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Archidply Industries good bet for investment
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Company: Archidply Industries
Issue Size: Rs 46.3- 52.9 crore
Price band: Rs 70-80
Date: June 11-17, '08

Archidply is one of the major plywood manufacturers in the organised sector in India. The Supreme Court (SC) had given an order barring unlicensed players in the plywood business.

This has improved the market share of organised sector players, whose growth was crippled in the past due to price competition from small-scale manufacturers. The SC order has set a high entry barrier for new entrants in the industry.

The company plans to set up manufacturing plants for particle wood and medium-density fibreboard (MDF) from its IPO proceeds. The particle wood plant will be set up at Chintamani in Karnataka, while the MDF plant is scheduled to come up at Rudrapur in Uttarakhand.

Particle wood is a potentially high-growth business in India, as it constitutes a mere 30% of decorative wood business, compared to 70% in other parts of the world. Particle wood is cheaper than plywood as a higher percentage of raw material gets converted to particle wood than plywood.

A particle wood plant needs an investment of around Rs 40 crore, which acts as an entry barrier in an industry which was earlier characterised by small players with investment not exceeding a few crores of rupees.

The company targets both institutional, as well as retail clients. Its institutional clients span sectors like banking, hospitality and IT.

This bodes well for Archidply, as banks have been opening new branches and the hospitality sector is also witnessing a boom. On the retail side, the company targets high net-worth clientele, primarily owners of bungalows, penthouses and 3-4 bedroom apartments.

At present, the company has plants at Mysore in Karnataka and Rudrapur in Uttarakhand. It is the only plywood company to have plants in both North and South India. Other players like Greenply and Century have plants only in the

northern and eastern parts, which increases their logistics costs. Moreover, the production facility at Uttarakhand enjoys exemption from entry tax, a lower rate of central sales tax and exemption of income tax for the first five years from FY07.

FINANCIALS:

The company is on an aggressive growth phase, as its FY08 net sales and profit registered a YoY growth of 52.7% and 185.5%, respectively. The revenue increased at such a high rate as the capacity utilisation at its Uttarakhand plant increased in FY08.

Improved capacity utilisation at the Uttarakhand plant helped improve the return on capital employed (RoCE) to 24.6% in FY08 from just 12.9% in FY07. The company's working capital was under pressure in FY08, as the wood product industry is largely credit-driven, which resulted in low free cash flow in FY08.

This happened because the company was still in the process of building its brand and, therefore, did not have high bargaining power with distributors. It expects that its marketing and brand-building will help it to push its products through the distribution network. In case it is unable to do so, it will be left with little free cash flows to fuel its growth plans in the long term.

VALUATIONS:

At the upper band, the issue comes at a P/E of 11.7. Its peers, Greenply and Uniply, trade at P/Es of 8 and 6.6, respectively. Moreover, Archidply has an operating margin of 20%, which is much higher than its competitors. A combination of reasonable multiples and higher margins makes Archidply a good bet for investment.