



Technocraft Industries

STOCK INFO.	BLOOMBERG
BSE Sensex:29,571	TIIL:IN
S&P CNX:8,910	REUTERS CODE TEIN.NS

28 January 2015

Buy

Initiating Coverage

INR196

	(INR CRORES)		
Y/E MARCH	FY15E	FY16E	FY17E
Net Sales	1079	1250	1433
EBITDA	146	173	199
RPAT	91	113	132
BV/Share (Rs)	202	229	261
Adj. EPS (Rs)	28.9	35.8	41.7
EPS Growth (%)	-8%	24%	17%
P/E (x)	6.8	5.5	4.7
P/BV (x)	1.0	0.9	0.8
EV/EBITDA (x)	4.5	3.8	3.3
Div yld (%)	3.1%	3.8%	4.6%
ROE (%)	14	16	16
ROCE (%)	19	20	20

KEY FINANCIALS

Shares Outstanding (cr)	3.15
Market Cap. (Rs cr)	618
Market Cap. (US\$ m)	103
Past 3 yrs Sales Growth (%)	23%
Past 3 yrs NP Growth (%)	41%

STOCK DATA

52-W High/Low Range (INR)	218/75
Major Shareholders (as of June 2014)	
Promoter	75.0
Non Promoter Corp Holding	3.1
Public & Others	21.9
Average Daily Turnover(6 months)	
Volume	36129
Value (Rs cr)	0.69
1/6/12 Month Rel. Performance (%)	13/-7/94
1/6/12 Month Abs. Performance (%)	19/5/106

Maximum Buy Price : INR220

We recommend to BUY Technocraft Industries for a target of INR 300 - valuing the company on SOTP basis. At our target price, the stock would trade at a P/E of 8.5x on FY17E EPS.

Drum closure division - cash cow with a sustainable moat:

Technocraft commands 36% market share of the Global (ex-China) steel drum closure industry having a size of INR 700 cr. With the largest player being Greif, having over 50% market share, the top two players together command over 86% of the Global (ex-China) market share thus making the industry a duopoly. Manufacturing steel drum closures requires a very high level of precision engineering which acts as a major entry barrier. Moreover, large global engineering companies find the steel drum closure industry too small to venture into. Further, the cost of a set of drum closure (INR 30) being just 3% of the cost of a steel drum (INR 900) enables drum closure players to easily pass on any cost pressures to the steel drum manufacturers for whom the cost of closures is insignificant. Thus Technocraft's drum closure division commands EBITDA margins of 30% along with an ROCE of over 70% thereby generating robust free cash flows.

Scaffolding division to drive growth: Technocraft is the largest scaffolding exporter from India. It manufactures scaffoldings as per the certifications/standards set by countries like US, Germany and UK where there is a huge demand for scaffoldings. Scaffolding revenues and profits have grown at a CAGR of 32% and 45% respectively over the last three years. Management has guided for 25% topline growth in coming years which we believe is achievable.

IT division to start contributing: Technocraft also offers engineering services to various manufacturing companies. Technocraft acquired Swift Engineering (Canada) in April 2013, which provides EPCM services to the oil & gas industry. The management aims to capitalize on the capabilities of Swift and expects it to drive growth in the IT division. IT division clocked revenues of INR 73 cr in FY14 (7% of revenue) along with EBITDA margins of 14%, in line with that of the company.

Valuations & View: Given Technocraft's superior industry positioning in drum closures, incremental growth being driven by the scaffolding division and increasing contribution from the IT division; we believe Technocraft is available at attractive valuations of 4.7x FY17E EPS. Our SOTP based price target for Technocraft is at INR 300 providing for an upside of 54% over the next one year.

CONCERNS

Lack of a sound capital allocation strategy: The success of the company's drum closure business in the 1980s-90s prompted the company to utilize its cash flows by expanding in new businesses. Thus the company ventured into steel tubes (now scaffoldings), textiles and IT. While it has achieved reasonable success in scaffoldings and IT, its performance in the textiles division has been disappointing. The company has cash & equivalents of INR 210 cr which is close to 30% of the total capital employed. Further, as the cash flows from the drum closure division continue to pour in, the cash position of the company would continue to increase. The management is planning to utilize its cash by venturing into new businesses or by acquiring a company. Any new venture or acquisition in an unrelated field having poor business economics is a risk.

Dependence on global demand: Technocraft has an export oriented business model with sales outside of India accounting for over 90%. Thus the company's growth depends upon the demand in International markets specially that in US and Europe. Any slowdown in these developed economies could have a bearing on the scaffolding, IT and textile divisions of the company.

Increase in cotton prices: The company's textile (yarn) business operates in a highly competitive environment and any sudden increase in cotton prices could impact profitability. The textile division's profitability has witnessed significant volatility in the past based on the movement in cotton & yarn prices.

BACKGROUND

Technocraft Industries was established in 1972 by two IITian brothers - Mr. Sharad Kumar Saraf and Mr. Sudarshan Kumar Saraf. Within a few years, the company started exporting to the Middle East, US and Europe and developed its marketing and warehousing presence in these countries which acted as the front end for its clients. Technocraft continued developing and increasing its production until it became the world's second largest supplier of drum closures. Subsequently, the company ventured in other businesses of steel tubes (now scaffoldings), textiles and IT. The company's manufacturing facilities are located at Murbad (Thane), just 50 kms from JNPT port, which makes the operations efficient as over 90% of the company's revenue is generated from overseas markets.

SOTP Target

Segment	Method	FY17 Multiple	Value per share	Contribution
Drum Closure	P/E	9.0	190	64%
Scaffoldings	P/E	5.0	62	21%
Textile	P/B	0.5	12	4%
Subsidiaries	P/B	0.75	36	11%
Total			300	100%
CMP			196	
Upside			54%	

Financials & Valuation (Consolidated)

INCOME STATEMENT						RATIOS					
(INRCR)											
Y/E MARCH	FY13	FY14	FY15E	FY16E	FY17E	Y/E MARCH	FY13	FY14	FY15E	FY16E	FY17E
Revenues	809	1045	1079	1250	1433	Adjusted EPS (INR)	23.5	31.4	28.9	35.8	41.7
Growth	24%	29%	3%	16%	15%	Book Value	159	180	202	229	261
COGS	458	621	651	749	857	Div Per Share	3.0	5.0	6.0	7.5	9.0
Gross Profit	351	424	428	501	576	Dividend Payout	15%	21%	24%	24%	25%
GP Margin	43.3%	40.6%	39.7%	40.1%	40.2%	Net Debt / Equity	0.2	0.2	0.1	0.1	0.1
Employee Cost	53	74	81	91	103	P/E	8.3	6.2	6.8	5.5	4.7
Other Expenses	175	195	202	237	274	P/BV	1.2	1.1	1.0	0.9	0.8
EBITDA	122	154	146	173	199	EV/EBITDA	5.4	4.3	4.5	3.8	3.3
EBITDA Margin	15.1%	14.8%	13.5%	13.8%	13.9%	EV/Sales	0.8	0.6	0.6	0.5	0.5
Depreciation	31	27	27	26	28	Dividend Yield	1.5%	2.6%	3.1%	3.8%	4.6%
Other Income	24	22	25	29	32	ROCE	19%	20%	19%	20%	20%
PBIT	115	149	144	175	204	ROE	15%	16%	14%	16%	16%
E/O. Inc/(Loss)	0	(15)	0	0	0	EBITDA Margin	15.1%	14.8%	13.5%	13.8%	13.9%
Interest Cost	8	5	11	10	11	PAT Margin	9.2%	9.5%	8.4%	9.0%	9.2%
PBT	107	130	133	165	192	Debtor days	98	98	98	99	99
Tax	33	41	42	51	60	Inventory days	104	94	103	98	98
Rate	31%	31%	31%	31%	31%	Creditor days	41	41	41	40	40
Adjusted PAT	74	99	91	113	132	W.Cap cycle	161	151	160	157	157
Growth	379%	34%	-8%	24%	17%						

BALANCE SHEET						CASH FLOW					
(INRCR)						(INRCR)					
Y/E MARCH	FY13	FY14	FY15E	FY16E	FY17E	Y/E MARCH	FY13	FY14	FY15E	FY16E	FY17E
Share Capital	32	32	32	32	32	EBITDA	122	154	146	173	199
Reserves	471	542	612	698	797	Adjustments	13	-2	-2	-1	0
Networth	502	573	643	729	829	(Inc)/Dec in W.Cap	(11)	(83)	(17)	(64)	(65)
Loans	118	157	135	145	165	Pre Tax OCF	125	69	127	107	134
SOURCES OF FUNDS	621	730	778	875	994	Tax Paid	(34)	(41)	(45)	(55)	(63)
Gross Fixed Assets	424	451	491	532	592	CF from Operations	91	28	82	53	71
Less: Depreciation	275	300	326	351	378	(Inc)/Dec in FA	(11)	(26)	(41)	(40)	(61)
Net Fixed Assets	150	150	165	180	214	Addition to Investments	(118)	6	(10)	(10)	(10)
Capital WIP	0	0	0	0	0	Interest Received	24	0	25	29	32
Inventories	142	179	187	215	246	CF from Investing act.	(106)	(20)	(26)	(21)	(38)
Debtors	218	279	288	337	387	Inc/(Dec) in Sh. Prem.	0	0	0	0	0
Cash & Investments	171	189	202	217	234	Inc/(Dec) in Debt	31	38	(22)	11	20
Loans & Advances	8	7	8	9	10	Interest Paid	(8)	(5)	(11)	(10)	(11)
Other Curr Assets	46	63	68	73	78	Divd Paid (incl Tax)	(11)	(18)	(22)	(28)	(33)
Curr. Assets	584	718	754	852	955	CF from Financing act.	12	15	(55)	(27)	(25)
Creditors and Prov.	110	142	148	167	188	Inc/(Dec) in Cash	(3)	23	2	4	7
Net Current Assets	475	575	606	685	767	Add: Opening Balance	22	19	43	45	49
Less Net Def. Tax Liab	4	-4	-7	-9	-12	Closing Balance	19	43	45	49	56
APPLICATION OF FUNDS	621	730	778	875	994						

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