

Polycab India

BSE Code	: 542652
Time Duration	: 18 months
CMP	: ₹697.50 (as on 26 September 2019)
Target Price	: ₹850



Large Rhino for the month of September 2019 is Polycab India. The company is involved in the business of manufacturing and selling wires and cables and fast-moving electrical goods (FMEG) under the POLY-CAB brand. The company commands nearly 18 per cent of organised market of wires and cables and 12 per cent of the overall market. Polycab is the largest manufacturer in the wires & cables industry in India with a production capacity of 3.5 million km of cables and wires. In 2009, the company entered the engineering, procurement and construction (EPC) business, which includes the design, engineering, supply, execution and commissioning of power distribution and rural electrification projects. Additionally, the company forayed into FMEG business in 2014 to produce and sell items such as electric fans, LED lighting and luminaires, switches and switchgears, solar products and conduits and accessories. In term of revenue mix, wires & cables generated nearly 86.2 per cent of revenue in FY19, whereas, FMEG and other business generated 8 per cent and 5.8 per cent of the total revenue, respectively. The company has around 24 production facilities across the India.

Growing FMEG business to aid the top-line

To transform itself from B2B to B2C, the company has forayed into FMEG business. The company's revenue from FMEG business has grown to 8 per cent of FY19 from mere 0.3 per cent in FY14 (when it started the FMEG business). Notably, the FMEG revenue has grown at a CAGR of 116 per cent since FY14. The company is leveraging its strong distribution network of more than 3,400 authorized dealers & distributors and more than 100,000 retail outlets (as on Q1FY20) to expand its FMEG business. The industry size of FMEG business is almost Rs. 60,000 crore, which is growing rapidly. In FY19, the company generated around Rs. 650 crore of revenue from its FMEG business, that translates into mere 1 per cent market share. We believe that new product launches on a regular basis coupled with strong distribution network and geographical expansion would help the company to expand its FMEG business. Also, the company's management believes that with increasing scale, the FMEG margin is likely to improve 100-150 bps over the next 2-3 years.

Backward integration enables seamless supply and lowers the cost

In 2016, the company had formed a joint venture with Trafigura for manufacturing copper wire rods, which is key raw material in the manufacturing of wire, cable and FMEG. This JV has helped the company to meet a substantial part of its requirement. Further, Polycab, in its existing manufacturing facilities, produces other key raw materials that are used in the manufacturing of wires and cables and FMEGs, including aluminium rods, higher size of copper rods, various grades of PVC, rubber, XLPE compounds, and GI wire and strip. This backward integration in manufacturing enables the company to reduce its dependence on third party for quality raw materials, and maintain control of the supply chain and lower the cost of operations.

Leader in the wire and cable industry

With increasing demand for power, light and communication including voice and data, the demand for cables and wires is surging. According to CRISIL, the market for wires is expected to grow at 15 per cent over the next 5 years. Unorganized market in cable and wire industry has reduced to 30 per cent in 2019 from 40 per cent in 2014 and is expected to further reduce to 20-25 per cent in next five year. Being a market leader in the industry, we believe Polycab to be a key beneficial from this shift. Going forward, the demand for wire & cable industry is likely to grow stronger, owing to various government initiatives in power and infrastructure such as huge spending on infrastructure, growth in fire survival cables underpinned by metro, airport and commercial real estate projects and investment by smart cities in underground cables.

The company has a diverse customer base which includes governmental authorities, retailers, distributors, dealers and industrial and institutional customers. Also, the clients belong to various industries such as power, oil and gas, construction, IT parks, infrastructure, metal and non-metal, cement, agriculture and real estate industries. This diversification reduces the risk of concentration.

Focus on R&D

The company spends heavily on the research and development which eventually helps Polycab to launch new and innovative products in the market. In 2017, the company had launched environmentally friendly power cables that consume less power, to meet the

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growing demand for green products. Further, the company is developing specialized, innovative and quality cables such as automotive cables, rubber (elastomeric) cables, and e-beam irradiated cables to serve the needs of the automobile, ship-building industry, mining, solar energy, and rolling-stock sectors.

Financial performance

Over the last five years, the company has recorded a strong growth of 14 per cent CAGR in its revenue, while, its EBITDA and profit after tax has grown at a CAGR of 22 per cent and 33 per cent, respectively.

In the recent quarter (Q1FY20), the company's consolidated net sales grew by nearly 15 per cent yoy to Rs. 1933 crore. Wire & Cable segment recorded revenue growth of 7.3 per cent yoy, while, FMEG business reported stellar 62 per cent yoy growth and revenue from other business jumped 136.6 per cent yoy. EBITDA for the period too increased by almost 19 per cent yoy to Rs. 205.3 crore with corresponding margin expansion of 35 bps. EBITDA margin for the quarter stood at 10.62 per cent. Notably, profit after tax surged almost 68 per cent yoy to Rs. 135 crore. PAT margin for the quarter too jumped to 6.99 per cent from 4.78 per cent in corresponding quarter of previous year.

In terms of leverage, the company is virtually debt free (0.06x of D/E) as on Q1FY20 and its net cash too stood healthy at Rs. 667.6 crore.

Valuation and outlook

In terms of return ratios, Polycab's ROE and ROCE have improved significantly from 10 per cent and 16 per cent in FY15 to 18 per cent and 28 per cent, respectively in FY19. However, currency fluctuations and major slowdown in demand may have adverse impact on company's performance. Company's backward integration plan would help in adequate & quality input materials and also to lower material cost. Being a market leader in the industry, Polycab is likely to benefit from the growing demand for wire and cable. Healthy balance sheet, strong return ratios coupled with industry leadership position gives us confidence to invest in the stock. Currently, the stock of Polycab is available at P/E multiple of 20.3x on TTM earnings. We believe the stock has potential to touch mark of Rs. 850 apiece, which represents potential upside of 22 per cent.

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

Description	201903	201803	201703	201603	201503
Net Sales	7955.98	6770.30	5500.12	5186.83	4708.12
Total Income	8049.33	6834.74	5575.33	5198.69	4719.27
Total Expenditure	7032.79	6041.42	5020.17	4700.85	4268.08
PBIDT	1016.54	793.32	555.16	497.84	451.19
PAT	502.63	358.46	233.08	187.96	160.32
Dividend %	30.00	10.00	10.00	17.50	15.00
Adj. EPS(Rs)	35.39	25.35	16.46	13.31	11.35

Quarter On Quarter (Consolidated) (Rs in Crore)

Particulars	201906	201903	Q on Q Var%	201806	Y on Y Var%
Net Sales	1932.98	2444.80	-20.93	1682.65	14.88
Total Expenditure	1727.70	2220.13	-22.18	1509.82	14.43
PBIDT (Excl OI)	205.29	224.67	-8.63	172.83	18.78
PAT	135.05	134.97	0.06	80.45	67.87
PBIDTM% (Excl OI)	10.62	9.19	15.56	10.27	3.41
PBIDTM%	13.31	10.66	24.86	11.64	14.35
PATM%	6.99	5.52	26.63	4.78	46.23
Adj. EPS(Rs)	9.10	9.72	-6.38	5.45	66.97

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