Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Vinati Organics Limited

On the cusp of a strong earnings growth cycle

Speciality Chemcials	Sharekhan code: VINATIORGA	Company Update

3R MATRIX	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)		✓	

\+ Positive = Neutral - Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↔	

Reco/View	Change
Reco: **Buy**	↔
CMP: **Rs. 1,460**	
Price Target: **Rs. 1,750**	↑

↑ Upgrade ↔ Maintain ↓ Downgrade

Company details

Market cap:	Rs. 15,001 cr
52-week high/low:	Rs. 1,527/651
NSE volume: (No of shares)	1.9 lakh
BSE code:	524200
NSE code:	VINATIORGA
Free float: (No of shares)	2.7 cr

Shareholding (%)

Promoters	74
DII	7
FII	4
Others	16

Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	16.2	24.3	46.2	44.0
Relative to Sensex	12.3	6.6	13.3	19.8

Sharekhan Research, Bloomberg

Summary

- We expect Vinati Organics earnings cycle to gain momentum with volume ramp-up for ATBS/Butyl Phenol and sharp recovery in EBITDA margin with improvement in revenue mix towards high-margin ATBS segment (from a low of 37% in 9MFY2021 versus 57% in FY2020).
- Our positive stance on ATBS demand (key input for oil industry) and margin recovery is underpinned by expectations of a 5.5-mbpd increase in oil demand in CY21 (as per IEA) and likely higher ATBS realisation (rising demand and increase in acrylonitrile prices)
- Overall, we expect a 33% revenue CAGR and 284bps margin expansion over FY21E-FY23E, which would drive strong 32% PAT CAGR over the same period. Vinati Organics' dominant market share in ATBS/IBB, debt-free status and solid RoE of 24% makes us constructive on the company.
- Improving near to medium-term earnings growth visibility and sustained long term high double-digit growth potential warrants higher valuation multiple for Vinati Organics. Hence, we maintain Buy rating with revised PT of Rs. 1,750.

Vinati Organics' earnings momentum is expected to gather pace over FY2022E-FY2023E as we expect a steady ramp-up of utilization rate across its product categories (ATBS expanded capacity of 40ktpa from 26ktpa earlier) and new plants (volume ramp-up for its new Butyl Phenol plant). Our positive stance on ATBS demand and margin recovery stems from the expectation of sharp recovery in oil demand (International Energy Agency expects 5.5-mbpd increase in oil demand in CY2021 on the back of recovery in global economic growth) and potential higher ATBS realisation (given rising demand and increase in price of its key input - acrylonitrile). Thus, we are optimistic of a strong 33% revenue CAGR over FY2021E-FY2023E. Moreover, revenue share of high margin ATBS segment (which had declined to 37% in 9MFY2021 versus 57% in FY2020) is also expected increase over FY2022-FY2023 as ATBS demand has witnessed strong improvement from December 2020 as per the company's management. This would mean a sharp margin recovery of 284bps over FY2021-FY2023 although lower than FY2020 level of 40.2%, as meaningful revenue contribution from relatively low margin Butyl Phenol would also kick start from FY2022. We thus expect strong EBITDA/PAT CAGR of 38%/32% over FY2021E-FY2023E. We like Vinati Organics' business (global market share of 65% each in IBB and ATBS), debt-free status and a solid return profile (RoE/RoCE of 24%/31%). Hence, we maintain our Buy rating on Vinati Organics with a revised PT of Rs. 1,750. At CMP, the stock trades at 39.5x its FY2022E EPS and 31.7x its FY2023E EPS.

Our Call

Valuation – Maintain Buy on Vinati Organics with a revised PT of Rs. 1,750: We maintain our FY2021-FY2022 earnings estimates but have increased our FY2023 earnings estimate as we now assume higher volume/margin for ATBS segment. Improving near to medium term earnings growth visibility given revival in ATBS demand and sustained long term high double digit growth potential (led by development of new products and massive export opportunities) warrants higher valuation multiple for Vinati Organics. We thus retain our Buy rating on Vinati Organics with higher PT to Rs. 1,750 (valued at 38x FY2023E EPS) The stock is trading at 39.5x FY2022E EPS and 31.7x FY2023E EPS.

Key Risks

- Lower demand due to economic slowdown and a delay in the completion of expansion projects might affect revenue growth.
- Higher raw material prices and a delay in the ability to pass on price hikes adequately and adverse forex fluctuations might affect margins.

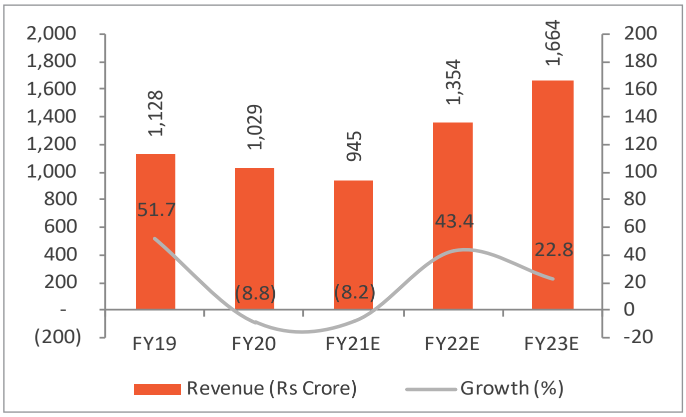
Valuation Rs cr

Particulars	FY19	FY20	FY21E	FY22E	FY23E
Net Sales	1,128	1,029	945	1,354	1,664
OPM (%)	37.5	40.2	34.9	36.9	37.8
Adjusted PAT	283	334	271	380	474
y-o-y growth (%)	107.2	18.0	(19.0)	40.5	24.6
Adjusted EPS (Rs.)	27.5	32.5	26.3	37.0	46.1
P/E (x)	53.1	44.9	55.5	39.5	31.7
P/BV (x)	14.3	11.7	10.2	8.5	7.0
EV/EBITDA (x)	35.2	35.6	44.5	28.9	22.6
RoCE (%)	41.8	34.1	22.9	30.2	31.3
RoE (%)	30.6	28.6	19.7	23.6	24.3

Source: Company; Sharekhan estimates

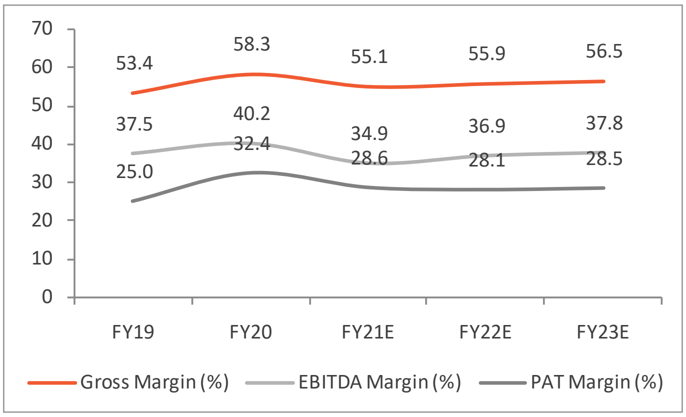
Financials in charts

Revenue growth to recover over FY22E-FY23E



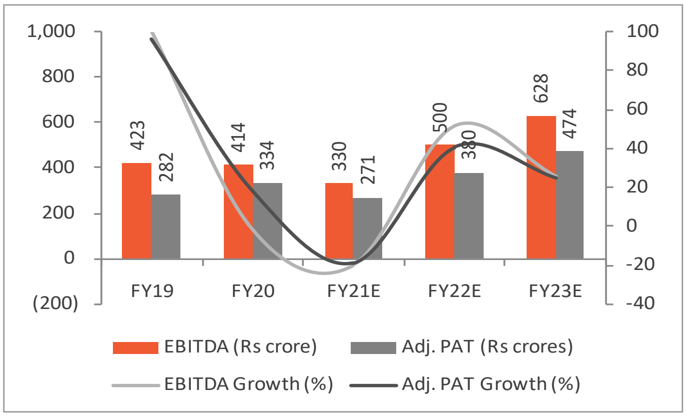
Source: Company, Sharekhan Research

Operates at a significantly higher margin profile



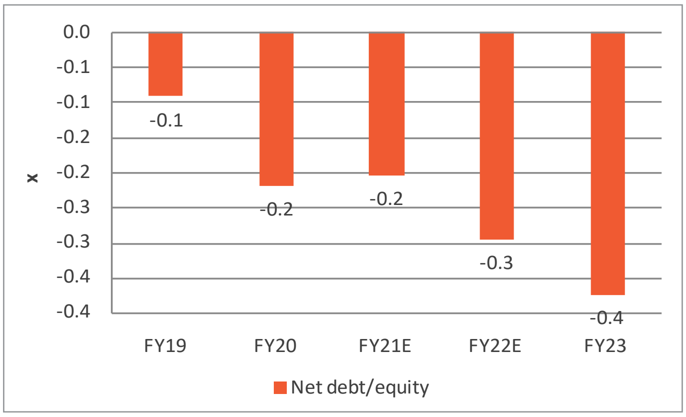
Source: Company, Sharekhan Research

EBITDA/PAT CAGR of 38%/32% over FY21E-FY23E



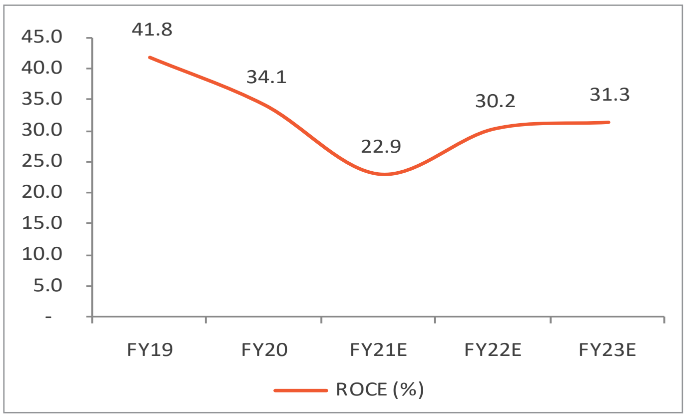
Source: Company, Sharekhan Research

Debt-free company; balance sheet to get strong further



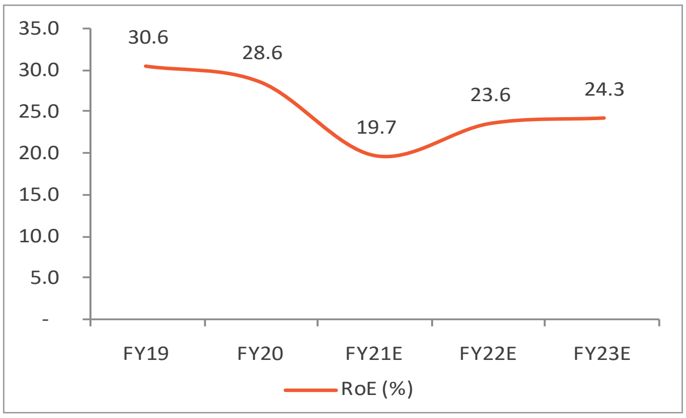
Source: Company, Sharekhan Research

RoCE trend



Source: Company, Sharekhan Research

RoE trend



Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector view - Structural growth drivers to propel sustained growth for the specialty chemicals sector in medium to long term

We remain bullish on the medium to long-term growth prospects of the specialty chemicals sector, given a massive revenue opportunity from the perspective of import substitution (India's total specialty chemical imports are estimated at $56 billion), potential increase in exports given China Plus One strategy by global customers, and favourable government policies (such as tax incentive and production-linked incentive scheme). In our view, conducive government policies, product innovation, a massive export opportunity and low input prices would help the sector sustain a high double-digit earnings growth trajectory in the next 2-3 years.

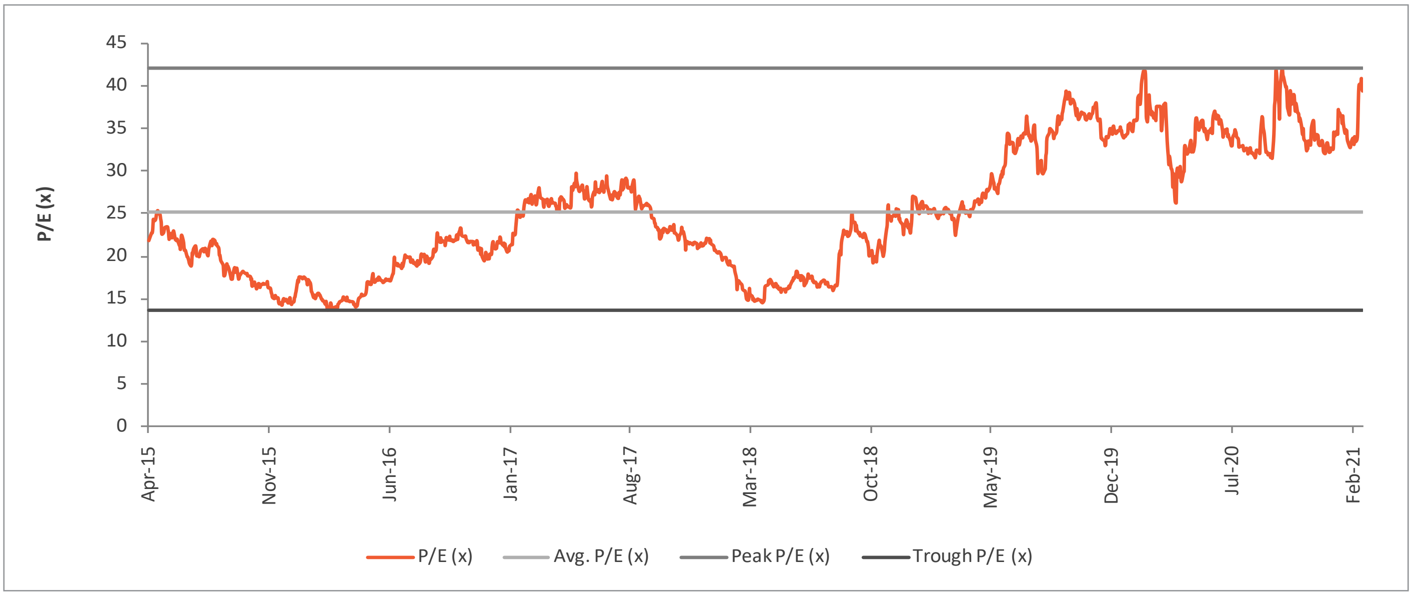
■ Company outlook - Niche business with significant market share, improvement in ATBS demand bodes well for earnings recovery

Vinati operates in niche segments and has an exceptional product basket that holds a significant market share globally. Hence, the company is able to generate significantly higher margins. This coupled with a debt-free balance sheet helps Vinati generate superior return ratios. A recovery in ATBS margins and demand and ramp-up of Butyl Phenol (peak revenue potential of Rs. 400-500 crore) would drive revenue/EBITDA/PAT CAGR of 33%/38%/32% over FY2021E-FY2023E.

■ Valuation - Maintain Buy on Vinati Organics a revised PT of Rs. 1,750

We maintain our FY2021-FY2022 earnings estimates but have increased our FY2023 earnings estimate as we now assume higher volume/margin for ATBS segment. Improving near to medium term earnings growth visibility given revival in ATBS demand and sustained long term high double digit growth potential (led by development of new products and massive export opportunities) warrants higher valuation multiple for Vinati Organics. We thus retain our Buy rating on Vinati Organics with higher PT to Rs. 1,750 (valued at 38x FY2023E EPS) The stock is trading at 39.5x FY2022E EPS and 31.7x FY2023E EPS.

One-year forward P/E (x) band



Source: Sharekhan Research

About company

Incorporated in 1989, Vinati Organics (Vinati) is one of India's leading manufacturers and exporters of specialty organic intermediaries, monomers, and polymers. Vinati is world's largest manufacturers and sellers of Isobutyl Benzene (IBB) and 2-Acrylamido 2- Methylpropane Sulfonic Acid (ATBS) having a significant market share in both the product categories. The company currently has a capacity of 25,000 TPA for IBB and 26000 TPA for ATBS. Vinati is an export oriented company, as ~70-75% of its overall revenues are derived from export markets.

Investment theme

Vinati Organics operates in niche segments and have an exceptional product basket with a significant market share in its products globally. Hence, the company is able to generate significantly higher margin profile. This coupled with a lean balance sheet (debt-free company) helps Vinati Organics to generate superior return ratios. Vinati Organics is expected to see increased volumes in ATBS (2-Acrylamido 2 Methylpropane Sulfonic Acid) due to a capacity expansion, while IB (Isobutylene) volumes are expected to rise due to enhancement of capacity utilisation and a gradual ramp-up in utilisation levels for butyl phenol.

Key Risks

Lower demand due to an economic slowdown and a delay in completion of expansion projects might impact revenue growth.Adverse raw material prices and a delay in the ability to pass on price hikes adequately and forex fluctuations might affect margins.

Additional Data

Key management personnel

Vinod Saraf	Chairman
Vinati Saraf Mutreja	Managing Director &CEO
Viral Saraf Mittal	Director-CSR & Corporate Strategy
Sunil Saraf	Non-Independent Director
N. K. Goyal	Chief Financial Officer
Milind A. Wagh	Company Secretary and Compliance Officer

Source: Bloomberg

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Mirae Asset Global Investments Company	3.2
2	Invesco Asset Management India Pvt	1.4
3	INVESTOR EDUCATION & PROTECTN FD	1.1
4	Canara Robeco Asset Management Company	0.9
5	Vanguard Group Inc/The	0.7
6	Goldman Sachs Group Inc/The	0.6
7	L&T Mutual Fund Trustee Ltd/India	0.5
8	Dimensional Fund Advisors LP	0.4
9	BlackRock Inc	0.3
10	LIC Mutual Fund Asset Management	0.3

Source: Bloomberg

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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