Twitter Thread by Darshan Mehta

Darshan Mehta
@darshanvmehta1

DAM capital on Deepak Nitrite

INITIATING COVERAGE

Deepak Nitrite

Shifting orbit

OUTPERFORMER

27 August 2021

BSE Sensex: 55949

Sector: Agri-inputs

Stock data

CMP (Rs)	2,086
Mkt Cap (Rs bn/USD m)	284.6 /3,834
Target Price (Rs)	2,635
Change in TP (%)	NA
Potential from CMP (%)	26.3
Earnings change (%)	
FY22E	⇔
FY23E	⇔
Bloomberg code	DN IN
1-yr high/low (Rs)	2,209/663
6-mth avg. daily volumes (m)	1.4
6-mth avg. daily traded value (Rsm/USDm)	2,569.9/34.6
Shares outstanding (m)	136.4
Free float (%)	54.3
Promoter holding (%)	45.7

Price performance – relative & absolute

(%)	3-mth	6-mth	1-yr
DN IN	17.0	52.5	181.2
BSE Sensex	9.7	13.9	43.2

Deepak Nitrite Ltd (DNL) has been a front runner in tapping import substitution opportunities in India's chemical space. Robust end-user demand and a likely burgeoning Indian economy place DNL in a sweet spot to realise its 'Make in India for the World' dream. DNL's diversified business model and track record in commissioning mega-scale projects for complex chemicals like phenol indicate its best-in-class process management capabilities, and provide comfort on its growth plans. After setting up a diversified business base, DNL is now looking to transition into high-margin chemical intermediates, from being a bulk chemical-focused entity. In its next leg of growth, the company is looking to invest ~Rs11bn to introduce multiple downstream products and complex chemistry platforms over the next 2-3 years. We expect DNL to post healthy 16.8% revenue and 14.6% EBITDA CAGR, respectively, over FY21-24E, primarily contributed by the Phenolics and Fine & Speciality Chemicals (FSC) divisions. We initiate coverage with an Outperformer rating, and a target price of Rs2,635 (35x FY23E PER).

Phenolics division continues to present immense opportunity: After successfully building large-scale capabilities in base products (phenol and acetone), DNL is now looking to forward integrate into value-added downstream products in phenols; it will likely invest ~Rs7bn over FY22-24E towards this project. Value-addition provides immense opportunity, as most downstream products are imported, given the lack of domestic manufacturers, despite sizeable demand for these products. We estimate 15% revenue and 13% EBITDA CAGR in this division over FY21-24E.

FSC margin expansion to boost profitability: DNL's FSC segment comprises high-margin niche products that require expertise in handling complex reactions. FSC registered 19.6% revenue and 42% EBIT CAGR over FY17-21, contributing 18% of total revenues. Management is looking to step up investments in this segment to improve the product mix, add new technology platforms and launch complex molecules. The company is looking to launch 2 molecules in FY22, and commercialise 5 new molecules over the next 2-3 years. We expect 25% revenue and 19% EBIT CAGR over FY21-24E, with strong 38% EBIT margins in FY24E.

Ready for the big leap: DNL is looking to transition from bulk chemical intermediates into complex advance intermediates, which would enhance its margins and return ratios. We expect the stock to re-rate, with increasing proportion of complex chemistry products in the overall revenue mix. At 28x FY23E P/E and 28.3%/35.7% RoE/RoCE, DNL trades at a discount to most of its chemical peers. We initiate coverage on the stock with an Outperformer rating.

Key valuation metrics

Year to 31 Mar	FY20	FY21	FY22E	FY23E	FY24E
Net sales (Rs m)	42,297	43,598	59,322	61,482	69,513
Adj. net profit (Rs m)	6,110	7,758	9,653	10,278	11,982
Shares in issue (m)	136	136	136	136	136
Adj. EPS (Rs)	44.8	56.9	70.8	75.4	87.8
% change	251.9	27.0	24.4	6.5	16.6
PE (x)	46.5	36.7	29.5	27.7	23.7
Price/ Book (x)	18.1	12.1	8.9	7.0	5.6
EV/ EBITDA (x)	28.7	23.1	19.2	17.5	14.8
RoE (%)	46.2	39.6	34.9	28.3	26.2
RoCE (%)	35.3	38.1	40.3	35.7	33.8

Source: Company, DAM Capital Research

Nitin Agarwal

Miloni Bagadia