

BSE SENSEX 31,449 S&P CNX 9,794

CMP: INR259 TP: INR298 (+15%) Buy

Motilal Oswal values your support in the Asiamoney Brokers Poll 2017 for India Research, Sales and Trading team. We request your ballot.



Bloomberg	SHKL IN
Equity Shares (m)	145
M.Cap.(INRb)/(USD b)	36.4 / 0.6
52-Week Range (INR)	362 / 245
1, 6, 12 Rel. Per (%)	0/-29/-12
Avg. Val, INRm	60
Free float (%)	42.6

Financials & Valuations (INR b)

Y/E Mar	2017	2018E	2019E
Net Sales	10.6	11.2	13.2
EBITDA	1.7	1.7	2.2
PAT	1.0	1.1	1.4
EPS (INR)	7.2	7.6	9.9
Gr. (%)	43.5	4.9	30.5
BV/Sh (INR)	56.1	61.5	68.6
RoE (%)	13.7	12.9	15.2
RoCE (%)	19.0	18.9	22.8
P/E (x)	35.7	34.1	26.1
P/BV (x)	4.6	4.2	3.8

Estimate change 

TP change 

Rating change 

Subdued performance; recovery expected in 2HFY18

GST-led cautiousness halts growth: SHKL's overall revenue declined 8.6% YoY to INR2,529m (est. of INR2,629m) in 1QFY18, driven by de-growth in the Fragrance business (-8.6% YoY to INR2,187m). EBTDA margin contracted marginally by 20bp YoY to 16.9% (est. of 17.5%), as expansion in gross margin (+290bp YoY to 51.7%) was partly offset by higher other expenses (+190bp). EBITDA declined 10% YoY to INR427m (est. of INR460m). Consequently, adj. PAT fell marginally by 2.5% to INR268m (est. of INR263m).

Fragrance division to recover post subdued performance: Fragrance business, which contributed 87% of total revenues, reported de-growth of 8.6% YoY (on account of lower offtake in the FMCG sector due to GST rollout), leading to a decline of 12% YoY in domestic revenues. 1QFY18 also witnessed a decline of ~45% YoY in service income to INR88m. However, the industry is expected to witness recovery in consumer demand, the impact of which is expected to be seen from 3QFY18. The recovery in domestic demand, coupled with steady growth in the overseas market, is expected to augur well for the business.

Cost-saving measures to boost profitability: 1QFY18 witnessed a sharp increase of 290bp YoY in gross margin on account of the company's continuous efforts to optimize cost. The company is further expected to invest INR500-600m to evaluate and improve current processes, which is expected to yield cost savings of ~EUR2m. In view of optimizing costs, the company is expected to continue optimizing operations in Netherlands, while simultaneously evaluating a shift to a lower-cost site over the next 12-15 months.

Valuation and view: We believe the company will revive from the transitional effect of GST and get back on the growth track. However, the impact of cost-cutting measures and recovery post GST will not be witnessed before 2HFY18. Hence, we cut our earnings estimates by 8%/4% for FY18/FY19, and expect SHK to post revenue and PAT CAGR of 12% and 17%, respectively, over FY17-19E. We maintain **Buy** with a target price of INR298 (30x FY19E EPS).

Consolidated - Quarterly Earning Model

Y/E March	FY17				FY18				FY17	FY18E	FY18	Var (%)
	1Q	2Q	3Q	4Q	1Q	2QE	3QE	4QE	10,421	11,198	2,629	
Net Sales	2,768	2,636	2,319	2,698	2,529	2,900	2,667	3,102	10,421	11,198	2,629	-4
YoY Change (%)	25.2	18.0	-5.3	-6.5	-8.6	10.0	15.0	15.0	6.6	7.5	2.8	
Total Expenditure	2,294	2,220	2,101	2,328	2,102	2,387	2,349	2,625	8,766	8,620	2,169	
EBITDA	474	416	218	370	427	513	317	478	1,655	2,578	460	-7
Margins (%)	17.1	15.8	9.4	13.7	16.9	17.7	11.9	15.4	15.9	23.0	17.5	
Depreciation	44	49	48	53	58	50	51	60	194	219	65	
Interest	17	22	2	10	6	6	3	6	51	21	11	
Other Income	32	29	19	40	38	33	25	44	119	140	37	
PBT before EO expense	444	375	186	346	401	490	288	456	1,529	2,477	421	-5
Extra-Ord expense	0	0	0	0	0	0	0	0	0	0	0	
PBT	444	375	186	346	401	490	288	456	1,529	2,477	421	-5
Tax	169	132	110	71	133	164	97	150	482	544	158	
Rate (%)	38.1	35.1	59.0	20.7	33.1	33.4	33.6	33.0	31.5	21.9	37.6	
Minority Interest & Profit/Loss of Asso.	0	0	0	0	0	0	0	0	0	0	0	
Reported PAT	275	243	76	274	268	327	191	305	1,047	1,934	263	2
Adj PAT	275	243	76	274	268	327	191	305	1,047	1,934	263	2
YoY Change (%)	41.0	246.0	-65.0	12.5	-2.5	34.4	150.6	11.3	43.9	84.8	-4.6	
Margins (%)	9.9	9.2	3.3	10.2	10.6	11.3	7.2	9.8	10.0	17.3	10.0	

E: MOSL Estimates

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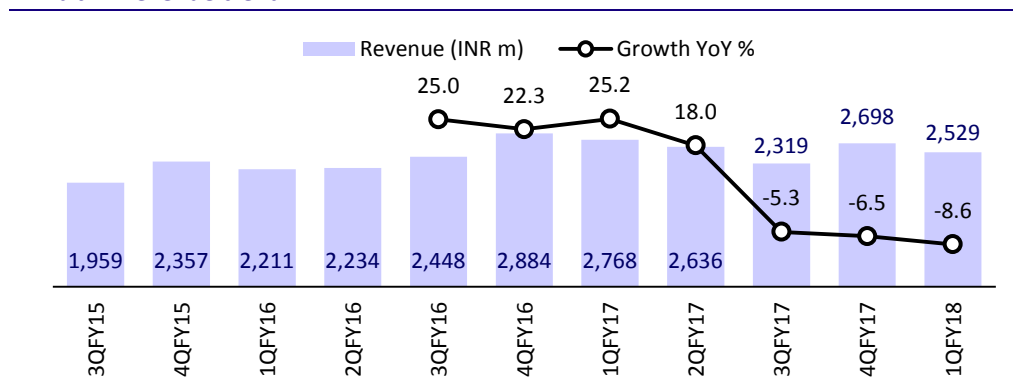
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Revenue, EBITDA miss estimates; PAT in-line

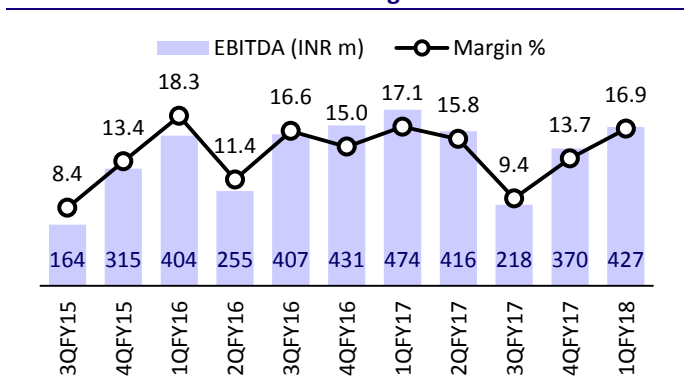
- SHKL’s overall revenue decline 8.6% YoY to INR2,529m (est. of INR2,629m) in 1QFY18, on account of de-growth in the Fragrance (-8.6% YoY to INR2,187m) and Flavor (-8.4% YoY to INR332m) businesses.
- EBTDA margin contracted marginally by 20bp YoY to 16.9% (est. of 17.5%) as the increase in gross margin (+290bp YoY to 51.7%) was partly offset by higher other expenses (+190bp). EBITDA declined 10% YoY to INR427m (est. of INR460m).
- PBIT margin for Fragrance stood at 16.7% (v/s 14.6% in 1QFY17) and Flavors at 18.9% (v/s 28.7% in 1QFY17).
- Consequently, adj. PAT declined marginally by 2.5% to INR268m (est. of INR263m).

Exhibit 1: Revenue trend



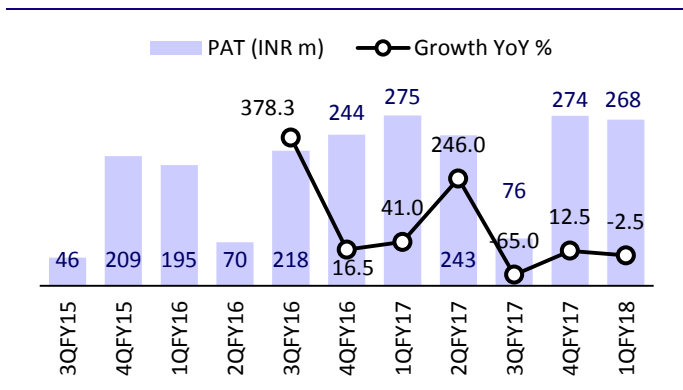
Source: MOSL, Company

Exhibit 2: EBITDA and EBITDA margin trend



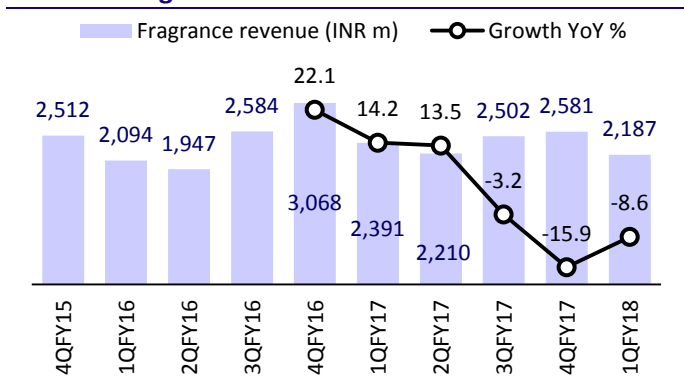
Source: MOSL, Company

Exhibit 3: PAT trend



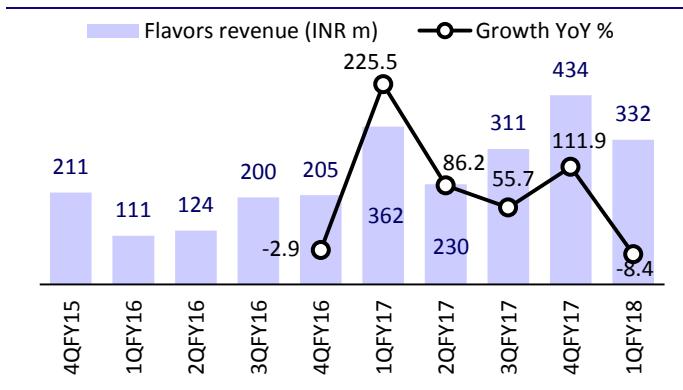
Source: MOSL, Company

Exhibit 4: Fragrance revenue trend



Source: MOSL, Company

Exhibit 5: Flavor revenue trend



Source: MOSL, Company

Exhibit 6: Fragrance PBIT margin trend

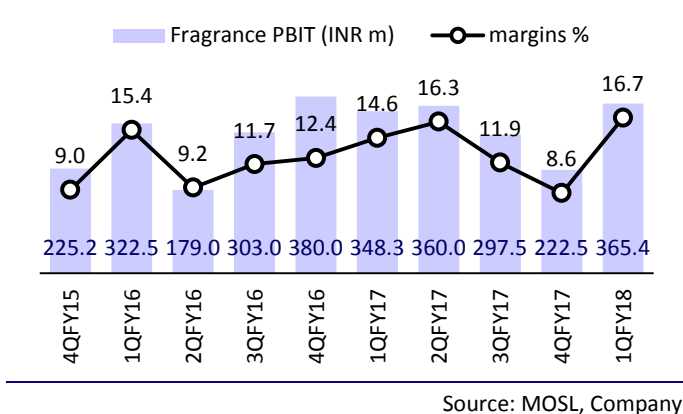


Exhibit 7: Flavor PBIT margin trend

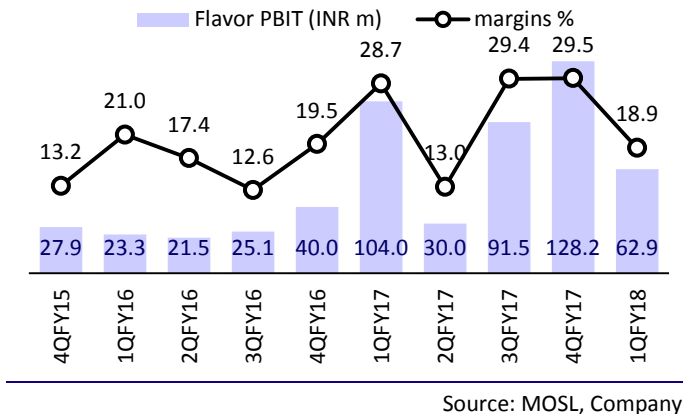
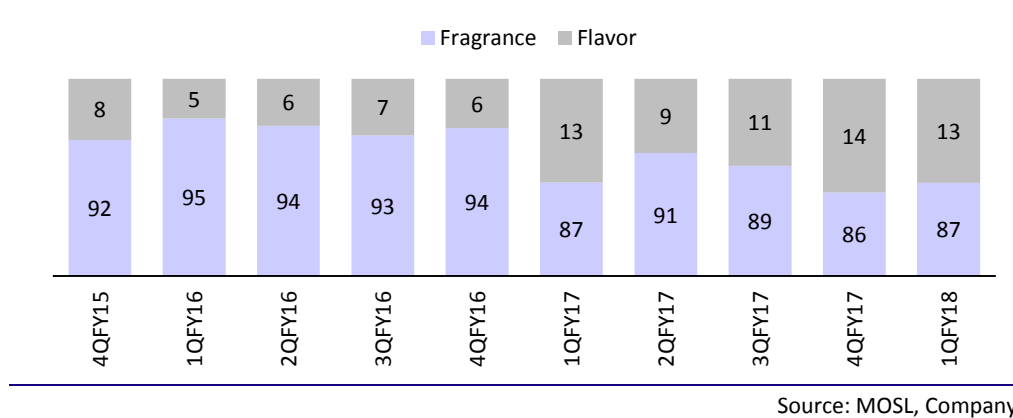


Exhibit 8: Revenue mix



Valuation and view

We believe the company will revive from transitional effect of GST and get back on the track of growth. However, the impact of cost cutting measures and recovery post GST will not be witnessed before 2HFY18. Hence, we cut our earnings estimates by 8%/4% for FY18/FY19 and expect SHK to post revenue and PAT CAGR of 12% and 17% over FY17-19E. We maintain Buy with a target price of INR298 (30x FY19E EPS).

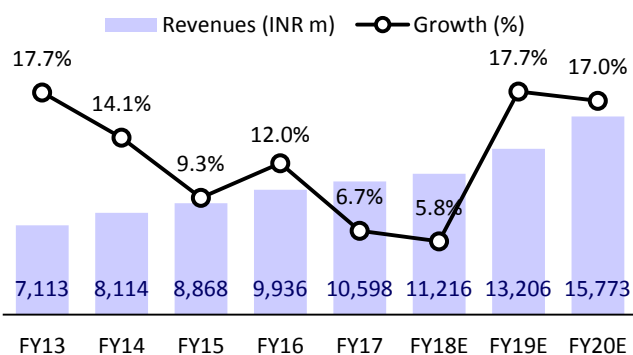
Exhibit 9: Assumptions

Assumptions	FY13	FY14	FY15	FY16	FY17	FY18E	FY19E
Fragrance (INR m)	6,285	7,204	7,763	8,642	8,568	9,385	10,787
Growth %		14.6	7.8	11.3	-0.9	9.5	14.9
Flavour (INR m)	366	410	607	587	1,244	1,831	2,419
Growth %		11.8	48.2	-3.3	112	47.2	32.1

Source: Company, MOSL

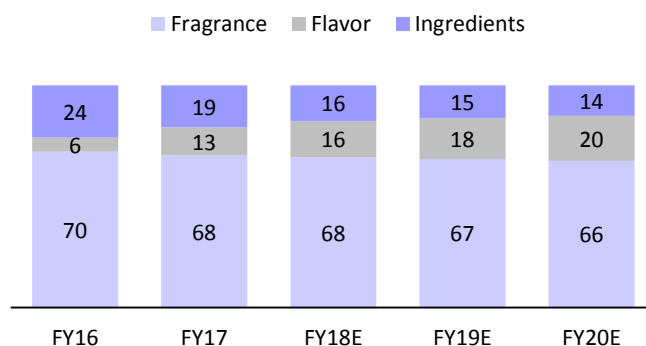
Story in charts

Exhibit 10: Revenue to post 12% CAGR over FY17-19E



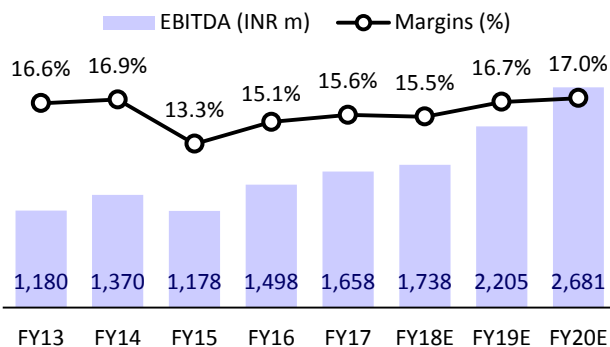
Source: MOSL, Company

Exhibit 11: Contribution of Flavor to increase



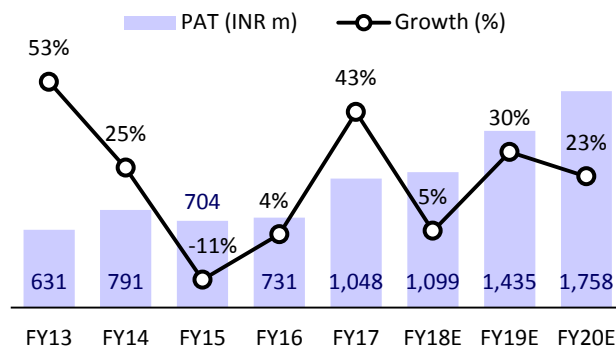
Source: MOSL, Company

Exhibit 12: EBITDA margins on uptrend



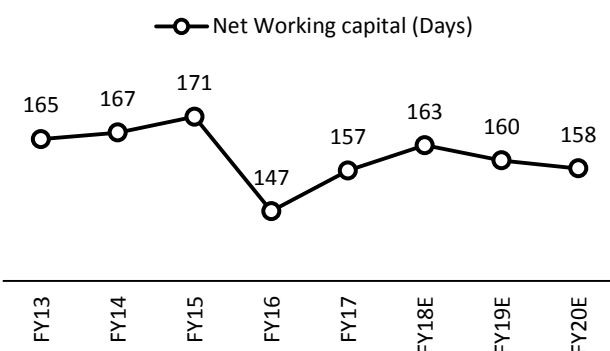
Source: MOSL, Company

Exhibit 13: PAT to record a CAGR of 17% over FY17-19E



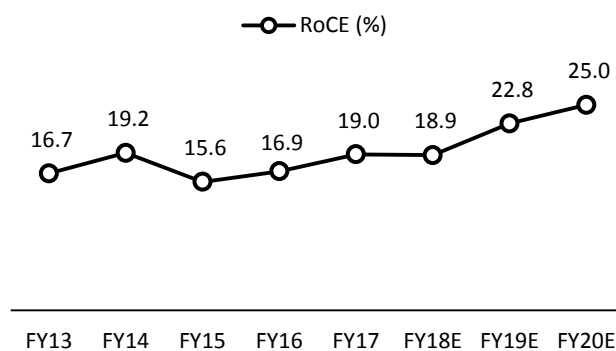
Source: MOSL, Company

Exhibit 14: Working capital days to gradually improve



Source: MOSL, Company

Exhibit 15: RoCE to improve to 25% by FY20E



Source: MOSL, Company

Financials and Valuations

Consolidated - Income Statement								(INR Million)
Y/E March	FY13	FY14	FY15	FY16	FY17	FY18E	FY19E	FY20E
Total Income from Operations	7,113	8,114	8,868	9,936	10,598	11,216	13,206	15,773
Change (%)	17.7	14.1	9.3	12.0	6.7	5.8	17.7	19.4
EBITDA	1,180	1,370	1,178	1,498	1,658	1,738	2,205	2,681
Margin (%)	16.6	16.9	13.3	15.1	15.6	15.5	16.7	17.0
Depreciation	173	188	293	297	194	211	232	251
EBIT	1,007	1,183	885	1,201	1,464	1,528	1,973	2,430
Int. and Finance Charges	218	175	185	202	52	26	0	0
Other Income	15	78	246	105	116	140	168	193
PBT bef. EO Exp.	805	1,085	945	1,103	1,528	1,641	2,141	2,623
EO Items	-23	0	0	0	0	0	0	0
PBT after EO Exp.	782	1,085	945	1,103	1,528	1,641	2,141	2,623
Current Tax	250	328	286	446	459	541	707	866
Deferred Tax	-7	-33	-45	-74	20	0	0	0
Tax Rate (%)	31.0	27.1	25.5	33.8	31.4	33.0	33.0	33.0
Less: Minority Interest	-76	0	0	0	0	0	0	0
Reported PAT	616	791	704	731	1,048	1,099	1,435	1,758
Adjusted PAT	631	791	704	731	1,048	1,099	1,435	1,758
Change (%)	-16.6	25.3	-11.0	3.7	43.5	4.9	30.5	22.5
Margin (%)	8.9	9.8	7.9	7.4	9.9	9.8	10.9	11.1

Consolidated - Balance Sheet								(INR Million)
Y/E March	FY13	FY14	FY15	FY16	FY17	FY18E	FY19E	FY20E
Equity Share Capital	120	132	1,323	1,446	1,446	1,446	1,446	1,446
Total Reserves	4,077	4,669	3,682	5,714	6,671	7,453	8,473	9,722
Net Worth	4,720	4,810	5,097	7,161	8,117	8,899	9,919	11,169
Deferred Tax Liabilities	6	-19	-50	57	73	73	73	73
Total Loans	1,518	2,111	2,427	732	624	0	0	-123
Capital Employed	6,244	6,902	7,474	7,949	8,814	8,972	9,992	11,119
Gross Block	3,655	4,233	4,573	4,976	5,860	6,195	6,702	7,243
Less: Accum. Deprn.	2,259	2,548	2,612	2,909	3,103	3,314	3,546	3,797
Net Fixed Assets	1,395	1,686	1,961	2,068	2,757	2,881	3,156	3,446
Goodwill on Consolidation	707	828	776	206	206	206	206	206
Capital WIP	432	503	105	181	75	290	333	342
Total Investments	410	2	0	354	497	497	497	497
Curr. Assets, Loans&Adv.	4,760	5,573	6,502	7,363	7,351	7,893	9,122	10,581
Inventory	2,254	2,788	3,175	3,352	3,502	4,051	4,641	5,452
Account Receivables	1,719	1,794	1,945	2,288	2,170	2,297	2,704	3,230
Cash and Bank Balance	332	415	759	822	555	356	376	225
Loans and Advances	456	576	622	901	1,124	1,190	1,401	1,673
Curr. Liability & Prov.	1,461	1,689	1,870	2,223	2,072	2,795	3,322	3,952
Account Payables	757	879	977	1,633	1,107	1,324	1,567	1,865
Other Current Liabilities	592	527	553	496	854	903	1,064	1,270
Provisions	112	283	340	93	111	568	691	817
Net Current Assets	3,299	3,885	4,632	5,141	5,279	5,098	5,800	6,628
Appl. of Funds	6,244	6,902	7,474	7,949	8,814	8,972	9,992	11,119

Financials and Valuations

Ratios

Y/E March	FY13	FY14	FY15	FY16	FY17	FY18E	FY19E	FY20E
Basic (INR)								
EPS	4.8	6.0	5.3	5.1	7.2	7.6	9.9	12.2
Cash EPS	5.9	7.4	7.5	7.1	8.6	9.1	11.5	13.9
BV/Share	35.7	36.4	38.5	49.5	56.1	61.5	68.6	77.2
DPS	0.6	1.1	1.1	1.5	1.7	1.8	2.4	2.9
Payout (%)	15.6	22.2	25.6	35.7	28.9	28.9	28.9	28.9
Valuation (x)								
P/E		43.3	48.6	51.3	35.7	34.1	26.1	21.3
Cash P/E		35.0	34.4	36.5	30.1	28.6	22.5	18.6
P/BV		7.1	6.7	5.2	4.6	4.2	3.8	3.4
EV/Sales		4.7	4.3	4.0	3.8	3.6	3.0	2.5
EV/EBITDA		26.2	30.5	24.9	22.6	21.3	16.8	13.8
Dividend Yield (%)	0.2	0.4	0.4	0.6	0.7	0.7	0.9	1.1
FCF per share	5.2	-0.5	3.0	4.3	1.5	4.4	1.8	2.0
Return Ratios (%)								
RoE	15.0	16.6	14.2	11.9	13.7	12.9	15.2	16.7
RoCE	16.7	19.2	15.6	16.9	19.0	18.9	22.8	25.0
Working Capital Ratios								
Asset Turnover (x)	1.1	1.2	1.2	1.2	1.2	1.3	1.3	1.4
Inventory (Days)	116	125	131	123	121	132	128	126
Debtor (Days)	88	81	80	84	75	75	75	75
Creditor (Days)	39	40	40	60	38	43	43	43
Leverage Ratio (x)								
Debt/Equity	0.3	0.4	0.5	0.1	0.1	0.0	0.0	0.0

Consolidated - Cash Flow Statement

(INR Million)

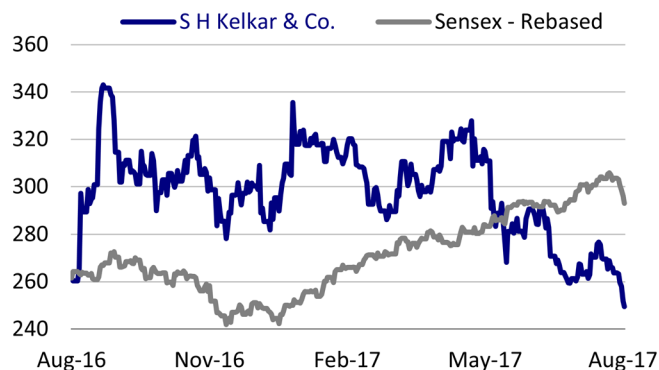
Y/E March	FY13	FY14	FY15	FY16	FY17	FY18E	FY19E	FY20E
OP/(Loss) before Tax	785	1,088	945	1,206	1,528	1,641	2,141	2,623
Depreciation	173	188	293	294	194	211	232	251
Interest & Finance Charges	201	146	175	130	-64	-113	-168	-193
Direct Taxes Paid	-259	-343	-285	-394	-480	-541	-707	-866
(Inc)/Dec in WC	103	-729	-375	-374	-406	-17	-682	-978
CF from Operations	1,005	350	753	863	772	1,180	816	838
Others	26	-29	-136	1	228	0	0	0
CF from Operating incl EO	1,031	321	617	864	1,001	1,180	816	838
(Inc)/Dec in FA	-344	-386	-219	-238	-778	-550	-550	-550
Free Cash Flow	687	-65	399	626	222	630	266	288
(Pur)/Sale of Investments	0	0	3	4	-143	0	0	0
Others	14	-211	17	-331	116	140	168	193
CF from Investments	-330	-597	-199	-565	-805	-410	-382	-357
Issue of Shares	10	0	-38	1,956	0	0	0	0
Inc/(Dec) in Debt	-259	527	322	-1,589	-108	-624	0	-123
Interest Paid	-210	-161	-183	-162	-52	-26	0	0
Dividend Paid	-114	0	-176	-441	-303	-318	-414	-508
Others	-34	-6	0	0	0	0	0	0
CF from Fin. Activity	-607	360	-75	-236	-463	-968	-414	-631
Inc/Dec of Cash	94	84	344	63	-268	-199	20	-150
Opening Balance	237	332	415	759	822	555	356	376
Closing Balance	332	415	759	822	555	356	376	225

Corporate profile

Company description

SH Kelkar (SHKL) is one of India's largest fragrance & flavor (F&F) companies with a market share of ~14% as of 2016. Its fragrance products are used as raw materials in personal & fabric care, skin & hair care, fine fragrance and household products, while flavor products are used in baked & dairy products, beverages and pharmaceuticals.

Exhibit 1: Sensex rebased



Source: MOSL/Bloomberg

Exhibit 2: Shareholding pattern (%)

	Jun-17	Mar-17	Jun-16
Promoter	57.4	57.0	56.7
DII	2.0	2.4	2.2
FII	21.5	17.4	14.1
Others	19.1	23.2	27.0

Note: FII Includes depository receipts

Source: Capitaline

Exhibit 3: Top holders

Holder Name	% Holding
Blackstone Capital Partners (Singapore) Vi Fdi Two Pte. Ltd.	10.0
T. Rowe Price International Discovery Fund	2.2
Prazim Trading And Investment Co. Pvt. Ltd.	1.5
Mondrian Emerging Markets Small Cap Equity Fund,L.P.	1.5
Smallcap World Fund, Inc	1.3

Source: Capitaline

Exhibit 4: Top management

Name	Designation
Ramesh Vinayak Vaze	Managing Director
Kedar Ramesh Vaze	Whole Time Director & CEO
Deepti Chandratre	Company Secretary

Source: Capitaline

Exhibit 5: Directors

Name	Name
Amit Dalmia	Amit Dixit
Prabha Ramesh Vaze	Alpana Parida
Dalip Sehgal	Jairaj Manohar Purandare
Nitin Potdar.	Sangeeta Singh

*Independent

Exhibit 6: Auditors

Name	Type
B S R & Co LLP	Statutory
B S R & Co LLP	Statutory

Source: Capitaline

Exhibit 7: MOSL forecast v/s consensus

EPS (INR)	MOSL forecast	Consensus forecast	Variation (%)
FY18	7.6	8.5	-10.9
FY19	9.9	10.3	-3.6
FY20	12.2	11.4	7.0

Source: Bloomberg

Disclosures:

The following Disclosures are being made in compliance with the SEBI Research Analyst Regulations 2014 (herein after referred to as the Regulations).

Motilal Oswal Securities Ltd. (MOSL) is a SEBI Registered Research Analyst having registration no. INH000000412. MOSL, the Research Entity (RE) as defined in the Regulations, is engaged in the business of providing Stock broking services, Investment Advisory Services, Depository participant services & distribution of various financial products. MOSL is a subsidiary company of Motilal Oswal Financial Service Ltd. (MOFSL). MOFSL is a listed public company, the details in respect of which are available on www.motilaloswal.com. MOSL is registered with the Securities & Exchange Board of India (SEBI) and is a registered Trading Member with National Stock Exchange of India Ltd. (NSE) and Bombay Stock Exchange Limited (BSE), Metropolitan Stock Exchange Of India Ltd. (MSE) for its stock broking activities & is Depository participant with Central Depository Services Limited (CDSL) & National Securities Depository Limited (NSDL) and is member of Association of Mutual Funds of India (AMFI) for distribution of financial products. Details of associate entities of Motilal Oswal Securities Limited are available on the website at <http://online-reports.motilaloswal.com/Dormant/documents/Associate%20Details.pdf>

Pending Regulatory Enquiries against Motilal Oswal Securities Limited by SEBI:

SEBI pursuant to a complaint from client Shri C.R. Mohanraj alleging unauthorized trading, issued a letter dated 29th April 2014 to MOSL notifying appointment of an Adjudicating Officer as per SEBI regulations to hold inquiry and adjudicate violation of SEBI Regulations; MOSL requested SEBI to provide all documents, records, investigation report relied upon by SEBI which were referred in Show Cause Notice and also sought personal hearing. The matter is currently pending.

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