9 August 2016

Skipper

Tower division delivers, but valuations rich; downgrading to Hold

Rating: **Hold**
Target Price: ₹182
Share Price: ₹158

Though Skipper's cost competitiveness (its locational advantage and backward integration) would ensure that it remains a beneficiary of capex on enhancing transformation capacity, rich valuations, we believe, cap the upside. Meaningful positive FCF too is unlikely to come true in the foreseeable future as its capex continues. Thus, we lower our rating from a Buy to a Hold.

Domestic compensates for lower exports: We estimate export revenues to have dipped on the lower order backlog. However, this seems to have been more than compensated by domestic tower orders to drive overall revenue growth of ~20% yoy. Among verticals, domestic orders led ~21% revenue growth for Engineering products. Polymer products saw growth moderate to ~14% whereas it stood at impressive ~31% for Infrastructure projects.

Healthy profitability: Lower segment margins for the Polymer products division (under absorption of fixed costs; as operations yet stabilising) compressed the overall EBITDA margin ~61bps yoy. Notwithstanding the margin compression, healthy revenue growth combined with contained finance costs (~5.6% of sales; ~6.2% a year ago) and a lower effective tax rate (~32.3%; ~34.7% a year ago) turned earnings growth a healthy ~37%.

Lines up new capex: The board has approved investment to set up a 30,000-tonne tower/distribution-poles manufacturing unit in Guwahati, to take care of greater business prospects in the north-eastern states. A 7,000-tonne CPVC and UPVC fittings unit has also been approved, to act as a feeder unit for high-value products to other polymer units. Investment for these two is pegged at ~₹0.7bn and is targeted to be expensed in FY17.

Valuation: At the CMP, the stock trades at PE of 15.8x FY17e and 13.0x FY18e marginally-revised earnings estimates (to factor in committed capex for the greenfield unit in Guwahati). We value the company at a PE of 15x FY18e and arrive at target price of ~₹182, implying an upside of ~15%. **Risk.** Any significant delay in order awarding.

Key data	SKIPPER IN / SKIP.BO
52-week high / low	₹220 / ₹116
Sensex / Nifty	28085/8678
3-m average volume	$0.3m
Market cap	₹16bn / $242.5m
Shares outstanding	102m

Shareholding pattern (%)	Jun'16	Mar'16	Dec'15
Promoters	72.4	72.4	72.4
- of which, Pledged	-	-	-
Free Float	27.6	27.6	27.6
- Foreign Institutions	0.2	0.2	1.1
- Domestic Institutions	3.0	3.2	0.0
- Public	24.5	24.3	26.5

Estimates revision (%)	FY17e	FY18e
Sales	-0.1	-0.1
EBITDA	0.0	-0.3
EPS	-0.1	-0.3

Financials (YE Mar)	FY17e	FY18e
Sales (₹ m)	17,758	20,481
Net profit (₹ m)	1,023	1,242
EPS (₹)	10.0	12.1
Growth (%)	32.9	21.4
PE (x)	15.8	13.0
PBV (x)	3.5	2.8
RoE (%)	24.1	23.9
RoCE (%)	23.4	24.0
Dividend yield (%)	0.9	0.9
Net debt / equity (x)	1.0	0.8

Source: Anand Rathi Research

Quarterly results (YE Mar)	Q1 FY16	Q1 FY17	% yoy	FY15	FY16	% yoy
Sales (₹ m)	2,367	2,844	20.2	12,708	14,881	17.1
EBITDA margin (%)	14.9	14.3	-60.9bps	13.6	13.5	-11.2bps
Interest (₹ m)	147	160	8.8	583	570	-2.2
Depreciation (₹ m)	59	67	14.7	220	241	9.7
Other income (₹ m)	6	8	26.7	17	52	212.0
Exceptional item (₹ m)	-	15	-	420	181	-56.8
PBT (₹ m)	153	203	31.9	1,366	1,433	4.9
Tax (₹ m)	53	65	22.6	474	482	1.6
Reported. PAT (₹ m)	100	137	36.9	892	951	6.7

Source: Company

Prem Khurana
Research Analyst
+9122 6626 6470
premkhurana@rathi.com

Bhalchandra Shinde
Research Analyst
+9122 6626 6615
bhalchandrashinde@rathi.com

Quick Glance – Financials and Valuations

Fig 1 – Income statement (₹ m)

Year-end: Mar	FY14	FY15	FY16	FY17e	FY18e
Net revenues	10,415	12,708	14,881	17,758	20,481
Revenue growth (%)	15.7	22.0	17.1	19.3	15.3
- Oper. expenses	9,313	10,976	12,870	15,345	17,692
EBIDTA	**1,102**	**1,732**	**2,011**	**2,414**	**2,788**
EBITDA margins (%)	10.6	13.6	13.5	13.6	13.6
- Interest	605	583	570	641	676
- Depreciation	151	220	241	256	286
+ Other income	21	17	52	41	48
- Tax	98	474	482	535	631
Effective tax rate (%)	26.7	50.1	38.5	34.3	33.7
+ Associates / (minorities)	-	-	-	-	-
Adjusted PAT	269	472	770	1,023	1,242
+ Extraordinary items	-	420	181	15	-
Reported PAT	269	892	951	1,038	1,242
Adj. FDEPS (₹ / sh)	2.6	4.6	7.5	10.0	12.1
Adj. FDEPS growth (%)	43.8	75.3	63.2	32.9	21.4

Source: Company, Anand Rathi Research

Fig 2 – Balance sheet (₹ m)

Year-end: Mar	FY14	FY15	FY16	FY17e	FY18e
Share capital	102	102	102	102	102
Reserves & surplus	2,209	2,936	3,713	4,566	5,624
Net worth	2,312	3,039	3,815	4,669	5,727
Total debt	4,395	3,829	4,682	4,999	5,212
Minority interest	-	-	-	-	-
Def. tax liab. (net)	218	265	315	315	315
Capital employed	**6,924**	**7,132**	**8,812**	**9,982**	**11,254**
Net fixed assets	3,456	3,535	4,239	4,623	4,826
Intangible assets	12	12	12	10	8
Investments	-	-	-	-	-
- of which, Liquid	-	-	-	-	-
Working capital	3,193	3,024	4,062	4,943	5,761
Cash	263	561	498	406	659
Capital deployed	**6,924**	**7,132**	**8,812**	**9,982**	**11,254**
Working capital (days)	112	87	100	102	103
Book value (₹ / sh)	22.6	29.7	37.3	45.6	56.0

Source: Company, Anand Rathi Research

Fig 3 – Cash-flow statement (₹ m)

Year-end: Mar	FY14	FY15	FY16	FY17e	FY18e
Adjusted PAT	269	892	951	1,038	1,242
+ Non-cash items	151	220	241	256	286
Cash profit	420	1,112	1,192	1,294	1,528
- Incr. / (decr.) in WC	134	-170	1,038	881	819
Operating cash-flow	286	1,281	154	413	710
- Capex	321	299	946	638	486
Free cash-flow	-35	982	-792	-224	224
- Dividend	18	160	172	184	184
+ Equity raised	-0	-5	-2	-0	-
+ Debt raised	188	-519	903	317	213
- Investments	-	-	-	-	-
- Misc. items	-	-	-	-	-
Net cash-flow	135	298	-63	-107	252
+ Op. cash & bank bal.	128	263	561	498	406
Cl. Cash & bank bal.	263	561	498	406	659

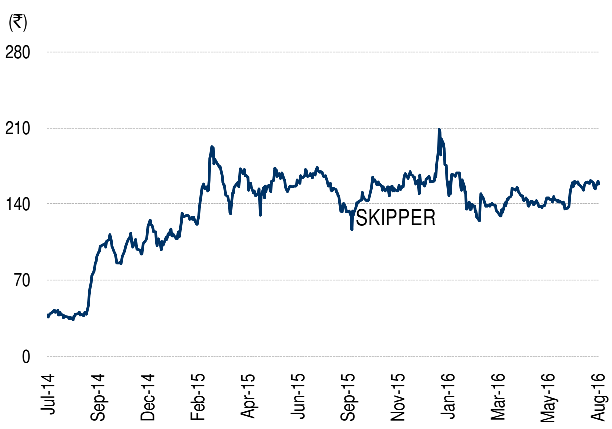
Source: Company, Anand Rathi Research

Fig 4 – Ratio analysis @ ₹158

Year-end: Mar	FY14	FY15	FY16	FY17e	FY18e
P/E (x)	60.2	34.4	21.1	15.8	13.0
Cash P/E (x)	38.6	23.4	16.0	12.7	10.6
EV / EBITDA (x)	18.5	11.2	10.1	8.6	7.4
EV / sales (x)	2.0	1.5	1.4	1.2	1.0
P/B (x)	7.0	5.3	4.2	3.5	2.8
RoE (%)	12.3	17.6	22.5	24.1	23.9
RoCE (%)	14.5	21.7	22.8	23.4	24.0
Dividend yield (%)	0.1	0.8	0.9	0.9	0.9
Dividend payout (%)	6.7	33.9	22.4	18.0	14.8
Net debt / equity (x)	1.8	1.1	1.1	1.0	0.8
Debtor (days)	81	108	91	99	99
Inventory (days)	80	66	61	67	67
Payables (days)	55	69	52	61	61
Interest cover (x)	1.6	2.6	3.2	3.4	3.8
Fixed asset T/O (x)	3.0	3.6	3.5	3.8	4.2

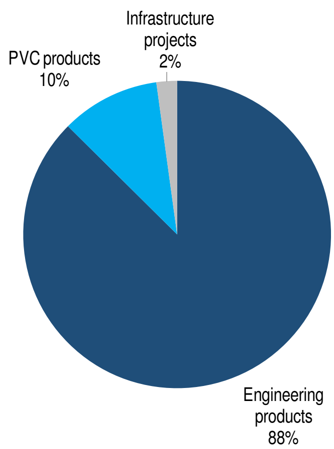
Source: Company, Anand Rathi Research

Fig 5 – Price movement



Source: Bloomberg

Fig 6 – FY16 Revenue break-up



Source: Company

Result / Concall Highlights

- For Q1 FY17, Skipper's Engineering products division (adj. for forex gains) registered ~21% yoy revenue growth and ~51bps margin contraction. On the lower order backlog, we estimate export revenues to have dipped ~20% yoy. Lower export revenues seem to have been more than compensated by domestic revenues. Segment margin shrank owing to the change in the revenue mix.
- For Q1 FY17, revenue growth in the Polymer products eased to ~14% owing to slower off-take by channel partners and delay in dispatch of quantities for two project orders (client approval delayed). With the 6,000-tonne unit commissioned in Hyderabad in Q1 and with operations at units commissioned during FY16 stabilising, revenues are expected to be better in coming quarters. Segment margins compressed by ~245bps yoy to owing to under-absorption of fixed costs for the recently-commissioned units.
- The Infrastructure projects division returned to positive growth after three consecutive quarters of yoy decline. The division registered ~31% yoy revenue growth (on account of new orders) with a ~13.4% margin.
- Volume growth in the Engineering products and the Polymer products divisions was seen to be in line with value growth.

Fig 7 – Segment-wise highlights

(YE: Mar)	Q1 FY16	Q1 FY17	% yoy	Q4 FY16	% qoq	FY15	FY16	% yoy
Segment revenue (₹ m)								
Engineering products	1,951	2,358	20.8	4,659	-49.4	11,348	13,079	15.3
Polymer products	333	378	13.7	558	-32.1	897	1,525	70.0
Infrastructure projects	83	108	30.7	81	34.4	462	277	-40.2
Total	**2,367**	**2,844**	**20.2**	**5,297**	**-46.3**	**12,708**	**14,881**	**17.1**
Segment margins (%)								
Engineering products	15.1	14.6	-	14.5	-	12.2	13.4	-
Polymer products	12.1	9.6	-	9.9	-	11.5	10.8	-
Infrastructure projects	23.4	13.4	-	5.5	-	23.8	15.5	-
Blended	**15.0**	**13.9**	**-**	**13.9**	**-**	**12.6**	**13.2**	**-**

Source: Company
Note: Figures adjusted for forex gain of ~₹15m in Q1 FY17, ~₹181m in FY16 and ~₹420m in FY15

- With modest growth in the Polymer division in Q1, management sees its full-year growth to turn out to be lower than the earlier guided ~70%. Management expects overall revenue growth of ~15-20%.
- Capacity utilisation in the Polymer division was ~90% for the East (Uluberia) and ~55-60% for the West (Ahmedabad). For other units, utilisation levels were below 50% and management expects a gradual ramp-up by Q3 FY17.
- **Capex for the new unit in Guwahati**
  - Apart from locational advantages, fiscal benefits (direct and indirect) that would be available to the unit also played a key role in firming up the capex plan.
  - Management identifies ~₹0.4bn of investment for tower/ distribution poles capacity and another ~₹0.3bn for CPVC and

UPVC fitting capacity.

- Capex (per unit) is on a higher side since it is a greenfield expansion, against the earlier practice of a brownfield expansion for tower-manufacturing capacity and leased facilities for the Polymer products division.
- Management hopes to fund this capex with ~₹450m-500m debt and ~`200-250m internal accruals.

- During the quarter, the company added orders of ~₹2.4bn to the end-FY16 order backlog of ~₹24.9bn. Orders secured during the quarter were a mix of international (~₹1bn) and domestic (~₹1.5bn) orders.
- Nearly 50% of the closing order backlog is from PGCIL, followed by other domestic orders (~25%). The share of exports was ~25%.
- In addition to the orders secured in Q1, management identifies bids under evaluation of ~₹10bn. Of these, bids under evaluation with PGCIL account for ~50%, South East Asian countries ~25% and the rest a mix of domestic and international orders.
- On inflow prospects, management sees meaningful awarding activity domestically (particularly from SEBs). It is eyeing a fair share in transmission-tower orders expected in north-east India under the NERPSIP.
- For geographic diversification, management efforts continue to enhance its international operations and it identifies Kenya, Egypt and South-East Asian countries (Philippines, Vietnam, Malaysia) as the areas with huge potential. However, management remains conscious of margins that it intends to bid with.

Earnings Revision and Valuation

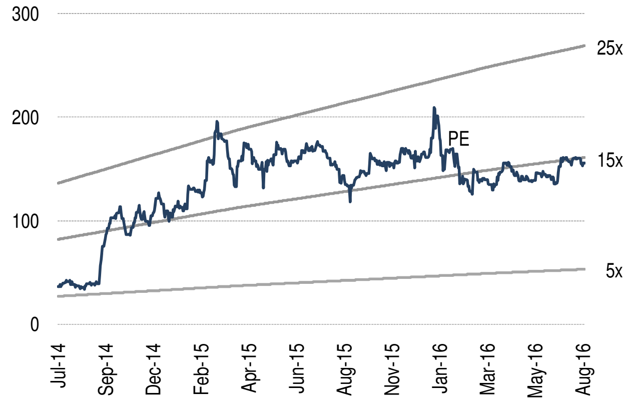
To factor in the new committed capex, we slightly lower our FY17 and FY18 earnings. As operations at the new unit would take time to stabilise, we believe finance costs and depreciation charges would cut into profitability. At the CMP, the stock trades at PE of 15.8x FY17 and 13.0x FY18 revised earnings estimates. We value the company at a PE of 15.0x FY18e and arrive at a target price of ~₹182, implying an upside of ~15%.

Fig 8 – Change in estimates

₹ m	Original Estimates		Revised Estimates		Change (%)	
	FY17e	FY18e	FY17e	FY18e	FY17e	FY18e
Revenue	17,777	20,502	17,758	20,481	-0.1	-0.1
EBITDA	2,413	2,798	2,414	2,788	0.0	-0.3
EPS (₹)	10.0	12.2	10.0	12.1	-0.1	-0.3

Source: Anand Rathi Research

Fig 9 – PE band



Source: Bloomberg, Company, Anand Rathi Research

Risk

- Any significant delay in order awarding.
- Failure of the performance of the Polymer division to improve.

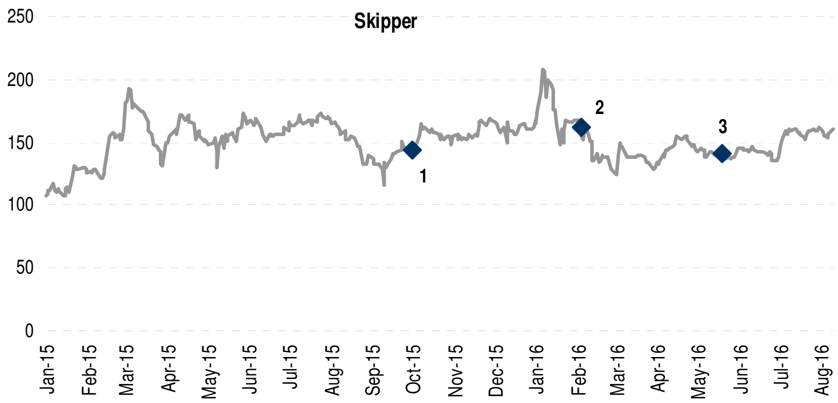
Appendix

Analyst Certification

The views expressed in this Research Report accurately reflect the personal views of the analyst(s) about the subject securities or issuers and no part of the compensation of the research analyst(s) was, is, or will be directly or indirectly related to the specific recommendations or views expressed by the research analyst(s) in this report. The research analysts are bound by stringent internal regulations and also legal and statutory requirements of the Securities and Exchange Board of India (hereinafter "SEBI") and the analysts' compensation are completely delinked from all the other companies and/or entities of Anand Rathi, and have no bearing whatsoever on any recommendation that they have given in the Research Report.

Important Disclosures on subject companies

Rating and Target Price History (as of 9 August 2016)



	Date	Rating	TP (₹)	Share Price (₹)
1	29-Sep-15	Buy	204	145
2	02-Feb-16	Hold	182	170
3	18-May-16	Hold	183	142

Anand Rathi Ratings Definitions

Analysts' ratings and the corresponding expected returns take into account our definitions of Large Caps (>US$1bn) and Mid/Small Caps (<US$1bn) as described in the Ratings Table below:

Ratings Guide (12 months)

	Buy	Hold	Sell
Large Caps (>US$1bn)	>15%	5-15%	<5%
Mid/Small Caps (<US$1bn)	>25%	5-25%	<5%

Research Disclaimer and Disclosure inter-alia as required under Securities and Exchange Board of India (Research Analysts) Regulations, 2014

Anand Rathi Share and Stock Brokers Ltd. (hereinafter refer as ARSSBL) (Research Entity) is a subsidiary of Anand Rathi Financial Services Ltd. ARSSBL is a corporate trading and clearing member of Bombay Stock Exchange Ltd, National Stock Exchange of India Ltd. (NSEIL), Multi Stock Exchange of India Ltd (MCX-SX), United Stock Exchange and also depository participant with National Securities Depository Ltd (NSDL) and Central Depository Services Ltd. ARSSBL is engaged in the business of Stock Broking, Depository Participant and Mutual Fund distributor.

The research analysts, strategists, or research associates principally responsible for the preparation of Anand Rathi research have received compensation based upon various factors, including quality of research, investor client feedback, stock picking, competitive factors and firm revenues.

General Disclaimer: This Research Report (hereinafter called "Report") is meant solely for use by the recipient and is not for circulation. This Report does not constitute a personal recommendation or take into account the particular investment objectives, financial situations, or needs of individual clients. The recommendations, if any, made herein are expression of views and/or opinions and should not be deemed or construed to be neither advice for the purpose of purchase or sale of any security, derivatives or any other security through ARSSBL nor any solicitation or offering of any investment /trading opportunity on behalf of the issuer(s) of the respective security (ies) referred to herein. These information / opinions / views are not meant to serve as a professional investment guide for the readers. No action is solicited based upon the information provided herein. Recipients of this Report should rely on information/data arising out of their own investigations. Readers are advised to seek independent professional advice and arrive at an informed trading/investment decision before executing any trades or making any investments. This Report has been prepared on the basis of publicly available information, internally developed data and other sources believed by ARSSBL to be reliable. ARSSBL or its directors, employees, affiliates or representatives do not assume any responsibility for, or warrant the accuracy, completeness, adequacy and reliability of such information / opinions / views. While due care has been taken to ensure that the disclosures and opinions given are fair and reasonable, none of the directors, employees, affiliates or representatives of ARSSBL shall be liable for any direct, indirect, special, incidental, consequential, punitive or exemplary damages, including lost profits arising in any way whatsoever from the information / opinions / views contained in this Report. The price and value of the investments referred to in this Report and the income from them may go down as well as up, and investors may realize losses on any investments. Past performance is not a guide for future performance. ARSSBL does not provide tax advice to its clients, and all investors are strongly advised to consult with their tax advisers regarding taxation aspects of any potential investment.

Opinions expressed are our current opinions as of the date appearing on this Research only. We do not undertake to advise you as to any change of our views expressed in this Report. Research Report may differ between ARSSBL's RAs and/ or ARSSBL's associate companies on account of differences in research methodology, personal judgment and difference in time horizons for which recommendations are made. User should keep this risk in mind and not hold ARSSBL, its employees and associates responsible for any losses, damages of any type whatsoever.

ARSSBL and its associates or employees may; (a) from time to time, have long or short positions in, and buy or sell the investments in/ security of company (ies) mentioned herein or (b) be engaged in any other transaction involving such investments/ securities of company (ies) discussed herein or act as advisor or lender / borrower to such company (ies) these and other activities of ARSSBL and its associates or employees may not be construed as potential conflict of interest with respect to any recommendation and related information and opinions. Without limiting any of the foregoing, in no event shall ARSSBL and its associates or employees or any third party involved in, or related to computing or compiling the information have any liability for any damages of any kind.

Details of Associates of ARSSBL and Brief History of Disciplinary action by regulatory authorities & its associates are available on our website i.e. www.rathionline.com

Disclaimers in respect of jurisdiction: This report is not directed to, or intended for distribution to or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction where such distribution, publication, availability or use would be contrary to law or regulation or which would subject ARSSBL to any registration or licensing requirement within such jurisdiction(s). No action has been or will be taken by ARSSBL in any jurisdiction (other than India), where any action for such purpose(s) is required. Accordingly, this Report shall not be possessed, circulated and/or distributed in any such country or jurisdiction unless such action is in compliance with all applicable laws and regulations of such country or jurisdiction. ARSSBL requires such recipient to inform himself about and to observe any restrictions at his own expense, without any liability to ARSSBL. Any dispute arising out of this Report shall be subject to the exclusive jurisdiction of the Courts in India.

Statements on ownership and material conflicts of interest, compensation - ARSSBL and Associates

Answers to the Best of the knowledge and belief of ARSSBL/ its Associates/ Research Analyst who is preparing this report

ARSSBL/its Associates/ Research Analyst/ his Relative have actual/beneficial ownership of one per cent or more securities of the subject company, at the end of the month immediately preceding the date of publication of the research report?	No
ARSSBL/its Associates/ Research Analyst/ his Relative have actual/beneficial ownership of one per cent or more securities of the subject company	No
ARSSBL/its Associates/ Research Analyst/ his Relative have any other material conflict of interest at the time of publication of the research report?	No
ARSSBL/its Associates/ Research Analyst/ his Relative have received any compensation from the subject company in the past twelve months	No
ARSSBL/its Associates/ Research Analyst/ his Relative have managed or co-managed public offering of securities for the subject company in the past twelve months	No
ARSSBL/its Associates/ Research Analyst/ his Relative have received any compensation for investment banking or merchant banking or brokerage services from the subject company in the past twelve months	No
ARSSBL/its Associates/ Research Analyst/ his Relative have received any compensation for products or services other than investment banking or merchant banking or brokerage services from the subject company in the past twelve months	No
ARSSBL/its Associates/ Research Analyst/ his Relative have received any compensation or other benefits from the subject company or third party in connection with the research report	No
ARSSBL/its Associates/ Research Analyst/ his Relative have served as an officer, director or employee of the subject company.	No

Other Disclosures pertaining to distribution of research in the United States of America

This report was prepared, approved, published and distributed by the Anand Rathi Share and Stock Brokers Limited (ARSSBL) located outside of the United States (a "non-US Group Company"). This report is distributed in the U.S. by Enclave Capital LLC, a U.S. registered broker dealer, on behalf of ARSSBL only to major U.S. institutional investors (as defined in Rule 15a-6 under the U.S. Securities Exchange Act of 1934 (the "Exchange Act")) pursuant to the exemption in Rule 15a-6 and any transaction effected by a U.S. customer in the securities described in this report must be effected through Enclave Capital. ARSSBL accepts responsibility for its contents. Any US customer wishing to effect transactions in any securities referred to herein or options thereon should do so only by contacting a representative of Enclave Capital LLC at 646-454-8600

Neither the report nor any analyst who prepared or approved the report is subject to U.S. legal requirements or the Financial Industry Regulatory Authority, Inc. ("FINRA") or other regulatory requirements pertaining to research reports or research analysts. No non-US Group Company is registered as a broker-dealer under the Exchange Act or is a member of the Financial Industry Regulatory Authority, Inc. or any other U.S. self-regulatory organization.

This material was produced by ARSSBL, solely for information purposes and for the use of the recipient. It is not to be reproduced under any circumstances and is not to be copied or made available to any person other than the recipient. It is distributed in the United States of America by Enclave Capital LLC (19 West 44th Street, Suite 1700, New York, NY 10036) and elsewhere in the world by ARSSBL or an authorized affiliate of ARSSBL (such entities and any other entity, directly or indirectly, controlled by ARSSBL, the "Affiliates"). This document does not constitute an offer of, or an invitation by or on behalf of ARSSBL or its Affiliates or any other company to any person, to buy or sell any security. The information contained herein has been obtained from published information and other sources, which ARSSBL or its Affiliates consider to be reliable. None of ARSSBL or its Affiliates accepts any liability or responsibility whatsoever for the accuracy or completeness of any such information. All estimates, expressions of opinion and other subjective judgments contained herein are made as of the date of this document. Emerging securities markets may be subject to risks significantly higher than more established markets. In particular, the political and economic environment, company practices and market prices and volumes may be subject to significant variations. The ability to assess such risks may also be limited due to significantly lower information quantity and quality. By accepting this document, you agree to be bound by all the foregoing provisions.

1. ARSSBL or its Affiliates may or may not have been beneficial owners of the securities mentioned in this report.

2. ARSSBL or its affiliates may have or not managed or co-managed a public offering of the securities mentioned in the report in the past 12 months.

3. ARSSBL or its affiliates may have or not received compensation for investment banking services from the issuer of these securities in the past 12 months and do not expect to receive compensation for investment banking services from the issuer of these securities within the next three months.

4. However, one or more of ARSSBL or its Affiliates may, from time to time, have a long or short position in any of the securities mentioned herein and may buy or sell those securities or options thereon, either on their own account or on behalf of their clients.

5. As of the publication of this report, ARSSBL does not make a market in the subject securities.

6. ARSSBL or its Affiliates may or may not, to the extent permitted by law, act upon or use the above material or the conclusions stated above, or the research or analysis on which they are based before the material is published to recipients and from time to time, provide investment banking, investment management or other services for or solicit to seek to obtain investment banking, or other securities business from, any entity referred to in this report.

Enclave Capital LLC is distributing this document in the United States of America. ARSSBL accepts responsibility for its contents. Any US customer wishing to effect transactions in any securities referred to herein or options thereon should do so only by contacting a representative of Enclave Capital LLC.

Additional information on recommended securities/instruments is available on request.

ARSSBL registered address: 4th Floor, Silver Metropolis, Jaicoach Compound, Opposite Bimbisar Nagar, Goregaon (East), Mumbai - 400 063.
Tel No: +91 22 4001 3700 | Fax No: +91 22 4001 3770 | CIN: U67120MH1991PLC064106.