

CMP : Rs. 1,070

Target : Rs. 1,740

Date : 10th September 2018

Sadhana Nitro Chem Ltd (SNCL) reported a topline of Rs. 65.82 crores against Rs. 51.39 crores in Q4 FY18, registering a growth of 28%. EBITDA grew by 78% to Rs. 34.78 crores in Q1 FY19 vs Rs. 19.52 crores in Q4 FY18.

SNCL reported a Rs. 22.32 crores in Q1 FY19 against Rs. 21.86 crores in Q4 FY18 reporting a growth of 2.10% mainly on account of one time increase in finance cost of Rs. 8.90 crores. The interest cost includes premium on redemption non cumulative non convertible preference share amounting to Rs. 7.68 crores.

We opine to **BUY** the stock and assign a target price of Rs. 1,740 based on a PE multiple of 6.2x FY20 earnings estimate implying an upside of 62% from the CMP of Rs. 1,070

	Q1 FY19	Q1 FY18	Y-o-Y Growth %	Q4 FY18	Q-o-Q Growth %
Gravita India Ltd Q4 FY18 Abridged Results (In Rs Cr)					
Gross Revenue	65.82	15.27	331.04%	51.39	28.08%
Gross Profit	48.96	7.56		37.00	
GPM %	74.38%	49.51%		72.00%	
Expenses	31.04	13.37		31.87	
EBITDA	34.78	1.90	1730.53%	19.52	78.18%
EBITDA %	52.84%	12.44%		37.98%	
Depreciation	0.58	0.47		0.46	
EBIT	34.20	1.43		19.06	
Interest	8.90	1.42		1.37	
PBT	25.30	0.01	252900.00%	17.69	43.02%
Tax	3.24	0.00		-4.05	
PAT	22.32	0.60	3620.00%	21.86	2.10%
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Business Overview

Established in 1973 as a nitrobenzene producer, Sadhana Nitro Chem Ltd (SNCL) has over the years transformed into producing high quality chemical intermediates. SNCL has one manufacturing plant located at Roha, about 135 kms from Mumbai with the capacity of producing 2000 MT of MAP (Meta Amino Phenol) and 250 MT of colourformers ODB 2 along with other intermediaries. The primary product nitro benzene is 100% used for captive consumption as a feed-stock for other products such as MAP, colourformers, aniline, metanilic acid, butane tetra carboxylic acid, diethyl sulphone and others.

Headed by Mr. Asit Javeri (Chairman) and Mr. Abhishek Javeri (MD & CFO) SNCL has a well-knit market network in countries like US, Europe, Japan, Korea, and South-East Asian countries. The company exports constitute ~ 72% of the overall sales in Q1 FY19.

Products

1. MAP - Meta Amino Phenol (~71% of FY18 revenue and ~ 49% of Q1 FY19 revenue)

MAP is an intermediary used in cosmetics, aerospace, military applications, pharmaceutical, agro chemicals and other small applications. With the current capacity of producing 2000 MT p.a. of MAP, SNCL is expanding its capacity to produce 3000 MT p.a. of MAP by end of FY19. De-bottlenecking of production facility will enhance the production capacity to 2400 MT p.a. by November 2018 following which brown-field capital expenditure of Rs. 60Cr shall further increase the capacity to 3000 MTPA.

2. Colourformers ODB 2 (20% of revenue in Q1 FY19)

SNCL has resumed the manufacturing of colourformers, a performance chemical with the capacity of 250 MT p.a. There were no colourformers sold in FY18. Colourformer is the key raw material for the coating of thermal paper and is a derivative of MAP. Thermal papers are used in credit-card billing machines, adding machines, cash registers & growth in usage of cards have aided SNCL to restart the production of colourformers. SNCL plans to double its capacity to 500 MT p.a. by October 2018.

Key highlights

1. Slow-down of competitors due to environmental norms , Growing MAP demand scenario & constrained supply side.

There are 4 major manufacturers of MAP globally and SNCL is the only major producer based in India. Hebei Jianxin and Shouguang Fukany are core competitors of SCNL based out of china & one another competitor with a small capacity catering only to the domestic market is present in Japan. The competitors are facing slow-down in production on account of stringent environmental / pollution control norms by the Chinese government. The Chinese counterparts have been manufacturing for just over a decade at a lower cost that SCNL without the relevant pollution and effluent treatment. The Japanese counterpart only manufactures MAP for the domestic consumption and has insignificant effect on the global supply and demand scenario. Coupled with recent crackdown, the application of MAP has increased from 4-5 industries to nearly 12 industries over a period of time whereas the supply side has not seen any major expansions.

2. MAP spot prices have quadrupled (4x) in under 8 months, with no significant change in input costs.

SNCL's Q1 FY19 MAP realisations were at ~\$20 per Kg or ₹ 1,300 per Kg which used to be \$8 - \$10 per Kg a year ago. Our research suggest that the weighted average prices for MAP have risen further to ~ \$26 per Kg with some spot contracts being executed at as high as ~ \$35 per Kg. Management has confirmed to some contracts happening at high levels but on spot basis. Around 10% of the contracts are legacy contracts (1 year contracts) at older prices while most contracts are quarterly contracts with the remaining contracts taking place at spot prices helping SNCL achieve higher realization. The total market size for MAP is ~ 7000 MT p.a. of which SNCL wants to cater to nearly 40% of the market.

3. Entering New Product – Colourformers OBD 2

SNCL had commissioned to manufacture colourformer in 2005 to cater to the paper industry however, it was stopped later. SNCL resumed the production of colourformers in Q1 FY19. With the capacity to produce ~ 250 MT p.a. of colourformers, SNCL's capacity utilization in Q1 FY19 stood at ~ 58% with plans of doubling the capacity by October to 500 MT p.a. The realization in Q1 FY19 stood at ~ ₹ 3,500 per Kg while our research suggests that the prices are on a rise to close to ~ ₹ 3,900 per Kg. Various different thermal paper colourformers contribute to a global market size of over 10,000 tons and growing, with less than 10 manufacturers in the world.

Risk

1. Falling MAP/Colourformer prices
2. Revamp of Chinese counterparts
3. Entering non-core business –(Strix Wireless Systems Ltd, a 100% subsidiary)

Financials

Income Statement (RS CR)	FY 17	FY 18	FY 19E	FY 20E
Total Revenue	55.64	110.77	400.60	637.32
COGS	26.62	40.44	93.67	160.78
Gross Profit	28.53	70.11	305.62	472.54
GPM	51.73%	63.42%	76.54%	74.61%
Employee Expenses	7.88	9.75	32.49	40
Other Expenses	12.51	25.58	37.52856	53.17258
Total Expenses	47.01	75.77	163.69	253.95
EBIDTA (Incl other income)	8.63	35	236.91	383.36
OPM (Incl other income)	15.51%	31.60%	59.14%	60.15%
Depreciation	1.92	1.88	2.53	3.75
PBIT	6.71	33.12	234.38	379.61
Finance Expenses	6.33	4.84	13.4	6
PBT	0.38	28.28	220.98	373.61
Taxes	0	-3.09	61.86314	112.0841
Tax %	0.00%	-10.93%	28.00%	30.00%
PAT	0.38	31.37	159.12	261.53
PAT Margin (%)	0.68%	28.32%	39.72%	41.04%

Valuation

Sharp increase in MAP prices, restarting colourformers ODB 2 production and increasing MAP capacities by 50% would help expand the PAT going forward. Assuming MAP prices sustaining at \$26 per Kg and colourformer prices at ~ ₹ 3,900 per Kg on a going concern basis, we expect Sadhana Nitrochem Ltd to report a PAT of Rs. 159.12 crores in FY19 and Rs. 261.53 crores in FY20. At the current share price of Rs. 1,070 Sadhana Nitrochem is trading at 3.81x FY20 estimates. We recommend to **BUY** the stock with a target price of Rs. 1,740 assigning a PE multiple of 6.2x FY20 earnings estimate with an EPS of 280x in next 12 – 18 months.

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