

Sharda Cropchem's 1QFY20 performance was below our expectations, Sales de-grew by 7.5% YoY to ₹ 4.23bn (D.est: ₹ 5.25bn). EBITDA/PAT de-growth was even sharper by 13.3/33.5% YoY to ₹ 616/228mn respectively. Gross margin contraction of 337 bps YoY and 331 bps QoQ was a function of consistently rising raw material prices and a sharp gross margin decline in Europe of 560bps YoY (to 36.5% in 1QFY20). The stress on gross margins is largely attributed to innovators not taking price hikes eventually deterring Sharda's ability to take pricing action.

### Europe and LATAM sales plummet, NAFTA witnesses erratic weather conditions

Sales from the European and LATAM region fell by 15.2% and 36.6% YoY to ₹ 1.68 bn and ₹ 323 mn respectively. Despite lower competitive intensity in the European region (with high concentration of innovators), margins contracted due to the company's inability to take price hikes as a proxy to innovators stance of maintaining status quo on prices in an inflationary RM cost environment. NAFTA witnessed a strong volume growth of 22.6% YoY to 1.9 mn KG's, however weaker product mix and negative realization growth took a toll on sales growth (NAFTA sales grew by 1.4% YoY to ₹ 954mn).

### Outlook and Valuation

The management has guided for a capex of ₹ 1.5-1.7bn in FY20E, capex over the next 2-3 years could be in the same range each year. We expect Sharda's strength in registrations in stricter and compliant markets could drive sales growth, we expect sales growth of 15.5% and 15.6% YoY in FY20E and FY21E respectively with a recovery in Europe and NAFTA. We have factored in lower gross margins in the range of 30-32% over FY20-21E (owing to continued pressure in China on polluting entities curtailing supply of technicals). Sharda Cropchem's rich experience in registrations and filling dossiers, net cash balance sheet (₹ 3.09bn net cash, as compared to net debt of ₹ 907mn in 1QFY19) and asset light business model is expected to drive profitability in the mid-term (with near term challenges ahead, gross margins could be under pressure). We continue to value Sharda cropchem at 15.0x FY21E EPS of ₹ 27.7, due to a correction in the stock price by 16.4% we foresee an upside of 43.0% with a target price of ₹ 415. We thus have to change our rating to Buy.

### Q1FY20 Result (₹ Mn)

Particulars	Q1FY20	Q1FY19	YoY (%)	Q4FY19	QoQ (%)
Revenue	4,230	4,571	(7.5)	7,644	(44.7)
Total Expense	3,614	3,861	(6.4)	6,102	(40.8)
EBITDA	616	711	(13.3)	1,542	(60.0)
Depreciation	352	184	92.1	380	(7.3)
EBIT	264	527	(50.0)	1,161	(77.3)
Other Income	84	35	143.1	92	(8.7)
Interest	6	36	(83.8)	2	181.1
EBT	342	526	(50.0)	1,252	(72.6)
Tax	115	184	(37.5)	195	(41.3)
RPAT	228	342	(33.5)	1,056	(78.5)
APAT	228	342	(33.5)	1,056	(78.5)
			(bps)		(bps)
Gross Margin (%)	27.8	31.2	(337)	31.1	(332)
EBITDA Margin (%)	14.6	15.5	(98)	20.2	(560)
NPM (%)	5.4	7.5	(211)	13.8	(844)
Tax Rate (%)	33.5	34.9	(140)	15.6	1791
EBIT Margin (%)	6.2	11.5	(530)	15.2	(896)

CMP	₹ 290
Target / Upside	₹ 415 / 43%
BSE Sensex	37,848
NSE Nifty	11,252

### Scrip Details

Equity / FV	₹ 902mn / ₹ 10
Market Cap	₹ 26bn
	US\$ 380mn
52-week High/Low	₹ 419/₹ 255
Avg. Volume (no)	8,142
NSE Symbol	SHARDACROP
Bloomberg Code	SHCR IN

### Shareholding Pattern Jun'19(%)

Promoters	74.8
MF/Banks/FIs	16.7
FII	5.5
Public / Others	3.1

### Valuation (x)

	FY19A	FY20E	FY21E
P/E	14.9	12.8	10.5
EV/EBITDA	7.0	5.8	4.7
ROE (%)	14.6	14.8	15.5
RoACE (%)	13.4	13.9	14.7

### Estimates (₹ mn)

	FY19A	FY20E	FY21E
Revenue	20,011	23,119	26,720
EBITDA	3,249	4,115	4,943
PAT	1,763	2,051	2,501
EPS (₹)	19.5	22.7	27.7

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## Other highlights

Overall, volumes and realizations (realisations+product mix) de-grew by 4.2% and 4.0% YoY while favorable forex gains of 0.7% YoY led to a sales decline of 7.5% YoY in 1QFY20. The total registrations at the end of 1QFY20 were at 2325 with a pipeline of 1095 registrations

## Conference Call Highlights Q1FY20

### Business updates

- Revenue declined by 7.5% YoY to ₹ 4.2 bn which is attributable to a 4.2% volume decline and 4.0% negative effect of change in product mix but saw a favourable forex gain of 0.7%.
- Depreciation increased by 92.0% YoY from ₹ 180mn to ₹ 350 mn on the back of higher capitalization of Intangible assets.
- Gross margin declined by 320 bps YoY to 31.0% in Q1FY20 largely due to higher prices of imported technicals the effect of which the company has been unable to pass on to its customers.
- Agrochemicals business witnessed a 16.0% decline on a YoY basis largely caused by unfavourable weather conditions in NAFTA. NAFTA region is severely affected by flooding.
- Revenues in LATAM grew by 1.4 % YoY despite a 22.3 % volume growth due to unfavorable mix.
- The management has witnessed an increase in the cost of registrations over a period of time especially in eurpe and NAFTA owing to stringent processes and increasing level of registration parameters.
- The gross margins are facing pressure due to the inaction on the part of innovators to increase their prices which affects the company's price levels as the company is compulsorily required to sell its products at lower prices than those charged by the innovators.
- The management expects the china situation to stabilize and expects the supply dynamics to gradually normalize with recent indications of softening of RM prices.
- The registration process has become stricter and lengthy with increase in parameters and tests to register a product which has led to increase in cost of registrations.
- The management mentioned that the company has not been able to increase its prices to cover the rising cost of RM due to pricing status quo maintained by major MNC's and pricing policy of the company is directly linked to the pricing level maintained by these MNC's.
- Benefit of the intangibles capitalised will be spread across the next 2-3 years.

### Key Data Points

#### Region wise Gross Margin –

- Europe saw a decline of 560 bps YoY to 36.5%.
- Nafta saw a decline of 10 bps to 19.7%.
- LATAM saw a increase of 360 bps to 29.1%.
- ROW saw a decline of 350 bps to 22.2%.

### Volume Data Q1FY20 vs Q1FY19

- Europe – Declined by 3.2% from 3.1 mn kgs to 3.0 mn YoY.
- NAFTA – Increased by 18.8% from 1.6 mn Kgs to 1.9 mn YoY.
- LATAM – Declined by 32.9% from 0.8 mn kgs to 0.6 mn kgs YoY
- ROW – Declined by 30.9% from 0.7 mn kgs to 0.5 mn kgs YoY.
- Overall volume levels were down by 3.3% from 6.1 mn kgs to 5.9 mn kgs YoY.

### Total Registrations Region Wise

- Europe – 1156 NAFTA - 209 LATAM – 728 ROW – 232

### Registration Pipeline Region Wise

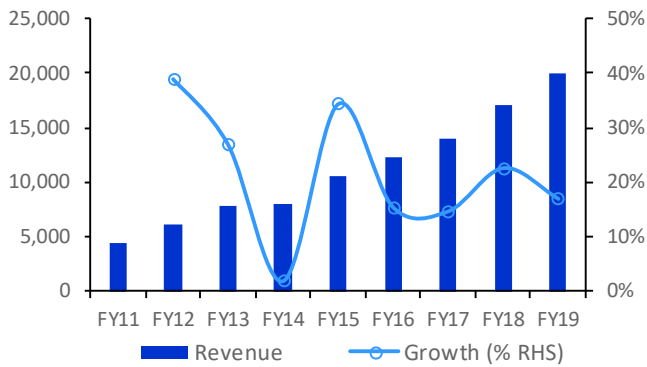
- Europe – 790 NAFTA – 83 LATAM – 168 ROW – 54

## Outlook for FY20

### Capex and guidance

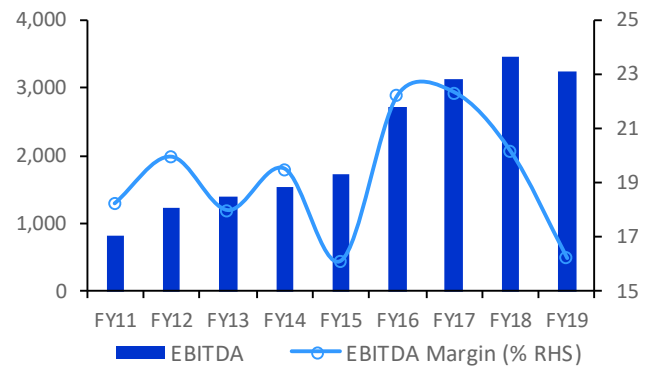
- The management has guided for a 18% growth in FY20 due to an expected recovery in the European market, normalised weather conditions in NAFTA and stable RM prices (as RM prices have peaked).
- Gross margins may not touch the previous levels of 35.0% to 36.0% and could be range bound within 28.0% to 32.0% for FY20E.
- The management guided for a Capex of ` 1.5 to 1.7bn for FY20E. The Capex for FY21 and FY22 could inch up to ` 2bn if registration cost increases. However, the management maintained a capex guidance of ` 1.5 bn to ` 1.7bn over the next 2 to 3 years.

**Exhibit 1: Revenue (₹ mn) and Growth (%)**



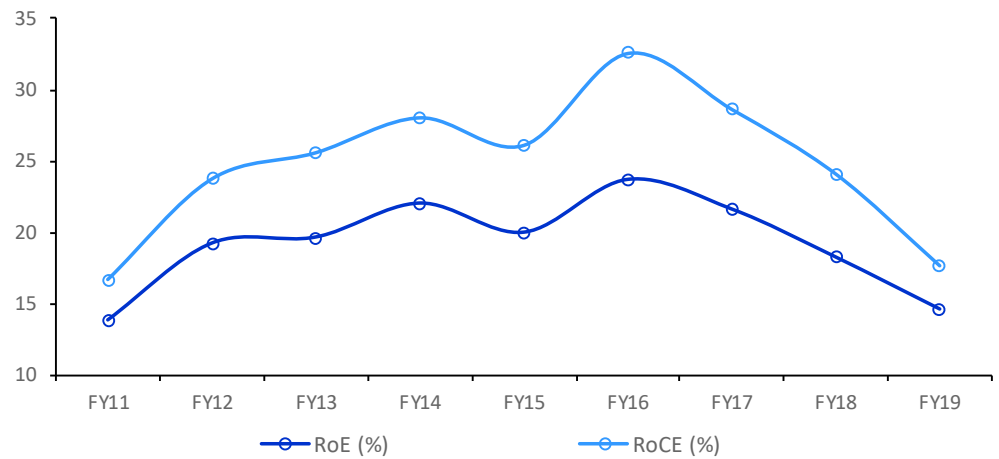
Source: Company, DART

**Exhibit 2: EBITDA (₹ mn) & EBITDA Margin (%)**



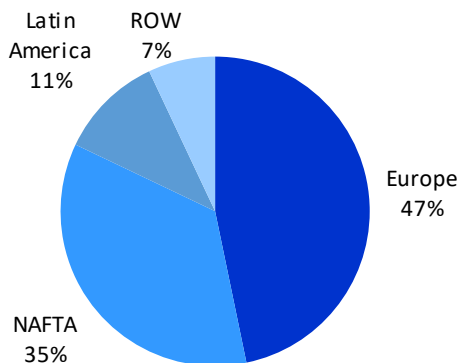
Source: Company, DART

**Exhibit 3: ROE vs ROCE (%)**



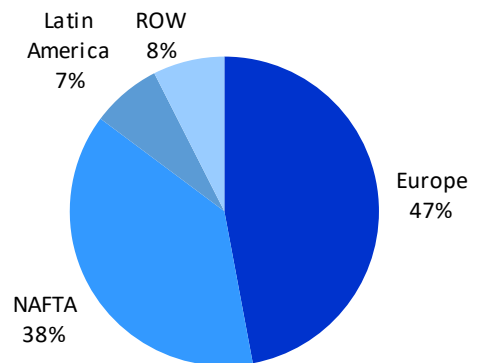
Source: Company, DART

**Exhibit 4: Revenue Share FY18 (%)**



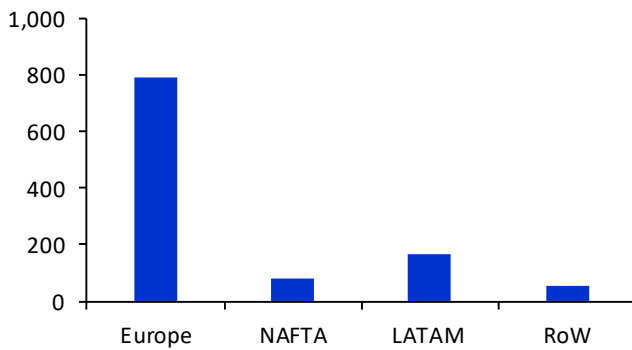
Source: Company, DART

**Exhibit 5: Revenue Share FY19 (%)**



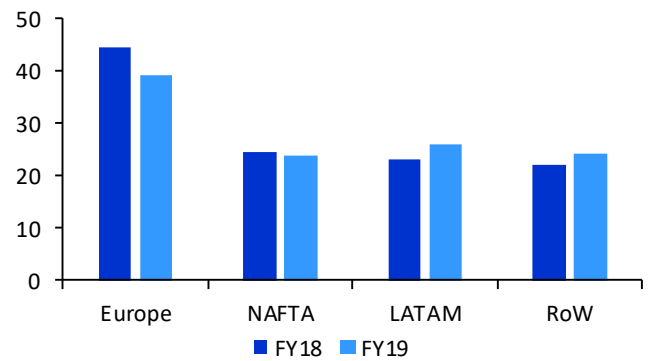
Source: Company, DART

**Exhibit 6: Registration Pipeline Q1FY20**



Source: Company, DART

**Exhibit 7: Annual Geographical Gross Margin (%)**



Source: Company, DART

**Exhibit 8: Quarterly Geographical Gross Margin (%)**

Particulars	Q1FY20 (%)	Q1FY19 (%)	Change in bps
Europe	36.5	42.1	(560)
NAFTA	19.6	19.7	(10)
LATAM	29.1	25.5	360
Rest Of the World	22.2	25.7	(350)

Source: Company, DART

**Profit and Loss Account**

(₹ Mn)	FY18A	FY19A	FY20E	FY21E
<b>Revenue</b>	<b>17,134</b>	<b>20,011</b>	<b>23,119</b>	<b>26,720</b>
<b>Total Expense</b>	<b>13,680</b>	<b>16,763</b>	<b>19,004</b>	<b>21,777</b>
COGS	11,437	13,876	15,883	18,170
Employees Cost	335	334	393	534
Other expenses	1,907	2,553	2,728	3,073
<b>EBIDTA</b>	<b>3,454</b>	<b>3,249</b>	<b>4,115</b>	<b>4,943</b>
Depreciation	699	994	1,250	1,400
<b>EBIT</b>	<b>2,755</b>	<b>2,255</b>	<b>2,865</b>	<b>3,543</b>
Interest	49	84	1	3
Other Income	166	179	220	220
Exc. / E.O. items	0	0	0	0
<b>EBT</b>	<b>2,872</b>	<b>2,350</b>	<b>3,084</b>	<b>3,761</b>
Tax	964	587	1,033	1,260
RPAT	1,908	1,763	2,051	2,501
Minority Interest	0	0	0	0
<b>Profit/Loss share of associates</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>APAT</b>	<b>1,908</b>	<b>1,763</b>	<b>2,051</b>	<b>2,501</b>

**Balance Sheet**

(₹ Mn)	FY18A	FY19A	FY20E	FY21E
<b>Sources of Funds</b>				
Equity Capital	902	902	902	902
Minority Interest	2	2	2	2
Reserves & Surplus	10,446	11,937	13,988	16,489
<b>Net Worth</b>	<b>11,348</b>	<b>12,839</b>	<b>14,890</b>	<b>17,391</b>
Total Debt	1,697	0	20	20
Net Deferred Tax Liability	831	910	910	910
<b>Total Capital Employed</b>	<b>13,879</b>	<b>13,752</b>	<b>15,822</b>	<b>18,323</b>

**Applications of Funds**

Net Block	5,862	5,915	6,315	6,515
CWIP	0	0	0	0
Investments	767	642	0	0
<b>Current Assets, Loans &amp; Advances</b>	<b>15,633</b>	<b>15,476</b>	<b>17,911</b>	<b>20,845</b>
Inventories	5,304	3,649	5,384	6,222
Receivables	8,919	8,114	9,839	11,372
Cash and Bank Balances	1,005	1,237	212	775
Loans and Advances	0	0	0	0
Other Current Assets	184	357	357	357
<b>Less: Current Liabilities &amp; Provisions</b>	<b>8,383</b>	<b>8,281</b>	<b>8,404</b>	<b>9,038</b>
Payables	6,338	6,361	6,484	7,417
Other Current Liabilities	2,045	1,920	1,920	1,620
<b>Net Current Assets</b>	<b>7,250</b>	<b>7,195</b>	<b>9,507</b>	<b>11,808</b>
<b>Total Assets</b>	<b>13,879</b>	<b>13,752</b>	<b>15,822</b>	<b>18,323</b>

E – Estimates

**Important Ratios**

Particulars	FY18A	FY19A	FY20E	FY21E
<b>(A) Margins (%)</b>				
Gross Profit Margin	33.2	30.7	31.3	32.0
EBIDTA Margin	20.2	16.2	17.8	18.5
EBIT Margin	16.1	11.3	12.4	13.3
Tax rate	33.6	25.0	33.5	33.5
Net Profit Margin	11.1	8.8	8.9	9.4
<b>(B) As Percentage of Net Sales (%)</b>				
COGS	66.8	69.3	68.7	68.0
Employee	2.0	1.7	1.7	2.0
Other	11.1	12.8	11.8	11.5
<b>(C) Measure of Financial Status</b>				
Gross Debt / Equity	0.1	0.0	0.0	0.0
Interest Coverage	56.8	26.9	2204.0	1362.8
Inventory days	113	67	85	85
Debtors days	190	148	155	155
Average Cost of Debt	5.7	9.9	13.0	13.0
Payable days	135	116	102	101
Working Capital days	154	131	150	161
FA T/O	2.9	3.4	3.7	4.1
<b>(D) Measures of Investment</b>				
AEPS (₹)	21.1	19.5	22.7	27.7
CEPS (₹)	28.9	30.6	36.6	43.2
DPS (₹)	4.0	5.0	5.5	5.5
Dividend Payout (%)	18.9	25.6	24.2	19.8
BVPS (₹)	125.8	142.3	165.0	192.8
RoANW (%)	18.2	14.6	14.8	15.5
RoACE (%)	16.1	13.4	13.9	14.7
RoAIC (%)	24.5	17.8	20.4	21.4
<b>(E) Valuation Ratios</b>				
CMP (₹)	290	290	290	290
P/E	13.7	14.9	12.8	10.5
Mcap (₹ Mn)	26,200	26,200	26,200	26,200
MCap/ Sales	1.5	1.3	1.1	1.0
EV	26,671	22,844	23,889	23,326
EV/Sales	1.6	1.1	1.0	0.9
EV/EBITDA	7.7	7.0	5.8	4.7
P/BV	2.3	2.0	1.8	1.5
Dividend Yield (%)	1.4	1.7	1.9	1.9
<b>(F) Growth Rate (%)</b>				
Revenue	22.5	16.8	15.5	15.6
EBITDA	10.6	(5.9)	26.7	20.1
EBIT	7.6	(18.1)	27.1	23.7
PBT	5.7	(18.2)	31.2	21.9
APAT	0.2	(7.6)	16.3	21.9
EPS	0.2	(7.6)	16.3	21.9
<b>Cash Flow</b>				
(₹ Mn)	FY18A	FY19A	FY20E	FY21E
CFO	170	5,026	(35)	2,166
CFI	(1,628)	(2,821)	(1,008)	(1,600)
CFF	1,323	(2,207)	(516)	(643)
FCFF	(1,848)	3,979	(1,685)	566
Opening Cash	724	612	610	(949)
Closing Cash	612	610	(949)	(1,027)

E – Estimates

### DART RATING MATRIX

Total Return Expectation (12 Months)

<b>Buy</b>	<b>&gt; 20%</b>
<b>Accumulate</b>	<b>10 to 20%</b>
<b>Reduce</b>	<b>0 to 10%</b>
<b>Sell</b>	<b>&lt; 0%</b>

### Rating and Target Price History



Month	Rating	TP (₹)	Price (₹)
Jan-18	Accumulate	484	430
May-18	Accumulate	488	428
Aug-18	Accumulate	410	369
May-19	Accumulate	415	344

\*Price as on recommendation date

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