

SELL

TP: Rs 1,325 | ▼ 9%

SUPREME INDUSTRIES

Plastic Products

28 October 2020

Margin expansion largely inventory-led; cut to SELL

Supreme Industries' (SI) Q2FY21 revenue grew 8% YoY, aided by a 1% rise in volumes. EBITDA margins expanded 500bps YoY to 18.6% on lower RM cost and other expense. EBITDA/PBT grew 48%/76% YoY. Management did not proffer FY21 guidance due to sustained Covid uncertainty. We hike FY21-FY23 earnings 9-49% due to the above-expected Q2 and raise our target P/E to 28x (from 27x). Rolling over, we have a revised Dec'21 TP of Rs 1,325 (vs. Rs 1,120). At 29.8x FY23E P/E, valuations look rich – cut from REDUCE to SELL.

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Volumes flattish: SI's revenue grew 8% YoY to Rs 13.7bn in Q2. Plastic piping/ industrials/packaging revenues increased 4%/7%/11% YoY, whereas the consumer segment declined 1%. Volume growth came from industrials (+13.4% YoY) and packaging (+10.6%); piping declined 1.8%, resulting in blended volume growth of 1.4% YoY. Management indicated a demand revival for housing pipes from September and anticipates further improvement provided the pandemic situation does not worsen.

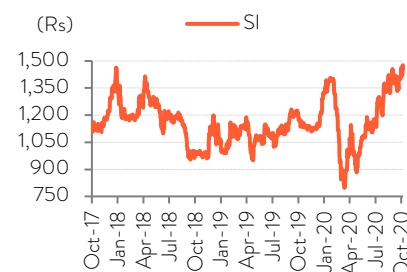
Inventory gains aid margins: SI's operating margins expanded 500bps YoY to 18.6% due to lower raw material cost (-425bps) and other expenditure (-48bps). Gross margins increased in Q2 mainly from inventory gains due to rising PVC resin prices and a better product mix. EBITDA/PBT for the quarter thus rose 48%/76% YoY. Per management, recent cost control measures would continue to aid margins, though SI could face inventory losses in Q4 when PVC prices likely normalise.

Downgrade to SELL: Though we like SI for its strong brand, comprehensive portfolio and sound balance sheet, we find current valuations of 29.8x FY23E P/E rich and hence downgrade the stock from REDUCE to SELL. Our revised Dec'21 TP stands at Rs 1,325.

Ticker/Price	SI IN/Rs 1,459
Market cap	US\$ 2.5bn
Shares o/s	127mn
3M ADV	US\$ 1.4mn
52wk high/low	Rs 1,500/Rs 773
Promoter/FPI/DII	49%/9%/42%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue (Rs mn)	56,086	55,087	54,211	61,249	67,734
EBITDA (Rs mn)	7,812	8,563	8,100	9,334	10,556
Adj. net profit (Rs mn)	3,683	4,866	4,534	5,429	6,212
Adj. EPS (Rs)	29.0	38.3	35.7	42.7	48.9
Adj. EPS growth (%)	(13.2)	32.1	(6.8)	19.8	14.4
Adj. ROAE (%)	18.2	22.0	19.1	20.6	21.2
Adj. P/E (x)	50.3	38.1	40.9	34.1	29.8
EV/EBITDA (x)	23.5	21.5	22.7	19.7	17.5

Source: Company, BOBCAPS Research

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



FIG 1 – CONSOLIDATED QUARTERLY PERFORMANCE

(Rs mn)	Q2FY21	Q2FY20	YoY (%)	Q1FY21	QoQ (%)	H1FY21	H1FY20	YoY (%)
Total revenues	13,748	12,709	8.2	10,539	30.4	24,287	27,077	(10.3)
Total raw material consumed	8,486	8,384	1.2	7,544	12.5	16,030	18,411	(12.9)
% of sales	61.7	66.0	(424bps)	71.6	(985bps)	66.0	68.0	(199bps)
Employee exps	727	685	6.1	633	14.9	1,360	1,371	(0.8)
% of sales	5.3	5.4	(10bps)	6.0	(72bps)	5.6	5.1	53bps
Power & fuel expense	535	519	3.1	349	53.5	884	1069	(17.3)
% of sales	3.9	4.1	(19bps)	3.3	58bps	3.6	3.9	(31bps)
Other exp	1,441	1,393	3.5	842	71.0	2,283	2,825	(19.2)
% of sales	10.5	11.0	(48bps)	8.0	249bps	9.4	10.4	(103bps)
Total expenditure	11,189	10,981	1.9	9,368	19.4	20,557	23,676	(13.2)
% of sales	81.4	86.4	(501bps)	88.9	(750bps)	84.6	87.4	(279bps)
EBITDA	2,559	1,728	48.1	1,171	118.5	3,730	3,402	9.6
% of sales	18.6	13.6	501bps	11.1	750bps	15.4	12.6	279bps
Depreciation	523	517	1.1	508	3.0	1,031	1,013	1.8
Other income	1	5	(85.2)	3	(71.4)	4	6	(36.8)
Interest cost	25	71	(64.8)	78	(68.0)	103	103	(0.5)
PBT	2,011	1,145	75.6	588	242.0	2,600	2,291	13.5
Taxes	527.0	(140.4)	(475.4)	146.4	260.0	673.4	259.1	159.9
Effective tax rate (%)	26	(12)	3,846bps	25	131bps	26	11	1,460bps
PAT	1,484	1,286	15.4	442	236.0	1,926	2,032	(5.2)
Share of profit of associate	265	110	141.2	(37)	(826.3)	229	235	(2.6)
RPAT	1,750	1,396	25.3	405	331.7	2,155	2,267	(5.0)

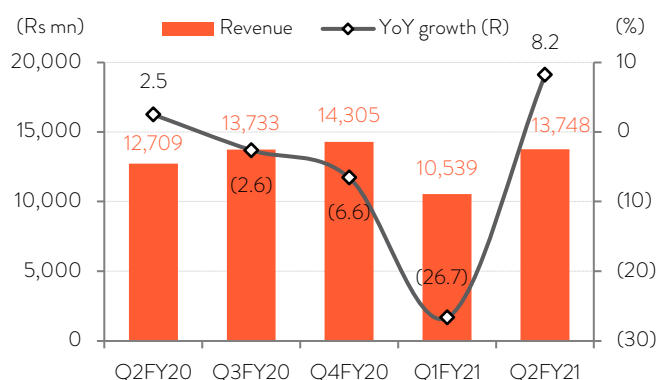
Source: Company, BOBCAPS Research

FIG 2 – SEGMENTAL PERFORMANCE

(Rs mn)	Q2FY21	Q2FY20	YoY (%)	Q1FY21	QoQ (%)	H1FY21	H1FY20	YoY (%)
(1) Segment revenue								
Plastic Piping Products	8,473	8,115	4.4	7,646	10.8	16,118	17,095	(5.7)
Industrial Products	1,815	1,691	7.3	705	157.4	2,519	3,574	(29.5)
Packaging Products	2,198	1,980	11.1	1,876	17.2	4,074	4,431	(8.0)
Consumer Products	855	863	(1.0)	280	205.3	1,135	1,837	(38.2)
Others	408	60	576.1	33	1154.5	440	142	210.9
Net Revenue from Operations	13,748	12,709	8.2	10,539	30.4	24,287	27,077	(10.3)
(2) EBIT								
Plastic Piping Products	1,475	1,099	34.3	665	122.0	2,140	1,882	13.7
Industrial Products	120	(20)	(711.7)	(76)	(257.8)	44	101	(56.4)
Packaging Products	256	38	569.9	183	39.6	439	244	79.9
Consumer Products	127	110	15.8	(45)	(382.0)	82	238	(65.6)
Others	100	3	3362.1	(1)	(8,466.7)	99	1	12,300.0
Total Segment Profit before Interest and Tax	2,079	1,230	69.0	726	186.4	2,804	2,465	13.8
Margins (%)								
Plastic Piping Products	17.4	13.5	388bps	8.7	872bps	13.3	11.0	227bps
Industrial Products	6.6	(1.2)	777bps	(10.8)	1,739bps	1.7	2.8	(108bps)
Packaging Products	11.6	1.9	971bps	9.8	187bps	10.8	5.5	527bps
Consumer Products	14.8	12.7	215bps	(16.1)	3,092bps	7.2	13.0	(575bps)

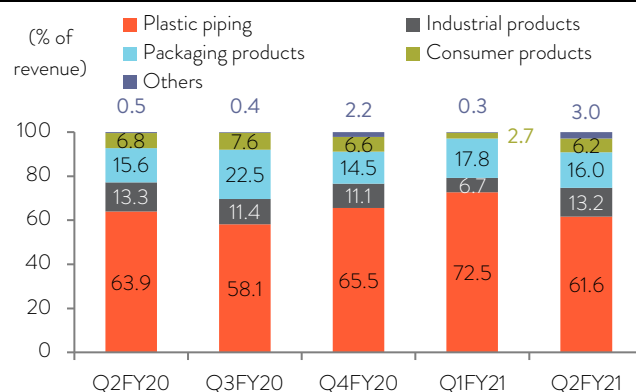
Source: Company, BOBCAPS Research

FIG 3 – CONSOLIDATED REVENUE GROWTH



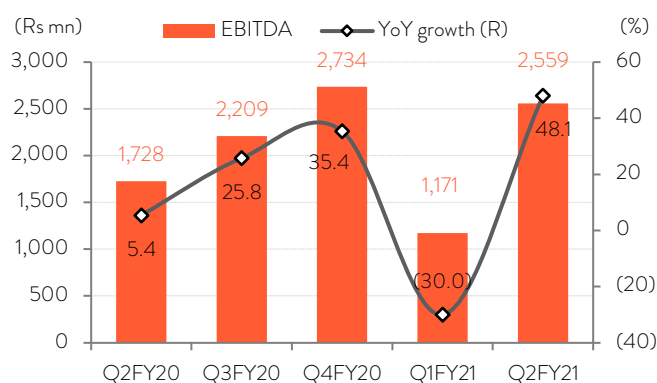
Source: BOBCAPS Research

FIG 4 – REVENUE MIX



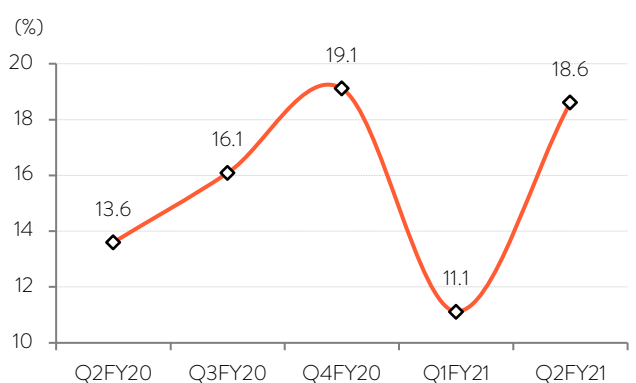
Source: BOBCAPS Research

FIG 5 – CONSOLIDATED EBITDA GROWTH



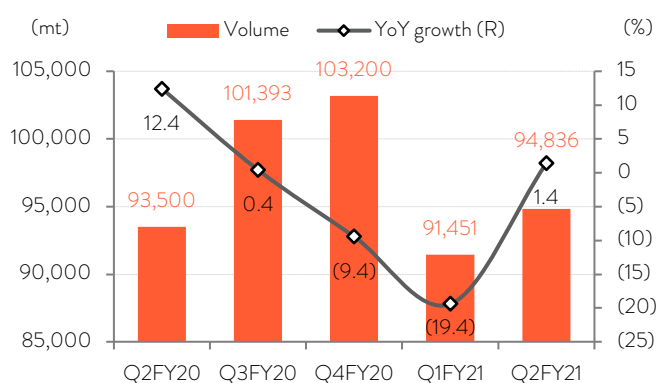
Source: BOBCAPS Research, Company

FIG 6 – CONSOLIDATED EBITDA MARGIN



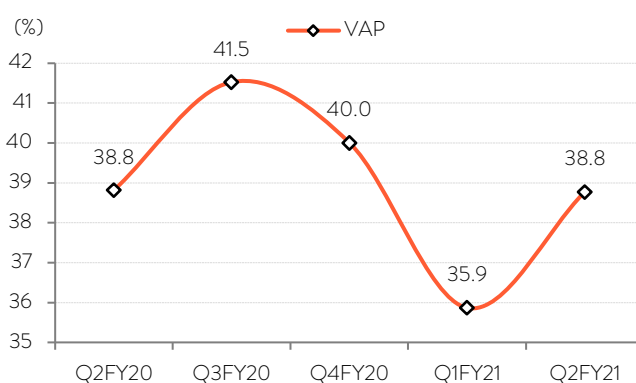
Source: BOBCAPS Research, Company

FIG 7 – VOLUME GROWTH



Source: BOBCAPS Research, Company

FIG 8 – REVENUE SHARE OF VALUE-ADDED PRODUCTS



Source: BOBCAPS Research, Company

FIG 9 – SEGMENTAL VOLUMES

(MT)	Q2FY21	Q2FY20	YoY (%)	Q1FY21	QoQ (%)
Plastic piping	66,609	67,812	(1.8)	74,992	(11.2)
Packaging Products	12,239	11,062	10.6	10,182	20.2
Industrial Products	11,285	9,953	13.4	4,770	136.6
Consumer Products	4,703	4,673	0.6	1,507	212.1
Total	94,836	93,500	1.4	91,451	3.7

Source: Company, BOBCAPS Research

Earnings call highlights

- During Q2FY21, demand picked up across SI's product categories as the economy opened up. Plant utilisation reached pre-Covid levels during the quarter. October also looks to be a growth month across categories.
- Piping demand from the housing segment has revived across markets, except the MMR.
- Management expects demand to continue improving MoM unless the Covid-19 situation worsens. SI nevertheless refrained from giving out FY21 guidance due to persisting pandemic uncertainties.
- PVC prices have been going up and may continue to do so till Q3FY21. Management expects prices to soften from January.
- Due to higher PVC prices, dealer stocking has been limited which has resulted in the company carrying higher stocks.
- SI had inventory gains in Q2 due to the rising PVC prices but expects a reversal in Q4 when prices are likely to fall.
- Prices of all other raw materials besides PVC are range-bound.
- Management believes some margin gains will be sustained due to recent cost and operational measures.
- SI believes it gained market share in pipes during H1. The PVC resin market declined by 25% in the first half of the year.
- The company plans to set up factories in Assam and Tamil Nadu and is in discussions for buying land there. The Odisha plant land deal should be concluded by Nov'20.
- SI is focused on increasing its dealer network and has added ~85 dealers in FY21, taking its total count to 1,300.

Valuation methodology

SI is a play on India’s growing housing and consumer market, backed by a strong brand, comprehensive product portfolio and wide distribution reach. A healthy operating margin profile (14-15%), impressive return ratios (ROE of 21% in FY23E) and negligible debt make the stock attractive.

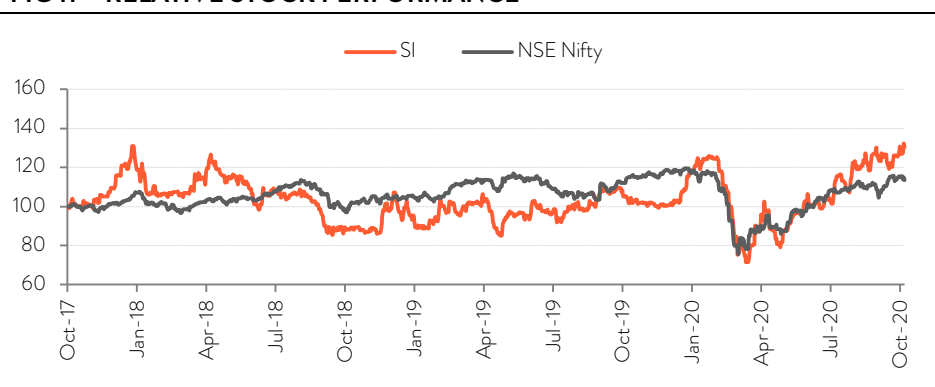
Post Q2, we increase FY21/FY22/FY23 earnings estimates by 49%/12%/9%. Our EBITDA revision in FY21 is partly driven by inventory gains whereas PAT revision is higher than EBITDA due to the above-expected performance at associate company Supreme Petrochem. Though we like SI for its product portfolio and strong balance sheet, current valuations of 29.8x FY23E P/E appear rich. We downgrade the stock from REDUCE to SELL and roll forward to a revised Dec’21 target price of Rs 1,325 (earlier Rs 1,120). We now value SI at a one-year forward P/E of 28x (earlier 27x), in line with the five-year average.

FIG 10 – REVISED ESTIMATES

(Rs mn)	Old			New			Change (%)		
	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E
Revenue	47,417	58,151	65,160	54,211	61,249	67,734	14.3	5.3	4.0
EBITDA	6,364	8,629	9,915	8,100	9,334	10,556	27.3	8.2	6.5
PAT	3,043	4,831	5,678	4,534	5,429	6,212	49.0	12.4	9.4

Source: BOBCAPS Research

FIG 11 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

Key upside risks to our call are:

- above-expected margins in the event of reduced raw material cost, and
- the unorganised market seeing a worse fall than anticipated.

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue	56,086	55,087	54,211	61,249	67,734
EBITDA	7,812	8,563	8,100	9,334	10,556
Depreciation	(1,835)	(2,057)	(2,194)	(2,395)	(2,644)
EBIT	5,977	6,506	5,906	6,939	7,912
Net interest income/(expenses)	(336)	(297)	(210)	(95)	(60)
Other income/(expenses)	56	84	88	123	148
Exceptional items	803	(192)	0	0	0
EBT	5,697	6,293	5,784	6,968	8,000
Income taxes	(2,158)	(1,739)	(1,560)	(1,868)	(2,138)
Extraordinary items	0	0	0	0	0
Min. int./Inc. from associates	144	312	310	330	350
Reported net profit	4,486	4,674	4,534	5,429	6,212
Adjustments	(803)	192	0	0	0
Adjusted net profit	3,683	4,866	4,534	5,429	6,212

Balance Sheet

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Accounts payables	5,574	5,475	5,198	5,873	6,495
Other current liabilities	2,123	2,347	2,079	2,349	2,598
Provisions	240	313	379	429	474
Debt funds	1,613	4,113	1,500	400	200
Other liabilities	843	947	947	947	947
Equity capital	254	254	254	254	254
Reserves & surplus	21,286	22,358	24,697	27,499	30,704
Shareholders' fund	21,540	22,612	24,951	27,753	30,958
Total liabilities and equities	31,932	35,807	35,055	37,751	41,672
Cash and cash eq.	373	1,614	157	458	1,424
Accounts receivables	3,874	3,128	3,565	4,363	4,825
Inventories	7,504	8,906	8,169	8,390	9,279
Other current assets	1,847	2,379	2,079	2,349	2,598
Investments	2,223	2,773	2,773	2,773	2,773
Net fixed assets	15,014	15,917	17,223	18,328	19,684
CWIP	900	929	929	929	929
Intangible assets	196	160	160	160	160
Total assets	31,932	35,807	35,055	37,751	41,672

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Net income + Depreciation	6,322	6,731	6,728	7,824	8,856
Interest expenses	336	297	210	95	60
Non-cash adjustments	0	0	0	0	0
Changes in working capital	674	(989)	123	(296)	(683)
Other operating cash flows	0	0	0	0	0
Cash flow from operations	7,331	6,038	7,061	7,623	8,233
Capital expenditures	(3,661)	(2,953)	(3,500)	(3,500)	(4,000)
Change in investments	287	(550)	0	0	0
Other investing cash flows	71	(211)	0	0	0
Cash flow from investing	(3,304)	(3,714)	(3,500)	(3,500)	(4,000)
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	(851)	2,500	(2,613)	(1,100)	(200)
Interest expenses	(336)	(297)	(210)	(95)	(60)
Dividends paid	(1,991)	(3,522)	(2,194)	(2,628)	(3,007)
Other financing cash flows	(840)	235	0	0	0
Cash flow from financing	(4,017)	(1,084)	(5,017)	(3,823)	(3,267)
Changes in cash and cash eq.	10	1,240	(1,456)	301	967
Closing cash and cash eq.	373	1,613	157	458	1,424

Per Share

Y/E 31 Mar (Rs)	FY19A	FY20A	FY21E	FY22E	FY23E
Reported EPS	35.3	36.8	35.7	42.7	48.9
Adjusted EPS	29.0	38.3	35.7	42.7	48.9
Dividend per share	13.0	14.0	14.3	17.1	19.6
Book value per share	169.6	178.0	196.4	218.5	243.7

Valuations Ratios

Y/E 31 Mar (x)	FY19A	FY20A	FY21E	FY22E	FY23E
EV/Sales	3.3	3.3	3.4	3.0	2.7
EV/EBITDA	23.5	21.5	22.7	19.7	17.5
Adjusted P/E	50.3	38.1	40.9	34.1	29.8
P/BV	8.6	8.2	7.4	6.7	6.0

DuPont Analysis

Y/E 31 Mar (%)	FY19A	FY20A	FY21E	FY22E	FY23E
Tax burden (Net profit/PBT)	56.7	79.8	78.4	77.9	77.7
Interest burden (PBT/EBIT)	108.8	93.8	97.9	100.4	101.1
EBIT margin (EBIT/Revenue)	10.7	11.8	10.9	11.3	11.7
Asset turnover (Revenue/Avg TA)	183.0	162.6	153.0	168.3	170.6
Leverage (Avg TA/Avg Equity)	1.5	1.5	1.5	1.4	1.4
Adjusted ROAE	18.2	22.0	19.1	20.6	21.2

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

Ratio Analysis

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
YoY growth (%)					
Revenue	13.0	(1.8)	(1.6)	13.0	10.6
EBITDA	(0.4)	9.6	(5.4)	15.2	13.1
Adjusted EPS	(13.2)	32.1	(6.8)	19.8	14.4
Profitability & Return ratios (%)					
EBITDA margin	13.9	15.5	14.9	15.2	15.6
EBIT margin	10.7	11.8	10.9	11.3	11.7
Adjusted profit margin	6.6	8.8	8.4	8.9	9.2
Adjusted ROAE	18.2	22.0	19.1	20.6	21.2
ROCE	17.9	18.7	16.2	18.6	19.6
Working capital days (days)					
Receivables	25	23	23	24	25
Inventory	69	84	87	75	72
Payables	40	43	42	39	39
Ratios (x)					
Gross asset turnover	2.1	1.9	1.7	1.7	1.7
Current ratio	1.4	1.3	1.5	1.7	1.9
Net interest coverage ratio	17.8	21.9	28.1	73.0	131.9
Adjusted debt/equity	0.1	0.1	0.1	0.0	0.0

Source: Company, BOBCAPS Research

Disclaimer

Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

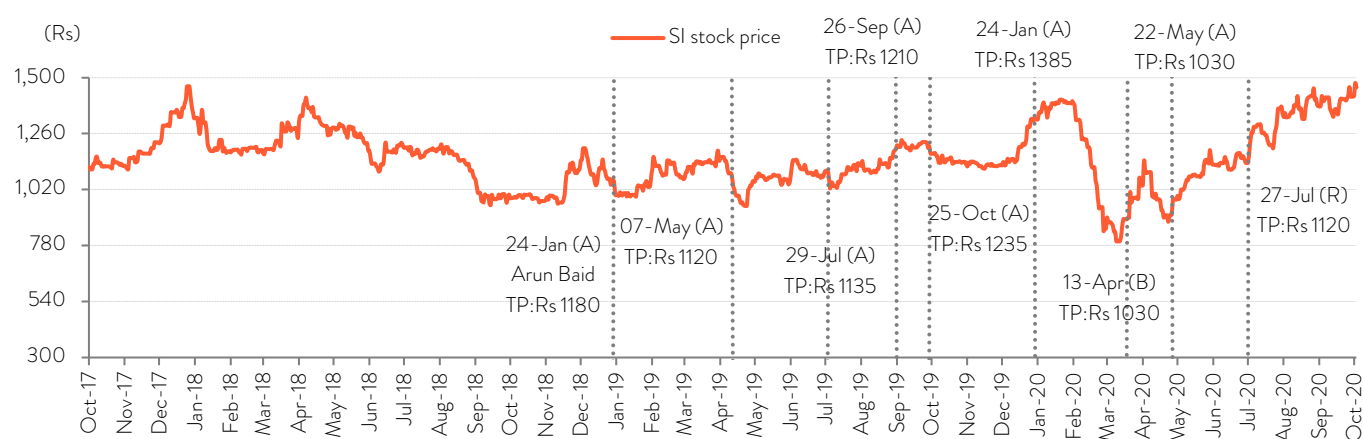
ADD – Expected return from >+5% to +15%

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): SUPREME INDUSTRIES (SI IN)



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

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