

24 October 2023

India | Equity Research | Q2FY24 Result Review

Finolex Industries

Plastic

Insipid Q2 result; future demand-margin scenario remains healthy

Finolex Industries (FNXP) has reported a tepid Q2FY24 pipe volume growth of 6.2% YoY (-31.7% QoQ, 4-year CAGR of 7.0%) on a low base due to lukewarm demand from agriculture segment (60% volume mix in Q2). Consolidated EBITDA margin contracted 127bps QoQ to 11.7% (vs EBITDA loss of ~INR 1.4bn YoY) due to lower profitability in pipes segment (EBIT/kg down 21.7% QoQ to INR 10.7). Profitability for pipes was lower QoQ due to significant decline in volumes resulting in negative operating leverage. Management has guided for pipe volume growth of 15-20% YoY in FY24 as PVC prices have now stabilised (post INR 10 decline in Oct'23-TD). It has guided for EBIT/kg in resin at INR 7-8 and for pipes at INR 10-12 in FY24. We cut our PAT estimates for FY24E by ~5% (FY25E, FY26E remain broadly unchanged) and maintain **BUY** with a rolled over SoTP-based Dec'24E target price of INR 237 (vs INR 230 earlier).

Tepid pipe volume growth of 6.2% YoY in Q2FY24

FNXP reported Q2FY24 pipe volume growth of 6.2% YoY (-31.7% QoQ, 4-year CAGR of 7.0%) on a low base, whereas PVC resin segment volume declined 30.6% YoY (-18.6% QoQ). Pipe volume growth was driven by continued demand from plumbing segment, whereas agri demand was dull (in anticipation of PVC price decline in Sep'23). PVC resin volume declined in Q2 due to supply issues from the Middle East, which are now resolving gradually. Management indicated PVC price has now stabilised (after declining INR10 in Oct'23-TD); it expects improved volumes going forward from agri segment which is very price elastic, and has thereby, guided for pipe volume growth of 15-20% YoY and resin volume of 0.2-0.22mn te in FY24. We model pipe volume CAGR of 10.2% over FY23-26E.

Lower pipe profitability in Q2FY24

Consolidated EBITDA margin declined 127bps QoQ to 11.7% (vs EBITDA loss of INR 1.4bn YoY) in Q2FY24 due to lower-than-expected profitability in both pipes and resin segments. Pipes EBIT/kg declined 21.7% QoQ to INR 10.7/kg (vs INR (-8)/kg YoY) due to lower volumes which led to negative operating leverage, and resin segment profitability grew 703% QoQ to INR 5.4/kg (vs avg FY14-23 EBIT/kg of INR 13.5). Resin profitability should improve as management indicated spreads are likely to normalise going ahead. It has guided for EBIT/kg of INR 7-8 for resin and INR 10-12 for pipes in FY24. We have modelled in FY24E/FY25E/26E resin EBIT/kg of ~INR 8-12 and pipe EBIT/kg of INR 11.5-12.5.

Financial Summary

Y/E March (INR mn)	FY23A	FY24E	FY25E	FY26E
Net Revenue	43,971	42,216	46,078	50,736
EBITDA	3,258	6,871	8,202	8,766
EBITDA %	7.4	16.3	17.8	17.3
Net Profit	2,149	5,524	6,203	6,597
EPS (Rs)	3.5	8.9	10.0	10.7
EPS % Chg YoY	(73.0)	157.1	12.3	6.3
P/E (x)	58.3	22.7	20.2	19.0
EV/EBITDA (x)	34.5	16.1	13.2	12.1
RoCE (%)	3.2	7.4	8.5	8.6
RoE (%)	4.9	10.9	11.5	11.5

Arun Baid

arun.baid@icicisecurities.com
+91 22 6807 7235

Sohil Kaura

sohil.kaura@icicisecurities.com

Market Data

Market Cap (INR)	126bn
Market Cap (USD)	1,512mn
Bloomberg Code	FNXP IN
Reuters Code	FINX.BO
52-week Range (INR)	260 /130
Free Float (%)	46.0
ADTV-3M (mn) (USD)	3.4

Price Performance (%)	3m	6m	12m
Absolute	8.3	22.9	47.5
Relative to Sensex	11.2	13.6	37.2

ESG Disclosure	2021	2022	Change
ESG score	28.4	29.1	0.7
Environment	2.1	2.1	-
Social	17.0	19.0	2.1
Governance	66.1	66.1	-

Note - Score ranges from 0 - 100 with a higher score indicating higher ESG disclosures.

Source: Bloomberg, I-sec research

Earnings Revisions (%)	FY24E	FY25E	FY26E
Revenue	1.3	(1.2)	(1.3)
EBITDA	(11.6)	0.2	0.4
EPS	(5.0)	0.2	0.3

Previous Reports

21-07-2023: [Q1FY24 results review](#)
24-05-2023: [Q4FY23 results review](#)

Valuation and view

FNXP's operational performance in Q2 has been subdued due to lower-than-expected profitability of both pipes and resin. We cut our FY24E PAT estimates by ~5% due to lower resin production and profitability but keep FY25-26E estimates largely unchanged. We believe there are demand and margin tailwinds for the company due to lower raw material prices in both agri and non-agri segments. However, we expect H2FY24 to witness lower volume growth than H1 due to high base. We continue to like FNXP due to reasonable valuations and maintain **BUY** with a rolled over SoTP-based Dec'24E target price of INR 237 (earlier INR 230).

Exhibit 1: Q2FY24 consolidated result review

INR mn	Q2FY24	Q2FY23	% YoY	Q1FY24	% QoQ	H1FY24	H1FY23	% YoY
Net Revenue	8,832	9,411	-6.2%	11,792	-25.1%	20,623	21,309	-3.2%
Raw Material	5,306	8,529	-37.8%	7,802	-32.0%	13,108	16,528	-20.7%
% of sales	60.1%	90.6%	-3055 bps	66.2%	-609 bps	63.6%	77.6%	-1400 bps
Employee expenses	503	423	18.9%	519	-3.1%	1,022	934	9.4%
% of sales	5.7%	4.5%	120 bps	4.4%	129 bps	5.0%	4.4%	57 bps
Other expenses	1,993	1,886	5.7%	1,946	2.4%	3,939	4,016	-1.9%
% of sales	22.6%	20.0%	253 bps	16.5%	607 bps	19.1%	18.8%	26 bps
Total Expenditure	7,802	10,838	-28.0%	10,267	-24.0%	18,069	21,477	-15.9%
% of sales	88.3%	115.2%	-2682 bps	87.1%	127 bps	87.6%	100.8%	-1317 bps
EBITDA	1,030	-1,427	Nm	1,525	-32.5%	2,555	-168	Nm
EBITDA margin (%)	11.7%	-15.2%	2682bps	12.9%	-127bps	12.4%	-0.8%	1317bps
Depreciation & amortisation	274	216	27.0%	344	-20.4%	618	429	44.0%
EBIT	756	-1,642	Nm	1,181	-36.0%	1,937	-597	Nm
EBIT margin (%)	8.6%	-17.5%	2601bps	10.0%	-145bps	9.4%	-2.8%	1219bps
Other income	614	388	58.0%	403	52.4%	1,016	639	59.0%
Finance costs	125	43	189.1%	90	38.1%	215	156	37.3%
Exceptional items	-	-4	Nm	-	nm	-	135	Nm
PBT	1,245	-1,301	Nm	1,493	-16.6%	2,738	21	Nm
Tax expenses	354	-354	Nm	416	-14.8%	770	-37	Nm
Share of profit from associates	89	-7	Nm	76	17.0%	164	-20	Nm
Reported PAT	980	-954	nm	1,153	-15.1%	2,133	38	nm
Adjusted PAT	980	-951	Nm	1,153	-15.1%	2,133	-97	Nm

Source: I-Sec research, Company data

Exhibit 2: Q2FY24 standalone result review

INR mn	Q2FY24	Q2FY23	YoY (%)	Q1FY24	QoQ (%)	H1FY24	H1FY23	% YoY
Net Revenue	8,832	9,411	-6.2%	11,792	-25.1%	20,623	21,309	-3.2%
Raw Material	5,306	8,529	-37.8%	7,802	-32.0%	13,108	16,528	-20.7%
% of sales	60.1%	90.6%	-3055 bps	66.2%	-609 bps	63.6%	77.6%	-1400 bps
Employee expenses	503	423	18.9%	519	-3.1%	1,022	934	9.4%
% of sales	5.7%	4.5%	120 bps	4.4%	129 bps	5.0%	4.4%	57 bps
Other expenses	1,993	1,886	5.7%	1,946	2.4%	3,939	4,016	-1.9%
% of sales	22.6%	20.0%	253 bps	16.5%	607 bps	19.1%	18.8%	26 bps
Total Expenditure	7,802	10,838	-28.0%	10,267	-24.0%	18,069	21,477	-15.9%
% of sales	88.3%	115.2%	-2682 bps	87.1%	127 bps	87.6%	100.8%	-1317 bps
EBITDA	1,030	-1,427	nm	1,525	-32.5%	2,555	-168	Nm
margin (%)	11.7%	-15.2%	2682bps	12.9%	-127bps	12.4%	-0.8%	1317bps
Depreciation & amortisation	274	216	27.0%	344	-20.4%	618	429	44.0%
EBIT	756	-1,642	nm	1,181	-36.0%	1,937	-597	Nm
margin (%)	8.6%	-17.5%	2601bps	10.0%	-145bps	9.4%	-2.8%	1219bps
Other income	625	393	59.1%	403	55.3%	1,028	644	59.7%
Finance costs	125	43	189.1%	90	38.1%	215	156	37.3%
Exceptional items	-	-	nm	-	nm	-	140	nm
PBT	1,257	-1,293	nm	1,493	-15.9%	2,750	30	9035.2%
Tax expenses	319	-353	nm	384	-17.1%	703	-32	Nm
Reported PAT	938	-939	nm	1109	-15.4%	2047	62	3217.0%
Adjusted PAT	938	-939	nm	1109	-15.4%	2047	-78	nm

Source: I-Sec research, Company data

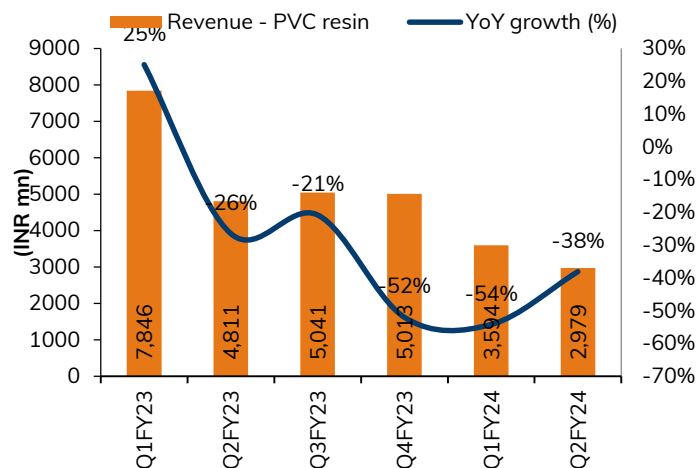
Exhibit 3: Q2FY24 segmental result review

INR mn	Q2FY24	Q2FY23	YoY (%)	Q1FY24	QoQ (%)	H1FY24	H1FY23	YoY
Revenue								
PVC	2,979	4,811	-38.1%	3,594	-17.1%	6,573	12,657	-48.1%
PVC pipes & fittings	8,572	8,017	6.9%	11,542	-25.7%	20,114	19,337	4.0%
Total	11,550	12,828	-10.0%	15,136	-23.7%	26,686	31,994	-16.6%
Inter-segment revenues	2,719	3,417	-20.4%	3,345	-18.7%	6,063	10,684	-43.3%
Net revenue	8,832	9,411	-6.2%	11,792	-25.1%	20,623	21,310	-3.2%
EBIT								
PVC	204	-1,107	-118.4%	31	553.8%	235	-378	-162.3%
PVC pipes & fittings	676	-476	-241.9%	1,264	-46.5%	1,940	-51	-3942.4%
Total	880	-1,583	-155.6%	1,296	-32.1%	2,176	-428	-608.0%
EBIT Margins (%)								
PVC	6.8%	-23.0%	2986 bps	0.9%	598 bps	3.6%	-3.0%	656 bps
PVC pipes & fittings	7.9%	-5.9%	1383 bps	11.0%	-307 bps	9.6%	-0.3%	991 bps
Total	10.0%	-16.8%	2679 bps	11.0%	-102 bps	10.5%	-2.0%	1256 bps
Per unit analysis								
Volume								
PVC (te)	37,516	54,063	-30.6%	46,074	-18.6%	83,590	1,16,810	-28.4%
PVC pipes (te)	62,914	59,218	6.2%	92,181	-31.7%	1,55,095	1,31,179	18.2%
Realisation								
PVC (INR/te)	79,393	88,983	-10.8%	78,007	1.8%	78,629	1,08,351	-27.4%
PVC pipes (INR/te)	1,36,242	1,35,386	0.6%	1,25,211	8.8%	1,29,686	1,47,412	-12.0%
EBIT/tonne								
PVC (INR/te)	5,438	-20,472	nm	677	703.0%	2,814	-3,234	nm
PVC pipes (INR/te)	10,745	-8,043	nm	13,716	-21.7%	12,511	-385	nm

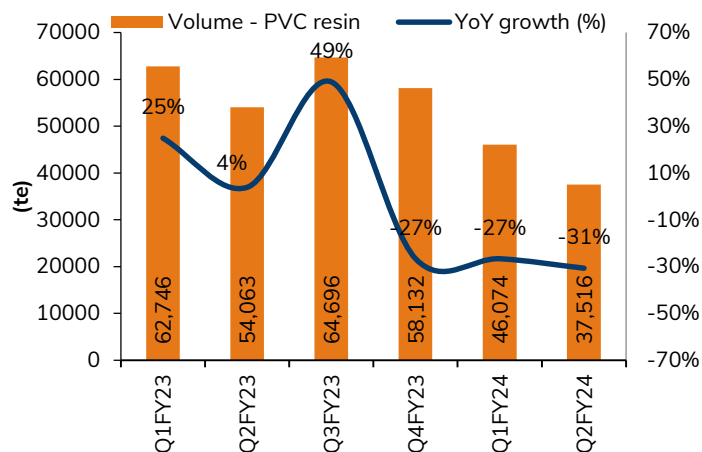
Source: I-Sec research, Company data

Takeaways from Q2FY24 earnings conference call

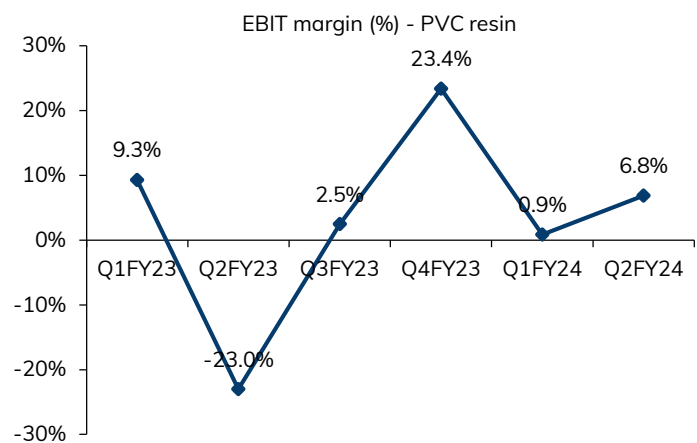
- **Demand:** Management indicated demand from plumbing and sanitation segments continue on a healthy momentum, but agri demand in Q2 was partly deferred in anticipation of a decline in PVC prices. Resin volumes declined 30.6%/18.6% YoY/QoQ due to supply-side issues arising out of geo-political instability in the Middle-East (which is in the process of normalising currently). With PVC prices stabilising, management expects improvement in sales volume from price sensitive consumer segments.
 - **Outlook:** Management is employing marketing approach in cities and towns with focus on plumbing and sanitation segments. It has also implemented various engagement initiatives with plumbing influencers to improve its connect in this segment.
 - **Pricing:** Management believes PVC prices have bottomed out after declining INR 10/kg in Oct'23-TD. This may result in a slight inventory loss in Q3FY24. CPVC prices have declined ~5% in Q2 (did not result in any significant inventory loss). PVC prices in Q2 stood at USD 847/te (vs USD 770/te currently), PVC-EDC spread was USD 571/te (vs USD 450/te currently) and PVC-VCM spread was USD 157/te (vs USD 95/te currently).
 - **Profitability:** Pipes profitability declined 21.7% QoQ due to negative operating leverage (sales volumes declined 31.7% QoQ due to deferred agri demand). Management expects normalisation in spreads in coming weeks and thus, resin profitability should improve going forward and is expected to normalise in Q4FY24.
 - **Product mix (%):** Agri segment formed 60% of volumes in Q2FY24 (vs 63% in Q2FY23) and 68% of volumes in H1FY24 (vs 30% YoY).
- Guidance:** Management has guided for pipes volume growth of 15-20% YoY and expects to produce resin volumes of 200,000-220,000te, in FY24. It has guided for pipes EBIT/kg of INR 10-12/kg and for resin of INR 7-8/kg in FY24. Management targets INR 14/kg for pipes in the long term supported by an improving product mix.
- As on Q2FY24, FNXP had net cash surplus of ~INR 15bn. Management stated it will distribute surplus cash if it does not find any proper avenue for investments. However, it refrained from giving a time frame within which this would be done.

Exhibit 4: Quarterly PVC resin revenue


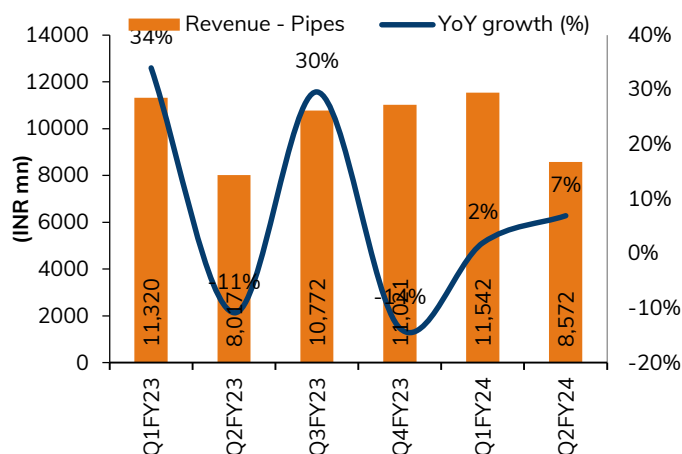
Source: I-Sec research, Company data

Exhibit 5: Quarterly PVC resin volume


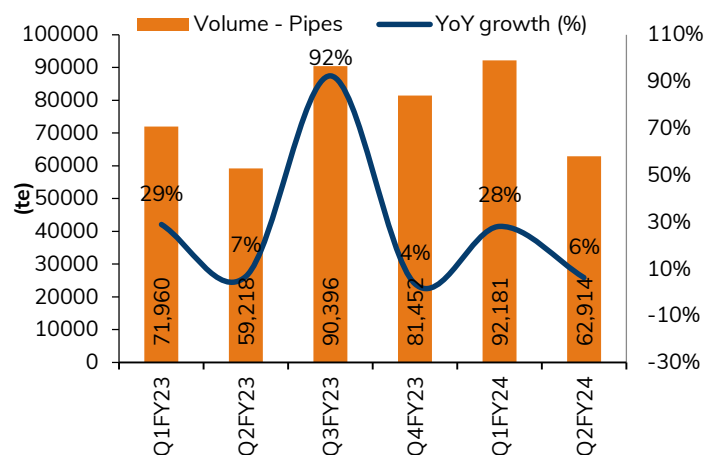
Source: I-Sec research, Company data

Exhibit 6: Quarterly PVC resin EBIT margin


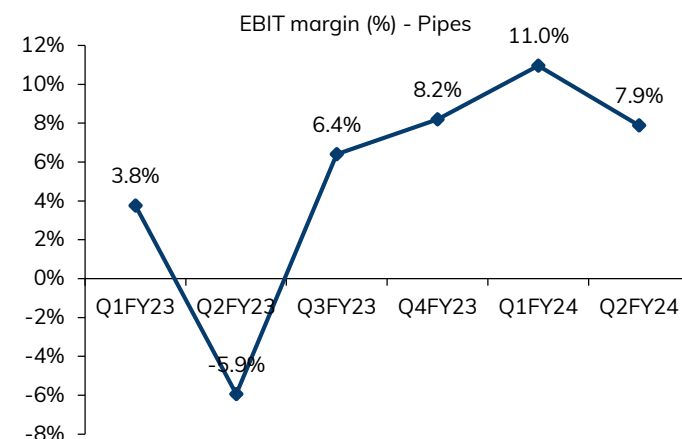
Source: I-Sec research, Company data

Exhibit 7: Quarterly pipes and fittings revenue


Source: I-Sec research, Company data

Exhibit 8: Quarterly pipes and fittings volume


Source: I-Sec research, Company data

Exhibit 9: Quarterly pipes and fittings EBIT margin


Source: I-Sec research, Company data

Valuation

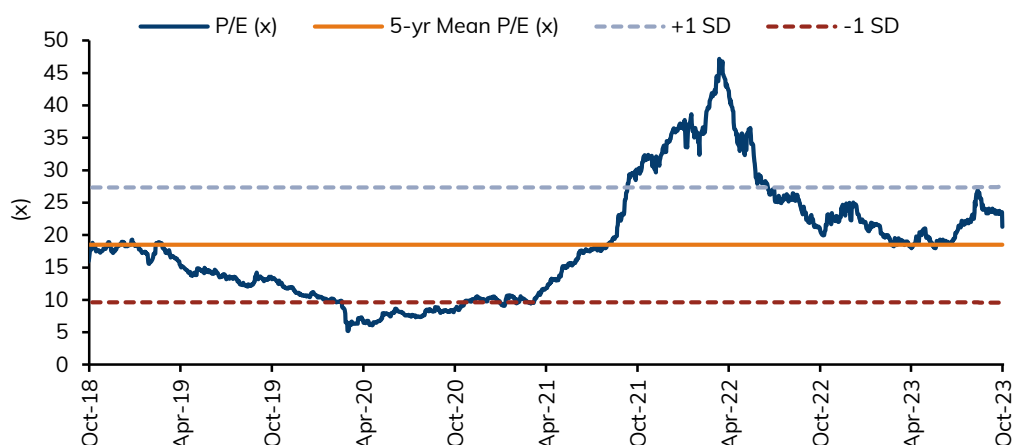
Finolex is a strong player in agricultural pipe market and is also expanding in plumbing segment. It has a strong brand with wide distribution and robust balance sheet. We like the company for its leadership position in agricultural pipe segment. We maintain BUY on the stock with rolled over SoTP-based Dec'24E target price of INR 237 (earlier: INR 230).

Exhibit 10: SoTP-based valuations

Particulars	EBIDTA-Dec'25 (INR Mn)	Target Multiple (x)	Amount (INR mn)
PVC resin	3,114	6	18,681
PVC pipe & fittings	5,512	18	99,209
Enterprise Value			1,17,891
Finolex cable investment value at 40% holding company disc			11,944
Add: Net (debt)/cash as of FY25E			16,873
Equity value			1,46,707
Total no. of Finolex shares (mn)			618
Target Price (INR/share)			237

Source: I-Sec research, Company data

Exhibit 11: 1-year forward P/E band



Source: I-Sec research, Bloomberg, Company data

Key downside risks

- Lower-than-expected demand for agricultural pipes may adversely affect volume growth for the company.
- Any slowdown in housing market may adversely affect volumes in the plumbing market.
- Sharp fall in PVC-EDC spreads.
- Inability to do proper capital allocation may result in derating of the stock.

Exhibit 12: Shareholding pattern

%	Sep'22	Dec'22	Mar'23
Promoters	52.5	52.5	52.5
Institutional investors	17.8	17.7	18.8
MFs and others	11.7	11.3	11.5
FIs/Banks	0.0	0.0	0.0
Insurance	0.5	0.5	0.6
FIIIs	5.5	5.8	6.7
Others	29.8	29.9	28.7

Source: Bloomberg, I-Sec research

Exhibit 13: Price chart



Source: Bloomberg, I-Sec research

Financial Summary

Exhibit 14: Profit & Loss

(INR mn, year ending March)

	FY23A	FY24E	FY25E	FY26E
Net Sales	43,971	42,216	46,078	50,736
Operating Expenses	40,713	35,345	37,875	41,970
EBITDA	3,258	6,871	8,202	8,766
EBITDA Margin (%)	7.4	16.3	17.8	17.3
Depreciation & Amortization	892	1,160	1,277	1,414
EBIT	2,366	5,712	6,925	7,352
Interest expenditure	272	434	354	320
Other Non-operating Income	506	1,787	1,422	1,487
Recurring PBT	2,599	7,065	7,993	8,519
Less: Taxes	(875)	(1,861)	(2,090)	(2,222)
PAT	1,724	5,204	5,903	6,297
Profit / (Loss) from Associates	243	320	300	300
Less: Minority Interest	-	-	-	-
Extraordinaries (Net)	540	-	-	-
Net Income (Reported)	2,507	5,524	6,203	6,597
Net Income (Adjusted)	2,149	5,524	6,203	6,597

Source Company data, I-Sec research

Exhibit 15: Balance sheet

(INR mn, year ending March)

	FY23A	FY24E	FY25E	FY26E
Assets				
Inventories	6,732	6,778	7,264	8,049
Cash & cash eqv.	18,277	19,747	21,237	23,520
Sundry Debtors	2,975	3,123	3,408	3,753
Other Current Assets	2,080	1,966	2,146	2,363
Trade payables	2,893	3,131	3,310	3,689
Other Current Liabilities	4,027	3,342	3,614	4,024
Net Current Assets	23,143	25,141	27,130	29,972
Investments	21,798	21,798	21,798	21,798
Net Fixed Assets	10,822	11,662	12,385	12,971
Other Non Current Assets	168	168	168	168
Total Assets	55,931	58,769	61,481	64,909
Liabilities				
Borrowings	5,264	5,064	4,364	4,164
Other Non Current Liabilities	1,636	1,636	1,636	1,636
Total Liabilities	6,900	6,700	6,000	5,800
Equity Share Capital	1,237	1,237	1,237	1,237
Reserves & Surplus	47,794	50,832	54,244	57,872
Total Net Worth	49,031	52,069	55,481	59,109
Minority Interest	-	-	-	-
Total Liabilities & Net Worth	55,931	58,769	61,481	64,909

Source Company data, I-Sec research

Exhibit 16: Quarterly trend

(INR mn, year ending March)

	Dec'22	Mar'23	Jun'23	Sep'23
Net Sales	11,248	11,411	11,792	8,832
% growth (YOY)	11.9	-28.4	-0.9	-6.2
EBITDA	919	2,174	1,525	1,030
Margin %	8.2	19.1	12.9	11.7
Other Income	278	292	403	614
Extraordinaries	-	-	-	-
Adjusted Net Profit	772	1,670	1,153	980

Source Company data, I-Sec research

Exhibit 17: Cashflow statement

(INR mn, year ending March)

	FY23A	FY24E	FY25E	FY26E
Operating Cashflow	3,827	5,836	6,681	7,152
Working Capital Changes	538	(527)	(500)	(559)
Capital Commitments	(1,687)	(2,000)	(2,000)	(2,000)
Free Cashflow	2,140	3,836	4,681	5,152
Other investing cashflow	(10,146)	-	-	-
Cashflow from Investing Activities	(11,833)	(2,000)	(2,000)	(2,000)
Issue of Share Capital	(4)	-	-	-
Inc (Dec) in Borrowings	2,484	(200)	(700)	(200)
Dividend paid	(2,482)	(2,486)	(2,791)	(2,968)
Others	9,950	320	300	300
Cash flow from Financing Activities	9,947	(2,366)	(3,191)	(2,868)
Chg. in Cash & Bank balance	1,941	1,470	1,490	2,283
Closing cash & balance	18,277	19,747	21,237	23,520

Source Company data, I-Sec research

Exhibit 18: Key ratios

(Year ending March)

	FY23A	FY24E	FY25E	FY26E
Per Share Data (INR)				
Reported EPS	4.1	8.9	10.0	10.7
Adjusted EPS (Diluted)	3.5	8.9	10.0	10.7
Cash EPS	4.9	10.8	12.1	13.0
Dividend per share (DPS)	4.0	4.0	4.5	4.8
Book Value per share (BV)	79.3	84.2	89.7	95.6
Dividend Payout (%)	115.5	45.0	45.0	45.0
Growth (%)				
Net Sales	(5.4)	(4.0)	9.1	10.1
EBITDA	(68.3)	110.9	19.4	6.9
EPS (INR)	(73.0)	157.1	12.3	6.3
Valuation Ratios (x)				
P/E	58.3	22.7	20.2	19.0
P/CEPS	41.2	18.7	16.8	15.6
P/BV	2.6	2.4	2.3	2.1
EV / EBITDA	34.5	16.1	13.2	12.1
EV / Sales	2.6	2.6	2.4	2.1
Dividend Yield (%)	2.0	2.0	2.2	2.4
Operating Ratios				
Gross Profit Margins (%)	30.1	39.8	41.7	41.0
EBITDA Margins (%)	7.4	16.3	17.8	17.3
Effective Tax Rate (%)	33.7	25.2	25.2	25.2
Net Profit Margins (%)	4.9	13.1	13.5	13.0
NWC / Total Assets (%)	7.7	8.3	8.6	8.9
Net Debt / Equity (x)	(0.3)	(0.3)	(0.3)	(0.3)
Net Debt / EBITDA (x)	(4.0)	(2.1)	(2.1)	(2.2)
Profitability Ratios				
RoCE (%) (post-tax)	3.2	7.4	8.5	8.6
RoE (%)	4.9	10.9	11.5	11.5
Cash Conversion Cycle (on net sales)				
Inventory Days	56	59	58	58
Receivables Days	25	27	27	27
Payables Days	24	27	26	27

Source Company data, I-Sec research

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Name of the Compliance officer (Research Analyst): Mr. Atul Agrawal, Contact number: 022-40701000, **E-mail Address** : complianceofficer@icicisecurities.com

For any queries or grievances: [Mr. Prabodh Avadhoot](mailto:Mr.Prabodh.Avadhoot) Email address: headservicequality@icicidirect.com Contact Number: 18601231122
