Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Supreme Industries Ltd

Strong Q3; Demand buoyancy to sustain

Building Materials	Sharekhan code: SUPREMEIND
Reco/View: Buy ↔	CMP: Rs. 2,399
	Price Target: Rs. 2,800 ↑

↑ 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 22.79

Updated Dec 08, 2022

Medium Risk

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

Source: Morningstar

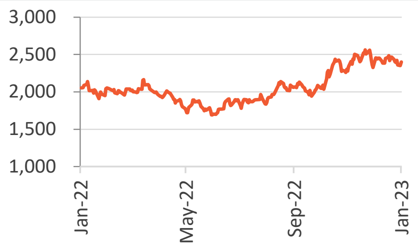
Company details

Market cap:	Rs. 30,475 cr
52-week high/low:	Rs. 2,605/1,669
NSE volume: (No of shares)	4.3 lakh
BSE code:	509930
NSE code:	SUPREMEIND
Free float: (No of shares)	6.5 cr

Shareholding (%)

FII	17
Institutions	19
Public & others	15
Promoters	49

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-2.3	17.3	32.0	16.9
Relative to Sensex	-3.0	14.9	22.7	11.5

Sharekhan Research, Bloomberg

Summary

- We retain Buy on Supreme Industries Limited (SIL) with a revised PT of Rs. 2,800, rolling forward our valuation multiple to FY2025E earnings and considering its healthy earnings growth outlook.
- SIL reported better-than-expected consolidated net profit for Q3FY2023 led by robust volume growth in plastic piping along with higher than expected overall OPMs. Net cash surplus increased q-o-q.
- Management upped plastic piping volume guidance to 35% plus for FY2023 and overall OPM to 12.5%+. Range bound PVC prices along with healthy demand is expected to drive earnings growth going ahead.
- Capex of Rs. 700 crore, including carry-forward commitments majorly to augment plastic piping capacities, is likely to aid in strong volume growth.

Supreme Industries Limited (SIL) reported better-than-expected consolidated net earnings for Q3FY2023, owing to robust volume growth in plastic piping and better-than-expected OPM. Consolidated revenue increased by 18.8% y-o-y to Rs. 2,311 crores, led by 51.4% y-o-y growth in plastic goods volumes (plastic piping reported 82% y-o-y volume growth). Lower PVC prices and re-stocking by retailers, improved business substantially in December. Further, consolidated OPM at 13.1% (down 321bps y-o-y, up 608bps q-o-q) came in better than our estimate of 12%. Consequently, operating profit (Rs. 303 crore, down 4.6% y-o-y) and net profit (Rs. 210 crore, down 14.5% y-o-y) were much ahead of our estimates. Strong Q3FY2023 performance led to management revising FY2023 volume guidance for plastic piping to 35% plus from 25% plus. It retained Rs. 9000 crore revenue target for FY2023 while upping OPM guidance to 12.5% plus (earlier 12-12.5%). It expects PVC prices to remain range-bound supporting healthy volume growth per annum post FY2023 while OPM are expected to normalize to 15-16% (assuming no steep volatility in PVC prices).

Key positives

- Higher-than-expected volume growth of 51% y-o-y led by 82% y-o-y growth in plastic piping.
- Turnover from value-added products increased by 24% y-o-y to Rs. 826 crores.
- Cash surplus increased to Rs. 687 crores from Rs. 493 crores in Q2FY2023.

Key negatives

- Packaging products registered a 12% y-o-y decline in volumes owing to fall in demand for cross-laminated products owing to lookalike products available at 30-40% lower prices.
- Consumer products reported 5.5% y-o-y decline in volumes and 9.1% y-o-y dip in revenues.

Management Commentary

- The company upped plastic piping volume growth of 35% plus y-o-y (earlier 25% plus) for FY2023, while overall volume growth is estimated at 25% y-o-y. It retained a consolidated revenues target of Rs. 9000 crore for FY2023.
- The EBITDA margin for FY2023 is expected to be 12.5%+ (earlier 12-12.5%). Over the next five years, it expects piping volume growth of 15% p.a., led by growth across agri, housing and infra sectors. The normalised OPM are pegged at 15-16%.
- PVC resin prices which have dropped by Rs. 66 per kg i.e 45% since April 2022 till November 2022, have recovered again by Rs. 15 per kg. since then. It looks like prices of PVC would remain range bound, which augurs well for the business.

Revision in estimates – We have fine-tuned our estimates for FY2023-FY2025.

Our Call

Valuation – Maintain Buy with a revised PT of Rs. 2,800: SIL is expected to benefit from sustained housing and infrastructure demand along with a strong demand outlook from the agri segment. The range bound polymer prices is expected to lead to healthy volume growth for the company going ahead. Additionally, lesser volatility in PVC prices is expected to lead to normalizing OPM of 15-16% from FY2024. The company's aggressive expansion plans, funded entirely through internal accruals, are expected to keep its balance sheet strong. A healthy demand outlook, along with incremental capacity additions, is likely to provide double-digit net earnings growth over FY2022-FY2025. We retain our Buy rating on the stock with a revised price target (PT) of Rs. 2,800, rolling forward our valuation multiple to FY2025E and considering its healthy earnings growth outlook.

Key Risks

The demand slowdown could affect revenue growth. Adverse commodity price fluctuation might impact the margin profile.

Valuation (Consolidated) Rs cr

Particulars	FY22	FY23E	FY24E	FY25E
Revenue	7,773	9,118	10,186	11,320
OPM (%)	16.0	12.5	15.1	15.6
Adjusted PAT	968	839	1,184	1,374
% YoY growth	(1.0)	(13.3)	41.1	16.0
Adjusted EPS (Rs.)	76.3	66.1	93.3	108.2
P/E (x)	31.5	36.3	25.7	22.2
P/B (x)	7.9	6.9	5.9	5.0
EV/EBITDA (x)	23.7	25.4	18.6	16.1
RoNW (%)	25.2	19.1	23.0	22.7
RoCE (%)	25.3	19.1	23.2	23.1

Source: Company; Sharekhan estimates

Strong outperformance led by plastic piping volume growth

The company reported consolidated net revenues of Rs. 2311 crore, up 18.8% y-o-y (up 10.7% q-o-q) which was 21% higher than our estimate. The company's volume grew by 51.4% y-o-y, led by strong volume growth in plastic piping (+82% y-o-y) and industrial products (+19.6% y-o-y) while Packaging (-12.3% y-o-y) and consumer products (-5.5% y-o-y) registered volume decline. The low prices of PVC and re-stocking by the retail chain improved business substantially in December. The turnover from value-added products grew by 24.2% y-o-y to Rs. 826 crore. Revenues from Plastic Piping/Packaging/Industrial/consumer products were +31.4%/-7.5%/23.7%/-9.1% y-o-y at Rs. 1509/342/336/116 crore. The OPM came in better than the estimate at 13.1% (down 321 bps y-o-y, up 608 bps q-o-q) as against our estimate of 12%. Gross profit margins declined by 326bps y-o-y at 28.8% (up 554bps q-o-q). Lower OPM y-o-y led to 4.6% y-o-y de-growth in operating profit at Rs. 303 crore, which was 33% higher than our estimate. Lower OPM y-o-y, along with lower income from JV, led to a 14.5% y-o-y decline in consolidated net profit at Rs. 210 crore, which was 21% higher than our estimate. The company's net cash surplus increased to Rs. 826 crores from Rs. 493 crores in Q2FY2023. The company expects to achieve 35% plus volume growth for FY2023. The Company's envisaged Capex plan of 700 crores for the year, including carried forward commitment of Rs. 280 crores is progressing with a little delay.

Key Conference Call Takeaways

- **Guidance:** The company upped plastic piping volume growth of 35% plus y-o-y (earlier 25% plus) for FY2023, while overall volume growth is estimated at 25% y-o-y. It retained a consolidated revenues target of Rs. 9000 crores for FY2023. The EBITDA margin for FY2023 is expected to be 12.5%+ (earlier 12-12.5%). Over next five years, it expects piping volume growth of 15% p.a. led by growth across agri, housing and infra sectors. The normalised OPM are pegged at 15-16%.
- **Q3FY2023 performance:** The company sold 1,38,362 tonnes, up 51% y-o-y plastic goods for Q3FY2023. The low prices of PVC and re-stocking by the retail chain improved business substantially in December. CPVC volumes grew by 32% y-o-y during 9MFY2023.
- **Segment-wise performance:** Segmentwise volume and value growth were as follows Plastic piping (82%/31%), Packaging (-12%/-7%), Industrial Products (20%/24%) and consumer products (-5%/-9%). Value-added products grew 24% y-o-y at Rs. 826 crores. Cash surplus stood at Rs. 687 crores versus Rs. 493 crores as on Q2FY2023.
- **Capacity addition:** The company is planning to reaching 8,13,000 tonnes by FY2023 end. The segment-wise capacity at the end of FY2023 will be as follows Plastic Piping 610,000 tonnes, Industrial products 83000 tonnes, Packaging 90,000 tonnes and Consumer products 30,000 tonnes.
- **PVC outlook:** PVC resin prices which have dropped by Rs. 66 per kg i.e 45% from April 2022 till November 2022 have recovered again by Rs. 15 per kg. since then. PVC are likely to remain range bound which augurs well for the business.
- **Packaging products:** The segment registered y-o-y decline in volumes and value due to fall in demand for cross laminated products (lookalike products sold at 30-40% lower prices).
- **Plastic pipe industry:** The industry is expected to grow its volumes by 21% y-o-y for FY2023 while the company is expected to grow its volumes at 35%.

Results (Consolidated) **Rs cr**

Particulars	Q3FY23	Q3FY22	YoY (%)	Q2FY23	QoQ (%)
Revenue	**2,310.7**	**1,945.1**	**18.8**	**2,086.6**	**10.7**
Total expenditure	2,007.4	1,627.2	23.4	1,939.5	3.5
EBITDA	**303.4**	**317.9**	**-4.6**	**147.1**	**106.2**
Depreciation	64.8	57.5	12.7	64.9	-0.1
EBIT	**238.6**	**260.4**	**-8.4**	**82.3**	**190.0**
Other income	8.3	2.9	182.0	5.5	50.2
Interest expenses	1.2	0.5	150.0	1.2	-4.2
PBT	**245.7**	**262.9**	**-6.5**	**86.6**	**183.8**
Tax expenses	63.3	67.8	-6.7	23.1	173.5
Share of profit from associate	-27.6	-50.7	-45.5	-18.6	48.6
Adjusted net profit	210.0	245.7	-14.5	82.0	156.1
Extra ordinary itmes	0.0	0.0	-	0.0	-
Reported net profit	**210.0**	**245.7**	**-14.5**	**82.0**	**156.1**
Adjusted EPS (Rs.)	16.5	19.3	-14.5	6.5	156.1
			BPS		**BPS**
EBITDA Margin (%)	13.1	16.3	-320	7.1	600
PAT Margin (%)	9.1	12.6	-350	3.9	520
Effective tax rate (%)	25.8	25.8	0	26.7	-90

Source: Company, Sharekhan Research

Outlook and Valuation

Sector view - Expect faster recovery in operations

The building materials industry was severely affected by the COVID-19-led lockdown during Q1FY2021, which affected its peak sales period. Additionally, its high fixed cost structure had affected OPM, dragging down its net earnings. However, from June, the sector has been one of the fastest to recover as the lockdown eased. The sector witnessed a resumption of dealer and distribution networks and a sharp improvement in capacity utilisation. Most players have begun to see demand and revenue run-rate reaching 80-90% as compared to pre-COVID levels. Scaling up of revenue is also expected to lead to better absorption of fixed costs going ahead, aiding net earnings recovery. The industry is expected to rebound with strong growth in FY2022.

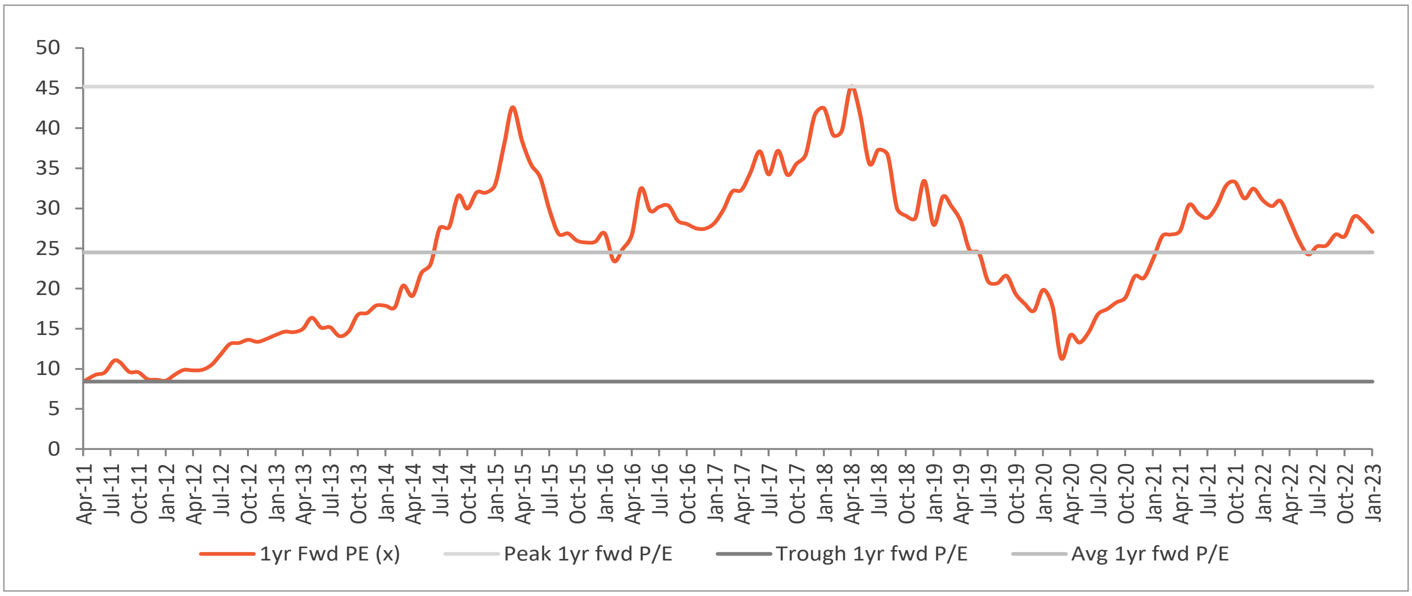
Company outlook - Eyeing healthy demand growth

The company is witnessing a pick-up in demand from metros in the housing sector. Demand for all its products remains strong along with a healthy revival in the agriculture sector. The company has gained market share during FY2022 in both PVC and CPVC segments and is expected to outperform in FY2023. SIL witnessed positive sales growth for July 2021 to date. Management remains optimistic about reporting minimum 35% y-o-y volume growth in plastic piping for FY2023. It expects OPM at 12.5% plus owing to strong OPM during Q3FY2023. It is expecting healthy demand from the infrastructure and housing sectors along with demand emanating from 'Nal Se Jal' scheme going ahead. The company has a capital expenditure plan of Rs. 700 crore, which would be entirely funded through internal accruals.

Valuation - Maintain Buy with a revised PT of Rs. 2,800

SIL is expected to benefit from sustained housing and infrastructure demand along with strong demand outlook from the agri segment. The range-bound polymer prices is expected to lead to healthy volume growth for the company going ahead. Additionally, lesser volatility in PVC prices is expected to normalizing OPM of 15-16% from FY2024. The company's aggressive expansion plans, funded entirely through internal accruals, are expected to keep its balance sheet strong. A healthy demand outlook, along with incremental capacity additions, is likely to provide double-digit net earnings growth over FY2022-FY2025. We retain our Buy rating on the stock with a revised price target (PT) of Rs. 2,800, rolling forward our valuation multiple to FY2025E and considering its healthy earnings growth outlook.

One-year forward P/E (x) band



Source: Sharekhan Research

Peer Comparison

Companies	P/E (x)		EV/EBITDA (x)		P/BV (x)		RoE (%)	
	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E
Supreme Industries	36.3	25.7	25.4	18.6	6.9	5.9	19.1	23.0
Astral Poly Technik	100.7	73.2	56.7	43.4	14.9	12.4	15.9	18.5

Source: Company; Sharekhan Research

About company

SIL is a leading manufacturer of plastic products with a significant presence across piping, packaging, industrial, and consumer segments. The company has emerged as one of the best proxy plays on growing plastic consumption in India because of a diversified product portfolio, an extensive distribution network, an improved capital structure, and the Government's thrust on building better infrastructure.

Investment theme

SIL is on a firm footing, with a strong product portfolio and new product launches, expected to drive growth in the coming years. The government's thrust on affordable housing and enhanced allocation towards irrigation projects will aid future growth for companies such as SIL. We remain positive about introducing value-added products and capacity expansion plans, which are largely funded by robust internal accruals. SIL enjoys superior return ratios with low gearing levels, and we expect the company to maintain high return ratios going forward.

Key Risks

Slowdown in demand offtake from the user industry can impact revenue growth rates. Adverse commodity price fluctuation might impact margin profile.

Additional Data

Key management personnel

Bajranglal Surajmal Taparia	Non Executive Chairman
Mahavirprasad Surajmal Taparia	Executive Director
ShivratanJeetmal Taparia	Executive Director
Vijaykumar Bajranglal Taparia	Executive Director
P C Somani	Chief Finance Officer
Rajendra J Saboo	AVP (Corporate Affairs) & Company Secretary & Compliance Officer

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Jovial Investment & Trading	16.12
2	Boon Investment & Trading	16.11
3	Venktesh Investment & Trading	14.20
4	Kotak Mahindra Asset Management	4.85
5	Nalanda India Fund Ltd	4.81
6	DSP Investment Managers	4.08
7	HDFC Asset Management	2.22
8	Axis Asset Management	2.07
9	Vanguard Group Inc	1.93
10	GOVERNMENT PENSION FUND - GLOBAL	1.79

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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