

SRF Ltd.: Q1FY18 Result Update

Specialty chemicals to turnaround by Q4FY18

CMP INR 1435 Target INR 1806

Rating: BUY Upside: 26%

SRF Ltd's (SRF) consolidated Q1FY18 sales came ~5% below our estimates and ~6% higher yoy driven by lower than expected growth in the Chemicals and Polymers Business (CPB) while growth was largely in line in the Technical Textiles Business (TTB) and Packaging Films Business (PFB). EBITDA at INR 209 cr was 29% lower than our estimates at INR 271 cr driven by an ~690 bps dip in gross margins while PAT at INR 104 cr was lower than our estimates by ~28%. Key highlights of the quarter were: (i) Gross revenues in the Chemicals and Polymers business (CPB) decreased by 8% YoY due to continued decline in the specialty chemical business while the domestic refrigerant business was impacted by GST implementation (ii) TTB reported 11% growth in gross revenues with NTCF performance impacted by weak raw material prices and competition from Chinese TBR impacting volumes (iii) Packaging films business (PFB) reported a 19% growth in gross revenues despite of power supply issues leading to volume losses in new DTA line while EBIT margins for the business improved sequentially to 10.5% in spite of industry wide margin pressure. Management expects a turnaround in the CPB segment from Q4FY18 and expect the division to return to the high growth high margin trajectory from FY19 onwards. We believe valuations have once again become attractive for the stock and we upgrade our rating on the stock to 'BUY' from 'HOLD' with a revised target price of 1806 implying a 26% upside from current levels.

CPB segment remains a drag in the quarter; turnaround expected from Q4FY18

SRF's Q1FY18 consolidated net revenues at INR 1293 cr were below our estimates mainly due to an 8% sales de-growth in the CPB segment while TTB and PFB sales were largely in line with the expectations. Decline in the CPB segment was on the back of continued subdued demand for the specialty chemical business although the management is seeing green shoots of recovery and expects growth to return from Q4FY18 for the specialty business. The domestic refrigerant business was also impacted by the implementation of GST in the month of June, despite this the company achieved highest ever production of R 32 and R134a. Management is also contemplating debottlenecking the R134a plant in view of increased demand from the US market in Q3FY18 and Q4FY18. Management expects the specialty chemical division to return to the high growth trajectory in FY19 while the endeavour is to sustain or slightly improve profitability in the CPB segment compared to FY17 levels. The company has announced a new capex of INR 85 cr for building a new plant (P33) to produce specialty chemicals for the agro industry with a peak production capacity of 800-1000 TPA.

TTB and PFB performance largely in line with expectations

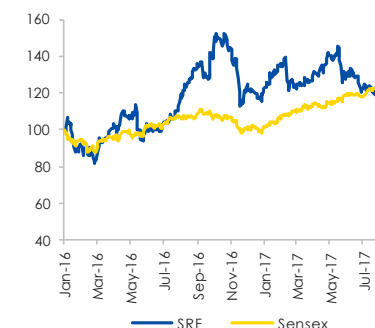
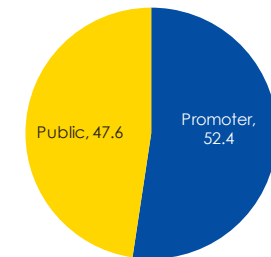
Gross revenues in the TTB segment increased by 11% yoy with the company maintaining leadership position in NTCF despite facing weak raw material prices and competition from Chinese TBR tyres impacting volumes. EBIT margins in the business improved by ~90 bps sequentially to 10.9%. Gross revenues for the PFB segment increased by 19% yoy slightly lower than expectation due to initial operational issues on account of power led to volume loss in new DTA line while GST implementation also impacted volumes. The BOPP plant at the Indore DTA remains on track to come online by end of FY18. Consolidated PAT came in at INR 104 cr (down 33% YoY and 28% lower than our est.) aided by higher other income in the quarter and lower than expected effective tax rate.

Outlook and valuations: Valuations attractive considering near term turnaround in specialty chemical business; Upgrade to BUY

We are revising our PAT estimates for FY18 and FY19 downwards by 16% and 5% respectively to account for slowdown in the specialty chemical business till 9MFY18. However, we expect the specialty chemical business to rebound in FY19 which coupled with improved volumes in the refrigerants business is likely to drive significant growth for the CPB segment. The upcoming capacity expansion in BOPET is likely to lead to strong sales in growth in the PFB segment while management is also confident of returning to 14-15% margins in the PFB segment by the end of FY18. The stock currently trades at P/E of 18.8x FY18E and 13.9x FY19E, respectively making it attractive at these levels with limited downside risk. We upgrade our rating to 'BUY' on the stock at the current price with a revised target price of INR 1806, valuing the company at ~17.5x FY19E EPS of INR 103.

Year to March (INR cr)	Q1FY18	Q1FY17	%Chg. YoY	Q4FY17	%Chg. QoQ	FY17	FY18E	FY19E
Net Revenues (incl Op. Inc.)	1,293	1,219	6	1,326	-3	4,822	5,299	6,112
% Growth (yoy)						5	10	15
EBITDA	209	296	-29	234	-11	997	994	1,238
% Growth (yoy)						4	0	25
Adjusted Net profit	104	154	-33	129	-20	515	446	602
Adjusted Diluted EPS	18	26	-33	22	-20	88	76	103
Diluted P/E (x)						16.3	18.8	13.9
EV/EBITDA (x)						10.0	10.0	8.1
ROCE (%)						14	12	15

Bloomberg:	SRF:IN
52-week range (INR):	1,970/ 1,351
Share in issue (cr):	5.8
M cap (INR cr):	8,882
Avg. Daily Vol.	222.335
BSE/NSE :('000):	

Date: 9th August 2017

Change in Estimates

	FY18E			FY19E		
	Previous	Revised	%Change	Previous	Revised	%Change
Sales	5,404	5,299	-2	6,139	6,112	0
EBITDA	1,147	994	-13	1,331	1,238	-7
EBITDA margin	21%	19%		22%	20%	
PAT	529	446	-16	635	602	-5
EPS	90	76	-16	109	103	-5

Q1FY18 Result Highlights

Particulars	Q1FY18	Q1FY17	%Change	Q4FY17	% Change
Net Revenues (incl Op. Inc.)	1,293	1,219	6	1,326	-3
Raw Materials Cost	718	593	21	699	3
Gross Profit	575	626	-8	626	-8
Operating Expenses	366	330	11	392	-7
EBITDA	209	296	-29	234	-11
EBITDA margin	16	24		18	
Depreciation	76	70	9	73	4
Other income	20	6		26	
Net finance expense	27	28	-4	23	19
Profit before tax	127	204	-38	164	-23
Provision for taxes	23	50		35	
Reported Net profit	104	154	-33	129	-20
Extraordinary items/Minority Interest	0	0		0	
Adjusted Net profit	104	154	-33	129	-20
As % of net revenues					
COGS	56	49		53	
Operating expenses	28	27		30	
EBITDA	16	24		18	
Reported net profit	8	13		10	
Tax Rate (% of PBT)	18	25		21	

Financials

Financial Statements						(INR cr)					Balance Sheet					(INR cr)					Profitability & efficiency ratios				
Year to March	FY15	FY16	FY17	FY18E	FY19E	As on 31st March	FY15	FY16	FY17E	FY18E	FY19E	Year to March	FY15	FY16	FY17	FY18E	FY19E	Year to March	FY15	FY16	FY17	FY18E	FY19E		
Net revenue	4,540	4,593	4,822	5,299	6,112	Equity capital	58	58	58	58	58	ROAE (%)	12.5%	17.0%	17.3%	13.3%	15.8%	ROAE (%)	9.6%	13.7%	14.1%	12.4%	14.9%		
Materials costs	2,551	2,341	2,391	2,821	3,068	Reserves & surplus	2,238	2,705	3,124	3,488	4,008	ROIC (%)	9.7%	15.8%	14.5%	12.2%	14.6%	Inventory days	109	105	128	120	127		
Gross profit	1,988	2,252	2,431	2,477	3,043	Borrowings	2,728	2,130	1,977	2,177	2,177	Debtors days	49	41	50	50	50	Payable days	63	111	123	123	123		
Power & fuel	123	130	136	150	172	Other long-term liabilities	67	22	30	30	30	Cash conversion cycle (days)	85	42	58	51	56	Current ratio	3.3	1.7	1.9	1.7	1.8		
Employee costs	356	386	434	477	550	Sources of funds	5,091	4,915	5,190	5,754	6,274	Debt/Equity	1.2	0.8	0.6	0.6	0.5	Core ROACE (%)	10.3%	15.5%	16.4%	14.1%	16.8%		
SG&A	791	773	864	857	1,083	Gross Block	6,585	7,019	7,719	8,569	9,169	Operating ratios	Year to March	FY15	FY16	FY17	FY18E	FY19E	Total asset turnover	0.9	0.9	1.0	1.0	1.0	
EBITDA	717	963	997	994	1,238	Accumulated Depreciation	(2,742)	(3,005)	(3,399)	(3,713)	(4,054)	Year to March	FY15	FY16	FY17	FY18E	FY19E	Fixed asset turnover	0.7	0.7	0.7	0.7	0.7		
Depreciation & Amortization	245	275	283	313	341	CWIP	104	117	259	409	509	Equity turnover	2.1	1.8	1.6	1.6	1.6	Du pont analysis	Year to March	FY15	FY16	FY17	FY18E	FY19E	
EBIT	472	688	714	681	896	Net Fixed Assets	3,947	4,131	4,578	5,265	5,623	Year to March	FY15	FY16	FY17	FY18E	FY19E	NP margin (%)	6.0%	9.4%	10.7%	8.4%	9.9%		
Other income	65	28	45	25	25	Net intangible assets	80	99	86	86	86	ROAE (%)	12.5%	17.0%	17.3%	13.3%	15.8%	Valuation parameters	Year to March	FY15	FY16	FY17	FY18E	FY19E	
EBIT incl. of other income	537	715	759	706	921	Investments	94	165	196	165	165	Diluted EPS (INR)	46.6	73.6	88.1	76.3	103.0	Y o Y growth (%)	69.1	57.8	19.8	-13.4	35.0		
Interest expenses	138	130	102	103	108	Inventories	764	671	838	924	1,066	Diluted PE (x)	30.8	19.5	16.3	18.8	13.9	Price/BV (x)	3.7	3.0	2.6	2.4	2.1		
Profit before tax	399	585	657	603	814	Sundry debtors	611	514	657	726	837	EV/Sales (x)	2.4	2.2	2.1	1.9	1.6	EV/EBITDA (x)	15.2	10.4	10.0	10.0	8.1		
Provision for tax	97	155	142	157	212	Cash and equivalents	107	389	96	20	(8)	Dividend yield (%)	0.7	0.7	0.8	0.8	0.8								
Adjusted Profit	303	430	515	446	602	Loans and advances	141	84	114	148	171														
Basic shares outstanding (crs)	5.8	5.8	5.8	5.8	5.8	Total current assets	1,622	1,659	1,705	1,818	2,066														
EPS (INR)	46.6	73.6	88.1	76.3	103.0	Sundry creditors and others	442	715	809	955	1,038														
Dividend per share (INR)	9.8	9.8	12.0	12.0	12.0	Provisions	12	31	36	96	99														
Dividend payout (%)	22%	16%	16%	18%	14%	Total current liabilities & provisions	454	746	845	1,050	1,137														
						Net current assets	1,168	913	860	768	929														
						Uses of funds	5,091	4,914	5,190	5,754	6,274														
						Book value per share (INR)	393	473	545	607	696														
						Free cash flow																			
						Year to March	FY15	FY16	FY17E	FY18E	FY19E														
						Net profit	303	430	515	446	602														
						Add : Depreciation	245	289	283	313	341														
						Others	96	148	56	78	83														
						Gross cash flow	643	867	855	837	1,026														
						Changes in WC	-101	223	-240	16	-190														
						Operating cash flow	542	1,090	615	853	836														
						Capex	-475	-614	-841	-1,000	-700														
						Free cash flow	67	476	-226	-147	136														
						Cash flow metrics																			
						Year to March	FY15	FY16	FY17E	FY18E	FY19E														
						Cash flow from operations	542	1,090	615	853	836														
						Cash Flow from investing activities	-532	-667	-827	-944	-675														
						Cash Flow from financing activities	-18	-182	-336	15	-190														
						Capex	-475	-614	-841	-1,000	-700														
						Dividends	-57	-57	-82	-82	-82														

Edelweiss Broking Limited, 1st Floor, Tower 3, Wing B, Kohinoor City Mall, Kohinoor City, Kiro Road, Kurla(W)
Board: (91-22) 4272 2200

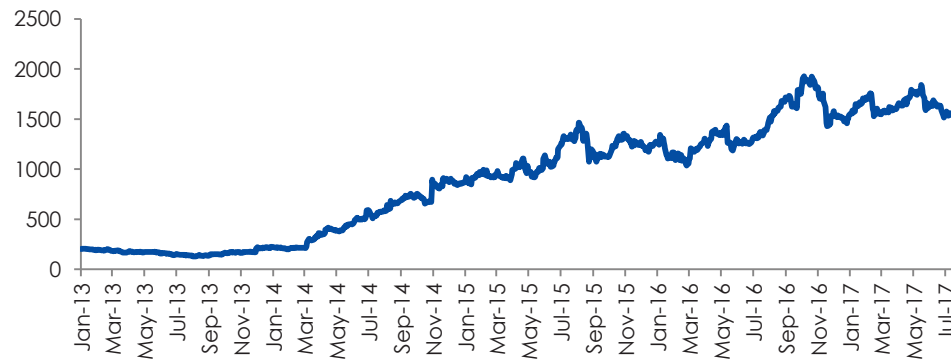
Vinay Khattar

Head Research

vinay.khattar@edelweissfin.com

Rating	Expected to
Buy	appreciate more than 15% over a 12-month period
Hold	appreciate between 5-15% over a 12-month period
Reduce	Return below 5% over a 12-month period

SRF 5 years price chart



Disclaimer

Edelweiss Broking Limited ("EBL" or "Research Entity") is regulated by the Securities and Exchange Board of India ("SEBI") and is licensed to carry on the business of broking, depository services and related activities. The business of EBL and its Associates (list available on www.edelweissfin.com) are organized around five broad business groups – Credit including Housing and SME Finance, Commodities, Financial Markets, Asset Management and Life Insurance.

Broking services offered by Edelweiss Broking Limited under SEBI Registration No.: INZ000005231; Name of the Compliance Officer: Mr. Brijmohan Bohra, Email ID: complianceofficer.ebl@edelweissfin.com Corporate Office: Edelweiss House, Off CST Road, Kalina, Mumbai - 400098; Tel. 18001023335/022-42722200/022-40094279

This Report has been prepared by Edelweiss Broking Limited in the capacity of a Research Analyst having SEBI Registration No. INH000000172 and distributed as per SEBI (Research Analysts) Regulations 2014. This report does not constitute an offer or solicitation for the purchase or sale of any financial instrument or as an official confirmation of any transaction. The information contained herein is from publicly available data or other sources believed to be reliable. This report is provided for assistance only and is not intended to be and must not alone be taken as the basis for an investment decision. The user assumes the entire risk of any use made of this information. Each recipient of this report should make such investigation as it deems necessary to arrive at an independent evaluation of an investment in the securities of companies referred to in this document (including the merits and risks involved), and should consult his own advisors to determine the merits and risks of such investment. The investment discussed or views expressed may not be suitable for all investors.

This information is strictly confidential and is being furnished to you solely for your information. This information should not be reproduced or redistributed or passed on directly or indirectly in any form to any other person or published, copied, in whole or in part, for any purpose. This report is not directed or intended for distribution to, or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject EBL and associates / group companies to any registration or licensing requirements within such jurisdiction. The distribution of this report in certain jurisdictions may be restricted by law, and persons in whose possession this report comes, should observe, any such restrictions. The information given in this report is as of the date of this report and there can be no assurance that future results or events will be consistent with this information. This information is subject to change without any prior notice. EBL reserves the right to make modifications and alterations to this statement as may be required from time to time. EBL or any of its associates / group companies shall not be in any way responsible for any loss or damage that may arise to any person from any inadvertent error in the information contained in this report. EBL is committed to providing independent and transparent recommendation to its clients. Neither EBL nor any of its associates, group companies, directors, employees, agents or representatives shall be liable for any damages whether direct, indirect, special or consequential including loss of revenue or lost profits that may arise from or in connection with the use of the information. Our proprietary trading and investment businesses may make investment decisions that are inconsistent with the recommendations expressed herein. Past performance is not necessarily a guide to future performance. The disclosures of interest statements incorporated in this report are provided solely to enhance the transparency and should not be treated as endorsement of the views expressed in the report. The information provided in these reports remains, unless otherwise stated, the copyright of EBL. All layout, design, original artwork, concepts and other Intellectual Properties, remains the property and copyright of EBL and may not be used in any form or for any purpose whatsoever by any party without the express written permission of the copyright holders.

EBL shall not be liable for any delay or any other interruption which may occur in presenting the data due to any reason including network (Internet) reasons or snags in the system, break down of the system or any other equipment, server breakdown, maintenance shutdown, breakdown of communication services or inability of the EBL to present the data. In no event shall EBL be liable for any damages, including without limitation direct or indirect, special, incidental, or consequential damages, losses or expenses arising in connection with the data presented by the EBL through this report.

We offer our research services to clients as well as our prospects. Though this report is disseminated to all the customers simultaneously, not all customers may receive this report at the same time. We will not treat recipients as customers by virtue of their receiving this report.

EBL and its associates, officer, directors, and employees, research analyst (including relatives) worldwide may: (a) from time to time, have long or short positions in, and buy or sell the securities thereof, of company(ies), mentioned herein or (b) be engaged in any other transaction involving such securities and earn brokerage or other compensation or act as a market maker in the financial instruments of the subject company/company(ies) discussed herein or act as advisor or lender/borrower to such company(ies) or have other potential/material conflict of interest with respect to any recommendation and related information and opinions at the time of publication of research report or at the time of public appearance. EBL may have proprietary long/short position in the above mentioned scrip(s) and therefore should be considered as interested. The views provided herein are general in nature and do not consider risk appetite or investment objective of any particular investor; readers are requested to take independent professional advice before investing. This should not be construed as invitation or solicitation to do business with EBL.

EBL or its associates may have received compensation from the subject company in the past 12 months. EBL or its associates may have managed or co-managed public offering of securities for the subject company in the past 12 months. EBL or its associates may have received compensation for investment banking or merchant banking or brokerage services from the subject company in the past 12 months. EBL or its associates may have received any compensation for products or services other than investment banking or merchant banking or brokerage services from the subject company in the past 12 months. EBL or its associates have not received any compensation or other benefits from the Subject Company or third party in connection with the research report. Research analyst or his/her relative or EBL's associates may have financial interest in the subject company. EBL, its associates, research analyst and his/her relative may have other potential/material conflict of interest with respect to any recommendation and related information and opinions at the time of publication of research report or at the time of public appearance.

Participants in foreign exchange transactions may incur risks arising from several factors, including the following: (i) exchange rates can be volatile and are subject to large fluctuations; (ii) the value of currencies may be affected by numerous market factors, including world and national economic, political and regulatory events, events in equity and debt markets and changes in interest rates; and (iii) currencies may be subject to devaluation or government imposed exchange controls which could affect the value of the currency. Investors in securities such as ADRs and Currency Derivatives, whose values are affected by the currency of an underlying security, effectively assume currency risk.

Research analyst has served as an officer, director or employee of subject Company: No
EBL has financial interest in the subject companies: No

EBL's Associates may have actual / beneficial ownership of 1% or more securities of the subject company at the end of the month immediately preceding the date of publication of research report.
Research analyst or his/her relative has actual/beneficial ownership of 1% or more securities of the subject company at the end of the month immediately preceding the date of publication of research report: No

EBL has actual/beneficial ownership of 1% or more securities of the subject company at the end of the month immediately preceding the date of publication of research report: No
Subject company may have been client during twelve months preceding the date of distribution of the research report.

There were no instances of non-compliance by EBL on any matter related to the capital markets, resulting in significant and material disciplinary action during the last three years.

Disclaimer

A graph of daily closing prices of the securities is also available at www.nseindia.com

Analyst Certification:

The analyst for this report certifies that all of the views expressed in this report accurately reflect his or her personal views about the subject company or companies and its or their securities, and no part of his or her compensation was, is or will be, directly or indirectly related to specific recommendations or views expressed in this report.

Additional Disclaimer for U.S. Persons

Edelweiss is not a registered broker – dealer under the U.S. Securities Exchange Act of 1934, as amended (the "1934 act") and under applicable state laws in the United States. In addition Edelweiss is not a registered investment adviser under the U.S. Investment Advisers Act of 1940, as amended (the "Advisers Act" and together with the 1934 Act, the "Acts"), and under applicable state laws in the United States. Accordingly, in the absence of specific exemption under the Acts, any brokerage and investment services provided by Edelweiss, including the products and services described herein are not available to or intended for U.S. persons.

This report does not constitute an offer or invitation to purchase or subscribe for any securities or solicitation of any investments or investment services and/or shall not be considered as an advertisement tool. "U.S. Persons" are generally defined as a natural person, residing in the United States or any entity organized or incorporated under the laws of the United States. US Citizens living abroad may also be deemed "US Persons" under certain rules.

Transactions in securities discussed in this research report should be effected through Edelweiss Financial Services Inc.

Additional Disclaimer for U.K. Persons

The contents of this research report have not been approved by an authorised person within the meaning of the Financial Services and Markets Act 2000 ("FSMA").

In the United Kingdom, this research report is being distributed only to and is directed only at (a) persons who have professional experience in matters relating to investments falling within Article 19(5) of the FSMA (Financial Promotion) Order 2005 (the "Order"); (b) persons falling within Article 49(2)(a) to (d) of the Order (including high net worth companies and unincorporated associations); and (c) any other persons to whom it may otherwise lawfully be communicated (all such persons together being referred to as "relevant persons").

This research report must not be acted on or relied on by persons who are not relevant persons. Any investment or investment activity to which this research report relates is available only to relevant persons and will be engaged in only with relevant persons. Any person who is not a relevant person should not act or rely on this research report or any of its contents. This research report must not be distributed, published, reproduced or disclosed (in whole or in part) by recipients to any other person.

Additional Disclaimer for Canadian Persons

Edelweiss is not a registered adviser or dealer under applicable Canadian securities laws nor has it obtained an exemption from the adviser and/or dealer registration requirements under such law. Accordingly, any brokerage and investment services provided by Edelweiss, including the products and services described herein, are not available to or intended for Canadian persons.

This research report and its respective contents do not constitute an offer or invitation to purchase or subscribe for any securities or solicitation of any investments or investment services.

Disclosures under the provisions of SEBI (Research Analysts) Regulations 2014 (Regulations)

Edelweiss Broking Limited ("EBL" or "Research Entity") is regulated by the Securities and Exchange Board of India ("SEBI") and is licensed to carry on the business of broking, depository services and related activities. The business of EBL and its associates are organized around five broad business groups – Credit including Housing and SME Finance, Commodities, Financial Markets, Asset Management and Life Insurance. There were no instances of non-compliance by EBL on any matter related to the capital markets, resulting in significant and material disciplinary action during the last three years. This research report has been prepared and distributed by Edelweiss Broking Limited ("Edelweiss") in the capacity of a Research Analyst as per Regulation 22(1) of SEBI (Research Analysts) Regulations 2014 having SEBI Registration No.INH000000172.