

November 11, 2020

Q2FY21 Result Update

Change in Estimates | Target | Reco

Change in Estimates

	Current		Previous	
	FY22E	FY23E	FY22E	FY23E
Rating	ACCUMULATE		ACCUMULATE	
Target Price	1,020		1,024	
Sales (Rs. m)	52,541	71,924	52,219	71,803
% Chng.	0.6	0.2		
EBITDA (Rs. m)	12,418	21,138	13,039	21,710
% Chng.	(4.8)	(2.6)		
EPS (Rs.)	42.5	80.9	42.7	80.7
% Chng.	(0.3)	0.2		

Key Financials - Standalone

Y/e Mar	FY20	FY21E	FY22E	FY23E
Sales (Rs. m)	39,944	35,605	52,541	71,924
EBITDA (Rs. m)	9,296	8,938	12,418	21,138
Margin (%)	23.3	25.1	23.6	29.4
PAT (Rs. m)	5,232	4,956	7,412	14,092
EPS (Rs.)	30.0	28.4	42.5	80.9
Gr. (%)	8.1	(5.3)	49.6	90.1
DPS (Rs.)	1.0	1.0	4.3	8.1
Yield (%)	0.1	0.1	0.4	0.8
RoE (%)	19.2	16.4	21.4	31.8
RoCE (%)	16.2	14.4	18.3	27.9
EV/Sales (x)	5.0	5.7	3.9	2.8
EV/EBITDA (x)	21.3	22.6	16.4	9.7
PE (x)	34.9	36.8	24.6	13.0
P/BV (x)	6.3	5.8	4.8	3.6

Key Data

ARTI.BO | ARTO IN

52-W High / Low	Rs.1,229 / Rs.662
Sensex / Nifty	43,594 / 12,749
Market Cap	Rs.183bn/ \$ 2,455m
Shares Outstanding	174m
3M Avg. Daily Value	Rs.772.81m

Shareholding Pattern (%)

Promoter's	47.55
Foreign	7.52
Domestic Institution	15.78
Public & Others	29.15
Promoter Pledge (Rs bn)	0.01

Stock Performance (%)

	1M	6M	12M
Absolute	4.9	2.3	28.4
Relative	(2.6)	(26.0)	18.9

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Pharma segment remains the bright spot

Quick Pointers:

- Inventory clear out of discretionary products in non-regular markets leading to lower margins in specialty chemicals segment.
- Pharma segment (~17% of revenues) remains as a key growth driver with 68%YoY EBIT growth in Q2FY21.
- Next leg of Aarti's growth will ride on long-term contracts worth Rs110bn, which has been delayed and will start from Q1FY22E.

We tweak our FY21 estimates to factor delay in commissioning of long term contract and make other changes. AIL's near term growth trajectory will face headwinds from weakness in discretionary spend (textiles, autos, aerospace etc; ~40% of AIL's revenues) and weak global macro-economic situation. Cancellation of high margin and higher profile agrochemicals contract is a major setback as it would have opened doors to other large contracts in the segment. AIL with a diversified product portfolio of 200 products remain well placed to capitalize on rising investment in domestic downstream industries along with production shift from China. We remain structurally positive on AIL's growth prospects but will wait for better entry points given the macro challenges. Maintain ACCUMULATE with a TP of Rs1,020 (Rs1,024 earlier).

- Results ahead of estimates:** Aarti Industries (AIL) reported better than expected stand-alone results with EBIDTA and PAT of Rs2.4n (1%YoY; PLe Rs2.2bn) and Rs1.4bn (-4%YoY; PLe Rs1.1bn). EBIDTA margins for Q2 was at 21.4% (FY20 23.3%). Q2 profitability was impacted by inventory clear out of discretionary products in non-regular markets leading to lower margins along with higher operating cost from commissioning of chlorination plant.
- Net revenues for Q2 were at Rs11.3bn (+11%YoY) and includes USD5mn towards part payment of cancellation of the multi-year agro chemicals contract.
- Specialty chemicals performance remain muted:** Specialty chemicals segment revenues were at Rs10.6bn (+26%YoY) and EBIT was at Rs1.8bn (-11%YoY). During Q2, the speciality business operated at 80-90%.
- AIL's next leg of growth is likely to ride on start of two large multi-year contracts worth Rs110bn, starting from Q1FY22E.
- Pharma performance remains the bright spot:** Pharma segment revenues were at Rs2.2bn (+22%YoY) and EBIT was at Rs565m (+68%YoY) due to continued focus in off-patented generics business in regulated markets. Major expansion of API and intermediate facilities is expected to be progressively commercialized in the next 2-3 quarters, which will further aid growth.

Exhibit 1: Q2FY21 Result Overview (Rs mn)

Y/e March	Q2FY21	Q2FY20	YoY gr. (%)	Q1FY21	H1FY21	H1FY20	YoY gr. (%)
Income From Operations	11,261	10,190	10.5	9,048	20,310	21,052	(3.5)
Total Expenditure							
Cost of Material Consumed	4,847	4,985	(2.8)	4,237	9,084	10,409	(12.7)
Purchase of stock in trade	548	367	49.2	458	1,006	710	41.6
Change in inventory of FG, WIP and SIT	182	(144)	(226.0)	(367)	(186)	(94)	96.6
Employee Cost	905	711	27.2	868	1,773	1,379	28.5
Other Expense	2,373	1,886	25.8	2,094	4,467	3,893	14.7
Total Expenditure	8,854	7,805	13.4	7,289	16,144	16,297	(0.9)
EBIDTA	2,407	2,385	0.9	1,759	4,166	4,754	(12.4)
<i>% of NS</i>	<i>21.4</i>	<i>23.4</i>		<i>19.4</i>	<i>20.5</i>	<i>22.6</i>	
Depreciation	518	425	21.8	488	1,006	826	21.7
EBIT	1,889	1,960	(3.6)	1,271	3,160	3,928	(19.5)
Interest	215	304	(29.1)	252	467	607	(23.0)
Other Income	0	56	(99.8)	0	0	99	(99.8)
PBT	1,674	1,712	(2.2)	1,020	2,693	3,420	(21.3)
Tax	310	290	6.9	205	515	625	(17.6)
<i>Tax rate %</i>	<i>18.5</i>	<i>16.9</i>		<i>20.1</i>	<i>19.1</i>	<i>18.3</i>	
Profit After Tax	1,364	1,422	(4.1)	815	2,178	2,795	(22.1)
Extraordinary Items	-	-		-	-	-	
Net Profit (after Extraordinary Items)	1,364	1,422	(4.1)	1,070	2,178	2,795	(22.1)
Segment revenue							
Speciality chemicals	9,200	9,202	(0.0)	10,006	36,525	38,220	(4.4)
Pharma	2,064	2,128	(3.0)	1,762	7,558	7,258	4.1
Home & personal care	-	785	NA	-	-	3,099	NA
EBIT							
Speciality chemicals	1,663	2,006	(17.1)	2,054	7,733	7,686	0.6
Pharma	358	276	29.9	360	1,375	1,127	22.0
Home & personal care	-	2	NA	-	-	(359)	NA
Total	2,021	2,283	(11.5)	2,414	9,108	8,454	7.7

Source: Company, PL

Conference Call Highlights

- Q2 capex at Rs3bn and will be at Rs10-12bn for FY21E.
- FY21 remains a challenging year given multiple demand disruption and volatility in RM prices. Company targets 15-20% PAT CAGR over FY20-22E.
- Pharma segment is likely to report 20% growth led by new capacity expansion. Speciality segment revenues will increase Rs10bn over 3-5 yrs.
- Aarti will manufacture Dicamba intermediates and sell to domestic and Chinese players who in turn will sell to US and European players.
- Domestic discretionary demand back to pre-Covid levels while for export markets it will return in next 3-6 months.

Financials

Income Statement (Rs m)

Y/e Mar	FY20	FY21E	FY22E	FY23E
Net Revenues	39,944	35,605	52,541	71,924
YoY gr. (%)	(0.8)	(10.9)	47.6	36.9
Cost of Goods Sold	19,673	15,629	24,886	29,928
Gross Profit	20,271	19,975	27,655	41,996
Margin (%)	50.7	56.1	52.6	58.4
Employee Cost	2,923	3,204	4,729	6,473
Other Expenses	-	-	-	-
EBITDA	9,296	8,938	12,418	21,138
YoY gr. (%)	1.4	(3.8)	38.9	70.2
Margin (%)	23.3	25.1	23.6	29.4
Depreciation and Amortization	1,726	1,739	2,069	2,519
EBIT	7,569	7,199	10,349	18,618
Margin (%)	18.9	20.2	19.7	25.9
Net Interest	1,216	1,185	1,314	1,348
Other Income	105	105	116	127
Profit Before Tax	6,459	6,118	9,150	17,397
Margin (%)	16.2	17.2	17.4	24.2
Total Tax	1,227	1,163	1,739	3,305
Effective tax rate (%)	19.0	19.0	19.0	19.0
Profit after tax	5,232	4,956	7,412	14,092
Minority interest	-	-	-	-
Share Profit from Associate	-	-	-	-
Adjusted PAT	5,232	4,956	7,412	14,092
YoY gr. (%)	8.7	(5.3)	49.6	90.1
Margin (%)	13.1	13.9	14.1	19.6
Extra Ord. Income / (Exp)	-	-	-	-
Reported PAT	5,232	4,956	7,412	14,092
YoY gr. (%)	8.7	(5.3)	49.6	90.1
Margin (%)	13.1	13.9	14.1	19.6
Other Comprehensive Income	-	-	-	-
Total Comprehensive Income	5,232	4,956	7,412	14,092
Equity Shares O/s (m)	174	174	174	174
EPS (Rs)	30.0	28.4	42.5	80.9

Source: Company Data, PL Research

Balance Sheet Abstract (Rs m)

Y/e Mar	FY20	FY21E	FY22E	FY23E
Non-Current Assets				
Gross Block	36,309	40,987	50,987	60,987
Tangibles	36,309	40,987	50,987	60,987
Intangibles	-	-	-	-
Acc: Dep / Amortization	13,298	15,037	17,106	19,626
Tangibles	13,298	15,037	17,106	19,626
Intangibles	-	-	-	-
Net fixed assets	23,012	25,950	33,881	41,361
Tangibles	23,012	25,950	33,881	41,361
Intangibles	-	-	-	-
Capital Work In Progress	14,176	15,499	15,499	15,499
Goodwill	5	-	-	-
Non-Current Investments	372	356	356	356
Net Deferred tax assets	(1,890)	(2,010)	(2,193)	(2,541)
Other Non-Current Assets	3,920	-	-	-
Current Assets				
Investments	-	-	-	-
Inventories	7,815	8,196	9,314	12,751
Trade receivables	7,825	8,591	9,326	12,767
Cash & Bank Balance	2,334	2,525	591	893
Other Current Assets	318	329	378	435
Total Assets	60,892	62,571	70,582	85,422
Equity				
Equity Share Capital	871	871	871	871
Other Equity	28,147	30,423	37,093	49,776
Total Networkth	29,018	31,294	37,964	50,647
Non-Current Liabilities				
Long Term borrowings	5,776	10,408	10,408	10,408
Provisions	-	-	-	-
Other non current liabilities	5,509	4,211	-	-
Current Liabilities				
ST Debt / Current of LT Debt	12,114	11,212	11,772	12,361
Trade payables	3,242	3,547	3,865	4,648
Other current liabilities	3,343	3,981	4,379	4,817
Total Equity & Liabilities	60,892	66,662	70,582	85,422

Source: Company Data, PL Research

Cash Flow (Rs m)

Y/e Mar	FY20	FY21E	FY22E	FY23E
PBT	6,459	6,118	9,150	17,397
Add. Depreciation	1,726	1,739	2,069	2,519
Add. Interest	1,216	1,185	1,314	1,348
Less Financial Other Income	105	105	116	127
Add. Other	2,707	(1,347)	61	349
Op. profit before WC changes	12,108	7,696	12,595	21,613
Net Changes-WC	547	(223)	(1,299)	(5,836)
Direct tax	(1,227)	(1,163)	(1,739)	(3,305)
Net cash from Op. activities	11,428	6,310	9,557	12,472
Capital expenditures	(11,179)	(5,998)	(9,997)	(10,000)
Interest / Dividend Income	-	-	-	-
Others	(38)	16	-	-
Net Cash from Inv. activities	(11,217)	(5,982)	(9,997)	(10,000)
Issue of share cap. / premium	(1,608)	(2,507)	(1)	(1)
Debt changes	(2,813)	3,730	561	589
Dividend paid	(210)	(174)	(741)	(1,409)
Interest paid	(1,216)	(1,185)	(1,314)	(1,348)
Others	-	-	-	-
Net cash from Fin. activities	(5,846)	(137)	(1,495)	(2,170)
Net change in cash	(5,635)	192	(1,935)	302
Free Cash Flow	249	312	(440)	2,472

Source: Company Data, PL Research

Key Financial Metrics

Y/e Mar	FY20	FY21E	FY22E	FY23E
Per Share(Rs)				
EPS	30.0	28.4	42.5	80.9
CEPS	39.9	38.4	54.4	95.3
BVPS	166.5	179.6	217.9	290.7
FCF	1.4	1.8	(2.5)	14.2
DPS	1.0	1.0	4.3	8.1
Return Ratio(%)				
RoCE	16.2	14.4	18.3	27.9
ROIC	13.8	12.3	15.0	22.9
RoE	19.2	16.4	21.4	31.8
Balance Sheet				
Net Debt : Equity (x)	0.5	0.6	0.6	0.4
Net Working Capital (Days)	113	136	103	106
Valuation(x)				
PER	34.9	36.8	24.6	13.0
P/B	6.3	5.8	4.8	3.6
P/CEPS	26.2	27.3	19.3	11.0
EV/EBITDA	21.3	22.6	16.4	9.7
EV/Sales	5.0	5.7	3.9	2.8
Dividend Yield (%)	0.1	0.1	0.4	0.8

Source: Company Data, PL Research

Quarterly Financials (Rs m)

Y/e Mar	Q3FY20	Q4FY20	Q1FY21	Q2FY21
Net Revenue	11,767	10,200	9,048	11,261
YoY gr. (%)	(7.2)	(15.8)	(16.7)	10.5
Raw Material Expenses	6,472	5,250	4,328	5,577
Gross Profit	5,295	4,949	4,721	5,684
Margin (%)	45.0	48.5	52.2	50.5
EBITDA	2,427	2,114	1,759	2,407
YoY gr. (%)	(1.7)	(10.8)	(25.8)	0.9
Margin (%)	20.6	20.7	19.4	21.4
Depreciation / Depletion	439	462	488	518
EBIT	1,989	1,652	1,271	1,889
Margin (%)	16.9	16.2	14.1	16.8
Net Interest	283	326	252	215
Other Income	3	4	-	-
Profit before Tax	1,708	1,330	1,020	1,674
Margin (%)	14.5	13.0	11.3	14.9
Total Tax	340	260	205	310
Effective tax rate (%)	19.9	19.6	20.1	18.5
Profit after Tax	1,368	1,070	815	1,364
Minority interest	-	-	-	-
Share Profit from Associates	-	-	-	-
Adjusted PAT	1,368	1,070	815	1,364
YoY gr. (%)	3.1	(14.0)	(40.7)	(4.1)
Margin (%)	11.6	10.5	9.0	12.1
Extra Ord. Income / (Exp)	-	-	-	-
Reported PAT	1,368	1,070	815	1,364
YoY gr. (%)	3.1	(14.0)	(40.7)	(4.1)
Margin (%)	11.6	10.5	9.0	12.1
Other Comprehensive Income	-	-	-	-
Total Comprehensive Income	1,368	1,070	815	1,364
Avg. Shares O/s (m)	-	-	-	-
EPS (Rs)	-	-	-	-

Source: Company Data, PL Research

Price Chart
Recommendation History


No.	Date	Rating	TP (Rs.)	Share Price (Rs.)
1	07-Oct-20	Accumulate	1,024	1,007
2	13-Aug-20	Accumulate	1,024	1,000
3	07-Jul-20	Accumulate	1,024	930
4	15-Jun-20	Accumulate	1,024	869
5	26-May-20	Accumulate	992	1,010
6	08-Apr-20	BUY	988	855
7	13-Feb-20	BUY	1,154	972
8	03-Jan-20	BUY	988	841
9	14-Nov-19	BUY	988	799

Analyst Coverage Universe

Sr. No.	Company Name	Rating	TP (Rs)	Share Price (Rs)
1	Aarti Industries	Accumulate	1,024	1,007
2	Bharat Petroleum Corporation	BUY	479	342
3	GAIL (India)	Accumulate	108	90
4	Gujarat Gas	BUY	403	301
5	Hindustan Petroleum Corporation	BUY	280	186
6	Indian Oil Corporation	BUY	118	78
7	Indraprastha Gas	BUY	590	384
8	Mahanagar Gas	BUY	1,226	829
9	NOCIL	BUY	169	143
10	Oil & Natural Gas Corporation	BUY	96	71
11	Oil India	Accumulate	110	89
12	Petronet LNG	BUY	384	219
13	Reliance Industries	BUY	2,232	2,055

PL's Recommendation Nomenclature (Absolute Performance)

Buy	: > 15%
Accumulate	: 5% to 15%
Hold	: +5% to -5%
Reduce	: -5% to -15%
Sell	: < -15%
Not Rated (NR)	: No specific call on the stock
Under Review (UR)	: Rating likely to change shortly

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