

SELL

TP: Rs 1,870 | ▼ 29%

PIDILITE INDUSTRIES

Construction Materials

11 August 2022

Sound business but valuations lofty; reiterate SELL

- Consolidated Q1 net revenue increased 60% YoY to Rs 31bn as the C&B/B2B segments grew 64%/50%
- Gross margin contracted 740bps YoY to ~42% due to a spike in VAM prices to US\$ 2,200-2400/mt from US\$ 1,608/mt in Q1FY22
- Maintain SELL as valuations do not adequately price in the risks to growth and margins; TP unchanged at Rs 1,870

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Sound revenue growth: PIDI's consolidated Q1FY23 net revenue grew 60% YoY to Rs 31bn led by a combination of higher volumes and measured price hikes. Consumer & Bazaar (C&B) segment revenue increased 64% YoY to Rs 24.4bn, but segmental EBIT margin contracted 295bps to 22%. The B2B segment grew 50% YoY to Rs 7.2bn with EBIT margin expanding 165bps to 10.4%.

RM cost eases sequentially: Gross margin contracted 740bps YoY (+180bps QoQ) to ~42% as prices of key raw material VAM soared to US\$ 2,200-2,400/mt vs. US\$ 1,608/mt in Q1FY22 (US\$ 2,600-2,700/mt in Q4FY22). Management expects VAM prices to be at US 2,300-2,500/mt in Q2. A decline in employee expenses (-430bps YoY to 10.2%) and other expenses (-220bps YoY to 14.4%) as a percentage of sales restricted EBITDA margin contraction to 90bps YoY at 17.1%.

Solid standalone performance: PIDI's standalone sales grew 62% YoY to Rs 27.9bn backed by underlying sales volume and mix growth of 44%. C&B/B2B revenue rose 66%/51% YoY to Rs 22bn/Rs 6.3bn. C&B/B2B volume and mix growth stood at 49%/29%. Gross/EBITDA margins contracted 800bps/140bps YoY to 40.8%/17.5%.

Near-term challenges to growth and margins: Despite a softening of commodity prices, PIDI witnessed record raw material costs in Q1. A major portion of these inputs will be consumed in Q2, implying sustained pressure on margins. This apart, demand weakness in rural areas and small towns poses a near-term challenge for the company.

Valuations lofty; reiterate SELL: PIDI has posted a 3Y revenue CAGR of 15% during Q1 vs. 19% for closest peer Asian Paints (APNT). In addition, consensus estimates peg APNT's revenue CAGR over FY22-FY24 at 17% vs. our 10% forecast for PIDI, implying that the latter's valuation premium (~10% historically) to APNT will shrink going forward. At current valuations of 104x/88x FY23E/FY24E EPS, the stock is well above its 5Y median P/E of 67x. In our view, valuations do not adequately price in the risks to growth and margins. We maintain SELL with an unchanged TP of Rs 1,870, valuing the stock at 62x FY24E EPS.

Key changes

Target	Rating
◀ ▶	◀ ▶

Ticker/Price	PIDI IN/Rs 2,641
Market cap	US\$ 16.9bn
Free float	30%
3M ADV	US\$ 12.1mn
52wk high/low	Rs 2,765/Rs 1,989
Promoter/FPI/DII	70%/11%/19%

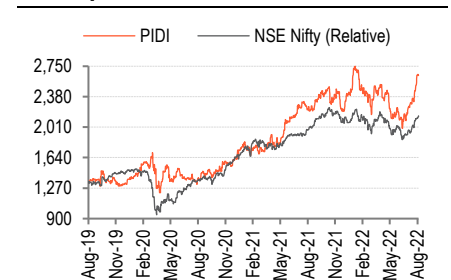
Source: NSE | Price as of 11 Aug 2022

Key financials

Y/E 31 Mar	FY22A	FY23E	FY24E
Total revenue (Rs mn)	99,210	1,03,920	1,19,726
EBITDA (Rs mn)	18,473	19,745	23,347
Adj. net profit (Rs mn)	11,965	12,932	15,307
Adj. EPS (Rs)	23.5	25.4	30.1
Consensus EPS (Rs)	23.5	33.1	38.9
Adj. ROAE (%)	19.9	19.4	21.1
Adj. P/E (x)	112.1	103.8	87.7
EV/EBITDA (x)	72.4	67.9	57.4
Adj. EPS growth (%)	5.5	8.1	18.4

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE



Earnings call highlights

- Management believes the near-term outlook remains challenging and is cautiously optimistic for the medium term given the recent softening of input costs (led by lower oil prices), a good monsoon and continued healthy demand conditions in the housing and home improvement sector. PIDI expects its performance in Q2FY23 to be similar to that in Q1.
- Management indicated that volumes are a bigger priority than margins, and guided for EBITDA margin to be in the range of 20-24% in FY23.
- VAM is moderating and currently, the spot has gone below US\$ 2,000/mt and is trading at US\$ 1,600-1,800/mt. Barring unforeseen geopolitical shocks, the company expects input cost inflation to ease going forward and to take 6-9 months to settle.
- The company has taken a weightage average price hike of 14-18% in the last 12 months, and its Fevicol product continues to be priced at the higher end. Prices will not be raised further if cost inflation continues to let up.
- In Q1FY23, imputed subsidiary revenue/EBITDA/adj. PAT came in higher YoY at Rs 3.1bn/Rs 423mn/Rs 207mn (vs. Rs 2.2bn/Rs 235mn/Rs 79mn in Q1FY22).
- Domestic subsidiaries registered good sales growth. EBITDA margins of B2B subsidiaries remained under pressure due to higher input costs. International subsidiaries maintained their positive momentum and reported high double-digit constant currency revenue growth led by judicious pricing action.
- Tiling adhesive is a fast-growing market – PIDI estimates this market grew at 15-20% in the last 12 months and indicated that the company is growing at a much higher rate.
- In Q1, urban markets contributed two-thirds of revenue and rural markets the balance. PIDI continues to focus on rural/smaller town markets for deeper product penetration. The company currently has 7,500 'Pidilite Ki Duniya' stores in smaller towns and has added 17,000 villages (population of 5,000-7,000 each) to its direct connect network.

Fig 1 – Consolidated quarterly performance

(Rs mn)	Q1FY23	Q1FY22	YoY (%)	Q4FY22	QoQ (%)	FY22	FY21	YoY (%)
Net revenues	31,011	19,368	60.1	25,071	23.7	99,210	72,927	36.0
Raw Material Cost	18,080	9,857	83.4	14,163	27.7	54,442	33,767	61.2
Employee cost	3,157	2,806	12.5	2,786	13.3	11,124	9,809	13.4
Other expenses	4,479	3,229	38.7	4,111	8.9	15,171	12,546	20.9
EBITDA	5,295	3,476	52.3	4,011	32.0	18,473	16,806	9.9
EBITDA margin (%)	17.1	17.9	(87bps)	16.0	108bps	18.6	23.0	(443bps)
Depreciation and amortization	613	566	8.3	622	(1.4)	2,396	2,007	19.4
EBIT	4,682	2,910	60.9	3,389	38.1	16,077	14,800	8.6
EBIT Margin (%)	15.1	15.0	7bps	13.5	158bps	16.2	20.3	(409bps)
Net Interest expenses	90	96	(6.1)	94	(3.4)	421	372	13.0
Foreign exchange gain (loss), net	0	0	n.m.	0	n.m.	0	0	n.m.
Other income	107	61	74.5	111	(3.9)	363	794	(54.3)
EBT and except. Items	4,698	2,875	63.4	3,407	37.9	16,019	15,221	5.2
Exceptional items	0	0	n.m.	0	n.m.	0	(36)	n.m.
Earnings before tax	4,698	2,875	63.4	3,407	37.9	16,019	15,185	5.5
Income taxes	1,157	721	60.5	915	26.4	4,070	3,964	2.7
Income tax as % of PBT	24.6	25.1	(45bps)	26.9	(224bps)	25.4	26.1	(69bps)
Earnings after tax	3,541	2,154	64.4	2,491	42.1	11,949	11,222	6.5
Profit in associate company	34	23	50.0	52	(34.5)	119	40	198.5
Minority interest (expense) income	(39)	24	n.m.	0	n.m.	0	51	(100.0)
Net income (loss), reported	3,536	2,201	60.7	2,544	39.0	12,068	11,348	6.3

Source: Company, BOBCAPS Research

Fig 2 – Consolidated segmental performance

(Rs mn)	Q1FY23	Q1FY22	YoY (%)	Q4FY22	QoQ (%)	FY22	FY21	YoY (%)
Revenue								
Consumer & Bazaar Products	24,358	14,862	63.9	19,132	27.3	77,944	58,089	34.2
Business to Business	7,220	4,820	49.8	6,453	11.9	22,783	15,754	44.6
Others	258	99	160.7	188	37.3	637	385	65.3
Total	31,836	19,782	60.9	25,773	23.5	1,01,364	74,228	36.6
Less: Inter Segment revenue	(825)	(414)	99.4	(702)	17.5	(2,155)	(1,301)	65.6
Net revenues	31,011	19,368	60.1	25,071	23.7	99,210	72,927	36.0
EBIT								
Consumer & Bazaar Products	5,352	3,704	44.5	4,177	28.1	19,337	17,736	9.0
Business to Business	748	420	78.1	444	68.5	1,527	1,181	29.3
Others	14	6	n.m.	(8)	(273.2)	(22)	(18)	17.4
Total	6,114	4,131	48.0	4,613	32.5	20,842	18,899	10.3
EBIT Margin (%)								
Consumer & Bazaar Products	22.0	24.9	(295bps)	21.8	14bps	24.8	30.5	(572bps)
Business to Business	10.4	8.7	165bps	6.9	348bps	6.7	7.5	(80bps)
Total	19.7	21.3	(161bps)	18.4	132bps	21.0	25.9	(491bps)

Source: Company, BOBCAPS Research

Fig 3 – Standalone quarterly performance

(Rs mn)	Q1FY23	Q1FY22	YoY (%)	Q4FY22	QoQ (%)	FY22	FY21	YoY (%)
Net revenues	27,897	17,194	62.3	22,298	25.1	88,956	62,163	43.1
Raw material exp	16,510	8,800	87.6	12,735	29.6	49,055	28,338	73.1
Employee exp	2,652	2,345	13.1	2,313	14.7	9,268	7,878	17.6
Other exp	3,864	2,808	37.6	3,368	14.7	12,910	10,472	23.3
EBITDA	4,872	3,241	50.3	3,882	25.5	17,724	15,477	14.5
EBITDA margin (%)	17.5	18.8	(138bps)	17.4	5bps	19.9	24.9	(497bps)
Depreciation and amortization	504	453	11.4	509	(0.8)	1,944	1,471	32.1
EBIT	4,368	2,788	56.7	3,374	29.5	15,780	14,006	12.7
EBIT Margin (%)	15.7	16.2	(56bps)	15.1	53bps	17.7	22.5	(479bps)
Net Interest expenses	44	63	(29.8)	53	(15.9)	272	170	60.3
Other income	107	65	65.8	98	8.8	400	735	(45.6)
PBT	4,431	2,790	58.8	3,419	29.6	15,907	14,571	9.2
Income taxes	1,097	715	53.5	899	22.1	3,993	3,752	6.4
Income tax as % of PBT	24.8	25.6	(86bps)	26.3	(153bps)	25.1	25.7	(64bps)
Earnings after tax, adjusted	3,334	2,075	60.7	2,520	32.3	11,914	10,819	10.1
Extraordinary	0	0	n.m.	0		0	(5)	(100.0)
Net income (loss), reported	3,334	2,075	60.7	2,520	32.3	11,914	10,815	10.2

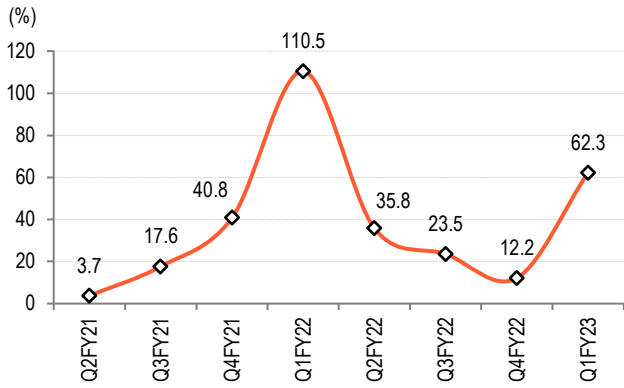
Source: Company, BOBCAPS Research

Fig 4 – Standalone segmental performance

(Rs mn)	Q1FY23	Q1FY22	YoY (%)	Q4FY22	QoQ (%)	FY22	FY21	YoY (%)
Revenue								
Consumer & Bazaar Products	21,983	13,213	66.4	15,992	37.5	70,180	49,982	40.4
Business to Business	6,329	4,204	50.6	5,234	20.9	19,873	12,827	54.9
Others	258	99	160.7	188	37.3	637	385	65.3
Total	28,570	17,516	63.1	21,414	33.4	90,690	63,194	43.5
Less: Inter Segment revenue	(672)	(322)	108.7	(570)	17.9	(1,734)	(1,031)	68.2
Net revenues	27,897	17,194	62.3	20,844	33.8	88,956	62,163	43.1
EBIT								
Consumer & Bazaar Products	5,104	3,489	46.3	3,735	36.6	18,748	16,586	13.0
Business to Business	749	551	35.9	467	60.4	1,950	1,676	16.4
Others	14	(11)	n.m.	(8)	(275.3)	(22)	(18)	17.4
Total	5,867	4,030	45.6	4,194	39.9	20,676	18,244	13.3
EBIT Margin (%)								
Consumer & Bazaar Products	23.2	26.4	(319bps)	23.4	(14bps)	26.7	33.2	(647bps)
Business to Business	11.8	13.1	(127bps)	8.9	291bps	9.8	13.1	(325bps)
Others	5.5	(10.9)	1643bps	(4.3)	982bps	(3.4)	(4.8)	138bps
Total	21.0	23.4	(241bps)	20.1	91bps	23.2	29.3	(610bps)

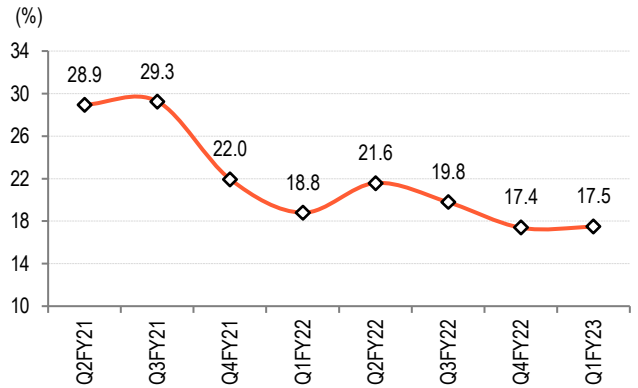
Source: Company, BOBCAPS Research

Fig 5 – Standalone revenue growth



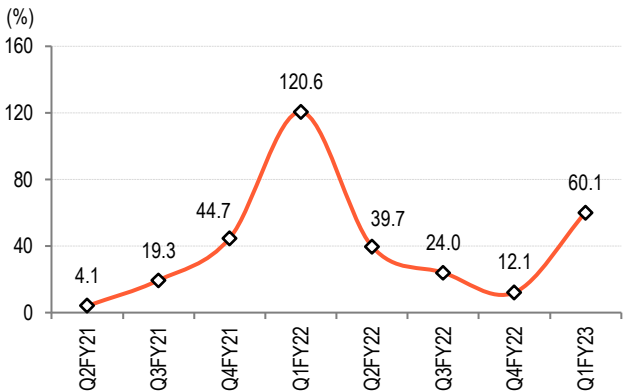
Source: Company, BOBCAPS Research

Fig 6 – Standalone EBITDA margin



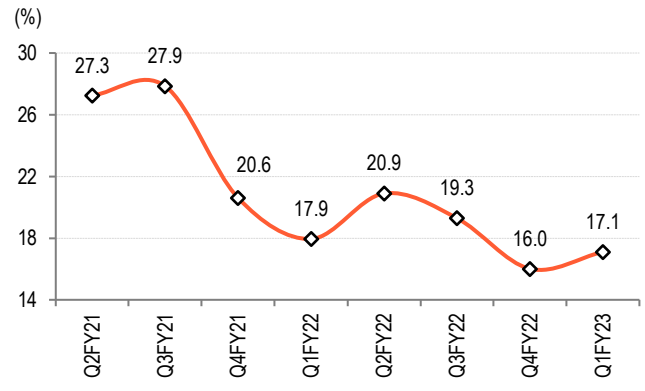
Source: Company, BOBCAPS Research

Fig 7 – Consolidated revenue growth



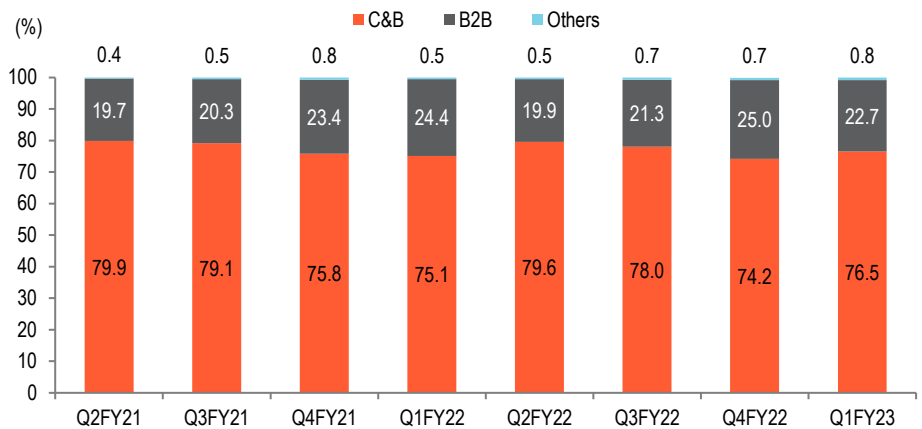
Source: Company, BOBCAPS Research

Fig 8 – Consolidated EBITDA margin



Source: Company, BOBCAPS Research

Fig 9 – Consolidated revenue break-up



Source: Company, BOBCAPS Research

Valuation methodology

Management is targeting growth at 1-2x GDP for the 'core' segment (adhesives and sealants) and 2-4x for the 'growth' segment over the long term, and expects the addition of premium products (Araldite) and cost optimisation measures to aid margins. On the margin front, we believe smoothening of raw material supply and judicious price hike will lead to normalised gross margin from H2FY23E onwards. Nevertheless, while the structural investment case remains intact, valuations are expensive; in our view.

PIDI has posted a 3Y revenue CAGR of 15% during Q1 vs. 19% for closest peer APNT. In addition, consensus estimates peg APNT's revenue CAGR over FY22-FY24 at 17% vs. our 10% forecast for PIDI, implying that the latter's valuation premium (~10% historically) to APNT will shrink.

At current valuations of 104x/88x FY23E/FY24E EPS, the stock is well above its 5Y median P/E of 67x. In our view, valuations do not adequately price in the risks to growth and margins. We maintain SELL with an unchanged TP of Rs 1,870, valuing the stock at 62x FY24E EPS.

Key risks

Key upside risks to our estimates are:

- **Sharp decline in raw material prices:** Any sudden, steep fall in RM prices, especially for crude-linked products, could drive above-expected margins.
- **Above-expected pickup in housing activity:** A stronger revival in the housing market than anticipated can take growth ahead of estimates.

Sector recommendation snapshot

Company	Ticker	Market Cap (US\$ bn)	Price (Rs)	Target (Rs)	Rating
Century Plyboards	CPBI IN	1.7	612	735	BUY
Cera Sanitaryware	CRS IN	0.8	4,894	5,225	HOLD
Greenpanel Industries	GREENP IN	0.7	435	595	BUY
Greenply Industries	MTLM IN	0.3	183	235	BUY
Kajaria Ceramics	KJC IN	2.2	1,125	1,460	BUY
Pidilite Industries	PIDI IN	16.9	2,641	1,870	SELL
Somany Ceramics	SOMC IN	0.3	655	835	BUY

Source: BOBCAPS Research, NSE | Price as of 11 Aug 2022

Financials

Income Statement

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22A	FY23E	FY24E
Total revenue	72,945	72,927	99,210	1,03,920	1,19,726
EBITDA	15,760	16,806	18,473	19,745	23,347
Depreciation	(1,699)	(2,007)	(2,396)	(2,598)	(2,993)
EBIT	14,061	14,800	16,077	17,147	20,353
Net interest inc./(exp.)	(336)	(372)	(421)	(130)	(60)
Other inc./(exp.)	396	794	363	361	282
Exceptional items	0	0	0	0	0
EBT	15,219	15,221	16,019	17,378	20,576
Income taxes	(3,477)	(3,964)	(4,165)	(4,518)	(5,350)
Extraordinary items	(552)	(36)	0	0	0
Min. int./Inc. from assoc.	(26)	91	111	72	81
Reported net profit	11,164	11,312	11,965	12,932	15,307
Adjustments	426	27	0	0	0
Adjusted net profit	11,590	11,339	11,965	12,932	15,307

Balance Sheet

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22A	FY23E	FY24E
Accounts payables	6,210	10,067	9,598	10,301	11,868
Other current liabilities	9,185	12,958	11,779	11,279	10,779
Provisions	735	829	895	1,045	1,195
Debt funds	1,691	2,139	2,873	850	850
Other liabilities	823	3,980	3,985	3,985	3,985
Equity capital	508	508	508	508	508
Reserves & surplus	44,048	55,421	63,529	68,808	75,056
Shareholders' fund	44,556	55,930	64,037	69,316	75,564
Total liab. and equities	65,357	88,304	95,156	98,829	1,06,370
Cash and cash eq.	7,033	4,515	3,552	4,694	6,009
Accounts receivables	10,885	13,210	14,305	14,236	16,401
Inventories	9,295	12,342	16,951	17,681	20,370
Other current assets	10,157	9,190	6,263	9,065	9,682
Investments	7,197	1,765	4,586	4,723	4,880
Net fixed assets	12,890	14,428	41,170	40,101	40,700
CWIP	2,593	2,939	2,939	2,939	2,939
Intangible assets	5,178	29,751	5,178	5,178	5,178
Deferred tax assets, net	130	166	213	213	213
Other assets	0	0	0	0	0
Total assets	65,357	88,304	95,156	98,829	1,06,370

Cash Flows

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22A	FY23E	FY24E
Cash flow from operations	13,474	14,866	10,472	12,615	14,182
Capital expenditures	(4,687)	(24,088)	(2,976)	(3,118)	(3,592)
Change in investments	4,317	5,433	(2,822)	(137)	(157)
Other investing cash flows	33	1,203	0	0	0
Cash flow from investing	(337)	(17,452)	(5,798)	(3,254)	(3,749)
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	581	448	734	(2,023)	0
Interest expenses	(336)	(372)	(421)	(130)	(60)
Dividends paid	(8,254)	(7)	(5,951)	(6,064)	(9,058)
Other financing cash flows	0	0	0	0	0
Cash flow from financing	(8,009)	69	(5,637)	(8,218)	(9,118)
Chg in cash & cash eq.	5,128	(2,517)	(963)	1,142	1,315
Closing cash & cash eq.	7,032	4,515	3,552	4,694	6,009

Per Share

Y/E 31 Mar (Rs)	FY20A	FY21A	FY22A	FY23E	FY24E
Reported EPS	22.0	22.3	23.5	25.4	30.1
Adjusted EPS	22.8	22.3	23.5	25.4	30.1
Dividend per share	13.5	8.5	11.1	12.0	14.2
Book value per share	87.7	110.1	126.0	136.4	148.7

Valuations Ratios

Y/E 31 Mar (x)	FY20A	FY21A	FY22A	FY23E	FY24E
EV/Sales	18.4	18.4	13.5	12.9	11.2
EV/EBITDA	85.1	79.7	72.4	67.9	57.4
Adjusted P/E	115.8	118.3	112.1	103.8	87.7
P/BV	30.1	24.0	21.0	19.4	17.8

DuPont Analysis

Y/E 31 Mar (%)	FY20A	FY21A	FY22A	FY23E	FY24E
Tax burden (Net profit/PBT)	76.2	74.5	74.7	74.4	74.4
Interest burden (PBT/EBIT)	108.2	102.8	99.6	101.3	101.1
EBIT margin (EBIT/Revenue)	19.3	20.3	16.2	16.5	17.0
Asset turnover (Rev./Avg TA)	117.2	94.9	108.2	107.1	116.7
Leverage (Avg TA/Avg Equity)	1.4	1.5	1.5	1.5	1.4
Adjusted ROAE	26.9	22.6	19.9	19.4	21.1

Ratio Analysis

Y/E 31 Mar	FY20A	FY21A	FY22A	FY23E	FY24E
YoY growth (%)					
Revenue	3.0	0.0	36.0	4.7	15.2
EBITDA	15.2	6.6	9.9	6.9	18.2
Adjusted EPS	30.2	(2.2)	5.5	8.1	18.4
Profitability & Return ratios (%)					
EBITDA margin	21.6	23.0	18.6	19.0	19.5
EBIT margin	19.3	20.3	16.2	16.5	17.0
Adjusted profit margin	15.9	15.5	12.1	12.4	12.8
Adjusted ROAE	26.9	22.6	19.9	19.4	21.1
ROCE	23.3	20.1	18.4	18.0	20.0
Working capital days (days)					
Receivables	54	60	51	50	47
Inventory	100	117	98	113	107
Payables	38	53	44	43	42
Ratios (x)					
Gross asset turnover	2.9	2.5	2.2	1.7	1.9
Current ratio	2.1	1.5	1.8	2.0	2.2
Net interest coverage ratio	41.8	39.8	38.2	131.6	342.1
Adjusted debt/equity	(0.1)	0.0	0.0	(0.1)	(0.1)

Source: Company, BOBCAPS Research | Note: TA = Total Assets

Disclaimer

Recommendation scale: Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

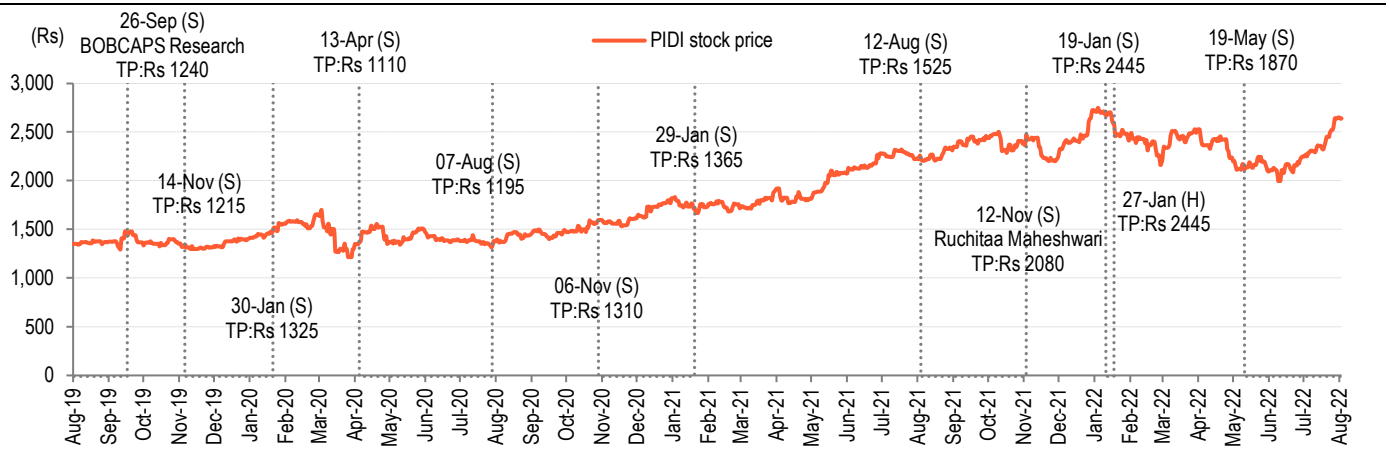
HOLD – Expected return from -6% to +15%

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

Our recommendation scale does not factor in short-term stock price volatility related to market fluctuations. Thus, our recommendations may not always be strictly in line with the recommendation scale as shown above.

Ratings and Target Price (3-year history): PIDILITE INDUSTRIES (PIDI IN)



B – Buy, H – Hold, S – Sell, A – Add, R – Reduce

Rating distribution

As of 31 July 2022, out of 119 rated stocks in the BOB Capital Markets Limited (BOBCAPS) coverage universe, 71 have BUY ratings, 26 have HOLD ratings, 5 are rated ADD*, 1 is rated REDUCE* and 16 are rated SELL. Of these, 2 companies rated BUY and 1 rated ADD have been investment banking clients in the last 12 months. (*Our ADD and REDUCE ratings are in the process of being migrated to the new recommendation structure.)

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