

## Strong performance but expensive valuations...

Solar Industries reported a commendable Q2FY21 performance led by strong performance in exports & overseas business as well as improved margins. Order backlog improved sharply as SCCL & defence order books got replenished. Revenue for the quarter came in at ₹ 587.3 crore, up 16% YoY. Explosives volume increased 9% YoY to 69194 MT while realisation dropped 6% YoY to ₹ 32074. Overall explosives segment posted a 3% rise in revenue to ₹ 222 crore on the back of improved volumes. Accessories segment reported a decline of 9% coming in at ₹ 61 crore. Gross margins expanded ~255 bps YoY on account of lower input costs. In contrast, employee cost & other expense increased 23.9% & 25.9% YoY, respectively, thus hindering transmission of higher margins at operating level, to a certain extent. EBITDA came in at ₹ 125.9, up 17.9% YoY with margin of 21.4% vs. 21.1% YoY. Consequent PAT came in at ₹ 67.6 crore in Q2FY21 vs. ₹ 86.6 crore in Q2FY20. The YoY decline is a consequence of negative tax charge of ₹ 9.1 crore in the comparable quarter. That being the case, PBT for the quarter came in at ₹ 92.2 crore, up 19% YoY.

## Overseas, exports witness uptick, sustenance expected...

SIL's Q2FY21 performance was largely the result of its all-time high revenue from overseas & exports with business in Turkey returning to normal whereas commencement of Ghana operations further aided the performance. During the quarter, exports came in at ₹ 81 crore and overseas at ₹ 393 crore. Ex-new geographies, O&E segment grew 18% YoY. Going ahead, SIL plans to add a few more markets to its overseas portfolio whereas in existing markets, the company plans to increase market share in South Africa (market size of US\$700 million with SIL's share being 2.5%) & Australia (setting up a new plant). Overall, the management is quite assertive of growth in O&E in coming years on the back of addition in new geographies and market share gains in the current ones.

## Defence to become longstanding opportunity...

The defence orderbook jumped from ₹ 338 crore in Q1 to ₹ 702 crore in Q2FY21 on the back of multi-mode hand grenade order. Revenue for the same is expected to start flowing in from Q4FY21. Currently, SIL is supplying propellants for Akash missile and also working on two other missiles. The management expects the defence segment to grow in double digits over the next five years.

## Valuation & Outlook

The overall performance was better than estimates. The management has also provided a better outlook for the future. However, at the current market price, SIL is trading at ~28.1x FY22E EPS, leaving little upside. We expect SIL will post revenue, EBITDA, PAT CAGR of 14.1%, 19.5%, 9.7%, respectively, in FY20-22E. We value the stock at 28x FY22E EPS of ₹ 35.5 to arrive at a target price of ₹ 995. We revise our rating from REDUCE to **HOLD**.

### Key Financial Summary

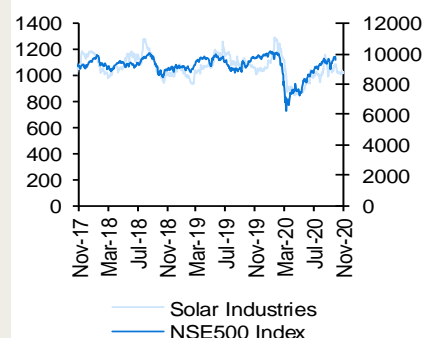
	FY18	FY19	FY20	FY21E	FY22E	CAGR (FY20-22E)
Revenue	1,916.1	2,461.6	2,237.3	2,430.9	2,912.3	14.1%
EBITDA	411.6	501.9	434.3	505.6	620.3	19.5%
EBITDA margin (%)	21.5	20.4	19.4	20.8	21.3	
Net Profit	220.6	267.7	267.4	252.4	321.5	9.7%
EPS (₹)	24.4	29.6	29.6	27.9	35.5	
P/E (x)	41.0	33.8	33.8	35.9	28.1	
EV/EBITDA (x)	22.9	18.8	21.7	18.9	15.3	
RoCE (%)	21.8	23.8	20.3	19.6	22.7	
RoE (%)	20.3	21.6	21.6	18.3	21.6	

Source: ICICI Direct Research, Company



Particulars	
Stock Data	Amount
Market Capitalization	₹9030.9 Crore
Debt (FY 20)	₹469.1 Crore
Cash and Inv (FY 20)	₹91.8 Crore
EV (FY 20)	₹9408.2 Crore
52 week H/L (BSE)	1350 / 772
Equity capital	₹18.1 Crore
Face value	₹2

### Price Graph



### Key Highlights

- SCCL, defence order books replenished. Overall orderbook at ₹ 1745 crore in Q2
- Housing, infra segments to pick up in H2
- Value at ₹ 28x FY22EPS to arrive at a target price of ₹ 995 per share. Revise rating from REDUCE to HOLD

### Research Analyst

Chirag Shah  
shah.chirag@icicisecurities.com

Adil Khan  
adil.khan@icicisecurities.com

Exhibit 1: Variance Analysis

	Q2FY21	Q2FY20	YoY (%)	Q1FY21	QoQ (%)	Comments
Total Revenues	587.3	506.6	15.9	491.1	19.6	Strong topline performance on the back of O&E & defence businesses
Raw materials costs	288.7	262.0	10.2	269.7	7.0	Ammonium nitrate prices decline 6% QoQ
Employees Cost	56.0	45.2	23.9	48.8	14.7	Higher employee costs on the back of employee welfare expenditure
Other Expenses	116.6	92.7	25.9	80.6	44.6	CSR expenses and forex losses impacted other expenses
Total Expenditure	461.4	399.8	15.4	399.2	15.6	
EBITDA	125.9	106.7	17.9	91.9	36.9	
EBITDA margins (%)	21.4	21.1	37 bps	18.7	272 bps	Minor increase in margins as overall increase in GMs were not transmitted owing to higher employee & other expenses
Depreciation	23.9	20.9	14.4	22.8	4.7	
EBIT	102.0	85.9	18.8	69.1	47.6	
Interest	11.7	14.4	-19.1	12.3	-5.1	
Other Income	1.9	6.1	-69.1	3.9	-51.8	
Extra Ordinary Item	0.0	0.0		0.0	0.0	
PBT	92.2	77.5	19.0	60.7	51.9	
Total Tax	24.6	-9.1	-370.6	16.8	46.9	
PAT(after MI)	65.2	84.4	-22.7	42.1	54.8	PAT declines YoY as there was a negative charge in comparable quarter
<b>Key Metrics</b>	<b>Q2FY21</b>	<b>Q2FY20</b>	<b>YoY (%)</b>	<b>Q1FY21</b>	<b>QoQ (%)</b>	
Ind. explosives volume (MT)	69,194	63,611	8.8	70,287	-1.6	Better volumes YoY
Realisation (₹/MT)	32,074	34,015	-5.7	34,238	-6.3	Realisations down on account of decline in ammonium nitrate
Value (₹ crore)	222	216	2.6	241	-7.8	
Initiating Systems (₹ crore)	61	67	-9.0	61	0.0	
Exports & Overseas (₹ crore)	266	202	31.5	207	28.5	Strong performance across geographies
Defence (₹ crore)	57	45	27.5	23	142.7	Defence also further grows on the back of MMHG

Source: Company, ICICI Direct Research

Exhibit 2: Change in estimates

	FY18	FY19	FY20	FY21E		FY22E
(₹ Crore)	Actual	Actual	Actual	Old	New	% Change
Revenue	1,916.1	2,461.6	2,237.3	2,764.7	2,430.9	-12.1
EBITDA	411.6	501.9	434.3	575.1	505.6	-12.1
EBITDA Margin (%)	21.5	20.4	19.4	20.8	20.8	0 bps
PAT	220.6	267.7	267.4	286.8	252.4	-12.0
EPS (₹)	24.4	29.6	29.6	31.7	27.9	-12.0

Source: Company, ICICI Direct Research

## Conference call key highlights

### Q2FY21 operational performance

- Achieved all-time high quarterly revenue from overseas
- H2 looks promising, FY21E to better than FY20, expecting 15-20%
- Margins to be sustained
- Higher other expenses on account of CSR expenses and forex loss
- Defence to grow in double digits in the next five years.
- Ammonium nitrate prices were down 6% sequentially
- We expect housing & infra to pick up in H2

### Developments in defence segment

- Received order for multi-mode hand grenade worth ₹ 404 crore and executable in the next two years
- Revenue from multi-mode hand grenade to start flowing in from Q4 onwards
- First ever Pinaka MK-1 enhanced rocket fully manufactured by SIL was successfully test fired
- Order book as on Q2FY21 is ₹ 702 crore

### Overseas & Exports

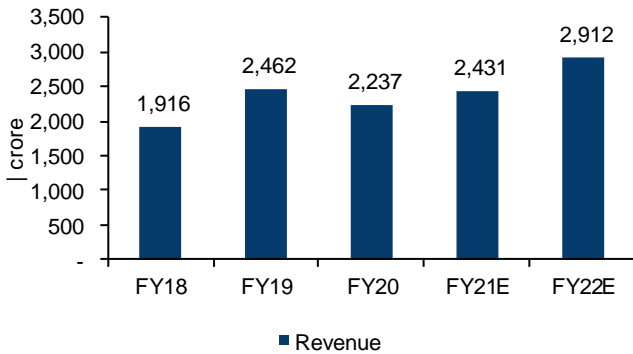
- Business in Turkey picked up vs. last year where it was down 30%. It is planning to expand in Balkan regions as well
- Ghana operations started, should be at breakeven this year
- South Africa is receiving orders as per management expectations. Losses expected to be minimal this year
- It is expecting to add a few more markets in overseas while growing market share in the existing regions
- To enter into Australia starting with Initiating systems

### Order book

- Order book backlog as on Q3FY20 - ₹ 1745 crore
- Breakup of the same – Coal India ~₹ 601 crore; Singareni Collieries Company (SCCL) - ₹ 442 crore and defence ~ ₹ 702 crore

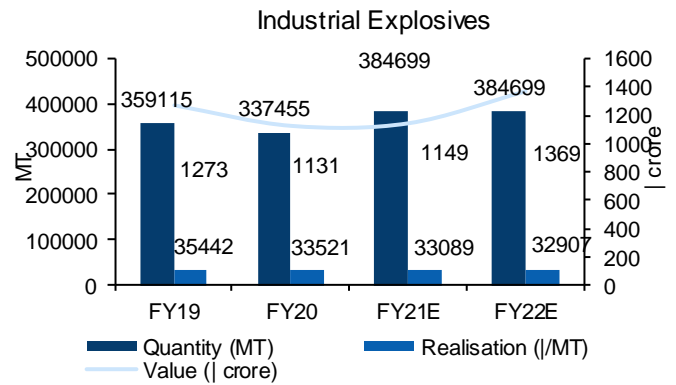
## Financial story in charts

Exhibit 3: Revenue trend



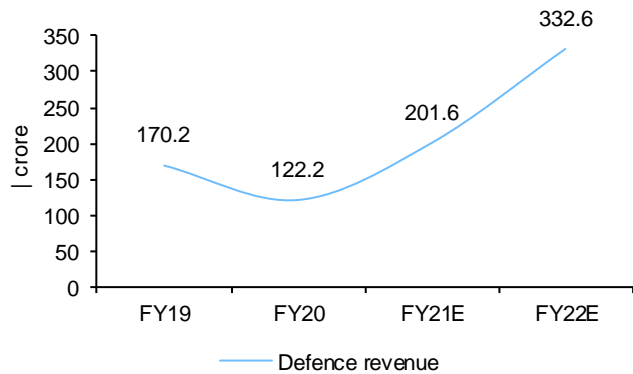
Source: Company, ICICI Direct Research

Exhibit 4: Industrial explosives growth trend



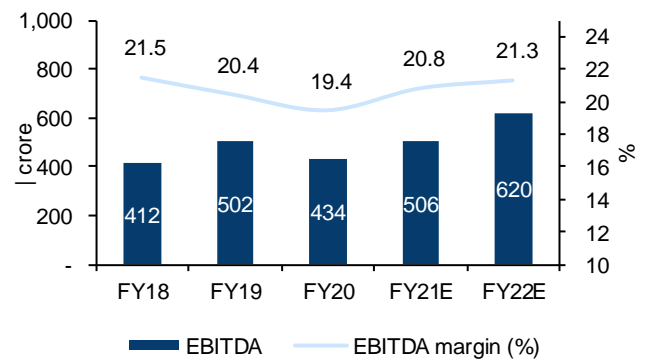
Source: Company, ICICI Direct Research

Exhibit 5: Defence segment revenue trend



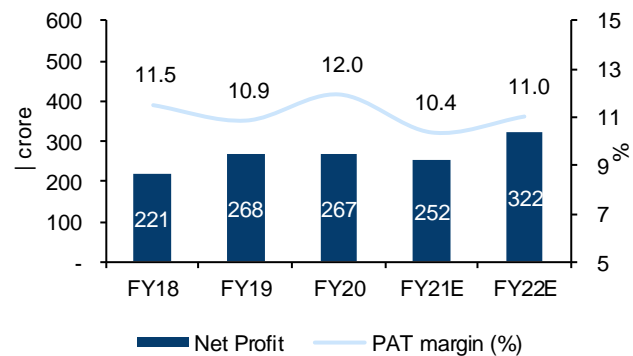
Source: Company, ICICI Direct Research

Exhibit 6: EBITDA and EBITDA margin trend



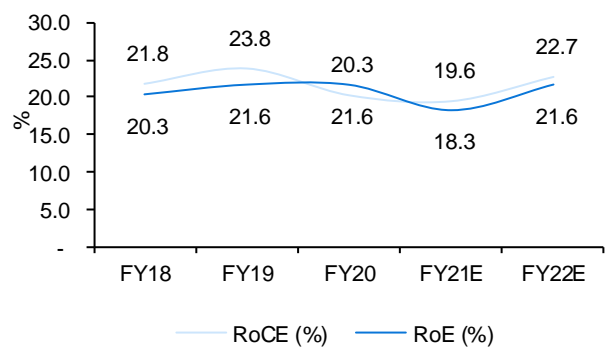
Source: Company, ICICI Direct Research

Exhibit 7: PAT and PAT margin trend



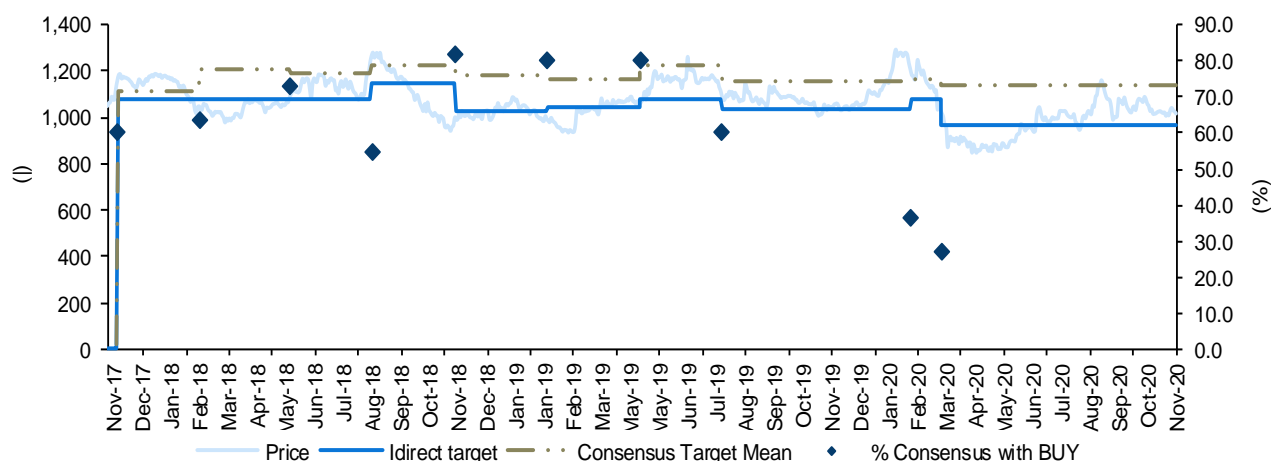
Source: Company, ICICI Direct Research

Exhibit 8: Return ratios trend



Source: Company, ICICI Direct Research

Exhibit 9: Recommendation history vs. consensus



Source: Company, ICICI Direct Research

Exhibit 10: Top 10 shareholders

Rank	Investor Name	Filing Date	% O/S	Position (%)	Change
1	Nuwal Manish Satyana	30-Jun-20	27.9	25.23m	0.00m
2	Nuwal Kailashchandra	30-Jun-20	23.1	20.88m	0.00m
3	Nuwal Satyanarayan N	30-Jun-20	14.6	13.24m	0.00m
4	Nuwal Indira Kailash	30-Jun-20	6.2	5.57m	0.00m
5	Sbi Funds Management	31-Aug-20	6.0	5.42m	0.03m
6	Kotak Mahindra Asset	31-Aug-20	4.0	3.65m	0.04m
7	Fmr Llc	31-Jul-20	3.3	2.97m	0.20m
8	Hdfc Asset Managemen	31-Aug-20	3.3	2.96m	0.00m
9	Dsp Blackrock Invest	31-Aug-20	2.4	2.14m	(0.01)m
10	Nuwal Nandlal Bodula	8-Jan-19	2.3	2.10m	0.00m

Source: Company, ICICI Direct Research

Exhibit 11: Shareholding pattern

(in %)	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20
Promoter	73.2	73.2	73.2	73.2	73.2
FII	3.6	3.6	4.0	4.4	4.8
DII	18.6	18.6	18.3	17.6	17.3
Others	4.6	4.7	4.5	4.8	4.7

Source: Company, ICICI Direct Research

## Financial Summary (Consolidated)

Exhibit 12: Profit and loss statement (₹ Crore)				
(Year-end March)	FY19	FY20	FY21E	FY22E
Revenue	2,462	2,237	2,431	2,912
Growth YoY (%)		(9.1)	8.7	19.8
Raw Material Expenses	1,401	1,215	1,325	1,602
COGS	56.9	54.3	54.5	55.0
Employee Expenses	184	207	211	253
Other Expenses	374	381	389	437
Total Operating Expenditu	1,960	1,803	1,925	2,292
Operating Profit (EBITDA)	502	434	506	620
Growth YoY (%)		(13.5)	16.4	22.7
Interest	50	55	67	60
Other Income	15	41	20	30
PBDT	467	420	458	590
Depreciation	59	85	93	105
PBT after Exceptional Item	408	336	365	485
Total Tax	125	57	102	136
PAT before MI	283	279	263	349
Minority Interest	15	11	11	28
PAT	268	267	252	322
Growth YoY (%)		(0.1)	(5.6)	27.4
EPS	29.6	29.6	27.9	36

Source: Company, ICICI Direct Research

Exhibit 14: Balance Sheet (₹ Crore)				
(Year-end March)	FY19	FY20	FY21E	FY22E
Equity Capital	18.1	18.1	18.1	18.1
Reserve and Surplus	1,220.2	1,362.0	1,469.0	1,643.1
Total Shareholders func	1,238.3	1,380.1	1,487.0	1,661.2
Secured Loan	156.1	261.8	450.0	300.0
Unsecured Loan	312.9	357.4	250.0	325.0
Total Debt	469.1	619.2	700.0	625.0
Deferred Tax Liability	119.5	104.9	104.9	104.9
Minority Interest	47.6	51.5	53.4	66.5
Total Liabilities	1921	2213	2402	2514
Gross Block	1,354.5	1,714.3	1,934.3	2,134.3
Accumulated Depreciat	297.5	382.1	475.0	579.6
Net Block	1,057.0	1,181.8	1,459.3	1,554.7
Capital WIP	177.6	152.2	50.0	50.0
Total Fixed Assets	1,234.5	1,334.0	1,509.3	1,604.7
Inventory	282.7	331.0	286.4	319.2
Debtors	399.0	370.3	399.6	438.8
Loans and Advances	2.3	5.7	1.9	2.3
Other Current Assets	66.7	69.8	53.5	64.1
Cash	91.8	120.1	285.7	264.8
Total Current Assets	969.0	983.5	1,113.7	1,175.8
Creditors	163.3	154.4	153.2	183.5
Provisions	194.2	162.1	168.5	183.5
Total Current Liabilities	361.0	319.8	324.9	370.3
Net Current Assets	608.0	663.7	788.8	805.6
Total Assets	1921	2213	2402	2514

Source: Company, ICICI Direct Research

Exhibit 13: Cash Flow Statement (₹ Crore)				
(Year-end March)	FY19	FY20	FY21E	FY22E
Profit after Tax	267.7	267.4	252.4	321.5
Add: Depreciation	58.9	84.5	93.0	104.6
Add: Interest Paid	49.9	55.0	67.5	60.3
Cash Flow before WC changes	376.4	407.0	412.9	486.4
(Increase)/Decrease in inventory	(50.3)	(48.2)	44.6	(32.8)
(Increase)/Decrease in debtors	(35.5)	28.7	(29.3)	(39.2)
(Increase)/Decrease Loan & Advan	10.2	(3.4)	3.7	(0.4)
(Increase)/Decrease in CA	7.6	(3.1)	16.3	(10.6)
Net Increase in Current Assets	(128.0)	13.8	35.3	(83.0)
Net Increase in Current Liabilities	87.2	(41.2)	5.1	45.3
Net CF from operating activities	336	380	453	449
(Purchase)/Sale of Fixed Assets	(270.9)	(265.0)	(210.0)	(200.0)
Inc / (Dec) in Deferred Tax Liability	18.4	(14.6)	-	-
Net CF from Investing Activities	-200	-379	-153	-187
Proceeds/(Repay) Secured Loan	(40.0)	105.7	188.2	(150.0)
Proceeds/(Repay) Unsecured Loan	83.1	44.5	(107.4)	75.0
(Payment) of DDT	(76.3)	(76.3)	(81.4)	(72.4)
Interest Paid	(49.9)		(67.5)	(60.3)
Net CF from Financing Activities	-113	25	-132	-283
Net Cash flow	22.3	25.4	168.5	(20.8)
Cash and Cash Eq. (beginning)	69.5	91.8	117.2	285.7
Cash and Cash Equivalent (end)	91.8	117.2	285.7	264.8

Source: Company, ICICI Direct Research

Exhibit 15: Key Ratios				
(Year-end March)	FY19	FY20	FY21E	FY22E
Per Share Data				
Reported EPS	29.6	29.6	27.9	35.5
Cash EPS	36.1	38.9	38.2	47.1
BV per share	136.8	136.8	152.5	164.3
Dividend per share	7.0	7.0	7.0	9.0
Cash Per Share	32.9	32.9	42.2	52.5
Operating Ratios (%)				
EBITDA Margin	20.4	19.4	20.8	21.3
EBIT / Net Sales	18.0	15.6	17.0	17.7
PAT / Net Sales	10.9	12.0	10.4	11.0
Inventory days	41.9	46.1	49.7	35.9
Debtor days	59.2	65.1	55.6	50.1
Creditor days	24.2	26.6	23.2	19.2
Return Ratios (%)				
RoE	21.6	21.6	18.3	21.6
RoCE	23.8	20.3	19.6	22.7
RoIC	30.6	24.2	23.1	27.5
Valuation Ratios (x)				
P/E	33.8	33.8	35.9	28.1
EV / EBITDA	18.8	21.7	18.9	15.3
EV / Net Sales	3.8	4.2	3.9	3.2
Market Cap / Sales	3.7	4.0	3.7	3.1
Price to Book Value	7.3	7.3	6.6	6.1
Solvency Ratios				
Debt / EBITDA	0.9	1.1	1.2	1.1
Debt / Equity	0.4	0.4	0.4	0.5
Current Ratio	2.1	2.1	2.4	2.3
Quick Ratio	1.3	1.3	1.4	1.4

Source: Company, ICICI Direct Research

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**Pankaj Pandey**

**Head – Research**

**pankaj.pandey@icicisecurities.com**

**ICICI Direct Research Desk,  
ICICI Securities Limited,  
1st Floor, Akruiti Trade Centre,  
Road No 7, MIDC,  
Andheri (East)  
Mumbai – 400 093  
research@icicidirect.com**

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