Atul Limited

IIFL Premia Research

CMP: ₹2,965; 1-year target: ₹3,590

Sector	Chemicals
Recommendation	BUY
Upside	**21.1%**

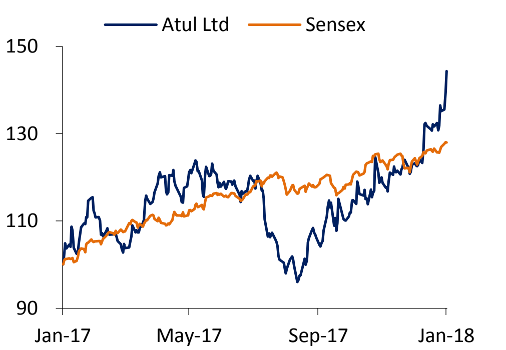
Stock Data	
Sensex	34,503
52 Week h/l (₹):	3,025/1,945
Market cap (₹ Cr) :	8,795
BSE code:	500027
NSE code:	ATUL
FV (₹):	10
Div yield (%):	0.35

Shareholding Pattern

	Mar-17	Jun-17	Sep-17
Promoters	44.63	44.63	44.64
DII+FII	27.00	27.67	28.02
Individuals	28.37	27.70	27.34

Source: www.bseindia.com

Share Price Trend



Prices as on 11/01/2018

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Atul Limited (Atul) is an integrated chemicals company having a diverse product portfolio across various business segments. Atul has executed major capex activity of ~₹360cr over last three years. We expect the company to focus on ramping up the utilization levels of newly commissioned plants. Its pricing for key products would increase in near future owing to supply side issues arising in China. We expect revenue CAGR of 11% with EBITDA margin expansion of ~460bps to 21.6% and PAT CAGR of 18%, over FY17-20E. We recommend BUY with a target price of ₹3,590 (21x FY20E EPS).

Utilization to improve as major capex ends: Atul has completed capex projects across business segments in FY17. It is now ramping up capacity utilization (CU) from newly commissioned capacities, majorly comprising crop protection (8% CU in FY17), specialty bulk chemical (3%) and specialty polymers (60-70%). Atul would witness higher utilization backed by increased global demand for Indian chemicals (Chinese government's restrictions on highly polluting industries, has caused supply issues in China, giving an edge to Indian chemical manufacturers). We expect EBITDA margin expansion of ~460bps to 21.6% over FY17-FY20E.

Earnings to rebound: Atul's return ratios have suffered in the past, mainly due to below potential use of assets, adverse price trends in key products, GST related issues and ₹ appreciation vs US$ as Atul is net exporter. However, as most of these issues are fading, net operating margins are expected to improve leading to better return ratios. We expect RoCE & RoE at 24.4% & 19.2% in FY20E as against 20% & 16% respectively in FY18E.

Outlook & Valuation: Atul's major phase of capex investments are nearing an end. Further, owing to the nearly debt free position of the company, we expect Atul to generate free cash flows to equity over FY18E-20E. The company is currently priced at reasonable valuation of 17.4x FY20E EPS and looks attractive amongst its peers.

Financial Summary

Consolidated ₹Cr.	FY16	FY17	FY18E	FY19E	FY20E
Revenue	2,595	2,834	3,237	3,548	3,860
YoY growth (%)	(2.33)	9.22	14.21	9.63	8.78
EBITDA Margin (%)	16.7	17.0	16.5	20.5	21.6
PAT	274.3	323.4	310.0	450.2	526.6
EPS (₹)	92.5	109.0	101.1	146.7	170.8
RoE (%)	20.7	18.1	16.0	19.3	19.2
P/E x	16.7	23.2	29.3	20.2	17.4
EV/EBITDA x	9.9	12.8	16.8	12.3	10.7

Source: IIFL Research

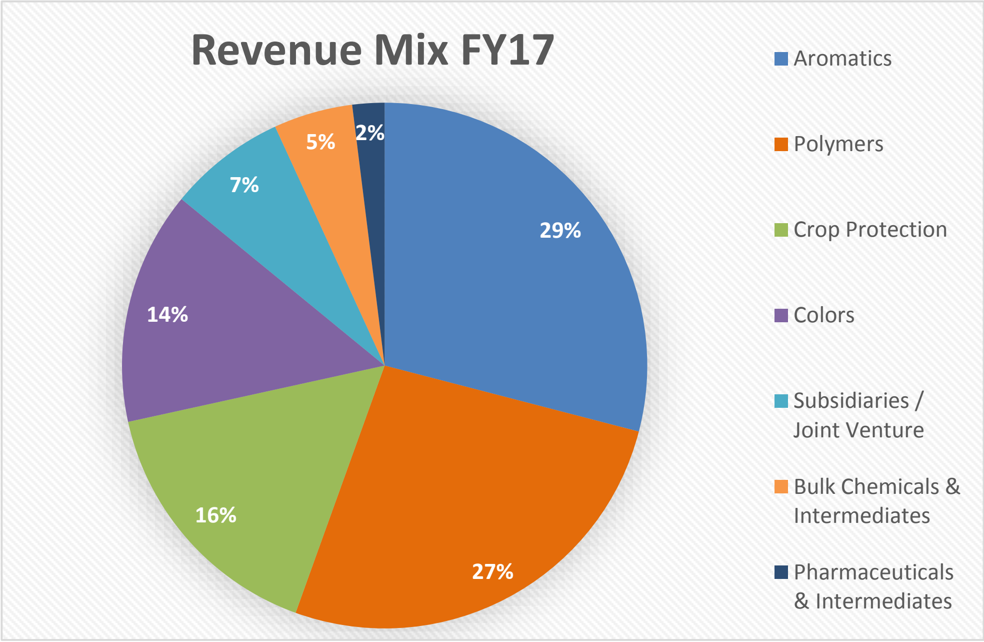
Company Overview

Atul is a diversified chemicals company incorporated in 1947 and headquartered in Gujarat. Atul manufactures about 920 products and 460 formulations across six business divisions i.e. aromatics, dyes, pharmaceutical chemicals, crop protection chemicals, polymers and bulk chemicals. It owns more than 65 brands and services about 6,000 customers in over 68 countries. It has production facilities at three locations in India and wholly owned subsidiaries in several countries. It has also entered into date palm cultivation with the intent of import substitution and economic upliftment of arid regions in Rajasthan. The promoter group holds ~44% stake in the company.

Product diversification to lead to de-risking: Atul has reported a stable top-line CAGR of 11.5% over FY13-17 on account of steady increase in volumes across business segments. Aromatics-II and Polymer segments contributed more than 50% of the consolidated revenue of the company (refer Exhibit 1).

Atul manufactures around 920 products and 460 formulations across its business divisions

Exhibit 1: Revenue mix FY17



Source: Company, IIFL Research

Increase in utilization rate for newly commissioned capacities in FY17 would assist operating margins

Exhibit 2: Segmental details for utilization and market dynamics

Products	Capacity utilization % of new capex (FY17)	Unrealized sales potential (₹ in Cr)	Market size (US$ in bn)	Market growth rate %
Crop Protection	8	98	56	4
Pharmaceuticals & Intermediates	-	84	1,200	4-7
Aromatics	85	90	34	4
Bulk Chemicals & Intermediates		53		
- Resorcinol	100		0.32	3
- CSA	3		70	6
Colours	-	30	5.6	3.5
Polymers				
- Epoxy Resins	80	120	6.3	2
- Sulphones	60	30	0.32	4
- Formulations	73	25	-	-

Source: Company, IIFL Research

Exhibit 3: Segment-wise outlook

₹ in Cr	FY16	FY17	FY18E	FY19E	FY20E
***Revenue**					
Life Science Chemicals	804	879	1,107	1,218	1,325
YoY %		9.2%	26.0%	10.0%	8.8%
Performance & Other Chemicals	1,790	1,955	2,130	2,331	2,535
YoY %		9.2%	8.9%	9.4%	8.8%
Total	**2,595**	**2,834**	**3,237**	**3,548**	**3,860**
EBIT					
Life Science Chemicals	172	154	166	225	252
EBIT margin %	21.4%	17.5%	15.0%	18.5%	19.0%
Performance & Other Chemicals	256	313	295	435	520
EBIT margin %	14.3%	16.0%	13.8%	18.7%	20.5%
Total	**428**	**467**	**461**	**660**	**772**

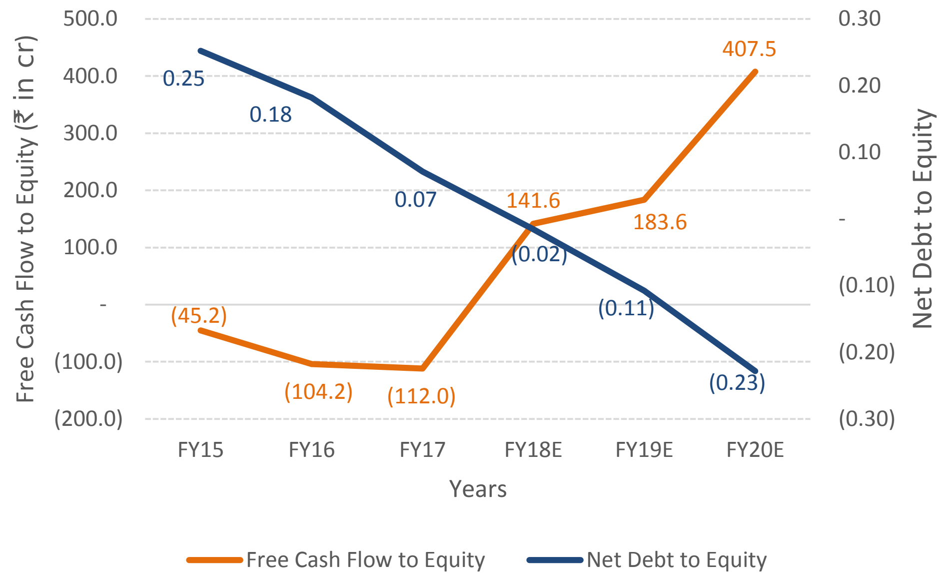
*Source: IIFL Research, * Revenue net off excise duty in FY16 & FY17*

Life Science Chemicals consists of crop protection, pharmaceuticals and aromatics-I chemical. We expect 15% revenue CAGR over FY17-20E in this segment with an improvement in EBIT margin by ~150bps to 19% over FY17-20E.

Performance & Other Chemicals consists of bulk chemicals & intermediaries, colors, polymers and aromatics-II chemical. We expect 9% revenue CAGR over FY17-20E in this segment with an improvement in EBIT margin by ~450bps to 20.5% over FY17-20E.

Exhibit 4: Improved free cash flows and net debt to equity

As the capex activity of the company has reduced coupled with increase in utilization, Atul would commence generating free cash flows from FY18E

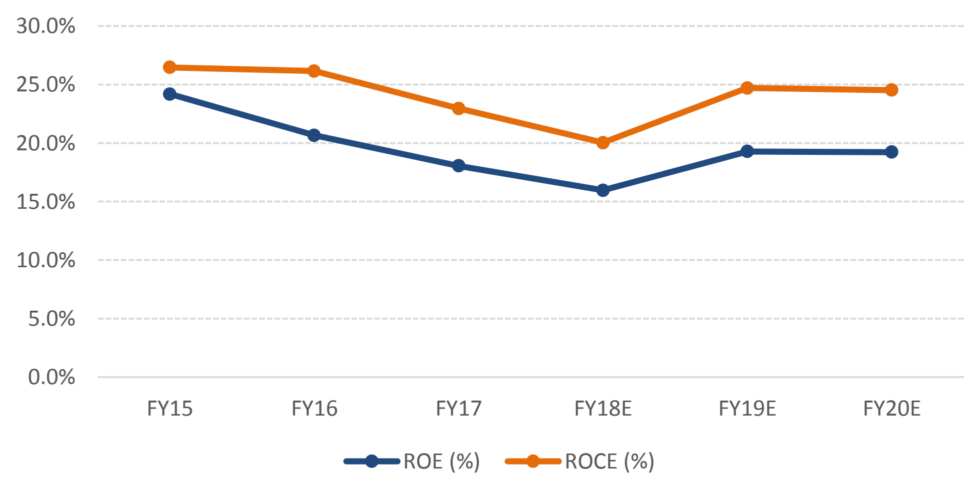


Source: IIFL Research

Lower capex investments compared to that of previous years as well as improvement in operating cash flows (driven by better earnings) would result in free cash flow generation. The robust free cash flow generation is expected to help the company become debt-free by end of FY18.

Exhibit 5: Recovery in return ratios

Return on Capital Employed and Return on Equity would increase on account of improving net margins and low debt



Source: IIFL Research

Atul's return ratios have suffered in the past few years, mainly due to below potential use of assets. However, increase in capacity utilization is expected to result in higher operating margins, thereby increasing net margins and improvement in return ratios.

Exhibit 6: Valuation and peer comparison

FY20E					
Peer Comparison	**EPS ₹**	**Price**	**P/E**	**EV/EBITDA**	**RoE%**
Atul	170.8	2,965	17.4	10.7	19.2%
Aarti Industries	64.6	1,130	17.5	10.6	22.8%
SRF	126.5	1,939	15.3	9.6	16.8%
BASF India	81.7	2,235	27.4	18.0	18.8%

Source: Bloomberg, IIFL Research

Atul Ltd is reasonably priced at 17.4x FY20E EPS, which is attractive in the peer group. We expect valuations to rise further to 21x FY20E EPS backed by improvement in margins, free cash flow generation and expected debt-free position of the company.

Disclaimer

Recommendation Parameters for Fundamental/Technical Reports:

Buy – Absolute return of over +10%
Accumulate – Absolute return between 0% to +10%
Reduce – Absolute return between 0% to -10%
Sell – Absolute return below -10%

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