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Q3FY20 conference call takeaways

Metals

Target price: Rs326

Earnings revision

(%)	FY20E	FY21E	FY22E
Revenue	-	↑ 5.3	↑ 15.9
EBITDA	↑ 17.1	↑ 21.8	↑ 26.1
EPS	↑ 23.3	↑ 29.4	↑ 35.0

Target price revision

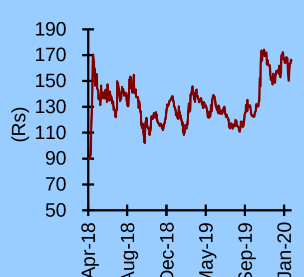
Rs326 from Rs242

Shareholding pattern

	Jun '19	Sep '19	Dec '19
Promoters	74.0	74.0	74.0
Institutional investors	20.1	20.1	19.2
MFs and others	10.0	11.5	13.3
Insurance Cos.	9.5	8.0	5.3
FIIs	0.6	0.6	0.6
Others	5.9	5.9	6.8

Source: www.nseindia.com

Price chart



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INDIA

Mishra Dhatu Nigam

BUY
Maintain

Blazing a trail

Rs180

Post Mishra Dhatu Nigam (MIDHANI)'s Q3FY20 conference call, it became clear that our FY22E PAT estimates will be achieved by FY20E. We, therefore, upgrade our PAT estimates for FY20/21/22E by 23/29/35%, respectively. This leads to an increase in the target price to Rs326 (from Rs242 earlier). Management highlighted some of the tailwinds in orders/margins/working capital that is led by the increased work share from ISRO. What was perhaps little discussed was that ISRO's capital budget has seen ~35% YoY increase (budgeted to budgeted) in FY21E annual budget and supports management claim of continued strength in order inflows for MIDHANI. Maraging steel (supplied to ISRO) forms >50% in 9MFY20 and is key in achieving ~100% YoY EBITDA jump and 950bps YoY margin expansion for 9MFY20. With 15-16 launches p.a. (as guided by ISRO and as confirmed by management), MIDHANI can be on course to convincingly beat our FY21-22E conservative estimates. We maintain BUY with a revised target price of Rs326/share (Rs242/share earlier).

- **Stable order inflows coupled with stabilizing orderbook.** ~Rs8-9bn of order inflow is expected every year of which, Rs3-4bn is expected from space, Rs2.5-3bn from defence and Rs1.5bn from others. In addition, company expects current orderbook of ~Rs17bn to normalise to ~9bn in the next 2-3 years. The execution pace of the order would therefore be faster than earlier envisaged.
- **What is driving topline?** Increasing order inflow from ISRO over the years has led to a higher topline. Also, MIDHANI has managed to better its yield i.e. more output from lesser input. Of the total volumes, ~50% is maraging steel and 10-20% is titanium alloys.
- **What is driving higher margin?** Some of the reasons which led to gross/EBITDA margin improving 734/948bps in 9MFY20 were: 1) MIDHANI's higher value of production (~Rs8bn in 9MFY20) leading to operating leverage benefits; 2) lower rejections; 3) lower power costs, and 4) bulk buying of raw materials. In addition, tax rate cuts led to tax lowering by Rs23bn (including deferred tax adjustment of Rs13bn).
- **Higher space launch expectation.** In-line with robust growth in space budget for the past 6-7 years, including FY21 budget being rolled out recently, the company expects ISRO to reach an annual launch of 15 from 6-7 witnessed in the last two years. The supply of material to ISRO typically starts 1.5-2 years prior to the launch. With MIDHANI's monopoly in supply of maraging steel to ISRO, the commentary of the management further adds to our confidence in the name. In-line with management's commentary for FY20, and the potential demand for various strategic materials going forward, we revise our estimates upwards for FY20/21/22.
- **Maintain BUY.** We expect RoCE to cross 20% as topline accretion takes shape. Capex will be normalised to Rs1bn each year from Rs2bn from FY21, as plate mill will get commissioned in Mar'21. Debtor days have come down to 130 from 180 YoY, which will be maintained, even after a slightly higher share of defence and energy in FY21. We maintain Buy with a revised target price of Rs326/share (Rs242/share earlier).

Market Cap	Rs33.7bn/US$473mn
Reuter/Bloomberg	MISR.BO/MIDHANI IN
Shares Outstanding (mn)	187.3
52-week Range (Rs)	180/108
Free Float (%)	26.0
FII (%)	0.6
Daily Volume (US$'000)	1,097
Absolute Return 3m (%)	5.7
Absolute Return 12m (%)	53.1
Sensex Return 3m (%)	2.4
Sensex Return 12m (%)	16.3

Year to March	FY19	FY20E	FY21E	FY22E
Revenue (Rs mn)	7,108	8,175	9,810	12,262
Net Income (Rs mn)	1,306	2,005	2,368	2,777
EPS (Rs)	7.0	10.7	12.6	14.8
% Chg YoY	(0.5)	53.6	18.1	17.3
P/E (x)	26.0	16.9	14.3	12.2
CEPS (Rs)	8.2	12.1	14.3	16.9
EV/E (x)	18.0	12.8	10.5	8.7
Dividend Yield (%)	2.2	3.2	3.8	4.4
RoCE (%)	17.1	22.3	23.0	23.6
RoE (%)	15.6	20.6	20.8	20.8

Other points

- **Orderbook breakup.** Of total ~Rs17bn orderbook, Rs8bn is a 1 year cycle order and Rs8-9bn is of 2-year cycle. Around Rs8-9bn of order inflow is expected every year of which, Rs3-4bn is expected from space, Rs2.5-3bn from defence and Rs1.5bn from others.
- **No impact on raw materials due to Corona.** Company imports cobalt and molybdenum from China, for which it already has inventory till July'20, so virus led trade slowdown will not impact their supply chain.
- **Scaling up strategy**. Company's further scaling up will be aided by modernised facility and entering export markets. Also, the company may supply to sectors like Railways, oil and gas. JV with NALCO would help in making aluminium alloys.
- **Funding for JV with NALCO.** Company may get a third party if it agrees to come for a small stake. It is also exploring an option to fund through CCD/normal debt from banks, in which case third party funding won't be required. The capacity of the plant would be 60000te in the next 4-5 years with per te realisation of ~Rs400,000/te. Around 30,000-35,000te is currently imported in this category, and by the time the plant commissions, the demand could go to 130,000te. The end product will to be used for Railways, defence aerospace and auto sectors.
- **Risks.** Management mentioned the risks they foresee to their business. First is on the competition side, where new players may enter, with the business being a low capex one, with decent margins. They are more insulated in space sector, as more than the capex, it's about the process of making the strategic material, which makes MIDHANI unique. Second is the risk of rapidly changing technology, which can be mitigated by continued innovation. The company is spending ~Rs200mn on R&D expense each year. Final risk is to comfortably source a raw material at competitive price.

Table 1: Q3FY20 result review

	Q3FY20	Q3FY19	% Chg YoY	Q2FY20	% Chg QoQ	9MFY19	9MFY20	% Chg YoY
Revenue	2,069	1,532	35.0	1,702	21.5	3,744	5,092	36.0
Other Operating Income	9	18	(50.6)	10	(13.0)	52	35	(31.8)
Operating revenue	2,060	1,515	36.0	1,692	21.8	3,692	5,057	37.0
Raw Material	441	532	(17.1)	181	143.1	817	738	(9.7)
Gross Margin	1,628	1,000	62.7	1,521	7.1	2,927	4,354	48.8
Gross Margin (%)	79	65		89	(11.9)	239	259	
Employee expenses	298	310	(3.9)	309	(3.7)	770	899	16.8
Other expenses	758	519	45.9	682	11.0	1,426	1,979	38.7
EBITDA	573	171	234.4	529	8.3	730	1,476	102.1
EBITDA Margin (%)	28	11		31	(10.9)	61	87	
Dep	71	60	18.7	63	12.8	172	195	13.1
Other income	94	135	(30.7)	65	44.8	245	222	(9.3)
EBIT	595	247	141.4	531	12.2	803	1,503	87.1
Interest	11	18	(38.2)	11	(0.8)	41	39	(4.6)
PBT	585	229	155.3	520	12.4	762	1,464	92.1
Tax	(21)	60	(134.3)	161	(112.7)	259	270	4.3
PAT	605	169	258.0	358	68.8	503	1,194	137.5

Source: Company data, I-Sec research

Change in earnings

We changed our earnings estimates in-line with 9MFY20 reported numbers and the recent management commentary. We, therefore, upgrade our PAT estimates for FY20/21/22E by 23/29/35%, respectively. This leads to an increase in target price to Rs326/share (from Rs242/share earlier).

Table 2: Earnings change

(Rs mn)

	New			Old			% Chg		
	FY20E	**FY21E**	**FY22E**	**FY20E**	**FY21E**	**FY22E**	**FY20E**	**FY21E**	**FY21E**
Revenue	8,175	9,810	12,262	8,175	9,319	10,577	-	5.3	15.9
EBITDA	2,681	3,178	3,801	2,289	2,609	3,015	17.1	21.8	26.1
PAT	2,005	2,368	2,777	1,626	1,830	2,057	23.3	29.4	35.0

Source: I-Sec research

Valuation methodology and key risks

We maintain our valuation multiple at 22x FY22E EPS and maintain **BUY** with a revised target price of Rs326/share (Rs242/share earlier). Sudden drop in space contract inflow/execution is the key risk to our call.

Financial summary

Table 3: Profit & loss statement

(Rs mn, year ending March 31)

	FY19	FY20E	FY21E	FY22E
Operating Income (Sales)	7,108	8,175	9,810	12,262
Operating Expenses	5,271	5,493	6,631	8,461
EBITDA	**1,837**	**2,681**	**3,178**	**3,801**
% margins	25.8	32.8	32.4	31.0
Depreciation & Amortization	232	267	310	398
Gross Interest	64	57	57	57
Other Income	369	316	346	356
Recurring PBT	**1,910**	**2,673**	**3,158**	**3,702**
Add: Extra ordinaries				
Less: Taxes	605	668	789	926
Less: Minority Interest				
Add: Share of profit from associates				
Net Income	**1,306**	**2,005**	**2,368**	**2,777**
Recurring Net Income	**1,306**	**2,005**	**2,368**	**2,777**

Source: Company data, I-Sec research

Table 4: Balance sheet

(Rs mn, year ending March 31)

	FY19	FY20E	FY21E	FY22E
Assets				
Total Current Assets	11,639	11,000	13,362	16,073
of which cash & cash eqv.	1,980	772	1,501	1,724
Total Current Liabilities & Provisions	4,274	4,124	4,918	6,288
Net Current Assets	7,365	6,876	8,444	9,785
Investments	21	21	21	21
Net Fixed Assets	4,249	5,671	6,423	8,225
Capital Work-in-Progress	1,751	3,061	4,000	3,800
Other non current assets	587	587	587	587
Total Assets	**13,973**	**16,217**	**19,475**	**22,419**
Liabilities				
Borrowings	1,067	1,067	1,067	1,067
Deferred Tax Liability				
Other long term liabilities	4,559	5,400	7,000	8,000
Minority Interest	-	-	-	-
Equity Share Capital	1,873	1,873	1,873	1,873
Face Value per share (Rs)	*10*	*10*	*10*	*10*
Reserves & Surplus	6,474	7,877	9,535	11,478
Net Worth	8,347	9,750	11,408	13,352
Total Liabilities	**13,973**	**16,217**	**19,475**	**22,419**

Source: Company data, I-Sec research

Table 5: Cashflow statement

(Rs mn, year ending March 31)

	FY19	FY20E	FY21E	FY22E
Operating Cash flow	1,232	2,013	2,389	2,876
Working Capital Changes	1,398	(720)	(838)	(1,119)
Capital Commitments	(2,138)	(3,000)	(2,000)	(2,000)
Free Cash flow	493	(1,707)	(449)	(243)
Investing Cash flow	84	316	346	356
Issue of Share Capital	-	-	-	-
Buyback of shares	-	-	-	-
Inc (Dec) in Borrowings	138	841	1,600	1,000
Dividend paid	(854)	(601)	(710)	(833)
Others	(64)	(57)	(57)	(57)
Extraordinary Items	-	-	-	-
Chg. in Cash	(203)	(1,208)	729	223

Source: Company data, I-Sec research

Table 6: Key ratios

(Year ending March 31)

	FY19	FY20E	FY21E	FY22E
Per Share Data (in Rs.)				
EPS(Basic Recurring)	7.0	10.7	12.6	14.8
Diluted Recurring EPS	7.0	10.7	12.6	14.8
Recurring Cash EPS	8.2	12.1	14.3	16.9
Book Value per share (BV)	44.6	52.0	60.9	71.3
Growth Ratios (%)				
Operating Income	7.4	15.0	20.0	25.0
EBITDA	(3.8)	46.0	18.5	19.6
Recurring Net Income	(0.5)	53.6	18.1	17.3
Valuation Ratios (x)				
P/E	26.0	16.9	14.3	12.2
P/CEPS	22.1	14.9	12.7	10.7
P/BV	4.1	3.5	3.0	2.5
EV / EBITDA	18.0	12.8	10.5	8.7
EV / FCF	40.1	(20.0)	(74.5)	(136.7)
Operating Ratios (%)				
Raw Material/Sales	-	-	-	-
Other Income / PBT	19.3	11.8	11.0	9.6
Effective Tax Rate	31.7	25.0	25.0	25.0
NWC / Total Assets	34.5	28.6	30.3	30.4
Inventory Turnover	1.4	1.4	1.4	1.3
Asset Turnover	0.4	0.4	0.4	0.4
Net D/E Ratio (x)	(0.1)	0.0	(0.0)	(0.0)
Profitability Ratios (%)				
Rec. Net Income Margins	18.4	24.5	24.1	22.6
RoCE	17.1	22.3	23.0	23.6
RoNW	15.6	20.6	20.8	20.8
EBITDA Margins	25.8	32.8	32.4	31.0

Source: Company data, I-Sec research

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