



**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**  
Updated Aug 08, 2023 **25.43**

**Medium Risk**

NEGL	LOW	<b>MED</b>	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

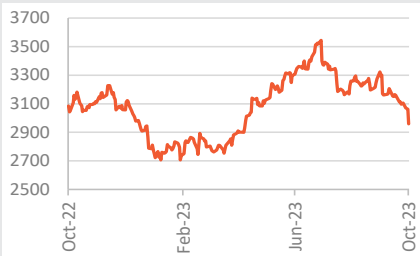
**Company details**

Market cap:	Rs. 2,83,769 cr
52-week high/low:	Rs. 3,567 / 2,686
NSE volume: (No of shares)	8.6 lakh
BSE code:	500820
NSE code:	ASIANPAINT
Free float: (No of shares)	45.4 cr

**Shareholding (%)**

Promoters*	52.6
FII	18.7
DII	10.1
Others	18.6

**Price chart**



**Price performance**

(%)	1m	3m	6m	12m
Absolute	-10.2	-12.7	2.0	-4.1
Relative to Sensex	-5.9	-8.2	-2.1	-10.2

Sharekhan Research, Bloomberg

**Asian Paints Ltd**  
**Muted Q2**

<b>Consumer Goods</b>	<b>Sharekhan code: ASIANPAINT</b>		
<b>Reco/View: Hold</b>	↔	<b>CMP: Rs. 2,958</b>	<b>Price Target: Rs. 3,180</b>
↑ Upgrade	↔ Maintain	↓ Downgrade	

**Summary**

- Asian Paints (APL) registered yet another muted quarter with revenues standing flat at Rs. 8,478 crore while a 573 bps y-o-y expansion in OPM to 20.2% led to 55% y-o-y growth in the PAT to Rs. 1,232.4 crore.
- Decorative paint volume growth slowed to 6% in Q2 due to shift of festive in Q3 and an erratic monsoon that hit consumer sentiments. Q3 would see volume growth improve to double digits on an extended festive season and strong wedding demand.
- OPM came in at 20.2% in Q2FY24 due to change in mix (versus 21.7% in H1FY24). Any significant increase in crude prices would pose a risk to margins. Management maintained its guidance of 18-20% OPM for FY2024.
- Stock trades at 55.1x and 46.6x its FY2024E and FY2025E EPS. Heightened competition in the domestic paint business might keep toll on margins and valuation in the near term. We maintain Hold with a revised PT of Rs. 3,180.

**APL registered muted performance in Q2FY2024 with consolidated revenues remaining flat driven by flat sales in the domestic decorative paints business and lower sales in the home improvement business. Overall consolidated revenues stood at Rs. 8,478.6 crore. Home improvement business (including kitchen and bath) registered a double digit decline while international business registered a mid-single decline. Lower input prices resulted in 764 bps and a 573 bps y-o-y rise in gross margins and OPM, to 43.4% and 20.2%, respectively, in Q2FY24, which was better than our as well as street expectation. This led to a strong PAT growth of 53.3% y-o-y to Rs. 1,232.4 crore. For H1FY2024, the company revenues grew by 3.5% y-o-y to Rs. 17,660.9 crore, EBITDA margins improved by 542 bps y-o-y to 21.7% and the adjusted PAT grew by ~50% y-o-y to Rs. 2782.4 crore.**

**Key positives**

- Industrial business AP-PPG grew 11.4% y-o-y to Rs. 250.6 crore.
- Gross margin/OPM expanded by 764 bps/573 bps y-o-y to 43.4%/20.2%, respectively.

**Key negatives**

- Kitchen and bath businesses' revenue declined by 18% and 20% y-o-y.
- International business saw a 3.9% y-o-y drop to Rs. 775 crore on the back of macro economic and forex challenges in key markets such as South Asia and Egypt.

**Management Commentary**

- Decorative paint volumes grew by 6% compared to 10% in Q1 affected by sporadic monsoon and shift of festive season to Q3. An extended festive season, strong wedding season in Nov-Dec and consistent growth in project and institutional business will help drive double digit volume growth in Q3.
- Industrial paints business is expected to maintain the double-digit growth momentum with Automotive OEM and higher growth in protective segment helping drive good growth.
- H1 was a lull for kitchen and bath businesses due to high base led by price increases. The company expects a gradual recovery in these businesses on an expected recovery in the retail demand.
- Raw material deflation stood at 4% in Q2FY2024. Crude prices have gone-up in the recent past due to global uncertainties and will act as a risk to profitability in the coming quarters. Further change in mix to lower-priced products is affecting the realisation growth. Thus management has maintained its cautious guidance of 18-20% EBITDA margins for FY2024 (stood at 21.7% in H1FY2024).
- Company invested ~Rs. 1,500 crore of the planned capex of Rs. 3,400 for expansion of capacity by more than 30% over the next three years to 22.7 lakh per annum (expansion at Khandala facility completed). Other projects related to backward integration are expected to get complete as scheduled.

**Revision in estimates** – We have reduced our earnings estimates by 3-4% for FY2024E and FY2025E to factor in lower than expected value growth in the domestic decorative paint business, decline in home improvement business and lower international sales.

**Our Call**

**View – Retain Hold with a revised PT of Rs. 3,180:** APL's management is confident of delivering double-digit volume growth in Q3FY2024 driven by factors such as shift of festive season and higher wedding demand. However, whether volume growth sustains amid a subdued demand environment remains to be seen. Further, an expected build-up in competition from newly entered large players would pose a risk to the profitability in the near term. Stock trades at 55.1x and 46.6x its FY2024E and FY2025E earnings. The rising risk of heightened competition pressure will put stress on the valuations in the near term. Hence, we maintain our Hold recommendation on the stock with a revised price target of Rs. 3,180.

**Key Risks**

No impact on sales volumes due to entry of large players in the domestic paints market would act as a key risk to our rating on the stock.

**Valuation (Consolidated)**

Particulars	Rs cr			
	FY22	FY23	FY24E	FY25E
Revenue	29,101	34,489	36,694	41,568
OPM (%)	16.5	18.2	19.9	20.5
Adjusted PAT	3,170	4,231	5,146	6,087
% YoY growth	-1.2	33.5	21.6	18.3
Adjusted EPS (Rs.)	33.1	44.1	53.6	63.5
P/E (x)	89.5	67.1	55.1	46.6
P/B (x)	20.5	17.7	15.5	13.5
EV/EBIDTA (x)	54.5	42.5	36.5	31.3
RoNW (%)	23.8	28.4	30.0	31.0
RoCE (%)	19.5	22.5	24.4	25.6

Source: Company; Sharekhan estimates

## Weak Q2 - Revenue came in lower; margin expansion led to strong PAT growth

APL's revenues stood flat y-o-y at Rs. 8,478.6 crore lower than our expectation of Rs. 8,869 crore and average consensus estimates of Rs. 8,958 crore. Revenue growth during the quarter was impacted by weak performance in international and kitchen Business Domestic decorative paints business registered 6% y-o-y volume growth lower than street expectation of 7-9%. Demand for home décor remained soft during the quarter. Gross margins increased by 764 bps y-o-y to 43.4% due to softening of raw material prices and improvement in profitability of the Industrial businesses. OPM improved by 573 bps y-o-y to 20.2% ahead of our expectation of 19% and in-line with average street expectation of 20%. Operating profit grew by ~40% y-o-y to Rs. 1,716.2 crore. In line with growth in operating profit and higher other income, adjusted PAT before increased by 53.3% y-o-y to Rs. 1,232.4 crore ahead of our and average street expectation of Rs. 1,173 crore. In H1FY2024, revenue grew by 3.5% y-o-y to Rs. 17,660.9 crore, OPM improved by 542 bps y-o-y to 21.7% and adjusted PAT increased by 49.4% y-o-y to Rs. 2,722.6 crore. The board has approved an interim dividend of Rs. 5.15 per share for FY2024.

## Standalone revenue growth stood flat y-o-y; OPM rises 639 bps y-o-y

Revenues stood flat y-o-y at Rs. 7,342 crore as erratic monsoon impacted market sentiment potentially leading to deferment of sales to October given a late Diwali this year. Gross margins expanded by 823 bps y-o-y to 44.1% and OPM came in higher by 639 bps y-o-y to 21.6% aided by moderating raw material prices coupled with operational efficiencies. Operating profit grew by 42.1% y-o-y to Rs. 1,585 crore and adjusted PAT grew by 52% y-o-y to Rs. 1,160 crore.

## Key quarterly highlights

- ◆ **Domestic volumes rose 6% in Q2; recovery likely in H2:** The company witnessed moderation in volume growth to 6% versus a double-digit volume growth for the past few quarters due to weak consumer sentiment. On a 4-year CAGR basis volume growth in Q2FY2024 stood at 14.7% (16% in H1FY2024). Within regions, APL witnessed high single-digit volume growth across urban markets, with rural growth reported a notch lower. However, over 4 years, both rural and urban centers grew equally well with similar double-digit CAGRs. Product mix was led by economy range of products, while luxury range also saw reasonable traction. Management indicated that it saw a reversal of trend in September. APL witnessed strong traction for its Safe Painting Service (SPS) and Trusted Contractor Service (TCS) as proven by exponential growth over last year due to enhanced customer experience. The management is expecting recovery in H2FY2024 aided by multiple factors including extended festive and marriage season, largely normal monsoon, moderating inflation and boost in government spending.
- ◆ **New categories in home décor continued to see growth momentum:** In Home décor business, new categories of fabrics, decorative lighting, UPVC doors and windows maintained growth trajectory in Q2FY2024, while kitchen and bath segments continued to be impacted by weak consumer sentiment. Kitchen business' revenue decreased by 17.9% y-o-y to Rs. 96.8 crore on a high base of Q2FY2023 due to price increases. The business achieved PBDIT break-even with PBDIT of Rs. 0.9 crore in Q2FY2024 as against a loss of Rs. 0.9 crore in Q2FY2023. The company is focusing on building a strong foothold in economy-price point kitchens. Bath fittings business' revenues declined by 20% y-o-y to Rs. 81.4 crore. PBDIT loss stood at Rs. 2.1 crore against a profit of Rs. 1.2 crore in Q2FY2023. The White Teak business reported a revenue growth of 8.5% y-o-y to Rs. 26.1 crore, while the Weatherseal business revenue nearly doubled to Rs. 12.6 crore supported by synergies with the Asian Paints network. In White Teak, the company is focusing on expanding store network and increasing traction across Beautiful Homes, while the Weatherseal business continues to gain from synergies with the projects business.
- ◆ **Global biz sees muted quarter:** Revenue declined by 3.9% y-o-y to Rs. 775 crore on the back of macro-economic and forex challenges in key markets of South Asia and Egypt. In constant currency terms, sales increased by 1.9% y-o-y. All regions in Middle East did well with double-digit growth in this geography, while Sri Lanka business is recovering on improving economic conditions. PBT before exceptional items came in at Rs. 40.4 crore against Rs. 43.5 crore in Q2FY2023.
- ◆ **Good quarter for industrial paints business:** The PPG-AP business grew by 5.6% y-o-y to Rs. 495.3 crore. PBT came in at Rs. 77.2 crore against Rs. 56.8 crore in Q2FY2023. Focused customer mix and moderating raw material prices led to improvement in margins. AP-PPG business grew by 11.4% y-o-y to Rs. 250.6 crore led by strong growth in protective and powder coating segments. PBT came in at Rs. 28.4 crore against Rs. 13.7 crore in Q2FY2023. An enhanced sales mix coupled with moderating raw material prices led to improved margins.

- ◆ **Distribution network continued to expand:** APL continued to expand its distribution footprint by adding 2,500 touchpoints in Q2. The company now caters to over 1.6 lakh retail touchpoints.
- ◆ **Continued focus on innovation:** As indicated by the management, new products contributed to ~11% of overall revenues.

#### Results (Consolidated)

Particulars	Q2FY24	Q2FY23	y-o-y (%)	Q1FY24	q-o-q (%)
<b>Total Revenue</b>	<b>8,478.6</b>	<b>8,457.6</b>	<b>0.2</b>	<b>9,182.3</b>	<b>-7.7</b>
Raw Material Cost	4,801.5	5,435.6	-11.7	5,240.4	-8.4
Employee Cost	596.1	512.6	16.3	545.7	9.2
Other Expenses	1,364.8	1,281.6	6.5	1,275.0	7.0
Total Operating Cost	6,762.3	7,229.9	-6.5	7,061.0	-4.2
<b>Operating Profit</b>	<b>1,716.2</b>	<b>1,227.7</b>	<b>39.8</b>	<b>2,121.3</b>	<b>-19.1</b>
Other Income	165.2	95.5	73.0	163.1	1.3
Interest & Other Financial Cost	50.9	35.4	43.8	45.8	11.3
Depreciation	208.7	215.7	-3.2	198.3	5.2
<b>Profit Before Tax</b>	<b>1,621.8</b>	<b>1,072.1</b>	<b>51.3</b>	<b>2,040.3</b>	<b>-20.5</b>
Tax Expense	418.6	290.3	44.2	521.0	-19.7
<b>Adjusted PAT</b>	<b>1,203.3</b>	<b>781.7</b>	<b>53.9</b>	<b>1,519.4</b>	<b>-20.8</b>
Share of profit from associates	29.1	22.1	31.9	30.7	-5.0
<b>Adjusted PAT after MI</b>	<b>1,232.4</b>	<b>803.8</b>	<b>53.3</b>	<b>1,550.0</b>	<b>-20.5</b>
Exceptional Items	0.0	0.0	-	-24.8	-
Reported PAT	1232.4	803.8	53.3	1574.8	-21.7
Adj. EPS (Rs. )	12.8	8.4	53.3	16.2	-20.5
			<b>bps</b>		<b>bps</b>
GPM (%)	43.4	35.7	764	42.9	44
OPM (%)	20.2	14.5	573	23.1	-286
NPM (%)	14.5	9.5	503	17.2	-262
Tax rate (%)	25.8	27.1	-127	25.5	27

Source: Company; Sharekhan Research

#### Business-wise performance

Particulars	Q2FY24	Q2FY23	y-o-y (%)	Q1FY24	q-o-q (%)
Standalone decorative paints	7,125.3	7,093.3	0.5	7,897.2	-9.8
Kitchen business	96.8	118.0	-18.0	96.0	0.8
Bath business	81.4	102.0	-20.2	85.0	-4.2
White Teak	26.1	24.0	8.8	26.0	0.4
Weatherseal	12.6	7.0	80.0	9.8	28.6
<b>Domestic standalone business</b>	<b>7,342.2</b>	<b>7,344.3</b>	<b>0.0</b>	<b>8,114.0</b>	<b>-9.5</b>
Africa	182.0	175.0	4.0	159.0	14.5
Middle East	246.0	221.0	11.3	249.0	-1.2
Asia	318.0	380.0	-16.3	275.0	15.6
South Pacific	44.0	40.0	10.0	34.0	29.4
<b>International business</b>	<b>790.0</b>	<b>816.0</b>	<b>-3.2</b>	<b>717.0</b>	<b>10.2</b>
PPG-AP	495.3	469.0	5.6	472.0	4.9
AP-PPG	250.6	225.0	11.4	294.0	-14.8
<b>Consolidated sales</b>	<b>8,478.6</b>	<b>8,457.6</b>	<b>0.2</b>	<b>9,182.3</b>	<b>-7.7</b>

Source: Company; Sharekhan Research

## Outlook and Valuation

### ■ Sector Outlook – Structural growth of the paint industry is intact

In Q1FY2024, paints companies reported strong volume-led revenue growth with recovery in domestic paints aided by distribution expansion and largely normal climate conditions. The decorative paints industry is expected to clock a 12% CAGR over FY2023-FY2027 to Rs. 1,00,000 crore, led by a reduction in the repainting cycle to 4-5 years (from 8-10 years earlier), increase construction activities of new real estate projects acceptance of better paint products in smaller towns, and upgradation of premium brands in cities and large towns. A better product mix and efficiencies would help paint companies post higher margins in the long run.

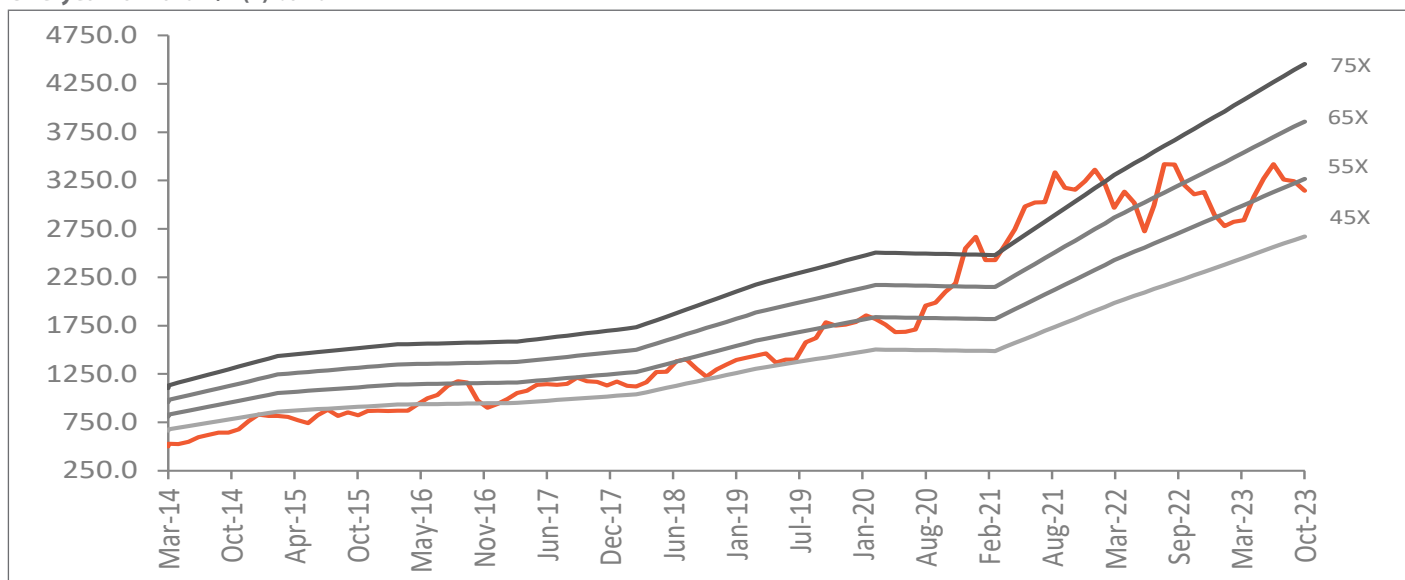
### ■ Company Outlook – Margin expansion to sustain in quarters ahead; sales volume to improve

APL's revenues grew by 3.5% y-o-y to Rs. 17,660.9 crore in H1FY2024, OPM improved by 542 bps y-o-y to 21.7% and adjusted PAT increased by 49.4% y-o-y to Rs. 2,722.6 crore. In the medium term, waterproofing products, construction chemicals and the projects business will continue to see strong traction from the real estate sector, government projects and housing society projects. With an expect recovery in rural demand and extended festive and wedding season, the management is confident of higher growth in H2FY2024. Raw material correction will help margins stay high in FY2024, with gross margins is expected to be at 38-40%. The company is banking on planned initiatives (of differentiated formulations and cost efficiencies) along with a better mix to achieve margins of 18-20% in the medium term.

### ■ Valuation – Retain Hold with a revised PT of Rs. 3,180

APL's management is confident of delivering double-digit volume growth in Q3FY2024 driven by factors such as shift of festive season and higher wedding demand. However, whether volume growth sustains amid a subdued demand environment remains to be seen. Further, an expected build-up in competition from newly entered large players would pose a risk to the profitability in the near term. Stock trades at 55.1x and 46.6x its FY2024E and FY2025E earnings. The rising risk of heightened competition pressure will put stress on the valuations in the near term. Hence, we maintain our Hold recommendation on the stock with a revised price target of Rs. 3,180.

#### One-year forward P/E (x) band



Source: Sharekhan Research

#### Peer Comparison

Particulars	P/E (x)			EV/EBITDA (x)			RoCE (%)		
	FY23	FY24E	FY25E	FY23	FY24E	FY25E	FY23	FY24E	FY25E
Indigo Paints	50.2	39.2	33.1	35.6	25.0	20.1	21.1	27.6	30.3
Asian Paints	67.1	55.1	46.6	42.5	36.5	31.3	22.5	24.4	25.6

Source: Company, Sharekhan estimates

## About the company

APL is the largest paint company in India with market leadership of over 50 years and stands among the top 10 paint companies in the world. The company has 27 paint manufacturing plants and operates in 15 countries, serving customers in over 60 countries globally. Deco India, including decorative paints, waterproofing, wall coverings, and adhesives, constitutes almost 84% of the company's total revenue, whereas the industrial coatings space, including automotive and non-automotive, constitutes only 2%, through two 50:50 JVs with PPG Industries Inc., USA (AP-PPG). The international business contributes ~12% to the total revenue mainly dominated by Nepal, Sri Lanka, and Bahrain. A small portion is contributed by kitchen and bath fittings through its subsidiary, Sleek International Pvt. Ltd. (Sleek Kitchens) and Ess Ess Bath Fittings. The company has forayed into the home décor space as it transitions its outlook from 'share of surface' to 'share of space'.

## Investment theme

The rising middle-income group, fast urbanisation, shift from the unorganised to organised space, and improving penetration in rural markets are some of the key revenue drivers for paint companies in the near to medium term. APL, with a leadership position in the decorative paint business and strong brand portfolio, will continue to deliver good earnings growth in the near term. APL is expected to benefit from its recent capacity expansion, vast distribution network, product innovation, and growth in its premium products. However expected built in competition from new large players in the domestic paint industry would act as risk to profitability in the near term.

## Key Risks

- ♦ **Increased raw-material prices:** Any significant increase in crude prices and other input costs will affect the company's profitability.
- ♦ **Slowdown in economic growth:** Any slowdown in economic growth will affect repainting demand, which constitutes almost 70% of the total paint demand.
- ♦ **Increase in competition from new players:** Any significant competition from the large players entering the market would act as key risk to the pricing power and profitability of the company.

## Additional Data

### Key management personnel

Deepak M Satwalekar	Chairman
Amit Syngle	Chief Executive Officer & Managing Director
R J Jeyamurugan	Chief Financial Officer, Company Secretary & Compliance Officer

Source: BSE; Company

### Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Siddhant Commercials Pvt Ltd	4.9
2	Life Insurance Corp of India	4.5
3	Vanguard Group Inc	1.9
4	Blackrock Inc	1.8
5	SBI Funds Management	1.6
6	Capital Group Companies	0.8
7	UTI Asset Management Co Ltd	0.8
8	JP Morgan and Chase	0.4
9	Norges Bank	0.4
10	FMR LLC	0.4

Source: Bloomberg

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## 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 deteriorating 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

# Sharekhan

by BNP PARIBAS

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