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ABG Shipyard

Cruising Ahead on Capex

The ongoing capex plans would hike ABG Shipyard's ship-building capacity substantially and build rig-making facility, which would augment its revenues in future. Kaustubh Ghotikar meets up with the management to get an insight and gauge the impact of the company's plans.

ABG Shipyard (ABG), the Gujarat-based ship-building company, has been in the news quite a lot lately, be it for the counter entering the F&O segment or its total order book touching a new high of Rs 9,400 crore or its future plans for a third shipyard at a huge capex. But despite all this hype, instead of the scrip moving up sharply the counter failed to attract investors' interest and has remained quite range bound since July. This has happened especially when one could have

actually expected some bounce-back in the scrip considering the fact that at CMP of Rs 354, it has corrected 64 per cent from its January peak of Rs 1030. Thus, in order to get more insight on the company and its plans and whether it can make sense for investors to enter it at this point of time, we had a tête-à-tête with ABG Shipyard's CFO Dhnananjay Datar.

Datar revealed that the company is currently focussing only on executing its plans at Surat and Dahej. However, when probed about the plans for the third shipyard, he was also quick

enough to clarify that though there are some future plans, these are only plans and there is not much progress on that front.

ABG is basically into shipbuilding business and had come out with an IPO in 2005 to partly fund its new shipyard at Dahej. As promised during the IPO, the company did commence its Dahej shipyard by end of March 2008. Dahej Shipyard has a capacity to build upto 12 vessels and will now power the future growth of ABG. However, ABG already has an existing shipyard at Surat with capacity of

building 36 vessels, which till FY08 has been the sole bread winner for the company. This shipyard has delivered more than 104 vessels. In a bid to drive its growth, ABG is not only undergoing re-engineering and expansion at its existing Surat facility, but also chalked out a huge capex to build a rigyard at its existing Dahej complex.

Surat expansion

The Surat expansion entails a capex of Rs 496 crore and would entirely be funded from the internal accruals. ABG has already utilized around Rs 170 crore for this project till date. The Surat shipyard is spread over 35 acres of land and has capacity to build 36 vessels. In 2007, it had also acquired a nearby shipyard called Vipul Shipyard, which is spread over seven acres with a capacity to build eight vessels. Through this expansion, the company aims at streamlining its operations whereby it will merge both the yards and shift its entire fabrication facility to Vipul Shipyard. This would lead to augmenting the capacities at existing facilities. ABG has also bought an additional 10 acres of land adjoining their facilities. The Surat expansion is expected to be fully operational by March 2009. Hence, the benefits of this expansion will bring be seen only in FY10.

Dahej rig project

The Dahej rig project entails a capex of Rs 675 crore, of which Rs 60 crore is through internal accruals, while the balance Rs 615 crore is funded through debt. ABG has already drawn Rs 250 crore for the project. This would increase ABG's average cost of borrowing to 7.37 per cent in FY09. This facility would have a rigyard with a capacity to build four rigs per year. The facility would be commissioned around March 2009. "Dahej rig project should be operational by March or April 2009, but full completion could stretch to June-July 2009," says Datar. On the orders for this rig facility, Datar explains, "Currently we have no orders for rigs, but we are marketing the same and the way the negotiations are on

with so many buyers, I think we should be close to getting orders." Apart from that, ABG also has plans to revive Western India Shipyard through restructuring. However, the company is waiting to have management control, which is expected by end of this fiscal.

We believe ABG is poised tantalisingly to take advantage of the opportunities that lie ahead. ABG has build a good order book of Rs 9,400 crore (almost 10 times its FY08 sales) till date, executable over the next four years. This gives good revenue visibility for the company. Secondly, with Dahej shipbuilding facility now on stream, the company could deliver more ships out of its yards in coming period, which is a good sign. Thirdly, the oil and gas exploration activities are on the rise and this would generate good demand for offshore supply vessels (OSVs). Besides, with 73 per cent of anchor handling tug supply (AHTS) fleet and 62 per cent of the platform supply vessels above the age of 20 years globally, there would be good

replacement demand for companies such as ABG. Currently, OSVs form 25 per cent of the total order book compared to 62 per cent of bulk carriers. But the management strongly believes in demand for OSVs in the future and hence wants to focus more on OSV in the coming years.

However, there are also certain concerns which cannot be overlooked. Firstly, though the company has a huge order book, there is always an execution risk, implying whether the company would be able to execute the orders within the stipulated time. Besides, this risk would further aggravate if the input costs keep rising. The prices of commodities such as steel continue to be a matter of concern for ABG. "The biggest challenge that we faced in the past six months is the commodity prices. Fortunately, the commodity prices have been cooling off. If the commodity prices come down, then we don't see any impact, but if they don't come down, we should be prepared to take a hit of at least three per cent on net profit margins," says Datar. Besides, concerns over global slowdown and credit crunch could also keep away buyers from placing new orders for ships, which could impact order book growth for companies such as ABG.

Financial Performance & Valuations

For Q1FY09, its topline increased 33.84 per cent to Rs 272.24 crore (Rs 203.34 crore), while the bottomline grew 40 per cent to Rs 47.01 crore (Rs 33.40 crore). The management expects its topline to grow around 40 per cent in the next 4-5 years, while it hopes to maintain its margins in FY09. Thus, ABG could post topline of around Rs 1,354 crore, while the bottomline on a conservative basis would be around Rs 184 crore for FY09, a growth of 14 per cent over FY08. At these estimates, ABG could notch up an EPS of around Rs 36, thereby posting a PE of 9.9x for FY09. At these valuations, we see an upside of about 21 per cent from the current levels. We recommend a buy on ABG with a one year price target of Rs 434.



FINANCIAL SNAPSHOT OF ABG V/S PEERS (Rs/Cr)		
Particulars (FY08)	ABG	Bharati
Sales	966.83	640
NP	161.09	106.35
Equity	50.92	27.57
FV (Rs)	10	10
CMP (Rs)	354	291
Market cap	1807	802
Mcap to Sales (x)	1.87	1.25
EPS (Rs)	31.53	38.58
P/E (x)	11.62	7.54
Dividend (Rs)	2	3
Promoters (%)	56.9	36.31
Institutional (%)	22.71	49.97