

V-Guard Industries Ltd (VGRD IN)

Revenue above expectations

INDIA | MIDCAP - ELECTRICALS | Quarterly Update

22 May 2017

Top takeaways from Q4FY17

- Higher sales volumes of pumps, stabilizer, fans, and switchgears resulted in a 21% revenue jump.
- Higher input cost (due to higher commodity prices) led to a fall in gross margin by 193bps yoy. Higher employee cost of 41% (one-time provision of Rs 35mn) led to a 284bps yoy fall in OPM to 9.5%.
- Controlled working-capital cycle resulted in lower interest outgo and higher other income.

Key highlights: Strong summer

VGRD gained from better penetration in non-south-Indian markets (non-south revenue up 31% yoy and south market up 17% yoy). Investments in infrastructure and higher employee cost hit margins.

Management comments/concall/analyst-meet takeaways

- ✓ Strong summer led to strong 32% growth in fans, 17% in pumps, 16% in stabilisers, and 11% in switchgears.
- ⇔ To offset a sharp increase in commodity prices in 4QFY17, the company increased prices. VGRD's gross margin improved by 1.5% in April 2017 vs. March 2017.
- ⇔ GST @ 28% on all products vs. expectation of 18%. Expect a price increase of 6% excluding cables, in which it will be about 9% to compensate for the higher tax rate. Management expects a slow shift to organised players from unorganized ones.
- ✓ Maintained revenue-growth guidance of 15% and margin guidance of 10-11% for FY18. Expects this run-rate to continue for the next two years.
- ✓ Has total 30,000 touch points. Adding 4,500 in FY18, mainly in the non-south market.
- ✓ Non-south market saw robust 31% yoy growth in 4Q. VGRD continued to increase its penetration and garner market share (currently accounts for 35% of sales). This market offers significant growth potential and operational leverage.

Outlook and valuation: While the scope for gross-margin improvement is limited, we believe increased channel sweating and tight working capital management should see better absorption of fixed costs. With demand for household goods improving, VGRD increasing its penetration in the non-south market, and improving product mix, we have increased our FY18/19 earnings by 2%/3%. In recognition of its debt-free balance sheet and better cash-conversion cycle, we have revised our earnings multiple to 35x (vs. 30x earlier). Consequently, we have raised our target price to Rs 185 (vs. Rs 154 earlier, adjusted).

Given the sharp run up, we maintain our Neutral rating. At this multiple, VGRD has little room to negotiate any disruption in its cash flows and earnings as a sizeable portion of its sales consist of seasonal products whose off-take is influenced by climatic conditions.

Neutral (Maintain)

CMP RS 194

TARGET Rs 185 (-5%)

COMPANY DATA

O/S SHARES (MN) :	425
MARKET CAP (RSBN) :	92
MARKET CAP (USDBN) :	1.4
52 - WK HI/LO (RS) :	221 / 84
LIQUIDITY 3M (USDMN) :	2.7
PAR VALUE (RS) :	10

SHARE HOLDING PATTERN, %

	Mar 17	Dec 16	Sep 16
PROMOTERS :	65.2	65.4	65.5
FII / NRI :	12.5	13.0	12.9
FI / MF :	10.1	10.6	11.6
NON PRO :	2.8	2.5	2.3
PUBLIC & OTHERS :	9.4	8.6	7.8

Key Financials

Rs mn	FY17E	FY18E	FY19E
Net Sales	21,506	24,609	28,447
EBIDTA	2,151	2,549	3,091
Net Profit	1,518	1,824	2,247
EPS, Rs	3.6	4.3	5.3
PER, x	54.3	45.2	36.7
EV/EBIDTA, x	35.6	30.2	24.9
P/BV, x	12.9	10.6	8.6
ROE, %	27.4	25.8	25.9

CHANGE IN ESTIMATES

Rs mn	Revised Est.		% Revision	
	FY18E	FY19E	FY18E	FY19E
Revenue	24,609	28,447	3%	4%
EBITDA	2,549	3,091	1%	3%
PAT	1,824	2,247	2%	3%

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(Rs mn)	Q4FY17	Q4FY16	yoy growth %	Q3FY16	qoq growth %	vs. expectations	Comments
Sales	6,233	5,133	21.4	4,596	35.6	6.5	Higher sales of seasonal products & strong non-south market
EBITDA	594	634	(6.4)	386	53.8	-4.3	Higher RM, employee & one-time exp.
EBITDA margin	9.5	12.4	-284bps	8.4	112.7	-107.6	
Interest	5	12	(61.4)	5	-5.4		
Depreciation	42	38	9.8	42	0.0		
Other income	32	21	53.3	33	-4.0		Surplus cash generated
PBT	579	605	(4.3)	372	55.5		
Tax	160	185	(13.3)	93	73.0		
Tax rate	28	31	-290bps	25	279.6		
PAT	419	420	(0.3)	280	49.7	-3.0	

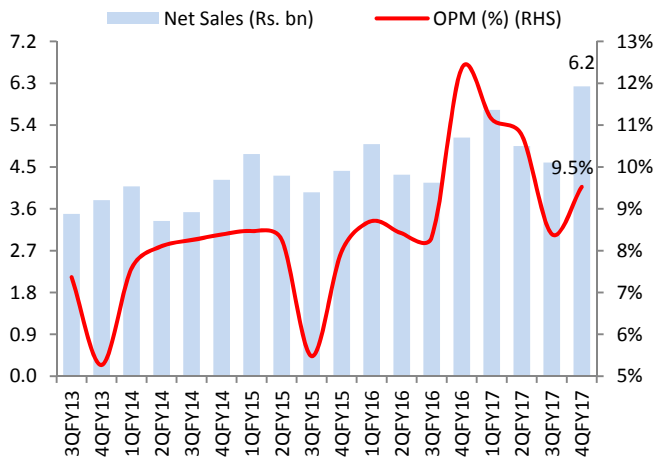
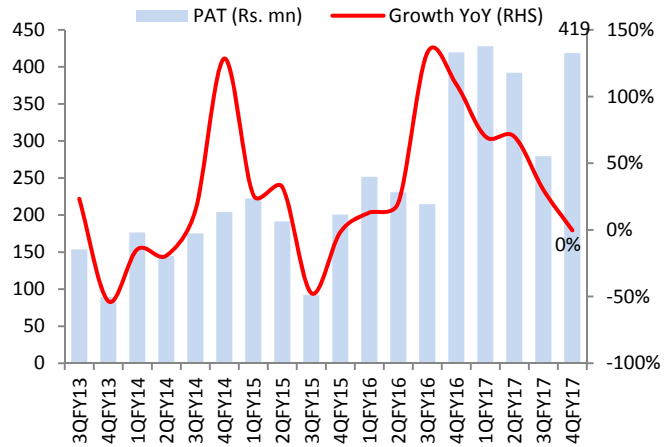
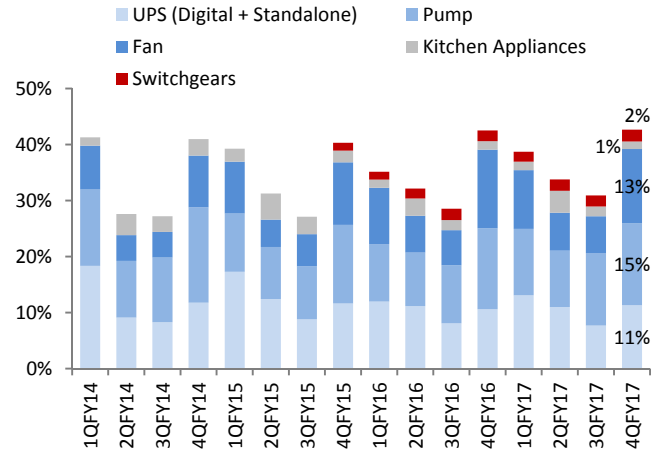
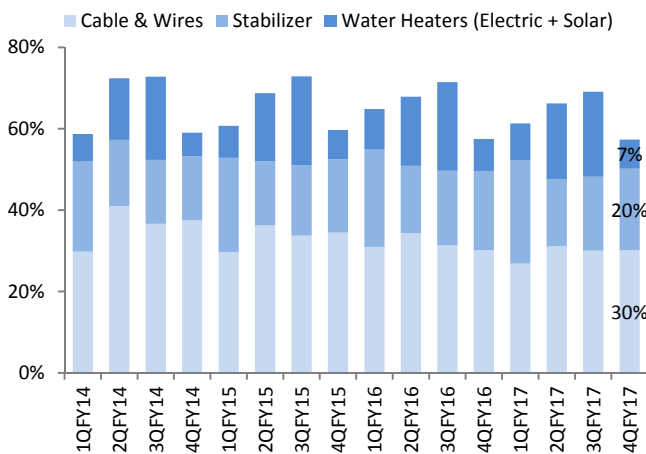
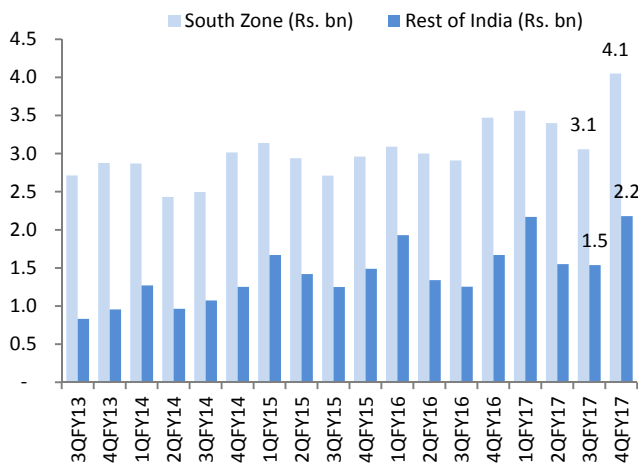
Segment-wise performance for 4QFY17

V-guard Product Portfolio:	Total Market Share (Rs bn)	Organised (%)	Unorganised (%)	VGRD - FY17 Rev. (Rs mn)	VGRD - FY16 Rev. (Rs mn)	YoY Growth (%)	Share (%)
Stabilizer	14	40%	60%	4,362	3,691	18.2%	20.3%
UPS (Digital + Standalone)	95	85%	15%	2,351	1,936	21.4%	10.9%
Pump	24	50%	50%	2,685	2,100	27.9%	12.5%
Cable & Wires	172	65%	35%	6,335	5,886	7.6%	29.5%
Water Heaters (Electric + Solar)	22	62%	38%	2,843	2,554	11.3%	13.2%
Fan	60	75%	25%	2,060	1,767	16.6%	9.6%
Kitchen Appliances	-	-	-	445	358	24.3%	2.1%
Switchgears	50	73%	27%	425	333	28.7%	2.0%

Source: Company, PhillipCapital India Research

Other key takeaways

- ✓ Fans revenue up 32% yoy, volume growth of 14%.
- ↔ Volatile copper prices resulted in 8% volume growth in wires and cables. Increased prices in 4Q mainly to pass on higher copper prices.
- ↔ Expect higher employee cost - 15-18% growth yoy in FY18, because ESOPs are now at market price.
- ✓ Expect price difference of VGRD products in south and non-south market to narrow over 2-3 years (current products in non-south market are ~4% lower than south market price).
- ✓ To increase its portfolio in the non-south market, VGRD will add products such as switchgears and kitchen appliances in FY18.
- ✓ Tight control resulted in creditor days improving by 12 to touch 54, helping the working capital cycle improve to 68 days vs. 70 yoy. Management sees more improvement with more channel financing and some improvement in debtors days (tight control on collection).
- ✓ To increase pan-India visibility, VGRD spent Rs 950mn FY17 (4.4% of sales) on advertising and promotion.
- ✓ Second phase of expansion of HW cable plant at Coimbatore is completed. Commercial production starting in May 2017. Capacity will increase to 870,000 coils /month. The total cost of the project is Rs 120mn.
- ✓ In 4Q, it acquired 74% equity stake in Guts Electromech Ltd (manufactures switchgears). Management expects revenue of Rs 1.2bn in its switchgears segment with full utilisation of Guts' plant and also sees margins of this segment improving.
- ✓ With the Sikkim facility commissioning, it expects its own manufacturing share increasing to 60% vs. 40% currently.
- ✓ In the quarter, VGRD launched smart-series inverters which can be configured to run iron box and other heavy appliances.

Net sales and OPM trend

Net profits trend

Product-wise revenue break-up (% of sales)

Geographical revenue breakup – Non south market at 35%

VGRD - Key Ratios

Key Ratios	4QFY17	3QFY17	4QFY16
Working Capital Days:	68	62	70
Debtors (days)	54	41	55
Inventory (days)	68	69	57
Creditors (days)	54	48	42
ROE (%)	24%	26%	24%
ROCE (%)	31%	34%	33%
Gross debt / Equity (x)	0.01	0.01	0.02

Source: Company, PhillipCapital India Research

Financials

Income Statement

Y/E Mar, Rs mn	FY16	FY17	FY18E	FY19E
Net sales	18,623	21,506	24,609	28,447
Growth, %	6.7%	15.5%	14.4%	15.6%
Raw Material expenses	13,208	14,780	16,753	19,308
Operating expenses	2,527	3,201	3,685	4,198
Employee expenses	1,108	1,375	1,623	1,850
EBITDA (Core)	1,780	2,151	2,549	3,091
Growth, %	33.8%	20.8%	18.5%	21.3%
Margin, %	10%	10%	10%	11%
Depreciation	154	162	180	195
EBIT	1,626	1,988	2,369	2,896
Growth, %	38.3%	22.3%	19.2%	22.2%
Margin, %	9%	9%	10%	10%
Interest paid	89	21	15	15
Other Non-Operating Income	72	135	145	155
Pre-tax profit	1,609	2,102	2,499	3,036
Tax provided	493	584	675	789
Profit after tax	1,117	1,518	1,824	2,247
Net Profit	1,117	1,518	1,824	2,247
Growth, %	57.9%	36.0%	20.2%	23.1%
Margin, %	6.0%	7.1%	7.4%	7.9%
Net Profit (adjusted)	1,117	1,518	1,824	2,247
No. of Eq. Sh O/S (m nos)	425	425	425	425

Balance Sheet

Y/E Mar, Rs mn	FY16	FY17	FY18E	FY19E
Cash & bank	76	157	116	540
Debtors	2,792	3,193	3,076	3,635
Inventory	2,047	2,736	3,983	4,578
Loans & advances	445	642	742	892
Total current assets	5,360	6,728	7,917	9,646
Gross fixed assets	2,526	2,762	3,172	3,592
Less: Depreciation	916	1,078	1,258	1,453
Add: Capital WIP	1	104	50	50
Net fixed assets	1,611	1,788	1,964	2,190
Total assets	7,165	9,407	10,923	13,078
Current liabilities	1,881	2,602	2,696	3,101
Provisions	398	320	320	320
Total current liabilities	2,279	2,922	3,016	3,421
Debt	104	60	60	60
Deferred Tax Liability	75	54	54	54
Total liabilities	2,457	3,036	3,130	3,535
Paid-up capital	301	425	425	425
Reserves & surplus	4,407	5,947	7,368	9,119
Shareholders' equity	4,708	6,372	7,793	9,544
Total equity & liabilities	7,165	9,407	10,923	13,078

Source: Company, PhillipCapital India Research Estimates

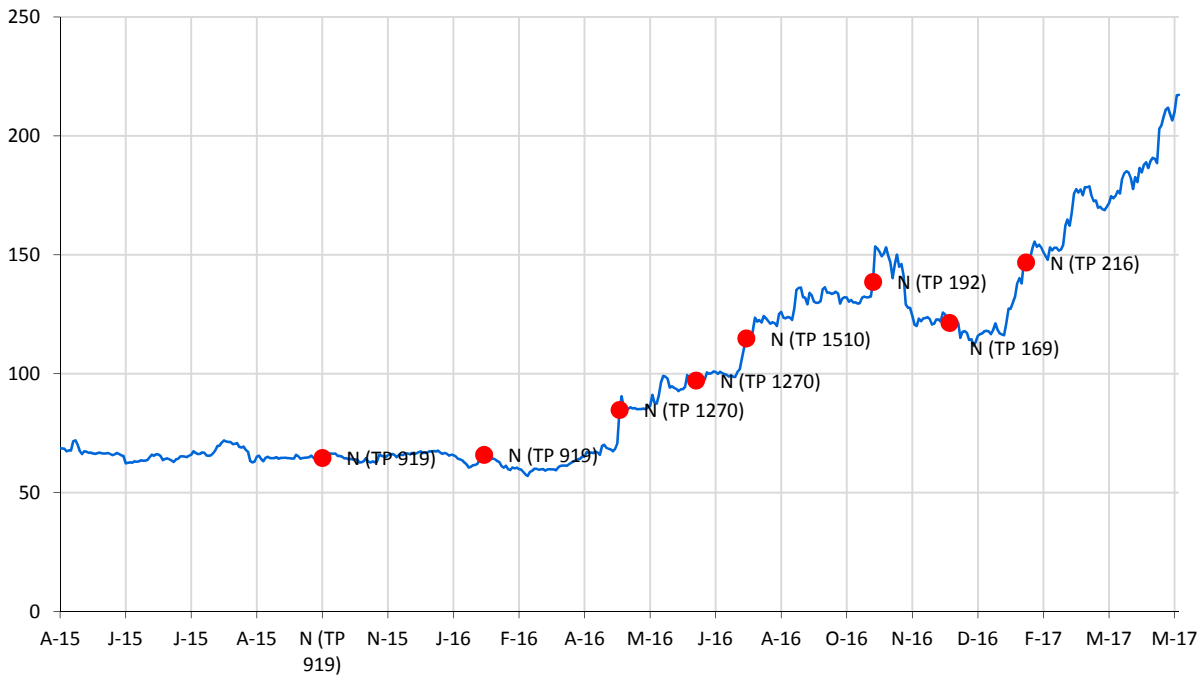
Cash Flow

Y/E Mar, Rs mn	FY16	FY17E	FY18E	FY19E
Pre-tax profit	1,609	2,102	2,499	3,036
Depreciation	154	162	180	195
Chg in working capital	-116	-644	-1,136	-901
Total tax paid	-498	-584	-675	-789
Other operating activities	163	-134	-130	-140
Cash flow from operating activ.	1,311	903	738	1,400
Capital expenditure	-140	-339	-356	-420
Chg in investments	-194	-697	-150	-200
Other investing activities	17	135	145	155
Cash flow from investing activ.	-316	-902	-361	-465
Free cash flow	995	1	377	935
Equity raised/(repaid)	31	481	0	0
Debt raised/(repaid)	-574	-44	0	0
Dividend (incl. tax)	-325	-335	-403	-496
Other financing activities	-73	-21	-15	-15
Cash flow from financing activi.	-941	80	-418	-511
Net chg in cash	54	81	-41	424

Valuation Ratios

	FY16	FY17	FY18E	FY19E
Per Share data				
Dil. EPS (INR)	2.6	3.6	4.3	5.3
Growth, %	57.9	36.0	20.2	23.1
Book NAV/ FD share (INR)	11.1	15.0	18.4	22.5
CEPS (INR)	4.2	4.0	4.7	5.7
CFPS (INR)	3.1	2.1	1.7	3.3
DPS (INR)	0.7	0.7	0.8	1.0
Return ratios				
Return on assets (%)	15.6	16.1	16.7	17.2
Return on equity (%)	26.3	27.4	25.8	25.9
Return on capital employed (%)	36.0	37.3	34.9	34.7
Turnover ratios				
Sales/Total assets (x)	3.8	3.3	3.1	2.9
Sales/Net FA (x)	11.6	12.8	12.9	13.3
Working capital/Sales (x)	0.2	0.2	0.2	0.2
Fixed capital/Sales (x)	0.1	0.1	0.1	0.1
Receivable days	54.0	43.0	45.0	46.0
Inventory days	43.8	63.0	65.0	65.0
Loans, Adv (days)	8.6	10.7	10.9	11.3
Payable days	40.2	46.0	44.0	44.0
Working capital days	66.1	70.7	76.9	78.3
Liquidity ratios				
Current ratio (x)	2.4	2.3	2.6	2.8
Quick ratio (x)	1.5	1.4	1.3	1.5
Interest cover (x)	15.2	81.0	135.4	164.8
Dividend cover (x)	5.3	5.3	5.3	5.3
Total debt/Equity (%)	0.0	0.0	0.0	0.0
Net debt/Equity (%)	0.0	(0.0)	(0.0)	(0.1)
Valuation				
PER (x)	73.8	54.3	45.2	36.7
PEG (x) - y-o-y growth	1.3	1.5	2.2	1.6
Price/Book (x)	17.5	12.9	10.6	8.6
Yield (%)	0.4	0.4	0.4	0.5
EV/Net sales (x)	3.1	3.8	3.3	2.8
EV/EBITDA (x)	31.4	35.6	30.2	24.9
EV/EBIT (x)	34.3	38.3	32.3	26.4

Stock Price, Price Target and Rating History



Rating Methodology

We rate stock on absolute return basis. Our target price for the stocks has an investment horizon of one year.

Rating	Criteria	Definition
BUY	$\geq +15\%$	Target price is equal to or more than 15% of current market price
NEUTRAL	$-15\% > \text{to} < +15\%$	Target price is less than +15% but more than -15%
SELL	$\leq -15\%$	Target price is less than or equal to -15%.

Management

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Nitesh Sharma, CFA (9122) 6246 4126	Shyamal Dhruve (9122) 6246 4110	Mehul Sheth (9122) 6246 4123
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Pradeep Agrawal (9122) 6246 4113		
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