AMBIT INSIGHTS

27 April 2018

AMBIT Acumen at work

DAILY

UPDATES

Ten Interesting Things

RESULTS UPDATE

Axis Bank (SELL)

Bad loan clean-up accelerates

Supreme Industries (SELL)

Realisations positively surprise

Rallis India (SELL)

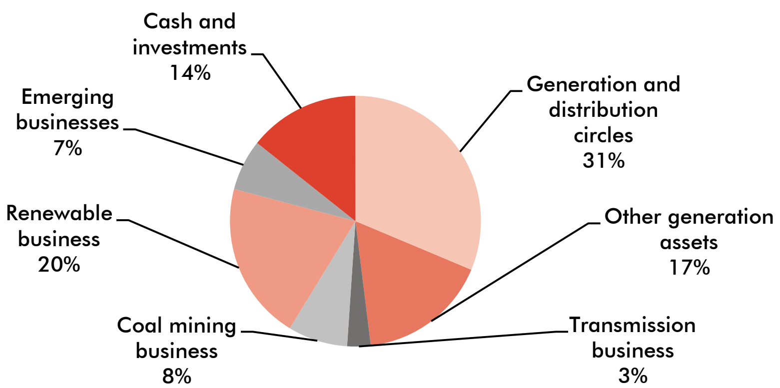
Another weak quarter

ANALYST NOTES: Power: Acme Solar drops IPO plans; limited read across for to-be listed renewable companies (Bhargav Buddhadev +91 22 3043 3252)

Acme Solar, the first renewable energy company to start listing procedure in India may have dropped its initial public offering (IPO) plans as the deadline for refiling its DRHP in light of reduction in valuation has expired. As per SEBI, DRHP has to be re-filed if the end use of the IPO is modified by more than 20%. Acme's valuation expectation was steep; expected EV/MW as per our calculation was >Rs100mn on commissioned capacity of 1GW; as compared to this, we value Tata Power Renewable's capacity at EV of <Rs80mn per MW. Moreover, Acme's equity investment (excludes promoter's loan) as per FY17 balance sheet is very low at Rs1.2bn, implying net debt:equity ratio of 98:2 vs general thumb rule of 70:30. If Acme's IPO plans don't fructify, it won't affect the IPO plans for other renewable companies'; ReNew Power is soon likely to file DRHP possibly followed by Tata Power Renewables. Tata Power remains our top pick with a TP of Rs125.

Source: Ambit Capital research

HAVE YOU SEEN THIS? Renewable business accounts for 20% of our Tata Power's SOTP



Source: Ambit Capital research

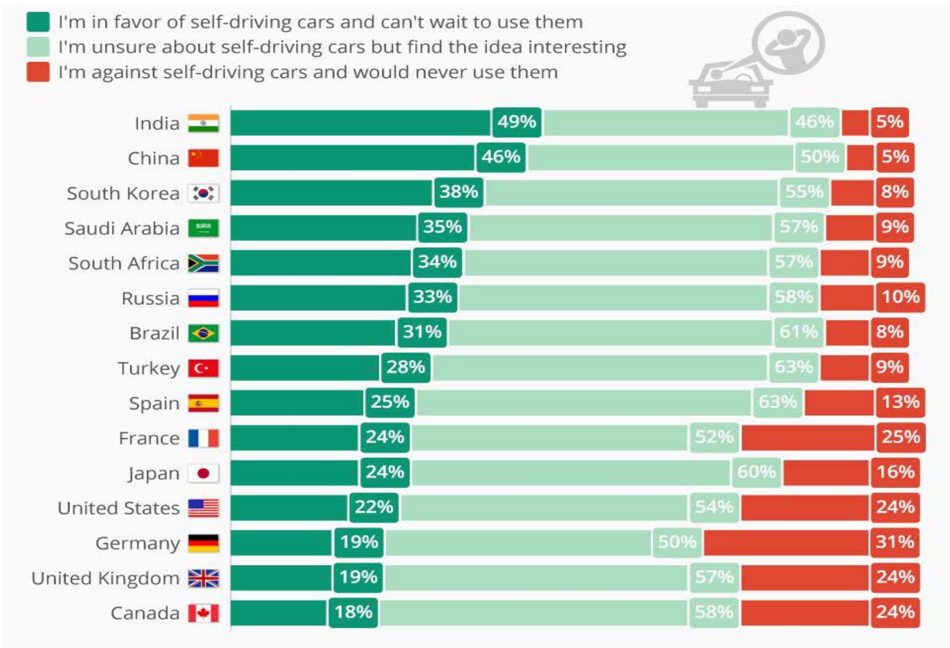
Please refer to our website for complete coverage universe

http://ambitresearch.co

At Ambit, we spend a lot of time reading articles that cover a wide gamut of topics, including investment analysis, psychology, science, technology, philosophy, etc. We have been sharing our favourite reads with clients under our weekly 'Ten Interesting Things' product. Some of the most interesting topics covered in this week's iteration are related to 'Big tech and barter', 'San Francisco's seismic gamble', and 'brain similarities in best friends'.

1. **China's Ant Financial shows cashless is king** [Source: Financial Times] (https://goo.gl/XYVpfb)
2. **How Big Tech brought back barter economy** [Source: Financial Times] (https://goo.gl/mh5tHv)
3. **How Domino's Pizza drove a 90x increase in stock value by acting like a tech start-up** [Source: producthabits.com] (https://goo.gl/vmQ6Ay)
4. **San Francisco's big seismic gamble** [Source: NY Times] (https://goo.gl/5HSUiq)
5. **Why is the human brain so efficient?** [Source: nautil.us] (https://goo.gl/MZbGhx)
6. **New Zealand to ban future offshore oil and gas exploration** [Source: Financial Times] (https://goo.gl/5dkcQD)
7. **You share everything with your bestie- even your brain waves** [Source: NY Time](https://goo.gl/JGYKGM)
8. **The Botch of the human body** [Source: WSJ] (https://goo.gl/yhfGXv)
9. **Global chocolate sales hit a sweet spot** [Source: Financial Times] (https://goo.gl/RUvVnt)
10. **"2001: A space odyssey": What it means and how it was made** [Source: New Yorker] (https://goo.gl/M4Cugv)

Indians are the most excited lot when it comes to self-driving cars



Source: Ipsos, Statista

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Axis Bank

SELL

Result Update

Bad loan clean-up accelerates

Axis Bank reported 4QFY18 net loss of Rs21.9bn vs our expectation of Rs6.4bn net loss and consensus estimate of Rs6.6bn profit. Very high slippages (Rs165bn vs Rs44bn in 3Q) arose chiefly from stressed standard loans transitioning to NPAs. Associated provisioning led to high credit cost. Thus, total stressed loans, net of provisions, declined by 10% QoQ and stood at 5.8% of loans (vs 6.7% of loans in 3Q). On operating performance, loan growth trends were resilient (up 18% YoY), but subdued NIM (down 50bps YoY) resulted in decrease in core operating profit by 12% YoY. With accelerated clean-up expected to continue, we expect reduction in net NPAs to be below 2% by end-FY19, but elevated credit costs (225bps in FY19E) should result in muted FY19E RoE (<10%). However, RoE should recover to 15-16% by FY20E on cleaner balance sheet. At the current valuation of 1.8x FY19E P/B, the stock is fairly valued given weak earnings in FY19E with improving strength of the franchise. Remain SELLers with an unchanged TP of Rs503.

Results overview: Axis Bank reported 4QFY18 net loss of Rs21.9bn vs our expectation of Rs6.4bn net loss and consensus estimate of Rs6.6bn profit. Fresh slippages jumped to Rs165bn (vs Rs44bn in 3Q) due to NPA recognition from the bank's stressed assets pool. Stressed standard assets pool thus shrunk by 47% QoQ. It now stands at 2.0% of loans (vs 4.0% at end-3Q). Loan book grew by 18% YoY with the retail loans (47% of the book) up 23%. NII was flat YoY, with NIM down 50bps YoY. Operating profit thus declined by 16% YoY.

Asset Quality – sharp pick-up in NPA recognition: In 4QFY18, gross NPAs grew by 37% QoQ, led by fresh addition of Rs165bn to gross NPAs (vs Rs44bn in 3Q). Slippages largely arose from the bank's corporate segment. The stressed standard asset pool continues to be the key source of the slippage (90% of corporate slippage in 4Q, in line with the trend seen in last eight quarters). Despite the large NPA addition, the bank's NPA provision coverage was stable QoQ (52%, excluding technical write-offs) and credit costs thus spiked sharply to 720ps (vs 20bps in 9MFY18).

The bank's stressed standard asset pool however declined by 47% YoY as these slipped to NPA. Total stressed standard loans thus stand at 2.0% of loans (vs 4.0% at end-3Q). Including NPAs, thus, total gross bad loans now stand at 9.9% of loans (vs 10.1% of loans at end-3Q). With migration to NPAs, however, provision cover on bad loans increased to 41% (vs 33% at end-3Q). Thus, residual stressed assets, net of provisions, now stand at 5.8% of loans (vs 6.7% at end-3Q).

Exhibit 1: Progression on Axis Bank's bad loans

As % of loans	4QFY16	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18
Gross NPAs	1.8%	2.8%	4.6%	5.9%	5.7%	5.7%	6.7%	5.9%	7.8%
Stressed std.	9.0%	9.7%	7.6%	6.8%	5.6%	5.6%	4.3%	4.1%	2.1%
Total bad	**10.8%**	**12.5%**	**12.2%**	**12.7%**	**11.3%**	**11.3%**	**10.9%**	**10.1%**	**9.9%**
Provision cover	11.2%	14.2%	21.5%	29.1%	32.1%	29.9%	31.7%	33.1%	41.3%
Net bad loans	**8.8%**	**9.5%**	**7.4%**	**6.6%**	**5.3%**	**5.4%**	**4.0%**	**4.0%**	**2.0%**

Source: Company, Ambit Capital research

Core operating profitability still subdued: In 4QFY18, loan growth picked up to 18% YoY, third straight quarter of resilient growth. Retail (47% of the book) grew by 23% YoY. SME (13% of the book) was up 19% YoY. Driven by working capital corporate loans, corporate loans grew by 12% YoY.

Within retail, the bank saw strong growth in personal loans & credit cards (up 43% YoY), auto loans (up 35% YoY) and loan against property (up 23% YoY).

CASA deposits grew by 15% YoY, taking CASA ratio to 54%. CASA and retail term deposits form 84% of loans (vs 81% at end-FY17). While there was pressure on yield on advances, due to change in loan mix and NPA slippages, proceeds of capital raise cushioned NIM (down 5bps QoQ). Fee income grew by 8% YoY with the retail fee

Stock Information

Bloomberg Code:	AXSB IN
CMP (Rs):	494
TP (Rs):	503
Mcap (Rs bn/US$ bn):	1,268/19.0
3M ADV (Rs mn/US$ mn):	4,229/63.4

Stock Performance (%)

	1M	3M	12M	YTD
Absolute	(3)	(20)	(5)	(12)
Rel. to Sensex	(8)	(16)	(20)	(14)

Source: Bloomberg, Ambit Capital research

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(~50% of the fee) up 22% YoY. Opex grew by 14% YoY, taking core operating profit down by 12% YoY. Core operating profitability (as a percentage of average assets) was at 2.1%, (vs 2.3% in 3QFY18). This is lower than what the bank has historically delivered (FY16: 3.0%; FY17: 2.5%).

Where do we go from here?

The acceleration in NPA recognition from the bank's stressed standard loans is in line with our expectation, with plateauing overall corporate stress and push from the regulator on banks to accelerate the clean-up. With residual bad loans (net of provisions), at 5.8% of loans, being still at meaningful level, we expect credit cost will remain elevated for a few more quarters. Subsequent to which, led by provisions and write-offs, we expect net NPAs to fall below 2% by end-FY19.

RoE will thus likely remain subdued at below 10% in FY19E, before normalising closer to 15-16% in FY20E on a cleaner balance sheet. At the current valuation of 1.8x FY19E P/B, the risk-reward remains evenly balanced given weak profitability in FY19 but improving franchise strength of the bank. We would watch out for stability in size of stressed assets pool and improving trends in loan yields before becoming more constructive on the bank and, hence, remain SELLers with an unchanged target price of Rs503 (11x FY20E P/E and 1.7x FY20E P/B).

Exhibit 2: Quarterly snapshot

Earnings Table (Rs mn)	**4QFY17**	**3QFY18**	**4QFY18**	**YoY (%)**	**QoQ (%)**	**4QFY18E**	**A/E (%)**
NII	**47,286**	**47,315**	**47,305**	**0%**	**0%**	**51,412**	**-8%**
Non-Interest income	**30,132**	**25,931**	**27,887**	**-7%**	**8%**	**25,630**	**9%**
Total Income	**77,418**	**73,246**	**75,191**	**-3%**	**3%**	**77,042**	**-2%**
Employee Cost	9,480	10,629	10,789	14%	2%	11,497	-6%
Other Operating Expenses	24,191	24,079	27,680	14%	15%	26,061	6%
Total Operating Expenses	33,670	34,708	38,469	14%	11%	37,558	2%
Operating Profit	**43,747**	**38,538**	**36,722**	**-16%**	**-5%**	**39,484**	**-7%**
Total Provisions	**25,813**	**28,110**	**71,795**	**178%**	**155%**	**48,358**	**48%**
PBT	17,935	10,428	-35,073	NA	NA	-8,874	NA
Tax	5,684	3,163	-13,186	NA	NA	-2,461	NA
Reported Profit	**12,251**	**7,264**	**-21,887**	**NA**	**NA**	**-6,413**	**NA**
Balance sheet (Rs bn)							
Deposits	4,143.8	4,089.7	4,536.2	9%	11%	4,498.6	1%
Net Advances	3,730.7	4,209.2	4,396.5	18%	4%	4,461.8	-1%
Total Assets	**6,014.7**	**6,439.4**	**6,913.3**	**15%**	**7%**	**6,938.3**	**0%**
Key Ratios							
Credit Quality							
Gross NPAs (Rs mn)	212,805	250,005	342,486	61%	37%	270,005	27%
Net NPAs (Rs mn)	86,266	117,695	165,917	92%	41%	121,502	37%
Gross NPA (%)	5.52%	5.76%	7.49%			5.86%	
Net NPA (%)	2.31%	2.80%	3.77%			2.72%	
Loan Loss Provisions (%)	2.87%	2.93%	6.67%			4.46%	
Coverage Ratio (%)	59.5%	52.9%	51.6%			55.0%	
Capital Adequacy							
Tier I (%)	11.87%	13.63%	13.04%				
CAR (%)	14.95%	17.50%	16.57%				
Du-pont Analysis							
NII / Assets (%)	3.21%	2.96%	2.83%			3.09%	
Non-Interest Inc. / Assets (%)	2.04%	1.62%	1.67%			1.54%	
Operating Cost / Assets (%)	2.28%	2.17%	2.30%			2.20%	
Operating Profits / Assets (%)	2.68%	2.28%	2.07%			2.30%	
Provisions / Assets (%)	1.75%	1.76%	4.30%			1.80%	
ROA (%)	**0.83%**	**0.45%**	**-1.31%**			**-0.39%**	

Source: Company; Ambit Capital research

Supreme Industries

SELL

Result Update

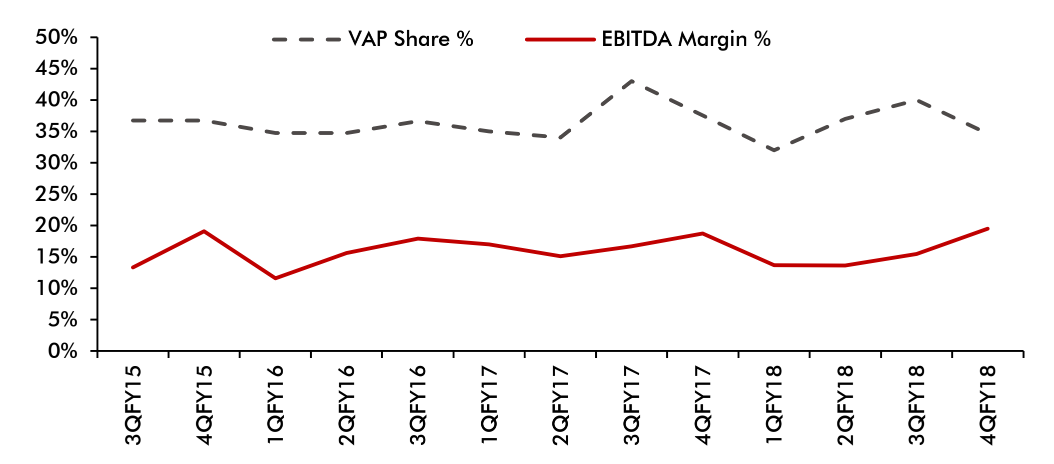
Realisations positively surprise

Supreme's overall volumes and blended realisations grew 8% and 7% YoY, respectively. While the volume growth was 3% below our estimate, blended realisation growth was a positive surprise. Growth in realisation was largely due to increased contribution (~16% of overall revenues) and 34% YoY realisation growth of industrial products division. Though EBITDA margins expanded marginally by 78bps YoY, sequentially it improved by ~400bps given 5% improvement in realisations and one-time inventory gain from the piping segment. FY18 EBITDA margin stood at 15.8%. Management guided for 12% overall volume growth for FY19 with strong demand expectation across all segments (including composite cylinders). Management announced fresh capex of Rs3-3.5bn for Greenfield capacities in AP and Assam. We upgrade our estimates for FY19 and FY20 to account for strong performance of industrial products division led by strong demand for auto components and consumer durables. FY19 volume/revenue should grow by 12%/17%. Low-teen volume growth, lack of high-margin product launches, high competition and limited scope to gain from unorganised will limit working capital and RoCE improvement. Our one-year TP of Rs1,100 implies rich valuation of 22x FY20E EPS (a lofty 21% EPS FY18-20 CAGR).

Key points to note from the results

- Share of VAP for FY18 was 36% vs. 38% in FY17. Higher growth in industrial products division and piping business, share of VAP should further come down.
- In 2QFY18, the management had revised its capex guidance of Rs3.5bn to Rs4.5bn to be spent over FY18-19 for increasing its capacity by 50k MT. Of these, Supreme has spent Rs2.6bn in FY18. In FY18, Supreme's overall capacity has increased by ~25k MT to 568K MT. The remaining of this capex is mainly committed for increase in capacities of industrial product and packaging division.
- Management further guided for Rs3-3.5bn capex for a Greenfield capacity in Andhra Pradesh and Assam. These capacities are expected by the management to come up in FY20.
- Management displays its astuteness in capital allocation – keeping debt low, increasing capex and divesting low-margin/RoCE industrial capacities (albeit keeping some ownership).

Exhibit 1: VAP Share vs. EBITDA Margins – Pressure from low share of VAP was mitigated by sequential improvement in realisations of Pipes and Industrial products segment



Source: Ambit Capital Research

Stock Information

Bloomberg Code:	SI IN
CMP (Rs):	1,303
TP (Rs):	1,100
Mcap (Rs bn/US$ mn):	166/2,474
3M ADV (Rs mn/US$ mn):	184/2.8

Stock Performance (%)

	1M	3M	12M	YTD
Absolute	6	(6)	17	(4)
Rel. to Sensex	(0)	(2)	1	(5)

Source: Bloomberg, Ambit Capital research

Ambit Estimates (Rs bn)

	FY18	FY19E	FY20E
Revenues	50	58	69
EBITDA	7.9	9.2	11.0
EPS (Rs)	34.2	41.3	50.4

Source: Bloomberg, Ambit Capital research

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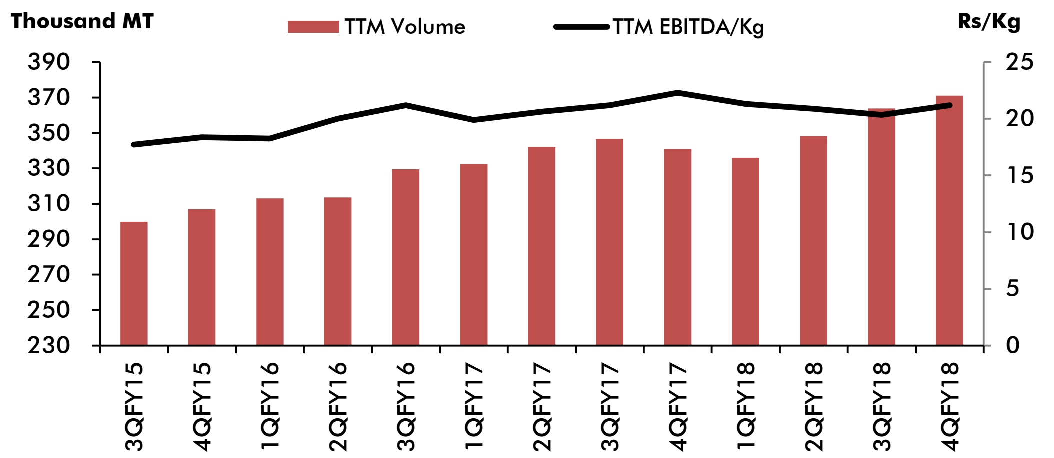
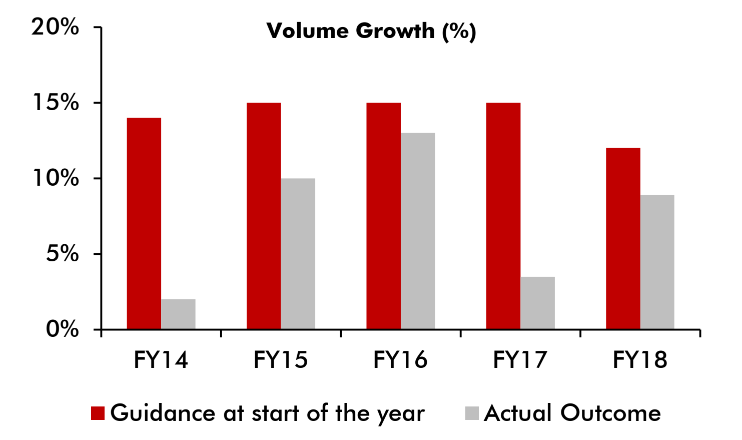
Exhibit 2: Trailing 12-month volumes at all-time highs but EBITDA (Rs/kg) has been trending lower for the last few quarters



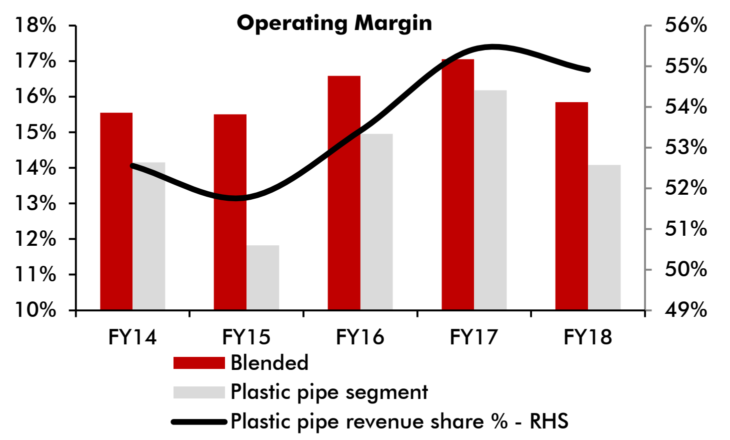
Source: Ambit Capital Research

Exhibit 3: Management has consistently missed volume growth guidance



Source: Bloomberg, Ambit Capital research.

Exhibit 4: Increasing competition amid weak pipe demand has led to lower margins despite share remaining same as last year



Source: Bloomberg, Ambit Capital research

Exhibit 5: Revision to our estimates

Particulars (Rs mn unless mentioned)	New estimates		Old estimates		Change in estimates		Comments
	FY19	FY20	FY19	FY20	FY19	FY20	
Volume growth							
Plastic piping systems	12.0%	14.0%	12.0%	14.0%	0 bps	0 bps	
Packaging products	10.0%	11.7%	10.0%	11.7%	0 bps	0 bps	We expect the strong volume growth in industrial products division to continue in FY19 and FY20, led by strong demand of auto components and consumer durables.
Industrial products	15.0%	14.0%	15.0%	14.0%	0 bps	0 bps	
Consumer durables	12.0%	14.0%	12.0%	14.0%	0 bps	0 bps	
Realisation growth							
Plastic piping systems	2.0%	2.0%	2.0%	2.0%	0 bps	0 bps	Realisations considerably improved for industrial products division in FY18. We expect realisations to further improve by 5% in FY19 and FY20
Packaging products	2.0%	3.5%	1.7%	3.5%	32 bps	0 bps	
Industrial products	5.0%	5.0%	2.5%	5.0%	250 bps	0 bps	Realisations for piping business will continue to be under pressure and so there will be limited pricing growth.
Consumer durables	2.5%	3.0%	2.5%	3.0%	0 bps	0 bps	
Net revenues (Rs mn)							
Plastic piping systems	31,155	36,228	31,323	36,422	-1%	-1%	
Packaging products	11,440	13,222	11,589	13,395	-1%	-1%	Revenue growth of Industrial products segment increased by 20% for both FY19 and FY20 due to strong performance of this segment in FY18 and we expect this momentum to continue over medium term.
Industrial products	9,658	11,560	8,042	9,627	20%	20%	
Consumer durables	4,038	4,742	3,922	4,606	3%	3%	
Composites	1,750	2,925	1,750	2,925	0%	0%	
Total	**58,041**	**68,676**	**56,627**	**66,974**	2%	3%	
EBIT margin							
Plastic piping systems	10.5%	11.0%	10.5%	11.0%	0 bps	0 bps	Piping business margins will continue to be under pressure given the increase in competitive intensity in the segment as both existing and new players mimic the portfolio range and geographical reach of the leaders.
Packaging products	17.5%	18.0%	17.6%	18.0%	-7 bps	0 bps	
Industrial products	14.0%	14.0%	12.0%	12.2%	209 bps	189 bps	We expect better margins for from Industrial products division in FY19 and FY20 but not as high as in FY18.
Consumer durables	14.0%	14.3%	14.0%	14.3%	0 bps	0 bps	
Composites	13.0%	14.0%	13.0%	14.0%	0 bps	0 bps	
Overall EBIT	12.5%	13.0%	12.2%	12.7%	32 bps	29 bps	Margins improve by ~30bps in FY19 and FY20 as benefit of improvement in margins of Industrial products segment offset by decrease in share of revenues of Packaging segment.
Overall EBITDA	15.8%	16.0%	15.7%	15.9%	11 bps	6 bps	
Interest	131	112	131	112	0%	0%	
Depreciation	1,908	2,125	1,978	2,226	-4%	-5%	
PAT	4,891	6,039	4,631	5,726	6%	5%	
EPS (in Rs)	41	50	41	50	1%	1%	
EPS growth	21%	22%	23%	21%	-202 bps	68 bps	
Profitability ratios							
RoCE	21%	23%	20%	22%	95 bps	99 bps	Improvement in RoCE and RoE due to improvement in margins
RoE	25%	28%	25%	27%	15 bps	29 bps	
Target Price	1,100		1,050				

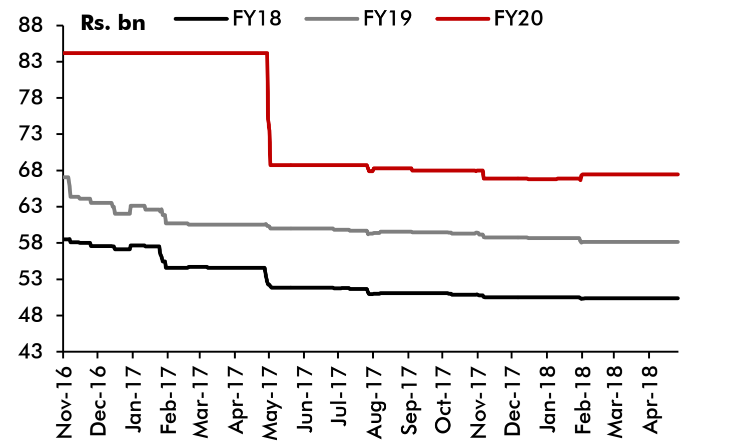
Source: Ambit Capital Research

Exhibit 6: Our EPS estimates for FY19 and FY20 are 6% and 5% ahead of consensus, respectively

(Rs mn)	Ambit estimates		Consensus estimates		Deviation	
	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E
Revenues	58,271	68,918	57,506	66,774	1%	3%
Growth %	17%	18%	16%	16%	154bps	215bps
EBITDA	9,188	11,026	9,083	10,833	1%	2%
EBITDA margin	15.8%	16.0%	15.8%	16.2%	-3bps	-22bps
EBIT	7,280	8,901	7,122	8,682	2%	3%
PBT	7,355	9,081	7,010	8,645	5%	5%
PAT	5,248	6,406	4,972	6,123	6%	5%
EPS (Rs)	41	50	39	48	6%	5%

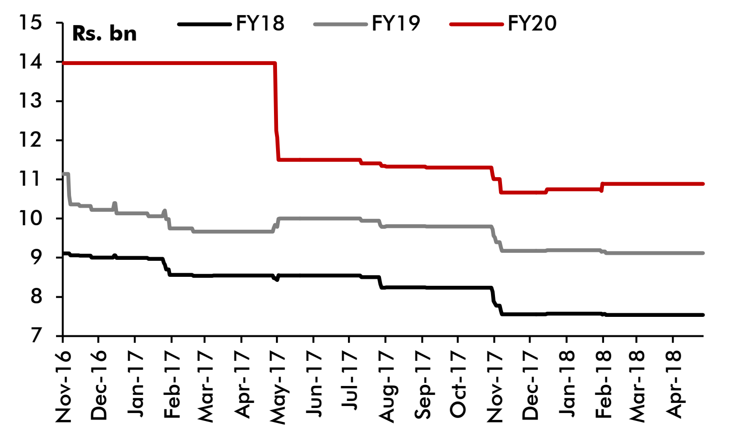
Source: Bloomberg, Ambit Capital Research

Exhibit 7: Consensus revenue estimates have been stable after cutting it for channel destocking in June'2017 owing to roll-out of GST



Source: Ambit Capital research

Exhibit 8: Recently, consensus has cut EBITDA margins by 150bps and 100bps for FY19 and FY20 respectively possibly due to falling realisations in pipes business as competition intensifies for the sector



Source: Ambit Capital research

Exhibit 9: 4QFY18 results summary

(Rs mn, unless specified)	4QFY17	3QFY18	4QFY18	YoY	QoQ	Ambit Est.	Deviation
Volumes Sold (MT)	95,870	96,737	103,214	8%	7%	106,218	-3%
Realization (Rs)	134	132	143	7%	8%	133	7%
Net Sales	12,826	12,783	14,713	15%	15%	14,069	5%
Total operating expenditure	10,427	10,806	11,845	14%	10%	11,894	0%
% of net sales	81%	85%	81%	-1%	-5%	85%	-5%
Reported EBITDA	2,399	1,977	2,868	20%	45%	2,468	16%
Reported EBITDA margin (%)	19%	15%	19%	78bps	402bps	18%	195bps
Depreciation	411.8	427.6	413.7	0%	-3%	425	-3%
Reported EBIT	1,988	1,550	2,454	23%	58%	2,043	20%
Reported EBIT margin	15%	12%	17%	8%	38%	15%	15%
Other income	26	5	37	44%	640%	50	-26%
Interest	34	79	56	63%	-29%	80	-30%
Reported Profit before tax	1,979	1,476	2,435	23%	65%	2,013	21%
Tax	724	518	774	7%	49%	664	16%
Tax rate (%)	37%	35%	32%			33%	
Adjusted Net profit	1,256	958	1,661	32%	73%	1,349	23%
Associate Income	208.5	83.9	121.7	-42%	45%	100	22%
Adjusted Net profit after MI	1,464	1,042	1,783	22%	71%	1,449	23%
Net profit margin (%)	11%	8%	12%	71bps	397bps	10%	182bps
No of shares(mn)	127	127	127	0%	0%	127	0%
EPS	11.5	8.2	14.0	22%	71%	11.4	23%

Source: Company, Ambit Capital research

Exhibit 10: Segmental results 4QFY18

Particulars	4QFY17	3QFY18	4QFY18	YoY	QoQ	Ambit Est.	Deviation
Volumes (MT)							
Plastic Piping Systems	67,549	64,435	72,779	8%	13%	77,006	-5%
Packaging products	12,245	15,806	11,905	-3%	-25%	11,971	-1%
Industrial products	10,817	11,350	12,600	16%	11%	11,682	8%
Consumer durables	5,054	5,143	5,909	17%	15%	5,559	6%
Composite products	205	3	21			-	
Total volumes	**95,870**	**96,737**	**103,214**	8%	7%	**106,218**	-3%
Realisation (Rs)							
Plastic Piping Systems	109	103	114	5%	10%	113	1%
Packaging products	209	202	207	-1%	2%	206	1%
Industrial products	151	170	203	34%	20%	170	20%
Consumer durables	161	178	161	0%	-9%	177	-9%
Net Realization per ton	134	132	143	7%	8%	133	7%
Revenues (Rs mn)							
Plastic Piping Systems	7,359	6,665	8,288	13%	24%	8,698	-5%
Packaging products	2,563	3,192	2,464	-4%	-23%	2,463	0%
Industrial products	1,637	1,927	2,558	56%	33%	1,981	29%
Consumer durables	815	913	953	17%	4%	984	-3%
Others	452	86	450	-1%	423%	-	
Net Revenue from Operations	**12,826**	**12,783**	**14,713**	**15%**	**15%**	**14,126**	4%
EBIT (Rs mn)							
Plastic Piping Systems	1,060	678	1,303	23%	92%	1,131	15%
Packaging products	532	614	493	-7%	-20%	517	-5%
Industrial products	237	185	331	40%	79%	258	29%
Consumer durables	196	121	248	26%	105%	138	80%
Others	1	(34)	120	11860%	-449%	-	
Total segmental PBIT	**2,025**	**1,563**	**2,495**	**23%**	**60%**	**2,043**	22%
Unallocated expense	12	9	3.60			-	
Reported EBIT	2,013	1,555	2,491	24%	60%	2,043	22%
EBIT Margin (%)							
Plastic Piping Systems	14%	10%	16%	132bps	555bps	13%	273bps
Packaging products	21%	19%	20%	-74bps	76bps	21%	-100bps
Industrial products	14%	10%	13%	-150bps	337bps	13%	-5bps
Consumer durables	24%	13%	26%	194bps	1273bps	14%	1196bps
Others	0%	-40%	0.3	2638bps	6653bps		
Total PBIT Margin Adj. (%)	16%	12%	17%	124bps	477bps	14%	247bps

Source: Company, Ambit Capital research

Balance sheet

Particulars (Rs mn)	FY16	FY17	FY18	FY19E	FY20E
Total Net worth	13,153	16,957	19,759	21,937	24,596
Loans	4,128	3,709	1,719	1,269	1,269
Deferred Tax Liability	1,053	1,163	1,163	1,163	1,163
Sources of funds	**20,818**	**21,829**	**22,641**	**24,369**	**27,028**
Net block	11,847	12,633	13,582	14,694	15,689
Capital work-in-progress	675	459	459	459	459
Investments	1,262	1,972	1,972	1,972	1,972
Cash and bank balances	289	850	2,344	3,946	5,584
Sundry debtors	2,362	2,753	4,490	5,268	6,231
Inventories	5,586	7,769	4,465	5,110	5,868
Loans and advances	2,130	15	2,513	2,949	3,488
Other Current Assets	20	1,723	1,723	1,723	1,723
Total Current Assets	10,388	13,110	15,535	18,996	22,894
Current liabilities & provisions	5,838	6,819	9,382	12,226	14,461
Net current assets	4,550	6,291	6,154	6,770	8,433
Application of funds	**20,818**	**21,829**	**22,641**	**24,369**	**27,028**

Source: Company, Ambit Capital research; Note: FY15 ends in June, rest March ending

Income statement

Particulars (Rs mn)	FY16	FY17	FY18	FY19E	FY20E
Operating Income	29,748	44,623	49,663	58,271	68,918
Reported EBITDA	4,611	7,619	7,871	9,188	11,026
Plastics EBITDA	4,611	7,619	7,919	9,188	11,026
Plastics EBITDA margin	15.5%	17.1%	15.9%	15.8%	16.0%
Net depreciation / amortisation	1,046	1,543	1,672	1,908	2,125
EBIT	3,566	6,076	6,199	7,280	8,901
Interest Expense/(income)	276	303	219	(26)	(127)
PBT	3,300	5,825	6,028	7,355	9,081
Share of associates	167	537	347	357	368
Consolidated PAT	2,395	4,412	4,349	5,248	6,406
Reported Consolidated PAT	2,212	4,304	4,317	5,248	6,406
Consolidated EPS (Rs.)	18.9	34.7	34.2	41.3	50.4

Source: Company, Ambit Capital research; Note: FY16 is a 9 month period

Cash flow statement

Particulars (Rs mn)	FY16	FY17E	FY18E	FY19E	FY20E
PBT	3,300	5,825	6,028	7,355	9,081
Depreciation	1,046	1,543	1,672	1,908	2,125
Interest expense/ (income)	276	283	219	(26)	(127)
Direct taxes paid	(1,313)	(1,705)	(2,057)	(2,464)	(3,042)
CFO (before exceptional)	**2,985**	**4,650**	**6,449**	**6,512**	**7,650**
CFO	**2,985**	**4,650**	**6,449**	**6,512**	**7,650**
Purchase of fixed assets	(2,334)	(2,099)	(2,620)	(3,020)	(3,120)
CFI	**(2,199)**	**(2,022)**	**(2,573)**	**(2,970)**	**(3,068)**
Net borrowings	200	(1,331)	(1,990)	(450)	-
Dividends paid	(2,217)	(459)	(173)	(1,515)	(3,070)
CFF	**(2,320)**	**(2,104)**	**(2,383)**	**(1,939)**	**(2,944)**
Net Cash	(1,534)	524	1,494	1,602	1,638
Free cash flow	**650**	**2,551**	**3,829**	**3,492**	**4,530**

Source: Company, Ambit Capital research; Note: FY16 is a 9 month period

Ratio analysis / Valuation parameters

Particulars	FY16	FY17E	FY18E	FY19E	FY20E
Net debt/Equity	0.3	0.2	(0.0)	(0.1)	(0.2)
Working capital turnover (x)	7.7	8.1	8.9	13.7	18.2
Gross block turnover (x)	1.7	2.2	2.2	2.5	2.7
Post-tax RoCE	22.1%	20.1%	18.5%	20.6%	23.0%
Pre-tax RoCE	29.0%	30.3%	27.9%	31.0%	34.6%
ROE	19.0%	29.3%	23.7%	25.2%	27.5%
P/E (x)	70.5	38.3	38.8	32.2	26.3
P/B (x)	12.8	10.0	8.5	7.7	6.9
EV/EBITDA (x)	26.3	15.8	14.8	12.5	10.2

Source: Company, Ambit Capital research

Rallis India

SELL

Another weak quarter

Result Update

Rallis' 4QFY18 results were weak with EBITDA/PAT substantially below our/consensus estimates. While sales grew 6% YoY, EBITDA/PAT declined 19%/37% YoY. Agrochemicals growth of ~6% was healthy though gross margins contracted by ~110bps due to RM pricing pressure and limited ability to take price hike amidst a weak season. For FY18, right reflection of numbers due to seasonality, sales/EBITDA grew 8%/0% while PBT declined 3% YoY; should lag peers. We expected flat EBITDA for 4Q given mixture of increased revenue realisations and dip in gross margins but that doesn't seem to have played out. We don't see any reason to hold the stock due to expensive valuation of ~20x FY19 EPS given no growth in EBITDA over FY14-FY18. We expect ~12% cut on our FY19 estimates which we will do post analyst meet on Monday. We reiterate our SELL stance as we believe Rallis will face challenges, such as a) seeds portfolio remaining a low-margin business; b) lagging revenue growth in the past is now accompanied with lower margins versus peers; c) exports positioning to play both high-end CSM and generics manufacturing is a confused positioning.

Stock Information

Bloomberg Code:	RALI IN
CMP (Rs):	234
TP (Rs):	205
Mcap (Rs bn/US$ bn):	45.5/0.7
3M ADV (Rs mn/US$ mn):	66.8/1.0

Stock Performance (%)

	1M	3M	12M	YTD
Absolute	7	(6)	(2)	(12)
Rel. to Sensex	2	(3)	(18)	(14)

Source: Bloomberg, Ambit Capital research

Ambit Estimates (Rs mn)

	FY18	FY19E	FY20E
Revenues	17,909	20,296	22,525
EBITDA	2,630	3,533	3,989
Adj EPS (Rs)	8.6	11.9	13.4

Source: Bloomberg, Ambit Capital research

Results overview

Standalone results - weaker as compared to our expectations

Rallies' 4QFY18 standalone results were weak as compared to our expectations. Standalone revenue grew 6% YoY to Rs3.5bn, ~3% lower than our estimate. Standalone gross margin at ~42.8% (down ~110bps YoY) was ~80bps higher than our estimate. Adding to this, 'Employee cost' and 'Other expenses' have increased ~15% and ~14% YoY respectively. Thus, the standalone EBITDA margin at ~12.2% (~318bps lower YoY) was ~63bps below our estimate and standalone absolute EBITDA at Rs0.4bn (down ~16% YoY) was ~8% below our estimate. PBT at Rs0.3bn was also ~11% below our estimate. A higher-than-expected tax rate (at ~26.6% against our expectation of ~20%) resulted in PAT (down ~21% YoY) being ~18% below our estimate.

Though increase in prices of raw materials (due to capacity shifts in China) has not impacted much unlike 3QFY18, yet substantial increase in employee cost and other expenses has resulted in a sharp decrease in operating profit.

Subsidiaries (mainly Metahelix) – back to its previous levels of losses

Metahelix revenues at Rs200mn (up ~8% YoY) were ~2% above our estimate. However, absolute EBITDA loss of Rs91mn (down ~2% YoY) was higher than our estimate of Rs43mn loss. Subsidiaries' PAT at negative Rs58mn (down ~374% YoY) was ~48% below of our estimate.

Consolidated performance – substantially below our estimate

Consolidated revenue of Rs3.7bn (up ~6% YoY) was ~3% below our estimate. Consolidated gross margin of ~45.6% (up 130bps YoY) was in line with our estimate. However, consolidated EBITDA margin of ~9.1% (down ~289bps YoY) was ~196bps below our expectation on account of higher 'employee cost' (~15% higher YoY). Thus, consolidated absolute EBITDA of Rs0.3bn (down ~19% YoY) was ~20% below our expectation. The worse EBITDA performance flow through PBT, which at Rs0.3bn (down ~20% YoY) was ~25% below our estimate. Consolidated PAT of Rs196mn was ~28% lower than our estimate due to lower EBITDA margins.

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Management's commentary is like 'Pollyanna Story'

Management's commentary highlights volumes growth as main contributor towards modest revenue growth. However, no numbers on volumes were being provided by the management. The company continues to face challenges due to increased raw materials prices and low pricing power. Management expects new launches in FY18 viz. Odis (Insecticides), Cenator (Fungicide for paddy) and Pulito (fungicide for fruits & vegetables) along with some current prominent brands like Applaud to be key growth drivers in coming years.

Where do we go from here?

We think there was a pressure of higher technical ingredient prices but the company seems to have managed it relatively well this quarter (unlike 3QFY18). However, there is spurt in 'employee expenses' and 'other expenses' which require clarity from the management, if there are any significant developments on this front. We will get more clarity on this post analyst meet. The Metahelix business disappointed yet again. Also, agrochemical markets have been facing challenges over the last few years which along with rising competitiveness have led to flat EBITDA for Rallis over FY14-18 despite forays into seeds, plant growth nutrients and contract manufacturing. We think that Rallis' execution can become much better in light of relative market-share losses over FY14-18. We reiterate our SELL stance on the stock. We expect 10-15% earnings downgrades for FY19 which we will do after FY18 analyst meet scheduled at 3pm on 30th April 2018.

Exhibit 1: 4QFY18 Standalone results snapshot

(Rs mn)	4QFY18A	4QFY18E	Divergence	4QFY17A	YoY	3QFY18A	QoQ	FY18A	FY17A	YoY
Total Operating Income	**3,491**	**3,604**	**-3%**	**3,283**	**6%**	**3,573**	**-2%**	**14,984**	**13,857**	**8%**
Cost of Materials	1,996	2,090	-4%	1,842	8%	2,066	-3%	**8,670**	**7,960**	9%
As % of sales	*57.2%*	*58%*	*(81)*	*56%*	*111*	*58%*	*(62)*	*57.9%*	*57%*	*42*
Gross profit	**1,494**	**1,514**	**-1%**	**1,442**	**4%**	**1,507**	**-1%**	**6,314**	**5,897**	**7%**
Gross margin	***42.8%***	***42%***	***81***	***43.9%***	***(111)***	***42%***	***62***	***42.1%***	***43%***	***(42)***
Employee Expenses	325	300	8%	282	15%	296	10%	**1,257**	**1,140**	10%
As % of sales	*9.3%*	*8.3%*	*99*	*8.6%*	*73*	*8.3%*	*104*	*8.4%*	*8.2%*	*16*
Other Expenses	742	750	-1%	654	14%	744	0%	**2,796**	**2,404**	16%
As % of sales	*21.3%*	*20.8%*	*45*	*19.9%*	*135*	*20.8%*	*43*	*18.7%*	*17.3%*	*131*
EBITDA	**427**	**464**	**-8%**	**506**	**-16%**	**467**	**-9%**	**2,262**	**2,353**	**-4%**
EBITDA margin	***12.2%***	***12.9%***	***(63)***	***15.4%***	***(318)***	***13.1%***	***(84)***	***15.1%***	***17.0%***	***(188)***
Depreciation	88	100	-12%	107	-18%	104	-16%	406	422	-4%
EBIT	**339**	**364**	**-7%**	**399**	**-15%**	**364**	**-7%**	**1,856**	**1,931**	**-4%**
EBIT Margin	***9.7%***	***10.1%***	***(37)***	***12.2%***	***(244)***	***10.2%***	***(45)***	***12.4%***	***13.9%***	***(155)***
Interest	11	12	-9%	4	148%	11	-4%	33	27	23%
Other Income	17	35	-51%	37	-53%	32	-46%	89	105	-15%
PBT	**346**	**387**	**-11%**	**432**	**-20%**	**384**	**-10%**	**1,913**	**2,009**	**-5%**
PBT Margin	***9.9%***	***10.7%***	***(83)***	***13.1%***	***(324)***	***10.7%***	***(84)***	***12.8%***	***14.5%***	***(174)***
Tax expenses	92	77	19%	109	-16%	53	72%	498	522	-5%
Effective Tax Rate	*26.6%*	*20.0%*	*662*	*25.3%*	*131*	*13.9%*	*1,270*	*26.0%*	*26.0%*	*6*
Adjusted PAT	**254**	**309**	**-18%**	**322**	**-21%**	**330**	**-23%**	**1,415**	**1,488**	**-5%**
Adjusted PAT Margin	***7.3%***	***8.6%***	***(132)***	***9.8%***	***(255)***	***9.2%***	***(198)***	***9.4%***	***10.7%***	***(129)***

Source: Company, Ambit Capital research

Exhibit 2: Subsidiary (mainly Metahelix) results snapshot

(Rs mn)	4QFY18A	4QFY18E	Divergence	4QFY17A	YoY	3QFY18A	QoQ	FY18A	FY17A	YoY
Sales	220	215	2%	205	8%	329	-33%	2,925	2,778	5%
EBITDA	**(91)**	**(43)**	111%	**(89)**	2%	**(92)**	-2%	**368**	**282**	31%
EBITDA Margin	***-41.2%***	***-20.0%***	***(2,119)***	***-43.5%***	***236***	***-28.0%***	***(1,314)***	***12.6%***	***10.1%***	***245***
PAT	**(58)**	**(39)**	48%	**(12)**	374%	**(81)**	-29%	**255**	**245**	4%

Source: Company, Ambit Capital research

Exhibit 3: 4QFY18 Consolidated results snapshot

(Rs mn)	4QFY18A	4QFY18E	Divergence	4QFY17A	YoY	3QFY18A	QoQ	FY18A	FY17A	YoY
Total Operating Income	**3,711**	**3,819**	**-3%**	**3,488**	**6%**	**3,902**	**-5%**	**17,909**	**16,635**	**8%**
Cost of Materials	2,019	2,090	-3%	1,944	4%	2,261	-11%	10,182	9,308	9%
As % of sales	*54%*	*55%*	*(33)*	*56%*	*(133)*	*58%*	*(354)*	*57%*	*56%*	*90*
Gross profit	**1,692**	**1,729**	**-2%**	**1,544**	**10%**	**1,641**	**3%**	**7,728**	**7,327**	**5%**
Gross margin	***45.6%***	***45.3%***	***33***	***44.3%***	***133***	***42.0%***	***354***	***43.1%***	***44.0%***	***(90)***
Employee Expenses	428	300	43%	373	15%	390	10%	1,649	1,477	12%
As % of sales	*11.5%*	*7.9%*	*368*	*10.7%*	*85*	*10.0%*	*155*	*9.2%*	*8.9%*	*33*
Other Expenses	928	1,008	-8%	754	23%	876	6%	3,448	3,215	7%
As % of sales	*25.0%*	*26.4%*	*(139)*	*21.6%*	*337*	*22.5%*	*254*	*19.3%*	*19.3%*	*(7)*
EBITDA	**336**	**421**	**-20%**	**417**	**-19%**	**375**	**-10%**	**2,630**	**2,634**	**0%**
EBITDA margin	***9.1%***	***11.0%***	***(196)***	***12.0%***	***(289)***	***9.6%***	***(55)***	***14.7%***	***15.8%***	***(115)***
Depreciation	100	115	-13%	121	-17%	120	-16%	460	474	-3%
EBIT	**236**	**306**	**-23%**	**297**	**-20%**	**255**	**-8%**	**2,170**	**2,161**	**0%**
EBIT Margin	***6.4%***	***8.0%***	***(165)***	***8.5%***	***(214)***	***6.5%***	***(18)***	***12.1%***	***13.0%***	***(87)***
Interest	12	13	-10%	26	-55%	12	-3%	43	73	-41%
Other Income	28	45	-39%	45	-39%	37	-25%	144	128	12%
PBT	**252**	**338**	**-25%**	**315**	**-20%**	**280**	**-10%**	**2,270**	**2,216**	**2%**
PBT Margin	***6.8%***	***8.8%***	***(206)***	***9.0%***	***(225)***	***7.2%***	***(39)***	***12.7%***	***13.3%***	***(64)***
Tax expenses	56	68	-17%	5	1000%	31	82%	**600**	**483**	24%
Effective Tax Rate	*22.3%*	*20.0%*	*227*	*1.6%*	*2,065*	*11.0%*	*1,128*	*26.4%*	*21.8%*	*462*
Adjusted PAT before MI	**196**	**270**	**-28%**	**310**	**-37%**	**249**	**-21%**	**1,670**	**1,732**	**-4%**
Adjusted PAT Margin	***5.3%***	***7.1%***	***(180)***	***8.9%***	***(361)***	***6.4%***	***(112)***	***9.3%***	***10.4%***	***(109)***
MI	**2**	**-**	-	**1**	**2**	1	43%	**6**	**4**	**54%**
Adjusted PAT after MI	**198**	**270**	-27%	**311**	**-36%**	**251**	-21%	**1,676**	**1,736**	**-3%**
Reported PAT	**198**	**270**	**-27%**	**311**	**-36%**	**251**	**-21%**	**1,676**	**2,975**	**-44%**

Source: Company, Ambit Capital research

Balance Sheet

Year to March (Rs mn)	FY16	FY17	FY18	FY19E	FY20E
Total Networth	8,922	11,116	11,917	13,952	15,779
Loans	898	390	200	390	390
Deferred tax liability (net)	358	498	405	498	498
Total liabilities	**10,178**	**12,004**	**12,523**	**14,840**	**16,667**
Net block	5,644	5,585	5680.8	6,010	6,278
CWIP	405	421	473.1	302	302
Investments (non-current)	281	2,392	956	2,392	2,392
Total Current Assets	8,596	8,886	12876	12,232	14,480
Current liabilities	4,483	4,997	7,159	5,675	6,268
Provisions	266	284	304	421	517
Total Current Liabilities	4,749	5,281	7,463	6,097	6,785
Total assets	**10,177**	**12,003**	**12,523**	**14,839**	**16,667**

Source: Company, Ambit Capital research

Income Statement

Year to March (Rs mn)	FY16	FY17	FY18	FY19E	FY20E
Revenue	**15,291**	**16,635**	**17,909**	**20,296**	**22,525**
Operating expenditure	13,001	14,001	15,279	16,763	18,535
EBITDA	**2,290**	**2,634**	**2,630**	**3,533**	**3,989**
Depreciation	436	474	460	557	619
EBIT	**1,854**	**2,161**	**2,170**	**2,975**	**3,370**
Interest expenditure	136	73	43	35	35
Non-operating income	143	128	144	137	151
Adjusted PBT	**1,860**	**3,799**	**2,270**	**3,078**	**3,486**
Tax	390	483	600	769	871
Adjusted PAT	**1,471**	**1,732**	**1,670**	**2,308**	**2,614**
EPS (Rs)	**7.4**	**8.9**	**8.6**	**11.9**	**13.4**

Source: Company, Ambit Capital research

Cash flow Statement

Year to March (Rs mn)	FY16	FY17	FY18E	FY19E	FY20E
PBT	1,857	3,799	2,331	3,078	3,486
Depreciation	436	473	502	557	619
Tax	(406)	(855)	(583)	(769)	(871)
(Incr)/decr in net w. capital	307	538	(50)	(664)	(335)
Cash flow from operations	**2,321**	**3,889**	**2,106**	**2,099**	**2,782**
Capex (net)	(724)	(467)	(700)	(785)	(887)
(Incr)/decr in investments	(39)	(2,111)	-	-	-
Other income (expenditure)	(706)	72	130	137	151
Cash flow from investments	**(1,469)**	**(2,701)**	**(570)**	**(648)**	**(736)**
Net borrowings	(103)	(151)	-	-	-
Dividend paid	(350)	(584)	(526)	(695)	(787)
Cash flow from financing	**(588)**	**(802)**	**(561)**	**(730)**	**(822)**
Net change in cash	**264**	**386**	**975**	**722**	**1,225**
Free cash flow	**1,597**	**3,422**	**1,406**	**1,314**	**1,895**
Opening cash balance	15	279	170	1,145	1,866
Closing cash balance	**279**	**170**	**1,145**	**1,866**	**3,091**

Source: Company, Ambit Capital research

Key ratios and valuation

Year to March	FY16	FY17	FY18E	FY19E	FY20E
Revenue growth	-16.1%	9.8%	6.7%	13%	11.0%
EBITDA growth	-17.4%	15.0%	-0.1%	34%	12.9%
Adjusted PAT growth	-8.8%	18.0%	-3.5%	38%	13.3%
EPS norm (dil) growth	-8.8%	18.0%	-3.5%	38%	13.3%
EBITDA margin	15.0%	15.7%	14.7%	17.4%	17.7%
EBIT margin	12.1%	12.9%	12.1%	14.7%	15.0%
Net margin	9.6%	17.7%	9.3%	11.4%	11.6%
RoCE	16.5%	16.8%	12.8%	17.3%	17.3%
RoIC	16.1%	18.6%	18.6%	23.3%	24.8%
RoE	16.8%	17.0%	14.5%	17.6%	17.6%
P/E (x)	32.0	27.0	26.3	19.9	17.6
P/B(x)	5.2	4.1	3.7	3.3	2.9
EV/EBITDA(x)	23.8	20.7	19.9	15.4	13.7
EV/EBIT (x)	29.4	25.2	24.4	18.3	16.2
EV/Sales (x)	3.6	3.2	3.0	2.7	2.4

Source: Company, Ambit Capital research

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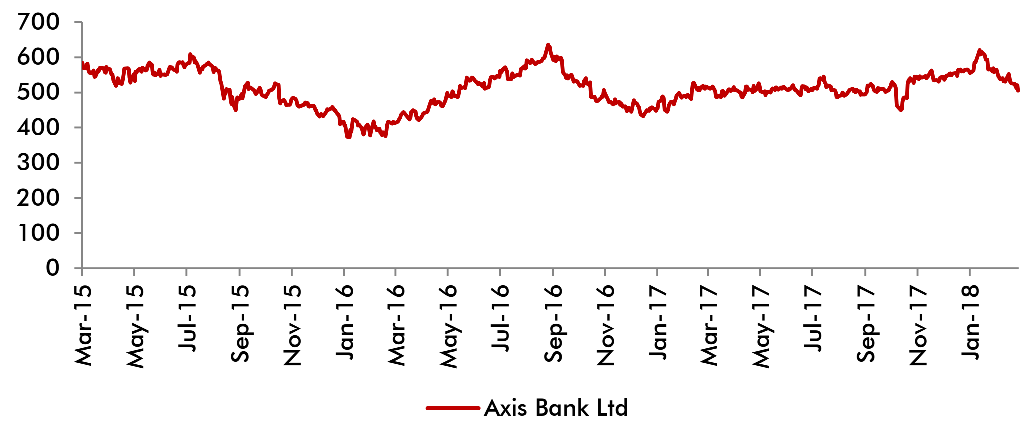

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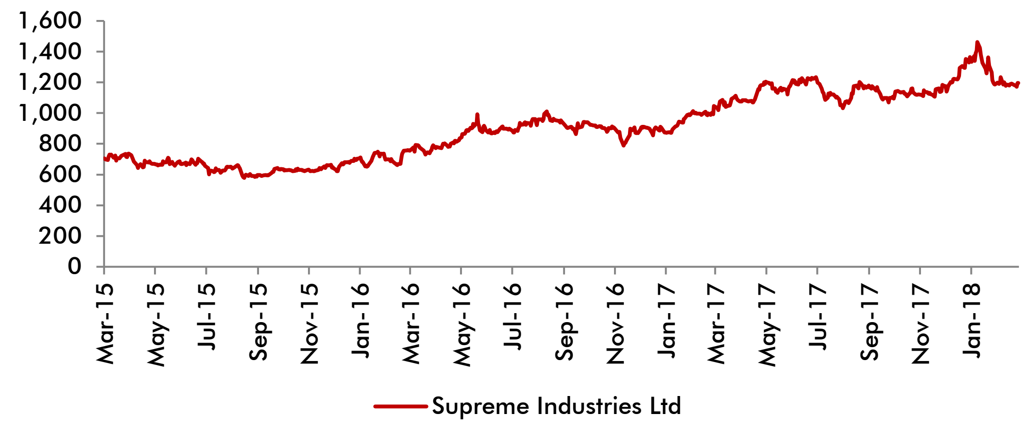

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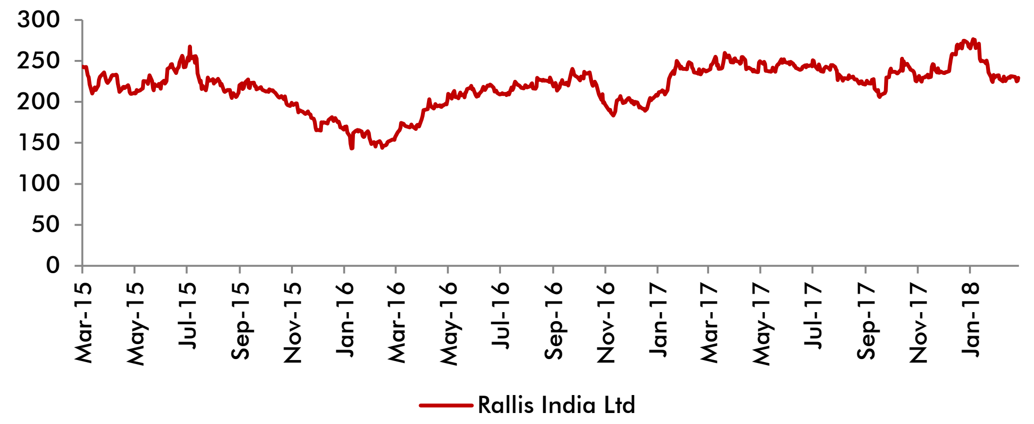

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