

May 18, 2016

Gandhi Special Tubes (GANSPE) ₹ 262

Outlook turns positive, bullishness reloaded...

- In Q4FY16, Gandhi Special Tubes (GST) reported a robust performance with sales growing 20% YoY after four quarters of continuous de-growth YoY. It largely tracked the 31% growth witnessed in sales of M&HCV during the quarter
- EBITDA margins improved 530 bps YoY to 29.2% in Q4FY16 primarily on the back of lower raw material and power expenses
- PAT in Q4FY16 was at ₹ 6.2 crore vs. ₹ 3.1 crore in Q4FY15 on account of higher margins and lower tax incidence (tax rate at 12%)
- Our interaction with the management suggests the inventory in the system has been exhausted with sales volume expected to grow ~20% in FY17E. All end user demand segments like M&HCV, tractor and refrigerator are witnessing good demand traction

Product segment catering to core industrial activity

GST is a manufacturer of small diameter seamless and welded steel tubes, which are used in automotive, hydraulics, refrigeration (condenser tubes) and other engineering services. In the automotive space, the company's products find application as fuel injection tubes in the M&HCV segment. GST is an OEM approved tier-2 supplier of seamless tubes, which are eventually used by Tata Motors, Ashok Leyland and M&M among others. In hydraulics, the company's products are used in material (bulk) handling equipment, which are used for construction & mining purposes. In the hydraulics segment, GST's clientele includes Larsen & Toubro, BEML, Bhel and Bosch Rexroth India, among others. Welded steel tubes find application in refrigeration and automobile (fuel lines, oil lines & air brake lines) segments.

Small diameter seamless tubes - dominant player, high margins business

Seamless tubes contributed a healthy 70% to overall sales (FY15 sales of ₹ 70 crore; total gross sales of ₹ 98 crore). It is a key revenue contributor for GST, which has on a consistent basis commanded a healthy 60%+ share in total sales. Out of ₹ 70 crore, ~₹ 35 crore (i.e. 33% of total sales) is realised from fuel injection tubes for CVs, in which GST enjoys a virtual monopoly and enjoys healthy 30%+ EBITDA margins in this segment.

M&HCV cycle on the uptick; GST seems to be gaining steam

The domestic M&HCV cycle is in an uptick with industry reporting robust growth numbers in FY15 & FY16. M&HCV sales growth in FY15 was at 17.4% YoY, which further grew 28.2%YoY in FY16. Sales are largely tracking the M&HCV cycle, with sales growing 10% YoY in FY15 and largely flat in FY16. Sales were flat in FY16 largely on account of a drop in realisation with underlying volume growth in tandem with M&HCV segment growth. Going forward, with sentiments upbeat in the M&HCV space on the back of a pick-up in industrial activity and anticipated growth in tractor sales, GST is on a robust growth journey ahead.

Lean balance sheet, high dividend payout to continue!

GST has a lean balance sheet with net cash & investments of ₹ 85 crore (FY16). With minimal capex requirements, GST has a robust dividend payout (~60%) with FY16 dividend per share at ₹ 7.5/share. Going forward, we expect the trend to continue with GST providing a dividend yield of ~4%. Working capital cycle has significantly improved with net working capital days coming in at 120 days in FY16 (155 days in FY15). We expect sales and PAT to grow at a CAGR of 17.5% and 21.2%, respectively, in FY16-18E. We have valued GST at ₹ 315, i.e. 17x P/E (0.8x PEG) on FY18E EPS of ₹ 18.5/share and upgrade GST to **BUY** rating.

Rating matrix		
Rating	:	Buy
Target	:	₹ 315
Target Period	:	12-18 months
Potential Upside	:	20%

What's changed?	
Target	Changed from ₹ 265 to ₹ 315
EPS FY17E	Changed from ₹ 16.6 to ₹ 15.8
EPS FY18E	Introduced at ₹ 18.5
Rating	Changed from Hold to Buy

Key financials				
₹ crore	FY15	FY16	FY17E	FY18E
Net Sales	86.8	87.2	104.7	120.4
EBITDA	23.3	26.9	33.9	40.0
Net Profit	15.8	18.5	23.3	27.2
EPS (₹)	10.7	12.6	15.8	18.5

Valuation summary				
	FY15	FY16	FY17E	FY18E
P/E	24.5	20.8	16.5	14.2
Target P/E	29.4	25.0	19.9	17.0
EV / EBITDA	13.6	11.2	8.9	7.4
P/BV	2.4	2.3	2.3	2.2
RoNW	9.8	11.2	13.6	15.4
RoCE	13.6	14.6	19.5	22.0
ROIC	18.4	25.1	30.9	36.4

Stock data	
Stock Data	
Market Capitalization	₹ 385 crore
Total Debt (FY16)	₹ 0 crore
Cash and Cash Equivalent (FY16)	₹ 85 crore
EV	₹ 300 crore
52 week H/L	300 / 198
Equity Capital	7.4
Face Value	₹ 5
MF Holding (%)	0.1
FII Holding (%)	3.8

Stock data				
	1M	3M	6M	12M
Gandhi Special Tubes	11.9	9.5	(7.9)	(12.5)
Maharashtra Seamless	(2.8)	45.6	32.2	(3.3)
Ratnamani Metals & Tubes	3.1	23.7	(10.7)	(20.9)

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Company Analysis

Gandhi Special Tubes (GST) is a manufacturer of small diameter seamless and welded steel tubes, which are used in automotive, hydraulics, refrigeration and other engineering services. The company commenced operations at its Halol (Gujarat) Plant in 1988 and was set up in technical collaboration with Benteler (Germany). In the automotive space, GST's products find application as fuel injection tubes in the M&HCV segment. In hydraulics, the company's products are used in material (bulk) handling equipment. Welded steel tubes find application in the refrigeration and automobile (fuel lines, oil lines) segments.

Topline directly linked to M&HCV sales

By virtue of seamless tubes contributing ~65% of the overall topline of GST, the topline can be easily traced to the performance of the M&HCV segment domestically.

GST also owns wind power capacity of ~5.3 MW in India with wind plants based out of Gujarat and Maharashtra. In Gujarat, the generated wind power is consumed captively while in Maharashtra, the generated wind power is sold to the state grid

Exhibit 1: GST sales vs. M&HCV sales

Year	GST Total Sales (₹ crore)	Seamless Tubes Sales (₹ crore)	Passenger Car Sales (units)	Utility Vehicle Sales (units)	Multi Purpose Vehicle Sales (units)	PV Sales (units)	M&HCV Sales (units)	LCV Sales (units)	CV Sales (Units)	YoY Growth (%)	YoY Growth (%)
FY07	60.1	41.9	1269263	224705	84421	1578389	294579	223136	517715	GST	MHCV
FY08	76.1	57.2	1414214	251220	101871	1767305	296317	252859	549176	26.7	0.6
FY09	56.2	33.4	1551990	228676	107787	1888453	201072	226505	427577	-26.2	-32.1
FY10	77.7	44.2	1970046	275564	151869	2397479	265369	312361	577730	38.2	32.0
FY11	92.3	59.3	2410374	320032	215940	2946346	351220	406508	757728	18.8	32.4
FY12	106.5	73.4	2531459	369972	236777	3138208	377711	524046	901757	15.5	7.5
FY13	95.9	64.4	2421277	564085	239067	3224429	288233	585025	873258	-9.9	-23.7
FY14	83.5	59.9	2334889	558670	192335	3085894	224432	485372	709804	-12.9	-22.1
FY15	92.0	69.6	2419818	629160	173599	3222577	263407	438480	701887	10.1	17.4
FY16	91.2	NA	2557532	705385	180650	3443567	337565	449828	787393	-0.8	28.2

Source: Company, SIAM, ICICIdirect.com Research

GST witnessed healthy growth in topline when the M&HCV segment was performing well domestically. Topline grew at a CAGR of 23.8% in FY09-12 (FY12: ₹ 106.5 crore, FY09: ₹ 56.2 crore) when M&HCV sales grew at a CAGR of 23.4% in the corresponding period (FY12 sales at ~3.8 lakh units, FY09 sales at ~2.0 lakh units). Sales at GST were flat in FY16 despite 28% YoY volume growth in the M&HCV segment, largely on account of a drop in realisation with underlying volume growth in tandem with M&HCV segment growth.

With the last three quarters of muted sales, the growth momentum seems to have returned at GST with sales growing 20% YoY in Q4FY16.

Exhibit 2: Sales trend (GST vs. M&HCV Sales)

Quarter	GST Total Sales (₹ crore)	M&HCV Sales Volume (Units)	GST YoY %	M&HCV YoY %
Q1FY15	23.2	57260	5.7	-4.7
Q2FY15	27.1	61811	16.5	10.6
Q3FY15	23.1	63781	35.6	43
Q4FY15	18.6	80550	-13.2	26
Q1FY16	25.6	70415	10.7	23
Q2FY16	22.8	85566	-14.6	38
Q3FY16	21.0	76399	-8.0	20
Q4FY16	21.9	105185	20.1	31

Source: Company, SIAM, ICICIdirect.com Research

Benefits of safeguard duty starting to fade away; interim relief provided!

In August 2014, the Customs department (Government of India) imposed a safeguard duty on imports of seamless steel tubes and pipes in India.

It is to be implemented in three phases:-

- Phase 1; 20% ad valorem; for August 2014 – August 2015;
- Phase 2; 10% ad valorem; for August 2015 – August 2016 and
- Phase 3; 5% ad valorem; for the period August 2016 – February 2017;

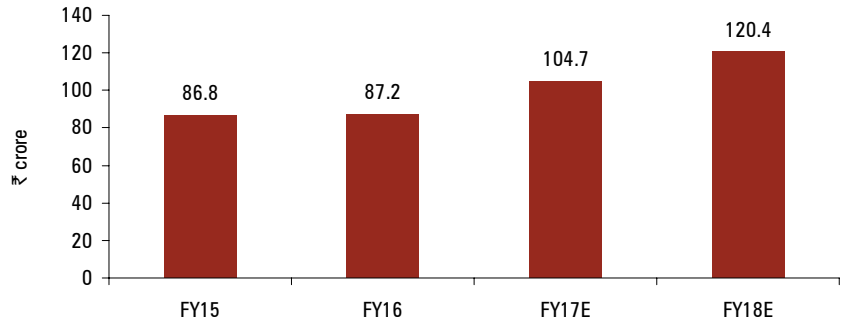
Thus, as we stand today, the benefits of safeguard duty have started to diminish. However, in a recent release (May 2016) by the customs department; the government has placed a provisional anti dumping duty on imports of seamless tubes and pipe into India for six months. This will act as a cushion for domestic players, including Gandhi Special Tubes.

Safeguard duty is imposed on imports of seamless tubes and pipes from developed countries and China

Sales to grow at 17.5% CAGR in FY16-18E

We expect GST to clock revenue growth of 17.5% CAGR in FY16-18E primarily on a pick-up in industrial activity domestically.

Exhibit 3: Sales trend

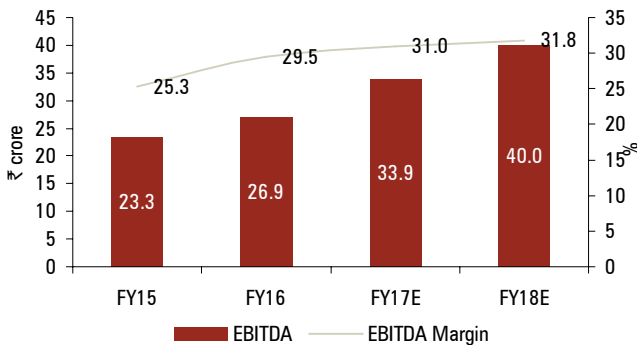


Source: Company, ICICIdirect.com Research

Margin expansion to drive EBITDA & PAT, going forward

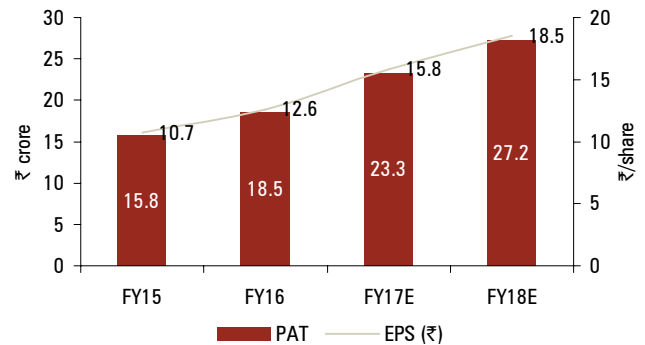
We expect the EBITDA to grow at a healthy rate in FY16-18E on account of expansion in margins by 230 bps over FY16-18E, albeit on a lower base. EBITDA margins came in at 29.5% in FY16 vs. 25.3% in FY15 due to lower raw material and power costs. We expect GST to clock EBITDA of ₹ 40.0 crore in FY18E (EBITDA margins at 31.8%). PAT is also expected to grow at a CAGR of 21.2% in FY16-18E with FY18E PAT expected at ₹ 27.2 crore (EPS at ₹ 18.5/share).

Exhibit 4: EBITDA & EBITDA margins trend



Source: Company, ICICIdirect.com Research

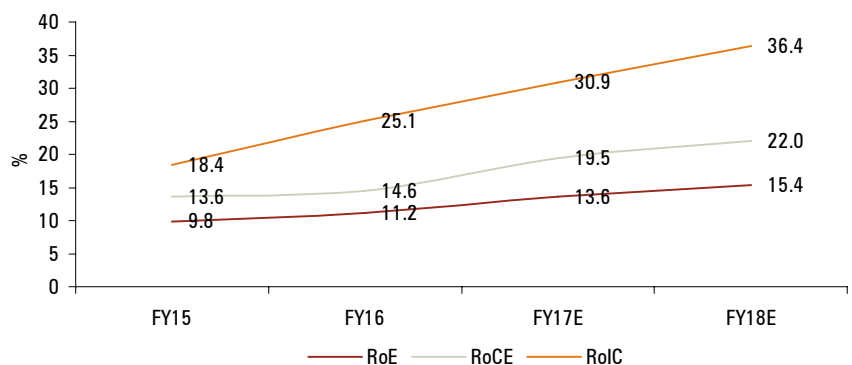
Exhibit 5: PAT & EPS trend



Source: Company, ICICIdirect.com Research

Return ratios had taken a hit due to the subdued demand scenario and consequent de-growth in the topline at GST. The return ratios (RoCE, RoE) have declined from a peak of 29.5%, 22.1% in FY11 to about 13.6%, 9.8%, respectively, in FY15. However, with the revival of the M&HCV cycle on the back of enhanced industrial activity, we expect return ratios to improve at GST with RoCE, RoE in FY18E expected at 22.0% and 15.4%, respectively

Exhibit 6: Return ratios set to improve over FY16-18E



Source: Company, ICICIdirect.com Research

Outlook and valuation

GST has a lean balance sheet with net cash & investments of ₹ 85 crore (FY16). With minimal capex requirements, GST has a robust dividend payout (~60%) with FY16 dividend per share at ₹ 7.5/share. Going forward, we expect the trend to continue with GST providing a dividend yield of ~4%. The working capital cycle has significantly improved with net working capital days coming in at 120 days in FY16 (155 days in FY15). We expect sales and PAT to grow at a CAGR of 17.5% and 21.2%, respectively, in FY16-18E. We have valued GST at ₹ 315, i.e. 17x P/E (0.8x PEG) on FY18E EPS of ₹ 18.5/share and upgrade the stock to **BUY** rating.

Exhibit 7: What's changed??

Particulars	FY17E			FY18E		
	Old	New	% Change	Old	New	% Change
Sales	105.7	109.5	3.6	NA	125.9	NA
EBITDA	34.8	33.9	(2.6)	NA	40.0	NA
EBITDA Margin %	32.9	31.0	-196 bps	NA	31.8	NA
PAT	24.4	23.3	(4.5)	NA	27.2	NA
EPS	16.6	15.8	(4.5)	NA	18.5	NA

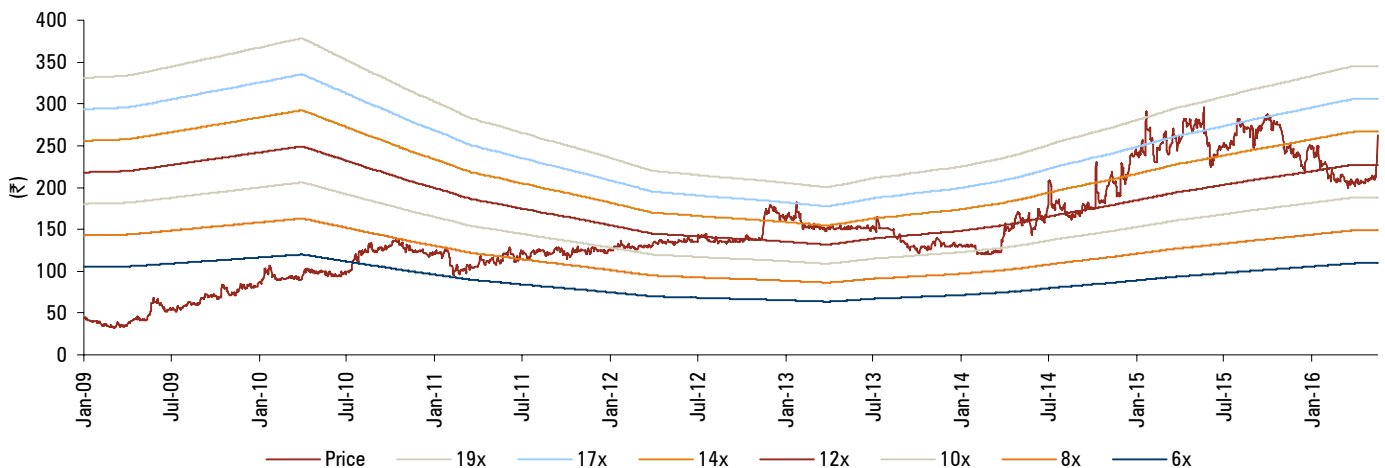
Source: Company, ICICIdirect.com Research

Exhibit 8: Valuation Summary

	Sales (₹ cr)	Growth (%)	PAT (₹)	Growth (%)	PE (x)	EV/EBITDA (x)	RoNW (%)	RoCE (%)
FY15	92.0	10.1	15.8	-9.0	24.5	13.6	9.8	13.6
FY16	91.2	-0.8	18.5	17.5	20.8	11.2	11.2	14.6
FY17E	109.5	20.0	23.3	25.8	16.5	8.9	13.6	19.5
FY18E	125.9	15.0	27.2	16.7	14.2	7.4	15.4	22.0

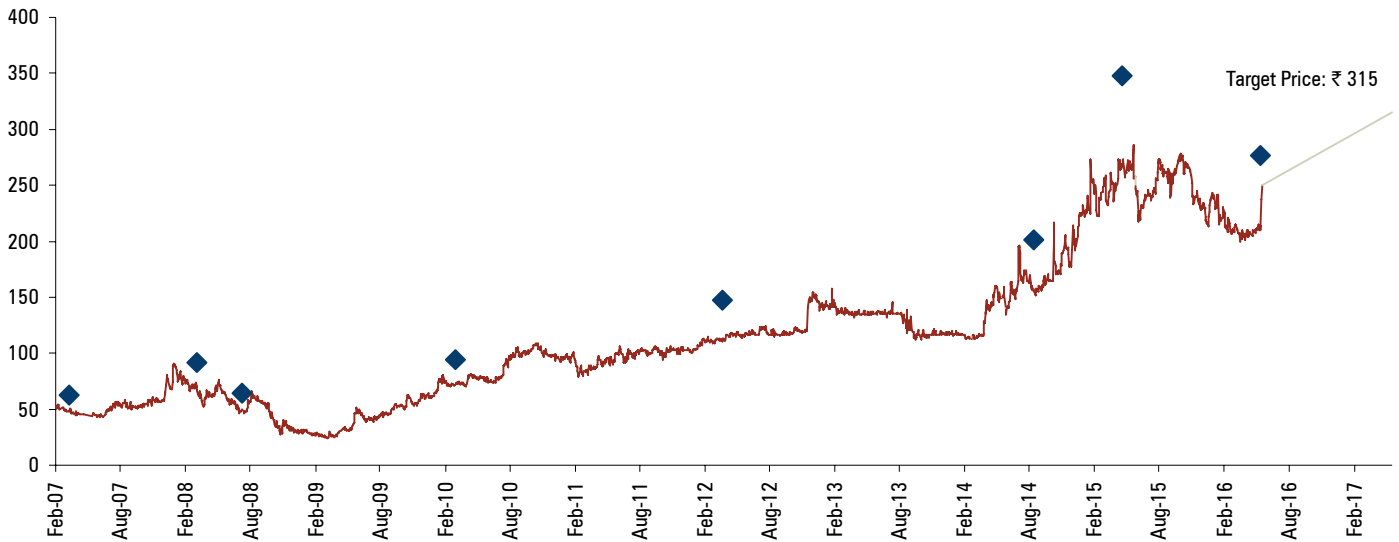
Source: Company, ICICIdirect.com Research

Exhibit 9: Two year forward P/E (GST currently trading at 14.2x)



Source: Reuters, ICICIdirect.com Research

Company snapshot



Source: Bloomberg, Company, ICICIdirect.com Research

Key events

Date/Year	Event
2007	Reports sales of ₹ 60.2 crore, limited due to capacity constraints. GST had undertaken a capex amounting to ₹ 12.8 crore in FY07, out of ₹ 12.6 crore was towards installation of plant and machinery. The entire capex was funded by the company's internal cash accruals
2008	Further undertakes capex amounting to ₹ 18.4 crore, out of which ₹ 3.3 crore was spent towards new factory building, ₹ 8.7 crore towards plant & machinery and ₹ 6.3 crore towards windmill. The entire capex was funded out of the company's internal cash accruals
2008	Closes down its Pune plant with effect from July 25, 2008. The said plant was engaged mainly in assembly of components transferred from the company's Halol plant and supplying the finished products to customers in nearby area. After completion of the expansion project at Halol, the company now had sufficient resources at its Halol Plant to undertake assembly and supply of products to all its customers from the said plant itself
2010	On occasion of silver jubilee year, board of directors of GST declares special interim dividend of ₹ 2.5 per equity shares of ₹ 5/- each. Regular interim dividend of ₹ 2.5 per equity share was also declared
2012	Stops production of refrigeration condenser coils; as business was highly seasonal. The company embarks upon the new capex plan amounting ₹ 40 crore. GST's planned capex includes capex of ₹ 10 crore for building, ₹ 20 crore for plant & machinery and ₹ 10 crore for new corporate office in Mumbai
2014	In August, Customs department (Government of India) imposes a safeguard duty on imports of seamless steel tubes and pipes of external diameter not exceeding 273.1 mm (outer diameter) on imports from developed countries and China. GST would also be a key beneficiary of the said judgement
2015	Reports subdued Q4FY15 with full year FY15 PAT at ₹ 15.8 crore, down 8.7% YoY. The interaction with the management suggests near exhaustion of inventory pertaining to company's product profile in the user market with turnaround in sales expected in Q2FY16
2016	Reports robust Q4FY16 with sales growing 20% YoY and EBITDA margins coming in at 29%. Full year FY16, Sales, EBITDA & PAT were at ₹ 91 crore, ₹ 27 crore & ₹ 19 crore, respectively. The company has also declared and distributed a dividend of ₹ 7.5/share for FY16

Source: Company, ICICIdirect.com Research

Top 10 Shareholders

Rank	Name	Latest Filing Date	% O/S	Position (m)	Change (m)
1	Gandhi (Manhar G)	31-Mar-16	15.9	2.3	0.0
2	Gandhi (Bhupatrai G)	31-Mar-16	14.9	2.2	0.0
3	Gandhi (Jayesh M)	31-Mar-16	7.9	1.2	0.0
4	Gandhi (Manoj B)	31-Mar-16	7.5	1.1	0.0
5	Gandhi (Bharati M)	31-Mar-16	5.3	0.8	0.0
6	B M Gandhi Investment Company Pvt. Ltd.	31-Mar-16	3.8	0.6	0.0
7	Gandhi Finance Company Pvt. Ltd.	31-Mar-16	3.5	0.5	0.0
8	Gandhi (Chandra B)	31-Mar-16	3.2	0.5	0.0
9	Gandhi (Gopi J)	31-Mar-16	3.1	0.5	0.0
10	Gandhi (Jigna M)	31-Mar-16	3.1	0.4	0.0

Source: Reuters, ICICIdirect.com Research

Shareholding Pattern

(in %)	Mar-15	Jun-15	Sep-15	Dec-15	Mar-16
Promoter	73.3	73.3	73.3	73.3	73.3
FII	2.1	2.5	3.1	3.1	3.8
DII	0.1	0.1	0.1	0.1	0.1
Others	24.6	24.2	23.6	23.6	22.9

Recent Activity

Buys				Sells			
Investor name	Value	Shares		Investor name	Value	Shares	
PineBridge Invnt. Asset Mgmt Co. (India) Pvt. Ltd.	0.58 Million	0.19 Million		No data provided			

Source: Reuters, ICICIdirect.com Research

Financial summary

Profit and loss statement		₹ Crore			
(Year-end March)	FY15	FY16	FY17E	FY18E	
Net Sales	86.8	87.2	104.7	120.4	
Other Operating Income	5.1	4.0	4.8	5.5	
Total Operating Income	92.0	91.2	109.5	125.9	
Growth (%)	10.1	-0.8	20.0	15.0	
Raw Material Expenses	33.9	33.3	39.4	45.3	
Employee Expenses	5.8	6.3	7.3	8.4	
Power & Fuel Expense	14.2	9.0	10.9	12.6	
Other Operating Expense	14.8	15.8	17.9	19.5	
Total Operating Expenditure	68.7	64.3	75.6	85.8	
EBITDA	23.3	26.9	33.9	40.0	
Growth (%)	-10.8	15.6	25.9	18.2	
Depreciation	4.9	4.8	5.1	5.1	
Interest	0.0	0.0	0.0	0.0	
Other Income	4.5	3.0	5.9	5.6	
PBT	22.8	25.2	34.8	40.6	
Exceptional Item	0.0	0.0	0.0	0.0	
Total Tax	7.1	6.7	11.5	13.4	
PAT	15.8	18.5	23.3	27.2	
Growth (%)	-9.0	17.5	25.8	16.7	
EPS (₹)	10.7	12.6	15.8	18.5	

Source: Company, ICICIdirect.com Research

Cash flow statement		₹ Crore			
(Year-end March)	FY15	FY16	FY17E	FY18E	
Profit after Tax	15.8	18.5	23.3	27.2	
Add: Depreciation	4.9	4.8	5.1	5.1	
(Inc)/dec in Current Assets	-1.0	7.2	-9.7	-6.9	
Inc/(dec) in CL and Provisions	-1.5	0.7	1.5	1.1	
Others	0.0	0.0	0.0	0.0	
CF from operating activities	18.2	31.1	20.1	26.5	
(Inc)/dec in Investments	-1.7	-16.3	0.0	-3.0	
(Inc)/dec in Fixed Assets	-3.5	-1.1	-2.0	-2.0	
Others	0.6	0.3	0.0	0.0	
CF from investing activities	-4.6	-17.1	-2.0	-5.0	
Issue/(Buy back) of Equity	0.0	0.0	0.0	0.0	
Inc/(dec) in loan funds	0.0	0.0	0.0	0.0	
Dividend paid & dividend tax	-13.3	-13.2	-17.6	-21.2	
Inc/(dec) in Share Cap	-0.4	0.4	0.0	0.0	
Others	0.0	0.0	0.0	0.0	
CF from financing activities	-13.7	-12.8	-17.6	-21.2	
Net Cash flow	-0.1	1.2	0.5	0.3	
Opening Cash	1.8	1.8	3.0	3.4	
Closing Cash	1.8	3.0	3.4	3.8	

Source: Company, ICICIdirect.com Research

Balance sheet		₹ Crore			
(Year-end March)	FY15	FY16	FY17E	FY18E	
Liabilities					
Equity Capital	7.4	7.4	7.4	7.4	
Reserve and Surplus	152.7	158.0	163.7	169.7	
Total Shareholders funds	160.1	165.4	171.0	177.1	
Total Debt	0.0	0.0	0.0	0.0	
Deferred Tax Liability	7.1	7.4	7.4	7.4	
Minority Interest / Others	0.0	0.0	0.0	0.0	
Total Liabilities	167.2	172.8	178.5	184.5	
Assets					
Gross Block	130.2	131.3	133.3	135.3	
Less: Acc Depreciation	67.4	72.2	77.3	82.4	
Net Block	62.7	59.1	56.0	52.9	
Capital WIP	0.0	0.0	0.0	0.0	
Total Fixed Assets	62.7	59.1	56.0	52.9	
Investments	65.3	81.6	81.6	84.6	
Inventory	27.8	17.0	22.9	26.4	
Debtors	12.7	16.1	20.1	23.1	
Loans and Advances	2.8	2.9	2.7	3.1	
Other Current Assets	0.5	0.5	0.5	0.6	
Cash	2.1	3.0	3.4	3.8	
Total Current Assets	45.8	39.5	49.7	57.0	
Current Liabilities	3.7	4.4	5.7	6.6	
Provisions	3.0	3.0	3.2	3.4	
Current Liabilities & Prov	6.7	7.4	8.9	10.0	
Net Current Assets	39.2	32.1	40.8	46.9	
Others Assets	0.0	0.0	0.0	0.0	
Application of Funds	167.2	172.8	178.5	184.5	

Source: Company, ICICIdirect.com Research

Key ratios					
(Year-end March)	FY15	FY16	FY17E	FY18E	
Per share data (₹)					
EPS	10.7	12.6	15.8	18.5	
Cash EPS	14.1	15.8	19.3	22.0	
BV	108.9	112.5	116.4	120.5	
DPS	7.5	7.5	10.0	12.0	
Cash Per Share (Incl Invst)	45.9	57.5	57.9	60.1	
Operating Ratios (%)					
EBITDA Margin	25.3	29.5	31.0	31.8	
PAT Margin	17.1	20.3	21.3	21.6	
Inventory days	117.0	71.1	80.0	80.0	
Debtor days	53.2	67.5	70.0	70.0	
Creditor days	15.4	18.4	20.0	20.0	
Return Ratios (%)					
RoE	9.8	11.2	13.6	15.4	
RoCE	13.6	14.6	19.5	22.0	
RoIC	18.4	25.1	30.9	36.4	
Valuation Ratios (x)					
P/E	24.5	20.8	16.5	14.2	
EV / EBITDA	13.6	11.2	8.9	7.4	
EV / Net Sales	3.7	3.4	2.9	2.5	
Market Cap / Sales	4.4	4.4	3.7	3.2	
Price to Book Value	2.4	2.3	2.3	2.2	
Solvency Ratios					
Debt/EBITDA	0.0	0.0	0.0	0.0	
Debt / Equity	0.0	0.0	0.0	0.0	
Current Ratio	6.5	4.9	5.2	5.3	
Quick Ratio	2.4	2.6	2.6	2.7	

Source: Company, ICICIdirect.com Research

RATING RATIONALE

ICICIdirect.com endeavours to provide objective opinions and recommendations. ICICIdirect.com assigns ratings to its stocks according to their notional target price vs. current market price and then categorises them as Strong Buy, Buy, Hold and Sell. The performance horizon is two years unless specified and the notional target price is defined as the analysts' valuation for a stock.

Strong Buy: >15%/20% for large caps/midcaps, respectively, with high conviction;
Buy: >10%/15% for large caps/midcaps, respectively;
Hold: Up to +/-10%;
Sell: -10% or more;



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