

MIDCAPS

26 September 2019

Tax cut benefits capped by demand headwinds

We upgrade FY20 earnings by 2-11% for midcap companies under our coverage post the recent corporate tax cut. Top gainers include SI (11%), FNXP (10%), VMART (10%) and PIDI (9%). Our estimates are adjusted for pass-along of partial benefits to customers as companies look to perk up stagnating demand and deliver on growth targets, especially in the high-competition tile, plywood, PVC pipe and retail segments. GIL and CRS remain our preferred picks in the midcap space.

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Earnings upgrade of 2-11%: Following the government announcement slashing corporate tax rates from 34.9% to 25.6% (incl. surcharge), we upgrade earnings estimates for midcap companies under our coverage by 2-11% from FY20. Supreme Infra (SI, 11%), Finolex Industries (FNXP, 10%), V-Mart (V-MART, 10%) and Pidilite Industries (PIDI, 9%) will see the biggest upsides. Century Ply sees no change as it was already at a low tax rate.

Upgrades not commensurate with rate cuts: We do not expect the entire tax benefit to percolate to earnings, as our coverage companies likely pass along a portion of the benefit to the distribution chain/consumers and also plough some into added promotion or branding activity to revive demand. Per our industry interactions, this trend is likely to be more pronounced in segments facing high competition such as tiles, plywood, PVC pipes and retail, as also in companies with higher B2B sales.

Target price changes across the board, ratings maintained: We raise target prices across our midcap universe to bake in the tax impact, but leave ratings unchanged. We also cut our target multiple on Somany Ceramics to 15x (~25% discount to five-year average fwd P/E) due to recent lapses in systems and processes accompanied by continued demand headwinds, but retain BUY on cheap valuations.

Greenply and Cera top picks: Greenply Industries (GIL, TP: Rs 200, BUY) and Cera Sanitaryware (CRS, TP: Rs 3,135, BUY) are our preferred picks in the midcap space despite the tepid near-term demand environment, due to their strong balance sheets and reasonable valuations.

KEY RECOMMENDATIONS

Ticker	Price	Target	Rating
KJC IN	569	650	BUY
SOMC IN	195	340	BUY
MTLM IN	162	200	BUY
CPBI IN	155	200	BUY
CRS IN	2,697	3,135	BUY
ASTRA IN	1,182	1,005	REDUCE
FNXP IN	576	610	ADD
SI IN	1,194	1,210	ADD
PIDI IN	1,439	1,240	SELL
MUNI IN	216	335	BUY
VMART IN	2,149	2,030	SELL

Price & Target in Rupees | MTLM = GIL



FIG 1 – REVISED EFFECTIVE TAX ASSUMPTIONS

Companies (%)	FY19 Effective tax rate	Earlier assumed tax rate			Revised tax rate		
		FY20E	FY21E	FY22E	FY20E	FY21E	FY22E
KJC	35.6	35.7	35.7	35.7	25.6	25.6	25.6
SOMC	32.1	34.0	34.0	34.0	25.6	25.6	25.6
MTLM	27.0	28.9	26.8	26.0	26.0	21.8	21.1
CPBI	25.7	26.0	26.0	26.0	25.6	25.6	25.6
CRS	39.2	35.0	35.0	35.0	25.6	25.6	25.6
ASTRA	28.7	30.0	30.0	30.0	25.6	25.6	25.6
FNXP	33.9	35.4	35.4	35.4	25.6	25.6	25.6
SI	37.9	35.0	35.0	35.0	25.6	25.6	25.6
PIDI	32.7	34.0	34.0	34.0	25.6	25.6	25.6
MUNI	36.5	34.0	34.0	34.0	25.6	25.6	25.6
VMART	33.5	33.5	33.5	34.0	25.6	25.6	25.6

Source: Company, BOBCAPS Research

FIG 2 – REVISED EARNINGS ESTIMATES

Company	Old EPS (Rs)			Revised EPS (Rs)			Change (%)		
	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E
KJC	18.3	21.9	25.1	19.1	22.4	25.9	4.4	2.3	3.2
SOMC	15.7	21.1	25.7	16.1	21.5	26.1	2.2	1.9	1.7
MTLM	8.2	10.4	12.0	8.3	10.8	12.5	2.1	4.5	3.9
CPBI	8.0	9.8	11.0	8.0	9.8	11.0	0.4	0.4	0.4
CRS	98.0	113.6	129.0	104.1	116.7	132.6	6.2	2.7	2.7
ASTRA	17.6	21.7	26.4	18.0	22.6	27.6	2.5	4.5	4.6
FNXP	25.5	27.1	29.5	28.2	29.7	32.6	10.4	9.8	10.4
SI	34.0	40.1	47.3	37.6	42.9	50.1	10.7	7.2	5.9
PIDI	23.0	26.9	31.2	25.1	29.8	34.6	9.4	11.0	10.9
MUNI	16.6	20.8	24.5	17.3	21.4	25.6	4.6	2.8	4.4
VMART	49.3	61.3	75.7	54.4	63.4	80.6	10.3	3.5	6.4

Source: BOBCAPS Research

FIG 3 – REVISED TARGET PRICES

Company	Target price (Rs)		Rating		Rationale
	Old	New	Old	New	
KJC	640	650	BUY	BUY	Earnings revision
SOMC	445	340	BUY	BUY	Reduce multiple to 15x (~25% discount to 5Y avg. fwd. P/E) due to recent lapses in systems & processes and continued demand headwinds
MTLM	195	200	BUY	BUY	Earnings revision
CPBI	200	200	BUY	BUY	No change in earnings
CRS	3,060	3,135	BUY	BUY	Earnings revision
ASTRA	960	1,005	REDUCE	REDUCE	Earnings revision
FNXP	560	610	ADD	ADD	Earnings revision
SI	1,135	1,210	ADD	ADD	Earnings revision
PIDI	1,120	1,240	SELL	SELL	Earnings revision
MUNI	330	335	BUY	BUY	Earnings revision
VMART	1,950	2,030	SELL	SELL	Earnings revision

Source: BOBCAPS Research

Stock performance

FIG 4 – KAJARIA CERAMICS

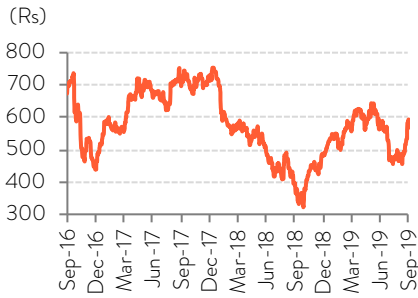


FIG 5 – SOMANY CERAMICS

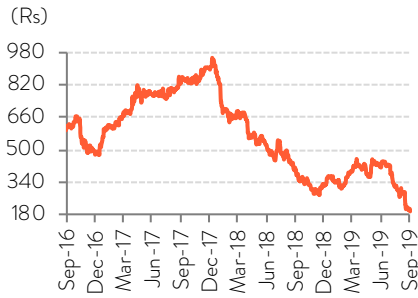


FIG 6 – GREENPLY INDUSTRIES

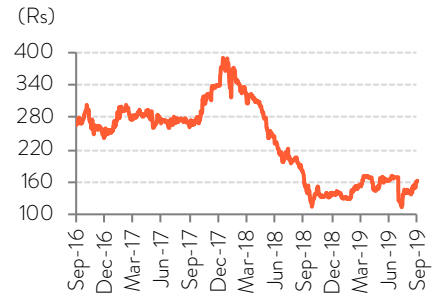


FIG 7 – CENTURY PLYBOARDS

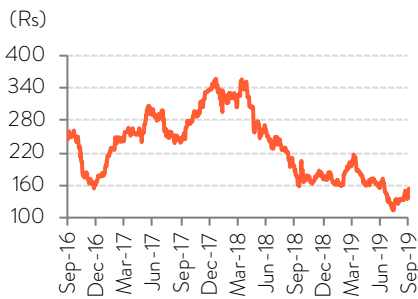


FIG 8 – CERA SANITARYWARE

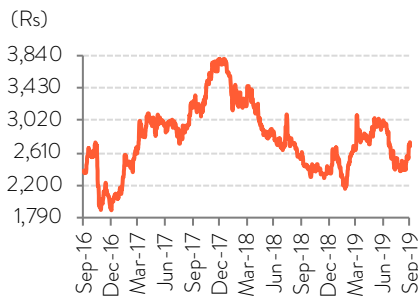


FIG 9 – ASTRAL POLY TECHNIK

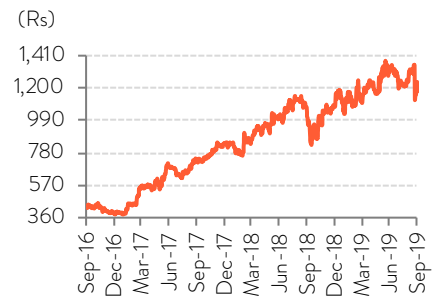


FIG 10 – FINOLEX INDUSTRIES

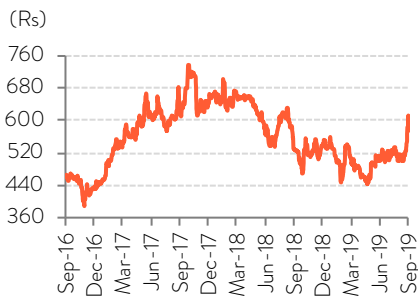


FIG 11 – SUPREME INDUSTRIES

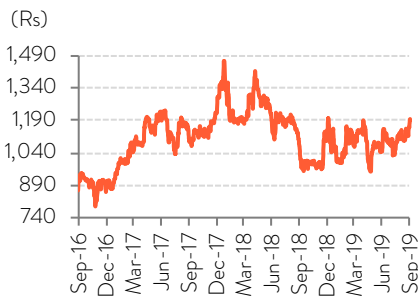


FIG 12 – PIDILITE INDUSTRIES

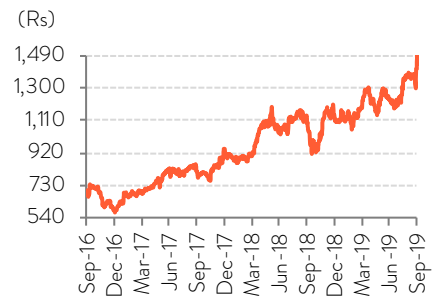


FIG 13 – MAYUR UNIQUOTERS

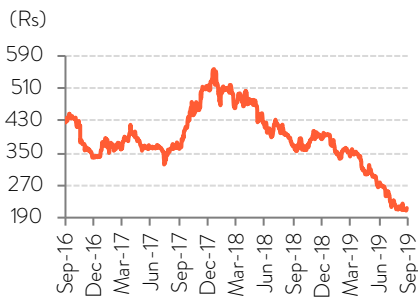
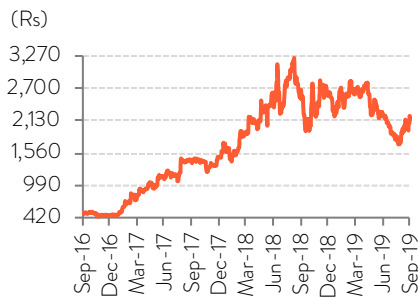


FIG 14 – V-MART RETAIL



Source: NSE

Disclaimer

Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

ADD – Expected return from >+5% to +15%

REDUCE – Expected return from -5% to +5%

SELL – Expected return <-5%

Note: Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

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