PL Capital
PRABHUDAS LILLADHER

Deepak Nitrite (DN IN)

Rating: REDUCE | CMP: Rs3,000 | TP: Rs2,582

October 17, 2024

Company Update

☑ Change in Estimates | ☑ Target | ■ Reco

Change in Estimates

	Current		Previous	
	FY26E	FY27E	FY26E	FY27E
Rating	**REDUCE**		**REDUCE**	
Target Price	**2,582**		**2,564**	
Sales (Rs. m)	89,057	97,753	89,057	97,753
% Chng.	-	-		
EBITDA (Rs. m)	14,005	15,860	14,005	15,860
% Chng.	-	-		
EPS (Rs.)	64.4	71.7	64.0	70.9
% Chng.	0.6	1.1		

Key Financials - Consolidated

Y/e Mar	FY24	FY25E	FY26E	FY27E
Sales (Rs. m)	76,818	85,925	89,057	97,753
EBITDA (Rs. m)	11,233	13,227	14,005	15,860
Margin (%)	*14.6*	*15.4*	*15.7*	*16.2*
PAT (Rs. m)	8,109	8,606	8,790	9,781
EPS (Rs.)	59.4	63.1	64.4	71.7
Gr. (%)	*(4.8)*	*6.1*	*2.1*	*11.3*
DPS (Rs.)	7.5	8.0	8.1	9.0
Yield (%)	*0.3*	*0.3*	*0.3*	*0.3*
RoE (%)	*18.2*	*16.6*	*14.8*	*14.5*
RoCE (%)	*20.9*	*20.1*	*17.6*	*17.0*
EV/Sales (x)	5.3	4.8	4.7	4.3
EV/EBITDA (x)	36.2	31.1	29.6	26.6
PE (x)	50.5	47.5	46.5	41.8
P/BV (x)	8.5	7.4	6.5	5.7

Key Data

Key Data	DPNT.BO | DN IN
52-W High / Low	Rs.3,169 / Rs.1,922
Sensex / Nifty	81,501 / 24,971
Market Cap	Rs.409bn/ $ 4,871m
Shares Outstanding	136m
3M Avg. Daily Value	Rs.1150.66m

Shareholding Pattern (%)

Promoter's	49.24
Foreign	6.86
Domestic Institution	21.21
Public & Others	22.69
Promoter Pledge (Rs bn)	-

Stock Performance (%)

	1M	6M	12M
Absolute	2.6	29.2	42.1
Relative	4.5	15.6	15.3

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Large capacity additions in China worrisome

Quick Pointers:

- China adding phenol capacity equivalent to ~20% of current global demand by 2027
- Polycarbonate resin project margin dilutive, as per our calculation

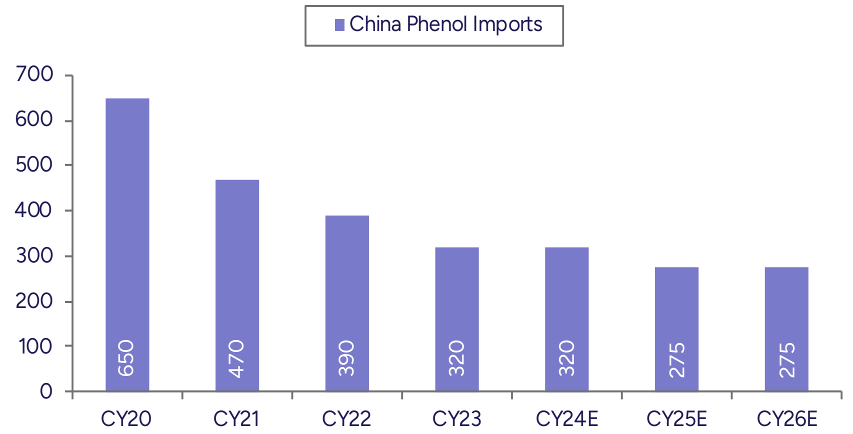
Deepak Nitrite Ltd (DN) is working towards doubling its phenol capacity over the next 4-5 years through multiple forward integration projects. However, margins are likely to come under pressure due to the ongoing capacity additions in China, which may soon outpace demand. Deepak Phenolics' EBIT/kg has dropped from Rs23/kg in FY22 to Rs17/kg; we expect it to remain in the Rs16-17/kg range until FY27. Like DN, expansions in China are also in integrated fashion, thereby impacting margins across the value chain. While DN's entry into polycarbonates and methyl methacrylate (MMA) targets import substitution to cater to the rising domestic demand, the influx of cheaper imports from China will pose a significant threat, potentially impacting margins. We anticipate ~8.7% EPS CAGR over FY24-27E. Considering largely commodity nature of the business, we value the stock at 36x FY27 EPS and retain 'Reduce' rating with TP of Rs2,582. Key risks to our recommendation would be imposing of anti-dumping duty, and diversification into value-added specialty chemicals.

- **DN on path to expand phenol capacity up to 700tmtpa in next 4-5 years:** DN has lined up ~Rs140bn investments over the next 4-5 years, mainly focused on phenol, polycarbonate, MMA and poly methyl methacrylate (PMMA) resins/compounds, primarily for import substitution. Polycarbonates find usage in a wide range of applications, including electrical and electronic components, high-end telecommunications devices, automotive, etc., while MMA and PMMA are used in construction lighting, and TV and smartphone displays.

- **China's phenol imports on a decline, marching towards self-sufficiency:** China has been actively expanding its phenol production capacity to reduce its import dependency. As a result, its total phenol imports have dropped by ~51%, from 650tmtpa in CY20 to 320tmtpa in CY23. We expect China to add phenol-acetone capacity of ~4mmtpa from CY24 to CY27. While peak global phenol utilization rate stood at 88% in CY19, the capacity additions are likely to reduce global utilization rate from ~75% in CY23 to ~68% by CY26, leading to suppressed phenol-acetone spreads.

- **Growing competition from China in integrated phenolic value chain:** By CY26, we anticipate that ~60% of China's 7.9mmtpa phenol capacity will be integrated into Bisphenol A (BPA), with 50% of the BPA further integrated into polycarbonates and epoxy resins. Wanhua Chemical alone is expanding its polycarbonate capacity by 20%, from 480tmtpa to 600tmtpa. As these capacities come online, we expect China's polycarbonate exports to rise, posing significant competition to DN.

Exhibit 1: China's phenol imports (000' mtpa)



Source: Industry, PL

Exhibit 2: New phenol-acetone capacity additions in China (mtpa)

Company Name	Phenol Capacity	Acetone Capacity	Start up	Current Status
Fuyu Chemical	2,20,000	1,30,000	2024	Constructing
Huasheng	4,00,000	2,40,000	2025	Constructing
Ruilin Chemical	2,20,000	1,30,000	2025	Constructing
Jilin PC	2,20,000	1,30,000	2025	Constructing
ZRCC Phase II	4,00,000	2,50,000	2026	Constructing
Fujian Gulei	2,50,000	1,50,000	2026	Constructing
Shiyou Phase II	2,80,000	1,70,000	2027	Planning
SanMu	4,00,000	2,50,000	2027	Planning
Jinkong Energy	2,00,000	1,20,000	2028+	Planning
Luxi	2,00,000	1,20,000	2028+	Planning
Jiantao	2,19,000	1,35,000	2028+	Planning
Bohai Chemica	2,20,000	1,30,000	2028+	Planning
Zhenghua	1,50,000	90,000	2028+	Planning
Xinhui	3,00,000	1,85,000	2028+	Planning
Baling PC	2,20,000	1,30,000	2028+	Planning
ZPC Jintang	4,00,000	2,50,000	2028+	Planning
Chuangui Energy	1,62,000	98,000	2028+	Planning
Rongsheng	4,00,000	2,50,000	2028+	Planning

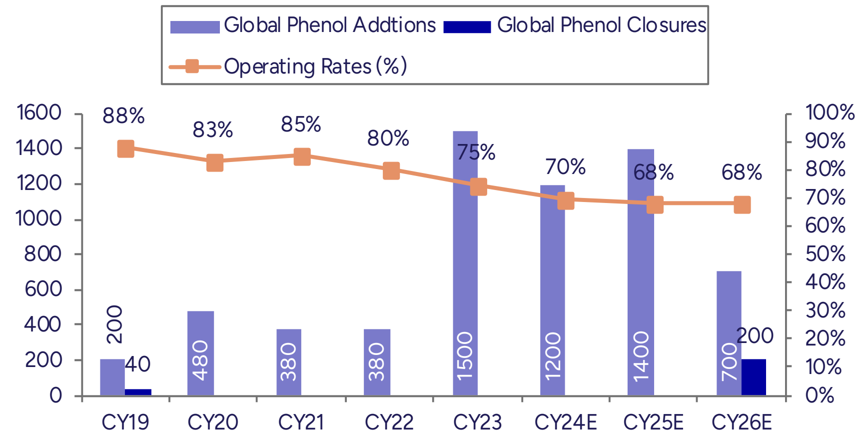
Source: Industry, PL

Exhibit 3: New BPA capacity additions in China (mtpa)

Company Name	BPA Capacity	Start up	Status
Haiwan Shandong	2,40,000	2024	In Operation
Hengli Liaoning	4,80,000	2024	In Operation
Kingboard Phase II	2,40,000	2024	Constructing
Fuyu Chemical	1,80,000	2024	Constructing
Shenma Phase II	2,40,000	2025	Constructing
Ruilin Chemical	2,40,000	2025	Constructing
Jilin PC	2,40,000	2025	Constructing
Shenghong	2,00,000	2026	Constructing
Huasheng Phase II	2,40,000	2026	Constructing
ZRCC Phase II	2,40,000	2026	Constructing
Fujian Gulei	2,70,000	2027	Constructing
Shiyou Phase II	2,40,000	2027	Planning
CSPC	2,40,000	2027	Planning
SanMu	5,00,000	2027	Planning
ZPC Jintang	4,80,000	2028+	Planning
Baling PC	2,40,000	2028+	Planning
Kingboard Caofeidian	1,80,000	2028+	Planning
Yingkou Jiafu	1,30,000	2028+	Planning
Bohai Chemical	3,40,000	2028+	Planning
Jinkong Energy	1,80,000	2028+	Planning
Zhenghua	1,80,000	2028+	Planning
Chuangui Energy	1,80,000	2028+	Planning
Rongsheng	4,80,000	2028+	Planning

Source: Industry, PL

Exhibit 4: Global phenol capacity additions ('000 mtpa)



Source: Industry, PL

- **DN's polycarbonate investment to generate 10-11% ROCE:** As of FY24, India's polycarbonate imports stood at 280tmtpa. Assuming DN captures 33% market share with a production capacity of 100tmtpa, the company would need to invest $250mn to establish the polycarbonate plant, as per our understanding. This project is expected to achieve peak revenue of $215mn. With an EBITDA margin of 13%, the investment would yield an ROCE of 10-11%, compared with average 23% during FY19-24.

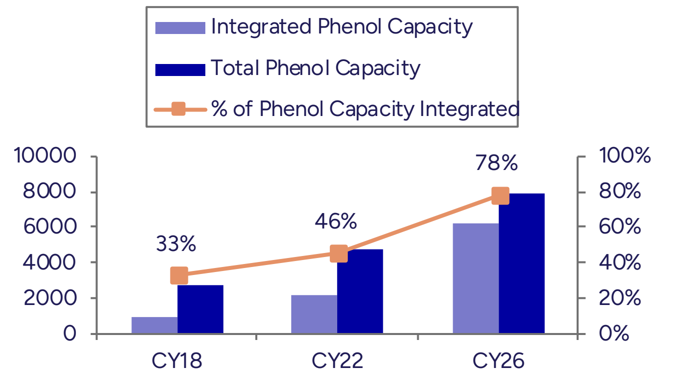
Exhibit 5: Polycarbonate investment ROCE calculations

Assumptions:	
Production capacity (mtpa)	1,00,000
Polycarbonate price (USD/mt)	2,154
Rev (USDmn)	215
EBITDAM (%)	13%
EBITDA (USDmn)	28
Capex (USDmn)	250
Depreciation (USDmn)	10
EBIT (USDmn)	38
EBIT (1-T)	28
ROCE (%)	11

Source: Industry, PL

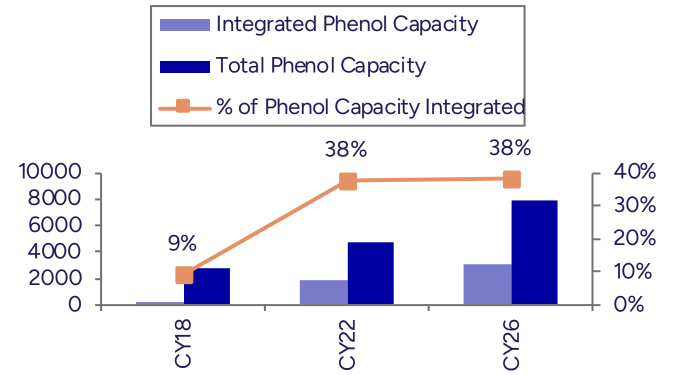
- **Any potential anti-dumping duty will be a risk to our call:** In 2018, DN began manufacturing isopropyl alcohol (IPA) as an import substitute. However, low-priced IPA imports from China to India surged by nearly 103% from FY22 to FY23, creating significant pricing pressure. To protect domestic producers, the Government of India is considering imposing an anti-dumping duty on IPA. If similar anti-dumping measures are implemented, it will be a risk to our call.

Exhibit 6: Integration of phenol to BPA in China



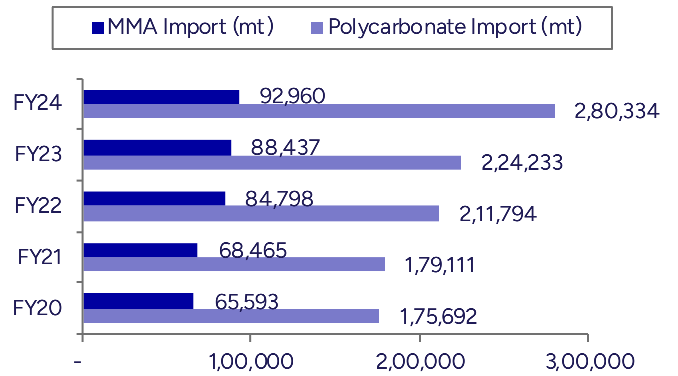
Source: Industry, PL

Exhibit 7: Integration of phenol to BPA & PC/epoxy in China



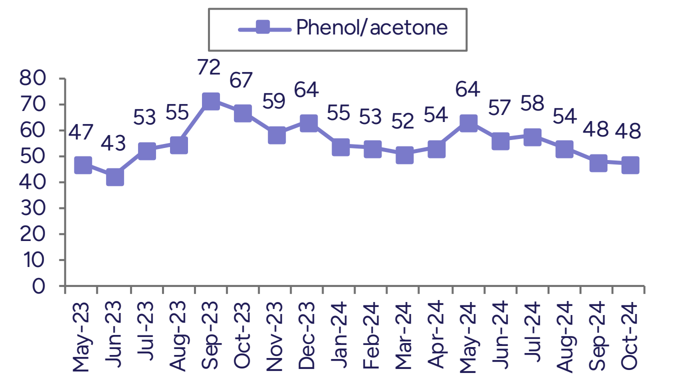
Source: Industry, PL

Exhibit 8: MMA and polycarbonate imports rising in India



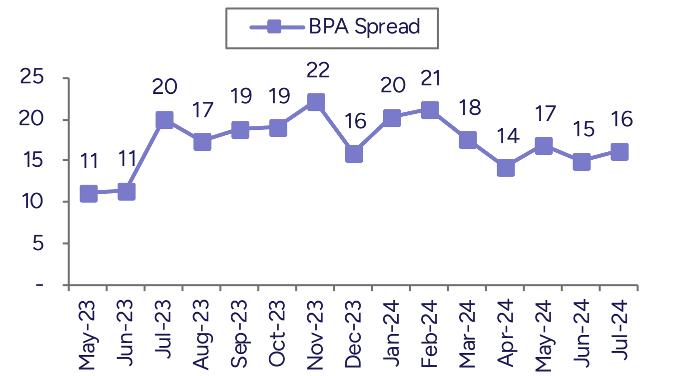
Source: MoC, PL

Exhibit 9: Phenol-acetone spread at Rs48/kg in Oct'24



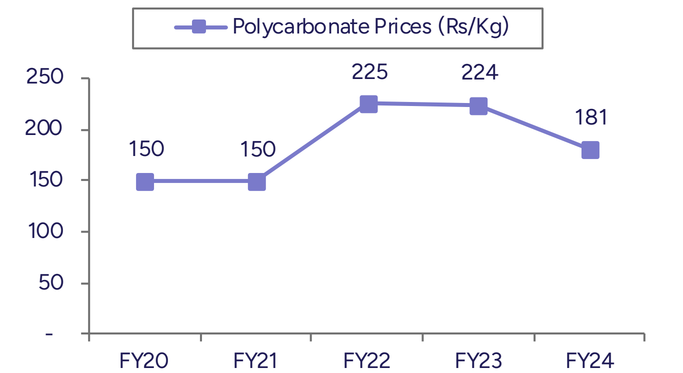
Source: Industry, PL

Exhibit 10: BPA spread at Rs16/kg in Jul'24



Source: MoC, PL

Exhibit 11: Polycarbonate prices declined by 19% in FY24



Source: MoC, PL

Financials

Income Statement (Rs m)

Y/e Mar	FY24	FY25E	FY26E	FY27E
Net Revenues	**76,818**	**85,925**	**89,057**	**97,753**
YoY gr. (%)	*(3.6)*	*11.9*	*3.6*	*9.8*
Cost of Goods Sold	52,361	58,515	60,114	65,494
Gross Profit	24,457	27,410	28,944	32,258
Margin (%)	*31.8*	*31.9*	*32.5*	*33.0*
Employee Cost	3,511	3,872	4,252	4,668
Other Expenses	9,714	10,311	10,687	11,730
EBITDA	**11,233**	**13,227**	**14,005**	**15,860**
YoY gr. (%)	*(12.9)*	*17.8*	*5.9*	*13.2*
Margin (%)	*14.6*	*15.4*	*15.7*	*16.2*
Depreciation and Amortization	1,657	1,999	2,314	2,636
EBIT	**9,576**	**11,228**	**11,691**	**13,224**
Margin (%)	*12.5*	*13.1*	*13.1*	*13.5*
Net Interest	118	286	525	788
Other Income	761	687	712	782
Profit Before Tax	**10,219**	**11,629**	**11,878**	**13,218**
Margin (%)	*13.3*	*13.5*	*13.3*	*13.5*
Total Tax	2,908	3,024	3,088	3,437
Effective tax rate (%)	*28.5*	*26.0*	*26.0*	*26.0*
Profit after tax	**7,311**	**8,606**	**8,790**	**9,781**
Minority interest	-	-	-	-
Share Profit from Associate	-	-	-	-
Adjusted PAT	**8,109**	**8,606**	**8,790**	**9,781**
YoY gr. (%)	*(4.8)*	*6.1*	*2.1*	*11.3*
Margin (%)	*10.6*	*10.0*	*9.9*	*10.0*
Extra Ord. Income / (Exp)	-	-	-	-
Reported PAT	**8,109**	**8,606**	**8,790**	**9,781**
YoY gr. (%)	*(4.8)*	*6.1*	*2.1*	*11.3*
Margin (%)	*10.6*	*10.0*	*9.9*	*10.0*
Other Comprehensive Income	-	-	-	-
Total Comprehensive Income	8,109	8,606	8,790	9,781
Equity Shares O/s (m)	**136**	**136**	**136**	**136**
EPS (Rs)	**59.4**	**63.1**	**64.4**	**71.7**

Source: Company Data, PL Research

Balance Sheet Abstract (Rs m)

Y/e Mar	FY24	FY25E	FY26E	FY27E
Non-Current Assets				
Gross Block	**31,690**	**43,690**	**59,690**	**75,690**
Tangibles	31,690	43,690	59,690	75,690
Intangibles	-	-	-	-
Acc: Dep / Amortization	**8,763**	**10,762**	**13,076**	**15,712**
Tangibles	8,763	10,762	13,076	15,712
Intangibles	-	-	-	-
Net fixed assets	**22,927**	**32,928**	**46,614**	**59,978**
Tangibles	22,927	32,928	46,614	59,978
Intangibles	-	-	-	-
Capital Work In Progress	7,735	7,735	7,735	7,735
Goodwill	-	-	-	-
Non-Current Investments	1,219	1,219	1,219	1,219
Net Deferred tax assets	(1,736)	(1,736)	(1,736)	(1,736)
Other Non-Current Assets	-	-	-	-
Current Assets				
Investments	-	-	-	-
Inventories	7,599	8,423	8,696	9,489
Trade receivables	12,984	14,523	12,200	13,391
Cash & Bank Balance	4,655	3,912	2,133	845
Other Current Assets	3,844	4,300	4,457	4,892
Total Assets	**60,962**	**73,040**	**83,053**	**97,548**
Equity				
Equity Share Capital	273	273	273	273
Other Equity	47,693	55,213	62,894	71,442
Total Networth	**47,966**	**55,486**	**63,167**	**71,715**
Non-Current Liabilities				
Long Term borrowings	2,170	6,000	8,000	13,000
Provisions	-	-	-	-
Other non current liabilities	-	-	-	-
Current Liabilities				
ST Debt / Current of LT Debt	-	-	-	-
Trade payables	5,823	6,454	6,663	7,270
Other current liabilities	3,007	3,364	3,486	3,827
Total Equity & Liabilities	**60,963**	**73,040**	**83,053**	**97,548**

Source: Company Data, PL Research

Cash Flow (Rs m)

Y/e Mar	FY24	FY25E	FY26E	FY27E
PBT	11,017	11,629	11,878	13,218
Add. Depreciation	1,657	1,999	2,314	2,636
Add. Interest	118	286	525	788
Less Financial Other Income	761	687	712	782
Add. Other	(627)	-	-	-
Op. profit before WC changes	12,165	13,914	14,717	16,642
Net Changes-WC	(720)	(1,831)	2,225	(1,471)
Direct tax	(2,665)	(3,024)	(3,088)	(3,437)
Net cash from Op. activities	**8,781**	**9,060**	**13,854**	**11,734**
Capital expenditures	(7,685)	(12,000)	(16,000)	(16,000)
Interest / Dividend Income	40	-	-	-
Others	427	-	-	-
Net Cash from Invt. activities	**(7,218)**	**(12,000)**	**(16,000)**	**(16,000)**
Issue of share cap. / premium	-	-	-	-
Debt changes	1,679	3,831	2,000	5,000
Dividend paid	(1,023)	(1,086)	(1,109)	(1,234)
Interest paid	(98)	(286)	(525)	(788)
Others	(123)	-	-	-
Net cash from Fin. activities	**435**	**2,459**	**366**	**2,978**
Net change in cash	**1,998**	**(482)**	**(1,780)**	**(1,288)**
Free Cash Flow	1,096	(2,940)	(2,146)	(4,266)

Source: Company Data, PL Research

Quarterly Financials (Rs m)

Y/e Mar	Q3FY24	Q4FY24	Q1FY25	Q2FY25E
Net Revenue	**20,092**	**21,262**	**21,668**	**21,481**
YoY gr. (%)	*0.9*	*8.4*	*22.5*	*20.8*
Raw Material Expenses	13,726	14,740	15,002	14,629
Gross Profit	6,366	6,522	6,667	6,852
Margin (%)	*31.7*	*30.7*	*30.8*	*31.9*
EBITDA	**3,047**	**3,011**	**3,092**	**3,307**
YoY gr. (%)	*(3.2)*	*(13.5)*	*47.4*	*9.4*
Margin (%)	*15.2*	*14.2*	*14.3*	*15.4*
Depreciation / Depletion	417	464	475	500
EBIT	**2,630**	**2,547**	**2,617**	**2,807**
Margin (%)	*13.1*	*12.0*	*12.1*	*13.1*
Net Interest	29	44	58	71
Other Income	136	191	188	172
Profit before Tax	**2,736**	**3,492**	**2,748**	**2,907**
Margin (%)	*13.6*	*16.4*	*12.7*	*13.5*
Total Tax	715	953	723	756
Effective tax rate (%)	*26.1*	*27.3*	*26.3*	*26.0*
Profit after Tax	**2,020**	**2,539**	**2,025**	**2,151**
Minority interest	-	-	-	-
Share Profit from Associates	-	-	-	-
Adjusted PAT	**2,020**	**2,539**	**2,025**	**2,151**
YoY gr. (%)	*(3.3)*	*8.6*	*35.1*	*4.9*
Margin (%)	*10.1*	*11.9*	*9.3*	*10.0*
Extra Ord. Income / (Exp)	-	-	-	-
Reported PAT	**2,020**	**2,539**	**2,025**	**2,151**
YoY gr. (%)	*(3.3)*	*8.6*	*35.1*	*4.9*
Margin (%)	*10.1*	*11.9*	*9.3*	*10.0*
Other Comprehensive Income	-	-	-	-
Total Comprehensive Income	**2,020**	**2,539**	**2,025**	**2,151**
Avg. Shares O/s (m)	136	136	136	136
EPS (Rs)	**14.9**	**18.7**	**14.9**	**15.8**

Source: Company Data, PL Research

Key Financial Metrics

Y/e Mar	FY24	FY25E	FY26E	FY27E
Per Share(Rs)				
EPS	59.4	63.1	64.4	71.7
CEPS	71.6	77.7	81.4	91.0
BVPS	351.7	406.8	463.1	525.8
FCF	8.0	(21.6)	(15.7)	(31.3)
DPS	7.5	8.0	8.1	9.0
Return Ratio(%)				
RoCE	20.9	20.1	17.6	17.0
ROIC	15.8	16.1	13.7	12.8
RoE	18.2	16.6	14.8	14.5
Balance Sheet				
Net Debt : Equity (x)	(0.1)	0.0	0.1	0.2
Net Working Capital (Days)	70	70	58	58
Valuation(x)				
PER	50.5	47.5	46.5	41.8
P/B	8.5	7.4	6.5	5.7
P/CEPS	41.9	38.6	36.8	32.9
EV/EBITDA	36.2	31.1	29.6	26.6
EV/Sales	5.3	4.8	4.7	4.3
Dividend Yield (%)	0.3	0.3	0.3	0.3

Source: Company Data, PL Research

Price Chart

Recommendation History

No.	Date	Rating	TP (Rs.)	Share Price (Rs.)
1	05-Oct-24	Reduce	2,564	2,829
2	22-Aug-24	Reduce	2,717	2,970
3	09-Aug-24	Reduce	2,780	3,055
4	04-Jul-24	Reduce	2,268	2,677
5	22-May-24	Reduce	2,268	2,464
6	09-Apr-24	Reduce	1,985	2,208
7	15-Feb-24	Reduce	1,985	2,283
8	08-Jan-24	Reduce	1,881	2,451
9	10-Nov-23	Reduce	1,935	2,076

Analyst Coverage Universe

Sr. No.	Company Name	Rating	TP (Rs)	Share Price (Rs)
1	Aarti Industries	Reduce	512	551
2	Ashok Leyland	Accumulate	257	222
3	Bajaj Auto	Hold	11,146	11,628
4	Bharat Forge	Accumulate	1,369	1,437
5	Bharat Petroleum Corporation	Sell	279	335
6	Bharti Airtel	Accumulate	1,831	1,657
7	CEAT	Hold	3,107	2,938
8	Clean Science and Technology	Hold	1,561	1,579
9	Deepak Nitrite	Reduce	2,564	2,829
10	Divgi Torqtransfer Systems	Hold	633	591
11	Eicher Motors	BUY	5,416	4,668
12	Endurance Technologies	Accumulate	2,569	2,182
13	Exide Industries	Hold	520	481
14	Fine Organic Industries	Accumulate	5,568	5,142
15	GAIL (India)	Sell	205	224
16	Gujarat Fluorochemicals	Reduce	3,771	4,065
17	Gujarat Gas	Hold	646	596
18	Gujarat State Petronet	Hold	422	411
19	Hero Motocorp	Accumulate	5,906	5,495
20	Hindustan Petroleum Corporation	Sell	362	394
21	Indian Oil Corporation	Reduce	156	163
22	Indraprastha Gas	Sell	407	543
23	Jubilant Ingrevia	Hold	770	794
24	Laxmi Organic Industries	Sell	218	276
25	Mahanagar Gas	Hold	2,050	1,825
26	Mahindra & Mahindra	BUY	3,458	3,060
27	Mangalore Refinery & Petrochemicals	Sell	128	173
28	Maruti Suzuki	BUY	15,045	12,528
29	Navin Fluorine International	Accumulate	3,680	3,419

PL's Recommendation Nomenclature (Absolute Performance)

Buy : > 15%
Accumulate : 5% to 15%
Hold : +5% to -5%
Reduce : -5% to -15%
Sell : < -15%
Not Rated (NR) : No specific call on the stock
Under Review (UR) : Rating likely to change shortly

ANALYST CERTIFICATION

(Indian Clients)

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