

One-offs drag Q4; strong visibility to support growth

Aarti Industries' Q4FY21 revenues grew 12.4% YoY to ₹ 1209.4 crore amid 14.2% growth in speciality chemicals to ₹ 1123 crore and 8.5% growth in pharma segment to ₹ 223.8 crore. EBITDA margins improved 118 bps YoY to 21.5%. Improvement in gross margins by 548 bps YoY was largely offset by higher other expenditure amid maintenance shutdown and commissioning of new plants. EBITDA grew 18.9% YoY to ₹ 260.3 crore. PAT grew 23.3% YoY to 136.1 crore amid strong operational performance.

Strong visibility in speciality chemical segment

The company is a preferred partner for customers from multiple industries for benzene-chain based solutions due to strong chemistry prowess, backward integration, larger products basket that is backed by continuous innovation and leadership position in its key products. It is the only domestic player to have products until the sixth level derivative of benzene chemistry. It also expects to leverage on its existing clientele to promote its toluene and other derivatives. Most contracts are long term cost+ contracts that offer better control on the overall cost structure. Recently, it signed three multiyear CRAMs contracts (one cancelled). Owing to strong order book visibility, Aarti is in an aggressive expansion mode. Focus on value-added products (~75% of FY21 revenues), integrated model and better operating leverage are likely to improve its margin profile. Speciality chemical segment revenues are expected to grow at ~28% CAGR in FY21-23E.

Aggressive expansion to support long term growth

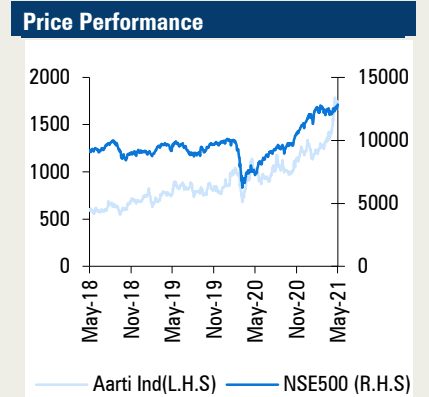
Aarti has spent ~₹ 4000 crore in capex during FY18-21, on three multiyear projects, new R&D unit, expansion of hydrogenation, NCB, de-bottlenecking in various specialty chemicals, and pharma. Going ahead, with guidance of 1-1.5x of assets turnover, which is embedded in the company's ambitious target of 1.7-2x sales by FY24 and 2.5-3.5x FY27, the company has to spend ₹ 1000+ crore of capex per annum to complete the existing pipeline, expansion in value added, pharma segments in the backdrop of strong demand visibility to drive long-term growth.

Valuation & Outlook

Q4 numbers were impacted by annual shutdown and commissioning of new plants. Demand for speciality chemical has almost reached to pre-COVID level. Based on visibility, the management has given ambitious revenues, EBIT and PAT guidance of 1.7-2x growth from FY21-24E. Leveraging on core knowledge of benzene-based derivatives, the company is continuously expanding product basket towards value added products covering the entire value chain. In pharma, strong growth is expected from developed markets backed by integrated model and new launches. Margins are also expected to improve due to incremental addition of high-value products. We maintain **BUY** with a target price of ₹ 1920 (32x FY23E EPS of ₹ 60) vs. ₹ 1340 earlier.



Particulars	
Particular	Amount
Market Capitalisation	₹ 29016 crore
Debt (FY21)	₹ 3022 crore
Cash (FY21)	₹ 412 crore
EV	₹ 31626 crore
52 week H/L	1815/851
Equity capital	₹ 87.1 crore
Face value	₹ 2



Source: ICICI Direct Research, Company

Key risks to our call

- Higher than expected volatility in raw material price
- Slowdown in end users demand

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Key Financial Summary

₹ Crore	FY20	FY21E	FY22E	FY23E	CAGR FY21-23 (%)
Revenues	4186.3	4506.1	5581.9	7127.1	25.8
EBITDA	977.3	981.5	1345.6	1775.7	34.5
EBITDA Margins (%)	23.3	21.8	24.1	24.9	
Adj. Net Profit	536.1	525.8	759.2	1045.3	41.0
EPS (Adjusted)	30.8	30.2	43.6	60.0	
PE (x)	54.1	55.2	22.9	27.8	
EV to EBITDA (x)	31.6	32.2	23.5	18.0	
RoCE (%)	13.5	10.7	12.7	15.3	
RoE (%)	18.0	15.0	16.3	18.7	

Source: ICICI Direct Research; Company

Exhibit 1: Variance Analysis

	Q4FY21	Q4FY21E	Q4FY20	Q3FY21	YoY (%)	QoQ (%)	Comments
Revenue	1,209.4	1,316.8	1,076.2	1,186.8	12.4	1.9	YoY growth was mainly due to strong volume growth in both chemical and pharma segments. Miss vis-à-vis I-direct estimates mainly due to temporary shutdown of plants
Raw Material Expense:	558.6	632.0	556.1	544.9	0.5	2.5	
Gross Margins	53.8	52.0	48.3	54.1	548 bps	-28 bps	YoY improvement amid better product mix
Employee Expenses	97.6	92.2	78.5	90.6	24.3	7.8	
Other Expenditure	292.8	258.3	222.6	266.4	31.6	9.9	Temporary shutdown of plants resulted in in higher costs by ~₹ 15 crore (₹ 12 crore for chemical plants and ₹ 2-3 crore for pharma plant)
Total Operating Expend	949.1	982.5	857.2	901.8	10.7	5.2	
EBITDA	260.3	334.2	218.9	285.0	18.9	-8.7	
EBITDA (%)	21.5	25.4	20.3	24.0	118 bps	-249 bps	YoY improvement was mainly due to better product mix. Sequential decline and miss vis-à-vis I-direct estimates mainly due to additional cost of plants shutdown and commercialisation of new plants
Interest	21.6	17.3	34.0	17.3	-36.4	25.1	
Depreciation	65.6	58.7	49.3	58.7	33.2	11.9	YoY increase mainly due to commercialisation of chlorination unit at Jhagadia and Phase 2 unit at Dahej SEZ
Other income	0.0	0.4	0.4	0.4	-97.6	-97.7	
PBT before EO	173.1	258.7	136.1	209.4	27.2	-17.4	
Less: Exceptional Item:	0.0	0.0	0.0	0.0	0.0	0.0	
PBT	173.1	258.7	136.1	209.4	27.2	-17.4	
Tax	33.7	54.3	25.7	40.3	31.0	-16.3	
MI & Share of loss/ (ga	3.2	3.9	0.0	3.9	0.0	-17.1	
Adj. Net Profit	136.1	200.5	110.4	165.3	23.3	-17.6	YoY growth mainly in sync with operational performance. Miss vis-à-vis I-direct estimates mainly due to lower-than-expected operational performance and higher depreciation

Key Metrics

Speciality Chemicals	1,123.0	1,217.2	983.5	1,078.8	14.2	4.1	Miss vis-à-vis I-direct estimates mainly due to annual maintenance shutdown at the acid division at Vapi and asset revamp linked maintenance shutdown at Jhagadia, impacted volumes
Pharma	223.8	237.3	206.4	232.2	8.5	-3.6	Miss vis-à-vis I-direct estimates due to sustainability initiative linked shutdown taken at pharma units in Q4FY21, impacting the operations partly

Source: ICICI Direct Research

Exhibit 2: Change in Estimates

(₹ Crore)	FY22E			FY23E		
	Old	New	% Change	Old	New	% Change
Revenue	5,417.0	5,581.9	3.0	6,959.0	7,127.1	2.4
EBITDA	1,345.5	1,345.6	0.0	1,750.6	1,775.7	1.4
EBITDA Margin (%)	24.8	24.1	-69 bps	25.2	24.9	-29 bps
PAT	775.9	759.2	-2.2	1,062.8	1,045.3	-1.6
EPS (₹)	44.5	43.6	-2.2	61.0	60.0	-1.7

Source: ICICI Direct Research

Exhibit 3: Change in Estimates

(₹ crore)	Current				Earlier		Comments
	FY20	FY21E	FY22E	FY23E	FY22E	FY23E	
Speciality Chemicals	3,865.0	4,151.6	5,204.3	6,773.3	4,956.4	6,505.6	Changed as per management guidance
Pharma	756.0	871.6	1,012.1	1,163.9	1,027.6	1,181.7	

Source: ICICI Direct Research

Conference Call Highlights

- Guided volume growth of 25-35% in FY22 and 30-40% growth in FY23 for both segments
- Ambitious target to achieve 1.7-2x revenues, EBIT and PAT by FY24 and 2.5-3.5x of revenues, 3-4x of EBIT and PAT by FY27 over FY21 numbers (excluding remittance received for cancelled contract).
- **Capex**
 - FY21 – ₹ 1300 crore;
 - ₹ 1500 crore for FY22 and FY23 for-
 - USFDA capacities expansion: API unit at Tarapur, & Intermediates unit at Vapi
 - Unit for second long term contracts at Dahej SEZ
 - Unit for third long term contract at Jhagadia
 - NCB capacity expansion at Vapi
 - Expansion cum asset upgradation for acid unit at Vapi
 - Expansion, asset restoration, sustainability initiatives etc.
 - Expects additional ₹ 3000 crore capex to support growth in FY24-27, spend on-
 - value added products like Florotoluene, Photochlorination and other downstream products and
 - universal multipurpose plant (UMPP) mainly for pharma and agro chemical sector
 - Maintenance capex – 200-250 crore per annum
- In Q4, the company completed the commercialisation of balance for the chlorination project and also for the Phase 2 unit at Dahej SEZ.
- Assets turnover expected to be 1-1.5x from new projects
- Site development work to commence on 100+ acre land at Jhagadia. Also acquired over 120 acres' land at Atali, Gujarat
- EBITDA margins are expected to be in the vicinity of 25-30% between FY24-27E mainly due to launch of value added products
- Total 75% contribution from value-added products in FY21
- The company selection of products based on import substitution, global growth and China + one opportunity

Exhibit 4: Trends in quarterly performance

(₹ crore)	Q3FY19	Q4FY19	Q1FY20	Q2FY20	Q3FY20	Q4FY20	Q1FY21	Q2FY21	Q3FY21	Q4FY21	YoY (%)	QoQ (%)
Total Operating Incom	1276.0	1141.1	1135.5	988.1	1083.6	1076.2	937.3	1172.6	1186.8	1209.4	12.4	1.9
Raw Material Expendi	739.9	597.8	604.2	462.7	530.4	556.1	447.0	578.1	544.9	558.6	0.5	2.5
% of Revenue	58.0	52.4	53.2	46.8	48.9	51.7	47.7	49.3	45.9	46.2	-548 bps	28 bps
Gross Profit	536.2	543.3	531.3	525.4	553.3	520.1	490.4	594.5	641.9	650.7	25.1	1.4
Gross Profit Margin (%)	42.0	47.6	46.8	53.2	51.1	48.3	52.3	50.7	54.1	53.8	548 bps	-28 bps
Employee Expenses	62.6	77.8	69.5	74.0	83.2	78.5	89.7	93.5	90.6	97.6	24.3	7.8
% of Revenue	4.9	6.8	6.1	7.5	7.7	7.3	9.6	8.0	7.6	8.1	77 bps	44 bps
Other Expenditure	220.5	214.8	211.7	197.3	215.8	222.6	218.7	246.7	266.4	292.8	31.6	9.9
% of Revenue	17.3	18.8	18.6	20.0	19.9	20.7	23.3	21.0	22.4	24.2	353 bps	177 bps
Total Expenditure	1022.9	890.4	885.4	734.0	829.4	857.2	755.3	918.4	901.8	949.1	10.7	5.2
% of Revenue	80.2	78.0	78.0	74.3	76.5	79.7	80.6	78.3	76.0	78.5	-118 bps	249 bps
EBITDA	253.1	250.7	250.1	254.1	254.2	218.9	182.0	254.3	285.0	260.3	18.9	-8.7
EBITDA Margin (%)	19.8	22.0	22.0	25.7	23.5	20.3	19.4	21.7	24.0	21.5	118 bps	-249 bps
Depreciation	43.7	45.5	43.2	45.7	47.0	49.3	52.0	55.0	58.7	65.6	33.2	11.9
Interest	42.0	43.8	31.0	31.1	28.7	34.0	25.3	22.2	17.3	21.6	-36.4	25.1
Other Income	4.0	0.0	2.5	5.6	0.4	0.4	0.2	0.4	0.4	0.0	-97.6	-97.7
Less: Exceptional Item	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
PBT	171.5	161.4	178.4	182.9	178.8	136.1	104.9	177.5	209.4	173.1	27.2	-17.4
Total Tax	31.8	34.3	36.5	31.1	36.1	25.7	21.7	33.7	40.3	33.7	31.0	-16.3
Tax rate (%)	18.5	21.3	20.4	17.0	20.2	18.9	20.7	19.0	19.2	19.5	57 bps	26 bps
PAT before MI	139.7	127.1	141.9	151.8	142.7	110.4	83.2	143.9	169.2	139.3	26.3	-17.6
Minority Interest	6.0	1.9	3.8	4.2	2.9	0.0	1.3	1.3	3.9	3.2		-17.1
PAT	133.7	125.3	138.1	147.6	139.8	110.4	81.9	142.5	165.3	136.1	23.3	-17.6
PAT Margin (%)	10.5	11.0	12.2	14.9	12.9	10.3	8.7	12.2	13.9	11.3	100 bps	-267 bps

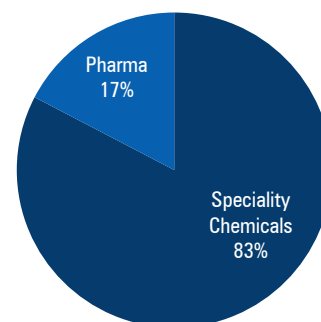
Source: ICICI Direct Research

Company Background

Aarti Industries (Aarti), established in 1984 by first generation technocrats Rajendra Gogri, is a leading benzene-based speciality chemical companies globally. The company primarily operates in two business segments – speciality chemicals (84%) and pharmaceuticals (14%). In speciality chemicals, the company is mainly into feedstock materials such as benzene, toluene, nitric acid, chlorine, methanol, aniline sulphur. In the pharmaceutical segment, Aarti is present in APIs, intermediates and xanthine derivatives for the pharmaceutical and food/beverages industry. Also, it has a de-risked portfolio that is multiproduct, multi-geography, multi-customer and multi-industry. The company ranks among the top five globally for 75% of its portfolio. Its 200+ products are sold to 700+ domestic and 400+ export customers across the globe in 60 countries with a major presence in the US, Europe and Japan. Also, among end user sectors, agrochemicals, pharmaceuticals and FMCG contribute 50-60% of Aarti’s revenue while other end-user industries include polymers, pigments, printing inks, dyes, fuel additives, aromatics, etc.

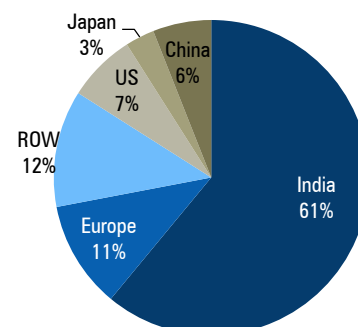
Aarti has 13 manufacturing units for speciality chemicals; five for pharma (two USFDA and three WHO/GMP), mostly located in close proximity to the large ports of western India. The company also has four R&D centres – one in Navi Mumbai, two in Vapi and one in Dombivali – which focus on innovations in new speciality chemicals and pharmaceutical applications.

Segment Bifurcation



Source: ICICI Direct Research, Company

Geographical Bifurcation



Source: ICICI Direct Research, Company

Exhibit 5: Timeline of company events

Years	Details
1984	Incorporated Aarti Organics Private Limited
1986	Commenced a 1,200 Tonnes Per Annum (TPA) unit for Nitro Chloro Benzenes (NCB) in Sarigram, Gujarat
1990	Set up the first large-scale organic plant in Vapi – a 4,500 TPA unit for NCB
2001	Set up a large-scale hydrogenation and nitration unit at Jhagadia (hydrogen gas via pipeline) Expanded the NCB and sulphuric acid capacity
2005-08	Set up a large-scale speciality chemical unit in Kutch Received US FDA approval for an Active Pharmaceutical Ingredient (API) unit in Tarapur Upgraded the hydrogenation unit from batch to continuous
2011	Received US FDA approval for the custom synthesis division at Vapi Commenced bulk shipment for global markets
2016	Commissioned an ethylation facility at Dahej SEZ (ethylene gas via pipeline) Expanded the NCB capacity from 57 KTPA to 75 KTPA
2017	Commenced the functioning of the calcium chloride facility Started operations at co-generation and solar power plants Commissioned the Nitro Toluene plant
2018	Signed two large multi-year contracts with global players Manufacturing facility being set up at Dahej SEZ
2019	Commissioned the Nitro Toluene hydrogenation facility at Jhagadia Signed another multi-year contract with a global player
2020	Operationalised Aarti Research and Technology Centre (ARTC) at Mahape, Navi Mumbai Commissioned two units at Dahej SEZ for high-value speciality chemicals

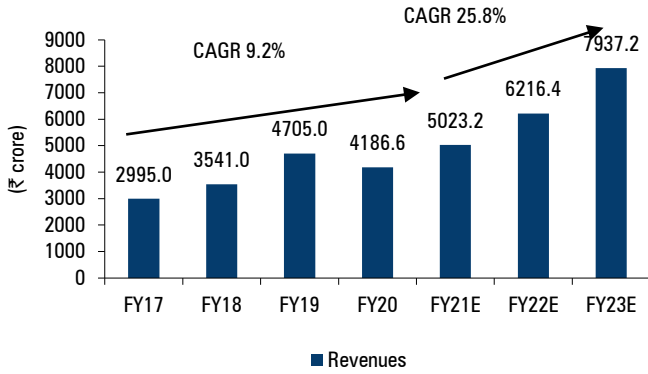
Source: ICICI Direct Research, Company

Exhibit 6: Multi-year projects

Projects	Project size (₹ cr)	Tenure (years)	Peak annual revenues (₹ cr)	Product	Status
Project 1	4000	10	400	agro chemical	Cancelled, expects to get US\$ 120-130 mn as competition (US\$ 20 each FY21E and FY22E and remaining US\$ 80-90 million in end of FY22E)
Project 2	10000	20	500	polymer application	Guided to commissioned in FY22E
Project 3	900	10	90	NA	Guided to commissioned in FY22E

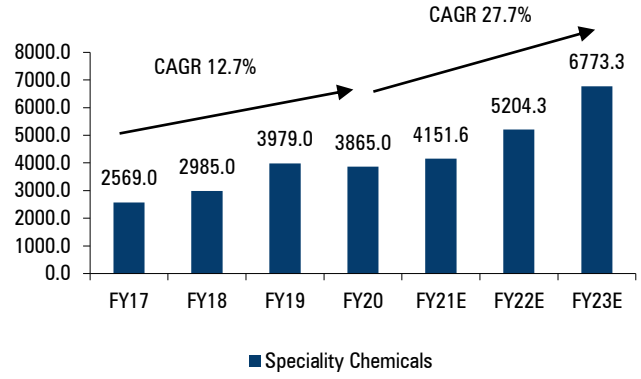
Source: ICICI Direct Research, Company

Exhibit 7: Revenues to grow at 26% CAGR in FY21-23E



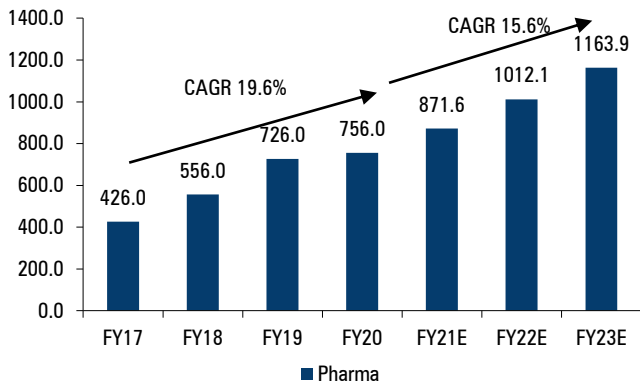
Source: ICICI Direct Research, Company; *Ex demerged entity

Exhibit 8: Chemicals to grow at 28% CAGR in FY21-23E



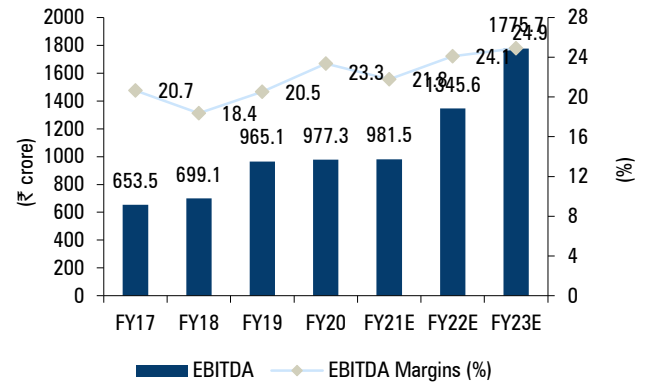
Source: ICICI Direct Research, Company

Exhibit 9: Pharma to grow at 16% CAGR in FY21-23E



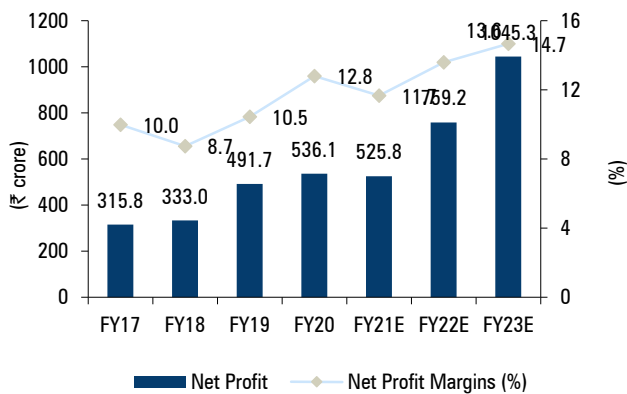
Source: ICICI Direct Research, Company

Exhibit 10: EBITDA & EBITDA margins trend



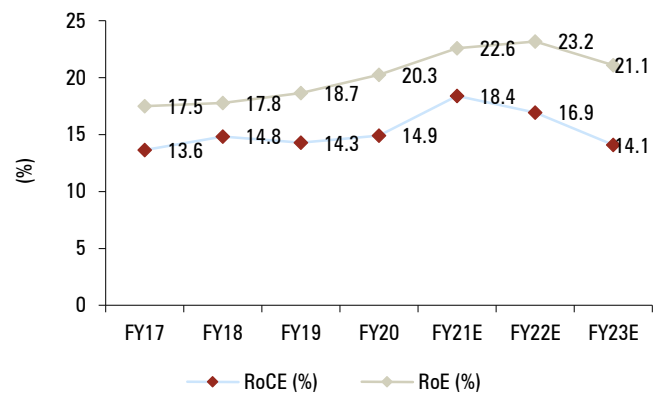
Source: ICICI Direct Research, Company

Exhibit 11: Adjusted PAT & PAT margins trend



Source: ICICI Direct Research, Company

Exhibit 12: RoE & RoCE trend



Source: ICICI Direct Research, Company

Financial Summary

Exhibit 13: Profit and loss statement				
	₹ crore			
(Year-end March)	FY20	FY21E	FY22E	FY23E
Total Operating Income	4,186.3	4,506.1	5,581.9	7,127.1
Growth (%)	-11.0	7.6	23.9	27.7
Raw Material Expenses	2,056.3	2,128.6	2,578.4	3,292.2
Gross Profit	2,130.0	2,377.5	3,003.5	3,835.0
Gross Profit Margins (%)	50.9	52.8	53.8	53.8
Employee Expenses	305.2	371.4	460.0	587.4
Other Expenditure	847.4	1,024.6	1,197.9	1,471.9
Total Operating Expenditure	3,209.0	3,524.6	4,236.3	5,351.4
EBITDA	977.3	981.5	1,345.6	1,775.7
Growth (%)	1.3	0.4	37.1	32.0
Interest	124.8	86.4	96.7	96.7
Depreciation	185.2	231.3	311.6	374.0
Other Income	8.8	1.1	27.9	17.8
PBT before Exceptional Item	676.2	664.9	965.2	1,322.8
Less: Exceptional Items	0.0	0.0	-637.5	0.0
PBT after Exceptional Items	676.2	664.9	1,602.7	1,322.8
Total Tax	129.4	129.3	320.5	264.6
PAT after MI	536.1	525.8	1,269.2	1,045.3
Adjusted PAT	536.1	525.8	759.2	1,045.3
Growth (%)	6.3	-1.9	44.4	37.7
EPS (Adjusted)	30.8	30.2	43.6	60.0

Source: ICICI Direct Research

Exhibit 14: Cash Flow Statement				
	₹ crore			
(Year-end March)	FY20	FY21E	FY22E	FY23E
Profit/(Loss) after taxation	512.3	567.9	1,269.2	1,045.3
Add: Depreciation & Amortiza	185.2	231.3	311.6	374.0
Net Increase in Current Asse	-68.6	-136.0	-328.9	-573.1
Net Increase in Current Liabil	358.8	128.8	36.8	170.8
Others	114.3	80.7	96.7	96.7
CF from Operating activities	1,102.1	872.7	1,385.4	1,113.6
Investments	1.3	-7.8	0.0	0.0
(Purchase)/Sale of Fixed Ass	-1,125.5	-1,314.4	-1,200.0	-1,200.0
Others	0.2	0.1	3.0	3.1
CF from Investing activities	-1,124.1	-1,322.1	-1,197.0	-1,196.9
(inc)/Dec in Loan	-303.2	745.9	200.0	0.0
Dividend & Dividend tax	-106.4	-45.1	-126.9	-104.5
Other	-125.4	-86.4	-96.7	-96.7
CF from Financing activities	-534.9	614.5	-23.6	-201.2
Net Cash Flow	-556.9	165.0	164.9	-284.5
Cash and Cash Equivalent	804.2	247.3	412.3	577.2
Cash	247.3	412.3	577.2	292.7
Free Cash Flow	-23.4	-441.7	185.4	-86.4

Source: ICICI Direct Research

Exhibit 15: Balance Sheet				
	₹ crore			
(Year-end March)	FY20	FY21E	FY22E	FY23E
Equity Capital	87.1	87.1	87.1	87.1
Reserve and Surplus	2,891.7	3,415.8	4,558.1	5,498.8
Total Shareholders funds	2,978.8	3,502.9	4,645.2	5,586.0
Total Debt	2,094.2	3,022.1	3,222.1	3,222.1
Deferred Tax Liability	211.0	233.9	238.6	243.4
Minority Interest	94.6	12.2	12.5	12.7
Other Non Current Liabilities	550.9	224.4	228.9	233.5
Source of Funds	5,929.5	6,995.6	8,347.3	9,297.7
Gross Block - Fixed Assets	3,837.0	5,192.4	6,492.4	7,792.4
Accumulated Depreciation	1,368.6	1,599.9	1,911.5	2,285.5
Net Block	2,468.5	3,592.6	4,580.9	5,506.9
Capital WIP	1,417.6	1,297.9	1,197.9	1,097.9
Fixed Assets	3,886.1	4,890.5	5,778.9	6,604.8
Investments	37.0	63.5	63.5	63.5
Other non-Current Assets	404.5	320.1	326.5	333.0
Inventory	835.7	935.7	1,070.5	1,366.8
Debtors	753.4	793.7	983.2	1,255.4
Other Current Assets	168.5	225.9	230.4	235.0
Cash	247.3	412.3	577.2	292.7
Total Current Assets	2,004.9	2,367.6	2,861.3	3,149.9
Creditors	345.2	576.3	611.7	781.1
Provisions	39.9	40.1	40.9	41.7
Other Current Liabilities	18.0	29.6	30.2	30.8
Total Current Liabilities	403.1	646.1	682.9	853.6
Net Current Assets	1,601.8	1,721.5	2,178.5	2,296.3
Application of Funds	5,929.5	6,995.6	8,347.3	9,297.7

Source: ICICI Direct Research

Exhibit 16: Ratio Analysis				
(Year-end March)	FY20	FY21E	FY22E	FY23E
Per share data (₹)				
Reported EPS	30.8	30.2	72.8	60.0
Cash EPS	23.3	25.6	36.3	54.0
BV per share	171.0	201.0	266.6	320.6
Cash per Share	14.2	23.7	33.1	16.8
Dividend per share	7.5	4.5	7.3	6.0
Operating Ratios (%)				
Gross Profit Margins	50.9	52.8	53.8	53.8
EBITDA margins	23.3	21.8	24.1	24.9
Adjusted PAT Margins	12.8	11.7	13.6	14.7
Cash Conversion Cycle	108.5	93.4	94.3	94.3
Asset Turnover	1.1	0.9	0.9	0.9
EBITDA conversion Rate	112.8	88.9	103.0	62.7
Return Ratios (%)				
RoE	18.0	15.0	16.3	18.7
RoCE	13.5	10.7	12.7	15.3
RoC	18.6	14.2	15.7	17.7
Valuation Ratios (x)				
P/E	54.1	55.2	22.9	27.8
EV / EBITDA	31.6	32.2	23.5	18.0
EV / Net Sales	7.4	7.0	5.7	4.5
Market Cap / Sales	6.9	6.4	5.2	4.1
Price to Book Value	9.7	8.3	6.2	5.2
Solvency Ratios				
Debt / EBITDA	2.1	3.1	2.4	1.8
Debt / Equity	0.7	0.9	0.7	0.6
Current Ratio	4.4	3.0	3.3	3.3

Source: ICICI Direct Research

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Hold: -5% to 15%;

Reduce: -5% to -15%;

Sell: <-15%



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