April 28, 2016

IDBI capital

COMPANY REPORT

Meghmani Organics Ltd.

Geared up smartly!

BUY

Analyst

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Nifty: 7,980; Sensex: 26,064

CMP	**Rs30**
Target Price	**Rs46**
Potential Upside/Downside	**+53%**

Key Stock Data

Sector	Speciality Chemicals
Bloomberg / Reuters	MEGH IN/MEGH.BO
Shares o/s (mn)	254
Market cap. (Rs mn)	7,620
Market cap. (US$ mn)	115
3-m daily average vol.	346,786

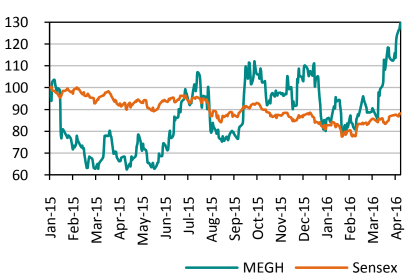
Price Performance

52-week high/low			Rs31/14
	-1m	-3m	-12m
Absolute (%)	51	50	95
Rel to Sensex (%)	46	44	99

Shareholding Pattern (%)

Promoters	50.52
FIIs	1.06
MFs/Banks/FIs	0.05
Public & Others	33.65

Relative to Sensex



Source: Capitaline

Summary

Meghmani Organics Ltd. (MOL), a part of the Meghmani group and well diversified chemical company (pigments, agro-chemical and basic chemical) is entering into new growth orbit post mega capex cycle (FY11-15). After passing through a tough time, MOL is charged up with capacity expansion in high margin Caustic Soda business, focus on branded agro formulation business and scaling up the distribution network in agri concentrated areas in India (17 States). We believe its pan India and international presence (75 Countries) through extensive network along with marquee clienteles (400+ customers) would help to deliver strong financial performance. Furthermore, better capacity utilisation (post relocation of plant), healthy product portfolio (global product registration at various stages) and strengthening position in basic chemical (high margin) business coupled with de-leveraging balance-sheet would accelerate earning pace. Moreover, with no major capex ahead and better working capital management, the visibility of improvement in return ratios and free cash flow persist. We expect consolidated revenue and earning CAGR of 10% & 41% in FY15-18E, respectively. The stock is currently trading at a P/E of 8.3x/6.3x to FY17E/FY18E earnings. Initiate with a BUY (TP Rs46/share; 53% upside).

Investment rationale and outlook

- **Most integrated player; diversified revenue stream**
  MOL, one of the top 3 global player in blue pigment (7% market share) has a strong product portfolio and marquee clients (400+) both in domestic and international market (Overall total export revenues 57%). It has vertically integrated business in pigment segment and strong presence in highly competitive agro-chemical business. After passing through a rough patch, it is set to deliver better financials due to (1) Capacity expansion (high margin)+ Volumes pick up (2) Margin expansion (3) Strong product portfolio and deleveraging balance-sheet.
- **Capacity in place; focus on branded formulation & high margin business**
  MOL is on the right track post mega capex plan (Rs5600mn across all verticals) in last 5 years. It has recently commissioned Caustic Potash facility in Dahej (21,000MT; Capex Rs650 mn with a revenue potential Rs1250mn + 30% EBITDA margin). After the relocation of agrochemical plant (FY12/13) and improving capacity utilisation, it is focusing to increase in distribution network (agrochemical segment) in major agriculture concentrated areas (17 States) and strengthening its branded agro formulation business (targeting revenue from Rs800 mn in FY15 to Rs2500 mn by FY18).
- **Better operating leverage; margins to sustain**
  Being an integrated company (both in pigments and agrochemicals), MOL to witness efficiency in business operations owing to stability of relocated plant, improvement in capacity utilisation and stable/lower RMC. Increasing contribution from high margin basic chemical segment post expansion would support the overall EBITDA margins (21.8% & 22% in FY17E & FY18E, respectively).
- **Major capex phase over; time to encash it**
  Better capacity utilization and debt reduction (Rs1000 mn p.a.) would translate into strong earnings growth. Moreover, with no major capex (Rs1210 mn spread in FY16-18E) and better working capital management [from 126 days (FY12) to 102 days (FY15)], the visibility of improvement in return ratios and free cash flow persist, which would give enough cash cushion to pare its debt.
- **SOTP Valuation: Attractive; initiate with a BUY**
  The stock is currently trading at a P/E of 8.3x/6.3x and EV/EBITDA of 3.9x/3.1x to FY17E/FY18E earnings. Given the multifold improvement (across all parameters), we believe the stock should command better valuation (broadly in-line with industry peers). We have valued the company on a SOTP basis by assigning EV/EBITDA multiple to its three segments, arriving at a TP of Rs46/share (53% upside). Hence, we initiate coverage on the company with a **BUY** recommendation.

Table: Financial snapshot (Consolidated) **(Rs mn)**

Year	Revenue	EBITDA	EBITDA (%)	Adj. PAT	EPS (Rs)	P/E (x)	EV/EBITDA (x)	RoE (%)	RoCE (%)
FY15	12,942	2,031	15.7	441	1.7	17.7	7.1	8.2	9.1
FY16E	13,338	2,894	21.7	806	3.2	9.7	4.7	14.0	15.6
FY17E	15,138	3,300	21.8	941	3.7	8.3	3.9	14.9	18.3
FY18E	17,300	3,806	22.0	1,240	4.9	6.3	3.1	17.6	21.8

Source: Company; IDBI Capital Research

Investment Rationale

- **Diversified business model; Geared up smartly post Capex**

Meghmani Organics limited has a well diversified revenue stream, operating in three different segments in India. It has wide geographic reach, strong product portfolio, healthy supply-chain and marquee clients across domestic and international market. Despite of vertically integrated business in pigment segment and strong presence in highly competitive agro-chemical business, it has passed through tough time in recent years attributed to (1) Major Capex cycle (spent Rs5,600 mn in last 5 years) (2) Lower capacity utilization (3) Relocation of plant in FY12/FY13 (4) Higher debt burden. However, the company's effort to bring the business operations on track through various initiatives (improving utilisation across verticals, capacity expansion, widening distribution channels and deleveraging the balance-sheet) would start bearing fruits in the coming years. It has now geared up smartly to showcase better financial performance.

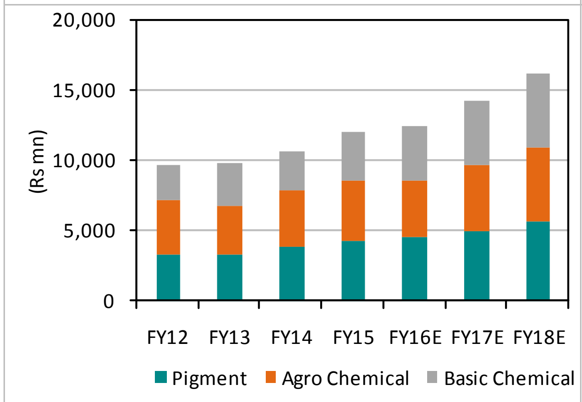
Table : Business Segments

Particulars (FY15)	Pigment	Agro-chemicals	Basic chemicals
Incorporation	1986	1995	2009
Market share (%)	7%	-	-
Capacity (MT)	31,140	19,200	1,54,100
Utilisation rate (%)	51%	60%	93%
End users	Ink, Paint, Plastic mfr.	Pesticides manufacturer, formulators, Institutional clients, farmers	Pulp, Paper, Soap & detergents, Textile, Paint, Coating
Revenue Mix (%)	33%	35%	28%
EBITDA margin (%)	10%	13%	31%
Domestic revenue (%)	20%	30%	100%
Export revenue (%)	80%	70%	-
Key competitors	Sudarshan Chemical, Asahi Songwon	Danuka, PI Ind, Rallis India, UPL	Gujarat Alkalies, DCM Shriram
Revenue CAGR (FY12-15)	9%	3%	12%

- **Sufficient capacity in place; Riding on strong recovery path**

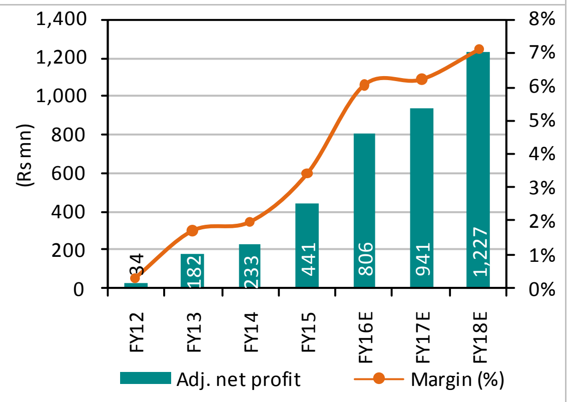
MOL is set to deliver better financial performance on the back of (1) Capacity expansion high margin business + improving capacity utilisation (2) Debt repayment (3) Sustainable margin profile and (4) Strong product folio (400 new product registrations in pipeline in the next 1-3 years). Under the Agrochemical segment, it is targeting to increase the distribution network across major agriculture concentrated areas (17 states) to strengthen branded formulation business while it has set up the new facility of Caustic Potash plant at Dahej (under Basic Chemical segment) by spending Rs650 mn, which has started operating from April 2016. With no major capex needs (Rs1,210 mn in FY16E-18E v/s Rs3550 mn in FY12-15) and focus on debt repayment (Rs1,000 mn+ p.a.), MOL is well poised to ride on the strong recovery path in the coming years. We expect revenue and earning CAGR of 10% and 41% in FY15-18E, respectively.

Figure: Revenue growth



Source: Company; IDBI Capital Research

Figure: PAT growth

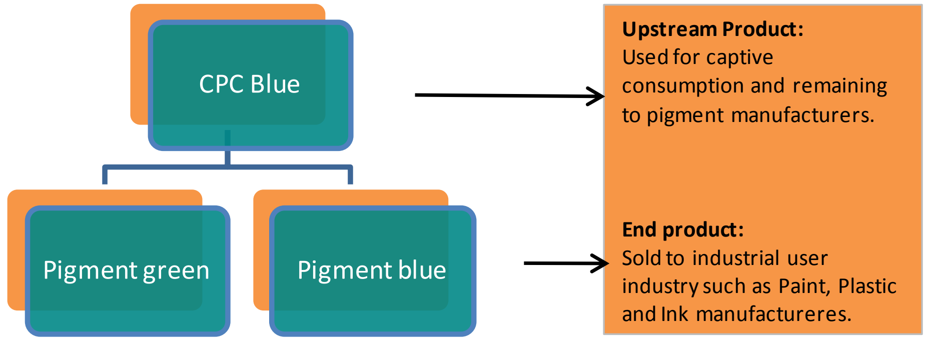


Source: Company; IDBI Capital Research

- **Pigment segment: Uniquely placed; Better capacity utilisation to aid growth**

MOL is the 3rd largest manufacturer of blue pigment in the world with 7% global market share, manufacturing CPC blue, pigment blue and pigment green. It is fully integrated player both in vertically and horizontally, gives it a competitive edge over peers (avail RM at reasonable costs). One interesting fact that it is generating major revenues (80% of pigment revenues) from export market through the strong distribution channel. It's high quality products and ability to manufacture customized products translates into 90% of repeated orders from their existing clientele (20 years long standing relationship). MOL has strong International and domestic customer base in the Ink, Plastics segment. This segment contributed 33% of overall revenue in FY15 (grew by 9% CAGR in FY12-15).

Diagram: Pigment - product chain



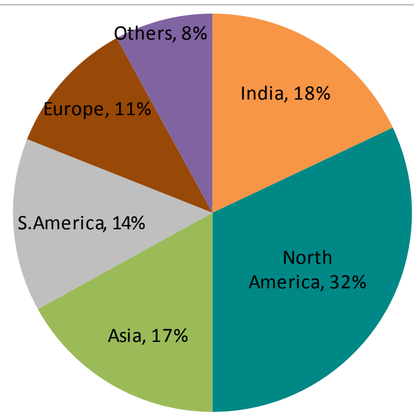
Source: Company; IDBI Capital Research

Table: Pigment (FY15) – Plant location, capacity and product range

Location	Year	Capacity (MT)	Utilisation rate (%)	Products
Vatva	1986	2,940	70	Pigment Green 7 (PG 7), PG 36 and additives for Ink & Paint
Panoli	1996	17,400	53	CPC Blue, Alpha Blue, Beta Blue
Dahej SEZ	2013	10,800	42	CPC Blue, Alpha Blue, Beta Blue

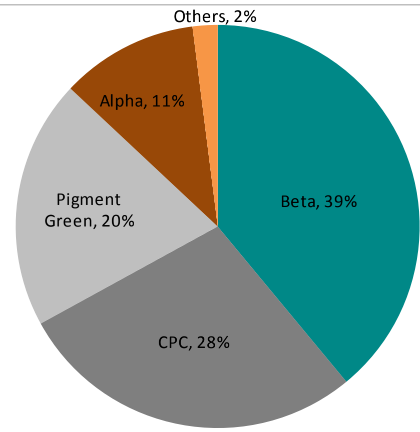
Source: Company; IDBI Capital Research

Figure: Revenue by country (FY15)



Source: Company; IDBI Capital Research

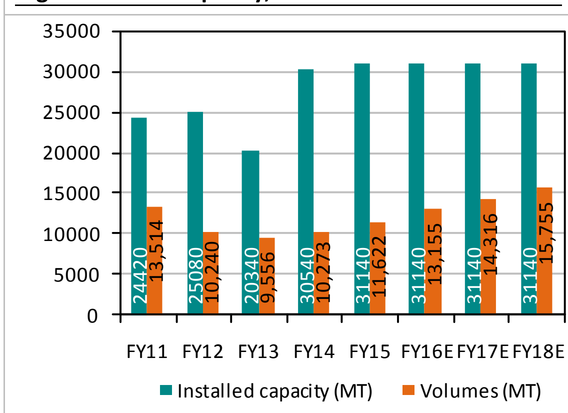
Figure: Revenue by product (FY15)



Source: Company; IDBI Capital Research

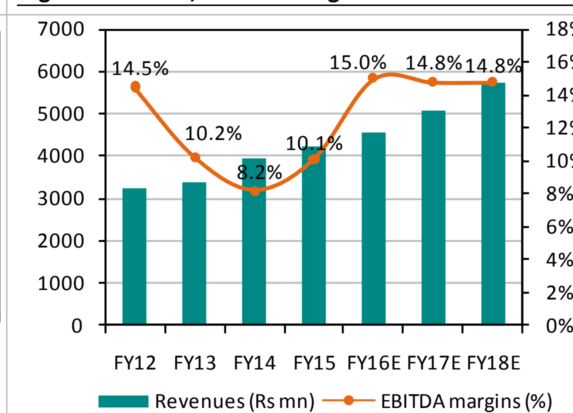
After the Greenfield expansion in Dahej during 2014 (added 10,800MT), the total pigment capacity stands at 31,140MT. The company is now focusing on high margin paint & plastic market by improving product-mix and speciality pigment products for International market. It is also in the preliminary talks with few international players to supply specialised pigment products on a long term basis (waiting for product approval) and eyeing untapped markets such as Japan and other countries. In addition, the recent shutdown of factories in China (a largest market of Speciality chemical business) would help Indian players including Meghmani to increase export business. Being one of the top leader in Indian pigment market (CPC Blue and green pigments) with strong international presence and strong client lists, we believe the company to see better days ahead in (capacity utilisation and better demand recovery) volumes and revenue growth (11% CAGR in FY15-FY18E).

Figure: Overall capacity, Sales volumes



Source: Company; IDBI Capital Research

Figure: Revenue, EBITDA margin



Source: Company; IDBI Capital Research

Table: Pigment (FY15) – Indian Peer matrix

Particulars (Rs mn)	Capacity (tonnes)	Revenues	Revenue mix (%)	EBITDA (%)	ROCE (%)
Meghmani*	31,140	4,318	33	10.1	9.1
Sudarshan Chemical	NA	9,628	89	12.2	23.3
Asahi Songwon	11,400	2,395	100	13.4	12.2

*Source: Company; Annual Report; IDBI Capital Research;*Segmental; NA- Not Available*

Pigment Industry

Global pigment industry (Organic, Inorganic, Speciality) is likely to grow by 4.5% (FY13-18E) to US$14.7 bn with an estimated volumes of 4.4 mn tonnes while Asia-pacific market, which is growing fastest, would reach US$6.4 bn by 2018 (contributes 45% of world market). The rising demand for speciality pigments, the growing market for coatings and paints, and the growth of the construction materials market would drive the pigment demand. Pigments play a vital role in the global colorants market.

Table: Type of pigments and categories

Types	Categories
Organic pigments	Quinacridone, Phthalocyanine, and Azo
Inorganic pigments	Chromium oxide, Carbon black, Cadmium pigments, Iron oxide pigments, and Titanium dioxide
Specialty pigments	Thermochromic pigments, fluorescent pigments, metallic pigments, and light interference pigments

Source: Company; IDBI Capital Research

Diagram: Segmental information and usages

Organic
- Heat stability and light fastness are good
- Used in Printing Inks, Coatings, Plastics, Textiles, Leather Paste

Inorganic
- Less fastness properties & heat stability is less around 200 degree C.
- Used in Paints & Plastic Industry

Speciality
- Coating segment (Automotive paints) - Light fastness are superior
- Fibre grade plastic application where the heat stability and dispersion properties should be superior then normal pigments.

Source: Company; Industry Report, TMR; IDBI Capital Research

Most manufacturers in the global pigments market are focusing more towards developing eco-friendly and safe chemicals. Some of the trends witnessed in dyes and pigments market are shifting of the manufacturing facilities from U.S. and Europe to India, China.

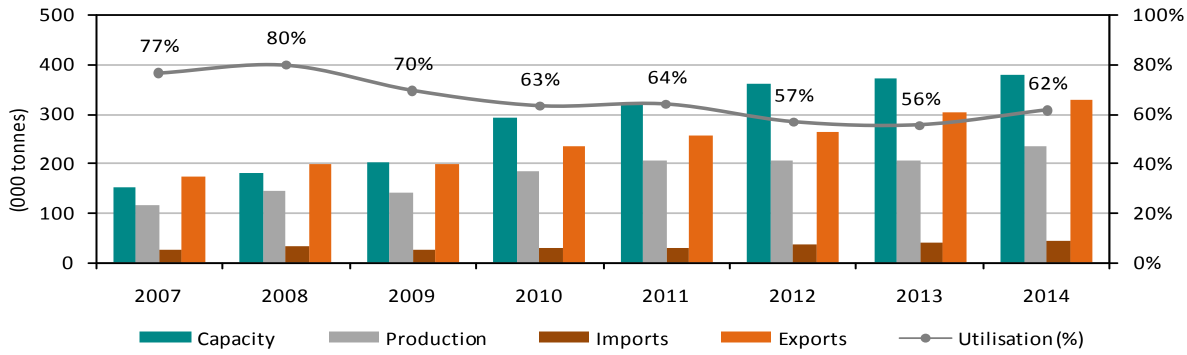
Asia-Pacific accounts for almost half of global consumption of pigments already and is expected to increase its share of the market even further. This region will continue to be the growth motor of the pigments industry, as China and India in particular are substantially increasing demand for pigments. Eastern Europe, the Middle East and South America will see demand rise by more than 3% p.a. each as well and thus contribute to the positive development of the pigment industry. The rather saturated markets in Western Europe and North America will slowly return onto a growth path after they suffered losses in the past couple of years.

The major driving factors of colorants market are growth in end user industries, rising demand for high performance pigments (HPP), and rising preference towards environment-friendly products. Pigments have a large number of applications ranging from paints & coatings, textile, construction, printing inks, and plastics. The paints & coatings industry is recording significant growth due to growing infrastructure while the demand for printing ink is driven by various factors such as technological developments and increasing demand for digital inks.

India

The Indian pigments industry has transformed from being import dependent to an export driven industry. Developed countries are now focusing on sourcing pigments from cost-effective Asian markets, owing to stringent measures taken on environmental issues. Exports have grown in double digit over the last few years. Indian pigment industry is growing at a healthy rate. The printing Inks, plastic and paint industry consumes over 90% of pigments. The Indian paints & coating industry (a major pigment user) is expected to grow by 5.1% in FY13-18E while printing Ink market has seen a 7.5% CAGR in the last decade. In India, it is the organics which are growing the fastest and, traditionally, India has dominated in the green and blue colour space or the copper pthalocynines. India is clearly the dominant player in the organic green pigments and a serious player in the blue pigments.

Figure: Indian – dyes & pigment industry at a glance



Source: Company; MOF; IDBI Capital Research

Table: Product-wise split of capacity between organized & unorganized market **(MT)**

Types of Pigments manufactured in India*	Organised	Unorganised	Total
Phthalos			
Blue 15	17,000	8,800	25,800
Green 7	8,000	4,700	12,700
CPC Blue	28,000	9,000	37,000
Azos	9,000	6,000	15,000
Pigments Violet 23	1,000	-	1,000

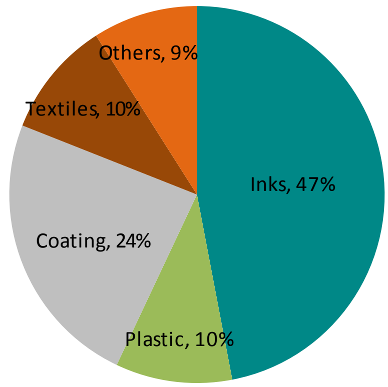
*Source: Industry; IDBI Capital Research,*Approx. figures from various sources*

Inorganic pigments segment is different story. In spite of having one of the world's largest and high quality reserves of limonite (from which one gets titanium dioxide pigment) in the coastal area of Kerala, Andhra and Orissa, the country has failed to take the advantage. India has a reasonable capacity of the carbon black. The country still produces chrome and lead based pigments, which are globally in the sunset phase for ecological reasons.

Specialty pigments market is expected to have fastest growth potential among the global pigments market. Availability of large variety of products and ability to encompass high and unique visual effects is primarily fueling the growth of the specialty pigments market. Specialty pigments are expected to be the most promising product segment, and are estimated to grow at a CAGR of 6.6% (in Asia pacific v/s 4.7% globally) from 2013 to 2018. Under growing regulatory pressure, specialty and organic pigments are being increasingly investigated for substitution potential over their inorganic counterparts.

End user Industry and demand drivers: The main end users of pigments in India are printing inks, plastics, rubber, paints and coatings. High performance pigments (HPP) and special effect pigments, such as metallic and pearlescent, are used as automotive coatings and are currently a nascent market in India.

Figure: Pigment - End user Industry in India



Source: Company; Indian Paint Industry 2015; IDBI Capital Research

- **Competitive Intensity**

There are few players in the pigment industry enjoying higher market share, strong brand image. Being amongst, Sudarshan Chemical is the largest pigment supplier (35% market share including Azo), among both Indian and MNC's, followed by Meghmani Organics Limited, Asahi Songwon.

Table: Presence of players across various pigment products

Type of Pigments	Major players	Products
Phthalo Blue	Asahi Songwon	Blue Finished
	Clariant	Green
	Heubach	Phthal Blue Crude
	Ishan Dyes	
	Meghmani	
	Sudarshan	
Azo Pigments	Clariant	Greenish Yellow
	Heubach	Yellow
	Micro/Huber Inks	Orange
	Pidilite	Red
	Sudarshan	Bluish red
Violet 23	Alpanil	Violet
	Meghmani unichem	
	Ami	
	Dipen	
	Heubach	
	Pidilite	

Source: Company; Industry; IDBI Capital Research

- **Agro chemical business: Vertically integrated; High focus on branded formulation business**

MOL is well positioned in highly competitive and regulated agrochemical market with a significant presence in branded agrochemical formulation business (few brands - Megastar, Megaban, Megacyper, Synergy etc). It manufactures pesticide intermediates as well as agro formulations (bulk & branded) for various institutional clients and end users. It has over 215 export registration, 247 CIB registrations and 27 registered trademarks and around 400 registrations are under pipeline (registration takes 1-3 years) as on date. It enjoys competitive advantage in highly regulated market owing to higher number of registrations and trademarks. It generates 70% of revenues from export market while it has presence in 17 States in India, particularly Gujarat, Karnataka, Rajasthan, M.P., A.P., Punjab etc.

Table: Product categories & end users

Categories	End users
Pesticide intermediates	Technical grade pesticides manufacturers
Technical grade	Pesticides formulators
Pesticide formulations	Institutional customers , Retailers, Dealers, Farmers

Source: Company; IDBI Capital Research

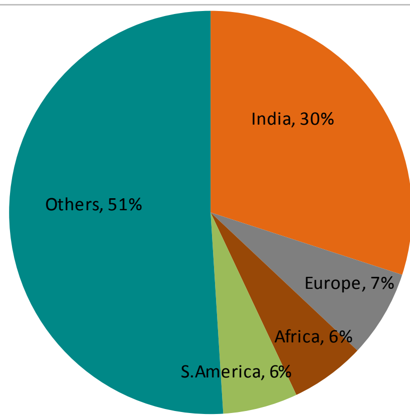
Table: Plant location, Capacity and Product range

Location	Year	Capacity (MT)	Utilisation rate (%)	Products
Ankaleshwar	2003	6,660	61	Chlorpriphos and intermediates
Dahej	2010	8,940	58	Cypermethrin, MPB, Profenophos,2-4D
Panoli	2009	3,600	65	Agro formulations

Source: Company; IDBI Capital Research

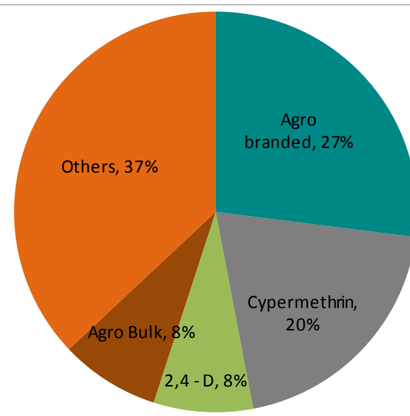
In recent years, the performance was muted due to relocation of Chharodi plant to Dahej in FY12/FY13 (due to intervention of Pollution Control Board) and lower capacity utilisation resulted in to 3% revenue CAGR in FY12-15). However, post stabilization of new plant, pick up in capacity utilization resulted into double-digit revenue growth in FY14 & FY15. At the same time, EBITDA margin improved from 9.2% (FY12) to 12.8% in FY15.

Figure: Revenue by country (FY15)



Source: Company; IDBI Capital Research

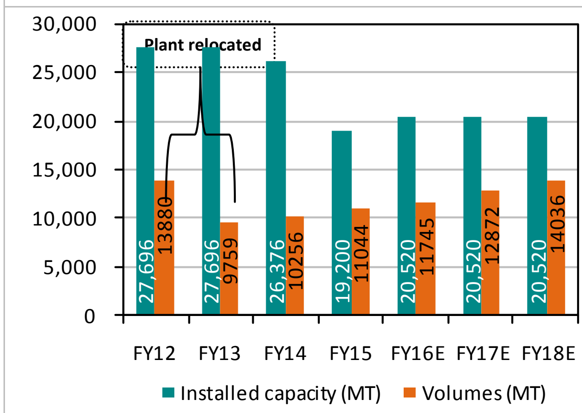
Figure: Revenue by product (FY15)



Source: Company; IDBI Capital Research

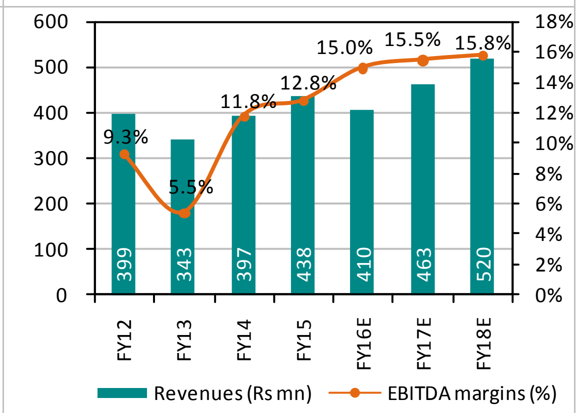
Being a vertically integrated player, it is now focusing to increase the exports and opportunities under CRAMS segment. Under its formulation business, it has established significant presence through 1,000 stockiest and strong distribution network and further aims to add 2,500 dealers' network in branded formulation segment to achieve revenue of Rs2,500 mn in the next 2-3 years (Current revenue Rs800 mn; EBITDA margin over 15%). Improving capacity utilisation, healthy product-mix and the anticipation of better monsoon arrival (after two consecutive droughts), we believe volumes to pick up at a faster rate (8% CAGR in FY15-18E v/s negative 7% in FY12-15), which would drive revenue growth.

Figure: Overall capacity, Sales volumes



Source: Company; IDBI Capital Research

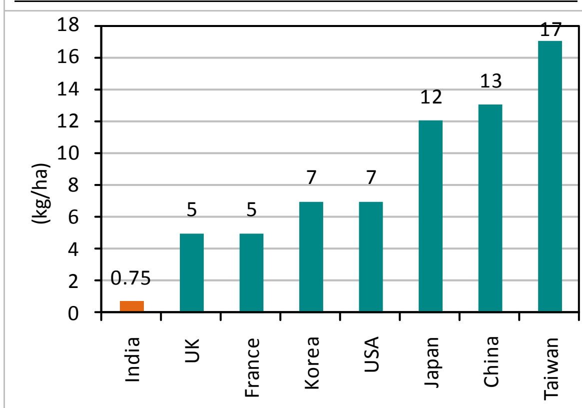
Figure: Revenue, EBITDA margin



Source: Company; IDBI Capital Research

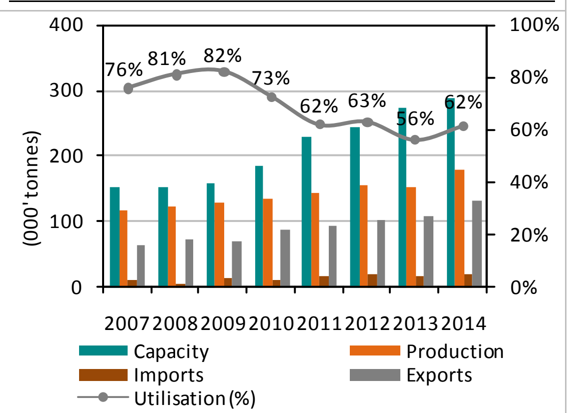
Agro-chemical Industry: India is the 4th largest producer globally, generating 50% of revenue from export revenue. The Indian crop protection industry is expected to grow at a 12% CAGR to US$7.5 bn by 2019 while the export contribution is likely to increase over 60% over the same period (at a CAGR growth of 16%). Despite the higher agriculture concentrated areas, the per capital consumption of pesticides is just 0.75 kg/ha in India as against UK (5kg/ha), USA (7k/ha), Taiwan (17kg/ha) and China (13k/ha).

Figure: Low pesticides penetration in India



Source: Company; IDBI Capital Research

Figure: Pesticides (Tech.) (in 000' tonnes)



Source: Company; IDBI Capital Research

Table: Peers group comparison

Name	Capacity (MT)	Utilisation rate (FY15)	Distributors	Dealers	Domestic revenue (%)	Export revenue (%)
Meghmani Organics*	20,520	60%	-	2,500	30%	70%
Dhanuka	Around 57,000 (KL+Tonne)	70%	8,600	80,000	100	-
PI Industries	NA	NA	8,000	35,000	40	60
Rallis	NA	NA	NA	NA	72	28
Insecticides	17,450 KL 75,600 MT granules 13,800 MT Bulk 16,980 MT powder	80%	5,000	60,000	100	-

*Source: Company; Annual Report; Industry; IDBI Capital Research;*Segmental*

Table: Agrochemicals (FY16E) – Indian Peer matrix (Rs mn)

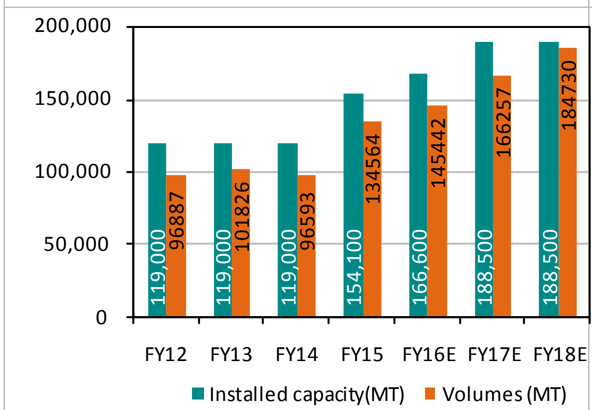
Particulars	Revenues	EBITDA (%)	EPS (Rs)	P/E (x)	EV/EBITDA (x)	RoE (%)	D/E (x)	W.cap days
Meghmani*	4,103	15.0	-	-	-	-	-	-
Dhanuka	8,102	17.3	19.4	31.4	3.7	21.8	0.1	150
PI Ind	21,151	20.7	21.0	29.6	19.5	27.7	0.1	85
UPL	128,773	20.1	29.5	17.5	9.5	19.6	0.5	130
Rallis	16,362	14.3	6.7	28.8	16.8	15.9	0.1	75
Insecticides	9,809	10.5	25.5	17.0	10.5	14.8	1.0	114

Source: Company; Annual Report; Bloomberg; IDBI Capital Research, Segmental*

- **Meghmani Finechem Ltd.: Basic chemicals business – a future growth engine**

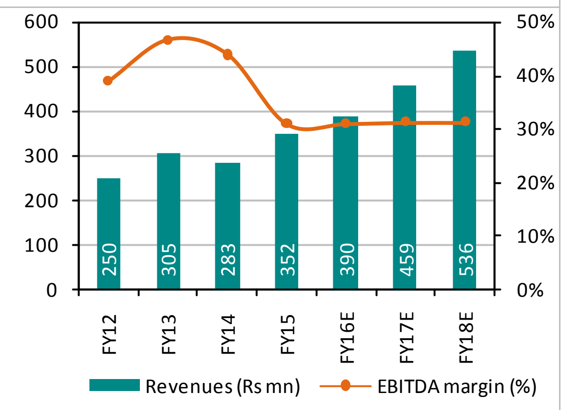
  MOL has the fourth largest capacity of Caustic-Chlorine flakes capacity in India with the advance technology of Asahi Kasei, Japan. With the 1,66,600MT capacity, it manufactures Caustic Soda, Chlorine gas and Hydrogen gas, which it sells to domestic market i.e. Pharmaceuticals, Soaps, detergent, Chemical and Textile Industry. This segment contributed 29% of overall FY15 revenues and registered healthy 31% EBITDA margin for the company. During 2014, it has expanded the capacity of Caustic Chlorine & power plant with an investment of Rs970mn while ramped up the utilization rate gradually, led to 12% revenue CAGR during FY12-15. It has set up the Caustic Potash plant at Dahej (21,000MT with a capex Rs650 mn; Revenue potential Rs1250 mn), which has commissioned during current month (April 2016). The plant is strategically located with proximity to raw materials and end user market. It is expected that the revenue contribution from this segment is likely to spur in the coming years, which would support margin profile to certain extent. We expect volumes and revenues to grow at 11% & 15% during FY15-18E respectively while EBITDA margins to remain over 31%.

Figure: Overall capacity, Sales volumes



Source: Company; IDBI Capital Research

Figure: Revenue, EBITDA margin



Source: Company; IDBI Capital Research

Table: Caustic Soda players (FY15) – Indian Peer matrix (Rs mn)

Particulars	Capacity (Tonnes)	Utilisation rate	Revenue mix	Revenues	EBIT (%)	P/E(x)	EV/EBITDA(x)
Meghmani*	1,54,100	93%	28%	3518	19.3%	-	-
Gujarat Alkalies	4,29,050	89%	46%	8961	NA	5.5	4.2
DCM Shriram	2,85,000	92%	12%	6830	26.1%	10.2	6.7

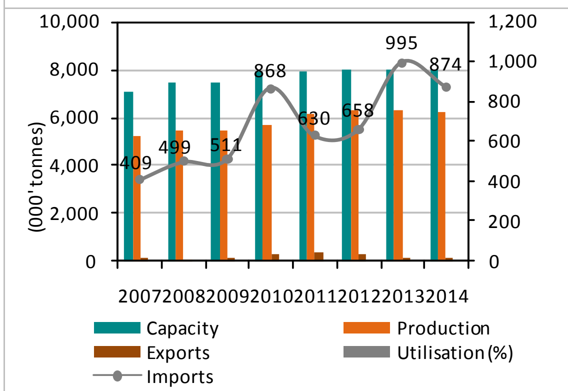
*Source: Company; Annual Report; IDBI Capital Research;*Segmental*

Indian basic chemical Industry

Global Chlor-Alkali industry is expected to grow by 6% CAGR in FY2014-19 (volumes to grow from 193 mn MT to 224mn MT). Asia-Pacific is the largest world market in which China is the leading consumer. Though India is growing at a faster pace with the capacity utilisation rate of 78%, it is still behind China with just 4% of world Caustic Soda capacity and 6% of Soda Ash capacity (v/s China of 35% & 40% respectively). Indian market is highly influenced by Caustic Soda against International market of Chlorine based chemicals. Indian alkali based chemical (Soda Ash+ Caustic Soda+ Chlorine) Industry is expected to grow by 7% CAGR in FY2014-19E.

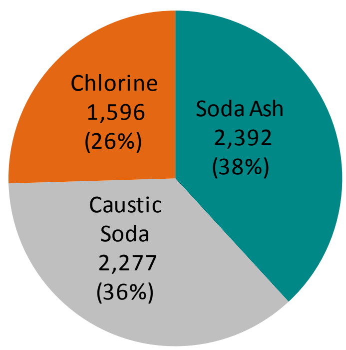
Gujarat is the largest manufacturer of Caustic soda (35% of total capacity). As per the data, India has a nearly 3.43mn tonnes of installed capacity with over 80% utilisation rate (almost fully operated). As the consumption exceeds production limit, 10-12% of required Caustic soda has been imported currently. The largest user industries are Pulp & Paper, Pharma, Alumina, Soaps, detergents and chemical industry.

Figure: Alkali based chemical - matrix



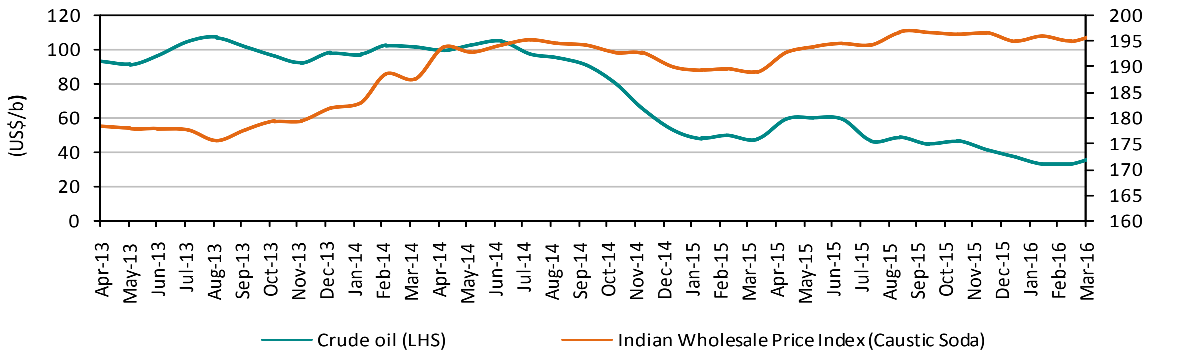
Source: Company; MOF; IDBI Capital Research

Figure: Production mix trend (FY14)



Source: Company; MOF; IDBI Capital Research

Figure: Crude Oil vs Indian Caustic Soda Index



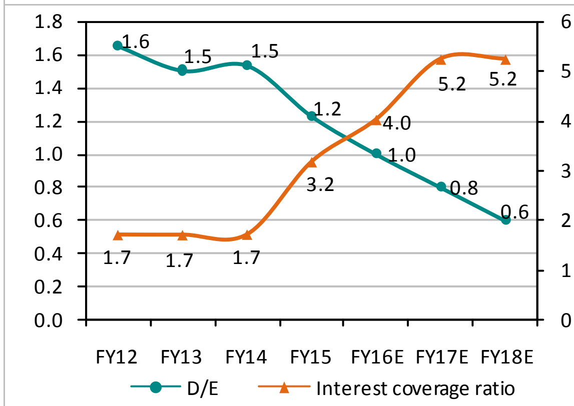
Source: Company; Bloomberg; IDBI Capital Research

- **Strong internal competencies; healthy product pipeline:** MOL is actively engaged in the development of new process technologies for its well equipped state-of-the-art R&D facilities. The focus is on to expand range of specialty products and move towards higher value-added products in the agrochemical by establishing strong supply chain to widen the reach. Moreover, the healthy product folios (400 registrations in pipeline in agrochemical) and continuous product innovation would remain the Key focus area going forward.

- **Deleveraging B/S + Margin expansion = Strong earnings visibility**

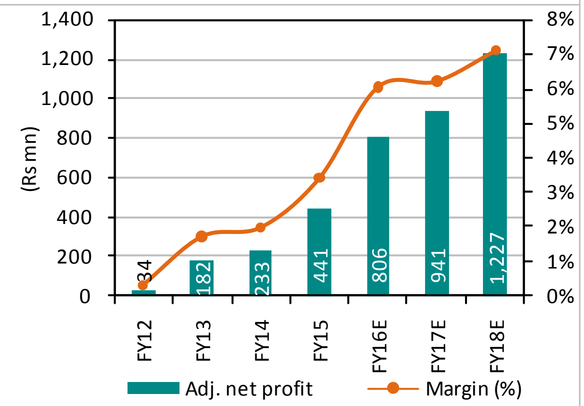
  In recent years, MOL has pass through a rough patch due to (1) Major capex cycle (total capex of Rs3,550 mn in FY12-15) (2) Stressed balance-sheet (3) Lower capacity utilisation. Though MOL was under major capex cycle in recent years, it managed to reduce the debt level (from 1.6x to 1.2x in FY15) and improved the working capital cycle. Going forward, better capacity utilization, low raw material costs and margin expansion along with the further debt reduction (targeting to repay Rs1000mn every year) would lead to a healthy earnings growth (CAGR of 41% in FY15-18E).

Figure: D/E and Interest coverage ratio trend



Source: Company; IDBI Capital Research

Figure: Adjusted PAT and margin trend

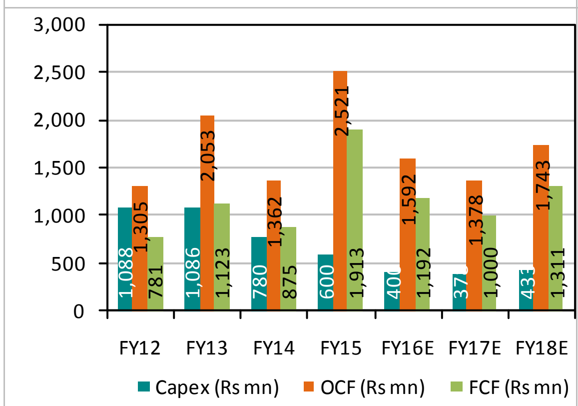


Source: Company; IDBI Capital Research

- **Major capex overdone; time to encash it**

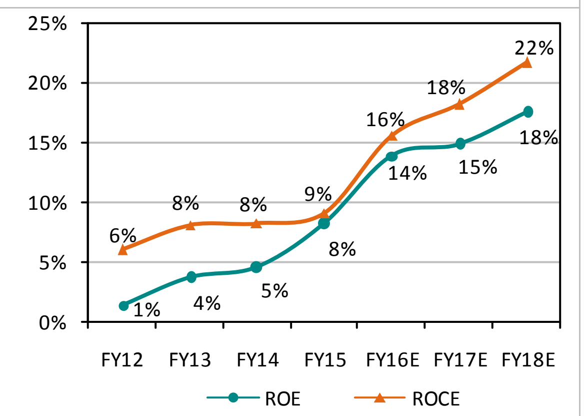
  We see significant uptick in the return ratios (18% RoE in FY18E; nearly 2x jump) from 8.2% (FY15) while with no major capex (Rs1,210 mn), margin expansion and healthy earnings, the FCF is likely to improve substantially (nearly Rs3,500 mn) in FY16E-18E. These would not only enable the company to pare its debt level but also provide a significant cash cushion (improvement in financial health) in the coming years.

Figure: Capex v/s FCF



Source: Company; IDBI Capital Research

Figure: Return ratios



Source: Company; IDBI Capital Research

Valuation and Outlook

- **Attractive; time to ride on it - Initiate with a BUY**

  We expect consolidated revenue and earning CAGR of 10% & 41% in FY15-18E, respectively. The stock is currently trading at a P/E of 8.3x/6.3x and EV/EBITDA of 3.9x/3.1x to FY17E/FY18E earnings. Given the multifold improvement (across all parameters), we believe the stock should command better valuation (broadly in-line with industry peers). We have valued the company on a SOTP basis by assigning EV/EBITDA multiple to its three segments, arriving at a Target Price of Rs46/share (53% upside). Hence, we initiate coverage on the company with a **BUY** recommendation.

Table: SOTP Valuation

Particulars	FY18E EBITDA	EV/EBITDA (x)	Rs mn
Pigment	849	3	2,548
Agro chemical	822	4	3,288
Basic Chemical	1,671	6	10,027
Total EV			15,864
Less: Debt			4,482
Add : Cash			344
Net value of equity			11,726
No. of shares			254.3
Fair value per share (Rs)			46
CMP (Rs)			30
Upside			53%

Source: Company; IDBI Capital Research

Key Risks

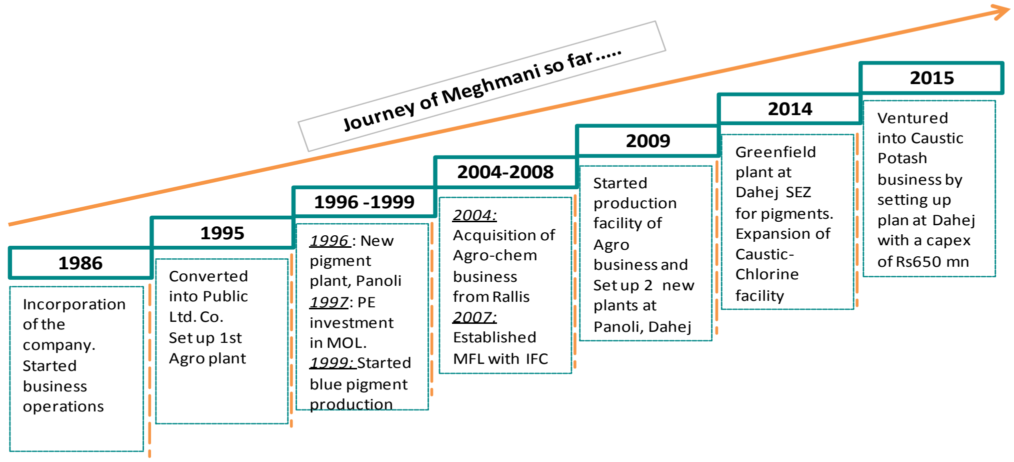
- High reliance on export business (Pigments + Agro-chemical) and competition from Chinese players could impact export revenues.
- Any failure in anticipated better monsoon (India + World) could impact the demand of its agro-chemical products and our assumptions.
- Specialty chemical business is highly competitive in nature (both in pricing + product substitution). Any cheap import or weak demand could negatively impact margin profile and earnings.

About the Company

Meghmani Organics Ltd. (MOL), a part of the Meghmani group, is a well diversified chemical company manufacturing pigments, agro-chemical and basic chemical products. It has pan India presence through stockiest, distributors and international market (presence over 75 countries) through extensive network of 70 overseas distributors. It serves to 400+ customers through subsidiaries in the US, Europe, Indonesia and Dubai. Export constitutes approximately 57% of overall revenues.

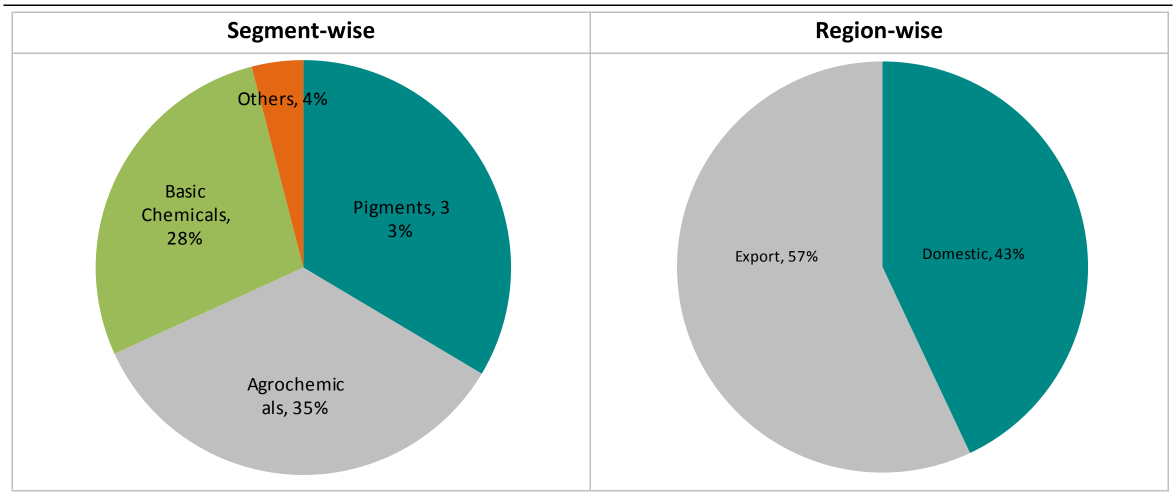
- **Company at glance**

Diagram: History so far…



Source: Company; IDBI Capital Research

Figure: Revenue mix (FY15)



Source: Company; IDBI Capital Research

Financial summary *(Consolidated)*

Profit & Loss Account (Rs mn)

Year-end: March	FY15	FY16E	FY17E	FY18E
Net sales	**12,942**	**13,338**	**15,138**	**17,300**
Growth (%)	*9.8*	*3.1*	*13.5*	*14.3*
Operating expenses	(10,911)	(10,444)	(11,838)	(13,494)
EBITDA	**2,031**	**2,894**	**3,300**	**3,806**
Growth (%)	*3.7*	*42.5*	*14.0*	*15.3*
Depreciation	(747)	(774)	(860)	(902)
EBIT	**1,284**	**2,121**	**2,440**	**2,904**
Interest paid	(746)	(667)	(606)	(554)
Other income	64	40	45	52
Pre-tax profit	**599**	**1,494**	**1,880**	**2,403**
Tax	(140)	(418)	(639)	(812)
Effective tax rate (%)	*23.3*	*28.0*	*34.0*	*33.8*
Net profit	**418**	**806**	**941**	**1,240**
Adjusted net profit	**441**	**806**	**941**	**1,240**
Growth (%)	*89.4*	*83.0*	*16.7*	*31.8*
Shares o/s (mn nos)	*254*	*254*	*254*	*254*

Cash Flow Statement (Rs mn)

Year-end: March	FY15	FY16E	FY17E	FY18E
Pre-tax profit	599	1,494	1,880	2,403
Depreciation	747	774	860	902
Tax paid	(161)	(418)	(639)	(812)
Chg in working capital	665	12	(423)	(385)
Other operating activities	649	(269)	(300)	(350)
CF from operations (a)	**2,499**	**1,592**	**1,378**	**1,757**
Capital expenditure	(459)	(400)	(378)	(433)
Chg in investments	0	-	-	-
Other investing activities	37	-	-	(13)
CF from investing (b)	**(586)**	**(400)**	**(378)**	**(446)**
Equity raised/(repaid)	-	-	-	-
Debt raised/(repaid)	(562)	(777)	(711)	(807)
Dividend (incl. tax)	(282)	(323)	(329)	(368)
Chg in minorities	-	-	-	-
Other financing activities	(1,287)	-	-	-
CF from financing (c)	**(2,130)**	**(1,100)**	**(1,040)**	**(1,175)**
Net chg in cash (a+b+c)	**(217)**	**93**	**(40)**	**136**

Balance Sheet (Rs mn)

Year-end: March	FY15	FY16E	FY17E	FY18E
Net fixed assets	8,042	7,669	7,187	6,718
Investments	179	179	179	179
Current assets	**7,227**	**7,208**	**7,745**	**8,466**
Inventories	2,158	2,047	2,245	2,346
Sundry Debtors	3,167	3,216	3,567	4,029
Cash and Bank	156	249	208	344
Loans and advances	1,383	1,334	1,362	1,384
Total assets	**15,448**	**15,057**	**15,112**	**15,363**
Shareholders' funds	**5,520**	**6,003**	**6,614**	**7,473**
Share capital	254	254	254	254
Reserves & surplus	5,261	5,745	6,356	7,215
Total Debt	**6,776**	**5,999**	**5,288**	**4,482**
Secured loans	3,129	2,700	2,115	1,793
Unsecured loans	3,647	3,299	3,173	2,689
Other liabilities	471	471	471	471
Curr Liab & prov	**1,738**	**1,639**	**1,794**	**1,994**
Current liabilities	1,434	1,335	1,490	1,689
Provisions	305	305	305	305
Total liabilities	**8,985**	**8,109**	**7,554**	**6,946**
Total equity & liabilities	**15,448**	**15,057**	**15,112**	**15,363**
Book Value (Rs)	**22**	**24**	**26**	**29**

Source: Company; IDBI Capital Research

Financial Ratios

Year-end: March	FY15	FY16E	FY17E	FY18E
Adj EPS (Rs)	1.7	3.2	3.7	4.9
Adj EPS growth (%)	89.4	83.0	16.7	31.8
EBITDA margin (%)	15.7	21.7	21.8	22.0
Pre-tax margin (%)	4.6	11.2	12.4	13.9
RoE (%)	8.2	14.0	14.9	17.6
RoCE (%)	9.1	15.6	18.3	21.8
Turnover & Leverage ratios (x)				
Asset turnover	0.8	0.9	1.0	1.1
Leverage factor	3.0	2.6	2.4	2.2
Net margin (%)	3.4	6.0	6.2	7.2
Net Debt/Equity	1.2	1.0	0.8	0.6
Working Capital & Liquidity ratios				
Inventory days	61	56	54	50
Receivable days	89	88	86	85
Payable days	48	47	46	46

Valuations

Year-end: March	FY15	FY16E	FY17E	FY18E
PER (x)	17.7	9.7	8.3	6.3
Price/Book value (x)	1.4	1.3	1.2	1.0
PCE (x)	6.6	4.9	4.3	3.6
EV/Net sales (x)	1.1	1.0	0.9	0.7
EV/EBITDA (x)	7.1	4.7	3.9	3.1

Notes

Dealing	(91-22) 6637 1150	dealing@idbicapital.com

Key to Ratings

Stocks:

BUY: Absolute return of 15% and above; **ACCUMULATE:** 5% to 15%; **HOLD:** Upto ±5%; **REDUCE:** -5% to -15%; **SELL:** -15% and below.

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