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Company update and
earnings and TP revision

Specialty Chemicals

Target price: Rs3,000

Earnings revision

(%)	FY22E	FY23E	FY24E
Revenue	↓ 8.4	↓ 0.3	↑ 6.5
EBITDA	↓ 20.3	↓ 5.6	↑ 3.3
PAT	↓ 14.7	↓ 5.8	↓ 3.5

Target price revision

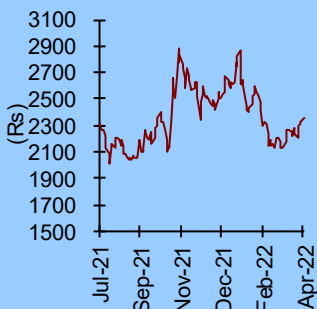
Rs3,000 from Rs3,110

Shareholding pattern

	Jun '21	Sep '21	Dec '21
Promoters	79.2	79.2	79.1
Institutional investors	9.6	10.9	10.8
MFs and others	3.4	6.8	7.5
Banks /FIs	1.6	0.0	0.0
Insurance Cos.	0.5	0.6	0.3
FIs	4.1	3.5	3.0
Others	11.2	9.9	10.1

Source: BSE

Price chart



Tatva Chintan Pharma Chem

BUY

Maintained

Rs2,348

Durable growth in niche chemistries

We hosted promoters of Tatva Chintan Pharma Chem – Mr. Chintan Shah and Mr. Shekhar Somani for investors meeting. The management expects growth in SDAs to continue, and opportunities are increasing for emission control beyond transport vehicles. Tatva Chintan should grow faster from new customer wins, and likely supply to developed market for Euro-7. It has cracked products that are high in purity, and has found application in semi-conductor industry. Super-capacitor batteries are being commercially launched which should drive growth for electrolyte salt. PASC will benefit from the knowledge of continuous flow chemistry, and the company is already in the process of commercialising products. It has reiterated its sustainable EBITDA margin guidance of 22-24%, and Dahej plant commissioning by Nov/Dec'22.

We have cut our EPS estimates by 15% for FY22 on lower SDA sales (on chip shortage) and by 4-6% for FY23-24E. We forecast revenue / EPS CAGR of 31% / 28% over FY22-24E. Accordingly, we cut our target price to Rs3,000 (from Rs3,110, 40x FY24E EPS). Maintain BUY. Our estimate does not completely capture the rising opportunities in semi-conductor industry and PASC.

SDA market remains exciting

- ▶ Tatva Chintan estimates SDA opportunity at 24-30ktpa for auto emission; the other next big segment is refining. The growth in auto is from NOx reduction which has been driven by the implementation of Euro-6 equivalent norms in India (BS-6) and China (China emission norm 6a). Tatva Chintan has market share of ~12-15% in emission control SDAs and SACHEM is the market leader.
- ▶ The high-entry barriers are technology (electrolysis process in organic chemistry) and long approval cycle. It does not anticipate any new entrant in the foreseeable future, thus, the industry will continue to remain only two-players market.
- ▶ For Tatva Chintan, SDAs for auto emission control are ~80% of SDA revenue of which ~80% comes from large commercial vehicles. Rest of SDA revenue comes from zeolites which find uses in petrochemicals refining, continuous flow chemistry etc.
- ▶ In near term, demand for SDAs has been impacted by chip shortage, but the company remains confident of achieving growth on normalisation.
- ▶ It has recently won a large customer for auto emission SDA in the US, and is in the process for approval from another large European customer. Tatva Chintan currently supplies to one Japanese, European and Chinese customer each. Globally, there are nine large zeolite manufacturers (which includes BASF, Clariant, Tosoh, PIDC and others) and four catalyst manufacturers (BASF, Clariant, Johnson Matthey and Umicore). Technology for emission control is controlled by catalyst manufacturers.

Market Cap	Rs52.1bn/US\$685mn	Year to Mar	FY21	FY22E	FY23E	FY24E
Bloomberg	TATVA IN	Revenue (Rs bn)	3.0	4.6	5.9	7.9
Shares Outstanding (mn)	22.2	EBITDA	0.7	1.1	1.6	2.2
52-week Range (Rs)	2878/1083	Rec. Net Income (Rs bn)	0.5	1.0	1.3	1.7
Free Float (%)	20.9	EPS (Rs)	26.0	45.5	56.6	75.0
FII (%)	3.0	P/E (x)	90.3	51.6	41.5	31.3
Daily Volume (US\$'000)	2,897	CEPS (Rs)	29.4	49.4	64.1	86.2
Absolute Return 3m (%)	(8.8)	EV/E (x)	73.1	46.2	32.2	23.8
Absolute Return 12m (%)	NA	Dividend Yield (%)	0.1	0.4	0.5	0.8
Sensex Return 3m (%)	0.1	RoCE (%)	21.9	23.4	20.2	23.3
Sensex Return 12m (%)	23.7	RoE (%)	36.8	31.6	24.0	26.2

Please refer to important disclosure at the end of this report

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SDA revenue growth to sustain

- ▶ SDA (for emission control) revenue growth would be driven by **1)** rising requirement for controlling harmful emission in auto. It is expected that Euro-7 (and equivalent norms) will focus on reducing NxO along with NOx. This means each catalyst will require 40% more zeolite / SDAs; **2)** NOx reduction by sea-vehicles has been notified and enforcement of these norms will drive demand. Demand from sea-vehicles could be very large; and **3)** other construction and farming vehicles may see similar stringent emission norms as transport vehicles.
- ▶ The emission regulation for industrial equipment (such as DG set, CPP etc) is very liberal (>100PPM vs <5PPM for auto) and if stringent regulations are enforced, then industrial equipment may also adopt catalyst based emission control system. This may open a new market for SDAs.
- ▶ Further, Tatva Chintan SDA revenue will benefit from winning new customers and supplies to developed market on implementation of Euro-7 norms. It missed developed market Euro-6 implementation as its SDA was approved only in CY15. Tatva Chintan is already supplying few quantities of SDAs for zeolites which will go in catalyst meeting requirement of Euro-7.
- ▶ Shift to EV is mostly in passenger vehicles, and commercial vehicles may take more time for EV transition. Tatva Chintan's customers are expanding capacity for emission control zeolites which provide comfort for its investment.

Opportunity in semi-conductor industry from high purity SDAs like products

- ▶ SDAs have purity of <5PPM; Tatva Chintan is testing products which have purity of <10PPB which find application in semi-conductor and printed circuits industry.
- ▶ It is difficult to achieve this purity on industrial scale, and the company said it has manufactured products at lab scale ahead of its estimated schedule. The break through establishes its focus on R&D and its capabilities; and opens up another niche market.

Electrolyte salt – auto and solar application had few commercial launches

- ▶ Super-capacitor batteries had few commercial launches in hybrid batteries for EVs and storage of renewable energy. It helps improve the life of lithium-ion batteries in EV by supplementing for burst in current release for acceleration, and allied applications. Lithium-ion batteries' performance is best when vehicle is in steady motion, but it deteriorates in case of sudden current release for acceleration, breaking etc. Super-cap can release and absorb current at a high voltage.
- ▶ Super-cap battery integration reduces total battery capacity requirement for storing solar power generation. First project by a US company is under implementation and if successful, it will open large market for super-caps.
- ▶ Electrolyte salt used in super-cap is an organic salt, unlike inorganic salt used in lithium-ion batteries. The product is forward integration of SDA for Tatva Chintan.
- ▶ There are three manufacturers of electrolyte salt for super-cap which find application in EV where two peers are Chinese. It is the sole supplier for solar power storage batteries under implementation.

PASC – R&D pipeline strong

- ▶ Tatva Chintan is exploring new product development under continuous flow chemistry, and thereby, increase its addressable market. The criteria for product selection under PASC is **1)** the peak opportunity should be at least Rs1bn; **2)** at least one step should be continuous flow chemistry; **3)** scope for improving efficiency and lowering total cost of product.
- ▶ The first product under consideration is monoglyme which is used as a solvent in pharmaceuticals and as a solvent to dissolve electrolyte salt in lithium-ion battery.

It is amongst the four solvents used in making electrolyte solution for lithium-ion batteries, and the biggest product in the family is dimethyl carbonate.

- ▶ Company currently makes 700-800tpa glyme through conventional route, and new capacity using continuous flow planned is 2.5-3ktpa.
- ▶ It has two products each for pharmaceuticals and agro-chemicals intermediates under development. Of these, two products have been successfully tested at lab levels, and plans are underway for a commercial setup.

Guidance reiterated.

- ▶ Management has reiterated sustainable EBITDA margin guidance at 22-24% in the long run.
- ▶ Capex in Dahej of Rs1.5bn will be commissioned by Nov / Dec'22. The asset turnover at peak will be 3x; likely to fully utilise plant in 3-3.5 years. The facility will have the debottlenecking opportunity if required for interim growth.
- ▶ Company has bought fresh land parcel in Dahej for unit 4; it expects EC in next 12-15 months. The land will be available FY24 onwards for building chemical facilities.

Table 1: Revenue and EPS CAGR of 38% / 42% over FY21-24E

Rs mn	FY18	FY19	FY20	FY21	FY22E	FY23E	FY24E	CAGR (%) FY21-24E
PTC	640	864	749	816	988	1,108	1,469	21.6
SDA	198	254	1,017	1,202	2,513	3,365	4,332	53.3
Electronic chemicals	9	32	46	30	73	111	171	77.8
PASC	490	875	765	912	1,033	1,265	1,935	28.5
Revenue	1,358	2,063	2,632	3,004	4,643	5,886	7,945	38.3
Gross profit	647	921	1,305	1,510	2,576	3,225	4,224	40.9
GPM (%)	47.7	44.6	49.6	50.3	55.5	54.8	53.2	
Operating cost	418	583	755	853	1,463	1,625	2,060	34.2
EBITDA	229	338	550	657	1,112	1,601	2,164	48.8
EBITDA (%)	16.9	16.4	20.9	21.9	24.0	27.2	27.2	
Tax	67	69	98	84	100	275	365	63.0
ETR (%)	35.4	25.7	20.6	13.9	9.0	18.0	18.0	
Adj. PAT	123	198	378	523	1,008	1,254	1,663	47.1
PAT (%)	9.0	9.6	14.4	17.4	21.7	21.3	20.9	
EPS	6.1	9.9	18.8	26.0	45.5	56.6	75.0	42.3
Growth (%)		61.1	90.9	38.3	74.8	24.4	32.6	
Gross Block	474	611	1,104	1,262	1,562	3,062	3,512	40.7
GB turnover (x)	2.86	3.38	2.39	2.38	2.97	1.92	2.26	
Fixed assets	670	727	1,161	1,303	2,168	2,851	3,063	33.0
Working capital (ex cash)	416	717	859	1,227	1,903	2,428	3,300	39.1
Cash conversion (days)	88	97	113	140	141	142	143	
Total assets	1,086	1,444	2,020	2,529	4,071	5,279	6,362	
Net debt	479	614	799	849	(668)	(464)	(628)	
Other liabilities	16	33	45	21	21	21	21	
Equity	591	797	1,177	1,660	4,719	5,722	6,970	
Total liabilities	1,086	1,444	2,020	2,529	4,071	5,279	6,362	
CFO	127	290	480	621	1,013	1,325	1,799	42.6
% of EBITDA	55.2	85.8	87.3	94.5	91.0	82.8	83.1	
Change in WC	(1)	(217)	(226)	(378)	(676)	(526)	(871)	
CFO (after WC)	126	74	253	243	337	800	928	
Capex	(180)	(98)	(482)	(210)	(952)	(850)	(460)	
FCF	(54)	(24)	(229)	33	(615)	(50)	468	
% of revenue	(4.0)	(1.2)	(8.7)	1.1	(13.2)	(0.9)	5.9	
post-tax ROCE (%)	12.2	16.3	21.8	21.9	23.4	20.2	23.3	
ROE (%)	22.6	29.6	38.3	36.8	31.6	24.0	26.2	

Source: Company data, I-Sec research

Table 2: Earnings revision

Rs mn	Revised			Earlier			Change (%)		
	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E
Revenue	4,643	5,886	7,945	5,071	5,905	7,462	(8.4)	(0.3)	6.5
Gross profit	2,576	3,225	4,224	2,859	3,262	4,161	(9.9)	(1.1)	1.5
GPM (%)	55.5	54.8	53.2	56.4	55.2	55.8			
EBITDA	1,112	1,601	2,164	1,396	1,695	2,238	(20.3)	(5.6)	(3.3)
EBITDA (%)	24.0	27.2	27.2	27.5	28.7	30.0			
PAT	1,008	1,254	1,663	1,182	1,332	1,723	(14.7)	(5.8)	(3.5)
EPS (Rs)	45.5	56.6	75.0	53.3	60.1	77.7	(14.7)	(5.8)	(3.5)

Source: Company data, I-Sec research

Financial summary

Table 3: Profit & loss statement
(Rs mn, year ending March 31)

	FY21	FY22E	FY23E	FY24E
Operating Income (Sales)	3,004	4,643	5,886	7,945
Gross profit	1,510	2,576	3,225	4,224
<i>Gross profit margin (%)</i>	<i>50.3</i>	<i>55.5</i>	<i>54.8</i>	<i>53.2</i>
Operating Expenses	853	1,463	1,625	2,060
EBITDA	657	1,112	1,601	2,164
<i>% margins</i>	<i>21.9</i>	<i>24.0</i>	<i>27.2</i>	<i>27.2</i>
Depreciation & Amortisation	67	86	167	248
Net Interest	42	37	28	19
Other Income	59	119	125	131
Recurring PBT	607	1,108	1,530	2,028
Add: Extraordinaries	-	-	-	-
Less: Taxes	84	100	275	365
- Current tax				
- Deferred tax				
Share from JV/associate				
Net Income (Reported)	523	1,008	1,254	1,663
Recurring Net Income	523	1,008	1,254	1,663

Source: Company data, I-Sec research

Table 4: Balance sheet
(Rs mn, year ending March 31)

	FY21	FY22E	FY23E	FY24E
Assets				
Total Current Assets	1,845	4,153	4,510	5,736
<i>of which cash & cash eqv.</i>	<i>53</i>	<i>1,371</i>	<i>966</i>	<i>930</i>
Total Current Liabilities & Provisions	565	880	1,116	1,506
Net Current Assets	1,280	3,274	3,394	4,230
Investments	-	-	-	-
<i>of which</i>				
Strategic/Group	-	-	-	-
Other Marketable	-	-	-	-
Net Fixed Assets	1,303	2,168	2,851	3,063
Goodwill				
Total Assets	2,583	5,442	6,245	7,293
Liabilities				
Borrowings	902	702	502	302
Deferred tax liability	21	21	21	21
Other financial liabilities	-	-	-	-
Equity Share Capital	201	222	222	222
<i>Face Value per share (Rs)</i>	<i>10.0</i>	<i>10.0</i>	<i>10.0</i>	<i>10.0</i>
Reserves & Surplus	1,459	4,497	5,500	6,748
Net Worth	1,660	4,719	5,722	6,970
Total Liabilities	2,583	5,442	6,245	7,293

Source: Company data, I-Sec research

Table 5: Quarterly trend
(Rs mn, year ending March 31)

	Mar-21	Jun-21	Sep-21	Dec-21
Net sales	1,087	1,068	1,236	1,047
% growth (YoY)	-	107.3	105.9	30.6
EBITDA	245	258	359	238
Margin (%)	22.5	24.2	29.0	22.7
Other income	26	30	28	47
Add: Extra ordinaries	-	-	-	-
Net profit	211	231	324	228

Source: Company data

Table 6: Cashflow statement
(Rs mn, year ending March 31)

	FY21	FY22E	FY23E	FY24E
Operating Cash flow	621	1,013	1,325	1,799
Working Capital Changes	(378)	(676)	(526)	(871)
Capital Commitments	(210)	(952)	(850)	(460)
Free Cash Flow	33	(615)	(50)	468
Cash flow from Investing Activities	(0)	119	125	131
Issue of Share Capital	-	2,253	-	-
Inc (Dec) in Borrowings	(4)	(200)	(200)	(200)
Dividend paid & Others	(84)	(239)	(279)	(435)
Chg. in Cash & Bank balance	(55)	1,317	(405)	(36)

Source: Company data, I-Sec research

Table 7: Key ratios
(Year ending March 31)

	FY21	FY22E	FY23E	FY24E
Per Share Data (in Rs.)				
Recurring EPS	26.0	45.5	56.6	75.0
Reported EPS	26.0	45.5	56.6	75.0
Recurring Cash EPS	29.4	49.4	64.1	86.2
Dividend per share (DPS)	2.1	9.1	11.3	18.8
Book Value per share (BV)	82.6	212.9	258.1	314.4
Growth Ratios (%)				
Operating Income	14.1	54.6	26.8	35.0
EBITDA	19.6	69.3	43.9	35.2
Recurring Net Income	38.3	92.9	24.4	32.6
Diluted Recurring EPS	38.3	74.8	24.4	32.6
Diluted Recurring CEPS	38.5	68.1	29.9	34.4
Valuation Ratios (x)				
P/E	90.3	51.6	41.5	31.3
P/CEPS	80.0	47.6	36.6	27.2
P/BV	28.4	11.0	9.1	7.5
EV / EBITDA	73.1	46.2	32.2	23.8
EV / Operating Income	16.0	11.1	8.8	6.5
	1,449.			
EV / Operating FCF	3	(103.5)	696.2	85.9
Operating Ratio				
Other Income / PBT (%)	9.8	10.7	8.1	6.5
Effective Tax Rate (%)	13.9	9.0	18.0	18.0
NWC / Total Assets (%)	47.5	35.0	38.9	45.2
Inventory Turnover (days)	87.5	88.0	88.5	89.0
Receivables (days)	110.3	110.8	111.3	111.8
Payables (days)	57.7	58.2	58.2	58.2
Net Debt/EBITDA Ratio (x)	1.3	(0.6)	(0.3)	(0.3)
Capex % of sales	7.0	20.5	14.4	5.8
Return/Profitability Ratio (%)				
Recurring Net Income Margins	17.4	21.7	21.3	20.9
RoCE -post tax	21.9	23.4	20.2	23.3
RoIC	22.6	28.5	25.2	27.1
RoNW	36.8	31.6	24.0	26.2
Dividend Yield	0.1	0.4	0.5	0.8
Gross Margins	50.3	55.5	54.8	53.2
EBITDA Margins	21.9	24.0	27.2	27.2

Source: Company data, I-Sec research

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