

Headwinds persist, demand recovery to be slow...

About the stock: Established in 1951, Sudarshan Chemical is a leading player in the Indian colour pigment industry with ~35% market share and is also among the top four players globally.

- It has a wide portfolio of 4,000+ varieties of products of Azos, blue and green, high performance pigments (HPPs), effects, pigment preparations and inorganics
- Among end users, coatings industries contribute highest followed by plastics, inks, cosmetics and other applications

Q3FY23 Results: Sudarshan Chemical's numbers came in below our estimates due to lower-than-expected growth in pigments segment.

- Reported revenue de-growth of 12.3% YoY to ₹ 528 crore, led by lower offtake from pigments (down 13.7%) even as other segment grew 7%
- Gross margins increased 24 bps YoY to ~40.8% while EBITDA margins contracted 439 bps YoY to 7.9% due to escalation in other expenses (up 5.8% YoY)
- EBITDA declined 43.6% YoY to ₹ 41.6 crore. The decline was led by elevated level of energy cost and foreign exchange loss of ₹ 8.6 crore.
- PAT was down 98.4% YoY to ₹ 60 lakh

What should investors do? The stock depreciated at 8.5% CAGR in the last three years.

- We maintain **HOLD** as we believe a margin recovery is key besides sustained revenues traction

Target Price and Valuation: We value Sudarshan Chemicals at 15x P/E FY25E EPS to arrive at a revised target price of ₹ 370/share (earlier ₹ 383/share).

Key triggers for future price performance:

- Upcoming capex bodes well for speciality pigments revenue growth
- Higher share of value added business portfolio is expected to improve the margin profile of the business
- Allocation of incremental FCF towards organic/inorganic growth is likely to expand return ratios further

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

- Trigger for SRF's future revenue growth would be increasing specialty chemical business
- BUY with a target price of ₹ 2550

SUDARSHAN

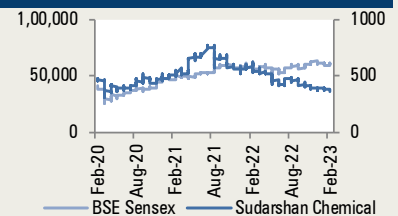
Particulars

Particular	Amount
Market cap (₹ Crore)	2,458
FY22 Total Debt (₹ Crore)	823
FY22 Cash & Inv (₹ Crore)	35
EV (₹ Crore)	3,246
52 Week H/L	613/344
Equity Capital (₹ Crore)	13.8
Face Value (₹)	2

Shareholding pattern

in %	Mar-22	Jun-22	Sep-22	Dec-22
Promoter	35.8	35.8	35.8	35.8
DII	11.5	13.0	14.2	14.3
FII	7.9	6.0	4.2	2.8
Others	44.7	45.1	45.8	47.0

Price Chart



Recent event & key risks

- Proposal for sale of freehold, clear and marketable titled land (~5.76 acre) in Pune
- Key Risk:** (i) Higher RMAT prices and inability to pass on to impact gross margins (ii) Faster than expected recovery in end user demand

Research Analyst

Siddhant Khandekar
siddhant.khandekar@icicisecurities.com

Karan Khona
karan.khona@icicisecurities.com

Key Financial Summary

(₹ Crore)	FY19	FY20	FY21	FY22	5 year CAGR (FY17-22)	FY23E	FY24E	FY25E	3 year CAGR (FY22-24E)
Net Revenue	1,593.1	1,708.2	1,864.1	2,200.8	11.4%	2,196.5	2,424.0	2,704.3	7.1%
EBITDA	204.1	246.3	287.8	274.8	7.8%	188.6	316.3	410.3	14.3%
EBITDA Margins (%)	12.8%	14.4%	15.4%	12.5%		8.6%	13.0%	15.2%	
Adj.PAT	132.8	145.1	141.1	130.0	5.2%	30.5	125.5	170.8	9.5%
Adj. EPS (₹)	8.7	18.5	20.4	18.8		4.4	18.1	24.7	
EV/EBITDA	18.2x	14.6x	12.9x	14.2x		20.2x	11.7x	8.6x	
P/E	65.3x	21.5x	22.1x	24.0x		102.3x	24.8x	18.2x	
ROE (%)	10.7	21.3	19.0	15.6		3.6	13.2	15.9	
ROCE (%)	14.4	15.2	14.4	10.9		4.7	12.3	15.3	

Key takeaways of recent quarter & conference call highlight

Q3FY23 Results: EBITDA margins impacted by escalation in energy, logistics cost and foreign exchange loss

- **Pigment business:** Revenues were down 13.7% YoY to ₹ 483.2 crore of which domestic revenues were at ₹ 251 crore vs. ₹ 306 crore in Q3FY22 & export revenues were at ₹ 232 crore vs. ₹ 254 crore in Q3FY22. Revenues from the speciality pigment declined by 9% YoY to ₹ 341 crore while the same from non-speciality pigment was down by 23% YoY to ₹ 143 crore.
- **Gross margins recovery seen in this quarter:** With reduction in prices of crude oil and its derivatives like benzene and toluene, raw material have started to see some softening. Gross margins for the quarters were at 40.8% (up 24 bps YoY and 206 bps QoQ)

Sudarshan-ESG Disclosure Score*

Score	FY20	FY21	FY22
Environmental	2.4	2.4	2.4
Social	33.3	33.3	22.1
Governance	84.9	84.9	84.9
Overall ESG Score	40.23	40.23	36.5

Source: Bloomberg, ICICI Direct Research, *Score ranges from 0 - 100 with a higher score indicating higher ESG disclosures

Q3FY23 Earnings Conference Call highlights

Management Commentary on financial results Q3FY23

- It was a challenging quarter both on the sales as well as on margins front, not only for Sudarshan but for the whole pigments industry
- We continue to see buying decision deferral in customers due to volatility in customer's prices, which resulted in lower inventory level at customer end
- The plastics segment was especially impacted due to volatility in overall prices, which remained till November 2022. From December, 2022 onwards the company witnessed some demand from the plastic industry
- SCL expects decent Q4 demand from the coating segment. Market share of the company is well maintained in coatings and plastics segment
- Logistics cost coming off from peak level

Capex - Update

- Total capex plan is ~₹ 750 crore of which total capex incurred is ₹ 730 crore
- Overall revenue potential is estimated at ~₹ 1500 crore out of which ~₹ 600 crore could be from new products
- New products have seen a good customer response. Due to demand contraction revenue ramp up is getting delayed
- With current capex getting commissioned the company is aiming for a peak of ₹ 3500 crore revenues. Ramping up will take three to four years from now

Demand outlook for new product

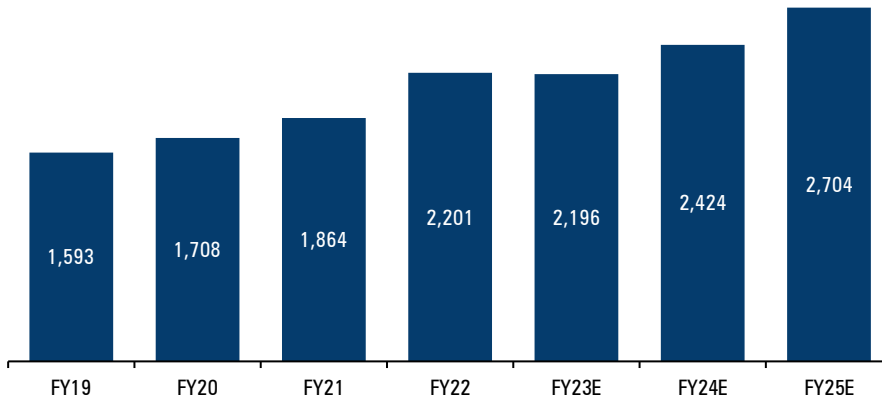
- Ramp up will be faster on new products

Others

- Currently China import is ~@30%
- Debt repayment annually will be ₹ 150-160 crore
- The company is witnessing early signs of a recovery in the plastic industry. SCL is focusing on growing in America and South America market
- Land of 5.76 acres is available for sale in Pune. This will help the company to reduce debt and plan for future growth

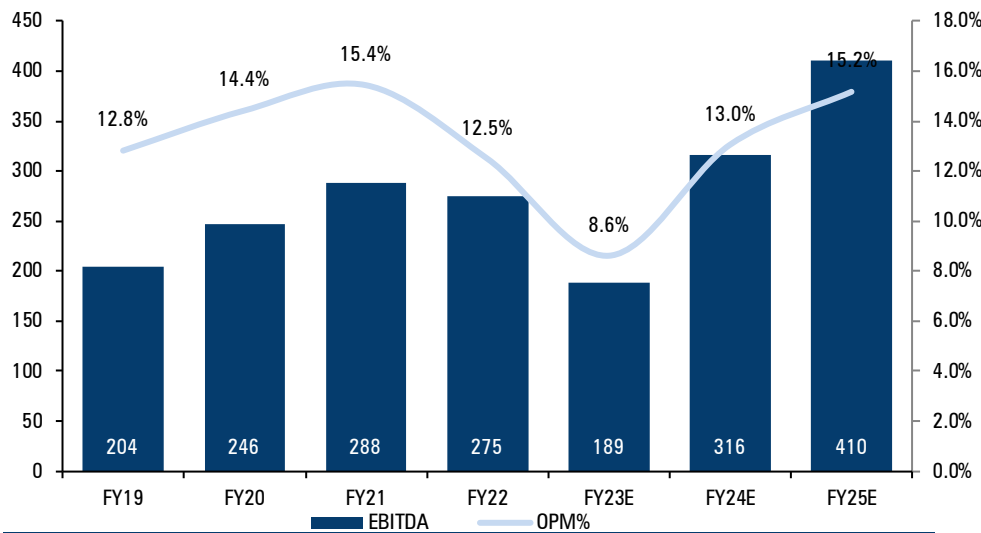
Financial story in charts....

Exhibit 1: Revenue trend (₹ crore)



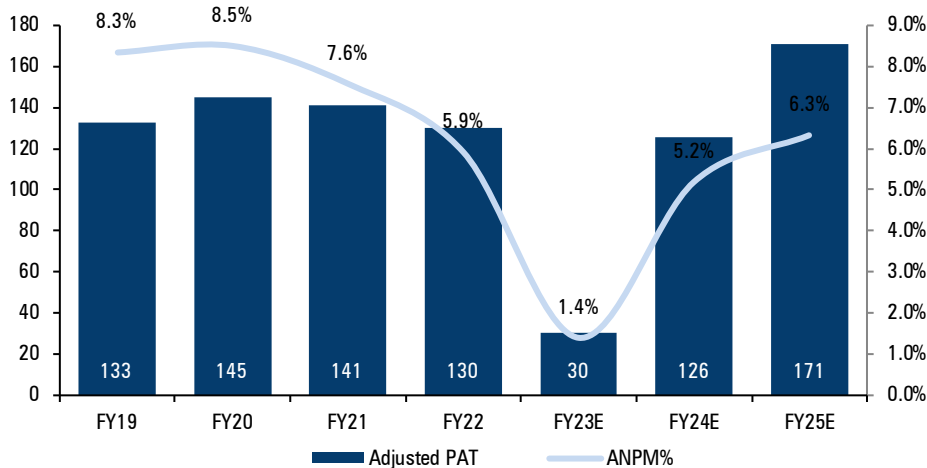
Source: Company, ICICI Direct Research

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	FY25E
Total Operating Income	1,864.1	2,200.8	2,196.5	2,424.0	2,704.3
Growth (%)	9.1	18.1	-0.2	10.4	11.6
Raw Material Expenses	1,060.5	1,270.4	1,312.8	1,400.7	1,545.4
Gross Profit	803.7	930.4	883.6	1,023.3	1,158.9
Gross Profit Margins (%)	43.1	42.3	40.2	42.2	42.9
Employee Expenses	155.7	184.0	183.9	201.2	224.5
Other Expenditure	360.2	471.6	511.2	505.8	524.2
Total Operating Expenditure	1,576.4	1,926.0	2,007.9	2,107.7	2,294.1
EBITDA	287.8	274.8	188.6	316.3	410.3
Growth (%)	16.8	-4.5	-31.4	67.7	29.7
Interest	17.9	19.4	37.4	41.0	36.0
Depreciation	86.5	89.3	113.7	120.0	160.0
Other Income	7.0	5.0	4.4	12.1	13.5
PBT before Exceptional Item	190.4	171.1	41.9	167.4	227.8
Less: Exceptional Items	0.0	0.0	0.0	0.0	0.0
PBT after Exceptional Items	190.4	171.1	41.9	167.4	227.8
Total Tax	49.3	41.2	11.5	41.8	56.9
PAT before MI	141.1	130.0	30.5	125.5	170.8
PAT	141.1	130.0	30.5	125.5	170.8
Growth (%)	-2.7	-7.9	-76.6	312.2	36.1
EPS (Adjusted)	20.4	18.8	4.4	18.1	24.7

Source: Company, ICICI Direct Research

Exhibit 5: Cash flow statement					
	₹ crore				
(Year-end March)	FY21	FY22	FY23E	FY24E	FY25E
Profit/(Loss) after taxation	151.6	171.1	30.5	125.5	170.8
Add: Depreciation & Amortization	86.5	89.3	113.7	120.0	160.0
Net Increase in Current Assets	-176.1	-143.1	0.0	-112.4	-138.0
Net Increase in Current Liabilities	85.4	82.8	0.8	55.8	68.4
Others	17.8	-22.0	37.4	41.0	36.0
CF from Operating activities	165.2	178.1	182.4	230.0	297.2
Investments	0.0	0.0	0.0	0.0	0.0
(Purchase)/Sale of Fixed Assets	-269.6	-310.2	-50.0	-50.0	-50.0
Others	4.2	3.6	1.2	1.2	1.2
CF from Investing activities	-265.4	-306.6	-48.8	-48.8	-48.8
(inc)/Dec in Loan	126.3	198.3	-80.0	-100.0	-100.0
Dividend & Dividend tax	-0.4	-41.1	-7.8	-32.3	-44.0
Other	-17.4	-19.4	-37.4	-41.0	-36.0
CF from Financing activities	108.5	137.8	-125.3	-173.3	-180.0
Net Cash Flow	8.2	9.3	8.3	7.8	68.4
Cash and Cash Equivalent	15.6	23.8	35.3	43.5	51.3
Cash	23.8	33.2	43.5	51.3	119.7
Free Cash Flow	-104.4	-132.1	132.4	180.0	247.2

Source: Company, ICICI Direct Research

Exhibit 6: Balance sheet					
	₹ crore				
(Year-end March)	FY21	FY22	FY23E	FY24E	FY25E
Equity Capital	13.8	13.8	13.8	13.8	13.8
Reserve and Surplus	729.7	819.3	842.0	935.1	1,062.0
Total Shareholders funds	743.6	833.2	855.8	949.0	1,075.8
Total Debt	614.6	819.3	739.3	639.3	539.3
Deferred Tax Liability	52.9	59.5	60.7	61.9	63.2
Long-Term Provisions	23.9	26.4	26.9	27.4	28.0
Other Non Current Liabilities	15.5	17.5	17.8	18.2	18.6
Source of Funds	1,450.5	1,755.8	1,700.5	1,695.8	1,724.8
Gross Block - Fixed Assets	939.9	1,177.6	1,437.6	1,562.3	1,612.3
Accumulated Depreciation	331.8	352.9	466.5	586.5	746.5
Net Block	608.0	824.8	971.1	975.8	865.8
Capital WIP	278.3	284.7	74.7	0.0	0.0
Goodwill	6.8	6.8	6.8	6.8	6.8
Fixed Assets	893.2	1,116.3	1,052.6	982.6	872.6
Investments	1.3	1.7	1.7	1.7	1.7
Other non-Current Assets	77.3	45.6	46.5	47.5	48.4
Inventory	411.6	566.0	564.9	623.4	695.5
Debtors	484.7	500.7	499.7	551.4	615.2
Other Current Assets	111.5	103.2	105.3	107.4	109.5
Cash	23.8	35.3	43.5	51.3	119.7
Total Current Assets	1,031.6	1,205.1	1,213.4	1,333.5	1,539.9
Creditors	441.1	521.8	520.7	574.7	641.1
Provisions	2.3	2.5	2.5	2.6	2.6
Other Current Liabilities	109.4	88.7	90.5	92.3	94.1
Total Current Liabilities	552.9	612.9	613.7	669.5	737.9
Net Current Assets	478.7	592.2	599.6	664.0	802.0
Application of Funds	1,450.5	1,755.8	1,700.5	1,695.8	1,724.7

Source: Company, ICICI Direct Research

Exhibit 7: Key ratios					
(Year-end March)	FY21	FY22	FY23E	FY24E	FY25E
Per share data (₹)					
Reported EPS	20.4	18.8	4.4	18.1	24.7
Cash EPS	15.1	13.9	3.3	13.5	18.3
BV per share	107.4	120.4	123.6	137.1	155.4
Cash per Share	3.4	5.1	6.3	7.4	17.3
Dividend per share	5.3	4.8	1.1	4.7	6.4
Operating Ratios (%)					
Gross Profit Margins	43.1	42.3	40.2	42.2	42.9
EBITDA margins	15.4	12.5	8.6	13.0	15.2
PAT Margins	7.6	5.9	1.4	5.2	6.3
Cash Conversion Cycle	89.1	90.4	90.4	90.4	90.4
Asset Turnover	2.0	1.9	1.5	1.6	1.7
EBITDA conversion Rate	57.4	64.8	96.7	72.7	72.4
Return Ratios (%)					
RoE	19.0	15.6	3.6	13.2	15.9
RoCE	14.4	10.9	4.7	12.3	15.3
RoC	17.5	12.9	4.7	11.9	15.6
Valuation Ratios (x)					
P/E	17.7	19.2	81.8	19.9	14.6
EV / EBITDA	10.7	11.9	16.9	9.7	7.1
EV / Net Sales	1.7	1.5	1.5	1.3	1.1
Market Cap / Sales	1.3	1.1	1.1	1.0	0.9
Price to Book Value	3.4	3.0	2.9	2.6	2.3
Solvency Ratios					
Debt / EBITDA	2.1	3.0	3.9	2.0	1.3
Debt / Equity	0.8	1.0	0.9	0.7	0.5
Current Ratio	1.8	1.9	1.9	1.9	1.9

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	2182	2,550	Buy	64,894	63.5	58.3	73.6	34.4	37.4	29.7	21.3	22.4	17.9	23.8	18.9	21.0	22.1	17.7	19.0
PI Industries	3620	3,930	Hold	50,572	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
Tata Chemical	965	1,170	Buy	24,642	93.0	97.3	110.6	10.4	9.9	8.7	6.6	5.5	5.4	11.8	11.3	11.7	11.6	11.0	11.2
Vinati Organics	1888	2,055	Hold	19,405	33.7	41.6	48.0	56.0	45.4	39.4	44.7	35.6	30.3	24.3	23.9	22.4	19.0	19.7	19.2
Sumitomo Chemical	438	525	Buy	21,860	8.5	10.8	12.4	51.6	40.5	35.2	35.7	28.4	24.2	30.2	30.1	28.1	22.0	22.4	20.9
Navin Fluorine	4162	4,285	Hold	20,668	52.3	65.7	86.0	79.6	63.4	48.4	57.9	42.3	31.2	17.8	18.3	19.1	14.0	15.5	17.4
Rallis India	224	223	Hold	4,353	8.4	8.7	11.8	26.5	25.7	18.9	15.2	15.5	11.4	12.7	11.4	14.7	9.7	9.4	11.6
Sudarshan chemical	360	370	Hold	2,458	18.8	4.4	18.1	19.2	81.8	19.9	11.9	16.9	9.7	10.9	4.7	12.3	15.6	3.6	13.2
Neogen Chemicals	1245	1,645	Buy	3,109	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	1387	1,307	Reduce	2,718	45.1	27.5	39.9	30.8	50.4	34.8	19.4	26.8	19.7	19.3	10.1	12.6	22.3	12.0	14.8

Source: Bloomberg, ICICI Direct Research

RATING RATIONALE

ICICI Direct endeavours to provide objective opinions and recommendations. ICICI Direct assigns ratings to its stocks according to their notional target price vs. current market price and then categorizes them as Buy, Hold, Reduce and Sell. The performance horizon is two years unless specified and the notional target price is defined as the analysts' valuation for a stock

Buy: >15%

Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



Pankaj Pandey

Head – Research

pankaj.pandey@icicisecurities.com

ICICI Direct Research Desk,
ICICI Securities Limited,
1st Floor, Akruiti Trade Centre,
Road No 7, MIDC,
Andheri (East)
Mumbai – 400 093
research@icicidirect.com

ANALYST CERTIFICATION

I/We, Siddhant Khandekar, Inter CA, Karan Khona, CA Research Analysts, authors and the names subscribed to this report, hereby certify that all of the views expressed in this research report accurately reflect our views about the subject issuer(s) or securities. We also certify that no part of our compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report. It is also confirmed that above mentioned Analysts of this report have not received any compensation from the companies mentioned in the report in the preceding twelve months and do not serve as an officer, director or employee of the companies mentioned in the report.

Terms & conditions and other disclosures:

ICICI Securities Limited (ICICI Securities) is a full-service, integrated investment banking and is, inter alia, engaged in the business of stock brokering and distribution of financial products.

ICICI Securities is Sebi registered stock broker, merchant banker, investment adviser, portfolio manager and Research Analyst. ICICI Securities is registered with Insurance Regulatory Development Authority of India Limited (IRDAI) as a composite corporate agent and with PFRDA as a Point of Presence. ICICI Securities Limited Research Analyst SEBI Registration Number – INH000000990. ICICI Securities Limited SEBI Registration is INZ000183631 for stock broker. ICICI Securities is a subsidiary of ICICI Bank which is India's largest private sector bank and has its various subsidiaries engaged in businesses of housing finance, asset management, life insurance, general insurance, venture capital fund management, etc. ("associates"), the details in respect of which are available on www.icicibank.com.

ICICI Securities is one of the leading merchant bankers/ underwriters of securities and participate in virtually all securities trading markets in India. We and our associates might have investment banking and other business relationship with a significant percentage of companies covered by our Investment Research Department. ICICI Securities and its analysts, persons reporting to analysts and their relatives are generally prohibited from maintaining a financial interest in the securities or derivatives of any companies that the analysts cover.

Recommendation in reports based on technical and derivative analysis centre on studying charts of a stock's price movement, outstanding positions, trading volume etc as opposed to focusing on a company's fundamentals and, as such, may not match with the recommendation in fundamental reports. Investors may visit icicidirect.com to view the Fundamental and Technical Research Reports.

Our proprietary trading and investment businesses may make investment decisions that are inconsistent with the recommendations expressed herein.

ICICI Securities Limited has two independent equity research groups: Institutional Research and Retail Research. This report has been prepared by the Retail Research. The views and opinions expressed in this document may or may not match or may be contrary with the views, estimates, rating, and target price of the Institutional Research.

The information and opinions in this report have been prepared by ICICI Securities and are subject to change without any notice. The report and information contained herein is strictly confidential and meant solely for the selected recipient and may not be altered in any way, transmitted to, copied or distributed, in part or in whole, to any other person or to the media or reproduced in any form, without prior written consent of ICICI Securities. While we would endeavour to update the information herein on a reasonable basis, ICICI Securities is under no obligation to update or keep the information current. Also, there may be regulatory, compliance or other reasons that may prevent ICICI Securities from doing so. Non-rated securities indicate that rating on a particular security has been suspended temporarily and such suspension is in compliance with applicable regulations and/or ICICI Securities policies, in circumstances where ICICI Securities might be acting in an advisory capacity to this company, or in certain other circumstances.

This report is based on information obtained from public sources and sources believed to be reliable, but no independent verification has been made nor is its accuracy or completeness guaranteed. This report and information herein is solely for informational purpose and shall not be used or considered as an offer document or solicitation of offer to buy or sell or subscribe for securities or other financial instruments. Though disseminated to all the customers simultaneously, not all customers may receive this report at the same time. ICICI Securities will not treat recipients as customers by virtue of their receiving this report. Nothing in this report constitutes investment, legal, accounting and tax advice or a representation that any investment or strategy is suitable or appropriate to your specific circumstances. The securities discussed and opinions expressed in this report may not be suitable for all investors, who must make their own investment decisions, based on their own investment objectives, financial positions and needs of specific recipient. This may not be taken in substitution for the exercise of independent judgment by any recipient. The recipient should independently evaluate the investment risks. The value and return on investment may vary because of changes in interest rates, foreign exchange rates or any other reason. ICICI Securities accepts no liabilities whatsoever for any loss or damage of any kind arising out of the use of this report. Past performance is not necessarily a guide to future performance. Investors are advised to see Risk Disclosure Document to understand the risks associated before investing in the securities markets. Actual results may differ materially from those set forth in projections. Forward-looking statements are not predictions and may be subject to change without notice.

ICICI Securities or its associates might have managed or co-managed public offering of securities for the subject company or might have been mandated by the subject company for any other assignment in the past twelve months.

ICICI Securities or its associates might have received any compensation from the companies mentioned in the report during the period preceding twelve months from the date of this report for services in respect of managing or co-managing public offerings, corporate finance, investment banking or merchant banking, brokerage services or other advisory service in a merger or specific transaction.

ICICI Securities or its associates might have received any compensation for products or services other than investment banking or merchant banking or brokerage services from the companies mentioned in the report in the past twelve months.

ICICI Securities encourages independence in research report preparation and strives to minimize conflict in preparation of research report. ICICI Securities or its associates or its analysts did not receive any compensation or other benefits from the companies mentioned in the report or third party in connection with preparation of the research report. Accordingly, neither ICICI Securities nor Research Analysts and their relatives have any material conflict of interest at the time of publication of this report.

Compensation of our Research Analysts is not based on any specific merchant banking, investment banking or brokerage service transactions.

ICICI Securities or its subsidiaries collectively or Research Analysts or their relatives do not own 1% or more of the equity securities of the Company mentioned in the report as of the last day of the month preceding the publication of the research report.

Since associates of ICICI Securities and ICICI Securities as a entity are engaged in various financial service businesses, they might have financial interests or actual/beneficial ownership of one percent or more or other material conflict of interest various companies including the subject company/companies mentioned in this report.

ICICI Securities may have issued other reports that are inconsistent with and reach different conclusion from the information presented in this report.

Neither the Research Analysts nor ICICI Securities have been engaged in market making activity for the companies mentioned in the report.

We submit that no material disciplinary action has been taken on ICICI Securities by any Regulatory Authority impacting Equity Research Analysis activities.

This report is not directed or intended for distribution to, or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject ICICI Securities and affiliates to any registration or licensing requirement within such jurisdiction. The securities described herein may or may not be eligible for sale in all jurisdictions or to certain category of investors. Persons in whose possession this document may come are required to inform themselves of and to observe such restriction.