Institutional Equity Research

Skipper

Capital Goods | India

2QFY18 Result Update | November 24, 2017

CMP (Rs)	262
Upside/ (Downside) (%)	10
Bloomberg Ticker	SKIPPER IN
Market Cap. (Rs bn)	26.9
Free Float (%)	29.6
Shares O/S (mn)	102.3

BUY

Target Price: Rs289

Well-placed in Power Transmission Space

Skipper continued to deliver a strong performance in 2QFY18. Its net revenue grew by 31.9% YoY to Rs5.1bn led by strong volume execution in Engineering Products business. However, GST-led disruption restricted revenue growth in PVC business. Though reported EBITDA dipped by 7.1% YoY to Rs516mn, adjusted EBITDA grew by 19.9% YoY. Owing to lower margin, higher depreciation and tax rate, its reported PAT declined by 30.2% YoY to Rs232mn, while adjusted PAT rose by 3.9% YoY. We continue to believe that a sizeable order book, huge imminent opportunity and diversification into PVC business continue to place Skipper firmly on a higher growth trajectory. **Revising our target multiple to 17x (from 15x earlier) on the back of strong revenue visibility and steady margin profile, we reiterate our BUY recommendation on the stock with a revised Target Price of Rs289 (from Rs254 earlier).**

Engineering Products Biz Aided Strong Revenue Growth

Volume in Engineering Products business – which forms 90% of its total sales – grew by a strong 27.8% to Rs4633.7mn. However, Skipper's PVC revenue – which contributes 8.0% to its total sales – declined by 7.0% YoY to Rs427.8mn owing to GST-led disruptions. Notably, the capacity utilisation level of Engineering Products and Infrastructure Products segments stood at 90% and 50-60%, respectively. Infrastructure Products revenue – which accounts for 1.8% of total sales – declined by 24.4% YoY to Rs94.7mn.

GST Disruptions, Higher Input Prices Impacted Segmental Margins

Owing to higher commodity prices, Skipper's adjusted EBITDA margin declined by 133bps YoY to 13.4%. Margin in Engineering Products business dipped by 150bps YoY to 13.6%, as Skipper executed high-margins projects in 2QFY17. While Infrastructure Products business showed a marginal 40bps YoY rise in EBITDA margin to 15.9%, margin in PVC business dipped by 110bps YoY to 9.3%.

Order Book

Skipper secured new orders worth Rs430mn in 2QFY18 for transmission tower supply. Outstanding order book – which stood at Rs25.8bn as of Sept'17 – is well-diversified between domestic (80%) and international (20%). Notably, order book to sales stands at 2.0x of FY17 sales.

Outlook & Valuation

Looking ahead, we believe that while robust order book provides revenue visibility in T&D business, expansion in PVC business would aid Skipper to sustain healthy earnings profile. We continue to remain positive on Skipper's fundamentals on the back of improved order inflow traction and diversified opportunities in other verticals. We expect Skipper's sales and net profit to witness 21.5% and 24.9% CAGR, respectively through FY17-FY19E, while RoCE is seen at 25.3% by FY19E. **Revising our target multiple to 17x (from 15x earlier), we reiterate our BUY recommendation on the stock with an upwardly revised Target Price of Rs289.**

Key Financials (Rs mn)	FY16	FY17	FY18E	FY19E
Net sales	15,062	17,030	21,373	25,152
PAT	951	1,115	1,295	1,739
EPS (Rs)	9.3	10.9	12.7	17.0
PE (x)	28.2	24.0	20.7	15.4
EV/EBITDA (x)	14.6	12.9	11.0	8.9
Book value (Rs/share)	37.3	48.3	59.3	74.6
P/BV (x)	7.0	5.4	4.4	3.5
ROCE	20.5	20.9	22.5	25.3
RONW	24.9	22.6	21.4	22.8

Source: Company, RSec Research

Share price (%)	1 mth	3 mth	12 mth
Absolute performance	17.4	27.0	90.6
Relative to Nifty	17.3	22.2	62.5

Shareholding Pattern (%)	Jun'17	Sept'17
Promoter	70.4	70.4
Public	29.6	29.6

1 Year Stock Price Performance

*Note: * CMP as on Nov. 24, 2017*

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Risks to the View

- Lower-than-expected order inflows from PGCIL.
- Any significant delay in project execution.

Key Business Highlights

- **JV with Metzerplas for Drip Irrigation Systems:** Skipper's Board of Directors has given in-principal approval to form a JV with Metzerplas, one of the largest and most specialised manufacturers of drip irrigation solutions in Israel. As per the Management, the drip irrigation business holds immense potential in India being one of the focal sectors of the government. The current domestic industry size is pegged at >Rs50bn. Under the flagship scheme Pradhan Mantri Krishi Sinchai Yojna (PMKSY) which has been launched with the aim of extending irrigation cover (Har Khet ko Pani) and improving water use efficiency (Per Drop More Crop), the Company expects this sector to grow at a robust pace.
- **PGCIL's Approval for New Guwahati Plant:** Skipper's newly-built Guwahati plant – having an annual capacity of 30,000MT for engineering products got approval from Power Grid Corporation (PGCIL) for supply of galvanised tower structures/parts. This will enable Skipper to actively support various transmission projects being undertaken by PGCIL in North-East region under NERPSIP scheme alongside large upcoming BOO projects.
- **Focus on Railway Electrification Projects:** Skipper intends to increasingly start bidding for railway electrification projects in strategic alliance with local private players initially. It is in the process of adding more manpower and building capacities to handle all future railways projects. The Company has already started bidding for such projects and is favorably placed to bag its first package valuing Rs160mn.
- **Reduction in Average Cost of Debt:** Considering various cost rationalisation initiatives and overall reduction in interest cost by the banks, the average cost of debt has come down to 8% level.

Exhibit 1: Quarterly Performance

(Rs mn)	2QFY18	1QFY18	QoQ (%)	2QFY17	YoY (%)	6MFY18	6MFY17	YoY (%)
Net Sales	**5,156**	**4,327**	**19.2**	**3,908**	**31.9**	**9,483**	**7,311**	**29.7**
Operating Costs	4,473	3,811	17.4	3,339	34.0	8,284	6,182	34.0
EBITDA	**683**	**516**	**32.3**	**569**	**19.9**	**1,199**	**1,129**	**6.2**
EBITDA Margin (%)	13.2	11.9	1.3	14.6	(1.326)	12.6	15.4	
Other Income	3.3	7.5	(56.6)	7.4	(55.9)	613	660	(7.1)
Interest	200	169	18.8	166	20.6	369	345	7.0
Depreciation	121	108	12.1	72	68.0	228	139	63.7
Profit Before Tax	**365**	**248**	**47.6**	**505**	**(27.7)**	**613**	**660**	**(7.1)**
Tax	133	88		172		221	221	
Tax Rate (%)	36.4	35.5		34.0		36	34	
Reported PAT	**232**	**160**	**45.5**	**333**	**(30.2)**	**392**	**439**	**(10.6)**

Source: Company, RSec Research

Exhibit 2: Segmental Revenues

(Rsmn)	Q2FY18	Q2FY17	YoY (%)	Q1FY18	QoQ (%)	1HFY18	1HFY17	YoY (%)
Revenue								
Engg. Products	4,634	3,627	27.8	3,651	26.9	8,285	6,198	33.7
Polymer Products	428	460	(7.0)	433	(1.2)	861	880	(2.1)
Infrastructure Products	95	125	(24.4)	243	(61.0)	338	233	44.5
TOTAL	**5,156**	**4,212**	**22.4**	**4,327**	**19.2**	**9,484**	**7,311**	**29.7**
EBIT								
Engg. Products	606	660	(8.1)	440	37.9	1,046	989	5.7
Polymer Products	28.2	39.7	(29.0)	30.9	(8.7)	59.7	75.9	(21.3)
Infrastructure Products	11.3	18.7	(39.6)	29.5	(61.7)	40.7	33.5	21.5
EBIT Margin (%)								
Engg. Products	13.1	18.2		12.0		12.6	16.0	
Polymer Products	6.6	8.6		7.1		6.9	8.6	
Infrastructure Products	11.9	14.9		12.2		12.1	14.3	

Source: Company, RSec Research

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Profit & Loss Statement

Y/E March (Rs mn)	FY16	FY17	FY18E	FY19E
Net sales	**15,062**	**17,030**	**21,373**	**25,152**
% yoy change	14.7	13.1	25.5	17.7
Raw Material cost	9,485	10,908	13,486	15,896
Employee expenses	500	732	898	1,044
Other expenses	2,885	2,930	4,168	4,754
Total operating expenditure	**12,870**	**14,569**	**18,551**	**21,694**
EBITDA	**2,192**	**2,460**	**2,821**	**3,458**
EBITDA margin (%)	14.6	14.4	13.2	13.8
Depreciation	241	315	347	362
EBIT	**1,951**	**2,145**	**2,474**	**3,096**
Other income	52	31	33	34
Interest costs	570	611	560	515
PBT	**1,433**	**1,565**	**1,947**	**2,615**
Taxes	482	450	652	876
Tax rate (%)	33.6	28.8	33.5	33.5
Adjusted PAT	**951**	**1,115**	**1,295**	**1,739**

Balance Sheet

Y/E March (Rs mn)	FY16	FY17	FY18E	FY19E
Liabilities				
Share capital	102	102	102	102
Reserves & Surplus	3,712	4,841	5,961	7,526
Total shareholder's funds	**3,815**	**4,943**	**6,063**	**7,628**
Secured loans	1,997	1,780	1,372	1,147
Unsecured loans	3,652	3,304	3,334	3,219
Total borrowings	**5,649**	**5,085**	**4,706**	**4,366**
Deferred tax liability	315	391	391	391
Capital employed	**9,779**	**10,419**	**11,160**	**12,385**
Net Block	3,852	4,642	4,645	4,558
Capital Work in Progress	399	144	400	500
Inventories	2,500	3,682	3,784	4,110
Sundry Debtors	3,724	3,730	3,817	4,573
Cash and Bank	498	249	391	513
Loans and Advances	929	863	1,069	1,132
Total Current Assets	7,651	8,524	9,061	10,328
Current liabilities	2,124	2,891	2,946	3,001
Total current liabilities	2,124	2,891	2,946	3,001
Net Current Assets	**5,527**	**5,633**	**6,115**	**7,327**
Capital Deployed	**9,779**	**10,419**	**11,160**	**12,385**

Cash Flow Statement

Y/E March (Rs mn)	FY16	FY17	FY18E	FY19E
PBT	**1,433**	**1,565**	**1,947**	**2,615**
Depreciation	241	315	347	362
Interest provided	570	611	560	515
Other adjustments	13	263		
Operating CF before WC requirement	**2,257**	**2,755**	**2,854**	**3,493**
Change in working capital	2,401	354	340	1,091
Tax Paid	482	450	652	876
Operating cash flow	**(625)**	**1,951**	**1,862**	**1,526**
FCF	(1,551)	1,101	1,255	1,151
Capex	926	850	606	375
Investing cash flow	**(926)**	**(850)**	**(606)**	**(375)**
Issue/repayment of debt	2,216	(564)	(379)	(340)
Dividends paid	158	174	174	174
Interest paid	(570)	(611)	(560)	(515)
Financing cash flow	**1,488**	**(1,350)**	**(1,113)**	**(1,030)**
Opening cash balance	**561**	**498**	**249**	**391**
Net change in cash	**(63)**	**(249)**	**142**	**122**
Closing cash balance	**498**	**249**	**391**	**513**

Key Ratios

Y/E March	FY16	FY17	FY18E	FY19E
EBITDA margins	14.6	14.4	13.2	13.8
PBT margins	9.5	9.2	9.1	10.4
PAT margins	6.3	6.5	6.1	6.9
ROCE	20.5	20.9	22.5	25.3
RONW	24.9	22.6	21.4	22.8
Debt/Equity Ratio	1.5	1.0	0.8	0.6
EPS	9.3	10.9	12.7	17.0
DPS	1.4	1.6	1.6	1.6
P/E	28.2	24.0	20.7	15.4
PBV	7.0	5.4	4.4	3.5
EV/EBITDA	14.6	12.9	11.0	8.9
EV/Sales	2.1	1.9	1.5	1.2

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Rating Guides

Rating	Expected absolute returns (%) over 12 months
BUY	>10%
HOLD	-5% to 10%
REDUCE	>-5%

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