

Deepak Nitrite

BSE SENSEX

59,606

S&P CNX

17,511

CMP: INR1,789 TP: INR1,890 (+6%)
Neutral


Stock Info

Bloomberg	DN IN
Equity Shares (m)	136
M.Cap.(INRb)/(USDb)	244 / 2.9
52-Week Range (INR)	2390 / 1682
1, 6, 12 Rel. Per (%)	-2/-10/-14
12M Avg Val (INR M)	1565
Free float (%)	54.3

Financials Snapshot (INR b)

Y/E March	FY23E	FY24E	FY25E
Sales	80.3	85.9	94.1
EBITDA	12.6	18.4	19.9
PAT	8.3	12.2	13.1
EPS (INR)	60.7	89.3	96.3
EPS Gr. (%)	(22.4)	47.2	7.7
BV/Sh.(INR)	296.3	372.3	454.1

Ratios

Net D:E	0.1	(0.0)	(0.1)
RoE (%)	22.4	26.7	23.3
RoCE (%)	20.4	24.9	22.6
Payout (%)	15.0	15.0	15.0

Valuations

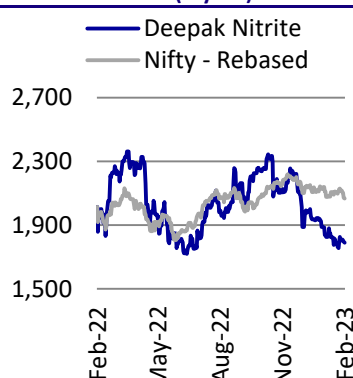
P/E (x)	29.7	20.2	18.8
P/BV (x)	6.1	4.8	4.0
EV/EBITDA (x)	19.8	13.3	12.0
Div. Yield (%)	0.5	0.7	0.8
FCF Yield (%)	0.2	2.6	3.9

Shareholding pattern (%)

As On	Dec-22	Sep-22	Dec-21
Promoter	45.7	45.7	45.7
DII	13.8	12.0	10.7
FII	8.7	8.5	8.8
Others	31.8	33.8	34.7

FII Includes depository receipts

Stock Performance (1-year)



Headwinds to persist as new capacities are added

- The phenol/acetone spread over raw materials has declined 16% YoY to INR90/kg during 2HFY23 till date (v/s INR107/kg in 2HFY22) on account of China's Covid-related lockdowns, which resulted in stockpiling of Phenol and disruption in trade activities.
- China's steps toward self-sufficiency in phenol and increased competition in the region could result in a structural glut in the overall market, in turn leading to the downtrend in phenol margins to continue.
- DN's planned capex of INR15b in FY23-24 aimed partly for backward integration and partly towards downstream products of Acetone (MIBK/MIBC) should drive growth in the near term. Moreover, the recently announced INR10b expansion into Polycarbonate compounding & Nitrite project in Oman would drive growth in the medium term.
- Although the company has aggressive growth plans, the commodity nature of its products does not leave much upside for investors. If it forays into specialty products or complex commodities, it would certainly command a better valuation multiple. We reiterate our Neutral recommendation with a target price of INR1,890.

Phenolic division margins expected to remain under pressure

- EBIT margins of DN's phenolic segment slipped to 8% in 2QFY23, the lowest level since 4QFY20. While margins improved sequentially to 11% in 3QFY23, they remain below the long term average of INR96/kg. With the phenol/acetone spread remaining flat QoQ at ~INR90/kg in 4QFY23 till date, margins are also expected to remain subdued.
- According to World Integrated Trade Solution (WITS), China is the single largest importer of phenol globally and accounted for ~52% of the top ten global phenol importing countries in CY20. With China moving toward self-sufficiency through capacity additions supported by increased feedstock availability (benzene & propylene) due to Beijing refinery restructuring, phenol realizations may see structural weakness going forward.
- Additionally, increased competition in the Asian phenolic market, due to the entry of global giant INEOS through Mitsui Chemicals' acquisition, may also lead to a glut if demand does not keep up pace with supply.

Downstream products to lead next leg of volume growth

- Upcoming capacities of MIBK (40ktpa), MIBC (8ktpa) and Polycarbonate should drive volume growth going ahead. While we do not expect margin accretion since the products are commodities in nature, vertical integration may lead to some reduction in margin volatility.
- MIBK is primarily used as a solvent for resins used in the paints and coatings industry. It could be an ideal import substitution play, considering India's entire MIBK demand of ~30,000mtpa is exclusively met through imports.
- Polycarbonate is a transparent thermoplastic polymer widely used in the electrical/electronics industry due to its excellent heat and electrical resistance property. According to ChemAnalyst, India's Polycarbonate demand stood at 180,000mtpa in FY22 and is expected to grow by ~4% over the next decade, driven by the building and construction materials end market.

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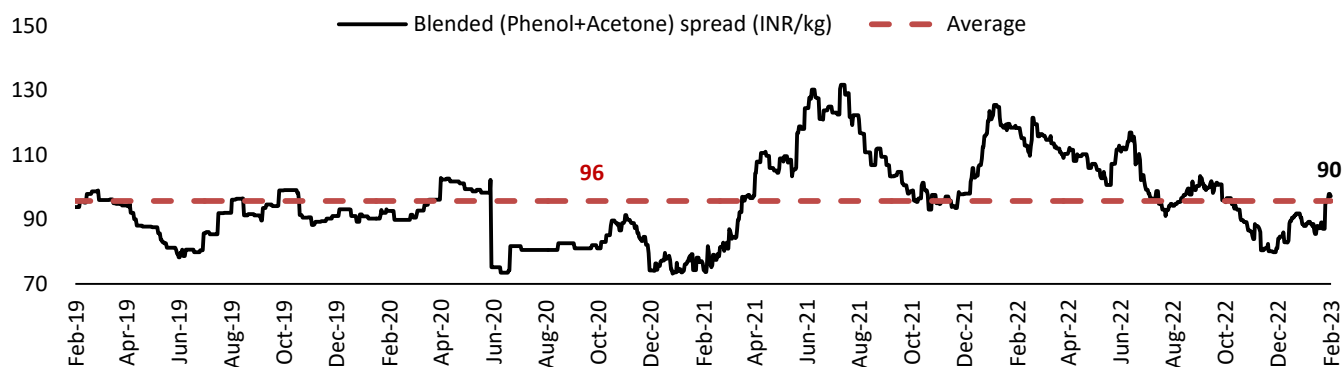
Motilal Oswal research is available on www.motilaloswal.com/Institutional-Equities, Bloomberg, Thomson Reuters, Factset and S&P Capital.

- Covestro, the world leader in Polycarbonate, expects a 4% CAGR in the global polycarbonate market till CY26, while the supply is expected to grow by 5-6% during the same period, led by major capacity additions in China by Hainan Huasheng, ZPC, SABIC-Sinopec, Wanhua and Shemna.

Valuation and View

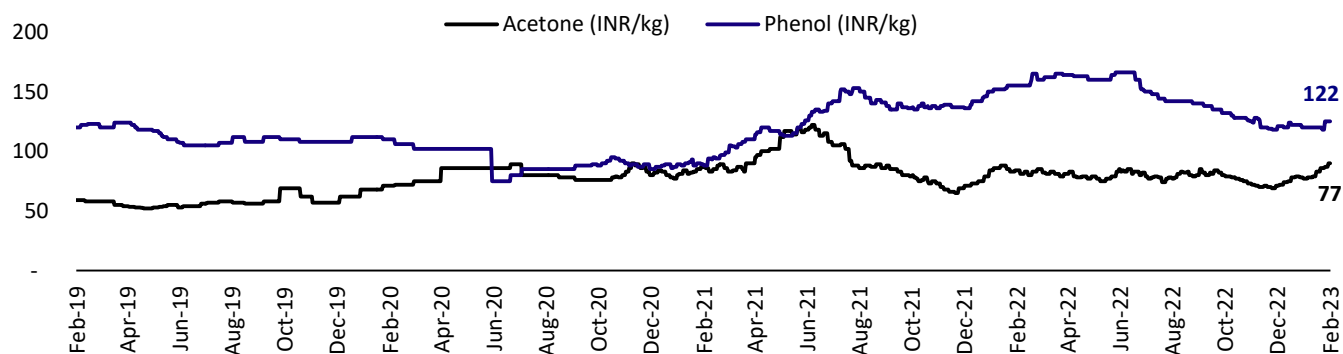
- The company aims to become the largest player in Solvents, with a play on import substitution. It has already announced its foray into MIBK (40ktpa), MIBC (8ktpa) and Polycarbonate.
- Despite a capex of INR20b over the next three years, DN is expected to turn net cash positive by FY24 with FCF generation of INR16.5b over FY23-25. Return ratios are expected to be at 24-27%, significantly lower than that of FY22.
- The company is on an aggressive path for backward as well as forward integration. However, the complete basket of products is commodity and the current valuation appears rich. We maintain our Neutral rating with a TP of INR1,890, valuing DN at 20x Dec'24E EPS of INR95.

Exhibit 1: Phenol/Acetone spread over raw materials has remained flat at QoQ at INR90/kg during 4QFY23'td

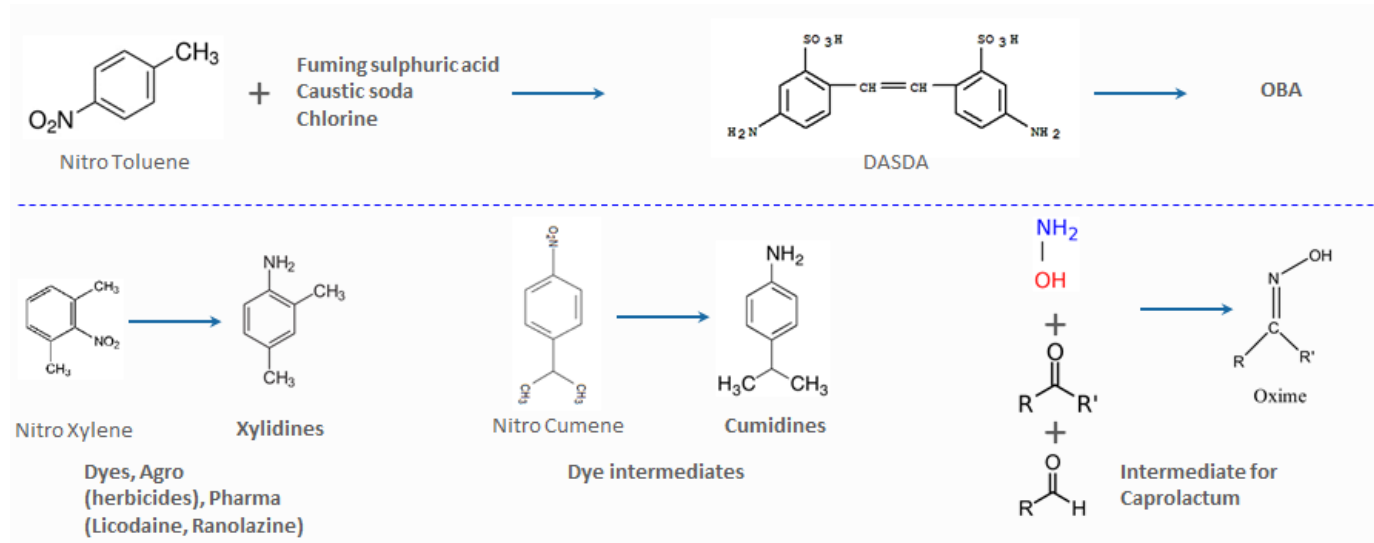


Source: Indianpetrochem, MOFSL

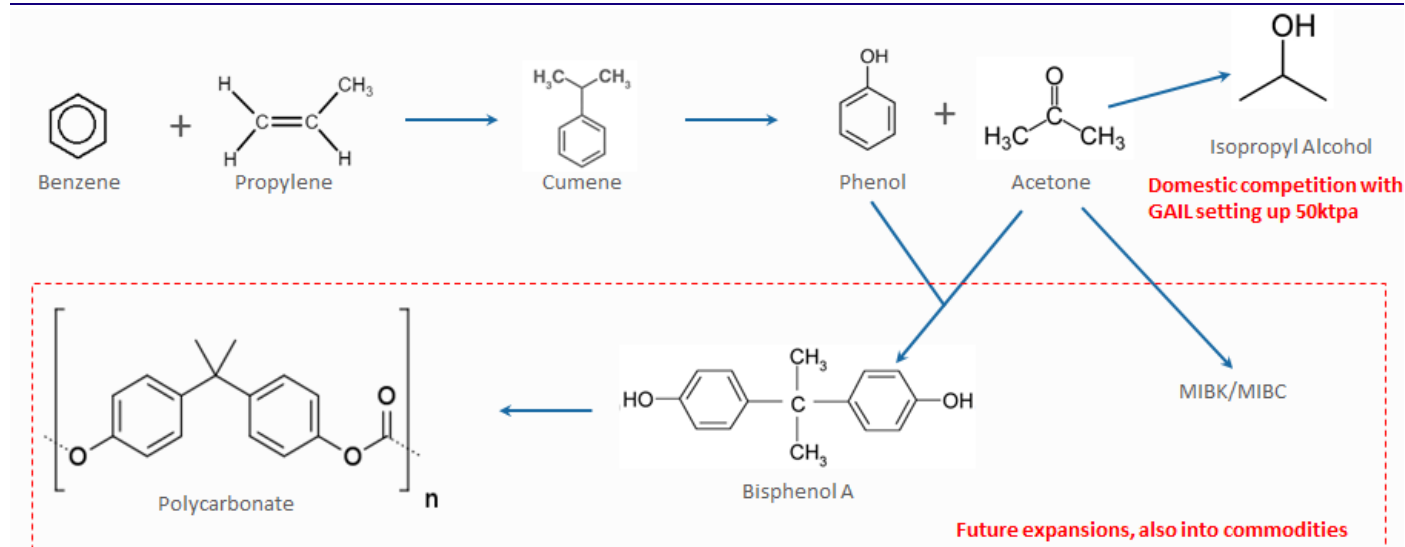
Exhibit 2: Phenol prices have come down in 4QFY23'td v/s 3QFY23, while Acetone prices have increased during the same period



Source: Indianpetrochem, MOFSL

Exhibit 3: DN's legacy products have been commodities

Source: Company, MOFSL

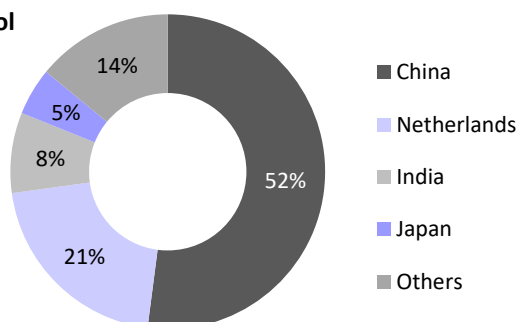
Exhibit 4: Upcoming phenol downstream products are also commodities in nature

Source: Company, MOFSL

Exhibit 5: 52% of the total Phenol imports by the top 10 importing countries is done by China (as of CY20)

as a % of top 10 importing countries

Phenol

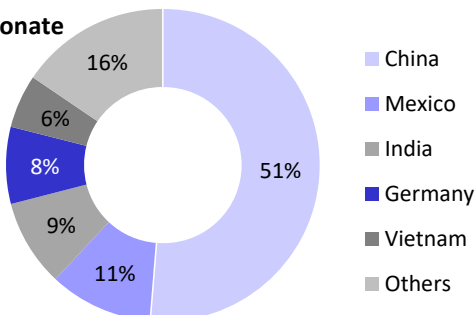


Source: WITS, MOFSL

Exhibit 6: India is the third largest importer of Polycarbonate in the world (as of CY21)

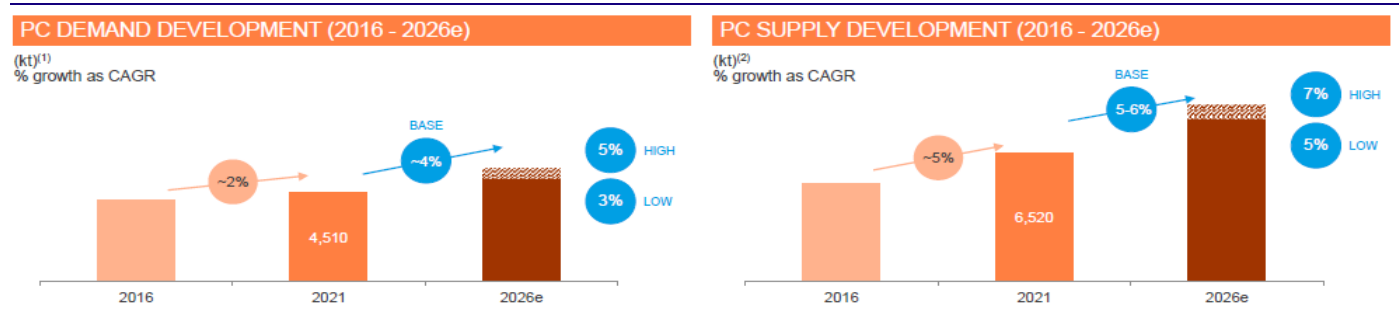
as a % of top 10 importing countries

Polycarbonate



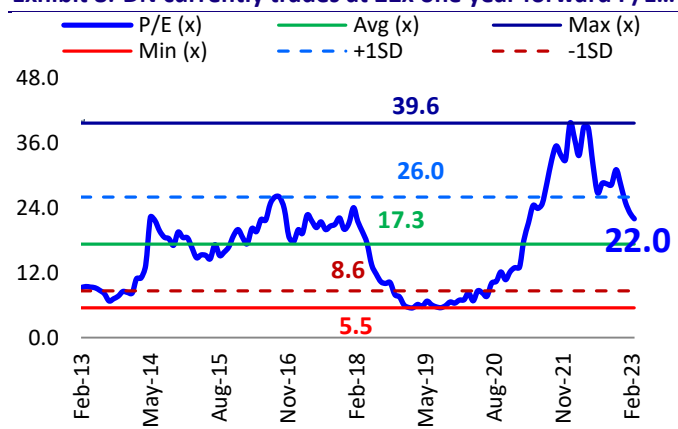
Source: WITS, MOFSL

Exhibit 7: Expect a 4% CAGR in the global Polycarbonate market till CY26, while the supply is expected to grow by 5-6% during the same period



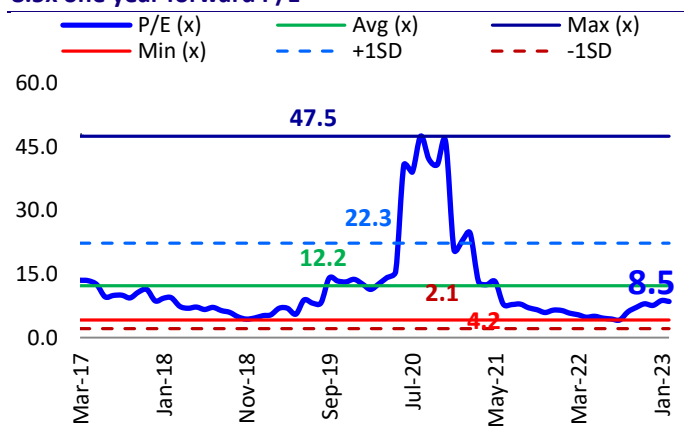
Source: Covestro, MOFSL

Exhibit 8: DN currently trades at 22x one year forward P/E...



Source: MOFSL

Exhibit 9: ...while Covestro, an international peer, trades at 8.5x one year forward P/E



Source: MOFSL

Exhibit 10: INEOS's acquisition of Mitsui Chemicals was also at modest valuation of 4.6x EV/EBITDA

Valuation metrics	CY21	Remarks
Acquired at	330	USD m
	26,235	INR m
Sales	750	USD m
	59,625	INR m
EBITDA	5,715	INR m
USD/ INR	80	as of 14th Sep'22
EBITDA Margin	10%	On Mitsui's Basic Materials division
EV/ EBITDA (x)	4.6	

Source: Mitsui Chemicals, MOFSL

Story in charts

Exhibit 11: Revenue growth is expected to peak as product prices in DPL normalize going forward...

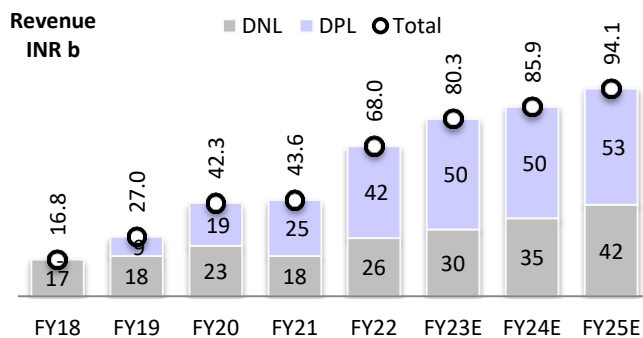


Exhibit 12: ...resulting in a lower contribution from DPL in the total revenue mix

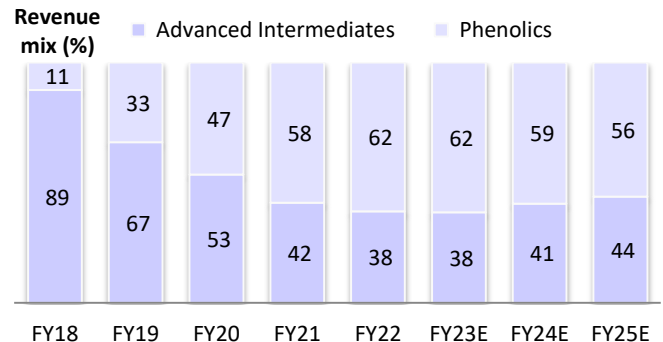


Exhibit 13: Expect normalized EBIT margins to be at ~16-17%...

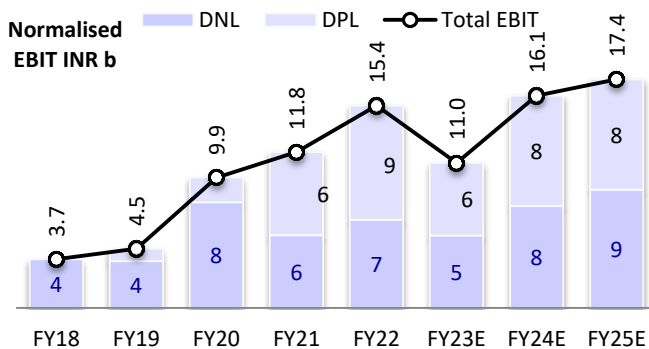


Exhibit 14: ...with Advanced Intermediates still enjoying higher EBIT margins (estimate ~22%)

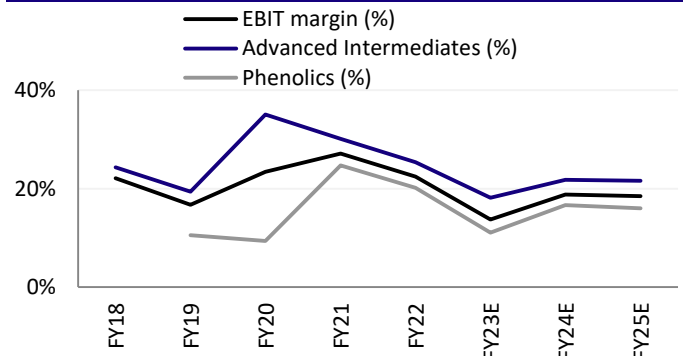


Exhibit 15: : EBITDA margins to normalize from FY22 levels

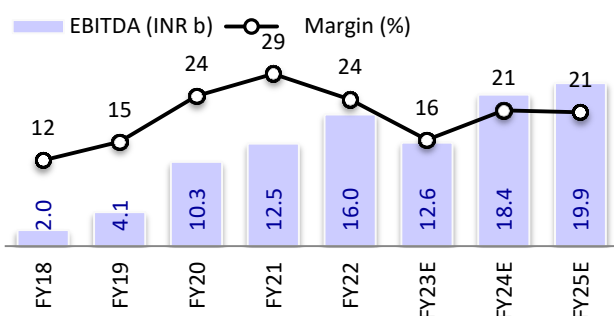


Exhibit 16: Expect ~7% PAT CAGR over FY23-25E

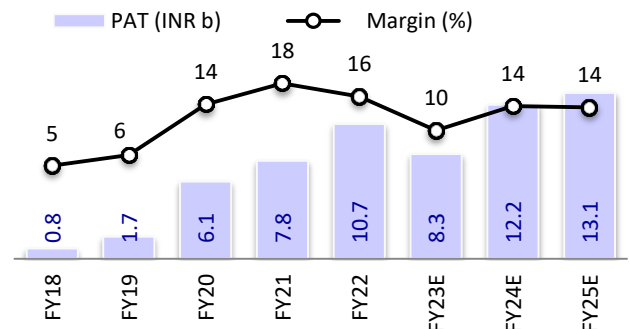


Exhibit 17: DN to incur ~INR20b in capex over FY23-24E...

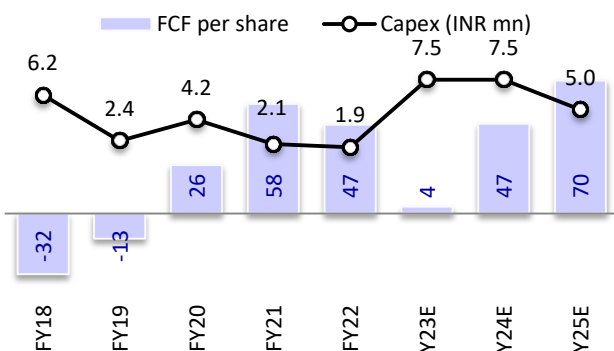
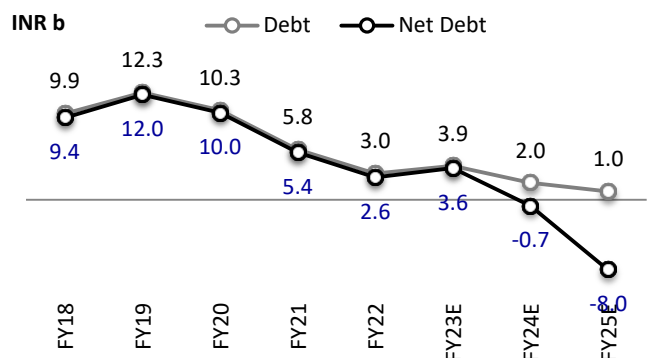


Exhibit 18: ...but is likely to turn net cash positive in FY24E



Source: Company, MOFSL

Source: Company, MOFSL

Financials and valuations

Consolidated - Income Statement

(INR m)

Y/E March	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E
Total Income from Operations	16,762	26,999	42,297	43,598	68,022	80,319	85,876	94,058
Change (%)	15.2	61.1	56.7	3.1	56.0	18.1	6.9	9.5
Gross Margin (%)	38.0	39.0	43.9	48.1	39.5	32.5	36.7	36.6
EBITDA	1,963	4,139	10,258	12,470	16,036	12,622	18,438	19,870
Margin (%)	11.7	15.3	24.3	28.6	23.6	15.7	21.5	21.1
Depreciation	526	778	1,397	1,526	1,777	1,675	2,378	2,574
EBIT	1,437	3,361	8,861	10,944	14,259	10,947	16,061	17,296
Int. and Finance Charges	451	832	1,149	742	340	277	293	297
Other Income	123	151	352	215	426	442	515	546
PBT bef. EO Exp.	1,109	2,680	8,064	10,417	14,345	11,112	16,283	17,545
EO Items	0	0	0	0	0	0	0	0
PBT after EO Exp.	1,109	2,680	8,064	10,417	14,345	11,112	16,283	17,545
Total Tax	318	943	1,954	2,659	3,678	2,833	4,098	4,416
Tax Rate (%)	28.7	35.2	24.2	25.5	25.6	25.5	25.2	25.2
Reported PAT	790	1,737	6,110	7,758	10,666	8,278	12,184	13,129
Adjusted PAT	790	1,737	6,110	7,758	10,666	8,278	12,184	13,129
Change (%)	72.4	119.8	251.9	27.0	37.5	-22.4	47.2	7.7
Margin (%)	4.7	6.4	14.4	17.8	15.7	10.3	14.2	14.0

Consolidated - Balance Sheet

(INR m)

Y/E March	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E
Equity Share Capital	273	273	273	273	273	273	273	273
Total Reserves	8,949	10,443	15,446	23,194	33,112	40,148	50,505	61,664
Net Worth	9,221	10,716	15,719	23,467	33,384	40,421	50,778	61,937
Total Loans	9,866	12,286	10,279	5,775	3,007	3,909	1,954	977
Deferred Tax Liabilities	454	775	796	1,078	1,229	1,229	1,229	1,229
Capital Employed	19,541	23,776	26,794	30,320	37,620	45,558	53,961	64,143
Gross Block	6,403	17,749	20,460	22,441	25,263	32,763	40,263	45,263
Less: Accum. Deprn.	528	743	2,140	3,666	5,443	7,118	9,496	12,070
Net Fixed Assets	5,875	17,006	18,320	18,774	19,820	25,645	30,767	33,193
Capital WIP	9,545	339	1,723	2,068	1,037	1,037	1,037	1,037
Total Investments	318	24	24	1,893	4,390	4,390	4,390	4,390
Curr. Assets, Loans, and Adv.	10,167	11,910	12,019	12,868	19,057	23,001	26,383	34,992
Inventory	3,272	4,107	3,945	3,827	5,846	7,612	7,583	8,342
Account Receivables	4,118	5,750	6,127	7,563	11,291	13,332	14,254	15,612
Cash and Bank Balance	482	258	314	334	418	282	2,649	8,960
Cash	94	30	21	89	229	92	2,459	8,770
Bank Balance	388	228	293	245	189	189	189	189
Loans and Advances	2,296	1,795	1,633	1,144	1,503	1,775	1,897	2,078
Curr. Liability and Prov.	6,364	5,502	5,292	5,283	6,684	8,514	8,617	9,470
Account Payables	5,953	4,724	3,643	4,367	5,117	6,664	6,638	7,303
Other Current Liabilities	280	587	1,385	640	1,272	1,501	1,605	1,758
Provisions	132	191	264	276	296	349	373	409
Net Current Assets	3,803	6,408	6,727	7,585	12,373	14,487	17,766	25,522
Appl. of Funds	19,541	23,776	26,794	30,320	37,620	45,558	53,961	64,143

Financials and valuations

Ratios

Y/E March	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E
Basic (INR)								
EPS	5.8	12.7	44.8	56.9	78.2	60.7	89.3	96.3
EPS Growth (%)	72%	120%	252%	27%	37%	-22%	47%	8%
Cash EPS	9.6	18.4	55.0	68.1	91.2	73.0	106.8	115.1
BV/Share	67.6	78.6	115.2	172.0	244.8	296.3	372.3	454.1
DPS	1.3	6.5	4.5	5.5	7.0	9.1	13.4	14.4
Payout (%)	27.0	61.6	12.1	9.7	9.0	15.0	15.0	15.0
Valuation (x)								
P/E	311.6	141.8	40.3	31.7	23.1	29.7	20.2	18.8
Cash P/E	187.1	97.9	32.8	26.5	19.8	24.7	16.9	15.7
P/BV	26.7	23.0	15.7	10.5	7.4	6.1	4.8	4.0
EV/Sales	15.2	9.6	6.1	5.8	3.7	3.1	2.9	2.5
EV/EBITDA	130.2	62.4	25.0	20.2	15.5	19.8	13.3	12.0
Dividend Yield (%)	0.1	0.4	0.2	0.3	0.4	0.5	0.7	0.8
FCF per share	-32.1	-13.3	25.6	57.8	46.8	3.5	47.2	70.0
Return Ratios (%)								
RoE	9.7	17.4	46.2	39.6	37.5	22.4	26.7	23.3
RoCE	6.5	10.5	27.6	29.1	32.1	20.4	24.9	22.6
RoIC	10.7	13.5	28.0	32.1	36.7	22.8	28.0	27.1
Working Capital Ratios								
Fixed Asset Turnover (x)	2.9	2.4	2.4	2.4	3.5	3.5	3.0	2.9
Asset Turnover (x)	0.9	1.1	1.6	1.4	1.8	1.8	1.6	1.5
Inventory (Days)	71	56	34	32	31	35	32	32
Debtor (Days)	90	78	53	63	61	61	61	61
Creditor (Days)	130	64	31	37	27	30	28	28
Leverage Ratio (x)								
Current Ratio	1.6	2.2	2.3	2.4	2.9	2.7	3.1	3.7
Interest Coverage Ratio	3.2	4.0	7.7	14.7	41.9	39.6	54.8	58.3
Net Debt/Equity ratio	1.0	1.1	0.6	0.2	0.1	0.1	0.0	-0.1

Consolidated - Cash Flow Statement

Y/E March	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E
(INR m)								
OP/(Loss) before Tax	1,109	2,680	8,064	10,417	14,345	11,112	16,283	17,545
Depreciation	528	778	1,397	1,526	1,777	1,675	2,378	2,574
Others	481	829	1,262	852	295	277	293	297
Direct Taxes Paid	-279	-561	-1,985	-2,365	-3,535	-2,833	-4,098	-4,416
(Inc.)/Dec. in WC	-9	-3,123	-1,092	-412	-4,643	-2,250	-913	-1,445
CF from Operations	1,830	603	7,647	10,019	8,239	7,980	13,942	14,554
(Inc.)/Dec. in FA	-6,206	-2,410	-4,160	-2,140	-1,862	-7,500	-7,500	-5,000
Free Cash Flow	-4,376	-1,808	3,487	7,879	6,377	480	6,442	9,554
Change in Investments	906	299	3	-1,854	-2,401	0	0	0
Others	53	486	-122	33	22	0	0	0
CF from Investments	-5,247	-1,626	-4,279	-3,961	-4,241	-7,500	-7,500	-5,000
Issue of Shares	1,463	0	0	0	0	0	0	0
Inc./(Dec.) in Debt	2,626	2,033	-1,088	-5,246	-2,812	902	-1,954	-977
Interest Paid	-450	-841	-1,134	-736	-320	-277	-293	-297
Dividend Paid	-188	-213	-1,060	-4	-750	-1,242	-1,828	-1,969
Others	2	-20	-94	-5	24	0	0	0
CF from Fin. Activity	3,453	958	-3,376	-5,990	-3,858	-616	-4,075	-3,243
Inc./Dec. in Cash	36	-64	-8	68	139	-136	2,366	6,311
Opening Balance	58	94	30	22	90	229	93	2,459
Closing Balance	94	30	22	90	229	93	2,459	8,771

NOTES

Explanation of Investment Rating	
Investment Rating	Expected return (over 12-month)
BUY	>=15%
SELL	< - 10%
NEUTRAL	< - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

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