

March 18, 2020

Covid-19 major threat to global growth but provides opportunity to build long term portfolio...

We have envisaged the impact of Coronavirus (Covid-19) on our midcap coverage universe based on the revenue contribution from both the US as well as Europe. Since we believe these two geographies are witnessing an upsurge in patients infected by Coronavirus, there is a high probability of city lockdowns in the near future as witnessed in a few European countries recently. We expect this to largely hamper manufacturing growth compared to the services sector, going ahead.

In our midcap universe of 11 companies, we expect Tata Chemicals, VA Tech Wabag, Emmbi Industries and Kanpur Plastipack to be the most impacted stocks given that all these have revenue contributions in excess of 30-35% from the said geographies. The rest from our universe could be impacted by supply chain issues related to raw material, which, we believe, is largely discounted in the stock price.

In terms of RM requirements, majority of the chemical inputs are imported from China. With China returning to action recently albeit at lower utilisation, we do not expect much impact from the supply side. **However, the real impact can come from the demand side due to the cascading impact of the slowdown. This can eventually lead to suppressed prices and, thereby, financial growth of most companies.** Further, a cash flow crunch can impact the debt repayment schedule. However, we expect the same to be refinanced largely as most economies are coming out with quantitative easing (QE) leading to lower interest rates. However, we expect companies with high levered balance sheet or low cash flows to face challenges to refinance. Thus, we believe one should select strong balance sheet companies with low leverage and higher cash flows during these turbulent time. We also believe the Covid-19 issue is not relevant only to one geography but is widespread globally. Hence, central government/central banks are expected to eventually come out with assistance to manage the entire global economy.

Valuation & Outlook

We believe majority of the negative outcomes from Covid-19, for at least the next two quarters, have already been discounted across global indices. However, either any delay beyond that or a substantial increase in infection can result in more negative outcomes. Hence, the probability of a further downside in equity indices cannot be ruled out. However, we believe majority of the stocks are available at suppressed valuations. Therefore, we believe this is the right time to build a portfolio in a gradual manner to gain from the roller coaster ride ahead.

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Exhibit 1: Revision of estimates

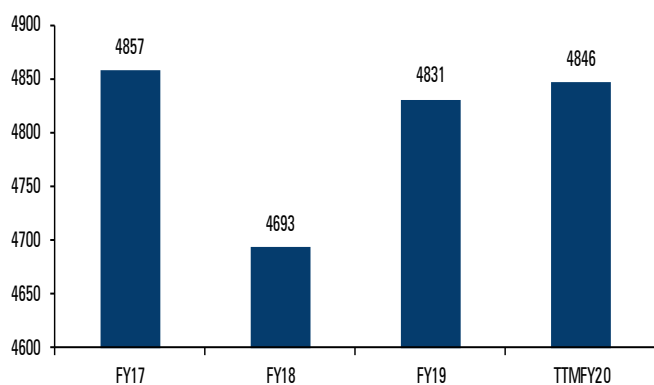
Company Name	Existing PAT estimates		Revised PAT estimates		CMP (₹)	Earlier Target Price (₹)	Revised Target Price (₹)	Upside (%)	Earlier Rating	Revised Rating
	FY20E	FY21E	FY20E	FY21E						
Tata chemical	1,081	1,224	1,074	1,043	239	360	220	-8%	HOLD	REDUCE
VA Tech Wabag	98	109	98	58	120	200	100	-17%	REDUCE	SELL
Apcotex Industries	50	66	14	20	79	205	70	-11%	HOLD	REDUCE
Emmbi Industries	21	26	14	13	56	180	50	-11%	BUY	REDUCE
Kanpur Plastipack	19	24	10	6	41	135	30	-27%	BUY	SELL

Source: ICICI Direct Research, Company

Tata Chemicals

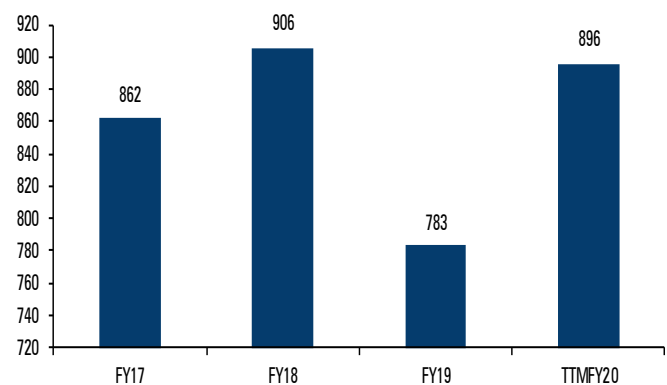
Tata Chemicals derives ~60% of basic chemical revenues from Europe and North America while the corresponding figure for EBITDA contribution is at ~50%. The company's UK capacity largely caters to the European market. We expect this to witness slower growth due to the ongoing Covid-19 issue. The North America plant exports soda ash to counterparts like Asian countries. We expect the same to also witness poor growth largely on account of the depressed demand environment across auto/construction sector, etc. For the same reason, we curb volume growth in both these geographies. **(Note: Covid-19 is still at an early stage and it is very difficult to assess the actual impact in case of prolonged infection).** On the other hand, although lower input cost could maintain basic chemical EBITDA/ton, we expect any negative development from the fear of recession in the US and Europe due to Covid-19 to translate into subdued demand outlook. Hence, we can expect pressure in soda ash prices. We cut our EV/EBITDA multiple for domestic basis chemical and overseas basic chemical businesses to factor in the potential negative impact in both volumes and margins, going ahead. We revise our target price to ₹ 220/share excluding investment portfolio value. We have a **REDUCE** rating on the stock.

Exhibit 2: Basic chemical revenues from Europe & North America (₹ crore)



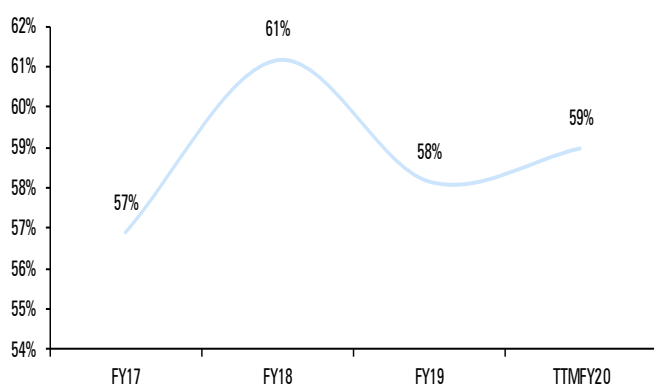
Source: ICICI Direct Research, Company

Exhibit 3: Basic chemical EBITDA from Europe & North America (₹ crore)



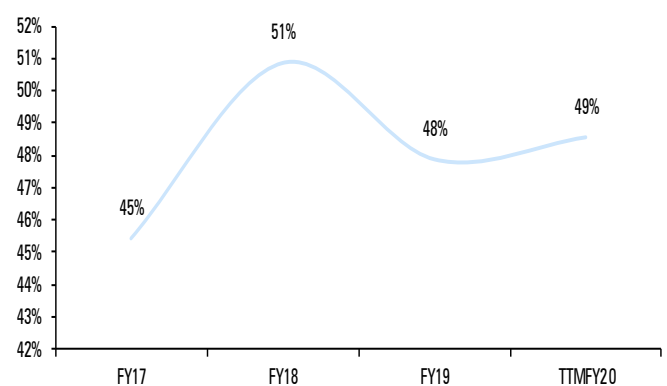
Source: ICICI Direct Research, Company

Exhibit 4: Europe & North America revenue contribution against overall basic chemical revenue



Source: ICICI Direct Research, Company

Exhibit 5: Europe & North America EBITDA contribution against overall basic chemical EBITDA



Source: ICICI Direct Research, Company

Exhibit 6: SOTP Analysis

In ₹ Crore unless other mentioned	Revenue			EBITDA			EV/EBITDA	EV
	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY21E	FY21E
Basic Chemical								
India	2,831	2,694	2,928	823	800	887	4.5x	3,599
ROW	5,272	4,586	4,670	972	841	864	3.0x	2,522
Speciality Products								
Rallis	2,276	2,564	2,877	283	328	386	11.7x	3,823
Other Speciality	70	283	396	15	56	78	8.0x	447
Consolidated EV								7,563
Less: Net debt								1,960
Target MCAP								5,603
No. of shares								25.5
Target price/share								220
CMP								239
Upside/downside								-8%

Source: ICICI Direct Research, Company

Exhibit 7: Key Financial Summary

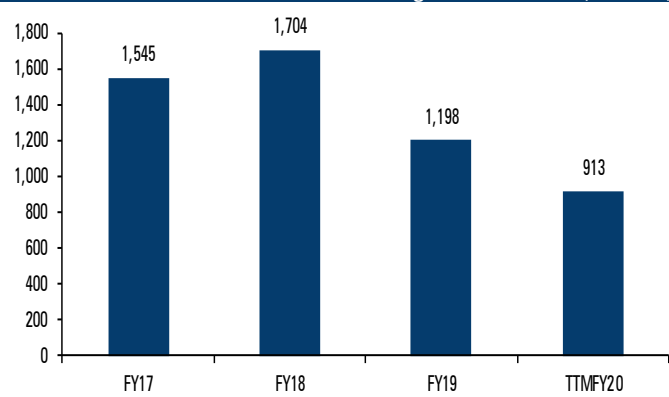
(₹ Crore)	FY16	FY17	FY18	FY19	FY20E	FY21E	FY22E	CAGR FY19-22E
Net Revenue	14,872.9	10,346.1	10,269.7	11,296.3	10,587.6	10,045.6	10,646.7	(2.0)
EBITDA	2,091.7	2,094.3	2,190.7	2,095.1	2,157.3	2,090.5	2,282.4	2.9
EBITDA Margins (%)	14.1%	20.2%	21.3%	18.5%	20.4%	20.8%	21.4%	
Adj. PAT	696.4	879.6	1,290.6	1,163.9	1,074.4	1,042.9	1,156.5	(0.2)
Adj. EPS (₹)	27.3	34.5	50.6	45.7	42.2	40.9	45.4	
EV/EBITDA	6.4x	4.4x	3.2x	3.4x	3.5x	3.8x	3.1x	
P/E	8.7x	6.9x	4.7x	5.2x	5.7x	5.8x	5.3x	
ROE (%)	10.2	11.1	11.6	9.4	8.4	7.8	8.3	
ROCE (%)	8.7	9.7	8.3	8.4	8.1	7.7	8.1	

Source: ICICI Direct Research, Company

VA Tech Wabag

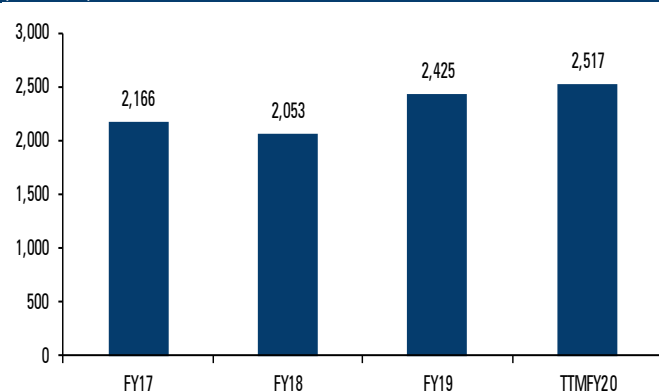
The order backlog of the company is at ₹ 10826 crore excluding framework contracts as on Q3FY20 of which Wabag's overseas segment constitutes 23% of the backlog. In terms of revenues, TTMFY20 revenues remained at ₹ 2586 crore of which Wabag's overseas share was at 35%. This represents a book to bill of 2.7x. The company has already been witnessing a slowdown in recovery of receivables. We expect the slowdown in Europe along with lower crude oil prices to translate into a fall in incremental capex there, in turn impact the backlog of company, going ahead. Apart from this, a stretch in the working capital cycle of the company can limit the execution capability and, thereby, revenue growth further, going ahead. We value the company at 9.5x FY21E PER and arrive at a target price of ₹ 100/share. We have a **SELL** rating on the stock.

Exhibit 8: Overseas revenue excluding Asian cluster (₹ crore)



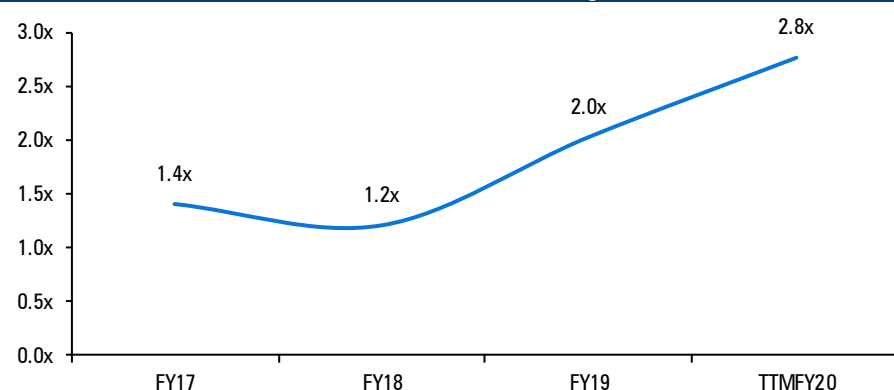
Source: ICICI Direct Research, Company

Exhibit 9: Overseas order backlog excluding Asian cluster (₹ crore)



Source: ICICI Direct Research, Company

Exhibit 10: Book to bill of overseas business excluding Asian cluster



Source: ICICI Direct Research, Company

Exhibit 11: Key financial summary (₹ crore)

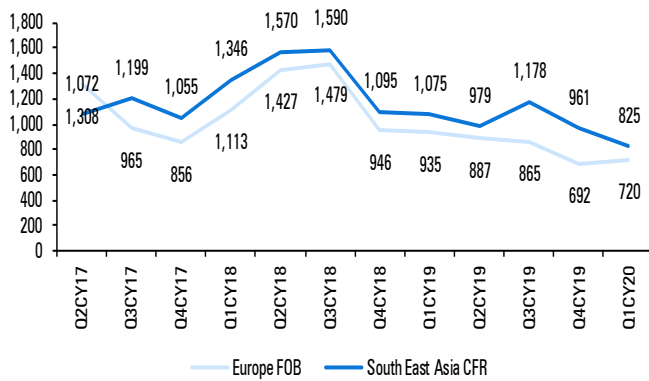
Key Financials	FY17	FY18	FY19	FY20E	FY21E	FY22E	CAGR (FY19-22E)
Net Revenue	3,208	3,457	2,781	2,816	2,632	2,850	0.8%
EBITDA	297	292	194	270	237	256	9.7%
EBITDA Margins (%)	9.2	8.4	7.0	9.6	9.0	9.0	
Net Profit	91	132	105	98	58	60	-17.1%
EPS (₹)	16.7	24.1	19.2	18.0	10.6	10.9	
P/E	6.9	4.8	6.0	6.5	11.0	10.6	
RONW (%)	9.4	12.3	9.5	8.8	5.0	5.0	
ROCE (%)	24.8	22.0	14.6	19.5	17.3	17.8	

Source: ICICI Direct Research, Company

Apcotex Industries

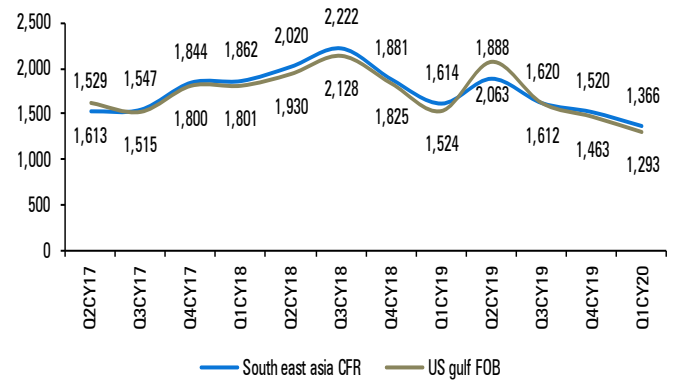
The export segment of the company remains at a mere 15%. Hence, we do not expect much of an impact due to Covid-19. Although we expect a lower price spread between Europe and South East Asia, butadiene prices can provide some assistance in terms of NBR prices. However, a slump in domestic auto sales volume can keep overall realisation under pressure and thereby gross margins. Until there is a revival in the auto sector, we expect gross margins to be lower than earlier levels of 30-32%. However, the power plant at Valia can provide some respite to the overall operational performance. We revise our estimates to factor in lower realisation growth. We value the company at 15x FY22E PER and arrive at a target price of ₹ 70/share. We have a **REDUCE** rating on the stock.

Exhibit 12: Butadiene price (US\$/tonne)



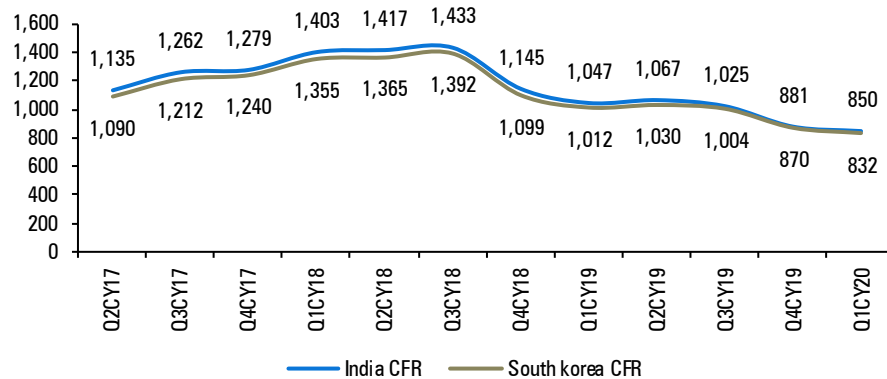
Source: ICICI Direct Research, Bloomberg

Exhibit 13: Acrylonitrile price (US\$/tonne)



Source: ICICI Direct Research, Bloomberg

Exhibit 14: Styrene price (US\$/tonne)



Source: ICICI Direct Research, Bloomberg

Exhibit 15: Key Financial Summary (₹ crore)

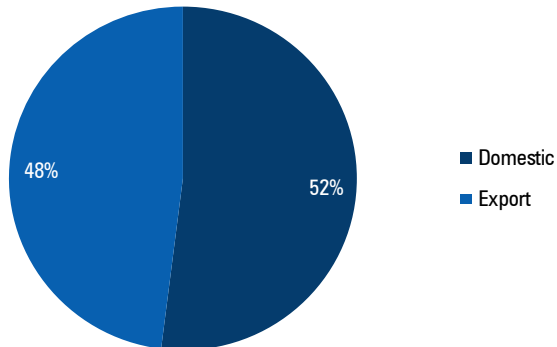
Key Financials	FY17	FY18	FY19	FY20E	FY21E	FY22E	CAGR (FY19-22E)
Net Sales	389	526	626	496	571	611	-1%
EBITDA	29	64	68	28	37	45	-19%
EBITDA Margins (%)	7.4	12.1	10.8	5.6	6.5	7.3	
Net Profit	19	39	47	14	20	24	-28%
EPS (₹)	3.7	7.6	9.0	2.7	3.8	4.7	
P/E	22.4	10.8	9.2	30.2	21.7	17.6	
RoNW (%)	8.6	16.1	16.8	5.9	8.3	10.1	
RoCE (%)	10.0	20.8	20.5	7.5	10.4	12.6	

Source: ICICI Direct Research, Company

Emmbi Industries

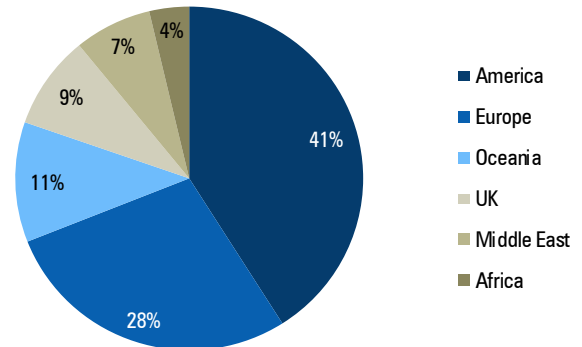
The export segment constitutes ~48% of overall revenues for Emmbi Industries, of which Europe, America and the Middle East together constitute ~85-88% of the export share. In turn, this poses downside risks to export revenue growth owing to suppressed demand due to Covid-19. Further, a fall in polypropylene price along with waiver of export benefit can lead to a fall in realisations and lower gross margins. We lower volume growth along with margins to factor in the negative outcome owing to Covid-19. We value the company at 7x FY21E PER and arrive at a target price of ₹ 50/share. We have **REDUCE** rating on the stock.

Exhibit 16: Geographical break-up



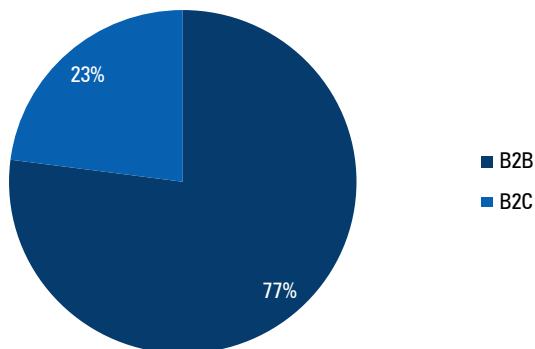
Source: ICICI Direct Research, Company

Exhibit 17: Export revenue break-up



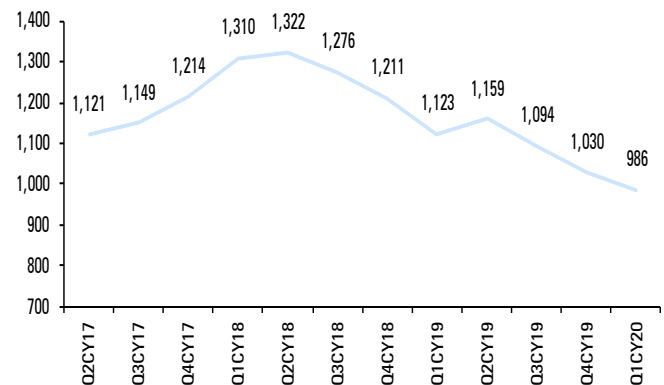
Source: ICICI Direct Research, Company

Exhibit 18: Business vertical break-up



Source: ICICI Direct Research, Company

Exhibit 19: Polypropylene price (US\$/tonne)



Source: ICICI Direct Research, Company

Exhibit 20: Financial Summary

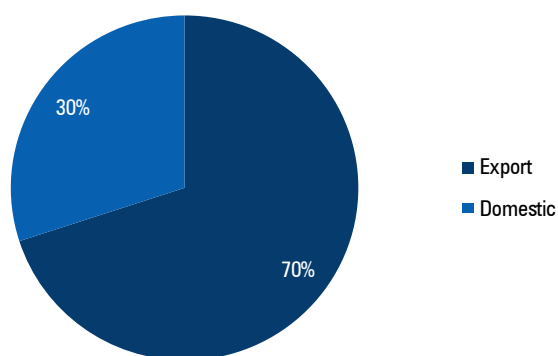
(₹ Crore)	FY17	FY18	FY19	FY20E	FY21E	FY22E	CAGR (FY19-22E)
Net Sales	228	254	289	309	300	297	1%
EBITDA	30	35	41	38	34	33	-10%
EBITDA Margins (%)	13.1	13.8	14.2	12.3	11.2	11.2	
Net Profit	13	15	18	14	13	13	-16%
EPS (₹)	7.2	8.7	10.0	8.2	7.2	7.1	
P/E	7.8	6.5	5.6	6.9	7.8	8.0	
RoNW (%)	14.9	15.6	15.4	11.2	9.1	8.3	
RoCE (%)	15.1	14.7	14.8	13.3	11.3	10.8	

Source: ICICI Direct Research, Company

Kanpur Plastipack

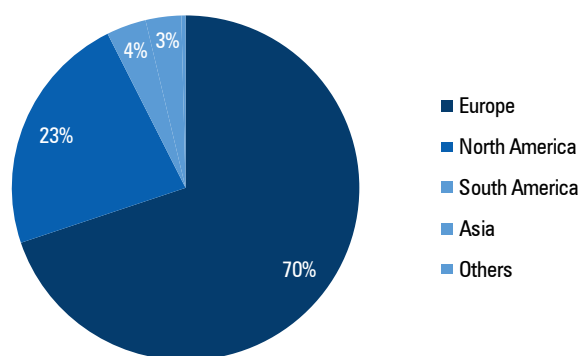
For Kanpur Plastipack, export revenues comprise ~70% of overall revenues of which both America and Europe constitute ~95% of overall revenues. We believe Kanpur Plastipack is at highest risk due to its inclination towards America and Europe. Any slowdown due to Covid-19 can impact the financial growth significantly, going ahead. Further, lower RMAT prices along with subdued demand can translate into more realisation de-growth, leading to poor gross margins. We cut our volume and margins estimates and revise our target price. We value the company at 7x FY21E PER and arrive at a target price of ₹ 30. We have a **SELL** rating on the stock.

Exhibit 21: Geographical break-up



Source: ICICI Direct Research, Company

Exhibit 22: Export revenue break-up



Source: ICICI Direct Research, Company

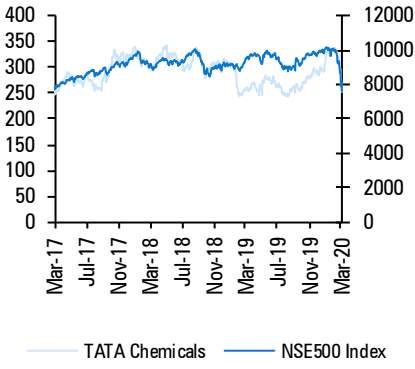
Exhibit 23: Financial Summary

(₹ Crore)	FY17	FY18	FY19	FY20E	FY21E	CAGR (FY19-21E)
Net Sales	244	282	322	301	286	-6%
EBITDA	33	36	27	20	17	-21%
EBITDA Margins (%)	13.7	12.7	8.4	6.6	5.9	
Net Profit	14	17	16	10	6	-40%
EPS (₹)	10.0	11.8	11.3	6.7	4.1	
P/E	4.2	3.6	3.7	6.3	10.2	
RoNW (%)	17.4	16.1	12.8	7.2	4.3	
RoCE (%)	17.2	16.1	12.2	8.5	7.4	

Source: ICICI Direct Research, Company

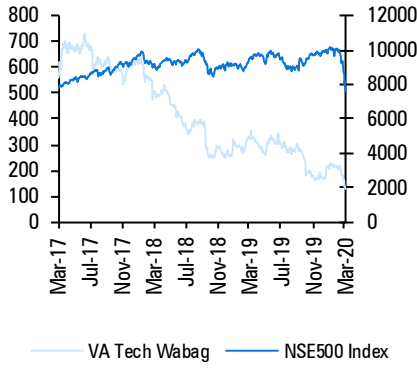
Exhibit 24: Price Charts

Tata Chemicals



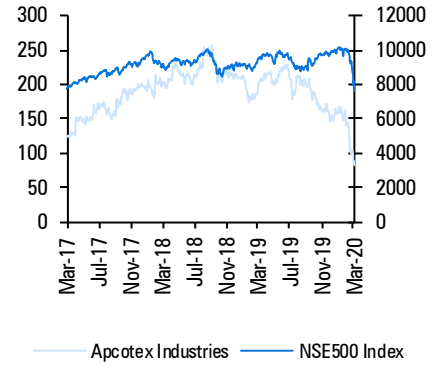
Source: Bloomberg, ICICI Direct Research

VA Tech Wabag



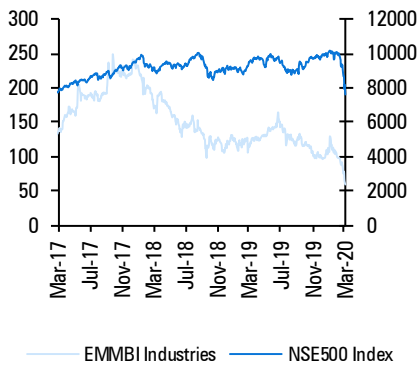
Source: Bloomberg, ICICI Direct Research

Apcotex Industries



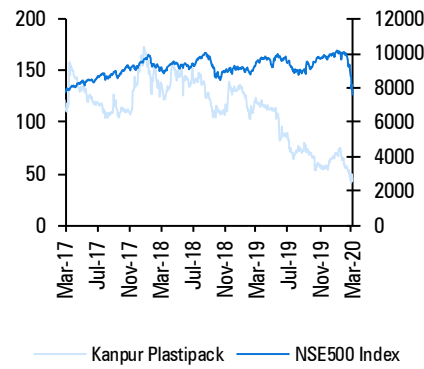
Source: Bloomberg, ICICI Direct Research

Emmbi Industries



Source: Bloomberg, ICICI Direct Research

Kanpur Plastipack



Source: Bloomberg, ICICI Direct Research

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Buy : > 15%

Hold : -5% to 15%;

Reduce : -5% to -15%;

Sell : < -15%



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