Sharekhan by BNP PARIBAS

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Stock Update

Company Update

V-Guard Industries Ltd

Pulling multiple growth levers

Capital Goods	Sharekhan code: VGUARD

Reco/View: Buy	↔	CMP: **Rs. 242**	Price Target: **Rs. 300**	↑

↑ Upgrade ↔ Maintain ↓ Downgrade

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		↔	

ESG Disclosure Score NEW

ESG RISK RATING 28.69

Updated Jul 08, 2022

Medium Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

Company details

Market cap:	Rs. 10,443 cr
52-week high/low:	Rs. 275/182
NSE volume: (No of shares)	3.9 lakh
BSE code:	532953
NSE code:	VGUARD
Free float: (No of shares)	19 cr

Shareholding (%)

Promoters	55.9
FII	12.4
DIIs	18.1
Others	13.6

Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	-2.6	13.3	12.3	-6.5
Relative to Sensex	-4.1	-1.3	5.5	-10.1

Sharekhan Research, Bloomberg

Summary

- We retain our Buy rating on V-Guard Industries Limited (V-Guard) with a revised PT of Rs. 300, given its expansion into non-South markets, entry into new product categories, and volume-driven growth across verticals.
- The company aims to scale up in-house manufacturing to 75% to enhance competitiveness and efficiency, which will lead to margin improvement. Manufacturing facilities for fans, inverters, and batteries are expected to come on board in the near future.
- Premiumisation of fans, digital UPS, and market share gain in batteries and inverters would aid revenue growth and margins.
- Improving working capital cycle and cash flows as well as negligible debt provide us further comfort. We expect Revenue/PAT CAGR of ~19%/~22% over FY2022-FY2024E EPS.

V-Guard Industries Limited (V-Guard) is on the cusp of a high-growth trajectory, as it is deploying multiple levers for the next level of growth. The company is expanding its product portfolio in all divisions to widen its customer and geographical base. The company also intends to increase contribution of products such as batteries, inverters, and pumps in total revenue. Further, in fans, the company's focus lies on premiumisation, leading to higher realisation and margins. The company would increase the in-house manufacturing base to 75% in the coming years, leading to more cost competitiveness and efficiency. We expect margins to improve going forward, driven by strong volumes, price increases in key product categories, and deeper penetration into non-South markets. We expect Revenue/PAT CAGR of ~19%/~22% over FY2022-FY2024E EPS. Hence, we retain Buy on V-Guard with a revised price target (PT) of Rs. 300.

In-house manufacturing would enhance efficiency and profitability: The company is strategically moving towards in-house manufacturing to enhance competitiveness and efficiency. The company expects in-house manufacturing to increase to 75% from current 55-60% in the next two-three years as manufacturing facilities for fans, inverters, and batteries come on board with more additions in the non-south region. Thus, the company sees revenue contribution from non-South markets to exceed 50% over the next 3-4 years, thereby diversifying the business and improving its risk profile. V-Guard targets 15% volume growth in FY2023.

Product portfolio expansion would lead to penetration into new markets: In consumer durables, the company has expanded its fans portfolio, targeting the mid-segment range in the decorative segment. The company expects good traction in the recently introduced BLDC fans segment, where it is preparing for the new energy-efficiency norms. V-Guard also introduced a range of water heaters to further strengthen portfolio in this segment during the year. The company launched a total of 377 new SKUs during FY2022 to expand the product portfolio to address the needs of neo consumers. The company aims 7% EBIT margin by January-March quarter in consumer durables. In electronics, its subsidiary V-Guard Consumer Products Limited's (VCPL) first plant has started operations with manufacturing of stabilisers; and by Q2FY2023, the plant would start production of inverters. In Electronics, in the digital UPS segment, the company has undertaken several initiatives towards premiumisation, which will enable deeper consumer engagement, better pricing power, and higher margins. In inverter and battery, the company has a mere 3% share in the Rs. 12,000 crore market, which provides wide scope for future growth.

Healthy demand, geographical expansion would drive earnings growth: The company expects healthy demand going forward as contribution from smaller product categories such as fans, batteries, inverters, and water heaters increases. Going ahead, margins would be driven by volume growth across categories, particularly with lower volume base. Further, an increase in in-house manufacturing would help the company become more cost competitive, thereby improving its market share. The company has continued to expand its market visibility and has grown its retailer base to over 50,000 touch points. The company seems well positioned to benefit from resilient customer demand based on its diversified product portfolio, increasing national presence (aims to add 3,000-4,000 dealers per annum), and capacity augmentation.

Revision in estimates – We have broadly maintained our FY2022-FY2024 estimates.

Our Call

Valuation – We maintain Buy with a revised PT of Rs. 300: V-Guard's future growth is likely to be led by expansion into non-South markets, introduction of new and innovative products, entry into additional product categories, volume-driven economies of scale, enhanced manufacturing capabilities, and technological improvements across products and processes. Operating profit margin (OPM) is expected to improve with price hikes, higher volumes, and increasing in-house manufacturing. Further, focus on increasing in-house manufacturing capacity would ensure better control on raw-material supply, thereby helping normalise inventory levels going forward. The company has a strong balance sheet and its cash flows and working capital cycle are expected to improve, backed by strong sales and earnings growth. Hence, we continue to maintain Buy on the stock with a revised PT of Rs. 300.

Key Risks

Relatively weak demand environment in some of the product categories may affect earnings.

Valuation (Standalone) Rs cr

Particulars	FY21	FY22	FY23E	FY24E
Net sales	2,699	3,475	4,098	4,913
OPM (%)	11.4	9.6	9.6	10.4
Net profit	199	227	251	335
% Y-o-Y growth	7.5	14	10.8	33.1
Adj. EPS (Rs.)	4.6	5.3	5.8	7.8
P/E (x)	52.5	46	41.6	31.2
P/B (x)	8.6	7.4	6.5	5.6
EV/EBIDTA (x)	30.9	29.8	24.9	19.1
RoNW (%)	18.1	17.4	16.7	19.2
RoCE (%)	26.1	22.6	22.8	26.1

Source: Company; Sharekhan estimates

In-house manufacturing would enhance efficiency and profitability

The company is strategically moving towards in-house manufacturing to enhance competitiveness and efficiency. The company expects in-house manufacturing to increase to 75% from 55-60% currently in the next two-three years as manufacturing facilities for fans, inverters, and batteries come on board with more additions in the non-south region. The company would invest Rs. 200 crore in capacity augmentation over the next three fiscals. Thus, the company sees revenue contribution from non-south markets to exceed 50% over the next 3-4 years, thereby diversifying the business and improving its risk profile. V-Guard targets 15% volume growth in FY2023.

Strategically located manufacturing facilities

Location	Products
Coimbatore, Tamil Nadu	House wiring cables, solar inverter, pump and motors, PVC compounding
Perundurai, Tamil Nadu	Solar water heater
Kashipur, Uttarak-hand	House wiring cables
Roorkee, Uttrakhand	Ceiling fan
Kala Amb, Himachal Pradesh	Electric water heater
Sikkim	Stabilizer, electric water heater

Source: Company, Sharekhan Research

Product portfolio expansion would lead to penetration into new markets

In consumer durables, the company has expanded its fans portfolio, targeting the mid-segment range in the decorative segment. The company expects good traction in the recently introduced BLDC fans segment, where it is preparing for the new energy-efficiency norms. The company is focusing on in-house manufacturing of premium category fans. Currently, premium fans are 40-50% of the total fan sales and its share is expected to rise as BLDC energy-efficient fans gain traction. The company also introduced a range of water heaters to further strengthen portfolio in this segment during the year. In water heaters, the company has regained its lost share and the growth trajectory is promising. Further, Sikkim plant expansion has helped strengthen the production of water heaters, with reduced dependence on Chinese imports. The plant, which primarily produces all types of vitreous-coated tanks, reported about 70% capacity utilisation in FY2022 and is likely to go up further in FY2023. The company launched a total of 377 new SKUs during FY2022 to expand the product portfolio to address the needs of new consumers. The company aims 7% EBIT margin by January-March quarter in consumer durables.

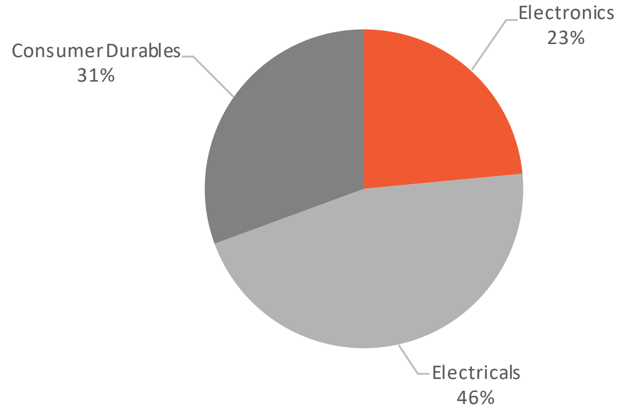
In electronics, VCPL's first plant has started operations with manufacturing of stabilisers; and by Q2FY2023, the plant would start production of inverters. The company has invested about Rs. 60 crore in VCPL's plant. In electronics, in the digital UPS segment, the company has undertaken several initiatives towards premiumisation, which will enable deeper consumer engagement, better pricing power, and higher margins. This category is a key growth driver for the company as it continues to expand into under-penetrated regions that are power deficient with regular outages. In inverter and battery, the company has a mere 3% share in the Rs. 12,000 crore market, which provides wide scope for future growth.

Diversified product basket

Electronics	Stabilisers, inverters, batteries, solar power system
Electrical	House wiring cables, switchgears, modular switches, pumps
Consumer Durables	Solar and electric water heaters, fans , air coolers, and kitchen appli-ances

Source: Company, Sharekhan Research

Segment-wise revenue break-up (%)



Source: Company, Sharekhan Research

Electricals segment to witness strong growth

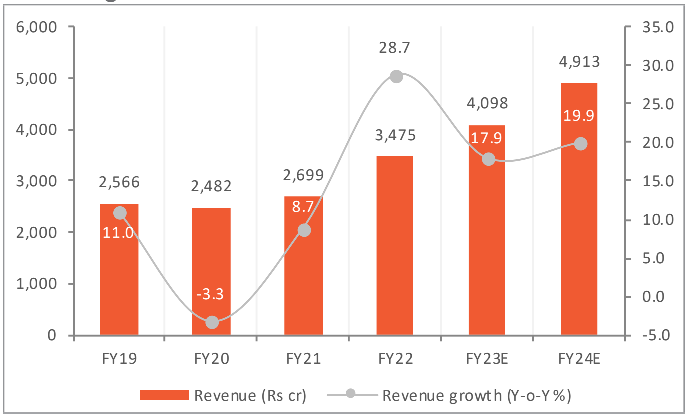
The company's electricals segment is the largest revenue contributor and includes construction-dependent product categories. House wiring cables is the largest product category for the company. Growth for this category has rebound and has witnessed significant price hikes by all major players. Pumps contribute ~10% to total electricals segment's revenue. The category has seen multiple rounds of price increases; however, volumes and margins are still subdued in this category but are expected to improve going forward. Thus, we expect the electricals segment is expected to post healthy sales and earnings over the next two-three years.

Healthy demand, geographical expansion would drive earnings growth

The company expects healthy demand going forward as contribution from smaller categories such as fans, batteries, inverters, and water heaters increases. Going ahead, margins would be driven by volume growth across categories, particularly with lower volume base. Further, an increase in in-house manufacturing would help the company become more cost competitive, thereby improving its market share. The company has continued to expand its market visibility and has grown its retailer base to over 50,000 touch points. The company seems well positioned to benefit from resilient customer demand based on its diversified product portfolio, increasing national presence (aims to add 3,000-4,000 dealers per annum), and capacity augmentation.

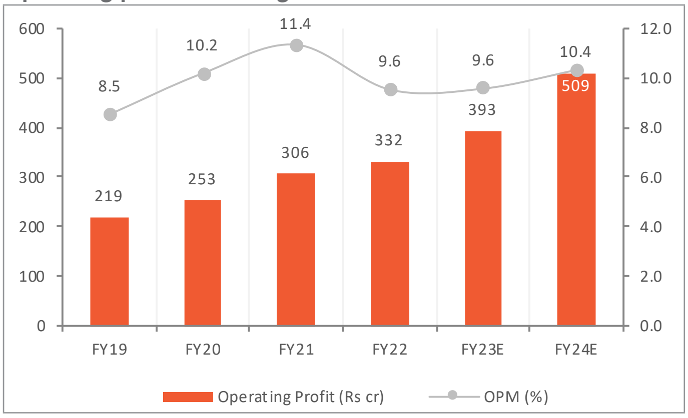
Financials in charts

Revenue growth trend



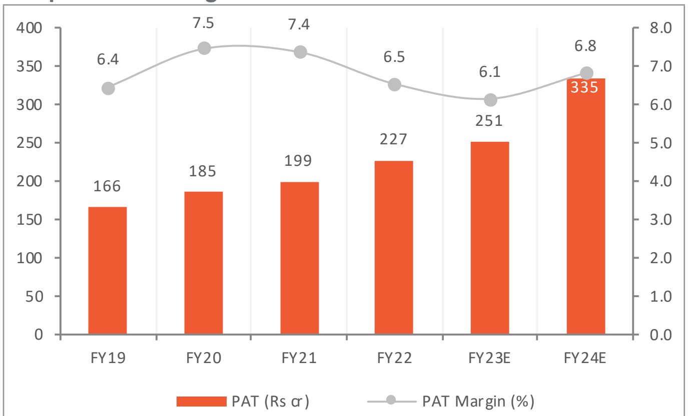
Source: Sharekhan Research

Operating profit and margin trend



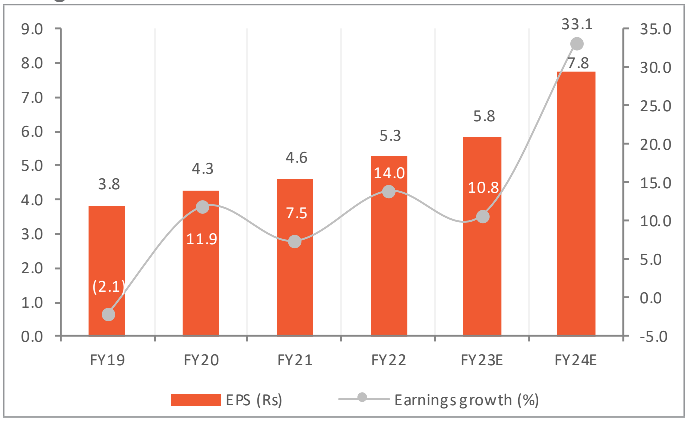
Source: Sharekhan Research

Net profit and margin trend



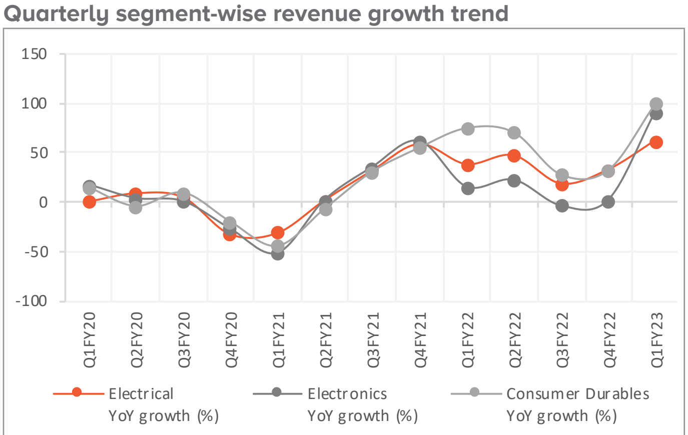
Source: Sharekhan Research

EPS growth trend



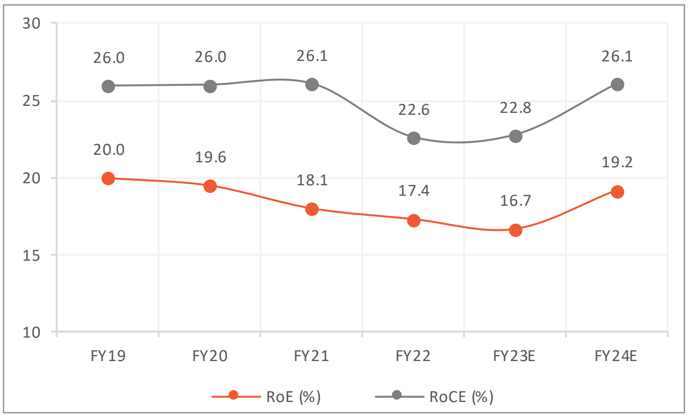
Source: Sharekhan Research

Quarterly segment-wise revenue growth trend



Source: Sharekhan Research

Return Ratios trend



Source: Sharekhan Research

Outlook and Valuation

■ Sector View – Growth momentum to continue in the medium to long term

The consumer durable/electrical industry has seen good demand since H2FY2021, the momentum of which is expected to continue further. The government's Atmanirbhar Bharat initiative is expected to benefit with capital subsidies and industrial benefit policies being doled out to give a push to in-house manufacturing. Further, demand for electricals and electronics from the housing sector has been robust due to low-interest cost and ease of financing. Management expects better supply security and margin improvement with an increase in in-house manufacturing. Healthy cash positions are likely to aid companies in inorganic growth opportunities, as organised players benefit from the tough environment.

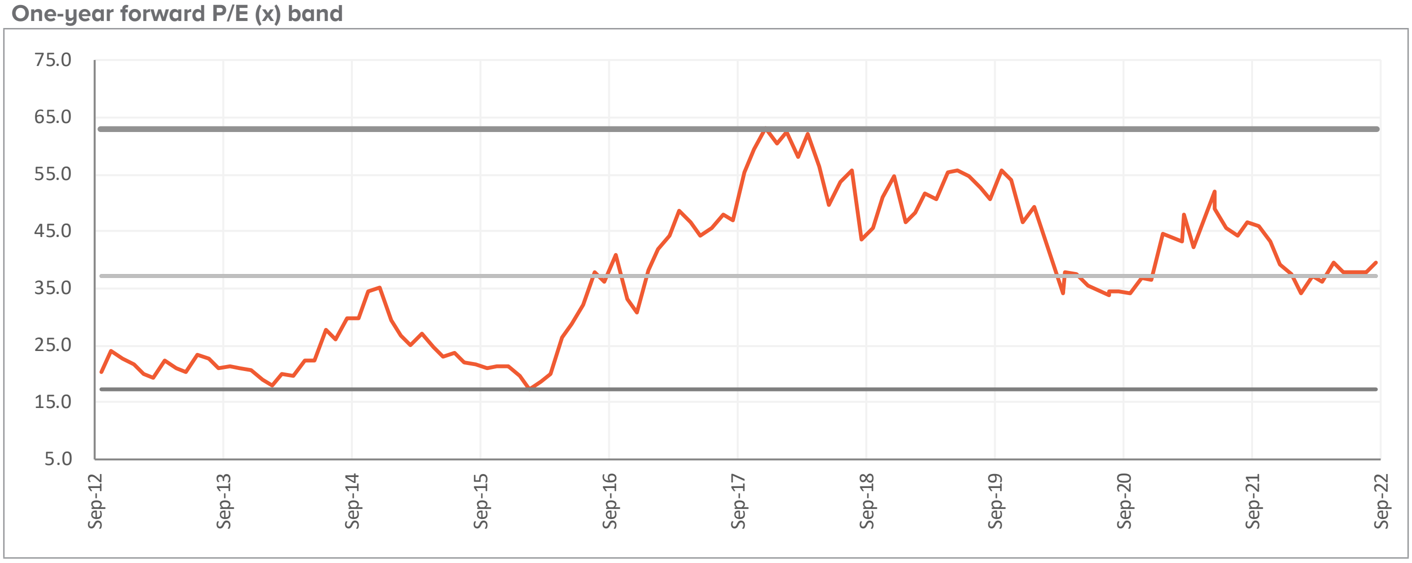
■ Company Outlook – Varied growth levers

Management expects healthy growth to sustain going forward. The company remains focused on 1) evolving category mix and product mix, 2) go-to-market with a focus on e-commerce and modern trade, and 3) distribution enhancement in smaller town and rural along with an increase in the non-south region. The company expects to add 3,000-4,000 retailers every year in the non-south region. V-Guard has 40,000 retail points – around 18,000 in the south and balance in non-south with continuous additions. Overall, management is focusing on maintaining a healthy cash position, cost rationalisation, and expediting digitisation.

■ Valuation – We maintain Buy with a revised PT of Rs. 300

V-Guard's future growth is likely to be led by expansion into non-South markets, introduction of new and innovative products, entry into additional product categories, volume-driven economies of scale, enhanced manufacturing capabilities, and technological improvements across products and processes. Operating profit margin (OPM) is expected to improve with price hikes, higher volumes, and increasing in-house manufacturing. Further, focus on increasing in-house manufacturing capacity would ensure better control on raw-material supply, thereby helping normalise inventory levels going forward. The company has a strong balance sheet and its cash flows and working capital cycle are expected to improve, backed by strong sales and earnings growth. Hence, we continue to maintain Buy on the stock with a revised PT of Rs. 300.

One-year forward P/E (x) band



Source: Sharekhan Research

About company

V-Guard is a major electrical appliances manufacturer in India and the largest in Kerala. The company is one of India's consumers goods companies with diversified product offerings. Headquartered in Kochi, Kerala, the company now has over 500 distributors, 30,000 retailers, and numerous branches across India. The company manufactures voltage stabilisers, electrical cables, electric pumps, electric motors, geysers, solar water heaters, air coolers, and UPSs. The company's business segments comprise electronics, electricals, and consumer durables, which contributed 23.5%, 30.6%, and 45.9%, respectively, to FY2022 revenue.

Investment theme

V-Guard is an established brand in the electrical and household goods space, particularly in south India. Over the years, the company has successfully ramped up its operations and network to become a multi-product company. The company has a strong presence in the southern region. The company is also aggressively expanding in non-south markets and is particularly focusing on tier-II and III cities, where there is immense demand for its products.

Key Risks

Relatively weak demand environment in southern and eastern regions may affect earnings in the near term.

Additional Data

Key management personnel

Mr. Kochouseph Chittilappilly	Chairman
Cherian Punnose	Vice-Chairman
Mithun K Chittilappilly	Managing Director
V Ramachandran	Director and Chief Operating Of-ficer
Sudarshan Kasturi	Senior VP and CFO

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	SBI Small Cap Fund	9.11
2	Arun K Chittilappilly	8.75
3	Kotak Small Cap Fund	5.27
4	Mithun Kochouseph Chittilappilly (anekha Chittilappilly Trust)	4.94
5	Kochouseph Thomas Chittilappilly	4.82
6	Kochouseph Chittilappilly	4.29
7	Nalanda India Equity Fund	4.23
8	Priya Sarah Cheeran Joseph	4.07
9	Nalanda India Fund	1.93
10	Aditya Birla Sun Life Trustee Private Limited	1.31

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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