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The Trick Is To  
**Spot Them** At The  
**Larval Stage**

BSE Code	: 506579
Time Duration	: 1 year
CMP	: ₹1292 (as on 23 November, 2017)
Target Price	: ₹1758

## Oriental Carbon and Chemicals VROOMING ON THE INSOLUBLE SULPHUR ROAD

Our Tiny Treasure for the month of November is Oriental Carbon and Chemicals, a Duncan JP Goenka group company. The company's product portfolio includes insoluble sulphur (93% of the revenue), sulphuric acid and olems (7% of the revenue) which are used in different grades for the tyre industry. It is one of the leaders in the production of insoluble sulphur and has a domestic market share of 55% and global market share of 10%. The company has expanded its capacity of insoluble sulphur from 3,000 MT in 1994 to 28,500 MT by Q1FY18. It has relationships with major tyre OEMs such as Apollo tyres, Bridgestone, Ceat, Goodyear, MRF etc. Company's return on equity is ~17.4% and its D/E is low at 0.3x.

### Industry growth to be driven by high performance tyres and radialisation

The growth of Oriental Carbon and Chemicals' insoluble sulphur is dependent on the growth of the tyre industry. Players like Apollo Tyres are planning capex to expand capacity. Also, most of the tyre companies have just completed expansion of capacities and are expecting high utilisation of the new capacities.

Apollo Tyre has capex plans of ~Rs 3,200cr-Rs 3,700cr for domestic and Rs1,500cr for the European market over 12-18 months. Also, imposition of anti-dumping duty on Chinese tyres will benefit the domestic tyre manufactures like Ceat, Apollo Tyres and JK Tyres.

The demand for sulphuric acid is driven by demand for fertilisers. The fertiliser industry has been battling with higher inventory up to Q4FY17. The inventory has, however, become lean and with normal monsoon, we expect refilling to boost demand. Sulphuric acid being a raw material for fertilisers is expected to see positive demand trends.

Also, with increase in radialisation, we expect demand for insoluble rubber to grow at higher rate with larger quantity of sulphur needed in high performance tyres.

### Capacity expansion

The company announced its intention to expand capacity at its Mundra plant for insoluble sulphur from 23,000MTPA in FY16 to 34,000MTPA by FY18. It has already completed the first phase of expansion of 5,500MT by Q1FY18 and the plant has commenced operations. For this, company has planned capex of Rs 63 crore,

which will be funded through debt and equity in the ratio of 2:1. The work on second phase of capacity expansion of insoluble sulphur at its Mundra plant is under progress and expected to be commissioned on schedule in the second quarter of 2018-19.

The company also expects to reap benefit of being in SEZ and expects lower tax on the new facility.

Mundra plant is also near to the port, which will reduce its logistics cost and considering that 70% of its sales are from exports, it makes it a strategic fit. Also, we expect higher margins as insoluble sulphur consumes higher electricity and Mundra plant will attract lower power tariffs due to its location.

### Sulphuric acid plant to turn profitable

The company's sulphuric acid capacity increased from 30,000 MTPA in 1974 to 46,000 MTPA in 2017. With higher utilisation and better demand, the company expects sulphuric acid plant to turn profitable. This will be driven by higher capacity utilisation and utilising its by-product steam for manufacturing insoluble sulphur.

With this plant turning profitable, we expect margins to expand by FY18. Also, the company expects self-sufficiency of steam for its plant at Dharuhera.

### Entry into new markets

The company is present in 21 countries and has relationships with 40-plus customers. It has been eyeing opportunities in the international markets. Since the company derives 71% of revenue from exports, it is constantly looking at new markets. It has expanded its footprint in China and the US and is seeing green shoots in these markets and expects these markets to be major growth drivers going forward. North America is the largest market for Insoluble sulphur with potential for growth.

### Financial performance

The company's revenue grew by 6.6% YoY in FY17 with a growth of about 9% in insoluble sulphur sales. The growth was achieved consequent to commissioning of the new line at Mundra SEZ in December 2016. The additional sales were mainly due to increase in domestic demand and increase in exports, which were mainly due to the addition of new geographies. The sales volume growth was in double digits in both the markets. The company's EBITDA

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grew by 7.4% YoY in FY17 with margins increasing from 24.3% in FY16 to 24.5% in FY17, due to better capacity utilisation. Its net profit grew marginally by 1.9% YoY in FY17. Its debt-equity ratio has improved from 0.8x in FY12 to 0.29x in FY17. Interest coverage ratio also improved from 6.35x in FY12 to 15.3x in FY17.

### Valuation and outlook

Oriental carbon and chemical is currently trading at 25.09x on TTM basis and P/B of 3.84x. We believe company is trading at par with its peers like phillip carbon black but has higher margins and

RoE and hence can attract premium. Also, considering its expansion and exposure to export markets we see it as a player who can benefit the most from industry shift towards high performance tyres.

We recommend investors to BUY the script with a potential upside of 36% from current levels to reach TP of Rs.1758 over a period of one year. However, they being in commodity business, the margins can vary in coming quarters and hence would urge investors to invest in three tranches.

### Inc/Exp Statement(Standalone) (Rs in Crore)

Description	201703	201603	201503	201403	201303
Net Sales	297.45	274.72	282.57	261.70	225.44
Total Income	304.05	280.40	295.43	265.19	230.32
Total Expenditure	210.18	193.64	211.29	193.55	167.89
PBIDT	93.87	86.76	84.14	71.64	62.43
PAT	53.43	52.99	51.32	40.44	27.38
Dividend %	100.00	85.00	85.00	70.00	50.00
Adj. EPS(Rs)	51.90	51.46	49.84	39.28	26.60

### Quarter On Quarter (Standalone) (Rs in Crore)

Particulars	201706	201703	Q on Q Var%	201606	Y on Y Var%
Net Sales	81.23	85.60	-5.10	78.78	3.10
Total Expenditure	55.78	60.76	-8.20	56.63	-1.50
PBIDT (Excl OI)	25.45	24.84	2.46	22.16	14.88
PAT	14.56	9.30	56.53	14.53	0.21
PBIDTM% (Excl OI)	31.33	29.02	7.96	28.12	11.42
PBIDTM%	32.73	30.38	7.74	29.60	10.57
PATM%	17.92	10.86	65.01	18.44	-2.82
Adj. EPS(Rs)	14.12	9.02	56.54	14.09	0.21

