Business Standard

Welspun Gujarat: Cheer in the Pipeline

Sunaina Vasudev / Mumbai November 3, 2009, 10:34 IST

Welspun Gujarat has the world's second largest pipe manufacturing capacity and is leading the case for a bounce-back in the global economy. It showed better pipe sales volumes this quarter (with 80% overseas revenues) which came off a strong order book.

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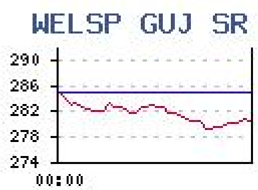

The company, which has a strong oil and gas clientele, is set to benefit from the ramp-up in gas pipelines and is an indirect play on higher oil prices– generally a negative for Indian equities. Investment in crude and produt pipelines is expected to increase by 17% y-o-y and investments in natural gas pipelines are expected to increase by 64% in 2009, according to the Oil & Gas Journal.

The company saw a sales volume growth of 2% for pipes which translated to a revenue growth of 21% y-o-y to nearly Rs 1,872 crore, which also included numbers for its US. Sequentially, however, revenues were down marginally (-3.5 % q-o-q).

Lower input costs boosted margins which blended EBITDA of Rs10, 994 / tonne, 8% higher than the previous quarter. The uptick in volumes has played up the economies of scale boosting blended EBITDA on pipes which was relatively higher than expected at Rs 11, 000 / tonne. Margin on plates was maintained at Rs 6, 000 / tonne in a challenging environment.

Operating profit was up 84 % y-o-y to Rs 297 crore with EBITDA margins at 16.4 % up 559 bps y-o-y and flat sequentially over the previous quarter. Consolidation of the US pipe plant, with an EBITDA contribution of Rs 663 million, also boosted the bottom-line. Net profit grew 115 % over Q2FY09 to Rs 140 crore and dipped marginally (3%) over the previous quarter.

Order book

The key for the company is its strong order book at Rs 7,800 crore, up from Rs 6,800 crore at the end of the last quarter. The company got additional orders worth Rs. 3,200 crore from domestic and international oil and gas companies in the quarter.

The order book was spurred by orders in the US where a major pipeline replacement is due as a large proportion of pipes were installed pre-1975 and have a standard life of 30 years. More than 40 pipeline projects have been approved in the US in the last few months, according to a Macquarie research report. The report pegs global pipe demand to be around $78 billion over the next five years. This is based on estimates by global consultancy, Simdex, that 710 pipeline projects of ~326,000km are to be constructed in this period, assuming that 200 tonnes of pipes are laid per kilometre with an average price of US$1,200/tonne.

The Pipeline and Gas Journal, quoted by Macquarie, states that approximately 43,000km of new pipelines will be under construction in the US in 2009, and natural gas will account for 27,000km. There are a total of 75 projects, 58 of which will involve pipes that are 30” or bigger. The company is expected to ramp up its US capacity in 2-3 years taking utilisation to 35-40 % by the end of this year. It has accredition and approvals from over 50 oil and gas companies globally.

Margins are expected to revert back to around Rs 10,000 / tonne after factoring in forex gains in the quarter as inputs costs could rise, estimates HSBC in a report. Depreciation will be higher going ahead with the consolidation of the US plant as will interest costs if one follows the trend in the first half of this year.

The company has gross debt of Rs 2,600 crore, with cash at about Rs 230 crore, and debt in US at Rs 4,000 crore. The company raised $150 million through 4.5 % FCCB (Foreign currency convertible bonds) on October 16, 2009, redeemable after five years at a conversion price of Rs 300/share.

The company share price was Rs 256.20 at close on October 30, 2009, It trades at a forward P/E of 10.6x and 9.7x of FY10 and FY11 consensus analyst EPS estimates.