

# Stock Idea

Sector: Consumer Goods

August 23, 2021

## Indigo Paints Ltd



Paint your portfolio bright

# Sharekhan

by BNP PARIBAS



Powered by Sharekhan's 3R Research Philosophy



## 3R MATRIX

	+	=	-
Right Sector (RS)	✓	■	■
Right Quality (RQ)	✓	■	■
Right Valuation (RV)	✓	■	■

+ Positive = Neutral - Negative

## Reco/View

Reco:	Buy
CMP:	Rs. 2,431
Price Target:	Rs. 3,305

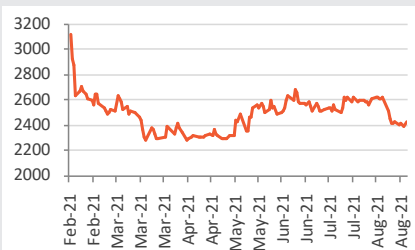
## Company details

Market cap:	Rs. 11,564 cr
52-week high/low:	Rs. 3,348/2,192
NSE volume: (No of shares)	0.6 lakh
BSE code:	543258
NSE code:	INDIGOPNTS
Free float: (No of shares)	2.2 cr

## Shareholding (%)

Promoters*	54.0
FII	40.3
DII	3.2
Others	2.52

## Price chart



## Price performance

(%)	1m	3m	6m	12m
Absolute	-7.4	-1.3	-4.4	-
Relative to Sensex	-13.4	-12.9	-15.6	-

Sharekhan Research, Bloomberg

## Summary

- We initiate coverage on Indigo Paints Ltd (IPL) with a Buy and assign a target price of Rs. 3,305. Differentiated business model, excellent return profile and strong structural growth outlook will keep valuation at a premium of 60x/44x its FY2023/24E earnings versus peers.
- With a differentiated product portfolio and bottom-up approach, IPL is emerging as one of India's fastest growing paints companies. Revenues and PAT clocked a CAGR of 22% and 71% over FY2018-21.
- Gross margins are highest among peers at ~48% led by IPL's locational advantage and healthy mix of revenues from differentiated products.
- Better working capital management has kept net working capital cycle low at 13-14 days. Operating cash flows (OCF) improved from Rs. 42.8 crore to Rs. 101.4 crore over FY2019-21.

Indigo Paints Limited (IPL) is an emerging player, which has created a niche for itself in the highly competitive paints industry by launching differentiated products, creating brand equity through one prominent brand 'Indigo' and follow bottoms-up approach to expand its distribution in the domestic market. It has market share of 2% but has strong potential to improve it in the coming years. IPL was the first among its competitors to introduce coatings for ceilings, tiles and floors, with competitors entering this space only now. Further, differentiated products helped IPL expand its dealers/distribution network into various markets. Differentiated products contribute ~30% of overall revenues and fetch higher margins compared to other products. IPL has used a bottom-up approach to expand its base in a particular market. To create demand for its differentiated products, IPL initially taps tier-3 and tier-4 cities and rural areas, where brand penetration is easier and dealers have a greater ability to influence customers' purchase decisions. IPL subsequently leverages on this network to engage with dealers in tier-1/tier-2 cities and metros to expand its base. It has presence in 27 states and is focusing on improving penetration in these states. The company has also introduced tinting machines in target markets to increase sales of emulsions. IPL's current dealer reach is 16% of the top player and 40% of second-largest paint player in India. Revenue per tinting machine is lowest at Rs. 14.5 lakh versus its peers, indicating a wide scope for growth. Further the company has a unique brand strategy where all products are bundled under one brand 'Indigo' which is promoted by brand ambassador – Mahendra Singh Dhoni who has a pan-India appeal. Being an emerging player, the company spends heavily on advertising ("Rs. 77 crore in FY2021, second only to the top player) in the past few years which helped it to establish strong brand equity. This differentiated approach for distribution expansion and higher brand investments will help it to promote conventional paint products in the coming years. A differentiated business model aided the company to achieve strong revenue and PAT growth of 22% and 71% over FY2018-21 with the highest gross margins of ~48% among peers. OPM improved to 16.9% in FY2021 from 6.5% in FY2018 (management targets to achieve OPM of ~18.5% in FY022). Differentiated product portfolio and calibrated pricing strategy helped the company sail through the uncertain business environment caused by second wave of COVID-19 and higher input prices by posting relative stable performance in Q1FY2022. With easing of lockdown norms and raw material prices correcting from its high, the company expects much better performance in the quarters ahead. The rising urbanization, higher willingness to spend behind home improvement in tier 2 and 3 towns, strong traction to differentiate products and market share gains would help IPL to achieve faster recovery in the coming years. Scale up in the business will help the operating margins to further improve and reach at ~22% in FY2024. Better working capital management aided net working capital days standing low at 13-14 days. The operating cash flows (OCF) improved from Rs. 42.8 crore to Rs. 101.4 crore over FY2019-21 and with sustain scale up margins, cash flows are expected to further improve in the coming years.

## Our Call

**View– Initiate with Buy assigning a Price Target of Rs. 3,305:** We expect IPL's revenue and PAT to grow at a CAGR of 31% and 55% over FY2021-24E driven by strong expansion in dealer network, improving market share and margin expansion. The company has strong balance sheet with stable working capital management and strong operating cash flows (average OCF to EBITDA ratio stood at 78% for past three years). Moreover, its return ratios are expected to improve strongly in the coming years (RoE and RoCE to stand at 26% and 34% in FY2024). The stock is currently trading at 60.4x its FY2023E EPS and 44.2x its FY2024E EPS (and 41.0x/30.1x its FY2023E/24E EV/EBIDTA). Differentiated business model with industry leading gross margins, sustained focus on improving market share, strong return profile and the structural growth story of the paints industry will keep valuations at a premium as compared to close peers. We initiate our coverage on Indigo Paints with a Buy recommendation and price target (PT) of Rs. 3,305 (valuing the stock at 60x its FY2024E earnings).

## Key risk

Late demand recovery or delay in expanding the distribution base or sustained increase in prices of crude oil and crude derivatives would act as a key risk to our earnings estimates.

## Valuation (standalone)

Particulars	Rs cr			
	FY21	FY22E	FY23E	FY24E
Revenue	723	968	1,258	1,624
OPM (%)	16.9	18.5	21.6	22.3
Adjusted PAT	71	127	191	262
% Y-o-Y growth	48.2	79.8	50.3	36.8
Adjusted EPS (Rs.)	14.9	26.8	40.2	55.0
P/E (x)	-	90.8	60.4	44.2
P/B (x)	20.5	16.7	13.1	10.1
EV/EBIDTA (x)	92.0	62.5	41.0	30.1
RoNW (%)	18.6	20.3	24.3	25.8
RoCE (%)	23.3	25.9	31.4	33.6

Source: Company, Sharekhan estimates

## Executive Summary

### 3R Research Positioning Summary

#### ■ Right Sector

Low per capita consumption, improving demographics, reduced re-painting cycle and higher spends on home improvement will drive demand for paints.

#### ■ Right Quality

Emerging paints company with differentiated portfolio, experienced management supported by a strong balance sheet.

#### ■ Right Valuation

Structural growth story of paints industry, differentiated growth strategies with strong growth prospects makes a good investment fit.

### Valuation and return potential

- **Valuations:** IPL recently listed on bourses and the stock is currently trading at 60.4x its FY2023E EPS and 41x its FY2023E EV/EBIDTA.
- **Valuations to remain at a premium:** Differentiated business model with industry-leading gross margins, sustained focus on improving market share, strong return profile and a steady structural growth outlook for paints industry will keep valuations at a premium.

### Key Catalysts for growth

#### Long-term triggers

- Low penetration with dealership network standing at 16% of large players and a lower tinting machine to dealer network ratio of 38% heightens the scope for growth in the long run.
- Sustained product additions in different categories will help IPL remain competitive.

#### Medium Term Triggers

- Consistent shift from unorganised to organised products (especially in tier-3/4 towns) will help drive consistent volume growth.
- Higher gross margins and scale up in revenues would help OPM expand strongly in the coming years.

#### Key Risks

Delayed volume recovery due to resurgence in COVID-19 cases and a sustained surge in crude oil prices would act as a risk to earnings estimates.

### Earnings and Balance sheet highlights

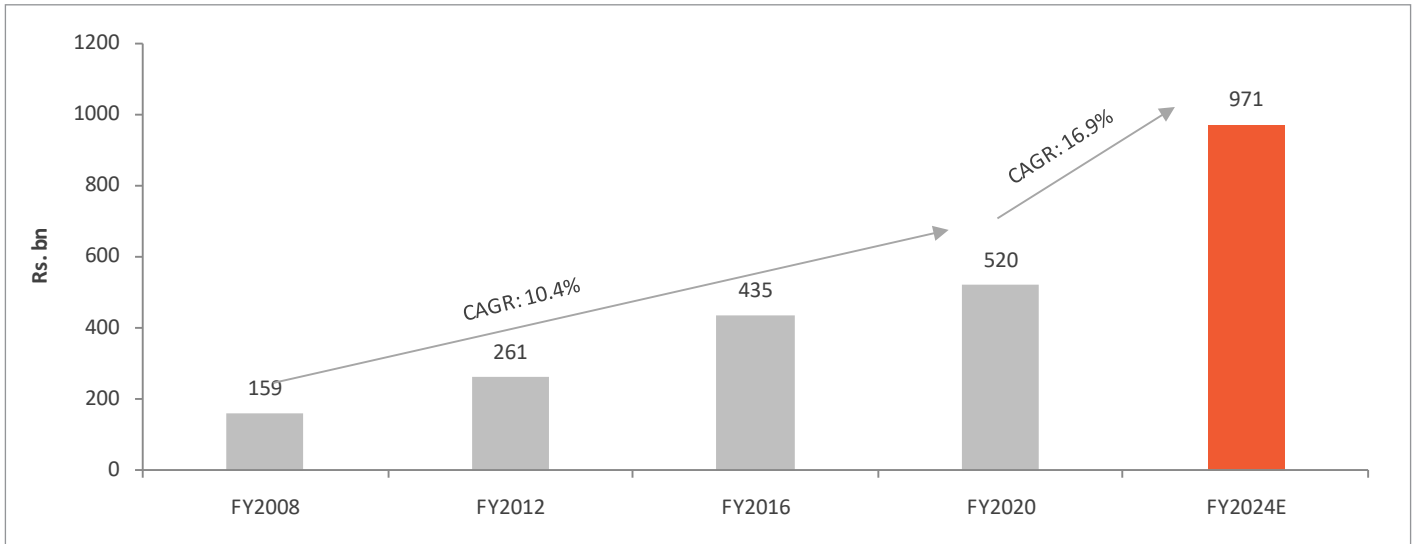
- **Consistent earnings growth:** Revenues and PAT grew at a CAGR of 22% and 71%, respectively, over FY2018-21.
- **Differentiated products:** These constitute ~30% of domestic revenues; have higher margins helping IPL post industry leading gross margins of 48%.
- **Strong balance sheet:** Zero debt on books; stable working capital with operating cash cycle of 13-14 days; operating cash flow improved to Rs. 101.4 crore in FY2021 from Rs. 42.8 crore in FY2019.

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### Why we like paints industry – Strong demand for decorative paints to be key growth lever

The Indian paints industry is correlated to GDP and is growing at 2x the GDP, led by strong demand in the decorative paints. The industry has registered a CAGR of ~10.4% during FY2008 to FY2020. Rising income levels, rapid urbanisation, shift from unorganised products (especially at the bottom of pyramid) and improving penetration for decorative paints are some of the key growth drivers. The industry size is expected to grow to ~Rs. 971 billion by 2024.

#### Paints industry to clock 17% CAGR over FY2020-24

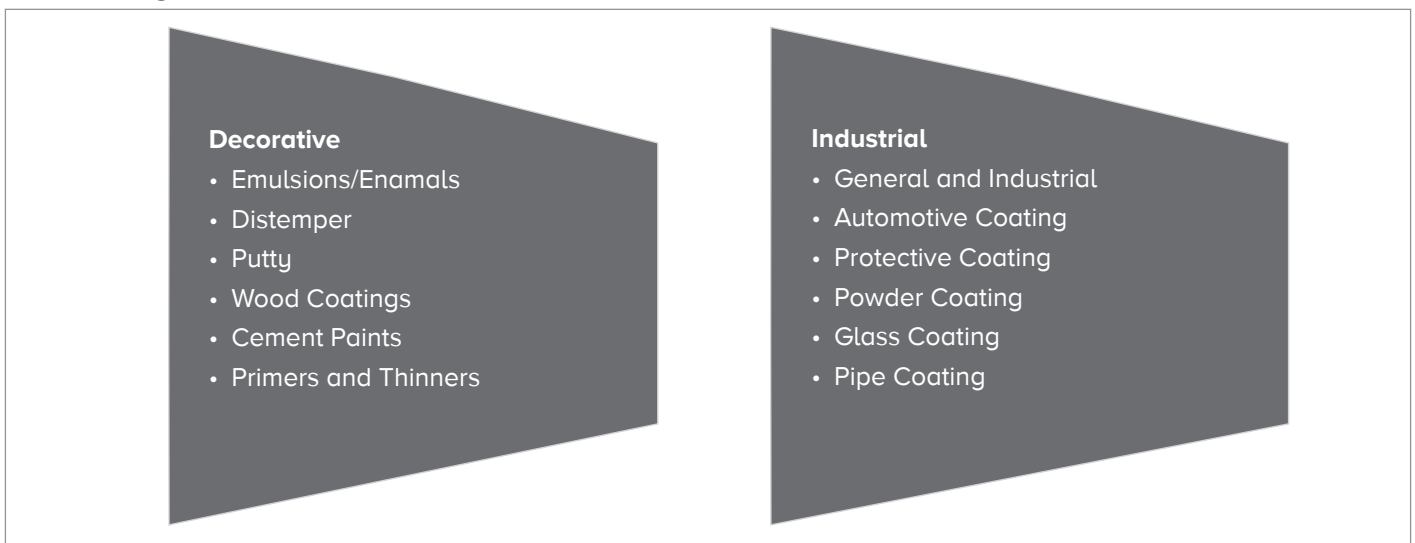


Source: Company; Sharekhan Research

#### Decorative paint industry grew at CAGR of 11.5% over 2014-19

The domestic paints industry comprises the decorative and industrial segments. Decorative paints constitute more than 75% of the market and are used mainly in the real estate sector for exterior and interior wall paints, wood finishes, enamels, undercoats such as primers, putties, etc. The industrial segment refers to paints that go into protective coatings largely for varied substrates like iron, galvanised iron, mild steel, aluminium, chimneys, etc. This comprises automotive, marine, packaging, powder, protective, floor and other general industrial coatings and accounts for the balance 25% of the paint market.

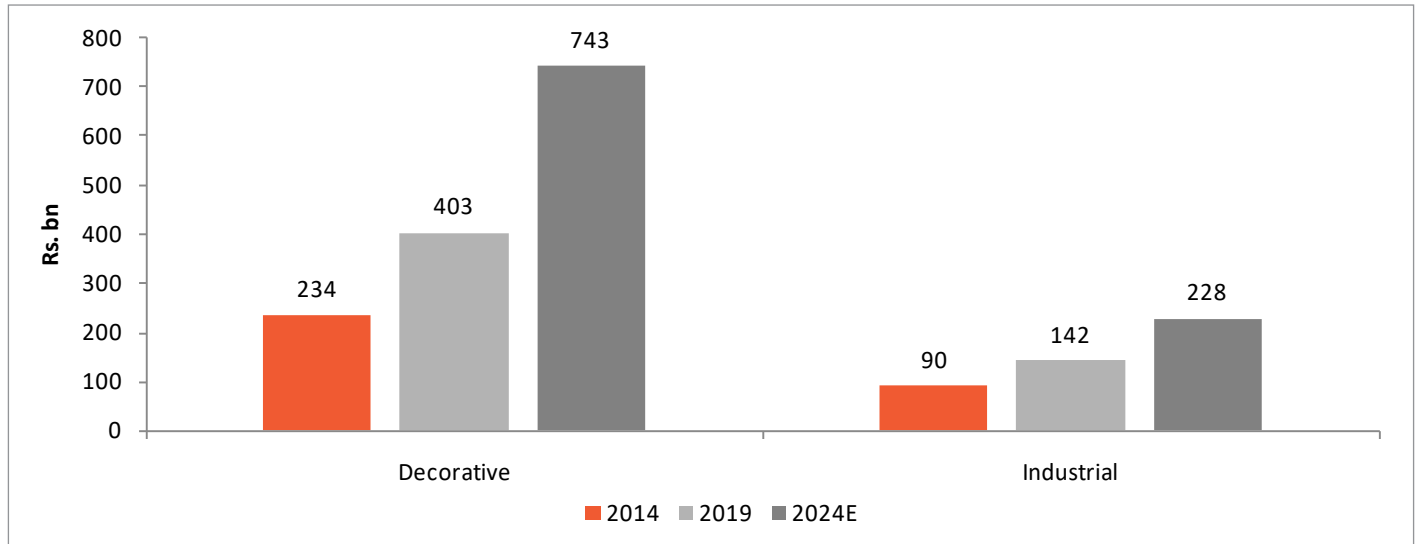
#### Paints industry – Broad structure



Source: Company; Sharekhan Research

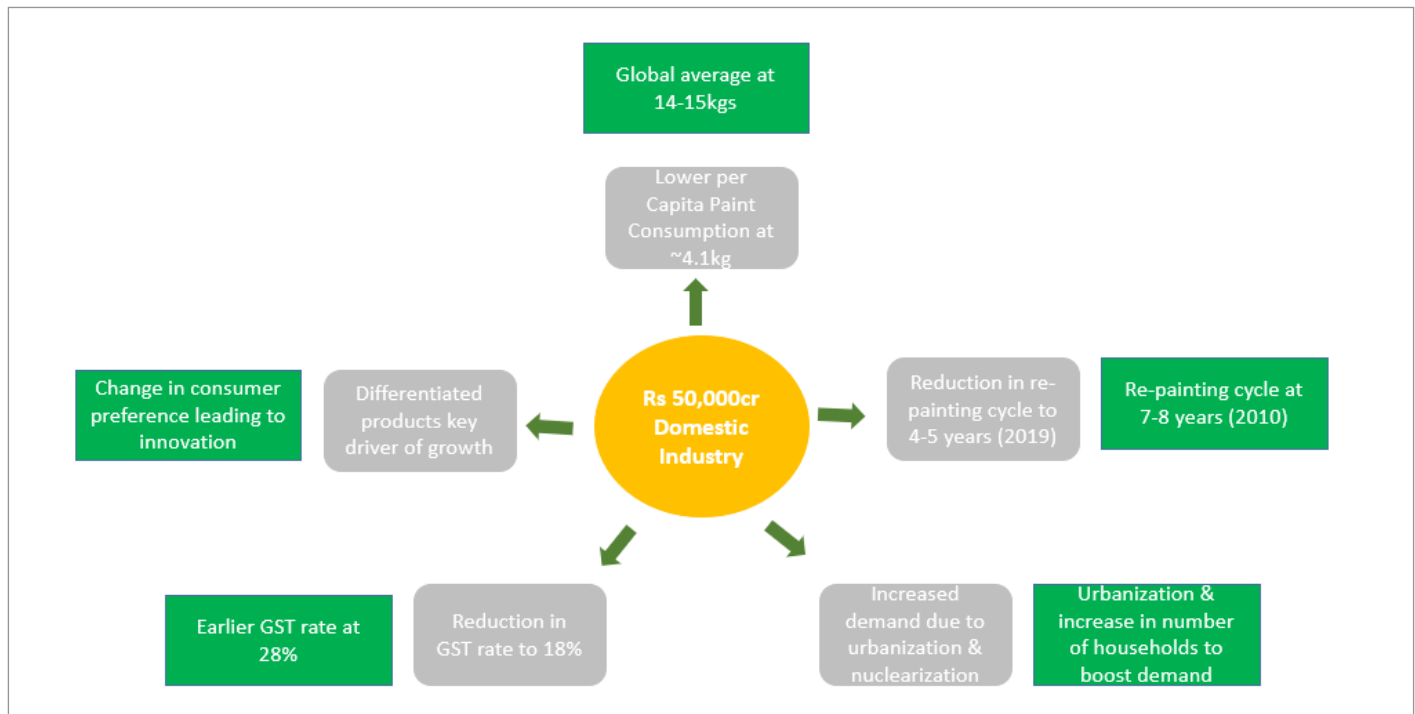
The decorative paints market clocked a CAGR of 11.5% during 2014 to 2019, led by an increase in consumption of paints in the tier 2, -3 and -4 cities. Going ahead, the market is expected to clock a CAGR of 13% from 2019 to 2024 led by factors such as increase in disposable income of individuals and various housing schemes. The industrial market grew at 9.5% during 2014 to 2019 and going ahead, it is expected to grow at 9.9% from 2019 to 2024.

**Decorative paint industry – Growth path**



Source: Company; Sharekhan Research

**Indian paints industry - Growth drivers**

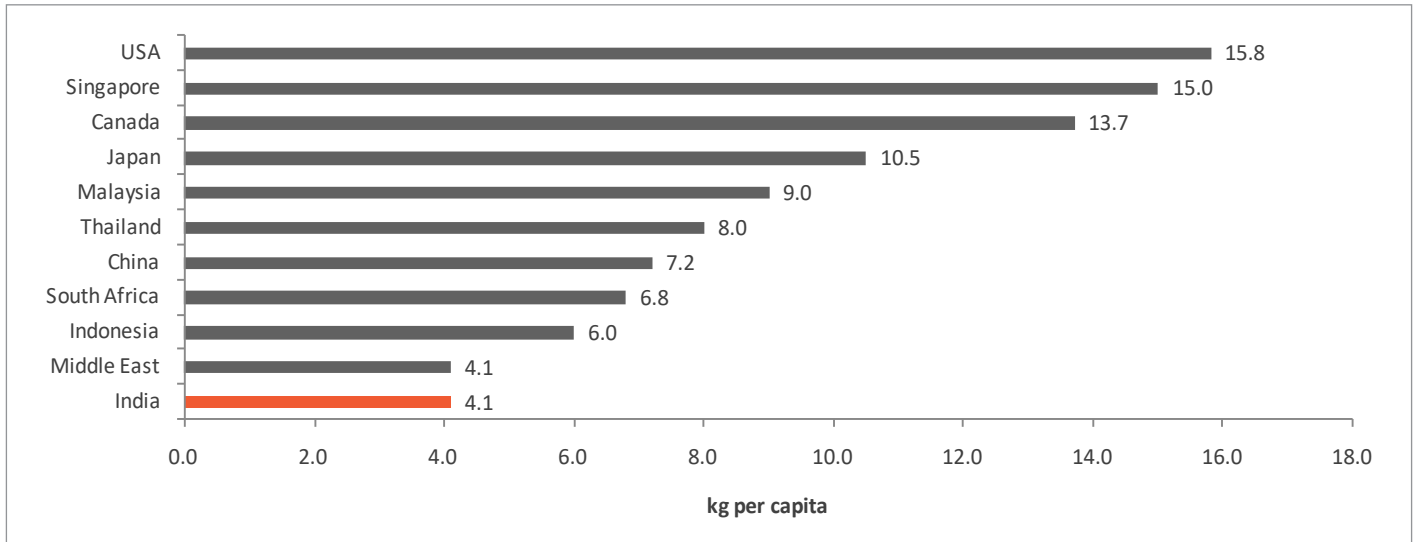


Source: Sharekhan Research

## 1. Higher growth opportunity due to low per capita paint consumption

India's per capita paint consumption recorded a CAGR of 6.8% in the last seven years from 2.6 kg in FY2012 to 4.1 kg in FY2019. Compared to the global average consumption of ~14-15 kg per capita, the per capita consumption of paints and coatings in India is low.

### Lower per capita consumption



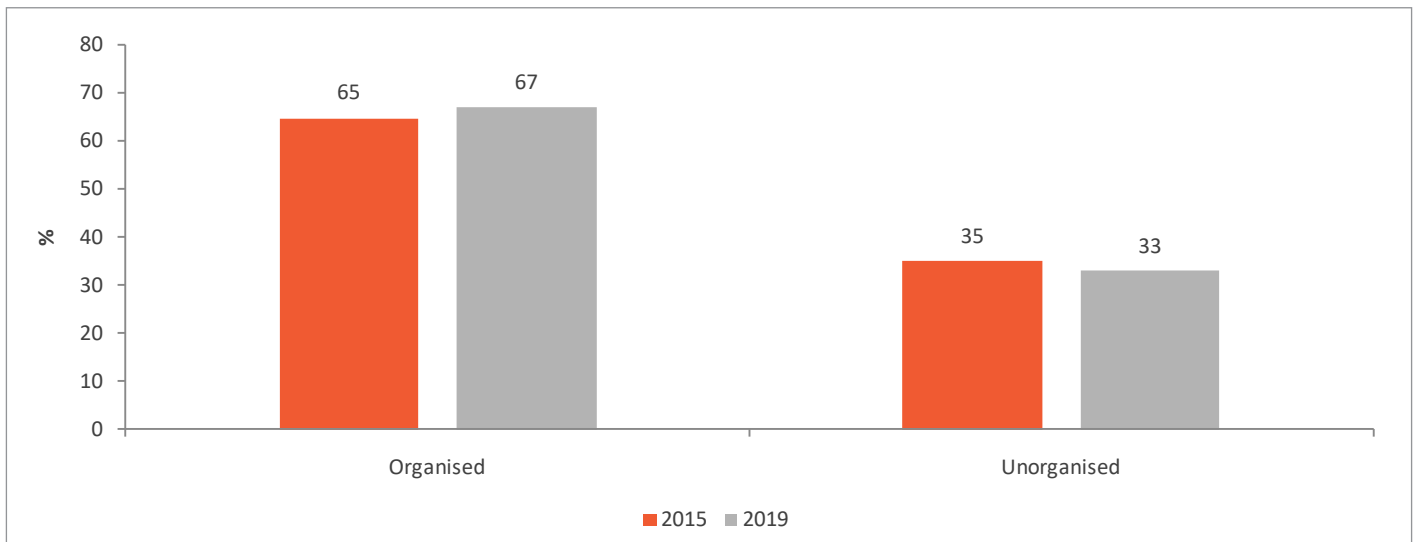
Source: Company; Sharekhan Research

There is a significant opportunity for market penetration in India in both the decorative and industrial paint segments. Due to rising spends on infrastructure, the consumption of coatings is expected to increase. Increasing urbanization coupled with rise in disposable incomes is driving up spends on decorative paints.

## 2. Organised players account for ~70% of total paint industry

The Indian paints industry is an oligopolistic market with a large number of regional, small players. It is dominated by the top four large and organised players who account for ~70% of the total market. Until 2015, the unorganised sector had a market share of approximately 35% and remaining 65% was held by the unorganised players. With demonetisation and implementation of the GST regime, organised players penetrated the market taking advantage of challenges faced by smaller players. As of 2019, the organised sector had a 67% market share, while the remaining 33% was held by unorganised players.

### Organised versus unorganized players

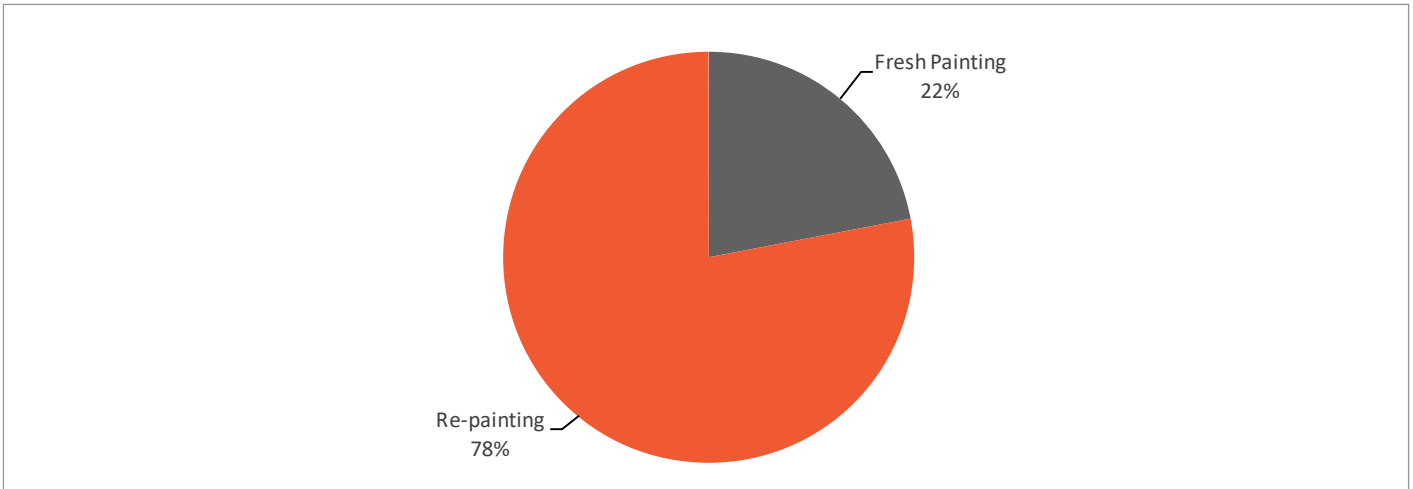


Source: Company; Sharekhan Research

### 3. Reduction in re-painting cycle to boost the decorative paint industry

As of 2019, fresh painting accounted for ~22% of demand for decorative paints, whereas the balance demand was due to the re-painting of households.

#### Repainting accounts for 78% of decorative paint industry



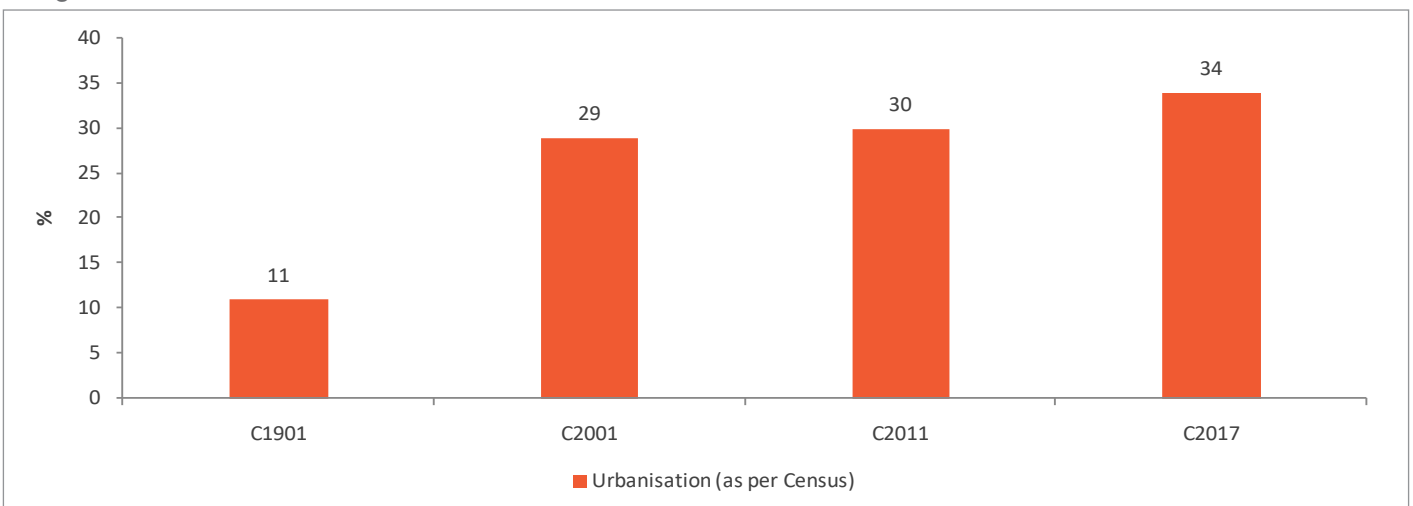
Source: Company; Sharekhan Research

In the last decade, the average re-painting cycle has gradually shrunk from an interval of 7-8 years in 2010 to 4-5 years in 2019 (mostly interiors). Earlier, repainting was done only when paint withered. However, a change in consumer behaviour with some consumers giving more importance to aesthetics, change in looks and appearance of their premises at regular intervals even while the condition of the existing paint is good, has shortened the re-painting cycle. Rising income levels, increase in number of rented houses (where the owners prefer re-painting to attract tenants) and significant ease of the painting process are few of the factors that have influenced reduction in the re-painting cycle.

### 4. Urbanisation and nuclearization of families led to increase in demand for paint

In India, the rate of urbanisation has increased from 25.6% in 1990 to 34.5% in 2017. The rise in urbanization, supported by demand for real estate and improved infrastructure, has increased applications for paints. The UN expects that by 2030, ~40% of the population of India will reside in urban areas. Thus, going ahead as well, increasing urbanization will aid growth of the decorative paints industry. Another factor that contributes to the growth of paint industry is the nuclearization of families. With increasing nuclearization of families, there is an increase in the number of households in the country. Further, many state governments in the recent years have undertaken a lot of initiatives to focus on economic growth of smaller towns. This led to strong demand for affordable housing in India.

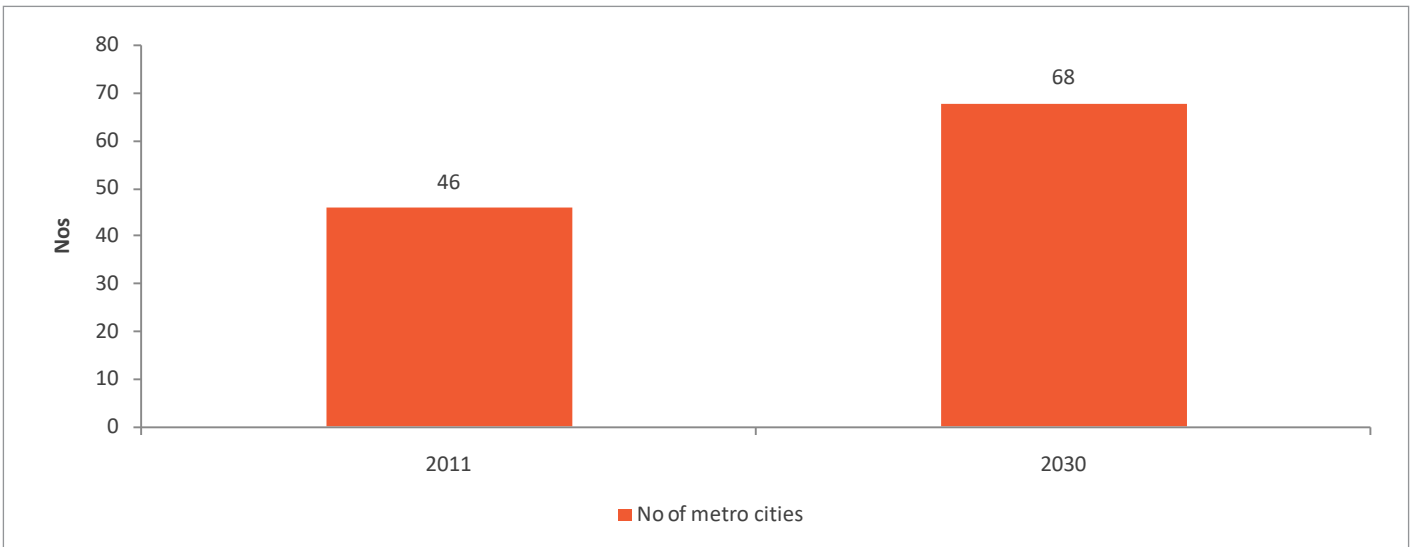
#### Rising Urbanisation



Source: Industry; Sharekhan Research



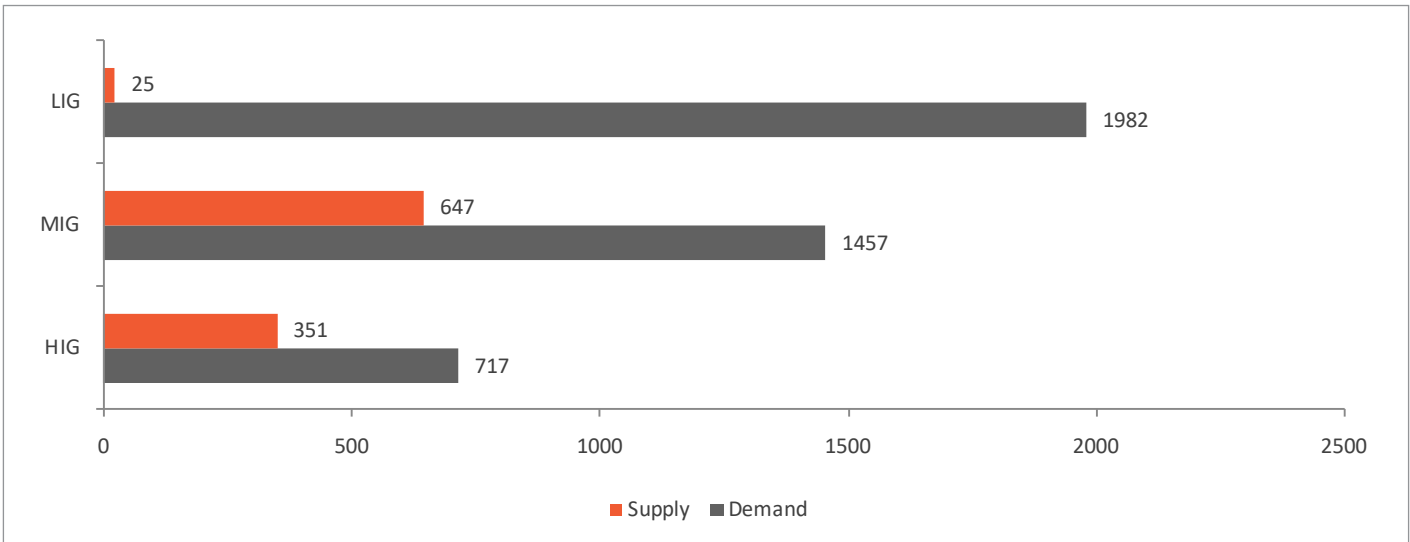
**More towns to turn into metros by 2030**



Source: Industry; Sharekhan Research

The government launched the Pradhan Mantri Aawas Yojana Scheme (PMAYS) in 2015 with an aim to build houses for all by 2022. Affordable and mid-segments accounts for 62% of new launches in India. Execution in the first phase was successful and in the phase-II, the government is planning to build 1.95 crore houses for the eligible beneficiaries. The three-year target appears realistic and achievable, considering that more than 1.5 crore rural homes have been completed in the last five years. This will be one of the key revenue drivers for building material companies (including paint manufacturers). Thus, rising demand for housing and rising regulatory pressures on real estate sector (especially on small players) to provide quality construction to the consumer will drive the demand for new painting (22% of overall decorative paints industry).

**Cumulative demand-supply over 2016-2020 in top 8 cities ('000s) units**



Source: Industry; Sharekhan Research

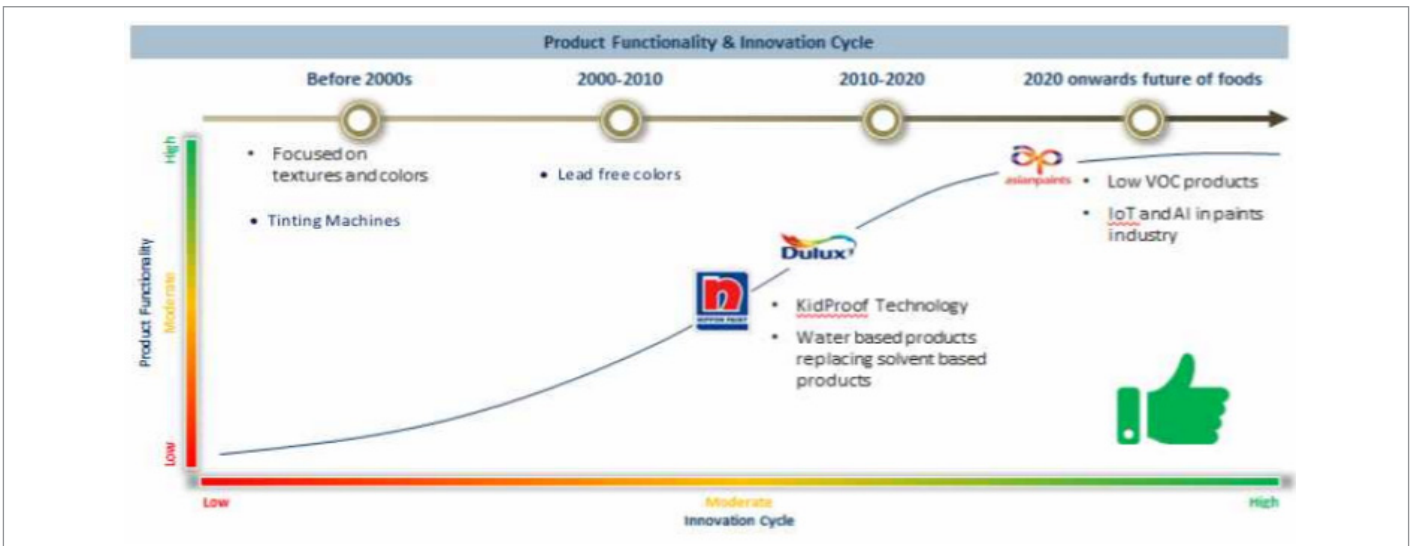
**5. GST rate cuts aided demand**

The GST rate for paints was earlier at 28%, which has now been reduced to 18%. This has driven up volumes of decorative paints, particularly in the lower-end segments like emulsions, distempers and putty. Further, demand was higher as paint firms passed on the cost benefits to the customers leading to lower prices.

## 6. Innovation / differentiated products is the key driver of growth going ahead

In the past few years, the industry has witnessed a gradual change in consumer’s preference with shifts towards 4upgrading/pre-minimisation. For example, there has been a substantial change in focus towards waterproofing over the last decade, this was previously considered as an extra expense in India. A change in trend is observed as consumers are moving from (i) distemper to interior emulsion; (ii) mid-segment to top-end segment; (iii) low-end to top-end segment; (iv) cement paint to exterior emulsions; and (v) unorganized to organized in smaller towns, especially in Tier-3 and -4 cities and rural areas.

Product innovation cycle in the Indian Paint industry

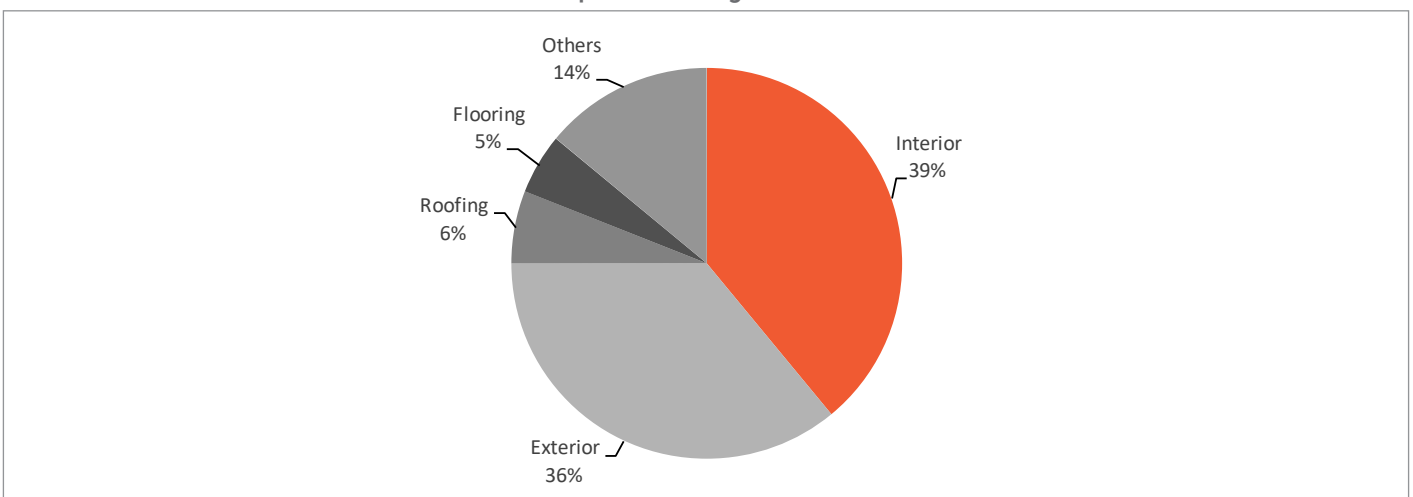


Source: Company

People are now eyeing unique products, which has led to a rise in innovation in the industry with companies coming out with differentiated, unique products to cater to this demand shift. Most companies are now venturing into new product segments and focusing on diversifying their product portfolio. The top-end market is led by the metros and tier-1 and -2 cities, but in the past few years, smaller towns have also indicated increased interest in premium products. This is on the back of increased consciousness of aesthetics and availability of resources to opt for better quality products at higher prices.

Demand for interior and exterior paints has been on the rise owing to customers’ growing preferences to aesthetics. Demand for roofing and flooring paints is also gaining momentum mainly from residential buildings. Paint companies are now promoting products and benefits associated with them, which has heightened consumer awareness and a corresponding rise in sales of roofing and flooring paints.

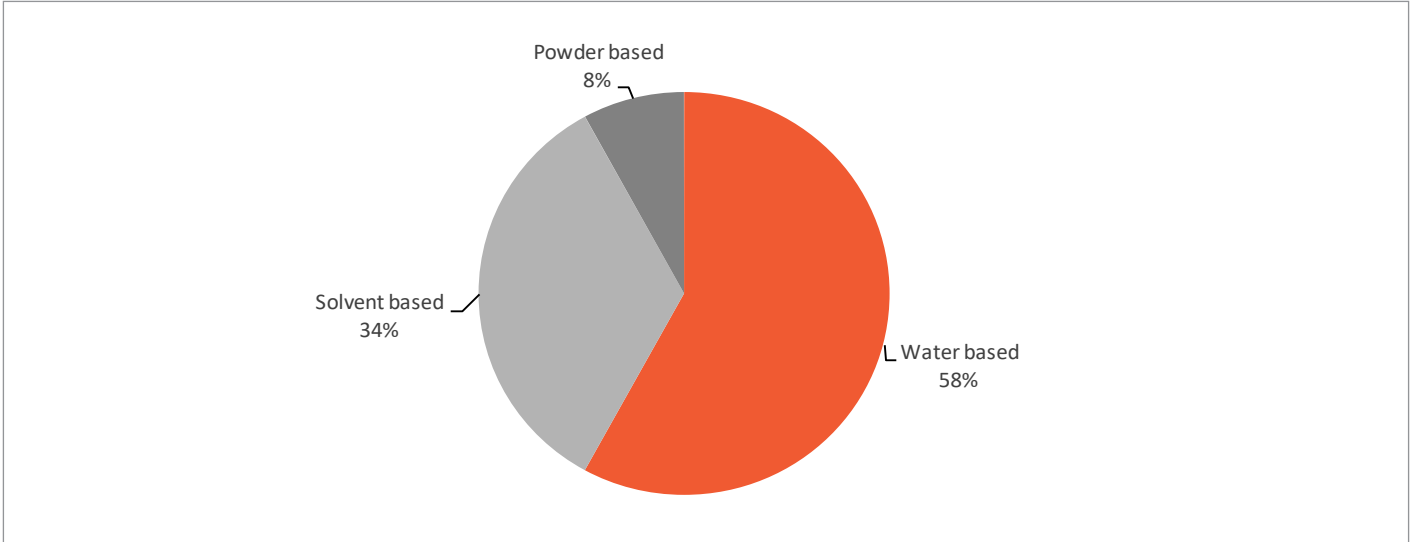
Interiors & exteriors accounts for ~75% of decorative paints industry



Source: Company; Sharekhan Research

The decorative paints industry, in terms of technology, has been witnessing a higher inclination toward water-based paints that are increasingly becoming the preferred choice for home interiors and exteriors. Most companies are establishing manufacturing units for water-based paints.

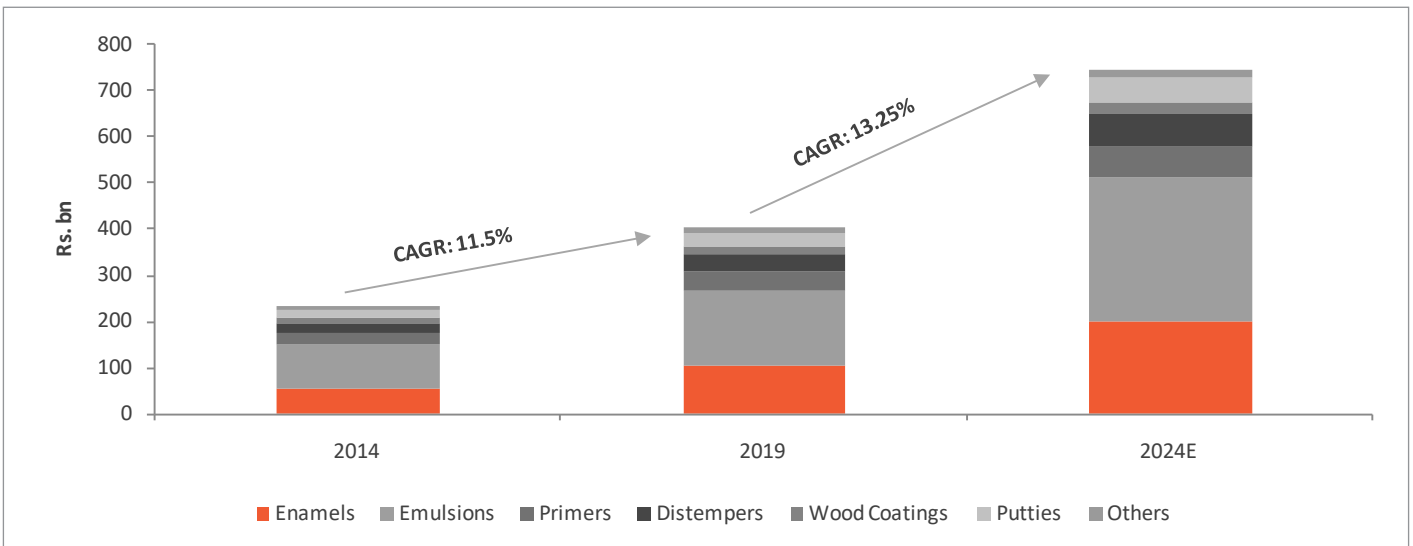
**Water based paints form 58% of overall industry**



Source: Company; Sharekhan Research

For interiors, there is a rise in demand for economy emulsions in place of lower-priced distempers, which has led to a higher growth of emulsion paints as compared to distempers. Even in the exterior category, emulsion-based coatings are being preferred against the conventional cement-based coatings.

**Enamels & emulsions are fastest growing paints categories**



Source: Company; Sharekhan Research

Within the decorative paints market, enamels and emulsion paints are the fastest growing segments. Increasing penetration of emulsions is driven by varying degrees of shine that manufacturers offer in these paints.

**Enamels and Emulsions are expected to grow faster due to uptick in demand**

	Enamels	Emulsions	Primers	Distempers	Wood Coatings	Putties	Others
2014-2019	13.6%	11.4%	11.8%	9.9%	8.6%	10.0%	8.4%
2019-2024E	14.2%	13.6%	12.3%	10.95%	9.6%	11.7%	11.0%

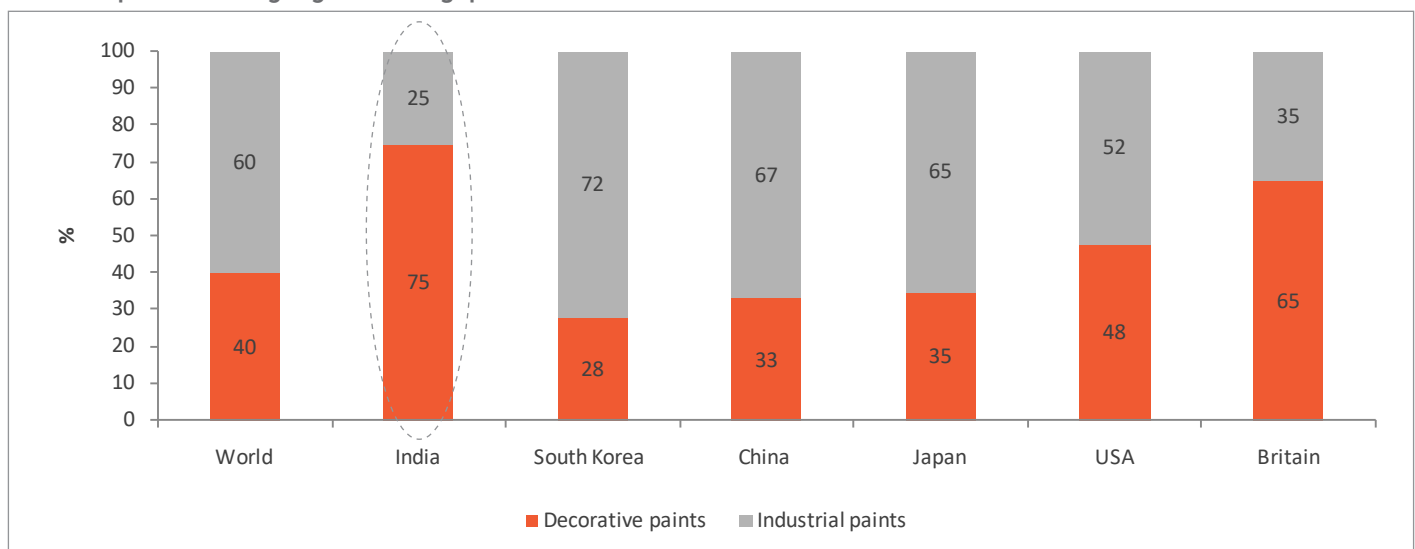
Source: Company; Sharekhan Research

Another reason behind customers opting for premium variants is inflexible labour cost at all levels, making option of paint variant relatively indifferent. There have currently been fewer options available in the value-added sub-category and mainly in the premium price range. However, with increasing demand for these products, companies are likely to launch specialised variants.

**7. Industrial paints constitute 25% of overall paint industry**

Industrial paints and auto coating constitute about 25% of the overall Indian paints industry. This is lesser as compared to developed economies where industrial paints constitute 50-75% of overall paint industry. Industrial paint demand is heavily dependent on auto coating/replenish segment (constitutes two-thirds of segment). Auto industry is cyclical in nature and currently reeling under pressure of slowdown and pandemic situation. On the other hand, rapid urbanisation and infrastructure development of roads, ports, refineries, etc. augured well for the industrial paint and protective coatings segment.

**Industrial paints industry is yet to set a grip in India**



Source: Industry, Sharekhan Research

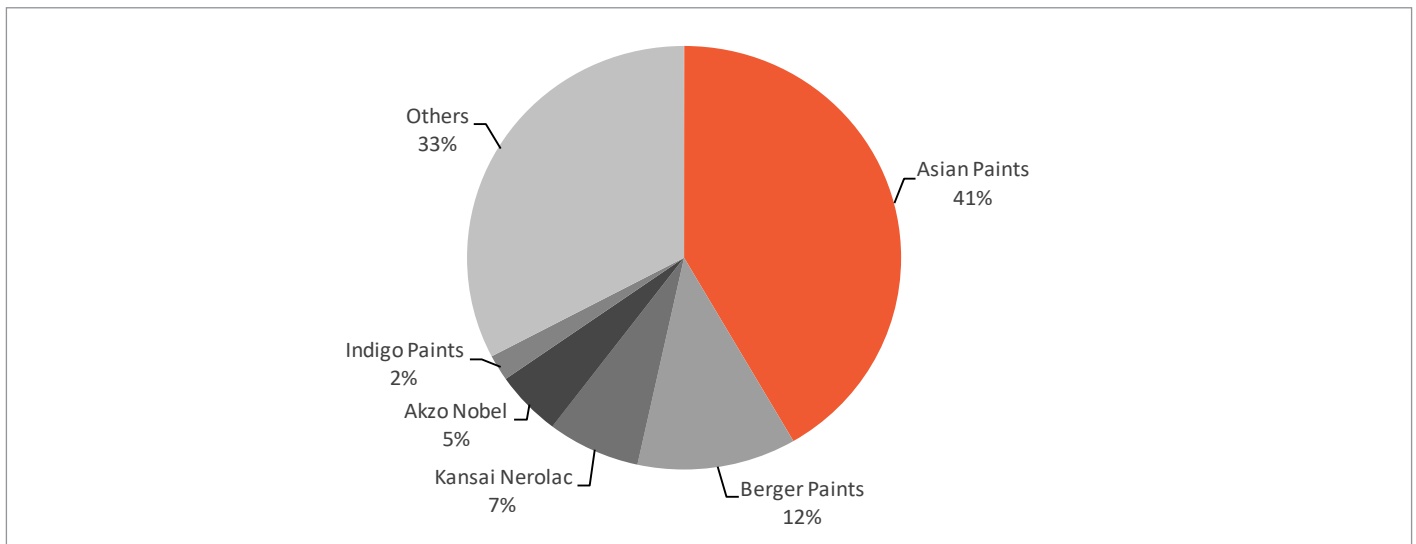
## Why we like Indigo Paints – Carved out a niche for itself in high entry barrier industry

*Indigo Paints Limited (IPL) is one of India's fastest-growing paints companies which has carved a niche for itself by developing and marketing differentiated products to establish its position in high-entry barrier paint industry. The company has strong recognition in tier-3, tier-4 towns and rural India where the demand for paint products is improving substantially in recent years due to rising income levels and large consumers upgrading to branded products. Its unique multi-pronged strategies have helped it achieve strong double-digit revenue growth with a consistent improvement in profitability.*

### Emerging player with distinctive growth strategies

Indigo Paints has created a niche for itself in the high entry barrier paint industry by launching differentiated products, following a bottom-up approach to expand its distribution base in the domestic market and creating brand-equity through one prominent brand 'Indigo'. It has extensive distribution spread over 27 states and seven union territories. Revenues grew at a CAGR of 22% over FY2018-21, which is way ahead of an 8% CAGR growth achieved by industry leader Asian Paints during the same period. The company has clocked a market share of 2% in the overall paints industry. It has gross margins of 48%, which is the highest compared to some leading peers in India due to its close proximity to raw material sources and differentiated products garnering higher margins. This along with a sharp expansion in the operating margins (OPM) led to 71% CAGR growth in PAT over FY2018-21.

### Fifth-largest player










Source: Company; Sharekhan Research

### Portfolio of 'differentiated' products distinguishes IPL from large peers

IPL has effectively managed to establish itself as a differentiator in the existing product categories and has also evolved as a category creator by bringing product innovations. IPL was the first among its competitors to introduce coatings for ceilings, tiles and floors, with competitors entering this space only recently. These products are differentiated based on the end-use they cater to, as well as added properties that they possess. Further, the differentiated products helped IPL to expand the dealers/distribution network in various markets. The company has introduced these products by identifying potential product needs from customers, thereby creating an altogether distinct market for itself. In South India, the demand for clay tiles is higher due to a hot and humid weather condition. With higher demand for clay tiles the demand for tile coating paints products is high. IPL acquired a Kerala-based paint company Hi-build Coatings, which was into manufacturing of solvent-based paints. Post this acquisition, IPL has strong market positioning in markets such as Kerala and Tamil Nadu. The southern region contributed close to 46% of the company's total revenues in FY2020.

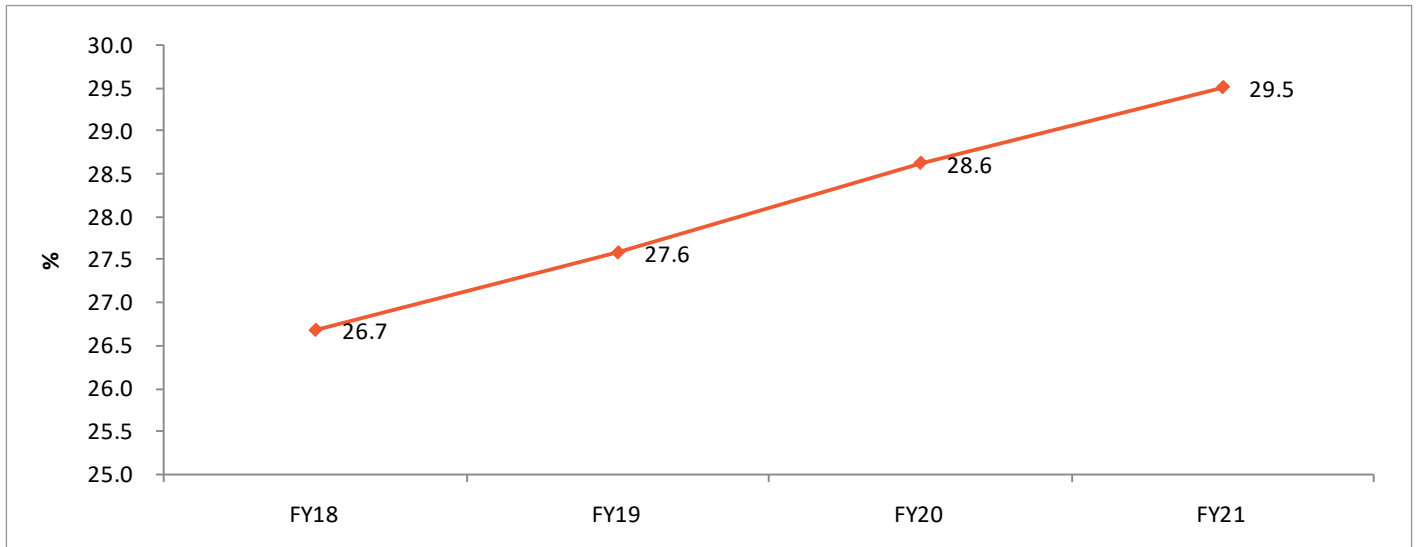
Differentiated product portfolio

Product	Features
<b>Unique Products in the Existing categories</b>	
	<p><b>Product: Dirt-proof &amp; Water-proof Exterior Laminate</b>  <b>Description:</b> Paint with double protection from dirt and water  <b>Application:</b> Cement plaster, concrete and other masonry  <b>Property:</b> Water based</p>
	<p><b>Product: Acrylic Laminate</b>  <b>Description:</b> High sheen paint for both the exteriors and interiors  <b>Application:</b> Cement plaster, concrete and other masonry  <b>Property:</b> Water based</p>
	<p><b>Product: PU Super Gloss Enamel</b>  <b>Description:</b> Enamel paint with very high gloss and finish, protects wood and metal with its anti-fungal and non-yellowing properties  <b>Application:</b> Wood and Metal  <b>Property:</b> Solvent based</p>
<b>Unique Products disrupting market to create a new category (first company to launch these products)</b>	
	<p><b>Product: Metallic Emulsion</b>  <b>Description:</b> Metallic finish paint for interior and exterior walls of homes and offices available in shades of Gold, Silver, and Copper  <b>Application:</b> Wood, metal and masonry  <b>Property:</b> Water-based</p>
	<p><b>Product: Tile Coat Emulsion</b>  <b>Description:</b> A paint for external roof tiles that provides gloss and sheen with protection against algae and fungus  <b>Application:</b> Concrete and roof tiles  <b>Property:</b> Water based</p>
	<p><b>Product: Bright Ceiling Coat</b>  <b>Description:</b> Offers brightness to the ceilings with a smooth matt finish to enhance the brightness of the room  <b>Application:</b> Concrete and plastered ceilings  <b>Property:</b> Water-based</p>
	<p><b>Product: Floor Coat Emulsion</b>  <b>Description:</b> Paint that offers a glossy finish while also protecting the terrace floor, driveways, walkways and cement surfaces  <b>Application:</b> Concrete, cement tiles, terrace floor tiles, paver blocks.  <b>Property:</b> Water-based</p>

Source: Company; Sharekhan Research

The contribution of differentiated products to revenues has increased to ~30% in FY2021 from 26.7% in FY2018. The company will continue to identify potential product opportunities in the market, and focus on developing category-creator products to cater to distinct requirements in the Indian decorative paint industry. To identify such opportunities, the company is regularly engaging with dealers and the painter community by conducting training programmes/seminars for painters and meets with dealers/distributors. On ground, the sales team is understanding demand dynamics for various products in the market. The company also seeks to innovate and develop products with distinguished properties by undertaking research, attending industry trade fairs, and keeping abreast with industry trends and practices. The company targets to increase the contribution of differentiated products by 1% every year.

**Different products contribute one-third of total revenues**



Source: Company; Sharekhan Research

**Focus on expanding distribution reach**

Expansion in dealer network and increase in the number of tinting machines will act as the main engine of growth for IPL in the next few years. The company has established its distribution network gradually and strategically through the bottom-up approach. To create demand for its differentiated products, IPL initially taps tier 3, tier 4 cities, and rural areas, where brand penetration is easier and dealers have greater ability to influence customer purchase decisions. IPL subsequently leverages on this network to engage with dealers in tier 1 and tier 2 cities and metros as well.

Further, the company has introduced tinting machines in target markets to increase sales of emulsion paints. For tinting machines as well, IPL follows the same strategy of initially entering tier 3/4 cities and rural areas where penetration is relatively low and eventually entering the nearby tier 1/2 cities and metros.

In comparison to peers, the tinting machine to dealer ratio and the revenue per tinting machine is very low in case of IPL (38% vs 66% of APNT and Rs. 14.5 lakh vs Rs. 48.4 lakh of Akzo Nobel, respectively) and hence, scope for further expansion is very wide for IPL.

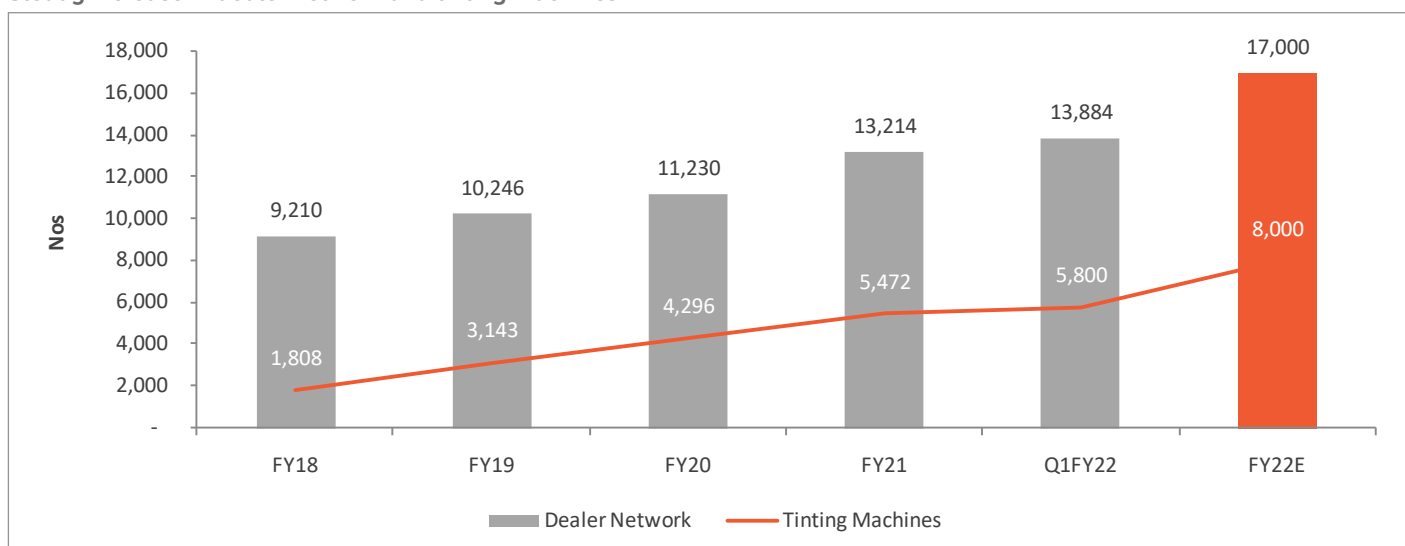
#### Dealer network of paint companies

	Asian Paints	Berger Paints	Kansai Nerolac	AkzoNobel	Indigo Paints
<b>Tinting Machines ('000s)</b>					
FY18	35	14	10	3.2	1.9
FY20	46	20	17	5.5	4.3
CAGR	14.6%	19.5%	30.4%	31.1%	51.2%
<b>Dealer Network ('000s)</b>					
FY18	53	21	25	16.5	9.2
FY20	70	27.5	30	15	11.2
CAGR	14.9%	17.3%	10.0%	-4.7%	10.4%
<b>Tinting Machine to dealer ratio</b>					
FY20	66%	67%	62%	37%	38%
<b>Revenue from operations (Rs. cr)</b>					
FY20	17,194	5,692	4,943	2,662	625
<b>Revenue/tinting machine (Rs. lacs)</b>					
FY20	37.4	28.5	29.1	48.4	14.5

Source: Company; Sharekhan Research

Despite COVID-19 led disruptions, IPL added 2,000 active dealers during the year to end FY21 at 13,214 dealers from 11,200 at the start of the year. In Q1FY2022, IPL further increased its dealer network to 13,884. The company expects the active dealer count to reach 17,000 by FY2022-end. Addition of tinting machines was very slow in H1FY21, but IPL gathered speed in this dimension in both Q3 and Q4 and IPL's tinting machine population increased by 1,200 during FY21 to end the fiscal at a population of 5,472 tinting machines on the ground. In Q1FY2022, IPL added 328 tinting machines taking the total to 5,800 tinting machines as of the end of the quarter. IPL targets to have 8,000 tinting machines by FY2022-end.

#### Steady increase in dealer network and tinting machines

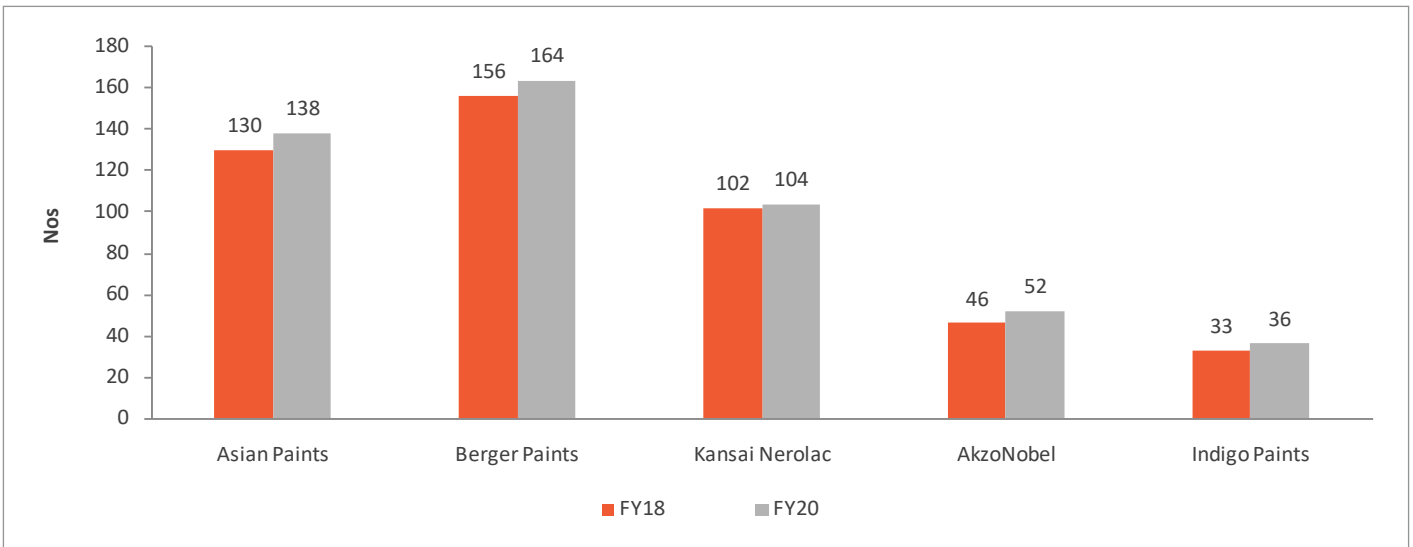


Source: Company; Sharekhan Research

For efficient services, IPL engages with dealers through depots that are set up at major locations across the distribution network. Finished products are dispatched from IPLs manufacturing facilities to the 22 depots, and are subsequently dispatched from the depots to individual dealers. During FY2021, IPL added 8 new depots in Jammu, Uttarakhand, Purnea, Silchar, Bhopal, Sambalpur, Kadapa and Aurangabad taking the total depot count to 44 at the end of FY2021.



**Total number of depots**

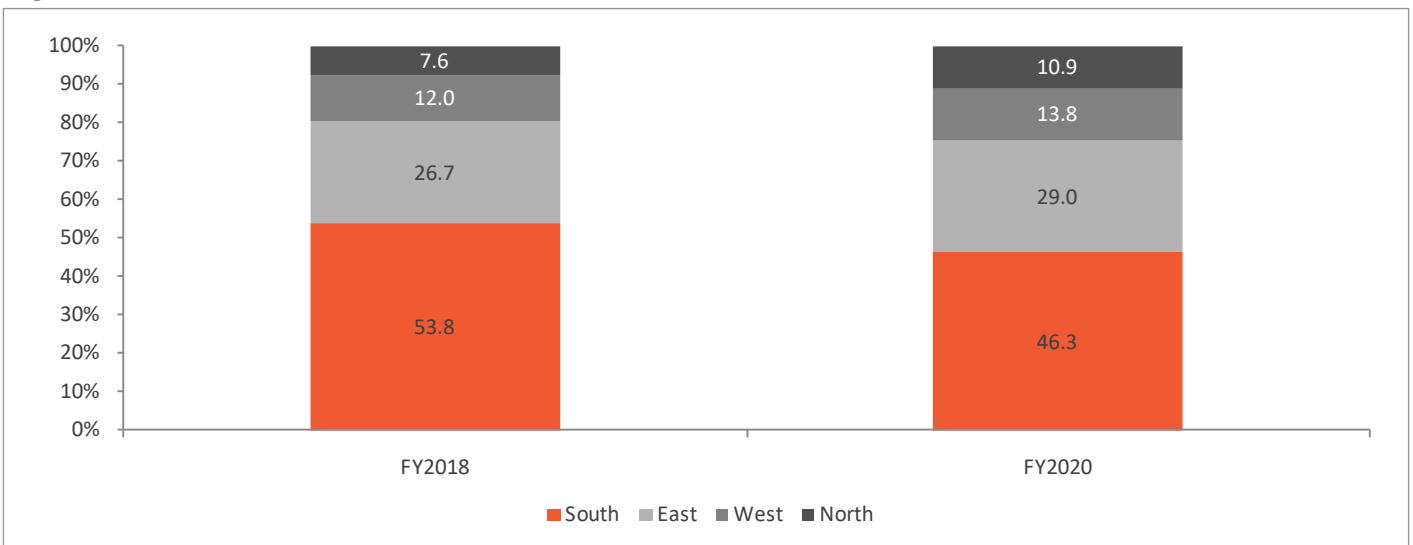


Source: Company; Sharekhan Research

**Deepening penetration in existing market; expanding presence in select new geographies**

IPL has maintained its focus on increasing its penetration in the markets where it has attained certain scale by using its bottom-up approach. It has strong presence in states of Kerala, West Bengal, Bihar, Jharkhand, Chhattisgarh, Odisha and Uttar Pradesh. In these states, the company has already expanded its footprints in tier 3, tier 4 cities and rural areas and focusing on expanding its reach in tier-1 and tier-2 cities. For example, IPL has strong presence in larger cities including Kochi (Kerala) and Thiruvananthapuram (Kerala), Patna (Bihar), Ranchi (Jharkhand) and Kanpur (Uttar Pradesh), and intends to continue to expand its network outwards into other tier 1 and 2 cities and metros in these states. Further it has large scope for dealer network expansion in recently entered states like Telangana, Gujarat, Maharashtra, Karnataka and Tamil Nadu. As on March 31, 2020, the company had a network of 3,292 active dealers in these five states, and intends to engage with more dealers to strengthen its existing sales infrastructure and network in these regions. Further, it is also strengthening its network in North India in Punjab, Uttarakhand and J&K. South India contributed ~46% of overall revenues of the company in FY2020, but the contribution has reduced from upwards of 50% in FY2018 as the company’s penetration in other regions is improving.

**Region-wise revenue contribution**



Source: Company; Sharekhan Research

### Dependence on Kerala is reducing

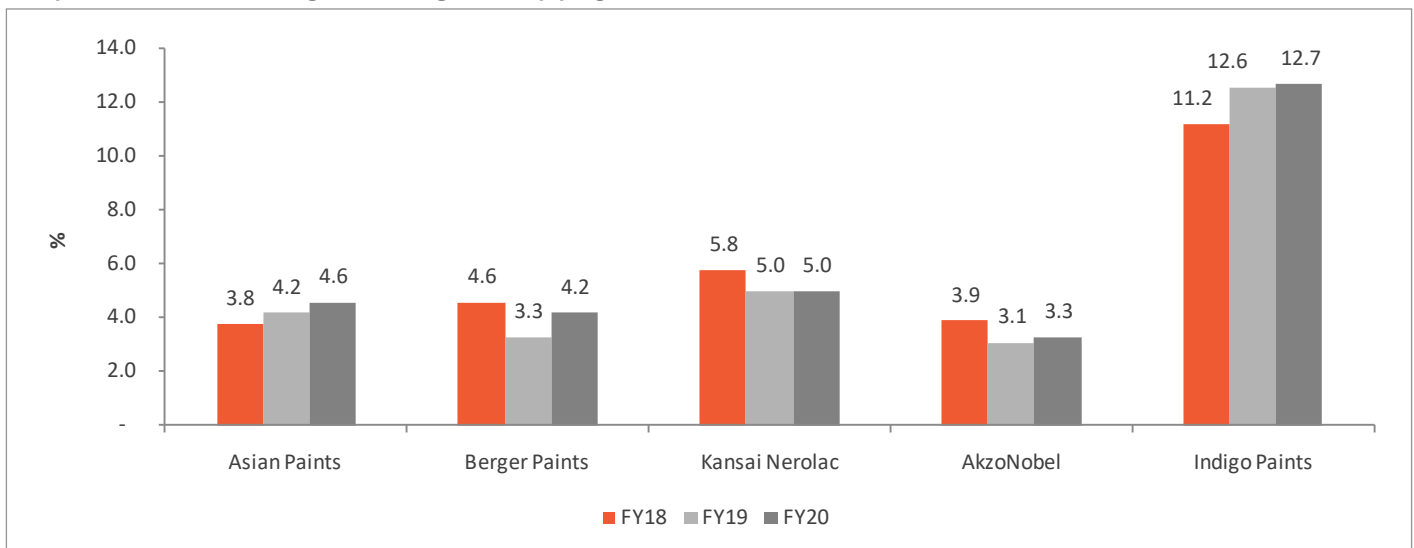
IPL has relatively higher market share in Kerala, which contributes about 30% of overall revenues (reduced from 35% in FY2020 and from 55% in FY20216). The company acquired Hi-Build Coatings, a Kerala centric company in FY2016 which led to higher contribution from Kerala. Kerala registered a revenue growth in low single digit in FY2021, which affected IPL's overall revenue growth. With strong distribution expansion in the other states, the company is expecting the dependence on Kerala will further reduce to 15-20% in the coming years. This will reduce the risk of one state not performing well during a particular year. Having said that, Kerala will remain one of the key markets for the company.

### Higher investment behind brand building activities to improve brand awareness

It is easier to create a brand recognition if all brands are brought under one brand. IPL followed the same strategy and all its products (differentiated and base products) are marketed under one brand name, "Indigo". This strategy has helped the customers connect to the brand immediately without having to remember multiple brand names. In order to enhance brand image among consumers, IPL engaged Mahendra Singh Dhoni, who has a pan-India appeal, as their brand ambassador. IPL has also created a mascot for their brand, a zebra with colourful stripes that regularly features on marketing materials, this helps to increase brand recall.

The paints industry is dominated by top players who have a very large share in the industry. To establish itself and strengthen the Indigo brand, A&P spends of IPL are on a higher side. In the initial years, IPL's advertising campaigns revolved around differentiated products to create a niche for itself. With differentiated products getting good recognition among dealers/distributors in various states. The company is leveraging brand goodwill of differentiated products for introducing and improving visibility for its conventional paints products (emulsion/distempers) in the markets where it already has extended dealers/distributor network.

### Ad-spends % of revenues highest amongst the top players



Source: Company; Sharekhan Research

### Capacity expansion on cards

IPL has periodically carried out capacity expansions at its facilities to cater to the increased demand for their products. As of September 30, 2020, IPL owned and operated three manufacturing facilities in Rajasthan, Kerala and Tamil Nadu. IPL's installed production capacity has increased over the years.

#### Capacity expansion at regular interval

	Mar'2018	Mar'2019	Mar'2020/Sep'2020
<b>Liquid Paints (KLPA)</b>			
Jodhpur (Rajasthan)	22,312	39,244	45,544
Kochi (Kerala)	15,640	27,958	42,701
Pudukkottai (Tamil Nadu)	8,656	9,034	13,658
<b>Total</b>	<b>46,608</b>	<b>43,939</b>	<b>101,903</b>
<b>Powder Paints (MTPA)</b>			
Jodhpur (Rajasthan)	48,944	48,944	93,118

Source: Company; Sharekhan Research

To capitalise on growing demand for water-based paints, IPL has proposed to expand their manufacturing capacities at their existing facility at Pudukkottai in Tamil Nadu, by setting up an additional unit to manufacture water-based paints. As of September 30, 2020, the Pudukkottai facility had an installed estimated production capacity of 13,658 KLPA. The installed production capacity of the proposed additional unit is 50,000 KLPA and it is expected to be operational during FY2023.

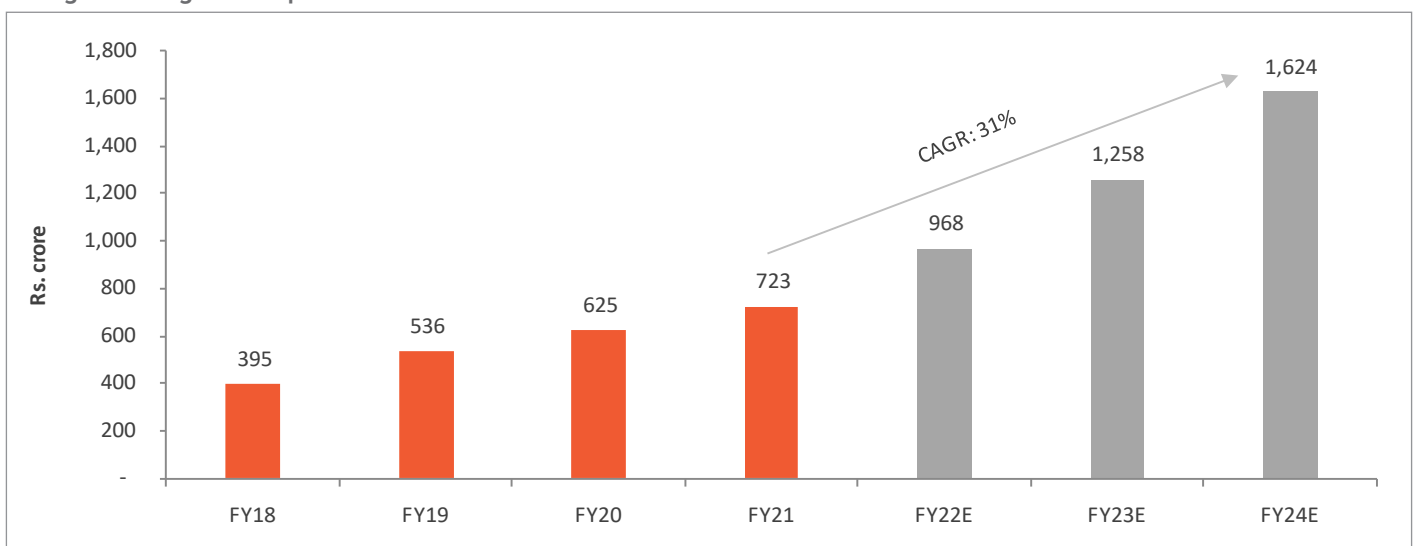
IPL is also in the process of carrying out capacity expansion at its Jodhpur facility. The putty plant's capacity in Jodhpur was doubled in FY2021. Expansion in water based paint capacities with respect to liquid paints such as emulsions and primers is in progress.

IPL has made and intends to continue investing on expanding capacity of their manufacturing facilities to aid in the company's growth efforts and consolidate their pan-India presence.

#### Revenues to grow at CAGR of 31% over FY2021-24

IPL's revenue growth saw strong pick in the H2FY2021 with revenues growing by 22% and 41% in Q3 and Q4FY2021. Overall revenue growth stood at 16% in FY2021. During Q1FY2022, revenues grew by 49.2% y-o-y on low base of Q1FY2021, sequentially revenues were down by 39% on account of the second wave of COVID-19. However, the company has witnessed good recovery in June-July 2021. The management is confident to grow by 35-40% versus the expected industry growth of 18-20% in FY2022. Going ahead, expansion of the distribution network and strong traction to differentiated products would aid strong double-digit revenue growth in the coming years. We expect IPL's revenues to grow at CAGR of 31% over FY2021-24 driven by 26% volume growth over the same period.

#### Strong revenue growth expected



Source: Company; Sharekhan Research

## Industry leading gross margins boosted by locational advantage and differentiated products

Gross margins have improved to 48% in FY2021 from 41.5% in FY2018. Its gross margins are higher compared to some leading players in the industry. The consistent improvement in the gross margins is attributable to 1) higher gross margins for differentiated products and 2) locational advantage with factories located close to areas of sourcing of raw materials.

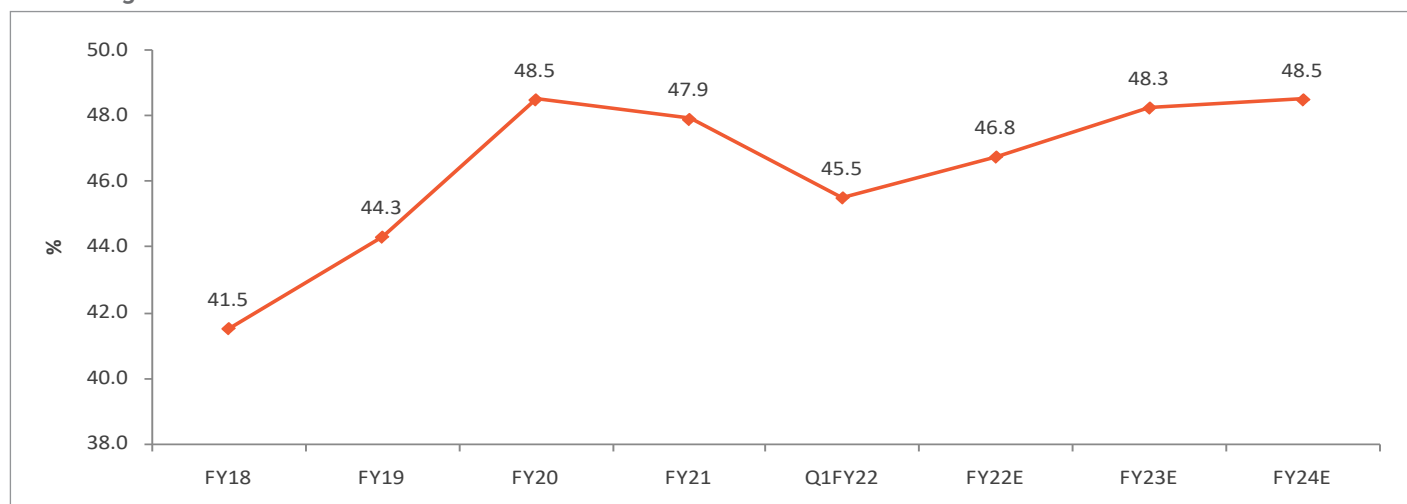
### IPL has industry leading gross margins

	Asian Paints	Berger Paints	Kansai Nerolac	AkzoNobel	Indigo Paints
FY18	42.4%	40.0%	38.3%	42.7%	41.5%
FY19	42.6%	38.1%	36.2%	42.1%	44.3%
FY20	44.7%	40.8%	38.1%	45.8%	48.5%

Source: Company; Sharekhan Research

Differentiated products contribute ~30% of IPL's overall revenues. The company does not have to pay higher trade margins to dealers for differentiated products as compared to conventional paint products. Also less competition in these products gives an advantage of higher pricing power for IPL. Despite undertaking a price hike of 5-6% during the quarter, margins declined sequentially in Q1FY2022 by 110 bps to 45.5% owing to adverse revenue mix and input price inflation of ~10% during the quarter. Going ahead, as the raw material prices cool down, the margins are expected to be normalised.

### Gross margins to remain at about 48%



Source: Company; Sharekhan Research

IPL has three manufacturing facilities located in Rajasthan, Kerala and Tamil Nadu. The company's manufacturing facilities are in close proximity to raw materials. The locational advantage results in lesser inward cost for the company compared to industry leaders.

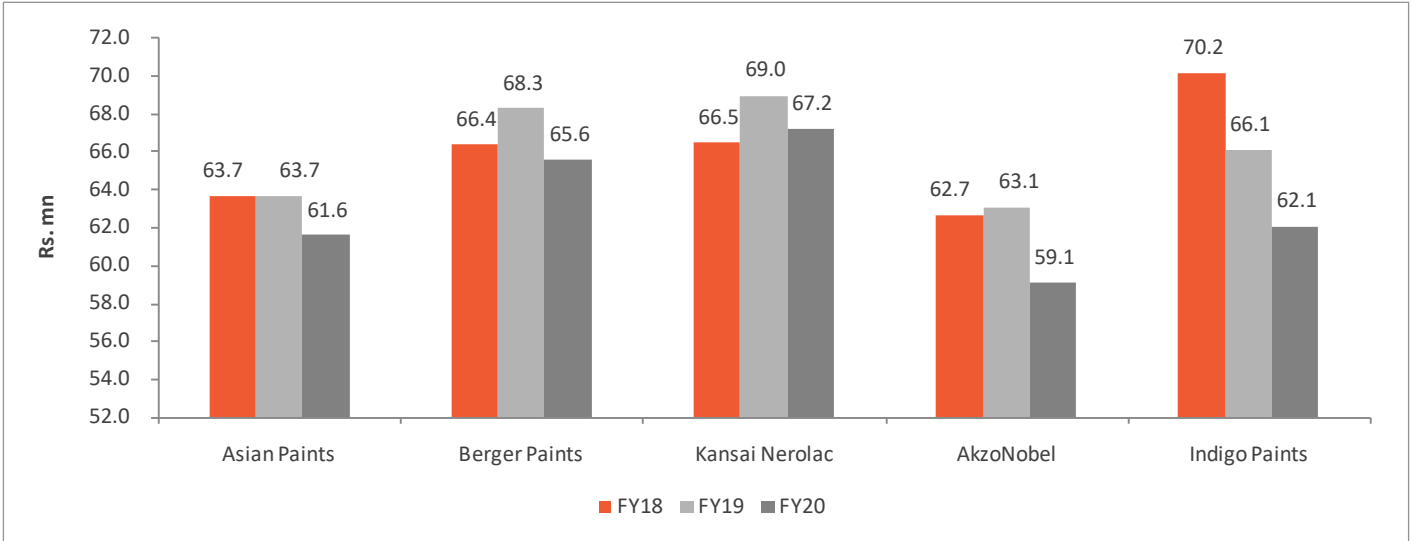
### Manufacturing facilities & locational advantage

Manufacturing facility	Capacity (KLPA)	Products manufactured	Key raw material	Locational advantage
Jodhpur, Rajasthan	45544	water-based paints	white cement and minerals including lime, dolomite, calcite and talcum	Raw material are available abundantly in Rajasthan and neighbouring parts of Gujarat
	93118	cement paints & putties		
Kochi, Kerala	42701	water-based paints	acylic emulsions	Source from neighbouring states of Tamil Nadu and Karnataka
Pudukkottai, Tamil Nadu	13568	water-based paints	alkyd resins and turpentine oil	Source from manufacturers based in Tamil Nadu

Source: Company; Sharekhan research

The material cost (excluding the freight cost) as a percentage of operating revenue is the lowest for IPL as the company is closely located to the source of raw materials. However, this leads to IPL spending greater amounts on outward freight charges to deliver the products to the consumption centers. The outward freight charges for its peers are comparatively lower as their manufacturing facilities are located close to consumption centers. On combining the material costs and freight and forwarding charges, IPL is effectively at par with peers with the range being comparable to the industry leader.

**Raw material cost (including freight cost) at par with Industry leader**

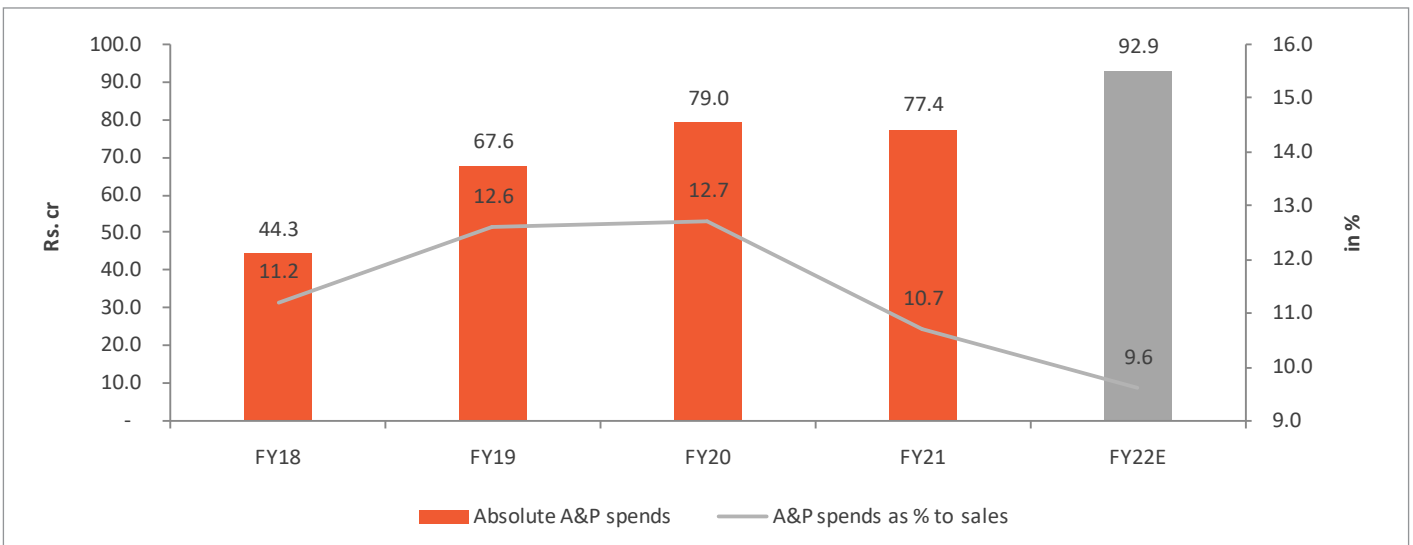


Source: Company; Sharekhan Research

**Advertisement spends as percentage to sales will reduce in the coming years**

In the advertising-intensive paints industry, it is difficult for new entrant to create brand equity. As a part of strategy, large advertisement spends were done on the differentiated products. IPL’s advertisement spends on absolute basis has grown at CAGR of 20% over FY2018-21 to Rs. 77 crore, which is equivalent to number 2 and number 3 player in the Industry. Going ahead the company expects absolute amount of ad-spends will increase but with increase in scale of business the advertisement spends as percentage to sales will come down. In FY2021, advertisement as percentage to sales was down to 10.7%.

**Ad-spends highest amongst industry after the leader**

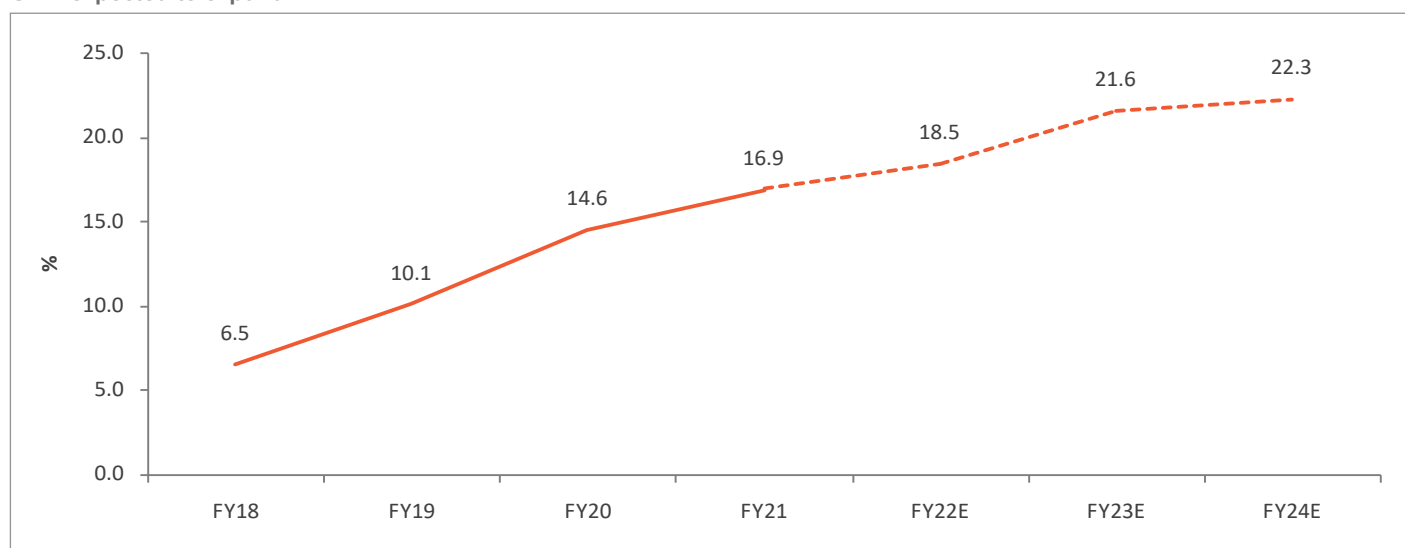


Source: Company; Sharekhan Research

## OPM to improve to 21-22% by FY2024; PAT to grow at CAGR of 55%

IPL's OPM improved to 16.9% in FY2021 from 6.5% in FY2018, largely driven by strong improvement in the gross margins. Gross margins improved to 48% in FY2021 from 41.5% in FY2018. Also in FY2021 the management focused on improving efficiencies, which resulted in reduction in the outward freight cost to 9.9% in FY2021 from 10.5% in FY2020 and overhead cost to 3.7% from 4% in FY2020. Further the ad-spend as percentage to sales reduced by 200 bps to 10.7%, though it remains higher on absolute basis. All these factors aided the company to post OPM improvement of 250 bps in FY2021 to 16.9% (despite Q1 sales were disrupted by first wave of covid-19 and Q4 gross margins were down by ~600 bps due to higher input prices). With expected strong scale-up in business led by distribution expansion, reduction in ad-spend as percentage to sales and sustained focus on curtailing the operating cost, the OPM is expected to improve by 510 bps over FY2021-24 to 22%.

### OPM expected to expand



Source: Company, Shrekhan research

## Better working capital management; operating cash flows improved consistently

Better working capital management aided net working capital days standing low at 13-14 days. The cash generation from operating activities improved from Rs. 42.8 crore to Rs. 101.4 crore over FY2019-21. Average OCF to EBIDTA ratio stood at 78% over the last three years. Higher cash generation took care of capex program. Hence debt:equity remained lower at 0.3x. The company repaid its entire on books through funds raised from IPO and currently stands debt-free.

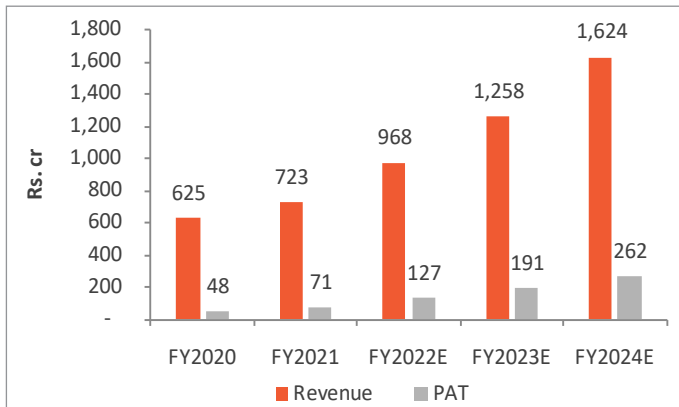
### Experienced management team

- o **Mr Hemant Jalan – Chairman & MD:** He holds B.Tech Degree in chemical Engineering from IIT, Kanpur. He holds Master degree in science from Stanford University and a business administration degree from the University of Chicago. He has over 20 years of experience in paint industry. He is also directors in Halogen Chemicals Pvt Ltd and Zeus Numerix Pvt. Ltd.
- o **Mr Thundijil Surendra Suresh Babu – Chief Operating Officer:** He holds a bachelor's degree in mechanical engineering from Sambalpur University and a post-graduate diploma in management from the Xavier Institute of Management, Bhubaneswar. Pursuant to the Scheme of Amalgamation, he joined Indigo on the effective date of the scheme, being April 19, 2017. He has over 16 years of experience in marketing and sales. Prior to joining Indigo, he was associated with Berger Paints Limited, Idea Cellular Limited as deputy general manager – sales, Etisalat DB Telecom Private Limited as an associate vice president – sales and Hi-Build Coatings Private Limited as general manager – marketing.

- o **Mr Chetan Bhalchandra Humane - Chief Financial Officer:** He holds a bachelor's and a master's degree in commerce from the University of Pune. He joined Indigo with effect from September 10, 2001 and has been appointed as the Chief Financial Officer of the Company with effect from March 11, 2020. He has over 19 years of experience in accounting and finance. Prior to joining Indigo, he was associated with Jenson & Nicholson (I) Ltd as a commercial assistant.
- o **Mr Varghese Idicula - Vice President; Technical of Indigo:** He holds a bachelor's degree in science and a Master's Degree in administrative management from the University of Bombay. He has also received a diploma in paint technology from the Colour Society and the Indian Paints Association. Pursuant to the Scheme of Amalgamation, he joined Indigo on the effective date of the scheme, being April 19, 2017. He has over 35 years of experience in research, development and production. Prior to joining Indigo, he was associated with Asian Paints (India) Limited in technical function, Pidilite Industries Limited as head of research & development (paint coating), Sherwin Williams Saudi Arabia Limited as technical and purchase in-charge and Hi-Build Coatings Private Limited as general manager – technical.

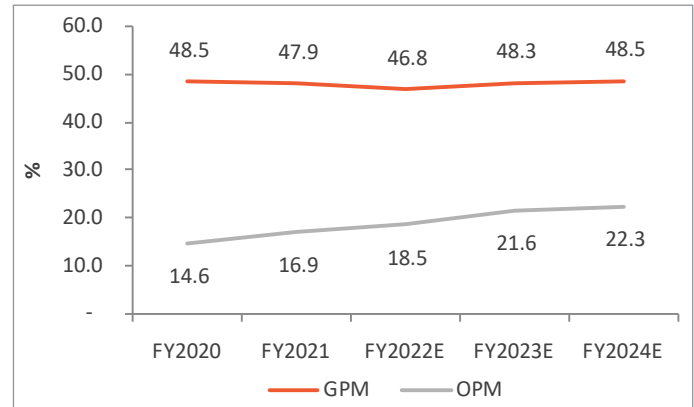
## Financials in charts

### Consistent growth in revenue and PAT



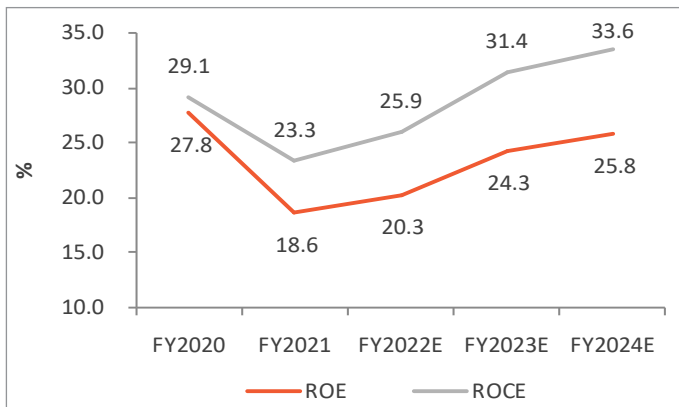
Source: Company, Sharekhan Research

### Trend in GPM and OPM



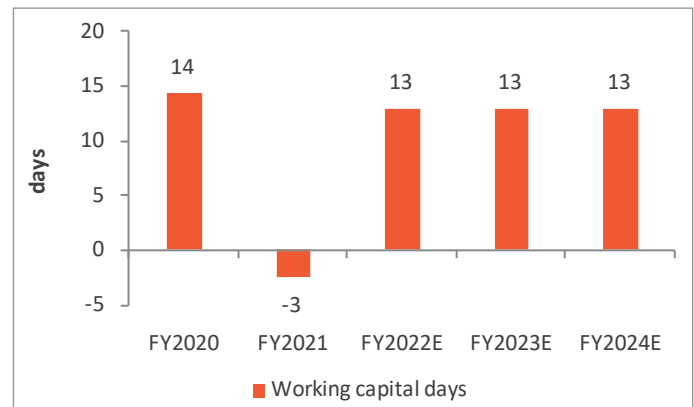
Source: Company, Sharekhan Research

### Return ratios to improve



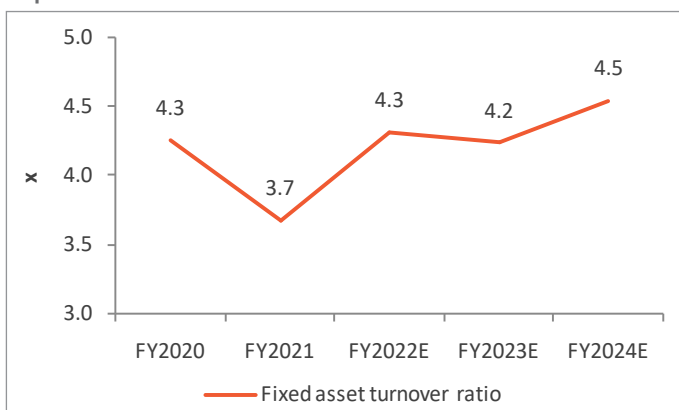
Source: Company, Sharekhan Research

### Consistent working capital days



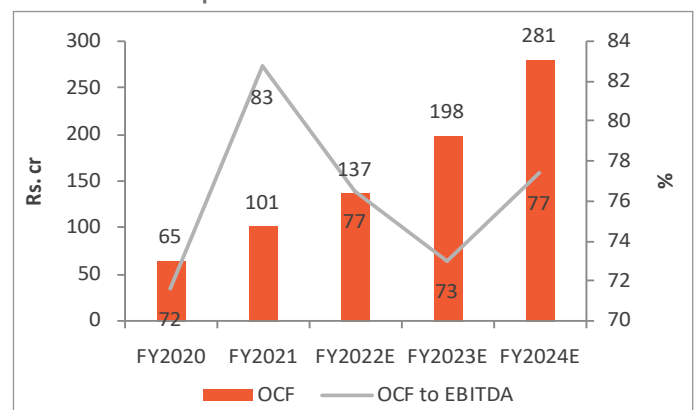
Source: Company, Sharekhan Research

### Improvement in fixed asset turnover ratio



Source: Company, Sharekhan Research

### Stable cash flow position



Source: Company, Sharekhan Research



## Valuation – Strong growth potential with differentiated business model

*IPL's differentiated business model would help it to achieve strong scale in the near to medium term. This along with strong balance sheet with strong cash flow (OCF/EBIDTA of 78%) makes it an emerging play in the paints industry. Differentiated business model, excellent return profile and strong structural growth outlook will keep valuation at a premium at 60.4x/44.2 its FY2023/24E EPS.*

### ■ Sector View - Structural growth of the paint industry is intact

The Indian paints industry reported an 11% CAGR over FY2011-FY2019 and stood at Rs. 545 billion. The decorative paint segment constitutes around 74% of total paint sales, resulting in the paint sector growing at a robust rate even at the time of an industrial slowdown. April and May (constitute ~25% of total annual sales) are two of the key months for re-painting activities in the domestic market. FY2021 was affected by COVID-19 lockdowns, resulting in almost NIL business in Q1FY2021. Paint industry registered a resilient performance in the second wave of COVID-19 and is expected to post strong performance in the quarters ahead with strong demand for decorative paint products. The decorative paints industry is expected to post a 13% CAGR over FY2019-FY2024, led by reduction in the repainting cycle to 4-5 years (from 7-8 years earlier), acceptance for better paint products in smaller towns, and upgradation of premium brands in cities and large towns.

### ■ Company Outlook - Growth levers in place

A differentiated business model aided the company to achieve strong top and earnings growth of 22% and 71% over FY2018-21 with the highest gross margins of 48% among the peers. The OPM improved to 16.9% in FY2021 from 6.5% in FY2018. Though near term pandemic-led uncertainties would impact the growth, the rising urbanization, willingness to spend behind home improvement, strong traction to differentiate products and market share gains would help IPL to achieve faster recovery in the coming years. A scale-up in the business will help OPM further improve and reach at ~22% in FY2024.

### ■ Valuation - Initiate with Buy assigning a price target of Rs. 3,305

We expect IPL's revenue and PAT to grow at a CAGR of 31% and 55% over FY2021-24E driven by strong expansion in dealer network, improving market share and margin expansion. The company has strong balance sheet with stable working capital management and strong operating cash flows (average OCF to EBIDTA ratio stood at 78% for past three years). Moreover, its return ratios are expected to improve strongly in the coming years (RoE and RoCE to stand at 26% and 34% in FY2024). The stock is currently trading at 60.4x its FY2023E EPS and 44.2x its FY2024E EPS (and 41.0x/30.1x its FY2023E/24E EV/EBIDTA). Differentiated business model with industry leading gross margins, sustained focus on improving market share, strong return profile and the structural growth story of the paints industry will keep valuations at a premium as compared to close peers. We initiate our coverage on Indigo Paints with a Buy recommendation and price target (PT) of Rs. 3,305 (valuing the stock at 60x its FY2024E earnings).

#### Peer Comparison

Companies	CAGR % (FY21-24)		P/E (x)			EV/EBIDTA (x)			RoCE (%)		
	Revenue	PAT	FY21	FY22E	FY23E	FY21	FY22E	FY23E	FY21	FY22E	FY23E
Asian Paints	16.6	18.8	93.1	75.8	64.1	57.3	48.5	41.2	22.9	23.8	23.7
Berger Paints*	15.6	25.9	110.3	87.8	66.4	66.5	54.4	42.4	20.7	22.3	25.4
Kansai Nerolac*	15	17.8	63.7	55.8	45.4	32.2	29.2	24.6	20.0	22.5	23.7
Pidilite Industries	17.1	20.8	102.6	86.4	69.1	66.2	56.4	45.7	16.7	17.4	19.9
Indigo paints	31.0	54.6	163.2	90.8	60.4	92.0	62.5	41.0	23.3	25.9	31.4

Source: Sharekhan estimates; \* Consensus estimates

## Financials

### Statement of Profit and Loss

Rs cr

Particulars	FY2020	FY2021	FY2022E	FY2023E	FY2024E
<b>Revenues</b>	<b>624.8</b>	<b>723.3</b>	<b>968.0</b>	<b>1258.2</b>	<b>1624.3</b>
<i>y-o-y %</i>	16.6	15.8	33.8	30.0	29.1
Raw Material Cost	322.0	376.5	515.5	651.1	836.5
Freight expenses	65.6	71.6	91.5	113.2	146.2
Employee Cost	42.0	48.3	57.0	66.1	78.0
Other Expenses	25.2	27.0	32.4	39.6	51.2
Advertisement spends	79.0	77.4	92.9	116.4	150.2
<b>Total Operating Cost</b>	<b>533.8</b>	<b>600.8</b>	<b>789.3</b>	<b>986.5</b>	<b>1262.2</b>
<b>Operating Profit</b>	<b>91.0</b>	<b>122.5</b>	<b>178.8</b>	<b>271.7</b>	<b>362.2</b>
<i>y-o-y %</i>	68.2	34.7	45.9	52.0	33.3
OPM(%)	14.6	16.9	18.5	21.6	22.3
Other Income	1.6	3.6	20.6	24.9	37.5
Interest & Other Financial Cost	5.6	3.8	0.9	0.7	0.7
Depreciation	19.6	24.4	28.2	39.9	48.9
<b>Profit Before Tax</b>	<b>67.4</b>	<b>97.9</b>	<b>170.3</b>	<b>255.9</b>	<b>350.0</b>
Tax Expense	19.6	27.1	42.9	64.5	88.2
<b>Reported PAT</b>	<b>47.8</b>	<b>70.9</b>	<b>127.4</b>	<b>191.4</b>	<b>261.8</b>
<i>y-o-y %</i>	77.9	48.2	79.8	50.3	36.8

Source: Company, Sharekhan estimates

### Cash flow statement

Rs cr

Particulars	FY2020	FY2021	FY2022E	FY2023E	FY2024E
Cash flow from operating activities	65.1	101.4	136.8	198.4	280.5
Cash flow from investing activities	-67.4	-317.4	-144.7	-220.0	-240.0
Cash flow from financing activities	-3.9	255.1	-5.0	0.2	0.2
<b>Net change in cash and cash equivalents</b>	<b>-6.2</b>	<b>39.1</b>	<b>-12.9</b>	<b>-21.4</b>	<b>40.7</b>
Opening cash balance	11.8	5.7	44.8	31.9	10.5
<b>Closing cash balance</b>	<b>5.7</b>	<b>44.8</b>	<b>31.9</b>	<b>10.5</b>	<b>51.2</b>
<b>Free cash flows</b>	<b>-3.4</b>	<b>26.4</b>	<b>103.6</b>	<b>18.4</b>	<b>250.5</b>

Source: Company, Sharekhan estimates

Balance sheet

Rs cr

Particulars	FY2020	FY2021	FY2022E	FY2023E	FY2024E
<b>Sources of Funds</b>					
Equity Capital	29.0	47.6	47.6	47.6	47.6
Instruments in the nature of equity	18.3	-	-	-	-
Reserves & Surplus	149.7	515.9	643.3	834.7	1096.6
<b>Net Worth</b>	<b>197.1</b>	<b>563.5</b>	<b>690.9</b>	<b>882.3</b>	<b>1144.1</b>
<b>Long term liabilities</b>					
Borrowings	24.7	-	-	-	-
Lease liabilities	2.8	5.5	5.5	5.5	5.5
Other liabilities	3.8	4.3	4.5	4.7	5.0
Deferred tax liabilities	7.0	7.0	7.0	7.0	7.0
<b>Total long term liabilities</b>	<b>38.4</b>	<b>16.7</b>	<b>17.0</b>	<b>17.2</b>	<b>17.4</b>
<b>Short term liabilities</b>					
Borrowings	14.5	-	-	-	-
Lease liabilities	3.4	3.3	3.3	3.3	3.3
Other financial liabilities	19.4	15.2	10.0	10.0	10.0
<b>Total short term liabilities</b>	<b>37.4</b>	<b>18.5</b>	<b>13.3</b>	<b>13.3</b>	<b>13.3</b>
<b>Capital Employed</b>	<b>272.8</b>	<b>598.7</b>	<b>721.1</b>	<b>912.8</b>	<b>1174.8</b>
<b>Application of Funds</b>					
Net Block	169.8	218.3	221.5	361.5	342.6
Capital WIP	1.1	3.1	5.0	5.0	5.0
Intangible Assets	0.4	0.5	0.5	0.5	0.5
Goodwill	30.6	30.6	30.6	30.6	30.6
Investment	20.8	49.7	49.7	49.7	49.7
<b>Current Assets</b>	<b>199.3</b>	<b>509.0</b>	<b>681.5</b>	<b>795.8</b>	<b>1163.4</b>
Other Current Assets	4.2	8.0	8.8	9.6	10.6
Inventories	76.8	94.7	111.2	146.4	189.5
Sundry Debtors	104.5	121.2	173.8	228.7	296.1
Fixed Deposits with Bank	0.0	213.5	325.0	365.0	575.0
Cash and Bank Balance	5.7	44.8	31.9	10.5	51.2
Loans and Advances	8.2	26.9	30.9	35.6	40.9
<b>Less: Current Liab. &amp; Provisions</b>	<b>149.2</b>	<b>212.4</b>	<b>267.6</b>	<b>330.3</b>	<b>416.9</b>
Trade Payables	138.6	185.6	237.9	297.3	380.4
Other Current Liabilities & Provisions	8.2	22.7	24.9	27.4	30.2
Provisions	2.4	4.2	4.8	5.6	6.4
<b>Net Current Assets</b>	<b>50.1</b>	<b>296.6</b>	<b>413.9</b>	<b>465.5</b>	<b>746.5</b>
<b>Net Assets</b>	<b>272.8</b>	<b>598.7</b>	<b>721.1</b>	<b>912.8</b>	<b>1174.8</b>

Source: Company, Sharekhan estimates

### Key Ratios

Particulars	FY2020	FY2021	FY2022E	FY2023E	FY2024E
<b>Margins &amp; Tax rate (%)</b>					
GPM	48.5	47.9	46.8	48.3	48.5
OPM	14.6	16.9	18.5	21.6	22.3
NPM	7.7	9.8	13.2	15.2	16.1
Tax rate	29.1	27.6	25.2	25.2	25.2
<b>Cost matrix (% of revenues)</b>					
Raw material cost	51.5	52.1	53.3	51.8	51.5
Freight cost	10.5	9.9	9.5	9.0	9.0
employee cost	6.7	6.7	5.9	5.3	4.8
Other expenses	4.0	3.7	3.4	3.2	3.2
Advertisement spends	12.7	10.7	9.6	9.3	9.3
Total operating cost	85.4	83.1	81.5	78.4	77.7
<b>Growth ratios (y-o-y %)</b>					
Revenues	16.6	15.8	33.8	30.0	29.1
Operating profit	14.6	16.9	18.5	21.6	22.3
PBT	98.2	45.2	74.0	50.3	36.8
Adjusted PAT	75.9	48.2	79.8	50.3	36.8
Reported PAT	77.9	48.2	79.8	50.3	36.8
<b>Per share (Rs.)</b>					
CMP	2431.0	2431.0	2431.0	2431.0	2431.0
Adjusted EPS - Diluted	10.1	14.9	26.8	40.2	55.0
Reported EPS - Diluted	10.1	14.9	26.8	40.2	55.0
Cash EPS	23.2	20.0	32.7	48.6	65.3
Book value per share (BVPS)	67.9	118.5	145.2	185.5	240.5
<b>Valuation ratios (x)</b>					
P/E	-	-	90.8	60.4	44.2
Price / Book value (BV)	35.8	20.5	16.7	13.1	10.1
EV / EBIDTA	-	92.0	62.5	41.0	30.1
EV / Sales	18.5	15.6	11.5	8.9	6.7
Market cap / Sales	18.5	16.0	11.9	9.2	7.1
<b>Working capital (Days)</b>					
Inventory Days	48	51	48	48	48
Debtors Days	66	66	75	75	75
Creditors Days	100	119	110	110	110
Operating cash cycle	14	-3	13	13	13
<b>Financial ratios</b>					
Fixed asset turnover ratio (x)	4.3	3.7	4.3	4.2	4.5
Total asset turnover ratio (x)	1.6	1.2	1.1	1.1	1.1
Operating cash flow/EBIDTA (%)	72	83	77	73	77
Debt / Equity (x)	0.2	0.0	0.0	0.0	0.0
RoE (%)	27.8	18.6	20.3	24.3	25.8
RoCE (%)	29.1	23.3	25.9	31.4	33.6

Source: Company, Sharekhan estimates

## About company

Incorporated in 2000, IPL is the 5th largest paint companies in India. It started its operations with manufacturing of lower end cement products and gradually expanded its range to cover most segments of water based paints like exterior emulsions, interior emulsions, distempers, primers etc. It kept churning out bright new ideas for painting solutions, with alarming regularity. It introduced India's first metallic paint, first floor coat paint, unique ceiling coat paint and first of its kind paint for roofs. Differentiated products contribute ~30% of the company revenues. The company has growing dealership base of 13,000+ dealers covering 27 states.

## Investment theme

IPL is fastest growing paints companies in India which has carved a niche for itself by developing and marketing differentiated product to establish its position in high entry barrier paint industry. It has highest gross margins of 48% amongst the paint companies. The differentiated business model aided the company to achieve strong top and earnings growth of 22% and 71% over FY2018-21 with highest gross margins of 48% amongst the peers. The OPM improved to 16.9% in FY2021 from 6.5% in FY2018. Though near term pandemic led uncertainties would impact the growth, the rising urbanization, willingness to spend behind home improvement, strong traction to differentiate products and market share gains would help IPL to achieve faster recovery in the coming years.

## Key Risks

- ◆ **Increase in raw material prices:** The raw materials used in manufacturing process are primarily sourced from third party suppliers in India. The company profitability remains susceptible to the risks arising out of raw material price fluctuations and in particular fluctuation of crude oil prices which could result in declining operating margins.
- ◆ **Delay in capacity expansion:** Delay in capacity expansion plan due to any regulatory hurdle or any other reason would affect the future growth prospects of the company.
- ◆ **Company does not enter into long-term arrangements with dealers:** Indigo presently does not have any long-term or exclusive arrangements with any of the dealers and cannot assure that they will be able to sell the same quantities as they supplied historically to such dealers.

## Additional Data

### Key management personnel

Hemant Jalan	MD & Chairman
Thundiyil Surendra Suresh Babu	COO
Chetan Bhalchandra Humane	CFO
Sujoy Bose	Company Secretary & Compliance Officer

Source: Company

### Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Sequoia Capital Investments	28.5
2	Ashoka India opportunity fund	1.5
3	SmallCap World Fund, Inc	1.4
4	Abhu Dhabi Investment Authority	1.4
5	Nomura India Investment Fund	1.3
6	Government of Singapore - E	1.0
7	SBI Fund Management Pvt. Ltd	0.7
8	Nomura Hold Inc	0.4
9	Axis asset management Co Ltd/India	0.2
10	Invesco Asset management India Pvt. Ltd	0.2

Source: Bloomberg

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## Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and deteriorating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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