

Upcoming capex offers strong visibility ahead...

About the stock: Established in 1951, Sudarshan Chemical is a leading player in the Indian colour pigment industry with ~35% market share and is also among the top four players globally.

- It has a wide portfolio of 4,000+ varieties of products of Azos, blue and green, high performance pigments (HPPs), effects, pigment preparations and inorganics
- Among end users, coatings industries contribute highest followed by plastics, inks, cosmetics and other applications

Q1FY22 Results: The topline was almost in line with estimates but margins missed owing to higher-than-expected other cost.

- Reported revenue growth of 34.5% YoY to ₹ 473.9 crore, led by higher growth from pigment segment (up 32.8% YoY)
- Gross margins rose 234 bps YoY to ~46.4% while EBITDA margin fell 190 bps YoY to 13.1%, due to higher other operating cost (+74% YoY)
- Adjusted EBITDA was up 28% YoY to ₹ 63.5 crore
- PAT increased 44% YoY to ₹ 26.2 crore owing to lower taxes (up 29.2% vs. 34.5% in Q1FY21)

What should investors do? The stock appreciated at 30% CAGR in last three years.

- We retain **BUY** rating on the back of better growth outlook from speciality pigments

Target Price and Valuation: We value Sudarshan Chemical at 25x P/E FY23E EPS to arrive at a revised target price of ₹ 795/share (earlier ₹ 775/share).

Key triggers for future price performance:

- Upcoming capex bodes well for speciality pigments revenue growth
- Higher share of value added business portfolio to improve margins profile of the business
- Allocation of incremental FCF towards organic/inorganic growth likely to expand return ratios further

Alternate Stock Idea: Apart from Sudarshan Chemical, in our chemical coverage we also like Neogen Chemical.

- For Neogen Chemical, future revenue growth is expected to be driven by increasing custom synthesis opportunity
- BUY with a target price of ₹ 1095

SUDARSHAN

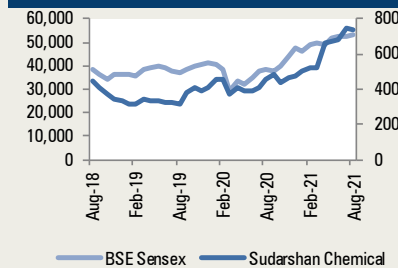
Particulars

| Particular | Amount |
|---------------------------|---------|
| Market cap (₹ Crore) | 4,447 |
| FY21 Total Debt (₹ Crore) | 618 |
| FY21 Cash & Inv (₹ Crore) | 24 |
| EV (₹ Crore) | 5,041 |
| 52 Week H/L | 792/407 |
| Equity Capital (₹ Crore) | 13.8 |
| Face Value (₹) | 2 |

Shareholding pattern

| in % | Sept-20 | Dec-20 | Mar-21 | Jun-21 |
|----------|---------|--------|--------|--------|
| Promoter | 42.7 | 40.0 | 40.0 | 39.6 |
| DII | 4.2 | 6.7 | 9.0 | 9.3 |
| FII | 8.1 | 9.3 | 9.4 | 8.8 |
| Others | 45.0 | 43.9 | 41.6 | 42.4 |

Price Chart



Recent event & key risks

- Revival in the domestic pigment demand witnessed
- Key Risk:** (i) Slowdown in end user demand ii) Higher RMAT prices and inability to pass on to impact gross margins

Research Analyst

Mitesh Shah
mitesh.shah@icicisecurities.com

Dhavan Shah
dhavan.shah@icicisecurities.com

Siddhant Khandekar
siddhant.khandekar@icicisecurities.com

Key Financial Summary

| (₹ Crore) | FY19 | FY20 | FY21 | 5 year CAGR (FY16-21) | FY22E | FY23E | 2 year CAGR (FY21-23E) |
|--------------------|---------|---------|---------|-----------------------|---------|---------|------------------------|
| Net Revenue | 1,593.1 | 1,708.2 | 1,864.1 | 5.9% | 2,182.2 | 2,530.6 | 16.5% |
| EBITDA | 204.1 | 246.3 | 287.8 | 11.1% | 355.9 | 422.6 | 21.2% |
| EBITDA Margins (%) | 12.8% | 14.4% | 15.4% | | 16.3% | 16.7% | |
| Adj.PAT | 132.8 | 145.1 | 141.1 | 15.1% | 181.4 | 219.6 | 24.7% |
| Adj. EPS (₹) | 8.7 | 18.5 | 20.4 | | 26.2 | 31.7 | |
| EV/EBITDA | 24.3x | 20.0x | 17.2x | | 13.7x | 11.4x | |
| P/E | 33.5x | 30.7x | 31.5x | | 24.5x | 20.3x | |
| ROE (%) | 10.7 | 21.3 | 19.0 | | 20.7 | 21.1 | |
| ROCE (%) | 14.4 | 15.2 | 15.2 | | 18.2 | 19.7 | |

Key takeaways of recent quarter & conference call highlight

Q1FY22 Results: Higher growth from speciality and non-speciality pigments led overall growth

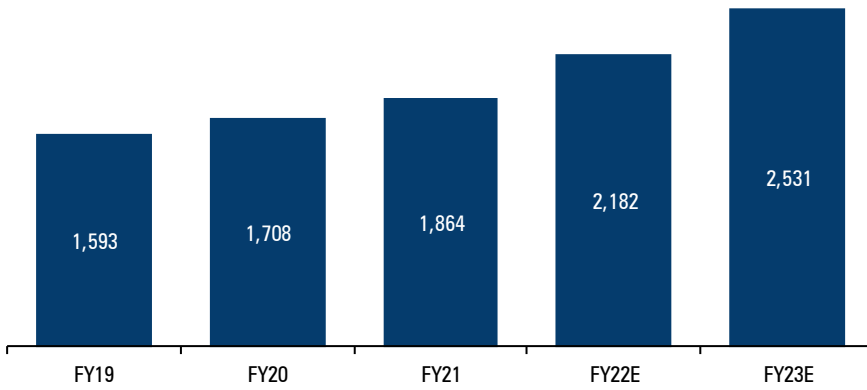
- **Pigment business:** Revenues were up 32.8% YoY to ₹ 453 crore, led by better growth from domestic pigment due to low base. Revenue from domestic pigment was up 68% YoY to ₹ 203 crore while exports were up 13% YoY to ₹ 250 crore. The revenue from speciality pigment increased 32% YoY to ₹ 318 crore while the same from non-speciality pigment was up 33% YoY to ₹ 135 crore
- **Operating margins remain soft:** Although there has been an improvement in gross margins by 240 bps YoY to 46.4%, OPM contracted 190 bps YoY to 13% owing to higher than expected other cost. Freight and power cost were higher, impacting the operational performance for the quarter. However, the same is expected to be passed on with one quarter lag impact.

Q1FY22 Earnings Conference Call highlights

- Due to lockdown in the domestic market, there had been impact on the plastic and coating segments
- Multiple products are planned to be launched during H2FY22, which should support growth, going ahead
- Due to lockdown in Q1, order execution at RIECO was impacted. However decent order backlog affirms the positive outlook for the business in the rest of the year
- Higher freight and power cost impacted other expenses, which, in turn, led to a subdued operational performance. The inflation in power and freight cost is expected to be passed on with one quarter lag impact
- **RODETP** (Remission of Duties or Taxes on Export Products) has been implemented from January 2021 but the rates have not been decided yet
- **Capex:** It is on track to complete capex this fiscal. It expects to do a capex of ₹ 120 crore by the end of Q2 while balance capex of ₹ 180-200 crore would be done by Q3FY22
- **Mahad plant** – The activity was impacted for around two weeks, which has resumed from this week. There had been some sales loss during this period

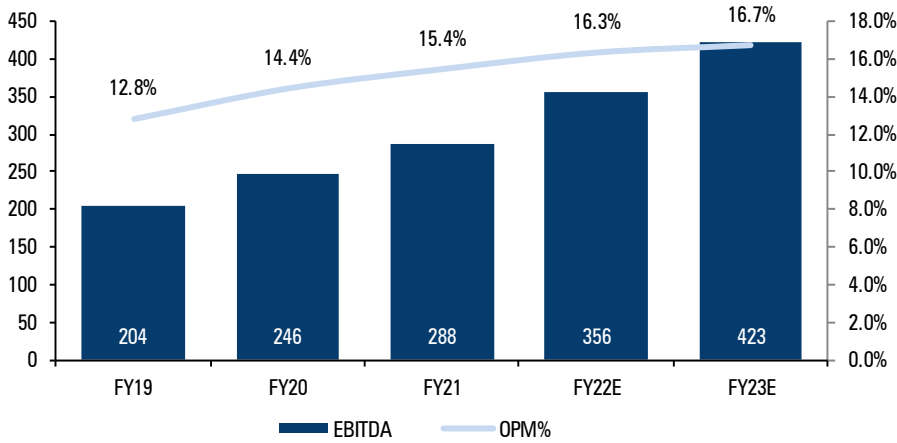
Financial story in charts....

Exhibit 1: Revenue trend (₹ crore)



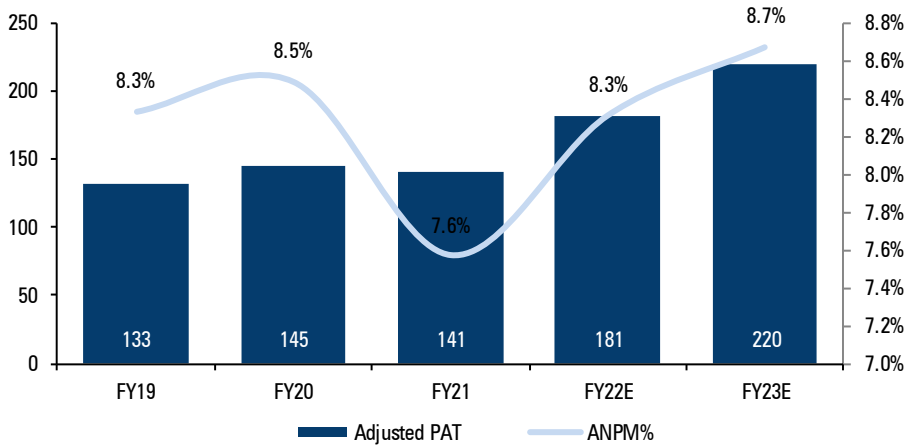
Source: Company, ICICI Direct Research

Exhibit 2: EBITDA (₹ crore) and OPM (%) trend



Source: Company, ICICI Direct Research

Exhibit 3: PAT growth trend (₹ crore)



Source: Company, ICICI Direct Research

Financial summary

| Exhibit 4: Profit and loss statement | | | | |
|--------------------------------------|--------------|--------------|--------------|--------------|
| | ₹ crore | | | |
| (Year-end March) | FY20 | FY21 | FY22E | FY23E |
| Total Operating Income | 1,708.2 | 1,864.1 | 2,182.2 | 2,530.6 |
| Growth (%) | 7.2 | 9.1 | 17.1 | 16.0 |
| Raw Material Expenses | 976.2 | 1,060.5 | 1,185.2 | 1,366.5 |
| Gross Profit | 732.0 | 803.7 | 997.0 | 1,164.1 |
| Gross Profit Margins (%) | 42.9 | 43.1 | 45.7 | 46.0 |
| Employee Expenses | 145.8 | 155.7 | 185.8 | 210.0 |
| Other Expenditure | 340.0 | 360.2 | 455.3 | 531.4 |
| Total Operating Expenditure | 1,461.9 | 1,576.4 | 1,826.3 | 2,108.0 |
| EBITDA | 246.3 | 287.8 | 355.9 | 422.6 |
| Growth (%) | 20.7 | 16.8 | 23.7 | 18.7 |
| Interest | 14.2 | 17.9 | 18.9 | 18.9 |
| Depreciation | 73.5 | 86.5 | 84.1 | 106.3 |
| Other Income | 4.7 | 7.0 | 3.2 | 12.7 |
| PBT before Exceptional Item | 163.2 | 190.4 | 256.2 | 310.1 |
| Less: Exceptional Items | -17.2 | 0.0 | 0.0 | 0.0 |
| PBT after Exceptional Items | 180.4 | 190.4 | 256.2 | 310.1 |
| Total Tax | 35.4 | 49.3 | 74.8 | 90.5 |
| PAT before MI | 145.1 | 141.1 | 181.4 | 219.6 |
| PAT | 145.1 | 141.1 | 181.4 | 219.6 |
| Growth (%) | 9.3 | -2.7 | 28.6 | 21.0 |
| EPS (Adjusted) | 18.5 | 20.4 | 26.2 | 31.7 |

Source: Company, ICICI Direct Research

| Exhibit 5: Cash flow statement | | | | |
|-------------------------------------|---------------|---------------|---------------|---------------|
| | ₹ crore | | | |
| (Year-end March) | FY20 | FY21 | FY22E | FY23E |
| Profit/(Loss) after taxation | 101.7 | 151.6 | 181.4 | 219.6 |
| Add: Depreciation & Amortiza | 73.5 | 86.5 | 84.1 | 106.3 |
| Net Increase in Current Asset | -51.0 | -176.1 | -58.4 | -154.3 |
| Net Increase in Current Liabili | 101.8 | 85.4 | 79.1 | 86.3 |
| Others | 36.6 | 17.8 | 18.9 | 18.9 |
| CF from Operating activities | 262.6 | 165.2 | 305.1 | 276.8 |
| Investments | 0.0 | 0.0 | 0.0 | 0.0 |
| (Purchase)/Sale of Fixed Ass | -253.8 | -269.6 | -159.5 | -150.0 |
| Others | 41.4 | 4.2 | 0.3 | 0.3 |
| CF from Investing activities | -212.4 | -265.4 | -159.2 | -149.7 |
| (inc)/Dec in Loan | 75.1 | 126.3 | 0.0 | 0.0 |
| Dividend & Dividend tax | -100.2 | -0.4 | -46.7 | -56.6 |
| Other | -14.2 | -17.4 | -18.9 | -18.9 |
| CF from Financing activities | -39.4 | 108.5 | -65.6 | -75.5 |
| Net Cash Flow | 10.9 | 8.2 | 80.2 | 51.6 |
| Cash and Cash Equivalent | 4.8 | 15.6 | 23.8 | 104.1 |
| Cash | 15.6 | 23.8 | 104.1 | 155.7 |
| Free Cash Flow | 8.8 | -104.4 | 145.6 | 126.8 |

Source: Company, ICICI Direct Research

| Exhibit 6: Balance sheet | | | | |
|-------------------------------|----------------|----------------|----------------|----------------|
| | ₹ crore | | | |
| (Year-end March) | FY20 | FY21 | FY22E | FY23E |
| Equity Capital | 13.9 | 13.8 | 13.8 | 13.8 |
| Reserve and Surplus | 586.9 | 729.7 | 864.4 | 1,027.4 |
| Total Shareholders funds | 600.8 | 743.6 | 878.3 | 1,041.3 |
| Total Debt | 498.6 | 535.0 | 535.0 | 535.0 |
| Deferred Tax Liability | 50.1 | 52.9 | 53.9 | 55.0 |
| Long-Term Provisions | 15.7 | 23.9 | 24.4 | 24.9 |
| Other Non Current Liabilities | 3.6 | 15.5 | 15.9 | 16.2 |
| Source of Funds | 1,168.8 | 1,370.9 | 1,507.4 | 1,672.3 |
| Gross Block - Fixed Assets | 870.2 | 939.9 | 1,368.4 | 1,518.4 |
| Accumulated Depreciation | 245.3 | 331.8 | 415.9 | 522.2 |
| Net Block | 624.9 | 608.0 | 952.4 | 996.2 |
| Capital WIP | 48.0 | 278.3 | 9.3 | 9.3 |
| Goodwill | 0.0 | 6.8 | 6.8 | 6.8 |
| Fixed Assets | 672.8 | 893.2 | 968.6 | 1,012.3 |
| Investments | 0.9 | 1.3 | 1.3 | 1.3 |
| Other non-Current Assets | 92.2 | 77.3 | 78.9 | 80.5 |
| Inventory | 410.7 | 411.6 | 478.3 | 554.6 |
| Debtors | 364.1 | 484.7 | 474.2 | 549.8 |
| Other Current Assets | 73.3 | 111.5 | 113.7 | 116.0 |
| Cash | 15.6 | 23.8 | 104.1 | 155.7 |
| Total Current Assets | 863.7 | 1,031.6 | 1,170.3 | 1,376.2 |
| Creditors | 371.7 | 441.1 | 516.4 | 598.9 |
| Provisions | 7.1 | 2.3 | 2.3 | 2.4 |
| Other Current Liabilities | 82.1 | 189.0 | 192.8 | 196.7 |
| Total Current Liabilities | 460.8 | 632.5 | 711.6 | 797.9 |
| Net Current Assets | 402.8 | 399.1 | 458.7 | 578.3 |
| Application of Funds | 1,168.8 | 1,370.9 | 1,507.4 | 1,672.3 |

Source: Company, ICICI Direct Research

| Exhibit 7: Key ratios | | | | |
|-----------------------------|-------|-------|-------|-------|
| (Year-end March) | FY20 | FY21 | FY22E | FY23E |
| Per share data (₹) | | | | |
| Reported EPS | 21.0 | 20.4 | 26.2 | 31.7 |
| Cash EPS | 10.9 | 15.1 | 19.5 | 23.5 |
| BV per share | 86.8 | 107.4 | 126.9 | 150.4 |
| Cash per Share | 2.3 | 3.4 | 15.0 | 22.5 |
| Dividend per share | 7.6 | 5.3 | 6.8 | 8.2 |
| Operating Ratios (%) | | | | |
| Gross Profit Margins | 42.9 | 43.1 | 45.7 | 46.0 |
| EBITDA margins | 14.4 | 15.4 | 16.3 | 16.7 |
| PAT Margins | 7.5 | 7.6 | 8.3 | 8.7 |
| Cash Conversion Cycle | 86.1 | 89.1 | 72.9 | 72.9 |
| Asset Turnover | 2.0 | 2.0 | 1.6 | 1.7 |
| EBITDA conversion Rate | 106.6 | 57.4 | 85.7 | 65.5 |
| Return Ratios (%) | | | | |
| RoE | 21.3 | 19.0 | 20.7 | 21.1 |
| RoCE | 15.2 | 15.2 | 18.2 | 19.7 |
| RoIC | 15.6 | 18.8 | 19.5 | 21.0 |
| Valuation Ratios (x) | | | | |
| P/E | 30.7 | 31.5 | 24.5 | 20.3 |
| EV / EBITDA | 20.0 | 17.2 | 13.7 | 11.4 |
| EV / Net Sales | 2.9 | 2.7 | 2.2 | 1.9 |
| Market Cap / Sales | 2.6 | 2.4 | 2.0 | 1.8 |
| Price to Book Value | 7.4 | 6.0 | 5.1 | 4.3 |
| Solvency Ratios | | | | |
| Debt / EBITDA | 2.0 | 1.9 | 1.5 | 1.3 |
| Debt / Equity | 0.8 | 0.7 | 0.6 | 0.5 |
| Current Ratio | 1.8 | 1.6 | 1.5 | 1.5 |

Source: Company, ICICI Direct Research

Exhibit 8: ICICI Direct coverage universe (Chemicals)

| Company | CMP | | | M Cap | EPS (₹) | | | P/E (x) | | | EV/EBITDA (x) | | | RoCE (%) | | | RoE (%) | | |
|--------------------|------|-------|--------|--------|---------|-------|-------|---------|-------|-------|---------------|-------|-------|----------|-------|-------|---------|-------|-------|
| | (₹) | TP(₹) | Rating | (₹ Cr) | FY21 | FY22E | FY23E | FY21 | FY22E | FY23E | FY21 | FY22E | FY23E | FY21 | FY22E | FY23E | FY21 | FY22E | FY23E |
| PI Industries | 3316 | 3,855 | Buy | 50,403 | 48.6 | 59.2 | 77.1 | 68.3 | 56.0 | 43.0 | 47.8 | 39.2 | 30.1 | 17.2 | 18.6 | 20.4 | 13.8 | 14.6 | 16.1 |
| Aarti Industries | 853 | 960 | Buy | 30,927 | 30.2 | 72.8 | 60.0 | 55.2 | 22.9 | 27.8 | 32.2 | 23.5 | 18.0 | 10.7 | 12.7 | 15.3 | 15.0 | 16.3 | 18.7 |
| Sumitomo Chemical | 431 | 505 | Buy | 21,513 | 6.9 | 8.5 | 10.1 | 62.3 | 50.6 | 42.6 | 43.1 | 35.1 | 29.0 | 29.8 | 29.3 | 28.1 | 22.4 | 22.1 | 21.2 |
| Vinati Organics | 1954 | 2,300 | Buy | 20,086 | 26.2 | 40.2 | 44.3 | 74.6 | 48.6 | 44.1 | 56.4 | 36.2 | 32.3 | 21.7 | 29.4 | 27.1 | 17.4 | 22.1 | 20.4 |
| Tata Chemical | 824 | 925 | Hold | 20,997 | 10.1 | 39.1 | 42.6 | 81.9 | 21.1 | 19.3 | 15.8 | 10.0 | 8.3 | 4.1 | 7.1 | 7.7 | 1.8 | 6.6 | 6.9 |
| Navin Fluorine | 3720 | 3,712 | Hold | 18,413 | 45.0 | 53.0 | 73.1 | 82.6 | 70.2 | 50.9 | 57.5 | 49.7 | 33.9 | 21.0 | 19.0 | 22.6 | 13.6 | 14.2 | 17.0 |
| Rallis India | 320 | 400 | Buy | 6,215 | 11.4 | 12.7 | 16.0 | 28.1 | 25.1 | 20.0 | 18.4 | 16.8 | 13.0 | 18.0 | 17.7 | 20.0 | 13.9 | 13.9 | 15.3 |
| Sudarshan chemical | 642 | 795 | Buy | 4,447 | 20.4 | 26.2 | 31.7 | 31.5 | 24.5 | 20.3 | 17.2 | 13.7 | 11.4 | 15.2 | 18.2 | 19.7 | 19.0 | 20.7 | 21.1 |
| Neogen Chemicals | 897 | 1,095 | Buy | 2,093 | 13.4 | 18.8 | 28.8 | 66.8 | 47.7 | 31.2 | 35.6 | 26.7 | 19.4 | 15.1 | 16.5 | 20.1 | 17.1 | 19.8 | 23.7 |

Source: Bloomberg, ICICI Direct Research

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Buy: >15%

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Reduce: -15% to -5%;

Sell: <-15%



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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