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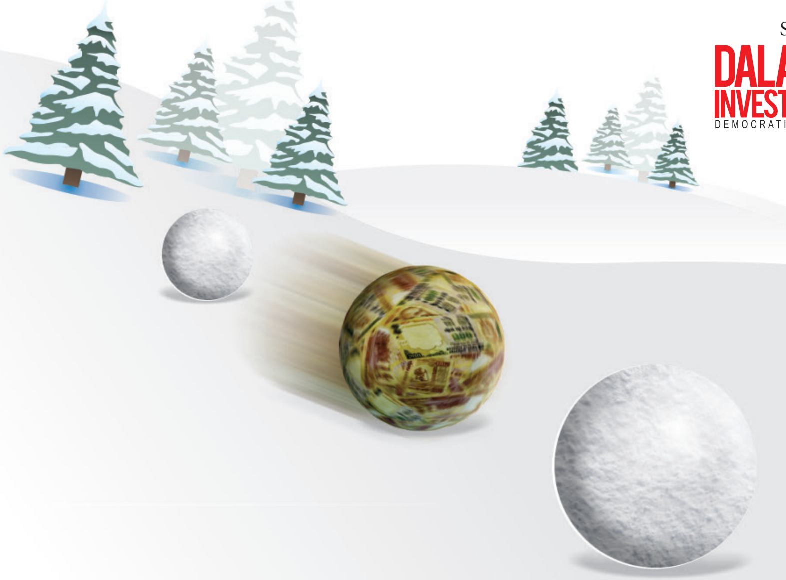
DALAL STREET INVESTMENT JOURNAL
DEMOCRATIZING WEALTH CREATION

MID BRIDGE
THE MIDCAP MARVEL

June 2017



COMPANY NAME	:	**Srikalahasthi Pipes**
BSE Code	:	**513605**
Time Duration	:	**1 year**
CMP	:	**₹350 (as on 15 June, 2017)**
Target Price	:	**₹482**

The Mid Bridge for the month of June is Srikalahasthi Pipes, which was formerly known as Lanco Industries. It is engaged in the manufacture of ductile iron pipes. These pipes form an important part of infrastructure related to drinking water supply, sewerage and irrigation. Its integrated manufacturing systems are located at Srikalahasthi, Chitoor district, Andhra Pradesh near the Tirupati temple with land coverage of ~330 acres. Its revenue mix includes DI pipes (82%), pig iron (1%), cement (2%), coke (3%) and others (12%).

In DI pipes segment, it enjoys 15% market share in India. However, with southern markets being its core region, it enjoys 77% market share in southern and western regions of India. We believe that development of water supply, irrigation and sanitation infrastructure will boost demand for DI pipes. With favourable marco-economic factors and strong market presence we see an upside of 37% from current the levels over a year.

Government initiatives to boost demand

We see company's product offering yielding benefits due to various programmes by the government and favourable macro-economic factors.

1) To support urbanisation, the government has launched a program named, 'Atal Mission for Rejuvenation and Urban Transformation' (AMRUT), under which basic water services are to be supplied across 500 cities and towns in India. Rs 50,000 cr have been allocated for this scheme for FY16-20.
2) For the 'Smart Cities Mission',Rs 100 cr have been allocated for each Smart City over a period of 5 years.
3) Another initiative which can boost the demand for company's product is 'Swachh Bharat Abhiyaan', which includes conversion of unsanitary toilets to pour flush toilets, eradication of manual scavenging and solid waste management.

Under all these initiatives, smooth and continuous water supply is an imperative and hence demand for DI pipes is going to increase. Many cities in South India are also under the ambit of these schemes which would prove beneficial for Srikalahasthi Pipes. It had bagged orders worth Rs 1151 cr from Telangana Government for supplying pipes under various projects. Till the end of December 2016, the company's order book stood at 2,50,000 tonnes.

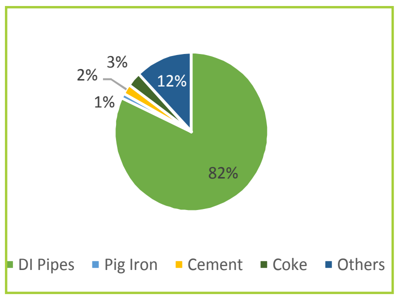
Capacity Expansion

Last year (FY16), the company had expanded the capacity of its plant at Chittoor from 2.25 lakh tonnes p.a. to 3 lakh tonnes p.a. with capex of Rs 100 cr. The management expects to gain benefits from this increased capacity from FY18. Recently, it is raised funds of Rs.250cr through qualified institutional placement. The funds would be utilized for expansion of coke oven plant and increase the capacity of power plant at a cost of Rs 65 cr. This expansion will provide intermediaries for production of DI pipes.

Also, the management has earmarked Rs 35 cr to be utilised for the organic and inorganic growth.

Low cost model with focus on reducing debt

The company is the lowest cost manufacturer as it is fully backward integrated and meets ~75% power demand internally, and with its new capacity, it will be augmented further. Also, pig iron which is a raw material for DI pipes, is manufactured internally.



Managing raw materials efficiently and effectively positively impacts the performance and working capital of the company. The company has adopted integrated basis of operations under which it focuses on material forecasting, planning and inventory control. By organizing and planning procurement of raw materials like coal and iron ore on long-term contracts basis at competitive prices, the company has managed to reduce inventory carrying cost. Due to such cost saving operations, we see that margins are improving on YoY basis. Its EBITDA margin in FY13 stood at 5.93% which improved to 23.26% till FY16. Debt also seems to have been reduced to Rs 444.7 cr in FY16, which was Rs 489.9 cr in FY13 due to efficient working capital management. The capacity expansion was also funded through internal accruals and with no fresh issues of equity.

Expected lower commodity prices

We see the iron ores prices have dipped from the highs seen over the last six months. With commodity prices smoothening, we see Srikalahasti benefitting from the same. We saw margin pressure in FY17, which should be less evident in FY18 and margins might return to the FY16 levels.

The company procures iron ore from open market and with prices coming off, it should lead to margin upside.

Financial Performance

A continuous growth in revenue is seen at CAGR of 9.5% over the past five years. In FY17, revenue grew marginally to Rs.1177.87 cr from Rs 1145.61 YoY. A consistent growth in EBITDA is also seen since FY12. However, for FY17, the EBITDA margin stood low at 21.08% as against 23.26% in FY16 due to planned shut-down of mini blast furnace for a month. The PAT decreased marginally in FY17 to Rs 140.24 cr from Rs 158.80 cr due steep rise in prices of coking coal. Its debt-equity ratio improved to 1.04x in FY16 from 2.37 in FY12. The interest coverage ratio also improved to 6.11x from 0.93 in FY12. Its ROA stood at 15.4% in FY16 versus -0.45% in FY12.

Valuation and Outlook

The company is trading at TTM P/E of 9.97x with TTM EPS of Rs 35.3. It has delivered ROE and ROCE of 17.24% and 26.27%, respectively. We see that the company is providing higher returns as against its peers, which shows it as an investor-friendly company. The government's initiatives and its strong order book would augur well for the company going forward. We recommend our investors to **BUY** this scrip in three tranches. We expect it to reach the target price of Rs.482 over a period of one year.

Inc/Exp Statement(Standalone) (Rs in Crore)

Description	201703	201603	201503	201403	201303
Net Sales	1203.40	1145.61	1083.55	989.40	863.89
Total Income	1233.87	1162.94	1095.54	997.95	879.37
Total Expenditure	966.47	879.13	901.26	873.70	818.10
PBIDT	267.40	283.81	194.28	124.26	61.28
PAT	140.23	158.80	82.17	38.70	-13.10
Dividend %	60.00	50.00	30.00	15.00	
Adj. EPS(Rs)	35.27	39.94	20.66	9.73	-3.29

Quarter On Quarter (Standalone) (Rs in Crore)

Particulars	201703	201612	Q on Q Var%	201603	Y on Y Var%
Net Sales	439.40	291.55	50.71	321.65	36.61
Total Expenditure	383.82	221.02	73.66	252.46	52.03
PBIDT (Excl OI)	55.58	70.54	-21.20	69.19	-19.67
PAT	31.19	40.10	-22.21	45.47	-31.40
PBIDTM% (Excl OI)	12.65	23.70	-46.62	21.51	-41.19
PBIDTM%	13.80	24.90	-44.58	23.85	-42.14
PATM%	7.10	13.47	-47.29	14.14	-49.79
Adj. EPS(Rs)	7.84	10.08	-22.22	11.43	-31.41