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VALUE PICK
CHASING VALUE, NOT PRICES

Company Name	:	**VINATI ORGANICS**
BSE Code	:	**524200**
Time Duration	:	**1 year**
CMP	:	**₹1155 (as on 11 Oct., 2018)**
Target Price	:	**₹1421**

The Value Pick for the month of October is Vinati Organics Limited (VOL). It is a specialty chemical company focusing on manufacturing specialty chemicals and organic intermediaries. The company is the market leader in key segments and generates 88-90% of revenue from ATBS, IB and IBB products. It has presence in over 22 countries and more than two-third of the revenue comes from exports.

The growth drivers for the company includes the ever-increasing global demand for ATBS in oil recovery and water treatment segments for which the company has planned capacity expansion. Also, the exit of its competitor Lubrizol has thrown open opportunities to increase its market share. The commercial production of butylphenol project from April 2019 would add to the top line of the company. The new product PAP too has a huge potential to drive the company's top line in the upcoming years. Also, as the company is majorly driven by exports, the current rupee depreciation would benefit the company up to some extent.

ATBS – major revenue driver

VOL is the largest manufacturer of ATBS in the world and the only manufacturer in India. It contributes about 50% to the overall revenue of the company. ATBS is used in the manufacture of polymers, which are further used in water treatment, oil recovery, personal care etc. Developed countries like USA, Canada, France, Germany, Norway, Sweden, among others, have witnessed robust demand in personal care sector which has driven the ATBS market.

Lubrizol, one of the global competitors of VOL, had 20% market share of ATBS globally. However, the ATBS segment contributed only about 1% of its total revenue. Hence, it exited from the business in December 2017. This led to an increase in the market share for the company from 45% to 60% in such a short span of time. The volumes increased by 20% and are expected to grow additionally by 20% in FY19.

In terms of volume and value, the ATBS segment grew 25% and 35%, respectively, on a YoY basis in FY18. Thus, due to exit of Lubrizol and growing global demand, VOL has planned to increase the ATBS capacities from 26,000 tonnes to 40,000 tonnes by incurring capex of Rs 80 crore. The enhanced capacity would become operational by April 2019. Thus, the top line is set to increase from FY20 onwards.

Butylated phenols – another major revenue driver

The butylphenol project is expected to come on stream by April 2019. In FY20, the capacity utilisation would be around 60-65% and would increase to 100% in FY21. The management is estimating to clock in sales of Rs.350 crore to Rs.400 crore from this project. The company has incurred capex of Rs 240 crore for this project. It is used as raw material in various industries such as fragranced perfumes and for adhesives, coating resins, insulating varnishes, etc.

PAP – New product with high potential

The company plans to launch new product named PAP (para amino phenol) for which it has set up a prototype pilot plant. It has been successfully demonstrated at the lab level and the company is running trials on the pilot plant, which will take another three to six months. Post the trial runs, the company would be able to decide the timeline for commercialisation of the project. The capex planned for this project is around Rs 600 crore. The management has estimated an investment-asset turnover of 1:1, which implies that with an investment of Rs 600 crore, the company has revenue potential of Rs 600 crore. The PAP is used in cosmetics and other personal care products. Also, it is used as pharmaceutical intermediate, rubber antioxidant, dyes and others.

Isobutyl benzene (IBB) – stable performance

The company's another core product after ATBS is Isobutyl benzene (IBB). VOL is the largest manufacturer of IBB in the world and holds 70% market share. IBB is the primary raw material for Ibuprofen and is a widely used drug in the US, Europe and Asia. BASF, which is the biggest client for IBB, has shut down its facility in the US leading to higher Ibuprofen prices. The first half of FY19 went flat due to the shutdown, but the company would cover up in the second half of FY19. Also, it has increased the IBB capacity

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from 16,000 tonnes to 25,000 tonnes in FY18, which would cater to the demand over the next 3-5 years. On volume basis, it expects double digit growth, i.e. around 15% in FY20.

Effect of rupee depreciation and rising crude oil prices

VOL's major revenue comes in USD. Its raw materials are also priced in USD. Thus, considering the imports and the locally sourced raw materials, the company's 25% of the overall revenues are exposed to the exchange rate fluctuation. So, if the rupee over six months has appreciated about 10-11%, the overall impact on the revenue would be about 2 to 3% in a positive way. VOL's raw materials significantly depend on crude. Yet, VOL's cost-plus pricing for the customers and fixed margins in terms of dollar per kg gives it advantage to cope up with volatility in crude oil prices. Although the prices of its raw materials like MTBE abd ACN rose by 28% and 52% YoY, respectively, the impact was negligible on margins due to better product mix.

Management estimates

The company's EBITDA margin stood at 27-28% for FY18. As ATBS is a high margin product and until butyl phenol comes into stream, the blended margin at the EBITDA level is expected to be in the range of 35% over three years. Moreover, the company expects revenue in the range of Rs 1,500-1,700 crore in the next three years, with 20-25% revenue growth in topline during FY19.

Financial Performance

As the company operates on cost-plus basis with customers, it passes on the raw material costs to its customers. Thus, the operating efficiency has improved in FY18 and Q1FY19 with stable margins. Also, the company has been debt-free over the last few years and would fund its capacity expansions through internal accruals.

In Q1FY19, the company's revenue was up by 43.6% YoY from Rs 184.4 cr to Rs 264.7 cr driven by strong volume growth of its main products. Its EBITDA for the quarter increased by 84% YoY from Rs 50 cr to Rs 92 cr. The EBITDA margin jumped from 27% to 35% on a YoY basis. The PAT has doubled from Rs 31.05 cr to Rs 64.22 cr in Q1FY19. The PAT margin too jumped from 16.8% to 24.3% on YoY basis.

Valuation

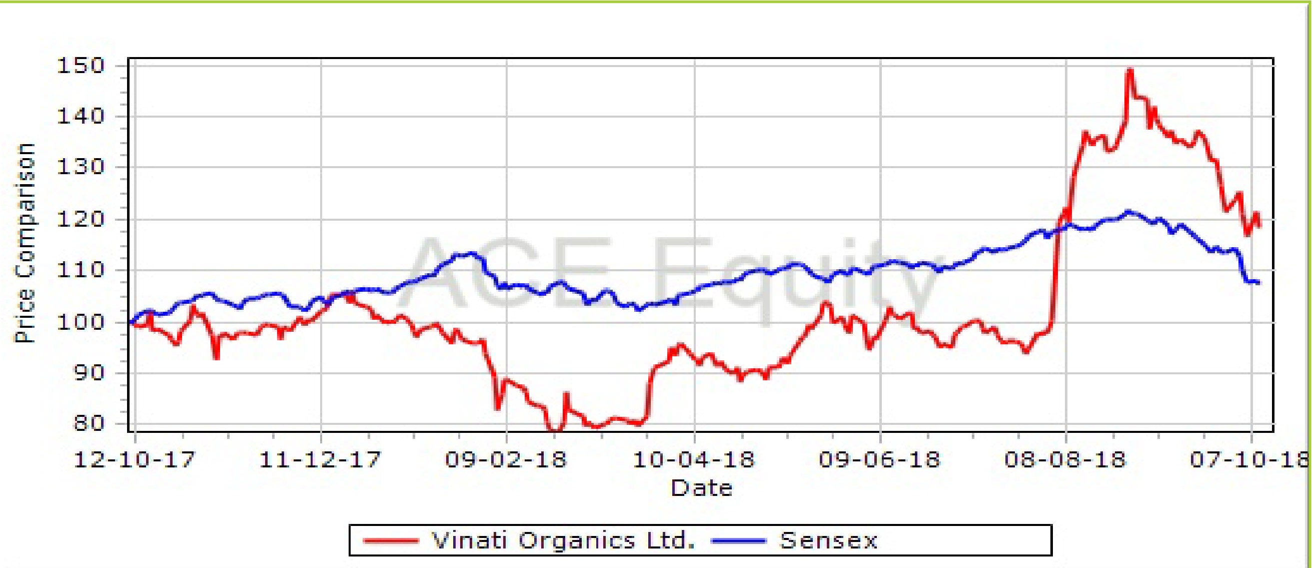
The company is trading at TTM P/E of 33.9x with TTM EPS of 34.45. It has delivered ROE and ROCE of 19.49% and 27.5%, respectively, in FY18. Considering the robust Q1FY19 performance, strong demand for ATBS globally, new capacity expansion plans for ATBS and butylphenol and launch of new products, we see that the company has a huge potential for growth in the upcoming 2-3 years. We see a potential upside of 23% with a target price of Rs 1421 over a period of one year. We urge investors to make investment in three tranches.

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

Description	201803	201703	201603	201503	201403
Net Sales	743.36	640.79	630.95	771.73	696.13
Total Income	760.38	653.28	637.11	780.87	705.30
Total Expenditure	531.47	422.95	424.17	579.96	543.24
PBIDT	228.91	230.32	212.93	200.91	162.06
PAT	143.88	140.28	131.57	115.79	86.15
Dividend %	225.00	25.00	200.00	175.00	150.00
Adj. EPS(Rs)	28.00	27.19	25.50	22.44	17.45

Quarter On Quarter (Standalone) (Rs in Crore)

Particulars	201806	201803	Q on Q Var%	201706	Y on Y Var%
Net Sales	264.75	212.61	24.52	196.94	34.43
Total Expenditure	173.00	147.65	17.17	146.75	17.89
PBIDT (Excl OI)	91.74	64.96	41.23	50.19	82.78
PAT	64.26	51.91	23.78	31.10	106.63
PBIDTM% (Excl OI)	34.65	30.55	13.42	25.49	35.94
PBIDTM%	39.22	34.20	14.68	27.52	42.51
PATM%	24.27	24.42	-0.61	15.79	53.70
Adj. EPS(Rs)	12.50	10.10	23.76	6.03	107.30



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