

Chemicals | Q1FY24 Result Update

Capex outlay intact amidst persisting challenges

- Q1FY24 performance was weak (below estimates) as revenue/ EBITDA/ PAT declined by 12%/ 28%/ 48% YoY; gradual recovery expected from H2FY24.
- Management indicated FY24 EBITDA to be lower vs. earlier guidance of 15% YoY growth. Previous FY25 guidance of Rs17bn is likely to be revised down.
- Capex outlay and timelines intact (Rs25-30bn over next 2 years) as management believes medium-long term outlook is largely unchanged and near term challenges are transient in nature.
- We assign 'Reduce' rating with TP of Rs480 (25x FY25E) as slow ramp-up of capacities on demand challenges, coupled with high cash outflows on capex to weaken balance sheet and keep return ratios subdued (<10%)

Weakness accentuates in Q1FY24

Revenue at Rs14.1bn (-12%YoY/ -15%QoQ) on volume contraction led by inventory correction across end use applications (including agrochemicals) coupled with decline in key RM prices. EBITDA at Rs2bn (-28%YoY/ -20%QoQ) and EBITDA Margin at 14.3% (-320 bps YoY/ -88 bps QoQ) were impacted by adverse operating leverage. APAT Rs0.7bn (-48%YoY/ -52%QoQ) was impacted by weaker operating performance and higher depreciation; despite low/ negligible tax in Q1 (benefit of higher tax depreciation and exemptions).

Outlook and valuation

Aarti Industries (ARTO) continues to be impacted by 1) persisting demand weakness in key end-use segments 2) slower than expected ramp-up in capacities meant for long term projects 3) elevated cost pressures on lower absorption of expansion led costs 4) stretched balance sheet on continuing capex led cash outflows. Weak performance in Q1FY24 was on restricted volumes on industry headwinds. We expect EBITDA & PAT CAGR of 16% & 13% over FY23-25E, on gradual increase in capacity utilization of recently commissioned plants (NCB expansion, two specialty chemical process blocks, 3rd long term contract and chlorination facility at Jhagadia, and Dahej phase-2). We assign 'Reduce' rating with TP of Rs 480 (25x FY25E EPS).

Q1FY24 Result (Rs Mn)

Particulars	Q1FY24	Q1FY23	YoY (%)	Q4FY23	QoQ (%)
Revenue	14,140	16,103	(12.2)	16,550	(14.6)
Total Expense	12,120	13,288	(8.8)	14,040	(13.7)
EBITDA	2,020	2,815	(28.2)	2,510	(19.5)
Depreciation	890	718	24.0	840	6.0
EBIT	1,130	2,098	(46.1)	1,670	(32.3)
Other Income	0	4	(100.0)	0	
Interest	400	445	(10.2)	330	21.2
EBT	730	1,656	(55.9)	1,340	(45.5)
Tax	20	301	(93.3)	(140)	(114.3)
RPAT	710	1,355	(47.6)	1,480	(52.0)
APAT	710	1,355	(47.6)	1,480	(52.0)
			(bps)		(bps)
Gross Margin (%)	39.7	42.5	(281)	41.9	(220)
EBITDA Margin (%)	14.3	17.5	(320)	15.2	(88)
NPM (%)	5.0	8.4	(340)	8.9	(392)
Tax Rate (%)	2.7	18.2	(1542)	(10.4)	1319
EBIT Margin (%)	8.0	13.0	(503)	10.1	(210)

*Change in lead analyst

CMP	Rs 473
Target / Upside	Rs 480 / 1%
NIFTY	19,633

Scrip Details

Equity / FV	Rs 1,813mn / Rs 5
Market Cap	Rs 172bn
	USD 2.1bn
52-week High/Low	Rs 924/ 445
Avg. Volume (no)	14,66,750
Bloom Code	ARTO IN

Price Performance	1M	3M	12M
Absolute (%)	4	(7)	(42)
Rel to NIFTY (%)	2	(14)	(56)

Shareholding Pattern

	Dec'22	Mar'23	Jun'23
Promoters	44.2	44.1	43.7
MF/Banks/FIs	14.6	14.8	14.9
FIs	12.1	12.3	12.2
Public / Others	29.2	28.9	29.3

Valuation (x)

	FY23A	FY24E	FY25E
P/E	32.4	36.2	24.5
EV/EBITDA	18.2	18.8	14.6
ROE (%)	11.2	9.4	12.8
RoACE (%)	9.1	7.9	9.5

Estimates (Rs bn)

	FY23A	FY24E	FY25E
Revenue	66.2	72.6	87.1
EBITDA	10.9	11.0	14.6
PAT	5.3	4.7	7.0
EPS (Rs.)	14.6	13.1	19.3

VP Research: Nitesh Dhoot

Tel: +9122 40969763

E-mail: niteshd@dolatcapital.com

Analyst: Tejas Sonawane

Tel: +91 22 40969792

E-mail: tejass@dolatcapital.com

Earnings call KTAs

Demand environment

- Significant demand pressure due to global destocking and slowdown in key developed markets. **Agrochemicals space saw sharp demand contraction during Q1FY24.**
- Products linked to **dyes and pigments and other discretionary uses are most impacted given prolonged demand weakness** and inventory correction.
- **Chinese dumping** of excess inventory in the global markets **resulted from an oversupply situation locally given weak demand.**
- **Demand contraction in the range of 10-20% across products/ segments.** Demand is **expected to recover starting Q3FY24** as per volume guidance given by customers.
- **Exports impacted more vs. domestic portfolio.** Exports (direct + indirect) form ~70% of its portfolio. Domestic portfolio (higher share of pharma), wasn't much impacted.
- Demand slowdown across specialty and commoditized products; **margin impact higher on commoditized products.**

Long term contracts

- 1st Long term contract (Dicamba intermediate) witnessed severe pressure owing to weak demand. While this is a specialized plant and difficult to modify, **management is evaluating if one of the two lines can be repurposed (to decide in next 2 quarters).**
- 2nd Long term contract (Specialty chemical intermediate) – No impact as **EBIDTA is assured irrespective of volume offtake**; expect full earnings in FY24.
- 3rd Long term contract – Stabilizing; **higher contribution expected in H2FY24.**

Capex Updates

- **Q1FY24 capex at Rs2.6bn**; Rs25-30bn capex outlay over next 2 years.
- **Capex timelines broadly remain intact**; no need to defer or realign any project due to ongoing challenges, which management believes are transient in nature and structural demand for chemicals from India (China+1) remains intact.
- **NCB expansion completed** (75,000mtpa to 108,000mtpa) during Q1FY24.
- New PNCB and ONCB capacities to commission in Q2FY24.
- **Nitro-toluene and ethylation** expansion progressing as per plan; expected by Q1FY25
- **First phase of Chloro-toluene (CT) and downstream capex** has an outlay of ~Rs 15bn and will be commissioned by FY25 end; further capex towards MPP's etc. to follow.
- **CT base capacity to be 42,000mtpa**; company to focus on downstreams

Debt metrics

- Gross debt of Rs30bn as on 30th June 2023, while **net debt stands at Rs 26.5bn.** Annual debt repayment target for FY24 is Rs 3.5bn.
- Secured USD10bn funding from IFC for capex initiatives. **Peak debt/ equity not to go beyond 0.7x**; also expecting release of working capital on contraction in demand.

Other highlights

- **Production figures for Q1FY24 (vs Q1FY23):** NCB at 17,293mt (vs 20515mt), hydrogenated products at 2,868tpm (vs 3,295 tpm), nitro toluene at 9327 mt (vs 5,252mt) and PDA at 135tpm (vs 375tpm).
- **FY24 effective tax rate to be <10%** given higher MAT credit.

Financial Performance

Profit and Loss Account

(Rs Mn)	FY22A	FY23A	FY24E	FY25E
Revenue	60,855	66,186	72,566	87,094
Total Expense	43,654	55,296	61,606	72,478
COGS	28,545	38,417	43,477	50,806
Employees Cost	3,570	3,853	4,644	5,661
Other expenses	11,540	13,026	13,485	16,011
EBIDTA	17,201	10,889	10,960	14,615
Depreciation	2,464	3,105	3,670	4,146
EBIT	14,737	7,785	7,290	10,470
Interest	1,023	1,683	2,020	2,240
Other Income	8	9	1	2
Exc. / E.O. items	0	0	0	0
EBT	13,722	6,111	5,270	8,232
Tax	1,862	824	527	1,235
RPAT	11,857	5,287	4,743	6,997
Minority Interest	2	0	0	0
Profit/Loss share of associates	0	0	0	0
APAT	17,967	5,287	4,743	6,997

Balance Sheet

(Rs Mn)	FY22A	FY23A	FY24E	FY25E
Sources of Funds				
Equity Capital	1,813	1,813	1,813	1,813
Minority Interest	7	7	7	7
Reserves & Surplus	43,354	47,388	50,370	55,493
Net Worth	45,167	49,201	52,183	57,306
Total Debt	25,680	28,740	36,435	45,017
Net Deferred Tax Liability	2,108	1,893	1,893	1,893
Total Capital Employed	72,961	79,841	90,518	1,04,223

Applications of Funds

Net Block	36,379	49,680	53,900	71,754
CWIP	13,030	9,890	14,000	5,000
Investments	283	172	172	172
Current Assets, Loans & Advances	28,540	25,537	27,947	33,900
Inventories	9,341	10,310	9,941	11,931
Receivables	10,915	9,405	11,929	14,317
Cash and Bank Balances	1,736	2,007	1,986	2,930
Loans and Advances	5,625	2,754	2,929	3,326
Other Current Assets	923	1,061	1,163	1,396
Less: Current Liabilities & Provisions	5,275	5,440	5,501	6,602
Payables	3,449	4,049	3,976	4,772
Other Current Liabilities	1,827	1,391	1,525	1,830
<i>sub total</i>				
Net Current Assets	23,265	20,097	22,446	27,297
Total Assets	72,957	79,839	90,518	1,04,223

E – Estimates

Important Ratios

Particulars	FY22A	FY23A	FY24E	FY25E
(A) Margins (%)				
Gross Profit Margin	53.1	42.0	40.1	41.7
EBIDTA Margin	28.3	16.5	15.1	16.8
EBIT Margin	24.2	11.8	10.0	12.0
Tax rate	13.6	13.5	10.0	15.0
Net Profit Margin	19.5	8.0	6.5	8.0
(B) As Percentage of Net Sales (%)				
COGS	46.9	58.0	59.9	58.3
Employee	5.9	5.8	6.4	6.5
Other	19.0	19.7	18.6	18.4
(C) Measure of Financial Status				
Gross Debt / Equity	0.6	0.6	0.7	0.8
Interest Coverage	14.4	4.6	3.6	4.7
Inventory days	56	57	50	50
Debtors days	65	52	60	60
Average Cost of Debt	3.8	6.2	6.2	5.5
Payable days	21	22	20	20
Working Capital days	140	111	113	114
FA T/O	1.7	1.3	1.3	1.2
(D) Measures of Investment				
AEPS (Rs)	49.6	14.6	13.1	19.3
CEPS (Rs)	56.4	23.1	23.2	30.7
DPS (Rs)	3.5	2.5	0.7	1.0
Dividend Payout (%)	7.1	17.2	5.0	5.0
BVPS (Rs)	124.6	135.7	144.0	158.1
RoANW (%)	29.6	11.2	9.4	12.8
RoACE (%)	18.3	9.1	7.9	9.5
RoAIC (%)	21.8	10.4	8.8	11.0
(E) Valuation Ratios				
CMP (Rs)	473	473	473	473
P/E	9.5	32.4	36.2	24.5
Mcap (Rs Mn)	1,71,537	1,71,537	1,71,537	1,71,537
MCap/ Sales	2.8	2.6	2.4	2.0
EV	1,95,481	1,98,270	2,05,986	2,13,624
EV/Sales	3.2	3.0	2.8	2.5
EV/EBITDA	11.4	18.2	18.8	14.6
P/BV	3.8	3.5	3.3	3.0
Dividend Yield (%)	0.7	0.5	0.1	0.2
(F) Growth Rate (%)				
Revenue	35.1	8.8	9.6	20.0
EBITDA	75.2	(36.7)	0.6	33.4
EBIT	96.4	(47.2)	(6.4)	43.6
PBT	106.5	(55.5)	(13.8)	56.2
APAT	243.2	(70.6)	(10.3)	47.5
EPS	243.2	(70.6)	(10.3)	47.5

E – Estimates

Cash Flow

Particulars	FY22A	FY23A	FY24E	FY25E
Profit before tax	13,720	6,110	5,270	8,232
Depreciation & w.o.	2,460	3,100	3,670	4,146
Net Interest Exp	1,020	1,680	2,019	2,238
Direct taxes paid	(2,460)	(910)	(498)	(1,169)
Change in Working Capital	(9,560)	3,120	(2,399)	(3,972)
Non Cash	(10)	(10)	0	0
(A) CF from Operating Activities	5,170	13,090	8,063	9,474
Capex {(Inc.)/ Dec. in Fixed Assets n WIP}	(11,650)	(13,260)	(12,000)	(13,000)
Free Cash Flow	(6,480)	(170)	(3,937)	(3,526)
(Inc.)/ Dec. in Investments	(50)	(40)	0	0
Other	10	0	1	2
(B) CF from Investing Activities	(11,690)	(13,300)	(11,999)	(12,998)
Issue of Equity/ Preference	11,870	0	0	0
Inc./(Dec.) in Debt	(5,460)	3,002	7,695	8,582
Interest exp net	(1,020)	(1,680)	(2,020)	(2,240)
Dividend Paid (Incl. Tax)	(1,270)	(910)	(237)	(350)
Other	69	3	(1,524)	(1,524)
(C) CF from Financing	4,189	415	3,913	4,468
Net Change in Cash	(2,331)	205	(23)	944
Opening Cash balances	4,135	1,804	2,010	1,987
Closing Cash balances	1,804	2,010	1,987	2,931

E – Estimates

Notes

DART RATING MATRIX

Total Return Expectation (12 Months)

Buy	> 20%
Accumulate	10 to 20%
Reduce	0 to 10%
Sell	< 0%

DART Team

Purvag Shah	Managing Director	purvag@dolatcapital.com	+9122 4096 9747
Amit Khurana, CFA	Head of Equities	amit@dolatcapital.com	+9122 4096 9745

CONTACT DETAILS

Equity Sales	Designation	E-mail	Direct Lines
Dinesh Bajaj	VP - Equity Sales	dineshb@dolatcapital.com	+9122 4096 9709
Kapil Yadav	VP - Equity Sales	kapil@dolatcapital.com	+9122 4096 9735
Jubbin Shah	VP - Equity Sales	jubbins@dolatcapital.com	+9122 4096 9779
Girish Raj Sankunny	VP - Equity Sales	girishr@dolatcapital.com	+9122 4096 9625
Pratik Shroff	AVP - Equity Sales	pratiks@dolatcapital.com	+9122 4096 9621
Equity Trading	Designation	E-mail	
P. Sridhar	SVP and Head of Sales Trading	sridhar@dolatcapital.com	+9122 4096 9728
Chandrakant Ware	VP - Sales Trading	chandrakant@dolatcapital.com	+9122 4096 9707
Shirish Thakkar	VP - Head Domestic Derivatives Sales Trading	shirisht@dolatcapital.com	+9122 4096 9702
Kartik Mehta	Asia Head Derivatives	kartikm@dolatcapital.com	+9122 4096 9715
Bhavin Mehta	VP - Derivatives Strategist	bhavinm@dolatcapital.com	+9122 4096 9705

Dolat Capital Market Private Limited.

Naman Midtown, A-1203, 12th Floor, Senapati Bapat Marg, Prabhadevi, Mumbai 400013

Analyst(s) Certification

The research analyst(s), with respect to each issuer and its securities covered by them in this research report, certify that: All of the views expressed in this research report accurately reflect his or her or their personal views about all of the issuers and their securities; and No part of his or her or their compensation was, is, or will be directly or indirectly related to the specific recommendations or views expressed in this research report.

I. Analyst(s) and Associate (S) holding in the Stock(s): (Nil)

II. Disclaimer:

This research report has been prepared by Dolat Capital Market Private Limited. to provide information about the company(ies) and sector(s), if any, covered in the report and may be distributed by it and/or its affiliated company(ies) solely for the purpose of information of the select recipient of this report. This report and/or any part thereof, may not be duplicated in any form and/or reproduced or redistributed without the prior written consent of Dolat Capital Market Private Limited. This report has been prepared independent of the companies covered herein. Dolat Capital Market Private Limited. and its affiliated companies are part of a multi-service, integrated investment banking, brokerage and financing group. Dolat Capital Market Private Limited. and/or its affiliated company(ies) might have provided or may provide services in respect of managing offerings of securities, corporate finance, investment banking, mergers & acquisitions, financing or any other advisory services to the company(ies) covered herein. Dolat Capital Market Private Limited. and/or its affiliated company(ies) might have received or may receive compensation from the company(ies) mentioned in this report for rendering any of the above services. Research analysts and sales persons of Dolat Capital Market Private Limited. may provide important inputs to its affiliated company(ies) associated with it. While reasonable care has been taken in the preparation of this report, it does not purport to be a complete description of the securities, markets or developments referred to herein, and Dolat Capital Market Private Limited. does not warrant its accuracy or completeness. Dolat Capital Market Private Limited. may not be in any way responsible for any loss or damage that may arise to any person from any inadvertent error in the information contained in this report. This report is provided for information only and is not an investment advice and must not alone be taken as the basis for an investment decision. The investment discussed or views expressed herein may not be suitable for all investors. The user assumes the entire risk of any use made of this information. The information contained herein may be changed without notice and Dolat Capital Market Private Limited. reserves the right to make modifications and alterations to this statement as they may deem fit from time to time. Dolat Capital Market Private Limited. and its affiliated company(ies), their directors and employees may; (a) from time to time, have a long or short position in, and buy or sell the securities of the company(ies) mentioned herein or (b) be engaged in any other transaction involving such securities and earn brokerage or other compensation or act as a market maker in the financial instruments of the company(ies) discussed herein or act as an advisor or lender/borrower to such company(ies) or may have any other potential conflict of interests with respect to any recommendation and other related information and opinions. This report is neither an offer nor solicitation of an offer to buy and/or sell any securities mentioned herein and/or not an official confirmation of any transaction. 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 Dolat Capital Market Private Limited. and/or its affiliated company(ies) 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 a certain category of investors. Persons in whose possession this report may come, are required to inform themselves of and to observe such restrictions.



Dolat Capital Market Private Limited.

Corporate Identity Number: U65990GJ993PTC116741

Member: BSE Limited and National Stock Exchange of India Limited.

SEBI Registration No: BSE - INZ000274132, NSE - INZ000274132, Research: INH000000685

Regd. office: 1401-1409, Dalal Street Commercial, Block 53 (Bldg. No.53E) Zone-5, Road-5E, Gift City, Sector 9, Gandhinagar-382355 Gujarat, India.

Board: +9122 40969700 | Fax: +9122 22651278 | Email: research@dolatcapital.com | www.dolatresearch.com
