Sharekhan
by BNP PARIBAS

Ratnamani Metals and Tubes

Expansion to fuel growth

Sector: Capital Goods
Company Update

	Change
Reco: **Buy**	↔
CMP: **Rs. 1,099**	
Price Target: **Rs. 1,225**	↑

↑ Upgrade ↔ No change ↓ Downgrade

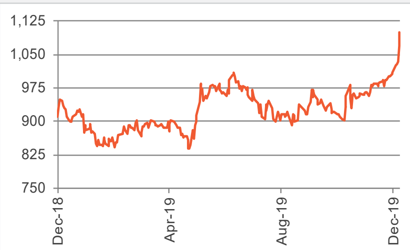
Company details

Market cap:	Rs. 5,135 cr
52-week high/low:	Rs. 1100/780
NSE volume: (No of shares)	0.2 lakh
BSE code:	520111
NSE code:	RATNAMANI
Sharekhan code:	RATNAMANI
Free float: (No of shares)	1.86 cr

Shareholding (%)

Promoters	60
FII	11
DII	10
Others	19

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	8.4	9.7	11.4	15.0
Relative to Sensex	7.0	2.3	5.5	-2.1

Sharekhan Research, Bloomberg

Ratnamani Metals & Tubes (RMTL) is expected to deliver healthy performance during Q3FY2020E on the back of healthy pace of order execution. Moreover, net profit growth is expected to see a significant jump during Q3FY2020E owing to reduced tax rate, as the company will opt for lower corporate tax rate of 25.2% (a one-time impact). Revenue visibility for the next 12-15 months remains strong, backed by robust order in-take (order book of Rs 1800 crore as of December 2019 and order intake of Rs 300 crore post that) as there has been a favourable demand outlook from key user industries such as the oil and gas sector and water usage. Management has reiterated its revenue and margin guidance of Rs. 2,600 crore-2,750 crore and 16-18%, respectively, for FY2020E. As input cost has been on an increasing trend off late, we believe it would have an adverse impact on gross margin in the near term, although the company has a mechanism to pass on enhanced input cost to its customers.

Revenue mix likely to move towards stainless steel (SS), a high-margin yielding segment: Management indicated that the expanded capacities are expected to commence commercial production during Q1FY2021E and Q2FY2021E. Revenue contribution from these expanded capacities is expected to accrue in FY2021E and beyond (asset turnover of 2x-2.5x at optimal utilisation). We believe SS revenue contribution to total revenue would move towards 45% over the next 3-4 years from the current level of 35%, which would result in enhancement of operating profitability given higher margin profile of SS pipes vis-à-vis. CS pipes. Moreover, coated CS pipes (higher demand from the oil and gas sector) command 100-200 bps higher margin compared to bare CS pipes, which are usually at 15-16%.

Our Call

Valuation: Healthy revenue visibility, reiterate Buy with a revised PT of Rs. 1,225: Based on management's interaction, we have fine tuned our numbers and revised upwards our earnings by 16% and 9% for FY2020E and FY2021E, respectively, to factor in the favourable impact of lower corporate tax rate (to be adopted from Q3FY2020E). We expect the company to report revenue and earnings CAGR of 5.7% and 13.7%, respectively, during FY2019-FY2021E. At the CMP, the stock is trading at 16.7x/15.7x its FY2020E/ FY2021E earnings. We remain Positive on RMTL, led by its strong balance sheet and ability to generate superior return ratios despite capacity expansion programmes (however, commissioning has been slightly delayed by a quarter or so). We reiterate our Buy rating on the stock with a revised PT of Rs. 1,225.

Key Risks

- Softness in demand offtake or delay in commissioning of plants might impact revenue growth momentum.
- Inability to take adequate and timely price hikes to mitigate adverse volatility in input cost material might impact margin profile.

Valuation Rs cr

Particulars	FY17	FY18	FY19	FY20E	FY21E
Revenue	1,412	1,767	2,755	2,611	3,079
OPM (%)	18.2	15.1	14.8	16.8	16.3
Adjusted PAT	144	152	253	308	327
% YoY growth	*(12.9)*	*5.1*	*66.6*	*21.6*	*6.2*
Adjusted EPS (Rs.)	30.9	32.5	54.1	65.8	69.9
P/E (x)	35.5	33.8	20.3	16.7	15.7
P/B (x)	4.3	3.9	3.4	2.9	2.5
EV/EBITDA (x)	19.6	19.6	11.9	10.5	8.9
RoNW (%)	13.0	12.2	17.9	18.6	16.9
RoCE (%)	18.2	17.7	25.1	24.4	22.3

Source: Company; Sharekhan Research

Strong order intake to help in achieving management's revenue guidance for FY2020E: The company had a healthy order in-take of Rs. 900 crore during the past nine months leading to a cumulative outstanding order book of Rs. 1,800 crore (including export order of $14.3 million for supply of bare CS pipes). Few of the recently bagged orders cumulating to Rs. 305 crore are i) Rs. 124 crore domestic order for supply of coated CS pipes in the oil and gas space; ii) Rs. 81 crore coated CS piping product in the oil and gas space; and iii) Rs. 100 crore order for water pipeline for exports to Middle East. Though orders in the nuclear power space are small in size, however during the year till-date, the company had bagged Rs. 100 crore order. The order book split continues to be tilted towards carbon steel as the demand outlook for stainless steel is yet to gain momentum. Management stated that in line with the company's strategy, the capacities are fully booked for the next 6-9 months. Of the newly bagged orders, domestic orders are expected to be completed between April-September 2020; and in case of exports, between May-June 2020.

Growth acceleration in FY2021E after decline in FY2020E: RMTL is expanding capacity in a calibrated manner, wherein it is focusing on keeping the revenue growth momentum as well as enhancing the margin profile. The company is adding 20,000 MT of capacity in the SS division and 1,20,000 MT of capacity in CS, which is expected to be commissioned by Q4FY2020E and Q1FY2021E, respectively (there has been a slight delay in commissioning). Of the 1,20,000 MT capacities, 40,000 MT of old capacities are being replaced (debottlenecking of capacities); hence, additional fresh capacity addition will only be 80,000 MT.

The expanded capacities in SS and CS are expected to commence commercial production during Q1FY2021E and Q2FY2021E. Major revenue contribution (management expects additional revenue at Rs. 500 crore-550 crore) from these two plants is expected to accrue in FY2021E and thereafter (2x-2.5x revenue at optimal utilisation).

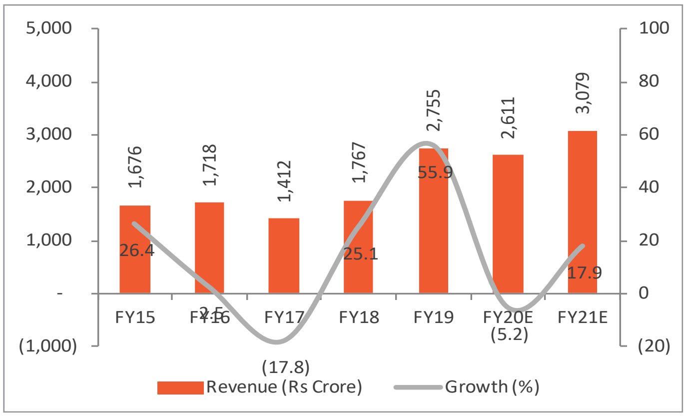
The company is expected to incur total capex of Rs. 550 crore-600 crore during FY2020E, of which the company has spent Rs. 400 crore in H1FY2020. The company is funding its capex programme by way of long-term borrowing of Rs. 300 crore (1.5+5 years) at a borrowing cost of less than 9% p.a. The company has raised debt of Rs. 150 crore for the expansion and the balance Rs. 150 crore is yet to be drawn. Capex outlined for FY2021E amounts to Rs. 40 crore-50 crore for debottlenecking of capacities in ERW. However, with expanded capacities coming fully on stream by FY2021E, working capital requirement is expected to increase by Rs. 150 crore or so.

Revenue mix likely to move towards SS, a high-margin yielding segment: RMTL is also converting part of its SS capacity into titanium tubes (largely to be supplied to Nuclear Power Corporation of India), which will be fully utilised in FY2020E and will help in increasing the contribution of value-added products in overall revenue and inching up the margin profile. Further, management has highlighted that it would manufacture import substitute products from its new SS plants from FY2021E, which are currently imported; and this augurs well for business visibility. Earlier, the revenue mix for SS:CS was 50:50, but over the past few years, the same has been more favourable for CS, wherein revenue contribution for CS increased to 60-65%, while that of SS reduced to by 40%-35%, however, the same is set to change again and move back to 45:55 revenue mix in a gradual manner post the scale up of utilisation levels at the expanded capacities over the next 3-4 years. As margins for SS pipes are higher than CS pipes (coated CS pipes command 200-300 bps higher margins fetched by bare CS pipes, which are usually in the range of 15-16%), the gradual improvement in contribution of SS revenue would help to enhance margin over a similar period.

Strong demand traction to help in scaling up utilisation levels of expanded capacities: Demand outlook remains strong because of increased bidding opportunities from the water segment (from Africa as well, however, RMTL has not focused on orders from the water segment), city-gas distribution (gas to every village, 9th and 10th round bidding expected soon), cross-country oil-gas pipeline, refinery upgradation, fertiliser plants and nuclear power (RMTL registered with Nuclear Power Corporation of India). The company has recently secured an order from an international nuclear plant. Demand outlook from the overseas market also looks strong in the oil and gas space, as new projects are coming up in Middle East, Thailand, Qatar, Abu Dhabi and Dangote.

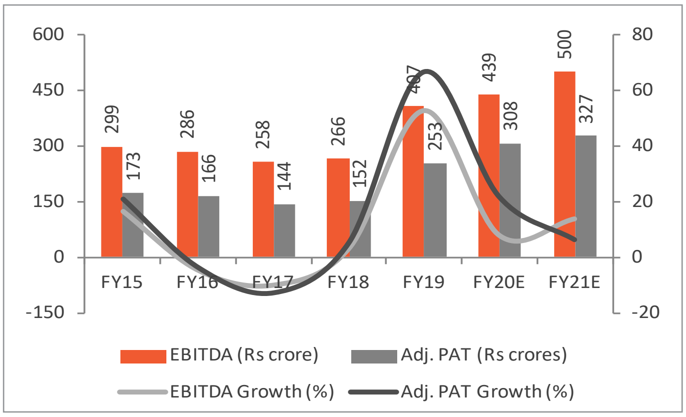
Financials in charts

Increased capacity to provide growth in FY2021E



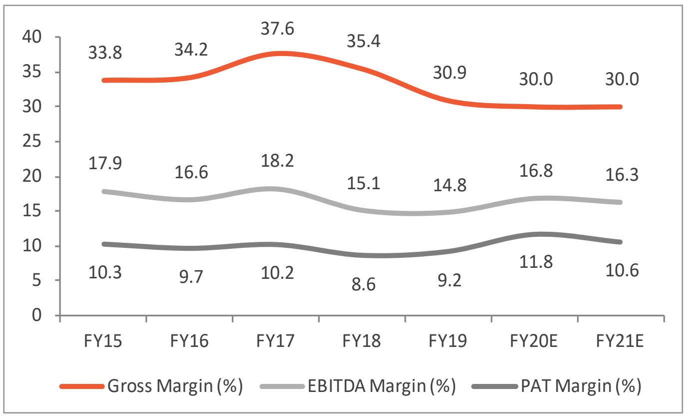
Source: Company, Sharekhan Research

Steady increase in profitability



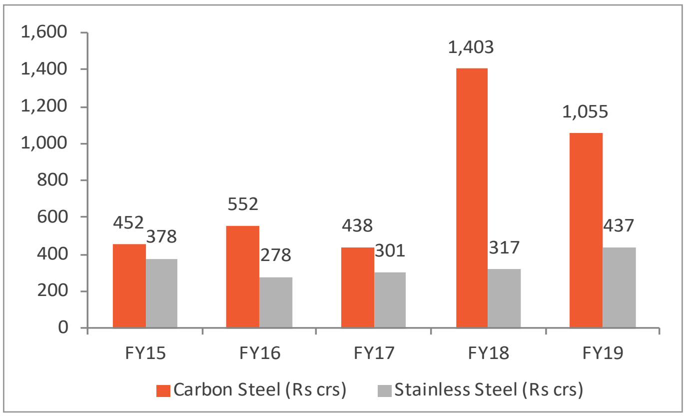
Source: Company, Sharekhan Research

Operates at a healthy margin profile



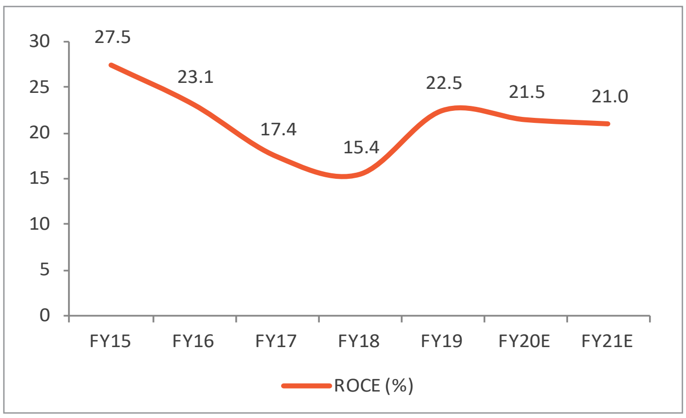
Source: Company, Sharekhan Research

Order book trend



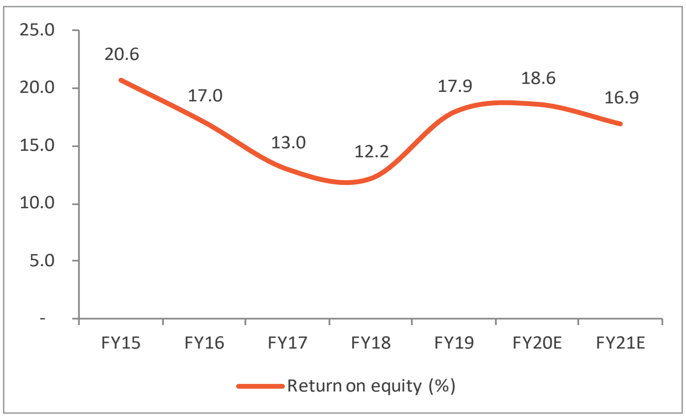
Source: Company, Sharekhan Research

RoCE to remain in excess of 20%



Source: Company, Sharekhan Research

RoE to remain in excess of 15%



Source: Company, Sharekhan Research

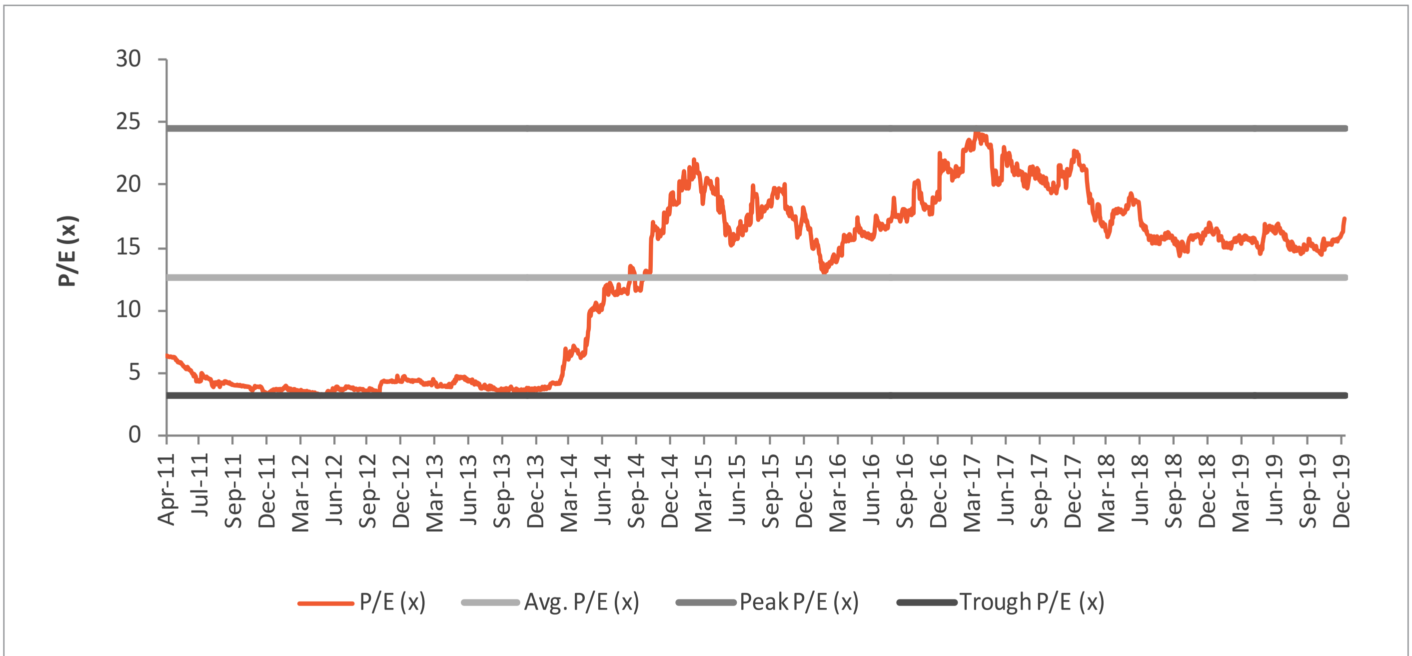
Outlook

Management reiterates FY2020E revenue and margin guidance, expansion to fuel growth momentum in FY2021E: Demand outlook remains strong because of increased bidding opportunities from the water segment, city-gas distribution, cross-country oil-gas pipeline, refinery upgradation, fertiliser plants and nuclear power. This is expected to enhance utilisation levels of the expanded capacities, which are to come on stream in Q4FY2020E and Q1FY2021E. Management has reiterated its revenue and margin guidance of Rs. 2,600 crore-2,750 crore and 16-18%, respectively, for FY2020E, as stated during Q2FY2020 results concall as demand outlook in the key user industry looks encouraging.

Valuation

Revenue visibility remains as order inflow continues, reiterate Buy with a revised PT of Rs. 1,225: Based on management's interaction, we have fine tuned our numbers and revised upwards our earnings by 16% and 9% for FY2020E and FY2021E, respectively, to factor in the favourable impact of lower corporate tax rate (to be adopted from Q3FY2020E). We expect the company to report revenue and earnings CAGR of 5.7% and 13.7%, respectively, during FY2019-FY2021E. At the CMP, the stock is trading at 16.7x/15.7x its FY2020E/FY2021E earnings. We remain Positive on RMTL, led by its strong balance sheet and ability to generate superior return ratios despite capacity expansion programmes (however, commissioning has been slightly delayed by a quarter or so). We reiterate our Buy rating on the stock with a revised PT of Rs. 1,225.

One-year forward P/E (x) band



Source: Company; Sharekhan Research

About company

Incorporated in 1983, RMTL is a key player in providing piping solutions in India. The company is the largest manufacturer of nickel alloy/stainless steel seamless and welded tube/pipe and titanium welded tubes in India. RMTL is also one of the leading manufacturers of carbon steel welded pipes (ERW, L-SAW and H-SAW), stainless steel/carbon steel pipes with three-layer PE/PP coating in India. The company has two manufacturing plants located in Gujarat and manufactures various products in stainless steel and carbon steel along with value-added products in each segment having capacity of 28,000 mtpa and 3,50,000 mtpa. The company caters to clients in refineries, petrochemicals, oil and gas, thermal power, nuclear power energy, fertilisers, water distribution, chemicals and aerospace.

Investment theme

RMTL is expected to maintain its growth momentum because of robust demand outlook coupled with healthy order book. The company is expanding capacities in a calibrated manner through a mix of internal accruals and debt. RMTL is a net debt-free company with stable margin profile (EBITDA margin ~15%, PAT margin ~7.5%) and healthy return ratios (RoCE>17.5% and RoE > 12.5%).

Key Risks

- Softness in demand offtake or delay in commissioning of plant might impact revenue growth momentum.
- Inability to take adequate and timely price hikes to mitigate adverse volatility in input cost material might impact margin profile.

Additional Data

Key management personnel

Prakash Misrimal Sanghvi	Executive Chairman
Jayantilal Mistrimal Sanghvi	Executive Director
Shantilal Mishrimal Sanghvi	Executive Director
Vimal Katta	Chief Financial Officer
Jigar Harshadkumar Shah	Company Secretary

Source: Bloomberg

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Sanghvi Prakash Mishrimal	15.38
2	Sanghvi Jayanti M	9.35
3	Sanghvi Jayantilal M	8.37
4	Nalanda India Fund Ltd	6.10
5	L&T Mutual Fund Trustee Ltd	4.98
6	Sanghvi Shantilal M	4.88
7	Sanghvi Chunilal M	3.60
8	Sanghvi Reshmidevi Prakash	3.35
9	Ssanghvi Chunilal Fojaji	3.29
10	L&T Investment Management	3.23

Source: Bloomberg

Sharekhan

by BNP PARIBAS

Know more about our products and services

For Private Circulation only

Disclaimer: This document has been prepared by Sharekhan Ltd. (SHAREKHAN) and is intended for use only by the person or entity to which it is addressed to. This Document may contain confidential and/or privileged material and is not for any type of circulation and any review, retransmission, or any other use is strictly prohibited. This Document is subject to changes without prior notice. This document does not constitute an offer to sell or solicitation for the purchase or sale of any financial instrument or as an official confirmation of any transaction. Though disseminated to all customers who are due to receive the same, not all customers may receive this report at the same time. SHAREKHAN will not treat recipients as customers by virtue of their receiving this report.

The information contained herein is obtained from publicly available data or other sources believed to be reliable and SHAREKHAN has not independently verified the accuracy and completeness of the said data and hence it should not be relied upon as such. While we would endeavour to update the information herein on reasonable basis, SHAREKHAN, its subsidiaries and associated companies, their directors and employees ("SHAREKHAN and affiliates") are under no obligation to update or keep the information current. Also, there may be regulatory, compliance, or other reasons that may prevent SHAREKHAN and affiliates from doing so. This document is prepared for assistance only and is not intended to be and must not alone be taken as the basis for an investment decision. Recipients of this report should also be aware that past performance is not necessarily a guide to future performance and value of investments can go down as well. The user assumes the entire risk of any use made of this information. Each recipient of this document should make such investigations as it deems necessary to arrive at an independent evaluation of an investment in the securities of companies referred to in this document (including the merits and risks involved), and should consult its own advisors to determine the merits and risks of such an investment. The investment discussed or views expressed may not be suitable for all investors. We do not undertake to advise you as to any change of our views. Affiliates of Sharekhan may have issued other reports that are inconsistent with and reach different conclusions from the information presented in this report.

This report is not directed or intended for distribution to, or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject SHAREKHAN and affiliates to any registration or licensing requirement within such jurisdiction. The securities described herein may or may not be eligible for sale in all jurisdictions or to certain category of investors. Persons in whose possession this document may come are required to inform themselves of and to observe such restriction.

The analyst certifies that the analyst has not dealt or traded directly or indirectly in securities of the company and that all of the views expressed in this document accurately reflect his or her personal views about the subject company or companies and its or their securities and do not necessarily reflect those of SHAREKHAN. The analyst further certifies that neither he or its associates or his relatives has any direct or indirect financial interest nor have actual or beneficial ownership of 1% or more in the securities of the company at the end of the month immediately preceding the date of publication of the research report nor have any material conflict of interest nor has served as officer, director or employee or engaged in market making activity of the company. Further, the analyst has also not been a part of the team which has managed or co-managed the public offerings of the company and no part of the analyst's compensation was, is or will be, directly or indirectly related to specific recommendations or views expressed in this document. Sharekhan Limited or its associates or analysts have not received any compensation for investment banking, merchant banking, brokerage services or any compensation or other benefits from the subject company or from third party in the past twelve months in connection with the research report.

Either SHAREKHAN or its affiliates or its directors or employees / representatives / clients or their relatives may have position(s), make market, act as principal or engage in transactions of purchase or sell of securities, from time to time or may be materially interested in any of the securities or related securities referred to in this report and they may have used the information set forth herein before publication. SHAREKHAN may from time to time solicit from, or perform investment banking, or other services for, any company mentioned herein. Without limiting any of the foregoing, in no event shall SHAREKHAN, any of its affiliates or any third party involved in, or related to, computing or compiling the information have any liability for any damages of any kind.

Compliance Officer: Mr. Joby John Meledan; Tel: 022-61150000; email id: compliance@sharekhan.com;

For any queries or grievances kindly email igc@sharekhan.com or contact: myaccount@sharekhan.com

Registered Office: Sharekhan Limited, 10th Floor, Beta Building, Lodha iThink Techno Campus, Off. JVLR, Opp. Kanjurmarg Railway Station, Kanjurmarg (East), Mumbai – 400042, Maharashtra. Tel: 022 - 61150000. Sharekhan Ltd.: SEBI Regn. Nos.: BSE / NSE / MSEI (CASH / F&O / CD) / MCX - Commodity: INZ000171337; DP: NSDL/CDSL-IN-DP-365-2018; PMS: INP000005786; Mutual Fund: ARN 20669; Research Analyst: INH000006183;