

22 July 2020

Polycab, India

Strongly placed in a tough FY21; retaining a Buy

Rating: **Buy**

Target Price: ₹945

Share Price: ₹820

Polycab's weak Q1 was operationally in line with our estimates. B2C/tier 1-2 markets did better than B2B/metros. While FY21 will be tough, strategic steps to improve working capital and cost optimisation will offer long-run benefits. We remain positive on Polycab, given its leadership in the fast-growing C&W (incl. exports), wide distribution network, strong management and healthy balance sheet. Thus, we maintain a Buy with a target of ₹945 (17x/20x FY22e P/Es for C&W/FMEG), earlier ₹884. Profitable growth in FMEG will support a re-rating.

Weak, but operationally in line Q1. Revenue/EBITDA/PBT/PAT fell 50%/74%/80%/13% y/y because of all segments. Lower revenues impacted EBITDA margin (5.9% vs. 12.9% in FY20). Tax write-back related items (₹1bn) and a ₹97m gain on the Rayker consolidation helped to a lesser PAT decline. Otherwise, adj. PAT came at a meagre ₹75m (down 94% y/y). Despite this, net cash improved to ₹2.1bn after the release of WC since Apr.

Exports/wires/FMEG did better in Q1. While institutional supplies fell 80% y/y in Q1, the B2C segment (wires, FMEG) saw better traction with revenue share at 43% (vs. 35%). Revenues from tier 1-2 markets were higher at 55% (vs 40%) while metros were subdued. Exports, up 116% y/y, at ~₹1bn was without Dangote order (to be completed in the next 1-2 quarters).

Strategic moves to aid long-term sustainable growth. Focus on working capital management (inventory reduction, channel financing) and cost optimisation are a few strategic moves to keep Polycab on the sustainable growth path in the long run. ₹2bn capex in building capacities and technology upgrading, even in a tough FY21, is a testimonial to this.

Tough FY21, long-term prospects persist though. Over FY15-20, Polycab's revenue/PAT registered 13%/36% CAGRs. After a weak FY21, we expect a strong FY22 with return ratios returning to healthy levels. Despite short-term hiccups, the company's long-term prospects are bright.

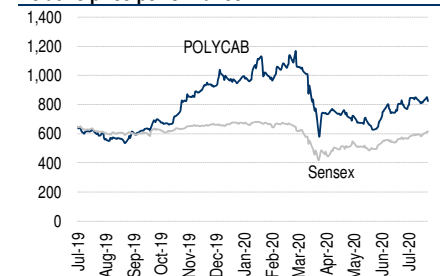
Valuation. We maintain a Buy on Polycab, with a revised target of ₹945. **Key risks:** Volatile raw-material prices, slowdown in government spend on infra.

| Key data | POLYCAB IN |
|--------------------|--------------------|
| 52-week high / low | ₹1182 / 525 |
| Sensex / Nifty | 37872 / 11133 |
| 3-m average volume | \$3.5m |
| Market cap | ₹123bn / \$1642.1m |
| Shares outstanding | 149m |

| Shareholding pattern (%) | Jun'20 | Mar'20 | Dec'19 |
|--------------------------|--------|--------|--------|
| Promoters | 68.6 | 68.6 | 68.6 |
| - of which, Pledged | - | - | - |
| Free float | 31.5 | 31.4 | 31.4 |
| - Foreign institutions | 4.5 | 4.9 | 4.6 |
| - Domestic institutions | 12.9 | 13.2 | 13.4 |
| - Public | 14.0 | 13.3 | 13.4 |

| Estimates revision (%) | FY21e | FY22e |
|------------------------|-------|-------|
| Sales | (1) | 1 |
| EBITDA | 8 | 1 |
| PAT | 34 | 1 |

Relative price performance



Source: Bloomberg

| Key financials (YE Mar) | FY18 | FY19 | FY20 | FY21e | FY22e |
|-------------------------|--------|--------|--------|--------|---------|
| Sales (₹ m) | 67,703 | 79,560 | 88,300 | 71,277 | 102,683 |
| Net profit (₹ m) | 3,525 | 5,003 | 7,717 | 5,432 | 8,070 |
| EPS (₹) | 25.0 | 35.4 | 51.8 | 36.5 | 54.3 |
| PE (x) | 33.0 | 23.3 | 15.9 | 22.6 | 15.2 |
| EV / EBITDA (x) | 17.2 | 12.5 | 10.1 | 14.0 | 8.8 |
| PBV (x) | 5.0 | 4.1 | 3.0 | 2.6 | 2.4 |
| RoE (%) | 15.0 | 17.6 | 20.1 | 12.1 | 16.3 |
| RoCE (%) after tax | 13.7 | 18.8 | 17.6 | 9.3 | 14.4 |
| Dividend yield (%) | 0.1 | 0.4 | 0.8 | 0.6 | 1.2 |
| Net debt / equity (x) | 0.3 | -0.0 | -0.1 | -0.2 | -0.1 |

Source: Company, Anand Rathi Research

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Quick Glance – Financials and Valuations (Consol.)

Fig 1 – Income statement (₹ m)

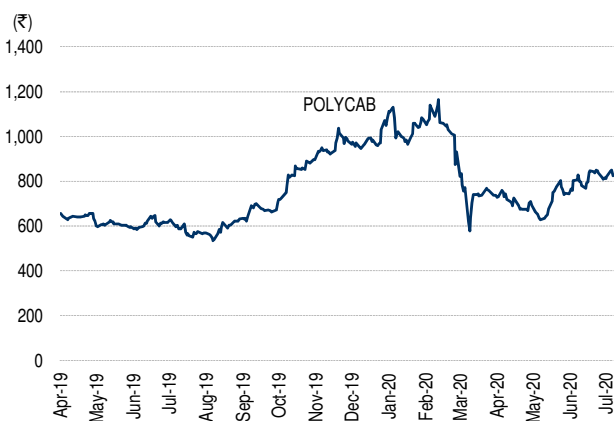
| Year-end: Mar | FY18 | FY19 | FY20 | FY21e | FY22e |
|-----------------------------|--------------|--------------|---------------|--------------|---------------|
| Net revenues | 67,703 | 79,560 | 88,300 | 71,277 | 102,683 |
| Growth (%) | 23.1 | 17.5 | 11.0 | (19.3) | 44.1 |
| Direct costs | 50,894 | 57,117 | 63,686 | 52,391 | 75,254 |
| SG&A | 9,608 | 13,211 | 13,263 | 11,177 | 14,919 |
| EBITDA | 7,201 | 9,232 | 11,350 | 7,709 | 12,510 |
| EBITDA margins (%) | 10.6 | 11.6 | 12.9 | 10.8 | 12.2 |
| - Depreciation | 1,330 | 1,414 | 1,609 | 1,789 | 1,837 |
| Other income | 644 | 933 | 928 | 636 | 440 |
| Interest expenses | 937 | 1,167 | 495 | 418 | 290 |
| PBT | 5,579 | 7,584 | 10,174 | 6,138 | 10,823 |
| Effective tax rate (%) | 36.8 | 33.7 | 24.0 | 11.4 | 25.5 |
| + Associates / (Minorities) | - | - | - | - | - |
| Net income | 3,525 | 5,003 | 7,717 | 5,432 | 8,070 |
| Adjusted income | 3,525 | 5,003 | 7,717 | 5,432 | 8,070 |
| WANS | 141 | 141 | 149 | 149 | 149 |
| FDEPS (₹ / sh) | 25.0 | 35.4 | 51.8 | 36.5 | 54.3 |
| FDEPS growth (%) | 51.2 | 41.9 | 46.3 | (29.5) | 48.6 |
| Gross margins (%) | 24.8 | 28.2 | 27.9 | 26.5 | 26.7 |

Fig 3 – Cash-flow statement (₹ m)

| Year-end: Mar | FY18 | FY19 | FY20 | FY21e | FY22e |
|--------------------------------|-------|---------|---------|---------|---------|
| EBIT (before other income) | 5,872 | 7,817 | 9,741 | 5,920 | 10,673 |
| + Non-cash items | 1,330 | 1,414 | 1,609 | 1,789 | 1,837 |
| Oper. prof. before WC | 7,201 | 9,232 | 11,350 | 7,709 | 12,510 |
| - Incr. / (decr.) in WC | 3,443 | (5,167) | 6,363 | (422) | 5,052 |
| Others incl. taxes | 1,056 | 3,083 | 3,726 | 1,596 | 3,653 |
| Operating cash-flow | 2,702 | 11,316 | 1,261 | 6,534 | 3,805 |
| - Capex (tang. + intang.) | 1,728 | 2,769 | 3,555 | 2,000 | 2,300 |
| Free cash-flow | 974 | 8,547 | (2,294) | 4,534 | 1,505 |
| Acquisitions | | | | | |
| - Div. (incl. buyback & taxes) | 169 | 508 | 1,251 | 892 | 1,784 |
| + Equity raised | - | - | 77 | - | - |
| + Debt raised | (931) | (5,357) | (699) | 20 | - |
| - Fin investments | (13) | (22) | 361 | 6,990 | (2,010) |
| - Misc. (CFI + CFF) | 82 | (357) | (4,174) | (2,570) | 1,147 |
| Net cash-flow | (195) | 3,060 | (354) | (760) | 584 |

Source: Company, Anand Rathi Research

Fig 5 – Price movement



Source: Bloomberg

Fig 2 – Balance sheet (₹ m)

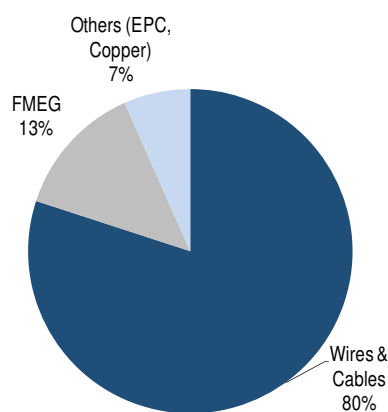
| Year-end: Mar | FY18 | FY19 | FY20 | FY21e | FY22e |
|--------------------------|---------------|---------------|---------------|---------------|---------------|
| Share capital | 1,412 | 1,412 | 1,489 | 1,486 | 1,486 |
| Net worth | 23,476 | 28,470 | 38,364 | 44,828 | 49,369 |
| Debt | 7,277 | 1,920 | 1,221 | 1,241 | 1,241 |
| Minority interest | 40 | 84 | 150 | 195 | 254 |
| DTL / (Assets) | 553 | 231 | 175 | 165 | 155 |
| Capital employed | 31,347 | 30,705 | 39,910 | 46,429 | 51,018 |
| Net tangible assets | 11,944 | 12,721 | 13,865 | 14,272 | 14,930 |
| Net intangible assets | 27 | 35 | 355 | 360 | 365 |
| Goodwill | - | - | - | - | - |
| CWIP (tang. & intang.) | 1,360 | 1,930 | 2,412 | 2,212 | 2,012 |
| Investments (strategic) | 314 | 294 | 255 | 245 | 235 |
| Investments (financial) | 1 | - | 400 | 7,400 | 5,400 |
| Current assets (ex cash) | 30,728 | 38,137 | 39,516 | 37,038 | 47,562 |
| Cash | 106 | 3,166 | 2,813 | 2,053 | 2,637 |
| Current liabilities | 13,134 | 25,578 | 19,706 | 17,149 | 22,122 |
| Working capital | 17,594 | 12,558 | 19,810 | 19,888 | 25,440 |
| Capital deployed | 31,347 | 30,705 | 39,910 | 46,429 | 51,018 |
| Contingent liabilities | 5,269 | 4,309 | 3,477 | - | - |

Fig 4 – Ratio analysis

| Year-end: Mar | FY18 | FY19 | FY20 | FY21e | FY22e |
|---------------------------------|------|-------|-------|-------|-------|
| P/E (x) | 33.0 | 23.3 | 15.9 | 22.6 | 15.2 |
| EV / EBITDA (x) | 17.2 | 12.5 | 10.1 | 14.0 | 8.8 |
| EV / Sales (x) | 1.8 | 1.4 | 1.3 | 1.5 | 1.1 |
| P/B (x) | 5.0 | 4.1 | 3.0 | 2.6 | 2.4 |
| RoE (%) | 15.0 | 17.6 | 20.1 | 12.1 | 16.3 |
| RoCE (%) - after tax | 13.7 | 18.8 | 17.6 | 9.3 | 14.4 |
| ROIC | 13.8 | 19.7 | 25.1 | 14.3 | 17.9 |
| DPS (₹ / sh) | 1.0 | 3.0 | 7.0 | 5.0 | 10.0 |
| Dividend yield (%) | 0.1 | 0.4 | 0.8 | 0.6 | 1.2 |
| Dividend payout (%) - incl. DDT | 4.0 | 8.5 | 13.5 | 13.7 | 18.4 |
| Net debt / equity (x) | 0.3 | (0.0) | (0.1) | (0.2) | (0.1) |
| Receivables (days) | 74.3 | 67.4 | 66.1 | 75.0 | 65.0 |
| Inventory (days) | 73.6 | 91.6 | 79.6 | 90.0 | 85.0 |
| Payables (days) | 49.7 | 69.7 | 56.0 | 55.0 | 55.0 |
| CFO : PAT % | 76.7 | 226.2 | 16.3 | 120.3 | 47.1 |

Source: Company, Anand Rathi Research

Fig 6 – Segment-wise revenue break-up (Q1 FY21)



Source: Company

Financial highlights

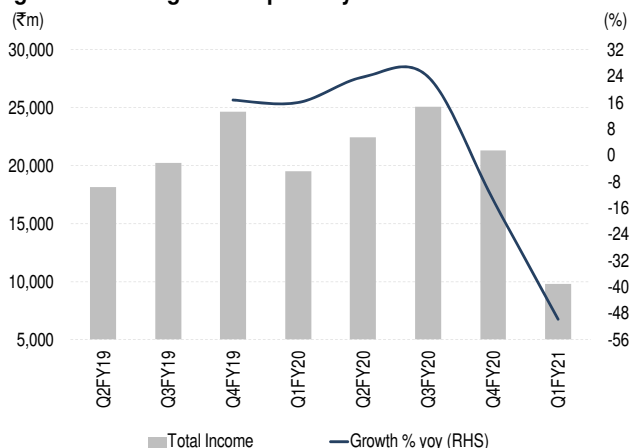
Fig 7 – Financials (consol.)

| ₹ m) | Q1 FY20 | Q2 FY20 | Q3 FY20 | Q4 FY20 | Q1 FY21 | % Y/Y | % Q/Q | FY20 | FY19 | % Y/Y |
|-------------------------------|---------------|---------------|---------------|---------------|---------------|----------------|----------------|---------------|---------------|----------------|
| Total Income | 19,513 | 22,419 | 25,073 | 21,294 | 9,766 | (50) | (54) | 88,300 | 79,830 | 11 |
| Raw material costs | 14,278 | 16,449 | 18,190 | 14,769 | 7,097 | (50) | (52) | 63,686 | 59,660 | 7 |
| Employee costs | 920 | 924 | 915 | 899 | 812 | (12) | (10) | 3,657 | 3,002 | 22 |
| Other expenses | 2,079 | 2,329 | 2,577 | 2,620 | 1,282 | (38) | (51) | 9,606 | 7,666 | 25 |
| EBITDA | 2,236 | 2,717 | 3,391 | 3,006 | 575 | (74) | (81) | 11,350 | 9,502 | 19 |
| Depreciation | 385 | 395 | 407 | 422 | 443 | 15 | 5 | 1,609 | 1,414 | 14 |
| Finance costs | 123 | 127 | 86 | 159 | 163 | 32 | 2 | 495 | 1,167 | (58) |
| Other income | 336 | 124 | 3 | 465 | 336 | 0 | (28) | 928 | 664 | 40 |
| Exceptional items | - | - | - | - | 97 | - | - | - | - | - |
| PBT | 2,064 | 2,319 | 2,902 | 2,889 | 403 | (80) | (86) | 10,174 | 7,584 | 34 |
| Tax | 713 | 365 | 686 | 680 | (785) | (210) | (215) | 2,444 | 2,558 | (4) |
| PAT | 1,353 | 1,938 | 2,214 | 2,151 | 1,176 | (13) | (45) | 7,656 | 5,003 | 53 |
| EPS (₹) | 9.1 | 13.0 | 14.9 | 14.5 | 7.9 | (13) | (45) | 51.4 | 33.6 | 53 |
| As % of total Income | | | | | | bps y/y | bps q/q | | | Bps y/y |
| Gross margin | 26.8 | 26.6 | 27.5 | 30.6 | 27.3 | 50 | (331) | 27.9 | 25.3 | 261 |
| Employee costs | 4.7 | 4.1 | 3.6 | 4.2 | 8.3 | 360 | 410 | 4.1 | 3.8 | 38 |
| Other expenses | 10.7 | 10.4 | 10.3 | 12.3 | 13.1 | 247 | 82 | 10.9 | 9.6 | 128 |
| EBITDA margin | 11.5 | 12.1 | 13.5 | 14.1 | 5.9 | (557) | (823) | 12.9 | 11.9 | 95 |
| Depreciation | 2.0 | 1.8 | 1.6 | 2.0 | 4.5 | 256 | 255 | 1.8 | 1.8 | 5 |
| Other income | 1.7 | 0.6 | 0.0 | 2.2 | 3.4 | 172 | 126 | 1.1 | 0.8 | 22 |
| Finance costs | 0.6 | 0.6 | 0.3 | 0.7 | 1.7 | 104 | 92 | 0.6 | 1.5 | (90) |
| PBT | 1.7 | 0.6 | 0.0 | 2.2 | 3.4 | 172 | 126 | 1.1 | 0.8 | 22 |
| Effective tax rate | 34.6 | 15.7 | 23.6 | 23.5 | (194.9) | | | 24.0 | 33.7 | (970) |
| PAT | 6.9 | 8.7 | 8.8 | 10.4 | 12.2 | 524 | 178 | 8.8 | 6.3 | 246 |
| Segment revenues (₹ m) | | | | | | % Y/Y | % Q/Q | | | % Y/Y |
| Wires & Cables | 16,375 | 19,222 | 21,696 | 18,605 | 8,252 | (50) | (56) | 75,898 | 70,643 | 7 |
| FMEG | 2,401 | 1,956 | 2,166 | 1,833 | 1,378 | (43) | (25) | 8,356 | 6,433 | 30 |
| Others | 1,226 | 1,638 | 1,510 | 1,592 | 684 | (44) | (57) | 5,965 | 4,637 | 29 |
| Total | 20,001 | 22,816 | 25,373 | 22,030 | 10,314 | (48) | (53) | 90,219 | 81,713 | 10 |
| Less: Inter segment revenue | 271 | 410 | 398 | 362 | 424 | 57 | 17 | 1,441 | 1,348 | 7 |
| Total revenue | 19,730 | 22,406 | 24,975 | 21,668 | 9,889 | (50) | (54) | 88,778 | 80,365 | 10 |
| Segment EBIT (%) | | | | | | bps y/y | bps q/q | | | bps y/y |
| Wires & Cables | 11.4 | 10.5 | 11.9 | 15.2 | 3.0 | (841) | (1,224) | 12.2 | 11.8 | 42 |
| FMEG | 3.7 | 3.3 | 0.6 | 0.1 | (4.0) | (769) | (410) | 2.0 | 1.2 | 86 |
| Others | 9.7 | 16.0 | 22.4 | 10.4 | 10.1 | 42 | (25) | 14.8 | 4.3 | 1,056 |
| Total | 10.3 | 10.3 | 11.6 | 13.7 | 2.6 | (772) | (1,107) | 11.5 | 10.7 | 74 |

Source: Company, Anand Rathi Research

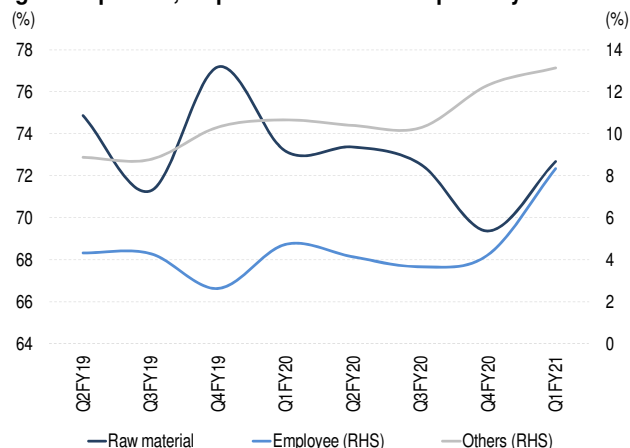
* Note: Segment EBIT margin is as per reported numbers and not adjusted for the un-allocable expenses/income

Fig 8 – Revenue growth - quarterly trend



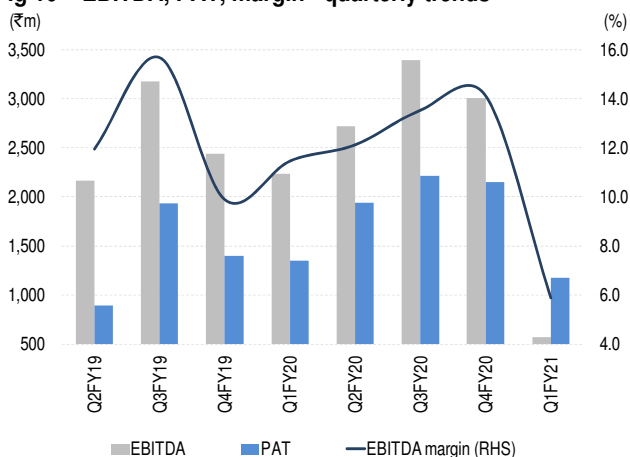
Source: Company, Anand Rathi Research

Fig 9 – Expenses, as percent of income – quarterly trend



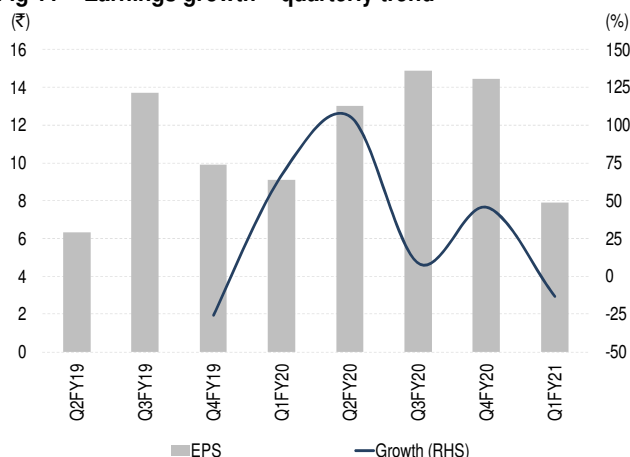
Source: Company, Anand Rathi Research

Fig 10 – EBITDA, PAT, margin - quarterly trends



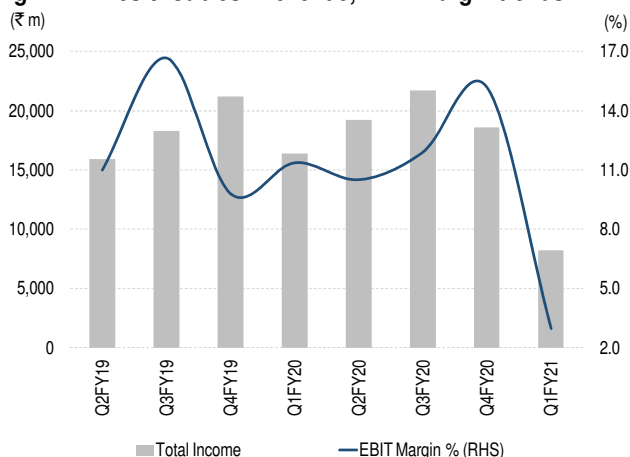
Source: Company, Anand Rathi Research

Fig 11 – Earnings growth – quarterly trend



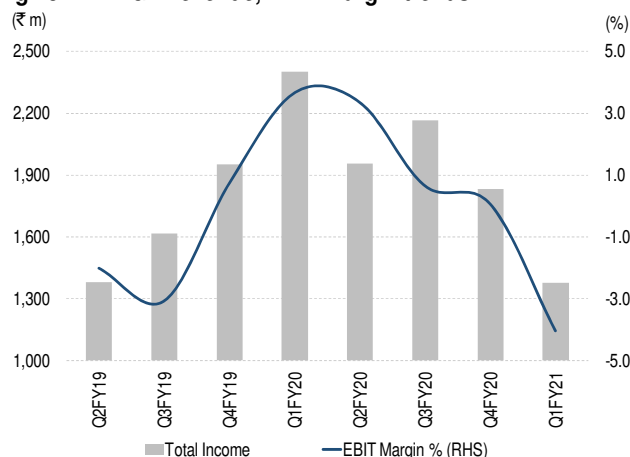
Source: Company, Anand Rathi Research

Fig 12 – Wires & Cables – revenue, EBIT-margin trends



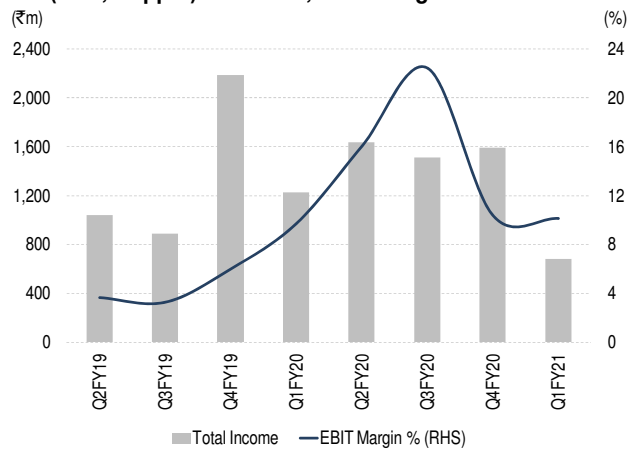
Source: Company, Anand Rathi Research

Fig 13 – FMEG – revenue, EBIT-margin trends



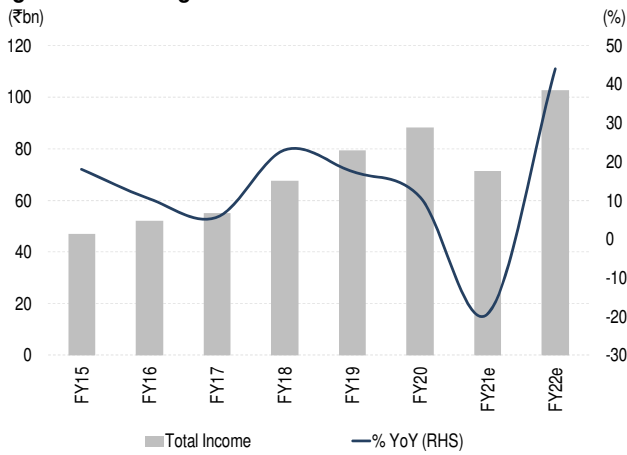
Source: Company, Anand Rathi Research

Fig 14 – Others (EPC, Copper) – revenue, EBIT-margin trends



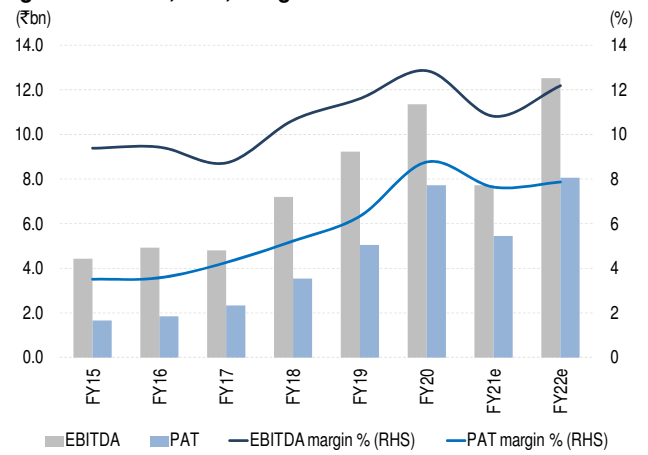
Source: Company, Anand Rathi Research

Fig 15 – Revenue growth – annual trend



Source: Company, Anand Rathi Research

Fig 16 – EBITDA, PAT, margin – annual trends



Source: Company, Anand Rathi Research

Valuation

After becoming the leader in wires & cables, in 2015 Polycab entered FMEG. We like it for its large manufacturing base, all-India distribution reach, induction of professional management, strong promoter family and focus on cash-flow. We believe all these factors, and its efforts to re-position itself as a consumer company, would drive a stock re-rating.

Over FY15-20, revenue/EBITDA/PAT registered 13%/21%/36% CAGRs. After anticipating a weak FY21, we now expect 8%/5%/2% CAGRs over FY20-22 with the RoE touching a healthy ~16% and FCF continuing.

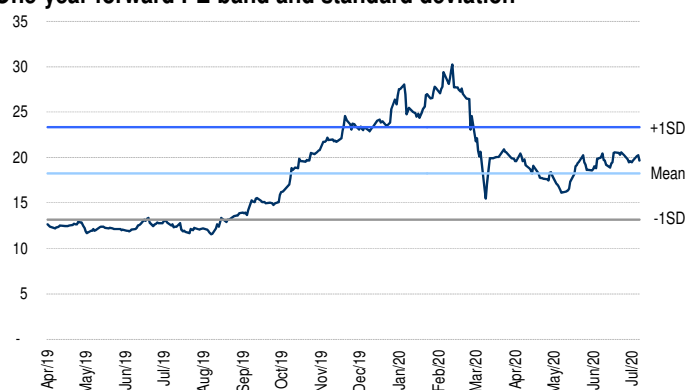
While short-term challenges to growth persist, we are upbeat about Polycab's long-term prospects in W&C, strong growth in FMEGs and a healthy balance sheet. Thus, we maintain a Buy, with a higher target price of ₹945 (17x/20x FY22e P/Es for W&C/FMEG), earlier ₹884. To its FMEG business we assign a lower multiple than to those of leading players due to its smaller size and weaker operating matrices. However, a strong re-rating is possible if it delivers strong profitable growth in coming years.

Fig 17 – Change in estimates

| ₹(m) | Old estimates | | New estimates | | % Var | |
|-----------------|---------------|---------|---------------|---------|-------|-------|
| | FY21e | FY22e | FY21e | FY22e | FY21e | FY22e |
| Total Income | 71,644 | 102,018 | 71,277 | 102,683 | (1) | 1 |
| EBITDA | 7,122 | 12,381 | 7,709 | 12,510 | 8 | 1 |
| EBITDA margin % | 9.9 | 12.1 | 10.8 | 12.2 | | |
| PAT | 4,068 | 8,027 | 5,432 | 8,070 | 34 | 1 |

Source: Anand Rathi Research

Fig 18 – One-year forward PE-band and standard deviation



Source: Bloomberg, Anand Rathi Research

Risks

- Volatile raw-material prices:** Copper and aluminium are key raw materials in W&C, constituting ~70% of costs. Any substantial volatility in raw-material prices would lead to operating-margin fluctuations and, thus, pose a key risk to our estimates.
- Slowdown in government's infra push:** The government's push to infra has been a key growth driver for W&C in the past few years. Hence, any slowdown in government spending on infra could significantly cut into Polycab's growth, especially given its huge investment in capacity and branding.

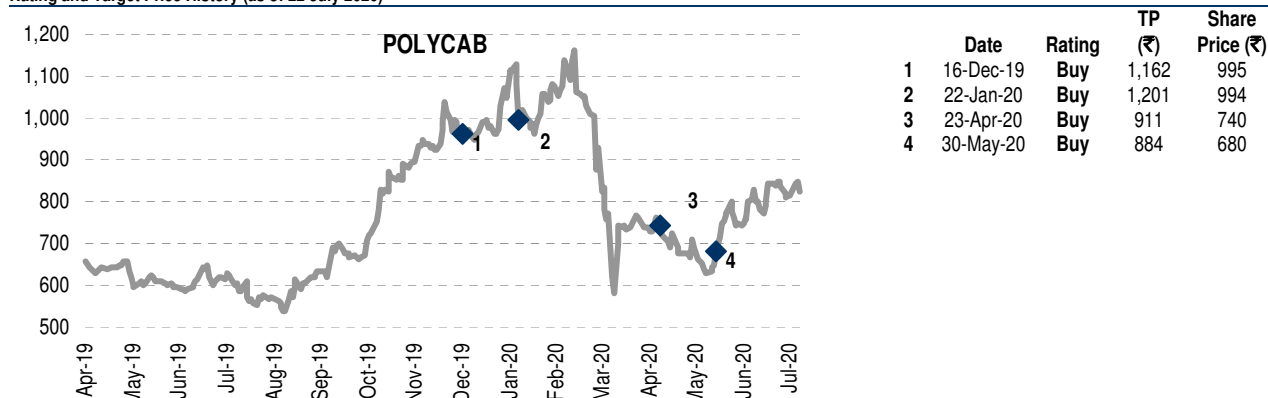
Appendix

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Rating and Target Price History (as of 22 July 2020)



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| | Buy | Hold | Sell |
|---------------------------|------|-------|------|
| Large Caps (>US\$1bn) | >15% | 5-15% | <5% |
| Mid/Small Caps (<US\$1bn) | >25% | 5-25% | <5% |

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