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DEMOCRATIZING WEALTH CREATION

UPSTREAM PICK

December 2018

THINK DIFFERENT PROFIT MORE

Company Name	:	**Supreme Industries**
BSE Code	:	**509930**
Time Duration	:	**2 year**
CMP	:	**₹964.50 (as on 06 December, 2018)**
Target Price	:	**₹1360**

Our Upstream Pick for the month of December is Supreme Industries Limited (SIL). It is India's leading plastics product manufacturing company, offering a wide and comprehensive range of plastic products. The company operates in various product categories, viz. plastic piping system, cross laminated films and products, protective packaging products, industrial moulded components, moulded furniture, storage and material handling products, performance packaging films and composite LPG cylinders.

The overall plastics industry faced headwinds in recent times, such as ban on plastics in Maharashtra state, with other states following suit. Also, the rise in crude oil prices with volatility in currency exchange rates brought an overall negativity in the industry. However, most of the companies were able to pass on the rise in input costs to their consumers, so margins of top companies remained reasonably stable. In the past six months, the stock price of Supreme Industries corrected by 30%. However, considering the recovery in plastics industry, the company's market leadership, strong brand value, leverage-free balance sheet, healthy cash flows, superior return ratios, steady dividend pay outs and capacity expansion, we see this as a good buying opportunity.

Segmental performance

Plastic piping (55.6% of revenue) : The revenue growth (20% YoY) in Q2FY19 was largely driven by higher realisation (up ~12% YoY) mainly due to price hike and change in product mix. This segment's exports during FY18 saw a growth of 48% in US dollar terms. Going forward, a strong demand is expected for piping products like PVC and CPVC.

Packaging products (20.8% of revenue) : Volume growth during the period declined ~3% YoY largely on a higher base (volume was up ~30% in Q2FY18) and lower demand of cross-laminated packaging products (delay in festive season).

Industrial products (16.3% of revenue) : A change in the product mix led to YoY growth in revenue by 37.4% driven by realisation growth of ~27% YoY, while volume growth was ~8% YoY. The bathroom fittings are expected to drive this segment in the near term.

Consumer products (7.1% of revenue) : The change in product mix helped drive the sales of the segment by 10.2% YoY. The company has now started exports to twelve countries and hopes to grow substantially from this segment. The company participates in several exhibitions to promote its products.

Value-added products (VAP) : The share of overall sales in the VAP has been 35% of total sales in Q2FY19 as against 37% in the corresponding quarter of the previous year. SIL plans to take the share up to 35% by 2020.

Foray into supplying composite LPG cylinder

From FY18, the company has received approval from TUV, PESO and KGS for supply of 15.6 kg and 20 kg. cylinders which have huge demand in Korea and Bangladesh. It has also elicited good response from the markets of Goa, Bangalore and Belgaum. Post the government approval for supply of full-fledged composite cylinders to companies in India, the company would earn additional revenue which would also aid its margins.

Capacity expansion & capex

The company's installed capacity has increased by 5% in FY18 to 568,000 MT. During FY19, it plans to invest Rs 300-350 crore, which would add another 50,000 tonnes to capacity. It intends to increase its capacity to 700,000 MT by FY21 at a capex of around Rs 1,200-1,300 crore. It would be funded through internal accruals. The capacity expansion plans includes starting two new greenfield plants, one each in Telangana and Rajasthan. Two new plants are on the anvil in Andhra Pradesh and Assam which would be operational in FY20.

The production of furniture and roto moulded production at the unit in Telangana will go into production during October-December quarter, while the production of foam products will start in the quarter of January-March 2019. The new plant for manufacturer of industrial components at Giloth (Rajasthan) has commenced commercial production in September 2018.

Also, the company had undertaken additional construction of buildings in existing plants located at Malanpur, Khopoli, Hosur and Kharagpur. The capacity of roto moulded products at Malanpur Unit III (M.P.) and at Kanpur (UP) has become operational. The expanded capacities of both the plants are 2400 MTPA. The new plant to make HDPE pipe of 9,000 MTPA capacity at Malanpur unit III has commenced trial production. The new plant to manufacture PP corrugated sheet with a capacity of 3,600 MTPA has been commissioned at Derabassi Unit (Punjab). Hosur unit will be streamlined with increased capacities at one site instead of two sites in the October-December quarter. The expanded capacities (5000 TPA) at the Khopoli unit will be in production during the quarter of January-March 2019.

Management Guidance

The management has given its full-year volume guidance at around 10% and the revenue to be clocked around Rs 5700-5900 crore. The company's operating profit margin is expected to be around 15 percent for the full year. The management expects commodity prices to cool off in the next few quarters, resulting in an increase in gross margin. The company aims to achieve EBITDA margin of ~16% from its core business as against ~14% during H1FY19.

Macro factors favourable for piping & industrial products

The key elements which can drive the demand for company's piping products are the government's thrust on agriculture and irrigation, push for housing and infrastructure, launches of new value-added products and shift in demand towards the organised sector. Considering Swachh Bharat Abhiyaan and housing for all initiatives, the demand for bathroom fittings is set to rise in the near term. Housing and infrastructure development would also aid the demand for company's consumer products like plastic furniture, which is affordable and sustainable.

Financial Performance

SIL's Q2FY19 revenue was 24.7% higher than its revenue in the same quarter last year at Rs 1,316 cr due to 5% growth in volumes and 12% rise in realisations. The volumes from the industrial and piping segments grew in the mid-single digits, but the overall growth was much higher on account of higher realisations. The EBITDA for the quarter jumped by 47.2% YoY from Rs 144 cr to Rs 212 cr. The improvement in realisations, along with lower employee costs, drove the significant jump in EBITDA. The EBITDA margin expanded from 13.6% to 16.1% on a YoY basis, while PAT grew by 50.7% YoY from Rs 71 cr to Rs 107 cr.

The company manages to fund its capex through internal accruals and plans to get debt-free in the next couple of years. In FY18, its debt-equity ratio stood at 0.14x and interest coverage ratio was at 23.8. It has maintained a healthy dividend pay out ratio of 40.88%.

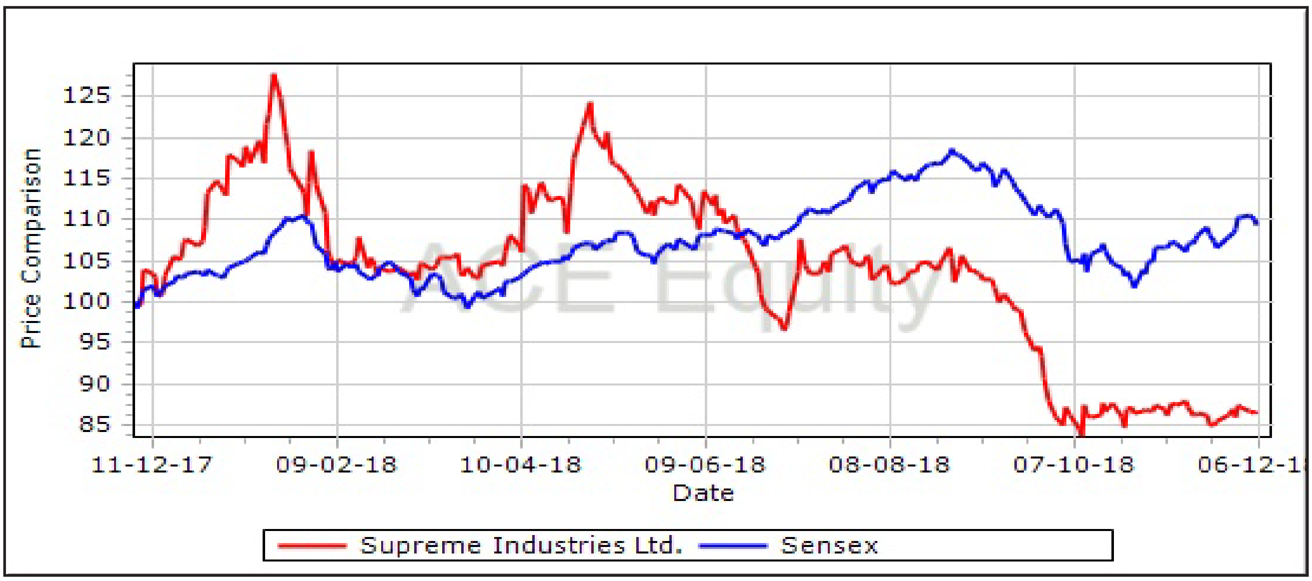
Valuation

SIL is trading at TTM P/E of 23.9x with TTM EPS of Rs 41.23. For FY18, it delivered ROE and ROCE of 24.9% and 33.6%, respectively, which is much higher than its peers. Its piping products would witness higher demand from agriculture, irrigation, housing and infrastructure segments. Also, its extensive capacity expansion to meet the demand and higher realisations through value-added products will boost its growth going forward. We see potential upside of 41% with a target price of Rs 1360 over a period of two years.

Inc/Exp Statement(Consolidated) (Rs in Crore)

Description	201803	201703	201603	201506	201406
Net Sales	4966.29	4462.26	2960.06	4255.19	3962.23
Total Income	4976.06	4471.12	2965.19	4259.87	3969.45
Total Expenditure	4179.18	3700.39	2499.08	3588.95	3374.70
PBIDT	796.88	770.73	466.11	670.92	594.75
PAT	397.09	376.67	204.34	311.71	274.35
Dividend %	600.00	750.00	375.00	450.00	400.00
Adj. EPS(Rs)	33.98	33.88	17.42	25.38	22.31

Quarter On Quarter (Consolidated) (Rs in Crore)					
Particulars	**201809**	**201806**	**Q on Q Var%**	**201709**	**Y on Y Var%**
Net Sales	1316.17	1345.71	-2.20	1055.06	24.75
Total Expenditure	1103.71	1160.02	-4.85	911.10	21.14
PBIDT (Excl OI)	212.46	185.69	14.42	143.96	47.58
PAT	104.75	130.36	-19.65	59.82	75.11
PBIDTM% (Excl OI)	16.14	13.80	16.96	13.64	18.33
PBIDTM%	16.56	13.84	19.65	13.66	21.23
PATM%	7.96	9.69	-17.85	5.67	40.39
Adj. EPS(Rs)	8.44	10.73	-21.34	5.57	51.53



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