CGSCIMB

Sector Note

INITIATION

InCred

Industrial - Overall

Strong tailwinds for an FMEG upcycle

- Large electrical companies are beneficiaries of improving housing & infrastructure capex and market share shift to organised players
- Deepening distribution network, branding spends, use of technology for product innovation and improving business economics are key growth levers.
- Initiate sector coverage with Overweight rating, upside potential of ~10-30%.

Demand drivers for electrical products point to recovery

Industrial/consumer electrical product demand is driven by government and private capex, demand for urban/rural real estate/housing, consumer aspirations and general increase in affordability standards. Poor economic growth over FY17-20 impacted these demand drivers that resulted into low corporate revenue/profit growth. The Indian government's thrust on infrastructure spending, recovery in urban real estate and strong rural demand are key structural demand trends going forward, in our view.

Market leaders have clear advantage over their smaller counterparts

Large organised electrical companies have gained significant revenue market share at the cost of their unorganised smaller counterparts over the past decade (Figure 16). COVID-19 pandemic disrupted supply chains of small players and it further benefitted incumbents. Proactive large companies have invested into brand awareness, deepening network penetration in tier-2/-3 markets and launching new-age products using artificial intelligence (AI)/Internet of Things (IoT). We believe large players have a clear advantage over their smaller counterparts and will grow faster going forward.

Share of B2C products increasing across our coverage universe

Electrical companies have been increasing their B2C revenue share gradually over the past few years. Higher B2C sales reduces business cyclicality, aids brand recall, improves pricing power and helps in overall better business economics. Improving revenue mix would aid operating profitability and improve working capital cycles, in our view. Most of our coverage universe in the electrical industry have net cash balance sheets with high return ratios and we estimate healthy FCF generation over FY21-23F.

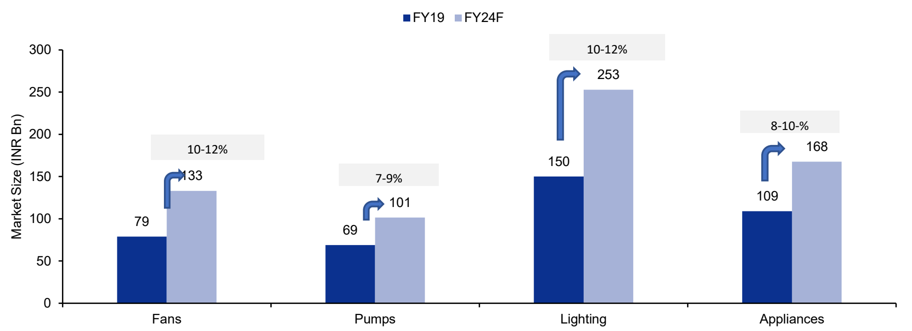
Valuation and risks

Capex recovery, high B2C revenue mix, wider distribution reach and improving balance sheets are factors that make us bullish. We expect P/E re-rating possibilities for C&W companies building their FMEG presence, while others to sustain their premium valuation multiples given sector uptrends. The stocks trade at P/E and EV/EBITDA of 10-50x and 6-33x our FY23F estimates. Downside risks: Pricing disruption by new entrants, delays in new product launches, slow ramp-up of dealer/retail touchpoint networks and adverse metal prices or forex rates.

Initiate with sector Overweight rating, upside of ~10-30%

We have Add ratings on Havells/Crompton with target price of Rs1,231/Rs465 respectively. Within the C&W players, we have Add ratings on Polycab/KEI with target prices of Rs1530/Rs645 respectively and expect them to re-rate further as they build their B2C franchises. We also initiate with Add ratings on Orient Electric, V-Guard and Finolex Cables with TPs of Rs328/Rs277/Rs504 respectively.

Figure 1: Consumer electricals presents a Rs400bn (2019) market opportunity, growing at 8-11% CAGR over FY19-24F



SOURCES: CROMPTON GREAVES (CG) CONSUMER CORPORATE PRESENTATION, EIP RESEARCH

India

Overweight *(Initiating coverage)*

Highlighted Companies

Havells India Ltd

ADD, TP Rs1231, Rs1103 close

Havells will continue to benefit from the upswing in the consumer electrical and appliances segment, in our view. Market share gains, operating leverage and improving Lloyd profitability are key stock catalysts going forward, in our view.

Polycab India Ltd.

ADD, TP Rs1530, Rs1360 close

Superior FMEG performance and dominant market position in the C&W market are Polycab's key strengths. Higher B2C share and its emergence as a national FMEG brand will drive re-rating, in our view.

KEI Industries Ltd

ADD, TP Rs645, Rs495 close

The business is improving on all counts – higher B2C mix, stable EBITDA margins, reducing EPC revenue, low net debt-to-equity and high RoE/RoCE over FY21-23F

Summary Valuation Metrics

P/E (x)	Mar21-F	Mar22-F	Mar23-F
Havells India Ltd	67.82	58.15	49.3
Polycab India Ltd.	23.37	24.02	21.32
KEI Industries Ltd	16.37	12.75	10.73

P/BV (x)	Mar21-F	Mar22-F	Mar23-F
Havells India Ltd	13.76	11.78	10.03
Polycab India Ltd.	4.42	3.84	3.35
KEI Industries Ltd	2.52	2.14	1.82

Dividend Yield	Mar21-F	Mar22-F	Mar23-F
Havells India Ltd	0.45%	0.5%	0.54%
Polycab India Ltd.	0.55%	0.81%	0.88%
KEI Industries Ltd	0.4%	0.81%	0.89%

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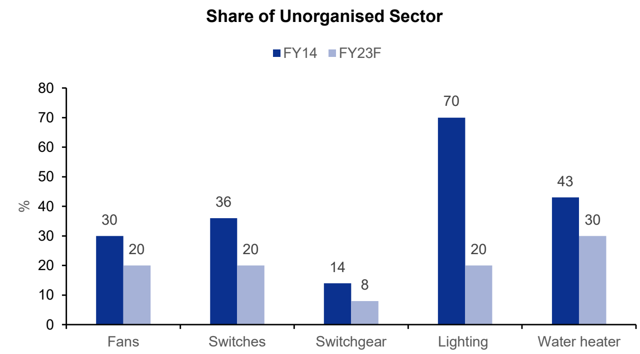
KEY CHARTS

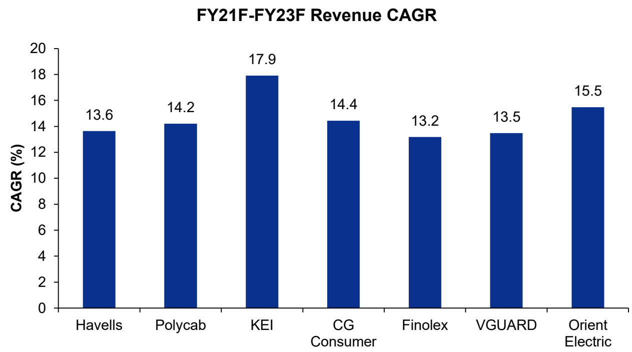
Unorganised players will continue to lose market share going forward

The Indian FMEG industry is gradually moving from a largely unorganised sector, comprising smaller regional players, towards an organised sector comprising pan-India branded market players across the categories. An increase in technological and product complexities, an increase in marketing and branding activities and the entry of newer players have all led to an increase in the proportion of the industry's revenue generated by the organised sector, in our view.



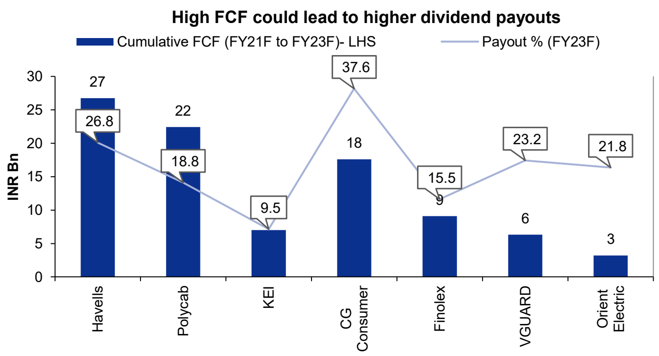
Most of our consumer electrical coverage universe to have double-digits revenue CAGR over FY21-23F

We expect KEI to grow revenue the fastest among our coverage companies, followed by Orient and Crompton. Havells and Polycab too will have revenue CAGR of 13.5-14.5% over FY21F-23F even on a much larger revenue base vs their peers.



High FCF generation could lead to higher dividend payouts

All of our coverage companies are net cash with estimated FCF generation of Rs3bn-30bn over FY21-23F. As these businesses accumulate more cash, we expect companies like KEI, V-Guard and Finolex Cables to step up their dividend payouts in case there are no meaningful reinvestment opportunities in the business.



Jul-Dec 2020 business recovery led to high stock prices

Our coverage companies reported solid financial performance in the 2Q and 3QFY21 on the back of festival season, pent-up demand, recovery in urban real estate and higher spends on home improvement. The stock prices have reacted equally with stocks trading at closer to their five-year mean P/E or +1SD to mean P/E.

	CMP	TP	P/E -2SD	P/E -1SD	P/E Mean (5 Yrs)*	P/E +1SD	P/E +2SD	FY23F P/E
Havells	1,103	1,231	22	32	42	52	62	49
Polycab	1,360	1,530	8	12	15	19	22	21
KEI	495	645	5	9	12	15	19	11
Crompton Consumer	410	465	23	29	34	39	44	35
Finolex Cables	403	504	6	12	17	23	28	11
V-Guard	230	277	26	36	46	57	67	36
Orient Electric	295	328	30	35	39	44	49	41

SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 2: Peer comparisons

Company Name	Bblg ticker	Rating	Market cap	Closing price	Target price	Upside (%)	P/E (x)		EV/EBITDA (x)		CAGR % (FY21-23F)		FY23F	
			US$m	Rs/share	Rs/share		FY22F	FY23F	FY22F	FY23F	Revenue	EPS	RoE (%)	RoCE (%)
Havells India Ltd	HAVL IN	ADD	9,487	1,103	1,231	11.6	58.2	49.3	38.7	32.8	13.6	17.3	22.0	27.5
Polycab India Ltd.	POLYCAB IN	ADD	2,785	1,360	1,530	12.6	24.0	21.3	14.8	12.9	14.2	4.7	16.8	21.6
KEI Industries Ltd	KEII IN	ADD	611	495	645	30.5	12.7	10.7	7.7	6.2	17.9	23.5	18.3	24.4
Crompton Greaves Consumer Electrical Ltd	CROMPTON IN	ADD	3,537	410	465	13.3	42.3	35.3	31.4	26.4	14.4	20.2	31.9	41.3
Finolex Cables Ltd	FNXC IN	ADD	846	403	504	25.1	12.6	11.4	8.6	7.0	13.2	16.0	13.6	14.4
V-Guard Industries Ltd	VGRD IN	ADD	1,356	230	277	20.4	40.9	35.7	26.9	23.4	13.5	18.2	19.2	25.5
Orient Electric Ltd	ORIENTEL IN	ADD	860	295	328	11.1	46.7	40.5	25.7	21.9	15.5	20.7	25.3	34.3
Voltas Ltd	VOLT IN	HOLD	4,786	1,053	1,070	1.6	44.7	36.0	34.2	27.4	20.2	42.1	17.8	19.9
Blue Star Ltd	BLSTR IN	NR	1,250	945	NA	NA	46.0	35.5	25.5	21.1	22.3	62.1	17.3	31.5
Whirlpool of India Ltd	WHIRL IN	NR	4,200	2,410	NA	NA	50.4	41.5	34.9	29.4	17.8	42.1	20.8	23.9
Amber Enterprises India Ltd	AMBER IN	NR	1,580	3,413	NA	NA	51.9	38.1	28.2	22.0	38.7	87.1	15.0	19.7
Dixon Technologies India Ltd	DIXON IN	NR	3,323	20,647	NA	NA	74.4	54.6	47.0	35.6	54.9	61.2	26.2	28.8
Dabur India Ltd	DABUR IN	ADD	12,710	523	586	11.9	44.8	40.0	36.9	32.9	12.3	12.2	24.7	28.6
Marico Ltd	MRCO IN	ADD	6,988	394	480	21.9	38.6	34.5	27.4	24.5	11.3	13.3	38.6	43.9
Johnson Controls-Hitachi Air Conditioning India Ltd	JCHAC IN	NR	1,013	2,711	NA	NA	59.1	39.9	31.7	23.9	25.2	79.2	12.8	13.0
IFB Industries Ltd	IFBI IN	NR	611	1,098	NA	NA	29.2	22.6	13.0	11.0	26.7	54.1	4.3	4.9

NR: NOT RATED ARE BLOOMBERG CONSENSUS ESTIMATES.
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS, BLOOMBERG. PRICED AS AT 12 MAR 2021

Strong tailwinds for an FMEG upcycle

Electrical product demand drivers point to recovery

Cables and wires industry

- **Investments in Infrastructure:** The Indian government announced an Rs111 lakh crore investment plan under the NIP scheme over FY20 to FY25 with the focus on Energy (24%), Roads (18%), Railways (12%) and Urban Infra (17%) constituting 70% of the aggregate spend. This will drive demand from capacity increase in electricity transmission / distribution & renewable energy generation, investment in ramping up urban infrastructure under the smart city mission and demand for residential infrastructure driven by the Affordable Housing Scheme and the government's agenda of housing for all.
- **Nuclearisation:** Growing nuclearisation of families will likely create demand for residential real estate, directly generating demand for cables and wires.
- **Incremental Adoption of Electrical Energy:** Adoption of renewable sources of energy and the shift to electricity as primary fuel in commercial operations as well, will catalyse demand for cables and wires (C&Ws).

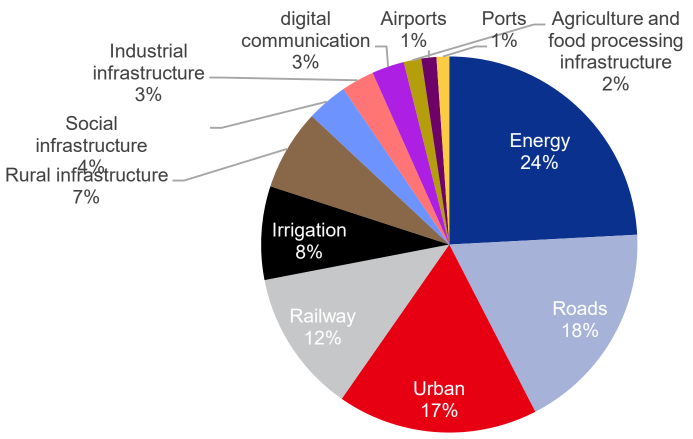
Fast Moving Electrical Goods (FMEG)

- **Electricity Penetration:** There has been a committed effort by the Indian government to make electricity available across the country.
- **Affluence:** Rising per capita Net National Income (NNI) and Private Final Consumption Expenditure (PFCE) are enabling higher demand for FMEG products across the country.
- **Convenience:** Convenience is the demand of the 21st century. The dual feature of convenience and low-ticket size of FMEG products make them well placed to gain penetration.

Government capex on infrastructure development

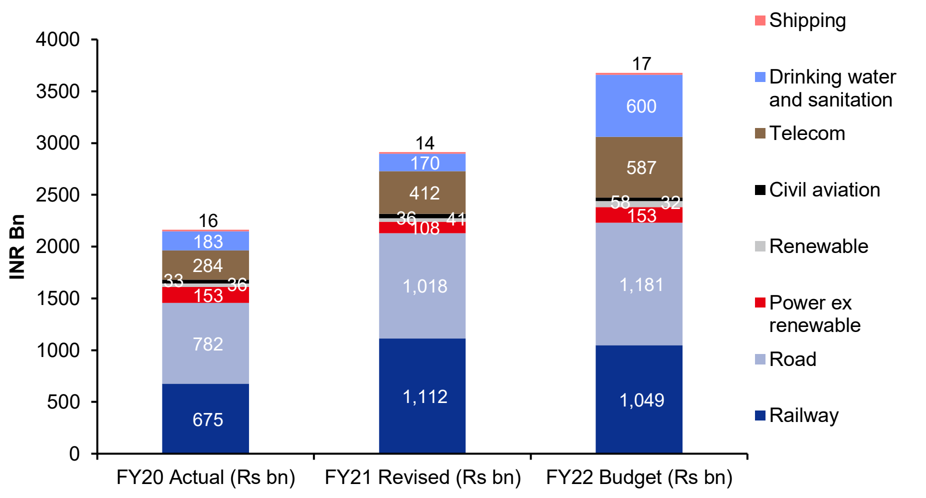
The government has an ambitious Rs111 lakh crore plan (National Infrastructure Pipeline) to ramp up urban and rural infrastructure.

Figure 3: 70% of government capex of Rs111 lakh crore for Infra Development under NIP allocated towards energy, roads, railways and urban infrastructure (FY20-FY25F)



SOURCES: DEPARTMENT OF ECONOMIC AFFAIRS (GOVERNMENT OF INDIA), EIP RESEARCH

Figure 4: Government spends on infrastructure



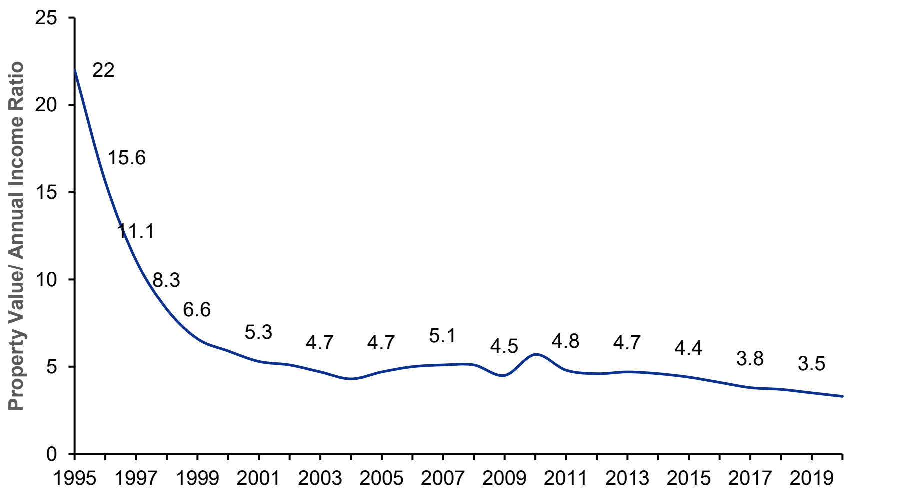
SOURCES: BUDGET DOCUMENTS, EIP RESEARCH

Recovery in real estate and housing market

Improving real estate affordability (property prices/annual income) is driving the recovery in housing market.

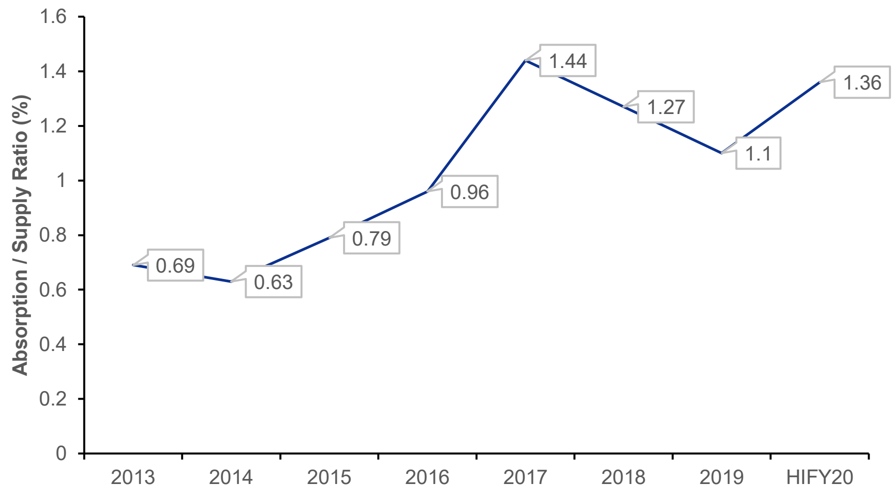
Channel checks and industry data from companies in cement, paints, building materials & housing finance companies suggest strong pick-up in individual home consumption. Real estate inventory has been consumed both in urban metros and in tier-2/-3 cities and small towns.

Figure 5: Improving real estate affordability (property prices/annual income) is driving the recovery in housing market



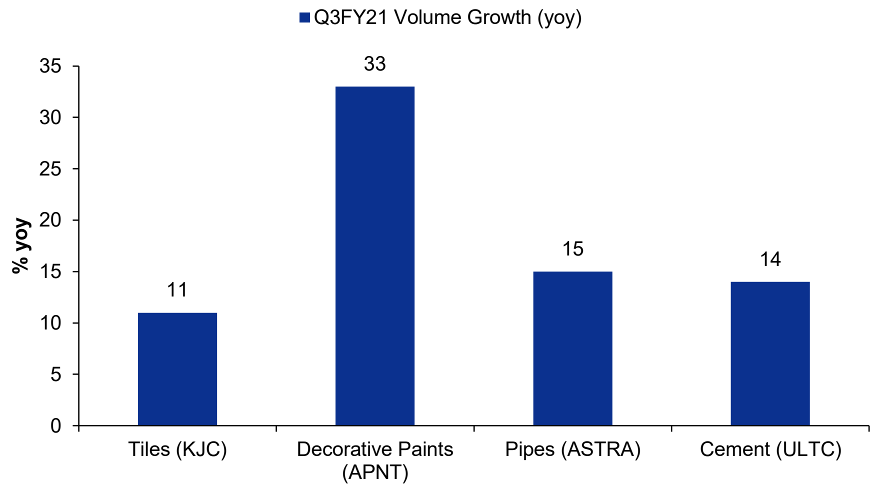
SOURCES: HOUSING DEVELOPMENT FINANCE CORPORATION (HDFC), EIP RESEARCH

Figure 6: Improving real estate absorption to supply ratio trend (top 7 cities in India in terms of population) indicates improved demand



SOURCES: FEDERATION OF INDIAN CHAMBERS OF COMMERCE & INDUSTRY (FICCI), EIP RESEARCH

Figure 7: Housing related sectors have shown uptick in customer demand in 3QFY21



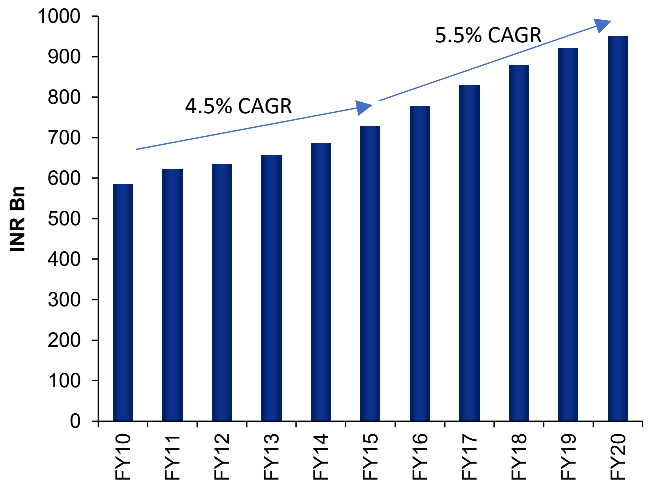
KJC IS KAJARIA CERAMICS, APNT IS ASIAN PAINTS, ASTRA IS ASTRAL PIPES, ULTC IS ULTRATECH CEMENT
SOURCES: EIP RESEARCH, COMPANY REPORTS

Improving consumer affordability

Rising discretionary spends and evolving household profiles are driving up demand for the FMEG segment.

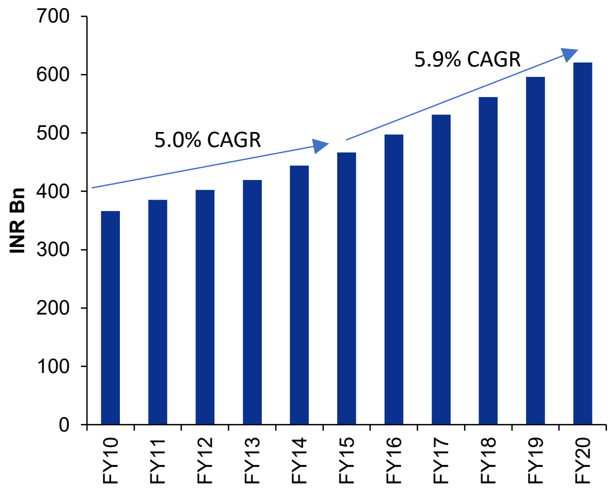
Per capita private final consumption expenditure (PFCE) growth has exceeded per capita Net National Income (NNI) over the past five years (Reserve Bank of India) indicating consumption is increasing with rising affluence. This is driving up discretionary spending and signaling consistent improvement in demand for consumer electrical products and services.

Figure 8: Per capita NNI growth accelerated over the past 5 years



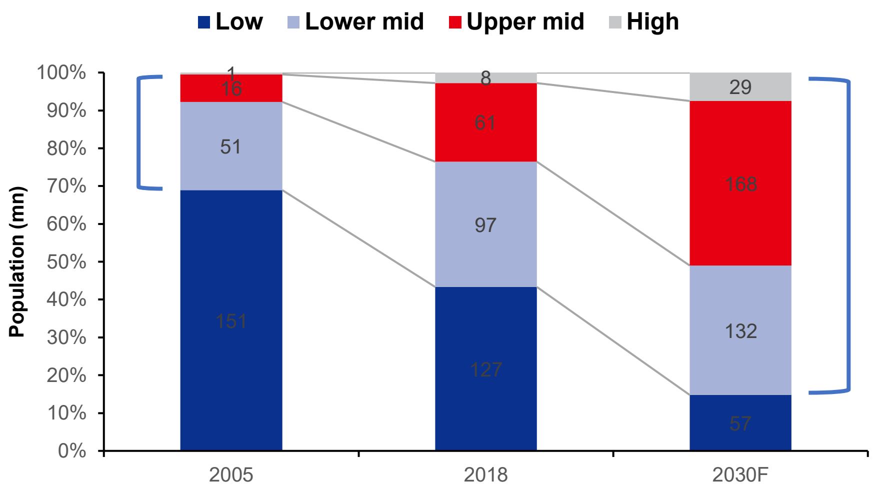
SOURCES: RESERVE BANK OF INDIA (RBI), EIP RESEARCH

Figure 9: PFCE continued to grow faster, indicating higher discretionary spending



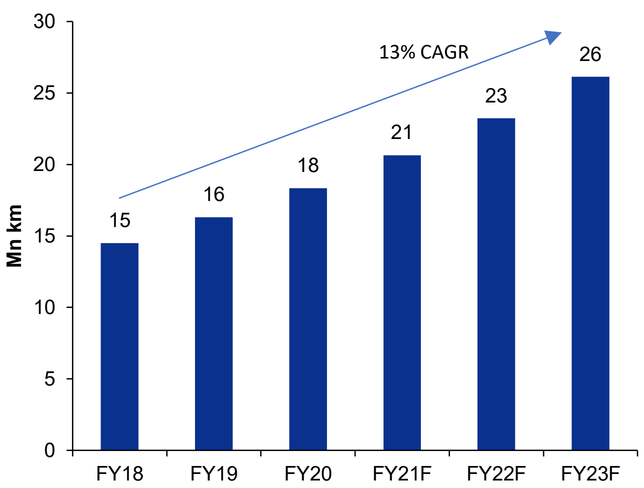
SOURCES: RBI, EIP RESEARCH

Figure 10: Addressable population (lower mid, upper mid and high-income households) are expected to double from 166m in 2018 to 329m by 2030F



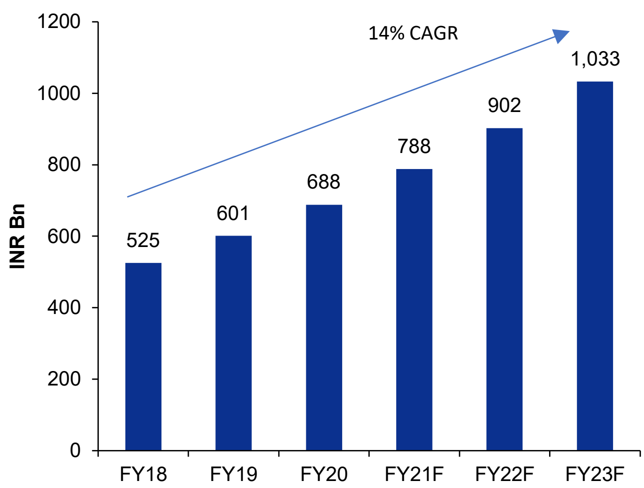
SOURCES: TATA CONSUMER ANNUAL REPORT (FY20), EIP RESEARCH

Figure 11: Cables and wires volume growth



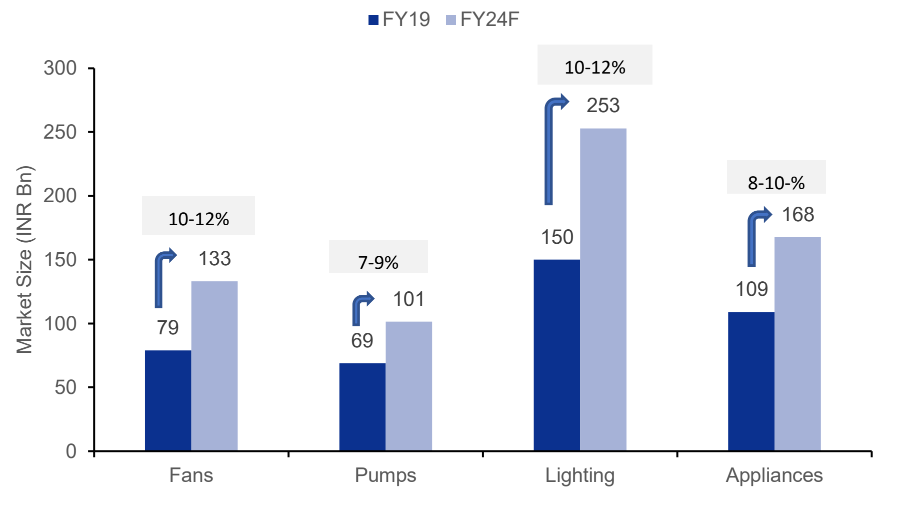
SOURCES: POLYCAB ESTIMATES, EIP RESEARCH

Figure 12: Cables and wires value growth



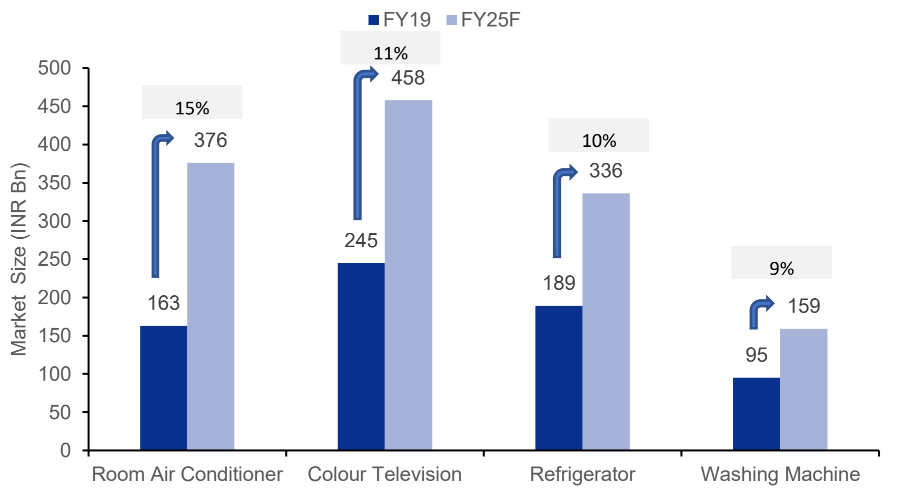
SOURCES: POLYCAB ESTIMATES, EIP RESEARCH

Figure 13: Consumer electricals is a Rs400bn (2019) market opportunity, growing at 8-11% CAGR



SOURCES: CROMPTON GREAVES (CG) CONSUMER CORPORATE PRESENTATION, EIP RESEARCH

Figure 14: White goods will also see high growth given same demand drivers as FMEG



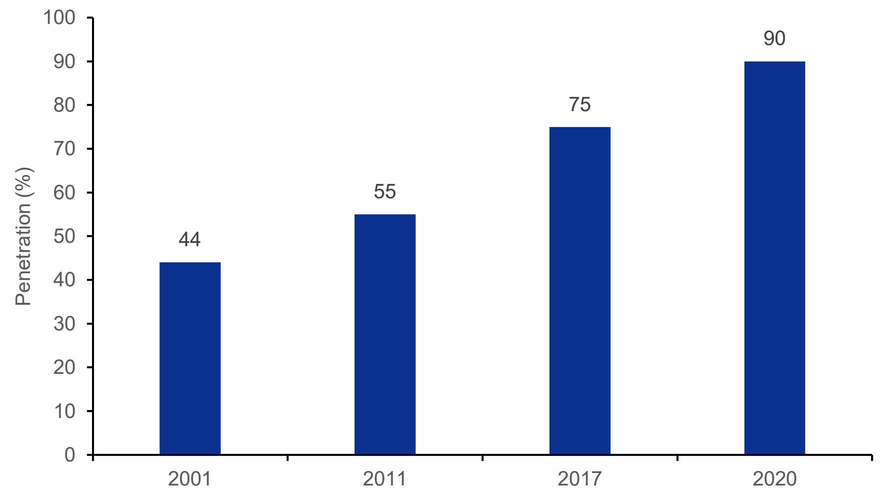
SOURCES: CG CONSUMER CORPORATE PRESENTATION, EIP RESEARCH

Rising electricity penetration

Rural electrification coupled with rising rural income will drive demand for FMEG.

Rural electrification penetration increased from 44% in 2001 to 90% in 2020 (Statista), increasing the addressable market for both cables & wires and FMEG.

Figure 15: Rural electrification penetration was 90% in 2020



SOURCES: STATISTA, EIP RESEARCH,

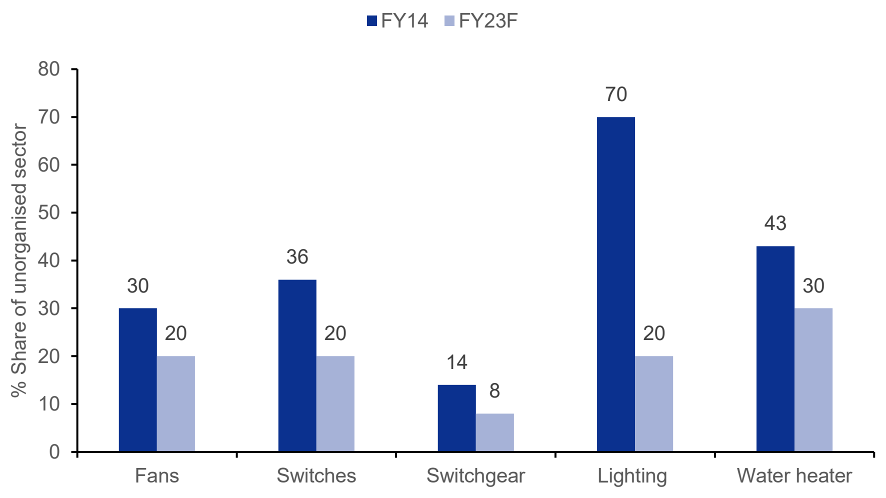
Market leaders have advantage over unorganised counterparts

Unorganised sector losing share to organised sector

Better brand visibility, deepening distribution network, investment in R&D and rising consumer aspirations are catalysing consumption shift to the organised sector.

Better brand visibility, deepening distribution network, investment in R&D and rising consumer aspirations are catalysing consumption shift from the unorganised to the organised sector. We notice the same trend in FMEG and expect it to continue enabling market share gains for organised players investing in brand and distribution network development.

Figure 16: Unorganised share has lost market share across FMEG products



SOURCES: POLYCAB 1QFY20 PRESENTATION, EIP RESEARCH

Better brand visibility and improving distribution network

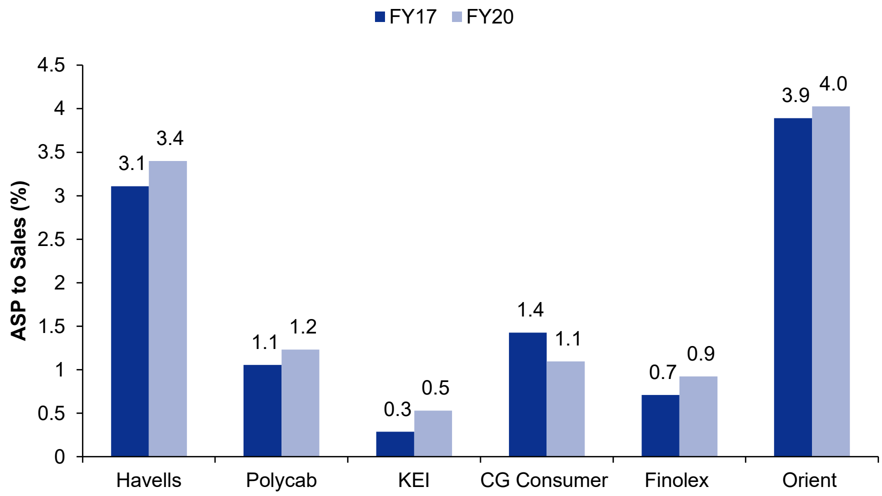
Companies consistently investing in brand building and focussing on widening distribution reach will benefit from larger market share gains.

We believe companies consistently investing in brand building and focussing on widening distribution reach will benefit the most from the shift to the organised sector, aiding in large market share gains. Management commentary on investor calls in the recent past has been a lot around distribution reach and penetration in non-metro markets and how that has helped to remain insulated due to lack of demand from metro markets suffering from severe COVID-19 lockdowns. Branding spends have been significantly lower in the 1HFY21, while we expect them to pick up meaningfully in 2HFY21 and FY22 yoy.

Figure 17: Industry participants enhancing brand visibility

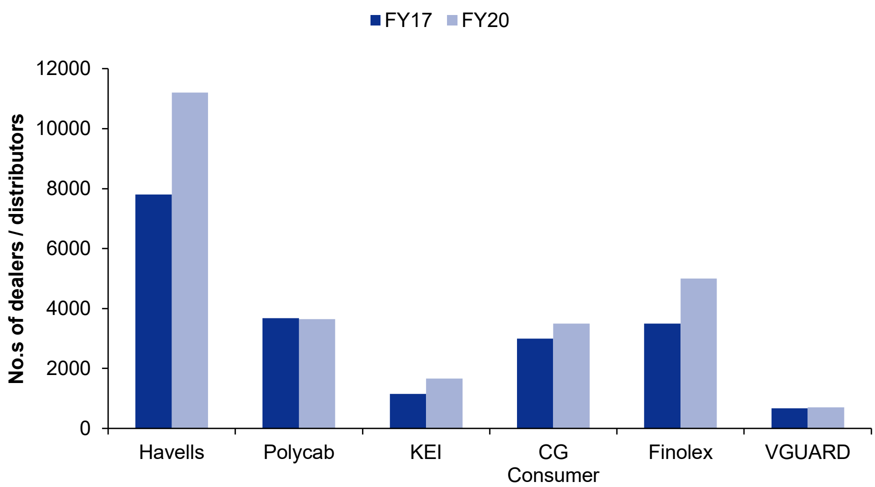
SOURCES: POLYCAB 1QFY20 PRESENTATION, EIP RESEARCH

Figure 18: Advertising and sales promotion (ASP) spends for companies



SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 19: Companies are expanding their distributor reach to be more available



SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 20: Management commentary from recent filings suggesting focus on distribution expansion

HAVELLS

Encouraging business performance with secular growth across divisions and regions led by Increased penetration in smaller towns and a higher rural reach

POLYCAB

Lower-tier towns, semi-urban areas and rural hold great potential for a well-established brand like ours. While affordability and awareness are increasing, availability is a key challenge, and we aim to address this issue by developing an active distributor network in towns below 5 lakh population for all our B2C products

Crompton Greaves

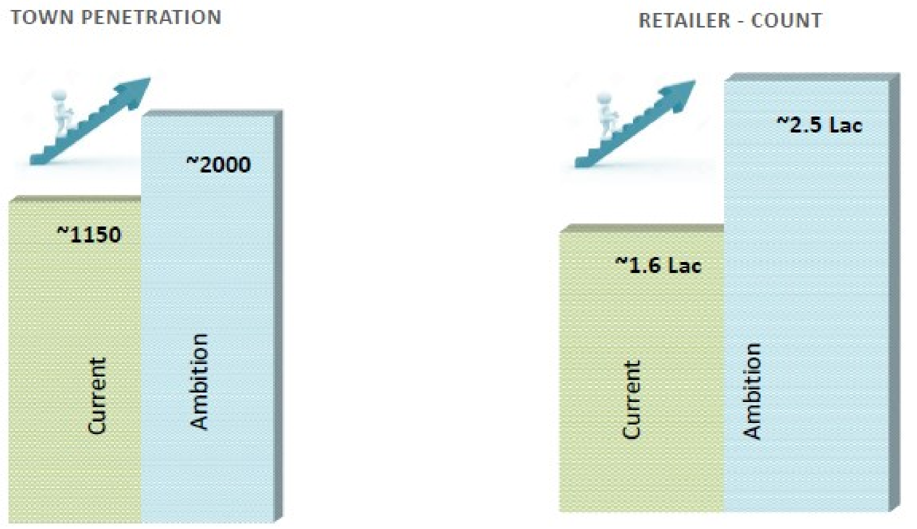
Our early focus in making further inroads into the rural channel where we have been investing and building a separate organization and capabilities have helped us with a faster rural revival and ensured consistent market share gains.

KEI

we'll be increasing penetration of dealers in the unrepresented areas, semi-urban areas and rural areas, across pan India

SOURCES: COMPANY REPORTS, EIP RESEARCH

Figure 21: Havells shared its ambitious plan on distribution expansion



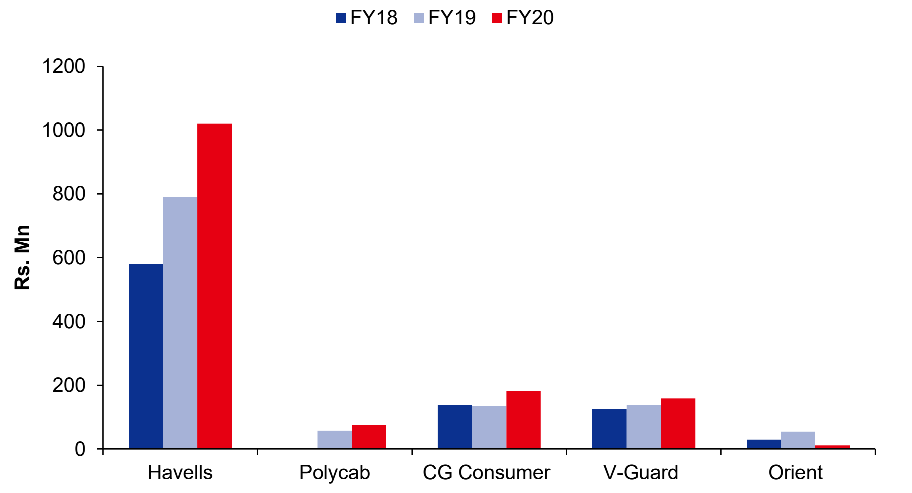
SOURCES: COMPANY REPORTS, EIP RESEARCH

Investment in product innovation also aiding consumer shift to organised sector ➤

New innovative product offerings provide the dual benefits of premiumisation and enhanced brand image.

R&D investments in the industry have achieved relatively higher importance now owing to use of Artificial Intelligence (AI) and Internet of things (IoT) for product innovation. Smart devices have gained revenue share across our coverage universe and companies continue to benefit from demand for premium products. Consistent R&D investment and changing as per consumer needs are critical for emerging FMEG players like Polycab to replicate the success of erstwhile FMEG leaders like Havells and Crompton Greaves Consumer.

Figure 22: Investment in innovation by organised players (rising R&D expenses)



SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 23: Product Innovation enabling entry in new products

Product	Traditional Products	Innovative Products
Fans	Traditional 3-blade fan	Purocoat/anti-virus fans, anti-dust fans, fans with integrated multi-functional LED lights, IOT-driven fan operation
Switches	Traditional plastic switches	Switches with soundless soft touch and remote control
Lighting	Regular LED lamps	Colour-changing RGBW (red-green-blue-white) bulbs with remote control, anti-bacterial bulb
Wires	Single-core PVC insulated wires	Green Wire – energy-efficient, recyclable (RoHS compliant), low smoke density and emits fewer toxic gases in extreme fire situation
Cables	Single-core copper cable	Speciality, cross-linked polyethylene, zero halogen cables

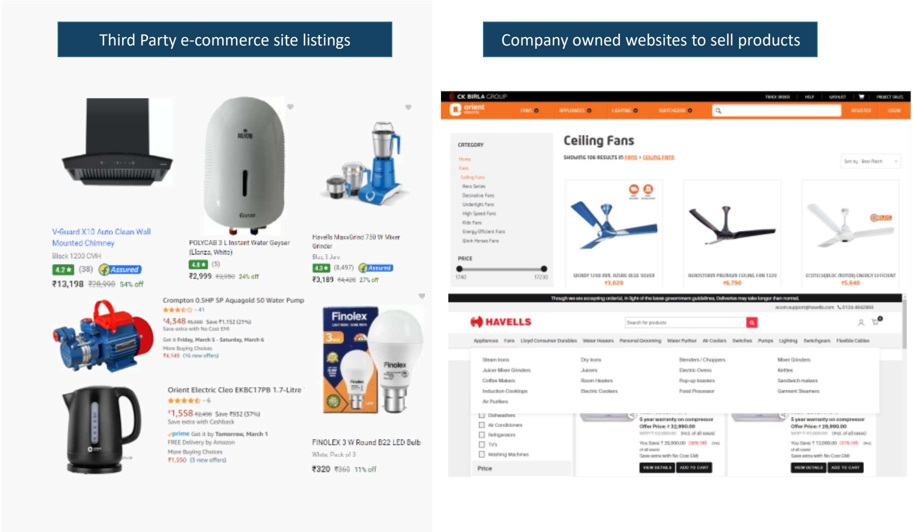
RESTRICTION OF THE USE OF CERTAIN HAZARDOUS SUBSTANCES IN ELECTRICAL & ELECTRONIC EQUIPMENT (ROHS)
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 24: New product innovations indicate shift towards wi-fi-enabled, remotely-controlled devices with digital displays

SOURCES: EIP RESEARCH, COMPANY REPORTS

E-commerce revenue share has been gradually increasing

Figure 25: Evolving share of e-commerce in the post-COVID era



SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 26: Most companies seeing strong demand traction on e-commerce channel

Crompton

We have significantly stepped up our focus in the e commerce channelin terms of portfolio across the price range to serve market demand for all product ranges on the channel.

orient electric

OEL leveraged its online presence, partnering with major online platforms to launch and promote its products with expanded range.

V-GUARD

If we take out products like wires, switch gear and pump, which we don't sell on e-commerce. I think on the remaining categories we should be doing about 6% to 7% of our revenue coming from e-commerce.

HAVELLS

We did see a major increase in ecommerce sales. In fact, now it has come to almost about 4-4.5% of consumer and residential demand. So that is quite strong and going forward with Lloyd now focusing on the e-commerce channel along with the traditional channel also should increase our share in the e-commerce.

SOURCES: EIP RESEARCH, COMPANY REPORTS

Share of B2C products increasing across our coverage universe

Most players concentrating on improving B2C revenue mix ➤

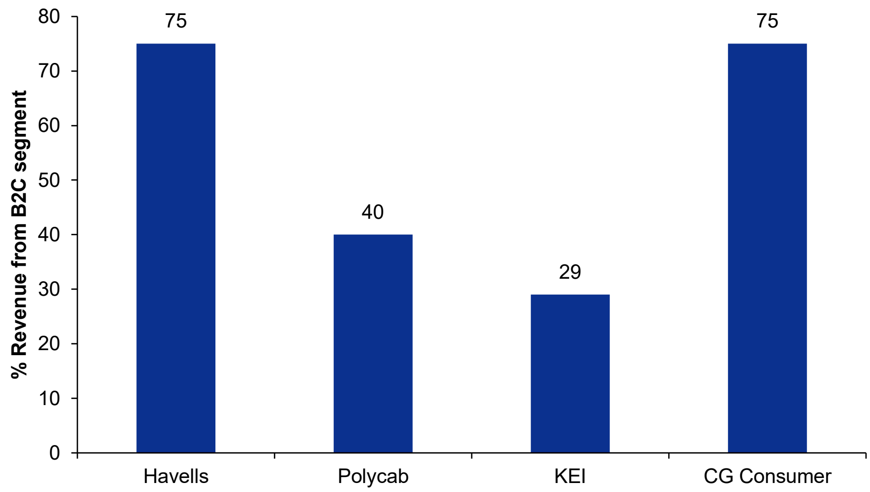
Electrical players are in various stages of their journey towards becoming a household name in the FMEG space. We believe electrical companies are moving from being B2B C&W players to transforming into retail branded B2C players with higher focus on consumer products like flexible housing wires, fast-moving electrical products and exploring the small domestic appliances segments. So far, Havells has made its mark by being among the Top 3 players across FMEG products. Polycab, Finolex Cables and KEI Industries have been building scale and will likely emerge as credible industry participants.

Figure 27: Journey of electrical companies (focussing on B2C segment)

B2B → B2C	Cables & Wires	Housing Wires	FMEG	Appliances
Havells	✓	✓	✓	✓
Polycab	✓	✓	✓	
KEI	✓	✓		
CG Consumer			✓	✓
Finolex Cables	✓	✓	✓	
V-Guard		✓	✓	✓
Orient Electric			✓	✓

SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 28: Estimated FY21F B2C revenue share



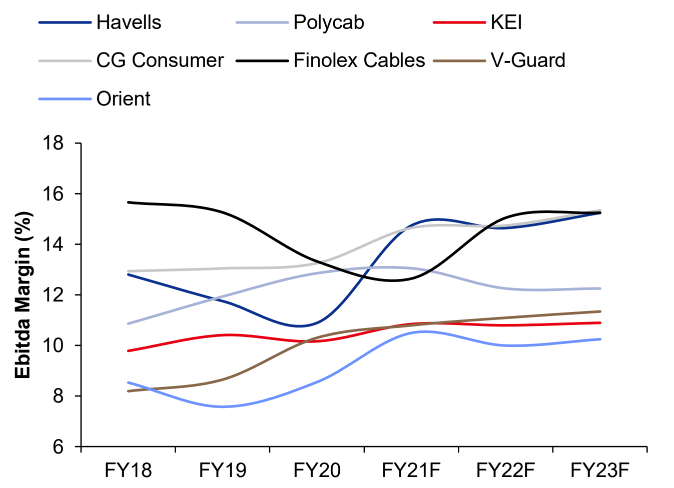
SOURCES: EIP RESEARCH ESTIMATES

Favourable revenue mix supports operating profitability and reduces incremental working capital deployment ➤

Higher salience of B2C business to improve operating margins and has lower working capital requirement, in our view.

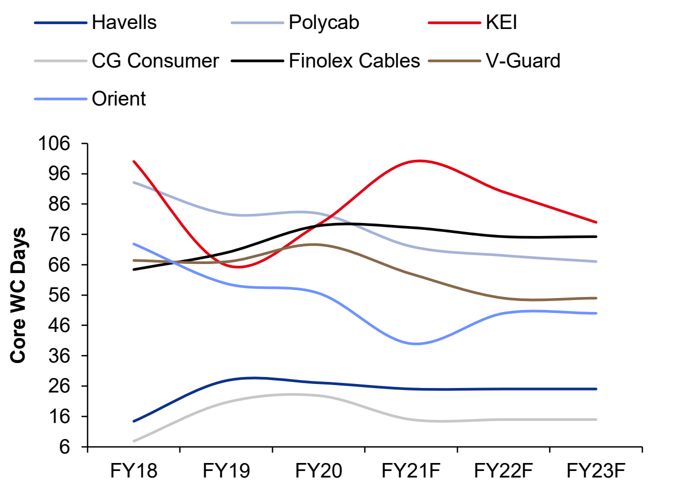
Changing revenue mix in favour of retail products and being closer to consumers strengthens brand recall, aids pricing power and reduces the share of credit sales. This encourages overall sustainability of operating margins by enabling pass through of higher raw material costs and reaps operating leverage benefits for established players. Though the number of SKUs might increase offering more choices to customers, channel financing through banks helps reduce the receivables cycle to a great extent lowering overall incremental working capital deployment.

Figure 29: EBITDA margins to sustain FY21 levels



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 30: Core WC cycle (Inventory + Debtors - Creditors)



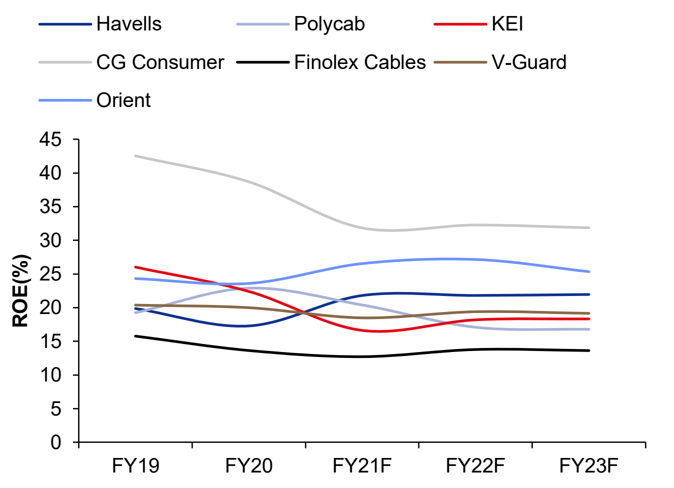
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Healthy return ratios and free cash flows over FY21-23F

All our coverage companies are likely to have net cash balance sheet as of Mar 2021F. We estimate the return on average equity (RoAE) and return on average capital employed (RoCE) to be between ~10%-40%.

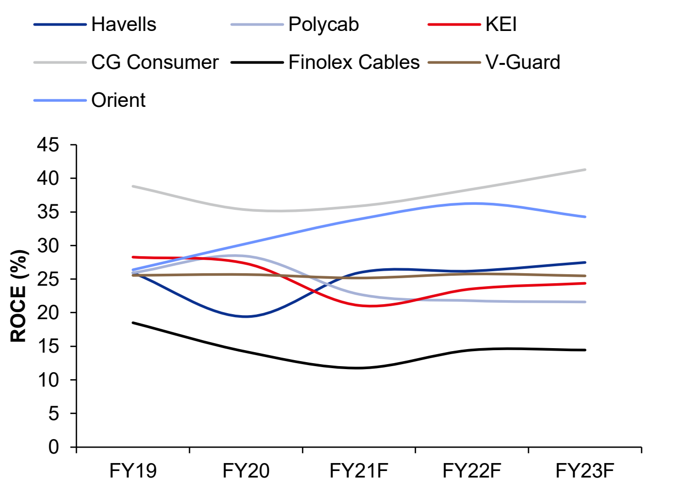
We expect cumulative FCF generation to be healthy to be deployed for developing in-house manufacturing capabilities, research and development expenses, reinvestment into brand building and new market/product development. We expect dividend payouts to rise as well over FY21-23F.

Figure 31: Return on equity (RoE)



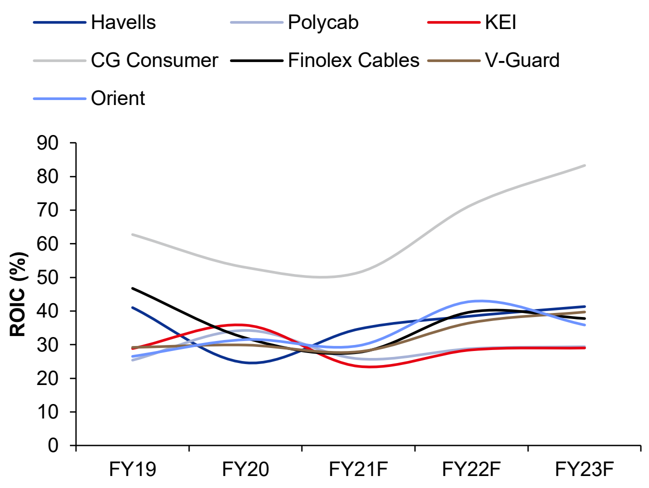
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 32: Return on capital employed (RoCE)



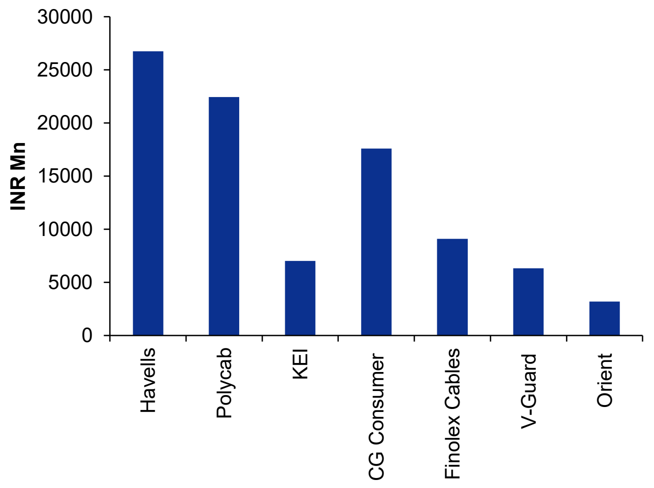
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 33: Return on invested capital (RoIC)



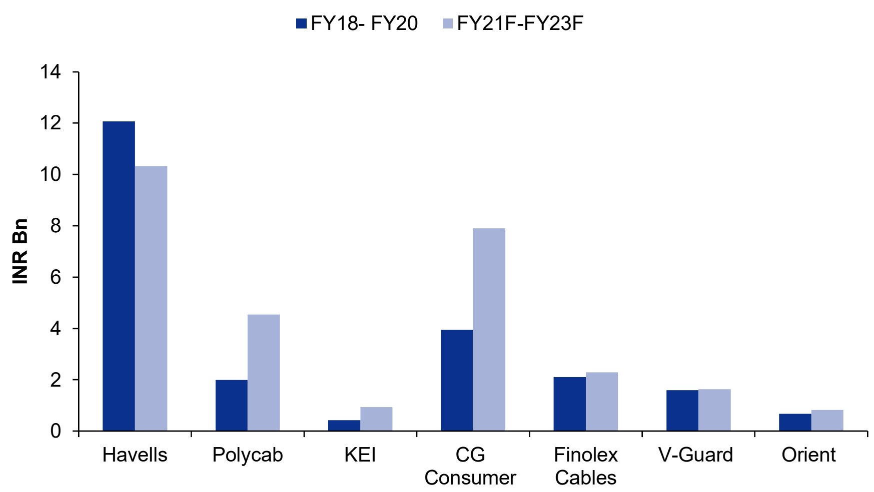
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 34: Cumulative FCFF (FY21F-FY23F)



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 35: Estimated cumulative dividend distribution



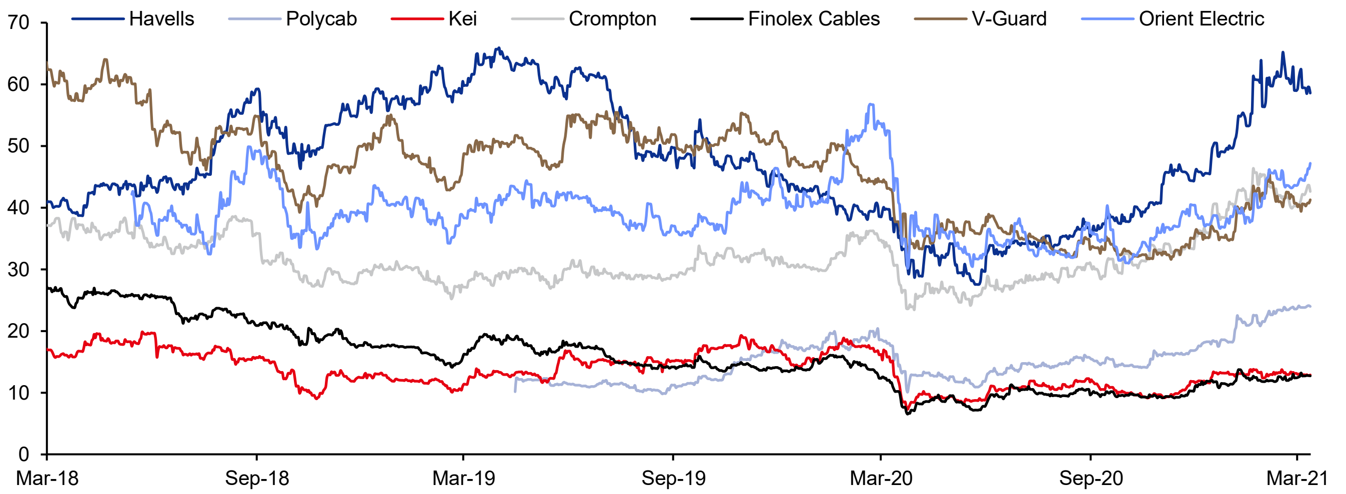
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Valuation

- Private and government capex recovery on infrastructure/new capacities, higher share of B2C sales and wider/deeper distribution network are structural positives for the sector.
- Market share gains, experienced and professional management teams and long runway for growth in a large consistently growing electrical industry are factors that drive premium valuations for the sector.
- We expect P/E multiple re-rating possibility for emerging B2C players like Polycab and KEI, while FMEG companies to largely sustain their premium valuations given our expectations of strong net profit CAGR going forward.
- Coverage stocks are trading between their three-/five-year mean P/E multiples and +1SD range reflecting market expectations of higher cash flow growth vs the past.
- We value our coverage universe relative to its mean P/E multiples. We expect lesser volatility in net profits over FY21-23F. Hence we believe, P/E multiples will help compare valuations in a simpler and effective way.
- Consumer electrical companies are in the growth phase in our view and have the potential to continue to grow revenue/profits at double-digit CAGR. We think growth businesses are better valued using P/E multiples vs the DCF-based valuation methodology used for matured businesses.

- We have Add rating on Havells and Crompton and expect them to deliver 17-20% EPS CAGR over FY21-23F. We expect most of our other coverage universe to deliver over 15% EPS CAGR except Polycab that will have EPS CAGR of 10.8% adjusted for tax refunds.

Figure 36: P/Es for coverage companies



SOURCES: EIP RESEARCH, BLOOMBERG

Figure 37: Valuation summaries of coverage companies (5 years)

	CMP	TP	P/E -2SD	P/E -1SD	P/E Mean (5 Yrs)*	P/E +1SD	P/E +2SD	FY23F P/E
Havells	1,103	1,231	22	32	42	52	62	49
Polycab	1,360	1,530	8	12	15	19	22	21
KEI	495	645	5	9	12	15	19	11
Crompton Consumer	410	465	23	29	34	39	44	35
Finolex Cables	403	504	6	12	17	23	28	11
V-Guard	230	277	26	36	46	57	67	36
Orient Electric	295	328	30	35	39	44	49	41

*SINCE LISTING / DEMERGER FOR POLYCAB, CROMPTON AND ORIENT ELECTRIC
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS, BLOOMBERG

Downside risks

- **Small Indian emerging companies and Chinese competition:** Previously, smaller emerging players entered into a new product segment and distorted prices owing to the market entry discounting strategy. Even imports from China across product categories slowed market share gains of organised Indian manufacturers. Stiff competition could result in lower revenues vs our expectations.
- **New product launches:** Much of the brand success and market share gains depend on the launch of consistent exciting innovative products. Continuous innovation and marketing spends help brands stay relevant and result in superior business performances vs competitors. Delays or poor designs could impact revenue growth for all the companies.
- **Widening and deepening of customer reach:** All of our coverage companies are committed to penetrating wider and deeper across India and diversifying their revenue-mix profiles. The dealer and retailer networks are ever increasing and are critical to support rising demand going forward.
- **Adverse raw material prices:** Metals and PVC are key raw materials for the C&W and FMEG businesses. Adverse price movements or sharp volatility might result in a temporary negative impact on gross margins and overall net profits.
- **Unfavourable forex rates:** Few companies still import some of their RM/FG requirements. Sharp drops in INR vs US$ could impact gross margin negatively if spreads are not effectively passed on to end customers.

India

ADD *(Initiating coverage)*

Consensus ratings*:	Buy 14 Hold 17 Sell 9
Current price:	Rs1,103
Target price:	Rs1,231
Previous target:	N/A
Up/downside:	11.6%
EIP Research / Consensus:	11.4%
Reuters:	HVEL.NS
Bloomberg:	HAVL IN
Market cap:	US$9,487m
	Rs6,90,555m
Average daily turnover:	US$36.8m
	Rs2681.7m
Current shares o/s:	625.7m
Free float:	40.5%

Source: Bloomberg

Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	(3.4)	33.3	90.6
Relative (%)	(2.0)	21.0	34.0

Major shareholders	% held
Promoters	59.5
Life Insurance Corporation Of India	5.5
Nalanda India Equity Fund Limited	5.3

Havells India Ltd

Leading the sectoral demand recovery

- Strong revenue market share gains ahead, driven by rural network expansion and focus on consumer and residential product innovation and marketing.
- Operating leverage and efficient working capital management will ensure consistent free cash flow generation going forward, in our view.
- Sustainable demand recovery augurs well for a 24% EPS CAGR (FY20-23F); We initiate coverage with an Add rating and target price of Rs1,231.

Urban demand recovery and rural penetration to drive sales growth

Havells management has its priorities clear in terms of growing in the right product categories and relevant geography, in our view. The electrical consumer durable (ECD) and Lloyd product portfolio will grow faster than the industrial/infrastructure segment on the back of strong recovery expected in urban consumption and continuing rural demand, in our view. Urban markets account for ~65-70% of Havells's FY21F revenues and this presents significant scope to penetrate deeper into the Indian hinterland. Havells is also exploring investment under the Indian government's flagship Production Linked Incentive (PLI) manufacturing scheme to build export competitiveness. We expect consolidated revenue CAGR of 11.7% driven by ECD/Lloyd CAGR of 15.3%/13.9% over FY20-23F.

Operating leverage benefits from optimum capacity utilisation

Stabilisation in volume growth and pricing of B2B products augur well for Havells. We expect company-wide optimum utilisation of manufacturing capacities and the company to reap scale benefits in the form of higher profitability also due to higher in-sourcing of Lloyd product manufacturing. We estimate consolidated EBITDA CAGR of 25% over FY20-23F and EBITDA margin of 14.5-15.5% over the same period.

Cumulative FCF of Rs27bn over FY21-23F, expect higher dividends

Working capital management has been the most efficient for Havells within our coverage universe given the scale and size the company operates currently. Our capex estimate of Rs13bn over FY21-23F includes Rs3bn of washing machine and air conditioning unit capex. Given limited incremental working capital deployment, we expect cumulative FCF of Rs27bn over FY21F-23F. We expect Havells to largely repay all COVID-19 related temporary raised debt of Rs10bn over the next 12 months and maintain its ~35% dividend payouts going forward.

Sustainable demand recovery, initiate coverage with Add rating

The stock trades at a P/E of 49.3x FY23F EPS. Given factors like cyclical recovery in housing demand and government thrust on infrastructure spends, we think the business environment augurs well for Havells going forward. Mean P/E for the past three and five years has been 42-48x. We value the stock at 30% premium to its 5-year mean P/E at 55x FY23F EPS and initiate coverage with an Add rating and a target price of Rs1231. Downside risks: Capex delays, slow ramp-up of new products and volatile metal prices.

Analyst(s)

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Financial Summary	Mar-19A	Mar-20A	Mar-21F	Mar-22F	Mar-23F
Revenue (Rsm)	1,00,734	94,403	1,01,924	1,17,976	1,31,611
Operating EBITDA (Rsm)	11,844	10,287	15,034	17,284	20,071
Net Profit (Rsm)	7,876	7,354	10,179	11,870	14,001
Core EPS (Rs)	12.6	11.8	16.3	19.0	22.4
Core EPS Growth	15.4%	(6.7%)	38.4%	16.6%	18.0%
FD Core P/E (x)	87.57	93.84	67.82	58.15	49.30
DPS (Rs)	4.5	4.0	5.0	5.5	6.0
Dividend Yield	0.49%	0.44%	0.45%	0.50%	0.54%
EV/EBITDA (x)	57.21	66.00	44.81	38.67	32.84
P/FCFE (x)	103.67	120.97	50.88	227.86	56.19
Net Gearing	(30.3%)	(26.3%)	(33.2%)	(37.3%)	(45.3%)
P/BV (x)	16.44	16.01	13.76	11.78	10.03
ROE	19.9%	17.3%	21.8%	21.8%	22.0%
% Change In Core EPS Estimates					
EIP Research/Consensus EPS (x)			1.04	1.06	1.04

SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS. PRICED AS AT 12 MAR 2021

Leading the sectoral demand recovery

Urban demand recovery and rural penetration to drive sales growth

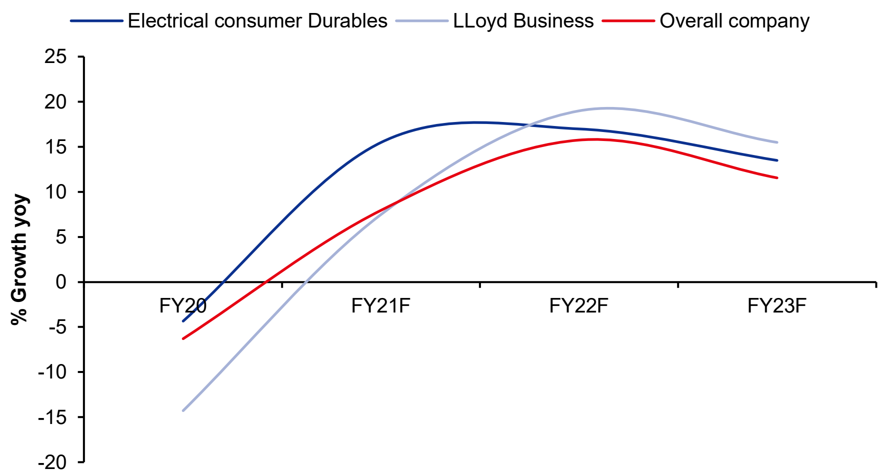
ECD and Lloyd are catalysts to drive consumer and residential category growth ➤

Havells has 20 product verticals serving 70% of household electric sockets. It is estimated that consumer and residential segment is ~75% of the FY21F consolidated revenue while the industrial/infrastructure segment forming the balance 25% of revenues.

Figure 38: Consumer and Residential product portfolio of Havells

SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 39: ECD and Lloyd business to grow ahead of other segments



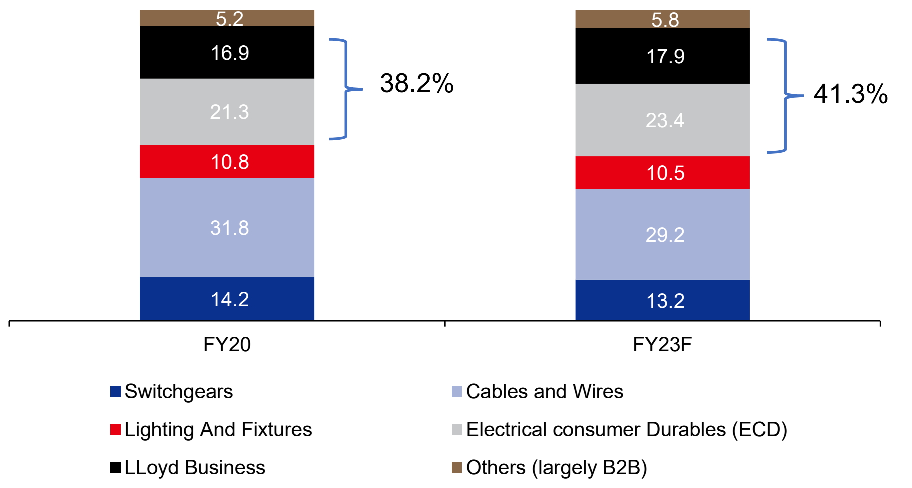
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 40: Havells's product range classification

Consumer and Residential	Industrial and Infrastructure
Low Voltage Switchgear	High Voltage Switchgear
Flexible Wires	Power and High – Tension cables
Consumer LED and Luminaries	Professional LED and Luminaries
Fans	Motors and Capacitors
Water Heaters	Solar Solutions – Lighting, Pumps
Air Coolers	Agriculture and Industrial Pumps
Small Domestic Appliances	
Lloyd (AC, Washing Machine, Refrigerator)	
Personal Grooming	
Air and Water Purifier	
Residential Pumps	

SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 41: Rising revenue share from B2C segments (Lloyd and ECD)



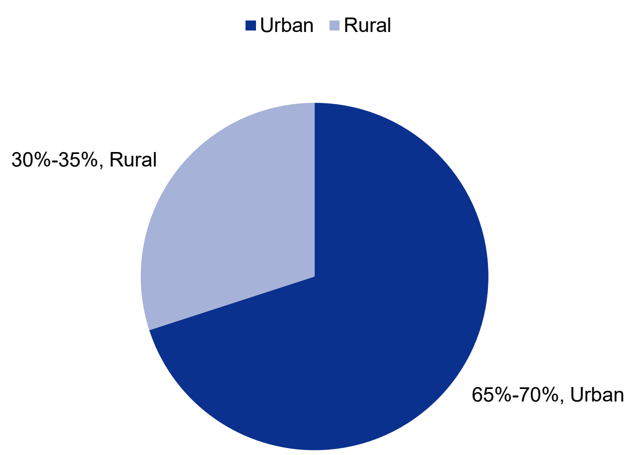
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Broadening distribution network into tier-3/-4 towns and rural markets would aid overall growth

"Expanding our distribution network with key focus on semi-urban and rural markets."
– Mr. Anil Rai Gupta, Chairman, Havells

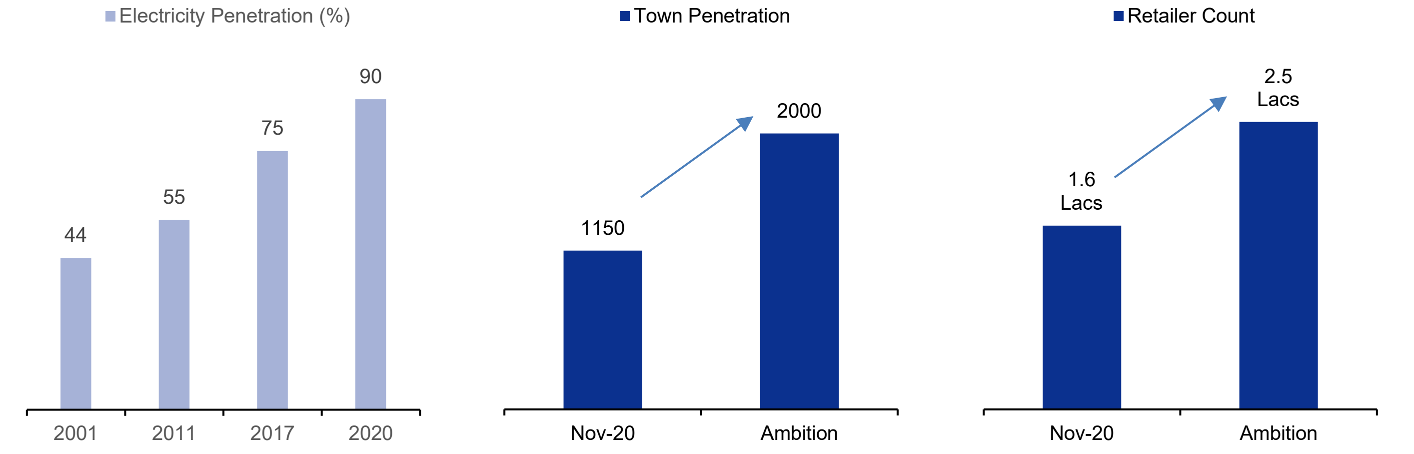
Havells derived ~65-70% of its revenue from metro and tier-1 markets in FY20. The company has been developing its distribution network pan India and had 11,200 dealers as of Mar 2020. The company intends to expand its reach further into the Indian hinterland and broaden its network across tier-3 and -4 towns and villages.

Figure 42: A large part of Havells revenue is from urban India (FY20)



SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 43: Rising rural electricity penetration and efforts to increase proximity to consumers will aid FMEG product demand. Havells provided a sense of its future plans

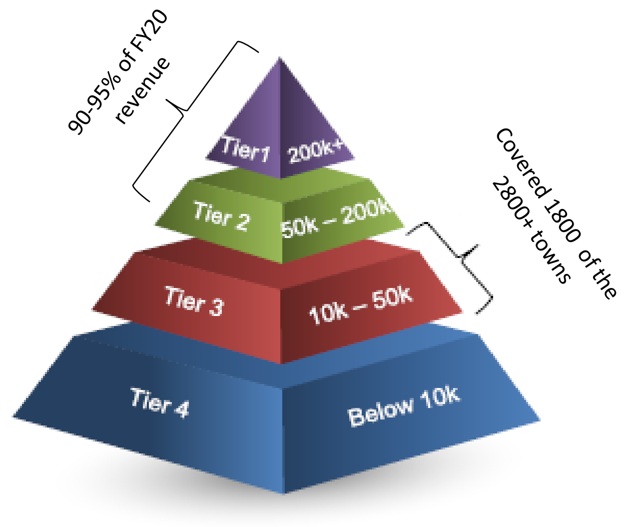


SOURCES: EIP RESEARCH, STAISTA

SOURCES: EIP RESEARCH, COMPANY REPORTS

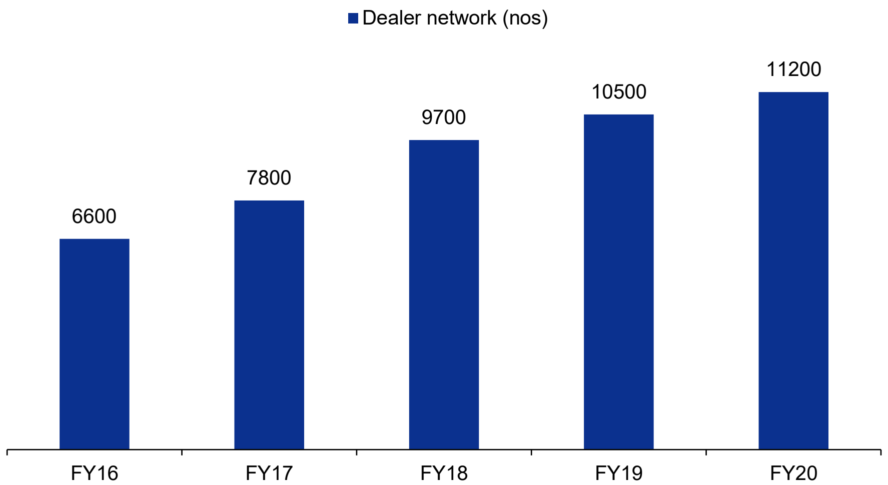
FMEG IS FAST-MOVING ELECTRICAL GOODS
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 44: Management identified ~2,800 towns with 10k-100k population to expand reach in tier-2/-3 markets; 1,800 towns done so far



SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 45: Rising pan-India dealer network



SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 46: Product and brand positioning for semi urban / rural markets

SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 47: Largest electrical exclusive brand outlets (EBOs) in India

SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 48: Lloyd distributor channel now much more diversified

Before Acquisition		After Acquisition	
80% of the business done through dealers/distributors	70% business sourced through top 15-20 distributors	35% business sourced from Modern Retail	65% contributed by dealers/ distributors (without concentration risk)

SOURCES: EIP RESEARCH, COMPANY REPORTS

Focus on gaining market share in small domestic appliances and exports

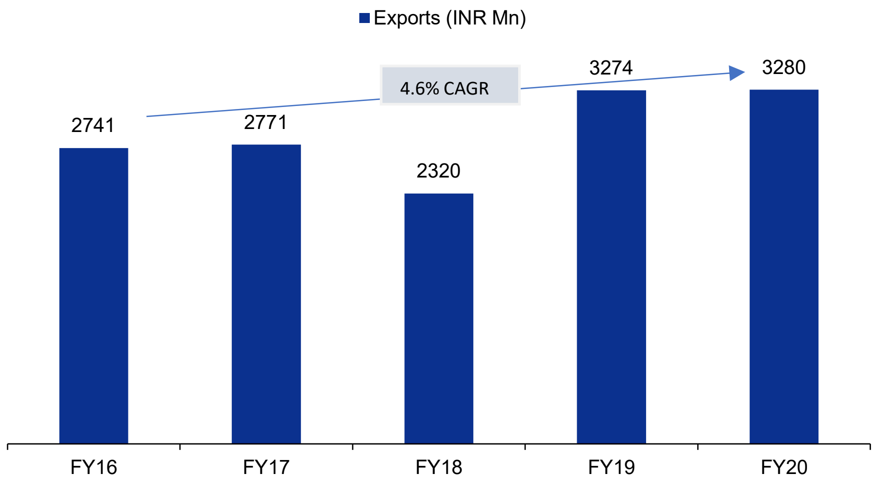
Havells' ECD segment has been focused on launching consumer-centric innovative products backed by technology to stay ahead of competition. Moreover, its focus on omni channel and e-commerce is likely to continue benefitting categories like Personal Grooming and Small Domestic Appliances.

Figure 49: Small Domestic Appliances

SOURCES: EIP RESEARCH, COMPANY REPORTS

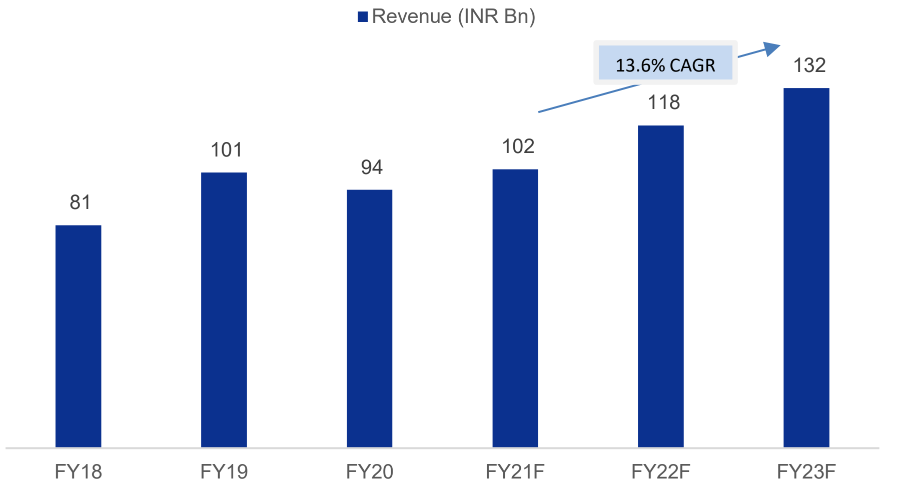
Exports accounted for 3-5% of consolidated revenues over FY16-20 and had a CAGR of 4.6% over the same period. Adjusted for the disinvestment of Sylvania – one of Havells businesses – in FY16 and rebasing FY16 exports, Havells export revenue CAGR was ~15%. In fact, Havells is the third largest exporter of fans to Bangladesh today. We believe there is meaningful opportunity to grow export revenue further in markets like the Middle East, Africa and other geographies and exports could reach Rs10bn/year potentially. Havells is also exploring opportunities, if any, within the Indian government's PLI scheme for related products like air conditioners, etc. that could further boost export revenues.

Figure 50: Exports grew 4.6% CAGR over FY16-20



SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 51: We estimate consolidated revenue CAGR of 13.6% over FY21F-23F



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Pricing and demand stability for B2B products and turnaround of Lloyd profitability would lead to EBITDA CAGR of 22% over FY20-23F

We believe demand recovery of industrial and other B2B products on the back of infrastructure and housing recovery across India will help in better utilisation of existing manufacturing capacities and efficient absorption of fixed costs. This, in turn, will improve operating performance and EBITDA margins, in our view. Stability of pricing in highly competitive segments like professional and consumer lighting would likely support revenue growth and lower operating costs. Industry players have highlighted that pricing erosion for LED Lighting since FY18 stabilised over 1HFY21 and they could potentially report growth in revenues yoy.

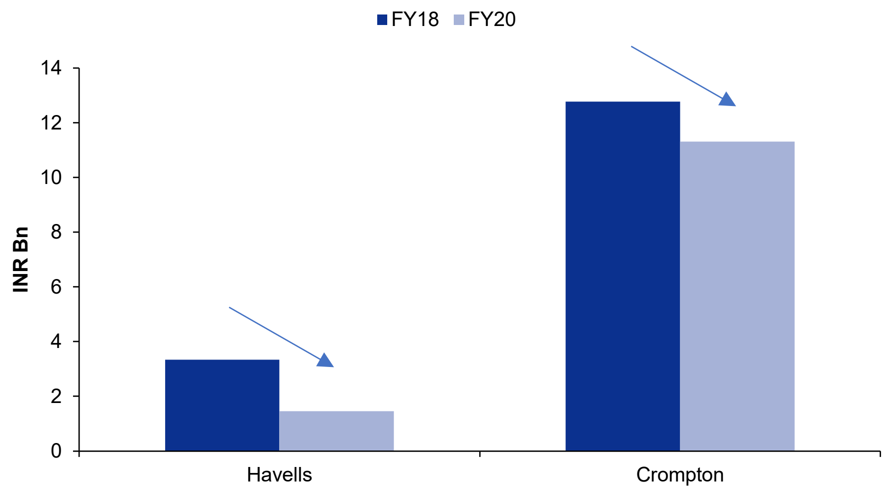
Figure 52: Housing demand recovery

COVID-19 Trend	Indicator of Demand Recovery
Work from home and online schooling is a new normal	• Remote working has led to the rise of demand for housing options in peripheral areas
De-densify to improve social distancing	• Close to 900 plotted units launched in the last 4-5 months in Chennai • NCR witnessed a huge demand for farmhouses, and average monthly transactions have gone up from 2-3 in the pre-COVID era to 10-12 as of now • In Ahmedabad, the demand for second homes, from areas around Shilaj to Racharda, has increased by around 40%
Preference to reside in a controlled environment	The growing demand for these townships is such that the past few years have seen markets beyond the metro cities becoming a prime destination for the segment
Reverse migration/work from hometown to redefine the real estate demand	According to a leading bank, the demand for home loans across the country has increased. Most of the demand is for small to mid-sized apartments where typically the property price would be about Rs35lakh-40lakh • As remote working continues, demand for housing in tier-2 and -3 cities are likely to rise
Avoidance of execution risk	• As of 2020, nearly 17% of the unsold inventory was ready-to-move-in across the top seven cities of India
Customers are ready to pay premium for quality	• Sales of the top eight listed players accounted for 25% of the overall sales (1HFY21) in the top seven cities of India compared to 14% in FY20

NCR IS THE NATIONAL CAPITAL REGION
SOURCES: EIP RESEARCH, ANAROCK

"We continue to see strong opportunities in lighting, in the B2C part now, having largely weathered the price erosion"
– Crompton Greaves Consumer 3QFY21 conference call

Figure 53: Lighting revenue growth for Havells and Crompton Greaves



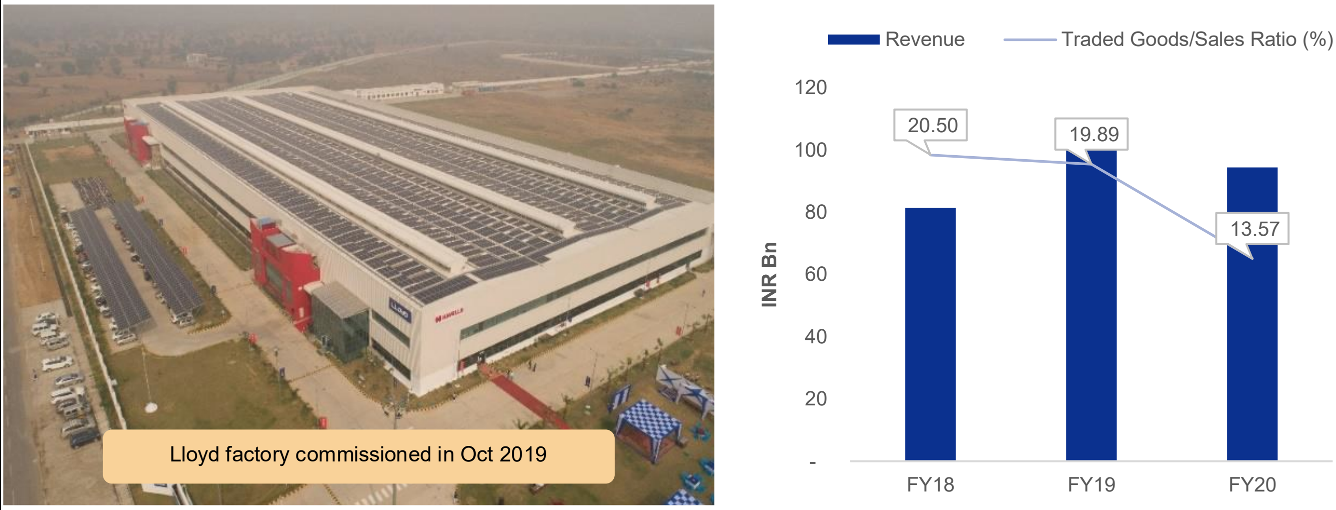
SOURCES: EIP RESEARCH, COMPANY REPORTS

Optimum capacity utilisation of in-house facilities would yield operating leverage

Havells has invested in captive manufacturing capacities for over 90% of its matured and high-potential product categories over past years. The company operates 14 plants in India today with the latest one set up at Guwahati, Assam.

Hitherto, Lloyd was disproportionately dependent on imports (70% of FY19 sales) for all its product categories, resulting in high-cost dependency on import duties and risk of rupee depreciation. Recent commissioning of Lloyd factory significantly reduces import dependence and enhances control over raw material/component costs. Overall bought-out / traded items are expected to reduce going forward aiding both gross and EBITDA margins.

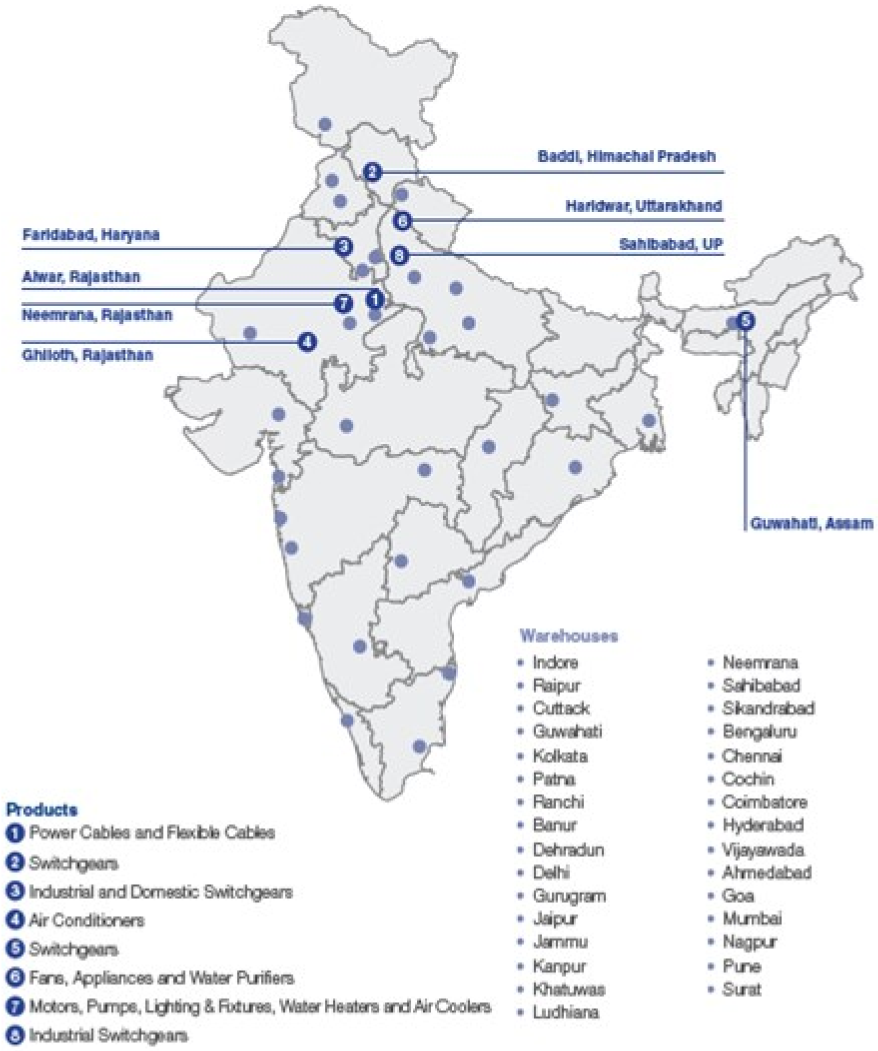
Figure 54: Focus on adding in-house manufacturing capacities and increasing capacity utilisation (declining ratio of traded goods to sales) will yield operating leverage



SOURCES: EIP RESEARCH, COMPANY REPORTS

SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 55: Havells manufacturing and warehousing network in India (FY20)

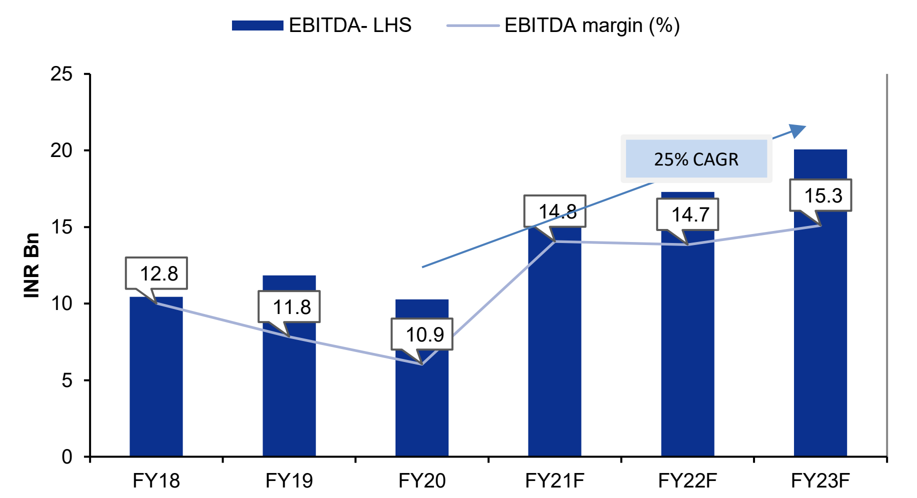


SOURCES: EIP RESEARCH, COMPANY REPORTS

Estimate EBITDA margins of 14.5-15.5%; EBITDA CAGR of 25% over FY20-23F

Significant discretionary cost cuts in light of the COVID-19 pandemic led to historical high EBITDA margins of ~15% in 9MFY21. Some of these costs, related to travel, advertising, sales and marketing, etc., will come back from FY22F and we expect partial benefits of cost cuts to sustain over FY21-23F. We build EBITDA margins within the range of 14.5-15.5% and expect EBITDA CAGR of 25% over the same period.

Figure 56: EBITDA and EBITDA margin trends



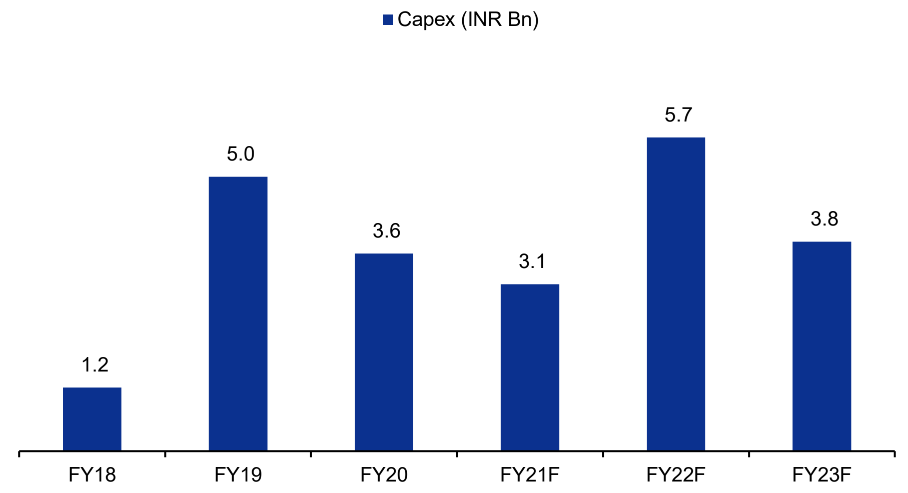
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Cumulative FCF of Rs27bn over FY21-23F

R&D and capex spends could pick up under the PLI scheme and launch of new innovative products

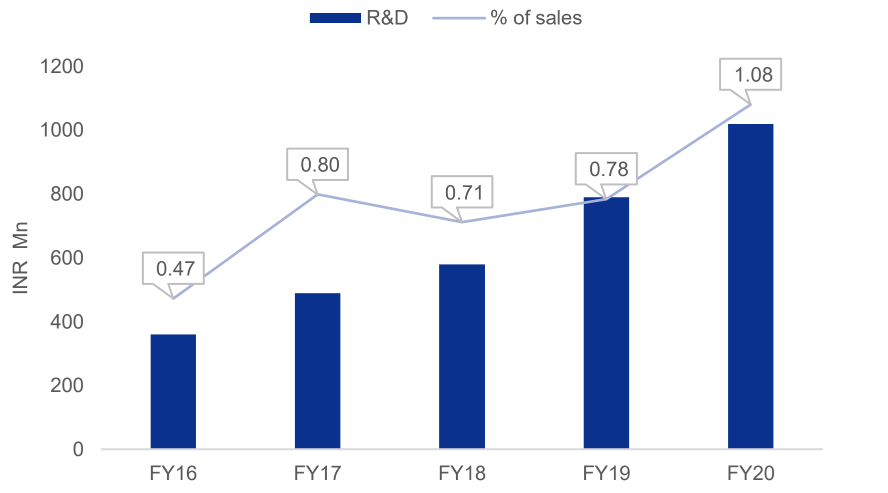
Havells has stated its intent to spend more on R&D going forward than in past years. The company spent ~1% of sales on R&D in FY20, which could rise to 3% of sales over the next five years in light of investments in new product technology related to IoT/AI, embedded software, intelligent hardware, etc. Also, the company would continue to invest in the expansion of manufacturing capacities and is also exploring options to benefit from the government's PLI scheme. We model Rs3bn-4bn/year of regular capex, account for the recent new plant capex of Rs3.2bn for Lloyd (0.3m/year units of washing machines and 0.6m/year units of air conditioners) and any incremental new plans related to PLI/Lloyd if any would be incorporated as and when announced.

Figure 57: We estimate Rs12.6bn of capex over FY21-23F



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 58: Consistent investment in R&D to drive product innovation

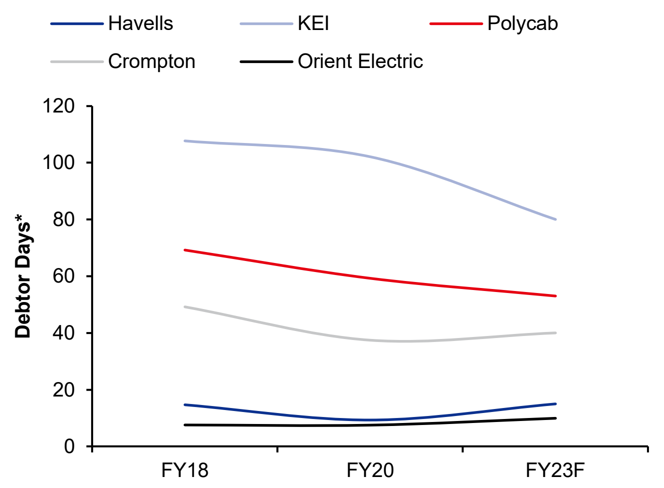


SOURCES: EIP RESEARCH, COMPANY REPORTS

Most efficient working capital management

Historically, Havells has one of the best working capital management within our coverage universe with the lowest receivable of 15 days and net working capital cycle of 30 days of FY21F sales. About 95% of company dealers/distributors avail of channel financing with non-recourse to Havells Ltd. We expect the company to continue with similar practices as it expands in rural areas and export markets.

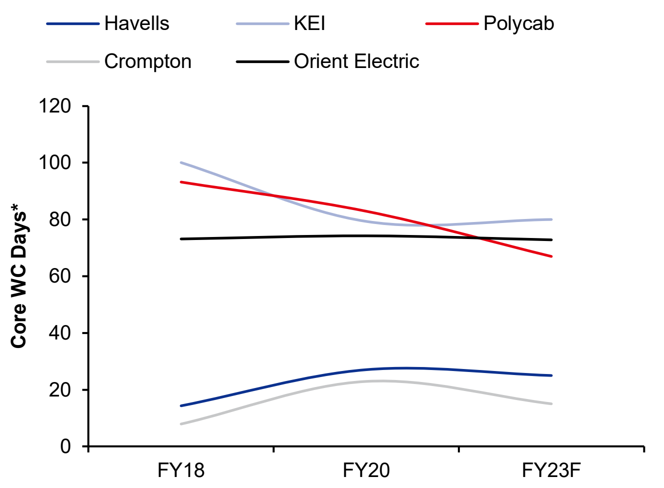
Figure 59: Receivable days



*DAYS OF SALE

OURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 60: Working capital (WC) days

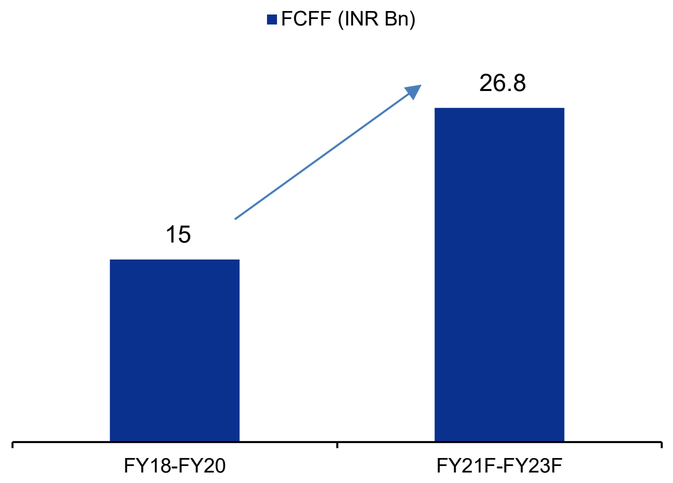


*DAYS OF SALE

SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

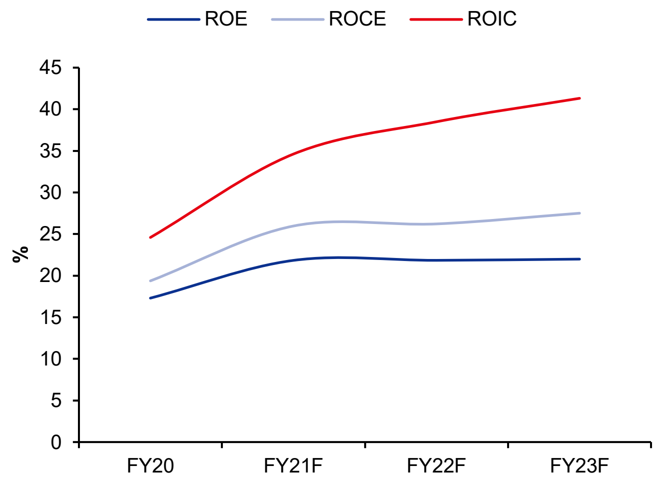
Strong FCF generation and return ratios

Figure 61: Cumulative FCFF of ~Rs27bn over FY21-23F



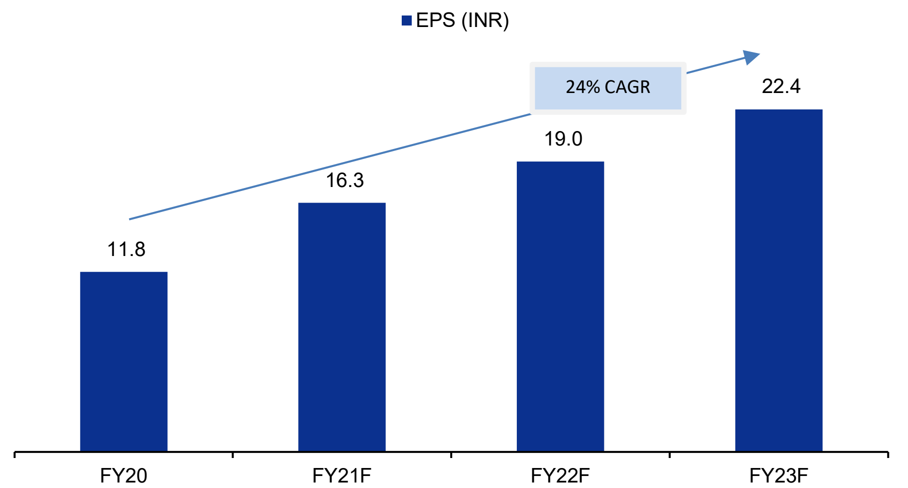
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 62: Return ratios



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 63: EPS CAGR to rise over the next 3 years



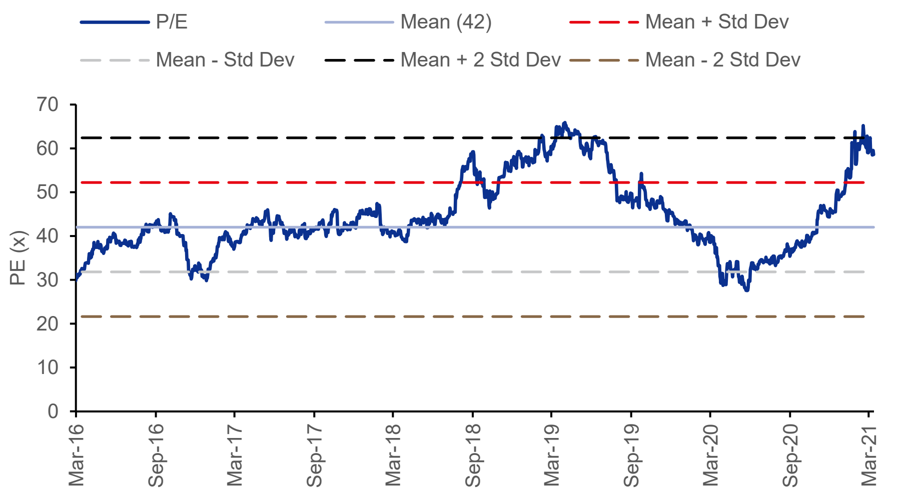
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Valuation and risk

Stock trading near +1SD to its 5-year mean P/E valuations

- Havells revenue growth has been largely range bound between FY13 and FY20 (excluding Lloyd acquisition).
- Revenue growth appears much more sustainable going forward given structural tailwinds for infrastructure development and recovery of urban housing/real estate absorption.
- The stock trades at a P/E of 49.3x FY23F EPS, closer to its +1SD above its five-year average P/E of 42x.
- We believe market leadership, potential PLI benefits and EPS CAGR of 24% over FY20-23F are key positives.
- Expect valuation multiples to sustain given strong sector tailwinds and structural benefits emerging from higher home improvement spend culture in the post COVID-19 pandemic era.
- We believe consumer electrical companies are in the growth phase and have the potential to continue to grow revenue/profits at double-digits CAGR. We think growth businesses are better valued using P/E multiples vs using the DCF-based valuation methodology for matured businesses.
- We value the stock at Rs1,231 (55x FY23F EPS) based on 30% premium to its five-year mean. We initiate coverage with an Add rating.
- We think the premium to historical multiples is justified given the sectoral recovery in demand appears sustainable and would result in higher revenue/profit growth going forward.

Figure 64: Havells trading around +1SD its 5-year mean P/E (1 year forward)



SOURCES: EIP RESEARCH, COMPANY REPORTS, BLOOMBERG

Figure 65: P/E Band Chart

SOURCES: EIP RESEARCH, COMPANY REPORTS, BLOOMBERG

Downside risks

- **Slow ramp-up of new products:** Havells has launched a variety of small and large domestic appliances. The success of these products in gaining market share in existing core markets and establishing a presence in new markets is critical. Slower ramp-up would lead to lower-than-estimated revenue growth.
- **Capex delays:** In line with management's strong belief in in-house manufacturing, the company announced new plants for washing machine and air conditioning units for a cumulative capex of Rs3.2bn over the next 12-15 months. Though all of this capex would be comfortably funded by internal accruals, execution delays could lead to lower-than-estimated revenue growth.
- **Volatile metal prices:** Metals form 45% of the total raw materials consumed for the company. Copper and aluminium are important inputs for Havells's product categories. Generally, material prices are passed through to end customers by way of regular price hikes as sharp movements in these metals are difficult to pass on. Thus, volatility in metal prices can result in lower gross margins vs our estimates.
- **High dependence on housing:** Switchgears and switches, housing flexible wires and lighting are segments hugely dependent on housing-related expenditure for their product demand. An elongated period of residential/commercial real estate demand slowdown impacts Havells's revenue and net profit growth meaningfully.

Business description and management profile

Havells India Limited is a leading fast moving electrical goods (FMEG) company and a major power distribution equipment manufacturer enjoying market dominance across a wide spectrum of products, including industrial & domestic circuit protection devices, cables & wires, motors, fans, modular switches, home appliances, air conditioners, electric water heaters, power capacitors, luminaires for domestic, commercial and industrial applications. The company pioneered Havells Galaxy – an exclusive brand showroom in the electrical industry. Today, Havells owns prestigious brands like Havells, Lloyd, Crabtree and Standard. The company has 13 state-of-the-art manufacturing plants, with over 90% of its products manufactured in-house.

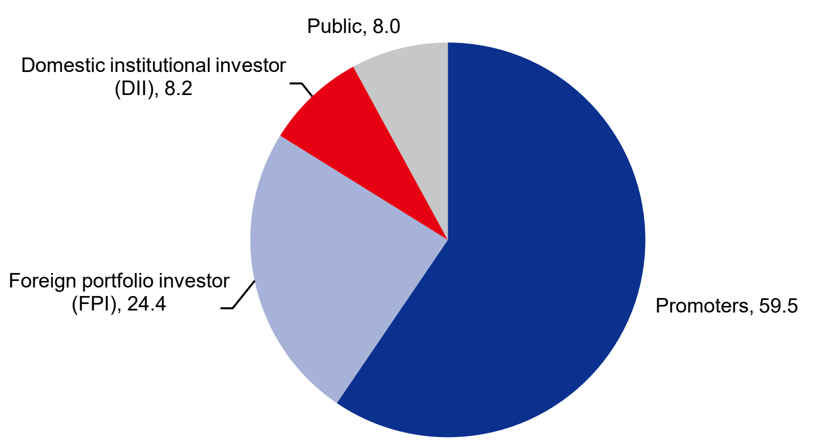
The board of directors consists of seven independent and non-independent directors each.

Figure 66: Key management profile (FY20)

Name and Designation	Profile
Anil Rai Gupta Chairman & Managing Director, Havells India Ltd.	Mr Anil Rai Gupta is the Chairman and Managing Director of Havells and is the son of the late Mr Qimat Rai Gupta. He was a constant support to his father for 22 years, until the duties and responsibilities were passed on to him in 2014. Mr Gupta has catered to the company's needs since 2006 and served as the company's Executive Director since 1992. He is a member of the Shri Ram College of Commerce alumni committee in New Delhi. Mr. Gupta pursued his higher studies at Wake Forest University in North Carolina, USA. He holds an MBA in Marketing and Finance. His marketing strategies proved to be fundamental in transforming Havells into a globally-recognised electricals and consumer durables company.
Rajesh Kumar Gupta Director (Finance) and Group CFO	Mr Rajesh Gupta is the Whole-time Director (Finance) and Group CFO of Havells Company and is a chartered accountant with rich experience in finance and allied fields. He has been associated with the promoter Group since the beginning of his career and has played a multi-dimensional role in creating the culture, systems and processes across the organisation.
Ameet Kumar Gupta Wholetime Director	Mr Ameet Kumar Gupta has a Bachelors in Engineering (Electronics & Communication) from Delhi University and an MBA (Marketing and Finance) from Wake Forest University, North Carolina, USA. Mr Ameet Gupta is part of the promoter group and is actively involved in new business development activities along with Mr Anil Rai Gupta. He oversees developing and introducing new products and setting up new plants and manufacturing facilities for the promoter Group. Mr Gupta's functions include spearheading new projects undertaken by the organisation.

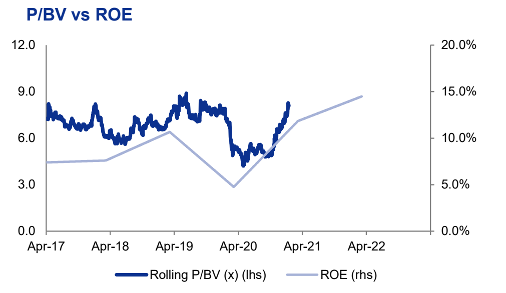
SOURCES: COMPANY WEBSITE

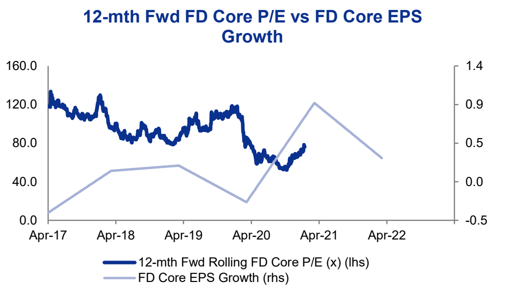
Figure 67: Share Holding Pattern (Dec 2020)



SOURCES: EIP RESEARCH, BSE WEBSITE

BY THE NUMBERS





Profit & Loss

(Rs mn)	Mar-19A	Mar-20A	Mar-21F	Mar-22F	Mar-23F
Total Net Revenues	**1,00,734**	**94,403**	**1,01,924**	**1,17,976**	**1,31,611**
Gross Profit	**37,909**	**36,071**	**38,731**	**45,716**	**51,987**
Operating EBITDA	**11,844**	**10,287**	**15,034**	**17,284**	**20,071**
Depreciation And Amortisation	(1,494)	(2,180)	(2,521)	(2,709)	(3,088)
Operating EBIT	**10,350**	**8,107**	**12,512**	**14,574**	**16,982**
Financial Income/(Expense)	634	569	390	688	1,115
Pretax Income/(Loss) from Assoc.					
Non-Operating Income/(Expense)	490	368	700	600	612
Profit Before Tax (pre-EI)	**11,474**	**9,044**	**13,602**	**15,862**	**18,710**
Exceptional Items	(3)	(3)			
Pre-tax Profit	**11,470**	**9,041**	**13,602**	**15,862**	**18,710**
Taxation	(3,594)	(1,688)	(3,423)	(3,992)	(4,709)
Exceptional Income - post-tax					
Profit After Tax	**7,876**	**7,354**	**10,179**	**11,870**	**14,001**
Minority Interests					
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	**7,876**	**7,354**	**10,179**	**11,870**	**14,001**
Recurring Net Profit	7,879	7,356	10,179	11,870	14,001
Fully Diluted Recurring Net Profit	**7,879**	**7,356**	**10,179**	**11,870**	**14,001**

Cash Flow

(Rs mn)	Mar-19A	Mar-20A	Mar-21F	Mar-22F	Mar-23F
EBITDA	11,844	10,287	15,034	17,284	20,071
Cash Flow from Invt. & Assoc.					
Change In Working Capital	(4,711)	(214)	(1,184)	(220)	(187)
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense					
Other Operating Cashflow	1,005	4,869	1,090	1,288	1,727
Net Interest (Paid)/Received	(651)	(535)	(390)	(688)	(1,115)
Tax Paid	(2,474)	(2,399)	(3,423)	(3,992)	(4,709)
Cashflow From Operations	**5,013**	**12,008**	**11,126**	**13,671**	**15,787**
Capex	(5,014)	(3,609)	(3,050)	(5,730)	(3,828)
Disposals Of FAs/subsidiaries	18	17			
Acq. Of Subsidiaries/investments	6,045	(2,508)	(500)	(1,000)	(1,000)
Other Investing Cashflow	800	625	990	1,088	1,325
Cash Flow From Investing	**1,849**	**(5,476)**	**(2,560)**	**(5,642)**	**(3,502)**
Debt Raised/(repaid)	(209)	(828)	5,000	(5,000)	
Proceeds From Issue Of Shares	180	242			
Shares Repurchased					
Dividends Paid	(3,016)	(6,413)	(3,129)	(3,442)	(3,755)
Preferred Dividends					
Other Financing Cashflow	(135)	(161)	(600)	(400)	(210)
Cash Flow From Financing	**(3,181)**	**(7,159)**	**1,271**	**(8,842)**	**(3,965)**
Total Cash Generated	3,681	(627)	9,837	(813)	8,320
Free Cashflow To Equity	**6,653**	**5,705**	**13,566**	**3,029**	**12,285**
Free Cashflow To Firm	**6,726**	**6,371**	**7,966**	**7,629**	**12,075**

SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

BY THE NUMBERS…cont'd

Balance Sheet

(Rs mn)	Mar-19A	Mar-20A	Mar-21F	Mar-22F	Mar-23F
Total Cash And Equivalents	13,113	11,325	21,662	21,849	31,170
Total Debtors	4,066	2,417	4,189	4,848	5,409
Inventories	19,190	18,719	19,547	22,626	25,241
Total Other Current Assets	2,071	2,345	2,792	3,232	3,606
Total Current Assets	**38,440**	**34,806**	**48,190**	**52,556**	**65,425**
Fixed Assets	25,935	30,391	31,281	33,302	35,041
Total Investments					
Intangible Assets	3,105	3,105	3,105	3,105	3,105
Total Other Non-Current Assets	4,002	2,432	2,071	3,071	2,071
Total Non-current Assets	**33,042**	**35,928**	**36,457**	**39,477**	**40,217**
Short-term Debt			3,250		
Current Portion of Long-Term Debt					
Total Creditors	15,598	14,141	16,755	19,393	21,635
Other Current Liabilities	9,796	9,128	8,377	9,697	10,817
Total Current Liabilities	**25,394**	**23,268**	**28,382**	**29,090**	**32,452**
Total Long-term Debt	405		1,750		
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	539	1,485	1,485	1,485	1,485
Total Non-current Liabilities	**944**	**1,485**	**3,235**	**1,485**	**1,485**
Total Provisions	3,168	2,865	2,865	2,865	2,865
Total Liabilities	**29,506**	**27,618**	**34,482**	**33,440**	**36,802**
Shareholders Equity	41,976	43,116	50,165	58,593	68,839
Minority Interests					
Total Equity	**41,976**	**43,116**	**50,165**	**58,593**	**68,839**

Key Ratios

	Mar-19A	Mar-20A	Mar-21F	Mar-22F	Mar-23F
Revenue Growth	23.7%	(6.3%)	8.0%	15.7%	11.6%
Operating EBITDA Growth	13.5%	(13.1%)	46.2%	15.0%	16.1%
Operating EBITDA Margin	11.8%	10.9%	14.7%	14.7%	15.3%
Net Cash Per Share (Rs)	20.32	18.10	26.63	34.92	49.81
BVPS (Rs)	67.12	68.90	80.17	93.64	110.01
Gross Interest Cover	63.69	41.11	20.85	36.44	80.87
Effective Tax Rate	31.3%	18.7%	25.2%	25.2%	25.2%
Net Dividend Payout Ratio	29.6%	33.4%	23.0%	21.7%	20.1%
Accounts Receivables Days	13.30	12.53	11.83	13.98	14.22
Inventory Days	103.18	118.60	110.51	106.51	109.71
Accounts Payables Days	92.95	93.04	89.23	91.29	94.04
ROIC (%)	41.0%	24.6%	34.6%	38.5%	41.3%
ROCE (%)	25.9%	19.4%	26.0%	26.2%	27.5%
Return On Average Assets	15.8%	11.9%	17.0%	17.2%	17.8%

SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

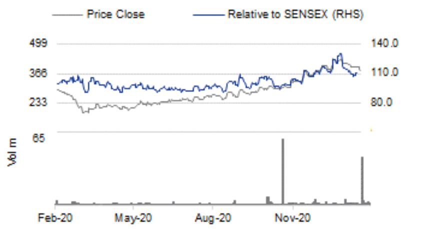
India

ADD *(Initiating coverage)*

Consensus ratings*:	Buy 36	Hold 2	Sell 2

Current price:	Rs410
Target price:	Rs465
Previous target:	0
Up/downside:	13.4%
EIP Research / Consensus:	0.8%
Reuters:	CROP.NS
Bloomberg:	CROMPTON IN
Market cap:	US$3,537m
	Rs2,57,467m
Average daily turnover:	US$12.0m
	Rs870.0m
Current shares o/s:	632.0m
Free float:	82.6%

Source: Bloomberg



Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	2.8	23.9	66.6
Relative (%)	4.3	12.5	17.1

Major shareholders	% held
Promoters	17.4
SBI-ETF SENSEX NEXT 50	6.4
ADITYA BIRLA SUN LIFE TRUSTEE	5.1

Crompton Greaves Consumer Electrical Ltd

Executing clearly stated goals

- Well-defined strategy to maintain core product leadership and target a Top 3 pan-India position for emerging categories of lighting and appliances.
- High EBITDA margins led by efficient cost management, cost savings program should continue to aid margin improvement.
- We expect 20% EPS CAGR over FY21-23F, initiate coverage with Add rating.

Crompton has consistently gained market share

Clear-cut growth strategies have helped Crompton gain market share and maintain its revenue market leadership position in the core portfolio of fans and residential pumps. Crompton has set a medium-term target to be among the Top 3 players in India in revenue market share for the emerging categories of LED lighting and consumer appliances like water heaters, air coolers and mixer grinders. We estimate Crompton's electrical consumer durable (ECD) segment revenue CAGR of 14.7% (FY21F-FY23F) to be higher than lighting's segment revenue CAGR of 13.5% (FY21-23F).

Cost management yielded higher operating margins

Crompton's cost management ensured cumulative cost savings of Rs5.4bn over FY17-20. EBITDA margins improved every year from 12.4% to 13.3% over FY17-20, rising 83bp over this period. Management has indicated the potential for further cost rationalisation still exists. We model an incremental 70bp margin increase to 15.4% by FY23F. We expect EBITDA CAGR of 17% over FY21-23F.

Lean balance sheet, no large capex planned, EPS CAGR of 20%

We expect net working capital (WC) cycle to be five days of sales for FY21F with receivables cycle at 40 days. Crompton maintains an optimum mix of in-house and outsourced manufacturing. As of Dec 2020, 60% of fans and 50% of lighting production was in-house, according to management. We expect annual capex of Rs300m-350m and cumulative free cash flow of ~Rs17.5bn (including treasury income) over FY21-23F. Gross debt of Rs4.8bn (Mar 2021F) will be largely repaid by Apr 2022. We estimate EPS CAGR of 20% over FY21-23F and RoE/RoCE of 32%/41% in FY23F.

Initiate coverage with Add rating, TP of Rs465

Consistent market share gains, strong business plan execution, solid cash flow growth and further scope for improvement in financial performance are the key upside catalysts for the stock, in our view. Crompton trades at FY23F P/E of 35.3x and EV/EBITDA of 26.4x. We expect strong net profit CAGR of 20% over FY21-23F and value Crompton at Rs465 FY23F EPS (20% premium to its five-year mean P/E of ~34x) and initiate coverage with an Add rating. Key risks: Loss of market share in core products and delays in new product launches.

Financial Summary	Mar-19A	Mar-20A	Mar-21F	Mar-22F	Mar-23F
Revenue (Rsm)	44,789	45,203	45,993	53,704	60,230
Operating EBITDA (Rsm)	5,843	5,991	6,738	7,921	9,245
Net Profit (Rsm)	4,014	4,964	5,086	6,136	7,347
Core EPS (Rs)	6.4	7.9	8.0	9.7	11.6
Core EPS Growth	23.7%	23.4%	2.5%	20.6%	19.7%
FD Core P/E (x)	64.39	52.18	50.97	42.25	35.29
DPS (Rs)	2.0	0.0	4.0	4.2	4.4
Dividend Yield	0.58%	0.00%	0.97%	1.02%	1.06%
EV/EBITDA (x)	44.31	42.88	37.46	31.43	26.43
P/FCFE (x)	197.85	233.26	33.50	122.73	47.31
Net Gearing	(3.2%)	(16.3%)	(39.9%)	(49.8%)	(58.9%)
P/BV (x)	23.58	17.66	15.02	12.49	10.23
ROE	42.5%	38.7%	31.8%	32.3%	31.9%
% Change In Core EPS Estimates					
EIP Research/Consensus EPS (x)			1.01	1.03	1.03

SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS. PRICED AS AT 12 MAR 2021

Analyst(s)

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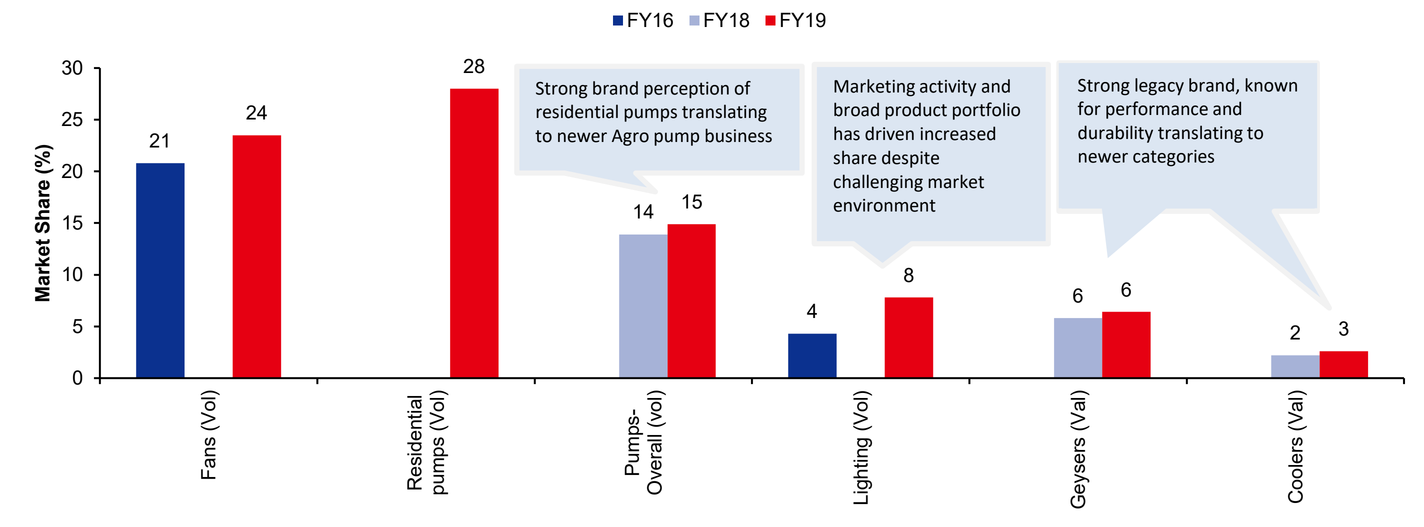
Executing clearly stated goals

Consistent market share gain has been the hallmark

Clear strategy for maintaining core product leadership and establishing presence in emerging categories

Figure 68: Crompton's well-thought-out strategy has been helping it gain market share



SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 69: Crompton has a clear growth strategy across product segments

	Major Destinations	Historical (FY15-FY19)	Medium Term (next 2-3 years)	Long Term (3-5 Years)	Focused Actions to meet the objective
CORE SEGMENTS	Fans	Maintained # 1 in Fans	Maintain # 1 in Fans	Achieve # 1 in Premium Fans (>Rs.2,500 per fan)	Company augmented its premium fan collection thereby increasing revenue of premium fans to 18% (as at Dec-20)
	Pumps	Maintained leadership in residential pumps	Maintain leadership in residential pumps and increase share in agricultural pumps	Maintain # 1 in Residential Pumps and top 3 in Agricultural Pumps	Leveraging strong brand perception of residential pumps for agricultural pump business
EMERGING	Lighting	Focus on B2C LED Lighting	Become a # 2 player in LED. Wind down CFL	Become a clear #2 in lighting	Marketing activity and broad product portfolio has driven increased share despite challenging market environment
	Appliances	Revamped Portfolio; # 5 in Geysers	Among top 3 in Geysers; Ramp up Coolers	Among Top 3 in Geysers, Coolers and Grinders.	In this segment, the company is focusing on increasing its product basket, product availability in its entire distribution channel and investment in increasing its brand visibility
NEW	New Segments	Evaluate Attractive Adjacencies	Evaluate an adjacent Segment	Top 3 Player in identified Adjacency	Exploring M&A opportunities to enter adjacent segments

SOURCES: EIP RESEARCH, COMPANY REPORTS

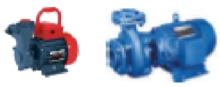
Well-defined top-down and bottom-up execution and delivery

Apart from the medium- and long-term goal mapping, the management team has a well-defined strategic roadmap from a top-down and bottom-up perspective to achieve company goals. We highlight a few of these:

- **Augment core portfolio:** The company is aiming to expand its portfolio with the launch of upgraded products in focus categories – premium fans, residential pumps and B2C LED lighting.
- **New launches:** Crompton is hoping to enter new adjacent products like solar pumps and kitchen appliances led by mixer grinders.
- **Product innovation:** It plans to invest in research and development to innovate and launch market-relevant products focused on energy efficiency (solar related) and connected technologies (Internet of Things)
- **Cost savings:** Its continued focus on cost rationalisation and operating lean operations offer it the scope to further expand EBITDA margins by 100-200bp over the next three years.
- **Go-to-market (GTM) strategy:** Adapt and implement new technology for better dealer engagement, deepen tier-2/-3 market presence and develop alternate sales channels of modern trade, e-commerce and institutional channels like Canteen Service Department (CSD) and Central Police Canteen (CPC).

Figure 70: Continuous revamp of Crompton's core and emerging product portfolio

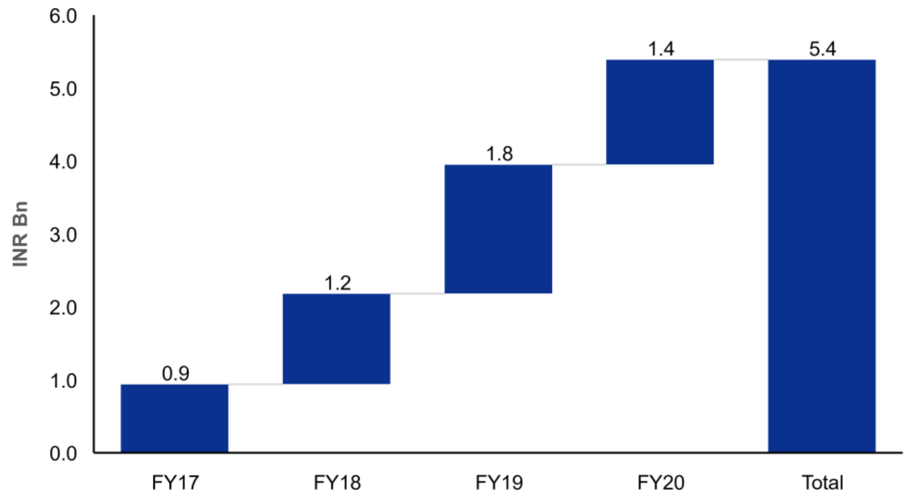
Key examples of successful innovations

Segment	Customer Insight	New Products	Year of launch	Key innovation
Fans	Accumulation of dust on the fans	**Premium Fans** : Aura Anti Dust Fan 	FY17	**Attracts 50% less** dust than regular fans
	Aesthetically appealing Fan with longer warranty	**Premium Fans** : Aura Fluidic 	FY18	**First 5 Year** warranty Fan in India – Duratech Technology
	Ceiling fans disturbs the gas flames while cooking in kitchen	**Premium Fans:** Air Buddy Kitchen Fan 	FY19	**Provides cooling** in the kitchen **without disturbing the flames**
Lighting	Anti-bacterial bulb	**LED**: Anti-bac LED Bulb 	FY19	**Kills micro-organisms/bacteria**
	Lighting coverage area & Energy efficiency	**LED**: LYOR LED Bulb	FY19	**India's first BEE 5 Star** rated energy efficient lamp; delivers light over 270 degrees
Pumps	Existing range doesn't cater to requirements	**Agri. Pump**: Mini Crest, Submersible Pump 	FY18	Redesigned product (spec change) to **lower cost and price**
Small Appliances	Product design aesthetically unappealing	**Air Coolers:** Optimus 	FY18	**Air cooler** with higher cooling, air delivery and lower humidity
	Limited functional properties	**Geysers:** Solarium Neo and Qube	FY19 (revamp)	**Entire range of water heaters** with enhanced aesthetics and features

New products contribute c. 44% of FY19 Revenue

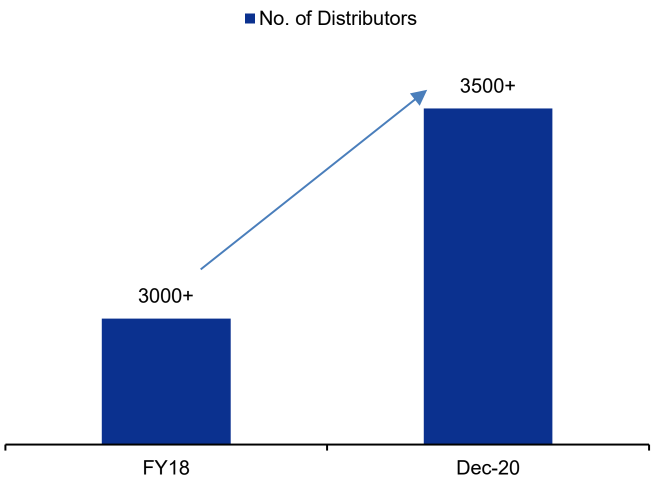
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 71: Crompton's cumulative cost savings of ~Rs5bn over FY17-20



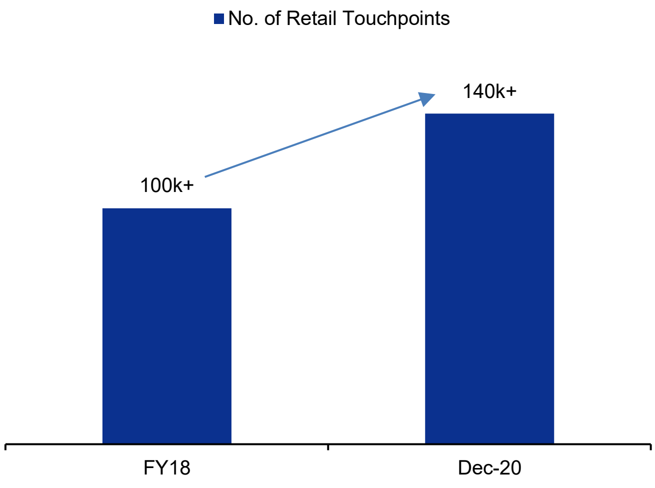
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 72: Crompton's distributor network



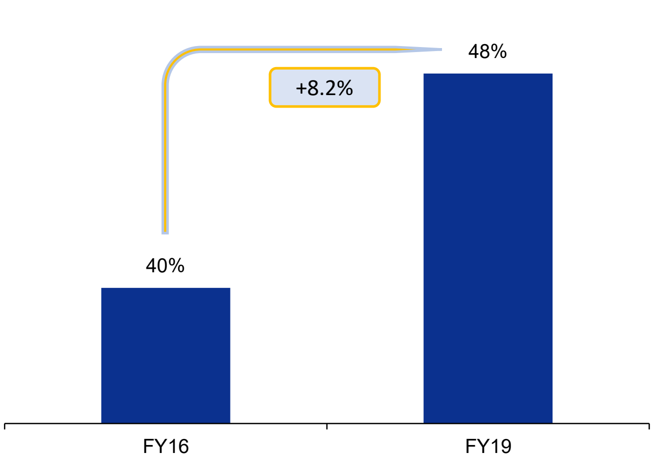
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 73: Crompton's retailer network



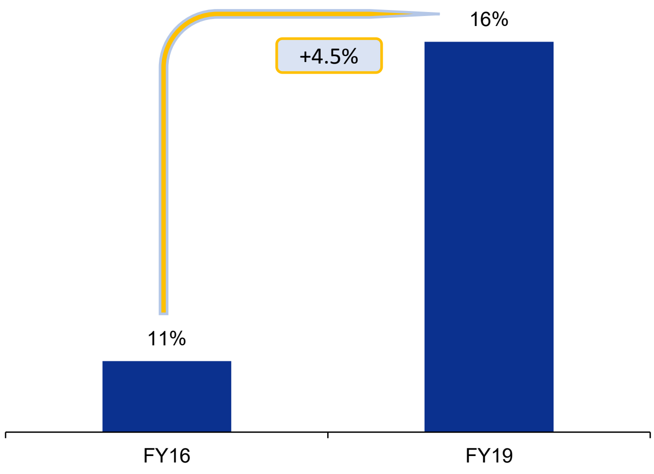
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 74: Crompton's % POS serviced (Fans – pan India)



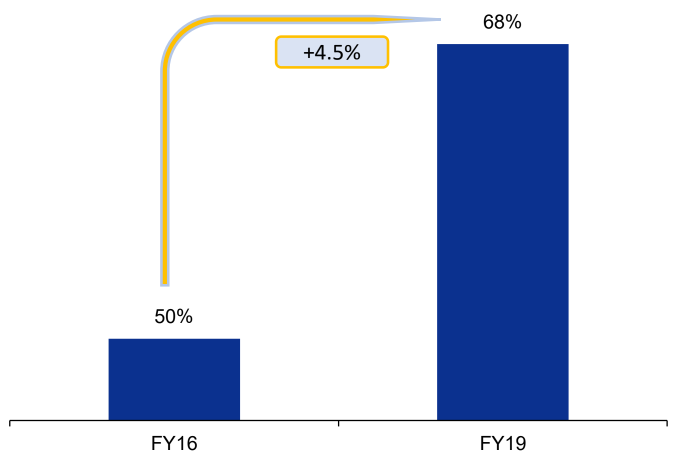
POS IS POINT OF SALE
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 75: Crompton's % POS serviced (LED Lights – pan India)



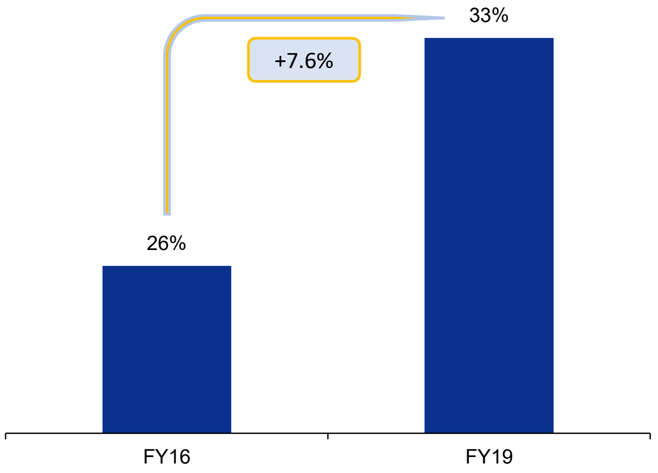
POS IS POINT OF SALE
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 76: Crompton's % POS serviced (Fans – South)



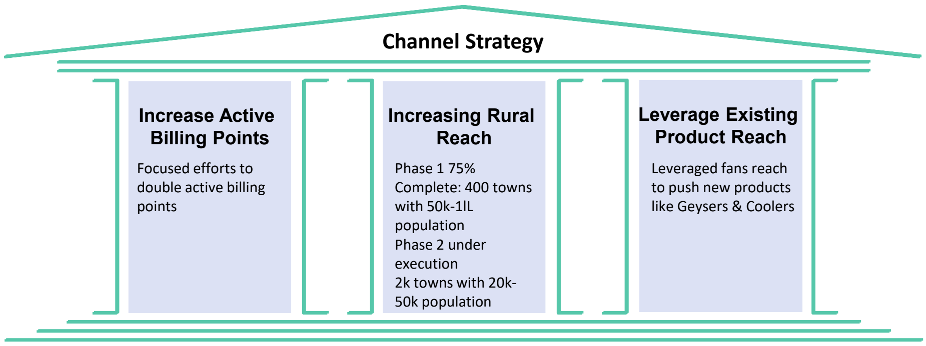
POS IS POINT OF SALE
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 77: Crompton's % POS serviced (LED Lights – South)



POS IS POINT OF SALE
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 78: Crompton's channel strategy



SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 79: Crompton's investment in channel engagement

Enables connections with channel partners and retailers thus helping track secondary sales. Tally patch now covers secondary sales of 76% of CG Consumer's total business

Mobile application that helps each salesperson create a week's plan on visits, calls, and orders.

This also helps the company track performance of sales team.

Dealer Portal helps company's channel partners monitor the status of the orders generated, schemes settlements, stocks etc.

SOURCES: EIP RESEARCH, COMPANY REPORTS

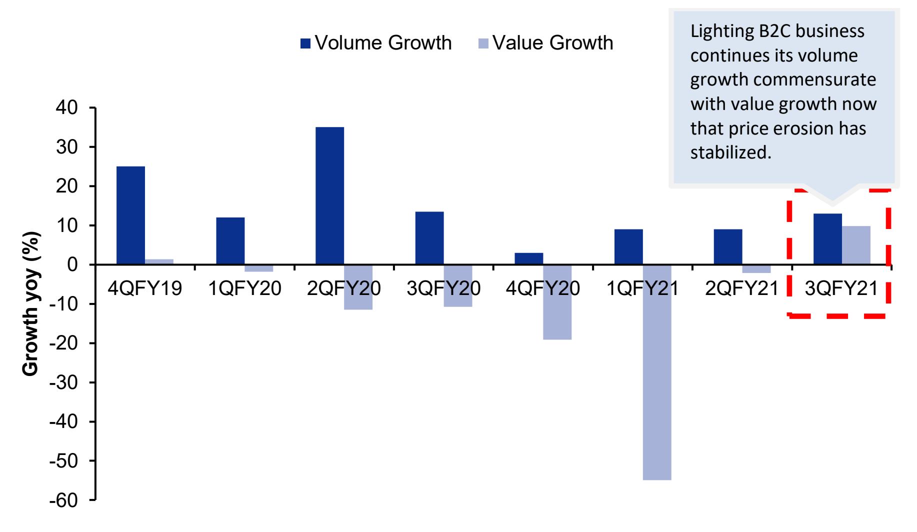
"What has fundamentally happened is that the LED price destruction, which was present for the last few years, seemed to have stopped for the past few quarters and that is extremely encouraging because that enables us to now deliver value, decent margins and continue growing the business."
– 2QFY21 investor conference call

ECD segment to grow faster; recovery in LED pricing augurs well for lighting revenue growth

Lighting revenue growth has been under pressure over FY17-21F even though volumes grew for Crompton due to significant LED price erosion over this period. Leading lighting players have struggled to grow revenues in this period. In 9MFY21, pricing stabilised leading to volume growth, which is now reflected in positive value growth.

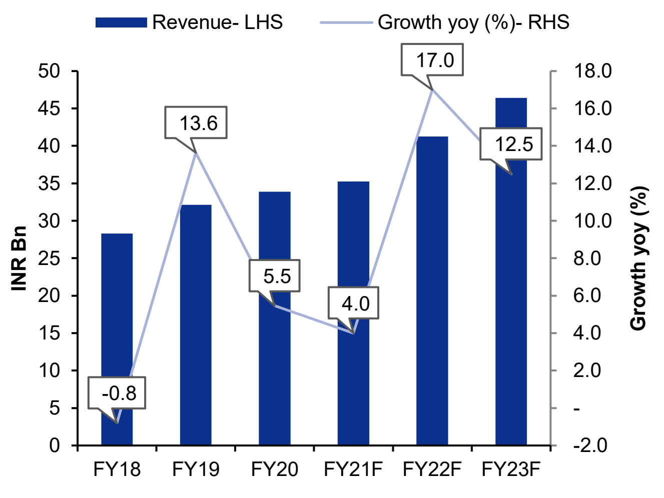
We expect the ECD segment (comprising fans, pumps and appliances) to grow faster than the lighting segment over FY21-23F. We model ECD/lighting revenue CAGR of 14.7%/13.5% respectively over FY21-23F. We estimate consolidated revenue CAGR of 14% over the same period.

Figure 80: Crompton's LED pricing stabilised over 9MFY21 (LED value & volume growth)



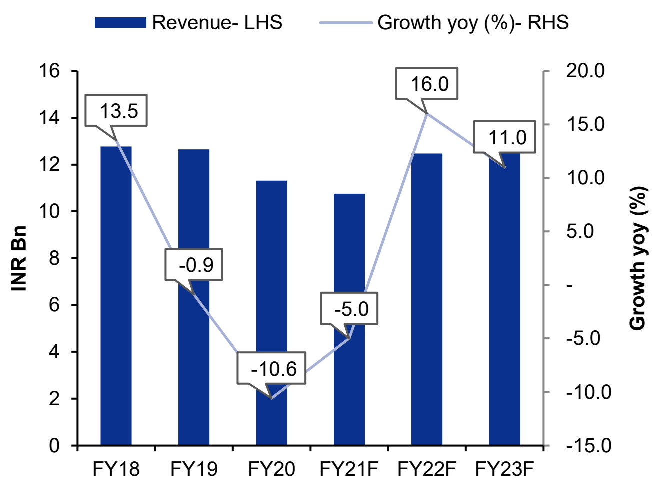
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 81: Crompton's ECD revenue



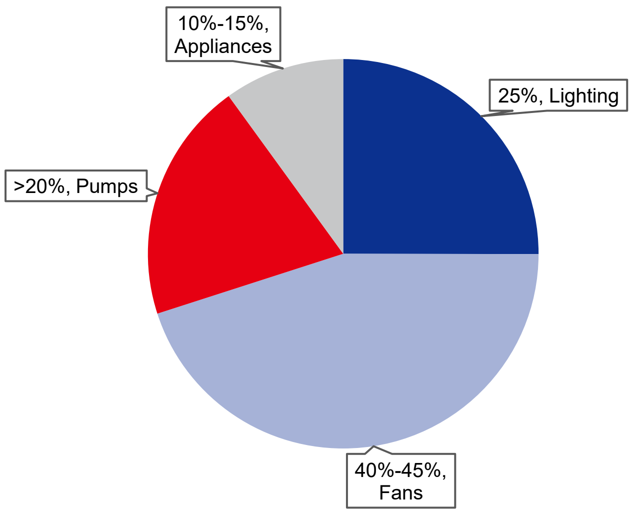
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 82: Crompton's lighting revenue



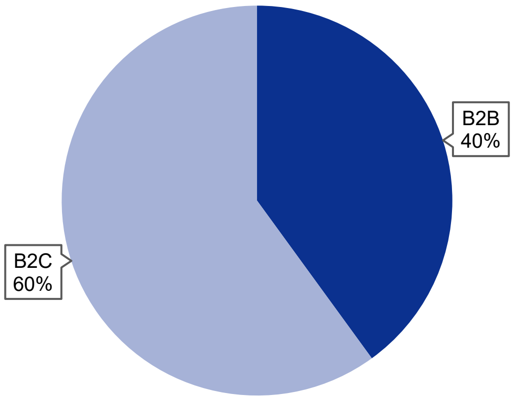
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 83: Crompton's estimated product mix (FY20F)



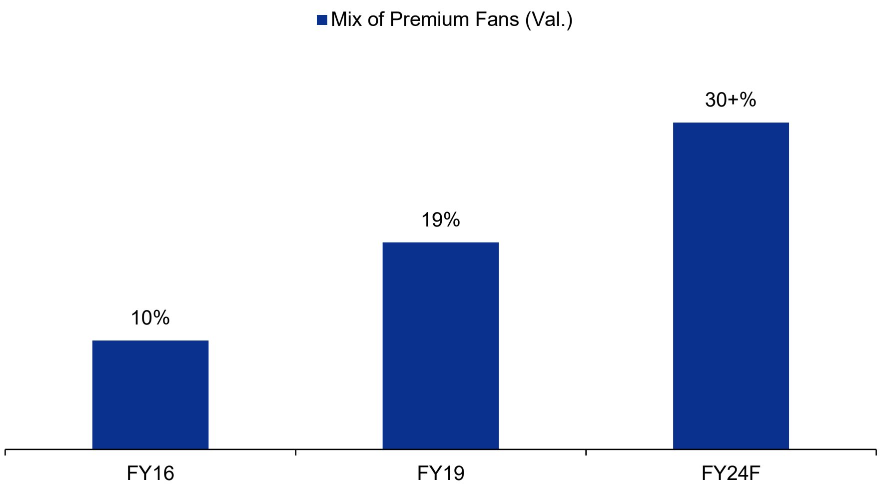
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 84: Crompton's estimated lighting revenue mix (FY21F)



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 85: Industry witnessing shift towards premiumisation



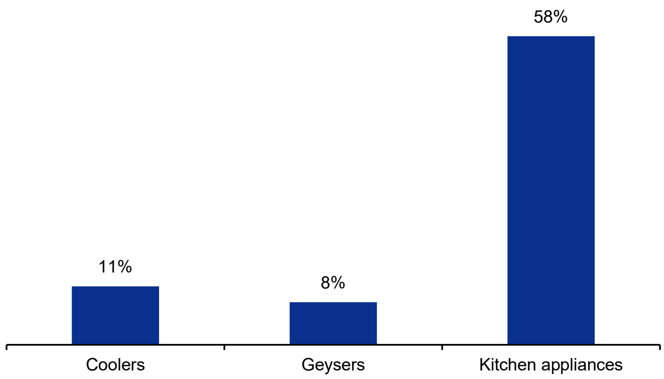
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 86: Crompton's ECD segment opportunity snapshot

	Market Size (INR bn)	Market Growth (CAGR 19-24)
Fans	79	10-12%
Pumps	69	7-9%
Lighting	150	10-12%
Appliances	109	8-10%

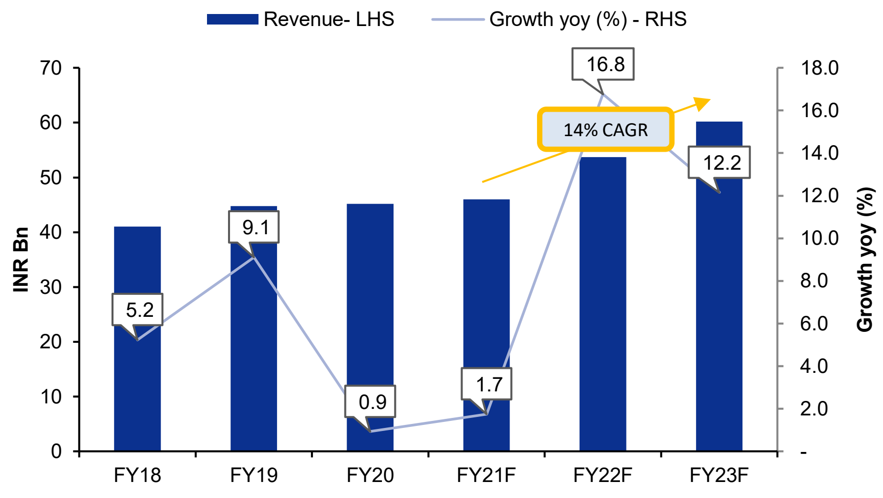
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 87: Low penetration of coolers, geysers and kitchen appliances provide Crompton ample scope for growth



SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 88: Revenue growth to pick up meaningfully over FY21-23F



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

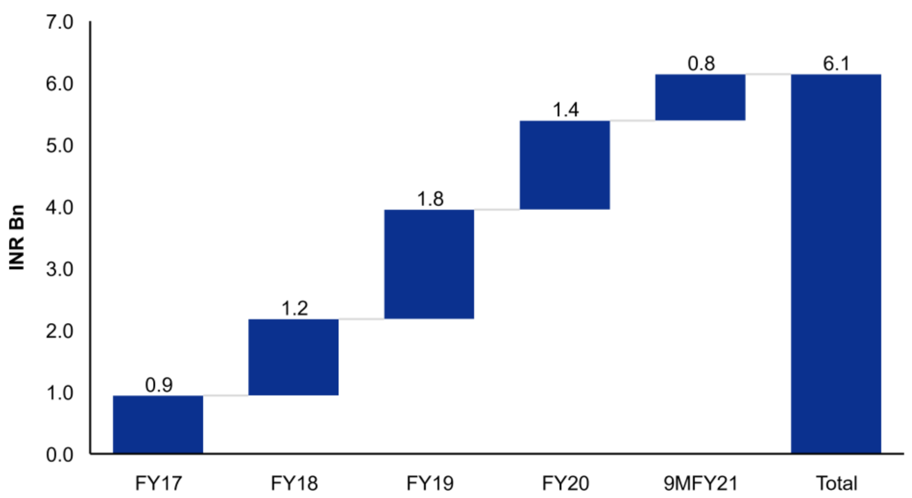
Solid cost rationalisation plans

Saved almost Rs1bn each year over last four years

"I am happy to report that through our cost control program Project Unnati, we have managed to save Rs1.4bn in the year under review. We are ploughing back these savings into disruptive concepts, designs, and technology."
– Chairman's letter to shareholders, FY20 Annual Report

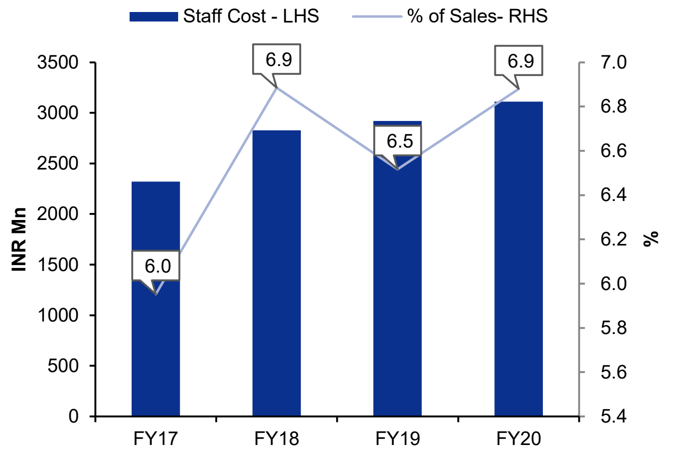
The management team delivered robust cumulative savings of ~Rs5bn over FY17-20. Management has guided for further potential operational cost rationalisation and continued increase in operating margins going forward.

Figure 89: Yearly operating cost savings since FY17



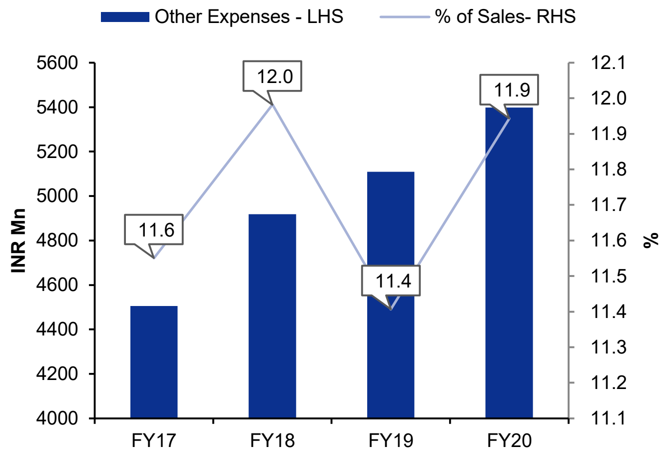
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 90: Crompton's tight control on staff costs



SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 91: … and on other expenses over the years

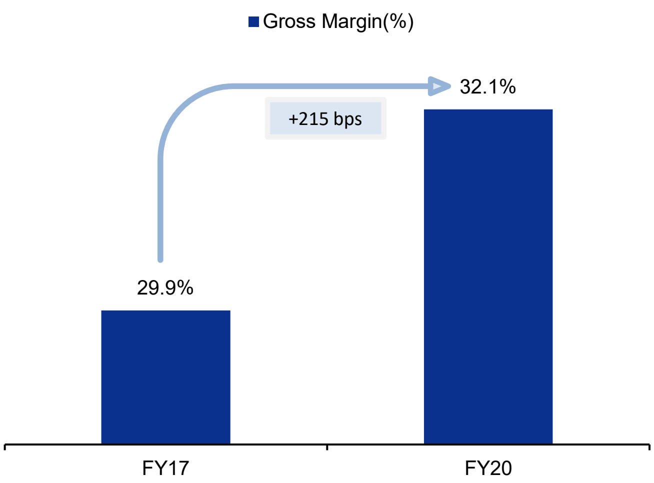


SOURCES: EIP RESEARCH, COMPANY REPORTS

Will likely continue to improve margins over the next three years ➤

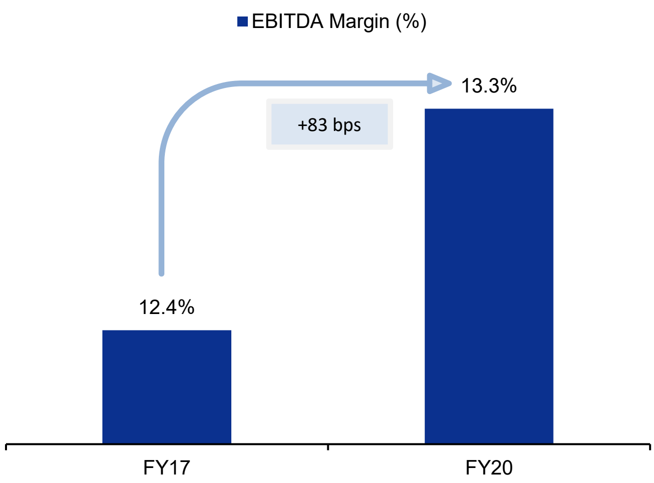
As a result of effective cost management programmes, Crompton improved EBITDA margins in each of the years over FY17-20. EBITDA margins increased by 90bp from 12.4% to 13.3% over this period. Management believes in further potential to cut avoidable costs and continue increasing margins. We model a further 70bp improvement in EBITDA margins to 15.4% over FY21-23F.

Figure 92: Gross margin improvement



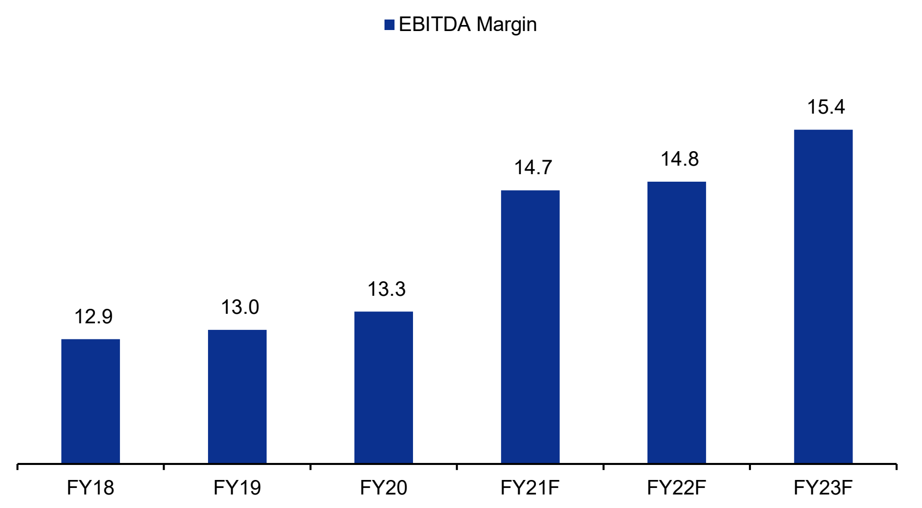
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 93: EBITDA margin improvement



SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 94: EBITDA margin FY18-23F (%)



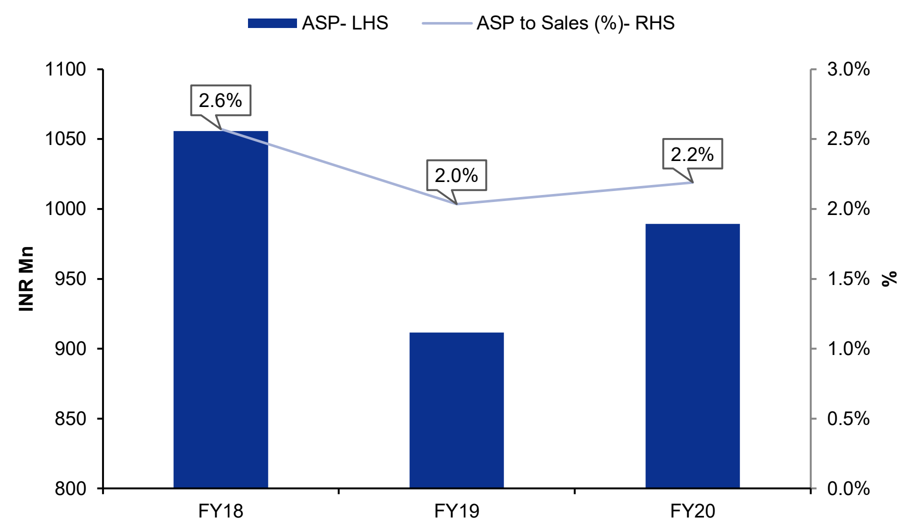
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

"We are leveraging technology significantly and improving our secondary sales tracking has enabled us to take more informed decisions. Our Tally patch now covers secondary sales of 76% of our total business."
– 3QFY21 investor conference call

ASPs have ranged between 2% and 2.5% of sales in FY18-FY20); redeploying cost savings for better tracking of primary/ secondary sales

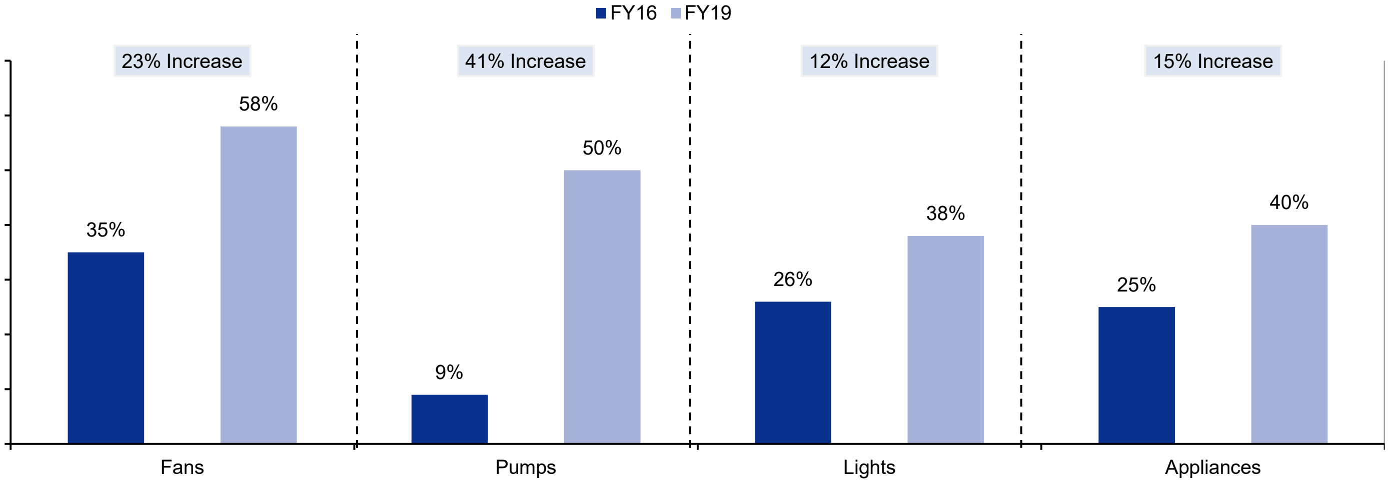
Crompton has historically spent 2-2.5% of sales on advertising and sales promotion. We expect these spends to continue in a similar range going forward. Also, Crompton is the only company in our coverage universe that can now track over ~76% of its secondary sales (as at Dec-2020) from dealer/distributor to retailer/end customer through advanced technology systems.

Figure 95: Crompton's advertising and sales promotion spends



SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 96: Sharp improvement in Crompton brand awareness (%)



BRAND AWARENESS INDICATES THE % PEOPLE THAT SPONTANEOUSLY RECALLED CROMPTON IN A 3RD PARTY SURVEY CONDUCTED FOR FANS, PUMPS, LIGHTS AND APPLIANCES
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 97: Crompton's TV advertisements

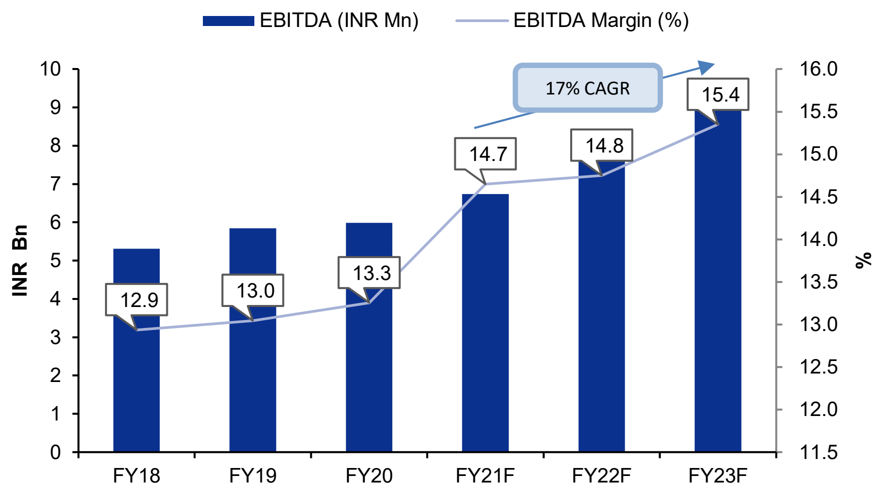
SOURCES: EIP RESEARCH, CROMPTON GREAVES'S ANNUAL REPORTS OF 2019 AND 2020

Figure 98: Crompton's social media advertisements

SOURCES: EIP RESEARCH, CROMPTON GREAVES'S ANNUAL REPORTS OF 2019 AND 2020

EBITDA CAGR of 17% (FY21F-23F) on the back of improving margins

Figure 99: EBITDA and EBITDA margin trend

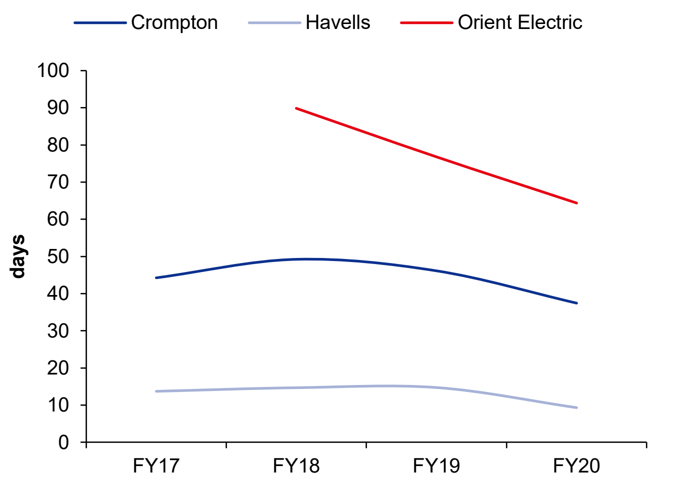


SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Lean balance sheet to maintain optimum mix of in-house and outsourced manufacturing

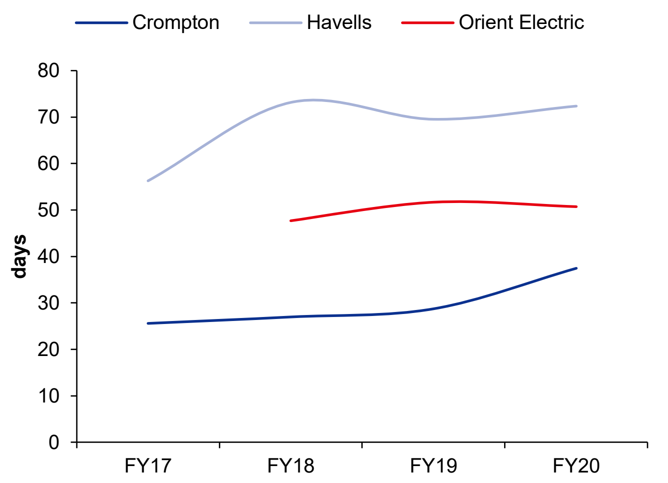
Lean net working capital cycle, strong free cash flows»

Figure 100: Debtor days peer comparison



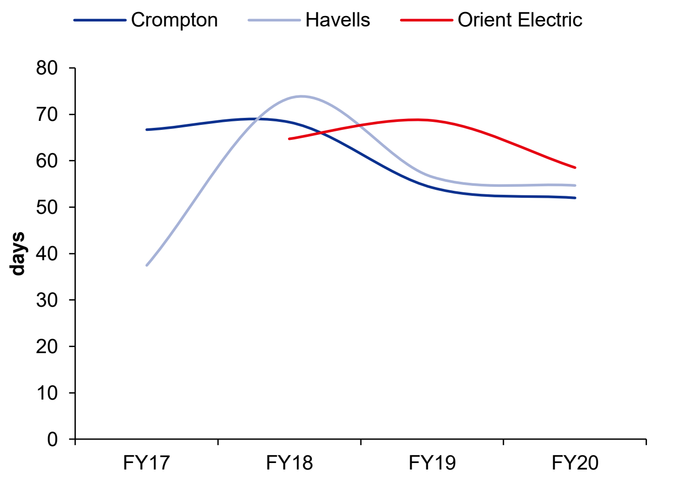
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 101: Inventory days peer comparison



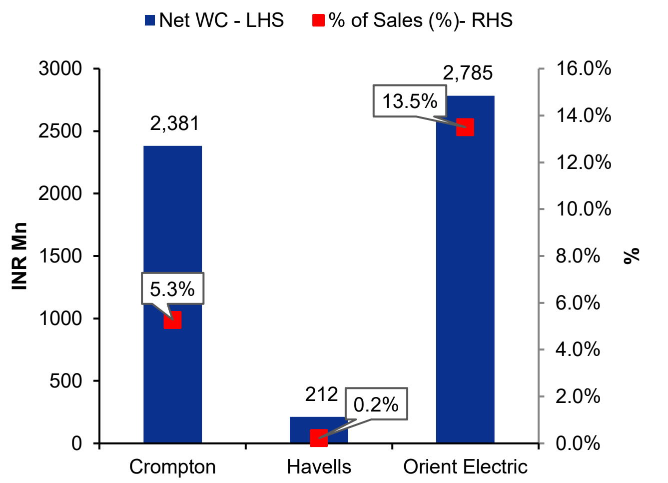
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 102: Creditor days peer comparison



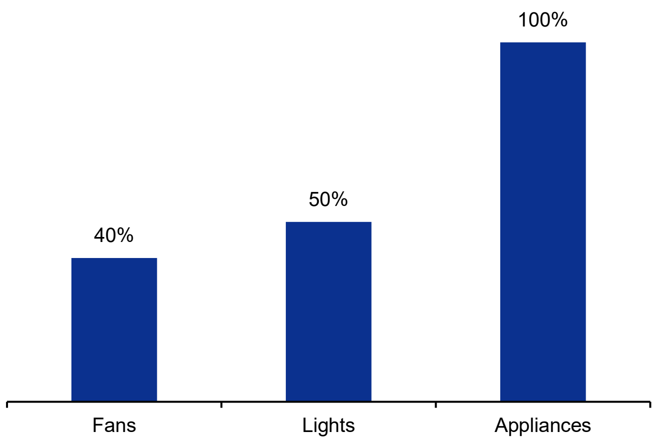
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 103: Net working capital (WC) ex-cash -FY20



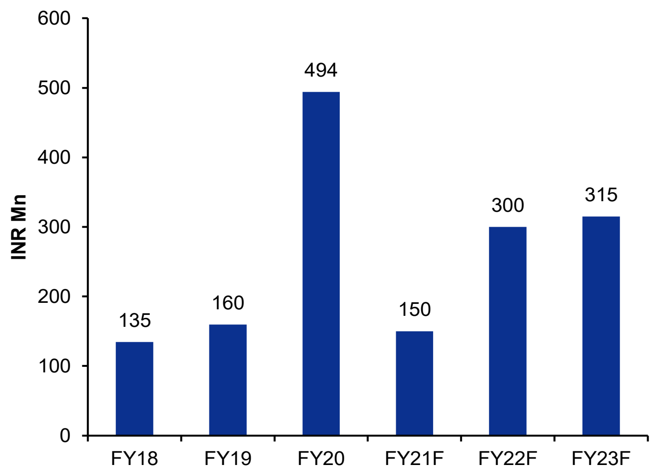
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 104: Crompton's outsourced manufacturing mix (FY21F)



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 105: Estimated annual capex plan

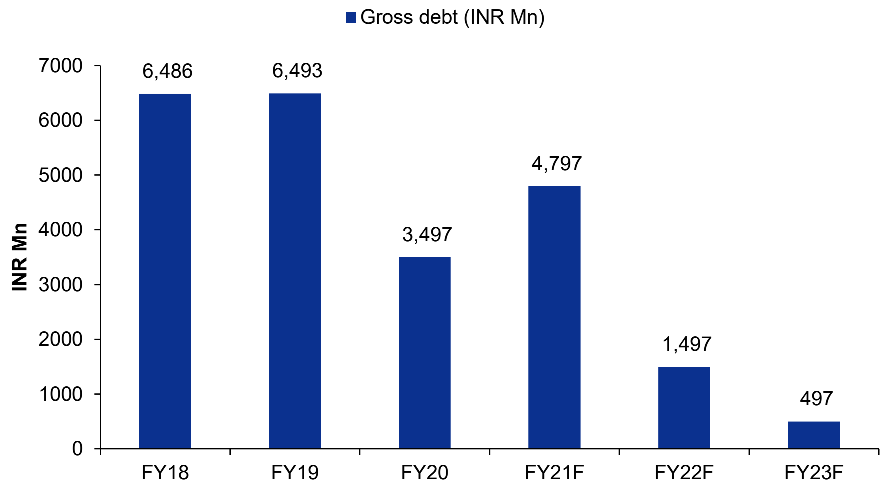


SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Contingency debt will be repaid by Apr 2022

Crompton issued non-convertible debentures (NCD) for Rs3bn in Apr 2020 to tide over any COVID-19 pandemic-related contingencies. We now expect gross debt of Rs4.8bn by Mar 2021, which will likely be repaid by Apr 2022, in our view.

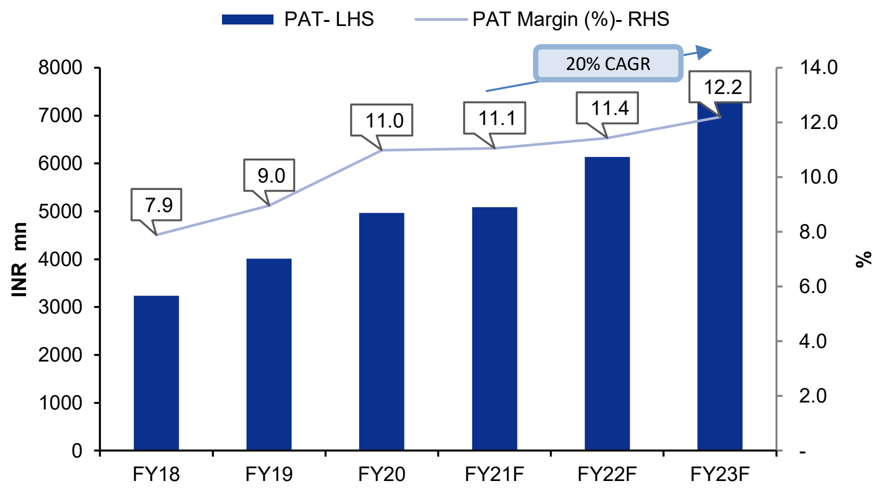
Figure 106: Gross debt reflects contingency debt raised during COVID-19 lockdown



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

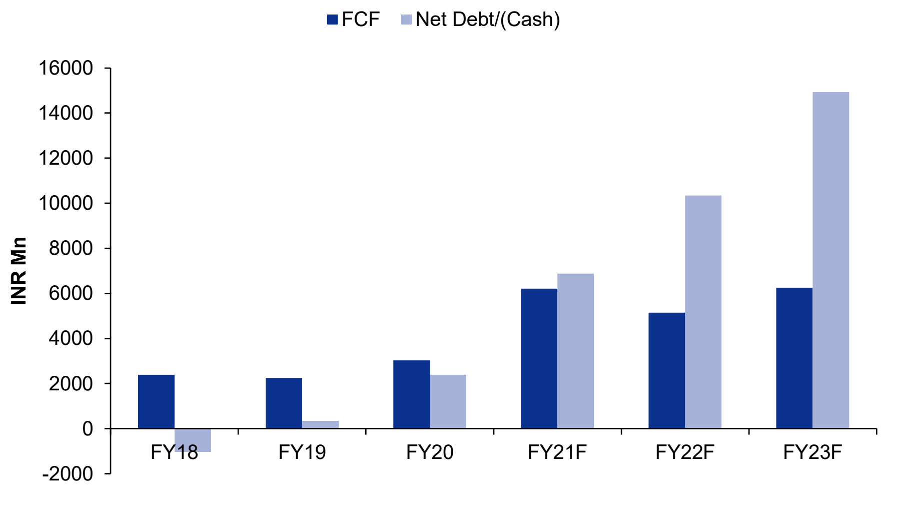
EPS CAGR of 20% over FY21-23F. Expect dividend payouts at ~50% of annual profits

Figure 107: Crompton's PAT and PAT margins



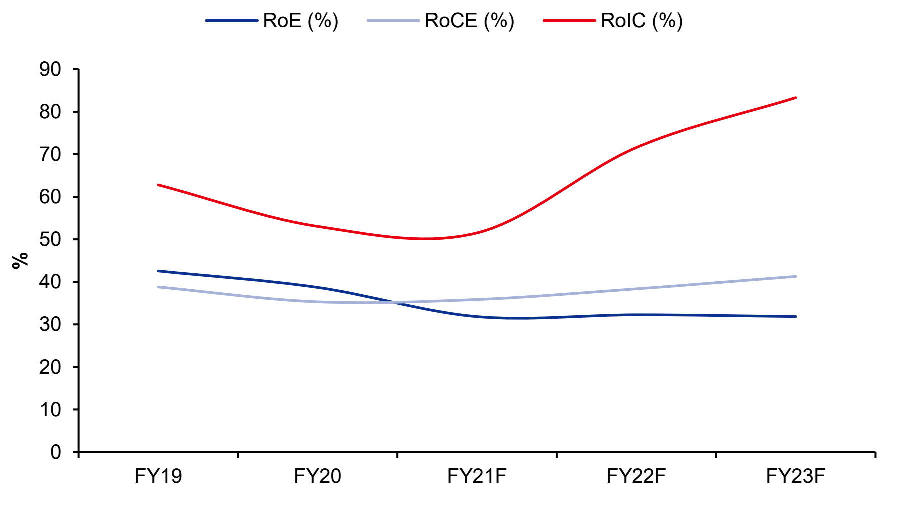
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 108: Healthy free cash flow generation



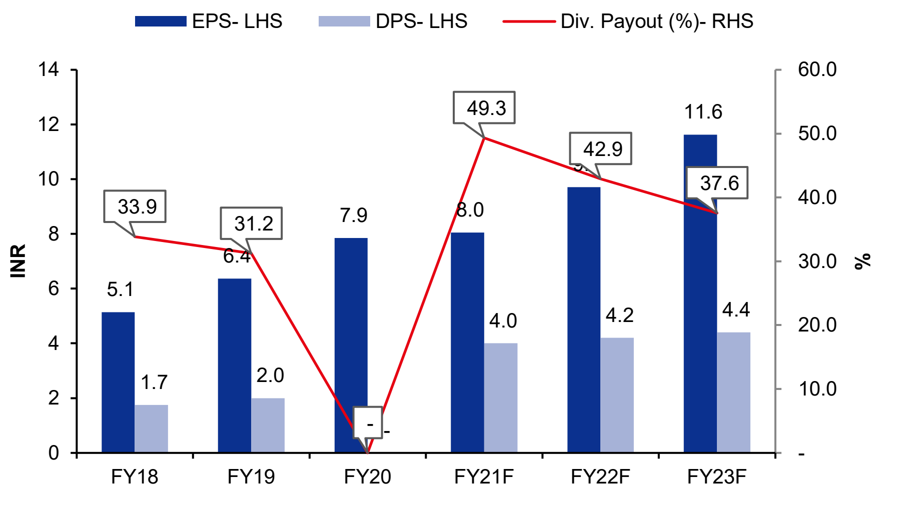
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 109: Return ratios consistently strong



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 110: Dividend payout at 40-50% of annual profits



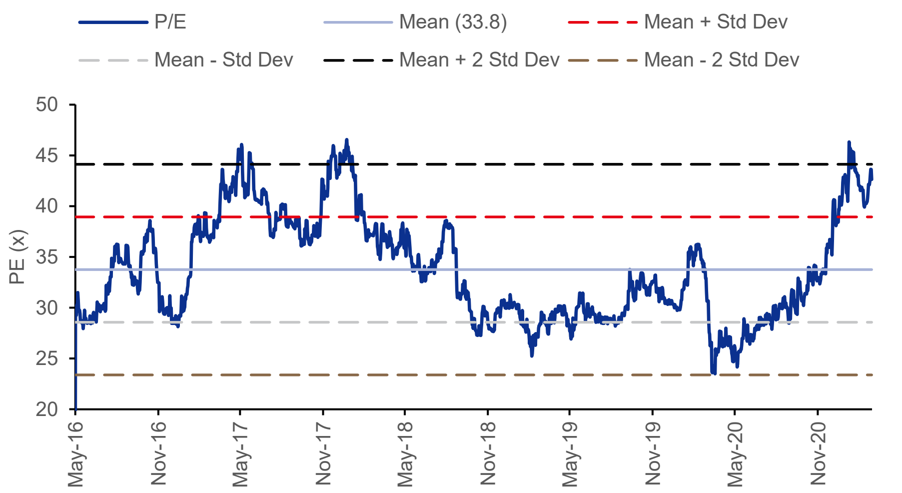
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Initiate with Add rating, target price of Rs465

Valuation

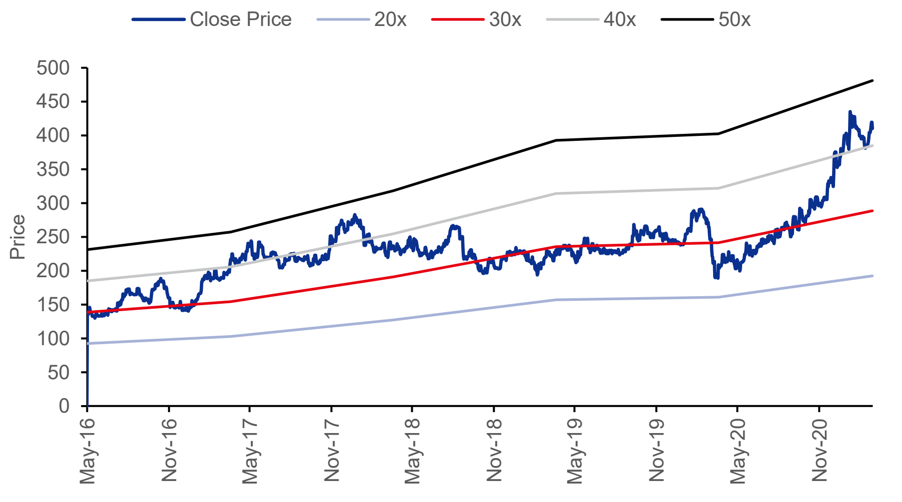
- Consistent market share gains over the past five years, robust cost savings plan execution and solid cash flow growth over FY17-20, combined with further scope for EBITDA margin improvement and net profit growth underpins our positives view on the stock.
- RoE/RoCE are estimated at 32%/41% in FY23F. Cumulative free cash flow generation is estimated to be of Rs17.6bn over FY21-23F.
- Crompton Greaves is an independent professionally managed entity with no promoter family ownership. Advent International and Temasek Holdings – the two major private equity holders – have now have balance equity stake of 5.4% and 6% (as of Feb 2021) respectively in the company.
- The stock trades at P/E of 35.3x and EV/EBITDA of 26.4x it FY23F estimates.
- We expect strong net profit CAGR of 20% over FY21-23F and hence value Crompton at Rs465 based on 40x FY23F EPS (~20% premium to its five-year mean P/E of ~34x. We initiate coverage with an Add rating with upside potential of ~13%.
- We think the recovery of macro demand drivers for the consumer electrical sector coupled with consistent superior performance in terms of market share gains and EBITDA margin increase by the company would attract higher valuation multiples for Crompton. A base case assumption of 20% premium to its historical five year mean P/E is justified given the strong profit momentum expected to continue till FY23F, in our view.

Figure 111: Crompton trades near +2SD to its five-year mean P/E (1 year forward)



SOURCES: EIP RESEARCH, COMPANY REPORTS, BLOOMBERG

Figure 112: PE band chart



SOURCES: EIP RESEARCH, COMPANY REPORTS, BLOOMBERG

Downside risks

- **Market share loss:** Crompton has consistently gained market share in its core product portfolio of fans and residential pumps. Market share loss in these segments could impact our revenue estimates negatively.
- **Delay in product launches:** Crompton has consistently revamped its product portfolio and upgraded products in existing categories. New products and adapting new technologies are very important for Crompton to stay relevant in the market place. Delays in new product roll-outs could negatively impact our revenue growth assumptions.
- **Cost savings may be peaking:** Crompton's operating margins continuously improved over FY17-20 on the back of consistent cost savings programmes. Though management has guided for further improvements in margins, the cost programmes would have peaked and limited benefits could flow through on cost savings going forward.
- **High competition:** The company is planning to be among the Top 3 players in the consumer appliances category for products such as water heaters, air coolers and mixer grinder. There are large pan-India brands present in each of these appliance categories. High competition by incumbents could impact Crompton's success in new products.

Business description and management profile

Crompton is one of India's leading consumer electrical companies present in the Electrical Consumer Durables "ECD" and Lighting segment. It manufactures and distributes a wide range of consumer products ranging from Fans, Pumps and Appliances (Water Heaters, Air Coolers, Mixer Grinders, Iron) in the ECD segment, and a full range of Lighting products. Your Company is a market leader in Fans, Domestic Pumps and Street Lighting segments.

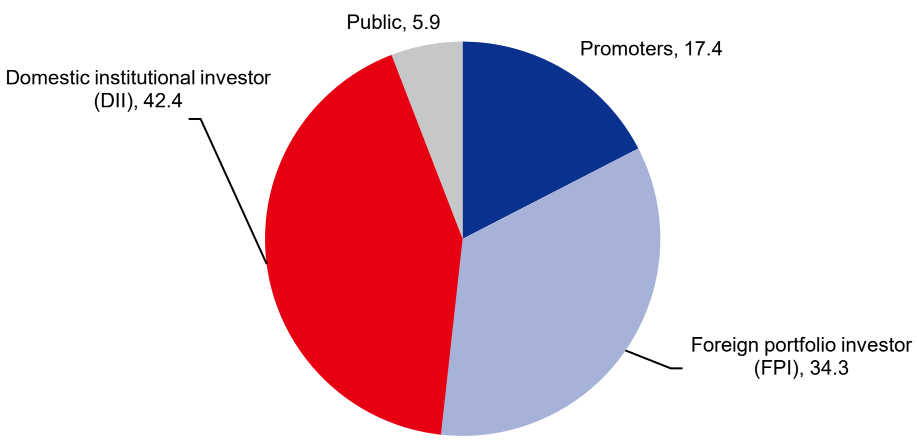
The board of directors consists of seven members, three independent and non-independent directors each and one Managing Director.

Figure 113: Key management profile (FY20)

Name and Designation	Profile
Mr. Shantanu Khosla, Managing Director	Mr. Khosla holds a Bachelor's degree in Mechanical Engineering from Indian Institute of Technology, Bombay and MBA from Indian Institute of Management, Calcutta. Prior to joining CGCEL, he served as the Managing Director and Chief Executive Officer (CEO) of Procter & Gamble from July 2002 to June 2015. Committee Membership at CGCEL: Stakeholders' Relationship and Share Transfer Committee and Corporate Social Responsibility Committee.
Mr. Mathew Job, Chief Executive Officer	Mr. Job holds a Bachelor's degree in Technology (Electrical and Electronics) from University of Kerala and MBA from Indian Institute of Management, Calcutta. Prior to joining CGCEL, he served as the Managing Director of Racold (Ariston) Thermo Limited till September 2015. Prior to that, he was the Vice President and Managing Director of Grohe India Private Limited from November 2009 to January 2012 and also held various key roles with Philips Electronics India Limited from June 1994 to October 2009.
Mr. Sandeep Batra, Chief Financial Officer	Mr. Batra is a qualified Chartered Accountant as well as a Company Secretary and is an alumnus of the prestigious St. Xavier's College, Calcutta. Prior to joining CGCEL, he served as the Chief Financial Officer of Pidilite Industries Limited. Prior to that, he was associated with ICI Limited from January 1988 to January 2009, wherein he held various positions and eventually assumed the role of CFO.
Ms. Pragya Kaul, Company Secretary	Ms. Kaul is a qualified Company Secretary as well as holds a Bachelor's degree in Law (LLB) and a Diploma in Business Management. She has over 16 years of experience and has worked with Welspun Group, Bajaj Group and Hindustan Dorr-Oliver Limited as Company Secretary and Compliance Officer prior to joining CGCEL.

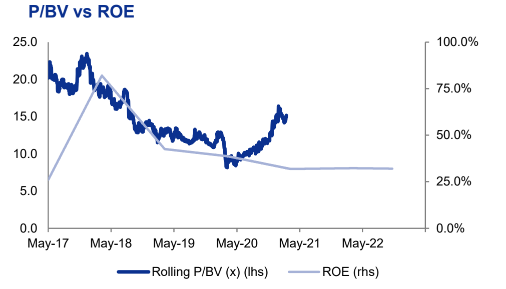
SOURCES: COMPANY WEBSITE

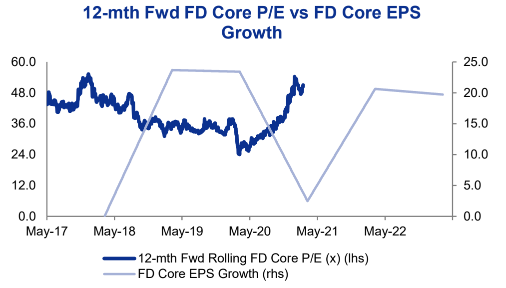
Figure 114: Share Holding Pattern (Dec 2020)



SOURCES: EIP RESEARCH, BSE WEBSITE

BY THE NUMBERS





Profit & Loss

(Rs mn)	Mar-19A	Mar-20A	Mar-21F	Mar-22F	Mar-23F
Total Net Revenues	**44,789**	**45,203**	**45,993**	**53,704**	**60,230**
Gross Profit	**13,871**	**14,499**	**14,718**	**17,185**	**19,424**
Operating EBITDA	**5,843**	**5,991**	**6,738**	**7,921**	**9,245**
Depreciation And Amortisation	(129)	(268)	(311)	(359)	(405)
Operating EBIT	**5,714**	**5,723**	**6,427**	**7,563**	**8,841**
Financial Income/(Expense)	(131)	167	350	617	957
Pretax Income/(Loss) from Assoc.					
Non-Operating Income/(Expense)	15	17	20	20	20
Profit Before Tax (pre-EI)	**5,598**	**5,907**	**6,797**	**8,200**	**9,817**
Exceptional Items					
Pre-tax Profit	**5,598**	**5,907**	**6,797**	**8,200**	**9,817**
Taxation	(1,585)	(943)	(1,711)	(2,064)	(2,471)
Exceptional Income - post-tax					
Profit After Tax	**4,014**	**4,964**	**5,086**	**6,136**	**7,347**
Minority Interests					
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	**4,014**	**4,964**	**5,086**	**6,136**	**7,347**
Recurring Net Profit	4,014	4,964	5,086	6,136	7,347
Fully Diluted Recurring Net Profit	**4,014**	**4,964**	**5,086**	**6,136**	**7,347**

Cash Flow

(Rs mn)	Mar-19A	Mar-20A	Mar-21F	Mar-22F	Mar-23F
EBITDA	5,843	5,991	6,738	7,921	9,245
Cash Flow from Invt. & Assoc.					
Change In Working Capital	(1,208)	(721)	1,751	(106)	(89)
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense					
Other Operating Cashflow	55	112	370	637	977
Net Interest (Paid)/Received	292	173	(350)	(617)	(957)
Tax Paid	(1,994)	(1,446)	(1,711)	(2,064)	(2,471)
Cashflow From Operations	**2,989**	**4,109**	**6,798**	**5,772**	**6,705**
Capex	(160)	(494)	(150)	(300)	(315)
Disposals Of FAs/subsidiaries	4	11			
Acq. Of Subsidiaries/investments	(1,787)	363	(1,000)	(1,000)	(1,000)
Other Investing Cashflow	259	209	791	940	1,090
Cash Flow From Investing	**(1,683)**	**89**	**(359)**	**(360)**	**(225)**
Debt Raised/(repaid)		(3,088)	1,300	(3,300)	(1,000)
Proceeds From Issue Of Shares	38	52			
Shares Repurchased					
Dividends Paid	(1,312)	(1,506)	(2,509)	(2,635)	(2,760)
Preferred Dividends					
Other Financing Cashflow	(587)	(586)	(440)	(324)	(133)
Cash Flow From Financing	**(1,862)**	**(5,128)**	**(1,649)**	**(6,258)**	**(3,893)**
Total Cash Generated	(555)	(929)	4,789	(846)	2,587
Free Cashflow To Equity	**1,306**	**1,110**	**7,739**	**2,112**	**5,480**
Free Cashflow To Firm	**710**	**3,792**	**5,998**	**5,089**	**6,347**

SOURCES: EIP RESEARCH, COMPANY REPORTS

BY THE NUMBERS…cont'd

Balance Sheet

(Rs mn)	Mar-19A	Mar-20A	Mar-21F	Mar-22F	Mar-23F
Total Cash And Equivalents	6,843	5,889	11,679	11,833	15,419
Total Debtors	5,660	4,635	5,040	5,885	6,601
Inventories	3,524	4,636	3,780	4,414	4,950
Total Other Current Assets	1,173	2,257	1,260	1,471	1,650
Total Current Assets	**17,199**	**17,417**	**21,759**	**23,603**	**28,620**
Fixed Assets	837	1,296	1,313	1,255	1,165
Total Investments					
Intangible Assets	7,794	7,794	7,794	7,794	7,794
Total Other Non-Current Assets	866	1,012	833	833	833
Total Non-current Assets	**9,498**	**10,102**	**9,940**	**9,882**	**9,792**
Short-term Debt	3,000	1,700	2,332	728	242
Current Portion of Long-Term Debt					
Total Creditors	6,650	6,436	6,930	8,092	9,076
Other Current Liabilities	2,407	2,711	2,520	2,943	3,300
Total Current Liabilities	**12,058**	**10,847**	**11,782**	**11,763**	**12,618**
Total Long-term Debt	3,493	1,797	2,465	769	256
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	173	191	191	191	191
Total Non-current Liabilities	**3,666**	**1,988**	**2,656**	**961**	**447**
Total Provisions					
Total Liabilities	**15,723**	**12,835**	**14,439**	**12,723**	**13,064**
Shareholders Equity	10,973	14,683	17,260	20,762	25,348
Minority Interests					
Total Equity	**10,973**	**14,683**	**17,260**	**20,762**	**25,348**

Key Ratios

	Mar-19A	Mar-20A	Mar-21F	Mar-22F	Mar-23F
Revenue Growth	9.1%	0.9%	1.7%	16.8%	12.2%
Operating EBITDA Growth	10.0%	2.5%	12.5%	17.6%	16.7%
Operating EBITDA Margin	13.0%	13.3%	14.7%	14.7%	15.4%
Net Cash Per Share (Rs)	0.55	3.79	10.89	16.35	23.61
BVPS (Rs)	17.40	23.23	27.31	32.85	40.11
Gross Interest Cover	9.59	14.07	14.60	23.37	66.30
Effective Tax Rate	28.3%	16.0%	25.2%	25.2%	25.2%
Net Dividend Payout Ratio	27.0%		36.9%	32.1%	28.1%
Accounts Receivables Days	45.62	41.56	38.39	37.13	37.83
Inventory Days	38.70	48.50	49.11	40.95	41.88
Accounts Payables Days	84.60	77.78	78.00	75.08	76.78
ROIC (%)	62.8%	53.0%	51.5%	71.5%	83.3%
ROCE (%)	38.8%	35.3%	35.9%	38.4%	41.3%
Return On Average Assets	22.5%	21.2%	21.8%	23.3%	24.6%

SOURCES: EIP RESEARCH, COMPANY REPORTS

CGSCIMB

INITIATION

InCred

Company Note

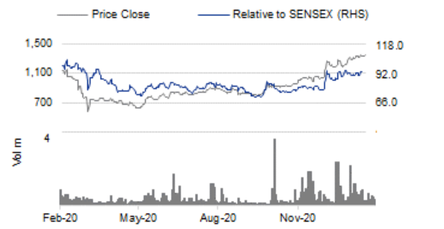
Industrial - Overall | India | March 15, 2021

India

ADD *(Initiating coverage)*

Consensus ratings*:	Buy 18 Hold 4 Sell 0
Current price:	Rs1,360
Target price:	Rs1,530
Previous target:	N/A
Up/downside:	12.5%
EIP Research / Consensus:	12.0%
Reuters:	POLC.NS
Bloomberg:	POLYCAB IN
Market cap:	US$2,785m
	Rs2,02,717m
Average daily turnover:	US$7.2m
	Rs527.4m
Current shares o/s:	149.1m
Free float:	31.6%

**Source: Bloomberg*



Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	2.3	30.9	55.3
Relative (%)	3.8	18.8	9.2

Major shareholders	% held
Promoters	68.4
INTERNATIONAL FINANCE	5.6
ANIL HARIRAM HARIANI	3.3

Polycab India Ltd.

Wired for the long haul

- Market leadership and incremental share gains to continue in Indian markets, exports and import substitution enhance addressable market potential.
- Leaner balance sheet can lead to higher return ratios and free cash flow.
- Scale advantage and transformation into a leading electrical consumer brand should lead to higher valuation multiples. Initiate coverage with Add rating.

Well-rounded growth with focus on multiple growth levers

Within the Indian market, Polycab is expanding its reach to tier-2 and below cities (~25% of FY20 sales) to drive revenue growth. India is a net exporter of cables and wires (C&W) and Polycab intends to grow its exports to 10% (~5% currently) of overall sales in the medium term by establishing distributors across USA, Australia, Asia and Middle East. Polycab is further expanding its C&W addressable market with the focus on developing specialty cables (used in defence, aviation, etc) to substitute imports. Moreover, we expect the share of business to consumer (B2C) revenue to go up led by higher growth in FMEG on the back of investments into brand recognition, digital initiatives and new product launches.

Captive manufacturing and backward integration support margins

Polycab manufactures most of its products in-house and believes self-control on supply chain management is key to efficient inventory management and quality control. Over the past five years, the company has incurred capex of Rs12.8bn to augment capacities across product lines while also investing in backward integration – captive processing of cathodes into copper rods. As a result, Polycab has been able to improve gross and EBITDA margins by 460bp and 350bp, respectively, over FY16-20. We expect EBITDA CAGR of 10.6% and the margins to be maintained at FY21F levels over FY21-23F.

Scope for improving working capital management and return ratios

The working capital (WC) cycle improved to 77 days from 94 days of sales over FY16-FY20. There is further scope to rationalize WC investments and Polycab has appointed external consultants for feedback. We await clarity on implementation of these initiatives but believe WC investment could gradually taper over the medium term. We estimate RoE of 17.1% and RoCE of 21.8% in FY22F and FCF of Rs17.7bn over FY21-23F.

Valuation and risks

The stock trades at 21.3x FY23F P/E (+2SD to mean P/E of 15.1x since listing in Apr 2019) and 12.9x FY23F EV/EBITDA. Superior FMEG business performance partially led to re-rating post its listing, in our view. We think valuation multiples could expand over time for the stock as it leverages its market leadership and transforms into a larger B2C brand. We value the stock at Rs1,530, based on 24x FY23F EPS and initiate coverage with an Add rating. Downside risks: Volatile raw material prices, adverse forex rates and slower FMEG revenue growth.

Financial Summary	Mar-19A	Mar-20A	Mar-21F	Mar-22F	Mar-23F
Revenue (Rsm)	79,856	88,299	88,875	1,04,070	1,15,913
Operating EBITDA (Rsm)	9,530	11,350	11,598	12,749	14,199
Net Profit (Rsm)	5,006	7,656	8,685	8,439	9,505
Core EPS (Rs)	35.4	52.7	57.6	56.6	63.8
Core EPS Growth	37.6%	48.6%	9.4%	(1.8%)	12.6%
FD Core P/E (x)	38.35	25.44	23.06	24.03	21.32
DPS (Rs)	0.0	10.0	7.5	11.0	12.0
Dividend Yield	0.00%	0.91%	0.55%	0.81%	0.88%
EV/EBITDA (x)	21.23	17.73	16.56	14.78	12.90
P/FCFE (x)	73.56	(129.51)	134.70	50.65	34.53
Net Gearing	(1.6%)	(4.3%)	(23.4%)	(27.2%)	(32.4%)
P/BV (x)	6.74	5.15	4.42	3.84	3.35
ROE	19.3%	22.9%	20.4%	17.1%	16.8%
% Change In Core EPS Estimates					
EIP Research/Consensus EPS (x)			1.09	0.92	0.90

SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS. PRICED AS AT 12 MAR 2021

Analyst(s)

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Wired for the long haul

Well-rounded growth; focus on multiple growth levers

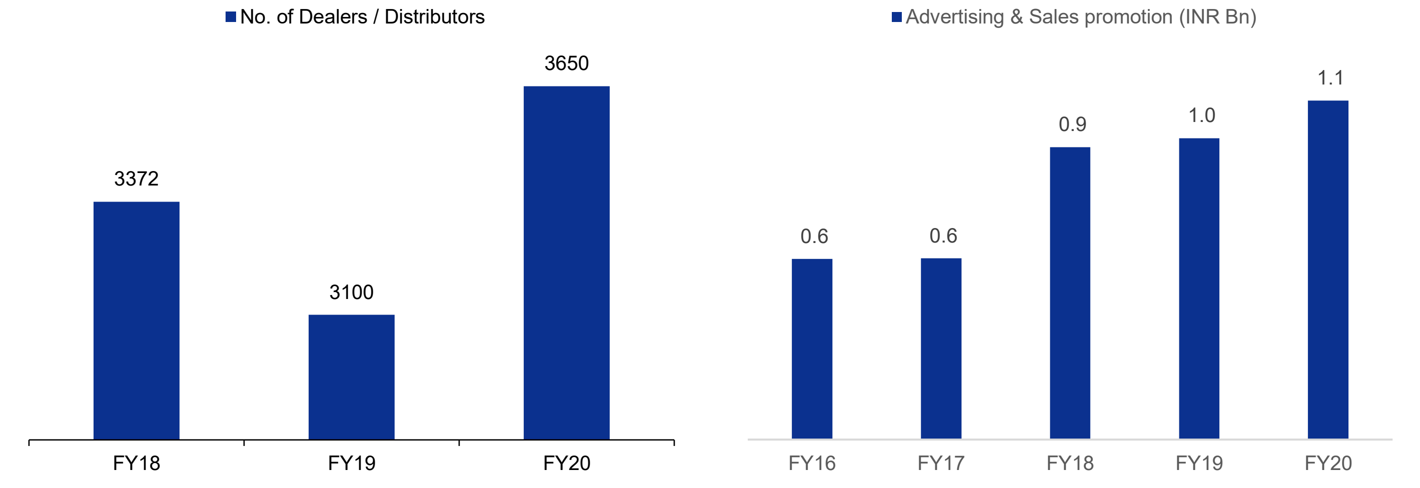
Polycab is focusing on:

- Widening dealer/distributor reach into tier-2/-3 towns and brand building
- Replicating the Indian distributor strategy to develop export markets by establishing a local presence in other countries
- Building specialty cable business and enabling cable import substitution
- Increasing its B2C product basket, led by FMEG products

Widening dealer/distributor reach into tier-2/-3 towns and commitment to brand building ➤

We believe Polycab has been investing in advertising and promotional spends for higher brand recall, to change its perception to a pan India consumer electrical product brand and to increase its product availability across tier-2/-3 towns to deliver strong revenue growth going forward.

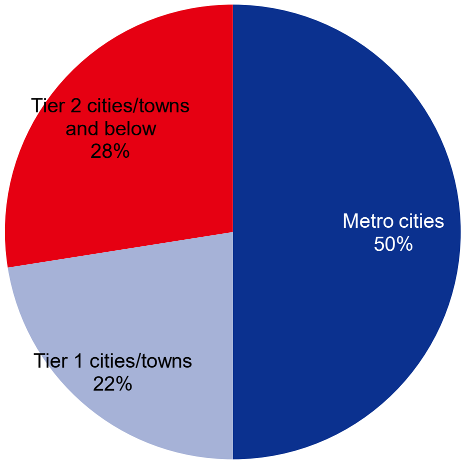
Figure 115: Penetration in tier-2/-3 towns (led by increasing distributor network) and investment in brand building to drive topline



SOURCES: EIP RESEARCH, COMPANY REPORTS

SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 116: Currently (FY20) ~28% of revenue comes from tier-2/-3 towns



SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 117: Polycab investing in brand building

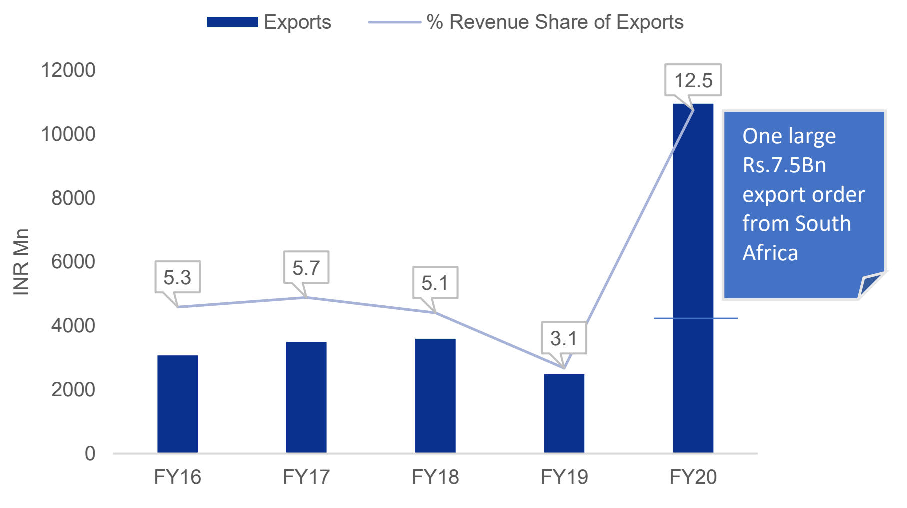
SOURCES: EIP RESEARCH, AFAQS.COM, INSIDESPORT.IN

Replicating Indian distributor strategy to develop export markets and establish local presence

"Expectation is that at least we should get 10% top line from exports."
- Company management on the 3QFY21 analyst conference call

Domestic markets accounted for 87.5% of FY20 revenues while exports stood at 12.5%. The company has undertaken various initiatives to grow faster in international markets by entering new geographies like USA, Australia, Asia and Middle East as well as launching new product segments. We believe Polycab will deepen its market presence further through FMEG exports and overall exports to be ~10% of overall business in the next five years.

Figure 118: Entering new markets to drive exports



SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 119: Management is driving international tie-ups to widen export reach (BASEC tie up for UK)

Case Study

International Cable Supply

Achieving global expansion, through the export of cable products into Europe and the United Kingdom

Established in 1964 as 'Sind Electric Stores', which dealt in various electrical products including fans, lighting, switches, and wires. In 1996, the Company was incorporated as 'Polycab Wires Private Limited' at Mumbai as a private limited company under the Companies Act, 1956. The India-based cable manufacturer Polycab India Limited has experienced significant growth over more than four decades in operation, enabled by third party testing and certification.

Manufacturing a range of wires, cables and electrical products across 25 facilities, Polycab has aligned product offering to market needs. Quality is at the forefront of their cable production processes.

Why BASEC?

Partnering with BASEC since 2009, for PCR management systems approval and 2011 for its first product approval, has meant that Polycab could obtain the competency required to access these very important markets and achieve competitive edge over other cable manufacturers based in the region.

In order to grow the business Polycab's research team are focused on construction building wires and telecommunications infrastructure markets. As the experts in cable testing and certification, BASEC's team has supported the transfer of cabling industry which in turn supports manufacturer's new market diversification goals.

Central to Polycab's international export market success, BASEC approvals pathed the way for the successful creation of strong distributor relationships.

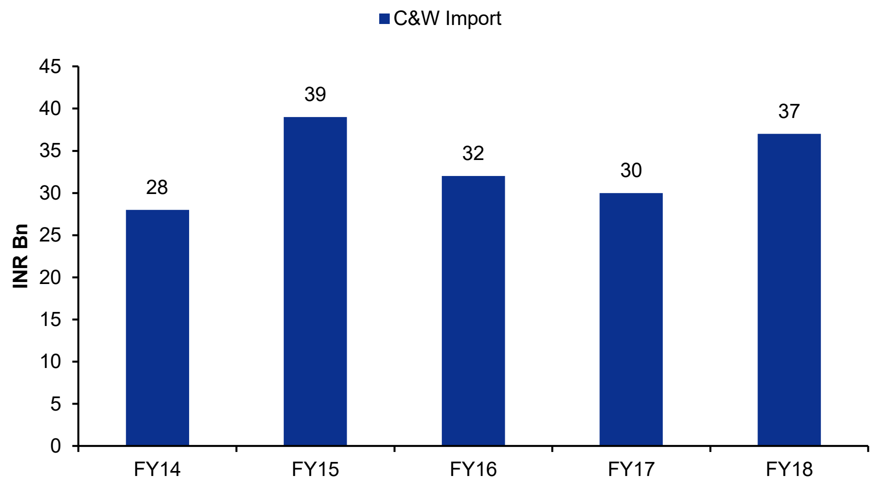
SOURCES: EIP RESEARCH, COMPANY REPORTS

Building specialty cable segment to enable import substitution ➤

"Special cable division has seen good progress, as we received approval for cables to be used in defence, railways and EVs."
- 3QFY21 analyst conference call

Government's Vocal for Local initiatives have opened new avenues of growth for Polycab into specialty cables (meant for precision customer segments like defence or aviation) which are currently being imported in India. The company recently received approvals for cable supply to defence, the Railways and electric vehicles (EV).

Figure 120: Import substitution could be Rs30bn-40bn annual opportunity going by imports data of FY14-18



SOURCES: EIP RESEARCH, COMPANY REPORTS

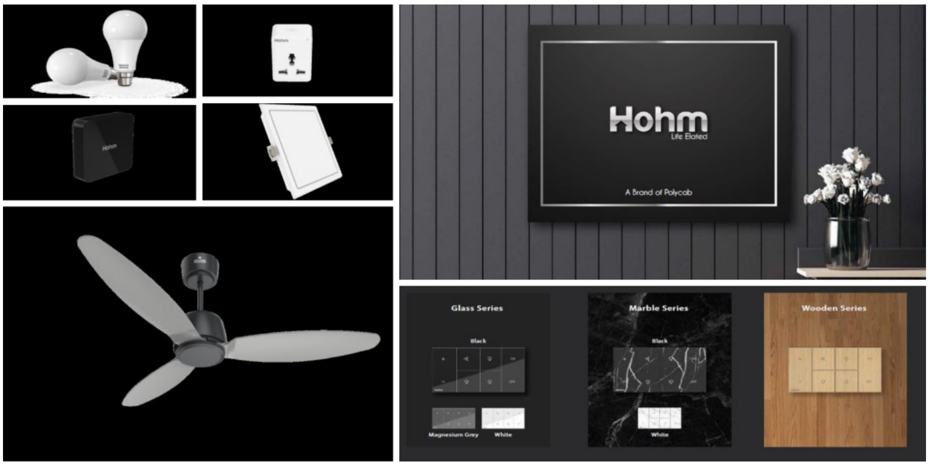
Increase in B2C product basket led by FMEG products; expect revenue CAGR of 14.2% over FY21-23F

Polycab entered the FMEG segment with switches in 2013 and expanded into fans and lights in 2014. The investment behind R&D to enhance consumer portfolio offerings will enable Polycab's FMEG business to grow faster at a CAGR of 22.5% vs the consolidated revenue CAGR of 14.2% over FY21-23F.

Figure 121: Polycab's B2C product basket

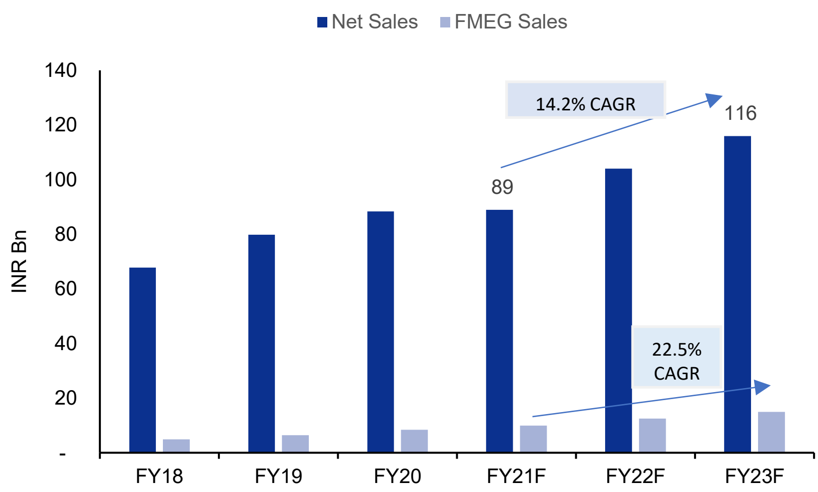
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 122: New brand of smart devices launched in 3QFY21 – Hohm



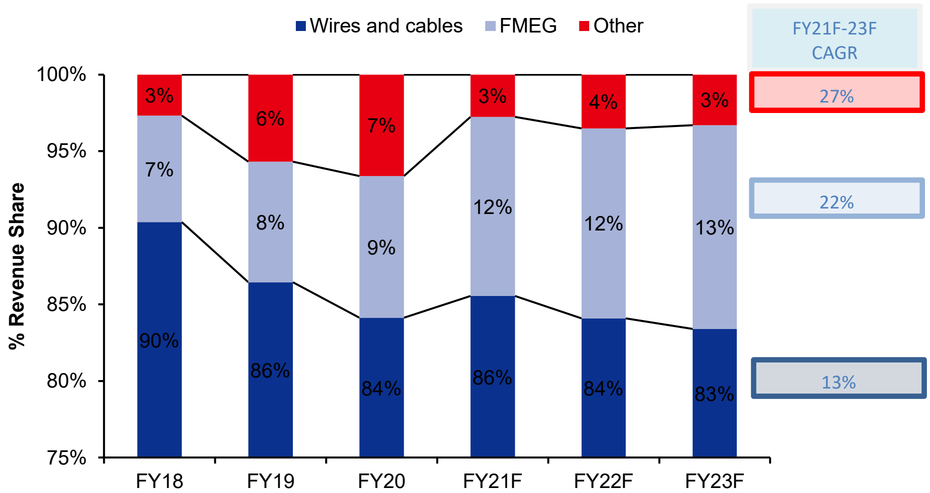
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 123: Faster growth of FMEG revenue to boost net sales over the next three years



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 124: Segment revenue share for Polycab



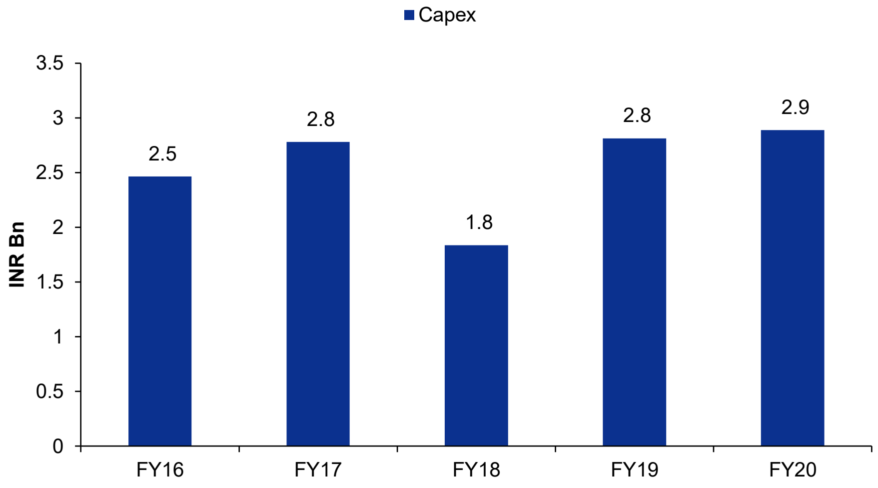
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Captive manufacturing and backward integration support margins

Polycab has invested reasonably well in product manufacturing and backward integration over the years

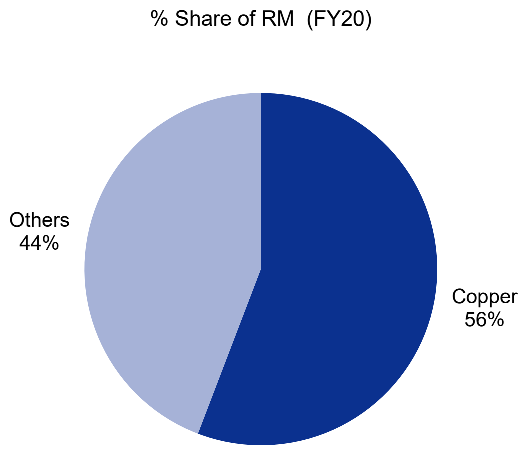
Polycab has been consistently investing in manufacturing capacity across C&W and FMEG product categories. Cumulative capex spent has been to the tune of ~Rs13bn over FY16-20. We expect asset turns of 3.5-4x over FY21-23F.

Figure 125: Polycab has invested reasonably well in manufacturing capability



SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 126: Company has backward integrated (Ryker plant) to secure stable supply for its major raw material - copper rods (more than 50% of RM)



SOURCES: EIP RESEARCH, COMPANY REPORTS

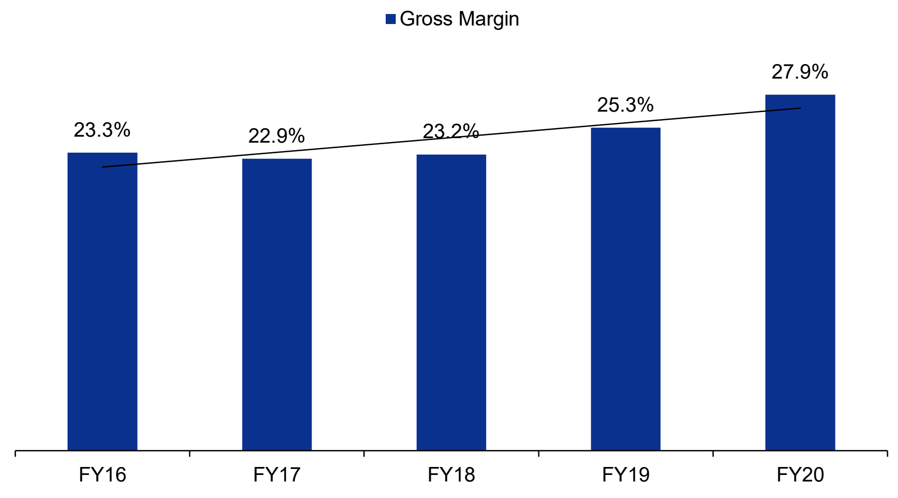
Figure 127: Polycab's manufacturing capacity

Product	Location	June 2019	Oct 2020
Wires & Cables	Halol / Daman, Gujarat	3.5m km	3.7m km
Lighting and Luminaires	Chhani, Gujarat	18.2m units	18.2m units
Switches and Switchgears	Nashik, Maharashtra	6m	7.2 m units
Fans	Roorkee, Uttarakhand	2.4m	3.1m units
Copper Rods	Waghodia, Gujarat	.22m tonnes	.22m tonnes

SOURCES: EIP RESEARCH, COMPANY REPORTS

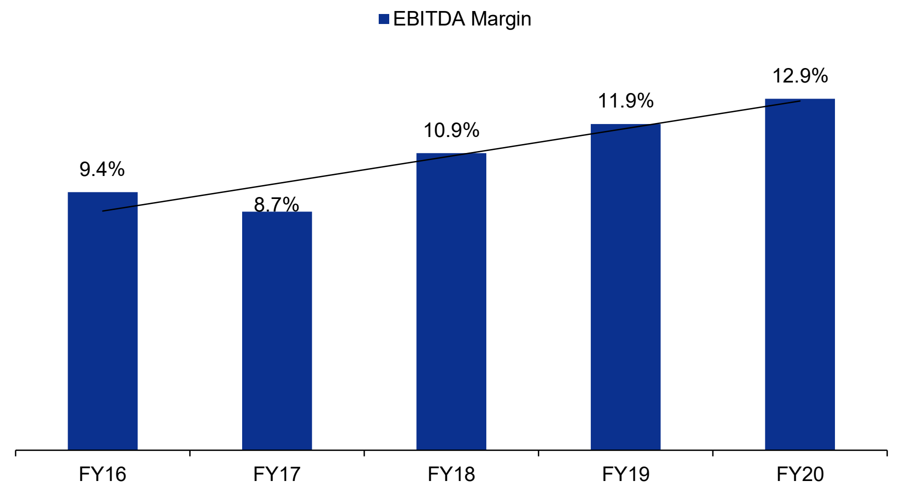
Polycab's investments led to increase in gross margins and operating margins over FY16-20

Figure 128: Backward integration and FMEG aided gross margin expansion



SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 129: EBITDA margins expanded by 350bp over the past five years

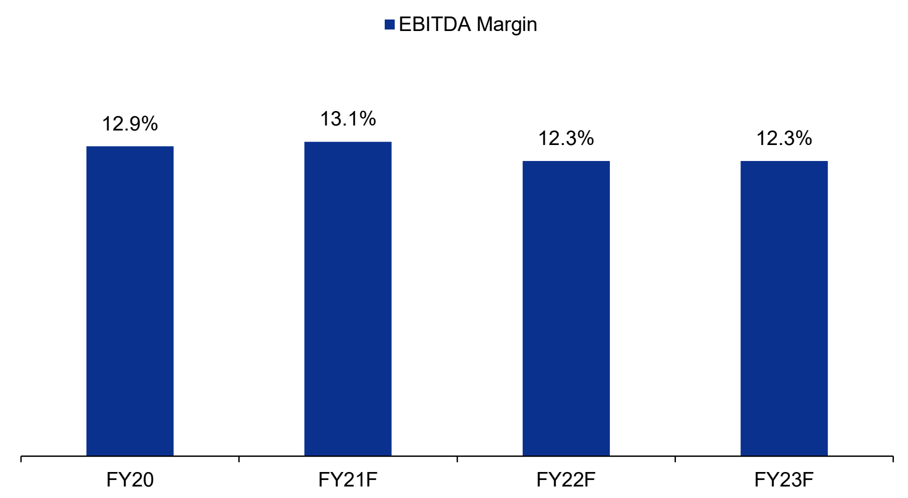


SOURCES: EIP RESEARCH, COMPANY REPORTS

Operating margins to be at 12-12.5% over FY22-23F

Polycab's FY20 EBITDA margins stood at 12.9% boosted by an exceptional large cable supply order from Dangote refinery in Africa. Even 9MFY21 saw substantial reduction in discretionary spends due to the COVID-19 pandemic lockdown that we expect to lead to higher EBITDA margins of 13.1% in FY21F. We think partial benefits of cost savings are likely to be sustained and Polycab's EBITDA margins to retrack to long term sustainable levels of 12-12.5% in FY22F/FY23F.

Figure 130: EBITDA margin to remain in 12-12.5% band over FY21-23F

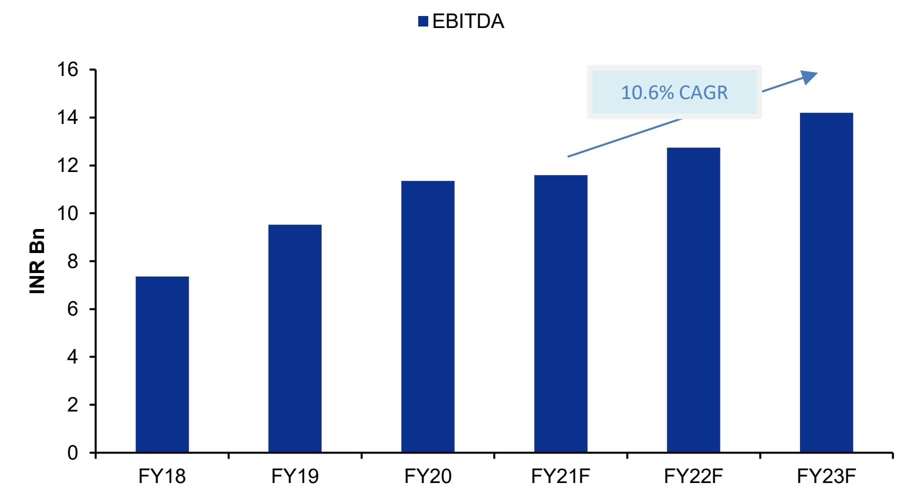


SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Estimate EBITDA CAGR of 10.6% over FY21-23F

On the back of strong revenue growth, favorable revenue mix and efficient operational cost controls, we expect EBITDA CAGR to be 10.6% over FY21-23F.

Figure 131: Expect EBITDA to rise on favorable revenue mix and cost controls



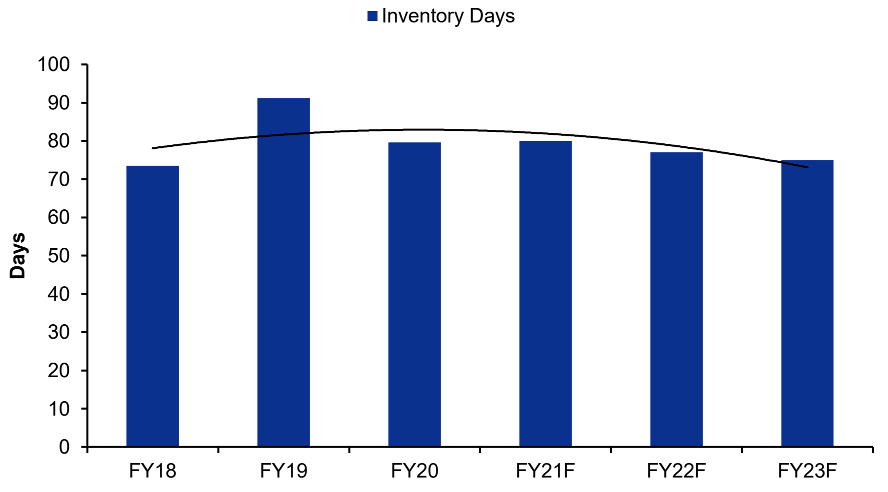
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Scope for improving working capital management and return ratios

Increase inventory turns based on internal initiatives and consultant feedback

Polycab management along with external consultants are working towards improving working capital management. The net working capital cycle (excluding cash and equivalents) was 94 days in FY16, which improved to 77 days of sales in FY20. There is further scope to improve this and we expect material release of working capital going forward. However, we are awaiting more clarity on the implementation initiatives and have modelled marginal reduction of nine days of sales over the next three years.

Figure 132: Inventory cycle can materially improve based on internal initiatives and consultant feedback

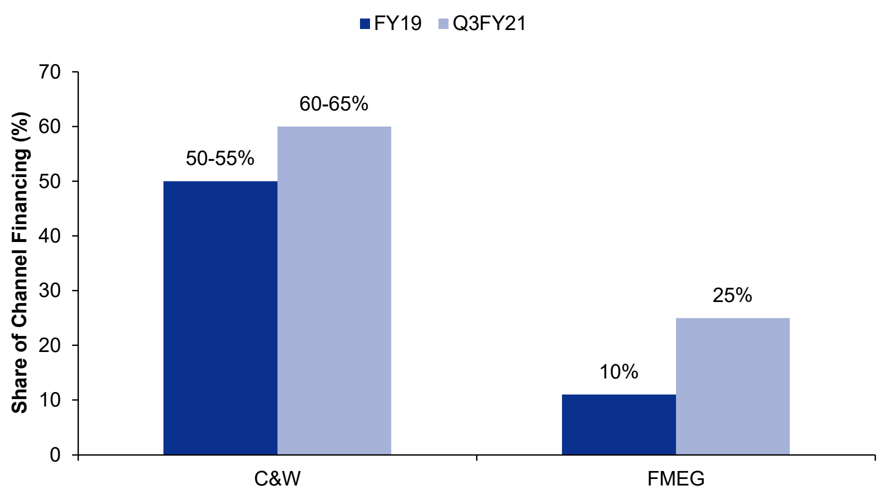


SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Reduce receivable days by increasing share of channel financing for C&W and FMEG segments

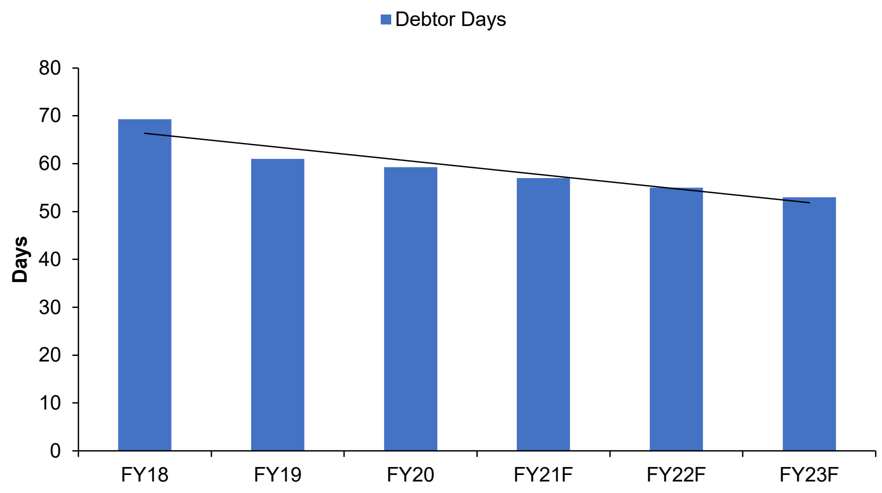
Receivable days reduced gradually to ~60 days of sales in FY20 as the share of channel financing for C&W and FMEG increased. As of Dec 2020, nearly 65% of C&W sales to distributors was funded through channel financing while it was ~25% (improving from ~11% in FY19) for FMEG sales (based on quarterly investor call transcripts).

Figure 133: Channel financing in C&W and FMEG increased



SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 134: Increased channel financing in C&W/FMEG helps reduce debtor days

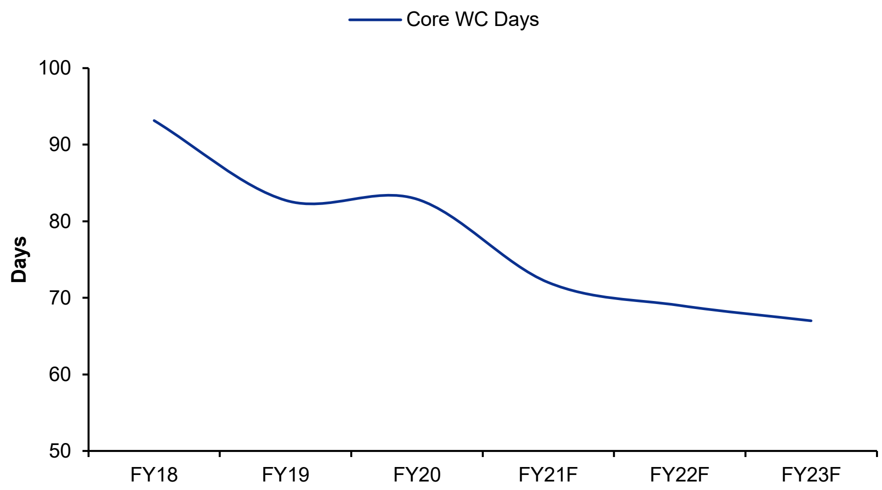


SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Reasonable case for WC cycle tapering over next 3 years

We model a modest improvement in the net WC cycle to 68 days of sales in FY23F and believe there is meaningful scope for further improvement in working capital management.

Figure 135: Expect steady decline in core working capital (WC) days

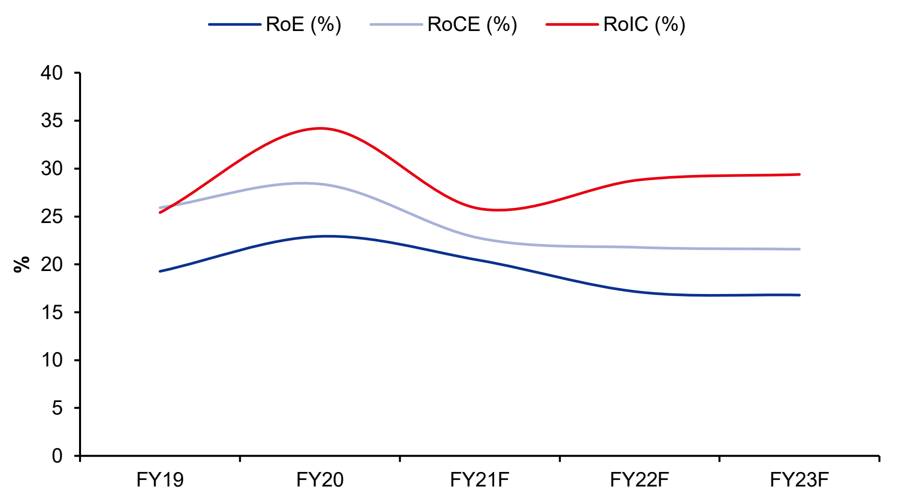


SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Estimate RoE of 17.1% and RoCE of 21.8% in FY22F; EPS CAGR of 5.3% (adjusted 10.8%) over FY21-23F

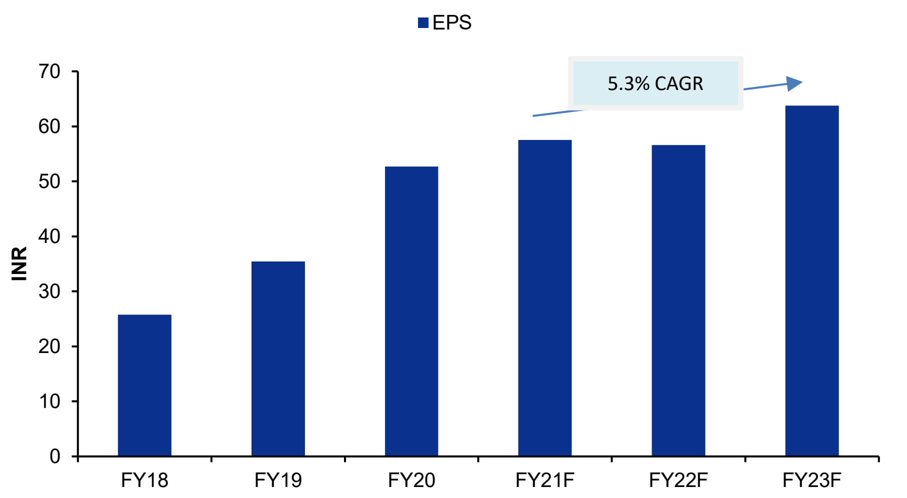
We estimate RoE of 17.1% and RoCE of 21.8% in FY22F. Our operating cash flow (OCF) to EBITDA estimates are at 60-70% over FY22F/FY23F. We estimate cumulative free cash flow (FCF) at Rs17.7bn over FY21-23F. We expect adjusted (income tax refund of Rs840m in FY21) EPS CAGR to be 10.8% over FY21-23F.

Figure 136: Return ratios



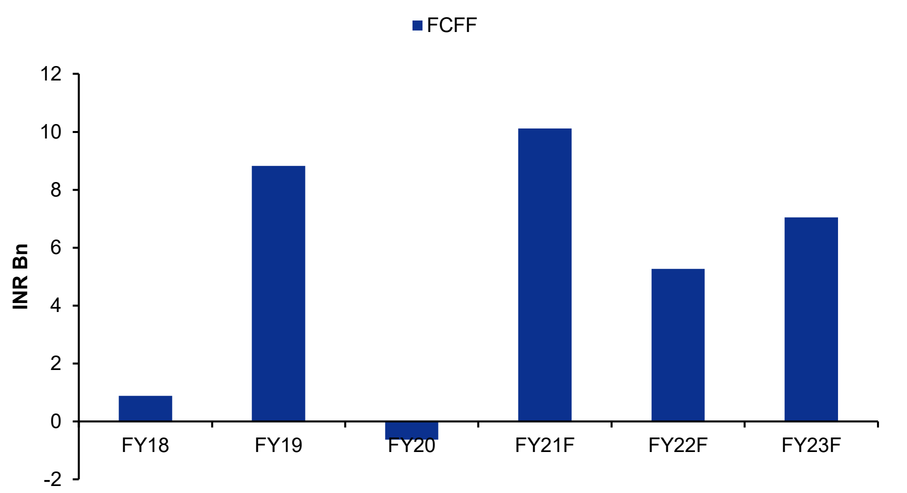
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 137: Earnings per share (EPS)



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 138: Free Cash Flow of Firm (FY19 had one-off benefit due to higher customer advances)



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Valuation

We note that the FMEG stocks in our coverage trade at substantial premium valuation multiples compared to C&W stocks owing to strong brand presence, miniscule project business, leaner balance sheets, high RoE and RoCE and positive investor perception of having non-cyclical demand for their products/services.

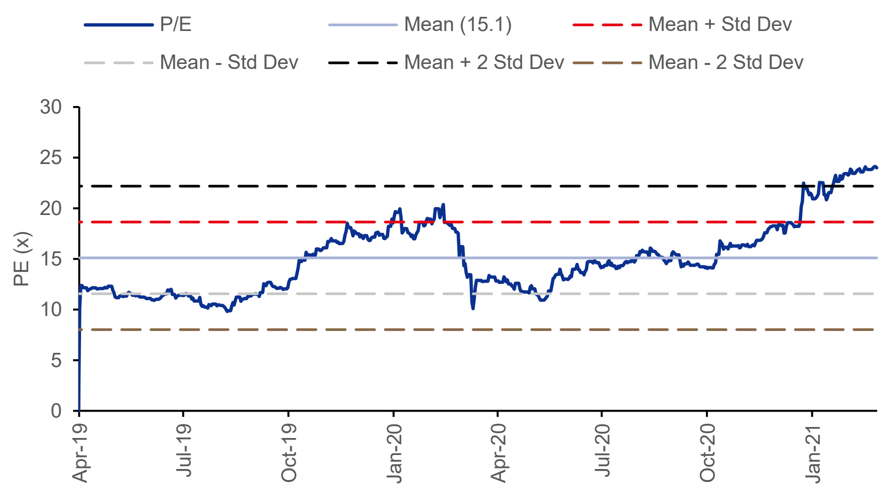
We think the following factors would determine valuation multiples for Polycab going forward:

- Continuing market leadership in the organised cable and wire segment and capitalising on the demand shift and market share gains from the unorganised sector;
- Emerging as a formidable FMEG brand in a highly competitive segment on the back of well penetrated distribution network pan India.
- Increasing share of B2C components in overall revenue led by relatively faster FMEG revenue growth;
- Scale benefits resulting in operating leverage flowing through sustainable and better operating profitability;
- Improving working capital cycle leading to higher return ratios and better capital allocation discipline;
- Consistency in free cash flow generation.

The stock has limited trading history (IPO in Apr 2019) and currently trades at +2SD its mean P/E of 15.1x (21.3x FY23F EPS) since listing. We think its superior FMEG performance is partially responsible for the re-rating post listing that is reflected in its current premium multiples to its C&W peers (KEI/Finolex Cables trade at 10.7/11.4x FY23F EPS). FMEG peers trade at substantial premiums (average P/E of 35-50x FY23F).

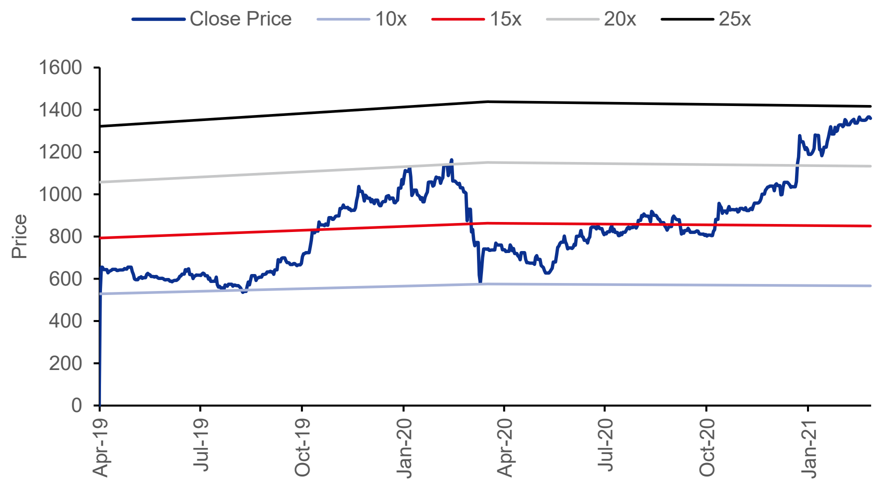
We believe Polycab's P/E would expand and move closer to FMEG peers gradually as it transforms into a large B2C franchise apart from maintaining its dominant market share in the C&W segment. Hence, we initiate coverage on Polycab with an Add rating and a target price of Rs1,530, valuing it at 24x FY23F EPS. We think the stock traded at lower P/E multiple since listing given the B2B nature of the cable and wire business. Over time, the company has delivered meaningful scalability in the FMEG business (~Rs10bn of annual sales expected in FY21F) and hence deserves a higher valuation multiple closer to its FMEG peers, in our view. We think the re-rating of the stock would continue over the medium term as the company achieves incremental scale and size in the electrical product space in India.

Figure 139: Polycab above +2SD its mean P/E since Listing (1 year forward)



SOURCES: EIP RESEARCH, COMPANY REPORTS, BLOOMBERG

Figure 140: P/E Band Chart



SOURCES: EIP RESEARCH, COMPANY REPORTS, BLOOMBERG

Downside risks

- **Volatile metal prices:** Copper, aluminium and steel account for ~80% of Polycab's total raw material (RM) costs. Typically, finished product price hikes cover most of the raw material price inflation. However, given sharp short-term movements and the time lag for price hikes to take full effect, gross margins could be affected negatively in the short term, in our view. Adverse forex movement and volatility in raw material pricing could impact our operating margin estimates.
- **Adverse forex rates:** Polycab imports 65%/25% of its copper/aluminium requirements. Similar to pass through of higher RM prices, adverse forex fluctuations are passed through as well. However, short-term volatility and adverse movements could result in untimely forex losses.
- **Slower pick up in FMEG business:** We have observed most of the C&W players have entered into the FMEG space and earn higher share of B2C revenues. FMEG is a highly competitive business segment with national and regional leaders with deep legacies competing for market share. Though Polycab has delivered strong FMEG revenue growth till date, tough competition from incumbents in new markets, etc, could lead to lower-than-expected revenues.
- **Volatile EPC business:** Polycab won large EPC orders in the past and the segment remains a tactical business opportunity for the company. However, one-off large orders could lead to sudden spikes in revenue/profits and volatility in EPS growth.

Business description and management profile

Polycab manufactures and sells wires and cables and fast-moving electrical goods (FMEG) under the Polycab brand. The company produces and sells a range of wires and cables. Key products in the wires and cables segment are power cables, control cables, instrumentation cables, solar cables, building wires, flexible cables, flexible/single multi core cables, communication cables and others, including welding cables, submersible flat and round cables, rubber cables, overhead conductors, railway signalling cables, specialty cables and green wires. FMEG products include electric fans, LED lighting and luminaires, switches and switchgear, solar products and conduits & accessories. Polycab's promoters collectively have more than four decades of experience. In 2009, Polycab diversified into the EPC business, which includes the design, engineering, supply, execution and commissioning of power distribution and rural electrification projects. In 2014, the company diversified into the FMEG segment.

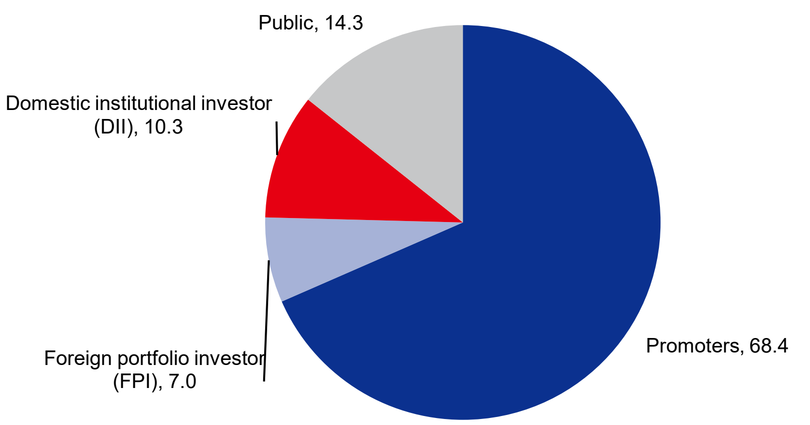
The company's board of directors consists of four independent and non-independent directors each.

Figure 141: Key management personnel (FY20)

Name and Designation	Profile
Inder T. Jaisinghani Managing Director	Mr Jaisinghani is the company's Chairman and Managing Director. He has been with the company since its inception. He has worked in Strategy and Planning, Administration and Management, Sales and Marketing, Governance, Operations and other support services and has played a major role in the leadership of the company.
Ramesh T. Jaisinghani Whole-time Director	Mr Ramesh T. Jaisinghani is a Whole-Time Director of the company. He has worked as a director with the company since its inception. He has worked in Administration and Management, Governance, Operations and other support services and played a major role in the company's leadership.
Ajay T. Jaisinghani Whole-Time Director	Mr Ajay T. Jaisinghani is a Whole-Time Director of the company. He has worked in Administration and Management, Sales and Marketing, Governance, Operations and other support services and has played a major role in the company's leadership.
Shyam Lal Bajaj CFO & Whole-Time Director	Mr Shyam Lal Bajaj is a Whole-Time Director of the company. He holds a bachelor's degree in Commerce from Rajasthan University and is a chartered accountant. Prior to joining the company, he served as the Director Finance at Vedanta Limited (including at Sesa Sterlite Limited now merged with Vedanta Limited). He has served as the Chief Financial Officer of Hindustan Zinc Limited, as Chief Financial Officer and Vice President of Finance at Sterlite Technologies Limited (formerly Sterlite Optical Technologies Limited) and Senior General Manager at Sterlite Industries (India) Limited now Vedanta Limited.

SOURCES: EIP RESEARCH, COMPANY REPORTS AND COMPANY WEBSITE

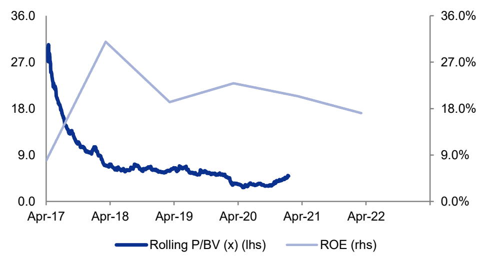
Figure 142: Share Holding Pattern (Dec 2020)



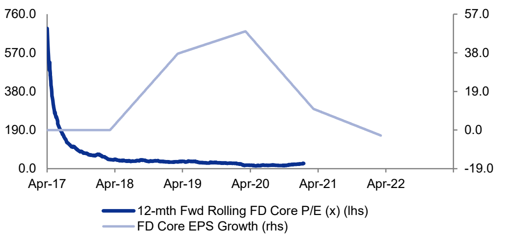
SOURCES: EIP RESEARCH, BSE WEBSITE

BY THE NUMBERS

P/BV vs ROE



12-mth Fwd FD Core P/E vs FD Core EPS Growth



Profit & Loss

(Rs mn)	Mar-19A	Mar-20A	Mar-21F	Mar-22F	Mar-23F
Total Net Revenues	**79,856**	**88,299**	**88,875**	**1,04,070**	**1,15,913**
Gross Profit	**20,197**	**24,613**	**23,330**	**26,538**	**29,558**
Operating EBITDA	**9,530**	**11,350**	**11,598**	**12,749**	**14,199**
Depreciation And Amortisation	(1,414)	(1,609)	(1,909)	(2,238)	(2,543)
Operating EBIT	**8,116**	**9,741**	**9,689**	**10,510**	**11,656**
Financial Income/(Expense)	(1,040)	(46)	(64)	247	526
Pretax Income/(Loss) from Assoc.	(23)	(74)		(30)	(30)
Non-Operating Income/(Expense)	510	479	800	600	600
Profit Before Tax (pre-EI)	**7,563**	**10,100**	**10,426**	**11,327**	**12,752**
Exceptional Items			97		
Pre-tax Profit	**7,563**	**10,100**	**10,523**	**11,327**	**12,752**
Taxation	(2,557)	(2,444)	(1,808)	(2,858)	(3,217)
Exceptional Income - post-tax					
Profit After Tax	**5,006**	**7,656**	**8,715**	**8,469**	**9,535**
Minority Interests			(30)	(30)	(30)
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	**5,006**	**7,656**	**8,685**	**8,439**	**9,505**
Recurring Net Profit	5,006	7,656	8,604	8,439	9,505
Fully Diluted Recurring Net Profit	**5,006**	**7,656**	**8,604**	**8,439**	**9,505**

Cash Flow

(Rs mn)	Mar-19A	Mar-20A	Mar-21F	Mar-22F	Mar-23F
EBITDA	9,530	11,350	11,598	12,749	14,199
Cash Flow from Invt. & Assoc.					
Change In Working Capital	3,054	(6,221)	2,498	(1,934)	(1,441)
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense					
Other Operating Cashflow	489	104	834	817	1,096
Net Interest (Paid)/Received	1,039	225	64	(247)	(526)
Tax Paid	(1,814)	(3,012)	(1,808)	(2,858)	(3,217)
Cashflow From Operations	**12,299**	**2,446**	**13,185**	**8,526**	**10,111**
Capex	(2,814)	(2,890)	(3,000)	(3,500)	(3,588)
Disposals Of FAs/subsidiaries					
Acq. Of Subsidiaries/investments					
Other Investing Cashflow	(1,263)	268	(9,448)	(272)	(83)
Cash Flow From Investing	**(4,076)**	**(2,622)**	**(12,448)**	**(3,772)**	**(3,670)**
Debt Raised/(repaid)	(5,613)	(1,328)	750	(750)	(570)
Proceeds From Issue Of Shares	(91)	3,661	2		
Shares Repurchased					
Dividends Paid	(29)	(1,793)	(1,118)	(1,640)	(1,789)
Preferred Dividends					
Other Financing Cashflow	(781)	(433)	(472)	(481)	(391)
Cash Flow From Financing	**(6,514)**	**107**	**(838)**	**(2,871)**	**(2,750)**
Total Cash Generated	1,709	(69)	(101)	1,883	3,690
Free Cashflow To Equity	**2,610**	**(1,504)**	**1,487**	**4,004**	**5,870**
Free Cashflow To Firm	**7,056**	**(671)**	**265**	**4,273**	**6,049**

SOURCES: EIP RESEARCH, COMPANY REPORTS

BY THE NUMBERS…cont'd

Balance Sheet

(Rs mn)	Mar-19A	Mar-20A	Mar-21F	Mar-22F	Mar-23F
Total Cash And Equivalents	3,167	3,213	13,112	15,995	20,685
Total Debtors	13,343	14,336	13,879	15,682	16,831
Inventories	19,958	19,249	19,479	21,954	23,818
Total Other Current Assets	2,774	3,700	3,852	4,477	4,964
Total Current Assets	**39,242**	**40,498**	**50,323**	**58,108**	**66,298**
Fixed Assets	12,721	13,865	16,118	17,380	18,425
Total Investments	294	255	111	111	111
Intangible Assets	35	17	17	17	17
Total Other Non-Current Assets	3,991	4,969	3,807	3,807	3,807
Total Non-current Assets	**17,041**	**19,106**	**20,053**	**21,315**	**22,360**
Short-term Debt	1,031	1,114	2,320	1,570	1,000
Current Portion of Long-Term Debt					
Total Creditors	15,201	13,536	15,827	17,963	19,372
Other Current Liabilities	9,153	5,060	4,870	5,702	6,351
Total Current Liabilities	**25,386**	**19,710**	**23,017**	**25,235**	**26,723**
Total Long-term Debt	1,693	456			
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	419	759	1,082	1,082	1,082
Total Non-current Liabilities	**2,112**	**1,215**	**1,082**	**1,082**	**1,082**
Total Provisions	231	165	165	165	165
Total Liabilities	**27,729**	**21,090**	**24,263**	**26,482**	**27,970**
Shareholders Equity	28,470	38,364	45,933	52,732	60,448
Minority Interests	84	150	180	210	240
Total Equity	**28,554**	**38,514**	**46,113**	**52,942**	**60,688**

Key Ratios

	Mar-19A	Mar-20A	Mar-21F	Mar-22F	Mar-23F
Revenue Growth	17.8%	10.6%	0.7%	17.1%	11.4%
Operating EBITDA Growth	29.4%	19.1%	2.2%	9.9%	11.4%
Operating EBITDA Margin	11.9%	12.9%	13.1%	12.3%	12.3%
Net Cash Per Share (Rs)	3.14	11.31	72.30	96.77	132.05
BVPS (Rs)	201.61	263.98	307.74	353.73	405.49
Gross Interest Cover	6.95	19.68	20.54	21.86	29.80
Effective Tax Rate	33.8%	24.2%	17.2%	25.2%	25.2%
Net Dividend Payout Ratio		23.4%	13.0%	19.4%	18.8%
Accounts Receivables Days	59.89	57.21	57.94	51.84	51.19
Inventory Days	102.83	112.35	107.83	97.53	96.73
Accounts Payables Days	74.71	82.35	81.76	79.54	78.90
ROIC (%)	25.4%	34.2%	25.8%	28.8%	29.4%
ROCE (%)	25.9%	28.4%	22.7%	21.8%	21.6%
Return On Average Assets	12.0%	13.3%	13.4%	11.0%	10.7%

SOURCES: EIP RESEARCH, COMPANY REPORTS

CGSCIMB

Company Note

INITIATION

InCred

Industrial - Overall | India | March 15, 2021

India

ADD *(Initiating coverage)*

Consensus ratings*: Buy 10 Hold 5 Sell 5

Current price:	Rs230
Target price:	Rs277
Previous target:	N/A
Up/downside:	20.4%
EIP Research / Consensus:	9.5%
Reuters:	VGUA.NS
Bloomberg:	VGRD IN
Market cap:	US$1,356m
	Rs98,675m
Average daily turnover:	US$2.7m
	Rs193.5m
Current shares o/s:	429.5m
Free float:	37.5%

Source: Bloomberg

Source: Bloomberg

Price performance	*1M*	*3M*	*12M*
Absolute (%)	2.1	23.0	27.4
Relative (%)	3.6	11.6	(10.5)

Major shareholders	% held
Promoters	62.6
Nalanda India Equity Fund Limited	4.3
Sbi Small Cap Fund	3.4

V-Guard Industries Ltd

Widening brand presence across India

- We expect FY21-23F revenue growth to be driven by new products, entry into new markets and new sale channels.
- Higher margins and operating leverage benefits likely will be reinvested in brand building over FY21-23F, in our view
- We expect steady EPS growth recovery over this period. Initiate coverage with Add rating and target price of Rs277.

New products, new markets and new channels

Recovery in urban housing/real estate demand, coupled with company initiatives, would provide V-Guard the much-needed impetus for revenue growth recovery (3.7% CAGR over FY18-20), in our view. Category extension into domestic appliances, widening/deepening of non-South India retail network and dedicated product lines for e-commerce augur well for growth recovery. We expect emerging/growth product categories (digital inverters, fans, electric water heaters, etc.) to deliver higher revenue growth than the matured products like stabilizers/flexible wires. We estimate overall/consumer durable revenue CAGR of 13.5%/16.2% over FY21-23F.

Operating leverage benefits to be used for brand building

Gross margins improved by ~500bp to 33.5% over FY17-20 and we expect them to improve further driven by better product mix, premiumization and incremental in-house manufacturing. Management intends to reinvest these gains and operating leverage benefits for brand building into new markets. Advertising and marketing spends will gradually increase (FY20: 2.5% of sales) with network expansion investments in the non-South India region over FY21-23F. According to management, V-Guard is also exploring inorganic growth options for faster revenue scale up or entry in new markets. We estimate EBITDA margins of 10.5-11% and EBITDA CAGR of 13% over FY21-23F.

Capex intensity to pick up, free cash generation to stay healthy

Nearly 50% of the products are manufactured in-house and would reach 60% over the next three to five years. We expect consolidated capex to pick up to Rs650m-800m/year, of which maintenance capex is likely to be Rs200m-300m/year – fully funded by internal accruals. V-Guard tightened the receivables cycle to 45-50 days of sales in 9MFY21. We expect RoE/RoCE of 18-26% and cumulative FCF of Rs5bn over FY21-23F.

Initiate with Add rating, non-South India competition is a key risk

Given the start of the recovery in urban housing, historical high real estate affordability, recovery in revenue growth rates, EPS CAGR of 15% over FY21-23F, high return ratios and net cash balance sheet, we expect the stock to continue to command premium valuations. The stock trades at FY23F P/E of 35.7x and EV/EBITDA of 23.4x. We value the stock at Rs277 based on its five-year mean P/E of 43x and initiate coverage with an Add rating. Downside risks: High incumbent competition in North/West India, delay in new product launches and supply chain disruption risks.

Financial Summary	Mar-19A	Mar-20A	Mar-21F	Mar-22F	Mar-23F
Revenue (Rsm)	25,940	25,029	26,986	31,397	34,754
Operating EBITDA (Rsm)	2,243	2,580	2,915	3,485	3,945
Net Profit (Rsm)	1,680	1,894	1,984	2,412	2,763
Core EPS (Rs)	3.9	4.4	4.6	5.6	6.4
Core EPS Growth	24.1%	13.1%	5.1%	22.0%	14.6%
FD Core P/E (x)	59.21	52.50	49.97	40.97	35.71
DPS (Rs)	0.7	1.7	1.0	1.3	1.5
Dividend Yield	0.36%	0.88%	0.43%	0.56%	0.65%
EV/EBITDA (x)	43.33	37.74	32.71	26.92	23.40
P/FCFE (x)	86.60	352.18	49.33	60.56	57.78
Net Gearing	(16.7%)	(13.5%)	(29.2%)	(36.5%)	(41.2%)
P/BV (x)	11.07	9.97	8.60	7.38	6.37
ROE	20.4%	20.0%	18.5%	19.4%	19.2%
% Change In Core EPS Estimates					
EIP Research/Consensus EPS (x)			1.01	0.97	0.98

SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS. PRICED AS AT 12 MAR 2021

Analyst(s)

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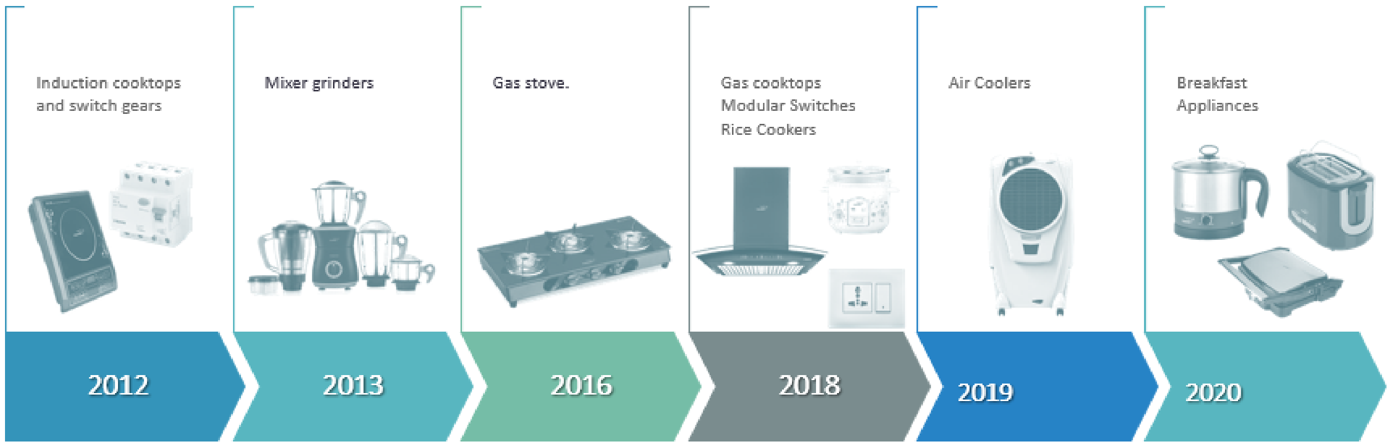
Widening brand presence across India

New products, new markets and new channels – all come together to drive revenue growth

Exciting category extension into small domestic appliances ›

Figure 143: V-Guard's recent product launches indicate focus on small domestic appliances

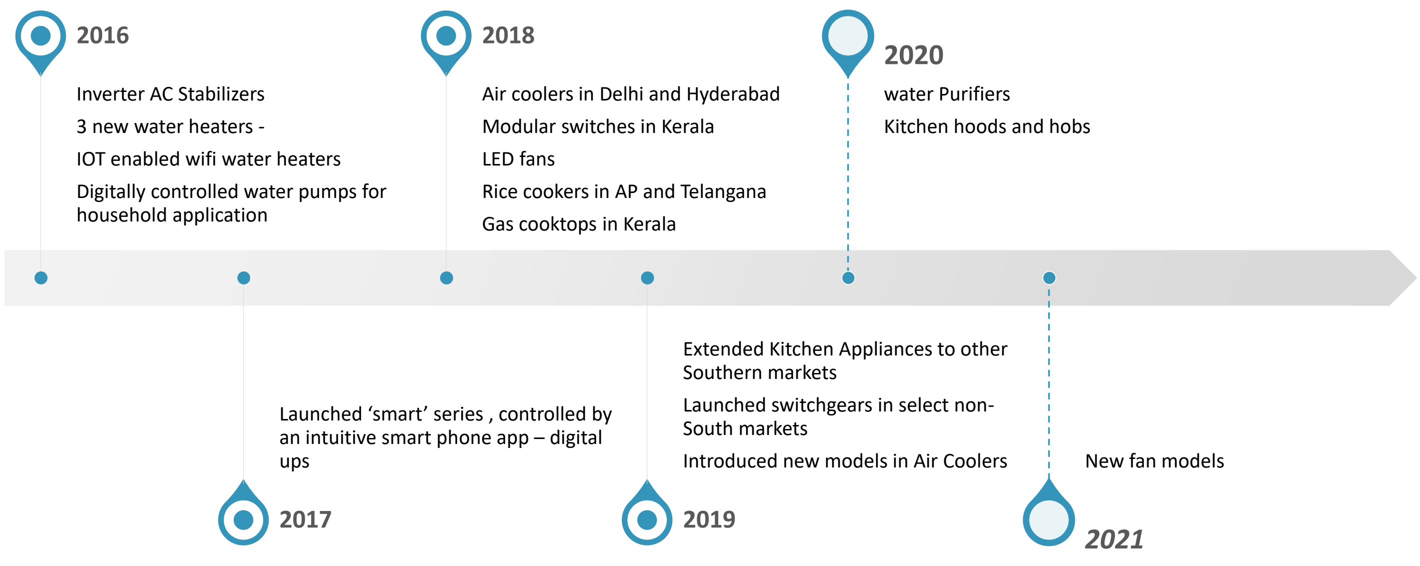


SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 144: V-Guard product portfolio

SOURCES: EIP RESEARCH, COMPANY REPORTS

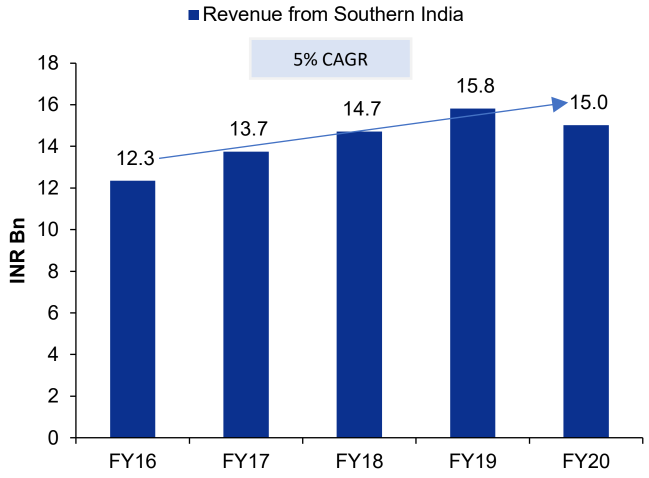
Figure 145: V-Guard's product innovation driving premiumisation



SOURCES: EIP RESEARCH, COMPANY REPORTS

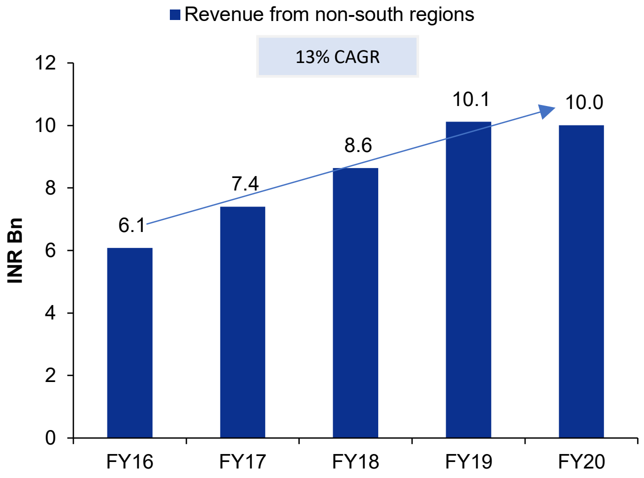
Successful regional diversification outside South India, lower revenue concentration risks

Figure 146: V-Guard – slow growth of South India revenue



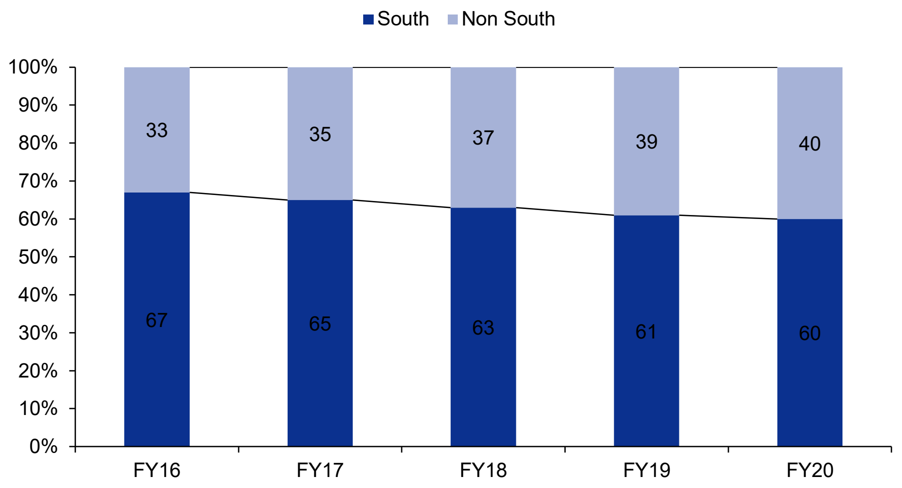
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 147: Non-South India regions led growth with 13% CAGR



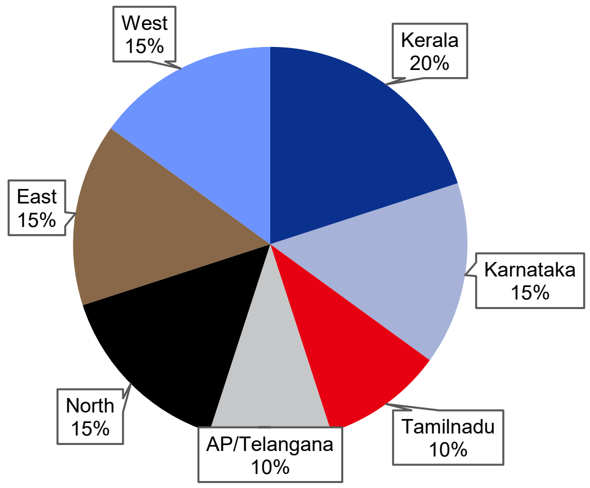
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 148: Rising share of non-South India revenue



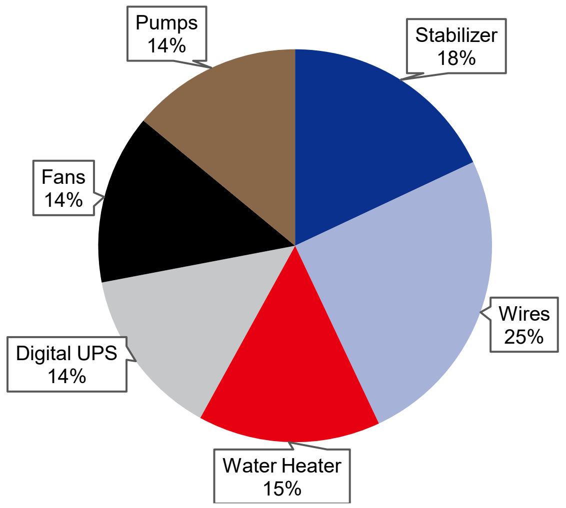
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 149: V-Guard's estimated region-wise revenue share (FY20)



SOURCES: EIP RESEARCH ESTIMATES

Figure 150: V-Guard's estimated product-wise revenue breakup (FY20)

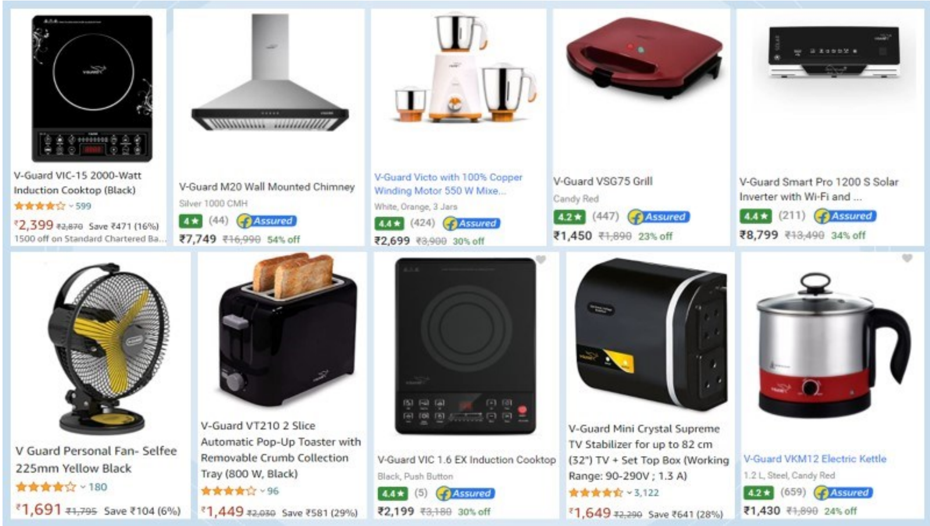


SOURCES: EIP RESEARCH ESTIMATES

Dedicated product line for e-commerce development

The company started the e-commerce initiative in 2017, launching dedicated product lines (water purifiers and breakfast appliances) to be exclusively sold online. V-Guard believes in developing this channel through market places like Amazon and Flipkart only and currently has not invested into its own e-commerce portal. The e-commerce channel enjoys superior margins compared to any other channel, according to management. As of Dec 2020, e-commerce had an 8% revenue share in overall revenues (excluding B2B product sales – wires, pumps, stabilisers, batteries, etc).

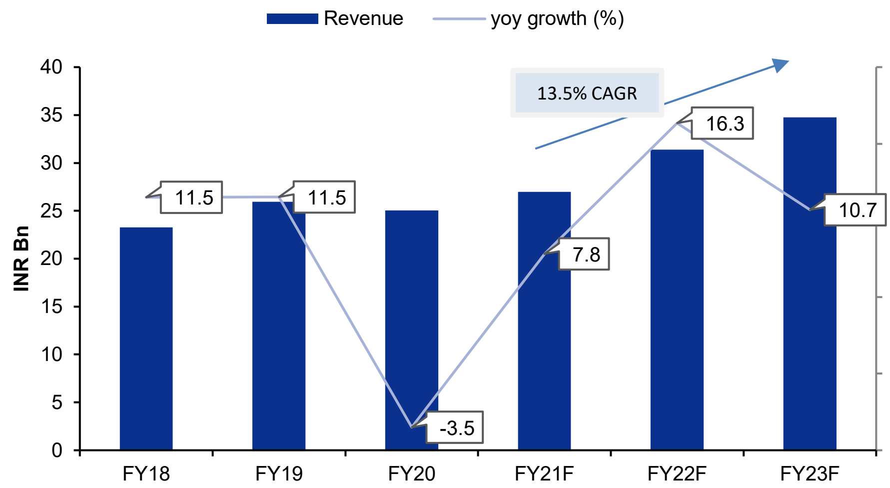
Figure 151: Presence across Amazon and Flipkart supported by a wide portfolio



SOURCES: EIP RESEARCH, AMAZON AND FLIPKART WEBSITES

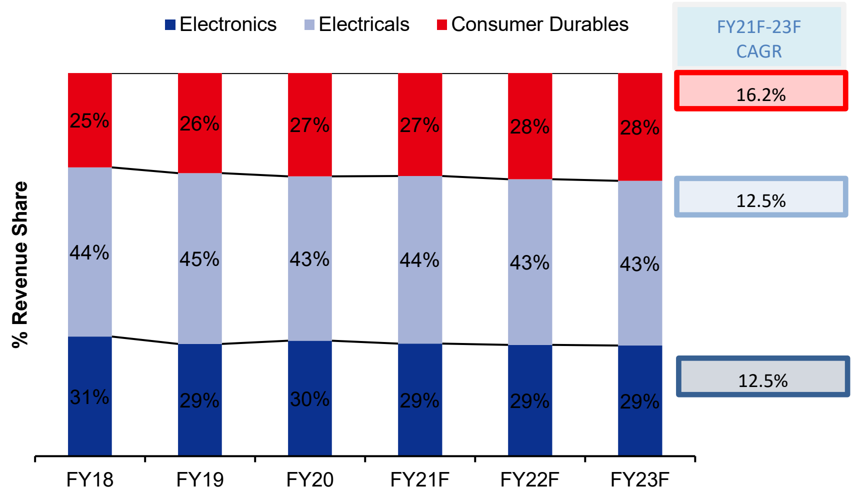
We expect revenue CAGR of 13.5% over FY21-23F

Figure 152: We expect revenue growth to pick up meaningfully



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 153: V-Guard's segmental revenue share trend and growth



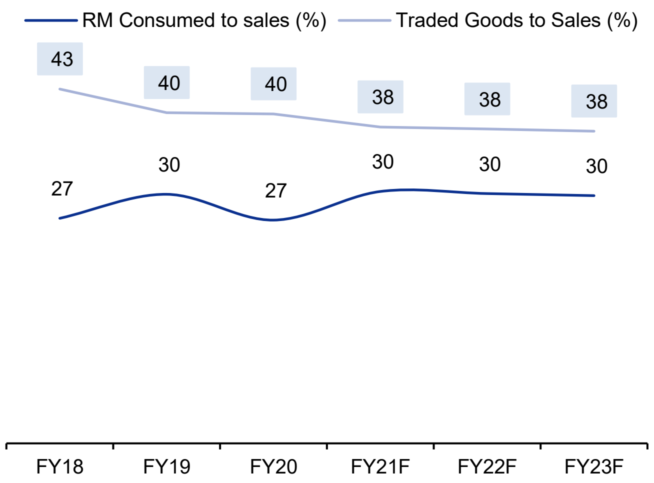
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Operating leverage benefits to be reinvested in brand building for new geographies

Expanding into higher gross margin categories

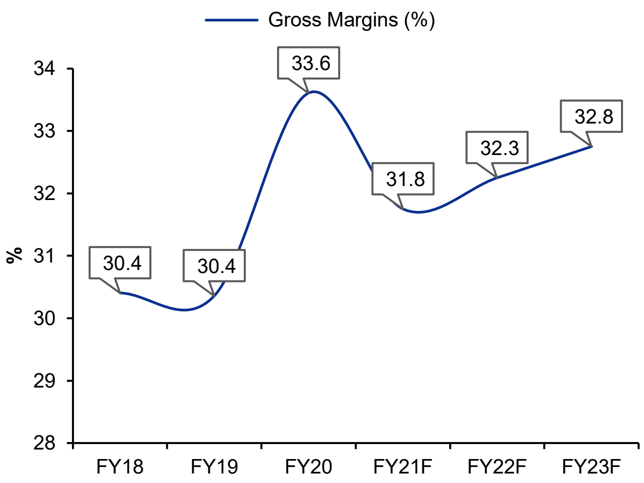
V-Guard management believes consistent gross margin improvements over the past three to five years will continue going forward owing to better product mix, category premiumisation and higher share of in-house manufacturing. The company improved gross margins by ~500bp over FY17-20. Gross margin for in-house manufactured products is 200-300bp higher than outsourced products currently. We build in marginal increase of 100bp of gross margins over FY21-23F.

Figure 154: V-Guard's raw materials & traded goods to sale (%) trend



RM IS RAW MATERIALS
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 155: V-Guard's gross margin trend



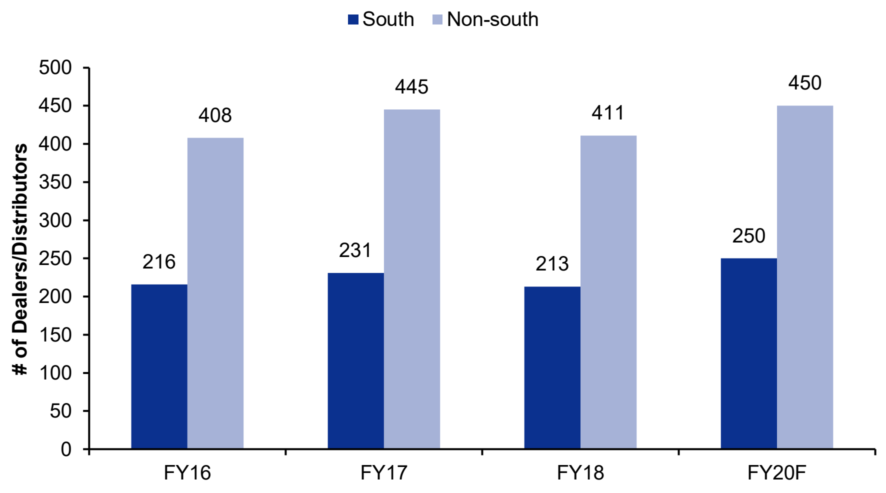
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Aggressive network expansion in non-South India markets

The company envisages adding 3,000-5,000 retailers across the country every year over the next five years, with higher addition in the non-South India regions.
– 3QFY21 investor call transcript

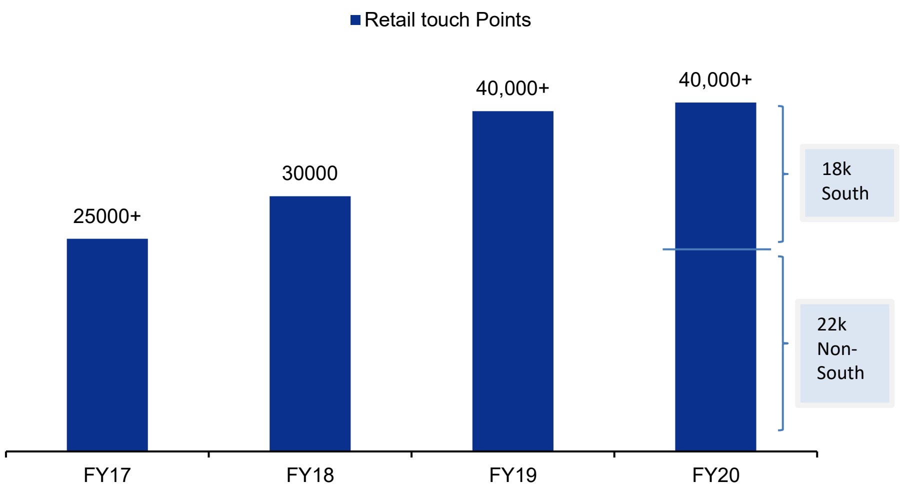
V-Guard expects the non-South India markets to contribute to 55-60% of overall revenues over the next five years. Of the total retail touchpoints of over 40k pan India, nearly 22k are in the non-South region. Management believes the non-South India market size is twice that of South India and the potential to add dealers/distributors and retail touchpoints is very large.

Figure 156: V-Guard's dealer / distributor network



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 157: V-Guard's widening retailer network (point of sale)



SOURCES: EIP RESEARCH, COMPANY REPORTS

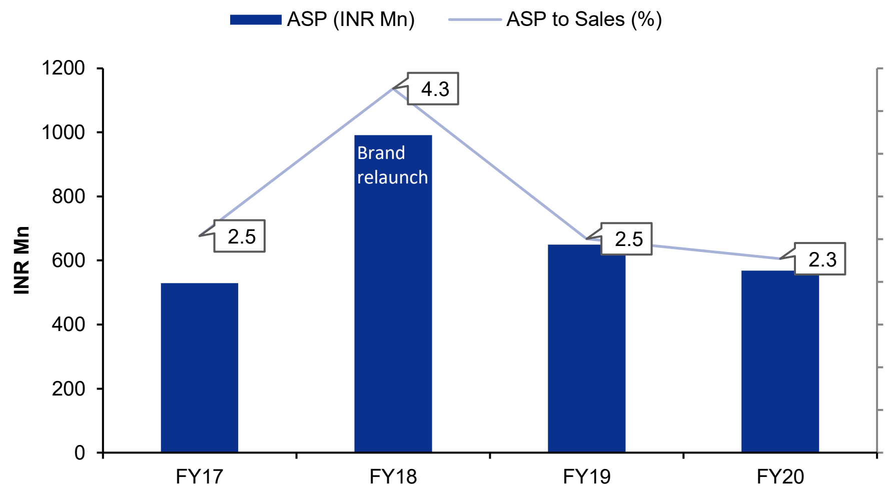
A&P activity to be maintained at least at historical levels; exploring inorganic growth options

V-Guard plans to reinvest most of the higher margin and operating leverage benefits into brand building through higher advertising and promotion (A&P) spends. Historically, the company has spent 2-2.5% of revenue on advertising and business promotion expenses every year and intends to gradually increase this in sync with the improvement in operating profitability.

V-Guard has been exploring inorganic growth options to plug product/geography gaps and scale up faster than industry growth. The company earlier showcased interest in kitchen appliances and adjacent categories and continues to look out for opportunities. M&A options within the unorganised sector post the COVID-19 pandemic disruption are of no interest to the company. According to management, it is focused on acquiring a sizable consumer brand with meaningful synergies and appropriate fitment to the existing product/regional presence, even if it entails marginal borrowings for funding the acquisition.

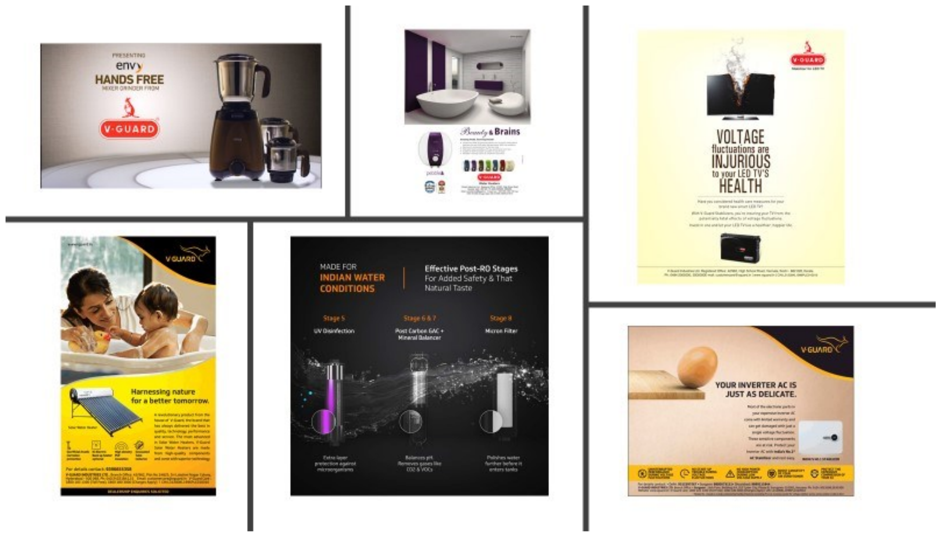
Recently, V-Guard funded a Series A round of investment for Gegadyne Energy, a Mumbai-based quick charging battery technology company, for an 18.8% equity stake worth US$5m in Jan 2021. The investment entails Gegadyne to commercialise its patented inventions and we expect commercial benefits to flow in over the next two to three years.

Figure 158: V-Guard's ASP to sales (%)



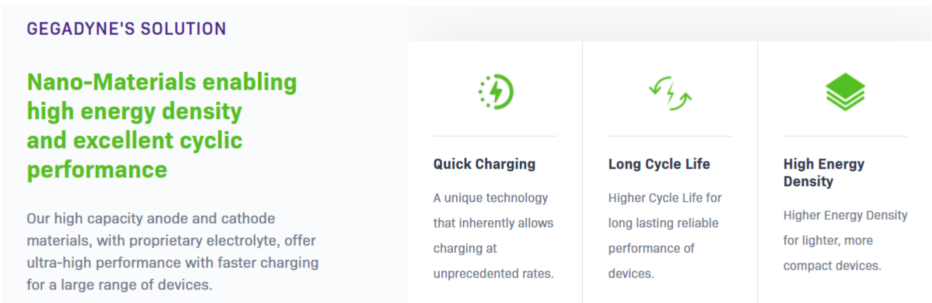
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 159: Various V-Guard advertisements



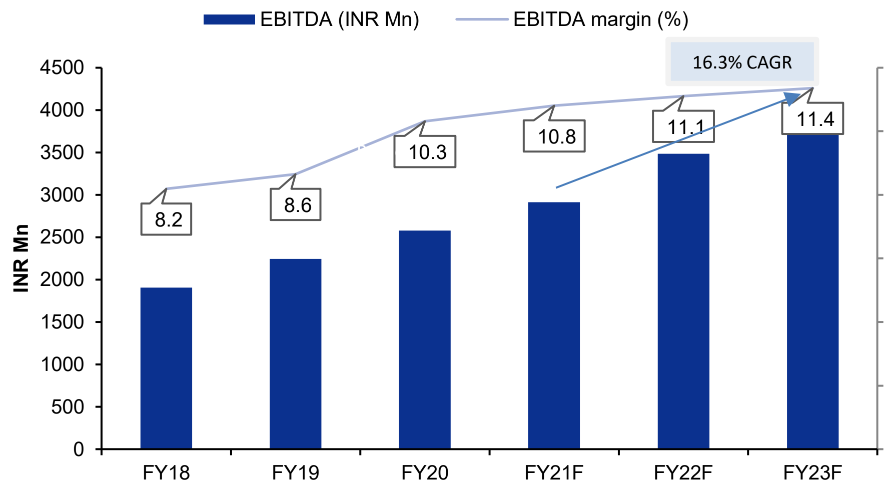
SOURCES: EIP RESEARCH, VGUARD.IN, ADVERTGALLERY.COM

Figure 160: V-Guard exploring inorganic growth options (bought stake in battery company Gegadyne in Jan 2021)



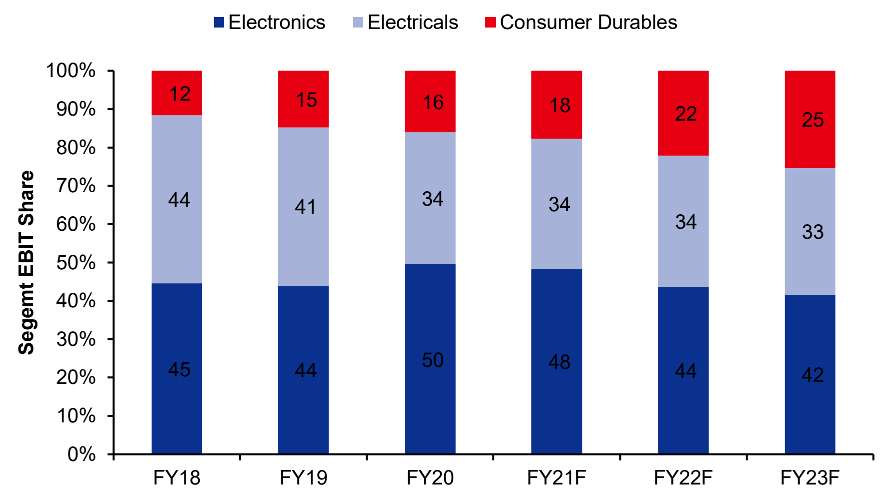
SOURCES: EIP RESEARCH, WWW.GEGADYNE.COM

Figure 161: We expect V-Guard's EBITDA CAGR of 16.3% over FY21-23F



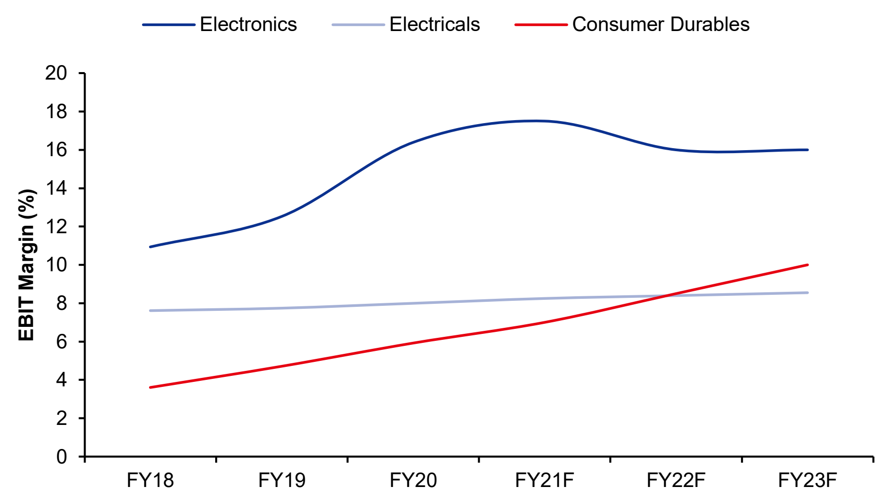
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 162: V-Guard's approximate segment EBIT mix



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 163: V-Guard's approximate segment EBIT margin



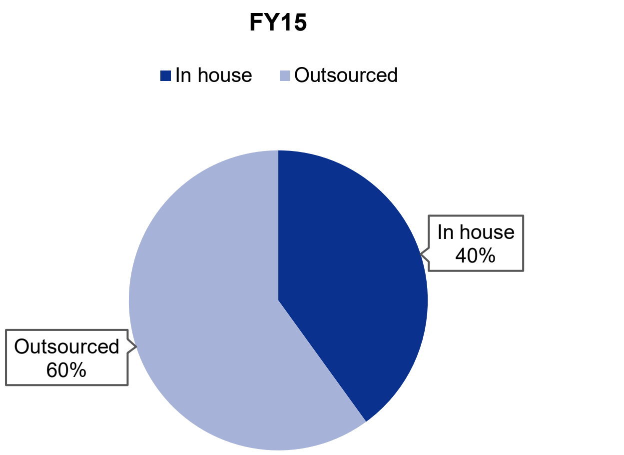
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Capex intensity to pick up, cash flow generation to stay healthy

Strict threshold for incurring capex for in-house manufacturing

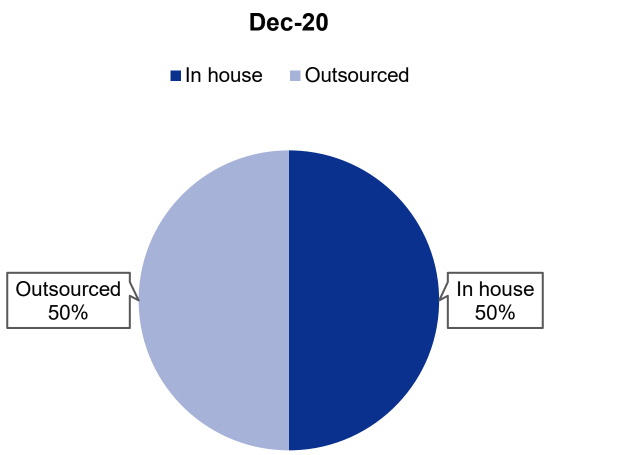
Typically, V-Guard prefers to manufacture a premium range of products in-house while outsourcing the manufacture of economy/standard range products. Currently, 50% of the products are manufactured in-house while management intends to increase this to 60% over the next three to five years. We estimate marginal increase in capex to Rs650m-800m/year including maintenance capex of Rs250m-300m/year over FY21-23F. V-Guard maintains a strict threshold for product categories and typically in-sources production once the category reaches meaningful scale of ~Rs1bn-1.5bn of revenues per year, according to management.

Figure 164: V-Guard's in-house manufacturing was at 40% in FY15



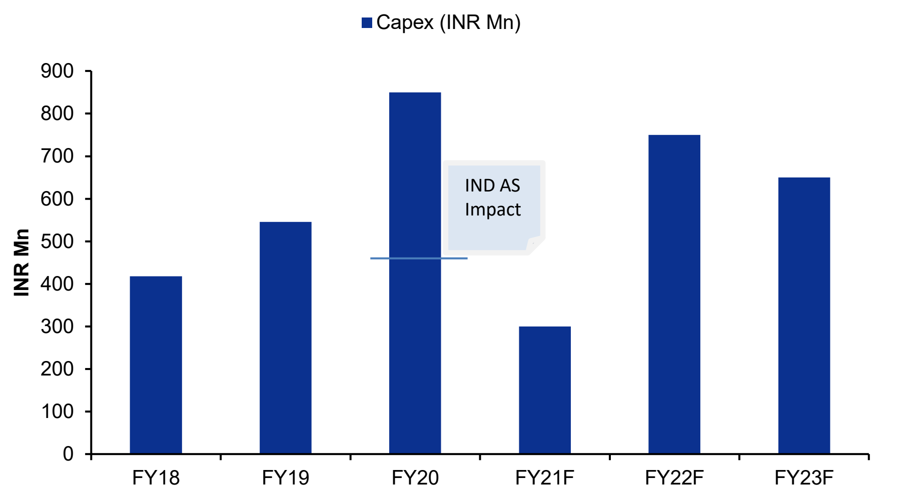
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 165: V-Guard's in-house production rose to 50% in Dec 2020



SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 166: V-Guard planning capex of Rs650m-800m per year



IND AS IS INDIAN ACCOUNTING STANDARD
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 167: Mix of in-house and outsourced manufacturing

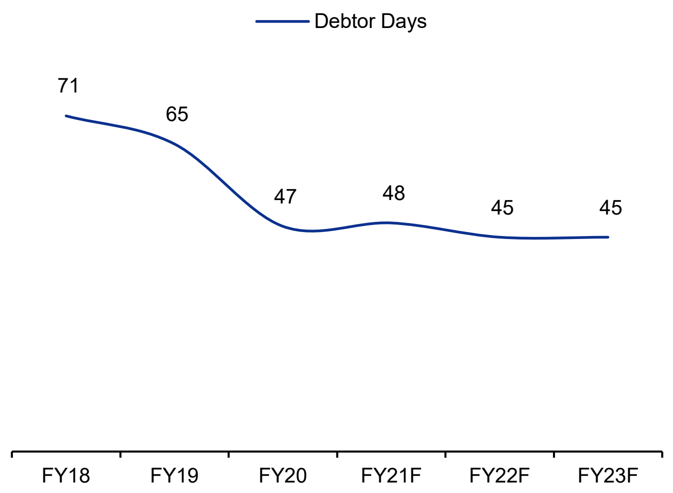
Product	No. of own manufacturing facilities	Location
PVC Wiring Cables	2	Coimbatore, Kashipur
Pumps & Motors	1	Coimbatore
Fans	2	Himachal Pradesh, Uttarakhand
Water Heater	2	Himachal Pradesh, Sikkim
Solar Water Heaters	1	Perundurai
Stabilisers	2	Sikkim
	Outsourced production facilities	
Stabilisers	57	Across India
Pumps	18	Across India
Fans	11	Across India
UPS	9	Across India

SOURCES: EIP RESEARCH, COMPANY REPORTS

Consistent discipline in working capital management ›

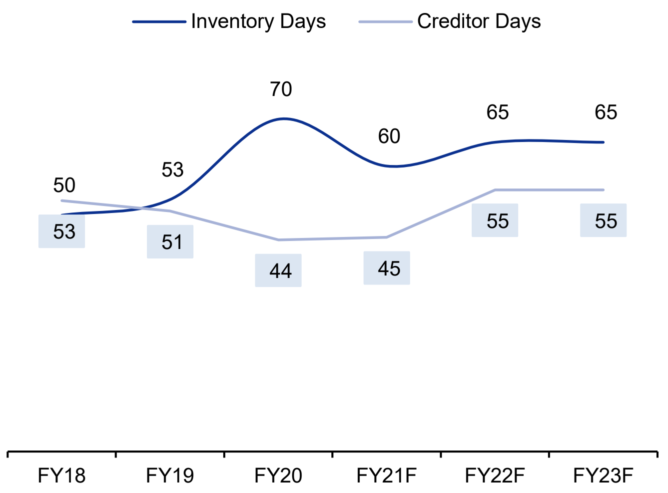
The company largely maintains its inventory and payables at similar levels of 55-65 days of sales, while receivables hover at ~45-50 days. However, the company further tightened trade practices and squeezed receivables to 40-45 days of sales during 9MFY21. We do not foresee further material improvements and expect net working capital to be maintained at ~50 days of sales over FY21-23F.

Figure 168: V-Guard's debtor days



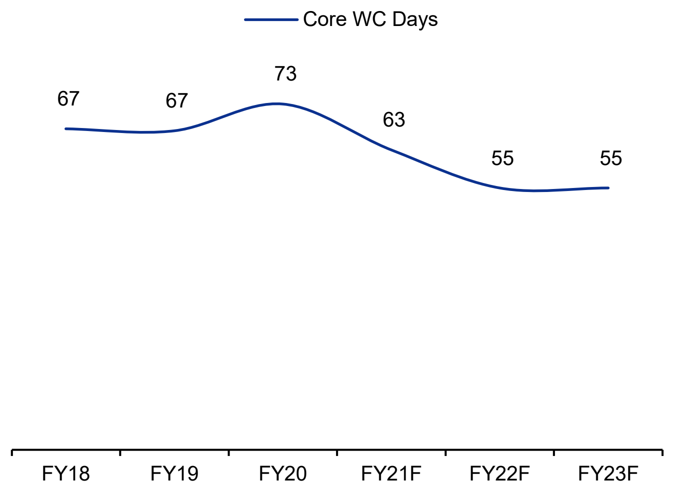
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 169: V-Guard's inventory and creditor days (of sales)



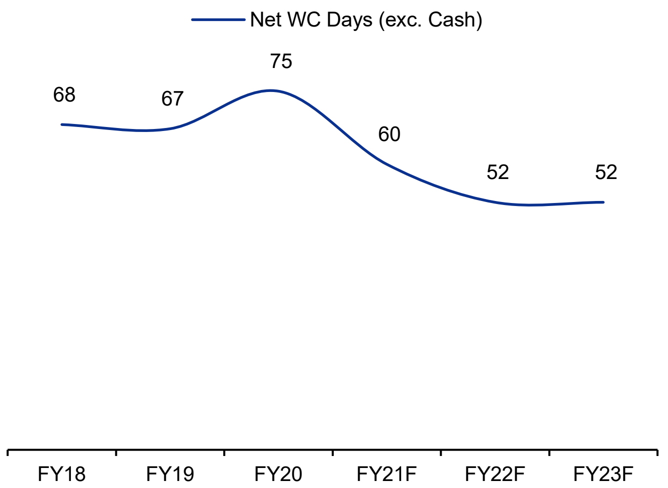
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 170: V-Guard's core working capital (WC) days



CORE WC DAYS = DEBTOR DAYS + INVENTORY DAYS – PAYABLE DAYS
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

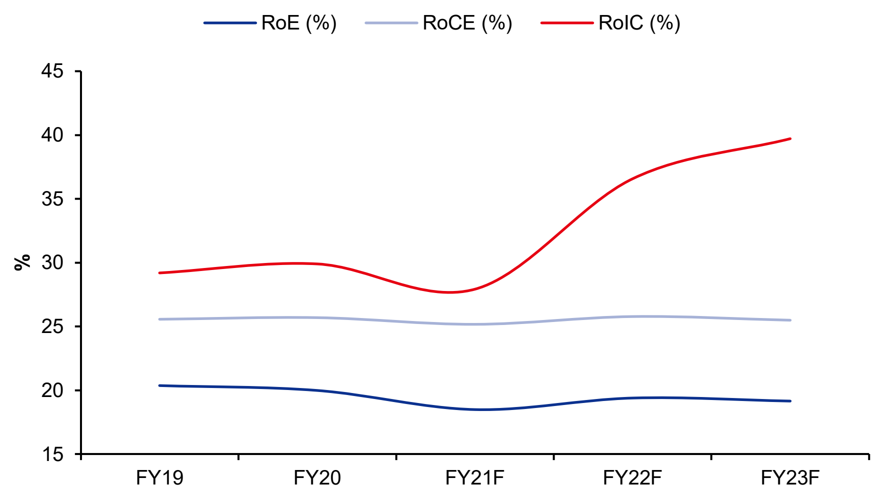
Figure 171: Net WC Days



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

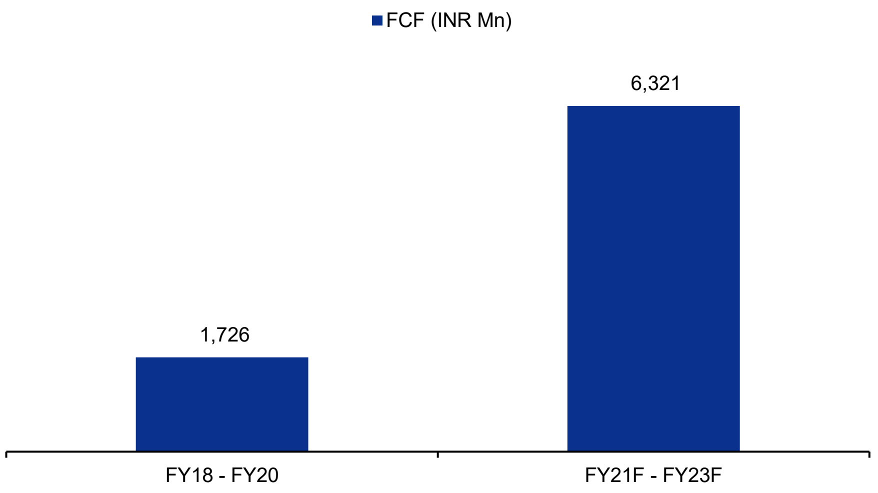
Expect return ratios to stay healthy in 18-40% range ›

Figure 172: V-Guard – Return ratios



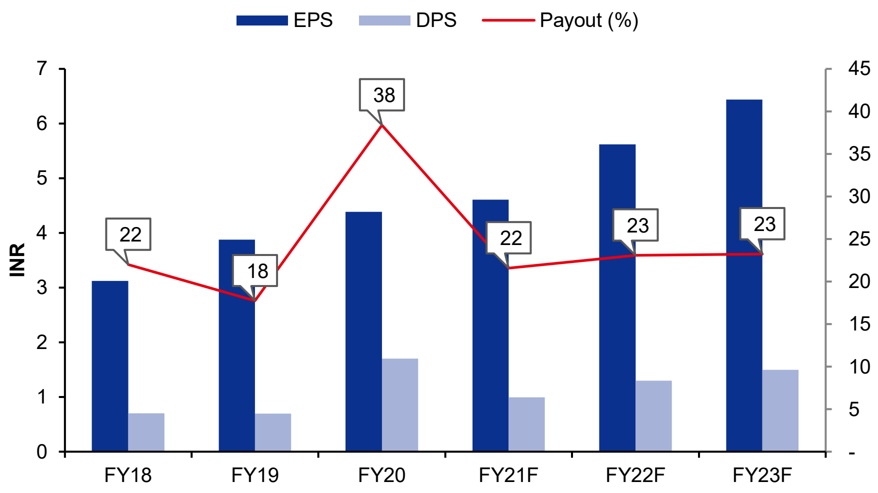
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 173: V-Guard – Cumulative free cash flow



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

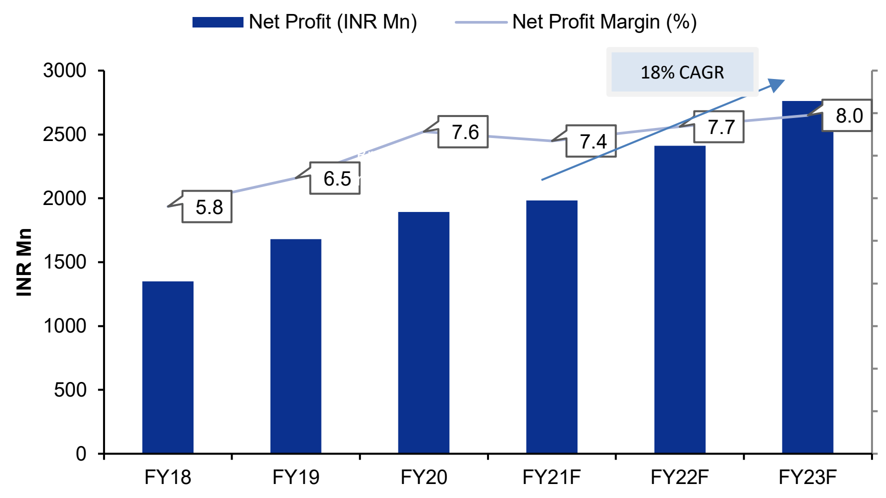
Figure 174: V-Guard's EPS, DPS and payout ratio (%)



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Net profit to rise gradually over the next three years

Figure 175: V-Guard's net profit CAGR of 18% over FY21-23F, net margins between 7-8%

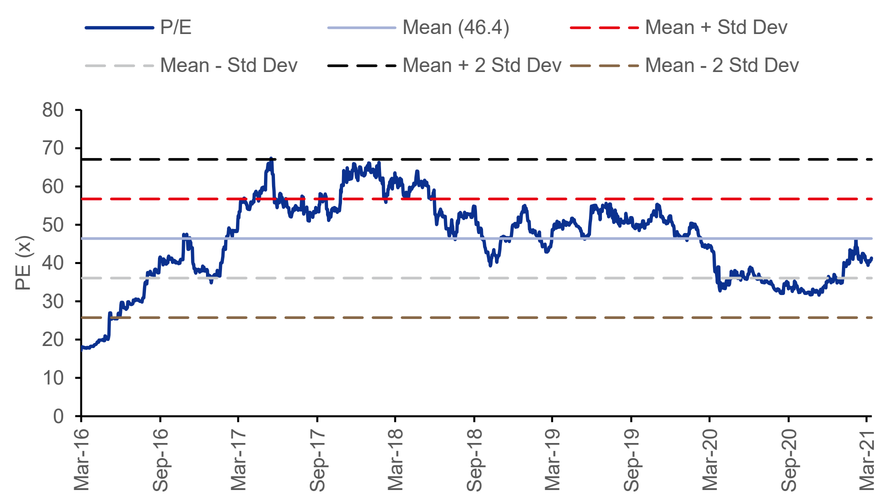


SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Valuation

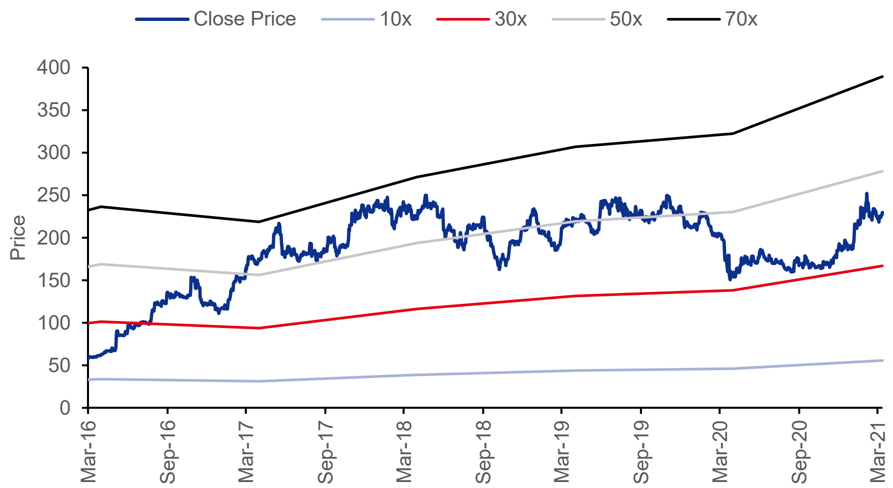
- The stock trades at P/E of 35.7x and EV/EBITDA of 23.4x FY23F estimates.
- Real estate demand has high correlation to V-Guard's revenue growth. Over the past five years, real estate sluggishness impacted revenue growth resulting in revenue CAGR of 3.7% over FY18-20.
- We believe the stock would re-rate and converge back to its five-year mean P/E, driven by a) reviving household improvement spends; b) revenue growth recovery to CAGR of 13.5% over FY21-23F; c) 18% EPS CAGR; d) cumulative free cash flow generation of Rs6.3bn over FY21-23F and; e) strong return ratios of 18-23% over the same period.
- We value at 43x (five-year mean) FY23F EPS and initiate coverage with an Add rating at Rs277 target price.

Figure 176: V-Guard's stock trading below its 5-year mean P/E (1 year forward)



SOURCES: EIP RESEARCH, COMPANY REPORTS, BLOOMBERG

Figure 177: P/E Band Chart



SOURCES: EIP RESEARCH, COMPANY REPORTS

Downside risks ›

- **High competition in new markets:** Over 40% of the revenues come from the Non-South India regions for V-Guard. Both the North and West India markets are dominated by larger and stronger FMEG brands. V-Guard's endeavour of further increasing its non-South India revenues to 60% over the next 5-10 years could be at risk in case of tough competition from incumbents in evolving geographies for V-Guard.
- **New product success:** Recent product launches of water purifiers, breakfast appliances, etc, are in line with widening the product portfolio and gaining market share in the small domestic appliances segment. In case the products do not find acceptance in the marketplace, this could impact our revenue estimates and lead to lower profits.
- **Supply chain risks:** Nearly 50% of product manufacturing is outsourced to third-party vendors by V-Guard. During the COVID-19 lockdown in India starting in Mar 2020, V-Guard suffered for lack of adequate product inventories owing to the vendor supply chains fractured due to raw material and labour availability. Similar events at vendor locations could negatively impact our revenue assumptions.
- **Distribution network reach:** The potential retail touchpoints in the North/West India markets are much higher vs the South. V-Guard has been gradually expanding its retail network by adding 3-5k touchpoints every year. It is critical for the company to consistently expand its distribution reach. Any slowness or delays could lead to lower revenues/profits vs our estimates.

Business description and management profile ›

V-Guard Industries (V-Guard) is a reputed Indian company manufacturing innovative and experiential products in electronics, electricals and consumer durables segments. V-Guard offers a range of products from voltage stabilisers to digital UPS, inverter batteries, electric and solar water heaters, domestic pumps, agricultural pumps, industrial motors, domestic switch gears, distribution boards, flexible wires, induction cooktops, mixer grinders, fans, rice cooker, gas stoves, solar power systems & air coolers.

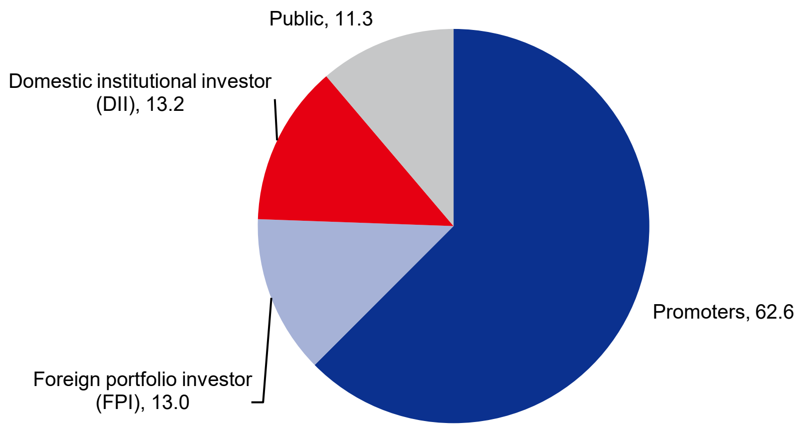
V-Guard's board of directors comprise four independent and non-independent directors each.

Figure 178: Key management personnel (FY20)

Name and Designation	Profile
Kochouseph Chittilappilly Chairman Emeritus V-Guard Industries	Mr Kochouseph Chittilappilly is the founder of V-Guard. He had been the Managing Director of the company since its inception. In Apr 2012, he passed on the baton to his son Mr Mithun Chittilappilly. In 2017 he assumed the position of Non-Executive Chairman of the Board and continued as such till Mar 2020. He assumed the office of Chairman Emeritus from Apr 2020. As Chairman, he was instrumental in adopting best governance practices and upholding the company's core values. He has been given numerous awards for exemplary performance in business. Among them are the Samman Pathra Award for top income taxpayer, Business Man of the Millennium 2000 from Rashtra Deepika and Tourism Man of the year from Destination Kerala.
Mithun K Chittilappilly Managing Director V-Guard Industries	Mr Mithun K Chittilappilly worked with MNCs like Deloitte and Hewlett Packard after graduating with a Bachelor of Commerce. In 2005 he took a break from work to pursue his post graduation in Management from the University of Melbourne, Australia. After graduating in May 2006, he joined the company as Executive Director and became the Managing Director of the company in Apr 2012. He holds a directorship on the board of V-Guard Foundation, the principal arm that implements V-Guard's CSR programmes.
V Ramachandran Director & Chief Operating Officer V-Guard Industries	Mr V. Ramachandran has over 30 years of cross-functional experience with companies like Hindustan Unilever and LG Electronics. In addition to leading the execution of corporate strategic initiatives and developing new growth platforms and business development, his mandate includes developing long-term business plans with supporting infrastructure development roadmap. Mr Ramachandran has been instrumental in several transformational processes being rolled out across Marketing, Customer Service, Supply Chain Management, Manufacturing Excellence and Research & Development.
Sudarshan Kasturi Chief Financial Officer V-Guard Industries	Sudarshan Kasturi is the Chief Financial Officer and Senior Vice President at V-Guard Industries. Mr Kasturi has a bachelor's degree from Birla Institute of Technology & Science and an MBA from the Indian Institute of Management Bangalore. Previously he was the Finance Director at Unilever Nigeria Plc.

SOURCES: COMPANY WEBSITE, COMPANY REPORTS

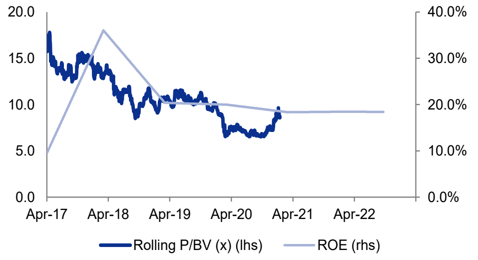
Figure 179: Share Holding Pattern (Dec 2020)



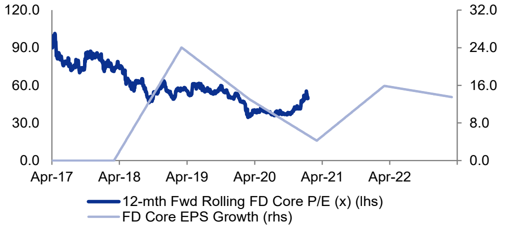
SOURCES: EIP RESEARCH, BSE WEBSITE

BY THE NUMBERS

P/BV vs ROE



12-mth Fwd FD Core P/E vs FD Core EPS Growth



Profit & Loss

(Rs mn)	Mar-19A	Mar-20A	Mar-21F	Mar-22F	Mar-23F
Total Net Revenues	**25,940**	**25,029**	**26,986**	**31,397**	**34,754**
Gross Profit	**7,875**	**8,412**	**8,568**	**10,126**	**11,382**
Operating EBITDA	**2,243**	**2,580**	**2,915**	**3,485**	**3,945**
Depreciation And Amortisation	(230)	(294)	(372)	(448)	(512)
Operating EBIT	**2,013**	**2,286**	**2,543**	**3,037**	**3,433**
Financial Income/(Expense)	122	157	148	160	233
Pretax Income/(Loss) from Assoc.					
Non-Operating Income/(Expense)	61	53	30	30	30
Profit Before Tax (pre-EI)	**2,196**	**2,496**	**2,721**	**3,227**	**3,696**
Exceptional Items					
Pre-tax Profit	**2,196**	**2,496**	**2,721**	**3,227**	**3,696**
Taxation	(515)	(613)	(732)	(810)	(928)
Exceptional Income - post-tax					
Profit After Tax	**1,680**	**1,883**	**1,989**	**2,417**	**2,768**
Minority Interests		11	(5)	(5)	(5)
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	**1,680**	**1,894**	**1,984**	**2,412**	**2,763**
Recurring Net Profit	1,680	1,894	1,984	2,412	2,763
Fully Diluted Recurring Net Profit	**1,680**	**1,894**	**1,984**	**2,412**	**2,763**

Cash Flow

(Rs mn)	Mar-19A	Mar-20A	Mar-21F	Mar-22F	Mar-23F
EBITDA	2,243	2,580	2,915	3,485	3,945
Cash Flow from Invt. & Assoc.					
Change In Working Capital	(416)	(515)	732	(37)	(478)
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense					
Other Operating Cashflow	339	247	178	190	263
Net Interest (Paid)/Received	(80)	(110)	(148)	(160)	(233)
Tax Paid	(524)	(788)	(732)	(810)	(928)
Cashflow From Operations	**1,563**	**1,414**	**2,944**	**2,669**	**2,569**
Capex	(545)	(850)	(300)	(750)	(650)
Disposals Of FAs/subsidiaries	16	4			
Acq. Of Subsidiaries/investments	(68)	(397)	(834)	(500)	(500)
Other Investing Cashflow	88	125	199	213	289
Cash Flow From Investing	**(508)**	**(1,118)**	**(935)**	**(1,037)**	**(861)**
Debt Raised/(repaid)	94	(13)			
Proceeds From Issue Of Shares	46	22			
Shares Repurchased					
Dividends Paid	(359)	(875)	(428)	(557)	(642)
Preferred Dividends					
Other Financing Cashflow	(33)	(48)	(51)	(53)	(56)
Cash Flow From Financing	**(252)**	**(915)**	**(480)**	**(610)**	**(698)**
Total Cash Generated	802	(619)	1,530	1,022	1,010
Free Cashflow To Equity	**1,149**	**282**	**2,009**	**1,632**	**1,708**
Free Cashflow To Firm	**1,046**	**264**	**1,958**	**1,578**	**1,652**

SOURCES: EIP RESEARCH, COMPANY REPORTS

BY THE NUMBERS…cont'd

Balance Sheet

(Rs mn)	Mar-19A	Mar-20A	Mar-21F	Mar-22F	Mar-23F
Total Cash And Equivalents	1,688	1,476	3,505	5,027	6,536
Total Debtors	4,591	3,243	3,549	3,871	4,285
Inventories	3,764	4,790	4,436	5,591	6,189
Total Other Current Assets	818	1,096	887	1,032	1,143
Total Current Assets	**10,861**	**10,604**	**12,377**	**15,521**	**18,153**
Fixed Assets	2,267	2,805	3,352	3,654	3,792
Total Investments	3	3	337	337	337
Intangible Assets	37	37	37	37	37
Total Other Non-Current Assets	549	1,100	481	481	481
Total Non-current Assets	**2,855**	**3,945**	**4,207**	**4,509**	**4,647**
Short-term Debt	141	128	128	128	128
Current Portion of Long-Term Debt					
Total Creditors	3,592	3,051	3,327	4,731	5,237
Other Current Liabilities	787	910	1,109	1,290	1,428
Total Current Liabilities	**4,520**	**4,089**	**4,564**	**6,149**	**6,793**
Total Long-term Debt	36				
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	115	469	469	469	469
Total Non-current Liabilities	**152**	**469**	**469**	**469**	**469**
Total Provisions	26				
Total Liabilities	**4,698**	**4,558**	**5,033**	**6,618**	**7,262**
Shareholders Equity	8,994	9,955	11,510	13,366	15,487
Minority Interests	25	36	41	46	51
Total Equity	**9,019**	**9,991**	**11,551**	**13,412**	**15,538**

Key Ratios

	Mar-19A	Mar-20A	Mar-21F	Mar-22F	Mar-23F
Revenue Growth	11.5%	(3.5%)	7.8%	16.3%	10.7%
Operating EBITDA Growth	17.8%	15.0%	13.0%	19.6%	13.2%
Operating EBITDA Margin	8.6%	10.3%	10.8%	11.1%	11.3%
Net Cash Per Share (Rs)	3.48	3.12	7.84	11.41	14.92
BVPS (Rs)	20.75	23.04	26.72	31.12	36.06
Gross Interest Cover	114.38	54.94	49.38	56.77	61.74
Effective Tax Rate	23.5%	24.6%	26.9%	25.1%	25.1%
Net Dividend Payout Ratio	16.4%	35.0%	15.8%	17.3%	17.4%
Accounts Receivables Days	63.91	57.12	45.93	43.13	42.83
Inventory Days	70.00	93.94	91.41	86.03	91.99
Accounts Payables Days	70.24	72.96	63.20	69.14	77.83
ROIC (%)	29.2%	29.9%	27.9%	36.6%	39.7%
ROCE (%)	25.6%	25.7%	25.2%	25.8%	25.5%
Return On Average Assets	16.3%	16.6%	16.5%	16.8%	16.2%

SOURCES: EIP RESEARCH, COMPANY REPORTS

CGSCIMB

Company Note

INITIATION

Industrial - Overall | India | March 15, 2021

InCred

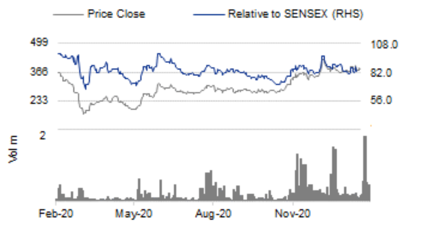
India

ADD *(Initiating coverage)*

Consensus ratings*:	Buy 8	Hold 1	Sell 0

Current price:	Rs403
Target price:	Rs504
Previous target:	N/A
Up/downside:	25.1%
EIP Research / Consensus:	5.2%
Reuters:	FNXC.NS
Bloomberg:	FNXC IN
Market cap:	US$846m
	Rs61,596m
Average daily turnover:	US$1.5m
	Rs108.9m
Current shares o/s:	153.0m
Free float:	64.1%

**Source: Bloomberg*



Source: Bloomberg

Price performance	*1M*	*3M*	*12M*
Absolute (%)	2.5	12.2	44.6
Relative (%)	4.0	1.8	1.6

Major shareholders	% held
Promoters	35.9
Finolex Industries Limited	14.5
Franklin India Taxshield	6.8

Finolex Cables Ltd

Fine and Flexible enough to bounce back

- We expect slow but steady revenue growth recovery over FY21-23F.
- We believe focus on backward integration and technology differentiates Finolex from its peers.
- We think the market is yet to fully appreciate the stock's intrinsic value potential; we initiate coverage with an Add rating and TP of Rs504.

Next three fiscals expected to be much better than the past three

We think improving urban real estate absorption rates, need for deeper optic fibre network (work from anywhere) and revenge-spending trends on home improvement spends over 2Q/3QFY21 are factors likely to revive demand for Electrical cables (FY20: ~80% revenue), Communication cables (~15% revenue) and FMEG product sales (~5% revenue) going forward. We feel underutilised capacities can cater to rising demand. FMEG network expansion/brand building will continue and take more time to reach meaningful scale, in our view. We expect revenue to recover to 13.2% CAGR (FY18-20: 1%) over FY21-23F.

Product quality, backward integration and lean cost of operations

We believe these factors drive superior gross/EBITDA margins for Finolex vs its cable and wires (C&W) peers (except Havells). Technical tie-ups, self-control on start-to-finish production value chain and focus on consistent product quality are key differentiators. The C&W segment earns premium EBIT margins. However lower communication/FMEG EBIT margins impact consolidated EBIT profitability. We expect better overall capacity utilisation, recovery in optical fibre cable (OFC) margins and higher FMEG margins (EBIT breakeven in FY21F) to aid EBITDA growth. We estimate EBITDA CAGR of 24.3% and EBITDA margins to scale back to 15-15.5% over FY21-23F.

Capex picks up, good inventory management; what to do with cash?

Finolex has announced capex of Rs2bn in fresh capacities of solar cables/instrumentation cables/conduit pipes and further backward integrate for solar (tinned copper) /power cables (copper-clad steel) over FY21-23F. Finolex has not availed of vendor channel financing and buys copper at negligible credit terms. B2C revenue share was ~65% (FY20) and we expect it to increase gradually as FMEG revenue scales up. There is limited clarity on redeployment of surplus cash (~Rs18bn by Mar 2021F) in the business, dividend payments or its usage for inorganic growth options. A clearer roadmap on cash utilisation would lead to clarity on company capital allocation policy, in our view.

Reasonable margin of safety due to intrinsic value; initiate with Add

Finolex offers a good investment opportunity due to high franchise value, solid cash flows, surplus cash of ~30% of current market cap (Feb 2021), 32.4% equity stake in Finolex Industries (worth ~Rs24bn) and the stock trading marginally higher to its 10-year mean P/E. We think the promoter family feud has led to a reasonable margin of safety given high intrinsic business value. We have a sum-of-parts-based TP of Rs504 based on Rs382/sh (P/E of 13x core FY23F EPS) and Rs122/sh (25% haircut to current market cap) for the equity stake in Finolex Industries. Key risks: Elongated inheritance settlement, capex execution delays.

Financial Summary	Mar-19A	Mar-20A	Mar-21F	Mar-22F	Mar-23F
Revenue (Rsm)	30,778	28,773	27,474	32,101	35,189
Operating EBITDA (Rsm)	4,697	3,835	3,475	4,831	5,366
Net Profit (Rsm)	4,074	3,911	4,028	4,881	5,417
Core EPS (Rs)	26.6	25.6	26.3	31.9	35.4
Core EPS Growth	23.4%	(4.0%)	3.0%	21.2%	11.0%
FD Core P/E (x)	15.12	15.75	15.29	12.62	11.37
DPS (Rs)	4.0	4.5	4.5	5.0	5.5
Dividend Yield	1.20%	1.35%	1.12%	1.24%	1.37%
EV/EBITDA (x)	10.51	12.29	12.56	8.57	6.98
P/FCFE (x)	140.82	6.89	16.78	24.08	14.43
Net Gearing	(44.7%)	(48.1%)	(53.7%)	(53.9%)	(57.4%)
P/BV (x)	2.25	2.05	1.85	1.64	1.46
ROE	15.8%	13.6%	12.7%	13.8%	13.6%
% Change In Core EPS Estimates					
EIP Research/Consensus EPS (x)			1.15	1.09	1.08

SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS. PRICED AS AT 12 MAR 2021

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Fine and Flexible enough to bounce back

Slow but steady revenue growth expected

Next three fiscals to be much brighter than the past three ›

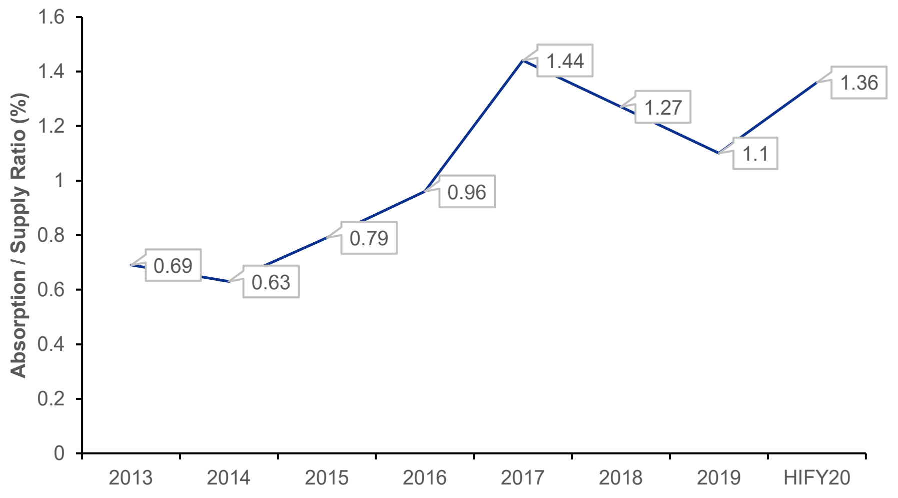
"We have to keep in mind the real estate sector has actually been in a bad way for the last three to four years and it is not only COVID which is coming and impacting a booming real estate sector. So, to a reasonable extent we believe that the impact has already been baked into the base trend. So, it is not that it was a booming real estate market which is suddenly going to collapse."
– Shantanu Khosla, MD, Crompton Greaves Consumer 4QFY20 investor call

"The key trends that we can point out are that there are structural tailwinds, which we experienced in the third quarter, the demand was definitely increasing even in the real estate and consumer segments, which had been tepid for a couple of years now."
– Anil Rai Gupta, CMD, Havells India 3QFY21 investor call

"Tailwinds due to heightened consumer demand for all types of home appliances in the wake of increased home bound working, together with a strong support of pent-up demand and festival season in the last quarter, led to encouraging growth in offtakes."
– Orient Electric 3QFY21 investor release

We believe consumer demand since the COVID-19 unlock (starting Jun 2021) has recovered strongly. The B2C product categories (housing wires, few communication type cables and FMEG) have seen faster recovery compared to their B2B counterparts (optical fibre cables (OFC) and auto/industrial/power cables). India saw a significant slowdown in discretionary consumption spending over FY18-20 and then the COVID-19 pandemic impacted FY21F. We think lead indicators of higher real estate inventory absorption rates in urban markets, better volume growth reported by consumer discretionary product companies and focused infrastructure investments by the Indian government should sustain demand growth over the medium term.

Figure 180: Real estate absorption to supply ratio (top 7 cities by population) in India



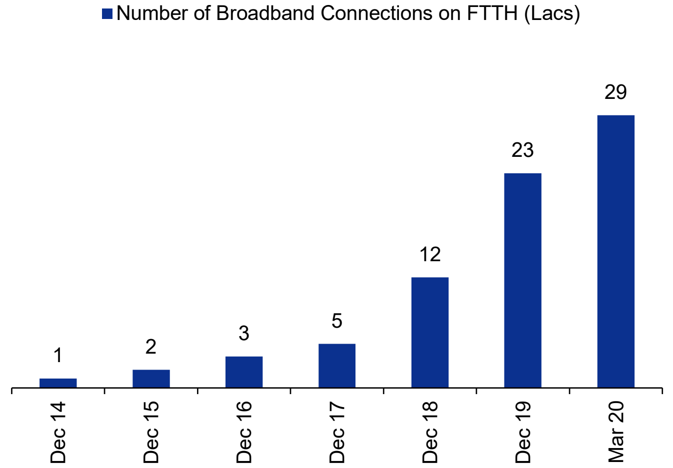
SOURCES: FEDERATION OF INDIAN CHAMBERS OF COMMERCE & INDUSTRY (FICCI), EIP RESEARCH

Figure 181: COVID-19 aiding real estate demand recovery

COVID-19 trend	Indicator of demand recovery
Work from home and online schooling is a new normal	• Remote working has led to the rise of demand for housing options in peripheral areas
De-densify to improve social distancing	• Close to 900 plotted units were launched in the last 4-5 months in Chennai • NCR witnessed huge demand for farmhouses, and average monthly transactions have gone up from 2-3 in the pre-COVID era to 10-12 as of now • In Ahmedabad, the demand for second homes, from areas around Shilaj to Racharda, has increased by around 40%
Preference to reside in a controlled environment	• The growing demand for these townships is such that the past few years have seen markets beyond the metro cities become a prime destination for the segment
Reverse migration/work from hometown to redefine the real estate demand	• According to a leading bank, the demand for home loans across the country has increased. Much of the demand is for small- to mid-sized apartments, where typically the property price would be about Rs35lakh-40 lakh • As remote working continues, demand for housing in tier-2 and -3 cities are likely to rise
Avoidance of execution risk	• As of 2020, nearly 17% of the unsold inventory was ready-to-move-in across the top seven cities of India
Customers are ready to pay premium for quality	• Sales of the top eight listed players accounted for 25% of the overall sales (1HFY21) in the top seven cities of India compared to 14% in FY20

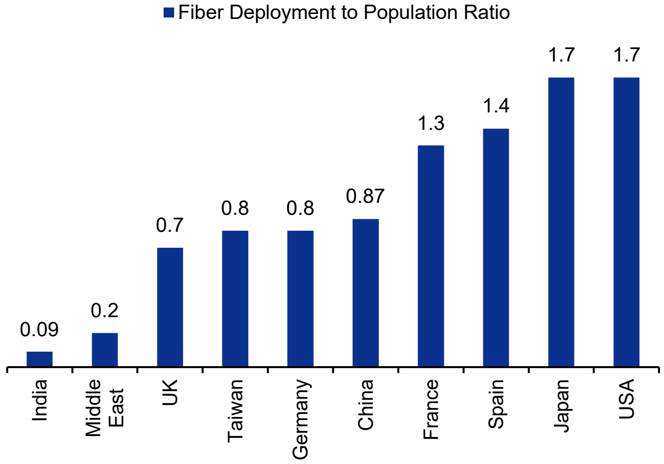
NCR IS THE NATIONAL CAPITAL REGION
SOURCES: EIP RESEARCH, ANAROCK

Figure 182: Rising demand for broadband services in India



FTTH IS FIBRE-TO-THE-HOME
SOURCES: EIP RESEARCH, TELECOM REGULATORY AUTHORITY OF INDIA (TRAI)

Figure 183: India's fiber network is still underpenetrated (Mar 2020)



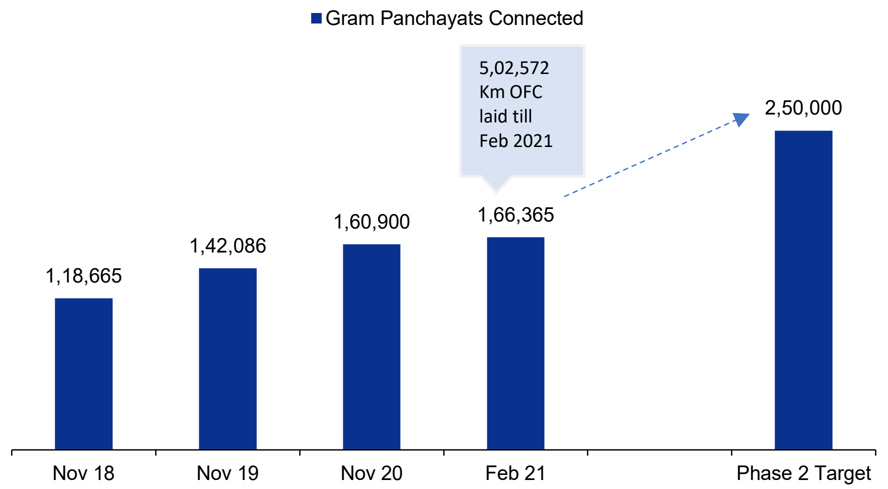
DATA AS AT MARCH 2020
SOURCES: EIP RESEARCH, TRAI

In terms of State-led fibre projects, there are two projects where we are involved. Kerala – we already got the order from Bharat Electronics. For the Telangana project our partners have bid and they have won and they have got the purchase orders."
– Tejas Networks, 3QFY20 investor call

Specifically, on the government side in BSNL we won a tender for BharatNet expansion in two states where there was not enough coverage as part of the 650,000-village programme. So, we should be getting the order in this current quarter.
– Tejas Networks, 3QFY21 investor call

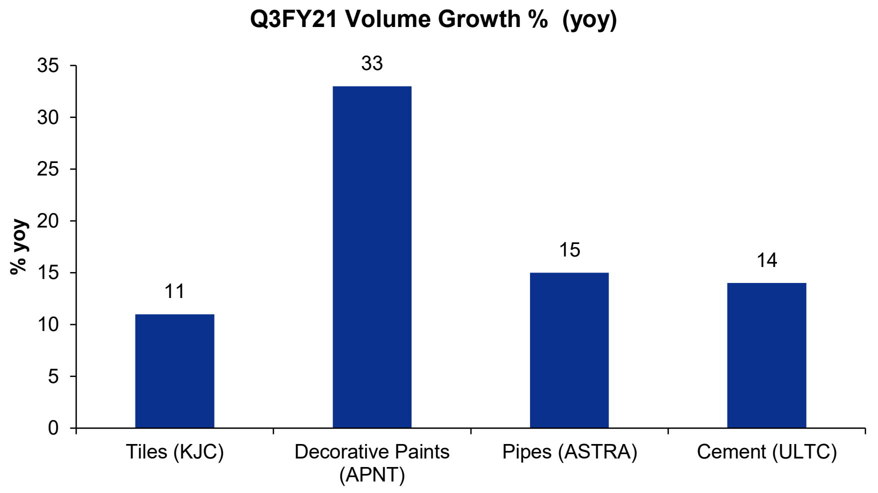
"Our vision is that all public institutions at Gram Panchayat-level such as Anganwadis, health and wellness centres, government schools, PDS outlets, post offices and police stations will be provided with digital connectivity – Fibre to the Home (FTTH) connections – through BharatNet, linking 100,000 Gram Panchayats this year."
– Nirmala Sitharaman, India Budget Feb 2021

Figure 184: BharatNet Progress – Programme to connect rural India with Internet



OFC IS OPTIC FIBRE CABLES
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 185: Housing related sectors saw pick-up in customer demand in 3QFY21



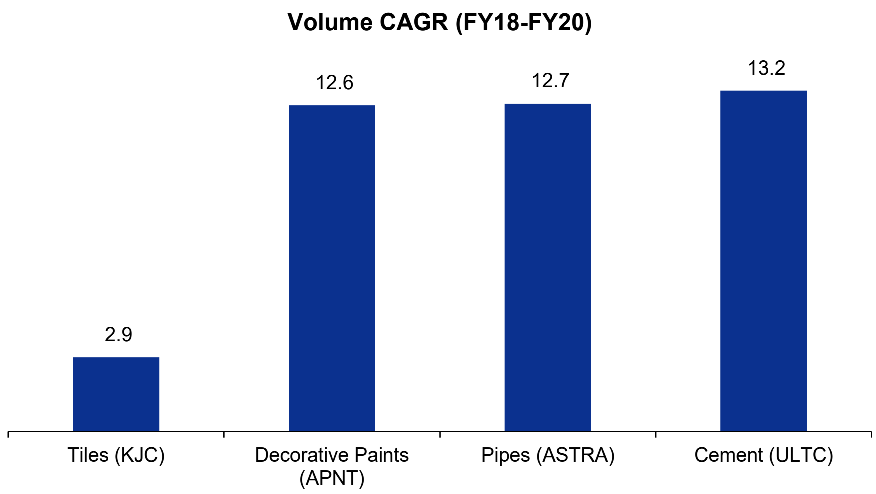
KJC IS KAJARIA CERAMICS, APNT IS ASIAN PAINTS, ASTRA IS ASTRAL PIPES, ULTC IS ULTRATECH CEMENT
SOURCES: EIP RESEARCH, COMPANY REPORTS

Dislocation of demand drivers led to slow revenue growth

China, after almost 10-odd years, there is 13% volume de-growth, which is happening in 2019 and that volume degrowth is coupled with supply-side economics which has happened and which has led to a price dip within the year.
– Sterlite Technologies, Oct 2019 investor call

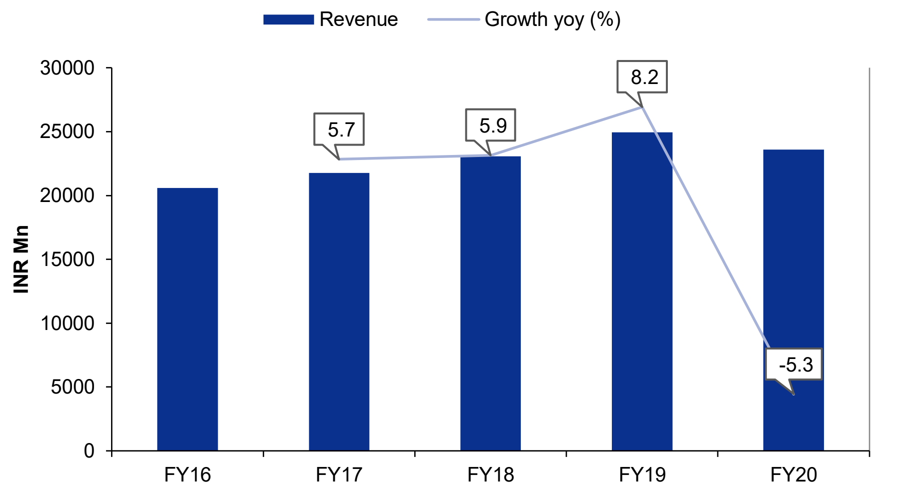
The pace of economic growth in India slowed over FY18-20 and impacted most of the demand drivers described in the section above. The figures below depict the nature and extent of the slowdown across sectors and Finolex Cables too saw flat revenue growth (1% CAGR) over this period.

Figure 186: Home improvement spends were relatively slow over FY18-20



KJC IS KAJARIA CERAMICS, APNT IS ASIAN PAINTS, ASTRA IS ASTRAL PIPES, ULTC IS ULTRATECH CEMENT
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 187: Low housing spends impacted Finolex's Electrical Cables revenue growth

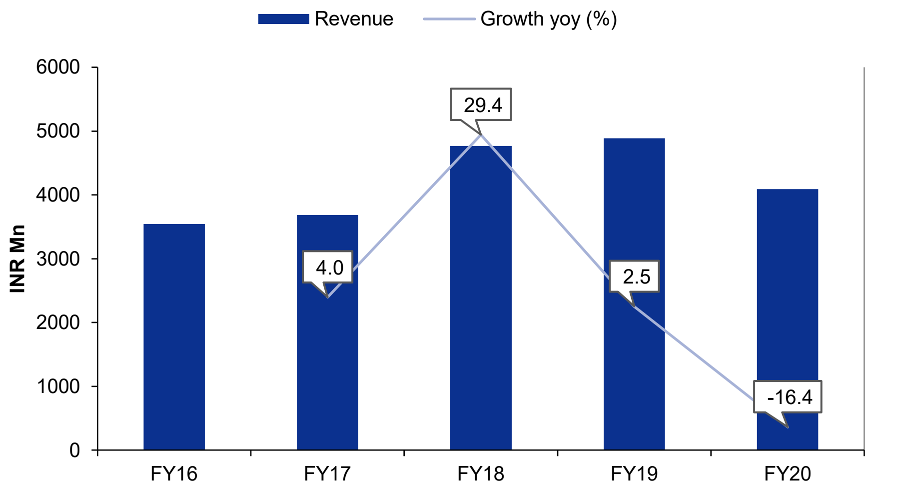


SOURCES: EIP RESEARCH, COMPANY REPORTS

"Even fibre prices have dropped from \$6 to \$3. Because China Mobile suddenly scrapped a 100m kilometre fibre tender, worldwide prices dropped."
– Finolex Cables, 2QFY21 investor call

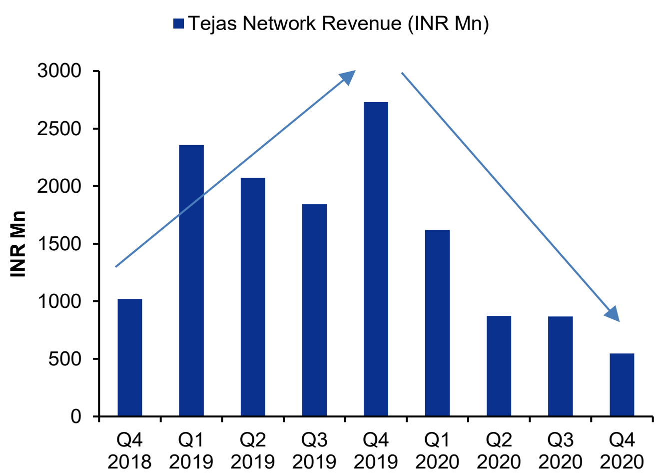
"The government business during the first half was very weak and we had a revenue decline of 88% yoy. We do not expect any new business from BSNL or BharatNet, at least the Central BharatNet for the rest of the year given where the government situation is."
– Tejas Networks, 2QFY20 investor call

Figure 188: Finolex's Communication Cable revenue growth suffered



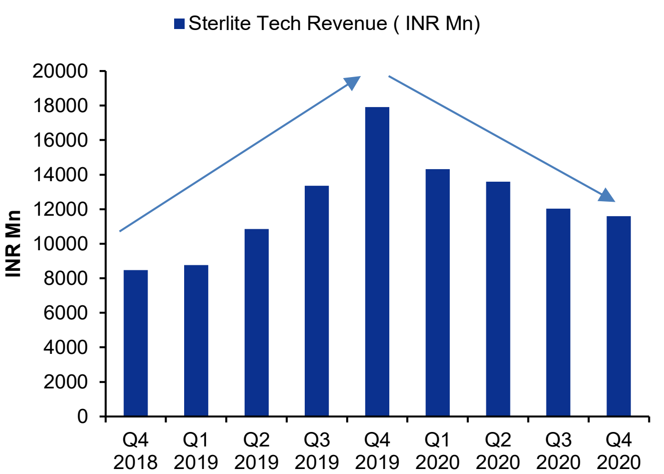
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 189: Volatile government/private OFC capex spends impacted Tejas Network's revenue



SOURCES: EIP RESEARCH, BLOOMBERG

Figure 190: Sterlite Tech impacted due of OFC volatility



SOURCES: EIP RESEARCH, BLOOMBERG

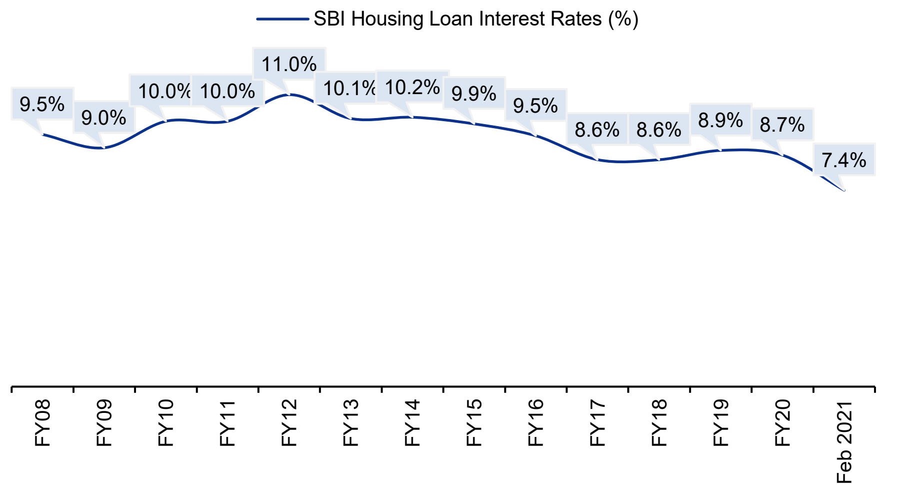
The Cables business segment registered a revenue decline of 37.5% yoy due to severe contraction in demand for optical fibre cables coupled with pricing pressures due to excess capacity globally and elevated inventory levels of optical fibre.

– Vindhya Telelinks – FY20 Annual Report

"Over the last two years, the investment in fibre assets by the private telcos has also not been of high value. They are now targeting to reach homes and, therefore, while there are more cable kilometres to be sold, the fibre content in them is very small, it is maybe one or two fibres. So, the value realised for that is not as high as you would when a trunk line is being commissioned."

– Finolex Cables, 3QFY21 investor call

Figure 191: Urban real estate affordability was low due to high interest rates

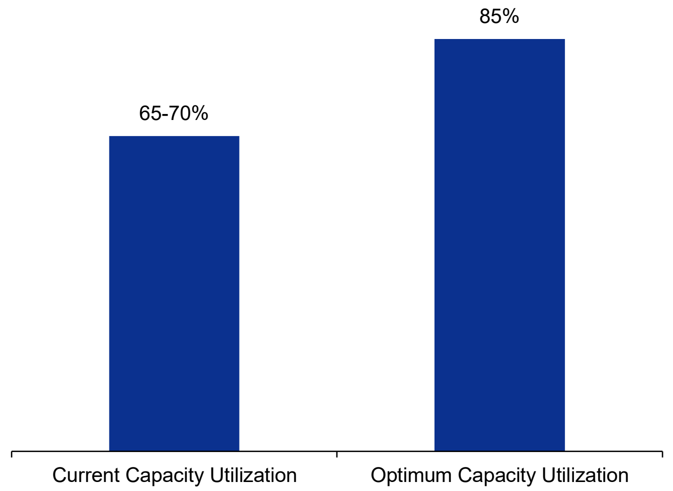


SOURCES: EIP RESEARCH, COMPANY REPORTS

Enough capacity available to cater to rising demand ›

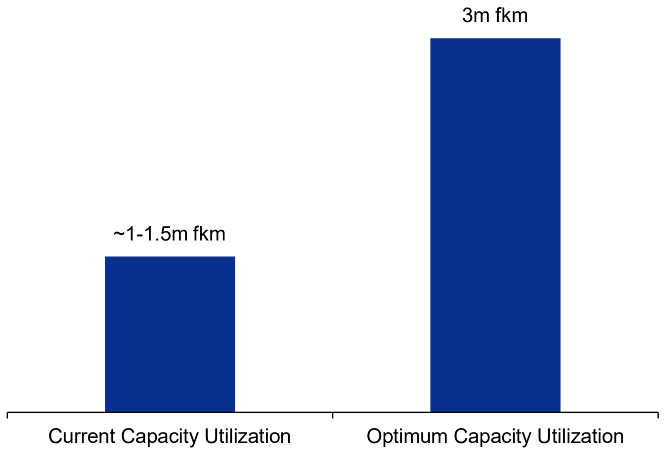
Finolex has 100% of the cables and wires manufactured in-house while the smaller FMEG products (~4% of FY21F sales) continue to be 100% outsourced. Capacity utilisation stood at 65% (75% excluding Ponda, Goa plant) in FY20 and dropped sharply due to COVID-19 lockdown in 1QFY21. In line with the consumer demand recovery, utilisations recovered to ~70% levels in 3QFY21 and we expect them to rise to 75-80% in the next 12 months. We believe most segments like housing wires, auto and industrial cables, communication cables (excluding OFC) and FMEG have enough spare capacity today to meet rising demand.

Figure 192: Finolex's Electrical Cables capacity utilisation (Dec 20)



SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 193: Finolex's Communication Cable capacity utilisation (Dec 20)



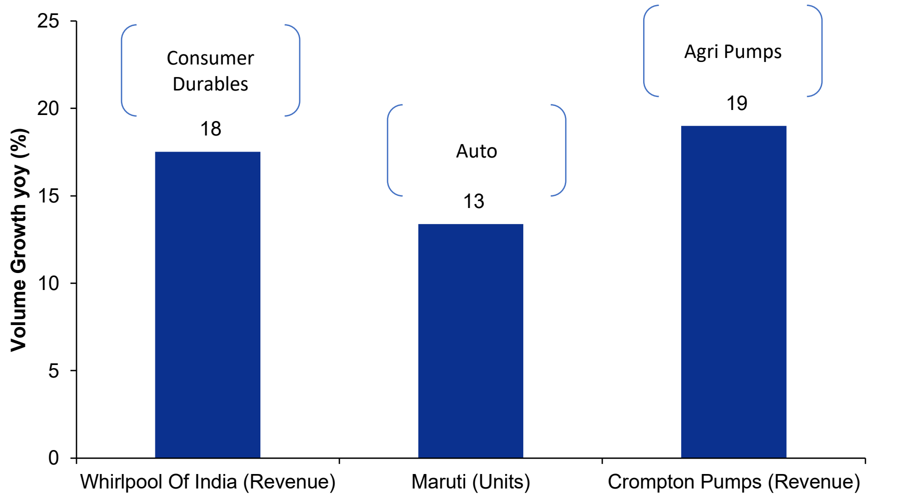
FKM IS FIBRE KILOMETRE
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 194: Manufacturing footprint (FY20)

Roorkee, Uttarakhand	Construction and automobile wires, switches and SG, agri applications
Shirwal, Maharashtra	Extra High Voltage (EHV) cables
Urse, Pune	Electrical cables, OFC, other communication cables
Pimpri, Pune	Telephone cables, winding wire for submersible pumps
Verna Goa	All products except power and LAN cables
Ponda Goa	Copper rods
100% Outsourced	FMEG

SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 195: Rising demand for instrumentation, auto and agri cables is evident from tailwinds for these players (3QFY21 yoy growth)



SOURCES: EIP RESEARCH, COMPANY REPORTS

Volume growth is gradually coming back for Finolex as well

Sharp recovery in 3QFY21 volume growth was partially due to the festive season demand while advance buying by dealers also helped due to anticipated price increases led by commodity cost pressures. For Finolex, wires grew 9% yoy while LAN cables, CCTV or coaxial cables, each grew 25% yoy in 3QFY21. OFC volumes rose 23% yoy and the newer product lines of switchgear, switches, fans, water heaters and lighting products, all grew over 30% yoy in 3QFY21.

Will need more patience for FMEG revenue to reach reasonable scale ›

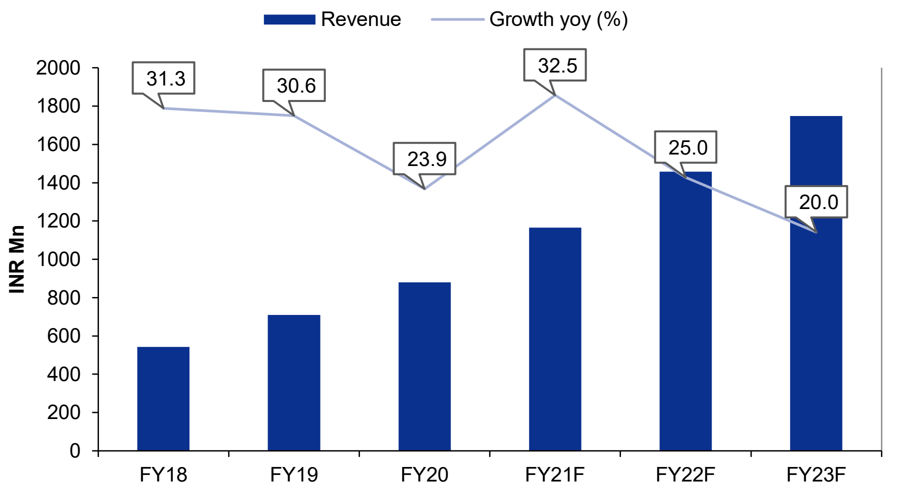
We estimate Finolex's FMEG revenue to surpass the Rs1bn mark by Mar 2021.

We estimate Finolex Cables to clock ~Rs1bn of FMEG revenues in FY21F. The company initiated its FMEG journey with electrical switches and lighting segments but could not scale up due to product design issues and fast-changing lighting technologies. Peers like Polycab (POLYCAB IN, Add, CMP Rs1360), which started much later, have scaled up faster and gained reasonable market share in terms of FMEG revenues. We estimate Polycab to reach nearly ~Rs10bn of FMEG revenues in FY21F. Finolex is gradually deepening its distribution network and leveraging the 4k C&W channel partner network to make its FMEG products widely available. We expect this exercise to take some more time after which the company would focus on increasing its brand recall through higher advertising and sales promotion spends in sync with FMEG market leaders.

In FY19, Finolex Cables launched the first of its exclusive retail store chains, Finolex House and opened four stores at Chennai, Vadodara, Bhopal and Ghaziabad. In FY20, the company opened a store each at Secunderabad, Jamshedpur, Bengaluru and Raipur. The company plans to open 50 such Finolex House stores across the country over the next two years.

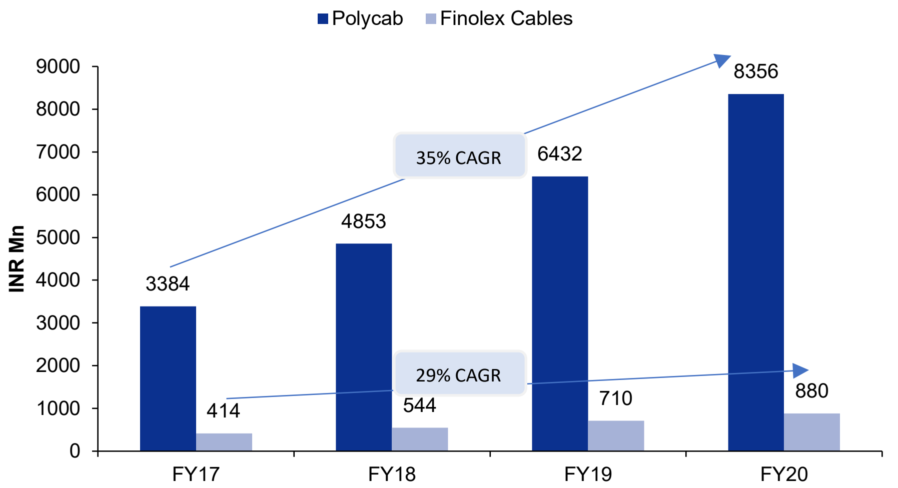
We estimate FMEG revenues for Finolex Cables to grow at over 20% CAGR and reach ~Rs2bn by FY23/24F.

Figure 196: Finolex Cables' FMEG revenue



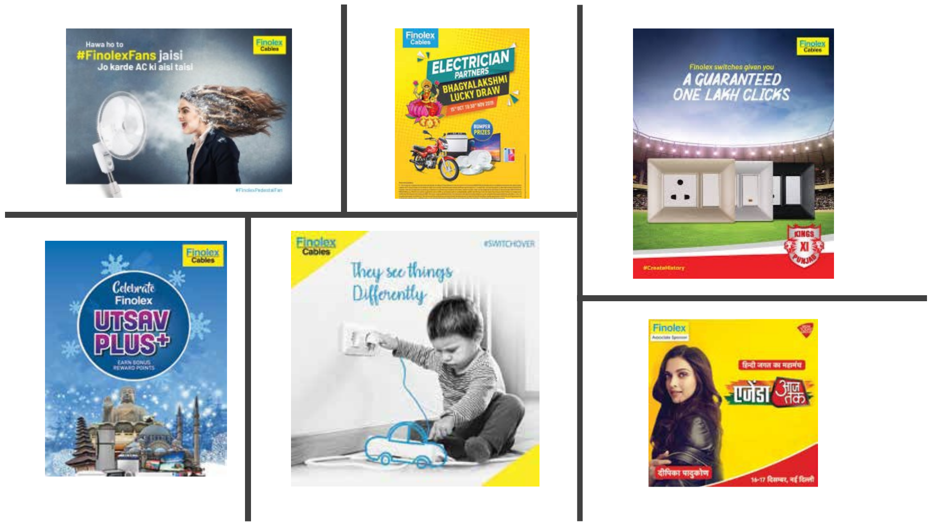
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 197: Finolex Cables' FMEG revenues grew slower than its peers



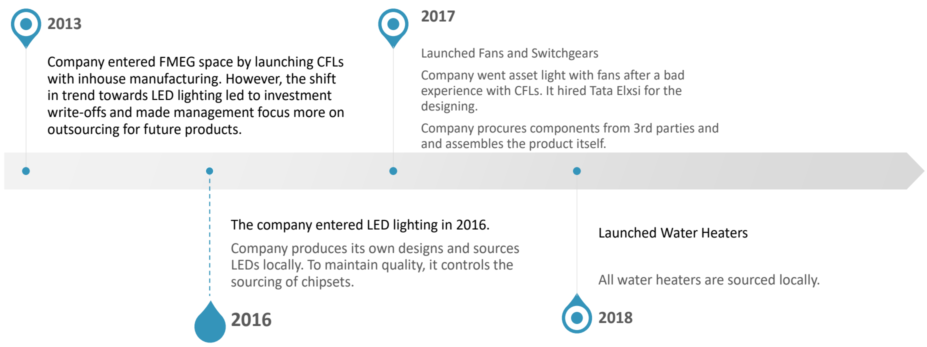
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 198: Finolex Cables' advertisements



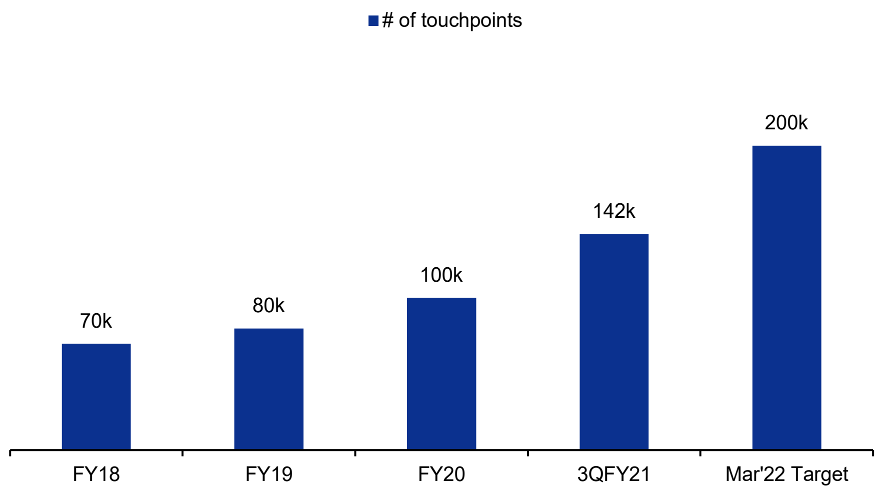
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 199: FMEG product launch timeline



SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 200: Pan India retail network



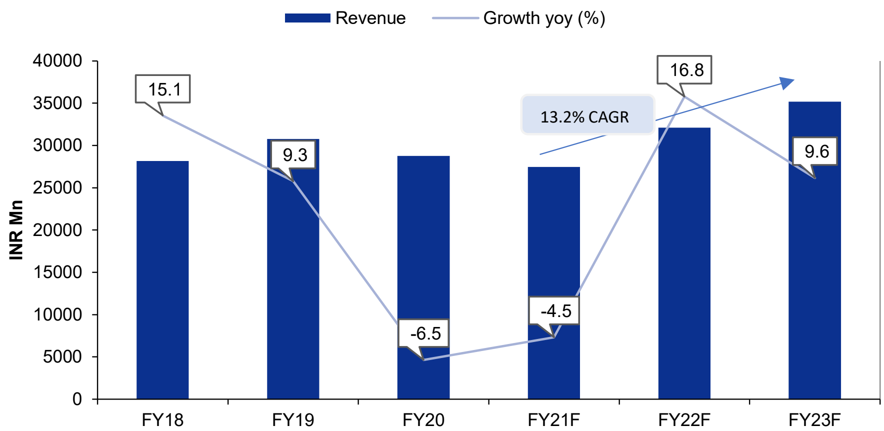
SOURCES: EIP RESEARCH, COMPANY REPORTS

Revenues to grow at double-digit CAGR

Revenue growth will be a function of macroeconomic growth recovery and higher management focus going forward for Finolex Cables, in our view.

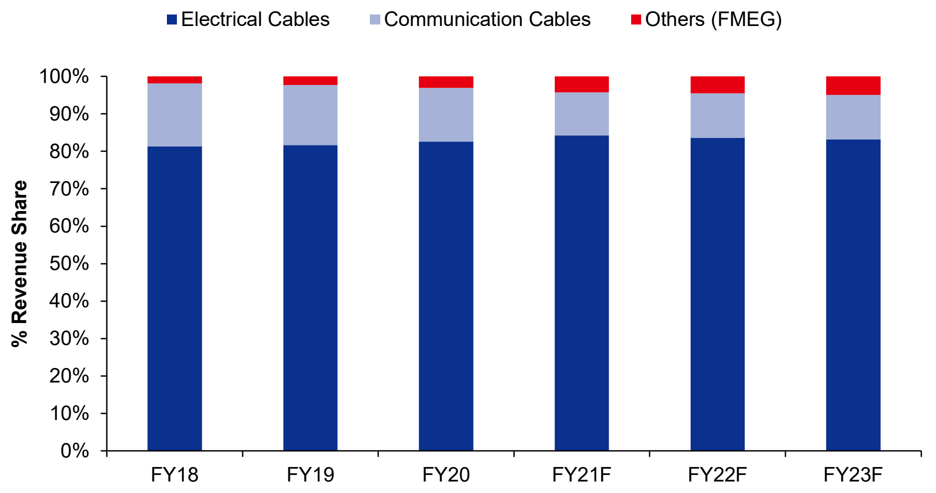
We expect Finolex Cables' consolidated revenue to grow at 13.2% CAGR while Electrical Cable revenue CAGR is estimated at 12.4% over FY21-23F. Communication Cables should see volume and pricing recovery and, hence, we estimate a revenue CAGR of 14.9% over the same period. FMEG should cross the ~Rs1bn revenue mark in FY21F and we expect the segment to grow at a CAGR of 22.5% over FY21-23F.

Figure 201: Finolex Cables – Revenue trend



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 202: Finolex Cables segmental revenue mix



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Effective cost control on the back of in-house manufacturing and backward integration

Consistent product quality – a function of technical expertise and fully-backward integrated manufacturing ➤

Finolex Cables has strongly believed in superior and consistent product quality over the years. The company has entered into technical tie-ups and joint ventures across product categories for technology transfers and maintaining relatively superior product quality vs its peers.

The company owns and operates five manufacturing plants and 28 depots (Mar 2020) to maintain a smooth supply chain and optimum product inventory. It manufactures its key raw materials – PVC compound and copper rods, optic fibre and Fibreglass Epoxy Pultruded (FRP) rods – as part of its backward integration strategy. This helps it to have greater control over its bottom line, secure its raw material supply, maintain high quality, and sell the final products at competitive prices.

"As part of our efforts to strengthen backward integration, we are installing a new line to make tinned copper and foray into instrumentation cables."
– D.K. Chhabria, Executive Chairman, Finolex Cables (Annual Report FY20)

Figure 203: Technical tie-ups (Mar 2020)

Technology Partners	Technology Area
AT&T (Lucent Technologies)	Optic Fibre Cables
Corning, USA	Optic Fibre
NSW, Germany	Winding Wires
Sumitomo, Japan	EHV Power Cables
GE, USA	Compounds
Essex Corp. USA (Superior)	Jelly-Filled Telephone Cables (JFTC) Cables, Copper Rods

SOURCES: EIP RESEARCH, COMPANY REPORTS

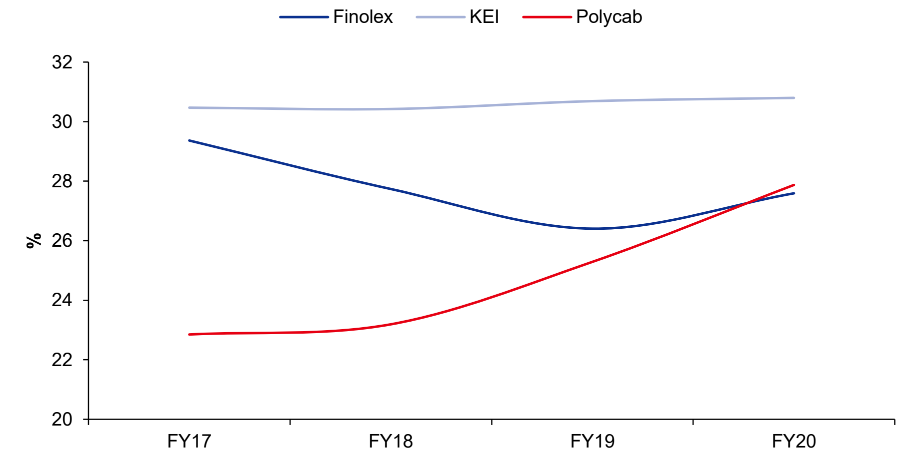
OFC & FMEG segment cyclicality affect C&W margins ➤

Cyclical OFC margin and the loss-making FMEG segment have impacted core cable segment margins for years.

Optimum control over manufacturing operations, inventory management, efficient supply chain and better revenue mix has earned Finolex Cables higher gross margins (28-29%) vs its C&W peers like Polycab and KEI.

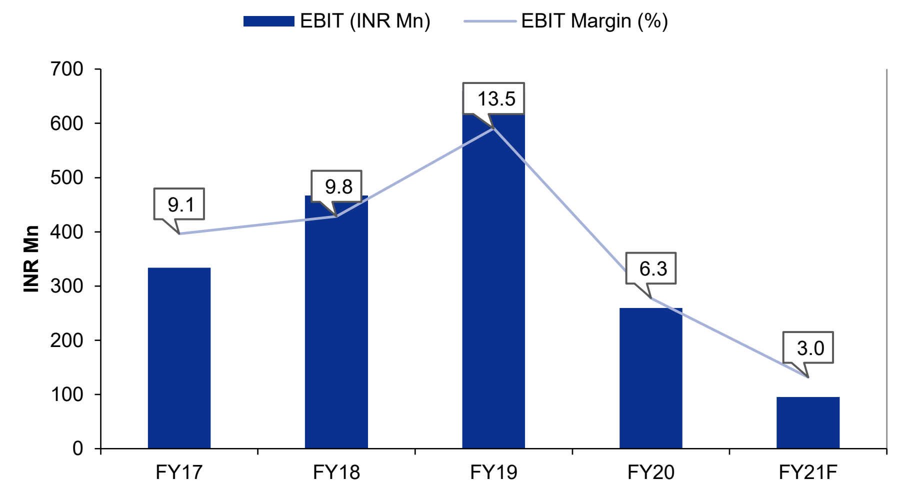
With regards to EBIT margins, C&W segment margins have remained steady at the 15-16% range although consolidated EBIT margins were impacted due to cyclicality in OFC segment margins (global commodity) and the loss-making FMEG segment over FY17-20.

Figure 204: Finolex Cables gross margin vs. KEI and Polycab



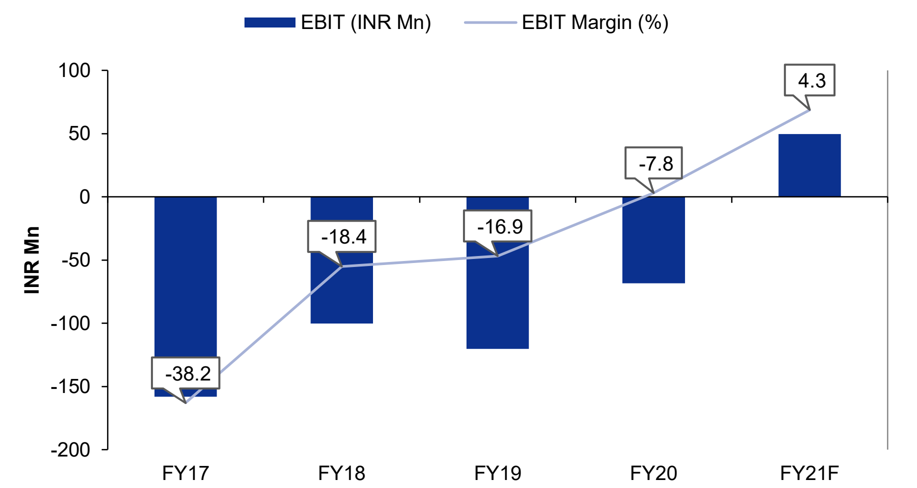
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 205: Finolex Cables' OFC segment EBIT margins are volatile and highly cyclical



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 206: Finolex Cables' EBIT losses in FMEG segment impacted consolidated margins



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Finolex's historical ASP spends in line with C&W peers; higher COVID-19 trade discounts in FY21F to reverse from FY22F

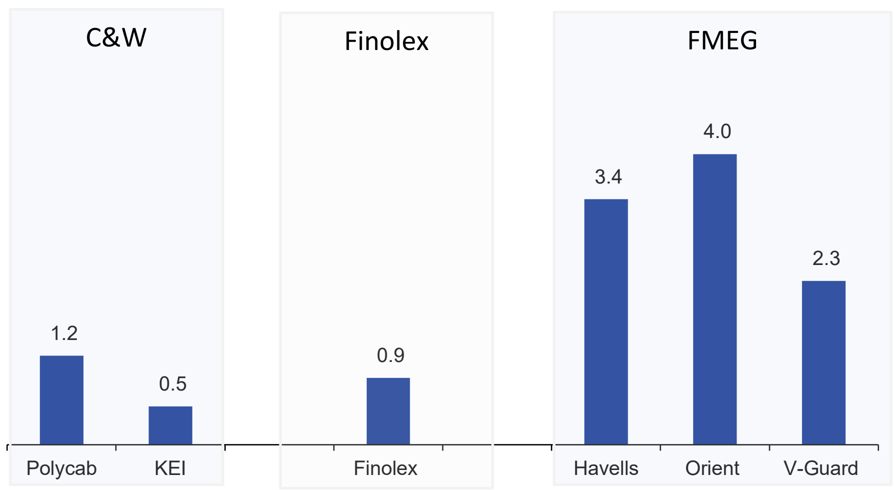
Trade promotions have been maintained at ~6-6.5% of sales over the last few years.

Owing to the extraordinary circumstance of COVID-19, the company passed on the entire reserve amount for trade incentive schemes to dealers in the form of discounted invoice value during 9MFY21. As a result, realisations fell by 150-160bp, impacting gross margins to a similar extent in 9MFY21.

Finolex Cables' management team clarified the change in handling of trade discounts in the 3QFY21 investor call: "So if at 100% achievement, somebody would have gotten 8% incentive in the past and actual performance was that not many people actually met that 100% of their target level. So, at the end, the payout from the company was around 6-6.25%. Whereas this year, we are giving that 8% off directly on the invoice, which means that my realisations are lower by 150bp and 160bp. And that is the reason for the lower gross margins across the board. And this has been a trend right from the first quarter this year."

Finolex Cables' advertising and sales promotion spends (ASPs) is in line with its C&W peers spending of 1-1.5% of FY20 sales annually. Management expects this to increase with the deepening of the FMEG distribution network gradually over the next 3-5 years. FMEG market leaders typically have ASP budget in the range of 2-5% of annual sales.

Figure 207: Finolex Cables' ASP more in line with C&W companies (FY20)



SOURCES: EIP RESEARCH, COMPANY REPORTS

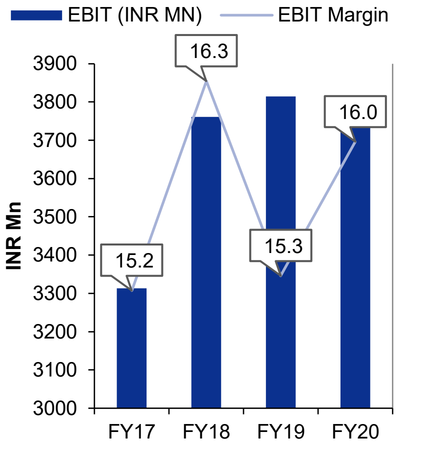
Expect bounceback of consolidated EBITDA margins, we expect OFC and FMEG segment margins to recover

Operating leverage benefits should flow through given higher capacity utilisations.

We expect better optic fibre pricing and higher order flows aiding sales volume growth over FY21-23F. Communication Cable EBIT margins contracted due to lower OFC margins to ~3% in FY21F from a high of 13.5% in FY19. FMEG segment has been loss making and we estimate the EBIT to breakeven in FY21F. We expect EBIT margins to stabilise at 6-9% for OFC and at 6-7.5% for FMEG over FY21-23F.

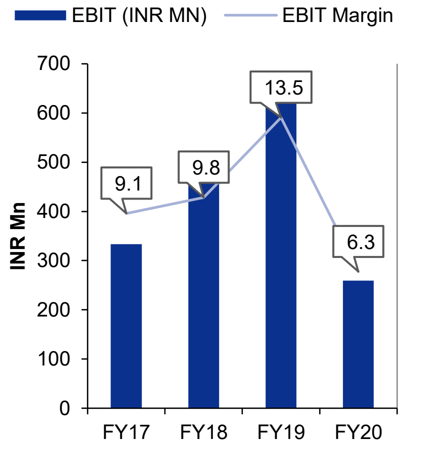
Overall consumer demand recovery should lead to higher capacity utilisation and in turn higher revenue growth for Finolex. In our view, the fixed-cost absorption will be much better on a higher revenue scale and operating leverage benefits should flow in the form of higher EBITDA margins over FY21-23F.

Figure 208: Electrical Cables EBIT & margin trend



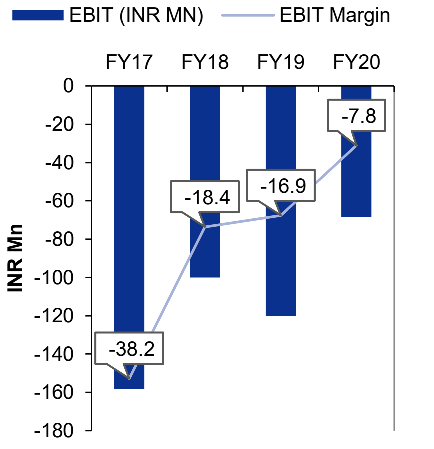
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 209: Communication Cables EBIT & margin trend



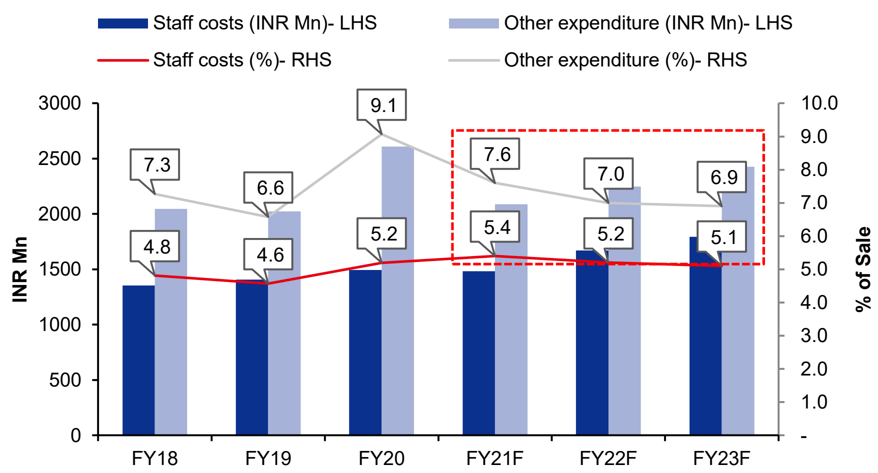
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 210: Others (FMEG) EBIT & margin trend



SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 211: Operating leverage

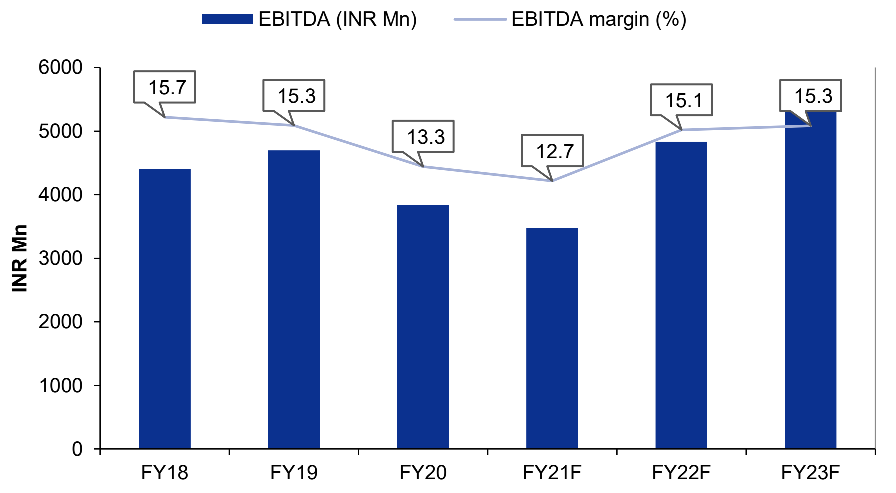


SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

EBITDA performance

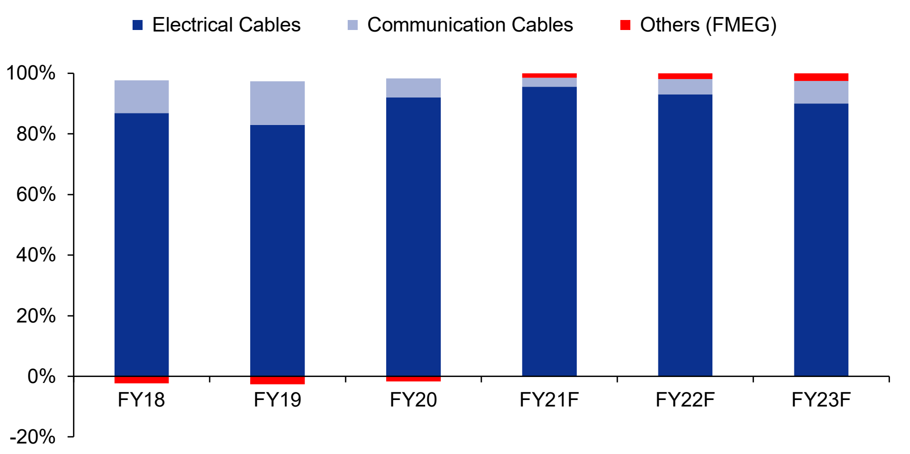
EBITDA de-grew at a CAGR of 6.7% over FY18-20. We expect EBITDA margins to bounce back to 15-15.5% over FY21-23F and EBITDA CAGR of over 24% over the same period. We expect the share of EBIT for communication/FMEG segment to rise from ~5% in FY21 to 10% in FY23F given our assumption of recovery in OFC pricing and higher order inflows from the private/government telcos and EBIT breakeven of FMEG business, respectively.

Figure 212: EBITDA trend



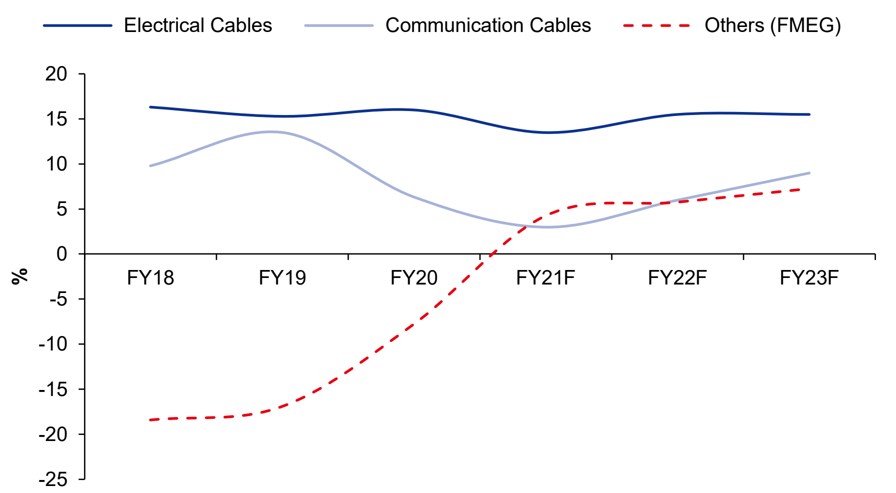
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 213: Segmental EBIT mix



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 214: Segment EBIT margin trend



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Fresh capacities being put up for new product launches, capex for backward integration as well

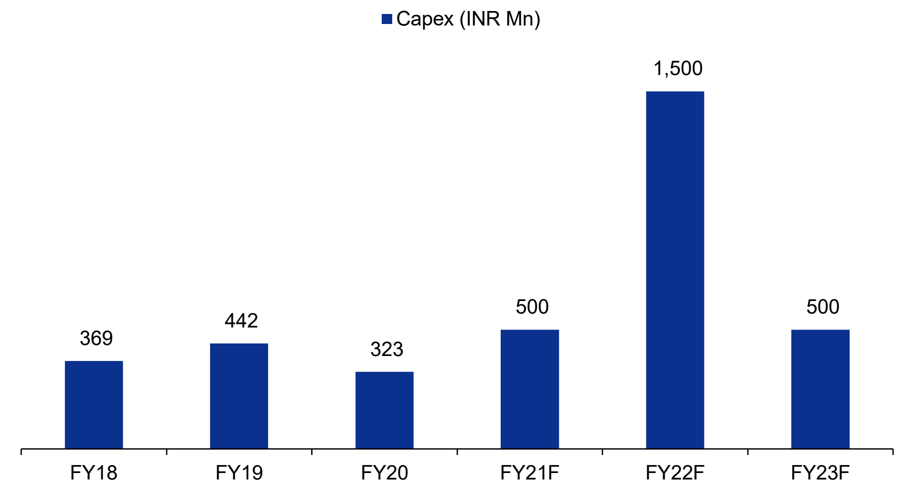
Finolex Cables has announced a capex of Rs2bn to be spent largely over FY21-23F. Of this, the ~Rs400m (revenue potential of Rs500m-750m) conduit pipe plant started operations in Feb 2021. The balance of Rs1.6bn is to be spent on fresh capacity for solar cable manufacturing and allied backward integration (tinned copper plant) and coper clad steel plant for reducing cost of production of power cables.

What are conduit pipes?

Conduit pipe – a Rs15bn market with target market share of 15-20% – implies a Rs3bn annual revenue opportunity for the company.
– 3QFY21 investor call

Conduit pipes are used for pulling wires within construction. The diameter is less than 25mm and these pipes go into the walls through which cables/wires run. There are very limited branded players in this segment and the market has seen recent launches by Polycab and Precision Wires for conduit pipes.

Figure 215: Annual capex plan over FY21-23F (includes Rs2bn of new product capacity and backward integration capex)



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

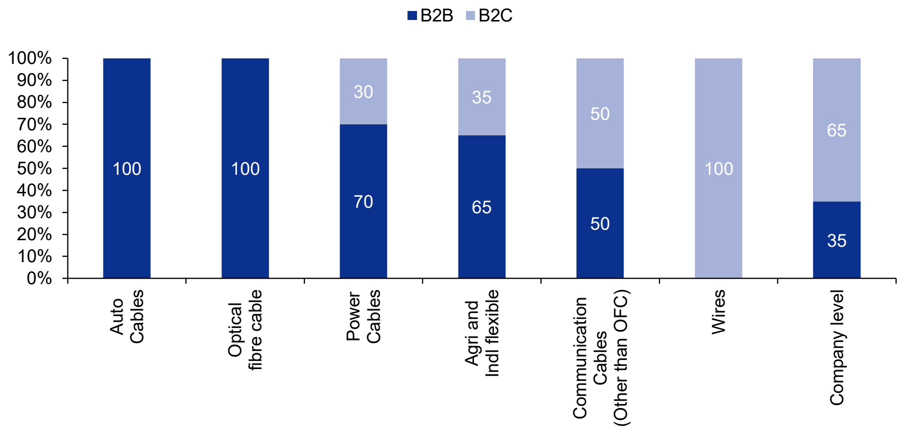
Efficient inventory management, no dependence on imports for finished goods

Finolex Cables' current B2C share is ~65% of overall revenue, in our view.

Finolex Cables follows best practices for inventory management and product quality control enabling it to command higher prices vs most of its C&W peers. Our channel checks reveal that dealer prices are nearly comparable for Havells and Finolex Cables in the housing wire category. The company does almost all the cable and wire manufacturing in-house. While FMEG production is fully outsourced currently, it is entirely sourced from Indian suppliers and there is virtually no import dependence on China/other countries, according to the company.

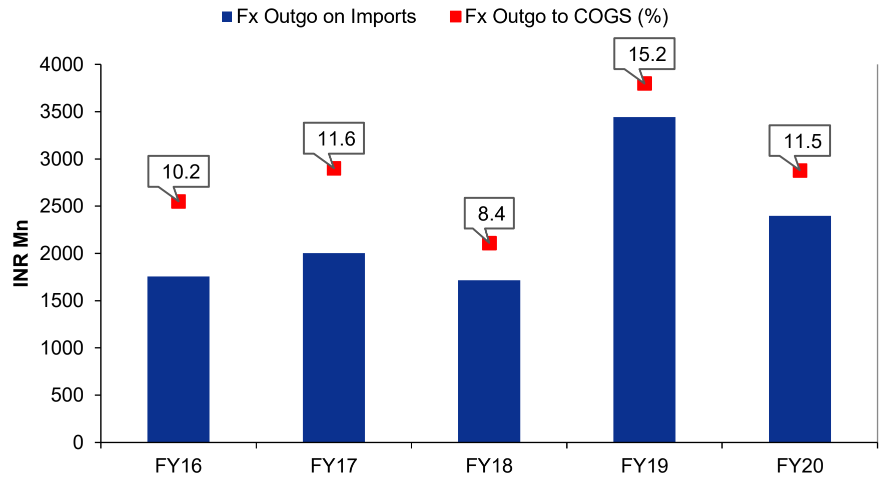
The company does not avail of the vendor financing facility to source raw materials, especially copper, and buys inventory in cash at monthly average prices without taking any copper-related pricing risks. These practices reflect better operating performance at Finolex in terms of higher gross margins and relatively higher pricing power in the C&W product category.

Figure 216: Finolex Cables' current segment-wise B2B/B2C revenue mix



SOURCES: EIP RESEARCH ESTIMATES

Figure 217: Finolex Cables' annual forex outgo



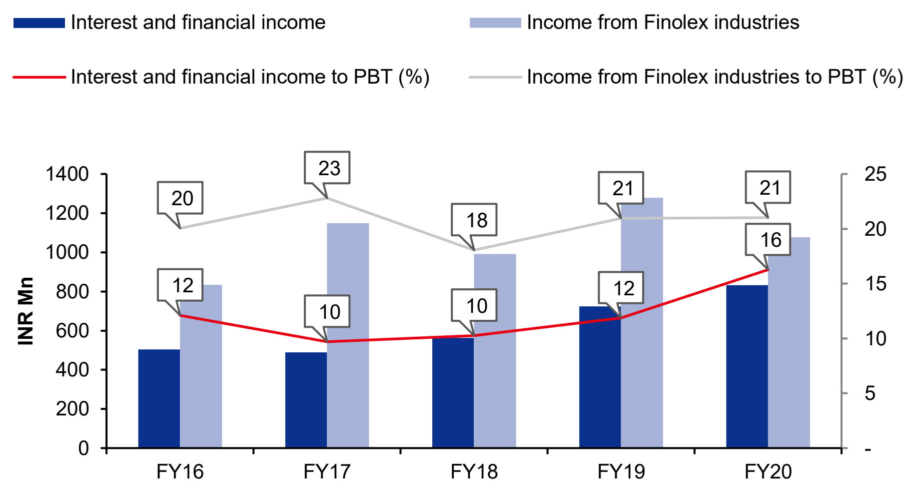
SOURCES: EIP RESEARCH, COMPANY REPORTS

Need clarity on capital allocation policy, treasury and other non-operating income forms over 30% of annual PBT

Clarity on cash utilisation or distribution would help improve return ratios. Dropping treasury yields are not good either.

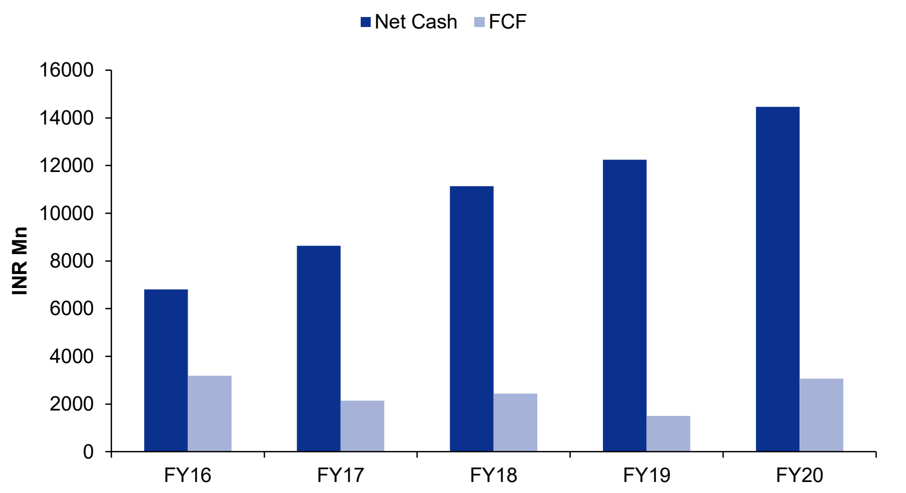
We expect net cash and liquid investments of ~Rs18bn by Mar 2021. Though the company has announced Rs2bn of fresh capex, management continues to explore inorganic opportunities for adjacent product categories or plug geographical gaps in terms of distribution reach in India. Non-core income (other income) is estimated at ~37% of the annual PBT in FY21F. Much of this is due to high surplus cash balances and profit share of the associate company – Finolex Industries (FNXP IN, Not Rated). As of Dec 2020, Finolex Cables held a 32.4% equity stake in Finolex Industries. Media reports (Source: Indian Express, Business Standard, Forbes, Economic Times) have suggested that the promoter family is in a tussle related to inheritance of the company's ownership rights. We believe an amicable settlement with regards to the inheritance issue is important. A clear plan for utilisation of cash would lend much confidence on the company's capital allocation policy to existing and potential equity investors.

Figure 218: Treasury income and associate profit as % to consolidated PBT



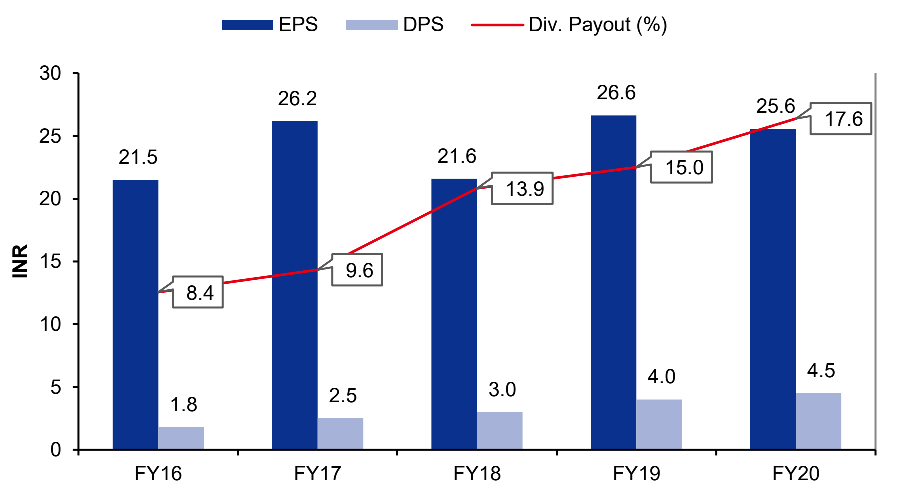
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 219: Net cash and FCF trend: Rs14bn of cash and liquid balances – Mar 2020



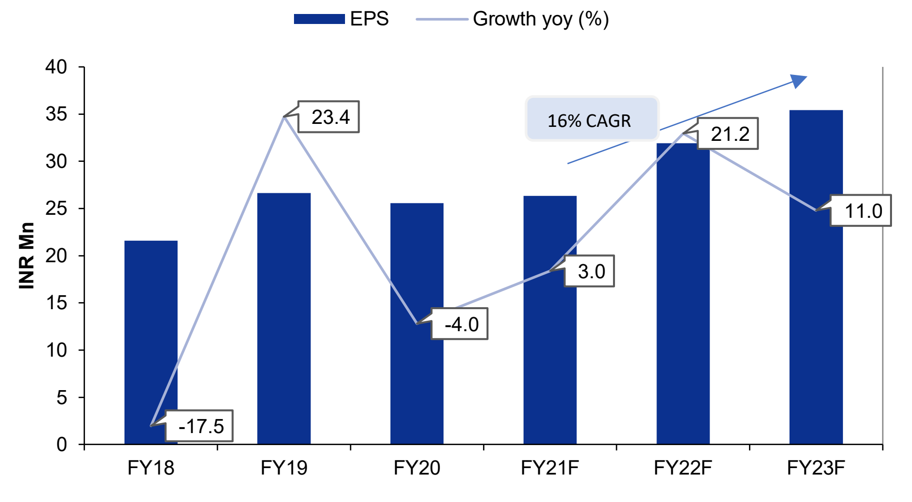
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 220: Distribution of cash through dividend payouts have increased gradually



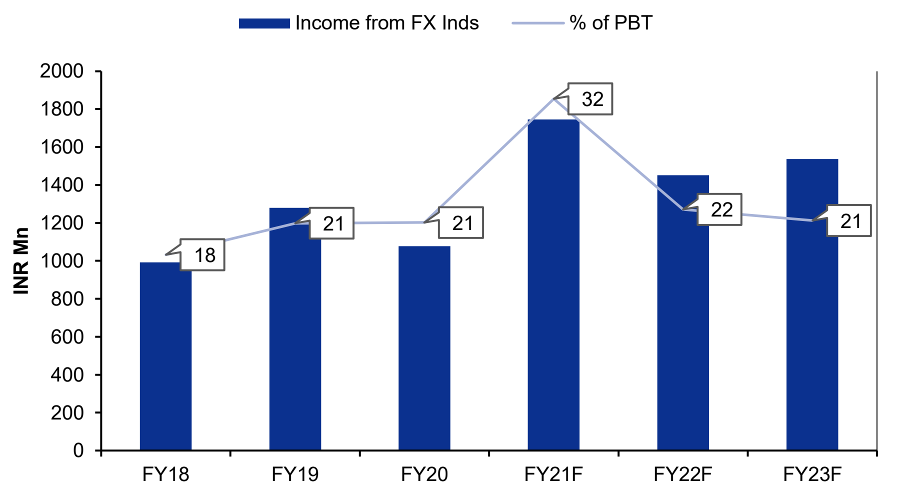
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 221: We estimate EPS CAGR of 16% over FY21-23F



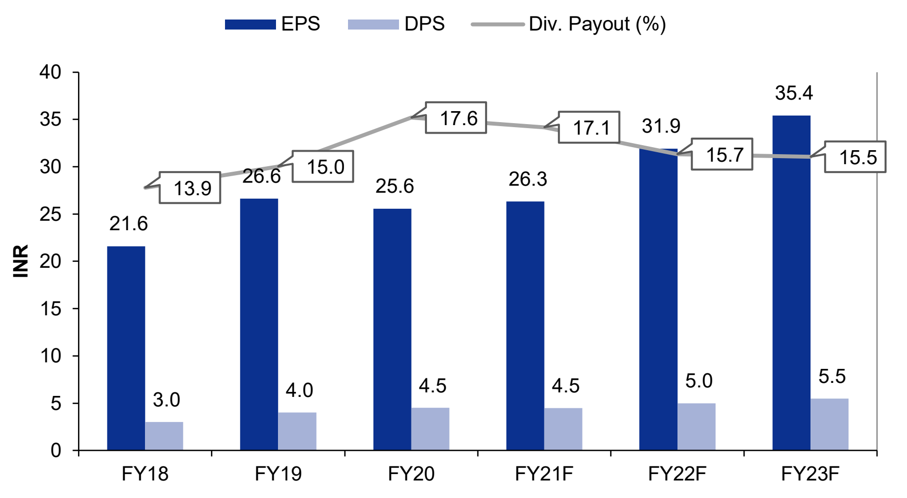
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 222: Finolex Industries share of profit (Bloomberg consensus) is estimated at ~20% of consolidated PBT



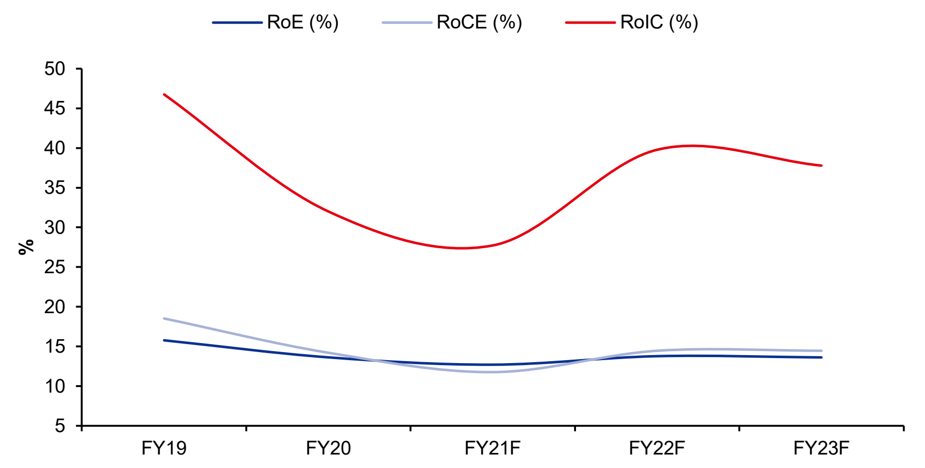
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS, BLOOMBERG

Figure 223: We estimate dividend payouts at past levels over FY21-23F



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 224: Finolex Cables – Relatively low RoE and RoCE due to high surplus cash



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

High intrinsic value; initiate with Add rating

Finolex Cables is an exceptional case in our coverage universe as it is the only company that has lost market share in its core business segment of flexible wires over the past decade. We believe market share lost could also be a result of family inheritance issues between promoter family apart from aggressive competition in the C&W market place. Clarity on company ownership and capital allocation policies are critical for any business to be fairly valued and attract long-term investors in the context of Indian public market investing, in our view.

Owing to legal disputes among the promoter family with regards to ownership rights of the holding company of Finolex Cables – Orbit Electricals – the company's market valuation has been impacted negatively in our view and the stock is now trading attractively at its long-term mean P/E multiples. Slow revenue growth over the past three fiscals, limited scale-up of the FMEG business and no clear decision making on the cash utilisation or its eventual distribution to shareholders are some of the factors responsible for the de-rating of the stock.

Legal suits (National Company Law Tribunal order dated 5 Dec 2018) have been filed by the Chhabria brothers against each other to claim ownership and management control of Finolex Cables. However, we note that there has not been any allegation by either party of any sort of misconduct in day-to-day business operations of Finolex Cables. We think the intrinsic business value should remain unaffected in case of ownership decision is made in favour of either of the parties involved.

Figure 225: Media articles on the family's inheritance issues

SOURCES: EIP RESEARCH, INDIAN EXPRESS, BUSINESS STANDARD, FORBES, ECONOMIC TIMES

We focus on strong franchise value and profit growth

Free cash addition of Rs3.5bn-4bn every year to the existing pile of Rs15bn of cash and liquid investments.

We think the Finolex brand has strong franchise value and high brand recall given its nearly 70 years of market legacy in India. We estimate net profit CAGR of 13.2% over FY21-23F with annual free cash generation of Rs3.5bn-4bn p.a. over this period. We believe the stock price would be driven by net profit and cash flow growth and any clarity on legal ownership of the company would incrementally help remove overhang on the stock.

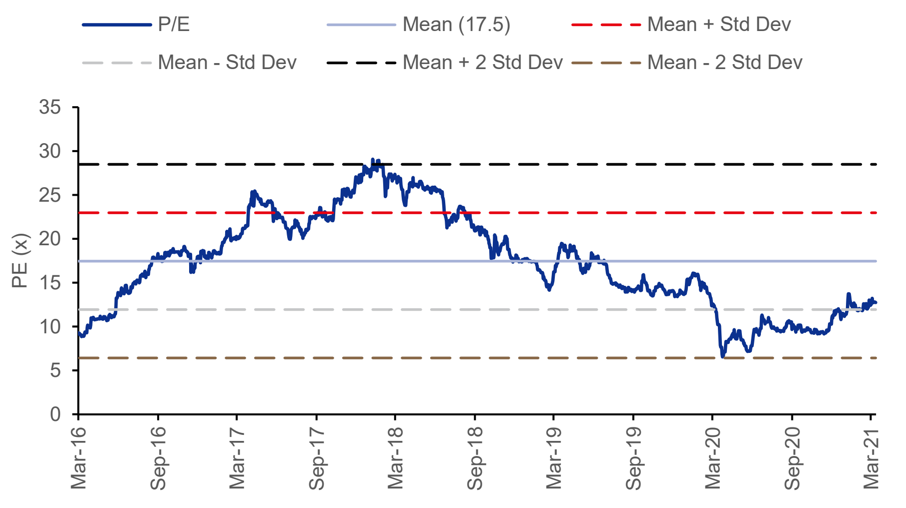
Valuation

An asset like Finolex Cables with great brand recall and pan-India distribution reach is very valuable, in our view.

The stock trades at FY23F P/E of 11.4x and EV/EBITDA of 7x. The long-term 10-year mean P/E has been ~13x. Given our view of demand recovery after a four-year lull in sector demand drivers, robust balance sheet and continuity in healthy cash flow generation, we think the stock is available at compelling valuations and offers an attractive investment opportunity.

We value the stock based on its core profitability (excluding share of profits from associate entity – Finolex Industries) and separately add the value for equity held in the associate entity. We assign an Add rating with a sum-of-parts based target price of Rs504 based on a) Rs382 per share based on 13x FY23F core EPS (in line with its long term ten-year mean P/E and; b) Rs122 per share for 32.4% equity stake in Finolex Industries assuming a 25% haircut to current market cap. Since the share of profits from the associate company account for over 20% of consolidated net profits for Finolex Cables, we think it is better to value the core business independently and add the equity stake valuation to arrive at a consolidated business valuation. Also, given the uncertainty with regards to cash flow distribution of Finolex Industries (given the promoter dispute), we assume a 25% haircut to existing market valuation in our base case assumptions.

Figure 226: Finolex is trading near -1SD its 5 year mean P/E (1 year forward)



SOURCES: EIP RESEARCH, COMPANY REPORTS, BLOOMBERG

Figure 227: P/E band Chart

SOURCES: EIP RESEARCH, COMPANY REPORTS, BLOOMBERG

Downside risks

- **Clarity on company ownership:** The Chhabria promoter family has filed legal suits claiming ownership and management control of Finolex Cables. The matter is sub judice. An amicable family settlement is important for investors to take a long-term view and value the business fairly.
- **Delay in capex execution:** The new plant for solar cables got delayed owing to delay in regulatory and other environment-related clearances. The company has announced a Rs2bn capex plan and execution delays could result in lower-than-estimated revenues for the company.
- **Reversal of demand trends:** Strong revenge-buying trends and related pick-up in the domestic demand for wires/FMEG products has led to recovery in volume growth over Jul-Dec 2020. Reversal of these demand trends could impact our revenue estimates negatively.
- **Capital allocation:** The net cash balance is estimated to be ~Rs18bn by Mar 2021. Management has been exploring M&A options to deploy cash and grow the business. However, any unrelated business diversification could impact investor confidence negatively on capital allocation policies of the company.

Business description and management profile

Finolex Cables was established 1958 and is India's largest and leading manufacturer of electrical and telecommunication cables. The company diversified into the FMEG segment with the aim of becoming a complete electrical products company. It has focussed on manufacturing excellence, innovation and gaining a technological edge. By maintaining the highest standards of quality and service, Finolex Cables has built a strong relationship with institutional and retail customers. Finolex Cables is debt free and has six manufacturing sites and 1,762 employees as of Mar 2020.

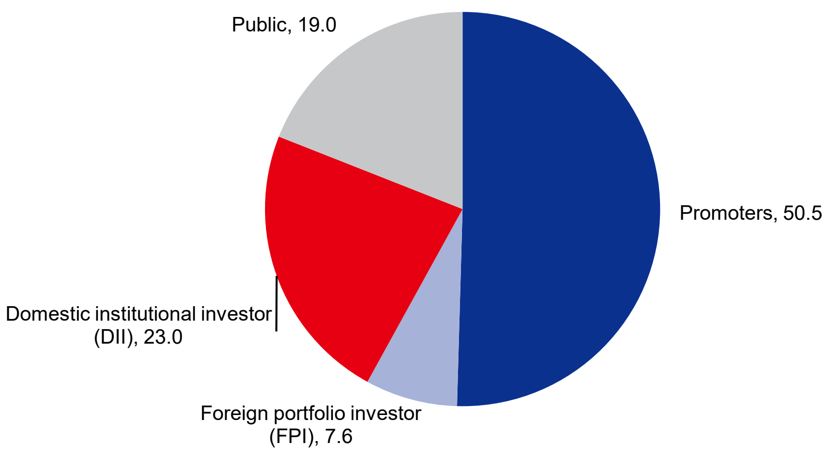
Finolex Cables' board comprises six directors – three independent and three non-independent.

Figure 228: Key management personnel (Mar 2020)

Name and Designation	Profile
Mr D. K. Chhabria Executive Chairman and Promoter Finolex Cables	Mr Deepak K. Chhabria is the Executive Chairman of Finolex Cables Limited. He finished school at Sevenoaks, Kent, England, and then completed his Bachelor of Science in Engineering Management from the University of Evansville, Indiana, USA. Mr Chhabria got his training in 1985 at Bajaj Tempo Ltd, the manufacturer of three- and four-wheeler vehicles. He joined Finolex Cables as Deputy Production Manager in 1986. He became Managing Director in 2001. Mr Chhabria was actively involved in setting up nine manufacturing plants across four locations in India. Under his guidance, the company now produces electrical and communication cable products, copper rods, electrical switches, compact fluorescent lamps, LED lights, MCB and fans.
Mr Mahesh Viswanathan Chief Financial Officer Finolex Cables	Mahesh Viswanathan is the Chief Financial Officer at Finolex Cables. Mr Viswanathan is on the board of Finolex J-Power Systems Pvt Ltd and Corning Finolex Optical Fibre Pvt Ltd.

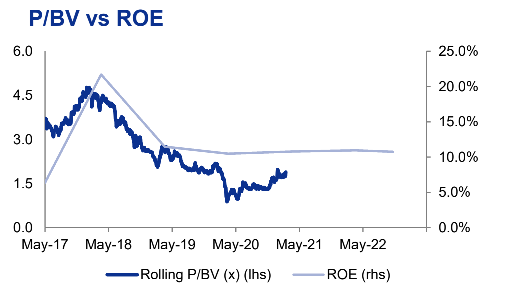
SOURCES: COMPANY WEBSITE, COMPANY REPORTS

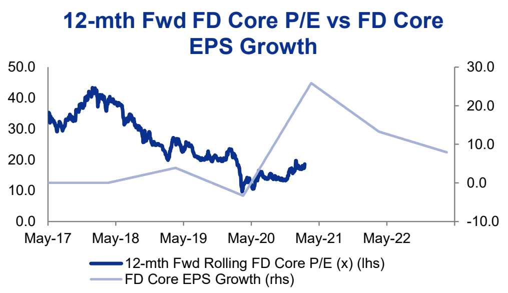
Figure 229: Share Holding Pattern (Dec 2020)



SOURCES: EIP RESEARCH, BSE WEBSITE

BY THE NUMBERS





Profit & Loss

(Rs mn)	Mar-19A	Mar-20A	Mar-21F	Mar-22F	Mar-23F
Total Net Revenues	**30,778**	**28,773**	**27,474**	**32,101**	**35,189**
Gross Profit	**8,129**	**7,940**	**7,047**	**8,748**	**9,589**
Operating EBITDA	**4,697**	**3,835**	**3,475**	**4,831**	**5,366**
Depreciation And Amortisation	(406)	(389)	(391)	(459)	(521)
Operating EBIT	**4,291**	**3,446**	**3,085**	**4,373**	**4,845**
Financial Income/(Expense)	715	817	802	946	1,102
Pretax Income/(Loss) from Assoc.	1,003	776	1,446	1,152	1,237
Non-Operating Income/(Expense)	92	82	50	53	55
Profit Before Tax (pre-EI)	**6,101**	**5,121**	**5,383**	**6,523**	**7,239**
Exceptional Items					
Pre-tax Profit	**6,101**	**5,121**	**5,383**	**6,523**	**7,239**
Taxation	(2,028)	(1,211)	(1,355)	(1,642)	(1,822)
Exceptional Income - post-tax					
Profit After Tax	**4,074**	**3,911**	**4,028**	**4,881**	**5,417**
Minority Interests					
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	**4,074**	**3,911**	**4,028**	**4,881**	**5,417**
Recurring Net Profit	4,074	3,911	4,028	4,881	5,417
Fully Diluted Recurring Net Profit	**4,074**	**3,911**	**4,028**	**4,881**	**5,417**

Cash Flow

(Rs mn)	Mar-19A	Mar-20A	Mar-21F	Mar-22F	Mar-23F
EBITDA	4,697	3,835	3,475	4,831	5,366
Cash Flow from Invt. & Assoc.					
Change In Working Capital	(1,787)	(135)	247	(789)	(677)
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense					
Other Operating Cashflow	285	68	2,298	2,151	2,394
Net Interest (Paid)/Received	(39)	(81)	(802)	(946)	(1,102)
Tax Paid	(1,616)	(1,097)	(1,355)	(1,642)	(1,822)
Cashflow From Operations	**1,541**	**2,590**	**3,864**	**3,605**	**4,160**
Capex	(442)	(323)	(500)	(1,500)	(500)
Disposals Of FAs/subsidiaries	1	6			
Acq. Of Subsidiaries/investments	(1,131)	5,843	(500)	(500)	(500)
Other Investing Cashflow	474	845	810	954	1,109
Cash Flow From Investing	**(1,099)**	**6,370**	**(190)**	**(1,046)**	**109**
Debt Raised/(repaid)	(4)	(23)	(3)		
Proceeds From Issue Of Shares					
Shares Repurchased					
Dividends Paid	(733)	(825)	(688)	(765)	(841)
Preferred Dividends					
Other Financing Cashflow	(9)	(16)	(8)	(8)	(7)
Cash Flow From Financing	**(746)**	**(864)**	**(699)**	**(772)**	**(848)**
Total Cash Generated	(305)	8,096	2,974	1,786	3,420
Free Cashflow To Equity	**437**	**8,937**	**3,671**	**2,558**	**4,269**
Free Cashflow To Firm	**432**	**8,945**	**3,666**	**2,551**	**4,261**

SOURCES: EIP RESEARCH, COMPANY REPORTS

BY THE NUMBERS…cont'd

Balance Sheet

(Rs mn)	Mar-19A	Mar-20A	Mar-21F	Mar-22F	Mar-23F
Total Cash And Equivalents	12,251	14,458	17,933	20,219	24,139
Total Debtors	2,109	1,870	1,882	2,199	2,410
Inventories	5,872	5,931	5,663	6,617	7,253
Total Other Current Assets	772	1,087	1,129	1,319	1,446
Total Current Assets	**21,004**	**23,346**	**26,606**	**30,353**	**35,248**
Fixed Assets	4,035	3,768	4,050	5,091	5,070
Total Investments	5,908	6,089	6,089	6,089	6,089
Intangible Assets	7	5	5	5	5
Total Other Non-Current Assets	588	861	688	688	688
Total Non-current Assets	**10,538**	**10,722**	**10,831**	**11,872**	**11,851**
Short-term Debt					
Current Portion of Long-Term Debt					
Total Creditors	2,083	1,587	1,656	2,199	2,410
Other Current Liabilities	529	802	766	895	981
Total Current Liabilities	**2,612**	**2,389**	**2,422**	**3,093**	**3,391**
Total Long-term Debt	4	3			
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	94	178	178	178	178
Total Non-current Liabilities	**98**	**182**	**178**	**178**	**178**
Total Provisions	1,461	1,460	1,460	1,460	1,460
Total Liabilities	**4,171**	**4,030**	**4,060**	**4,732**	**5,029**
Shareholders Equity	27,371	30,037	33,377	37,494	42,070
Minority Interests					
Total Equity	**27,371**	**30,037**	**33,377**	**37,494**	**42,070**

Key Ratios

	Mar-19A	Mar-20A	Mar-21F	Mar-22F	Mar-23F
Revenue Growth	9.3%	(6.5%)	(4.5%)	16.8%	9.6%
Operating EBITDA Growth	6.5%	(18.3%)	(9.4%)	39.0%	11.1%
Operating EBITDA Margin	15.3%	13.3%	12.6%	15.0%	15.3%
Net Cash Per Share (Rs)	80.08	94.52	117.25	132.19	157.82
BVPS (Rs)	178.98	196.41	218.24	245.14	275.06
Gross Interest Cover	466.43	222.32	385.58	575.34	671.07
Effective Tax Rate	33.2%	23.6%	25.2%	25.2%	25.2%
Net Dividend Payout Ratio	12.1%	16.2%	12.8%	11.7%	11.6%
Accounts Receivables Days	22.88	25.24	24.92	23.20	23.90
Inventory Days	87.53	103.39	103.58	95.96	98.88
Accounts Payables Days	31.08	32.15	28.97	30.12	32.86
ROIC (%)	46.7%	32.0%	27.7%	39.8%	37.8%
ROCE (%)	18.5%	14.2%	11.7%	14.4%	14.4%
Return On Average Assets	18.1%	13.1%	12.8%	14.0%	13.7%

SOURCES: EIP RESEARCH, COMPANY REPORTS

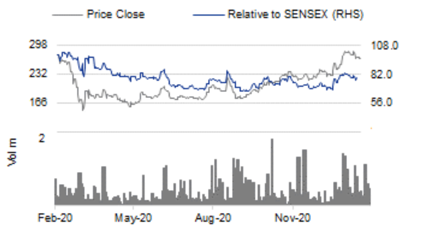
India

ADD *(Initiating coverage)*

Consensus ratings*:	Buy 9	Hold 1	Sell 0

Current price:	Rs295
Target price:	Rs328
Previous target:	N/A
Up/downside:	11.2%
EIP Research / Consensus:	6.3%
Reuters:	ONTE.NS
Bloomberg:	ORIENTEL IN
Market cap:	US$860m
	Rs62,627m
Average daily turnover:	US$1.6m
	Rs114.0m
Current shares o/s:	212.2m
Free float:	61.5%

**Source: Bloomberg*



Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	7.5	33.6	39.8
Relative (%)	9.1	21.3	(1.8)

Major shareholders	% held
Promoters	38.5
NIPPON INDIA NIFTY SMALL CAP	7.5
MIRAE ASSET FOCUSED FUND	2.8

Orient Electric Ltd

Growth driven by consistent innovation

- Focussed innovation drives market share gains over past years across product segments in India
- Cost controls, digitisation and process transformation aids EBITDA margins
- Initiate coverage with Add rating and a TP of Rs 328.

Consistent market share gains for core product categories

Product innovation and new market expansion has driven realisations and volume growth ahead of the market for Orient in core categories of fans and lighting in India over the past three years. Orient is part of the top five Indian brands in terms of fans and lighting category revenues and has continuously grown its core categories, albeit on a large base. Diversification into small domestic appliances like breakfast appliances, induction cooktops, coolers, water heaters, etc, has helped reduce revenue concentration risks in favor of core products. We expect strong growth in the electrical consumer durables (ECD) and the lighting and switchgear segments and estimate overall revenue CAGR of ~15.5% over FY21-23F.

Internal initiatives have led to higher operating margins

Since the executive management change in Dec 2014, Orient has focussed on transforming and digitising operations. Post the demerger in Dec 2017, incremental focus on cutting operating expenses (opex) led to higher EBITDA margins of 8-8.5% despite gross margins losing steam. COVID-19-led cost cuts will lead EBITDA margins to hit a peak of ~10.5% in FY21F, in our view. We expect recovery in opex spends led by advertising (30% of opex) and estimate EBITDA margins of 10.5-11% over FY21-23F.

Efficient working capital management, net cash balance sheet soon

Driven by regular efforts to increase the share of dealer channel financing, Orient has efficiently managed working capital cycles in recent years. Receivables cycle improved 35% to 65 days over FY18-20, while the net working capital (WC) cycle improved to 45-50 days on a steady state basis. Optimum outsourcing mix has kept capex in check at Rs350m-500m/year. Driven by COVID-19-led lower FY21 sales, we expect a meaningful release of working capital to be used for debt repayment and Orient to be a net cash company by Mar 2021. RoE/RoCE would be at 25-35% over FY21-23F.

Initiate with Add rating

The stock trades at P/E of 40.5x and EV/EBITDA of 21.8x. Since its demerger (from Orient Paper and Industries) and independent listing in May 2018, the stock has traded at a mean P/E of ~45x its one-year forward earnings. Given the macro recovery in housing/real estate in urban markets, market share gains, strong management execution history and EPS CAGR of 20.7% over FY21-23F, we value the stock at Rs328 based on 45x FY23F EPS. Downside risks: Delay in new product launches, tough competition in North and West India and raw material price inflation.

Financial Summary	Mar-19A	Mar-20A	Mar-21F	Mar-22F	Mar-23F
Revenue (Rsm)	18,644	20,618	19,328	23,305	25,770
Operating EBITDA (Rsm)	1,413	1,764	2,029	2,435	2,835
Net Profit (Rsm)	693	786	1,061	1,341	1,546
Core EPS (Rs)	3.3	3.7	5.0	6.3	7.3
Core EPS Growth	8.2%	13.4%	34.9%	26.5%	15.2%
FD Core P/E (x)	90.36	79.66	59.05	46.69	40.51
DPS (Rs)	1.0	1.1	1.2	1.2	1.5
Dividend Yield	0.41%	0.46%	0.41%	0.41%	0.51%
EV/EBITDA (x)	45.13	36.04	30.51	25.68	21.86
P/FCFE (x)	126.55	203.15	58.40	(430.13)	55.91
Net Gearing	36.9%	26.4%	(16.1%)	(1.8%)	(10.1%)
P/BV (x)	20.43	17.43	14.23	11.42	9.33
ROE	24.3%	23.6%	26.5%	27.1%	25.3%
% Change In Core EPS Estimates					
EIP Research/Consensus EPS (x)			1.04	0.98	0.91

SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS. PRICED AS AT 12 MAR 2021

Analyst(s)

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Growth driven by consistent innovation

Double-digit revenue growth well supported by market share gains in new products and new geographies

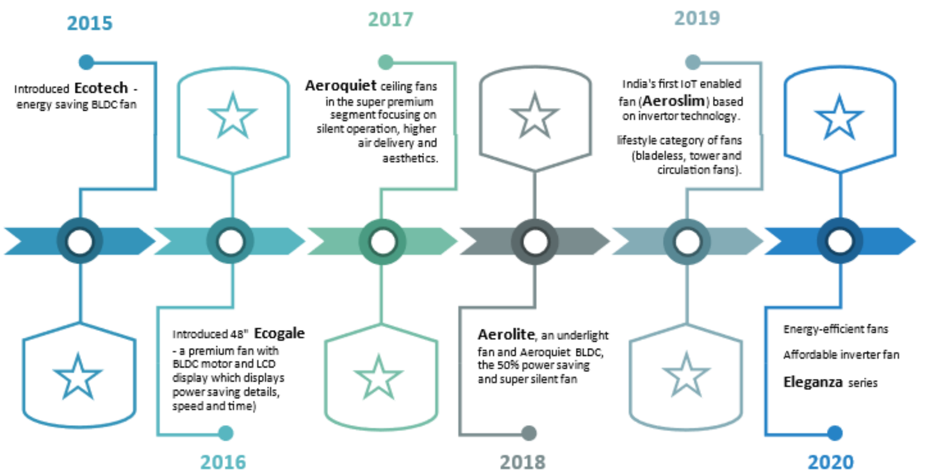
Strong pricing power driven by consistent product innovation and new designs ➤

"The way to our future will not just be about the incremental but increasingly about the radical. We believe that the best way to protect our prospects would be through introduction of disruptive products. These products will not be as much about capturing market share as they would be about creating new markets."
-Mr. C. K. Birla, Chairman
(Source: Corporate Presentation)

- Consistent innovation and timely launch of relevant products has been the key to Orient's success since the change of management (current CEO joined in Dec 2014) and its new independent avatar post the demerger (Dec 2017) from its holding company Orient Paper and Industries.
- Orient gained market share in fans, overall LED lighting and appliances by innovating ahead of time and launching disruptive designs. It is important to recollect that in FY18-20, urban housing/real estate markets were reeling from very low demand and oversupply inventory issues.
- The company has focussed on capturing the changing underlying trend of shorter product life due to ever-increasing replacement demand from aspirational Indian consumers.
- Internal initiatives have led to higher premium product sales and improved per-unit realisations in categories like fans and in appliances like coolers and water heaters.
- Achieved success in the "premium" category (Aero Slim fans – over 40% market share within three years of launch). Now positioning itself as a "mass premium" player – a key success strategy for Havells India.
- New markets: Increasing smartphone usage has improved access to best-in class products via e-commerce. The Hyderabad greenfield expansion facility's ground breaking is expected in 1QFY22 and would start commercial production by Sep 2022.

Here we show Orient's product launch timelines over the years. The company has continuously upgraded and adopted new-age technology to stay relevant in the marketplace, in our view.

Figure 230: Innovation in Fans



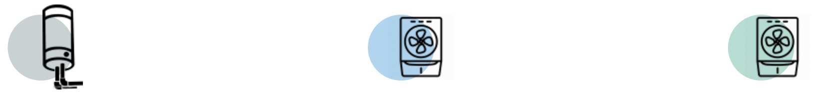
BLDC IS BRUSHLESS DIRECT CURRENT
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 231: Innovation in Lighting

2016	2018	2019	2020
The first Indian brand to receive BEE 3-star rating in 2016 for LED bulbs	Expanded LED lighting portfolio with a new range of LED battens which offer high lumen efficacy	Launched smartphone controlled smart-lamp Awarded 5-Star BEE (Bureau of Energy Efficiency) rating for 9W LED bulbs	Launch of EyeLuv series: Flicker control LED lamp

SOURCES: EIP RESEARCH, COMPANY REPORTS

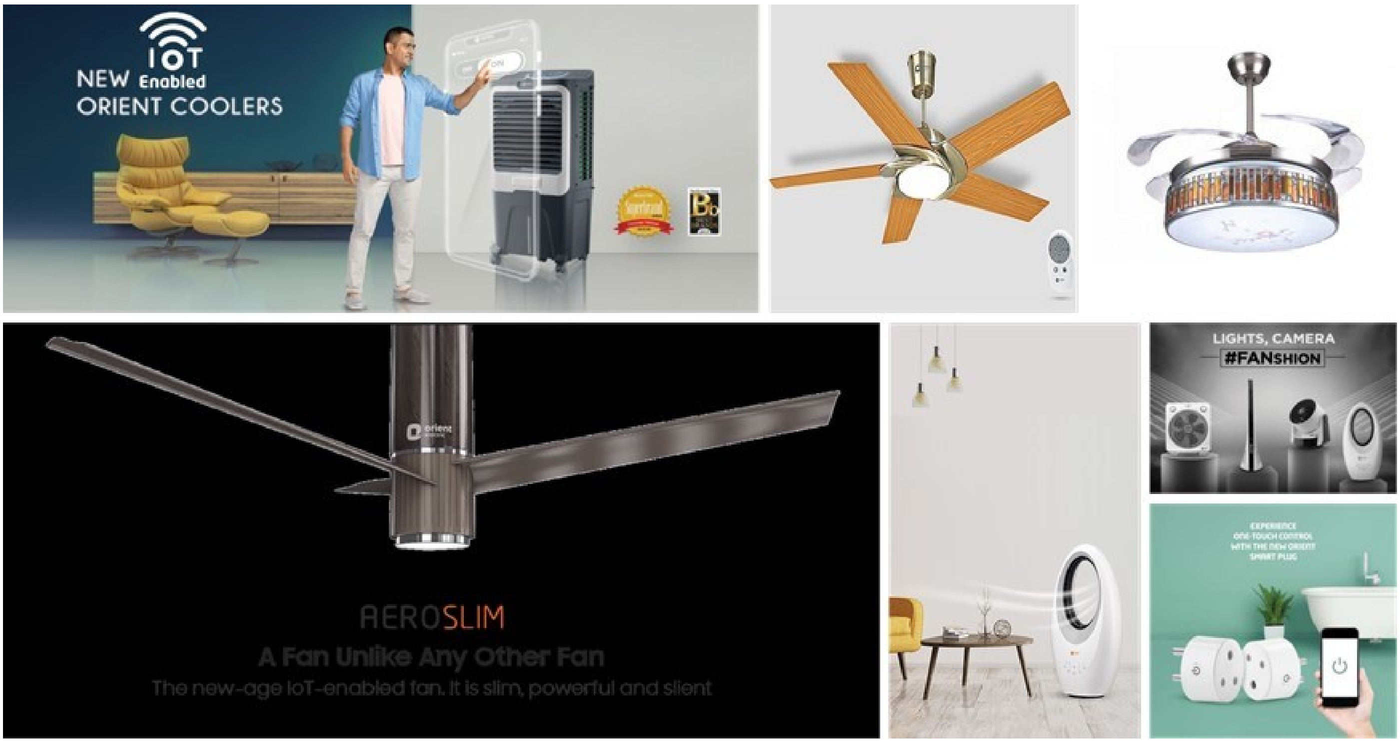
Figure 232: Innovation in Appliances



2018	2019	2020
Launched 18 new models of water heaters	Launched metal bodied, modular outdoor air cooler that can be assembled and dissembled quickly.	Energy-efficient Inverter Coolers

SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 233: New Age Product Portfolio



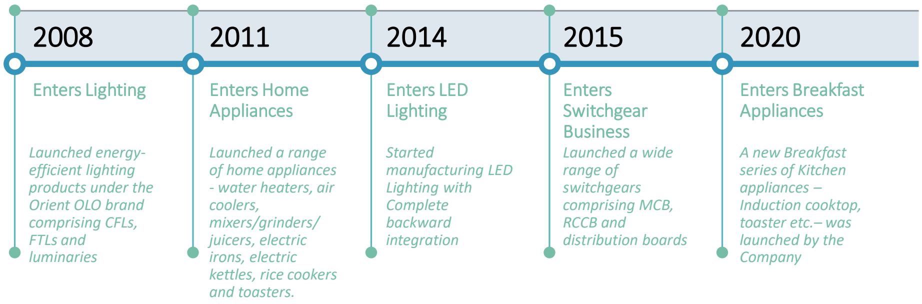
SOURCES: EIP RESEARCH, COMPANY REPORTS

Diversification in new products helping reduce revenue concentration risks

"Our Electrical Consumer Durables segment, largely dominated by summer-relevant products comprising fans and coolers, accounted for 71% of our revenue."
– FY19 annual report

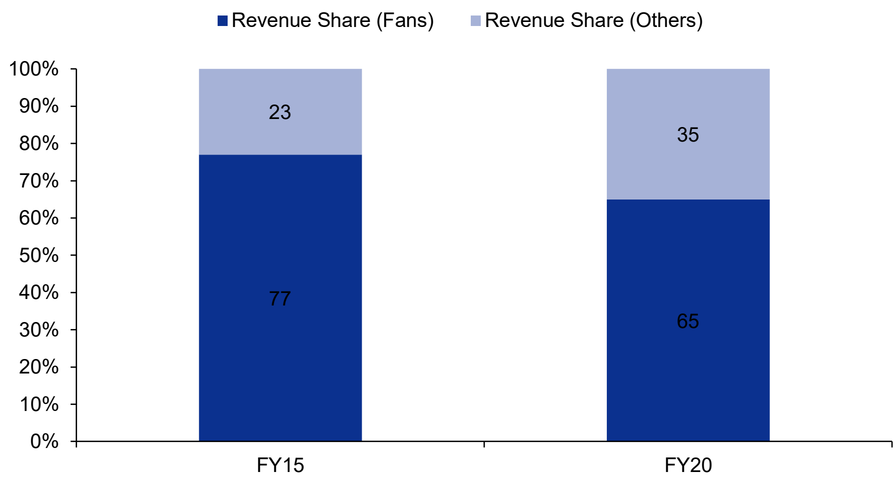
Orient's dependence on the ECD category – mainly fans – has been gradually coming down, improving revenue concentration risks in favour of one large segment. Orient Electric (OEL) embarked on its transformation journey with the start of the lighting business in 2008 and home appliances in 2011. In FY15, it rationalised its appliances portfolio by exiting small appliances and focussing primarily on high-growth products like air coolers, water heaters and mixer grinders. It entered the switchgear segment in 2015 in collaboration with a technology partner – the Slovenia-based ETI Group.

Figure 234: Orient has been adding new categories, aiding revenue growth, and helping reduce concentration of revenue from fans



SOURCES: EIP RESEARCH, COMPANY REPORTS

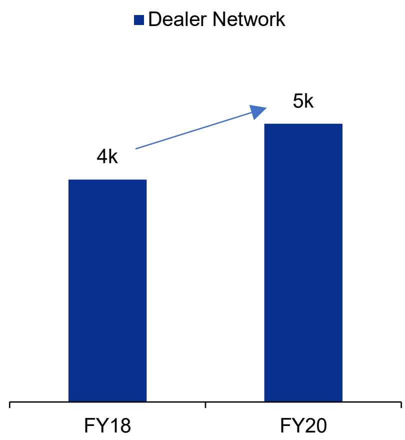
Figure 235: Declining share of revenue from Fans



SOURCES: EIP RESEARCH , COMPANY REPORTS

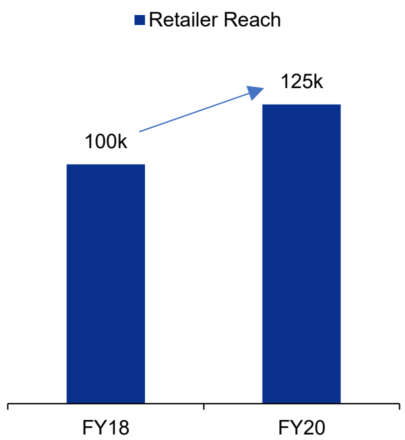
Consistent network expansion is the key enabler for driving growth. Retail Connect programmes are being leveraged to track markets and harness expansion opportunities.
– 3QFY21 Investor Release

Figure 236: Dealer network growth



SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 237: Retailer network growth



SOURCES: EIP RESEARCH, COMPANY REPORTS

Orient Electric Smart Shops serve as exclusive and franchised one-stop shops offering consumers the opportunity to experience and purchase various products of Orient Electric under one roof.

Figure 238: Orient Smart Shop

SOURCES: EIP RESEARCH, COMPANY

Figure 239: Current presence of Orient Smart Shops

State	City
Chattisgarh	Raipur
Haryana	Ballabgarh and Karnal
Karnataka	Bengaluru
Punjab	Chandigarh and Zirakpur
Rajasthan	Jaipur
UP	Kanpur, Moradabad

SOURCES: COMPANY REPORTS, BLOOMBERG

Company's relationship with organised retail partners has grown with the augmentation of brands like De'Longhi in the product portfolio.

Figure 240: Orient Electric to distribute De'Longhi products

SOURCES: EIP RESEARCH, COMPANY

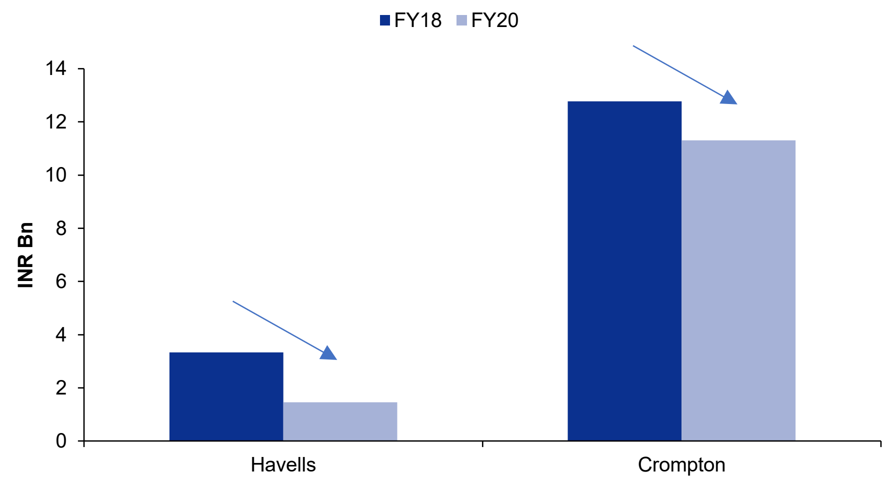
__CSD and B2B:__ Advancing quality enhancement initiatives, OEL introduced ISI-certified ceiling fans in canteen stores department (CSD).

Driving focus on B2B channel through stronger relationships with B2B partners across all verticals propelling growth by ~200%.
– 2019 Annual Report

Core segments of fans and lighting to continue to grow

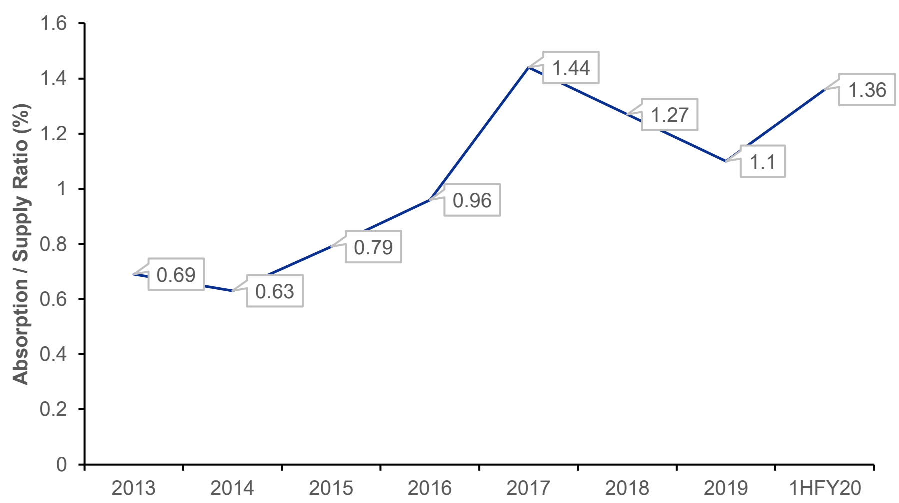
- Orient has been expanding its market share in the LED lighting space in the B2C and B2B segments.
- The company has increased engagement with architects, designers and builders to enhance its share in B2B institutional business, façade lighting and plug distribution gaps in the B2C segment.
- Lighting and switchgear had a revenue CAGR of 18% over FY18-20, with lighting accounting for the majority of revenue.
- Both Havells and Crompton Greaves de-grew their lighting revenue over this period due to LED pricing erosion globally.
- Orient has consistently been within the top three fan brands (Crompton and Havells are the other two brands) in India with an estimated overall revenue market share of 13-14% in the fan category, in our view.
- Historically, the company had a 60% market share (2017 annual report) of fans exported from India. It exports to over 32 countries and barring hiccups in FY19/FY20 due to political unrest in export geographies, we expect the export traction to pick up going forward.
- Given recovery in urban housing/real estate consumption demand over the past year, we expect core revenue segments of fans and lighting to continue to grow at low double digits.

Figure 241: Lighting segment having weathered price erosion in the past is looking at faster growth in future (Lighting Segment revenue for Havells and Crompton)



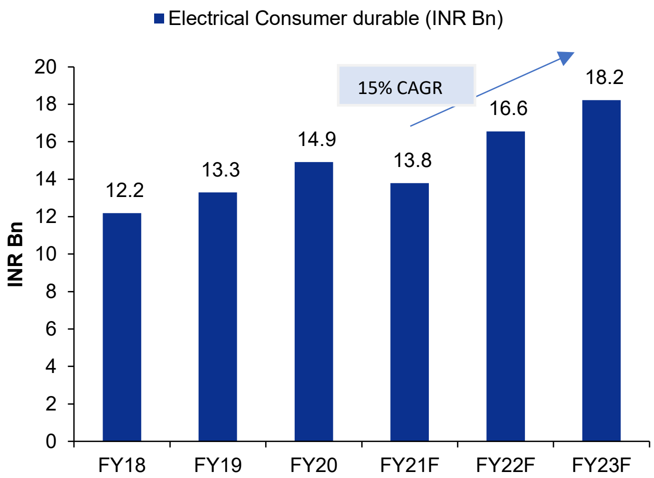
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 242: Absorption to supply ratio (top 7 cities)



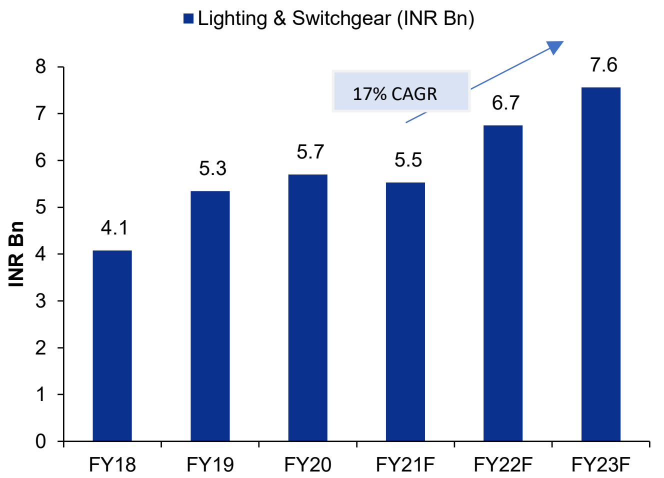
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 243: ECD segment revenue growth



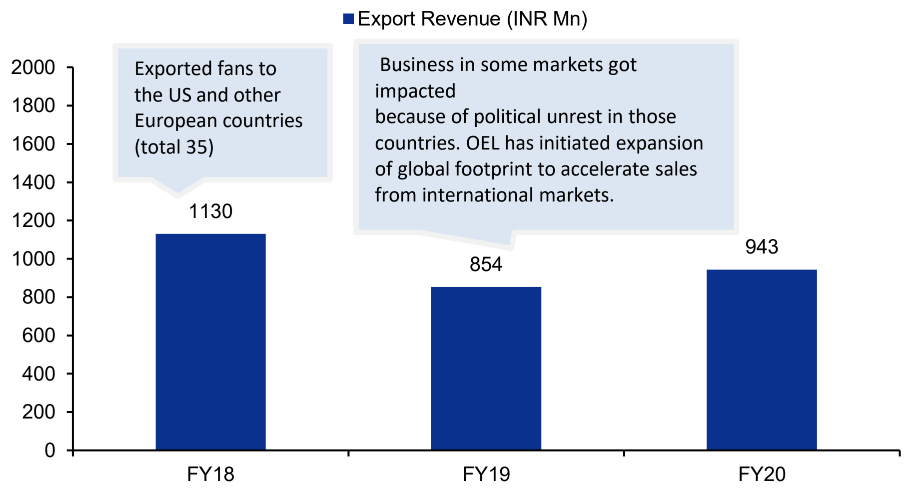
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 244: Lighting segment revenue growth



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

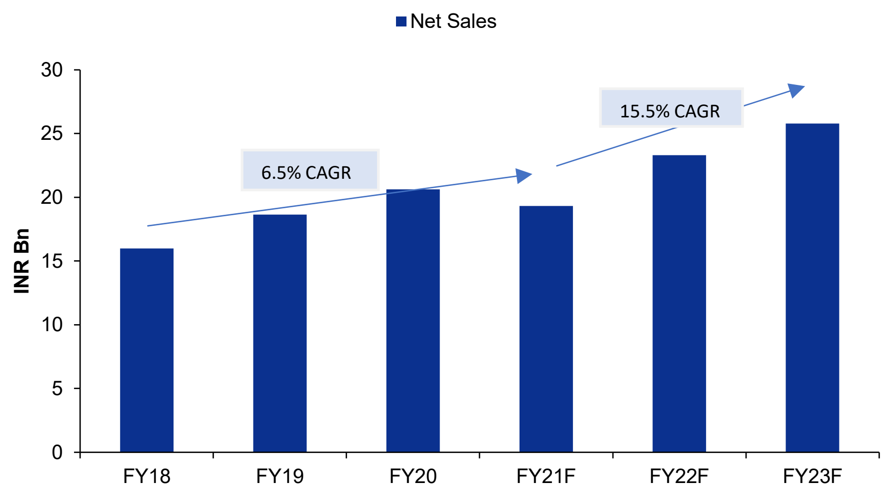
Figure 245: OEL has been one of the leading fan exporters from India



SOURCES: EIP RESEARCH, COMPANY REPORTS

Expect revenue CAGR to be 15.5% over FY21-23F, much higher than past three fiscals

Figure 246: Faster revenue growth expected over FY21-23F



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

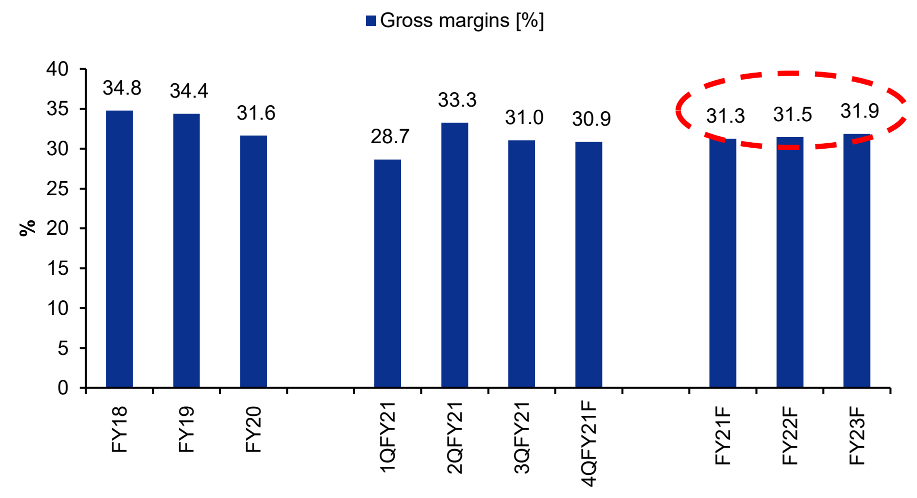
EBITDA margins estimated at 10.5-11% over FY21-23F

Gross margins under pressure due to high input prices

"With steep input cost increases resulting from ongoing commodity trends, gross margin is likely to be under continued pressure."
– 3QFY21 Investor Release

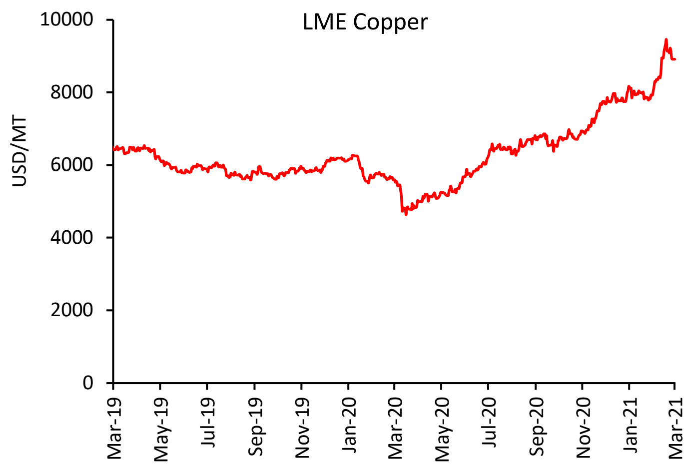
Management has been highlighting raw material price inflation risks since supplies were disrupted globally due to COVID-19 pandemic-induced lockdown. Prices of key raw materials like copper, aluminium and plastic have risen materially. To counter this, Orient has hiked prices across product categories, in line with industry peers, in 3QFY21 and would continue to do so in 4QFY21F to offset gross margin (GM) pressures at least partially. We expect GM to rise marginally by 60bp to 31.9% over FY21-23F.

Figure 247: Gross margins tough to expand till raw material prices cool off



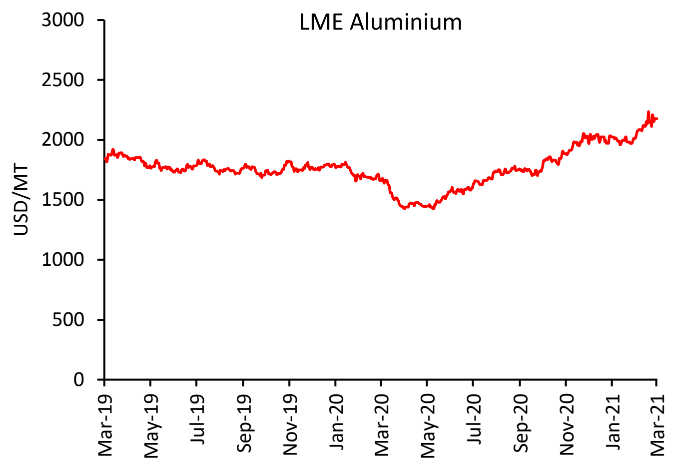
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 248: 24-month copper price trend



SOURCES: EIP RESEARCH, BLOOMBERG

Figure 249: 24-month aluminum price trend



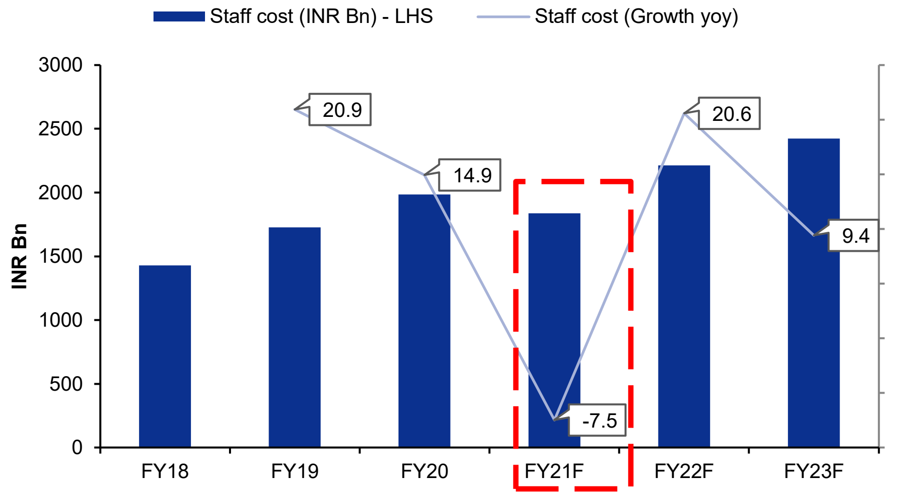
SOURCES: EIP RESEARCH, BLOOMBERG

Low staff costs and other expenditure leads to high EBITDA margins in FY21F

"The company capitalised on the one country one tax GST and consolidated its fans warehouses to just two, reducing stocking area by nearly half, generating savings in logistics cum inventory-carrying costs and improving its response time to market.
– 2018 Annual Report

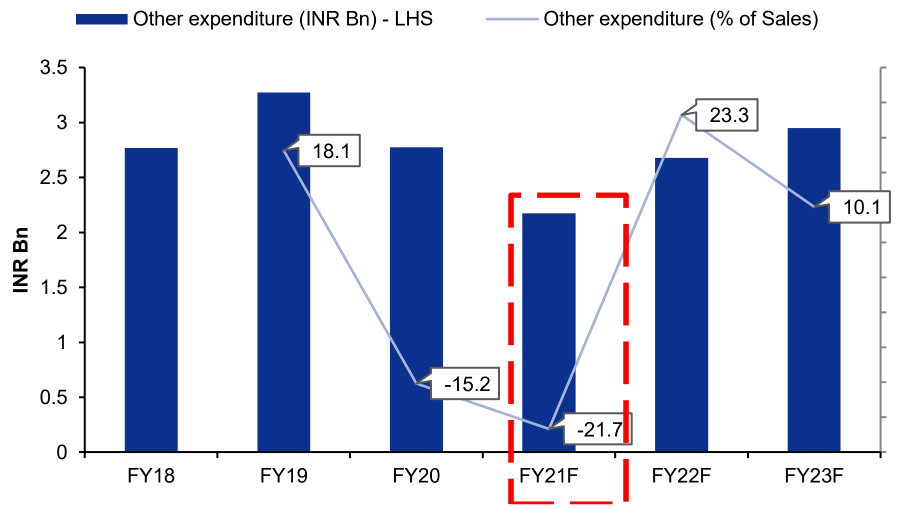
We estimate EBITDA margins to be within the 10-10.5% range over FY21-23F. A significant reduction in operating costs in FY21F led to historical high EBITDA margins of 13-13.5% in 2Q/3QFY21 and we estimate them to cool off going forward.

Figure 250: OEL staff cost expected to decline 7.5% in FY21F



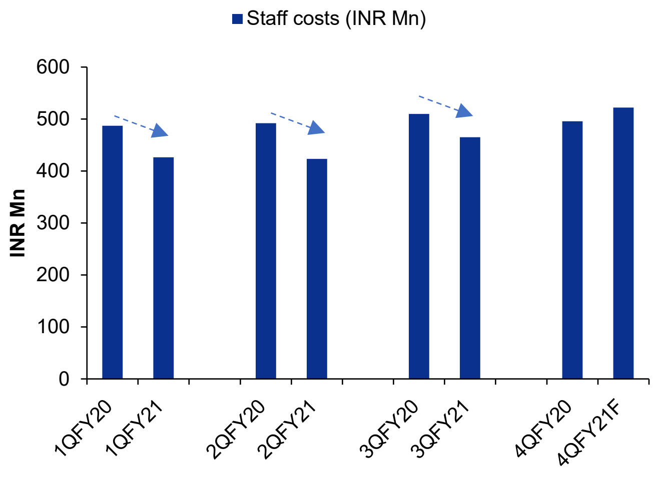
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 251: Significantly lower discretionary spends in FY21



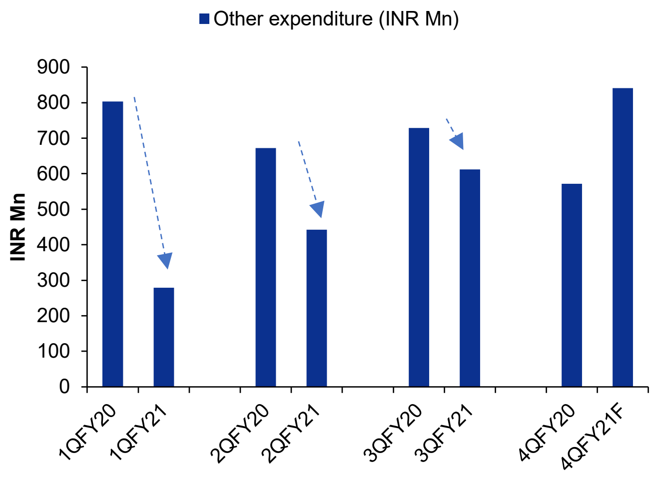
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 252: OEL's FY21 staff cost



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 253: OEL's FY21 other expenditure



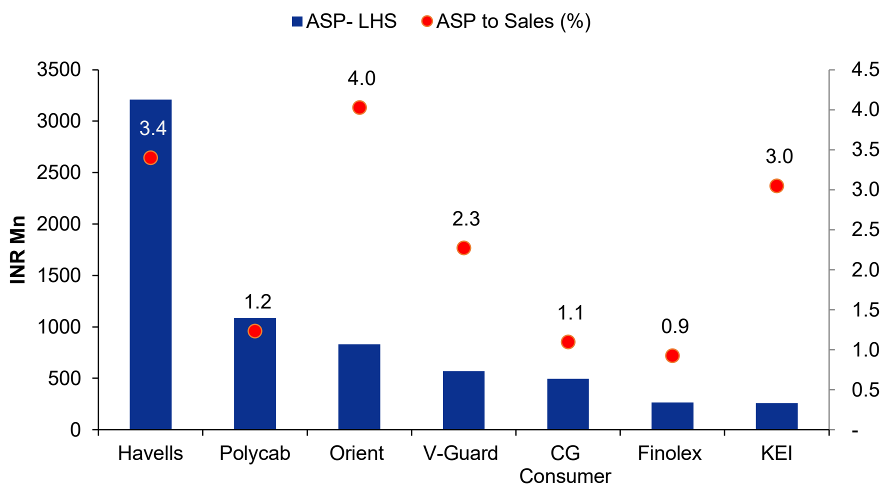
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

A&P spends have been lower this year, will likely return to normalcy

Advertisement and promotion expenses have resumed at last year's levels during the quarter.
- 3QFY21 Investor Release

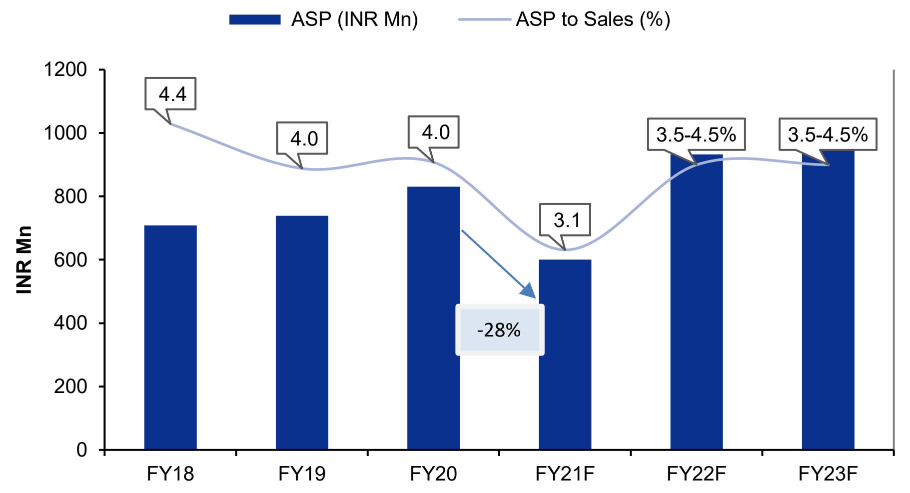
Substantially lower advertisement and promotion (A&P) discretionary expenses helped deliver better EBITDA margins in 9MFY21. With normalcy gradually returning, management expects marketing expenses and brand investments to increase. Orient's advertising and sales promotion budget is within the top quartile of our coverage universe with annual spends at 4-4.5% of sales, which if not spent (in one-off cases like COVID-19 lockdowns) leads to substantially higher operating margins periodically. A&P accounted for 30% of overall other expenditure in FY20.

Figure 254: Brand-building spend (FY20)



SOURCES: EIP RESEARCH, COMPANY REPORTS

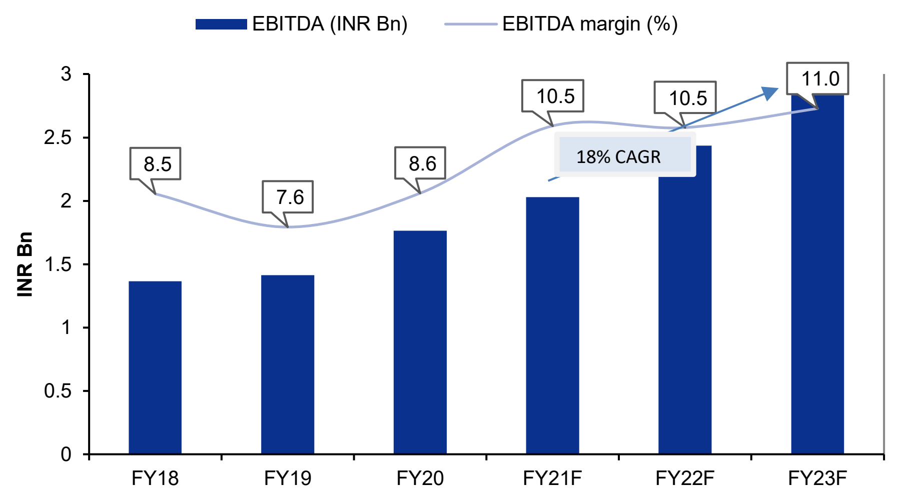
Figure 255: ASP spends have been lower in FY21F, will likely return to normalcy



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Expect EBITDA margins of 10.5-11% over FY21-23F, EBITDA CAGR of 18%

Figure 256: EBITDA and EBITDA margin trend



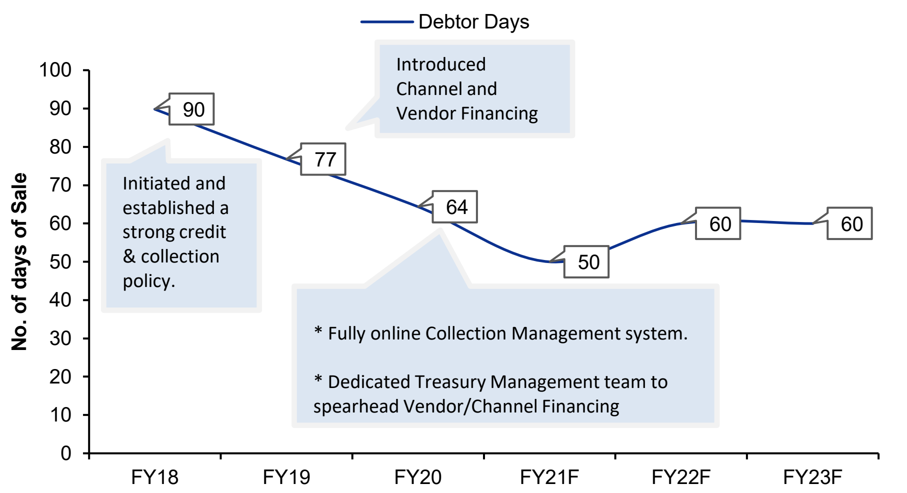
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Net cash balance sheet a function of efficient working management and high return ratios

Significant improvement in receivables management, can improve further

The company strengthened its liquidity by facilitating financing arrangement for channel partners via vendor financing and channel financing routes.
- FY20 Annual Report

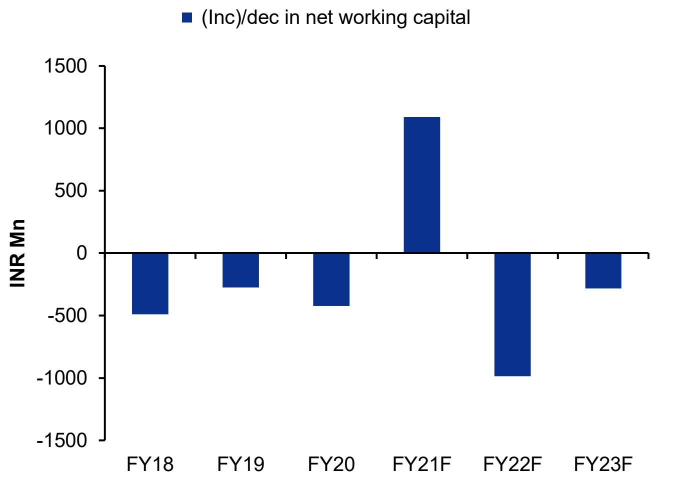
Figure 257: Debtor days



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

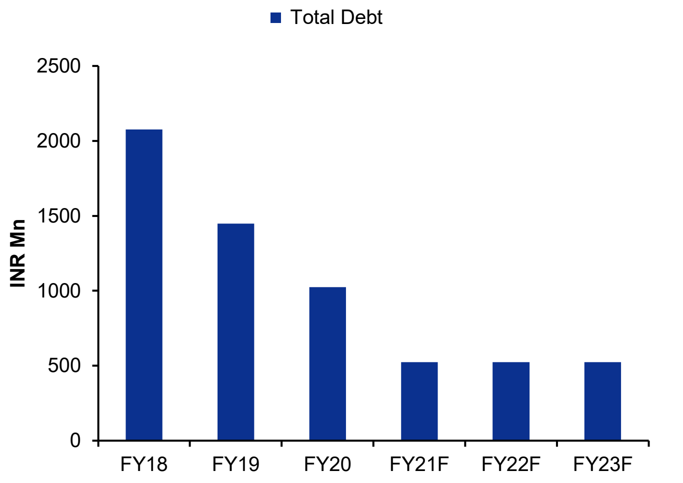
Expect balance sheet to be net cash by Mar 2021

Figure 258: Release of WC due to drop in FY21F revenues



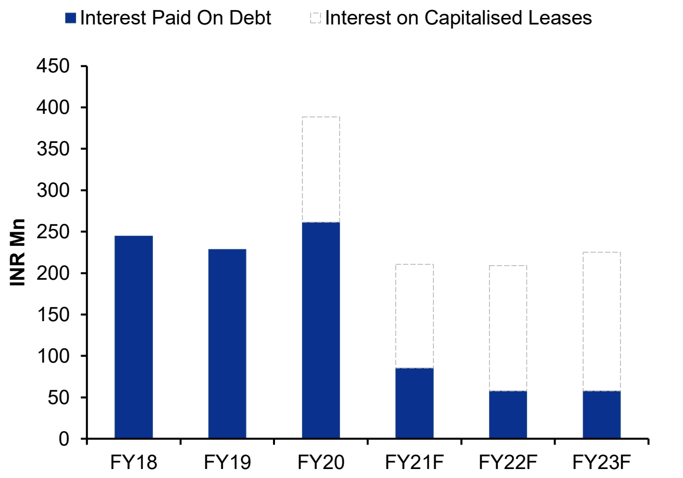
SOURCES: COMPANY REPORTS ESTIMATES, BLOOMBERG

Figure 259: Declining gross debt since FY18



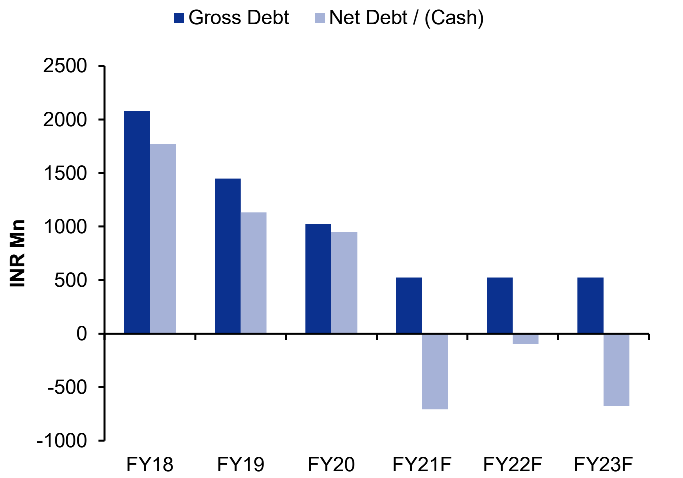
SOURCES: COMPANY REPORTS ESTIMATES, BLOOMBERG

Figure 260: P&L interest costs largely reflect Ind-AS adjustments



SOURCES: EIP RESEARCH ESTIMATES COMPANY REPORTS, BLOOMBERG

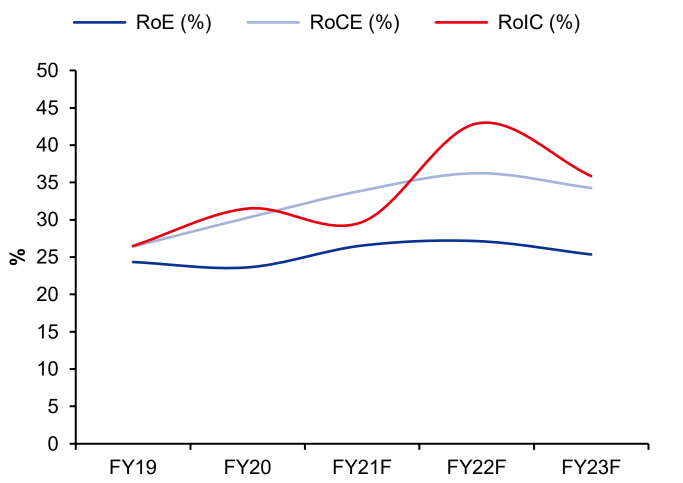
Figure 261: Gross and Net Debt / (Cash)



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS, BLOOMBERG

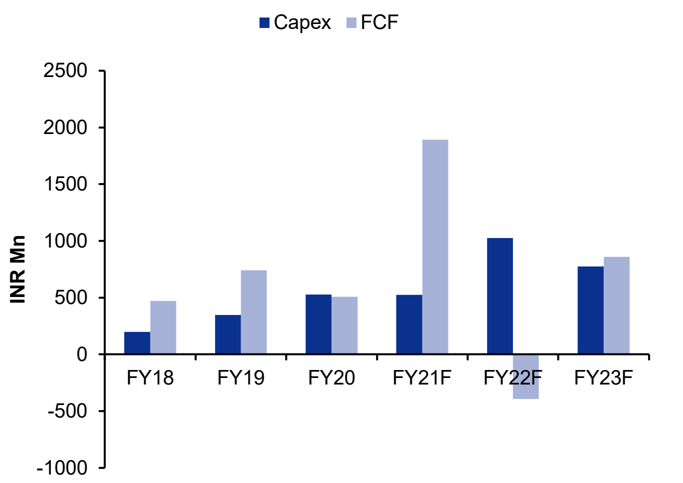
RoE and RoCE to be maintained at ~25-35% aiding free cash generation

Figure 262: Return ratios



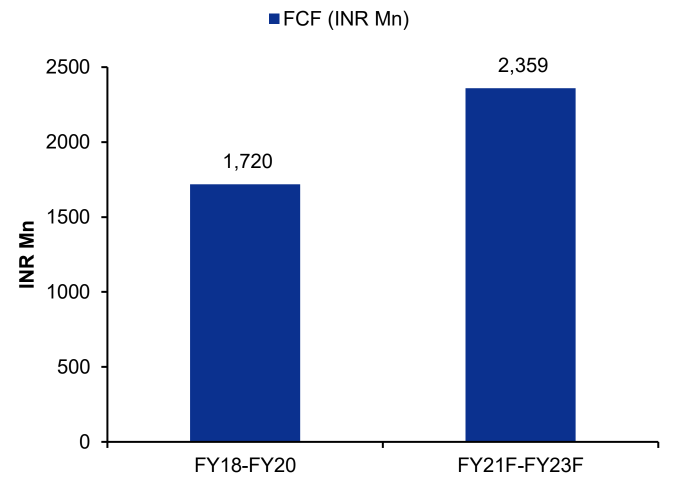
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 263: Capex & FCF trend



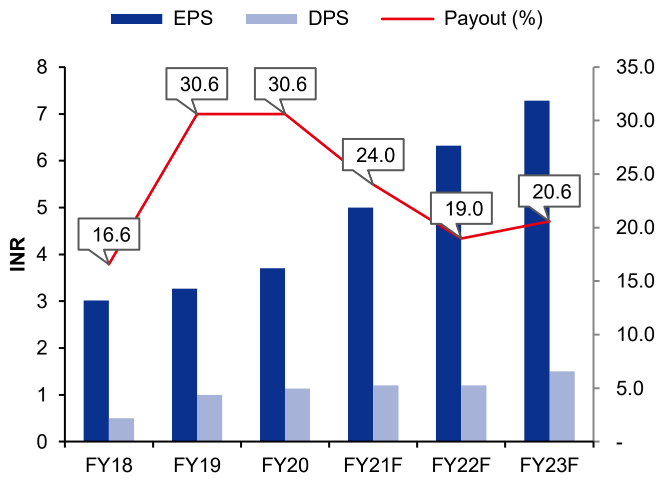
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 264: Cumulative FCF



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

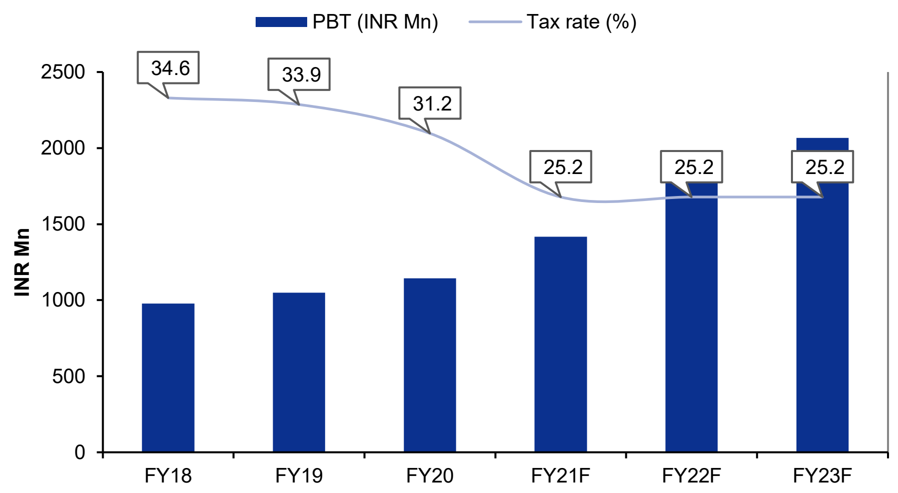
Figure 265: EPS, DPS and % payout



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

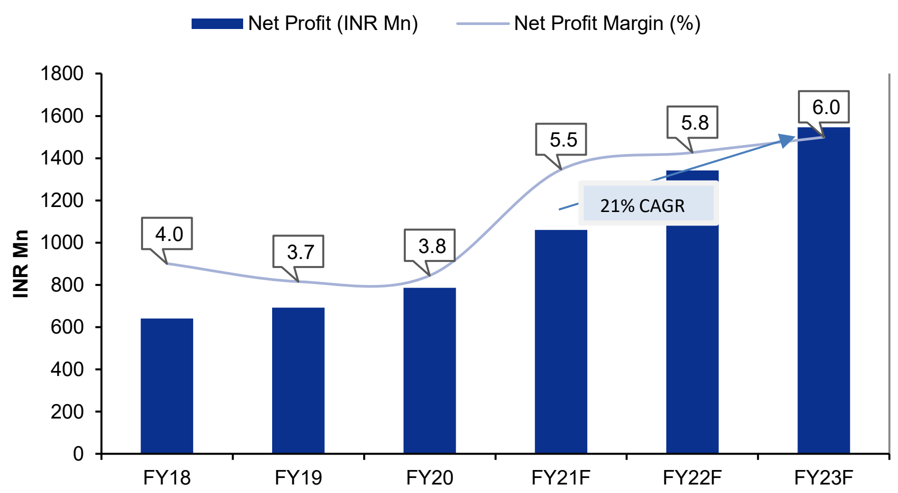
Net profit margins to sustain over 5.5%, EPS CAGR of 21% over FY21-23F

Figure 266: Declining tax rates



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 267: Net profit trend

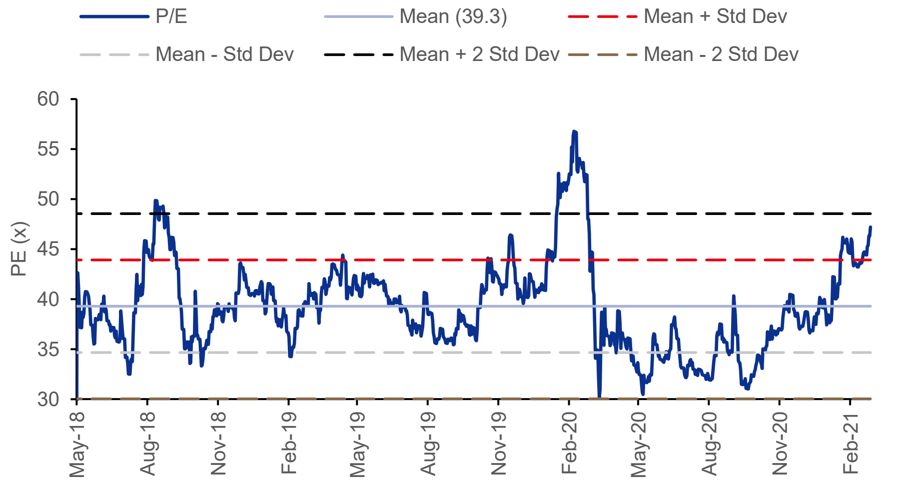


SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Valuation

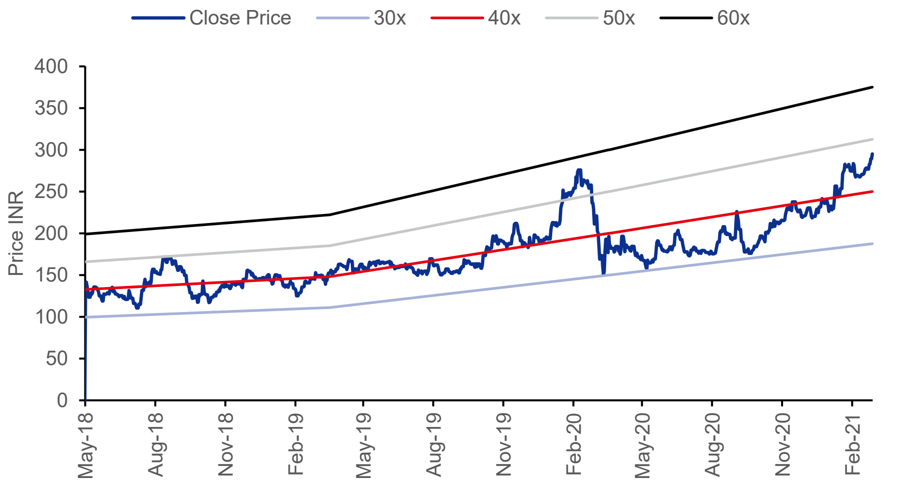
- The stock trades at P/E of 40.5x and EV/EBITDA of 21.9x on our FY23 estimates.
- The stock has traded at a mean P/E of ~45x of its one-year forward earnings since listing in May 2018.
- Coupled with macro demand recovery, we think Orient has delivered on superior execution of its premiumisation plan, gained market share in new products/markets and we estimate healthy EPS CAGR of 20.7% over FY21-23F.
- Given the upcycle expected in sectoral demand drivers, we believe the stock should re-rate to its mean valuation multiples.
- We have a target price of Rs328 based on 45x its FY23F EPS and initiate coverage with an Add rating.

Figure 268: Orient Electric trading close to +2SD its mean P/E since listing (1 year forward)



SOURCES: EIP RESEARCH, COMPANY REPORTS, BLOOMBERG

Figure 269: P/E Band Chart



SOURCES: EIP RESEARCH, COMPANY REPORTS, BLOOMBERG

Downside risks

- **Competition:** Orient has established significant market presence in the fans and lighting categories across India. Launch of new products and entry into new markets will be challenging going forward due to stiff competition from existing strong brands. This could have a material impact on our revenue estimates going forward.
- **Consistent innovation:** Orient has built its brand presence by way of continuous design innovation and launching feature-rich products. We believe it is important for the company to continue to deliver on the same path and any slack could negatively impact its revenue growth profile.
- **Raw material price inflation:** Raw material prices have a reasonable bearing on the profitability of the company. In case of a time lag between pass through of increased RM prices, this could negatively impact our EBITDA estimates for the company.
- **Supply chain risks:** Orient has partially outsourced product manufacturing of domestic appliances. During the COVID-19 lockdown, vendor supplies were lumpy due to transport restrictions. These supply chain risks impact timely fulfillment of demand and negatively impact the brand value and revenue/profit of the company.

Business description and management profile

Orient Electric Limited (OEL) is part of the diversified Indian conglomerate CK Birla Group. A well-known name in the Indian fan industry for more than 60 years, OEL has today established itself in the market as a one-stop brand for lifestyle electrical solutions which include fans, lighting, home appliances and switchgears. A Fortune India 500 company, OEL is focussed on carving out larger market shares, delivering compelling consumer experiences and creating markets niches through differentiated products. The company has fully integrated manufacturing facilities based in Kolkata, Faridabad and Noida. OEL is the largest manufacturer and exporter of fans from India with a presence in over 40 international markets. It is the second largest manufacturer of LED bulbs in India and the first Indian lighting brand to have been awarded a BEE star rating for LED bulbs, according to the company.

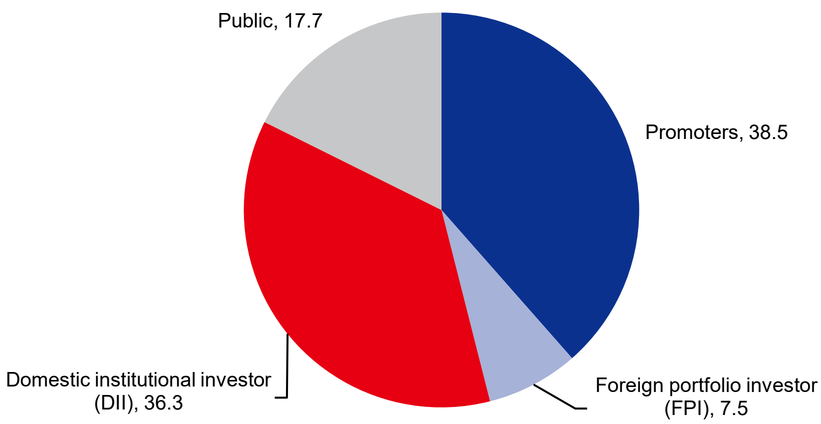
Orient Electric's board has six directors equally distributed between independent and non-independent.

Figure 270: Key management personnel (FY20)

Name and designation	Profile
Chandra Kant Birla, Chairman CK Birla Group	Chandra Kant Birla, 65 years, is the Chairman and Non-Executive Director of the company. He is the chairman of several companies of the CK Birla Group. The group has interests across industries such as automotive, technology, infrastructure, building products, healthcare and education.
Deepak Khetrapal, Vice Chairman CK Birla Group	Desh Deepak Khetrapal, 65 years, holds an Honours degree in Business Economics, a Master of Marketing and Finance from Delhi University and is an alumnus of the Faculty of Management Studies, University of Delhi. He has rich experience in the industrial, consumer and retail businesses. He has a track record of leading and transforming large and diversified organisations across various industries, including services, industrials, consumer and retail businesses.
Rakesh Khanna, Managing Director & CEO Orient Electric Ltd.	Rakesh Khanna, 57 years, holds a Bachelor of Engineering (Mechanical Engineering) from the Thapar Institute of Engineering and Technology and a Master of Management Studies from the University of Mumbai. He has more than 31 years of work experience in India and abroad in the consumer durables, consumer electronics, electrical and lighting sectors. He has worked with Jumbo Electronics, Hitachi Home & Life Solutions and Wipro.
Saibal Sengupta, Chief Financial Officer Orient Electric Ltd.	Saibal Sengupta is Chief Financial Officer of Orient Electric Ltd. Mr. Sengupta is also a member of The Institute of Chartered Accountants of India. He was previously the Chief Financial Officer of Usha International Ltd, and worked with Dabur India.

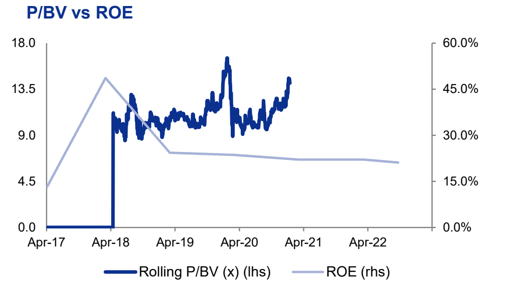
SOURCES: EIP RESEARCH, COMPANY WEBSITE, COMPANY REPORTS

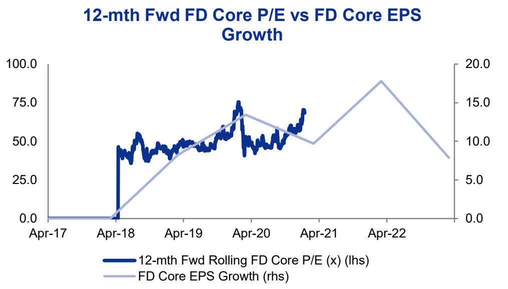
Figure 271: Share Holding Pattern (Dec 2020)



SOURCES: EIP RESEARCH, BSE WEBSITE

BY THE NUMBERS





Profit & Loss

(Rs mn)	Mar-19A	Mar-20A	Mar-21F	Mar-22F	Mar-23F
Total Net Revenues	**18,644**	**20,618**	**19,328**	**23,305**	**25,770**
Gross Profit	**6,412**	**6,525**	**6,040**	**7,329**	**8,208**
Operating EBITDA	**1,413**	**1,764**	**2,029**	**2,435**	**2,835**
Depreciation And Amortisation	(231)	(401)	(431)	(491)	(601)
Operating EBIT	**1,182**	**1,363**	**1,598**	**1,945**	**2,233**
Financial Income/(Expense)	(193)	(242)	(191)	(172)	(189)
Pretax Income/(Loss) from Assoc.					
Non-Operating Income/(Expense)	60	22	10	20	21
Profit Before Tax (pre-EI)	**1,049**	**1,143**	**1,417**	**1,793**	**2,066**
Exceptional Items					
Pre-tax Profit	**1,049**	**1,143**	**1,417**	**1,793**	**2,066**
Taxation	(356)	(357)	(357)	(451)	(520)
Exceptional Income - post-tax					
Profit After Tax	**693**	**786**	**1,061**	**1,341**	**1,546**
Minority Interests					
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	**693**	**786**	**1,061**	**1,341**	**1,546**
Recurring Net Profit	693	786	1,061	1,341	1,546
Fully Diluted Recurring Net Profit	**693**	**786**	**1,061**	**1,341**	**1,546**

Cash Flow

(Rs mn)	Mar-19A	Mar-20A	Mar-21F	Mar-22F	Mar-23F
EBITDA	1,413	1,764	2,029	2,435	2,835
Cash Flow from Invt. & Assoc.					
Change In Working Capital	(276)	(423)	1,090	(987)	(284)
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense					
Other Operating Cashflow	286	189	(326)	(327)	(361)
Net Interest (Paid)/Received	199	244	191	172	189
Tax Paid	(301)	(482)	(357)	(451)	(520)
Cashflow From Operations	**1,320**	**1,292**	**2,628**	**842**	**1,859**
Capex	(348)	(526)	(525)	(1,025)	(775)
Disposals Of FAs/subsidiaries	4	5			
Acq. Of Subsidiaries/investments	3	(4)	(550)		
Other Investing Cashflow	30	17	20	37	36
Cash Flow From Investing	**(312)**	**(508)**	**(1,055)**	**(988)**	**(739)**
Debt Raised/(repaid)	(513)	(476)	(500)		
Proceeds From Issue Of Shares					
Shares Repurchased					
Dividends Paid	(256)	(294)	(255)	(255)	(318)
Preferred Dividends					
Other Financing Cashflow	(229)	(259)	(211)	(209)	(225)
Cash Flow From Financing	**(998)**	**(1,029)**	**(965)**	**(464)**	**(543)**
Total Cash Generated	10	(245)	607	(609)	577
Free Cashflow To Equity	**495**	**308**	**1,072**	**(146)**	**1,120**
Free Cashflow To Firm	**779**	**523**	**1,362**	**(355)**	**895**

SOURCES: EIP RESEARCH, COMPANY REPORTS

BY THE NUMBERS…cont'd

Balance Sheet

(Rs mn)	Mar-19A	Mar-20A	Mar-21F	Mar-22F	Mar-23F
Total Cash And Equivalents	316	75	1,232	623	1,199
Total Debtors	3,924	3,637	2,648	3,831	4,236
Inventories	2,640	2,865	2,648	3,192	3,530
Total Other Current Assets	357	427	530	638	706
Total Current Assets	**7,237**	**7,004**	**7,057**	**8,284**	**9,672**
Fixed Assets	1,166	1,358	1,490	1,399	2,666
Total Investments					
Intangible Assets					
Total Other Non-Current Assets	486	1,243	1,350	2,150	1,250
Total Non-current Assets	**1,651**	**2,601**	**2,840**	**3,549**	**3,916**
Short-term Debt	999	947	484	484	484
Current Portion of Long-Term Debt					
Total Creditors	3,509	3,305	3,177	3,831	4,236
Other Current Liabilities	735	840	953	1,149	1,271
Total Current Liabilities	**5,243**	**5,091**	**4,615**	**5,464**	**5,991**
Total Long-term Debt	449	76	39	39	39
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	129	843	843	843	843
Total Non-current Liabilities	**579**	**919**	**882**	**882**	**882**
Total Provisions					
Total Liabilities	**5,822**	**6,011**	**5,497**	**6,346**	**6,873**
Shareholders Equity	3,066	3,594	4,400	5,487	6,714
Minority Interests					
Total Equity	**3,066**	**3,594**	**4,400**	**5,487**	**6,714**

Key Ratios

	Mar-19A	Mar-20A	Mar-21F	Mar-22F	Mar-23F
Revenue Growth	16.5%	10.6%	(6.3%)	20.6%	10.6%
Operating EBITDA Growth	3.5%	24.9%	15.0%	20.0%	16.4%
Operating EBITDA Margin	7.6%	8.6%	10.5%	10.5%	11.0%
Net Cash Per Share (Rs)	(5.34)	(4.47)	3.34	0.47	3.19
BVPS (Rs)	14.45	16.94	20.73	25.86	31.64
Gross Interest Cover	5.17	5.22	7.59	9.30	9.92
Effective Tax Rate	33.9%	31.2%	25.2%	25.2%	25.2%
Net Dividend Payout Ratio	24.4%	25.4%	18.0%	14.2%	15.4%
Accounts Receivables Days	76.96	66.92	59.34	50.73	57.13
Inventory Days	70.58	71.28	75.71	66.72	69.86
Accounts Payables Days	94.68	88.23	89.02	80.06	83.83
ROIC (%)	26.5%	31.5%	29.7%	42.9%	35.8%
ROCE (%)	26.4%	30.3%	33.9%	36.3%	34.3%
Return On Average Assets	14.6%	15.0%	16.5%	18.1%	17.7%

SOURCES: EIP RESEARCH, COMPANY REPORTS

India

ADD *(Initiating coverage)*

Consensus ratings*:	Buy 13	Hold 0	Sell 0

Current price:	Rs495
Target price:	Rs645
Previous target:	N/A
Up/downside:	30.3%
EIP Research / Consensus:	10.9%
Reuters:	KEIN.NS
Bloomberg:	KEII IN
Market cap:	US$611m
	Rs44,451m
Average daily turnover:	US$1.5m
	Rs107.7m
Current shares o/s:	89.9m
Free float:	59.7%

Source: Bloomberg

Source: Bloomberg

Price performance	*1M*	*3M*	*12M*
Absolute (%)	(1.1)	17.5	26.0
Relative (%)	0.3	6.7	(11.4)

Major shareholders	% held
Promoters	40.3
FRANKLIN BUILD INDIA FUND	5.3
HDFC Retirement Saving Fund	4.5

KEI Industries Ltd

Improving on all counts

- Growing fastest among peers in a large cable and wire (C&W) market.
- Time/capital invested aimed at increasing B2C (business to consumer) sales.
- Working capital improvement a big positive, FY21-23F EPS CAGR of 24% and P/E rerating to drive stock price; Add with TP of Rs645.

Fastest-growing cable and wire player among domestic peers

As organised players continue to win market share over their smaller unorganised peers across industries in India, KEI is also a beneficiary and grew its consolidated revenues at a CAGR of 20% over FY16-20 while the C&W industry grew at a CAGR of 10-11% (Polycab 1QFY20 presentation). KEI is planning a large greenfield capacity expansion of retail-focused products and is exploring entry into new product segments like fast-moving electrical goods (FMEG). Management stated at its 3QFY21 investor call its intent to double its topline to Rs100bn over the next five years. We estimate a revenue CAGR of 18% over FY21-23F and KEI to be the fastest-growing player in the Indian C&W market.

Revenue mix tilting towards high operating margin segments

Most of the recent and future greenfield capex was and is directed towards doubling capacities of housing wires (HW), low/high tension (LT/HT) cables and extra high voltage (EHV) cables. The sales channel mix has been gradually moving to a higher share of B2C sales, driving EBITDA margin expansion (EHV/HW currently have ~11-15% EBITDA margins). We expect the lower-margin institutional and engineering, procurement and construction (EPC) segment sales to continue to decline while the dealer/distributor channel sales to rise going forward. Changing revenue mix in favour of higher margin segments would drive EBITDA CAGR of 18.2% over FY21-23F.

Return ratios to trend back to pre-COVID levels

KEI has decided to shift focus away from the working capital (WC) intensive EPC segment and limit revenues to Rs5bn-6bn (Rs8bn-9bn earlier) annually going forward. This would lead to lower incremental WC needs, in our view, apart from the release of WC blocked as retention money (~Rs1bn-1.5bn) in previously executed EPC projects. We estimate lower working capital investment of Rs1.7bn (FY18-20: Rs2.8bn) over FY21-23F and all capex to be funded internally. We estimate cumulative FCFF of Rs7bn over FY21-23F and RoE/RoCE to increase by 171bp/329bp to 18.3%/24.4% respectively by FY23F.

Earnings growth and scope for valuation re-rating make us bullish

The stock trades at 10.7x FY23F EPS and EV/EBITDA of 6.2x. Factors like improving B2C revenue mix, better operating margins vs. the past, net cash balance sheet, capital allocation discipline and strong cash flows make us bullish on the stock. We expect EPS CAGR of 23.5% over FY21-23F and value KEI at a three-year mean P/E of 14x FY23F EPS and initiate coverage on KEI Industries with a TP of Rs645 and an Add rating. Risks: Capex delays, high raw material prices and stiff competition in new markets by incumbents.

Financial Summary	Mar-19A	Mar-20A	Mar-21F	Mar-22F	Mar-23F
Revenue (Rsm)	42,310	48,878	42,467	51,444	59,034
Operating EBITDA (Rsm)	4,405	4,971	4,608	5,556	6,435
Net Profit (Rsm)	1,789	2,554	2,715	3,487	4,142
Core EPS (Rs)	22.9	31.6	30.2	38.8	46.1
Core EPS Growth	23.7%	38.2%	(4.5%)	28.5%	18.8%
FD Core P/E (x)	21.68	15.46	15.56	12.75	10.73
DPS (Rs)	1.2	2.8	2.0	4.0	4.4
Dividend Yield	0.29%	0.69%	0.40%	0.81%	0.89%
EV/EBITDA (x)	11.00	9.25	9.44	7.66	6.20
P/FCFE (x)	36.22	(16.81)	18.63	(168.05)	20.55
Net Gearing	51.7%	10.0%	(5.4%)	(9.2%)	(18.7%)
P/BV (x)	5.00	2.66	2.52	2.14	1.82
ROE	26.0%	22.4%	16.6%	18.2%	18.3%
% Change In Core EPS Estimates					
EIP Research/Consensus EPS (x)			1.05	1.08	1.09

SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS. PRICED AS AT 12 MAR 2021

Analyst(s)

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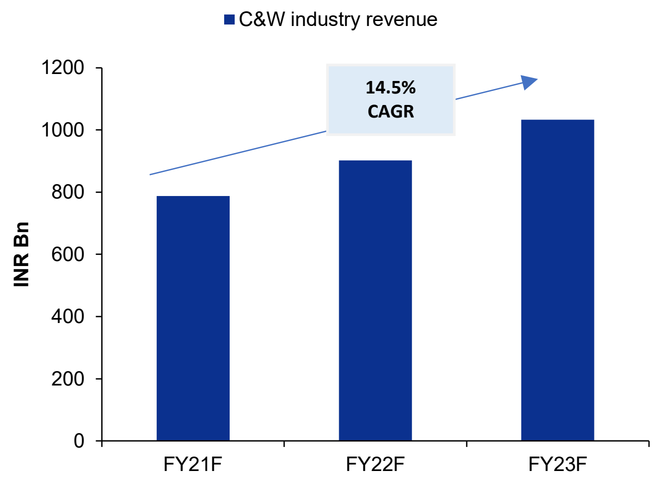
Improving on all counts

Fastest-growing player in a large domestic cable and wire market

Target revenue CAGR likely to exceed industry's

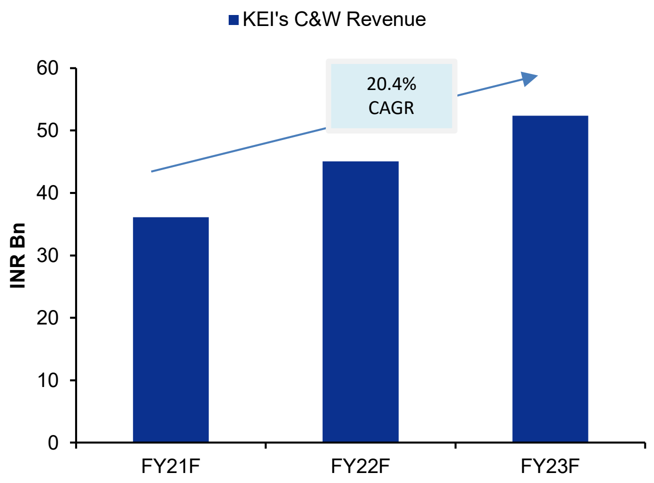
KEI's management intends to double sales to Rs100bn over the next five years (Source: KEI's 3QFY21 investor call). The company's strong foothold in the institutional project business in India, coupled with higher focus on increasing B2C sales, would lead to industry-leading revenue growth over FY21-23F. We expect KEI to be the fastest-growing C&W company in our coverage universe and gain meaningful market share over this period.

Figure 272: Cables and Wires (C&W) industry growth



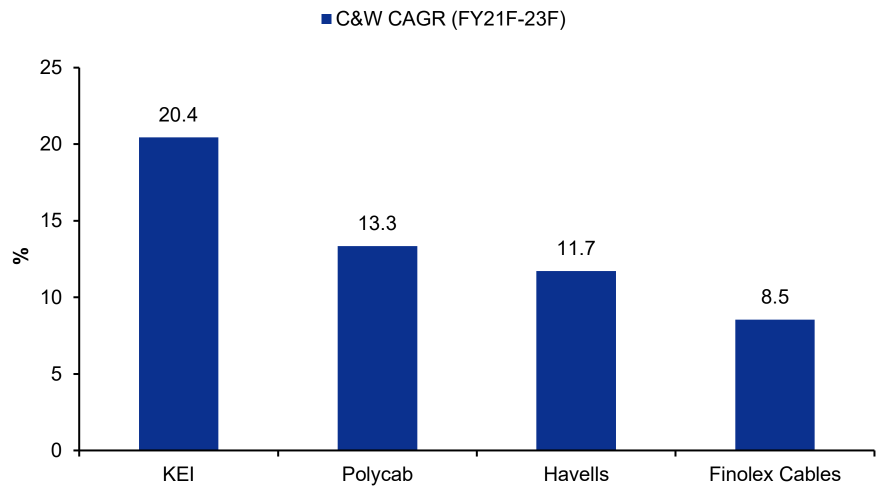
SOURCES: EIP RESEARCH ESTIMATES, POLYCAB

Figure 273: KEI's C&W business to exceed industry growth



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 274: We expect KEI's C&W revenue growth to exceed its peers



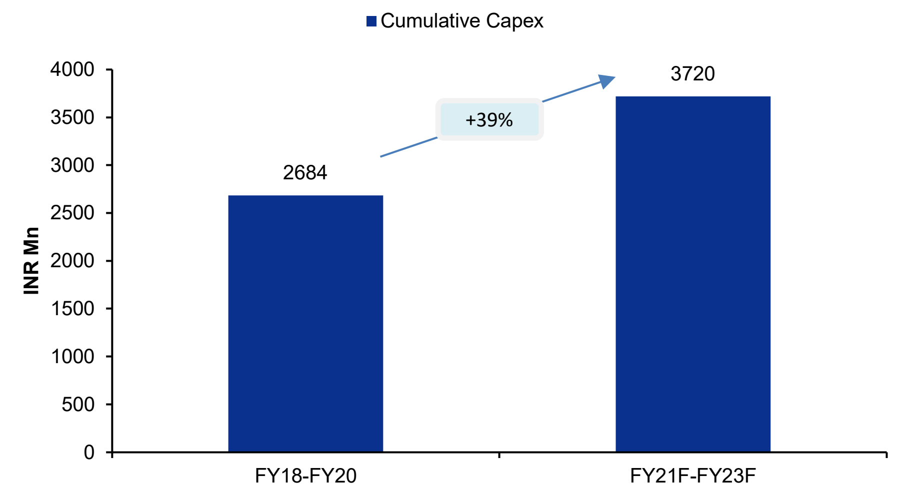
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Capex plan in sync with targeted revenue growth

Management intends to double sales over the next five years to Rs100bn.

Management has guided for a Rs6bn-7bn (includes land cost) greenfield capital expenditure to double manufacturing capacity mainly of low tension (LT), high tension (HT) and extra high voltage (EHV) cables over the next four fiscals. This is in line with management's intention of doubling sales over the next five years. Most of this capex will be funded through internal accruals and no incremental debt would be drawn for this expansion.

Figure 275: Meaningful (~40%) rise in capex over FY21-23F

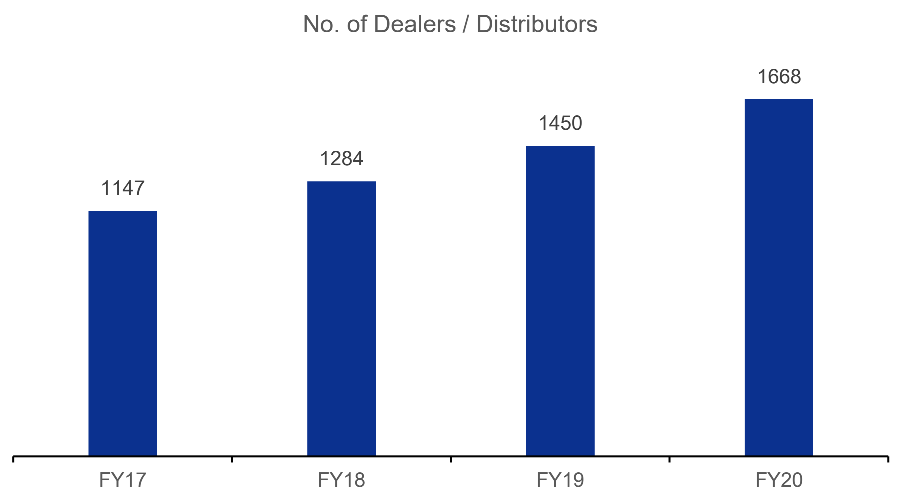


SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Expanding dealer network would facilitate entry into new retail product segments, widening total addressable market (TAM)

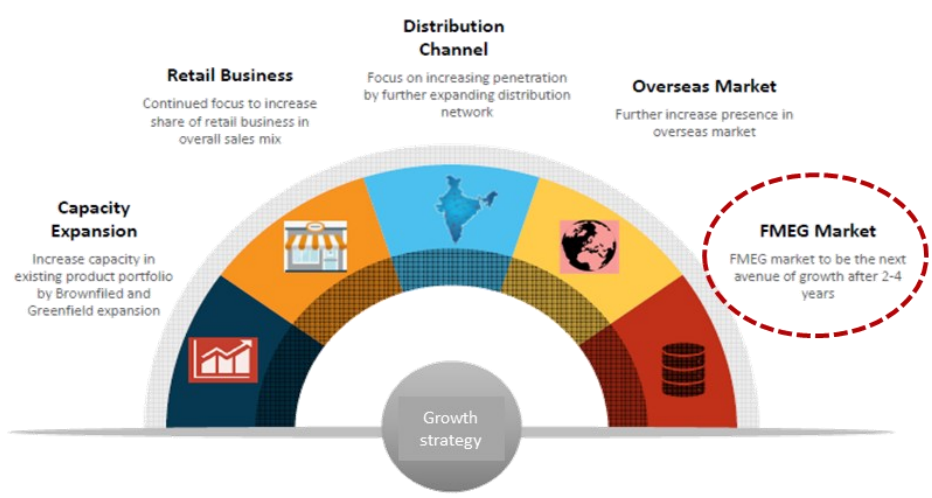
KEI expanded its dealer network and deepened its presence into metros and rural markets over the past five years. Retail revenue share increased to over 30% in the same period and we expect this to continue going forward. KEI is exploring its entry into the lucrative fast-moving electricals goods (FMEG) segment. If KEI decides to enter the space, the total addressable market (TAM) significantly increases for KEI and opens an opportunity to gain market share in the overall electrical segment. The Indian FMEG industry was estimated at ~Rs600bn as of FY20 (Source: Polycab 1QFY20 investor presentation).

Figure 276: Expanding dealer network to facilitate higher retail sales



SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 277: Management has identified FMEG market as a key growth strategy area, thereby widening the addressable market

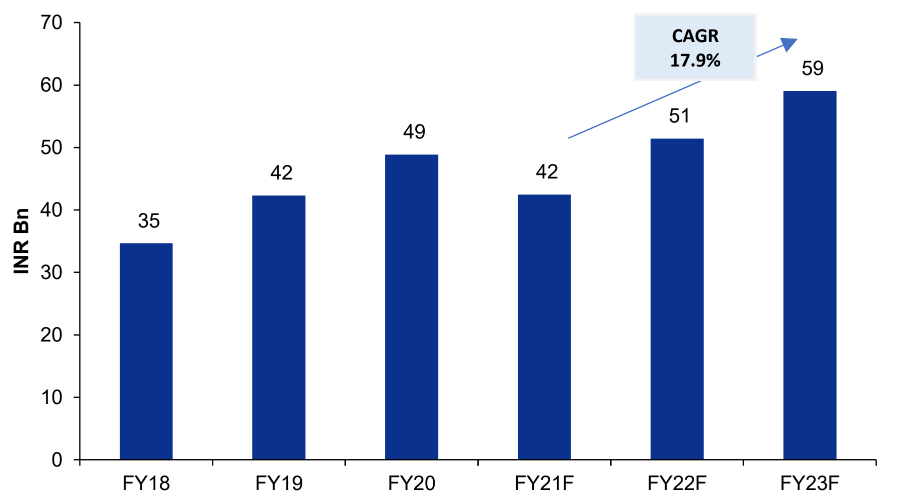


SOURCES: EIP RESEARCH, COMPANY REPORTS

Housing wire to lead growth over FY21-23F

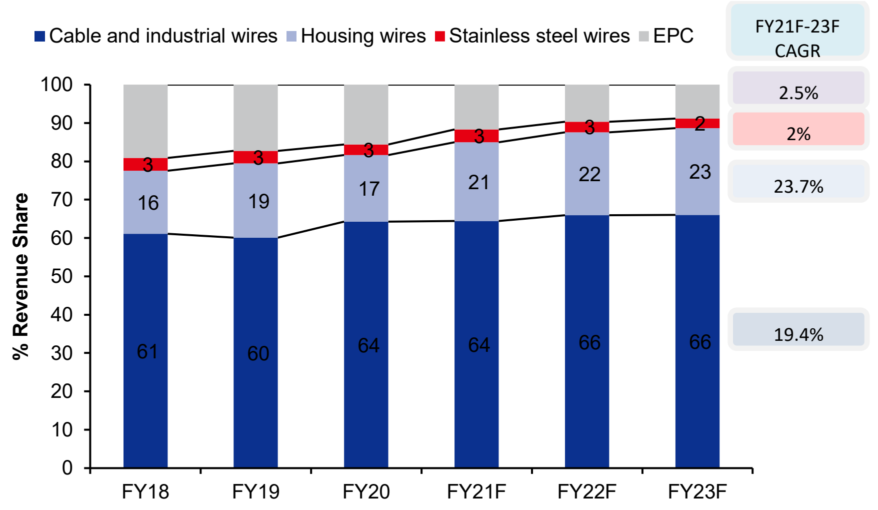
We estimate KEI's share of flexible housing wires to increase by 520bp to 22.6% by FY23F from 17.4% in FY20. Housing wire revenue CAGR is estimated at 23.7% over FY21-23F, much higher than KEI's consolidated revenue CAGR of 17.9% over the same period.

Figure 278: Expect 17.9% revenue CAGR for KEI over FY21F-FY23F



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 279: Housing wires will post the fastest growth, aiding revenue share gains



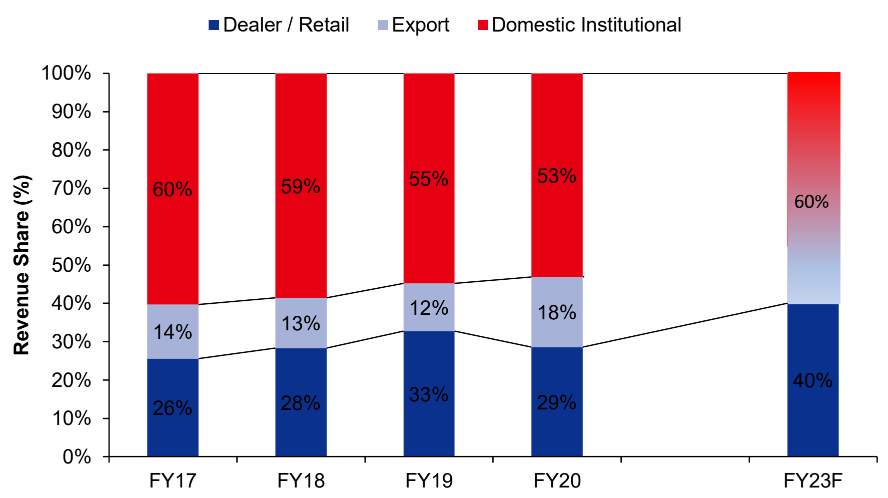
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Cost savings benefit to remain largely sustainable going forward, EBITDA to grow faster than revenues

Institutional business to decline gradually, management aims to raise B2C sales to 40% of overall business

KEI's operating margin band moved up gradually to the 10-11% range over the past two years (from 9-10% earlier) due to the change in sales mix (higher retail sales) and cost savings initiatives undertaken during the pandemic. Management intends to increase the share of retail business to 40% of overall business (9MFY21: 32% of sales) over the medium term. The share of the institutional business would continue to decline as we expect revenue growth to be much higher in the LT and housing wires segment.

Figure 280: Revenue mix tilting towards LT/HT and housing wire sales

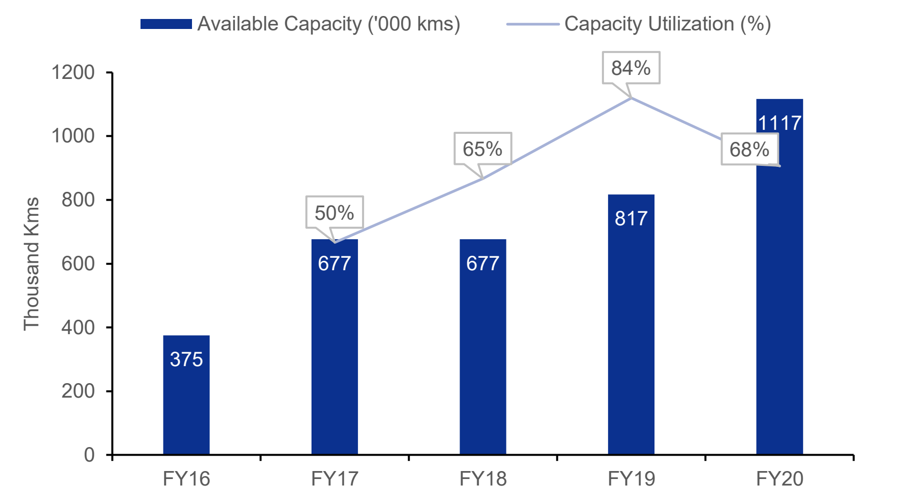


SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Underutilised housing wire capacities drive higher B2C sales

KEI nearly doubled its housing wire manufacturing capacity over FY18-20. Management estimated the peak revenue potential post expansion at Rs16bn over the next four to five years. It expects capacity utilisation to improve after the FY21F pandemic impact and we expect housing wires to account largely for the increase in the share of B2C segment going forward.

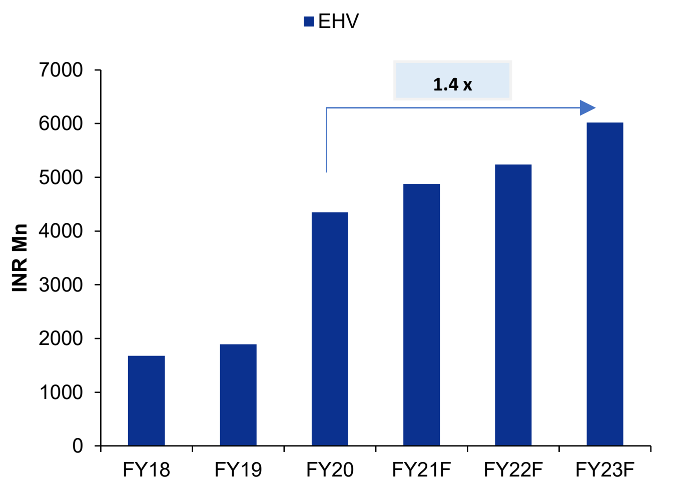
Figure 281: Housing wire capacity nearly doubled over FY18-20



SOURCES: EIP RESEARCH, COMPANY REPORTS

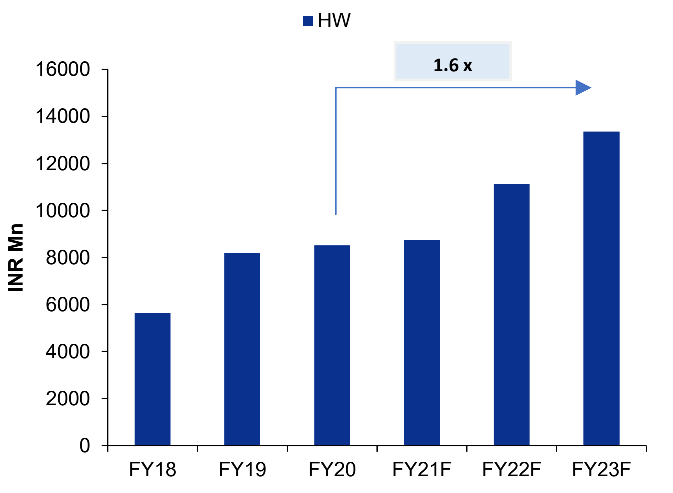
Revenue mix shifting towards higher margin EHV and housing wires segment

Figure 282: EHV cable revenue to grow 1.4x over FY20-23F



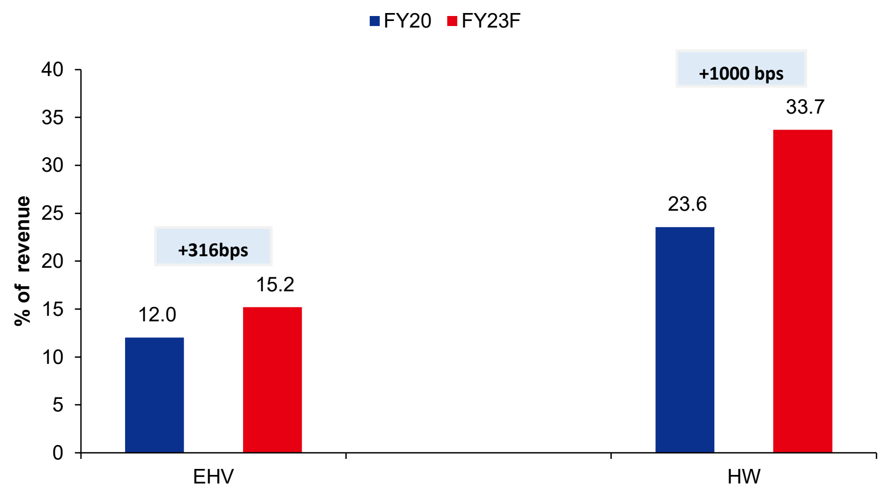
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 283: HW cable revenue to grow 1.6x over FY20-23F



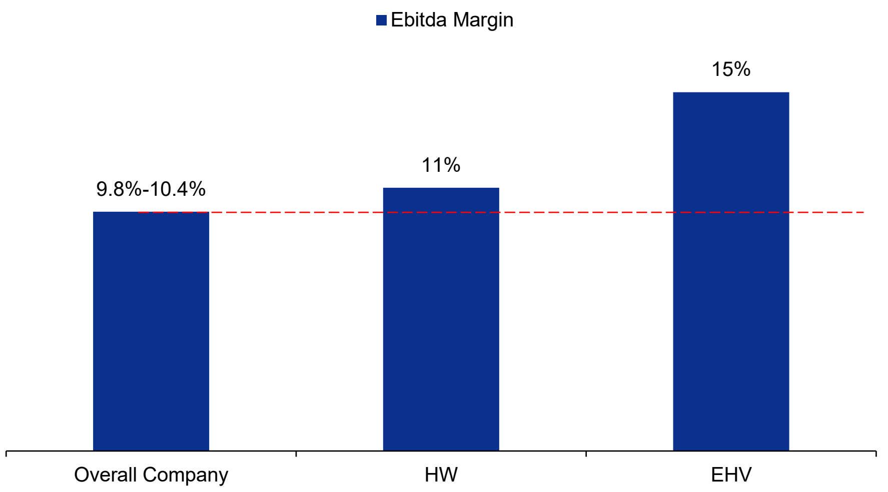
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 284: Revenue share of higher margin EHV & HW to aid EBITDA margin expansion



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

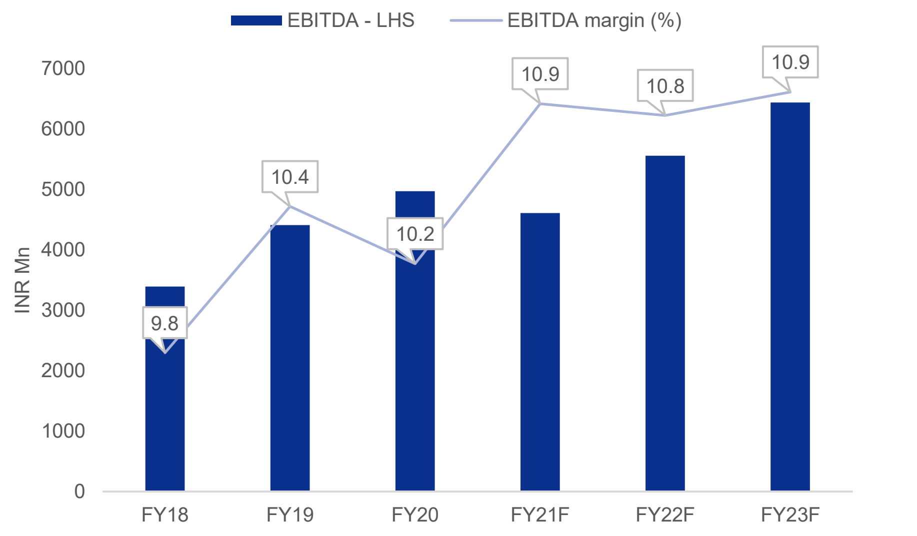
Figure 285: Approximate segment-wise EBITDA margins (FY18-20)



SOURCES: EIP RESEARCH, COMPANY REPORTS

We expect KEI to post EBITDA CAGR of 18.2% over FY21-23F though operating margins may remain in a tight band

Figure 286: EBITDA margins being retained in a band of 10.5-11%



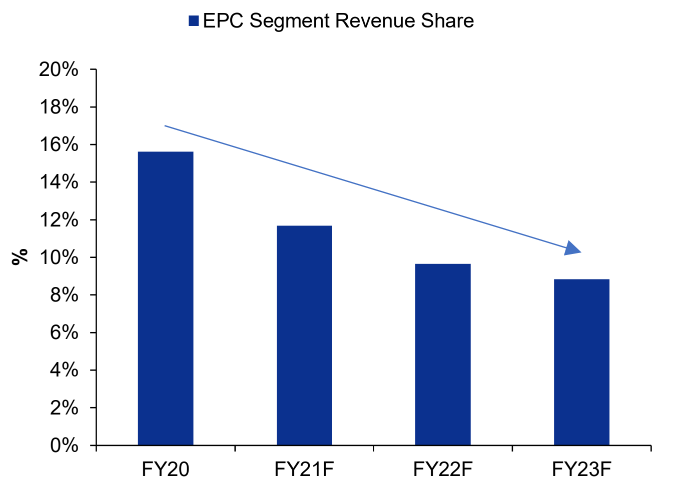
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

KEI to be debt free soon with higher FCF generation and strong return ratios

Pursuant to the QIP in Jan 2020, KEI raised Rs4.9bn (net of issue expenses) and utilised most of it to repay outstanding debt. Further, limiting the EPC revenue exposure de-risks the business and would enable a meaningful release of working capital deployed in the business. Incremental needs for working capital are lower while most of the greenfield capex would be funded through internal accruals without resorting to any new debt, in our view.

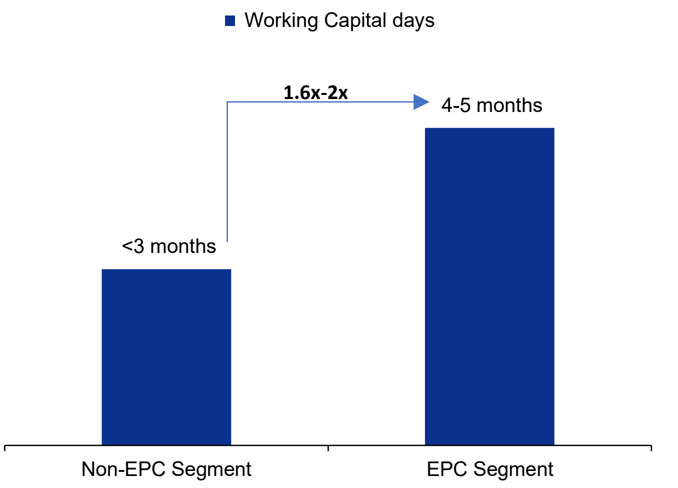
Reducing focus on working capital intensive-EPC segment would unlock meaningful capital deployed in the business

Figure 287: KEI reducing its focus on EPC segment



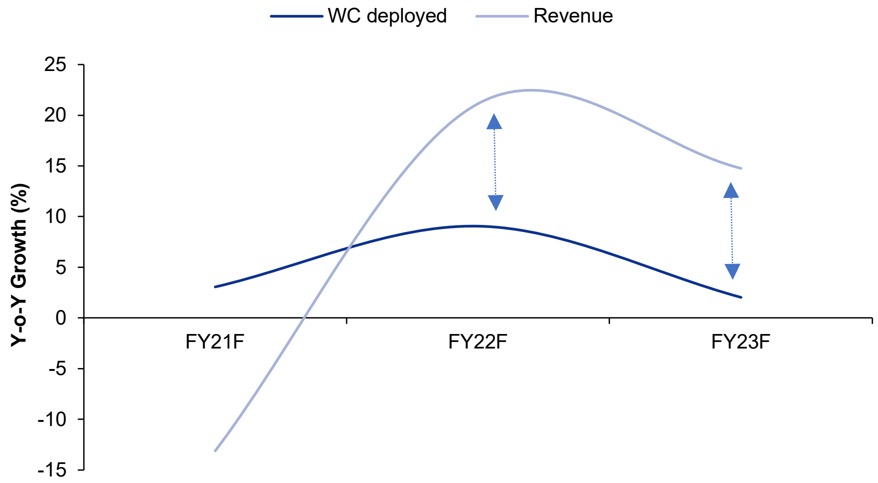
SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 288: WC needs (~1.6-2x) are higher in EPC business



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

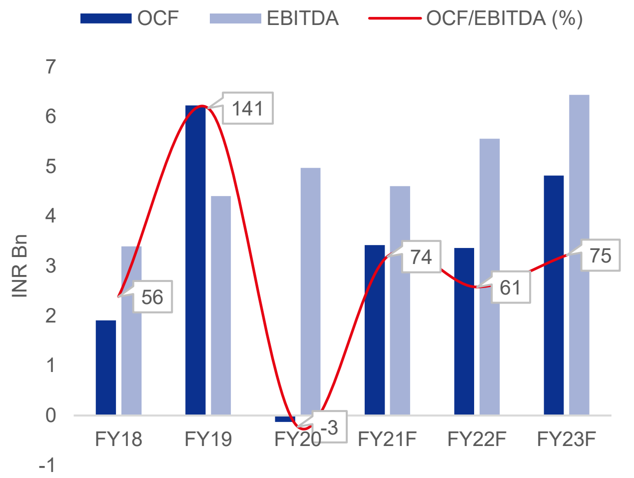
Figure 289: Lower saliency of EPC business will ensure lower incremental WC deployed compared to revenue growth



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

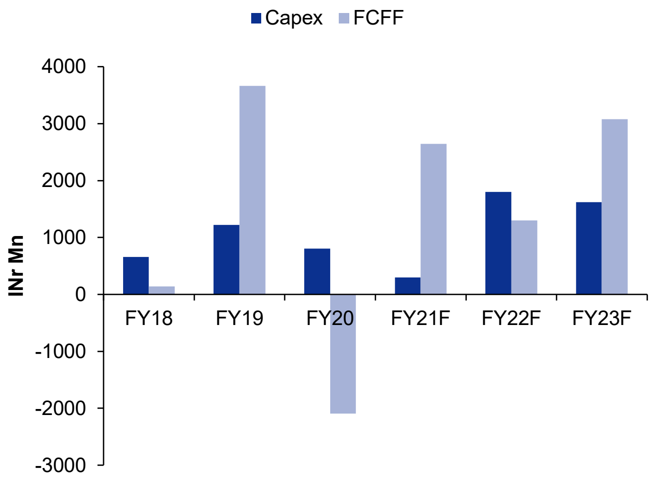
We expect much lower debt over the next 12 months; KEI could soon be debt free

Figure 290: KEI – Healthy OCF generation



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Figure 291: FCFF rising despite aggressive capex plan



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

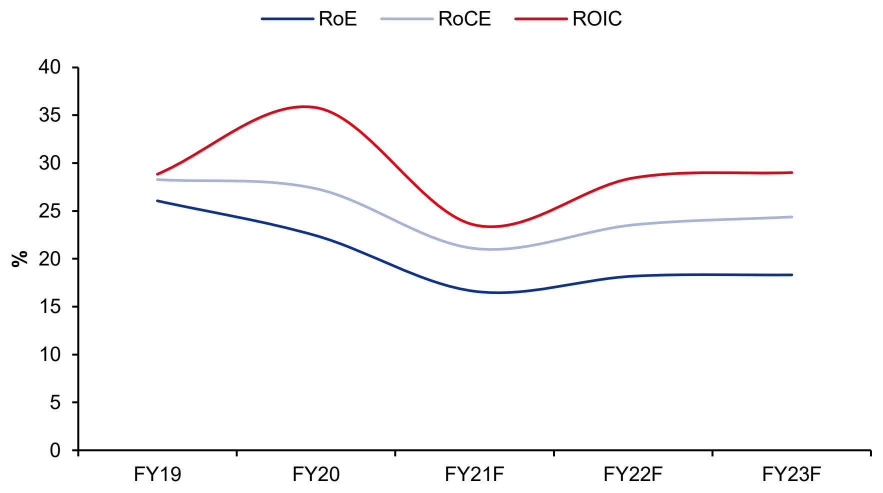
Figure 292: KEI will be able to reduce debt meaningfully

SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

Return ratios to rise again after the pandemic hitch

We expect RoE (return on equity) and RoCE (return on capital employed) to improve by 171bp and 329bp over FY21-23F respectively. We expect RoIC (return on invested capital) to trend back to 23-30% levels over the same period.

Figure 293: Return ratios to trend back to healthy levels



SOURCES: EIP RESEARCH ESTIMATES, COMPANY REPORTS

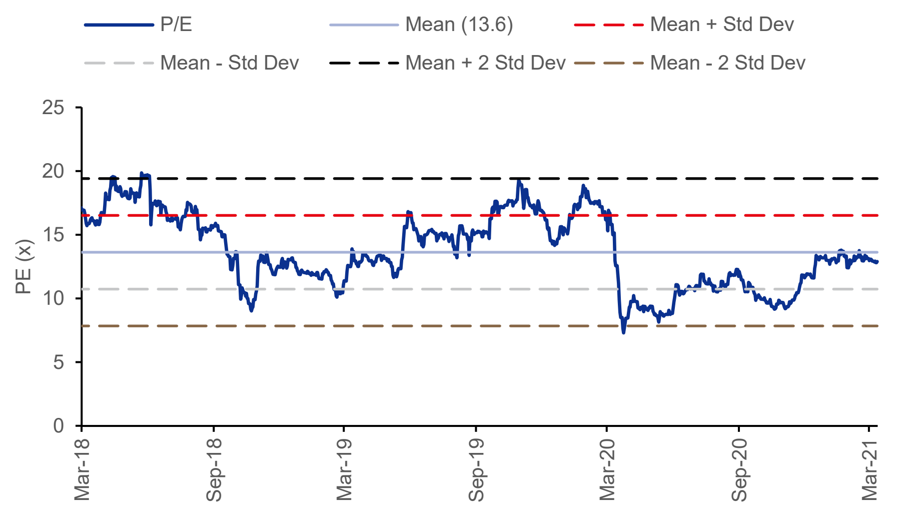
Valuation

- Improving B2C share of business, emerging brands in the flexible housing wires segment, higher operating margin profile, leaner balance sheet and strong free cash flow generation are key positives.
- Traditionally, long working capital cycle and related debt have been concerns for KEI's stock valuation. Capital allocation discipline, clear priorities to de-focus from the EPC segment and a well-defined unlevered debt strategy should help address investor concerns going forward.
- The stock trades at P/E of 10.7x its FY23F EPS, much lower than its three-year mean P/E of 13.6x.
- KEI has been improving its franchise value, network presence, stability in revenue and EBITDA margin profile, lower incremental working capital investments and we expect strong return ratios going forward.
- Hence, we value KEI in line with its three-year mean P/E with potential for further re-rating as the company successfully delivers on its B2C journey. We

use the three year mean P/E (1 year forward) as the B2C share of the business has materially improved over this period and is reflective of the change in the nature of KEI's business with a higher share of retail revenues.

- Our price target of Rs645 is based on 14x FY23F EPS with upside potential of 30%. We initiate coverage on KEI with an Add rating.

Figure 294: KEI trading near its 3-year mean P/E (1 year forward)



SOURCES: EIP RESEARCH, COMPANY REPORTS, BLOOMBERG

Figure 295: P/E Band Chart

SOURCES: EIP RESEARCH, COMPANY REPORTS, BLOOMBERG

Downside risks

- **Large capex plans:** KEI has embarked on a journey of large capital expenditure plan of Rs6bn-7bn over the next four to five years. The execution of this plan is critical for our revenue CAGR estimate of 18% over FY21-23F to play out. Any execution delays in the form of right of way issues, land acquisition, regulatory clearances, equipment supply, etc, could lead to lower-than-estimated revenues.
- **Regional revenue concentration risk:** KEI derived ~70% of its total FY20 revenues from North and West India and is heavily dependent on these regions for revenue growth. A sharp rise in competition in these markets could affect KEI's growth and profitability.
- **High raw material prices:** Copper is the key raw material for C&W manufacturing. The recent spike in copper and most commodity prices has led the company to hike prices repeatedly to pass on RM inflation. However, short-term wild swings impact product demand and margins.

Stiff competition: Competition is fairly high in the C&W and FMEG spaces given most of our coverage universe are market leaders in the space. Stiff competition may lead to price wars or higher trade incentives, leading to lower profitability for the company.

Business description and management profile

KEI is a leading manufacturer of cables and wires in India, with its product portfolio ranging from house wires to low tension (LT) power cables, high tension (HT) cables and extra high voltage (EHV) cables, catering to retail and institutional customers. It is one of the few manufacturers of EHV cables in India. KEI's market share in the total cables and wires industry was 5.2% whereas share in the organised cables and wires industry was 7.3% in 2019. The company operates its business under three segments – retail, institutional and exports segments.

KEI's board consists of six independent directors and four non-independent directors.

Figure 296: Promoter profile

Name and Designation	Profile
Mr. Anil Gupta Chairman-cum-Managing Director	Mr. Anil Gupta is an expert in the Indian cables and wires industry and a strong believer in modern technology. Mr. Gupta has initiated various policies on marketing, production, quality control and product development. He has spearheaded some pathbreaking innovations in the industry and been the guiding force behind KEI's vision to become the undisputed leader in its category and build a robust corporate identity. Mr. Gupta began his journey with KEI in 1979 as a partner in the erstwhile Krishna Electrical Industries and soon rose to become its Chairman-cum-Managing Director. With almost 39 years of experience at the helm, Mr. Gupta has helped the company scale new heights of success.

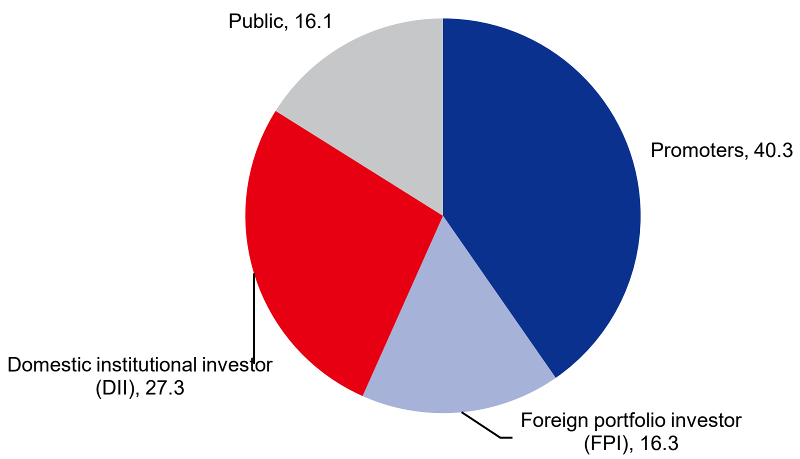
SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 297: Key management

Name	Designation	Education	Experience	Prior Employment
Mr. Rajeev Gupta	ED (Finance) & CFO	Bachelor of Commerce (Hons.), CA	27 years	NA
Mr. Pawan Kumar Aggarwal	Executive Director (Projects)	B.Sc., Diploma (Electronics)	38 years	NA
Mr. Manoj Kakkar	Executive Director (Sales & Marketing)	Bachelor of Commerce, PGDM (Marketing)	31 years	Premier Cable
Mr. Lalit Sharma	COO	Bachelor of Technology (E&C)	24 years	Plaza Group
Mr. Kishore Kunal	GM (Corporate) & Company Secretary	Bachelor of Commerce, CS, LLB	17 years	Shri Rathi Steel Limited

SOURCES: EIP RESEARCH, COMPANY REPORTS

Figure 298: Share Holding Pattern (Dec 2020)



SOURCES: EIP RESEARCH, BSE WEBSITE

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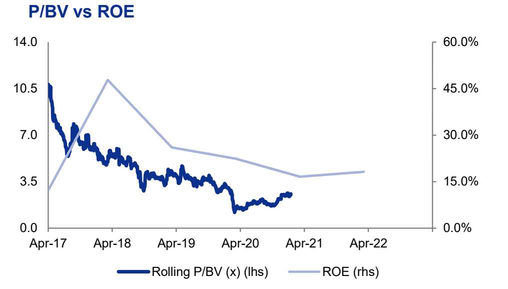

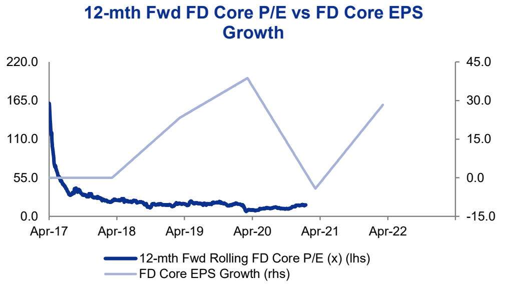

Profit & Loss

(Rs mn)	Mar-19A	Mar-20A	Mar-21F	Mar-22F	Mar-23F
Total Net Revenues	**42,310**	**48,878**	**42,467**	**51,444**	**59,034**
Gross Profit	**12,986**	**15,056**	**12,740**	**15,485**	**17,828**
Operating EBITDA	**4,405**	**4,971**	**4,608**	**5,556**	**6,435**
Depreciation And Amortisation	(339)	(567)	(578)	(666)	(814)
Operating EBIT	**4,066**	**4,404**	**4,029**	**4,889**	**5,621**
Financial Income/(Expense)	(1,317)	(1,157)	(478)	(265)	(123)
Pretax Income/(Loss) from Assoc.					
Non-Operating Income/(Expense)	33	32	75	35	37
Profit Before Tax (pre-EI)	**2,782**	**3,279**	**3,627**	**4,659**	**5,535**
Exceptional Items	(19)	(9)	1		
Pre-tax Profit	**2,763**	**3,270**	**3,628**	**4,659**	**5,535**
Taxation	(974)	(716)	(913)	(1,173)	(1,393)
Exceptional Income - post-tax					
Profit After Tax	**1,789**	**2,554**	**2,715**	**3,487**	**4,142**
Minority Interests					
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	**1,789**	**2,554**	**2,715**	**3,487**	**4,142**
Recurring Net Profit	1,801	2,561	2,714	3,487	4,142
Fully Diluted Recurring Net Profit	**1,801**	**2,561**	**2,714**	**3,487**	**4,142**

Cash Flow

(Rs mn)	Mar-19A	Mar-20A	Mar-21F	Mar-22F	Mar-23F
EBITDA	4,405	4,971	4,608	5,556	6,435
Cash Flow from Invt. & Assoc.					
Change In Working Capital	2,593	(4,328)	(347)	(1,055)	(259)
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense					
Other Operating Cashflow	(1,226)	(984)	(402)	(230)	(86)
Net Interest (Paid)/Received	1,319	1,159	478	265	123
Tax Paid	(865)	(947)	(913)	(1,173)	(1,393)
Cashflow From Operations	**6,227**	**(130)**	**3,424**	**3,363**	**4,820**
Capex	(1,223)	(805)	(300)	(1,800)	(1,620)
Disposals Of FAs/subsidiaries	3	3			
Acq. Of Subsidiaries/investments	(1,567)	780		(750)	(500)
Other Investing Cashflow	37	133	144	173	213
Cash Flow From Investing	**(2,751)**	**110**	**(156)**	**(2,377)**	**(1,907)**
Debt Raised/(repaid)	(2,406)	(2,328)	(1,000)	(1,250)	(750)
Proceeds From Issue Of Shares	20	4,890	1		
Shares Repurchased					
Dividends Paid	(94)	(276)	(180)	(359)	(395)
Preferred Dividends					
Other Financing Cashflow	(1,378)	(1,292)	(622)	(438)	(336)
Cash Flow From Financing	**(3,858)**	**994**	**(1,801)**	**(2,047)**	**(1,482)**
Total Cash Generated	(382)	974	1,467	(1,062)	1,431
Free Cashflow To Equity	**1,070**	**(2,348)**	**2,268**	**(264)**	**2,163**
Free Cashflow To Firm	**2,120**	**(1,312)**	**2,646**	**548**	**2,577**

SOURCES: EIP RESEARCH, COMPANY REPORTS

BY THE NUMBERS…cont'd

Balance Sheet

(Rs mn)	Mar-19A	Mar-20A	Mar-21F	Mar-22F	Mar-23F
Total Cash And Equivalents	1,953	2,144	3,611	3,299	5,230
Total Debtors	10,909	13,676	11,635	12,685	12,939
Inventories	6,932	8,638	7,563	8,457	9,704
Total Other Current Assets	2,462	2,401	1,771	2,145	2,462
Total Current Assets	**22,256**	**26,858**	**24,579**	**26,585**	**30,335**
Fixed Assets	4,856	4,960	4,694	5,677	6,484
Total Investments	24	17	17	17	17
Intangible Assets					
Total Other Non-Current Assets	507	854	842	992	992
Total Non-current Assets	**5,386**	**5,831**	**5,553**	**6,686**	**7,493**
Short-term Debt	3,865	2,624	2,652	1,402	652
Current Portion of Long-Term Debt					
Total Creditors	3,152	1,711	1,745	2,114	2,426
Other Current Liabilities	10,206	11,690	7,563	8,457	9,704
Total Current Liabilities	**17,224**	**16,025**	**11,959**	**11,972**	**12,782**
Total Long-term Debt	2,113	1,028			
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	86	257	257	257	257
Total Non-current Liabilities	**2,200**	**1,285**	**257**	**257**	**257**
Total Provisions	441	308	308	308	308
Total Liabilities	**19,864**	**17,618**	**12,525**	**12,537**	**13,347**
Shareholders Equity	7,779	15,071	17,607	20,734	24,481
Minority Interests					
Total Equity	**7,779**	**15,071**	**17,607**	**20,734**	**24,481**

Key Ratios

	Mar-19A	Mar-20A	Mar-21F	Mar-22F	Mar-23F
Revenue Growth	22.1%	15.5%	(13.1%)	21.1%	14.8%
Operating EBITDA Growth	29.8%	12.8%	(7.3%)	20.6%	15.8%
Operating EBITDA Margin	10.4%	10.2%	10.8%	10.8%	10.9%
Net Cash Per Share (Rs)	(51.18)	(18.63)	10.67	21.12	50.96
BVPS (Rs)	98.91	186.15	195.96	230.76	272.46
Gross Interest Cover	3.00	3.41	6.48	11.17	16.72
Effective Tax Rate	35.3%	21.9%	25.2%	25.2%	25.2%
Net Dividend Payout Ratio	4.1%	8.4%	5.0%	7.7%	7.1%
Accounts Receivables Days	91.18	91.80	108.77	86.27	79.21
Inventory Days	77.72	84.01	99.46	81.30	80.43
Accounts Payables Days	25.80	26.24	21.22	19.59	20.11
ROIC (%)	28.8%	35.8%	23.5%	28.4%	29.0%
ROCE (%)	28.3%	27.3%	21.1%	23.5%	24.4%
Return On Average Assets	16.4%	14.7%	13.1%	15.5%	15.9%

SOURCES: EIP RESEARCH, COMPANY REPORTS

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1 CG Score 2019 from Thai Institute of Directors Association (IOD)
2 AGM Level 2018 from Thai Investors Association
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SET and mai listed companies passed the assessment conducted by the Stock Exchange of Thailand: THSI (SET) and THSI (mai)
SET listed companies passed the assessment conducted by the Dow Jones Sustainability Indices (DJSI)

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Hold	The stock's total return is expected to be between 0% and positive 10% over the next 12 months.
Reduce	The stock's total return is expected to fall below 0% or more over the next 12 months.

The total expected return of a stock is defined as the sum of the: (i) percentage difference between the target price and the current price and (ii) the forward net dividend yields of the stock. Stock price targets have an investment horizon of 12 months.

Sector Ratings	Definition:
Overweight	An Overweight rating means stocks in the sector have, on a market cap-weighted basis, a positive absolute recommendation.
Neutral	A Neutral rating means stocks in the sector have, on a market cap-weighted basis, a neutral absolute recommendation.
Underweight	An Underweight rating means stocks in the sector have, on a market cap-weighted basis, a negative absolute recommendation.

Country Ratings	Definition:
Overweight	An Overweight rating means investors should be positioned with an above-market weight in this country relative to benchmark.
Neutral	A Neutral rating means investors should be positioned with a neutral weight in this country relative to benchmark.
Underweight	An Underweight rating means investors should be positioned with a below-market weight in this country relative to benchmark.