FIRST LIGHT

01 April 2022

RESEARCH

Wood Panels

MDF remains a strong growth driver

India Strategy | Monthly Wrap

Commodity prices appear to have peaked

Daily macro indicators

Indicator	29-Mar	30-Mar	Chg (%)
US 10Y yield (%)	2.39	2.35	(5)
India 10Y yield (%)	6.82	6.78	(4)
USD/INR	75.99	75.91	0.1
Brent Crude (US$/bbl)	110.2	113.5	2.9
Dow	35,294	35,229	(0.2)
Hang Seng	21,928	22,232	1.4
Sensex	57,944	58,684	1.3
India FII (US$ mn)	**28-Mar**	**29-Mar**	**Chg ($ mn)**
FII-D	(81.9)	(90.0)	(8.2)
FII-E	(51.2)	(23.3)	27.9

Source: Bank of Baroda Economics Research

SUMMARY

Wood Panels

- MDF growth continue to outpace plywood led by strong OEM demand, increasing applications and lower imports
- Underlying demand remains robust owing to traction in real estate, new construction and market share gains from the informal sector
- GREENP and CPBI – our top picks thus far – downgraded from BUY to HOLD as the recent rally prices in positives; maintain BUY on Greenply

Click here for the full report.

India Strategy: Monthly Wrap

- Global commodity prices (ex-agri) have likely peaked in Mar'22 unless the Russia-Ukraine war escalates and/or sanctions are widened
- March saw small- and mid-caps slightly outperform large-caps; valuations are now largely in line with the 5Y average for most sectors ex-IT
- We remain constructive on the market and believe the Nifty will likely perform in line with nominal GDP growth over CY22

Click here for the full report.

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WOOD PANELS

31 March 2022

MDF remains a strong growth driver

- **MDF growth continue to outpace plywood led by strong OEM demand, increasing applications and lower imports**
- **Underlying demand remains robust owing to traction in real estate, new construction and market share gains from the informal sector**
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Rising acceptance of MDF in India: Industry experts (Niveshaay) estimate India's MDF market size at 2.8mn cbm (Rs 30bn) in 2021 and expect it to grow at a 15-20% CAGR to Rs 60bn by 2026. Rising demand for branded, readymade and low-maintenance furniture is propelling growth in MDF. We believe the entry of Ikea in India is likely to widen the acceptability of factory-made furniture.

Lower imports aiding growth: MDF imports catered to ~30% of demand before Covid. However, imports have not picked up post pandemic due to a shortage of MDF in the international market (no new capacity, plant shutdowns) and high logistics cost. This has boosted export realisations from US$ 190/cbm to US$ 250-270/cbm. We expect MDF imports to remain limited for the next couple of quarters due to elevated global prices and freight costs, thus benefitting domestic players.

Organised plywood players to witness strong growth: In our view, organised plywood companies will continue to perform well over FY22-FY24 supported by demand from the real estate/replacement market, a narrowing price differential to unorganised players post GST (from ~25% pre-GST to 10-15% currently) and an enhanced distribution reach.

Q4 to see volume and margin stress: Weak demand in Jan'22 due to the third Covid wave is likely to subdue Q4FY22 MDF volumes QoQ. Still, underlying demand remains robust given strong OEM demand, wider distribution, lower imports, rising acceptance of readymade furniture and a shorter replacement cycle. On the margin front, raw material cost forms ~40% of revenue (of which chemical cost is 20-50% of RM cost) and is at elevated levels. Wood panel players have been hiking prices with a lag effect (2-2.5% for plywood in mid-Feb, 17% for MDF in Q3) to negate cost inflation. However, the rise in crude-derived chemical prices (Brent up 75% YTD) can exert margin pressure in Q4.

Recent rally prices in positives: GREENP (TP Rs 595) and CPBI (TP Rs 735) – our top picks in the wood panel space thus far – have rallied over 25% in the past month and achieved our target price. We thus cut both stocks from BUY to HOLD. Greenply's (GIL) upcoming foray into MDF should fortify valuations – retain BUY (TP Rs 260).

Recommendation snapshot

Ticker	Price	Target	Rating
CPBI IN	716	735	HOLD
GREENP IN	585	595	HOLD
MTLM IN	220	260	BUY

Price & Target in Rupees | Price as of 31 Mar 2022

MONTHLY WRAP | Volume #2 | 31 March 2022

Commodity prices appear to have peaked

- **Global commodity prices (ex-agri) have likely peaked in Mar'22 unless the Russia-Ukraine war escalates and/or sanctions are widened**
- **March saw small- and mid-caps slightly outperform large-caps; valuations are now largely in line with the 5Y average for most sectors ex-IT**
- **We remain constructive on the market and believe the Nifty will likely perform in line with nominal GDP growth over CY22**

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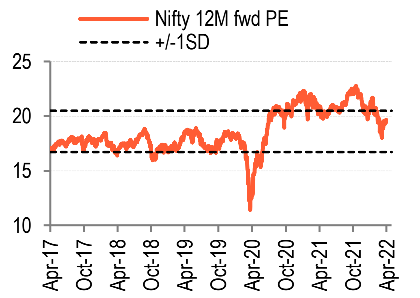
Russia-Ukraine crisis and commodities: The Russia-Ukraine war continues to impact both equity and commodity markets. While equities have recovered to pre-war levels, commodity prices remain elevated despite cooling down from recent highs. Given slowing demand in China, we believe commodity prices have largely peaked in Mar'22 unless the war escalates further or more sanctions are levied by the US and EU.

Impact on India to be limited for now: As stated in our note No winners in war dated 10 March 2022, the spike in oil price is negative for India's inflation and forex outgo given its oil imports of ~4mbpd, but we believe the economy may not suffer materially in the longer run. The metals sector could gain near term though Russia's dominance in metals such as palladium and nickel and Ukraine's role in the chip supply chain will likely be adverse for the Indian auto sector. Fertiliser prices have also shot up due to supply constraints from Russia, which would adversely impact India's fiscal deficits as fertiliser is supplied at subsidised rates to farmers.

Market delivered 4% returns in March: Indian equity markets underperformed the US and Japan but outperformed the EU and UK in March. Further, small- and mid-cap indices outperformed large-caps. Baring the Nifty Auto index, all other sectoral indices clocked positive returns for the month. Nifty Media gained the most (+18.3%), Metal (+8.9%) and Energy (+6.6%) benefited from commodity inflation, and IT (+7.3%) and Realty (+6.2%) also rose after a selloff in previous months. Auto (-2.5%) and FMCG (+2.2%) were hit by the rising raw material cost.

Valuations climbed after a sharp decline: Valuations for most sectors (ex-IT, banks) are now largely in line with their five-year 12-month forward average P/E. After the gains in March, the broader Nifty 50 index is currently trading at a modest 2.2% premium to its five-year average as compared to a 6.1% discount at the start of the month. Note there was no major earnings upgrades during the month as the six-month change in 12-month forward earnings showed a mere 20bps rise. Higher raw material costs will likely hurt the earnings of Indian stocks in Q4FY22, though we believe companies have levers to cushion the impact to a large extent.

Nifty valuation



Source: Bloomberg, BOBCAPS Research

Disclaimer

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.

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