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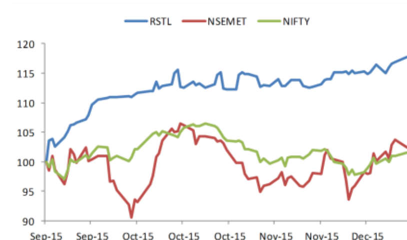
Rama Steel Tubes Limited

29 December 2015

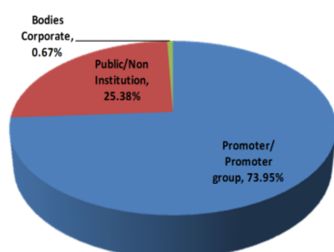
Capacity expansion coupled with rise in demand to drive growth — Strong Buy

Sector	: Steel Tubes/Pipes
Target Price	: Rs 1346
Current Market Price	: Rs 925
Market Cap	: Rs 1379.9 mn
52-week High/Low	: Rs 950/750
Daily Avg. Volume	: 7,226
Shares in issue	: 1.5 mn
Face Value	: Rs 10
Beta	: 0.53
Pledged Shares	: 0%
Year End	: 31st March
BSE Scrip Code	: 539309
NSE Scrip Code	: RAMASTEEL
Bloomberg Code	: RASTL IN
Reuters Code	: RAMA.NS
Nifty	: 7,925
Sensex	: 26,034
Analyst	: Raj Kumar Jha & Ronak Jhaveri

Price Performance



Shareholding Pattern



Investment Summary

Aggressive Capacity Expansion to drive growth

Rama Steel Tubes Limited (RST) has an aggressive expansion plan to raise its capacity to 340,000 metric tonnes per annum (MTPA) over FY19-20E from around 99,000 MTPA currently. The expansion is targeted in the value-added segment, commanding higher margins.

Strategically-located plant helps trim logistics cost

The industry faces a problem of high logistics cost which the company is trying to fix by full-fledged production at its Khapoli (Maharashtra) plant. This strategically-located plant (near the port) will gradually cater to rising demand from the export market. It now caters to demand from Maharashtra and Gujarat. Assuming that it cuts transportation and logistics cost by being located closer to the port, the expense component could come down by nearly 20% (of selling and distribution expenses).

Expansion in margins likely from 1Q FY17

With commencement of production of an additional 72,000 MTPA (from two new plants) along with higher capacity utilisation rates, we believe that margin expansion will be seen from 1Q FY17. Production from the first plant commenced in June 2015 and the management expects the second plant to start by April 2016. This will not only raise the revenue but will also improve the overall margin.

Leveraging through operations in overseas markets

In April 2015, RST set up M/s RST International Trading FZE, a wholly-owned subsidiary in Dubai to open avenues for more international business in steel products. With negligible costs of running the trading business, the company wishes to leverage its goodwill of having been in the business for more than four decades. The management anticipates that its Dubai foothold will serve as a stepping stone to other markets in European and African nations. We expect that in FY16 revenue from the subsidiary would cross Rs 600-650 mn with a PAT margin of 5-6%, with handsome ROI.

Industry in a consolidation phase

At present, the Indian steel tube and pipe sector is highly fragmented, with more than 50% held by the informal segment. It is expected that the Indian steel tube industry will go through a consolidation phase, helping regulated operators to take part of the pie from the informal segment.

Valuation

We initiate a Strong Buy report on RST at CMP of Rs 925 with a target price of Rs 1,346, a ~46% upside. Our target price is based on a sum-of-parts valuation methodology (50% weight) and DCF valuation methodology (50% weight). Valuation of RST's core business is Rs 1050/share and valuation of the Dubai subsidiary is Rs 321/share after offering a discount of 20% on derived valuation. We reach a sum-of-parts valuation of Rs 1,371 and our DCF valuation is Rs 1,322 based on WACC of 11.7% and perpetual growth rate of 4%. At the CMP of Rs 925, we recommend a "**Strong Buy**" with a target price of Rs 1,346/share, a ~ 46% upside.

Exhibit 1: Key financials

INR mn	FY13	FY14	FY15	FY16E	FY17E	FY18E
Net Revenue	1,852	1,813	1,924	2,106	3,146	4,194
Y-o-Y Growth	20.5%	-2.1%	6.1%	9.4%	49.4%	33.3%
EBITDA	32.3	51.7	57.6	99.7	133.0	166.6
EBITDA Margin	1.8%	2.9%	3.1%	4.9%	4.4%	4.1%
Adjusted PAT	11.1	17.1	4.8	26.7	58.8	80.2
Adj PAT Margin	0.6%	1.0%	0.3%	1.3%	1.9%	2.0%
Adj. EPS (Rs)	44.5	68.6	3.2	17.9	39.4	53.7
P/E (x)	21	13	287	52	23	17

Source: Khambatta research, Company data

Company Profile

Incorporated in 1974, Rama Steel Tubes Limited transforms basic steel to tubes, galvanized products, structures, etc. These are value-added products for infrastructure projects and the new emerging sectors such as automobiles and oil pipe-lines. With experience of more than four decades in the steel component sector, RST has diversified business segments catering to domestic and export markets. It is a steel processor not a steel manufacturer.

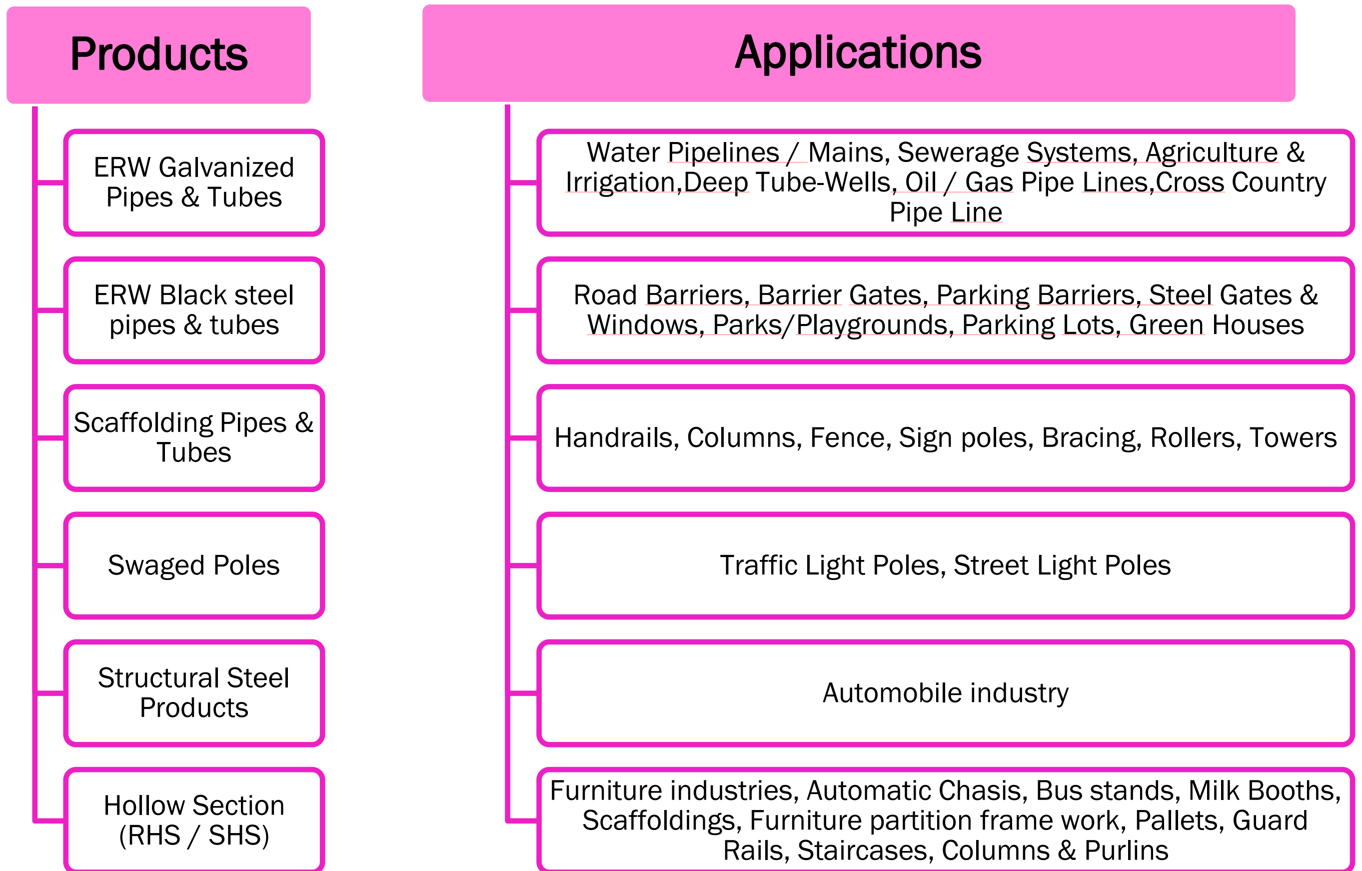
It has three manufacturing plants: two at Sahibabad (Uttar Pradesh) with capacities of 75,000 MTPA and 24,000 MTPA, and one at Khopoli (Maharashtra) with capacity of 36,000 MTPA. For the Khopoli plant, the company is planning to ramp up capacity to 240,000 MTPA, taking its overall installed capacity to around 340,000 MTPA. It has operations in the United Kingdom, the UAE, Sri Lanka, Ethiopia, Kenya, Uganda, Ghana, Kuwait, etc. By recognizing the contribution of the company to exports, the Government of India has cleared it as an export house. It was formerly listed on the Delhi Stock Exchange and has recently been listed on the NSE and the BSE.

With experience of more than four decades in the steel component sector, RST has diversified business segments catering to domestic and export markets

Exhibit 2: Customer Base

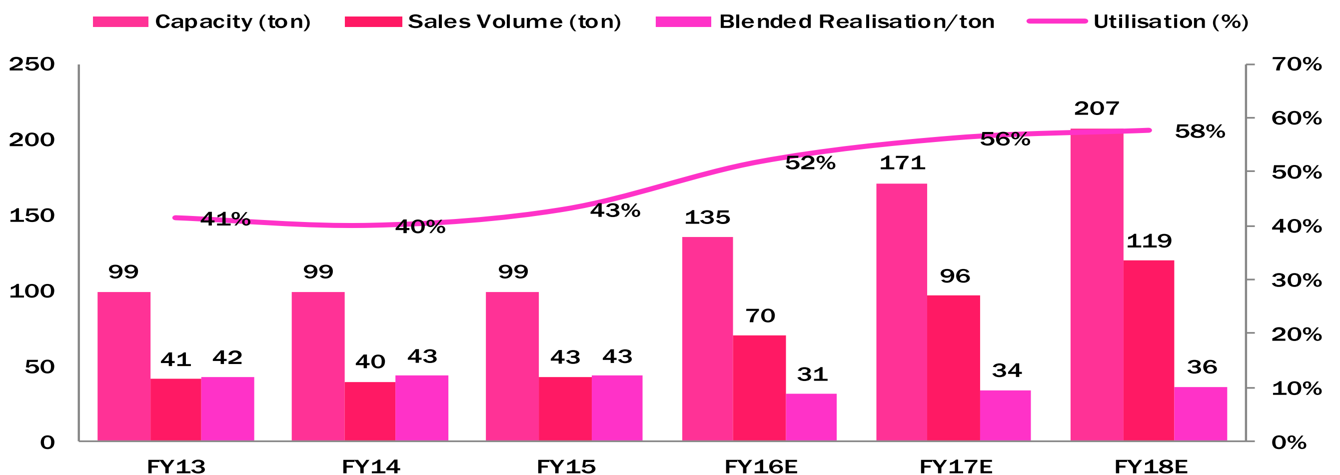
Source: Company data

Exhibit 3: Diversified product line



Source: Khambatta research, Company data

Exhibit 4: Capacity Utilisation-Trend



Source: Khambatta research, Company data

The Steel Sector

Introduction

India is the world's third-largest producer of crude steel after China and Japan. The growth in the Indian steel sector has been driven by the domestically available raw material iron ore and by cost-effective labour. India's steel production capacity expanded from about 75 million tonnes per annum (MTPA) in FY10 to about 90.5 MT in FY15.

India's production capacity is projected to increase to about 300 MT by 2025

India's production capacity is projected to increase to about 300 MT by 2025. However, per-capita steel consumption is quite low, 60 kg, against the world average of 216 kg. This low consumption indicates the huge growth potential for the Indian steel industry. We believe that it is already in expansion mode. In line with the strong economic outlook and plans to expand steel production, it is likely that India will be on a fast-track growth path in steel production to lead to it being the second-largest steel producer within a few years.

In FY15, the consumption of finished steel rose to 76.36 MT. Rising domestic demand by sectors such as infrastructure, real estate and automobiles has put the Indian steel industry on the world map. The country's steel consumption is expected to reach 104 MT by 2017. Growth in the private sector is expected to be boosted by the new policies on Make in India, import of foreign technology and foreign direct investment.

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After the slowdown of the last few years, demand for steel in India is showing signs of rebounding. The World Steel Association (WSA) expects that India's use will rise 7.6% to 87.6 MT in CY16. According to the WSA, India's outlook has been improving after the election of the new government, which has been promising pro-business reforms. However, the high degree of inflation and fiscal consolidation are key downside risks to the outlook.

We believe that the worst in the Indian steel sector appears to be over. Being a cyclical industry, there might be gradual improvement but recent developments such as an increase in automobile sales, lower interest rates and greater industrial production seem encouraging.

The Steel Pipe Market

The global export market of steel pipes is stated to be nearly US $27 bn a year, with the US, Western Europe, Australia and Japan being the largest importers. India is one of the major exporting nations besides Indonesia, Malaysia and Thailand.

The Indian steel-pipe sector consists of firms primarily manufacturing seamless or welded steel pipes or tubes or ferrous pipe or tube fittings. In the recent past, steel-pipe manufacturers have added significant capacities perceiving strong domestic and export demand. We believe that, with the increase in demand, utilisation rates for ERW pipe-makers will improve. Further, growing oil and gas demand across the world and with new pipeline infrastructure in process, revenue of Indian steel pipe-makers should be on the higher side.

The rise in demand for housing and commercial spaces in urban regions has led to huge demand in the hollow section and ERW pipes. The rising number of malls and high-rises has led to increased demand for structural/hollow steel products as they are stronger and have a better aesthetic.

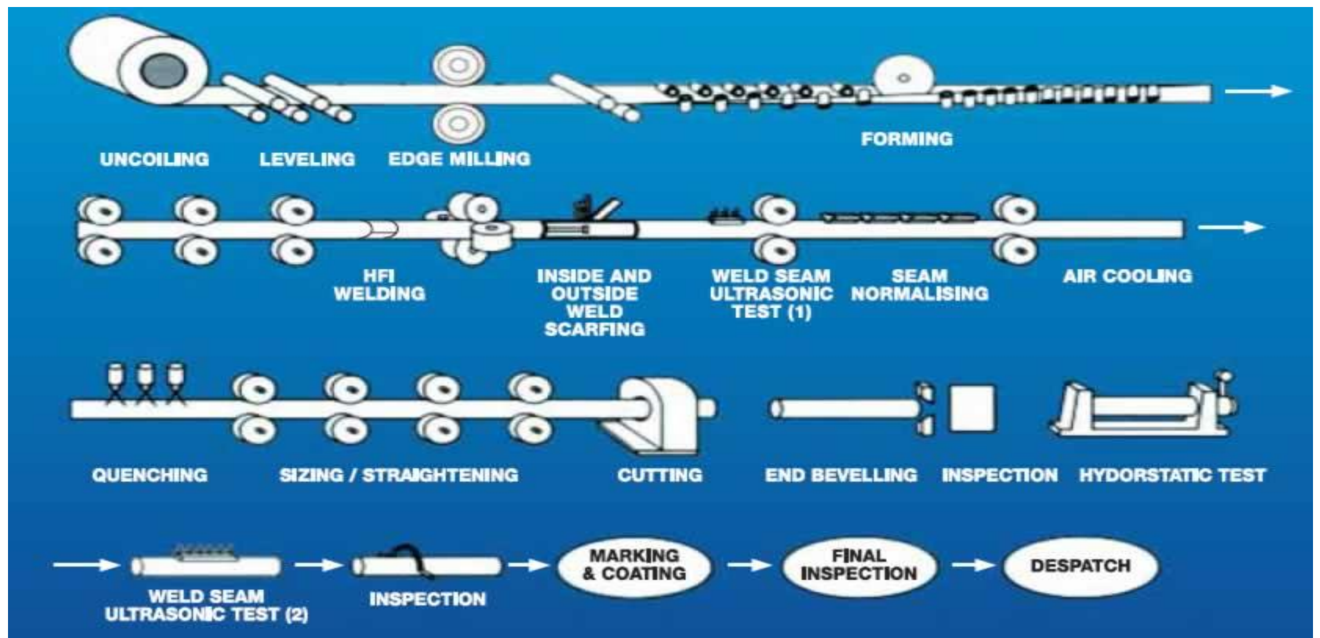
Electrical-Resistance Welded (ERW) Steel Pipes and Tubes

ERW steel pipes and tubes are widely used across industries. They are used for water, oil and gas distribution, line pipes, fencing, scaffolding, etc. Further uses are drinking water supply, thermal power for hand pumps for deep-bored wells and as protection for cables (telecoms). Depending on the requirement of the end-user industry, ERW steel pipes and tubes are available in various wall thicknesses, diameters and qualities. The different types are line precision pipes, tubular poles, electric poles, lightweight galvanised pipes for sprinkler irrigation, among others.

The comprehensive global report "Electric-Resistance Welded Pipes and Tubes: A Global Strategic Business Report," released by Global Industry Analysts, Inc., projects that the global market for ERW pipes and tubes will reach 76.8 MT by 2020, driven by the recovery in key end-user markets and the need to replace aging pipelines installed at major oil and gas project sites.

Although economic uncertainty and low oil prices have led oil companies to curtail operations and cut back on drilling budgets, the demand outlook for ERW pipes continues to be positive, given the steady rise in oil consumption and the need for infrastructure to support sustained production and transportation of oil.

Exhibit 5: Manufacturing Process



Source: Company

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Investment Rationale

Installed Capacity to reach 0.34 MTPA

Industry reports indicate that the market for steel tubes & pipe is likely to double in the next four years.

The shift in the steel pipe segment from seamless to ERW pipes (due to cost benefits) is one of the key reasons for the company's revenue. Rising demand from emerging segments such as airports, malls, metros, solar power and irrigation has opened up opportunities for domestic ERW steel-pipe manufacturers. Industry reports indicate that the market is likely to double in the next four years. The Indian pipe segment is among the top three manufacturing hubs after Japan and Europe. However, the penetration level of pipelines in oil & gas transportation is quite low in India, indicating a huge business opportunity. The company, sensing the opportunity, has responded in equal measures through capacity expansion and wider reach. It is focused on expansion plans. It intends to more than triple its manufacturing capacity to 340,000 TPA by 2019-20.

Strategically-located plant helps trim logistics costs

RST recently added one more plant at Khopoli, Raigad, Maharashtra, which commenced commercial production in June 2015. The first plant has installed capacity of 36,000 TPA. Further, the company has 20 acres at Khopoli, sufficient to manufacture around 30,000 MT of pipes/tubes a month. In the next two years, it plans to enhance capacity at Khapoli to 240,000 TPA through the use of internal accruals.

The value-added products and cost-optimization efforts at the Khapoli plant would help improve the overall margin

The Khapoli plant benefits from its location. Aiming to eventually route most exports through this plant due to its proximity to the Jawaharlal Nehru Port, RST is currently catering to rising demand from Maharashtra and Gujarat. Assuming that it cuts transportation and logistics cost by being located closer to the port, the expense component could come down by nearly 20% (of selling and distribution expenses).

The new capacity is likely to come into production in FY 17.

Expansion in margins likely from Q1 FY17

The market size of India's ERW pipe segment is around Rs.300 bn or 7 MT. Along with the implementation of additional capacity, RST plans to shift towards higher-margin businesses. The value-added products and cost-optimization efforts at the Khapoli plant would help improve the overall margin. The management expects that per-tonne realisation would be highest at the Khapoli plant.

Leveraging through overseas operations

In April 2015, the company set up M/s RST International Trading FZE, a wholly-owned subsidiary in Dubai to open avenues for more international business in steel products. Rama Steel already has active operations in the UAE, Sudan, Ethiopia and Ghana. It anticipates that its Dubai foothold will serve as a stepping stone to other markets in European and African nations. We expect that in FY16 revenue from the subsidiary would cross Rs 600-650 mn with a PAT margin of 5-6%.

Cleaning up the balance sheet

In FY15, long-term debt was Rs 168.5 mn. RST has immovable property at Jaypee Green, Noida. It wishes to dispose of it in the next two or three quarters. Acccording to discussion with the management, the property is expected to fetch Rs. 90 to 100 mn. This will help reduce overall debt.

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Joint venture with 25% share in profit

The company, with three other companies, has entered into a joint venture called M/s Pir Panchal Constructions Pvt Ltd. The State Power Development Corporation (in Jammu) has awarded a contract for electrification of un-electrified/ de-electrified/ partially-electrified villages of the Poonch district on a turn-key basis to this joint venture. The management expects additional profit of Rs 200 mn in the next three years through the joint venture. RST, with a 25% stake, will have Rs 50 mn additional profit, not taxable. Projects of Rs 1.5 bn have already been completed and three tenders of Rs 1 bn have been bid for; management expects around 50% of the bids to be in its favour. This would further improve the bottom line. However, due to much litigation in these contracts, payments are delayed, which is one of the worrisome factors.

From the JV, the management expects additional profit of Rs 200 mn in the next three years

Rental income

RST has land in Gurgaon (around 1,000 sq.mtr., 20,000 sq. ft. built up). It earns rental income of Rs. 16-18 mn a year. The contracts are renewed yearly. Though the rental income is not the key business, the yield on it seems decent, bringing sort of fixed returns on the balance sheet.

Capex cycle to bear fruit in the near future

RST has 20 acres at Khapoli (Maharashtra). The first plant has been already set up and production in FY16 is expected to be 18,000 - 20,000 tonnes (total capacity: 36,000 MTPA). As per the management discussion, production at the second plant would commence by April 2016. Hence, two plants with capacity of 36,000 MTPA each should be fully operational by FY17. We believe that the capex of previous years will now bear fruit. With the rise in land prices, specifically in Maharashtra, acquiring new land for a plant would be a costly affair. The existing units, along with additional capacity would drive growth and bear fruit.

2Q FY16 Financial Overview

We believe sales volume will grow following the additional capacity, and we expect realisations to improve as demand from the construction sector is seeing a marginal improvement

RST reported strong figures in 2Q FY16, aided by robust volume growth. During the quarter, it reported 21% y-o-y growth in sales volumes, offset by lower realisations, resulting in subdued growth in net revenue to Rs 538 mn, against Rs 528 mn in 2Q FY15 and 497 mn in 1Q FY16. During the quarter, sales volumes grew 21% y-o-y to 13.5k tonnes, while net realisation-per-ton declined 22% y-o-y to Rs 35,315. During the quarter, RST's EBITDA grew 65.7% y-o-y and 67.1% q-o-q to Rs 34.2 mn, resulting in a 253-bp y-o-y and a 226-bp q-o-q improvement in the margin. During the quarter, EBIT grew 59.9% y-o-y and 68.9% q-o-q to Rs 25.9 mn, translating to a 181-bp y-o-y and a 175-bp q-o-q margin expansion to 4.88%. During the quarter, RST's net profit grew 64.3% y-o-y and 174.6% q-o-q to Rs 10.7 mn; consequently EPS improved to Rs 7.2 against Rs 4.4 in 2Q FY15 and Rs 2.6 in 1Q FY16. We believe scalability will improve the performance.

Exhibit 6: Capacity Utilisation-Trend

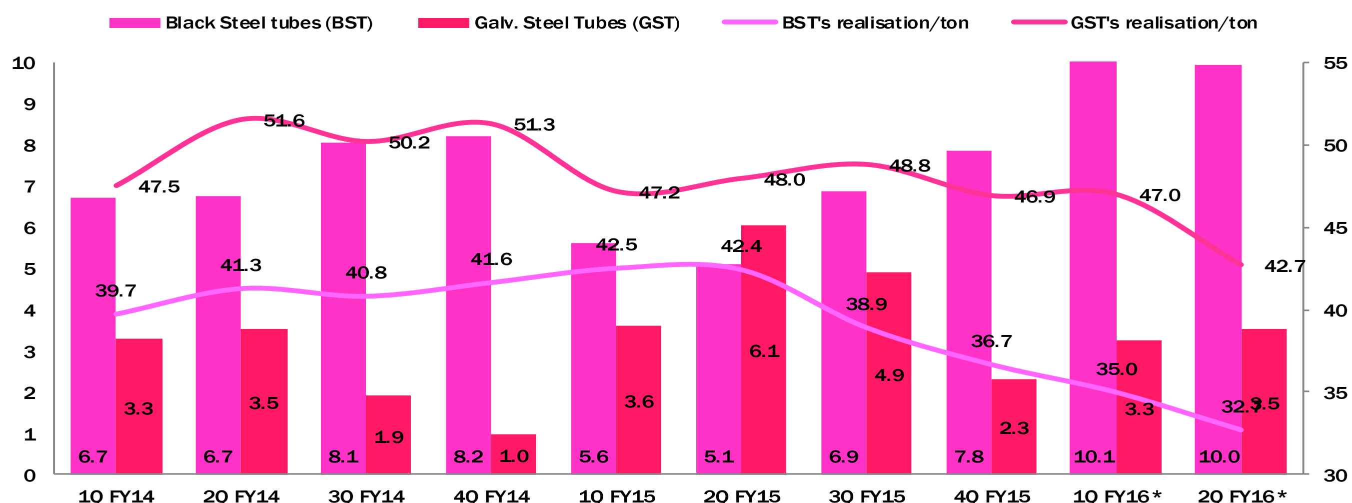
INR Mn	2Q FY15	1Q FY16	2Q FY16	Q-o-Q Change	Y-o-Y Change
Net Revenue	527.9	497.4	537.6	8.1%	1.8%
EBITDA	20.7	20.5	34.2	67.1%	65.7%
EBITDA margin	3.92%	4%	6.45%	226bps	253bps
EBIT	16.2	15.3	25.9	68.9%	59.9%
EBIT margin	3.07%	3%	4.88%	175bps	181bps
Adj. PAT	6.5	3.9	10.7	174.6%	64.3%
PAT margin	1.24%	1%	2.02%	122bps	78bps
Adj. EPS (Rs)	4.4	2.6	7.2	174.6%	64.3%

Source: Khambatta research, Company data

Strong volumes lead to revenue growth

RST saw a significant jump in sales volumes, especially in black steel tubes in the last two quarters, aided by Khopoli's volume. We believe sales volume will grow following the additional capacity, and we expect realisations to improve as demand from the construction sector is seeing a marginal improvement backed by the strengthening economy. We expect that the 36,000 tonnes of additional capacity in 1Q FY17 and 36,000 tonnes in 1Q FY18 at Khopoli will enhance volumes.

Exhibit 7: Quarterly Volume and Realisation



*Source: Khambatta research, Company data, *Khapoli plant's volume is added*

Volumes will be a game changer from FY16

RST Khopoli plants will be the game changer following the capacity expansion. The company is planning to expand capacity to 240,000 tonnes in the next few years, from 36,000 tonnes. RST will be adding 36,000 tons every year at Khopoli in the value-added segment. We expect capacity will grow from 99,000 tonnes to 207,000 tonnes by FY18; utilisation is expected to improve from 43% to 58% following higher utilisation at the Khopoli plants. We believe realisations have

bottomed out and expect marginal improvement ahead. From FY13 to FY15, realisations were almost flat at Rs. 43,000/tonne. This plummeted to Rs. 28,500/ton in 1H FY16. however, it is likely to improve in 2H FY16. We expect a marginal improvement in realisation.

Valuation

We expect realisation for the full year to fall by 29.2% to Rs 31,286 a ton, and climb to Rs 33,837 in FY17 and Rs 36,158 in FY18

We expect net revenue and EBITDA over FY15-18 to grow by 30% and 42% respectively, and adj. PAT by 155% following the addition of value-added products at Khopoli and the capacity expansion. In the same period, we expect capacity to grow by 72,000 tonnes to 207,000 tonnes (99,000 tonnes at Sahidabad and 108,000 tonnes at Khopoli). We assume that sale volumes would grow 37% following higher utilisation at the Khopoli plants while realisations would be under pressure. In FY15, the blended realisation was Rs 44,187 a ton, declining to about Rs 28,500 in 1H FY16. We expect that realisations would fall 29.2% for the full year to Rs 31,286 a ton, climbing to Rs 33,837 in FY17 and Rs 36,158 in FY18.

RST has a wholly-owned subsidiary, “M/s RST International Trading FZE”, which trades in steel, pipes and tubes. In FY16, revenue is expected at about Rs 600-650 mn, with an expected PAT margin of 5%. The very experienced team, which has over two decades of experience in handling the overseas business of steel, tubes and pipes manages this business. We have assumed Rs 3.99 mn in PAT in FY18 with 10% growth over the period and valued at 15x FY18E EPS. The valuation of “M/s RST International Trading FZE” is Rs 599 mn; after a 20% holding discount, we arrive at a valuation of Rs 321 per share.

Based on the sum-of-parts and DCF valuation methods, we arrive at a target price of Rs 1,346

We have initiated coverage of RST at the CMP of Rs 925 a share, with a target price of Rs 1,346 a share, a 46% upside. Our target price is based on the sum-of-parts valuation methodology and the DCF valuation methodology. Having assigned a 50% weight for the sum-of-parts valuation and a 50% weight for the DCF valuation, we reach a target price of 1,346 a share. The valuation of RST’s core business is Rs 1,050 a share and that of M/s RST International Trading FZE Rs 321 a share after a 20% holding discount. Our sum-of-parts valuation is Rs 1,371 and our DCF valuation is Rs 1,322, based on a WACC of 11.71% and a perpetual growth rate of 4%. At the CMP of Rs 925, we recommend a **“Strong Buy”,** with a target price of Rs 1,346 a share, a ~ 46% upside.

Exhibit 8: Sum-of-parts valuation

Particlular	Methodology	Value (INR: Mn)	Value Per Share
Valuation of RSTL	EV/EBITDA of 12x FY18E	1999	1338
Total Debt	-	632	423
Cash & Cash Equivalent	-	202	135
Stanalone Valuation of RSTL	-	-	1050
Valuation of M/s RST International Trad	P/E of 15 FY18E	599	401
Discount	20%	120	80
Valuation of M/s RST International Trad	-	-	321
Fair Value of RSTL	-	-	1371
CMP	-	-	925
Upside/Downside	-	-	48%

Source: Khambatta research, Company data

Exhibit 9: Key DCF Assumptions

Risk free rate	7.5%
Market return	13.0%
Risk premium	5.5%
Beta	1.00
Cost of equity	13.00%
Post-tax cost of debt	8.9%
Weight of equity	68.6%
Weight of debt	31.4%
WACC	11.71%
Perpetual Growth Rate	4.0%

Source: Khambatta research, Company data

Exhibit 10: DCF Calculation

DCF Elements	Value in : mn
PV of Forcast Period up to 2030E	1,755
PV of Terminal Value	650
Enterprise Value	2,405
Net Debt	430
Implied Equity Value	1,975
O/S Shares	1.5
Price/Share (Rs)	1,322

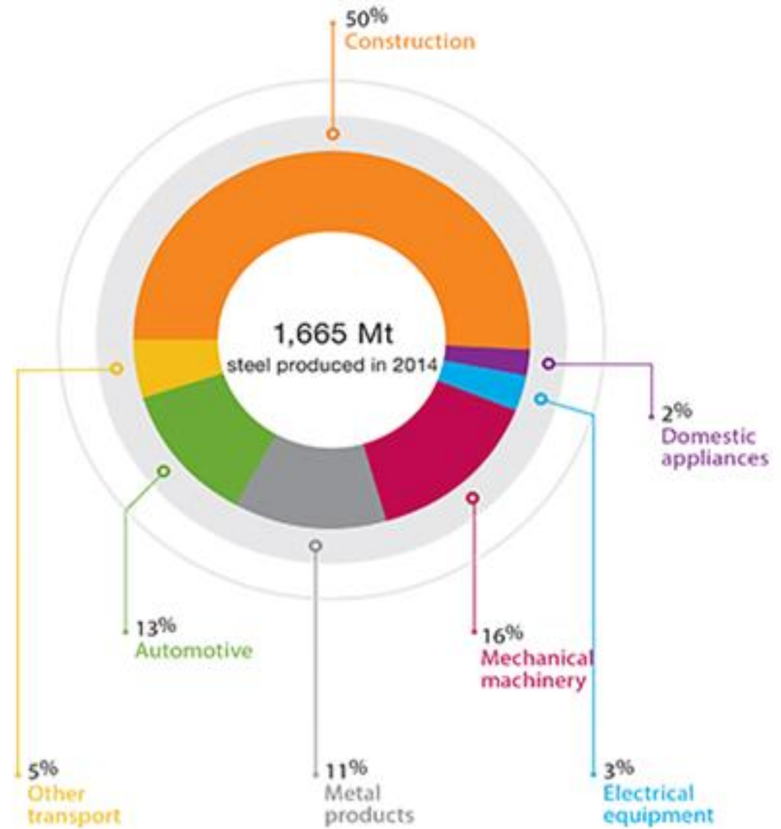
Source: Khambatta research, Company data

Exhibit 11: Weights of SOTP and DCF

Methodologies	Weights	Price	Target Price
SOTP Valuation	50%	1,371	686
DCF Valuation Using FCFF	50%	1,322	661
Target Price	-	-	1,346
Current Price	-	-	925
Upside	-	-	46%

Source: Khambatta research, Company data

Exhibit 12: Sector-wise Steel Consumption



Source: Worldsteel.org

Global construction Industry

The world global construction market is US $7.2 tn; China, the USA and Japan have 15%, 14% and 9% market shares, respectively. India is in the 4th position, with a 5% market share. According to one study, global construction will grow 5.5% while China and India will grow 8.84%, the US will grow 6%, Japan's and France's growth rate will decline to 1.1% and 2.3% respectively, and the rest of the world will grow 4.2%. At present, the Indian construction market is US $360 bn, expected at US $840 bn by 2020, with a growth rate of 8.84%. This creates huge headroom for steel tubes and pipe demand in India and across the globe.

Key Focus on 12th Five-year Plan

Most Indian companies are banking on infrastructure expenditure of US $1 trillion in the 12th Five-year Plan. According to India's 12th Five-year Plan (2012-17) document, the two most important segments of construction are infrastructure and housing. Since infrastructure spending is expected to go up to 9% of gross domestic product (GDP) or US $1 trillion for the Plan period (2012-17), this should translate into incremental growth for steel industry.

Financial Statements

Exhibit 13: Income Statement

INR mn	FY13	FY14	FY15	FY16E	FY17E	FY18E
Net Revenue	1,852	1,813	1,924	2,106	3,146	4,194
Y-o-Y Growth	20.5%	-2.1%	6.1%	9.4%	49.4%	33.3%
EBITDA	32.3	51.7	57.6	99.7	133.0	166.6
EBITDA Margin	1.8%	2.9%	3.1%	4.9%	4.4%	4.1%
Depreciation	17.9	17.7	22.6	24.8	28.0	33.6
EBIT	14.5	34.0	35.0	74.9	105.1	132.9
EBIT Margin	0.8%	1.9%	1.9%	3.7%	3.5%	3.3%
Interest	54.1	45.6	52.7	66.6	68.8	84.4
Other Income	55.7	31.2	23.9	27.2	42.1	58.3
PBT	16.0	19.5	6.1	35.5	78.5	106.9
Tax	4.9	3.1	1.8	8.9	19.6	26.7
PAT	11.1	16.4	4.3	26.7	58.8	80.2
PAT margin	0.6%	0.9%	0.2%	1.3%	1.9%	1.9%
Adjustment	-	0.6	0.5	-	-	-
Adjusted PAT	11.1	17.1	4.8	26.7	58.8	80.2
Adj. EPS (Rs)	44.5	68.6	3.2	17.9	39.4	53.7

Source: Khambatta research, Company data

Exhibit 14: Balance Sheet

INR mn	FY13	FY14	FY15	FY16E	FY17E	FY18E
Share Capital	2.5	2.5	14.9	14.9	14.9	14.9
Reserve & Surplus	166.5	197.9	192.0	218.7	277.5	357.7
Networth	169.0	200.4	207.0	233.6	292.5	372.6
Total Debt	410.9	394.6	632.3	663.4	743.6	982.8
Net deferred Tax Liabilities	8.6	6.5	2.7	4.1	6.1	8.0
Long Term Debt	95.8	91.4	168.5	168.5	108.5	108.5
Other non-current Liabilities	-	-	-	-	-	-
Total non-current Liabilities	104.4	97.9	171.2	172.6	114.5	116.5
Short Term Debt	315.1	303.2	463.8	495.0	635.1	874.3
Sundry Creditiors	54.2	74.4	23.4	43.4	56.0	78.3
Other current Liabilities	58.3	70.7	96.5	78.2	98.8	133.9
Current Liabilities	427.6	448.3	583.7	616.6	789.9	1,086.6
Total Libilities	701.1	746.6	961.9	1,022.7	1,196.9	1,575.7
Net Fixed Assets	152.8	144.6	118.1	157.1	191.5	309.9
CWIP	1.9	6.1	63.8	62.4	64.9	142.5
Non Current Investment	23.8	28.6	127.4	134.0	168.5	223.8
Other non-current assets	79.9	96.6	11.4	15.6	22.8	35.2
Total Non-current Assets	258.4	275.9	320.6	369.1	447.8	711.4
Current Investment	-	-	-	-	-	-
Cash & Bank Balance	21.4	22.4	74.5	82.6	44.1	17.5
Loan & Advances	25.1	63.8	199.0	173.7	174.9	105.6
Inventories	164.7	207.2	256.2	249.2	325.5	456.6
Sundry Debtors	166.0	175.8	111.3	128.6	179.3	249.4
Other current Assets	65.4	1.5	0.2	19.6	25.3	35.2
Total Current Assets	442.7	470.6	641.2	653.6	749.2	864.3
Net current Assets	15.1	22.3	57.6	37.1	(40.7)	(222.3)
Total Assets	701.1	746.6	961.9	1,022.7	1,196.9	1,575.7

Source: Khambatta research, Company data

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Exhibit 15: Ratio Analysis

Particulars	FY13	FY14	FY15	FY16E	FY17E	FY18E
EPS (Rs)	7.4	11.4	3.2	17.9	39.4	53.7
CEPS (Rs)	19.4	23.3	18.4	34.5	58.1	76.2
Book Value (Rs)	113.2	134.2	138.6	156.4	195.8	249.5
Long Term D/E (x)	0.6	0.5	0.8	0.7	0.4	0.3
Total D/E (x)	2.43	1.97	3.05	2.84	2.54	2.64
Inventory Days	33.0	42.9	50.1	45.3	39.4	41.4
Debtor Days	10.9	15.4	4.6	7.9	6.8	7.1
Creditor Days	33.3	35.8	21.7	23.0	21.6	22.6
ROACE	1.7%	5.1%	3.9%	6.5%	8.2%	8.3%
ROAE	6.8%	9.2%	2.4%	12.1%	22.4%	24.1%
ROAA	1.4%	4.1%	3.2%	5.7%	7.1%	7.2%
Dupont Analysis						
Tax Burden	0.69	0.70	0.56	0.75	0.75	0.75
Interest Burden	1.11	0.72	0.25	0.47	0.75	0.80
EBIT M	1%	2%	2%	4%	3%	3%
Assets T/O	2.60	2.48	2.19	2.05	2.73	2.90
Finanical Leverage	4.28	3.92	4.19	4.50	4.22	4.17
ROAE	6.77%	9.24%	2.36%	12.10%	22.37%	24.10%
Valuation Ratio						
PE (x)	124.67	80.92	286.68	51.79	23.47	17.23
EV/EBITDA (x)	44.99	28.02	25.61	14.71	10.86	8.84
Cash P/E (x)	47.71	39.67	50.33	26.84	15.90	12.14
Price/book value (x)	8.17	6.89	6.67	5.91	4.72	3.71
EV/sales (x)	0.80	0.81	0.79	0.72	0.48	0.37
Margin						
EBITDA margin	1.8%	2.9%	3.1%	4.9%	4.4%	4.1%
EBIT margin	0.8%	1.9%	1.9%	3.7%	3.5%	3.3%
Adj. PAT margin	0.6%	0.9%	0.3%	1.3%	1.9%	1.9%

Source: Khambatta research, Company data

Key risks

- The Khopoli expansion would cater to the export market as well as the local market. If the global economy does not improve now, the risk of under-utilization would change our revenue and profitability projections.
- The Sahidabad plant is facing an acute power shortage as the company primarily depends on government power supply. We assume power supply will remain at the current level. Any major shortfall in power supply at the Sahibabad plant might change our projection and profitability estimates.
- RST's products are primarily linked to economic growth. We assume an uptrend in the economic cycle for the next few years. Any major delay in an economic pick-up may impact our assumptions.
- Slowing domestic demand has dented realisations in the last few quarters. We believe that demand will improve following more construction activity and the Power-to-All programme by 2022. We project a marginal improvement in realizations based on the above assumption; any major delay in demand turning up would impact our projection.

Guide to Khambatta's research approach

Valuation methodologies

We apply the following absolute/relative valuation methodologies to derive the 'fair value' of the stock as a part of our fundamental research:

DCF: The Discounted Cash Flow (DCF) method values an estimated stream of future free cash flows discounted to the present day, using a company's WACC or cost of equity. This method is used to estimate the attractiveness of an investment opportunity and as such provides a good measure of the company's value in absolute terms. There are several approaches to discounted cash flow analysis, including Free Cash Flow to Firm (FCFF), Free Cash Flow to Equity (FCFE) and the Dividend Discount Model (DDM). The selection of a particular approach depends on the particular company being researched and valued.

ERE: The Excess Return to Equity (ERE) method takes into consideration the absolute value of a company's return to equity in excess of its cost of equity discounted to the present day using the cost of equity. This methodology is more appropriate for valuing banking stocks than FCFF or FCFE methodologies.

Relative valuation: In relative valuation, various comparative multiples or ratios including Price/Earnings, Price/Sales, EV/Sales, EV/EBITDA, Price/Book Value are used to assess the relative worth of companies which operate in the same industry/industries and are thereby in the same peer group. Generally our approach involves the use of two multiples to estimate the relative valuation of a stock.

Other methodologies such as DuPont Analysis, CFROI, NAV and Sum-of-the-Parts (SOTP) are applied where appropriate.

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Strong Buy recommendations are expected to improve, based on consideration of the fundamental view and the currency impact (where applicable) by at least 15%.

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