Century Plyboards

BUY

Result Update

Top-line miss offset by positive margin surprise

Strong margin expansion (to 17.5%, up 660bps YoY) offset the revenue miss (10% lower than our estimate) in 4QFY15; however, the following points are worth noting: (a) slowdown in plyboard volume growth (5-6% vs 13% in 9MFY15), (b) low EBIT margin in laminates (8% despite near-full capacity utilisation), and (c) increase in the cash conversion cycle. Whilst lower plyboard volume growth can be explained by weak demand and rising aggression of peers, margin expansion was on account of lower costs of face veneer and crude-linked derivatives; as a result, EBITDA and PAT jumped 93% and 462% in 4QFY15. Whilst we do not doubt the company's long-term growth capability owing to its scale, investments in raw material security, distribution, branding and professional management, this deceleration in growth of building materials could adversely impact our optimistic near-term growth estimates (29%/34% revenue/EBITDA CAGR in FY15-17E). The stock is trading at 23x FY16E EPS. Our target price implies 21x FY17E EPS.

Stock Information

Bloomberg Code:	CPBI IN
CMP (Rs):	217
TP (Rs):	275
Mcap (Rs bn/US$ bn):	48/0.8
3M ADV (Rs mn/US$ mn):	146/2.3

Stock Performance (%)

	1M	3M	12M	YTD
Absolute	(5)	17	515	37
Rel. to Sensex	(5)	24	494	37

Source: Bloomberg, Ambit Capital research

Ambit Estimates (Rs bn)

	FY15	FY16	FY17
Revenues	15.5	20.5	25.7
EBITDA	2.5	3.4	4.5
EPS (Rs)	6.8	9.6	13.5

Source: Bloomberg, Ambit Capital research

Results overview—Slow growth in ply; lower raw material cost support margin expansion

Century's 4QFY15 revenue was 9% lower than our estimate, on account of only 5% volume growth in plyboard as against our expectation of 13-14%. However, strong EBITDA margin (17.4% excluding forex gains; up 660bps YoY) offset the lower revenue and led to 93%/462% YoY EBITDA/PAT growth.

The segment-wise summary is as follows:

Plyboards—strong 19.8% margins but slowest growth is last six quarters

Revenue in this segment grew by 11% YoY (slowest in the last six quarters), led by 4-5% volume growth (indicative, the management is still to share volume details) and 5-6% realisation growth. EBIT margins improved to 19.8% vs 11.2% last year on account of: **(a)** realisation improvement for organised players such as Century given declining competitiveness of unorganised from low-quality product and irregular supplies, post the ban on timber exports from Myanmar and **(b)** raw material cost savings from declining face veneer prices in Myanmar, procurement of low cost "beech" core timber from Germany and cost savings in crude-linked inputs such as phenol and formaldehyde. Another possible reason for margin expansion could be sales of face veneer at a high gross margin to the unorganised manufacturers.

In FY15, the plyboard segment's revenue grew by 19%, implying 13% volume growth and 6% realisation growth.

Laminates—near-full capacity utilisation, but lower margins

Laminates revenue grew by 31% YoY led by significant utilisation ramp-up, post doubling of capacities last year. The segment operated at near-full capacity utilisation and the company has increased the working shift to seven days (from six days earlier) and is looking at adding a unit in western India. Whilst investments in advertisements and ramp up of the dealer network facilitated market share gains from other organised players, EBIT margin remained low at 8% (up 90bps QoQ) due to high sales and marketing expenses. In FY15, the laminate segment's revenue grew by 20%, implying 19% volume growth and 4% realisation growth.

FY15 balance sheet shows increase in cash conversion cycle

Century's FY15 balance sheet shows: **(a)** reduction in debt/equity to 1.3x vs 2.0x in FY14 (owing to increase in net worth and Rs700mn repayment of buyers credit (outstanding balance Rs1.5bn vs Rs2.2bn in FY14), **(b)** CFO generation of Rs1.4bn (implying 69% pre-tax CFO/EBITDA conversion vs 26% last year), **(c)** increase in cash

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conversion cycle (working capital days increased to 166 vs 157 in FY14) on account of increase in debtor days (to 63 vs 57 in FY14) and higher finished goods inventory days (although raw material inventory days dropped sharply) and **(d)** increase in RoCE to 22% (vs 19% in FY14) and RoE (adjusted for forex lass/gains) to 36.5% vs 36% in FY14.

Where do we go from here? Expect the growth momentum to sustain further

Century's stellar performance in FY15 (18% revenue growth and 41% EBITDA growth) was supported by its scale expansion and significant increase in distribution and branding amid declining competitiveness of unorganised peers facing raw material procurement constraints. Whilst we retain our long-term thesis that Century's elevated scale, strong brand and expansion of product-lines will further improve market share, low plyboard revenue growth and increase in debtor debtors in 4Q raise concerns on near-term momentum, as the home building materials sector comes under pressure from decelerating home sales/construction.

Our current estimates are optimistic and build in 18%/15% volume growth in plyboards (basis sustained market share gains amid improving industry volumes) and 35% volume growth in laminate (given near-full capacity utilisation) in FY16 and 15% in FY17. Alongside, we build in EBITDA margin of 16.2% in FY16 and 16.9% in FY17. Whilst the company may achieve the higher EBITDA margin (given benign crude prices and savings in timber costs), our volume growth estimate faces downside risks.

We await certain clarifications from the management in the conference call scheduled on Thursday (30 April 2015) before revisiting our estimates.

Valuation and recommendation—growth longevity supports rich multiples

Post the recent re-rating, the stock is trading at 25x FY16E EPS, in line with categories such as tiles but at a 35% discount to paints, despite high RoEs of 35-37% and visibility of 35-40% earnings CAGR over FY15-17E. We highlight that most of the home building material companies/sectors went through multiple re-ratings, as brand association with customers rose and the share of the unorganised market shrunk. Our target price of Rs275 implies 21.0x FY17 EPS; we expect RoCEs to expand to 29% RoCE in FY17 from better cash conversion. Whilst we believe that the company's multiples can sustain further, given the longevity of high growth, multiples in the near term face the risk from decelerating demand and non-improvement in cash generation.

Questions for the management

The company will host a conference call on Thursday. We suggest the following questions for investors to seek answers from the management:

- The company's plyboard volume growth has decelerated in 4Q, similar to other home building categories; is this decline on account of relatively weaker demand conditions or higher aggression of players such as Greenply?
- How has the company's plyboard product mix shifted? What proportion of the overall sales comprised *"Sainik"* and *"Maxima"*?
- The company targets 20%-plus revenue growth in FY16; what is the strategy to achieve that given the evident slowdown in home building materials' sales? How sustainable are the cost savings in raw materials and how much inventory is the company holding at present? Is there a chance that some of the savings will be shared with the customers in the next few quarters given weak demand?
- Did the company need to undercut pricing to gain market share in laminates? With the laminates capacity achieving peak capacity utilisations, what are the expansion plans for this segment? How much money will the company commit and when will the expansion be complete?

- What is the outstanding debt and of that how much is Buyers credit and ECBs? What is the repayment plan for the debt and is the foreign currency loan completely unhedged and susceptible to currency volatilities?
- Will the company sustain the high rate of dealer/distributor addition in FY16?
- Has production at the Laos facility commissioned and if not what is the expected timeline? What quantity of plyboard manufacturing would the Myanmar and Laos unit be able to support?
- What proportion of your total PBT is currently generated from the tax-exempt North East unit and what is the tax rate guidance for FY16 and FY17?

Exhibit 1: Quarterly snapshot (Rs mn unless mentioned)

Particulars	4QFY14	3QFY15	4QFY15	YoY (%)	QoQ (%)	Ambit Est	Dev (%)	Comments
Net Sales	3,404	3,818	4,049	19.0	6.0	4,507	(10.2)	Lower-than-expected revenue growth owing to low plyboard volume growth
Operating costs	2,830	3,129	3,299	16.6	5.4	3,750	(12.0)	Margin expansion driven by raw material cost savings
EBITDA	599	730	793	32.5	8.8	738	7.5	
EBITDA margin	17.6	19.1	19.6	199bps	49bps	16.4	322bps	Higher-than-expected margin was a function of better realisations and raw material cost savings
EBITDA (ex-forex)	368	710	710	93.0	0.1	738	(3.7)	
EBITDA margin (ex-forex)	10.8	18.6	17.5	673bps	-105 bps	16.4	117 bps	
Other income	7	9	9	20.2	(7.6)	10	(13.5)	
Depreciation	89	116	119	33.8	2.2	112	6.3	YoY increase on account of depreciation of recently added capacities
EBIT	518	623	592	14.3	(5.0)	636	(7.0)	Strong EBIT growth was a function of high EBITDA growth and no forex losses
Interest cost	206	144	90	(56.1)	(37.4)	130	(30.6)	
PBT	312	479	593	90.2	23.9	506	17.2	
Tax	18	64	114	532.9	76.2	81	40.1	Higher-than-expected EBITDA and forex gains of Rs80mn drove higher reported PAT; however, PAT adjusted for forex gains was in line with our estimate,
PAT	294	414	480	63.2	15.8	425	12.8	
PAT (adj for forex gains/ losses)	**76**	**397**	**429**	**461.7**	**7.9**	**425**	**0.8**	
EPS	1.3	1.9	2.2	63.2	15.8	1.9	12.8	

Source: Company, Ambit Capital research

Exhibit 2: Significant improvement in plyboards EBIT margin

	4QFY14	3QFY15	4QFY15	YoY (%)	QoQ (%)
Segmental Sales (Rs mn)					
Plyboard	2,638	2,810	2,918	10.6	3.9
Laminates	617	716	805	30.5	12.4
CFS	120	186	174	45.0	(6.2)
Others	34	114	160	366.3	40.2
Segmental EBIT (Rs mn)					
Plyboard	436	540	576	32.1	6.7
Laminates	33	51	65	94.7	26.9
CFS	28	60	60	112.9	(0.8)
Others	(6)	(8)	(8)	38.1	(4.7)
Segmental EBIT (%)					
Plyboard	16.5	19.2	19.8	321 bps	53 bps
Laminates	5.4	7.1	8.0	265 bps	92 bps
CFS	23.3	32.4	34.2	1092 bps	187 bps
Others	(16.8)	(7.3)	(5.0)	1184 bps	234 bps

Source: Company, Ambit Capital research

Balance Sheet

Year to March (Rs mn)	FY14	FY15E	FY16E	FY17E
Total Networth	2,931	3,749	5,878	8,355
Loans	5,276	4,677	4,526	4,176
Sources of funds	8,314	8,418	10,578	12,741
Net block	3,164	2,781	4,012	4,055
Investments	31	4	31	31
Total Current Assets	6,793	7,819	9,471	12,311
Current liabilities and provisions	1,914	2,041	2,936	3,656
Net current assets	4,879	5,778	6,535	8,655
Application of funds	8,314	8,418	10,578	12,741

Source: Company, Ambit Capital research

Income statement

Year to March (Rs mn)	FY14	FY15E	FY16E	FY17E
Revenue	13,477	15,525	20,525	25,668
Total expenses	11,961	13,015	17,175	21,326
EBITDA	1,766	2,488	3,393	4,492
Net depreciation / amortisation	387	448	465	504
EBIT	1,416	2,231	3,014	4,094
PBT	629	1,654	2,697	3,793
Adjusted PAT	786	1,365	2,124	2,998
EPS diluted (Rs)	2.7	6.8	9.6	13.5

Source: Company, Ambit Capital research

Cash flow statement

Year to March (Rs mn)	FY14	FY15E	FY16E	FY17E
PBT	**629**	**1,799**	**2,697**	**3,793**
Change in working capital	(1,168)	(911)	(1,137)	(1,267)
Direct taxes paid	(117)	(290)	(539)	(759)
CFO	**338**	**1,432**	**1,717**	**2,467**
Capex	643	400	1,137	547
CFI	**(706)**	**(327)**	**(1,051)**	**(442)**
Proceeds from borrowings	372	364	(250)	(350)
CFF	**(281)**	**(1,118)**	**(936)**	**(1,172)**
Net increase in cash	(649)	(13)	(270)	853
FCF	**(305)**	**1,032**	**580**	**1,920**

Source: Company, Ambit Capital research

Ratio analysis / Valuation parameters

Year to March	FY14	FY15E	FY16E	FY17E
RoCE	19	22	25	28
RoIC	23	27	32	37
RoE	36	36	36	36
Debt/Equity(x)	1.7	1.2	0.7	0.5
Net debt/Equity(x)	1.6	1.1	0.6	0.3
P/E (x)	62.3	35.4	23.0	16.3
P/B(x)	16.1	12.7	8.1	5.7

Source: Company, Ambit Capital research