

India

REDUCE (no change)

Consensus ratings*: Buy 5 Hold 2 Sell 2

Current price:	Rs8,850
Target price:	Rs6,370
Previous target:	Rs6,370
Up/downside:	-28.0%
InCred Research / Consensus:	-22.7%
Reuters:	ATLP.NS
Bloomberg:	ATLP IN
Market cap:	US\$3,583m Rs261,845m
Average daily turnover:	US\$3.7m Rs267.4m
Current shares o/s:	29.6m
Free float:	55.2%

*Source: Bloomberg



Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	6.3	31.4	96.1
Relative (%)	(1.2)	27.2	26.2

Major shareholders	% held
Promoter & Promoter Group	44.8
HDFC Trustee Company Ltd	6.5
DSP Midcap Fund	5.2

Analyst(s)


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Atul Ltd

Gross margins likely to come under pressure

- With most of the product price spread over raw materials under pressure, we expect the gross margin to decline in the coming quarters.
- Bloomberg consensus estimates for PAT and revenue are likely to have negative surprises in the coming quarters, in our view.
- We maintain our non-consensus Reduce rating on the stock. We value Atul at 25x FY23F EPS to arrive at our TP of Rs6,370.

Consensus PAT estimates too high, disappointment likely

Consensus estimates for PAT are too high, and disappointment is likely in the near to medium term, in our view. While Bloomberg consensus estimates gross margins of 54.3% in FY22F and 54.4% in FY23F (vs 52.8% for 4QFY21), we estimate that the gross margins for FY22F/23F are likely to be near 50%. In FY21, owing to a supply chain shortages-led price rise, Atul's gross margin touched a 12-year high of 54.6%. However, with supply normalising prices are falling and consequently gross margins to decline (as we saw in 4QFY21). We estimate the company's gross profit margin will fall by 400bp from FY22F, and consequently our estimates for FY22F/FY23F PAT are 15% below Bloomberg consensus'.

Raw material costs are rising, gross margins to fall

ECH (epichlorohydrin), BIS Phenol-A (BPA) and phenol are the most important raw materials for Atul. Atul imports almost all its ECH and BPA requirements. ECH is manufactured using propylene, while benzene is BPA and phenol's base raw material. The prices of crude oil, the basic ingredient for all three chemicals, rose by 50% on average over CY20. Consequently, in the first couple of months of 1QFY22, BPA prices rose by 45% and ECH by 15% over the 4QFY21 average import price (Source: Corpiness Global Private Limited, an exports data provider). At the same time, apart from Cresols, all other product prices are stagnant or declining. The textile sector slowdown is hitting Atul as prices, and hence, gross profit for the VAT and NOVATIC series of dyes are declining. Anisic aldehyde, an important product for Atul (10-12% of sales), is also witnessing margin pressures after a brief recovery in Apr 2021. On an overall basis, we expect Atul's gross margin to decline sequentially in 1QFY22F.

Valuation and risks

We value Atul at 25x FY23F EPS, which is +1SD of long-term mean P/E and at a 15% discount to its peers, to arrive at our target price of Rs6,370. Our PAT estimates are 15% below Bloomberg consensus estimates (FY22F/23F) and, hence, we believe an EPS disappointment is likely. Key risks: Any sudden correction in raw materials will maintain gross margins, hence, EPS could be higher than our estimate. Despite poor earnings growth, the stock could continue to re-rate if global liquidity persists.

Financial Summary

	Mar-20A	Mar-21A	Mar-22F	Mar-23F	Mar-24F
Revenue (Rsm)	40,931	37,315	45,524	50,987	57,105
Operating EBITDA (Rsm)	9,020	9,171	10,070	11,557	13,432
Net Profit (Rsm)	6,659	6,528	6,476	7,564	8,975
Core EPS (Rs)	224.4	220.3	218.2	254.8	302.4
Core EPS Growth	54.5%	(1.8%)	6.1%	16.8%	18.7%
FD Core P/E (x)	39.44	40.18	40.56	34.73	29.27
DPS (Rs)	27.5	26.5	26.2	30.6	36.3
Dividend Yield	0.31%	0.30%	0.30%	0.35%	0.41%
EV/EBITDA (x)	27.93	26.88	24.16	20.57	17.20
P/FCFE (x)	175.79	292.19	53.21	39.12	32.35
Net Gearing	(17.7%)	(25.6%)	(33.5%)	(40.3%)	(46.7%)
P/BV (x)	8.25	6.84	6.16	5.35	4.63
ROE	22.5%	18.6%	16.3%	16.5%	17.0%
% Change In Core EPS Estimates					
InCred Research/Consensus EPS (x)			0.86	0.87	0.00

SOURCES: INCRED RESEARCH ESTIMATES, COMPANY REPORTS. PRICED AS AT 11 JUN 2021

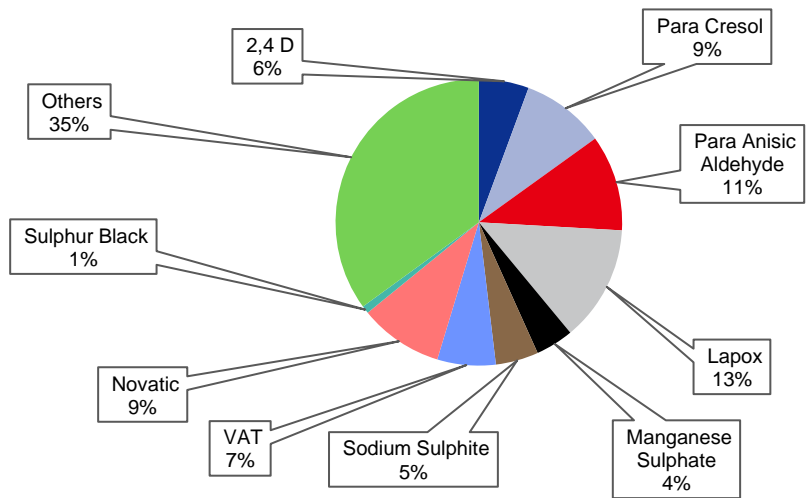
Gross margins likely to come under pressure

Most of Atul's product margins are under pressure

Our analysis of Atul's product portfolio indicates that the top eight of its products formed about two-thirds of its overall sales as at FY21 and are facing margin pressures.

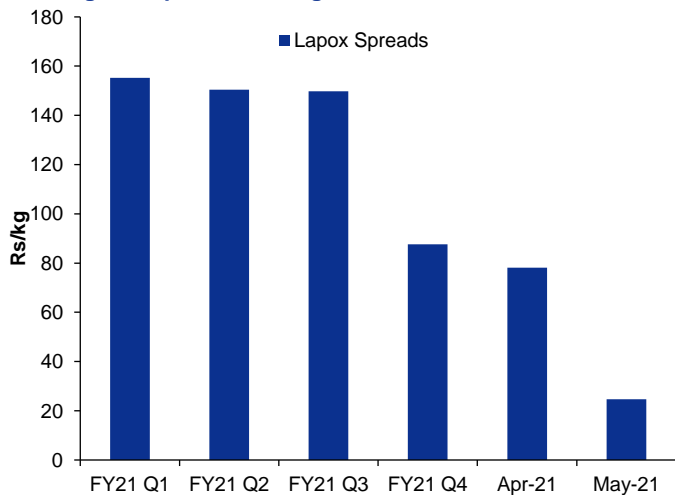
Product spread analysis of 8 principal products that form the bulk of Atul's sales is given below ➤

Figure 1: Top 8 products formed ~2/3rd of exports in FY20. We estimate they will form ~2/3 of overall sales in FY21F as well



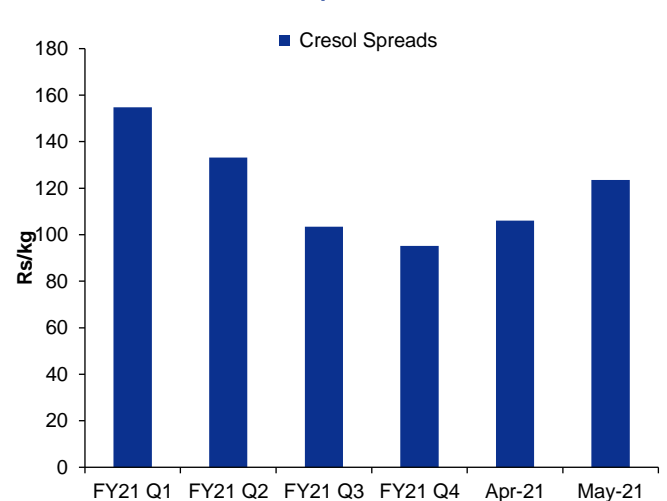
SOURCES: INCRED RESEARCH, CORPINESS GLOBAL PRIVATE LIMITED

Figure 2: Atul sells epoxy resins under the brand name Lapox, whose gross spread is falling



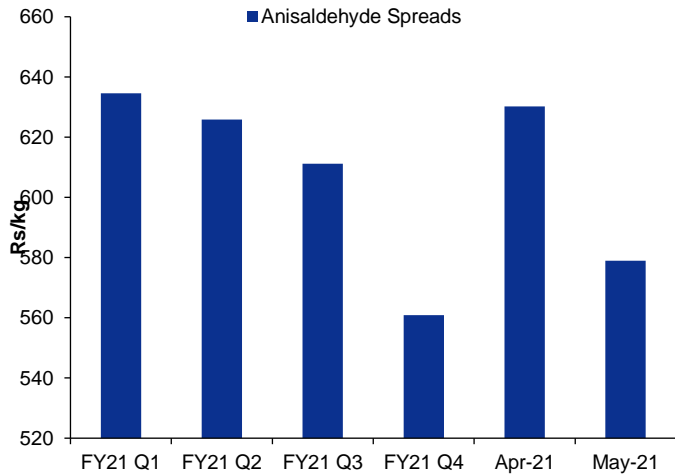
SOURCES: INCRED RESEARCH, CORPINESS GLOBAL PRIVATE LIMITED

Figure 3: Cresol (para and ortho cresol) spreads rose in May 2021 vis-à-vis 4QFY21 and Apr 2021



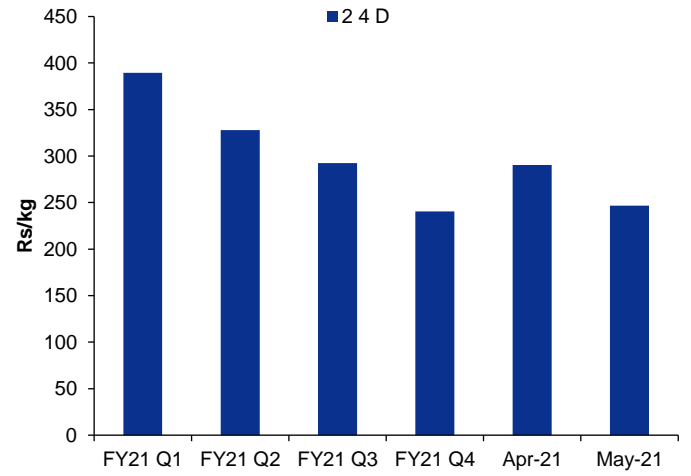
SOURCES: INCRED RESEARCH, CORPINESS GLOBAL PRIVATE LIMITED

Figure 4: After recovery in the month of Apr, anisaldehyde spreads over raw materials declined in May



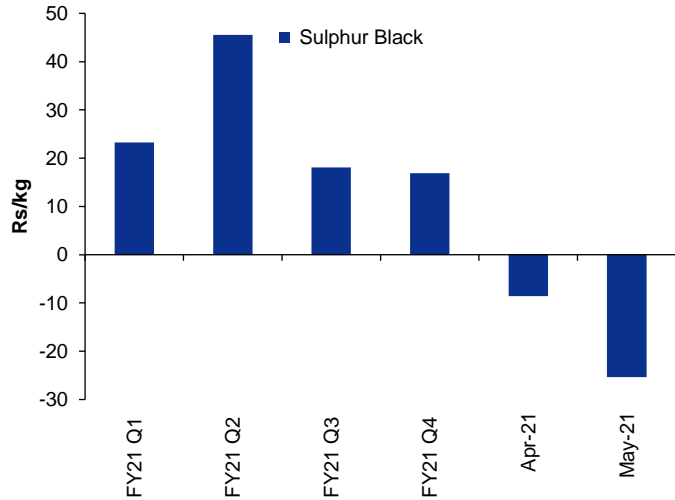
SOURCES: INCRED RESEARCH, CORPINESS GLOBAL PRIVATE LIMITED

Figure 5: 2,4 D is an old herbicide and its prices are under pressure, which shows in declining product spreads



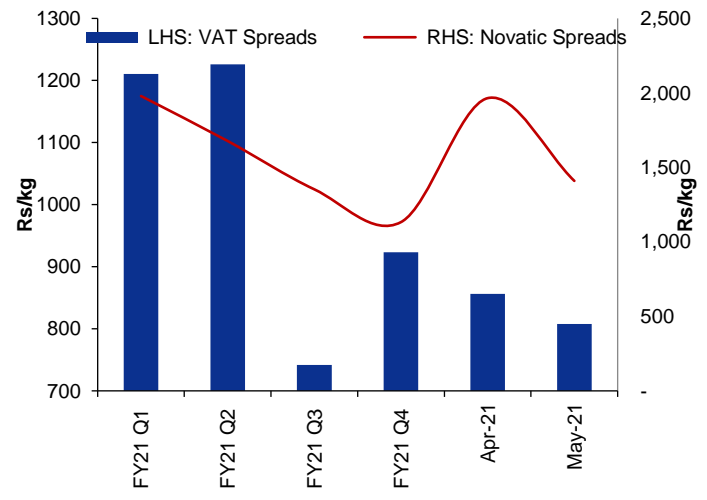
SOURCES: INCRED RESEARCH, CORPINESS GLOBAL PRIVATE LIMITED

Figure 6: Sulphur black (~1-2% of sales) saw its steepest decline in the past couple of months



SOURCES: INCRED RESEARCH, CORPINESS GLOBAL PRIVATE LIMITED

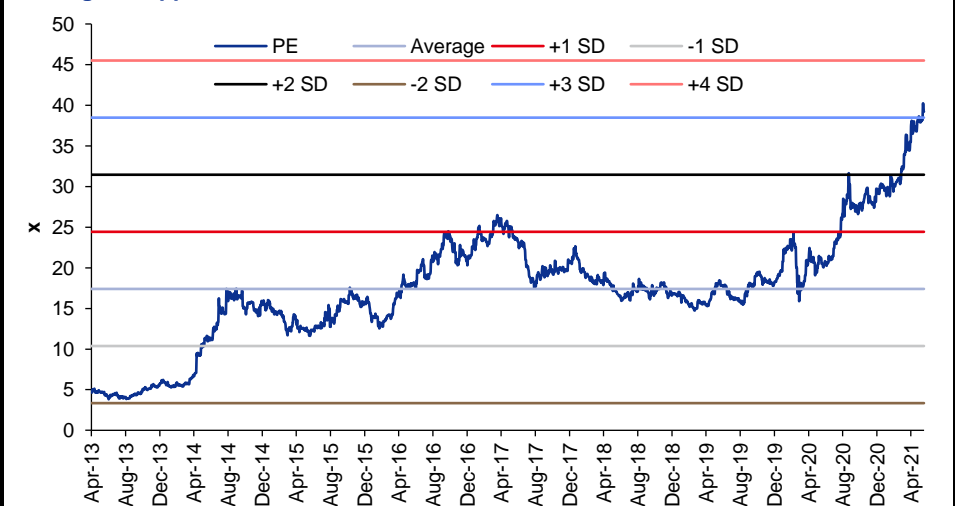
Figure 7: Textile sector pressure is apparent in falling gross margin of dyes



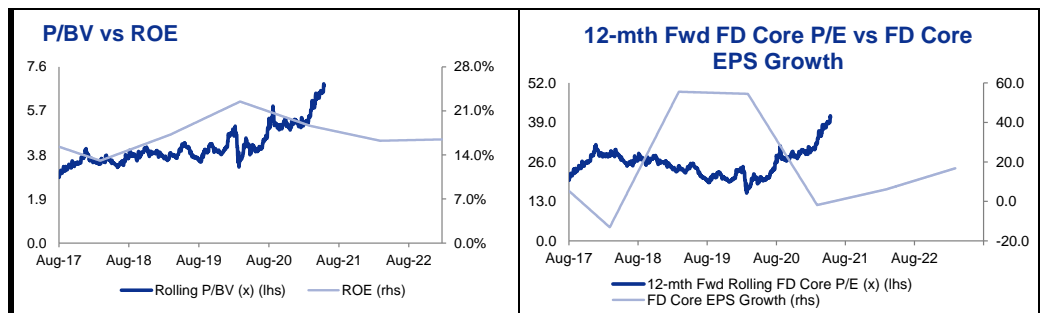
SOURCES: INCRED RESEARCH, CORPINESS GLOBAL PRIVATE LIMITED

At +3SD of long-term mean, Atul's valuation leaves no room for disappointment ➤

Figure 8: Atul Ltd is trading at +3SD of the long-term mean, which leaves no room for earnings disappointment



SOURCES: INCRED RESEARCH, COMPANY REPORTS, BLOOMBERG

BY THE NUMBERS

Profit & Loss

(Rs mn)	Mar-20A	Mar-21A	Mar-22F	Mar-23F	Mar-24F
Total Net Revenues	40,931	37,315	45,524	50,987	57,105
Gross Profit	21,230	20,363	22,762	25,748	29,124
Operating EBITDA	9,020	9,171	10,070	11,557	13,432
Depreciation And Amortisation	(1,302)	(1,363)	(1,551)	(1,679)	(1,806)
Operating EBIT	7,718	7,808	8,519	9,878	11,626
Financial Income/(Expense)	(94)	(94)	(94)	(94)	(94)
Pretax Income/(Loss) from Assoc.					
Non-Operating Income/(Expense)	780	1,030	633	822	1,067
Profit Before Tax (pre-EI)	8,404	8,744	8,658	10,112	11,998
Exceptional Items					
Pre-tax Profit	8,404	8,744	8,658	10,112	11,998
Taxation	(1,745)	(2,217)	(2,182)	(2,548)	(3,023)
Exceptional Income - post-tax					
Profit After Tax	6,659	6,528	6,476	7,564	8,975
Minority Interests					
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	6,659	6,528	6,476	7,564	8,975
Recurring Net Profit	6,659	6,528	6,476	7,564	8,975
Fully Diluted Recurring Net Profit	6,659	6,528	6,476	7,564	8,975

Cash Flow

(Rs mn)	Mar-20A	Mar-21A	Mar-22F	Mar-23F	Mar-24F
EBITDA	9,020	9,171	10,070	11,557	13,432
Cash Flow from Invt. & Assoc.					
Change In Working Capital	1,618	(245)	(2,012)	(1,159)	(1,298)
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense	(486)	(826)			
Other Operating Cashflow	924	1,196	726	915	1,160
Net Interest (Paid)/Received	(94)	(94)	(94)	(94)	(94)
Tax Paid	(2,168)	(2,023)	(2,182)	(2,548)	(3,023)
Cashflow From Operations	8,814	7,180	6,437	8,215	9,619
Capex	(3,740)	(3,225)	(2,684)	(1,500)	(1,500)
Disposals Of FAs/subsidiaries	6	10			
Acq. Of Subsidiaries/investments	(4,365)	(3,958)			
Other Investing Cashflow	243	709			
Cash Flow From Investing	(7,857)	(6,464)	(2,684)	(1,500)	(1,500)
Debt Raised/(repaid)	537	182			
Proceeds From Issue Of Shares		(617)	1		
Shares Repurchased					
Dividends Paid	(1,504)		(932)	(1,089)	(1,292)
Preferred Dividends					
Other Financing Cashflow	(109)	(87)	(94)	(94)	(94)
Cash Flow From Financing	(1,076)	(522)	(1,026)	(1,183)	(1,386)
Total Cash Generated	(119)	194	3,910	5,532	6,733
Free Cashflow To Equity	1,494	898	4,937	6,715	8,119
Free Cashflow To Firm	1,051	809	5,031	6,809	8,213

SOURCES: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS...cont'd

Balance Sheet					
(Rs mn)	Mar-20A	Mar-21A	Mar-22F	Mar-23F	Mar-24F
Total Cash And Equivalents	6,871	10,885	15,553	21,086	27,818
Total Debtors	7,197	7,332	8,731	9,778	10,952
Inventories	5,034	5,941	6,236	6,984	7,823
Total Other Current Assets	2,008	1,482	1,482	1,482	1,482
Total Current Assets	21,110	25,641	32,309	39,579	48,257
Fixed Assets	14,824	13,777	14,910	14,731	14,425
Total Investments	4,671	5,964	4,671	4,671	4,671
Intangible Assets	291	291	291	291	291
Total Other Non-Current Assets	900	843	843	843	843
Total Non-current Assets	20,687	20,875	20,715	20,536	20,230
Short-term Debt	104	35	35	35	35
Current Portion of Long-Term Debt					
Total Creditors	4,776	5,631	5,312	5,950	6,664
Other Current Liabilities	1,763	2,395	2,395	2,395	2,395
Total Current Liabilities	6,643	8,061	7,742	8,380	9,094
Total Long-term Debt	1,096	982	982	982	982
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	605	153	153	153	153
Total Non-current Liabilities	1,701	1,135	1,135	1,135	1,135
Total Provisions	1,348	1,604	1,604	1,604	1,604
Total Liabilities	9,692	10,801	10,482	11,119	11,833
Shareholders Equity	31,840	38,265	42,607	49,081	56,762
Minority Interests	264	306	264	264	264
Total Equity	32,104	38,572	42,870	49,344	57,026

Key Ratios					
	Mar-20A	Mar-21A	Mar-22F	Mar-23F	Mar-24F
Revenue Growth	1.4%	(8.8%)	22.0%	12.0%	12.0%
Operating EBITDA Growth	17.6%	1.7%	9.8%	14.8%	16.2%
Operating EBITDA Margin	22.0%	24.6%	22.1%	22.7%	23.5%
Net Cash Per Share (Rs)	191.07	333.48	483.60	670.01	896.84
BVPS (Rs)	1,072.79	1,293.18	1,435.54	1,653.66	1,912.47
Gross Interest Cover	82.11	83.51	90.63	105.09	123.68
Effective Tax Rate	20.8%	25.3%	25.2%	25.2%	25.2%
Net Dividend Payout Ratio	12.3%	12.0%	12.0%	12.0%	12.0%
Accounts Receivables Days	63.23	71.06	64.39	66.25	66.25
Inventory Days	94.05	118.15	97.64	95.60	96.57
Accounts Payables Days	79.42	112.05	87.74	81.44	82.27
ROIC (%)	27.4%	22.9%	25.1%	27.2%	30.8%
ROCE (%)	24.1%	20.7%	19.1%	19.4%	19.9%
Return On Average Assets	17.4%	14.9%	13.1%	13.5%	14.1%

SOURCES: INCRED RESEARCH, COMPANY REPORTS

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Definition:

- Add** The stock's total return is expected to exceed 10% over the next 12 months.
- Hold** The stock's total return is expected to be between 0% and positive 10% over the next 12 months.
- Reduce** The stock's total return is expected to fall below 0% or more over the next 12 months.

The total expected return of a stock is defined as the sum of the: (i) percentage difference between the target price and the current price and (ii) the forward net dividend yields of the stock. Stock price targets have an investment horizon of 12 months.

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Definition:

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- Neutral** A Neutral rating means stocks in the sector have, on a market cap-weighted basis, a neutral absolute recommendation.
- Underweight** An Underweight rating means stocks in the sector have, on a market cap-weighted basis, a negative absolute recommendation.

Country Ratings

Definition:

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