

# Deepak Nitrite

Estimate changes

TP change

Rating change



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Bloomberg	DN IN
Equity Shares (m)	136
M.Cap.(INRb)/(USD\$)	278.1 / 3.7
52-Week Range (INR)	2085 / 567
1, 6, 12 Rel. Per (%)	13/96/191
12M Avg Val (INR M)	1641

## Financials & Valuations (INR bn)

Y/E March	FY21	FY22E	FY23E
Sales	43.6	54.4	62.3
EBITDA	12.5	14.6	16.3
PAT	7.8	9.5	10.7
EPS (INR)	56.9	69.4	78.2
EPS Gr. (%)	27.0	21.9	12.7
BV/Sh.(INR)	172	231	297

## Ratios

Net D:E	0.2	0.1	(0.0)
RoE (%)	39.6	34.4	29.6
RoCE (%)	29.4	29.4	26.9
Payout (%)	9.7	15.0	15.0

## Valuations

P/E (x)	35.8	29.4	26.1
P/BV (x)	11.9	8.8	6.9
EV/EBITDA (x)	22.7	19.2	17.0
Div. Yield (%)	0.3	0.5	0.6
FCF Yield (%)	2.8	1.5	2.1

## Shareholding pattern (%)

As On	Jun-21	Mar-21	Jun-20
Promoter	45.7	45.7	45.7
DII	10.4	11.6	13.5
FII	11.4	11.9	11.5
Others	32.5	30.8	29.3

FII Includes depository receipts

CMP: INR2,039

TP: INR2,350 (+15%)

Buy

## Focus on advance/high-value products intensifies

- Deepak Nitrite (DN) reported a beat on our estimates, driven by better-than-expected margins in Phenolics and margins expansion in Basic Chemicals. The EBIT margin for the Fine & Specialty and Performance Products segments contracted.
- Despite the huge beat on our estimate, we continue to highlight the risk of overall margin contraction from the normalization of phenolics product prices. As a result, we build in an EBITDA margin of 27% in FY22E (up from 26% earlier) and 26% for FY23/24E. That said, strong domestic demand for phenolics, with higher exports to countries such as the US and China, could keep product prices and margins strong in this segment – presenting an upside risk to our estimates.
- At the 50<sup>th</sup> AGM, the management guided that the company aims to transition from being a chemical intermediates company to an advance products one (leaning towards life sciences – the need of the hour). On this path:
  - DN would continue to focus on bringing more products under the Fine & Specialty segment and close the gaps in the production value chain. Around 125 acres of land at Dahej (called Dahej-II) would be developed to focus primarily on advance specialty/intermediates in the Life Sciences segment, especially in fluorination.
  - In addition to the capex plans of INR4b per year in Deepak Nitrite, the board has approved further investments in Deepak Phenolics (DPL): (a) INR3.5b in specialty intermediates and (b) INR7b in downstream products (for the higher production of solvents). It aims to be the largest player in Solvents and capitalize on import substitution.
- We reiterate that the increased focus on advance/high-value products would aid margin expansion and sustainability for the company – of which investors are most wary. This would further result in re-rating of multiples for the stock – as the mix of specialty/complex chemistry products increases.
- Even on a conservative margin assumption, we forecast an EBITDA/PAT CAGR of 14–16% over FY22–24E. The stock trades at relatively cheaper valuations (v/s peers in our Coverage Universe) of 26x FY23E EPS and 17x FY23E EV/EBITDA. Valuing the company at 28x Sep'23E EPS, we arrive at TP of INR2,350. Maintain Buy.

## Beat on our estimates ...

- Revenue came in at INR15.3b (+20% est.; +126% YoY / +4% QoQ), driven by a continually robust performance from the Phenolics segment.
- Revenue for Phenolics grew 7% QoQ to INR10b (+202% YoY) on the back of sturdy product prices in 1QFY22.
- Revenue for Basic Chemicals was up 2% QoQ (+70% YoY) to INR2.5b.
- Revenue for Fine & Specialty was flat QoQ at INR2.1b (+48% YoY).

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Investors are advised to refer through important disclosures made at the last page of the Research Report.

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- Revenue for Performance Products at INR0.9b, missed our estimate (-14% est.; +55% YoY / +8% QoQ).
- EBITDA posted a beat of 27% at INR4.5b in 1QFY22 (+149% YoY / -1% QoQ). **The gross margin saw a 200bp QoQ drop to 46%. The EBITDA margin contracted 150bp QoQ to 29.6%.** PAT stood at INR3b (+30% est.; +206% YoY / +4% QoQ).

#### ...driven by margin expansion in Phenolics and Basic Chemicals

- EBIT in Phenolics rose 8% QoQ to INR2.9b, with the margin at 29% (+100bp QoQ). The margin continued to witness an uptick for eight quarters on the trot.
- EBIT in Basic Chemicals grew 20% QoQ to INR0.85b, led by a spike in margins to 34% (+500bp QoQ – the highest ever after 4QFY18).
- The EBIT margin in Performance Products stood at just 2%, continuing its sequential drop (declining for the last six quarters now).
- EBIT in Fine & Specialty stood at INR0.7b, with 600bp QoQ margin contraction to 33% (v/s 44% in FY21). In percentage terms, contribution from this segment to the total revenue shrank further to 13% (from 18% in FY21), with EBIT contribution of 15% (v/s 30% in FY21).

#### Valuation and view

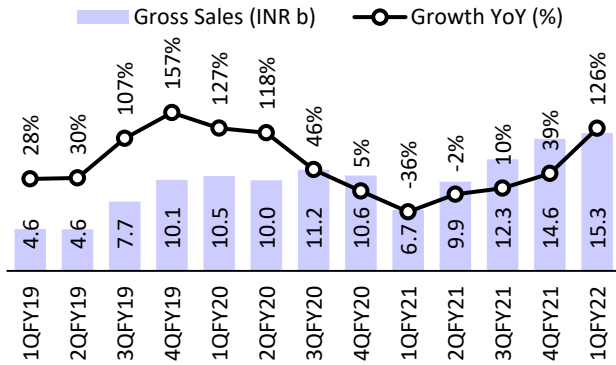
- The management guided that it would continue to look at first-time products in the country, which would facilitate import substitution, with further integration in current processes. The company has been investing in building up the market intelligence team, which studies opportunities in newer and existing markets.
- The IPA expansion and captive power plant are expected to get commissioned by end-1HFY22. The captive power plant would make DPL more competitive in this segment.
- Further recovery in demand for OBA and DASDA (i.e., performance chemicals) is expected over FY22, while demand for agrochemical and personal care products continues to be robust.
- **Despite a capex plan of INR18b over the next three years, it is expected to turn net cash positive by FY23E, with FCF generation of INR17.4b over FY22–24E.** We maintain a Buy rating, with one of the best ROE profiles under our coverage.

#### Consolidated - Quarterly Snapshot

Y/E March	(INR m)											
	FY21				FY22				FY21	FY22E	FY22	Var (%)
	1Q	2Q	3Q	4Q	1Q	2QE	3QE	4QE			1QE	
<b>Gross Sales</b>	<b>6,745</b>	<b>9,873</b>	<b>12,347</b>	<b>14,632</b>	<b>15,262</b>	<b>13,180</b>	<b>13,179</b>	<b>12,821</b>	<b>43,598</b>	<b>54,443</b>	<b>12,770</b>	<b>20%</b>
YoY Change (%)	-35.8	-1.6	10.3	38.6	126.3	33.5	6.7	-12.4	3.1	24.9	89.3	
Gross Margins (%)	51%	51%	45%	48%	46%	45%	45%	45%	48%	45%	46%	
<b>EBITDA</b>	<b>1,816</b>	<b>2,757</b>	<b>3,350</b>	<b>4,547</b>	<b>4,515</b>	<b>3,513</b>	<b>3,475</b>	<b>3,074</b>	<b>12,470</b>	<b>14,576</b>	<b>3,548</b>	<b>27%</b>
Margins (%)	26.9	27.9	27.1	31.1	29.6	26.7	26.4	24.0	28.6	26.8	27.8	
Depreciation	310	312	339	565	436	448	448	460	1,526	1,792	379	15%
Interest	247	196	157	142	109	88	70	92	742	358	114	-4%
Other Income	68	40	49	59	83	41	51	43	215	218	59	39%
<b>PBT before EO expense</b>	<b>1,326</b>	<b>2,288</b>	<b>2,903</b>	<b>3,899</b>	<b>4,053</b>	<b>3,019</b>	<b>3,008</b>	<b>2,564</b>	<b>10,417</b>	<b>12,643</b>	<b>3,115</b>	<b>30%</b>
<b>PBT</b>	<b>1,326</b>	<b>2,288</b>	<b>2,903</b>	<b>3,899</b>	<b>4,053</b>	<b>3,019</b>	<b>3,008</b>	<b>2,564</b>	<b>10,417</b>	<b>12,643</b>	<b>3,115</b>	<b>30%</b>
Tax	337	587	737	998	1,026	760	757	639	2,659	3,182	784	
Rate (%)	25.4	25.6	25.4	25.6	25.3	25.2	25.2	24.9	25.5	25.2	25.2	
<b>Reported PAT</b>	<b>990</b>	<b>1,702</b>	<b>2,166</b>	<b>2,901</b>	<b>3,026</b>	<b>2,259</b>	<b>2,251</b>	<b>1,925</b>	<b>7,758</b>	<b>9,461</b>	<b>2,331</b>	<b>30%</b>
YoY Change (%)	-24.8	13.2	38.2	68.4	205.8	32.7	3.9	-33.6	27.0	21.9	135.6	
Margins (%)	14.7	17.2	17.5	19.8	19.8	17.1	17.1	15.0	17.8	17.4	18.3	

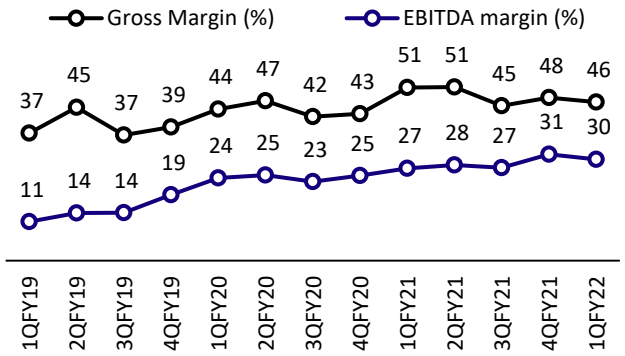
## 1QFY22 – quarter in charts

**Exhibit 1: Sales up 4% QoQ, led by Phenolics business**



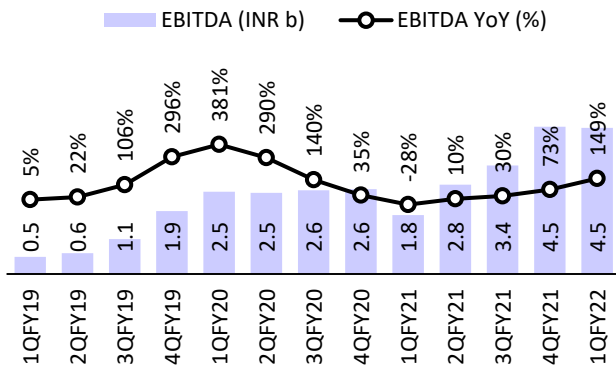
Source: Company, MOFSL

**Exhibit 2: Margin contraction mainly due to Fine & Specialty**



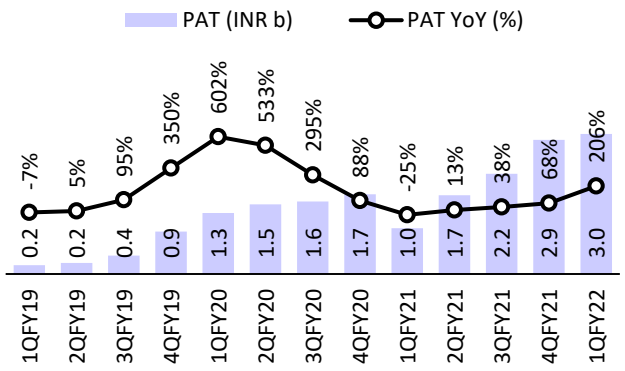
Source: Company, MOFSL

**Exhibit 3: EBITDA flat QoQ (margin at 29.6%)**



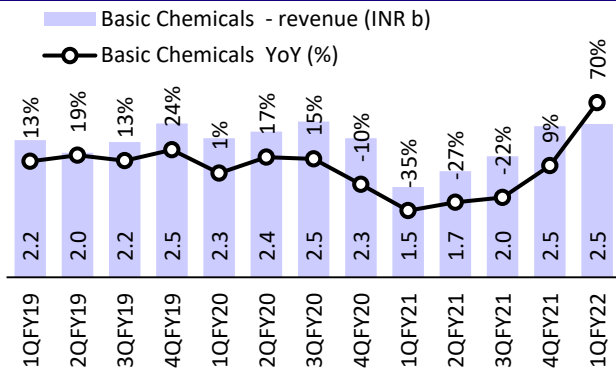
Source: Company, MOFSL

**Exhibit 4: PAT up 4% QoQ (margin at 19.8%)**



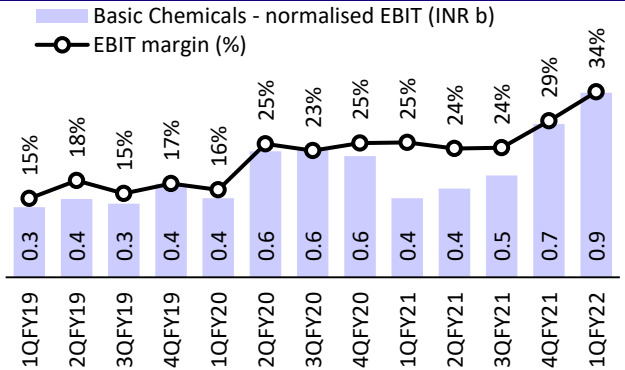
Source: Company, MOFSL

**Exhibit 5: Basic Chemicals revenue up 2% QoQ...**



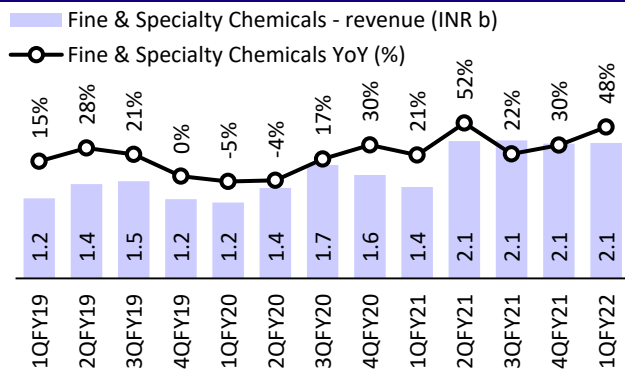
Source: Company, MOFSL

**Exhibit 6: ...while EBIT margin expands (+500bps QoQ)**



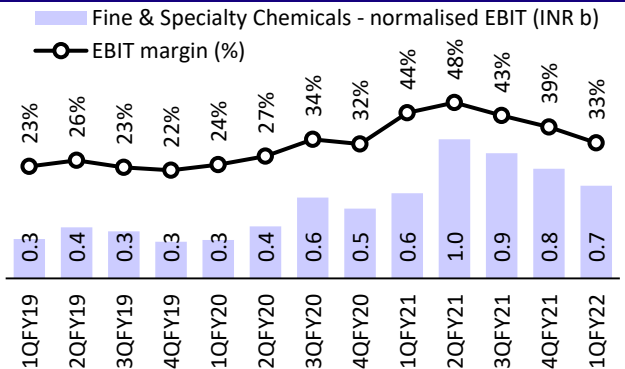
Source: Company, MOFSL

**Exhibit 7: Fine & Specialty revenue flat QoQ...**

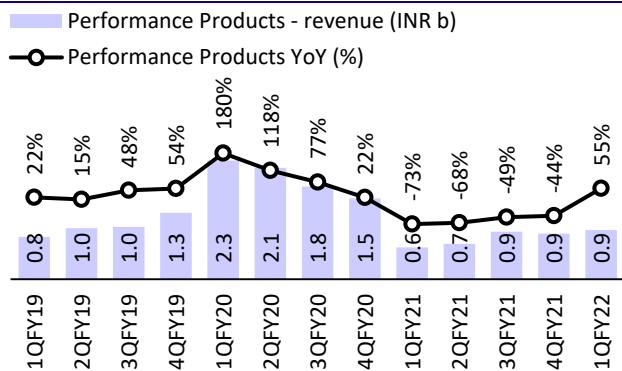


Source: Company, MOFSL

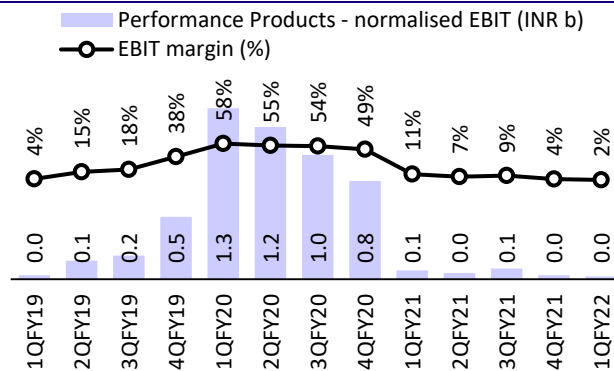
**Exhibit 8: ...although EBIT margin contracts (-600bps QoQ)**



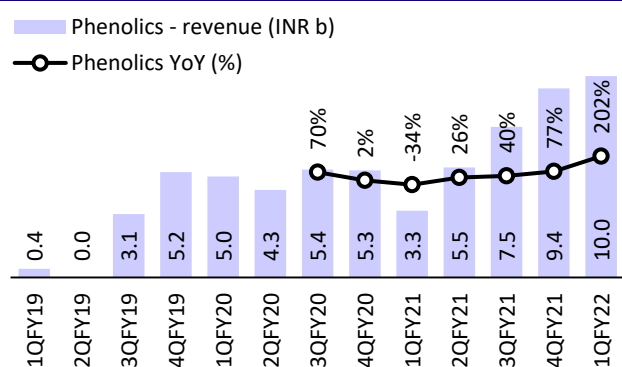
Source: Company, MOFSL

**Exhibit 9: Performance Products revenue up 8% QoQ...**

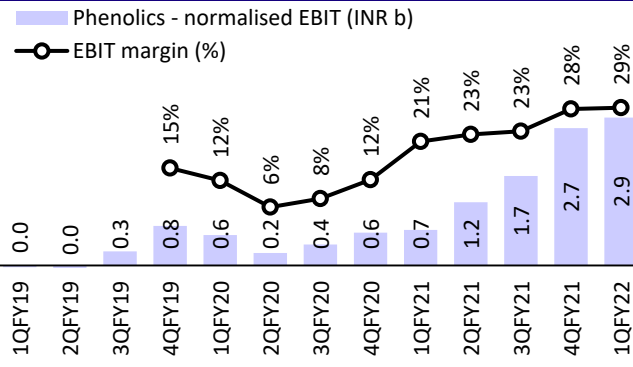
Source: Company, MOFSL

**Exhibit 10: ...with EBIT margin at just 2%**

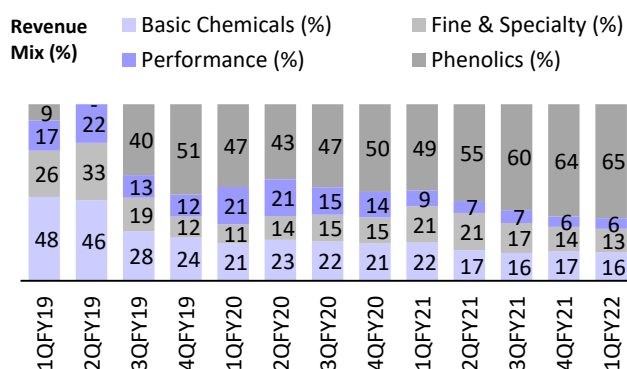
Source: Company, MOFSL

**Exhibit 11: Deepak Phenolics revenue up 7% QoQ (34% ahead of our estimates)...**

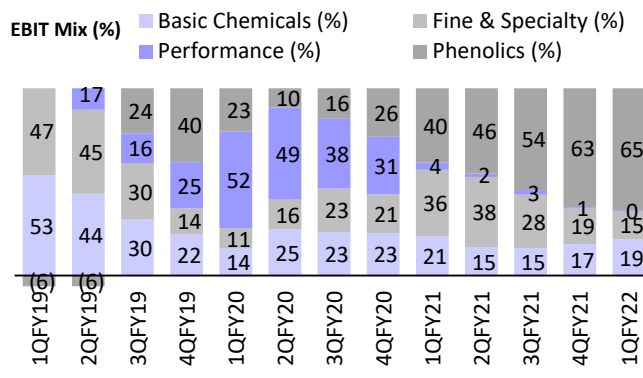
Source: Company, MOFSL

**Exhibit 12: ...as product prices and margins remain robust (EBIT margin at 29%)**

Source: Company, MOFSL

**Exhibit 13: Contribution of Phenolics to total revenue and EBIT keeps increasing (65% in 1QFY22)...**

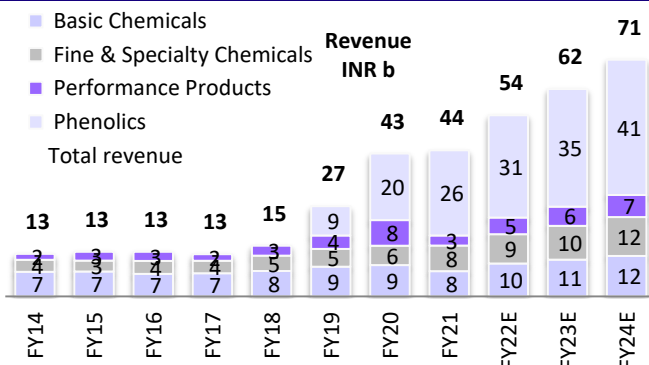
Source: Company, MOFSL

**Exhibit 14: ...while contribution of Fine & Specialty contracts to 13% and 15% for revenue and EBIT, respectively**

Source: Company, MOFSL

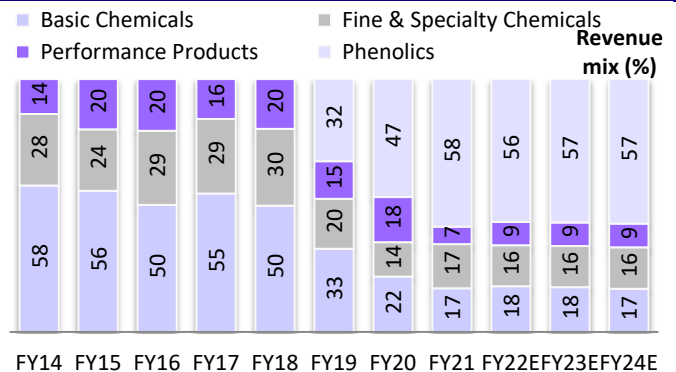
## Financials – story in charts

**Exhibit 15: Achieved ~90% utilization rate in Phenolics business in first year (FY20); currently operates at 115%**



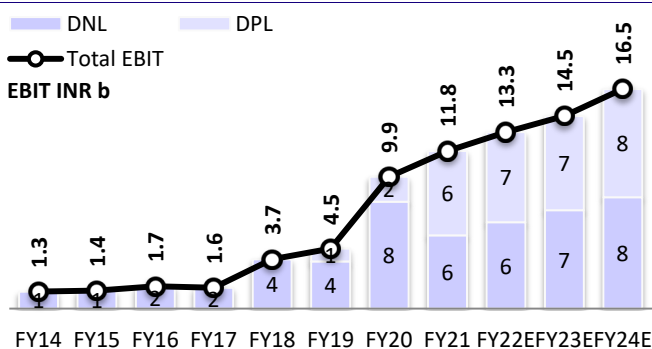
Source: MOFSL

**Exhibit 16: DPL constitutes over 58% of consolidated revenue; likely to stay at current levels**



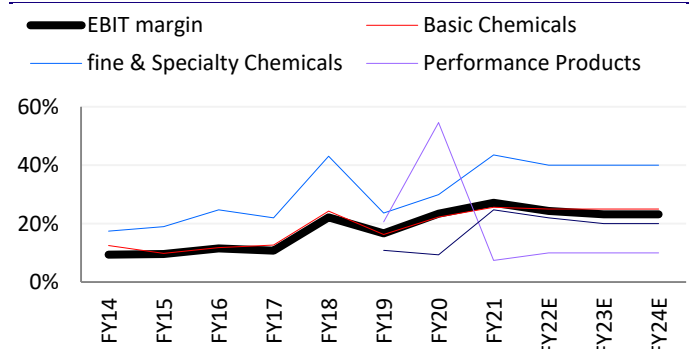
Source: Company, MOFSL

**Exhibit 17: Expect EBIT CAGR of ~14% over FY21–24 (as per company's segmental guidance)...**



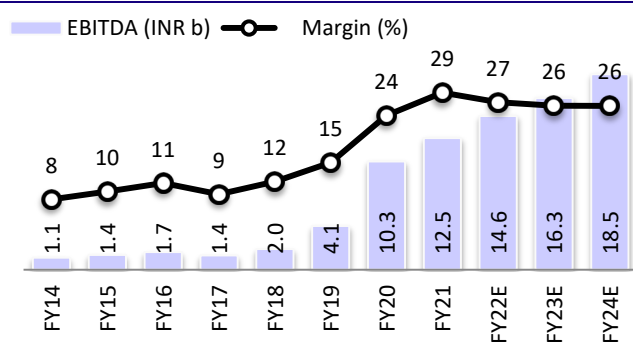
Source: Company, MOFSL

**Exhibit 18: ...with Fine & Specialty enjoys highest EBIT margin**



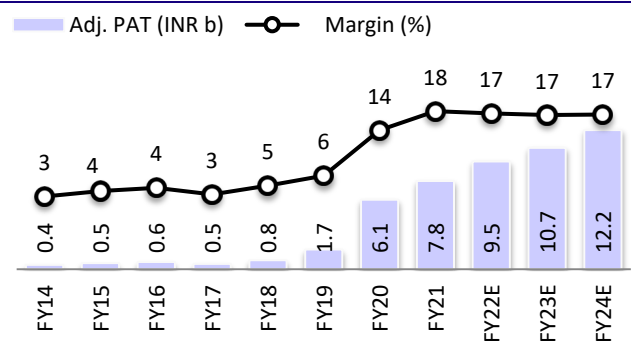
Source: Company, MOFSL

**Exhibit 19: EBITDA margin to normalize from FY21 levels**



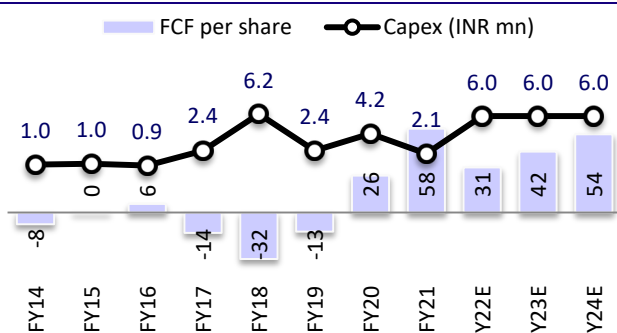
Source: Company, MOFSL

**Exhibit 20: Expect ~16% PAT CAGR over FY21–24**



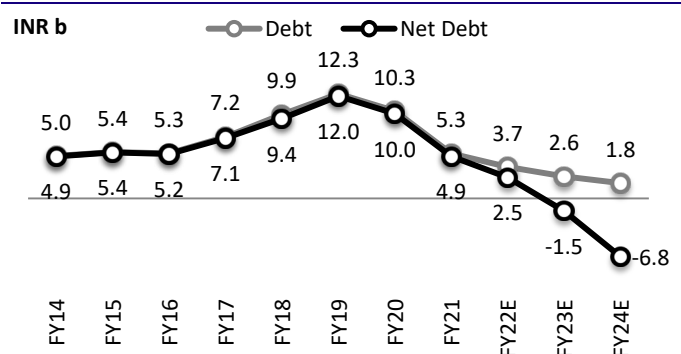
Source: Company, MOFSL

**Exhibit 21: DN to incur ~INR18b capex over FY22–24E...**



Source: Company, MOFSL

**Exhibit 22: ...but likely to turn net cash positive**



Source: Company, MOFSL

## Financials and valuations

Y/E March	FY16	FY17	FY18	FY19	FY20	FY21	FY22E	FY23E	FY24E
<b>Total Income from Operations</b>	<b>14,571</b>	<b>14,547</b>	<b>16,762</b>	<b>26,999</b>	<b>42,297</b>	<b>43,598</b>	<b>54,443</b>	<b>62,312</b>	<b>71,106</b>
Change (%)	3.0	-0.2	15.2	61.1	56.7	3.1	24.9	14.5	14.1
Gross Margins (%)	43.3	41.9	38.0	39.0	43.9	48.1	45.3	44.3	43.9
<b>EBITDA</b>	<b>1,668</b>	<b>1,355</b>	<b>1,963</b>	<b>4,139</b>	<b>10,258</b>	<b>12,470</b>	<b>14,576</b>	<b>16,273</b>	<b>18,533</b>
Margin (%)	11.4	9.3	11.7	15.3	24.3	28.6	26.8	26.1	26.1
Depreciation	395	480	526	778	1,397	1,526	1,792	2,056	2,319
<b>EBIT</b>	<b>1,273</b>	<b>874</b>	<b>1,437</b>	<b>3,361</b>	<b>8,861</b>	<b>10,944</b>	<b>12,784</b>	<b>14,217</b>	<b>16,213</b>
Int. and Finance Charges	397	341	451	832	1,149	742	358	220	154
Other Income	16	109	123	151	352	215	218	249	284
<b>PBT bef. EO Exp.</b>	<b>891</b>	<b>642</b>	<b>1,109</b>	<b>2,680</b>	<b>8,064</b>	<b>10,417</b>	<b>12,643</b>	<b>14,247</b>	<b>16,344</b>
EO Items	0	705	0	0	0	0	0	0	0
<b>PBT after EO Exp.</b>	<b>891</b>	<b>1,347</b>	<b>1,109</b>	<b>2,680</b>	<b>8,064</b>	<b>10,417</b>	<b>12,643</b>	<b>14,247</b>	<b>16,344</b>
Total Tax	262	382	318	943	1,954	2,659	3,182	3,586	4,114
Tax Rate (%)	29.4	28.4	28.7	35.2	24.2	25.5	25.2	25.2	25.2
<b>Reported PAT</b>	<b>627</b>	<b>963</b>	<b>790</b>	<b>1,737</b>	<b>6,110</b>	<b>7,758</b>	<b>9,461</b>	<b>10,661</b>	<b>12,230</b>
<b>Adjusted PAT</b>	<b>627</b>	<b>458</b>	<b>790</b>	<b>1,737</b>	<b>6,110</b>	<b>7,758</b>	<b>9,461</b>	<b>10,661</b>	<b>12,230</b>
Change (%)	18.6	-26.9	72.4	119.8	251.9	27.0	21.9	12.7	14.7
Margin (%)	4.3	3.2	4.7	6.4	14.4	17.8	17.4	17.1	17.2

### Consolidated - Balance Sheet

Y/E March	FY16	FY17	FY18	FY19	FY20	FY21	FY22E	FY23E	FY24E
Equity Share Capital	233	261	273	273	273	273	273	273	273
Total Reserves	4,496	6,887	8,949	10,443	15,446	23,194	31,235	40,297	50,693
<b>Net Worth</b>	<b>4,729</b>	<b>7,149</b>	<b>9,221</b>	<b>10,716</b>	<b>15,719</b>	<b>23,467</b>	<b>31,508</b>	<b>40,570</b>	<b>50,966</b>
Total Loans	5,288	7,239	9,866	12,286	10,279	5,271	3,690	2,583	1,808
Deferred Tax Liabilities	567	391	454	775	796	1,078	1,078	1,078	1,078
<b>Capital Employed</b>	<b>10,583</b>	<b>14,778</b>	<b>19,541</b>	<b>23,776</b>	<b>26,794</b>	<b>29,816</b>	<b>36,276</b>	<b>44,231</b>	<b>53,852</b>
Gross Block	8,842	6,106	6,403	17,749	20,460	22,304	28,304	34,304	40,304
Less: Accum. Deprn.	2,924	306	528	743	2,140	3,666	5,459	7,514	9,833
<b>Net Fixed Assets</b>	<b>5,918</b>	<b>5,801</b>	<b>5,875</b>	<b>17,006</b>	<b>18,320</b>	<b>18,637</b>	<b>22,845</b>	<b>26,790</b>	<b>30,470</b>
Capital WIP	319	3,492	9,545	339	1,723	2,068	2,068	2,068	2,068
<b>Total Investments</b>	<b>866</b>	<b>1,198</b>	<b>318</b>	<b>24</b>	<b>24</b>	<b>1,893</b>	<b>1,893</b>	<b>1,893</b>	<b>1,893</b>
<b>Curr. Assets, Loans&amp;Adv.</b>	<b>5,838</b>	<b>7,385</b>	<b>10,167</b>	<b>11,910</b>	<b>12,019</b>	<b>13,005</b>	<b>16,126</b>	<b>21,145</b>	<b>28,171</b>
Inventory	1,210	1,671	3,272	4,107	3,945	3,827	4,909	5,669	6,473
Account Receivables	3,132	3,603	4,118	5,750	6,127	7,563	7,887	9,027	10,300
Cash and Bank Balance	65	145	482	258	314	334	1,229	4,044	8,652
Cash	48	58	94	30	21	89	983	3,799	8,406
Bank Balance	17	87	388	228	293	245	245	245	245
Loans and Advances	1,431	1,965	2,296	1,795	1,633	1,281	2,102	2,406	2,745
<b>Curr. Liability &amp; Prov.</b>	<b>2,358</b>	<b>3,097</b>	<b>6,364</b>	<b>5,502</b>	<b>5,292</b>	<b>5,787</b>	<b>6,656</b>	<b>7,664</b>	<b>8,750</b>
Account Payables	1,331	2,146	5,953	4,724	3,643	4,367	4,533	5,234	5,977
Other Current Liabilities	776	832	280	587	1,385	1,144	1,783	2,041	2,328
Provisions	251	119	132	191	264	276	340	390	444
<b>Net Current Assets</b>	<b>3,480</b>	<b>4,288</b>	<b>3,803</b>	<b>6,408</b>	<b>6,727</b>	<b>7,218</b>	<b>9,471</b>	<b>13,481</b>	<b>19,421</b>
<b>Appl. of Funds</b>	<b>10,583</b>	<b>14,779</b>	<b>19,541</b>	<b>23,776</b>	<b>26,794</b>	<b>29,816</b>	<b>36,276</b>	<b>44,231</b>	<b>53,852</b>

E: MOFSL Estimates

## Financials and valuations

### Ratios

Y/E March	FY16	FY17	FY18	FY19	FY20	FY21	FY22E	FY23E	FY24E
<b>Basic (INR)</b>									
<b>EPS</b>	<b>4.6</b>	<b>3.4</b>	<b>5.8</b>	<b>12.7</b>	<b>44.8</b>	<b>56.9</b>	<b>69.4</b>	<b>78.2</b>	<b>89.7</b>
Cash EPS	7.5	6.9	9.6	18.4	55.0	68.1	82.5	93.2	106.7
BV/Share	34.7	52.4	67.6	78.6	115.2	172.0	231.0	297.4	373.6
DPS	1.0	1.1	1.3	6.5	4.5	5.5	10.4	11.7	13.4
Payout (%)	26.8	19.6	27.0	61.6	12.1	9.7	15.0	15.0	15.0
<b>Valuation (x)</b>									
P/E	443.4	606.7	352.0	160.2	45.5	35.8	29.4	26.1	22.7
Cash P/E	271.9	296.3	211.3	110.6	37.0	30.0	24.7	21.9	19.1
P/BV	58.8	38.9	30.2	26.0	17.7	11.9	8.8	6.9	5.5
EV/Sales	19.4	19.6	17.2	10.7	6.8	6.5	5.2	4.4	3.8
EV/EBITDA	169.9	210.5	146.5	70.1	28.1	22.7	19.2	17.0	14.6
Dividend Yield (%)	0.1	0.1	0.1	0.3	0.2	0.3	0.5	0.6	0.7
FCF per share	5.9	-14.1	-32.1	-13.3	25.6	58.0	31.2	42.1	54.0
<b>Return Ratios (%)</b>									
RoE	15.3	7.7	9.7	17.4	46.2	39.6	34.4	29.6	26.7
RoCE	9.1	5.6	6.5	10.5	27.6	29.4	29.4	26.9	25.2
RoIC	9.9	6.5	10.7	13.5	28.0	32.4	33.8	31.6	31.3
<b>Working Capital Ratios</b>									
Fixed Asset Turnover (x)	2.6	2.5	2.9	2.4	2.4	2.4	2.6	2.5	2.5
Asset Turnover (x)	1.4	1.0	0.9	1.1	1.6	1.5	1.5	1.4	1.3
Inventory (Days)	30	42	71	56	34	32	33	33	33
Debtor (Days)	78	90	90	78	53	63	53	53	53
Creditor (Days)	33	54	130	64	31	37	30	31	31
<b>Leverage Ratio (x)</b>									
Current Ratio	2.5	2.4	1.6	2.2	2.3	2.2	2.4	2.8	3.2
Interest Cover Ratio	3.2	2.6	3.2	4.0	7.7	14.7	35.7	64.8	105.5
Net Debt/Equity	1.1	1.0	1.0	1.1	0.6	0.2	0.1	0.0	-0.1

### Consolidated - Cash Flow Statement

(INR m)

Y/E March	FY16	FY17	FY18	FY19	FY20	FY21	FY22E	FY23E	FY24E
OP/(Loss) before Tax	891	1,347	1,109	2,680	8,064	10,417	12,643	14,247	16,344
Depreciation	395	480	528	778	1,397	1,526	1,792	2,056	2,319
Others	403	-403	481	829	1,262	853	358	220	154
Direct Taxes Paid	-188	-162	-279	-561	-1,985	-2,365	-3,182	-3,586	-4,114
(Inc)/Dec in WC	171	-772	-9	-3,123	-1,092	-440	-1,358	-1,195	-1,332
<b>CF from Operations</b>	<b>1,673</b>	<b>490</b>	<b>1,830</b>	<b>603</b>	<b>7,647</b>	<b>9,991</b>	<b>10,254</b>	<b>11,741</b>	<b>13,371</b>
(Inc)/Dec in FA	-865	-2,412	-6,206	-2,410	-4,160	-2,086	-6,000	-6,000	-6,000
<b>Free Cash Flow</b>	<b>808</b>	<b>-1,922</b>	<b>-4,376</b>	<b>-1,808</b>	<b>3,487</b>	<b>7,905</b>	<b>4,254</b>	<b>5,741</b>	<b>7,371</b>
<b>CF from Investments</b>	<b>-1,694</b>	<b>-3,526</b>	<b>-5,247</b>	<b>-1,626</b>	<b>-4,279</b>	<b>-3,962</b>	<b>-6,000</b>	<b>-6,000</b>	<b>-6,000</b>
Inc/(Dec) in Debt	-254	2,160	2,626	2,033	-1,088	-5,217	-1,581	-1,107	-775
Interest Paid	-372	-342	-450	-841	-1,134	-736	-358	-220	-154
Dividend Paid	-125	-167	-188	-213	-1,060	-4	-1,419	-1,599	-1,835
<b>CF from Fin. Activity</b>	<b>51</b>	<b>3,046</b>	<b>3,453</b>	<b>958</b>	<b>-3,376</b>	<b>-5,962</b>	<b>-3,359</b>	<b>-2,926</b>	<b>-2,763</b>
<b>Inc/Dec of Cash</b>	<b>30</b>	<b>10</b>	<b>36</b>	<b>-64</b>	<b>-8</b>	<b>67</b>	<b>895</b>	<b>2,815</b>	<b>4,608</b>
Opening Balance	17	47	58	94	30	22	89	984	3,799
<b>Closing Balance</b>	<b>48</b>	<b>58</b>	<b>94</b>	<b>30</b>	<b>21</b>	<b>89</b>	<b>983</b>	<b>3,799</b>	<b>8,406</b>

## NOTES

Explanation of Investment Rating	
Investment Rating	Expected return (over 12-month)
BUY	>=15%
SELL	< - 10%
NEUTRAL	< - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

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