

Chemicals continue to deliver amid challenges in others...

About the stock: Incorporated in 1970, SRF started with nylon cord tyres and thereafter diversified into refrigerant gases, speciality chemicals and packaging film to name a few over time.

- Chemical division forms 43% of overall revenue followed by packaging film (39%), technical textile (15%) and others (3%)
- The company exports to more than 90+ countries. Revenue from international market constitutes 57% of overall revenue while rest is from the domestic market segment

Q2FY23 Results: Sales growth was in line with estimates led by chemicals while margins were below expectations due to cost pressure in packaging and technical textiles divisions.

- Reported revenue growth was 31% YoY to ₹ 3727.8 crore, led by chemical (up 62% YoY), technical textile (down 16% YoY), packaging film (up 24% YoY) and other segment (up 16% YoY)
- Gross margins contracted 200bps YoY to 47.6% while EBITDA margin fell 310 bps YoY to 20.6%. Absolute EBITDA was up 14% YoY to ₹ 769.1 crore.
- PAT increased 26% YoY to ₹ 481 crore

What should investors do? The stock appreciated at 62% CAGR in last three years.

- We retain **BUY** rating on SRF on the back of 1) Sustained efforts to ride on increasing opportunities for fluoro chemicals across key industries, 2) entering into new segment of fluoropolymer PTFE and 3) visibility capex in specialty chemical segment

Target Price and Valuation: We value SRF on an SOTP basis to arrive at a target price of ₹ 2900/share (earlier ₹ 2735/share).

Key triggers for future price performance:

- Continuous capex towards speciality chemical on the back of higher consumption of fluoro compounds across agrochemical and pharma to support strong business performance in years to come
- Venturing into PTFE through backward integration of R22 diversifies business risk, to a certain extent
- Control over working capital along with better operational performance to improve FCF generation

Alternate Stock Idea: Apart from SRF, in our chemical coverage, we also like Neogen Chemical.

- Trigger for Neogen Chemical's future revenue growth would be increasing CRAMS opportunity
- BUY with a target price of ₹ 1645



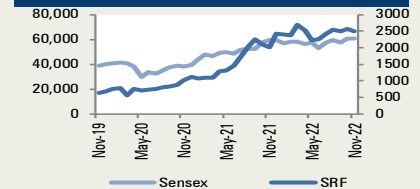
Particulars

Particular	Amount
Market cap (₹ Crore)	73,579
FY22 Total Debt (₹ Crore)	3,655
FY22 Cash & Inv (₹ Crore)	776
EV (₹ Crore)	76,458
52 Week H/L	2865/1973
Equity Capital (₹ Crore)	297.4
Face Value (₹)	10

Shareholding pattern

in %	Dec-21	Mar-22	Jun-22	Sep-22
Promoter	50.7	50.7	50.7	50.5
DII	9.2	8.7	9.4	14.0
FII	19.1	19.6	19.2	19.2
Others	21.0	21.0	20.7	16.2

Price Chart



Recent event & key risks

- Capex announcement of ₹ 604 crore towards chemical segment
- **Key Risk:** (i) Stretched payback of specialty chemicals capex due to lower margins or longer execution. (ii) Persistent pricing pressure in other segments

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Key Financial Summary

(₹ Crore)	FY19	FY20	FY21	FY22	5 year CAGR (FY17-22)	FY23E	FY24E	2 year CAGR (FY22-24E)
Net Revenue	7,099.6	7,209.4	8,400.0	12,433.7	20.9%	14,191.1	17,406.6	18.3%
EBITDA	1,297.0	1,454.9	2,144.9	3,175.9	26.1%	3,204.1	4,197.5	15.0%
EBITDA Margins (%)	18.3%	20.2%	25.5%	25.5%		22.6%	24.1%	
Adj.PAT	641.6	1,019.1	1,197.9	1,888.9	29.7%	1,816.2	2,414.7	13.1%
Adj. EPS (₹)	21.6	34.3	40.3	63.5		61.1	81.2	
EV/EBITDA	59.2x	52.8x	35.7x	24.2x		24.5x	18.7x	
P/E	115.1x	72.4x	61.6x	39.1x		40.6x	30.6x	
ROE (%)	15.5	20.7	17.5	22.1		18.4	20.5	
ROCE (%)	15.2	16.1	18.7	23.8		19.6	22.6	

Key takeaways of recent quarter & conference call highlight

Q2FY23 Results: Strong growth across specialty chemical continues

- **Stellar growth from chemical leads overall performance:** Revenues were up 31% YoY to ₹ 3727.8 crore, led by chemical segment, which was up 62% YoY to ₹ 1830.2 crore. Growth from the chemical segment was driven by new products witnessing significant traction and strong customer engagement on flagship and downstream products. Apart from this, higher realisation growth and stable volumes in the HFC segment along with pharma grade gas (Dymel HFA 134a/P) supported overall growth, to a certain extent
- **Margins under pressure across all segment except specialty chemical:** OPM for the quarter declined 310 bps YoY to 20.6%. OPM from the chemical segment remained at 30.6% (+350bps YoY) while the same from technical textile, packaging film and other segments was at 15.4% (-1270 bps YoY), 9.6% (-1060 bps YoY) & 8% (-4 bps YoY), respectively.

Q2FY23 Earnings Conference Call highlights

- **Speciality Chemical Business**
 - Strong performance in Q2FY23 led by strong traction for new products and downstream derivatives registered healthy growth. Also, traction witnessed from global innovators to encourage R&D team on more complex products
 - The company had launched three new agro products and one new pharma product in H1FY23
 - Furthermore, raw material prices are expected to trend downwards. The company is continuously working on delisting supply chain from any shocks or geopolitical situation
 - MPP project in Dahej is starting to ramp up
 - YTD announced capex of ~₹ 1250 crore. SRF is well on track to fulfil the stated objective the company had spoken of earlier
 - Despite the global scenario, the company has stayed bullish on specialty chemical business as the order book remains strong. SRF is optimistic on achieving growth in the business more than projected at the beginning of the year (+20%)
- **Fluorochemical business**

The segment reported a steady performance on the back of higher realisation and stable volumes despite the impact of seasonally soft quarter.

 - Dymel® HFA 134a/P (pharma grade gas) continued to do well and reported significant growth
 - The management continued to focus on operating facilities as efficiently as possible to maintain business dominant position
 - R-125 completed expansion and is expected to report revenue in H2FY23
 - The management has seen structurally demand trends emerging in refrigerant. They expect to deliver a much stronger performance in the second half. Q3 will remain focused on order booking for some light demand from the US market in Q4 for reg gas
 - The second CMS plant is in final stages of being commissioned. They hope to ramp up capacity from the plant in the near future
 - Additionally, key point is to get product approval for PTFE plant, which is likely to start commercial production very soon. The management expects it to get commercialised in Q4FY23. Revenue can be expected from Q4. Further, SRF has thought of entering the business of new fluoropolymers (PVDF, FPM, etc) but has not committed to it currently

- **Packaging films business**
 - The segment faced several headwinds that impacted the performance during the quarter including significant supply addition in BOPET, global demand slowdown, rising energy costs in Europe and sharp fall in commodity prices. However, this trend was partially offset by sustained demand for BOPP films
 - Successfully commissioned a new BOPP film line in Indore during the quarter. The line will further boost the company's position in the BOPP market in India and ramp up volume growth for Q3 in India. BOPP films demand and margins remain relatively stable
 - BOPET films margins are likely to remain subdued in the near term. For BOPET, the next two quarters will be a bit tight
 - Appropriate order or appropriate price for Hungary division is ~€8-9 million for annual FY22. Due to energy prices, the company has witnessed customers buying from another player
- **Technical textiles business**
 - The performance was impacted by subdued demand for nylon tyre demand. However, melting fabrics and polyester industrial yarn witness healthy growth
 - NTCF demand dropped significantly in the new and replacement market
- **Others**
 - **Coated Fabrics** – SRF maintained its dominant position market leadership in coated fabrics on the back of steady demand
 - **Laminated fabrics** – In laminated fabrics segment, SRF retained its volume and pricing trend. The plant is operating at full capacity.

New capex

- The board has approved a project aggregating ₹ 604 crore for four new plants in the agrochemical space and capacity enhancement of an existing plant at Dahej. The proposed capacity addition is of ~4000 MTPA and estimated period is 10-12 months. The mode of financing is a mix of debt and internal accruals. The project is basically a margin expansion project and will probably be dedicated to AI
- In addition, the board has approved a project to develop a Kilo Lab at Bhiwadi to address the needs of the pharma market at a projected cost of ₹ 9.8 crore

Other points

- Q2FY23 witnessed the impact of volatility in exchange rates where the rupee depreciated against the dollar by ~3%. The US also appreciated against major currency. The effect of the same was part of forex loss of ₹ 36 crore that was incurred during the quarter. SRF is overall a net exporter
- The company is also witnessing some impact on earning interest curves both on rupee and dollar leading to higher interest cost
- The management vision on achieving +20% growth in FY23 for specialty chemical segment is eminently achievable led by a strong order book
- The pricing trend can remain stable for all HFCs. Some volatility can be seen in some HFCs. Overall, in the medium to long term, prices remain stable. Also, SRF has witnessed Chinese pricing coming downwards but there are various factors due to which such production is happening in China. Further the US has reconfirmed duty on 134a for Chinese exports into US. Demand outlook as well as price stability can continue in HFC space, going forward
- Net debt increased by ₹ 300 crore due to capex of ₹ 1250 crore in H1. Capex announcement is expected to remain robust

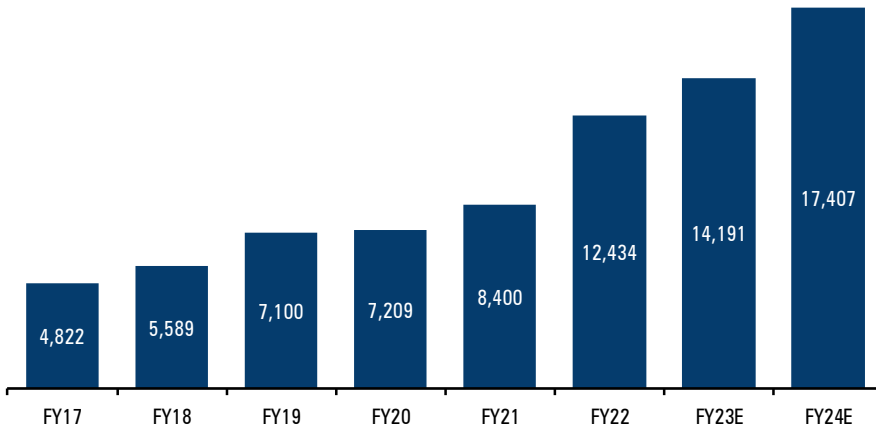
SOTP valuation

In ₹ Crore unless other mentioned	Revenue		EBITDA		EV/EBITDA	EV
	FY23E	FY24E	FY23E	FY24E	FY24E	FY24E
Technical textile	2,247	2,359	337	378	10.0x	3,775
Chemical Business	6,274	8,556	1,882	2,567	29.0x	74,434
Packaging film	5,313	6,116	956	1,223	10.0x	12,233
Other business	357	375	29	30	5.0x	150
Consolidated EV						90,592
Less: Net debt						4,671
Target MCAP						86,272
No. of shares						29.7
Target price/share						2,900
CMP						2,482
Upside/downside						17%

Source: ICICI Direct Research

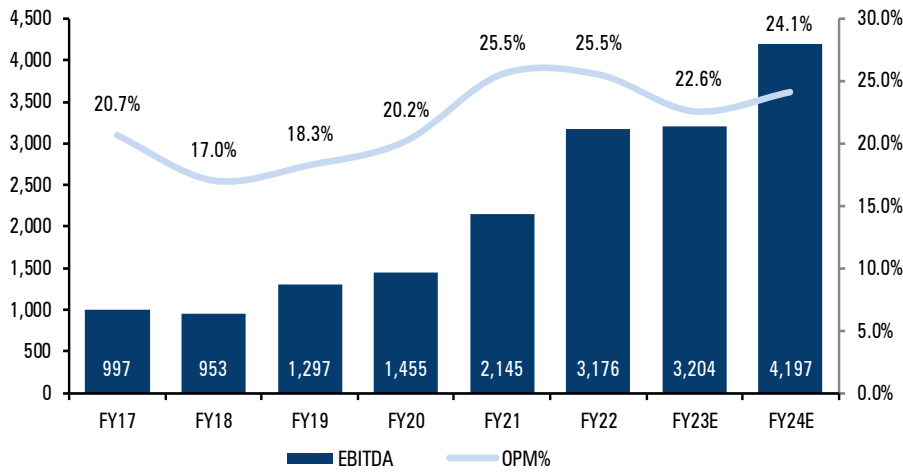
Financial story in charts....

Exhibit 1: Better growth visibility from ongoing capex to aid topline (₹ crore)



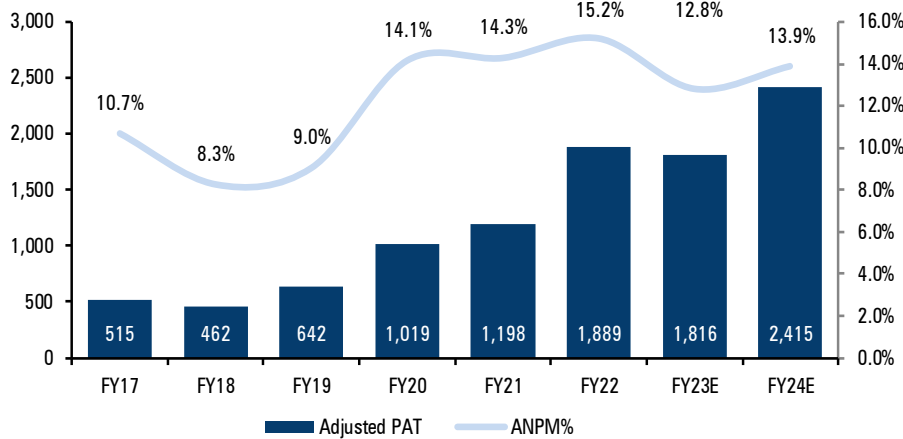
Source: Company, ICICI Direct Research

Exhibit 2: EBITDA (₹ crore) and OPM (%) trend



Source: Company, ICICI Direct Research

Exhibit 3: PAT growth trend (₹ crore)



Source: Company, ICICI Direct Research

Financial summary

Exhibit 4: Profit and loss statement				
	₹ crore			
Year end March	FY21	FY22	FY23E	FY24E
Total Operating Income	8,400.0	12,433.7	14,191.1	17,406.6
Growth (%)	16.5	48.0	14.1	22.7
Raw Material Expenses	4,018.9	6,066.9	7,095.6	8,355.2
Gross Profit	4,381.1	6,366.7	7,095.6	9,051.4
Employee Cost	621.4	780.0	908.2	1,096.6
Other Operating Expenses	1,614.8	2,410.8	2,983.2	3,757.4
EBITDA	2,144.9	3,175.9	3,204.1	4,197.5
Growth (%)	47.4	48.1	0.9	31.0
Other Income	54.5	42.8	51.5	58.8
EBITDA, including OI	2,199.4	3,218.7	3,255.7	4,256.2
Depreciation	453.1	517.2	594.6	747.0
Net Interest Exp.	134.0	115.9	175.2	204.2
Other exceptional items	0.0	0.0	0.0	0.0
PBT	1,612.3	2,585.6	2,485.9	3,305.0
Total Tax	414.4	696.6	669.8	890.5
Tax Rate	25.7%	26.9%	26.9%	26.9%
PAT	1,197.9	1,888.9	1,816.1	2,414.5
Adj.PAT after Minority interest	1,197.9	1,888.9	1,816.2	2,414.7
Adj. EPS (₹)	40.3	63.5	61.1	81.2
Shares Outstanding	6.0	29.7	29.7	29.7

Source: Company, ICICI Direct Research

Exhibit 5: Cash flow statement				
	₹ crore			
Year end March	FY21	FY22	FY23E	FY24E
PBT & Extraordinary	1,609.9	2,585.6	2,486.0	3,305.2
Depreciation	453.1	517.2	594.6	747.0
After other adjustments				
(Inc) / Dec in Working Capital	-123.6	-664.5	-521.7	-571.5
Taxes	-255.3	-401.6	-669.8	-890.5
Others	87.6	69.0	175.2	204.2
CF from operating activities	1,771.7	2,105.7	2,064.3	2,794.4
Purchase of Fixed Assets	-1,204.7	-1,817.1	-3,175.0	-2,100.0
Others	-294.0	229.4	0.0	0.0
CF from investing activities	-1,498.7	-1,587.7	-3,175.0	-2,100.0
Proceeds from issue of shares	750.0	0.2	0.0	0.0
Borrowings (Net)	-691.0	147.2	1,450.0	0.0
Others	-310.1	-354.7	-673.4	-702.4
CF from financing activities	-251.1	-207.3	776.6	-702.4
Net cash flow	21.8	310.7	-334.1	-8.0
Effects of foreign currency translation	0.0	1.5	0.0	0.0
Opening Cash	125.5	282.0	459.4	125.2
Closing Cash	282.0	459.4	125.2	117.2

Source: Company, ICICI Direct Research

Exhibit 6: Balance sheet				
	₹ crore			
Year end March	FY21	FY22	FY23E	FY24E
Liabilities				
Share Capital	60.3	297.4	297.4	297.4
Reserves	6,796.2	8,267.9	9,585.9	11,502.4
Total Shareholders Funds	6,856.4	8,565.4	9,883.3	11,799.8
Minority Interest	0.0	0.0	0.0	0.0
Long Term Borrowings	2,028.8	1,848.5	2,848.5	2,848.5
Net Deferred Tax liability	386.2	677.5	677.5	677.5
Other long term liabilities	43.3	193.4	89.6	109.9
Long term provisions	43.6	51.6	88.9	109.1
Current Liabilities and Provisions				
Short term borrowings	1,439.8	1,806.7	2,256.7	2,256.7
Trade Payables	1,585.2	2,096.4	2,527.2	3,099.8
Other Current Liabilities	537.5	529.9	610.7	749.1
Short Term Provisions	8.7	7.4	8.5	10.4
Total Current Liabilities	3,571.1	4,440.3	5,403.1	6,116.0
Total Liabilities	12,929.4	15,776.6	18,990.9	21,660.7
Assets				
Net Block	7,827.0	8,425.3	11,102.3	13,530.3
Capital Work in Progress	772.3	1,671.6	1,575.0	500.0
Intangible assets under devel.	0.0	0.0	0.0	0.0
Goodwill on Consolidation	0.0	0.0	0.0	0.0
Non-current investments	4.2	4.2	4.2	4.2
Deferred tax assets	18.1	11.6	11.6	11.6
Long term loans and advances	91.1	155.2	126.8	155.5
Other Non Current Assets	277.8	254.4	472.9	580.1
Current Assets, Loans & Advances				
Current Investments	412.5	316.7	316.7	316.7
Inventories	1,465.8	2,138.5	2,488.3	3,052.1
Sundry Debtors	1,274.6	1,792.5	2,138.4	2,622.9
Cash and Bank	282.0	459.4	125.2	117.2
Loans and Advances	11.2	8.8	8.8	8.8
Other Current assets	492.8	538.5	620.7	761.3
Current Assets	3,938.9	5,254.3	5,698.1	6,879.1
Total Assets	12,929.4	15,776.6	18,990.9	21,660.7

Source: Company, ICICI Direct Research

Exhibit 7: Key ratios				
Year end March	FY21	FY22	FY23E	FY24E
Per share data (₹)				
Adj. EPS	40.3	63.5	61.1	81.2
Adj. Cash EPS	55.5	80.9	81.1	106.3
BV	230.5	288.0	332.3	396.7
DPS	24.0	16.8	16.8	16.8
Operating Ratios (%)				
Gross Margin (%)	52.2	51.2	50.0	52.0
EBITDA Margin (%)	25.5	25.5	22.6	24.1
PAT Margin (%)	14.3	15.2	12.8	13.9
Debtor Days	56	53	55	55
Inventory Days	64	63	64	64
Creditor Days	70	62	65	65
Cash Conversion Cycle	51	54	54	54
Return Ratios (%)				
Return on Assets (%)	9.3	12.0	9.6	11.1
RoCE (%)	18.7	23.8	19.6	22.6
Core RoIC (%)	17.6	23.2	17.9	20.9
RoE (%)	17.5	22.1	18.4	20.5
Solvency Ratios				
Total Debt / Equity	0.5	0.4	0.5	0.4
Interest Coverage	13.0	23.3	15.2	17.2
Current Ratio	1.1	1.2	1.1	1.1
Quick Ratio	0.7	0.7	0.6	0.6
Valuation Ratios (x)				
EV/EBITDA	35.7	24.2	24.5	18.7
P/E	61.6	39.1	40.6	30.6
P/B	10.8	8.6	7.5	6.3
EV/Sales	9.1	6.2	5.5	4.5

Source: Company, ICICI Direct Research

Exhibit 8: ICICI Direct coverage universe (Chemicals)

Company	CMP			M Cap (₹ Cr)	EPS (₹)			P/E (x)			EV/EBITDA (x)			RoCE (%)			RoE (%)		
	(₹)	TP(₹)	Rating		FY22	FY23E	FY24E	FY22	FY23E	FY24E	FY22	FY23E	FY24E	FY22	FY23E	FY24E	FY22	FY23E	FY24E
SRF	2482	2,900	Buy	73,579	63.5	61.1	81.3	39.1	40.6	30.5	24.2	24.5	18.7	23.8	19.6	22.6	22.1	18.4	20.5
PI Industries	2987	3,710	Buy	45,324	55.5	67.2	82.4	57.6	47.6	38.8	40.8	34.2	27.8	16.3	17.1	18.2	13.8	14.5	15.2
Aarti Industries	768	885	Hold	27,822	36.1	25.1	31.6	22.7	32.7	25.9	24.0	19.6	16.0	12.0	13.0	13.9	13.3	13.5	14.8
Tata Chemical	1134	1,345	Buy	28,832	47.5	61.2	70.7	23.9	18.5	16.0	14.4	11.1	8.5	6.6	8.1	8.8	6.6	8.0	8.6
Vinati Organics	2016	2,320	Hold	20,717	33.7	40.1	51.5	56.0	47.1	36.7	44.7	37.0	28.3	24.3	23.2	23.9	19.0	19.1	20.5
Sumitomo Chemical	493	570	Buy	24,735	8.5	11.2	12.9	58.1	44.1	38.3	40.3	31.0	26.6	30.2	30.9	28.7	22.0	23.0	21.4
Navin Fluorine	4400	4,570	Hold	21,738	52.3	64.4	91.4	84.2	68.3	48.1	61.2	45.5	31.3	17.8	18.0	20.1	14.0	15.2	18.4
Rallis India	227	250	Hold	4,420	8.4	8.9	12.4	26.9	25.6	18.3	15.5	15.6	11.1	12.7	11.6	15.3	9.7	9.5	12.1
Sudarshan chemical	416	515	Hold	2,882	18.8	19.3	28.5	24.0	23.3	15.8	14.2	12.8	9.6	10.9	11.3	15.4	15.6	14.3	18.3
Neogen Chemicals	1513	1,645	Buy	3,773	17.9	27.2	32.9	79.5	52.2	43.2	41.8	30.2	25.0	12.0	15.0	16.2	10.2	13.6	14.3
Astec Lifesciences	2134	2,186	Hold	4,184	45.1	53.0	66.3	47.3	40.2	32.2	28.9	24.9	19.8	19.3	17.2	18.8	22.3	20.8	20.6

Source: Bloomberg, ICICI Direct Research

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Buy: >15%

Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



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