Stock Update

Result Update

Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Astral Ltd

Lofty valuation; Downgrade to reduce

Building material	Sharekhan code: ASTRAL
Reco/View: Reduce ↓	CMP: Rs. 2,035 / Price Target: Rs. 1,825 ↓

↑ 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 Dec 08, 2022

Medium Risk

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

Source: Morningstar

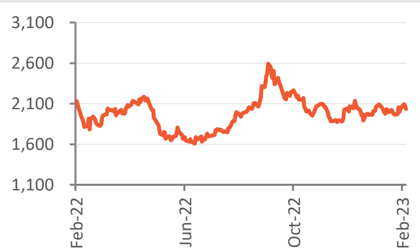
Company details

Market cap:	Rs. 41,000 cr
52-week high/low:	Rs. 2,654 / 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
FII	15
DII	15
Others	14

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-2.7	-2.8	4.9	-4.6
Relative to Sensex	-2.6	-2.1	1.7	-8.4

Sharekhan Research, Bloomberg

Summary

- We downgrade Astral Limited (Astral) to Reduce with a revised price target of Rs. 1825 led by downwardly revised estimates and unfavourable risk reward ratio at current valuation.
- In Q3, the company reported better than expected consolidated revenues led by strong volume growth in plumbing business. OPM stayed in-line affected by inventory losses. Net profi dip 27% y-o-y.
- Sustained demand environment to lead to healthy volume growth for FY2023 along with long term volume growth pegged at 12-15% y-o-y in plumbing. Reversal of raw material prices to improve OPM going ahead.
- The adhesives business is expected to face slower growth than earlier expected while bathware segment would require scale to make contribution to overall profitability. The scale-up of new businesses to be focus areas.

Astral Limited (Astral) reported better than expected consolidated revenues at Rs. 1268 crore (up 15% y-o-y) as its plumbing segment reported 11% y-o-y growth in revenues at Rs. 932 crores (aided by 30% y-o-y growth in volumes while blended realisations declined 15% y-o-y). Paints & Adhesive reported 29% y-o-y growth in revenues at Rs. 336 crore (flat q-o-q). Consolidated OPM at 14.7% (down 322bps y-o-y) stayed in line affected by inventory losses in both Piping and Paints & Adhesives. Weak OPM y-o-y and higher interest and depreciation led by operating profit/net profit decline of 6%/27% y-o-y at Rs. 186 crore/Rs. 93 crore. Post Q3FY2023, PVC prices remained stable, while the benefit of rise in PVC prices from December onwards is expected to lead to the possibility of inventory gain in the plumbing business in Q4FY2023. Sustained healthy demand environment is expected to lead to high double digit revenue growth for FY2023 while long term volume growth is pegged at 12-15% y-o-y. The management remains focused on scaling up the tank business (target to cross Rs. 100 crore by FY2023 end), bath-ware business (500 dealer display centres by FY2023 end), valves (120 SKUs by Q4FY2023) and higher contribution from paints business.

Key positives

- Revenues were higher than estimates led by strong 30% y-o-y growth (up 13% q-o-q) in the Plumbing business.
- OPMs in Plumbing improved over 200bps q-o-q to 15.4% despite higher inventory loss of ~Rs. 25 crore booked during the quarter. There might be an inventory gain in Q4FY2023 with a rise in PVC prices from December 2022.

Key negatives

- Adhesives segment reported flattish q-o-q revenues with a 44bps dip in OPM owing to weak demand in rural segment and inventory loss in raw materials for chemicals.
- Other income stood at negative two crores owing to Rs. 5.5 crore loss in its UK operations.

Management Commentary

- It would be growing at a high double-digit in volumes during FY2023. Over the long term, it retained its conservative volume growth guidance of 12-15% y-o-y. it maintained its long-term guidance of doubling revenues every five years. It has announced a bonus issue of 1:3.
- It incurred Rs. 190 crore capex during 9MFY2023, including Jamnagar faucet plant capex. Another Rs. 35-40 crore will be incurred for the balance fiscal.
- Adjusting for the UK business loss of Rs. 5.5 crore, adjusted EBITDA margins in Adhesives was 13.8%. Adjusting for Rs. 4 crore loss of Sanitary business, adjusted piping business margins were 15.83%.

Revision in estimates – We have lowered our net earnings estimates for FY2023-FY2025, factoring lower growth in adhesives business along with marginal downward revision in margins in the Pipes vertical.

Our Call

Valuation – Downgrade to Reduce with a revised price target of Rs. 1,825: Astral, like its industry peers, is expected to benefit from a strong demand environment led by the reversal of PVC prices since December 2022 along with expected improvement in operating margins from Q4FY2023. However, the adhesives business is expected to face slower growth than earlier expected while bath ware segment would require scale to make a contribution to overall profitability. The scale-up of new businesses viz. plastic tanks, valves, paints, faucets and sanitaryware, would remain key focus areas for the company. The stock is currently trading at a P/E of 81x/65x its FY2024E/FY2025E earnings, which we believe provides unfavourable risk reward ratio considering 31% CAGR in net earnings over FY2023E-FY2025E. Hence, we downgrade the stock to Reduce with a revised price target of Rs. 1,825, factoring downwardly revised estimates and an unfavourable risk reward ratio.

Key Risks

- Sharp improvement in adhesives business growth run-rate along with the profitability of bath ware business.
- Faster scale-up in revenues and profitability in new business verticals.

Valuation (Consolidated) Rs cr

Particulars	FY22	FY23E	FY24E	FY25E
Revenue	4,394	5,045	5,821	6,746
OPM (%)	17.2	13.5	14.6	15.4
Adjusted PAT	484	370	502	633
% Y-o-y growth	*19.6*	*(23.6)*	*35.9*	*26.0*
Adjusted EPS (Rs.)	24.1	18.4	25.0	31.5
P/E (x)	84.6	110.7	81.4	64.6
P/B (x)	17.5	15.2	12.9	10.8
EV/EBITDA (x)	53.4	59.4	47.1	38.3
RoNW (%)	22.9	14.7	17.2	18.2
RoCE (%)	29.4	19.7	22.7	23.9

Source: Company; Sharekhan estimates

Revenues above estimate while OPM stayed in-line

Astral reported consolidated net revenues growth of 15% y-o-y (+8.2% q-o-q) at Rs. 1268 crore, which was 13% higher than our estimate. The revenues from the Pipes segment grew by 11% y-o-y (+11% q-o-q) to Rs. 932 crore. The volumes in Pipes division grew by 30% y-o-y (+13% q-o-q), while realizations declined by 17% y-o-y (-1% q-o-q). The revenues from adhesive business rose 29% y-o-y (flat q-o-q) to Rs. 336 crores. The company reported consolidated OPM at 14.7% (-386bps y-o-y, +241bps q-o-q), which was in line with our estimate of 14.6%. Pipe business EBITDA margin stood at 15.4% (-484bps y-o-y, +193bps q-o-q) while adhesives was at 12.2% (-189bps y-o-y, -44bps q-o-q). Consolidate operating profit declined by 9% y-o-y (+29% q-o-q) at Rs. 186 crore, which was 14% higher than our estimate. Weak OPM, along with higher interest expense (up 4.7x y-o-y), depreciation (up 42% y-o-y) and lower other income, led to a consolidated net profit decline of 27% y-o-y (+35% q-o-q) at Rs. 93 crore (versus our estimate of Rs. 89 crore). The company approved the issue of bonus shares in the proportion of 1:3. Consolidated cash and bank balances as at December 31, 2022 was Rs. 477 crores.

Key Conference Call Takeaways

- **Guidance:** It would be growing at a high double-digit in volumes during FY2023. Over the long term, it retained its conservative volume growth guidance of 12-15% y-o-y. it maintained its long-term guidance of doubling revenues every five years. It has announced a bonus issue of 1:3.
- **Q3FY2023 performance:** Consolidated revenues were up 15% y-o-y while EBITDA declined by 9.5% y-o-y because of inventory loss in RM for both PVC and chemicals. The inventory loss in PVC has estimated at Rs. 25 crore for Q3FY2023. The piping business reported 15.4% EBITDA margin, while Adhesives reported 12.2% EBITDA margin. Adjusting for the UK business loss of Rs. 5.5 crore, adjusted EBITDA margins in Adhesives was 13.8%. Adjusting for Rs. 4 crore loss of Sanitary business, adjusted piping business margins were 15.83%.
- **Piping business:** It operated at 57% capacity utilisation during 9MFY2023. PVC prices increased by Rs. 13 per kg in December while remaining stable since January 2023.
- **Adhesives:** It operated at 55-60% capacity utilisation during 9MFY2023. There was some pressure on demand in Q3FY2023 due to weak rural demand. Its UK operations remained under pressure affecting overseas revenues. It is shutting down some capacity at Unnav, Kanpur and shifting it to Dahej.
- **Valves:** It has started generating revenues from a few SKUs and by Q4FY2023, it expects all 120 SKUs to be in the market. It expects good numbers in FY2024.
- **Adhesives:** The high cost inventory due to falling chemical prices impacted margins. It would see improvement in margins from Q4FY2023 onwards.
- **Paints:** Over 9MFY2023, the division has grown by 15% y-o-y. In Q3FY2023, the revenues from paints stood at Rs. 52 crores with 12.6% EBITDA margins (adjusted for the UK, margin were 14.5%).
- **Bathware:** It completed 231 showrooms/display centres, and 80 more are under construction. It is planning to have 500 showrooms/display centres by FY2023 end. The project pipeline looks healthy while it has quoted for 25000 bathrooms and has supplied 3800 crores already. From FY2024, it expects good numbers. For Q3FY2023, the segment reported Rs. 9.68 crore revenues with a loss of Rs. 4-4.5 crores. For 9MFY2023, the segment made loss of Rs. 13 crores.
- **Tanks:** Currently, margins in the tank business I 12-13% which is expected to settle down around 14-15% going ahead.
- **Dahej:** The Dahej plant can generate Rs. 1800 crore in revenues from Rs. 1000 crore with addition of adhesives business.
- **Other income:** The other income stood at a negative two crore on account of netting off Rs. 5.5 crore losses in the U.K. and Rs. 3 crore gain in other treasury operations.
- **Capex:** It incurred Rs. 190 crore capex during 9MFY2023, including Jamnagar faucet plant capex. Another Rs. 35-40 crore will be incurred for the balance fiscal.

Results (Consolidated) **Rs cr**

Particulars	Q3FY2023	Q3FY2022	Y-o-Y %	Q2FY2023	Q-o-Q %
Revenue	**1,267.8**	**1,102.7**	**15.0**	**1,171.6**	**8.2**
EBITDA	**186.4**	**204.7**	**(8.9)**	**144.0**	**29.4**
Other Income	(2.0)	6.2	(132.3)	10.9	(118.3)
Depreciation	45.5	32.1	41.7	44.8	1.6
Finance Cost	9.4	2.0	370.0	14.0	(32.9)
PBT	**129.5**	**169.7**	**(23.7)**	**96.1**	**34.8**
Tax Expenses	34.6	41.8	(17.2)	24.1	43.6
PAT	94.9	127.9	(25.8)	72.0	31.8
Adj PAT	**93.0**	**127.3**	**(26.9)**	**69.1**	**34.6**
EPS (Rs)	**4.6**	**6.3**	**(26.9)**	**3.4**	**34.6**
Margin			**BPS**		**BPS**
EBITDA Margin	14.7	18.6	(386)	12.3	241
PAT Margin	7.5	11.6	(411)	6.1	134
Tax rate	26.7	24.6	209	25.1	164

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, affecting its peak sales period. 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.

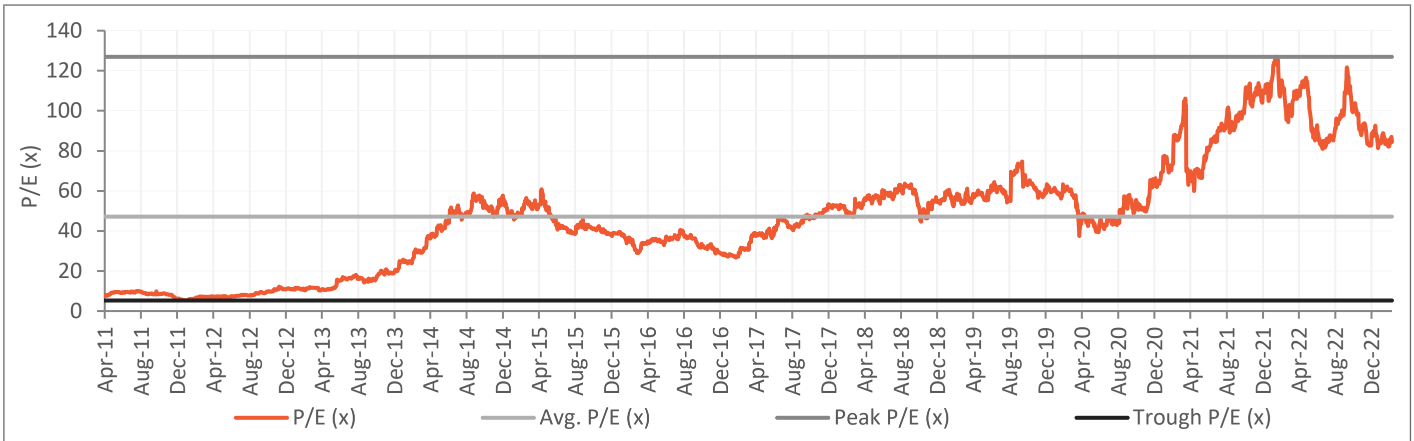
■ Company Outlook – Expect healthy growth in both Pipes and adhesives

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 normalised 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 20-25% per annum. Further, the company would be scaling up its new products.

■ Valuation – Downgrade to Reduce with a revised price target of Rs. 1825

Astral, like its industry peers, is expected to benefit from strong demand environment led by a reversal of PVC prices since December 2022 along with expected improvement in operating margins from Q4FY2023. However, the adhesives business is expected to face slower growth than earlier expected, while bathware segment would require scale to contribute to overall profitability. The scale-up of new businesses viz. plastic tanks, valves, paints, faucets and sanitaryware would remain key focus areas for the company. The stock is currently trading at a P/E of 81x/65x its FY2024E/FY2025E earnings, which we believe provides an unfavourable risk-reward ratio considering 31% CAGR in net earnings over FY2023E-FY2025E. Hence, we downgrade the stock to Reduce with a revised price target of Rs. 1,825, factoring downwardly revised estimates and unfavourable risk-reward ratio.

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	110.7	81.4	59.4	47.1	15.2	12.9	14.7	17.2
Pidilite Industries	83.1	59.1	54.3	39.5	16.2	13.4	20.8	24.8

Source: Sharekhan Research

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, the US, and Kenya, having over 4,000 employees. The company has over 800 and 1,800 distributors in the plastic and adhesive segments. 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 normalised environment. The company's pipes and adhesives businesses are expected to fare well over the long term, with pipes volumes expected to grow at 15% per annum while adhesives are expected to grow at 20-25% per annum. Further, the company would be scaling up its tank business, complementing its pipe business.

Key Risks

- Sharp improvement in adhesives business growth run-rate along with the profitability of bathware business.
- Faster scale-up in revenues and profitability in new business verticals.

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 Sandeep Pravinbhai	31.58
2	SAUMYA POLYMERS	9.83
3	Engineer Jagruti Sandeep	7.56
4	Kairav Chemicals Ltd	6.88
5	Axis Asset Management Co Ltd/India	3.81
6	Steadview Capital Mauritius Ltd	2.76
7	UTI Asset Management Co Ltd	2.22
8	Life Insurance Corp of India	2.11
9	Tree Line Asia Master Fund	1.5
10	Vanguard Group Inc/The	1.45

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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