Dec 12, 2017 PICK OF THE MONTH VOL-3, NO-26

Kokuyo Camlin Limited

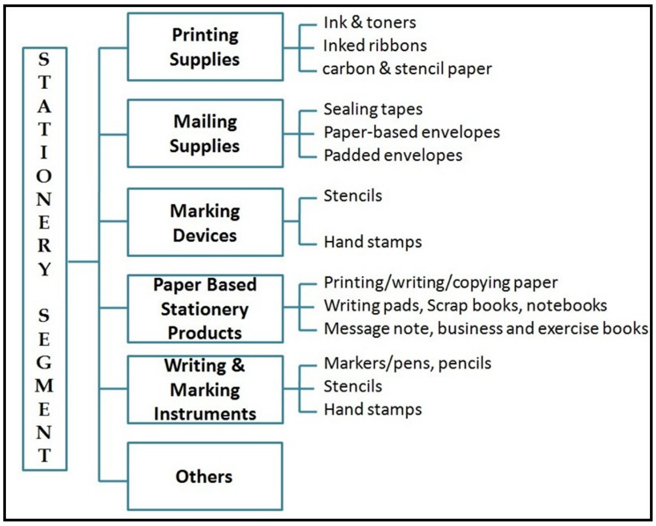
BUY

CMP: Rs. 132 **TARGET PRICE: Rs. 175** **TIME : 12 months**

OVERVIEW: Industry:

Over years, decades and many centuries, one of the integral part of human consumption has been stationery products. These are used as utility items (like paper products, desk supplies, filing supplies etc.) in offices and commercial spaces for several purposes. The market for office stationery and supplies will grow gradually but at its own pace. In current times as well, despite technological advancements, the traditional stationery, writing instruments and paper-oriented products are widely purchased. Despite the minute increase in the prices over the last 3-4 years, this market is poised to grow stronger. The major users of these products are school children, various offices and commercial spaces. The strongest spending growth has been seen in the students sector, where a healthy balance is maintained between the usage of traditional products as well as the products which are technologically advanced. Some of the major global stationery market players include Pilot Corporation, True Color, ITC, Shanghai M&G Stationery, Zebra Pen Corporation, Kokuyo Camlin, Navneet, Beifa Group, Uni Mitsubishi, Pentel, Wenzhou Aihao Pen, Guangbo Group, Snowhite Stationery, Lion Pencil Co Ltd, G M Pens International, Cello Corporate (BIC) and Shenzhen Comix Group etc.

Major factors driving the global stationery products market include growing level of literacy, increasing number of population receiving education, rise in number of schools, more youth going to schools and other educational institutions. Demand for premium branded pens and marking instruments which are considered as a status symbol is also increasing. Increasing number of start-ups and establishments is also fuelling the demand for stationery products which is also driving the market for stationery products. Government initiative towards educational programs is also driving the market positively.



Source: Company

Asia is anticipated to be the world's largest market for stationery products in 2017. This will continue to soar higher in times to come due to favourable demography in the markets here. As per some research reports global revenue from the segment of hobby and stationery is estimated to reach around USD130bn with an annual CAGR of 11.3% between the periods from 2017 to 2021. Asian countries are forecasted to emerge as the highest revenue contributor at nearly 40-42% of the global revenues. Asia is thus poised to be the largest stationery market in near term as well as distant future. The ever increasing population across the globe and especially in the APAC region will fuel the growth and requirement for the stationery products. Large youth population in India and China (most rapidly growing countries in the APAC region) provide a vision for the upcoming demand for these products. While at the same time, the countries in the Middle East & African zone are predicted to witness high growth rate due to increasing literacy rates. North America which held the largest market share in 2016-17 will also deliver a steady growth rate in near future.

Please Turn Over

SNAPSHOT

52 week H / L	Mcap (INR mn)
135 / 77	13,240
Face value: 1	
BSE Code	NSE CODE
523207	KOKUYOCMLN

Annual Performance

(Rs mn)	FY15	FY16	FY17	FY18E
Sales (Net)	5,439	6,142	6,403	7,008
EBITDA	174	245	216	249
EBITDA (%)	3.2	4.0	3.4	3.6
Other Income	77	54	29	31
Interest	98	107	105	95
Depreciation	110	119	124	146
PBT	43	73	15	39
PAT	49	53	10	25
Equity	100	100	100	100
EPS (INR)	0.49	0.52	0.10	0.25

Quarterly Performance

Parameters (Rs mn)	Dec-16	Mar-17	June-17	Sept-17
Sales (Net)	1,287	1,930	1,616	1,343
EBITDA	16	91	15	70
EBITDA (%)	1	5	1	5
Other Income	5	4	26	1
Interest	29	19	24	22
Depreciation	30	33	37	46
PAT	(26)	29	(13)	3
Equity (Rs mn)	100	100	100	100

Ratio Analysis

Parameters (Rs mn)	FY15	FY16	FY17	FY18E
EV/EBITDA (x)	76.0	55.1	64.8	55.7
EV/Net Sales (x)	2.4	2.2	2.2	2.0
M Cap/Sales (x)	2.4	2.2	2.1	1.9
M Cap/EBITDA (x)	76.3	54.0	61.3	53.2
Debt/Equity (x)	0.3	0.4	0.4	0.3
ROCE (%)	6%	7%	5%	5%
Price/Book Value (x)	6.2	6.1	6.1	6.0
P/E (x)	268	253	1394	526

Share Holding Pattern as on 30th Sept 2017

Parameters	No of Shares	%
Promoters	75215950	74.99
Institutions	146115	0.15
Public	24941741	24.87
TOTAL	100303806	100

Note: All the data is calculated as per Price of Rs132 on 12th Dec 2017.

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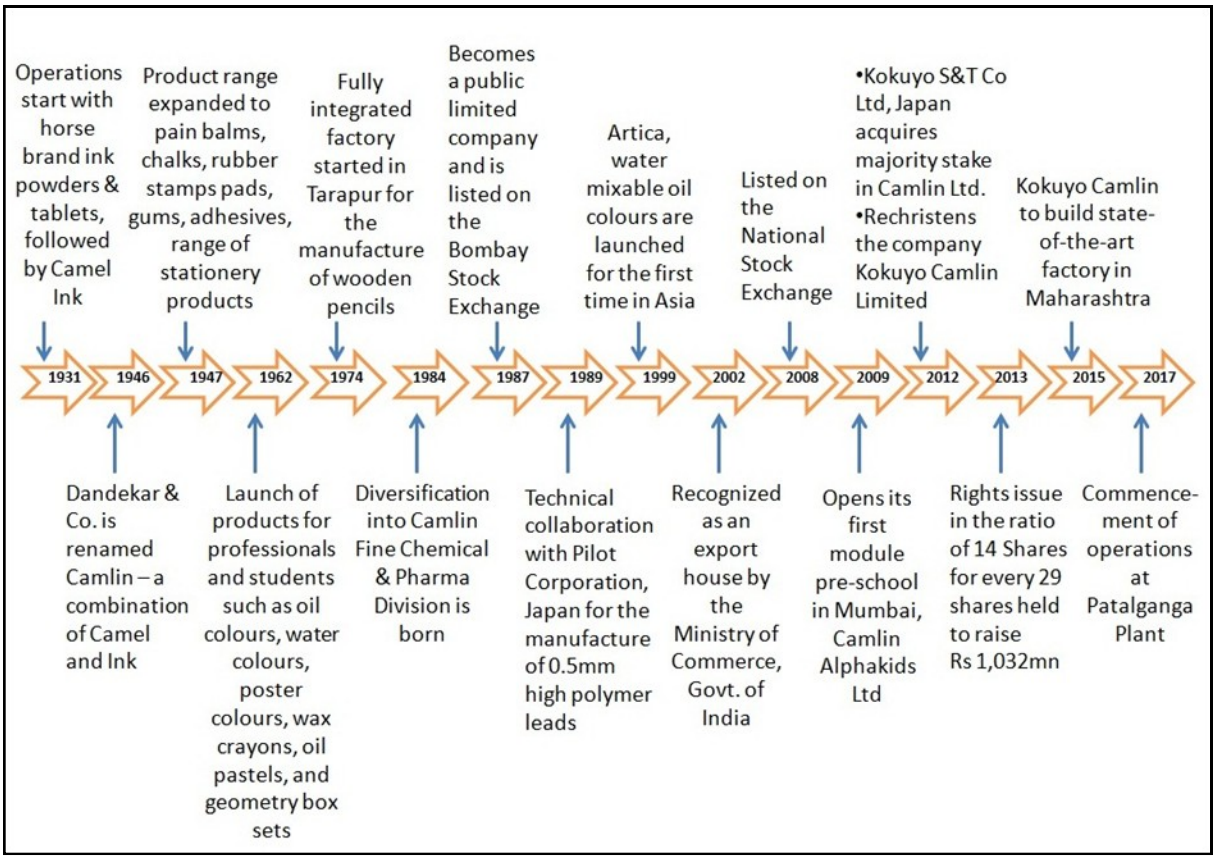
OVERVIEW: Industry: (contd.)

The education supplies market is growing ahead of the overall economy and well ahead of the office products market. In December 2016, stationery industry in India was around Rs200bn. This industry is poised for innovation and growth in tune of CAGR of 15% in the next few years. As per Federation of Maharashtra Stationery Manufacturers & Traders Association (FMSMTA), the writing paper industry was estimated to be at Rs100bn and notebooks had a share of Rs70bn in 2016-17. There is still more room for growth in the Indian market as there are more than 220mn to 240mn students studying who will require notebooks and other stationery materials. Moreover, the government's ambitious plans of Sarva Shiksha Abhiyan will also benefit the industry. With the awareness towards girl education picking up demand in the rural parts of India; participants requiring stationery products are added. Some of the key players in the Indian market include ITC, Navneet, Kokuyo Camlin, Anupam and Sundaram.

Rapid digitization is a major hindrance to the global market for stationery products. With increase in use of laptops and smart phones, the demand for some stationery products has reduced. For segments such as inked ribbons, printing papers, labels and marking devices, digitization has brought new opportunities. There is no doubt that there is digital erosion, however the same is in certain selected categories only. The diversity in the stationery market is so vast, that the digital erosion as of now is meager to have any meaningful impact on the total growth. Digital disruption has moderately impacted the traditional stationery, but the same cannot affect the usage amongst school students. If we look at the brighter side, ordering products online is gradually picking up and will continue with times ahead. Disruptions will come; however, there is still a lot of time for full replacement in this sector; whenever a disruption comes in the market, there are innovative products launched in the stationery market to off-set the impact.

About the Company:

Kokuyo Camlin limited (KCL), is one of the leading stationery brands in India. Camlin Limited was nearly 8 decade old company wherein the operations commenced in 1931, with its well known brand Camel and Camlin. In 2011, the company was acquired by a leading stationery manufacturer of Japan-Kokuyo Co. Ltd, post which the company was renamed as Kokuyo Camlin Limited. Recently with some top management level changes that have taken place; the company is now completely under the management of the Japanese. The company has its plants located at Taloja, Jammu, Tarapur, Vasai and the new plant at Patalganga. Brand name-Camlin is the biggest asset for the company. The Company does not have any material subsidiary.



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INVESTMENT RATIONALE

(A) Patalganga Plant: The Game Changer

The size of the property at Patalganga is somewhere around 14 acres of land, while the company is currently using only half of it (maybe around 6.5acres). The capacity created is good enough for the next 5-6 years. This clearly shows the scope of further addition of capacity if the management intends to expand in times to come. This is bound to happen, as they will be launching new products to capture the market further. This could also be the case, once the plant is stabilized.

This is a green factory and the plant is quite futuristic in design. The Japanese management has been very calculative and taken every care and already made a provision for growth and expansion if needed in future. Some of the salient features of the facility are LED lights used, zero discharge of waste, future provisions for solar on the roof top (as and when they intend to cut costs to bring in better operational efficiencies) and also has the ability to conserve water and water harvesting (water saved in monsoon can be used by plant for next 3-5 months. The plant has many large windows to use day light in order to save power. The machines installed are very sophisticated, as per estimates approximately 3-4 people are sufficient to monitor 10 machines; thus, the cost of production is therefore reduced. The Japanese Management (which is nearly 73.7% of the shareholdings holding) will try to introduce their culture of Kaizen and JIT; so we are looking at cost cutting, better operationally efficiencies and more automation.

One must also note that the company currently maintains 29 depots which shall come down to nearly 5 to 6 depots post implementation of GST. This will also contribute to the cost savings in operation of depots and enable huge savings in logistics of the company. The plant will consolidate and help enable localization of manufacturing in one place. This will also lead to logistics benefits. Integrated manufacturing at a single site would reduce the production cost owing to reduced transportation cost and enhanced shop- floor efficiency. All these factors will further strengthen the belief of cost reductions which appears to be an icing on the cake.

Patalganga plant is anticipated to be an absolute game changer for the company. One can expect nearly 200 products to be launched in next 3-4 years (off course by reworking, re-designing or new packaging).
The company has five plants. There is a possibility that the company will try to close down the plants which are a cost to the company and affect the bottom-line. In this sight, the plant in Vasai is on lease and a bright candidate for possible shut down. Needless to mention, if the same occurs, one might see onetime expenses like financial charges, VRS etc. The investment in the Patalganga plant is a part of the long term strategy to have a stronger foundation for growth and expansion in future. This is the biggest plant from the stable of Kokuyo not only in India but all over the world. This plant can help open vista for exports to the neighbouring nations and then to the Asian markets. This can be a blend of Make in India and also revive the GOI focus on Manufacturing and promoting exports.

(B) Market– Itself is a Trigger:

In India, there is huge scope for improvement in the education sector. There is a large population of adult illiterates in the country. In addition to this, the number of enrollments in the basic education is also growing on a constant rate since last 3-5 years. In the budget for FY17-18, the government had increased the educational allocation for the sector by 9.9% to approximately Rs796bn. The GOI has laid more emphasis on educating the girl child which will also be in line with the objective of empowering Women in India. Moreover, the shift to the organized sector will also benefit KCL. Overall, the industry itself is providing a lot of opportunities for growth which is line with the triggers shown in the current Indian market scenario.

Kokuyo Camlin has a legacy of being associated with schools, offices and other stationery related segments through its superior quality in innovative and niche products. The company maintains its leadership position in the segments of arts & hobby materials, scholastics products, school products, artistic products, office stationery etc. The portfolio of products offered by the company caters to masses as well as the classes i.e. the mass segment as well as the premium segments. Kokuyo Camlin aims to attain leadership position in key categories like crayons, water colours, mechanical pencils, geometry boxes, markers etc. In the long term, the company intends to strengthen its portfolio and gain market share in the pen and notebook segment as well. In the current scenario, the management believes that the market for notebooks is very good. New books with Kokuyo technology have been received very well in market. Management is anticipating this wing to perform much better in the next 1-2 years.

For the company to maintain the growth momentum, launching new products in the market is very critical. Some of the best innovative and the first in the industry products are launched by Kokuyo Camlin. Some of the products launched recently were Camel Gel Crayons, Kokuyo Square glue Sticks, 2mm Mechanical Pencils, Foldable Scale etc.

The strength of the company lies in its sales force; the company has a sales team which is IT-enabled and empowered. The company intends to further strengthen and empower the sales force. It has a robust pan-India distribution network. KCL has more than 2000 stock keeping units (SKUs). The company has planned 40-50 new SKUs for the current financial year. They also cover the modern distribution channels like those of online stores, partnering with e-commerce etc., to further penetrate the market. In addition to this, as a part of the long term strategy, the company continues to invest in technology. Management believes investment in IT and Technology is critical to steer them in the right direction to improve every aspect of operations. The acquisition acts as a boon to control the synergies of Kokuyo and Camlin via a combination of R&D capabilities of Kokuyo and strong brand name of Camlin. In the past, Camlin has launched a wide range of products catering to Indian markets and so will the synergy also continue the legacy.

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INVESTMENT RATIONALE (contd.)

(C) Kokuyo Camlin - The Joint Venture

Camlin has a rich legacy and a proud history in the products they have existed in. The company is as old as 8 decades when its operations began in 1931 by manufacturing Horse Brand Ink powders and tables followed by Camel Ink which lead to the creation of the brand Camlin (created from the words Camel + Ink = Camlin) in early 1946. From there on, Camlin expanded and diversified into various segments of art materials, scholastic materials, hobby materials, office stationery products, corporate gifts etc. Camlin has more than 2100 products in their basket.

Products

Students
- Adhesives
- Brush Pens
- Cartridge Fountain Pen
- Clay and Dough
- Color Pens & Pencils
- Drawing Books, Notebooks
- Fountain Pens & Ink
- Plastic & Gel Crayons
- Geometry Box & Accessories
- Gift Sets and Kits
- Mechanical Pencils & Leads
- Pastels
- Pens, Pencils & Pals
- Sketch Pen
- Student poster colours, Water Colour cakes &Tubes
- Technical Instruments
- Washable & Wax Crayons

Office Professionals
- Correction Pens
- Gum and Paste
- Markers & Marker Inks
- Office products accessories

Artists and Designers
- Art Materials
- Artist's Pastels
- Artist's Water Colours
- Artists Acrylic Colour
- Artists Oil Colour
- Brushes
- Canvas
- Drawing Inks
- Drawing Pencils/Charcoal
- Others Art Materials
- Painting Mediums
- Premium Bi-Colour Pencils
- Premium Colour Pencils
- Premium Poster Colours
- Students' Oil Colour
- Water Colour Pencils

Hobbyists
- Fabrica 3D Glitter
- Fabrica Colours
- Fabrica Coneliner
- Hobby Brushes
- Hobby Mediums
- Sparkle Colours

Source: Company

Like Camlin, the Kokuyo group- a Japanese business house has a legacy of more than a century. The group was founded in 1905 in Osaka, Japan. From book-cover makers for "Wacho" (Traditional Japanese Account Book), the companys' main product lines now include office stationery notebooks, office supplies and office furniture. The Kokuyo group has its businesses spread across Asia & Europe and has offices in China, Hong Kong, Thailand, Singapore, Malaysia, Vietnam etc. The controlling stake in Camlin Limited was acquired by Kokuyo S&T Co. Ltd., a wholly owned subsidiary of Kokuyo Company Limited in May 2011. The aim of the synergy was to blend the expertise, reach and brand equity of Camlin along with Kokuyo's R&D for new innovative (office stationery) products and capitalize on its strong presence in the Asian market. The synergy was created to strengthen the success in the stationery business. Brand name- Camlin is the biggest Asset for the company.

Financials:

In the past (FY16-17), the company was compelled to reduce the price of the products and could grow only via volumes. The management has an ambitious vision to be a debt free company in next 3-5 years. The management's vision is simple and straightforward to strengthen their portfolio and gain market share. Due to the implementation of GST, the effective rate has come down to 16.6% from 16.8% earlier (assuming the sales mix is kept constant). Currently, the company is growing through volumes growth; the next trigger for increasing profits could be by taking a price rise of nearly 2-3%. In times to come, the Management will strengthen its performance with focus on optimum levels of inventory, operating efficiencies and cost savings.

Risks and concerns:

The product pricing is significantly driven by the prices of crude oil and petrochemicals which is also the key raw material for stationery manufacturing. Threat of entry of new players is always there in this business. Cost of importing certain products like erasers, sharpeners and pencils is lower as compared to manufacturing in India. The business is cyclical in nature.

Outlook and valuations:

The company's brand name has an emotional connect with its end users. Management is very optimistic with the commencement of the new plant. It believes this could be a game changer for company. Considering the commencement of the new plant recently, FY2017-18 is most likely to be a year of consolidation; however, some green shoots are already visible and the effect of new facility has started getting reflected in the numbers for the quarterly results. Some of the macro economic factors like ease of doing business, GST via logistics will be beneficial for the company. During the entire year, there will be a movement of production of products from other plants to the new plant. This movement is anticipated with minimal disruption as the capacity is already created in new plant. All in all, this year appears to be a year of consolidation for the company. Moreover, the company is investing time in training the workers for the new equipments. KCL is preparing to kick start the future operations and the real impact will be seen from next year (FY18-19) when all processes are shifted and manpower is adequately trained. As the stock is grossly under-owned by MFs and FIIs; there could be a possibility of buying spree by institutions with increase in visibility. We initiate a BUY on the stock with a target of Rs175 over a horizon of 12 months.

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