

# Sintex Industries

18 November 2011

Reuters: SNTX.BO; Bloomberg: SINT IN

## Weak Corporate Governance To Cap Valuation

Sintex Industries (SIL) clarified on 17 November 2011 that it has received a power EPC order from Shirpur Power, sponsored by its promoter. To fulfill the ambition of its promoter, SIL tried to diversify in unrelated power and oil & gas ventures in FY10, but following the concerns raised by investors, the promoter decided to set up the power plant in his personal capacity. But SIL's arm accepting the power EPC order from Shirpur Power and hiding this information from investors for four months has led to a corporate governance issue. Factoring in the order win, we revise our FY13 revenue/EBITDA/PAT estimates by 4.8%/1.1%/0.3%, respectively, but due to corporate governance issue we downgrade SIL to Hold from Buy with a revised TP of Rs96 (from Rs167 earlier).

**Sintex kept large order win a secret since a long time:** In a clarification issued on 17 November 2011, SIL stated that Sintex Infra Projects or SIPL (a100% subsidiary) received a Rs7bn order from Shirpur Power. As per information on the Department of Heavy Industries' web site, SIPL sub-contracted 2x150MW BTG (boiler, turbine and generator) order worth Rs7bn to Bharat Heavy Electricals in July 2011. The delay in making public the information regarding SIPL getting the order raises a serious corporate governance issue. However, as per our interaction with SIL management, total value of the order received by SIPL relating to the 2x150MW EPC project was ~Rs11bn out of which BTG order worth Rs7bn was sub-contracted to BHEL, while the Balance of Plant (BoP) work would be executed by SIPL along with its arm Durha Construction.

**Related party transaction raises concerns over corporate governance:** SIL's promoter and his relatives are shareholders of Sintex Power, one of the sponsors of Shirpur Power. Receipt of such large order by SIPL, SIL's arm, from Shirpur Power raises the issue regarding related party transaction, particularly when SIPL has not executed any power EPC job. Majority of established EPC/BoP players like BGR Energy, Larsen & Toubro etc are facing dearth of orders, as the new order pipeline of the power sector has dried up and competition intensified. In such a scenario, we are not bullish about SIL's entry into the power EPC business. Following aggressive bidding at Rs37/MW, we expect SIL to report lower margin on this order. In addition, due to the group company's transaction, prospects of favourable working capital terms can't be ruled out, which might elongate SIL's working capital cycle.

**Valuation:** Factoring weak corporate governance and other factors, SIL has declined 20% in the past three days and 40% in the past three months. It is trading at the lower end of its valuation band at 4.1x/3.7x FY13E P/E and EV/EBITDA, below the seven-year median of 8.9x/6.6x. Following weak corporate governance we expect the stock's valuation to remain capped and downgrade it to Hold with a revised TP of Rs96 (from Rs167) valuing it at 3.9x EV/EBITDA (40% discount to its median of 6.6x).

Y/E Mar (Rsmn)	FY09	FY10	FY11	FY12E	FY13E
Revenue	30,639	32,816	44,752	52,778	64,977
YoY (%)	34.6	7.1	36.4	17.9	23.1
EBITDA	4,500	5,005	8,069	9,283	10,789
EBITDA (%)	14.7	15.3	18.0	17.6	16.6
Reported PAT	3,251	3,290	4,600	4,052	5,812
Adj PAT	3,095	3,215	4,492	4,648	5,812
FDEPS (Rs)	11.4	11.9	16.6	17.1	21.4
YoY (%)	40.7	3.9	39.7	3.5	25.0
RoE (%)	19.1	17.6	20.7	17.9	19.0
RoCE (%)	8.9	8.3	13.5	13.7	15.6
P/E (x)	7.7	7.4	5.3	5.1	4.1
EV/EBITDA (x)	7.4	7.7	4.7	4.3	3.7

Source: Company, Nirmal Bang Institutional Equities Research

## Hold

Sector: Diversified

CMP: Rs88

Target Price: Rs96

Upside: 9%

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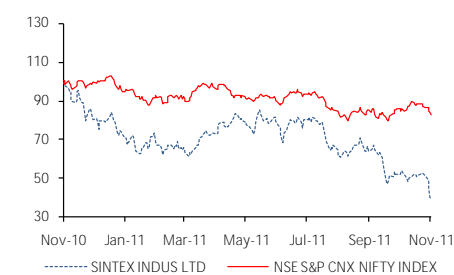
### Key Data

Current Shares O/S (mn)	273.0
Mkt Cap (Rsbn/US\$mn)	23.9/470.3
52 Wk H / L (Rs)	235/84
Daily Vol. (3M NSE Avg.)	2,284,779

### Share holding (%)

	4QFY11	1QFY12	2QFY12
Promoter	35.0	35.0	35.0
FII	33.7	38.2	38.6
DII	8.8	5.8	8.2
Corporate	11.4	10.3	9.8
General Public	11.2	10.8	8.5

### One Year Indexed Stock Performance



### Price Performance (%)

	1 M	6 M	1 Yr
Sintex	(26.5)	(50.0)	(60.6)
Nifty Index	(2.0)	(9.0)	(17.7)

Source: Bloomberg

**Change in estimate:** Based on the receipt of 2x150MW order from Shirpur Power, we are revising our estimates for FY13. As the order is to be executed over a period of 48 months, it will not have any impact on our FY12 estimates. We increase our net revenue guidance by 4.8% to Rs65bn for FY13. Following lower margin on the EPC order, we reduce our consolidated margin estimate by 61bps to 16.6% for FY13, following which we increase our operating profit estimate by 1.1%. Due to lower margin and higher working capital requirement, we expect net profit to increase by a mere 0.3% in FY13.

### Exhibit 1: Change in earnings estimates

Y/E March (Rsmn)	Earlier assumption		New assumption		Change (%)	
	FY12E	FY13E	FY12E	FY13E	FY12E	FY13E
Net sales	52,778	61,977	52,778	64,977	-	4.8
EBITDA	9,283	10,669	9,283	10,789	-	1.1
EBITDA	17.6	17.2	17.6	16.6	-	(61)
RPAT	4,052	5,797	4,052	5,812	-	0.3
APAT	4,648	5,797	4,648	5,812	-	0.3

Source: Bloomberg, Company, Nirmal Bang Institutional Equities Research

### Rating track

Date	Rating	CMP	Target Price (Rs)
15 July 2011	Buy	181	224
4 October 2011	Buy	112	179
11 October 2011	Buy	116	167
18 November 2011	Hold	88	96

Source: Nirmal Bang Institutional Equities Research

## Disclaimer

### Stock Ratings Absolute Returns

BUY > 15%

HOLD 0-15%

SELL < 0%

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