

25 October 2020

Atul

Margins surprise, positive on growth; upgrading to a Buy

Atul's Q2 revenue/EBITDA/PAT recovered well, rising 52%/65%/48% q/q even as low demand from certain user industries tempered its y/y performance. We are upbeat on its future performance, considering its greater focus on retail and branded products, ongoing capex to support revenue growth coupled with strong performances across business verticals, subsidiaries, Associates and JVs. We upgrade our recommendation to a Buy, at a target of Rs7,500 (earlier Rs5,550), valuing the stock at 25x FY23e EPS.

Mixed segment performance. Atul's Q2 revenue was Rs10bn, down 4.2% y/y (but q/q up 51.7%) on the soft showing in Performance & Other chemicals. Life-science chemicals revenue grew 5.3% y/y, 28.3% q/q while that of Performance & Other chemicals slipped 7.7% y/y, though q/q up 64%. Ahead, we expect revenue to clock a 16.6% CAGR over FY21-23 supported by capex, greater utilisation of present capacities, rising share of its retail business, value-added and high-margin products.

The highest EBITDA margin. Q2 and H1 FY21 EBITDA margins were 26.1% and 25.3% respectively, up from 21.5% and 22.3% a year ago. The fall in raw-material prices, better realisations, a change in the product mix and operating efficiencies resulted in the margin expansion. Considering the current revival in Q2, the H1 performance and management's guidance at the AGM, we raise our EBITDA margin to 23.5% for FY21 and 24% for FY22.

Outlook, Valuation. Extension of existing products to complementary segments, greater acceptance of brand-named products and capacity expansions would drive growth. We expect sales/EBITDA/PAT to grow 17%/18%/16%. We roll forward our valuation to FY23 and assign a Buy rating with a higher target of Rs7,500, ascribing an implied multiple of 25x FY23e EPS and 15.4x FY23e EV/EBITDA. **Risks:** Drop in spreads of major products, delay in capex and debottlenecking implementation, erratic increase in crude and derivatives prices.

Key financials (YE Mar)	FY19	FY20	FY21e	FY22e	FY23e
Sales (Rs m)	40,378	40,931	41,593	49,296	56,545
Net profit (Rs m)	4,322	6,665	6,623	7,841	8,907
EPS (Rs)	145.6	224.5	223.2	264.2	300.1
PE (x)	42.0	27.2	27.4	23.2	20.4
EV / EBITDA (x)	23.4	19.5	17.8	14.6	12.4
PBV (x)	6.7	5.8	4.8	4.1	3.5
RoE (%)	16.0	21.1	17.7	17.7	17.0
RoCE (%)	16.4	21.3	18.0	18.1	17.6
Dividend yield (%)	0.2	0.4	0.4	0.5	0.6
Net debt / equity (x)	-	-	-	-	-

Source: Company, Anand Rathi Research

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Rating: **Buy**

Target Price: Rs7,500

Share Price: Rs6,118

Key data	ATLP IN / ATLP.BO
52-week high / low	Rs7021 / 2923
Sensex / Nifty	40686 / 11930
3-m average volume	\$4.9m
Market cap	Rs181bn / \$2465m
Shares outstanding	30m

Shareholding pattern (%)	Sep'20	Jun'20	Mar'20
Promoters	44.8	44.8	44.8
- of which, Pledged	5.3	3.8	3.8
Free float	55.2	55.2	55.2
- Foreign institutions	8.2	6.7	6.9
- Domestic institutions	23.4	25.3	24.5
- Public	23.6	23.2	23.8

Estimates revision (%)	FY21e	FY22e
Sales	(5.6)	(5.4)
EBITDA	0.8	3.2
EPS	(0.3)	2.4

Relative price performance



Source: Bloomberg

Nav Bhardwaj
Research AnalystBhawana Israni
Research Associate

Quick Glance – Financials and Valuations

Fig 1 – Income statement (Rs m)

Year-end: Mar	FY19	FY20	FY21e	FY22e	FY23e
Net revenues	40,378	40,931	41,593	49,296	56,545
Growth (%)	22.5	1.4	1.6	18.5	14.7
Direct costs	21,061	19,700	19,341	22,676	26,011
SG&A	11,650	12,210	12,478	14,789	16,963
EBITDA	7,668	9,020	9,774	11,831	13,571
EBITDA margins (%)	19.0	22.0	23.5	24.0	24.0
- Depreciation	1,189	1,302	1,717	2,310	2,778
Other income	349	780	832	986	1,131
Interest expenses	74	94	87	87	87
PBT	6,753	8,404	8,802	10,420	11,837
Effective tax rate (%)	36.2	20.8	25.0	25.0	25.0
+ Associates / (Minorities)	12	5	22	26	29
Net income	4,322	6,665	6,623	7,841	8,907
Adjusted income	4,322	6,665	6,623	7,841	8,907
WANS	30	29.7	30	30	30
FDEPS (₹ / sh)	145.6	224.5	223.2	264.2	300.1
FDEPS growth (%)	56.3	54.2	-0.6	18.4	13.6
Gross margins (%)	47.8	51.9	53.5	54.0	54.0

Source: Company, Anand Rathi Research

Fig 2 – Balance sheet (Rs m)

Year-end: Mar	FY19	FY20	FY21e	FY22e	FY23e
Share capital	297	297	297	297	297
Net worth	27,057	31,549	37,510	44,410	52,249
Debt	548	1,085	1,085	1,085	1,085
Minority interest	238	264	308	360	419
DTL / (Assets)	1,390	1,078	1,078	1,078	1,078
Capital employed	29,232	33,976	39,981	46,933	54,831
Net tangible assets	10,492	10,615	13,607	18,269	20,992
Net intangible assets	197	163	163	163	163
Goodwill	323	291	291	291	291
CWIP (tang. & intang.)	1,723	3,681	3,973	3,000	2,500
Investments (strategic)	5,464	4,888	6,088	6,088	6,088
Investments (financial)	2,088	6,517	6,517	7,517	7,517
Current asset (ex cash)	14,604	14,926	14,949	17,666	20,222
Cash	545	354	1,890	2,507	6,885
Current liabilities	6,203	7,460	7,496	8,568	9,827
Working capital	8,401	7,466	7,453	9,098	10,395
Capital deployed	29,232	33,976	39,981	46,933	54,831
Contingent liabilities	1,203	1,148	-	-	-

Source: Company, Anand Rathi Research

Fig 3 – Cash-flow statement (Rs m)

Year-end: Mar	FY19	FY20	FY21e	FY22e	FY23e
PBT adj. OI and interest	6,479	7,718	8,057	9,521	10,793
+ Non-cash items	1,189	1,302	1,717	2,310	2,778
Oper. prof. before WC	7,668	9,020	9,774	11,831	13,571
- Incr. / (decr.) in WC	784	(935)	(14)	1,645	1,297
Others incl. taxes	2,436	2,129	2,201	2,605	2,959
Operating cash-flow	4,448	7,826	7,587	7,581	9,315
- Capex (tang. + intang.)	2,721	3,319	5,000	6,000	5,000
Free cash-flow	1,727	4,507	2,587	1,581	4,315
Acquisitions					
-Div.(incl. buyback, tax)	536	983	662	941	1,069
+ Equity raised	-	-	-	-	-
+ Debt raised	388	537	-	-	-
- Fin Investments	2,822	3,853	1,200	1,000	-
-Misc. items (CFI+CFF)	(1,293)	400	(811)	(977)	(1,133)
Net cash-flow	51	(191)	1,536	617	4,379

Source: Company, Anand Rathi Research

Fig 4 – Ratio analysis

Year-end: Mar	FY19	FY20	FY21e	FY22e	FY23e
P/E (x)	42.0	27.2	27.4	23.2	20.4
EV / EBITDA (x)	23.4	19.5	17.8	14.6	12.4
EV / Sales (x)	4.4	4.3	4.2	3.5	3.0
P/B (x)	6.7	5.8	4.8	4.1	3.5
RoE (%)	16.0	21.1	17.7	17.7	17.0
RoCE (%) - after tax	16.4	21.3	18.0	18.1	17.6
RoIC	16.7	21.6	18.6	19.1	19.4
DPS (₹ / sh)	15.0	27.5	22.3	31.7	36.0
Dividend yield (%)	0.2	0.4	0.4	0.5	0.6
Dividend payout (%) - incl. DDT	10.3	12.2	10.0	12.0	12.0
Net debt / equity (x)	0	0	0	0	0
Receivables (days)	62	63	65	65	65
Inventory (days)	87	92	93	94	94
Payables (days)	65	87	90	86	86
CFO : PAT %	102.9	117.4	114.6	96.7	104.6

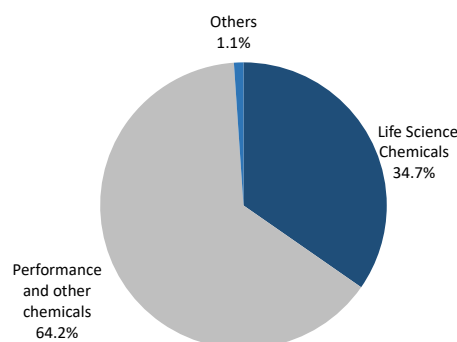
Source: Company, Anand Rathi Research

Fig 5 – Price movement



Source: Bloomberg

Fig 6 – Revenue contribution, by category



Source: Company

Result Update

Subdued operating performance

Standalone

Standalone revenue was Rs9.6bn, down 5.5% y/y, 58.8% q/q, driven by strong recovery in the demand. The gross margin expanded to ~53.9%, up 253bps y/y, down 398bps q/q as it reported the highest gross margin in Q1 (57.9%). The EBITDA margin rose 470bps y/y, 227bps q/q, to 25.8%, supported by lower other expenses. PAT was Rs1.7bn, down 18.6% y/y, (though q/q up 45.1%) as the tax rate returned to 25% against only 0.3% a year ago due to a tax benefit u/s 115BBA.

Consolidated

Atul's (consolidated) Q2 FY21 revenue was down 4.2% y/y, up 51.7% q/q, to Rs10bn, on the mixed performance of segments. The gross margin expanded 276bps y/y to 54.2% due to lower input costs. Absolute EBITDA grew 16.4% y/y, 64.6% q/q, to Rs2.6bn.

The EBITDA margin expanded a strong 460bps y/y, 204bps q/q, to 26.1% mainly due to the higher gross margin and lower other expenses, partially hit by higher employee costs. Due to the normalized 25.7% tax rate compared to 1.1% a year ago, PAT was Rs1.7bn (down 16.6% y/y, though q/q up 48%).

Subsidiaries

Revenue from subsidiaries grew 38.2% y/y, down 22.1% q/q, to Rs451m, bringing 4.5% to consolidated revenue. EBITDA and PAT were up 33.6% and 641% y/y respectively to Rs141m and Rs47m.

Expanding MCA capacity

On 21st Oct'20, Atul announced that its JV with Nouryon, a leading global technology manufacturer of mono-chloro-acetic acid (MCA), had received environmental clearance for its 32,000-ton MCA plant in Gujarat. Construction is expected to be complete this year, aiming to supply MCA to the Indian market by the year-end and to reach full production in H1 CY21.

MCA is an essential ingredient for the growing Indian agricultural, personal care and pharmaceutical markets. The JV will have the largest MCA plant in India, which will use chlorine and hydrogen manufactured by Atul to produce up to 32,000 tons of MCA, with the possibility of expanding this to 60,000 tons in future. Atul will consume a portion of the MCA for its own production; the balance will be marketed in India.

Financial highlights

Fig 7 – Financial trend

Particulars (Rsm)	Q3 FY19	Q4 FY19	Q1 FY20	Q2 FY20	Q3 FY20	Q4 FY20	Q1 FY21	Q2 FY21	% Y/Y	% Q/Q	H1 FY20	H1 FY21	% Y/Y
Income	10,315	10,580	10,406	10,456	10,414	9,655	6,606	10,021	(4.2)	51.7	20,862	16,627	(20.3)
RM costs	5,334	5,507	5,077	5,073	4,967	4,583	2,843	4,586	(9.6)	61.3	10,150	7,429	(26.8)
Employee expenses	662	704	699	771	754	785	740	768	(0.5)	3.7	1,470	1,508	2.6
Other expenses	2,186	2,340	2,228	2,368	2,200	2,406	1,436	2,056	(13.2)	43.2	4,595	3,492	(24.0)
EBITDA	2,134	2,031	2,403	2,244	2,493	1,881	1,587	2,612	16.4	64.6	4,647	4,198	(9.6)
Depreciation	291	330	318	323	324	338	331	332	2.8	0.3	641	663	3.5
Interest	19	17	19	20	31	24	27	22	6.4	(19.1)	39	48	23.8
Other income	(42)	42	100	210	115	356	406	65	(69.3)	(84.1)	310	471	52.0
PBT	1,782	1,726	2,166	2,111	2,253	1,875	1,635	2,323	10.0	42.0	4,277	3,958	(7.5)
Tax	628	607	689	24	572	460	459	596	2,405.5	30.1	713	1,055	47.9
PAT	1,154	1,119	1,477	2,087	1,680	1,415	1,177	1,726	(17.3)	46.7	3,564	2,903	(18.5)
MI	(6)	17	14	11	8	12	2	7	(32.4)	343.8	25	9	(64.6)
Profit from asso. & JV	11	13	11	13	17	9	3	24	89.1	771.4	24	27	14.3
Consol PAT	1,170	1,116	1,473	2,090	1,689	1,413	1,178	1,744	(16.6)	48.0	3,563	2,921	(18.0)
EPS (Rs)	39.4	38	49.6	70.4	56.9	47.6	39.7	58.7	(16.6)	48.0	120.0	98.4	(18.0)

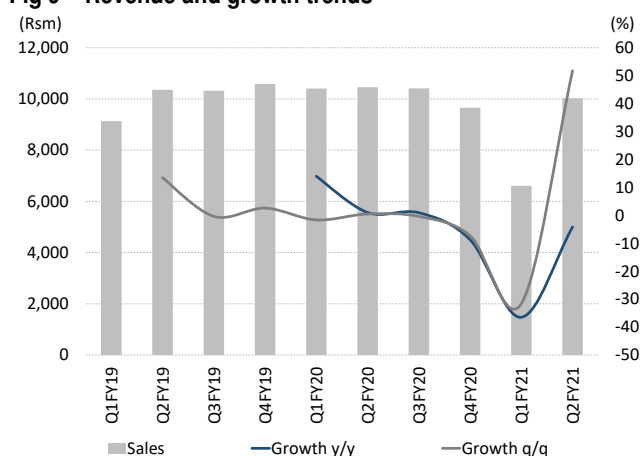
Source: Company, Anand Rathi Research *MI - minority Interest

Fig 8 – Quarterly trend, as percent of sales

Particulars (%)	Q3 FY19	Q4 FY19	Q1 FY20	Q2 FY20	Q3 FY20	Q4 FY20	Q1 FY21	Q2 FY21	bps Y/Y	bps Q/Q	H1 FY20	H1 FY21	bps Y/Y
Gross margins	48.3	48.0	51.2	51.5	52.3	52.5	57.0	54.2	276	(273)	51.3	55.3	397
Employee costs	6.4	6.6	6.7	7.4	7.2	8.1	11.2	7.7	28	(355)	7.0	9.1	202
Other expenses	21.2	22.1	21.4	22.6	21.1	24.9	21.7	20.5	(213)	(122)	22.0	21.0	(103)
EBITDA margins	20.7	19.2	23.1	21.5	23.9	19.5	24.0	26.1	460	204	22.3	25.3	298
Depreciation	2.8	3.1	3.1	3.1	3.1	3.5	5.0	3.3	23	(170)	3.1	4.0	92
Interest	0.2	0.2	0.2	0.2	0.3	0.2	0.4	0.2	2	(19)	0.2	0.3	10
Other income	(0.4)	0.4	1.0	2.0	1.1	3.7	6.2	0.6	(137)	(551)	1.5	2.8	135
PBT margins	17.3	16.3	20.8	20.2	21.6	19.4	24.8	23.2	299	(158)	20.5	23.8	330
Effective tax rate	35.2	35.2	31.8	1.1	25.4	24.5	28.0	25.7	2,455	(237)	16.7	26.7	998
PAT margins	11.3	10.5	14.2	20.0	16.2	14.6	17.8	17.4	(259)	(43)	17.1	17.6	49

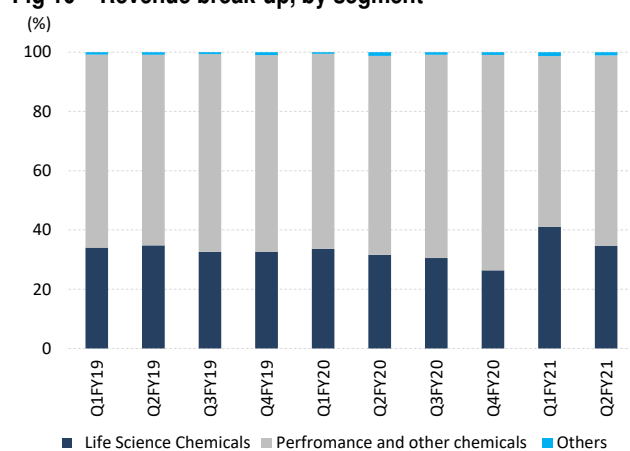
Source: Company, Anand Rathi Research

Fig 9 – Revenue and growth trends



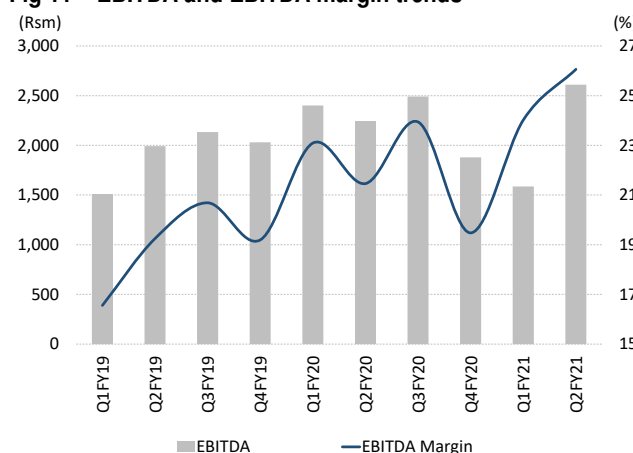
Source: Company, Anand Rathi Research

Fig 10 – Revenue break-up, by segment



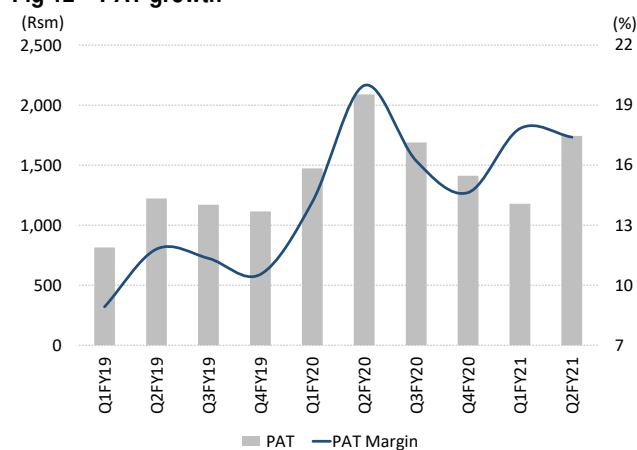
Source: Company, Anand Rathi Research

Fig 11 – EBITDA and EBITDA margin trends



Source: Company, Anand Rathi Research

Fig 12 – PAT growth



Source: Company, Anand Rathi Research

Consolidated performance, by segment

Life-science chemicals

Revenue of the life-science-chemicals division grew 5.3% y/y, 28.3% q/q, to Rs3.5bn. Absolute EBIT increased 7.7% y/y, 31.5% q/q, to Rs671m with a 19.3% EBIT margin (up 43bps y/y, 47bps q/q). The RoCE of the Life-science chemicals division was 12.5% (11.2% a year ago). The segment's capital employed decreased 3% y/y to Rs5.4bn.

Performance and other chemicals

Q2 FY21 revenue slipped 7.7% y/y, though q/q up 64%, to Rs6.9bn. The EBIT margin was 23.1%, up 411bps y/y, 276bps q/q. Absolute EBIT was Rs1.6bn, up 12.2% y/y, 86.3% q/q. The RoCE was 12.5% (11.2% a year ago). Investment in the business was Rs12.7bn.

Fig 13 – Quarterly (consolidated) trends, by segment

Particulars (Rs m)	Q2 FY20	Q1 FY21	Q2 FY21	% Y/Y	% Q/Q	H1 FY20	H1 FY21	% Y/Y
Revenue								
Life Science chemicals	3,301	2,709	3,475	5.3	28.3	6,799	6,184	(9.0)
Specialty chemicals	7,473	4,205	6,896	(7.7)	64.0	14,801	11,101	(25.0)
Others	129	87	108	(16.6)	23.8	185	195	5.5
Inter-segment	447	395	458	2.4	16.0	923	853	(7.6)
Net sales	10,456	6,606	10,021	(4.2)	51.7	20,862	16,627	(20.3)
EBIT								
Life Science chemicals	623	510	671	7.7	31.5	1,325	1,182	(10.8)
Specialty chemicals	1,420	856	1,594	12.2	86.3	2,888	2,449	(15.2)
Others	50	-5	48	(3.8)	L2P	61	43	(29.9)
EBIT margins (%)								
Life Science chemicals	18.9	18.8	19.3	43	47	19.5	19.1	(38)
Specialty chemicals	19.0	20.3	23.1	411	276	19.5	22.1	255
Others	38.8	(6.0)	44.7	594	NA	33.2	22.1	(1,113)

Source: Company, Anand Rathi Research

Valuation

Change in estimates

Fig 14 – Change in estimates

(Rs m)	Old estimates		New estimates		Change (%)	
	FY21e	FY22e	FY21e	FY22e	FY21e	FY22e
Revenue	44,058	52,115	41,593	49,296	(5.6)	(5.4)
EBITDA	9,693	11,465	9,774	11,831	0.8	3.2
PAT	6,643	7,659	6,623	7,841	(0.3)	2.4

Source: Anand Rathi Research

To arrive at the value of Atul, we use the DCF method. The 11% WACC used has been arrived at as follows:

Fig 15 – WACC

Equity (FY20) (Rs m)	31,549
Cost of equity (%)	11
Debt (FY20) (₹ m)	1,085
Cost of debt (%)	8.0
Weighted average cost of capital (%)	10.9

Source: Anand Rathi Research

To arrive at future cash flows, a 5% terminal growth rate has been assumed.

Fig 16 – Present value of FCFF

(Rs m)	FY21e	FY22e	FY23e	FY24e	FY25e	FY26e	FY27e	FY28e	FY29e	FY30e	FY31e
EBIT	8,889	10,507	11,924	14,128	16,535	19,189	22,267	25,840	29,986	34,798	40,381
EBIT (1-t)	6,667	7,880	8,943	10,596	12,402	14,391	16,701	19,380	22,490	26,098	30,286
Depreciation	1,717	2,310	2,778	3,054	3,181	3,356	3,540	3,735	3,940	4,156	4,384
WC changes	14	(1,645)	(1,297)	(1,611)	(1,730)	(2,008)	(2,330)	(2,704)	(3,138)	(3,642)	(4,226)
Capex	(5,000)	(6,000)	(5,000)	(1,500)	(1,500)	(2,000)	(2,110)	(2,226)	(2,348)	(2,477)	(2,613)
FCFF	3,398	2,545	5,424	10,538	12,352	13,739	15,801	18,185	20,943	24,136	27,831
PV of FCFF	3,064	2,069	3,976	6,967	7,364	7,385	7,659	7,948	8,254	8,577	8,918

Source: Anand Rathi Research

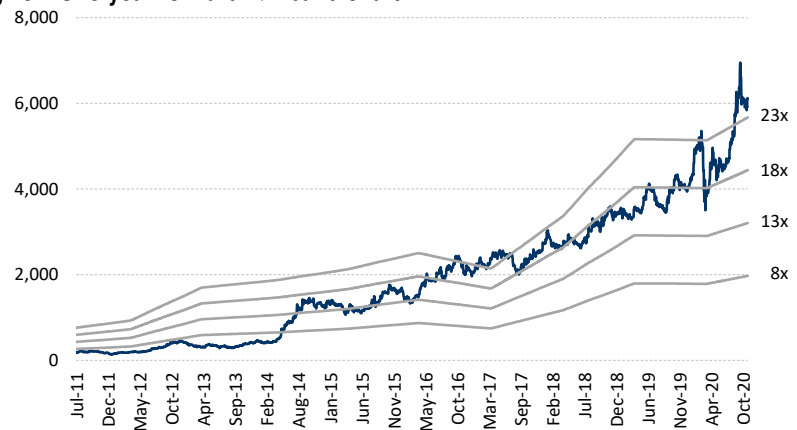
DCF-based valuation

Fig 17 – Target price (Rsm)

Present value	72,180
Terminal value	151,146
Debt	(1,085)
Cash	354
Total value	222,595
No. of shares (m)	30
Target price (Rs)	7,500

Source: Anand Rathi Research

At the target price of Rs7,500, the stock is valued at a PE multiple of 28.4x FY22e and 25x FY23e. On an EV/EBITDA multiple, it is valued at 18.1x FY22e and 15.4x FY23e.

Fig 18 – One-year-forward P/E band chart

Source: Bloomberg, Anand Rathi Research

Risks

- Drop in spreads of major products
- Decrease in prices of major products such as p-cresol, resorcinol, 44 DDS, 2,4- D, dapsone, vat dyes, etc.
- Delay in capex and debottlenecking
- Erratic increase in prices of crude and crude derivatives.
- Global slowdown, leading to a deceleration in key consumer sectors (agro-chemicals, pharmaceuticals, dyes & pigments).

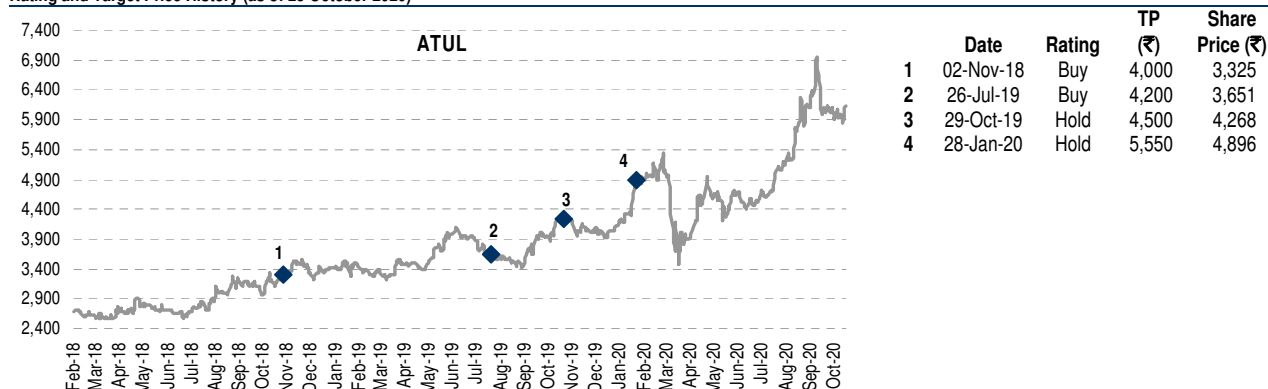
Appendix

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Rating and Target Price History (as of 25 October 2020)



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Analysts' ratings and the corresponding expected returns take into account our definitions of Large Caps (>US\$1bn) and Mid/Small Caps (<US\$1bn) as described in the Ratings Table below:

Ratings Guide (12 months)

	Buy	Hold	Sell
Large Caps (>US\$1bn)	>15%	5-15%	<5%
Mid/Small Caps (<US\$1bn)	>25%	5-25%	<5%

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