

**BUY**

TP: Rs 560 | ▲ 24%

**FINOLEX INDUSTRIES**

Plastic Products

10 August 2020

## Tough quarter but outlook healthy; raise to BUY on low valuations

Finolex Industries' (FNPX) Q1 revenue declined 40% YoY, with volumes sliding 42% in both PVC pipe and resin segments amid the lockdown. EBITDA margins expanded 260bps YoY to 15.7% on higher gross margins and lower other expense. EBITDA/PAT contracted 29%/39% YoY. Management indicated strong demand for agri pipes in Q1 and a gradual pick-up in the non-agri segment too. We raise FY21 earnings by 4% (FY22 unchanged) and roll over to a new Sep'21 TP of Rs 560 (vs. Rs 545). Upgrade from ADD to BUY on reasonable valuations.

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**Lockdown hurts volumes:** FNPX's Q1FY21 standalone revenue dropped 42% YoY to Rs 5.6bn. The PVC resin segment declined 45% YoY with volumes/realisations slipping 42%/5%. PVC pipes & fittings revenue also fell 40% YoY, with volumes down 42% whereas realisations increased 3%. Management stated that agricultural pipe volumes could have been better but for logistical/production issues due to the lockdown. June saw 85% of year-ago volumes and July 96%. FNPX expects agri pipe segment (~70% of total volumes in FY20) to be flat YoY in FY21.

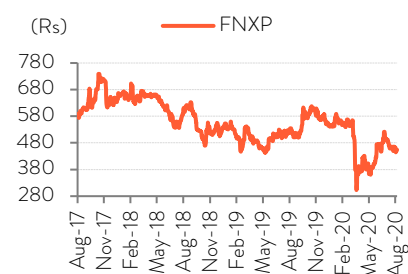
**Margins increase:** Operating margins increased by 260bps YoY on higher gross margins (+260bps) and lower other expense (-243bps), partly offset by higher employee cost (+243bps). EBITDA/PBT declined 28%/33% YoY. Gross margins expanded due to better realisations whereas other expenses declined on the back of cost control initiatives. Management stated that PVC prices have increased nearer to pre-Covid levels and hence should not be a drag on margins.

**Valuations reasonable – upgrade to BUY:** We increase PAT estimates for FY21 by 4% (FY22 unchanged) and roll forward to a revised Sep'21 TP of Rs 560 (earlier Rs 545), based on an unchanged 20x one-year forward P/E. Upgrade to BUY as current valuations look reasonable at 16.8x FY22E.

Ticker/Price	FNPX IN/Rs 453
Market cap	US\$ 751.0mn
Shares o/s	124mn
3M ADV	US\$ 0.3mn
52wk high/low	Rs 627/Rs 290
Promoter/FPI/DII	52%/2%/45%

Source: NSE

## STOCK PERFORMANCE



Source: NSE

## KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20P	FY21E	FY22E	FY23E
Total revenue (Rs mn)	30,913	29,860	28,490	30,992	33,397
EBITDA (Rs mn)	6,043	4,481	4,630	4,755	5,046
Adj. net profit (Rs mn)	3,857	3,327	3,207	3,349	3,611
Adj. EPS (Rs)	31.1	26.8	25.8	27.0	29.1
Adj. EPS growth (%)	28.9	(13.8)	(3.6)	4.4	7.8
Adj. ROAE (%)	14.4	14.6	15.5	14.9	14.8
Adj. P/E (x)	14.6	16.9	17.5	16.8	15.6
EV/EBITDA (x)	9.4	12.4	12.0	11.7	10.6

Source: Company, BOBCAPS Research

**BOB Capital Markets Ltd is a wholly owned subsidiary of Bank of Baroda**

Important disclosures, including any required research certifications, are provided at the end of this report.



**FIG 1 – STANDALONE QUARTERLY PERFORMANCE**

(Rs mn)	Q1FY21	Q1FY20	YoY (%)	Q4FY20	QoQ (%)
<b>Net sales</b>	<b>5,621</b>	<b>9,438</b>	<b>(40.4)</b>	<b>7,661</b>	<b>(26.6)</b>
COGS	3,826	6,668	(42.6)	5,009	(23.6)
Employee expenses	346	354	(2.1)	408	(15.1)
Other expenses	567	1,181	(52.0)	1,203	(52.9)
<b>EBITDA</b>	<b>882</b>	<b>1,236</b>	<b>(28.6)</b>	<b>1,041</b>	<b>(15.2)</b>
EBITDA margin (%)	15.7	13.1	261bps	13.6	211bps
Depreciation & amortisation	188	168	12.3	189	(0.3)
<b>EBIT</b>	<b>694</b>	<b>1,068</b>	<b>(35.0)</b>	<b>852</b>	<b>(18.5)</b>
EBIT margin (%)	12.3	11.3	104bps	11.1	123bps
Other income	83	57	46.0	10	749.0
Finance costs	33	9	277.0	90	(63.7)
<b>Profit before tax</b>	<b>745</b>	<b>1,116</b>	<b>(33.3)</b>	<b>771</b>	<b>(3.5)</b>
Tax expenses	193	391	(50.6)	214	(9.8)
<b>Reported Net profit</b>	<b>551</b>	<b>725</b>	<b>(24.0)</b>	<b>557</b>	<b>(1.1)</b>

Source: Company, BOBCAPS Research

**FIG 2 – STANDALONE SEGMENTAL PERFORMANCE**

(Rs mn)	Q1FY21	Q1FY20	YoY (%)	Q4FY20	QoQ (%)
<b>Revenue</b>					
PVC	2,943	5,349	(45.0)	4,336	(32.1)
PVC pipes & fittings	5,070	8,512	(40.4)	6,322	(19.8)
Total	8,013	13,861	(42.2)	10,658	(24.8)
Inter-segment revenues	2,392	4,423	(45.9)	2,996.7	(20.2)
<b>Net sales (inc. other op. inc.)</b>	<b>5,621</b>	<b>9,438</b>	<b>(40.4)</b>	<b>7,661</b>	<b>(26.6)</b>
<b>EBIT</b>					
PVC	232	413	(43.8)	315.3	(26.4)
PVC pipes & fittings	514	724	(28.9)	629.1	(18.2)
<b>Total</b>	<b>747</b>	<b>1,137</b>	<b>(34.3)</b>	<b>944</b>	<b>(21.0)</b>
<b>EBIT MARGINS</b>					
PVC	7.9	7.7	16bps	7.3	62bps
PVC pipes & fittings	10.1	8.5	165bps	10.0	20bps
<b>Total</b>	<b>13.3</b>	<b>12.0</b>	<b>124bps</b>	<b>12.3</b>	<b>95bps</b>

Source: Company, BOBCAPS Research

**FIG 3 – CONSOLIDATED QUARTERLY PERFORMANCE**

(Rs mn)	Q1FY21	Q1FY20	YoY (%)	Q4FY20	QoQ (%)
<b>Net sales</b>	<b>5,621</b>	<b>9,438</b>	<b>(40.4)</b>	<b>7,661</b>	<b>(26.6)</b>
COGS	3,826	6,668	(42.6)	5,009	(23.6)
Employee expenses	346	354	(2.1)	408	(15.1)
Other expenses	567	1,181	(52.0)	1,203	(52.9)
<b>EBITDA</b>	<b>882</b>	<b>1,236</b>	<b>(28.6)</b>	<b>1,041</b>	<b>(15.2)</b>
EBITDA margin (%)	15.7	13.1	261bps	13.6	211bps
Depreciation & amortisation	188	168	12.3	189	(0.3)
<b>EBIT</b>	<b>694</b>	<b>1,068</b>	<b>(35.0)</b>	<b>852</b>	<b>(18.5)</b>
EBIT margin (%)	12.3	11.3	104bps	11.1	123bps
Other income	83	57	46.0	10	749.0
Finance costs	33	9	277.0	90	(63.7)
<b>Profit before tax</b>	<b>745</b>	<b>1,116</b>	<b>(33.3)</b>	<b>771</b>	<b>(3.5)</b>
Tax expenses	206	403	(48.8)	301	(31.4)
Share of profit from associates	29	19	56.2	116	(75.1)
<b>Reported Net profit</b>	<b>567</b>	<b>732</b>	<b>(22.5)</b>	<b>587</b>	<b>(3.3)</b>

Source: Company, BOBCAPS Research

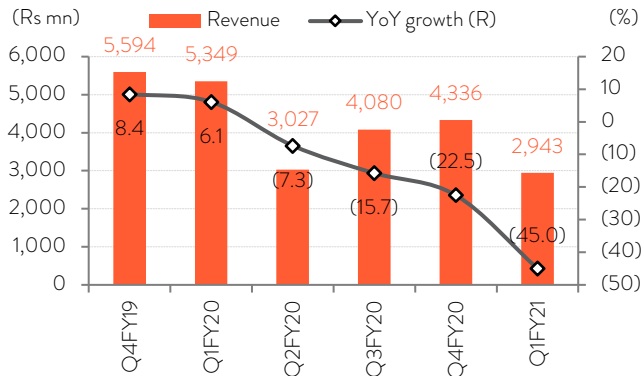
**FIG 4 – VOLUME AND REALISATION TRENDS**

Particulars	Q1FY21	Q1FY20	YoY (%)	Q4FY20	QoQ (%)
<b>Volume</b>					
PVC (MT)	45,435	78,512	(42.1)	60,100	(24.4)
PVC pipes (MT)	52,911	91,655	(42.3)	62,464	(15.3)
<b>Realisation</b>					
PVC (Rs/t)	64,769	68,128	(4.9)	72,146	(10.2)
PVC pipes (Rs/t)	95,818	92,871	3.2	1,01,209	(5.3)
<b>EBIT/tonne</b>					
PVC (Rs/t)	5,108	5,262	(2.9)	5,246	(2.6)
PVC pipes (Rs/t)	9,722	7,895	23.1	10,071	(3.5)

Source: Company, BOBCAPS Research

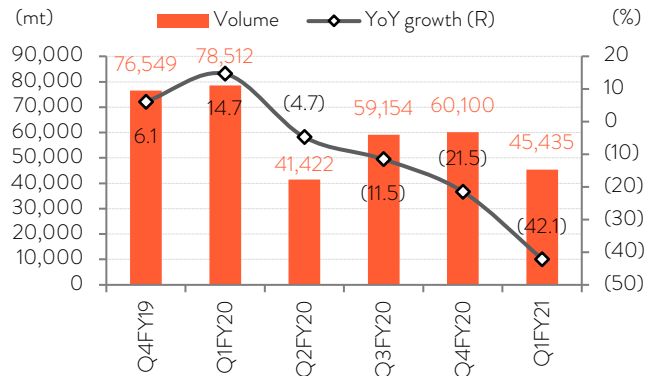
STANDALONE QUARTERLY TRENDS

FIG 5 – PVC RESIN REVENUE GROWTH



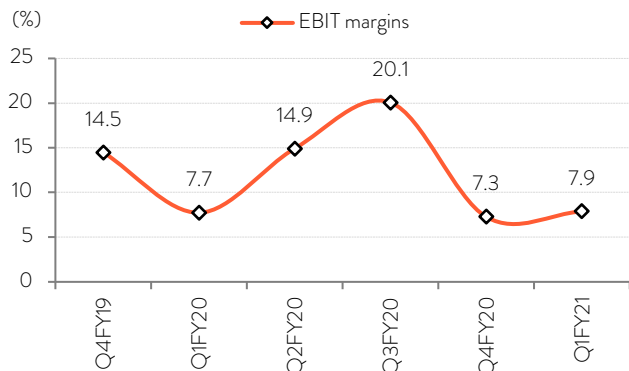
Source: Company, BOBCAPS Research

FIG 6 – PVC RESIN VOLUME GROWTH



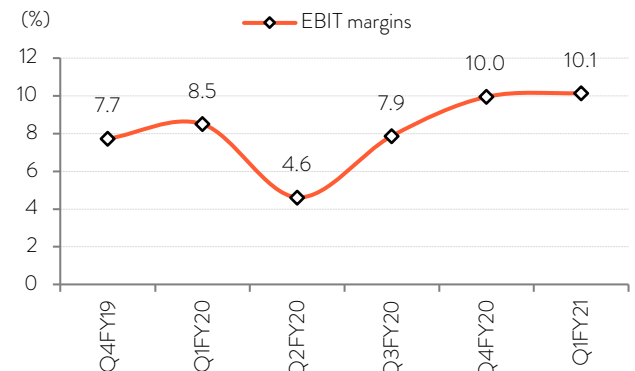
Source: Company, BOBCAPS Research

FIG 7 – PVC RESIN EBIT MARGINS



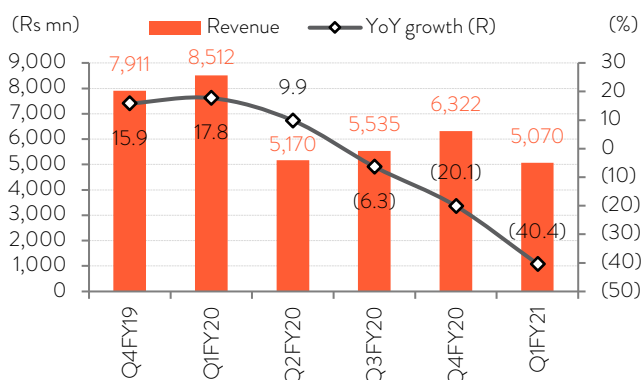
Source: Company, BOBCAPS Research

FIG 8 – PVC PIPES & FITTINGS EBIT MARGINS



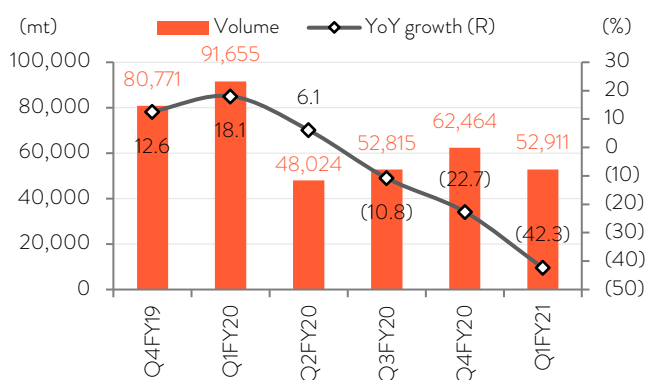
Source: Company, BOBCAPS Research

FIG 9 – PVC PIPES & FITTINGS REVENUE GROWTH



Source: Company, BOBCAPS Research

FIG 10 – PVC PIPES & FITTINGS VOLUME GROWTH



Source: Company, BOBCAPS Research

FIG 11 – PVC-EDC DELTA

PVC/EDC Spread	Q4FY19	Q1FY20	Q2FY20	Q3FY20	Q4FY20	Q1FY21
Spread (US\$/mt)	523	490	583	589	574	547
YoY (%)	(33.4)	(28.8)	(9.0)	10.1	9.8	11.6

Source: Company, BOBCAPS Research

## Earnings call highlights

- FNXP's Q1FY21 performance was adversely affected by the lockdown which coincided with the peak season for agricultural pipe sales (March to June). The company earns ~70% of revenues from the agri pipe sector and the balance from the non-agriculture sector.
- Demand for agricultural pipes did pick up in May and June as the lockdown eased. The month of May saw 25% of year-ago volumes, which rose to 85% in June and 96% in July.
- Agri pipe offtake has come down following onset of monsoon which is part of the seasonal trend. At the same time, non-agri pipes have shown some demand traction in July with the return of migrant labourers.
- Management anticipates robust demand for agricultural pipes going ahead and expects to maintain FY20 volumes levels this year as well despite the decline in Q1. The outlook on non-agri pipes remains unclear, though management is hopeful of flattish growth here too.
- The PVC-EDC delta in the quarter was US\$ 547/mt (vs. US\$ 490/mt YoY).
- Despite price declines in PVC resin, the company did not take price cuts in the PVC pipe segment during Q1 as demand was strong and availability was limited due to production issues. This resulted in better segmental margins.
- PVC resin prices are now near pre-Covid levels which should cushion the company from high-cost inventory carried over from FY20.
- FNXP has been giving 30 days of credit in non-agri pipes for the last year-and-a-half and continues with cash & carry policy in the agri segment.
- The company aims to increase non-agri pipe segment revenues from 30% of turnover to 40% over the next three years.

### Valuation methodology

FNXP is one of the major PVC pipe players in India with 18,000 dealers and sub-dealers spread across the country. The company has a strong presence in the agricultural pipe market and plans to build a significant footprint in the plumbing market following its recent foray into CPVC pipes.

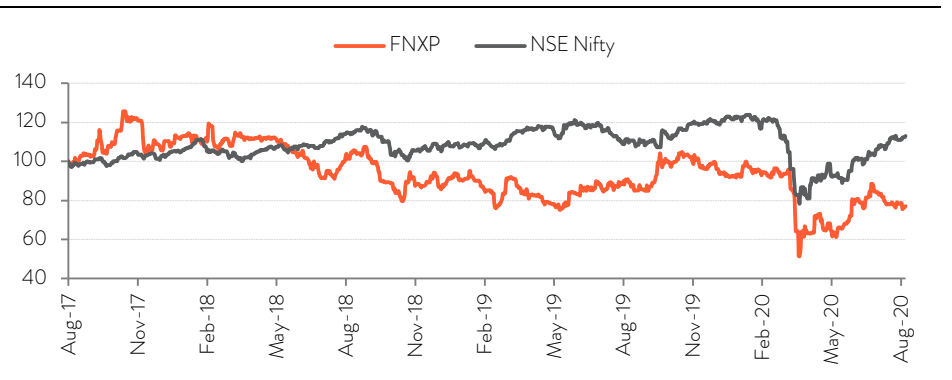
Post Q1, we increase our FY21 PAT estimate by 4% (unchanged for FY22) and roll over to a revised Sep'21 TP of Rs 560 (earlier Rs 545), based on an unchanged 20x one-year forward P/E multiple. We upgrade our rating from ADD to BUY as the stock has corrected ~10% following our downgrade on 24 June, thus rendering valuations reasonable and the upside attractive.

**FIG 12 – REVISED ESTIMATES**

(Rs mn)	New		Old		YoY (%)	
	FY21E	FY22E	FY21E	FY22E	FY21E	FY22E
Revenue	28,490	30,992	26,456	31,225	7.7	(0.7)
EBITDA	4,630	4,755	4,403	4,754	5.2	0.0
PAT	3,207	3,349	3,075	3,358	4.3	(0.3)

Source: BOBCAPS Research

**FIG 13 – RELATIVE STOCK PERFORMANCE**



Source: NSE

### Key risks

Key downside risks to our estimates are:

- volatility in PVC-EDC spreads,
- slowdown in agricultural/housing markets, and
- increased competition from unorganised players, leading to lower profitability.

## FINANCIALS

### Income Statement

Y/E 31 Mar (Rs mn)	FY19A	FY20P	FY21E	FY22E	FY23E
<b>Total revenue</b>	<b>30,913</b>	<b>29,860</b>	<b>28,490</b>	<b>30,992</b>	<b>33,397</b>
EBITDA	6,043	4,481	4,630	4,755	5,046
Depreciation	(701)	(738)	(826)	(790)	(852)
EBIT	5,342	3,743	3,804	3,965	4,194
Net interest income/(expenses)	(123)	(119)	(113)	(58)	(44)
Other income/(expenses)	404	299	200	289	344
Exceptional items	0	0	0	0	0
EBT	5,624	3,923	3,891	4,196	4,494
Income taxes	(1,812)	(852)	(904)	(1,116)	(1,204)
Extraordinary items	(279)	0	0	0	0
Min. int./Inc. from associates	140	256	220	270	320
<b>Reported net profit</b>	<b>3,672</b>	<b>3,327</b>	<b>3,207</b>	<b>3,349</b>	<b>3,611</b>
Adjustments	184	0	0	0	0
<b>Adjusted net profit</b>	<b>3,857</b>	<b>3,327</b>	<b>3,207</b>	<b>3,349</b>	<b>3,611</b>

### Balance Sheet

Y/E 31 Mar (Rs mn)	FY19A	FY20P	FY21E	FY22E	FY23E
Accounts payables	2,838	2,334	2,190	2,483	2,685
Other current liabilities	1,387	1,723	1,249	1,359	1,464
Provisions	230	297	234	340	366
Debt funds	906	2,827	927	727	527
Other liabilities	2,205	1,873	1,763	1,653	1,543
Equity capital	1,241	1,241	1,241	1,241	1,241
Reserves & surplus	24,521	18,619	20,382	22,225	24,211
Shareholders' fund	25,762	19,860	21,623	23,466	25,451
<b>Total liabilities and equities</b>	<b>33,327</b>	<b>28,913</b>	<b>27,986</b>	<b>30,026</b>	<b>32,036</b>
Cash and cash eq.	291	932	1,096	2,310	2,681
Accounts receivables	743	732	781	849	915
Inventories	6,205	8,578	7,130	6,715	7,262
Other current assets	1,035	710	937	1,019	1,098
Investments	13,619	5,772	6,272	6,472	7,172
Net fixed assets	9,489	10,988	10,662	11,372	11,520
CWIP	902	73	0	0	0
Intangible assets	20	16	16	16	16
Other assets	1,023	1,113	1,093	1,274	1,372
<b>Total assets</b>	<b>33,327</b>	<b>28,913</b>	<b>27,986</b>	<b>30,026</b>	<b>32,036</b>

Source: Company, BOBCAPS Research

**Cash Flows**

Y/E 31 Mar (Rs mn)	FY19A	FY20P	FY21E	FY22E	FY23E
Net income + Depreciation	6,045	4,661	4,717	4,986	5,346
Interest expenses	123	119	113	58	44
Non-cash adjustments	0	0	0	0	0
Changes in working capital	(209)	(2,295)	574	486	(483)
Other operating cash flows	(2,425)	(1,428)	(1,105)	(1,405)	(1,548)
<b>Cash flow from operations</b>	<b>3,535</b>	<b>1,057</b>	<b>4,300</b>	<b>4,125</b>	<b>3,359</b>
Capital expenditures	(1,366)	(603)	(427)	(1,500)	(1,000)
Change in investments	0	0	0	0	0
Other investing cash flows	(1,605)	942	(500)	(200)	(700)
<b>Cash flow from investing</b>	<b>(2,971)</b>	<b>340</b>	<b>(927)</b>	<b>(1,700)</b>	<b>(1,700)</b>
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	(101)	1,921	(1,900)	(200)	(200)
Interest expenses	(123)	(119)	(113)	(58)	(44)
Dividends paid	(1,532)	(2,873)	(1,443)	(1,507)	(1,625)
Other financing cash flows	1,416	315	247	554	580
<b>Cash flow from financing</b>	<b>(340)</b>	<b>(756)</b>	<b>(3,209)</b>	<b>(1,211)</b>	<b>(1,288)</b>
<b>Changes in cash and cash eq.</b>	<b>223</b>	<b>641</b>	<b>164</b>	<b>1,214</b>	<b>371</b>
<b>Closing cash and cash eq.</b>	<b>291</b>	<b>932</b>	<b>1,096</b>	<b>2,310</b>	<b>2,681</b>

**Per Share**

Y/E 31 Mar (Rs)	FY19A	FY20P	FY21E	FY22E	FY23E
Reported EPS	29.6	26.8	25.8	27.0	29.1
Adjusted EPS	31.1	26.8	25.8	27.0	29.1
Dividend per share	10.0	10.0	9.3	9.7	10.5
Book value per share	207.6	160.0	174.2	189.1	205.1

**Valuations Ratios**

Y/E 31 Mar (x)	FY19A	FY20P	FY21E	FY22E	FY23E
EV/Sales	1.8	1.9	2.0	1.8	1.6
EV/EBITDA	9.4	12.4	12.0	11.7	10.6
Adjusted P/E	14.6	16.9	17.5	16.8	15.6
P/BV	2.2	2.8	2.6	2.4	2.2

**DuPont Analysis**

Y/E 31 Mar (%)	FY19A	FY20P	FY21E	FY22E	FY23E
Tax burden (Net profit/PBT)	68.6	84.8	82.4	79.8	80.3
Interest burden (PBT/EBIT)	105.3	104.8	102.3	105.8	107.2
EBIT margin (EBIT/Revenue)	17.3	12.5	13.4	12.8	12.6
Asset turnover (Revenue/Avg TA)	90.4	95.9	100.1	106.8	107.6
Leverage (Avg TA/Avg Equity)	1.3	1.4	1.4	1.3	1.3
Adjusted ROAE	14.4	14.6	15.5	14.9	14.8

Source: Company, BOBCAPS Research | Note: TA = Total Assets



**Ratio Analysis**

Y/E 31 Mar	FY19A	FY20P	FY21E	FY22E	FY23E
<b>YoY growth (%)</b>					
Revenue	12.9	(3.4)	(4.6)	8.8	7.8
EBITDA	24.9	(25.9)	3.3	2.7	6.1
Adjusted EPS	28.9	(13.8)	(3.6)	4.4	7.8
<b>Profitability &amp; Return ratios (%)</b>					
EBITDA margin	19.5	15.0	16.3	15.3	15.1
EBIT margin	17.3	12.5	13.4	12.8	12.6
Adjusted profit margin	12.5	11.1	11.3	10.8	10.8
Adjusted ROAE	14.4	14.6	15.5	14.9	14.8
ROCE	19.2	15.2	16.8	17.0	16.7
<b>Working capital days (days)</b>					
Receivables	7	9	10	10	10
Inventory	117	139	154	123	115
Payables	39	37	35	33	33
<b>Ratios (x)</b>					
Gross asset turnover	1.4	1.3	1.2	1.2	1.2
Current ratio	1.5	1.5	2.2	2.2	2.4
Net interest coverage ratio	43.5	31.4	33.8	68.5	95.6
Adjusted debt/equity	0.0	0.1	0.0	(0.1)	(0.1)

Source: Company, BOBCAPS Research

## Disclaimer

### Recommendations and Absolute returns (%) over 12 months

**BUY** – Expected return >+15%

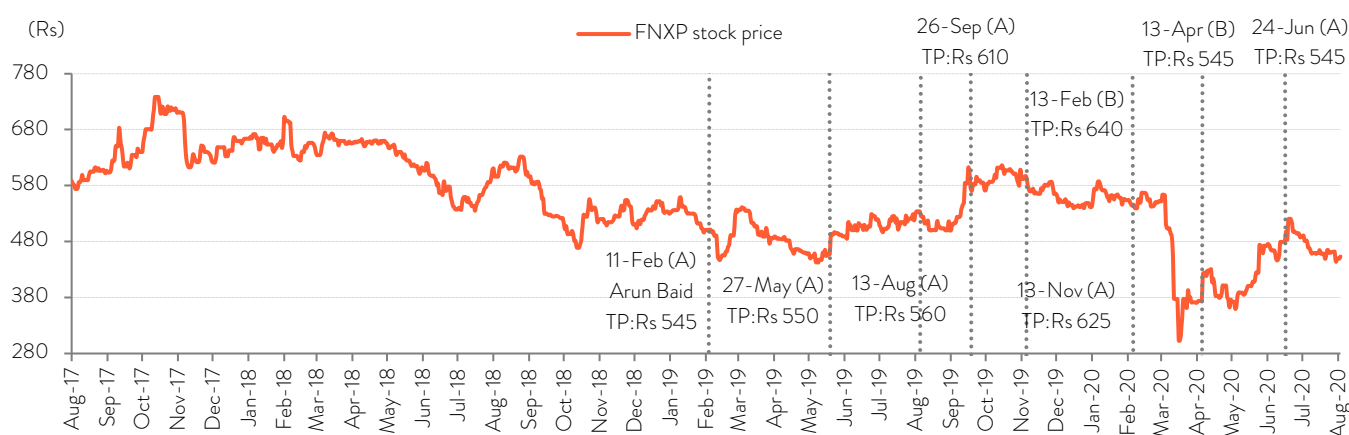
**ADD** – Expected return from >+5% to +15%

**REDUCE** – Expected return from -5% to +5%

**SELL** – Expected return <-5%

**Note:** Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

### RATINGS AND TARGET PRICE (3-YEAR HISTORY): FINOLEX INDUSTRIES (FNPX IN)



B – Buy, A – Add, R – Reduce, S – Sell

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