Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

NOCIL Ltd

Stellar Q1, well-placed to strengthen global market share

Specialty Chemicals	Sharekhan code: NOCIL

Reco/View: Buy	↔	CMP: **Rs. 278**	Price Target: **Rs. 348**	↔

↑ Upgrade ↔ Maintain ↓ Downgrade

3R MATRIX	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)	✓		

\+ Positive = Neutral – Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↔	

Company details

Market cap:	Rs. 4,624 cr
52-week high/low:	Rs. 321/191
NSE volume: (No of shares)	9.5 lakh
BSE code:	500730
NSE code:	NOCIL
Free float: (No of shares)	11.0 cr

Shareholding (%)

Promoters	33.9
FII	2.9
DII	4.9
Others	58.3

Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	9.7	22.4	18.4	6.2
Relative to Sensex	1.1	21.5	17.8	(3.2)

Sharekhan Research, Bloomberg

Summary

- NOCIL reported yet another quarter of strong performance with PAT sharply beating estimates by 36% at Rs. 66 crore, up 40% y-o-y, led by better-than-expected volumes and a beat in EBITDA margin
- Strong volume growth of 16%/11% y-o-y/q-o-q to all-time high of 15521 tonnes reflects robust domestic demand while EBITDA margins at Rs. 67/kg (up 20% y-o-y) indicates strong realisation (largely flat q-o-q) and benefit of operating leverage (utilisation rate of 75%).
- Management expects muted demand in near term and has guided for 10% volume growth for H1FY23. It now expects optimum utilisation of expanded capacity to be delayed by 3-6 months from earlier guidance of Sep'23. Debottlenecking plan to expand existing capacity in order to cater to the rise in demand for the next 1-2 years.
- We maintain Buy on NOCIL with an unchanged PT of Rs. 348 as we expect robust 24% PAT CAGR over FY22-24E led by potential gain in global market share (benefit of China Plus One strategy) and sustained strong margin. Valuation of 19x/17x FY23E/FY24E EPS seems reasonable considering strong growth prospects.

NOCIL report robust Q1FY23 results with consolidated Q1FY23 revenue at Rs. 509 crore (up 47.7% y-o-y; up 10% q-o-q), which was 8% above our estimates of Rs. 473 crore on account of 9% beat in sales volume to 15,251 tonnes (up 16% y-o-y; up 11% q-o-q). Blended realisation of Rs. 334/kg (down 0.9% q-o-q) was largely in line with expectation of Rs. 337/kg. EBITDA margin improved by 20% y-o-y (down 17% q-o-q) to Rs. 67/kg and was significantly above our estimate of Rs. 57/kg led by higher-than-expected gross margin at Rs. 155/kg (up 19.5% y-o-y and 9% above our estimate) and benefit of operating leverage (sharp volume growth). Margins declined sequentially due to exceptionally higher margins in Q4FY22. Consequently, operating profit/PAT at Rs. 103 crore/Rs. 66 crore, up 39%/40% y-o-y and 29%/36% above our estimate supported by strong volume and margin performance.

Key positives

- Sharp beat in gross/EBITDA margins at Rs. 155/Rs. 67 per kg, up 19.5%/19.8% y-o-y and above the average of previous quarters.
- Better than expected volume at 15,251 tonnes, up 11% q-o-q versus our estimate of 9% q-o-q rise.
- Company improved domestic market share to 42-43%.

Key negatives

- Muted demand outlook in near term is due to recessionary environment and now NOCIL expects a 3-6 month delay in achieving optimum capacity utilisation versus earlier guidance of September 2023.

Management Commentary

- Muted demand outlook in the coming months due to recessionary environment and guided for 10% volume growth in H1FY23.
- Management did not give specific margin guidance but stated that current deltas are maintained by all industry players. Raw material prices are likely to remain flat in near term.
- Q1FY23 utilisation level was at 75% and due to recessionary environment, company now expects its earlier target to achieve optimum capacity utilisation by Sep 2023 could get extended by 3-6 months.
- Domestic market share is at 42-43% and the company aims to increase revenue share of exports to 40% versus 35% in FY22.
- Company is looking at debottlenecking existing capacities at a small capex and the same would help it cater to demand for another 1-2 years.

Revision in estimates – We have increased our FY23 earnings estimates to factor higher margin assumption partially offset by lower volume growth. We have fine-tuned our FY24 earnings estimates.

Our Call

Valuation – Maintain Buy on NOCIL with an unchanged PT of Rs. 348: We believe that the strong growth outlook for tyre industry and resilient price environment would result in volume/margin-led earnings growth. NOCIL is a play on import substitution and China Plus One strategy by global customers and the same would drive market share gains with improved financials. Valuation of 19.4x/17.1x FY23E/FY24E EPS is attractive considering our expectation of a sharp 1.5x rise in earnings over FY22-24E and improvement in RoE to 16% (versus 12.9% in FY22). Hence, we maintain a Buy on NOCIL with an unchanged PT of Rs. 348.

Key Risks

A slowdown in auto/tyre industry and delay in ramp-up of new capacity could impact volume growth. Competition from Chinese players could affect pricing and margins.

Valuation (Consolidated) Rs cr

Particulars	FY21	FY22	FY23E	FY24E
Revenue	925	1,571	2,046	2,273
OPM (%)	14.1	18.2	17.5	17.5
Adjusted PAT	88	176	239	271
Adjusted EPS (Rs.)	5.3	10.6	14.3	16.2
P/E (x)	52.2	26.3	19.4	17.1
EV/EBITDA (x)	35.0	16.1	12.5	11.3
RoNW (%)	7.2	12.9	15.7	16.1
RoCE (%)	6.9	16.0	18.0	18.0

Source: Company; Sharekhan estimates

Stellar Q1 performance with beat on all fronts

Consolidated Q1FY23 revenue at Rs. 509 crore (up 47.7% y-o-y; up 10% q-o-q), was 8% above our estimates of Rs. 473 crore on account of a 9% beat in sales volume to 15,251 tonnes (up 16% y-o-y; up 11% q-o-q). Blended realisation of Rs. 334/kg (down 0.9% q-o-q) was largely in line with expectation of Rs. 337/kg. EBITDA margin improved by 20% y-o-y (down 17% q-o-q) to Rs. 67/kg and was significantly above our estimate of Rs. 57/kg led by higher-than-expected gross margin at Rs. 155/kg (up 19.5% y-o-y and 9% above our estimate) and benefit of operating leverage (sharp volume growth). Margins declined sequentially due to exceptionally higher margins in Q4FY22. Consequently, operating profit/PAT at Rs. 103 crore/Rs. 66 crore, up 39%/40% y-o-y and 29%/36% above our estimate supported by strong volume and margin performance.

Q1FY23 conference call highlights

- **Demand outlook:** Company expects muted demand in the coming months and guided for 10% volume growth in H1FY23 given decent demand traction from domestic tyre industry (both OEM and replacement).
- **Margin outlook:** Management did not give margin outlook as raw material prices have been volatile. R.M prices however stayed flat sequentially and the management expects the trend to continue for the next month. Further the management indicated the product deltas are maintained by all players in the industry.
- **Utilization guidance:** Q1FY23 utilisation level was at 75%. Due to recessionary environment company said that its earlier target to achieve full capacity utilisation by September 2023 has been extended by 3-6 months.
- **Market Share:** Company has improved it market share to 42-43% and aims to further increase it going forward.
- **Debottlenecking capacity to capture demand:** The company is looking at debottlenecking of exiting capacities at a small capex and the same would help it cater to demand for another 1-2 years. Company will decide on further capacity expansion once the global situation improves. Land utilisation at Navi Mumbai facility is at 100% and at the Dahej facility it is at 50-60%, thus having further scope for brownfield expansion.
- **Domestic versus export sales:** Q1FY23 revenue mix was 68:32 for domestic and export sales. Sequential growth for domestic sales was higher than exports sales as there is de-growth in the global economy. The company targets to improve its export share to 40% going forward.

Results (consolidated) Rs cr

Particulars	Q1FY23	Q1FY22	YoY (%)	Q4FY22	QoQ (%)
Revenue	**509**	**345**	**47.7**	**463**	**10.0**
Total Expenditure	406	271	50.0	351	15.6
Operating profit	**103**	**74**	**39.2**	**111**	**-7.9**
Other Income	1	1	29.6	1	-13.2
Interest	0	0	21.7	0	-28.2
Depreciation	14	11	29.9	16	-16.0
PBT	90	64	40.7	96	-6.5
Tax	23	16	41.9	27	-14.1
Reported PAT	**66**	**47**	**40.2**	**69**	**-3.5**
Equity Cap (cr)	17	17		17	
Reported EPS (Rs.)	4.0	2.9	39.9	4.1	-3.5
Margins (%)			**BPS**		**BPS**
OPM	20.2	21.4	-123.8	24.1	-391.7
NPM	13.1	13.8	-69.9	14.9	-183.0
Tax rate	25.9	25.6	22.7	28.2	-229.4

Source: Company, Sharekhan Research

Key operating metrics

Particulars	Q1FY23	Q1FY22	YoY (%)	Q4FY22	QoQ (%)
Volume (tonnes)	15,251	13,130	16.2%	13,736	11.0%
Realisation (Rs. /kg)	334	262	27.2%	337	-0.9%
RM cost (Rs. /kg)	179	133	34.7%	168	6.2%
Gross margin (Rs. /kg)	155	130	19.5%	169	-8.1%
EBITDA margin (Rs. /kg)	67	56	19.8%	81	-17.1%

Source: Company, Sharekhan Research

Outlook and Valuation

■ **Sector view - Import substitution and export opportunities bode well for domestic rubber chemical players**

Global rubber consumption stands at ~30 million tonnes annually and of this, rubber chemical has a ~3.5% share and is dominated by China, which accounts for ~75% of global rubber chemical production. Global customers are shifting sourcing of rubber chemicals from China to India and this provides strong export growth opportunities for domestic players like NOCIL. Additionally, domestic demand for rubber chemicals is also expected to remain strong supported by restriction on tyre imports, improvement in tyre demand from both OEM and replacement market and capex by tyre companies to expand capacity. Moreover, a potential anti-dumping duty on major rubber chemicals would result in import substitution and drive up domestic players' volumes.

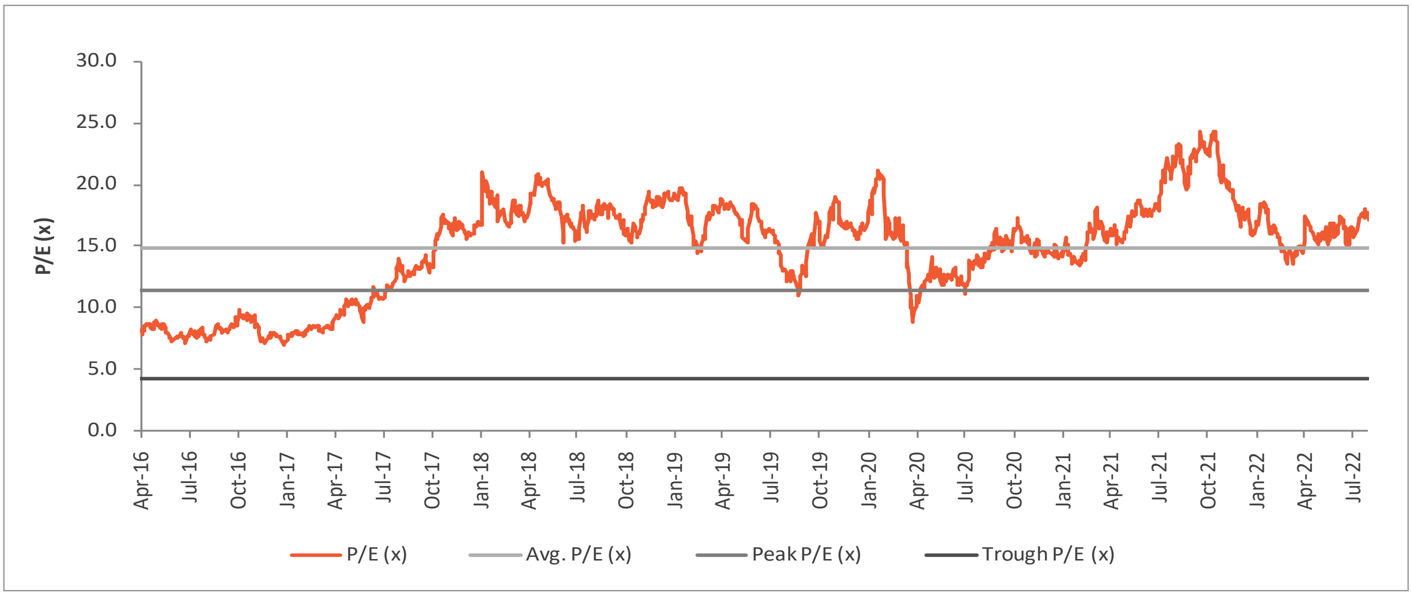
■ **Company outlook - Volume and margin growth to drive 24% PAT CAGR over FY22-24E**

NOCIL has recently doubled production capacity to 110,000 tonnes in time for a rubber chemical demand recovery cycle both in domestic and export markets. We thus expect a 21% volume CAGR over FY2022-FY2024E. Ramp-up in utilisation rates and strong pricing environment would mean sustained high margin of >Rs. 50/kg. Thus, we expect NOCIL's PAT to register a 24% CAGR over FY2022-FY2024E.

■ **Valuation - Maintain Buy on NOCIL with an unchanged PT of Rs. 348**

We believe that the strong growth outlook for tyre industry and resilient price environment would result in volume/margin-led earnings growth. NOCIL is a play on import substitution and China Plus One strategy by global customers and the same would drive market share gains with improved financials. Valuation of 19.4x/17.1x FY23E/FY24E EPS is attractive considering our expectation of a sharp 1.5x rise in earnings over FY22-24E and improvement in RoE to 16% (versus 12.9% in FY22). Hence, we maintain a Buy on NOCIL with an unchanged PT of Rs. 348.

One-year forward P/E (x) band



Source: Sharekhan Research

About company

NOCIL, incorporated in 1975, is part of Arvind Mafatlal Group and is the largest rubber chemical manufacturer in India with production capacity of 110 ktpa and market share of ~42%/5% in domestic/global markets. The company has presence in over 40 countries with exports accounting for 36% of FY2022 revenues. The business segments include Accelerator, Anti-oxidant, Pre/Post vulcanization inhibitor/stabilizer and Zinc based applications.

Investment theme

NOCIL is the key beneficiary of China plus one strategy and import substitution in niche market of rubber chemicals. Recent doubling of capacity has made in third largest rubber chemical manufacturers in term of capacity and ramp-up of utilisation would drive sustainable double digit volume growth and help expand global market share to ~8% over next 2-3 years as compared to 5% currently. Volume growth coupled with margin expansion would drive strong earnings growth and consistent FCF generation. Balance sheet remains strong with net cash position.

Key Risks

- Slowdown in auto/tyre industry and delay in ramp-up of new capacity could impact volume growth.
- Competition from Chinese players could impact pricing and margin.

Additional Data

Key management personnel

Mr. Hrishikesh Arvind Mafatlal	Chairman
Mr. S.R. Deo	Managing Director
P Srinivasan	Chief Financial Officer

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Tejas Trivedi	1.75
2	Trivedi Shivani Tejas	1.63
3	Canara Robeco Asset Management Co Ltd	1.52
4	Aagam Agencies Pvt Ltd	1.16
5	HN Safal Infra Space Pvt Ltd	1.10
6	IDFC Mutual Fund	1.04
7	Trivedi Minaxi Balchandra	0.99
8	Trivedi Khushi Tejas	0.99
9	Dimensional Fund Advisors LP	0.89
10	Deo Sudhir Ramchandra	0.48

Source: Bloomberg

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 detoriating 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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