Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Finolex Cables

Decent Q4; on a sustainable growth path led by industry demand

Capital Goods	Sharekhan code: FINCABLES
Reco/View: Buy ↔	CMP: Rs. 1,519
	Price Target: Rs. 1,800 ↑

↑ 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		↔	

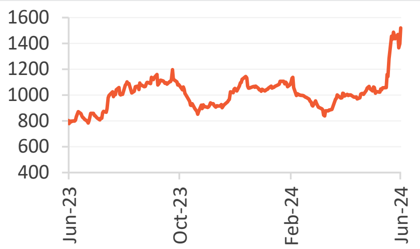
Company details

Market cap:	Rs. 23,236 cr
52-week high/low:	Rs. 1,540/780
NSE volume: (No of shares)	4.6 lakh
BSE code:	500144
NSE code:	FINCABLES
Free float: (No of shares)	9.8 cr

Shareholding (%)

Promoters	35.9
FII	11.8
DII	15.6
Others	37.3

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	47.2	67.6	44.6	94.9
Relative to Sensex	46.6	65.7	36.8	75.4

Sharekhan Research, Bloomberg

Summary

- Q4FY24 numbers were decent, with Revenue/operating profit/PAT of Rs. 1,401/162/186 crore and a growth of 14%/11%/6% y-o-y respectively. Revenue growth was led by strong demand from the construction sector.
- Segment wise – Electric cables/communication cables/Copper rods/FMEG reported revenues of Rs. 1,201/128/481/64 crore with a growth of 16%/-9%/24%/41% on a y-o-y basis.
- Capex of Rs. 340 crore in next 12-24 months for upgrading its offerings in OFC, auto wires and backward integration would boost volumes and margins going forward. The company has healthy cash, zero debt and a lean working capital cycle.
- Strong demand in the real estate and infrastructure sectors bodes well for the company. Also, in the long term optic fiber cables should do well as India as a country remains underpenetrated in the segment. With good growth, we expect the valuation multiple of the company to narrow vs its peers. We assign a multiple of 30x on FY26 EPS and arrive at a revised PT of Rs. 1,800. At CMP, the company trades at a valuation of 26x on FY26 earnings.

For Q4FY2024, Finolex reported an in-line quarter with a revenue of Rs. 1,401 crore, up 14% y-o-y. Electric cable revenue grew 16% y-o-y led by a strong demand in the construction segment. Communication cables was weak with a revenue decline of 9% y-o-y. Copper rods grew 24% y-o-y and FMEG grew 41% y-o-y on a weak base. In terms of volume, electrical wires grew 15% y-o-y, while cables volumes increased 50%. Lack of government tenders and delay by private telecom companies affected the performance of communication cables. FMEG did well in the quarter but lighting products continue to see price erosion. Operating profit grew 11% y-o-y to ~Rs. 162 crore, while OPM decreased 34bps y-o-y to 11.6%. Net profit came in at Rs. 186 crore, a growth of 6% y-o-y. There was lesser profit from JV and a higher tax rate.

Key positives

- FMEG revenue rose 41% y-o-y.
- Copper rods revenue increased 24% y-o-y.

Key negatives

- Communication cables revenues fell 9% y-o-y.

Management Commentary

- In volume terms, electrical wires increased 15% y-o-y, driven by demand from construction, realty, and other infrastructure segments. Cables volume also grew well at 50% y-o-y on a low base.
- Optic fiber cables has been weak due to no tenders from government and a delay from private players but revenue will start flowing from Sept-Oct as a new tender comes up in June. Also overall, the segment remains unpenetrated in India.
- Management believes margins will come back to 12-13% in the coming year.
- The company will carry out capex of ~Rs. 340 crore in the next 12-18 months for expanding capacities in auto wires, fibers and cables.

Revision in estimates – We have increased our FY25-26 earnings estimates to reflect the performance of the quarter.

Our Call

Retain Buy with a revised PT of Rs. 1,800: We expect the company's long-term growth momentum to continue, backed by demand from key sectors such as construction and infrastructure. Further, the government's push through the Bharat Net programme would boost demand for the company's communication cables. The company is also expanding capacity in all its product categories and backward integrating in OFC, which shall help the company increase volumes and margins in the long run. Finolex's debt-free balance sheet and strong cash position provide us comfort. With good growth, we expect Finolex's valuation multiple to narrow vs its peers. We assign a multiple of 30x on FY26 EPS and arrive at a revised PT of Rs. 1,800. At CMP, the company trades at a valuation of 26x on FY26 earnings.

Key Risks

- Any sharp increase or decrease in key raw-material (copper) prices would lead to volatility in the company's margins.
- Weak demand in the FMEG segment and inflationary pressures could affect earnings.

Valuation (Consolidated) Rs cr

Particulars	FY23	FY24	FY25E	FY26E
Net sales (Rs. cr)	4,481	5,014	5,824	6,702
Growth (YoY, %)	18.9	11.9	16.1	15.1
Operating Profit (Rs. cr)	509	588	697	866
OPM (%)	11.4	11.7	12.0	12.9
Net profit (Rs. cr)	505	652	784	903
Adjusted EPS (Rs.)	33.0	42.6	51.3	59.1
Growth (YoY, %)	(15.8)	29.2	20.3	15.2
PER (x)	46.0	35.7	29.6	25.7
P/B (x)	5.3	4.7	4.2	3.7
EV/EBIDTA (x)	36.9	30.2	24.2	20.5
RoCE (%)	13.9	15.4	16.9	17.6
RoE (%)	25.1	44.0	36.4	30.8

Source: Company; Sharekhan estimates

Finolex's Q4FY2024 conference call and investor update highlights

Wires & cables: In Q4, wires volumes increased 15% y-o-y due to good demand from the construction sector. Cables volume rose an impressive 50% y-o-y on a low base For FY24, wires volume increased 15% y-o-y as well and cables grew 26% y-o-y. Company aims to grow the segment revenue at 2x the nominal GDP growth.

Of the Rs. 4,200 crore revenue of W&C segment, Rs. 4000 crore comes from wires and Rs. 200 crore from cables. Wires business has 4 revenue streams – About 60-65% comes from construction/general usage, 10-15% each from both auto and industrial and the rest from agriculture. Currently, construction sector is doing very well, auto is also doing decent and agricultural applications have bounced back. Construction wires and agricultural wires have high margins, then comes industrial and auto wires has the lowest margin as it is a B2B business.

Communication cables: Optic fiber cables (OFC) saw some recovery in the latter half of the quarter but the business continues to be affected by lack of government tenders and delay in contract closing with telecom companies. OFC volumes fell 30% in FY24. Overall, communication cables revenue decreased 9% y-o-y in Q4. BSNL will float out tenders for Bharat Net Phase III in next month and company expects revenue to come from it in Sept-Oct.

Copper rods: Metal-based products are doing well with a growth of 24% y-o-y and 10% q-o-q.

FMEG: The segment reported a good 41% growth y-o-y but the lighting segment continues to be affected by price erosion. Overall, segment sales stood at Rs. 225 crore in FY24, up 15% y-o-y. The aim is to increase it to 500 crore in 2-3 years.

Capex: Company had planned a capex of Rs. 500 crore at the start of FY24. In the current year, they spent Rs. 160 crore. Most of the remaining capex will come in FY25 with some spillover in FY26.

There are 3 major expansion items- 1) E-beam capex which had been delayed for a long time. One machine has been installed and will undergo certification. The second machine will be received in June and in Aug-Sept products from both machines will come in the market 2) Products from the pre-form facility will be launched in the market by December. Will increase the fibre drawing capacity from 4mn to 8mn kilometres. Company will also increase the capacity to cable from 8 mn to 10 mn kilometres. 3) Expansion of auto wires capacity by a third in Uttarakhand.

Capacity utilization: In wires, capacity utilization is 72%, in cables it is less than half and in optic fiber cables also it is 50%. Company will look to add capacity in wires after it exceeds 75% utilization.

Others:

1) Overall margins will come back to 12-13% in the next year.

2) Company has taken a price hike of 10-11% in March-April due to the increase in copper price.

3) E-beam revenue at full potential to be Rs 500-600 crore.

4) About 1.5% of revenue will be used for marketing spends.

5) Company is weak in North and East of the country.

6) There is an orderbook of Rs. 280 crore in EHV JV and 190 crore worth of orders are to be awarded in June. EHV market size in India is Rs. 3,500 crore and competitors in the space are Universal Cables, KEI, KEC, Polycab and LS Cable (Korean company).

Results (Consolidated) Rs cr

Particulars	Q4FY24	Q4FY23	YoY (%)	Q3FY24	QoQ (%)
Net Sales	1,401	1,224	14.4	1,222	14.7
Operating Profit	162	146	11.1	134	21.1
Other Income	50	42	18.8	45	10.3
Interest	0.9	0.85	3.5	0.42	109.5
Depreciation	12	15	(23.1)	11	7.3
Share of profit of associate/JV	51	56	(10.2)	30	66.6
PBT	186	175	6.3	151	23.3
Adj PAT	186	175	6.3	151	23.3
Adj. EPS (Rs.)	12.2	11.4	6.3	9.9	23.3
Margin (%)			**BPS**		**BPS**
OPM (%)	11.6	11.9	(34)	10.9	61
NPM (%)	13.3	14.3	(101)	12.4	92
Tax rate (%)	25.4	22.5	299	23.4	200

Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector view - Ample levers for long-term growth

The cables & wires (C&W) industry contributes 40-45% of India's electrical equipment industry. In terms of volumes, the Indian C&W industry (including exports) is estimated to have grown in low teens in FY2023 to Rs. 68.000-73,000 crore in size. The Indian C&W market is projected to grow to Rs. 90,000-95,000 crore by FY2026. Sectors such as power, Railways, infrastructure, oil and gas, telecom, real estate, renewables, defence, and automobiles are the largest demand drivers for the industry. Organised players command a lion's share of the market, at roughly 70%, while unorganised players largely dominate the rural geographies. The government has envisaged Rs. 111 lakh crore capital expenditure in infrastructure sectors in India from FY2020 to FY2025. The government's continued thrust on infrastructure investment is expected to improve the demand environment for the W&C industry. The Indian FMEG industry has many growth opportunities, led by macro drivers such as evolving consumer aspirations, rising awareness, rising income, rural electrification, urbanisation, and digital connectivity. Further, ongoing government programmes (Bharat Net Phase III) are expected to improve broadband connectivity, and related technologies will continue to drive growth for communication cables.

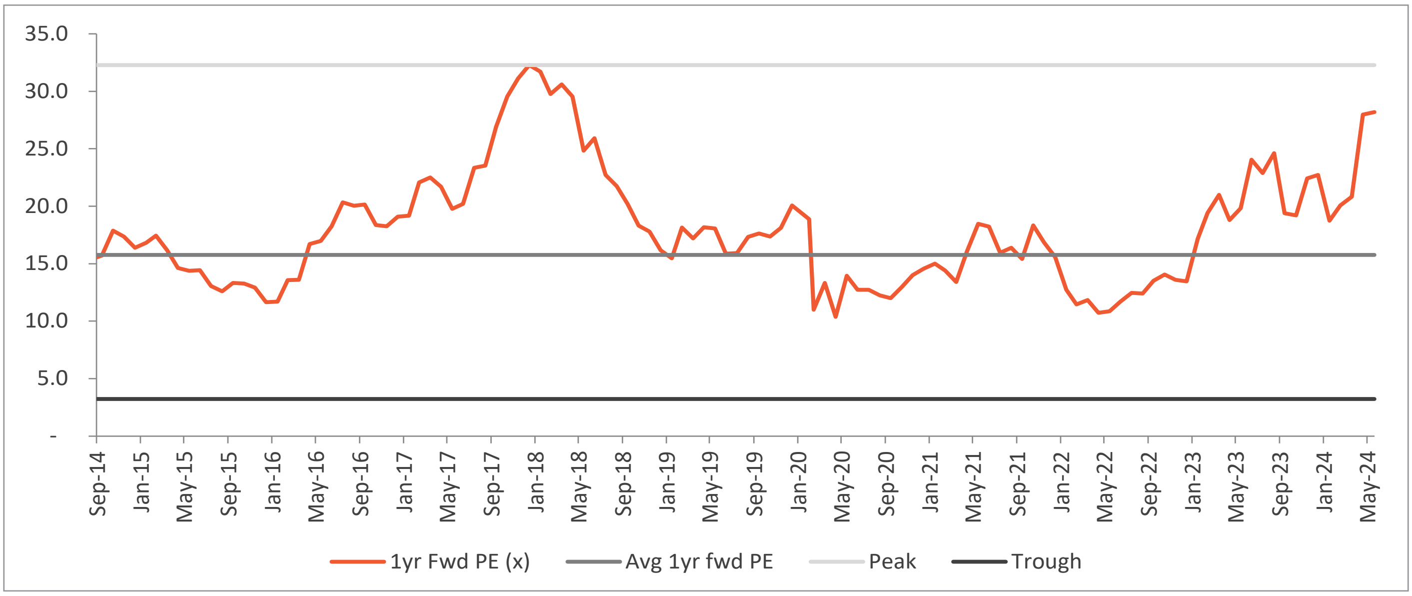
■ Company outlook - On a strong growth trajectory

Demand for electric cables and wires is on a strong footing due a thriving construction sector and bodes well for company's growth. Communication cables segment is soft currently due to lack of tenders but India as a country remains underpenetrated in the optic fibre cables segment and there is a huge runway for growth. Healthy operating cash flow generation, tight working capital management (policy of advance payments from dealers), and capex to expand capacity to meet rising demand are expected to further build upon its cash reserves. The company also has the opportunity to increase its market share organically by penetrating into markets in certain product categories.

■ Valuation - Retain Buy with a revised PT of Rs. 1,800

We expect the company's long-term growth momentum to continue, backed by demand from key sectors such as construction and infrastructure. Further, the government's push through the Bharat Net programme would boost demand for the company's communication cables. The company is also expanding capacity in all its product categories and backward integrating in OFC, which shall help the company increase volumes and margins in the long run. Finolex's debt-free balance sheet and strong cash position provide us comfort. With good growth, we expect Finolex's valuation multiple to narrow vs its peers. We assign a multiple of 30x on FY26 EPS and arrive at a revised PT of Rs. 1,800. At CMP, the company trades at a valuation of 26x on FY26 earnings.

One-year forward P/E (x) band



Source: Sharekhan Research

About company

Finolex is India's largest and leading manufacturer of electrical and communication cables. The company offers a wide range of electrical and communication cables. The company's wire and cable products are used in applications such as automobiles, lighting, cable TV, telephone, and computers for industrial applications. Finolex has added electrical switches, LED-based lamps, fans, low-voltage MCBs, and water heaters to its product range.

Investment theme

Pick-up in capex in real estate, construction and industrial sector is likely to lead to robust demand for housing wires and cables. Further, ongoing government programmes (Bharat Net Phase III) are expected to improve broadband connectivity, and related technologies will continue to drive growth for communication cables. Moreover, FMEG products would aid revenue growth once the products reach a sizeable revenue. The company also plans to pursue inorganic opportunities to expand its product portfolio.

Key Risks

- Any sharp increase or decrease in key raw-material (copper) prices would lead to volatility in the company's margins for the short term.
- Weak demand in some segments and inflationary pressures could affect earnings.

Additional Data

Key management personnel

D.K. Chhabria	Executive Chairperson
Mahesh Vishwanathan	Deputy MD and CFO

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Nippon Life India Asset Management	3.17
2	L&T Mutual Fund Trustee Ltd/India	2.63
3	HDFC Asset Management Co Ltd	1.97
4	Vanguard Group Inc/The	1.96
5	Tata AIA Life Insurance Co Ltd	1.89
6	LGOF GLOBAL OPPORTUNITIES	1.88
7	HDFC Life Insurance Co Ltd	1.52
8	GOVERNMENT PENSION FUND - GLOBAL	1.42
9	BlackRock Inc	0.96
10	Dimensional Fund Advisors LP	0.93

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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