

SELL

TP: Rs 1,120 | ▼ 13%

PIDILITE INDUSTRIES

Construction Materials

07 August 2019

In-line quarter; cut to SELL on rich valuations

Pidilite Industries (PIDI) reported in-line consolidated Q1FY20 revenue growth of 10% YoY, aided by a 6% rise in consumer & bazaar (CBP) volumes. A 120bps increase in operating margins to 22% drove EBITDA/PAT growth of 16%/23% YoY. Management expects margins to remain favourable in light of benign RM prices, but indicated that demand conditions are challenging. We find valuations expensive at 48x FY21E P/E and thus downgrade the stock to SELL from REDUCE. Rolling forward, we have a new Jun'20 TP of Rs 1,120 (vs. Rs 1,080).

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Modest revenue growth: PIDI's consolidated Q1 revenues grew 10% YoY to Rs 20.2bn, with 11.3% constant currency growth in overseas subsidiaries. Standalone revenues increased 10.6% YoY to Rs 17.8bn, backed by volume growth of 11% (6% in the CBP segment and 12% in industrial segment). Management has indicated that demand conditions remain challenging, but the company is countering this by expanding its product portfolio and extending its direct distribution reach to small towns.

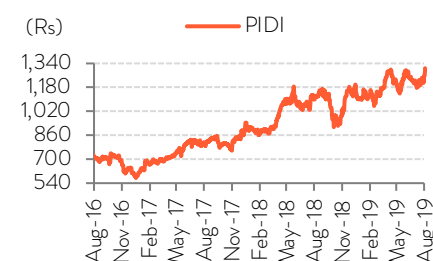
Margin trends favourable: Consolidated operating margins swelled 120bps YoY to 22% as higher gross margins (+86bps) and lower other expenses (-110bps) mitigated the impact of increased employee expenses (+80bps). EBITDA/PAT for the quarter grew 16%/23% YoY. Gross margins expanded as raw material prices softened. Management expects the favourable margin trends to hold as RM prices remain benign in Q2.

Downgrade to SELL on expensive valuations: While we like PIDI for its strong franchise and broad portfolio, valuations at 48x FY21E P/E look rich, especially against the backdrop of weakening demand. Downgrade to SELL from REDUCE with a revised Jun'20 TP of Rs 1,120 (earlier Rs 1,080), set at 40x one-year forward P/E.

Ticker/Price	PIDI IN/Rs 1,290
Market cap	US\$ 9.3bn
Shares o/s	508mn
3M ADV	US\$ 10.7mn
52wk high/low	Rs 1,324/Rs 895
Promoter/FPI/DII	70%/11%/19%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Adj. net profit (Rs mn)	9,159	8,901	11,669	13,648	15,830
Adj. EPS (Rs)	18.0	17.5	23.0	26.9	31.2
Adj. EPS growth (%)	7.5	(2.9)	31.1	17.0	16.0
Adj. ROAE (%)	26.0	23.1	26.1	26.4	26.5
Adj. P/E (x)	71.5	73.6	56.1	48.0	41.4
EV/EBITDA (x)	48.9	47.9	36.6	31.5	27.5

Source: Company, BOBCAPS Research

BOB Capital Markets Ltd is a wholly owned subsidiary of Bank of Baroda

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FIG 1 – CONSOLIDATED QUARTERLY PERFORMANCE

(Rs mn)	Q1FY20	Q1FY19	YoY (%)	Q4FY19	QoQ (%)
Net revenues	20,168	18,341	10.0	16,389	23.1
Raw material cost	9,805	9,074	8.1	8,148	20.3
Other expenses	5,926	5,450	8.7	5,453	8.7
Other operating inc (exp), net	0	0	n.m.	0	n.m.
EBITDA	4,437	3,817	16.3	2,788	59.2
EBITDA margin (%)	22.0	20.8	119bps	17.0	499bps
Depreciation and amortization	377	301	25.3	390	(3.2)
EBIT	4,060	3,516	15.5	2,398	69.3
EBIT margin (%)	20.1	19.2	96bps	14.6	550bps
Net interest expenses	73	73	1.0	66	11.7
Foreign exchange gain (loss), net	0	0	n.m.	0	n.m.
Other income	399	321	24.1	562	(29.1)
EBT And Except. items	4,385	3,764	16.5	2,895	51.5
Exceptional items	0	0	n.m.	419	(100.0)
Earnings before tax	4,385	3,764	16.5	3,314	32.3
Income taxes	1,444	1,361	6.2	960	50.5
Income tax as % of PBT	32.9	36.1	(321bps)	29.0	397bps
Earnings after tax	2,941	2,404	22.4	2,354	24.9
Profit in associate company	3	4	(31.0)	15	(80.3)
Minority interest (expense) income	(15)	(21)	n.m.	(17)	n.m.
Net income (loss) adjusted	2,929	2,387	22.7	1,932	51.6
Non-recurring items	0.0	0.0	NM	0.0	NM
Net income (loss), reported	2,929	2,387	22.7	2,351	24.6

Source: Company, BOBCAPS Research

FIG 2 – CONSOLIDATED SEGMENTAL PERFORMANCE

(Rs mn)	Q1FY20	Q1FY19	YoY (%)	Q4FY19	QoQ (%)
Revenue					
Consumer & Bazaar Products	17,364	15,886	9.3	13,645	27.3
Industrial Products	2,935	2,576	13.9	2,923	0.4
Others	225	217	3.7	142	58.7
Total	20,524	18,679	9.9	16,709	22.8
Less: Inter Segment revenue	(356)	(338)	5.3	(320)	11.3
Net revenues	20,168	18,341	10.0	16,389	23.1
Profit before interest & tax					
Consumer & Bazaar Products	4,625	4,030	14.8	3,010	53.6
Industrial Products	453	379	19.3	432	4.8
Others	(14)	(33)	n.m.	(19)	(28.4)
Total	5,064	4,376	15.7	3,423	47.9
EBIT Margin (%)					
Consumer & Bazaar Products	26.6	25.4	127bps	22.1	457bps
Industrial Products	15.4	14.7	70bps	14.8	64bps
Total	25.1	23.9	125bps	20.9	422bps

Source: Company, BOBCAPS Research

FIG 3 – STANDALONE PERFORMANCE

(Rs mn)	Q1FY20	Q1FY19	YoY (%)	Q4FY19	QoQ (%)
Net revenues	17,791	16,083	10.6	13,787	29.0
Raw material expenses	8,616	7,968	8.1	6,720	28.2
Other expenses	4,995	4,539	10.0	4,448	12.3
Other operating inc (exp), net	0	0	n.m.	0	n.m.
EBITDA	4,180	3,576	16.9	2,619	59.6
EBITDA margin (%)	23.5	22.2	126bps	19.0	450bps
Depreciation and amortization	281	229	22.3	298	(5.9)
EBIT	3,899	3,347	16.5	2,321	68.0
EBIT margin (%)	21.9	20.8	111bps	16.8	508bps
Net interest expenses	27	20	34.8	19	46.5
Other income	390	645	(39.6)	525	(25.8)
PBT	4,262	3,972	7.3	2,828	50.7
Income taxes	1,387	1,302	6.5	924	50.0
Income tax as % of PBT	32.5	32.8	(26bps)	32.7	(16bps)
Earnings after tax, adjusted	2,876	2,669	7.7	1,903	51.1
Extraordinary items	0	0	NA.	529	NA
Net income (loss), reported	2,876	2,669	7.7	2,432	18.2

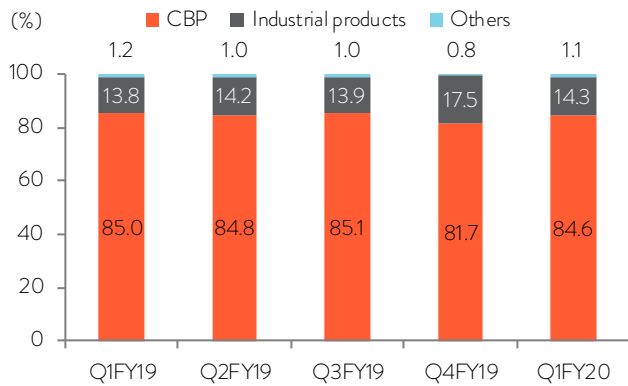
Source: Company, BOBCAPS Research

FIG 4 – STANDALONE SEGMENTAL PERFORMANCE

(Rs mn)	Q1FY20	Q1FY19	YoY (%)	Q4FY19	QoQ (%)
Revenue					
Consumer & Bazaar Products	14,987	13,683	9.5	11,042	35.7
Industrial Products	2,935	2,576	13.9	2,923	0.4
Others	225	162	38.8	142	58.7
Total	18,147	16,421	10.5	14,107	28.6
Less: Inter Segment revenue	(356)	(338)	5.3	(320)	11.3
Net revenues	17,791	16,083	10.6	13,787	29.0
Profit before interest & tax					
Consumer & Bazaar Products	4,493	4,219	6.5	2,931	53.3
Industrial Products	453	379	19.3	432	4.8
Others	(14)	(33)	n.m.	(19)	(28.4)
Total	4,932	4,565	8.0	3,344	47.5
EBIT Margin (%)					
Consumer & Bazaar Products	30.0	30.8	(85bps)	26.5	344bps
Industrial Products	15.4	14.7	70bps	14.8	64bps
Others	(6.0)	(20.3)	1,423bps	(13.4)	734bps
Total	27.7	28.4	(66bps)	24.3	347bps

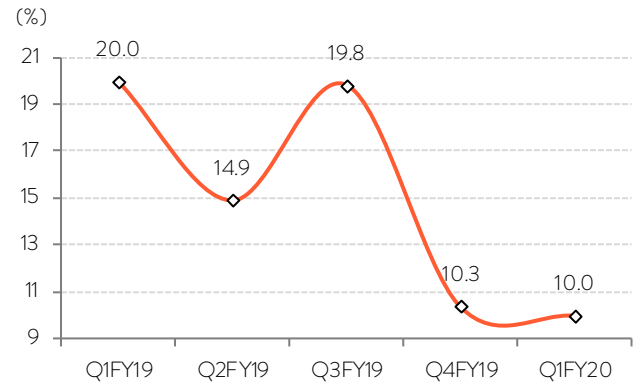
Source: Company, BOBCAPS Research

FIG 5 – CONSOLIDATED REVENUE BREAK-UP



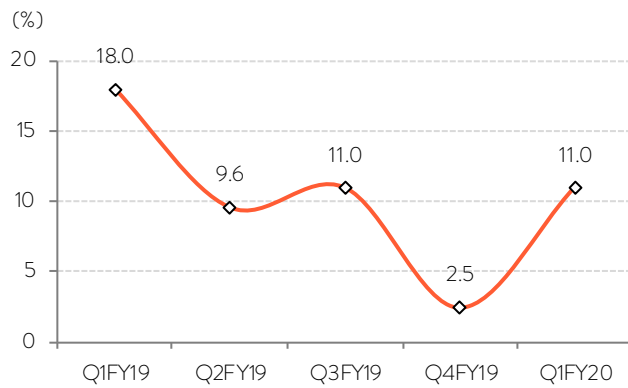
Source: Company, BOBCAPS Research

FIG 6 – CONSOLIDATED REVENUE GROWTH



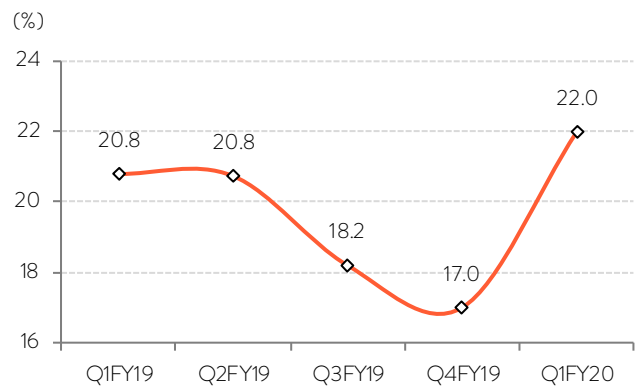
Source: Company, BOBCAPS Research

FIG 7 – TOTAL VOLUME GROWTH



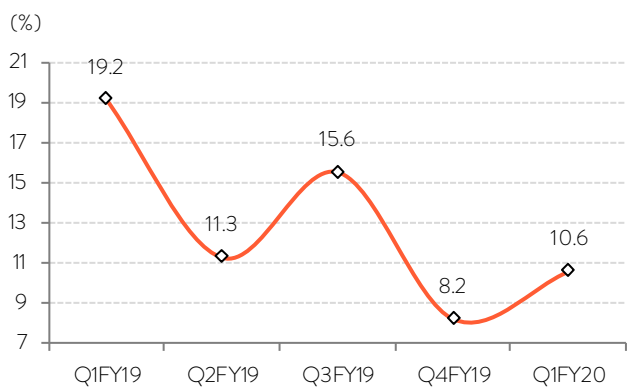
Source: Company, BOBCAPS Research

FIG 8 – CONSOLIDATED EBITDA MARGIN



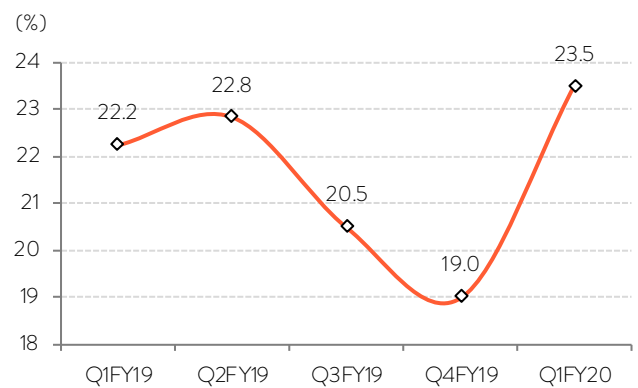
Source: Company, BOBCAPS Research

FIG 9 – STANDALONE REVENUE GROWTH



Source: Company, BOBCAPS Research

FIG 10 – STANDALONE EBITDA MARGIN



Source: Company, BOBCAPS Research

Earnings call highlights

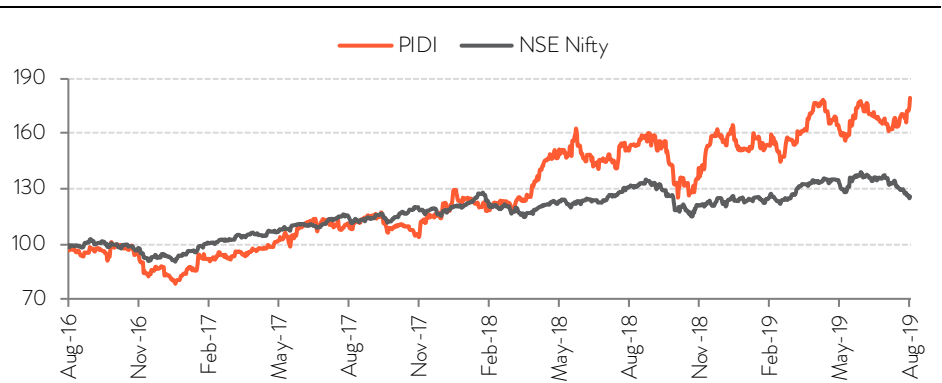
- Market demand conditions remain difficult. Nevertheless, PIDI has clocked 6% YoY volume growth in the CBP segment aided by an expanded product portfolio and a wider direct reach in small towns. The company is increasingly building its direct distribution reach in areas with sub-200,000 population.
- Management is yet to see a marked shift in demand from unorganised to organised players as heralded by GST implementation.
- During Q1FY20, revenues at subsidiary Nina-Percept declined 17% YoY as pressure mounted on the real estate sector. PIDI also saw a slowdown in areas linked to construction, such as water proofing and related chemicals.
- The raw material price index has come down sequentially in Q1. VAM prices averaged ~US\$ 980/t for the quarter and are currently at US\$ 870/t. PIDI normally has 1-2 months of VAM inventory and hence the full benefit of lower prices will accrue with a lag.
- The company took price corrections in a few products as raw material prices have fallen, but expects to retain some portion of the RM benefit.
- Management is comfortable with operating margins in the 22-24% range.
- Distributor inventory levels are normal though dealer level stocks may have increased amid weak demand.
- PIDI is seeing good traction in the Bangladesh (where it will start an additional factory in Q2) and Sri Lankan markets. The US subsidiary also did well during the quarter.
- Capex for FY20 is pegged at ~3% of revenues, and the tax rate at 32-33%.

Valuation methodology

PIDI is the leader in India’s adhesive market with a strong brand, extensive distribution reach and large product portfolio. The company has a unique distribution framework, with products available in both building material as well as FMCG channels. While we like PIDI for its strong franchise and broad portfolio, current valuations at 48x FY21E P/E appear rich, especially against the backdrop of weakening demand.

We largely maintain our estimates and roll over to a revised Jun’20 target price of Rs 1,120 (from Rs 1,080), based on an unchanged one-year forward P/E multiple of 40x. Downgrade to SELL from REDUCE.

FIG 11 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

- **Sharp decline in raw material prices:** Any sudden, steep fall in RM prices, especially for crude-linked products, could drive above-expected margins.
- **Above-expected pick-up in housing activity:** A stronger revival in the housing market than anticipated can take growth ahead of estimates.

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Total revenue	60,324	70,787	81,970	94,596	1,08,262
EBITDA	13,412	13,682	17,869	20,717	23,818
EBIT	12,213	12,355	16,353	18,967	21,815
Net interest income/(expenses)	(155)	(261)	(289)	(124)	(114)
Other income/(expenses)	560	586	1,626	1,852	2,306
Exceptional items	0	0	0	0	0
EBT	13,542	13,560	17,690	20,694	24,007
Income taxes	(4,392)	(4,661)	(6,015)	(7,036)	(8,162)
Extraordinary items	465	349	0	0	0
Min. int./Inc. from associates	9	1	(6)	(10)	(14)
Reported net profit	9,623	9,249	11,669	13,648	15,830
Adjustments	(465)	(349)	0	0	0
Adjusted net profit	9,159	8,901	11,669	13,648	15,830

Balance Sheet

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Accounts payables	5,438	5,806	5,966	6,885	7,879
Other current liabilities	5,353	6,837	6,337	5,837	5,337
Provisions	1,431	637	5,251	6,142	7,124
Debt funds	1,226	1,111	335	285	285
Other liabilities	1,107	1,201	1,201	1,201	1,201
Equity capital	508	508	508	508	508
Reserves & surplus	35,233	40,973	47,391	54,897	63,604
Shareholders' fund	35,740	41,481	47,899	55,405	64,112
Total liabilities and equities	52,045	59,145	69,107	77,926	88,171
Cash and cash eq.	1,636	1,904	2,206	733	533
Accounts receivables	9,381	10,560	11,453	13,218	15,127
Inventories	8,043	9,345	9,979	11,892	13,610
Other current assets	4,767	8,818	9,467	9,952	10,476
Investments	12,459	11,514	18,054	23,097	28,145
Net fixed assets	15,699	16,897	17,840	18,928	20,173
CWIP	0	0	0	0	0
Intangible assets	0	0	0	0	0
Deferred tax assets, net	59	107	107	107	107
Other assets	0	0	0	0	0
Total assets	52,045	59,145	69,107	77,926	88,171

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Net income + Depreciation	14,741	14,888	19,207	22,444	26,009
Interest expenses	155	261	289	124	114
Non-cash adjustments	0	0	0	0	0
Changes in working capital	(1,795)	(5,472)	2,096	(2,852)	(2,676)
Other operating cash flows	(4,517)	(4,671)	(5,975)	(6,992)	(8,114)
Cash flow from operations	8,584	5,006	15,617	12,724	15,334
Capital expenditures	(1,768)	(1,327)	(2,459)	(2,838)	(3,248)
Change in investments	1,972	945	(6,540)	(5,044)	(5,048)
Other investing cash flows	(319)	(247)	(1,289)	(891)	(982)
Cash flow from investing	(116)	(628)	(10,288)	(8,772)	(9,278)
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	250	(115)	(775)	(50)	0
Interest expenses	(155)	(261)	(289)	(124)	(114)
Dividends paid	(7,927)	(3,733)	(3,962)	(5,251)	(6,142)
Other financing cash flows	0	0	0	0	0
Cash flow from financing	(7,832)	(4,109)	(5,027)	(5,425)	(6,256)
Changes in cash and cash eq.	636	268	302	(1,473)	(200)
Closing cash and cash eq.	1,636	1,904	2,206	733	533

Per Share

Y/E 31 Mar (Rs)	FY18A	FY19A	FY20E	FY21E	FY22E
Reported EPS	19.0	18.2	23.0	26.9	31.2
Adjusted EPS	18.0	17.5	23.0	26.9	31.2
Dividend per share	6.0	6.5	8.2	9.6	11.2
Book value per share	70.4	81.7	94.3	109.1	126.2

Valuations Ratios

Y/E 31 Mar (x)	FY18A	FY19A	FY20E	FY21E	FY22E
EV/Sales	10.9	9.3	8.0	6.9	6.0
EV/EBITDA	48.9	47.9	36.6	31.5	27.5
Adjusted P/E	71.5	73.6	56.1	48.0	41.4
P/BV	18.3	15.8	13.7	11.8	10.2

DuPont Analysis

Y/E 31 Mar (%)	FY18A	FY19A	FY20E	FY21E	FY22E
Tax burden (Net profit/PBT)	67.6	65.6	66.0	66.0	65.9
Interest burden (PBT/EBIT)	110.9	109.8	108.2	109.1	110.0
EBIT margin (EBIT/Revenue)	20.2	17.5	20.0	20.1	20.2
Asset turnover (Revenue/Avg TA)	120.9	127.3	127.8	128.7	130.4
Leverage (Avg TA/Avg Equity)	1.4	1.4	1.4	1.4	1.4
Adjusted ROAE	26.0	23.1	26.1	26.4	26.5

Source: Company, BOBCAPS Research | Note: TA = Total Assets

Ratio Analysis

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
YoY growth (%)					
Revenue	8.0	17.3	15.8	15.4	14.4
EBITDA	6.5	2.0	30.6	15.9	15.0
Adjusted EPS	7.5	(2.9)	31.1	17.0	16.0
Profitability & Return ratios (%)					
EBITDA margin	22.2	19.3	21.8	21.9	22.0
EBIT margin	20.2	17.5	20.0	20.1	20.2
Adjusted profit margin	15.2	12.6	14.2	14.4	14.6
Adjusted ROAE	26.0	23.1	26.1	26.4	26.5
ROCE	21.8	19.4	22.7	23.1	23.1
Working capital days (days)					
Receivables	52	51	49	48	48
Inventory	96	88	89	87	89
Payables	36	36	34	32	32
Ratios (x)					
Gross asset turnover	2.3	2.4	2.6	2.8	2.9
Current ratio	1.8	2.1	1.9	1.9	1.9
Net interest coverage ratio	78.6	47.4	56.6	152.9	191.3
Adjusted debt/equity	0.0	0.0	0.0	0.0	0.0

Source: Company, BOBCAPS Research

Disclaimer

Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

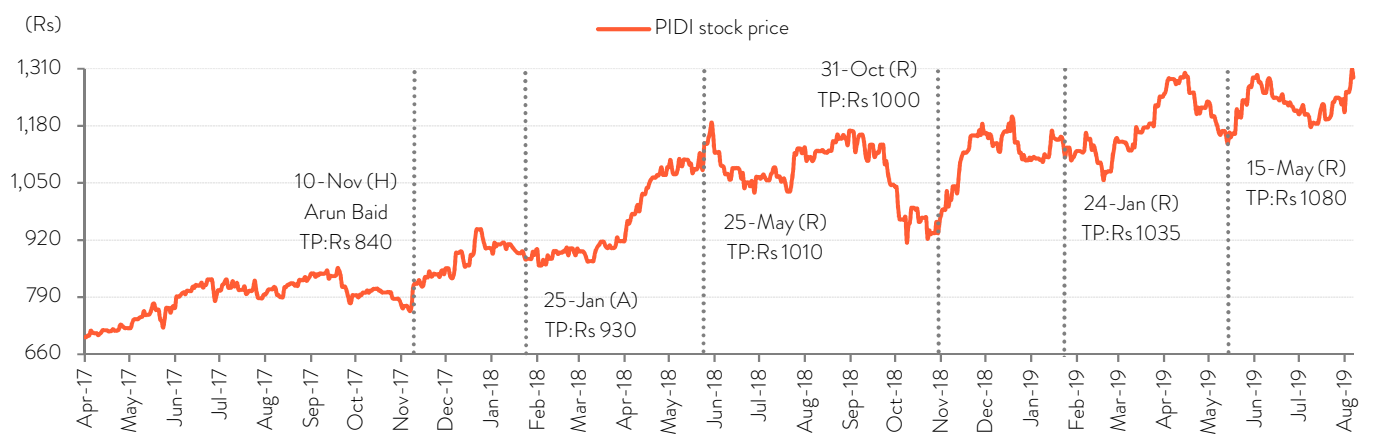
ADD – Expected return from >+5% to +15%

REDUCE – Expected return from -5% to +5%

SELL – Expected return <-5%

Note: Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

HISTORICAL RATINGS AND TARGET PRICE: PIDILITE INDUSTRIES (PIDI IN)



B – Buy, A – Add, R – Reduce, S – Sell

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