Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Stock Update

Result Update

Astral Ltd

Healthy outlook barring near-term OPM woes

Building material	Sharekhan code: ASTRAL

Reco/View: Buy	↔	CMP: Rs. 1,986	Upside potential: 2,300	↑

↑ 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		↔	

ESG Disclosure Score NEW

ESG RISK RATING 26.37

Updated July 08, 2022

Medium Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

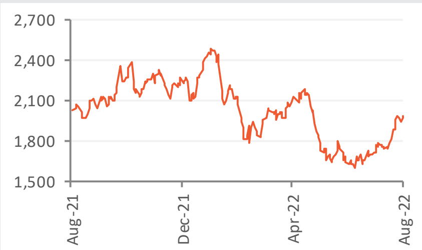
Company details

Market cap:	Rs. 39,897 cr
52-week high/low:	Rs. 2,525/1,584
NSE volume: (No of shares)	1.6 lakh
BSE code:	532830
NSE code:	ASTRAL
Free float: (No of shares)	8.89 cr

Shareholding (%)

Promoters	56
DII	14
FII	16
Others	15

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	12.0	15.0	0.5	-2.5
Relative to Sensex	0.8	2.3	-4.9	-9.7

Sharekhan Research, Bloomberg

Summary

- We retain a Buy on Astral Limited (Astral) with a revised price target of Rs. 2300 owing to strong growth potential in its existing and new businesses.
- In Q1, the company reported higher than expected revenues although OPM disappointed due to inventory losses & spends on faucets & sanitaryware. Net profit lagged owing to forex losses & amortisation related to paints business.
- Q2 may see margin pressures continuing in pipes, led by declining PVC prices. However, expected stabilising of PVC prices in H2FY2023 would lift demand.
- Its new businesses viz. plastic tanks, Valves, Paints, faucets and sanitaryware would provide a sustainable growth trajectory going ahead.

Astral Limited (Astral) reported better than expected consolidated revenues at Rs. 1213 crore, up 73% y-o-y led by strong rise in volumes (up 48.5% y-o-y) and realisations (up 17.1% y-o-y) of the pipes business (revenues up 74% y-o-y at Rs. 900 crore) while adhesive & paints revenues were up 74% y-o-y at Rs. 334 crore. OPM at 14.3% (-419bps y-o-y) disappointed led by inventory losses (~Rs. 25 crore led by declining PVC prices) and employee & launch costs for faucets & sanitaryware (Rs. 5 crores). Consequently, consolidated operating profit at Rs. 173 crore (up 34% y-o-y) lagged our estimate. Further, it booked additional amortization (Rs. 7 crores) related to its paints acquisition and forex loss (Rs. 11.7 cror) related to CPVC imports, which led to lower than expected consolidated net profit at Rs. 89 crore (up 20% y-o-y). A decline in PVC prices continued post Q1FY2023 till date and is likely to further tread downwards in the near term and is expected to lead to inventory loss in Q2FY2023. However, stabilisation of PVC prices in H2FY2023 would provide fillip to pipe demand. Its acquisition of faucet manufacturing plant at an investment of Rs. 28-30 crores has a revenue potential of Rs. 150 crore per annum and would contribute towards 80% in-house production.

Key positives

- Better-than-expected revenue growth led by strong volume growth in pipes division.
- Adhesives & paints division OPM at 13.8% owing to GEM paints OPM of 15% during Q1FY2023.

Key negatives

- Pipes saw a 527 bps correction in OPM at 15.4% led by inventory losses and spends towards new businesses of faucets and sanitaryware.
- PVC prices continue to tread downward post Q1FY2023 till date which is likely to result in inventory losses in Q2FY2023.

Management Commentary

- It has defined two verticals viz. 1) Plumbing – Pipes, fittings, water tanks, faucets and sanitaryware and 2) Paints and Adhesives. The plumbing business reported revenues and EBITDA growth of 73% and 30% y-o-y. Adhesives reported revenues and EBITDA growth of 45% and 43% y-o-y.
- Q2 is expected to be challenging due to continuous decline in PVC prices and raw materials.
- It retained its target of doubling topline over five years on consolidated basis. The initial costs towards new businesses Faucets and Sanitaryware are likely to put pressure on OPM over 18-24 months.

Revision in estimates – We have lowered our net earnings estimates for FY2023-FY2024 factoring lower margins in Pipes vertical.

Our Call

Valuation – Retain Buy with a revised price target of Rs. 2,300: Astral is expected to feel operating margin pressure in pipes vertical in the near term due to a sustained decline in PVC prices. However, with expected stabilization of PVC prices in H2FY2023, it should benefit from revival in demand led by channel re-stocking. Further, in-house manufacturing of faucets & sanitaryware is likely to provide better operating margins for the vertical. The scale-up of new businesses viz. plastic tanks, valves, paints, faucets and sanitaryware are likely to provide sustainable growth trajectory for the company going ahead. The stock is currently trading at a P/E of 61.5x its FY2024E earnings, which we believe provides further room for an upside owing to strong growth potential for its existing and new businesses. Hence, we retain a Buy with a revised price target of Rs. 2,300.

Key Risks

- Lower demand due to an economic slowdown, a delay in the completion of expansion projects, and heightened competitive intensity might affect revenue growth.
- Higher raw material prices and a delay in the ability to pass on price hikes adequately, adverse forex fluctuations, and interest rate movements might affect margins

Valuation (Consolidated) Rs cr

Particulars	FY21	FY22	FY23E	FY24E
Revenue	3,176	4,394	5,421	6,337
OPM (%)	20.3	17.2	14.7	16.4
Adjusted PAT	404	484	478	649
% Y-o-y growth	*63.1*	*19.6*	*(1.1)*	*35.6*
Adjusted EPS (Rs.)	20.1	24.1	23.8	32.3
P/E (x)	98.7	82.5	83.4	61.5
P/B (x)	21.1	17.1	14.3	11.7
EV/EBITDA (x)	61.3	52.1	48.9	37.1
RoNW (%)	23.8	22.9	18.6	20.9
RoCE (%)	29.9	29.4	24.2	27.1

Source: Company; Sharekhan estimates

PVC price slump and one-off costs affected net earnings

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Key Conference call takeaways

- **Q1FY2023 performance:** Astral has defined two verticals viz. 1) Plumbing – Pipes, fittings, water tanks, faucets and sanitaryware and 2) Paints and Adhesives. The Plumbing business reported revenues and EBITDA growth of 73% and 30% y-o-y. Adhesives reported revenues and EBITDA growth of 45% and 43% y-o-y. The Adhesives growth was lower on account of just 4-5% y-o-y growth in its UK operations while Resinova grew by 80% y-o-y. Adhesives margins at 13.6% remained under pressure due to cost pressures. Gem paints sales grew by 91% y-o-y to Rs. 55.3 crore. Pipe volumes grew by 48% y-o-y.
- **One-off costs:** The company incurred ~Rs. 48 crore one-off costs during Q1FY2023 which includes forex loss of Rs. 11.7 crore (on account of CPVC imports), additional amortisation of Rs. 7 crores (under depreciation because of paint business consolidation), Inventory loss of ~Rs. 25 crore (decline in PVC prices), Employee costs of Rs. 1.5 crore (manpower additions in Faucets, sanitaryware etc), Launch event costs of faucets & sanitaryware of Rs. 3.5 crore (in other expenses).
- **Q2FY2023 outlook:** Q2 is expected to be challenging due to continuous decline in PVC prices and raw materials. Reliance has decreased PVC prices by Rs. 2/kg today. Q2 would have inventory losses.
- **Long term outlook:** It retained its target of doubling topline over five years on a consolidated basis. The initial costs towards new businesses Faucets and Sanitaryware are likely to put pressure on OPM over 18-24 months.
- **Expansions:** It completed its expansion in East. The Dahej adhesives plant is expected to get completed by Q3FY2023 with trial production and commercial production in Q4FY2023 and Q1FY2024 respectively. It added 8000 tonnes capacity in Q1FY2023 taking total capacity to 2,82,338 tonnes. It would be further adding 10,000 tonnes in pipes in East.
- **GEM Paints:** GEM Paints' revenues stood at Rs. 55.3 crore for Q1FY2023 with OPM of ~15%.
- **Faucet plant acquisition:** It purchased faucet manufacturing plant at Jamnagar at a cost of Rs. 22-23 crores while it would be spending another Rs. 4-5 crores for upgradation. Post upgradation, 80% of the company's requirement would be met in-house. The facility can generate Rs. 150 crore turnover. It has started first display gallery for faucets in Ahmedabad and has started appointing distributors. The sales from faucets would pick up from Q3FY2023.
- **Paints:** It has completed legal documentation. It is in NCLT approval stage for demerging of business from GEM paints.
- **Valves:** The valve technology is outsourced. It has completed 50% range while some moulds need minor corrections. In next couple of months, phase I will be completed. The phase II and III will add another category of valves.

- **Capex:** It would incur a Rs. 200 crore capex in FY2023.
- **Cash:** Consolidated cash balance stood at Rs. 542 crore including Rs. 197 crores related to GEM paints under OCD.
- **Working capital:** It maintained inventory and receivable days.

Results (Consolidated) Rs cr

Particulars	Q1FY2023	Q1FY2022	y-o-y (%)	Q4FY2022	q-o-q (%)
Revenue	**1,212.9**	**700.1**	**73.2**	**1,390.6**	**(12.8)**
EBITDA	**173.4**	**129.4**	**34.0**	**216.8**	**(20.0)**
Other Income	11.4	4.3	165.1	16.4	(30.5)
Depreciation	43.3	30.6	41.5	32.8	32.0
Finance Cost	14.4	4.6	213.0	5.2	176.9
PBT	**127.7**	**98.5**	**29.6**	**193.3**	**(33.9)**
Tax Expenses	31.6	23.4	35.0	49.2	(35.8)
PAT	96.1	75.1	28.0	144.1	(33.3)
Adj PAT	**88.9**	**73.9**	**20.3**	**141.4**	**(37.1)**
EPS (Rs)	**4.4**	**3.7**	**20.3**	**7.0**	**(37.1)**
Margin			**BPS**		**BPS**
EBITDA Margin	14.3	18.5	(419)	15.6	(129)
PAT Margin	7.9	10.7	(280)	10.4	(244)
Tax rate	24.7	23.8	99	25.5	(71)

Source: Company; Sharekhan Research

Outlook and Valuation

■ Sector View – Strong recovery in business operations

The building materials industry has been severely affected by COVID-19-led lockdowns during Q1FY2021, which had affected its peak sales period of the year. Additionally, its high fixed cost structure had affected OPM, dragging down net earnings. However, since June, the sector has been one of the fastest in recovery with the easing of the lockdown domestically. The sector witnessed a resumption of dealer and distribution networks and a sharp improvement in capacity utilisation. Most players have begun to see strong demand growth compared to pre-COVID levels. Scaling up of revenue is also expected to lead to better absorption of fixed costs going ahead, aiding net earnings recovery. The industry is expected to show strong growth in FY2022-FY2023.

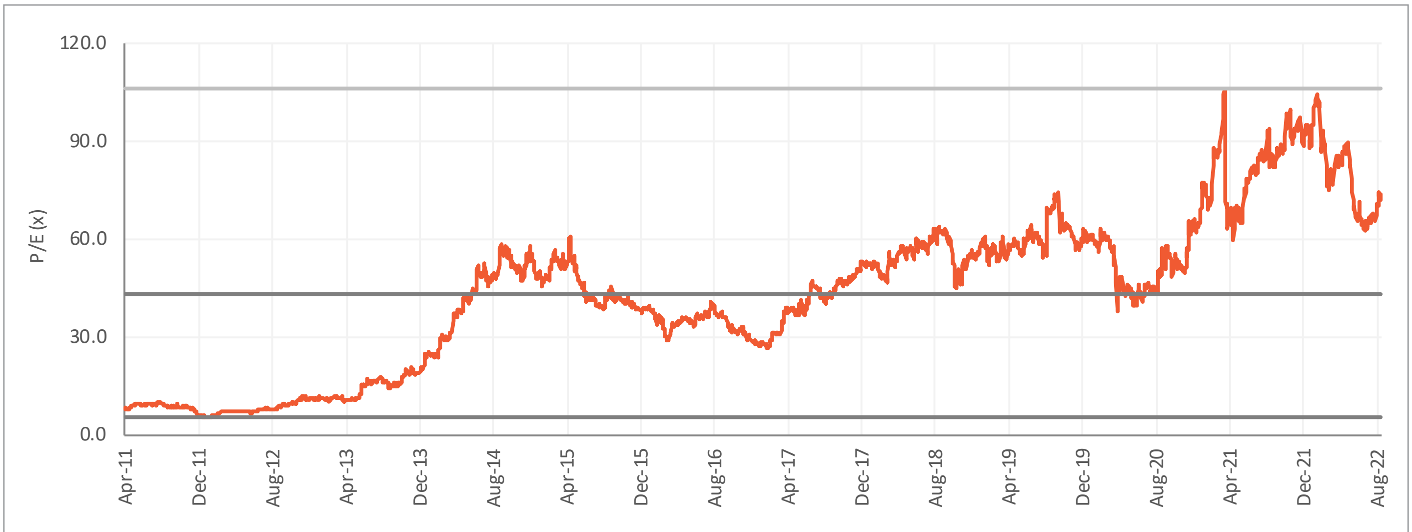
■ Company Outlook – Expect healthy growth in both Pipes and adhesives

Astral is well-positioned to capture the growth opportunities unveiled by the government through its various schemes such as Housing for All by 2022, *PMAY, Smart Cities Mission, AMRUT, HRIDAY, Har Ghar Jal* by 2024, Nal se Jal by 2024, and PMKSY. Capacity expansion and improved utilisation of expanded capacity to drive volume growth in the pipes business. Strategic steps taken during the last year in the adhesive business have now expected to show favourable results in a normalized environment. Both pipes and adhesives businesses are expected to fare well over the long-term with pipe volumes expected to grow at 15% per annum, while adhesive is expected to grow at 15-20% per annum. Further, the company would be scaling up its new products.

■ Valuation – Retain Buy with a revised price target of Rs. 2300

Astral is expected to feel operating margin pressure in pipes vertical in the near term due to a sustained decline in PVC prices. However, with expected stabilization of PVC prices in H2FY2023, it should benefit from revival in demand led by channel re-stocking. Further, in-house manufacturing of faucets & sanitaryware is likely to provide better operating margins for the vertical. The scale-up of new businesses viz. plastic tanks, valves, paints, faucets and sanitaryware are likely to provide sustainable growth trajectory for the company going ahead. The stock is currently trading at a P/E of 61.5x its FY2024E earnings, which we believe provides further room for an upside owing to strong growth potential for its existing and new businesses. Hence, we retain a Buy with a revised price target of Rs. 2,300.

One-year forward P/E (x) band



Source: Sharekhan Research

Peer Comparison

Particulars	P/E (x)		EV/EBITDA (x)		P/BV (x)		RoE (%)	
	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E
Astral Ltd	83.4	61.5	48.9	37.1	14.3	11.7	18.6	20.9
Pidilite Industries	85.9	65.2	56.6	43.6	18.0	14.9	22.5	25.0

Source: Company, Sharekhan estimates

About company

Established in 1996, Astral is among the country's leading manufacturers of plastic pipes used across industries. The company is now making strong inroads into the adhesives segment and infrastructure products. Astral currently operates in four countries with manufacturing facilities at 12 locations spread across India, the UK, US, and Kenya, having over 4,000 employees. The company has over 800 and 1,800 distributors in the plastic and adhesive segments, respectively. Astral is present across India through more than 30,000 and 4lakh dealers in the plastic and adhesive segments.

Investment theme

Currently, Astral has a market share of 25% in CVPC pipes and 5% in PVC pipes and is well placed to grab the significant growth opportunities unveiled by the government through its various schemes such as Housing for All by 2022, *PMAY, Smart Cities Mission, AMRUT, HRIDAY, Har Ghar Jal* by2024, Nal se Jal by 2024, and PMKSY. Strategic steps over the past year in the adhesive business have now expected to show favourable results in a normalized environment. Both pipes and adhesives businesses of the company are expected to fare well over the long term with pipes volumes expected to grow at 15% per annum while adhesives expected to grow at 20-25% per annum. Further, the company would be scaling up its tank business complementing its pipe business.

Key Risks

- Lower demand offtake due to the economic slowdown and delay in completion of expansion projects coupled with increased competitive intensity might affect revenue growth momentum.
- Higher raw-material prices and delay in the ability to pass on price hikes adequately, adverse forex fluctuations, and interest rate movement might affect margins.

Additional Data

Key management personnel

Sandeep Pravinbhai Engineer	Chairman cum Managing Director
Jagruti Sandeep Engineer	Executive Director
Hiranand A Savlani	Chief Financial Officer
Krunal Bhatt	Company Secretary and Compliance Officer

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Engineer Sandip Pravinbhai	31.39
2	Saumya Polymers	9.85
3	Steadview Capital Mauritius Ltd	7.90
4	Engineer Jagruti Sandeep	7.59
5	Kairav Chemicals Pvt Ltd	6.90
6	Axis Asset Management Co Ltd	3.89
7	UTI Asset Management Co Ltd	2.54
8	Tree Line Asia Master Fund	2.24
9	ICICI Prudential Life Insurance Co Ltd	1.11
10	Parikh Vijay Suresh	0.91

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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