

# DEEPAK FERTILIZER

## NPK plant ramps up as per plans

India Equity Research | Fertilisers

Deepak Fertiliser's (DFPC) Q2FY18 numbers were marginally below estimates. PAT came in at INR462mn (up 72% YoY on low base) versus INR566mn estimate due to lower-than-expected fertiliser margin and higher tax provisioning. Commissioning of NPK plant and higher chemical trading propelled top line 34% YoY to INR12.3bn. Factoring in weak H1FY18 numbers, we revise FY18E EBITDA/PAT down 15%/20%. However, as we expect DFPC's earnings momentum to pick up fuelled by fertiliser business and higher utilisation in TAN, we revise up FY19E EPS 5%. On anticipated sustenance of earnings momentum underpinned by significant capex planned over 2-3 years, we revise up our target multiple from 12x to 14x FY19E EPS. DFPC also entails rerating potential from DBT and rerating in chemical sector. Consequently, we raise our TP to INR531 (INR438 earlier) and maintain 'BUY'.

### Chemical margin rebounds

Chemical revenue jumped 12% YoY to INR7.7bn (flat in Q1FY18) with growth coming primarily from the traded segment—up 58% YoY to INR3.2bn. TAN also reported strong volume spurt, partially aided by low base. Post Q1FY18 margin, which had been impacted by inventory losses due to volatility in ammonia prices, Q2FY18 chemical margin improved ~240bps YoY to 16.3% (~570bps QoQ). While H1FY18 has been impacted by inventory losses, we expect FY19E margin to improve driven by improved TAN pricing, benefiting from imposition of anti-dumping duty and higher utilisation.

### Scale up of NPK plant as per expectation; slight miss on margin

Fertiliser segment's revenue jumped 43% YoY to INR4.5bn driven by commissioning of its NPK plant (0.5mn mtpa). This led to manufactured revenue catapulting ~2x to INR3.5bn, while traded revenue contracted 46% YoY. Margin also improved 570bps to 4.2% (estimate 5%). DFPC also reported an INR60m forex related loss in the fertilizer segment.

### Outlook and valuations: Strong capex plans; maintain 'BUY'

Factoring the impact of lower margin in the chemical segment in H1FY18 (inventory losses related to ammonia and lower TAN prices), we revise our FY18E EBITDA/PAT down 15%/20%. However, as we expect DFPC's earnings momentum to pick up fuelled by fertilizer business and higher utilisation in TAN, we revise up FY19E EPS 5%. Also, factoring in revenue potential from planned capex (NPK of 0.3MTPA and Dahej nitric acid Plant) we revise up our multiple to 14.0x. Maintain 'BUY' with TP of INR531.

#### Financials

Year to March	Q2FY18	Q2FY17	% change	Q1FY18	% change	FY17	FY18E	FY19E
Net rev. (INR mn)	12,313	9,164	34.4	12,803	(3.8)	41,501	47,855	54,327
EBITDA (INR mn)	1,439	918	56.8	1,225	17.4	4,734	5,790	7,380
Adj. profit (INR mn)	462	268	72.3	374	23.5	1,757	2,302	3,348
Adj. Dil EPS (INR)	5.2	3.0	72.3	4.2	23.5	19.9	26.1	38.0
Diluted P/E (x)						22.6	17.3	11.9
EV/EBITDA (x)						11.8	9.7	7.6

#### EDELWEISS RATINGS

Absolute Rating	BUY
Investment Characteristics	Growth

#### MARKET DATA (R: DPFE.BO, B: DFPC IN)

CMP	: INR 452
Target Price	: INR 531
52-week range (INR)	: 500 / 165
Share in issue (mn)	: 88.2
M cap (INR bn/USD mn)	: 40 / 616
Avg. Daily Vol. BSE/NSE ('000)	: 391.0

#### SHARE HOLDING PATTERN (%)

	Current	Q1FY18	Q4FY17
Promoters *	51.1	51.1	51.1
MF's, FI's & BKs	4.0	3.9	3.1
FII's	9.3	11.4	13.3
Others	35.6	33.6	32.6
* Promoters pledged shares (% of share in issue)	:		NIL

#### PRICE PERFORMANCE (%)

	BSE Midcap Index	Stock	Stock over Index
1 month	7.4	22.0	14.6
3 months	9.0	42.8	33.8
12 months	28.4	118.9	90.5

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## Fertilisers

**Table 1: Operational Performance (INR mn)**

Segment revenue	Q2FY18	Q2FY17	% YoY	Q1FY18	% QoQ
a) Chemicals					
Manufactured	4,518	4,860	(7.0)	5,196	(13.1)
Traded	3,222	2,036	58.2	2,912	10.6
Total	7,739	6,896	12.2	8,108	(4.5)
b) Fertilisers					
Manufactured	3,475	1,253	177.2	3,617	(3.9)
Traded	1,030	1,894	(45.6)	1,000	2.9
Total	4,505	3,147	43.1	4,617	(2.4)
c) Realty					
	42	24	77.4	42	0.0
d) Others					
	27	30	(9.9)	36	(24.1)
<b>Total</b>	<b>12,313</b>	<b>10,097</b>	<b>21.9</b>	<b>12,803</b>	<b>(3.8)</b>
Less: Inter segmental revenue	0	443	(100.0)	0	
<b>Net revenue from operations</b>	<b>12,313</b>	<b>9,654</b>	<b>27.5</b>	<b>12,803</b>	<b>(3.8)</b>
<b>Net profit before interest and tax</b>					
a) Chemicals	1,262	960	31.5	862	46.4
b) Fertilisers	190	(48)	(496.2)	261	(27.4)
c) Realty	(42)	(47)	NA	(45)	NA
d) Others	19	20		27	
Total	1,429	886	61.4	1,106	29.2
Less: Interest	430	269	59.8	373	15.1
Less: Other unallocable expenditure	356	263	35.0	253	40.6
<b>Total profit before tax</b>	<b>644</b>	<b>353</b>	<b>82.3</b>	<b>480</b>	<b>34.3</b>
<b>PBIT (%)</b>					
a) Chemicals	16.3	13.9		10.6	
b) Fertilisers	4.2	(1.5)		5.7	
c) Realty	(101.7)	(199.1)		(106.7)	
d) Others	70.8	65.8		74.2	
<b>Capital employed</b>					
a) Chemicals	15,620	16,037		15,456	
b) Fertilisers	6,345	9,197		7,543	
c) Realty	2,270	2,331		2,299	
d) Others	286	313		263	
e) Unallocated	(6,542)	(11,886)		(7,879)	
<b>Total</b>	<b>17,979</b>	<b>15,992</b>		<b>17,681</b>	

Source: Company, Edelweiss research

**Financial snapshot**

(INR mn)

Year to March	Q2FY18	Q2FY17	% change	Q1FY18	% change	YTD18	FY18E	FY19E
Net revenues	12,313	9,164	34.4	12,803	(3.8)	25,116	47,855	54,327
Raw material	8,840	6,556	34.8	8,780	0.7	17,620	35,366	39,351
Staff costs	571	484	17.9	548	4.1	1,120	1,924	2,183
Other expenses	1,464	1,206	21.3	2,249	(34.9)	3,713	4,775	5,413
Total expenditure	10,875	8,247	31.9	11,578	(6.1)	22,452	42,065	46,947
EBITDA	1,439	918	56.8	1,225	17.4	2,664	5,790	7,380
Depreciation	391	325	20.3	408	(4.1)	799	1,696	1,983
EBIT	1,048	592	76.8	818	28.1	1,865	4,095	5,397
Other income	26	30	(13.3)	35	(25.9)	61	517	575
Interest	429	269	59.7	373	15.1	803	1,448	1,415
Add: Prior period items								
Profit before tax	644	354	82.2	480	34.3	1,124	3,163	4,558
Provision for taxes	172	76	128.1	103	67.8	275	861	1,210
Minority interest								
Associate profit share								
Profit- Discontinued Ops								
Exceptional Items								
Reported net profit	472	278	69.7	377	25.2	849	2,302	3,348
Adjusted Profit	462	268	72.3	374	23.5	836	2,302	3,348
Diluted shares (mn)	88	88		88		88	88	88
Adjusted Diluted EPS	5.2	3.0	72.3	4.2	23.5	9.5	26.1	38.0
Diluted P/E (x)	-	-		-		-	17.3	11.9
EV/EBITDA (x)	-	-		-		-	9.7	7.6
ROAE (%)	-	-		-		-	13.1	17.4
<b>As % of net revenues</b>								
Raw material	71.8	71.5		68.6		70.2	73.9	72.4
Employee cost	4.6	5.3		4.3		4.5	4.0	4.0
Other expenses	11.9	13.2		17.6		14.8	10.0	10.0
EBITDA	11.7	10.0		9.6		10.6	12.1	13.6
Reported net profit	3.8	2.9		2.9		3.3	4.8	6.2

**Change in Estimates**

	FY18E			FY19E			Comments
	New	Old	% change	New	Old	% change	
Net Revenue	47,855	50,832	(5.9)	54,327	53,483	1.6	
EBITDA	5,790	6,761	(14.4)	7,380	7,239	2.0	Lower margin in chemical segment
EBITDA Margin	12.1	13.3		13.6	13.5		
Adjusted PAT	2,302	2,885	(20.2)	3,348	3,222	3.9	
Net Profit Margin	4.8	5.7		6.2	6.0		
Capex	4,910	1,738	182.6	2,000	1,500	33.3	

### Company Description

DFPCL was incorporated in 1979 by Mr. C.K. Mehta as a private limited company. It is currently one of the leading manufacturers of industrial chemicals and fertilisers in India. The company operates in three business segments—chemicals, agribusiness, and specialty retailing. It has emerged as an integrated multi-product company manufacturing ammonia, iso propyl alcohol, methanol, nitric acid, low-density prilled ammonium nitrate, and nitrophosphate fertilisers in its state-of-the-art plants operating with world class technology.

### Investment Theme

DFPCL is the leader in the Indian Technical Ammonium Nitrate (TAN) market, with 30% share. The company has increased its TAN capacity further by 300K MT from 132K MT, at a capex of ~INR 6 bn. With increased capacity, DFPCL's market share in TAN is estimated to rise to over 50% in FY13 by replacing the cheaper grade TAN imports. Also, the company is set to benefit from the increasing TAN demand on account of the growing demand for coal and limestone production.

With better gas availability, Ammonium Nitrophosphate (ANP) fertiliser capacity utilisation is poised to increase from 25% in FY09 to ~80% in FY13. DFPCL is well connected to the National Gas Grid to receive gas from multiple sources like Panna-Mukta-Tapti (PMT) gas field, Krishna-Godavari (KG) Basin and ONGC.

### Key Risks

Any delay in scaling up of operations of the new TAN plant will cause opportunity loss for the company and downside risks to our estimates.

Though the company has tied up with Middle East suppliers for ammonia and for natural gas with multiple sources in India, any issues on this front may pose a risk for DFPCL.

High volatility in crude prices could adversely impact the company's raw material costs and, hence, its profitability.

Any delay in the payment of subsidies by Gol or payment of the same by means of fertiliser bonds, could strain the company's working capital cycle. The Indian finance minister has, however, assured that the entire subsidy amount will be paid in cash and not bonds.

INR volatility may impact the operating margin of the chemicals segment of DFPCL.

## Financial Statements

### Key Assumptions

Year to March	FY16	FY17	FY18E	FY19E
<b>Macro</b>				
GDP(Y-o-Y %)	7.9	6.6	6.8	7.4
Inflation (Avg)	4.9	4.5	4.0	4.5
Repo rate (exit rate)	6.8	6.3	5.8	5.8
USD/INR (Avg)	65.5	67.1	65.0	66.0
<b>Company</b>				
Chemicals EBITDA margin (%)	12.4	23.0	24.8	24.4
Fertiliser EBITDA margin (%)	2.2	(0.7)	6.5	7.0

### Income statement

(INR mn)

Year to March	FY16	FY17	FY18E	FY19E
Net revenue	43,092	41,501	47,855	54,327
Materials costs	33,432	29,432	35,366	39,351
Gross profit	9,660	12,069	12,489	14,977
Employee costs	1,830	2,102	1,924	2,183
Other Expenses	4,265	5,234	4,775	5,413
EBITDA	3,565	4,734	5,790	7,380
Depreciation	1,218	1,364	1,696	1,983
EBIT	2,347	3,370	4,095	5,397
Add: Other income	724.24	158.65	517.12	574.94
Less: Interest Expense	1,300	1,215	1,448	1,415
Profit Before Tax	1,771	2,313	3,163	4,558
Less: Provision for Tax	599	533	861	1,210
Less: Minority Interest	16	23	-	-
Reported Profit	1,157	1,757	2,302	3,348
Adjusted Profit	1,157	1,757	2,302	3,348
Shares o/s (mn)	88	88	88	88
Adjusted Basic EPS	13.1	19.9	26.1	38.0
Diluted shares o/s (mn)	88	88	88	88
Adjusted Diluted EPS	13.1	19.9	26.1	38.0
Adjusted Cash EPS	26.8	35.1	45.3	60.4
Dividend per share (DPS)	5.0	6.0	7.0	8.0
Dividend Payout Ratio(%)	46.1	35.2	31.4	24.7

### Common size metrics

Year to March	FY16	FY17	FY18E	FY19E
Gross margin	22.4	29.1	26.1	27.6
EBITDA margins	8.3	11.4	12.1	13.6
EBIT margins	5.4	8.1	8.6	9.9
Net Profit margins	2.7	4.3	4.8	6.2

### Growth ratios (%)

Year to March	FY16	FY17	FY18E	FY19E
Revenues	13.0	(3.7)	15.3	13.5
EBITDA	20.5	32.8	22.3	27.5
Adjusted Profit	94.7	51.9	31.0	45.4
EPS	94.7	51.9	31.0	45.4

# Fertilisers

Balance sheet		(INR mn)			
As on 31st March	FY16	FY17	FY18E	FY19E	
Share capital	882	882	882	882	
Reserves & Surplus	14,395	16,121	17,074	19,572	
Shareholders' funds	15,277	17,003	17,956	20,454	
Minority Interest	77	79	79	79	
Short term borrowings	14,812	13,823	13,812	12,812	
Long term borrowings	4,884	4,716	4,884	4,884	
Total Borrowings	19,696	18,539	18,696	17,696	
Def. Tax Liability (net)	1,224	1,189	1,224	1,224	
<b>Sources of funds</b>	<b>36,274</b>	<b>36,810</b>	<b>37,955</b>	<b>39,453</b>	
Gross Block	14,260	22,389	25,760	32,260	
Net Block	13,190	20,127	21,614	26,131	
Capital work in progress	3,962	3,853	5,511	1,011	
Total Fixed Assets	201	320	201	201	
Total net fixed assets	17,353	24,300	27,326	27,343	
Non current investments	147	124	147	147	
Cash and Equivalents	2,684	2,392	2,091	1,447	
Inventories	6,059	5,045	5,630	5,612	
Sundry Debtors	15,481	11,834	10,140	13,301	
Loans & Advances	476	406	634	634	
Other Current Assets	2,339	3,068	3,000	3,000	
Current Assets (ex cash)	24,355	20,354	19,404	22,546	
Trade payable	4,701	4,152	4,531	5,031	
Other Current Liab	3,564	6,208	6,470	6,970	
Total Current Liab	8,265	10,360	11,001	12,001	
Net Curr Assets-ex cash	16,090	9,994	8,403	10,545	
<b>Uses of funds</b>	<b>36,274</b>	<b>36,810</b>	<b>37,955</b>	<b>39,453</b>	
BVPS (INR)	173.2	192.8	203.6	231.9	

Free cash flow		(INR mn)			
Year to March	FY16	FY17	FY18E	FY19E	
Reported Profit	1,157	1,757	2,302	3,348	
Add: Depreciation	1,218	1,364	1,696	1,983	
Interest (Net of Tax)	871	814	970	948	
Others	1,194	1,341	931	840	
Less: Changes in WC	4,672	(5,002)	(1,591)	2,142	
Operating cash flow	(1,104)	9,464	6,520	4,028	
Less: Capex	3,480	7,000	4,910	2,000	
<b>Free Cash Flow</b>	<b>(4,584)</b>	<b>2,464</b>	<b>1,610</b>	<b>2,028</b>	

## Peer comparison valuation

Name	Market cap (USD mn)	Diluted P/E (X)		EV / EBITDA (X)		ROAE (%)	
		FY18E	FY19E	FY18E	FY19E	FY18E	FY19E
Deepak Fertilizer Ltd	616	17.3	11.9	9.8	7.6	13.1	17.4
Coromandel International	2,329	24.5	20.2	14.3	12.3	19.7	20.6
Zuari Agro Chemicals	398	13.0	12.1	12.9	12.3	12.7	12.8
Median	-	17.3	12.1	12.9	12.3	13.1	17.4
AVERAGE	-	18.3	14.7	12.3	10.7	15.2	16.9

Source: Edelweiss research

Cash flow metrics				
Year to March	FY16	FY17	FY18E	FY19E
Operating cash flow	(1,104)	9,464	6,520	4,028
Investing cash flow	(622)	(7,932)	(3,875)	(2,000)
Financing cash flow	3,502	(2,678)	(1,513)	(2,682)
Net cash Flow	1,776	(1,146)	1,132	(654)
Capex	(3,480)	(7,000)	(4,910)	(2,000)
Dividend paid	(956)	(1)	(722)	(826)

## Profitability and efficiency ratios

Year to March	FY16	FY17	FY18E	FY19E
ROAE (%)	7.8	11.0	13.1	17.4
ROACE (%)	9.6	10.0	12.7	15.9
ROA	3.5	4.9	6.2	8.6
Inventory Days	55	69	55	52
Debtors Days	106	120	84	79
Payable Days	46	55	45	44
Cash Conversion Cycle	116	134	94	87
Current Ratio	3.3	2.2	2.0	2.0
Gross Debt/EBITDA	5.5	3.9	3.2	2.4
Gross Debt/Equity	1.3	1.1	1.0	0.9
Adjusted Debt/Equity	1.3	1.1	1.0	0.9

## Operating ratios

Year to March	FY16	FY17	FY18E	FY19E
Total Asset Turnover	1.3	1.1	1.3	1.4
Fixed Asset Turnover	3.2	2.5	2.3	2.3
Equity Turnover	2.9	2.6	2.7	2.8

## Valuation parameters

Year to March	FY16	FY17	FY18E	FY19E
Adj. Diluted EPS (INR)	13.1	19.9	26.1	38.0
Y-o-Y growth (%)	94.7	51.9	31.0	45.4
Adjusted Cash EPS (INR)	26.8	35.1	45.3	60.4
Diluted P/E (x)	34.5	22.7	17.3	11.9
P/B (x)	2.6	2.3	2.2	1.9
EV / Sales (x)	1.3	1.3	1.2	1.0
EV / EBITDA (x)	16.0	11.8	9.8	7.6
Dividend Yield (%)	1.1	1.3	1.5	1.8

## Additional Data

### Directors Data

S.C. Mehta	Chairman & Managing Director	C.K.Mehta	Chairman Emeritus
Parul S. Mehta	Director	R.A. Shah	Independent Director
N.C. Singhal	Independent Director	S.R.Wadhwa	Independent Director
Anil Sachdev	Independent Director	D.Basu	Independent Director
U.P.Jhaveri	Independent Director	S. Rama Iyer	Independent Director
Pranay Vakil	Independent Director	Partha Bhattacharyya	Director

Auditors - B.K.Khare & Co.

*\*as per last available data*

### Holding Top -10

	Perc. Holding		Perc. Holding
Fidelity Management and Research	8.46	ICICI Lombard	1.10
ICICI Prudential Life Insurance	4.08	UTI Asset Mgmt	0.28
BNP Paribas	1.73	New Zeleand Super Annuation Fund	0.14
BNP Paribas Asset management	1.73	Wisdom Tree	0.05
Dimensional Fund Advisor	1.53	Principal PNB Asset Mgmt	0.04

*\*as per last available data*

### Bulk Deals

Data	Acquired / Seller	B/S	Qty Traded	Price
28 Mar 2017	Parul Sailesh Mehta	Sell	3012000	248.05
28 Mar 2017	Sailesh Mehta	Sell	21283000	248.05
28 Mar 2017	Nova Synthetic Ltd	Buy	24295000	248.05
23 Jan 2017	Parul Sailesh Mehta	Sell	1032000	257.00
23 Jan 2017	Nova Synthetic Ltd	Buy	1032000	257.00

*\*as per last available data*

### Insider Trades

Reporting Data	Acquired / Seller	B/S	Qty Traded
02 May 2017	SOFOTEL INFRA PRIVATE LIMITED	Buy	300000.00
02 May 2017	CHIMANLAL K MEHTA	Sell	300000.00
03 Apr 2017	PARUL S MEHTA	Sell	3012000.00
03 Apr 2017	SAILESH MEHTA	Sell	21283000.00
03 Apr 2017	NOVA SYNTHETIC LIMITED	Buy	24295000.00

*\*as per last available data*

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## Coverage group(s) of stocks by primary analyst(s): Fertilisers

Chambal Fertilisers and Chemicals, Coromandel International, Deepak Fertilizer Ltd, Zuari Agro Chemicals

### Recent Research

Date	Company	Title	Price (INR)	Recos
28-Oct-17	<b>Zuari Agrochem.</b>	Rerating continues; <i>Result Update</i>	614	Buy
26-Oct-17	<b>Coromandel International</b>	Fertiliser segment margins shine; <i>Result Update</i>	488	Buy
16-Aug-17	<b>Jain Irrigation Systems</b>	GST dampener; guidance maintained; <i>Result Update</i>	95	Buy

### Distribution of Ratings / Market Cap

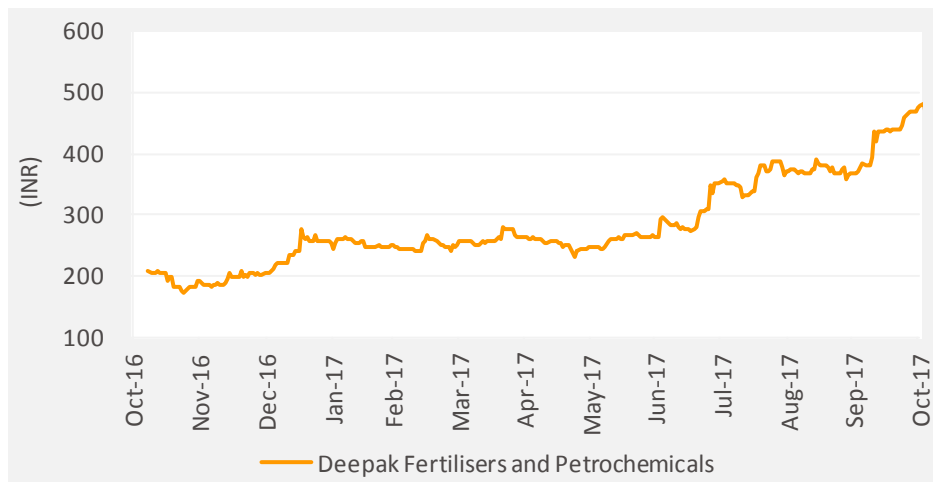
Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution*	161	67	11	240
* 1stocks under review				
	> 50bn	Between 10bn and 50 bn	< 10bn	
Market Cap (INR)	156	62	11	

### Rating Interpretation

Rating	Expected to
<b>Buy</b>	appreciate more than 15% over a 12-month period
<b>Hold</b>	appreciate up to 15% over a 12-month period
<b>Reduce</b>	depreciate more than 5% over a 12-month period

One year price chart





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