

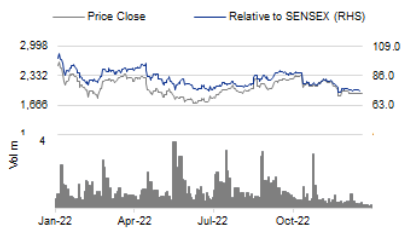
India

REDUCE (no change)

Consensus ratings*: Buy 10 Hold 2 Sell 3

Current price:	Rs1,925
Target price:	Rs1,460
Previous target:	Rs1,745
Up/downside:	-24.2%
InCred Research / Consensus:	-34.3%
Reuters:	DPNT.NS
Bloomberg:	DN IN
Market cap:	US\$3,228m
	Rs262,618m
Average daily turnover:	US\$18.6m
	Rs1514.3m
Current shares o/s:	136.4m
Free float:	54.3%

*Source: Bloomberg



Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	(7.8)	(14.3)	(27.4)
Relative (%)	(6.5)	(16.7)	(29.0)

Major shareholders	% held
Promoter & Promoter Group	45.7
Nippon Life India Ltd	3.3
Franklin India Smaller Companies Fund	3.2

Deepak Nitrite Ltd

Analyzing its probable polycarbonate project

- Our analysis of the global polycarbonate market and its spreads over bisphenol-A indicate that in an average case scenario, a 0.2mt capacity plant can make Rs12bn in gross profit.
- Please note that Deepak Nitrite (DNL) has not yet finalized this project, but currently DNL is evaluating it. (Source: DNL's post-results conference call).
- Polycarbonate market is heavily oversupplied and currently the industry's capacity utilization is ~70% with multiple capex (globally) in the pipeline. This project (if it fructifies) will increase the commodity chemicals nature of DNL.

Deepak Nitrite is contemplating setting up a polycarbonate plant

We quote from Deepak Nitrite's management commentary during the 1QFY23 results conference call: "Polycarbonate will again be a total downstream what we are talking. That has been our strategy, and we have been discussing this for quite some time. So, phenol downstream going up to polycarbonate, this is how we will grow. So, then obviously all these things will require around Rs6,500 crore to Rs7,000 crore based on current estimation." The capex part of the polycarbonate plant is still not clear and we believe that Rs60-70bn is the overall capex. However, going by the global standards, a 0.2mt plant can cost around US\$250m.

Polycarbonate is an oversupplied commodity

Global demand for polycarbonate is around 5mt whereas the global capacity is ~7.2mt and further capacity expansion is in the pipeline. With 75% of the demand for polycarbonate coming from consumer appliances, automotive and electronics sectors, polycarbonate is highly linked to the global demand cycle. In CY20, global demand for polycarbonate declined by 10%. We believe that CY22 demand was ~5mt. Global polycarbonate demand CAGR has been ~3% (over CY11-CY22).

Polycarbonate will only increase earnings volatility of Deepak Nitrite

The spreads of polycarbonate over bisphenol-A are highly volatile. Based on the average spreads of the last six years, a 0.2mt plant can add Rs12bn to gross profit. However, please note that even a 1SD variation can lead gross profit to be in the Rs24bn to Rs4bn range. At -1 SD plant won't make any EBITDA. Setting up a polycarbonate plant will only increase the commodity nature of Deepak Nitrite's business and hence, it will get a lower multiple.

Consensus EPS estimates too high and need a huge cut; REDUCE

Consensus EPS estimates of Deepak Nitrite are too high. FY23F, FY24F and FY25F EPS estimates need to be cut by 20%, 30% and 30%, respectively. The stock trades at a lofty valuation. We retain our REDUCE rating on it with a lower target price of Rs1,460 (Rs1,745 earlier). We have valued the stock at 20x FY25F EPS. Upside risk: Higher-than-estimated phenol spreads can lead to a higher price for the stock.

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Financial Summary

	Mar-21A	Mar-22A	Mar-23F	Mar-24F	Mar-25F
Revenue (Rsm)	43,598	68,022	75,595	81,010	92,170
Operating EBITDA (Rsm)	12,470	16,036	12,799	13,796	15,478
Net Profit (Rsm)	7,758	10,666	8,097	8,823	9,946
Core EPS (Rs)	56.9	78.2	59.4	64.7	72.9
Core EPS Growth	27.0%	37.5%	(24.1%)	9.0%	12.7%
FD Core P/E (x)	33.85	24.62	32.44	29.77	26.41
DPS (Rs)	5.5	7.0	4.9	4.9	4.9
Dividend Yield	0.34%	0.44%	0.30%	0.30%	0.30%
EV/EBITDA (x)	21.30	16.27	20.55	19.03	16.91
P/FCFE (x)	323.48	221.41	187.26	298.29	155.90
Net Gearing	13.1%	(5.3%)	0.9%	(0.3%)	(1.5%)
P/BV (x)	11.19	7.87	6.46	5.39	4.54
ROE	39.6%	37.5%	21.9%	19.7%	18.7%
% Change In Core EPS Estimates			(18.78%)	(14.56%)	
InCred Research/Consensus EPS (x)					

SOURCE: INCRED RESEARCH, COMPANY REPORTS

Analyzing its probable polycarbonate project

In our earlier report of Jan 2022, we had analysed all the expansion projects of Deepak Nitrite. Please click the link for this report: [IN: Deepak Nitrite Ltd - Deep dive into company's expansion project \(REDUCE - Maintained\)](#). We had highlighted in the report that the best-case EPS for the company when all expansions come on stream will be around Rs120. However, in the recent past the company had indicated that it is also considering the polycarbonate project on which street has become quite bullish. Our report did not analyse the company's probable project (probable because it's still in the planning stage) in detail.

Polycarbonate is a normal commodity

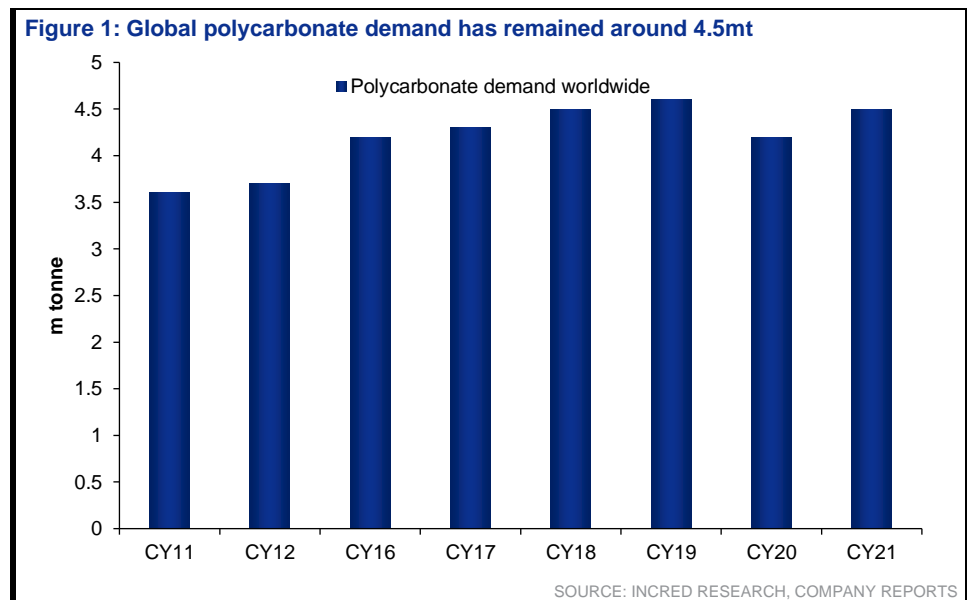
What is polycarbonate? >

Polycarbonate refers to a group of thermoplastic polymers containing carbonate groups in their chemical structures. Polycarbonate that is used in engineering is a strong, tough material and some grades are optically transparent. It can be easily worked upon, moulded, and thermoformed. Because of these properties, polycarbonate finds many applications.

How is polycarbonate produced? >

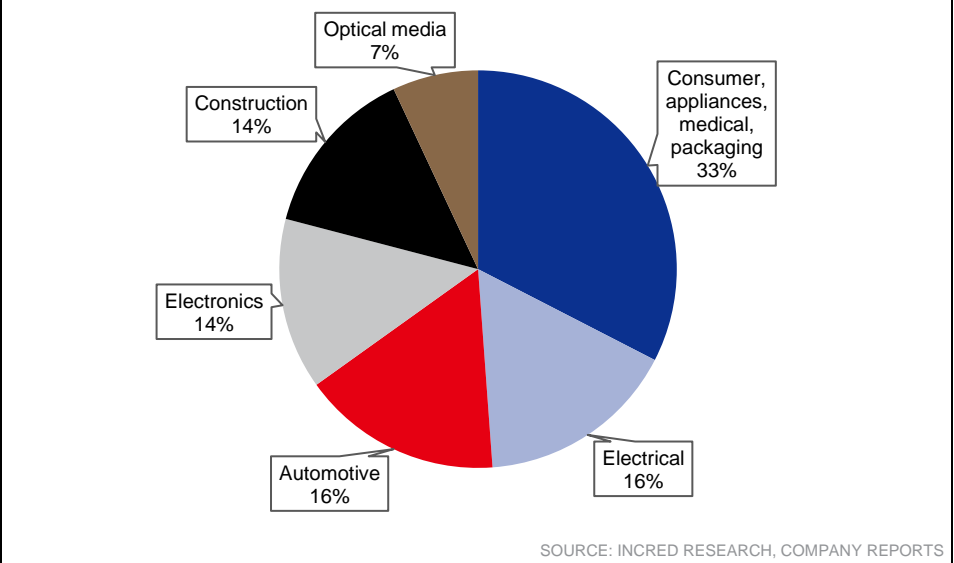
Most of the polycarbonate is produced through the reaction of bisphenol-A with phosgene gas. Please note that Deepak Nitrite is setting up a bisphenol-A plant and India is an importer of polycarbonate to the extent of ~150kt and hence, it's natural that the company is thinking of setting up a polycarbonate plant.

Global polycarbonate demand has been around 4.5mt >



Polycarbonate is primarily used in consumer applications ➤

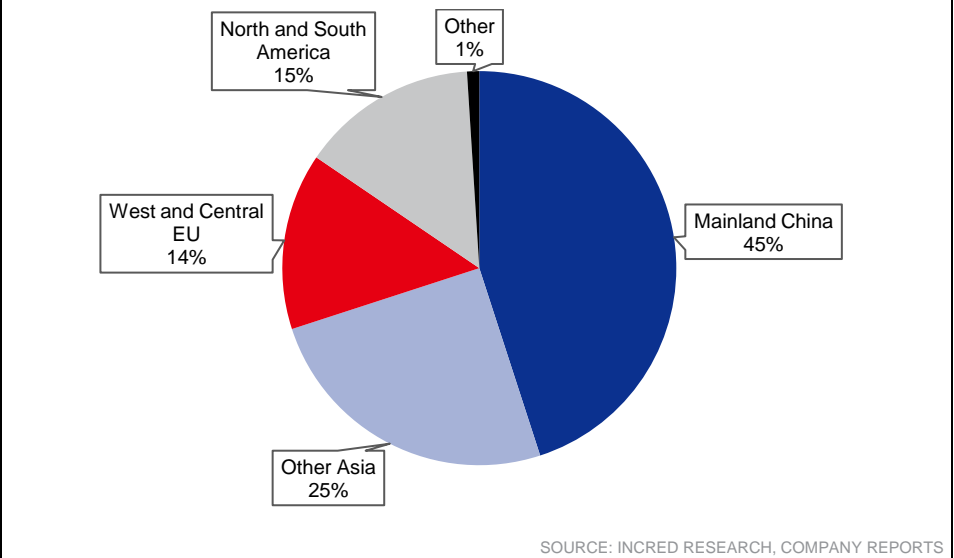
Figure 2: Consumer sector is one the major users of polycarbonate



SABIC, Covestro and Mitsubishi are the main players in global polycarbonate market; geography-wise, China dominates ➤

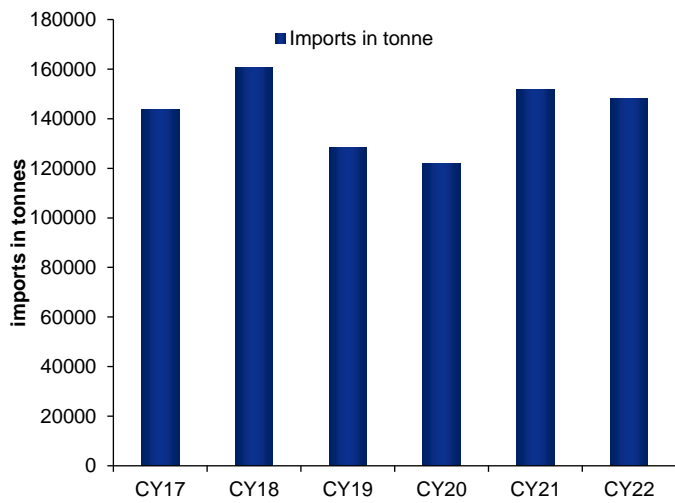
SABIC, Covestro and Mitsubishi are the main players in the global market. Given that phenol is the principal input material, which is manufactured from benzene and propylene, it's not surprising that SABIC is one of the major players with ~1.5mt capacity.

Figure 3: China accounts for 45% of global polycarbonate capacity; all global majors have their presence in China



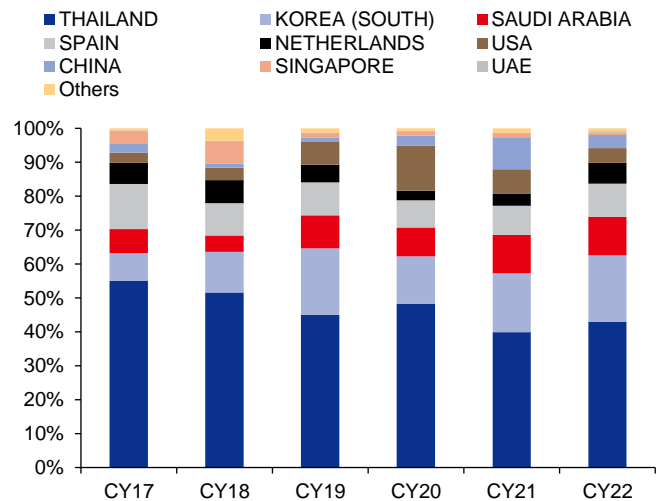
India has been a big importer of polycarbonate from Thailand and South Korea

Figure 4: India's polycarbonate imports have been around 0.15mt over the last six years



SOURCES: INCRED RESEARCH, COMPANY REPORTS

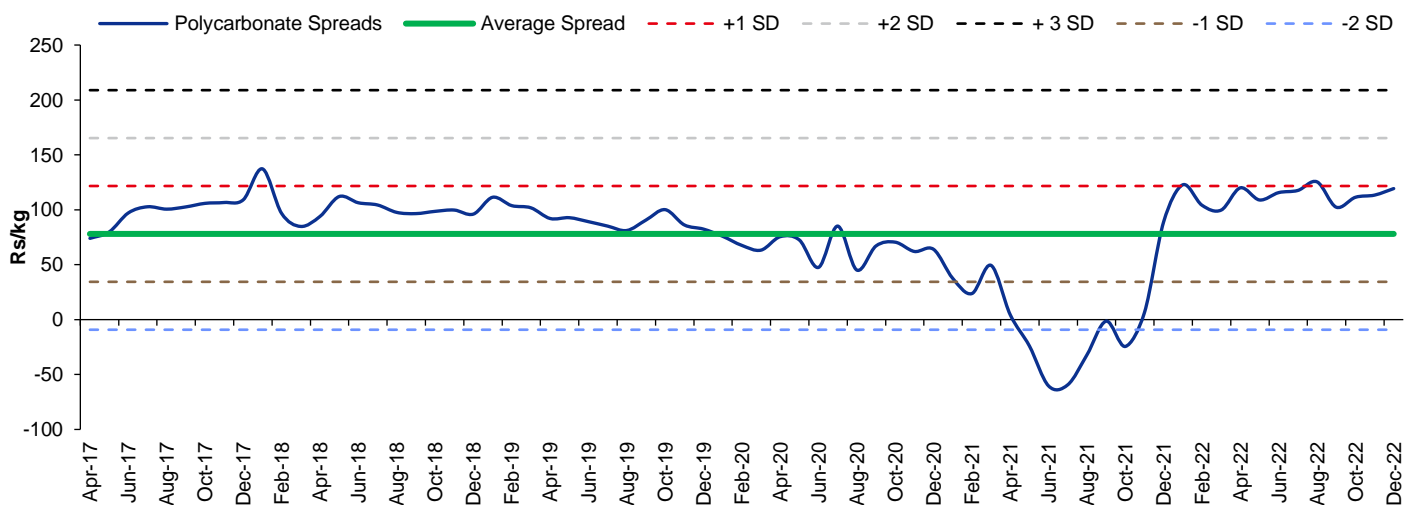
Figure 5: Thailand and Korea are the major polycarbonate exporters to India



SOURCES: INCRED RESEARCH, COMPANY REPORTS

Polycarbonate spreads over bisphenol-A are highly volatile

Figure 6: Average polycarbonate spreads over bisphenol-A have been around Rs78/kg for the last six years

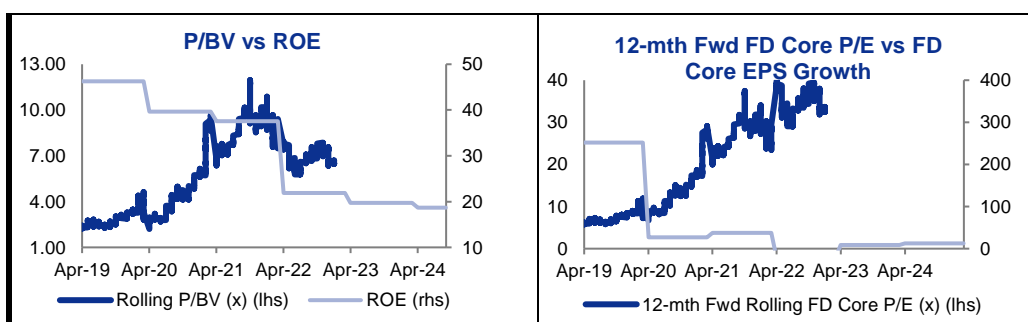


SOURCE: INCRED RESEARCH, COMPANY REPORTS

Adjusted for phosgene cost, a 0.2mt plant at full capacity can make Rs12bn in gross profit

Adjusted for phosgene and other raw material cost, a 0.2mt plant can make Rs12 bn in gross profit. However, the standard deviation in gross profit is quite high, and it can range from Rs24bn to Rs4bn.

BY THE NUMBERS



Profit & Loss

(Rs mn)	Mar-21A	Mar-22A	Mar-23F	Mar-24F	Mar-25F
Total Net Revenues	43,598	68,022	75,595	81,010	92,170
Gross Profit	20,955	26,878	22,679	24,303	27,651
Operating EBITDA	12,470	16,036	12,799	13,796	15,478
Depreciation And Amortisation	(1,526)	(1,777)	(1,790)	(1,896)	(2,038)
Operating EBIT	10,944	14,259	11,009	11,900	13,440
Financial Income/(Expense)	(742)	(340)	(399)	(319)	(359)
Pretax Income/(Loss) from Assoc.					
Non-Operating Income/(Expense)	215	426	215	215	215
Profit Before Tax (pre-EI)	10,417	14,345	10,825	11,796	13,297
Exceptional Items					
Pre-tax Profit	10,417	14,345	10,825	11,796	13,297
Taxation	(2,659)	(3,678)	(2,728)	(2,973)	(3,351)
Exceptional Income - post-tax					
Profit After Tax	7,758	10,666	8,097	8,823	9,946
Minority Interests					
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	7,758	10,666	8,097	8,823	9,946
Recurring Net Profit	7,758	10,666	8,097	8,823	9,946
Fully Diluted Recurring Net Profit	7,758	10,666	8,097	8,823	9,946

Cash Flow

(Rs mn)	Mar-21A	Mar-22A	Mar-23F	Mar-24F	Mar-25F
EBITDA	12,470	16,036	12,799	13,796	15,478
Cash Flow from Invt. & Assoc.					
Change In Working Capital	(441)	(11,712)	(1,146)	(943)	(1,943)
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense	111	(89)			
Other Operating Cashflow	957	810	399	319	359
Net Interest (Paid)/Received	(742)	(340)	(399)	(319)	(359)
Tax Paid	(2,365)	3,535	(2,728)	(2,973)	(3,351)
Cashflow From Operations	9,990	8,238	8,925	9,880	10,184
Capex	(2,096)	(1,868)	(9,500)	(8,500)	(8,500)
Disposals Of FAs/subsidiaries	10	7			
Acq. Of Subsidiaries/investments	(1,854)	(2,401)			
Other Investing Cashflow	(21)	22			
Cash Flow From Investing	(3,962)	(4,241)	(9,500)	(8,500)	(8,500)
Debt Raised/(repaid)	(5,217)	(2,812)	1,977	(500)	
Proceeds From Issue Of Shares					
Shares Repurchased					
Dividends Paid	(4)	(750)	(800)	(800)	(800)
Preferred Dividends					
Other Financing Cashflow	(741)	(296)			
Cash Flow From Financing	(5,961)	(3,858)	1,177	(1,300)	(800)
Total Cash Generated	68	140	603	80	885
Free Cashflow To Equity	812	1,186	1,403	880	1,685
Free Cashflow To Firm	6,771	4,338	(176)	1,699	2,043

SOURCE: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS...cont'd

Balance Sheet					
(Rs mn)	Mar-21A	Mar-22A	Mar-23F	Mar-24F	Mar-25F
Total Cash And Equivalents	2,202	4,786	4,635	4,611	5,352
Total Debtors	7,563	11,291	12,427	13,317	15,151
Inventories	3,827	5,846	7,249	7,768	8,838
Total Other Current Assets	1,175	1,183	1,183	1,183	1,183
Total Current Assets	14,767	23,105	25,493	26,879	30,524
Fixed Assets	20,596	20,857	28,703	35,307	41,769
Total Investments	25	22	22	22	22
Intangible Assets					
Total Other Non-Current Assets	214	321	321	321	321
Total Non-current Assets	20,836	21,200	29,046	35,650	42,112
Short-term Debt	31	1,132	2,484	2,484	2,484
Current Portion of Long-Term Debt					
Total Creditors	4,367	5,117	6,510	6,977	7,938
Other Current Liabilities	1,136	1,220	1,220	1,220	1,220
Total Current Liabilities	5,535	7,469	10,215	10,681	11,642
Total Long-term Debt	5,240	1,875	2,500	2,000	2,000
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	111	129	129	129	129
Total Non-current Liabilities	5,352	2,004	2,629	2,129	2,129
Total Provisions	1,250	1,447	1,015	1,015	1,015
Total Liabilities	12,137	10,920	13,858	13,824	14,785
Shareholders Equity	23,467	33,384	40,681	48,705	57,851
Minority Interests					
Total Equity	23,467	33,384	40,681	48,705	57,851

Key Ratios					
	Mar-21A	Mar-22A	Mar-23F	Mar-24F	Mar-25F
Revenue Growth	3.1%	56.0%	11.1%	7.2%	13.8%
Operating EBITDA Growth	21.6%	28.6%	(20.2%)	7.8%	12.2%
Operating EBITDA Margin	28.6%	23.6%	16.9%	17.0%	16.8%
Net Cash Per Share (Rs)	(22.50)	13.04	(2.56)	0.93	6.36
BVPS (Rs)	172.04	244.75	298.25	357.07	424.12
Gross Interest Cover	14.75	41.89	27.61	37.33	37.47
Effective Tax Rate	25.5%	25.6%	25.2%	25.2%	25.2%
Net Dividend Payout Ratio	11.6%	10.7%	9.9%	9.1%	8.0%
Accounts Receivables Days	57.31	50.58	57.26	57.99	56.37
Inventory Days	62.64	42.90	45.16	48.33	46.97
Accounts Payables Days	64.56	42.07	40.10	43.40	42.19
ROIC (%)	30.5%	38.0%	24.8%	21.1%	20.2%
ROCE (%)	38.7%	42.3%	26.2%	23.7%	23.0%
Return On Average Assets	24.6%	27.3%	17.0%	15.5%	15.1%

SOURCE: INCRED RESEARCH, COMPANY REPORTS

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