

HOLD

TP: Rs 230 | ▼ 1%

FINOLEX INDUSTRIES

Building Materials

19 January 2024

Weak quarter on slow recovery in agri pipe demand

- Missed our Q3 EBITDA estimate by 16% on slow recovery in agri pipe demand
- Positive plastic pipe demand outlook on affordable resin prices and rising share of non-agri pipes in the mix
- Maintain HOLD on limited growth prospects and weak return ratios; TP unchanged at Rs 230

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Weak quarter: FNXP missed our revenue/EBITDA/adj. PAT estimates for Q3FY24 by 17%/16%/11% due to lower-than-expected pipe volumes (-10% YoY vs. our estimate of +5%), as agricultural pipes saw slow demand and a high base (+92% YoY in Q3FY23). Overall, FNXP's revenue declined 9% YoY whereas EBITDA/adj. PAT grew 30%/24% YoY owing to a low base (on account of MTM inventory loss). Net cash balance has improved slightly from Rs 15bn in Sep'23 to Rs 15.7bn in Dec'23.

Key result highlights: FNXP's pipe volumes fell 10% YoY but grew at a healthy 11.4% on a 4Y CAGR basis in Q3FY24. Despite lower volumes, pipe segment EBITDA grew 10% YoY in Q3 as pipe EBITDA per unit rose 23% YoY to Rs 10.7/kg, surpassing the pre-Covid range of Rs 7-9/kg due to a rising share of non-agri pipes in the mix. PVC resin segment EBITDA climbed 47% QoQ due to a 26% QoQ rise in segment EBITDA per unit to Rs 7.6/kg, albeit still well below the historical average of Rs 15/kg. Management believes PVC resin prices are likely to remain range bound and affordable, which would drive demand for plastic pipes.

Maintain HOLD: We maintain our TP of Rs 230 and HOLD rating on the stock due to the company's limited growth prospects (EPS estimated to log a slow 9% CAGR over FY19-FY26) and weak return ratio profile amidst poor capital allocation. We cut our EPS estimates by 18% for FY24 due to the weak third-quarter results, but largely maintain our forecasts for FY25/FY26. At CMP, the stock trades at 24.3x one-year forward P/E. Our target P/E multiple remains unchanged at 22x on Sep'25E EPS, a 10% premium to the stock's 5Y average to account for an improving risk profile.

Key changes

Target	Rating
◀ ▶	◀ ▶

Ticker/Price	FNXP IN/Rs 231
Market cap	US\$ 1.7bn
Free float	47%
3M ADV	US\$ 3.1mn
52wk high/low	Rs 260/Rs 158
Promoter/FPI/DII	52%/7%/12%

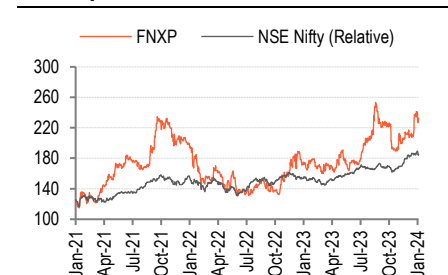
Source: NSE | Price as of 19 Jan 2024

Key financials

Y/E 31 Mar	FY23A	FY24E	FY25E
Total revenue (Rs mn)	43,971	41,747	45,236
EBITDA (Rs mn)	3,258	4,679	8,200
Adj. net profit (Rs mn)	2,604	3,736	6,276
Adj. EPS (Rs)	4.2	6.0	10.1
Consensus EPS (Rs)	4.2	8.0	9.9
Adj. ROAE (%)	5.9	7.5	11.8
Adj. P/E (x)	54.9	38.3	22.8
EV/EBITDA (x)	47.7	33.9	19.3
Adj. EPS growth (%)	(65.9)	43.5	68.0

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE



Fig 1 – Quarterly performance – Consolidated

(Rs mn)	Q3FY24	Q3FY23	YoY (%)	Q2FY24	QoQ (%)	9MFY24	9MFY23	YoY (%)
Revenue	10,197	11,248	(9.3)	8,832	15.5	30,820	32,557	(5.3)
RM	6,522	7,602	(14.2)	5,306	22.9	19,633	24,129	(18.6)
Gross Profit	3,675	3,646	0.8	3,526	4.2	11,187	8,428	32.7
Employee	526	484	8.7	503	4.6	1,547	1,417	9.2
Others	1,950	2,243	(13.1)	1,993	(2.2)	5,887	6,260	(6.0)
EBITDA	1,199	919	30.5	1,030	16.4	3,754	751	399.7
D&A	276	225	22.5	274	0.7	893	654	36.6
EBIT	923	694	33.1	756	22.1	2,860	97	2845.5
Interest cost	77	51	49.3	125	(38.5)	291	208	40.3
Int. & other income	468	407	15.1	702	(33.3)	1,649	1,025	60.8
PBT	1,315	1,049	25.3	1,334	(1.4)	4,217	915	361.1
Tax	361	254	42.3	354	2.0	1,131	81	1297.4
PAT	954	795	19.9	980	(2.6)	3,087	834	270.2
Adj. PAT	948	761	24.5	980	(3.2)	3,081	664	363.8
As % of net revenues			(bps)		(bps)			(bps)
Gross margin	36.0	32.4	363	39.9	(389)	36.3	25.9	1,041
Employee	5.2	4.3	86	5.7	(54)	5.0	4.4	67
Others	19.1	19.9	(82)	22.6	(345)	19.1	19.2	(13)
EBITDA margin	11.8	8.2	359	11.7	10	12.2	2.3	987
Tax rate	27.5	24.2	327	26.5	91	26.8	8.8	1,796
APAT margin	9.3	6.8	253	11.1	(180)	10.0	2.0	796

Source: Company, BOBCAPS Research

Fig 2 – Segment financials

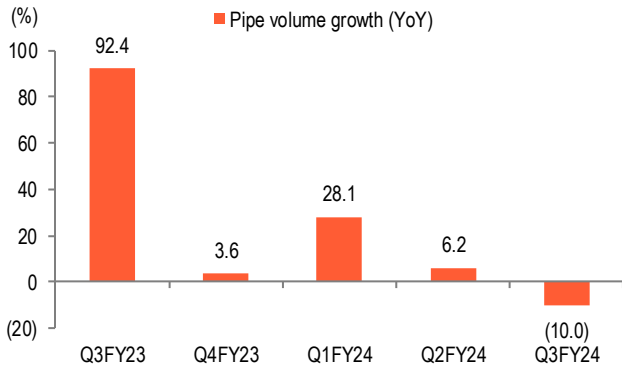
Particulars	Q3FY24	Q3FY23	YoY (%)	Q2FY24	QoQ (%)	9MFY24	9MFY23	YoY (%)
Revenue (Rs mn)								
External PVC Resin	281	476	(41.0)	260	8.0	790	2,448	(67.7)
Pipes & Fittings	9,916	10,772	(7.9)	8,572	15.7	30,030	30,109	(0.3)
Sales Volume (KT)								
External PVC Resin	3	5	(43.3)	3	8.4	8	24	(67.0)
Pipes & Fittings	81	90	(10.0)	63	29.2	236	222	6.7
Average Realization (Rs/kg)								
External PVC Resin	102	98	4.0	102	(0.3)	102	104	(2.2)
Pipes & Fittings	122	119	2.3	136	(10.5)	127	136	(6.5)
Adjusted EBITDA (Rs/kg)								
PVC resin	7.6	2.1	265.8	6.0	26.2	4.9	(1.2)	NM
Pipes & Fittings	10.7	8.7	22.9	12.8	(16.6)	13.3	4.4	203.1

Source: Company, BOBCAPS Research

Earning call highlights

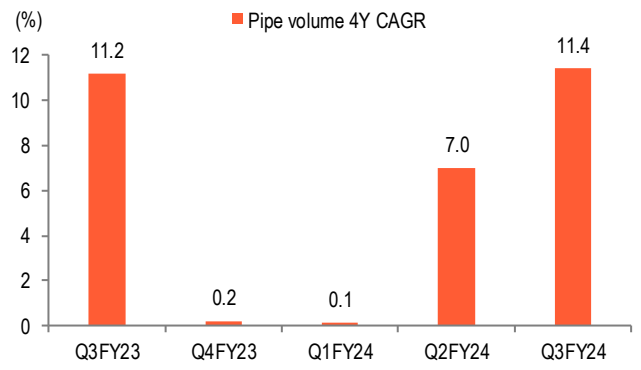
- **PVC resin:** Global PVC resin prices are currently trading ~US\$ 750/t and FNXP expects a range of US\$ 750-850/t in the near term. The company's PVC resin operations were affected in Q3FY24 as one of its raw materials suppliers declared force majeure. However, management expects resin production to return to normal from Q4FY24 onwards.
- **Pipe industry demand:** FNXP saw weak demand for agricultural pipes due to declining PVC resin prices, but non-agri pipe volumes grew at a healthy double-digit rate in Q3FY24 led by an increase in construction activity. Going ahead, the company expects the non-agri pipe industry to grow at >15% due to the pick-up in real estate activity and believes agri pipe demand will also gather pace.
- **Channel inventory:** Restocking of channel inventories is expected once PVC resin prices start to harden.
- **Pipe volume outlook:** The company expects its agri pipe portfolio to grow in single digits and non-agri pipe portfolio to grow at 15-20% in coming quarters.
- **Pipe volume mix:** Non-agri pipe volume share has gone up 500bps YoY to 32% in Q3FY24.
- **Margin outlook:** FNXP maintained guidance of pipe EBIT per unit in the range of Rs 10-12/kg in the near term and sees further improvement with a rising share of plumbing pipes over the long term.
- **Strategy:** The company has no plans to incur major capex in the PVC resin segment and plans to focus on growth in its existing pipe product portfolio. Management is evaluating plans to set up a new pipe manufacturing facility over the next two years to cater to future growth requirements.
- **Capital allocation:** FNXP plans to divest a 35-acre non-core land parcel in Pune which is valued ~Rs 3.8bn and would distribute the surplus cash to shareholders in the form of dividend or buyback in future.
- **MTM inventory loss:** The company has booked an MTM inventory loss in Q3 due to a steep decline in PVC resin prices in the month of Oct'23.

Fig 3 – FNXP’s pipe volumes fell 10% YoY in Q3FY24 on slow recovery in agri pipes and a high base effect...



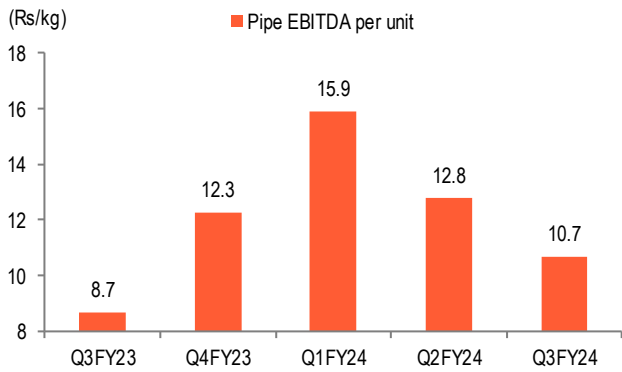
Source: Company, BOBCAPS Research

Fig 4 – ...but grew at a healthy 11.4% rate on a 4Y CAGR basis



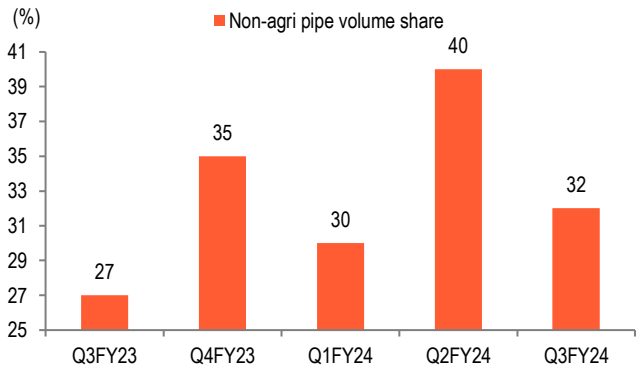
Source: Company, BOBCAPS Research

Fig 5 – Pipe EBITDA per unit improved by 23% YoY to Rs 10.7/kg...



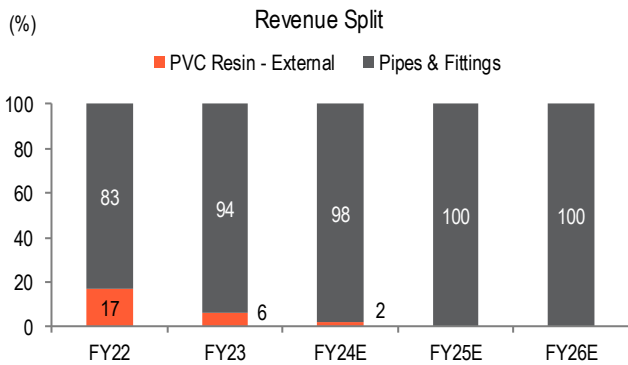
Source: Company, BOBCAPS Research

Fig 6 – ...on a rising share of non-agri pipes in total volumes



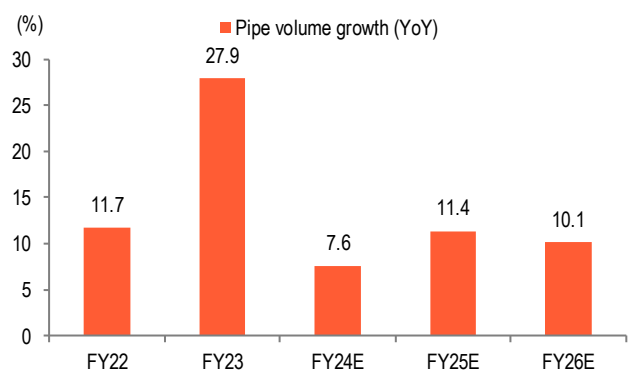
Source: Company, BOBCAPS Research

Fig 7 – Business risk profile to improve as no major capex plan for B2B PVC resin segment



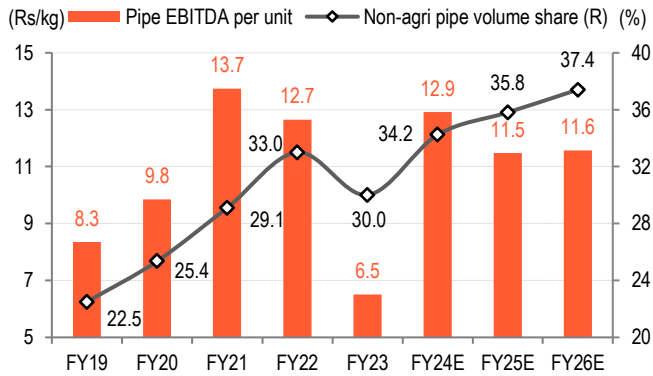
Source: Company, BOBCAPS Research

Fig 8 – Pipe volumes forecast to grow in double digits over the medium term



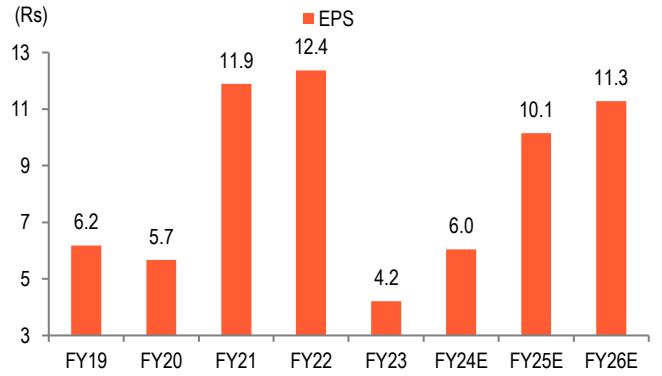
Source: Company, BOBCAPS Research

Fig 9 – Pipe EBITDA per unit trending up on rising share of higher margin non-agri pipes



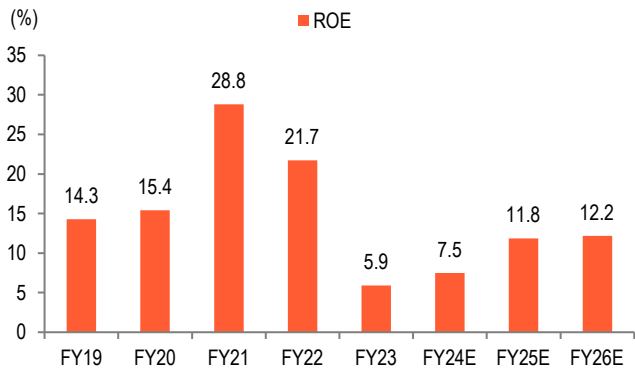
Source: Company, BOBCAPS Research

Fig 10 – EPS projected to log a slow 9% CAGR over FY19-FY26E



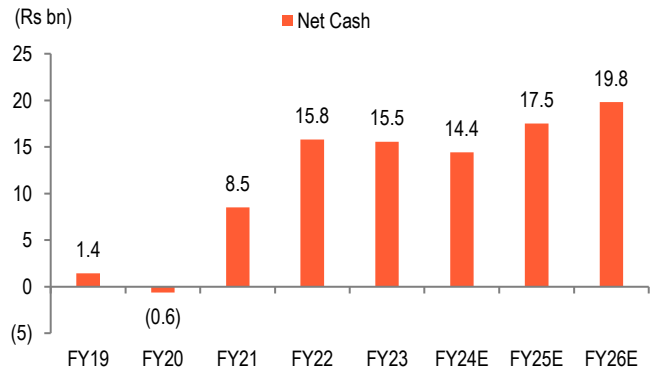
Source: Company, BOBCAPS Research

Fig 11 – ROE to fall from 14.3% in FY19 to ~12% in FY25E-FY26E...



Source: Company, BOBCAPS Research

Fig 12 – ...due to poor capital allocation as there is no concrete plan for using surplus cash for growth



Source: Company, BOBCAPS Research

Valuation methodology

While we believe FNXP’s business risk profile will improve on a structural basis due to a rising share of B2C pipe revenue, we maintain our HOLD rating on the stock with an unchanged TP of Rs 230 due to its limited growth prospects (EPS estimated to log a slow 9% CAGR over FY19-FY26) and weak return ratio profile amidst poor capital allocation. Per our estimates, ROE could drop from 15.4% in FY20 to ~12% in FY25-FY26 in the absence of a concrete plan for better utilisation of surplus cash for growth.

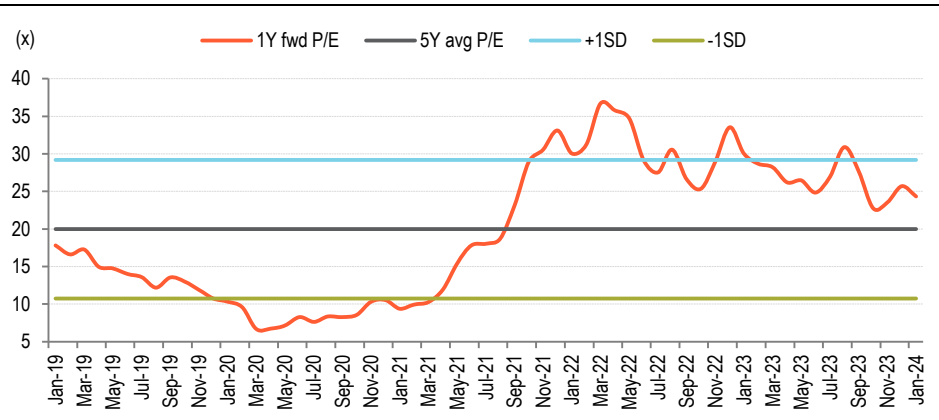
We cut our EPS estimates by 18% for FY24 due to the weak third-quarter results, but largely maintain our forecasts for FY25/FY26. At CMP, the stock trades at 24.3x one-year forward P/E. Our target P/E multiple remains unchanged at 22x on Sep’25E EPS, a 10% premium to the stock’s five-year average to account for an improving risk profile.

Fig 13 – Revised estimates

Consolidated (Rs bn)	New			Old			Change (%)		
	FY24E	FY25E	FY26E	FY24E	FY25E	FY26E	FY24E	FY25E	FY26E
Revenue	41.7	45.2	51.3	44.5	49.4	55.5	(6.2)	(8.4)	(7.6)
EBITDA	4.7	8.2	9.2	5.8	8.4	9.4	(19.3)	(2.8)	(1.9)
EBITDA margin	11.2	18.1	18.0	13.0	17.1	16.9	(182bps)	105bps	106bps
Adjusted PAT	3.7	6.3	7.0	4.5	6.3	7.0	(17.6)	(1.0)	(0.3)
Adjusted EPS (Rs)	6.0	10.1	11.3	7.3	10.3	11.3	(17.6)	(1.0)	(0.3)

Source: BOBCAPS Research

Fig 14 – Trading at 24.3x 1Y forward P/E vs. 5Y average of 20x



Source: Bloomberg, BOBCAPS Research

Fig 15 – Key assumptions

Parameter (%)	FY21A	FY22A	FY23A	FY24E	FY25E	FY26E
Revenue mix						
PVC resin	23.9	17.1	6.5	1.9	0.0	0.0
Pipes & Fittings	76.1	82.9	93.5	98.1	100.0	100.0
Sales volume growth						
Pipes & Fittings	(16.8)	11.7	27.9	7.6	11.4	10.1
Realisation growth						
Pipes & Fittings	24.1	30.9	(16.5)	(7.4)	(0.8)	3.0
EBITDA unit (Rs/kg)						
PVC resin	29.6	32.4	4.0	8.0	15.4	16.4
Pipes & Fittings	13.7	12.7	6.5	12.9	11.5	11.6

Source: Company, BOBCAPS Research

Key risks

- Better utilisation of surplus cash, strong agricultural pipe demand and settlement of a long-pending family dispute related to control of Finolex Cables (FNXC) would be key upside risks.
- A steep decline in PVC resin prices and market share loss in the plumbing pipe portfolio would represent key downside risks

Sector recommendation snapshot

Company	Ticker	Market Cap (US\$ bn)	Price (Rs)	Target (Rs)	Rating
Apollo Pipes	APOLP IN	0.4	729	650	HOLD
Astral	ASTRA IN	6.1	1,851	2,000	HOLD
Century Plyboards	CPBI IN	2.2	803	800	HOLD
Cera Sanitaryware	CRS IN	1.3	8,170	8,100	HOLD
Finolex Industries	FNXP IN	1.7	231	230	HOLD
Greenlam Industries	GRLM IN	0.8	524	600	HOLD
Greenpanel Industries	GREENP IN	0.6	396	400	HOLD
Greenply Industries	MTLM IN	0.4	238	300	BUY
Hindware Home Innovation	HINDWARE IN	0.4	485	700	BUY
Kajaria Ceramics	KJC IN	2.7	1,390	1,450	HOLD
Prince Pipes & Fittings	PRINCPIN IN	0.9	695	800	HOLD
Somany Ceramics	SOMC IN	0.4	703	900	BUY
Supreme Industries	SI IN	6.4	4,124	4,300	HOLD

Source: BOBCAPS Research, NSE | Price as of 19 Jan 2024

Financials

Income Statement

Y/E 31 Mar (Rs mn)	FY22A	FY23A	FY24E	FY25E	FY26E
Total revenue	46,473	43,971	41,747	45,236	51,287
EBITDA	10,276	3,258	4,679	8,200	9,214
Depreciation	834	892	1,099	1,123	1,201
EBIT	9,442	2,366	3,580	7,077	8,013
Net interest inc./(exp.)	(141)	(272)	(368)	(306)	(306)
Other inc./(exp.)	822	1,209	1,538	1,373	1,373
Exceptional items	39	332	0	0	0
EBT	10,085	2,970	4,751	8,144	9,080
Income taxes	3,317	706	1,257	2,111	2,346
Extraordinary items	(3,761)	0	0	0	0
Min. int./Inc. from assoc.	(15)	243	243	243	243
Reported net profit	10,513	2,507	3,736	6,276	6,976
Adjustments	(2,841)	97	0	0	0
Adjusted net profit	7,672	2,604	3,736	6,276	6,976

Balance Sheet

Y/E 31 Mar (Rs mn)	FY22A	FY23A	FY24E	FY25E	FY26E
Accounts payables	4,631	2,893	2,769	3,001	3,402
Other current liabilities	4,535	3,158	3,158	3,158	3,158
Provisions	42	45	43	46	52
Debt funds	2,780	5,264	5,264	5,264	5,264
Other liabilities	2,187	2,460	2,460	2,460	2,460
Equity capital	1,241	1,237	1,237	1,237	1,237
Reserves & surplus	38,037	47,794	49,675	53,787	58,289
Shareholders' fund	39,278	49,031	50,912	55,023	59,526
Total liab. and equities	53,454	62,851	64,606	68,953	73,863
Cash and cash eq.	18,573	20,812	19,701	22,809	25,092
Accounts receivables	3,345	2,975	2,825	3,061	3,471
Inventories	10,155	6,732	8,887	8,937	10,226
Other current assets	625	940	900	975	1,106
Investments	9,415	19,262	19,262	19,262	19,262
Net fixed assets	9,923	10,376	11,277	12,154	12,953
CWIP	95	438	438	438	438
Intangible assets	9	176	176	176	176
Deferred tax assets, net	256	245	245	245	245
Other assets	1,060	894	894	894	894
Total assets	53,454	62,851	64,606	68,953	73,863

Cash Flows

Y/E 31 Mar (Rs mn)	FY22A	FY23A	FY24E	FY25E	FY26E
Cash flow from operations	6,113	3,622	1,574	6,205	5,689
Capital expenditures	(801)	(1,868)	(2,000)	(2,000)	(2,000)
Change in investments	160	(9,848)	0	0	0
Other investing cash flows	4,544	877	1,538	1,373	1,373
Cash flow from investing	3,904	(10,839)	(462)	(627)	(627)
Equities issued/Others	0	(4)	0	0	0
Debt raised/repaid	742	2,484	0	0	0
Interest expenses	(2,482)	(928)	(1,855)	(2,164)	(2,473)
Dividends paid	(141)	(272)	(368)	(306)	(306)
Other financing cash flows	(143)	8,177	0	0	0
Cash flow from financing	(2,024)	9,457	(2,223)	(2,471)	(2,780)
Chg in cash & cash eq.	7,993	2,240	(1,111)	3,108	2,282
Closing cash & cash eq.	18,573	20,812	19,701	22,809	25,092

Per Share

Y/E 31 Mar (Rs)	FY22A	FY23A	FY24E	FY25E	FY26E
Reported EPS	16.9	4.1	6.0	10.1	11.3
Adjusted EPS	12.4	4.2	6.0	10.1	11.3
Dividend per share	4.0	1.5	3.0	3.5	4.0
Book value per share	63.3	79.3	82.3	89.0	96.3

Valuations Ratios

Y/E 31 Mar (x)	FY22A	FY23A	FY24E	FY25E	FY26E
EV/Sales	3.2	3.5	3.8	3.5	3.1
EV/EBITDA	14.3	47.7	33.9	19.3	17.3
Adjusted P/E	18.7	54.9	38.3	22.8	20.5
P/BV	3.7	2.9	2.8	2.6	2.4

DuPont Analysis

Y/E 31 Mar (%)	FY22A	FY23A	FY24E	FY25E	FY26E
Tax burden (Net profit/PBT)	76.1	87.7	78.7	77.1	76.8
Interest burden (PBT/EBIT)	106.8	125.6	132.7	115.1	113.3
EBIT margin (EBIT/Revenue)	20.3	5.4	8.6	15.6	15.6
Asset turnover (Rev./Avg TA)	86.9	70.0	64.6	65.6	69.4
Leverage (Avg TA/Avg Equity)	1.5	1.4	1.3	1.3	1.3
Adjusted ROAE	21.7	5.9	7.5	11.8	12.2

Ratio Analysis

Y/E 31 Mar	FY22A	FY23A	FY24E	FY25E	FY26E
YoY growth (%)					
Revenue	34.2	(5.4)	(5.1)	8.4	13.4
EBITDA	3.8	(68.3)	43.6	75.3	12.4
Adjusted EPS	3.9	(65.9)	43.5	68.0	11.2
Profitability & Return ratios (%)					
EBITDA margin	22.1	7.4	11.2	18.1	18.0
EBIT margin	20.3	5.4	8.6	15.6	15.6
Adjusted profit margin	16.5	5.9	9.0	13.9	13.6
Adjusted ROAE	21.7	5.9	7.5	11.8	12.2
ROCE	24.4	6.6	9.1	14.0	14.5
Working capital days (days)					
Receivables	26	25	25	25	25
Inventory	80	56	78	72	73
Payables	36	24	24	24	24
Ratios (x)					
Gross asset turnover	1.9	1.8	1.6	1.6	1.7
Current ratio	2.7	2.8	2.9	3.1	3.4
Net interest coverage ratio	67.0	8.7	9.7	23.1	26.2
Adjusted debt/equity	(0.4)	(0.3)	(0.3)	(0.3)	(0.3)

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

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Recommendation scale: Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

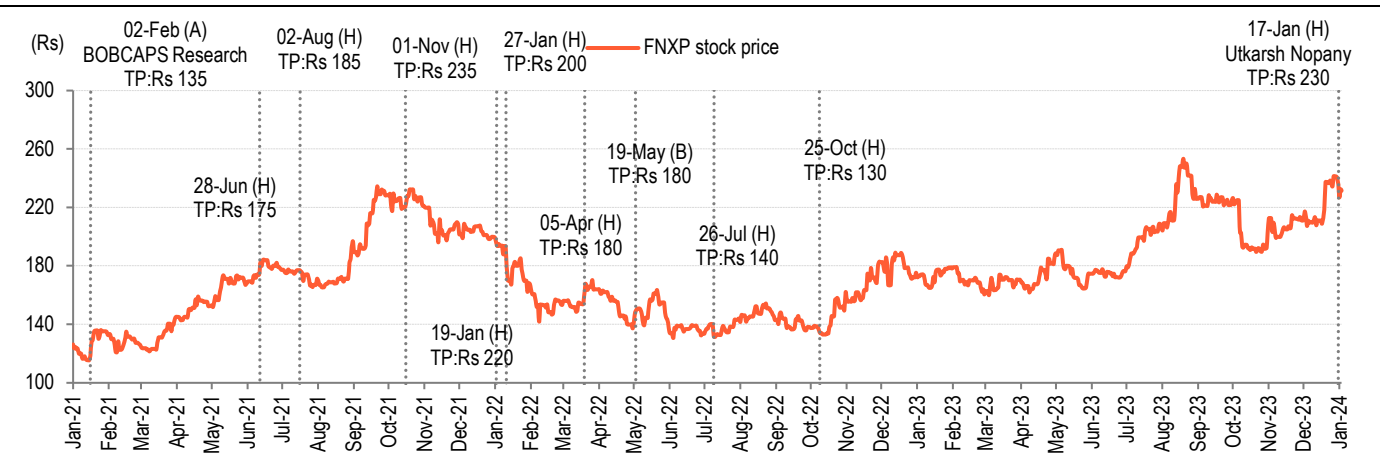
HOLD – Expected return from -6% to +15%

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

Our recommendation scale does not factor in short-term stock price volatility related to market fluctuations. Thus, our recommendations may not always be strictly in line with the recommendation scale as shown above.

Ratings and Target Price (3-year history): FINOLEX INDUSTRIES (FNXP IN)



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

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