



TM

SYSTEMATIX INSTITUTIONAL EQUITIES

Systematix

Institutional Equities

Finolex Industries

23 October 2023

RESULT UPDATE

Sector: Plastic Pipes

Rating: HOLD

CMP: Rs 200

Target Price: Rs 210

Stock Info

Sensex/Nifty	65,398/19,543
Bloomberg	FNXP IN
Equity shares (mn)	618.4
52-wk High/Low	253/133
Face value	Rs 2
M-Cap	Rs 124bn/ USD 1.5bn
3-m Avg turnover	USD 3mn

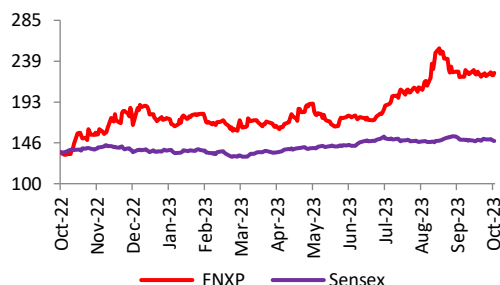
Financial Snapshot (Rs mn)

Y/E Mar	FY23	FY24E	FY25E
Net sales	43,971	50,056	56,291
EBITDA	2,925	6,779	7,792
OPM (%)	6.7	13.5	13.8
PAT (adj.)	2,507	5,313	5,975
EPS (adj.) (Rs)	4.1	8.6	9.7
PE (x)	49.3	23.3	20.7
P/B (x)	2.5	2.4	2.2
EV/EBITDA (x)	37.8	16.0	13.6
RoE (%)	5.1	10.1	10.7
RoCE (%)	6.5	12.6	13.1
Net-D/E (x)	(0.3)	(0.3)	(0.3)

Shareholding Pattern (%)

	Sep'23	Jun'23	Mar'23
Promoter	52.5	52.5	52.5
- Pledged			
FII	6.7	5.8	5.5
DII	12.2	11.9	12.6
Others	28.7	29.8	29.4

Stock Performance (1-year)



Low Pipes volumes, overall weak results in PVC-resin hurt 2Q

Finolex Industries's (FNXP) large revenue/PAT miss in 2Q was driven by volume miss in Pipes (up 6% YoY vs. 25% estimated) and PVC-resin (down 31% YoY; 40% miss), and weak PVC-resin EBIT (6.8%, Rs 5.4/kg). Lower Pipes volumes were driven by channel destocking in the price sensitive agri segment in anticipation of further reduction in PVC prices. Healthy demand in non-agri segment (40% vs. 37% in 2QFY23) sustained though. Superior product mix aided to healthy Pipes EBIT (7.9% margin, Rs 10.7/kg). FNXP expects 15-20% volume growth in FY24E (1H: 18%) with Rs 10-12/kg EBIT (1H: Rs 12.5; aims Rs 14 in few years with rise in non-agri mix towards 50% from 30-35% currently). PVC-resin volume/revenue in 2Q fell 31%/38% YoY (~40% miss) mainly due to raw materials supply disruption from Middle East. The current low spreads (PVC-EDC: USD 450/t; PVC-VCM: USD 95/t) suggest weak margins in 2H. We cut earnings estimates by 4% each for FY24E and FY25E mainly on lower than expected margins in PVC-resin segment. We now estimate 13%/63%/54% CAGR in FNXP's revenue/EBITDA/PAT over FY23-25E (FY18-23: 10%/-10%/-4% CAGR), as volume growth and margins in pipes segment likely normalise. Given its low RoCE profile (~13% in FY25E) and ~23x FY25E P/E, we maintain HOLD rating on the stock, with a revised target price of Rs 210 (earlier Rs 214), based on ~22x FY25E P/E (26x/15x FY25E P/E for pipes/PVC-resin). High volatility in PVC resin margins could continue to suppress FNXP's valuations vs. peers. Higher-than-estimated margin would be a key upside risk to our call. ([Concall KTAs](#))

2Q - large miss in revenue/PAT: Consolidated revenue declined 6% YoY (24% miss) driven by large volume miss in Pipes (up 6% YoY) and PVC-resin (down 31% YoY). While gross margin expanded 609bps QoQ due to superior product mix towards non-agri segment, lower volumes restricted EBITDA margin to 11.7% (down 127bps QoQ). Richer mix also drove Pipes EBIT (7.9%, Rs 10.7/kg); it came weak for PVC-resin (6.8%, Rs 5.4/kg). Management is yet to decide on the usage plan for its Rs 15bn cash balance.

Pipes & Fittings - missed estimates on lower volumes in non-agri segment; healthy industry outlook intact: Volume/revenue in 2Q were up by a low 6%/7% YoY (10-15% miss), driven by channel destocking in the price sensitive agri segment in anticipation of further reduction in PVC prices. Healthy demand in non-agri segment (40% vs. 37% in 2QFY23) sustained though. Superior product mix aided to healthy EBIT (7.9% margin, Rs 10.7/kg). Marginal Inventory gain aided as well. Management expects 15-20% volume growth in FY24E (1H: 18%) with Rs 10-12/kg EBIT (1H: Rs 12.5; aims Rs 14 in few years with rise in non-agri mix towards 50% from 30-35% currently). Likely removal of anti-dumping duty on CPVC resin will help in reducing product prices and boost volumes.

PVC-resin: large volume miss in 2Q; EBIT margin remains weak and volatile: 2Q volume/revenue fell 31%/38% YoY (~40% miss) mainly due to raw materials supply disruption from Middle-East. At USD 571/t PVC-EDC and USD 157/t PVC-VCM spreads, the segment EBIT margin stood low at 6.8%. The current low spreads (USD 450/t and USD 95/t, respectively) suggest weak margins in 2H. PVC-resin is a commodity business with no pricing power, hence the volatility in margins.

Financial outlook and View: We cut earnings estimates by 4% each for FY24E and FY25E mainly on lower than expected margins in PVC-resin segment. We now estimate 13%/63%/54% CAGR in FNXP's revenue/EBITDA/PAT over FY23-25E (FY18-23: 10%/-10%/-4% CAGR), as volume growth and margins in pipes segment likely normalise. Given its low RoCE profile (~13% in FY25E) and ~23x FY25E P/E, we maintain **HOLD** rating on the stock, with a revised target price of Rs 210.

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Investors are advised to refer disclosures made at the end of the research report.

Earnings conference call KTAs (2QFY24)

Business dynamics & Outlook

- Low 2Q volumes in agri segment was mainly due to channel keeping low inventory towards quarter end in anticipation of price fall
- Healthy demand seen in non-agri pipes segment
- PVC resin volumes were impacted due to raw material supply issues from Middle-East; company is in the process of sorting the same out soon
- Marginal inventory gains were registered in 2Q
- **Pipes volume growth of 15-20% is likely in FY24E**
- **Pipes EBIT:** currently Rs 10-12/kg; likely to expand to Rs 14/kg in few years with rise in non-agri mix
- **PVC-resin margin:** current low spreads suggest weak margins in 2H
- Fittings capacity at 48kt, with 12kt in-house capacity; rest is outsourced but on exclusive terms

Spreads – key monitorable for PVC-resin spread

- PVC-EDC spread (\$ /t): **571 in 2Q; 450 currently**
- PVC-VCM spread (\$ /t): **157 in 2Q; 95 currently**
- 2Q (\$ /t): PVC 847, EDC 276, VCM 690
- Current prices (\$ /t): PVC 770, EDC 320, VCM 675

Product mix

- 2Q non-agri mix: 40% vs. 37% in 2QFY23
- 1H non-agri mix: 32% vs. 30%
- **Aims 50% mix from each of these segments** in few years

CPVC resin: ADD on imports from Korea to expire soon

- Removal of ADD will help in reducing prices and boost volumes for pipe manufacturer

Exhibit 1: FNXP – quarterly performance (Consolidated)

(Rs mn)	2QFY23	3QFY23	4QFY23	1QFY24	2QFY24	YoY (%)	QoQ (%)	1HFY24	1HFY23	YoY (%)
Total Income	9,411	11,248	11,411	11,792	8,832	(6)	(25)	20,623	21,309	(3)
Raw material costs	8,529	7,602	6,592	7,802	5,306	(38)	(32)	13,108	16,528	(21)
Employee costs	423	484	480	519	503	19	(3)	1,022	934	9
Other expenses	1,886	2,243	2,165	1,946	1,993	6	2	3,939	4,016	(2)
EBITDA	(1,427)	919	2,174	1,525	1,030	na	(32)	2,555	(168)	na
Depreciation	216	225	238	344	274	27	(20)	618	429	44
Finance costs	43	51	65	90	125	189	38	215	156	37
Other income	388	278	292	403	614	58	52	1,016	639	59
PBT	(1,297)	921	2,164	1,493	1,245	na	(17)	2,738	(114)	na
Tax	(350)	254	633	416	354	na	(15)	770	(173)	na
PAT (after JV/ Assoc.)	(954)	795	1,665	1,153	980	na	(15)	2,133	38	5,469
EPS (Rs)	(1.5)	1.3	2.7	1.9	1.6	na	(15)	3.4	0.1	5,469
As % Total Income						YoY (bps)	QoQ (bps)			YoY (bps)
Gross margin	9.4	32.4	42.2	33.8	39.9	3,055	609	36.4	22.4	1,400
Employee costs	4.5	4.3	4.2	4.4	5.7	120	129	5.0	4.4	57
Other expenses	20.0	19.9	19.0	16.5	22.6	253	607	19.1	18.8	26
EBITDA margin	(15.2)	8.2	19.1	12.9	11.7	2,682	(127)	12.4	(0.8)	1,317
Depreciation	2.3	2.0	2.1	2.9	3.1	81	18	3.0	2.0	98
Finance costs	0.5	0.5	0.6	0.8	1.4	95	65	1.0	0.7	31
Other income	4.1	2.5	2.6	3.4	6.9	282	353	4.9	3.0	193
PBT margin	(13.8)	8.2	19.0	12.7	14.1	2,788	143			
Effective tax rate	27.0	27.6	29.3	27.8	28.4	146	60	28.1	151.4	(12,334)
PAT (after JV/ Assoc.)	(10.1)	7.1	14.6	9.8	11.1	2,123	131	10.3	0.2	1,016
Pipes & Fittings						YoY (%)	QoQ (%)			YoY (%)
Volume (t)	59,219	90,396	81,452	92,181	62,914	6	(32)	1,55,095	1,31,179	18
<i>Realisation (Rs/kg)</i>	<i>135</i>	<i>119</i>	<i>135</i>	<i>125</i>	<i>136</i>	<i>1</i>	<i>9</i>	<i>130</i>	<i>147</i>	<i>(12)</i>
Revenue (Rs mn)	8,017	10,772	11,021	11,542	8,572	7	(26)	20,114	19,337	4
EBIT (Rs mn)	(477)	689	903	1,264	676	(242)	(47)	1,940	(51)	(3,920)
<i>EBIT margin (%)</i>	<i>(5.9)</i>	<i>6.4</i>	<i>8.2</i>	<i>11.0</i>	<i>7.9</i>			<i>9.6</i>	<i>(0.3)</i>	
EBIT/kg (Rs)	(8)	8	11	14	11	(234)	(22)	13	(0)	(3,350)
PVC Resin						YoY (%)	QoQ (%)			YoY (%)
Volume (t)	54,063	64,697	58,132	46,074	37,516	(31)	(19)	83,590	1,16,810	(28)
<i>Realisation (Rs/kg)</i>	<i>89</i>	<i>78</i>	<i>86</i>	<i>78</i>	<i>79</i>	<i>(11)</i>	<i>2</i>	<i>79</i>	<i>108</i>	<i>(27)</i>
Revenue (Rs mn)	4,811	5,041	5,013	3,594	2,979	(38)	(17)	6,573	12,657	(48)
EBIT (Rs mn)	(1,107)	124	1,173	31	204	(118)	554	235	(378)	(162)
<i>EBIT margin (%)</i>	<i>(23.0)</i>	<i>2.5</i>	<i>23.4</i>	<i>0.9</i>	<i>6.8</i>			<i>3.6</i>	<i>(3.0)</i>	
EBIT/kg (Rs)	(20)	2	20	1	5	(127)	703	3	(3)	(187)
<i>Un-allocated exp (as % rev)</i>	<i>(3.5)</i>	<i>(1.4)</i>	<i>(1.3)</i>	<i>(2.4)</i>	<i>(5.5)</i>			<i>(3.8)</i>	<i>(2.2)</i>	
EBIT mix (%)										
Pipes & Fittings	30	85	44	98	77			89	12	
PVC Resin	70	15	56	2	23			11	88	

Source: Company, Systematix Institutional Research

Exhibit 2: EBIT mix – quarterly trend

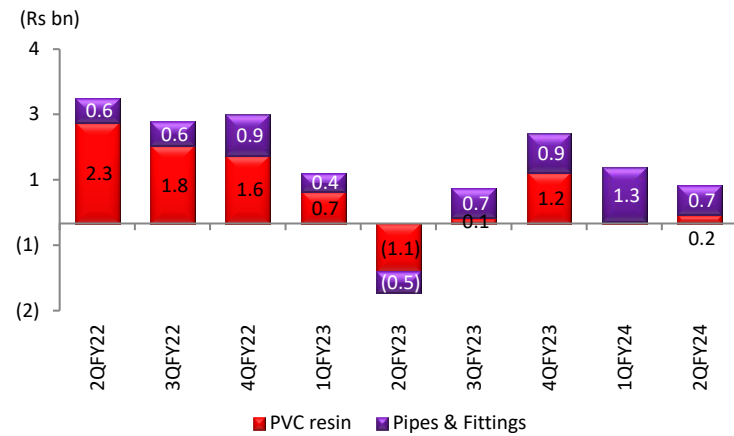


Exhibit 3: Volumes – quarterly trend

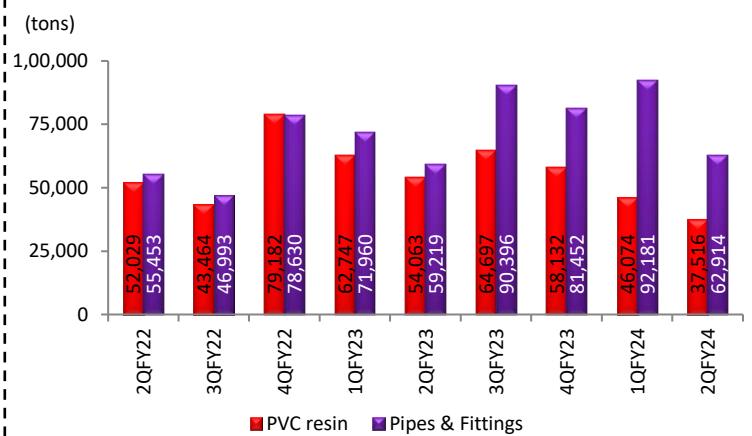


Exhibit 4: PVC resin – revenue, EBIT quarterly trend (%)

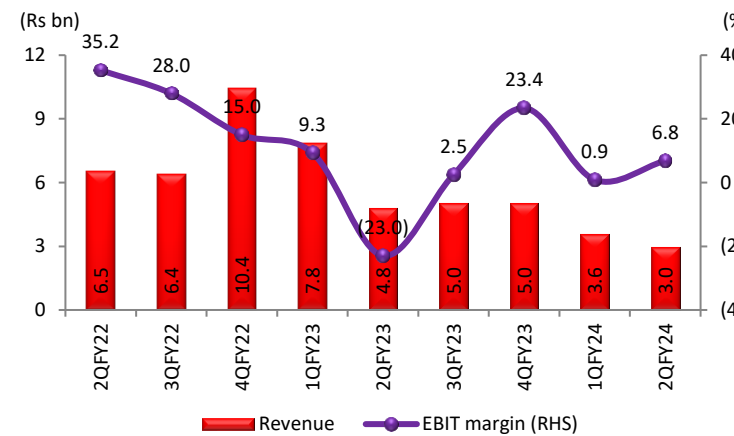


Exhibit 5: Pipes & fittings – revenue, EBIT quarterly trend (%)

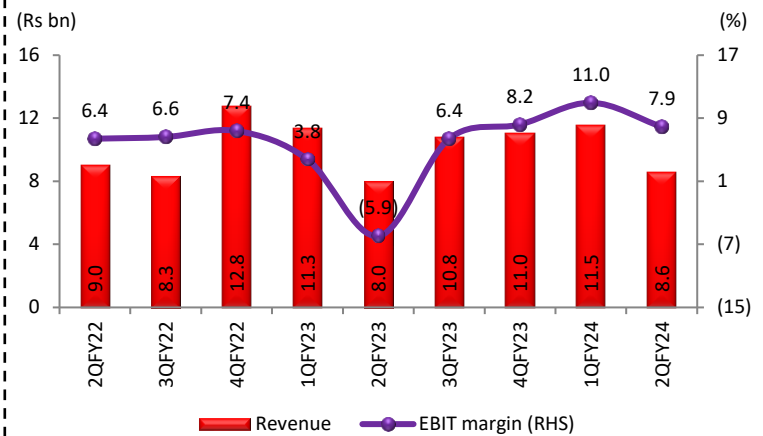
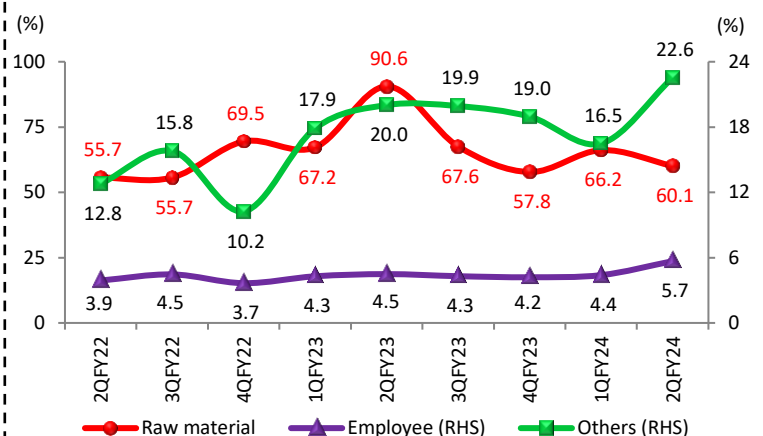


Exhibit 6: Income growth – quarterly trend



Exhibit 7: Expenses as a percentage of income – quarterly trend



Source: Company, Systematix Institutional Research

Exhibit 8: EBITDA and margin – quarterly trend

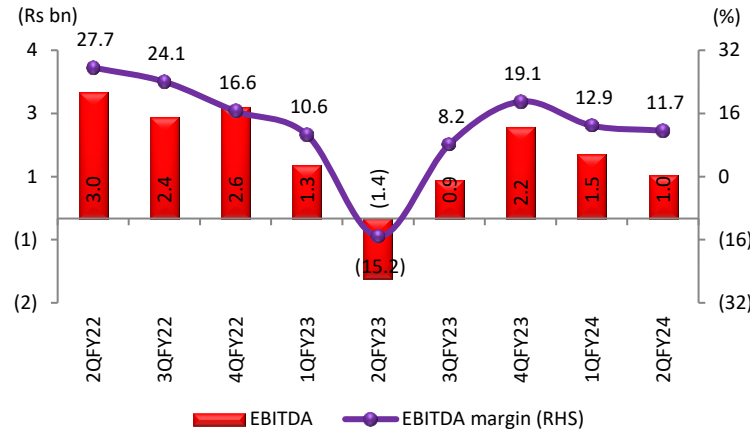


Exhibit 9: Earnings – quarterly trend

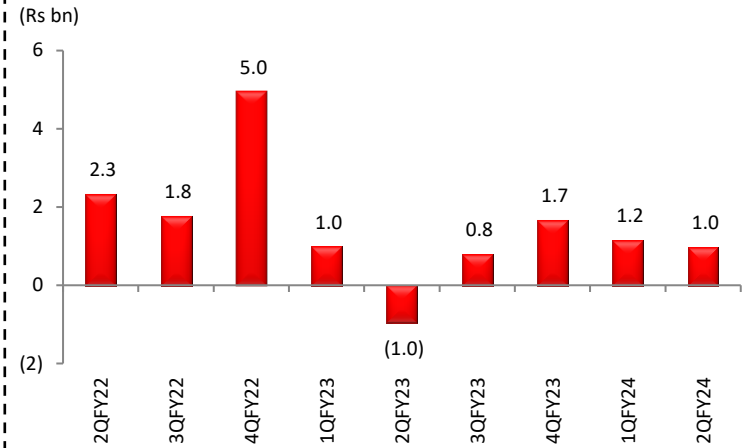


Exhibit 10: Income – Annual growth trend

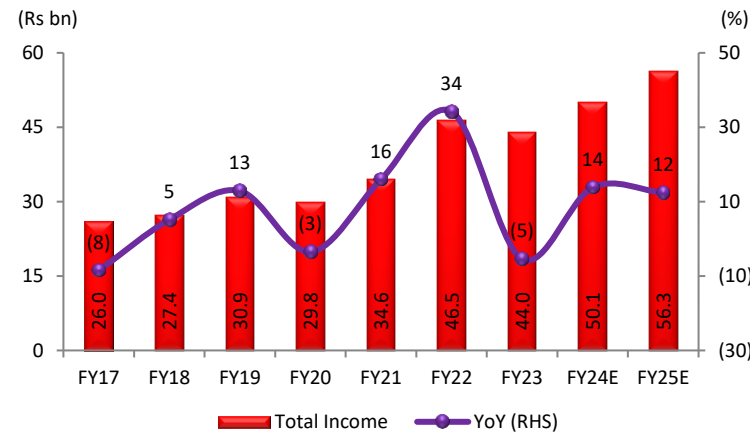


Exhibit 11: EBITDA, PAT – Annual growth, margin trends

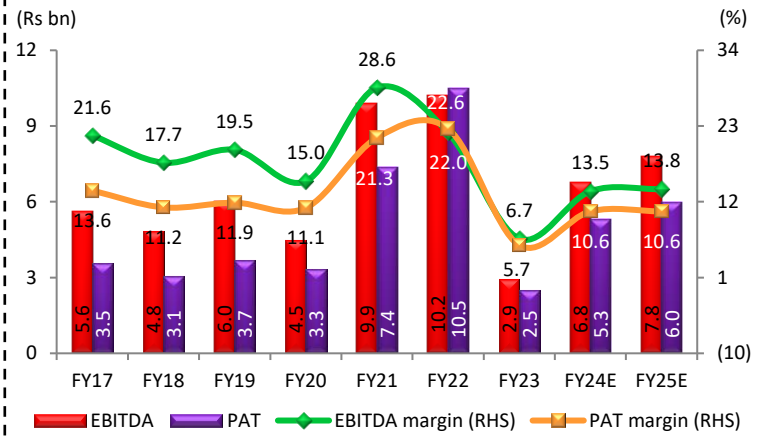


Exhibit 12: EBIT mix – Annual trend

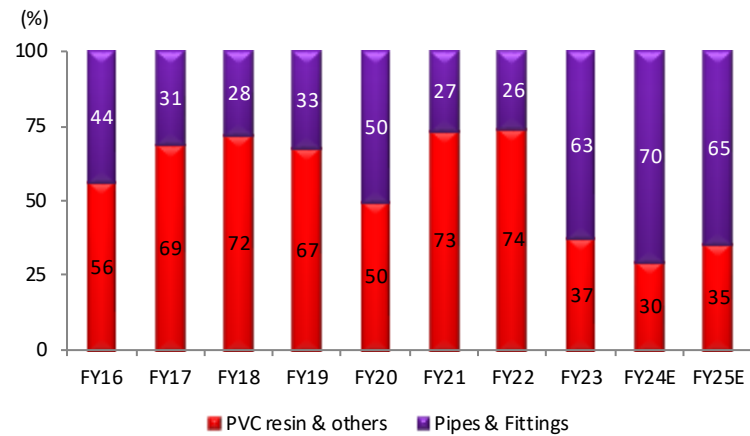
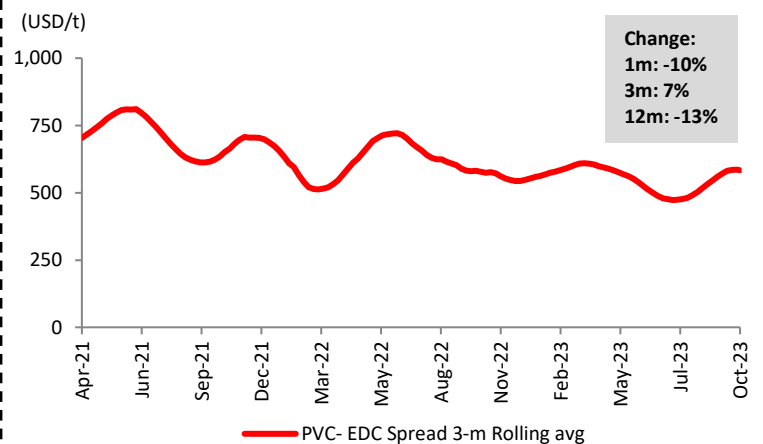


Exhibit 13: PVC/EDC spread



Source: Company

Source: Company, Systematix Institutional Research

Valuation and View

We like FNXP for its leadership in agri pipes, healthy FCF, greater focus on portfolio (CPVC/SWR pipes) and network (north, east) expansion. Much of its sales in the agri-pipes segment is based on cash and carry (unlike peers), which reflects its strong market position and brand equity. However, we remain concerned on volatility in PVC resin margins. Additionally, high cash investments (low yield) have suppressed its return ratios.

Significantly high realisations and PVC EBIT margin (~31%) rendered FNXP's FY21 and FY22 PAT base high. We cut earnings estimates by 4% each for FY24E and FY25E mainly on lower than expected margins in PVC-resin segment. We now estimate 13%/63%/54% CAGR in FNXP's revenue/EBITDA/PAT over FY23-25E (FY18-23: 10%/-10%/-4% CAGR), as volume growth and margins in pipes segment likely normalise.

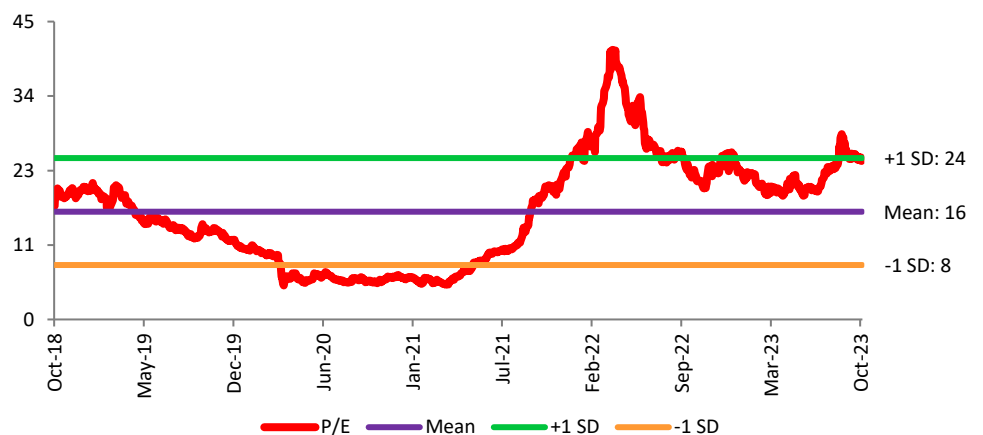
Given its low RoCE profile (~13% in FY25E) and ~23x FY25E P/E, we maintain **HOLD** rating on the stock, with a revised target price of Rs 210 (earlier Rs 214), based on ~22x FY25E P/E (26x/15x FY25E P/E for pipes/PVC-resin). High volatility in PVC resin margins could continue to suppress FNXP's valuations vs. peers. Higher-than-estimated margin would be a key upside risk to our call.

Exhibit 14: Change in estimates

(Rs mn)	Old estimates		New estimates		% Variance	
	FY24	FY25	FY24	FY25	FY24	FY25
Total Income	51,590	57,034	50,056	56,291	(3)	(1)
EBITDA	7,113	8,035	6,779	7,792	(5)	(3)
EBITDA margin (%)	13.8	14.1	13.5	13.8		
PAT	5,537	6,251	5,313	5,975	(4)	(4)
EPS	9.0	10.1	8.6	9.7	(4)	(4)

Source: Systematix Institutional Research

Exhibit 15: P/E band – 1-year-forward and standard deviation



Source: BSE, Systematix Institutional Research

Risks

- Higher-than-estimated PVC margin is a key upside risk to our earnings estimates.

FINANCIALS (CONSOLIDATED)

Profit & Loss Statement

YE: Mar (Rs mn)	FY21	FY22	FY23	FY24E	FY25E
Net revenues (Rs mn)	34,623	46,473	43,971	50,056	56,291
Growth (%)	16	34	(5)	14	12
RM costs	19,288	28,491	30,721	32,533	36,417
Gross Margin (%)	44.3	38.7	30.1	35.0	35.3
SG&A	5,442	7,745	10,324	10,744	12,082
EBITDA	9,893	10,237	2,925	6,779	7,792
EBITDA margins (%)	28.6	22.0	6.7	13.5	13.8
- Depreciation	777	834	892	1,180	1,245
Other income	716	822	1,209	1,610	1,346
Interest Exp	73	141	272	415	220
PBT	9,759	13,845	2,970	6,794	7,672
Effective tax rate (%)	26.1	24.0	23.8	26.6	26.8
+ Associates/(Minorities)	-	-	-	-	-
Net Income	7,378	10,513	2,507	5,313	5,975
Adjusted income	7,378	7,505	2,507	5,313	5,975
WANS	621	621	618	618	618
FDEPS (Rs /share)	11.9	23.1	4.1	8.6	9.7
FDEPS growth (%)	122	93	(82)	112	12

Balance Sheet

YE: Mar (Rs mn)	FY21	FY22	FY23	FY24E	FY25E
Share capital	1,241	1,241	1,237	1,237	1,237
Net worth	31,390	39,278	49,031	52,488	55,990
Total debt	2,039	2,780	5,264	4,774	4,284
Minority interest	-	-	-	-	-
DT Liability/(Asset)	1,395	1,360	1,493	1,582	1,672
Capital Employed	34,823	43,419	55,788	58,845	61,946
Net tangible assets	10,013	9,923	10,544	10,864	11,118
Net Intangible assets	11	9	8	8	8
Goodwill	-	-	-	-	-
CWIP	82	95	438	438	438
Investments (Strategic)	-	-	-	-	-
Investments (Financial)	16,792	27,177	39,468	40,468	42,468
Current Assets	12,679	15,440	11,787	14,271	15,793
Cash	3,363	810	606	1,329	1,313
Current Liabilities	8,116	10,035	7,063	8,533	9,193
Working capital	4,563	5,405	4,723	5,738	6,600
Capital Deployed	34,823	43,419	55,788	58,845	61,946
Contingent Liabilities	1,011	767	765	-	-

Cash Flow

YE: Mar (Rs mn)	FY21	FY22	FY23	FY24E	FY25E
EBIT (before other income)	9,227	9,498	2,000	5,951	6,916
+ Non-cash items	777	834	892	1,180	1,245
OCF before WC changes	10,004	10,332	2,892	7,132	8,162
- Incr./ (decr.) in WC	(1,524)	756	(804)	1,035	882
Others including taxes	2,118	3,356	679	1,724	1,958
Operating cash-flow	9,410	6,220	3,017	4,373	5,322
- Capex	649	(2,962)	1,677	1,500	1,500
Free cash-flow	8,761	9,182	1,340	2,873	3,822
Acquisitions	-	-	-	-	-
- Dividend	42	2,482	2,482	1,855	2,473
+ Equity raised	-	-	-	-	-
+ Debt raised	(784)	728	2,445	(490)	(490)
- Fin Investments	8,376	7,910	1,620	1,000	2,000
- Misc. Items (CFI + CFF)	(182)	(403)	(167)	(1,195)	(1,126)
Net cash-flow	(259)	(78)	(150)	723	(16)

Ratios @ Rs 200

YE: Mar	FY21	FY22	FY23	FY24E	FY25E
P/E (x)	16.8	8.7	49.3	23.3	20.7
EV/EBITDA (x)	11.9	10.8	37.8	16.0	13.6
EV/sales (x)	3.4	2.4	2.5	2.2	1.9
P/B (x)	3.9	3.1	2.5	2.4	2.2
RoE (%)	23.5	26.8	5.1	10.1	10.7
RoCE (%)	33.4	26.1	6.5	12.6	13.1
ROIC	39.3	36.5	9.0	17.2	18.2
DPS (Rs per share)	4.0	4.0	1.5	3.0	4.0
Dividend yield (%)	2.0	2.0	0.8	1.5	2.0
Dividend payout (%)	34	24	37	35	41
Net debt/equity (x)	(0.2)	(0.3)	(0.3)	(0.3)	(0.3)
Receivables (days)	16	26	25	25	25
Inventory (days)	97	80	56	65	65
Payables (days)	46	36	24	35	35
CFO:PAT (%)	128	59	120	82	89

Source: Company, Systematix Institutional Research

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