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Q4FY20 result review and reco change

Mid-Cap

Target price: Rs1,325

Earnings revision

(%)	FY21E	FY22E
Sales	0.0	0.0
EBITDA	↓ 2.7	↓ 1.1
EPS	↓ 6.7	↓ 3.8

Target price revision

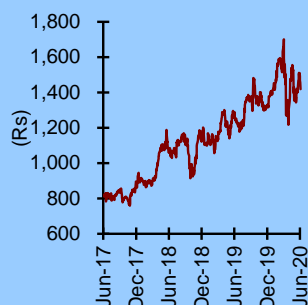
Rs1,325 from Rs1,378

Shareholding pattern

	Sep '19	Dec '19	Mar '20
Promoters	69.7	70.0	69.9
Institutional investors	19.8	19.5	19.4
MFs and other	4.5	3.7	3.4
Insurance	3.9	4.2	4.1
FII	11.4	11.6	11.9
Others	10.5	10.5	10.7

Source: BSE, NSE

Price chart



Research Analysts:

Nehal Shah

nehal.shah@icicisecurities.com
+91 22 6637 7235

Jigar Shah

jigar.shah@icicisecurities.com
+91 22 6637 7416

INDIA

Pidilite Industries

HOLD

Upgrade from Reduce

Gross margin surprises positively

Rs1,391

Despite reporting 5.8% decline in consolidated revenue, Pidilite Industries (PIDI) has reported record gross margin (up 510bps YoY) in Q4FY20 driven by lower input costs. With recovery already seen in rural and semi-urban markets (accounting for 30-35% of PIDI's revenues) and in some of its product segments like cyanoacrylate, construction chemical segments, etc, we expect sizeable volume recovery for PIDI in H2FY21. Likely cost rationalisation and further improvement in gross margin in near term (due to falling input costs) is expected to drive its consolidated EBITDA margin higher to 24.8% in FY21E. Upgrade to HOLD.

- **Valuation and outlook:** Factoring in Q4FY20 performance, we cut our earnings estimates by 6.8%/3.8% for FY21/FY22 while maintaining our revenue estimates. We now expect PIDI to report revenue and PAT CAGRs of 4.4% and 12%, respectively, over FY20-22E. We, thus, revise our target price to Rs1,325 (earlier: Rs1,378) based on 48x FY22E earnings and upgrade the stock to Hold from Reduce earlier. Key downside risks: Increase in VAM prices, high competitive intensity in construction chemical segment and sustained consumption slowdown.
- **Consolidated sales declined 5.8% YoY.** Despite registering standalone revenue growth of 9.6% YoY (until 21st Mar'20), PIDI's Q4FY20 standalone revenue declined 4.3% YoY to Rs15.4bn (I-Sec: Rs15bn) led by volume and mix decline of 4.2% (3.1% decline in consumer & bazaar segment and 4.5% decline in B2B segment). Consolidated sales too declined 5.8% YoY to Rs16.5bn. The growth was muted due to lost sales of Rs1.5bn on account of Covid-19 led lockdown in the last 10 days of Mar'20. While Apr'20 has been a washout due to the complete lockdown, May and Jun'20 have seen gradual recovery in operations. PIDI, which derives 30-35% of its sales from semi-urban/rural areas, has already seen faster recovery there and is hopeful of gradual recovery once urban areas open up. We expect PIDI's consolidated revenue to grow at 4.4% CAGR over FY20-22E.
- **Gross margin surprises positively led by softening input cost.** PIDI has reported 510bps expansion in consolidated gross margin YoY (160bps QoQ) to 55.4% as a result of further moderation in input cost QoQ. The price of vinyl acetate monomer (VAM) continues to remain at benign levels. With crude prices continuing to tread lower, we expect gross margin to sustain in the near term. EBITDA margin, which stood at 19.5%, however, was impacted due to operating deleverage. We expect benefits of lower input cost to drive EBITDA margin higher in FY21 to 24.8% despite the likely impact of operating deleverage in H1FY21.
- **Reported PBT at Rs2.6bn, down 12% YoY:** The company has reported consolidated PBT of Rs2.55bn, down 12% YoY, due to lower than expected other income and higher-than-expected depreciation. Exceptional loss of Rs330mn on account of one-time impairment of its elastomer project led to 33% YoY decline in PAT at Rs1.57bn.

Market Cap	Rs707bn/US\$9.3bn	Year to Mar (Cons)		FY19	FY20	FY21E	FY22E
Reuters/Bloomberg	PIDI.BO / PIDI IN	Revenue (Rs mn)	70,780	72,945	69,660	79,501	
Shares Outstanding (mn)	508.1	Rec. Net Income (Rs mn)	9,340	11,515	12,520	13,946	
52-week Range (Rs)	1700/1178	Rec. EPS (Rs)	18.6	22.8	24.7	27.5	
Free Float (%)	30.0	% Chg YoY	(2.0)	22.9	8.3	11.6	
FII (%)	11.9	P/E (x)	74.9	61.0	56.3	50.5	
Daily Volume (US\$/'000)	17,160	CEPS (Rs)	20.8	25.3	28.4	31.6	
Absolute Return 3m (%)	(7.0)	EV/E (x)	51.6	44.5	40.8	37.1	
Absolute Return 12m (%)	13.5	Dividend Yield (%)	0.5	0.5	0.6	0.7	
Sensex Return 3m (%)	18.8	RoCE (%)	32.3	32.7	31.8	30.8	
Sensex Return 12m (%)	(11.5)	RoE (%)	23.3	25.7	25.0	24.2	

Please refer to important disclosures at the end of this report

Table 1: Q4Y20 result review (consolidated)

(Rs mn, year ending March 31)

Particulars	Q4FY20A	Q4FY20E	Q4FY19	YoY (%)	Q3FY20	QoQ (%)	FY20	FY19	YoY (%)
Net Sales	15,447	15,046	16,393	(5.8)	19,266	(19.8)	72,945	70,786	3.0
Expenditure	12,438	11,736	13,605	(8.6)	14,634	(15.0)	57,185	57,122	0.1
Raw Materials	5,877	6,361	7,379	(20.4)	8,195	(28.3)	30,189	31,903	(5.4)
Cost of traded goods	1,018	725	769	32.3	709	43.6	3,836	3,963	(3.2)
Staff Cost	2,131	2,050	2,171	(1.9)	2,361	(9.7)	9,272	8,367	10.8
Other Expenditure	3,412	2,600	3,285	3.9	3,371	1.2	13,887	12,889	7.7
Operating Profit	3,009	3,310	2,788	7.9	4,632	(35.0)	15,760	13,664	15.3
OPM (%)	19.5	22.0	17.0	250bps	24.0	-450bps	21.6	19.3	230bps
Other Income	140	525	562	(75.2)	398	(65.0)	1,494	1,466	1.9
Interest	98	73	66	49.0	82	19.5	336	261	28.9
Depreciation	501	434	390	28.6	419	19.7	1,699	1,327	28.0
Exceptional items	(330)	0	(110)		0		(552)	(154)	
PBT	2,550	3,328	2,895	(11.9)	4,530	(43.7)	15,219	13,543	12.4
Tax	656	825	431	52.1	1,084	(39.5)	3,477	4,132	(15.9)
PAT	1,894	2,503	2,464	(23.1)	3,445	(45.0)	11,742	9,410	24.8
Minority Interest	10	(10)	(17)	(159.0)	(43)	(123.6)	(10)	(35)	(71.3)
Profit in associate company	1	17	15	(93.2)	16	(93.7)	15	27	(44.6)
Adjusted PAT	1,905	2,510	2,461	(22.6)	3,418	(44.3)	11,747	9,403	24.9
Reported PAT	1,575	2,510	2,351	(33.0)	3,418	(53.9)	11,195	9,249	21.0
Adjusted NPM (%)	10.2	16.7	14.3	-410bps	17.7	-750 bps	15.3	13.1	400bps
Gross margins (%)	55.4	52.9	50.3	510bps	53.8	160bps	53.4	49.3	410bps

Source: Company data, I-Sec research

Table 2: Segment-wise consolidated revenue breakup

(Rs mn)

	Q4FY20A	Q4FY19	YoY (%)	Q3FY20	QoQ (%)	FY20	FY19	YoY (%)
Revenue								
Consumer & Bazaar Products	11,244	11,975	-6.1%	14,783	-23.9%	55,739	54,192	2.9%
Industrial Products	4,411	4,549	-3.0%	4,626	-4.7%	17,968	17,302	3.8%
Others	151	213	-28.9%	216	-29.9%	765	899	-14.9%
Total	15,806	16,737	-5.6%	19,625	-19.5%	74,471	72,393	2.9%
Less: Inter Segment revenue	-359	-344	4.3%	-359	0.0%	-1,526	-1,613	-5.4%
Net revenues	15,447	16,393	-5.8%	19,266	-19.8%	72,945	70,780	3.1%

Source: Company data, I-Sec research

Table 3: Segment-wise consolidated PBIT

(Rs mn)

	Q4FY20A	Q4FY19	YoY (%)	Q3FY20	QoQ (%)	FY20	FY19	YoY (%)
PBIT								
Consumer & Bazaar Products	2,787	2,874	-3.0%	4,488	-37.9%	15,473	13,867	11.6%
Industrial Products	732	565	29.7%	688	6.4%	2,710	2,160	25.5%
Others	-11	-16	-30.8%	3	-532.0%	-46	-80	-43.1%
Total	3,509	3,423	2.5%	5,179	-32.2%	18,137	15,947	13.7%

Source: Company data, I-Sec research

Table 4: Segment-wise consolidated PBIT margin

(%)

	Q4FY20A	Q4FY19	YoY (%)	Q3FY20	QoQ (%)	FY20	FY19	YoY (%)
PBIT Margin (%)								
Consumer & Bazaar Products	24.8%	24.0%	79 bps	30.4%	-557 bps	27.8%	25.6%	217 bps
Industrial Products	16.6%	12.4%	420 bps	14.9%	173 bps	15.1%	12.5%	260 bps
Total	22.7%	20.9%	183 bps	26.9%	-417 bps	24.9%	22.5%	233 bps

Source: Company data, I-Sec research

Table 5: Change in estimates

Estimates	Old		New		Change (%)	
	FY21E	FY22E	FY21E	FY22E	FY21E	FY22E
Revenue	69,660	79,501	69,660	79,501	0.0%	0.0%
EBITDA	17,763	19,080	17,276	18,874	-2.7%	-1.1%
EBITDA margins	25.5%	24.0%	24.8%	23.7%	-70bps	-30bps
Reported PAT	13,453	14,551	12,545	13,996	-6.7%	-3.8%
Reported EPS	26.5	28.6	24.7	27.5	-6.8%	-3.8%

Source: Company data, I-Sec research

Key takeaways from conference call:

Standalone business performance

- Overall standalone revenue declined 4.3% for the quarter with sales volume and mix declining 4.2% YoY.
- C&B segment saw 4.8% decline in growth for the quarter due to Covid-19 led lockdown in Mar'20 which led to revenue loss for a period of 10 days. Sales volume and mix declined 3.1% for the segment.
- B2B segment saw 3.2% decline in growth for the quarter due to revenue loss on account of lockdown for a period of 10 days (in Mar'20). Sales volume and mix declined 4.5% for the segment.
- Overall standalone revenue loss for the last 10 days stood at Rs1.5bn or 11% of Q4FY19 sales. Adjusted for the same, standalone revenue for the quarter would have grown by 6% YoY.
- Gross margin for the quarter improved 470+bps YoY and 190+bps QoQ driven by lower input costs.

Consolidated business performance

- C&B segment saw 6.1% decline in growth for the quarter due to Covid-19 led lockdown in Mar'20 which led to revenue loss for a period of 10 days.
- B2B segment saw 3% decline in growth for the quarter due to revenue loss on account of lockdown for a period of 10 days.
- Gross margin for the quarter improved 500+bps YoY and 150+bps QoQ driven by lower input costs.

Performance of domestic subsidiaries

- Growth of domestic subsidiaries was impacted due to Covid-19 led lockdown. While Cipy Polyurethane saw 27% YoY decline in growth, Nina Percept and ICA Pidilite had single digit decline in growth.
- Nina Percept delivered loss for the quarter at EBITDA level while ICA Pidilite posted impressive growth at EBITDA level driven by scaling up of its local manufacturing.
- Nina Percept and Cipy continue to face challenging market conditions in the wake of economic slowdown in real estate, auto and engineering sectors and Covid-19 led lockdown.
- PIDI has entered into a definitive agreement with Tenax SPA Italy (Tenax Italy - leading manufacturer of adhesives, coating, surface treatment chemicals and abrasives for the marble, granite and stone industry) for acquiring 70% of share capital in Tenax India Stone Products for a cash consideration of Rs0.8bn.
- Tenax India is a subsidiary of Tenax Italy and is engaged in sales and distribution of Tenax Italy products for the retail market in India.

Performance of international subsidiaries

- Subsidiary in Bangladesh has reported higher sales (24% growth YoY) and impressive EBITDA growth (32% growth YoY) for the quarter.
- Dubai and Egypt subsidiaries also delivered impressive performance for the quarter.
- Sales for subsidiaries in Sri Lanka, USA and Brazil got severely impacted in March 2020 due to lockdown in respective geographies.
- Apr'20 was a complete wash out for the company. However, May and June has seen the country gradually opening up for business.
- Rural/semi urban areas which contribute 30-35% to PIDI's revenues have seen faster recovery and are likely to outpace urban areas in terms of growth in the near term.
- In terms of states, Maharashtra and Gujarat are unlocking gradually – particularly in cities like Mumbai, Pune and Surat.
- Markets in South (excluding Chennai) and East India are opening much faster compared to markets in North, West and Central India.
- **Input prices**
 - Muted demand for PVA has led to VAM prices hovering around US\$650-700/te
 - These prices are unlikely to sustain going forward.
 - Average pricing of VAM consumption for Q4FY20 was at US\$840-850/te.
 - PIDI currently has two months of high cost inventory of VAM. The benefits of lower VAM prices are likely to trickle down post Aug'20.
- PIDI sources key RMs (chemicals) from multiple vendors and has not been solely dependent on China. The company sees no risk in sourcing RM going forward. Maintenance and repair-related adhesive and construction chemical products (like Cyanoacrylate, waterproofing, etc.) have seen faster recovery versus other portfolio products.
- Migration of masons and carpenters has created shortage of manpower but they are likely to head back to work once demand starts reviving.
- Company has higher business contribution from individual home owner's vs large real estate projects.
- Company acquired 2.04% stake in Pepperfry for an amount of Rs715mn during the quarter. The investment is strategic in nature with a long-term perspective.
- As far as cost rationalisation is concerned, PIDI has deferred salary increments for the current year and would take a call on the same over the next two quarters.
- Other income was lower mainly due to lower interest rates during the quarter and higher MTM gain on investments in the corresponding quarter of the previous year.
- Inventory levels at dealer's end remain at 7-15 days while at company level it is at 30 days, which are normalised levels.

- Company has maintained or strengthened its market share in select products in FY20.
- PIDI's construction and paint chemicals segment grew in double digit in FY20.
- Company has shifted institutional-related revenue/businesses - joinery business and institutional business of construction chemicals (CIPY and waterproofing services) from consumer & bazaar segment to erstwhile industrial segment business which is now renamed as business to business segment (B2B). At standalone level, the movement is to the tune of Rs2.3bn while at consolidated level it is more than Rs5bn.

Financial summary (consolidated)

Table 6: Profit & loss statement
(Rs mn, year ending March 31)

	FY19	FY20	FY21E	FY22E
Net Revenues	70,780	72,945	69,660	79,501
Operating Expenses	57,098	57,185	52,384	60,627
EBITDA	13,682	15,760	17,276	18,874
% margins	19.3%	21.6%	24.8%	23.7%
Depreciation & Amortisation	1,327	1,699	1,879	2,047
Gross Interest	261	336	355	261
Other Income	1,286	942	1,393	1,749
Recurring PBT	13,380	14,667	16,435	18,315
Less: Taxes	4,132	3,477	3,862	4,304
Less: Minority Interest	35	56	52	65
Net Income (Reported)	9,213	11,134	12,520	13,946
Extraordinaries (Net)	(127)	(381)	-	-
Recurring Net Income	9,340	11,515	12,520	13,946

Source: Company data, I-Sec research

Table 7: Balance sheet
(Rs mn, year ending March 31)

	FY19	FY20	FY21E	FY22E
Assets				
Total Current Assets	26,664	32,705	33,234	38,212
of which cash & cash eqv.	1,904	7,033	4,231	7,759
Total Current Liabilities & Provisions	13,281	16,130	13,816	14,834
Net Current Assets	13,383	16,574	19,418	23,377
Investments				
of which	15,477	11,862	14,862	17,862
Strategic/Group	16,897	20,660	21,881	22,934
Others	-	-	-	-
Net Fixed Assets	-	-	-	-
Goodwill	45,757	49,097	56,161	64,174
Total Assets				
Liabilities	1,111	1,691	1,691	1,791
Borrowings	1,094	693	693	693
Deferred Tax Liability	2,072	2,157	2,209	2,274
Minority Interest	508	508	508	508
Equity Share Capital	1	1	1	1
Face Value per share (Rs)	40,973	44,048	51,060	58,908
Reserves & Surplus				
Net Worth	41,481	44,556	51,568	59,416
Total Liabilities	45,757	49,097	56,161	64,174

Source: Company data, I-Sec research

Table 8: Quarterly trends
(Rs mn, year ending March 31)

	Jun-19	Sep-19	Dec-19	Mar-20
Total Income	20,166	18,066	19,266	15,447
% growth (YoY)	10.0%	2.8%	4.3%	-5.8%
EBITDA	4,437	3,682	4,632	3,009
Margin (%)	22.0	20.4	24.0	19.5
Other income	399	558	398	140
Add: Extraordinaries	-	(222)	-	(330)
Net profit	2,929	3,445	3,418	1,575

Source: Company data, I-Sec research

Table 9: Cashflow statement
(Rs mn, year ending March 31)

	FY19	FY20	FY21E	FY22E
Operating Cash flow	10,651	9,385	14,425	16,042
Working Capital Changes	(1,557)	1,914	(5,695)	(482)
Capital Commitments	(2,114)	(5,462)	(3,100)	(3,100)
Free Cash Flow	6,980	5,837	5,630	12,461
Cash flow from Investing Activities	(3,018)	3,615	(3,000)	(3,000)
Issue of Share Capital	-	-	-	-
Inc (Dec) in Borrowings	(115)	581	-	100
Dividend paid	(3,674)	(4,526)	(5,481)	(6,083)
Change in Deferred Tax Liability	95	(379)	50	50
Chg. in Cash & Bank balance	269	5,128	(2,801)	3,528

Source: Company data, I-Sec research

Table 10: Key ratios
(Year ending March 31)

	FY19	FY20	FY21E	FY22E
Per Share Data (in Rs.)				
EPS(Basic Recurring)	18.6	22.8	24.7	27.5
Diluted Recurring EPS	20.8	25.3	28.4	31.6
Recurring Cash EPS	6.5	7.5	9.0	10.0
Dividend per share (DPS)	85.7	91.9	105.8	121.4
Book Value per share (BV)				
Growth Ratios (%)	16.4	3.1	-4.5	14.1
Operating Income	2.0	15.2	9.6	9.2
EBITDA	-2.0	22.9	8.3	11.6
Recurring Net Income	-2.3	21.6	12.1	11.2
Diluted Recurring EPS				
Diluted Recurring CEPS	74.9	61.0	56.3	50.5
Valuation Ratios	66.8	54.9	49.0	44.1
P/E	16.2	15.1	13.1	11.5
P/CEPS	51.6	44.5	40.8	37.1
P/BV	10.0	9.6	10.1	8.8
EV / EBITDA				
EV / Operating Income	50.7	46.6	45.8	46.7
EV / Op. FCF (pre -Capex)	11.8	12.7	11.7	11.3
Operating Ratios	11.2	11.0	11.0	11.3
COGS/Sales (%)	0.1	0.1	0.1	0.1
Employee/Sales (%)	30.9	23.7	23.5	23.5
SG&A/Sales (%)	72.7	79.0	87.0	75.0
Other Income / PBT (%)	48.2	52.0	58.0	50.0
Effective Tax Rate (%)	54.5	58.0	60.0	55.0
Receivables (days)	29.9	31.0	31.0	30.0
Payables (days)	0.0	-0.1	0.0	-0.1
Profitability Ratios (%)				
Recurring Net Income	13.3	15.9	18.0	17.6
Margins	32.3	32.7	31.8	30.8
RoCE	23.3	25.7	25.0	24.2
Dividend Payout Ratio	43.2	41.3	44.1	43.9
Dividend Yield	0.5	0.5	0.6	0.7
EBITDA Margins	19.3	21.6	24.8	23.7

Source: Company data, I-Sec research

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