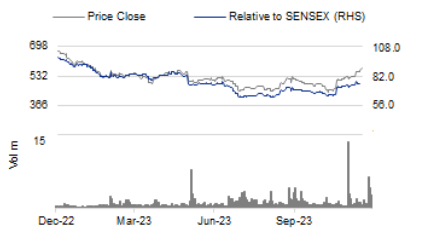


India

REDUCE (no change)

Consensus ratings*:	Buy 9	Hold 6	Sell 9
Current price:	Rs576		
Target price:	Rs435		
Previous target:	Rs435		
Up/downside:	-24.5%		
InCred Research / Consensus:	-19.2%		
Reuters:	ARTI.NS		
Bloomberg:	ARTO IN		
Market cap:	US\$2,505m	Rs208,694m	
Average daily turnover:	US\$9.8m	Rs819.8m	
Current shares o/s:	362.5m		
Free float:	60.5%		

*Source: Bloomberg



Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	12.9	11.6	(14.0)
Relative (%)	5.2	6.2	(23.0)

Major shareholders	% held
Promoter & Promoter Group	39.5
Morgan Stanley	3.1
HDFC Asset Management	2.7

Aarti Industries

Russian INR reserves won't help for long

- Aarti Industries is experiencing rising optimism due to MMA sales. Investors are misinterpreting rising sales as the China+1 strategy by Aarti's customers.
- Russia is importing MMA for the first time (significant qty) from Aarti by paying in Rs as it has high Rs reserves (It sold crude to India in Rs during CY22-23)
- Domestic concerns persist as YoY export growth is likely but a significant recovery in domestic demand, mostly for PDCB, is unlikely. Retain REDUCE.

Mono methyl-driven bullishness won't work for even two quarters

Rising MMA (mono methyl aniline) sales are fuelling the excitement among investors as many believe it's a China+1 strategy by buyers and may be that we have touched the cyclical bottom. In a nutshell, MMA exports are rising because suddenly Aarti Industries has found a new buyer, Russia, for its products. Russia is buying because it must utilize INR reserves which it has accumulated over the past 12 months when India and Russia were trading crude oil in INR (to circumvent the US sanctions). As it is widely known that now Russia wants the Chinese yuan in lieu of oil, this trade has a limited shelf life (please see the 'Times of India' article on this aspect by clicking this link). MMA exports to the UAE were always there and as the new refinery has started, they have picked up. Apart from MMA, nothing else is doing great. Even for MMA, rising aniline prices will lead to a fall in gross spreads. The cyclical recovery in the company's overall business is still far away. At best, Aarti Industries is a tactical trade as of now, but sell the stock before the results.

Domestic business raises concern

Aarti Industries' exports rely on two key products, namely PDCB (para-dichlorobenzene) and MMA (mono methyl aniline). Currently, the increase in export volume is primarily driven by higher MMA exports. While we can witness a YoY increase in exports in 3QFY24F, there isn't a significant recovery expected in domestic demand, particularly for PDCB, the traditionally significant molecule for Aarti Industries. PDCB margins remain stable QoQ but have witnessed a considerable YoY decline. Given PDCB's significance, its margin decline is likely to result in lower gross margin YoY, ultimately leading to a reduction in EPS. The overall slowdown in agrochemicals is impacting various chemical companies, and Aarti Industries is no exception to this trend.

Headwinds in its broader portfolio; retain REDUCE rating

Across the broader product portfolio, including di methyl sulphate (DMS), ortho nitro aniline (ONA), di methyl phthalate, and di chloro aniline, we have observed the trend of lower realization, and we believe this trend will persist. The demand for these commodity-nature products has remained weak. Once the situation stabilizes, it is likely that the spreads of most products will decline as most products manufactured by Aarti Industries are commodity chemicals. Our REDUCE rating on the stock remains unchanged with a target price of Rs435. Upside risk: Recovery in the prices of products in its portfolio. Check our earlier report on its product portfolio [Link](#).

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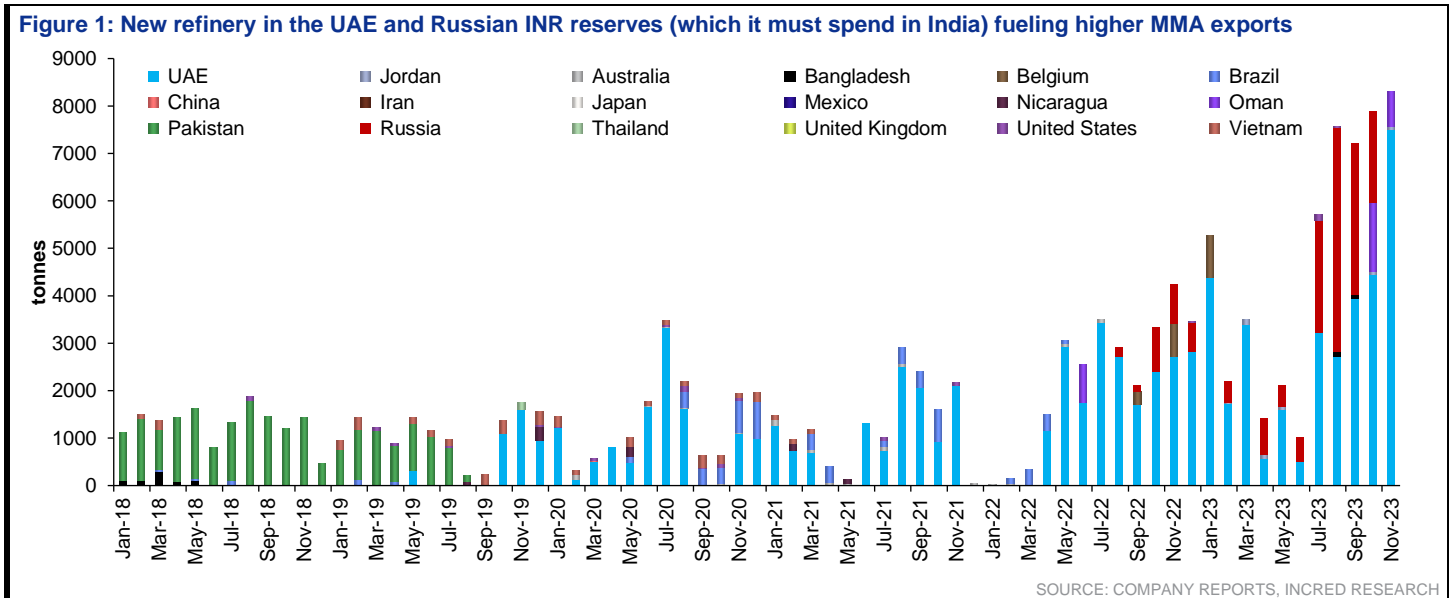
Financial Summary	Mar-22A	Mar-23A	Mar-24F	Mar-25F	Mar-26F
Revenue (Rsm)	70,000	66,186	68,171	74,989	83,987
Operating EBITDA (Rsm)	19,288	10,890	11,324	13,215	14,826
Net Profit (Rsm)	13,074	5,452	4,381	5,250	6,298
Core EPS (Rs)	36.1	15.0	12.1	14.5	17.4
Core EPS Growth	149.8%	(58.3%)	(19.7%)	19.9%	20.0%
FD Core P/E (x)	15.73	37.72	46.95	39.17	32.66
DPS (Rs)	3.5	2.5	2.5	2.5	2.5
Dividend Yield	0.62%	0.44%	0.44%	0.44%	0.44%
EV/EBITDA (x)	11.68	21.34	21.36	18.88	16.58
P/FCFE (x)	(18.68)	(1,029.45)	55.41	34.71	99.42
Net Gearing	33.1%	54.3%	68.7%	76.8%	64.3%
P/BV (x)	3.48	4.18	3.90	3.61	3.30
ROE	27.8%	10.1%	8.6%	9.6%	10.5%
% Change In Core EPS Estimates					
InCred Research/Consensus EPS (x)					

SOURCE: INCRED RESEARCH, COMPANY REPORTS

Russian INR reserves won't help for long

Rising MMA sales are fuelling the excitement among investors as many believe it's the China+1 strategy by customers and may be that we have touched the cyclical bottom. In a nutshell, MMA exports are rising because suddenly Aarti Industries has found a new buyer, Russia, for its products. Russia is buying because it must utilize INR reserves it has accumulated over the past 12 months when India and Russia were trading crude oil in INR (to circumvent the US sanctions). As it is widely known that now Russia wants the Chinese yuan in lieu of oil, so this trade has a limited shelf life ([please see the 'Times of India' report on this aspect by clicking the link](#)). Apart from MMA, nothing is doing great for the company. For MMA also, rising aniline prices are leading to a collapse in gross spreads.

MMA exports are suddenly exploding to the highest- ever level since the last six years



The UAE has always been a key destination for Aarti Industries' MMA exports. Russia is the new addition to the list. Please note that Russia has been importing MMA by making the payments in INR. As MMA is a low-value product, it doesn't make sense for Russia to import it from India by incurring higher freight costs but because of unusable INR reserves, it is forced to do the same.

MMA has wide usage in the industry ➤

Mono methyl aniline (MMA), also known as N-methylaniline or methyl aniline, is a chemical compound primarily used in various industrial applications due to its properties. Some common uses of mono methyl aniline include:

Chemical intermediates: MMA serves as an important intermediate chemical in the production of various compounds. It's used in the synthesis of dyes, pigments, pharmaceuticals, agrochemicals, and other organic chemicals.

Polyurethane production: It's used as a raw material in the production of polyurethane, a versatile polymer used in foams, coatings, adhesives, sealants, and elastomers in various industries, including construction, automotive, and furniture.

Corrosion inhibitors: MMA is employed in formulations for corrosion inhibitors to protect metals and alloys against corrosion in different industries, such as oil and gas, transportation, and manufacturing.

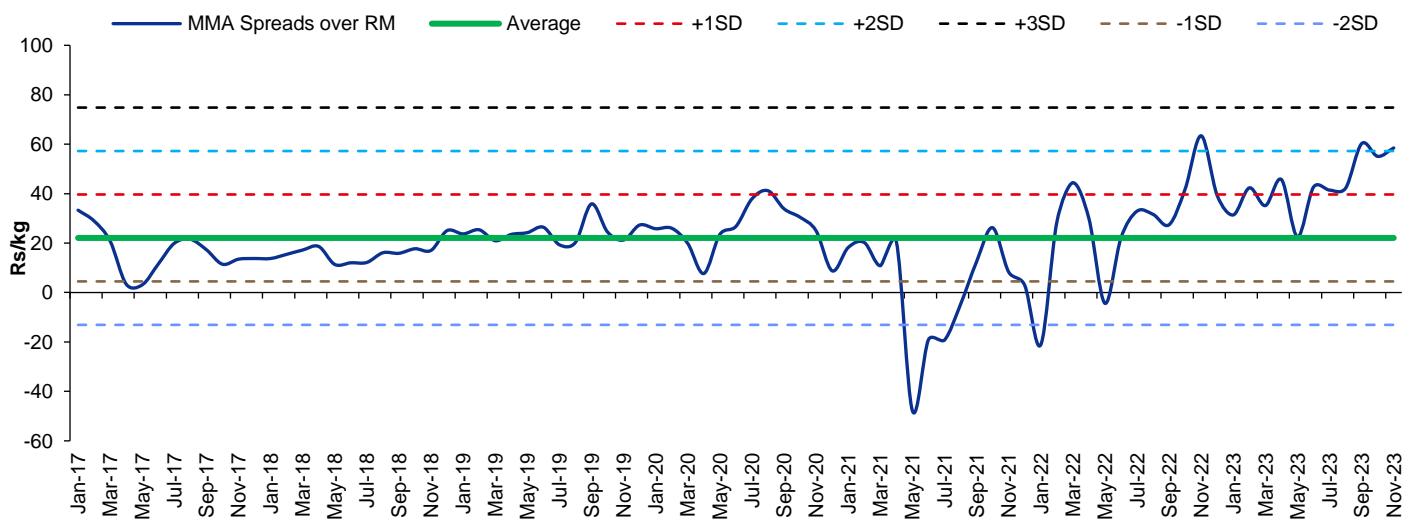
Chemical reactions: It's utilized as a reactant in several chemical reactions, particularly those involving aromatic compounds, in various synthesis processes across industries.

Research and development: MMA is also used in research and development endeavours for its chemical properties. It plays a role in the development of new compounds and materials.

Aarti Industries buys aniline to make MMA and hence, MMA spreads fall when aniline prices rise ➤

Normally 1 tonne (t) of MMA needs 0.89t of aniline. The MMA spreads over aniline are touching +2SD of the long-term mean. The sudden rise in demand for Indian aniline is fuelling this rise and we believe it will continue for some time.

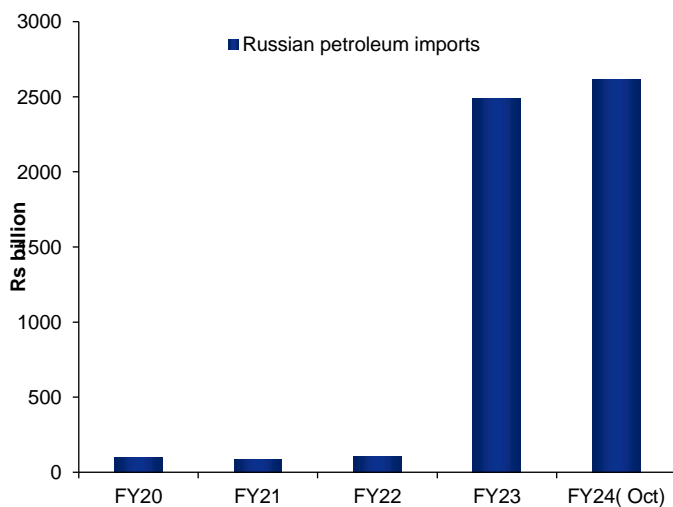
Figure 2: MMA spreads over aniline are at +2 SD of the long-term mean level and given the sudden spurt in demand for Indian MMA, they can remain elevated



SOURCE: INCRED RESEARCH, COMPANY REPORTS

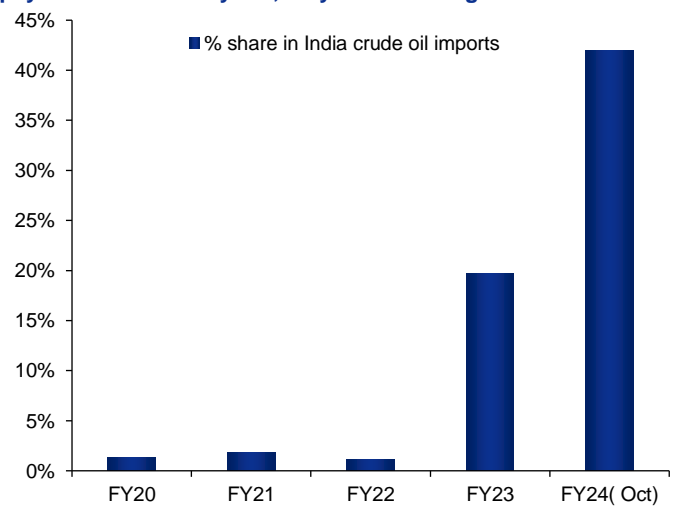
Russia's exports of crude oil to India touched Rs2.6tr so far in FY24 (YTD Oct) ➤

Figure 3: Russia exported ~Rs2.6tr worth of crude oil to India



SOURCES: INCRED RESEARCH, COMPANY REPORTS

Figure 4: In % terms, India's crude oil imports from Russia touched ~40% so far in FY24F but as Russia is insisting on payment in Chinese yuan, they are declining

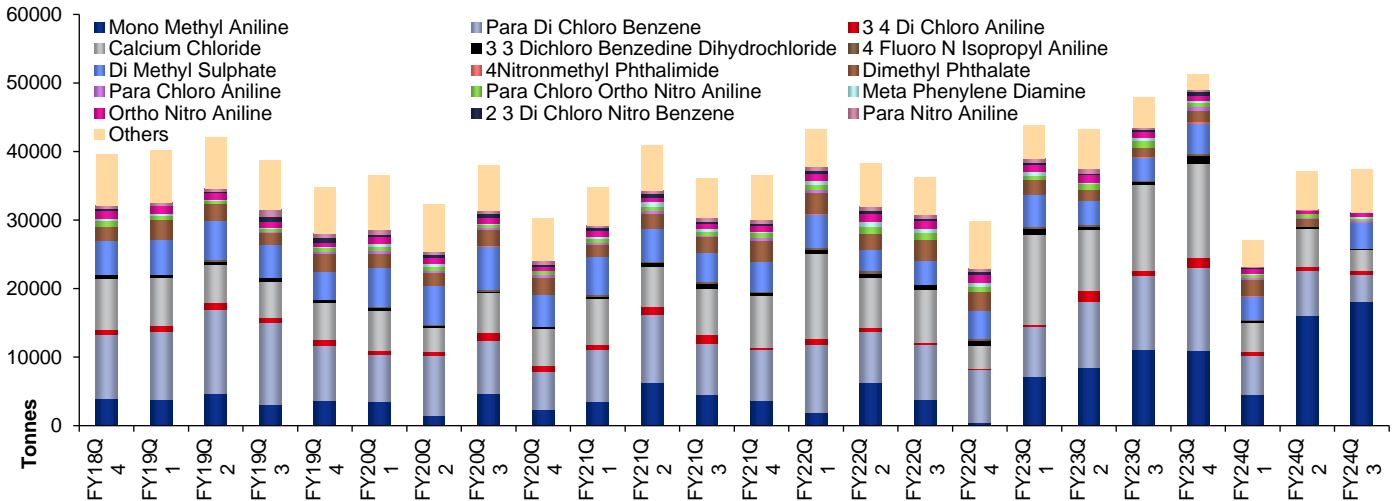


SOURCE: INCRED RESEARCH, COMPANY REPORTS

Led by MMA, the company's exports have recovered a bit in volume terms

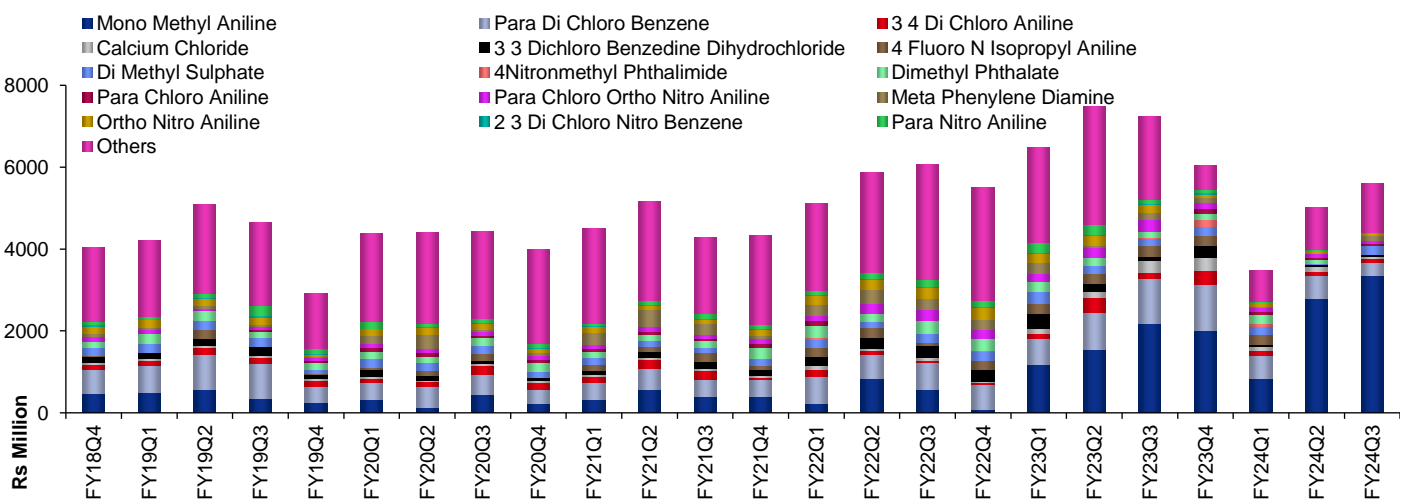
Following the large growth in MMA exports, there has been a marked increase in overall exports in the Q3FY24. Sustainability of MMA exports is always a question mark and the slowdown in domestic chemical sales is also true. We also know that the huge capacity of Aarti Industries is lying unused.

Figure 5: The increase in exports in volume terms is primarily driven by higher MMA exports; PDCB, which is the traditional biggest molecule for Aarti Industries, is still subdued



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 6: The value is also dominated by MMA exports, which are primarily driven by Russian demand

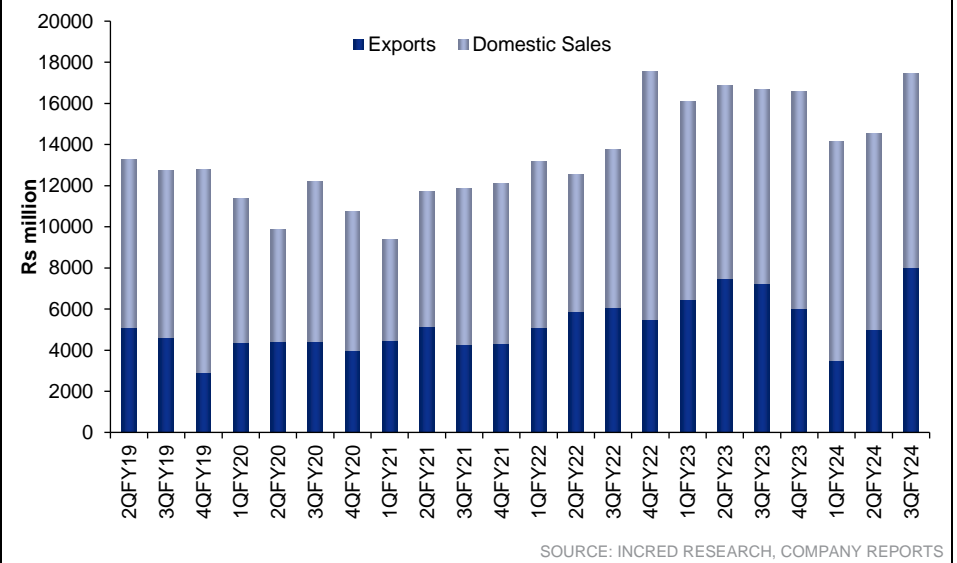


SOURCE: INCRED RESEARCH, COMPANY REPORTS

While there will be a YoY increase in exports, we don't expect a big recovery in domestic demand➤

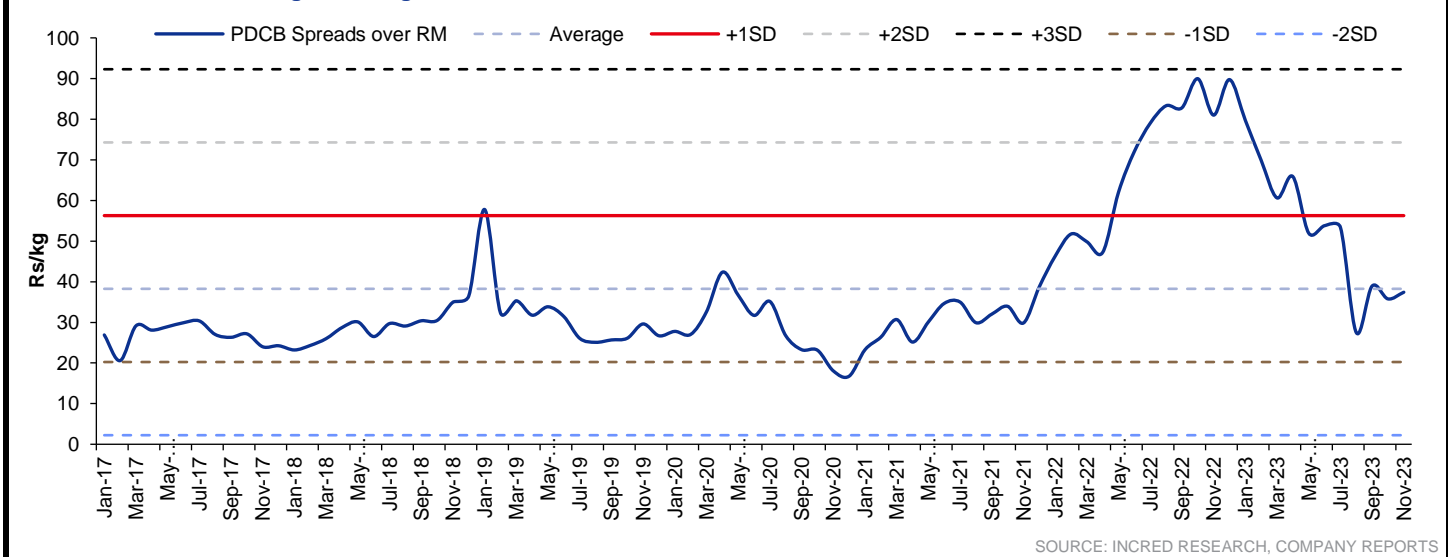
The slowdown in agrochemicals demand is hitting all chemical companies hard and Aarti Industries is no exception. We expect a YoY increase in exports in 3QFY24F, but we don't expect a big recovery in domestic sales.

Figure 7: Exports to grow in 3QFY24F to around Rs8bn, but the slowdown in domestic business to keep overall revenue at the same level



Decline in PDCB margin to sustain pressure on gross margin of the company➤

Figure 8: PDCB margin is at the same level QoQ, but declined significantly YoY; as PDCB is one of the main products, its margin decline will lead to lower gross margin YoY



Usage of PDCB also indicate that's a near-term recovery is unlikely➤

Mothballs: One of its most common uses is in mothballs, where it acts as a fumigant to repel moths and prevent damage to stored clothing and fabrics.

Insecticides: It's also used in insecticides to control pests like cockroaches, ants, and silverfish.

Deodorizers: PDCB is used in various deodorizing products, such as room deodorizers and toilet bowl fresheners, due to its ability to mask odours.

Chemical intermediate: It serves as a chemical intermediate in the production of other chemicals, including dyes, pharmaceuticals, and plastics.

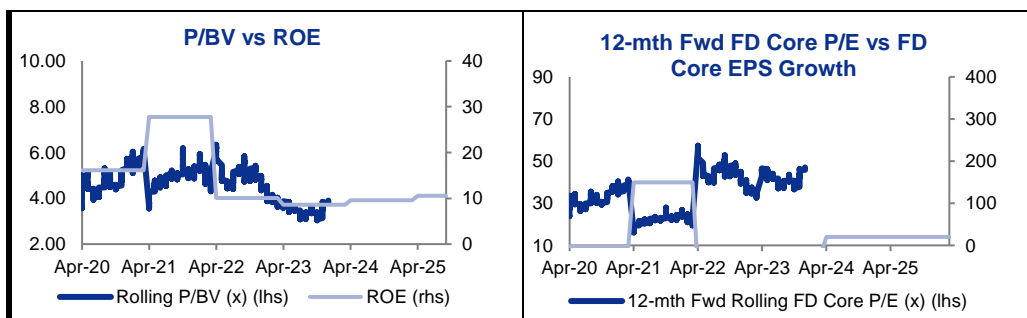
No big change in earnings trajectory- 3QFY24F can be good QoQ but flattish YoY

Figure 9: We expect 3QFY24F PAT to be at the same level as 3QFY23 PAT

	1QFY23	2QFY23	3QFY23	4QFY23	1QFY24	2QFY24	3QFY24F
Net Revenue	16,103	16,850	16,677	16,560	14,140	14,540	17,437
Expenses							
Total Cost of Goods Sold	9,262	9,781	9,757	9,620	8,530	8,540	10,462
Employee Benefit Expenses	910	928	927	1,090	1,010	990	990
Other Expenses	3,116	3,471	3,107	3,330	2,580	2,670	2,670
Total Expenses	13,288	14,180	13,790	14,040	12,120	12,200	14,122
EBITDA	2,815	2,670	2,887	2,520	2,020	2,340	3,315
Depreciation	718	729	821	840	890	930	930
EBIT	2,098	1,941	2,066	1,680	1,130	1,410	2,385
Other Income	4	0	3	0	0	0	
Interest Expenses	445	437	470	330	400	580	580
Exceptional Items							
Profit Before Tax	1,656	1,504	1,599	1,350	730	830	1,805
Current Tax	285	270	290	230	130	140	
Deferred Tax	75	40	44	-170	20	-90	
Other Tax Expenses	-60	-50	-100	-200	-110	-140	
Total Tax Expenses	301	259	234	-140	40	-90	451
Profit After Tax	1,355	1,245	1,365	1,490	690	920	1,354

SOURCE: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS



Profit & Loss

(Rs mn)	Mar-22A	Mar-23A	Mar-24F	Mar-25F	Mar-26F
Total Net Revenues	70,000	66,186	68,171	74,989	83,987
Gross Profit	37,061	27,769	29,314	32,995	36,954
Operating EBITDA	19,288	10,890	11,324	13,215	14,826
Depreciation And Amortisation	(2,885)	(3,105)	(4,097)	(4,397)	(4,607)
Operating EBIT	16,403	7,785	7,227	8,819	10,220
Financial Income/(Expense)	(1,143)	(1,683)	(2,025)	(2,581)	(2,736)
Pretax Income/(Loss) from Assoc.					
Non-Operating Income/(Expense)	8	9	9	9	9
Profit Before Tax (pre-EI)	15,268	6,111	5,211	6,246	7,492
Exceptional Items					
Pre-tax Profit	15,268	6,111	5,211	6,246	7,492
Taxation	(2,194)	(659)	(830)	(995)	(1,194)
Exceptional Income - post-tax					
Profit After Tax	13,074	5,452	4,381	5,250	6,298
Minority Interests					
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	13,074	5,452	4,381	5,250	6,298
Recurring Net Profit	13,074	5,452	4,381	5,250	6,298
Fully Diluted Recurring Net Profit	13,074	5,452	4,381	5,250	6,298

Cash Flow

(Rs mn)	Mar-22A	Mar-23A	Mar-24F	Mar-25F	Mar-26F
EBITDA	19,288	10,890	11,324	13,215	14,826
Cash Flow from Invt. & Assoc.					
Change In Working Capital	(11,858)	3,118	210	(1,949)	(2,572)
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense	(61)	(9)		646	
Other Operating Cashflow	(4,189)	(126)	372	599	357
Net Interest (Paid)/Received	(1,143)	(1,683)	(2,025)	(2,581)	(2,736)
Tax Paid	2,670	909	830	995	1,194
Cashflow From Operations	4,708	13,098	10,713	10,926	11,069
Capex	(13,050)	(13,263)	(15,000)	(15,000)	(4,000)
Disposals Of FAs/subsidiaries					
Acq. Of Subsidiaries/investments					
Other Investing Cashflow	(5)	(35)			
Cash Flow From Investing	(13,055)	(13,298)	(15,000)	(15,000)	(4,000)
Debt Raised/(repaid)	(2,663)		8,000	10,000	(5,000)
Proceeds From Issue Of Shares	11,867	3,061			
Shares Repurchased					
Dividends Paid	(1,269)	(906)	(906)	(906)	(906)
Preferred Dividends					
Other Financing Cashflow	(1,143)	(1,683)	(2,025)	(2,581)	(2,736)
Cash Flow From Financing	6,792	472	5,069	6,512	(8,642)
Total Cash Generated	(1,555)	272	781	2,438	(1,573)
Free Cashflow To Equity	(11,010)	(200)	3,712	5,926	2,069
Free Cashflow To Firm	(7,204)	1,483	(2,263)	(1,493)	9,805

SOURCE: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS...cont'd

Balance Sheet					
(Rs mn)	Mar-22A	Mar-23A	Mar-24F	Mar-25F	Mar-26F
Total Cash And Equivalents	2,568	2,007	521	2,960	1,621
Total Debtors	13,905	9,405	13,074	14,381	16,107
Inventories	14,113	10,311	11,206	12,327	13,806
Total Other Current Assets	2,150	2,870	2,147	2,158	2,173
Total Current Assets	32,737	24,593	26,949	31,826	33,707
Fixed Assets		58,182	72,333	82,937	82,330
Total Investments	731	172	172	172	172
Intangible Assets					
Total Other Non-Current Assets	4,177	2,863	1,861	1,215	980
Total Non-current Assets		61,216	74,366	84,324	83,482
Short-term Debt	12,872	22,393	22,393	22,393	22,393
Current Portion of Long-Term Debt					
Total Creditors	4,901	3,075	3,922	4,314	4,832
Other Current Liabilities	5,597	2,365	5,570	5,668	5,798
Total Current Liabilities	23,370	27,833	31,886	32,376	33,023
Total Long-term Debt	9,304	6,347	14,347	24,347	19,347
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	2,400	2,421	2,400	2,400	2,400
Total Non-current Liabilities	11,704	8,768	16,747	26,747	21,747
Total Provisions	2,502				
Total Liabilities	37,576	36,601	48,633	59,123	54,771
Shareholders Equity	59,145	49,201	52,675	57,019	62,411
Minority Interests	7	7	7	7	7
Total Equity	59,152	49,208	52,682	57,026	62,418

Key Ratios					
	Mar-22A	Mar-23A	Mar-24F	Mar-25F	Mar-26F
Revenue Growth	39.4%	(5.4%)	3.0%	10.0%	12.0%
Operating EBITDA Growth	96.5%	(43.5%)	4.0%	16.7%	12.2%
Operating EBITDA Margin	27.6%	16.5%	16.6%	17.6%	17.7%
Net Cash Per Share (Rs)	(54.09)	(73.75)	(99.91)	(120.77)	(110.67)
BVPS (Rs)	163.16	135.72	145.31	157.29	172.17
Gross Interest Cover	14.35	4.63	3.57	3.42	3.74
Effective Tax Rate	14.4%	10.8%	15.9%	15.9%	15.9%
Net Dividend Payout Ratio	9.7%	16.6%	20.7%	17.3%	14.4%
Accounts Receivables Days	56.95	64.27	60.18	66.82	66.25
Inventory Days	130.04	116.03	101.06	102.27	101.40
Accounts Payables Days	(59.09)	(37.89)	(32.87)	(35.80)	(35.49)
ROIC (%)		10.0%	7.9%	8.6%	9.8%
ROCE (%)	22.4%	9.6%	8.6%	9.1%	9.8%
Return On Average Assets			6.8%	7.2%	7.7%

SOURCE: INCRED RESEARCH, COMPANY REPORTS

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	Analyst/ Relative	Entity/ Associates
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any other material conflict of interest at the time of publication of the research report or at the time of public appearance	NO	NO
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managed or co-managed public offering of securities for the subject company in the last twelve months	NO	NO
received any compensation or other benefits from the subject company or third party in connection with the research report	NO	NO
served as an officer, director or employee of the subject company	NO	NO
been engaged in market making activity for the subject company	NO	NO

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