

1 June 2021

Sudarshan Chemicals

Strong Q4, sound revenue assurance; maintaining a Buy

Backed by good demand domestically, in exports and across product categories, Sudarshans' Q4 revenue climbed 28.4% y/y, 13.9% q/q to Rs5.7bn, its highest. Considering its large ongoing expansions, launch of key products in Q2 FY22, leading position and focus on high-margin products, we are upbeat about its future performance. We maintain our stock rating with a higher TP of Rs850 (29x FY23e EPS), earlier Rs650.

EBITDA margin rose y/y. Driven by strong revenue growth in its specialty chemicals (up 28% y/y, 10% q/q) and non-specialty chemicals (43% y/y, 15% q/q) businesses, Sudarshan's Q4FY21 revenue rose a strong 28.4% y/y, 13.9% q/q, to Rs5.7bn. The gross margin contracted 205bps y/y, 74bps q/q, to 42%, on the steep rise in prices of some intermediates. Despite the lower gross margin, the EBITDA margin was higher, up 315bps y/y (though q/q down 55bps) on operating efficiencies and the better absorption of fixed costs. Higher other income and a better margin rocketed PAT 95.7% y/y, 36.4% q/q, to Rs534m.

Guidance. The company expects the proportion of exports to rise in coming years following its ongoing capex plans and sales-force expansion in global markets. It has a strong product pipeline and expects major launches in Q2 FY22. Of its Rs6bn guided-to capex, the company has capitalised Rs2.2bn in FY20 and Rs710m in FY21. It has Rs2.7bn capex in CWIP (Mar'21), expected to be capitalised in FY22. Management intends to invest the balance Rs380m and an added Rs1.35bn on infrastructure development and capacity expansion. Major investments would be for revenue generation, added products and better margins through cost-optimisation and backward-integration measures. At optimum utilisation, it aims to generate Rs10-12bn revenue from capex.

Valuation. We maintain our Buy rating on the stock, with a higher TP of Rs.850, valuing it at 29x FY23e EPS and 15x FY23e EV/EBITDA. **Risks:** Raw-material price fluctuations; unfavourable forex movements.

Key financials (YE Mar)	FY19	FY20	FY21	FY22e	FY23e
Sales (Rs m)	15,930	17,082	18,641	21,326	25,416
Net profit (Rs m)	1,351	1,445	1,411	1,520	2,016
EPS (Rs)	12.6	18.9	20.4	22.0	29.1
P/E (x)	52.5	35.1	32.5	30	22.7
EV / EBITDA (x)	24.2	20.6	17.7	15.1	12.0
P/BV (x)	8.1	7.6	6.2	5.4	4.6
RoE (%)	17.3	22.4	21.0	19.1	21.9
RoCE (%)	10.1	13.4	12.5	11.8	14.4
Dividend yield (%)	0.9	0.9	0.9	1.0	1.3
Net debt / equity (x)	0.6	0.8	0.7	0.7	0.5

Source: Company, Anand Rathi Research

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Rating: **Buy**

Target Price: Rs.850

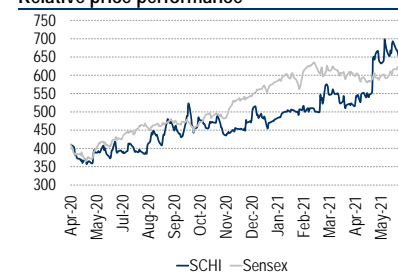
Share Price: Rs.666

Key data	SCHI IN / SDCH.BO
52-week high / low	Rs730 / 364
Sensex / Nifty	51945 / 15579
3-m average volume	\$3.7m
Market cap	Rs46bn / \$635m
Shares outstanding	69m

Shareholding pattern (%)	Mar'21	Dec'20	Sep'20
Promoters	40.0	40.0	42.7
- of which, Pledged	-	-	-
Free float	60.0	60.0	57.3
- Foreign institutions	9.3	9.3	8.1
- Domestic institutions	6.8	6.8	4.3
- Public	43.9	43.9	45.0

Estimates revision (%)	FY22e	FY23e
Sales	4.0	4.1
EBITDA	4.0	5.4
EPS	6.3	7.4

Relative price performance



Source: Bloomberg

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Quick Glance – Financials and Valuations

Fig 1 – Income statement (Rsm)

Year-end: Mar	FY19	FY20	FY21	FY22e	FY23e
Net revenues	15,930	17,082	18,641	21,326	25,416
<i>Growth (%)</i>	<i>19.8</i>	<i>7.2</i>	<i>9.1</i>	<i>14.4</i>	<i>19.2</i>
Direct costs	9,422	9,762	10,605	11,943	14,055
SG&A	4,468	4,857	5,159	5,971	7,117
EBITDA	2,040	2,463	2,878	3,412	4,245
<i>EBITDA margins (%)</i>	<i>12.8</i>	<i>14.4</i>	<i>15.4</i>	<i>16.0</i>	<i>16.7</i>
- Depreciation	656	735	865	1,092	1,171
Other income	70	47	70	64	76
Interest expenses	170	142	179	212	269
PBT	2,007	1,804	1,904	2,172	2,881
<i>Effective tax rate (%)</i>	<i>33.9</i>	<i>19.6</i>	<i>25.9</i>	<i>30.0</i>	<i>30.0</i>
+ Associates / (Minorities)	-	-	-	-	-
Net income	1,351	1,445	1,411	1,520	2,016
Adjusted income	873	1,307	1,411	1,520	2,016
WANS	69	69	69	69	69
FDEPS (Rs / sh)	12.6	18.9	20.4	22.0	29.1
<i>FDEPS growth (%)</i>	<i>3.0</i>	<i>49.7</i>	<i>7.9</i>	<i>7.7</i>	<i>32.6</i>
<i>Gross margins (%)</i>	<i>40.9</i>	<i>42.9</i>	<i>43.1</i>	<i>44.0</i>	<i>44.7</i>

Source: Company, Anand Rathi Research

Fig 2 – Balance sheet (Rsm)

Year-end: Mar	FY19	FY20	FY21	FY22e	FY23e
Share capital	138	138	138	138	138
Net worth	5,677	6,008	7,436	8,500	9,912
Debt	3,671	5,006	5,389	5,889	5,389
Minority interest	-	-	-	-	-
DTL/(Assets)	546	446	490	490	490
Capital employed	9,894	11,460	13,315	14,879	15,790
Net tangible assets	4,542	6,011	5,820	8,179	8,791
Net intangible assets	107	192	260	260	260
Goodwill	-	68	68	68	68
CWIP (tang. & intang.)	240	480	2,783	1,082	300
Investments (strategic)	0	9	13	13	13
Investments (financial)	-	-	-	-	-
Current asset (ex cash)	8,613	9,325	10,812	12,625	14,792
Cash	81	156	238	206	459
Current liabilities	3,690	4,781	6,680	7,555	8,892
Working capital	4,923	4,544	4,132	5,070	5,900
Capital deployed	9,894	11,460	13,315	14,879	15,790
Contingent liabilities	165	200	-	-	-

Source: Company, Anand Rathi Research

Fig 3 – Cash-flow statement (Rsm)

Year-end: Mar	FY19	FY20	FY21	FY22e	FY23e
PBT adj. OI and interest	2,107	1,900	2,012	2,320	3,074
+ Non-cash items	656	735	865	1,092	1,171
Oper. prof. before WC	2,763	2,635	2,878	3,412	4,245
- Incr. / (decr.) in WC	723	(379)	(413)	939	830
Others incl. taxes	638	403	395	652	864
Operating cash-flow	1,402	2,611	2,895	1,822	2,551
- Capex (tang. + intang.)	736	2,597	3,046	1,750	1,000
Free cash-flow	667	14	(152)	72	1,551
Acquisitions					
-Div.(incl. buyback, tax)	500	500	415	456	605
+ Equity raised	-	-	-	-	-
+ Debt raised	(638)	1,335	383	500	(500)
- Fin Investments	(5)	9	4	-	-
-Misc. items (CFI+CFF)	(406)	766	(270)	148	193
Net cash-flow	(61)	75	82	(32)	252

Source: Company, Anand Rathi Research

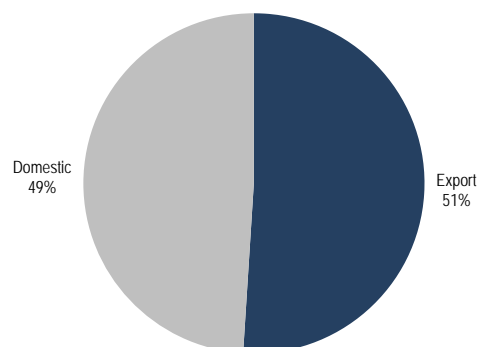
Fig 4 – Ratio analysis

Year-end: Mar	FY19	FY20	FY21	FY22e	FY23e
P/E (x)	52.5	35.1	32.5	30.1	22.7
EV / EBITDA (x)	24.2	20.6	17.7	15.1	12.0
EV / Sales (x)	3.1	3.0	2.7	2.4	2.0
P/B (x)	8.1	7.6	6.2	5.4	4.6
RoE (%)	17.3	22.4	21.0	19.1	21.9
RoCE (%) - after tax	10.1	13.4	12.5	11.8	14.4
RoIC	10.2	13.5	12.7	12.0	14.7
DPS (Rs / sh)	6.0	6.0	6.0	6.6	8.7
Dividend yield (%)	0.9	0.9	0.9	1.0	1.3
Dividend payout (%) - incl. DDT	30.7	28.7	29.4	30.0	30.0
Net debt / equity (x)	0.6	0.8	0.7	0.7	0.5
Receivables (days)	79	78	95	95	91
Inventory (days)	119	154	142	150	152
Payables (days)	94	139	152	155	155
CFO : PAT %	160.6	199.7	205.1	119.8	126.5

Source: Company, Anand Rathi Research

Fig 5 – Price movement


Source: Bloomberg

Fig 6 – Revenue contribution, by area


Source: Company

Result Update

Strong operating performance

Standalone

- Standalone revenue was Rs.5.2bn, up 42.2% y/y, 12.6% q/q, driven by demand traction domestically and in exports.
- The gross margin contracted 548bps y/y, 186bps q/q, to 39.6%, due to rise in several intermediate products prices. The pass-through effect shows after a quarter.
- Despite the sharp gross margin contraction, the EBITDA margin was impacted by just 82bps y/y, 335bps q/q due to lower employee and other expenses, and aided by the better absorption of fixed costs.
- Despite the good, 42%, revenue growth, reported PAT was Rs395m, up only 17% y/y (though q/q down 13%) due to lower margins, higher other expenses and higher tax expenses.
- On adjusting for the Rs107m exceptional gain related to the reversal of the impairment of its investment in its wholly-owned subsidiary, RIECO Industries in Q3 FY21, sequentially PAT grew 4.7%.

Consolidated

- Consolidated Q4FY21 revenue was up 28.4% y/y, 13.9% q/q, to Rs5.7bn, supported by the strong demand pick-up from end-user industries in its home market and in exports.
- The gross margin contracted 205bps y/y, 74bps q/q, to 42%, due to higher input costs and lower export benefits. The margin was impacted by 1% y/y due to the withdrawal of export incentive scheme (MEIS). The government announced a new scheme, the Remission of Duties and Taxes on Exported Products (RoDTEP). The company awaits more clarity, eligibility and products covered under this scheme.
- Despite the lower gross margin, the EBITDA margin rose 315ps y/y (but q/q down 55bps) to 15.2%, aided by lower operating expenses. Thus, absolute EBITDA grew a strong 62% y/y, 9.8% q/q, to Rs.875m.
- Reported PAT grew 95.7% y/y, 36.4% q/q, to Rs.534m, supported by the good operating performance and higher other income, though partially hit by higher finance and tax expenses.

Fig 7 – Financial trend

Particulars (Rs m)	Q4 FY19	Q1 FY20	Q2 FY20	Q3 FY20	Q4 FY20	Q1 FY21	Q2 FY21	Q3 FY21	Q4 FY21	% Y/Y	% Q/Q	FY20	FY21	% Y/Y
Income	4,299	3,964	4,249	4,235	4,491	3,523	4,289	5,064	5,765	28.4	13.9	17,082	18,641	9.1
RM costs	2,588	2,309	2,418	2,412	2,511	1,972	2,394	2,897	3,342	33.1	15.3	9,762	10,605	8.6
Employee expenses	266	322	352	353	411	368	365	429	395	(4.0)	(7.9)	1,457	1,557	6.8
Other expenses	791	687	815	841	1,029	653	853	942	1,154	12.2	22.6	3,400	3,602	6.0
EBITDA	654	646	663	629	540	529	677	796	875	62.0	9.8	2,463	2,877	16.8
Depreciation	169	169	171	178	216	216	219	217	214	(1.1)	(1.4)	735	865	17.7
Interest	51	33	37	38	30	39	51	46	42	39.8	(7.8)	142	179	25.6
Other income	38	9	15	14	10	3	18	26	23	136.7	(8.3)	47	70	49.9
Exceptional Items	(1)	193	-	(22)	-	-	-	-	-	-	-	172	-	NA
PBT	472	647	470	406	303	278	425	559	642	111.6	14.8	1,804	1,904	5.5
Tax	197	193	8	123	30	96	121	168	108	254.6	(35.7)	353	493	39.4
PAT from continuing oper.	275	454	462	283	273	182	303	392	534	95.7	36.4	1,451	1,411	(2.7)
PAT from discontinuing op.	(16)	(27)	-	-	-	-	-	-	-	-	-	(5)	-	NA
Reported PAT	258	427	462	283	273	182	303	392	534	95.7	36.4	1,445	1,411	(2.4)
Reported EPS (Rs)	3.7	6.2	6.7	4.1	3.9	2.6	4.4	5.7	7.7	95.7	36.4	20.9	20.4	(2.4)
Adjusted PAT	259	291	462	298	273	182	303	392	534	95.7	36.4	1,307	1,411	7.9
Adjusted EPS (Rs)	3.7	4.2	6.7	4.3	3.9	2.6	4.4	5.7	7.7	95.7	36.4	18.9	20.4	7.9

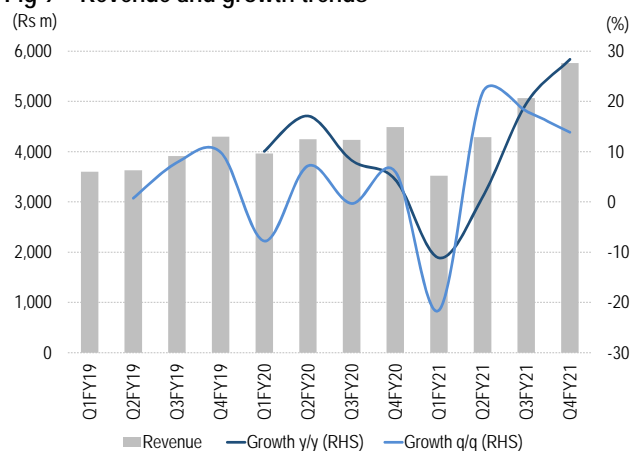
Source: Company, Anand Rathi Research *MI - minority Interest

Fig 8 – Quarterly trend, as percent of sales

Particulars (%)	Q4 FY19	Q1 FY20	Q2 FY20	Q3 FY20	Q4 FY20	Q1 FY21	Q2 FY21	Q3 FY21	Q4 FY21	bps Y/Y	bps Q/Q	FY20	FY21	bps Y/Y
Gross margins	39.8	41.8	43.1	43.0	44.1	44.0	44.2	42.8	42.0	(205)	(74)	42.9	43.1	26
Employee costs	6.2	8.1	8.3	8.3	9.2	10.4	8.5	8.5	6.8	(231)	(161)	8.5	8.4	(18)
Other expenses	18.4	17.3	19.2	19.9	22.9	18.5	19.9	18.6	20.0	(288)	143	19.9	19.3	(58)
EBITDA margins	15.2	16.3	15.6	14.9	12.0	15.0	15.8	15.7	15.2	315	(55)	14.4	15.4	102
Depreciation	3.9	4.3	4.0	4.2	4.8	6.1	5.1	4.3	3.7	(111)	(57)	4.3	4.6	34
Interest	1.2	0.8	0.9	0.9	0.7	1.1	1.2	0.9	0.7	6	(17)	0.8	1.0	13
Other income	0.9	0.2	0.3	0.3	0.2	0.1	0.4	0.5	0.4	19	(10)	0.3	0.4	10
PBT margins	11.0	16.3	11.1	9.6	6.8	7.9	9.9	11.0	11.1	438	9	10.6	10.2	(35)
Effective tax rate	41.8	29.8	1.6	30.3	10.0	34.5	28.6	30.0	16.8	677	(1,319)	19.6	25.9	629
PAT margins	6.0	10.8	10.9	6.7	6.1	5.2	7.1	7.7	9.3	319	153	8.5	7.6	(89)

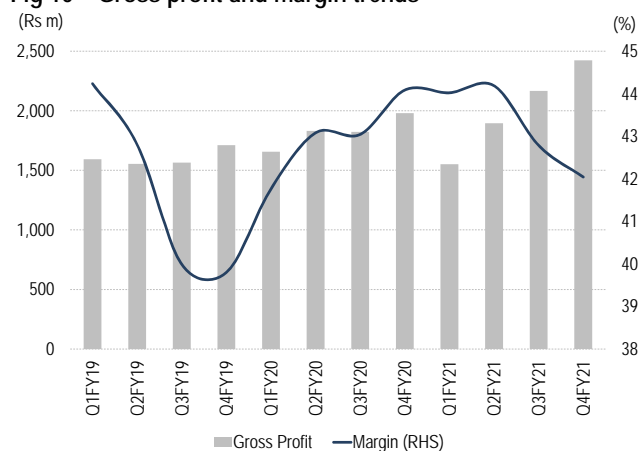
Source: Company, Anand Rathi Research

Fig 9 – Revenue and growth trends



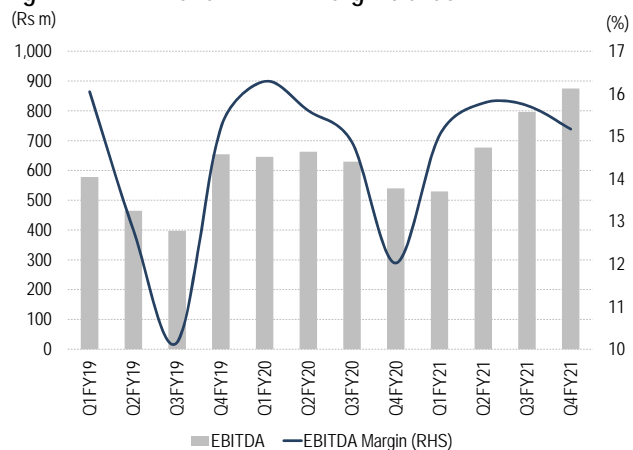
Source: Company, Anand Rathi Research

Fig 10 – Gross profit and margin trends



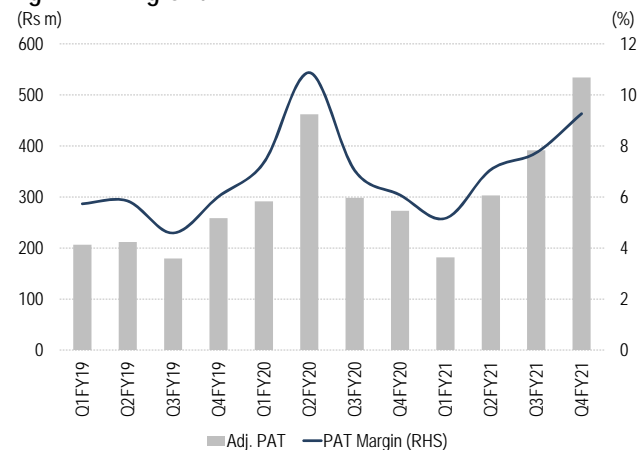
Source: Company, Anand Rathi Research

Fig 11 – EBITDA and EBITDA margin trends



Source: Company, Anand Rathi Research

Fig 12 – PAT growth



Source: Company, Anand Rathi Research

Operating highlights

- The company is seeing good traction in both markets, domestic and exports, and in all its product categories. It expects the growth trend to continue in coming quarters.
- Export demand is rising steadily. Q4 export revenue grew 32% y/y, 20% q/q, to Rs2.6bn. Exports bring ~49% to its revenue.
- Domestic revenue grew 33% y/y, 5% q/q, to Rs2.7bn.
- Pigment revenue grew 33% y/y, 12% q/q, to Rs5.3bn, supported by better end-user-industry demand.
- In FY21, the proportion of revenue from specialty pigments rose to 69% from 64% in FY18.
- Growth in its non-specialty business was good. Revenue here grew 14% y/y to Rs5.5bn in FY21. The company expects steady growth in its non-specialty business following cost competitiveness and optimum utilisation of capacities.
- Other expenses in Q4 rose to Rs1.15bn, up 12.2% y/y, 22.6% q/q, due to the rise in power, freight and shipment costs. Shipment cost went up due to non-availability of containers during the quarter.

Capex

- The company has a current capex plan of Rs6bn. It capitalised Rs2.9bn in the last two years and had Rs2.7bn under CWIP on 31st Mar'21. It expects to capitalise this CWIP and implement the balance capex (Rs380m, of the Rs6bn) in FY22. Further, it plans to invest an added Rs1.35bn in FY22 to develop infrastructure for future growth.
- It expects further revenue of Rs10bn-12bn in the coming 3-4 years.
- Management said major capex would be for revenue generation followed by margin expansion and infrastructure development.
- For future expansions, it has enough land.

Outlook

- Management expects a good performance in coming quarters following the strong recovery in demand, domestically and in exports.
- It is receiving more enquiries at home and from abroad. It expects strong export demand to continue.
- Margins would expand in coming years, backed by the rising proportion of value-added products and greater operating efficiencies.
- The long-term outlook is positive.

Valuation

Change in estimates

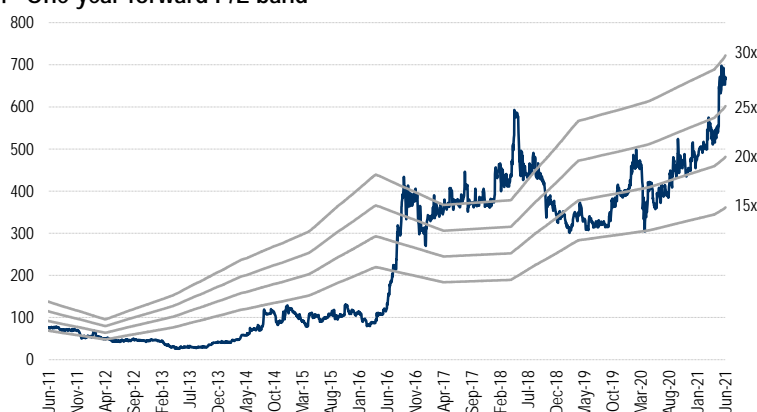
Fig 13 – Change in estimates

(Rs m)	Old estimates		New estimates		Change (%)	
	FY22e	FY23e	FY22e	FY23e	FY22e	FY23e
Revenue	20,502	24,407	21,326	25,416	4.0	4.1
EBITDA	3,280	4,027	3,412	4,245	4.0	5.4
PAT	1,430	1,878	1,520	2,016	6.3	7.4

Source: Anand Rathi Research

We maintain our Buy rating on the stock with a higher target price of Rs.850. At this, the stock is valued at PEs of 39x FY22e and 29x FY23e. On an EV/EBITDA, it is valued at 19x FY22e and 15x FY23e.

Fig 14 –One-year-forward P/E band



Source: Bloomberg, Anand Rathi Research

Risks

- **Fluctuations in raw-material prices.** The company's largest expense (58% of revenue) is raw-material cost. Any rise in such costs due to disruption in China would slash margins and profitability.
- **Foreign currency fluctuation.** ~50% of revenue is generated from exports denominated primarily in dollars and euros. Fluctuations in the value of the rupee against such foreign currencies, to the extent not hedged, would result in gains or losses.
- **Delay in capex implementation**
- **Protracted global slowdown,** leading to a continual deceleration in key consumer sectors.

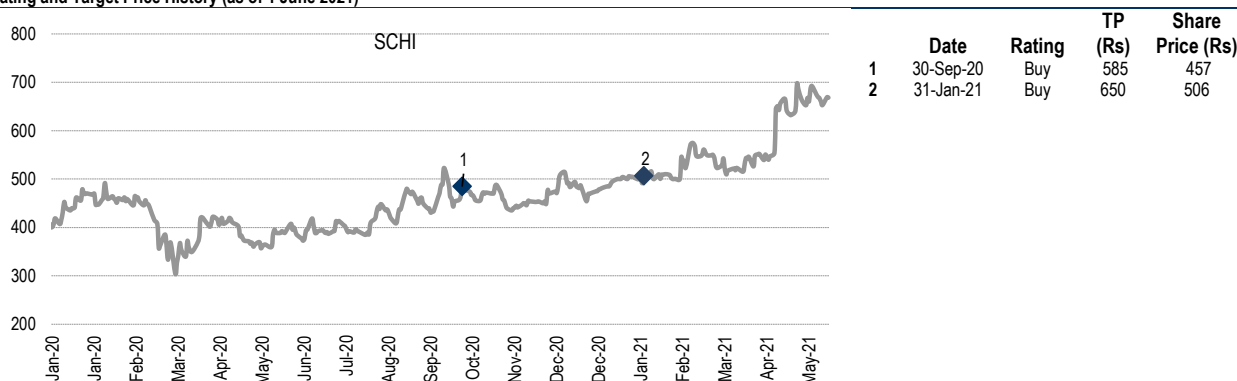
Appendix

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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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