

CMP: ₹ 110

Target: ₹ 135 (23%)

Target Period: 12 months

July 6, 2020

BUY

Steady state performance, inexpensive valuations

Phillips Carbon (PCBL) reported a steady performance in Q4FY20. Net sales in Q4FY20 were at ₹ 700 crore, down 24% YoY. Carbon black sales were at ₹ 680 crore, down 24% YoY, while power segment sales were at ₹ 39 crore, down 7% YoY. Carbon black sales volume in Q4FY20 was at ~99,000 tonne (down 3% YoY) with consequent realisations at ₹ 69/kg vs. ₹ 88/kg in Q4FY19. EBITDA in Q4FY20 was at ₹ 99 crore with EBITDA margins at 14.2% and consequent EBITDA/tonne at ₹ 10,000/tonne. PAT in Q4FY20 was at ₹ 72 crore, almost flat YoY, supported by a negative tax rate. On the B/S side, gross debt was down from ₹ 796 crore in FY19 to ₹ 719 crore in FY20. On the cash flow front, CFO for FY20 was at ~₹ 550 crore led by improved net working capital cycle with FCF for the year at ~₹ 200 crore (>10% FCF yield).

Replacement tyre market to support volumes in near term

Carbon black finds major application in the tyre industry wherein it is used a reinforcement agent and constitutes ~23-25% of tyre by weight. Tyre industry derives ~30% of its demand from the OEM market and rest ~70% from the replacement market, which is steady state and recurrent in nature. It is more dependent on movement of goods and people as well as general economic activity. With economic activity recovering post relaxation of nationwide lockdown amid Covid-19 outbreak, we expect replacement market demand to limit de-growth in overall tyre industry and consequent support carbon black sales. PCBL, by virtue of being the market leader in this segment, is expected to benefit from this trend. However, de-growth in FY21E is inevitable. Consequently, we expect carbon black volumes of PCBL to drop to 3.25 lakh tonne from 4.06 lakh tonne in FY20, amid nearly 45 days of production loss in Q1FY21. Carbon black sales volume is then expected to recover to 4.1 lakh tonne in FY22E, up 26% YoY.

ADD revision pending in November 2020, extension likely

To safeguard domestic industry, there is an anti-dumping duty (ADD) on import of carbon black from China into India to the tune of ~US\$400/tonne. ADD is due to be revised in November 2020. In all likelihood, it is expected to get extended amid government emphasis on self-reliance (Atmanirbhar). It does not lead to an immediate rise in realisations or margins but guarantees volume offtake for domestic manufacturers, a tad better pricing and operating leverage benefits. Domestic carbon black consumption is pegged at ~8 lakh tonne with ~15-20% of carbon black (~1.5 lakh tonne in FY20E) consumption being met through imports.

Valuation & Outlook

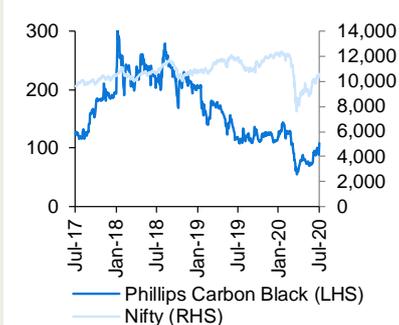
We like PCBL for its capital efficient business model (RoCE > 15%), controlled leverage on B/S (debt: equity at 0.4x in FY20) as well as robust cash flow generation. We maintain our **BUY** rating on the stock with a target price of ₹ 135 valuing it at 5.5x EV/EBITDA (8.5x implied P/E) on FY22 numbers.



Particulars

Stock Data	₹ crore
Market Capitalization	1895
Total Debt (FY20P)	719
Cash and Cash Equivalent (FY20P)	111
Enterprise Value	2503
52 week H/L (₹)	147 / 54
Equity Capital	34.5
Face Value	₹ 2

Price Chart



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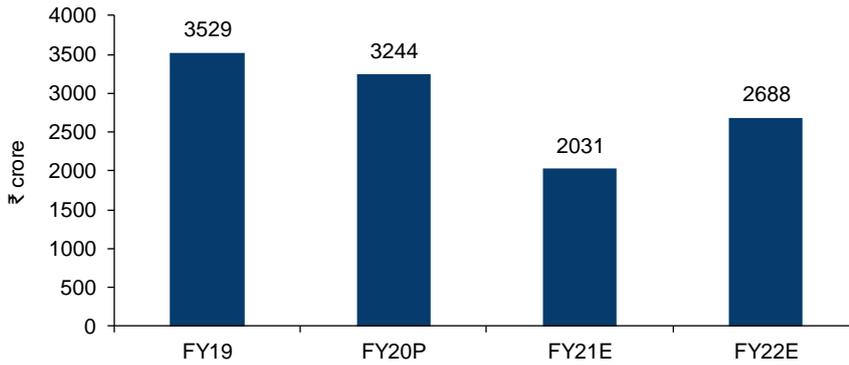
Key Financial Summary

Key Financials	FY18	FY19	FY20P	FY21E	FY22E	CAGR (FY20P-22E)
Net Sales	2,546.9	3,528.6	3,243.5	2,030.8	2,687.8	-9.0%
EBITDA	386.0	622.8	461.7	342.0	493.1	3.3%
EBITDA Margins (%)	15.2	17.6	14.2	16.8	18.3	
Net Profit	229.8	388.5	283.5	168.9	275.2	-1.5%
EPS (₹)	13.3	22.5	16.5	9.8	16.0	
P/E	8.2	4.9	6.7	11.2	6.9	
RoNW (%)	16.7	23.6	16.8	9.4	13.8	
RoCE (%)	15.6	22.8	15.4	9.7	14.9	

Source: Company, ICICI Direct Research

Financial story in charts

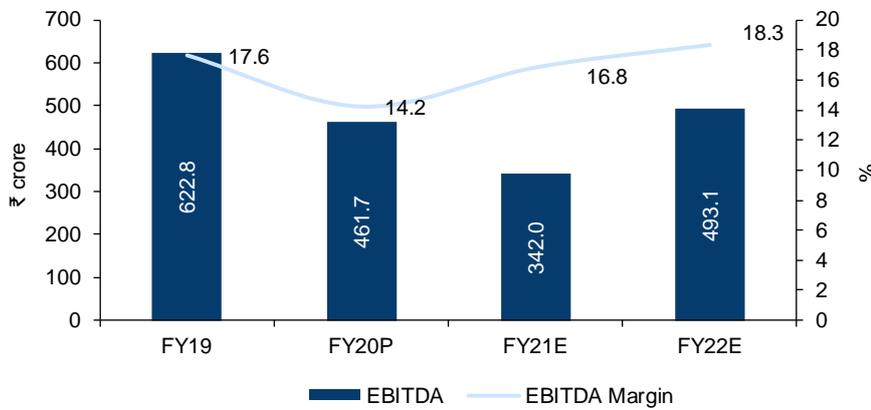
Exhibit 1: Topline trend



Revenues are seen declining at a CAGR of ~9% over FY20-22E largely driven by drop in realisations due to decline in crude price. Volumes in the aforesaid period is expected to be flat on CAGR basis at 4.1 lakh tonne in FY22E vs. 4.06 lakh tonne in FY20 and 3.25 lakh tonne in FY21E.

Source: Company, ICICI Direct Research

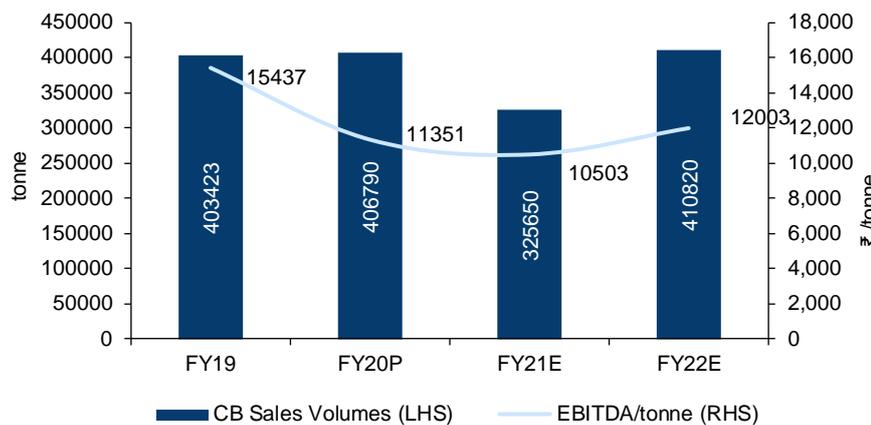
Exhibit 2: EBITDA and EBITDA margins trend



EBITDA at PCBL is seen growing at a CAGR of 3.3% over FY20-22E. Margins are expected to inch up optically tracking nearly fixed spread or EBITDA/tonne being realised by the company amidst decline in realisations.

Source: Company, ICICI Direct Research

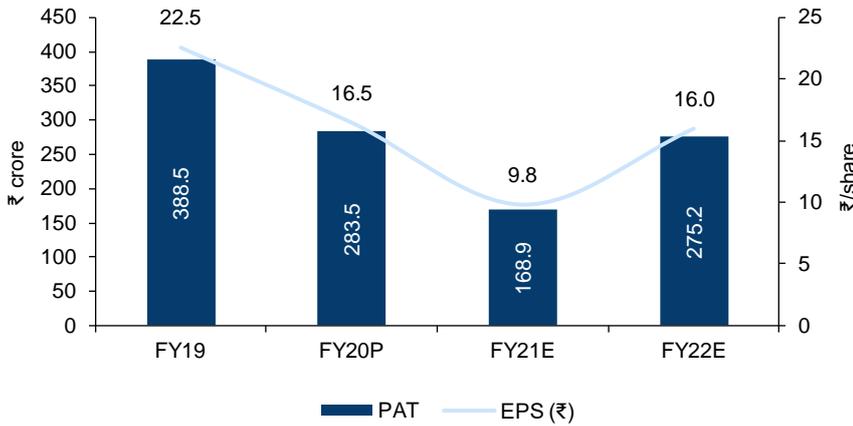
Exhibit 3: Carbon black sales volume and EBITDA/tonne trend



Sales volumes are expected to be largely flat over FY20-22E. EBITDA/tonne is expected to be steady in the range of |10,000-12,000/tonne. Increasing share of speciality grade carbon black will support the upward trajectory of EBITDA/tonne, going forward

Source: Company, ICICI Direct Research

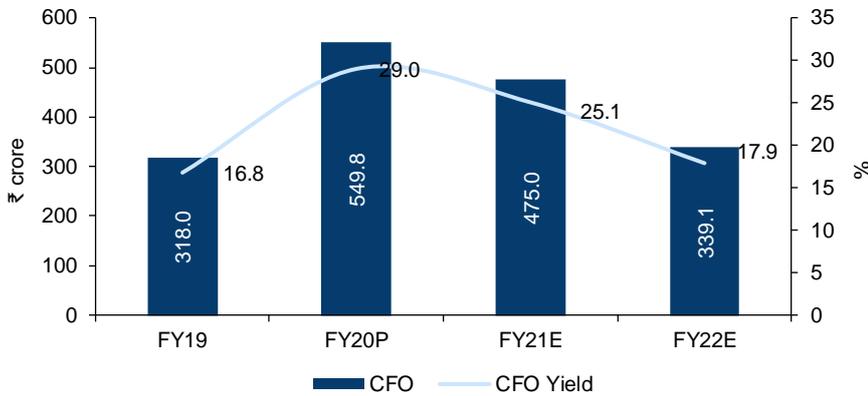
Exhibit 4: PAT and EPS trend



PAT is expected to decline at a CAGR of 1.5% over FY20-22E. We expect PCBL to clock an EPS of ₹ 16/share in FY22E

Source: Company, ICICI Direct Research

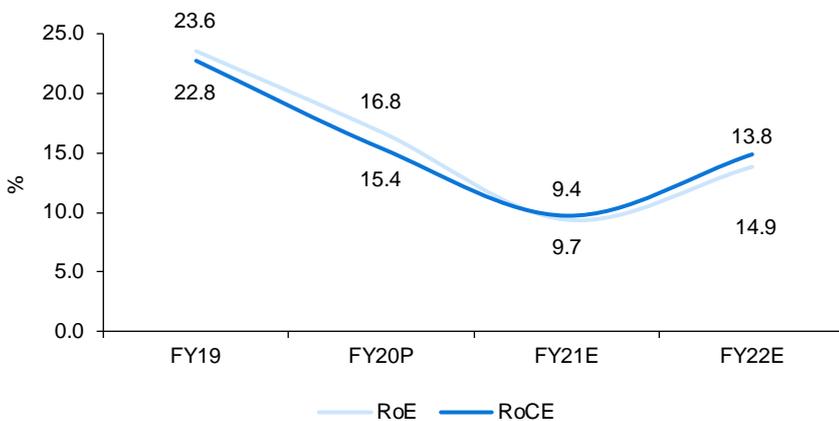
Exhibit 5: CFO and CFO yield trend



Robust cash flow generation is USP of PCBL with company offering healthy cash flow yield > 15% on consistent basis over FY19-22E. It provides much support to our investment thesis for PCBL

Source: Company, ICICI Direct Research

Exhibit 6: Return ratios trend



Return ratios are seen muted in FY21E due to drop in sales and earnings due to Covid-19. They are expected to recover to its more sustainable range of ~15% in FY22E

Source: Company, ICICI Direct Research

Financial Summary

Exhibit 7: Profit and loss statement					₹ crore
(Year-end March)	FY19	FY20P	FY21E	FY22E	
Net Sales	3528.6	3243.5	2030.8	2687.8	
Other Operating Income	0.0	0.0	0.0	0.0	
Total Operating Income	3528.6	3243.5	2030.8	2687.8	
Growth (%)	39.0	-8.1	-37.4	32.4	
Raw Material Expenses	2,296.6	2,189.5	1,235.9	1,653.0	
Employee Expenses	110.9	134.4	136.1	140.7	
Selling Expense	141.1	129.7	81.2	107.5	
Other Operating Expense	357.2	328.2	235.5	293.5	
Total Operating Expenditur	2,905.8	2,781.8	1,688.7	2,194.7	
EBITDA	622.8	461.7	342.0	493.1	
Growth (%)	49.0	-25.9	-25.9	44.2	
Depreciation	66.4	90.6	106.8	119.7	
Interest	36.4	44.5	43.5	37.0	
Other Income	18.8	24.2	19.4	20.4	
PBT	538.8	350.8	211.1	356.8	
Exceptional Item	0.0	0.0	0.0	0.0	
Total Tax	150.3	67.3	42.2	81.6	
PAT	388.5	283.5	168.9	275.2	
Growth (%)	69.1	-27.0	-40.4	62.9	
EPS (₹)	22.5	16.5	9.8	16.0	

Source: Company, ICICI Direct Research

Exhibit 8: Cash flow statement					₹ crore
(Year-end March)	FY19	FY20P	FY21E	FY22E	
Profit after Tax	388.5	283.5	168.9	275.2	
Add: Depreciation	66.4	90.6	106.8	119.7	
(Inc)/dec in Current Assets	-319.0	177.3	384.2	-218.3	
Inc/(dec) in C L and Provision	145.7	-46.1	-228.5	125.5	
Others	36.4	44.5	43.5	37.0	
CF from operating activitie	318.0	549.8	475.0	339.1	
(Inc)/dec in Investments	-46.4	207.1	-125.0	10.0	
(Inc)/dec in Fixed Assets	-275.8	-360.8	-120.0	-120.0	
Others	18.3	-2.8	0.0	0.0	
CF from investing activitie:	-303.9	-156.5	-245.0	-110.0	
Issue/(Buy back) of E equity	0.0	0.0	0.0	0.0	
Inc/(dec) in loan funds	75.6	-77.3	-100.0	-100.0	
Interest & Dividend paid	-108.8	-189.2	-103.8	-123.1	
Inc/(dec) in Share Cap	0.0	0.0	0.0	0.0	
Others	-40.4	-95.1	0.0	0.0	
CF from financing activitie	-73.5	-361.6	-203.8	-223.1	
Net Cash flow	-59.4	31.7	26.2	6.0	
Opening Cash	139.0	79.6	111.3	137.4	
Closing Cash	79.6	111.3	137.4	143.4	

Source: Company, ICICI Direct Research

Exhibit 9: Balance Sheet					₹ crore
(Year-end March)	FY19	FY20P	FY21E	FY22E	
Liabilities					
Equity Capital	34.5	34.5	34.5	34.5	
Reserve and Surplus	1,613.6	1,657.2	1,765.8	1,954.9	
Total Shareholders fund	1648.1	1691.7	1800.3	1989.3	
Total Debt	796.3	719.0	619.0	519.0	
Deferred Tax Liability	257.6	254.9	254.9	254.9	
Minority Interest / Others	0.0	0.0	0.0	0.0	
Total Liabilities	2701.9	2665.6	2674.2	2763.2	
Assets					
Gross Block	1746.5	1976.7	2296.7	2492.3	
Less: Acc Depreciation	246.1	336.8	443.6	563.3	
Net Block	1500.3	1640.0	1853.1	1929.0	
Capital WIP	175.0	305.6	105.6	30.0	
Total Fixed Assets	1,675.4	1,945.6	1,958.7	1,959.0	
Investments	383.8	176.7	301.7	291.7	
Inventory	460.3	326.2	222.5	294.6	
Debtors	652.7	588.2	361.6	478.7	
Loans and Advances	102.3	91.6	57.4	75.9	
Other Current Assets	20.8	52.7	33.0	43.6	
Cash	79.6	111.3	137.4	143.4	
Total Current Assets	1,315.6	1,170.0	812.0	1,036.2	
Current Liabilities	573.3	530.5	333.8	441.8	
Provisions	84.5	85.9	54.1	71.6	
Current Liabilities & Prov	657.8	616.4	387.9	513.4	
Net Current Assets	657.8	553.6	424.1	522.8	
Others Assets	-15.0	-10.3	-10.3	-10.3	
Application of Funds	2701.9	2665.6	2674.2	2763.2	

Source: Company, ICICI Direct Research

Exhibit 10: Key ratios				
(Year-end March)	FY19	FY20P	FY21E	FY22E
Per share data (₹)				
EPS	22.5	16.5	9.8	16.0
Cash EPS	26.4	21.7	16.0	22.9
BV	95.7	98.2	104.5	115.5
DPS	3.5	7.0	3.5	5.0
Cash Per Share (Incl Invst)	26.9	16.7	25.5	25.3
Operating Ratios (%)				
EBITDA Margin	17.6	14.2	16.8	18.3
PAT Margin	11.0	8.7	8.3	10.2
Inventory days	47.6	36.7	40.0	40.0
Debtor days	67.5	66.2	65.0	65.0
Creditor days	59.3	59.7	60.0	60.0
Return Ratios (%)				
RoE	23.6	16.8	9.4	13.8
RoCE	22.8	15.4	9.7	14.9
RoIC	23.6	16.4	9.9	14.4
Valuation Ratios (x)				
P/E	4.9	6.7	11.2	6.9
EV / EBITDA	4.0	5.4	6.7	4.6
EV / Net Sales	0.7	0.8	1.1	0.8
Market Cap / Sales	0.5	0.6	0.9	0.7
Price to Book Value	1.2	1.1	1.1	1.0
Solvency Ratios				
Debt/EBITDA	1.3	1.6	1.8	1.1
Debt/Equity	0.5	0.4	0.3	0.3
Current Ratio	1.9	1.7	1.7	1.7
Quick Ratio	1.2	1.2	1.2	1.2

Source: Company, ICICI Direct Research

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Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: < -15%



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