Sharekhan by BNP PARIBAS

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Stock Update

Polyplex Corporation Limited

Margin to moderate; downgrade to Hold

Plastic & Packaging	Sharekhan code: POLYPLEX	Result Update

3R MATRIX	+	=	-
Right Sector (RS)		✓	
Right Quality (RQ)	✓		
Right Valuation (RV)		✓	

+ Positive = Neutral - Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↓	

Reco/View	Change
Reco: **Hold**	↓
CMP: **Rs. 918**	
Price Target: **Rs. 950**	↑

↑ Upgrade ↔ Maintain Downgrade

Company details

Market cap:	Rs. 2,882 cr
52-week high/low:	Rs. 945/283
NSE volume: (No of shares)	1.5 lakh
BSE code:	524051
NSE code:	POLYPLEX
Free float: (No of shares)	1.5 cr

Shareholding (%)

Promoters	51.0
FII	7.5
DII	6.1
Others	35.4

Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	28.3	22.6	22.5	70.5
Relative to Sensex	24.2	3.8	-11.8	46.5

Sharekhan Research, Bloomberg

Summary

- Post a sharp increase in PCL's stock price, valuation of 6.3x FY2023E EPS is above its 5-year average one-year forward PE multiple of 5.2x and limits further valuation re-rating given cyclical natural of the business. Hence, we downgrade PCL to Hold (from Buy) with a revised PT of Rs.950.
- Q3FY21 consolidated adjusted operating profit at Rs. 329 crore (up 54.6% y-o-y; up 1.6% q-o-q) slightly lagged estimates as beat in volumes (up 19.6% y-o-y) was offset by a miss in OPM by 89 bps to 26.6%.
- BOPET spreads seem to have peaked out and could contract going forward as realisations fall with a rise in supplies, while raw material costs also harden as oil prices surge to $61/bbl.
- We believe that PCL's FY2021E margin/PAT of 26.7%/Rs. 516 crore are near peaks of the BOPET margin cycle and are not sustainable over FY2022E-FY2023E despite addition of new capacities (capex plan of $195 million).

Polyplex Corporation Limited's (PCL) Q3FY2021 consolidated revenues increased by 13.3% y-o-y (largely flat q-o-q) to Rs. 1,237 crore, in-line with our estimates of Rs. 1,266 crore. Strong revenue growth was drive by sharp 19.6% y-o-y increase in volume to 80,283 mt but the same was partially offset by a 5.2% y-o-y decline in blended realisation. Adjusted operating profit at Rs.329 crore (up 54.6% y-o-y; up 4.6% q-o-q) was 2% below our estimate of Rs. 337 crore due to miss of 89 bps in OPM at 26.6% (up 710 bps; up 20 bps q-o-q). Gross margin remained strong at 53.1% (up 687 bps y-o-y; up 228 bps q-o-q) although slightly lower than our estimate of 53.6%. The value-added-spreads remained largely stable q-o-q at $1.04/kg. Adjusted PAT before minority interest at Rs. 269 crore (up 81.4% y-o-y; flat q-o-q) was marginally above estimate of Rs. 221 crore due to higher other income and lower depreciation which offset slight in miss in OPM. However, adjusted PAT after minority interest at Rs. 131 crore (up 57.2% y-o-y; up 43.8% q-o-q) was significantly below our estimate of Rs.171 crore. In our view, BOPET spreads have peaked out and expected to contract from hereon given addition of new lines globally (one line recently commissioned in Nigeria) and likely increase in raw material cost (as oil price recovered sharply to $61/bbl). We thus believe that PCL's FY2021E EBITDA margin/PAT of 26.7%/Rs.516 crore are near peak level of BOPET margin cycle and not sustainable over FY2022E-FY2023E despite addition of new capacities (capex plan of $195 million). Also, PCL's valuation of 6.3x FY2023E EPS is above its 5-year average one-year forward PE multiple of 5.2x and limits further valuation re-rating given cyclical nature of the business. Hence, we downgrade PCL to Hold (from Buy) with a revised PT of Rs. 950.

Key positives

- Better-than-expected volume growth of 19.5% y-o-y to 80,283 mt versus expectation of 10% y-o-y volume growth.
- Special dividend of Rs.100/share takes total dividend to Rs.147/share (implies 16% dividend yield) for FY2021.

Key negatives

- Lower-than-expected OPM at 26.6% versus expectation of 27.5%.

Our Call

Valuation – Downgrade PCL to Hold with revised PT of Rs. 950: PCL stock price has rallied sharply by 71% in the last one year led by strong earnings performance supported by ramp-up of volumes and high EBITDA margins. Moreover, the management's focus to reward shareholders through dividends [Rs. 147/share for FY2021 (16% dividend yield) including special dividend of Rs.100/share] has been taken positively by the investors. We believe that PCL's earnings momentum would taper off over FY2022-FY2023 despite addition of new capacities (post expectation of record PAT of Rs.516 crore in FY2021E) as BOPET spreads seems to be peaked out and likely to contract with higher supplies from addition of BOPET lines globally. Moreover, PCL's valuation of 6.3x FY2023E EPS is above its 5-year average one year forward PE multiple of 5.2x and limits further valuation re-rating given cyclical natural of the business. Hence, we downgrade PCL to Hold (from Buy) with a revised PT of Rs. 950.

Key risk

Lower capacity addition globally could result into higher BOPET film margin and better-than-expected demand could result in higher volume growth.

Valuation (Consolidated) Rs cr

Particulars	FY19	FY20	FY21E	FY22E	FY23E
Revenues	4,570	4,487	4,966	4,991	5,608
OPM (%)	16.0	17.4	26.7	23.6	22.7
Adjusted PAT	330	282	516	437	475
% YoY growth	107.0	-14.5	82.8	-15.3	8.7
Adjusted EPS	101.4	86.6	158.4	134.2	145.8
P/E (x)	9.1	10.6	5.8	6.8	6.3
P/B (x)	1.1	1.0	0.9	0.8	0.7
EV/EBITDA (x)	3.9	3.4	1.8	1.9	1.6
RoNW (%)	12.4	9.7	16.1	12.5	12.5
RoCE (%)	15.2	11.9	19.7	15.0	14.9

Source: Company; Sharekhan estimates

Broadly in-line performance as higher-than-expected volume growth gets off by miss in OPM: Q3FY2021 consolidated revenues increased by 13.3% y-o-y (largely flat q-o-q) to Rs. 1,237 crore, in-line with our estimates of Rs. 1,266 crore. Strong revenue growth was drive by sharp 19.6% y-o-y increase in volume to 80,283 mt but the same was partially offset by a 5.2% y-o-y decline in blended realisation. Operating profit at Rs.329 crore (up 54.6% y-o-y; up 4.6% q-o-q) was 2% below our estimate of Rs. 337 crore due to miss of 89 bps in OPM at 26.6% (up 710 bps; up 20 bps q-o-q). Gross margin remained strong at 53.1% (up 687 bps y-o-y; up 228 bps q-o-q) although slightly lower than our estimate of 53.6%. The value-added-spreads remained largely stable q-o-q at $1.04/kg. Adjusted PAT before minority interest at Rs. 269 crore (up 81.4% y-o-y; flat q-o-q) was marginally above estimate of Rs. 221 crore due to higher other income and lower depreciation which offset slight in miss in OPM. However, adjusted PAT after minority interest at Rs. 131 crore (up 57.2% y-o-y; up 43.8% q-o-q) was significantly below our estimate of Rs.171 crore.

Capex to expand BOPP and BOPET lines – to drive volume growth in FY2023: The recently-commissioned BOPET line at Indonesia has been fully ramped and is driving volume growth in current fiscal. Further, the company is setting up 60 ktpa BOPP line in Indonesia ($53 million capex and scheduled to be commissioned in H1FY2022), 50-ktpa BOPET line in the US ($83 million capex and to be commissioned by H2FY2023). Overall capex plan is at $195 million over FY2021E-FY2023E for expansion of the BOPP and BOPET lines, which would drive sustained volume growth over the next few years.

Capex schedule over FY2022-FY2023

Projects	Location	Capital cost ($ million)	Likely Start Up
Brownfield - BOPP	Indonesia	53	H1FY2022
Brownfield - BOPET	USA	83	H2FY2023
Other Projects	India	3	Upto Q3FY2022
Other Projects	Overseas	56	Upto Q4FY2022
Total		**195**	

Source: Company; Sharekhan Research

Results (consolidated) **Rs cr**

Particulars	Q3FY21	Q3FY20	YoY (%)	Q2FY21	QoQ (%)
Net Sales	**1,237**	**1,092**	**13.3**	**1,227**	**0.8**
Total Expenditure	908	879	3.3	1,047	-13.3
Operating profit	**329**	**213**	**54.6**	**181**	**82.4**
Adjusted operating profit	**329**	**213**	**54.6**	**324**	**1.6**
Other Income	14	3	407.2	13	11.1
Interest	4	4	-2.3	4	-7.4
Depreciation	71	61	16.5	69	1.9
Exceptional income/(expense)	0	0	NA	0	NA
Reported PBT	**269**	**151**	**77.9**	**120**	**124.7**
Adjusted PBT	**269**	**151**	**77.9**	**263**	**2.1**
Tax	44	27	61.9	17	153.5
RPAT before minority interest	225	124	81.4	102	119.8
Adjusted PAT before minority interest	225	124	81.4	225	-0.1
Minority interest	93	53	76.5	26	262.6
RPAT after minority interest	**131**	**71**	**85.0**	**77**	**71.7**
Adjusted PAT after minority interest	**131**	**71**	**85.0**	**168**	**-22.0**
Equity Cap (cr)	3	3		3	
Reported EPS (Rs.)	41.1	22.2	85.0	23.9	71.7
Adjusted EPS	41.1	22.2	85.0	52.6	-22.0
Margins (%)			**BPS**		**BPS**
OPM	26.6	19.5	710	26.4	20
Effective tax rate	16.4	18.0	-162	14.5	186
NPM	**10.6**	**6.5**	**411**	**13.7**	**-310**

Source: Company; Sharekhan Research

Outlook and Valuation

■ Sector View – BOPET demand to remain strong but margins to decline as new capacities come onstream

The flexible packaging segment has witnessed strong demand traction from the consumer staples, food and health & hygiene segments, which in turn is expected drive volumes for producers of BOPET films in the near to medium term. Overall, BOPET demand is expected to grow at a healthy rate of 7-8% over the next few years. However, we believe that BOPET margin have peaked out and expected to moderate as new BOPET lines are expected to come on-stream and thus we expect margins to decline over FY2022-F2023.

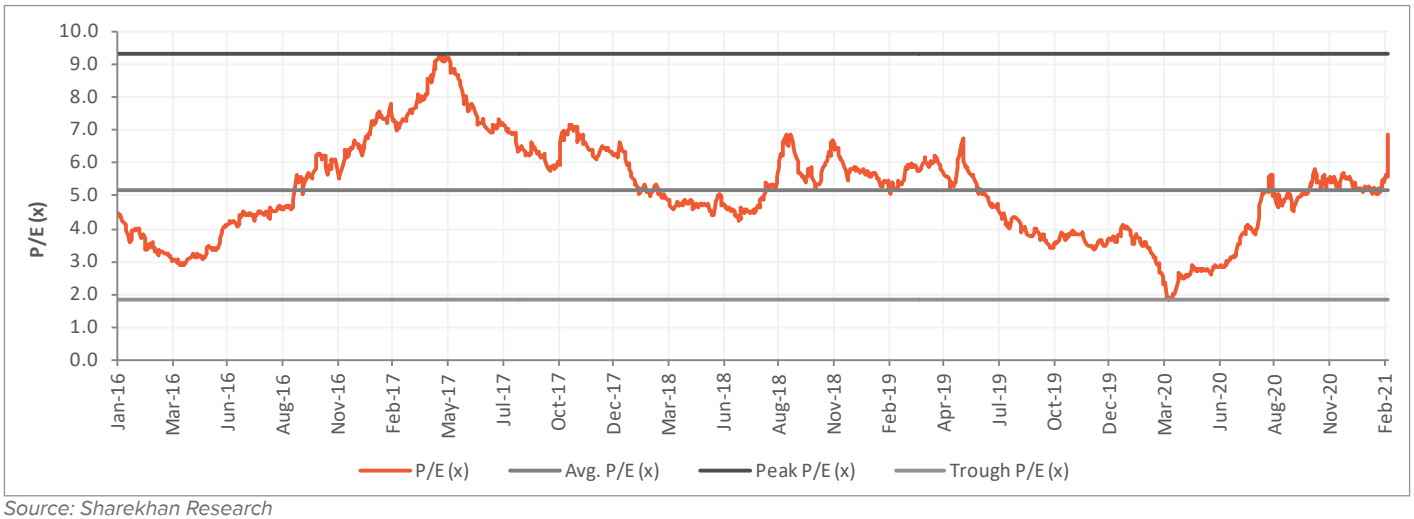
■ Company Outlook – Profitability at peak; earnings to moderate over FY2022E-FY2023E

Volume growth is likely to remain strong, supported by its recent BOPET capacity expansion by 16% to 312,645 tonnes (recent commissioning of BOPET capacity of 44,000 MT in Indonesia). The company is also expanding its BOPP capacity by 19% and the same is expected to get completed in H1FY2022. Hence, we believe capacity expansion would drive a 9% volume CAGR for PCL over FY2020-FY2023E. However, EBITDA margins are expected to contract by 401 bps over FY2021-FY2023 as BOPET spread expected to contract going forward.

■ Valuation – Downgrade PCL to Hold with revised PT of Rs. 950

PCL stock price has rallied sharply by 71% in the last one year led by strong earnings performance supported by ramp-up of volumes and high EBITDA margins. Moreover, the management's focus to reward shareholders through dividends [Rs. 147/share for FY2021 (16% dividend yield) including special dividend of Rs.100/share] has been taken positively by the investors. We believe that PCL's earnings momentum would taper off over FY2022-FY2023 despite addition of new capacities (post expectation of record PAT of Rs.516 crore in FY2021E) as BOPET spreads seems to be peaked out and likely to contract with higher supplies from addition of BOPET lines globally. Moreover, PCL's valuation of 6.3x FY2023E EPS is above its 5-year average one year forward PE multiple of 5.2x and limits further valuation re-rating given cyclical natural of the business. Hence, we downgrade PCL to Hold (from Buy) with a revised PT of Rs. 950.

One-year forward P/E (x) band



Source: Sharekhan Research

About company

PCL is among the largest BOPET film company globally in terms of capacities. The company's polyester capabilities include both PET thin film (230,000 tonne) and PET thick films (28,800 tonne) and its business portfolio includes BOPP, Blown PP/PE, and CPP films. The company has manufacturing units in India (90,000 tonne – 29% of capacity), Thailand (89,645 tonne – 29% of capacity), Turkey (58,000 tonne – 19% of capacity), US (31,000 tonne – 10% of capacity), and Indonesia (44,000 tonne – 14% of capacity).

Investment theme

Robust demand for packaging and capacity additions by PCL in the BOPET segment would aid volume growth. However, we believe that BOPET margin cycle is near peak levels and spreads are expected to contract from current level with rise in supplies are higher raw material cost. Hence, we believe that PCL's profitability has also peak out and not sustainable as margin would decline over FY2022E-FY2023E.

Key Risks

- Lower BOPET capacity addition globally could result into higher BOPET film margin.
- Better-than-expected demand could result higher volume growth for PCL and vice versa.

Additional Data

Key management personnel

Sanjiv Saraf	Chairman
Pranay Kothari	Chief Executive Officer
Manish Gupta	Chief Financial Officer

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Reliance Capital Trustee Co Ltd	4.6
2	KESWANI HARESH TIKAMDAS	3.2
3	Haresh Keswani	3.0
4	BHANSHALI AKASH	1.7
5	Finquest Securities Pvt Ltd	1.3
6	Soyuz Trading Co Ltd	1.3
7	IL&FS Trust Co Ltd	1.2
8	Kirpalani Ricky Ishwardas	1.1
9	WisdomTree Investments Inc	1.0
10	Dimensional Fund Advisors LP	0.9

Source: Bloomberg; Note: Shareholding as on November 13, 2020

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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