

Veto Switchgears and Cables Ltd

CMP : ₹173.75

Target price: ₹281

HP* : Upto 3 years

Our Vriddhi pick for the month of July is Veto Switchgear and Cable. The company's product range includes industrial cables, stand cables, telephone & co-axial wires, general switches and modular switches, ceiling fans, rechargeable fans, compact fluorescent lamps, LED bulbs and other electrical accessories. The company also deals in electrical accessories like switch socket, MCB, bell and all electrical accessories which are used for household purposes and manufacture wires and cables. Cable thickness start from 0.75 mm to 10 mm. The company's main brands are VETO and VIMAL POWER and has launched LED lights portfolio under the brand VYOMA, recently.

As of FY17, company derived 43% of revenue from Wire & Cables, 43% from Accessories and other and 14% from Lightning. Lightning being a newly launched segment. Company's subsidiary, Veto Electricals Pvt Ltd is now a wholly-owned subsidiary of the company. Company also has a subsidiary Veto Overseas Private F.Z.E which has trading operations in Dubai and has reported revenues of ~Rs.122cr and net profit of Rs.8.8cr as of FY17.

We see company as a 'Vriddhi' stock due to 3-year CAGR profit growth of 44.2% and ROE improving consistently and currently at 20%. Also, the company has reported increase in EBITDA margins in a highly competitive environment and has got best in the industry margins due to its unique business model.

Key Levers Driving Growth

1) High margin business model - Company generates a large portion of its revenue from the state of Rajasthan. Company operates through dealers directly in this region and eliminates distributors. Due to this, the company enjoys better margin in this region and its operating metrics are superior to its peers. However, this model requires higher working capital and higher inventory levels with the company.

However to expand in other regions, the company has chosen the standard distributor model and has been able to increase its presence in 10 cities.

2) Growing into a national player - Company has been evolving from being a regional player to a national player by spreading its wings in western and northern regions. It is looking to expand in Maharashtra, Punjab, Madhya Pradesh, Haryana, Uttar Pradesh, Jharkhand, Kerala, New Delhi and Assam. Company currently has about 2,200 dealers in Rajasthan and its overall dealer count is 3,000, which it plans to expand to over 5,000. It also exports to Middle East through its subsidiary Veto Electricals Pvt Ltd. Company's Dubai business has a working capital requirement of 90 days,

*HP : Holding Period

Company Details

Industry	Electric Equipment
Chairman	
Managing Director	Akshay Kumar Gurnani
Company Secretary	Shilpi Keswani
ISIN	INE918N01018
Bloomberg Code	VSCL IN
BSE Code	539331

Key Market Indicators (Consolidated)

Latest Date	12-Jul-2018
Latest Price (Rs)	173.75
Previous Close (Rs)	177.45
1 Day Price Var%	-1.49
1 Year Price Var%	-5.49
52 Week High (Rs)	265.00
52 Week Low (Rs)	167.00
Beta	1.78
Face Value (Rs)	10.00
Industry PE	44.62
TTM Period	201803
TTM EPS(Rs)	15.16
TTM CEPS(Rs)	15.98
Price/TTM CEPS(x)	10.94
TTM PE (x)	11.53
Price/BV(x)	2.24
EV/TTM EBITDA(x)	8.21
EV/TTM Sales(x)	1.40
Dividend Yield%	1.14
MCap/TTM Sales(x)	1.32
Latest Book Value (Rs)	78.07
Market Cap (Rs. In Crores)	334.13
EV (Rs. In Crores)	355.24
Latest no. of shares (In Crores)	1.91

Share Holding Pattern as on 201803

Promoter No of shares (In Crores)	0.84
Promoter %	45.94
FII No of Shares (In Crores)	0.13
FII %	6.88
Total No of Shares (In Crores)	1.83
Free Float %	54.06

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while African business is on advance basis. Company currently has a B2C model in Rajasthan and Gujarat and needs working capital of ~90days. The company plans to increase its B2C business with working capital cycle of 30 days in other states.

3) In-house production vs import from China - Company has been rebasing its manufacturing facility in India vs import from China. With the setting up of new LED assembly plant in Vasai, Maharashtra, it expects to meet demand from India and Dubai from this facility rather than sourcing from China. We expect this facility to help meet demand from new regions as it will have the scale to give the company a competitive edge over importing. Also, with capex of Rs. 2.5cr, the company over a period of time expects revenue of Rs.30cr from this unit. This facility had received order of 6 lakh pieces per annum in FY18.

Also, its wires and cables manufacturing plant in Mahindra SEZ, Rajasthan is expected to further reduce its dependence on Chinese imports by 50%. This plant required capex of Rs.4cr.

Company has launched LED panel Lights, LED Flood Light, Slim Panel Light, LED Flood Light under the brand name Vyoma. Its major distribution in India covers more than 10 states including major sale in Rajasthan and Gujarat.

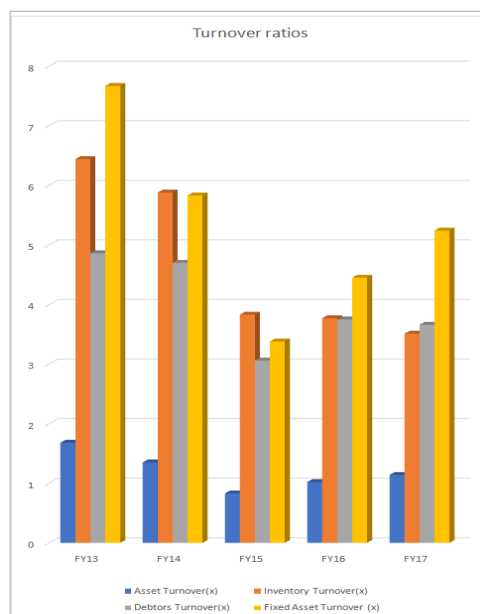
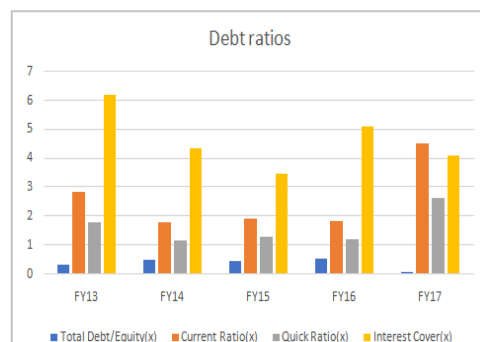
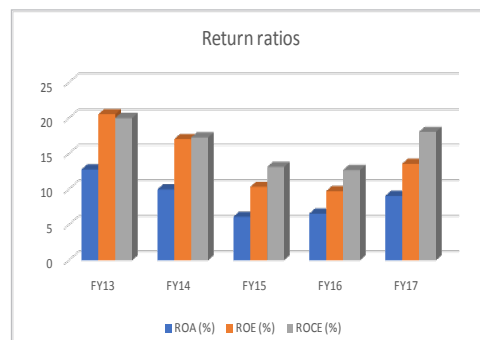
4) Price based competitive edge - Company states that its switch gears and cables have a pricing edge compared to its competitors with company's prices being lower by 10% and 7%, respectively. Also, company provides higher margins to dealer of 6% vs 3% in the industry. This is expected to help company gain higher market share and play on volumes.

5) Financials and Valuation - Veto switchgear reported almost flat growth of 2.8% yoy in FY18 due to the impact of GST. However due to lower employee cost, operating profit jumped by 61.5% to Rs.33.98cr. Also due to lower interest, the PAT rose by 62.3% yoy.

Company is currently trading at attractive P/E of 11.4x. Its competitors Havelis, KEI industries and Finolex cable are trading at 50.39x, 25.01x and 22.31x respectively. We believe that due to changing product mix and higher penetration in other states, the company is expected to see sales growth of 15-18% in FY19. Hence we expect company to lead to achieve target price of **Rs.281** over 3 years.

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

Description	201803	201703	201603	201503	201403
Net Sales	123.80	120.34	112.09	97.30	94.48
Total Income	129.64	124.79	112.88	97.84	95.35
Total Expenditure	95.66	103.67	92.20	82.12	83.67
PBIDT	33.98	21.11	20.67	15.72	11.69
PAT	19.93	12.19	7.66	7.15	6.09
Dividend %	0.00	20.00	20.00		
Adj. EPS(Rs)	10.88	6.65	4.18	3.90	3.32



Source: ACE Equity

Quarter On Quarter (Standalone) (Rs in Crore)

Particulars	201803	201712	Q on Q Var%	201703	Y on Y Var%
Net Sales	43.37	30.30	43.15	33.15	30.83
Total Expenditure	34.39	24.11	42.66	28.69	19.89
PBIDT (Excl OI)	8.98	6.19	45.07	4.47	101.05
PAT	5.28	4.16	27.01	3.30	59.90
PBIDTM% (Excl OI)	20.71	20.44	1.32	13.47	53.75
PBIDTM%	22.53	24.32	-7.36	16.52	36.38
PATM%	12.17	13.72	-11.30	9.96	22.19
Adj. EPS(Rs)	2.88	2.27	26.87	1.80	60.00

Industry growth

Cable and Wires market is expected to grow at a CAGR of 15% over the next 5 years. The key drivers of this growth are expected to be

1) Growth in renewable energy - Government is targeting capacity addition of 100 GW under the 13th 5 year plan 2017-22. This emphasis on commercialization of renewable energy boosts the demand for cables and wires. India like many emerging nations is on threshold of integrating regional grid to form a national grid network, which will provide seamless flow of electricity.

2) Increase in communication - With the telecom industry increasing its rural penetration and the government emphasis on digitalization of day to day operations, there is a humongous need for high speed cables and last mile connectivity.

3) Rural electrification - Emphasis on rural electrification gathered pace in the last few years leading to higher demand for electrical wires. Along with this, there is increased awareness and emphasis on energy saving LEDs. However, LEDs complying to the laid norms with details of manufacturer is still to be achieved, better compliance to government standards will enhance consumer trust and increase demand.

4) GST - GST roll out will help the organized sector in the long-term as they would be able to claim input GST and hence will benefit from lower taxes.

About Veto

Veto Switchgear is engaged in the manufacturing of electrical accessories, and wires and cables. In cables, it is the number one brand in Rajasthan, followed by Finolex Cables and then RR Cables and Polycab. In electrical accessories, Veto ranks second after Anchor, while in Gujarat it ranks second. Rajasthan till FY17 accounted for 70% of the revenue, which company plans to deconcentrate to 50-55% with further penetration in 10 states like Gujarat, NCR, Punjab, Assam, Jharkhand etc. To expand further, the company is also evolving its business model in which it is dealing with distributors in its core region, than directly selling to dealers. Company is also making few dealers as channel partners and opening exclusive stores of Veto.



Cables and wires market is expected to grow at a CAGR of 15%



Evolving business model to include distributors to help expand in other states



GST to positively benefit organised sector

Company through its Dubai subsidiary caters to global markets. The company used to import goods from China and sells to international markets such as Africa (30%), Russia & Europe (30%) and the Gulf (40%). However, with hike of labour and electricity prices in China, the company has shifted its focus to in-house production.

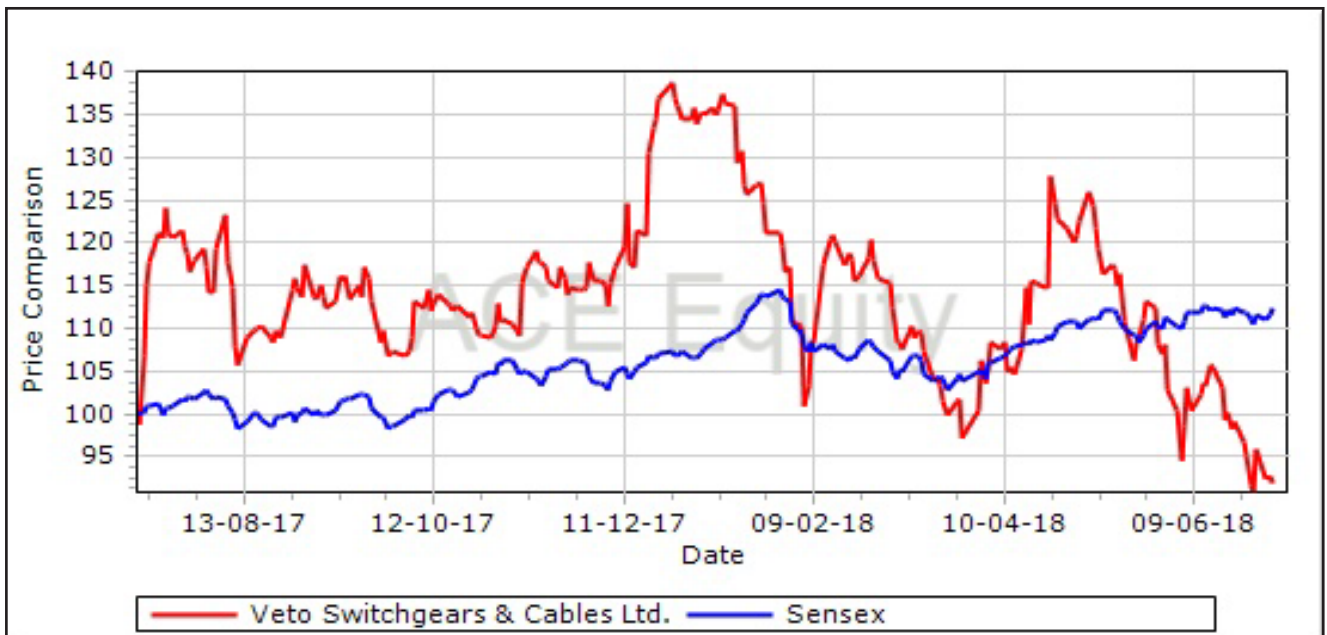
Currently Veto has 3 factories - Haridwar, Jaipur (Mahindra SEZ) and Vasai, Maharashtra. Company by Dec 2017 was manufacturing DP switches, switchgears and MCBs at the SEZ.

Company as of FY16-17 had an installed capacity of 20 lakh bundles for its Wires & Cables division, while for electrical accessories it's 600 lakh pieces.

Gross margins on electrical accessories and LED are higher at ~25%, while for wires its 10%. The lowest margins are in CFL, Fans and Cooler Kit at ~5%.



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