



Maharashtra Seamless :: Seamless turnaround.



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Our Take

Maharashtra Seamless Ltd. one of India's leading seamless & ERW pipe manufacturer with a mammoth capacity of 5,50,000 Tonnes per annum is set to benefit from the following:

- 1) Demand ramp up due to growth in Oil & Gas industries Capex(ex Ril) from 66000 crs (12-17) to 82000 crs.(17-20)
- 2) Anti-Dumping duty on imports of seamless pipes from China for the next 5 years.
- 3) Weak financial state of its major domestic competitors namely Jindal Saw & ISMT.
- 4) Large scope of production ramp-up with fy17 utilizations below 40%.

At current price of Rs. 449 Maharashtra Seamless Ltd. trades at 12.03x FY19E EPS of Rs. 37.32, we believe that strong demand, coupled with high operating leverage, curtailed domestic & Chinese competition can massively benefit this company and re-rating of this stock is a no brainer. **We assign a PE multiple of 16x to our estimated FY19 EPS of Rs.37.32 and give a target of Rs. 597 for the stock. An upside 33% in 12-18 months.**

Business Summary

Maharashtra Seamless Limited (MSL) incorporated on May 10, 1988 belonging to the D.P Jindal group is a leading manufacturer of Seamless and ERW carbon & alloy steel pipes and tubes in India. MSL has 2 plants located in Nagothane and Mangaon, about 100 km's from Mumbai. Both seamless & ERW plants have a technical collaboration with SMS MEER (earlier known as Mannesmann Demag) of Germany.

What is a seamless pipe?

Seamless Steel Pipe is made from a solid round steel 'billet' which is heated and pushed or pulled over a form until the steel is shaped into a hollow tube. These pipes are known for withstanding higher amount of pressure, temperature and corrosive atmosphere.

What is an ERW pipe?

Electric Resistance Welding (ERW) pipe is manufactured by rolling metal and then welding it longitudinally across its length. ERW pipe have a welded joint in its cross-section, while seamless pipe does not have any joint in its cross-section through-out its length.

Application :

Maharashtra Seamless' products predominantly cater to Oil & Gas Industry. **Carbon/Alloy steel seamless pipes** find their application in Oil & gas drilling, casing, tubing, refineries, power, Whereas **ERW pipes** are used for short distance oil & gas/ water transportation.

Business Verticals**1) Steel Pipes and Tubes (96% of FY17 revenues)****a) Seamless pipes and tubes** (79% of the Steel Pipes and Tubes segmental revenue)

These pipes are known for withstanding higher amount of pressure, temperature and corrosive atmosphere. It is used mainly for oil and gas drilling, casing, tubing, refineries, power. There is a drastic reduction in the competitive intensity due to the anti-dumping duty on the Chinese seamless pipes. 'MAHA' is a globally recognized brand for seamless pipes.

b) ERW pipes and tubes (21% of the Steel Pipes and Tubes segmental Revenue)

The raw material of this pipe is steel coils which have been procured from Steel Authority of India (SAIL). ERW pipes are formed by cold forming of steel coil into cylindrical shape. They are mainly used in agriculture, oil and gas, housing, engineering sectors. 'Jindal Star' enjoys brand leadership in the ERW segment.

2) Power and electricity (3% of FY17 revenues)

MSL has commissioned a new solar project in Rajasthan and are planning a 12 MW captive solar project for the seamless and welded facilities in Nagothane. This will reduce the cost of power and make them more cost competitive. The company generates 27% power through renewable energy sources (Wind Power & Solar Power) equivalent to its total electricity consumption of FY 2016-17.

Investment Highlights

1) Oil and Gas industry CAPEX in India is seeing revival from stagnation in the previous few years to meet BS VI standards by 2020. Investments in domestic oil & gas exploration and refinery space is expected to go up from INR 66,000 cr in 2012-17 to average INR 82,000cr in the period from 2017-20. Seamless tubes industry– carbon and stainless steel combined, which constitutes about 8-12% of the overall capex in either exploration or refineries, is set to be a large beneficiary of the underlying capex momentum.

2) High operating leverage:

Maharashtra seamless has a total capacity of 5,50,000 tonnes spanning across 2 units however the Mangaon facility with 2,00,000 tonnes capacity had been shut due to demand constraint and utilization levels have remained under 50% in previous few years thereby leaving a high scope for production ramp up in changing industry dynamics. The Mangaon facility it has been revived in Q1FY17. FY17 witnessed ~2,09,000 tonnes of production which is expected to clock 2,90,000 & 3,77,000 respectively in FY18E & FY19E. In tandem with the demand growth seamless pipes production stood at 70,184 units in FY 18 an increase of 48.67% Q-o-Q basis.

3) Anti-Dumping Duty imposed on Seamless Pipes and Tubes from China

Government of India imposed an anti-dumping on imports of seamless pipes and tubes from China in February, 2017 for a period of 5 years. The levy has been imposed in the range of \$961.33 to \$1,610.67 which would eliminate the injury caused to domestic players by the unfair trade practices of dumping. Imposing of the duty might affect the realization level which stood ~ Rs. 53000 (as guided by the management) in FY 17. Management is confident about the realizations being above current levels in the range of ~ Rs 58000 – Rs 62000 in FY 18 on expectation of revival of Oil & Gas industry backed by anti-dumping duty. Competition from Japanese & Korean players persists however it is healthy competition and shall not impact Maharashtra seamless' margins.

4) MSL positioned substantially better than its competitors

Domestic competitors include ISMT and Jindal Saw. ISMT has excessively decreased its production volumes to ~80,000 tonnes and continues to remain under corporate debt restructuring. Jindal Saw volume also declined in forgone years along with heavy debt burden of ~5500 Cr Rs and debt to equity ratio of 1.1 & also product categories of Jindal saw & Maharashtra seamless have a good amount of distinction with a few overlaps.

Companies	Installed Capacity FY 17	Volumes FY 14	Volumes FY 17
Maharashtra Seamless	5,50,000	1,52,629	2,09,211
ISMT	4,75,000	1,45,052	*80,000
Jindal Saw	2,25,000	~1,28,000	*80,000

* Estimates for FY 17

Investment Highlights (Cont.)**5) Healthy order book**

The order book of the company as on August 22, 2017 stood at 652 Cr Rs with seamless pipes contributing around 502 Cr Rs (77% of the order book) and remaining order for ERW pipes at 150 Cr Rs (23% of the order book). The export to domestic ratio stood at 17:83 in terms of pipes breakup. With Q1FY18 reporting a top-line of Rs.481 crs. & an order book of Rs. 652 Crs. There is a clear visibility of 1133 Crs. For FY18E already in 2nd quarter as compared to the annual top-line of Rs.1433 Crs

Key Risks**1) Delay in Capex in ONGC & Oil India**

MSL is ideally positioned to benefit from the expected capex from ONGC/OIL in India as 2/3 of its revenue comes from Oil & Gas sector. As a thumb rule, capex for carbon seamless pipes is around 8% - 12% of the total spend for exploration activity. A delay in CAPEX plans for oil giants, essentially means delay in growth for the company.

Also, if the size of the CAPEX by oil companies turns out to be smaller than expected there could be a change in expected production numbers thereby affecting topline of the company.

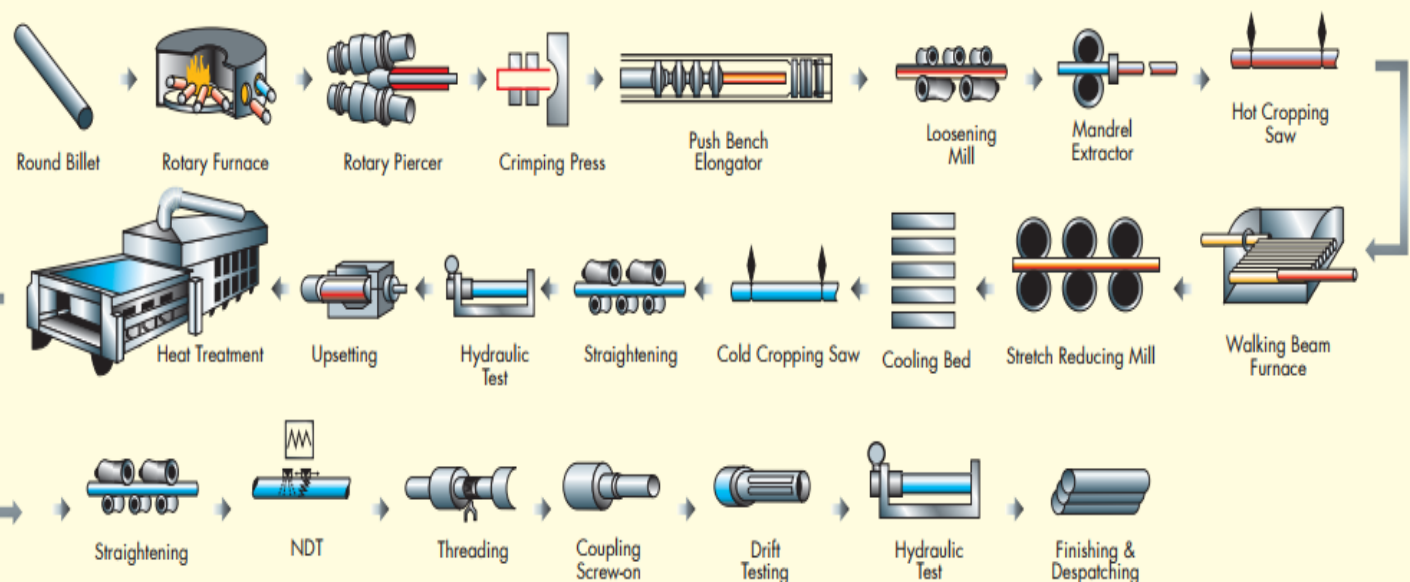
2) Other notable risks

- Stiffening of competition from Japanese & Korean international players dragging margins.
- Oil rigs held by subsidiaries remain un-operational beyond estimated time, stretching the balance sheet further, continuing to dilute return ratios

Business Process Flow

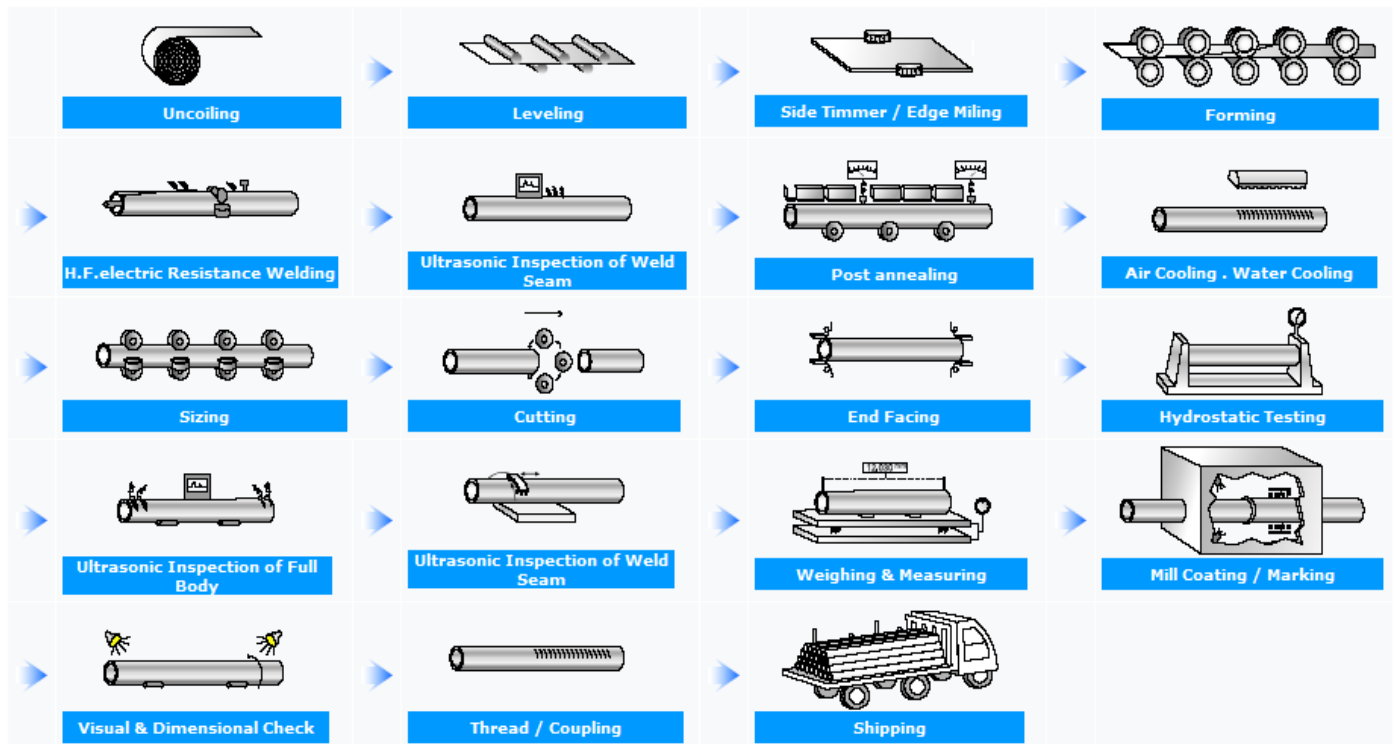
1) Seamless Pipes Process

CPE PROCESS



The CPE (Cross Roll Piercing and Elongation) process begins with the piercing of a hot billet on the piercer, followed by crimping and then elongation on the push-bench. Finally, the dimensions are controlled within specified variation on the stretch reducing mill (SRM). This process minimizes longitudinal and transverse defects in pipes and tubes. It also ensures better control over wall thickness variation as compared to other manufacturing process.

2) ERW Pipes Process



Maharashtra Seamless Limited (MSL) as an ERW pipe manufacturer in India, manufacture ERW pipes (MS Black and Galvanized) in various sizes, grades and specifications as per various national and international specifications (IS, BS API, ASTM, DIN) ranging from 1/2" to 20" with wall thickness ranging from 2mm to 12.7mm. ERW pipe manufacturing plant having maximum welding speed of 33 meters per minute with an installed capacity of 2,00,000 MT per annum. JINDAL STAR ERW Steel Pipes are serving the Oil and Gas Sector, including Cross Country Pipelines. These pipes are also utilized in petrochemical industries, re-neries, water and sewage applications.

Financials

Profit & Loss Account (RS CR)	FY 19E	FY 18E	FY 17	FY 16
Net Revenue	2719.1	2160.7	1433.4	1017.8
Other Income	90.0	78.9	77.2	90.4
Total Income	2809.1	2239.6	1510.6	1108.2
COGS	1868.4	1495.0	920.9	739.5
Employee Expenses	85.0	65.1	52.7	46.7
Other Expenses	356.9	285.4	235.6	193.8
Total Expenses	2310.3	1845.5	1209.1	980.1
EBIDTA (Excl other income)	408.7	315.2	224.3	131.9
OPM (Excl other income)	0.2	0.1	0.1	0.1
EBIDTA (Inc other income)	498.7	394.1	301.5	128.2
OPM (inc other income)	0.2	0.2	0.2	0.1
Depreciation	71.0	70.6	70.6	71.1
PBIT	427.7	323.5	230.9	57.1
Financial Expenses	43.0	37.0	33.9	26.0
PBT	384.7	286.5	197.0	31.0
Provision for Tax	134.7	100.3	80.5	22.8
Tax %	0.4	0.4	0.4	0.7
PAT (Before Minority interest)	250.1	186.2	116.5	8.2
Profit/loss in association	0.0	0.0	0.0	-32.3
Minority Interest	0.0	0.0	0.0	
PAT (after minority interest)	250.1	186.2	116.4	-24.1
PAT Margin	0.1	0.1	0.1	0.0
Other Comprehensive Income	0.0	0.0	5.5	1.5
Total Income	250.1	186.2	122.0	-22.6
EPS	37.3	27.8	18.2	-3.4

Balance Sheet (in Rs Cr0)	FY19E	FY18E	FY 17	FY 16
Equity Share Capital	96.1	96.1	96.1	96.1
Reserves & Surplus	3,086.6	2,836.5	2,650.3	2,549.5
Net worth	3,182.7	2,932.6	2,746.4	2,645.6
Long term debt	160.0	170.0	179.8	272.0
Short term debt	632.8	506.0	460.2	298.8
Total debt	792.8	676.0	640.0	570.8
Total capital employed	3,975.5	3,608.6	3,386.3	3,216.3
Fixed Assets	1,135.0	1,175.0	1,214.0	1,152.0
Current Assets	1,992.0	1,595.0	1,437.1	1,435.5
Cash & Cash Equivalents	310.0	72.0	4.4	2.8
Non-Current Assets	1,363.5	1,299.6	1,205.0	1,096.2
Current Liabilities	263.0	209.0	217.5	202.9
Non-Current Liabilities	252.0	252.0	252.3	264.5
Net Working Capital	1,419.0	1,314.0	1,215.1	1,229.9
Total Capital Deployed	3,975.5	3,608.6	3,386.3	3,216.3

Financials

Cash flows (Rs. Crs.)	FY19E	FY18E	FY17	FY16
Net Profit	250.07	186.23	116.44	-24.10
Add: Depreciation	71	70.59	70.59	71.1
Add: Misc expenses Written Off	0	0	15	-11
Add: Deferred Tax	0	0	147	7
Gross Cashflow	321.07	256.82	349.03	43.00
Less: Changes in Wcap	105.00	98.86	-14.73	-50.00
Operating Cash Flow	216.07	157.95	334.30	-7.00
Less: Capex	30	30	343	0
Free Cash Flow	186.07	127.95	-8.70	-7.00

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