

Varun Shipping Company Limited
Rs 71

... company update

Buy

Industry	: Shipping	BSE / NSE code	: 500465/ VARUNSHIP
Company P/E	: 4x FY'10E	52-Week H/L (Rs)	: Rs.54 / Rs.110
Market Cap. (Rs)	: 10,650 mn	Avg. Daily traded volume	: 218,800/ 310,900
Face Value (Rs)	: 10	Dividend (FY08)	: 50%

Key Highlights

- **Capital expenditure:** Varun Shipping embarked on capital expenditure since CY07 with \$ 400mn. It accomplished the capital expenditure of \$320mn for CY07, balance carried forward to next year. It has planned a further capital expenditure of \$400mn (including \$80mn from last year) for CY08. The fleet additions are as follows:

FY	Name of the vessel	Date of addition	Type of vessel	Amt in Mn.(\$)*
FY2007	Maharshi Vamadeva	Dec-06	LGC	60
	MT Amba Bhargavi	Jan-07	Aframax	80
	MV Subhiksha	Jan-07	AHTSV	60
				200
FY2008	MV Sudaksha	May-07	AHTSV	60
	Maharshi Bharadwaj	Jun-07	VLGC	60
	MV Suvarna	Mar-08	AHTSV	100
				220
FY2009	Other assets planned	By Dec-08		300

* individual asset prices are assumed

It has added 2 new Anchor Handling Towing Supply Vessels (AHTSV) having largest bollard pull capacities under Indian flag and are currently employed on time charter with Reliance Industries Limited. It has acquired another specialized AHTSV, Suvarna, which is used for deep sea oil exploration activities going on in the areas like North Sea.

- **Fleet Addition:** The total capital expenditure laid out in 2 calendar years thus totals to \$720mn. However, VSL still has \$300mn of capital to be expended. This possible stream of revenues from new fleet addition does not form a part of our revenue projections. A further upside to this extent cannot be ruled on completion of this fleet addition plan.
- **Margin expansion:** The share of revenues from Offshore segment has witnessed an increase from 3% in FY07 to 19% in FY08, beating our expectations. With addition of one more AHTSV MV Suvarna in March 2008, we expect to witness its full contribution to the topline from FY09E. With this, we expect the share of revenues for this segment to increase significantly. This will further lead to expansion in operating margins by 433bps to 62.42% by FY10E.
- **Dividend yield :** VSL has been one of the most stable players in the shipping industry posting continuous profits for more than two decades and maintaining dividend paying history of more than 24 years. We expect the dividends to be maintained at current levels. Hence, investors can look at good dividend yields along with capital appreciation from the investment.
- **Slowdown of industry:** Any slowdown in the freight rates in LPG Carrier segment can be a dampener to VSL's business. However, a strong demand outlook for LPG consumption supports the secular growth of this segment. Also, with close to 80% of its revenues coming from pool and time charter agreements, VSL is insured against the cyclicity of the industry segments.
- **Operational Costs:** Rising operational costs and increase in crew wage bills may lead to minor contraction of operating margins. However, with increase in freight rates as well as chartering agreements in place, we believe VSL shall be able to pass on these costs to maintain its profitability.

Company Profile

Varun Shipping is the owner and operator of largest LPG fleet under Indian Flag. VSL owns a well diversified fleet of 20 vessels comprising 11 LPG carriers, 3 crude oil tankers, 1 product tanker, and 5 AHTSs. All these vessels are placed directly or indirectly with the end users under time charter, pool charter or voyage charter arrangements. With a well diversified fleet, VSL is able to offer a comprehensive shipping solution across the entire hydrocarbon product chain.

Business Profile

Varun Shipping has added 3 new vessels in FY08; one AHTSV being added in March 2008. VSL has recorded Operating revenues of Rs.8.5bn in FY08 against Rs.6.7bn in FY07, posting a growth of 27%. It recorded an operating profit of Rs.4.9bn vis-a-vis profit of Rs.4.3bn (excluding foreign exchange adjustments). EBIDTA at core levels has remained flat year on year at 58.06% v/s. 58.96% last year. VSL declared the highest dividend in its corporate history at 50% this year, thus maintaining itself as one of the best dividend yield stocks.

Outlook and Valuations

Considering that the LPG shipping market is not a volatile segment in shipping industry, we re-iterate our confidence in the core growth story of the company. Further, with the substantial rise in offshore business revenues for the company, we feel the company is available at cheap valuations. VSL is expected to post an earnings of Rs.14 and Rs.16 for FY09E and FY10E respectively. Effective asset deployment and equivalent depreciation merit attention to cash EPS numbers at an expected of Rs.29 and Rs.32 for FY09E and FY10E. A further upside in revenues due to completion of fleet addition plan can be envisaged. We re-iterate our Buy on the stock with a revised target of Rs. 96, giving an appreciation of 37% over a medium term perspective with low risk.

Table 1: Profit & Loss A/c

Y E June (Rs. Mn.)	2006A	2007A	2008E	2009E	2010E
Income from Operation	6,619	6,845	8,508	9,163	9,741
P/L on Sale Of Assets	1	497	19	20	20
Other Income	15	20	48	45	45
Total Income	6,636	7,361	8,575	9,228	9,806
Operating Expenses	1,305	1,097	1,032	1,247	1,313
Employee Cost	527	808	934	1,026	1,072
Repairs & Maintenance	660	802	777	779	828
Admin. O & M, & Other Exp	264	314	852	458	472
Total Expenditure	2,756	3,021	3,594	3,510	3,685
Operating Profit	3,879	4,340	4,981	5,717	6,121
Interest	742	1,192	1,395	1,394	1,279
Gross Profit	3,137	3,148	3,586	4,323	4,843
Depreciation	1,268	1,629	2,120	2,125	2,380
Profit Before Tax	1,86	1,519	1,466	2,198	2,463
Total Tax	29	70	24	32	41
Net Profit	1,840	1,449	1,441	2,166	2,422
Provisions & contingencies*	0	0	818		
Adjusted Net Profit	1,840	1,449	2,259	2,166	2,422

* Foreign Exchange and Impairment of Assets Adjustments

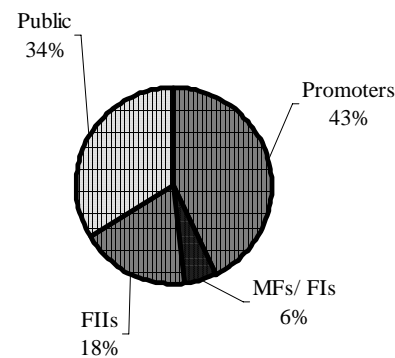
Table 2: Balance Sheet

Y E June (Rs. Mn.)	2006A	2007A	2008E	2009E	2010E
Share Capital	1,177	1,482	1,500	1,500	1,500
Reserves Total	3,799	6,092	8,351	10,517	12,940
Total Shareholders Funds	4,976	7,574	9,851	12,017	14,440
Other Liabilities	32	19	0	0	0
Secured Loans	12,744	17,930	22,970	24,256	22,235
Total Debt	12,776	17,950	22,970	24,256	22,235
Total Liabilities	17,752	25,524	32,822	36,273	36,674
Gross Block	22,080	29,144	38,494	42,494	42,494
Less : Accu. Dep.	4,559	6,188	8,308	8,308	10,433
Net Block	17,521	22,956	30,186	34,186	32,061
Investments	183	205	250	200	200
Inventories (Store & Spare)	37	43	85	73	78
Sundry Debtors	470	528	936	916	974
Cash and Bank	421	718	839	440	2,874
Other Current Assets	0	0	100	0	0
Loans and Advances	195	521	893	9629	1,023
Total Current Assets	1,123	1,811	2,854	2,391	4,949
Current Liabilities	837	574	425	458	487
Provisions	238	303	43	46	49
Total Current Liabilities	1,075	878	468	504	536
Net Current Assets	48	933	2,386	1,887	4,413
Total Assets	17,752	24,094	32,822	36,273	36,674

Table 3: Key Ratios

Year End June	2006A	2007A	2008E	2009E	2010E
Diluted EPS	15.92	10.71	9.61	14.44	16.15
P/E	4.46	6.63	7.39	4.92	4.40
BV	33.17	50.49	65.67	80.11	96.26
P/BV	2.14	1.41	1.08	0.89	0.74
Cash EPS	20.72	20.52	29.19	28.60	32.01
P/CEPS	3.43	3.46	2.43	2.48	2.22
Debt-Equity Ratio	2.57	2.37	2.33	2.02	1.54
EBIDTA Margin (%)	58.46	58.96	58.09	61.96	62.42
PAT Margin (%)	27.73	19.69	16.81	23.47	24.70
ROCE (%)	14.55	10.35	8.64	9.82	10.09
RONW (%)	36.98	19.13	14.63	18.02	16.78
EV/EBIDTA	5.93	6.42	6.58	6.03	4.90

Shareholding Pattern



Price Performance Chart

