

**Key data**

Sector	Steel Pipes
Market Cap	Rs34bn/US\$0.8bn
52 Wk H/L (Rs)	675/381
Avg. daily vol. (6 month)	201,577

BSE Code	500265
NSE Code	MAHSEAMLES
Bloomberg	MHS IN
Reuters	MHSM.BO

Sensex	19,035
Nifty	5,695

**Shareholding pattern (%)**

	30-Jun-07	30-Sep-07
FII's NRI, ADR/GDR	15.4	14.1
MFs and institutions	14.6	15.8
Promoters	41.7	42.0
Others	28.3	28.1

**Absolute returns (%)**

	1mth	3mth	12mth
MHS	(9.9)	(14.7)	3.6
Sensex	3.3	26.8	42.1
BSE Metals	14.9	54.8	87.4

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# Maharashtra Seamless

**Accumulate**
**Current Price: Rs493**
**Target price: Rs610**
**Results were below our estimates.**
**Figure 1: Actual Vs Religare Estimates**

	Q2FY08A	Q2FY08E	Difference (%)
Net sales	3,856	4,745	(18.7)
EBITDA	833	1,160	(28.2)
EBITDA margins (%)	21.6	24.5	-284bps
PAT	581	830	(30.0)
PAT margins (%)	15.1	17.5	-242bps

Source: Religare Institutional Equity Research

**Financial highlights**

- **Net Sales** have risen by 11.3% YoY to Rs3.9bn.
- **EBITDA** declined by 9.4% YoY to Rs834mn. EBITDA margins have declined to 21.6%, a drop of 500bps over Q2FY07. EBITDA margins have been impacted because of increase in share of revenues from the low margin ERW segment (24.4% of net sales in Q2FY08, an increase of 400bps YoY). EBIT margins have significantly declined in the seamless segment (decline of 339bps YoY to 29.2%) because of the lack of high margin 14" pipe orders due to the postponement of capex in the E&P sector due to lack of availability of equipments including rigs.
- **Adjusted PAT** has declined by 6.2% YoY to Rs582mn. Adj PAT margins have declined to 15.1%, a decrease of 280bps over Q2FY07. Decline in PAT is lower than EBITDA because of lower effective tax rate, which declined by 260bps YoY to 30.9%.

**Valuations and Recommendation**

The stock currently trades at 12.5x 1-year forward diluted earnings. We are revising our one year target price from Rs800 to Rs610 because of a downward revision in our earnings estimate. To reflect this we are downgrading our rating from **Buy** to **Accumulate**. Despite the sharp downward revision we remain bullish on company's prospects as the outlook for the industry is still positive and we believe that the current slowdown will start reversing soon.

**Figure 2: Quarterly Performance**

	FY07				FY08E		(Rs mn)	
	1Q	2Q	3Q	4Q	1Q	2QA	FY07	FY08E
<b>Net Sales</b>	<b>3,388</b>	<b>3,465</b>	<b>3,426</b>	<b>3,668</b>	<b>3,519</b>	<b>3,856</b>	<b>13,947</b>	<b>16,193</b>
Change %	67.3	67.4	26.5	25.6	3.9	11.3	43.4	16.1
<b>EBITDA</b>	<b>900</b>	<b>920</b>	<b>862</b>	<b>740</b>	<b>820</b>	<b>834</b>	<b>3,422</b>	<b>3,578</b>
EBITDA margin (%)	26.6	26.6	25.2	20.2	23.3	21.6	24.5	22.1
Change (%)	120.7	114.4	36.5	18.4	(8.9)	(9.4)	63.5	4.6
Depreciation	45	45	42	39	44	44	171	174
Other Income	61	69	79	109	109	58	317	362
Interest exp/(inc)	10	10	6	7	7	6	33	25
<b>PBT</b>	<b>906</b>	<b>934</b>	<b>892</b>	<b>803</b>	<b>878</b>	<b>842</b>	<b>3,535</b>	<b>3,741</b>
PBT margin (%)	26.7	27.0	26.0	21.9	24.9	21.8	25.3	23.1
PBT growth (%)	143.2	124.1	41.9	28.1	(3.1)	(9.8)	70.7	5.9
Extraordinary exp/(Inc)	0	0	0	0	0	0	0	0
Tax	305	313	293	270	297	261	1,181	1,256
Effective tax rate (%)	33.7	33.5	32.8	33.7	33.8	30.9	33.4	33.6
<b>PAT reported</b>	<b>601</b>	<b>621</b>	<b>600</b>	<b>533</b>	<b>581</b>	<b>582</b>	<b>2,354</b>	<b>2,486</b>
<b>Adjusted PAT *</b>	<b>601</b>	<b>621</b>	<b>600</b>	<b>533</b>	<b>581</b>	<b>582</b>	<b>2,354</b>	<b>2,486</b>
Adj PAT margin (%)	17.7	17.9	17.5	14.5	16.5	15.1	16.9	15.0
Change (%)	143.0	119.2	43.7	26.9	(3.2)	(6.3)	72.1	5.6
Equity Capital (Rs mn)	298	308	334	350	353	353	350	353
Adj EPS	10.1	10.1	9.0	7.6	8.2	8.2	33.7	35.2

\* Excluding extraordinary

## Other business highlights

- Order book:** The current order book of the company stands at Rs8.0bn (as against Rs11bn in Q1FY08) which is 0.52x its FY07 gross sales. This decline in order book is largely because of the postponement of capex by oil & gas companies due to non availability of equipment & rigs.

**Figure 3: Segment results - Maharashtra Seamless**

(Rs mn)	Q2FY08	Q2FY07	Difference (%)	Q1FY08	Difference (%)
<b>Revenue</b>					
Seamless Pipes	2,893	2,735	5.8	2,732	5.9
ERW Pipes	940	708	32.7	777	20.9
<b>EBIT</b>					
Seamless Pipes	846	892	(5.2)	838	0.9
ERW Pipes	102	94	8.1	35	193.9
<b>EBIT margins (%)</b>					
Seamless Pipes	29.2	32.6	-339bps	30.7	-145bps
ERW Pipes	10.8	13.3	-247bps	4.5	637bps

Source: Religare Institutional Equity Research

**ERW segment:** In the last few quarters, the company has seen a sharp erosion in the margins of the ERW pipe segment. Margins declined from 13.3% in Q2FY07 to as low as 4.5% in Q1FY08, largely because of heavy dumping of cheap ERW pipes by Chinese companies in India and the presence of a large number of small manufacturers throughout India. Approval norms for ERW pipes are not as stringent as in seamless or SAW pipes. This had led to the creation of capacities by various smaller players across the country, which primarily sells to state water bodies or through dealer networks, where margins are lower because of intense competition.

To counter this the company is now focusing more on the industrial segment, where the competitive intensity is lower because of stringent approvals norms and requirement of timely delivery of large orders, which makes most of the smaller manufacturers ineligible. Thus, this sub-segment offers higher margins. The company has made some technological improvements like anti corrosion coating to improve margins. All these initiatives have led to a margin improvement by 637bps QoQ to 10.8% in Q2FY08. Margin improvement was also aided because of the reduction in the export rebate for Chinese companies, which in turn increased the value of imports from China.

We believe that margins of around 10% are sustainable because of the above mentioned initiatives by the company. However the presence of Chinese companies and lower barriers to entry will keep a check on the margins and they have now structurally moved down from their earlier levels.

**Seamless segment:** During the quarter the company has seen a decline in the margin of its seamless pipes due to higher contribution of lower diameter seamless pipes, where margins are lower than those of higher diameter seamless pipes.

In the lower diameter pipes, there is pressure on margins because of competition from Chinese companies and this is expected to continue and will structurally push down margins, till volumes rebound sharply. In the higher diameter seamless pipes, the major consumers who are oil & gas companies have postponed their E&P capex for the time being due to non availability of equipment and rigs. This in turn has pushed forward orders for the higher diameter pipes by 6-9 months. In the higher diameter pipes segment

competitive intensity is low as there is no other Indian company operating in this segment.

We believe that this slump in the demand in the high diameter seamless pipes is temporary because all the oil & gas companies have already placed the order for the equipment and will increase the E&P activity once they start receiving the delivery. In anticipation of this demand, the company plans to increase its seamless capacity by 75,000 to 500,000 TPA by the end of FY09. However, because of pushing forward of orders by 6-9 months we have revised our volume estimates downwards. Margins for the seamless segment will rebound with any increase in the share of higher margin higher diameter pipes and strong volumes growth. We have been conservative in our margins assumption for the seamless segment and have assumed margins at ~29% for the next two years.

**Figure 4: Table for earnings revision**

(Rs mn)	Earlier estimates			Revised estimates			Upgrade/ (downgrade) (%)		
	FY08E	FY09E	FY10E	FY08E	FY09E	FY10E	FY08E	FY09E	FY10E
Net Sales	19,096	23,175	27,652	16,193	19,452	24,580	(15.2)	(16.1)	(11.1)
EBITDA	4,705	5,839	6,995	3,578	4,194	5,225	(23.9)	(28.2)	(25.3)
EBITDA margin (%)	24.6	25.2	25.3	22.1	21.6	21.3	-254bps	-363bps	-404bps
PBT	5,033	6,321	7,526	3,741	4,502	5,625	(25.7)	(28.8)	(25.3)
Adj PAT	3,393	4,267	5,086	2,486	2,996	3,739	(26.7)	(29.8)	(26.5)
Adj PAT margin (%)	17.8	18.4	18.4	15.4	15.4	15.2	-242bps	-301bps	-318bps
Adj EPS (Rs)	48.1	60.5	72.1	35.2	42.5	53.0	(26.7)	(29.8)	(26.5)

Source: Religare Institutional Equity Research

We have revised our FY08, FY09 and FY10 net sales estimates downwards by 15.2%, 16.1% and 11.1% because of lower than expected volume growth in the seamless segment largely due to pushing back of orders by 6-9 months as discussed earlier in this report.

Our EBITDA margin estimates stands revised downwards for FY08, FY09 & FY10 by 254bps, 363bps and 404bps because of the higher share of low margin ERW segment, pushing forward of orders for the high margin 14" pipes and competition from the Chinese companies in the lower diameter seamless pipe segment.

We have revised our earning estimates downwards by 26.7%, 29.8% and 26.5% for FY08, FY09 and FY10 respectively to reflect downwards revision in our EBITDA margin estimates.

The downward revision in our volume and EBITDA margins assumption factors in the worst case scenario.

## Valuations and Recommendation

The stock currently trades at 12.5x 1-year forward diluted earnings. We are revising our one year target price from Rs800 to Rs610 because of a downward revision in our earnings estimate. To reflect this we are downgrading our rating from **Buy** to **Accumulate**.

Despite the sharp downward revision in our earnings and price target we remain bullish on company's prospects as the outlook for the industry is still positive and we believe that the current slowdown in industry growth is temporary and the sharp correction in the stock price reflects the worst. Hence any positive trigger including increase in order book position mainly because

of pickup in E&P activity or improvement in margins will lead to a spurt in stock price.

The company will be the key beneficiary of any improvement in the prospects of the seamless pipe segment as it is the only company in India to be present in both the lower and the higher diameter pipes segment.

**Figure 5: Valuation summary – Steel Pipes**

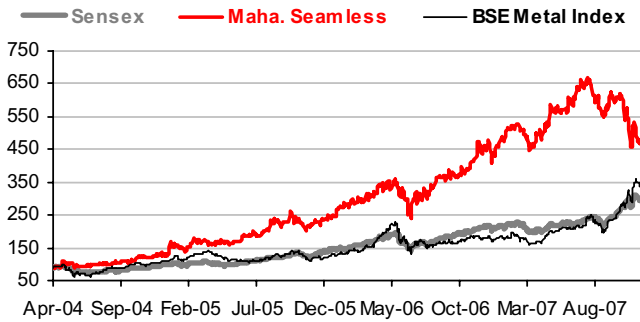
Company	Price (Rs)	Rating	Target Price (Rs)	Mkt Cap (Rs mn)	Sales		EBITDA		Adj PAT		Adj EPS		FY08E		FY09E	
					Q2FY08A (Rs mn)	YoY (%)	Q2FY08A (Rs mn)	YoY (%)	Q2FY08A (Rs mn)	YoY (%)	Q2FY08A (Rs)	YoY (%)	Adj EPS (Rs)	P/E (x)	Adj EPS (Rs)	P/E (x)
<b>Man Ind</b>	120	Accumulate	162	6,396	3,547	21.2	428	29.7	189	27.6	3.6	28.6	13.0	9.3	14.7	8.2
<b>Jindal Saw</b>	747	Accumulate	808	36,155	14,286	27.2	1,699	70.3	901	89.1	18.6	89.7	58.4	12.8	86.3	8.7
<b>Maharashtra Seamless</b>	493	Accumulate	610	34,776	3,856	11.3	834	(9.4)	582	(6.3)	8.2	18.8	35.4	13.9	42.5	11.6
<b>PSL</b>	488	Accumulate	456	16,641	4,965	60.9	499	43.8	191	41.5	4.4	41.9	27.3	17.9	42.2	11.6
<b>Welspun</b>	409	Buy	445	70,180	9,276	37.5	1,533	92.8	825	146.3	4.8	92.0	19.0	21.6	31.0	13.2

Source: Religare Institutional Equity Research  
 Jindal Saw is Dec ending co

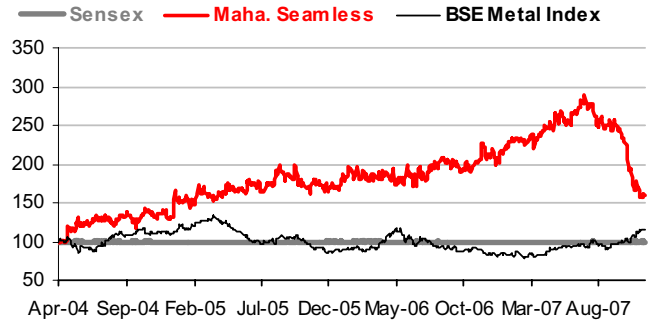
# Stock performance

## Maharashtra Seamless

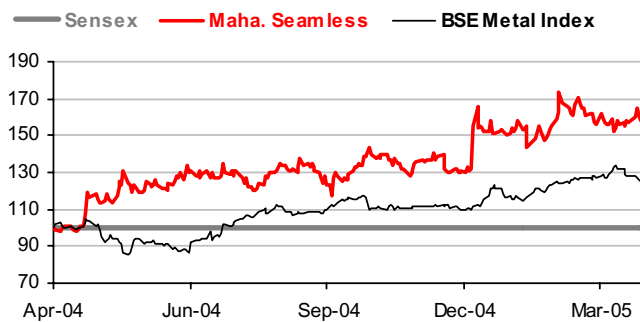
**Absolute Perf. From Apr 04**



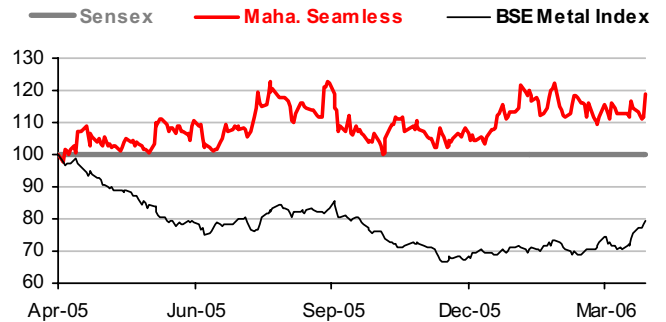
**Relative Perf. From Apr 04**



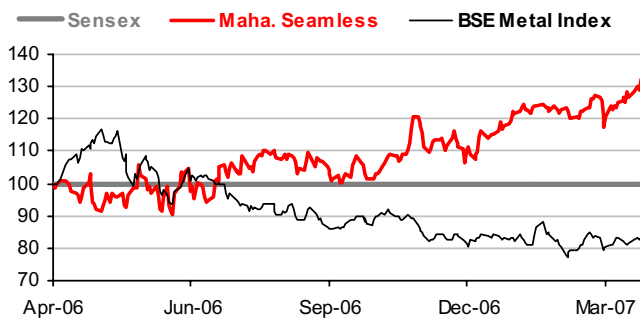
**Relative Perf. From Apr 04 to Mar 05**



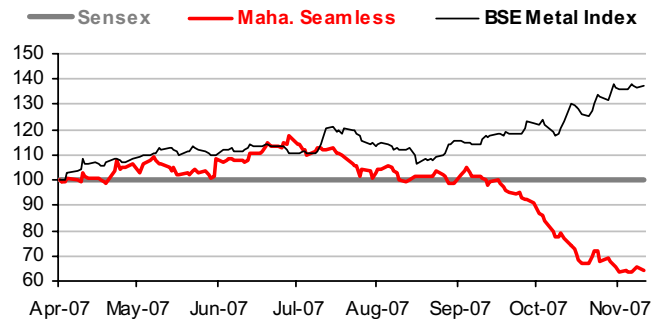
**Relative Perf. From Apr 05 to Mar 06**



**Relative Perf. From Apr 06 to Mar 07**



**Relative Perf. From Apr 07**

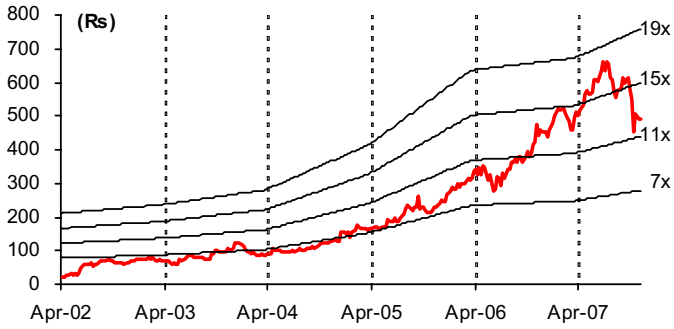


Source: Bloomberg, Religare Institutional Equity Research

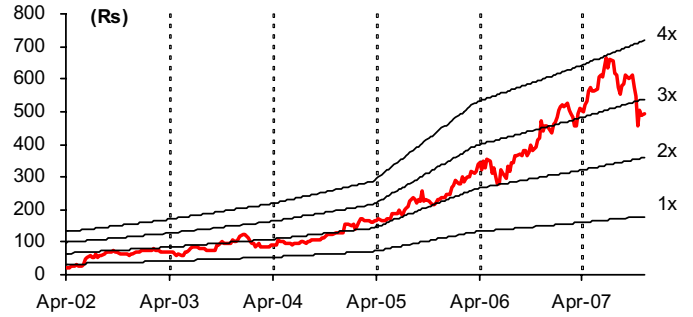
# 12 month forward rolling band charts

## Maharashtra Seamless

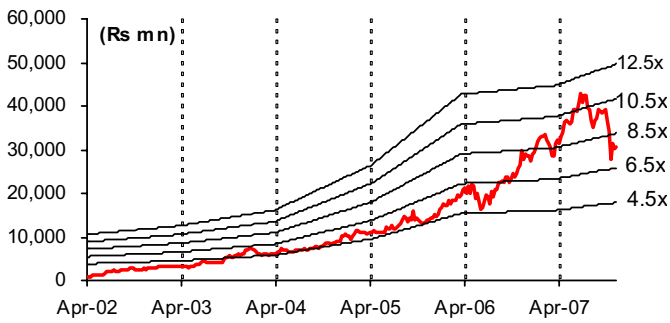
**P/E Band**



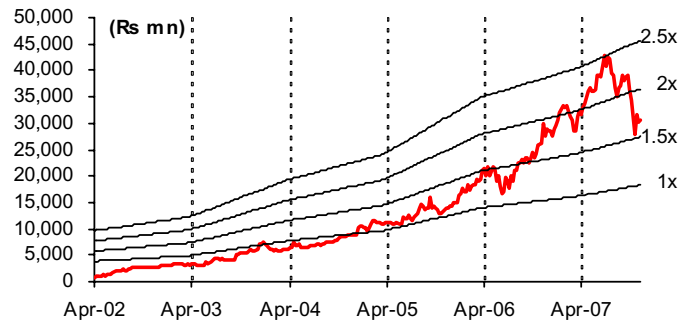
**P/BV Band**



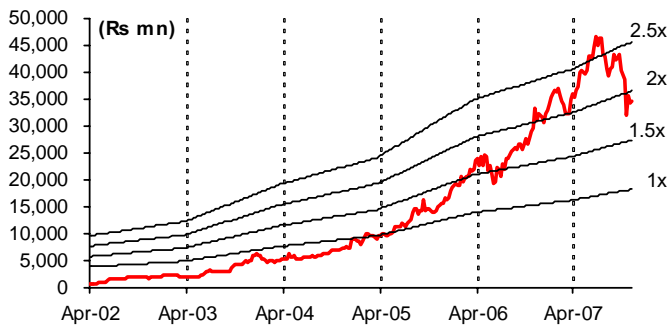
**EV/EBITDA Band**



**EV/Sales Band**



**Mkt cap/Sales Band**



## Financials

### Income statement

(Rs mn)

Y/E, 31st March	FY06	FY07	FY08E	FY09E	FY10E
Net sales	9,662	13,975	16,193	19,452	24,580
EBITDA	2,080	3,415	3,578	4,194	5,225
EBITDA margin (%)	21.5	24.4	22.1	21.6	21.3
Depreciation	146	163	174	179	180
EBIT	1,934	3,252	3,404	4,015	5,045
Other income	182	314	362	502	595
Interest Exp/(Inc)	48	35	25	15	15
PBT (Operating)	2,068	3,532	3,741	4,502	5,625
PBT margin (%)	21.4	25.3	23.1	23.1	22.9
Extra ord (inc)/exp	0.0	0.0	0.0	0.0	1.0
Taxes	678	1,188	1,256	1,506	1,887
Minority interest	0	0	0	0	0
PAT (Reported)	1,391	2,343	2,486	2,996	3,740
Less: Extra ordinary income / Others	0	0	0	0	0
Adj PAT	1,391	2,343	2,486	2,996	3,739
Adj PAT margin (%)	14.4	16.8	15.4	15.4	15.2

### Quarterly – Financials

(Rs mn)

(Rs mn)	Q2FY07	Q3FY07	Q4FY07	Q1FY08	Q2FY08
Net sales	3,465	3,426	3,668	3,519	3,856
Changes (%)	67.4	26.5	25.6	3.9	11.3
EBITDA	920	862	740	820	834
Changes (%)	114.4	36.5	18.4	(8.9)	(9.4)
Margin (%)	26.6	25.2	20.2	23.3	21.6
PAT	621	600	533	581	582
PAT adj	621	600	533	581	582
Changes (%)	119.2	43.7	26.9	(3.2)	(6.3)
Margin (%)	17.6	17.1	14.1	16.0	14.9
EPS adj (Rs)	10.1	9.0	7.6	8.2	8.2
EPS dil (Rs)	8.8	8.5	7.6	8.2	8.2

### Ratios

Y/E, 31st March	FY06	FY07	FY08E	FY09E	FY10E
<b>Growth</b>					
Net sales (%)	25.6	44.6	15.9	20.1	26.4
EBITDA (%)	61.9	64.2	4.8	17.2	24.6
PAT adjusted (%)	63.4	68.5	6.1	20.5	24.8
EPS adjusted (%)	63.4	38.9	5.2	20.5	24.8
EPS diluted (%)	47.7	53.7	5.6	20.0	24.8

### Valuations

P/E (x)	22.6	14.7	13.9	11.6	9.3
P/BV (x)	8.3	3.7	3.1	2.6	2.1
EV/EBITDA (x)	14.4	9.3	8.7	7.2	5.7
EV/Sales (x)	3.1	2.3	1.9	1.6	1.2

### Profitability

EBITDA margin (%)	21.5	24.4	22.1	21.6	21.3
Adj PAT margin (%)	14.4	16.8	15.4	15.4	15.2
RoE (%)	38.3	35.0	24.3	24.2	25.1
RoCE (%)	31.9	36.8	33.6	35.3	37.8
RoIC (%)*	26.2	35.4	32.1	32.4	33.6

### B/S ratios

Inventory days	166.3	109.9	120.0	125.0	135.0
Creditor days	44.5	15.8	15.8	15.8	15.8
Debtor days	52.9	52.1	52.1	52.1	52.1
Working Capital days	99.3	98.8	104.9	108.4	110.8
Net debt/equity	0.2	0.1	0.1	0.0	0.0

\* ROIC is calculated on post tax basis.

### Balance sheet

(Rs mn)

Y/E, 31st March	FY06	FY07	FY08E	FY09E	FY10E
<b>Liabilities</b>					
Equity share capital	288	350	353	353	353
Total Res. & Surplus	3,851	8,891	10,907	13,128	15,942
<b>Total Shareholders' fund</b>	<b>4,139</b>	<b>9,241</b>	<b>11,260</b>	<b>13,481</b>	<b>16,295</b>
Convertible Debt	3,343	152	0	0	0
Others Debt	1,587	930	833	33	33
<b>Total Loans</b>	<b>4,930</b>	<b>1,082</b>	<b>833</b>	<b>33</b>	<b>33</b>
<b>Deferred tax liability (net)</b>	<b>388</b>	<b>411</b>	<b>434</b>	<b>457</b>	<b>482</b>
<b>Total liabilities</b>	<b>9,457</b>	<b>10,734</b>	<b>12,527</b>	<b>13,971</b>	<b>16,810</b>

### Assets

Net fixed assets & others	2,644	2,802	3,104	3,302	3,517
Capital WIP & others	163	58	58	58	58
<b>Total non-current assets</b>	<b>2,808</b>	<b>2,859</b>	<b>3,162</b>	<b>3,360</b>	<b>3,575</b>
<b>Total investments - non current</b>	<b>43</b>	<b>43</b>	<b>43</b>	<b>43</b>	<b>43</b>
<b>Current assets</b>					
Inventories	2,755	2,513	3,285	4,137	5,682
Sundry debtors	1,400	1,996	2,313	2,778	3,510
Cash & cash equivalents	3,354	3,727	4,460	4,554	5,195
Cash	3,192	3,232	2,965	3,059	2,500
Liquid investments	162	495	1,495	1,495	2,695
Other current assets	309	394	486	584	737
<b>Total current assets</b>	<b>7,817</b>	<b>8,631</b>	<b>10,543</b>	<b>12,053</b>	<b>15,125</b>
<b>Total current liabilities</b>	<b>968</b>	<b>644</b>	<b>919</b>	<b>1,107</b>	<b>1,403</b>
<b>Total provisions</b>	<b>243</b>	<b>156</b>	<b>302</b>	<b>378</b>	<b>529</b>
<b>Net current assets</b>	<b>6,606</b>	<b>7,831</b>	<b>9,323</b>	<b>10,568</b>	<b>13,192</b>
<b>Misc. expenditure</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>Total assets</b>	<b>9,457</b>	<b>10,734</b>	<b>12,528</b>	<b>13,971</b>	<b>16,810</b>

### Cash flow

Y/E, 31st March	FY06	FY07	FY08E	FY09E	FY10E
<b>Cash from operations</b>					
PBT	2,068	3,527	3,741	4,502	5,625
Tax paid	(673)	(1,118)	(1,232)	(1,483)	(1,863)
Dep & amortization	25	(22)	199	194	195
Working capital changes	(1,583)	(859)	(905)	(1,227)	(2,135)
Others	0	0	0	0	1
<b>Net cash from operations</b>	<b>(162)</b>	<b>1,528</b>	<b>1,803</b>	<b>1,986</b>	<b>1,822</b>
<b>Cash from investments</b>					
Capital expenditure	(254)	(213)	(476)	(377)	(393)
Sale/purchase of inv & others	220	258	0	0	0
<b>Net cash from investments</b>	<b>(33)</b>	<b>45</b>	<b>(476)</b>	<b>(377)</b>	<b>(393)</b>
<b>Cash from financing</b>					
Issue of shares & share premium	0	0	3	0	0
Dividend paid	(163)	(461)	(473)	(699)	(773)
Debt change	3,709	(657)	(249)	(800)	0
Others	(18)	(12)	124	(15)	(15)
<b>Net cash from financing</b>	<b>3,528</b>	<b>(1,131)</b>	<b>(594)</b>	<b>(1,515)</b>	<b>(788)</b>
<b>Net change in cash &amp; cash equivalents</b>	<b>3,332</b>	<b>373</b>	<b>733</b>	<b>94</b>	<b>641</b>

### Per share data

Y/E, 31st March	FY06	FY07	FY08E	FY09E	FY10E
EPS adjusted	24.1	33.5	35.2	42.5	53.0
EPS diluted - wtd	21.8	33.5	35.4	42.5	53.0
CEPS	26.7	35.8	37.7	45.0	55.6
Book value	71.8	132.1	159.6	191.1	231.0
Dividend	4.2	6.1	7.5	9.4	11.2
O/s shs.-actual (mn)	57.6	69.9	70.5	70.5	70.5
O/s shs.-diluted (mn)	69.9	69.9	70.5	70.5	70.5
O/s shs wtd / diluted (mn)	57.6	69.9	70.5	70.5	70.5



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**Rating definition**

<b>Buy</b>	: > 15% returns relative to Sensex	<b>Accumulate</b>	: +5 to +15% returns relative to Sensex
<b>Sell</b>	: > (-)15% returns relative to Sensex	<b>Reduce</b>	: (-) 5 to (-) 15% returns relative to Sensex
<b>Hold</b>	: Upto + / (-) 5% returns relative to Sensex		



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