Stock Update

Result Update

Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

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		↔	

ESG Disclosure Score NEW

ESG RISK RATING Updated Feb 08, 2022	31.27

High Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

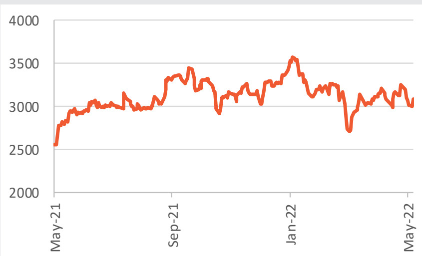
Company details

Market cap:	Rs. 2,95,788 cr
52-week high/low:	Rs. 3,588 / 2,521
NSE volume: (No of shares)	12.6 lakh
BSE code:	500820
NSE code:	ASIANPAINT
Free float: (No of shares)	45.4 cr

Shareholding (%)

Promoters	52.6
FII	20.7
DII	7.6
Others	19.1

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-2.3	-4.5	-2.0	20.6
Relative to Sensex	5.5	2.5	8.1	10.8

Sharekhan Research, Bloomberg

Asian Paints Ltd

Good Q4; Volume growth momentum to sustain

Consumer Goods	Sharekhan code: ASIANPAINT
Reco/View: Buy ↔	CMP: **Rs. 3,084**
	Price Target: **Rs. 3,689** ↔

↑ Upgrade ↔ Maintain ↓ Downgrade

Summary

- Asian Paints Ltd's (APL's) Q4 results were largely in line with expectations with an 8% rise in volumes of the decorative paints business and consolidated OPM of 18.3%. Revenue & PAT grew by 18% and 10% y-o-y, respectively.
- For FY22, decorative paint volumes grew by 31%. With strong demand in Tier-1 & 2 towns, the management is confident of achieving double-digit volume growth in FY2023 (February, March and April 2022 saw double-digit volume growth).
- Though volatile raw material prices will keep margins stressed in the near term, the management is confident of achieving OPM of 18-20% once raw material inflation stabilises while planned initiatives and better mix will support the profitability in the medium term.
- The stock trades at 72x/55x its FY2023E/34E EPS. We maintain a Buy on the stock with an unchanged PT of Rs. 3,689.

In Q4FY2022, Asian Paints Ltd's (APL's) consolidated revenues grew by 19% to Rs. 7,892.7 crore driven by an 8% rise in volumes (two-year CAGR of 26%) in domestic decorative paints business while realisation growth stood at 12% during the quarter. Raw material inflation on y-o-y basis stood at 26%, reducing the gross margins by 448 bps y-o-y to 38.7% (same improved by 195 bps q-o-q as inflation remained stable) and OPM decreased by 153 bps y-o-y to 18.3% (remained stable compared to 18.1% in Q3). PAT grew by 10.3% y-o-y to Rs. 959.7 crore. The third wave of COVID-19 led to a short blip in January sales while February, March and April saw strong double-digit volume growth. In FY2022 consolidated revenues grew by 34% y-o-y (with decorative volume growth at 31%), while adjusted PAT grew by 11% (led by a 586 bps decline in the OPM).

Key positives

- February-March 2022 saw strong double-digit volume growth resulting 8% volume growth in Q4FY022 (on a high base of 48% volume growth).
- Kitchen business saw third consecutive quarter of Rs. 100+ crore revenues while Bath business delivered second consecutive quarter of Rs. 100+ crore revenues; losses of kitchen business reduced significant on y-o-y basis.
- Industrial business PPG-AP and AP-PPG registered double-digit revenue growth of 16% and 28% respectively on back of good recovery in the auto sector and industrial coatings segment.

Key negatives

- International business' operating margins was profitability significantly impacted by the steep material inflation & currency devaluations in Sri Lanka, Ethiopia and Egypt resulting in 56% decline in IB PBT.

Management Commentary

- January retail sales were affected by third COVID-19 wave. However strong recovery was witnessed in February, which result in high double digit volume growth in the rest of the quarter. T1/T2 towns saw double-digit growth (especially in luxury and premium range). Tier-3/Tier-4 towns saw some effect of inflation with cut on consumption/downtrading to low price products was seen in mass-end categories. The company posted double-digit growth in March-April 2022 and expect momentum to sustain in the coming months.
- Waterproofing products, construction chemicals and project business will continue to witness strong traction from real-estate sector, government projects and housing society projects in the medium term. The fourth consecutive year of a normal monsoon and stable inflationary environment might help recovery in the rural demand. Thus, management is confident of achieving double digit growth in FY2022 despite 31% volume growth (3-year CAGR of 18%).
- Recent acquisitions, expansion of retail reach and sustain growth in kitchen/bath business will help home décor business revenue contribution to reach to 10% by FY2025/26 from current 4%.
- Raw material inflation stood at 32-33%, while the company implemented price increase of 24-25% in FY2022. It expects additional inflation of ~5% in Q1FY2023 and has undertaken a minor price hike of 2%. Thus, gross margin pressures are expected to sustain in the medium term. The company is banking on planned initiatives (of differentiated formulations and cost efficiencies) along with better mix to achieve margins of 18-20% in the medium term.

Revision in estimates – We have broadly maintained our earnings estimates for FY2023 and FY2024 and keenly monitor the input price momentum and demand in the key markets in the coming months to make any revision in the earnings estimates.

Our Call

View: Maintain Buy with an unchanged PT of Rs. 3,689: APL's dominant positioning in the domestic decorative paints business and focus on becoming complete home décor play in the long run gives us a visibility of better earnings growth in the medium term. Market share gains, distribution expansion and sustained new product additions will help the company achieve volume growth better than peers in the medium term. With the company focusing on becoming a complete home décor play (contributing 10% of revenues by FY2026), its valuation will continue to remain premium in the consumer space. The stock trades at 71.8x and 54.9x its FY2023E and FY2024E EPS. We maintain our Buy rating on the stock with an unchanged price target of Rs. 3,689.

Key Risks

Sustained high inflationary pressure putting pressure on sales volume in Tier2/4 market and volatile input prices would act as a key risk to our earnings estimates.

Valuation (Consolidated) Rs cr

Particulars	FY21	FY22	FY23E	FY24E
Revenue	21,713	29,101	33,896	38,827
OPM (%)	22.4	16.5	17.8	19.8
Adjusted PAT	3,207	3,170	4,122	5,387
% YoY growth	*15.4*	*-1.2*	*30.0*	*30.7*
Adjusted EPS (Rs.)	33.4	33.1	43.0	56.2
P/E (x)	92.2	93.3	71.8	54.9
P/B (x)	23.1	21.4	18.7	15.5
EV/EBITDA (x)	56.8	56.8	45.6	35.9
RoNW (%)	28.0	23.8	27.8	30.8
RoCE (%)	22.4	19.5	22.5	25.2

Source: Company; Sharekhan estimates

Consolidated revenue grew by 19% y-o-y; OPM remained stable sequentially

Q4FY2022 revenues grew by 18.7% y-o-y to Rs. 7,892.7 crore. The domestic decorative paints business grew by 20% y-o-y with an 8% volume growth, in-line with our as well as street expectation of 6-8% for the quarter. Price-led growth stood at ~12%. Home improvement segment recorded yet another strong quarter, with revenues growing by 4% y-o-y to Rs. 232.4 crore (doubled as compared to Q4FY2020 revenues). The International Business delivered a double-digit revenue growth of 12%yoy despite severe challenges in key markets. The industrial coatings and automotive paints business closed the quarter with another round of robust double-digit revenue growth. Higher input prices led to 448 bps y-o-y decline in gross margins to 38.7% (up 195 bps q-o-q). Consolidated OPM decreased by 153 bps y-o-y to 18.3% (yet stood stable sequentially). The operating profit decreased by 9.5% y-o-y to Rs. 1,443.3 crore. Adjusted PAT grew by 10.3% y-o-y to Rs. 959.7 crore.

Standalone revenue grew by 19% y-o-y; PAT grew by 14% y-o-y

Standalone revenue grew by 19% y-o-y to Rs. 6,759.6 crore. Domestic decorative business registered 20% y-o-y growth, while home improvement business grew by 17% y-o-y to Rs. 109 crore. Higher input cost led to 752bps/605 bps y-o-y decline in gross margins/OPM to 38.0%/20.0%. Operating profit grew by 11.5% to Rs. 1,362.7 crore and PAT 14.7% y-o-y to Rs. 939.7 crore..

Key highlights of the quarter

- **Domestic decorative business volume growth momentum continued:** The domestic decorative business reported an 8% volume growth and 21% value growth in Q4FY2022 with two-year volume/value CAGR at 26%/32%, respectively. Tier-1/Tier-2 cities reported higher volume growth than Tier 3/Tier 4 towns. Tier-1/Tier-2 towns saw high double-digit volume growth with premium and luxury range registering strong traction. On the other hand, Tier-3/Tier-4 town saw double digit growth in the economy range. The company witnessed some slowdown at the lower end of the category due to high inflation. In terms of regions, highest growth was seen in the Western & Eastern regions. The project/ institutional business reported strong growth with greater traction across segments – building construction, government projects, factories and co-operative housing societies in T1/T2/T3. Waterproofing/wood finish category is gaining strong traction and growing strongly q-o-q.
- **Home improvement business gaining traction:** The home improvement business' revenues grew by 4% y-o-y with the kitchen business revenues growing by 34% y-o-y to Rs. 128 crore and bath business growing by 17% y-o-y to Rs. 109 crore. Strong growth in the kitchen business was driven by strong performance in full kitchen solutions and components business. APL continues to focus on its new propositions in the high-end range. For FY2022, the kitchen business registered revenues of Rs. 410 crore, while losses at PBT level reduced to Rs. 9 crore in FY2022 from a loss of Rs. 21 crore in FY2021. Bath business registered revenues of Rs. 360 crore in FY2022 with PBT of Rs. 4 crore. Both the kitchen and bath businesses are expected to maintain good growth momentum in the coming years with improvement in profitability due to improvement in scale of the business.
- **International business revenues grew by 12%; profitability hit by rise in raw material prices & currency devaluation:** International business reported revenue growth of 12% to Rs. 818 crore. Asia, Middle East and South Pacific reported strong growth of 18%, 8% and 10% y-o-y to Rs. 442 crore, Rs. 197 crore and Rs. 32 crore, respectively. High inflation and regional disturbances continued to hurt market conditions in Africa, which reported flat sales during the quarter. Profitability was impacted substantially due to input cost inflation, currency devaluations in Sri Lanka, Ethiopia and Egypt. The international business' PBT stood at Rs. 15 crore in Q4FY2022 versus Rs. 34 crore in Q4FY2021.
- **Industrial paints business improving:** PPG Asian Paints (AP) business registered good recovery with revenue growth of 19% yoy to Rs. 396 crore despite challenges faced by auto industry. The company is giving a strong push for implementing price increases across its B2B customers. Asian Paints (AP) PPG business continued to perform well led by growth in protective coatings segment registering strong y-o-y growth of 28% to Rs. 247 crore. Collaboration with Decorative project team lead to strong performance in Floor coating. Efficiency measures and cost-control activities limited the impact on the gross margins. PBT of PPG AP and AP PPG grew by 56% and 83% respectively.

Key conference call highlights

- **Management confident of achieving double-digit volume growth in FY2023:** January retail sales were affected by third COVID-19 wave. However strong recovery was witnessed in February, which result in high double-digit volume growth in the rest of the quarter. T1/T2 towns saw double-digit growth (especially in the luxury and premium range). T3/T4 towns saw some impact of inflation with cut on consumption/ downtrading to low-priced products was seen in mass end categories. The company posted double-digit growth in March April 2022 and expect the momentum to sustain in the coming months. Waterproofing products, construction chemicals and project business will continue to witness strong traction from real estate sector, government projects and housing society projects in the medium term. A fourth consecutive year of normal monsoon and expectation of a stable inflationary environment might help a recovery in the rural demand. Thus management is confident of achieving double digit growth in FY2022 despite 31% volume growth (3-year CAGR of 18%).
- **Strong growth in the project business & waterproofing segment:** The project business reported strong growth, outgrowing retail business growth. Waterproofing/wood finish segment reported strong double digit growth which aided growth in the projects business. Waterproofing segment is expected to grow at a strong rate much higher than other segments in 5-7 years.
- **Network expansion continued:** APL has continuously expanded its Rurban footprint by entering into big cities, suburbs and Tier-3/4 towns. It added more than 15,000 retail points taking the company's presence across 1,45,000 retail footprints.
- **Focus remains on increasing per-capita consumption:** APL is focusing on increasing the per-capita consumption by introducing new and innovative products, which will enhance the market as well. It introduced products such as Wood Polish Market – Glow Max, Super Economy Emulsions – Tractor/Ace Sparc Range and introduced new categories such as hygiene paints, fire retardant paints/floor-paints, which will help the company to achieve sustained increase in the paint consumption and gain market share in the medium term.
- **Home décor business to scale up with new acquisitions:** APL is focusing on become a unique player in the home décor space which operates in the e-commerce, physical and service space with value-for-money preposition with all categories being owned/manufactured by the brand. The company is expanding the retail reach of the business to 75 home décor stores by end of FY2023 from current 29 stores. The company is coming up with new factory for Kitchen and bath in Maharashtra in FY2023. It did green field expansion in designer tiles/wardrobe and vanities in FY2021-22. APL acquisition of White Teak and Weatherseal are done in line with its focus of transforming itself from company focusing on 'share of surface' to 'share of space' in the long run. APL targets revenue contribution from home décor business to increase to 10% from current 4%.
- **Raw material inflation to rise further:** Raw material inflation stood at 32-33%, while the company implemented price increase of 24-25% in FY2022. It expects additional inflation of ~5% in Q1FY2023 and has undertaken small price increase of 2%. Thus, gross margin pressures are expected to sustain in the medium term. The company is banking on planned initiatives (of differentiated formulations & cost efficiencies) along with better mix to achieve margins of 18-20% in the medium term.
- **Exceptional loss of Rs. 115 crore in Q4:** A delay in receipt of subsidy amounts from the State governments, an expense of Rs. 53.7 crore recognized as Exceptional Item, towards time value of money computed under 'expected credit loss' method based on reassessment of expected timing of cash inflows for subsidy income. In addition, subsidy income disclosed under Operating income for Q4 FY21-22 and FY21-22 lower by Rs. 31.1 crore to recognise the impact of reassessment of expected timing of cash inflows for the subsidy income accrued in FY2021-22. The current economic crisis in Sri Lanka has led to sharp currency devaluation, resulting in recognition of an expense of Rs. 48.5 crore towards exchange loss on foreign currency obligation of Causeway Paints (investment made in Sri Lanka).

Results (Consolidated) Rs cr

Particulars	Q4FY22	Q4FY21	Y-o-Y %	Q3FY22	Q-o-Q %
Total Revenue	**7,892.7**	**6,651.4**	**18.7**	**8,527.2**	**-7.4**
Raw Material Cost	4,838.1	3,779.3	28.0	5,393.3	-10.3
Employee Cost	457.4	412.1	11.0	455.7	0.4
Other Expenses	1,154.0	1,141.7	1.1	1,135.9	1.6
Total Operating Cost	6,449.4	5,333.2	20.9	6,984.9	-7.7
Operating Profit	**1,443.3**	**1,318.3**	**9.5**	**1,542.3**	**-6.4**
Other Income	80.4	75.4	6.6	71.8	11.9
Interest & Other Financial Cost	22.6	29.9	-24.2	27.5	-17.6
Depreciation	205.1	213.4	-3.9	207.9	-1.3
Profit Before Tax	**1,296.0**	**1,150.5**	**12.6**	**1,378.8**	**-6.0**
Tax Expense	345.2	286.4	20.5	362.4	-4.8
Adjusted PAT	950.7	864.0	10.0	1,016.3	-6.5
Share of profit from associates	8.9	5.9	52.6	15.0	-40.3
Adjusted PAT after MI	**959.7**	**869.9**	**10.3**	**1,031.3**	**-6.9**
Exceptional Items	85.62	0.00	-	0.00	-
Reported PAT	874.1	869.9	0.5	1031.3	-15.3
Adj. EPS (Rs)	10.0	9.1	10.3	10.8	-6.9
			BPS		**BPS**
GPM (%)	38.7	43.2	-448	36.8	195
OPM (%)	18.3	19.8	-153	18.1	20
NPM (%)	11.1	13.1	-200	12.1	-102
Tax rate (%)	26.6	24.9	174	26.3	35

Source: Company; Sharekhan Research

Results (standalone) Rs cr

Particulars	Q4FY22	Q4FY21	Y-o-Y %	Q3FY22	Q-o-Q %
Total Revenue	6759.6	5670.8	19.2	7491.1	-9.8
Operating Profit	1362.7	1222.4	11.5	1468.2	-7.2
Profit Before Tax	1256.3	1103.5	13.8	1367.4	-8.1
Tax Expense	316.5	283.9	11.5	347.2	-8.8
Adjusted PAT before MI	939.7	819.6	14.7	1020.3	-7.9
Exceptional Items	39.8	0.0	-	0.0	-
Reported PAT	900.0	819.6	9.8	1020.3	-11.8
Adj. EPS (Rs)	9.8	8.5	14.7	10.6	-7.9
			BPS		**BPS**
GPM (%)	39.7	44.7	-500	37.5	221
OPM (%)	20.2	21.6	-140	19.6	56

Source: Company; Sharekhan Research

Outlook and Valuation

■ Sector outlook – Structural growth of the paint industry is intact

The Indian paints industry reported an 11% CAGR or FY2011-FY2019 and stood at Rs. 545 billion. The decorative paint segment constitutes around 74% of total paint sales, resulting in the paint sector growing at a robust rate even at the time of an industrial slowdown. April and May (that constitute ~25% of total per annum sales) are two key months for re-painting activities in the domestic market. FY2021 was affected by the pandemic, led by lockdown, resulting in almost no business in Q1FY2021. Volatile input prices and a slowdown in the rural India are near-term headwinds for paint industry. The decorative paint industry is expected to post a 13% CAGR over FY2019-FY2024, led by reduction in the repainting cycle to 4-5 years (from 8-10 years earlier), acceptance for better paint products in smaller towns, and upgradation of premium brands in cities and large towns. Higher input prices will keep toll margins of the paint companies in the near term.

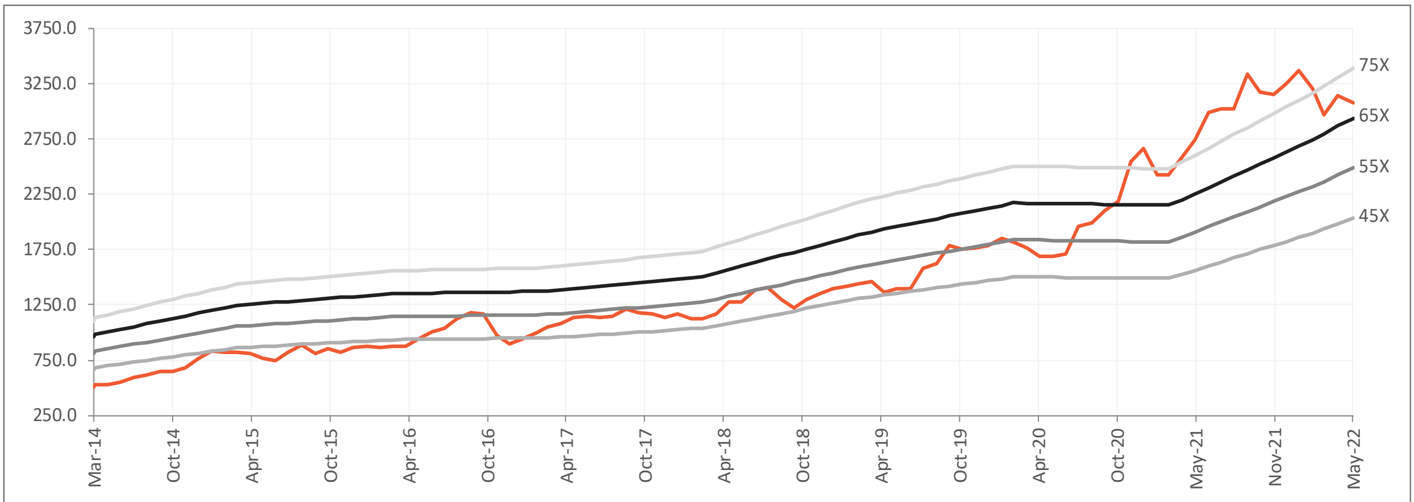
■ Company outlook – Volume growth momentum to sustain; margins to improve as input costs stabilise

Revenues grew by 36% in FY2022 with volume growth standing at 31% in the decorative paints business (two-year CAGR of 20%+). OPM decreased to 16.5% led by sharp increase in the input prices during the year. Waterproofing products, Construction chemicals and the project business will continue to witness strong traction from real-estate sector, government projects and housing society projects in the medium term. The company targets double digit volume growth in the near term. Price increase will help the revenue growth to remain in high double digits. Volatile crude prices will keep margins under pressure in the near term. The company has undertaken 25-27% price hike in the portfolio and might take calibrated price increase if required in the coming months. APL targets OPM of 18-20% in the medium term.

■ Valuation – Maintain Buy with an unchanged PT of Rs. 3,689:

APL's dominant positioning in the domestic decorative paints business and focus on becoming complete home décor play in the long run gives us a visibility of better earnings growth in the medium term. Market share gains, distribution expansion and sustained new product additions will help the company achieve volume growth better than peers in the medium term. With the company focusing on becoming a complete home décor play (contributing 10% of revenues by FY2026), its valuation will continue to remain premium in the consumer space. The stock trades at 71.8x and 54.9x its FY2023E and FY2024E EPS. We maintain our Buy rating on the stock with an unchanged price target of Rs. 3,689.

One-year forward P/E (x) band



Source: Sharekhan Research

Peer Comparison

Particulars	P/E (x)			EV/EBIDTA (x)			RoCE (%)		
	FY22	FY23E	FY24E	FY22	FY23E	FY24E	FY22	FY23E	FY24E
Berger Paints	75.1	59.8	49.4	47.1	39.4	24.4	25.8	28.1	28.9
Indigo Paints	70.4	41.0	28.5	46.9	27.1	18.8	20.7	29.4	33.3
Asian Paints	93.3	71.8	54.9	56.8	45.6	35.9	19.5	22.5	25.2

Source: Company, Sharekhan estimates

About company

APL is the largest paint company in India with market leadership of over 50 years and stands among the top 10 paint companies in the world. The company has 26 paint manufacturing plants in 15 countries, serving customers in over 60 countries globally. The company offers paints – decorative and industrial, wall coverings, and waterproofing along with kitchen and bath fittings, adhesives, and services. Deco India, including decorative paints, water proofing, wall coverings, and adhesives, constitutes almost 84% to the company's total revenue, whereas the industrial coatings space, including automotive and non-automotive, constitutes only 2%, through two 50:50 joint ventures with PPG industries Inc., USA (AP-PPG). The international business contributes ~12% to the total revenue mainly dominated by Nepal, Sri Lanka, and Bahrain. A small portion is contributed by kitchen and bath fittings through its subsidiary, Sleek International Pvt. Ltd. (Sleek Kitchens) and Ess Ess Bath Fittings.

Investment theme

The rising middle-income group, fast urbanisation, shift from the unorganised to organised space, and improving penetration in rural markets are some of the key revenue drivers for paint companies in the near to medium term. APL, with a leadership position in the decorative paint business and strong brand portfolio, will continue to deliver good earnings growth in the near term. APL is expected to benefit from its recent capacity expansion, vast distribution network, product innovation, and growth in its premium products.

Key Risks

- **Increased raw-material prices:** Any significant increase in crude prices and other input costs will affect the company's profitability.
- **Slowdown in economic growth:** Any slowdown in economic growth will affect repainting demand, which constitutes almost 70% of the total paint demand.
- **Slowdown in the auto industry:** Further sluggishness in demand in the auto industry or slowdown in infrastructure development will affect the industrial coatings segment.

Additional Data

Key management personnel

Deepak Satwalekar	Chairman
Amit Syngle	Managing Director and CEO
R J Jeyamurugan	CFO and Company Secretary

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Teesta Retail Pvt Ltd	4.90
2	Life Insurance Corp of India	1.85
3	Blackrock Inc	1.67
4	Vanguard Group Inc	1.57
5	Capital Group Companies	1.31
6	SBI Funds Management	1.30
7	JP Morgan and Chase	0.61
8	UTI Asset Management Co Ltd	0.57
9	St James Place PLC	0.54
10	Axis Asset Management Co Ltd	0.36

Source: Bloomberg

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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

Sharekhan

by BNP PARIBAS

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