

28th October 2020

CMP – ₹945.05/-

View – POSITIVE

Company Background

POLYCAB INDIA Ltd is an established player in the wires and cables business with more than 5 decades of experience and is a market leader with more than 12% share. The company provides its products under brand "**Polycab**". Polycab's business is spread over three segments: **Wires & Cables, FMEG** and **EPC**. It has managed to give a branding flavour to an otherwise commoditized wires and cables business. It has diversified into the FMEG segment in the past 5 years and forward integrated into the EPC segment. The company's product portfolio in the wires and cables segment includes power, control, instrumentation, solar, building, multi core, communication, welding, rubber, submersible flat & round, railway signaling, and specialty other cables. The FMEG segment includes electric fans, LED lighting and luminaries, switches, switchgears, solar products, water heaters and conduits & accessories. Polycab has 25 manufacturing facilities spread across 7 locations in India. Of the 25 manufacturing units, four units are for the production of FMEG products including a 50:50 joint ventures with Techno Electromech Pvt Ltd for the manufacturing of LED products and the manufacturing of copper rods in Ryker. The company recently purchased the balance 50% stake in Ryker plant from Trafigura Pte Ltd to make it a wholly-owned subsidiary. The company has backward integrated its operations by building manufacturing capabilities for all the key raw materials such as aluminum rods, copper rods, and various grades of PVC, rubber, XLPE compounds, GI wire and strip. Polycab supplies its products to retail outlets through a supply chain network of dealers, distributors and warehouses. It has a distribution network of more than 3,500 distributors and 125,000+ retails outlets evenly spread across all the regions in India. The company has 30 warehouses across 20 states & union territories to support its extensive distribution network for faster deliveries.

Important Statistics

MCap (₹ bn)	140.84
52week H/L (₹)	1180/572
NSE Code	POLYCAB
BSE Code	542652

Shareholding pattern (%) Sep'20

Promoter	68.5
DII	12.3
FII	6.1
Public & Others	13.1

Investment Arguments

- **Good Inroads in the FMEG segment** – With a highly diversified product mix, Cables & Wires accounts for 84-85% of total revenues. It is a market leader with more than 12% market share in the overall wires & cables market and more than 18% market share in the organized market. Over the last five years, Polycab has grown its revenue at a CAGR of 14% outpacing the overall industry growth of ~11%. The company has been improving its mix over the last few years from a relatively commoditized cable and wire business to making inroads in the FMEG (Fast Moving Electrical Goods) segment, which currently contributes 8-9% to the revenue mix. Over the last 4 years, its cable business has grown at a ~9% CAGR while the FMEG business has grown at ~43% CAGR though from a low base, resulting in a profit CAGR of 37% over the same period. The plan for the company is to drive synergies from the wires and cables business where it can also leverage on the brand and distribution network. 34% of the dealer network is still exclusive wires and cables. This provides the company with an opportunity to push its FMEG products through these dealers. The company's inhouse manufacturing strategy helps it get better control over the supply chain and quality of the products. This should help strengthen its position in the market where it can continue to garner share in this highly competitive space. It has successfully transitioned its 20% RoE business from being a B2B business to a B2C business by leveraging its tremendous brand equity through innovative ASP strategies and CRM programs. Polycab's FMEG business has lower margins due to higher upfront investment in setting up manufacturing facilities, setting up distribution networks, organizing supply chains and A&P spends. We expect operating

Financials

(₹mn)

Particulars	FY18	FY19	FY20	1HFY21
Revenue	67,703	79,856	88,300	30,903
<i>Wires and Cables</i>	62,423	69,295	75,192	25,343
<i>% of Revenue</i>	92.2	86.8	85.2	82.0
<i>FMEG</i>	4,853	6,433	8,536	3,818
<i>% of Revenue</i>	7.2	8.1	9.7	12.4
EBITDA	7,289	9,528	11,350	3,685
<i>EBITDA Margin (%)</i>	10.8	11.9	12.9	11.9
Net Profit	3,586	5,003	7,656	3,271
EPS (₹)	24.1	33.6	51.4	22.7
P/E (x)	39.2	28.1	18.4	
EV/EBITDA (x)	1.1	9.5	9.5	
P/BV (x)	5.7	3.2	2.8	
RoE (%)	16.5	19.3	22.9	
RoCE (%)	15.0	20.0	23.3	

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leverage benefits to drive the number closer to its peers. The company started with bigger segments like lights, fans, switches and switchgear. However, as these segments achieved a strong foothold in the market, the company moved its focus on improving profitability. To grow further and achieve economy of scope, the company entered smaller segments like pipes, pumps, etc. It now targets to quickly grow revenues of these smaller segments to reach ₹1bn each, post which it will focus on improving profitability in these segments.

- **It has also backward integrated to manufacturing copper rods**, which helps it have control over quality and timing of manufacturing. It also increased its backward integration by acquiring the other 50% of its JV with Trafigura in FY20 and is now a 100% owner of Ryker that manufactures copper rods. The copper rod plant began commercial operation in Q1FY20 with an annual capacity of 225,000 tonnes. The current utilization is at ~50% and for a part of the unutilized facility, the company is looking at alternatives and is open to partnerships. It has a wide range of products across customers with limited customer concentration risk. There is negligible dependence on China for raw materials as, for metals, most of the procurement is done from Japan and domestically and for non-metals, most of the procurement is done domestically and suppliers spread across the globe.
- **EPC business is a strategic forward integration where it seeks to bag those projects with 40-60% cabling requirements** – The EPC exposure helps the company set up a base in this segment for any future focus on this segment and helps in acquiring pre-qualifications. The Government's push on infra, digitization, smart cities, etc. augurs well for the company's EPC segment prospects. Similarly, India has less than 1% share in the global wire market of \$145bn and the China+1 strategy presents strong export opportunities for the company. To pursue exports, the company has identified 10- 12 new geographies with good business potential and has created 2 subsidiaries, one each in Australia and USA.
- **The focus on increasing the distribution network**, which currently comprises of more than 3,500 dealers (of this 34% are exclusively for wires and cables and 50% are exclusively for FMEG) should aid its scale up. The dealer network reduced from FY16 to FY19 as the company made a strategic decision to discontinue some smaller dealers and to focus instead on larger distributors who in turn would also cater to these smaller dealers. With the major part of the shift being completed, we expect the dealer network to only expand going forward. The combination of a multi-pronged growth strategy has enabled the company to grow its profits at a CAGR of 37% over the last five years.
- **Growth Strategy for wires and cables** – The plan for the company is to continue to invest in improving technology and drive revenues through secular business growth, garnering share from unorganized and increasing sustainable exports to 10% of total revenues. In FY20, the revenues from outside India seem higher on account of a one-time large order of ₹9.5bn from Dangote refinery in Nigeria. In FY20, ₹7.5bn of the Dangote order has been executed and the remaining order of ₹2bn is expected to be executed in FY21. The Dangote order is of great significance as the company proves itself as capable of handling large and complex orders and delivering it within a timeframe.

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- **Strategy to improve exports in Africa, Europe and the Middle East –** Profitability is likely to improve as the company achieves more scale and widens and deepens its distribution network. Polycab has a relatively lower A&P spends at 1.2% of sales when compared to peers, though currently only 35% of its business is B2C. However, as the FMEG business scales up, we expect them to increase investments in A&P over the medium term. Debottlenecking in the cables and wires business and focus to improve working capital through better inventory management and increased channel financing should further aid the margins and profitability. The plan is to merge the switchgears and wires business to drive synergies and increase cross-selling. The strategy to increase exports is through identified geographical clusters and penetrating business in those clusters. The company has identified 10-12 geographies where it can penetrate to achieve good business. There have been areas identified in Africa, Europe and the Middle East. It has also incorporated 2 subsidiaries, one each in Australia and US. For example, in Africa, a lot of World Bank projects get implemented and there is no import duty barrier, which provides an edge and a level playing field for Indian players.
- **Rebound in Q2FY21 –** The businesses got impacted due to the pandemic related lockdown. With the lockdown restrictions easing mid-May'20, trade sentiments improved and business started progressing. June ended sales down ~15% YoY. The first half of Jun'20 was good, but the second half lost steam as the company increased prices to pass on some of the copper price increase. Jul'20 had been growing strong with slight growth YoY till the first 3 weeks. Most of this could be attributed to pent up demand and some due to stocking on account of rising copper prices. Till 3rd week of Jul'20, sales in metros had returned to 30%-40% of normalcy while that of Tier 2 cities had returned to 80% normalcy. Improving overall business environment with staggered unlocking led to better performance sequentially. Revenue declined by 6% YoY in Q2FY21 to ₹21,137mn as against 50% YoY decline seen in Q1FY21. EBITDA increased by 16% YoY to ₹3,122mn with 272bps YoY improvement in margin, despite steady A&P spends, on account of higher contribution and cost saving initiatives. PAT was up 14% YoY to ₹2,216mn with PAT margin at 10.5%. Q2FY20 had a tax write back of ₹243mn due to reduction in statutory tax rate. Adjusting for that, PAT would have grown by 31% YoY in Q2 FY21 reflecting overall improved profitability.
- **Wires and Cables business** saw improving momentum with growth of 119% QoQ to ₹17,408mn on resumption of economic activities. The demand trends are encouraging and bodes well going ahead. B2C and exports sustained the strong traction. Domestic distribution channel sales performed better than institutional business with Tier 1 & below towns posting YoY growth. Metros continue to remain affected by localised lockdowns Within domestic distribution channel sales, housing wires business continued its momentum posting a double-digit growth in Q2FY21. Overall exports revenue grew by 47% YoY and contributed 10.7% to overall top-line in Q2FY21. Sales to Dangote amounted to ₹440mn in Q2FY21. Normalising it, exports grew strongly by about 400% YoY led by US, Australia, Asia, and Middle East.

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View – **POSITIVE****Polycab offers all the products in the wires & cables segment**

Players	Power & Power Control Cables (LT/HT)	Power Cables (EHV)	Control & Instrumentation Cables	House Wires	Flexible and Industrial Cables incl. specialty cables
Polycab India Ltd	✓	✓	✓	✓	✓
Finolex Cables Ltd	✓	✓	✓	✓	✓
Havells India Ltd	✓		✓	✓	✓
KEI Industries Ltd	✓	✓	✓	✓	✓
R R Kabel Ltd	✓		✓	✓	✓
V-Guard Industries	✓			✓	✓

Source: Company Data, Way2Wealth Inst Equity

Polycab Commands a Larger Pie in Wires & Cables Business

Polycab India Ltd	12%
Finolex Cables Ltd	5%
Havells India Ltd	6%
KEI Industries Ltd	7%
R R Kabel Ltd	4%
V-Guard Industries	1%
Other Organized Players	33%
Unorganized Players	32%

Source: Company Data, Way2Wealth Inst Equity

Cables & wires FY20 Revenues (₹mn) & EBIT Margin (%)

Players	Revenues (₹mn)	EBIT Margin
Polycab India Ltd	75,898	12.3
Finolex Cables Ltd	27,701	14.6
Havells India Ltd	29,942	16.3
KEI Industries Ltd	41,235	10.9

Source: Company Data, Way2Wealth Inst Equity

- **FMEG** saw a strong bounce back with total income growing by 25% YoY to ₹2440mn in Q2FY21 led by pricing, better product mix, distribution augmentation and reviving consumer demand. There was Resilient growth across the categories and regions. FMEG contribution to overall sales increased 268bpsYoY to 11.4%.

Fans grew strongly despite higher competitive intensity. 14 new products and over 40 new SKUs were launched in 1HFY21. Relatively stable price environment in Lighting business aided value growth. Pumps sales more than doubled on YoY basis. Switchgears saw a revival however switches remained muted due to operational issues.

Profitability in Q2FY21 improved sharply despite rising input costs on account of calibrated pricing actions, premiumisation and working capital interventions with EBIT margins at 8% compared to 3.3% last year.

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FMEG (Consumer Electric Durables) Product offerings of Players

Players	Fans	Lightings	Switches	Switchgears	Water Heater	Home app.	Kitchen App.
Polycab India Ltd	✓	✓	✓	✓	✓		
Bajaj Electricals	✓	✓			✓	✓	✓
Crompton Greaves Consumer	✓	✓			✓	✓	✓
Finolex Cables	✓	✓	✓	✓	✓		
Havells India	✓	✓	✓	✓	✓	✓	✓
Orient Electric	✓	✓		✓	✓	✓	✓
Philips India		✓				✓	✓
Schneider Electric India Pvt. Ltd	✓	✓	✓	✓			
Surya Roshni	✓	✓			✓	✓	✓
Usha International	✓					✓	✓
V-Guard Industries	✓			✓	✓	✓	✓

Source: Company Data, Way2Wealth Inst Equity

Products	Market Size (In ₹bn)	As a % of Polycab's FMEG Revenue	Polycab's Market Share %	Organized Penetration	Peers	Market Leader-Share (%)
Fans	80	40-45	~5	High	Crompton, Orient, Usha, Havells	Crompton - 25%
Lighting & Fixtures	100	20-25	~2	Medium	Phillips, Wipro, Syska, Crompton	Phillips - 23%
Switchgears	210	15-20	<1	High	Havells, Legrand, Schneider	Havells - 26%
Switches	45	15-20	<1	Medium	Panasonic (Anchor), Legrand, Havells	Anchor - 30-35%
Water Heaters	25	<5	<1	Medium	Racold, Havells, AO Smith	Havells - 17%

Source: Company Data, Way2Wealth Inst Equity

FMEG FY20 Revenues (₹mn) & EBIT Margin (%)

	Revenues (₹mn)	EBIT Margin
Polycab India Ltd	8,356	2.0
Crompton Greaves Consumer	45,203	16.5
Bajaj Electricals	30,948	6.5
Havells India	48,558	30.4

Source: Company Data, Way2Wealth Inst Equity

Players	Key Product Segments	Distributor Dealers / No of Retail Outlets (Approx.)
Polycab India Ltd	Cables, FMEG and EPC	3,500+ / 125,000+
Crompton Greaves Consumer	FMEG & Power Solutions	3,000+ / 150,000+
Bajaj Electricals	FMEG & EPC	1,000 / 160,000
Havells India	Cables, FMEG & Others	9,500 / 150,000+
Finolex Cables	Cables & FMEG	3,500+ / 40,000
KEI Industries	Cables & EPC	1,600
Orient Electric	FMEG	4,000+ / 100,000
Surya Roshni	FMEG	2,000 / 200,000
Usha International	FMEG & others	500 / 20,000
V-Guard Industries	Cables, FMEG & Others	564 / 25,000-30,000

Source: Company Data, Way2Wealth Inst Equity

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- **EPC business** was down on account of a stronger base. Total income and segmental EBIT in Q2FY21 declined by 65% YoY and 60% YoY, respectively. Annual sustainable operating margin in this business is expected to be in high single digit over mid to long term.

In a bid to gather sufficient liquidity to derive some financial comfort in this pandemic created uncertain business environment, the company resorted to initiatives like conserving liquidity through prudent cost management, deferring non-critical spends and availing additional credit lines. The company has strengthened its net cash position from ~₹1.6 bn at Mar'20-end to ~₹6.2bn at Sep'20-end.

➤ **Key Risks**

- **Raw Material Cost** – Copper and Aluminium form ~59% and ~14% of total cost of materials consumed respectively. PVC compounds / HDPE / LDPE / XLPE / Resin form ~13% of total cost of materials consumed. The total cost of materials consumed form ~67% of total revenues as of FY20. Prices of copper and aluminium are linked to prices on the London Metal Exchange while price of PVC compounds are linked to crude oil price. The company stores three to four weeks of inventory for all their primary raw materials. Usually the company is able to pass on the prices
- 84-85% of the company's revenue is from the wires and cables segment. The company is on the path to diversifying this risk by increasing the FMEG business. Increase in exports too should provide some geographical diversification benefits in the wires and cables segments. Current working capital days at 68 which is slightly higher than it peers

View

The company has an extensive distribution network, it has created a strong brand value through aggressive advertising and promotional campaigns. It is constantly increasing its distribution network by spending on advertising and promotions through multiple channels. Strong brand value along with extensive distribution network will help the company in launching new products. Its forward and backward integration plan augers well structurally for transformation in the current uncertain period to achieve higher future growth trajectory. Hence at a trailing *P/E 18.6x FY20* we are **POSITIVE** about the company with a fair value of ₹1,020-1,050.

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Financial Performance

	(₹mn)					
Particulars	FY18	FY19	FY20	1HFY21	1HFY20	YoY (%)
Revenue	67,703	79,856	88,300	30,903	41,933	(26.3)
Wires and Cables	62,423	69,295	75,192	25,343	34,916	(27.4)
% of Revenue	92.2	86.8	85.2	82.0	83.3	
FMEG	4,853	6,433	8,536	3,818	4,357	(12.4)
% of Revenue	7.2	8.1	9.7	12.4	10.4	
EBITDA	7,289	9,528	11,350	3,685	4,939	(25.4)
EBITDA Margin (%)	10.8	11.9	12.9	11.9		
Net Profit	3,586	5,003	7,656	3,271	4,369	(25.1)
EPS (₹)	24.1	33.6	51.4	22.7	22.0	
P/E (x)	39.2	28.1	18.4			
EV/EBITDA (x)	1.1	9.5	9.5			
P/BV (x)	5.7	3.2	2.8			
RoE (%)	16.5	19.3	22.9			
RoCE (%)	15.0	20.0	23.3			

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Disclosure of Interest Statement Polycab India Ltd. as on October 28th, 2020

Name of the Security	Polycab India Ltd.
Name of the analyst	Jayakanth Kasthuri
Analysts' ownership of any stock related to the information contained	NIL
Financial Interest	
Analyst :	No
Analyst's Relative : Yes / No	No
Analyst's Associate/Firm : Yes/No	No
Conflict of Interest	No
Receipt of Compensation	No
Way2Wealth ownership of any stock related to the information contained	NIL
Broking relationship with company covered	NIL
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