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APL Apollo Tubes

10 August, 2018

Volume guidance lowered, focus to improve EBITDA/tn

RESULT UPDATE

Sector: Steel Pipes Rating: Buy

CMP: Rs1,757 Target Price: Rs2,470

Stock Info

Sensex/Nifty	37,869 / 11,429
Bloomberg	APAT IN
Equity shares (mn)	23.7
52-wk High/Low	Rs2587/ 1444
Face value	Rs10
M-Cap	Rs41.7bn/ \$632mn
3-m Avg volume	\$1.0mn

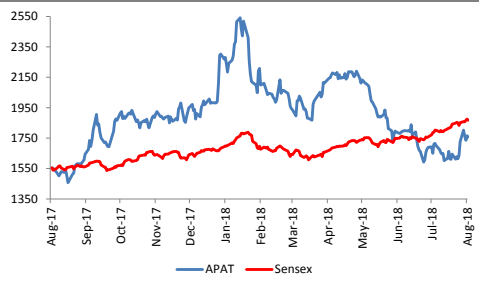
Financial Snapshot (Rs mn)

Y/E Mar	FY18	FY19e	FY20e
Net sales	53,348	67,954	82,661
EBITDA	3,710	4,468	5,330
PAT	1,600	2,024	2,554
EPS (Rs)	67.4	85.3	107.6
PE (x)	26.1	20.6	16.3
EV/EBITDA (x)	13.4	11.3	9.6
P/B (x)	5.0	4.2	3.5
RoE (%)	20.5	22.1	23.3
RoCE (%)	20.5	21.2	22.8
D/E (x)	1.0	0.9	0.8
OPM (%)	7.0	6.6	6.4

Shareholding pattern (%)

	Jun'18	Mar'18	Dec'17
Promoter	37.25	37.25	37.25
- Pledged	-	-	-
FII	0.02	0.02	-
DII	11.94	14.79	13.64
Others	50.79	47.92	49.11

Stock Performance (1-year)



APAT's volumes increased by 14/0.5% yoy/qq to 302,000tn, lower than the normal run-rate of ~20%, mainly due to (1) slower infra spend by the government, (2) lower GI pipe production (21/14% yoy/qq) and (3) increasing competition. Overall revenue grew by 45/10% yoy/qq to Rs16.7bn. EBITDA/tn improved by 21/5% yoy/qq to Rs3,583 and was mainly led by a higher inventory gain of ~250tn. EBITDA grew by 27/8% yoy/qq to Rs1.1bn, while EBITDA margin declined by 30bps yoy/qq to 6.5%. PAT grew by 21/6% yoy to Rs470mn. The management lowered the volume guidance from 20-22% to 15-18% led by slower execution of infra spend by the government. However the management aims to maintain EBITDA/tn of Rs3,300-3,500 over the next two to three years. It is expected to spend Rs0.8-1bn (in FY19) to set up a stripping mill and GI pipeline.

Management lowers volume guidance -- lower infra spend, completion and high base: Citing a slower infra spent by the government, increasing competition and a high base, the management lowered the volume guidance from 20-22% to 15-18% range. Since APAT is the role model for many ERW pipe manufacturers, its peers have followed its distribution model and plant locations (in regions) – like Surya Roshni and Hi-Tech pipes have set up plants in Hindupur (Southern region) with a capacity of 150,000tpa and 120,000tpa respectively. Meanwhile Rama Steel and Hi-Tech pipes are expanding their presence in the Western region. We believe APAT will be able to compete with peers with its brand, innovation ability, scale and distribution reach, though it is expecting a lower volume growth in this period. Thus we have lowered the volume estimates from 25% and 22% in FY19e and FY20e to 16% in the same years.

Focus to improve EBITDA/tn, with backward integration and increase in GI & GP pipes capacities: Post achieving scale, APAT's focus is to improve EBITDA/tn and the company is taking several measures to improve profitability – (1) stripping mill (capex: ~Rs500mn): this will be backward integrated to reduce HRC thickness, normal HRC from JSW and others come with 2.5mm and above thickness, while to produce ERW pipe of lower than 2.5mm thickness, the company is paying higher prices to get thinner-sized HRC. By setting up a stripping mill, APAT can save cost by purchasing normal HRC and further reducing the thickness in-house; the mill to commence operations in 4QFY19. (2) It is expanding GI and GP capacities from current ~350,000tpa to ~450,000tpa; these are high-margin pipes with less competitive intensity. We expect EBITDA/tn for FY19e and FY20e to be Rs3,421 and Rs3,523 respectively.

Key takeaways from conference call

- ~85% of the pipes are being sold through distributors, 6-7% through large customers (direct) and 6-7% via exports.
- The company is gaining traction in Eastern markets and in the first year it sold 3,000tn of products.
- It has 400 distributors, of which 50-60 are large, especially in metro cities.
- The management is targeting to improve the receivable cycle every year. It is entering channel financing schemes for its dealers.
- DFT technology opens up the US market, and the company plans to increase the export share from 5-6% currently.
- APAT has embarked on a brand building exercise with the digital campaign already underway. It plans to enter the mainstream media campaign this year. The spend on advertisements is earmarked at ~Rs250mn per annum.

Valuation and view

We estimate APAT's total revenue/PAT to post a CAGR of 24/26% respectively over FY18-20e, with healthy return ratios and positive FCF. We believe the stock deserves a premium valuation of 11x FY20e EV/EBITDA due to scale, brand and reach. We have revised the target price to Rs2,470 (earlier Rs2,734), by estimating lower volume growth of 16% for FY19e and FY20e and cut estimates by 9% and 6% in respective years. We have a **Buy** rating on the stock.

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Exhibit 1: Quarterly financial statement

Particulars (Rs mn)	1QFY19	1QFY18	y-o-y	4QFY18	q-o-q
Net sales	16,765	11,556	45.1%	15,194	10.3%
Other income	37	95	-60.8%	19	96.8%
Total Income	16,803	11,652	44.2%	15,213	10.4%
Expenditure:					
Cost of material	14,658	9,743	50.4%	13,291	10.3%
Employees expenses	261	212	23.3%	234	11.6%
Other expenses	760	814	-6.7%	643	18.3%
Total expenditure	15,679	10,769	45.6%	14,168	10.7%
EBITDA	1,124	882	27.4%	1,045	7.5%
EBITDA (Excl. OI)	1,087	787	38.1%	1,026	5.9%
Depreciation	152	122	24.6%	150	1.6%
EBIT	972	760	27.8%	896	8.5%
Finance Cost	263	177	48.7%	226	16.4%
EBT	709	583	21.5%	670	5.9%
Tax	239	195	22.5%	225	6.4%
Tax rate	34%	33%		34%	
PAT	470	388	21.0%	445	5.6%
PAT (adj)	470	388	21.0%	445	5.6%
EPS (Rs.)	20	16	20.5%	19	3.2%
EPS Diluted (Rs.)	19	16	20.9%	19	3.2%
EBITDA margin	6.5%	6.8%	-33 bps	6.8%	-27 bps
PAT margin	2.8%	3.4%	-56 bps	2.9%	-13 bps

Source: Company, Systematix Institutional Research

FINANCIALS

Profit & Loss Statement

YE: Mar (Rs mn)	FY16	FY17	FY18	FY19e	FY20e
Net revenues	42,136	45,450	53,348	67,954	82,661
Revenue growth (%)	34.3	7.9	17.4	27.4	21.6
- Op. expenses	39,573	42,206	49,637	63,486	77,331
EBITDA (Excl. OI)	2,563	3,244	3,710	4,468	5,330
EBITDA margins (%)	6.1	7.1	7.0	6.6	6.4
- Interest expenses	695	683	813	974	1,029
- Depreciation	341	512	534	610	654
+ Other income	103	38	80	136	165
- Tax	624	627	844	997	1,258
Effective tax rate (%)	38	30	35	33	33
Reported PAT	1,006	1,459	1,600	2,024	2,554
+/- Extraordinary items	-160	-6	-	-	-
+/- Minority interest	-	-	-	-	-
Adjusted PAT	1,165	1,465	1,600	2,024	2,554
EPS (Rs/share)	42.9	61.8	67.4	85.3	107.6

Source: Company, Systematix Institutional Research

Balance Sheet

YE: Mar (Rs mn)	FY16	FY17	FY18	FY19e	FY20e
Share capital	234	236	237	237	237
Reserves & Surplus	5,441	6,967	8,132	9,711	11,703
Networth	5,676	7,203	8,370	9,948	11,941
Minority interest	-	-	-	-	-
Total Debt	6,567	6,044	8,277	9,112	9,517
Def. tax liab. (net)	859	905	1,003	1,003	1,003
Capital employed	13,101	14,152	17,650	20,063	22,461
Net Fixed assets	6,982	8,570	9,209	8,939	9,086
Investments	131	127	120	120	120
Net Working capital	5,975	5,438	8,253	10,891	13,170
Cash and bank balance	14	17	68	113	85
Capital deployed	13,101	14,152	17,650	20,063	22,461
Net debt	6,553	6,028	8,209	8,999	9,432
WC (days)	46	27	45	46	46
Book value (Rs/sh)	242.1	305.3	352.7	419.2	503.2

Source: Company, Systematix Institutional Research

Cash Flow

YE: Mar (Rs mn)	FY16	FY17	FY18	FY19e	FY20e
PAT	1,165	1,465	1,600	2,024	2,554
+ Non cash items	455	558	632	610	654
Cash profit	1,621	2,023	2,232	2,634	3,208
- Incr/(Decr) in WC	2,177	-536	2,814	2,638	2,279
Operating cash flow	-556	2,559	-582	-5	929
- Capex	942	2,100	1,173	340	800
Free cash flow	-1,498	459	-1,755	-345	129
- Dividend	234	283	283	405	511
+ Equity raised	-	2	1	-	-
+ Debt raised	1,705	-522	2,233	835	405
- Investments	-59	-4	-7	-	-
- Misc. items	206	-345	152	40	51
Net cash flow	-175	3	51	45	-28
+ Opening cash	188	14	17	68	113
Closing cash	14	17	68	113	85

Source: Company, Systematix Institutional Research

Ratios

YE: Mar	FY16	FY17	FY18	FY19e	FY20e
P/E (x)	41.0	28.4	26.1	20.6	16.3
P/BV (x)	7.3	5.8	5.0	4.2	3.5
EV/EBITDA (x)	18.6	14.6	13.4	11.3	9.6
RoE (%)	18.9	22.7	20.5	22.1	23.3
RoCE (%)	19.7	20.3	20.5	21.2	22.8
Fixed Asset turnover (x)	5.5	5.2	5.0	5.9	6.7
Dividend (%)	100	120	119	171	215
Dividend yield (%)	0.6	0.7	0.7	1.0	1.2
Dividend payout (%)	23.3	19.4	17.7	20.0	20.0
Debtors days	19	24	30	30	30
Creditor days	28	37	28	28	28
Inventory days	55	41	43	43	43
Revenue growth (%)	34.3	7.9	17.4	27.4	21.6
PAT growth (%)	57.7	45.1	9.7	26.5	26.2
EBITDA growth (%)	41.1	26.6	14.4	20.4	19.3

Source: Company, Systematix Institutional Research

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