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Chemical Sector - Catalytic Substitution in Play

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Thematic
Chemical Sector

Catalytic substitution in play

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The Indian Chemical Industry is presently positioned in front of a set of developments that would result in strong growth opportunities in both the overseas and the domestic markets for Indian players. Strong demand from downstream industries and a trend of shift in supply chain from China are the key factors to watch out as part of this tailwind. While COVID-19 has temporarily impacted the demand side of the equation for a few end-industries, we believe that this is a minor deviation in the long term story which would normalize over some period of time.

'Shift from China' could augur well for Indian chemical manufacturers

While China is a behemoth in global chemical manufacturing, constituting ~39% of market share, supply chain disruptions which happened over the last few years – due to reduction in capacities as a fallout of increasing environmental compliance of chemical facilities, trade war with the United States, and off-late the COVID-19 crisis led lockdowns – could increasingly prompt global players to de-risk their sourcing strategy to other countries.

We believe that India's low manufacturing cost structure could aid in grabbing a share of this pie, particularly in the specialty chemicals side which already form a significant share of our exports. Players in specialty chemicals, and those in the contract research/manufacturing could particularly benefit. Additionally, we think chemical companies who have already forged strong relationships with global players would see more engagements on the back of their technical capabilities and track record.

Improving downstream demand opens up room for import substitution

Domestic manufacturers have also shown intent of sourcing raw materials locally and government impetus for chemical and pharmaceutical manufacturing could open opportunities for import substitution. Several players have already undertaken capacity expansion for such chemicals. Additionally, we think that vertically integrated companies would be able to manage raw material price volatilities in a better manner.

Ways to play the growth in the chemical sector

We believe that companies exposed to pharmaceutical and agrochemical industries, which appear to be bright spots, could provide good investment opportunities. Additionally, strong technical and technological expertise and track record in the export markets would bode well for long-term growth. However, given the strength in business model and earnings visibility of a few such companies, valuation levels may fairly represent the growth and the play will be mostly on their earnings momentum.

We think players like SRF (BUY), PI Industries (Tactical BUY), Navin Fluorine International (initiating coverage with a BUY) and Aarti Industries (Tactical BUY) are well placed to capitalize on the overseas demand of specialty chemicals in their respective niches. Balaji Amines (BUY) and Deepak Nitrite (BUY) are plays for the domestic import substitution theme.

Date: June 18, 2020

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Valuation

	CMP	Market Cap	PE (x)		EV/EBITDA (x)		ROACE (%)	
	INR	INR Cr	FY21E	FY22E	FY21E	FY22E	FY21E	FY22E
Aarti Industries	935	16292	29.7	21.2	16.4	12.1	16.2	18.9
Balaji Amines	445	1431	11.4	9.8	7.4	6.4	24.4	24.8
Deepak Nitrite	463	6313	11.3	10.2	7.5	6.6	25.2	22.2
Navin Fluorine	1602	7921	38.0	26.7	23.7	18.1	18.6	21.6
PI Industries	1585	21886	73.9	55.0	53.3	40.0	24.0	28.3
SRF	3621	20815	25.3	19.1	14.8	12.2	13.6	15.3

A. Indian chemicals: Long-term benefits emerge out of short-term disruptions

The Indian chemical sector has been on a strong growth path in recent years and is expected to surpass this going forward. However, the spread of novel coronavirus, or COVID-19, and the ensuing lockdown by the government has cast a shadow on this solid growth story for the near term. The supply chain was in a disarray and the eventual concern is fall in end-user industry demand on the back of recessionary scenarios. As the Indian economy takes the initial steps towards normalization, we evaluate the trends which could be visible over the near-term and longer time horizons in the industry.

As we highlight in the following table, the more defensive end-user segments in the present scenario would be pharmaceuticals and agrochemicals. Pharmaceuticals were classified as essential products from the start of lockdown and hence several domestic companies in the pharma value chain (like Aarti Industries, Alkyl Amines and Balaji Amines) had continued to run their operations. Hygiene and personal care segments would potentially benefit from this trend. Players in this space are Deepak Nitrite (the company has commissioned an Isopropyl Alcohol plant which sees use in hand sanitizers) and Galaxy Surfactants.

Exhibit 1: Pharma and agrochemical sectors will see limited impact on demand

End-user segment	Near-term impact	Comment
Pharmaceuticals		Limited impact on the demand side. Sourcing raw materials from China can be challenging in some cases
Agrochemicals		Limited impact on the demand side. Sourcing raw materials from China can be challenging in some cases
Hygiene and personal care		Demand can be high due to greater focus on hygiene: soaps and hand sanitisers
Flavours and Fragrances, Food additives		Low impact on the demand side. Some discretionary consumption may see softened demand in the short term
Alkali chemicals		Some impact will be visible due to lower demand from glass (used in auto sector), which may be offset by higher demand from detergents
Colourants		Moderate impact may come from lower demand from automobiles and textiles
Polymers and additives		Moderate impact may come from lower demand from auto and aviation segments
Rubber chemicals		Moderate to high impact seen from lower tyre sales to original equipment manufacturers (OEMs), partly offset by replacement demand

Source: Company, Edelweiss Professional Investor Research

Loss of production and challenges on the logistics and manpower front are bound to impact Q1FY21 earnings similar to what we are seeing for Q4FY20. It is worth noting that while loss of production in Q4FY20 was around 10 days, it was longer in Q1FY21 for most companies.

As the sector gets back on its feet, with most companies in our radar resuming manufacturing in early to mid-April (refer Exhibit 2), with required measures in place to ensure safety and well-being of their employees, we believe that this is but a short-term blip in a growth story that will see benefits arising out of the situation. Logistics and supply chain conditions are also improving.

Exhibit 2: Operating status of various companies after imposition of the lockdown

Company	Summary
Aarti Industries	Continued to operate partially in products that are used in the manufacture of essentials
Alkyl Amines	Continued to operate partially in products that are used in the manufacture of essentials
Atul	Resumed operations from mid-April
Balaji Amines	Continued to operate partially in products that are used in the manufacture of essentials
Deepak Nitrite	Resumed operations across facilities from early April. Commissioned plant will be used to manufacture isopropyl alcohol, which is seeing strong demand due to increasing offtake of hand sanitisers.
Fine Organics	Resumed operations from end-March
Galaxy	Resumed operations from early April
Navin Fluorine	Resumed operations from mid-April
NOCIL	Resumed partial operations from early May
PI Industries	Continued to partially operate its plants located at Panoli and Jambusar
SRF	Resumed operations from early-April
Sudarshan Chemical	Resumed operations from early-April
Vinati Organics	Resumed operations from mid-April

Source: Company, Edelweiss Professional Investor Research

In this evolving situation, growth of the defensive sectors to some extent show certainty. Below we highlight commentary by global chemical majors on the ramifications of COVID-19 on their business.

Exhibit 3: Recent commentaries by global chemical players during their Q1CY20 results

Company	Commentaries
BASF	• Some industries such as pharma, cleaning and nutrition are resilient. They are even experiencing additional demand due to measures adopted to address the coronavirus • Industries impacted negatively are construction, electronics, consumer goods, energy, rubber and plastics, transportation and autos • At the end of April, the average plant utilisation rate was still over 60%.
DuPont	• Through April, we continue to see strength in personal protection, water filtration, food and beverage, electronics and probiotics. Autos, oil and gas, and select industrial end-markets continue to suffer
Clariant	• Looking at 2020, Clariant anticipates a negative impact on sales and profitability from the COVID-19 pandemic. • The outbreak is strongly expected to impact from the second quarter of 2020
Bayer	• While COVID-19 led to higher demand, partly due to inventory build-up - and thus an increase in sales at some business units, the restrictions related to the pandemic are adversely impacting parts of the company's business. • Following a positive start to the year, Bayer expects COVID-19 to impact its business over the course of the year. It will not be possible to reliably assess the positive and negative effects until later in the year.

Source: Company, Edelweiss Professional Investor Research

Despite the challenges anticipated in FY21, Indian chemical companies will revert back to their strong growth path over a longer time horizon in our opinion. We evaluate that in our next section.

Tailwind over the longer term emerges for India, more so in specialty chemicals

Owing to the back-to-back supply-side disruptions emerging out of China (first from a stringent environmental protection regime, which resulted in closure of capacities of several chemicals, and then dislocations in the supply chain owing to the COVID-19 situation), global manufacturers are expected to diversify a part of their sourcing from there.

This shift will particularly occur in specialty chemicals, which are low volume, high value products. As China commands ~39% share in the global chemical market, we believe it would be challenging to replicate capacities at a similar level in bulk chemicals in a short span of time. However, a smaller shift from China to India could in itself be beneficial given that the former's global market share is more than 10x that of ours, although, building up capacities to capitalize on the export markets may come with a lead time.

We remain positive on the fact that any shift is a tailwind for R&D driven companies in the specialty chemicals space, who are collaborating with global innovators through contract research/manufacturing/custom synthesis business models. A lower cost base, availability of technically skilled manpower and stronger intellectual property laws position Indian companies as capable partners for global players.

Interestingly, specialty chemicals form the largest share of exports for Indian chemical manufacturers and constitutes more than half of the country's exports. Despite this, India accounts for ~3% of global export value, less than a quarter of what China commands. However, the situation is not as low as in the case of bulk chemicals, implying a better market penetration for Indian players. Agrochemicals, dyes and pigments, and intermediates for active pharmaceutical ingredients (API) are key segments in terms of specialty chemicals being exported.

We think players like PI Industries, SRF, Navin Fluorine and Aarti Industries are well placed to capitalise on this trend, given their track record and existing relationship with global innovators.

Import substitution in domestic market will resolve feedstock insecurity

Indian manufacturers import a large share of their raw materials and API intermediates from China. Disruptions over the last two years have added significantly to the challenges, and we are seeing trends among manufacturers to shift their raw material sourcing to other geographies.

Significant government impetus is visible in this area, outlined by the recent bulk drug policies that emphasizes on development of integrated bulk drug parks for cost efficient production of APIs and production linked incentives for twenty-six chemical synthesis-based APIs. This could in turn bode well for chemical manufacturers in the pharmaceutical value chain. This initiative is similar to the PCPIR initiatives taken by the government. We discuss these in detail in a later section.

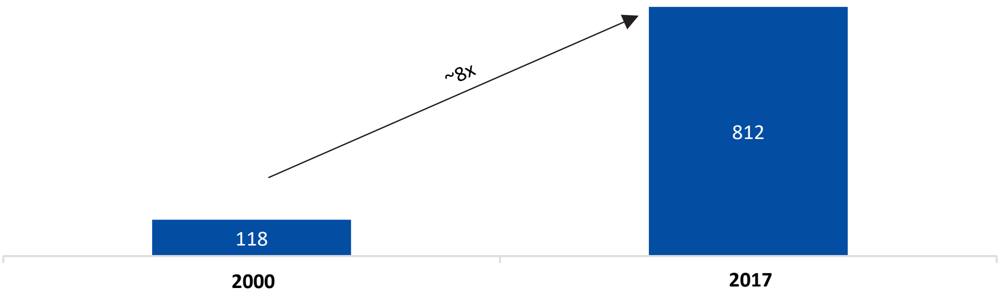
As a response, we see several companies undertaking capex for products which will be import substitutes. Cases in point are players like Deepak Nitrite, Balaji Amines and Vinati Organics who are focusing on import substitutes in the domestic market. We believe that readily available demand and strong relationships with domestic companies will help these companies to harness these opportunities.

Apart from the above-mentioned players, other specialty chemical manufacturers like Aarti Industries, Navin Fluorine and Alkyl Amines can be beneficiaries due to the presence of their products in the pharmaceutical value chain.

B. The 'China' tailwind – India gains from disruptions

Over the last few decades, China had emerged a behemoth in global manufacturing. Its chemical production capacity rose eight-fold since 2000 (Exhibit 4). The sheer size of the country's chemical industry leaves the global supply chain vulnerable to any disruptions arising out of China, which have been frequent in the recent past through various events like environmental protection policies, trade war with the US and the recent lockdowns due to the spread of the coronavirus pandemic.

Exhibit 4: Chinese capacities rose 8x between 2000 and 2017 (in million MT)



Source: UNESCO, Edelweiss Professional Investor Research

These developments would be particularly beneficial for Indian chemical manufacturers, both bulk and specialty chemicals, as it opens up opportunities for import substitution and avenues for export.

I. Spread of coronavirus casts temporary uncertainty on the demand side

Immediate impact of the disruption due to the coronavirus outbreak had been initially cushioned as the spread of infections and subsequent lockdown in China coincided with the holiday period – a period prior to which chemical companies keep enough inventories of intermediates.

However, as Chinese capacities remained shut, sourcing of raw materials emerged a challenge for companies across the globe. As an immediate impact, a few companies (who compete with Chinese companies in their respective product areas) saw increased enquires for their products.

However, as infections spread through the globe, the global supply chain was significantly impacted. In India, with the national lockdown, logistics initially became a challenge for chemical manufacturers who were operating at full/partial capacities as their products in the pharmaceutical chain were declared essential.

However, recent inputs from our channel checks highlight that the scenario has started to improve for both domestic as well as export shipments. The Chinese supply chain has also recovered, and ahead of others as their domestic COVID-19 situation saw normalization.

Exhibit 5: Summary of management commentaries on new sales opportunities arising out of COVID-19

Company	Summary of comments
Aarti Industries	<u>Q4FY20</u> • Revenues from agrochemicals, pharma and FMCG are not expected to see big impact. • Expansions are expected to create significant benefits as India strengthens its position and market share in global supply chains that are increasingly looking to source from fully integrated players with no dependency on China. <u>Q3FY20</u> • Chemical business will benefit as end-product prices are increasing because of China shutdown but no impact on raw material prices because of integrated nature. • API demand will switch to India temporarily, as customers diversify.
Balaji Amines	<u>Q3FY20</u> • There could be opportunities for specialty chemicals like NMP, NEP, Morpholine. As customers might have inventory for 3-4 weeks, post which there might be good opportunity if the situation continues
Deepak Nitrite	<u>Q4FY20</u> • Demand for specialty chemical intermediates is expected to be resilient as reduced demand from established customers and end-user industries is partially replaced by increased demand for intermediates required for products such as pharmaceuticals, agro-chemicals, sanitizers and disinfectants. <u>Q3FY20</u> • Have benefitted from China's environmental protection.
Galaxy Surfactants	• Continuation of the Chinese situation could open up opportunities in international markets like Latin America and Europe.
NOCIL	<u>Q3FY20</u> • Have received enquiries from domestic and international customers on ability to deliver additional volume if asked for though things are yet to materialize.
PI Industries	<u>Q4FY20</u> • Not only due to COVID-19, but for the last 1-1.5 years reshoring is happening from China. PI has got decent enquiries during this time. <u>Q3FY20</u> • China is one of the reasons for increase in demand of existing products and new enquiries.
Sudarshan Chemical	<u>Q3FY20</u> • Looking at several good enquiries, however, too fast to run to a conclusion that this is going to be a long-term or a mid-term kind of opportunity.
Tata Chemicals	<u>Q3FY20</u> • It could be an opportunity for non-Chinese producers, though end industries demand may be a question mark.
Vinati Organics	• ATBS is seeing increased enquiries.

Source: Companies, Edelweiss Professional Investor Research

Companies with integrated business model will be less vulnerable to disruption

Several key Indian chemical companies have developed integrated business models, which will be key to their profitability while shielding them from any sort of disruption that may occur in the value chain. Below we list a few players who have significantly integrated their business:

Exhibit 6: Examples of companies with integrated business models

Company	Business model
Aarti Industries	Integrated business model in the benzene derivatives and the nitrotoluene chains.
Atul	Integrated player across chemistries
Deepak Nitrite	Vertically integrated business across segments. New products (like isopropyl alcohol or IPA) are also forward integration of existing products (acetone)
Vinati Organics	Integrated in the isobutylene and isobutyl benzene value chains. New product butyl phenols are also forward integration of isobutylene

Source: Edelweiss Professional Investor Research

Companies have made headways in diversifying raw material sourcing from China

Given the recent experience, several players have focused on sourcing raw materials from other geographies or have alternative arrangements in place in case of disruptions. In the following table, we list management commentary from listed chemical players during their Q3FY20/Q4FY20 earnings conference calls or recent meetings and interviews:

Exhibit 7: Summary of management commentaries on raw material sourcing from China

Company	Summary of comments
Aarti Industries	Q4FY20 • Post-march, issues related to supplies from China for the Pharma segment has improved. Company is maintaining higher inventory for some critical raw material. Q3FY20 • Fully backward integrated in Chemical business with no import from China • In Pharma division 40-50% of raw materials come from China, but have sufficient inventory for a month; performance may be impacted if persists more than a month (10-15% of the segment - mainly Steroids business). Q2FY20 • Tried to mitigate raw material supply volatility from China, with some increase in working capital days.
Balaji Amines	Q3FY20 • Sourcing raw material BDO from alternate sources. • No major dependence for raw materials on China. Q2FY20 • Observing price volatility in China, however no major dependence on raw materials from China.

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Company	Summary of comments
Deepak Nitrite	<u>**Q3FY20**</u> • Procure some raw materials from China, but covered till April-May in terms of contract and pricing from suppliers.
Fine Organics	• No raw materials are sourced from China.
Navin Fluorine	<u>**Q4FY20**</u> • Diversified sourcing for key raw materials, some smaller raw materials in Specialty Chemicals or CRAMS are imported from China where the company has started initiatives like backward integration or alternate sourcing <u>**Previously**</u> • 90% of Fluorspar is sourced from countries other than China, and the balance 10% can also be sourced if disruptions are faced.
Neogen Chemicals	<u>**Q4FY20**</u> • 2-3 raw materials are sourced from China, out of which only one is only sourced from China while others have alternates in India. <u>**Previously**</u> • China constitutes 10% of raw materials imported (around 40-50%). • Have some domestic sources of some raw materials and alternate products which they can prepare.
NOCIL	<u>**Q3FY20**</u> • No sourcing concerns as of now as have adequately covered raw materials. • Couple of raw materials are sourced from China but no supply constraints till now.
PI Industries	<u>**Q3FY20**</u> • Well covered till April-May. Raw materials supply from China is in single digits proportion of total. • Have alternate suppliers for raw materials sourced from China.
SH Kelkar	<u>**Q3FY20**</u> • Does not see any disruption till end of April. Covered with all raw materials and alternatives to continue production.
SRF	<u>**Q4FY20**</u> • Completely de-risked fluorspar sourcing from China. Sources a few other raw materials from China, which can be fully sourced from alternative geographies. <u>**Q3FY20**</u> • No impact on supply of Fluorspar as it can be sourced from alternate locations like from South Africa, Russia, Kenya and others.
Sudarshan Chemical	<u>**Q3FY20**</u> • Raw material sourcing diversified across Chinese provinces. • Only one supplier at epicentre of the crisis. • Some of the Chinese suppliers have begun production. • Do not expect any disruption in Q1FY21.
Vinati Organics	• No raw material is imported from China.

Source: Companies, Edelweiss Professional Investor Research

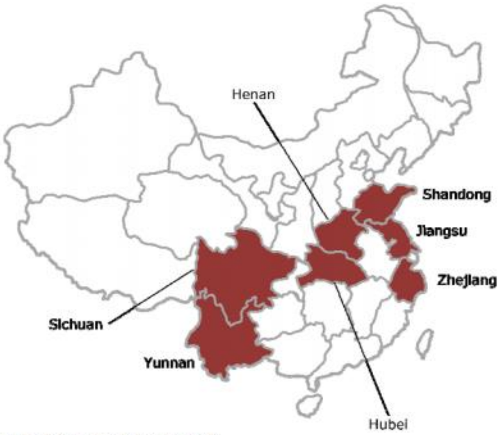
II. Environmental controls increased in China

China has been ramping up environmental regulations in the last few years. Not only have the regulations been strict, the enforcement has been strong as well. The new regulations have resulted in an overhaul for chemical producers in terms of infrastructure, involving relocation of chemical production facilities from urbanised areas to chemical parks, and away from the Yangtze river.

Such regulations have had multiple ramifications on the chemical industry. Starting with closure of chemical plants, the goal for the regulators were to undertake relocation of small, medium and large sized entities with potential risks to be undertaken at a faster pace (mostly by 2020-end), while the deadline for large-scale enterprises is around 2025. This was to have ~90% of plants within chemical parks by 2025 as compared to under 50% in 2018, so that risks from hazardous material can be controlled and tracked.

This exercise has resulted in closure of chemical plants, mostly those producing bulk chemicals and downstream product formulators (source: Journal of Business Chemistry), many of whom would not be able to withstand a higher cost structure owing to rising pollution control costs. Players able to relocate to chemical parks are facing additional pressures in terms of costs of relocations, sourcing of manpower, loss of production and smooth ramp-up of capacities once relocated. China had 676 chemical parks at the end of 2018.

Exhibit 8: Key chemical producing provinces



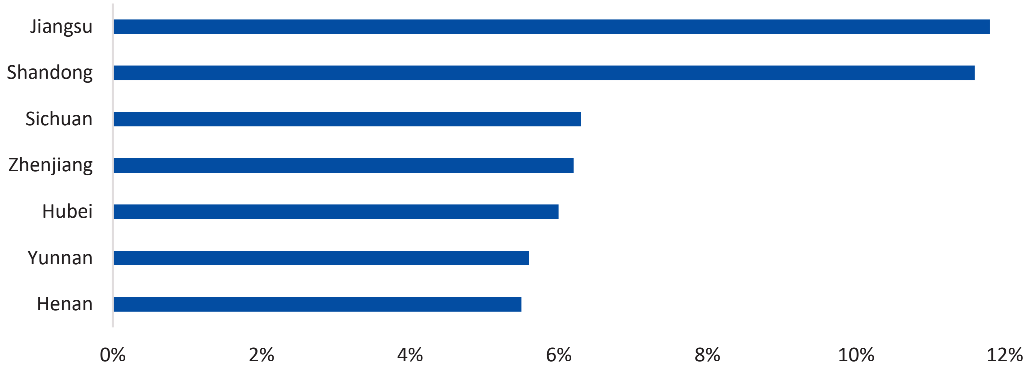
Source: China Statistical Yearbook 2006

Exhibit 9: Provinces affected by regulations

Source: Media reports, Edelweiss Professional Investor Research

Coastal provinces of Jiangshu and Shangdong have been the most affected, as reports suggest that China planned to close down ~2,100 and ~1,000 chemical plants in 2018, respectively. A recent report highlighted that Jiangsu province planned to close 9 chemical parks and 1,431 chemical companies in 2019. China plans to relocate 80% of chemical production capacity by the end of next year. Enforcement has become stricter after the Jiangshu chemical factory blast, with many plants being asked to relocate a second time owing to a stricter zoning requirement, Reuters reported.

Exhibit 10: Provincial contributions to Chinese chemical sector output

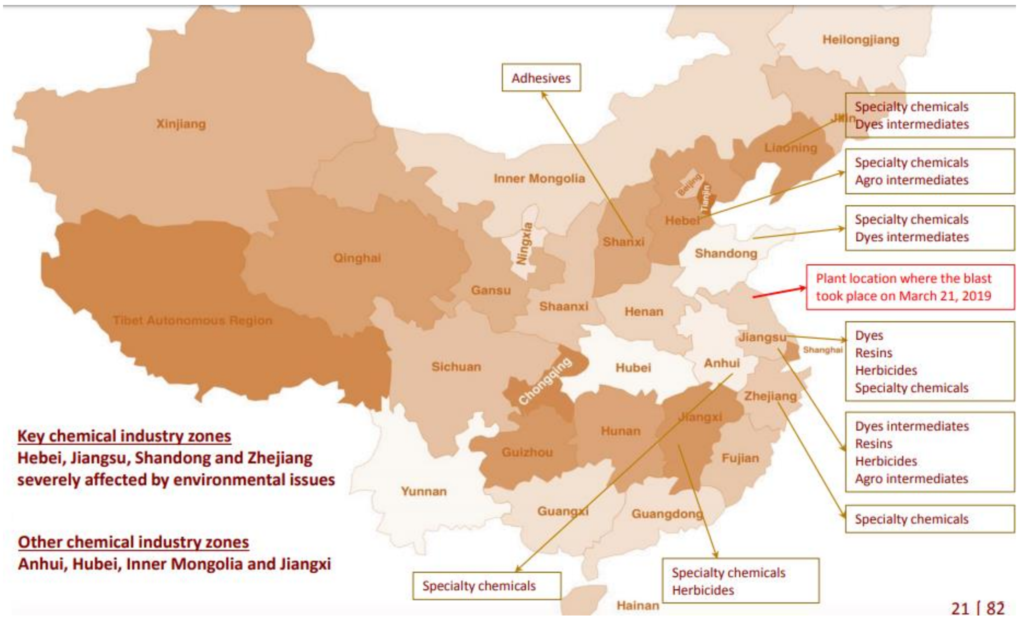


Source: China Statistical Yearbook 2006

Jiangsu blasts and the aftermath

A major explosion at the Yangcheng Industrial Park in Jiangsu province in March 2019 left 78 dead and over 600 injured. The Jiangsu province is a key chemical producing region and manufactures dyes, resins, herbicides and specialty chemicals. While China was already clamping down on non- or under-compliant chemical facilities, this event defined an inflection point that resulted in stricter enforcements.

Exhibit 11: Key chemical producing provinces in China



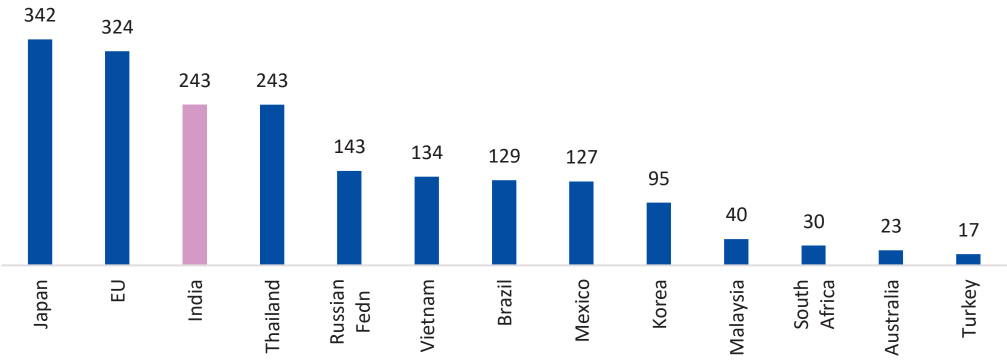
Source: Atul

III. US China trade war

The trade war between the US and China resulted in additional disruptions to the chemical supply chain. This is beneficial for Indian chemical manufacturers as it raises the scope for increased exports to the US. A large share of additional chemical exports coming the Indian way gives us confidence that any eventual shift in global sourcing would augur well for Indian manufacturers.

As per a study by the United Nations Conference on Trade and Development (UNCTAD), Taiwan was the biggest beneficiary of the diversion in trade, accounting for USD4.2bn of additional exports to the US in H1CY19. However, exports out of Taiwan included majorly machineries (electrical, office and precision). Mexico, EU, Vietnam, Japan, Korea and Canada were other countries ahead of India.

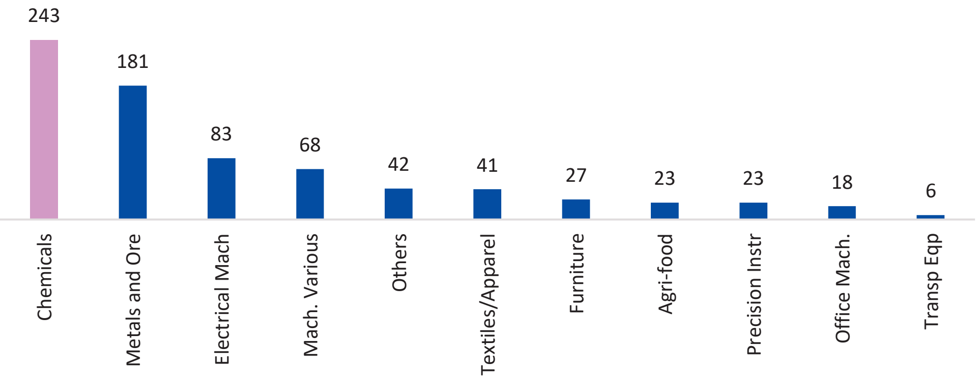
Exhibit 12: Trade diversion impact - Chemicals (USDmn)



Source: UNCTAD, Edelweiss Professional Investor Research

However, in terms of the chemical sector, India was a clear beneficiary. Of the USD755mn additional exports by India to the US in H1CY19, the chemical sector saw the highest contribution of USD243mn, almost a third of the share. This was second only to Japan (USD342mn) among the Asian peers and at par with Thailand. It constituted ~11% of the total benefits from diversion of trade in H1CY19.

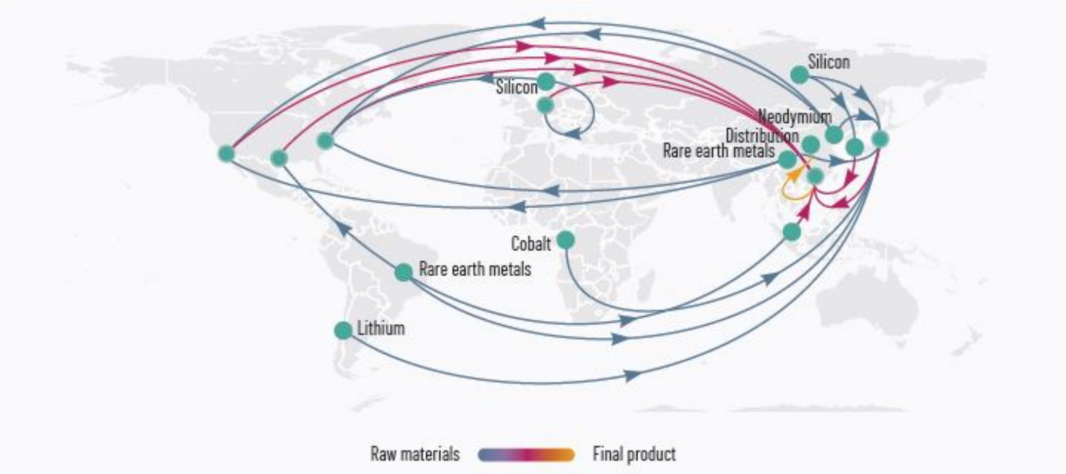
Exhibit 13: Trade diversion impact by sectors for India (USDmn)



Source: UNCTAD, Edelweiss Professional Investor Research

IV. Supply scenario is gradually evolving

Exhibit 14: Complexity of global supply chain

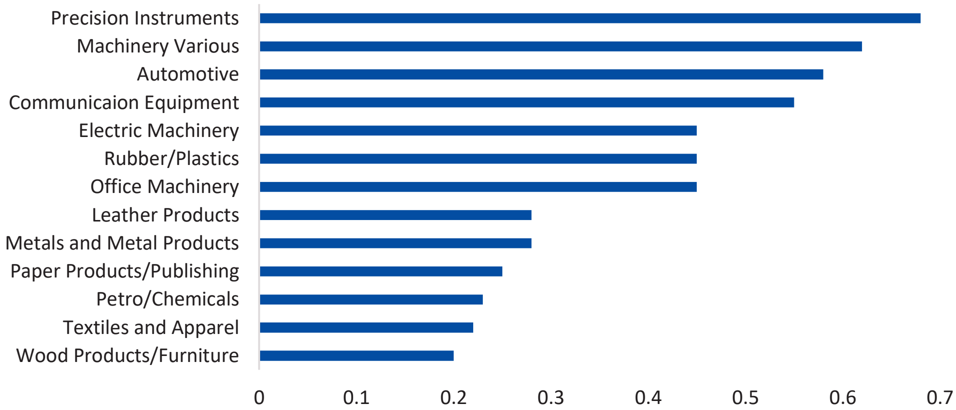


Source: UNESCO, Edelweiss Professional Investor Research

The global supply chain is inherently complex and manufacturers at the global scale focus on diversification of their feedstock sourcing. The recent disruptions in China have resulted in reduced capacity and operating rates for local chemical manufacturers, particularly in bulk and intermediate chemical segments. As per media articles, around 40% of the country's total manufacturing capacity was temporarily shut down over the last few years owing to environmental strictures.

This resulted in differentiated impacts across the chemical spectrum. Prices of certain chemicals, like dyestuffs, dye intermediates, methylene diphenyl isocyanate (MDI) and toluene diisocyanate (TDI) experienced a surge owing to the environmental clean-up. Within the Indian listed chemical companies, we saw few players capitalize on the same. For example, Deepak Nitrite saw one of its intermediate products - DASDA - see realizations treble in FY20 and was able to capitalize on the same resulting in significant profitability.

Exhibit 15: China's integration in global value chains, by sector (Grubel-Lloyd Index)



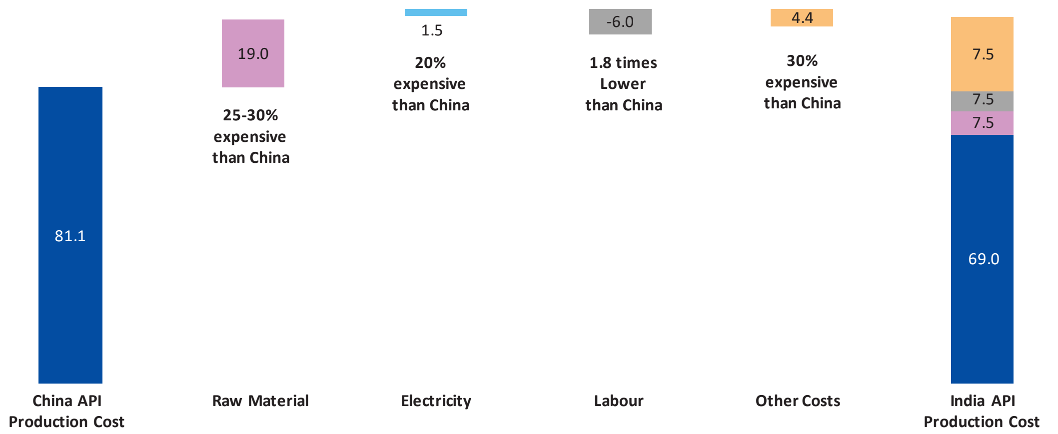
Source: UNCTAD, Edelweiss Professional Investor Research

What could possible aid a shift in the supply chain is the degree to which the Chinese industry is integrated globally. A measure of the integration of Chinese sectors in the global value chain (refer Exhibit 15) highlights that the integration of the chemical sector is lower than others (for instance: precision instruments, machineries, automotive, etc).

India scores well on the labour cost front

Cost of manufacturing in India is among the lowest globally. While costs are low for China as well, they are expected to increase due to high overheads for adhering to stricter environmental rules. The chart below outlines the relative comparison in costs. Additionally, India is better positioned in terms of intellectual property rules among a few competing countries and leading players in India have already demonstrated their technical and process chemistry skills to global partners.

Exhibit 16: China's cost of API production is ~20% lower than India



Source: KPMG Report on Indian API Industry, Edelweiss Professional Investor Research

Cost comparison of API manufacturing in China and India throws light on cost structure

The cost of production of APIs in China continues to remain 20-30% lower than India, primarily aided by lower cost of raw materials and utilities. India fares well in terms of labour cost, which is almost half of Chinese manufacturers. We use such comparison as an indicative for how the comparable costs could stand in chemical manufacturing. Exhibit 18 throws light on how labour costs in China has continuously increased.

Exhibit 17: Global cost comparison of manufacturing drugs (indicative)

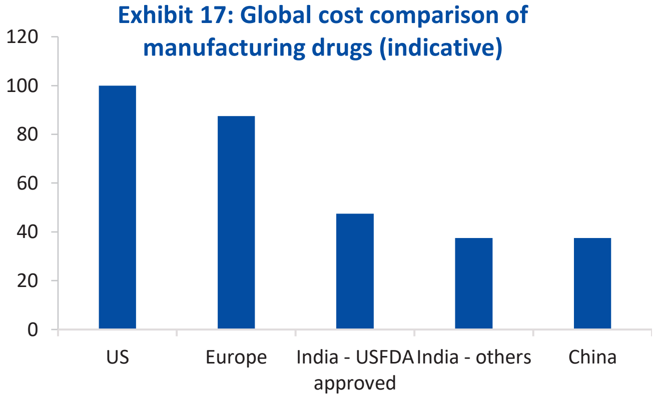
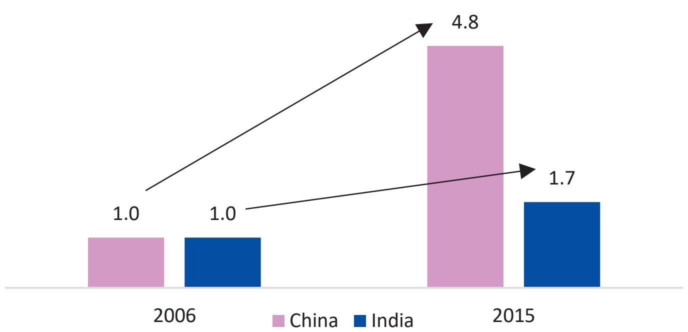


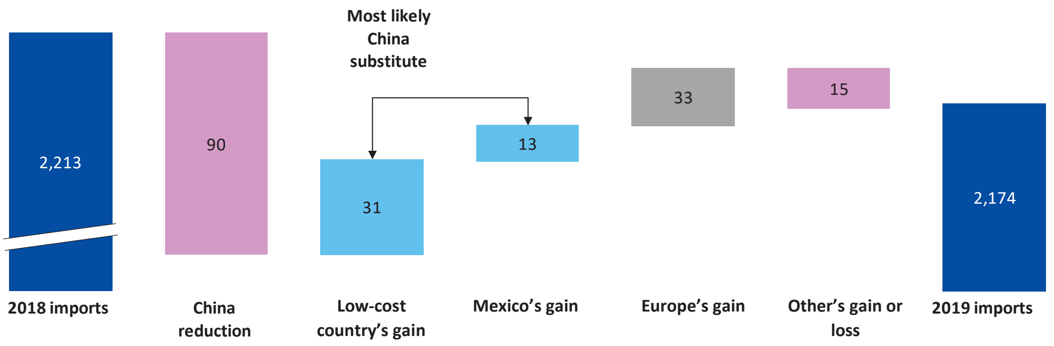
Exhibit 18: Comparison of costs between China and India ($ per hour)



Source: Neogen Chemicals, CRISIL, Edelweiss Professional Investor Research

Despite the relative cost advantage that Chinese manufacturers are enjoying, we see a shift happening from China. Analysis from AT Kearney shows that of the USD90bn fall in Chinese imports (across products in the US, around a third (USD30bn) has moved to low-cost Asian countries.

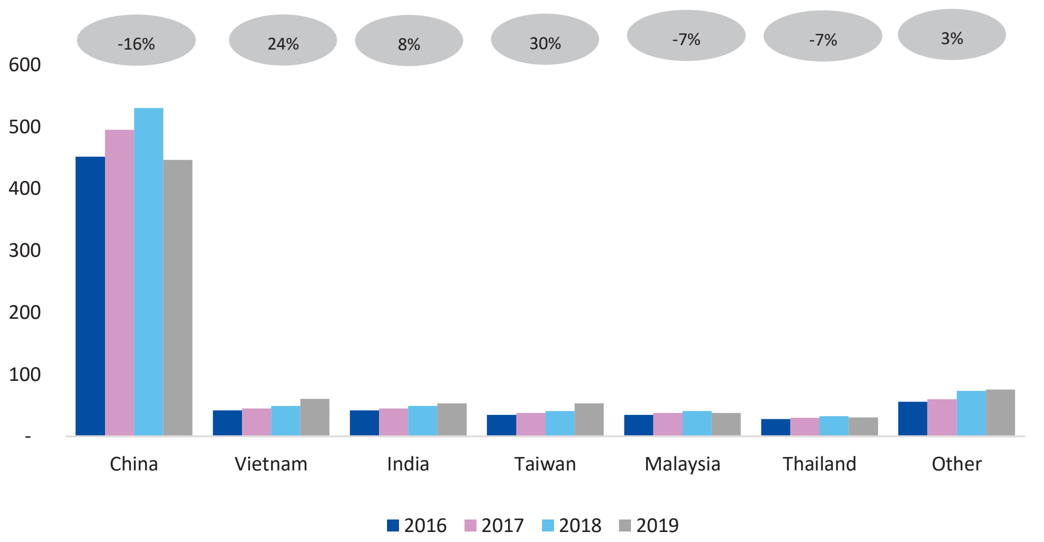
Exhibit 19: Manufacturing imports show clear trends of shift from China (USDbn)



Source: A.T. Kearney, Edelweiss Professional Investor Research

Between 2018 and 2019, India's share of exports to the United States have moved up ~10% to ~USD53bn.

Exhibit 20: US manufacturing imports from Asian countries (USDbn)



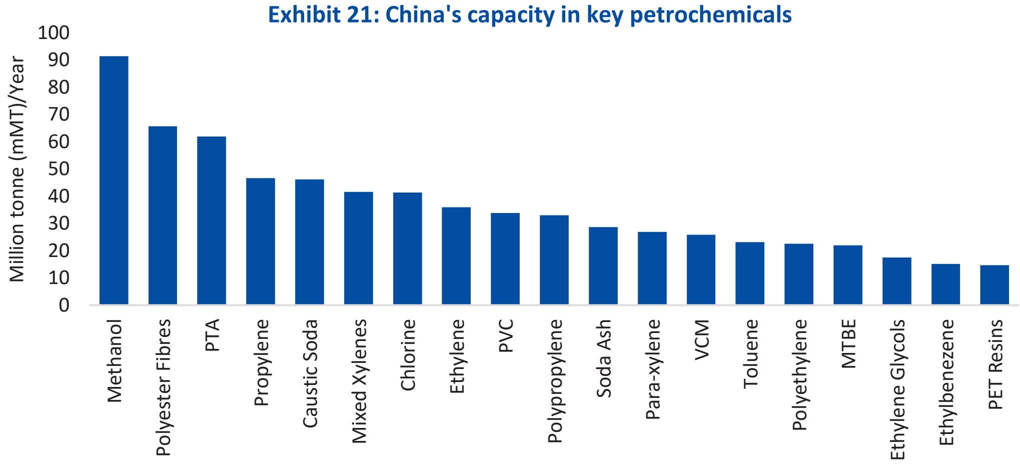
Note: Figures in bubbles are 2018-19 growth rate. Source: AT Kearney, Edelweiss Professional Investor Research

However, a large share has gone to Vietnam and Taiwan as we highlight in Exhibit 20.

These statistical trends tie up with what we saw materialize as an effect of the US China trade war in H1CY19. Consequently, it could be a possibility, in line with what was observed due to diversion during the trade war, that the Chemical sector will be a key beneficiary of any further trade diversion that may happen from China to India.

V. Replacing China may be difficult in bulk chemicals in the near term

Exhibit 21: China's capacity in key petrochemicals

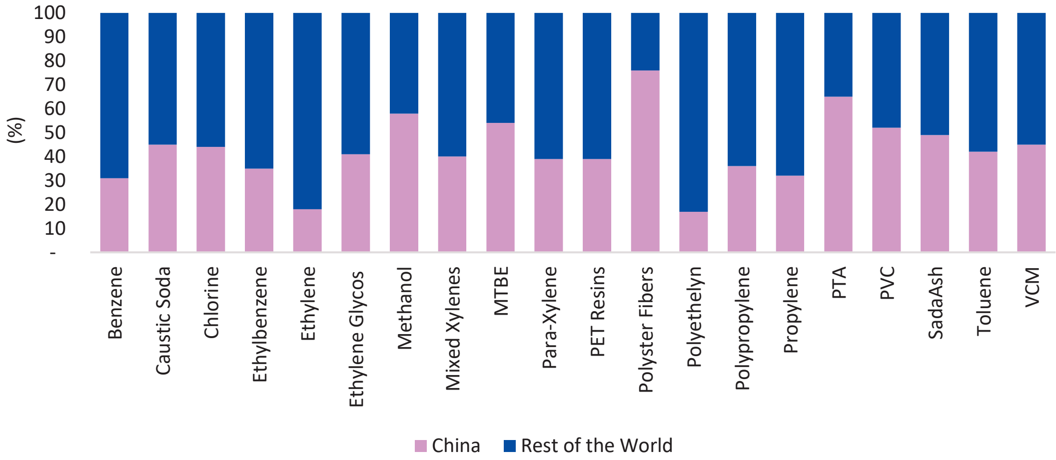


Source: ICIS

China has some of the world's largest manufacturing capacities in bulk chemicals, which has resulted in domestic manufacturers commanding significant market share in these products globally. This is evident from the fact that China commands ~39% market share in the global chemical market.

For example, China's share in most key petrochemicals are over 30% and touches around 60% in the case of methanol, polyester fibres and purified terephthalic acid (PTA). In most cases, these are bulk chemicals, which are the building blocks of a large array of downstream products.

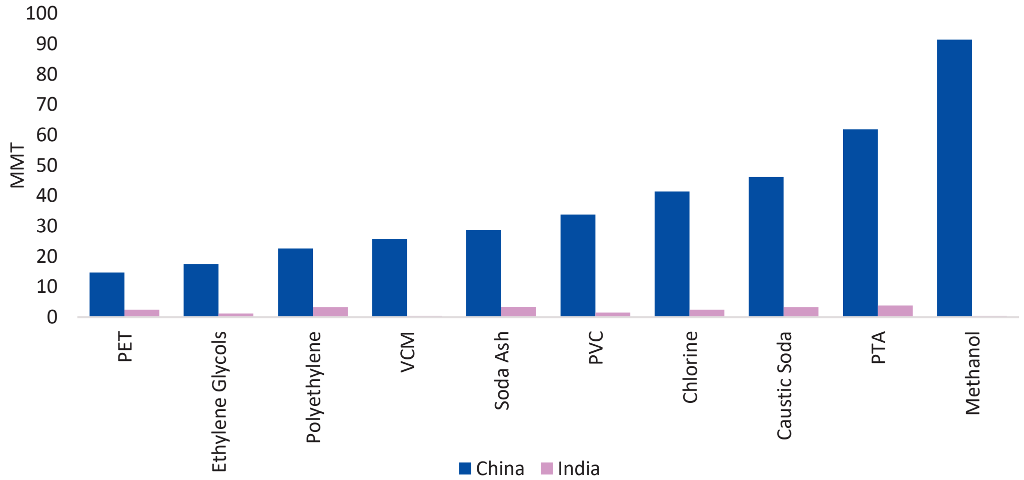
Exhibit 22: China's share of world petchem production capacity by product (%)



Source: ICIS

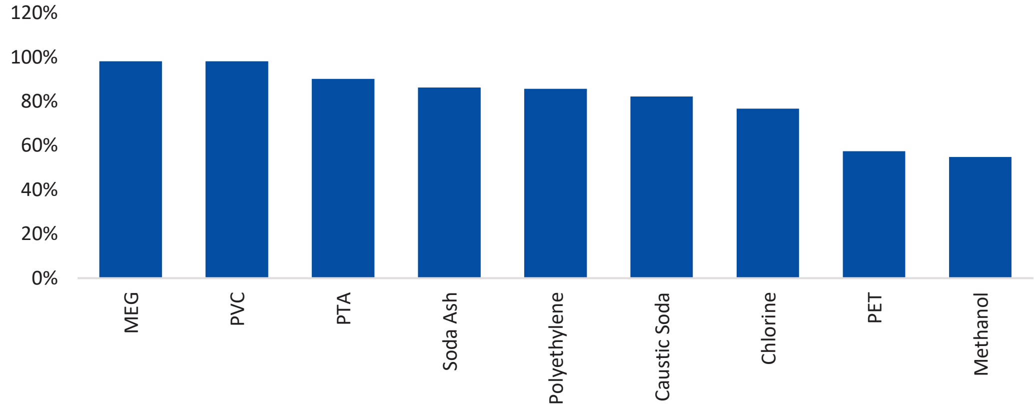
In comparison, Indian capacities are considerably lower and several of them are running close to optimum utilisation for most products.

Exhibit 23: Capacities of some key chemicals in India and China



Source: ICIS, Ministry of Chemicals and Fertilizers, FICCI

Exhibit 24: Capacity Utilizations of some key chemicals in India - 2018



Source: Ministry of Chemicals and Fertilisers, FICCI, Edelweiss Professional Investor Research

Owing to this, we believe China will continue to be a formidable player in bulk chemicals. Any incremental demand for bulk chemicals in the export market for Indian producers would need to be supplemented by sizeable capital expenditures, which would come with a lead time. We expect that competition for grabbing this part of the pie will also be higher among geographies. However, given the difference in the scale of capacities between China and India, we believe a small shift from China to India would bode well for Indian manufacturers in the bulk chemical segment.

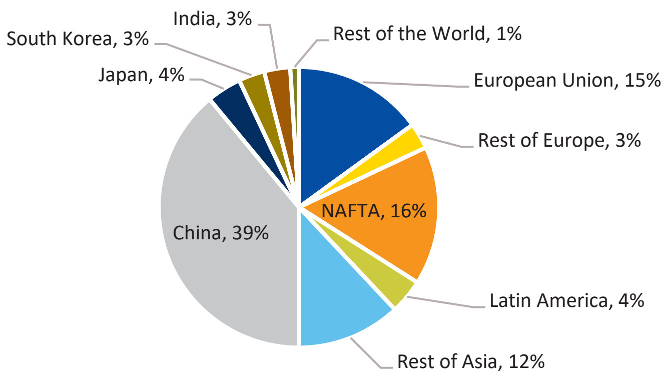
Parallelly, Indian manufacturers are well positioned to capture market share in specialty chemicals, which are smaller volume products with generally a higher margin profile as compared to bulk chemicals.

C. Indian chemical industry – capturing the tailwinds

I. India's share in global chemical industry is small

When compared globally, India contributes ~3% of global chemical sales despite being the the sixth largest chemical industry globally, behind China, EU, the US, Japan and South Korea. India is the third largest consumer of polymers in the world, fourth largest producer of agrochemicals in the world and sixth largest producer of chemicals in the world.

Exhibit 25: Global chemical sales region-wise

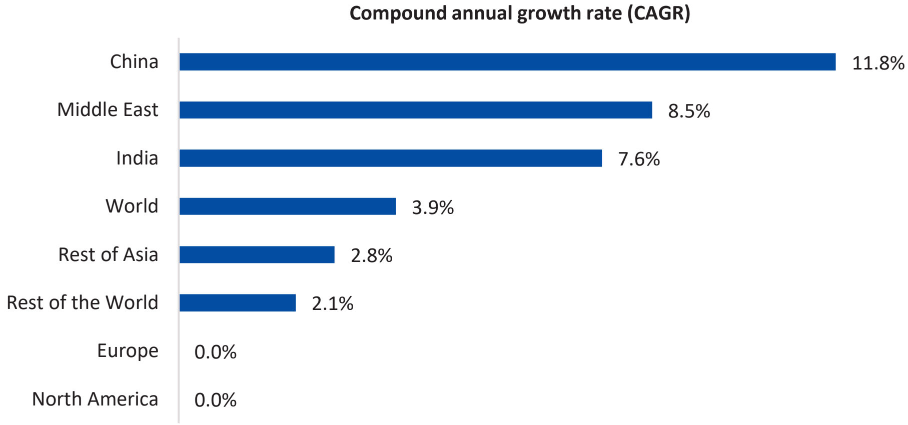


Source: CEFIC, Edelweiss Professional Investor Research

Increase in market share by Asian countries came at the expense of EU, US and Japan, who were the dominating regions prior to ramp up of capacities by the Asian players. India's share was 2.3% of the global chemical industry in 2008, which improved 40bps over the next 10 years to 2.7%.

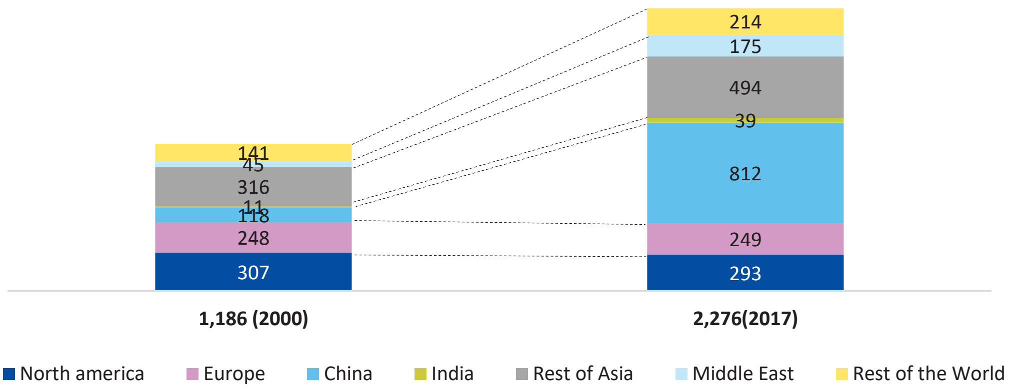
In comparison, China's share rose to 39% from 18% in 2007, due to the rapid built up of capacities with a competitive cost structure as compared to European players. The increase in the Indian industry's share in the global pie was in tandem with other southeast Asian players. For example, South Korea's share rose to 3.7% from 3.1% during this period. For the rest of Asia, the increase was a modest 150bps to 11%.

Exhibit 26: Growth in production volume over 2000-17



Source: UNESCO, Edelweiss Professional Investor Research

Exhibit 27: Capacity growth in global chemical industry over 2000-17 (in MT)



Source: UNESCO, Edelweiss Professional Investor Research

The compounded annual growth rate (CAGR) in production volumes of the Indian industry was quite strong (at 7.6%) and almost twice the rate of global growth (at 3.8%), but was behind that of China (sole key country recording a double-digit growth of 11.8%) and Middle East (~8.5%) over 2000-2017. In comparison, the same for developed countries in Europe and North America remained flat at an aggregate level.

In the process, Indian capacities almost quadrupled over this period to 39 MT from 11 MT. India, China and Middle East were the key regions that helped in doubling the global capacity during this period. While Middle East's capacities rose to 494 MT in 2017 from 316 MT in 2000, China's volumes increased an astonishing 8x during this period. This led to higher contribution of chemicals in global trade volumes, with the trade valued at USD750bn in 2017.

The movement is fuelled by growing demand in downstream industries in these emerging regions (booming industries like construction, automobile, textiles, electronics and water treatment) and a low-cost labour base resulting in competitive products in the bulk chemical segments and improving technical capabilities that enable collaboration and outsourcing arrangements with global innovators.

Growing consumption for chemicals in the country is creating additional tailwinds for domestic growth. India's per capita chemical consumption remains very low (~10% of world average) and there is substantial headroom for growth.

II. Indian chemical sector to see high single-digit growth over the medium term as COVID-19 related situation normalizes

Contributing ~15% of the Indian manufacturing sector and ~2% of GDP, the chemical sector has played a key role in providing raw material and intermediates to a host of end-user industries like pharmaceuticals, agriculture, automobiles, fast moving consumer goods (FMCG), paints, textiles and paper.

The sector had a total market size of USD163bn in FY18 and is expected to grow ~9% annually to ~USD300bn by FY25. Of this, the specialty chemicals industry is expected to contribute ~5% of global sales by FY21.

While the lockdowns and economic challenges due to the COVID-19 situation will impact the growth rate during FY21, we believe that over a longer period of time, the growth rates would be broadly similar to what was expected prior to the pandemic.

Exhibit 28: Pre-COVID-19 expectation: Indian Chemical Industry poised to grow at ~9% over FY18-25E (USDbn)

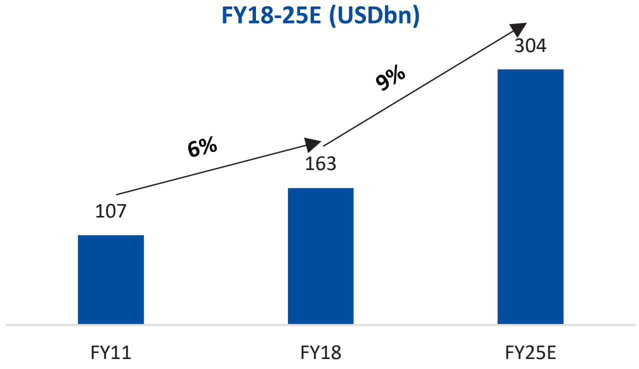
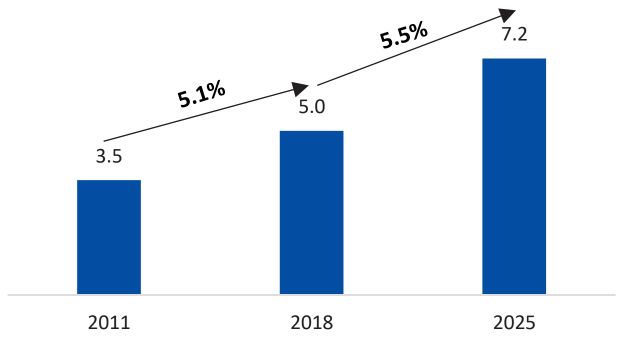


Exhibit 29:Pre-COVID-19 expectation: Global Chemical Industry is on its way to become USD 7trn by 2025 (USDtrn)

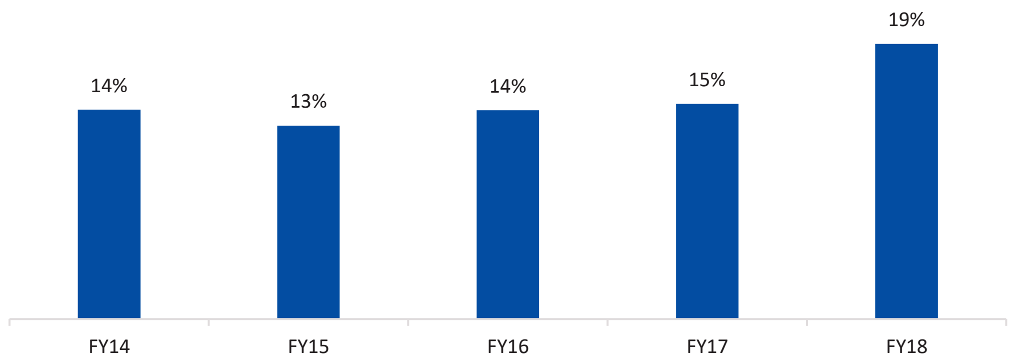


Source: FICCI, Edelweiss Professional Investor Research

India is well positioned to harness growth in global specialty chemicals market

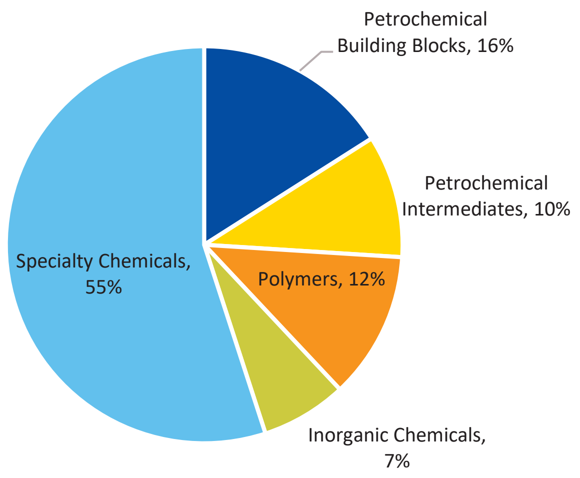
Indian manufacturers are better positioned to gain market share in the global specialty chemicals market. Around 20% of India’s domestic production is now being exported, of which specialty chemicals account for more than half of the pie.

Exhibit 30: Share of domestic production being exported



Source: FICCI, Edelweiss Professional Investor Research

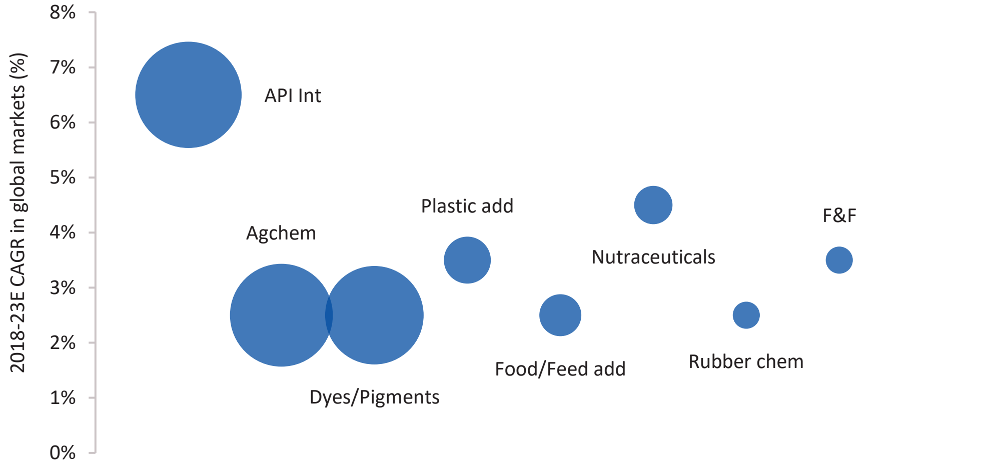
Exhibit 31: Specialty chemicals constitute more than half of India's exports



Source: McKinsey Report, Edelweiss Professional Investor Research

Despite this, India's share in the specialty chemical global market remains in low single-digits. This is about a quarter of China's capacity. Intermediates for APIs, agrochemicals and colourants (dyes and pigments) are the key segments where India eyes exports. Apart from these, strong growth is expected in electronic chemicals and nutraceuticals.

Exhibit 32: Global specialty chemicals' market size and expected growth rates

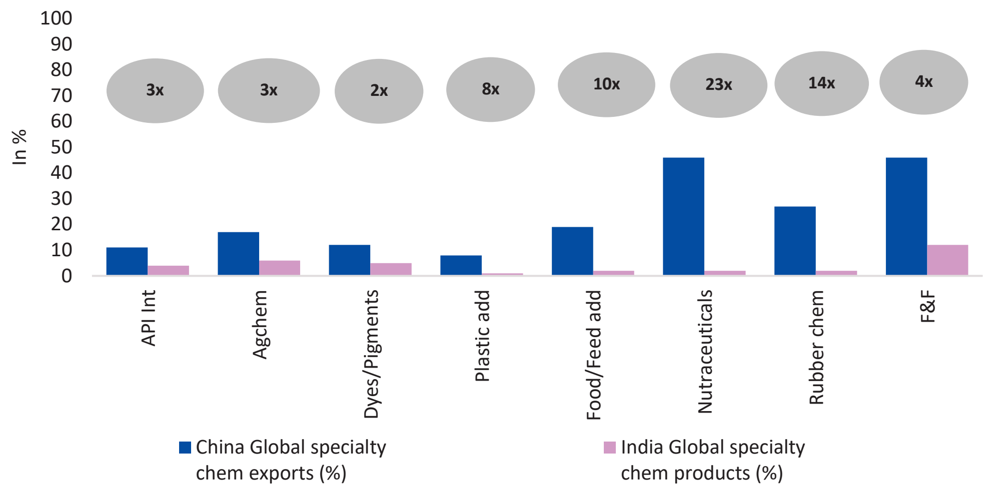


Note: Growth rate expectations are pre-COVID-19.

Source: McKinsey Report, Edelweiss Professional Investor

India's market share in key products like API intermediates, agrochemicals and colourants range from around a half to a third of China's market share. It's relatively better position in specialty chemicals (as compared to bulk chemicals) implies better market penetration by Indian companies and hence could lead to more engagements with global players going forward.

Exhibit 33: Market share of China and India in specialty chemicals



Note: Figures in bubbles represent the size of China's market share with respect to India

Source: Edelweiss Professional Investor Research

III. Chemical companies with existing global relationships to benefit

Apart from the shorter-term disruption and the consequent benefits/detriments on a case-to-case basis, global manufacturers would try to de-risk their supply chain by moving a part of their supply chain to countries other than China. India could be a key beneficiary of this trend.

This would in effect be a structural shift, a portion of which would come to Indian companies, and would aid those who have: a) Developed scale; b) Proven technical expertise; c) Existing customer relationships; and d) Demonstrated track record of delivery. Indian players are better positioned in terms of technical capability and maintaining intellectual property standards when compared to certain competitors.

Several Indian players have already forged strong relationships with global large-scale manufacturers and will see benefits of the same. Chemical industry is characterised by development of relationships, which is a result of consistent delivery of quality product in prior engagements. We list details of some players who are partnering with global counterparts.

Exhibit 34: Foreign partnerships/collaborations forged by key companies

Company	Partnership/collaboration details	Year
Aarti Industries	A 20-year exclusive supply contract with a global chemical manufacturer (~INR 10,000 crore)	FY18
Aarti Industries	INR 900 crore contract to supply a specialty chemical intermediary to a global manufacturer	FY19
Navin Fluorine	Five-year contract with a US customer for contract research and manufacturing services (CRAMS)	FY20
Navin Fluorine	INR 2,900 crore 7-year contract with a global manufacturer for production and supply of a high performance product	FY20
PI Industries	Co-marketing of BASF's products for domestic agrochemical market	FY18
PI Industries	Formed joint venture (JV) with Mitsui Chemicals to provide registration for the latter's proprietary agrochemicals	FY17
PI Industries	Formed JV with Kumiai Chemical Industry Co to manufacture and distribute bispyribac-sodium, the flagship agrochemical product of Kumiai in India, and may also add more products	FY18
Vinati Organics	Entered into long-term contract to supply isobutyl benzene (IBB) to BASF US	FY08

Source: Companies, Edelweiss Professional Investor Research

Several other players undertake custom synthesis manufacturing (CSM) in India as highlighted in the table below.

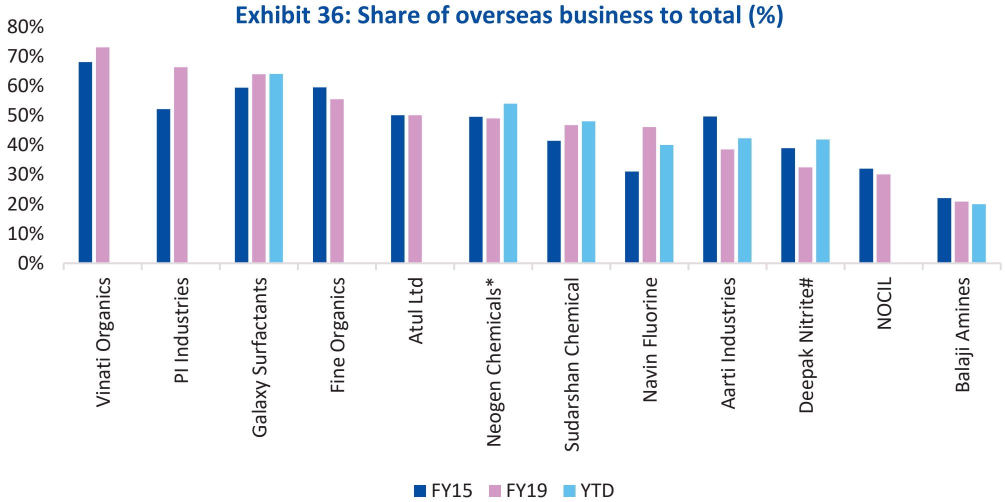
Exhibit 35: Other players who are undertaking CSM/CRAMS

Company	Comments
SRF	Undertakes contract manufacturing of active ingredients/intermediates for global agrochemical and pharmaceutical companies
PI Industries	In its CSM division, PI Industries undertakes custom synthesis for global innovators in predominantly patented products
Neogen Chemicals	Undertakes custom synthesis in organic chemicals for agrochemical innovators or pharma players with process know-how and in-house technical specifications. Management is focusing on CSM in the upcoming capacity expansion.

Given that significant approvals result in longer timeline for sales gestation in most chemical businesses, players who already have strong overseas relationships would be well placed to capture any incremental demand.

We list the share of overseas sales of key chemical companies. Companies shown below have been able to develop strong position in overseas markets (through demonstration of R&D, process research capabilities, technology partnerships, outsourcing mandates, etc) and would see any benefit of a shift from China, demonstrated by their stable or increasing share of the export pie.

Exhibit 36: Share of overseas business to total (%)



Note: Overseas share have been calculated by disclosed exports/foreign market sales as a percentage of total sales, except for Galaxy Surfactants where volume data has been used. *For Neogen Chemicals, FY16 share has been provided instead of FY15. #For Deepak Nitrite, standalone information has been used. YTD refers to 9MFY20.

Source: Companies, Edelweiss Professional Investor Research

Exhibit 37: Details of overseas business by key chemical companies

Company	Details on exports
Vinati Organics	Global leader in ATBS and IBB, which see significant exports. New product – butyl phenols – is an import substitute which may skew the mix towards domestic sales going forward. However, export-oriented products, particularly ATBS, are expected to see strong growth at the absolute level
PI Industries	Two-thirds business accrues from the CSM division, where PI partners with global innovators for manufacturing agrochemical intermediates. This remains a growing segment and further growth is expected as the company moves into CSM in other segments like pharma or specialty chemicals
Galaxy Surfactants	Two-thirds of the business comes from Western countries and Asia, Middle East and Turkey
Fine Organics	Large share of global customers, which could increase as new products are developed
Atul	Large share of exports across segments
Neogen Chemicals	Significant share of global customers in the organic chemicals segment. Focus on CSM and active intermediates would be instrumental in bringing up this share
Sudarshan Chemical	Among the top pigment manufacturers globally. Aims to be the third largest player as export share increases
Navin Fluorine	CRAMS segment is fully export oriented. A significant portion of exports is to global agrochemical/pharma customers in specialty chemicals segment
Aarti Industries	Supplies to several global customers in specialty chemicals and pharma divisions
Deepak Nitrite	Fine and specialty chemicals and performance products segments are export oriented
NOCIL	Exports latex products to south-east Asia, focusing on US customers
Balaji Amines	Exports several chemicals, particularly in amines derivatives and specialty products, with REACH (Registration, Evaluation, Authorisation and Restriction of Chemicals) registration in place to export to Europe

IV. Specialty chemicals to grow faster than bulk chemicals in domestic markets

As end-user industries in India undergo changes in terms of value addition in product categories, demand for specialty chemicals is expected to grow at a faster rate. Specialty chemicals are characterised by low volumes and higher margins, and in a large share of products require significant technological knowhow for manufacturing.

Despite being fragmented in nature, the penetration of specialty chemicals in the domestic market remains low. This is likely to change as technologies mature in the end-industry segments, which in effect will bolster demand for these products. Additional demand of specialty chemicals will come from overseas markets, as outlined earlier.

As per CRISIL, the global specialty chemicals segment was valued at USD743bn in 2017, and is expected to grow in mid-single digits to ~USD1trillion by 2022. China and India, which forms a sizeable part of the Asia Pacific market, are expected to drive growth of the region by ~7% to ~USD400bn in 2022 from ~USD300bn in 2017.

Exhibit 38: Significant opportunity of growth for specialty chemicals market (USD bn)

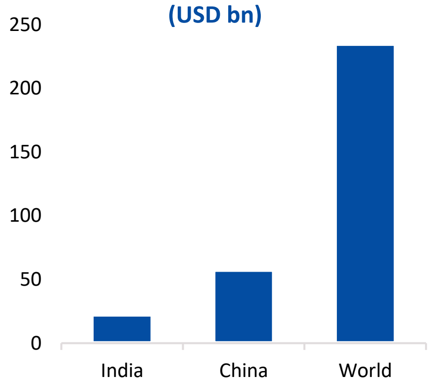
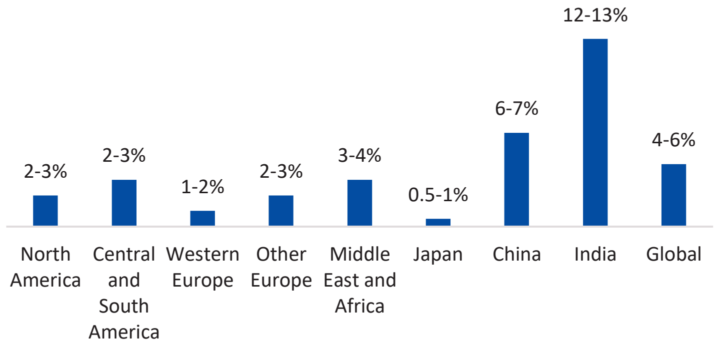


Exhibit 39: Expected growth rate of speciaty chemicals markets by region (FY18-23E)



Note: Growth expectations are pre-COVID-19 and can moderate in the near term

Source: Aarti Industries, CRISIL, Edelweiss Professional Investor Research

Exhibit 40: Market size of global specialty chemicals (USDbn)

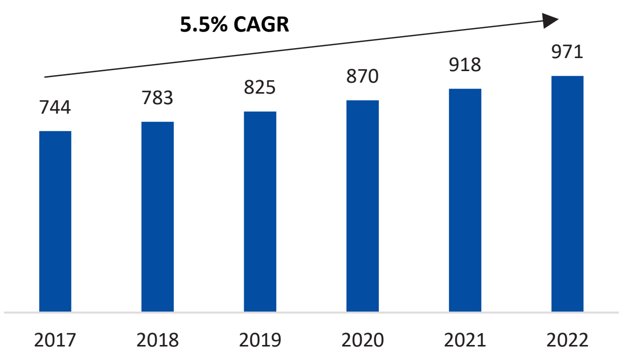
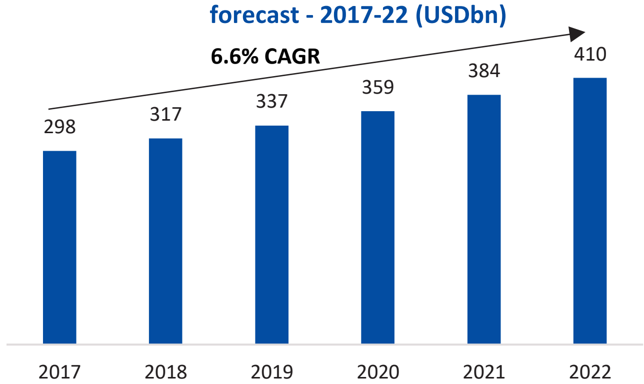


Exhibit 41: Asia-Pacific specialty market size and forecast - 2017-22 (USDbn)

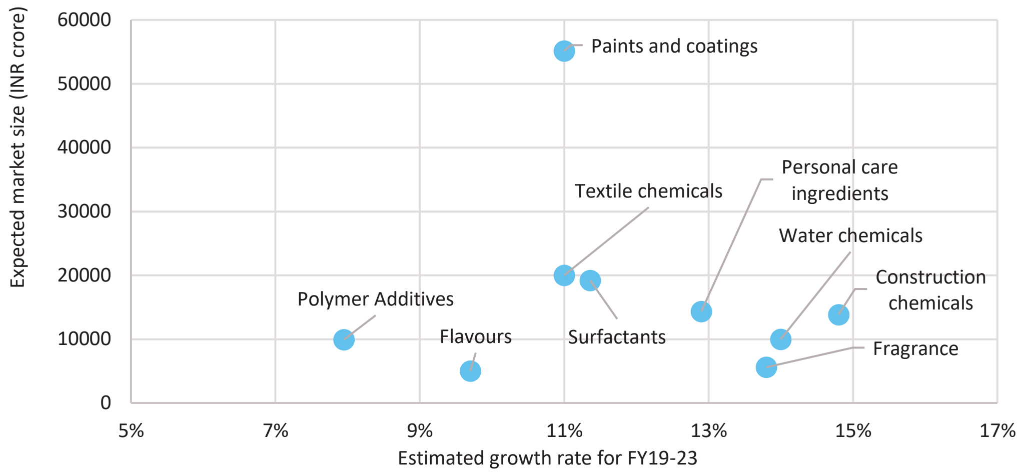


Note: Growth expectations are pre-COVID-19 and can moderate in the near term.

Source: Neogen Chemicals, CRISIL, Edelweiss Professional Investor Research

Within the Asia-Pacific basket, over FY19-22E, the Indian specialty chemicals sector is expected to grow at ~12% CAGR. Construction chemicals, water chemicals, flavours and fragrances, surfactants and personal care ingredients are forecasted to grow at mid- to low- double digit rates over FY19-23E. While the growth rate could be impacted by the COVID-19 related scenario in the near term, burgeoning downstream demand should aid in normalization of the rate towards expectation in the medium term.

Exhibit 42: Specialty chemicals are expected to grow at a higher rate than bulk chemicals



Note: Expectations are Pre-COVID-19. Could moderate in the near term.

Source: FICCI, Edelweiss Professional Investor Research

Several listed players in the chemicals sector are poised to capitalise on this growth. We highlight a few of the same in the table below.

Exhibit 43: Key listed chemical companies manufacturing specialty products

Chemical	FY19-23E growth	Companies
Fragrance	14%	SH Kelkar – significant share of the business
Personal care ingredients	13%	Galaxy Surfactants – mild surfactants for personal care focus area
Surfactants	11%	Galaxy Surfactants
Paints and coatings	11%	Sudarshan Chemicals – domestic and global leader
Flavours	10%	SH Kelkar
Polymer additives	8%	Fine Organics - Polymer additives is a major product category

Note: Expectations are Pre-COVID-19. Could moderate in the near term.

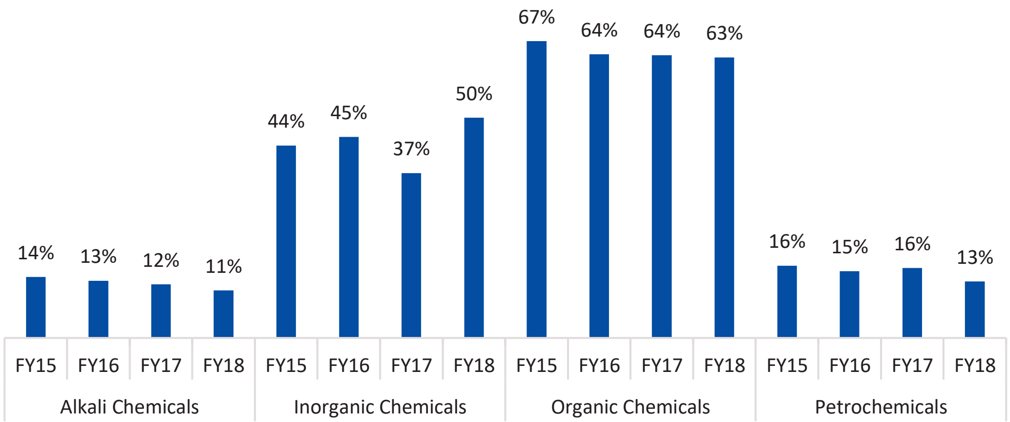
Source: FICCI, Edelweiss Professional Investor Research

Apart from these broad categories, there are several diversified players in the specialty chemicals business who are expected to see strong growth. Players in the amines segment (Alkyl Amines and Balaji Amines), benzene-toluene chain (Aarti Industries, Atul and Vinati Organics) and halogen chemistry (SRF, Navin Fluorine and Neogen Chemicals) would also enjoy tailwinds from the growth in downstream industries.

V. Domestic production of bulk chemicals is not sufficient to meet internal demand

The current production capacity of the Indian chemical industry is lower than the domestic demand. Given the sheer volume of production, the shortfall compared to overall domestic demand is relatively lower in case of petrochemicals (in the range of 13-16% over FY15-18) and alkali chemicals (11-14% in FY15-18 with a consistent improving trend). The shortfall is significant in case of organic and inorganic chemicals, where it is at ~50% and over 60% respectively.

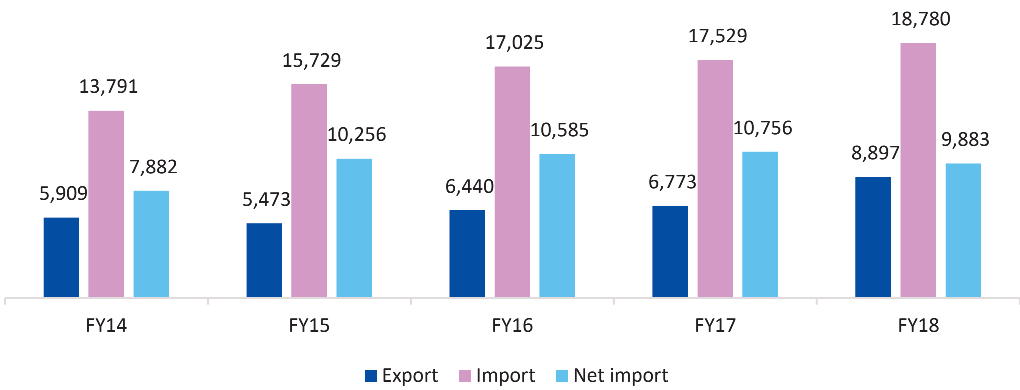
Exhibit 44: Production-consumption gap as a percentage of consumption



Source: FICCI, Edelweiss Professional Investor Research

In order to meet this shortfall, India imports a large volume of chemicals, as compared to exports. With imports pegged at 18,780 thousand MT in FY18 (which has seen a consistent rise from around 13,791 thousand MT in FY14), India remains a net importer of chemicals.

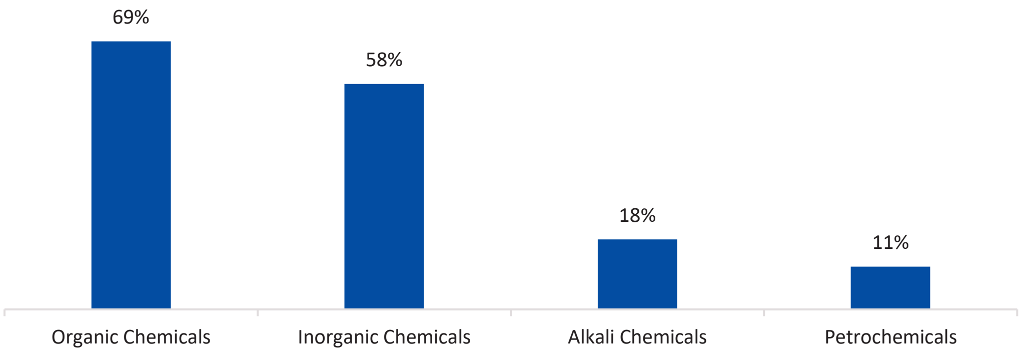
Exhibit 45: Foreign trade in chemicals (in '000 MT)



Source: FICCI, Edelweiss Professional Investor Research

Similar to what we observed in Exhibit 44 related to production-consumption gap, India's largest share of imports are in organic and inorganic chemicals, which are close to 70% and 60% respectively. For alkali and petrochemicals, the import share is at around 18% and 11% respectively.

Exhibit 46: Proportion of imports in domestic demand



Source: FICCI, Edelweiss Professional Investor Research

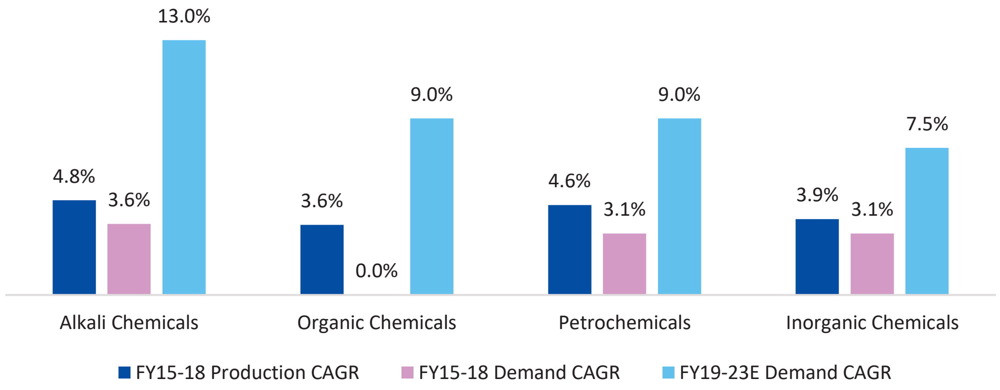
Future growth rate to be higher than the past

Recent impetus on domestic production is expected to fuel the growth rate in the chemical industry going forward. We expect growth rates to be higher than that experienced over the last few years, driven by factors like import substitution and focus of domestic manufacturers on exports as they see stronger demand from global customers.

A study by FICCI estimates (pre-COVID-19) FY19-23 growth rates of ~13/9/9/8% for alkali/ inorganic/ organic/ petrochemicals as compared to FY15-18 demand growth of 4/0/3/3%, respectively.

Growth in key end-user industries like FMCG and textiles for alkali chemicals, aluminium and steel, which would be a reflection of broad-based industrial activity and capex for inorganic chemical, and higher demand for polymers and plastics from packaging and textile industry would auger well for growth in petrochemicals and organic chemicals, along with growth in the pharmaceutical and agrochemical industries.

Exhibit 47: Historical and expected growth rates of bulk chemicals



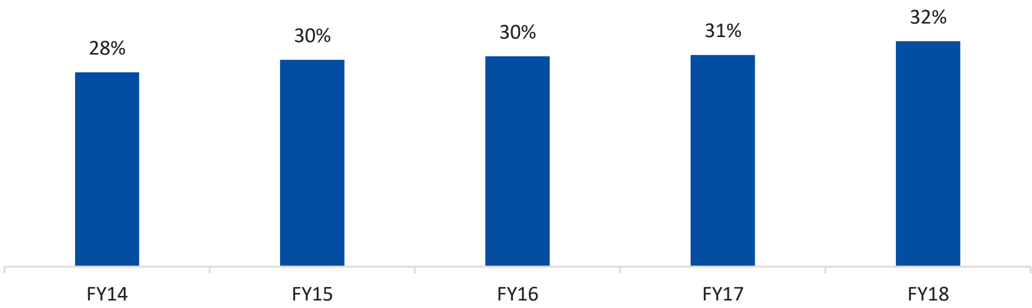
Note: FY19-23E growth rates are pre-COVID-19 estimates and are expected to moderate in the short term.

Source: FICCI, Edelweiss Professional Investor Research

Government initiatives to be pivotal for growth

Several initiatives have been taken by the Indian government to boost capacity and integration in the chemical value chain, which would play a key role in providing the much-required stability in terms of feedstock sourcing, a weak point in the current scheme of things.

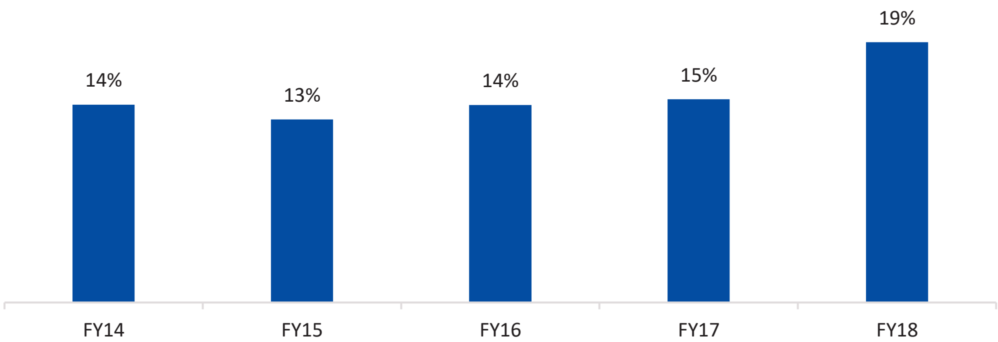
Exhibit 48: Share of domestic consumption being imported



Source: FICCI, Edelweiss Professional Investor Research

As highlighted previously, India is a net importer of chemicals with a large share of overall domestic demand met by imports. The consumption-production gap during FY15-18 was 18-20%, with overall import share higher than 30%, given that around 20% of domestic production is exported. We see both these shares showing an increasing trend.

Exhibit 49: Share of domestic production being exported



Source: FICCI, Edelweiss Professional Investor Research

The government's Make in India initiative was undertaken to reduce the country's import bill. Under this, the following initiatives were provided:

- PCPIRs – The plan was adopted in 2007 to develop integrated chemical hubs in Petroleum, Chemicals and Petrochemicals Investment Regions (PCPIR). Four regions have been identified in Dahej (Gujarat), Vishakhapatnam (Andhra Pradesh), Paradip (Odisha) and Cuddalore (Tamil Nadu).
- The aim of PCPIRs is to provide integrated chemical manufacturing hubs with feedstock anchors (similar to global hubs like Jurong Island in Singapore). Among the four PCPIRs, Dahej has progressed the most.
- PCPIRs are spread over an area of over 250 square km with a minimum processing areas of ~100 sq km (i.e. 40% of total).

- Attracting investments to Vizag, Paradip and Cuddalore has not been at a similar pace as Dahej, and the government is now also focused on rejuvenating these PCPIRs.
- Such integrated hubs would eventually result in strong efficiencies in terms of easy availability of feedstock, reduced logistic and operating costs and ease of transport due to the proximity to ports.

Exhibit 50: 4 PCPIR regions that have been set up

- Other policies like the National Policy on Petrochemicals and Chemicals Promotion Development Schemes would also be instrumental for growth of the industry through technology, process and product improvements. Additional incentives like tax reductions (on R&D) and also the recently announced lower tax rate for newly incorporated companies will be beneficial for growth of the industry.
- 100% Foreign Direct Investment (FDI) has also been allowed under the automatic route.

New Bulk Drug Promotion Policy could aid chemical players in the pharma chain

Additionally, we believe government impetus on domestic API manufacturing, ease of doing business and faster clearances for capex would be pivotal for growth of the sector. The government has recently incentivised the Bulk Drug manufacturing sector through the new Bulk Drug promotion scheme. Salient features of the scheme are:

- Three mega bulk drug parks are to be set up with state partnerships with Central Government grants up to INR 1,000 cr par park, i.e. INR 3,000 cr approved for next five years
- The parks will have common facilities such as solvent recovery plant, distillation plant, power & steam units, common effluent treatment plant etc.
- Production linked incentive to be given for manufacture of 53 bulk drugs, out of which 27 are chemical synthesis (10% incentive) based bulk drugs and the remaining are fermentation based (20% incentive). ~INR 7,000 cr has been approved for the next eight years for this.
- It is estimated that this will result in additional sales of INR 46,400 cr over the next eight years

We believe that this could be a positive for the chemical players in the pharma value chain. We highlight a few players in the chain. India currently imports 70% of APIs from China, which has resulted in challenges during the supply chain disruption. We believe that bulk drug manufacturers may source critical raw materials for their products from domestic suppliers. Few Indian companies who are in the pharma value chain in India are listed below:

Exhibit 51: Companies in India with pharma segment as key end user industry

Company	Comments
Aarti Industries	Supplies to domestic generic players, with Pharma API and Intermediates contributing 60% of the pharma segment revenue
Alkyl Amines	Supplies amines derivatives and specialty chemicals to domestic pharma companies
Balaji Amines	Supplies amines derivatives and specialty chemicals to domestic pharma companies; Pharma segment contributes 51% to the top-line
Deepak Nitrite	Key products in Deepak Phenolics are Acetone and Isopropyl Alcohol which are used in the pharma industry
Navin Fluorine	Supplies off-patent or generic fluorine based molecules to domestic pharma companies in the specialty chemicals segment; pharma segment contributes ~40% of the specialty chemical segment. Additionally R-22 refrigerant gas is used in pharma industry which is seeing increasing offtake
SRF	Supplies specialty chemicals to pharma companies, also R-134a is used as a propellant in the pharma industry

VI. Domestic listed players to capture growth in increasing demand for bulk chemicals in the country

As per a recent FICCI report, several bulk chemicals are expected to see strong demand. Notable among these are aluminium fluoride, soda ash, phenol, acetone etc. We see several listed players present in these product lines, who will be able to capitalize on such demand.

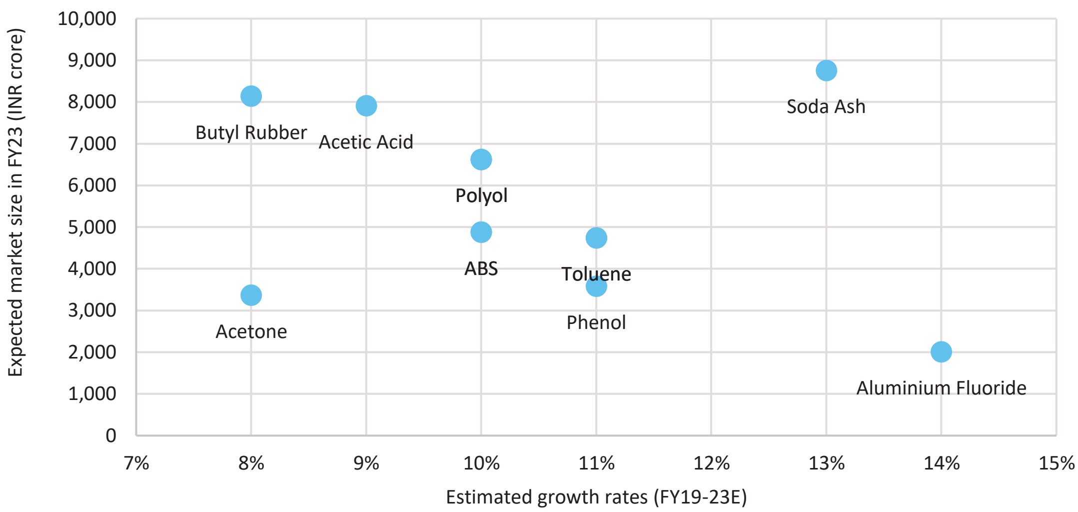
Exhibit 52: Bulk chemical companies exposed to domestic growth

Chemical	FY19-23E growth	Companies enjoying tailwind
Aluminium fluoride	14%	Navin Fluorine – inorganic fluoride business
Soda ash	13%	Tata Chemicals, GHCL
Phenol	11%	Deepak Nitrite – Deepak Phenolics' key product
ABS	10%	INEOS Styrolution, Bhansali Engineering Polymers
Acetone	8%	Deepak Nitrite – Deepak Phenolics' key product
Butyl rubber	8%	Apcotex Industries
Carbon black	6%	Phillips Carbon Black, Himadri Speciality Chemical

Note: FY19-23E growth rates are Pre-COVID19 estimates
Source: FICCI, Companies, Edelweiss Professional Investor Research

Deepak Nitrite (BUY), which has commissioned a large-scale phenol manufacturing plant in FY19, is well positioned to capitalise on strong demand for the chemical and its by-product acetone. Phenol, which was previously primarily imported to meet domestic demand before Deepak Nitrite's plant was commissioned, is expected to see a demand growth of 11% over FY19-23. Acetone is expected to see demand growth of 8% over the same period.

Exhibit 53: Expect growth in bulk chemicals on strong domestic demand



Note: FY19-23E growth rates are Pre-COVID19 estimates

Source: FICCI, Edelweiss Professional Investor Research

Increase in demand for inorganic fluorides will augur well for Navin Fluorine. The company manufactures anhydrous hydrofluoric acid (AHF), a key raw material for aluminium fluoride, which is expected to growth ~14% over FY19-23, as per a FICCI report.

Soda ash, which accounts for more than 40% demand among alkali chemicals, is expected to grow at 13% CAGR over FY19-23 due to a strong medium term demand outlook for glass and detergent markets. Producers will see tailwinds from this trend and Tata Chemicals would be a key beneficiary.

Similarly, colourants, which include both dyes and pigments, is expected to see 9% growth. This should be beneficial for pigment players like Sudarshan Chemical and dyes/dye intermediate manufacturers. Part of the demand for pigment players should accrue from the 11% growth rate in paints and coatings industries.

It is important to note that players moving into specialty carbon black value chain like Phillips Carbon Black and Himadri Speciality Chemical could enjoy some tailwind from this trend as this chemical is predominantly used for their black pigmentation properties in inks, paints and coatings. Being products which are of higher margin nature and a stickier customer base (characterised by stringent approvals given the performance nature of the products), this could be a growth driver in an industry.

Import substitute products are also seeing increased capacity expansions in India

Apart from the bulk chemicals, we expect demand traction from domestic players as capacities of more import substitutions are added. Below are few of import substitute products from key chemical companies.

Exhibit 54: Key products of few companies which are import substitutes

Company	Products
Alkyl Amines	Acetonitrile, Amine Derivatives and Specialty Chemicals
Balaji Amines	NMP, NEP, Morpholine, Acetonitrile, Other derivatives and Specialty Chemicals
Deepak Nitrite	Phenol, Acetone, Isopropyl Alcohol
Vinati Organics	Butyl Phenols
NOCIL	TBBS

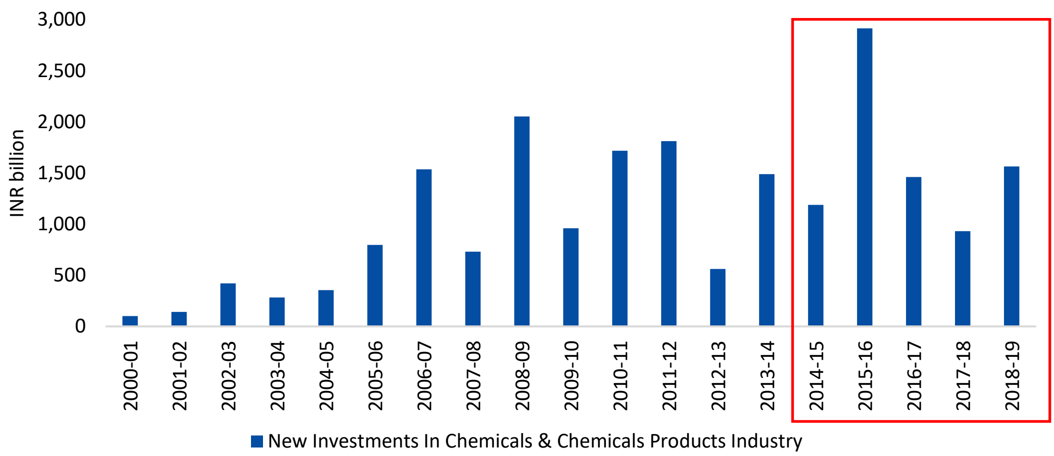
Source: Edelweiss Professional Investor Research

D. Capex is being undertaken to capitalise on this shift

Identifying the opportunity at hand, Indian chemical companies have undertaken significant capex in the last few years (to the tune of INR 14 lakh crore), a large part of which (around INR 8 lakh crore) happened in the last five years (Exhibit 55).

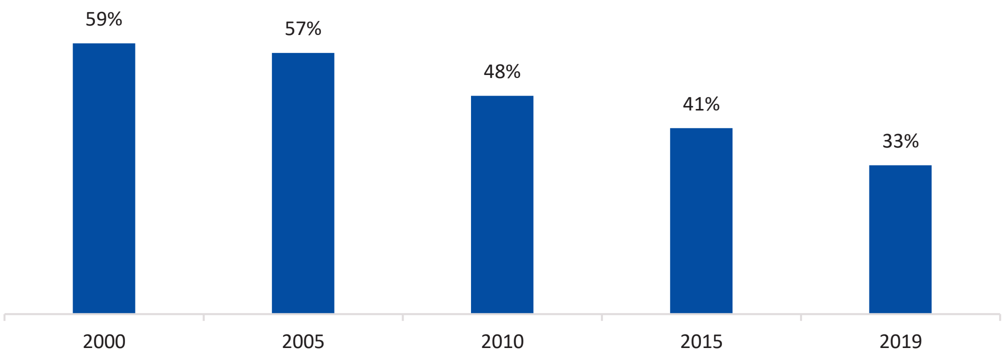
Capital expenditures have increased as companies started getting overseas mandates for manufacturing and identified domestic import substitution and export opportunities. Additionally government initiatives like 'Make in India' also helped in this regard.

Exhibit 55: INR 8 trillion of new capex was undertaken in the chemicals sector in the last 5 years



Source: CMIE, Edelweiss Professional Investor Research

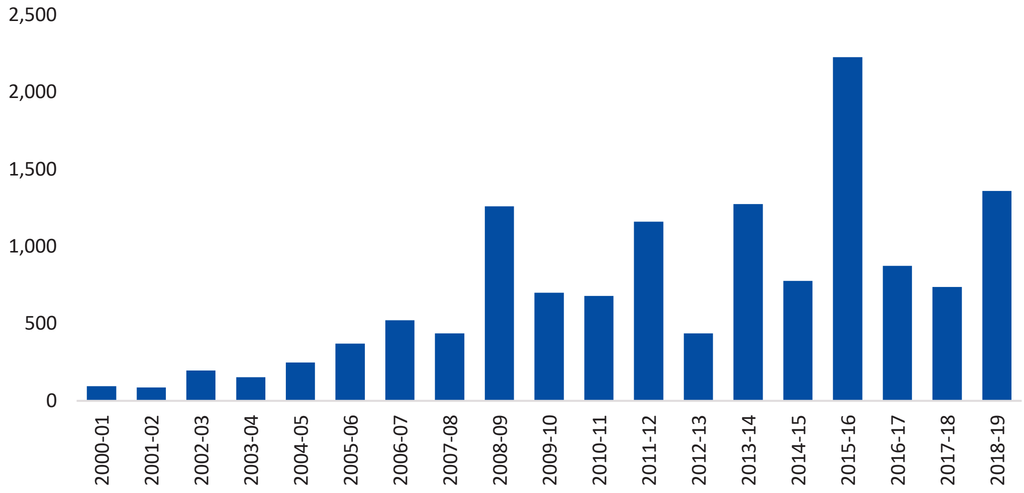
Exhibit 56: Proportion of chemical projects being implemented when compared to outstanding projects



Source: CMIE, NSE, Edelweiss Professional Research

India's capacity, although relatively smaller than several global peers, have increased at a rapid pace. At the end of each five year interval, the proportion of chemical projects under implementation was a large share of outstanding projects. In 2000, this metric stood at 59% owing to a much smaller base, but was a robust 33% in 2019 (despite a larger base).

Exhibit 57: Sizes of Capex has also increased (INR crore)



Source: CMIE, NSE, Edelweiss Professional Research

As we see in Exhibit 57, capital outlay per project has also increased in the last ten years. Increasing focus on downstream demand emanating from both domestic and export markets, and government initiatives like 'Make in India', PCPIRs etc. have played a key role in larger sized projects getting developed. In Exhibit 58, we list the key companies that have undertaken substantial capex or are planning to undertake capex.

With several downstream products in the petrochemical chain being largely imported, there remains a significant opportunity for domestic players for import substitution. We see players like Deepak Nitrite, Vinati Organics and Balaji Amines undertaking such initiatives.

Exhibit 58: Recent capex or capex plans by key chemical companies

Company	Details on recent capex undertaken	Future capex plans/guidances provided by management
Aarti Industries	Commissioned facility for first long-term contract in Q4FY20. FY20 capex is ~INR 1,200 cr.	Capex to be to the tune of INR 1,000-1,200 cr and capitalization of INR 1,400-1,500 cr in FY21. These include capex for long-term projects, NCB, Chlorination facility etc.
Alkyl Amines	Capex guidance for FY20 was INR 80-90 cr	Capex guidance for FY21 was INR 100-120 cr for Amines Derivatives and infrastructure
Balaji Amines	Commissioned brownfield capex for Acetonitrile, Morpholine and THF in FY20 after receiving MPCB approvals, as well as greenfield capacity in BSC	Undertaking INR 150 cr capex for Mega Project
Camlin Fine Science	Dahej plant commercial production expected to commence before end-FY20	
Deepak Nitrite	In FY20: INR 200-250 cr to be used for debottlenecking/brownfield expansion in base business and INR 100-150 for DPL. Commissioned IPA plant in April 2020.	Capex in pipeline for downstream projects.
Himadri Speciality Chemicals	Commissioned 60,000 MT of Specialty Carbon Black in FY20.	Advanced Carbon Materials capacities to be commissioned in phases
Fine Organics	3rd Ambernath Facility with 32,000 MT commenced operation in FY20	10,000 MT Patalganga facility and 10,000 MT German facility expected to be commissioned in FY21 and FY22 respectively
Galaxy Surfactants	FY19 capex was ~INR 170 cr, and in 9MFY20 has been over INR 110 cr, capex to be at similar level in FY20	
Navin Fluorine	Capex of INR 115 cr undertaken for cGMP3 plant for the CRAMS segment	INR 365 cr for manufacturing capacity for the recently won long-term contract and INR 71 cr for a captive power plant. Debottlenecking in Surat and further capex in Dahej for Specialty Chemicals
Neogen Chemical	Commissioned new inorganic chemicals facility in FY20	INR 75-80 cr capex for the doubling of capacity in the organic chemicals and ~INR 10 cr for debottlenecking. Will evaluate further capex needs as the new capacities reach close to optimal utilization
NOCIL	Capacity to double to 110,000 MT including that for captive consumption. Capex of INR 255 cr undertaken. First phase has come on stream in Q1FY19.	Second phase to be capitalized once orders are in place
OCCL		Insoluble Sulphur expansion in to be done in two phases of 5500 MT each to 45000 MT. Insoluble sulphur phase I capex and sulphuric acid to be commissioned in Q3FY21, for outlay of INR 216 cr including WC
PCBL		Addition of 32,000 MT of specialty carbon black expected in Q2FY21
SRF	Commissioned HFC plant in late FY20. BOPET line in Thailand has been commercialized and BOPET line in Hungary to be commissioned in Q2FY21.	Multiple projects across segments totalling to around INR 800 cr in expected capex in FY21: Specialty chemicals INR 238 cr capex for, INR 65 cr capex for HFC expansion and previously announced capex for BOPP plant in Thailand, NTCF Plant, Specialty Chemicals and PTFE
Sudarshan Chemical	Capex was expected to be INR 225-230 cr with remaining of INR 300 cr to spill over to FY21	
Vinati Organics	Butyl Phenols capacity has been commissioned, which required a capex of ~INR 150 cr	Additional capacity of ATBS of 14,000 MT to be commissioned by Q2FY21

E. Playing the themes in the chemical sector

With COVID-19 casting some shadow on the near-term earnings for most chemical companies, we would urge investors to look at the stocks in this sector with a longer-term investment horizon.

We see several players well positioned to reach leadership positions in their respective chemistries/areas of expertise over a medium to long-term horizon, through successful execution of strategies to take advantage of the tailwinds. Many of those players, however, are reasonably valued in the market, due to the quality of their business model and earnings visibility. This leaves us to play the earnings CAGR which will drive the stock price performance, which are in themselves quite robust for several companies, aided by the strong demand coming from both global and domestic markets. However, market volatilities could result in temporary drawdowns.

To play the themes in the chemical sector, we recommend two approaches.

First, invest in players who have already proven their mettle or are in the process of. Such players would share some of the following characteristics: 1) Building capacities of scale; 2) Have/building expertise in process chemistry; 3) Development of superior expertise in niche areas; and 4) Successful in integrating the value chain. These businesses generally have strong customer relationships and their control on processes helps them deliver products with consistent quality without much impact from disruptions, which enables them to further deepen their business relationships.

We believe players like SRF (BUY), PI Industries (Tactical BUY), Navin Fluorine (initiating coverage with BUY) and Aarti Industries (Tactical BUY) fit in this bucket.

The second way one can play the chemical growth story in India is through players who are ramping-up substantial capex or are currently undertaking large capex to respond to the domestic demand. Balaji Amines (BUY) has recently commissioned large capacities and growth in earnings is expected to be strong over FY21-23E. This, coupled with possible expansion in multiples, makes it an interesting play.

Deepak Nitrite (BUY) is also consistently undertaking forward integration, which would make it a suitable investment opportunity under this theme. Owing to its fully integrated nature, diversified business models and emerging scale Deepak Nitrite could see consistent earnings growth in future.

Company Section

Aarti Industries Ltd

Long-term growth story intact

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Aarti Industries (AIL) is a global leader in benzene-based derivatives and also operates in toluene and sulphur chemistries, which comprise its speciality chemicals segment. Its pharmaceuticals business manufactures active pharmaceutical ingredients (APIs) and active ingredients for generic players and innovators. With a large share of business accruing from overseas markets, AIL's business model remains diversified across customer segments, not only in terms of geography but also end-user industries. An integrated business model, diversified business mix and global partnerships would enable AIL to maintain consistent growth going forward. AIL's earning visibility is further bolstered by two long-term projects whose capacities are being developed and will start adding to the revenue stream FY22 onwards.

CMP: INR 935

RATING: Tactical Buy

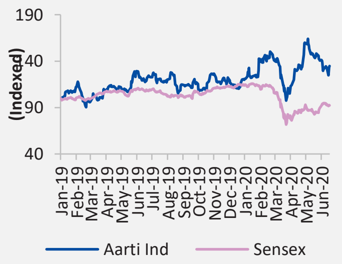
Target: INR 1,088

Upside: 16%

Key investment highlights

- AIL has an integrated business model spread across the 3 chemistries it operates in its speciality chemicals business: benzene chain, toluene chain and sulphur chain. It is the industry leader in key products and is regarded among the top-3 players in dichloride benzene (DCB) and nitro chloro benzene (NCB) products globally.
- The company has developed capabilities in undertaking reactions like chlorination and nitration (which contributes 30%) as well as in areas like ammonolysis, hydrogenation and halex chemistry. The company continues to focus on research and development, demonstrated by opening a new R&D centre with focus on newer chemistries like photochlorination, which could be a revenue contributor from FY23 onwards.
- A diverse set of products reduces product concentration risks with the top-10 products contributing 55% revenue in the speciality chemicals segment. AIL's products go to a host of end-industries like agrochemicals, dyes and pigments, polymer additives, etc.
- The company has a fast-growing pharma business, which exports a large share to both regulated and non-regulated markets. Products in this segment are in the area of APIs, active ingredients as well as xanthine derivatives.
- AIL has developed strong customer relationships with a large contribution in total sales from customers who have been with the company for more than 5 years. It has bagged long-term contracts, which provides earnings visibility.
- Capex guidance remains strong with ~INR 1,000-1,200 cr capex and ~INR 1,400-1500 cr capitalization in FY21, which would include capex for long-term contracts, NCB and chlorination plant among others.
- Management has guided that while growth in FY21 is expected to be flattish owing to demand side scenario (demand to remain strong in pharma and agro, while could be muted in other segments like polymers, colourants etc), 15-20% growth will resume post that.

Relative price performance



Bloomberg:	ARTO:IN
52-week range (INR):	668 /1,192
Share in issue (crore):	17
M-cap (INR crore):	16,103
Promoter holding (%)	47.75

Valuation and outlook

Given its strong, diversified and integrated business model, which provides earnings visibility and an expected earnings growth rate of 15-20% over FY21-23E post a flattish FY21 as guided by the management, we believe the valuation multiples will sustain and that growth over a longer period of time should remain robust, driven by higher demand from export markets. We remain positive on the company given its ability to create value for shareholders in the long run, and recommend a Tactical BUY, with a target price of INR 1,088, valuing the company at 25x FY22E EPS.

Year to March (INR crore)	FY18	FY19	FY20	FY21E	FY22E
Net revenue	3,806	4,705	4,620	4,208	5,212
EBITDA	699	965	977	1,091	1,419
Adjusted PAT	332	491	536	537	752
EBITDA margin (%)	14.5	17.0	17.1	20.2	21.5
PAT margin (%)	9.0	10.7	11.8	13.0	14.7
EPS basic (INR)	20.4	28.3	30.9	31.0	43.4
Diluted P/E (x)	45.1	32.5	29.8	29.7	21.2
EV/EBITDA (x)	24.5	18.3	18.0	16.4	12.1
RoCE (%)	16.6	18.1	16.0	16.2	18.9

Date: 18th June, 2020

Focus Charts

Exhibit 62: Revenue (INR crore)

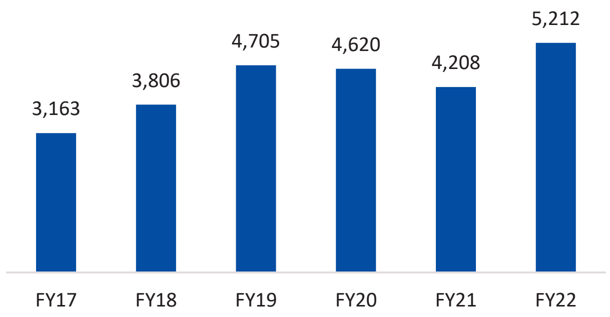


Exhibit 63: EBITDA (INR crore)

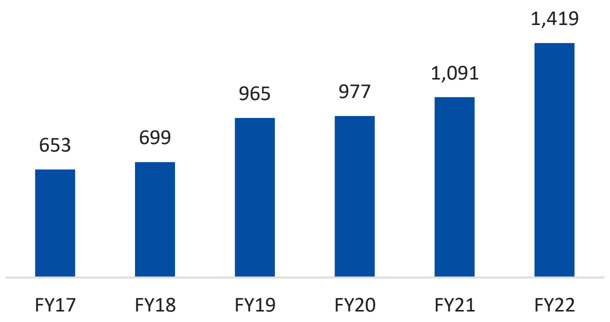


Exhibit 64: EBITDA margin (%)

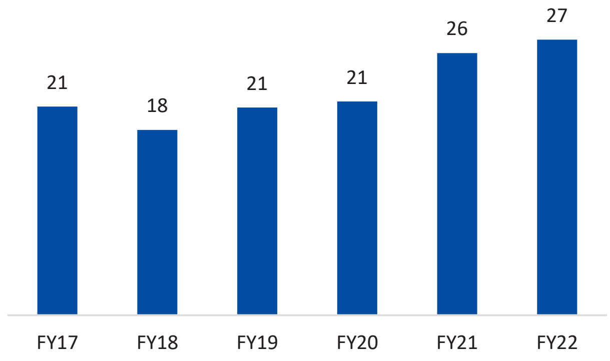


Exhibit 65: RoAE (%)

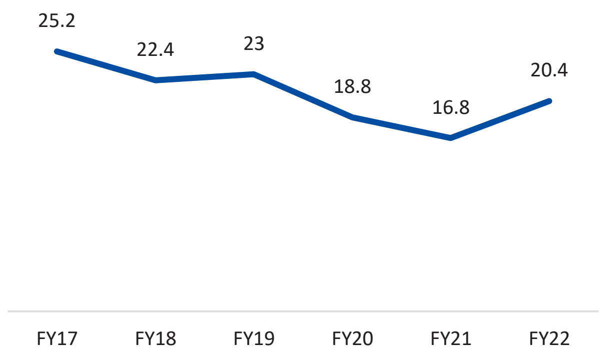


Exhibit 66: PAT (INR crore)

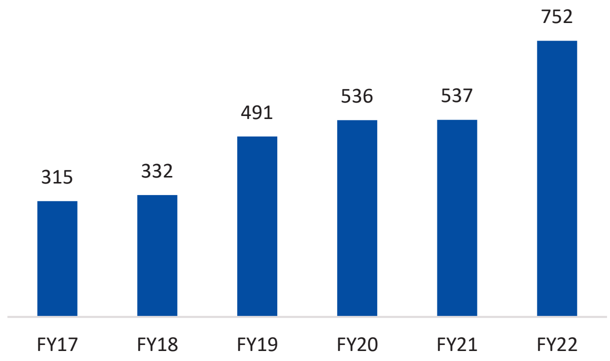
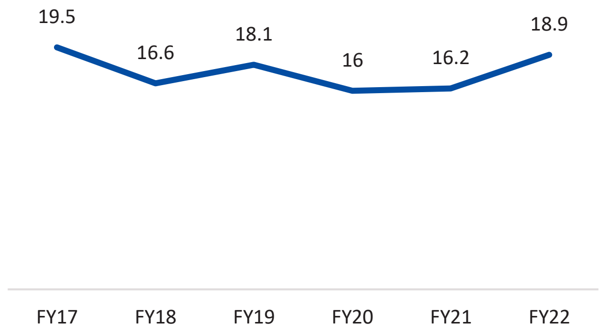


Exhibit 67: RoACE (%)



Source: Edelweiss Professional Investor Research

Company profile

Global leader in benzene derivatives

AIL manufactures benzene, toluene and sulphur-based derivatives and is a global leader in these segments. The company is among the top 3 players in NCB and DCB. Around 40% of its products are exported as the company has developed relationships with global partners.

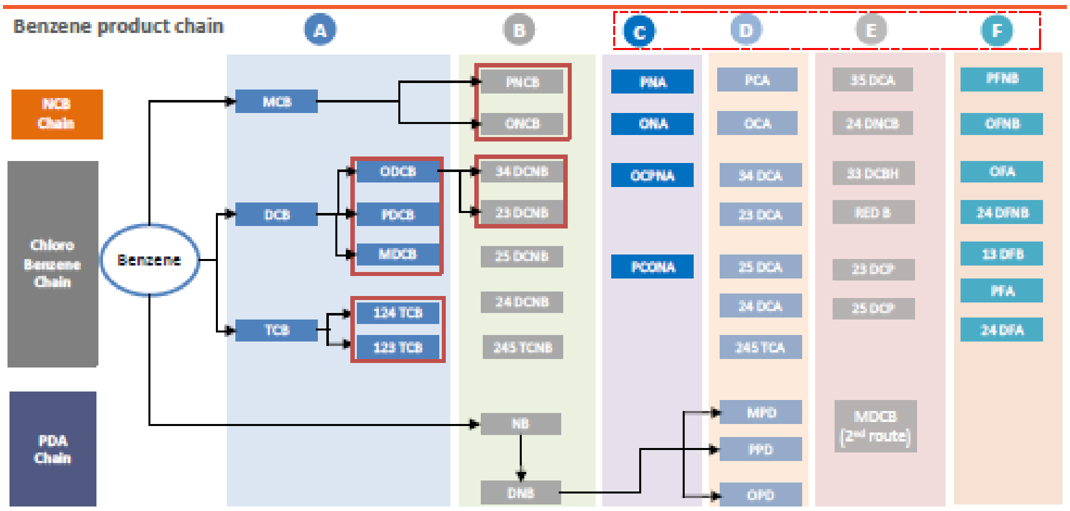
The business model is fully integrated and diversified with over 200 products and more than 400 global customers. The management's focus remains on cost optimisation across the plants it operates in 11 locations. Top 10 customers account for less than 30% of revenue, with the largest customer commanding a 4% share.

Strong growth track record across segments

AIL's revenue has grown at 11% CAGR during FY16-20, aided by volume growth in both business segments – speciality chemicals and pharmaceuticals. Over this period, CAGR in the pharma segment has exceeded that of the specialty chemicals segment.

Management has guided 15-20% growth to continue over FY22 onwards owing to ramp-up of new capex and growth in end-industries. FY21 is expected to be flattish due to demand side scenarios, where demand from agrochemicals and pharma customers are expected to be strong, while that for polymers, colourants etc. are expected to be muted.

Exhibit 59: Integrated business model of AIL in the Specialty Chemicals segment



Source: Company

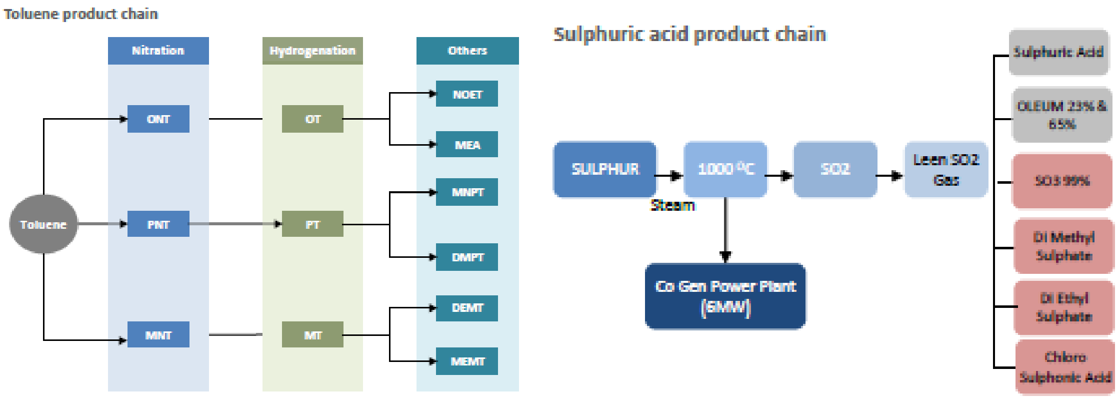
Specialty Chemicals segment is backward integrated and diversified

The specialty chemicals segment contributed 83% to FY20 revenue and has grown ~12% during FY16-20. This segment has applications across end-industries like agrochemicals, pharma, polymer additives, pigments and dyes. The business is fully integrated across benzene, toluene and sulphur chains as shown in exhibits 59 and 60. Chlorination and nitration accounts for around 30% of AIL's revenue, with the remaining 70% products being value-added and specialty in nature. Product mix remains fairly diversified with top 5 and 10 products contributing ~35% and ~55%, respectively.

The pharma segment is expected to show strong growth

The pharmaceuticals business contributed ~17% to the company's FY20 revenue. The business saw strong growth over the last 5 years, clocking 16% revenue CAGR over FY16-20. In this business, AIL supplies to generic pharma companies, both global and local, as well as global innovators. Pharma APIs and intermediates account for ~60% of the segment's revenue, while the remaining comes from xanthine derivatives with applications in beverages, nutraceuticals etc. The segment manufacturers intermediates used in drugs catering to anticancer, anti-asthma and antihypertensive drugs oncology therapies. Management expects the pharma segment to remain strong and is targeting 20-25% growth driven by volume and product mix change.

Exhibit 60: Integrated business model of AIL in the Specialty Chemicals segment



Source: Company

The pharma intermediate business has 4 plants, of which 2 are approved by US Food & Drug Administration (USFDA) and 2 are World Health Organisation (WHO)/good manufacturing practice (GMP) certified. Almost 50% of APIs business accrues from the domestic market and the remaining from exports (31% from regulated markets and 19% from non-regulated markets). As of FY19, this segment was manufacturing various commercial APIs, with 30 US drug master files, 12 DMFs (with seven under assessment) and 18 Certificate of Suitability (CEP, with two under assessment). Xanthine derivatives have a higher share of exports (~55%) to regulated and non-regulated markets.

Strong customer relationships

AIL has developed strong relationships with customers, with 9 out of top 10 customers being with the company for more than 5 years. Long-term customers contributed over 80% of total revenue. While a recent long-term contract was terminated due to the change of the customer's, AIL remains well protected under guarding provisions of contracts, with compensation of USD 120-130m to be received over FY21-FY22, covering for the capex undertaken and also a large share of the expected profitability from the project. Details of AIL's other long-term contracts are given below.

Exhibit 61: AIL's long-term contracts

Partnership/collaboration details	Year
A 20-year exclusive supply contract with a global chemical manufacturer (~INR 10,000 crore)	FY18
INR 900 crore contract to supply a specialty chemical intermediate to a global manufacturer	FY19

Source: AIL, Edelweiss Professional Investor Research

Income statement (INR Cr)	FY18	FY19	FY20	FY21E	FY22E
Net Revenue	3,806	4,705	4,620	4,208	5,212
Cost of materials consumed	2,181	2,694	2,490	2,020	2,606
Employee costs	190	242	305	351	421
Other Expenses	735	803	847	746	764
Total operating expenses excluding depreciation and amortisation	3,106	3,740	3,643	3,117	3,792
EBITDA	699	965	977	1,091	1,419
Depreciation & Amortization	146	162	185	240	294
EBIT	552	802	792	851	1,125
Interest expenses	131	182	124	179	185
Other income	7.77	2.1	8.84	7.5	7.5
Profit before tax	429	621	676	679	946
Provision for tax	82	117	129	129	179
Minority interest (before Core Profit)	13	12	10	12	14
Reported PAT	332	491	536	537	752
Adjusted PAT	332	491	536	537	752
Basic shares outstanding (mn)	16	17	17	17	17
Basic EPS (INR)	20.4	28.3	30.9	31	43.4
Diluted equity shares (mn)	16	17	17	17	17
Diluted EPS (INR)	20.4	28.3	30.9	31	43.4
CEPS (INR)	30.2	38.4	42.2	45.5	61.2
Dividend per share (INR)	1	5	5	8	8
Dividend payout (%)	5.9	21.3	19.5	31.1	22.2

Growth (%)	FY18	FY19	FY20	FY21E	FY22E
Revenues Growth	20.3	23.6	-2	-9	23.8
EBITDA Growth	6.9	38	1.2	11.6	30.1
EBIT Growth	4.1	45.1	-1	7.4	32.1
PBT Growth	3.2	44.9	8.7	0.4	39.3
Net profit Growth	5.4	47.6	9	0.3	39.9
EPS Growth	6.5	38.5	9	0.3	39.9

Balance sheet (INR Cr)	FY18	FY19	FY20	FY21E	FY22E
Equity capital	40	43	87	87	87
Reserves & surplus	1,537	2,587	2,891	3,261	3,846
Shareholders funds	1,578	2,630	2,978	3,348	3,933
Minority interest (BS)	77	83	94	106	121
Long term debt	908	814	580	580	580
Short term debt	1,174	1,586	1,229	1,629	1,629
Borrowings	2,083	2,401	1,810	2,210	2,210
Long Term Liabilities & Provisions	64	203	550	550	550
Deferred Tax liability	177	193	211	234	267
Sources of funds	3,979	5,511	5,645	6,451	7,084
Tangible assets	1,996	2,145	2,467	3,627	4,032
Intangible assets	1	1	0	0	0
CWIP (incl. intangible)	436	794	1,417	1,000	1,000
Non current investments	47	33	37	37	37
Cash and equivalents	32	804	247	402	1,103
Inventories	747	771	835	760	356
Sundry debtors	654	776	753	807	856
Loans and advances	449	497	540	540	540
Other current assets	25	34	32	32	32
Total current assets (ex cash)	1,878	2,079	2,162	2,140	1,786
Trade payable	357	279	345	415	535
Others current liabilities	54	66	341	341	341
Total current liabilities & provisions	411	346	686	756	877
Net current assets (ex cash)	1,466	1,733	1,475	1,383	909
Uses of funds	3,979	5,511	5,645	6,451	7,084
Book value per share (INR)	97	151.7	171.8	193.2	226.9

Free cash flow	FY18	FY19	FY20	FY21E	FY22E
Net profit	332	491	536	537	752
Depreciation	146	162	185	240	294
Interest (Net of Tax)	106	147	100	145	150
Others	52	55	87	62	75
Gross cash flow	339	729	1,515	1,077	1,747
Less: Changes in WC	298	127	-605	-91	-474
Less: Capex	613	669	1,130	982	700
Free Cash Flow	-274	60	385	95	1,047

Cash flow metrics	FY18	FY19	FY20	FY21E	FY22E
Operating cash flow	339	729	1,515	1,077	1,747
Financing cash flow	270	695	-947	52	-353
Investing cash flow	-606	-653	-1,125	-974	-692
Net Cash Flow	3	772	-556	155	701
Capex	-613	-669	-1,130	-982	-700
Dividend paid	-19	-104	-104	-167	-167

Profitability and efficiency ratios	FY18	FY19	FY20	FY21E	FY22E
ROAE (%)	22.4	23	18.8	16.8	20.4
ROACE (%)	16.6	18.1	16	16.2	18.9
Inventory day	110	102	117	144	78
Debtors days	56	55	60	67	58
Payable days	54	43	45	68	66
Cash conversion cycle (days)	111	115	132	143	69
Current ratio	4.6	8.3	3.5	3.3	3.2
Gross Debt/EBITDA	2.9	2.4	1.8	2	1.5
Gross Debt/Equity	1.2	0.8	0.5	0.6	0.5
Adjusted debt/equity	1.3	0.9	0.6	0.6	0.5
Net Debt/Equity	1.2	0.5	0.5	0.5	0.2
Interest coverage	4.1	4.3	6.3	4.7	6

Valuation parameters	FY18	FY19	FY20	FY21E	FY22E
EPS (INR) diluted	20.4	28.3	30.9	31	43.4
Y-o-Y growth (%)	6.5	38.5	9	0.3	39.9
Cash EPS	30.2	38.4	42.2	45.5	61.2
Diluted PE (x)	45.1	32.5	29.8	29.7	21.2
Price/BV (x)	9.5	6	5.3	4.7	4
EV/Sales (x)	4.2	3.5	3.6	4	3.1
EV/EBITDA (x)	24.5	18.3	18	16.4	12.1
Dividend yield (%)	0.1	0.5	0.5	0.8	0.8

Balaji Amines Ltd

New capacities provide multiple levers of growth

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Balaji Amines (BAL) is a leading player in aliphatic amines in India. It has a product portfolio of over 25 products, with leadership position in several of them. It is the sole domestic manufacturer for a few of these products. The aliphatic amines industry is oligopolistic in nature as there are considerable entry barriers in terms of technological knowhow, ability to handle hazardous chemicals, among others. The management had embarked on capacity expansion, which would result in considerable growth in top- and bottom-line, along with an expansion in product portfolio that would be import substitutes.

CMP: INR 445

RATING: BUY

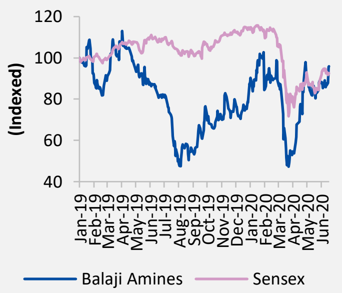
Target: INR 500

Upside: 12%

Key investment highlights

- BAL has received environmental clearance for its greenfield project in MIDC Chincholi, Solapur (Maharashtra). In Phase I of the project, the company intends to incur a capex of INR 150 crore, of which INR 35-50 crore has already been spent. The project would be fully funded through internal accruals. It has received 'mega project' status, which grants it certain tax benefits.
- It will manufacture ethylamines (50 million tonne/day) and dimethyl carbonate (DMC-30 MT/day) in the mega project. Both products are seeing growing end-use in pharmaceuticals/active pharmaceutical ingredients (API) space in India, with demand being largely met by imports. Additional tailwinds for DMC will accrue from the setting up of polycarbonate manufacturing facilities in India, where it is a feedstock. GAIL (India) has plans to manufacture the same. Phase I of the project is expected to be commissioned in Q4FY21. The management expects INR 200 crore in revenue in FY22, with INR 300-350 crore in revenue at full utilisation in FY23 and an EBITDA margin of 18-20% over this period.
- With the brownfield manufacturing facility coming on stream, the company can capitalise on higher prices of acetonitrile, which is currently trading ~INR 260/kg (as against normalised price levels of INR 140-160/kg). If prices sustain at this level, BAL may set up another plant with a capacity of 20 MT/day at a capex of INR 50-60 crore.
- BAL has increased supply of dimethylformamide (DMF) due to shortage in the market. As against the current market price of INR 60/kg, its breakeven price is INR 56-58/kg. This was the only key product in its existing business, which was running at low capacity utilisation due to the impact of dumping from China. Revenue from the standalone business is expected to be in the INR 1,000-1,050 crore range in FY20.
- Subsidiary Balaji Speciality Chemicals (BSC) will manufacture ethylenediamine (EDA), piperazine, diethylenetriamine (DETA) and AEEA, which should add INR 50/250-300/350 crore in FY20/21/22E, respectively. The company is expected to see strong demand as UPL, Coromandel International and Indofil Industries are likely to source 60% of their EDA requirement from BSC. The subsidiary has repaid INR 50 crore of the INR 75 crore loan taken from its parent company.

Relative price performance



Bloomberg:	BLA:IN
52-week range (INR):	200/489
Share in issue (crore):	3
M-cap (INR crore):	1,424
Promoter holding (%)	53.67

Valuation and outlook

We expect FY21 to be a strong year as utilisation of the newly added capacity of BAL/BSC improves. But keeping in view the delay that was experienced in starting new capacities and the current low pricing environment for chemicals, we have revised our FY21E/FY22E EPS to INR 39/45, respectively. We maintain our BUY recommendation with a target price of INR 500 per share, valuing the company ~11x FY22E EPS.

Year to March (INR crore)	FY18	FY19	FY20E	FY21E	FY22E
Net revenue	864	943	931	1126	1318
EBITDA	182	192	179	220	261
Adjusted PAT	113	115	103	126	147
EBITDA margin (%)	21.1	20.31	19.2	19.6	19.8
PAT margin (%)	13.0	12.16	11.10	11.21	11.15
EPS basic (INR)	35	35	32	39	45
Diluted P/E (x)	12.8	12.5	13.9	11.4	9.8
EV/EBITDA (x)	8.6	8.6	8.7	7.4	6.3
RoCE (%)	27.2	22.2	17.1	18.4	19.3

Date: 18th June, 2020

Focus Charts

Exhibit 68: Revenue (INR crore)

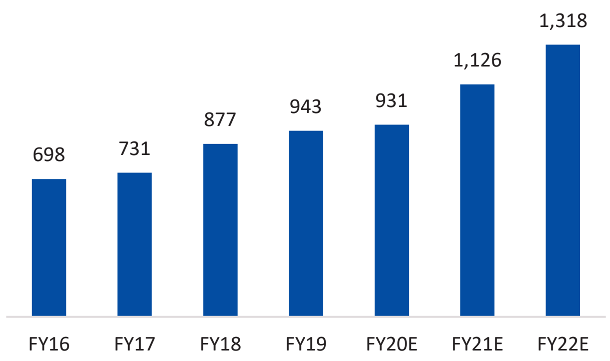


Exhibit 69: New capacities to drive growth in FY21/FY22

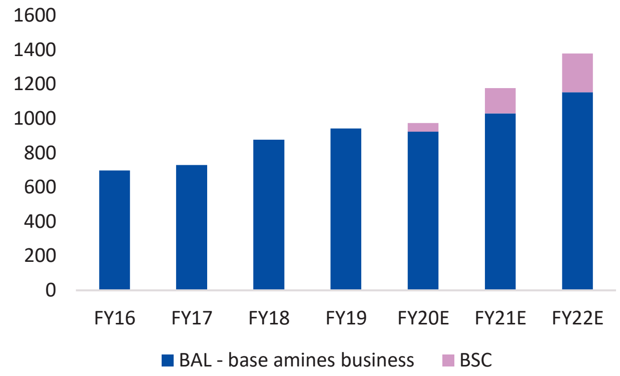


Exhibit 70: EBITDA (INR crore)

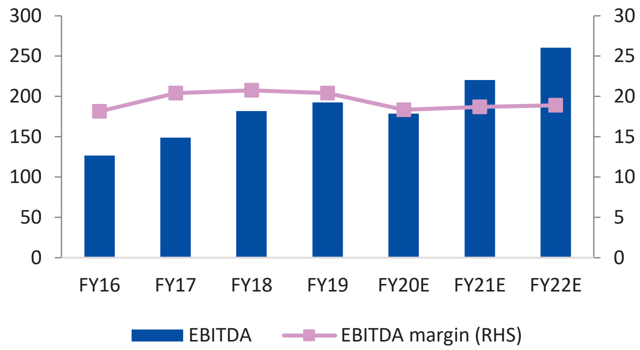


Exhibit 71: RoAE (%)

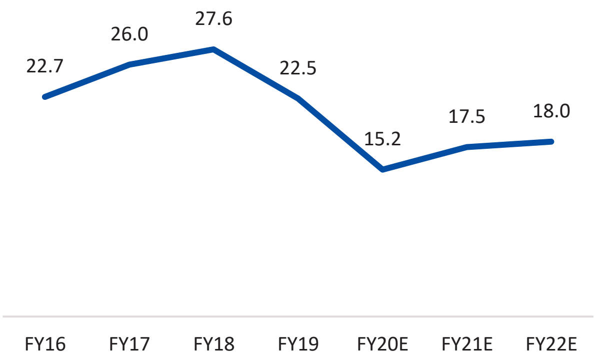


Exhibit 72: PAT (INR crore)

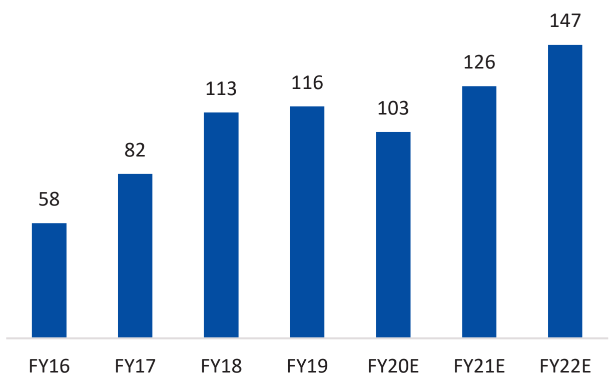
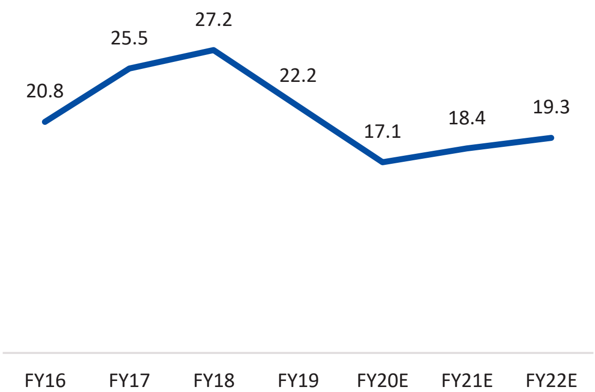


Exhibit 73: RoACE (%)



Source: Edelweiss Professional Investor Research

Income statement (INR crs)

Year to March	FY18	FY19	FY20E	FY21E	FY22E
Income from operations	864	943	931	1126	1318
Total operating expenses	682	751	752	906	1058
EBITDA	182	192	179	220	261
Depreciation and amortisation	19	20	29	29	35
EBIT	163	172	150	191	225
Interest expenses	9	13	26	23	21
Profit before tax	166	169	128	172	208
Provision for tax	53	52	34	45	54
Core profit	113	117	94	127	154
Minority interest	0	0	9	-1	-7
Extraordinary items	0	-2	0	0	0
Profit after tax	113	115	103	126	147
Adjusted net profit	113	115	103	126	147
Equity shares outstanding (mn)	3	3	3	3	3
EPS (INR) basic	35	35	32	39	45
Diluted shares (Cr)	3	3	3	3	3
EPS (INR) fully diluted	35	35	32	39	45
Dividend per share	3	3	2	3	3
Dividend payout (%)	7	7	7	7	7

Common size metrics- as % of net revenues (INR crs)

Year to March	FY18	FY19	FY20E	FY21E	FY22E
Operating expenses	78.9	79.7	80.8	80.4	80.2
Depreciation	2.2	2.1	3.1	2.6	2.7
Interest expenditure	1.0	1.4	2.8	2.0	1.6
EBITDA margins	21.1	20.31	19.2	19.6	19.8
Net profit margins	13.06	12.16	11.10	11.21	11.15

Growth metrics (%)

Year to March	FY18	FY19	FY20E	FY21E	FY22E
Revenues	28.8	9.2	(1.3)	20.9	17.1
EBITDA	22.1	5.2	(6.7)	23.2	18.3
PBT	31.9	1.7	(24.1)	34.5	21.0
Net profit	37.4	3.5	(19.5)	35.0	21.2
EPS	39.9	1.7	(9.9)	22.2	16.4

Balance sheet (INR Crs)

As on 31st March	FY18	FY19	FY20E	FY21E	FY22E
Equity share capital	6	6	6	6	6
Preference Share Capital	0	0	0	0	0
Reserves & surplus	461	568	664	781	917
Shareholders funds	467	574	671	788	924
Secured loans	143	213	85	85	85
Unsecured loans	9	14	5	5	5
Borrowings	152	227	90	90	90
Minority interest	18	18	18	18	18
Sources of funds	**637**	**819**	**779**	**896**	**1,032**
Gross block	479	502	702	852	852
Depreciation	163	182	211	240	275
Net block	316	320	491	612	576
Capital work in progress	124	269	60	20	80
Total fixed assets	440	589	551	632	656
Unrealised profit	0	0	0	0	0
Investments	0	0	0	0	0
Inventories	89	163	161	195	228
Sundry debtors	173	167	165	200	234
Cash and equivalents	31	21	22	8	69
Loans and advances	69	99	99	99	99
Other current assets	0	0	0	0	0
Total current assets	362	450	447	501	629
Sundry creditors and others	72	86	85	103	120
Provisions	75	79	79	79	79
Total CL & provisions	147	165	163	181	199
Net current assets	214	285	283	319	430
Net Deferred tax	-50	-46	-46	-46	-46
Misc expenditure	33	-9	-9	-9	-9
Uses of funds	**637**	**819**	**779**	**896**	**1,032**
Book value per share (INR)	144	177	207	243	285

Cash flow statement (INR crs)

Year to March	FY18	FY19	FY20E	FY21E	FY22E
Net profit	114	119	94	127	154
Add: Depreciation	19	20	29	29	35
Add: Misc expenses written off	-36	42	0	0	0
Add: Deferred tax	-1	-4	0	0	0
Gross cash flow	96	177	123	157	190
Less: Changes in W. C.	24	81	-3	51	50
Operating cash flow	72	96	127	106	140
Less: Capex	108	169	-9	110	0
Free cash flow	**-37**	**-74**	**136**	**-4**	**140**

Ratios

Year to March	FY18	FY19	FY20E	FY21E	FY22E
ROAE (%)	27.6	22.5	15.2	17.5	18.0
ROACE (%)	27.2	22.2	20.1	24.4	24.8
Debtors (days)	73	65	65	65	65
Current ratio	2.5	2.7	2.7	2.8	3.2
Debt/Equity	0.3	0.4	0.1	0.1	0.1
Inventory (days)	38	63	63	63	63
Payable (days)	30	33	33	33	33
Cash conversion cycle (days)	80	95	95	95	95
Debt/EBITDA	0.8	1.2	0.5	0.4	0.3
Adjusted debt/Equity	0.3	0.4	0.1	0.1	0.0

Valuation parameters

Year to March	FY18	FY19	FY20E	FY21E	FY22E
Diluted EPS (INR)	34.8	35.4	31.9	39.0	45.4
Y-o-Y growth (%)	*39.9*	*1.7*	*(9.9)*	*22.2*	*16.4*
CEPS (INR)	40.9	42.2	38.1	48.3	58.5
Diluted P/E (x)	12.8	12.6	14.0	11.4	9.8
Price/BV(x)	3.1	2.5	2.2	1.8	1.6
EV/Sales (x)	1.8	1.7	1.6	1.4	1.1
EV/EBITDA (x)	8.6	8.6	8.5	6.9	5.6
Diluted shares O/S	3.2	3.2	3.2	3.2	3.2
Basic EPS	34.8	35.4	31.9	39.0	45.4
Basic PE (x)	12.8	12.6	14.0	11.4	9.8
Dividend yield (%)	0.6	0.6	0.5	0.6	0.8

Deepak Nitrite Ltd

Tailwinds in multiple business lines

Deepak Nitrite (DEN) is a diversified chemical manufacturer that operates in 4 business segments: basic chemicals (BC), fine and specialty chemicals (FSC), performance products (PP) and manufactures phenol/acetone via its wholly owned subsidiary Deepak Phenolics (DPL). Its business model is integrated in nature in various sub-segments and several products have significant share in the domestic as well as global market. All business segments have been experiencing strong growth, with DPL continuing to run at record turnover levels.

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CMP: INR 462

RATING: BUY

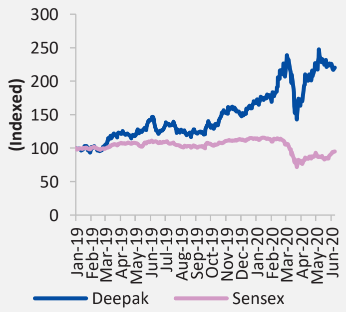
Target: INR 570

Upside: 23%

Key investment highlights

- The BC segment has seen strong growth during the last few quarters. Excluding the impact of loss of production during the lockdown, it saw sustained growth momentum on the back of increasing volumes due to cost leadership and increasing customer base. Its margin profile remained broadly stable sequentially. In this segment, DEN manufactures bulk chemicals like sodium nitrate and sodium nitrite.
- FSC returned to the growth path during Q3FY20, and Q4FY20 saw the segment maintain its elevated margin levels. Exports and changing product mix aided revenue growth and margin expansion. The management expects the strong run in FSC to continue, led by robust demand from end-segments like agrochemicals and pharmaceuticals, particularly in the overseas markets. Agrochemicals being a key end-industry could aid growth in this segment in FY21. FSC along with PP is a key driver of DEN's overseas sales, which has consistently increased as we highlight in Exhibit 75.
- The PP segment has benefited from short supply of optical brightening agent (OBA) intermediate diamino stilbene disulfonic acid (DASDA) due to environmental strictures in China. This resulted in strong playout of operating leverage in the segment and solid revenue and margin development. The segment also saw the impact of improving product mix in OBA products. Trends of normalization of DASDA prices are visible (a key export focused product), although the supply side remains intact with no new capacities added globally last year.
- DPL has been operating at high utilisation levels and has commissioned a plant of downstream acetone product isopropyl alcohol (IPA), which will reduce the impact of volatility in feedstock and finished good prices. The IPA facility that was commissioned in April will aid revenue in FY21. The management guided an annual run-rate of ~INR 300 crore (at current prices) from this product at optimum utilisation levels. IPA sees use in hand sanitisers and in the pharmaceutical industry and is seeing strong demand off late leading to better realizations.

Relative price performance



Bloomberg:	DN:IN
52-week range (INR):	257/568
Share in issue (crore):	14
M-cap (INR crore):	6,434
Promoter holding (%):	45.69

Valuation and outlook

DEN will continue to remain resilient in our opinion given its focus on forward integration (it has acquired land for future expansions at most locations that it operates from, with capex plans in pipeline) and a diversified business mix. Agrochemicals remains a key end-user industry for the company, which is a bright spot in the current scenario, and will aid the FSC segment. We expect an improvement in DPL's profitability to offset any effect of DASDA price normalization. We maintain our 'BUY' rating with a target price of INR 570 per share, valuing the company at 12.5x FY22E EPS compared to its current market valuation of 11x.

Year to March (INR crore)	FY18	FY19	FY20	FY21E	FY22E
Net revenue	1651	2700	4230	4420	4770
EBITDA	199	417	1025	933	1019
Adjusted PAT	83	176	611	556	621
EBITDA margin (%)	12.0	15.5	24.2	21.1	21.4
PAT margin (%)	12.0	13.1	12.2	11.0	10.7
EPS basic (INR)	6.1	12.9	44.8	40.8	45.6
Diluted P/E (x)	76.3	35.8	10.3	11.4	10.2
EV/EBITDA (x)	36.5	17.9	7.7	7.5	6.6
RoCE (%)	8.5	15.8	32.1	25.2	22.2

Date: 18th June, 2020

Focus Charts

Exhibit74: Revenue (INR crore)

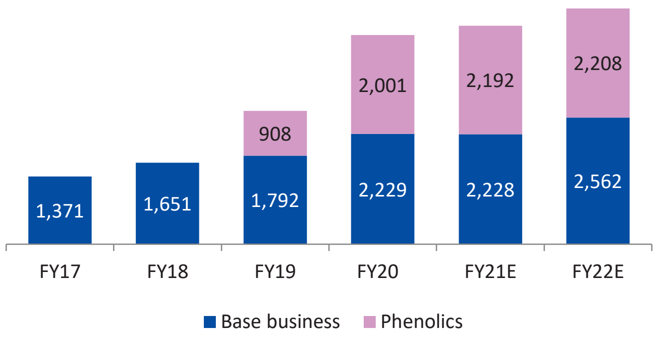


Exhibit 75: Rising share of exports in overall sales

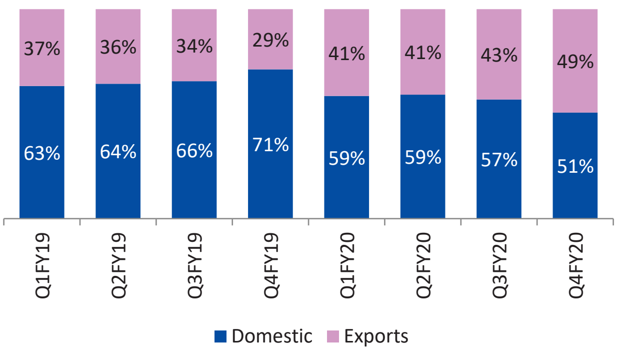


Exhibit 76: EBIT margin remains strong, improves across segments

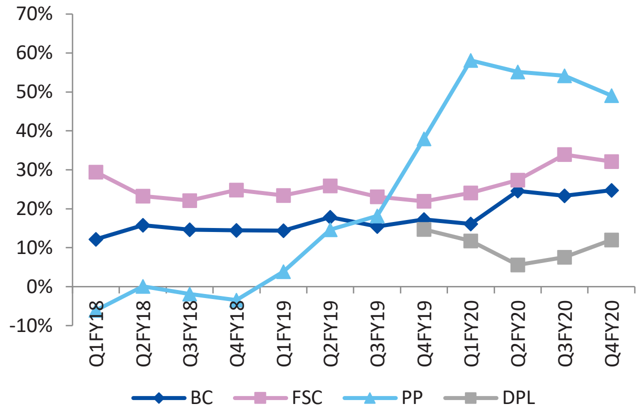


Exhibit 77: Consolidated PAT (INR crore)

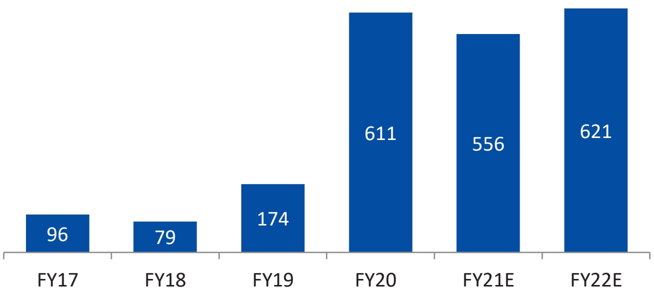


Exhibit 78: RoAE (%)

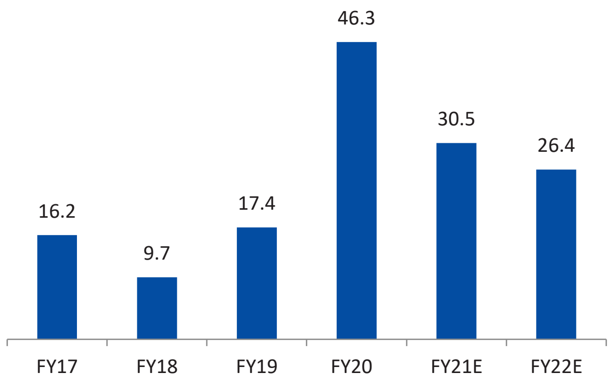
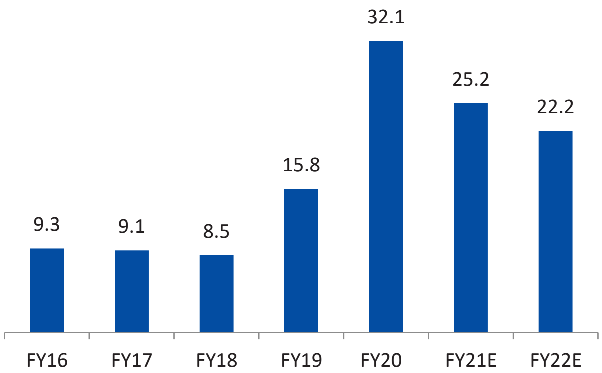


Exhibit 79: RoACE (%)



Source: Edelweiss Professional Investor Research

Income statement (Consolidated) (INR crs)

Year to March	FY18	FY19	FY20	FY21E	FY22E
Income from operations	1651	2700	4230	4420	4770
Direct costs	1134	1827	2658	2947	3177
Employee costs	136	180	219	219	219
Other expenses	319	455	546	540	574
Total operating expenses	1453	2283	3205	3486	3751
EBITDA	199	417	1025	933	1019
Depreciation and amortisation	53	78	140	141	141
EBIT	146	339	885	792	878
Interest expenses	47	87	115	108	108
Profit before tax	111	268	807	734	820
Provision for tax	32	94	195	178	199
Core profit	79	174	611	556	621
Extraordinary items	4	3	0	0	0
Profit after tax	83	176	611	556	621
Adjusted net profit	83	176	611	556	621
Equity shares outstanding (mn)	14	14	14	14	14
EPS (INR) basic	6	13	45	41	46
Diluted shares (Cr)	14	14	14	14	14
EPS (INR) fully diluted	6.1	12.9	44.8	41	46
Dividend per share	1	1	5	4	5
Dividend payout (%)	20	10	10	10	10

Common size metrics- as % of net revenues (INR crs)

Year to March	FY18	FY19	FY20	FY21E	FY22E
Operating expenses	88.0	84.5	75.8	78.9	78.6
Depreciation	3.2	2.9	3.3	3.2	3.0
Interest expenditure	2.9	3.2	2.7	2.4	2.3
EBITDA margins	12.0	15.5	24.2	21.1	21.4
Net profit margins	5.0	6.5	14.5	12.59	13.03

Growth metrics (%)

Year to March	FY18	FY19	FY20	FY21E	FY22E
Revenues	20.5	63.5	56.7	4.5	7.9
EBITDA	44.0	110.1	145.7	(8.9)	9.2
PBT	(17.6)	141.8	201.0	(9.0)	11.7
Net profit	78.0	113.2	246.5	(9.0)	11.7
EPS	70.5	113.2	246.5	(9.0)	11.7

Balance sheet (INR cr)

As on 31st March	FY18	FY19	FY20	FY21E	FY22E
Equity share capital	27	27	27	27	27
Preference Share Capital	0	0	0	0	0
Reserves & surplus	895	1,044	1,545	2,044	2,602
Shareholders funds	922	1,072	1,572	2,071	2,629
Secured loans	868	1,044	1,414	1,414	1,414
Unsecured loans	119	143	193	193	193
Borrowings	987	1,187	1,607	1,607	1,607
Minority interest	0	0	0	0	0
Sources of funds	**1,909**	**2,258**	**3,179**	**3,678**	**4,236**
Gross block	640	1,794	2,004	2,376	2,776
Depreciation	53	78	140	281	422
Net block	588	1,716	1,864	2,095	2,354
Capital work in progress	955	34	172	1	1
Total fixed assets	1,542	1,750	2,036	2,096	2,355
Unrealised profit	0	0	0	0	0
Investments	32	2	2	2	2
Inventories	327	418	395	685	739
Sundry debtors	412	575	613	941	1,016
Cash and equivalents	48	26	31	918	1,162
Loans and advances	178	150	0	0	0
Other current assets	0	0	0	0	0
Total current assets	965	1,169	1,039	2,544	2,916
Sundry creditors and others	608	556	723	910	982
Provisions	5	19	26	27	29
Total CL & provisions	613	574	749	937	1,010
Net current assets	352	595	290	1,607	1,906
Net Deferred tax	-45	-77	0	0	0
Misc expenditure	28	-11	-26	-26	-26
Uses of funds	**1,909**	**2,258**	**2,302**	**3,679**	**4,237**
Book value per share (INR)	68	79	115	152	193

Cash flow statement (INR cr)

Year to March	FY18	FY19	FY20	FY21E	FY22E
Net profit	79	174	611	556	621
Add: Depreciation	53	78	140	141	141
Add: Misc expenses written off	62	40	15	0	0
Add: Deferred tax	6	32	-77	0	0
Gross cash flow	200	323	688	698	763
Less: Changes in W. C.	-17	279	-311	431	55
Operating cash flow	217	44	999	267	707
Less: Capex	660	285	426	201	400
Free cash flow	**-443**	**-241**	**573**	**66**	**307**

Ratios

Year to March	FY18	FY19	FY20	FY21E	FY22E
ROAE (%)	9.7	17.4	46.3	30.5	26.4
ROACE (%)	8.5	15.8	32.1	25.2	22.2
Debtors (days)	91	78	78	78	78
Current ratio	1.6	2.0	1.4	2.7	2.9
Debt/Equity	1.1	1.1	1.0	0.8	0.6
Inventory (days)	72	57	57	57	57
Payable (days)	134	75	75	75	75
Cash conversion cycle (days)	29	59	59	59	59
Debt/EBITDA	5.0	2.8	1.6	1.7	1.6
Adjusted debt/Equity	1.0	1.1	1.0	0.3	0.2

Valuation parameters

Year to March	FY18	FY19	FY20	FY21E	FY22E
Diluted EPS (INR)	6.1	12.9	44.8	40.8	45.6
Y-o-Y growth (%)	*70.5*	*113.2*	*246.5*	*(9.0)*	*11.7*
CEPS (INR)	10	18	55	51	56
Diluted P/E (x)	76.3	35.8	10.3	11.3	10.2
Price/BV(x)	6.8	5.9	4.0	3.0	2.4
EV/Sales (x)	4.4	2.8	1.9	1.6	1.4
EV/EBITDA (x)	36.5	17.9	7.7	7.5	6.6
Diluted shares O/S	13.6	13.6	13.6	13.6	13.6
Basic EPS	6.1	12.9	44.8	40.8	45.6
Basic PE (x)	76.3	35.8	10.3	11.3	10.2
Dividend yield (%)	0.2	0.3	1.0	0.9	1.0

Long-term Recommendation
Navin Fluorine International

Edelweiss PROFESSIONAL INVESTOR RESEARCH
PMS • AIF • Prop Funds • Family offices

Compounding story in a niche industry

Swarnabha Mukherjee
Research Analyst
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CMP: INR 1,612

Rating: BUY

Target: INR 1,837

Upside: 15%

Navin Fluorine International (NFIL) is one of the pioneers in the fluorochemical space in India and operates in 4 business segments — refrigerants, inorganic fluorides, specialty chemicals and contract research and manufacturing services (CRAMS). It saw robust growth over the past 2 years across these segments (except for CRAMS in FY19 whose performance was impacted by order deferrals). With 2 recent multi-year deals being inked and CRAMS facility in Dewas commissioned in December 2019, we expect these segments to be key growth drivers going forward. CRAMS is now at an inflection point with the larger capacity cGMP plant commissioned which has a strong order pipeline. We expect NFIL to gain traction in its specialty chemicals business and see increasing use of HCFC-22 for non-emissive purposes, which would cushion any outcome of the production cut for emissive usage. Additionally, a larger contribution from higher value businesses in the mix would result in improving profitability.

Key investment highlights

- NFIL has entered into an INR 2,900 crore multi-year deal with a global company for manufacture and supply of a high performance product. This is the start of a new leg of growth as it establishes its fluorination capabilities in high performance product segments. The product is a new age application of fluorine molecule and not part of NFIL's existing portfolio.

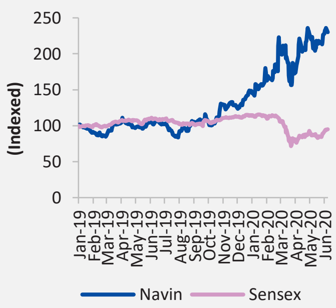
- Its specialty chemicals business, which manufactures niche molecules, is seeing strong traction from pharma, agro and industrial customers with a large share going to overseas customers. With strong growth clocked by this segment (33% in FY19 and 27% in FY20), the outlook remains strong. Growth in FY21 is expected to come from the Industrial chemicals which constitute 20% of the segment's revenue, and is expected to be in similar lines as of FY20.

- In CRAMS, with the commissioning of the cGMP3 plant in December last year, NFIL has seen new projects getting signed up and product enquiries coming in. The management has guided that the full impact will be visible in Q1FY21, with optimal capacity reached in the next 3-4 years. Its customers include pharma innovator companies based out of Europe and the US. Subsidiary Manchester Organics (MOL) is playing a key role in improving access to innovator companies.

- The refrigerant gas business continues to see demand from non-emissive uses. The management also intends to move into new age refrigerant gases in future. Management has plans of moving into the HFCs and HFOs segments. However, this segment may see performance moderate due to a reduced end industry demand due to the ongoing COVID-19 crisis.

- In inorganic fluorides, which sees major use in the steel and glass industry, NFIL has managed to maintain realisation and volumes. The same is expected to improve as the situation in end-industries improve.

Relative price performance (CHART WRONG)



Bloomberg:	NFIL:IN
52-week range (INR):	568/257
Share in issue (crore):	5
M-cap (INR crore):	7,722
Promoter holding (%)	30.51

Valuation and outlook

Owing to multiple growth levers that NFIL enjoys, it is capable of ~24% revenue CAGR over FY20E-23E, in our view. In the near term, specialty chemicals and CRAMS will be the key growth drivers with incremental growth coming from Navin Fluorine Advance Sciences (FY23E onwards). There could be further improvement to the earnings outlook as new deals are undertaken by NFASL (most of which will accrue from FY23 onwards)/CRAMS and addition of new molecules (in specialty chemicals)/products. We believe that NFIL is well positioned to cement its position as a key fluorochemicals player globally on the back of these capabilities. We initiate coverage with a target price of INR 1,837, valuing the company at 22x its FY23E EPS. We believe that NFIL will see its valuation multiples sustain, resulting in investment gains emanating from robust earnings momentum.

Year to March (INR crore)	FY19	FY20	FY21E	FY22E	FY23E
Net revenue	1000	1062	1215	1479	2046
EBITDA	222	263	318	415	582
Adjusted PAT	148	194	208	296	413
EBITDA margin (%)	22.2	24.8	26.2	28.1	28.4
PAT margin (%)	14.8	18.3	17.2	20.0	20.2
EPS basic (INR)	30	39	42	60	83
Diluted P/E (x)	53.6	40.9	38.0	26.7	19.2
EV/EBITDA (x)	35.5	29.0	23.7	18.1	12.8
RoCE (%)	18.2	18.0	18.6	21.6	26.6

Date: 18th June, 2020

Focus Charts

Exhibit 83: Revenue (INR crore)

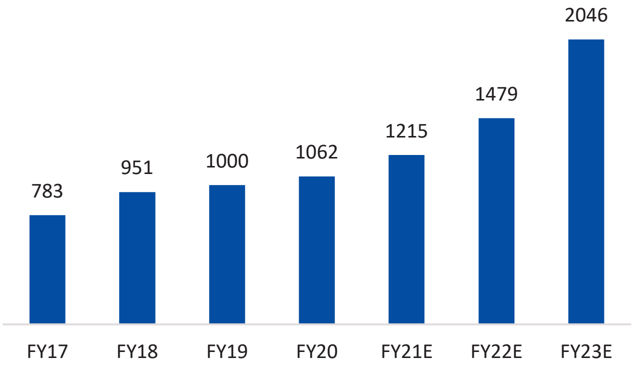


Exhibit 84: Growing share of high value businesses

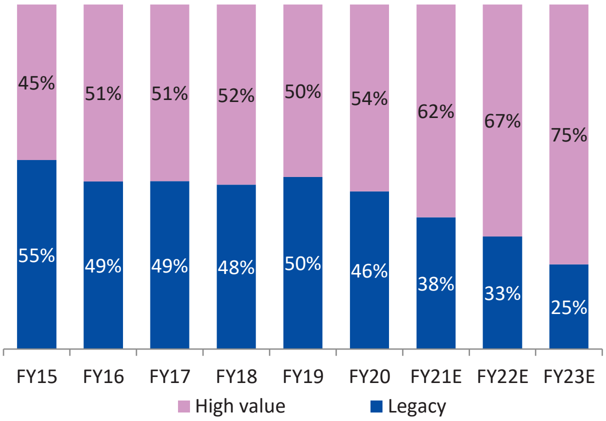


Exhibit 85: EBITDA (INR crore)

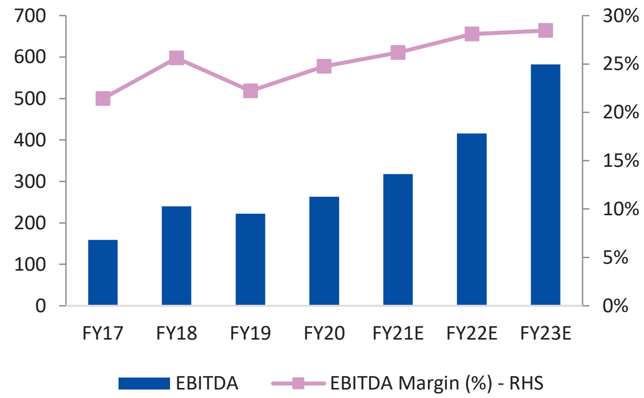


Exhibit 86: RoAE (%)

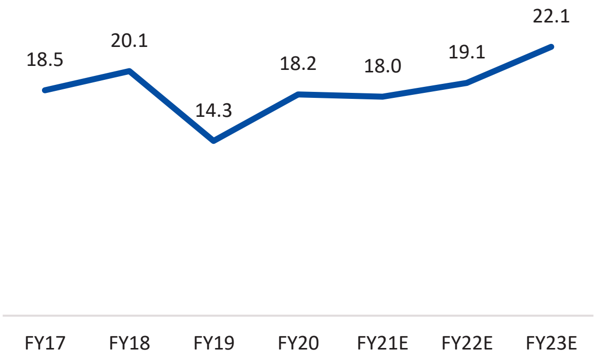


Exhibit 87: PAT (INR crore)

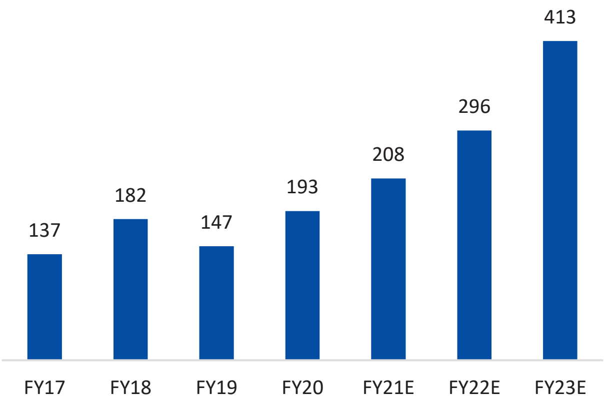
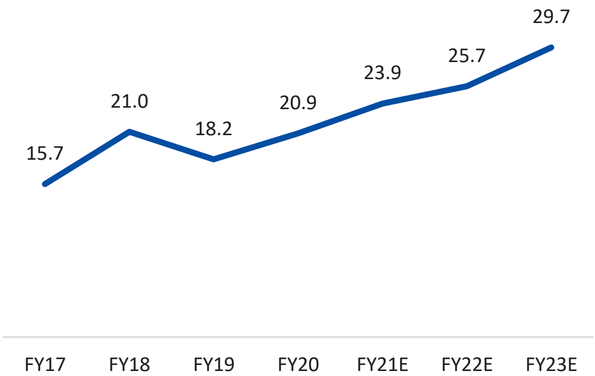


Exhibit 88: RoACE (%)



Source: Edelweiss Professional Investor Research

Company profile

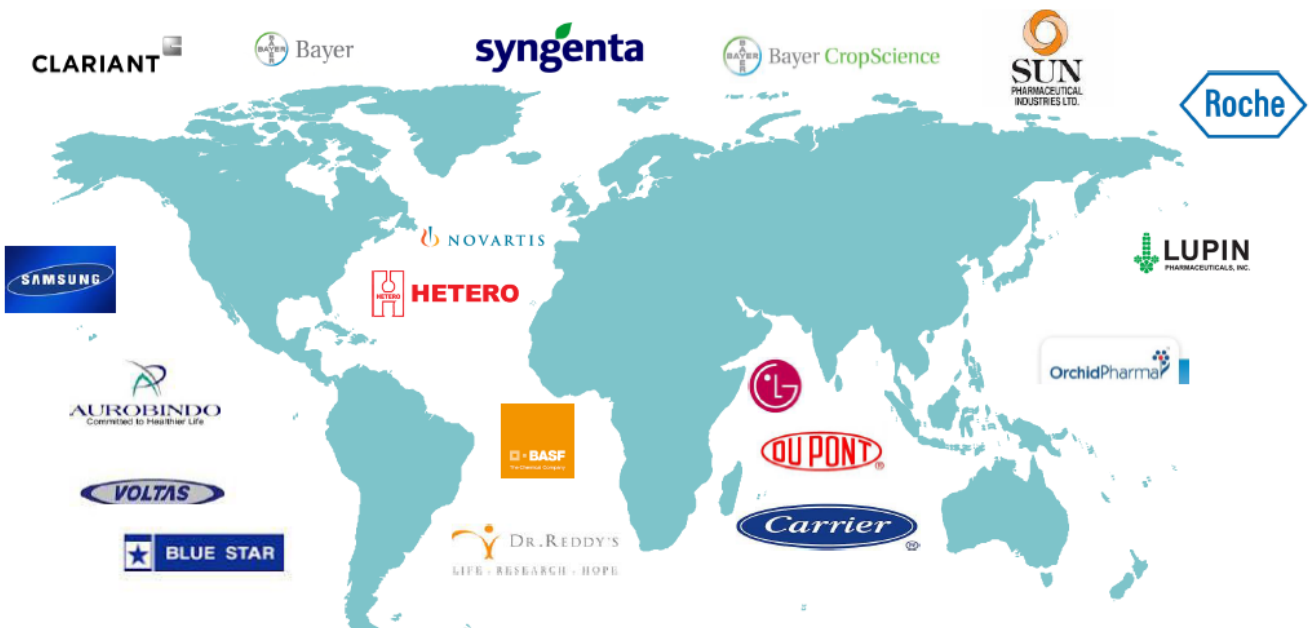
Well positioned to capture sectoral tailwind

NFIL has a fairly even revenue mix with both high value (specialty chemicals and CRAMS) and legacy (refrigerant gases and inorganic fluoride) segments contributing around 54%: 46% in the revenue mix in FY20. We expect this to change significantly over the next 3 years. By FY23E, the share of high value businesses could rise to around three quarters of the pie.

Such high growth in the newer age applications of fluorination stems from sectoral development. Fluorine, owing to its properties, increases the efficacy of drugs and absorption in the body (fluorine is lipophilic – soluble in fat). This is the key reason for high demand for fluoro-specialty products from pharma and agrochemical segments.

NFIL has marquee clients across segments as shown in Exhibit 80.

Exhibit 80: NFIL's key clients



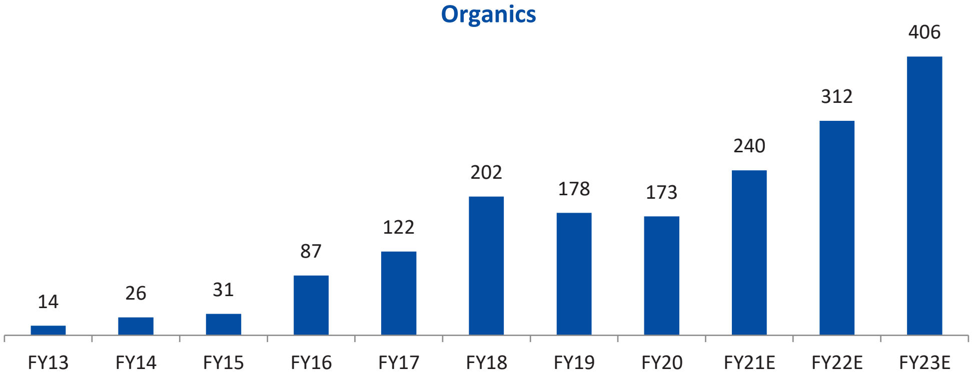
Source: NFIL

CRAMS: The growth lever

The company's CRAMS business had a lacklustre FY19 due to order deferrals. However, tailwinds in this segment are now visible with the signing of a multi-year sales agreement with one key US pharma client for a commercialised molecule. The cGMP3 plant has come on stream in Q3FY20 and is expected to ramp up in 3-4 years with an asset turnover of 2.25-2.5x at full utilisation. We expect CRAMS to be one of the primary growth levers over FY21-23E due to the above developments.

NFIL has seen new projects getting signed up and product enquiries coming in. The management has guided that the full impact will be visible in Q1FY21. NFIL's customers include pharma innovator companies based out of Europe and the US.

Exhibit 81: Revenue from the CRAMS segment excluding Manchester Organics



New contract further bolsters earnings outlook

NFIL has struck a new deal worth INR 2,900 crore, which is a 7-year contract for a high performance product not currently in its portfolio. This would entail a capex of INR 436 crore, of which INR 365 crore will be used to develop a manufacturing facility and remaining for a captive power plant. The management highlighted that the product enjoys a tailwind and the customer, who already manufactures this product, needed new production facilities which resulted in this contract.

This a reflection of NFIL's capabilities in complex fluorine chemistry. We expect the company to crack more such deals in the future, which will be a key driver of earnings growth. The business will operate through NFASL, a wholly-owned subsidiary. The management guided that revenue for the project is expected to start from Q4FY22.

Revenue is expected to be evenly distributed over the contract period. The project will have an asset turnover of 1.2x and a margin profile similar to the current business. At present, the management intends to finance the project from internal accruals.

Specialty chemicals: On a strong footing

NFIL's specialty chemicals business is gaining strong traction in pharma, agrochemical and industrial chemical segments, led by new product launches. It manufactures niche molecules, which are used in pharma and agrochemical industries, and services global players in life science, crop science and petrochemical space.

Around 40% of business comes from agrochemicals, which depend on customer relationships and development of new molecules. Another 40% of business accrues from pharma companies and relates to generic and fluoromolecules, which are going off patent. Industrial application of fluorochemicals contributes 20% to the specialty business.

This segment contributed 37% to topline in FY20 and we see continued growth ahead. The company has a portfolio of around 20+ products and is currently running ~85% capacity utilisation in the segment at its Surat facility. This segment will see solid growth going forwards due to higher off-take of fluorinated molecules in the agrochemical space. Growth in FY20/21 will be coming from debottlenecking in Surat, while capex for new opportunities will be undertaken at Dahej, which will aid in growth from the later part of FY22.

Legacy businesses continue to provide opportunities

NFIL's refrigerants business contributes ~26% to the company's overall revenue in FY20. It manufactures HCFC-22 refrigerant gas, which is sold under the Mafron brand. As this gas has high global warming potential, its emissive usage is being reduced. In India, HCFC-22 is to be phased out by 2030 and 25% reduction has been applied from January 1, 2020 (10% reduction already in place).

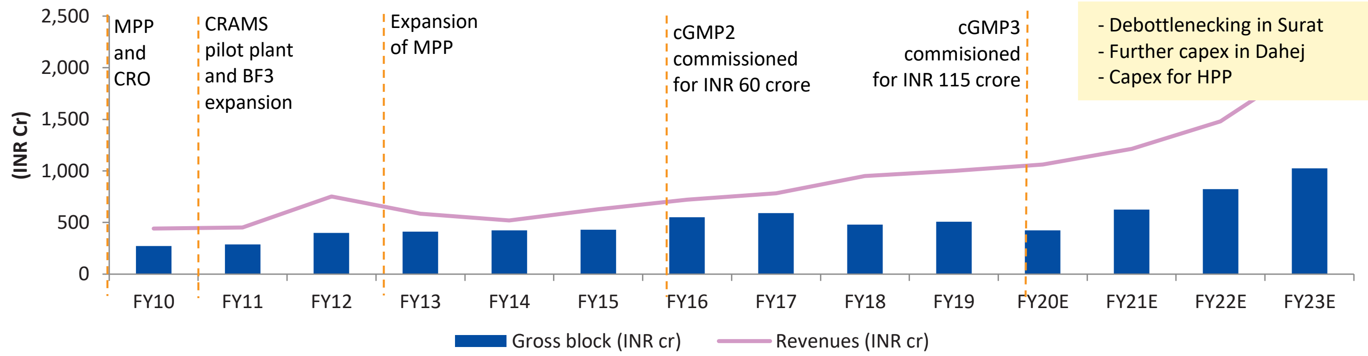
A loss of production due to the aforementioned cut is expected to be offset by increase in prices of HCFC-22 due to lower supply and strong demand, particularly in export markets and for non-emissive uses in the pharma industry. International business contributes ~44% to the segment's revenue. The management expects this segment to see flattish trends in FY21, while future growth opportunities remain in expanding into HFCs and HFOs.

Inorganic fluorides, which see major use in the steel and glass industry, have managed to maintain realisation and volumes, which are expected to improve as the situation in end-industries improve.

Capex outlook positive

NFIL had earlier announced a capex of over INR 450 crore for Dahej. The management has guided that further capex announcements may come over and above the INR 436 crore that is being undertaken for the current deal under Navin Fluorine Advanced Sciences (NFASL). At present, capex will be undertaken from internal accruals (including debottlenecking in Surat). However, a mix of debt and internal accruals can be used in future if needed.

Exhibit 82: NFIL has historically supported growth by timely capex



Source: Edelweiss Professional Investor Research

Income statement					(INR crs)
Year to March	**FY19**	**FY20**	**FY21E**	**FY22E**	**FY23E**
Income from operations	1000	1062	1215	1479	2046
Total operating expenses	778	798	897	1064	1464
EBITDA	222	263	318	415	582
Depreciation and amortisation	28	37	43	58	73
EBIT	195	226	275	357	509
Interest expenses	1	2	2	2	2
Profit before tax	224	258	311	398	555
Provision for tax	77	64	103	102	142
Core profit	147	194	208	296	413
Extraordinary items	0	0	0	0	0
Profit after tax	148	409	208	296	413
Adjusted net profit	148	194	208	296	413
Equity shares outstanding (mn)	5	5	5	5	5
EPS (INR) basic	30	39	42	60	83
Diluted shares (Cr)	5	5	5	5	5
EPS (INR) fully diluted	30	39	42	60	83
Dividend per share	8	11	12	17	23
Dividend payout (%)	26	28	28	28	28

Common size metrics- as % of net revenues					(INR crs)
Year to March	**FY19**	**FY20**	**FY21E**	**FY22E**	**FY23E**
Operating expenses	77.8	75.2	73.8	71.9	71.6
Depreciation	2.8	3.5	3.6	3.9	3.6
Interest expenditure	0.1	0.2	0.2	0.1	0.1
EBITDA margins	22.2	24.8	26.2	28.1	28.4
Net profit margins	14.8	18.3	17.2	20.0	20.2

Growth metrics (%)					
Year to March	**FY19**	**FY20**	**FY21E**	**FY22E**	**FY23E**
Revenues	6.6	6.2	14.5	21.7	38.3
EBITDA	(7.6)	18.7	20.7	30.6	40.1
PBT	(15.8)	14.9	20.6	28.1	39.4
Net profit	(19.2)	31.4	7.5	42.2	39.4
EPS	(20.5)	31.1	7.5	42.2	39.4

Navin Fluorine International

Financials

Balance sheet					(INR crs)
As on 31st March	**FY19**	**FY20**	**FY21E**	**FY22E**	**FY23E**
Equity share capital	10	10	10	10	10
Preference Share Capital	0	0	0	0	0
Reserves & surplus	1,063	1,402	1,552	1,765	2,062
Shareholders funds	1,072	1,412	1,562	1,775	2,072
Secured loans	0	0	0	0	0
Unsecured loans	0	0	0	0	0
Borrowings	4	1	1	1	1
Minority interest	0	0	0	0	0
Sources of funds	**1,077**	**1,414**	**1,563**	**1,777**	**2,074**
Gross block	509	480	680	880	1,080
Depreciation	79	116	159	218	291
Net block	430	364	521	662	789
Capital work in progress	39	39	200	200	200
Total fixed assets	470	403	721	862	989
Unrealised profit	0	0	0	0	0
Investments	427	155	155	155	155
Inventories	112	158	181	220	304
Sundry debtors	173	218	250	304	421
Cash and equivalents	37	284	372	390	446
Loans and advances	51	12	14	17	23
Other current assets	0	0	0	0	0
Total current assets	372	672	817	931	1,194
Sundry creditors and others	134	173	198	241	333
Provisions	38	3	3	3	3
Total CL & provisions	173	176	201	244	337
Net current assets	200	496	616	687	858
Net Deferred tax	-35	15	15	15	15
Misc expenditure	15	57	57	57	57
Uses of funds	**1,077**	**1,126**	**1,563**	**1,777**	**2,074**
Book value per share (INR)	217	285	316	359	419

Cash flow statement					(INR crs)
Year to March	**FY19**	**FY20**	**FY21E**	**FY22E**	**FY23E**
Net profit	147	194	208	296	413
Add: Depreciation	28	37	43	58	73
Add: Misc expenses written off	-18	-42	0	0	0
Add: Deferred tax	4	-50	0	0	0
Gross cash flow	160	139	252	355	486
Less: Changes in W. C.	46	50	31	53	115
Operating cash flow	115	89	221	301	371
Less: Capex	49	-29	361	200	200
Free cash flow	**65**	**118**	**-140**	**101**	**171**

Ratios

Year to March	FY19	FY20	FY21E	FY22E	FY23E
ROAE (%)	14.3	15.6	14.0	17.8	21.5
ROACE (%)	18.2	18.0	18.6	21.6	26.6
Debtors (days)	63	75	75	75	75
Current ratio	2.2	3.8	4.1	3.8	3.5
Debt/Equity	0.0	0.0	0.0	0.0	0.0
Inventory (days)	41	54	54	54	54
Payable (days)	49	59	59	59	59
Cash conversion cycle (days)	55	70	70	70	70
Debt/EBITDA	0.0	0.0	0.0	0.0	0.0
Adjusted debt/Equity	0.0	-0.2	-0.2	-0.2	-0.2

Valuation parameters

Year to March	FY19	FY20	FY21E	FY22E	FY23E
Diluted EPS (INR)	29.9	39.2	42.1	59.9	83.5
Y-o-Y growth (%)	*(20.5)*	*31.1*	*7.5*	*42.2*	*39.4*
CEPS (INR)	35	47	51	72	98
Diluted P/E (x)	53.6	40.9	38.0	26.7	19.2
Price/BV(x)	7.4	5.6	5.1	4.5	3.8
EV/Sales (x)	7.9	7.2	6.2	5.1	3.7
EV/EBITDA (x)	35.5	29.0	23.7	18.1	12.8
Diluted shares O/S	4.9	4.9	4.9	4.9	4.9
Basic EPS	29.9	39.2	42.1	59.9	83.5
Basic PE (x)	53.6	40.9	38.0	26.7	19.2
Dividend yield (%)	0.5	0.7	0.7	1.1	1.5

PI Industries Ltd

Trinity of factors driving growth

PI Industries (PIIL) is a key player in the agrochemical space, with around two-third revenue being contributed by the high value custom synthesis and manufacturing business (CSM), and the balance accruing from domestic agrochemical distribution business. It has seen strong growth in its CSM business by virtue of a strong order book and key chemistry capabilities that it has developed. This, along with the Isagro (Asia) Agrochemicals acquisition and further growth that may accrue from utilisation of the planned fund raise, gives us confidence on its long term growth trajectory.

Swarnabha Mukherjee
Research Analyst
swarnabha.mukherjee@edelweissfin.com

CMP: INR 1,584

RATING: Tactical Buy

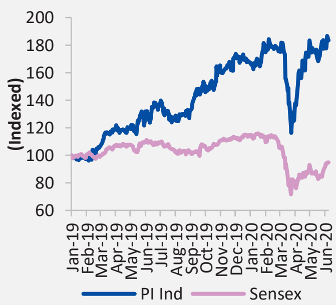
Target: INR 1,837

Upside: 16%

Key investment highlights

- Being a player in the agrochemical CSM space, PIIL partners with global innovators in development, scale up and commercialisation of products.
- This segment is seeing increasing contribution as PIIL continues to undertake R&D and offered a larger bouquet of chemistry capabilities to its customers. This would be a key driver of growth and profitability ahead. The company's abilities in process research, undertake complex chemistries and deliver products across batch sizes, while maintaining consistent quality, are key competitive advantages.
- PIIL's CSM business is primarily in patented molecules (over 90% share), which provides it order book visibility. Its current order book stands at USD1.5bn, which will be executed over the next few years.
- Recently, the company has diversified into the pharma segment and has developed an intermediate for a promising COVID-19 drug, in which it is currently operating at a pilot scale and working towards commercialization, with tie ups with customers in Japan and India. Over the next few years, the management intends contribution from pharma sector to be in double digits.
- Over FY16-20E, PIIL has clocked ~11% CAGR in revenue, primarily driven by ~17% growth in the CSM business, while revenue growth for the domestic business remained flattish. This has resulted in CSM's share increasing to ~72% in FY20 from under ~58% in FY16.
- The uniqueness of its domestic business model lies in the fact that the company in-licences or co-markets products with global partners for the domestic agrochemical market. In the domestic market, PIIL has come up with several successful brands like Nominee Gold, Osheen etc, and has recently seen traction in wheat herbicide Awkira.
- We see inorganic growth opportunities over FY21-22 as it recently acquired Isagro Spa's domestic arm. Isagro (Asia) Agrochemicals' plant is adjacent to PIIL's Panoli plant and provides it additional space, synergistic product portfolio, and a CSM agreement with Isagro Spa.
- A qualified institutional placement (QIP) of INR 2,000 crore will help it explore opportunities in CSM and allied spaces in pharmaceuticals or specialty chemicals in personal care, imaging chemicals, electronic chemicals etc.
- PIIL is undertaking consistent capex to fuel growth. Capex in FY20 was at INR 635 cr, while capex in FY21 is expected to be at INR 600 cr.
- Management has retained 20%+ growth guidance for FY21, on the back of encouraging commentary from global customers, expectation of a good monsoon in India and ramp-up in Isagro.

Relative price performance



Bloomberg:	PI:IN
52-week range (INR):	2,468/4,260
Share in issue (crore):	50
M-cap (INR crore):	22,365
Promoter holding (%)	51.35

Valuation and outlook

PIIL's unique business model, fast growing CSM business, a strong balance sheet, and entry into the pharma segment (we believe that PIIL will get increasingly delinked from the cyclicality agrochemical industry) positions itself favourably for organic growth. Maintaining the growth guidance of 20%+ for FY21 further bolsters our conviction on execution in the current scenario, backed by a strong order book of USD 1.5bn in the CSM business and introduction of new product in the domestic market. Ramp-up in Isagro and any inorganic growth opportunity would further improve earnings outlook. We value the company at 35x its FY22E EPS, recommending a Tactical BUY with a target price of INR 1,837.

Year to March (INR crore)	FY18	FY19	FY20	FY21E	FY22E
Net revenue	2,277	2,840	3,366	4,182	4,973
EBITDA	495	569	717	892	1,079
Adjusted PAT	367	410	455	593	724
EBITDA margin (%)	18.1	16.7	17.2	17.4	17.8
PAT margin (%)	16.1	14.4	13.5	14.1	14.5
EPS basic (INR)	26.6	29.7	33.0	43.0	52.5
Diluted P/E (x)	59.5	53.3	47.9	36.8	30.1
EV/EBITDA (x)	43.6	38.0	30.8	24.6	20.0
RoCE (%)	25.6	25.5	23.2	23.4	24.1

Date: 18th June, 2020

Focus Charts

Exhibit 92: Revenue (INR crore)

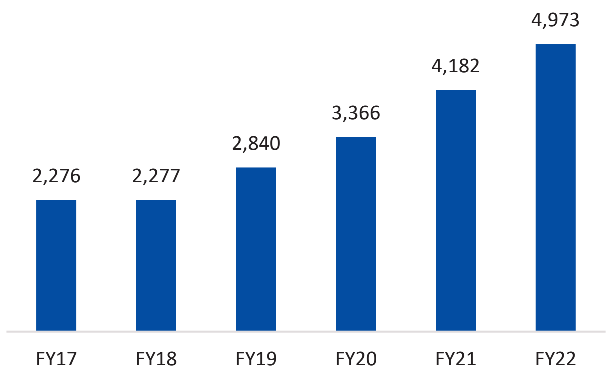


Exhibit 93: Share of CSM has consistently improved in Revenue mix

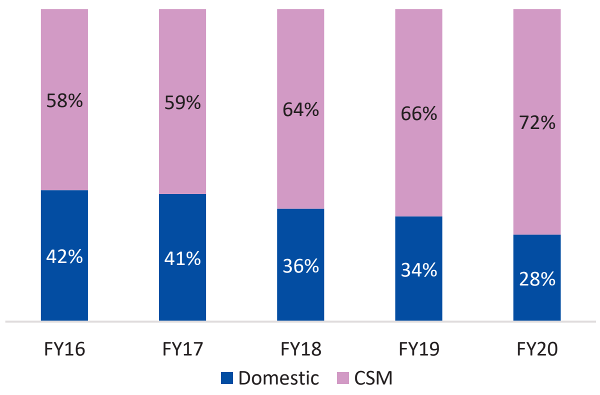


Exhibit 94: EBITDA (INR crore)

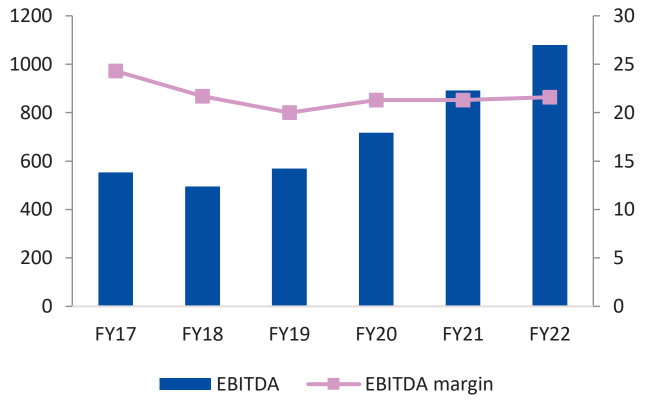


Exhibit 95: RoAE (%)

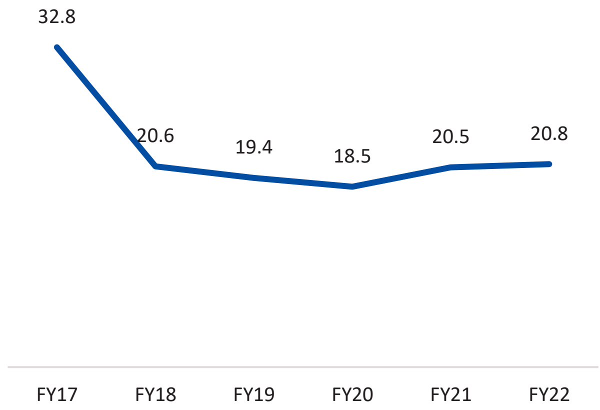


Exhibit 96: PAT (INR crore)

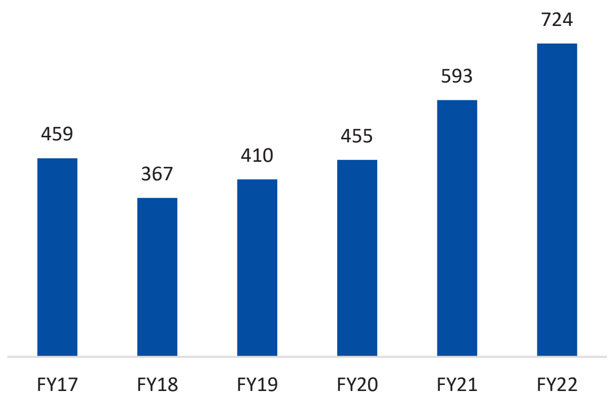
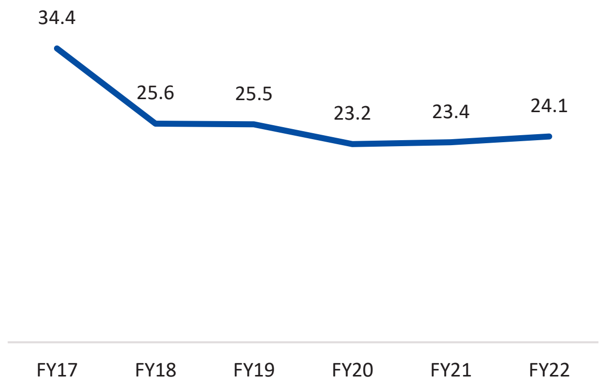


Exhibit 97: RoACE (%)



Source: Edelweiss Professional Investor Research

Company profile

Leading player in custom synthesis for agrochemical intermediates

PIIL is a key player in the agrochemical industry. The custom synthesis (CSM) business is a large contributor to its topline. In FY20, this business commanded a share of ~71% in its revenue mix, while the domestic agrochemical business contributed 29%. In the latter, PIIL in-licences or co-markets products of global players.

Over FY16-20, PIIL clocked ~11% CAGR in revenue. This was primarily driven by ~17% growth in its CSM business during this period, while revenue growth from the domestic business remained flat. This resulted in CSM's share increasing to ~72% to FY20 from under ~58% in FY16. We highlight this shift in exhibit 93.

Success in CSM business based on strong process chemistry capabilities

In the CSM business, PIIL partners with global innovators and engages in various stages of product development – from pre-launch levels to when the product goes off-patent.

With over 90% revenue accruing from patented products, PIIL's proposition to CSM customers is its process chemistry skills, ability to undertake reaction in complex chemistries and multiple processes, and support across stages through kilo- to multi-tonne level manufacturing.

Exhibit 89: PIIL's focus areas in CSM

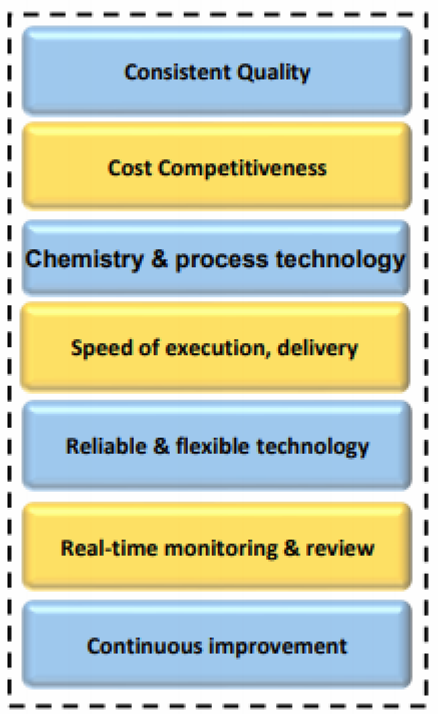
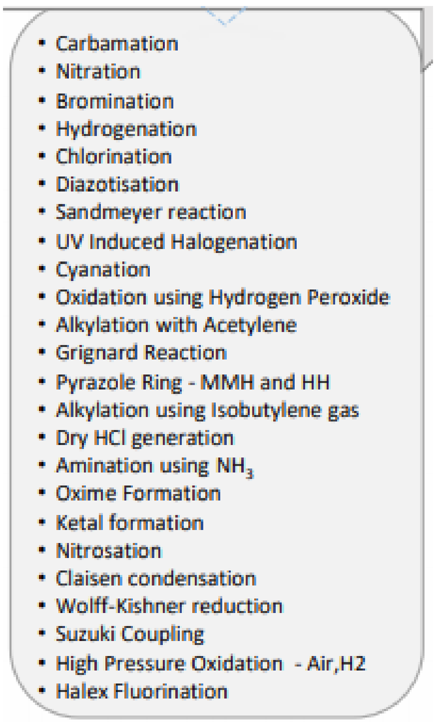


Exhibit 90: PIIL's reaction capabilities

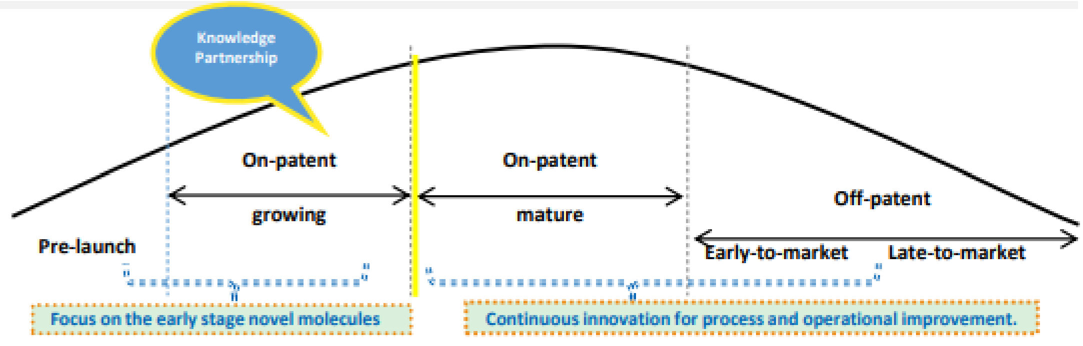


Source: Company, Edelweiss Professional Investor Research

Products in this segment are largely high value, having complex chemistry and backed by intellectual property (IP), which needs to be supplied for lower volume requirements. PIIL is generally the single supplier or one out of 2-3 suppliers.

Additionally, PIIL has recently diversified into the pharma segment, which we believe is a big positive and will lead to increasingly de-risk the company's revenue from agrochemical cycle. The company has already tied up with Japanese and Indian customer for an intermediate used in a COVID-19 drug.

Exhibit 91: PIIL's engagement in various phases of product development



Source: Company, Edelweiss Professional Investor Research

This has resulted in an order book of USD1.5bn, which has been consistently growing for PIIL.. Growth in the CSM business depends on the global agrochemical cycle to some extent (however entry into adjacencies like the recent move in the pharma segment and future inorganic opportunities will increasingly de-risk PIIL's business model from the agrochemical cycle). Its revenue profile remained flat during FY17-18, in line with global developments. After that, the segment continued to witness growth of ~25-30%. Over a longer time horizon, cyclicality in the segment would be offset by strong growth.

Domestic agrochemical business: Strong product line, but dependent on weather

In the domestic business, PIIL has strong products, which are generally in-licenced or co-marketed with global innovators. This model further bolsters the company's relationships with global players as it enables new market entry for customers and increases product cycles.

PIIL has partnership with over 20 global innovators in this segment and banks on their extensive distribution network. Its key products -- NOMINEE GOLD, OSHEEN, KEEFUN and VIBRANT -- have consistently performed well in the Indian market. We expect the domestic business's growth rate to be modest and reflect the trajectory experienced in the recent past.

The recent launch of AWKIRA has also seen success in the domestic market, and would play a role in also further diversifying PIIL's revenue across seasons.

Opening up of opportunities through the inorganic growth

PIIL recently acquired Isagro (Asia) Agrochemicals Pvt (Isagro) from Isagro SPA for ~INR 345 crore plus surplus cash. Isagro is engaged in contract manufacturing, which is running at low utilisation, and used to supply to its parent earlier. Additionally, the company also manufactures and distributes agrochemicals locally and through exports.

The management has informed that the acquisition will provide additional manufacturing capacity (production plant for agrochemical technical and formulations are adjacent to PIIL's plants in Panoli), long term contracts with Isagro Spa and benefit from Isagro's synergistic product portfolio in the domestic market. The acquisition will be a driver of growth for PIIL in FY21-22.

The management has also received board approval to raise funds via a QIP of up to INR 2,000 crore, which will be used to fund future growth. The proceeds of which will be used for:

- Organic business growth by pursuing further opportunities and scale up of existing products
- Scale up of new niche technologies that it has been working on for the last couple of years
- Diversifying into adjacent verticals like pharma, specialty chemicals, nutraceuticals, imaging chemicals, etc through the CSM model.

Along with organic growth, driven by strong order book visibility in the existing business, particularly CSM, these developments will be growth accretive for PIIL.

Income statement (INR Cr)	FY18	FY19	FY20	FY21	FY22
Net Revenue	2,277	2,840	3,366	4,182	4,973
Materials costs	1,169	1,550	1,847	2,264	2,660
Gross profit	1,108	1,290	1,519	1,917	2,312
Employee costs	243	264	320	376	462
Other Expenses	369	456	480	648	770
EBITDA	495	569	717	892	1,079
Depreciation and amortisation	83	93	136	163	189
EBIT	412	476	581	729	889
Interest expenses	7	7	17	33	31
Other income	60.2	68.4	48.9	65	72
Profit before tax	465	537	613	760	929
Provision for tax	97	127	157	167	204
Reported PAT	367	410	455	593	724
Adjusted PAT	367	410	455	593	724
Basic shares outstanding (mn)	13	13	13	13	13
Adjusted basic EPS (INR)	26.6	29.7	33	43	52.5
Diluted equity shares (mn)	13	13	13	13	13
Adjusted diluted EPS (INR)	26.6	29.7	33	43	52.5
CEPS (INR)	32.6	36.4	42.9	54.8	66.2
Dividend per share (INR)	4	4	4	4	4
Dividend payout (%)	15	13.4	13.4	9.3	9.3

Growth (%)	FY18	FY19	FY20	FY21	FY22
Revenues Growth	0.0	24.7	18.5	24.2	18.9
EBITDA Growth	-11.0	14.9	26.0	24.3	20.8
PBT Growth	-9.0	15.5	13.9	24.1	22.1
Net profit Growth	-20.0	11.6	11.1	30.1	22.1
EPS Growth	-20.0	11.6	11.1	30.1	22.1

Balance sheet (INR Cr)	FY18	FY19	FY20	FY21	FY22
Equity capital	13	13	13	13	13
Reserves & surplus	1,911	2,271	2,605	3,132	3,790
Shareholders funds	1,924	2,285	2,619	3,146	3,804
Long term debt	46	9	399	399	399
Short term debt	0	0	108	108	108
Borrowings	46	9	507	507	507
Long Term Liabilities & Provisions	41	48	95	95	95
Deferred Tax liability	-26	-14	10	10	10
Sources of funds	1,986	2,329	3,232	3,759	4,417
Gross block	1,206	1,479	2,171	2,771	3,071
Net block	997	1,179	1,733	2,170	2,280
Intangible assets	20	28	33	33	33
CWIP (incl. intangible)	69	154	237	200	200
Total net fixed assets	1,087	1,361	2,004	2,404	2,514
Non current investments	1	17	17	17	17
Cash and equivalents	290	201	266	382	784
Inventories	452	535	798	770	904
Sundry debtors	526	661	646	794	944
Loans and advances	1,363	87	162	236	279
Other current assets	72	268	204	258	297
Total current assets (ex cash)	2,414	1,553	1,812	2,059	2,427
Trade payable	368	513	590	747	878
Others current liabilities	1,439	298	401	480	571
Total current liabilities & provisions	1,807	811	992	1,228	1,449
Net current assets (ex cash)	607	742	819	830	977
Uses of funds	1,986	2,329	3,232	3,759	4,417
Book value per share (INR)	139.4	165.6	189.7	227.9	275.6

Free cash flow (INR Cr)	FY18	FY19	FY20	FY21	FY22
Net profit	367	410	456	593	724
Depreciation	83	93	136	163	189
Interest (Net of Tax)	5	5	12	26	24
Others	-32	32	66	-57	-64
Less: Changes in WC	104	150	-25	11	146
Operating cash flow	319	390	698	714	728
Less: Capex	169	368	674	562	300
Free Cash Flow	149	22	23	151	428

Cash flow metrics	FY18	FY19	FY20	FY21	FY22
Operating cash flow	319	390	698	714	728
Financing cash flow	-106	-125	350	-100	-98
Investing cash flow	-180	-312	-985	-497	-228
Net Cash Flow	32	-46	63	116	401
Capex	-169	-368	-674	-562	-300
Dividend paid	-55	-83	-74	-66	-66

Profitability and efficiency ratios	FY18	FY19	FY20	FY21	FY22
ROAE (%)	20.6	19.4	18.5	20.5	20.8
ROACE (%)	25.6	25.5	23.2	23.4	24.1
Inventory day	137.0	116.0	131.0	126.0	114.0
Debtors days	76.0	76.0	70.0	62.0	63.0
Payable days	102.0	103.0	109.0	107.0	111.0
Cash conversion cycle (days)	111.0	88.0	93.0	81.0	67.0
Current ratio	1.4	2.1	2.0	1.9	2.2
Debt/EBITDA	0.0	0.0	0.7	0.5	0.4
Debt/Equity	0.0	0.0	0.1	0.1	0.1
Adjusted debt/equity	0.0	0.0	0.1	0.1	0.1
Net Debt/Equity	0.0	0.0	0.0	0.0	0.0

Valuation parameters	FY18	FY19	FY20	FY21	FY22
EPS (INR) diluted	26.6	29.7	33	43	52.5
Y-o-Y growth (%)	-20	11.6	11.1	30.1	22.1
Cash EPS	32.6	36.4	42.9	54.8	66.2
Diluted PE (x)	59.5	53.3	47.9	36.8	30.1
Price/BV (x)	11.3	9.5	8.3	6.9	5.7
EV/Sales (x)	9.4	7.6	6.5	5.2	4.3
EV/EBITDA (x)	43.6	38	30.8	24.6	20
Dividend yield (%)	0.2	0.2	0.2	0.2	0.2

SRF Ltd

Riding the specialty chemicals wave

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SRF is a leading fluorochemicals player in India, with business interest in packaging films and technical textiles. Its chemical business (CB) operates in the fluorochemical industry, which is fast-growing, particularly the fluorospecialty segment. CB also houses the refrigerant gases business. The packaging films business (PFB) manufactures BOPP (biaxially oriented polypropylene) and BOPET (biaxially-oriented polyethylene terephthalate) films while the technical textiles business (TTB) manufactures nylon and polyester tyre cord fabrics, belting fabrics, industrial yarns, among others.

Key investment highlights

- CB has seen solid growth in recent times, driven by the specialty chemicals business (SCB). Sustained demand from agrochemical customers due to growth in Latin American markets and strong demand from the pharmaceutical sector has been driving growth. In FY20, growth was well over the previously guided 40-50% growth rate. The segment clocked revenue in excess of INR 1,650 crore, an over-60%-growth-rate during the fiscal, due to strong demand and improving capacity utilisation. The management guided at a 20-25% growth rate in FY21, led by a strong order book. This segment will be a major growth driver for SRF as its contribution in the revenue mix improves (~23% in FY20 from ~15% in FY19).

- To aid growth in the SCB, SRF will spend INR 238 crore to produce intermediates for agrochemicals. This facility will be utilised for new products to be launched or for existing products from its multi-purpose plants (MPPs), which are supplied in batch quantities. We maintain our view of this segment being the key growth driver for the company.

- The fluorochemicals business, which consist of refrigerant gases including their pharma-related uses, chlorinated solvents etc, has been impacted lately by the slowdown in the automobile sector and lower prices of refrigerant gases due to weak demand. Going forward, the management expects better demand from the replacement market and faster utilisation (from 3 years expected earlier) in the recently commissioned hydrofluorocarbon (HFC) capacity. Current utilisation levels stand at 70-75% on a pro-rated basis. Volumes in the chloromethane segment were positive during Q4.Commissioning of brownfield hydrofluorocarbon (HFC) facilities impacted CB margin sequentially, owing to higher fixed costs. We expect better cost absorption as the new capacity ramps up. SRF's board has approved a capex of INR 65.5 crore to address future demand in HFCs. Unlike other domestic players, the company has diversified into various newer-age refrigerant gases, which would be a key demand driver.

- PFB margin has been strong off-late due to steady demand for BOPET and BOPP with growth in sales of value added products (VAP). Oversupply in the BOPET business can dent its margin profile going forward. However, it can occur at a slower pace than expected. Growth drivers for this segment are expansion projects in Thailand and Hungary, with the former being commissioned in Q4FY20, while commissioning of the Hungary plant has been pushed to Q2FY21 due to COVID-19 related delays. These new capacities will drive growth for the PFB segment in FY21/FY22. We expect TTB to remain weak on lower demand from the auto sector and moderated raw material prices due to lower crude oil prices.

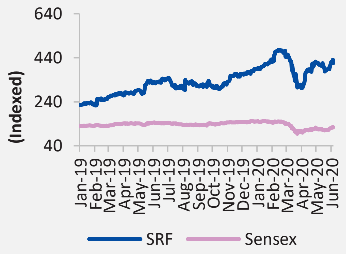
CMP: INR 3,621

Rating: BUY

Target: INR 4,007

Upside: 11%

Relative price performance



Bloomberg:	SRF:IN
52-week range (INR):	2,468/4,260
Share in issue (crore):	6
M-cap (INR crore):	20,780
Promoter holding (%)	52.32

Valuation and outlook

SCB will be a key value creator for SRF's shareholders given its R&D capabilities in the fluorination space, product development and customer relationships, resulting in a larger contribution to its revenue and profits. Growth in the PFB segment will be driven by overseas expansions. Weak demand may persist in FCB and TTB in the near term. Factoring these, a reduction in debt, consistent capex and lower tax rate, we estimate FY21/FY22 EPS to be at INR 144/191, respectively. We maintain BUY with a target price of INR 4,007 per share, valuing the company at 21x its FY22E EPS.

Year to March (INR crore)	FY18	FY19	FY20	FY21E	FY22E
Net revenue	5589	7,100	7,209	7,299	8,446
EBITDA	906	1,297	1,455	1,622	1,942
Adjusted PAT	461	592	916	828	1,096
EBITDA margin (%)	16.2	18.3	20.2	22.2	23.0
PAT margin (%)	8.3	8.3	12.7	11.3	13.0
EPS basic (INR)	80	103	159	144	191
Diluted P/E (x)	45.5	35.5	22.9	25.3	19.1
EV/EBITDA (x)	26.5	18.6	16.6	14.8	12.2
RoCE (%)	9.2	12.7	13.2	13.6	15.3

Date: 18th June, 2020

Financials Charts

Exhibit 98: Revenue (INR crore)

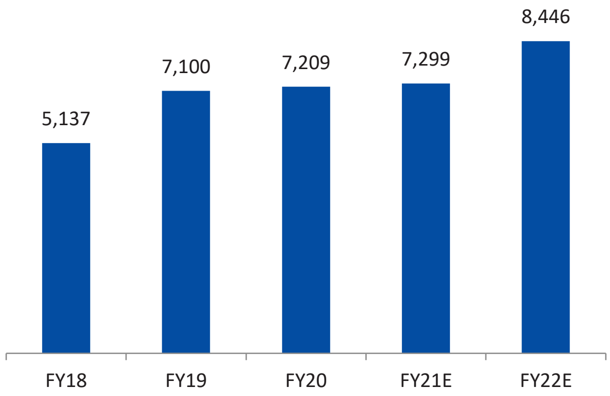


Exhibit 99: SCB' Revenue Contribution - Estimated

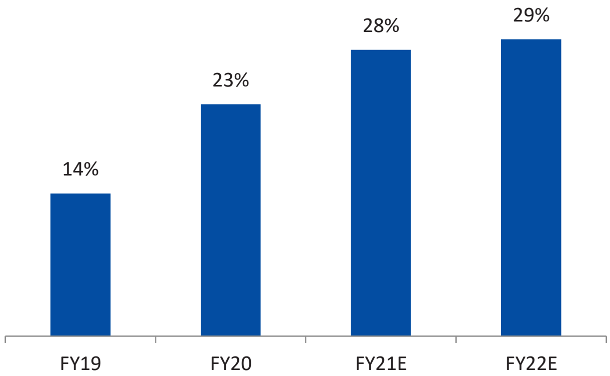


Exhibit 100: EBITDA (INR crore)

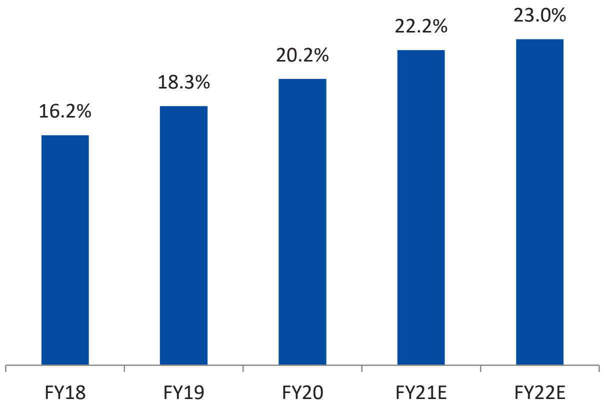


Exhibit 101: RoAE (%)

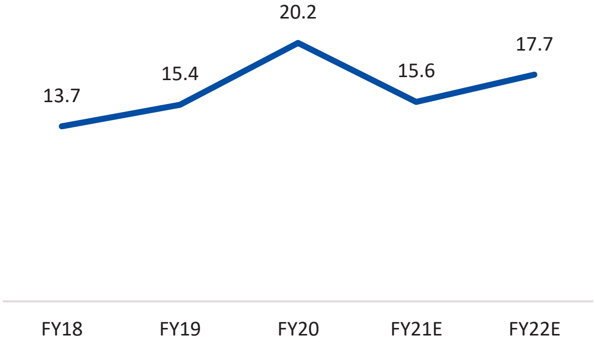


Exhibit 102: PAT (INR crore)

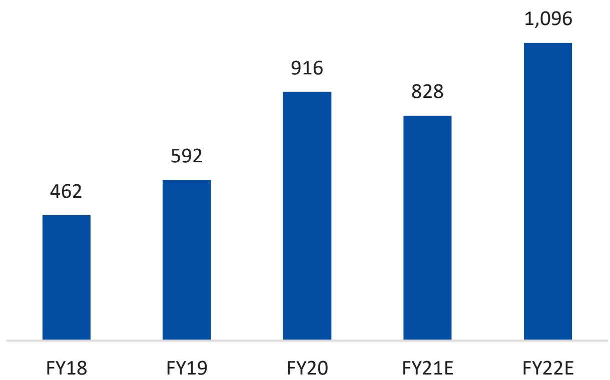
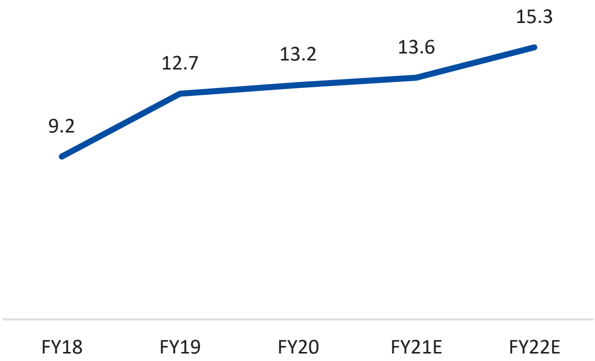


Exhibit 103: RoACE (%)



Source: Edelweiss Professional Investor Research

Income statement					(INR crs)
Year to March	**FY18**	**FY19**	**FY20**	**FY21E**	**FY22E**
Income from operations	5589	7,100	7,209	7,299	8,446
Total operating expenses	4683	5,803	5,754	5,678	6,504
EBITDA	906	1,297	1,455	1,622	1,942
Depreciation and amortisation	316	358	389	440	499
EBIT	590	939	1,066	1,182	1,443
Interest expenses	124	198	201	196	122
Profit before tax	582	769	914	1,035	1,371
Provision for tax	120	177	- 1	207	274
Core profit	462	592	916	828	1,096
Extraordinaries	0	-	-	-	-
Profit after tax	461	592	916	828	1,096
Adjusted net profit	461	592	916	828	1,096
Equity shares outstanding (mn)	6	6	6	6	6
EPS (INR) basic	80	103	159	144	191
Diluted shares (Cr)	6	6	6	6	6
EPS (INR) fully diluted	80	103	159	144	191
Dividend per share	12	12	14	14	14
Dividend payout (%)	15	12	9	10	7

Common size metrics- as % of net revenues					(INR crs)
Year to March	**FY18**	**FY19**	**FY20**	**FY21E**	**FY22E**
Operating expenses	83.8	81.7	79.8	77.8	77.0
Depreciation	5.7	5.0	5.4	6.0	5.9
Interest expenditure	2.2	2.8	2.8	2.7	1.4
EBITDA margins	16.2	18.3	20.2	22.2	23.0
Net profit margins	8.3	8.3	12.7	11.3	13.0

Growth metrics (%)					
Year to March	**FY18**	**FY19**	**FY20**	**FY21E**	**FY22E**
Revenues	15.9	27.0	1.5	1.2	15.7
EBITDA	(6.5)	43.1	12.2	11.5	19.7
PBT	(11.5)	32.1	19.0	13.2	32.4
Net profit	(10.3)	28.1	54.7	(9.5)	32.4
EPS	(10.4)	28.3	54.7	(9.5)	32.4

Balance sheet					(INR crs)
As on 31st March	**FY18**	**FY19**	**FY20**	**FY21E**	**FY22E**
Equity share capital	58	59	59	59	59
Preference Share Capital	0	0	0	0	0
Reserves & surplus	3,506	4,071	4,875	5,623	6,640
Shareholders funds	3,565	4,129	4,933	5,682	6,698
Borrowings	3,142	3,289	3,267	3,117	2,967
Minority interest	0	0	0	0	0
Sources of funds	**6,706**	**7,418**	**8,200**	**8,799**	**9,665**
Gross block	5,993	6,250	6,999	7,999	8,999
Accumulated Depreciation	871	587	976	1,416	1,914
Net block	5,122	5,663	6,023	6,583	7,084
Capital work in progress	559	754	1,393	1,393	1,393
Total fixed assets	5,680	6,417	7,416	7,976	8,478
Investments	122	101	203	203	203
Inventories	958	1,225	1,201	1,216	1,407
Sundry debtors	681	1,029	891	902	1,044
Cash and equivalents	97	199	125	94	262
Other current assets	569	619	478	584	676
Total current assets	2,304	3,072	2,696	2,796	3,388
Sundry creditors and others	1,283	1,382	1,112	1,126	1,302
Provisions	15	970	960	1,008	1,058
Total CL & provisions	1,298	2,352	2,071	2,133	2,360
Net current assets	1,007	719	625	663	1,028
Net Deferred tax	-291	-342	-176	-176	-176
Others	189	690	132	132	132
Uses of funds	**6,706**	**7,585**	**8,200**	**8,799**	**9,665**
Book value per share (INR)	620	719	858	989	1,166

Cash flow statement					(INR crs)
Year to March	**FY18**	**FY19**	**FY20**	**FY21E**	**FY22E**
Net profit	462	592	916	828	1,096
Add: Depreciation	316	358	389	440	499
Add: Misc expenses written off	-48	-501	558	0	0
Add: Deferred tax	7	51	-166	0	0
Gross cash flow	737	499	1,696	1,268	1,595
Less: Changes in W. C.	143	-389	-21	70	197
Operating cash flow	594	889	1,717	1,198	1,398
Less: Capex	1,333	928	1,555	1,000	1,000
Free cash flow	**-739**	**-39**	**162**	**198**	**398**

Ratios

Year to March	FY18	FY19	FY20	FY21E	FY22E
ROAE (%)	13.7	15.4	20.2	15.6	17.7
ROACE (%)	9.2	12.7	13.2	13.6	15.3
Debtors (days)	44	53	45	45	45
Current ratio	1.8	1.3	1.3	1.3	1.4
Debt/Equity	0.9	0.8	0.7	0.5	0.4
Inventory (days)	63	63	61	61	61
Payable (days)	84	71	56	56	56
Cash conversion cycle (days)	23	45	50	50	50
Debt/EBITDA	3.5	2.5	2.2	1.9	1.5
Adjusted debt/Equity	0.9	0.7	0.6	0.5	0.4

Valuation parameters

Year to March	FY18	FY19	FY20	FY21E	FY22E
Diluted EPS (INR)	80.3	103.0	159.3	144.1	190.8
Y-o-Y growth (%)	*(10.4)*	*28.3*	*54.7*	*(9.5)*	*32.4*
CEPS (INR)	135	165	227	221	278
Diluted P/E (x)	45.5	35.5	22.9	25.3	19.1
Price/BV(x)	5.9	5.1	4.3	3.7	3.1
EV/Sales (x)	4.3	3.4	3.3	3.3	2.8
EV/EBITDA (x)	26.5	18.6	16.6	14.8	12.2
Diluted shares O/S	5.7	5.7	5.7	5.7	5.7
Basic EPS	80.3	103.0	159.3	144.1	190.8
Basic PE (x)	45.5	35.5	22.9	25.3	19.1
Dividend yield (%)	0.3	0.3	0.4	0.4	0.4

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Board: (91-22) 4272 2200

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Rating	Expected to
BUY	appreciate more than 15% over a 12-month period
HOLD	appreciate between 5-15% over a 12-month period
REDUCE	return below 5% over a 12-month period

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