Sharekhan by BNP PARIBAS

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Stock Update

Result Update

Polycab India Ltd

Strong Q3, growth momentum to continue

Capital Goods	Sharekhan code: POLYCAB

Reco/View: Buy ↔	CMP: Rs. 2,761	Price Target: Rs. 3,320 ↑

↑ 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 Updated Dec 08, 2022				25.10
Medium Risk				
NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

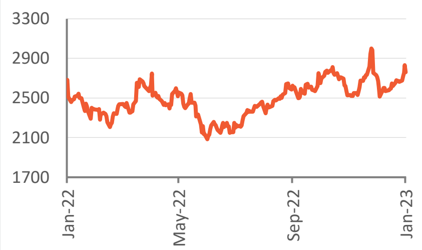
Company details

Market cap:	Rs. 41,261 cr
52-week high/low:	Rs. 3,025 / 2,044
NSE volume: (No of shares)	4.1 lakh
BSE code:	542652
NSE code:	POLYCAB
Free float: (No of shares)	4.8 cr

Shareholding (%)

Promoters	68.0
FII	6.4
DII	10.4
Others	15.2

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	3.6	4.6	25.8	6.6
Relative to Sensex	5.2	1.7	14.7	5.4

Sharekhan Research, Bloomberg

Summary

- Q3FY2023 performance was marked by strong volume growth of 18-20% in the Wires & Cables (W&C) business and significant improvement in profitability despite higher A&P spends.
- Increasing traction in exports, improvement in the FMEG segment, and sustained demand momentum in B2B/ B2C segments in W&C are key growth catalysts.
- The company has forayed into the EHV cables through a technological tie-up with Brugg Cables. It is setting up a manufacturing facility in Halol, Gujarat which would help cater to Rs. 4,000-5,000 crore EHV market by 2025.
- We retain a Buy on Polycab India Limited (Polycab) with a revised PT of Rs. 3,320 (based on FY25E EPS) given consistent outperformance versus peers, product portfolio expansion, market share gains and a healthy balance sheet.

Q3FY23 results exceeded our and street expectations on the profitability front. Its revenue grew by ~10% y-o-y to Rs 3,715crore (versus our estimate of Rs. 3,776 crore) driven by healthy volume growth in W&C. W&C revenue grew by ~11% y-o-y driven by domestic distribution business. However, FMEG sales remained flat, while others (EPC) segment posted growth of ~27% y-o-y. Operating profit grew by 39% y-o-y to Rs 504crore and OPM improved by 284 bps y-o-y to 13.6% (vs our estimate of 13%) due to better operating leverage despite input cost pressures and ~4x increase in A&P spends. Net profit grew by ~45% y-o-y to ~Rs 358 crore (Vs our estimate of Rs 330cr). EBIT margin in wires & cables segment (adjusting for inter-segment revenue) jumped to 14.1% (vs 10.3% in Q3FY22), while FMEG reported loss of Rs 3 mn at the EBIT level. As of December 31, 2022, net cash position improved to Rs. 1,870 crore vs Rs. 670 crore last year.

Key positives

- W&C business' volumes grew by 18-20% in Q3FY23 and total revenue grew by ~11% y-o-y driven by domestic distribution business.
- In Q3FY23, revenue contribution of wires has increased to 40% from 30% in the previous quarter. Higher contribution from wires led to an improvement in OPM as wires have margin of around 15%.
- For 9MFY23, volumes grew strongly by 26% y-o-y on the back of improving government spend and private capex cycle.
- Operating profit grew 39% y-o-y to Rs. 504 crore and OPM improved by 284 bps y-o-y to 13.6% (vs our estimate of 13%) due to better operating leverage despite input cost pressures and ~4x increase in advertising & promotion (A&P) spends.

Key negatives

- FMEG business had a weak quarter with flat revenues and a loss of Rs. 3 mn at the EBIT level.
- Gross margins declined by 40 bps q-o-q to 25.7% in Q3FY23.

Management Commentary

- The company expects exports to contribute ~8-10% to FY23 revenue. The company is seeing strong traction in its distribution business in exports. The company expects strong growth and profit trajectory in exports going forward.
- Polycab plans to enter Extra High Voltage (EHV) market and would build in-house manufacturing capacity. The market size is expected to be Rs 4,000-Rs 5,000 crore by 2025 and the company expects meaningful contribution from these products from FY26 onwards.
- In FMEG, the company believes that optimum product mix (increasing share of high-margin products like switchgear and switches), product innovation and high A&P spend should result in better revenue growth and profitability in the coming quarters.
- The company has cash & investments of Rs. 2,015 crore.

Revision in estimates – We have revised our earnings estimates upwards for FY2023/FY2024/FY2025 to build in higher profitability.

Our Call

Valuation – Retain Buy with a revised PT of Rs. 3,320: Polycab has successfully consolidated its leading position in the W&C industry by performing consistently. Going forward, growth in B2C business, continued demand momentum in B2B segment, scaling up FMEG business and exports are the key growth catalysts. Further, its foray into EHV segment bodes well from long-term prospects. In the long term, Polycab is expected to benefit from government infrastructure investments, increase in housing demand and pick up in private capex spending. We expect its operating performance to improve given robust volume growth and backward integration. The company is well poised for a healthy growth trajectory given its widening distribution network and in-house manufacturing capabilities. Hence, we maintain a Buy with a revised PT of Rs. 3,320 (rolling forward our estimates to FY25E EPS).

Key Risks

Fluctuations in raw-material prices and intense competition are key concerns.

Valuation (Consolidated) Rs cr

Particulars	FY22	FY23E	FY24E	FY25E
Revenues	12,204	14,193	16,398	18,843
OPM (%)	10.4	12.6	12.5	12.7
Adj. Net profit	845	1,211	1,385	1,615
Growth (Y-o-y) %	0.4	43.3	14.4	16.6
Adj. EPS (Rs)	56.7	81.2	92.9	108.3
PER (x)	48.7	34.0	29.7	25.5
P/B (x)	7.4	6.3	5.4	4.6
EV/EBIDTA (x)	29.6	21.0	18.1	15.4
RoCE (%)	21.7	27.2	26.4	26.1
RoNW (%)	16.4	20.1	19.5	19.3

Source: Company; Sharekhan estimates

Performance driven by healthy volume growth and operating leverage

Consolidated revenues grew by ~10% y-o-y to Rs 3,715crore (vs our estimate of Rs 3,776 crore) driven by healthy volume growth in the W&C business. Notably, the company registered highest ever quarterly production volumes in Q3FY23. W&C revenue grew by ~11% y-o-y driven by domestic distribution business. The merger of HDC and LDC verticals last year contributed to the outperformance. However, FMEG sales remained flat, while others (EPC) segment posted a ~27% y-o-y growth. On a positive note, FMEG sales reported growth of 12% q-o-q as October and November were stronger as compared to the months of Q2FY23, and demand picked up considerably in December. Operating profit grew by 39% y-o-y to Rs 504 crore and OPM improved by 284 bps y-o-y to 13.6% (versus our estimate of 13%) due to better operating leverage despite input cost pressures and ~4x increase in A&P spends. Net profit grew by ~45% y-o-y to ~Rs. 358 crore (versus our estimate of Rs 330 crore) led by strong operating profit and higher other income. EBIT margin in W&C (adjusting for inter-segment revenue) jumped to 14.1% (vs 10.3% in Q3FY22), while FMEG reported an EBIT loss of Rs 3 million. As of December 31, 2022, net cash position improved to Rs 1,870 crore versus Rs. 670 crore last year.

Turnaround of FMEG, traction in exports are the key growth enablers going forward

Polycab is confident of delivering strong performance as it aims to deliver industry leading growth in B2B in W&C through growth in both domestic and exports and scaling up of B2C business. It is also focused on ramping up FMEG business through realignment of its distribution strategy and merging of verticals. The company reiterated its initiative, Project Leap, through which it intends to achieve a revenue of Rs. 20,000 crore, by FY2026E and aims to grow faster than the industry. The company would incur an annual capex of ~Rs. 600 crore per annum for CY2023 of which 3/4th would be spent towards W&C segment including EHV and the rest would be towards FMEG for enhancing product portfolio and expanding market reach. Thus, Polycab is well poised for a sustainable and healthy growth in the medium to long term.

Key result highlights from Concall

- **Robust volumes and profitability in W&C segment:** In the W&C segment, revenue was driven by robust volume growth of 18-20% amid favorable demand. Apart from the distribution business, in wires, B2B segment is doing well as major demand is coming from real estate sector. In Q3FY23, revenue contribution of wires has increased to 40% from 30% in the previous quarter. Higher contribution from wires has led to improvement in OPM as wires margin are ~15%, while cables margin are ~ 11%. For 9MFY23, volume growth has been strong at 26% y-o-y on the back of improving government spend and private capex cycle.

- **Exports would be a key growth enabler in the long-term:** For 9MFY23, revenue from exports grew by 32% Y-o-y. Overall, exports business contributed to 5.9% of consolidated revenue in Q3FY23 and 8.6% in 9MFY23. The company expects exports to contribute ~8-10% to FY23 revenues. The company is seeing strong traction in its distribution business in exports. The company expects strong growth and profit trajectory in exports going forward.

- **Foray into EHV cables:** Polycab plans to enter Extra High Voltage (EHV) market through the EPC route. Power demand in tier-1 and tier-2 cities is constantly increasing and as smart cities are coming up, entire overhead high voltage transmission line conductors would have to go underground and thus demand for high voltage and extra high-voltage cables would increase exponentially. Also, transmission lines are being upgraded to 400 KV and 550KV. Thus, in order to capitalize this opportunity, the company is kicking off EHV production line in Halol, Gujarat and expects the production to start in 2025. For this purpose, the company has entered into a technology tie-up with Swiss company called Brugg Cables in which the latter would transfer technology for upto 550 KV voltage products to Polycab. This would help the company cater to a Rs. 4,000-5,000 crore market by FY26. It also opens the door for the company in the export markets. Thus, the company has raised its capex guidance to Rs 600 crore for 2023 of which three-fourths would be utilised for W&C including EHV and the rest would go towards scaling up FMEG business and exports. Currently, there are only two key large players in the EHV space.

- **FMEG segment should grow substantially in the coming years:** In Q3FY23, the fans business saw good growth as distributors started restocking ahead of transition to the new BEE norms. Switchgears business witnessed healthy growth driven by the company's influencer incentive program. Pipes & fittings and switches businesses too posted decent growth. The company is pulling several levers in order to grow its FMEG business. Firstly, it is working out the right optimum product mix in the FMEG category. Currently, fans and lighting comprise 2/3 of the revenues. However, the company is keen on expanding presence in high margin products like switchgear and switches. For this purpose, the company is coming up with a new facility in Daman for switches and is also expanding its Nasik switchgear facility. Also, Sylvan innovation labs, a subsidiary of the company is carrying out R&D and innovation and the company should be able to improve its product portfolio and command a premium in the market in the coming years. Further, the company has been spending considerable amount on advertising and promotion and improving product availability, which should result in better revenue growth and profitability in the coming quarters.

- **Capex plans:** The company plans to incur capex of Rs 600 crore in calendar year 2023 of which 3/4th would go towards W&C and rest should be utilised for scaling up of FMEG business and exports.
- **Raw material sourcing mix:** Copper is largely sourced from overseas, while aluminum is sourced mostly from domestic sources.

Results (Consolidated) Rs cr

Particulars	Q3FY23	Q3FY22	Y-o-Y %	Q2FY23	Q-o-Q %
Net Sales	3,715	3,372	10.2	3,332	11.5
Operating profit	504	362	39.3	428	17.8
Other Income	40	22	83.3	(2)	NM
Interest	9	8	18.5	14	-33.4
Depreciation	52	51	2.6	52	0.4
PBT	482	324	48.5	359	34.1
Tax	120	76	57.5	88	36.6
Reported PAT	361	248	45.3	270	33.4
Adjusted PAT	358	247	45.0	268	33.6
Adj. EPS (Rs.)	23.9	16.5	45.0	17.9	33.6
Margin			**BPS**		**BPS**
GPM (%)	25.7	22.6	309	26.1	-40
OPM (%)	13.6	10.7	284	12.8	73
NPM (%)	9.6	7.3	231	8.0	159
Tax rate (%)	25.0	23.5	148	24.5	51

Source: Company; Sharekhan Research

Segment wise revenue break-up

Particulars	Q3FY23	Q3FY22	Y-o-Y %	Q2FY23	Q-o-Q %
Net sales					
*Wires & Cables (W&C)	3,259	2,943	10.7	2,901	12.3
FMEG	342	340	0.5	305	12.0
Others	126	99	27.4	105	19.9
Total Net sales	**3,727**	**3,383**	**10.2**	**3,312**	**12.5**
PBIT					
Wires & Cables (W&C)	459	302	51.9	346	32.6
FMEG	-2	6	NM	-3	-10.8
Others	15	13	20.3	16	-4.2
Total PBIT	**472**	**321**	**46.9**	**359**	**31.3**
PBIT Margin (%)			**BPS**		**BPS**
Wires & Cables (W&C)	14.1	10.3	382	11.9	216
FMEG	-0.7	1.8	NM	-0.9	NM
Others	12.1	12.8	-71	15.1	-304

*Source: Company Data, Sharekhan research, * adjusted for inter-segment revenue*

Outlook and Valuation

Sector View – Ample scope for growth:

The W&C industry contributes 40-45% of India's electrical equipment industry. In terms of volumes, the Indian W&C industry (including exports) has grown from 6.3 million km in FY2014 to 14.5 million km 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 W&C industry is expected to register a 14.5% CAGR from Rs. 52,500 crore in FY2018 to Rs. 1,03,300 crore by FY2023. The government has envisaged Rs. 111 lakh crore capital expenditure in infrastructure sectors in India during FY2020 to FY2025. The continued thrust of the government on infrastructure investment is expected to improve demand 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, urbanization, 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.

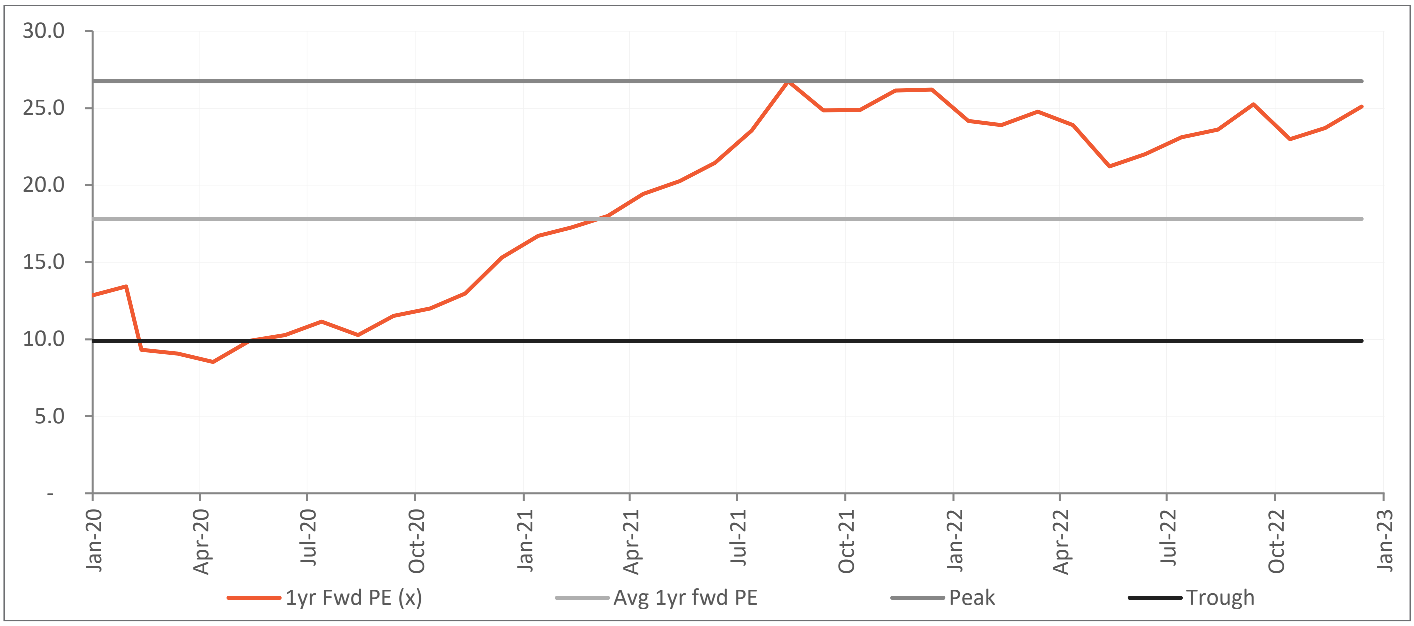
Company Outlook – Growth prospects bright

Overall, the outlook remains positive despite near-term challenges, which remains transient given the growth prospects ahead through various initiatives taken by the company such as Project Udaan and Project Leap. Polycab has gained share in the organized market (20-22% from 18% in FY2020), auguring well for growth. The company has outlined its new initiative Project Leap through which it intends to achieve Rs. 20,000 crore in revenues by FY2026E on superior growth versus the industry in B2C segments (2x in FMEG and 1.5x in retail wires) and stronger position in B2B segments.

Valuation – Retain Buy with a revised PT of Rs. 3,320

Polycab has successfully consolidated its leading position in the W&C industry by performing consistently. Going forward, growth in B2C business, continued demand momentum in B2B segment, scaling up FMEG business and exports are the key growth catalysts. Further, its foray into EHV segment bodes well from long-term prospects. In the long term, Polycab is expected to benefit from government infrastructure investments, increase in housing demand and pick up in private capex spending. We expect its operating performance to improve given robust volume growth and backward integration. The company is well poised for a healthy growth trajectory given its widening distribution network and in-house manufacturing capabilities. Hence, we maintain a Buy with a revised PT of Rs. 3,320 (rolling forward our estimates to FY25E EPS).

One-year forward P/E (x) band



Source: Company, 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. POLYCAB's five-year roadmap to achieve to achieve Rs. 20,000 crore in FY2026E with more focus towards brand positioning, operations and business growth along with strong emphasis on governance and sustainability outpacing the industry's growth provides healthy visibility ahead. Revenue from the wires and cable segment has seen a decent 14.4% CAGR during FY2018-FY2022 and FMEG grew by ~27% CAGR during the same period. Further, increasing market share of organized players, which grew from 61% in FY2014 to 66% in FY2018, is expected to touch 74% in FY2023E, which augurs well for the industry leaders.

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) could impact margins.
- **Increasing competition:** W&C and FMEG industry is highly fragmented and has many unorganized players. Hence, competitive intensity is high.

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	Chief Financial Officer

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Dsp Investment Managers Pvt Ltd	1.62
2	Aditya Birla Sun Life Asset Management Ltd	1.21
3	Capital Group Cos Inc	0.87
4	Vanguard Group Inc	0.78
5	Canara Robeco Asset Management Co Ltd	0.77
6	Sundaram Asset Management Co Ltd	0.68
7	T Rowe Price Group Inc	0.67
8	Tata Asset Management Pvt Ltd	0.56
9	Nippon Life Asset Management	0.47
10	Blackrock Inc	0.47

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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