

# Welspun Corp (WLCO IN)

## 'Piping' up the volume

### INDIA | MID-CAPS | Management Meeting Update

13 April 2016

#### Leading global manufacturer of line pipes

WCL is a leading manufacturer of submerged arc welded (SAW) and electric resistance welded/high-frequency induction welded (ERW/HFIW) pipes with manufacturing facilities in India, the US, and Saudi Arabia. It has been supplying large-diameter line pipes to big players in the domestic and international oil & gas and water infrastructure industries, including to prestigious projects such as the pipeline project in the Gulf of Mexico in the USA (the world's deepest), a project in the Persian Gulf (heaviest), an LNG pipeline project in Peru (highest), and the pipeline project from Canada to the US (longest).

#### Reach and scale ensure global competitiveness

WCL's pipe mills are located in India and in the biggest global hydrocarbon markets (USA and the Middle East), all of which are port-based. In addition to 1.6mn MT of capacity in India, it also has 0.5mn MT and 0.3mn MT in the US and the Middle East. Thus, depending on the economics of order execution and project supplies, it has the option to export from India or to manufacture locally. This is reflected in its regional sales break-up, where the US and Saudi plants account for ~45% of volumes sold in FY15.

#### Supplies largely to hydrocarbons projects

86% of WCL's sales of 1.15mn MT in FY15 were to the hydrocarbons sector, despite easing prices of hydrocarbons, underlining this sector's focus on reducing its transportation costs. The specialised nature of supplies and stringent quality parameters in this sector translates into healthy profitability for WCL. Conversely, intense competition, commoditised nature of supplies, and lower profitability in the domestic water-infrastructure space saw WCL participate selectively in tenders. Consequently, its supplies to this sector accounted for 14% of revenues in FY15. It has largely maintained this sales mix in 9MFY16.

#### Operational discipline facilitates stable profitability and cash conversion

While tendering for an order, WCL enters into price and volume arrangements for the supply of the appropriate grade of steel. It mainly imports specialty grades of API steel (used in the hydrocarbons sector) – hence the forex angle. With exports forming a significant chunk of revenues, it hedges the differential amount (conversion profit) through simple forward covers. It has reasonably good credit terms (~3 months) and realises its dues within 30 days of supplies, effectively maintaining a net working capital cycle of 50-60 days.

#### Stable financials and order book

With an average EBIDTA/MT of Rs ~9,000 and sales of 1.1mn MT, WCL earned an EBIDTA of Rs 9.5bn in FY15. Its debt and networth stood at Rs 28bn and Rs 27bn respectively, implying a debt/equity ratio and debt/EBIDTA ratio of 1x and 2.9x respectively. In 9MFY16, its performance metrics have improved, with EBIDTA at Rs 7.9bn (vs. Rs 5.4bn in 9MFY15), sales of 0.84mn MT (vs. 0.83mn MT) and debt of ~Rs 26bn, thus implying debt/EBIDTA ratio of 2.7x (annualised for FY16). It ended 3QFY16 with an order book of 1.14mn MT (vs. 1.03mn MT in 3QFY16) and is fairly confident of matching its sales volumes of FY15.

**Outlook and valuation:** Stable operations and cash flows coupled with an absence of significant capex could see WCL utilising operating cash flows to de-leverage its balance sheet. At the CMP of Rs 101, it trades at FY15 PE and EV/EBIDTA of 38x and 5.3x.

#### Not Rated

CMP RS 101

#### COMPANY DATA

O/S SHARES (MN) :	263
MARKET CAP (RSBN) :	27
MARKET CAP (USDBN) :	0.4
52 - WK HI/LO (RS) :	153/54
LIQUIDITY 3M (USDMN) :	0.75
PAR VALUE (RS) :	5

#### SHARE HOLDING PATTERN, %

	Dec 15	Sep 15	Jun 15
PROMOTERS :	45.1	40.9	40.6
FII / NRI :	5.9	4.0	5.5
FI / MF :	9.1	9.9	8.4
NON PRO :			
PUBLIC & OTHERS :	39.9	45.4	45.5

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**Other key takeaways**

- Globally, the US and Middle East remain the largest hydrocarbon markets. Even South East Asia is shaping up well for WCL. However, other large energy markets such as Brazil, Russia, and Europe remain inaccessible to exporters due to strong incumbent players (Tenaris, TMK, and Euro Pipe) and protectionist policies.
- With global hydrocarbon prices still soft, viable projects are focussing on lowering costs of evacuation, thereby generating demand for line pipes. At present, the company estimates an addressable market of 12mn MT over the next 24 months.
- Globally, project execution is slightly slow with execution delays of 3-6 months. However, the management does not anticipate any orders being scrapped because most are in advanced stages of completion.
- WCL has bid for projects totalling 3.5mn MT for the next few quarters. While the management didn't disclose its order win ratio, it was hopeful of maintaining its current rate in the near term (~1-1.1mn MT p.a.).
- While it did not state specifics, the management believes that the water infrastructure segment in India holds promise and that demand should materialise over a few quarters.
- The management indicated that its maintenance capex in FY17 would be ~Rs 1bn and that there were no brownfield/greenfield expansions on the anvil.

## Financials

### Income Statement

Y/E Mar, Rs mn	2012	2013	2014	2015
Revenues	89,766	108,701	77,047	84,505
Expenses	81,195	102,752	70,350	76,083
<b>Operating Profit</b>	<b>8,571</b>	<b>5,949</b>	<b>6,697</b>	<b>8,422</b>
Other income	2,676	3,110	1,742	1,086
<b>EBIDT</b>	<b>11,246</b>	<b>9,059</b>	<b>8,439</b>	<b>9,508</b>
Depreciation	3,515	3,531	4,063	4,365
Interest expense	3,999	4,931	2,964	2,830
Exceptional Expenses	-	(1,091)	-	-
<b>Profit before tax</b>	<b>3,732</b>	<b>(494)</b>	<b>1,412</b>	<b>2,313</b>
Taxes incl deferred taxation	1,503	390	432	177
<b>Profit after tax</b>	<b>2,229</b>	<b>(884)</b>	<b>981</b>	<b>2,135</b>
Min. Int & Sh. of Profit from Assoc	156	181	(247)	(1,445)
<b>Net Profit</b>	<b>2,385</b>	<b>(703)</b>	<b>734</b>	<b>690</b>
<b>Diluted EPS (INR)</b>	<b>2.1</b>	<b>(0.5)</b>	<b>0.6</b>	<b>0.5</b>

### Balance Sheet

Y/E Mar, Rs mn	2012	2013	2014	2015
Share Capital	1,139	1,315	1,315	1,316
Reserves & Surplus	39,794	55,263	27,178	26,672
<b>Networth</b>	<b>40,933</b>	<b>56,578</b>	<b>28,492</b>	<b>27,988</b>
Minority Interest	3,433	3,546	2,088	3,563
Debt	55,371	51,574	33,026	28,044
Deferred Tax Liability	4,970	5,512	5,609	5,697
<b>Capital Employed</b>	<b>104,707</b>	<b>117,209</b>	<b>69,216</b>	<b>65,291</b>
Gross Fixed Assets	80,685	98,443	68,494	70,707
Accumulated Depreciation	13,443	18,230	19,263	24,088
<b>Net Assets</b>	<b>67,242</b>	<b>80,214</b>	<b>49,231</b>	<b>46,619</b>
Capital work in progress	6,271	5,464	1,146	801
Investments	19,785	18,671	11,398	8,049
<b>Current Assets, Loans &amp; Advances</b>				
Inventory	25,632	25,669	12,815	22,082
Debtors	15,260	17,614	6,374	11,301
Cash & Bank balance	10,255	6,989	1,408	3,327
Loans & advances and others	13,531	14,204	5,929	5,977
<b>Current Liabilities &amp; Provisions</b>				
Creditors	32,923	30,380	6,510	24,634
Other liabilities & provisions	20,347	21,236	12,576	8,230
Misc Expenses not written off	0	0	0	0
<b>Net Current Assets</b>	<b>11,409</b>	<b>12,860</b>	<b>7,441</b>	<b>9,823</b>
<b>Application of Funds</b>	<b>104,707</b>	<b>117,209</b>	<b>69,216</b>	<b>65,291</b>

### Cash Flow

Y/E Mar, Rs mn	2012	2013	2014	2015
<b>PBT</b>	<b>3,732</b>	<b>(494)</b>	<b>1,412</b>	<b>2,313</b>
Depreciation & amortisation	3,515	4,867	4,075	4,365
Interest expense	1,733	1,905	1,044	1,397
Interest / Dividend Recd	(445)	(277)	(13)	(36)
Other Adjustments	279	(1,679)	56	(593)
(Inc)/Dec in working capital	6,925	(3,123)	(3,876)	1,810
Tax paid	(1,453)	(173)	(429)	(245)
<b>CF from operating activities</b>	<b>14,286</b>	<b>1,025</b>	<b>2,270</b>	<b>9,011</b>
Capital expenditure	(4,897)	(6,578)	(1,574)	(894)
(Purchase) / Sale of Investments	(18,021)	2,341	(1,087)	3,249
Income from investments	864	2,565	1,439	1,023
<b>CF from investing activities</b>	<b>(22,054)</b>	<b>(1,672)</b>	<b>(1,222)</b>	<b>3,377</b>
Inc/(Dec) in share capital	5,079	10	1,076	-
Inc/(Dec) in debt	6,585	1,320	(3,353)	(8,507)
Dividends & Interest paid	(3,031)	(3,978)	(2,986)	(2,552)
Other Financial Activities	1,000	-	(3)	-
<b>CF from financing activities</b>	<b>9,634</b>	<b>(2,648)</b>	<b>(5,265)</b>	<b>(11,058)</b>

### Valuation Ratios

	2012	2013	2014	2015
<b>Growth Indicators (%)</b>				
Revenue	11.9	21.1	(29.1)	9.7
EBITDA	(31.9)	(30.6)	12.6	25.8
PAT	(62.3)	(129.5)	(204.4)	(5.9)
EPS	(66.1)	(125.5)	(204.4)	(6.0)
<b>Valuation (x)</b>				
PE	10.9	(37.0)	35.5	37.7
P/BV	0.6	0.5	0.9	0.9
EV/EBITDA	6.3	7.8	6.8	5.3
EV/Sales	0.8	0.6	0.7	0.6
Dividend Yield (%)	0.0	0.0	0.0	0.0
<b>Financial Ratios</b>				
RoE (%)	5.8	(1.2)	2.6	2.5
RoCE (%)	7.4	2.7	8.0	10.4
Debt/Equity (x)	1.4	0.9	1.2	1.0
EBIT/Interest (x)	1.9	1.1	1.5	1.8

Source: Company, PhillipCapital India Research Estimates

## Rating Methodology

We rate stock on absolute return basis. Our target price for the stocks has an investment horizon of one year.

Rating	Criteria	Definition
BUY	>= +15%	Target price is equal to or more than 15% of current market price
NEUTRAL	-15% > to < +15%	Target price is less than +15% but more than -15%
SELL	<= -15%	Target price is less than or equal to -15%.

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