

26 September 2022

Nilkamal

Aims to scale up non-plastic furniture vigorously; retaining a Buy

Nilkamal management expects 11-15% overall volume growth in FY23. It aims to double revenue in the next 5-6 years, with 12-15% margins

Performance expected to be healthy. The demand environment seems encouraging. Price hikes in material handling would continue as earlier higher input costs were not fully passed on. In the furniture business, however, earlier price hikes have been adequate.

Raw material tailwinds expected by Q4. Volatility in key raw materials such as polyethylene and polypropylene continues. However, prices, which were softer in Jul/Aug, started firming up in Sep. Management expects a favourable pricing scenario from Q4 FY23.

Aims to be a one-stop home-furnishing-solutions provider. Plastic furniture has a small market size, while in non-plastic furniture the opportunity size is significant. Hence, after the Boston Consulting group report on the furniture business revamp, the company is striving to scale up the non-plastic furniture business.

Strengthening its manufacturing, marketing abilities in non-plastic furniture. Capex at Hosur for non-plastic furniture is progressing. On the land acquisition being completed by Dec, the facility is expected to be operational within 6-9 months, ie, Q1/Q2 FY24.

Outlook, Valuation. The demand environment looks encouraging. Input cost tailwinds would provide headroom for margin expansion. Hence, we expect 13% and 54% CAGRs over FY22-24 in revenue and earnings, respectively. We have a Buy rating on the stock, with an unchanged TP of Rs.2,985, based on 22.5x FY24 earnings.

Key financials (YE Mar)	FY20	FY21	FY22	FY23e	FY24e
Sales (Rs m)	22,572	20,922	27,301	31,560	34,893
Net profit (Rs m)	1,421	1,129	834	1,518	1,979
EPS (Rs)	95.2	75.7	55.9	101.7	132.6
P/E (x)	21.7	27.2	36.8	20.3	15.5
EV / EBITDA (x)	11.0	11.9	14.2	9.9	8.2
P/BV (x)	3.0	2.7	2.5	2.3	2.0
RoE (%)	14.4	10.4	7.1	12.0	13.9
RoCE (%) – post-tax	13.2	9.5	6.5	9.8	11.4
Dividend yield (%)	1.0	0.2	0.3	0.5	0.6
Net debt / equity (x)	0.0	(0.1)	0.1	0.1	0.1

Source: Company, Anand Rathi Research

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Rating: **Buy**

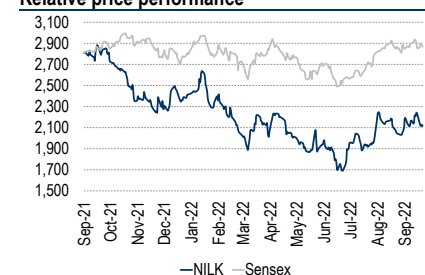
Target Price: Rs.2,985

Share Price: Rs.2,098

Key data	NILK IN / NKLM.BO
52-week high / low	Rs.2940 / 1693
Sensex / Nifty	58099 / 17327
3-m average volume	\$0.3m
Market cap	Rs.32bn / \$395m
Shares outstanding	15m

Shareholding pattern (%)	Jun'22	Mar'22	Dec'21
Promoters	64.5	64.5	64.5
- of which, Pledged	-	-	-
Free float	35.5	35.5	35.5
- Foreign institutions	2.0	2.2	2.2
- Domestic institutions	19.8	19.6	19.5
- Public	13.7	13.7	13.8

Relative price performance



Source: Bloomberg

Rishab Bothra
Research Analyst

Quick Glance – Financials and Valuations (consol.)

Fig 1 – Income statement (Rs m)

Year-end: Mar	FY20	FY21	FY22	FY23e	FY24e
Net revenues	22,572	20,922	27,301	31,560	34,893
Growth (%)	-4.5	-7.3	30.5	15.6	10.6
Direct costs	12,471	11,772	16,612	18,739	20,500
SG&A	7,289	6,619	8,475	9,567	10,468
EBITDA	2,812	2,531	2,213	3,254	3,926
EBITDA margins (%)	12.5	12.1	8.1	10.3	11.3
- Depreciation	942	972	1,010	1,144	1,183
Other income	144	160	119	118	87
Interest expenses	261	235	284	330	355
PBT	1,753	1,485	1,038	1,898	2,474
Effective tax rate (%)	22.3	24.9	25.1	25.0	25.0
+ Associates / (Minorities)	59	14	56	95	124
Net income	1,421	1,129	834	1,518	1,979
Adjusted income	1,421	1,129	834	1,518	1,979
WANS	14.9	14.9	14.9	14.9	14.9
FDEPS (Rs / sh)	95.2	75.7	55.9	101.7	132.6
FDEPS growth (%)	21.1	-20.5	-26.2	82.1	30.4
Gross margins (%)	44.8	43.7	39.2	40.6	41.3

Fig 3 – Cash-flow statement (Rs m)

Year-end: Mar	FY20	FY21	FY22	FY23e	FY24e
PBT (adj. for int. exp./ other inc.)	1,753	1,485	1,038	1,898	2,474
+ Non-cash items	942	972	1,010	1,144	1,183
Oper. prof. before WC	2,695	2,456	2,048	3,042	3,657
- Incr. / (decr.) in WC	(35)	(407)	(1,235)	(1,940)	(922)
Others incl. taxes	(199)	(139)	18	(144)	(263)
Operating cash-flow	2,462	1,910	831	958	2,472
- Capex (tang. + intang.)	(2,941)	(1,308)	(1,695)	(1,380)	(1,408)
Free cash-flow	(479)	602	(864)	(422)	1,064
Acquisitions					
- Div.(incl. buyback & taxes)	(425)	(75)	(112)	(149)	(187)
+ Equity raised	-	0	-	-	-
+ Debt raised	(35)	6	1,261	368	159
- Fin investments	170	(6)	(6)	-	-
- Misc. (CFI + CFF)	843	137	(501)	(314)	(709)
Net cash-flow	74	665	(222)	(517)	327

Source: Company, Anand Rathi Research

Fig 5 – Price movement



Source: Bloomberg

Fig 2 – Balance sheet (Rs m)

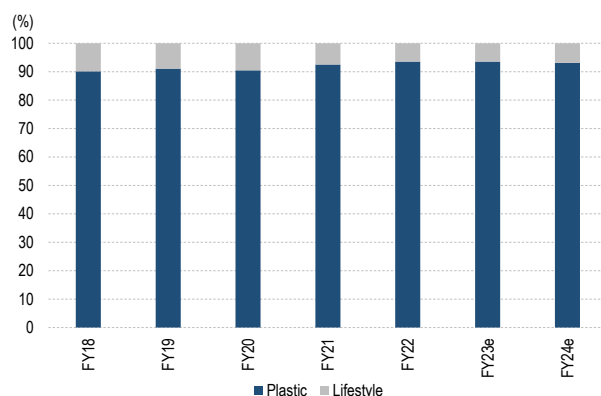
Year-end: Mar	FY20	FY21	FY22	FY23e	FY24e
Share capital	149	149	149	149	149
Net worth	10,172	11,245	11,866	13,235	15,028
Debt	479	485	1,747	2,115	2,274
Minority interest	9	10	7	-	-
DTL / (Assets)	134	127	122	122	122
Capital employed	10,943	12,017	13,891	15,621	17,573
Net tangible assets	5,842	6,265	6,866	7,241	7,491
Net intangible assets	14	9	14	14	14
Goodwill	68	68	68	68	68
CWIP (tang. & intang.)	266	184	264	125	100
Investments (strategic)	176	191	212	212	212
Investments (financial)	167	157	142	142	142
Current assets (excl. cash)	1,423	1,397	1,531	1,747	1,883
Cash	240	905	684	167	494
Current liabilities	3,035	3,295	3,432	3,606	3,347
Working capital	5,783	6,135	7,542	9,511	10,516
Capital deployed	10,943	12,017	13,891	15,621	17,573
Contingent liabilities	145	130	155	-	-

Fig 4 – Ratio analysis

Year-end: Mar	FY20	FY21	FY22	FY23e	FY24e
P/E (x)	21.7	27.2	36.8	20.3	15.5
EV / EBITDA (x)	11.0	11.9	14.2	9.9	8.2
EV / Sales (x)	1.4	1.5	1.1	1.0	0.9
P/B (x)	3.0	2.7	2.5	2.3	2.0
RoE (%)	14.4	10.4	7.1	12.0	13.9
RoCE (%) - after tax	13.2	9.5	6.5	9.8	11.4
RoIC	14.0	10.3	7.1	10.4	11.9
DPS (Rs / sh)	24.0	5.0	7.5	10.0	12.5
Dividend yield (%)	1.0	0.2	0.3	0.5	0.6
Dividend payout (%) - incl. DDT	29.9	6.6	13.4	9.8	9.4
Net debt / equity (x)	0.0	(0.1)	0.1	0.1	0.1
Receivables (days)	52.6	53.7	42.0	50.0	50.0
Inventory (days)	65.7	86.9	88.4	90.0	90.0
Payables (days)	24.7	33.6	29.5	30.0	30.0
CFO : PAT %	173.2	169.2	99.7	63.1	124.9

Source: Company, Anand Rathi Research

Fig 6 – Revenue mix



Source: Company

Management call KTAs

- **Q1 FY23 performance** was better than a year ago (low-base effect of the partial lockdown on Covid-19 resurfacing). The company continued to deliver volume and value growth, but the focus continues on improving margins (hurt largely by high input costs in FY22 which continued in Q1 FY23).
- **Price hikes in material handling to persist.** Furniture prices have been hiked adequately to mitigate input cost increases; in material handling, however, further price increases of 5-7% are required as higher input costs have not been passed on completely.
- **Raw material pricing environment challenging.** For key plastic product manufacturers/convertors, the key raw material is PVC or other grades. For Nilkamal, however, the key raw materials is polyethylene and polypropylene. Prices of these have not changed materially except for some softness toward end-Jul and Aug. They have now started firming up and this is expected to continue for at least two quarters or so (margins would remain under pressure).
- **The variables affecting margins have increased.** The gross margin correlation with crude oil price movements seems to be fading. Though crude oil prices have come down, it has not materially altered the raw material price scenario for the company. Earlier raw material prices were more directly correlated with international crude prices. That seems to be fading as raw material prices now depend on many factors such as i) the international geopolitical situation, ii) international price trends, iii) forex movements, iv) prevailing domestic gas prices, iv) maintenance shutdowns curtailing raw material supply and impacting gas prices.
- **Focus on non-plastic furniture to become a one-stop-solutions provider in home furnishings.** On suggestions from the Boston Consulting Group (BCG), the company is focusing more on non-plastic furniture as the plastic furniture category is almost stagnant or growing slowly because of its size, with similar custom-moulded products in existence for more than 20-30 years.

Based on the BCG report, the company has re-focused and re-strategized its furniture business by making a foray into and focusing on non-plastic furniture. It is now building physical (manufacturing capability) and marketing infrastructure for the business. Non-plastic furniture manufacturing started 18 months ago in rented premises in Hosur, while manufacturing of mattresses had started across the country. Manufacturing metal furniture such as seatings was also begun. The manufacturing plant to come up at Hosur would enhance the furniture revenue base.

The company aims to be a one-stop solutions provider in home furnishings (plastic, non-plastic and metal furniture, mattresses, etc.) as it is in the material handling business (different products for various sectors and industries).

- **Setting up a non-plastic furniture manufacturing plant.** The company intends to put up one more large plant in Hosur to manufacture non-plastic furniture: factory-manufactured automated particle-board and medium-density fibre-board furniture, and sofas among others.

For this, Plant envisaged to be setup on 70 acres. However the acquisition has been delayed by more than six months, since it is being acquired from various individuals, not from industrial associations/ government bodies). Only 30 acres have been acquired; the balance is expected to be acquired by end-Sep/Oct'22.

Construction of the plant will take 7-9 months from complete land acquisition. Land required to set up a plant is 45 acres, the balance kept for future expansions.

The asset turnover expected would be 3x-4x depending on products offered.

- **Capex largely on track:** The company had earlier envisaged capex of Rs2,500m (Rs1,400 m for the Hosur plant). Considering the delay in land acquisition, the company now anticipates FY23 capex of ~Rs2,000m. It has invested Rs750m till now (Rs110 m for the Hosur land acquisition, Rs500m for seven large imported injection moulding machines (increasing capacity for pallets and bins mainly in material handling by 8,400 tpa, to 110,000 tpa).
- **Focus on increasing warehousing capacity.** The company has warehouses at Bhiwandi in the west, Hosur in the south, and Baroda in the east. It is attempting to fill the gap by building one at Noida in north India.
- **To scale up is retail network vigorously.** The company has all-India operations, focusing on tier-2, -3 and -4 cities, and stores of 4,000-10,000 sq.ft. It currently operates 80+ stores under the Nilkamal brand through franchisees, and ~35 large format tier-1 stores under Atom. Key sales channels are i) dealers/distributors, ii) e-commerce platforms, iii) large outlets for furniture, iv) franchisee model (FOFO)/Atom (plastic furniture sold through 20,000 retailers across India). The company aims to increase the number of stores to 300+. Minimum revenue expectation of Rs10-12.5m for a retail store of 4,000 sq.ft. (from Rs0.2/0.3m a month to Rs1/1.2m).
- **Increasing its manufacturing ability in non-plastic furniture.** The non-plastic business growth should be sustainable and scalable. In the next five years management expects more than 60% of non-plastic furniture sold would be manufactured in-house (two years ago 100% was imported; now only 10-15%). The company imports furniture mainly from Malaysia and China.
- **Merger approved, to be completed by Dec'22, effective 1st Oct'22.** In material handling, other than crates, bins and pallets, the company also makes racks/shelves (a second factory in Sinnar near Nasik had Rs2,800m revenue through a 100% subsidiary, to be merged effective 1st Oct'22, and completed by Dec. The company expects more than Rs3,500m revenue from this business in FY23.
- **Product launches in material handling to further scale up business.** The company will launch material-handling products for various industries based on their needs.
- **Business operations in Sri Lanka hit, though not materially.** Sri Lanka has been going through crises such as currency devaluation, political instability, etc. Volumes are down 50% but the company's business there continues to be profitable. The business in Sri Lanka is too small, hence not material.

- **Ad spends to increase (non-plastic furniture):** H2 FY23 ad-spend is expected at ~3-5% for schemes to dealers and distributors; for FY23 it is expected at Rs150m-250m.
- **Huge stock levels to normalise.** Stock levels average 15-20 days, and now are 20-30 days. More inventory days were due to non-plastic furniture, largely imported to mitigate issues like container non-availability (lead time) and higher shipping charges (freight cost). This should become normal in a quarter or so.
- **Debt likely to increase.** Long-term debt is now Rs1,250m. The company expects net debt to peak at Rs3,000m, of which Rs1,000m would be for working capital.
- **Overall guidance.** Management expects 11-15% FY23 volume growth (16% in Q1 FY23; till Aug'22, 11%), and double-digit margins likely by Q4 FY23. It expects to double revenue in the next 5-6 years. EBITDA margins would come at 12-15%.
- **Huge expectations of the PLI scheme extended to furniture.** A government notification with respect to extending the PLI scheme to furniture might come by end-Q3 or early Q4 FY23 (as suggested by consultants). The company will benefit from the scheme as it intends to set up a large manufacturing plant for non-plastic furniture.

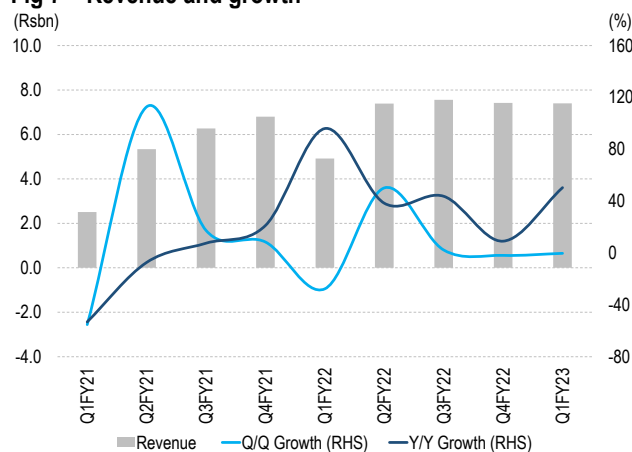
The Furniture Manufacturers Association has not proposed to the commerce ministry to extend the PLI scheme to the industry. Tamil Nadu, however, had established a furniture industrial park at Thoothukudi (formerly Tuticorin) for exports. As this did not work out, the state government is trying to make it workable by roping in industries and giving incentives for domestic consumption as well (as transport from the coastal region to land-locked areas will be incurred).

- **To benefit from the PM SHRI schools scheme.** Under the prime minister's SHRI schools scheme, 14,500 schools will be developed at a Rs273.6bn (Rs181.28bn to come from the Central government) for five years starting 2022-23. This is expected to benefit the company in both plastic and non-plastic furniture.

In a Telangana government order the company is L1 and expects more such orders from other state governments. It has a Rs250m order from the Andhra Pradesh government. To avoid stress in collection, it intends to work on such projects through a contractor who would take the risk of collection. Such projects help ramp up utilisation. Educational institutions and hospital are also being focused on to generate business in the furniture category. Competition arises from Godrej Interio (non-plastic furniture) and Supreme Industries (plastic furniture, one-third of Nilkamal).

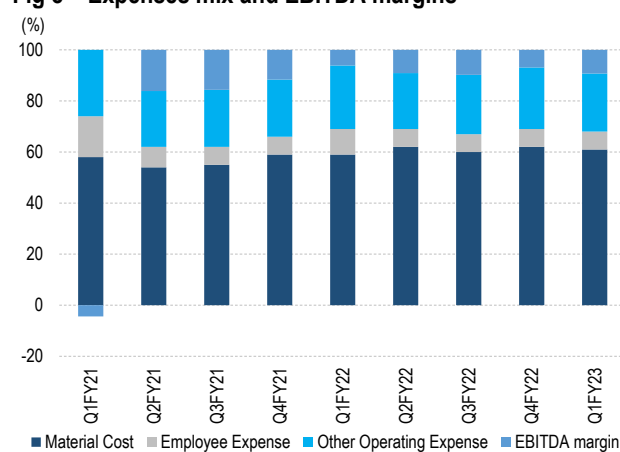
Story in charts

Fig 7 – Revenue and growth



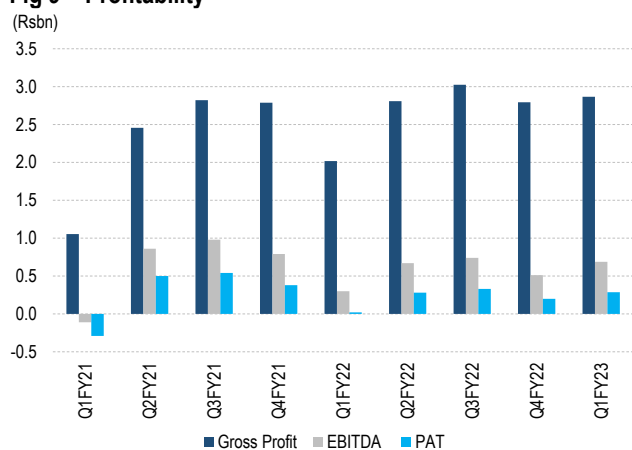
Source; Company, Anand Rathi Research

Fig 8 – Expenses mix and EBITDA margins



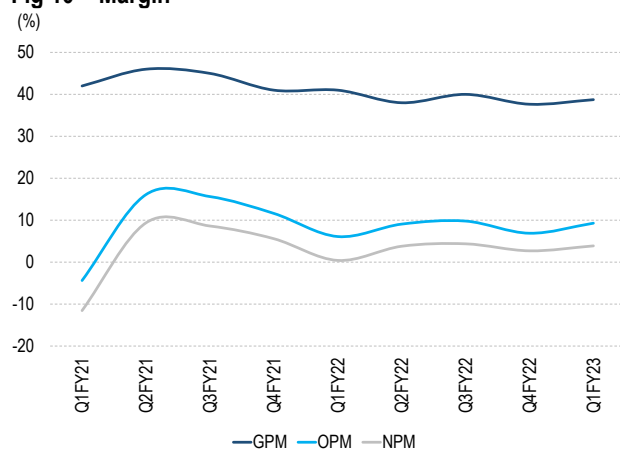
Source; Company, Anand Rathi Research

Fig 9 – Profitability



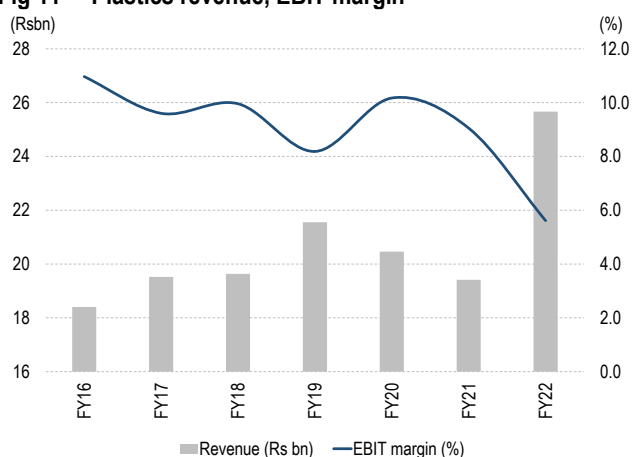
Source; Company, Anand Rathi Research

Fig 10 – Margin



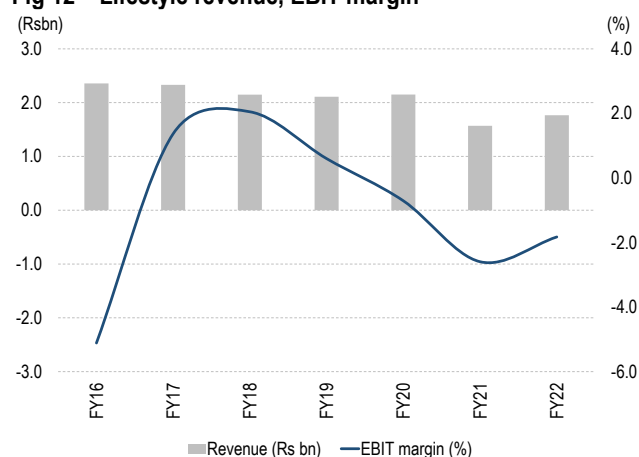
Source; Company, Anand Rathi Research

Fig 11 – Plastics revenue, EBIT margin



Source; Company, Anand Rathi Research

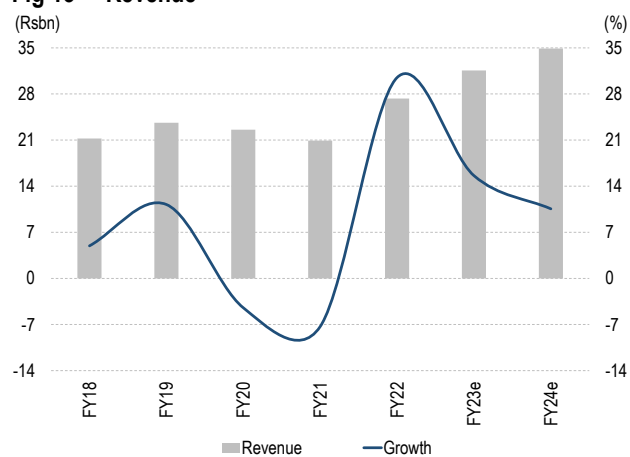
Fig 12 – Lifestyle revenue, EBIT margin



Source; Company, Anand Rathi Research

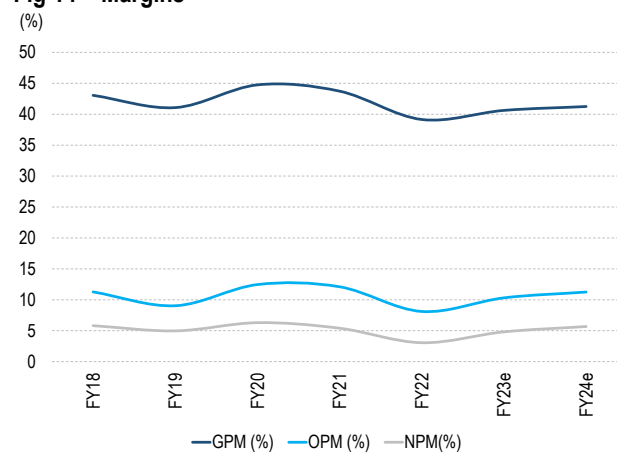
Story in charts continues

Fig 13 – Revenue



Source; Company, Anand Rathi Research

Fig 14 – Margins



Source; Company, Anand Rathi Research

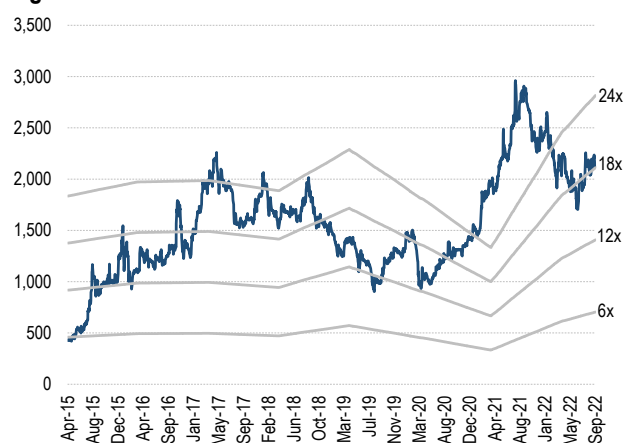
Valuation

We see bright prospects for Nilkamal for its market-share gains from the informal sector, greater focus on non-plastic furniture and online sales, deeper penetration in e-commerce and rising industrial activity. Its vast distribution network, plants at various locations, lean balance sheet and FCF generation are key strengths.

It will continue to invest in product development and manufacturing abilities (Rs1bn+ yearly capex planned incl. on non-plastic furniture). On its entry into new businesses (non-plastic furniture, mattresses, bubble-guard sheets), it is exploring options to add business verticals (and revenue streams). '@home' did not lead to the desired result and is only now slightly profitable.

Demand looks encouraging, and input cost tailwinds would offer headroom for margin expansion. Hence, we expect 13% and 54% CAGRs over FY22-24 in revenue and earnings respectively. We maintain our Buy rating, with a TP of Rs.2,985 based on 22.5x FY24e EPS.

Fig 15 – PE band



Source: BSE, Anand Rath Research

Fig 16 – PE Mean and SD



Source: BSE, Anand Rath Research

Risks

Upside

- **Exploring business opportunities.** The company has been attempting a foray into a related business vertical so as to enhance and diversify its products. The ramp-up and faster scalability would help accelerate its revenue growth momentum

Downside

- **Slowdown in the economy/industrial capex.** Slow recovery in industrial capex could curtail demand for material-handling products, while low economic growth would dampen consumer spending on furniture, etc.
- **Adverse movement in input costs, and inability to pass them on fully.** Higher key input costs (polyethylene, polypropylene, ~50% of raw material costs) and the company's inability to pass them on completely would eat into profits.
- **Mounting competition.** Keener competition from non-regulated as well as regulated manufacturers could constrict growth and margins.

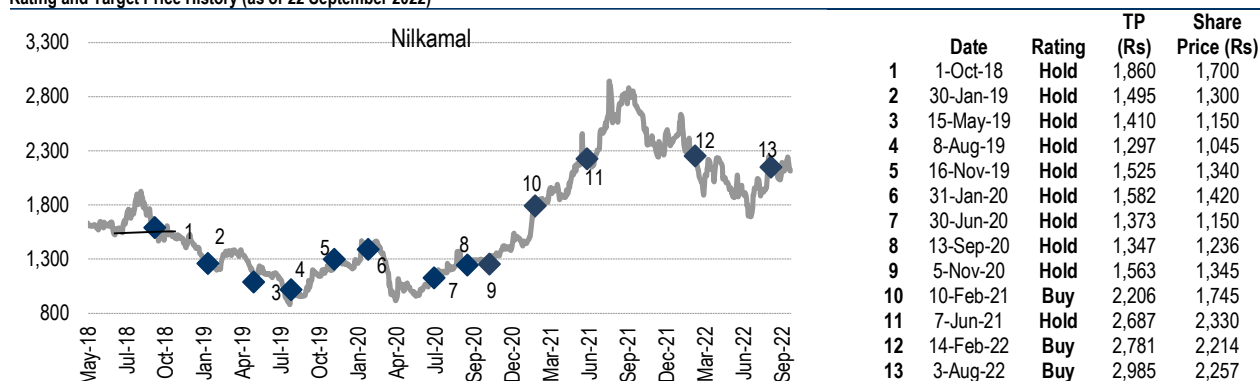
Appendix

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