AMSEC Raising the bar

Asian Markets Securities Pvt. Ltd.

Institutional Research

Specialty Chemicals | 3QFY19 Result Update

Deepak Nitrite Ltd

BUY

CMP (Rs)	**228**
Target (Rs)	**300**
Upside	**32%**

Nifty: 11,062; Sensex: 36,975

Key Stock Data

Bloomberg	DNLL IN
Shares O/s Mn (FV INR2)	136.4
Mkt Cap(USD Bn/INR Bn)	0.4/31.1
52-week high/low	305/205
6m daily avg vol(INR Mn)	94
Free Float %	53%

Rel. Performance

(%)	1m	3m	12m
DNL	3.1	(17.8)	(11.3)
NIFTY	3.1	5.1	5.4
SENSEX	3.6	5.7	8.1

Shareholding Pattern

(%)	Jun18	Sep18	Dec18
Promoter	44.6	44.6	44.6
FII	10.5	9.9	10.7
DII	13.6	14.1	14.6
Others	31.3	31.4	30.1

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Performance beat on all fronts

Deepak Nitrite (DNL) reported a robust standalone revenue growth of 21.9% y/y led by strong growth across segments especially performance products. Higher realisation and favourable product mix led to 325bps y/y expansion in gross margins to 44.3%. DNL started commercial production of phenol-acetone during the quarter and is already operating at ~85% capacity utilisation currently. Revenue from the phenol-acetone business was Rs3.21bn leading to a consolidated revenue of Rs7.79bn (+110% y/y) in the quarter. Management mentioned that the overall acceptance for its phenol-acetone business has been strong and expects the business to deliver ~16-18% average RoCE in the long run. With the standalone business delivering robust growth on 9MFY19 nos. (23/27% revenue/EBITDA) and with strong initial execution of the phenol-acetone business, we believe the stock has a strong re-rating potential. While we upgrade our FY19EEPS estimates by 17.8%, we maintain our FY20EEPS estimates as we await further clarity on the performance of the new business. Maintain BUY with Rs300TP.

Favourable product mix continue to drive margin expansion

DNL reported a robust growth across segment for the second consecutive quarter with performance products reporting 47.8% y/y revenue growth to Rs995m. DNL's focused approach on driving margin led growth in the segment coupled with supply disruption in DASDA has led to sharp 18.2% EBIT margins in the segment (+355bps expansion q/q). Basic chemicals (BC) and Fine & Specialty chemical (FSC) segments grew 15.9% and 21.2% y/y to Rs 2,194m and 1,484m respectively. While margins in BC and FSC segments expanded by 46bps & 93bps y/y to 15.4% and 23.1% respectively, currency fluctuations during the quarter led to marginal dip in margins sequentially in both the segments. Overall standalone EBITDAM expanded 57bps y/y to 14.6%. Strong growth coupled with higher other income (+Rs55m vs 5m y/y) led to a robust 55.4% growth in net profit to Rs316m.

Initial updates from the phenol-acetone business quite encouraging

DNL reported Rs3,210m revenue from the newly commissioned phenol-acetone business and achieved operational breakeven with EBITDA of ~Rs370m and PBT of ~Rs120m. Management highlighted that the ramp-up of the business is on track with the plant already operating at ~85% utilisation levels. Company expects to achieve ~90%+ full-year utilisation levels starting FY20 onwards. The average input-output spread during the quarter was ~US$580-600/MT and the current spread levels are at ~US$800/MT. DNL has been able to capture domestic market share and has not witnessed any strong competitive pressure from importers currently. Company has started supplying pharma grade acetone and is also in process of developing further applications of acetone. DNL has also started some initial exports of acetone.

Maintain BUY

At13.5x FY21EEPS (0.23x FY21 PEG), DNL is trading at attractive valuations and in-light of the recent PE re-rating seen in other chemical companies, we believe DNL is one company which has a strong re-rating potential especially with successful initial commissioning of its phenol-acetone business. Along with this, a sharp turnaround in its performance products business coupled with sustained growth momentum in BC and FSC segment has helped DNL achieve strong profitability. We expect DNL to achieve 70% EPS CAGR over FY18-20E with strong expansion in RoACE from 9.2% in FY18 to 19.4% by FY20E. Maintain BUY with Rs300TP (18x FY20EEPS)

Exhibit 1: Key Financials (Consolidated)

Y/E Mar (Rs mn)	FY17	FY18	FY19E	FY20E
Sales	13707	16515	24895	39994
yoy (%)	*-0.2*	*20.5*	*50.7*	*60.7*
EBIDTA	1355	1962	4145	6085
yoy (%)	*-18.8*	*44.8*	*111.2*	*46.8*
PAT	458	790	1439	2274
yoy (%)	*-26.9*	*72.4*	*82.1*	*58.0*
Equity	261.4	272.8	272.8	272.8
EPS (Rs)	3.5	5.8	10.5	16.7

Exhibit 2: Key Indicators

Y/E Mar	FY17	FY18	FY19E	FY20E
EBIDTAM (%)	9.9	11.9	16.6	15.2
NPM (%)	3.3	4.8	5.8	5.7
PER (x)	65.0	39.4	21.6	13.7
P/BV (x)	4.2	3.4	3.0	2.5
EV/Sales (x)	2.7	2.5	1.8	1.1
EV/ EBITDA (x)	27.2	20.6	10.6	7.3
RoCE (%)*	7.8	9.2	15.1	19.4
RoE (%)	16.2	9.7	14.6	20.0

*Source: Company, AMSEC Research, *Core RoCE is Pretax EBIT/Capital employed less cash and investments*

Exhibit 3: 3QFY19 Performance (Standalone)

(Rs mn)	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	YoY(%)	QoQ(%)	9MFY18	9MFY19	YoY(%)
Net sales	3,373	3,536	3,711	3,929	4,210	4,327	4,523	21.9%	4.5%	10,620	13,060	23.0%
Consumption of raw materials	1,943	1,960	2,144	2,352	2,566	2,402	2,628	22.6%	9.4%	6,047	7,596	25.6%
Changes in inventories	-40	49	43	-13	-76	-147	-110	na	na	52	-333	na
Power & Fuel cost	288	298	300	313	319	393	368	22.5%	-6.4%	885	1,079	21.9%
Employee cost	315	330	346	330	366	403	417	20.5%	3.4%	991	1,187	19.8%
Other expenditure	363	389	356	457	475	590	558	56.7%	-5.6%	1,108	1,580	42.6%
Total expenditure	2,868	3,025	3,189	3,440	3,649	3,641	3,861	21.1%	6.0%	9,082	11,109	22.3%
Ebitda	**504**	**511**	**522**	**490**	**561**	**686**	**662**	**26.8%**	**-3.5%**	**1,538**	**1,952**	**26.9%**
Other income	21	26	5	65	8	3	55	1014.2%	1553.6%	52	23	-54.6%
Depreciation	123	133	130	134	126	132	133	2.7%	1.0%	386	391	1.4%
Interest	95	107	90	111	109	117	103	14.8%	-11.4%	292	329	12.7%
Exceptional	0	0	0	0	0	0	0	na	na	0	0	na
Profit before tax	**307**	**297**	**307**	**309**	**334**	**441**	**480**	**56.4%**	**9.0%**	**912**	**1,255**	**37.6%**
Provision for taxation	106	71	104	106	116	160	164	58.4%	2.7%	280	440	56.9%
PAT	**201**	**226**	**203**	**203**	**218**	**281**	**316**	**55.4%**	**12.7%**	**631**	**815**	**29.0%**
Other comprehensive income	-4	0	-4	16	1	1	-4	-8.7%	-407.9%	-7	-1	na
TCI	**197**	**226**	**199**	**219**	**219**	**282**	**313**	**56.7%**	**10.9%**	**624**	**814**	**30.4%**
Equity Capital (FV=Rs1)	261	261	261	273	273	273	273	na	na	261	273	4.3%
O/S Shares	131	131	131	136	136	136	136	na	na	131	136	4.3%
Adj. EPS (Rs)	**1.5**	**1.7**	**1.6**	**1.5**	**1.6**	**2.1**	**2.3**	**49.0%**	**12.7%**	**4.8**	**6.0**	**23.7%**

Source: Company, AMSEC Research

Exhibit 4: Common Size (% of Revenue)

Particulars	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19
COGS	56.4%	56.8%	58.9%	59.5%	59.1%	52.1%	55.7%
Power & Fuel	8.4%	8.1%	8.0%	7.6%	9.1%	9.1%	8.1%
Employee expenses	9.3%	9.3%	8.4%	8.7%	9.3%	9.3%	9.2%
Other expenses	11.0%	9.6%	11.6%	11.3%	13.6%	13.6%	12.3%
EBITDA	**14.4%**	**14.1%**	**12.5%**	**13.3%**	**15.9%**	**15.9%**	**14.6%**
Other income	0.7%	0.1%	1.6%	0.2%	0.1%	0.1%	1.2%
Depreciation	3.8%	3.5%	3.4%	3.0%	3.0%	3.0%	2.9%
Finance costs	3.0%	2.4%	2.8%	2.6%	2.7%	2.7%	2.3%
PBT	8.4%	8.3%	7.9%	7.9%	10.2%	10.2%	10.6%
Tax expenses (% of PBT)	23.8%	33.8%	34.2%	34.7%	36.3%	36.3%	34.2%
PAT	**6.4%**	**5.5%**	**5.2%**	**5.2%**	**6.5%**	**6.5%**	**7.0%**

Exhibit 5: Segment Revenue (Rs Mn)

Particulars	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	YoY(%)	QoQ(%)	9MFY18	9MFY19	YoY(%)
Basic Chemical	1,972	1,700	1,892	1,975	2,226	2,017	2,194	15.9%	8.8%	5,605	6,437	15%
Fine & Speciality Products	1,129	1,129	1,224	1,212	1,224	1,438	1,484	21.2%	3.2%	3,421	4,145	21%
Performance products	842	842	674	820	805	968	995	47.8%	2.8%	2,173	2,769	27%
Other un-allocable	1	0	0	0	0	0	0	na	na	1	0	na
less: Intersegment	83	134	78	77	45	96	150	90.8%	56.6%	337	290	-14%
Total	**3,615**	**3,536**	**3,711**	**3,929**	**4,210**	**4,327**	**4,523**	**21.9%**	**4.5%**	**10,863**	**13,060**	**20%**

Source: Company, AMSEC Research

Exhibit 6: EBIT Margin (% of Revenue)

Particulars	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19
Basic Chemical	12.0%	15.4%	15.0%	14.4%	14.5%	17.9%	15.4%
Fine & Speciality Products	29.4%	23.2%	22.1%	24.8%	23.4%	25.9%	23.1%
Performance products	-6.1%	0.1%	-1.9%	-3.5%	3.8%	14.6%	18.2%

Source: Company, AMSEC Research

Exhibit 7: 3QFY19 Revenue Mix

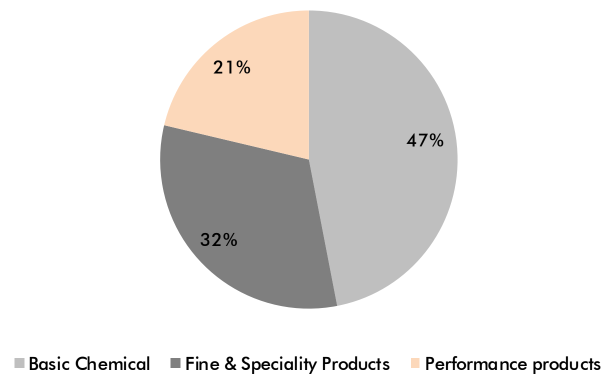


Exhibit 8: 3QFY19 - EBIDTA Mix

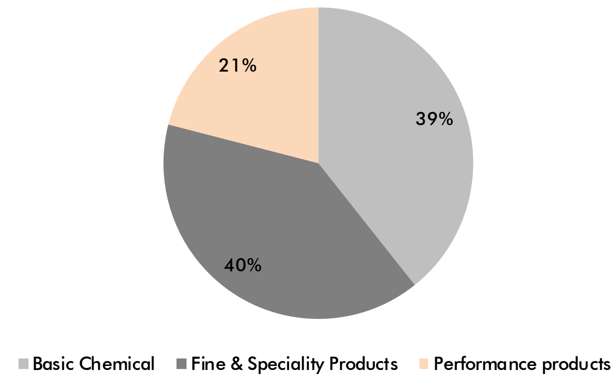


Exhibit 9: Robust revenue growth of 21.9% y/y to Rs4,523m

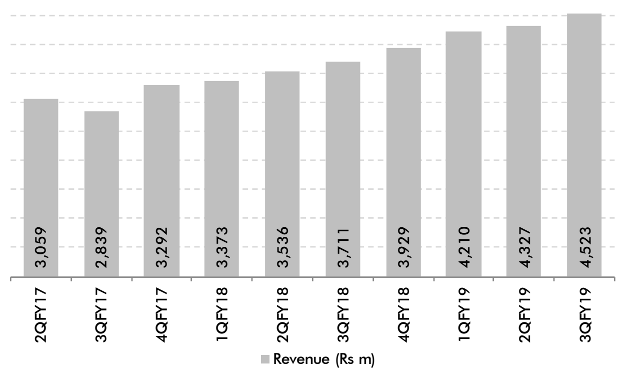


Exhibit 10: Gross margins expansion of 325bps y/y to 44.3%

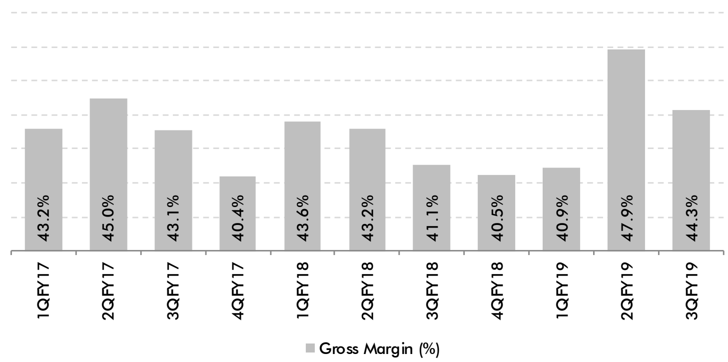


Exhibit 11: EBITDAM improved marginally by 57bps y/y to 14.6%

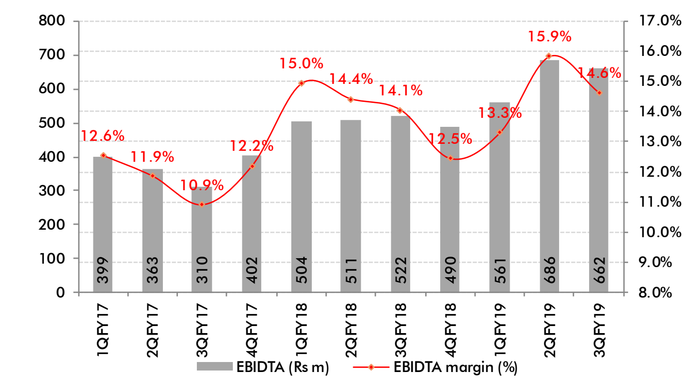
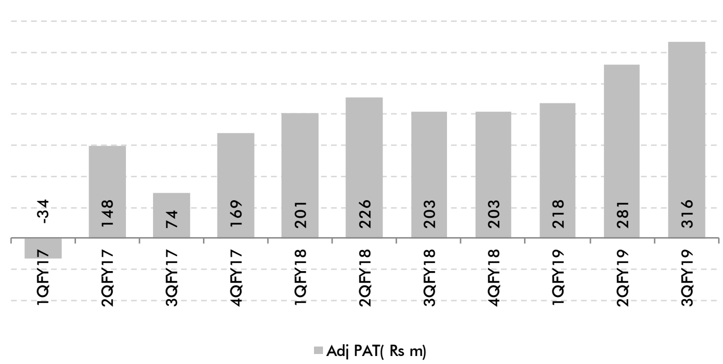


Exhibit 12: Strong operational growth coupled with higher other income led to strong 55% growth in net profit



Source: Company, AMSEC Research

Financials (Consolidated)

(Rs mn)

Profit & Loss Account

Y/E (Mar)	FY17	FY18	FY19E	FY20E
Net sales	**13707**	**16515**	**24895**	**39994**
COGS	8459	10388	15807	26271
Staff Expenses	1223	1362	1636	1750
Other Operating expenses	2671	2803	3307	5887
Total expenditure	12352	14553	20750	33908
EBITDA	**1355**	**1962**	**4145**	**6085**
Depreciation	480	526	1002	1250
Operating Profit	**874**	**1436**	**3142**	**4836**
Other income	109	124	76	123
EBIT	**983**	**1560**	**3218**	**4959**
Interest	341	451	1163	1711
Exceptional income/expense	705	0	0	0
Profit Before Tax	**1347**	**1109**	**2056**	**3248**
Tax	382	318	617	974
Reported Net Profit	**965**	**790**	**1439**	**2274**
Extra Ordinary Items	0	0	0	0
Share of profit/(Loss) of associate	-1	0	0	0
Adjusted Net Profit	**458**	**790**	**1439**	**2274**
Share O/s mn	130.7	136.4	136.4	136.4
Adj. EPS Rs	**3.5**	**5.8**	**10.5**	**16.7**

Cash Flow Statement

Y/E (Mar)	FY17	FY18	FY19E	FY20E
PBT	1347	1109	2056	3248
Non-cash adjustments	77	1009	2165	2960
Changes in working capital	-772	-9	-2958	-2546
Tax Paid	162	279	617	974
Cashflow from operations	**490**	**1830**	**646**	**2688**
Capital expenditure	-2962	-6223	-2700	-1200
Change in investments	0	0	0	0
Other investing activity	-563	976	0	0
Cashflow from investing	**-3526**	**-5247**	**-2700**	**-1200**
Issue of equity	1464	1463	0	0
Proceeds from security premiu	2184	4758	0	0
Issue/repay debt	-24	-2132	4000	-361
Interest Paid	-342	-450	-1163	-1711
Dividends paid	-167	-188	-214	-433
Others	-69	2	0	0
Cashflow from financing	**3046**	**3453**	**2623**	**-2504**
Change in cash & cash eq	11	36	569	-1016
Opening cash & cash eq	**48**	**58**	**482**	**1051**
Closing cash & cash eq	**58**	**94**	**1051**	**35**
Free Cash Flow to firm	**-2472**	**-4393**	**-2054**	**1488**

Balance Sheet

Y/E (Mar)	FY17	FY18	FY19E	FY20E
SOURCES OF FUNDS :				
Share Capital	261	273	273	273
Reserves Total	6887	8949	10174	12015
Total Shareholders Funds	**7149**	**9221**	**10446**	**12288**
Minority Interest	0	0	0	0
Non-Current Liabilites	2653	6208	10253	10289
Long term borrowings	2184	5505	9505	9505
Defered tax liability	391	454	454	454
Other Long Term Liabilities	0	170	170	170
Long-term provisons	78	79	124	160
Long term trade payable				
Current Liabilities	**8073**	**10476**	**12553**	**16193**
Short term borrowings	5055	4361	4361	4000
Trade payables	2146	4824	6275	9314
Other current liabilties	832	1255	1867	2800
Short term provisions	41	35	50	80
Total Equity & Liabilities	**17875**	**25906**	**33252**	**38770**
APPLICATION OF FUNDS :				
Non Current Assets	**10369**	**15977**	**17686**	**17652**
Fixed Assets				
Gross Block	6165	6383	18628	19828
Less : Accumulated Depreciation	306	507	1509	2759
Net block	5859	5876	17119	17069
Capital Work in Progress	3492	9545	0	0
Intangible Asset under development	0	0	0	0
Goodwill on consolidation				
Non current investment	37	23	23	23
Long term loan and advances	14	13	25	40
Other non-current assets	967	520	520	520
Current Assets	**7506**	**9929**	**15566**	**21118**
Investment	1143	294	294	100
Inventories	1671	3254	4570	6574
Sundry Debtors	3603	4118	7161	10409
Cash and Bank	145	482	1051	35
Others Current Assets	943	1781	2489	3999
Total Assets	**17875**	**25906**	**33252**	**38770**
Net current asset	3199	3038	6029	8790
Total Gross Debt	7239	9865	13865	13505
Total Net debt	7094	9383	12814	13470
Total Capital Employed	14856	19791	25061	26576

Key Ratios

Y/E (Mar)	FY17	FY18	FY19E	FY20E
PER SHARE				
EPS	3.5	5.8	10.5	16.7
CEPS	7.2	9.6	17.9	25.8
BV	54.7	67.6	76.6	90.1
VALUATION				
EV/SALES	2.7	2.5	1.8	1.1
EV/EBIDTA	27.2	20.6	10.6	7.3
P/E RATIO	65.0	39.4	21.6	13.7
P/BV RATIO	4.2	3.4	3.0	2.5
GROWTH YOY%				
Sales Growth	-0.2	20.5	50.7	60.7
EBITDA Growth	-18.8	44.8	111.2	46.8
Net Profit Growth	-26.9	72.4	82.1	58.0
Gross Fixed Asset Growth	-30.7	3.5	191.8	6.4
PROFITABILITY				
Gross Profit/ Net sales (%)	38.3	37.1	36.5	34.3
EBITDA / Net Sales (%)	9.9	11.9	16.6	15.2
NPM / Total income (%)	3.3	4.8	5.8	5.7
Raw Material/Net Sales (%)	61.7	62.9	63.5	65.7
Int/PBIT (%)	34.7	28.9	36.1	34.5
ROE (%)	16.2	9.7	14.6	20.0
ROCE (%)*	7.8	9.2	15.1	19.4
ROIC (%)	7.7	9.0	14.4	19.2
Tax / PBT (%)	29.4	28.4	28.7	30.0
TURNOVER (Days)				
Net Working Cycle	83	56	80	70
Debtors Velocity	96	91	105	95
Inventory	45	72	67	60
Creditors Velocity	57	107	92	85
Gross Asset Ratio	1.8	2.6	2.0	2.1
Total Asset Ratio	0.9	0.8	0.8	1.1
LIQUIDITY (x)				
Gross Debt-Equity Ratio	1.0	1.1	1.3	1.1
Net Debt-Equity Ratio	1.0	1.0	1.2	1.1
Interest Coverage	2.9	3.5	2.8	2.9
Current Ratio (x)	0.9	0.9	1.2	1.3
Quick Ratio (x)	0.7	0.6	0.9	0.9
PAYOUT				
Payout (%)	19.6	27.1	30.1	30.1
Dividend (%)	60.0	65.0	158.2	250.1
Yield (%)	0.5	0.6	1.4	2.2

Source: Company, AMSEC Research, Core RoCE is Pretax EBIT/Capital employed less cash and investments

Recommendation rationale

Buy: Potential upside of	>+15% (absolute returns)
Accumulate:	>+5 to +15%
Hold/Reduce:	+5 to -5%
Sell:	< -5%
Not Rated (NR):	No investment opinion on the stock

Sector rating

Overweight:	The sector is expected to outperform relative to the Sensex.
Underweight:	The sector is expected to underperform relative to the Sensex.
Neutral:	The sector is expected to perform in line with the Sensex.

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