



JainMatrix Investments

A quality report by JainMatrix Investments

Inox Wind IPO – Positive for the Environment



- Date 18th March 2015
- Price range: Rs. 315-325 and Period: 18-20th Mar 2015
- Advice: medium risk BUY, for a period of 2 years

- Mid Cap – Rs 7200 cr Mkt Cap
- Industry – Wind Power (Equipment and Projects)

Summary

- INOX is certainly in the right sector of Wind power generation, where we should see good double digit growth for a decade. It also is an environmentally positive segment. The government is doing a lot to promote / subsidize it.
- The firm itself has scaled up well so far, and the promotor group is good. There is also a scarcity of good quality listed firms in this sector.
- The challenge for this firm is to manage costs, cash flows and technology stability. It has to perhaps slow down growth in the next few years order to be a more financially feasible concern.
- The INOX Wind IPO is rated a medium risk BUY, investors can purchase for a 2 year holding period.

Here is a note on Inox Wind Ltd. IPO (INOX).

IPO highlights

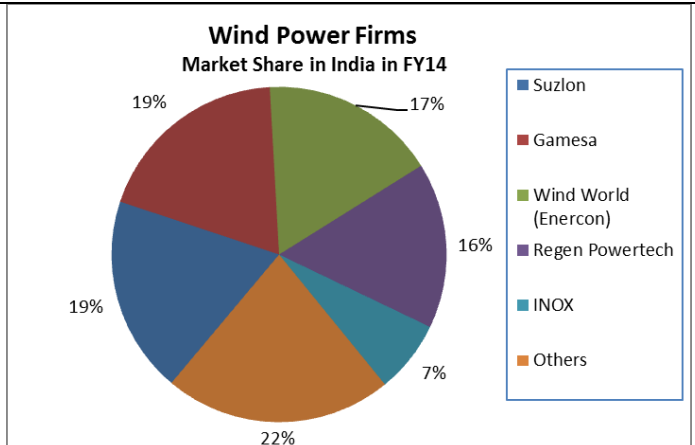
- IPO is open from 18-20th Mar 2015 with Issue Price band: Rs.315-325 per share
- There is a discount of Rs 15 for retail and employee categories
- Shares offered to public: 3.26 crores of Face Value: Rs.10 per share
- Shares offered as portion of equity post issue: 13.9%
- Amount proposed to be raised: Rs.1025 crores (at upper end). The IPO proceed will be used for:
 - 300 crore is an exit by Inox Wind promoter Gujarat Fluorochemicals
 - 300 crore will be used to fund long term working capital requirements
 - 150 crore towards expansion of manufacturing facilities in Himachal Pradesh and Gujarat
 - 150 crore for project site development, mostly by subsidiary IWISL
 - The rest of about 100 crore will be for General Corporate Purposes
- These objects appear to be reasonable and will grow the core business of wind power generation.

Introduction

- INOX is a part of the 12,000 crore Inox group which includes Gujarat Fluorochemicals, a manufacturer of refrigerants, Inox Leisure, the well known multiplex firm, and Inox Air Products, a manufacturer of Industrial gas. The group employs over 8000 people.
- INOX is in the business of Wind power generation, and it does mfg. of parts and sets up the entire wind powergen farm including the windmill/ tower, turbine and all parts on a turnkey basis.
- FY15 revenues till Decv31 2014 were Rs 1661 cr and Profits 19.8 cr.

- INOX Wind has its Head office in Noida near New Delhi. It has about 1400 employees on its rolls.
- It concentrates on two models of the 2 MegaWatt capacity generator model. The wind farms can have a number of such turbines. The technology is sourced and licensed from AMSC, Austria.

- It has manufacturing units in Una, Himachal Pradesh and Rohika, in Ahmedabad district of Gujarat.
- Its market share in the Indian Wind energy sector is estimated at 7-10%. It's the 5th largest player in FY14 in this sector. See Fig 1. Except Suzlon, the other major players operate in India as private subsidiaries, and so there are not many listed alternatives to INOX.
- **Fig 1 – Market shares of Wind Firms**



Quick review of Gujarat Flurochemicals and Inox Leisure

A look at the listed group companies of Gujarat Flurochemicals (GFL) and Inox Leisure (INOL) is below:



Fig 2 – Price history of GFL and Inox Leisure

- It's clear at a glance that GFL has rewarded shareholders with a 6X gain in 5 years, and dividend yield is 0.5%.
- INOL is also been quite positive with a 3X gain in 5 years, no dividend. Here we can say that this firm is investing in a consumer oriented brand, and has done quite well so far.

Financials of INOX

- While financials of INOX Fig 3 look good

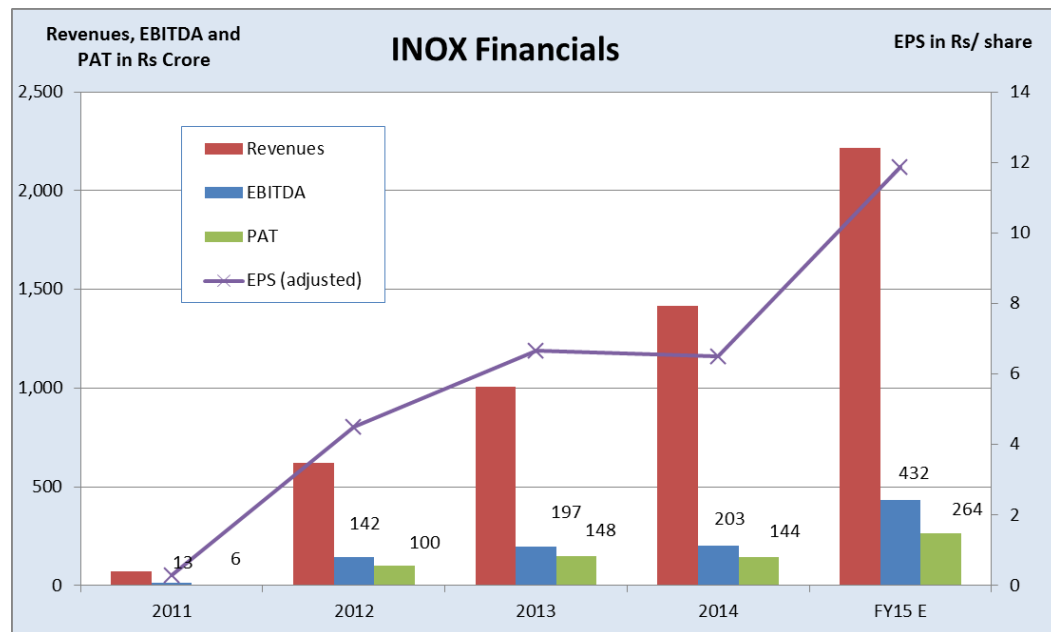


Fig 3 – Financials

- Here we have estimated FY15 financials simply based on the 9 month performance. Actual performance may differ especially since lots of revenues are booked in Q4 for such firms.
- The Cash flow is negative, see Fig 4, and debt is piling up

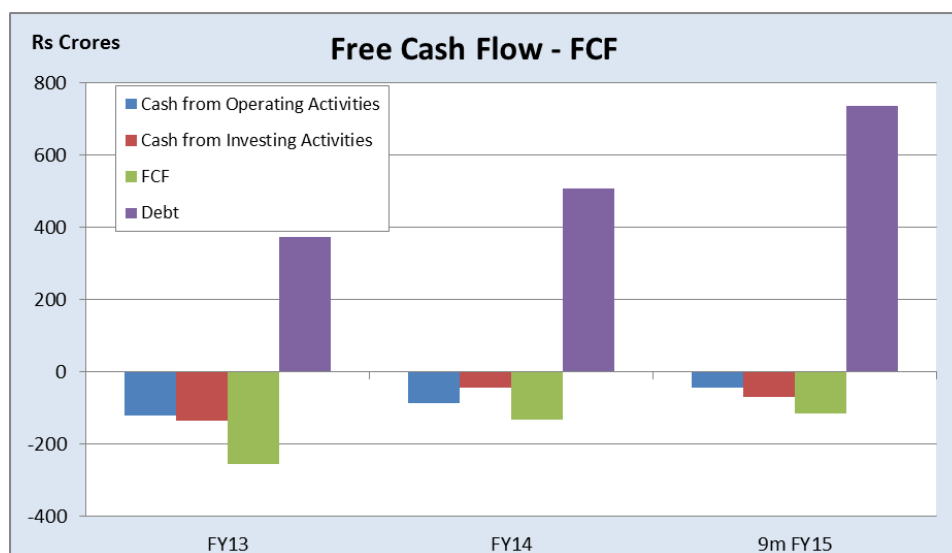


Fig 4 – Cash Flow

- The debt equity as per the INOX prospectus is 1.2 post IPO, however our feel is that debt is on a serious upward spiral and this is a negative.
- Valuations for INOX are at a P/E of 26.5-27.4 times estimated FY15 EPS. This is a bit high, but seeing the high growth of INOX, this may not be excessive. Plus there is a discount for retail.

Business Review

- INOX is in a sunrise industry in India – renewal power generation from wind energy.
- India has historically been power deficit, and there has been an 8-12% annual shortfall in power generated over the last 5 years.
- There is a governmental/ regulatory push towards renewable power like solar and wind in the past decade, and the wind power sector is supported with a series of benefits such as tax breaks, accelerated depreciation, 100% foreign direct investment, excise, customs duty and VAT concessions.
- In this environment INOX has in the last 5 years shown a remarkable emergence as a player in the wind power segment. It started by catering to internal/ group energy requirements (100% of revenues till FY12), and has then accelerated its commercial business and is in FY15 earning 100% revenues from external customers.
- Another factor helping renewables is that fossil fuels are polluting and non-sustainable. This environmental factor is pushing governments worldwide to strongly encourage renewables. Germany has taken a lead by in 2014 having the largest generation by renewables at 27% (but includes Hydro power). The current pollution problems in Chinese are an accelerator to the renewables policy path.
- The current customers include Green Infra, Continuum Wind Energy, Tata Power Renewable Energy, Welspun Energy, Bhilwara Energy, ReNew Power Ventures and Hero Future Energies.
- Technology Partnerships: INOX has a perpetual license from AMSC Austria GmbH (formerly Windtec GmbH), or AMSC, a wind energy technology firm, to manufacture 2 MW WTGs in India. They also have non-exclusive licenses from WINDnovation Engineering Solutions GmbH (based in Germany), or WINDnovation, for custom-made rotor blade sets.
- As per some reports, there exists good potential in India to tap wind energy and establish wind farms that can generate power. However the wind product needs to be able to tap low speed winds.

Strengths and Positives

- Emerging, high potential industry in India.
- Promoter group has a good reputation in other group companies of rewarding shareholders.
- Current revenues are almost entirely from external customers and commercial relationships.
- The Technology partnerships look good for their current business operations, and lets INOX focus on manufacture and sales.
- High growth 3 year history.
- Helpful regulatory / policy environment.

Weaknesses, Negatives and Challenges

- INOX has to show the ability to sustain its rapid growth in 3 years from an INOX group internal wind power supply department to a vibrant commercially successful wind power EPC player.
- The positive financials Fig 3 hide a spiraling debt and receivables challenges, seen in Fig 4 Cash Flow.
- The reality is that this is a high competition sector, and INOX has no option but to take on projects which require large working capital for their execution. The entire Power EPC sector such as NTPC, BGR Energy, NTPC, BHEL, L&T, and AIA Engg. are facing cash flow, execution and closure issues.
- Thus INOX needs to be able to access low cost capital to sustain costs, or even switch to an EPC model (rather than turnkey) where they can collect payments on installation. (On a similar note, the roads sector in India is moving back from Turnkey to EPC due to execution and toll challenges).
- Suzlon energy, the leader by capacity, revenues and brand is a well-known example in wind power sector of success, followed by ambition, aggressive acquisitions internationally, quality problems in manufacturing and decline in business. At today's prices, the Suzlon share is at 6% of its all-time in Jan 2008. It has destroyed a lot of shareholder value in the last 7 years.
- To grow successfully in the long run, INOX needs to stabilize its product technologies. It has to master the current technologies and be able to sustain in case a partner pulls the plug. So it has to invest in R&D. On a related note, the key tech partner AMSC Austria GmbH and American Superconductor Corporation, USA have financial difficulties that can affect INOX in future.

Overall Opinion

- INOX is certainly in the right sector, where we should see double digit growth for a decade. It also is an environmentally positive segment. The government is doing a lot to promote / subsidize it.
- The firm itself has scaled up well so far, and the promoter group is good. There is also a scarcity of paper in this sector.
- The challenge for this firm is to manage costs, cash flows and technology stability. It has to perhaps slow down growth in order to be a more financially feasible concern.
- As an investment, the INOX Wind IPO is rated medium risk, but a BUY, with a 2 year holding period.

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