

India

REDUCE (no change)

Consensus ratings*:	Buy 10	Hold 3	Sell 7
Current price:	Rs334		
Target price:	Rs300		
Previous target:	Rs305		
Up/downside:	-10.2%		
InCred Research / Consensus:	-13.4%		
Reuters:	KANE.NS		
Bloomberg:	KNPL IN		
Market cap:	US\$3,249m	Rs269,837m	
Average daily turnover:	US\$1.6m	Rs133.7m	
Current shares o/s:	808.4m		
Free float:	25.0%		
<small>*Source: Bloomberg</small>			

Key changes in this note

- Lower target price to Rs300 from Rs305.
- Lower FY25F/26F EPS by 3.8%/3.9%.



Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	(0.9)	9.2	20.8
Relative (%)	(1.1)	(1.8)	0.9

Major shareholders	% held
Promoter & Promoter Group	75.0
LIC	3.6
ICICI Prudential Life Insurance	1.2

Kansai Nerolac Paints Limited

Focus remains on improving market share

- Consolidated/standalone revenue grew 5%/5.7% yoy to Rs19.2bn/Rs18.1bn, respectively, in 3QFY24. Volume grew in double digits.
- Given the efforts made to premiumize its industrial range, the EBITDA margin guidance for the segment in low double digits for FY24F is underwhelming.
- While KNPL is taking the right steps, timing is not on its side due to the evolving competitive landscape. Retain REDUCE rating on it with a lower TP of Rs300.

Festive bump lifts decorative segment's volume in double digits

Kansai Nerolac Paints' (KNPL) 3QFY24 consolidated/standalone net sales grew by 5%/5.7% yoy to Rs19.2bn/Rs18.1bn, respectively. Volume grew in double digits led by a festive bump, but demand softness was visible in Dec 2023. Some green shoots are visible in rural markets, which are expected to gradually improve. New business and projects business posted healthy growth. The Paint + range's salience increased during the quarter. The projects business has been expanded to more towns. The industrial business posted healthy growth led by green shoots in the two-wheeler segment, aided by passenger vehicle or PV/ commercial vehicle or CV segments. The tractor segment continued to remain muted. In terms of international operations, Nepal grew in low single digits, which continues to be impacted by a liquidity crunch in the market while Sri Lanka posted high single-digit growth during the quarter. Bangladesh business declined in 3Q, largely due to high inflation and political uncertainty. Both Sri Lanka and Bangladesh saw forex devaluation, impacting reported growth. In the decorative paints segment, the incremental focus is on 1) driving painting services (witnessing higher conversion), 2) increasing the engagement with influencers, and 3) driving premiumization (Paint + range, Kansai Select). However, with the competitive intensity higher than it was ever before, we believe that regaining market share in the decorative paint business will remain a tall task.

Moderation of input cost inflation aids margin expansion

In 3QFY24, KNPL's consolidated gross margin expanded by 570bp yoy (up 50bp qoq) to 36.1%. However, the EBITDA margin, on a qoq basis, fell by 120bp to 12.7%. The industrial segment's EBITDA margin remained in high single digits. Prices have been cut by 3% as of Jan 2024 (cut by 1.2% in 3Q). We find the EBITDA margin outlook in low double digits (10-11%) for the industrial segment to be underwhelming given 1) the efforts made to premiumize offerings, and 2) cutting down low-margin products, with a higher focus on innovation.

Regaining market share remains challenging; retain REDUCE rating

Our concerns over KNPL regaining its market share in the decorative paints segment and operating in a lower margin band for a prolonged period makes us retain our REDUCE rating on the stock with a new target price of Rs300 (30x Dec 2025F EPS), from Rs305 earlier. Upside risks: Market share gain in the decorative paints segment and/or a sharp decline in crude oil prices.

Research Analyst(s)



Rohan KALLE
T (91) 22 4161 1561
E rohan.kalle@incredresearch.com

Nishant BAGRECHA
T (91) 22 4161 1564
E nishant.bagrecha@incredresearch.com

Financial Summary

	Mar-22A	Mar-23A	Mar-24F	Mar-25F	Mar-26F
Revenue (Rsm)	63,694	75,427	79,156	84,861	91,506
Operating EBITDA (Rsm)	6,494	8,180	10,793	11,046	11,542
Net Profit (Rsm)	3,432	4,685	1,826	7,300	7,675
Core EPS (Rs)	6.4	8.7	7.5	13.5	14.2
Core EPS Growth	(34.7%)	36.5%	(13.4%)	79.9%	5.1%
FD Core P/E (x)	52.42	38.40	44.33	24.64	23.44
DPS (Rs)	4.0	4.7	5.6	6.6	7.8
Dividend Yield	1.80%	2.12%	2.50%	2.95%	3.48%
EV/EBITDA (x)	27.74	21.61	15.45	14.98	14.30
P/FCFE (x)	66.67	239.72	19.52	26.94	26.28
Net Gearing	0.1%	(7.4%)	(25.0%)	(26.5%)	(26.7%)
P/BV (x)	4.35	3.97	3.38	3.26	3.19
ROE	8.4%	10.8%	8.2%	13.5%	13.8%
% Change In Core EPS Estimates			(3.70%)	(3.78%)	(3.84%)
InCred Research/Consensus EPS (x)					

SOURCE: INCRED RESEARCH, COMPANY REPORTS

Focus remains on improving market share

Key takeaways from the earnings call

Highlights

- Industrial paints: The two-wheeler segment, which wasn't doing well, saw some green shoots. PVs/CVs witnessed decent demand. Performance coatings did well, benefitted by infrastructure development spending by the government.
- Decorative paint volume was in double digits, led by the festive season. Demand was weaker in Dec 2023. Will lower prices if sales do not pick up.
- Some green shoots are visible in the rural markets.
- New business (wood finish, waterproofing and construction chemicals) and project business posted healthy growth. The Paint + range saliency increased. The projects business has been expanded to more towns, aiding growth.
- Lower margin products like putty and construction chemicals led to widening of the gap in value/volume growth terms. Premium saliency was 25% pre-Covid, now closer to 30% in the overall portfolio.
- Launched a new range of Italian designer textures under 'Kansai Select' (premium segment). NPD saliency saw an uptick. Introduced new sheen variants in the economy range.
- The influencer program is making further progress.
- The architect channel program is seeing good traction. This channel has a higher saliency of premium products.
- Capacity expansion is going on, as per plan.

Industrial business

Automotive business

- The PV segment saw moderate growth driven by the sports utility vehicle or SUV segment and new models.
- The two-wheeler segment posted a strong double-digit growth.
- The CV segment continued its growth momentum led by the medium and heavy commercial vehicle or M&HCV segment.
- The tractor industry is saddled with high inventory due to low demand.

Auto refinish

- The premium/overall segments posted good growth.

Performance coatings

- Liquids posted a double-digit growth led by construction equipment, helmet, appliances and the railway segment. Anti-carbonation paint is being extended to new customers.
- Powder coatings maintained their growth momentum in the premium segment.

International subsidiaries

- Nepal grew in low single digits. Economic challenges continue to impact liquidity.
- Bangladesh declined in 3QFY24, hit hard by high inflation and political uncertainty as well as forex devaluation.
- Sri Lanka posted high single-digit growth in 3QFY24. Forex devaluation impacted reported growth.

Input costs and margins

- Raw material prices were stable in 3QFY24 and are expected to remain stable in the near term.
- Spending on advertisements is expected to remain firm (5% of sales in 9MFY24; slightly higher in 3QFY24).
- 1.2% price cuts taken in 3Q (-3% taken in Jan 2024) in water-based products, which have higher margins.

Outlook

- Growth will be volume-led, closer to double-digit growth. The decorative paint business can do a 8-10% yoy growth in FY24F. The industrial segment's outlook is positive (8-10% yoy growth expected in FY24F) as PV production is up 5-6% this year and the two-wheeler revival will aid growth. General industrial is also expected to do well, aided by the government's spending.
- The EBITDA margin will be around 13-14% in FY24F.
- Market share and competitive intensity: In wood-finish projects, KNPL is growing ahead of the industry. In selective markets, it is giving discounts to aid growth. The overall market share is growing in line with the industry's growth. Market share in North and East India are healthy, incrementally focusing on increasing salience in the southern and western regions to drive growth. Targeting salience in line with the industry (slightly lower currently).
- Distribution reach: 29-30k in FY23, expected to grow by 10% yoy in FY24F, with stronger position in North and East India. Tinting machine penetration is at 70% (85% contribution to sales).
- Services business can go to 10% of the market in a few years, from 1-2% currently.

Figure 1: Quarterly results summary – consolidated

Y/E, Mar (Rs. m)	3QFY23	2QFY24	3QFY24	YoY (%)	QoQ (%)	9MFY23	9MFY24	Gr (%)
Revenue	18,268	19,565	19,187	5.0	-1.9	58,091	60,321	3.8
Expenditure	16,313	16,833	16,747	2.7	-0.5	51,593	51,833	0.5
Consumption of RM	12,714	12,600	12,266	-3.5	-2.7	40,837	38,827	-4.9
as % of Sales	69.6%	64.4%	63.9%			70.3%	64.4%	
Employee Costs	938	1,085	1,171	24.8	8.0	2,762	3,328	20.5
as % of Sales	5.1%	5.5%	6.1%			4.8%	5.5%	
Other Expenditure	2,661	3,148	3,310	24.4	5.2	7,993	9,678	21.1
as % of Sales	14.6%	16.1%	17.3%			13.8%	16.0%	
EBITDA	1,955	2,732	2,440	24.8	-10.7	6,499	8,487	30.6
Depreciation	460	474	484	5.3	2.2	1,343	1,425	6.1
EBIT	1,495	2,259	1,956	30.8	-13.4	5,156	7,062	37.0
Other Income	74	220	201	172.8	-8.6	163	594	264.6
Interest	74	76	75			222	222	
PBT	1,495	2,403	2,082	39.3	-13.3	5,097	7,434	45.9
Total Tax	405	648	561	38.7	-13.4	1,375	2,108	53.3
Adjusted PAT	1,090	1,755	1,521	39.6	-13.3	3,722	5,326	43.1
Minority Interest	-10	-17	-22			-76	-78	
APAT after MI	1,099	1,772	1,543	40.3	-12.9	3,798	5,405	42.3
Extraordinary Items	0	0	0	-	-	0	-5,290	
Reported PAT	1,099	1,772	1,543	40.3	-12.9	3,798	10,695	181.6
Adjusted EPS	1.4	2.2	1.9	40.3	-12.9	4.7	13.2	181.6
Margins (%)	3QFY23	2QFY24	3QFY24	YoY (bp)	QoQ (bp)	9MFY23	9MFY24	(bp)
Gross Margin	30.4%	35.6%	36.1%	570	50	29.7%	35.6%	590
EBITDA	10.7%	14.0%	12.7%	200	-120	11.2%	14.1%	290
EBIT	8.2%	11.5%	10.2%	200	-140	8.9%	11.7%	280
EBT	8.2%	12.3%	10.9%	270	-140	8.8%	12.3%	360
PAT	6.0%	9.0%	7.9%	200	-100	6.4%	8.8%	240
Effective Tax Rate	27.1%	27.0%	27.0%	(10)	0	27.0%	28.4%	140

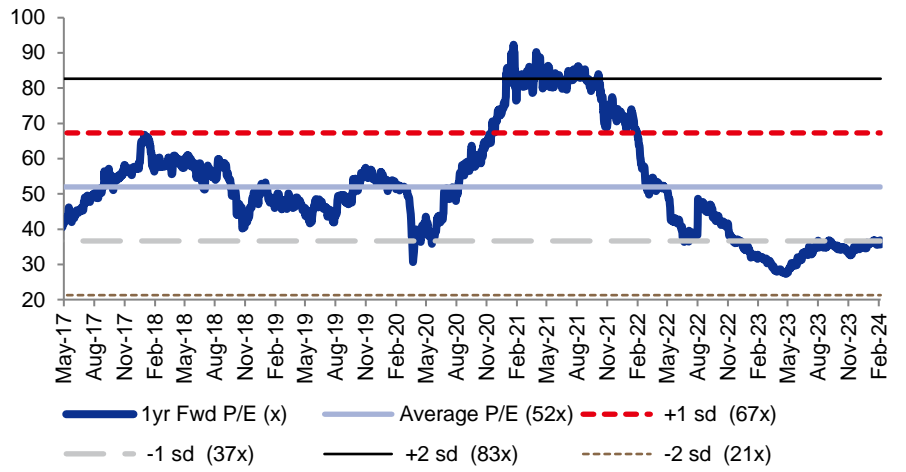
SOURCES: INCRED RESEARCH, COMPANY REPORTS

Figure 2: Our revised earnings estimates

Y/E, Mar (Rs. m)	FY24F			FY25F			FY26F		
	Earlier	Revised	% change	Earlier	Revised	% change	Earlier	Revised	% change
Revenue	79,610	79,156	(0.6)	85,340	84,861	(0.6)	98,468	98,929	0.5
EBITDA	11,159	10,793	(3.3)	11,434	11,046	(3.4)	12,534	12,091	(3.5)
EBITDA Margin (%)	14.0%	13.6%	-40 bp	13.4%	13.0%	-40 bp	12.6%	12.2%	-40 bp
APAT	7,386	7,116	(3.7)	7,587	7,300	(3.8)	8,423	8,095	(3.9)
EPS	9.1	8.8	(3.7)	9.4	9.0	(3.8)	10.4	10.0	(3.9)

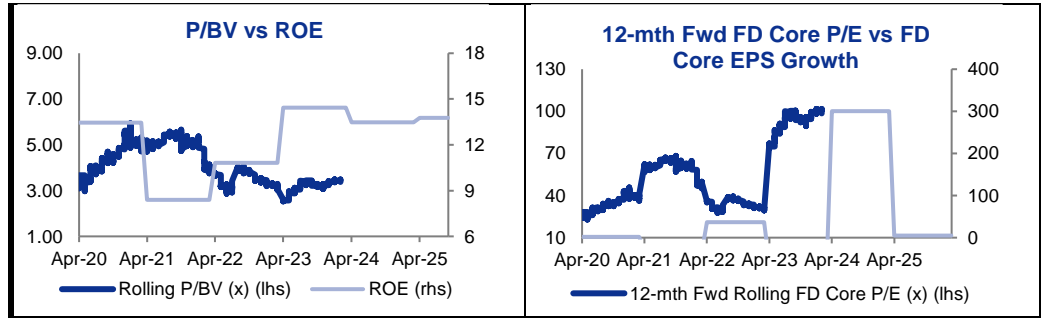
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 3: KNPL's one-year forward P/E trades at -1SD



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	63,694	75,427	79,156	84,861	91,506
Gross Profit	19,421	22,785	28,119	29,799	31,761
Operating EBITDA	6,494	8,180	10,793	11,046	11,542
Depreciation And Amortisation	(1,698)	(1,801)	(1,918)	(2,000)	(2,075)
Operating EBIT	4,796	6,379	8,875	9,047	9,467
Financial Income/(Expense)	(32)	(30)	741	817	901
Pretax Income/(Loss) from Assoc.					
Non-Operating Income/(Expense)					
Profit Before Tax (pre-EI)	4,764	6,349	9,616	9,864	10,369
Exceptional Items			(5,290)		
Pre-tax Profit	4,764	6,349	4,326	9,864	10,369
Taxation	(1,333)	(1,664)	(2,500)	(2,564)	(2,694)
Exceptional Income - post-tax					
Profit After Tax	3,432	4,685	1,826	7,300	7,675
Minority Interests					
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	3,432	4,685	1,826	7,300	7,675
Recurring Net Profit	3,432	4,685	4,058	7,300	7,675
Fully Diluted Recurring Net Profit	3,432	4,685	4,058	7,300	7,675

Cash Flow

(Rs mn)	Mar-22A	Mar-23A	Mar-24F	Mar-25F	Mar-26F
EBITDA	6,494	8,180	10,793	11,046	11,542
Cash Flow from Invt. & Assoc.	51				
Change In Working Capital	(4,912)	(706)	1,780	(1,273)	(1,553)
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense					
Other Operating Cashflow					
Net Interest (Paid)/Received	(286)	(290)	(257)	(257)	(257)
Tax Paid	(1,333)	(1,664)	(2,500)	(2,564)	(2,694)
Cashflow From Operations	14	5,520	9,815	6,952	7,038
Capex	(2,715)	(1,804)	(1,600)	(1,350)	(1,350)
Disposals Of FAs/subsidiaries					
Acq. Of Subsidiaries/Investments	4,585	(2,908)			
Other Investing Cashflow	254	260	998	1,074	1,158
Cash Flow From Investing	2,124	(4,453)	(602)	(276)	(192)
Debt Raised/(repaid)	560	(317)			
Proceeds From Issue Of Shares					
Shares Repurchased					
Dividends Paid	(3,233)	(3,815)	(4,502)	(5,313)	(6,269)
Preferred Dividends					
Other Financing Cashflow	244	3,223	5,295	(60)	(136)
Cash Flow From Financing	(2,430)	(910)	792	(5,373)	(6,405)
Total Cash Generated	(291)	158	10,006	1,304	441
Free Cashflow To Equity	2,698	750	9,213	6,677	6,846
Free Cashflow To Firm	2,424	1,357	9,471	6,934	7,103

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	3,155	6,250	16,256	17,559	18,001
Total Debtors	10,933	12,379	10,977	11,753	12,636
Inventories	16,296	17,291	14,285	15,262	16,439
Total Other Current Assets	4,492	4,900	6,545	6,982	7,493
Total Current Assets	34,876	40,821	48,062	51,556	54,569
Fixed Assets	22,010	22,013	21,695	21,045	20,321
Total Investments	11	32	32	32	32
Intangible Assets	198	198	198	198	198
Total Other Non-Current Assets					
Total Non-current Assets	22,218	22,243	21,925	21,275	20,551
Short-term Debt	2,157	1,824	1,824	1,824	1,824
Current Portion of Long-Term Debt					
Total Creditors	10,898	13,011	12,486	13,403	14,421
Other Current Liabilities					
Total Current Liabilities	13,054	14,834	14,310	15,227	16,245
Total Long-term Debt	1,031	1,047	1,047	1,047	1,047
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities					
Total Non-current Liabilities	1,031	1,047	1,047	1,047	1,047
Total Provisions	1,494	1,579	1,119	1,119	1,119
Total Liabilities	15,579	17,460	16,475	17,392	18,410
Shareholders Equity	41,322	45,337	53,245	55,172	56,442
Minority Interests	193	267	267	267	267
Total Equity	41,515	45,604	53,512	55,439	56,709

Key Ratios

	Mar-22A	Mar-23A	Mar-24F	Mar-25F	Mar-26F
Revenue Growth	25.5%	18.4%	4.9%	7.2%	7.8%
Operating EBITDA Growth	(24.8%)	26.0%	31.9%	2.3%	4.5%
Operating EBITDA Margin	10.2%	10.8%	13.6%	13.0%	12.6%
Net Cash Per Share (Rs)	(0.06)	6.27	24.84	27.26	28.08
BVPS (Rs)	76.68	84.13	98.80	102.38	104.74
Gross Interest Cover	16.78	22.00	34.49	35.16	36.79
Effective Tax Rate	28.0%	26.2%	57.8%	26.0%	26.0%
Net Dividend Payout Ratio	94.2%	81.4%	63.3%	72.8%	81.7%
Accounts Receivables Days	58.73	56.41	53.85	48.88	48.64
Inventory Days	116.55	116.44	112.91	97.93	96.83
Accounts Payables Days	88.20	82.88	91.17	85.81	84.99
ROIC (%)	11.1%	14.6%	21.5%	21.6%	22.2%
ROCE (%)	10.7%	13.4%	18.0%	16.9%	17.3%
Return On Average Assets	6.2%	7.8%	9.6%	9.1%	9.2%

Key Drivers

	Mar-22A	Mar-23A	Mar-24F	Mar-25F	Mar-26F
Revenue growth (%)	25.5%	18.4%	4.9%	7.2%	7.8%
Gross margin (%)	30.5%	30.2%	35.5%	35.1%	34.7%

SOURCE: INCRED RESEARCH, COMPANY REPORTS

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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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been engaged in market making activity for the subject company	NO	NO

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