ArihantCapital
Generating Wealth

Initiating Coverage
24 October 2018

Ador Welding Ltd

With expected recovery in private capex cycle, Ador Welding to clock 23.6% PAT CAGR over FY18-20E, initiate coverage with BUY and TP of Rs 517

CMP : Rs 354

Rating : BUY

Target : Rs 517

STOCK INFO	
INDEX	
BSE	517041
NSE	ADORWELD
Bloomberg	AWL IN
Reuters	ADOR.BO
Sector	Industrial Goods
Face Value (Rs)	10
Equity Capital (Rs mn)	136
Mkt Cap (Rs mn)	4,956
52w H/L (Rs)	650 / 266
Avg Weekly Vol (BSE+NSE)	286,870

SHAREHOLDING PATTERN	%
(As on September, 2018)	
Promoters	56.7
Public & Others	43.3

STOCK PERFORMANCE(%)	3m	6m	12m
Ador Welding	27.8	-15.1	-34.0
SENSEX	-7.8	-1.8	7.8

Ador Welding v/s SENSEX



Source: ACE Equity, Arihant Research

With expected recovery in private capex cycle alongwith domestic demand revival, we expect Ador Welding Ltd (AWL) to report 8.8% CAGR in its revenues over FY18-20E, while PAT will witness a CAGR of 23.6% over the same period. EBITDA margin is expected to expand by 130 bps to 8.7% in FY20E from 7.4% in FY18. We remain positive on AWL's future growth prospects, and initiate coverage on the stock with a BUY rating and a target price of Rs 517 (25x FY20E earnings), giving an upside potential of 46%.

- **Demand revival to drive volume growth in consumables**

  Welding consumables contributed ~67% of revenue of AWL for FY18. In India, the welding consumables market is expected to exhibit a CAGR of 5.6% from 2014 to 2020. With gradual recovery expected in the IIP index over FY18-20E, the demand for industrial products will also improve. This in turn will help AWL to clock 10% CAGR growth in welding consumable over FY18-20E.

- **Change in revenue mix towards projects will aid margins**

  Over the last few years equipment and project segment's share in AWL's revenue mix has steadily increased from 20% in FY10 to 33.1% in FY18. Going forward we expect AWL's equipment and project segment revenues to contribute 33.8% and 34.7% respectively to its consolidated revenue in FY19E and FY20E. As the equipment and project segment offers better margins compared to consumables, AWL's EBITDA margin is expected to witness decent expansion of 130bps over FY18-20E with higher share of equipment business.

- **PAT to witness 23.6% CAGR over FY18-20E**

  With 8.8% CAGR revenue growth over FY18-20E and improving EBITDA margin from 7.4% in FY18 to 8.7% in FY20E, we expect AWL's PAT to grow from Rs 184mn in FY18 to Rs 281mn in FY20E, thereby registering a CAGR of 23.6% over FY18-20E.

- **Consistent dividend payout with high dividend yield**

  The current cash balance of AWL at the end of FY18 stands at Rs 175mn, which is expected to increase to Rs 383mn by FY20E. Further AWL has a track record of paying dividend for more than 15 years with the current dividend yield placed at 1.7%. Going forward with improving EBITDA margins and profitability, we expect AWL's dividend yield to reach 2.2% in FY20E from 1.7% in FY18.

Valuations

At CMP of Rs 354, AWL is trading at FY19E and FY20E, P/E multiples of 22.8x and 17.1x respectively. We value the stock at a FY20E target P/E multiple of 25x, which yields a target price of Rs 517 per share. We remain positive on AWL from a longer term perspective and initiate coverage on the stock with a BUY rating and a target price of Rs 517, which gives an upside potential of 46%.

Financial Performance

YE March (Rs Mn)	Net Sales	EBITDA	PAT	EPS (Rs)	EBITDA Margin %	RoE (%)	P/E (x)	EV/EBITDA (x)
FY16	4083	409	224	16.5	10.0	9.9	21.5	11.5
FY17	4424	301	179	13.1	6.8	7.6	27.0	16.5
FY18	4583	340	184	13.5	7.4	7.5	26.2	16.0
FY19E	4915	413	211	15.5	8.4	8.0	22.8	12.1
FY20E	5421	473	281	20.7	8.7	9.5	17.1	10.0

Source: Company, Arihant Research

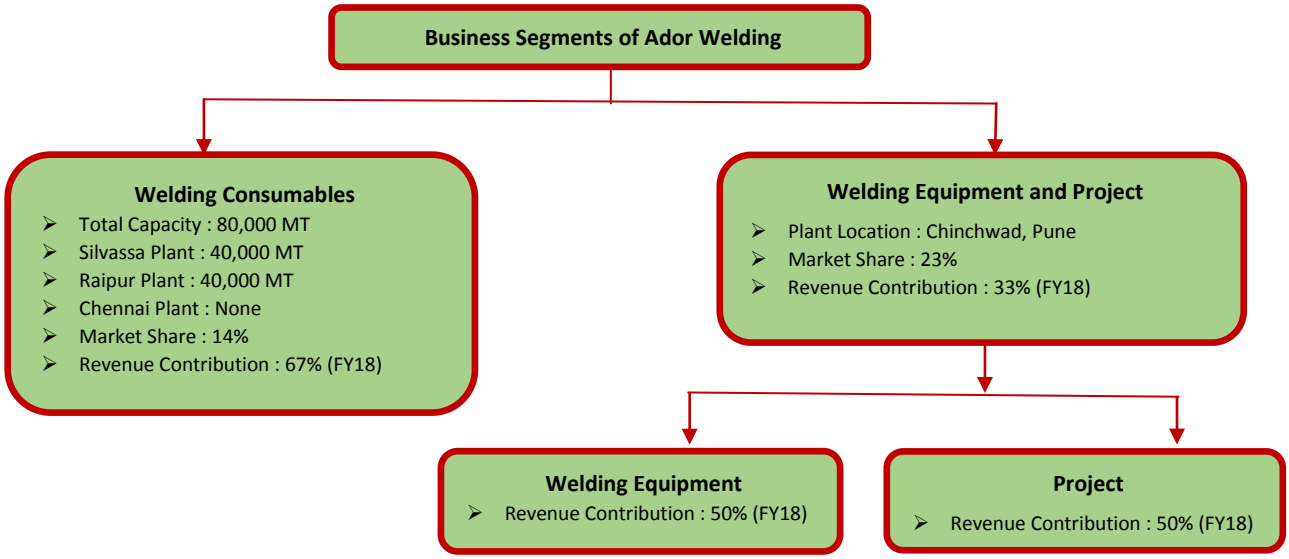
Arihant Capital Markets Limited | Research Analyst SEBI Registration No:INH000002764
1011, Solitaire Corporate Park, Bldg No.10, 1st Floor, Andheri Ghatkopar Link Rd, Chakala, Andheri (E), Mumbai 400 093.

Company Background

Ador Welding Ltd. (AWL) incorporated in the year 1951, is one of India's leading players in the field of Welding Products Technologies and Services. AWL offers comprehensive welding solutions, which includes a wide variety of electrodes, fluxes, flux-cored wires and special customised electrodes. The company covers the need of a whole range of industries like, steel, petro-chemicals, fertiliser, hydro-electric, thermal and nuclear power, heavy machinery, ship-building etc. AWL has reach in 70 plus countries and a comprehensive distribution network across the country with 300 plus distributors.

Business Verticals

AWL operates in two business segments; 1) Welding Consumables and 2) Welding Equipment and Project. In the organised segment of the Indian welding industry, AWL has ~14% market share in welding consumables and ~23% market share in welding equipment. The company has four manufacturing plants across India, out of which three (Raipur, Silvassa, Chennai) are for consumables and the fourth one at Chinchwad in Pune caters to AWL's equipment and project engineering business (PEB).



Source: Company, Arihant Research

- **Welding Consumables**

  This segment is into manufacturing of welding consumables (both manual and continuous) which include electrodes, fluxes, flux cored wires and special customised electrodes. At present the installed capacity of welding consumables stands at ~40,000MT spread across its three plants, Silvassa, Raipur and Chennai. Due to industrial slowdown in last few years, its Silvassa and Raipur plants are operating at 60% capacity utilisation, while the operation at its Chennai plant is currently suspended and the company has shifted some of its Chennai capacity to other two plants and only some job work is now done in Chennai plant.

- **Welding Equipment and Project**

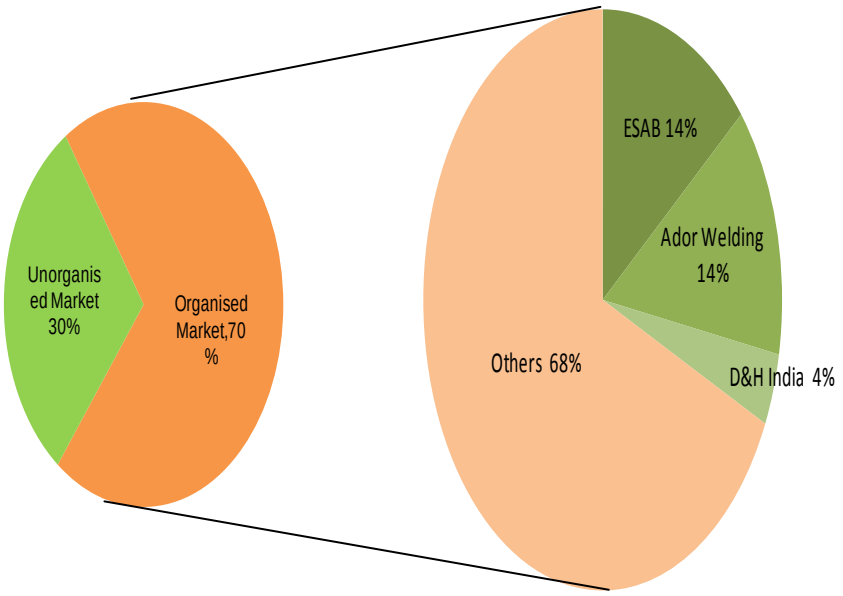
  This segment includes Equipment, Spares, Cutting Products and agency items related to equipment and cutting products. Apart from the welding equipment, this segment also has a division of Project Engineering Business (PEB) which undertakes services like design, manufacture, erection & commissioning, mechanical, electrical and instrumentation of process packages, process equipment, flare system & components, LSTK Turnkey projects and EPC contracts.

Investment Rationale

- **Ador Welding has a good brand name and market share in consumables market**

The welding industry in India has been expanding due to growth in end-use industries such as automobile & transportation, and building & construction. The welding consumables market accounts for a significant share in the welding industry compared to welding equipment and welding services. In India the welding consumables market is expected to exhibit a CAGR of 5.6% from 2014 to 2020. The relevant domestic market size is around Rs 31-35bn, out of which Rs 8-10bn is in imports/un-orgainsied sector, while rest Rs 23-25bn is in organised sector.

Market share of various players in welding consumables



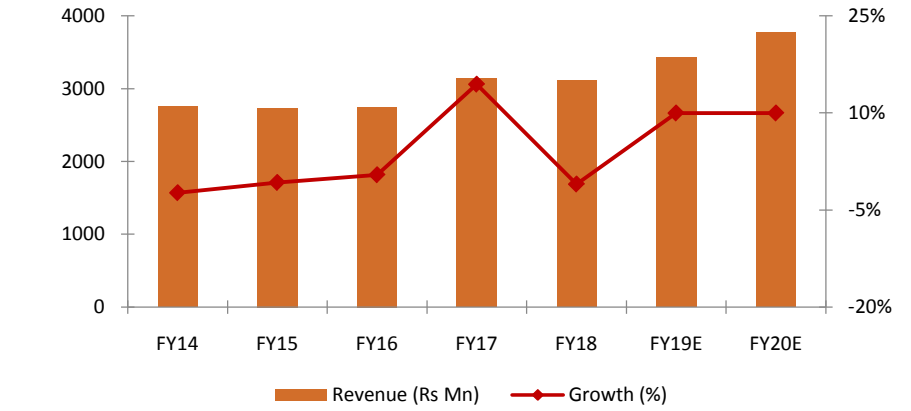
Source: Company, Arihant Research

By the end of 2020 the overall value of the India welding consumables market is expected to reach Rs 45.3bn from the present Rs 35bn. The domestic welding consumables industry is moderately fragmented with 30% being shared by hundred's of unorganized (small & regional) manufacturers while the balance 70% is accounted by the organized players like AWL, ESAB, D&H Welding etc. Currently AWL's share in the organized market for consumables stands at ~14%, similar to its closest peer ESAB which also has a market share of ~14%. Ador Welding has a good and established brand name in the consumables market and have good marquee clients with a decent 14% market share among the orgainsed players which augurs well for the company.

- **Domestic growth driver – demand revival to drive volume growth in consumables**

Welding consumables & equipment caters to the need of a whole range of industries such as steel, petrochemicals, fertilizers, hydro electric and thermal power, nuclear power, ship building, heavy machinery, defense, automobile, general fabrication and engineering. The growth in these sectors is merely the reflection of how the Index of Industrial Production (IIP) shapes up in the economy. With gradual recovery expected in the IIP index over FY18-20E, the demand for industrial products will also improve. This demand revival will in turn drive the volume growth of consumables for AWL. In our model we have factored in a 10% CAGR growth in welding consumable segment for AWL over FY18-20E.

Welding Consumable Segment Revenue Growth Trend

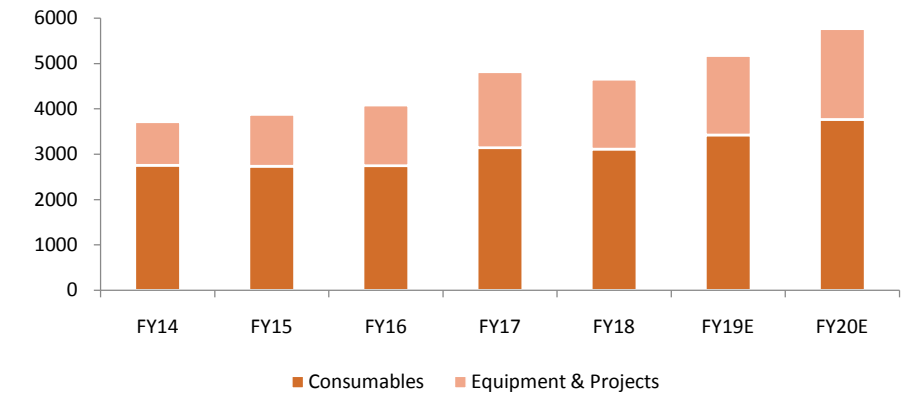


Source: Company, Arihant Research

- **Change in revenue mix towards more of equipment and projects will aid margins**

The welding consumables segment currently contributes 66.9% of the total revenues whereas rest 33.1% is accounted for by the Equipment and Project Engineering Business (PEB). Further in the latter segment, 50% of the revenue is contributed by the welding equipment while the balance comes from the PEB segment. Over the last few years equipment and project segment's share in AWL's revenue mix has steadily increased from 20% in FY10 to 33.1% in FY18. Going forward we expect AWL's equipment and project segment revenues to contribute 33.8% and 34.7% respectively to its consolidated revenue in FY19E and FY20E.

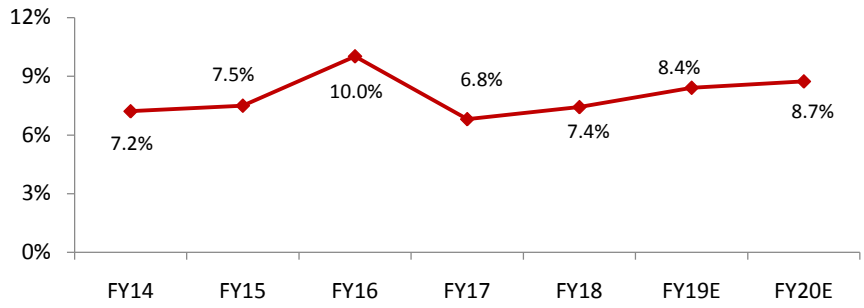
AWL's revenue mix over the years



Source: Company, Arihant Research

As the equipment and project segment offers better margins compared to consumables, AWL's EBITDA margin is expected to witness decent expansion going forward with higher share of equipment business. In our model we have factored in a 130bps expansion in AWL's EBITDA margin over FY18-20E.

AWL's EBITDA margin trend over the years

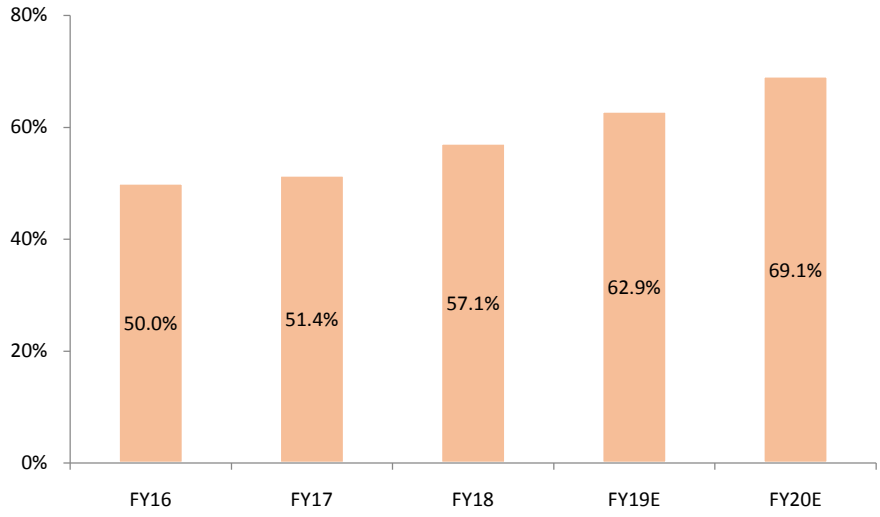


Source: Company, Arihant Research

- **Capacity utilisation to improve going forward**

At present, the total installed capacity of welding consumables stands at ~40,000MT spread across its three plants at Silvassa, Raipur and Chennai. Due to industrial slowdown in last few years its Silvassa and Raipur plants are operating at 50-60% capacity utilization, while the operation at its Chennai plant is currently suspended (from May 2014) and the company has shifted some of its Chennai capacity to other two plants and only some job work is now done in Chennai plant. With gradual recovery expected in the IIP index over FY18-20E, the demand for industrial products will also improve. This demand revival will in turn help AWL to improve its capacity utilization going forward which will in turn drive the volume growth of consumables for AWL. In our model we have factored in a gradual increase in AWL's capacity utilisation from 57.1% in FY18 to 62.9% in FY19E and 69.1% in FY20E.

AWL's capacity utilisation rate for its Silvassa & Raipur plants over the years

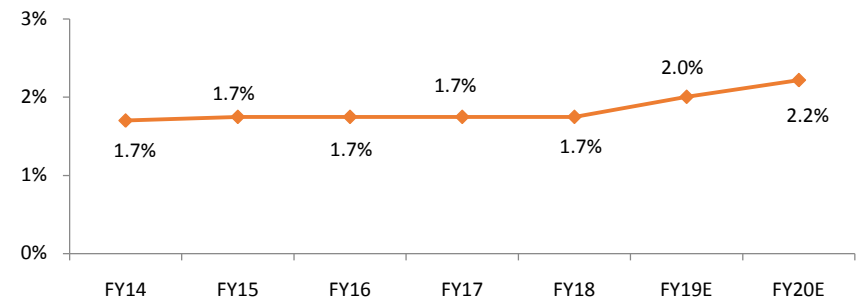


Source: Company, Arihant Research

- **Consistent dividend payout with high dividend yield**

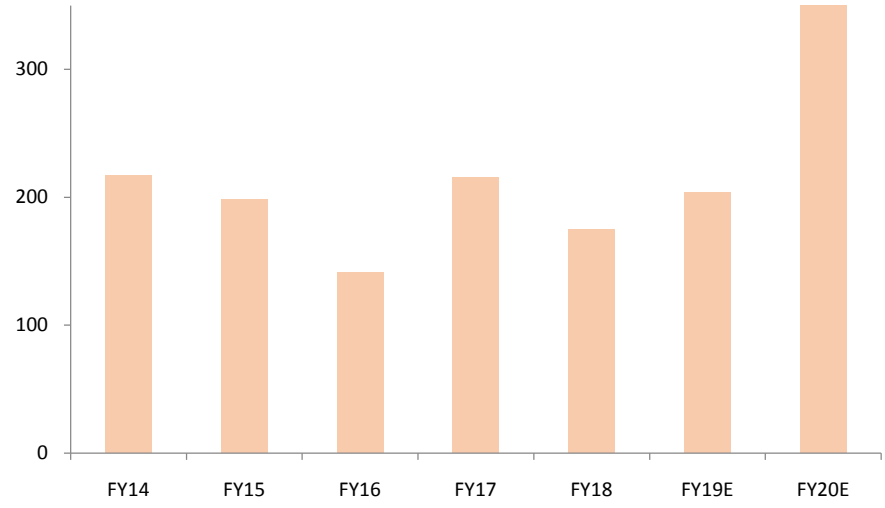
AWL used to be a debt free company with a clean balance sheet till FY16. However the company won a big PEB contract worth more than Rs 1bn from Kuwait in FY16. To execute this contract AWL has piled up debt in its books and consequently its working capital cycle got stretched and interest costs shot up from Rs 9mn in FY16 to Rs 53mn in FY18. As per company management this interest cost will peak out in FY19 to approx Rs 80mn and by end of FY19 the company will repay around 50-60% of its debt. As a result its interest cost will come down to a more normalised level of Rs 21mn in FY20E. The current cash balance of AWL at the end of FY18 stands at Rs 175mn, which is expected to increase to Rs 383mn by FY20E. Further AWL has a track record of paying dividend for more than 15 years with the current dividend yield placed at 1.7%. Going forward with improving EBITDA margins and profitability, we expect AWL's dividend yield to reach 2.2% in FY20E from 1.7% in FY18.

AWL's Dividend Yield over the years



Source: Company, Arihant Research

AWL's cash balance over the years

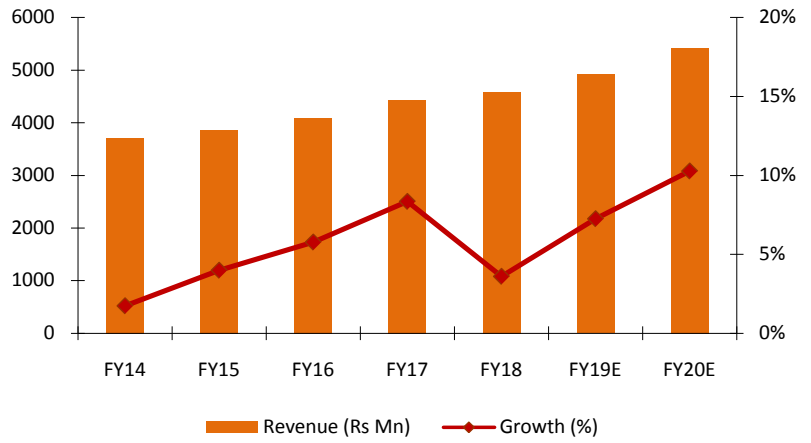


Source: Company, Arihant Research

Financial Performance Analysis

- **Revenue to witness 8.8% CAGR over FY18-20E**

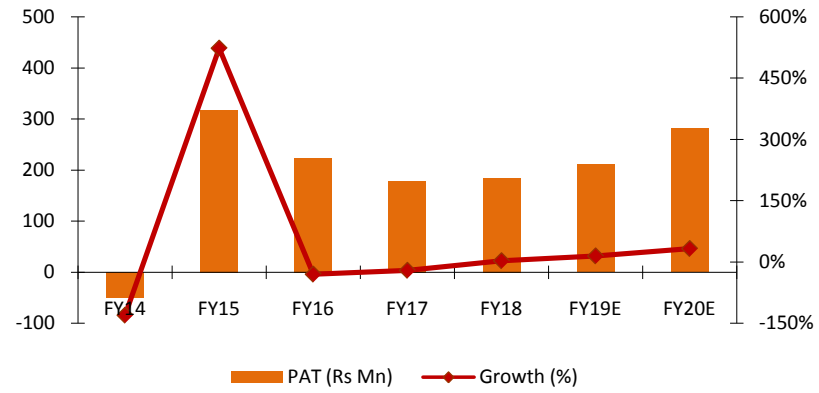
Due to lower capacity utilisation and subdued demand environment, AWL faced subdued growth in its revenues in past few years. With gradual increase expected in capacity utilisation from 57.1% in FY18 to 69.1% in FY20E, we expect revenue growth of AWL to bounce-back strongly to 10.3% YoY in FY20E from 3.6% in FY18.



Source: Company, Arihant Research

- **PAT to grow at 23.6% CAGR over FY18-FY20E**

With 8.8% CAGR revenue growth over FY18-20E and improving EBITDA margin from 7.4% in FY18 to 8.7% in FY20E, we expect AWL's PAT to grow from Rs 184mn in FY18 to Rs 281mn in FY20E, thereby registering a CAGR of 23.6% over FY18-20E.



Source: Company, Arihant Research

Q1FY19 and FY18 Financial Performance

Rs Mn	Q1FY19	Q4FY18	Q1FY18	Q-o-Q	Y-o-Y	FY18
Net Revenue	**1,026**	**1,452**	**871**	***-29.3%***	***17.8%***	**4,577**
Raw Material Cost	687	1,013	635	*-32.2%*	*8.2%*	3,272
Employee cost	106	91	96	*16.0%*	*10.3%*	383
Other Expenses	158	181	136	*-12.7%*	*16.2%*	583
EBITDA	**75**	**167**	**4**	***-54.8%***	***1780.0%***	**339**
EBITDA margin %	***7.3%***	***11.5%***	***0.5%***	***-414***	***687***	***7.4%***
Other Income	22	21	30	*6.2%*	*-25.2%*	97
Depreciation	24	24	26	*1.7%*	*-7.7%*	101
EBIT	**74**	**164**	**8**	***-55.2%***	***842.3%***	**336**
Finance cost	16	18	9	*-10.4%*	*85.2%*	53
Exceptional Item	-	-	-			-
PBT	**57**	**146**	**-1**	***-60.7%***	***NA***	**283**
Tax Expense	16	51	-0	*-69.0%*	*NA*	97
Effective tax rate %	27.8%	35.2%	30.0%			34.3%
Reported Net Profit	41	94	-1	*-56.3%*	*NA*	186
Adj Net Profit	**41**	**94**	**-1**	***-56.3%***	***NA***	**186**
Adj Net margin %	*3.9%*	*6.4%*	*-0.1%*	*-247*	*402*	*4.0%*
Reported EPS (Rs)	*3.0*	*6.9*	*-0.1*	*-56.3%*	*NA*	*13.6*
Adj EPS (Rs)	**3.0**	**6.9**	**-0.1**	***-56.3%***	***NA***	**13.6**

Source: Company, Arihant Research

Valuations

At CMP of Rs 354, AWL is trading at FY19E and FY20E, P/E multiples of 22.8x and 17.1x respectively. We value the stock at a FY20E target P/E multiple of 25x, which yields a target price of Rs 517 per share. We remain positive on Ador Welding from a longer term perspective and expect the financial performance of the company to improve substantially in the next 2-3 years, with revival in the capex cycle of the Indian economy. We initiate coverage on the stock with a BUY rating and a target price of Rs 517 (25x FY20E earnings), which gives an upside potential of 46%.

Peer Comparison

AWL's closest peer companies are ESAB India and D&H India. In the following table we have compared AWL with its peers ESAB India on key parameters. D&H is not covered by analysts and hence no forward data are available for it in Bloomberg.

Company Name (FY20E estimates)	Sales (Rs Mn)	EBITDA (Rs Mn)	EBITDA Margin (%)	PAT (Rs Mn)	EPS (Rs)	P/E (x)	P/BV (x)	ROE (%)
Ador Welding	5421	473	8.7	281	20.7	17.1	1.6	9.5
ESAB India	6162	654	10.6	458	29.8	29.3	2.9	9.9

Source: Company, Bloomberg, Arihant Research

Income Statement (Consolidated)

Y/E March (Rs Mn)	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E
Revenues	3,713	3,861	4,083	4,424	4,583	4,915	5,421
Change (%)	1.7%	4.0%	5.8%	8.3%	3.6%	7.2%	10.3%
Raw materials	2,455	2,549	2,614	3,060	3,216	3,515	3,849
Stock Adjustments	-47	55	-18	-35	-13	0	0
Employee costs	398	370	386	394	385	418	472
Other expenses	591	552	599	612	587	570	627
Total Expenses	**3,445**	**3,571**	**3,674**	**4,123**	**4,243**	**4,502**	**4,947**
EBITDA	**268**	**289**	**409**	**301**	**340**	**413**	**473**
Other Income	50	44	53	92	96	88	81
Depreciation	123	125	118	114	102	97	101
Interest	21	12	9	11	53	80	21
PBT	**174**	**196**	**335**	**269**	**281**	**325**	**433**
Extra-ordinary	130	-282	20	0	0	0	0
PBT after ext-ord.	**44**	**478**	**316**	**269**	**281**	**325**	**433**
Tax	95	159	92	90	97	114	152
Rate (%)	*54.8%*	*33.3%*	*29.1%*	*33.6%*	*34.5%*	*35.0%*	*35.0%*
PAT	**-51**	**319**	**224**	**179**	**184**	**211**	**281**
Change (%)	*-130.3%*	*-723.5%*	*-29.7%*	*-20.3%*	*3.1%*	*14.7%*	*33.2%*

Source: Company, Arihant Research

Balance Sheet (Consolidated)

Y/E March (Rs Mn)	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E
Sources of Funds							
Share Capital	136	136	136	136	136	136	136
Reserves & Surplus	1,549	1,889	2,116	2,213	2,314	2,504	2,826
Net Worth	**1,685**	**2,025**	**2,252**	**2,349**	**2,450**	**2,640**	**2,962**
Loan Funds	**173**	**2**	**27**	**356**	**813**	**400**	**300**
Deferred Tax & other liabilities	5	86	74	78	85	84	84
Capital Employed	**1,863**	**2,113**	**2,356**	**2,783**	**3,348**	**3,125**	**3,346**
Application of Funds							
Gross Block	2,294	2,313	2,247	2,350	2,423	2,523	2,623
Less: Depreciation	1,521	1,340	1,342	1,420	1,481	1,578	1,679
Net Block	774	974	905	931	942	945	944
CWIP	18	16	109	132	101	101	101
Other non current assets	8	9	198	213	255	205	305
Deferred tax assets	0	0	15	26	35	35	35
Net fixed assets	**799**	**998**	**1,227**	**1,303**	**1,332**	**1,285**	**1,384**
Investments	**138**	**65**	**134**	**107**	**24**	**24**	**24**
Debtors	783	833	1,184	765	920	1,010	1,114
Inventories	515	431	439	478	538	578	633
Cash & bank balance	217	198	141	215	175	204	383
Loans & advances & other CA	352	318	234	911	1,293	943	743
Total current assets	**1,868**	**1,779**	**1,998**	**2,370**	**2,927**	**2,734**	**2,872**
Current liabilities	767	552	926	897	891	875	891
Provisions	174	177	78	98	44	44	44
Net current assets	**927**	**1,050**	**994**	**1,374**	**1,992**	**1,815**	**1,937**
Total Assets	**1,863**	**2,113**	**2,356**	**2,783**	**3,348**	**3,125**	**3,346**

Source: Company, Arihant Research

Cash Flow Statement (Consolidated)

Y/E March (Rs Mn)	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E
PBT	**44**	**478**	**316**	**269**	**281**	**325**	**433**
Depreciation	123	125	118	114	102	97	101
Interest & others	-29	-32	-44	-81	-43	-8	-60
Cash flow before WC changes	138	571	390	301	340	413	473
(Inc)/dec in working capital	**-49**	**-266**	**-132**	**-402**	**-736**	**88**	**-120**
Operating CF after WC changes	89	305	257	-101	-396	501	353
Less: Taxes	-89	-52	-92	-90	-97	-114	-152
Operating cash flow	**-1**	**253**	**165**	**-191**	**-493**	**388**	**202**
(Inc)/dec in F.A + CWIP	176	-18	-136	-154	-92	-50	-200
(Pur)/sale of investment	134	73	-70	28	82	0	0
Cash flow from investing	**310**	**55**	**-206**	**-126**	**-10**	**-50**	**-200**
Free cash flow (FCF)	**-71**	**235**	**234**	**-319**	**-535**	**288**	**102**
Loan raised/(repaid)	83	-171	25	330	457	-413	-100
Equity raised	0	0	0	0	0	0	0
Interest & others	-143	-73	41	144	87	198	381
Dividend	-80	-82	-82	-82	-82	-94	-104
Cash flow from financing activities	**-140**	**-326**	**-16**	**391**	**462**	**-309**	**177**
Net inc /(dec) in cash	**170**	**-19**	**-57**	**74**	**-40**	**29**	**179**
Opening balance of cash	47	217	198	141	215	175	204
Closing balance of cash	217	198	141	215	175	204	383

Source: Company, Arihant Research

Key Ratios (Consolidated)

Y/E March (Rs Mn)	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E
Per share (Rs)							
EPS	-3.8	23.4	16.5	13.1	13.5	15.5	20.7
CEPS	5.3	32.6	25.1	21.5	21.0	22.7	28.1
BVPS	123.9	148.9	165.6	172.7	180.2	194.2	217.8
DPS	5.9	6.0	6.0	6.0	6.0	6.9	7.6
Payout (%)	-155.8%	25.7%	36.5%	45.8%	44.4%	44.4%	36.9%
Valuation (x)							
P/E	-94.2	15.1	21.5	27.0	26.2	22.8	17.1
P/CEPS	67.1	10.8	14.1	16.5	16.8	15.6	12.6
P/BV	2.9	2.4	2.1	2.0	2.0	1.8	1.6
EV/EBITDA	17.8	16.0	11.5	16.5	16.0	12.1	10.0
Dividend Yield (%)	1.7%	1.7%	1.7%	1.7%	1.7%	1.9%	2.2%
Return ratio (%)							
EBIDTA Margin	7.2%	7.5%	10.0%	6.8%	7.4%	8.4%	8.7%
PAT Margin	-1.4%	8.3%	5.5%	4.0%	4.0%	4.3%	5.2%
ROE	-3.0%	15.7%	9.9%	7.6%	7.5%	8.0%	9.5%
ROCE	7.8%	7.8%	12.4%	6.7%	7.1%	10.1%	11.1%
Leverage Ratio (%)							
Total D/E	0.1	0.0	0.0	0.2	0.3	0.2	0.1
Net D/E	0.0	-0.1	-0.1	0.1	0.3	0.1	0.0
Turnover Ratios							
Asset Turnover (x)	2.0	1.8	1.7	1.6	1.4	1.6	1.6
Inventory Days	77	59	60	56	60	60	60
Receivable Days	77	79	106	63	73	75	75
Payable days	93	69	90	82	74	65	60

Source: Company, Arihant Research

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Stock Rating Scale

	Absolute Return
BUY	>20%
ACCUMULATE	12% to 20%
HOLD	5% to 12%
NEUTRAL	-5% to 5%
REDUCE	<-5%

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