

Finolex Industries Ltd.

No. of shares (m)	124.1
Mkt cap (Rs crs/\$m)	8092/1206.3
Current price (Rs/\$)	652/9.7
Price target (Rs/\$)	814/12.1
52 W H/L (Rs.)	753/530
Book Value (Rs/\$)	189/2.8
Beta	0.6
Daily volume NSE (avg. monthly)	26480
P/BV (FY18e/19e)	3.2/3.0
EV/EBITDA (FY18e/19e)	16.7/13.9
P/E (FY18e/19e)	29.6/24.0
EPS growth (FY17/18e/19e)	51.6/-21.5/21.8
OPM (FY17/18e/19e)	21.6/15.8/16.3
ROE (FY17/18e/19e)	19.9/11.8/12.7
ROCE(FY17/18e/19e)	18.9/11.5/12.5
D/E ratio (FY17/18e/19e)	0.0/0.1/0.0
BSE Code	500940
NSE Code	FINPIPE
Bloomberg	FNXP IN
Reuters	FINX.BO

Shareholding pattern

	%
Promoters	52.5
MFs / Banks / FIs/Others	8.8
FPIs	4.4
Govt. Holding	0.0
Public & Others	34.1
Total	100.0

As on Mar 31, 2018

Recommendation

BUY

Analyst

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Company Brief

Headquartered in Pune, Finolex Industries is one of India's leading manufacturers of pvc -U pipes & fittings and pvc resin. Its pipes and fittings largely find use in the agriculture segment followed by construction and industrial segments. Its plants are located in Maharashtra and Gujarat.

Highlights

- Various Government of India sponsored schemes of a motley of outlay and focus - from PMAY which centers on both subsidized rural and urban housing to AMRUT that focuses on strengthening urban infrastructure including water supplies to PMKSY that lays impetus on irrigation sector to Swachh Bharat Mission that mainly emphasizes on building toilets in rural and urban areas. All these schemes not only patently boost demand for both agri and non-agri pipes but also help migration of value added products - cpvc products case in point.
- Unbridled demand for pvc resin in India largely emanating from irrigation and construction sectors have little mustered per capita consumption which is still a sixth of US and a fifth of China's. Yet GOI's renewed focusing on housing and agriculture has resurrected demand for pvc pipes, aggravating reliance on pvc imports. Diverse application of pvc - profiles & tubes; wires & cables; flooring; moulded products- has little restrained demand.
- Greater focus on expanding distribution network in northern and eastern regions to enhancing volume share of fittings segment to gradually erect capacities of pvc pipes - 290000 mt in FY17 to 370000 mt this fiscal - all manifest unflinching focus on tweak in its business model from B2B to B2C, not quashed by rising captive use of pvc and not subdued brand initiatives.
- Backward integration into pipe manufacturing has ensured steadier supplies of pvc - also earning Finloex a distinction of India's sole integrated pvc pipe manufacturer. Wherefore, external sales of pvc has abysmally plunged in last few years, helping redefining of its business model.
- The stock currently trades at 29.3x FY18e EPS of Rs 22.28 and 24x FY19e EPS of Rs 27.13. India's low per capita pvc consumption coupled with GOI growth propping initiatives would circumvent suppression of demand for external factors - vagaries of monsoons; depressing volatility in global pvc prices. Measured expansion of pvc pipe & fittings capacity would help expand market reach; and so would vigorous roll out of cpvc products. Weighing odds, we assign a buy rating on the stock with target of Rs 814 based on 30x FY19e earnings (forward peg: 1.4) over a period of 9-12 months.

(Figures in Rs crs)

	FY15	FY16	FY17	FY18e	FY19e
Income from operations	2476.15	2481.91	2602.36	2890.48	3351.42
Other Income	20.24	64.12	24.34	32.04	36.75
EBITDA (other income included)	209.83	468.56	587.36	487.91	581.66
Profit after EO	48.25	232.26	352.18	276.47	336.66
EPS (Rs)	3.89	18.72	28.38	22.28	27.13
EPS growth (%)	-71.6	381.4	51.6	-21.5	21.8

Company Overview

Leading supplier of PVC pipes & fittings, Finolex Industries also manufactures PVC resin (both suspension and emulsion PVC) at its Ratnagiri plant -set up in technical collaboration with Uhde GmbH, Germany with Hoechst technology - having installed capacity of 2.72 lakh mtpa. To ensure seamless supply of materials, it has also set up an open cryogenic jetty as part of its PVC complex. Fortified by its wide network of 18000 retail outlets, Finolex supplies various kinds of ISO 9001:2008 certified PVC pipes for agricultural and plumbing and sanitation applications; agricultural pipes include casing pipes; column pipes; plumbing and sanitation pipes & fittings include astm pipes; cpvc pipes; sewerage pipes; swr pipes

Apart from Ratnagiri facility, it has pvc pipe manufacturing facilities at Urse (Maharashtra) and Masar (Gujarat). Its products have bagged certifications from BIS (Bureau of Indian Standards) and MCGM (Municipal Corporation of Greater Mumbai). To ensure faster and efficient distribution of its wares, warehouses have been set up in Chinchwad, Cuttack, Delhi, and Indore.

Product Profile

PVC resin division

With an installed capacity of 2.72 lakh mtpa - last time capacity increased by 12000 mtpa in FY13 - Finolex's resin manufacturing plant in Ratnagiri - spread over 650 acres -imports key raw materials like ethylene dichloride (EDC), ethylene, and vinyl chloride monomer (VCM) from international markets for producing PVC resin of both suspension and emulsion types; uses its own jetty in Ratnagiri for import of aforesaid raw materials. Set up with an initial capacity of 1.3 lakh mtpa in 1994, the plant's pvc resin capacity was doubled to 2.6 lakh mtpa in 2006. For information pvc resin finds application in numerous areas including pipe manufacturing, cable insulation, window profiles and blister packaging.

PVC-U Pipes Division

Pipes of various sizes, pressure classes and diameters are being rolled out from its plants at Ratnagiri, Urse and Masar for catering to both agricultural and non-agricultural sectors including housing, industrial and construction. To meet rising demand, Finolex has relentlessly increased its pipes capacity; new plant set up in Masar, Gujarat in 2012; capacity increased by 30000 mtpa to 2.8 lakh mtpa in 2016 and further to 2.9 mtpa in FY17. PVC used for pipe manufacturing is largely taken from its plant in Ratnagiri, ensuring seamless supplies of materials.

Agricultural pipes

- **Agriculture pipes and fittings** - Selfit pvc-U pipes; Ringfit pvc-U pipes; various types of moulded and fabricated fittings
- **Casing pipes:** CS casing pipes; CM casing pipes; screen pipes with ribs; SDR series casing Pipes
- **Column pipes-** pvc -U column pipes
- **Solvent cement:** pvc-U solvent cement for agriculture applications; pvc-U solvent cement for higher dia agriculture applications; rubber lubricant

Non -Agricultural pipes

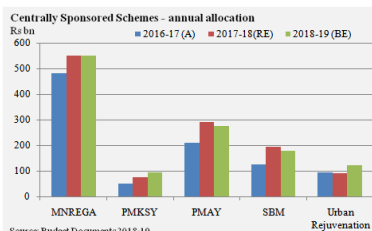
- **Finolex FlowGuard Plus CPVC pipes and fittings-** Finolex FlowGuard Plus CPVC pipes; various types of Finolex FlowGuard fittings
- **Plumbing pipes and fittings:** heavy pressure plumbing pipes; ASTM PVC-U Pipes; various types of fittings
- **Sewerage pipes (underground drainage pipes):** Selfit sewerage pipes; Ringfit sewerage pipes
- **Solvent cement:** medium duty PVC-U solvent cement for plumbing applications; heavy duty PVC-U solvent cement for plumbing applications; PVC-U solvent cement for SWR applications; CPVC solvent cement for hot and cold water plumbing applications; rubber lubricant; primer
- **SWR pipes and fittings:** SWR Selfit pipes; SWR pipes with integrated rings; SWR Selfit moulded fittings and SWR fittings with integrated rings

Investment Thesis

GOI Initiatives

If Indian government schemes have anything worthy of demonstration, then Indian housing and irrigation sectors are agog with not puny opportunities. Much touted Prime Minister Awas Scheme proposes to complete construction of 10m rural houses by 2019; already sanctioned 3.7m houses for construction in urban areas; though the pace of urban house building dreadfully slowed in 2016-17 - only 1.49 lakh houses were built as against a target of 32.6 lakh units, barely preventing the India government to set a target of constructing 12 lakh urban houses in 2017-18. To give a fillip to affordable housing sector, the Government of India in its recently unveiled federal budget, announced setting up a dedicated affordable housing fund under the National Housing Board (NHB) - funded by priority sector lending shortfall and GOI's authorized bonds.

Widening the reach of AMRUT, the federal budget 2019 announced that the scheme would focus on water supply to all households in 500 Indian cities; GOI to award nearly 500 contracts worth Rs 19428 crs. To give an impetus to the irrigation sector, budgetary allocation under Prime Minister Krishi Sinchai Yojna (PMKSY) was all but doubled recently and an additional budgetary support of Rs 15000 crs was provided for completing 48 priority projects under PMKSY-AIBP to be completed by December 2019. Indeed GOI's unstinted focus on rejuvenating the hinterland has cornered much of the attention of Indian pipe manufacturers.



	PMAY Progress (Urban)*						
	project proposal considered	Financial progress (Rs crs)			Physical progress (lakh units)		
		investment	central assistance involved	released	houses involved	under construction	completed
States	8776	243627	64666	22988	42	18	4
NE States	323	6315	3504	1225	2	1	0
Uts	22	1035	246	139	0	0	0
total	9121	250977	68416	24352	44.4	19.3	4.0

Source: Ministry of Housing & Urban Affairs, GOI

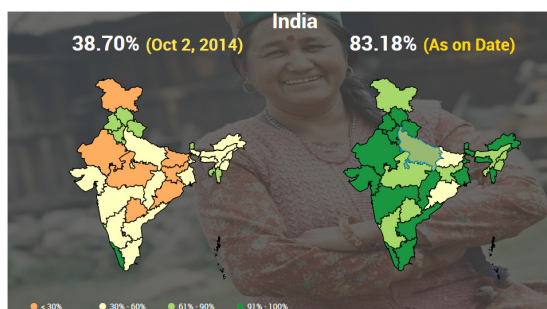
* including RAY and CLSS components

Rural sanitation got a leg up from GOI's intent on widening rural coverage under Swachh Bharat Mission (Gramin) - already up from 42% in 2014 to 64%. Increased allocation for land mark GOI schemes like Pradhan Mantri Fasal Bima Yojana, Pradhan Mantri Krishi Sinchai Yojana and MGNREGA are patently aimed at emboldening Indian agriculture sector. At the heart of Indian agriculture is the irrigation infrastructure for more than half of India's cultivated land is affected by vagaries of monsoons.

SBM (Gramin) - Household Toilet Coverage

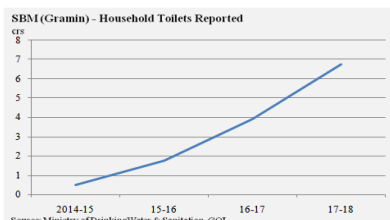
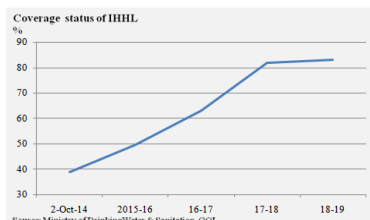
PMAY (Gramin) - 2017-18 Allocation (Rs crs)			
	MoRD Target	Central allocation	State allocation
States	31801	24249	15969
NE States	491	597	66
Uts	11	14	0
total	32303	24860	16035

Source: Ministry of Rural Development, GOI



Source: Ministry of Drinking Water and Sanitation, GOI

Housing demand from middle income group is expected to rise with increased focus on affordable housing, which would also get a boost from refinancing by National Housing Board. Implementation of RERA would do wonders for the Indian housing sector.



Lubrizol tie up

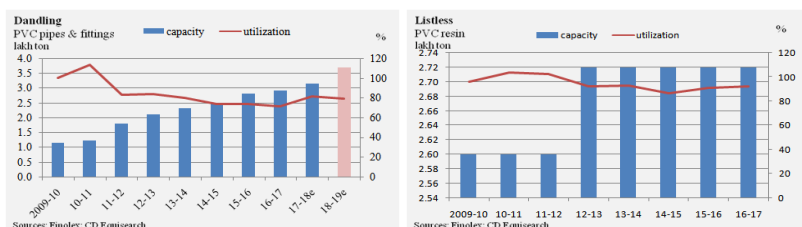
Capitalizing on not yielding demand for cpvc products in India, Finolex tied up with Lubrizol Corporation, world leaders in cpvc resin and compounds, for sourcing cpvc compound for manufacturing of Finolex FlowGuard Plus pipes and fittings in India for sale to building & construction industry. Used largely for hot & cold plumbing in homes, hotels, hospitals etc, cpvc pipes has yet to convincingly test waters in India - accounting for less than 10% of the overall pipes and fittings market by volumes. Yet the demand would remain little subdued for the builders have started to use common cpvc pipes for both hot and cold water application instead of separate pipes. Government initiatives to promote housing - both rural and urban - would also do its bit to buoy demand. Though on low base, Finolex's cpvc volumes have stunningly risen - up by nearly 50% in nine months of FY18, not alleviating need for ramp up in production at its Pune plant.

Capex

Gauging rising demand for pvc pipes & fittings, Finolex is pulling out all stops to boost capacity by some 80000 mt - entailing capex of Rs 250 crs (\$37.3m), almost equally split between FY18 & FY19, furthering its cause of gradual asset accretion. Motley of schemes to corner regional markets have been carved in the past - from setting up of plant in Masar (Gujarat) for vanquishing North Indian market to setting up a pipes and fittings warehouse in Cuttack to expand operations in East India and North East India to erecting warehouses in Delhi and Indore to service north and central India markets. Yet little capacity of PVC resins has undergone little change in last few years, save for doubling to emulsion pvc resin capacity by 11000 mt in FY13, not least due to higher capital costs involved. Resultantly pvc resin capacity utilization has barely dipped below 90% in the past.

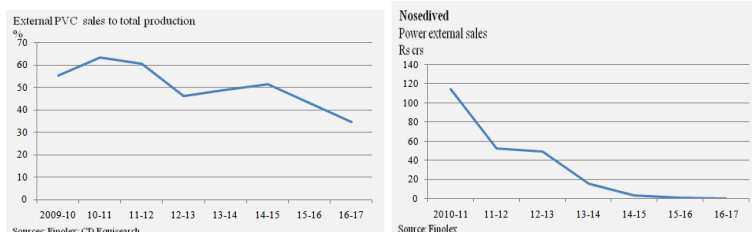
CD Equisearch Pvt Ltd

Yet product tweaks / introductions has been barely missed - from introduction of underground sewerage pipes in 2007 to lead free plumbing pipes as per ASTM standard in 2008 to setting up plant in Pune for agriculture pipes and casing pipes in 2009 to rolling out of ASTM pipes for plumbing sector a couple of decades back. Seasonality of demand for agricultural pipes has doubtlessly stressed capacity utilization, most pertinently in five years ending FY17 (see chart).



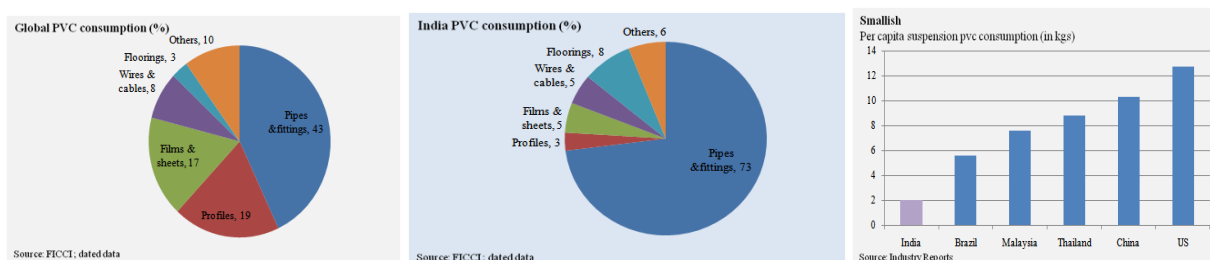
Backward Integration

Cost optimization coupled with regular supply of pvc resin for pvc pipe & fittings production has been one of the cornerstones of Finolex's backward integration strategy. Wherefore, pvc resin external sales have woefully vacillated over the years - from 1.71 lakh mtpa in FY11 to 0.87 lakh mtpa in FY17, thus trending with unrelenting production of pvc pipes & fittings. Yet unsettling variations in prices of key crude oil based raw materials - ethylene; EDC; vcm - and tightening supplies (as seen in the past) perils perpetuating EDC-PVC spreads; shortfalls in key raw materials like vcm stifled its ability to optimally run its plants in FY07 and FY08. Finolex's captive power plant at Ratnagiri has barely evaded scrutiny for external sales of power have noticeably dwindled in last few years, alluding substantial cost benefits (compared to grid cost).



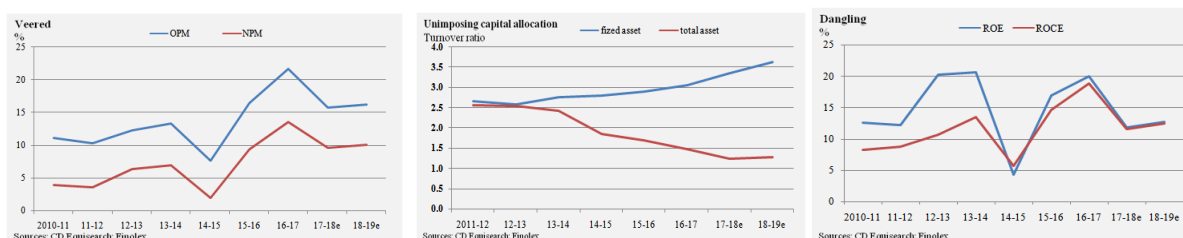
Financials & Valuations

PVC global market estimates of Research and Markets, a market research firm, point to 3.74% (CAGR) during 2017-2021 driven by some 5.5% CAGR in global infrastructure with APAC leading the pack; China major growth driven followed by India and other developing Asian economies. Infrastructural spending - buttressed by electricity and power projects and higher investments in railways, road projects, airports and docks and water and sewage projects - would buoy global pvc demand. Adoption of new technologies in refracturing of old shale wells has boosted US shale gas output and thus low-cost ethylene - a major pvc material. It also reckons that increasing use of high performance plastics to reduce vehicle weight and for higher fuel efficiency, growing demand from construction industry in APAC region and growing application in healthcare industry and medical devices market have done little to distress pvc output.

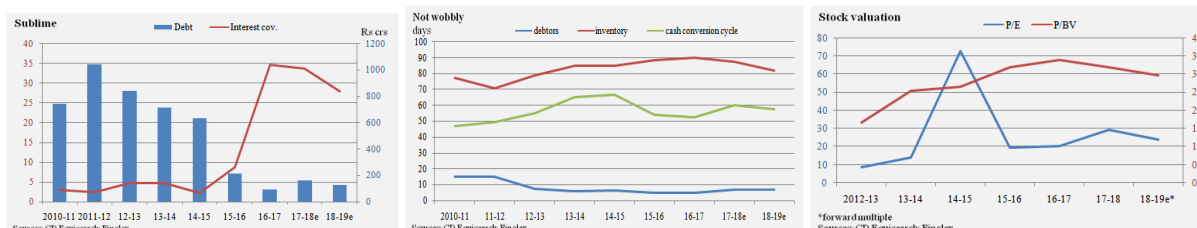


Not oblivious of changing global landscape - most pertinently in India of pvc pipes - Finolex Industries have been assiduously rummaging opportunities for increased national presence - with enhanced focus on eastern and northern markets, aptly supported by higher installed capacities. Thence pvc pipes & fittings dispatches have shown little weakling in past few quarters - for Finolex has gone on rampage to grab larger market share not without loss of pricing power; dispatches up by 50.2% in Q3. Disdainful withering of margins - OPMs slid from 22.5% to 15.7% in Q3- on backdrop of record volume growth is not stirring.

Yet sustaining unreasonable business growth is not without perils. Its pvc pipes & fittings volume growth would probably settle at sub 15% this fiscal year with slightly higher margins. Large operating cash flows would not only help fund capex of Rs 250 crs (FY18 & FY19 combined) but also check debt accretion. Still not paltry challenges have come to fore in revving un-striking return on capital not least due to timid profits in FY18 and relentless revaluation of FVOCI equity instruments - ROE estimated to wither to 11.8% in FY18 from 19.9% a year before.



The stock currently trades at 29.3x FY18e EPS of Rs 22.28 and 24.1x FY19e EPS of Rs 27.17. Unrelenting growth in APAC pvc market paired with huge under penetration of pvc market in India has no austere effect. Though Finolex's debt accretion has been contained but cross holdings have stymied efficient capital allocation, pinching return on capital. Moderation in pvc pipe & fittings volume would scarcely stymie growth in earnings - estimated to grow by 22% in FY19. On balance we recommend buying the stock with target of Rs 815 based on 30x FY19e earnings.



Risks & Concerns

Commodity price fluctuations

For PVC manufacturing, Finolex imports key petrochemical products namely, vinyl chloride monomer (VCM), ethylene and ethylene dichloride (EDC) from international markets. Though its pvc prices are regularly adjusted for import parity price of PVC in international market, little scope exists for evading adverse impact of short term fluctuations in key raw material prices. Crude oil prices continue to exert great impact on prices of its finished goods; VCM, EDC and ethylene together constituted nearly 60% of total raw material cost in FY16.

Foreign exchange risk

Although Finolex is greatly exposed to fluctuations in exchange rates - not least due to its very large import bill, its revenues (arising from PVC resin) are linked to import parity pricing of PVC resin, acting as a natural hedge.

Cross Sectional Analysis

Company	Equity*	CMP	Mcap*	Sales*	Profit*	OPM (%)	NPM (%)	Int. Cov.	ROE (%)	DER	Mcap / sales	P/BV	P/E
Astral Poly	12	969	11612	2042	166	14.1	8.3	19.3	25.9	0.3	5.7	16.2	69.8
Finolex Ind.	124	652	8092	2825	308	17.0	10.9	60.1	14.0	0.1	2.9	3.5	26.2
Supreme Inds	25.4	1374	17459	4966	432	15.8	8.0	28.5	26.4	0.1	3.5	9.9	40.4

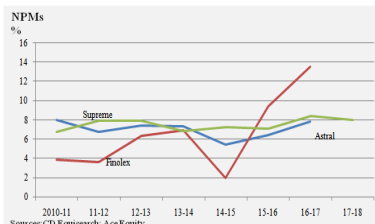
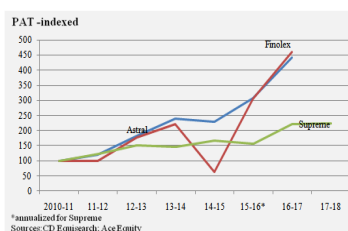
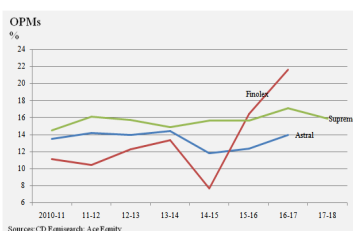
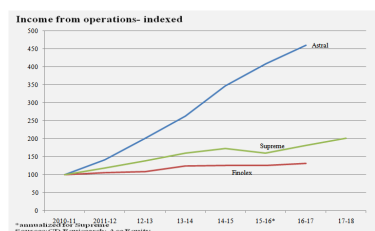
*figures in crores; calculations on ttm basis

Book value adjusted for goodwill and revaluation reserves where applicable

Hindered by placid recovery in its plastic piping system business and pinching capacity constraints in packaging products, Supreme Industries overall volume fluttered last fiscal - second consecutive year of sub 10% growth; growth quivered in Q4 for dispatches of its most illustrious plastic piping systems business markedly slowed to 7.7% in Q4; packaging products' slid 2.8%. Yet generally not so effervescent industrial products bucked the trend to post 16.5% volume growth in Q4; led by 16.9% rise in consumer products.

After realigning planned capex with ground realities last fiscal, Supreme now plans to spend Rs 300-350 crs in the current fiscal largely in setting up a couple of greenfield units in Assam and Andhra Pradesh ; two more greenfield units would get commission in the current fiscal - one at Telangana and the other at Rajasthan. Capex for current fiscal also include new plant for protective packaging product at Jadcharla and higher capacities for HDPE and plastic pipes.

Faster shift to organized market - instigated by both GST and demonetization - partially helped explain some 19% growth in Astral's plumbing prejudiced pipes & fittings volumes in 9M - 28.4% in Q3 - though not aptly supported by the real estate market. Thanks to fall in raw material prices, gross margins expanded for its plastic business so far this fiscal. Cut throat competition in Indian agricultural piping segment has caught producers unawares, prompting Astral to assiduously focus on the plumbing market. For expanding its footprint in North and North-East regions and also save on logistics the company is hastening completion of its plant at Rajasthan by this month end. Capacity at its Hosur plant is being doubled - production to be commenced in Q1 not only to enhance its Southern market presence but also save logistics costs.



Financials

Quarterly Results

Figures in Rs crs

	Q3FY18	Q3FY17	% chg.	9MFY18	9MFY17	% chg.
Income from operations	722.72	576.50	25.4	1928.66	1706.18	13.0
Other Income	10.25	2.86	258.6	25.02	14.97	67.1
Total Income	732.98	579.36	26.5	1953.68	1721.15	13.5
Total Expenditure	609.39	446.79	36.4	1635.10	1330.24	22.9
EBIDTA (other income incl.)	123.58	132.57	-6.8	318.58	390.91	-18.5
Interest	-0.36	5.93	-106.0	6.45	14.20	-54.6
Depreciation	15.37	14.03	9.6	45.01	41.17	9.3
PBT	108.58	112.61	-3.6	267.12	335.54	-20.4
Tax	39.03	40.66	-4.0	89.53	114.23	-21.6
Net Profit	69.55	71.95	-3.3	177.60	221.31	-19.8
Extraordinary Item	-	-	-	-	-	-
Adjusted Net Profit	69.55	71.95	-3.3	177.60	221.31	-19.8
EPS	5.60	5.80	-3.3	14.31	17.83	-19.8

Segment results

Figures in Rs crs

	Q3FY18	Q3FY17	% chg.	9MFY18	9MFY17	% chg.
Segment Revenue						
PVC	459.84	437.88	5.0	1262.54	1147.39	10.0
PVC Pipes & Fittings	532.01	444.58	19.7	1646.16	1512.69	8.8
Power	37.68	37.84	-0.4	101.84	108.76	-6.4
Total	1029.53	920.30	11.9	3010.54	2768.84	8.7
Less: Inter-segment revenue	306.81	257.87	19.0	988.26	806.09	22.6
Income from operations	722.72	662.43	9.1	2022.28	1962.75	3.0
Segment EBIT						
PVC	80.24	93.32	-14.0	212.56	237.56	-10.5
PVC Pipes & Fittings	29.57	30.27	-2.3	72.18	112.23	-35.7
Power	2.05	8.58	-76.1	6.38	27.31	-76.7
Total	111.86	132.17	-15.4	291.11	377.10	-22.8
Interest	-0.36	5.93	-106.0	6.45	14.20	-54.6
Unallocable exp.(net of income)	3.64	13.63	-73.3	17.54	27.36	-35.9
PBT	108.58	112.61	-3.6	267.12	335.54	-20.4

Income Statement

Figures in Rs crs

	FY15	FY16	FY17	FY18e	FY19e
Income from operations	2476.15	2481.91	2602.36	2890.48	3351.42
<i>Growth (%)</i>	0.9	0.2	4.9	11.1	15.9
Other Income	20.24	64.12	24.34	32.04	36.75
Total Income	2496.39	2546.03	2626.70	2922.52	3388.16
Total Expenditure	2286.56	2077.48	2039.35	2434.61	2806.50
EBIDTA (other income incl.)	209.83	468.56	587.36	487.91	581.66
Interest	70.37	44.71	15.34	12.69	17.60
EBDT	139.45	423.85	572.01	475.22	564.07
Depreciation	58.67	50.57	55.05	61.03	68.23
Tax	33.00	118.87	164.78	137.72	158.67
Net Profit	47.78	254.41	352.18	276.47	337.17
EO	-0.47	22.15	-	-	-
Adjusted Net Profit	48.25	232.26	352.18	276.47	337.17
EPS (Rs)	3.89	18.72	28.38	22.28	27.17

Balance Sheet

Figures in Rs crs

	FY15	FY16	FY17	FY18e	FY19e
SOURCES OF FUNDS					
Share Capital	124.10	124.10	124.10	124.10	124.10
Reserves	1233.79	1445.75	2167.30	2610.76	2805.70
Total Shareholders Funds	1357.89	1569.85	2291.39	2734.85	2929.80
Long term debt	183.29	-	-	-	-
Total Liabilities	1541.17	1569.85	2291.39	2734.85	2929.80
APPLICATION OF FUNDS					
Gross Block	867.77	896.52	955.90	1030.90	1205.90
Less: Accumulated Depreciation	0.00	46.87	100.77	161.81	230.04
Net Block	867.77	849.65	855.13	869.10	975.86
Capital Work in Progress	10.40	6.62	21.75	50.00	0.00
Investments	720.40	817.21	1222.17	1659.49	1751.57
Current Assets, Loans & Advances					
Inventory	558.65	447.22	557.40	608.65	645.50
Sundry Debtors	48.70	17.63	52.49	57.81	67.03
Cash and Bank	12.30	10.41	16.34	25.82	29.98
Loans and Advances	123.61	123.06	92.96	90.53	87.95
Total CA & LA	743.27	598.32	719.20	782.81	830.45
Current Liabilities	737.57	585.74	455.46	536.96	525.15
Provisions	0.93	1.09	1.23	1.39	1.55
Total Current Liabilities	738.50	586.84	456.70	538.35	526.70
Net Current Assets	4.77	11.48	262.50	244.46	303.75
Net Deferred Tax	-111.94	-127.61	-131.61	-142.49	-159.78
Other Assets (Net Of Liabilities)	49.77	12.50	61.46	54.29	58.39
Total Assets	1541.17	1569.85	2291.39	2734.85	2929.80

Cash Flow Statement

Figures in Rs crs

	FY17	FY18e	FY19e
Net Income (a)	352.18	276.47	336.66
Non cash exp. & others (b)	35.70	49.87	51.78
Depreciation	55.05	61.03	68.23
Deferred tax	5.45	10.88	17.29
Interest income	-2.17	-2.30	-2.30
Loss on asset sale	0.02	0.00	0.00
Others	-22.64	-19.74	-31.45
(Increase) / decrease in NWC & others (c)	-169.80	-31.13	-24.17
Inventory	-110.18	-51.25	-36.84
Other assets (net of liabilities)	-59.63	20.12	12.67
Operating cash flow (a+b+c)	218.07	295.21	364.27
Purchase of fixed assets	-94.42	-103.25	-125.00
sale of fixed assets	0.80	0.00	0.00
Sale of investments	122.83	-86.64	-47.25
Interest received	2.17	2.30	2.30
Grants	9.74	0.00	0.00
Dividend received	6.71	7.81	8.69
Investing cash flow (d)	47.83	-179.79	-161.26
Net borrowings	-112.54	65.82	-35.00
Dividends paid (including CDT)	-147.44	-171.77	-164.30
Financing cash flow (e)	-259.98	-105.95	-199.30
Net change (a+b+c+d+e)	5.93	9.47	3.71

Key Financial Ratios

	FY15	FY16	FY17	FY18e	FY19e
Growth Ratios (%)					
Revenue	0.9	0.2	4.9	11.1	15.9
EBIDTA (other income included)	-43.1	107.0	34.7	-16.9	19.2
Net Profit	-71.6	381.4	51.6	-21.5	22.0
EPS	-71.6	381.4	51.6	-21.5	22.0
Margins (%)					
Operating Profit Margin	7.7	16.4	21.6	15.8	16.3
Gross Profit Margin	5.7	15.8	22.0	16.4	16.8
Net Profit Margin	1.9	9.4	13.5	9.6	10.1
Return (%)					
ROCE	5.7	14.6	18.9	11.5	12.5
ROE	4.3	16.9	19.9	11.8	12.7
Valuations					
Market Cap / Sales	1.4	1.8	2.8	2.8	2.4
EV/EBIDTA	19.4	10.4	12.3	16.7	13.9
P/E	73.0	19.5	20.4	29.6	24.0
P/BV	2.7	3.2	3.4	3.2	3.0
Other Ratios					
Interest Coverage	2.2	8.6	34.7	33.6	29.2
Debt-Equity Ratio	0.5	0.1	0.0	0.1	0.0
Current Ratio ^a	1.0	1.0	1.2	1.3	1.5
Turnover Ratios					
Fixed Asset Turnover	2.8	2.9	3.1	3.4	3.6
Total Asset Turnover	1.9	1.7	1.5	1.2	1.3
Debtors Turnover	55.2	74.8	74.2	52.4	53.7
Inventory Turnover	4.3	4.1	4.1	4.2	4.5
Creditors Turnover	14.7	9.4	8.7	10.6	11.9
WC Ratios					
Debtor days	6.6	4.9	4.9	7.0	6.8
Inventory days	85.0	88.5	89.9	87.4	81.6
Creditor days	24.9	39.0	42.1	34.4	30.6
Cash conversion cycle	66.7	54.4	52.7	60.0	57.8

Cumulative Financial Data

Figures in Rs crs	FY11-13	FY14-16	FY17-19
Income from operations	6222	7411	8844
Operating profit	701	925	1564
EBIT	590	846	1473
PBT	404	664	1427
PAT	289	451	966
Dividends	166	281	530
PVC pipe sales (mt lakh tons)	4.64	5.71	7.60
PVC resin production (mt lakh tons)	7.88	7.34	8.27
PVC resin sales (mt lakh tons)	4.50	3.52	2.67
OPM (%)	11.3	12.5	17.7
NPM (%)	4.6	6.1	10.9
Interest coverage	3.2	4.7	32.3
ROE (%)	14.6	14.0	15.5
ROCE (%)	9.4	12.2	14.8
Fixed asset turnover	2.4	2.9	3.2
Debtors turnover	55.4	87.7	69.6
Inventory turnover	4.5	4.6	4.4
Creditors turnover	9.9	10.1	10.1
Debtors days	6.6	4.2	5.2
Inventory days	81.6	78.5	82.2
Creditor days	36.9	36.1	36.2
Cash conversion cycle	51.3	46.6	51.2
Dividend payout ratio (%)	57.8	59.4	54.9

FY11-13 implies three years ending fiscal 13; *as on terminal year

If it would not have been for cumulative effect of higher pvc realization (up ~30%) and lower prices of key raw materials like EDC and ethylene, operating profits would have scarcely grown in FY17 - up by 38.2% - an outlier by past measures and thus low chance of reoccurrence. As a consequence of this and robust pvc pipe volume growth so far in FY18 - 24% in 9M; cumulative volume in FY17-19 period projected a third higher - cumulative operating profit in FY17-19 period is not expected to meanly grow (69.1%) - see table - and post tax earnings to more than double. Merged impact of higher earnings and not puny debt retirement helped discernibly boost interest coverage ratio to the highest level in years. Higher captive consumption of pvc has relentlessly stymied external sales.

Though working capital has not soared yet - cash conversion cycle not refute that - noticeable gains in return on capital has not been unrestrained (see table), presumably due to unflinching accretion to its total asset base - precipitated by marking to market of FVOCI equity instruments. Still near optimum utilization of pvc resin capacity and so brisk ramp up of pvc pipe facility have little deleterious impact on asset turnover - fixed asset turnover ratio to soar to 3.2 in FY17-19 period from 2.9 in previous three year period.

Financial Summary – US dollar denominated

million \$	FY15	FY16	FY17	FY18e	FY19e
Equity capital	19.8	18.7	19.1	19.1	18.5
Equity shareholders' funds	212.2	214.1	326.9	395.2	407.7
Total debt	101.7	31.9	14.5	24.6	18.6
Net fixed assets (incl CWIP)	140.3	129.1	135.2	141.3	145.5
Investments	115.1	123.2	188.5	255.1	261.1
Net current assets	-4.0	-20.8	14.0	12.3	16.3
Total assets	241.5	214.1	326.9	395.2	407.7
Revenues	405.0	379.1	387.9	448.5	499.6
EBITDA	34.4	66.6	87.5	75.7	86.7
EBDT	22.9	59.8	85.3	73.7	84.0
PBT	13.3	52.1	77.1	64.3	73.8
PAT	7.9	35.5	52.5	42.9	50.2
EPS(\$)	0.06	0.29	0.42	0.35	0.40
Book value (\$)	1.71	1.73	2.63	3.18	3.29
Operating cash flow			33.6	45.4	54.3
Investing cash flow			7.4	-27.6	-24.0
Financing cash flow			-40.1	-16.3	-29.7

income statement figures translated at average rates; balance sheet and cash flow at year end rates; projections at current rate (\$67.08/\$)

Recommendation

Double digit growth in Indian PVC sector for last few years have not come about through a handful of factors but successes in varied means: agriculture; housing; infrastructure; retail. GOI's unstinted focus on building rural water and sanitation infrastructure and 'smart cities' project would undoubtedly buoy PVC demand and so would be an emphasis on bringing land under irrigation. Most notably, GOI's housing scheme for both rural and urban areas - Prime Minister Awas Scheme proposes to complete construction of 10m rural houses by 2019; already sanctioned 3.7m houses for construction in urban areas - does not have little demand galvanizing potential - by some measure one urban unit requires 200 kg of pvc in various applications while the same is approximately 75 kgs for a rural unit. Fledgling state of some new applications like wall cladding, liners for landfill application, decking and waterproofing membranes hold no smallish potential.

With Asia - Pacific now commanding over 50% of the global PVC market, center of activity has shifted to developing economies in Asia, namely China, India, Vietnam and Indonesia. Large drivers include a large population base coupled with a need for considerable infra spend. Industry reports suggest that Chinese pvc demand in 2018 is expected to remain stable-to firm as it develops new areas; however, no less grave uncertainty looms over environmental inspections, whose scale and severity would impact market, ordered by the government.

Setting up regional capacities to local warehouses - in Cuttack for east and north east India; in Indore for central India; Delhi for north India - have been done to corner larger market share in key markets. Yet high capital costs of pvc resin projects have ruled out a parallel asset erection binge - as a result captive consumption of pvc resin has spiked up over the years numbering some two-thirds in FY17, accentuated by its unflinching focus on backward integration. Yet propitious worthwhile benefits of backward integration have oftentimes been wrecked by high volatility in prices of key crude based raw materials like ethylene, EDC and VCM.

Expansion of Finolex product base has come to fore with its tie up with Lubrizol for sourcing cpvc compounds for manufacturing cpvc pipes & compounds, a giant leap from rolling out underground sewerage pipes in 2007 to lead free plumbing pipes in 2008. Yet it's too early to rejoice for the Indian cpvc industry is at a nascent stage forming less than a tenth of overall pipes & fittings market by volumes. Though Finolex's cpvc volumes have grown at a brisk pace in 9MFY18 but it has not advanced enough to make a weighty dent.

The stock currently trades at 29.3x FY18e EPS of Rs 22.28 and 24x FY19e EPS of Rs 27.13. While business growth has been barely austere for last few quarters but suppression in margins (high base effect) has constricted earnings growth, invoking ostensibly perceptible risks of varied kind - heavy rainfall; inadequate monsoons; gut-wrenching volatility in pvc prices. Yet with not so perilous impact of GST now, pvc pipes demand has started to gradually recover, helping Finolex to post robust earnings growth (22%) in current fiscal on subdued leverage. Its aggressive market expansion (volumes up over 50% in Q3) would also hold sway. Weighing odds, we assign a buy rating on the stock with target of Rs 814 based on 30x FY19e earnings (forward peg: 1.4) over a period of 9-12 months.

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buy: >20% accumulate: >10% to ≤20% hold: ≥-10% to ≤10% reduce: ≥-20% to <-10% sell: <-20%

Exchange Rates Used- Indicative

Rs/\$	FY14	FY15	FY16	FY17	FY18
Average	60.5	61.15	65.46	67.09	64.45
Year end	60.1	62.59	66.33	64.84	65.04

All \$ values mentioned in the write-up translated at the average rate of the respective quarter/ year as applicable. Projections converted at current exchange rate. Cumulative dollar figure is the sum of respective yearly dollar value.