Sharekhan
by BNP PARIBAS

Supreme Industries

Impressive margin performance, reasonable valuation

Sector: Building Material
Results Update

	Change
Reco: **Buy**	↔
CMP: **Rs. 979**	
Price Target: **Rs. 1,120**	↔

↑ Upgrade ↔ No change ↓ Downgrade

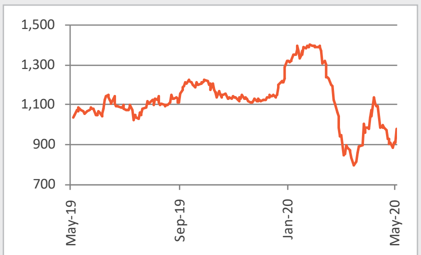
Company details

Market cap:	Rs. 12,432 cr
52-week high/low:	Rs. 1,413/79
NSE volume: (No of shares)	40,085
BSE code:	509930
NSE code:	SUPREMEIND
Sharekhan code:	SUPREMEIND
Free float: (No of shares)	6.4 cr

Shareholding (%)

Promoters	49.7
FII	8.6
DII	23.5
Others	18.2

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-5.6	-29.5	-13.9	-5.8
Relative to Sensex	-3.3	-5.5	10.5	15.2

Sharekhan Research, Bloomberg

Supreme Industries Limited (SIL) delivered in-line revenue and net profit performance, while EBITDA margin beat our estimates led by lower input cost, higher contribution of value-added products and price hike in CPVC. Revenue declined by 6.6% y-o-y to Rs. 1,430.5 crore, in-line with our expectations, owing to substantial reduction of operations at various plants due to outbreak of COVID-19. EBITDA margins improved by 590 BPS y-o-y to 19.1%, exceeding our estimates, led by better product mix, higher contribution of value-added products, good inventory gains and support from suppliers (discount on raw material). Reported net profit came at Rs. 117 crore (up 4% y-o-y) and in-line with our estimates owing to higher tax provision. The company suspended providing annual volume and margin guidance due to COVID-19 related uncertainties. As the company's products don't fall under essential category, the lockdown restrictions have severely impacted its operations in the month of April and May (historically Q1 & Q2 are strong quarters for the company). Further, the sharp fall in PVC prices is expected to impact its plastic piping segment (was only solace till now). We expect muted performance in 1HFY2021 owing to continued slowdown in growth across its segments and reduction in discretionary spends, followed by a gradual recovery from 2HFY2021. Margins are expected to decline to 13.5% in FY2021 owing to higher inventory loss and anticipated decline in margins across the segments. However, we expect margins to improve gradually in FY2022E on the back of recovery in revenue growth in plastic piping segment and transport benefits from setting up plants in eastern India (Odisha & Telangana).

Key positives

- EBITDA margin expanded by 590 BPS y-o-y, ahead of expectations
- Strong demand from agri segment given government's support to farmers
- Blended realisations improved 2.4% y-o-y

Key negatives

- Overall volume declined 9.5% y-o-y
- PVC price correction will lead to huge inventory loss in Q1FY2021

Our Call

Valuation: Maintain Buy with a PT of Rs. 1,120: We have fine-tuned our earnings estimates for FY2021/FY2022E factoring in Q4FY2020 performance and weak demand environment for plastic piping segment in affordable housing and infrastructure. We remain Positive on SIL for the long term, given recovery in rural economy, affordable housing sector and the new scheme for piped water connection – 'Nal se Jal'. Even though FY2021E is going to be a weak year, we expect gradual recovery of growth in FY2022E on account of pick-up in demand led by higher demand in the housing segment and infrastructure and upcoming opportunities in 'Nal se Jal' scheme. The stock price has corrected more than 40% from the peak over last four months. At CMP, the stock is currently trading at 34x/26x FY2021E/FY2022E, implying a ~20% discount to one year average 1-year forward valuation. Hence, we retain our Buy rating on the stock with a SoTP price target (PT) of Rs. 1,120.

Key Risks

Slowdown in demand offtake could impact revenue growth rates. Adverse commodity price fluctuation might impact the margin profile.

Valuation Rs cr

Particulars	FY18	FY19	FY20	FY21E	FY22E
Revenue	4,970.1	5,612.0	5,511.5	5,645.4	6,619.6
OPM (%)	15.8	14.0	15.1	13.5	14.3
Adjusted PAT	431.8	381.4	405.0	368.7	475.1
% YoY growth	14.6	(11.7)	6.2	(8.9)	28.8
Adjusted EPS (Rs.)	34.0	30.0	31.9	29.0	37.4
P/E (x)	28.8	32.6	30.7	33.7	26.2
P/B (x)	6.6	5.8	5.1	4.7	5.0
EV/EBITDA (x)	15.5	15.7	14.8	16.5	13.1
RoNW (%)	22.8	17.7	16.8	13.9	19.1
RoCE (%)	27.5	24.5	23.7	18.8	25.6

Source: Company; Sharekhan estimates

Revenue in-line, margins beat estimates: SIL delivered in-line revenue and net profit performance, while EBITDA margin beat our estimates led by lower input cost, higher contribution of value-added products and price hike in CPVC. Revenue declined by 6.6% y-o-y to Rs. 1,430.5 crore, in-line with our expectations, owing to substantial reduction of operations at various plants due to the outbreak of COVID-19.Volume growth in plastic piping, packaging, industrial products and consumer products segments declined 7.4% y-o-y, 17.6% y-o-y, 13% y-o-y and 14% y-o-y respectively. Overall volume declined by 9.5% y-o-y, while blended realisation grew by 2.4% y-o-y. EBITDA margin improved by 590 BPSy-o-y to 19.1%, exceeding our estimates, led by better product mix, higher contribution of value-added products, good inventory gains and support from suppliers (discount on raw material). Reported net profit came at Rs. 117 crore (up 4% y-o-y) and remained in-line with our estimates despite higher profitability, owing to to higher tax provision.

Near-term blip owing to COVID-19, expect gradual recovery in FY2022E: The company suspended providing annual volume and margin guidance in the wake of uncertainties due to COVID-19. As the company's products don't fall under the essential services category, the lockdown restrictions have severely impacted its operations in the month of April. The management indicated that commodity prices have started improving after reaching to bottoms, but the sharp fall in PVC resin prices is expected to impact its plastic piping segment (only solace till now). The management expects normalcy to return from September 2020 and move to a growth path by November 2020.We expect muted growth in 1HFY2021 owing to slowdown in growth across segments, followed by gradual recovery from 2HFY2021.

Capital outlay plans remains intact despite COVID-19 led business disruption: Demand for plastic piping system looks encouraging in long-term on account of higher urbanization, potential infrastructure spending, demand from affordable housing, roll out of 'Nal se Jal' scheme in certain states and higher demand from the agriculture segment. Hence, the company has maintained its earlier investment commitments around Rs. 500 crore, which would result in an increase in total capacity from 6,36,000 tonne to 7,00,000 tonne by March 2021. The company has incurred capex of Rs. 241 crore in FY2020 and further committed Capex of about Rs. 182 Crs to set up new production units and expansion of capacity in existing facilities. The company plans capex in the range Rs. 150-200 crore for FY2021. Management indicated that maximum capacity addition (around 70-80% of total incremental capacity) would be in the plastic piping system. This would increase plastic piping capacity from 4,40,000 tonne to 5,00,000 tonne by March 2021.

Q4FY2020 results concall highlights

- **COVID-19 update:** Nationwide lockdown restrictions had substantially reduced its operations at various plants between 25 to 35 days. The company has since, after receiving applicable permissions, partially commenced operations including dispatch of goods to customers at all its manufacturing facilities and scaling up the same gradually. Management expects normalcy to return in its businessfrom September 2020 and will move to growth path by November 2020.
- **Volume growth impacted owing to COVID-19 outbreak:** The company reported a 9.5% y-o-y decline in volume during the quarter owing to nationwide lockdowns in the last two weeks of March. Volume of plastic piping, packaging, industrial products and consumer products segments declined 7.4% y-o-y, 17.6% y-o-y, 13% y-o-y and 14% y-o-y respectively. The management indicated that there would be no degrowth in consumer products and packaging volume if it had no lockdown restrictions.
- **Realisations improved:** Blended realisations improved 2.4% y-o-y during the quarter after last three consecutive quarters of fall. Relaisations of plastic piping and consumer products improved 7.3% y-o-y and 15.5% y-o-y during the quarter, while realisations of packaging and industrial products continued to fall 5.7% y-o-y and 10.3% respectively. Management highlighted that price gap between the company's products and competitor's products have not narrowed down owing to the superior quality of products manufactured by SIL.
- **Outlook on raw-material prices:** Raw material prices have started showing an increasing trend after reaching to the bottoms in March except PVC Resin. Overall, it is expected that raw material prices shall remain range bound and affordable.
- **Segment performance in FY2019:** Plastic pipe business grew by 8% in volume and 9% in value terms. Packaging product business de-grew by 2% in volume and 8% in value terms. Industrial product business de-grew by 13% in volume and 24% in value terms. Consumer products segment business de-grew by 3% in volume and 4% in value terms.

- **Results excluding construction business:** After excluding construction business, the company reported revenue of Rs. 1,412 crore and EBITDA of Rs. 276 crore. The company sold real estate assets of 10,000 sq. feet during the quarter.
- **Good growth in value-added products:** Revenue from value-added products grew by 6% y-o-y to Rs.2,070 crore in FY2020.
- **Suspended annual guidance:** Management suspended providing annual volume growth and margin guidance for FY2021E owing to uncertainties in the view of COVID-19. The management has indicated that current margin level is not sustainable in coming quarters.
- **Net borrowing:** Total net borrowing stood at Rs. 217 crore in FY2020 as against Rs. 162 crore in FY2019. Average cost of borrowings in FY2020 increased to 8.35 % p.a. as against 8.23 % p.a. in FY2019.
- **Addressed issues in Bangladesh:** The Company addressed and settled the issues regarding the complaints of Composite cylinders from Bangladesh in FY2020. The newly designed product in composite cylinder segment has been successfully tested by customer in Bangladesh. The company expects good business volume from this customer in FY2021E.
- **Capex:** The company has incurred capex of Rs. 241 crore in FY2020 and further committed Capex of about Rs.182 Crs to set up new production units and expansion of capacity in existing facilities. The company has capex plans in the range Rs. 150-200 crore for FY2021.

Results Rs cr

Particulars	Q4FY20	Q4FY19	y-o-y (%)	Q3FY20	q-o-q (%)
Net sales	1,430.5	1,530.9	-6.6%	1,373.3	4.2%
Total expenditure	1,157.1	1,328.9	-12.9	1,152.4	0.4
EBITDA	**273.4**	**202.0**	**35.4**	**220.9**	**23.8**
Depreciation	52.9	48.1	9.8	51.5	2.6
EBIT	**220.6**	**153.9**	**43.4**	**169.4**	**30.2**
Other income	0.1	3.1	-98.1	0.8	-92.5
Interest expenses	4.2	6.4	-34.4	5.7	-25.5
PBT	**216.4**	**150.5**	**43.8**	**164.5**	**31.5**
Tax expenses	106.1	48.9	117.2	41.9	153.2
Share of profit from association	-7.0	-11.1	-37.2	-0.8	817.1
Adjusted net profit	**117.3**	**124.1**	**-5.5**	**123.4**	**-5.0**
Adjusted EPS (Rs.)	9.2	8.9	4.0	9.7	-5.0
Margins (%)			**BPS**		**BPS**
EBITDA margin	19.1	13.2	590	16.1	300
PAT margin	8.2	7.4	80	9.0	-80

Source: Company; Sharekhan Research

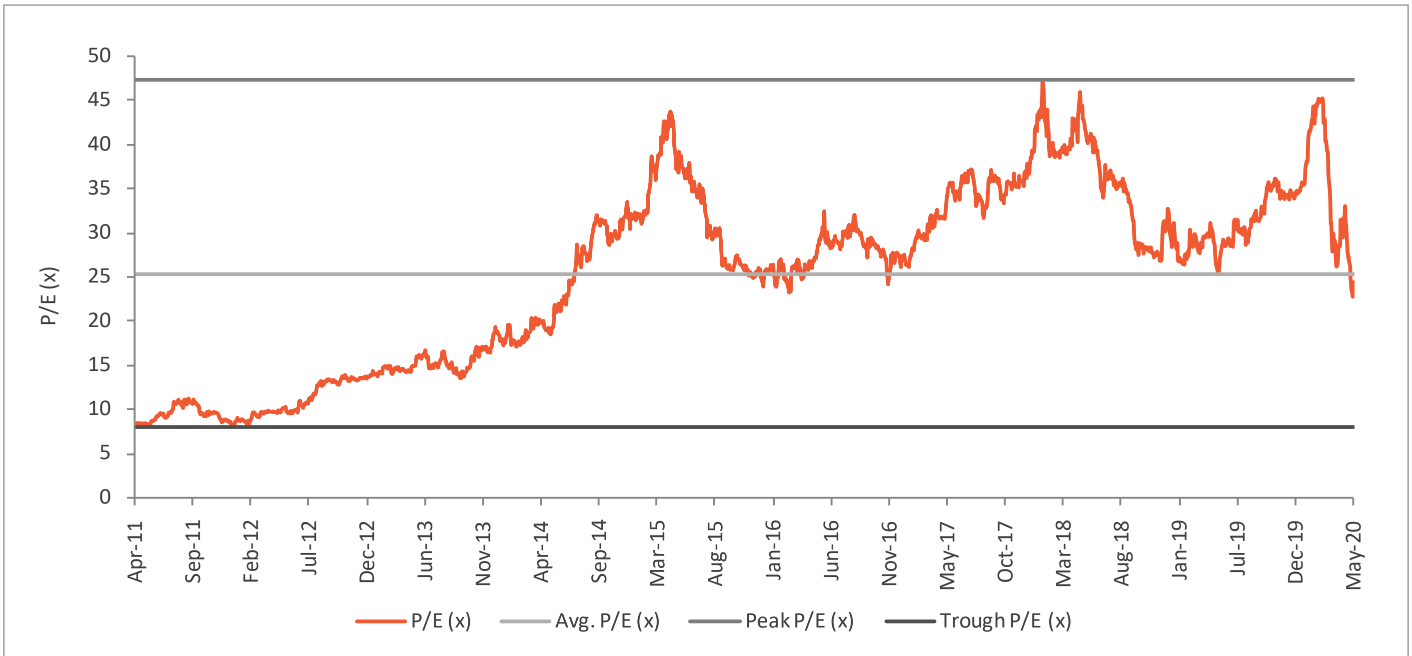
Outlook

Expect normalization of growth in FY2022E: We expect washout 1HFY2021 owing to lower demand environment (usually March-June is strong period for the company) since the nationwide lockdown restrictions and sharp fall in PVC prices (the company has passed the benefits to the customers). Though demand for agri pipes remains strong as farmers are getting funds quickly from the government, the demand for affordable housing and infrastructure will remain weak due to a nationwide lockdown and migrant labor issues. Even though FY2021E is going to be a weak year, we gradual recovery of growth in FY2022E on account of pick-up in demand led by higher demand in the housing segment and infrastructure and upcoming opportunities in 'Nal se Jal' scheme. Margin is expected to decline in FY2021 owing to higher inventory loss (sharp fall in PVC prices), lower revenue and reduction in discretionary spends (especially in SILPAULIN). We expect margin to improve in FY2022 on the back of a recovery in revenue growth in plastic piping segment and transport benefits from setting up plants in eastern part of India.

Valuation

We have fine-tuned our earnings estimates for FY2021/FY2022E factoring in Q4FY2020 performance and weak demand environment for plastic piping segment in affordable housing and infrastructure.We remain Positive on SIL for the long term, given the recovery in rural economy, affordable housing sector and the new scheme for piped water connection – 'Nal se Jal'. Even though FY2021E is going to be a weak year, we expect gradual recovery of growth in FY2022E on account of pick-up in demand led by higher demand in the housing segment and infrastructure and upcoming opportunities in 'Nal se Jal' scheme. The stock price has corrected more than 40% from the peak over last four months. At CMP, the stock is currently trading at 34x/26x FY2021E/FY2022E, implies `20% discount to one year average 1-year forward valuation. Hence, we retain our Buy rating on the stock with an SoTP price target (PT) of Rs. 1,120.

One-year forward P/E (x) band



Source: Sharekhan Research

About company

SIL is a leading manufacturer of plastic products with a significant presence across piping, packaging, industrial and consumer segments. The company has emerged as one of the best proxy plays on the growing plastic consumption in India because of a diversified product portfolio, an extensive distribution network, improved capital structure and government thrust on building a better infrastructure.

Investment theme

SIL is on a firm footing, with a strong product portfolio and new product launches, which are expected to drive growth in the coming years. The government's thrust on affordable housing and enhanced allocation towards irrigation projects will aid future growth for the companies such as SIL.We remain positive on the introduction of value-added products and capacity expansion plans, which are largely funded by robust internal accruals. SIL enjoys superior return ratios with low gearing levels, and we expect the company to maintain high return ratios going forward.

Key Risks

Slowdown in demand offtake from the user industry can impact revenue growth rates. Adverse commodity price fluctuation might impact margin profile.

Additional Data

Key management personnel

Bajranglal Surajmal Taparia	Non Executive Chairman
Mahavirprasad Surajmal Taparia	Executive Director
Shivratan Jeetmal Taparia	Executive Director
Vijaykumar Bajranglal Taparia	Executive Director
P C Somani	Chief Finance Officer
Rajendra J Saboo	AVP (Corporate Affairs) & Company Secretary & Compliance Officer

Source: Bloomberg

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Nalanda India Fund Ltd	4.81
2	Axis Asset Management Co Ltd/India	3.90
3	JPMorgan Chase & Co	3.48
4	Kotak Mahindra Asset Management Co	3.05
5	HDFC Asset Management Co Ltd	2.38
6	L&T Mutual Fund Tustee Ltd/India	2.31
7	DSP Investment Managers Pvt Ltd	1.90
8	Norges bank	1.48
9	GOVERNMENT PENSION FUND - GLOBAL	1.47
10	IDFC Mutual Fund/India	0.88

Source: Bloomberg

Sharekhan

by BNP PARIBAS

Know more about our products and services

For Private Circulation only

Disclaimer: This document has been prepared by Sharekhan Ltd. (SHAREKHAN) and is intended for use only by the person or entity to which it is addressed to. This Document may contain confidential and/or privileged material and is not for any type of circulation and any review, retransmission, or any other use is strictly prohibited. This Document is subject to changes without prior notice. This document does not constitute an offer to sell or solicitation for the purchase or sale of any financial instrument or as an official confirmation of any transaction. Though disseminated to all customers who are due to receive the same, not all customers may receive this report at the same time. SHAREKHAN will not treat recipients as customers by virtue of their receiving this report.

The information contained herein is obtained from publicly available data or other sources believed to be reliable and SHAREKHAN has not independently verified the accuracy and completeness of the said data and hence it should not be relied upon as such. While we would endeavour to update the information herein on reasonable basis, SHAREKHAN, its subsidiaries and associated companies, their directors and employees ("SHAREKHAN and affiliates") are under no obligation to update or keep the information current. Also, there may be regulatory, compliance, or other reasons that may prevent SHAREKHAN and affiliates from doing so. This document is prepared for assistance only and is not intended to be and must not alone be taken as the basis for an investment decision. Recipients of this report should also be aware that past performance is not necessarily a guide to future performance and value of investments can go down as well. The user assumes the entire risk of any use made of this information. Each recipient of this document should make such investigations as it deems necessary to arrive at an independent evaluation of an investment in the securities of companies referred to in this document (including the merits and risks involved), and should consult its own advisors to determine the merits and risks of such an investment. The investment discussed or views expressed may not be suitable for all investors. We do not undertake to advise you as to any change of our views. Affiliates of Sharekhan may have issued other reports that are inconsistent with and reach different conclusions from the information presented in this report.

This report is not directed or intended for distribution to, or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject SHAREKHAN and affiliates to any registration or licensing requirement within such jurisdiction. The securities described herein may or may not be eligible for sale in all jurisdictions or to certain category of investors. Persons in whose possession this document may come are required to inform themselves of and to observe such restriction.

The analyst certifies that the analyst has not dealt or traded directly or indirectly in securities of the company and that all of the views expressed in this document accurately reflect his or her personal views about the subject company or companies and its or their securities and do not necessarily reflect those of SHAREKHAN. The analyst further certifies that neither he or its associates or his relatives has any direct or indirect financial interest nor have actual or beneficial ownership of 1% or more in the securities of the company at the end of the month immediately preceding the date of publication of the research report nor have any material conflict of interest nor has served as officer, director or employee or engaged in market making activity of the company. Further, the analyst has also not been a part of the team which has managed or co-managed the public offerings of the company and no part of the analyst's compensation was, is or will be, directly or indirectly related to specific recommendations or views expressed in this document. Sharekhan Limited or its associates or analysts have not received any compensation for investment banking, merchant banking, brokerage services or any compensation or other benefits from the subject company or from third party in the past twelve months in connection with the research report.

Either SHAREKHAN or its affiliates or its directors or employees / representatives / clients or their relatives may have position(s), make market, act as principal or engage in transactions of purchase or sell of securities, from time to time or may be materially interested in any of the securities or related securities referred to in this report and they may have used the information set forth herein before publication. SHAREKHAN may from time to time solicit from, or perform investment banking, or other services for, any company mentioned herein. Without limiting any of the foregoing, in no event shall SHAREKHAN, any of its affiliates or any third party involved in, or related to, computing or compiling the information have any liability for any damages of any kind.

Compliance Officer: Mr. Joby John Meledan; Tel: 022-61150000; email id: compliance@sharekhan.com;

For any queries or grievances kindly email igc@sharekhan.com or contact: myaccount@sharekhan.com

Registered Office: Sharekhan Limited, 10th Floor, Beta Building, Lodha iThink Techno Campus, Off. JVLR, Opp. Kanjurmarg Railway Station, Kanjurmarg (East), Mumbai – 400042, Maharashtra. Tel: 022 - 61150000. Sharekhan Ltd.: SEBI Regn. Nos.: BSE / NSE / MSEI (CASH / F&O / CD) / MCX - Commodity: INZ000171337; DP: NSDL/CDSL-IN-DP-365-2018; PMS: INP000005786; Mutual Fund: ARN 20669; Research Analyst: INH000006183;