Deepak Nitrite Ltd. (DNL)	
No. of shares (m)	130.7
Mkt cap (Rs crs/$m)	2797/428.5
Current price (Rs/$)	214/3.3
Price target (Rs/$)	251/3.8
52 W H/L (Rs.)	234/76
Book Value (Rs/$)	56/0.9
Beta	1.5
Daily volume NSE (avg. monthly)	491100
P/BV (FY18e/19e)	3.6/3.0
EV/EBITDA (FY18e/19e)	16.6/7.8
P/E (FY18e/19e)	32.9/20.5
EPS growth (FY17/18e/19e)	-36.1/71.1/60.8
OPM (FY17/18e/19e)	10.5/13.4/15.2
ROE (FY17/18e/19e)	7.6/11.616.1
ROCE(FY17/18e/19e)	6.1/6.3/10.4
D/E ratio (FY17/18e/19e)	1.1/1.9/1.4
BSE Code	506401
NSE Code	DEEPAKNTR
Bloomberg	DN IN
Reuters	DPNT.BO

Shareholding pattern	%
Promoters	46.5
MFs / Banks / FIs	11.7
Foreign Portfolio Investors	14.1
Govt. Holding	0.0
Public & others	27.7
Total	**100.0**

As on June 30, 2017

Recommendation

ACCUMULATE

Analyst

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Company brief

Sorted into basic chemicals, fine & speciality chemicals (FSC) and performance products, DNL's product portfolio comprises organic, inorganic and fine chemicals - for use in detergents, colorants, paper, agro chemicals, rubber etc.

Highlights

- Vitality in DNL's basic chemicals business (gross revenues up 12.6%; EBIT up 38.3%) and recognition of insurance claim of Rs 18.33 crs ($2.8m) on account of loss of profits due to business interruption from the fire at its Roha facility last fiscal, failed to buttress revenues (net revenues up a measly 6.1%) last quarter. Delays in getting clearance from local authorities for select high value products in the FSC segment coupled with short supply of some products precluded production of some high margin products. As a result, FSC's gross revenues (excluding insurance claim sum) nosedived 12.9% and EBIT by a worrying 52%.
- Exports tumbled (-24.8%) too mainly due to part functioning of fire-ridden Roha facility last quarter. Domestic revenues however rose by a pleasing 17%. Post commissioning of Telangana State Pollution Control Board order afflicted Hyderabad plant, volumes of its performance products business rose 4% but with a wider loss. DNL's most sturdy basic chemicals business too reversed course from the fuel additives lackluster demand induced last fiscal to post 5% volume growth and 230 bps expansion in EBIT margins.
- Going ahead, DNL's FSC segment is expected to recognize some more earnings (~ Rs 6 crs/$0.9m) arising from insurance claims for the Roha facility. By latest update, Deepak Phenolics phenol and acetone project was rapidly heading towards mechanical completion to finally commission the project by fourth quarter of current fiscal. It seed marketing initiatives are not aimed at selling high quantities of the new products but at understanding demand patterns and building customer relationships.
- The stock currently trades at 32.9x FY18e EPS of Rs 6.50 and 20.5x FY19e EPS of Rs 10.45. Recovery in earnings this fiscal partly rests on sustained firmness in crude oil markets and resurrection in exports of key FSC intermediates. Widening on newer regions (Europe for instance) and end-user industries with patented products for performance products segment is aimed at curtailing losses. Yet vulnerability of earnings to near unpredictability of market reach with regards to phenol and acetone capacities cannot be sorely gainsaid. We therefore assign accumulate rating on the stock with revised target of Rs 251 (previous target: Rs 144) based on 24xFY19 earnings, over a period of 6-9 months.

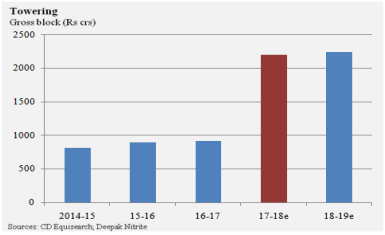
Consolidated (Rs crs)	FY15	FY16	FY17	FY18e	FY19e
Income from operations	1327.16	1372.93	1360.44	1503.82	2856.42
Other Income	2.07	1.59	75.38*	3.89	1.75
EBITDA (other income included)	141.31	168.39	216.04	205.69	435.28
Profit after associate profit (adjusted for EO)	52.98	63.88	44.60	84.91	138.12
EPS**(Rs)	5.07	5.94	3.80	6.50	10.45
EPS growth (%)	-	17.3	-36.1	71.1	60.8

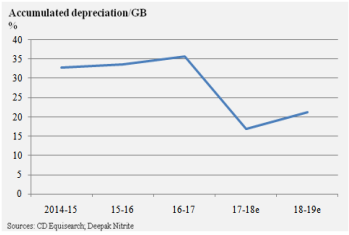
*includes Rs 70.48 crs profit on sale of land and surrender of leasehold rights; ** calculated on weighted average equity.

Outlook & Recommendation

Phenol project

To quicken commissioning of its all engrossing phenol & acetone project by fourth quarter of current fiscal, Deepk Phenolics (DPL), wholly owned subsidiary of Deepak Nitrite, is pulling out all stops to recruit commissioning and operational teams to speedup seed marketing initiatives to finalize construction work. By last count, DPL invested nearly Rs 800 crs and committed over Rs 950 crs in this mammoth project - a significant ramp from some Rs 475 crs invested till April. By Q1, Deepak Nitrite has infused a significant portion (Rs 300 crs) of the total equity component (Rs 480 crs) of the core project cost of Rs 1200 crs (save interest capitalization and working capital requirements), while large debt raising is scheduled in the current fiscal. Local availability of key raw materials like benzene and propylene would not be without distinct cost advantage but would also facilitate roll out of phenol derivatives and downstream intermediates in future. Further equity raising (Rs 150 crs concluded in March) for funding the non-core sum would be procrastinated to next fiscal.

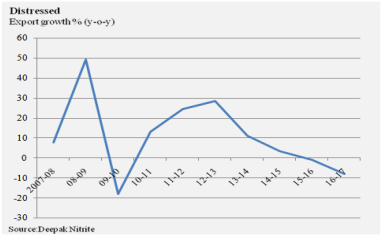


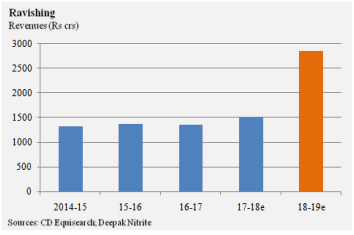


Financials & Valuations

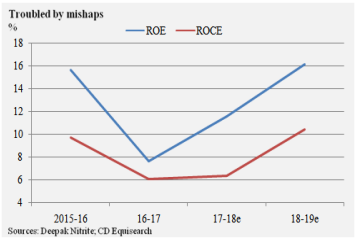
According to the latest report by Hexa Research, a market research & consulting organization, the global phenol market is expected to reach $31.7bn by 2025, accentuated by rising demand for derivatives like epoxy resins, polycarbonates, nylon, phenolic resins, detergents and pharmaceuticals. Asia Pacific is expected to maintain its pole position in global market share with China and India driving the regional market owing to increased demand for phenol based derivatives that have large industrial applications. Other reports contend that the global resins market would grow at a CAGR of 6.7% during 2016-2022 to reach $16.1bn during the end of the projected period. Setting up of more construction and furniture industry, the report posits, would make China and India the key consuming nations - Asia Pacific region accounts for 64% of global phenolic resin consumption.

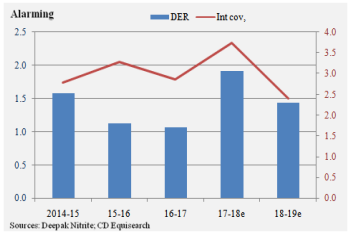
According to MarketsandMarkets, a B2B research provider, rapid expansions by phenol producers in major Asian economies like China, India, Japan, South Korea, and Taiwan is driving demand for phenol. By setting up gargantuan capacities of both phenol & acetone, Deepak Nitrite targets to tap a largely import demand for these chemicals. Sub-optimal capacity utilization (~50% for both phenol and acetone) of Indian suppliers has had cost escalation ramifications, enticing imports. Its seed marketing initiatives are intended to gain palatable market presence in the first year of operations of the project.

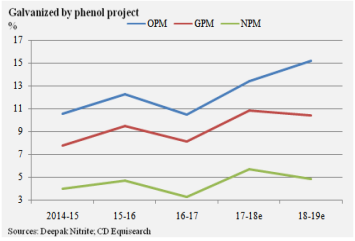




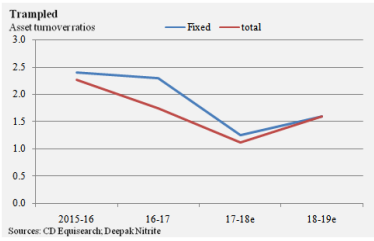
Yet mere erection of capacities does not assure market control. DNL's internal target of achieving 75% capacity utilization in phenol and acetone project next fiscal is not devoid of slippages not least due to the fledgling enterprise. Post full commissioning, earnings would rise by over 60% with bulk of profits emerging from these nestling products. Imposition of anti-dumping duty on imports of sodium nitrite from China would further invigorate its basic chemicals business. Exports of FSC intermediates would resurrect with full scale operations of the Roha facility, though not withstanding degradation of competitive advantage emanating from the appreciation of the Indian currency.

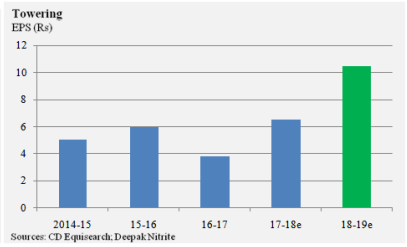






The stock currently trades at 32.9x FY18e EPS of Rs 6.50 and 20.5x FY19e EPS of Rs 10.45. Earnings revival this fiscal would stem from vigorous rebound in dispatches of key product categories - basic chemicals; pharmaceutical and personal care intermediates and recognition of insurance claims from Roha facility. Huge debt amassment (debt -equity ratio 1.4 for FY19) for funding phenol and acetone project would grant little forbearance to production slippages of phenol and acetone. Volatile crude oil markets would pose grave challenges to re-pricing of bulk chemicals. On balance, we maintain our "accumulate" rating on the stock with revised target of Rs 251 (previous target: Rs 144) based on 24x FY19e earnings (three year average TTM P/E: 20 -on year end prices) over a period of 6-9 months. For more info, refer to our March report.





Risks & Concerns

Business risks

DNL's various businesses - agro chemicals; colorants; fuel additives - suffer from uncertainties of different kinds - agro chemicals from vagaries of monsoons; colorants from fragility of demand from end user industries; fuel additives from vicious regulatory issues concerning fuel pricing. Weak environmental control activities and intense competitive intensity - more evident in bulk chemicals intermediates - pose noteworthy risks.

Currency risks

Given its net long dollar position arising out of exports, appreciation of rupee impacts its competitiveness, particularly against Chinese firms.

Cross Sectional Analysis

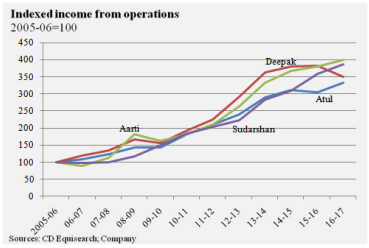
Company	Equity*	CMP (Rs crs)	Mcap*	Inc. from ops. (Rs crs)	Profit*	OPM (%)	NPM (%)	Int. coverage	ROE (%)	Mcap / IO	P/BV	P/E
Aarti Inds.	41	917	7529	3107	287	19.1	9.2	4.0	22.6	2.4	5.5	26.2
Atul Ltd	30	2326	6898	2710	237	15.8	8.7	22.6	13.3	2.5	3.6	29.2
Deepak Nitrite	26	214	2797	1241	62	12.8	5.0	3.6	9.6	2.3	3.8	41.6
Sudarshan Chem	14	378	2619	1272	82	12.8	6.5	5.6	21.5	2.1	6.4	31.8

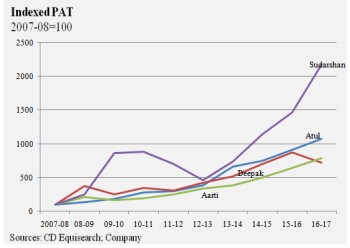
*figures in crores; calculations on ttm basis; all standalone data
Companies not truly comparable due to product dissimilarity

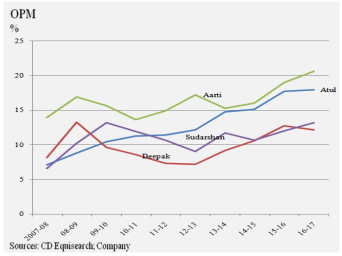
Stung by GST implementation, Sudarshan Chemicals revenues nearly flat lined last quarter with revenues of its flag bearer pigments business rose by 8.1% while that of agro chemicals dived by over a third. Rupee appreciation against both euro and USD impact margins - OPMs slid 364 bps y-o-y. To augment its global position in the pigments market, subsidiaries in Mexico and China have been set up. Risks of mass scale dumping by China loom large over the Indian pigment industry largely due to excess capacities existing in China. Also Sudarshan continues to face challenges in procuring key intermediates from China.

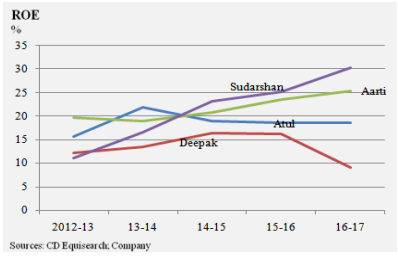
Beset by an annual maintenance shutdown of its acid division in Q1, Aarti's illustrious speciality chemicals volumes grew by a puny 2%. (10% growth in Q4; 8% in FY17) As a result, its EBIT margins plunged nearly 450 bps (y-o-y). To boost its pipeline of value added products, it has set aside annual capex of Rs 400-450 crs ($61.3m-68.9m) over the next three years. Recently it announced signing of multi-year agrochemical intermediary supply deal with a global agriculture company. Supplies of the product - to be used in herbicides - which is expected to commence from FY20, would generate revenues of nearly Rs 4000 crs ($612.8m). Aarti Industries would incur a capex of Rs 400 crs ($61.3m) to fund supplies for this contract.

Imperiled by Chinese competition, Atul's performance and other chemicals revenues declined 9.8% and EBIT by over 50%, resulting in 57.3% drop in post tax earnings. . In its bulk chemicals business, plans are afoot to boost capacity utilization of its new caustic chlorine plant - subject to external demand - and launch chlorine derivative products. Sensing increased demand for its polymers, higher capacities are planned for specialty resins, suplhone intermediates and other upstream/downstream products. For aromatics, building capacities for fragrance intermediate and downstream and launching new products from its newly established kilo lab facility are also on the anvil. Notwithstanding nearly unsurpassable business opportunity in global specialty chemicals industry, risks in form of crude oil price volatility, Chinese competition (mainly for crop protection and aromatics businesses), lengthy qualification process and forex fluctuations cannot be discredited.









All consolidated data except Deepak Nitrite

Financials

Quarterly Results -Standalone

Figures in Rs crs

	Q1FY18	Q1FY17	% chg.	FY17	FY16	% chg.
Income from operations	**337.36**	**317.91**	**6.1**	**1221.56**	**1335.73**	**-8.5**
Other Income	1.97	73.23	-97.3	78.91	1.54	5013.0
Total Income	**339.34**	**391.14**	**-13.2**	**1300.47**	**1337.27**	**-2.8**
Total Expenditure	286.83	277.98	3.2	1075.00	1167.39	-7.9
PBIDT (other income included)	**52.50**	**113.16**	**-53.6**	**225.47**	**169.87**	**32.7**
Interest	9.46	8.37	12.9	32.31	39.10	-17.4
Depreciation	12.34	12.29	0.4	42.28	39.45	7.2
PBT	**30.71**	**92.49**	**-66.8**	**150.87**	**91.33**	**65.2**
Tax	10.60	25.10	-57.8	38.83	26.18	48.4
PAT	**20.10**	**67.38**	**-70.2**	**112.04**	**65.15**	**72.0**
Extraordinary Item	0.00	54.50	-100.0	57.67	-1.16	-5061.8
Adjusted Net Profit	**20.10**	**12.88**	**56.1**	**54.37**	**66.31**	**-18.0**
EPS (F.V. 2)*	1.54	1.11	38.9	4.63	6.17	-25.0
Equity	26.14	23.26	12.4	26.14	23.26	12.4

*quarterly EPS on quarter end equity; yearly EPS on weighted average equity

Segment Results

Figures in Rs crs

	Q1FY18	Q1FY17	% chg.	FY17	FY16	% chg.
Segment Revenue						
Basic Chemicals	193.95	172.31	12.6	634.57	674.56	-5.9
Fine & Speciality Chemicals	106.81	101.56	5.2	359.36	393.37	-8.6
Performance Products	65.78	67.37	-2.4	240.09	273.68	-12.3
Others - unallocable	0.15	1.70	-91.0	4.89	5.78	-15.5
Total	**366.69**	**342.94**	**6.9**	**1238.91**	**1347.39**	**-8.1**
Inter segment revenue	5.07	3.55	42.7	17.35	11.67	48.7
Income from operations**	**361.63**	**339.39**	**6.6**	**1221.56**	**1335.73**	**-8.5**
Segment EBIT						
Basic Chemicals	23.61	17.07	38.3	90.93	79.59	14.2
Fine & Speciality Chemicals	31.43	27.29	15.2	85.09	97.19	-12.4
Performance Products	-4.01	-2.81	42.8	-14.19	-8.71	63.0
Total	**51.03**	**41.56**	**22.8**	**161.83**	**168.07**	**-3.7**
Interest	9.46	8.37	12.9	30.89	37.45	-17.5
Other Unallocable Exp. (net of income)	10.87	-59.30	-118.3	-19.93	39.30	-150.7
PBT	**30.71**	**92.49**	**-66.8**	**150.87**	**91.33**	**65.2**

** gross for quarterly data; net for yearly

Financials

Income Statement - Consolidated

Figures in Rs crs

	FY15	FY16	FY17	FY18e	FY19e
Income from operations	**1327.16**	**1372.93**	**1360.44**	**1503.82**	**2856.42**
Growth (%)		3.4	-0.9	10.5	89.9
Other Income	2.07	1.59	75.38	3.89	1.75
Total Income	**1329.23**	**1374.52**	**1435.83**	**1507.71**	**2858.17**
Total Expenditure	1187.92	1206.13	1219.79	1302.02	2422.89
EBITDA (other income included)	**141.31**	**168.39**	**216.04**	**205.69**	**435.28**
Interest	37.99	39.71	36.54	43.35	138.21
EBDT	**103.31**	**128.67**	**179.50**	**162.34**	**297.07**
Depreciation	36.02	39.54	42.72	43.38	103.68
Tax	14.30	26.23	38.84	33.90	55.11
Net profit	**52.99**	**62.90**	**97.94**	**85.06**	**138.27**
Profit of associate	-0.09	-0.17	-0.15	-0.15	-0.15
Net profit after associate profit	**52.90**	**62.73**	**97.79**	**84.91**	**138.12**
Extraordinary item	-0.08	-1.15	53.19	0.00	0.00
Adjusted Net Profit	**52.98**	**63.88**	**44.60**	**84.91**	**138.12**
EPS (Rs.)	5.07	5.94	3.80	6.50	10.45

Segment Results

Figures in Rs crs

	FY15	FY16	FY17	FY18e	FY19e
Segment Revenue					
Basic Chemicals	749.59	674.56	634.57	712.41	792.55
Fine & Speciality Chemicals	326.20	393.37	359.36	410.19	445.49
Performance Products	266.18	273.68	242.96	255.11	280.62
Others - unallocable	5.42	42.99	140.90	145.20	1358.76
Total	**1347.39**	**1384.60**	**1377.79**	**1522.90**	**2877.42**
Inter segment revenue	20.23	11.67	17.35	19.09	20.99
Income from operations	**1327.16**	**1372.93**	**1360.44**	**1503.82**	**2856.42**
Segment EBIT					
Basic Chemicals	73.54	79.59	91.00	106.86	118.88
Fine & Speciality Chemicals	61.88	97.19	85.09	109.30	111.37
Performance Products	0.66	-8.71	-18.75	-14.00	-2.81
Unallocable					169.85
Sub Total	**136.08**	**168.07**	**157.34**	**202.16**	**397.29**
Interest	36.41	37.65	34.12	41.10	132.50
Other Unallocable Exp. (net of income)	32.38	41.29	-13.56	42.11	71.41
PBT	**67.29**	**89.13**	**136.78**	**118.96**	**193.38**

Consolidated Balance Sheet

Figures in Rs crs

	FY15	FY16	FY17	FY18e	FY19e
SOURCES OF FUNDS					
Share Capital	20.91	23.26	26.14	26.14	26.74
Reserves	325.31	449.61	690.95	761.15	939.79
Total Shareholders Funds	**346.22**	**472.87**	**717.09**	**787.29**	**966.53**
Long term debt	238.60	158.93	238.30	995.07	875.07
Total Liabilities	**584.82**	**631.79**	**955.39**	**1782.36**	**1841.60**
APPLICATION OF FUNDS					
Gross Block	817.38	899.03	918.04	2198.31	2238.31
Less: Accumulated Depreciation	268.65	301.31	327.52	370.89	474.58
Net Block	**548.73**	**597.72**	**590.52**	**1827.42**	**1763.74**
Capital Work in Progress	43.96	31.93	349.31	20.00	20.00
Investments	2.98	86.60	116.58	2.52	2.37
Current Assets, Loans & Advances					
Inventory	105.04	121.02	135.82	156.19	234.29
Sundry Debtors	310.99	313.19	360.33	389.16	603.19
Cash and Bank	3.06	6.49	14.49	34.78	13.10
Other Assets	54.14	56.67	67.72	70.69	95.12
Total CA & LA	**473.23**	**497.37**	**578.36**	**650.81**	**945.70**
Current liabilities	469.73	577.73	768.98	703.80	843.04
Provisions	14.32	20.25	4.10	4.65	5.78
Total Current Liabilities	**484.05**	**597.98**	**773.07**	**708.46**	**848.82**
Net Current Assets	-10.82	-100.61	-194.71	-57.64	96.88
Net Deferred Tax (net of liability)	-46.32	-56.65	-65.72	-73.72	-126.92
Other Assets (Net of liabilities)	46.29	72.81	159.40	63.79	85.54
Total Assets	**584.82**	**631.79**	**955.39**	**1782.36**	**1841.60**

Key Financial Ratios

	FY15	FY16	FY17	FY18e	FY19e
Growth Ratios					
Revenue (%)		3.4	-0.9	10.5	89.9
EBIDTA (%)		20.2	-13.5	39.9	111.6
Net Profit (%)		20.6	-30.2	90.4	62.7
EPS (%)		17.3	-36.1	71.1	60.8
Margins					
Operating Profit Margin (%)	10.6	12.3	10.5	13.4	15.2
Gross Profit Margin (%)	7.8	9.5	8.1	10.8	10.4
Net Profit Margin (%)	4.0	4.7	3.3	5.7	4.8
Return					
ROCE (%)		9.7	6.1	6.3	10.4
ROE (%)		15.6	7.6	11.6	16.1
Valuations					
Market Cap / Sales	0.5	0.6	1.3	1.9	1.0
EV/EBIDTA	8.9	7.2	15.9	16.6	7.8
P/E	13.5	11.4	34.6	32.9	20.5
P/BV	2.1	1.7	2.5	3.6	3.0
Other Ratios					
Interest Coverage	2.8	3.3	2.9	3.7	2.4
Debt-Equity Ratio	1.6	1.1	1.1	1.9	1.4
Current Ratio	1.0	1.0	0.9	0.9	1.1
Turnover Ratios					
Fixed Asset Turnover		2.4	2.3	1.2	1.6
Total Asset Turnover		2.3	1.7	1.1	1.6
Debtors Turnover		4.4	4.0	4.0	5.8
Inventory Turnover		10.7	9.5	8.9	12.4
Creditors Turnover		9.9	8.6	8.1	10.8
WC Ratios					
Debtor Days		83.0	90.4	91.0	63.4
Inventory Days		34.3	38.5	40.9	29.4
Creditor Days		36.8	42.4	45.3	33.8
Cash Conversion Cycle		80.5	86.4	86.6	59.0

Cumulative Financial Data

Figures in Rs crs	FY09-11	FY12-14	FY15-17
Income from operations	1796	3079	3884
Operating profit	187	247	459
EBIT	143	188	348
PBT	110	137	238
PAT	74	95	174
Dividends	19	29	48
OPM (%)	10.4	8.0	11.8
NPM (%)	4.1	3.1	4.5
Interest coverage	4.3	3.7	3.2
ROE (%)	12.3	11.7	11.4
ROCE (%)	10.7	7.8	8.1
Debt-equity ratio*	0.2	1.6	0.7
Fixed asset turnover	3.7	3.3	2.5
Debtors turnover	5.4	4.9	4.3
Inventory turnover	8.7	10.0	8.9
Creditors turnover	9.6	9.2	8.3
Debtors days	68.1	74.7	85.7
Inventory days	42.0	36.5	40.8
Creditor days	38.1	39.8	44.0
Cash conversion cycle	71.9	71.5	82.4
Dividend payout ratio (%)	25.2	29.6	20.9

FY09-11 implies three years ending fiscal 11; *as on terminal year; standalone data

Twin effects of a conspicuous turnaround in profitability of fluorescent whitening agent (FWA) business in FY15 - when revenues expanded over 50% due to healthy pick up in volumes of both OBA and DASDA in both domestic and export markets - and remarkable expansion volume expansion (24%) in fine & speciality chemicals (FSC) business in FY16 - fomented by beneficial traction in certain products and contribution from newly introduced pharmaceutical and personal care intermediates - cumulative operating profit grew by a blistering 86% and post tax earnings (adjusted) by 82% in FY15-17 period compared to that in the previous three year period. Vivacity in OBA (revenues up eight fold during FY15-17 period), agro chemical intermediates and inorganic salts (over over 60%) made up for languidness in revenues of certain product categories - nitro aromatic, aromatic amines and color intermediates - during FY15-17 period.

Perceptible drop in prices of crude based raw materials like benzene, toluene and 2 ethyl hexanol helped aid margins (OPMs 11.8% Vs 8% - see table) for raw material costs as a proportion of revenues plunged to 60.6% in FY15-17 period compared to arresting 68% in the previous three year period. Yet return on capital suffered thanks to frequent equity raising to fund the ambitious phenol project and relentless fall in crude oil prices. Cash conversion cycle too lengthened from ~72 days in FY12-14 period to ~82 days (see table). Still a modest capex program kept a tab on debt build up.

Financial Summary – US dollar denominated

million $	FY15	FY16	FY17	FY18e	FY19e
Equity capital	3.3	3.5	4.0	4.0	4.1
Shareholders funds	55.2	71.2	107.6	117.6	144.5
Total debt	87.0	79.7	114.7	225.5	207.9
Net fixed assets (incl CWIP)	94.6	94.8	144.8	282.9	273.2
Investments	0.5	13.1	18.0	0.4	0.4
Net current assets	-1.7	-15.2	-32.9	-11.7	11.4
Total assets	93.3	95.1	144.3	270.1	278.6
Revenues	217.0	209.7	202.8	230.4	437.6
EBITDA	23.1	26.0	21.9	31.5	66.7
EBDT	16.9	19.9	16.5	24.9	45.5
PBT	11.0	13.9	10.1	18.2	29.6
Profit after associate profit	8.7	9.8	6.6	13.0	21.2
EPS($)	0.08	0.09	0.06	0.10	0.16
Book value ($)	0.53	0.61	0.82	0.90	1.08

income statement figures translated at average rates; balance sheet and cash flow at year end rates; projections at current rates (Rs 65.27/$). All dollar denominated figures adjusted for extraordinary items.

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buy: >20%	accumulate: >10% to ≤20%	hold: ≥-10% to ≤10%	reduce: ≥-20% to <-10%	sell: <-20%

Exchange Rates Used- Indicative

Rs/$	FY14	FY15	FY16	FY17
Average	60.5	61.15	65.46	67.09
Year end	60.1	62.59	66.33	64.84

All $ values mentioned in the write-up translated at the average rate of the respective quarter/ year as applicable. Projections converted at current exchange rate. Cumulative dollar figure is the sum of respective yearly dollar value.