

RESEARCH
INDIA STRATEGY | MONTHLY WRAP

Global headwinds plateauing

SUPREME INDUSTRIES | TARGET: Rs 2,055 | -5% | HOLD

Muted quarter but H2 revival on track

Daily macro indicators

Indicator	27-Oct	28-Oct	Chg (%)
US 10Y yield (%)	3.92	4.01	9bps
India 10Y yield (%)	7.41	7.42	1bps
USD/INR	82.50	82.47	0.0
Brent Crude (US\$/bbl)	97.0	95.8	(1.2)
Dow	32,033	32,862	2.6
Hang Seng	15,428	14,863	(3.7)
Sensex	59,757	59,960	0.3
India FII (US\$ mn)	25-Oct	27-Oct	Chg (\$ mn)
FII-D	7.0	45.9	38.9
FII-E	40.0	424.7	384.7

Source: Bank of Baroda Economics Research

SUMMARY
INDIA STRATEGY: MONTHLY WRAP

- Nifty underperformed global peers in October; banks and IT outperformed, pharma and FMCG lagged
- Earnings season modest so far as companies face margin stress; on the positive side, the global macro climate is at the trough, in our view
- Nifty valuation has inched up towards +1SD of its 5Y average; we retain our conservative investment approach

[Click here for the full report.](#)
SUPREME INDUSTRIES

- Q2 revenue grew 8% YoY led by a 9% volume uptick despite seasonal weakness
- EBITDA margin contracted 905bps YoY to 7.1% as RM-to-sales cost surged 830bps on higher inventory losses
- Volume guidance upped but margins cut on volatile PVC prices. We lower FY23 EPS 10% (FY24 unchanged); retain HOLD and TP of Rs 2,055

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Global headwinds plateauing

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Nifty underperforms in October: The Nifty 50 delivered returns of 5.4% in Oct'22, underperforming the US, EU and Japan. Sector-wise, we saw gains across banks (+6.9%), with public-sector players (+15.6%) outperforming private peers (+6.3%). The technology sector (+6.5%) mimicked a rebound on Wall Street. Pharma (+1.9%) and FMCG (-0.2%) lagged.

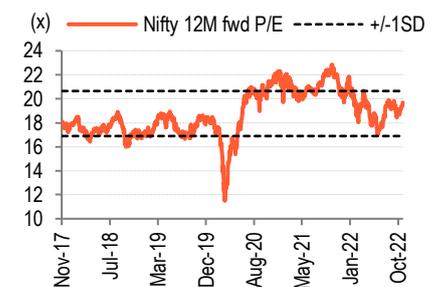
Earnings season modest so far: According to the Centre for Monitoring Indian Economy (CMIE), ~549 companies have reported an aggregate increase of 30% YoY in Q2FY23 net income so far. Expenses continue to rise faster than income, but the aggregate net profit margin has recovered to 10% (vs. 7.3% in June and 8.8% in March). Windfall tax has limited cyclical upsides for refiners, even as the consumer business was a bright spot for Reliance Industries. Most consumer durable players, however, suffered a margin crunch during the quarter.

Subtle shift in macro narrative: The US Fed has hiked interest rates by 300bps this year and the forward curve is pricing in another ~150bps hike over the next six months given persistent inflation and a strong labour market. The US bond market has had one of its worst years since 1930. Though near-term inflation expectations remain high, some surveys indicate a moderation in long-term estimates. The ~7% mortgage rate is clearly hurting the US real estate market, a key component of the inflation index. In Europe, temperature data thus far suggests a warmer winter than 2021, which could mean less energy-related fiscal stress this winter.

We expect a moderate pace of rate hikes in the US and EU going forward, which will augur well for the Indian currency and inflows, but remain cautious on Europe's energy situation as weather fluctuations could ratchet up energy prices.

Outlook: A slowing Europe and moderating China coupled with the usual year-end book closures by some institutions will continue to pose near-term challenges to the Indian stock market. We, thus, expect the Nifty 50 to be largely range-bound in the short run, but remain bullish over the longer term given several extant growth levers in the Indian economy. We continue to like domestic consumption-focused businesses.

Nifty valuations now reapproaching +1SD above 5Y avg.



Source: Bloomberg, BOBCAPS Research



HOLD

TP: Rs 2,055 | ▼ 5%

SUPREME INDUSTRIES

Plastic Products

31 October 2022

Muted quarter but H2 revival on track

- Q2 revenue grew 8% YoY led by a 9% volume uptick despite seasonal weakness
- EBITDA margin contracted 905bps YoY to 7.1% as RM-to-sales cost surged 830bps on higher inventory losses
- Volume guidance upped but margins cut on volatile PVC prices. We lower FY23 EPS 10% (FY24 unchanged); retain HOLD and TP of Rs 2,055

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Healthy volumes drive topline growth: SI's Q2FY23 revenue grew 8.2% YoY to Rs 20.9bn as volumes in plastic pipes/industrial products/packaging products grew 9%/19%/3% YoY. Overall volumes increased 9% YoY (+2.6% QoQ) to 111,803mt.

EBITDA margin contracts 905bps: Gross margin declined 830bps YoY to 23.2% due to a drop in polymer prices and inventory losses. Further, the prices of different polymers, particularly polypropylene (PP), LDPE and PVC, have fallen between Rs 31/kg and Rs 55/kg since Jan'22 – a reduction of 21-38%. This has fuelled inventory losses and, in turn, a 905bps YoY drop in EBITDA margin to 7.1% (-515bps QoQ).

Volume guidance upped, margins reduced: Management has guided for 20% volume growth in FY23 (vs. 15% earlier) and 16% topline growth to Rs 90bn. EBITDA margin is now guided to be in the region of 12-12.5% (vs. 15% earlier). According to management, the steep fall in PVC resin prices by Rs 55/kg or 38% since April this year augurs well for volume growth in H2FY23 as products become more affordable.

Better quarter than FNXP: SI reported 9.3% YoY volume growth in plastic pipes vs. 6.8% for FNXP in Q2 and a 6.5% drop in realisations vs. a 16.5% decline for its peer. Revenue in plastic pipes grew 2.2% YoY vs. a 11% fall for FNXP. On a three-year basis, the company's plastic pipe revenue has clocked a 16.8% CAGR (Q2FY20-Q2FY23) vs. a 15.7% increase for its peer over the same period.

Maintain HOLD: The correction in PVC prices has cheered sentiments across the value chain, as reflected in the 9% YoY volume growth. However, channel inventory remains low. With PVC prices now trading close to normal levels, we expect volumes to pick up in H2FY23, further supported by rising agricultural demand and better affordability. We raise FY23/FY24 topline estimates 10%/18% given the higher volume guidance, but cut FY23 PAT by 10% (FY24E unchanged) to bake in the weaker margin outlook. We continue to value SI at 29x FY24E EPS vs. its 5Y median of 31.2x and maintain our TP of Rs 2,055 with a HOLD rating given limited upside potential.

Key changes

Target	Rating
◀ ▶	◀ ▶

Ticker/Price	SI IN/Rs 2,170
Market cap	US\$ 3.3bn
Free float	51%
3M ADV	US\$ 1.8mn
52wk high/low	Rs 2,493/Rs 1,666
Promoter/FPI/DII	49%/16%/35%

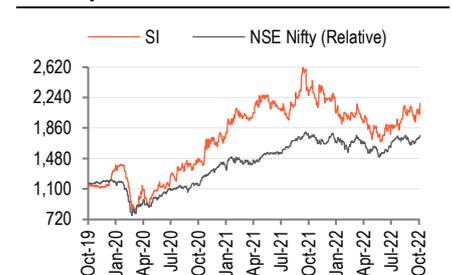
Source: NSE | Price as of 31 Oct 2022

Key financials

Y/E 31 Mar	FY22A	FY23E	FY24E
Total revenue (Rs mn)	77,728	86,486	1,00,916
EBITDA (Rs mn)	12,421	10,647	13,019
Adj. net profit (Rs mn)	9,684	7,319	8,998
Adj. EPS (Rs)	76.2	57.6	70.8
Consensus EPS (Rs)	76.2	76.3	84.6
Adj. ROAE (%)	27.6	18.1	20.3
Adj. P/E (x)	28.5	37.7	30.6
EV/EBITDA (x)	22.1	26.2	21.6
Adj. EPS growth (%)	1.0	(24.4)	22.9

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE



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Recommendation scale: Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

HOLD – Expected return from -6% to +15%

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

Our recommendation scale does not factor in short-term stock price volatility related to market fluctuations. Thus, our recommendations may not always be strictly in line with the recommendation scale as shown above.

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