

Graphite India (CAREVE)

₹ 950

No volume loss; cost impact fractional...

According to media sources, officials from the Karnataka State Pollution Control Board (KSPCB) inspected two units of Graphite India (GIL) in Bengaluru. Prima facie, the team indicated the plant is not complying with the required air pollution norms. KSPCB is expected to submit a report on the same to the National Green Tribunal (NGT) in a week. Earlier, KSPCB in 2012 served the plant a closure notice on which the company got a stay from the appeals court. Following the stay, the residents approached the NGT where the case is currently pending.

Stack emissions within prescribed norms, NGT outcome crucial...

In its filing, GIL has clarified that post the favourable court ruling in 2013, the company had rationalised its operations at the Bengaluru plant wherein in accordance with the business needs the extent of production activities were reduced. GIL also decommissioned the extrusion and old baking furnaces thereby significantly reducing stacks and fuel consumption resulting in reduction of emissions. The company indicated the stack emissions are well within prescribed norms. With regard to the ambient air quality GIL has indicated besides emission from the industry there are various other contributing factors like heavy vehicular traffic, construction activity, metro rail work and other industrial activities for the said pollution. We believe the outcome of the matter at NGT remains a key monitorable.

In case of adverse outcome - no volume loss, fractional impact on cost...

Graphite electrode production involves six steps, of which the Bengaluru plant is involved only in the graphitisation process. In case of an adverse outcome of the NGT hearing, the company will most likely shift its graphitisation operations from Bengaluru to other plants (Nashik or Durgapur), thereby insulating itself from any volume loss. The Bengaluru plant accounts for ~13% of total installed capacity of 98000 tonne. The graphitisation process is power intensive. Thus, shifting the plant will impact power cost. We believe power cost would increase by ~₹ 3/unit. Our back of the envelope calculation indicates the absolute impact of this increase in power cost on EBITDA will be ~0.5% (₹ 20 crore).

Growing EAF production points to healthy demand prospects...

Due to stringent environmental norms, China has shut ~155-160 million tonne (MT) of largely unaccounted induction furnace capacity along with ~115 MT steelmaking capacity in 2016-17. These capacity cuts have led to steel export reduction by ~40% from the region, thereby encouraging steel production via EAF route in other countries. Industry sources indicate that globally ~55 MT of EAF steel production was added in 2017. On the back of stringent pollution control norms, China is also aiming to increase the share of EAF route of steelmaking in its total steel production. In its effort to shift toward more environmental friendly steel production, China is likely to commission 66 MT of EAF capacity in CY18.

Favourable operating environment; maintain BUY

Given the strong demand and elevated prices, the operating environment continues to remain healthy for domestic graphite electrode player like Graphite India. We expect the topline, EBITDA and PAT to grow at a CAGR of 53%, 66% and 63%, respectively during FY18-FY20E. We continue to value the stock at 10x FY20E EPS of ₹ 140 and arrive at a target price of ₹ 1400. We reiterate our **BUY** recommendation on the stock.

Rating matrix	
Rating	: Buy
Target	: ₹ 1400
Target Period	: 12 months
Potential Upside	: 47%

What's Changed?	
Target	Unchanged
EPS FY19E	Unchanged
EPS FY20E	Unchanged
Rating	Unchanged

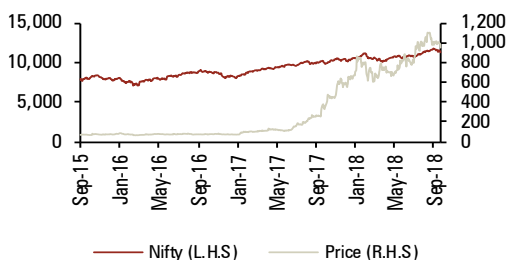
Key Financials				
(₹ Crore)	FY17	FY18	FY19E	FY20E
Total Operating Income	1467.8	3266.0	7347.2	7620.6
EBITDA	39.6	1444.2	3966.1	3980.8
Net Profit	70.5	1032.0	2697.3	2736.1
EPS	3.6	52.8	138.0	140.0

Valuation summary				
	FY17	FY18	FY19E	FY20E
PE (x)	263.5	18.0	6.9	6.8
Target PE (x)	388.3	26.5	10.1	10.0
EV/EBITDA (x)	458.7	12.2	4.3	4.0
P/BV (x)	10.0	6.8	4.8	3.5
RoNW (%)	3.8	37.8	70.4	51.8
RoCE (%)	-0.3	47.1	98.8	74.2

Stock data	
Particular	Amount
Market Capitalisation (₹ crore)	₹ 18563
Debt (FY18) (₹ crore)	₹ 272
Cash & Cash Equivalent (FY18) (₹ crore)	₹ 1263
EV (₹ crore)	₹ 17572
52 week H/L	1126 / 317
Equity capital (₹ crore)	₹ 39.1
Face value	₹ 2

Price performance (%)				
Return %	1M	3M	6M	12M
HEG	(6.8)	24.7	17.5	317.9
Graphite India	(13.0)	20.8	19.8	156.2

Share Price Chart



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ANALYST CERTIFICATION

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