

November 3, 2017

Graphite India (CAREVE)

₹ 575

Performance to improve notably...

Graphite India has been one of the good wealth creators for investors with the stock price nearly multiplying ~3.3x since our [Sector Update](#) in July, 2017. However, we believe there is more leg room in the stock price appreciation given the bright outlook of the global graphite electrode sector. Graphite India is the largest producer of graphite electrodes by capacity in India and accounts for 12.6% of global capacity (ex-China).

Multiple triggers put graphite electrode industry in sweet spot...

The fortunes of the graphite electrode sector have been on an uptrend. Over the last few months, spot graphite electrode prices have registered a notable increase. Key triggers have been 1) consolidation of the graphite electrode market globally, 2) ~20% of global graphite electrode capacity (ex-China) shutting down in the last three years, 3) increase in steel production through EAF route (outside China) coupled with an increase in global steel prices, 4) closure of steel capacity in China has led to a decline in both steel and graphite electrode exports from the region.

Exhibit 1: Change in Estimates

(₹ Crore)	FY17	FY18E			FY19E		
		Old	New	% Change	Old	New	% Change
Revenue	1,467.8	2,299.4	2,523.7	9.8	3,460.8	3,811.5	10.1
EBITDA	39.6	426.3	631.4	48.1	940.7	1,249.0	32.8
EBITDA Margin (%)	2.7	18.5	25.0	648 bps	27.2	32.8	559 bps
PAT	70.5	301.4	457.8	51.9	664.8	899.2	35.3
EPS (₹)	3.6	15.4	23.4	51.9	34.0	46.0	35.3
Standalone capacity utilisation	79%	91%	91%	-	80%	80%	-
Consolidated capacity utilisation	74%	84%	84%	-	75%	75%	-

Source: Company, ICICIdirect.com Research

Capacity shutdown in China augurs well for the sector...

On account of stringent environmental norms China has been witnessing capacity cuts in both steel as well as graphite electrodes. The capacity cuts in steel have led to a decline in steel exports from the region, thereby encouraging steel production through EAF route in other countries (boosting demand for graphite electrodes). Concurrently, over the last few months, ~50% of the Chinese graphite electrode capacity has closed down, resulting in China becoming a net importer of electrodes from net exporter earlier. The lower exports from the region have vacated a substantial part of the global electrode market. This has tilted the graphite electrode demand-supply dynamics in favour of domestic players like Graphite India. The demand-supply imbalance has boosted graphite electrode prices.

Good times ahead, reiterate BUY!

For H1FY18, Graphite India reported a strong performance driven by better capacity utilisation and a sharp increase in realisation. For H1FY18, the company reported standalone revenues of ₹ 812.9 crore with EBITDA of ₹ 165.4 crore implying an EBITDA margin of 20.3% (vs. H1FY17: standalone revenues of ₹ 594.8 crore and EBITDA of ₹ 24.6 crore, EBITDA margin of 4.1%). Going forward, we expect EBITDA margins and return ratios to improve substantially. We value the stock at 10x FY19E EV/EBITDA thereby arriving at a target price of ₹ 725. Graphite India has a robust balance sheet, net cash status and healthy cash flow generation, which augurs well. We maintain our **BUY** recommendation on the stock.

Rating matrix	
Rating	: Buy
Target	: ₹ 725
Target Period	: 15-18 months
Potential Upside	: 26%

What's Changed?	
Target	Changed from ₹ 550 to ₹ 725
EPS FY18E	Changed from ₹ 15.4 to ₹ 23.4
EPS FY19E	Changed from ₹ 34.0 to ₹ 46.0
Rating	Unchanged

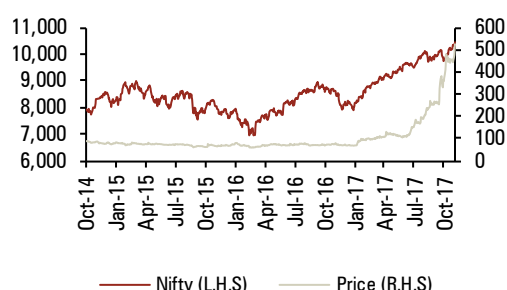
Key Financials (Consolidated)				
(₹ Crore)	FY16	FY17	FY18E	FY19E
Total Operating Income	1532.3	1467.8	2523.7	3811.5
EBITDA	134.6	39.6	631.4	1249.0
Net Profit	82.8	70.5	457.8	899.2
EPS	4.2	3.6	23.4	46.0

Valuation summary				
	FY16	FY17	FY18E	FY19E
PE (x)	135.7	159.5	24.5	12.5
Target PE (x)	171.2	201.2	31.0	15.8
EV/EBITDA (x)	82.5	273.4	17.0	8.1
P/BV (x)	6.4	6.0	5.4	4.2
RoNW (%)	4.7	3.8	22.1	33.3
RoCE (%)	4.2	-0.3	25.3	43.7

Stock data	
Particular	Amount
Market Capitalisation (₹ crore)	₹ 11236
Debt (FY17) (₹ crore)	₹ 259
Cash & Cash Equivalent (FY17) (₹ crore)	₹ 683
EV (₹ crore)	₹ 10812
52 week H/L	575 / 70
Equity capital (₹ crore)	₹ 39.1
Face value	₹ 2

Price performance (%)				
Return %	1M	3M	6M	12M
HEG	87.8	251.8	470.1	927.1
Graphite India	47.4	161.1	349.7	576.7

Share Price Graph



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Financial summary (Cons)

Profit and loss statement (₹ crore)				
(Year-end March)	FY16	FY17	FY18E	FY19E
Total Operating Income	1532.3	1467.8	2523.7	3811.5
Growth (%)	-10	-4	72	51
Raw Material Expenses	646.1	585.1	824.0	1,287.3
Employee Expenses	201.2	222.5	265.7	341.0
Other expenses	550.4	620.6	802.6	934.2
Total Operating Expenditure	1,397.8	1,428.2	1,892.3	2,562.5
EBITDA	134.6	39.6	631.4	1249.0
Growth (%)	-1.6	-70.6	1,496.6	97.8
Depreciation	49.2	46.4	54.6	55.8
Interest	9.5	7.9	7.0	3.5
Other Income	49.4	86.5	113.5	152.5
PBT	125.4	71.8	683.3	1,342.1
Exceptional Item	0.0	0.0	0.0	0.0
Total Tax	42.6	1.3	225.5	442.9
PAT	82.8	70.5	457.8	899.2
Growth (%)	43.8	-14.9	549.8	96.4
EPS (₹)	4.2	3.6	23.4	46.0

Source: Company, ICICIdirect.com Research

Balance sheet (₹ crore)				
(Year-end March)	FY16	FY17	FY18E	FY19E
Liabilities				
Equity Capital	39.1	39.1	39.1	39.1
Reserve and Surplus	1,712.0	1,818.5	2,032.4	2,663.3
Total Shareholders funds	1,751.1	1,857.6	2,071.5	2,702.4
Total Debt	302.3	259.2	205.2	30.2
Deferred Tax Liability	72.8	85.0	85.0	85.0
Minority Interest / Others	0.0	0.0	0.0	0.0
Total Liabilities	2,126.2	2,201.8	2,361.7	2,817.6
Assets				
Gross Block	1,416.5	1,539.1	1,583.1	1,608.1
Less: Acc Depreciation	825.3	871.7	926.3	982.2
Net Block	591.2	667.4	656.8	625.9
Capital WIP	65.5	32.1	3.1	3.1
Total Fixed Assets	656.7	699.5	659.8	629.0
Investments	416.0	631.0	681.0	1,081.0
Inventory	748.5	602.1	613.7	647.8
Debtors	484.8	441.5	454.6	448.5
Loans and Advances	112.3	11.7	95.8	50.8
Other Current Assets	17.1	103.5	78.5	53.5
Cash	21.0	51.5	271.0	634.2
Total Current Assets	1,383.7	1,210.1	1,513.6	1,834.8
Current Liabilities	271.2	316.0	409.1	598.0
Provisions	58.9	25.7	83.5	129.2
Current Liabilities & Prov	330.1	341.7	492.7	727.2
Net Current Assets	1,053.6	868.4	1,020.9	1,107.6
Others Assets	0.0	2.9	0.0	0.0
Application of Funds	2,126.2	2,201.8	2,361.7	2,817.6

Source: Company, ICICIdirect.com Research

Cash flow statement (₹ crore)				
(Year-end March)	FY16	FY17	FY18E	FY19E
Profit after Tax	82.8	70.5	457.8	899.2
Add: Depreciation	49.2	46.4	54.6	55.8
(Inc)/dec in Current Asset	182.2	204.0	-84.0	42.0
Inc/(dec) in CL & Provision	-69.3	11.6	151.0	234.5
Others	-9.3	9.3	2.9	0.0
CF from operating activities	235.5	341.7	582.4	1,231.6
(Inc)/dec in Investments	-46.6	-215.1	-50.0	-400.0
(Inc)/dec in Fixed Assets	-56.5	-89.1	-15.0	-25.0
Others	0.0	0.0	0.0	0.0
CF from investing activities	-103.2	-304.2	-65.0	-425.0
Issue/(Buy back) of Equity	0.0	0.0	0.0	0.0
Inc/(dec) in loan funds	-64.8	-43.1	-54.0	-175.0
Dividend paid & div. tax	-47.0	-47.0	-137.5	-270.1
Inc/(dec) in Share Cap	-31.2	83.0	-106.4	1.7
Others	0.0	0.0	0.0	0.0
CF from financing activities	-142.9	-7.1	-297.9	-443.4
Net Cash flow	-10.5	30.4	219.5	363.2
Opening Cash	31.5	21.0	51.5	271.0
Closing Cash	21.0	51.5	271.0	634.2

Source: Company, ICICIdirect.com Research

Key ratios				
(Year-end March)	FY16	FY17	FY18E	FY19E
Per share data (₹)				
EPS	4.2	3.6	23.4	46.0
Cash EPS	6.8	6.0	26.2	48.9
BV	89.6	95.1	106.0	138.3
DPS	2.0	2.0	5.9	11.5
Cash Per Share	1.1	2.6	13.9	32.5
Operating Ratios (%)				
EBITDA Margin	8.8	2.7	25.0	32.8
PBT / Total Operating income	8.2	4.9	27.1	35.2
PAT Margin	5.4	4.8	18.1	23.6
Inventory days	178.3	149.7	135.0	130.0
Debtor days	115.5	109.8	100.0	90.0
Creditor days	64.6	78.6	90.0	120.0
Return Ratios (%)				
RoE	4.7	3.8	22.1	33.3
RoCE	4.2	-0.3	25.3	43.7
RoIC	4.2	-0.3	28.8	56.9
Valuation Ratios (x)				
P/E	135.7	159.5	24.5	12.5
EV / EBITDA	82.5	273.4	17.0	8.1
EV / Net Sales	7.2	7.4	4.2	2.6
Market Cap / Sales	7.3	7.7	4.5	2.9
Price to Book Value	6.4	6.0	5.4	4.2
Solvency Ratios				
Debt/EBITDA	2.2	6.6	0.3	0.0
Debt / Equity	0.2	0.1	0.1	0.0
Current Ratio	4.2	3.5	3.1	2.5
Quick Ratio	1.9	1.8	1.8	1.6

Source: Company, ICICIdirect.com Research

ICICIdirect.com coverage universe (Graphite steel electrodes)

Sector/Company	CMP			M Cap	EPS (₹)			P/E (x)			EV/EBITDA (x)			ROCE(%)			ROE(%)		
	(₹)	TP (₹)	Rating		FY17	FY18E	FY19E	FY17	FY18E	FY19E	FY17	FY18E	FY19E	FY17	FY18E	FY19E	FY17	FY18E	FY19E
Graphite India	575	725	Buy	11,236	3.6	23.4	46.0	159.5	24.5	12.5	273.4	17.0	8.1	-0.3	25.3	43.7	3.8	22.1	33.3
HEG	1840	2250	Buy	7,360	-12.5	76.9	152.4	NA	23.9	12.1	95.2	13.5	7.1	0.9	28.4	44.0	-5.7	26.1	34.1

Source: Company, ICICIdirect.com Research

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