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KSB Pumps – Long term buy

General - KSB Pumps is a global market leader in water / oil / any liquid transport business, by way of it's products like valves, pumps and allied equipment. It employs 13300 people worldwide. It caters to industries like water engineering, mining, energy, chemicals, petrochemicals, flammable and inflammable liquids and industrial processes. These valves and pumps are hardy and can withstand any pressure and temperature that the business requires. The pumps are also in use in diverse industries like fire fighting, irrigation, paper, air conditioning, municipal water supply, mine de-watering, sea water desalination, sugar plants, processed food plants, paper pulp, refineries, steam generation, sewage & effluent handling and pressure boosting. KSB valves are in use in the transport of gas, oil, chemicals, water and non aggressive media. The emphasis on expansion in activities like waste water management, oil and gas pipelines will see demand for the company's products picking up over the years.

Pedigree – the Company is of German origin, acclaimed leaders in precision engineering. It was incorporated in 1871. It was incorporated as KSB Pumps Ltd in India in 1960.

Investor perception – the Company is favoured by long term investors as it has a generous dividend paying philosophy and the last fiscal year on record with us 2008 (the co follows December year ending accounting) saw a 55 % dividend. For investor reaction to the share performance vis-à-vis the fundamentals, please refer to the technical analysis section below.

Forward guidance – the CY 2008 results have shown a robust increase in topline and bottom line growth. The same was inspite of the beginning of the world wide recessionary trends. Being a manufacturer of capital intensive products, the Company outllook has been cautious as expansion / modernisation plans of big ticket consumer industries like fertilizers, refineries and petrochemical companies are likely to be on hold. Exports had rise 250 % in 2008 but are likely to witness a temporary downturn, only to pick up in 2010 – 2011. The 9 monthly performance between Jan – Sep 2009 shows the topline and bottomline have remained more or less constant inspite of adverse business environment. The Company focused on lower value pumps and valves during these 9 months where margins were lower but the profitability was protected from year-on-year erosion. We view that as a positive indicator as both parameters are likely to rally once economic activity perks up in the coming year/s. Exports are likely to jump in the coming years too.

Stock category – value stock, long term investment. Small cap scrip.

Recommendation – buy on all declines for long term capital appreciation. We expect the dividend yield to remain < 2 %. Please refer to our fair disclosure below before buying the stock.

Fundamental highlights – the company has been a robust and consistent performer. From net profits of Rs 300 Mn in 2004, they stand at Rs 638 Mn in 2008 thereby logging a CAGR of 17 %. Retained earnings have grown from Rs 227 Mn in 2004 to Rs 535 Mn in 2008, logging a 19 % CAGR in the period. The EPS was Rs 37.19 in 2008 from Rs 17.61 in 2004, logging a CAGR of 16 %. The return on capital was 31 % and has never dipped below 26 % in the last 5 years. The Company has paid a minimum dividend of 40 % in the last 5 years. The BV stands at 167 as on Dec 2008 and the debt to equity is 0.11, current ratio is 1.95 on the same date.

Shareholding pattern (Dec 2009) - source : Nseindia.com

Promoters - Indian	26.26 %
Promoters – Overseas	40.54 %
Institutions	11.80 %
FII's	00.13 %
Corporate investors	05.20 %
Individual investors	15.10 %
NRI's	00.75 %
Directors relatives	00.09 %
Clearing members	00.12 %

It is apparent that 21.26 % of the paid up equity vests with individual and non-individual investors. On a low capital base of Rs 17.40 Crs, this stock is unlikely to see major share holding changes anytime soon.

Our estimates – fair price to buy the stock is around Rs 360, which is a theoretical ideal level. The markets may choose to over / under discount the price as per prevailing sentiments. Therefore some room for averaging must be always maintained, to exploit opportunities in case of market declines. The ideal PBV is around 4 - 4.5 times (Rs 700) over the long term.

Unique selling proposition (USP) – German MNC co. with a strong growth record and a minimum dividend payout ratio of atleast 12 % of it's net profits in the last 5 years. The 2008 dividend payout was 15 % of net profits. The more the authorities emphasise on gas / oil / water transport, treatment or desalination, the more this Company will gain in sales and profits. The Company seems to be growing inspite of the higher base effect of the net profits, which is a rare achievement. The high pressure valve range is being expanded from 12" to 24" and new age condensate extraction pumps – a first in the Country, for use in UMPP's (Ultra Mega Power Plants). The Company is enhancing the capacity of it's sewage pumps from 65 Kw to 165 Kw. This is to garner a higher market share in the ballooning water / sewage treatment business in the Country. The CAGR growth of 18 % in net profits over the last half a decade imbibes bullish confidence in us and enables us to project a market out performer view on this counter for long term investors.

In it's guidance, the management has opined that cheaper imports, especially from China were not expected to adversely impact it's dominant market position due to the customer loyalty, durability of it's products and dependable after sales service.

Technicals – the weekly chart of the stock indicates a few interesting aspects – a) the stock is relatively illiquid as a few thousand shares are traded daily b) the price / volume activity shows concerted buying since July 09 from the 360 levels, which should now be a de facto support area to watch in case of a decline and c) a breakout past the 470 levels will be needed to trigger a fresh upthrust. The relative strength comparative is higher than the Nifty at 148 (where 100 = base), making this stock a market out-performer. The 52 week SMA has turned upwards and will act as a meaningful support on declines which too happens to be at the 360 levels. Fundamental analysis indicates the 360 mark as a “fair value” buy point. All in all, a long term buy on all dips in small lots. Take a 36 month view and invest for long term capital appreciation.

Your call of action – risk takers may buy the stock at current levels for long term delivery investments. However, room for averaging must be maintained to arrive at a lower average acquisition cost. Patient investors may await for dips to the 375 levels and then commence buying. All bullish bets are off below 300 and we expect to book profits past the 700 – 750 band in 36 months or so.

Fair disclosure – the analyst, his family and corporate holding company have investment exposure to this stock and therefore have a vested interest in this buy recommendation. Please do your due diligence before investing. Disclaimers apply.

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