

17 May 2021

Vinati Organics

Pre-Covid levels attained, strong revenue visibility; maintaining a Buy

Rating: Buy

Target Price: Rs.2,000

Share Price: Rs.1,734

Following a pickup in butyl phenol utilization and recovery in ATBS demand, Vinati reported a good Q4. Despite its Q4 revenue growth in, full year revenue/EBITDA/PAT fell 7%/14%/19% y/y on less demand for ATBS. We expect revenue/EBITDA/PAT to clock 34%/38%/37% CAGRs over FY21-23, driven by rising demand for its products, greater utilisation of butyl phenol and a pickup in demand for ATBS. Further, the amalgamation with Veeral would add to revenue in coming years. We maintain a Buy rating, with a higher target of Rs.2,000 (earlier 1,475), valuing the stock at 41x FY23e EPS.

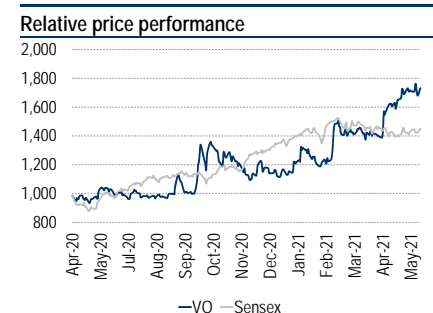
Strong Q4 revenue growth. Revenue grew 14% y/y, 25% q/q, to Rs.2.8bn backed by demand recovery in ATBS and higher utilisation in butyl phenol. The gross margin was 59%, down 47bps y/y, up 424bps q/q following better realizations. Despite the good gross margin, the Q4 EBITDA margin contracted a sharp 601bps y/y, though q/q up 317bps, to 35.4%, due to higher operating expenses. Profit was down 5% y/y to Rs709m, hurt by the lower margin, higher depreciation and lower other income.

Working capital rose to 54%. In FY21, Vinati's working capital as percent of sales rose to 54% (vs.~28% a year ago and averaging ~28% in the last decade) on the increase in long-term loan & advances and higher inventory and receivables. Capex was ~Rs725m. Cash-conversion lengthened to ~158 days (vs. 104 the year prior, and ~102 over the last seven years).

Outlook, valuation. The company guided to ~40-50% revenue growth in FY22 on the pickup in ATBS demand from Jan'21 and the rise in butyl phenol utilisation. We are upbeat about the company's performance and maintain a Buy, with the higher target of Rs2,000, at multiples of 41x FY23e EPS and 30x FY23e EV/EBITDA. **Risks:** Delay in expansion and scaling up from laboratory to commercial scale; slowdown in R&D.

Key data	VO IN/ VNTI .BO
52-week high / low	Rs1818 / 923
Sensex / Nifty	49581 / 14923
3-m average volume	\$3.2m
Market cap	Rs178bn / \$2429.9m
Shares outstanding	103m

Shareholding pattern (%)	Mar'21	Dec'20	Sep'20
Promoters	74.1	74.1	74.1
- of which, Pledged	-	-	-
Free float	25.9	25.9	25.9
- Foreign institutions	3.5	3.7	3.9
- Domestic institutions	7.3	6.7	6.6
- Public	15.2	15.6	15.4



Source: Bloomberg

Key financials (YE Mar)	FY19	FY20	FY21	FY22e	FY23e
Sales (Rs m)	11,279	10,289	9,543	13,225	17,147
Net profit (Rsm)	2,825	3,338	2,694	3,749	5,051
EPS (Rs)	27.5	32.5	26.2	36.5	49.1
P/E (x)	63.1	53.4	66.1	47.5	35.3
EV / EBITDA (x)	41.9	42.4	49.7	34.2	25.8
P/BV (x)	17.0	13.9	11.5	9.7	7.9
RoE (%)	30.6	28.6	19.1	22.1	24.7
RoCE (%)	27.9	26.9	18.1	21.2	23.8
Dividend yield (%)	0.4	0.3	0.3	0.4	0.6
Net debt / equity (x)	(0.1)	(0.2)	(0.2)	(0.2)	(0.2)

Source: Company, Anand Rathi Research

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Quick Glance – Financials and Valuations

Fig 1 – Income statement (Rsm)

Year-end: Mar	FY19	FY20	FY21	FY22e	FY23e
Net revenues (Rs m)	11,279	10,289	9,543	13,225	17,147
Growth (%)	51.7	(8.8)	(7.3)	38.6	29.7
Direct costs	5,251	4,287	3,877	5,621	7,202
SG&A	1,794	1,862	2,140	2,513	3,258
EBITDA	4,234	4,139	3,526	5,092	6,687
<i>EBITDA margins (%)</i>	<i>37.5</i>	<i>40.2</i>	<i>37.0</i>	<i>38.5</i>	<i>39.0</i>
- Depreciation	274	332	429	491	562
Other income	302	450	259	410	621
Interest expenses	9	11	2	12	12
PBT	4,252	4,247	3,353	4,999	6,734
<i>Effective tax rate (%)</i>	<i>33.6</i>	<i>21.4</i>	<i>19.7</i>	<i>25.0</i>	<i>25.0</i>
+ Associates / (Minorities)	0	0	0	0	0
Net income	2,825	3,338	2,694	3,749	5,051
Adjusted income	2,825	3,338	2,694	3,749	5,051
WANS	103	103	103	103	103
FDEPS (Rs / sh)	27.5	32.5	26.2	36.5	49.1
<i>FDEPS growth (%)</i>	<i>96.3</i>	<i>18.2</i>	<i>-19.3</i>	<i>39.1</i>	<i>34.7</i>
<i>Gross margins (%)</i>	<i>53.4</i>	<i>58.3</i>	<i>59.4</i>	<i>57.5</i>	<i>58.0</i>

Fig 3 – Cash-flow statement (Rsm)

Year-end: Mar	FY19	FY20	FY21	FY22e	FY23e
PBT before OI and Interest	3,960	3,808	3,097	4,601	6,125
+ Non-cash items	274	332	429	491	562
Oper. prof. before WC	4,234	4,139	3,526	5,092	6,687
- Incr. / (decr.) in WC	1,096	(862)	2,289	730	1,768
Others incl. taxes	1,390	1,049	585	1,250	1,684
Operating cash-flow	1,748	3,952	652	3,113	3,236
- Capex (tang.+ intang.)	2,013	1,492	727	1,500	1,500
Free cash-flow	(265)	2,460	(75)	1,613	1,736
Acquisitions					
- Div. (incl. buyback & taxes)	866	681	617	750	1,010
+ Equity raised	-	-	-	-	-
+ Debt raised	(115)	(33)	17	-	-
- Fin investments	(353)	1,309	613	1,000	1,500
- Misc. (CFI+CCF) (adj OI & int)	(880)	(63)	(819)	(398)	(609)
Net cash-flow	(14)	499	(469)	261	(165)

Source: Company, AnandRathi Research

Fig 5 – Price movement



Source: Bloomberg

Fig 2 – Balance sheet (Rsm)

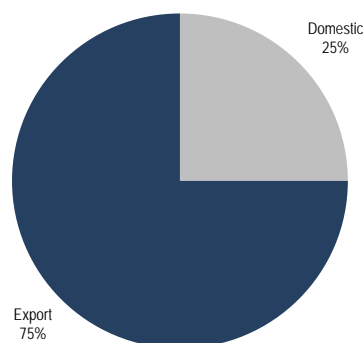
Year-end: Mar	FY19	FY20	FY21	FY22e	FY23e
Share capital	103	103	103	103	103
Net worth	10,513	12,794	15,434	18,433	22,474
Debt	37	3	20	20	20
Minority interest	-	-	-	-	-
DTL / (Assets)	846	705	779	779	779
Capital employed	11,395	13,502	16,234	19,233	23,274
Net tangible assets	4,719	7,491	7,557	8,498	9,450
Net intangible assets	26	17	12	12	12
Goodwill	-	-	-	-	-
CWIP (tang. & intang.)	1,912	310	547	614	600
Investments (strategic)	-	-	-	-	0
Investments (financial)	965	2,274	2,887	3,887	5,387
Current assets (ex cash)	4,616	3,802	6,265	7,247	9,397
Cash	38	537	68	329	164
Current liabilities	880	928	1,102	1,355	1,736
Working capital	3,736	2,874	5,163	5,893	7,661
Capital deployed	11,395	13,502	16,234	19,233	23,274
Contingent liabilities	233	-	-	-	-

Fig 4 – Ratio analysis

Year-end: Mar	FY19	FY20	FY21	FY22e	FY23e
P/E (x)	63.1	53.4	66.1	47.5	35.3
EV / EBITDA (x)	41.9	42.4	49.7	34.2	25.8
EV / Sales (x)	15.7	17.0	18.4	13.2	10.1
P/B (x)	17.0	13.9	11.5	9.7	7.9
RoE (%)	30.6	28.6	19.1	22.1	24.7
RoCE (%) - after tax	27.9	26.9	18.1	21.2	23.8
RoIC	31.5	31.7	21.5	24.7	29.0
DPS (Rs / sh)	7.0	5.5	6.0	7.3	9.8
Dividend yield (%)	0.4	0.3	0.3	0.4	0.6
Dividend payout (%) - incl. DDT	25.5	16.9	22.9	20.0	20.0
Net debt / equity (x)	(0.1)	(0.2)	(0.2)	(0.2)	(0.2)
Receivables (days)	79.0	71.6	106.0	80.3	80.3
Inventory (days)	64.2	79.3	114.8	85.9	86.9
Payables (days)	36.9	47.4	62.5	51.1	51.1
CFO : PAT %	61.9	118.4	24.2	83.0	64.1

Source: Company, AnandRathi Research

Fig 6 – Revenue break-up, FY20



Source: Company

Company Update

Financial highlights

- Vinati's Q4 revenue grew 14% y/y, 25% q/q, to Rs.2.8bn due to higher realisations and demand for ATBS picking up from Dec'20 and returning to pre-Covid levels from Jan'21.
- The gross margin was 59%, down 47bps y/y, up 424bps q/q. Despite maintaining the gross margin level, the EBITDA margin contracted 601bps y/y (though q/q up 317bps), to 35% because of higher operating expenses.
- Other expenses rose 69% y/y, 51% q/q, to Rs488m due to CSR expenses of Rs53m, rise in packaging and logistic costs. Management clarified that logistic costs globally have risen. Employee expenses were down 15bps y/y, 193bps, to 6.3%, against an average ~8.2% in 9MFY21.
- Despite Q4FY21 revenue growth, EBITDA fell 2.5% y/y to Rs.991m on higher operating expenses. On q/q, though, it was up 38%.
- PAT declined 5% y/y (though q/q up 10.5%), to Rs709m, because of the muted operating performance compounded by higher depreciation and lower other income, but partially supported by lower tax expenses.
- The effective Q4 tax rate was 25%, against 31% a year ago, 9% the quarter prior, due to earlier years' income-tax adjustments. Income-tax adjustments for earlier years were of accrued tax benefits based on judicial pronouncements, amounting to Rs173m for FY21.

Update on amalgamation

- To forward integrate, Vinati's Board approved the amalgamation of Veeral Additives Pvt. Ltd. with Vinati Organics. On this acquisition, butyl phenols will be the key raw materials to manufacture antioxidants. Vinati will be the largest and only integrated manufacturer of such antioxidants in India.
- With the acquisition, Vinati will be adding a new revenue stream, specialty chemicals, which have good growth potential domestically and globally. Growth would be driven by greater consumption of various plastics such as LDPE, LLDPE and PP, etc.
- Of the available 40,000 tonnes of butyl phenol capacity, ~45% will be used to manufacture antioxidants. The scheme of amalgamation is subject to approval by the shareholders and the NCLT.

About Veeral Additives

Veeral Additives Pvt. Ltd. manufactures specialty chemicals. It has yet to start production, and this is the first project to manufacture antioxidants.

Fig 7 – Manufacturing capacity (Veeral)

Product	Capacity (tpa)
Anti-oxidants -- AO-1010 and AO-1076	16,000
Anti-oxidants -- AO-168	8,000
Intermediates for anti-oxidants (Metilox)	16,000
By-Products	
Methanol	1,600
32% HCl	6,000

Source: Anand Rathi Research

Key takeaways:Concall highlights

Operating highlights

- FY21 revenue was down y/y due to lower ATBS sales, hit by the global slowdown owing to the pandemic, though offset by increased sales of IBB and other products.
- Receivable days increased in FY21 due to higher sales of IBB and butyl phenol (than of ATBS).
- Inventory days rose due to the build-up of stocks of ~Rs200m, stuck due to the global logistics freeze in Mar '21.
- Loan and advances increased as the company has given a loan to Veeral Additives. The latter had raised debt from HDFC and other banks. The loan would be nullified in the books on completion of the amalgamation.

ATBS

- The company has a ~70% market share in the global ATBS market and expects to maintain or increase it as no additional capacity is coming from existing or new competitors. Of the ATBS it manufactures, ~95% is exported.
- It is seeing a strong upswing in ATBS demand due to recovery in the North America and Europe and the global economy.
- Domestic demand for ATBS is growing slower. The company expects ~20-25% growth in the global ATBS market. In the last decade it grew ~15%.
- Key global customers are BASF, Dow Chemicals and SNF.
- Management clarified that the price of ATBS is not as volatile as that of crude. Key raw materials for ATBS are acrylonitrile and IBB. On the 10% change in the price of crude, ATBS prices change ~1%. ATBS price movements were ~\$2.5-3.5/kg in the last ten years.
- At present, there are three biggies in the global ATBS market, the largest being Vinati. The second is a Chinese company, which has not expanded capacity in the last 5-6 years and has no expansion plans. The third, in Japan, has ~6,000 tons manufacturing capacity and has not expanded in the last 10 years.
- Management guided to ~80-85% y/y ATBS volume growth in FY22 due to the low base. Growth on the base of a normal year would be ~35%. The company manufactured 24,000 tons of ATBS in FY20 operating at full capacity. In FY21, capacity increased to 40,000 tons. Volumes declined to ~16,000 tons in FY21 due to lower demand globally. The company is experiencing strong demand from Jan'21 and getting strong order projections from customers. It expects sales of ~30,000 tons of ATBS in FY22.

IBB

- The company has maintained a 70% market share in IBB. It recorded the highest sales of IBB in FY21 due to the low base. Its IBB revenue was down in FY20 as the plant of one of its largest customers was shut down. At present, Vinati has 40,000 tons capacity and is running at full capacity, though it can increase this ~50,000 tons.

- Management guided to double-digit growth in IBB revenue in FY22 and FY23, supported by strong demand for Ibuprofen. Such growth is expected following new manufacturers and capacity expansion by existing ones.

Butyl Phenol

- The greenfield plant was operationalised last year. It is now running at ~50-60% capacity. The company expects Rs2.5bn revenue from these four butyl phenol products. Management says all butyl phenol products have been well received domestically and is exports.
- The backward integration into IBB helped the company gain market share in a short time.
- At present, it manufactures four types of butyl phenol
 - Para-tertiary butyl phenol (PTBP)
 - Ortho-tertiary butyl phenol (OTBP)
 - 2,4-di tertiary butyl phenol (2,4-DTBP)
 - 2,6-di tertiary butyl phenol (2,6-DTBP)
- The PTBP and OTBP are used mainly in the fragrance and resin industries. The global market is very vast and the company has only 35,000 tons of manufacturing capacity.
- Management says 2,4-DTBP and 2,6-DTBP will be used to manufacture antioxidants. The global market for antioxidants is more than 300,000 tons, the domestic market, 25,000 tons. The company is coming up with 25,000 tons of antioxidant capacity, and expects to sell 50% in the home market and export 50%.
- Key manufacturers are BASF, SI and Songwon. The company expects an ~80% share domestically and be among the top-5 globally in the coming 4-5 years.

Other products (including Isobutylene, HPMTBE, PCBA, others)

- The contribution from a few customized products was ~25% in FY21.
- The company expects double-digit growth in these products.

PAP project

- This project is in a pilot stage and the company does not expect revenue generation in the next three years.

New products and expansion

- The company is working on new products. Management says that these products will have some synergies with existing products.
- The major growth contributor would be antioxidants, the direct forward integration of butyl phenol.
- Further, the company is working on other butyl phenol downstream products; O-sec-Butylphenol (OSBP), Di-sec-Butylphenol (DSBP) and T-butyl-o-cresol (TBOC). This would be a horizontal integration with similar processes but different applications.

Capex

- The company has guided to do ~Rs3bn capex in the next 2-3 years.
 - ~Rs2bn for new products
 - ~Rs0.5bn-0.7bn on Veeral Additives
 - Further capex to expand ATBS or other capacity
- The company has enough land (~25 acres) for expansions.

Guidance

- Management guided to ~40%-50% revenue growth in FY22.

Fig 8 – Quarterly trend

Particulars(Rs m)	Q3FY19	Q4FY19	Q1FY20	Q2FY20	Q3 FY20	Q4 FY20	Q1 FY21	Q2 FY21	Q3 FY21	Q4FY21	% Y/Y	% Q/Q	FY20	FY21	% Y/Y
Income	3,031	3,019	2,907	2,491	2,385	2,453	2,316	2,194	2,235	2,798	14.0	25.2	10,237	9,543	(6.8)
RM costs	1,479	1,328	1,230	984	1,083	990	849	880	1,007	1,142	15.3	13.4	4,287	3,877	(9.6)
Employee exp	140	130	153	160	171	159	184	181	184	177	11.4	(4.1)	643	726	13.0
Other expenses	347	310	323	309	300	288	311	293	323	488	69.3	51.3	1,220	1,414	16.0
EBITDA	1,064	1,251	1,202	1,039	830	1,017	972	841	721	991	(2.5)	37.5	4,087	3,525	(13.8)
Depreciation	69	68	70	72	93	97	106	108	108	107	10.6	(0.4)	332	429	29.4
Interest	3	2	3	3	3	3	0	0	0	1	(57.1)	1,032.7	11	2	(80.6)
Other income	73	50	114	71	154	162	86	14	93	66	(59.5)	(29.3)	502	259	(48.5)
PBT	1,065	1,230	1,243	1,036	889	1,079	951	747	706	949	(12.1)	34.3	4,246	3,353	(21.1)
Tax	358	405	419	(64)	220	333	228	127	65	240	(27.9)	271.1	908	659	(27.4)
Reported PAT	707	825	824	1,100	668	746	723	620	641	709	(5.0)	10.5	3,338	2,693	(19.3)
EPS(Rs)	6.9	8.0	8.0	10.7	6.5	7.3	7.0	6.0	6.2	6.9	(5.0)	10.5	32.5	26.2	(19.3)

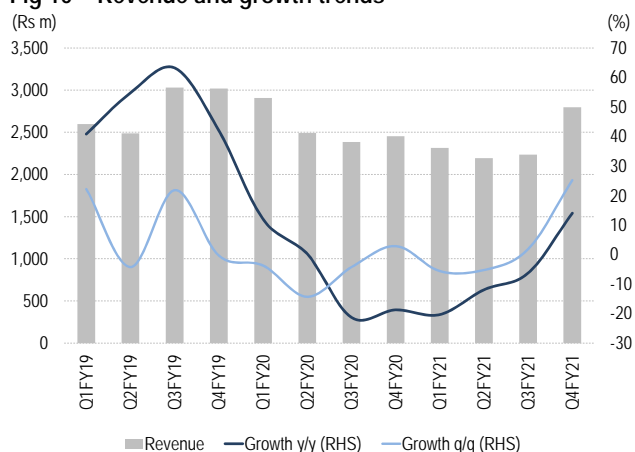
Source: Company

Fig 9 – Quarterly trend, as percent of sales

Particulars	Q3FY19	Q4 FY19	Q1 FY20	Q2 FY20	Q3 FY20	Q4 FY20	Q1 FY21	Q2 FY21	Q3 FY21	Q4 FY21	bps Y/Y	bps Q/Q	FY20	FY21	bps Y/Y
Gross margins	51.2	56.0	57.7	60.5	54.6	59.7	63.4	59.9	55.0	59.2	(47)	424	58.1	59.4	126
Employee costs	4.6	4.3	5.2	6.4	7.2	6.5	8.0	8.2	8.3	6.3	(15)	(193)	6.3	7.6	133
Other expenses	11.4	10.3	11.1	12.4	12.6	11.7	13.4	13.3	14.4	17.4	569	301	11.9	14.8	291
EBITDA margins	35.1	41.4	41.3	41.7	34.8	41.4	42.0	38.3	32.3	35.4	(601)	317	39.9	36.9	(298)
Depreciation	2.3	2.3	2.4	2.9	3.9	4.0	4.6	4.9	4.8	3.8	(12)	(98)	3.2	4.5	126
Interest	0.1	0.1	0.1	0.1	0.1	0.1	0.0	0.0	0.0	0.0	(7)	4	0.1	0.0	(8)
Other income	2.4	1.6	3.9	2.9	6.5	6.6	3.7	0.6	4.2	2.3	(426)	(181)	4.9	2.7	(219)
PBT margins	35.1	40.7	42.8	41.6	37.3	44.0	41.1	34.0	31.6	33.9	(1,008)	231	41.5	35.1	(635)
Effective tax rate	33.6	32.9	33.7	(6.2)	24.8	30.8	24.0	17.0	9.2	25.3	(556)	1,614	21.4	19.7	(173)
PAT margins	23.3	27.3	28.3	44.1	28.0	30.4	31.2	28.3	28.7	25.3	(509)	(337)	32.6	28.2	(438)

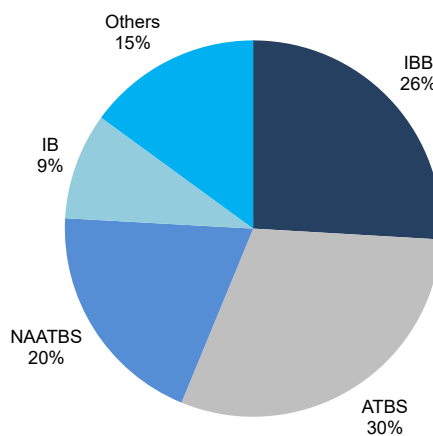
Source: Company

Fig 10 – Revenue and growth trends



Source: Company

Fig 11 – Revenue, business-wise FY20



Source: Company, Anand Rathi Research

Fig 12 – Acrylonitrile price movement



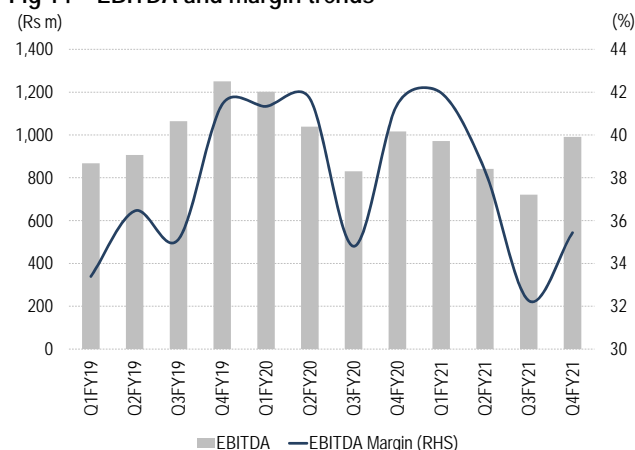
Source: Bloomberg

Fig 13 – Phenol price movement



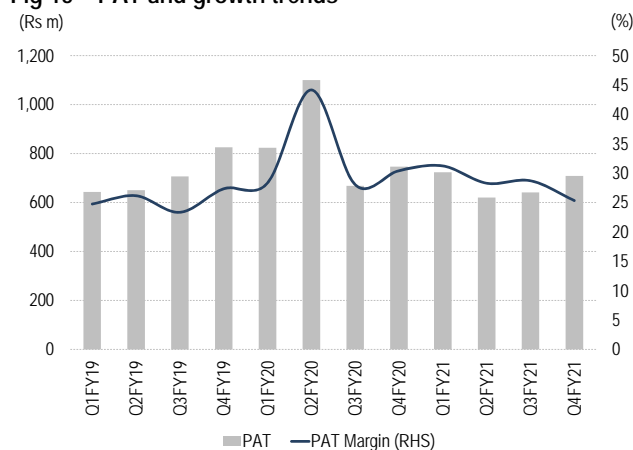
Source: Bloomberg

Fig 14 – EBITDA and margin trends



Source: Company

Fig 15 – PAT and growth trends



Source: Company

Revenue growth prospects

Butyl phenol - The ~39,000tpa butyl phenol plant was commissioned in Q2FY20. Being the leading manufacturer of IB, it will be easy for Vinati to forward integrate. Total revenue potential is ~Rs4bn-4.5bn. Plant in FY21 utilisation was low due to the Covid-19 outbreak and the challenging business environment. Utilisation is expected to improve and Rs2.5bn revenue be attained in FY23e.

PTBBA expansion The company announced Rs1.5bn capex in Oct'20 to manufacture four new specialty chemical products of the PTBBA plant. These will be used mainly in agrochemicals, dyes and plastic additives. The company can generate Rs2.4bn revenue from this expansion. Further, in Nov'20 it announced additional capex of Rs600m for new products and expansions. Expected revenue potential would be Rs3bn from the total capex of Rs2.1bn.

ATBS expansion. In FY20 the company expanded its ATBS capacity by 14,000 tons to 40,000 tons at Rs1.1bn capex. It expects to generate additional revenue of Rs2.5bn-3bn from this expansion. Margins are expected to be strong in Q1 due to the added contribution from high-margin ATBS. The company has guided to ~80-85% volume growth in ATBS in FY22.

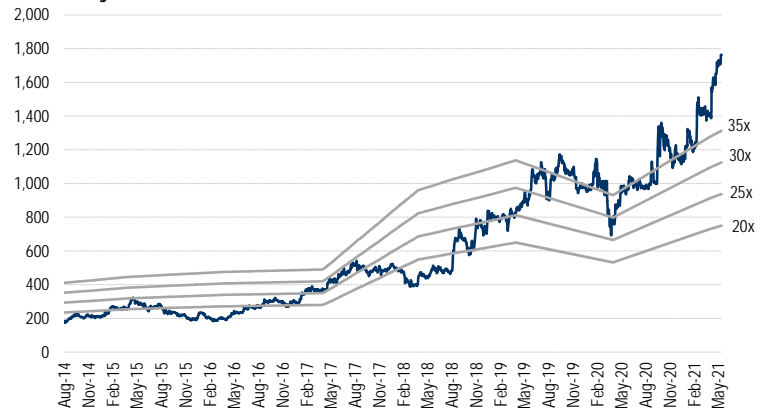
The Veeral acquisition. The Board approved the Veeral Additives amalgamation with Vinati. The former manufactures antioxidants (24,000 tpa). This acquisition is a forward integration for Vinati as its butyl phenol products will be used to manufacture antioxidants. After the acquisition, Vinati will become the largest and only integrated manufacturer of such antioxidants in India. Veeral can generate Rs.3bn revenue.

Strong cash position. We estimate that after the Rs5bn capex (as indicated by management) from FY20 to FY23, the company will have cash and investments of over Rs.5bn in FY23e. This will be 46% of its gross block. We believe that management will continue to find avenues to invest this accumulated cash at similar RoICs of 25%+, thus paving the way to further growth.

Valuation

We maintain a Buy, with a higher target of Rs.2,000. At this, the stock is valued at PEs of 55x FY22e and 41x FY23e. On an EV/EBITDA multiple, it is valued at 40x FY22e and 30x FY23e.

Fig 16 – One-year-forward P/E band



Source: Anand Rathi Research

Risks

- Shutdown of key clients' manufacturing plants.
- Delay in scaling up from laboratory stage to commercial scale.
- Slowdown in R&D and new product pipeline.
- Unfavourable forex movements.
- Global slowdown, leading to a deceleration in key consumer sectors.

Appendix

Analyst Certification

The views expressed in this Research Report accurately reflect the personal views of the analyst(s) about the subject securities or issuers and no part of the compensation of the research analyst(s) was, is, or will be directly or indirectly related to the specific recommendations or views expressed by the research analyst(s) in this report. The research analysts are bound by stringent internal regulations and also legal and statutory requirements of the Securities and Exchange Board of India (hereinafter "SEBI") and the analysts' compensation are completely delinked from all the other companies and/or entities of Anand Rathi, and have no bearing whatsoever on any recommendation that they have given in the Research Report.

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Ratings Guide (12 months)	Buy	Hold	Sell
Large Caps (>US\$1bn)	>15%	5-15%	<5%
Mid/Small Caps (<US\$1bn)	>25%	5-25%	<5%

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