



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

30.77

High Risk

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

Source: Morningstar

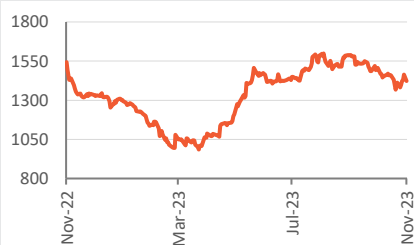
Company details

Market cap:	Rs. 6,769 cr
52-week high/low:	Rs. 1,700 / 981
NSE volume: (No of shares)	0.9 lakh
BSE code:	543258
NSE code:	INDIGOPNTS
Free float: (No of shares)	2.2 cr

Shareholding (%)

Promoters	54.0
FII	34.4
DII	3.0
Others	8.67

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-5.6	-10.2	11.5	-7.8
Relative to Sensex	-4.0	-8.8	6.3	-14.4

Sharekhan Research, Bloomberg

Indigo Paints Ltd

Decent Q2; eyeing recovery in H2

Consumer Goods

Sharekhan code: INDIGOPNTS

Reco/View: Buy



Upgrade



Maintain



Downgrade

CMP: Rs. 1,422

Price Target: Rs. 1,850

Summary

- Indigo paints Limited's (IPL's) revenue and PAT grew by 11.5% and 25.9% y-o-y in Q2FY2024 to Rs. 271 crore and Rs. 26.1 crore, respectively; OPM rose 153 bps y-o-y to 15.4%.
- Revenue growth stood ahead of industry growth. Management expects the gap to widen in H2 led by strategic initiatives and festive demand.
- We expect revenue and PAT to clock a 19% CAGR each over FY2023-26E, led by double-digit volume growth, driven by distribution expansion, focus on brand building, capacity addition, foray into project business and scale-up in the B2B business.
- The stock trades at 44x/36x/30x its FY2024E/25E/26E earnings. We maintain our Buy rating with an unchanged PT of Rs. 1,850.

IPL's Q2FY2024 was decent, with revenues growing 11.5% y-o-y to Rs. 270.5 crore and OPM higher by 153 bps y-o-y to 15.4%. However, performance missed our as well as consensus estimates on all fronts. Sales grew at more than 3x-4x the industry growth rate for two consecutive quarters, largely aided by outperformance in tier-1/2 markets. In line with operating profit growth of 23.7% y-o-y to Rs. 41.8 crore, adjusted PAT grew by 25.9% y-o-y to Rs. 26.1 crore. In Q2FY2024, IPL added two depots (one each in West India & East India) and 457 tinting machines. In H1FY2024, revenues grew by 17.3% y-o-y to Rs. 547.5 crore, OPM improved by 155 bps y-o-y to 16.4% and adjusted PAT grew by 41.2% y-o-y to Rs. 57.4 crore. Commercial production of water-based paint products commenced in Q2, while work has started on new plant at Jodhpur.

Key positives

- Sales grew at more than 3x-4x the industry growth rate for two consecutive quarters.
- Cement and putty volumes grew strongly by 50.6%.
- Gross margins rose by 400 bps y-o-y to 45.7%; OPM increased by 153 bps y-o-y to 15.4%.
- Tinting machine count increased by 457 to 9,114 from 8,657 at Q1FY2024-end; added two more depots (one each in West and East India).

Key negatives

- Enamels delivered a soft quarter with y-o-y volume growth at 5.4%.

Management Commentary

- IPL witnessed exceptionally good sales in October 2023. Thus, the management expects Q3 to be better than Q2 and Q4 is expected to be the best quarter. Further, in the long term, IPL aims to increase the gap between the company's and industry's growth rate led by initiatives taken in FY23.
- Share of premium products rises in Q3 and Q4. Thus, management expects gross margin and OPM to be higher in the coming quarters.
- Company added two more depots, one each in West India & East India during Q2FY2024 to improve its distribution efficiency and is planning to add a few more depots in the coming months. IPL's focus would be on improving throughput per dealer than focusing on adding dealers, so higher tinting machines per dealer would be targeted.
- Management expects Apple Chemie to deliver 45-50% revenue growth in FY24 (Rs. 55-60 crore revenue) and further strengthen sales force and expand to a few other states in FY25.
- IPL is building a team for entering project sales in several states, with focus on eight states initially where the company's retail presence is strong. The company plans to gradually scale up across India depending on the response.
- The management plans to leverage Apple Chemie's strong knowledge in construction chemicals. The company is setting up a separate team for construction chemicals & water proofing in all depots.

Revision in estimates – We reduce our estimates for FY2024 and FY2025 to factor in lower-than-expected performance in Q2FY2024. However, the management is confident of good performance in H2. We have introduced FY2026 estimates through this note.

Our Call

View – Maintain Buy with an unchanged PT of Rs. 1,850: IPL posted decent performance in Q2FY2024, with double-digit revenue growth and y-o-y expansion in OPM. The company's revamped strategy is showing good results and will help the company to achieve growth ahead of the industry over the next 2-3 years. Further, entry into project sales and construction chemicals & waterproofing segments (both B2 and retail) and capacity addition in water-based paints will act as additional drivers. Focused strategies will help IPL to achieve consistent revenue and PAT growth of 19%, each, over FY2023-FY2026E. The stock trades at 44x/36x/30x its FY2024E/25E/26E EPS. We maintain our Buy rating on the stock with an unchanged price target (PT) of Rs. 1,850.

Key Risks

Increased competitive pressures from large players or a rise in key input prices would act as a risk to our earnings estimates.

Valuation (Consolidated)

Rs cr

Particulars	FY23	FY24E	FY25E	FY26E
Revenue	1,073	1,292	1,535	1,796
OPM (%)	16.9	18.8	20.2	20.7
Adjusted PAT	132	153	188	223
% Y-o-Y growth	57.0	15.6	23.2	18.7
Adjusted EPS (Rs.)	27.7	32.1	39.5	46.9
P/E (x)	51.3	44.3	36.0	30.3
P/B (x)	8.7	8.4	7.7	6.9
EV/EBIDTA (x)	36.4	27.5	21.6	18.0
RoNW (%)	18.5	19.2	22.3	24.0
RoCE (%)	21.1	25.2	29.2	31.5

Source: Company; Sharekhan estimates

Decent Q2 – Revenue grew by 12% y-o-y; OPM up by 153 bps y-o-y

IPL's revenues grew by 11.5% y-o-y to Rs. 270.5 crore, below our and average street expectation of Rs. 287-289 crore, aided by double-digit volume growth in most categories. Tier 1/2 cities continued to outperform Tier 3/4 cities and rural areas. Sales grew at more than 3x-4x the industry rate for two consecutive quarters indicating significant market share gains. Softening of input cost inflation drove up gross margin by 400 bps y-o-y to 45.7%, while higher employee and other expenses limited the rise in OPM to 153 bps y-o-y to 15.4%, much lower than our and average street expectation of 17.7%. Operating profit grew by 23.7% y-o-y to Rs. 41.8 crore and adjusted PAT grew by 25.9% y-o-y to Rs. 26.1 crore (missing ours and the average street's expectation of Rs. 33 crore). The company continued to improve its distribution efficiency with the addition of two more depots (one each in West India & East India) and addition of 457 tinting machines. In H1FY2024, revenue grew by 17.3% y-o-y to Rs. 547.5 crore and OPM improved by 155 bps y-o-y to 16.4%. This coupled with higher other income led to 41.2% y-o-y growth in the adjusted PAT to Rs. 57.4 crore in H1FY2024.

Key conference call highlights

- ♦ **Tier-1/2 towns outperformed in Q2; demand outlook for H2 strong:** In Q2FY2024, IPL's revenue growth was largely driven by the company's special focus on Tier-1/2 cities led by various initiatives. Growth in Tier-1/2 cities is ahead of Tier-3/4 and rural areas and management expects the trend to continue. Kerala reported muted growth in the past few quarters, however, other states have made up for weak performance by Kerala. The management has indicated that the company witnessed exceptionally good sales in October 2023, with timely monsoon withdrawal and a long festive season. Thus, Q3 is expected to be better than Q2 and Q4 is expected to be the best quarter. Further, in the long term, IPL aims to increase the gap between the company's and industry's growth rate led by initiatives taken in FY23 including shift of focus on larger cities, increasing tinting machine count, focus on influencer community and ramp up of sales force.
- ♦ **Soft Q2 for enamels & wood coatings; other categories post double-digit volume growth:** The strongest growth was reported in the cement and putty category, with value/volume growth coming in at 47.9%/50.6% y-o-y, followed by primers and distempers category, with registered y-o-y value/volume growth of 26.6%/28.8%. The emulsions category posted y-o-y value growth of 15.4% and volume growth of 20%. Enamels delivered a soft quarter with category's y-o-y value growth reported at 3% and volume growth at 5.4%. As volume growth gains momentum, volume growth and value growth for most categories is now at par against the earlier trend of high value-led growth due to price increases.
- ♦ **Continued focus on A&P spends for brand building:** IPL will continue to focus on brand building through investments in advertisement and promotions (A&P). Management has guided that absolute A&P spends would marginally rise, while spends as a percentage of sales are expected to decline in the coming years. IPL has recently launched a campaign using MS Dhoni & Mohan Lal together (in Kerala) to promote its most premium emulsion: Dirt & Waterproof Exterior Paint.
- ♦ **Margins to improve in H2:** Management indicated that volume growth was higher than value growth across categories in Q2 as economy range growth was higher than premium range growth in Q2. However, the share of premium products rises in Q3 and Q4. Thus, management expects gross margin and OPM to be higher in the coming quarters.
- ♦ **Widening distribution:** The company added two more depots, one each in West India & East India during Q2FY2024 to improve its distribution efficiency and is planning to add a few more depots in the coming months. IPL increased its tinting machine to 9,114 from 8,657 at Q1FY202-end, while the number of active dealers rose to 17,148 from 16,693 at Q1FY2024-end. As per management, IPL's focus would be on improving throughput per dealer than focusing on adding dealers, so higher tinting machines per dealer would be eyed. Management

highlighted that IPL's tinting machines are unique compared to competitors as these tinting machines have inbuilt computer and are compact, which acts as an added advantage.

- ♦ **B2B segment likely to pick up momentum:** Apple Chemie (B2B business) is expected to pick up in the coming quarters as the company has sharply increased its salesforce in various parts of India. Apple Chemie has strong B2B relationships with customers like L&T, Shapoorji Pallonji and is a strong player in Maharashtra. IPL plans to leverage these factors and now plans to expand B2B business in 7-8 other states. Management expects Apple Chemie to deliver 45-50% revenue growth in FY24 (Rs. 55-60 crore revenue) and further strengthen sales force and expand to few other states in FY25. Apple Chemie has differentiated products which are sold at competitive prices due to the company's advanced technology.
- ♦ **Foray into project sales:** IPL is building a team for entering project sales in several states, with focus on eight states initially where the company's retail presence is strong. The company plans to gradually scale up pan-India depending on the response.
- ♦ **Construction chemicals – building another growth driver:** Management plans to leverage Apple Chemie's strong knowledge in construction chemicals. Growth in construction chemicals is expected to be driven by superior products, advertisement (new advertisement likely to be on air in January, and by building a network outside paint dealers (building parallel team). The company is also setting up a separate team for construction chemicals & water proofing in all depots.
- ♦ **Project sales and B2B business likely to pick up in the coming quarters:** IPL is building a team for entering project sales in several states and a separate team for construction chemicals & water proofing also being setup in all depots. On B2B front, Apple Chemie has sharply increased its sales manpower in various parts of India, which is expected to yield significant growth in sales in the upcoming quarters.
- ♦ **Capacity expansion on track:** Commercial production of water-based paints began at the new plant in Tamil Nadu in September 2023, while work has started on new water-based plant (90,000 KLPA) and a solvent based plant (12,000 KLPA) at Jodhpur (expected to be operational by FY2025-end).

Results (Standalone)

					Rs cr
Particulars	Q2FY24	Q2FY23	Y-o-Y %	Q1FY24	Q-o-Q %
Net revenue	270.5	242.6	11.5	277.0	-2.4
Material cost	146.8	141.4	3.8	145.2	1.1
Employee cost	23.5	17.5	33.9	22.6	3.8
Other expenses	58.4	49.9	17.0	61.5	-5.0
Total expenditure	228.7	208.8	9.5	229.3	-0.3
Operating profit	41.8	33.8	23.7	47.7	-12.5
Other income	3.0	3.2	-6.8	3.5	-15.6
Interest expenses	0.5	0.3	76.7	0.4	11.2
Depreciation	10.0	8.5	17.7	8.8	13.5
Profit Before Tax	34.3	28.2	21.6	42.0	-18.4
Tax	8.2	7.4	9.5	10.7	-24.0
Adjusted PAT	26.1	20.8	25.9	31.3	-16.5
Extra-ordinary gain / loss	0.0	16.3	-	0.0	-
Reported PAT	26.1	37.1	-29.5	31.3	-16.5
EPS (Rs.)	5.5	4.4	25.9	6.6	-16.5
			bps		bps
GPM (%)	45.7	41.7	400	47.6	-186
OPM (%)	15.4	13.9	153	17.2	-178
NPM (%)	9.7	8.6	111	11.3	-163
Tax rate (%)	23.8	26.4	-262	25.6	-176

Source: Company; Sharekhan Research

Results (Consolidated)

					Rs cr
Particulars	Q2FY24	Q2FY23	Y-o-Y %	Q1FY24	Q-o-Q %
Net revenue	279.0	242.6	15.0	288.4	-3.3
Operating profit	42.1	33.8	24.7	49.1	-14.2
Adjusted PAT	25.3	20.8	21.9	31.5	-19.7
EPS (Rs.)	5.3	4.4	21.9	6.6	-19.7
			bps		bps
GPM (%)	45.6	41.7	384	47.3	-176
OPM (%)	15.1	13.9	117	17.0	-193
NPM (%)	9.1	8.6	52	10.9	-186
Tax rate (%)	24.3	26.4	-208	25.6	-124

Source: Company; Sharekhan Research

Category-wise volume/value growth

Product Category	Value growth (%)	Volume growth (%)
Cement paints + Putty	47.9	50.6
Emulsions	15.4	20.0
Enamels + Wood Coatings	3.0	5.4
Primers + Distempers + Others	26.6	28.8

Source: Company; Sharekhan Research

Outlook and Valuation

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

In H1FY2024, paint companies reported 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 report 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), increased 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 – Growth momentum to sustain

In H1FY2024, revenue by 17.3% y-o-y to Rs. 547.5 crore and OPM improved by 155 bps y-o-y to 16.4%, leading to 41.2% y-o-y growth in the adjusted PAT to Rs. 57.4 crore. Growth was supported by double-digit volume growth across most categories and by correction in key raw-material prices. The company expects strong sales volume growth (2x that of the industry) in the coming quarters because of its renewed focus on increasing output per dealer in Tier-1 and Tier-2 cities. Rising urbanisation, willingness to spend on home improvement, strong traction to differentiate products, distribution expansion, and market share gains would help IPL to grow faster than the industry in the coming years. Scale-up in the business will help OPM to improve further and reach 21% in FY2026.

■ Valuation – Maintain Buy with an unchanged PT of Rs. 1,850

Q2 was decent, with double-digit revenue growth and y-o-y expansion in OPM. The company's revamped strategy is showing good results and will help the company to achieve growth ahead of the industry over the next 2-3 years. Further, entry into project sales and construction chemicals & waterproofing segments (both B2 and retail) and capacity addition in water-based paints will act as additional drivers. Focused strategies will help IPL to achieve consistent revenue and PAT growth of 19%, each, over FY2023-FY2026E. The stock trades at 44x/36x/30x its FY2024E/25E/26E EPS. We maintain our Buy rating on the stock with an unchanged price target (PT) of Rs. 1,850.

Peer Comparison

Particulars	P/E (x)			EV/EBITDA (x)			RoCE (%)		
	FY23	FY24E	FY25E	FY23	FY24E	FY25E	FY23	FY24E	FY25E
Asian Paints	68.6	56.4	47.7	43.5	37.3	32.0	22.5	24.4	25.6
Indigo paints	51.3	44.3	36.0	36.4	27.5	21.6	21.1	25.2	29.2

Source: Company, Sharekhan estimates

About company

Incorporated in 2000, IPL is the fifth-largest paint company in India. The company started its operations by manufacturing lower-end cement products and gradually expanded its range to cover most segments of water-based paints such as exterior emulsions, interior emulsions, distempers, and primers. The company kept churning out bright new ideas for painting solutions, with alarming regularity. IPL introduced India's first metallic paint, first-floor coat paint, unique ceiling coat paint, and first-of-its-kind paint for roofs. Differentiated products contribute ~30% to the company's revenue. The company has a growing dealership base of ~17,100 dealers covering 27 states.

Investment theme

IPL is the fastest-growing paints company in India, which has carved a niche for itself by developing and marketing differentiated products to establish its position in the high entry-barrier paint industry. The company has the highest gross margin of ~45% among paint companies. The differentiated business model aided the company to achieve strong topline and earnings growth of 15% and 37%, respectively, over FY2019-FY2023, with the highest gross margin of ~45% among peers. Rising urbanisation, willingness to spend on home improvement, strong traction to differentiate products, and market share gains would help IPL to achieve strong growth in the coming years.

Key Risks

- ♦ **Increased raw-material prices:** Any significant increase in crude prices and other input costs will affect the company's profitability.
- ♦ **Delay in capacity expansion:** Delay in capacity expansion plans due to any regulatory hurdle or any other reason would affect the company's future growth prospects.
- ♦ **The company does not enter into long-term arrangements with dealers:** IPL presently does not have any long-term or exclusive arrangements with any of the dealers and cannot assure that it will be able to sell the same quantities as it supplied historically to such dealers.

Additional Data

Key management personnel

Hemant Kamala Jalan	Chairman-Managing Director
Chetan Bhalchandra Humane	Chief Financial Officer
Dayeeta Gokhale	Company Secretary and Compliance Officer

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Sequoia Cap India Inv Hldg	12.14
2	Capital Group Cos Inc.	2.55
3	Small Cap World Fund Inc.	2.32
4	Carne Global Fund Managers	1.46
5	ICICI Prudential Life Insurance Co.	1.42
6	Emirate of Abu Dhabi United Arab Emirates	1.35
7	Pictet Funds SA	0.78
8	Nomura Holdings Inc.	0.45
9	Caisse de Depot et Placement du Quebec	0.37
10	SBI Funds Management Ltd.	0.19

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

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Registration and Contact Details: Name of Research Analyst - Sharekhan Limited, Research Analyst Regn No.: INH000006183. CIN): - U99999MH1995PLC087498. Registered Office: The Ruby, 18th Floor, 29 Senapati Bapat Marg, Dadar (West), Mumbai – 400 028, Maharashtra, INDIA. Tel: 022-6115000.

Correspondence/Administrative Office: Gigaplex IT Park, Unit No 1001, 10th Floor, Building No.9, TTC Industrial Area, Digha, Airoli-West, Navi Mumbai – 400 708. Tel: 022 61169000 / 61150000, Fax No. 61169699.

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Compliance Officer: Ms. Binkle Oza; Tel: 022-62263303; email id: complianceofficer@sharekhan.com

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