

## RPG TRANSMISSION

INR 205

*Reinforcing foundations*

BUY



RPG Transmission (RPGT) declared impressive Q4 results with profitability surprising positively despite sub-par revenue performance. Q4FY07 revenues were up ~4% Y-o-Y at INR 1 bn. EBITDA, at INR 119 mn, was up by ~9% Y-o-Y, while net profit, at INR 100 mn, was up ~166% Y-o-Y for the quarter.

For FY07, revenue growth was encouraging at ~43% Y-o-Y to INR 3.7 bn. EBITDA, at INR 427 mn, was up by ~64% Y-o-Y, while net profit, at INR 257 mn, was up by 157% Y-o-Y for FY07. EBITDA margins expanded by ~60bps Y-o-Y to 11.8% in Q4FY07. However, on a sequential basis, EBITDA margin was down by ~60bps. The net margin was at 10%, up by ~610bps Y-o-Y, on account of write back of tax charges in the quarter. For FY07, EBITDA margins expanded by ~150bps Y-o-Y driven by operating leverage and improvement in project profile. Net margins improved by ~290bps Y-o-Y to 6.9% driven by lower interest expense and tax rate in FY07. Order backlog at the end of Q4FY07 was INR 4.5 bn, implying an order intake of INR 1.3 bn in the quarter, compared to INR 2.1 bn in Q3FY07. The yearly order accretion increased by ~52% Y-o-Y to INR 4.2 bn in FY07, reflecting robust demand traction. We believe, RPGT is benefiting from the rapid pace of capacity ramp up in the 'power T&D' space in India. We are upgrading our EPS estimates by ~13% and ~2% to INR 22 and INR 27 for FY08 and FY09, respectively, driven primarily by improving profitability. The stock is trading at a P/E of 10x and 8x our EPS estimates for FY08 and FY09, respectively. We continue to maintain our 'BUY' recommendation.

\* **Robust margins ...close to industry average**

Profitability across the power transmission towers industry has expanded in FY07. However, from here on we expect margins to be maintained between ~11% and 12% with few positive surprises as we do not expect significant re-pricing of contracts. Additionally, increased activity in a competitive scenario is likely to keep margins under check.

\* **At-par capability with sector peers driving profitable growth**

RPGT's at-par capability with sector peers in terms of pre-qualifications and a robust macro scenario is likely to drive strong revenue growth at a CAGR of ~33% from FY07-09E. Revenue growth and enhanced profitability coupled with improving working capital metrics and low capital expenditure are likely to result in positive free cash flow and improving return ratios leading us to repose faith in the company's growth and earnings.

### Financials

Year to March	Q4FY07	Q4FY06	% change	Q3FY07	% change	FY07UA	FY08E
Revenues (INR mn)	1,007	970	3.8	905	11.3	3,722	5,009
EBITDA (INR mn)	119	109	9.2	112	6.3	427	592
Net profit (INR mn)	100	38	165.6	59	70.5	257	337
EPS (INR)	6.4	2.4	165.6	3.8	70.5	16.5	21.5
PE (x)						12.4	9.5
EV/EBITDA (x)						8.9	6.4
ROAE (%)						34.3	38.5

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### Market Data

52-week range (INR) : 238 / 75  
Share in issue (mn) : 15.6  
M cap (INR bn/USD mn) : 3.2 / 78.3  
Avg. Daily Vol. BSE ('000) : 80.4

### Share Holding Pattern (%)

Promoters : 37.5  
MFs, Fls & Banks : 17.5  
Fls : 10.7  
Others : 34.4

### \* Key revisions in estimates

We are downgrading our revenue estimates by 7% and 8% to INR ~5 bn and INR ~6.5 bn for FY08 and FY09, respectively, due to a lower revenue base of INR 3.7 bn reported in FY07 versus our estimate of INR 4 bn. However, we are increasing our net profit estimates by ~13% and ~2% to INR 337 mn and INR 426 mn in FY08 and FY09, respectively, on account of significant improvement in margins. The key revisions are given in the table below:

**Table 1: Revised estimates**

	Previous estimates		Revised estimates		Remarks
	FY08E	FY09E	FY08E	FY09E	
Revenues (INR mn)	5,412	7,074	5,009	6,536	Downgrading revenue estimates due to lower revenue in FY07 than our estimates. However growth in FY08 at ~35% is marginally better than earlier estimates of ~34%
EBITDA (INR mn)	509	706	592	768	Higher margins due to better price realizations in recent contracts and larger order sizes. Margins likely to stabilize at current levels
EBITDA margin (%)	9.4	10.0	11.8	11.8	
PAT (INR mn)	299	418	337	426	
Net margin (%)	5.5	5.9	6.7	6.5	
EPS (INR)	19.1	26.8	21.5	27.3	

Source: Edelweiss research

### \* Outlook and valuations

Order visibility remains strong with plans of T&D network enhancement (for the 11<sup>th</sup> plan) being clearly articulated by the Ministry of Power. While quarterly volatility in order intake may impact the timing of revenues in the short term, the growth scenario in the medium to long term is on a fundamentally strong footing. On our EPS estimate of INR 22 and INR 27 for FY08 and FY09, respectively, RPGT trades at a P/E of 10x and 8x, respectively. We continue to maintain our 'BUY' recommendation.

(INR mn)

Financials snapshot								
Year to March	Q4FY07	Q4FY06	% change	Q3FY07	% change	FY06*	FY07UA	FY08E
Revenues (net)	1,007	970	3.8	905	11.3	1,951	3,722	5,009
Raw material	491	575	(14.6)	399	23.0	1,365	1,945	2,968
Staff cost	71	65	9.0	64	9.6	181	253	701
Other operating expenses	327	222	47.5	330	(0.8)	209	1,097	748
Total expenditure	888	861	3.2	793	12.0	1,756	3,295	4,417
EBITDA	119	109	9.2	112	6.3	196	427	592
Depreciation	6	5	5.8	5	19.6	15	20	36
EBIT	113	104	9.4	107	5.7	180	407	556
Interest	18	25	(30.0)	19	(6.3)	66	75	82
Other income	1	3	NA	3	(67.9)	5	6	7
Extraordinary items			NA	-	-	-	-	-
PBT	97	81	18.7	91	5.9	120	338	481
Tax	(4)	44	(109.0)	32	(112.1)	45	81	144
Adjusted net profit	100	38	165.6	59	70.5	75	257	337
Reported net profit	100	38	165.6	59	70.5	75	257	337
Equity capital(FV:INR10)	156	156	-	156	-	156	156	156
# of shares (mn)	16	16	-	16	-	16	16	16
EPS (INR)	6.4	2.4	165.6	3.8	70.5	4.8	16.5	21.5
Market cap. (INR mn)						3,198	3,198	3,198
PE (x)						32.0	12.4	9.5
EV/EBITDA (x)						19.4	8.9	6.4
Market cap / Revenues (x)						1.6	0.9	0.6
<b>as % of net revenues</b>								
Raw material	48.7	59.2	(17.8)	44.1	10.5	70.0	52.3	59.3
Other operating expenses	32.5	22.9	42.1	36.4	(10.9)	10.7	29.5	14.9
EBITDA	11.8	11.2	5.1	12.4	(4.5)	10.0	11.5	11.8
Adjusted net profit	10.0	3.9	155.8	6.5	53.2	3.8	6.9	6.7
Tax rate	(4.0)	53.5	(107.6)	35.3	(111.4)	37.5	23.9	30.0

\* For nine months

## Company Background

RPG Transmission (RPGT) was incorporated in 1951 and is promoted by the RPG group. RPGT is in the business of design and manufacture of transmission towers. RPGT is one of the key players in the Indian power tower industry. The company derives its revenues from the Indian market and has no international presence. The order backlog at the end of Q4FY07 was INR 4.5 bn.

## Investment Theme

India's inter-regional power transmission capacity is likely to increase from ~11,500 MW currently to ~16,450 MW at the end of the tenth plan (FY07-end) and to ~37,150 MW at the end of the eleventh plan (FY12-end). Progress on planned power T&D infrastructure upgradation is driving the current phase of growth. We expect an investment of ~INR 2,475 bn for the expansion of the transmission infrastructure during the eleventh plan. Consequently, the addressable market for the power transmission tower industry from this opportunity is likely to be ~INR 250 bn over the eleventh plan period. We believe, RPGT is well placed to leverage from the opportunity thrown up.

## Key Risks

Power T&D investments are executed by state utilities, which, in turn, are mandated by the government. Hence, any change in the political environment can potentially impact the pace of execution in the industry, thus impacting the timing of revenue growth. Additionally, the customer concentration risk is high in the business and this in turn impacts the bargaining power of transmission tower companies.

## Financial Statements

Income statement					(INR mn)
Year to financial year ending	FY05#	FY06E^	FY07UA	FY08E	FY09E
Income from operations	1,278	1,951	3,722	5,009	6,536
Direct costs	921	1,365	1,945	2,968	3,877
Employee costs	232	181	253	701	914
Other expenses	177	209	1,097	748	977
Total operating expenses	1,331	1,756	3,295	4,417	5,768
EBITDA	(52)	196	427	592	768
Depreciation and amortisation	32	15	20	36	45
EBIT	(84)	180	407	556	723
Interest expenses	27	66	75	82	107
Other income	170	5	6	7	11
Profit before tax	59	120	338	481	627
Provision for tax	(114)	45	81	144	201
Extraordinary items	(126)	-	-	-	-
Reported profit	46	75	257	337	426
Adjusted net profit	173	75	257	337	426
Shares outstanding	12.9	15.6	15.6	15.6	15.6
Dividend per share	-	-	2.2	2.4	3.0
Dividend payout %	-	-	13.6	11.0	11.0

### Common size metrics- as % of net revenues

Year to financial year ending	FY05#	FY06E^	FY07UA	FY08E	FY09E
Operating expenses	104.1	90.0	88.5	88.2	88.2
Depreciation	2.5	0.8	0.5	0.7	0.7
Interest expenditure	2.1	3.4	2.0	1.6	1.6
EBITDA margins	(4.1)	10.0	11.5	11.8	11.8
Net profit margins (reported)	3.6	3.8	6.9	6.7	6.5

### Growth metrics (%) annualised

Year to financial year ending	FY05#	FY06E^	FY07UA	FY08E	FY09E
Revenues	28.6	154.4	43.1	34.6	30.5
EBITDA	59.7	725.6	63.6	38.6	29.8
PBT	117.6	240.2	111.0	42.3	30.4
Net profit	113.8	169.1	156.7	30.9	26.7
EPS	113.3	121.7	156.7	30.9	26.7

Cash flow statement					(INR mn)
Year to financial year ending	FY05#	FY06E^	FY07E	FY08E	FY09E
Net profit	173	75	257	337	426
Add: Depreciation	32	15	20	36	45
Add: Deferred tax	(115)	90	28	38	63
Gross cash flow	90	181	305	411	534
Less: Dividends	-	-	39	42	53
Less: Changes in W. C.	(280)	233	149	53	167
Operating cash flow	370	(53)	117	316	315
Less: Change in investments	(329)	-	-	-	-
Less: Capex	3	9	34	50	50
<b>Free cash flow</b>	<b>696</b>	<b>(62)</b>	<b>83</b>	<b>266</b>	<b>265</b>

<b>Balance sheet</b>					(INR mn)
<b>As on Financial year end</b>	<b>FY05#</b>	<b>FY06E^</b>	<b>FY07E</b>	<b>FY08E</b>	<b>FY09E</b>
Equity capital	129	156	156	156	156
Preference capital	0	13	13	13	13
Reserves & surplus	(64)	216	495	790	1,163
Shareholders funds	298	385	664	959	1,332
Secured loans	748	691	311	311	311
Unsecured loans	72	0	320	320	320
Borrowings	820	692	631	631	631
<b>Sources of funds</b>	<b>1,118</b>	<b>1,076</b>	<b>1,295</b>	<b>1,590</b>	<b>1,964</b>
Gross block	627	617	637	687	737
Accumulated epreciation	469	464	484	519	565
Net block	157	153	153	168	172
Capital work in progress	2	0	-	-	-
Total fixed assets	159	153	153	168	172
Investments	0.0	0.0	0.0	0.0	0.0
Inventories	284	417	644	845	1,105
Sundry debtors	1,168	1,422	1,479	1,990	2,597
Cash and equivalents	270	91	189	455	720
Loans and advances	282	337	337	337	337
Total current assets	2,003	2,266	2,649	3,627	4,758
Sundry creditors and others	1,285	1,496	1,561	2,144	2,799
Provisions	53	51	120	198	241
Total CL & provisions	1,338	1,547	1,682	2,342	3,041
Net current assets	665	719	967	1,286	1,718
Add / (Less) : Deferred tax asset/ liability	294	203	175	137	74
<b>Uses of funds</b>	<b>1,118</b>	<b>1,076</b>	<b>1,295</b>	<b>1,590</b>	<b>1,964</b>
Book value per share (INR)	23	25	42	61	85

**Ratios**

<b>Year to financial year ending</b>	<b>FY05#</b>	<b>FY06E^</b>	<b>FY07E</b>	<b>FY08E</b>	<b>FY09E</b>
ROAE (%)	29.4	22.0	49.0	41.5	37.2
ROACE (%)	(6.8)	16.4	34.3	38.5	40.7
Current ratio	1.5	1.5	1.6	1.5	1.6
Debtors (days)	334	266	145	145	145
Fixed assets t/o (x)	8.4	11.4	21.5	26.4	33.5
Average working capital t/o (x)	1.9	2.8	4.4	4.4	4.4
Average capital t/o (x)	1.0	1.8	3.1	3.5	3.7
Net debt/Equity	1.8	1.6	0.7	0.2	(0.1)
Gross debt/Equity	2.8	1.8	1.0	0.7	0.5

**Valuations parameters**

<b>Year to financial year ending</b>	<b>FY05#</b>	<b>FY06E^</b>	<b>FY07E</b>	<b>FY08E</b>	<b>FY09E</b>
EPS (INR) (annualised)	2.9	6.4	16.5	21.5	27.3
Y-o-Y growth (%) (annualised)	113.3	121.7	156.7	30.9	26.7
CEPS (INR) (annualised)	4.9	7.7	17.7	23.8	30.2
PE (x)	70.9	32.0	12.4	9.5	7.5
Price/BV(x)	8.8	8.3	4.8	3.3	2.4
EV/Sales (x)	3.0	1.9	1.0	0.8	0.6
EV/EBITDA (x)	n.a	19.4	8.9	6.4	4.9

# FY05 is 15 months year to June ending

^ FY06E is 9 months year to March ending

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### RATING INTERPRETATION

<b>Buy</b>	Expected to appreciate more than 20% over a 12-month period	<b>Reduce</b>	Expected to depreciate up to 10% over a 12-month period
<b>Accumulate</b>	Expected to appreciate up to 20% over a 12-month period	<b>Sell</b>	Expected to depreciate more than 10% over a 12-month period
<b>Trading Buy</b>	Expected to appreciate more than 10% over a 45-day period	<b>Trading Sell</b>	Expected to depreciate more than 10% over a 45-day period

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