



INDIA RESEARCH

# Welspun Gujarat

**Rs198**  
**NEUTRAL**

RESULT NOTE

Mkt Cap: Rs37bn, US\$769m

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**Result:** Q1FY10

**Comment:** Extraordinary income boost up profits

**Last report:** 30<sup>th</sup> January 2009 (Price Rs71; Recommendation: Neutral)

## Key valuation metrics

Year to March (Rs m)	Net Revenues	yoy chg (%)	Net Profit	EPS (Rs.)	yoy chg (%)	PER (x)
FY2007	26,784	46	1,425	7.6	48	26.0
FY2008	40,104	50	3,514	18.8	147	10.5
FY2009P	58,783	47	2,336	12.5	-34	15.9
FY2010E*	56,916	-3	4,213	22.5	80	8.8
FY2011E	48,709	-14	4,224	22.6	0	8.8

Source: IDFC-SSKI Estimates, \*includes expected reversal in forex provisioning during the year

## KEY RESULT HIGHLIGHTS

- WGSR's reported net profits for Q1FY10 grew by 94%yoy to Rs1.4bn, significantly ahead of our estimates (at Rs806m). However, this included significant extra-ordinary gains of Rs375m on account of reversal of forex provisioning and coil sales. Profits were also boosted by ~Rs150m of coating related income in the US subsidiary.
- WGSR Q1FY10 revenues grew by 72%yoy to Rs18.8bn. Higher than expected sales volumes in LSAW pipes and (external) plate segment resulted in higher than expected revenues for the quarter. LSAW pipe and external plate sales volumes increased by 195% and 243%qoq respectively to 86,058 and 27,921tonnes respectively. HSAW pipe sales volumes stood at 105,686tonnes for the quarter, broadly in line with estimates.
- EBITDA/tonne for the pipe and plate segment for the quarter stood at Rs10,503/tonne and Rs6,000/tonne respectively broadly inline with estimates.
- WGSR's newly commissioned 0.3mt spiral mill at Little Rock, USA registered 13,500 tonnes of sales volumes in Q1FY10. Net sales and EBITDA for WGSR's US operations for the quarter stood at Rs1.3bn and Rs300m respectively. However, operating profit for the quarter included a significant ~Rs150m of coating related income.
- Order book: WGSR added Rs12bn of orders during the quarter taking the order book position to Rs68bn (~1.1x FY09 sales) at the end of the quarter. The entire order book corresponds to 0.68m tonnes of pipe and 0.125m tonnes of external pipe orders ensuring reasonable revenue visibility for FY10. Having said that, WGSR's order book position has continued to decline sequentially (over 4 consecutive quarters now), thereby offering limited revenue visibility over FY11.
- 'Non SEZ status' for 0.3mt LSAW pipe mill: Announcement of investment linked tax benefits for laying cross country pipe networks along with proposal to develop long distance gas highways (National Gas Grid) in recent union budget is expected to boost domestic line pipes demand. To capture the expected opportunity in domestic line pipe demand, WGSR has initiated the process to transfer the status of its 0.3mt LSAW pipe mill in Anjar,

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Gujarat from SEZ to Non-SEZ. Successful transfer to non-SEZ status in our view would help WGSR eliminate pricing related uncertainties while catering to domestic market, on back of changes in custom duties (if any).

- Expansion plans: WGSR announced to incur a capex of Rs5.5bn over next 12-15months. A large 65% of the envisaged capex would be utilized towards setting up a new 0.3mtpa HSAW pipe mill in South East India. Management indicated that the new spiral mill would be commissioned by Q3FY11, and would service oil & gas and water segments. The balance 35% capex (~Rs2bn) would be utilized for 0.3mt LSAW pipe facility at Anjar, Gujarat.
- The de-merger scheme for transfer of Plate and Coil Mill Division along with all associated assets/liabilities, to wholly owned subsidiary 'Welspun Steel Plates and Coil Mills Pvt. Ltd' has been approved by creditors and petition for the same has been filed in Gujarat High Court. The de-merger would become effective retrospectively from April 01, 2009.

### □ Maintain Neutral

A rise in Baltic freight index, trends observed in global rig count and crude prices point towards marginal improvement in global OCTG markets. Favorable investment linked tax incentive schemes announced in the recent union budget could lead to higher investment in cross-country pipe networks domestically, thereby boosting pipe demand. Even as we spot green shoots for the OCTG industry, we believe 'sustained' recovery in global crude prices would be a must for revival in revenues visibility of the pipe mills. WGSR's order book at Rs68bn (~1.1x FY09 revenues) ensures reasonable revenue visibility for FY10. However, WGSR's order book has witnessed four consecutive quarters of decline, indicating incremental orders coming slow. Slower order book addition offers limited revenue visibility for WGSR over FY11. Given lower growth visibility, we believe the current valuations at ~9x FY11 earnings are reasonable. Maintain Neutral rating on the stock with a 12-month DCF based price target of Rs218/share.

#### Quarterly Results

Particulars ( Rs m)	1QFY09	2QFY09	3QFY09	4QFY09	FY09	1QFY10
<b>Net Sales</b>	<b>10,903</b>	<b>14,928</b>	<b>14,566</b>	<b>18,318</b>	<b>58,783</b>	<b>18,798</b>
%change yoy	35	61	41	49	47	72
Other Income	63.7	(845)	(369.7)	26	178.8	40
Total Income	10,967	14,083	14,196	18,344	58,962	18,838
Total Expenditure	9,164	12,474	13,138	16,709	52,437	15,768
<b>EBITDA</b>	<b>1,739</b>	<b>2,453</b>	<b>1,851</b>	<b>1,606</b>	<b>6,346</b>	<b>3,030</b>
%change yoy	30	60	6	(18)	0	74
Interest	439	314	480	501	1,735	617
PBDT	1,364	1,294	1,001	1,131	4,790	2,452
Depreciation	294	300	316	344	1,254	362
<b>PBT</b>	<b>1,070</b>	<b>994</b>	<b>686</b>	<b>787</b>	<b>3,536</b>	<b>2,091</b>
Tax	358	341	231	269	1,200	708
<b>Reported PAT</b>	<b>712</b>	<b>653</b>	<b>455</b>	<b>518</b>	<b>2,336</b>	<b>1,382</b>
%change yoy	3	(21)	(53)	(49)	(34)	94
Extra-ordinary Items		884	804	-	-	375
Adj. PAT	712	1,537	1,259	518	2,336	1,007

Source: IDFC-SSKI Research

Production mix

(tonnes)	1QFY10	1QFY09	% chg yoy
LSAW	81,293	49,475	(39.1)
HSAW	116,507	91,364	(21.6)
ERW	32,450	19,215	(40.8)
<b>Total Pipes</b>	<b>230,250</b>	<b>160,054</b>	<b>(30.5)</b>
<b>Plates</b>	<b>92,252</b>	<b>31,541</b>	<b>(65.8)</b>

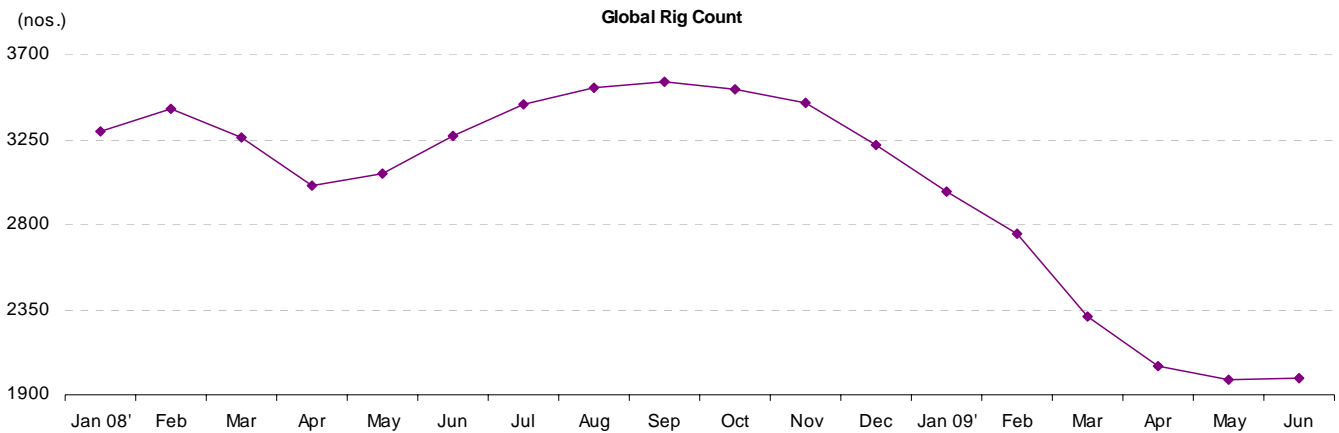
Source: Company, IDFC-SSKI Research

Sales mix

(tonnes)	1QFY10	1QFY09	% chg yoy
LSAW	86,058	40,077	(53.4)
HSAW	105,686	87,236	(17.5)
ERW	25,363	17,137	(32.4)
<b>Total Pipe Sales (In tonnes)</b>	<b>217,107</b>	<b>144,450</b>	<b>(33.5)</b>
Plates (external sales only)	27,921	5,565	(80.1)
<b>Total sales tonnes (Incl plates ext sales)</b>	<b>62,338</b>	<b>17,890</b>	<b>(71.3)</b>

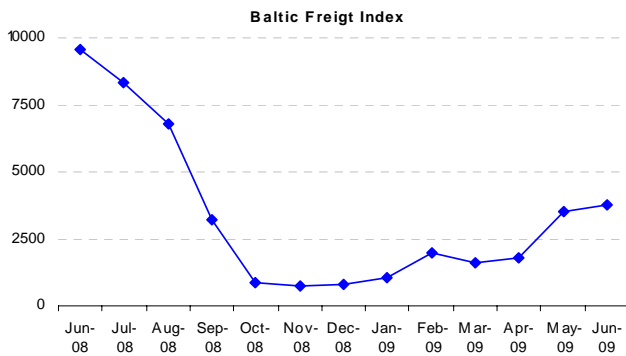
Source: Company, IDFC-SSKI Research

Exhibit: Global Rig Count - already at a bottom?

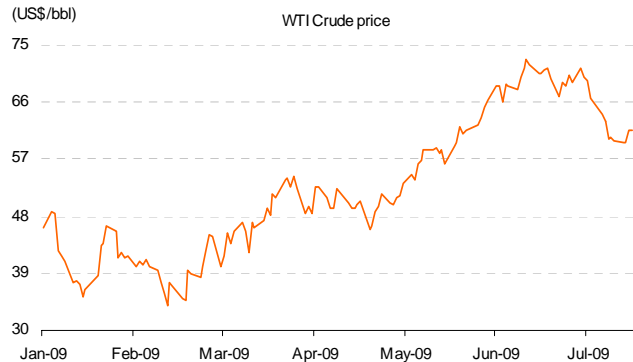


Source: Baker Hughes

Exhibit: Baltic Freight Index - is the trend sustainable?



WTI Crude prices - finding momentum?



Source: IDFC-SSKI Research, Bloomberg

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