Sharekhan by BNP PARIBAS

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Stock Update

Polycab India Limited

Good quarter, growth longevity remains

Capital Goods	Sharekhan code: POLYCAB	Result Update

3R MATRIX	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)	✓		

\+ Positive = Neutral - Negative

What has changed in 3R MATRIX	Old		New
RS		↔	
RQ		↔	
RV		↔	

Reco/View	Change
Reco: **Buy**	↔
CMP: **Rs. 1,212**	
Price Target: **Rs. 1,530**	↔

↑ Upgrade ↔ Maintain ↓ Downgrade

Company details

Market cap:	Rs. 18,068 cr
52-week high/low:	Rs. 1,324/572
NSE volume: (No of shares)	14.0 lakh
BSE code:	542652
NSE code:	POLYCAB
Free float: (No of shares)	4.7 cr

Shareholding (%)

Promoters	68.3
FII	12.6
DII	4.0
Others	15.1

Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	15	27	48	19
Relative to Sensex	12	6	21	3

Sharekhan Research, Bloomberg

Summary

- We retain Buy on Polycab India Limited (Polycab) with an unchanged PT of Rs. 1,530, given the improvement in demand in underlying user-industries.
- Polycab reported good performance across segments, leading to healthy revenue growth along with stable margins despite commodity headwinds leading to 20% y-oy- growth in net profit, which is slightly better than estimates.
- Broad-based recovery across regions seen, wherein B2C demand has sharply recovered with sentiment improvement, construction activity has picked up, and private sector investment has picked up resulting in pickup in B2B business, which bodes well for the company.
- Polycab's strong balance sheet and net cash position provide comfort in the present environment. The company's strong focus on its distribution currently at 4,000 dealers/distributors will help deepen its presence in semi-urban and rural markets.

Polycab India Limited (Polycab) reported good performance in Q3FY2021. Growth can be attributed to improving business environment and improving share of B2C business. Revenue grew by 11.6% y-o-y to Rs. 2,799 crore (marginally better than estimates) as wires and cables revenue improved by 5.6% y-o-y (B2C categories continued to see strong traction, while B2B has seen improvement on a q-o-q basis) to Rs. 2,270 crore and distribution-led business continued to see handsome growth. FMEG continued its growth trajectory despite facing high competition, posting strong 41% y-o-y growth to Rs. 305.5 crore because of buoyant consumer demand, distribution expansion, better product mix, and pricing actions. The company reported flat operating profit margin (OPM) at 13.4% (in line with estimates), despite higher input cost, however it was supported by lower other expenses, improved product mix, and price hikes. Consequently, EBITDA improved by 10.8% y-o-y to Rs. 376 crore. Higher other income was offset by higher tax rate (25.6% in Q3FY2021 versus 23.6% in Q3FY2020), which led to net profit at Rs. 263 crore (up 20% y-o-y, marginally better than estimates). On the export front, Polycab is witnessing good traction (grew by 29% y-o-y excluding Dangote orders) led by developed geographies (Australia, Asia, and U.K.). Management indicated that the market is witnessing broad-based recovery across regions wherein B2C demand has sharply recovered with improving sentiment, pickup in construction activity, improvement in private sector investment, resulting in pickup in B2B business, which bodes well for the company. Management believes it will maintain its growth trajectory led by B2C (wires and FMEG), introduction of premium products, and new launches. In FMEG, the company would be launching IoT based, technology-driven, app-based new products (New brand HOHM) having voice command feature, which will be available on the online platform from next month. Margins are expected to be better than the base products. All these products are expected to be manufactured in-house. Overall, despite commodity headwinds the company expects margins to be at 11%-13% in wires and cables, with Project Udaan and other such cost initiatives to aid in improving margins going ahead. The company is strongly focusing on its distribution, currently at 4,000 dealers/distributors, catering to 1,50,000 retailers; and its distribution enhancement programme is on track, which will help deepen its presence in semi-urban and rural market. With improving business environment, domestic demand for FMEG from tier I, II, and below towns is expected to continue its growth trajectory, while wires and cables (demand being back ended) are expected to see improvement as infrastructure investments rise, further supported by Union Budget 2021, wherein focus is expected to remain on infra. We have fine tuned our estimates for FY2021E-FY2022E. We believe the company is on a healthy growth trajectory owing to its leadership position and a strong product portfolio both in wires and cables and FMEG businesses along with robust distribution, in-house manufacturing capabilities, strong balance sheet, and healthy cash position. The stock is currently trading at P/E of 22.4x/20.2x its FY2022E/FY2023E EPS. Hence, we retain Buy on the stock with an unchanged price target (PT) of Rs. 1,530.

Key positives

- FMEG continued its growth trajectory (+41% y-o-y) despite competition.
- Exports grew strongly by about 29% y-o-y (excluding Dangote order).
- The company's net cash position as of December 31, 2020, doubled to Rs. 1,333.5 crore versus Rs. 640 crore in Q3FY2020.

Key negatives

- Gross margin impacted due to rising commodity prices.

Our Call

Valuation – Retain Buy with an unchanged PT of Rs. 1,530: Polycab is expected to maintain healthy performance led by strong traction in the housing segment, input cost led price hikes undertaken, rising exports, and scaling up of the FMEG business with new product launches. The company also has strong growth tailwinds in terms of rising infrastructure investments and revival in private capital expenditure. Polycab's strategy of deepening penetration in semi-urban and rural markets bodes well in providing sustainable long-term growth. Overall, we believe the company is on a healthy growth trajectory, owing to its leadership position and a strong product portfolio both in wires and cables and FMEG businesses along with strong distribution and in-house manufacturing capabilities. Further, the strong balance sheet, improving working capital requirement, and faster growth in the B2C business provides comfort. The stock is currently trading at P/E of 22.4x/20.2x its FY2022E/FY2023E EPS. We retain Buy on the stock with an unchanged PT of Rs. 1,530.

Key risk

Fluctuations in raw-material prices would affect margins sharply.

Valuation (Consolidated) Rs cr

Particulars	FY20	FY21E	FY22E	FY23E
Revenue	8,830	8,325	9,604	10,583
OPM (%)	12.9	11.6	12.1	12.4
Adjusted PAT	766	653	806	893
% YoY growth	53.0	(14.7)	23.5	10.8
Adjusted EPS (Rs.)	54.2	43.8	54.1	60.0
P/E (x)	22.4	27.6	22.4	20.2
P/B (x)	4.7	4.1	3.5	3.1
EV/EBITDA (x)	14.5	16.4	14.5	11.5
RoNW (%)	22.9	15.9	17.0	16.3
RoCE (%)	30.5	21.4	22.6	22.3

Source: Company; Sharekhan estimates

Good quarter: Polycab reported good performance in Q3FY2021. Growth can be attributed to improving business environment and share of B2C business. Revenue grew by 11.6% y-o-y to Rs. 2,798 crore (marginally better than estimates) as wires and cables revenue improved by 5.6% y-o-y (B2C categories continued to see strong traction, while B2B has seen improvement on a q-o-q basis) to Rs. 2,270 crore and distribution-led business continued to see handsome growth. FMEG continued its growth trajectory despite facing high competition, posting strong 41% y-o-y growth to Rs. 305.5 crore because of buoyant consumer demand, distribution expansion, better product mix, and pricing actions. The company reported flat OPM at 13.4% (in line with estimates), despite higher input cost. However, it was supported by lower other expenses, improved product mix, and price hikes. Consequently, EBITDA improved by 10.8% y-o-y to Rs. 376 crore. Higher other income was offset by higher tax rate (25.6% in Q3FY2021 versus 23.6% in Q3FY2020), which led to net profit at Rs. 263 crore (up 20% y-o-y, marginally better than estimates). On the export front, Polycab is witnessing good traction (grew by 29% y-o-y excluding Dangote orders) led by developed geographies (Australia, Asia, and U.K.).

Business gaining traction: Management indicated that the market is witnessing broad-based recovery across regions wherein B2C demand has sharply recovered with improving sentiment, pickup in construction activity, improvement in private sector investment, resulting in pickup in B2B business, which bodes well for the company. Management believes it will maintain its growth trajectory led by B2C (wires and FMEG), introduction of premium products, and new launches. In FMEG, the company would be launching IoT based, technology-driven, app-based new products (new brand HOHM) having voice command feature, which will be available on the online platform from next month. Margins are expected to be better than the base products. All these products are expected to be manufactured in-house. Overall, despite commodity headwinds, the company expects margins to be at 11%-13% in wires and cables, with Project Udaan and other such cost initiatives to aid in improving margins going ahead. The company's strong focus on its distribution, which is currently at 4,000 dealers/distributors catering to 1,50,000 retailers and on-track distribution enhancement programme, will help deepen its presence in semi-urban and rural market. With improving business environment, domestic demand for FMEG from tier I, II, and below towns is expected to continue its growth trajectory, while wires and cables (demand being back ended) are expected to see improvement as infrastructure investments rise further supported by Union Budget 2021, wherein focus is expected to remain on infrastructure.

Key Conference call takeaways

- **Market overview:** Broad-based recovery across regions, B2C demand has sharply recovered with sentiment improvement, construction activity has picked up, private sector investment has picked up resulting in pickup in B2B business
- **B2C and B2B categories update:** The company's B2C categories continued to see strong traction, while B2B has seen improvement on a q-o-q basis. A&P spends were higher on IPL-related expenses. Commodity price increase continues to post challenges.
- **Wires & Cables:** It grew by 6% y-o-y; domestic wires posted double-digit growth, while cables business remained flat. Instructional business was muted. Distribution-led business continued to see handsome growth. Export business declined on a high base of Dangote order. Margins in wires and cables are likely to remain at 11%-13%.
- **FMEG:** FEMG continued its growth trajectory despite facing high competition, unavailability of product, supply, and logistics issues in Q3FY2021.
- **Demand across segments:** Demand of lighting products remained upbeat because of the festive season. Switchgear and switches have seen growth because of home improvement. FMEG has seen margin

improvement due to change in product mix and cost rationalisation. The company is on track to achieve high single-digit margin in the next two years.

- **Geographical gains:** The company has seen higher growth in East with market share gains in fans.
- **Market share:** Market share gains have been across the board. The company is confident of continued market share gains in the medium term over the next five years.
- **Gross Margin:** Gross margins were affected because of rising commodity prices. Complete cost of commodity price increase has not been passed on; it is likely to be passed on in a calibrated manner.
- **New brand HOHM:** HOHM is the new brand of Polycab consisting of premium IOT-based products, which will be available on the online platform from next month. Margins are expected to be better than the base products. All these products are expected to be manufactured in-house.
- **Distribution:** The company has 4,000 dealers/distributors catering to 1,50,000 retailers and distribution enhancement programme is on track. Focus will be on increasing experience centres.
- **Working capital:** Working capital has seen improvement on higher channel financing and increasing in payables. The company is confident of further improving its working capital by reducing inventory levels and keeping payable at optimal level. Reduction in working capital has led to strong cash generation.
- **Cash Generation:** Cash generation will be used as the company required capex for getting into the defense and railway sectors. It will be also used to improve capability for getting more exports orders.
- **New product category:** The company will continue to focus on existing product categories as there is huge scope of increasing share in FMEG.
- **New launches:** Looking to enter new product categories will let market and investors know as and when things materialise.

Results (consolidated) **Rs cr**

Particulars	Q3FY21	Q3FY20	YoY (%)	Q2FY21	QoQ (%)
Revenue	2,798.8	2,507	11.6%	2,114	32.4%
Operating profit	376	339	10.8%	312	20.3%
Other Income	34	0	-	33	5.3%
Interest	9	9	2.9%	11	-22.4%
Depreciation	48	41	17.6%	46	4.9%
PBT	354	290	21.9%	288	22.7%
Tax	90	69	32.0%	66	36.2%
EO	-	-		-	
Reported PAT	263	219	20.0%	221	19.0%
Adj. PAT	263	219	20.0%	221	19.0%
Adj. EPS (Rs.)	17.6	14.7	20.0%	14.8	19.0%
Margin			**BPS**		**BPS**
OPM (%)	13.4	13.5	(10)	14.8	(136)
NPM (%)	9.4	8.7	65	10.4	(106)
Tax rate	25.6	23.6	-	23.0	-

Source: Company; Sharekhan Research

Outlook and Valuation

■ Sector View – Ample levers offer scope for growth

Domestic demand side is improving with unlocking, infrastructure, and construction back in action with labour issues largely resolved, which provides a positive outlook ahead. The wires and cables industry contributes 40%-45% to India's electrical equipment industry. In terms of volumes, the Indian wires and cables industry (including exports) has grown from 6.3million kms in FY2014 to 14.5million kms in FY2018, posting a ~23% CAGR over the period. The industry registered an ~11% CAGR in value terms, from Rs. 34,600 crore in FY2014 to Rs. 52,500 crore in FY2018. The C&W industry was expected to register a CAGR of 14.5% from Rs. 52,500 crore in FY2018 to Rs. 1,03,300 crore by FY2023. However, slowdown in infrastructure growth and uncertainty in real estate will lead to moderation in growth for the C&W segment. Gradual resumption of normal economic activity and infrastructure projects will push recovery to H2FY2021. The government has envisaged Rs. 111 lakh crore capital expenditure in infrastructure sectors in India during FY2020 to FY2025. Sectors such as energy (24%), roads (18%), urban (17%), and railways (12%) amount to ~71% of the projected infrastructure investment. The continued thrust of the government on infrastructure investment is expected to improve the demand environment for the W&C industry. The Indian FMEG industry has many growth opportunities, led by macro drivers such as evolving consumer aspirations, increasing awareness, rising income, rural electrification, urbanisation, and digital connectivity. Products such as energy-efficient fans, modular switches, building and home automation, and LED lights are riding an ever-increasing wave of consumer demand. There is also a rising demand for various electrical appliances.

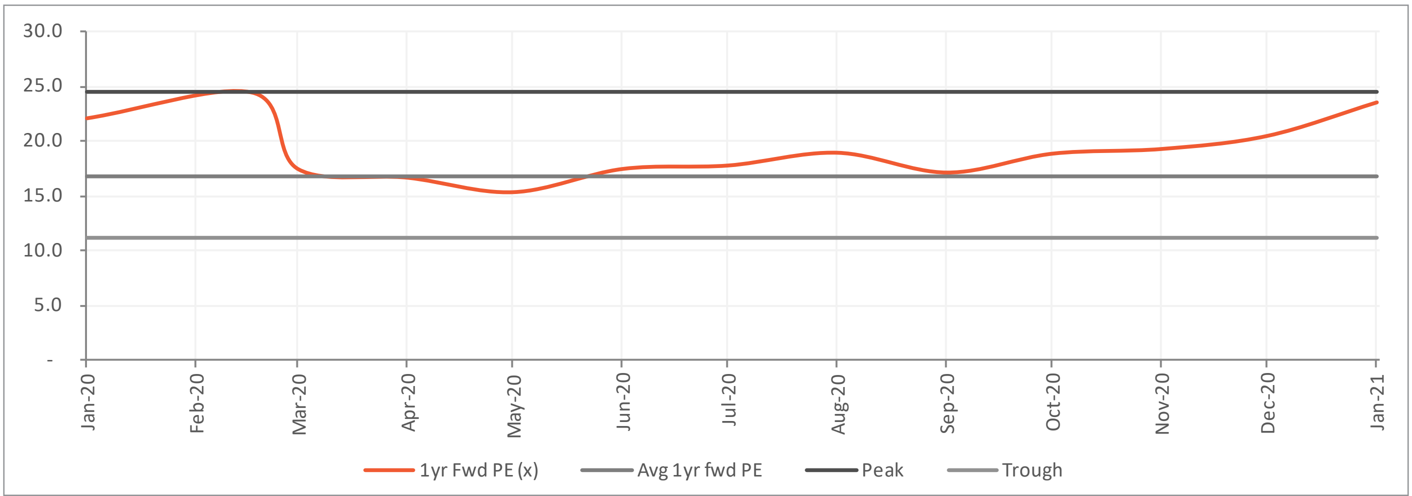
■ Company Outlook – Improving business environment

Domestic demand witnessed bounce back with improving business environment. Post easing of the lockdown, the company is witnessing demand from tier 2 and tier 3 cities and rural India. The company is gradually bouncing and expected to improve ahead owing to its leadership position and a strong product portfolio both in wires and cables and FMEG businesses along with strong distribution and in-house manufacturing capabilities. The company is expecting better Q3FY2021 compared to Q2FY2021. Strong traction seen in new launches and sales in pan-India residential market are expected to drive the company's housing wires and FMEG segments. The company is likely to deepen its presence in semi-urban and rural markets to drive the FMEG business. Exports are expected to remain the focus area to aid C&W revenue growth.

■ Valuation – Retain Buy with an unchanged PT of Rs. 1,530

Polycab is expected to maintain healthy performance led by strong traction in the housing segment, input cost led price hikes undertaken, rising exports, and scaling up of the FMEG business with new product launches. The company also has strong growth tailwinds in terms of rising infrastructure investments and revival in private capital expenditure. Polycab's strategy of deepening penetration in semi-urban and rural markets bodes well in providing sustainable long-term growth. Overall, we believe the company is on a healthy growth trajectory, owing to its leadership position and a strong product portfolio both in wires and cables and FMEG businesses along with strong distribution and in-house manufacturing capabilities. Further, the strong balance sheet, improving working capital requirement, and faster growth in the B2C business provides comfort. The stock is currently trading at P/E of 22.4x/20.2x its FY2022E/FY2023E EPS. We retain Buy on the stock with an unchanged PT of Rs. 1,530.

One-year forward P/E (x) band



Source: Sharekhan Research

About company

Polycab manufactures and sells wires and cables and FMEGs, besides executing a few EPC projects. The company has 25 manufacturing facilities, including two joint ventures with Techno and Trafigura, located across Gujarat, Maharashtra, Uttarakhand, and the union territory of Daman and Diu. Polycab strives to deliver customised and innovative products with speed and quality service.

Investment theme

Polycab is the market leader in the wires and cables space with an extensive product portfolio and distribution reach coupled with accelerated growth in the FMEG space, which augurs well for growth visibility. The company's market position and success are driven by its robust distribution network, wide range of product offerings, efficient supply chain management, and strong brand image. Revenue from the wires and cable segment has seen a decent 10.5% CAGR during FY2016-FY2019. Further, increasing market share of organised players, which grew from 61% in FY2014 to 66% in FY2018, is expected to touch 74% in FY2023E, which augurs well for the industry leader.

Key Risks

- **Fluctuations in raw-material prices pose a key challenge:** Any sharp increase or decrease in the prices of key raw material (copper and aluminium) will sharply impact margins.
- **Currency risk:** Polycab faces forex risks as a significant portion of its raw-material purchases, particularly aluminum, copper, and PVC compound, are priced with reference to benchmarks quoted in US Dollar terms. Hence, expenditure is largely influenced by the value of US Dollar.

Additional Data

Key management personnel

Inder T. Jaisinghani	Chairman and Managing Director
Ajay T. Jaisinghani	Whole-Time Director
R. Ramakrishnan	Chief Executive Officer
Bharat A. Jaisinghani	Director – FMEG Business (Non-board member)
Manoj Verma	Executive President and Chief Operating Officer (CE)
Gandharv Tongia	Deputy Chief Financial Officer

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Jaisinghani Inder	14.41
2	Jaisinghani Girdhari T	14.34
3	Jaisinghani Ajay T	14.29
4	Jaisinghani Ramesh T	14.29
5	IFC	9.48
6	International Finance Corp	9.48
7	JaisinghaniKunal	3.91
8	Jaisinghani Bharat	3.68
9	Jaisinghani Nikhil	3.68
10	Hariani Anil	3.57

Source: Bloomberg

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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