

Buy

Sudarshan Chemicals reported a healthy 3QFY21 performance in an otherwise weak demand scenario.

- Sales grew by 19.6% YoY to Rs 5.06bn (D.est: Rs 4.2bn). Gross margins remained flattish on a YoY basis at 42.8%.
- EBITDA grew by 26.5% YoY to Rs 796mn (D.est: Rs 641mn), with healthy EBITDA margin of 15.7% (up 90bps YoY).
- PAT growth too beat our estimates as the company reported a growth of 38.3% YoY.

Outlook and Valuation

Out of the planned Capex of Rs 5.85bn over FY20-21, Capex for projects worth Rs 1.5bn will be completed in FY21 while an amount of Rs 2.1bn will be spent in FY22. Market share gains from the incremental demand that may transpire amidst transitioning global supply chains (away from China) would translate into an earnings CAGR of 14.0% over FY20-23E. Backed by a strong capex program (~Rs 5.8bn over FY20-22E) the company is well placed to seize opportunities on a global landscape. Introduction of new high performance pigments (expected 4-5 new launches over FY21-22) is likely to be margin/RoCE accretive and will garner superior asset turns (~3.0x on capex earmarked for growth capex ~Rs 4.0bn). We thus believe that RoCE's are set to improve by 300 bps from FY20 to FY23E to 19.3% as assets begin sweating. We like Sudarshan Chemical focused approach on the Pigments business, prudent capital allocation in a much commoditised business, global presence, strong SHE practices and growth opportunities cropping up from consolidation in the global pigments arena. We have upgraded our FY21/FY22/FY23 earnings by 32.9/8.2/12.8% owing to a strong 3QFY21 performance coupled with growth coming in from new geographies like Japan and rich product mix. We revise our target price to Rs 621/share and maintain buy rating on the stock.

Q3FY21 Result (Rs Mn)

Particulars	Q3FY21	Q3FY20	YoY (%)	Q2FY21	QoQ (%)
Revenue	5,064	4,235	19.6	4,289	18.1
Total Expense	4,267	3,606	18.3	3,612	18.1
EBITDA	796	629	26.5	677	17.7
Depreciation	217	178	21.8	219	(1.0)
EBIT	580	451	28.4	458	26.6
Other Income	26	14	83.5	18	40.7
Interest	46	38	21.7	51	(10.7)
EBT	559	411	36.1	455	22.8
Tax	168	128	31.1	123	36.1
RPAT	392	283	38.3	332	17.9
APAT	392	300	30.7	301	29.9
			(bps)		(bps)
Gross Margin (%)	42.8	43.0	(26)	44.2	(140)
EBITDA Margin (%)	15.7	14.9	87	15.8	(6)
NPM (%)	7.7	6.7	105	7.7	(1)
Tax Rate (%)	30.0	31.1	(113)	27.1	292
EBIT Margin (%)	11.4	10.7	79	10.7	77

CMP	Rs 506
Target / Upside	Rs 621 / 23%
NIFTY	13,635

Script Details

Equity / FV	Rs 138mn / Rs 2
Market Cap	Rs 35bn
	USD 481mn
52-week High/Low	Rs 538/ 290
Avg. Volume (no)	2,44,529
Bloom Code	SCHI IN

Price Performance	1M	3M	12M
Absolute (%)	6	15	12
Rel to NIFTY (%)	6	15	18

Shareholding Pattern

	Jun'20	Sep'20	Dec'20
Promoters	42.7	42.7	40.0
MF/Banks/FIs	3.2	4.2	6.7
FII's	8.3	8.1	9.3
Public / Others	45.8	45.0	43.9

Valuation (x)

	FY21E	FY22E	FY23E
P/E	26.7	22.5	18.0
EV/EBITDA	14.5	12.7	10.5
ROE (%)	20.4	21.1	22.7
RoACE (%)	11.9	13.3	14.9

Estimates (Rs mn)

	FY21E	FY22E	FY23E
Revenue	17,877	20,114	22,636
EBITDA	2,759	3,215	3,757
PAT	1,315	1,558	1,953
EPS (Rs.)	19.0	22.5	28.2

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Exhibit 1: Actual vs DART Estimates

Particulars	Actual	Estimated	Variance (%)	Comments
Revenue	5,064	4,220	20.0	Better than expected Domestic sales
EBITDA	796	641	24.3	Higher than expected gross margin
EBITDA Margin(%)	15.9	15.2	69	
PAT	392	278	40.8	Lower than expected Depreciation and interest cost

Source: DART, Company

Exhibit 2: Change in Estimates

Particulars (Rs Mn)	FY21E			FY22E			FY23E		
	New	Previous	Chg.(%)	New	Previous	Chg.(%)	New	Previous	Chg.(%)
Revenue	17,877	16,120	10.9	20,114	18,506	8.7	22,636	21,249	6.5
EBITDA	2,759	2,306	19.6	3,215	2,860	12.4	3,757	3,285	14.4
EBITDA Margin(%)	15.4	14.3	110.0	16.0	15.5	50.0	16.6	15.5	110.0
PAT	1,315	992	32.6	1,558	1,441	8.1	1,953	1,733	12.7
EPS(Rs)	19.0	14.3	32.9	22.5	20.8	8.2	28.2	25.0	12.8

Source: DART, Company

Concall Highlights

Business Updates

- Pigment business registered a growth of 22.1% to Rs 4.70bn on the back of good traction from Coatings, Plastics and Inks business.
- Domestic business has seen strong demand surge with fast pace recovery in economic activities in India with Exports also continuing to see steady demand inflow.
- Demand from End User industry of Coatings, Paints and Inks has improved.
- Coatings has seen good traction across Asia with India seeing strong demand. Plastics and Inks have also seen good amount of offtake. However, Europe and North America which have been impacted by 2nd Covid wave have seen subdued demand specially in Plastics.
- Company plants have reached pre-covid utilization levels.
- Domestic Export Mix – 56:44
- Employee costs jumped 21% YoY to Rs 429mn on the back of increments offered in Q3FY21 and new hiring for expanding other newer markets and onboarding of new team for penetrating into the newly entered Japanese market.
- Employees cost is expected to be on similar lines as Q3FY21 going ahead.
- The company has opted for the lower tax regime under section 115BAA from FY 2019-20 onwards.
- The new subsidiary opened last year in Japan has seen good progress and the company expects to generate higher margins from the Japanese market.

New Launches

- Company's new product under development - High Performance Yellow pigment (Yellow 138) is showing good progress in Q3FY21 with product trials already underway and sampling expected to start very soon.
- The company expects to receive customer approvals for this new product by the end of Q1FY22.
- The company targets to launch 4-5 major High Performance Pigments next year which include the previously announced 2 new HPP slated to launch in March 21 and September 21.
- New HPP planned to be launched in March 21 is progressing as per schedule, however the HPP targeted for Sep 21 launch is estimated to be delayed by 1-2 months due to the ongoing pandemic disruptions.
- New product launches are expected to contribute 15-20% to total revenues going forward.
- The company is looking to launch new products and add new customer in newer geographies of Europe, US and South East Asia.
- New product launches will help in improving product mix which will in turn lead to higher margins, the full impact of which will be seen after 2-3 years.

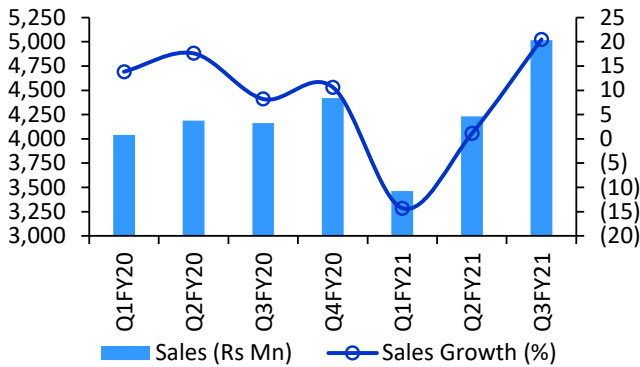
Raw Material Scenario

- Raw material prices for select intermediates saw an increase in Q3FY21 which the company was not able to pass on to customers as there is a lag of almost 3 months in passing of rise in costs.
- Export benefits under the MEIS scheme have been capped from September 2020 and the MEIS scheme will cease to exist and will be replaced with a new scheme called Remission of Duties and Taxes on Exported Products (RoDTEP) from 1st January 2021 onwards.
- The sectors to be covered and the applicable rates have still not been notified for the RoDTEP scheme and are currently still under evaluation.
- Pigment business margins were impacted due to the rise in Raw material costs and lower export benefits for selling under MEIS scheme.
- RM prices are expected to stabilize in the coming months and the company is already under process to pass on the price hike.

Capex Update

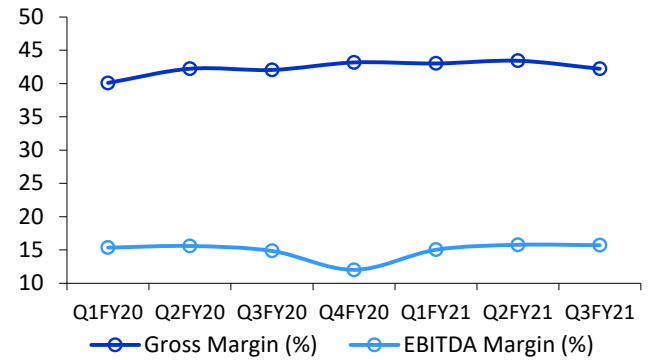
- Out of the planned Capex of Rs 5.85bn over FY20-21, Capex for projects worth Rs 1.5bn will be completed in FY21 while an amount of Rs 2.1bn will be spent in FY22.
- Out of the total Capex 70% would be towards Growth with balance 30% towards Infrastructure and technological developments.
- New Capex is expected to generate Asset tons of 2-2.5x at peak utilization

Exhibit 3: Sales and Sales Growth



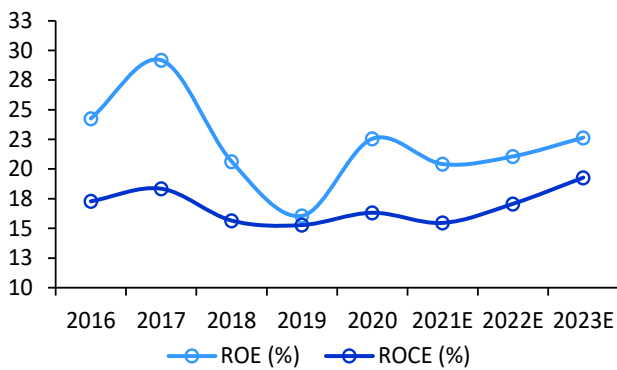
Source: DART, Company

Exhibit 4: Gross/EBITDA Margin



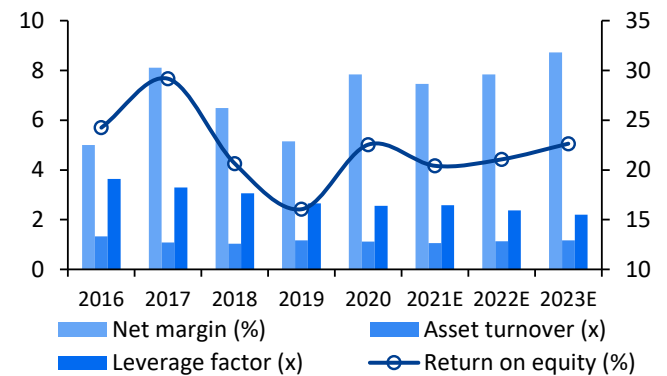
Source: DART, Company

Exhibit 5: ROE/ROCE



Source: DART, Company

Exhibit 6: DuPont Analysis



Source: DART, Company

Profit and Loss Account

(Rs Mn)	FY20A	FY21E	FY22E	FY23E
Revenue	17,082	17,877	20,114	22,636
Total Expense	14,619	15,118	16,899	18,879
COGS	9,762	10,125	11,415	12,870
Employees Cost	1,457	1,659	1,811	1,981
Other expenses	3,400	3,334	3,673	4,029
EBIDTA	2,463	2,759	3,215	3,757
Depreciation	735	872	922	945
EBIT	1,728	1,887	2,294	2,812
Interest	142	188	299	297
Other Income	47	58	83	89
Exc. / E.O. items	163	0	0	0
EBT	1,796	1,757	2,077	2,604
Tax	351	442	519	651
RPAT	1,445	1,315	1,558	1,953
Minority Interest	0	0	0	0
Profit/Loss share of associates	0	0	0	0
APAT	1,317	1,315	1,558	1,953

Balance Sheet

(Rs Mn)	FY20A	FY21E	FY22E	FY23E
Sources of Funds				
Equity Capital	138	138	138	138
Minority Interest	0	0	0	0
Reserves & Surplus	5,869	6,729	7,776	9,178
Net Worth	6,008	6,868	7,915	9,316
Total Debt	4,986	5,912	5,762	5,712
Net Deferred Tax Liability	694	694	694	694
Total Capital Employed	11,688	13,474	14,371	15,722

Applications of Funds

Net Block	6,202	6,780	8,074	7,628
CWIP	440	700	400	400
Investments	1,017	1,017	1,017	1,017
Current Assets, Loans & Advances	8,637	8,450	8,689	10,864
Inventories	4,107	3,408	3,840	4,327
Receivables	3,641	4,034	4,545	5,121
Cash and Bank Balances	156	864	141	1,233
Loans and Advances	0	0	0	0
Other Current Assets	733	145	163	184
Less: Current Liabilities & Provisions	4,608	3,473	3,808	4,186
Payables	3,717	2,630	2,965	3,343
Other Current Liabilities	891	843	843	843
		<i>sub total</i>		
Net Current Assets	4,028	4,977	4,881	6,678
Total Assets	11,688	13,474	14,371	15,722

E – Estimates

Important Ratios

Particulars	FY20A	FY21E	FY22E	FY23E
(A) Margins (%)				
Gross Profit Margin	42.9	43.4	43.3	43.1
EBIDTA Margin	14.4	15.4	16.0	16.6
EBIT Margin	10.1	10.6	11.4	12.4
Tax rate	19.5	25.2	25.0	25.0
Net Profit Margin	8.5	7.4	7.7	8.6
(B) As Percentage of Net Sales (%)				
COGS	57.1	56.6	56.7	56.9
Employee	8.5	9.3	9.0	8.8
Other	19.9	18.6	18.3	17.8
(C) Measure of Financial Status				
Gross Debt / Equity	0.8	0.9	0.7	0.6
Interest Coverage	12.1	10.0	7.7	9.5
Inventory days	88	70	70	70
Debtors days	78	82	82	83
Average Cost of Debt	3.3	3.5	5.1	5.2
Payable days	79	54	54	54
Working Capital days	86	102	89	108
FA T/O	2.8	2.6	2.5	3.0
(D) Measures of Investment				
AEPS (Rs)	19.0	19.0	22.5	28.2
CEPS (Rs)	29.6	31.6	35.8	41.9
DPS (Rs)	4.7	5.3	5.9	6.4
Dividend Payout (%)	24.6	27.7	26.0	22.8
BVPS (Rs)	86.8	99.2	114.3	134.6
RoANW (%)	24.7	20.4	21.1	22.7
RoACE (%)	13.1	11.9	13.3	14.9
RoAIC (%)	16.1	15.6	17.1	19.6
(E) Valuation Ratios				
CMP (Rs)	506	506	506	506
P/E	26.6	26.7	22.5	18.0
Mcap (Rs Mn)	35,060	35,060	35,060	35,060
MCap/ Sales	2.1	2.0	1.7	1.5
EV	39,890	40,109	40,681	39,539
EV/Sales	2.3	2.2	2.0	1.7
EV/EBITDA	16.2	14.5	12.7	10.5
P/BV	5.8	5.1	4.4	3.8
Dividend Yield (%)	0.9	1.0	1.2	1.3
(F) Growth Rate (%)				
Revenue	7.2	4.7	12.5	12.5
EBITDA	20.7	12.0	16.5	16.8
EBIT	24.8	9.2	21.6	22.6
PBT	(12.1)	(2.2)	18.2	25.3
APAT	62.9	(0.2)	18.5	25.3
EPS	62.9	(0.2)	18.5	25.3
Cash Flow				
(Rs Mn)	FY20A	FY21E	FY22E	FY23E
CFO	3,121	2,125	2,110	2,451
CFI	(3,051)	(1,706)	(1,876)	(465)
CFF	5	288	(956)	(894)
FCFF	70	419	234	1,986
Opening Cash	81	156	864	141
Closing Cash	156	864	141	1,233

E – Estimates

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