PROFITMART

RESEARCH REPORT

13th April 2021

IFGL REFRACTORIES LIMITED

BSE : IFGLEXPOR **Sector: ABRASIVES & REFRACTORIES** **BSE: 540774**

View - BUY

CMP : Rs. 348

Target Price: Rs 450 (In next 12 to 18 mths)

Suggested Buying Range (Between Rs 320to Rs 355)

BUSINESS BACKGROUND

IFGL Refractories Limited is a Kolkata-based Indian multinational company. Co was promoted by S. K. Bajoria Group (56.92%), India and Krosaki Harima Corporation (15.51%), Japan, a subsidiary of Nippon Steel Corporation, in 1993. IFGL manufactures specialised refractories and requisite operating systems for flow control in steel teeming and continuous casting of steel with facilities located in Kandla, Gujarat Rourkela, Odisha with a combined annual production capacity of 27,15,408 pieces of shaped refractories & 52,260 metric tonnes of unshaped refractories. IFGL is also setting up a new unit in Vizag, Andhra Pradesh to produce monolithics and precast shapes with an installed capacity of 48,000 MTPA. IFGL is a subsidiary of Bajoria Financial Services Private Limited, which holds a 51.21% stake in the company.

INVESTMENT HIGHLIGHTS

Steady Financial Performance for FY20 & Q3FY21 –

IFGL reported a steady set of FY20 numbers in a difficult year with net sales at Rs 917 crs as compared to a revenue of Rs 950 crs last year, with EBIDTA placed at Rs 92 crs from Rs 109 crs last year with the PAT placed at Rs 19.46 crs from Rs 50 crs. IFGL declared a dividend of 25% for FY20.

For IFGL for the first 9 months of FY21 Revenue was Rs 738.43 crs with EBIDTA at Rs 111 crs vs Rs 72 crs in 9 months last year with the PAT at Rs 68 crs vs Rs 34 crs in the same period last year

Established relationship with reputed clientele and diversified geographical presence –

Over the years, the company has been able to maintain a stable customer base in an intensely competitive market. The clientele of the company is diversified with the top five customers accounting for around 39% of the total revenue in FY2020. ICRA also notes that the reputed customer base leads to a low counterparty risk. Around 50-60% of the company's revenue is generated from export sales

On a consolidated basis, IFGL's operations are spread across China, Germany, India, the UK and the US through its various subsidiaries and step-down subsidiaries. The customer profile of the company is reputed and primarily comprises large steel producers, namely Tata Steel, SAIL, JSPL, ArcelorMittal etc

KEY DATA

FACE VALUE Rs	10.00
DIVD YIELD %	0.82
52 WK HI/LOW	324/64
NSE CODE	**IFGLEXPOR**
BSE CODE	**IFGLEXPOR**
MARKET CAP	RS 1100 CRS

SHAREHOLDING PATTERN

PROMOTERS	-	72%
BANKS, MFs & DIIs	-	17%
FIIs	-	%
PUBLIC	-	11%

KEY FUNDAMENTALS

YE	FY21	FY22	FY23
Rev Gr%	12	15	13
EBIDTA Gr%	76	15	13
PAT Gr%	381	28	25
EPS Gr%	381	28	25
EPS (Rs)	26.73	34.24	42.80
ROE %	11	13	14
ROCE %	12	14	15
P/E(x)		9	7

Long term Drivers for DHFL look good in view of the follow18

What are Refractories

Refractories are material having high melting points, with properties that make them suitable to act as heat- resisting barriers between high and low temperature zones. Refractories are inorganic non metallic material which can withstand high temperature without undergoing physical or chemical changes while remaining in contact with molten slag, metal and gases

Raw Materials

Principal raw materials used in the production of refractories are oxides of silicon, aluminum, magnesium, calcium and zirconium and somenon-oxide refractories like alumina, carbides, nitrides, borides, silicates and graphite

Types of Refractories

There are many types of refarctories like Isostatic Refractories, Slide Gate Refractories & Systems, Tube Changer Refractories & System, Purging System & Refractories, Cast Products & Zirconia Nozzles, Monolithics/Castable & Foundry Ceramics

Some Key Marquee Customers include –

ArcelorMittal NUCOR TATA

IFGL has strong net cash balance sheet and a strong cash flow generation business –

IFGL has Rs2.4bn net cash on its BS as at Dec’20 (accounting for >25% of current Mcap) and we see high probability of increased payouts through dividends and/or buyback.

IFGL has best cash flow generation track record in the industry (well ahead of MNC peers) with cumulative OCF/FCF of Rs 4.1bn & Rs 2.7bn over FY16-20 vs cumulative EBITDA of Rs 4.6bn which implies >100% EBITDA to OCF conversion

Market’s perception on low return ratios changing leading to re-rating –

IFGL has traditionally traded at large discount to other MNC refractory companies (Orient Refractories and Vesuvius) led mainly by low return ratios of IFGL which in turn were impacted due to large goodwill on the books

We see the discount narrowing led by lowering of impact of goodwill as IFGL has been writing down Rs 27 crs of goodwill every year (5 years already done and 5 more are left), large earnings growth aiding return ratios and better performance by IFGL vs MNC peers on most metrics from FY21 onwards

Corporate governance has very strong at IFGL which investors appreciate. While the reported ROE/ROCE are impacted by cash and goodwill, adjusted ratios are much better (with adjusted ROCE/ROIC at 22%/35% in FY21E) and are expected to keep improving as EBITDA improves and goodwill write-off builds

Strong Earnings growth expected ahead after 4-5 years of consolidation –

IFGL is expected to deliver a strong earnings growth with Consolidated EBITDA expected to double to Rs180-200cr (in FY22-23E) vs Rs90-100cr range of last 3-4 years

This will be led by several proactive steps taken by the management (capacity expansion at all domestic plants of Kandla/Orissa/Vizag and recruitment of industry veterans from peers at key positions), gain in market share in domestic refractory business through increased product offerings and better customer reach (already visible in 9MFY21 nos as IFGL has added several clients in both mini-mills and large mills in the last few years) and favourable demand scenario from end-user industry of steel globally

We also expect IFGL's overseas subs (all 100% owned) to do very well in next two years as those markets recover from Covid & where it benefits from spare capacity, solid client base and established product profile

Refractory Industry expected to benefit significantly over the next 2 years largely on the back of strong Steel and Cement demand ahead –

Much like the global refractories industry for glass, Indian suppliers have undergone a number of changes in recent years. Reducing specific consumption, the entrance of specialised producers and wider ranges of refractories available from leading producers have made the industry very competitive.

The improvement of refractory materials has played an important role in reducing specific refractory consumption per ton of glass produced and increased furnace performance. The latter factor has also led to much higher melting temperatures and allowed a much higher throughput of molten glass.

Conventional products are losing ground, while customer-driven product designs are gaining importance. Furthermore, there is increasing demand for total refractories solutions

The global Refractories market includes major Tier I and II suppliers like as Saint-Gobain (France), RHI Magnesita (Austria), Corning Incorporated (US), Morgan Advanced Materials (UK), and Shinagawa Refractories (Japan). These suppliers have their manufacturing facilities spread across various countries across Asia Pacific, Europe, North America, South America, and Middle East & Africa. COVID-19 has impacted their businesses as well.

These players have announced the suspension of production due to the lowered demand, supply chain bottlenecks, and to protect the safety of their employees in the US, France, Germany, Italy, and Spain during the COVID-19 pandemic. As a result, the demand for refractories is expected to decline in 2020. Manufacturers are likely to adjust production to prevent bottlenecks and plan production according to demand from tier 1 manufacturers.

Growing urbanization and industrialization, especially in emerging economies such as India and China, has led to significant investment in the construction of residential and commercial buildings. According to the Global Construction Perspective and Oxford Economics, the global construction market will grow by 85% to USD 15.55 trillion worldwide by 2030, with three countries China, India and the US accounting for 57% of the global growth

China is one of the fastest-growing economies; rising travel demand requires constant development of railways and roadways in the country. This has also boosted the growth of the automotive industry in China

The increased pace of infrastructure development in these emerging countries has led to an increase in the construction of residential and commercial buildings, which is expected to drive the demand for refractories in the iron & steel and cement industries. Increasing construction activities in emerging economies are also expected to drive the glass industry, which, in turn, will drive the refractories demand.

The refractories market is highly dependent on the iron & steel industry, which covers around 60% of the global market

The rest 40% share is covered by end-use industries such as power generation, cement, glass, non-ferrous metal, petrochemical, chemical, and paper & pulp.

The global Refractories market is estimated to be USD 23.2 billion in 2020 and is projected to reach USD 27.4 billion by 2025, at a CAGR of 3.4% from 2020 to 2025.

The market is witnessing moderate growth, owing to increasing application, technological advancements, and growing demand for these refractories in the Asia Pacific and Europe. Refractories are largely used in the iron & steel industry. The increasing use of refractories and the rising construction activities is driving the refractories market

In 2020 world steel forecasts that steel demand will contract by 2.4%, dropping to 1,725.1 Mt due to the COVID-19 pandemic. In 2021 steel demand is expected to recover to 1,795.1 Mt, an increase of 4.1% over 2020

The post lockdown recovery in steel demand in the rest of the world has been stronger than was earlier expected

India had implemented one of the strictest lockdown in world which disrupted demand of steel for a short period of time. However, as lockdown started easing, the country has witnessed a strong bounce back in demand led by increased manufacturing activities across all the consuming sectors

Hence, although steel demand may decrease in 2020 but demand for steel in India in 2021 is expected to be extremely strong as Government has unveiled various infrastructure investments, production linked incentives, support for rural people through infra development in rural areas complemented by restarting of construction activities across India & recovery of the auto industry

The Government has also unveiled the multimillion-dollar National Infrastructure Pipeline (NIP), with projects spread across 18 states over the next five years

India needs to spend about $1.4 trillion on infrastructure to become a $5 trillion economy by FY25

This fresh investment in power, railways, and water, coupled with renewed interest in the automobile sector is bound to bring in fresh demand for steel

AATMANIRBHAR BHARAT is the vision of the Government to make India a self-reliant nation. PM Modi has promoted “Vocal about Local” campaign which promotes Indian Companies to lead India to become self reliant

Alhe the increased capital expenditure for infrastructure projects in the UnionBudget 2021-22 will push the demand for steel in the country

IFGL enjoys a strong balance sheet with huge scalability potential going ahead –

IFGL runs a strong business model covering multiple product segments across multi locations with a efficient working capital management while it continues to invest on a sustained basis largely from its internal accruals.

We expect that going ahead overall bottomline growth in the next 3 years starting FY20 onwards should easily increase at a CAGR of 15-18% and with capex funded largely from internal cash flows.

What is important is that CFO have remained positive since 2017 till date while borrowings have reduced every year from 84 crs in FY17 to 65 crs in FY20 and to Rs 42 crs as on Sept 2020

IFGL has Rs 2.4bn net cash on its BS as at Dec’20 (accounting for >25% of current Mcap) and we see high probability of increased payouts through dividends and/or buyback

Business Outlook & Stock Valuation –

On a rough cut basis, in FY21E, Topline is expected to touch Rs 1028 crs, followed by Rs 1182 crs in FY22E and Rs 1336 crs in FY23E.

On the bottomline level we expect the company to record a PAT of Rs 94 crs in FY21E which is expected to bounce back to Rs 120 crs in FY22 and Rs 150 crs in FY23.

Thus on a conservative basis, IFGL should record a EPS of Rs 27 for FY21E. For FY22E and FY23E our expectation is that earnings traction for IFGL would continue to be strong wherein we expect a EPS of Rs 34 and Rs 43 respectively.

The iron & steel industry will continue to lead the Refractories market, accounting for a share of 60% of the overall market, in 2019 terms of value. This was due to the increasing demand for infrastructure development and mounting demand for consumer goods such as automobiles. The increasing preference for high-cost, high-performance refractories is driven by the need to improve the quality of life, health & environment, and shift to clean, alternative sources of manufacturing

Asia Pacific accounted for the largest share of the Refractories market in 2020. Factors such as the rapidly increasing consumption of refractories in the iron & steel, power generation cement, and glass industries in countries such as China, Japan, India, South korea and Australia have led to an increased demand for Refractories in the Asia Pacific region

The company management is confident of improving EBIDTA margins in going ahead via operational efficiency and better product mix.

Looking at IFGL’s steady financial track record, strong product domain and dominant market share and strong promoters we expect the stock to get re rated in future.

Hence we believe that the IFGL stock should be purchased at the current price for a price target of around Rs 450 over the next 18 months.

FINANCIALS

For the Year Ended March RsCrs	FY19	FY20	FY21	FY22	FY23
Net Sales	950.41	917.35	1028.00	1182.20	1335.89
EBIDTA	108.70	91.58	160.92	184.42	208.40
EBIDTA %	11.44	9.98	15.65	15.60	15.60
Interest	3.68	3.61	3.00	3.00	3.00
Depreciation	46.02	48.34	50.00	53.00	56.00
Non Operational Other Income	5.02	10.95	17.00	15.00	15.00
Profit Before Tax	64.04	50.58	124.92	143.42	164.40
Profit After Tax	50.46	19.46	93.69	120.00	150.00
Diluted EPS (Rs)	14.40	5.55	26.73	34.24	42.80
Equity Capital	35.05	35.05	35.05	35.05	35.05
Reserves	758.61	772.90	846.59	945.59	1070.59
Borrowings	84.57	48.50	35.00	35.00	37.00
Gross Block	728.00	761.00	811.00	851.00	901.00
Investments	45.53	94.00	95.00	100.00	120.00

Source Company our Estimates

KEY CONCERNS

Any sharp rise in raw material costs can impact IFGL’s financials adversely.

Also any negative development in the export markets could also impact IFGL’s financials negatively

Disclaimer –