

**HOLD**

TP: Rs 260 | ▲ 6%

**V-GUARD INDUSTRIES**

Consumer Durables

03 February 2023

## Topline intact while margin pressure persists

- EBITDA margin deteriorated further to 6.7% in Q3; recovery on the anvil as high-cost inventory nearly exhausted
- Non-south market (+11% YoY) shored up the topline whereas core southern region declined on a high base
- We cut FY23 EPS by 23% but retain FY24 forecasts on expected margin recovery; on rollover, our TP rises to Rs 260 (vs. Rs 250)

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**Resilient topline:** VGRD's Q3FY23 topline at Rs 9.8bn (flat YoY/QoQ) was in line with our expectations as the non-south region grew 11% YoY. The fans vertical posted lower growth because the company operated at a low inventory of non-BEE-compliant fans which were preferred by channel partners. Management expects improved demand from March as the non-compliant stock gets exhausted at the channel level.

**Durables business outperforms:** The consumer durables vertical remained resilient (+5% YoY) amidst a tough demand environment, whereas the electronics division declined 4% YoY and electricals was largely flat. Working capital days reduced to 70 from 89 days in the preceding quarter.

**Margin contraction continues:** EBITDA margin deteriorated for the third straight quarter, falling to 6.7% in Q3 (-230bps YoY, -70bps QoQ), primarily due to the consumption of high-cost inventory. A tilt in product mix towards the durables business and incremental A&P spends (2.7% of sales vs. 1.7% last year) also exerted pressure on margins. Gross margin at 29.6% (+40bps QoQ) is guided to revert to pre-Covid levels led by the anticipated reduction in expensive inventory.

**Sunflame acquisition completed:** VGRD has completed the acquisition of Sunflame and has guided for a flat 9MFY23 performance, in line with other appliances players. Institutional business is likely to be affected due to GST slab alteration. Management expects to expand its kitchen business to non-southern regions given Sunflame's strong brand recall in the northern and western markets.

**Maintain HOLD:** While long-term growth levers are intact in the form of regional diversification, thrust on the high-growth durables business, and synergies from Sunflame, the near-term outlook is hindered by benign demand, slow margin recovery and higher competition. We cut FY23 EPS by 23% to bake in the Q3 print while maintaining FY24 estimates on expected margin recovery. We continue to value the stock at 35x FY24E EPS, in line with the 3Y average on 2Y fwd basis. On rolling valuations over to Dec'24E, our TP rises to Rs 260 (vs. Rs 250); retain HOLD.

## Key changes

Target	Rating
▲	◀ ▶

Ticker/Price	VGRD IN/Rs 246
Market cap	US\$ 1.3bn
Free float	44%
3M ADV	US\$ 0.8mn
52wk high/low	Rs 275/Rs 181
Promoter/FPI/DII	56%/13%/19%

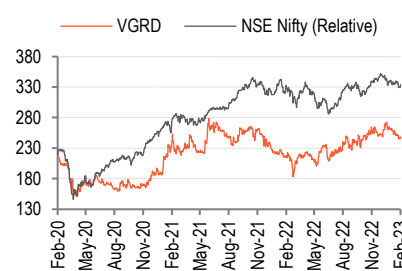
Source: NSE | Price as of 3 Feb 2023

## Key financials

Y/E 31 Mar	FY22A	FY23E	FY24E
Total revenue (Rs mn)	34,982	39,932	44,168
EBITDA (Rs mn)	3,382	3,140	4,595
Adj. net profit (Rs mn)	2,277	1,998	3,021
Adj. EPS (Rs)	5.3	4.6	7.0
Consensus EPS (Rs)	5.3	6.9	8.2
Adj. ROAE (%)	17.4	13.5	18.1
Adj. P/E (x)	46.6	53.2	35.2
EV/EBITDA (x)	31.4	33.8	23.1
Adj. EPS growth (%)	13.4	(12.3)	51.2

Source: Company, Bloomberg, BOBCAPS Research

## Stock performance



Source: NSE



**Fig 1 – Quarterly performance**

Particulars (Rs mn)	Q3FY23	Q3FY22	YoY (%)	Q2FY23	QoQ (%)	9MFY23	9MFY22	YoY (%)
Revenue	9,808	9,674	1.4	9,861	(0.5)	29,859	24,410	22.3
EBITDA	659	868	(24.1)	727	(9.4)	2,213	2,282	(3.1)
EBITDA Margin (%)	6.7	9.0	(230bps)	7.4	(70bps)	7.4	9.4	(190bps)
Depreciation	167	138	-	150	-	454	362	-
Interest	24	15	-	19	-	60	61	-
Other Income	60	27	-	33	-	138	81	-
PBT	528	742	(28.8)	592	(10.7)	1,837	1,940	(5.3)
Tax	136	203	-	155	-	473	551	-
Adjusted PAT	393	532	(26.1)	437	(10.0)	1,363	1,380	(1.2)
Exceptional item	-	-	-	0	-	-	-	-
Reported PAT	393	532	(26.1)	437	(10.0)	1,363	1,380	(1.3)
Adj. PAT Margin (%)	4.0	5.5	(150bps)	4.4	(40bps)	4.6	5.7	(110bps)
EPS (Rs)	0.9	1.2	(27.2)	1.0	(10.0)	3.2	3.2	(1.8)

Source: Company, BOBCAPS Research

**Fig 2 – Actual vs. Estimates**

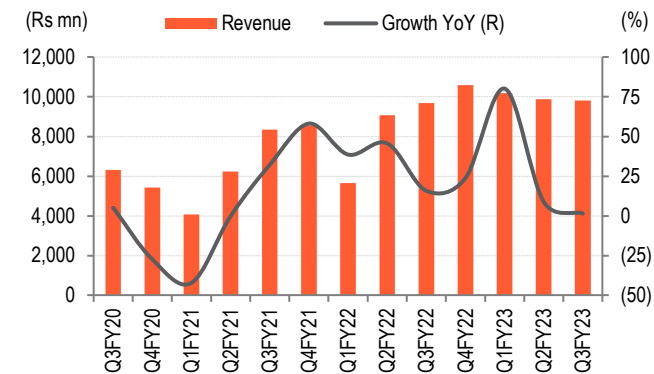
Particulars (Rs mn)	Actual	Estimates	Variance (%)
Revenue	9,808	9,680	1.3
EBITDA	659	929	(29.1)
EBITDA Margin (%)	6.7	9.6	(290bps)
Adj. PAT	393	618	(36.5)

Source: Company, BOBCAPS Research

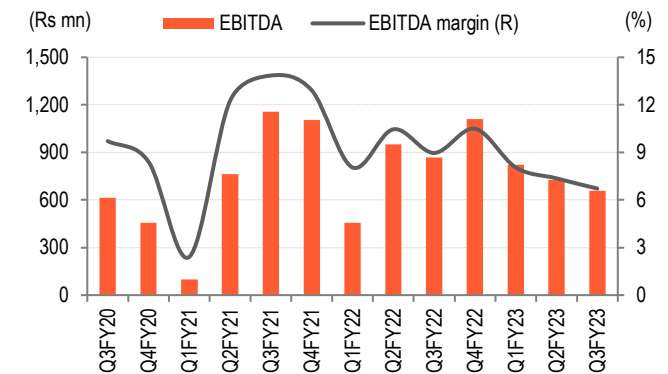
**Fig 3 – Segment-wise performance**

(Rs mn)	Q3FY20	Q4FY20	Q1FY21	Q2FY21	Q3FY21	Q4FY21	Q1FY22	Q2FY22	Q3FY22	Q4FY22	Q1FY23	Q2FY23	Q3FY23	3Y CAGR (%)
<b>Revenues</b>														
Consumer Durables	2,020	1,442	855	1,634	2,641	2,237	1,497	2,794	3,384	2,959	2,991	3,372	3,537	20.5
% of sales	32.0	26.6	21.0	26.2	31.6	26.2	26.5	30.8	35.0	28.0	29.4	34.2	36.1	-
Electricals	2,762	2,467	1,848	2,886	3,635	3,888	2,565	4,188	4,292	5,152	4,159	4,216	4,358	16.4
% of sales	43.7	45.6	45.3	46.3	43.5	45.5	45.4	46.2	44.4	48.7	40.8	42.8	44.4	-
Electronics	1,538	1,503	1,377	1,710	2,074	2,428	1,590	2,092	1,999	2,471	3,034	2,274	1,914	7.6
% of sales	24.3	27.8	33.7	27.4	24.8	28.4	28.1	23.1	20.7	23.4	29.8	23.1	19.5	-
<b>EBIT</b>														
Consumer Durables	113	35	(87)	136	264	89	(59)	85	96	50	38	97	(45)	(173.4)
Margin (%)	5.6	2.5	(10.2)	8.3	10.0	4.0	(3.9)	3.0	2.8	1.7	1.3	2.9	(1.3)	-
Electricals	229	192	59	287	331	427	254	421	355	555	283	228	397	20.2
Margin (%)	8.3	7.8	3.2	9.9	9.1	11.0	9.9	10.1	8.3	10.8	6.8	5.4	9.1	-
Electronics	244	213	93	306	512	531	207	392	338	431	429	333	222	(3.2)
Margin (%)	15.9	14.1	6.8	17.9	24.7	21.9	13.0	18.7	16.9	17.4	14.1	14.6	11.6	-

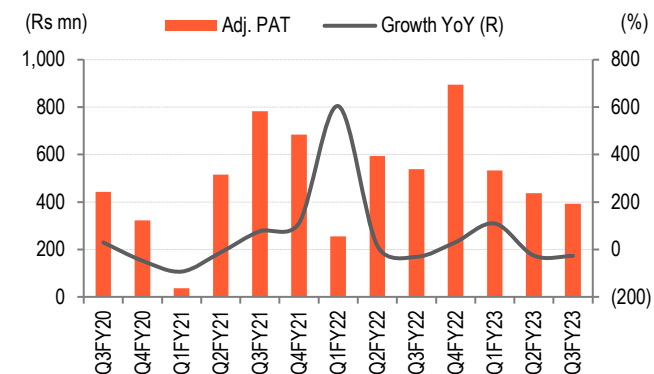
Source: Company, BOBCAPS Research

**Fig 4 – Topline remained intact...**

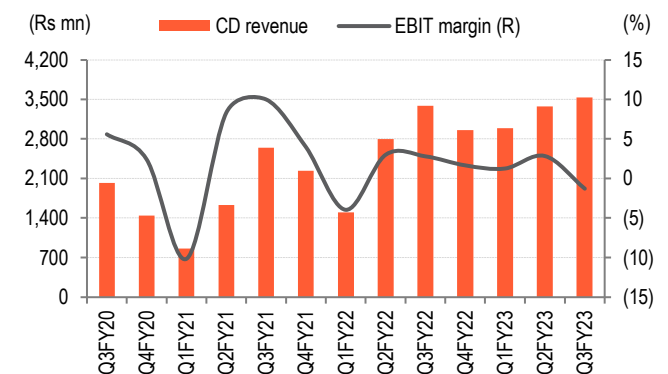
Source: Company, BOBCAPS Research

**Fig 5 – ...while margins deteriorated**

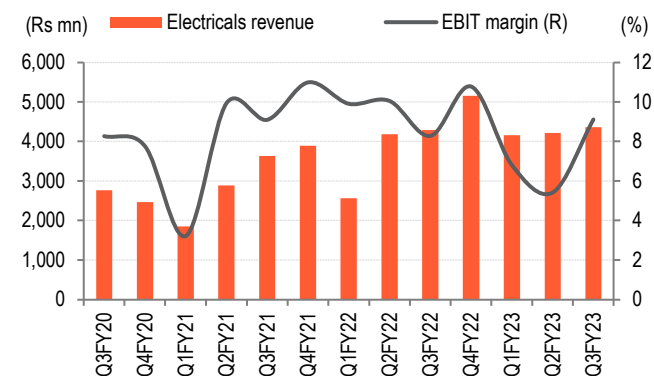
Source: Company, BOBCAPS Research

**Fig 6 – PAT posted a decline**

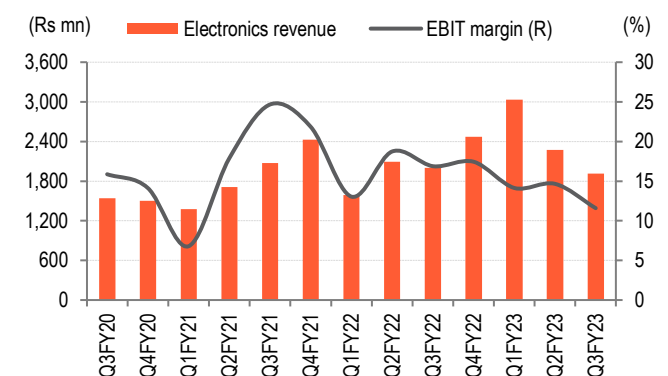
Source: Company, BOBCAPS Research

**Fig 7 – Consumer durables (CD) business resilient**

Source: Company, BOBCAPS Research

**Fig 8 – Electricals business saw margin expansion**

Source: Company, BOBCAPS Research

**Fig 9 – Electronics business remained weak**

Source: Company, BOBCAPS Research

## Earning call highlights

- **Demand:** VGRD's sales in its core southern market declined 5% YoY in Q3FY23 (+15% in FY23 YTD) on account of a high base of last year. Also, given its relatively higher market share for most products, achieving incremental growth is a challenge in the current low demand environment.
- **Pricing:** Margins for most industry players have remained under pressure over the last few quarters, and management sees little scope for price cuts to boost demand.
- **Gross margin:** Management anticipates continued gross margin expansion with a return to pre-Covid levels of 32-34% as high-cost inventory is fully absorbed. In-house manufacturing is expected to further bolster gross margins in due course.
- **Inventory:** VGRD has cleared the high-cost inventory for most of its product portfolio, barring water heaters which will take a couple of quarters more.
- **Fans:** Volume growth in fans was muted at in Q3 as the company had a low inventory of non-compliant fans which were being pushed by channel partners ahead of the new Bureau of Energy Efficiency (BEE) norms. Peers with higher stocks of non-compliant fans, thus, posted stronger sales during the quarter. The company expects upward price revisions of 6-8% overall in fans, which includes relatively higher hikes for the premium segment (in double-digits for some products) and lower hikes in economy fans.
- **Pumps:** The pumps business remained under pressure, more so in the agricultural segment than in residential pumps, as lean demand triggered competitive pricing action by peers. The upcoming summer season could be a potential demand catalyst.
- **Sunflame:** The subsidiary's 9MFY23 numbers are largely flat (down 2-3% vs. the year-ago quarter). The institutional business was affected during the period due to GST slab alteration. Additionally, the company has a large chimney business which is likely to be adversely impacted following the budgetary announcement of a 7.5% customs duty hike on electric kitchen chimneys. Management believes the impact will be transient in nature as Sunflame is establishing a manufacturing facility which could offset imports and is targeted to be commissioned in H2FY24.

Sunflame's Faridabad facility is only 50% utilised and the same is true for its Baddi plant; hence, there is no further capex requirement in the subsidiary for the next 2-3 years. The Sunflame acquisition was funded via debt of ~Rs 2.8bn (at ~9% interest) and internal accruals for the balance Rs 4bn.

## Valuation methodology

While long-term growth levers are intact in the form of regional diversification, thrust on the high-growth durables business, and synergies from Sunflame, the near-term outlook is hindered by benign demand, slow margin recovery and higher competition.

We cut FY23 EPS by 23% to bake in the Q3FY23 print while maintaining FY24 estimates on expected margin recovery. We continue to value the stock at 35x FY24E EPS, in line with the three-year average on two-year forward basis. On rolling valuations over to Dec'24E, our TP rises to Rs 260 (vs. Rs 250); retain HOLD.

**Fig 10 – Revised estimates**

(Rs mn)	New			Old			Change (%)		
	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E
Sales	39,932	44,168	49,878	40,013	44,258	49,978	(0.2)	(0.2)	(0.2)
EBITDA	3,140	4,595	5,151	3,992	4,611	5,169	(21.4)	(0.3)	(0.3)
PAT	1,998	3,021	3,329	2,588	2,990	3,296	(22.8)	1.0	1.0
EPS (Rs)	4.6	7.0	7.7	6.0	6.9	7.6	(22.8)	1.0	1.0
EBITDA Margin (%)	7.9	10.4	10.3	10.0	10.4	10.3	(210bps)	0bps	0bps

Source: Company, BOBCAPS Research

## Key risks

Key risks to our estimates are:

- **Upside risks:** Above-expected market share gains in non-core northern regions
- **Downside risks:** Intensifying competition in the kitchen appliances segment, resulting in lower-than-expected synergetic benefits from the Sunflame acquisition

## Sector recommendation snapshot

Company	Ticker	Market Cap (US\$ bn)	Price (Rs)	Target (Rs)	Rating
Amber Enterprises	AMBER IN	0.8	1,899	2,100	HOLD
Blue Star	BLSTR IN	1.6	1,358	1,450	BUY
Crompton Greaves	CROMPTON IN	2.4	305	440	BUY
Dixon Technologies	DIXON IN	2.0	2,755	4,100	BUY
Havells India	HAVL IN	9.2	1,197	1,500	BUY
KEI Industries	KEII IN	1.9	1,678	1,900	BUY
Orient Electric	ORIENTEL IN	0.7	283	290	HOLD
Polycab India	POLYCAB IN	5.4	2,949	3,300	BUY
Syrma SGS	SYRMA IN	0.5	253	390	BUY
V-Guard Industries	VGRD IN	1.3	246	260	HOLD
Voltas	VOLT IN	3.3	813	950	HOLD

Source: BOBCAPS Research, NSE | Price as of 3 Feb 2023

## Financials

### Income Statement

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23E	FY24E	FY25E
<b>Total revenue</b>	<b>27,212</b>	<b>34,982</b>	<b>39,932</b>	<b>44,168</b>	<b>49,878</b>
EBITDA	3,121	3,382	3,140	4,595	5,151
Depreciation	386	491	623	753	917
EBIT	2,735	2,891	2,517	3,842	4,234
Net interest inc./(exp.)	(61)	(79)	(48)	(25)	(25)
Other inc./(exp.)	207	128	192	211	232
Exceptional items	0	0	0	0	0
EBT	2,881	2,940	2,661	4,028	4,441
Income taxes	862	655	670	1,015	1,119
Extraordinary items	0	0	0	0	0
Min. int./Inc. from assoc.	0	0	0	0	0
<b>Reported net profit</b>	<b>2,008</b>	<b>2,277</b>	<b>1,998</b>	<b>3,021</b>	<b>3,329</b>
Adjustments	0	0	0	0	0
<b>Adjusted net profit</b>	<b>2,008</b>	<b>2,277</b>	<b>1,998</b>	<b>3,021</b>	<b>3,329</b>

### Balance Sheet

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23E	FY24E	FY25E
Accounts payables	4,747	4,880	6,017	6,656	7,516
Other current liabilities	1,050	1,166	1,331	1,473	1,663
Provisions	0	0	0	0	0
Debt funds	130	118	250	250	250
Other liabilities	710	732	828	910	1,021
Equity capital	430	432	432	432	432
Reserves & surplus	11,683	13,638	15,075	17,448	20,043
Shareholders' fund	12,113	14,070	15,506	17,879	20,475
<b>Total liab. and equities</b>	<b>18,750</b>	<b>20,966</b>	<b>23,933</b>	<b>27,168</b>	<b>30,925</b>
Cash and cash eq.	2,812	613	839	1,952	2,599
Accounts receivables	3,881	4,841	5,689	6,292	7,106
Inventories	6,315	8,596	9,846	10,891	12,299
Other current assets	1,003	1,152	1,315	1,454	1,642
Investments	0	0	0	0	0
Net fixed assets	3,913	4,842	5,219	5,466	6,049
CWIP	185	92	104	116	130
Intangible assets	129	200	200	200	200
Deferred tax assets, net	0	0	0	0	0
Other assets	513	631	721	797	900
<b>Total assets</b>	<b>18,750</b>	<b>20,966</b>	<b>23,933</b>	<b>27,168</b>	<b>30,925</b>

### Cash Flows

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23E	FY24E	FY25E
<b>Cash flow from operations</b>	<b>3,695</b>	<b>1,390</b>	<b>1,662</b>	<b>2,765</b>	<b>2,888</b>
Capital expenditures	0	0	(1,000)	(1,000)	(1,500)
Change in investments	26	0	0	0	0
Other investing cash flows	383	(1,198)	(6)	(5)	(7)
<b>Cash flow from investing</b>	<b>409</b>	<b>(1,198)</b>	<b>(1,006)</b>	<b>(1,005)</b>	<b>(1,507)</b>
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	2	(12)	132	0	0
Interest expenses	0	0	0	0	0
Dividends paid	(60)	(603)	(561)	(647)	(734)
Other financing cash flows	0	0	0	0	0
<b>Cash flow from financing</b>	<b>(58)</b>	<b>(615)</b>	<b>(429)</b>	<b>(647)</b>	<b>(734)</b>
<b>Chg in cash &amp; cash eq.</b>	<b>4,047</b>	<b>(423)</b>	<b>227</b>	<b>1,112</b>	<b>647</b>
<b>Closing cash &amp; cash eq.</b>	<b>2,812</b>	<b>613</b>	<b>839</b>	<b>1,952</b>	<b>2,599</b>

### Per Share

Y/E 31 Mar (Rs)	FY21A	FY22A	FY23E	FY24E	FY25E
Reported EPS	4.7	5.3	4.6	7.0	7.7
Adjusted EPS	4.7	5.3	4.6	7.0	7.7
Dividend per share	1.2	1.3	1.3	1.5	1.7
Book value per share	28.1	32.6	35.9	41.4	47.4

### Valuations Ratios

Y/E 31 Mar (x)	FY21A	FY22A	FY23E	FY24E	FY25E
EV/Sales	3.9	3.0	2.7	2.4	2.1
EV/EBITDA	34.0	31.4	33.8	23.1	20.6
Adjusted P/E	52.9	46.6	53.2	35.2	31.9
P/BV	8.8	7.5	6.8	5.9	5.2

### DuPont Analysis

Y/E 31 Mar (%)	FY21A	FY22A	FY23E	FY24E	FY25E
Tax burden (Net profit/PBT)	69.7	77.5	75.1	75.0	75.0
Interest burden (PBT/EBIT)	105.3	101.7	105.7	104.8	104.9
EBIT margin (EBIT/Revenue)	10.0	8.3	6.3	8.7	8.5
Asset turnover (Rev./Avg TA)	7.0	7.2	7.7	8.1	8.2
Leverage (Avg TA/Avg Equity)	0.4	0.4	0.4	0.3	0.3
Adjusted ROAE	18.2	17.4	13.5	18.1	17.4

### Ratio Analysis

Y/E 31 Mar	FY21A	FY22A	FY23E	FY24E	FY25E
<b>YoY growth (%)</b>					
Revenue	8.7	28.6	14.2	10.6	12.9
EBITDA	21.0	8.4	(7.2)	46.4	12.1
Adjusted EPS	7.3	13.4	(12.3)	51.2	10.2
<b>Profitability &amp; Return ratios (%)</b>					
EBITDA margin	11.5	9.7	7.9	10.4	10.3
EBIT margin	10.0	8.3	6.3	8.7	8.5
Adjusted profit margin	7.4	6.5	5.0	6.8	6.7
Adjusted ROAE	18.2	17.4	13.5	18.1	17.4
ROCE	18.3	17.6	13.5	17.9	17.2

### Working capital days (days)

Receivables	52	51	52	52	52
Inventory	85	90	90	90	90
Payables	64	51	55	55	55

### Ratios (x)

Gross asset turnover	6.5	6.1	5.8	5.6	5.4
Current ratio	2.4	2.5	2.3	2.5	2.5
Net interest coverage ratio	44.8	36.7	53.0	153.7	169.4
Adjusted debt/equity	0.0	0.0	0.0	0.0	0.0

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%

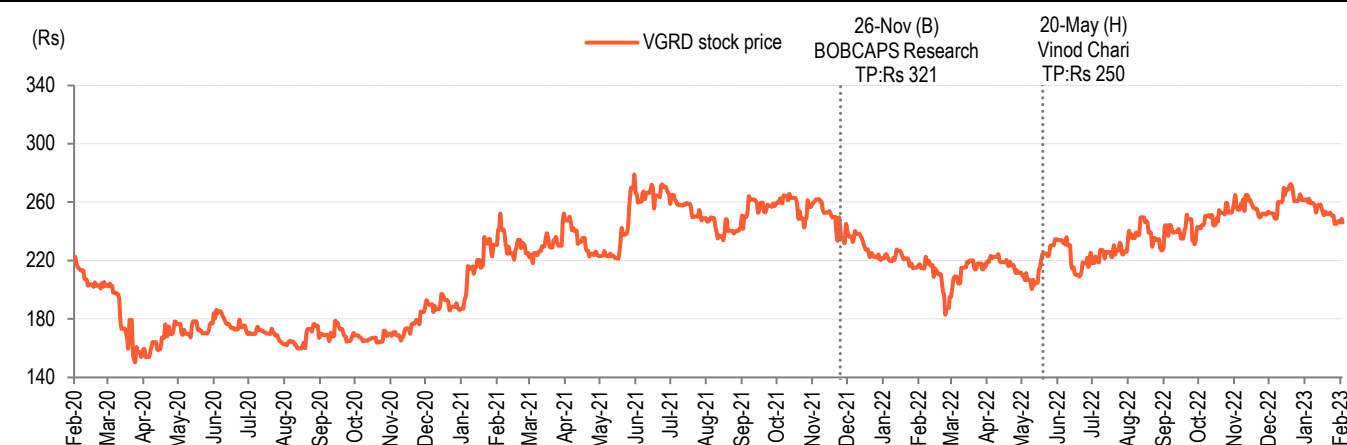
**HOLD** – Expected return from -6% to +15%

**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): V-GUARD INDUSTRIES (VGRD IN)



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

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