

Green shoots visible with demand revival, margin improvement...

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

Q4FY23 Results: Beat across the board driven by demand revival.

- Reported revenue growth of 10.2% YoY and 30.9% QoQ to ₹ 691.2 crore, led by growth from pigments (up 6.2% YoY, 23% QoQ) and decent growth in other segment (up 34% YoY, 106% QoQ)
- Gross margins increased 112 bps YoY and 120 bps to ~42% while EBITDA margins contracted 147 bps YoY and grew 437 bps QoQ to 12.3%. Absolute EBITDA came in at ₹ 84.7 crore
- PAT was down 27.1% YoY to ₹ 32.6 crore

What should investors do? The stock appreciated at 6% CAGR in last three years.

- We upgrade our rating from HOLD to **BUY** on the back of 1) New product pipeline that caters to niche category to boost revenue growth, 2) gradual improvement in margins, 3) upbeat management guidance to cross ₹ 3000-3300 crore topline on ramping up of new products in pigments

Target Price and Valuation: We value Sudarshan Chemicals at 19x P/E FY25E EPS to arrive at a revised target price of ₹ 555/share (earlier ₹ 370/share).

Key triggers for future price performance:

- Demand recovery from end user industry especially from pigments and plastics industry
- Higher share of value-added business portfolio expected to improve margin profile of the business
- Allocation of incremental FCF towards organic/inorganic growth 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 ₹ 3000

SUDARSHAN

Particulars

Particular	Amount
Market cap (₹ Crore)	3,171
FY22 Total Debt (₹ Crore)	829
FY22 Cash & Inv (₹ Crore)	29
EV (₹ Crore)	3,971
52 Week H/L	496/341
Equity Capital (₹ Crore)	13.8
Face Value (₹)	2

Shareholding pattern

in %	Jun-22	Sep-22	Dec-22	Mar-22
Promoter	35.8	35.8	35.8	35.8
DII	13.0	14.2	14.3	14.2
FII	6.0	4.2	2.8	3.1
Others	45.1	45.8	47.0	46.9

Price Chart



Recent event & key risks

- Sold land in Pune of 5.76 acre for ₹ 356 crore to Birla Estate Pvt Ltd
- Key Risk:** (i) Higher RMAT prices and inability to pass on to impact gross margins (ii) Slowdown in end user demand

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Key Financial Summary

(₹ Crore)	FY19	FY20	FY21	FY22	FY23	5 year CAGR (FY18-23)	FY24E	FY25E	2 year CAGR (FY23-25E)
Net Revenue	1,593.1	1,708.2	1,864.1	2,200.8	2,301.7	8.6%	2,603.9	2,933.7	12.9%
EBITDA	204.1	246.3	287.8	274.8	210.7	7.3%	340.4	449.5	46.1%
EBITDA Margins (%)	12.8%	14.4%	15.4%	12.5%	9.2%		13.1%	15.3%	
Adj. PAT	132.8	145.1	141.1	130.0	44.8	10.7%	144.3	201.1	111.9%
Adj. EPS (₹)	8.7	18.5	20.4	18.8	6.5		20.8	29.1	
EV/EBITDA	15.1x	12.1x	10.7x	11.9x	15.6x		8.5x	6.0x	
P/E	65.3x	17.2x	17.7x	19.2x	55.6x		17.3x	12.4x	
ROE (%)	10.7	21.3	19.0	15.6	5.4		15.4	18.5	
ROCE (%)	14.4	15.2	14.4	10.9	5.7		15.8	19.9	

Key takeaways of recent quarter & conference call highlight

Q4FY23 Results: EBITDA margins impacted by escalation hike in energy, logistics cost and foreign exchange loss

- **Pigment business:** Revenues were up 6.2% YoY and 23% QoQ to ₹ 593 crore of which domestic revenues were at ₹ 301 crore vs. ₹ 286 crore in Q4FY22 and export revenues were at ₹ 293 crore vs. ₹ 272 crore in Q4FY22. Revenue from the specialty pigment increased 8% YoY and 21% QoQ to ₹ 412 crore while the same from non-speciality pigment was up 3% YoY and 21% QoQ to ₹ 181 crore
- **Gross margin recovery seen in this quarter:** With a reduction in prices of crude oil and its derivatives like benzene and toluene, raw material has started to see some softening. Gross margins for the quarter were at 42% (up 112 bps YoY, 120 bps QoQ)

Q4FY23 Earnings Conference Call highlights

- The company is witnessing early signs of a demand revival in both domestic and exports market from both plastics and pigments segment
- Sudarshan witnessed a softening in raw material prices in Q4FY23 due to a drop in basic cost drivers such as crude oil, benzene, toluene, etc. This should help the company to stabilise gross margins level
- Apart from raw material cost, the company also witnessed softening of energy cost in Q4 led by a reduction in coal prices, which will benefit manufacturing costs in coming quarters. Logistics cost are also coming down from peak level and the management expects the trend to continue in coming quarters
- The company has completed the sale of its freehold land of ~5.76 acres at Pune, for a total net consideration of ₹ 356 crore to Birla Estates Pvt Ltd
- For new products, the company is in the process of getting approvals and ramping of sales. Approval time is expected to be three to six months
- New products will cater to both domestic and export side market
- There was a volume pick-up in Q4 sequentially led by growth in both exports and domestic market. The management is focusing on specialty product side and expects the ratio to move up from current level of 69:31
- With capacity ramping up and pricing to stabilised management expects revenue to be ~3000-3300 crore in the coming three to four years

Capex

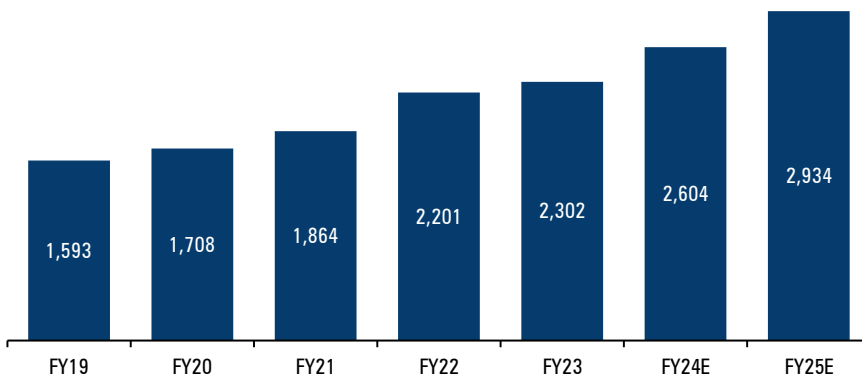
- The company has successfully commissioned all capex projects in FY23
- For new product line, the company is getting good response from the customers and the products are in advanced stages of execution
- Given the global scenario, the management expects a slow ramp up in the short-term but remains confident in the mid-term that the capex will benefit the topline strongly in coming years
- The management expects no new capex except regular maintenance capex

Tailwinds for industry

- Consolidation of top players in industry
- Supply disruption from prominent players in North America
- Emergence of India as a key global manufacturing industry
- Softening of raw material prices and energy cost

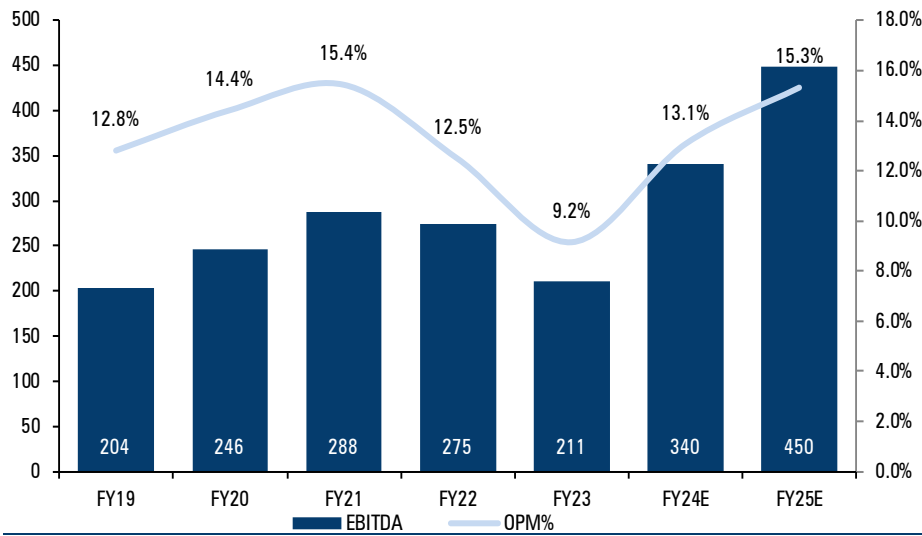
Financial story in charts....

Exhibit 1: Revenue trend (₹ crore)



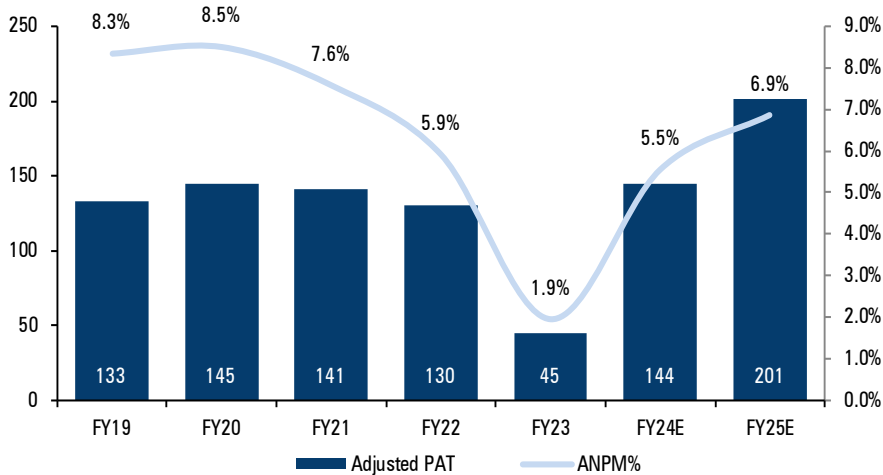
Source: Company, ICICI Direct Research

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



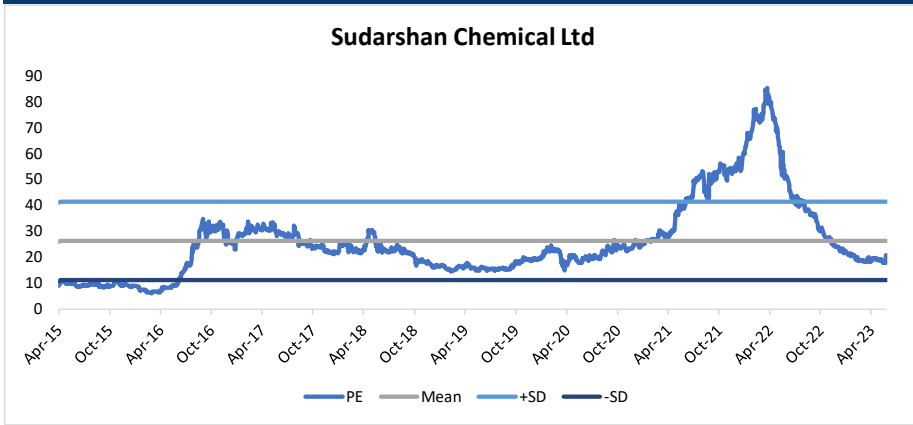
Source: Company, ICICI Direct Research

Exhibit 3: PAT growth trend (₹ crore)



Source: Company, ICICI Direct Research

Exhibit 4: PE Band



Financial summary

Exhibit 5: Profit and loss statement				
	₹ crore			
(Year-end March)	FY22	FY23	FY24E	FY25E
Total Operating Income	2,200.8	2,301.7	2,603.9	2,933.7
Growth (%)	18.1	4.6	13.1	12.7
Raw Material Expenses	1,270.4	1,368.3	1,504.5	1,673.5
Gross Profit	930.4	933.5	1,099.5	1,260.2
Gross Profit Margins (%)	42.3	40.6	42.2	43.0
Employee Expenses	184.0	184.0	216.1	243.5
Other Expenditure	471.6	538.8	543.0	567.2
Total Operating Expenditure	1,926.0	2,091.1	2,263.6	2,484.2
EBITDA	274.8	210.7	340.4	449.5
Growth (%)	-4.5	-23.3	61.6	32.1
Interest	19.4	41.5	41.0	36.0
Depreciation	89.3	114.2	120.0	160.0
Other Income	5.0	4.8	13.0	14.7
PBT before Exceptional Item	171.1	59.8	192.4	268.2
Less: Exceptional Items	0.0	0.0	0.0	0.0
PBT after Exceptional Items	171.1	59.8	192.4	268.2
Total Tax	41.2	15.0	48.1	67.0
PAT before MI	130.0	44.8	144.3	201.1
PAT	130.0	44.8	144.3	201.1
Growth (%)	-7.9	-65.5	222.2	39.4
EPS (Adjusted)	18.8	6.5	20.8	29.1

Source: Company, ICICI Direct Research

Exhibit 6: Cash flow statement				
	₹ crore			
(Year-end March)	FY22	FY23	FY24E	FY25E
Profit/(Loss) after taxation	171.1	59.7	144.3	201.1
Add: Depreciation & Amortization	89.3	114.2	120.0	160.0
Net Increase in Current Assets	-143.1	69.4	-131.8	-143.6
Net Increase in Current Liabilities	82.8	11.0	69.1	75.2
Others	-22.0	32.6	41.0	36.0
CF from Operating activities	178.1	287.0	242.5	328.7
Investments	0.0	0.0	0.0	0.0
(Purchase)/Sale of Fixed Assets	-310.2	-190.6	250.0	-50.0
Others	3.6	1.3	1.2	1.2
CF from Investing activities	-306.6	-189.3	251.2	-48.8
(inc)/Dec in Loan	198.3	-32.8	-400.0	-100.0
Dividend & Dividend tax	-41.1	-34.3	-37.2	-51.8
Other	-19.4	-35.7	-41.0	-36.0
CF from Financing activities	137.8	-102.7	-478.2	-187.8
Net Cash Flow	9.3	-4.9	15.5	92.1
Cash and Cash Equivalent	23.8	35.3	29.4	44.9
Cash	33.2	30.4	44.9	137.0
Free Cash Flow	-132.1	96.4	492.5	278.7

Source: Company, ICICI Direct Research

Exhibit 7: Balance sheet				
	₹ crore			
(Year-end March)	FY22	FY23	FY24E	FY25E
Equity Capital	13.8	13.8	13.8	13.8
Reserve and Surplus	819.3	814.4	921.5	1,070.8
Total Shareholders funds	833.2	828.2	935.3	1,084.6
Total Debt	819.3	829.1	429.1	329.1
Deferred Tax Liability	59.5	71.6	73.1	74.5
Long-Term Provisions	26.4	28.2	28.8	29.4
Other Non Current Liabilities	17.5	12.8	13.1	13.3
Source of Funds	1,755.8	1,770.0	1,479.3	1,530.9
Gross Block - Fixed Assets	1,177.6	1,586.4	1,380.9	1,430.9
Accumulated Depreciation	352.9	467.1	587.1	747.1
Net Block	824.8	1,119.3	793.8	683.8
Capital WIP	284.7	44.5	0.0	0.0
Goodwill	6.8	6.8	6.8	6.8
Fixed Assets	1,116.3	1,170.6	800.6	690.6
Investments	1.7	2.1	2.1	2.1
Other non-Current Assets	45.6	54.4	55.5	56.6
Inventory	566.0	494.1	559.0	629.7
Debtors	500.7	486.1	550.0	619.6
Other Current Assets	103.2	155.2	158.3	161.5
Cash	35.3	29.4	44.9	137.0
Total Current Assets	1,205.1	1,164.9	1,312.2	1,547.9
Creditors	521.8	508.7	575.5	648.4
Provisions	2.5	2.7	2.8	2.8
Other Current Liabilities	88.7	110.6	112.8	115.0
Total Current Liabilities	612.9	622.0	691.1	766.3
Net Current Assets	592.2	542.9	621.1	781.6
Application of Funds	1,755.8	1,770.0	1,479.3	1,530.9

Source: Company, ICICI Direct Research

Exhibit 8: Key ratios				
(Year-end March)	FY22	FY23	FY24E	FY25E
Per share data (₹)				
Reported EPS	18.8	6.5	20.8	29.1
Cash EPS	13.9	4.8	15.5	21.6
BV per share	120.4	119.6	135.1	156.7
Cash per Share	5.1	4.2	6.5	19.8
Dividend per share	4.8	1.7	5.4	7.5
Operating Ratios (%)				
Gross Profit Margins	42.3	40.6	42.2	43.0
EBITDA margins	12.5	9.2	13.1	15.3
PAT Margins	5.9	1.9	5.5	6.9
Cash Conversion Cycle	90.4	74.8	74.8	74.8
Asset Turnover	1.9	1.5	1.9	2.1
EBITDA conversion Rate	64.8	136.3	71.3	73.1
Return Ratios (%)				
RoE	15.6	5.4	15.4	18.5
RoCE	10.9	5.7	15.8	19.9
RoIC	12.9	5.7	15.4	20.8
Valuation Ratios (x)				
P/E	19.2	55.6	17.3	12.4
EV / EBITDA	11.9	15.6	8.5	6.0
EV / Net Sales	1.5	1.4	1.1	0.9
Market Cap / Sales	1.1	1.1	1.0	0.8
Price to Book Value	3.0	3.0	2.7	2.3
Solvency Ratios				
Debt / EBITDA	3.0	3.9	1.3	0.7
Debt / Equity	1.0	1.0	0.5	0.3
Current Ratio	1.9	1.8	1.8	1.8

Source: Company, ICICI Direct Research

Exhibit 9: 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	2570	3,000	Buy	76,218	63.5	72.7	79.4	34.4	30.0	27.5	21.3	19.3	17.8	23.8	21.9	20.6	22.1	20.9	19.4
PI Industries	3289	3,880	Buy	49,894	55.5	80.9	94.2	59.2	40.7	34.9	42.0	30.3	25.9	16.3	20.5	20.1	13.8	17.1	16.9
Aarti Industries	502	515	Hold	18,373	32.7	15.0	18.0	25.1	54.4	45.4	28.9	29.7	24.6	11.8	9.7	10.4	14.6	11.1	11.9
Tata Chemical	978	1,130	Buy	24,807	47.5	89.5	109.3	20.6	10.9	8.9	12.7	7.7	5.2	6.6	10.4	10.8	6.6	11.6	12.5
Vinati Organics	2027	2,055	Hold	20,829	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	386	420	Hold	19,289	8.5	10.1	11.0	45.5	38.4	35.2	31.4	28.1	23.8	30.2	27.7	25.6	22.0	21.1	19.0
Navin Fluorine	4748	5,160	Hold	23,539	52.3	75.7	91.1	90.8	62.7	52.1	66.0	44.2	35.4	17.8	17.2	17.5	14.0	17.2	17.7
Rallis India	206	223	Hold	4,000	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	461	555	Buy	3,171	18.8	6.5	20.8	19.2	55.6	17.3	11.9	15.6	8.5	10.9	5.7	15.8	15.6	5.4	15.4
Neogen Chemicals	1480	1,424	Hold	3,688	17.9	20.0	24.8	82.7	74.0	59.6	43.5	35.4	28.5	12.0	11.8	11.6	10.2	10.3	11.5
Astec Lifesciences	1483	1,350	Reduce	2,963	45.1	12.2	29.5	32.9	121.1	50.2	20.7	42.6	26.7	19.3	7.3	11.8	22.3	5.7	12.3

Source: Bloomberg, ICICI Direct Research

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Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



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