Q1FY22 Result Review

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Kansai Nerolac (KNPL) SELL

Below expected; inflation remains chief concern

TP	Rs562
CMP	Rs629
Potential upside / downside	-11%

V/s Consensus

EPS (Rs)	FY22E	FY23E
IDBI Capital	11.0	14.0
Consensus	11.0	14.1
% difference	0.3	(0.7)

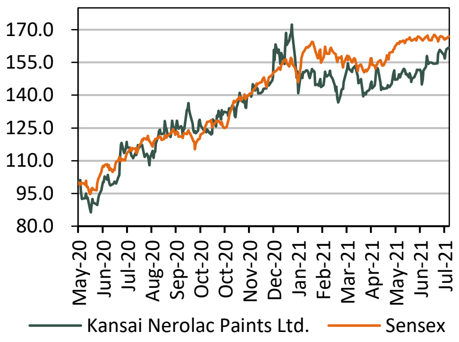
Key Stock Data

Bloomberg / Reuters	KNPL IN/KANE.BO
Sector	Paints
Shares o/s (mn)	539
Market cap. (Rs mn)	338,792
Market cap. (US$ mn)	4,553
3-m daily average value (Rs mn)	118.0
52-week high / low	Rs680 / 420
Sensex / Nifty	52,951 / 15,885

Shareholding Pattern (%)

Promoters	75.0
FII	3.7
DII	11.5
Public	9.8

Relative to Sensex (%)



Price Performance (%)

	-1m	-3m	-12m
Absolute	7.0	13.0	45.3
Rel to Sensex	6.1	4.5	4.5

Summary

Kansai Nerolac (KNPL) result was below our estimates due to higher than expected inflation in raw material cost. Demand in decorative coating business remained resilient during days when lockdown restrictions were minimal. Positively, value growth stood higher than volume growth driven by higher contribution from emulsions. Also, management guides to maintain focus on premium portfolio as, due to inflation, value products (like putty) will put pressure on operating margins due to inferior economics. Inflation continues to put pressure on gross margin. KNPL guides for more price hikes to offset inflation going forward. However, taking price hike in industrial coatings will be relatively tougher. Revenue from new products (including construction chemical) is tracking well (10% of sales in 1QFY22). KNPL can sell new products at +50% of existing dealers. We have trimmed our EPS estimate by 6-12% during FY22-23E due to rise in inflationary pressure. Our revised TP stands at Rs 562 with SELL rating.

Key Highlights and Investment Rationale

- **Value growth ahead of volume growth; industrial continues to be impacted**
  Revenue grew 118%YoY (on a low base; -59%YoY in 1QFY21) led by revival in decorative coatings demand during initial weeks of Apr'21 and in Jun'21 when lockdown restrictions were eased. Value growth stood at higher than volume growth due to higher revenue share from emulsions. However, Industrial demand continues to be impacted due to slower than expected production in auto manufacturing. Revenue from new product launches now contributes c. 10% to sales. In international market; 45-50 days lockdown in Nepal and Bangladesh impacted paint demand. However, Bangladesh recorded good growth despite lockdown.
- **Judicious cost control aids EBITDA margin expansion**
  Despite price hikes taken in both decorative and industrial coatings, Gross margin contracted 743bp YoY (2nd consecutive quarter) to 34% due to significant inflation in raw material prices. EBITDA margin expanded by 92 bps to 14.4% due to judicious control over cost and overheads
- **Trim EPS estimates; SELL**
  We have reduced our margin expectations due to input cost inflation. Consequently, we have trimmed our EPS estimates for FY22E by 12% and for FY23E 6%. Our revised TP stands at Rs 562 (vs previous TP of Rs 599). At current price, we have SELL rating.

Financial snapshot **(Rs mn)**

Year	FY19	FY20	FY21	FY22E	FY23E
Revenue	51,736	49,432	46,127	55,155	64,022
EBITDA	7,420	7,816	8,005	9,049	11,319
EBITDA (%)	14.3	15.8	17.4	16.4	17.7
Adj. PAT	4,674	5,354	5,204	5,940	7,569
EPS (Rs)	8.7	9.9	9.7	11.0	14.0
EPS Growth (%)	(9.5)	14.5	(2.8)	14.1	27.4
PE (x)	68.5	59.8	61.6	53.9	42.3
Dividend Yield (%)	0.4	0.4	0.7	0.4	0.4
EV/EBITDA (x)	43.1	40.8	39.9	34.7	27.5
RoE (%)	14.3	14.8	13.2	13.8	15.6
RoCE (%)	19.3	17.8	16.3	17.0	19.5

Source: IDBI Capital Research;

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Exhibit 1: Actual vs. Estimates

(Rs mn)

	Actual	IDBI Estimate	*% variation IDBI*
Revenue	13,012	12,531	*3.8%*
EBITDA	1,872	2,193	*-14.7%*
Margin (%)	*14.4%*	*17.5*	
APAT	1,187	1,405	*-15.5%*

Source: Company; IDBI Capital Research

Exhibit 2: Standalone Quarterly Snapshot

(Rs mn)

Financial Snapshot	Q1FY22	Q1FY21	*YoY (%)*	Q4FY21	*QoQ (%)*	FY21	FY20	*YoY (%)*
Revenues	**13,012**	**5,981**	***117.6***	**13,305**	***-2.2***	**46,900**	**49,432**	***-5.1***
COGS	8,560	3,490	*145.3*	8,729	*-1.9*	29,114	30,576	*-4.8*
Gross profit	4,452	2,491	*78.7*	4,576	*-2.7*	17,786	18,856	*-5.7*
Gross Margin (%)	*34.2*	*41.6*	*-743 bps*	*34.4*	*-18 bps*	*37.9*	*38.1*	*-22 bps*
Employee expenses	698	645	*8.2*	659	*6.0*	2,586	2,694	*-4.0*
% of net sales	*5.4*	*10.8*	*-542 bps*	*5.0*	*42 bps*	*5.5*	*5.4*	*6 bps*
Other Expenses	1,882	1,041	*80.8*	1,884	*-0.1*	6,869	8,346	*-17.7*
% of net sales	*14.5*	*17.4*	*-294 bps*	*14.2*	*30 bps*	*14.6*	*16.9*	*-224 bps*
EBITDA	**1,872**	**805**	***132.5***	**2,034**	***-8.0***	**8,331**	**7,816**	***6.6***
EBITDA Margin (%)	*14.4*	*13.5*	*92 bps*	*15.3*	*-90 bps*	*17.8*	*15.8*	*195 bps*
Depreciation	358	318	*12.3*	405	*-11.6*	1,390	1,199	*15.9*
EBIT	**1,514**	**487**	***211.0***	**1,629**	***-7.05***	**6,941**	**6,617**	***4.9***
Other Income	97	79	*21.9*	124	*-21.9*	387	269	*44.1*
Interest Expenses	25	13	*90.9*	40	*-37.3*	75	50	*49.8*
PBT	**1,586**	**553**	***186.8***	**1,713**	***-7.4***	**7,253**	**6,836**	***6.1***
Taxes	399	126		435		1,835	1,482	
Adjusted PAT	**1,187**	**427**	***177.9***	**1,278**	***-7.1***	**5,418**	**5,354**	***1.2***
Extra-ordinary items	0	0		0		108	0	
Reported PAT	**1,187**	**427**	***177.9***	**1,278**	***-7.1***	**5,310**	**5,354**	***-0.8***
Diluted EPS (Rs)	**2.20**	**0.79**	***177.9***	**2.37**	***-7.1***	**9.85**	**9.93**	***-0.8***

Source: Company; IDBI Capital Research

Exhibit 3: Consolidated Quarterly Snapshot **(Rs mn)**

Financial Snapshot	Q1FY22	Q1FY21	*YoY (%)*	Q4FY21	*QoQ (%)*	FY21	FY20	*YoY (%)*
Revenues	**14,028**	**6,389**	**119.6**	**14,596**	**-3.9**	**50,743**	**52,800**	***-3.9***
COGS	9,230	3,741	146.7	9,552	-3.4	31,465	32,586	*-3.4*
Gross profit	4,798	2,649	81.1	5,044	-4.9	19,277	20,213	*-4.6*
Gross Margin (%)	34.2	41.5	-725 bps	34.6	-36 bps	*38.0*	*38.3*	*-29 bps*
Employee expenses	821	748	9.7	787	4.3	3,047	3,104	*-1.8*
% of net sales	5.8	11.7	-586 bps	5.4	46 bps	*6.0*	*5.9*	*13 bps*
Other Expenses	2,072	1,132	83.0	2,123	-2.4	7,598	9,065	*-16.2*
% of net sales	14.8	17.7	-295 bps	14.5	23 bps	*15.0*	*17.2*	*-220 bps*
EBITDA	**1,905**	**768**	**148.0**	**2,135**	**-10.7**	**8,633**	**8,044**	***7.3***
EBITDA Margin (%)	13.6	12.0	156 bps	14.6	-104 bps	*17.0*	*15.2*	*178 bps*
Depreciation	417	379	10.0	482	-13.4	1,653	1,421	*16.3*
EBIT	**1,488**	**389**	**282.5**	**1,653**	**-9.98**	**6,980**	**6,623**	***5.4***
Other Income	99	82	21.8	109	-9.1	382	255	*49.7*
Interest Expenses	67	55	20.9	78	-14.4	237	209	*13.5*
PBT	**1,521**	**416**	**266.0**	**1,684**	**-9.7**	**7,125**	**6,669**	***6.8***
Taxes	407	119		448		1,867	1,512	
Adjusted PAT	**1,114**	**296**	**275.8**	**1,236**	**-9.9**	**5,257**	**5,157**	***1.9***
Extra-ordinary items	0	0		0		0	0	
Minority Interest	27	38		7		38	52	
Profit attributable to owners	**1,141**	**335**	**240.9**	**1,243**	**-8.2**	**5,296**	**5,210**	***1.6***
EPS	**2.12**	**0.62**	**240.9**	**2.31**	**-8.2**	**9.8**	**9.7**	***1.7***

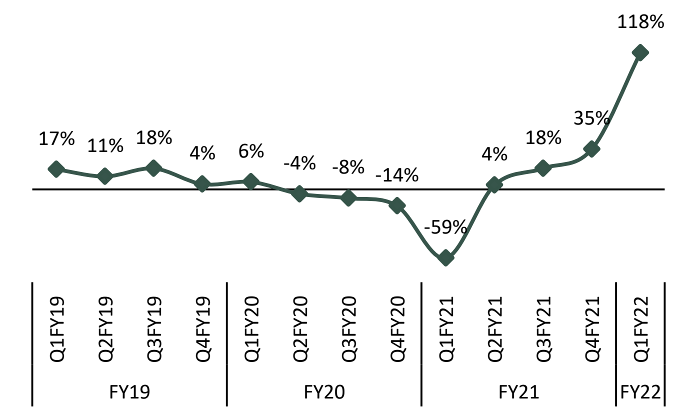
Source: Company; IDBI Capital Research

Exhibit 4: Change in estimates

	FY22E			FY23E		
	New	Old	*(%) Chg*	New	Old	*(%) Chg*
Revenue (Rs mn)	55,155	55,155	*0.0%*	64,022	64,022	*0.0%*
EBITDA (Rs mn)	9,049	10,196	*-11.3%*	11,319	11,982	*-5.5%*
EBITDA margin (%)	*16.4%*	*18.5%*		*17.7%*	*18.7%*	
Net profit (Rs mn)	5,940	6,769	*-12.2%*	7,569	8,061	*-6.1%*
EPS (Rs)	11.0	12.6	*-12.2%*	14.0	15.0	*-6.1%*

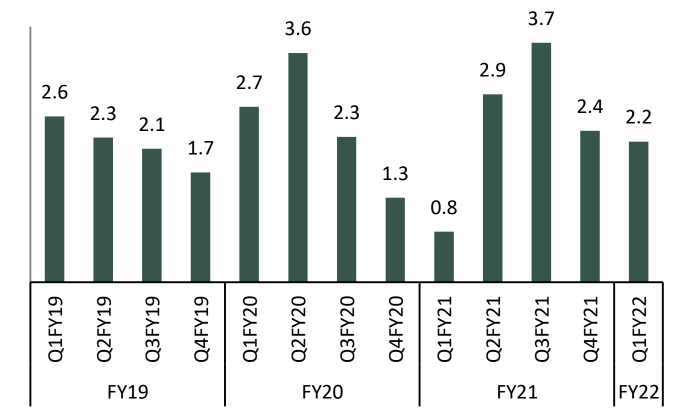
Source: Company; IDBI Capital Research

Exhibit 5: Revenue growth trend (% YoY)



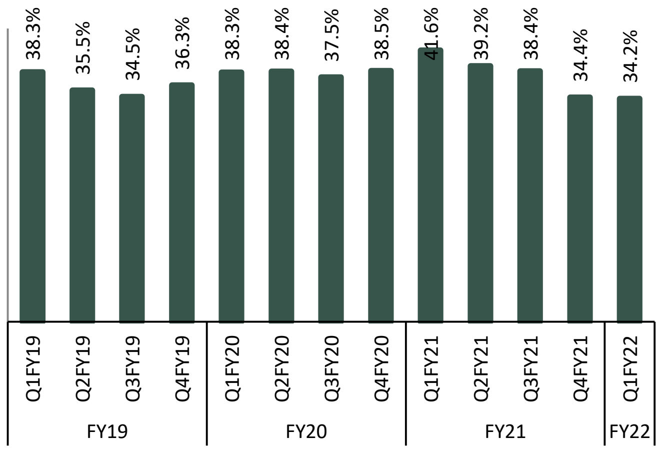
Source: Company; IDBI Capital Research

Exhibit 6: EPS trend



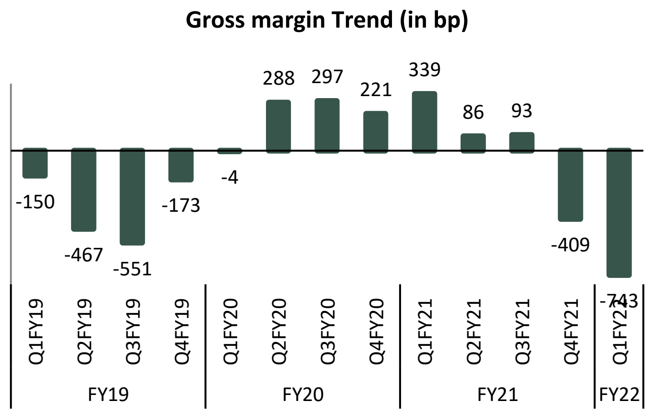
Source: Company; IDBI Capital Research

Exhibit 7: Gross margin trend (% YoY)



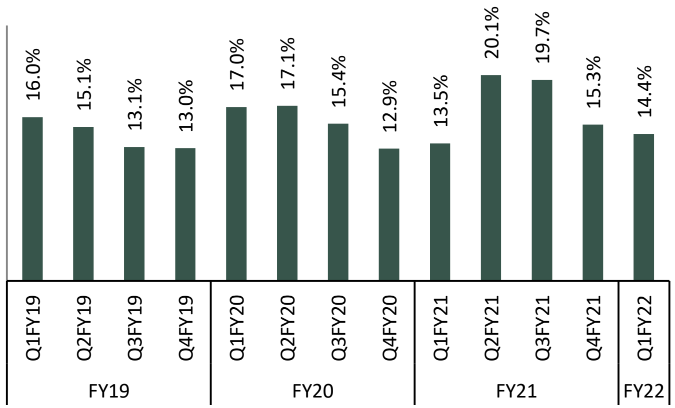
Source: Company; IDBI Capital Research

Exhibit 8: Change in gross margin (YoY in bp)



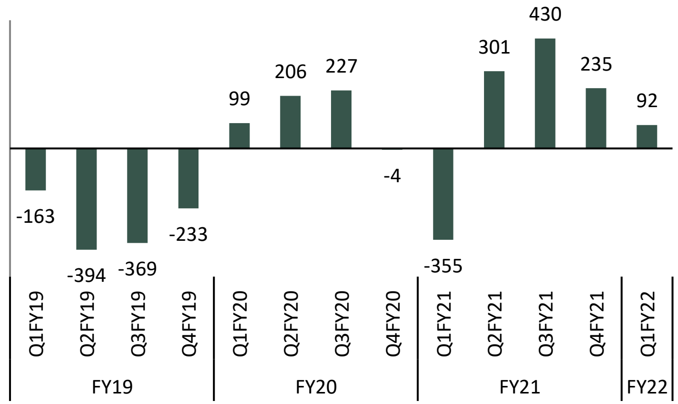
Source: Company; IDBI Capital Research

Exhibit 9: EBITDA margin trend (% YoY)



Source: Company; IDBI Capital Research

Exhibit 10: Change in EBITDA margin (YoY in bp)



Source: Company; IDBI Capital Research

Financial Summary

Profit & Loss Account

(Rs mn)

Year-end: March	FY20	FY21	FY22E	FY23E
Net sales	**49,432**	**46,127**	**55,155**	**64,022**
Growth (%)	*(4.5)*	*(6.7)*	*19.6*	*16.1*
Operating expenses	(41,616)	(38,121)	(46,107)	(52,702)
EBITDA	**7,816**	**8,005**	**9,049**	**11,319**
Growth (%)	*5.3*	*2.4*	*13.0*	*25.1*
Depreciation	(1,199)	(1,361)	(1,434)	(1,548)
EBIT	**6,617**	**6,644**	**7,615**	**9,771**
Interest paid	(50)	(55)	(55)	(55)
Other income	269	359	378	399
Pre-tax profit	**6,836**	**6,948**	**7,938**	**10,115**
Tax	(1,482)	(1,744)	(1,998)	(2,546)
Effective tax rate (%)	*21.7*	*25.1*	*25.2*	*25.2*
Minority Interest	-	-	-	-
Net profit	**5,354**	**5,204**	**5,940**	**7,569**
Exceptional items	-	-	-	-
Adjusted net profit	**5,354**	**5,204**	**5,940**	**7,569**
Growth (%)	*14.6*	*(2.8)*	*14.1*	*27.4*
Shares o/s (mn nos)	*539*	*539*	*539*	*539*

Cash Flow Statement

(Rs mn)

Year-end: March	FY20	FY21	FY22E	FY23E
Pre-tax profit	6,836	6,948	7,938	10,115
Depreciation	1,199	1,390	1,434	1,548
Tax paid	(1,560)	(1,463)	(1,998)	(2,546)
Chg in working capital	(147)	(631)	1,303	(1,879)
Other operating activities	(122)	(55)	55	55
Cash flow from operations (a)	**6,206**	**6,190**	**8,732**	**7,293**
Capital expenditure	(2,170)	(965)	(1,500)	(2,800)
Chg in investments	(1,310)	(3,648)	-	-
Other investing activities	41	-	-	-
Cash flow from investing (b)	**(3,439)**	**(4,613)**	**(1,500)**	**(2,800)**
Equity raised/(repaid)	-	-	0	-
Debt raised/(repaid)	(63)	-	-	-
Dividend (incl. tax)	(1,401)	(2,371)	(1,348)	(1,348)
Chg in minorities	-	-	-	-
Other financing activities	(455)	(311)	(55)	(55)
Cash flow from financing (c)	**(1,920)**	**(2,682)**	**(1,402)**	**(1,403)**
Net chg in cash (a+b+c)	**847**	**(1,105)**	**5,830**	**3,090**

Balance Sheet

(Rs mn)

Year-end: March	FY20	FY21	FY22E	FY23E
Net fixed assets	18,731	19,318	19,384	20,636
Investments	1,499	1,655	1,655	1,655
Other non-curr assets	3,061	2,179	2,179	2,179
Current assets	**22,634**	**28,940**	**35,000**	**41,524**
Inventories	9,301	10,902	11,182	12,980
Sundry Debtors	6,745	8,362	8,362	9,998
Cash and Bank	1,663	753	6,533	9,623
Marketable Securities	-	-	-	-
Loans and advances	-	-	-	-
Total assets	**45,924**	**52,091**	**58,217**	**65,994**
Shareholders' funds	**37,869**	**40,809**	**45,401**	**51,623**
Share capital	539	539	539	539
Reserves & surplus	37,330	40,270	44,863	51,084
Total Debt	**-**	**-**	**-**	**-**
Secured loans	-	-	-	-
Unsecured loans	-	-	-	-
Other liabilities	1,340	1,611	1,611	1,611
Curr Liab & prov	**6,716**	**9,671**	**11,205**	**12,760**
Current liabilities	6,559	9,481	11,015	12,570
Provisions	157	190	190	190
Total liabilities	**8,056**	**11,282**	**12,816**	**14,371**
Total equity & liabilities	**45,924**	**52,091**	**58,217**	**65,994**
Book Value (Rs)	**70**	**76**	**84**	**96**

Source: Company; IDBI Capital Research

Financial Ratios

Year-end: March	FY20	FY21	FY22E	FY23E
Adj. EPS (Rs)	9.9	9.7	11.0	14.0
Adj. EPS growth (%)	*14.5*	*(2.8)*	*14.1*	*27.4*
EBITDA margin (%)	*15.8*	*17.4*	*16.4*	*17.7*
Pre-tax margin (%)	*13.8*	*15.1*	*14.4*	*15.8*
ROE (%)	*14.8*	*13.2*	*13.8*	*15.6*
ROCE (%)	*17.8*	*16.3*	*17.0*	*19.5*
Turnover & Leverage ratios (x)				
Asset turnover (x)	1.1	0.9	1.0	1.0
Leverage factor (x)	1.2	1.2	1.3	1.3
Net margin (%)	*10.8*	*11.3*	*10.8*	*11.8*
Net Debt/Equity (x)	(0.0)	(0.0)	(0.1)	(0.2)
Working Capital & Liquidity ratio				
Inventory days	69	86	74	74
Receivable days	50	66	55	57
Payable days	46	77	77	78

Valuation

Year-end: March	FY20	FY21	FY22E	FY23E
P/E (x)	59.8	61.6	53.9	42.3
Price / Book value (x)	8.5	7.9	7.1	6.2
PCE (x)	48.9	48.8	43.4	35.1
EV / Net sales (x)	6.4	6.9	5.7	4.9
EV / EBITDA (x)	40.8	39.9	34.7	27.5
Dividend Yield (%)	*0.4*	*0.7*	*0.4*	*0.4*

Notes

Dealing	(91-22) 6836 1111	dealing@idbicapital.com

Key to Ratings Stocks:

BUY: 15%+; **HOLD:** -5% to 15%; **SELL:** -5% and below.

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