Sharekhan
by BNP PARIBAS

Ratnamani Metals & Tubes

Stable quarter, focus shifts to FY2022E

Sector: Capital Goods

Result Update

	Change
Reco: **Buy**	↔
CMP: **Rs. 994**	
Price Target: **Rs. 1,250**	↔

↑ Upgrade ↔ No change ↓ Downgrade

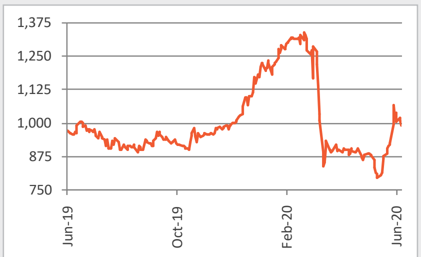
Company details

Market cap:	Rs. 4,648 cr
52-week high/low:	Rs. 1,383/715
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	10
DII	13
Others	17

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	15	-13	-1	2
Relative to Sensex	3	-29	18	16

Sharekhan Research, Bloomberg

Ratnamani Metals & Tubes Limited (RMTL) reported in-line revenue performance, while margins and net profit remained above our expectations. RMTL reported revenue decline of 12.1% y-o-y, in line with our modest estimates, owing to closure of plants during the last 10 days of March due to nationwide lockdown restrictions. Ease in input cost pressures along with revenue mix change led to 320 bps y-o-y improvement in gross margin to 33.3%. However, gross margin expansion was offset by 29.5% y-o-y and 31.2% y-o-y increase in employee expenses and other expenses, resulting in 265 bps y-o-y contraction in operating profit margin (OPM) to 15.3% (exceeding our estimates). The company's order book as on June 1, 2020, stood at Rs. 1,380 crore (down 7.5% y-o-y and 12% q-o-q). Management indicated that the pace of order inflows has been impacted owing to fall in crude price, delay in decision-making process for finalisation of orders, and deteriorating financial health of the government. Management believes that normalcy of order inflow is likely to return during Q4FY2021E. Further, Ministry of Petroleum and Natural Gas & Steel has recently stressed on increased usage of domestic steel for meeting requirements of the oil and gas sector to localisation of supply chain, which is expected to create around Rs. 8,000 crore opportunities for the piping industry in the next 8-12 months. Management has guided revenue in the range of Rs. 2,000 crore – Rs. 2,400 crore (implying a revenue decline of 7-23%) and margin in the range of 16-18%. Even though FY2021E is going to be a weak year, we assume sharp recovery in revenue growth would come back in FY2022E because of pent-up demand, higher order inflow on account of expanded capacity, and anticipated increase in government's spending on infrastructure schemes.

Key positives

- Cash and cash equivalents stood at Rs. 173 crore, up 22% y-o-y
- Management provided OPM guidance of 16-18% for FY2021E

Key negatives

- Muted revenue growth guidance of Rs. 2,000 crore – 2,400 crore for FY2020E

Our Call

Valuation: Maintain Buy with a PT of Rs. 1,250: We have lowered our earnings estimates for FY2021E/FY2022E to factor in FY2021E revenue growth guidance, slowdown in order inflows, and delay in commissioning of additional capacity. We remain Positive on RMTL, led by a strong balance sheet and its ability to generate superior return ratios despite capacity expansions. Further, new stainless steel plant would enable the company to manufacture import substitute products, which would provide business visibility with entering into new areas (i.e., oil exploration) in export markets. At the CMP, the stock is trading at 17x/14x its FY2021E/FY2022E earnings. We maintain our Buy rating on RMTL with a PT of Rs. 1,250.

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 have an impact on margins.

Valuation Rs cr

Particulars	FY18	FY19	FY20	FY21E	FY22E
Revenues	1,766.8	2,784.0	2,583.1	2,393.2	2,911.8
OPM (%)	15.1	15.6	16.4	16.3	16.9
Adjusted PAT	151.8	282.0	307.5	276.5	328.4
% YoY growth	5.1	85.7	9.0	-10.1	18.7
Adjusted EPS (Rs.)	32.5	60.4	65.8	59.2	70.3
P/E (x)	30.6	16.5	15.1	16.8	14.2
P/B (x)	3.6	3.1	2.7	2.4	2.1
EV/EBITDA (x)	17.8	10.5	11.1	11.1	8.6
RoNW (%)	12.2	19.9	19.0	15.1	15.6
RoCE (%)	15.4	24.4	20.3	16.0	17.9

Source: Company; Sharekhan estimates

Revenue in-line, margin above expectation: RMTL reported in-line revenue performance, while margin and net profit remained above our expectations. RMTL reported revenue decline of 12.1% y-o-y, in line with our modest estimates, owing to closure of its three plants during the last 10 days of March due to nationwide lockdown mandates. Weak revenue performance was due to 22.9% y-o-y decline in carbon steel revenue (contributed 64% of total revenue), while revenue in the stainless steel segment grew by 14.1% y-o-y. Ease in input cost pressures along with revenue mix change led to 320 bps y-o-y improvement in gross margin to 33.3%. However, gross margin expansion was offset by 29.5% y-o-y and 31.2% y-o-y increase in employee expenses and other expenses, resulting in 265 bps y-o-y contraction in OPM to 15.3%, exceeding our estimates. Net profit declined by 27% y-o-y to Rs. 67 crore, owing to lower operating profit coupled with higher interest expense (up by 2.7x y-o-y) and higher tax incidence of 25.3% as compared to 18.9% during Q4FY2019.

Pie of the carbon steel segment remains high both in revenue and order book: Revenue mix for carbon steel and stainless steel remained at 63:37 as against 71:29 during Q4FY2019. Revenue in the carbon steel segment declined by 23% y-o-y to Rs. 405 crore, owing to lower volume (down by 20% y-o-y to 60,663 MT) and lower realisation (down 3% y-o-y to Rs. 66,750/tonne). Revenue in the stainless steel segment grew by 14.1% y-o-y to Rs. 242 crore, led by higher volumes (up 22.9% y-o-y to 6,644 MT) though realisation remained soft (down by 7% y-o-y to Rs. 364,825/tonne).

The company's order book as on May 1, 2020, stood at Rs. 1,380 crore (down 7.5% y-o-y and 12% q-o-q). Order book in carbon steel stood at Rs. 720 crore (down 32% y-o-y/q-o-q), while order book in stainless steel stood at Rs. 660 crore (up 51% y-o-y and 28% q-o-q). The order book split between carbon steel and stainless steel stood at 52:48 as against 71:29 in Q4FY2019. The order book split between domestic and exports stood at 64:36 as compared to 82:18. The domestic order stood at Rs. 877 crore (down 29% y-o-y and 22% q-o-q), while export order stood at Rs. 503 crore (up by 92% y-o-y and 12% q-o-q).

Capacity expansion likely to be delayed due to travel restrictions: The company is adding 20,000 MT of capacity in the SS division and 1,20,000 MT of capacity in CS. Of the 120,000 MT capacities in CS, 40,000 MT of old capacities are being replaced; hence, additional fresh capacity addition will only be 80,000 MT. Management highlighted that there could be a further delay in the trial run of its expanded manufacturing plants, owing to non-arrival of technicians due to travel restrictions. Hence, the trial run is now expected in October-November against May-June earlier. Further, management has highlighted that it would manufacture import substitute products from its new SS plants, which are currently imported and augurs well for business visibility.

Pace of order inflows slowed down; Expect to pick up from FY2022E: The company's order book as on June 1, 2020, stood at Rs. 1,380 crore (down 7.5% y-o-y and 12% q-o-q), which is to be executed by December 2020. Management indicated that the pace of order inflows has slowed down in the wake of fall in crude price (lower capex by refineries), delay in decision making for finalisation of order, and deteriorating financial position of central and state governments owing to recent economic implications from the virus outbreak. However, the company would be able to secure orders worth Rs. 200 crore in the past two months despite a challenging environment. The company expects an order worth Rs. 180 crore in July 2020. Management believes that normalcy of order inflow is likely to return during Q4FY2021E as a number of orders are in the pipeline pending final discussion and a number of tenders are in the stage of finalisation. Further, Ministry of Petroleum and Natural Gas & Steel has stressed on increased usage of domestic steel for meeting requirements of the oil and gas sector, which is expected to create around Rs. 8,000 crore worth of opportunities for the piping industry in the next 8-12 months. Though we believe the current implications on the economy owing to the Coronavirus outbreak would defer government spending infrastructure projects (Jal se Nal, expansion of the National Gas Grid and among others) in the near-to-medium term, these spendings would come back in FY2022E once the situation settles down.

Results Rs cr

Particulars	Q4FY20	Q4FY19	YoY %	Q3FY20	QoQ %
Net sales	629.1	715.8	-12.1	756.0	-16.8
Operating expenses	533.1	587.6	-9.3	647.6	-17.7
EBIDTA	96.0	128.2	-25.1	108.4	-11.4
Depreciation	14.6	15.0	-2.7	15.2	-3.8
Other income	14.3	2.6	445.6	14.9	-4.1
Interest	5.6	2.1	172.5	5.9	-4.2
PBT	90.1	113.8	-20.8	102.3	-11.9
Tax	22.8	21.5	6.0	1.3	1639.8
PAT	67.3	92.3	-27.0	101.0	-33.3
EPS (Rs.)	14.4	19.8	-27.0	21.6	-33.3
Margins			**BPS**		**BPS**
EBITDA (%)	15.3	17.9	-265	14.3	92
PAT (%)	10.7	12.9	-219	13.4	-266

Source: Company; Sharekhan Research

Highlights of Q4FY2020 results concall

- **Q4FY2020 performance could have been better:** Management stated that the performance in Q4FY2020 could have been better as business during the last 10 days of March was impacted owing to nationwide shutdown as a result of COVID-19, which impacted dispatches as well. Even in Q1FY2021, performance is likely to remain impacted owing to lockdown and logistics issues. However, post lifting of the lockdown, the company has started operations in all its three facilities, which are currently operating at ~60% utilisation levels and expects it to operate at optimal utilisation in the next few months.
- **Slowdown in capex cycle to impact order intake:** The company has been witnessing slowdown in capex cycle as customers are trying to conserve cash in the current environment of COVID-19 led crisis. Moreover, bidding process and award of contracts are slightly taking longer time than before. All this has resulted in lower order intake (~Rs. 200 crore order received in the past two months) till date. Management is hopeful that tendering activities would show pickup in by Q3FY2020. The company has participated in tenders worth Rs. 400 crore-500 crore and expects Rs. 180 crore order inflow by the end of July 2020.
- **Low exposure to oil exploration business:** The crude oil crash has impacted the exploration business and is not likely to impact the company's business as it has no exposure to the exploration business. Moreover, projects for refining, city gas distribution, and cross-country pipeline among other seem to look healthy in the medium to long run.
- **To maximise plant utilisation:** Management stated that raw material availability is not a concern and production is not going to get impacted due to non-availability of raw materials. Moreover, the company is working in two shifts of 12 hours each instead of three shifts of eight hours so as to enhance plant productivity level considering the availability of manpower and to adhere to social distancing norms.
- **Stainless steel and carbon steel capacity expansion almost complete:** Management highlighted that capacity expansion in both stainless steel and carbon steel segments has been completed; however, commissioning of the same has been delayed owing to COVID-19, as technicians need to come from Germany and Italy to do trial production. Moreover, API approval is required for carbon steel, while domestic approvals such as BIS and others will be obtained. In stainless steel, no approvals are pending as such; however, trial production needs to be carried out by the vendor, post which handover of the plant will be taken.
- **Advantage in respect of Make in India, Vocal for Local and Atmanirbhar Bharat:** The current duty structure is 10-12% in case of imports. However, it is likely to increase to 25% in the near future as a number of new capacities are coming up. Moreover, anti-dumping duty on imports of stainless steel pipes from China is already in place. In respect of government motivating vocal for local initiative, central or state government owned PSUs need not invite international bidding for orders up to Rs. 200 crore, as these will be available for domestic players.
- **Performance to remain weak in FY2021, expects to pick up in FY2022E:** Management has guided that revenue will be Rs. 2,000 crore to Rs. 2,400 crore (implying a decline of 7-23%) owing to lower order intake, while OPM is likely to remain at 16-18% in FY2021E. Growth momentum is expected to pick up in FY2022E as the expanded capacities in both stainless steel and carbon steel will be available for full year and capex cycle environment will improve coupled with uncertainty over COVID-19 crisis being over. Employee cost is not expected to rise much despite capacity expansion as facilities are highly automated and existing manpower will be able to operate the plant.

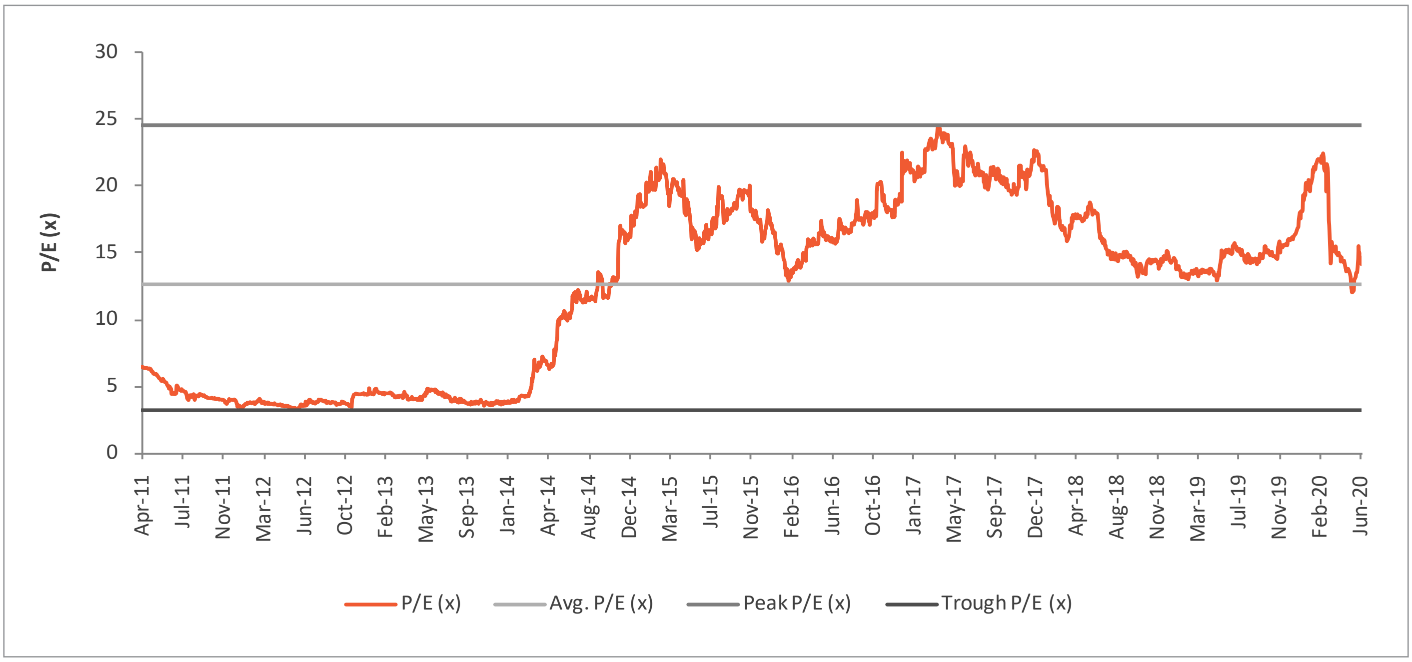
Outlook

Focus shifts to FY2022E: With the delay in decision making by customers, slowdown in order inflows (due to lower crude price, and deterioration of government's financial position), closure of plants for around 20 days in Q1FY2021 and deferment in expansion activity, management guided FY2021E revenue of Rs. 2,000 crore – Rs. 2,400 crore, implying a revenue decline of 23-7%. Further, management indicated the plants have been operating at 60-70% utilisation level owing to labour shortage, further rise in coronavirus cases in Gujarat, and challenges in supply chain. Though FY2021E is going to be a weak year, we assume sharp recovery in revenue growth would come back in FY2022E because of pent-up demand, higher order inflow on account of expanded capacity, and anticipated increase in government's spending on infrastructure schemes. On the margin front, management guided that EBITDA margin would remain at 16-18% in FY2021E, given its better product mix and cost-efficiency measures.

Valuation

Maintain Buy with a PT of Rs. 1,250: We have lowered our earnings estimates for FY2021E/FY2022E to factor in FY2021E revenue growth guidance, slowdown in order inflows, and delay in commissioning of additional capacity. We remain Positive on RMTL, led by a strong balance sheet and its ability to generate superior return ratios despite capacity expansions. Further, new stainless steel plant would enable the company to manufacture the import substitute products, which would provide business visibility with entering into new areas (i.e., oil exploration) in export markets. At the CMP, the stock is trading at 17x/14x its FY2021E/FY2022E earnings. We maintain our Buy rating on RMTL with a PT of Rs. 1,250.

One-year forward P/E (x) band



Source: Sharekhan Research

About company

Incorporated in 1983, RMTL is a key player in piping solutions in India. The company is the largest manufacturer of nickel alloy/stainless steel seamless and welded tubes/pipes 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. RMTL caters to clients in refineries, petrochemicals, oil and gas, thermal power, nuclear power energy, fertilisers, water distribution, chemicals, and aerospace, among others.

Investment theme

RMTL is expected to maintain its growth momentum because of robust demand outlook coupled with a 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

PrakashMisrimalSanghvi	Executive Chairman
JayantilalMistrimalSanghvi	Executive Director
ShantilalMishrimalSanghvi	Executive Director
Vimal Katta	Chief Financial Officer
JigarHarshadkumar Shah	Company Secretary

Source: Bloomberg

Top shareholders

Sr. No.	Holder Name	Holding (%)
1	Nalanda India Fund Ltd	6.10
2	L&T Mutual Fund Trustee Ltd	5.52
3	L&T Investment Management	5.52
4	Kotak Mahindra Asset Management	3.41
5	Nalanda India Equity Fund Ltd	3.13
6	Vaghela Divya	2.98
7	DSP Investment Managers Pvt Ltd	2.44
8	SAIF India V FII Holdings Ltd	1.67
9	BNP Paribas Asset Management India Pvt	0.42

Source: Bloomberg

Sharekhan

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