

Corporate tax rate cut to boost earnings

The recent tax cut by the government from 33% to 25.2% is likely to boost earnings of Kansai Nerolac (Kansai) by 3% and 6% for FY20E and FY21E respectively. We change our earnings estimates and target price accordingly. We believe a tax cut would help demand revival in both decorative and industrial paint demand (with revival in automotive industry). This would also help organised players to gain market share from the unorganised segment, which are ~25% of the domestic paint industry.

Decorative segment to drive volume growth

Kansai is the largest industrial paint company in India with more than 35% market share in industrial paints and third largest player with an overall market share of 14%. With sustainable growth in decorative paints and subdued industrial demand, company has increased its revenue contribution from decorative paints to 55% while rest comes from the Industrial. In order to increase market share, Kansai continues to invest in brands with 4-5% of sales going towards advertisement and promotion. We believe decorative paints would continue to grow at rapid pace with the presence of limited players and strong repainting demand. We expect a revival in industrial paints demand led by a recovery in automotive segments. We expect blended volume CAGR 9% for FY19E-21E led by ~13% volume CAGR in the decorative paints category.

Revival in industrial paint demand to help in margin expansion

Kansai's gross margin during Q1FY20 remained flat despite pressure in the industrial paints category. We believe a price hike in the decorative segment helped offset lower profitability from industrial segment. While there was a slowdown in industrial paint demand, we believe margin pressure will ease, going forward, owing to a change in product mix and gradual price hike

Valuation & Outlook

Increasing urbanisation, higher rural income levels and a brief repainting cycle have been the main reason for sustainable decorative paints demand. This coupled with social schemes such as Housing for All and better monsoons (would help in improving rural income) would be a strong trigger for the paint industry. We believe, strong revenue earning CAGR of 16% and 20% in FY19-21E supported by recent corporate tax rate cut. Given the strong balance sheet, zero debt on the books, higher operating margins and sustainable free cash flows, we expect return ratios to remain at elevated level in FY19-21E. We maintain our **BUY** rating on stock



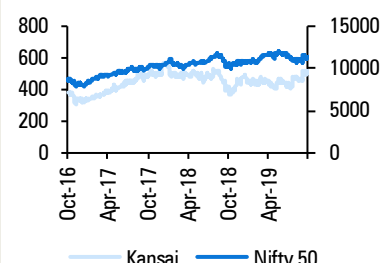
Particulars

Particular	Amount
Market Capitalization (₹ Crore)	28,239.4
Debt (FY19) (₹ Crore)	3.4
Cash & Inv (FY19) (₹ Crore)	78.9
EV (₹ Crore)	25,954.3
52 week H/L	535 / 343
Equity capital (₹ Crore)	53.9
Face value (₹)	1.0

Key Highlights

- Tax cut to boost earnings growth by ~3% and 6% for FY20E and FY21E respectively
- Strong volume growth in the decorative segment
- Maintain **BUY** rating with revised target price of ₹ 620/ share

Price Chart



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Key Financial Summary

(₹ Crore)	FY17	FY18	FY19	FY20E	FY21E	CAGR(FY19-21E)
Net Sales	3988.2	4569.6	5138.9	5583.1	6876.0	15.7
EBITDA	730.7	789.8	742.0	782.0	973.0	14.5
EBITDA Margin (%)	18.3	17.2	14.3	13.9	14.1	
Net Profit	505.9	516.4	467.3	544.2	677.2	20.4
EPS (₹)	9.4	9.6	8.7	10.1	12.6	
P/E (x)	55.8	54.7	60.4	51.9	41.7	
Price/Book (x)	9.3	8.3	7.6	7.3	6.4	
Mcap/Sales (x)	7.1	6.2	5.5	5.1	4.1	
RoE (%)	18.0	16.5	13.6	15.1	16.6	
RoCE (%)	26.2	24.5	20.2	19.9	21.8	

Source: Company, ICICI Direct Research

Financial summary

Exhibit 1: Profit and loss statement		₹ crore			
(Year-end March)	FY18	FY19	FY20E	FY21E	
Total operating Income	4,569.6	5,138.9	5,583.1	6,876.0	
Growth (%)		12.5	8.6	23.2	
Raw Material Expenses	2,774.1	3,302.5	3,658.6	4,481.5	
Employee Expenses	226.6	255.4	283.9	329.4	
Other expenses	681.7	873.7	1,437.7	1,858.2	
Total Operating Expenditure	3,796.8	4,431.6	4,840.0	5,946.5	
EBITDA	789.8	742.0	782.0	973.0	
Growth (%)		-6.0	5.4	24.4	
Depreciation	75.8	90.5	100.5	116.9	
Interest	0.0	0.0	2.5	2.5	
Other Income	72.4	61.9	49.5	53.0	
Exceptional Income	0.0	0.0	0.0	0.0	
PBT	786.4	713.4	728.5	906.6	
Total Tax	270.0	246.1	184.3	229.4	
PAT	516.4	467.3	544.2	677.2	

Source: Company, ICICI Direct Research

Exhibit 2: Cash flow statement		₹ crore			
(Year-end March)	FY18	FY19	FY20E	FY21E	
Profit before Tax	516.4	467.3	544.2	677.2	
Add: Depreciation	75.8	90.5	100.5	116.9	
(Inc)/dec in Current Assets	-159.3	373.6	-158.3	-464.7	
Inc/(dec) in CL and Provisions	158.1	-79.7	240.8	254.0	
Others	0.0	0.0	2.5	2.5	
CF from operating activities	591.0	851.7	729.7	585.9	
(Inc)/dec in Investments	-4.9	-71.7	0.0	0.0	
(Inc)/dec in Fixed Assets	-336.7	-371.5	-350.0	-350.0	
Others	93.0	71.7	0.0	0.0	
CF from investing activities	-248.6	-659.0	-350.0	-350.0	
Inc/(dec) in loan funds	-8.6	-6.3	3.0	3.0	
Dividend paid & dividend tax	-169.4	-169.4	-208.5	-208.5	
Others	-27.1	1.4	-182.5	0.0	
CF from financing activities	-205.2	-174.3	-388.0	-205.5	
Net Cash flow	16.5	18.4	-0.2	43.7	
Opening Cash	43.9	60.5	78.9	78.7	
Closing Cash	60.5	78.9	78.7	122.4	

Source: Company, ICICI Direct Research

Exhibit 3: Balance sheet		₹ crore			
(Year-end March)	FY18	FY19	FY20E	FY21E	
Liabilities					
Equity Capital	53.9	53.9	53.9	53.9	
Reserve and Surplus	3,071.2	3,370.6	3,523.2	3,987.0	
Total Shareholders funds	3,125.1	3,424.5	3,577.1	4,040.9	
Total Debt	9.7	3.4	6.4	9.4	
Deferred Tax Liability	80.4	105.1	105.1	105.1	
Total Liabilities	3,215.3	3,533.0	3,688.6	4,155.4	
Assets					
Gross Block	1,709.4	2,109.4	2,674.0	3,024.0	
Less: Acc Depreciation	703.0	793.4	893.9	1,010.8	
Net Block	1,006.4	1,315.9	1,780.1	2,013.2	
Capital WIP	343.1	314.7	100.0	100.0	
Total Fixed Assets	1,349.5	1,630.6	1,880.1	2,113.2	
Non-Current Investments	37.3	108.9	108.9	108.9	
Inventory	805.8	1,052.8	1,086.0	1,337.5	
Debtors	675.7	674.0	749.5	923.1	
Loans and Advances	3.3	17.9	4.1	5.0	
Investments & Other CA	898.7	351.9	415.2	453.9	
Cash	60.5	78.9	78.7	122.4	
Total Current Assets	2,530.6	2,175.5	2,333.5	2,841.9	
Creditors	683.6	631.9	856.6	1,073.8	
Provisions & other CL	169.0	141.1	157.2	194.0	
Total Current Liabilities	852.6	773.0	1,013.8	1,267.8	
Net Current Assets	1,678.0	1,402.5	1,319.8	1,574.1	
Others Non-Current Assets	150.5	391.0	391.0	391.0	
Application of Funds	3,215.3	3,533.0	3,688.6	4,155.4	

Source: Company, ICICI Direct Research

Exhibit 4: Key ratios		₹ crore			
(Year-end March)	FY18	FY19	FY20E	FY21E	
Per share data (₹)					
EPS	9.6	8.7	10.1	12.6	
Cash EPS	11.0	10.4	12.0	14.7	
BV	58.0	63.5	66.4	75.0	
DPS	3.1	3.1	3.9	3.9	
Cash Per Share	13.0	14.7	16.6	18.8	
Operating Ratios (%)					
EBITDA Margin	17.2	14.3	13.9	14.1	
EBIT Margin	15.6	12.7	12.2	12.5	
PAT Margin	11.3	9.1	9.7	9.8	
Inventory days	64	75	71	71	
Debtor days	54	48	49	49	
Creditor days	55	45	56	57	
Return Ratios (%)					
RoE	16.5	13.6	15.1	16.6	
RoCE	24.5	20.2	19.9	21.8	
RoIC	38.8	25.5	23.4	25.4	
Valuation Ratios (x)					
P/E	54.7	60.4	51.9	41.7	
EV / EBITDA	32.9	35.0	33.2	26.6	
EV / Net Sales	5.7	5.1	4.6	3.8	
Market Cap / Sales	6.2	5.5	5.1	4.1	
Price to Book Value	8.3	7.6	7.3	6.4	
Solvency Ratios					
Debt/EBITDA	0.0	0.0	0.0	0.0	
Debt / Equity	0.0	0.0	0.0	0.0	
Current Ratio	1.9	2.5	2.0	1.9	
Quick Ratio	1.0	1.1	0.9	0.9	

Source: Company, ICICI Direct Research

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Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



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