

31 July 2019

## Asian Paints –BUY

**CMP** :Rs.1,507.0  
**Target Price** :Rs.1,850.0  
**Upside** : 22%+  
**Stop Loss** :Rs.1,340.0 (Closingbasis)

### Investment Thesis

Recently, the stock price of Asian Paints Ltd.(Asian Paints) corrected by ~17% from 52-week high of Rs.1,820 as it reported lower than expected margin due to change in product mix towards lower end of products.

With its innovative and premium products, Asian Paints has emerged as industry leader in the decorative paint segment with ~53% market share. Over the period, it has spread its presence pan India with its dealer network of over 60,000 across India. Its decorative segment contributes ~83% of its revenue while the rest comes from the industrial segment. It has plans to add ~3,000 dealer and ~4,000 colour world every year to further increase its penetration. A reduction in the GST rate from 28% to 18% would benefit organized players in the long run while rising tax compliance would hit the unorganized segment, which is commanding ~25% of the total industry. Asian Paints is well placed to capture sustained demand of decorative paints going ahead. We expect Asian Paint will grow at healthy rate going ahead led by volume growth owing to sustained demand for decorative paints in tier-II and tier-III cities as well as a shorter repainting cycle.

Owing to lower raw material prices and rising proportion of premium products, Asian Paints has witnessed a significant expansion in EBITDA margin, which improved by ~400bps during FY15-17. However, a reversal was witnessed from FY18 onwards, owing to inability to pass on a sudden rise in crude based raw material prices. Asian Paints has taken a price hike of ~6% during May-December 2018. However, change in product mix towards lower-end products weighed on margins. We believe, increasing proportion of premium products and price hike at regular interval will counter rise in raw material prices and help to sustain EBITDA margin at current level.

### Financials

- During the past 5 years, revenue of Asian Paints grew at a CAGR of 9.0% while PAT grew at a CAGR of 11.4% in the same period.

Consol. (Rs. Mn)	FY17	FY18	FY19	FY20E	FY21E
Revenue	1,70,848	1,72,622	1,93,498	2,22,523	2,55,902
EBITDA	30,214	31,976	35,245	40,532	46,612
% growth	7.6	5.8	10.2	15.0	15.0
PAT	19,666	20,517	21,711	24,968	28,713
EPS (INR)	20.5	21.4	22.6	26.0	29.9
P/E (x)	73.5	70.5	66.6	57.9	50.3
RoE (%)	28.3%	26.3%	24.4%	25.6%	26.7%

- Asian Paints has reported 11.9% YoY growth in revenue in Q4FY19 to Rs.50,182mn largely driven by ~11.0% YoY volume growth in decorative paints in Q4FY19.

### Stock Data

Market Cap (Rs. Mn)	1,698,451
Market Cap (\$ Mn)	23,962.3
Shares O/S (in Mn)	959.2
Avg. Volume (3 month)	1,335,000
52-Week Range (Rs.)	1,820/ 1,118

### Shareholding Pattern

Promoters	52.79%
FII's	16.33%
Institutions	9.56%
Others (incl. body corporate)	21.32%

Performance (%)	1M	6M	1Yr
Absolute	10.8%	19.2%	38.1%
BSE 500	5.4%	-0.6%	1.6%

### Key Ratios

Div Yield	0.6%
TTM PE	75.3x
ROE	24.5%
TTM EPS (Rs.)	23.5/-

- Asian Paints' decorative paint volume grew at ~11.0% YoY mainly driven by economy product range such as distemper and putty.
- Asian Paints' EBITDA grew by 15.1% YoY to Rs.8,798mn in Q4FY19. However, EBITDA margin has declined by 233bps YoY to 16.4% due to change in product mix towards lower end of products. Further, higher fixed cost associated with new plants also weigh on EBITDA margin.
- Asian Paints' PAT marginally declined by 1.7% YoY to Rs.4,872mn attributable to higher depreciation and lower margins during Q4FY19.

## Key Business Highlights

- Asian Paints is India's largest and Asia's third largest paint company with ~53% market share in the domestic decorative paint market.
- With operation in 16 countries and 26 paint manufacturing facilities in the world, Asian Paints serves consumers in over 65 countries with its 7,000 employees. It has the widest distribution network with retail reach of 55,000 outlets of which 27,000 are colour world outlets.
- Asian Paints has entered into a JV with PPG of the US for the industrials and automotive segment. It has also acquired Berger International of Singapore to expand its operations in other markets in Asia, the Middle East and the Caribbean.

## Valuation

- To further expand its capacity to cater growing demand, Asian Paints is setting up a paint manufacturing plant with a capacity of 4,00,000KL in phases at Vizag in Andhra Pradesh at an approximate investment of Rs.17.5bn. First phase of Vizag plant has commenced its production by end of FY19. Additionally, the company is also investing ~Rs.23.0bn to set up a paint manufacturing facility with a capacity of 6,00,000KL in phases at Mysuru in Karnataka. The first phase of Mysuru plant has commenced operation in September 2018. Asian Paints has incurred a total capex of Rs.10,000mn in FY19 and envisages a capex of Rs.7,000mn for FY20E. Once the entire capacity become operational, Asian Paints will be able to cater the future paint demand.
- Asian Paints has built a strong supply chain as it has rapidly identified lucrative catchment areas and set-up depots around it to cater the local demands. This led them to achieve the shortest delivery time of 4-5 hours compared to 24 hours of peers. It also has a wide product portfolio that spans all price points from distempers to premium emulsions. The company is able to deliver 90-95% of the order placed as inventory availability is high at all times as compared to 60-65% of peers. The inventory churn is also much faster due to strong supply chain and wider distribution network at all levels. The strength of its network and supply chain has giving it the pricing power to charge a premium of 5% over other players in all the segments.
- With market leader in paint industry with 53% market share, growing demand due to government's initiatives, indication to further price hike to counter raw material price inflation, EBITDA margin is expected to remain flat, expansion plan to auger capacities and strong supply chain management along with strong dealer networks, we value Asian Paints at 61.8x FY21E EPS of Rs.29.90 to arrive at target price of Rs.1,850.00, an upside of ~22%.

## Risk & Concern

- Any delay in pick up in domestic investment cycle may lead to lower than expected volume growth of Asian Paints.
- Rupee depreciation against the major currencies may lead to erosion of margin of Asian Paints as it imports ~40% of its raw materials.
- Any increase in prices of its main raw material may lead Asian Paints to increase prices of its paints and hence weaken volume growth.

## Graphs & Charts

Figure 1: Net Sales Trend

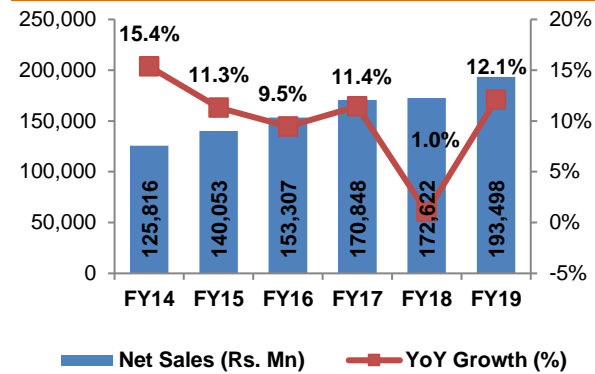


Figure 2: EBITDA & EBITDA Margin Trend

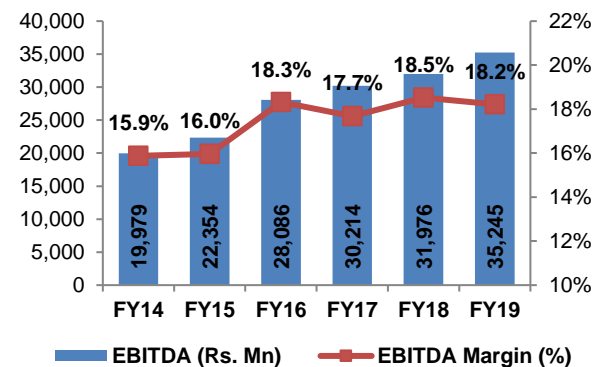


Figure 3: PAT Trend

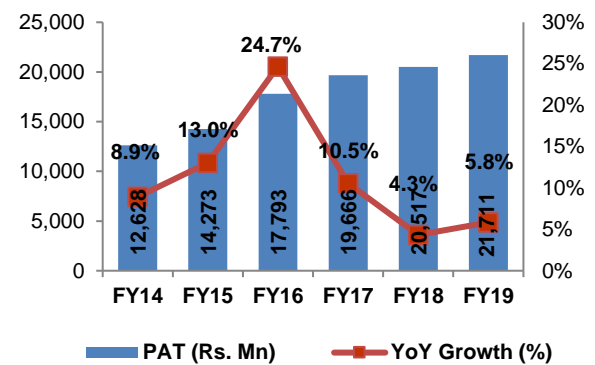
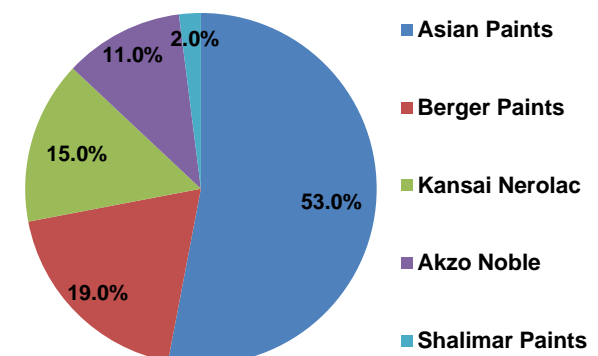


Figure 4: Market-share of Paint Companies



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