

#### Continuing stellar performance; revise to Hold

Aarti Industries Ltd (AIL), for Q3FY19, reported strong set of numbers. Revenue has grown by 28.1% mainly due to robust performance in Specialty Chemical segment. EBITDA grew by 38.8%YoY to Rs 2,469mn with 151bps improvement in margins to 19.5% on account of favorable revenue mix. Net profit grew at a higher pace of 47% to Rs 847mn, due to slower growth in depreciation and interest expenses bolstered by operationally strong performance. Overall volumes in the specialty chemical segment grew by 4% YoY in Q3FY19 (9MFY19: 8%); For FY19, the management has revised their volume growth guidance to 8-10% from 12-15% earlier. However, they have alluded an increase in realization in many of the products leading to a better margin profile, which would aid in supporting growth going forward. During the quarter exports accounted for ~40% of revenue.

#### Better realization with favorable margin profile compensated to low volume growth in specialty chemicals

During the quarter, the speciality chemicals business, which accounts around 80% of AIL's overall revenues has shown margin expansion on the back of optimum utilization of capacities with 4% volume growth compared to the corresponding quarter last year. Improving product mix has also resulted in expansion in margins, as increasing raw material costs, which are typically built into as a pass through mechanism in their selling prices. During the quarter production of nitrochlorobenzene stood at 17,700 tons compare to 18,360 tons in Q3FY18, operating at >90% utilization level. The board has approved for a brownfield capacity expansion plan in nitrochlorobenzene from 75,000MTPA to 108,000 MTPA resulting in a capex of Rs1.5bn. These capacities would be fully commissioned in two phases, Phase 1 in FY20 and Phase 2 in FY21. The expanded capacity would not only help in meeting the increasing domestic demand but also for downstream captive requirement. AIL's nitrotoluene facility reached 53% utilization level, since its commissioning in Sep 2017 during Q3FY19, which the management expects to be ramped up to at least 80% by FY20.

#### Pharma business: Momentum accelerate

The pharmaceutical segment reported strong growth of 23.1% in Q3FY19, lead by expanding volumes across markets. EBIT margin witnessed 544bps improvement to 17.5% compared to Q3FY18, due to operating leverage benefit. The Management expects pharma revenues to grow at 25% along margin improvement. Since major fixed costs are already built-in, incremental volumes will result in significant increase in segment profits. We expect AIL's pharma segment to deliver strong revenue growth of 24.7% CAGR over F18-FY21E.

#### Stock Rating

BUY	HOLD	SELL
> 15%	-5% to 15%	< -5%

Sector Outlook **Positive**

#### Stock

CMP (Rs)	1,707
Target Price (Rs)	1,866
BSE code	524208
NSE Symbol	AARTIIND
Bloomberg	ARTO IN
Reuters	ARTI.BO

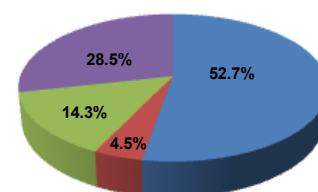
#### Key Data

Nifty	10,912
52WeekH/L(Rs)	1,714/1,033
O/s Shares (Mn)	81
Market Cap (Rs bn)	139
Face Value (Rs)	5

#### Average volume

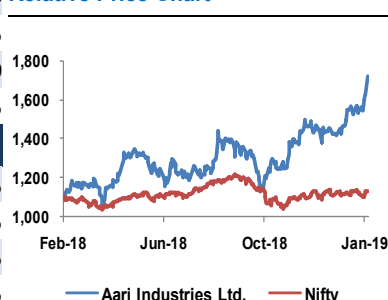
3 months	69,239
6 months	56,449
1 year	61,858

#### Share Holding Pattern (%)



■ Promoter ■ FII ■ DII ■ Others

#### Relative Price Chart



#### Research Analyst

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Key Financials					
YE March (Rs. mn)	FY17	FY18	FY19E	FY20E	FY21E
Net Sales	29,977	36,993	48,753	56,593	69,721
Growth %	10%	23%	32%	16%	23%
EBIDTA	6,084	6,567	9,064	10,680	14,087
Growth%	15%	8%	38%	18%	32%
Net Profit	3,067	3,164	4,627	5,076	7,224
Growth %	21%	3%	46%	10%	42%
Diluted EPS	38	39	57	62	89
Growth %	23%	3%	46%	10%	42%
Profitability & Valuation					
EBIDTA (%)	20.3%	17.8%	18.6%	18.9%	20.2%
NPM (%)	10.2%	8.6%	9.5%	9.0%	10.4%
RoE (%)	25.8%	22.4%	26.6%	22.9%	25.6%
RoCE (%)	20.3%	17.6%	20.6%	18.8%	20.3%
P/E (x)	45.3	43.9	30.0	27.3	19.2
EV/EBITDA (x)	25.1	24.0	17.6	15.4	11.6
P/BV (x)	10.6	9.2	7.0	5.6	4.4

Source: Company, BP Equities Research

## Aarti Industries Ltd Q3FY19 Quarterly Result

YE March (Rs. mn)	Q3 FY19	Q2 FY19	Q-o-Q change %	Q3 FY18	Y-o-Y change %
Net Sales	12,682	12,995	(2.4%)	9,902	28.1%
Other Operating Income	0	0		0	
<b>Total Revenue</b>	<b>12,682</b>	<b>12,995</b>	<b>(2.4%)</b>	<b>9,902</b>	<b>28.1%</b>
<b>Less:</b>					
Raw Material Cost	7,468	7,943	(6.0%)	5,774	29.3%
Operating & Manufacturing Expenses	2,121	2,103	0.8%	1,893	12.0%
Employee Cost	624	529	18.1%	457	36.5%
<b>Total Expenditure</b>	<b>10,213</b>	<b>10,574</b>	<b>(3.4%)</b>	<b>8,124</b>	<b>25.7%</b>
<b>EBIDTA</b>	<b>2,469</b>	<b>2,421</b>	<b>2.0%</b>	<b>1,778</b>	<b>38.8%</b>
Less: Depreciation	406	389	4.5%	342	18.7%
<b>EBIT</b>	<b>2,063</b>	<b>2,032</b>	<b>1.5%</b>	<b>1,436</b>	<b>43.6%</b>
Less: Interest	423.5	513.1	(17.5%)	337.0	25.7%
Add: Other income	2	2		8	
<b>Profit before tax</b>	<b>1,642</b>	<b>1,522</b>	<b>7.9%</b>	<b>1,107</b>	<b>48.3%</b>
<b>Adjusted Profit before Tax</b>	<b>1,642</b>	<b>1,522</b>	<b>7.9%</b>	<b>1,107</b>	<b>48.3%</b>
Less: Total Tax	315	293	7.7%	205	53.7%
<b>Profit After Tax</b>	<b>1,327</b>	<b>1,229</b>	<b>7.9%</b>	<b>902</b>	<b>47.1%</b>
Other comprehensive Income	0	0		0	
Minority Interest	0	0		0	
<b>Adjusted Profit After Tax</b>	<b>1,327</b>	<b>1,229</b>	<b>7.9%</b>	<b>902</b>	<b>47.1%</b>
<b>Diluted EPS (Rs.)</b>	<b>16.2</b>	<b>15.0</b>	<b>7.9%</b>	<b>11.0</b>	<b>47.1%</b>
<b>Adjusted Diluted EPS</b>	<b>16.2</b>	<b>15.0</b>	<b>7.9%</b>	<b>11.0</b>	<b>47.1%</b>
Diluted No of Share (mn)	82.1	82.1		82.1	
<b>Margin Analysis %</b>			<b>Change in bps</b>	<b>Change in bps</b>	
<b>EBIDTA Margin %</b>	<b>19.5%</b>	<b>18.6%</b>	<b>84</b>	<b>18.0%</b>	<b>151</b>
EBIT Margin %	16.3%	15.6%	63	14.5%	176
<b>NPM %</b>	<b>10.5%</b>	<b>9.5%</b>	<b>100</b>	<b>9.1%</b>	<b>135</b>
Effective Tax Rate %	19.2%	19.2%	(3)	18.5%	67

Revenue were above our estimates of Rs 11,667mn mainly driven by stellar growth in Speciality chemicals and Pharmaceutical segment

Adj. PAT came above our estimate of Rs 1,073mn due to operationally strong performance

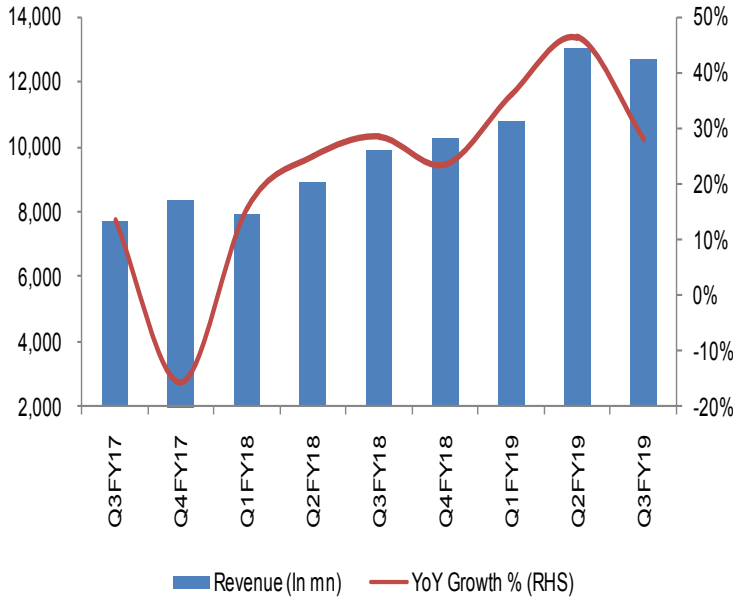
The EBITDA margin, at 19.5% was above our estimate of 18.6% mainly due to favorable product mix

Source: Company, BP Equities Research

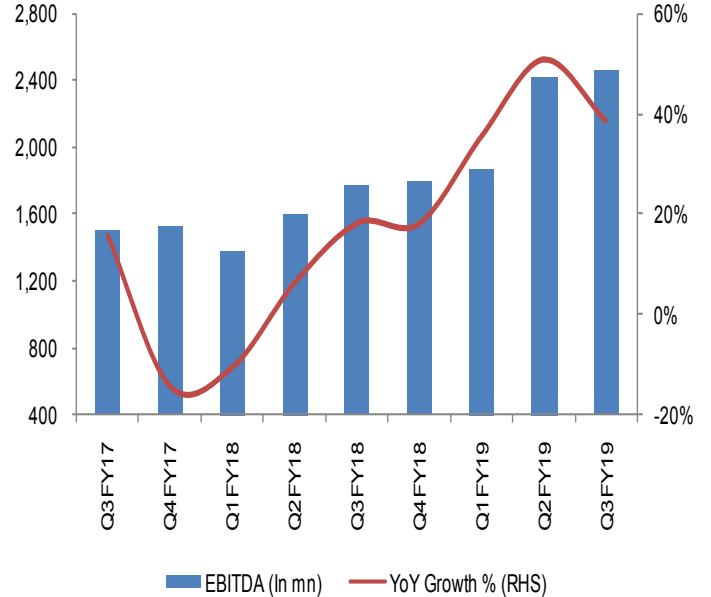
### Valuation and Outlook

AIL is well placed to capture the benefit on account of shift in manufacturing base from western countries to emerging economics like India and China. With China facing environmental and cost pressures leading to the creation of a supply risk situation. This situation is beneficial for the company and it is expected to capitalize this opportunity and increase its market penetration. Improving demand visibility and new product introduction would lead to increased capacity utilization. Further, strong volume growth and new high margin order wins are expected to drive healthy revenue and profitability growth going ahead. Overall, we remain optimistic on the future growth prospects of the company. However, the recent run in stock price limits upside from the current level. Hence, we revise our rating to Hold (earlier BUY), with an upgraded price target of Rs 1,866 (earlier Rs1,709) by assigning P/E of 21x on its FY21E earnings.

**Strong revenue growth of 28% YoY**

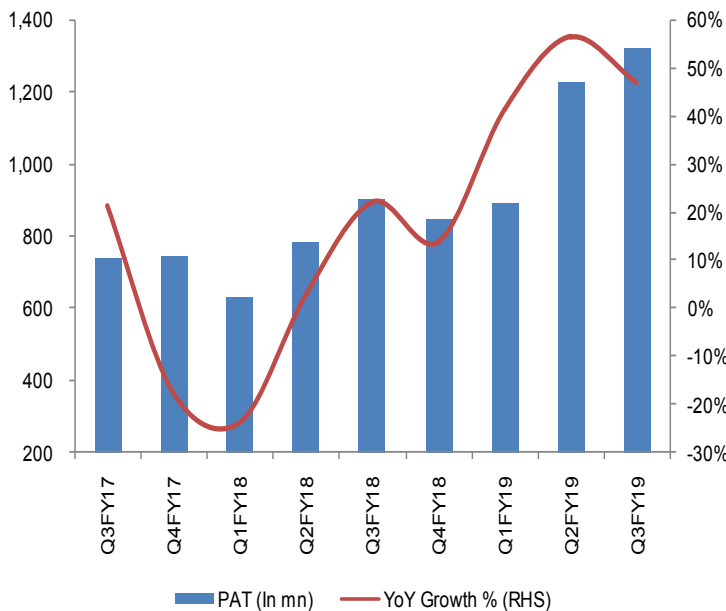


**EBITDA surged by 38.8% YoY**

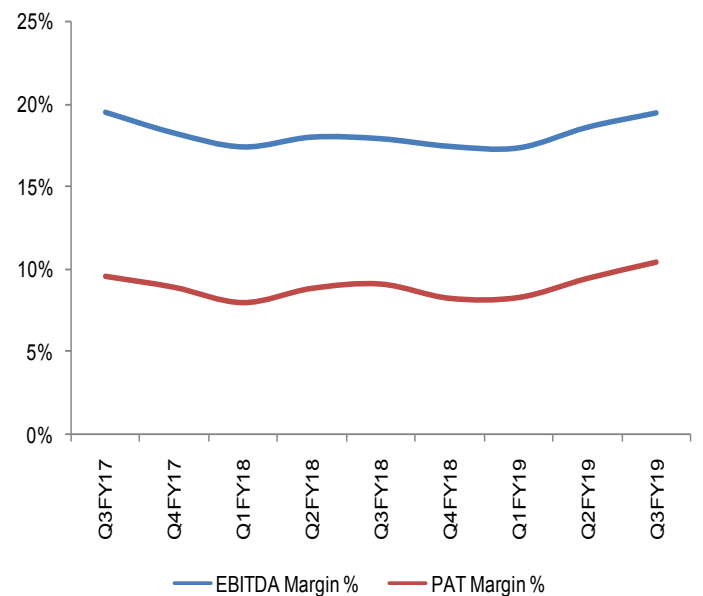


Source: Company, BP Equities Research

**PAT showed growth of 47% YoY**

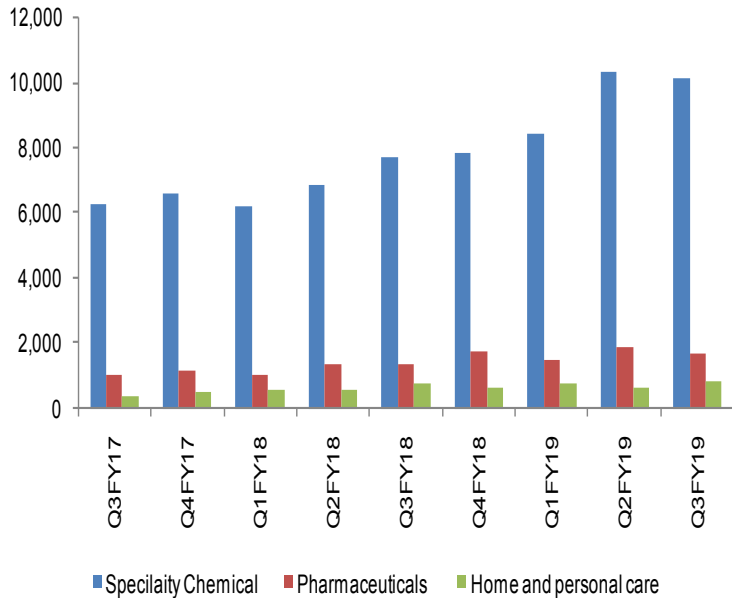
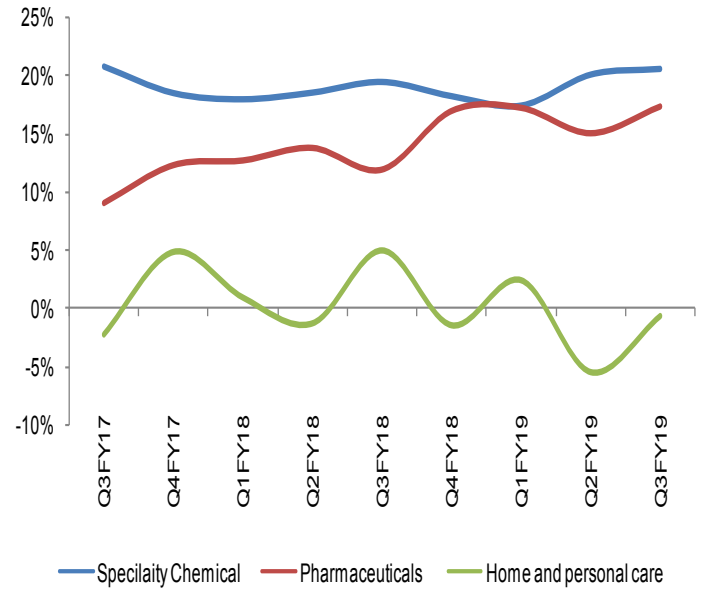


**EBITDA/ PAT margin trend**

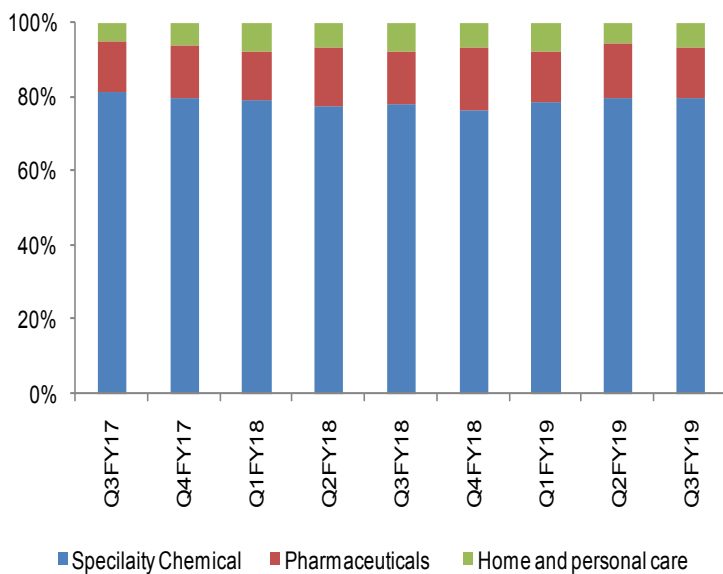
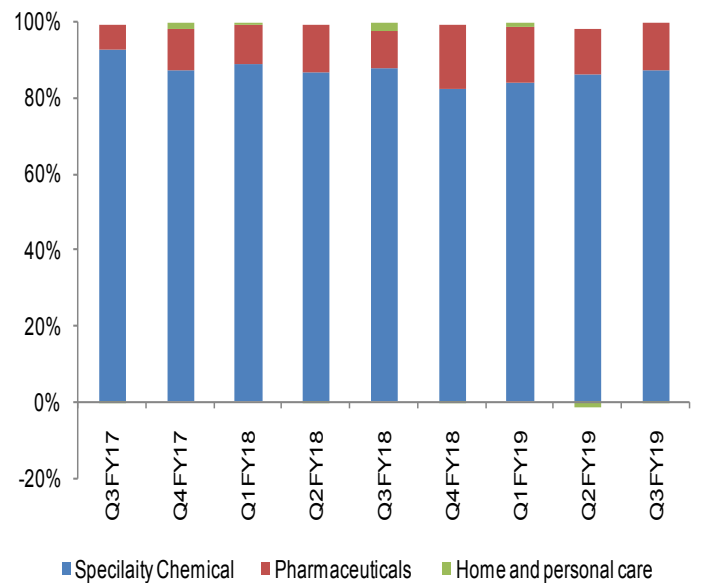


Source: Company, BP Equities Research

### Quarterly Performance In Charts

**Revenue by Segment (In mn)**

**Segment wise EBIT margin (%)**


Source: Company, BP Equities Research

**Segment Wise Revenue Contribution (%)**

**Segment Wise EBIT Contribution %**


Source: Company, BP Equities Research



Profit & Loss A/c					
YE March (Rs. mn)	FY17	FY18	FY19E	FY20E	FY21E
<b>Revenue</b>	<b>30,502</b>	<b>36,993</b>	<b>48,753</b>	<b>56,593</b>	<b>69,721</b>
Growth %	12.3%	21.3%	31.8%	16.1%	23.2%
<b>Total Revenue</b>	<b>30,502</b>	<b>36,993</b>	<b>48,753</b>	<b>56,593</b>	<b>69,721</b>
<b>Less:</b>					
Raw Material Consumed	15,156	19,010	29,489	33,747	40,576
Employee Cost	1,402	1,768	2,190	2,547	3,207
Other Expenses	7,861	9,648	8,010	9,619	11,851
<b>Total Operating Expenditure</b>	<b>24,418</b>	<b>30,426</b>	<b>39,688</b>	<b>45,913</b>	<b>55,634</b>
<b>EBIDTA</b>	<b>6,084</b>	<b>6,567</b>	<b>9,064</b>	<b>10,680</b>	<b>14,087</b>
Growth %	14.8%	7.9%	38.0%	17.8%	31.9%
Less: Depreciation	1,148	1,358	1,564	2,019	2,743
<b>EBIT</b>	<b>4,936</b>	<b>5,210</b>	<b>7,500</b>	<b>8,661</b>	<b>11,344</b>
Growth %	12.8%	5.5%	44.0%	15.5%	31.0%
Interest Paid	1,174	1,307	1,840	2,387	2,387
Non-operating Income	25	21	49	57	58
Extraordinary Income	0	0	0	0	0
<b>Profit Before tax</b>	<b>3,787</b>	<b>3,924</b>	<b>5,709</b>	<b>6,330</b>	<b>9,015</b>
Tax	721	759	1,082	1,255	1,792
<b>Net Profit</b>	<b>3,067</b>	<b>3,164</b>	<b>4,627</b>	<b>5,076</b>	<b>7,224</b>
<b>Adjusted Profit</b>	<b>3,067</b>	<b>3,164</b>	<b>4,627</b>	<b>5,076</b>	<b>7,224</b>
<b>Reported Diluted EPS Rs</b>	<b>37.7</b>	<b>38.9</b>	<b>56.9</b>	<b>62.4</b>	<b>88.9</b>
Growth %	22.7%	3.2%	46.2%	9.7%	42.3%
<b>Adjusted Diluted EPS Rs</b>	<b>37.7</b>	<b>38.9</b>	<b>56.9</b>	<b>62.4</b>	<b>88.9</b>
Growth %	22.7%	3.2%	46.2%	9.7%	42.3%

Source: Company, BP Equities Research

Cash Flows Statement					
YE March (Rs. Mn)	FY17	FY18	FY19E	FY20E	FY20E
<b>PAT</b>	<b>3,066.8</b>	<b>3,164.4</b>	<b>4,627.2</b>	<b>5,075.6</b>	<b>7,223.6</b>
(Less)/Add: Extraordinary Income/Expense	0.0	0.0	0.0	0.0	0.0
Less: Non Operating Income	(25.1)	(21.3)	(48.8)	(56.6)	(57.6)
Add: Depreciation	1,148.0	1,357.7	1,564.1	2,019.3	2,743.0
Add: Interest Paid	1,173.8	1,307.4	1,839.7	2,386.8	2,386.8
Tax Adjustment	0.0	0.0	0.0	0.0	0.0
<b>Operating Profit before Working Capital Changes</b>	<b>5,363.5</b>	<b>5,808.2</b>	<b>7,982.2</b>	<b>9,425.1</b>	<b>12,295.9</b>
(Inc)/Dec in Current Assets	(662.0)	(1,481.3)	(2,136.2)	(1,464.4)	(2,383.7)
Inc/(Dec) in Current Liabilities	649.1	878.1	2,005.7	876.3	1,349.7
Changes in Inventory	(723.5)	(1,401.6)	(2,090.7)	(1,405.0)	(2,194.0)
<b>Net Cash Generated From Operations</b>	<b>4,627.1</b>	<b>3,803.4</b>	<b>5,761.1</b>	<b>7,432.0</b>	<b>9,067.8</b>
<b>Cash Flow from Investing Activities</b>					
(Inc)/Dec in Fixed Assets	(5,113.3)	(4,128.5)	(6,000.0)	(10,000.0)	(5,000.0)
(Inc)/Dec in Capital Work In Progress	399.7	(1,643.9)	0.0	0.0	0.0
(Inc)/Dec in Investment (Strategic)	0.0	0.0	0.0	0.0	0.0
(Inc)/Dec in Investment (Others)	2,765.7	(497.5)	(217.0)	(238.7)	(262.6)
Add: Non Operating Income	25.1	21.3	48.8	56.6	57.6
(Inc)/Dec in Intangible Assets	(293.0)	58.0	0.0	0.0	0.0
<b>Net Cash Flow from/(used in) Investing Activities</b>	<b>(2,215.8)</b>	<b>(6,190.6)</b>	<b>(6,168.3)</b>	<b>(10,182.1)</b>	<b>(5,205.0)</b>
<b>Cash Flow from Financing Activities</b>					
Inc/(Dec) in Total Loans	(592.4)	4,837.3	2,662.8	7,723.6	441.8
Inc/(Dec) in Reserves & Surplus	(578.8)	(1,027.3)	0.0	0.0	0.0
Inc/(Dec) in Equity	(6.0)	(4.1)	0.0	0.0	0.0
Dividend Paid	(82.1)	(82.1)	(84.3)	(86.4)	(88.7)
Less: Interest Paid	(1,173.8)	(1,307.4)	(1,839.7)	(2,386.8)	(2,386.8)
Adjustments	(3.4)	(6.3)	0.0	0.0	(0.0)
Exceptional Item	0.0	0.0	0.0	0.0	0.0
<b>Net Cash Flow from Financing Activities</b>	<b>(2,436.5)</b>	<b>2,410.1</b>	<b>738.9</b>	<b>5,250.3</b>	<b>(2,033.7)</b>
<b>Net Inc/Dec in cash equivalents</b>	<b>(25.2)</b>	<b>22.9</b>	<b>331.7</b>	<b>2,500.2</b>	<b>1,829.1</b>
<b>Opening Balance</b>	<b>241.6</b>	<b>216.4</b>	<b>239.3</b>	<b>571.0</b>	<b>3,071.2</b>
<b>Closing Balance Cash and Cash Equivalents</b>	<b>216.4</b>	<b>239.3</b>	<b>571.0</b>	<b>3,071.2</b>	<b>4,900.3</b>

Source: Company, BP Equities Research



## Balance Sheet

YE March( Rs. mn)	FY17	FY18	FY19E	FY20E	FY21E
<b>Liabilities</b>					
Equity Capital	411	407	407	407	407
Reserves & Surplus	12,690	14,745	19,288	24,277	31,412
<b>Equity</b>	<b>13,101</b>	<b>15,152</b>	<b>19,695</b>	<b>24,684</b>	<b>31,819</b>
<b>Net Worth</b>	<b>13,101</b>	<b>15,152</b>	<b>19,695</b>	<b>24,684</b>	<b>31,819</b>
Minority Interest					
Net Deferred tax liability/(Asset)	1,420	1,594	1,657	1,880	2,322
<b>Total Loans</b>	<b>14,179</b>	<b>18,843</b>	<b>21,443</b>	<b>28,943</b>	<b>28,943</b>
<b>Capital Employed</b>	<b>28,700</b>	<b>35,588</b>	<b>42,794</b>	<b>55,507</b>	<b>63,083</b>
<b>Assets</b>					
Gross Block	24,745	28,873	34,873	44,873	49,873
Less: Depreciation	9,079	10,430	11,994	14,014	16,757
<b>Net Block</b>	<b>15,666</b>	<b>18,443</b>	<b>22,879</b>	<b>30,859</b>	<b>33,116</b>
Capital WIP	2,668	4,312	4,312	4,312	4,312
<b>Investments</b>	<b>1,673</b>	<b>2,170</b>	<b>2,387</b>	<b>2,626</b>	<b>2,888</b>
Others - A	617	559	559	559	559
<b>Current Assets</b>					
Inventories	5,466	6,868	8,958	10,363	12,557
Sundry Debtors	5,474	6,392	8,424	9,779	12,048
Cash and Bank Balance	216	239	571	3,071	4,900
Loans and Advances	1,425	1,948	2,050	2,158	2,272
Other Current Assets	205	245	246	248	250
<b>Total Current Assets</b>	<b>12,786</b>	<b>15,692</b>	<b>20,250</b>	<b>25,620</b>	<b>32,026</b>
<b>Less: Current Liabilities &amp; Provisions</b>					
Sundry Creditors	2,949	3,466	5,377	6,153	7,398
Provisions	238	275	278	281	284
Other Current Liabilities	1,523	1,846	1,938	2,035	2,137
<b>Total Current Liabilities &amp; Provisions</b>	<b>4,709</b>	<b>5,587</b>	<b>7,593</b>	<b>8,469</b>	<b>9,819</b>
<b>Capital Applied</b>	<b>28,700</b>	<b>35,588</b>	<b>42,794</b>	<b>55,507</b>	<b>63,083</b>

Source: Company, BP Equities Research

## Key Ratios

YE March (Rs. mn)	FY17	FY18	FY19E	FY20E	FY21E
<b>Key Operating Ratios</b>					
EBITDA Margin (%)	19.9%	17.8%	18.6%	18.9%	20.2%
Tax / PBT (%)	19.0%	19.3%	19.0%	19.8%	19.9%
Net Profit Margin (%)	10.1%	8.6%	9.5%	9.0%	10.4%
RoE (%)	25.8%	22.4%	26.6%	22.9%	25.6%
RoCE (%)	20.3%	17.6%	20.6%	18.8%	20.3%
Current Ratio (x)	2.7x	2.8x	2.7x	3.0x	3.3x
Dividend Payout (%)	2.7%	2.7%	2.7%	2.7%	2.7%
Book Value Per Share (Rs.)	161.1	186.4	242.2	303.6	391.4
<b>Financial Leverage Ratios</b>					
Debt/ Equity (x)	1.1x	1.2x	1.1x	1.2x	0.9x
Interest Coverage (x)	5.2x	5.0x	4.9x	4.5x	5.9x
Interest / Debt (%)	8.9%	7.9%	9.1%	9.5%	8.2%
<b>Growth Indicators %</b>					
Growth in Gross Block (%)	26.0%	16.7%	20.8%	28.7%	11.1%
Sales Growth (%)	12.3%	21.3%	31.8%	16.1%	23.2%
EBITDA Growth (%)	14.8%	7.9%	38.0%	17.8%	31.9%
Net Profit Growth (%)	21.5%	3.2%	46.2%	9.7%	42.3%
Diluted EPS Growth (%)	22.7%	3.2%	46.2%	9.7%	42.3%
<b>Turnover Ratios</b>					
Debtors Days	66	63	63	63	63
Creditors Days	71	67	67	67	67
Inventory Days	82	82	82	82	82

Source: Company, BP Equities Research

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