

NOT RATED**CHEMPLAST SANMAR**

| Oil & Gas

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Uptick in PVC prices could aid margin recovery

- Management expects to see benefit of PVC price recovery from Q4 after a muted Q3
- CSL poised to grow custom manufacturing business with phase-1 expansion delivery in Q2FY24 and plans to expedite phase-2
- Management focused on accelerating growth in specialty segment and conserving cash for growth capital

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We hosted N Muralidharan, Chief Financial Officer of Chemplast Sanmar (CSL, Not Rated). Key takeaways:

PVC recovery faster than expected: While CSL's Q3FY23 results are likely to be muted due to the effect of 14 successive price cuts between Apr'22 and Nov'22, management indicated that recovery has set in from Dec'22. With stronger domestic demand, the pace of recovery was faster than CSL's expectation in Dec'22, marked by five price hikes in suspension PVC (S-PVC) cumulating to Rs 14k/t (or ~15%) and three in paste PVC (P-PVC) cumulating to Rs 17.5k/t. With a lag in absorbing raw material prices, gross margin has started inching up. Recovery in China post lunar holidays will provide additional support and is likely to outweigh the slowdown in the western world. Restart of carbide-based capacity in China is not seen as a major risk.

PVC market deficit to persist even after expansion: With new expansion likely to add 2.5mt of capacity in phases to the industry's existing 1.5mt capacity, and domestic demand expected to climb to 4.5-5.0mt over the next 3-4 years, deficit is likely to persist in the Indian market. The impact of material carbide-based capacity addition will depend upon cost economics for imported coal.

Customs manufacturing poised for growth: After raising FY23 topline growth guidance to 30% YoY last quarter, CSL confirmed that it is on track to deliver bigger phase-1 expansion in Q2FY24 and further ramp-up over two years. With advancing of civil works, management plans to expedite phase-2 delivery within 10-12 months of startup. The company is focusing on agrochemical innovators for further growth and highlighted its elevation of vendor status with one large customer.

Expansion benefits from FY24: Management aims to deliver 41kt of S-PVC expansion in H2FY24 with ramp-up to full capacity within 3-4 months, and 20kt of chlorine restoration in H1FY24 with ramp-up by year-end.

Targeting accelerated growth in specialty segment: CLS is looking to spur growth in the specialty segment and is conserving capital for additional growth projects.

| | |
|------------------|--------------------|
| Ticker/Price | CHEMPLAS IN/Rs 425 |
| Market cap | US\$ 0.8bn |
| Free float | 44% |
| 3M ADV | US\$ 0.1mn |
| 52wk high/low | Rs 685/Rs 358 |
| Promoter/FPI/DII | 55%/26%/18% |

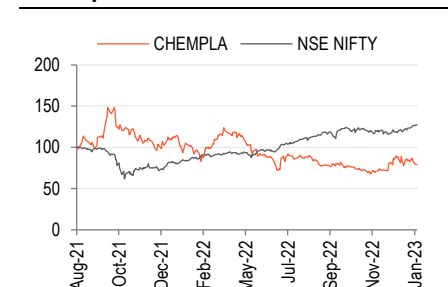
Source: NSE | Price as of 12 Jan 2023

Key financials

| Y/E 31 Mar | FY20A | FY21E | FY22E |
|-------------------------|--------|--------|--------|
| Total revenue (Rs mn) | 12,577 | 37,987 | 58,920 |
| EBITDA (Rs mn) | 3,181 | 9,615 | 11,968 |
| Adj. net profit (Rs mn) | 461 | 4,101 | 6,351 |
| Adj. EPS (Rs) | 2.04 | 30.59 | 42.75 |
| Consensus EPS (Rs) | | | |
| Adj. ROAE (%) | - | - | 2.09 |
| Adj. P/E (x) | - | - | 15.2 |
| EV/EBITDA (x) | - | - | 8.5 |
| Adj. EPS growth (%) | - | - | 39.8 |

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE



Additional takeaways

Improving near-term outlook

- CSL's S-PVC gross margin inched up from US\$ 180-190/t in Nov'22 to US\$ 200/t currently but is still short of the mid-cycle level of US\$ 250/t. P-PVC contribution has also improved but is still below the mid-cycle level of Rs 30-40k/t.
- Higher energy cost (i.e. natural gas and coal) has a harsher impact on integrated P-PVC than S-PVC due to higher usage of energy in caustic soda production. Stronger chlorine prices in Q3FY23 reflected the impact of higher energy costs. Caustic soda prices have weakened recently.
- While the S-PVC CFR India price has recovered from the recent bottom of US\$ 700/t to US\$ 930/t, the P-PVC CFR India price has recovered to US\$ 1,100/t.
- Import pressure from China has significantly eased with imports reducing from a peak of 98kt in Jun'22 to just 12kt in Dec'22. Other S-PVC importers include Japan, Taiwan, South Korea and, to some extent, the US.
- For P-PVC, India's key import partners are Japan and Taiwan. South Korea has now backed out after a supply shortfall in its domestic market.
- Indian demand has recovered strongly and is likely to surpass pre-Covid levels of 3.3mt in FY23. Restocking demand has returned as well with multiple price hikes. CSL has completely sold off its inventory and is running only 3-4 days of stock.
- Chloromethane prices have remained reasonably stable.
- Hydrogen peroxide prices have stabilised after facing pressure from an increase in imports from Bangladesh in Q3.

Global PVC market to tighten over medium term

- While global PVC capacity stands at 56mt, current global demand totals 47mt. Amongst regional markets, China accounts for 26mt of capacity and 19mt of demand. North America accounts for 8mt of capacity and 5mt of demand.
- Based on announced expansion projects, global capacity will increase to 61mt whereas global demand will rise by 9mt to 56mt over the medium term.
- Average utilisation of 90% would be required over medium-term, tightening global markets. With ~20mt of Chinese capacity typically delivering average utilisation of 70%, tightness for the rest of the markets will increase significantly.

Strong Indian demand

- The Indian pipes market accounts for 70% of domestic PVC resin demand. Specifically, usage of pipes in irrigation, affordable housing and water supply is estimated to account for 8.5mt of total demand over the medium term.
- The use of PVC resin in PVC profiles for doors/windows accounts for just 4% of PVC resin consumption in India against 25% in western markets. This is likely to increase sharply in India given a growing share of large builders in the residential segment, which drives standardisation and increased use of PVC profiles.

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BUY – Expected return >+15%

HOLD – Expected return from -6% to +15%

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

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