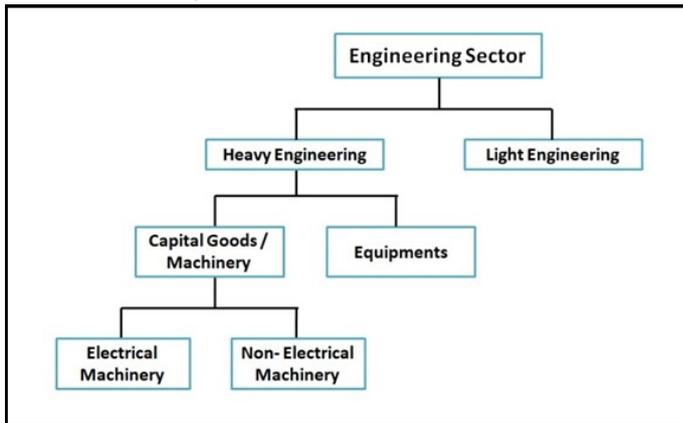


**OVERVIEW: Industry:**

Engineering is a large diverse industry with various segments. It spans across a range of companies from different domains. It could have players from the electrical, non-electrical machinery or a static equipment manufacturer. All from a power equipment manufacturer like catering to transformers or boilers, to an Engineering, Procurement and Construction (EPC) company or for that matter niche players that provide environment friendly solutions like waste water and air pollution treatment plants.

**Exhibit: Industry Bifurcation:**



Source: Market Reports

The Indian engineering sector is divided into two major segments- heavy engineering and light engineering. The capital turnover in India which was ~USD70bn in 2017 is expected to grow to USD115bn by 2025. Likewise, the electrical equipment market size is expected to reach USD100bn by FY21-22. Comparative advantage vis-a-vis peers in terms of manufacturing costs, market knowledge, technology and creativity has been a driving force for engineering exports from India.

With the evident lack of quality infrastructure in India; the construction industry has been witnessing strong growth with large spends on Housing, commuting modes like Roads, Ports, Rail Transport and Airport Development. The subdued growth of the sector is attributed to the delays of various big ticket projects in recent years due to myriad reasons. Infrastructure is one of the key areas of operation for major Indian engineering companies and a potential sector of growth for them. Further, the Construction equipment market is projected to reach USD7bn by 2020 from USD4.2bn in FY17 adding impetus to growth opportunities.

Almost 70-75% of the revenues of the Engineering sector is garnered from the Power sector. With the govt. plans chalked for addition of large generation and T&D capacities, huge potential is awaited by the engineering players once the short term challenges are met.

Any company in the engineering sector will be gauged by the order book size, one of the key determinants of performance. This is applicable for construction companies as well, as their indicator of revenue visibility.

The demand for the engineering sector comes from the capex across different sectors like Infrastructure, Power, Mining, Oil & Gas, Refinery, Steel, Automotive and Consumer to mention a few. The other triggers include, 100% Foreign Direct Investment (FDI) allowed through the automatic route and initiatives like 'Make in India', due to which there has been entry of different international players as well. (Source: IBEF).

SNAPSHOT				
52 week H / L	Mcap (INR mn)			
135 / 53	2,359			
Face value: 1				
BSE Code	NSE CODE			
522134	-			
Annual Performance				
(Rs mn)	FY16	FY17	FY18	FY19E
Sales (Net)	1,107	1,006	1,322	1,784
EBITDA	42	44	27	89
EBITDA (%)	3.8	4.3	2.0	5.0
Other Income	32	62	93	70
Interest	37	40	54	61
Depreciation	19	9	10	13
PBT	19	57	55	85
PAT	19	272	14	43
Equity (Rs mn)	37	37	37	37
EPS (INR)	1	7	0.4	1
Quarterly Performance				
Parameters (Rs mn)	Sep-17	Dec-17	Mar-18	June-18
Sales (Net)	281	280	467	362
EBITDA	14	-0.1	-6	-15
EBITDA (%)	5	-0.04	-1	-4
Other Income	14	33	41	2
Interest	14	13	13	15
Depreciation	2	2	4	3
PAT	5	4	-1	-29
Equity (Rs mn)	37	37	37	37
Ratio Analysis				
Parameters (Rs mn)	FY16	FY17	FY18	FY19E
EV/EBITDA (x)	68	58	97	29
EV/Net Sales (x)	3	3	2	1
M Cap/Sales (x)	2	2	2	1
M Cap/EBITDA (x)	56	54	87	26
Debt/Equity (x)	-1	4	5	3
ROCE (%)	-23	-	46	52
Price/Book Value (x)	-4	39	40	23
P/E (x)	127	9	171	28
Share Holding Pattern as on 30th June, 2018				
Parameters	No of Shares	%		
Promoters	2,76,90,000	75.0		
Institutions	5,045	0.01		
Public	92,24,955	25.0		
TOTAL	3,69,20,000	100.0		

Source: Annual Report

Note: All the data is calculated as per Market Price on 04th September 2018

**Artson Engineering Limited**

**BUY**

**CMP: Rs.64**

**TARGET PRICE: Rs.95**

**TIME : 12 months**

**About the Company:**

Artson Engineering Limited (AEL) a multi-disciplinary design and construction services company is a majority owned subsidiary of TATA Projects Limited (TPL). Tata Projects is one of India's fastest growing Industrial & Urban Infrastructure companies and owns 75% of paid-up equity shares of AEL. The Company is engaged in the business as EPC contractor in the field of Oil & Gas and Hydrocarbon Processing Industry, specialized in Tankages, Piping and other Mechanical Packages. It has executed many large and prestigious Projects in Oil Refinery Tankages, Piping & Mechanical packages, Chemical, Oil & Gas, Refinery Product storage & Distribution Terminals, Cross-country Pipelines and Mechanical equipment construction projects in Metals, Mining, Power etc. The Company has manufacturing facilities in Nasik, Nagpur and Jamshedpur. Through the manufacturing facility located in Nasik, AEL is equipped to manufacture high quality/ certified pressure vessels, columns, heat exchangers and other process equipments. This facility along with the one located at Nagpur is accredited with major certifications needed by a fabrication company. The company has proven track record of manufacturing complex equipment with various materials of Construction like Carbon Steel, Stainless Steel, Hastelloy, Alloy 20 and Incoloy. The company has Mr. Vinayak Deshpande as the Chairman and Mr. Saket Mathur as the manager and COO of the company.

**INVESTMENT RATIONALE:**

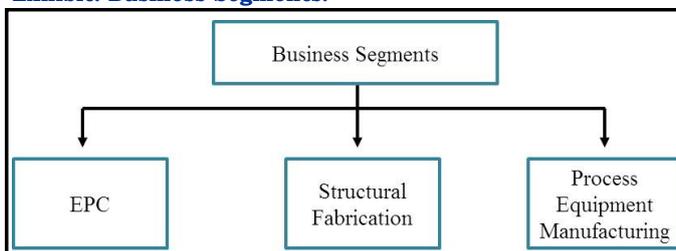
**A) Business Structure:**

The three major business divisions of the company include:

**(i) EPC Division:**

AEL specializes in Engineering, Procurement & Construction of large diameter storage tanks, Equipment & Piping projects, Structural Fabrication Projects for variety of Process plants including Oil & Gas, Steel and Thermal Power. The efficient Supply Chain Management handles all the procurement related activities including long term partnership & strategic procurement and ensures timely deliveries to the Projects.

**Exhibit: Business Segments:**



Source: Company's Website

With regard to the EPC services in Oil and Gas Sector, the company specializes in storage terminals for Oil and Gas. The company has a strong base in Engineering encompassing Designing, Detailing, Layouts, Pipe stress analysis, Civil, Mechanical, Electricals and Instrumentation and commissioning assistance. In the near future, AEL foresees good business opportunities in tank construction and expects more structural fabrication orders going forward.

**(ii) Structural Fabrication:**

AEL has invested in large fabrication yards located in Nagpur, Jamshedpur and Ranchi to cater to Structural steel fabrication and maintenance / erection services for variety of industries including Oil & Gas, Steel and Thermal Power. With a summated production capacity of more than 2000MT/month and fabrication yard area of more than 50,000 sq.mt, the company is equipped for manufacturing Plant building structures (Rolled & Built-up sections), Technology structures, Pipe Racks, Plate fabricated pipes & Mitre bends of large diameter, Stack / Chimney, Silos of large diameter, Ducting / Cladding etc.

**(iii) Process Equipments Manufacturing:**

AEL is equipped to manufacture high quality / certified Pressure vessels, Buffer Vessels, Columns, Heat exchangers, Stacks, Storage Tanks, LPG/Propane Bullets complying with International Codes such as ASME, PD 5500, API, TEMA, IBR and Indian Standards.

**Key Clients of the Company:**

Some of the key clients of the company include, GAIL, Aditya Birla, Lubrizol, L&T, Cylingas, Essar, BPCL, Deepak Fertilizers, Technip, Cairn, Heisco, SAIL, BARC, IOL, Toyo Engineering, Tata Steel, Enoc, HMEL, Tata projects, RIL, UPL, Aegis, Godrej to mention a few.

**B) The Company So Far:**

AEL has seen it all from being a successful company to BIFR and back on track poised to grow.

**Growth Path:**

AEL is engaged in pioneering work in developing products and systems in fuel handling and tankage construction activities in refineries, making it one of the foremost companies in India with specialization in Petroleum Storage and handling systems. Over the years, the company has developed its capabilities in the multi-disciplinary construction fields for the Hydrocarbon process industry and has successfully executed, on turnkey basis, many prestigious construction contracts. AEL has thus emerged as one of the leading Design, Engineering, Procurement and Construction Companies in the Petroleum Storage and handling system. During the span of three decades, the Company has successfully commissioned, on turnkey basis, several fuel storage and handling facility systems and emerged as one of the foremost companies in the country which specializes in such systems. AEL's expertise has gradually expanded beyond the country and has been executing prestigious overseas contracts as well.

It went to BIFR and in order to capitalise on the fabrication technology of the company, Tata Projects Limited (TPL), entered as the strategic investor and co-promoter of the Company by acquiring 75% stake. The Company could not post positive PAT till 2015-16 due to the challenging economic conditions and financial pre-qualification issue in PSU sector. Since FY17 however, the Company has improved the financial position substantially and is net worth positive having technical as well as financial ability to service the PSU sector of interest.

**B) The Company So Far (contd.):**

TPL is providing full support and AEL has recently passed an enabling resolution where TPL can give orders to the company to the extent of Rs500cr per year. It has also financially extended a loan of Rs40cr and this loan is repayable over 20 years for which the interest rate is nil. The only condition is that AEL cannot declare any dividend until the entire loan is repaid. AEL's management aims to clear this in coming 3-4 years. The company has now turned the corner and being net worth positive has enabled it to bid for large size and big-ticket orders. It has improved the order book position substantially over the past 2 years. The management is ensuring that the right size teams are built to execute the projects in these opportunities and also is focusing on operational excellence initiatives to improve its productivity.

**C) Reviving the Order Flow: Tapping Different Genres:**

During the year under review, the company achieved major progress related to construction of tank farm and civil/mechanical work for connector pipelines project at domestic airport, Mumbai. Construction of 1 tank out of 4 nos. Of large diameter (79Mtrs.) tanks for storage of crude oil at IOCL, Paradip is completed. In addition to above, contracts related to piping packages at APGENCO Krishnapatnam and NTPC Ramagundam are under execution. Successful completion of these projects will enable AEL a better pre-qualification eligibility to pursue more projects of similar nature. The Company is also executing orders for supply of approx. 1000MT of fabricated steel structures to FL Smidth from Nagpur facility and approx. 200MT of process equipment orders are completed for various chemical and process industries from Nashik facility.

**Orders Received in FY18:**

- Rs73.8mn work order from M/s ISGEC Heavy Engineering Limited for fabrication and erection of CHP structure at Krishnapatnam.
  - Rs47mn order from M/s FL Smidth Ltd. for fabrication and supply of building structures.
  - Orders worth Rs1,285mn from the Holding Company, i.e., Tata Projects Limited (TPL) for fabrication and supply of structures and site works for piping, tankages, equipment erection for their various projects in India and abroad.
  - Orders worth approx. Rs45mn from M/s UPL Limited; M/s Indian Oil Corporation Limited and M/s Hindalco Industries Limited.
- During FY18, AEL received fresh orders worth Rs1,340mn. It concluded the year with an order backlog of Rs1,520mn vs. Rs1,500mn the previous year.

**Some of the Recent Orders Received:**

- Order worth Rs150mn from ThyssenKrupp Industries India Private Limited for fabrication and supply of approximately 2000 metric tonne of CHP structures for a power plant in Uttar Pradesh which is expected to get executed in 5 months.
- Order worth Rs257mn was awarded by Bharat Petroleum Corporation Limited for construction of 19 tanks of various types.
- Order worth Rs242mn awarded by GMR Hyderabad International Airport Limited for ATF tanks and associated work on EPC basis.

**(D) Structural Fabrication- The Scope Ahead:**

Structural Steel Fabrication is about to witness exponential growth in India over the next 10 years with different Government initiatives like "Make In India" to augur well for the expansion. In developed countries more than 70% single storey commercial buildings are developed with Pre-Engineered Building (PEB) concept whereas in India it is below 1% which leaves a huge scope for penetration into this segment. With the growth potential visible across the Steel sector indicated by the statistics of Per Capita Consumption of Steel in developed countries being more than 200kg whereas in India it is below 60kg, would give impetus to the fabrication aspect of business. Even in the commercial space, the sector (excluding Housing) is expected to reach 20.44bn sq.ft. by 2030 against current 8bn. Taking it further, different other boosters to the fabrication space include, Rs7060cr allocated for developing 100 Smart Cities and India Green Building Council (IGBC) targeting to cover 10bn Sq. Ft by 2022 with Green Buildings against current 2bn Sq. Ft. Overall, there is untapped potential seen across the fabrication space for different industries and the company stands to benefit from the same.

**(E) Oil & Gas sector - Impetus for Storage Tanks Requirements:**

Oil production has witnessed significant growth rate as compared to the demand from end-use industries. This has urged the suppliers to enhance their inventories and infrastructure to store large quantities of crude oil and also providing a hedge to fluctuating crude oil prices. Adding to this, the major challenge faced by the Ministry of Petroleum and Natural Gas is the fact that a hefty 77% of the country's energy requirements including oil, gas, and petroleum are sourced from abroad, thereby consuming large reserves of India's foreign exchange. Prime Minister Modi has asked the ministry to work overtime to reduce this import dependence to 67% by the year 2022.

In order to deal with the above situation, fabricating steel tanks is pre-requisite, giving a huge scope for fabricating segment of the company.

**F) Modular Warehousing and Molding Fabrication- Focus Going Forward:**

**What is Modular warehousing?**

Modular warehousing is a segmented yet strategic approach to distribution center (DC) design. It consists of (a) "deconstructing" a traditional warehouse by identifying its various essential functions and (b) developing a variety of scalable, agile modules for each function that can either be integrated with other functional modules within the same DC or serve as standalone yet virtually connected operations. With the supply chain challenges that companies will inevitably face, the time is now to explore a more varied approach to warehousing.

**Artson Engineering Limited**

**BUY**

**CMP: Rs.64**

**TARGET PRICE: Rs.95**

**TIME : 12 months**

**Modular Warehousing and Molding Fabrication- Focus Going Forward: (contd.)**

Advantages over the traditional:

**Long life span:** Due to its modular nature, the building can be demounted, and moved to another location if ever required.

**Easy to erect:** The building frame is manufactured to enable quick and easy erection at remote sites and the modular format makes for easy and economical transportation.

The beauty of the concept is that modules can be assembled and located in a wide variety of ways based on the current needs of various customer segments and then relocated, rearranged or replaced as these requirements or other market conditions change. Warehousing being one of the essentials for the Logistics sector, growth projected across the industry will give impetus to this latest smart solution of storage / warehousing. (Source: Market research reports).

AEL has identified this as one of the prospective areas of growth going forward and hence has started the required spade work for the same.

In addition to the above diversification, the company is also looking at Molding fabrication as another avenue of opportunity. In layman terms, molding is the process used in Manufacturing to shape different materials. The company intends to enter molded fabricated material used in the construction equipment. We all know that the company has strong fabrication facilities and technology and in order to capitalise on this it has plans to look into mould fabrication for the construction sector and it is learnt that some trial orders are already being done.

Overall, these two segments would be the on the radar of the business development of the company.

**Positive Outlook: Management efforts:**

Structural steel fabrication and manufacturing is expected to witness strong growth in India for the next 10 years. With recent positive political and economic developments, and 'Make in India' initiative, India is poised to take Lion's share of Global investment and anticipated to achieve high GDP growth rates in the coming years. AEL is pursuing mechanization of manufacturing facilities to cater to market requirements. It is also focusing on building capabilities to become an equipment builder, integrator and end to end solution provider to Indian industry. In spite of an optimistic future outlook, the rising input cost of raw steel, uncertain delivery schedule from steel manufacturers and pressure on working capital are major risks to business pursued by the Company. In the near future, AEL foresees good business opportunities in tank construction and more structural fabrication orders from the market. It has focused on recruitment and re-skilling of execution team to address the delivery of various projects to be executed and is confident of completing the projects within the scheduled time and thus achieving growth in the near future. It is also focusing on liquidating the matters pertaining to refunds from the statutory authorities and efforts have resulted in the receipt of certain refunds from the various authorities such as Income Tax and VAT. The company is optimistic on receipt of substantial refunds during the year 2018-19. AEL with the support of TPL, is putting earnest efforts to further improve the operations and record better performance going forward.

**Financials:**

Post the BIFR exit, the infusion done and positive waivers that the company enjoys provided by TPL has helped it revive in term of financials. FY18 numbers show the requisite turnaround, although not at the operational levels though but for the PBT levels.

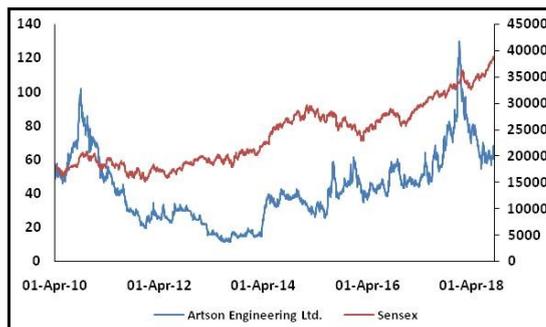
**Risks and Concerns:**

In spite of an optimistic future outlook, the rising input cost of raw steel, uncertain delivery schedule from steel manufacturers and pressure on working capital are major risks to business pursued by the Company. In the near future, the Company foresees good business opportunities in tank construction and more structural fabrication orders from the market.

**Outlook and Valuations:**

With the kind of growth expected in the segments that the company caters to and also the turnaround that the company is working towards to get back to operational efficiency, one can expect that slowly and gradually it would be one of the apt contenders in the space. Earnest efforts are being made to ramp up on the clients being served and the industries being catered. It would definitely be time consuming for the company to get back on track but the initial steps have been chalked well, boosting the confidence in the business strategies. This would also expect patience from the investors. Also to add, is the strong parentage that the company enjoys in terms of financial aid as well future order pipeline. We believe that this would be the right time to SIP into the stock and thereby we initiate BUY on the stock with a target price of Rs95 over a 12 months horizon.

**Exhibit: Artson vs. Sensex**



Source: Ace Equity

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