

SELL

TP: Rs 1,365 | ▼ 18%

PIDILITE INDUSTRIES

Construction Materials

29 January 2021

Margin headwinds expected in the near future

Pidilite Industries (PIDI) reported healthy Q3FY21 consolidated revenue growth of 19% YoY, supported by a 22%/12% rise in standalone C&B/B2B volumes. Operating margins expanded 385bps YoY to 27.9% due to lower RM and employee/other expenses-to-sales, aiding EBITDA/PBT growth of 38%/32% YoY. Margins are expected to come under pressure given a surge in RM cost. We raise our FY21 PAT estimate by 9% and roll over to a revised Mar'22 TP of Rs 1,365 (vs. Rs 1,310). Retain SELL as current valuations of 51.4x FY23E P/E look rich.

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Healthy revenue growth: PIDI's consolidated Q3 revenue grew 19% YoY to Rs 23bn (16% ex-Hunstman) with 21% constant currency growth in overseas subsidiaries. Standalone revenue increased 18% YoY to Rs 19.6bn aided by a tepid base last year and volume growth of 19% YoY (+22% in the consumer & bazaar (C&B) segment and 12% in B2B). Management stated that demand growth spanned across categories and was fuelled by continued momentum in rural areas along with strong recovery in urban markets including metros.

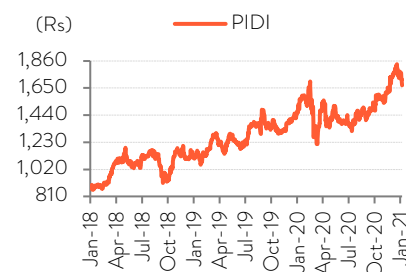
Margin expansion unsustainable: Consolidated operating margins rose 385bps YoY to 27.9% due to a decline in raw material cost (-97bps), employee cost (-93bps) and other expenses (-194bps). Consequently, EBITDA/PBT grew 38%/32% YoY. Gross margins increased as RM prices softened, whereas other expenses reduced due to lower A&P. Management stated that RM prices have been hardening in Q4 (VAM is currently at US\$ 1300/mt from a Q3 average of US\$ 875) and that margins are likely to revert to the guided range of 21-24%.

Valuations expensive; SELL: We increase our FY21 PAT estimate by 9% to factor in the 9MFY21 beat. On rollover, we have a new Mar'22 TP of Rs 1,365, based on an unchanged 42x FY23E P/E. Though we like PIDI's business model, current valuations look rich at 51.4x FY23E – maintain SELL.

Ticker/Price	PIDI IN/Rs 1,670
Market cap	US\$ 11.6bn
Shares o/s	508mn
3M ADV	US\$ 21.9mn
52wk high/low	Rs 1,842/Rs 1,186
Promoter/FPI/DII	70%/11%/18%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue (Rs mn)	70,787	72,945	69,275	89,678	1,03,628
EBITDA (Rs mn)	13,682	15,760	15,864	20,895	24,145
Adj. net profit (Rs mn)	8,901	11,590	10,607	14,166	16,499
Adj. EPS (Rs)	17.5	22.8	20.9	27.9	32.5
Adj. EPS growth (%)	(2.9)	30.2	(8.5)	33.5	16.5
Adj. ROAE (%)	23.1	26.9	22.7	27.4	28.4
Adj. P/E (x)	95.3	73.2	80.0	59.9	51.4
EV/EBITDA (x)	62.0	53.8	53.3	40.6	35.3

Source: Company, BOBCAPS Research

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

Important disclosures, including any required research certifications, are provided at the end of this report.



FIG 1 – CONSOLIDATED QUARTERLY PERFORMANCE

(Rs mn)	Q3FY21	Q3FY20	YoY (%)	Q2FY21	QoQ (%)	9MFY21	9MFY20	YoY (%)
Net revenues	22,990	19,266	19.3	18,803	22.3	50,572	57,498	(12.0)
Raw Material Cost	10,402	8,903	16.8	8,284	25.6	22,770	27,130	(16.1)
Employee cost	2,603	2,361	10.3	2,421.4	7.5	7,182	7,142	0.6
Other expenses	3,577	3,371	6.1	2,972	20.4	8,422	10,475	(19.6)
EBITDA	6,408	4,632	38.4	5,126	25.0	12,198	12,751	(4.3)
EBITDA margin (%)	27.9	24.0	383bps	27.3	61bps	24.1	22.2	194bps
Depreciation and amortization	495	419	18.2	479	3.3	1,435	1,198	19.7
EBIT	5,913	4,213	40.4	4,648	27.2	10,764	11,553	(6.8)
EBIT Margin (%)	25.7	21.9	385bps	24.7	100bps	21.3	20.1	119bps
Net Interest expenses	121	82	47.4	87	39.5	298	238	25.1
Foreign exchange gain (loss), net	0	0	n.m.	0	n.m.	0	0	n.m.
Other income	204	398	(48.8)	217	(6.0)	621	1,355	(54.2)
EBT and except. Items	5,997	4,530	32.4	4,778	25.5	11,086	12,670	(12.5)
Exceptional items	0	0	n.m.	0	n.m.	0	(222)	n.m.
Earnings before tax	5,997	4,530	32.4	4,778	25.5	11,086	12,447	(10.9)
Income taxes	1,548	1,084	42.8	1,220	26.9	2,926	2,821	3.7
Income tax as % of PBT	25.8	23.9	188bps	25.5	29bps	26.4	22.7	373bps
Earnings after tax	4,449	3,445	29.1	3,558	25.0	8,160	9,626	(15.2)
Profit in associate company	16	16	0.0	6	159.0	27	29	(9.2)
Minority interest (expense) income	(46)	(43)	n.m.	(0)	n.m.	63	(67)	(195.3)
Net income (loss), reported	4,418	3,418	29.3	3,564	24.0	8,250	9,589	(14.0)

Source: Company, BOBCAPS Research

FIG 2 – CONSOLIDATED SEGMENTAL PERFORMANCE

(Rs mn)	Q3FY21	Q3FY20	YoY (%)	Q2FY21	QoQ (%)	9MFY21	9MFY20	YoY (%)
Revenue								
Consumer & Bazaar Products	18,489	14,783	25.1	15,277	21.0	40,786	44,495	(8.3)
Business to Business	4,751	4,626	2.7	3,771	26.0	10,404	13,557	(23.3)
Others	122	216	(43.6)	72	70.2	211	613	(65.5)
Total	23,361	19,625	19.0	19,119	22.2	51,401	58,665	(12.4)
Less: Inter Segment revenue	(371)	(359)	3.4	(316)	17.4	(830)	(1,167)	(28.9)
Net revenues	22,990	19,266	19.3	18,803	22.3	50,572	57,498	(12.0)
EBIT								
Consumer & Bazaar Products	6,451	4,488	43.7	5,324	21.2	13,059	12,705	2.8
Business to Business	558	688	(18.9)	290	92.4	657	1,958	(66.4)
Others	(5)	3	n.m.	8	(167.5)	(33)	(35)	(6.3)
Total	7,004	5,179	35.3	5,621	24.6	13,684	14,629	(6.5)
Margin (%)								
Consumer & Bazaar Products	34.9	30.4	453bps	34.8	5bps	32.0	28.6	347bps
Business to Business	11.7	14.9	(313bps)	7.7	405bps	6.3	14.4	(813bps)
Total	30.5	26.9	359bps	29.9	57bps	27.1	25.4	162bps

Source: Company, BOBCAPS Research

FIG 3 – STANDALONE QUARTERLY PERFORMANCE

(Rs mn)	Q3FY21	Q3FY20	YoY (%)	Q2FY21	QoQ (%)	9MFY21	9MFY20	YoY (%)
Net revenues	19,567	16,634	17.6	16,302	20.0	43,593	50,140	(13.1)
Raw material exp	8,791	7,658	14.8	7,090	24.0	19,394	23,551	(17.7)
Employee exp	2,050	1,873	9.4	1,954	4.9	5,721	5,726	(0.1)
Other exp	3,000	2,809	6.8	2,541	18.1	7,079	8,880	(20.3)
EBITDA	5,727	4,294	33.4	4,719	21.4	11,400	11,984	(4.9)
EBITDA margin (%)	29.3	25.8	345bps	28.9	32bps	26.1	23.9	225bps
Depreciation and amortization	371	318	16.7	359	3.1	1,078	901	19.6
EBIT	5,356	3,977	34.7	4,359	22.9	10,322	11,083	(6.9)
EBIT Margin (%)	27.4	23.9	347bps	26.7	63bps	23.7	22.1	157bps
Net Interest expenses	62	34	84.3	30	106.3	126	97	29.9
Other income	195	391	(50.2)	225	(13.5)	616	1,353	(54.5)
PBT	5,489	4,334	26.6	4,554	20.5	10,812	12,339	(12.4)
Income taxes	1,394	1,030	35.4	1,162	20.0	2,758	2,696	2.3
Income tax as % of PBT	25.4	23.8	164bps	25.5	(11bps)	25.5	21.9	366bps
Earnings after tax, adjusted	4,094	3,304	23.9	3,392	20.7	8,054	9,643	(16.5)
Extraordinary	0	0	n.m.	(5)	-	(5)	(222)	(98.0)
Net income (loss), reported	4,094	3,304	23.9	3,388	20.9	8,049	9,420	(14.6)

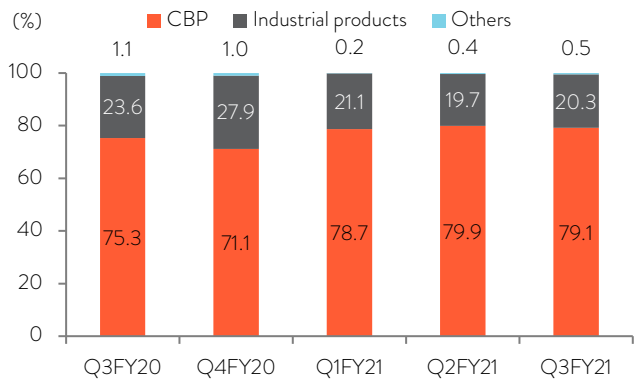
Source: Company, BOBCAPS Research

FIG 4 – STANDALONE SEGMENTAL PERFORMANCE

(Rs mn)	Q3FY21	Q3FY20	YoY (%)	Q2FY21	QoQ (%)	9MFY21	9MFY20	YoY (%)
Revenue								
Consumer & Bazaar Products	15,975	13,263	20.4	13,352	19.6	35,472	40,059	(11.5)
Business to Business	3,786	3,443	10.0	3,150	20.2	8,620	10,446	(17.5)
Others	122	216	(43.6)	72	70.2	211	613	(65.5)
Total	19,883	16,921	17.5	16,574	20.0	44,303	51,119	(13.3)
Less: Inter Segment revenue	(316)	(287)	10.2	(272)	16.4	(710)	(978)	(27.4)
Net revenues	19,567	16,634	17.6	16,302	20.0	43,593	50,140	(13.1)
Profit before interest & tax								
Consumer & Bazaar Products	5,911	4,419	33.8	4,911	20.4	12,292	12,501	(1.7)
Business to Business	576	577	(0.1)	438	31.4	1,070	1,809	(40.9)
Others	(5)	3	n.m.	8	(167.5)	(33)	(35)	(6.3)
Total	6,482	4,998	29.7	5,357	21.0	13,329	14,275	(6.6)
Margin (%)								
Consumer & Bazaar Products	37.0	33.3	368bps	36.8	22bps	34.7	31.2	345bps
Business to Business	15.2	16.7	(153bps)	13.9	130bps	12.4	17.3	(491bps)
Others	(4.3)	1.2	(543bps)	10.8	(1,504bps)	(15.4)	(5.7)	(972bps)
Total	33.1	30.0	308bps	32.9	27bps	30.6	28.5	210bps

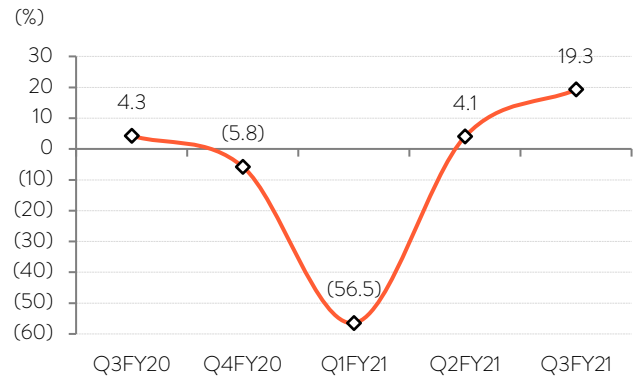
Source: Company, BOBCAPS Research

FIG 5 – CONSOLIDATED REVENUE BREAKUP



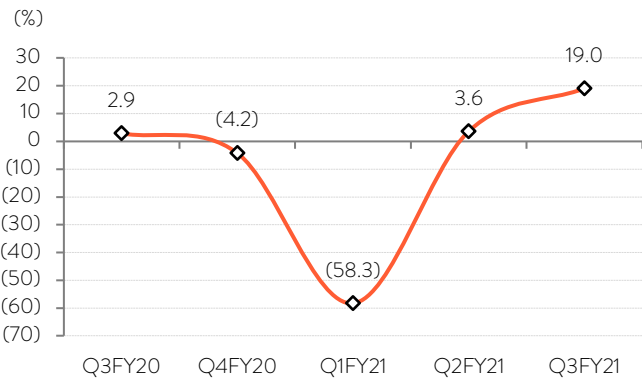
Source: Company, BOBCAPS Research

FIG 6 – CONSOLIDATED REVENUE GROWTH



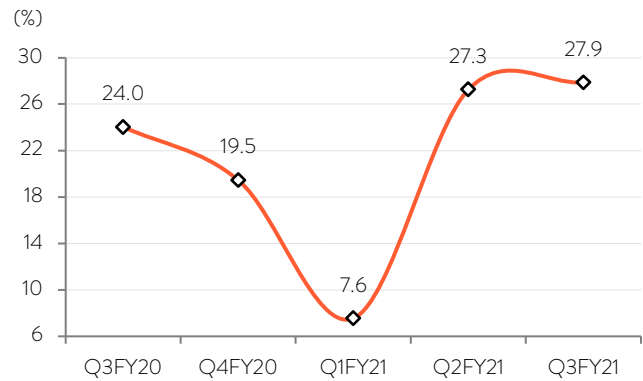
Source: Company, BOBCAPS Research

FIG 7 – TOTAL VOLUME GROWTH



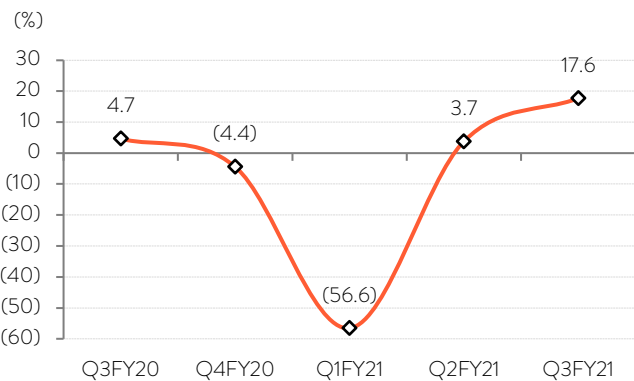
Source: Company, BOBCAPS Research

FIG 8 – CONSOLIDATED EBITDA MARGIN



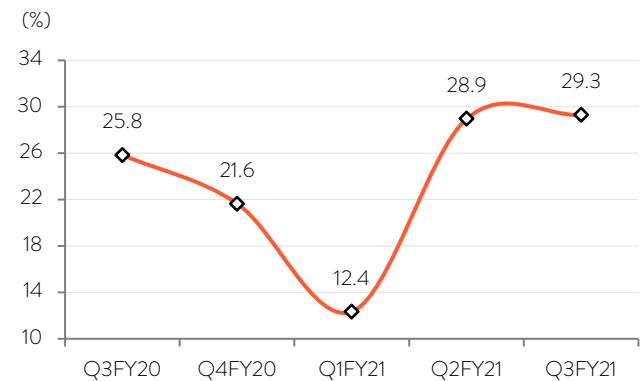
Source: Company, BOBCAPS Research

FIG 9 – STANDALONE REVENUE GROWTH



Source: Company, BOBCAPS Research

FIG 10 – STANDALONE EBITDA MARGIN



Source: Company, BOBCAPS Research

Earnings call highlights

- Demand for all PIDI's products picked up in Q3FY21. Momentum continued in rural areas and strong demand recovery was seen in urban markets, including metros. The B2B segment also garnered traction as industrial activity is reviving.
- Hunstman, acquired in Nov'20, posted revenues of Rs 591mn in Q3 and EBITDA of Rs 258mn. Per management, margins in the business benefited from low-cost inventory and will normalise going ahead.
- Organic revenue/EBITDA growth ex-Hunstman stood at 16%/33% YoY.
- Operating margins increased due to low-cost inventory and reduced A&P spend during the quarter.
- Management expects to revert to the targeted EBITDA margin band of 21-24% (vs. ~29% in Q3) given rising RM cost and other expenditure. Prices of key input VAM have hardened to ~US\$ 1,300/t (vs. US\$ 875 in Q3).
- The company has no plans to take price hikes immediately and will look to raise productivity in order to offset the margin impact from higher RM costs, but will pass on some of the burden to consumers if prices keep rising.
- PIDI stated that it is targeting volume growth and will reinvest profits to achieve this.
- Capacity utilisation is at 85-90%. Annual capex will remain at 4-5% of sales.
- In the international business, the Americas grew 48% YoY due to good demand from Brazil and the US. In Brazil, government incentives helped boost construction activity while in the US, art & hobby activity perked up due to the lockdown, which benefitted PIDI.

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.

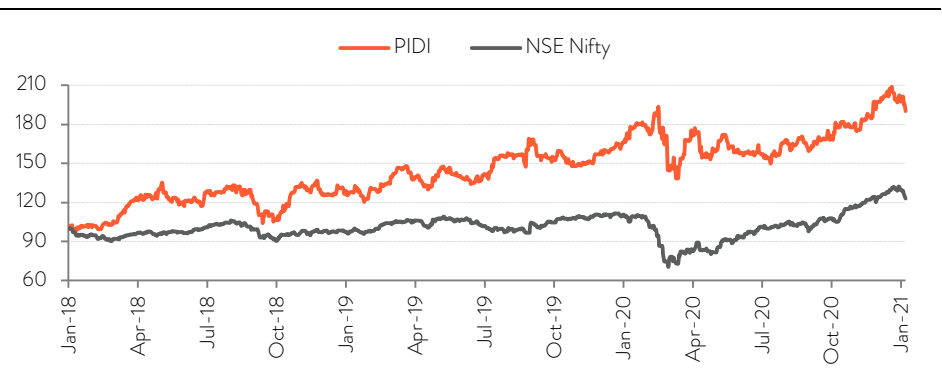
While we like PIDI’s business model, current valuations at 51.4x FY23E P/E appear rich. We increase our FY21 PAT estimate by 9% (FY22/FY23 largely unchanged) to factor in the 9MFY21 beat, but maintain our SELL rating. On rolling valuations forward, we move to a revised Mar’22 target price of Rs 1,365 (earlier Rs 1,310), set at an unchanged 42x FY23E P/E multiple.

FIG 11 – REVISED ESTIMATES

(Rs mn)	FY21E			FY22E			FY23E		
	New	Old	Change (%)	New	Old	Change (%)	New	Old	Change (%)
Revenue	69,275	65,827	5.2	89,678	87,454	2.5	1,03,628	101,049	2.6
EBITDA	15,864	14,219	11.6	20,895	20,377	2.5	24,145	23,545	2.6
PAT	10,607	9,689	9.0	14,166	13,975	1.4	16,499	16,408	0.6

Source: Company, BOBCAPS Research

FIG 12 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

Upside risks to our estimates:

- **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 pickup 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)	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue	70,787	72,945	69,275	89,678	1,03,628
EBITDA	13,682	15,760	15,864	20,895	24,145
Depreciation	(1,327)	(1,699)	(1,940)	(2,242)	(2,591)
EBIT	12,355	14,061	13,924	18,653	21,555
Net interest income/(expenses)	(261)	(336)	(413)	(287)	(135)
Other income/(expenses)	586	396	836	814	921
EBT	13,560	15,219	14,347	19,180	22,341
Income taxes	(4,661)	(3,477)	(3,787)	(4,987)	(5,809)
Extraordinary items	349	(552)	0	0	0
Min. int./Inc. from associates	1	(26)	48	(27)	(33)
Reported net profit	9,249	11,164	10,607	14,166	16,499
Adjustments	(349)	426	0	0	0
Adjusted net profit	8,901	11,590	10,607	14,166	16,499

Balance Sheet

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Accounts payables	5,806	6,210	5,662	7,605	8,807
Other current liabilities	6,837	9,185	8,685	8,185	7,685
Provisions	637	735	865	995	1,125
Debt funds	1,111	1,691	5,200	3,000	850
Other liabilities	1,201	823	823	823	823
Equity capital	508	508	508	508	508
Reserves & surplus	40,973	44,048	48,378	54,161	60,896
Shareholders' fund	41,481	44,556	48,886	54,669	61,404
Total liabilities and equities	59,145	65,357	72,267	77,494	82,994
Cash and cash eq.	1,904	7,033	157	358	1,066
Accounts receivables	10,560	10,885	10,183	12,530	14,480
Inventories	9,345	9,295	8,579	9,795	11,342
Other current assets	8,818	10,157	6,184	7,154	7,882
Investments	11,514	7,197	26,235	26,279	26,329
Net fixed assets	9,133	12,890	13,028	13,476	13,995
CWIP	2,421	2,593	2,593	2,593	2,593
Intangible assets	5,343	5,178	5,178	5,178	5,178
Deferred tax assets, net	107	130	130	130	130
Total assets	59,145	65,357	72,267	77,494	82,994

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Net income + Depreciation	14,888	16,919	16,286	21,422	24,931
Interest expenses	261	336	413	287	135
Changes in working capital	(5,472)	120	4,473	(2,961)	(3,393)
Other operating cash flows	(4,671)	(3,900)	(3,750)	(4,943)	(5,758)
Cash flow from operations	5,006	13,474	17,423	13,805	15,916
Capital expenditures	(1,327)	(4,687)	(2,078)	(2,690)	(3,109)
Change in investments	945	4,317	(19,038)	(44)	(50)
Other investing cash flows	(247)	33	0	0	0
Cash flow from investing	(628)	(337)	(21,116)	(2,734)	(3,159)
Debt raised/repaid	(115)	581	3,509	(2,200)	(2,150)
Interest expenses	(261)	(336)	(413)	(287)	(135)
Dividends paid	(3,733)	(8,254)	(6,277)	(8,383)	(9,764)
Cash flow from financing	(4,109)	(8,009)	(3,182)	(10,870)	(12,049)
Changes in cash and cash eq.	268	5,128	(6,875)	201	708
Closing cash and cash eq.	1,904	7,032	157	358	1,066

Per Share

Y/E 31 Mar (Rs)	FY19A	FY20A	FY21E	FY22E	FY23E
Reported EPS	18.2	22.0	20.9	27.9	32.5
Adjusted EPS	17.5	22.8	20.9	27.9	32.5
Dividend per share	6.5	13.5	9.8	13.1	15.3
Book value per share	81.7	87.7	96.2	107.6	120.9

Valuations Ratios

Y/E 31 Mar (x)	FY19A	FY20A	FY21E	FY22E	FY23E
EV/Sales	12.0	11.6	12.2	9.5	8.2
EV/EBITDA	62.0	53.8	53.3	40.6	35.3
Adjusted P/E	95.3	73.2	80.0	59.9	51.4
P/BV	20.5	19.0	17.4	15.5	13.8

DuPont Analysis

Y/E 31 Mar (%)	FY19A	FY20A	FY21E	FY22E	FY23E
Tax burden (Net profit/PBT)	65.6	76.2	73.9	73.9	73.9
Interest burden (PBT/EBIT)	109.8	108.2	103.0	102.8	103.6
EBIT margin (EBIT/Revenue)	17.5	19.3	20.1	20.8	20.8
Asset turnover (Revenue/Avg TA)	127.3	117.2	100.7	119.8	129.1
Leverage (Avg TA/Avg Equity)	1.4	1.4	1.5	1.4	1.4
Adjusted ROAE	23.1	26.9	22.7	27.4	28.4

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

Ratio Analysis

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
YoY growth (%)					
Revenue	17.3	3.0	(5.0)	29.5	15.6
EBITDA	2.0	15.2	0.7	31.7	15.6
Adjusted EPS	(2.9)	30.2	(8.5)	33.5	16.5
Profitability & Return ratios (%)					
EBITDA margin	19.3	21.6	22.9	23.3	23.3
EBIT margin	17.5	19.3	20.1	20.8	20.8
Adjusted profit margin	12.6	15.9	15.3	15.8	15.9
Adjusted ROAE	23.1	26.9	22.7	27.4	28.4
ROCE	19.4	23.3	19.6	23.8	25.6
Working capital days (days)					
Receivables	51	54	56	46	48
Inventory	88	100	104	80	79
Payables	36	38	41	35	38
Ratios (x)					
Gross asset turnover	3.3	2.9	2.4	2.9	3.0
Current ratio	2.1	2.1	1.6	1.7	2.0
Net interest coverage ratio	47.4	41.8	33.7	65.0	160.0
Adjusted debt/equity	0.0	(0.1)	0.1	0.0	0.0

Source: Company, BOBCAPS Research

Disclaimer

Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

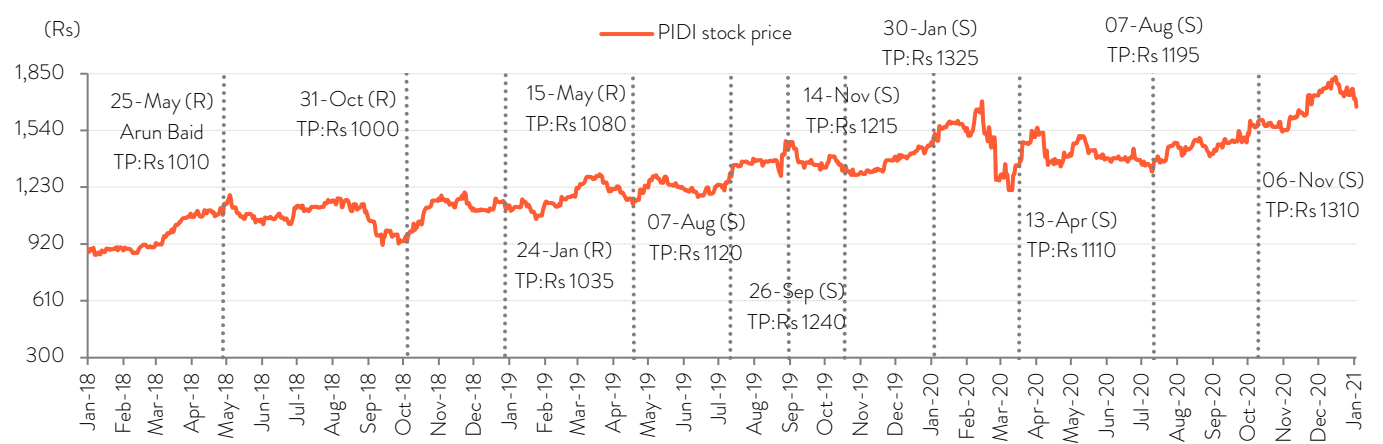
ADD – Expected return from >+5% to +15%

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)

RATINGS AND TARGET PRICE (3-YEAR HISTORY): PIDILITE INDUSTRIES (PIDI IN)



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

Rating distribution

As of 31 December 2020, out of 88 rated stocks in the BOB Capital Markets Limited (BOBCAPS) coverage universe, 43 have BUY ratings, 14 have ADD ratings, 6 are rated REDUCE and 25 are rated SELL. None of these companies have been investment banking clients in the last 12 months.

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