

Strong quarter amid glyphosate restriction noise...

About the stock: Incorporated in 2000, Sumitomo Chemical India (SCI) is present in the three business verticals of agro solutions (ASD), environmental health (EHD) and animal nutrition business (AND).

- SCI provides solutions for insecticide, herbicide, fungicide, plant growth regulator (PGR) under agro segment. Under animal nutrition, it manufactures methionine for feed additive use
- In terms of revenue contribution, insecticide constitutes ~51% while ~19% is from herbicide, 9% from fungicide and 20% from other segments like PGR, AND & EHD

Q2FY23 Results: Topline numbers were slightly above our estimates led by strong growth from herbicide and insecticides while EBITDA and PAT were in line.

- Reported revenue was up 23.2% YoY to ₹ 1121.7 crore, led by 103.4% YoY growth in herbicide along with 13.8% YoY growth in insecticides
- Gross margins were down 110 bps YoY to 37.9% while EBITDA margin rose 120 bps YoY to 24.8%
- EBITDA was up 30% YoY to ₹ 278 crore while PAT increased 31% YoY to ₹ 201.5 crore

What should investors do? The stock appreciated at 20% CAGR in last two years.

- We retain **BUY** rating on the back of 1) Better growth outlook from outsourcing opportunity of SCC Japan, 2) management capability to tackle glyphosate situation and 3) increase in farmer's income and the company's ability to pass on the elevated cost

Target Price and Valuation: We value Sumitomo Chemicals at 45x FY24E EPS of ₹ 38.7 to arrive at a target price of ₹ 570/share (earlier ₹ 565/share).

Key triggers for future price performance:

- Upcoming capex for five molecules, which will be supplied to SCC Japan. Capex has been earmarked at ₹ 120 crore with an asset turn of ~2-2.5x
- Potential opportunity of technical manufacturing for Nufarm to improve export share meaningfully
- Allocation of incremental FCF towards organic/inorganic growth likely to expand return ratios further

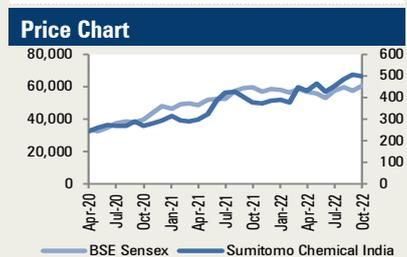
Alternate Stock Idea: Apart from Sumitomo Chemicals, in our chemical coverage we like PI Industries.

- Trigger for PI Industries' future revenue growth would be strong order backlog in CSM and proposed foray into pharma CDMO
- BUY with a target price of ₹ 3710.



Particulars	
Particular	Amount
Market cap (₹ Crore)	24,735
FY22 Total Debt (₹ Crore)	0
FY22 Cash & Inv (₹ Crore)	435
EV (₹ Crore)	24,300
52 Week H/L	541/341
Equity Capital (₹ Crore)	499.1
Face Value (₹)	10

Shareholding pattern				
in %	Dec-21	Mar-22	Jun-22	Sep-22
Promoter	75.0	75.0	75.0	75.0
DII	6.2	6.4	6.7	6.4
FII	1.4	1.7	1.9	2.1
Others	17.5	17.0	16.4	16.6



- ### Recent event & key risks
- Domestic segment witnessed strong growth in the quarter
 - **Key Risk:** (i) Restriction on use of glyphosate (herbicide product) in India. (ii) Higher RMAT prices and inability to pass on could impact gross margins

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Key Financial Summary

(₹ Crore)	FY19	FY20	FY21	FY22	4 year CAGR (FY18-22)	FY23E	FY24E	2 year CAGR (FY22-24E)
Net Revenue	2,228.4	2,424.7	2,644.9	3,064.6	12.5%	3,740.6	4,237.7	17.6%
EBITDA	290.6	333.2	486.9	599.9	28.9%	763.1	873.0	20.6%
EBITDA Margins (%)	13.0%	13.7%	18.4%	19.6%		20.4%	20.6%	
Adj. PAT	165.7	204.7	345.4	423.5	30.7%	555.2	635.5	22.5%
Adj. EPS (₹)	3.3	4.1	6.9	8.5		11.1	12.7	
EV/EBITDA	46.5x	73.3x	49.5x	40.3x		31.2x	26.8x	
P/E	148.5x	120.2x	71.2x	58.1x		44.3x	38.7x	
ROE (%)	15.8	16.8	22.4	22.0		22.9	21.2	
ROCE (%)	25.3	24.8	29.8	30.2		30.7	28.5	

Key takeaways of recent quarter & conference call highlight

Q2FY23 Results: Strong growth from herbicides, fungicides lead overall performance

- **Domestic business:** Revenues grew 21.1% YoY to ₹ 918.4 crore, largely driven by robust growth from branded business, which was up 70% YoY to ₹ 783.9 crore. Revenue from bulk business was up 15.9% YoY to ₹ 133.6 crore

Export business: Revenue increased 18% YoY to ₹ 203.3 crore, driven by bulk and branded business. The revenue from the bulk business was up 33% YoY to ₹ 150.3 crore while the same from branded rose 34% YoY to ₹ 53 crore. In terms of geography, revenue from Asia (excluding India) surged 85% YoY to ₹ 33.7 crore while the same from Africa was at ₹ 35 crore (up 80% YoY)

Q2FY23 Earnings Conference Call highlights

Industry Overview

- Overall trend of monsoons was erratic. Several regions received less than normal rainfall while some other regions received normal to abnormally surplus rainfall. Across several districts in Bihar, Jharkhand, West Bengal sowing of Kharif crop was less than 75% due to deficiency in rains
- Rain in September & October has helped in adapting the soil moisture and water reservoir to the coming Rabi season
- Income of farmers has grown in the range of 1.3-1.7x, which the management believes is a welcome sign for the company
- Another growth driver for the quarter's results was increase in minimum support price (MSP). MSP has increased by 1.5-2.3x
- SCI witnessed a global increase in stakes of herbicide and better sales of branded generics. Despite the agrochemical industry taking price hikes, falling raw material prices from July 2022 onwards amid high cost carrying inventory has likely impacted gross margins of Indian agrochemical industry
- The company was able to fully pass on rising cost to customers, which resulted in improved margins compared to the overall industry

Business Update:

- SCI has seen robust growth in the export market in H1 (up +53% YoY)
- Volumes and prices sales contributed in expansion of animal nutrition and EHD. Demand for herbicide, fungicide, insecticide, PGR remains strong. The company was successful in garnering market share from unorganised player during the quarter
- Herbicide, PGR, bio-rational products are key segments in which the company expects to see most growth, stability and profit. The management is also planning to expand PGR segment in future
- During H1, the company has launched three insecticides, one fungicide, one metal phosphide and three PGR products. The management plans to launch a few more products in the coming Rabi season
- Bio rational – Key market is India. It come from the US (subsidiary of Sumitomo Japan). Three products to get registered under Fertiliser Act in India. Free trials are done. The management believes it will start production in FY24

Capex update:

- In FY21 – Two Make in India projects were launched. Additional capex apart from maintenance and capital enhancement was at ₹ 120 crore. Objective of the project was to make five SSC proprietary products for the parent company and affiliate all over the world

- Timeline for other projects
 - Bhavnagar – Important global proprietary product has begun commercial production recently. The company expects revenue from H2FY23 and full revenue next year
 - Tarapur – Involves multiple products for the parent company and is expected to begin commercial production in Q1FY24
 - Expected EBITDA margins will be comparable to margins the company is earning on similar projects. The company believes that if global demand for product rises then it will have enough capacity to expand the market

Glyphosate:

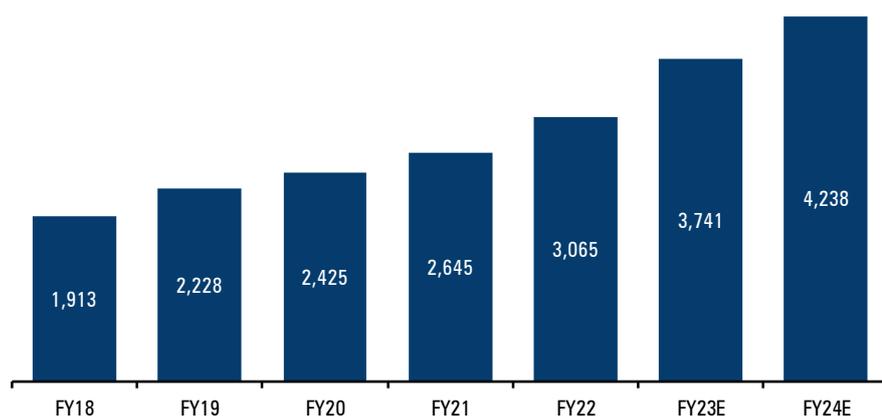
- The management pointed out that the government has put restrictions on mode of usage and not banned buying or selling of glyphosate or its use (spraying has to be done from authorised pest control operators).
- Statistics for H1FY23 of glyphosate product
 - Domestic sales volumes came down by 40% YoY
 - Export sales volumes increased 451% YoY to 54 crore. Domestic sales of glyphosate are 85% of total glyphosate revenue and export sales is 15%
 - In Rabi season i.e. H2, glyphosate products are generally exported from India
 - Size of glyphosate market is in the range of ₹ 1100-1200 crore. The company share is ~35-40%
- Solutions that can be adopted by the management to tackle the situation
 - The company can offer value added solutions to farmers by way of creating the infrastructure to become a pest control operator (PCO). SCI sees this as a possible move
 - The company requires at least three to six months to develop this infrastructure. Simultaneously, it will request the government to provide some time by removing restrictions
- The management believes that glyphosate is an important and economical product for farmers. There is no replacement for glyphosate in the market currently
- For PCO – The management expects training period of 15 days with minimal fees. Spraying cost for farmers will be ~₹ 300-500 per acre. Thus, this creates an opportunity for the company

Other Update:

- Working capital has increased to 94 days in H1FY23 compared to 72 days in H1FY22. This was due to high inventory levels during the period and slow receivables

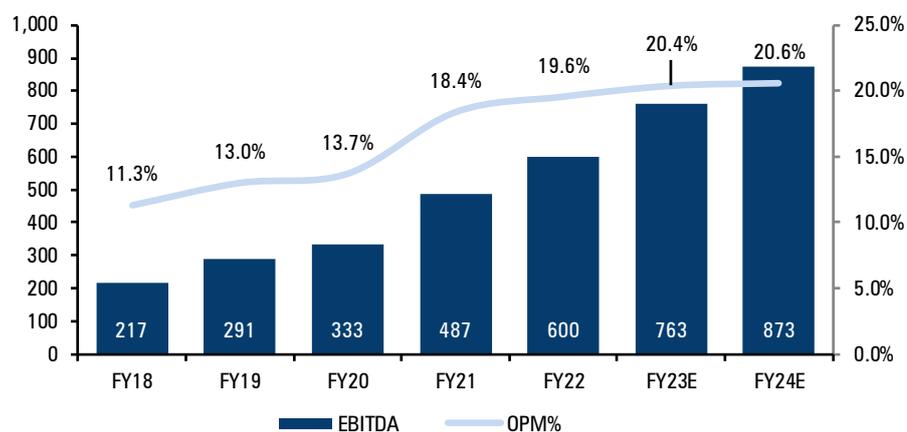
Financial story in charts....

Exhibit 1: Revenue trend (₹ crore)



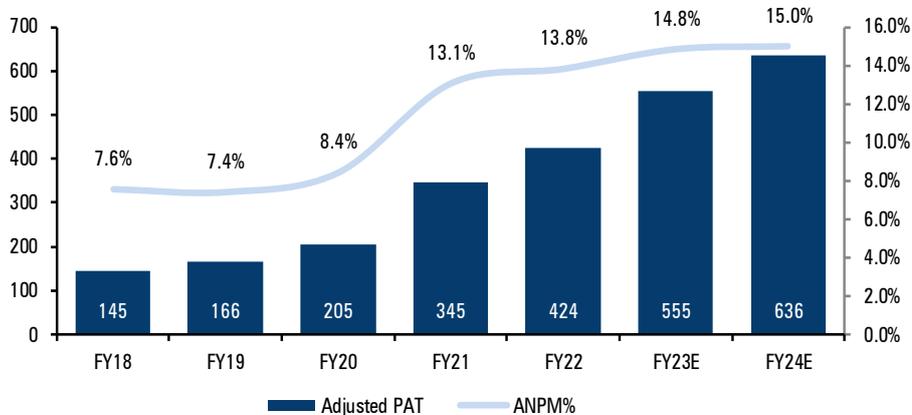
Source: Company, ICICI Direct Research

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



Source: Company, ICICI Direct Research

Exhibit 3: PAT growth trend (₹ crore)



Source: Company, ICICI Direct Research

Financial summary

Exhibit 4: Profit and loss statement				
	₹ crore			
Year end March	FY21	FY22	FY23E	FY24E
Net Revenues	2,644.9	3,064.6	3,740.6	4,237.7
Cost Of Revenues	1,655.4	1,908.0	2,319.2	2,627.4
Gross Profit	989.5	1,156.6	1,421.4	1,610.3
Employee Cost	194.3	202.0	235.7	262.7
Other Operating Expenses	308.4	354.7	422.7	474.6
EBITDA	486.9	599.9	763.1	873.0
Other Income	18.6	26.8	26.7	32.3
EBITDA, including OI	505.4	626.7	789.7	905.3
Depreciation	46.6	44.8	43.5	52.0
Net Interest Exp.	5.6	6.2	6.0	6.0
Other exceptional items	0.0	0.0	0.0	0.0
PBT	453.3	575.7	740.2	847.3
Taxes	107.9	152.2	185.1	211.8
Tax Rate	23.8%	26.4%	25.0%	25.0%
PAT	345.4	423.5	555.2	635.5
Adjusted Net Profit	345.4	423.5	555.2	635.5
Adj. EPS (INR)	6.9	8.5	11.1	12.7
Shares Outstanding	49.9	49.9	49.9	49.9

Source: Company, ICICI Direct Research

Exhibit 5: Cash flow statement				
	₹ crore			
Year end March	FY21	FY22	FY23E	FY24E
PBT & Extraordinary	453.3	575.7	740.2	847.3
Depreciation	46.6	44.8	43.5	52.0
After other adjustments				
(Inc) / Dec in Working Capital	25.6	-257.6	-49.7	-88.1
Taxes	-107.9	-142.6	-185.1	-211.8
Others	7.9	1.5	6.0	6.0
Cash from Ops.	425.4	221.8	555.0	605.4
Purchase of Fixed Assets	-43.3	-113.5	-130.0	-135.0
Others	-214.4	-176.7	0.0	0.0
Cash from Investing	-257.7	-290.2	-130.0	-135.0
Proceeds from issue of shares	0.0	0.0	0.0	0.0
Borrowings (Net)	0.0	0.0	0.0	0.0
Others	-47.1	-62.6	-61.5	-69.6
Cash from Financing	-47.1	-62.6	-61.5	-69.6
Net Change in Cash	120.7	-131.1	363.5	400.9
Effects of foreign currency translation	0.0	0.0	0.0	0.0
BF Cash & Bank	93.5	242.1	79.1	442.6
END Cash & Bank	242.1	79.1	442.6	843.5

Source: Company, ICICI Direct Research

Exhibit 6: Balance sheet				
	₹ crore			
Year end March	FY21	FY22	FY23E	FY24E
Liabilities				
Share Capital	499.1	499.1	499.1	499.1
Reserves	1,042.1	1,428.1	1,927.7	2,499.7
Total Shareholders Funds	1,541.2	1,927.2	2,426.9	2,998.8
Minority Interest	0.1	0.0	0.0	0.0
Long Term Borrowings	0.0	0.0	0.0	0.0
Net Deferred Tax liability	5.0	13.9	13.9	13.9
Other long term liabilities	15.3	24.7	0.0	0.0
Long term provisions	29.2	22.3	27.3	30.9
Current Liabilities and Provisions				
Short term borrowings	0.0	0.0	0.0	0.0
Trade Payables	598.3	517.2	717.4	870.8
Other Current Liabilities	475.2	497.1	614.9	696.6
Short Term Provisions	5.6	7.2	8.7	9.9
Total Current Liabilities	1,079.2	1,021.4	1,341.0	1,577.3
Total Liabilities	2,670.1	3,009.6	3,809.0	4,620.9
Assets				
Net Block	309.3	390.4	427.9	505.9
Capital Work in Progress	4.3	21.1	70.0	75.0
Intangible assets under devl.	10.0	14.1	14.1	14.1
Goodwill on Consolidation	0.0	0.0	0.0	0.0
Non-current investments	0.1	0.1	0.1	0.1
Deferred tax assets	18.5	30.0	30.0	30.0
Long term loans and advances	6.0	0.8	0.9	1.0
Other Non Current Assets	17.6	31.2	38.0	43.1
Current Assets, Loans & Advances				
Current Investments	290.2	356.0	356.0	356.0
Inventories	754.4	937.8	1,178.5	1,277.1
Sundry Debtors	848.2	843.1	1,024.8	1,219.1
Cash and Bank	242.1	79.1	442.6	843.5
Loans and Advances	7.7	0.5	0.5	0.5
Other Current assets	161.7	305.5	225.5	255.4
Current Assets	2,304.3	2,522.0	3,227.9	3,951.6
Total Assets	2,670.1	3,009.6	3,809.0	4,620.9

Source: Company, ICICI Direct Research

Exhibit 7: Key ratios				
Year end March	FY21	FY22	FY23E	FY24E
Per share data (₹)				
Adj. EPS	6.9	8.5	11.1	12.7
Adj. Cash EPS	7.9	9.4	12.0	13.8
BV	30.9	38.6	48.6	60.1
DPS	0.0	1.0	1.1	1.3
Operating Ratios (%)				
Gross Margin (%)	37.4	37.7	38.0	38.0
EBITDA Margin (%)	18.4	19.6	20.4	20.6
PAT Margin (%)	13.1	13.8	14.8	15.0
Debtor Days	117	100	100	105
Inventory Days	104	112	115	110
Creditor Days	83	62	70	75
Cash Conversion Cycle	139	151	145	140
Return Ratios (%)				
Return on Assets (%)	12.9	14.1	14.6	13.8
RoCE (%)	29.8	30.2	30.7	28.5
RoE (%)	22.4	22.0	22.9	21.2
Solvency				
Total Debt / Equity	-	-	-	-
Interest Coverage	NM	NM	NM	NM
Current Ratio	2.1	2.5	2.4	2.5
Quick Ratio	1.4	1.6	1.5	1.7
Valuation Ratios (x)				
EV/EBITDA	49.5	40.3	31.2	26.8
P/E	71.2	58.1	44.3	38.7
P/B	16.0	12.8	10.1	8.2
EV/Sales	9.1	7.9	6.4	5.5

Source: Company, ICICI Direct Research

Exhibit 8: ICICI Direct coverage universe (Chemicals)

Company	CMP			M Cap (₹ Cr)	EPS (₹)			P/E (x)			EV/EBITDA (x)			RoCE (%)			RoE (%)		
	(₹)	TP(₹)	Rating		FY22	FY23E	FY24E	FY22	FY23E	FY24E	FY22	FY23E	FY24E	FY22	FY23E	FY24E	FY22	FY23E	FY24E
SRF	2520	2,735	Buy	74,699	63.5	68.9	82.7	36.1	33.2	27.7	22.4	20.6	17.0	23.8	21.6	22.5	22.1	20.3	20.4
PI Industries	2987	3,710	Buy	45,324	55.5	67.2	82.4	57.6	47.6	38.8	40.8	34.2	27.8	16.3	17.1	18.2	13.8	14.5	15.2
Aarti Industries	768	885	Hold	27,822	36.1	25.1	31.6	22.7	32.7	25.9	24.0	19.6	16.0	12.0	13.0	13.9	13.3	13.5	14.8
Tata Chemical	1134	1,345	Buy	28,832	47.5	61.2	70.7	23.9	18.5	16.0	14.4	11.1	8.5	6.6	8.1	8.8	6.6	8.0	8.6
Vinati Organics	2016	2,320	Hold	20,717	33.7	40.1	51.5	56.0	47.1	36.7	44.7	37.0	28.3	24.3	23.2	23.9	19.0	19.1	20.5
Sumitomo Chemical	493	570	Buy	24,735	8.5	11.2	12.9	58.1	44.1	38.3	40.3	31.0	26.6	30.2	30.9	28.7	22.0	23.0	21.4
Navin Fluorine	4400	4,570	Hold	21,738	52.3	64.4	91.4	84.2	68.3	48.1	61.2	45.5	31.3	17.8	18.0	20.1	14.0	15.2	18.4
Rallis India	227	250	Hold	4,420	8.4	8.9	12.4	26.9	25.6	18.3	15.5	15.6	11.1	12.7	11.6	15.3	9.7	9.5	12.1
Sudarshan chemical	416	515	Hold	2,882	18.8	19.3	28.5	24.0	23.3	15.8	14.2	12.8	9.6	10.9	11.3	15.4	15.6	14.3	18.3
Neogen Chemicals	1513	1,645	Buy	3,773	17.9	27.2	32.9	79.5	52.2	43.2	41.8	30.2	25.0	12.0	15.0	16.2	10.2	13.6	14.3
Astec Lifesciences	1867	2,215	Buy	3,660	45.1	54.8	69.3	39.7	32.7	25.9	24.6	20.7	16.5	19.3	17.7	19.4	22.3	21.3	21.2

Source: Bloomberg, ICICI Direct Research

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Buy: >15%

Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



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