Gandhi Special Tubes (GANSPE)

₹ 330

Rating matrix		
Rating	:	Hold
Target	:	₹ 345
Target Period	:	12-18 months
Potential Upside	:	5%

What's changed?	
Target	Changed from ₹ 335 to ₹ 345
EPS FY18E	Changed from ₹ 18.1 to ₹ 21.0
EPS FY19E	Changed from ₹ 20.8 to ₹ 23.0
Rating	Unchanged

Key financials

₹ crore	FY16	FY17E	FY18E	FY19E
Net Sales	87.2	94.3	105.6	116.2
EBITDA	26.9	32.9	39.1	43.0
Net Profit	18.5	29.7	30.9	33.9
EPS (₹)	12.6	20.2	21.0	23.1

Valuation summary

	FY16	FY17E	FY18E	FY19E
P/E	26.2	16.3	15.7	14.3
Target P/E	27.4	17.1	16.4	15.0
EV / EBITDA	14.9	11.8	9.6	8.3
P/BV	2.9	2.7	2.5	2.3
RoNW	11.2	16.6	16.1	16.3
RoCE	14.6	19.9	22.0	22.4
ROIC	25.2	31.8	39.3	43.6

Stock data

Stock Data	
Market Capitalization	₹ 485 crore
Total Debt (FY17)	₹ 0 crore
Cash and Cash Equivalent (FY17)	₹ 97 crore
EV	₹ 388 crore
52 week H/L	375 / 280
Equity Capital	7.4
Face Value	₹ 5
MF Holding (%)	0.0
FII Holding (%)	4.2

Stock data

	1M	3M	6M	12M
Gandhi Special Tubes	6.4	1.2	0.3	4.4
Maharashtra Seamless	0.8	12.0	30.2	81.8
Ratnamani Metals & Tubes	0.8	8.5	13.5	47.7

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Healthy H1FY18, steady growth prospects...

- Gandhi Special Tubes (GST) reported a healthy Q2FY18 performance (sales up 8.4% YoY, margins up 440 bps YoY) despite one of its main business segment (fuel injection tubes) going off stream due to mandatory conversion to BS-IV norms in the domestic M&HCV space
- Net sales for the quarter came in at ₹ 29.8 crore. EBITDA in Q2FY18 was at ₹ 11.4 crore with corresponding EBITDA margins at 38.3%, up 440 bps. Savings were realised across variables viz. raw material costs, power & fuel costs and other expenses
- PAT in Q2FY18 was at ₹ 8.7 crore, up 41% YoY
- For H1FY18, net sales were at ₹ 58 crore, up 7% YoY while EBITDA was at ₹ 22 crore, up16% YoY and PAT came in at ₹ 18 crore. PAT is flat YoY due to higher tax incidence in H1FY18 vs. H1FY17

Monsoon 2017 satisfactory; ends at near normal (-5% of LPA)

Monsoon 2017 began with bright, widespread distribution across India with rainfall in June at +4% LPA and July at +2% of LPA before slowing down in August (-13% of LPA) & September (-12% of LPA) to finally end the season at -5% of LPA. On the spatial distribution front, monsoon 2017 was normal in southern, eastern India and below normal in northern, central India. However, the impact of near normal monsoon on farm income may be limited, given high irrigation penetration in key rainfall deficient agrarian states like Punjab (99%), Haryana (86%) and Uttar Pradesh (76%), auguring well for agri input companies. GST supplies fuel injection tubes to the tractor segment. Hence, it would be a key beneficiary of robust tractor demand domestically.

Product segment catering to core industrial activity

GST is a manufacturer of small diameter seamless and welded steel tubes, which find application in automotive, hydraulics, refrigeration (condenser tubes) and other engineering services. In the automotive space, the company's products find application as fuel injection tubes in the tractor segment. GST is an OEM approved tier-II supplier of seamless tubes. In hydraulics, the company's products find application in material (bulk) handling equipment, which are used for construction & mining purposes. In the hydraulics segment, GST's clientele includes Larsen & Toubro, BEML, Bhel and Bosch Rexroth India, among others. Welded steel tubes find application in refrigeration and automobile (fuel lines, oil lines & air brake lines) segments. Thus with Goods & Services Tax in place and the government's focus on pick-up in industrial activity on account of ambitious Bharatmala project (National Highways, Roads), we expect GST to witness strong product demand with robust prospects, going forward.

Impressive balance sheet, return ratios, ascribe HOLD rating!

GST's performance in H1FY18 is impressive amid a challenging demand scenario, depicting diversification of product and customer base. Sustenance of 37%+ EBITDA margins is also encouraging given capacity utilisations at muted levels of below 50%. It has a lean balance sheet with surplus cash & investments of ₹ 97 crore (FY17). With robust dividend payout (>40%) amid high double digit margins, GST realises robust return ratios with RoCEs & RoICs in excess of 20% & 30%, respectively. The company also holds an option value of any global technology tie-up to better utilise its idle capacity at its plant in Gujarat. Going forward, we expect sales & PAT to grow at a CAGR of 9.1% & 6.9%, respectively, over FY17-19E. We now value GST at ₹ 345, i.e. 15x P/E on FY19E EPS of ₹ 23.1/share with a **HOLD** rating on the stock.

GST also owns ~5.3 MW of wind power capacity in India with wind plants based out of Gujarat and Maharashtra. In Gujarat, the generated wind power is consumed captively while in Maharashtra, the generated wind power is sold to the state grid.

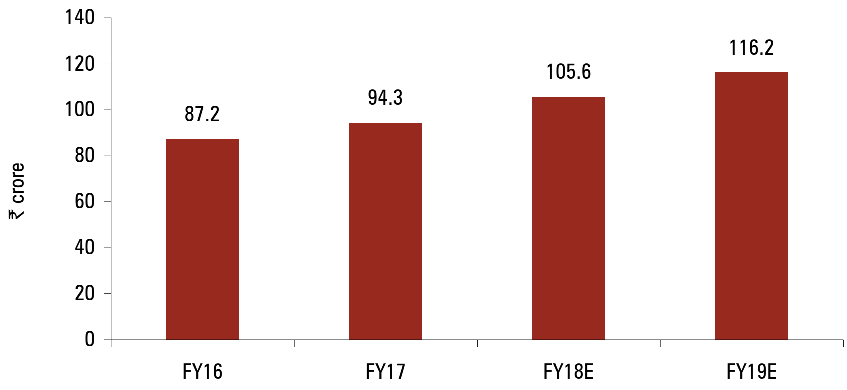
Company Analysis

Gandhi Special Tubes (GST) is a manufacturer of small diameter seamless and welded steel tubes, which find application in automotive, hydraulics, refrigeration (condenser tubes) and other engineering services. The company commenced operations at its Halol (Gujarat) Plant in 1988 and was set up in technical collaboration with Benteler (Germany). GST also manufactures cold formed tube nuts for fuel injection tube assemblies, hydraulic & other tube assemblies, which act as an auxiliary unit for its seamless tube segment. In the automotive space, GST's products find application as fuel injection tubes in the M&HCV segment including tractors. In hydraulics, the company's products find application in material (bulk) handling equipment. Welded steel tubes find application in the refrigeration and automobile (fuel lines, oil lines etc) segments.

Sales to grow 9.1% CAGR in FY17-19E

We expect GST to clock revenue growth of 9.1% CAGR in FY17-19E primarily on a pick-up in tractor sales domestically and rebound expected in bulk handling equipment space over FY18E-19E. We expect the company to clock sales of ₹ 105.6 crore in FY18E & ₹ 116.2 crore in FY19E

Exhibit 1: Sales trend

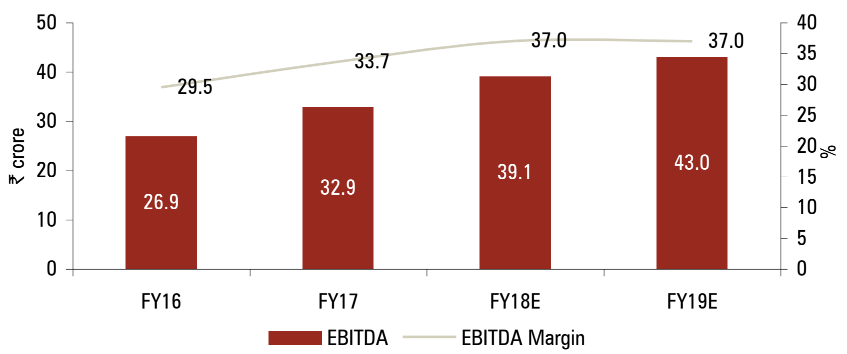


Source: Company, ICICIdirect.com Research

Margin expansion underway, EBITDA to grow 14.3% CAGR over FY17-19

GST recorded a 420 bps improvement in EBITDA margin in FY17 with corresponding EBITDA margin at 33.7%. It was largely tracking lower power & fuel costs and lower other expenses. Gaining further on its expertise of managing the raw material costs and other overheads it has progressively expanded its margins with EBITDA margins in FY18E expected at 37%, up 330 bps YoY.

Exhibit 2: EBITDA & EBITDA margin trend

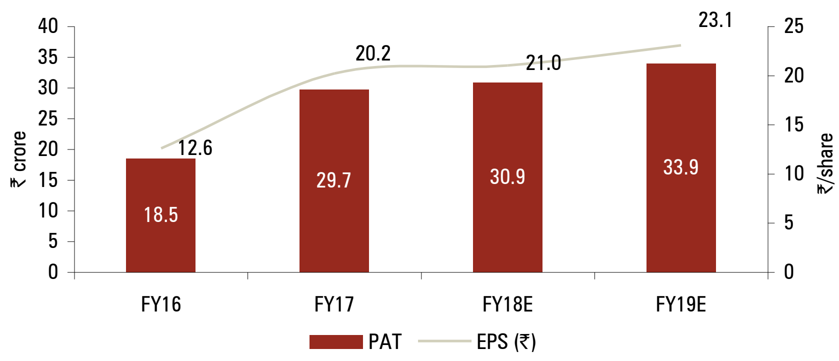


Source: Company, ICICIdirect.com Research

PAT to grow at 6.9% CAGR over FY17-19E

PAT is expected to lag the EBITDA growth with consequent CAGR of 6.9% in FY17-19E primarily tracking a lower effective tax rate in the base year at 20% (FY17) vs. the usual rate of ~30%.

Exhibit 3: PAT & EPS trend

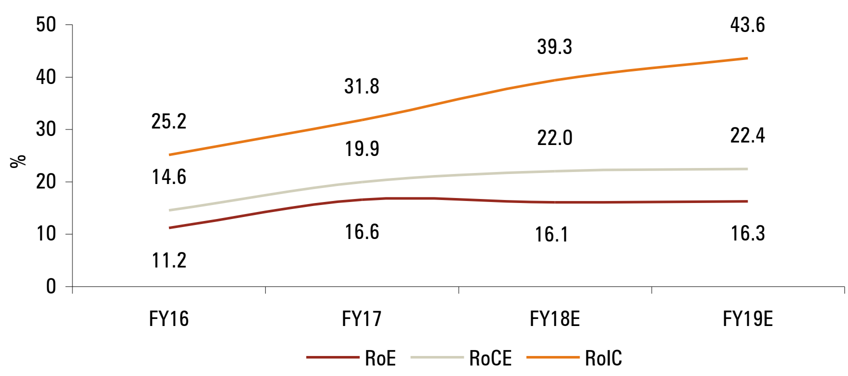


Source: Company, ICICIdirect.com Research

Impressive return ratios; RoCE>20% & RoICs>30% over FY17-19E

Return ratios had taken a hit due to the subdued demand scenario and consequent de-growth in the topline. The return ratios (RoCE, RoE) have declined from a peak of 29.5%, 22.1% in FY11 to about 13.6%, 9.8%, respectively, in FY15. However, with the revival in tractor sales domestically and expectations of a pick-up in industrial activity, we expect return ratios to improve with RoCE, RoICs in FY19E expected at 22.4% and 43.6%, respectively.

Exhibit 4: Return ratios set to improve over FY17-19E



Source: Company, ICICIdirect.com Research

Outlook and valuation

GST's performance in H1FY18 is impressive amid challenging demand scenario, depicting diversification of product and customer base. Sustenance of 37%+ EBITDA margins is also encouraging given capacity utilisation at muted levels of below 50%. It has a lean balance sheet with surplus cash & investments of ₹ 97 crore (FY17). With a robust dividend payout (>40%) amid high double digit margins, GST realises robust return ratios with RoCEs & RoICs in excess of 20% & 30%, respectively. The company also holds an option value of any global technology tie-up to better utilise its idle capacity at its plant in Gujarat. Going forward, we expect sales & PAT to grow at a CAGR of 9.1% & 6.9%, respectively, over FY17-19E. We now value GST at ₹ 345, i.e. 15x P/E on FY19E EPS of ₹ 23.1/share with a **HOLD** rating on the stock.

Exhibit 5: What's changed??

Particulars	FY18E			FY19E		
	Old	New	% Change	Old	New	% Change
Sales	102.5	105.6	3.1	114.8	116.2	1.2
EBITDA	35.3	39.1	10.8	40.2	43.0	6.9
EBITDA Margin %	34.4	37.0	260 bps	35.0	37.0	198 bps
PAT	26.6	30.9	16.2	30.6	33.9	10.9
EPS	18.1	21.0	16.2	20.8	23.1	10.9

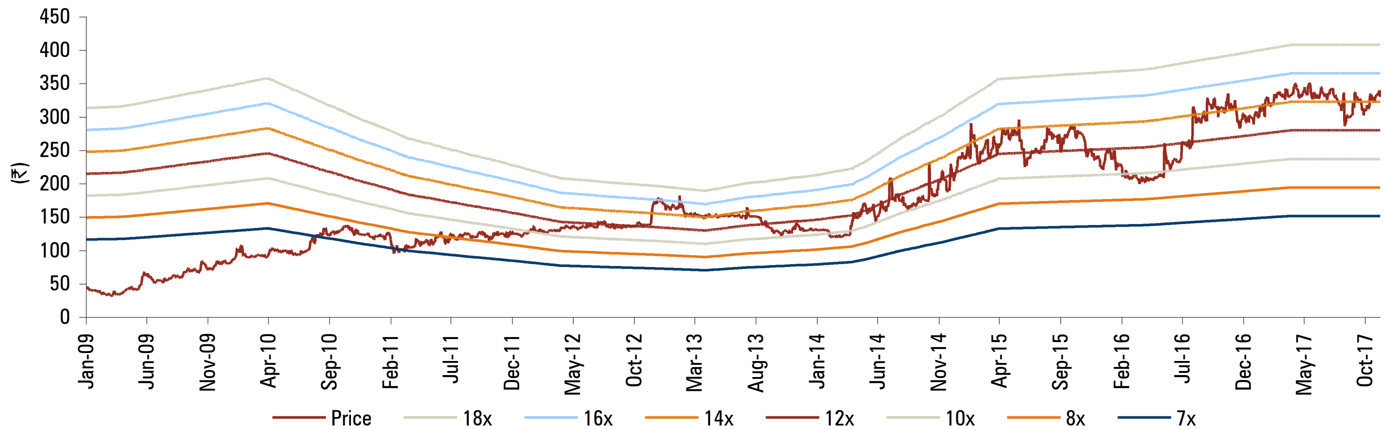
Source: Company, ICICIdirect.com Research

Exhibit 6: Valuation Summary

Year	Sales (₹ cr)	Growth (%)	PAT (₹)	Growth (%)	PE (x)	EV/EBITDA (x)	RoNW (%)	RoCE (%)	RoIC (%)
FY16	91.2	-0.8	18.5	17.5	26.2	14.9	11.2	14.6	25.2
FY17	97.6	7.0	29.7	60.5	16.3	11.8	16.6	19.9	31.8
FY18E	105.6	8.2	30.9	4.0	15.7	9.6	16.1	22.0	39.3
FY19E	116.2	10.0	33.9	9.8	14.3	8.3	16.3	22.4	43.6

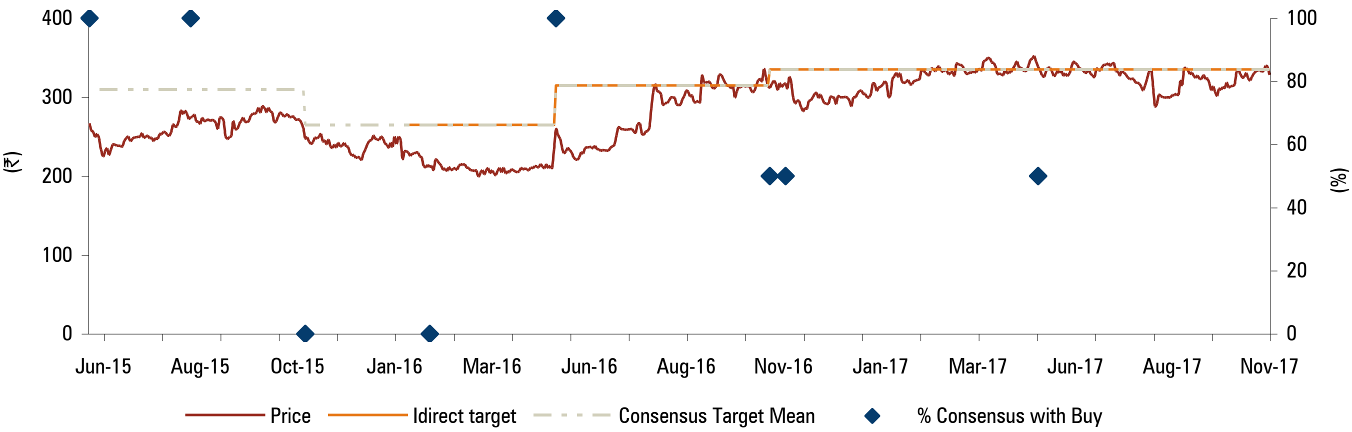
Source: Company, ICICIdirect.com Research

Exhibit 7: Two year forward P/E (GST currently trading at 14.3x)



Source: Reuters, ICICIdirect.com Research

Recommendation history vs. Consensus



Source: Bloomberg, Company, ICICIdirect.com Research

Key events

Date/Year	Event
2007	Reports sales of ₹ 60.2 crore, limited due to capacity constraints. GST had undertaken a capex amounting to ₹ 12.8 crore in FY07, out of ₹ 12.6 crore was towards installation of plant and machinery. The entire capex was funded by the company's internal cash accruals
2008	Further undertakes capex amounting to ₹ 18.4 crore, out of which ₹ 3.3 crore was spent towards new factory building, ₹ 8.7 crore towards plant & machinery and ₹ 6.3 crore towards windmill. The entire capex was funded out of the company's internal cash accruals
2008	Closes down its Pune plant with effect from July 25, 2008. The said plant was engaged mainly in assembly of components transferred from the company's Halol plant and supplying the finished products to customers in nearby area. After completion of the expansion project at Halol, the company now had sufficient resources at its Halol Plant to undertake assembly and supply of products to all its customers from the said plant itself
2010	On occasion of silver jubilee year, board of directors of GST declares special interim dividend of ₹ 2.5 per equity shares of ₹ 5/- each. Regular interim dividend of ₹ 2.5 per equity share was also declared
2012	Stops production of refrigeneration condensor coils; as business was highly seasonal. The company embarks upon the new capex plan amounting ₹ 40 crore. GST's planned capex includes capex of ₹ 10 crore for building, ₹ 20 crore for plant & machinery and ₹ 10 crore for new corporate office in Mumbai
2014	In August, Customs department (Government of India) imposes a safeguard duty on import of seamless steel tubes and pipes of external diameter not exceeding 273.1 mm (outer diameter) on imports from developed countries and China. GST would also be a key beneficiary of the said judgement
2015	Reports subdued Q4FY15 with full year FY15 PAT at ₹ 15.8 crore, down 8.7% YoY. The interaction with the management suggests near exhaustion of inventory pertaining to company's product profile in the user market with turnaround in sales expected in Q2FY16
2016	Reports robust Q4FY16 with sales growing 20% YoY and EBITDA margins coming in at 29%. Full year FY16, Sales, EBITDA & PAT were at ₹ 91 crore, ₹ 27 crore & ₹ 19 crore, respectively. The company has also declared and distributed a dividend of ₹ 7.5/share for FY16
2017	For full year FY17, GST clocked sales of ₹ 97.6 crore, up 7% YoY with EBITDA at ₹ 32.9 crore (EBITDA margins at 33.7%) and PAT at ₹ 29.7 crore. EPS in FY17 stood at ₹ 20.2 with dividend per share at ₹ 9. Improvement in EBITDA margins was encouraging though management commentary on future sales growth was cautious given transition of M&HCV segment to new emission norms (BS-4) and GST implementation domestically

Source: Company, ICICIdirect.com Research

Top 10 Shareholders

Rank	Name	Latest Filing Date	% O/S	Position (m)	Change (m)
1	Gandhi (Manhar G)	30-Sep-17	14.4	2.1	0.0
2	Gandhi (Bhupatrai G)	30-Sep-17	13.2	1.9	0.0
3	Gandhi (Jayesh M)	30-Sep-17	7.9	1.2	0.0
4	Gandhi (Manoj B)	30-Sep-17	7.5	1.1	0.0
5	Gandhi (Bharati M)	30-Sep-17	5.3	0.8	0.0
6	B M Gandhi Investment Company Pvt. Ltd.	30-Sep-17	3.8	0.6	0.0
7	Gandhi Finance Company Pvt. Ltd.	30-Sep-17	3.5	0.5	0.0
8	Gandhi (Chandra B)	30-Sep-17	3.2	0.5	0.0
9	Gandhi (Gopi J)	30-Sep-17	3.1	0.5	0.0
10	Gandhi (Jigna M)	30-Sep-17	3.1	0.4	0.0

Source: Reuters, ICICIdirect.com Research

Shareholding Pattern

(in %)	Sep-16	Dec-16	Mar-17	Jun-17	Sep-17
Promoter	73.3	73.3	73.3	73.3	73.3
FII	4.1	4.2	4.3	4.2	4.2
DII	0.0	0.0	0.0	0.0	0.0
Others	23.6	22.6	22.4	22.5	22.5

Recent Activity

Buys			Sells		
Investor name	Value	Shares	Investor name	Value(US$M)	Shares(M)
Nil			PineBridge Investments LLC	-0.14	-0.03

Source: Reuters, ICICIdirect.com Research

Financial summary

Profit and loss statement				₹ Crore
(Year-end March)	FY16	FY17	FY18E	FY19E
Net Sales	87.2	94.3	105.6	116.2
Other Operating Income	4.0	3.3	0.0	0.0
Total Operating Income	91.2	97.6	105.6	116.2
Growth (%)	-0.8	7.0	8.2	10.0
Raw Material Expenses	33.3	30.9	33.8	38.0
Employee Expenses	6.3	7.3	8.1	8.7
Power & Fuel Expense	9.0	11.0	10.4	11.4
Other Operating Expense	15.8	15.5	14.2	15.1
Total Operating Expenditure	64.3	64.7	66.5	73.2
EBITDA	26.9	32.9	39.1	43.0
Growth (%)	15.6	22.2	18.9	9.9
Depreciation	4.8	4.4	3.9	4.0
Interest	0.0	0.0	0.0	0.0
Other Income	3.0	8.7	8.8	9.5
PBT	25.2	37.1	44.0	48.5
Exceptional Item	0.0	0.0	0.0	0.0
Total Tax	6.7	7.4	13.1	14.5
PAT	18.5	29.7	30.9	33.9
Growth (%)	17.5	60.5	4.0	9.8
EPS (₹)	12.6	20.2	21.0	23.1

Source: Company, ICICIdirect.com Research

Cash flow statement				₹ Crore
(Year-end March)	FY16	FY17	FY18E	FY19E
Profit after Tax	18.5	29.7	30.9	33.9
Add: Depreciation	4.8	4.4	3.9	4.0
(Inc)/dec in Current Assets	7.2	-6.3	-3.2	-3.0
Inc/(dec) in CL and Provisions	0.7	1.1	1.4	1.0
Others	0.0	0.0	0.0	0.0
CF from operating activities	31.1	28.9	33.0	35.9
(Inc)/dec in Investments	-16.3	-12.2	-11.0	-15.0
(Inc)/dec in Fixed Assets	-1.0	-0.6	-2.0	-2.0
Others	0.3	0.0	0.0	0.0
CF from investing activities	-17.0	-12.8	-13.0	-17.0
Issue/(Buy back) of Equity	0.0	0.0	0.0	0.0
Inc/(dec) in loan funds	0.0	0.0	0.0	0.0
Dividend paid & dividend tax	-13.3	-15.9	-17.6	-17.6
Inc/(dec) in Share Cap	0.4	0.0	0.0	0.0
Others	0.0	0.0	0.0	0.0
CF from financing activities	-12.9	-15.9	-17.6	-17.6
Net Cash flow	1.2	0.3	2.3	1.3
Opening Cash	1.8	3.0	3.3	5.6
Closing Cash	3.0	3.3	5.6	6.9

Source: Company, ICICIdirect.com Research

Balance sheet				₹ Crore
(Year-end March)	FY16	FY17	FY18E	FY19E
Liabilities				
Equity Capital	7.4	7.4	7.4	7.4
Reserve and Surplus	158.0	171.8	185.1	201.4
Total Shareholders funds	165.4	179.2	192.5	208.8
Total Debt	0.0	0.0	0.0	0.0
Deferred Tax Liability	7.4	7.4	7.4	7.4
Minority Interest / Others	0.0	0.0	0.0	0.0
Total Liabilities	172.8	186.6	199.9	216.2
Assets				
Gross Block	130.2	130.0	132.0	134.0
Less: Acc Depreciation	71.1	74.8	78.7	82.7
Net Block	59.0	55.2	53.3	51.3
Capital WIP	0.0	0.0	0.0	0.0
Total Fixed Assets	59.0	55.2	53.3	51.3
Investments	81.6	93.8	104.8	119.8
Inventory	17.0	24.3	24.6	25.5
Debtors	16.1	16.3	18.8	20.7
Loans and Advances	2.9	1.6	2.1	2.3
Other Current Assets	0.5	0.6	0.5	0.6
Cash	3.0	3.3	5.6	6.9
Total Current Assets	39.5	46.1	51.7	56.0
Current Liabilities	4.4	4.9	5.8	6.4
Provisions	3.0	3.6	4.1	4.5
Current Liabilities & Prov	7.4	8.5	9.8	10.8
Net Current Assets	32.1	37.6	41.8	45.1
Others Assets	0.0	0.0	0.0	0.0
Application of Funds	172.8	186.6	199.9	216.2

Source: Company, ICICIdirect.com Research

Key ratios				
(Year-end March)	FY16	FY17	FY18E	FY19E
Per share data (₹)				
EPS	12.6	20.2	21.0	23.1
Cash EPS	15.8	23.2	23.7	25.8
BV	112.5	121.9	130.9	142.0
DPS	7.5	9.0	10.0	10.0
Cash Per Share (Incl Invst)	57.6	66.0	75.1	86.2
Operating Ratios (%)				
EBITDA Margin	29.5	33.7	37.0	37.0
PAT Margin	20.3	30.4	29.3	29.2
Inventory days	71.1	94.2	85.0	80.0
Debtor days	67.5	63.0	65.0	65.0
Creditor days	18.4	19.0	20.0	20.0
Return Ratios (%)				
RoE	11.2	16.6	16.1	16.3
RoCE	14.6	19.9	22.0	22.4
RoIC	25.2	31.8	39.3	43.6
Valuation Ratios (x)				
P/E	26.2	16.3	15.7	14.3
EV / EBITDA	14.9	11.8	9.6	8.3
EV / Net Sales	4.6	4.1	3.5	3.1
Market Cap / Sales	5.6	5.1	4.6	4.2
Price to Book Value	2.9	2.7	2.5	2.3
Solvency Ratios				
Debt/EBITDA	0.0	0.0	0.0	0.0
Debt / Equity	0.0	0.0	0.0	0.0
Current Ratio	4.9	5.1	4.7	4.5
Quick Ratio	2.6	2.2	2.2	2.2

Source: Company, ICICIdirect.com Research

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Sell: -10% or more;

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