

Capacity expansion to continue

27th April 2007

BUY

Price	Target Price
Rs190	Rs205

Sensex - 14,229

Price Performance

(%)	1M	3M	6M	12M
Absolute	13	11	37	1
Rel. to Sensex	4	10	23	(15)

Source: Bloomberg

Stock Details

Sector	Graphite
Reuters	HEGL.BO
Bloomberg	HEG@IN
Equity Capital (Rs mn)	403.1
Face Value (Rs)	10
52 Week H/L (Rs)	207/98
Market Cap (Rs bn)	7.7
Daily Avg Vol (No of shares)	60127
Daily Avg Turnover (US\$ mn)	0.3

Shareholding Pattern (%)

(31st Mar.'06)

Promoters	56.6
FII/NRI	8.0
Institutions	16.6
Private Corp.	5.4
Public	13.5

HEG declared its 4QFY07 and annual results. The numbers were in line with our expectations. During 4QFY07, The company reported PAT of Rs299mn, yoy up 138% and qoq up 80.9%, while revenue grew to Rs2.44bn yoy up 26.1% and qoq up 29.9%. EBITDA margins moved up to 23.1% up by 526bps yoy and by 104bps qoq. HEG reported basic EPS of Rs7.41 for 4QFY07 up 138% yoy and 80.9% qoq. For full year FY07, HEG reported PAT of Rs738mn yoy up 89.7% and net sales of Rs8.179bn yoy up 55.7%.

Other key points:

- HEG has already booked 90% of the graphite electrode capacity for FY08 at higher rates as compared to FY07.
- With a strong outlook for steel, demand for graphite electrode likely to be robust for FY08.
- The steel business has reported profit at PBT level in the reported quarter due to improvement in realizations.
- The company will invest Rs800mn to set up a 30MW merchant thermal power plant.
- It will also invest Rs350mn to increase the capacity of graphite electrode from 52,000t to 57,000t through de-bottlenecking in the re-baking division.
- HEG expects the payback in 30 months for both the projects.
- The stock currently trades at 8.3x our FY08 FDEPS estimate of Rs22.8. We maintain buy on the stock.

Valuations

At CMP of Rs 190, the stock currently trades at 8.3x our estimated FY08 FDEPS of Rs22.8. We maintain our buy recommendation on the stock with a target price of Rs205.

	Net Sales	EBITDA (Core)	EBITDA (%)	RocE (%)	EV/ EBITDA	P/BV	Div Yld (%)	EPS (Rs)	P/E
YE-Mar									
FY05	4,550	798	17.5	12.6	15.3	2.7	1.5	10.3	19.0
FY06	5,292	5,292	21.8	12.3	15.3	2.5	2.2	1.5	23.5
FY07E	8,179	1,746	21.4	15.1	8.4	2.1	2.2	15.8	12.4
FY08E	10927	2491	22.8	20.2	5.9	1.7	2.6	22.9	8.5

Vishal Chandak

vishal.chandak@emkayshare.com

+91 22 6612 1251

Quarterly Results

	4QFY07	4Q 2006	% yoy	3QFY07	% qoq	FY07	FY06	% yoy
	31-Mar-07	31-Mar-06		31-Dec-06		31-Mar-07	31-Mar-06	
Domestic Sales	1,332	1,171	13.8%	1,232	8.1%	4,857	3,458	40.4%
Export Sales	1,548	1,096	41.2%	1,046	47.9%	4,919	2,905	69.3%
Inter- div sales	-299	-222	34.6%	-274	9.1%	-1,100	-759	44.9%
Gross Sales	2,581	2,045	26.2%	2,005	28.8%	8,675	5,604	54.8%
Excise	-137	-107	28.3%	-124	10.8%	-497	-351	41.3%
Adjusted Net Sales	2,444	1,938	26.1%	1,881	29.9%	8,179	5,253	55.7%
Expenditure								
Consumption of raw material	952	1,058	-10.0%	1,076	-11.5%	4,091	2,669	53.3%
as a % to net sales	39.0%	54.6%				50.0%	50.8%	-80 bps
Change in stock	239	-130	-283.8%	-353	-167.6%	-353	-565	-37.5%
Total cost of goods sold	1,191	928	28.4%	723	64.8%	3,738	2,104	77.7%
as a % to net sales	48.7%	47.9%		38.4%		45.7%	40.1%	
Gross profit	1,253	1,010	24.1%	1,158	8.2%	4,441	3,149	41.0%
Gross margin	51.3%	52.1%	-85 bps	61.6%	-1,031 bps	54.3%	59.9%	-565 bps
Personnel exp	91	84	8.3%	89	1.8%	352	327	7.6%
Power and fuel	157	201	-22.2%	193	-19.0%	660	584	13.0%
Other exp	441	380	16.3%	461	-4.2%	1,683	1,123	49.9%
as a % to net sales		19.6%				20.6%	21.4%	-79 bps
Total operating exp	689	665	3.7%	744	-7.3%	2,695	2,034	32.5%
EBITDA	564	345	63.4%	414	36.1%	1,746	1,115	56.6%
Ebitda margin	23.1%	17.8%	526 bps	22.0%	104 bps	21.4%	21.2%	12 bps
Depreciation	130	125	4.2%	115	13.0%	477	396	20.3%
Amortization						10	0	
EBIT	434	220	96.9%	299	44.9%	1,259	719	75.1%
EBIT margin	17.8%	11.4%		15.9%		15.4%	13.7%	171 bps
Interest	121	93	29.7%	107	13.0%	461	288	59.9%
Other income	106	45	136.5%	27	287.9%	202	99	103.8%
PBT	419	172	143.5%	220	90.5%	1,001	530	88.8%
Provision for tax	120	47	158.5%	55	119.3%	262	141	86.3%
As a % to PBT	28.7%	27.0%	6.2%	24.9%		26.2%	26.6%	
- Current tax	73	22	233.2%	15	405.5%	119	52	130.2%
- Deferred tax liability	46	23	101.3%	39	17.9%	140	82	70.4%
- Fringe benefit tax	1	2		1		4	7	-49.3%
PAT	299	126	137.9%	165	80.9%	738	389	89.7%
Net margin	12.2%	6.5%	574 bps	8.8%	344 bps	9.0%	7.4%	162 bps
less: E/o Items adjusted for tax	0	0		0				
Adjusted PAT	299	126	137.9%	165	80.9%	738	389	89.7%
Adjusted PAT margin	12.2%	6.5%	574 bps	8.8%	344 bps	9.0%	7.4%	162 bps
Equity capital (basic)	403	403		403		403	403	
Equity capital (Fully diluted)	469	469		469		469	469	
Reported EPS								
- Basic	7.41	3.11	138.0%	4.10	80.9%	18.32	9.66	89.7%
- Diluted	6.37	2.68	137.9%	3.52	80.9%	15.76	8.31	89.7%
Adjusted EPS								
- Basic	7.41	3.11	138.0%	4.10	80.9%	18.32	9.66	89.7%
- Diluted	6.37	2.68	137.9%	3.52	80.9%	15.76	8.31	89.7%

Segment Analysis

	4QFY07	4Q 2006	% yoy	3QFY07	% qoq	FY07	FY06	% yoy
	31-Mar-07	31-Mar-06		31-Dec-06		31-Mar-07	31-Mar-06	
Segment Revenue								
Graphite	1,941	1,368	42%	1,371	42%	6,301	4,089	54%
Steel	499	534	-6%	427	17%	1,740	1,064	64%
Power	325	281	16%	332	-2%	1,229	898	37%
Others	82	21	293%	52	59%	211	60	250%
Less: inter-segment sales	-299	-222	35%	-274	9%	-1,100	-759	45%
Less: Other Income incl in sales	-106	-45	137%	-27	288%	-202	-99	104%
Total Revenue	2,444	1,938	26%	1,881	30%	8,179	5,253	56%

Segment PBT

Graphite	273	193	41%	181	51%	892	531	68%
Steel	11	-11	-196%	-27	-139%	-46	-18	152%
Power	137	78	76%	136	1%	464	264	76%
Others	58	5	1033%	37	55%	151	41	267%
Less: Interest charges	-60	-93	-36%	-107	-44%	-461	-288	60%
Reported Profit Before Tax	419	172	143%	220	90%	1,001	530	89%

Segment PBT margin

Graphite	14%	14%	-5 bps	13%	90 bps	14%	13%	116 bps
Steel	2%	-2%	424 bps	-6%	851 bps	-3%	-2%	-92 bps
Power	42%	28%	1,443 bps	41%	112 bps	38%	29%	840 bps

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Emkay Share and Stock Brokers Ltd.,

Paragon Center, Ground Floor, C-6

Pandurang Budhkar Marg, Worli, Mumbai – 400 013. , Tel no. 66121212. Fax: 66121299