4.6	5.4	14.3
	<b>Target</b>	76.0	<b>FY10E</b>	1555.5	11.5	6.1	3.4	14.8	17.3
<b>MCap</b>	267.5 <b>Upside (%)</b>	7.7	<b>FY11E</b>	1320.0	12.6	5.6	2.9	14.2	17.6

<b>PSL Limited</b>				<b>Sales(Rs Cr.)</b>	<b>EPS (Rs)</b>	<b>PE (x)</b>	<b>EV/EBITDA (x)</b>	<b>RoNW (%)</b>	<b>RoCE (%)</b>
<b>Idirect Code</b>	PSLHOL <b>CMP</b>	148.1	<b>FY09</b>	3559.9	22.3	6.6	5.0	15.1	14.5
	<b>Target</b>	186.0	<b>FY10E</b>	2727.1	17.4	8.5	5.6	11.5	12.5
<b>MCap</b>	789.8 <b>Upside (%)</b>	25.6	<b>FY11E</b>	3033.5	20.4	7.3	5.1	11.2	13.3

<b>Welspun Gujarat*</b>				<b>Sales(Rs Cr.)</b>	<b>EPS (Rs)</b>	<b>PE (x)</b>	<b>EV/EBITDA (x)</b>	<b>RoNW (%)</b>	<b>RoCE (%)</b>
<b>Idirect Code</b>	WELGUJ <b>CMP</b>	265.6	<b>FY09</b>	5739.5	11.2	23.8	10.3	13.7	12.5
	<b>Target</b>	325.0	<b>FY10</b>	7350.2	29.9	8.9	5.5	29.4	23.7
<b>MCap</b>	5426.7 <b>Upside (%)</b>	22.4	<b>FY11E</b>	6702.7	27.7	9.6	5.4	20.0	19.0

\* Financials not in consolidation with MSK projects

Source: Company, ICICIdirect.com Research

## RATING RATIONALE

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Strong Buy: 20% or more;  
 Buy: Between 10% and 20%;  
 Add: Up to 10%;  
 Reduce: Up to -10%  
 Sell: -10% or more;

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## ANALYST CERTIFICATION

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