GLOBAL NETWORK FOR ADVANCED MANAGEMENT

IIMB

तेजस्वि नावधीतमस्तु

Coromandel

BUY

Target Price: INR 590	Current Price: INR 514.60	Upside: 14.7%
(March 31, 2018)	(November 12, 2017)	

PRIMUS INTER PARES:

AMIT KUMAR ONKAR

JASKARAN SINGH

KARISHMA BHURA

KOUSTAV MANDAL

SOUMIK SARANGI

Direct Benefit Transfer , Nutrient Based Subsidy

Coromandel is poised to be the biggest beneficiary in the complex fertilizer space in India with the implementation positive policy measures as DBT and the NBS. NBS will benefit in the long term by easing working capital pressure and lesser volatility in earnings, on the back of its raw material linkages, scale of operations and operational efficiencies.

Robust Marketing and improved operations

The company's marketing strength comes by means of direct contact with farmers through Mana Gromor Centers. The company has also witnessed improvement in operational efficiency in Retail & Single Super Phosphate (SSP) businesses after streamlining its supply chain and process efficiencies.

Strategic Partnerships

The fertilizer segment, has of long term tie-ups with Foskor, South Africa and Group Chemique, Tunisia, for phosphoric acid along with supply agreements for Ammonia and Sulphur with Mitsui. Furthermore, its stake in Andhra Pradesh Gas Power Plant removes volatility in power supply.

Expansion across Portfolio

The company's crop protection segment is also likely to benefit from the addition of new capacities for its key molecule, Mancozeb. This will be supported by brownfield expansion at Dahej plant (10,000TPA). We expect it to provide the company with scale and help it take advantage of the demand in international markets.

MARKET OVERVIEW

Exchange	BSE
Sector	Fertilizers
Market Cap (INR bn.)	150.38
Avg. Volume ('000)	310.8
P/E	22.31
EPS Trailing (12 m)	23.07

Shortlisting Methodology

Companies listed in NSE/BSE

↓

Return on capital employed > 12%

↓

CAGR of Revenue over past 4 years > 12%

↓

CAGR of EBITDA over past 4 years > 12%

↓

Positive PAT margins over past 5 years

↓

22 Candidates

↓

Technical Analysis

↓

Piotroski Score

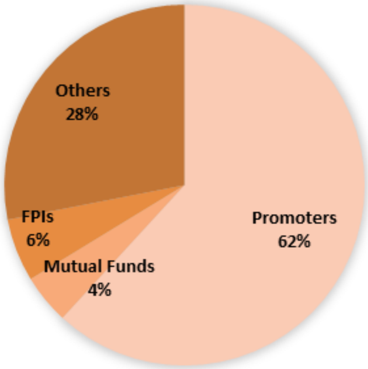
↓

Sector Attractiveness

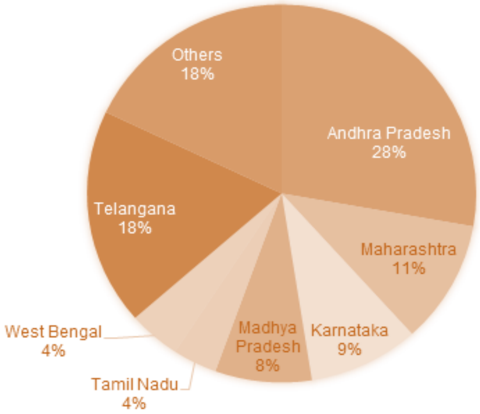
↓

Coromandel International

SHAREHOLDING PATTERN



STATEWISE SALES



OFFERINGS

- ✓ Offers farming solutions through Fertilisers, Crop protection, Specialty Nutrients, Organic compost
- ✓ India's largest private sector **Phosphatic fertiliser producer** and is also **lead organic manure producer**
- ✓ Wide portfolio of over **60 brands**

MANUFACTURING FACILITIES & RETAIL OUTLETS

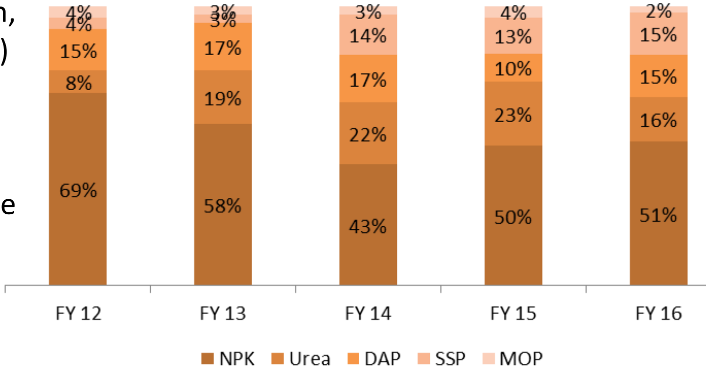
- ✓ **15 manufacturing facilities** in India, located in the 9 Indian states
- ✓ Network of over **800 rural retail outlets** under its retail network in its core market of Andhra Pradesh, Karnataka and Telangana (**largest rural retail chain**)
- ✓ Over **9000 retail touchpoints**

PRESENCE

- ✓ Caters to **2 mn farmers**, covering a total retail space of **0.7 mn square feet**
- ✓ **Presence in 71 countries**, including China and several Latin American, African, South East Asian and Middle East nations
- ✓ **40% export share**

CREDIT RATING	
CRISIL	
Long Term	*AA+*
Short Term	*A1+*
Outlook	*Stable*

Product wise sales

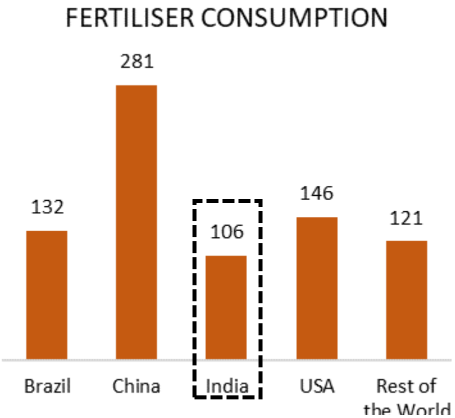


KEY ISSUES

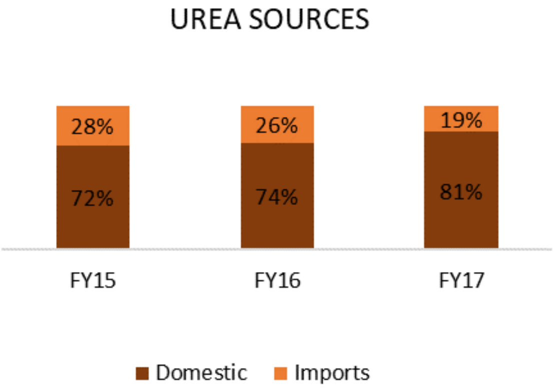
- **Low mechanisation** - meagre growth of <5%; SMFs issue
- **Rain fed irrigation** - shortage of water for 7.5-10 months/yr
- **Lower crop yield** – India 3rd in production of rice, yield is lower than Brazil, China
- **Less nutrient** - >90M agriculture land has nutrient deficient soil & >50% districts have low nutrient content
- **Less crop protection usage -** crop protection (kg/hectare) in India = 0.6 much less than 7 for USA, 13 for China

Opportunities

- **Impetus for improving agriculture** – Gov. aim to double farm income by 2022; budget allocation = INR 5.5bn
- **Make in India –** domestic production ↑; policy target - to become self – sufficient in Urea by 2022
- **Improving pest problem -** ↑ed pest problem is healthy signal for herbicide manufacturing
- **Scope for water soluble fertilisers -** More Crop Per Drop aims to ↑ micro irrigation coverage from 8M hectare to 69M



Source: FAO, IFA



Source: Ministry of Commerce & Industry

INCREASING PEST PROBLEM

	1940		2017	
	Total Pests	Serious Pests	Total Pests	Serious Pests
Rice	35	10	240	17
Wheat	20	2	100	19
Sugarcane	28	2	240	43
Ground Nut	10	4	100	12
Mustard	10	4	38	12
Pulses	35	6	250	34

Solvency Analysis

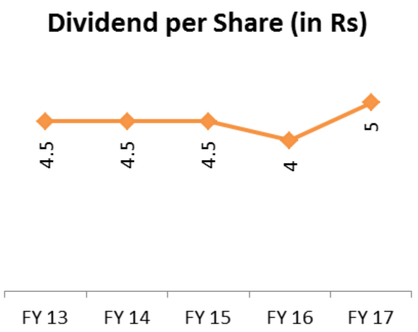
	FY 14	FY 15	FY 16	FY 17
Debt to Capital	44.4%	51.0%	50.4%	43.5%
Debt to Equity	0.62	0.97	0.93	0.79
Interest Coverage Ratio	3.4	3.85	3.32	4.18

- ✓ **Decline in Debt to capital and Debt to equity ratios.**
- ✓ **Improving leverage -> Better interest coverage ratio -> Better solvency**
- ✓ **Advantage Coromandel as farm mechanisation strengthens in India.**

Liquidity Analysis

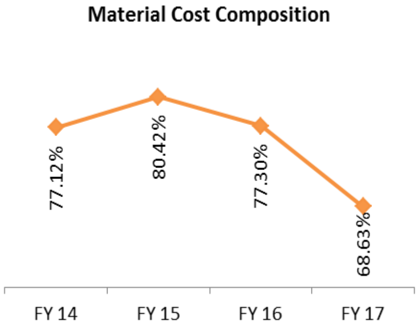
	FY 14	FY 15	FY 16	FY 17
Current Ratio	1.15	1.13	1.15	1.22
Quick Ratio	0.77	0.73	0.77	0.91

- ✓ **Improved Quick and Current Ratio -> Improved liquidity**



Dividend Analysis

- ✓ **Stable dividend per share across years**
- ✓ **Increase in DPS -> Positive signal to investors regarding cash outlook**



Expense Analysis

- ✓ **Decline in the material cost composition due to softer raw material prices**
- ✓ **Locked prices -> Higher margins for the next 1-2 quarters**

Our three stage DCF model at 9.90% WACC gave a target price of 590 at an upside of 14.5%. Valuation using multiples like P/E and EV/EBITDA gave a target price of 602 and 607 respectively.

Activity Ratio Analysis

	FY 14	FY 15	FY 16	FY 17
Total Asset Turnover Ratio	1.22	1.61	1.29	1.20
Inventory Turnover Ratio	5.69	5.09	4.97	5.91
Receivables Turnover Ratio	3.24	2.91	2.47	2.05
Payables Turnover Ratio	2.31	2.35	2.02	1.80
Cash Conversion Cycle	18.9	41.8	40.5	37.0

- ✓ **Improved Inventory Turnover Ratio -> Efficient inventory management-> Improved cash conversion cycle -> Faster Realisation of revenues**

Profitability Analysis

	FY 14	FY 15	FY 16	FY 17
Net Profit Margin	3.67%	3.57%	3.14%	4.75%
ROCE	19.79%	18.89%	15.87%	18.55%
ROE	15.42%	18.62%	15.18%	16.95%

- ✓ **Improved operational efficiency and softening raw material prices-> Improved profitability and better margins**

Factors supporting financials in next few quarters:

- ✓ Agricultural reforms, improved minimum support prices and government's focus towards improving soil health and rural technology
- ✓ Higher contribution from unique grade fertilisers and crop protection segment
- ✓ Higher operating leverage due to better utilization rate in fertilisers and higher usage of captive phosphoric acid (Management is targeting 90% utilization in FY18)
- ✓ Low channel inventory due to higher liquidation of channel inventory and healthy demand

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3 step DCF model:
- ✓ 2018-21: Estimation of FCFF
- ✓ Next 4 years: 10% growth
- ✓ Terminal growth: 4%

3 step model used because of relatively growing business due to farm mechanization.

Tax Rate	30%

(in Rs mn)	2018 E	2019 E	2020 E	2021 E
EBIT	10500	12420	14120	16000
EBIT after tax	7350	8694	9884	11200
YoY growth	19.0%	18.3%	13.7%	13.3%
Depreciation & Amortisation	1074	1145	1220	1298
Working Capital Change	2833	1326	1032	987
Capex	-2000	-2100	-2205	-2315
FCFF	9257	9065	9931	11169

Risk free rate	6.96%
Market return rate	12.68%
Risk Premium	5.72%
Beta	1.06
Long Term Rating	AA+
Short Term Rating	A1+
Cost of debt	8.5%
Cost of equity	13.02%
Debt/Equity	0.79
WACC	9.90%
Terminal Growth Rate	4.00%

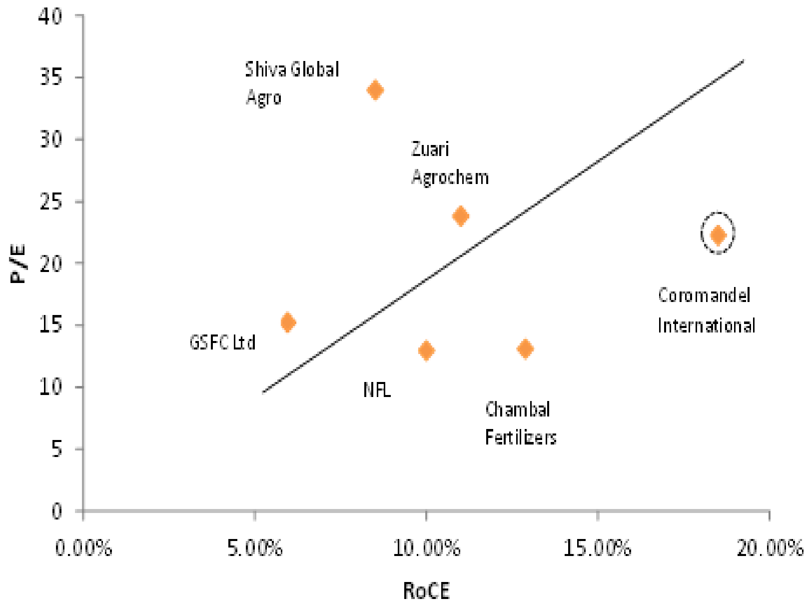
Sensitivity Analysis

	WACC									
	590	8.30%	8.70%	9.10%	9.50%	9.90%	10.30%	10.70%	11.10%	11.50%
Terminal growth	0%	764	707	657	613	575	540	510	482	457
	1%	770	712	661	617	578	544	513	485	460
	2%	775	717	666	622	582	547	516	488	462
	3%	781	722	671	626	586	551	519	491	465
	4%	787	727	675	630	590	554	522	494	468
	5%	792	732	680	634	594	558	526	497	471
	6%	798	737	684	638	597	561	529	500	473
	7%	803	742	689	642	601	565	532	503	476

Assuming growth rate to be 10% for next 4 years from 2022 to 2025 and terminal growth rate of 3% thereafter,

PV (2022-2025)	30694		
PV (terminal)	114675		
PV (2018-2021)	31066		
PV (Total FCFF value)	176435		
Market value of debt	4236		
Market value of equity	172199		
Shares Outstanding	292	Entry Price	515
Share price	590	Upside	14.5%

Our three stage DCF model at 9.90% WACC gave a target price of 590 at an upside of 14.5%. Valuation using multiples like P/E and EV/EBITDA gave a target price of 602 and 607 respectively.



Scatter plot of P/E and RoCE amongst the peers of fertilizers industry; Coromandel International is attractive (cheap) amongst its peer on the basis of the current valuation

Trading in a channel; difference between MACD and signal is negative, contrarian view implies bullishness; Fibonacci retracement: Target : 627 (at 123.6% levels); high deliverables in futures contract.

We recommend a "BUY" given the Fibonacci and MACD analysis and Coromandel's attractiveness as exhibited by the P/E and ROCE plot

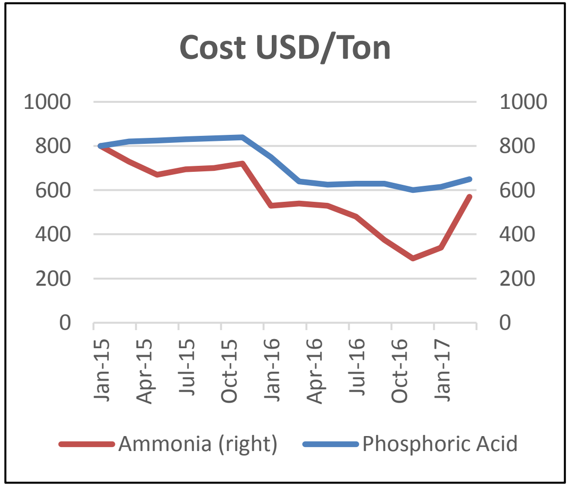
Investment Thesis | Company Overview | Industry Overview | Financials | Valuation | Risks

COMPANY RISKS

- **Delay in expansion of Kakinada plant:** The Rs. 225 Cr expansion plan at the Kakinada plant might be delayed due to potential increase in pollution levels as well as problems on acquisition of land. Hence, there is a potential for opportunity cost being incurred on the capital invested here

- **Volatility in raw material prices:** The cost of production can be directly impacted by volatility in crude oil productions as most of the raw materials are derived from crude oil. The chart alongside shows that the cost Phosphoric acid and Ammonia has slowed down and become stable but there is quite significant supply risk associated with oil based inputs

- **Operational Risks:** A significant amount of risk is posed due to obsolescence of technology in the near future being a possibility. Also, there is a significant threat posed due to development of BT crops which might affect the demand of fertilizers



Government has been implementing **Nutrient Based Subsidy (NBS)** Policy for decontrolled P&K fertilizers which might impact the sales of Coromandel fertilizers which are phosphatic in nature

EXTERNAL RISKS

- **Financial Risks:** Large part of revenue comes from government as part of subsidy; any fluctuation in the exchange rate will lead to under recovery of the subsidy revenue; direct impact on the business profitability of the company

- **Macro Risk:** The expected GDP growth for 2018 has reduced from 7.4% to 6.9% (Fitch rating) after the GDP growth flattered in the first quarter of the current fiscal year. This is likely to adversely impact demand for fertilizers

- **Regulatory Risk:** Poor handling of hazardous material like Ammonia might cause a similar case as in 2015. Moreover there is a risk of crackdown by the Pollution Control Board.

THANK YOU!