

# Gandhi Special Tubes (GANSPE)

**₹ 370**

## Steady growth trajectory lies ahead...

- Gandhi Special Tubes (GST) reported a healthy performance in Q2FY19 with net sales for the quarter coming in at ₹ 33.6 crore, up 12.9% YoY. Corresponding EBITDA in Q2FY19 was at ₹ 12.9 crore with subsequent EBITDA margins at 38.3%, flat YoY
- PAT in Q2FY19 was at ₹ 10.0 crore, up 15.1% YoY
- Topline growth of 12.9% can be considered a temporary blip vs. ~30% in last three quarters (Q3FY18, Q4FY18 & Q1FY19). The management attributed it to fewer working days in the quarter with trend normalising, going forward, from Q3FY19 onwards
- GST holds >20% of MCap in cash on its books. With no substantial capex plans in place amid ~70% capacity utilisation levels, GST intends to share the surplus cash with shareholders through greater dividends and buybacks, going forward

### Focus on farm income to aid farm mechanisation play; GST to benefit

The current political will domestically, is to address the plight of farmers through various productivity as well as marketing initiatives. On the one hand, the government is increasing allocation towards irrigation projects, promoting micro irrigation (increases yield by ~20%), increasing MSPs, increasing penetration of farm insurance, etc. On the other hand, it is integrating domestic mandis through electronic platform to garner better price for farm produce. These initiatives are aimed at augmenting farm income and de-risking their income from the vagaries of monsoons. More recently, many new state governments have rolled out schemes for farm loan waiver aggregating >₹ 50,000 crore. Though structurally flawed, they can boost farmer spending, especially on tractors that have been at the forefront of farm mechanisation in India. GST's small diameter tubes find application in tractors. Hence, they stand to gain from increase in farm income & consequent spend on farm equipment (tractor).

### GST key beneficiary of infra activity pick, end use in capital equipment

GST is a manufacturer of small diameter seamless and welded steel tubes, which find application in automotive, hydraulics, refrigeration and other engineering services. In the automotive space, the company's products find application as fuel injection tubes in the tractor segment. In hydraulics, the company's products find application in material (bulk) handling equipment (including cranes), which are used for construction & mining purposes. In the hydraulics segment, GST's clientele includes L&T, BEML, Bhel and Bosch Rexroth India, among others. Welded steel tubes find application in refrigeration and automobile (fuel lines, oil lines & air brake lines) segments. Thus, with uptick in domestic industrial activity, GST is on a strong footing with robust business prospects, going forward.

### Healthy growth prospects, robust return ratios, un-levered B/S, value buy

With healthy tractor as well as capital equipment sales domestically, GST is on a healthy growth trajectory with bright prospects, going forward. It has a cash surplus balance sheet (>₹ 100 crore, ~20% of MCap) and has been generous in sharing the same with shareholders with dividend payout in excess of 35% and share buyback in the past at ₹ 500/share. We believe the management will continue to do so, going forward, and offer attractive dividend yield of ~2.5%. Going forward, we expect sales & PAT to grow at a CAGR of 16.5% and 19.4%, respectively, in FY18-20E. We value the company at ₹ 450 i.e. 13x P/E on FY20E EPS of ₹ 34.6 and maintain our **BUY** rating on the stock. We also derive comfort from healthy return ratios (RoCE>25%, RoIC>50%) and CFO yield of ~8%.

Rating matrix	
Rating	: Buy
Target	: ₹ 450
Target Period	: 12-18 months
Potential Upside	: 22%

What's changed?	
Target	Changed from ₹ 535 to ₹ 450
EPS FY19E	Changed from ₹ 31.9 to ₹ 30.2
EPS FY20E	Changed from ₹ 35.7 to ₹ 34.5
Rating	Unchanged

Key financials				
₹ crore	FY17	FY18	FY19E	FY20E
Net Sales	94.3	113.9	134.4	154.6
EBITDA	32.9	41.1	52.0	59.5
Net Profit	29.7	33.6	41.7	47.8
EPS (₹)	20.2	24.3	30.2	34.6

Valuation summary				
	FY17	FY18	FY19E	FY20E
P/E	18.3	15.2	12.3	10.7
Target P/E	22.3	18.5	14.9	13.0
EV / EBITDA	12.6	9.9	7.6	6.3
P/BV	3.0	2.9	2.6	2.3
RoNW	16.6	18.9	20.9	21.4
RoCE	19.9	24.4	27.1	27.5
RoIC	31.8	45.4	51.6	57.0

Stock data	
Stock Data	
Market Capitalization	₹ 511 crore
Total Debt (FY18)	₹ 0 crore
Cash and Cash Equivalent (FY18)	₹ 105 crore
EV	₹ 407 crore
52 week H/L	445 / 340
Equity Capital	₹ 6.9 crore
Face Value	₹ 5
MF Holding (%)	0.0
FII Holding (%)	1.9

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## Company Analysis

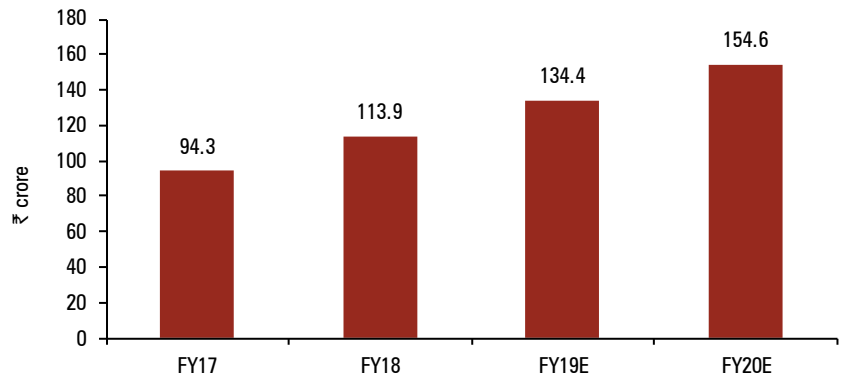
Gandhi Special Tubes (GST) is a manufacturer of small diameter seamless and welded steel tubes, which find application in automotive, hydraulics, refrigeration (condenser tubes) and other engineering services. The company commenced operations at its Halol (Gujarat) Plant in 1988 and was set up in technical collaboration with Benteler (Germany). GST also manufactures cold formed tube nuts for fuel injection tube assemblies, hydraulic & other tube assemblies, which act as an auxiliary unit for its seamless tube segment. In the automotive space, GST's products find application as fuel injection tubes in the M&HCV segment including tractors. In hydraulics, the company's products find application in material (bulk) handling equipment. Welded steel tubes find application in the refrigeration and automobile (fuel lines, oil lines etc) segments.

GST also owns ~5.3 MW of wind power capacity in India with wind plants based out of Gujarat and Maharashtra. In Gujarat, the generated wind power is consumed captively while in Maharashtra, the generated wind power is sold to the state grid.

### Sales to grow 16.5% CAGR in FY18-20E

We expect GST to clock revenue growth of 16.5% CAGR in FY18-20E, primarily on a pick-up in tractor sales domestically and rebound being witnessed in bulk handling equipment space. We expect the company to clock sales of ₹ 134.4 crore in FY19E & ₹ 154.6 crore in FY20E.

**Exhibit 1: Sales trend**

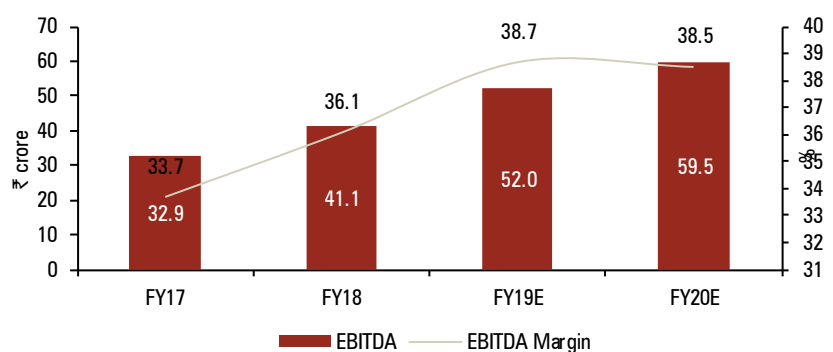


Source: Company, ICICI Direct Research

### Margin expansion under way, EBITDA to grow at 20.4% CAGR in FY18-20

GST recorded a 240 bps improvement in EBITDA margin in FY18 with corresponding EBITDA margin at 36.1%. It was largely tracking lower power & fuel costs and lower other expenses. Gaining further on its expertise of managing the raw material costs amid operating leverage benefits that kick in on account of better capacity utilisation levels, we expect EBITDA margins to further expand to 38.5% by FY20E.

**Exhibit 2: EBITDA & EBITDA margin trend**

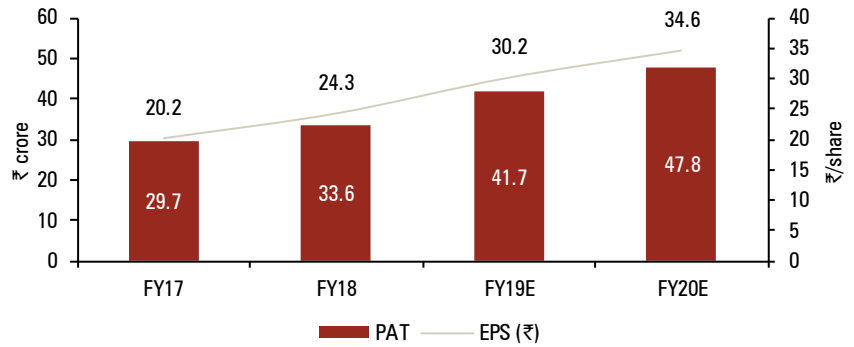


Source: Company, ICICI Direct Research

### PAT to grow at 19.4% CAGR in FY18-20E

PAT is expected to grow at a CAGR of 19.4% in FY18-20E. PAT growth is also supported by tax benefits available to company following the Union Budget 2018-19 (effective tax rate at ~25% for MSME with turnover less than ₹ 250 crore as of FY17)

**Exhibit 3: PAT & EPS trend**

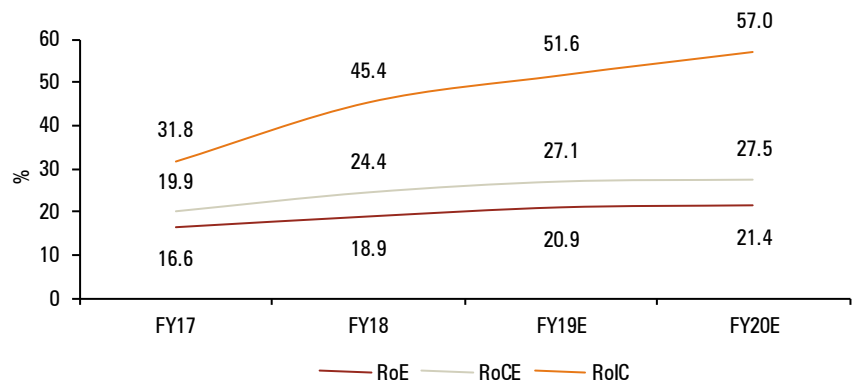


Source: Company, ICICI Direct Research

### Impressive return ratios; RoCE > 24% & RoIC's > 45% over FY18-20E

Return ratios are expected to remain in an uptrend as the capacity utilisation increases amidst robust demand prospects. RoE & RoCE over FY18-20E are expected at ~20% & ~25%, respectively. On account of surplus cash on books and no incremental capex, RoIC in the aforesaid period is expected to be in excess of 50%.

**Exhibit 4: Return ratios set to improve over FY18-20E**



Source: Company, ICICI Direct Research

## Outlook and valuation

With healthy tractor as well as capital equipment sales domestically, GST is on a healthy growth trajectory with bright prospects, going forward. It has a cash surplus balance sheet (>₹ 100 crore, ~20% of MCap). GST has been generous in sharing the same with shareholders with dividend payout in excess of 35% and share buyback in the past at ₹ 500/share. We believe the management will continue to do so, going forward, and offers attractive dividend yield of ~2.5%. Going forward, we expect sales and PAT to grow at a CAGR of 16.5% and 19.4%, respectively, in FY18-20E. We value the company at ₹ 450 i.e. 13x P/E on FY20E EPS of ₹ 34.6 and maintain our **BUY** rating on the stock. We also derive comfort from healthy return ratios (RoCE>25%, RoIC>50%) and CFO yield of ~8%.

**Exhibit 5: What's changed??**

Particulars	FY19E			FY20E		
	Old	New	% Change	Old	New	% Change
Sales	139.6	134.4	(3.7)	153.5	154.6	0.7
EBITDA	53.7	52.0	(3.2)	59.9	59.5	(0.6)
EBITDA Margin %	38.5	38.7	20 bps	39.0	38.5	-52 bps
PAT	44.1	41.7	(5.5)	49.3	47.8	(3.0)
EPS	31.9	30.2	(5.5)	35.7	34.6	(3.0)

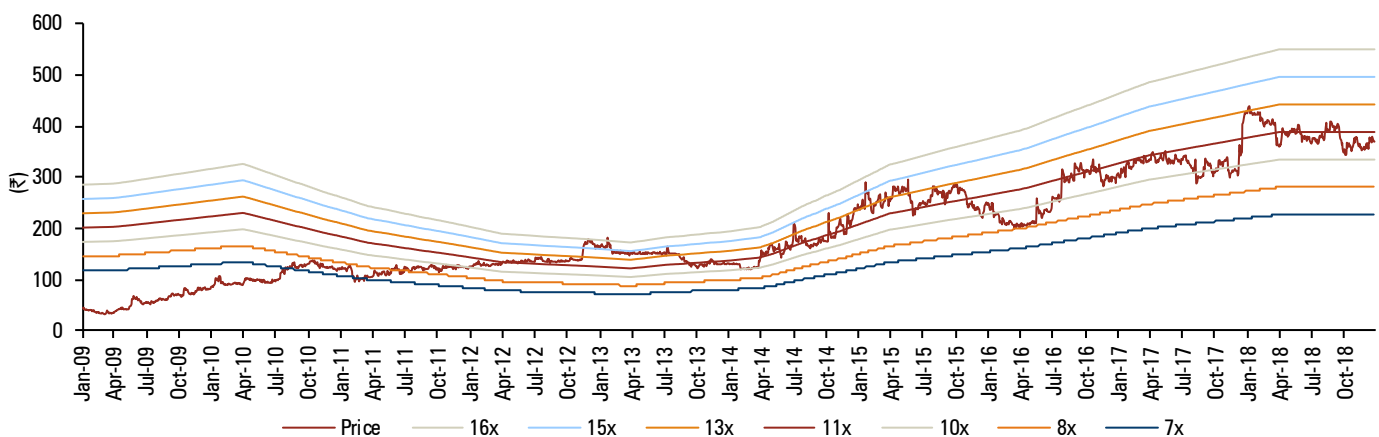
Source: Company, ICICI Direct Research

**Exhibit 6: Valuation Summary**

Year	Sales (₹ cr)	Growth (%)	PAT (₹)	Growth (%)	PE (x)	EV/EBITDA (x)	RoNW (%)	RoCE (%)	RoIC (%)
FY17	97.6	7.0	29.7	60.5	18.3	12.6	16.6	19.9	31.8
FY18	113.9	16.7	33.6	12.9	15.2	9.9	18.9	24.4	45.4
FY19E	134.4	18.0	41.7	24.2	12.3	7.6	20.9	27.1	51.6
FY20E	154.6	15.0	47.8	14.8	10.7	6.3	21.4	27.5	57.0

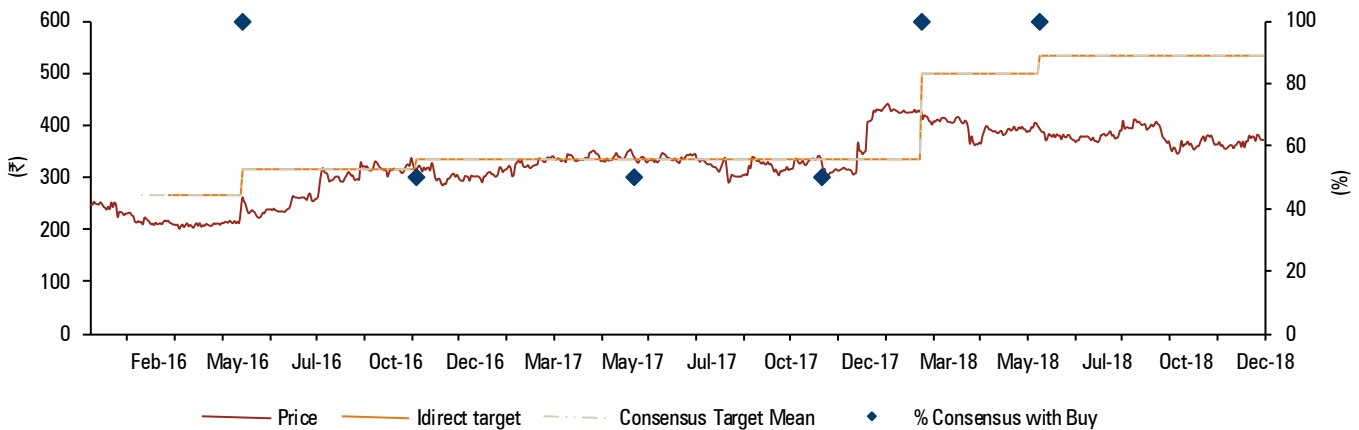
Source: Company, ICICI Direct Research

**Exhibit 7: Two year forward P/E (GST currently trading at 10.7 x)**



Source: Reuters, ICICI Direct Research

### Recommendation history vs. Consensus



Source: Bloomberg, Company, ICICI Direct Research

### Key events

Date/Year	Event
2007	Reports sales of ₹ 60.2 crore, limited due to capacity constraints. GST had undertaken a capex amounting to ₹ 12.8 crore in FY07, out of ₹ 12.6 crore was towards installation of plant and machinery. The entire capex was funded by the company's internal cash accruals
2008	Further undertakes capex amounting to ₹ 18.4 crore, out of which ₹ 3.3 crore was spent towards new factory building, ₹ 8.7 crore towards plant & machinery and ₹ 6.3 crore towards windmill. The entire capex was funded out of the company's internal cash accruals
2008	Closes down its Pune plant with effect from July 25, 2008. The said plant was engaged mainly in assembly of components transferred from the company's Halol plant and supplying the finished products to customers in nearby area. After completion of the expansion project at Halol, the company now had sufficient resources at its Halol Plant to undertake assembly and supply of products to all its customers from the said plant itself
2010	On occasion of silver jubilee year, board of directors of GST declares special interim dividend of ₹ 2.5 per equity shares of ₹ 5/- each. Regular interim dividend of ₹ 2.5 per equity share was also declared
2012	Stops production of refrigeration condenser coils; as business was highly seasonal. The company embarks upon the new capex plan amounting ₹ 40 crore. GST's planned capex includes capex of ₹ 10 crore for building, ₹ 20 crore for plant & machinery and ₹ 10 crore for new corporate office in Mumbai
2014	In August, Customs department (Government of India) imposes a safeguard duty on import of seamless steel tubes and pipes of external diameter not exceeding 273.1 mm (outer diameter) on imports from developed countries and China. GST would also be a key beneficiary of the said judgement
2015	Reports subdued Q4FY15 with full year FY15 PAT at ₹ 15.8 crore, down 8.7% YoY. The interaction with the management suggests near exhaustion of inventory pertaining to company's product profile in the user market with turnaround in sales expected in Q2FY16
2016	Reports robust Q4FY16 with sales growing 20% YoY and EBITDA margins coming in at 29%. Full year FY16, Sales, EBITDA & PAT were at ₹ 91 crore, ₹ 27 crore & ₹ 19 crore, respectively. The company has also declared and distributed a dividend of ₹ 7.5/share for FY16
2017	For full year FY17, GST clocks sales of ₹ 97.6 crore, up 7% YoY with EBITDA at ₹ 32.9 crore (EBITDA margins at 33.7%) and PAT at ₹ 29.7 crore. EPS in FY17 was at ₹ 20.2 with dividend per share at ₹ 9. Improvement in EBITDA margins was encouraging though management commentary on future sales growth was cautious given transition of M&HCV segment to new emission norms (BS-4) and GST implementation domestically
2018	For FY18, net sales stood ₹ 113.9 crore, up 20.8% YoY while EBITDA stood at ₹ 41.1 crore, up 24.9% YoY and PAT came in at ₹ 33.6 crore. For FY18, the company has announced a dividend of ₹ 9/share and also executed a buy-back amounting to ~₹ 44 crore @ 500/share

Source: Company, ICICI Direct Research

### Top 10 Shareholders

Rank	Name	Latest Filing Date	% O/S	Position (m)	Change (m)
1	Gandhi (Manhar G)	30-Sep-18	14.4	2.0	0.0
2	Gandhi (Bhupatrai G)	30-Sep-18	13.2	1.8	0.0
3	Gandhi (Jayesh M)	30-Sep-18	8.0	1.1	0.0
4	Gandhi (Manoj B)	30-Sep-18	7.5	1.0	0.0
5	Gandhi (Bharati M)	30-Sep-18	5.3	0.7	0.0
6	B M Gandhi Investment Company Pvt. Ltd.	30-Sep-18	3.7	0.5	0.0
7	Gandhi Finance Company Pvt. Ltd.	30-Sep-18	3.4	0.5	0.0
8	Gandhi (Chandra B)	30-Sep-18	3.2	0.4	0.0
9	Gandhi (Gopi J)	30-Sep-18	3.1	0.4	0.0
10	Gandhi (Jigna M)	30-Sep-18	3.1	0.4	0.0

Source: Reuters, ICICI Direct Research

### Shareholding Pattern

(in %)	Sep-17	Dec-17	Apr-18	Jun-18	Sep-18
Promoter	73.3	73.3	73.3	73.3	73.3
FII	4.2	1.9	1.9	1.9	1.9
DII	0.0	0.0	0.0	0.0	0.0
Others	22.5	24.8	24.8	24.9	24.9

### Recent Activity

Buys			Sells		
Investor name	Value (US\$ M)	Shares (M)	Investor name	Value(US\$M)	Shares(M)
Warden (Kavas N.)	0.16	0.03	PineBridge Investments Asia Limited	-0.08	-0.01

Source: Reuters, ICICI Direct Research

## Financial summary

Profit and loss statement		₹ Crore			
(Year-end March)	FY17	FY18	FY19E	FY20E	
Net Sales	94.3	113.9	134.4	154.6	
Other Operating Income	3.3	0.0	0.0	0.0	
<b>Total Operating Income</b>	<b>97.6</b>	<b>113.9</b>	<b>134.4</b>	<b>154.6</b>	
Growth (%)	7.0	16.7	18.0	15.0	
Raw Material Expenses	30.9	37.2	44.8	51.0	
Employee Expenses	7.3	8.4	9.5	11.6	
Power & Fuel Expense	11.0	11.2	12.8	14.7	
Other Operating Expense	15.5	16.2	15.4	17.8	
<b>Total Operating Expenditure</b>	<b>64.7</b>	<b>72.8</b>	<b>82.4</b>	<b>95.1</b>	
<b>EBITDA</b>	<b>32.9</b>	<b>41.1</b>	<b>52.0</b>	<b>59.5</b>	
Growth (%)	22.2	24.9	26.5	14.5	
Depreciation	4.4	3.9	4.0	4.4	
Interest	0.0	0.0	0.0	0.0	
Other Income	8.7	8.3	8.2	8.8	
PBT	37.1	45.5	56.2	63.9	
Exceptional Item	0.0	0.0	0.0	0.0	
Total Tax	7.4	11.9	14.5	16.1	
<b>PAT</b>	<b>29.7</b>	<b>33.6</b>	<b>41.7</b>	<b>47.8</b>	
Growth (%)	60.5	12.9	24.2	14.8	
EPS (₹)	20.2	24.3	30.2	34.6	

Source: Company, ICICI Direct Research

Balance sheet		₹ Crore			
(Year-end March)	FY17	FY18	FY19E	FY20E	
<b>Liabilities</b>					
Equity Capital	7.4	6.9	6.9	6.9	
Reserve and Surplus	171.8	170.3	192.1	216.7	
<b>Total Shareholders funds</b>	<b>179.2</b>	<b>177.2</b>	<b>199.0</b>	<b>223.6</b>	
Total Debt	0.0	0.0	0.0	0.0	
Deferred Tax Liability	7.4	8.8	8.8	8.8	
Minority Interest / Others	0.0	0.0	0.0	0.0	
<b>Total Liabilities</b>	<b>186.6</b>	<b>186.0</b>	<b>207.8</b>	<b>232.4</b>	
<b>Assets</b>					
Gross Block	130.0	130.1	135.1	137.1	
Less: Acc Depreciation	74.8	78.7	82.7	87.0	
Net Block	55.2	51.4	52.4	50.1	
Capital WIP	0.0	0.0	0.0	0.0	
<b>Total Fixed Assets</b>	<b>55.2</b>	<b>51.4</b>	<b>52.4</b>	<b>50.1</b>	
Investments	93.8	98.9	108.9	128.9	
Inventory	24.3	20.0	25.8	29.6	
Debtors	16.3	19.5	23.9	27.5	
Loans and Advances	1.6	2.5	2.7	3.1	
Other Current Assets	0.6	0.0	0.7	0.8	
Cash	3.3	5.2	5.9	6.8	
<b>Total Current Assets</b>	<b>46.1</b>	<b>47.1</b>	<b>59.0</b>	<b>67.8</b>	
Current Liabilities	4.9	7.7	7.4	8.5	
Provisions	3.6	3.7	5.2	5.9	
Current Liabilities & Prov	8.5	11.4	12.5	14.4	
<b>Net Current Assets</b>	<b>37.6</b>	<b>35.7</b>	<b>46.5</b>	<b>53.4</b>	
Others Assets	0.0	0.0	0.0	0.0	
<b>Application of Funds</b>	<b>186.6</b>	<b>186.0</b>	<b>207.8</b>	<b>232.4</b>	

Source: Company, ICICI Direct Research

Cash flow statement		₹ Crore			
(Year-end March)	FY17	FY18	FY19E	FY20E	
Profit after Tax	29.7	33.6	41.7	47.8	
Add: Depreciation	4.4	3.9	4.0	4.4	
(Inc)/dec in Current Assets	-6.3	0.9	-11.1	-8.0	
Inc/(dec) in CL and Provisions	1.1	2.9	1.1	1.9	
Others	0.0	0.0	0.0	0.0	
<b>CF from operating activities</b>	<b>28.9</b>	<b>41.2</b>	<b>35.7</b>	<b>46.1</b>	
(Inc)/dec in Investments	-12.2	-5.1	-10.0	-20.0	
(Inc)/dec in Fixed Assets	-0.6	-0.1	-5.0	-2.0	
Others	0.0	1.3	0.0	0.0	
<b>CF from investing activities</b>	<b>-12.8</b>	<b>-3.8</b>	<b>-15.0</b>	<b>-22.0</b>	
Issue/(Buy back) of Equity	0.0	-0.4	0.0	0.0	
Inc/(dec) in loan funds	0.0	0.0	0.0	0.0	
Dividend paid & dividend tax	-15.9	-14.9	-19.9	-23.2	
Inc/(dec) in Share Cap	0.0	-33.9	0.0	0.0	
Others	0.0	13.8	0.0	0.0	
<b>CF from financing activities</b>	<b>-15.9</b>	<b>-35.5</b>	<b>-19.9</b>	<b>-23.2</b>	
<b>Net Cash flow</b>	<b>0.3</b>	<b>1.9</b>	<b>0.8</b>	<b>0.9</b>	
Opening Cash	3.0	3.3	5.2	5.9	
<b>Closing Cash</b>	<b>3.3</b>	<b>5.2</b>	<b>5.9</b>	<b>6.8</b>	

Source: Company, ICICI Direct Research

Key ratios					
(Year-end March)	FY17	FY18	FY19E	FY20E	
<b>Per share data (₹)</b>					
EPS	20.2	24.3	30.2	34.6	
Cash EPS	23.2	27.1	33.0	37.8	
BV	121.9	128.2	144.0	161.8	
DPS	9.0	9.0	12.0	14.0	
Cash Per Share (Incl Invst)	66.0	75.3	83.1	98.2	
<b>Operating Ratios (%)</b>					
EBITDA Margin	33.7	36.1	38.7	38.5	
PAT Margin	30.4	29.5	31.0	30.9	
Inventory days	94.2	64.1	70.0	70.0	
Debtor days	63.0	62.3	65.0	65.0	
Creditor days	19.0	24.8	20.0	20.0	
<b>Return Ratios (%)</b>					
RoE	16.6	18.9	20.9	21.4	
RoCE	19.9	24.4	27.1	27.5	
RoIC	31.8	45.4	51.6	57.0	
<b>Valuation Ratios (x)</b>					
P/E	18.3	15.2	12.3	10.7	
EV / EBITDA	12.6	9.9	7.6	6.3	
EV / Net Sales	4.4	3.6	2.9	2.4	
Market Cap / Sales	5.4	4.5	3.8	3.3	
Price to Book Value	3.0	2.9	2.6	2.3	
<b>Solvency Ratios</b>					
Debt/EBITDA	0.0	0.0	0.0	0.0	
Debt / Equity	0.0	0.0	0.0	0.0	
Current Ratio	5.1	3.7	4.2	4.2	
Quick Ratio	2.2	1.9	2.2	2.2	

Source: Company, ICICI Direct Research

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Strong Buy: > 15%/20% for large caps/midcaps, respectively, with high conviction;

Buy: > 10%/15% for large caps/midcaps, respectively;

Hold: Up to +/-10%;

Sell: -10% or more;



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## ANALYST CERTIFICATION

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