EQUITIES | INDIA | COMPRESSORS

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DOHA BROKERAGE

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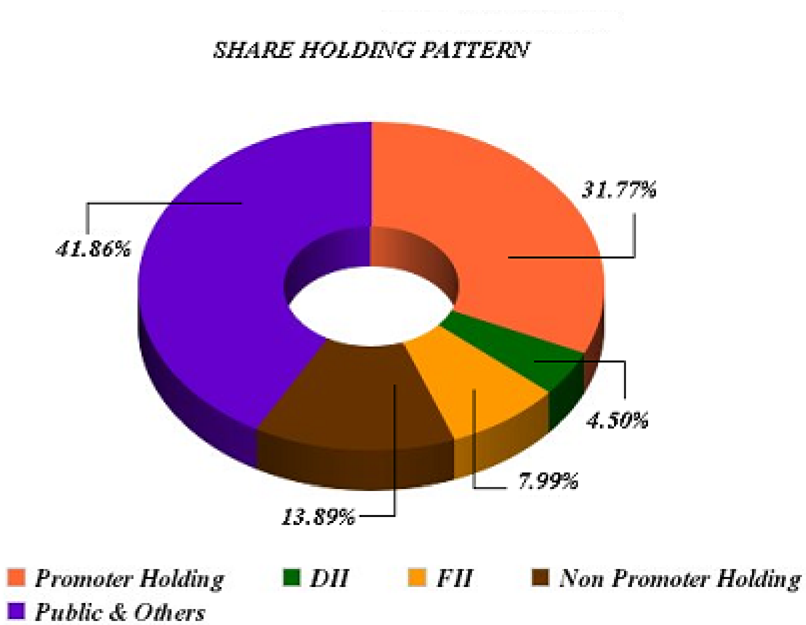
associate of DOHA BANK

Elgi Equipments Ltd

BUY



Stock Data

CMP	69.85
Target Price	84.00
NSE Code	ELGIEQUIP
BSE Code	522074
Bloomberg Code	ELEQ:IN
Reuters Code	ELGE.NS
52 Week High	102.25
52 Week Low	62.65
Market Cap (cr)	1106.80
Face Value	1.00
DPS	1.01
M Cap/Sales	1.178 times
Stock Beta	0.831
PE Multiple	12.44
P/BV	3.24
EV/EBITDA	6.37
Downside risk	Moderate

Investment Rationale:

The compressor market is a very essential product involved in the manufacturing of diverse products in various sectors. Compressors are used in almost in all sectors from mining, transport, pharmaceuticals, power, oil, railways, chemicals, textiles, printing paper, telecommunications, plastics, beverages, medical, food etc. One of the main factors that draws our attention to this business is the fact that the product's usability in diverse sectors without any major change in its operations gives ample chance for sustained earnings predictability without being impacted much by the vicissitudes of a changing economic scenario.

Company Description:

ELGI Equipment is today, the market leader and Asia's largest manufacturer of air compressors and automobile service station equipment. ELGI's products are used in a wide range of applications in areas ranging from mining, transport, pharmaceuticals, power, oil, railways, chemicals, textiles, printing to ship building, paper, electronics, telecommunications, medical, food & beverages and plastics. The company continues to maintain its strong presence in the compressor segment.

a s s o c i a t e o f D O H A B A N K

What makes the company a good investment pick?

- A strong balanced portfolio: The company has a balanced portfolio of various ranges of compressors. The compressors can be used for various number of industries and is an essential part of many manufacturing machineries in diverse sectors.

- Sustained long term performance: The Company has maintained its supremacy by innovating from time to time. The company has one of the most advanced products in the industry.

- Strong Economic growth: The Indian economy has been witnessing a fast growth trajectory for the past few years and going forward we feel that the company should be able to sell its products easily as these are critical and basic products for the development of the economy.

- Low Debt: The Company has low debt in its Balance Sheet indicating the strong cash flow and profitability of the company. The low debt in the balance Sheet should be acting as a good hedge in a high interest rate scenario.

Product Portfolio:

1. *Railway Compressors:* The Company manufactures a variety of compressors for the railway applications. The applications include circuit breakers, engine starting, and breaking etc. The company manufactures various models of compressors for the Electrical locomotives, Diesel locomotives, etc.

2. *New Generation Compressors:* These are compressors that are developed and are generally small, light, strong and portable. They are for special customized application. Vayu is the newest addition to the product range.

3. *Rotary Screw Air Compressors:* These are involved with design, development and manufacturing of electric and diesel powered screw air compressors. These are generally used in industrial applications. They have a lot of advantages over the normal piston compressors. Some of them including low vibration and ability to compress more air than the normal compressors.

4. *Reciprocating Compressors:* These are compressors that are being used by sending gas through the compression cylinder where it gets compressed by a piston driven in a reciprocating motion via a crankshaft, and is then discharged. Applications include oil refineries, gas pipelines, chemical plants, natural gas processing plants and refrigeration plants. One specialty application is the blowing of plastic bottles made of Polyethylene Terephthalate.

Compressor Prospects:

Compressors are products which play a pivotal role in the functioning of manufacturing and heavy machinery. The energy can be used for various activities. Thus it can be assumed that going forward; compressors are not going to be out of fashion. No matter how much technology improves in the future, compressors only evolve accordingly and do not loose out their usability due to change in technology. The company operates especially in the railways, which is expected to witness a huge demand growth in the coming years. Going forward , it is certain that the demand for compressors is likely to keep on increasing in the coming future and ELGI Equipments should be getting its fair share of the market.

Low Debt:

The company does not have a history of relying much on debt. The company continues to rely on its own retained earnings to fund its future expansion activities. We are not anticipating any earnings dilution in the near future via a FPO. We expect the company to weather through the difficult times and should be able to demonstrate spectacular results once the tide turns around.

Competition - A concern for the future ?

There is no doubt that competition is increasing in the compressor. On analyzing the peers, we found that most of the peer group companies were diversified in their operations of which compressor manufacturing was just a part of their revenue inflow. Their stocks are not likely to move in accordance with compressor sales and are currently trading in the higher valuation band. This also makes most of these companies difficult to adjust with the changing business scenario.

Overall Analysis and Recommendation:

On analyzing the company, we found that the company's valuation has historically traded in a range below most of its peers. Most of the peers are well diversified in their operations giving them an upper hand in the subsequent difficult quarters. Elgi Equipments has been able to perform fairly well in previous recessions, thanks to the railway demand that continues to be robust. The company is trading at a moreover fair valuation when comparing with peers. The company's portfolio of products is limited. But the products are generic in nature and are regularly used. A good rise in sales indicates that the company is improving its market share as well as increasing the sales in value and numbers. On a traditional valuation perspective, the company seems to be on the fair value zone whereas when looking on the DCF valuation methodology the stock sees potential upside. We have attached weights to be slightly conservative in our approach thus arriving to a marginal upside of 20% which we believe should be achieved in a one year perspective should the situation does not deteriorate further from hereon. Hence we feel that it would be appropriate to recommend a BUY at these levels.

FINANCIAL STATEMENTS

CASH FLOW STATEMENT	**FY10A**	**FY11A**	**FY12E**	**FY13E**	**FY14E**
CASH FLOW FROM OPERATING ACTIVITIES					
Net Profit after Tax	579.23	889.91	871.77	1089.08	1171.12
Depreciation	104.53	111.62	124.89	138.62	153.87
Goodwill Amortized	3.11	3.09	3.06	3.03	3.00
Others	382.66	(518.27)	(315.19)	0.07	(123.89)
Net cash flow from operating activities	**1069.53**	**486.35**	**684.53**	**1230.80**	**1204.10**
CASH FLOW FROM INVESTING ACTIVITIES					
Purchase of fixed assets, net of reimbursements	(178.85)	(259.51)	(225.02)	(249.77)	(277.24)
Increase in Investments	0.00	(30.01)	(43.25)	(54.06)	(67.57)
Decrease in Loans Advanced	(99.35)	17.00	(235.80)	(722.77)	(617.51)
Others	46.85	90.86	98.25	103.25	98.25
Net Cash used for investing activities	**(231.35)**	**(181.66)**	**(405.82)**	**(923.35)**	**(864.07)**
CASH FLOW FROM FINANCING ACTIVITIES					
Proceeds from Issue of Equity Shares	16.19	0.58	0.00	0.00	0.00
Borrowings from banks net	27.57	22.28	7.48	8.60	9.89
Dividend Paid	(150.44)	(116.27)	(209.85)	(235.03)	(263.23)
Others	214.67	(4.36)	(8.29)	(7.69)	(9.68)
Net Cash generated from financing activities	**107.99**	**(97.77)**	**(210.66)**	**(234.12)**	**(263.02)**
NET CHANGE IN CASH & CASH EQUIVALENTS	**946.17**	**206.92**	**68.05**	**73.34**	**77.01**
Opening Balance of Cash Cash Equivalents	245.67	1191.84	1398.76	1466.81	1540.15
Closing Balance of Cash Cash Equivalents	1191.84	1398.76	1466.81	1540.15	1617.16

FINANCIAL STATEMENTS

PROFIT & LOSS ACCOUNT	FY10A	FY11A	FY12E	FY13E	FY14E
Income					in Millions
Net Sales	6769.57	9390.14	9859.65	11042.80	12699.23
Other Income	37.58	45.63	78.88	88.34	101.59
Interest Income	43.92	88.34	49.30	55.21	63.50
Total Income	6851.07	9524.11	9987.82	11186.36	12864.32
Expenditure					
Cost of Materials	4086.30	5610.95	6014.38	6625.68	7619.54
Salaries & Wages	642.18	914.63	936.67	1104.28	1333.42
Other Expenses	993.43	1473.47	1577.54	1656.42	1968.38
Total Expenses	5721.91	7999.05	8528.59	9386.38	10921.33
Operating Profit	**1091.58**	**1479.43**	**1380.35**	**1711.63**	**1841.39**
EBITDA	1129.16	1525.06	1459.23	1799.98	1942.98
Interest	0.00	0.00	4.59	5.27	6.07
PBDT	**1129.16**	**1525.06**	**1454.64**	**1794.70**	**1936.92**
Exceptional Items	3.11	3.09	3.06	3.03	3.00
Depreciation	104.53	111.62	124.89	138.62	153.87
Profit Before Tax	**1021.52**	**1410.35**	**1326.70**	**1653.05**	**1780.05**
VRS- Compensation	81.08	1.54	2.06	1.15	1.60
Employees Stock Purchase Scheme	0.00	47.36	0.00	0.00	0.00
Provision for Tax	339.87	458.45	437.81	545.51	587.42
Deffered Tax Liability	21.34	13.09	15.05	17.31	19.91
Reported Net Profit	**579.23**	**889.91**	**871.77**	**1089.08**	**1171.12**
Dividend Paid	144.75	160.14	179.36	200.88	224.99
Corporate Dividend Tax Paid	24.60	25.99	30.49	34.15	38.25
Per share					
Earning Per Share	*7.34*	*5.62*	*5.50*	*6.87*	*7.39*
Cash EPS	*8.70*	*6.34*	*6.31*	*7.77*	*8.38*
Earnings Yield	*5.25%*	*8.04%*	*7.88%*	*9.84%*	*10.58%*
DPS	*1.83*	*1.01*	*1.13*	*1.27*	*1.42*
Dividend Yield	*1.31%*	*1.45%*	*1.62%*	*1.82%*	*2.03%*
Valuation Ratios					
P/E	*19.03*	*12.44*	*12.70*	*10.16*	*9.45*
P/BV	*4.16*	*3.24*	*2.71*	*2.24*	*1.90*
EV/EBITDA	*8.73*	*6.37*	*6.62*	*5.33*	*4.90*
Return on Investment					
ROCE	*21.78%*	*25.92%*	*21.25%*	*21.93%*	*19.91%*
ROIC	*28.26%*	*29.74%*	*22.97%*	*23.49%*	*21.32%*
ROTA	*11.20%*	*13.37%*	*11.99%*	*13.01%*	*11.96%*
Debt Equity	*1.05%*	*1.47%*	*1.42%*	*1.35%*	*1.31%*
Profitability Ratios					
EBITDA Margin	*16.68%*	*16.24%*	*14.80%*	*16.30%*	*15.30%*
PBT Margin	*15.09%*	*15.02%*	*13.46%*	*14.97%*	*14.02%*
PAT Margin	*8.56%*	*9.48%*	*8.84%*	*9.86%*	*9.22%*

FINANCIAL STATEMENTS

BALANCE SHEET	FY10A	FY11A	FY12E	FY13E	FY14E
Sources Of Funds					
Equity Share Capital	78.92	158.45	158.45	158.45	158.45
Reserves & Surplus	2553.23	3224.78	3886.71	4740.76	5648.65
Networth	**2632.15**	**3383.23**	**4045.16**	**4899.21**	**5807.10**
Secured Loans	26.62	49.85	57.33	65.93	75.82
Unsecured Loans	0.95	0.00	0.00	0.00	0.00
Deferred Tax Liability	17.44	30.53	45.80	36.64	31.14
Current Liabilities & Provisions					
Creditors	1365.88	1502.13	1577.54	1700.82	2031.88
Provisions	1130.92	1691.32	1545.99	1666.81	1849.01
Total Liabilities	**5173.96**	**6657.06**	**7271.81**	**8369.41**	**9794.95**
Application Of Funds					
Goodwill	18.12	18.12	18.12	18.12	18.12
Gross Block	1810.18	2045.62	2270.64	2520.41	2797.65
Less: Accum. Depreciation	1100.33	1201.82	1326.71	1465.33	1619.20
Net Block	**709.85**	**843.80**	**943.93**	**1055.08**	**1178.45**
Capital Work in Progress	21.26	34.16	42.48	47.48	58.92
Investments	142.99	172.99	216.24	270.30	337.87
Current Assets Loans and Advances					
Inventories	810.01	1147.61	1290.35	1325.14	1396.91
Sundry Debtors	906.64	1175.49	1183.16	1269.92	1714.40
Cash and Bank Balance	1191.84	1398.76	1466.81	1540.15	1617.16
Other Current Assets	22.19	29.74	38.96	49.09	61.85
Loans & Advances	1339.53	1827.95	2063.75	2786.52	3404.03
Miscellaneous Expense	11.53	8.44	8.02	7.62	7.24
Total Assets	**5173.96**	**6657.06**	**7271.81**	**8369.41**	**9794.95**

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