

14 May 2014

Graphite India

Cash generation accelerates; Buy

Rating: **Buy**

Target Price: ₹119

Share Price: ₹85

Key takeaways

Revenues driven by greater volumes. Graphite India's 4QFY14 sales volumes increased 4% yoy, offset by lower price realization. Export volumes were subdued while strong domestic volume growth sustained the growth rates. With 83% capacity utilization to 16,600 tonnes, production rose 7% yoy. Management has guided to a ~70% utilization rate at the consolidated level in FY15 but we believe the guidance would be surpassed by the upswing in steel volumes in developed countries and the brightening Indian outlook.

EBITDA margin sustained. EBITDA increased 10.3% yoy and the margin expanded 185bps to 13.9% due to greater export incentives. Management has been focusing on production rationalisation in order to maintain the margin profile. PAT increased 22.2% yoy due to higher other income and lower finance costs.

Cash generation accelerates adding to balance-sheet strength. Post-capex, ₹5bn in cash was generated, turning the standalone balance sheet net cash positive, and dividend of ₹3.5 a share was declared for FY14. From the consolidated results, it could be inferred that the German subsidiary suffered an EBITDA loss of ₹343m as volumes declined ~30%, but recovery in demand is progressing as the management expects better volumes in FY15.

Our take. Graphite India has scale in the global league of graphite electrode operators, with annual production capacity of 98,000 tonnes; ~65% of the production is exported to 30 countries. Strong product knowledge has been built since 1960. Sturdy operating margins driven by operational efficiency, productivity, technology, and access to low-cost sources of power would sustain cash generation during the cycle. At the CMP, the stock trades at 3x FY16e EV/EBITDA and we maintain a Buy on it, with a price target of ₹119 based on 4.5x FY16e EV/EBITDA. **Risks.** Adverse currency movements and sharp raw-material price volatility.

Key data	GRIL IN / GRPH.BO
52-week high / low	₹95/₹57
Sensex / Nifty	23871/7109
3-m average volume	US\$0.1m
Market cap	₹17bn/US\$0.3bn
Shares outstanding	195m

Shareholding pattern (%)	Mar'14	Dec'13	Sep'13
Promoters	65.0	64.5	63.9
- of which, Pledged	-	-	-
Free Float	35.1	35.5	36.1
- Foreign Institutions	15.7	15.5	15.2
- Domestic Institutions	3.5	4.0	4.8
- Public	15.8	16.0	16.2

Estimates revision (%)	FY15e	FY16e
Revenues	(3.0)	(4.0)
EBITDA	(0.8)	(2.4)
PAT	1.7	1.4

Financials (YE Mar)	FY15e	FY16e
Revenues (₹m)	18,471	21,033
EBITDA (₹m)	3,407	4,383
EBITDA margin (%)	18.4	20.8
PAT (₹m)	2,080	2,818
EPS (₹)	10.6	14.4
EPS growth (%)	21.7	35.5
P/E (x)	8.0	5.9
P/BV (x)	0.9	0.8
EV/EBITDA (x)	4.3	3.0
ROAE (%)	11.6	14.7

Source: Anand Rathi Research

Quarterly results (YE Mar)	4QFY13	4QFY14	YoY(%)	FY13	FY14	YoY(%)
Sales (₹m)	5,112	4,890	(4.3)	17,649	17,681	0.2
EBITDA (₹m)	618	682	10.3	2,789	2,843	1.9
EBITDA margin (%)	12.1	13.9	185bps	15.8	16.1	28bps
Interest (₹m)	71	39	(44.5)	221	170	(23.4)
Depreciation (₹m)	137	134	(1.8)	500	536	7.1
Other income (₹m)	98	159	62.0	264	402	52.4
PBT (₹m)	509	667	31.1	2,331	2,539	8.9
Tax (₹m)	93	218	133.9	700	830	18.6
Tax rate (%)	18.3	32.6	1,433bps	30.0	32.7	266bps
PAT (₹m)	416	449	8.1	1,631	1,709	4.8

Source: Company

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Quick Glance – Financials and Valuations

Fig 1 – Income statement (₹ m)

Year-end: Mar	FY12	FY13	FY14e	FY15e	FY16e
Net revenues	16,708	17,649	17,681	18,471	21,033
Revenue growth (%)	36.3	5.6	0.2	4.5	13.9
- Oper. expenses	13,596	14,860	14,838	15,063	16,650
EBIDTA	3,112	2,789	2,843	3,407	4,383
EBITDA margin (%)	18.6	15.8	16.1	18.4	20.8
- Interest expenses	144	221	170	175	115
- Depreciation	404	500	536	569	593
+ Other income	346	264	402	440	531
- Tax	828	700	830	1,024	1,388
Effective tax rate (%)	25.8	30.0	32.7	33.0	33.0
Reported PAT	2,379	1,631	1,709	2,080	2,818
+/- Extraordinary items	296	-	-	-	-
+/- Minority interest	-	-	-	-	-
Adjusted PAT	2,379	1,631	1,709	2,080	2,818
Adj. FDEPS (₹/sh)	12.2	8.3	8.7	10.6	14.4
Adj. FDEPS growth (%)	38.1	(31.4)	4.8	21.7	35.5

Source: Company, Anand Rathi Research

Fig 2 – Balance sheet (₹ m)

Year-end: Mar	FY12	FY13	FY14e	FY15e	FY16e
Share capital	391	391	391	391	391
Reserves & surplus	15,228	16,059	16,968	18,075	19,409
Net worth	15,619	16,450	17,359	18,465	19,800
Minority interest	-	-	-	-	-
Total debt	4,617	5,676	3,410	2,410	1,410
Def. tax liab. (net)	708	950	897	897	897
Capital employed	20,945	23,077	21,666	21,772	22,107
Net fixed assets	6,700	6,626	6,415	6,646	6,353
Investments	2,051	1,093	1,576	1,576	1,576
- of which, Liquid	-	-	-	-	-
Net working capital	12,850	14,026	10,009	9,126	9,171
Cash and bank balance	1,395	2,424	3,666	4,425	5,007
Capital deployed	20,945	23,077	21,666	21,772	22,107
Net debt	3,222	3,252	(256)	(2,015)	(3,598)
WC days	281	290	207	180	159
Book value (₹/sh)	64.0	78.3	97.4	118.7	119.7

Source: Company, Anand Rathi Research

Fig 3 – Cash-flow statement (₹ m)

Year-end: Mar	FY12	FY13	FY14e	FY15e	FY16e
PAT	2,379	1,631	1,709	2,080	2,818
+ Non-cash items	404	500	536	569	593
Cash profit	2,783	2,131	2,245	2,648	3,411
- Incr./Decr. in WC	2,101	2,349	(2,924)	(884)	46
+ Net finance exp	168	253	572	615	646
- Misc	564	(69)	804	880	1,062
Operating cash-flow	286	104	4,937	3,267	2,949
- Capex	1,321	408	325	800	300
Free cash-flow	(1,035)	(305)	4,612	2,467	2,649
- Dividend and interest	947	1,024	970	1,148	1,598
+ Equity raised	-	-	0	-	-
+ Debt raised	1,752	1,241	(2,266)	(1,000)	(1,000)
- Investments	(4)	3	-	-	-
+ Other income and misc	(33)	(41)	(402)	(440)	(531)
Net cash-flow	(193)	(49)	1,778	759	582

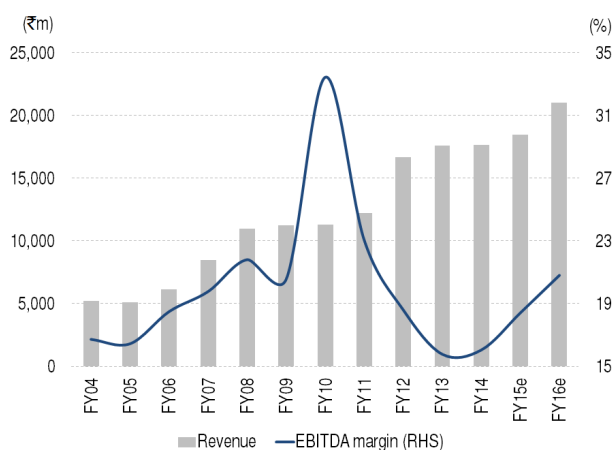
Source: Company, Anand Rathi Research

Fig 4 – Ratio analysis @ ₹85

Year-end: Mar	FY12	FY13	FY14e	FY15e	FY16e
P/E (x)	6.0	8.7	9.2	8.0	5.9
P/B (x)	0.9	0.9	0.8	0.9	0.8
P/CF (x)	5.1	6.7	6.8	6.3	4.9
EV/Sales (x)	1.0	1.0	0.8	0.8	0.6
EV/EBITDA (x)	5.6	6.3	5.0	4.3	3.0
Dividend yield (%)	4.8	4.8	3.3	5.0	7.6
Dividend payout (%)	28.7	41.9	30.0	40.0	45.0
RoAE (%)	16.0	10.2	9.2	11.6	14.7
RoACE (%)	16.0	11.6	11.0	15.1	19.7
Net Debt/Equity (x)	0.3	0.3	0.3	0.1	0.1
EBIT/Interest (x)	18.8	10.3	8.2	16.3	33.1
EBITDA growth (%)	10.1	(10.4)	3.5	19.9	28.6
EBITDA margin (%)	18.6	15.8	17.0	18.4	20.8
EBIT margin (%)	16.2	13.0	13.8	15.4	18.0
PAT margin (%)	14.2	9.2	9.1	11.3	13.4

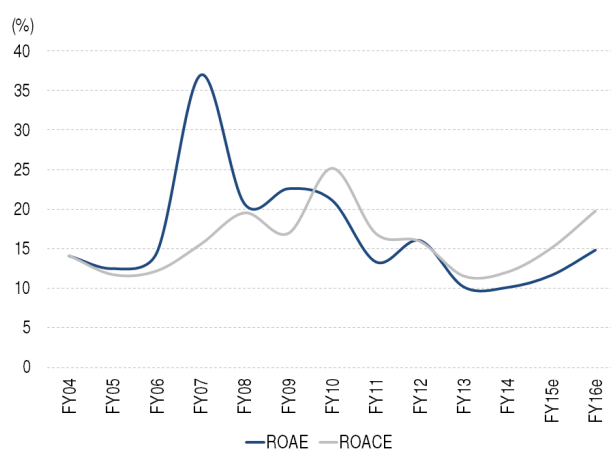
Source: Company, Anand Rathi Research

Fig 5 – Earnings driven by EBITDA margin



Source: Company, Anand Rathi Research

Fig 6 – Stabilizing returns



Source: Company, Anand Rathi Research

Result Highlights

Fig 7 – Results vs Estimates

(₹ m)	4QFY14	4QFY14e	Var%	4QFY13	YoY%	3QFY14	QoQ%
Revenues	4,890	4,202	16.4	5,112	(4.3)	4,345	12.5
EBITDA	682	726	(6.1)	618	10.3	685	(0.5)
EBITDA Margin (%)	13.9	17.3	(334)	12.1	185	15.8	(183)
PAT	449	441	1.9	416	8.1	422	6.6

Source: Company, Anand Rathi Research

With strong sequential volume growth, Graphite India's 4QFY14 results were surprising as the guidance and global peer performance suggested otherwise. 4QFY14 utilisation, at 83%, saw sales volume growth of 4% yoy (16.6k tonnes) after almost six quarters. 4QFY14 realizations declined ~16% yoy pressured by weak demand and lower raw material costs. Sequential realizations are expected to stabilize at current levels. The dollar realization has stabilized sequentially and is expected to hold at similar levels (US\$4,918 a tonne). Average capacity utilization for FY14 was 72%/66% for the Indian/consolidated operations.

The management focus on inventory reduction in graphite electrodes (as evident from high volumes vs margins) would continue to see accelerated cash release over the next 3-6 quarters (~₹1.7bn in working capital reduction in FY14). Due to lower interest expenses and higher other income, PAT grew 8% yoy to ₹441.

We expect the management to surpass its guidance of 70% consolidated utilization in FY15 as domestic demand for graphite electrodes is strong and European steel volumes are picking up (2-3% growth expected in CY14 vs a decline since 2008). The lagged inventory impact would see a strong, 25%, CAGR in EBITDA over FY14-FY16e as lower raw material prices flow through.

We have finetuned our estimates to factor in the USD-INR rate at 60 (earlier at 63) but higher other income has cushioned the impact on the bottom line.

Fig 8 – Standalone details

	1QFY13	2QFY13	3QFY13	4QFY13	1QFY14	2QFY14	3QFY14	4QFY14
Capacity (tonnes)	60,000	60,000	60,000	60,000	80,000	80,000	80,000	80,000
Capacity utilisation (%)	89	91	96	103	67	66	70	83
Production (tonnes)	13,350	13,650	14,400	15,450	13,400	13,200	14,000	16,600
Chg YoY (%)		2.2	5.5	7.3	(13.3)	(1.5)	6.1	18.6
Realization (USD)	5,055	4,972	4,788	5,671	4,957	5,023	4,776	4,281
Chg YoY (%)		(1.7)	(3.7)	18.4	(12.6)	1.3	(4.9)	(10.4)
Revenues (₹m)								
Graphite & Carbon	3,657	3,745	3,733	4,746	3,717	4,111	4,146	4,391
Steel	241	86	245	215	191	182	149	165
Others	338	285	359	151	130	118	50	334
EBIT (₹m)								
Graphite & Carbon	747	544	700	618	778	874	626	663
Steel	4	(6)	14	77	36	6	(2)	80
Others	44	77	(5)	(36)	(8)	(6)	(4)	(4)
Capital Employed (₹m)								
Graphite & Carbon	16,828	17,356	19,377	19,729	18,306	17,991	17,660	16,379
Steel	1,859	1,814	1,863	1,942	1,970	1,980	1,975	2,044
Others	1,048	1,005	1,017	486	444	459	296	446

Source: Company, Anand Rathi Research

Valuations

Graphite India has scale in the global league of graphite electrode operators, with annual production capacity of 98,000 tonnes; ~65% of the production is exported to 30 countries. Strong product knowledge has been built since 1960. Sturdy operating margins driven by operational efficiency, productivity, technology, and access to low-cost sources of power would sustain cash generation during the cycle. At the CMP, the stock trades at 3x FY15e EV/EBITDA and we maintain a Buy on it, with a price target of ₹119 based on 4.5x FY16e EV/EBITDA.

Risks

- Adverse currency movements.
- Sharp raw-material price volatility.

Fig 9 – Valuations

₹ m	FY16e
FY16e EBITDA	4,383
Multiple (x)	4.5
EV	19,724
Net debt	(3,597)
MCAP	23,322
Value per share (₹)	119

Source: Anand Rathi Research

Fig 10 – Business model

	FY08	FY09	FY10	FY11	FY12	FY13	FY14	FY15e	FY16e
Capacity (tonnes)	55,000	55,000	55,000	55,000	60,000	60,000	80,000	80,000	80,000
Chg YoY (%)	0.0	0.0	0.0	0.0	9.1	0.0	0.0	0.0	0.0
Capacity utilisation (%)	132.5	120.4	73.7	102.9	95.4	94.8	71.5	75.0	85.0
Chg YoY (%)	10.0	(9.1)	(38.8)	39.6	(7.3)	(0.7)	(24.5)	4.9	13.3
Production (tonnes)	72,874	66,208	40,529	56,593	57,241	56,850	57,200	60,000	68,000
Chg YoY (%)	10.0	(9.1)	(38.8)	39.6	1.1	(0.7)	0.6	4.9	13.3
Realization (USD/tonne)	3,240	3,233	4,680	4,014	5,190	5,348	4,731	4,542	4,633
Chg YoY (%)	30.7	(0.2)	44.7	(14.2)	29.3	3.1	(11.5)	(4.0)	2.0
Expenses (USD/tonne)	2,928	2,947	3,916	3,657	4,954	4,803	4,290	4,045	4,032
Chg YoY (%)	28.7	0.6	32.9	(6.6)	35.5	(3.0)	(10.7)	(5.7)	(0.3)
EBITDA (USD/tonne)	735	861	1,970	1,096	1,134	901	822	946	1,001
Chg YoY (%)	(6.4)	17.2	128.8	(44.3)	3.4	(20.5)	(8.8)	15.2	5.7

Source: Company, Anand Rathi Research

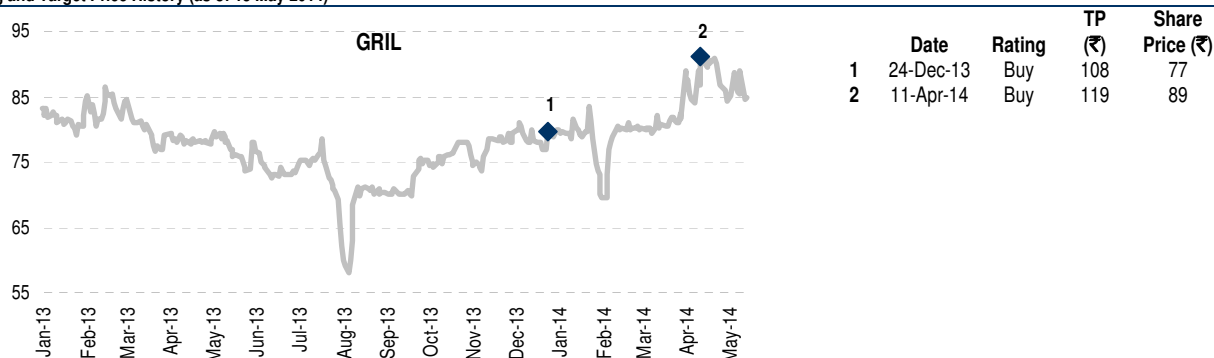
Appendix

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