Company Note

ICICI direct.com Research
It's Advice, Not Adventure

Rating Matrix

Rating :	Unrated

YoY growth (%)

(YoY Growth)	FY14	FY15	FY16E	FY17E
Total Op. Income (%)	14.5	9.5	4.7	5.9
EBITDA (%)	127.1	58.6	7.1	9.1
Profit after tax (%)	LP	114.4	21.0	14.8
EPS (%)	LP	114.4	21.0	14.8

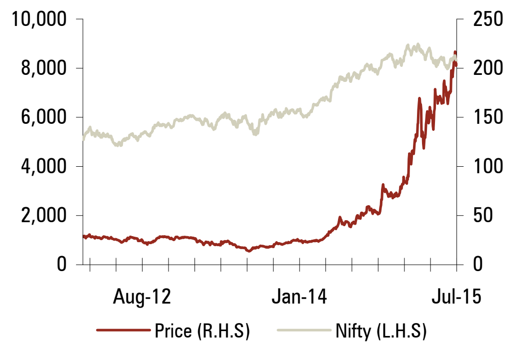
Current multiple

	FY14	FY15	FY16E	FY17E
P/E (x)	21.0	9.8	8.1	7.0
EV / EBITDA (x)	10.3	6.4	6.0	5.3
Book Value (₹)	56.7	73.8	95.5	121.0
P/BV (x)	3.6	2.8	2.1	1.7
RoNW (%)	17.2	28.3	26.4	24.0
RoCE (%)	13.2	21.4	21.0	20.9

Stock Data

Bloomberg/Reuters Code	SRIK IN/SRIK.BO
Sensex	27,586
Average volumes	365,784
Market Cap (₹ crore)	811.2
52 week H/L	222/37
Equity Capital (Rs crore)	39.8
Promoter's Stake (%)	50.8
FII Holding (%)	1.1
DII Holding (%)	0.8

Price movement



Research Analysts

Dewang Sanghavi
dewang.sanghavi@icicisecurities.com

Srikalahasthi Pipes (LANIND)

₹ 204

Opportunity in pipeline!

Srikalahasthi Pipes (SPL), formerly known as Lanco Industries (LIL), is a South-India based integrated pipe manufacturing company engaged in supply of ductile iron (DI) pipes. While on a pan-India basis, SPL commands 13% market share in the DI pipes segment, in its focussed markets i.e. south and west zone (Andhra Pradesh, Telangana, Karnataka, Kerala, Tamil Nada, Maharashtra and Goa) SPL's market share is as high as ~75%. Given the strong push by the government on improving water supply and sewerage infrastructure coupled with leadership position in southern and western Indian market (75% share in south and west zone), SPL is well placed to cater to the rising demand. On the back of rising demand from the user industry segment, the company has recently augmented its DI pipe capacity from 180 KTPA to 225 KTPA. Driven by higher production, we expect SPL's topline to grow at a CAGR of 5.3% in FY15-17E and PAT to report a CAGR of 17.9% during the same period led by margin expansion (18.0% in FY17E vs. 17.1% in FY15).

Improvement in water infrastructure to perk up demand

As per the 2011 Census, currently only 31% of India's population has access to improved sanitation. In order to provide a better habitat facility, continued emphasis is being given by the government on improving the water supply and sewerage infrastructure. Priority attention has been given to the state government and centre sponsored programmes such as JNNURM, NRDWP and UIDSSM. Under the Twelfth Five Year Plan (2012-17), ~₹ 2500 billion has been allocated for development of water supply and sanitation infrastructure. As fortunes of ductile iron pipes are closely linked to investment in water supply infrastructure, with its presence in the DI pipes segment, SPL is likely to be the key beneficiary.

Backward integration to aid in maintaining healthy margins…

SPL has taken various initiatives to reduce its operating cost, which has resulted in margin expansion. One of the key backward integration initiatives was setting up a sinter plant (commenced operation from January 2013), which resulted in usage of low cost iron ore fines instead of lump ores. Subsequently EBITDA margins improved from 3.9% in Q3FY13 to 11.8% in Q4FY13 and further to 18.8% in Q4FY15.

On strong footing, well placed to cater to rising demand…

On the back of a healthy demand scenario for key user industries, we believe SPL is well placed to cater to the rising demand. Driven by healthy volume growth, we expect SPL's topline, EBITDA and PAT to grow at a CAGR of 5.3%, 8.1% and 17.9%, respectively, during FY15-17E.

Exhibit 1: Valuation Metrics

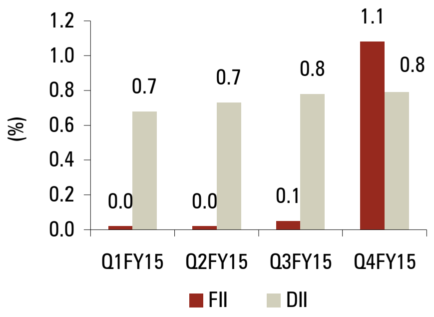
₹ crore	FY13	FY14	FY15	FY16E	FY17E
Total Operating Income (₹ crore)	863.9	989.4	1,083.6	1,134.4	1,201.5
EBITDA (₹ crore)	51.5	117.0	185.6	198.8	216.8
Profit after tax (₹ crore)	(13.1)	38.7	83.0	100.4	115.3
EPS (₹)	(3.3)	9.7	20.9	25.2	29.0
P/E (x)	NA	21.0	9.8	8.1	7.0
Price / Book (x)	4.2	3.6	2.8	2.1	1.7
EV/EBITDA (x)	24.6	10.3	6.4	6.0	5.3
RoCE (%)	4.4	13.2	21.4	21.0	20.9
RoE (%)	(6.8)	17.2	28.3	26.4	24.0

Source: Company, ICICIdirect.com Research

Shareholding pattern (Q4FY14)

Shareholder	Holding (%)
Promoters	50.8
Institutional investors (FII/DII)	1.9
General public	47.4

FII & DII holding trend (%)



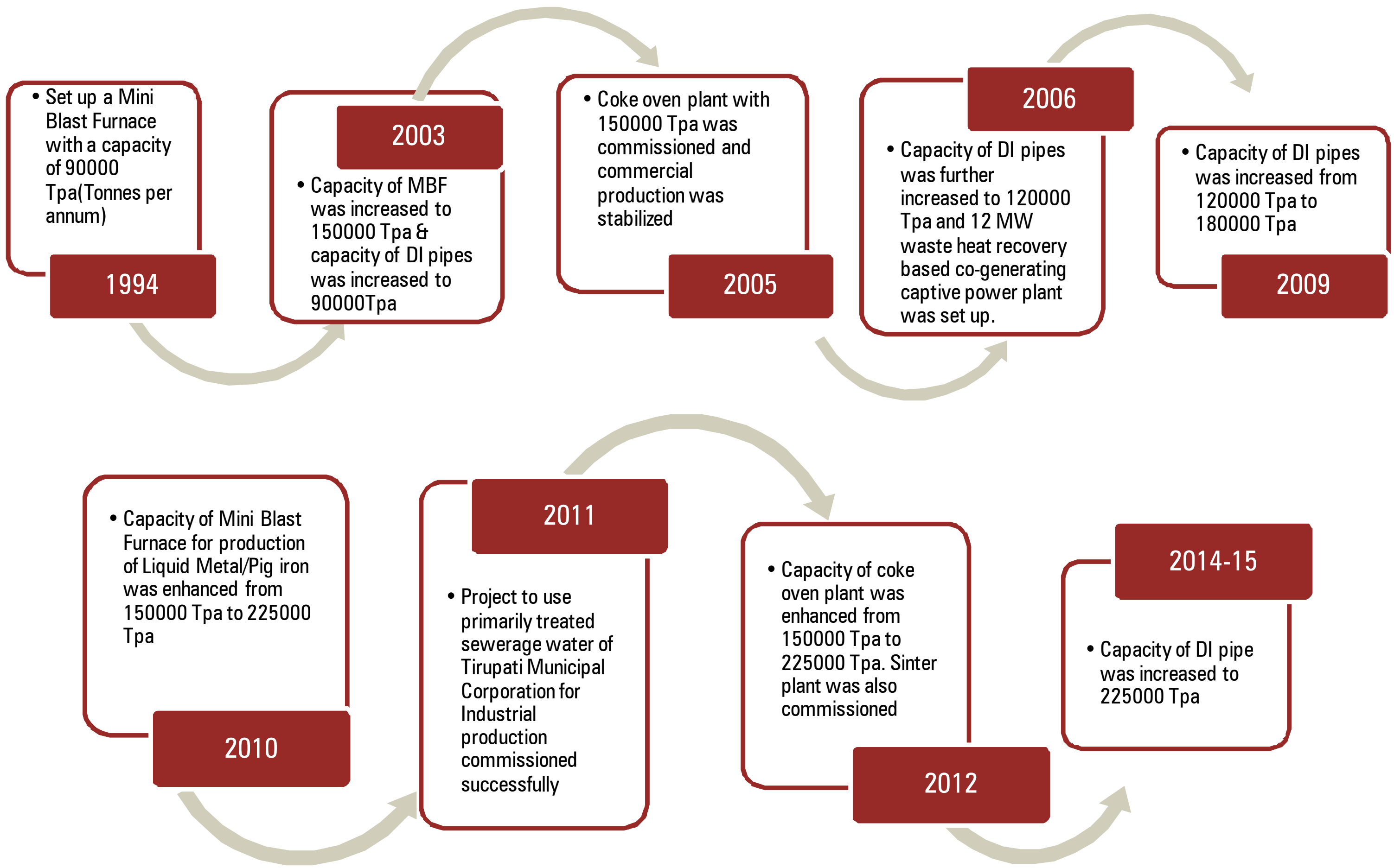
Company background

Srikalahasthi Pipes (SPL), formerly known as Lanco Industries (LIL), was established in 1991 by Lanco group of companies to manufacture pig iron using Korf (German) Technology. The company commenced its operations in 1994 by setting up a mini blast furnace (MBF) with an installed capacity of 90000 tonne per annum (TPA).

In March 2002, Electrosteel Castings (ECL) entered into a strategic alliance with LIL and Lanco Kalahasthi Castings (LKCL) by acquiring 46.43% and 48.89% stake in the companies, respectively. ECL also infused fresh funds into LIL by way of equity participation and also re-modelled the financial structure. On account of close synergies, LKCL got merged with LIL (with effect from April 1, 2003). SPL is currently engaged in manufacturing and supply of ductile iron (DI) pipes. In addition to DI pipes, SPL also produces low ash metallurgical (LAM) coke and power for captive consumption in its integrated complex. SPL is also engaged in manufacturing and selling slag cement and producing pig iron through the mini blast furnace route.

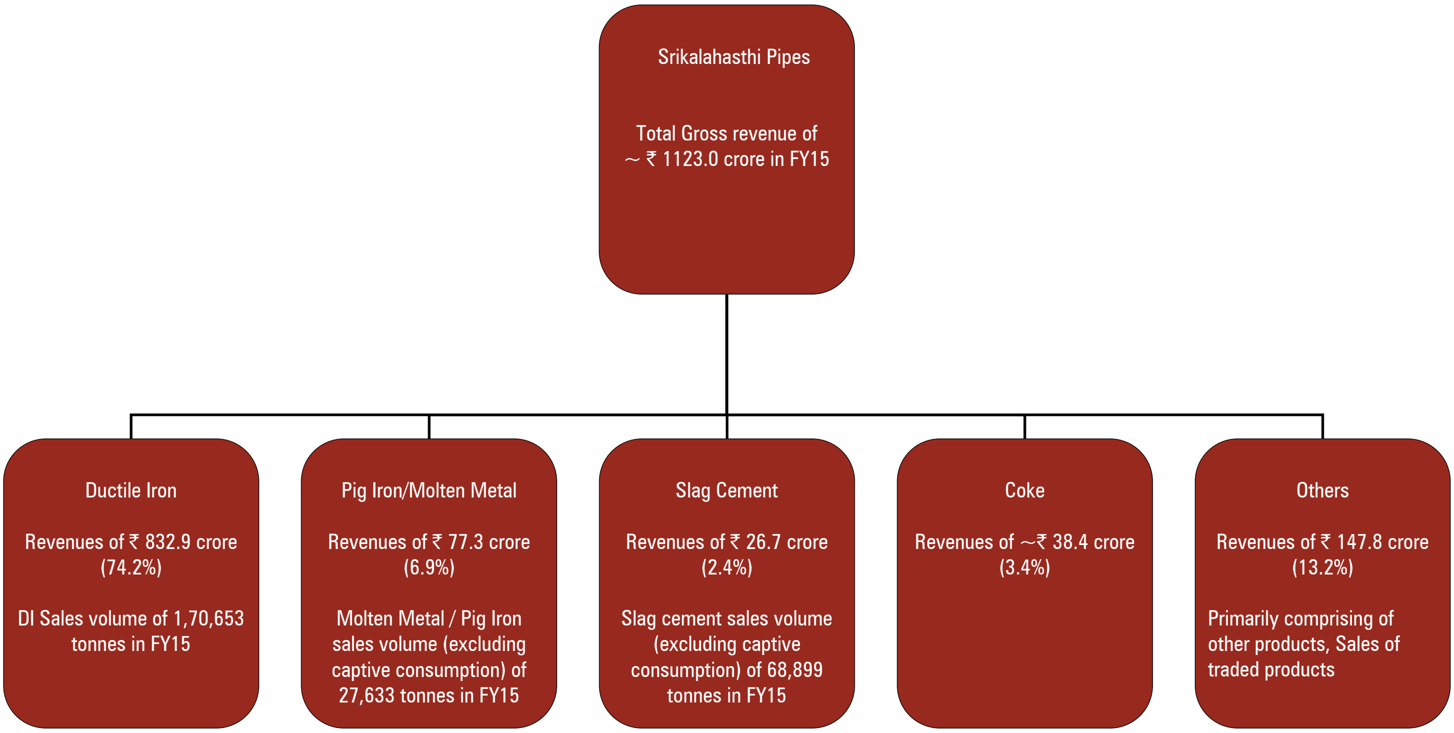
SPL's client list includes marquee names such as Larsen & Toubro, Hyderabad Metro (HMWSSB), VA Tech Wabag, Sriram EPC, etc.

Exhibit 2: Srikalahasthi Pipes – Timeline of company milestone



Source: Company, ICICIdirect.com Research

Exhibit 3: Srikalahasthi Pipes - Topline break-up for FY15 (Gross)



Source: Company, ICICIdirect.com Research,

Exhibit 4: Srikalahasthi Pipes – Overview of operations

	Capacity & Description
Ductile Iron (DI) pipes	Capacity – 225000 tonnes per annum, DI pipes is the core product of SPL. DI pipes aids in efficient & safe transportation of water. Product size range is from 100 mm to 1100 mm diameter
Pig Iron	Mini blast furnace has a capacity of 275000 tonnes per annum. Majority of pig iron produce by SPL is used for captive consumption with balance is sold to nearby foundries & steel factories
Sinter Plant	Capacity – 500000 tonnes per annum, in place of high cost lump ores, low cost iron ore fines are used at feed for sinter plant which results substantial cost saving
Coke oven Plant	Capacity – 225000 tonnes per annum, aids in converting coal into coke
Power	Two power plants with capacity of 14.5 MW, SPL generates power from waste heat gases of coke oven plant and Mini blast furnace
Slag cement	Capacity – 90000 tonnes per annum, 20% of cement produced is used in captive consumption for inner coating of DI pipes

Source: Company, ICICIdirect.com Research

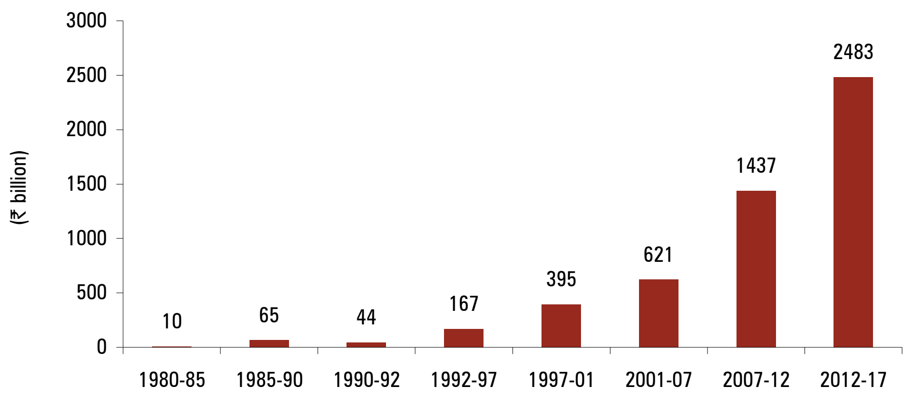
Investment Rationale

Investment in water, sanitation infrastructure to perk up demand for DI pipes

Fortunes of ductile iron (DI) pipes are closely linked to investment in water and sanitation infrastructure. DI pipes are widely recognised as the industry standard for modern water & wastewater system and find application in water transportation & sewage management. As per the 2011 Census, currently only 31% of India's population has access to improved sanitation. To provide a better habitat, continued emphasis is given by the government on improving the water supply and sewerage infrastructure. Priority attention has been given to the state government and Centre sponsored programmes such as JNNURM, NRDWP & UIDSSM. Under the Twelfth Five Year Plan (2012-17), ₹ 2483 billion has been allocated for development of water supply & sanitation infrastructure (up 73% compared to the Eleventh Five Year Plan).

Furthermore, in the recent Budget, tax-free bonds were introduced for projects in the irrigation sector. As DI pipes also find application in the irrigation sector, we believe the demand push given to the irrigation segment will provide a further boost to demand for DI pipes. Subsequently, over a medium to longer term horizon, the demand for DI pipes is likely to grow at a healthy CAGR of ~15-17%. SPL's current order book in DI pipes stands at about 1,70,000 MT (equivalent to about 10 months production).

Exhibit 5: Plan wise allocation to water supply & sanitation (in ₹ billion)



Source: Company PPT's, ICICIdirect.com Research,

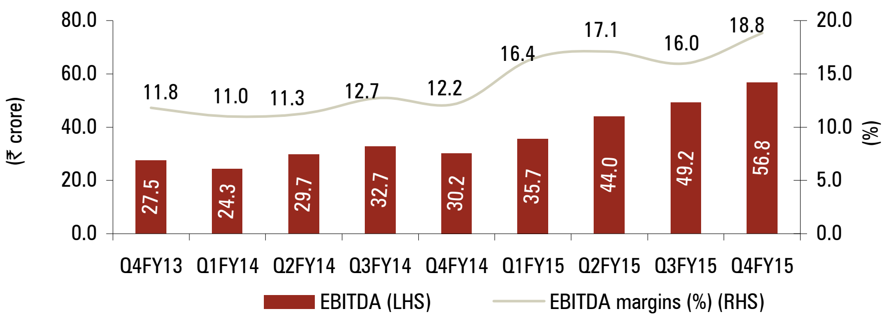
DI pipes preferred over CI pipes and mild steel

DI pipes have been increasingly replacing cast iron (CI) pipes and mild steel pipes in most applications, which augur well for DI pipe manufacturers. This is primarily due to the qualitative and structural benefits provided by DI pipes in comparison to CI pipes and mild steel pipes such as superior tensile strength, yield strength, greater impact resistance, corrosion resistance and ductility. In addition, DI pipes require less support and provide greater flow area compared to pipes made from other materials. Hence, in a difficult terrain, DI pipes can be a better choice than polyvinyl chloride concrete, polyethylene and steel pipes.

Margins to remain firm on the back of cost saving initiatives & muted input costs…

Over the last couple of years, SPL has undertaken various cost saving initiatives like reduction of coke consumption, CRC scrap, HSD oil coupled with effective utilisation of sinter plant in terms of capacity, consumption ratio and reduction of power cost by increased power generation. Furthermore, SPL has been also a key beneficiary of falling iron ore and coking coal prices, which has aided margin expansion. Going forward, iron ore prices are likely to remain at subdued levels on the back of increased supplies by global iron ore majors. Coking coal prices are also expected to sustain at muted levels on the back of increased supply from Australia and the US. Subsequently, we expect EBITDA margins to remain firm. We have modelled an EBITDA margin of 17.5% for FY16E and 18.0% for FY17E. Furthermore with the planned increase in the coke oven plant, captive power capacity will increase from 12 MW to 18 MW, thus making SPL self-sufficient for its power requirements.

Exhibit 6: Healthy growth in EBITDA, EBITDA margin on the back of cost saving initiatives



Source: Company, ICICIdirect.com Research,

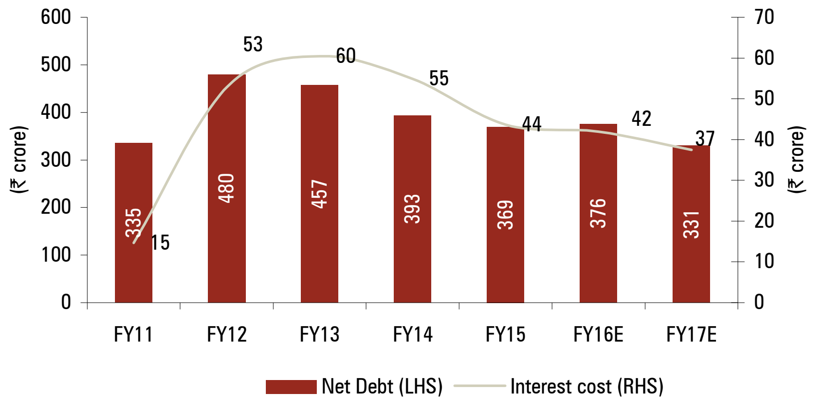
Anti-dumping duty aids in successfully curbing imports of DI pipes from China

Import of DI pipes from China is currently subject to anti-dumping duty in the range of US$127.4/tonne to US$139.8/tonne. Originally imposed in September 2007 for five years, the anti-dumping duty was reinforced by the government during 2013-14 and will be in place for next five years until 2017-18, unless revoked. The duty has been successful in curbing imports of DI pipes from China.

Debt reduction plans augurs well for the company

SPL has progressively reduced its net debt from ₹ 480 crore at the end of FY12 to ₹ 369 crore at the end of FY15 through improved operational performance and better working capital management. Going forward we expect SPL's net debt to further decline to ₹ 331 crore at the end of FY17E. Reduction in debt levels has also aided in reduction of interest expense which has declined from ₹ 60 crore in FY13 to ₹ 55 crore in FY14 and further to ₹ 44 crore in FY15. We expect interest expense to stay in the range of ₹37-42 crore over next couple of year.

Exhibit 7: Debt reduction plans augurs well



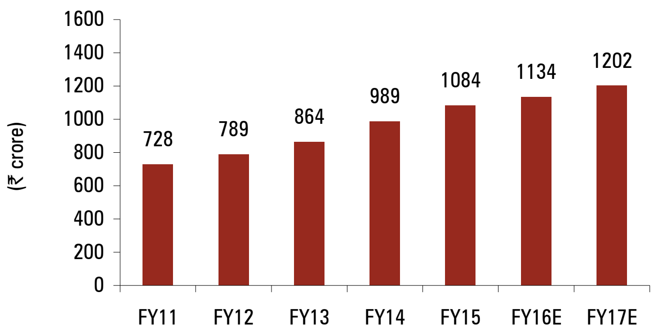
Source: Company, ICICIdirect.com Research,

Financials

Revenue to grow at CAGR of 5.3% in FY15-17E, driven by higher volume

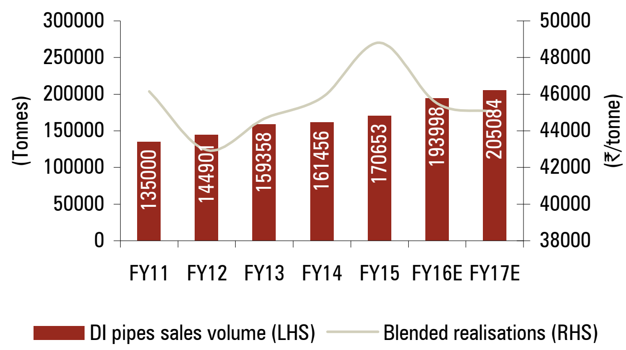
We expect SPL to clock revenue growth of 5.3% CAGR in FY15-17E primarily on the back of an increase in DI pipes sales volume. On the back of healthy demand from key user industries, we expect DI pipes sales to increase at a CAGR of 9.6% in FY15-17E. We have modelled DI pipes sales volume of ~194000 tonnes in FY16E and ~205000 tonnes in FY17E. However on the back of declining prices of key raw materials (iron ore and coking coal) we expect the blended realisations of DI pipes to stay muted and decline from ₹ 48804/tonne in FY15 to ₹ 45055/tonne in FY17E.

Exhibit 8: Revenue growth trend



Source: Company, ICICIdirect.com Research

Exhibit 9: DI pipes sales volume & blended realisation trend

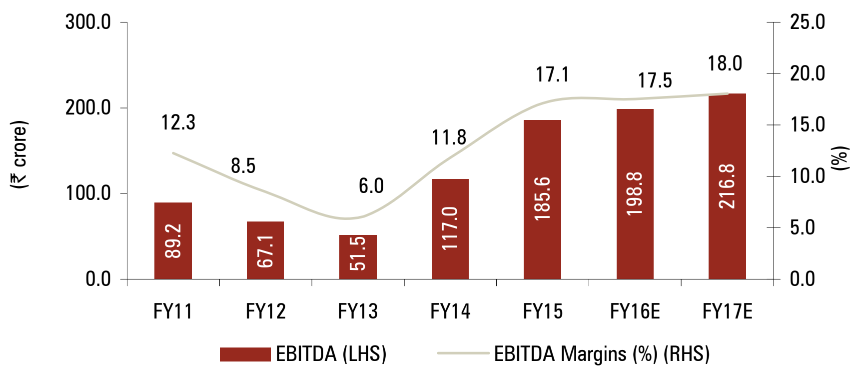


Source: Company, ICICIdirect.com Research

EBITDA to grow at 8.1% CAGR during FY15-17E…

Operational efficiencies coupled with steep fall in raw material prices (iron ore and coking coal) is likely to more than compensate muted realisations of DI pipes. We expect EBITDA to grow at a CAGR of 8.1% in FY15-17E primarily on the back of an increase in DI pipes sales volume and expansion in EBITDA margins from 17.1% in FY15 to 18.0% in FY17E.

Exhibit 10: EBITDA and EBITDA margins trend…

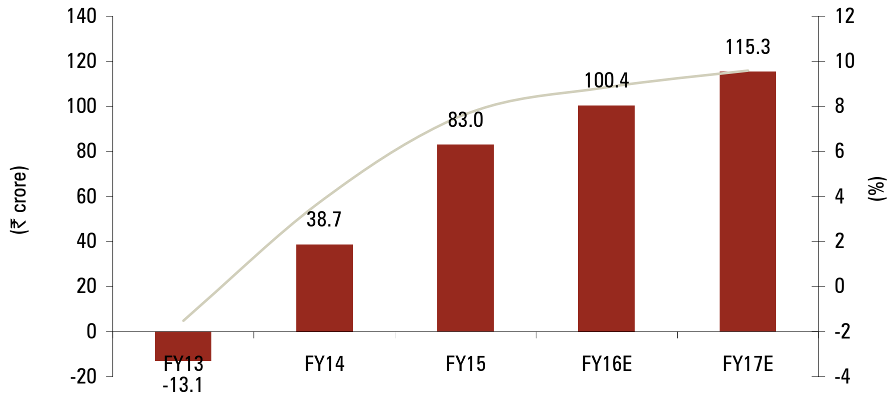


Source: Company, ICICIdirect.com Research,

PAT growth of 17.9% CAGR in FY15-17E

After reporting a loss for a couple of years (FY12 and FY13), SPL witnessed a turnaround and reported healthy profits in subsequent years. Going forward, we expect SPL's good performance to continue. On the back of an improvement in operating margins coupled with a marginal reduction in interest charge and tax incidence, we expect PAT to grow at a CAGR of 17.9% in FY15-17E.

Exhibit 11: PAT & PAT margin trend

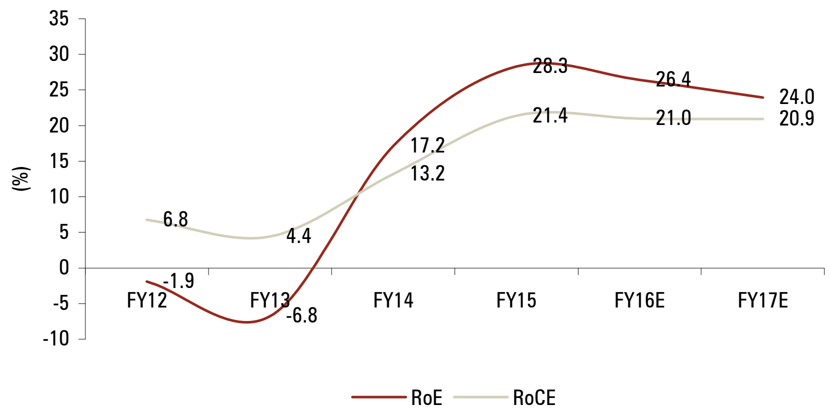


Source: Company, ICICIdirect.com Research

Return ratios to remain firm…

The company witnessed healthy return ratios with RoCE and RoE in FY15 at 28.3% and 21.4%, respectively. Going forward, we expect SPL's return ratios to remain firm (RoE of 26.4% in FY16E and 24.0% in FY17E and RoCE of 21.0% in FY16E and 20.9% in FY17E).

Exhibit 12: RoE and RoCE trend…



Source: Company, ICICIdirect.com Research

Risk and concern

Slowdown in order intake

Over the last couple of years, on the back of a demand pick-up from key user industry segments, there has been strong growth in the company's order intake, resulting in healthy topline growth. However, going forward, any slowdown in demand from key user industries may adversely impact the order book intake for the company. This may further impact the overall operating performance of the company.

Steep rise in prices of key raw materials

Over the last few quarters, EBITDA margins of SPL have witnessed healthy growth primarily on the back of softening prices of key raw materials i.e. iron ore and coking coal. Going forward, any steep rise in prices of iron ore and coking coal is likely to adversely impact operating margins and profitability of the company.

Competition

SPL enjoys dominant position in the south and west zone due to the absence of any major player. Going forward, SPL's operational performance can be notably impacted if any other market player enters/expands its capacity in the company's focused southern and western zone.

Tables and ratios

Exhibit 13: Profit & loss account

(Year-end March)	FY13	FY14	FY15	FY16E	FY17E
Net Sales	857.4	987.2	1,083.6	1,134.4	1,201.5
Other Operating Income	6.4	2.2	-	-	-
Total Operating Income	863.9	989.4	1,083.6	1,134.4	1,201.5
Other Income	9.8	7.2	8.7	10.0	11.5
Total Revenue	873.6	996.6	1,092.2	1,144.4	1,213.0
-	-	-	-	-	-
Raw Material Expenses	592.5	585.0	595.8	618.0	654.3
Employee Expenses	38.0	44.4	48.4	51.0	54.1
Other Expenditure	181.9	243.0	253.7	266.6	276.4
Total Operating Expenditure	812.4	872.4	897.9	935.6	984.7
EBITDA	51.5	117.0	185.6	198.8	216.8
Interest	60.4	54.9	43.7	42.0	37.5
PBDT	0.9	69.4	150.6	166.8	190.8
Depreciation	22.2	27.9	31.2	32.9	37.2
PBT	(21.3)	41.4	119.4	133.8	153.7
Total Tax	(8.2)	2.7	36.4	33.5	38.4
PAT	(13.1)	38.7	83.0	100.4	115.3
EPS	(3.3)	9.7	20.9	25.2	29.0

Source: Company, ICICIdirect.com Research

Exhibit 14: Balance sheet

(Year-end March)	FY13	FY14	FY15	FY16E	FY17E
Equity Capital	39.8	39.8	39.8	39.8	39.8
Reserve and Surplus	154.0	185.7	253.5	339.9	441.2
Total Shareholders funds	193.8	225.5	293.3	379.7	481.0
	-	-	-	-	-
Total Debt	466.8	450.3	428.6	410.7	377.9
Other Non Current Liabilities	74.0	49.5	13.1	18.1	23.1
Deferred Tax Liability	27.7	30.4	65.5	65.5	65.5
Liability side total	762.3	755.7	800.5	874.0	947.5
Gross Block	612.7	634.6	717.7	832.7	915.7
Less Accumulated Depreciation	171.3	199.2	230.3	263.3	300.4
Net Block	441.4	435.5	487.3	569.4	615.2
Total CWIP	17.0	20.0	8.9	8.9	8.9
Total Fixed Assets	458.4	455.5	496.2	578.3	624.1
Inventory	208.3	236.8	134.6	139.9	148.1
Debtors	119.4	148.0	186.0	195.8	207.4
Loans and Advances	79.1	82.4	44.8	45.4	48.1
Other Current Assets	30.3	38.2	50.3	56.7	60.1
Cash	10.2	57.4	59.2	34.8	47.0
Total Current Assets	447.2	562.7	475.0	472.6	510.7
Creditors	104.8	195.7	102.4	108.8	115.2
Short and Long term Provisions	4.2	12.4	21.6	22.7	24.0
Other Current Liabilities	34.3	54.4	46.6	45.4	48.1
Total Current Liabilities	143.3	262.5	170.7	176.8	187.3
Net Current Assets	303.9	300.2	304.3	295.7	323.4
Assets side total	762.3	755.7	800.5	874.0	947.5

Source: Company, ICICIdirect.com Research

Exhibit 15: Cash flow statement

(Year-end March)	FY13	FY14	FY15	FY16E	FY17E
Profit after Tax	(13.1)	38.7	83.0	100.4	115.3
Depreciation	22.2	27.9	31.2	32.9	37.2
Interest	60.4	54.9	43.7	42.0	37.5
Cash Flow before working capital changes	69.5	121.5	157.8	175.3	189.9
Net Increase in Current Assets	119.2	(68.3)	89.5	(22.0)	(25.9)
Net Increase in Current Liabilities	(12.0)	119.2	(91.8)	6.2	10.5
Net cash flow from operating activities	176.7	172.4	155.6	159.5	174.4
Increase / (decrease) in deferred tax liability	(8.2)	2.7	35.1	-	-
(Purchase)/Sale of Fixed Assets	(105.9)	(25.0)	(71.9)	(115.0)	(83.0)
Other Non Current Liabilities	20.9	(24.6)	(36.3)	5.0	5.0
Net Cash flow from Investing Activities	(93.3)	(46.9)	(73.2)	(110.0)	(78.0)
Proceeds/(Repayment) of Secured Loan	6.6	(16.6)	(31.6)	(18.0)	(32.8)
Proceeds/(Repayment) of Unsecured Loan	(29.6)	0.1	9.9	-	-
Interest Paid	(60.4)	(54.9)	(43.7)	(42.0)	(37.5)
(Payment) of Dividend and Dividend Tax	-	(7.0)	(14.0)	(14.0)	(14.0)
Adjustment / One time payment in P&L appro.	-	-	(1.2)	-	-
Net Cash flow from Financing Activities	(83.5)	(78.3)	(80.5)	(73.9)	(84.2)
Net Cash flow	(0.0)	47.2	1.9	(24.4)	12.2
Cash and Cash Equivalent at the beginning	10.2	10.2	57.4	59.2	34.8
Closing Cash/ Cash Equivalent	10.2	57.4	59.2	34.8	47.0

Source: Company, ICICIdirect.com Research

Exhibit 16: Ratio analysis

(Year-end March)	FY13	FY14	FY15	FY16E	FY17E
Per Share Data					
EPS	(3.3)	9.7	20.9	25.2	29.0
Cash EPS	2.3	16.8	28.7	33.5	38.3
BV	48.7	56.7	73.8	95.5	121.0
Operating profit per share	13.0	29.4	46.7	50.0	54.5
Operating Ratios					
EBITDA / Total Operating Income	6.0	11.8	17.1	17.5	18.0
PAT / Total Operating Income	(1.5)	3.9	7.7	8.8	9.6
Inventory Days	88.7	87.5	45.3	45.0	45.0
Debtor Days	50.8	54.7	62.7	63.0	63.0
Creditor Days	44.6	72.4	34.5	35.0	35.0
Return Ratios					
RoE	(6.8)	17.2	28.3	26.4	24.0
RoCE	4.4	13.2	21.4	21.0	20.9
RoIC	4.0	13.1	21.1	20.0	20.2
Valuation Ratios					
EV / EBITDA	24.6	10.3	6.4	6.0	5.3
P/E	NA	21.0	9.8	8.1	7.0
EV / Net Sales	1.5	1.2	1.1	1.0	1.0
Sales / Equity	4.4	4.4	3.7	3.0	2.5
Market Cap / Sales	0.9	0.8	0.7	0.7	0.7
Price to Book Value	4.2	3.6	2.8	2.1	1.7
Turnover Ratios					
Asset turnover	1.1	1.3	1.4	1.4	1.3
Debtors Turnover Ratio	7.2	6.7	5.8	5.8	5.8
Creditors Turnover Ratio	8.2	5.0	10.6	10.4	10.4
Solvency Ratios					
Debt / Equity	2.4	2.0	1.5	1.1	0.8
Current Ratio	3.1	2.1	2.8	2.7	2.7
Quick Ratio	1.7	1.2	2.0	1.9	1.9

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;

Pankaj Pandey **Head – Research** **pankaj.pandey@icicisecurities.com**

ICICIdirect.com Research Desk,
ICICI Securities Limited,
1st Floor, Akruti Trade Centre,
Road No. 7, MIDC,
Andheri (East)
Mumbai – 400 093

research@icicidirect.com

ANALYST CERTIFICATION

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