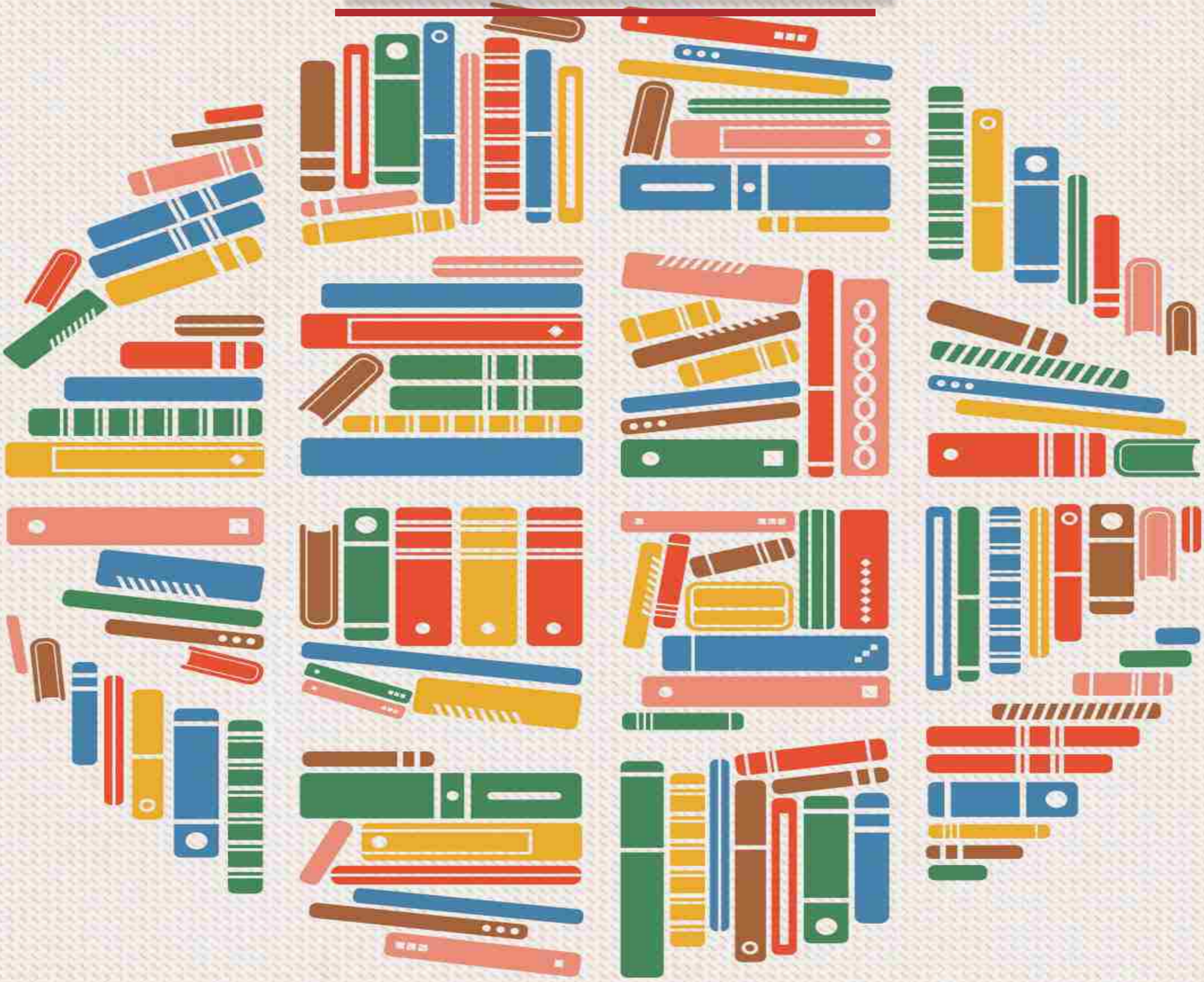
ICICI direct Research

September 16, 2019

Stock TALES



Stock Tales are concise, holistic stock reports across wider spectrum of sectors. Updates will not be periodical but based on significant events or change in price.

Tata Chemicals (TATCHE)

CMP: ₹ 597 | Target: ₹ 690 (16%) | Target Period: 12 months | BUY

September 16, 2019

Residual business available at attractive valuations…

Commencing operation in 1944 as a soda ash manufacture in India, Tata Chemicals (TCL) has come a long way to become one of the top five players in the global soda ash market. The company forayed into different business verticals (agrochemicals, HDS, neutraceuticals & consumer business) coupled with expansion of the base business across different markets over the period. Going ahead, we expect incremental utilisation of new capex at India basic chemical unit along with emerging businesses like HDS, nutrition to drive the performance. Furthermore, **the nutrition business has RoCE of 18-20% against base business RoCE of ~10%. Thus, increasing contribution from nutrition is expected to drive group return rations and thereby valuations. Apart from this, we believe demerger of consumer business provides base business of TCL at ₹ 301/share vs. fair value of ₹ 395/share. We have a BUY rating on Tata Chemicals.**

Global demand supply dynamics may support steady base operations

The global soda ash market has been operating at 91% utilisation. Assuming production levels remain the same as FY19 and with no major plans of capacity addition, except GHCL and TCL, we expect global soda ash capacity utilisation to reach ~87% by FY23E. Historically, average utilisation level is 83-84% commensurate with average US FOB price of $205/MT & China FOB of $240/MT, against prevailing FOB price at $223/MT & $265/MT, respectively. Hence, 4-5% cut in utilisation may not meaningfully impact the realisations/tonne as witnessed in the past. On the other hand, lower input cost along with a change in mix towards value added products and control over other costs can either maintain or improve its EBITDA/tonne.

Emerging specialty business to drive performance ahead

TCL entered the HDS and nutrition business with a combined capex of ₹ 565 crore. Assuming asset turn of 1x with average OPM of 18-20% can translate into EBITDA of ₹ 100 crore (~5% of present EBITDA) in the medium term. Further, TCL also commenced recovery of cathode material from lithium-ion cells/batteries on a pilot basis. This can be an attractive long term proposition for a shift towards specialised chemistry as the domestic market opportunity size for the same is pegged at ~₹ 1500 crore initially *(refer page no. 11 for detail).*

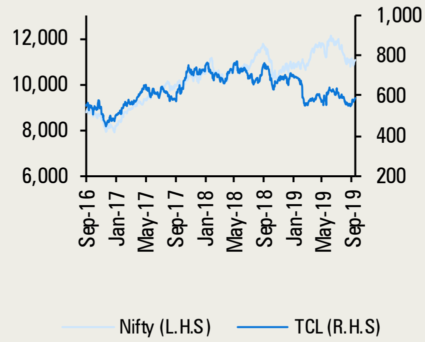
Valuation and outlook

We value TCL India's basic chemical at EV/EBITDA of 5x FY21E and the ROW basic chemical at EV/EBITDA of 4x FY21E, translating into a fair value of basic chemical business at ₹ 272/share. Apart from this, other businesses with investment in group companies account for another ₹ 123/share leading to a residual business target price of ₹ 395/share. Adding consumer business value of ₹ 295/share (1.14 x TGBL CMP), we arrive at a target of ₹ 690/share, a potential upside of ~16%. We have a **BUY** recommendation on TCL.

Particulars

Particular	Amount
Market cap (₹ Crore)	15,200
Total Debt (₹ Crore)	6,138
Cash & Inv (₹ Crore)	4,205
EV (₹ Crore)	17,133
52 Week H/L	762/544
Equity Capital (₹ Crore)	254.8
Face Value (₹)	10

Price Performance



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Key Financial Summary

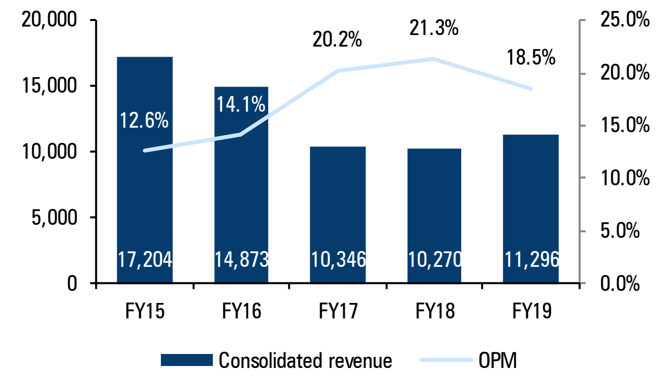
(₹ Crore)	FY16	FY17	FY18	FY19	FY20E	FY21E	CAGR FY19-21E
Net Revenue	14,872.9	10,346.1	10,269.7	11,296.3	11,731.1	12,474.5	5.1
EBITDA	2,091.7	2,094.3	2,190.7	2,095.1	2,387.1	2,644.5	12.4
EBITDA Margins (%)	14.1%	20.2%	21.3%	18.5%	20.3%	21.2%	
Adj.PAT	696.4	879.6	1,290.6	1,163.9	1,220.0	1,395.0	9.5
Adj. EPS (₹)	27.3	34.5	50.6	45.7	47.9	54.7	
EV/EBITDA	10.8x	8.8x	7.4x	7.7x	6.9x	6.4x	
P/E	21.8x	17.3x	11.8x	13.1x	12.5x	10.9x	
ROE (%)	10.2	11.1	11.6	9.4	9.5	10.3	
ROCE (%)	8.7	9.7	8.3	8.4	9.0	9.9	

Company Background

Tata Chemicals (TCL) offers solutions across basic chemical, consumer products and speciality chemical segment. Under basic chemical, TCL offers soda ash, soda bicarbonate, cement, salt, marine chemicals and crushed refined soda. TCL is a leading global chemical player with around 4.2 million metric tonnes (MMT) of soda ash and 0.24 MMT of sodium bicarbonate capacities. Under the consumer product segment, the company offers salt, pulses, spices, etc, while speciality chemical consists solution towards agro chemical through Rallis and other specialty solutions such as nutritional products and HDS. Post complete exit from fertiliser business in FY16, TCL witnessed an improvement in the operational performance and working capital. Going ahead, increase in the share of nutritional business is expected to drive return ratios for the company. The company recently announced a demerger of its consumer business from its portfolio. However, it will continue to manufacture salt & supply to Tata Global Beverages.

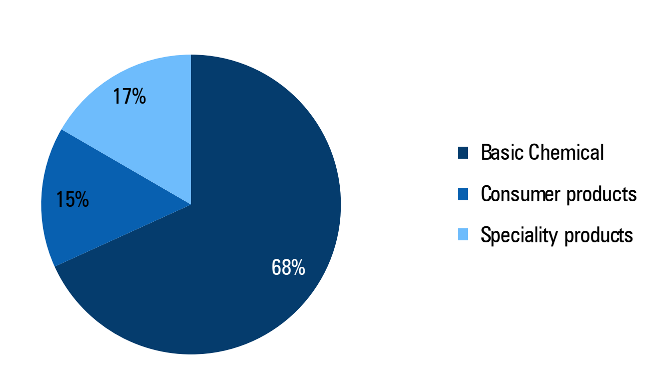
Post exiting fertilisers, TCL's revenue grew at 4% CAGR in FY17-19 while OPM improved from 14.1% in FY16 to 18.5% in FY19. In terms of segmental revenue break-up, basic chemical segment forms 68% followed by specialty chemical (17%) and consumer products (15%) in FY19.

Exhibit 1: Revenue (₹ crore) & OPM (%)



Source: Company, ICICI Direct Research

Exhibit 2: Revenue breakup in FY19



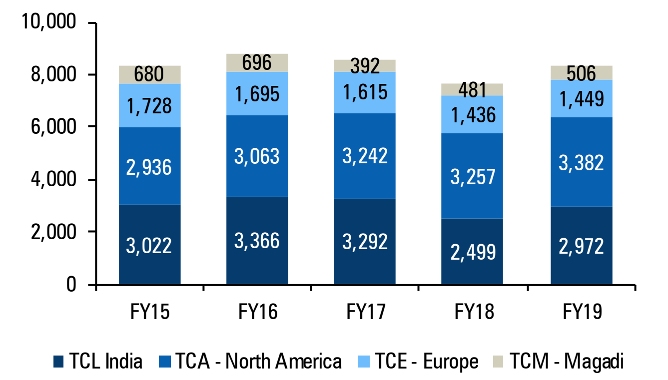
Source: Company, ICICI Direct Research

Basic chemical segment

TCL's operations are spread across India (Tata Chemicals), US (Tata Chemicals North America), UK (Tata Chemicals Europe) and Kenya (Tata Chemicals Magadi). Both the US and Kenya units produce natural soda ash. Both these plants have access to huge raw materials resources – the US plant is in Wyoming that has the world's largest deposits of trona. The Kenya plant is near Magadi Lake, which is a regenerating lake. On the other hand, Europe and India produce soda ash through the Solvay process. These two units also manufacture sodium bicarbonate.

The basic chemical segment contributed 68% to overall revenues in FY19. Of the overall basic chemical, North America commands ~41% revenue share contribution followed by India (~36%), Europe (~17%) and Magadi (~6%). In terms of EBITDA/tonne, the India unit generates highest profitability compared to other units.

Exhibit 3: Revenue break-up (₹ crore)



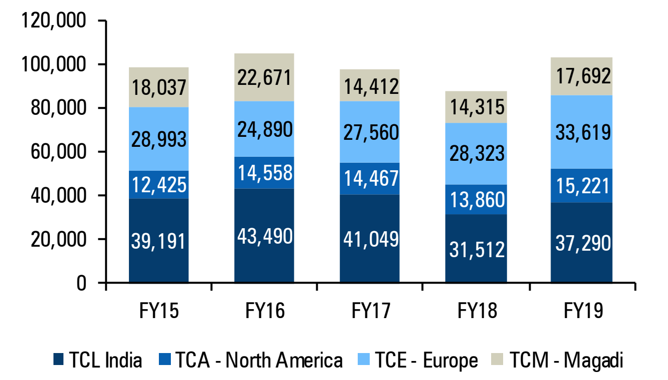
Source: Company, ICICI Direct Research

Exhibit 4: Basic chemical sales volume (in KT)

Basic Chemical Sales volume (in KT)	FY15	FY16	FY17	FY18	FY19
TCL India	**771**	**774**	**802**	**793**	**797**
Soda Ash	683	685	708	693	694
Sodium Bicarbonate	88	89	94	100	103
TCA - North America	**2363**	**2104**	**2241**	**2350**	**2222**
Soda Ash	2363	2104	2241	2350	2222
TCE - Europe	**596**	**681**	**586**	**507**	**431**
Soda Ash	511	580	481	394	324
Sodium Bicarbonate	85	101	105	113	107
TCM - Magadi	**377**	**307**	**272**	**336**	**286**
Soda Ash	377	307	272	336	286

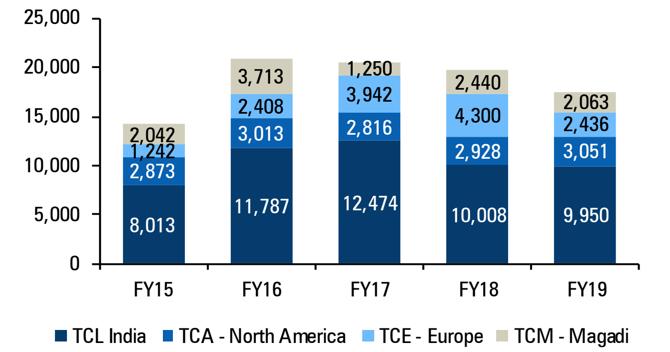
Source: Company, ICICI Direct Research

Exhibit 5: Realisation/tonne across different units



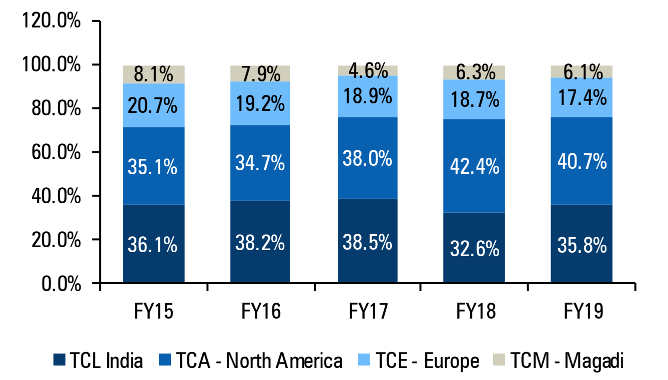
Source: Company, ICICI Direct Research

Exhibit 6: EBITDA/tonne across different units



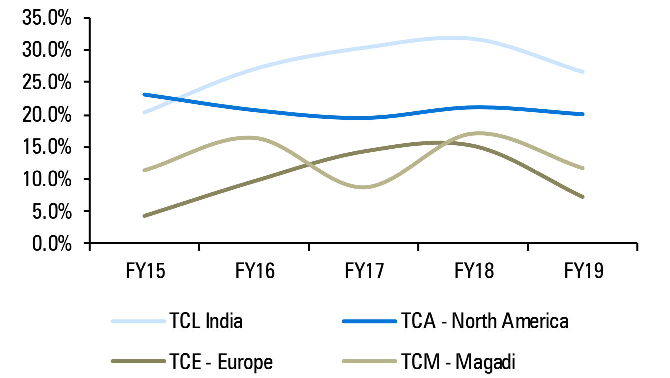
Source: Company, ICICI Direct Research

Exhibit 7: Geographical revenue share in basic chemical segment



Source: Company, ICICI Direct Research

Exhibit 8: EBITDA margin of each unit



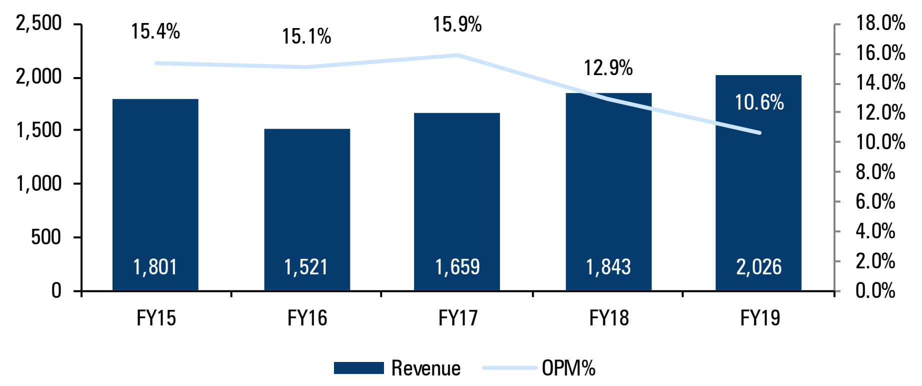
Source: Company, ICICI Direct Research

Specialty chemical segment

Rallis is the key contributor to TCL's specialty chemical segment. The company has also ventured into the neutraceuticals and HDS segment recently. Under neutraceuticals, the company offers an innovative range of nutritional solutions, prebiotics and healthier alternatives to regular sugar for consumers. Tata Nx Zero Sugar is a one-of-its-kind offering made from non-artificial sugar substitute – lactose (natural milk sugar), steviol glycosides (extracted from stevia herb) and a fruit extract. A 100% natural, with no sugar, this product has a low Glycaemic Index compared to regular sugar, making it appropriate for people who have been advised to avoid or reduce their sugar intake. This product is available online as well as at selected outlets in India. Tata NQ solutions find application across multiple categories of food and beverages (F&B) and neutraceuticals. TCL is among the few manufacturers of prebiotic dietary fibres using a nature inspired fermentation route. The customer base spans across North America, Australia, Europe, Middle East and Asia. The company has installed capacity of 5,000 MTPA (expandable up to 20,000 MTPA) for FOS. The manufacturing plant is near Nellore, Andhra Pradesh.

Under the silica business, TCL is targeting the high-growth market of tyres, especially the green tyre made of HDS whose demand is being propelled by stringent emission norms and tyre labelling. TREADSIL™ is the company's HDS brand, targeting energy efficient tyres for vehicles. The products also find application in rubber and non-rubber goods – TYSIL™ is conventional silica brand for tyres and other rubber goods applications. While TAVERSIL™ for non-rubber applications like food, feed, detergents, oral care and agro chemicals. To strengthen its foothold in the segment, TCL had acquired 900 TPM precipitated silica plant at Cuddalore in Tamil Nadu.

Exhibit 9: Revenue (₹ crore) & OPM (%)



Source: Company, ICICI Direct Research

Industry Overview

Soda ash is largely used in segments like flat glass, container glass, detergent, pulp & paper, alumina, metals/mining, etc. Soda ash can be manufactured through three different processes: (i) natural, (ii) Solvay and (iii) HoU. Since trona reserves are more found in the US, Turkey and Africa, these geographies are leading producers of natural soda ash. In the Solvay route, soda ash is produced through key ingredients like industrial salt, limestone, coke and steam coal. In India, more limestone reserves are found in Gujarat. Hence, players like Tata Chemical, GHCL and Nirma play a notable role in the synthetic soda ash market given their strategic position in the domestic market. On the other hand, China produces majority of soda ash through the HoU process.

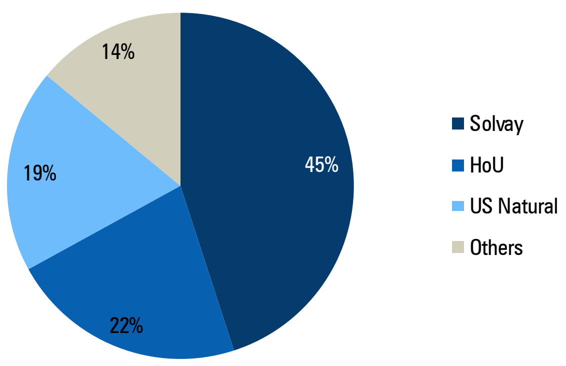
Exhibit 10: Key inputs prerequisite for 1 MT of soda ash

Process	Key inputs for 1 MT of soda ash		Waste Residue
Solvay	Industrial salt	1.5 MT	Will discharge
	Limestone	1.4 MT	10M3 waste water
	Coke	0.115 MT	(produce CaCl2)
	Steam coal (energy)	0.4 MT	and 300-400kg
HoU	Industrial salt	1.15 MT	Will have by
	Ammonia	0.345 MT	product 1.03MT
	Steam coal	0.26 MT	ammonium chloride
Natural	Trona	1.5-1.8 MT	

Source: Industry, ICICI Direct Research

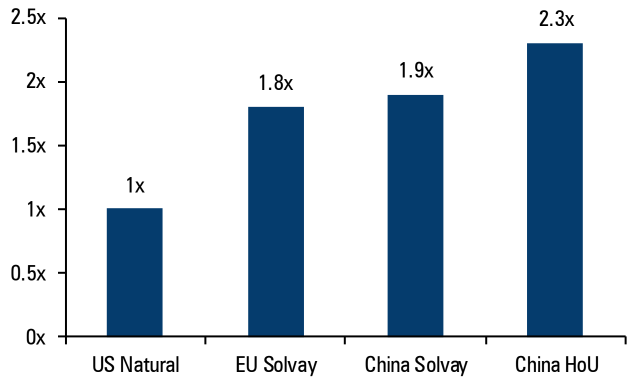
It is estimated that of the overall global soda ash production (64.2 MMT), ~45% is manufactured through Solvay process followed by 22% from HoU, 19% from US natural (trona) and 14% from others. Further, in terms of cost dynamics of soda ash through different process, it is estimated that average cost to produce natural soda ash ($130-140/tonne) is 50% lower than the Solvay route. This is largely as the Solvay process consumes more energy along with higher costs associated with obtaining by-products. In terms of key players in the soda ash market, Solvay remains the top player with 7.3 MMT capacity followed by Ciner (4.6 MMT), Tata Chemical (3.7 MMT) and Genesis Alkali (3.7 MMT) in 2018 (source IHS). However, the current capacity of TCL remains around 4.2 MMT. It is estimated that top 10 players held 52.5% (22.97 MMT) of the global soda ash market in 2000, which came down to 47.1% (33.57 MMT) in 2018 (source IHS).

Exhibit 11: Share of soda ash production....



Source: Genesis Alkali IP, ICICI Direct Research

Exhibit 12: Cost dynamics over US natural (Trona)



Source: Genesis Alkali IP, ICICI Direct Research

Exhibit 13: Top 10 soda ash players share to global soda ash market over the period….

2000			2017			2018		
Company	**Capacity MMT**	**% Share**	**Company**	**Capacity MMT**	**% Share**	**Company**	**Capacity MMT**	**% Share**
Solvay	6.79	15.5%	Solvay	7.32	10.7%	Solvay	7.32	10.3%
FMC	3.50	8.0%	Tata Chemical	3.73	5.5%	Ciner	4.60	6.5%
General Chemical	2.55	5.8%	Tronox (FMC)	3.68	5.4%	Tata Chemical	3.73	5.2%
Sterlitamak	2.30	5.2%	Ciner Group	3.06	4.5%	Genesis Alkali	3.68	5.2%
OCI Enterprises	2.09	4.8%	Shandong Haihua	2.85	4.2%	Shandong Haih	2.85	4.0%
Brunner Mond	1.48	3.4%	NIRMA	2.70	4.0%	NIRMA	2.73	3.8%
IMC Global	1.36	3.1%	Ciech	2.41	3.5%	Ciech	2.43	3.4%
Ciech	1.10	2.5%	Sanyou Chemical	2.30	3.4%	Sanyou Chemi	2.20	3.1%
Lianyungang Soda	0.90	2.1%	Hubei Yuhua	2.10	3.1%	Hubei Yuhua	2.10	2.9%
Shandong Haihua	0.90	2.1%	Sisecam	1.93	2.8%	Sisecam	1.93	2.7%
Total	**22.97**	**52.5%**		**32.08**	**47.1%**		**33.57**	**47.1%**

Source: IHS, ICICI Direct Research

Global soda ash capacity is estimated at 70.6 MMT of which production & consumption remains at 64.2 MMT (utilisation rate of ~91%). In terms of geography, China remains the largest producer with production run rate of 30.8 MMT per annum followed by North America (12.4 MMT) and Europe (11.7 MMT). In terms of applications of soda ash, flat glass constitute 27% share followed by container glass at 21%. The detergent market constitutes 15% of global soda ash consumption. Hence, any adverse demand scenario in these segments play a predominant role in determining realisations of soda ash.

To manufacture container glass of 1 tonne, 0.15-0.17 tonne (~15-17%) of soda ash is estimated to be required. The same proportion is ~5% for flat glass players. However, flat glass manufacturers also require float glass as their raw material, which, we believe, consumes soda ash. Hence, the proportion of soda ash consumption should be in the low to mid-teens across flat and container glass industry.

Exhibit 14: Global soda ash industry snapshot in terms of capacity, production, consumption by segment….

	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
N.A. (U.S.): Domestic Market, EXW	$165	$193	$193	$193	$198	$207	$209	$223	$223	$223	$223	$223
China - Spot Export FOB				$265	$208	$243	$228	$190	$243	$293	$265	$265
Utilization (%)	**86%**	**76%**	**77%**	**77%**	**82%**	**82%**	**82%**	**86%**	**88%**	**89%**	**88%**	**91%**
Capacity (million metric tons)	**55.1**	**59.2**	**62.8**	**64.2**	**65.3**	**65.7**	**66.8**	**65.4**	**66.6**	**67.9**	**70.3**	**70.6**
China	19.2	22.0	24.3	27.1	28.6	28.9	30.6	29.5	29.6	29.9	30.2	30.2
North America	14.8	14.8	14.8	14.8	14.8	14.9	14.9	15.0	15.0	15.0	15.0	15.0
West Europe	9.5	9.6	9.6	9.4	9.5	9.5	8.8	8.8	8.9	8.9	8.9	8.9
East Europe	4.1	4.1	4.8	4.2	3.7	3.7	3.9	3.9	4.0	4.0	4.0	4.0
South & Southeast Asia	4.0	4.5	4.5	4.3	4.1	4.1	3.9	4.0	4.6	4.9	4.9	5.0
Middle East & Africa	2.3	2.9	3.5	3.5	3.5	3.7	3.7	3.7	3.9	4.7	6.8	6.9
Northeast Asia	0.7	0.7	0.7	0.7	0.7	0.7	0.7	0.4	0.4	0.4	0.4	0.4
South America	0.5	0.5	0.5	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3
Production (million metric tons)	**47.6**	**45.0**	**48.3**	**49.5**	**53.3**	**54.1**	**55.0**	**56.5**	**58.3**	**60.3**	**62.2**	**64.2**
China	18.5	19.4	20.4	21.0	24.0	24.5	25.2	26.0	27.3	28.5	29.6	30.8
North America	11.5	9.6	10.8	10.9	11.3	11.8	12.0	12.1	12.4	12.4	12.4	12.4
West Europe	8.4	7.4	7.2	7.5	7.4	7.3	7.3	7.2	7.2	7.2	7.3	7.3
East Europe	3.9	3.3	3.5	3.6	3.9	3.7	3.9	4.2	4.2	4.3	4.3	4.3
South & Southeast Asia	2.8	2.8	3.1	3.2	3.1	3.1	2.8	3.2	3.3	3.3	3.4	3.5
Middle East & Africa	1.8	2.1	2.7	2.8	3.0	3.1	3.2	3.3	3.4	4.0	4.6	5.1
Northeast Asia	0.4	0.4	0.4	0.4	0.3	0.4	0.4	0.4	0.4	0.4	0.4	0.4
South America	0.2	0.2	0.2	0.2	0.1	0.2	0.2	0.2	0.2	0.2	0.3	0.3
Consumption by Region (million metric tons)	**47.2**	**45.0**	**48.0**	**49.5**	**53.2**	**54.3**	**55.4**	**56.5**	**58.3**	**60.3**	**62.2**	**64.2**
China	16.7	17.0	18.8	19.3	22.3	23.0	23.5	23.7	24.8	25.8	26.9	28.1
West Europe	8.1	7.4	7.6	7.8	7.7	7.7	7.8	7.9	8.0	8.2	8.3	8.4
North America	7.3	6.3	6.6	6.7	6.6	6.6	6.7	6.7	6.8	6.9	7.0	7.1
South & Southeast Asia	5.2	5.2	5.5	5.7	6.1	6.1	6.3	6.5	6.8	7.0	7.3	7.6
East Europe	3.7	3.2	3.4	3.5	3.7	3.7	3.8	3.9	4.0	4.1	4.2	4.3
Middle East & Africa	2.5	2.5	2.6	2.7	3.1	3.3	3.4	3.6	3.8	3.9	4.1	4.3
South America	2.0	1.8	2.0	2.1	2.3	2.4	2.5	2.6	2.6	2.7	2.7	2.8
Northeast Asia	1.7	1.5	1.6	1.6	1.5	1.5	1.5	1.5	1.5	1.6	1.6	1.6
Consumption by Product (million metric tons)	**47.2**	**45.0**	**48.0**	**49.5**	**53.2**	**54.3**	**55.4**	**56.5**	**58.3**	**60.3**	**62.2**	**64.2**
Consumption in Glass	25.1	23.5	25.3	26.1	27.7	28.3	28.8	29.4	30.4	31.4	32.4	33.4
Consumption in Soaps & Detergents	6.4	6.4	6.7	6.9	7.1	7.2	7.4	7.5	7.8	8.0	8.2	8.5
Consumption in Inorganic Chemicals	6.4	6.0	6.2	6.5	6.5	6.6	6.8	6.9	7.1	7.4	7.6	7.8
Consumption in Other Uses	5.8	5.8	6.3	6.4	8.3	8.4	8.5	8.6	9.0	9.3	9.6	10.0
Consumption in Organic Chemicals	1.2	1.2	1.2	1.3	1.3	1.3	1.4	1.4	1.5	1.5	1.6	1.6
Consumption in Alumina	0.9	0.8	0.8	0.9	0.9	0.8	0.9	0.9	0.9	1.0	1.0	1.0
Consumption in Paper & Pulp	0.8	0.8	0.8	0.8	0.8	0.8	0.9	0.9	0.9	0.9	0.9	1.0
Consumption in Neutralisation	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.4	0.4	0.4	0.4	0.4
Consumption in Drinking Water	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Consumption in Flu Gas Desulphurisation	0.1	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2

Source: Bloomberg, ICICI Direct Research

The Indian soda ash market is estimated to be around 3.8 MMT while production is at ~3 MMT. Exports & imports remain at 0.1 MMT & 0.8 MMT, respectively. The Indian soda ash market constitute two varieties viz. light grade (used in detergent industry) and dense grade (used in glass industry). The domestic share of light grade soda ash is estimated at 60% while dense is at 40%. According to Hindustan National Glass annual report, domestic container glass industry size is estimated at 2.2 MMT. We expect soda ash demand to be around ~0.35 MMT (~8% of domestic soda ash demand) in the container glass industry. The remaining demand is to the tune of ~1.2 MMT (~32% of domestic soda ash demand) that should be coming from flat glass players like Asahi India Glass. This is given the soda ash consumption is at ~15-17% in the container glass industry.

Given the US, Kenya and Turkey enjoy low cost of production due to natural soda ash, these geographies are top in terms of soda ash exports to India. On the other hand, due to proximity advantage for domestic soda ash players, exports to countries like Sri Lanka, Bangladesh and Nepal remain in a sweet spot.

Exhibit 15: India soda ash market snapshot

Year	Production	Import	Export	Consumption
2011	2.30 MMT	0.49 MMT	0.20 MMT	2.59 MMT
2012	2.41 MMT	0.45 MMT	0.26 MMT	2.60 MMT
2013	2.44 MMT	0.69 MMT	0.08 MMT	3.05 MMT
2014	2.39 MMT	0.57 MMT	0.08 MMT	2.88 MMT
2015	2.46 MMT	0.73 MMT	0.03 MMT	3.16 MMT
2016	2.58 MMT	0.63 MMT	0.02 MMT	3.20 MMT
2017	2.61 MMT	0.70 MMT	0.06 MMT	3.24 MMT
2018	2.99 MMT	0.77 MMT	0.11 MMT	3.65 MMT

Source: Chemical Statistics 2018, ICICI Direct Research

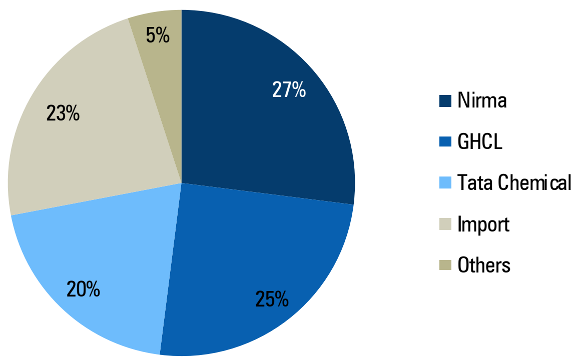
Exhibit 16: Top five import/export destination for India

Top 5 Import destination in 2018			Top 5 Export destination in 2018		
Country	Imports	% of Imports	Country	Exports	% of Exports
Romania	0.18 MMT	23%	Indonesia	0.04 MMT	32%
USA	0.15 MMT	19%	Bangladesh	0.03 MMT	31%
Kenya	0.10 MMT	13%	Nepal	0.01 MMT	8%
Turkey	0.09 MMT	12%	Sri Lanka	0.01 MMT	8%
Bulgaria	0.08 MMT	11%	Philippines	0.01 MMT	8%
Total	**0.60 MMT**	**78%**	**Total**	**0.10 MMT**	**86%**

Source: Chemical Statistics 2018, ICICI Direct Research

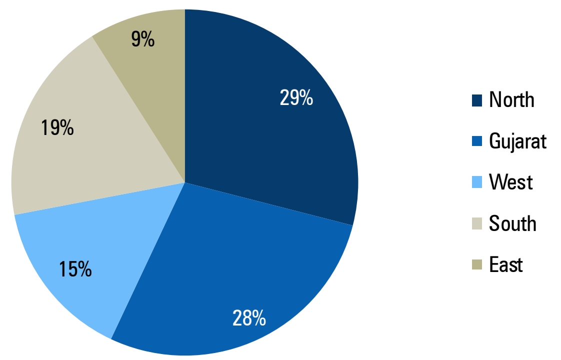
In terms of soda ash production break up between domestic players, Nirma leads with 27% market share followed by GHCL (25%) and Tata Chemical (20%). In terms of geographical break-up, the west market including Gujarat has ~43% market share followed by north (29%). Demand in southern (~19%) and eastern (~9%) markets is estimated to be normally met through imports primarily due to cost dynamics.

Exhibit 17: Percentage market share for India soda ash market



Source: GHCL IP, ICICI Direct Research

Exhibit 18: Percentage of soda ash consumption region wise



Source: GHCL IP, ICICI Direct Research

Investment Rationale

Global demand supply dynamics likely to support steady base operations

The US-China trade war has resulted in a subdued demand environment across the globe particularly in China (PRC). China is perceived to have witnessed a slowdown in auto and real estate sales due to the ongoing trade war. This led to production cuts by auto manufacturers/real estate developers in PRC. Consequently, this translated to a fall in demand for glass and, thereby, soda ash. Further, a poor growth outlook in Europe along with an enduring slowdown in auto and real estate in India also dimmed the prospects of soda ash demand, going ahead.

We expect Tata Chemical's India market (TCL India) to be impacted primarily by the aforementioned factors along with incremental supplies from GHCL, Rohit Surfactant and RoW despite there being some relief from Pakistan supplies to the tune of 50,000 MT due to additional surcharge. Further, switching pattern to liquid detergent from powder detergent is also likely to drive down overall soda ash demand, going ahead. Hence, we expect realisation cut of ~5% & 3% for TCL India basic chemical segment for both FY20E and FY21E, respectively. The fall is expected to be largely negated by an improvement in realisation of soda bicarb owing to incremental Medikarb sales post capacity expansion (~2x realisation of base bicarb). Furthermore, we expect a fall in natural gas prices to assist lower production cost for Tata Chemical North America. In terms of Tata Chemical Europe (TCEM), the management is more focused on improving mix towards soda bicarb against soda ash. Thus, firmness in realisation/tonne can also be assessed.

In terms of EBTIDA/tonne, we expect Tata Chemical to see an improvement across all geographies primarily on account of the low base in different markets due to varied reasons. Additionally, the global soda ash market has been operating at 91% utilisation level, which is the highest in a decade. Further, no new capacity has been coming up except GHCL (~0.1 MMT by FY21E & 0.5 MMT greenfield capacity by FY23/24E) and Tata Chemical (~0.2 MMT). Since new greenfield capacity would take at least four years to be commissioned and given that there has been no announcement by major players, we expect further de-bottlenecking across the global soda ash market. We believe this should not lead to significant risk to the demand/supply trade off. We expect total installed capacity to reach around 74 MMT by FY23-24E. Assuming consumption remains at the same level of FY19 in a conservative scenario, the global soda ash market should utilise ~87% of its capacity. Historically, the average utilisation level at 83-84% showed average US FOB price of $205/MT and China FOB of $240/MT while the prevailing FOB price of the US and China remains at $223/MT & $265/MT, respectively. Hence, 4-5% cuts in utilisation may not meaningfully impact the realisation/tonne as witnessed in the past. Further, lower input cost along with a change in mix towards value added products along with control on other costs can either maintain or improve its EBITDA/tonne.

Exhibit 19: Average price at different utilisation level for global soda ash market

	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
N.A. (U.S.): Domestic Market, EXW	$165	$193	$193	$193	$198	$207	$209	$223	$223	$223	$223	$223
China - Spot Export FOB				$265	$208	$243	$228	$190	$243	$293	$265	$265
Utilization (%)	**86%**	**76%**	**77%**	**77%**	**82%**	**82%**	**82%**	**86%**	**88%**	**89%**	**88%**	**91%**
Capacity (million metric tons)	**55.1**	**59.2**	**62.8**	**64.2**	**65.3**	**65.7**	**66.8**	**65.4**	**66.6**	**67.9**	**70.3**	**70.6**
Production (million metric tons)	**47.6**	**45.0**	**48.3**	**49.5**	**53.3**	**54.1**	**55.0**	**56.5**	**58.3**	**60.3**	**62.2**	**64.2**

Source: Bloomberg, ICICI Direct Research

India EBITDA/tonne last year was impacted by higher freight/power cost. We believe this may not be the case this fiscal owing to a fall in crude prices. We also expect crude prices to remain subdued due to the suppressed demand outlook across globe primarily on account of a trade war. In case we see any trade truce between the US and China, there could be a sentimental progress in the demand stance for both soda ash and crude oil, which could largely offset any negative impact on EBITDA/tonne in the medium term. Further, a better mix towards Medikarb can also assist expansion in EBITDA/tonne for TCL India. For TCNA, we expect a fall in input cost to largely offset the pricing pressure and, therefore, stability in the EBITDA/tonne can be expected. In TECM terms, we expect a higher sales mix of soda bicarb to drive EBITDA/tonne. However, an increase in prices of coke can limit an improvement in operational performance. For Magadi, we expect operating leverage to aid EBITDA/tonne, going ahead.

Exhibit 20: Segment wise revenue (₹ crore) & EBITDA/tonne

	Revenue			EBITDA/ton		
	FY19	**FY20E**	**FY21E**	**FY19**	**FY20E**	**FY21E**
TCL India	2,972	2,814	2,994	9,950	10,149	10,251
TCA - North America	3,382	3,462	3,596	3,051	3,356	3,424
TCE - Europe	1,449	1,426	1,497	2,436	3,411	3,479
TCM - Magadi	506	540	564	2,063	2,991	3,051
Consol Basic Chemical	**8,309**	**8,242**	**8,650**	**4,376**	**4,779**	**4,927**

Source: Company, ICICI Direct Research

Emerging specialty business to drive performance ahead

Consistent efforts of the management to improve specialty business contribution to group revenue led the company to foray into neutraceuticals, High dispersible silica (HDS) segments recently. Further, the management also announced its entry into recovery of cathode active materials from spent lithium-ion cells/batteries. We expect this emerging specialty business to drive the financial performance of the group in the medium to long run. A neutraceuticals plant has been set up at Nellore with a capacity of 5000 MTPA prebiotics (FOS & GOS), expandable up to 20,000 MTPA.

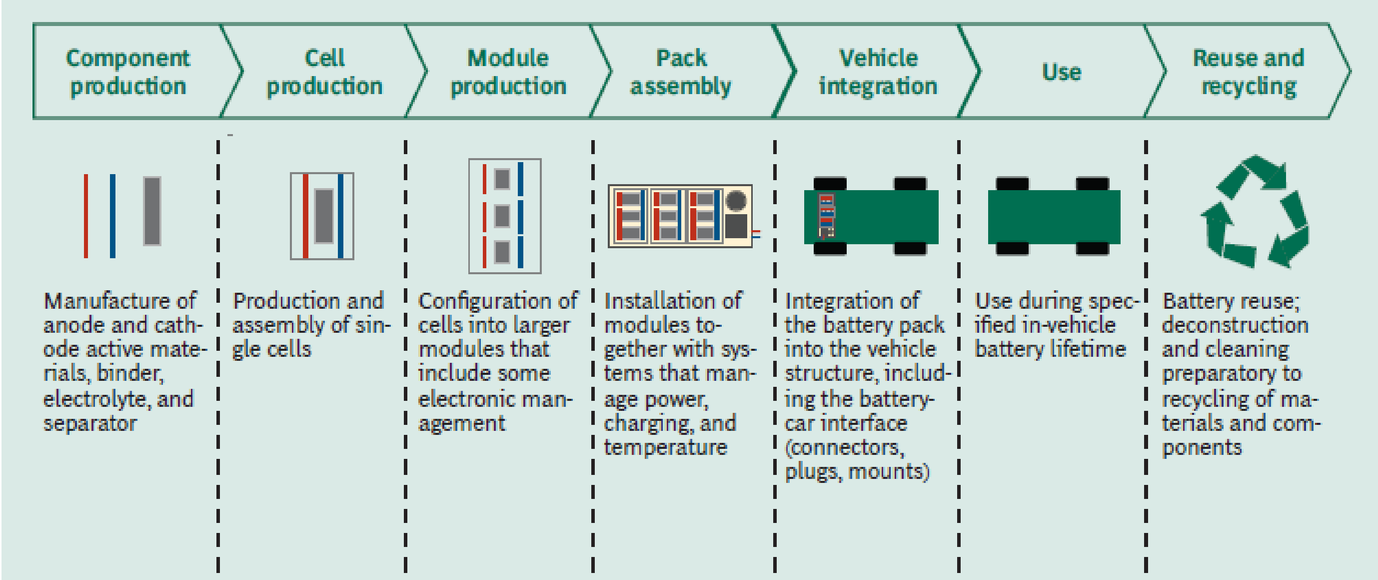
TCL spent around ₹ 270 crore on Nellore facility. Under Fructo-Oligosaccharide (FOS) & Galacto-Oligosaccharide (GOS), the company will market prebiotics dietary fibre for bakery, dairy, sweets, health drink supplements, infant foods, sports nutrition products. According to reports, the neutraceuticals market in India was valued at ₹ 26,000 crore in 2017 and is expected to reach ₹ 80,800 crore by 2023, growing at a CAGR of around 17%. This provides an immense opportunity for TCL neutraceuticals segment over the long run. The company already manufactures nutritional products at Sriperumbudur plant and recorded revenues of ₹ 41 crore (~+22% YoY) in FY19. For Nellore, the management anticipates to commercialize production from H2FY20 and thus we expect it to make a material impact from FY22/23E onwards. Assuming 1x asset turn can provide ₹ 270 crore revenues from this segment. The management already highlighted ~18-20% RoCE for this vertical, translating into OPM of around 22-25%. Increasing contribution from this segment would result to better return ratios for the overall group in the medium to long run.

Apart from this, TCL made an investment to the tune of ₹ 295 crore for HDS plant in Cuddalore. The company currently manufactures food grade and rubber grade HDS, while trial run for tyre grade silica have been commenced. Management expects commercial production for tyre grade silica to commence soon. The global silica market is pegged at US$4.5 billion while the domestic market size is estimated at ₹ 1,000 crore. HDS will be used to make green tyre, which will be propelled by stringent emission norms and tyre labelling. Apart from this, HDS is also used in personal care. Aksharchem had also set up 10,000 MTPA capacity for HDS at a capex of ₹ 70 crore. Aksharchem's management estimates 1x asset turn with OPM of around 15%. Assuming the same run rate, the HDS business for TCL should contribute incremental revenues and EBITDA to the tune of ₹ 295 crore and ~₹ 44 crore, respectively, going ahead.

In addition to this, according to a press release on August 26, 2019 by TCL, the company successfully commenced the commercial recovery of cathode active materials from spent lithium-ion cells/batteries on a pilot basis. The company continued its efforts to scale it up to recycle 500 tonnes of lithium ion batteries. As per BASF factbook, lithium ion battery market is expected to grow at 20-25% CAGR over the next five to seven years. By 2025, annual EV sales globally are estimated at 10-15 million. This would translate into a 700-1000 kt market for cathode active materials, which could be valued at €25-30 billion. According to this, the per vehicle cathode active material requirement is estimated at 67 kg. The per kg cost of cathode active material is estimated at around ₹ 2400. In India, the government has recently announced setting up of a 6 GW factory of 10 Gwh each with total investment of US$4 billion by 2025. The government is also planning to incentivise it with tax soaps for setting up gigafactories in India. We believe this clearly shows the motive of the present government towards electrifying the vehicle base in India. Thus, assuming these plants would operate even at 50% utilisation by 2025, the potential opportunity size for active cathode material would be ₹ 4200 crore ***(battery cost assumed at $200/Kwh with active cathode material share of 10% in battery cost).***

We also estimate requirement of active cathode material based on EV demand in India. The two-wheeler (2-W) sales are estimated around 2.2 crore units every year while three wheeler (3-W) sales remains at 7 lakh. This is given the EV ramp up should initially commence from 2-W, 3W and EV battery weight should constitute ~25-30% of the overall vehicle weight. Thus, assuming 15% EV penetration of present annual sales *(EV battery demand of 9.9 Gwh & 0.74 Gwh from 2-W & 3-W, respectively)* with 10% share of active materials in EV battery, opportunity size could be ~₹ ~1500 crore at the initial stage. ***(the government will also undertake to transform public transport onto EV platform, providing an additional opportunity).***

Exhibit 21: Value chain for electric-car batteries comprises seven steps…



Source: BCG Analytics, ICICI Direct Research

Exhibit 22: Cathode material requirements globally…

Cathod active material cost in EV vehicle	
EV Vehicles Demand yearly globally by FY25E	10-15 million
Cathode Active Materials Demand yearly	700-1000 kt
Cathode active material requirement per vehicle	67 kg
Per kg cost of cathode active material	₹ 2400
Per vehicle cathod material cost	₹ 160,800

Source: BASF Factbook, ICICI Direct Research

Exhibit 23: Sensitivity analysis of cathode material size (₹ crore)

EV penetration in 3W (%) \ EV penetration in 2W (%)	5%	10%	15%	20%	25%	30%	35%
5%	496	958	1,420	1,882	2,344	2,806	3,268
10%	531	993	1,455	1,917	2,379	2,841	3,303
15%	565	1,027	1,489	1,951	2,413	2,875	3,337
20%	599	1,061	1,523	1,985	2,447	2,909	3,371
25%	634	1,096	1,558	2,020	2,482	2,944	3,406
30%	668	1,130	1,592	2,054	2,516	2,978	3,440
35%	702	1,164	1,626	2,088	2,550	3,012	3,474

Source: ICICI Direct Research

Residual business available at attractive valuation

The management decided to demerge the consumer business of Tata Chemical and merge it with Tata Global Beverages in May 2019. The consumer business was valued at ₹ 5,750 crore (EV/EBITDA 18.3x & EV/Revenue 3.1x FY19). This is given the exchange ratio remains at 1.14 shares and prevailing CMP of Tata Global is at ₹ 259/share. Tata Chemical shareholders' value in consumer business is at ₹ 295/share. Since Tata Chemical is trading at ₹ 597/share, **the residual business is available at ₹ 301/share (EV/EBITDA 3.5x FY21E).**

Since the company is undergoing capex in TCL India's basic chemical segment, we expect incremental revenue to commence from FY21E. Further, higher sales from Medikarb post capacity expansion can limit downside pressure on realisation/tonne and assist in stability and improvement in EBITDA/tonne. Further, operating leverage at Magadi will drive operational performance for Africa operations. All these could translate into basic chemical EBITDA CAGR of 8% in FY19-21E. We value TCL India's basic chemical at EV/EBITDA of 5x FY21E while RoW basic chemical at EV/EBITDA of 4x FY21E. This translates to a fair value of basic chemical business at ₹ 272/share.

Apart from this, we expect Rallis to clock EBITDA of ₹ 379 crore in FY21E, valuing at 8x EV/EBITDA translates into SOTP value of ₹ 41/share (assuming 50.06% stake with 20% holdco discount). Further, we expect HDS to clock OPM of 15%, while with FOS & GOS at 25%, combined EBITDA could reach ₹ 56 crore in FY21E. We value this segment at 11x EV/EBITDA, resulting into fair value of ₹ 24/share. Along with this, we expect non-current investment portfolio at 40% discount to contribute ₹ 58/share to the residual value of Tata Chemical. **All these translate into SOTP value of ₹ 395/share, while Tata Chemical residual business is currently available at ₹ 301/share,**

(Note: We have not considered salt business valuation in our estimates. As per the arrangement, Tata Chemical will continue to manufacture salt and supply to Tata Global Beverages. The company will record manufacturing margins. Given the salt business contributes ~₹ 1200 crore revenues. Hence, valuing at EV/revenue of 1x can provide upside of ₹ 47/share to our estimates).

Key risks and concerns

Prolonged slowdown in China to hurt soda ash demand

The ongoing trade war between the US and China has brought global growth virtually to a standstill. Given China is a dominant player in the global soda ash industry, a prolonged slowdown in construction activity along with lower automobile sales is likely to impact glass demand there, in turn, dampening the growth outlook of the global soda ash market. This can put pressure on realisations of soda ash manufacturers.

Substituting detergent demand to liquid from powder affects domestic soda ash market

The India detergent market size is expected to be ₹ 18,000 crore of which 98% is from powder detergent and the rest from liquid detergent. Given the preferences of Indian youth changes towards liquid detergent, we can expect lower consumption of soda ash from powder detergent manufactures in the medium to long run. However, any signs of a ramp up in demand for automobile and real estate in India can provide sentimental relief to the soda ash market.

Higher input cost, lower soda ash demand impacts EBITDA/tonne

In a weak demand scenario, TCL's operational performance is negatively correlated with crude oil largely due to freight and power costs constituting ~30% of sales. Given the imminent signs of global growth slowdown being visible, any upside in crude prices due to production cut by Opec can impact EBITDA/tonne of Tata Chemical.

Valuation and outlook

The management plans to increase revenue share of specialty chemical from 20% currently to 50% over the next five years with revenue target of ₹ ~13,000 crore from ₹ ~2050 crore in FY19, translating into a CAGR of ~44%. We believe growth could largely be driven by inorganic expansion along with organic growth in Rallis. Apart from this, emerging business such as HDS, neutraceutical and EV would also contribute to the overall performance, going ahead. We also expect that given the specialty chemical business enjoys better operating margins along with return ratios, the group financial profile will improve materially over the medium to long term. In terms of free cash flows, we believe the company generates decent operating cash flows (~15-20% of revenue), which helps them to meet any incremental capex. TCL has already announced a capex of ₹ 2400 crore for basic chemical business, which we expect the company to meet from internal accruals. Further, the company has liquid cash & investment to the tune of ₹ 4200 crore, which will help them to retire schedule debt repayment in FY21E.

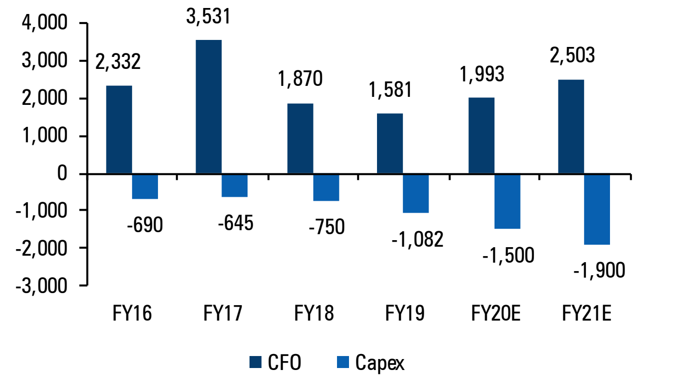
All these, in turn, would help the company to fetch better valuations. We value the company on an SOTP basis and arrive at a target price of ₹ 690/share, with potential upside of ~16% from CMP. **We assign a BUY rating to the stock.**

Exhibit 24: SOTP analysis

In ₹ Crore unless other mentioned	Revenue		EBITDA		EV/EBITDA		EV	
	FY20E	FY21E	FY20E	FY21E	FY20E	FY21E	FY20E	FY21E
Basic Chemical								
India	2,814	2,994	806	893	5.5x	5.0x	4,434	4,466
ROW	5,428	5,656	979	1,028	4.5x	4.0x	4,404	4,111
Speciality Products								
Rallis	2,188	2,442	282	329	9.0x	8.0x	2,535	2,629
Other Speciality	70	283	15	56	13.0x	11.0x	189	615
Consolidated EV							**10,042**	**10,244**
Less: Net debt							1,385	1,643
Residual business MCAP							8,658	8,601
Add: NC investment portfolio @ 40% disc							1,470	1,470
Residual business fair value							**10,128**	**10,072**
No.of shares							25.5	25.5
Residual business Fair value/Share							**398**	**395**
Add: Consumer Products Fair value/share							295	295
Target price/share							**692**	**690**
CMP							597	597
Upside/downside							**16%**	**16%**

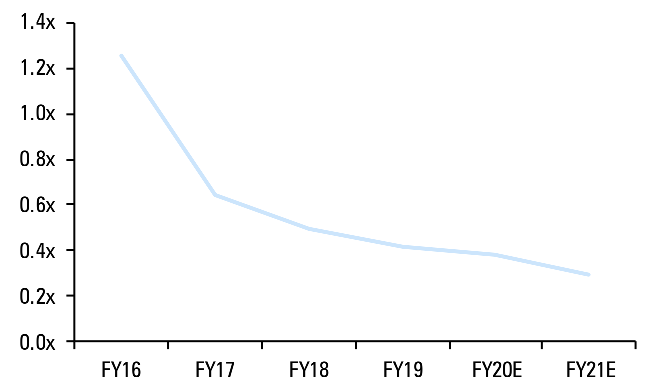
Source: ICICI Direct Research

Exhibit 25: CFO & capex (₹ crore)



Source: Company, ICICI Direct Research

Exhibit 26: D/E ratio expected to come down further..



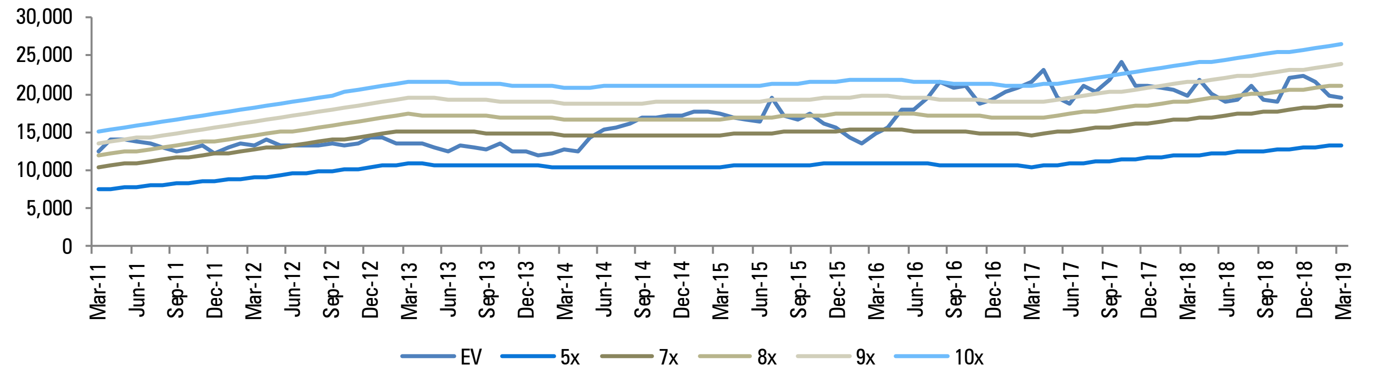
Source: Company, ICICI Direct Research

Exhibit 27: Valuation matrix

Company	Revenue			EBITDA			Adj PAT			ROE			EV/EBITDA		
	FY19	FY20E	FY21E	FY19	FY20E	FY21E	FY19	FY20E	FY21E	FY19	FY20E	FY21E	FY19	FY20E	FY21E
Tata Chemical	11,296	11,731	12,474	2,095	2,387	2,645	1,156	1,220	1,395	9.4%	9.5%	10.3%	7.7x	6.9x	6.4x
GHCL	3,341	3,543	3,774	759	848	914	350	407	450	19.8%	18.7%	17.6%	4.6x	3.6x	3.3x
Solvay	83,632	86,355	89,040	17,960	18,757	19,761	6,867	7,193	7,895	8.6%	8.6%	9.3%	7.2x	7.0x	6.6x
Sisecam	24,321	28,813	32,103	4,979	5,880	6,755	2,547	2,830	2,892	12.8%	12.8%	12.4%	4.8x	4.0x	3.4x

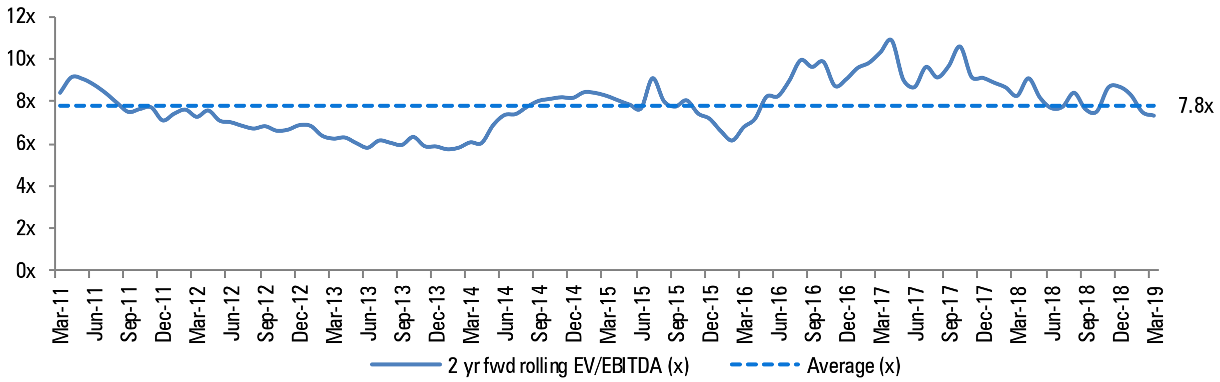
Source: Company, Bloomberg, ICICI Direct Research

Exhibit 28: Two year forward rolling EV/EBITDA band



Source: Company, Bloomberg, ICICI Direct Research

Exhibit 29: Two year forward EV/EBITDA vs. average EV/EBITDA (x) traded in past



Source: Company, Bloomberg, ICICI Direct Research

Financial Summary

Exhibit 30: Profit & Loss statement (₹ crore)

Year end March	FY18	FY19	FY20E	FY21E
Net Revenues	**10,269.7**	**11,296.3**	**11,731.1**	**12,474.5**
Cost Of Revenues (incl Stock Adj)	1,755.5	2,137.7	2,170.3	2,282.8
Gross Profit	**8,514.2**	**9,158.7**	**9,560.9**	**10,191.7**
Employee Cost	1,270.2	1,351.8	1,442.9	1,521.9
Other Operating Expenses	2,202.0	2,488.1	2,375.7	2,470.0
EBITDA	**2,190.7**	**2,095.1**	**2,387.1**	**2,644.5**
Other Income	159.5	411.6	377.9	381.6
EBITDA, including OI	**2,350.2**	**2,506.7**	**2,765.0**	**3,026.1**
Depreciation	518.0	571.4	622.8	685.2
Net Interest Exp.	325.6	363.1	335.9	267.9
Other exceptional items	64.3	70.3	0.0	0.0
EBT	**1,570.9**	**1,642.5**	**1,806.3**	**2,073.0**
Taxes	60.1	346.9	451.6	518.3
Tax Rate	3.8%	21.1%	25.0%	25.0%
Net Income	**1,510.8**	**1,295.6**	**1,354.7**	**1,554.8**
Adj. NI after Minority interest	1,290.6	1,163.9	1,220.0	1,395.0
Adj. EPS (INR)	50.6	45.7	47.9	54.7
Shares Outstanding	25.5	25.5	25.5	25.5

Source: Company, ICICI Direct Research

Exhibit 31: Cash flow statement (₹ crore)

Year end March	FY18	FY19	FY20E	FY21E
PBT & Extraordinary	3,271.8	1,730.4	1,806.3	2,073.0
Depreciation	596.0	571.4	622.8	685.2
After other adjustments				
(Inc) / Dec in Working Capital	-569.1	-214.4	-320.9	-5.0
Taxes	-514.7	-484.9	-451.6	-518.3
Others	-913.9	-21.3	335.9	267.9
Cash from Ops.	**1,870.1**	**1,581.3**	**1,992.5**	**2,502.8**
Purchase of Fixed Assets	-750.3	-1,082.3	-1,500.0	-1,900.0
Others	3,457.3	-875.9	109.1	572.4
Cash from Investing	**2,707.0**	**-1,958.2**	**-1,390.9**	**-1,327.6**
Proceeds from issue of shares	0.0	0.0	0.0	0.0
Borrowings (Net)	-1,240.6	-576.2	-200.0	-1,000.0
Others	-848.9	-1,135.7	-1,055.4	-981.4
Cash from Financing	**-2,089.5**	**-1,711.8**	**-1,255.4**	**-1,981.4**
Net Change in Cash	2,487.7	-2,088.7	-653.8	-806.2
Effects of foreign currency translation	6.8	31.2	0.0	0.0
BF Cash & Bank	1,664.8	4,483.0	1,952.2	1,298.4
END Cash & Bank	4,483.0	1,952.2	1,298.4	492.2

Source: Company, ICICI Direct Research

Exhibit 32: Balance Sheet Statement (₹ crore)

Year end March	FY18	FY19	FY20E	FY21E
Liabilities				
Share Capital	254.8	254.8	254.8	254.8
Reserves	10,846.9	12,086.5	12,586.9	13,268.3
Total Shareholders Funds	**11,101.7**	**12,341.3**	**12,841.8**	**13,523.2**
Minority Interest	2,717.2	2,914.7	3,158.5	3,438.4
Long Term Borrowings	5,394.0	4,782.9	4,382.9	3,182.9
Net Deferred Tax liability	1,191.6	1,297.1	1,297.1	1,297.1
Other long term liabilities	95.8	116.4	104.0	110.6
Long term provisions	1,675.1	1,503.9	2,020.6	2,148.6
Current Liabilities and Provisions				
Short term borrowings	140.2	352.5	552.5	752.5
Trade Payables	1,478.6	1,475.3	1,542.7	1,640.5
Other Current Liabilities	1,878.8	1,840.5	803.5	854.4
Short Term Provisions	205.8	280.3	289.3	307.6
Total Current Liabilities	3,703.3	3,948.6	3,187.9	3,554.9
Total Liabilities	**25,878.6**	**26,904.9**	**26,992.8**	**27,255.7**
Assets				
Net Block	11,026.9	11,664.8	12,277.8	13,092.5
Capital Work in Progress	373.9	735.8	1,000.0	1,400.0
Intangible assets under devl.	35.0	38.0	38.0	38.0
Goodwill on Consolidation	1,731.9	1,859.0	1,859.0	1,859.0
Non-current investments	2,748.6	3,362.9	3,362.9	3,362.9
Deferred tax assets	20.8	36.2	36.2	36.2
Long term loans and advances	9.7	7.9	9.1	9.7
Other Non Current Assets	892.4	1,102.0	775.9	823.3
Current Assets, Loans & Advances				
Current Investments	91.8	2,252.3	2,252.3	1,800.0
Inventories	1,462.3	1,725.6	1,799.8	1,913.9
Sundry Debtors	1,307.9	1,452.5	1,542.7	1,640.5
Cash and Bank	4,483.0	1,952.2	1,298.4	492.2
Loans and Advances	1.6	1.3	1.3	1.3
Other Current assets	1,692.9	714.4	739.2	786.1
Current Assets	9,039.6	8,098.3	7,633.9	6,634.0
Total Assets	**25,878.6**	**26,904.9**	**26,992.8**	**27,255.7**

Source: Company, ICICI Direct Research

Exhibit 33: Key Ratios

Year end March	FY18	FY19	FY20E	FY21E
Per share data (₹)				
Adj. EPS	50.6	45.7	47.9	54.7
Adj. Cash EPS	71.0	68.1	72.3	81.6
BV	435.7	484.3	504.0	530.7
DPS	22.0	23.5	23.5	23.3
Operating Ratios (%)				
Gross Margin (%)	82.9	81.1	81.5	81.7
EBITDA Margin (%)	21.3	18.5	20.3	21.2
PAT Margin (%)	12.6	10.3	10.4	11.2
Debtor Days	46	47	48	48
Inventory Days	52	56	56	56
Creditor Days	53	48	48	48
Cash Conversion Cycle	46	55	56	56
Return Ratios (%)				
Return on Assets (%)	5.0	4.3	4.5	5.1
RoCE (%)	8.3	8.4	9.0	9.9
RoE (%)	11.6	9.4	9.5	10.3
Solvency				
Total Debt / Equity	0.5	0.4	0.4	0.3
Interest Coverage	5.6	5.3	6.4	8.7
Current Ratio	2.4	2.1	2.4	1.9
Quick Ratio	2.0	1.6	1.8	1.3
Valuation Ratios (x)				
EV/EBITDA	7.4	7.7	6.9	6.4
P/E	11.8	13.1	12.5	10.9
P/B	1.4	1.2	1.2	1.1
EV/Sales	1.6	1.4	1.4	1.4

Source: Company, ICICI Direct Research

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Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%

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