

Sector: Capital Goods  
Results Update

	Change
Reco: <b>Buy</b>	↑
CMP: <b>Rs. 295</b>	
Price Target: <b>Rs. 360</b>	↑
↑ Upgrade   ← No change   ↓ Downgrade	

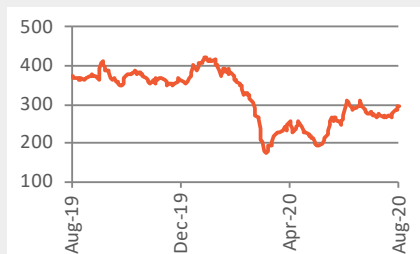
## Company details

Market cap:	Rs. 4,507 cr
52-week high/low:	Rs. 433/165
NSE volume: (No of shares)	1.4 lakh
BSE code:	500144
NSE code:	FINCABLES
Sharekhan code:	FINCABLES
Free float: (No of shares)	9.8 cr

## Shareholding (%)

Promoters	35.9
FII	7.0
DII	19.8
Others	37.3

## Price chart



## Price performance

(%)	1m	3m	6m	12m
Absolute	-3	51	-18	-21
Relative to Sensex	-6	27	-11	-24

Sharekhan Research, Bloomberg

Finolex Cables reported better than expected numbers during Q1FY2021 despite effectively operating for only about a month during the quarter. Its standalone revenues declined by 63% y-o-y to Rs. 377 crore (but was higher than estimate) as factory operations gradually resumed from May 20, 2020, followed by channel partners. OPM contracted by 396 bps y-o-y to 9.2% (much better than estimates) owing to a dip in gross margins (as it doled out the entire 8% target-based incentives versus the normal of 6% to channel partners to support them and strengthen long-term relationships during the quarter). A dip in revenues and OPM led to a 57% y-o-y decline in net profit to Rs. 35 crore (but was higher than our estimate). The company operated on an average 40% capacity utilisation which has now crossed 50%. Its electric cable division (~70% revenue share) is seeing healthy demand from housing wire and agriculture cables. Demand for automobile cables picked from 10% to 30-40% of pre-COVID levels while telecom cables has seen demand for LAN and co-axial. The company expects demand for electric cables to normalise going ahead as labour, transport and supply chain issues get resolved. Communication cables (forming ~12% mix) is expected to be muted on account of funding issues from government (BSNL/BBNL). New products (~2-3% mix) are performing well and would have surpassed Q4FY2020 run-rate in Q1FY2021 if COVID-19 issue was not there. Finolex will continue its Rs. 200 crore capex plan at Urse and Goa over 18 months. Finolex has built a strong cash balance of Rs. 934 crore (excluding investments) as on FY2020 end. Healthy operating cash flow generation, tight working capital management (policy of advance payments from dealers) and limited capex are expected to further build upon its cash reserves. Consequently, it may look at inorganic growth opportunities in its allied business verticals. The company also has opportunity to increase market share organically as the pandemic has had a severe impact on unorganised sector players. We have fine-tuned our net earnings estimates for FY2021-FY2022E and introduced FY2023E earnings. Finolex is currently trading at a PE of 11.5x its FY2023E earnings which is at a 10-20% discount to its peers. Considering its improving growth outlook organically and opportunity for inorganic growth, we upgrade our rating on the stock to Buy with revised PT of Rs. 360.

## Key positives

- Strong cash balance apart from investment provides opportunity for inorganic growth.
- Target to reach 500 (from currently 388) distributors and 150,000 (currently 112,000) dealers still on track.
- Capex of Rs. 200 crore on track over next 18 months.

## Key negatives

- Overall volumes and demand remained at 50% due to COVID-19 impact.
- Slowdown in the industrial and real estate activity affected electrical business (as segment's revenues declined by 50% y-o-y).

## Our Call

**Valuation: Upgrade to Buy with revised PT of Rs. 360:** We believe Finolex has performed well despite the effect of COVID-19 on the quarter, maintaining relatively better OPM despite steep dip in revenues. The company's operations are further expected to improve post monsoon as labour, transportation and supply chain issues get settled. Meanwhile, it has built a strong cash balance to consider inorganic growth opportunities. The COVID-19 led impact on unorganized players provides the company to increase its market share. We have fine-tuned our net earnings estimates for FY2021-FY2022E and introduced FY2023E earnings. Finolex is currently trading at a PE of 11.5x its FY2023E earnings, which is at a 10-20% discount to its peers. Considering its improving growth outlook organically and opportunity for inorganic growth, we upgrade our rating on the stock to Buy with revised PT of Rs. 360.

## Key Risks

Fluctuations in raw-material prices could sharply affect margins.

## Valuation (standalone)

Particulars	FY20	FY21E	FY22E	FY23E
Revenue	2,877	2,498	2,851	3,280
OPM (%)	12.9	11.5	12.5	12.9
Adjusted PAT	402	268	330	390
% y-o-y growth	17.0	(33.4)	23.2	18.3
Adjusted EPS (Rs.)	26.3	17.5	21.6	25.5
P/E (x)	11.2	16.8	13.7	11.5
P/B (x)	1.7	1.5	1.4	1.3
EV/EBITDA (x)	6.6	8.8	7.1	6.0
RoNW (%)	18.6	11.8	14.6	16.1
RoCE (%)	19.5	12.7	14.4	15.6

Source: Company; Sharekhan estimates

**Results better than estimates:** Finolex Cables clocked better than expected performance during Q1FY2021 despite effectively operating for about a month during the quarter. Its standalone revenues declined by 63% y-o-y to Rs. 377 crore (but still was higher than estimates) as factory operations gradually resumed from May 20, 2020 followed by channel partners. Among segments, electric cables revenue declined by 50.2% y-o-y to Rs. 332 crore while those of communication cables segment clocked a decline of 75.3% y-o-y to Rs 27 crore, while the New Business (FMEG) revenues declined 32.7% y-o-y. Volumes decline was similarly across all product lines (~50% decline y-o-y). OPM contracted by 396 bps y-o-y to 9.2% (but was much better than estimate) owing to dip in gross margins (as it doled out entire 8% target based incentives versus normal 6% to channel partners to support during current environment and strengthen long term relationships). Dip in revenues and OPM led to a 57% y-o-y decline in net profit to Rs. 35 crore (much higher than our estimate). The company operated on an average 40% capacity utilisation which has now crossed 50%. Its Electric cable division (~70% revenue share) is seeing healthy demand from housing wire and agriculture cables. Auto cables demand picked from 10% to 30-40% of pre-COVID levels while telecom cables has seen demand for LAN and co-axial. The company expects electric cables to normalise going ahead as labour, transport and supply chain issues get resolved. Communication cables (forming ~12% of mix) is expected to be muted on account of funding issues from government (BSNL/BBNL). New products (~2-3% of mix) are performing well and would have surpassed Q4FY2020 run-rate in Q1FY2021 if COVID-19 issue was not there.

**Capex plans remain intact:** Finolex will continue its Rs. 200 crore capex plan at Urse and Goa to be spread over 18 months. Finolex has build strong cash balance of Rs. 934 crore (excluding investments) as on FY2020-end. Healthy operating cash flow generation, tight working capital management (policy of advance payments from dealers) and limited capex is expected to further add to its cash reserves.

### Key conference call highlights

- ◆ **Distribution network:** Target to reach 500 (currently 388) distributors and 150,000 (currently 112,000) dealers still on track.
- ◆ **Capacity utilisation:** Capacity utilisation improved m-o-m from 40% to more than 50% currently.
- ◆ **Inorganic growth opportunities:** Company looking at inorganic growth opportunities in its allied business verticals.
- ◆ **Current labour scenario:** While the permanent labourers have returned to factories, the company is facing some contract labourer issues but expected to improve as situation improves.
- ◆ **Capex plans:** The company plans to spend ~Rs. 200 crore in next 18 months. Wherein construction has Urse has commenced (Ebeam facility and other products and plant at Goa for conduit is ready, installation of machinery is pending).
- ◆ **Cost optimization initiatives:** Company has come up with several measures to contain costs and stated that it will reduce Rs. 40-45 crore from cost base over a period of time once these measures are implemented.
- ◆ **Dependence on China reduces:** Finolex used to get coating material for communication cables from China, for which it has developed a new source from Korea and are not dependent on china anymore.

Results (Standalone)					Rs cr
Particulars	Q1FY21	Q1FY20	YoY (%)	Q4FY20	QoQ (%)
Revenue	377.1	807.7	-53.3%	651	-42.1%
Operating profit	34.5	106.0	-67.4%	87	-60.3%
Other Income	22.5	22.0	2.3%	59	-61.7%
Interest	0.17	0.2	-22.7%	1	
Depreciation	10.0	9.9	1.2%	10	4.7%
PBT	46.8	117.9	-60.3%	136	-65.4%
Tax	11.9	36.3	-67.3%	18	-35.4%
EO	-	-		-	
Reported PAT	35.0	81.6	-57.1%	117	-70.1%
Adj.EPS	2.3	5.3	-57.1%	7.7	-70.1%
<b>Margin</b>			<b>BPS</b>		<b>BPS</b>
OPM (%)	9.2	13.1	(396)	13.4	(421)
NPM (%)	9.3	10.1	(82)	18.0	(871)
Tax rate	25.3	30.8	-	13.5	-

Source: Company; Sharekhan Research

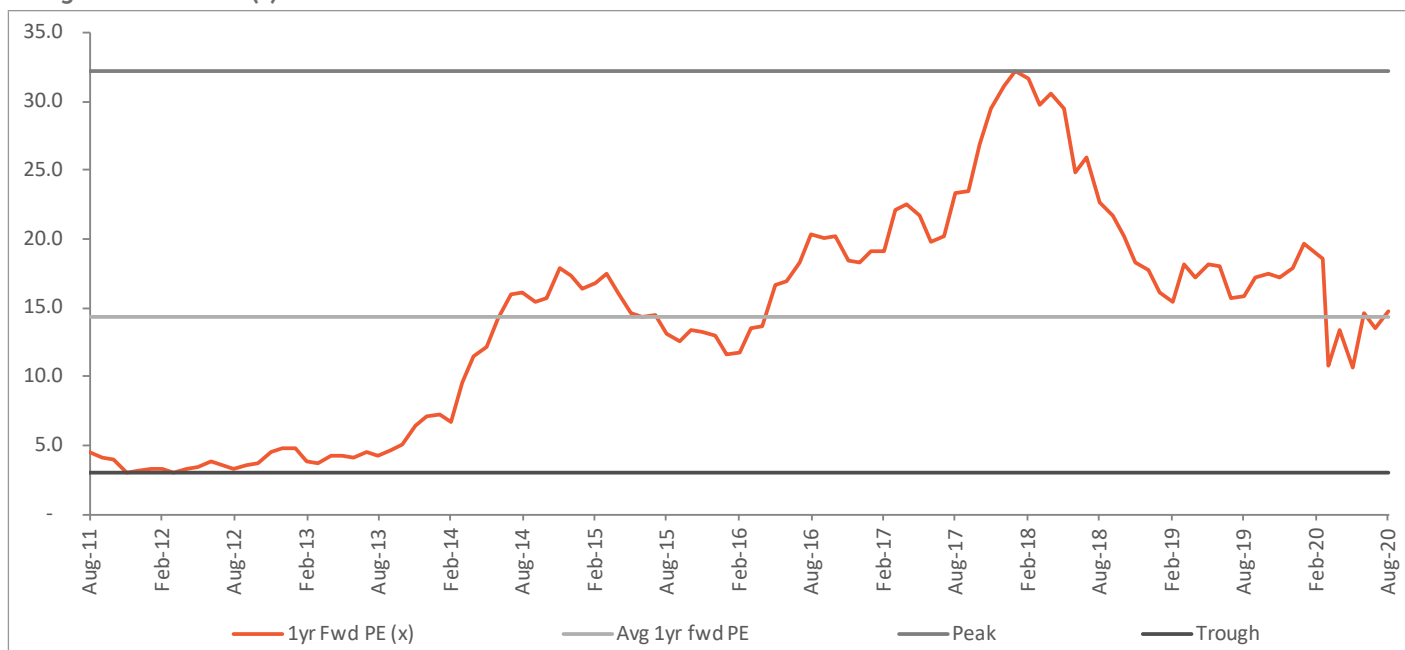
## Outlook

**Operations on an improving trajectory:** Capacity utilisation is improving m-o-m and its various businesses such as the electric cables division are witnessing healthy demand for housing wires and agriculture cables. A gradual pick-up in auto cables demand has been witnessed, in telecom cables demand has seen for LAN and co-axial cables. The company expects electric cables to normalise going ahead as labour, transport and supply chain issues get resolved. Although communication cable business is expected to be muted on account of funding issues from government (BSNL/BBNL). New products (~2-3% mix) are performing well and are expected to scale-up further as situation improves. Finolex will continue its Rs. 200 crore capex plan at be spread over 18 months and the company's healthy operating cash flow generation, tight working capital management (policy of advance payments from dealers) and limited capex is expected to further add to its cash reserves. Consequently, it may look at inorganic growth opportunities in its allied business verticals. The company also has opportunity to increase market share organically as the pandemic has had a severe impact on unorganised sector players.

## Valuation

**Upgrade to Buy with revised PT of Rs. 360:** We believe Finolex has performed well despite the effect of COVID-19 on the quarter, maintaining relatively better OPM despite steep dip in revenues. The company's operations are further expected to improve post monsoon as labour, transportation and supply chain issues get settled. Meanwhile, it has built a strong cash balance to consider inorganic growth opportunities. The COVID-19 led impact on unorganized players provides the company to increase its market share. We have fine-tuned our net earnings estimates for FY2021-FY2022E and introduced FY2023E earnings. Finolex is currently trading at a PE of 11.5x its FY2023E earnings, which is at a 10-20% discount to its peers. Considering its improving growth outlook organically and opportunity for inorganic growth, we upgrade our rating on the stock to Buy with revised PT of Rs. 360.

### One-year forward P/E (x) band



Source: Sharekhan Research

## About company

Finolex is India's largest and leading manufacturer of electrical and communication cables. The company offers a wide range of electrical and communication cables. The company's wire and cable products are used in applications such as automobile, lighting, cable TV, telephone and computers to industrial applications touching every person in his daily life. Finolex has added electrical switches, LED-based lamps, fans, low-voltage MCBs and water heaters to its range of products.

## Investment theme

While the government's focus on Housing for All by FY2022 is expected to drive demand for housing wires, slowdown in housing demand continues to affect performance of the electrical cables segment—65% of the company's total revenue constitutes housing wires. Further, ongoing government programmes (Bharat Net Phase II) are expected to improve broadband connectivity and related technologies will continue to drive growth for communication cables but due to the recent pandemic and government resources more routed towards the there might be delays in tendering for the same.

## Key Risks

- ♦ **Fluctuations in raw-material prices:** Any sharp increase or decrease in key raw-material (copper) prices will sharply affect the company's margins.
- ♦ Weak housing demand and construction activity will impact the company's electrical cables growth.

## Additional Data

### Key management personnel

Mr. D.K. Chhabria	Executive Chairperson
Mr. Mahesh Vishwanathan	Deputy MD & CFO

Source: Company Website

### Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Orbit Electricals Pvt Ltd	30.7
2	Finolex Industries Ltd	14.51
3	Franklin Resources Inc	6.76
4	DSP Investment Managers Pvt Ltd	5.13
5	L&T Mutual Fund Trustee Ltd/India	3.38
6	Chhabria Anil R	3.11
7	HDFC Life Insurance Co Ltd	1.98
8	LGOF Global Opportunities	1.88
9	Gopichand Parmanand Hinduja	1.88
10	Katara Aruna Mukesh	1.84

Source: Bloomberg

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by BNP PARIBAS

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