



The Trick Is To Spot Them At The Larval Stage

BSE Code	: 506854
Time Duration	: 1 year
CMP	: ₹185.50 (as on 23 May, 2019)
Target Price	: ₹242

Tanfac Industries Capitalising On The Demand-Supply Gap

Our Tiny Treasure for the month of May is Tanfac Industries Limited. It is joint sector company promoted by Aditya Birla Group and Tamil Nadu Industrial Development Corporation (TIDCO). It is amongst the leading producers of hydrofluoric acid (HF) and its derivatives, sulphuric acid and aluminium fluoride (ALF).

A major turnaround in the company's operations has been seen since last 2-3 years as the company has been focusing on developing its product mix which are generating higher margins and, thereby, its market share in speciality fluorides has been rising.

The partial transfer of supply of sulphuric acid due to shutdown of Sterlite copper plant to other domestic companies like Tanfac has led to company generating higher realisations and margins. The shutdown of chemical plants in China has also led to price hike, which is benefiting the company. FY18 and FY19 have been exceptional years for the company considering its stellar financial performance. However, the net profit in March quarter of FY19 declined as the company recognised impairment loss, which is a one-time event. Although adverse reaction is seen on the company's stock price, we see this as an opportunity to enter, considering that the strong trend in demand is expected to continue in the near term.

Turnaround in HF and ALF segment

Over the last 15 years, China has become the largest producer of fluorochemicals in the world by increasing its production capacity manifold. However, in the last two years, due to the shutdown of various chemicals plants, the overall production level and supply from China has declined. Even though the prices of key raw materials like fluorspar and sulphur have increased, the profitability of the company in HF and ALF segments has increased due to higher volumes and higher realisations. Tanfac, along with its nearest competitor, cater to 14% demand in the domestic market. Thus, it has huge scope for growth and to substitute imports from China. Also, the company's continuous focus and penetration in value-added products like photovoltaic and specialty grade HF markets has led to rise in profits. In FY18, it undertook contract manufacturing for products like poly aluminium chloride (PAC) and purified acetic acid, leading to growth in revenues. It is planning replacement capex of ~Rs 12 crore in

FY20, which will result in improved capacity utilisation. The capex will be partly funded by debt, yet the capital structure is expected to remain healthy.

Sulphuric acid segment contributing to higher margins

The company's revenues of ~20% are generated from the sulphuric acid segment. The Sterlite copper plant at Thoothukudi, Tamil Nadu, has been shut down since March 2018, firstly for maintenance purposes. However, since May 2018, the state government has ordered for its shutdown due to environmental issues raised by the residents living in the vicinity of the plant. Due to the shutdown, the prices of sulphuric acid have risen considering the scenario of decline in supply and rising demand. Tanfac Industries has benefited from this, leading to higher revenues and operating margins generated from this segment. Looking at the current developments regarding the copper plant shutdown, it seems the matter would take some time to get resolved due to legal issues. Further, the company has also benefited from the shift to usage of lower cost molten sulphur and other cost control measures.

ICRA ratings upgrade

In March 2019, ICRA upgraded the ratings for the company to a 'stable' outlook, considering the improvement in its financial profile. The stable outlook reflects ICRA's expectation that the company's credit profile will remain healthy in the near to medium term, aided by favourable market conditions. On the back of improved profitability, the company has repaid the ICD availed from group entities, which has led to improvement in capital structure and coverage indicators.

Positive demand outlook for Tanfac's products

The outlook for demand for HF seems to be positive in the long run across the globe. The market is expected to grow at CAGR of 5.5% between 2018 to 2023. The global hydrofluoric acid market is dominated by anhydrous content, i.e. AHF is used for manufac-

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turing of fluorochemicals. The diluted form of HF is used for applications like steel pickling and metal processing industry, rust remover, printed circuit boards, etc. It is also used to improve the fuel efficiency in the alkylation process in the petrochemical industry. ALF is used as a flux in reducing the melting point of alumina in the electrolytic process of manufacturing aluminium. The global ALF market is expected to grow at CAGR of 4.6% over 2018-2028. The speciality fluorides are sold to diverse customers, such as alloy manufacturers, pharmaceutical and agrochemical companies. Sulphuric acid is mainly used in the manufacture of fertilisers, and considering the stable outlook of agriculture, the sulphuric acid market in India is expected to grow at CAGR of 3.35% over 2016-25.

Stellar Financial Performance

Tanfac Industries' standalone revenue for Q4FY19 came in at Rs. 53.93 crore as against Rs. 47.74 crore in the corresponding quarter last year, registering 13% yoy increase. The EBITDA for the quarter rose by 127% yoy to Rs. 10.69 crore as against Rs. 4.71 crore in the corresponding quarter last year, with a corresponding margin expansion of 996 bps. EBITDA margin for the quarter

stood at 19.8%. The PAT for the quarter came in at Rs. 3.29 crore as against Rs. 2.29 crore in the corresponding quarter last year, yoy increase of 43.7%. Depreciation in this quarter was exceptionally high as the impairment provision for intangible asset in 2012-13 was recognised during this period.

Looking at the FY19 numbers, the revenue jumped by 34% to Rs. 221.71 crore, while EBITDA rose by 154.1% to Rs. 51.76 crore. Further, the company reported net profit of Rs.35.96 crore, up 271.9% yoy. The debt-equity ratio has improved tremendously from 16.5x in FY17 to 0.24x in FY19.

Valuation

The company is trading at TTM P/E of 5.9x with TTM EPS of Rs 35.05. Tanfac has a backing from strong business group such as the Aditya Birla Group. The prices of not only sulphuric acid but also fluorine-based chemicals are rising, which is collectively contributing to company's growth story. The shutdown in China and growing demand in India will continue to be beneficial for the company. We see potential upside of 30% with target price of Rs 242 over a period of one year. We urge investors to make investment in a staggered manner.

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

Description	201903	201803	201703	201603	201503
Net Sales	221.71	161.88	126.39	133.32	119.92
Total Income	222.65	162.21	127.14	133.68	120.20
Total Expenditure	181.02	140.88	111.91	124.57	111.97
PBIDT	41.63	21.33	15.23	9.11	8.24
PAT	35.96	9.68	3.29	0.40	-5.29
Adj. EPS(Rs)	36.06	9.70	3.30	0.40	-5.30

Quarter On Quarter (Standalone) (Rs in Crore)

Particulars	201903	201812	Q on Q Var%	201803	Y on Y Var%
Net Sales	53.94	57.09	-5.52	47.75	12.95
Total Expenditure	43.24	45.04	-4.00	43.02	0.51
PBIDT (Excl OI)	10.69	12.05	-11.22	4.73	126.14
PAT	3.30	7.88	-58.18	2.30	43.60
PBIDTM% (Excl OI)	19.83	21.10	-6.02	9.90	100.30
PBIDTM%	21.42	21.10	1.52	10.22	109.59
PATM%	6.11	13.81	-55.76	4.81	27.03
Adj. EPS(Rs)	3.31	7.90	-58.10	2.30	43.91

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